South Africa's long-term economic policy options beyond 2021

From a presentation by Dr Asghar Adelzadeh

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Can South Africa achieve 6% growth per annum? Can it achieve this growth while maintaining social welfare benefits for its poorest citizens? Can it also expand essential services and social and physical infrastructure? "Yes," "yes" and "yes," said DR ASGHAR ADELZADEH, according to a new analysis by ADRS. In his presentation, he set about answering the next important question: How will this be done?

This is an edited transcription of a powerpoint presentation given by Dr Adelzadeh at the Macroeconomic Policy Dialogue hosted by the Human Sciences Research Council. IFAA thanks Dr Adelzadeh for granting permission to publish a shortened summary of his address.

ECONOMIC MODELS:

An economic model is a theoretical framework that explains how the real economy works. Due to the immense complexity of economic interrelationships, it is impossible to understand them all at once. And the importance of different factors will vary, depending on the particular economic phenomenon under scrutiny. So if your concern is unemployment, you will choose variables that relate to unemployment – such as wage levels, the availability of skills, the state of demand, inflation trends, investment trends and so on – which your theoretical framework links together. These are translated into mathematical equations, which may number in the thousands for a model of the entire economy. Using regression techniques, the behavioural equations of the model, that, for example, capture the private sector investment decisions or the household consumption behaviour, are empirically tested and expressed. By applying the equations to data inputs, the model will produce a set of conclusions that follow from the base assumptions. It is a huge and difficult task to develop and maintain an economic model – and its conclusions could be spot-on or wildly inaccurate when put to the test. Economic models do not pretend to foretell the future – as humans have attempted for five thousand years, aided by astrology and entrail reading. But they do make forecasts, and their figures are used to inform policy and business decisions - Editor.

SCENARIOS: PLOTTING PATHWAYS INTO THE FUTURE

Scenarios are not predictive at all. They are devices for high-level strategic planning. Based on present facts, informed by experts, they are the outcome of a process to help a team to imagine different futures and question how the best could be achieved and the worst avoided. Scenarios have peppered and prodded South Africa since the high road/low road alternatives framed by Anglo American in the 1980s. Long a tool of business consultants, scenarios became an adjunct of the bosberaad/lekgotla/ indaba. Talk with a purpose. Evidence-based contrasts to spur negotiation and clarify mandates. The Nedcor/Old Mutual scenarios with ruddy-cheeked Bob Tucker (who had lied when he said the Perm would never be limited); the Mont Fleur scenarios with their themes of the ostrich, the lame duck, Icarus (flying too close to the sun) and the dawn-soaring pink flamingo's representing "inclusive democracy and growth." Since the unjust transition, scenarios have made frequent re-visits, often featuring some token original participants, perhaps to ground expectations. Worth re-reading is the searing analysis of the September Commission (Cosatu 1997) which identified every aspect of the impending fall of the proud trade union movement – except its imminence. Forgettable are the Presidency's Scenarios 2025 from the season of high hope in 2008, the chaotic Dinokeng Scenarios of 2009 and the careless employment scenarios presented in the National Development Plan in 2012. Moving out of the diversion of the Zuma years, a host of business donors funded the Indlulamithi (giraffe, above the trees) Scenarios to imagine pathways to 2030 (Indlulamithi South Africa Scenarios 2030 Trust, 2019). The three scenarios are *iSbhujwa* [based on continuing present trends]; — a nation torn by deepening social divides, daily protests and cynical self-interest – where the rich do well; *Gwara Gwara* — 'A floundering false dawn': a demoralised land of disorder and decay; and *Nayi le Walk* — 'a nation in step with itself', where growing social cohesion, economic expansion, and a renewed spirit of constitutionalism get SA going. – *Editor.*

In 2018, the Indlulamithi Scenarios 2030 released three non-technical socio-economic and political future scenarios for South Africa. In 2019, ADRS was commissioned to use its economic models of South Africa to identify and quantify possible policy roadmaps for the three Indlulamithi scenarios.[1] In 2020, ADRS used its Linked National-Provincial Model (SA-LNP) to examine the impact of Covid-19 and to put forward alternative post pandemic recovery plans, including a six-pillar policy proposal. The Indlulamithi Scenarios 2030 launched the ADRS Covid-19 report in February 2021 (Adelzadeh et al., 2021).

The focus of Dr Adelzadeh's HSRC presentation on 30 September 2021 was on three possible post-pandemic economic policy roadmaps and their likely implications for South Africa's chronic crises of low growth and high rates of unemployment, poverty and inequality.

UNDERSTANDING THE SA POST 1994 ECONOMIC POLICY FRAMEWORK

Dr Adelzadeh began with a short, guided tour through the past 27 years of South African macroeconomic policy in order to understand how we have got to the undesirable situation in which we find ourselves.

He recalled that when the ANC embraced the market economy in the late 1980s and early 1990s, the question was which approach to capitalism would the new state adopt to build the post-apartheid economic system? Would it pursue:

- the free-market neoliberal capitalism of Margaret Thatcher and Ronald Reagan;
- the shock therapy approach of post-Soviet Union Russia;
- a social democracy model of northern Europe; or
- the East Asian state-led model of capitalism?

In the early 1990s, the Reconstruction and Development Programme (RDP) provided a broad consensus on reconstruction and redistribution as the way in which South Africa could achieve growth and development (ANC, 1994).

This was an integral element of the ANC manifesto for the first democratic elections in 1994. It rejected the trickle-down approach of free-market capitalism and sought to directly target the disadvantaged by developing government capacity and enabling it to undertake strategic interventions in social and economic development.

To build this post-apartheid system, the RDP stated: "the democratic government must play a leading and enabling role in guiding the economy and the market toward reconstruction and development" (ANC, 1994: Section 4.2.3). ➤➤

However, between 1994 and 1996, the government gradually distanced itself from the RDP approach and embraced a variant of free-market capitalism for the country's post-apartheid economic system. This was achieved through at least the following five undertakings:

- In December 1993, the ANC approved a loan agreement with the International Monetary Fund (IMF) whose terms and conditions included "a package of macroeconomic and structural policies" similar to the IMF's much criticised Structural Adjustment Programme.
- In 1994, the RDP Green Paper and White Paper downplayed the central role of 'redistribution' in the RDP (Adelzadeh and Padayachee, 1994). At the same time, the government distanced itself from the report by the Macroeconomic Research Group (MERG) that provided the policy blueprint for implementing the RDP (MERG, 1993; Freund, 2013).
- In early 1995, South Africa joined the World Trade Organisation (WTO) as a 'developed' and not a 'developing' country, thus agreeing to a sharp liberalisation of its trade and investment policies.
- In 1996, the government submitted a non-negotiable policy framework on Growth, Employment and Redistribution (GEAR) to Parliament (RSA, 1996). GEAR postulated that the post-apartheid economic system would achieve transformation and development through economic growth that would result from the expansion of a free-market economy in the country. The proponents of GEAR argued that a higher growth rate would automatically deal with unemployment, which would also solve the problems of poverty and inequality. In essence, GEAR accepted the premise that the trickle-down effect would distribute the benefits of growth to the disadvantaged (Adelzadeh, 1996). Moreover, GEAR considered "the only way to improve growth is through the supply side. It advocated for lower tax rates, privatisation, liberalisation, deregulation and competition in the hope of stimulating private sector investment, higher growth and employment. The argument [was] that any alternative strategy would be counter-productive since it would limit or crowd out private sector potential" (MERG, 1993: 5-6).
- In 1999, the Reserve Bank adopted inflation targeting as its framework for monetary policy, making inflation – rather than employment, output or some other criterion or combination of criteria – the primary goal of monetary policy.

Therefore, by the end of the 1990s, the ANC government had basically adopted free-market ideology and its policy agenda for the post-apartheid South African economic system. Successive governments have since defended and implemented the core policy agenda of this ideology.

The adopted post-apartheid economic policy framework has consistently produced:

- low economic growth;
- high rates of unemployment;
- a high poverty rate;
- high inequality; and
- de-industrialisation.

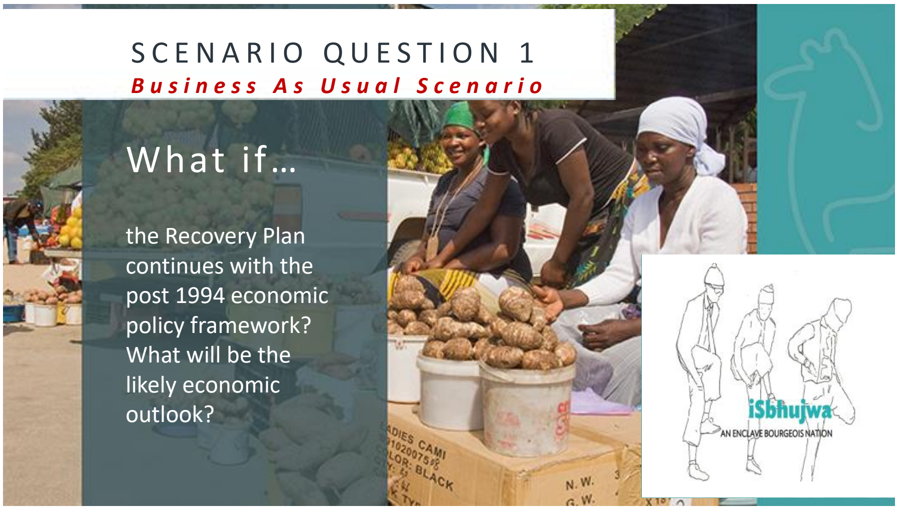
Between 1996 and 2020 the average annual growth of GDP was 2.2% and per capita GDP growth was 0.6%. The official unemployment rate in 2020 was 32.6%, although according to the expanded definition of unemployment (which includes those who had given up looking for work) the unemployment rate was 47.9%. The Poverty Headcount stood at 43.2% and income inequality was reflected in a Gini-coefficient of 0.71. The share of manufacturing in total employment declined from 15.6% in 1996 to 9.2% in 2020. The UNIDO Competitive Industrial Performance Index fell from 0.069 in 2000 to 0.057 in 2019.

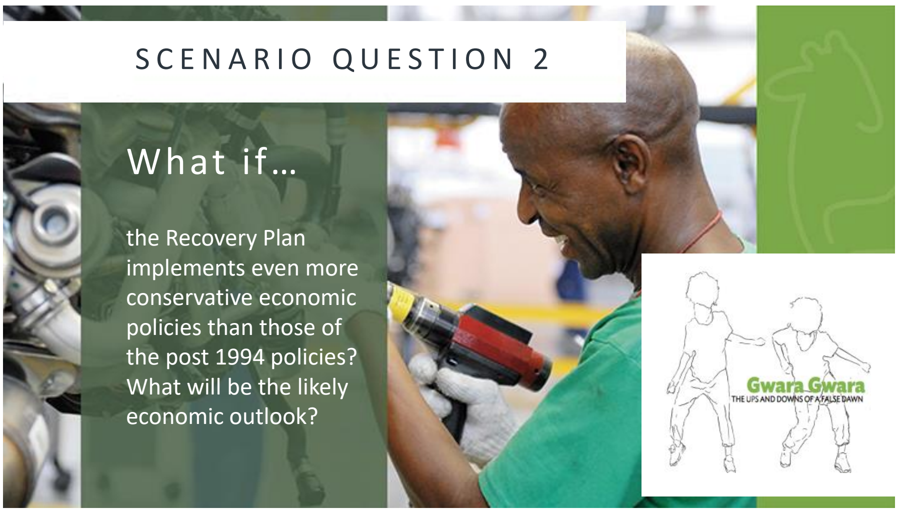
While there were positive aspects during this time, the overall growth and development outcomes of the post-1994 economic policy framework have been extremely disappointing. The economic policy framework that was adopted in the 1990s, and which has since informed policies, bears significant responsibility for these outcomes and the overall failed economic transformation. Moreover, the country's struggling economy was hit in 2020 by the ongoing coronavirus pandemic with extensive domestic and international negative shocks.

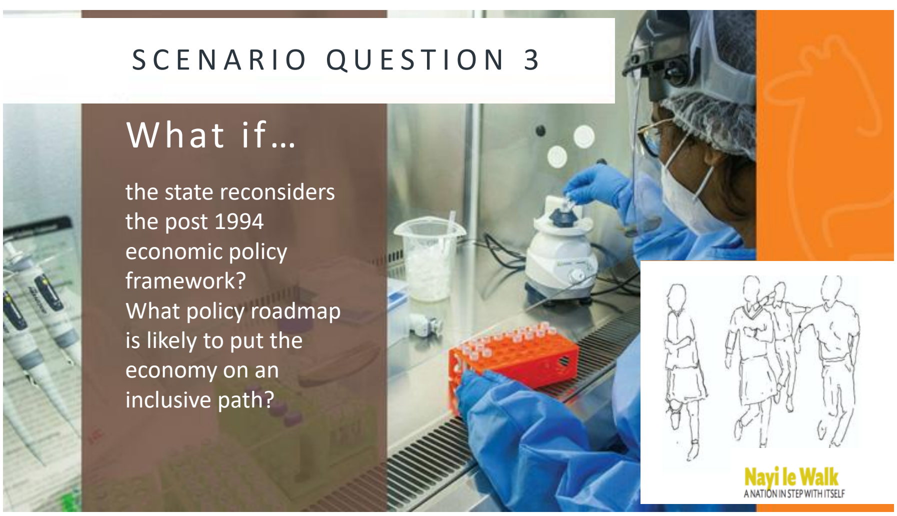
RECOVERY SCENARIOS

As the country plans for the post-Covid-19 recovery, the most pressing question on everyone's minds is: What will that recovery look like and what will it mean to South Africans? Will the recovery mean a return to the weak economic performance of pre-Covid-19 levels with the benefit of growth mainly going to the top layer of the population, and only a relatively small amount trickling down to the rest? Or will the recovery mean recovery from the country's chronic crisis and realising pro-poor inclusive outcomes?

ADRS's SA-LNP model replicates the working of the South African economy, including its 52 districts and 234 municipalities. It is developed to identify policy choices and future possibilities and outcomes. Dr Adelzadeh has used the model to pose the question: What policy scenarios are available to South Africa during the next 10 years?







Scenario 1: Business As Usual – the iSbhujwa trickle-down outlook, for an enclave bourgeois nation

What will the likely economic outlook be if the recovery plan continues with the post-1994 economic policy framework? This Business As Usual scenario is represented by the post-1994 economic and social policy roadmap that includes:

- General government's annual spending on goods and services increases by 7.5% with weak support for industrial policy.
- Economic and social infrastructure investment increases annually by 6%.
- Investment by public enterprises increases by 6% annually.
- The Reserve Bank continues with inflation targeting and credit extension to the private sector annually grows by 6%.
- The government continues the current Extended Public Works Programme and the social grants programme.

The model generated 10-year outlook under the Business As Usual scenario sees:

- GDP grow from R3.2 trillion in 2020 to R3.6 trillion in 2030 (economic growth of about 2.2% per annum).
- The unemployment rate falls from 33% in 2020 to 27% by 2030.
- The poverty rate moves from just under 40% in 2020 to 34% in 2030, effectively returning to the pre-Covid trend.

Overall, with the Business As Usual scenario, the low growth with high unemployment and poverty trends of the past 20 years are re-established. This would mean the economy will continue to disproportionately benefit the non-poor. »

> **By the end of the 1990s, the ANC government had basically adopted free market ideology and its policy agenda for the post-apartheid South African economic system.**

Scenario 2: Austerity – Gwara Gwara, the ups and downs of a false dawn

Over the last two years, the Treasury and the Reserve Bank have proposed policy measures that are consistent with an even more conservative policy framework. In the face of the country's economic crisis, they have proposed mainly supply-side reforms, a much more austere fiscal policy, and a stricter target for the inflation rate for monetary policy. What will be the likely economic outlook if the recovery plan implements even more conservative economic policies than those of the post-1994 period?

This Gwara Gwara scenario is represented by the following austere policy roadmap:

- Government spending on goods and services are cut by 10%.
- Capital spending by the government is reduced by 5%.
- Monetary policy is tightened by lowering the current 6% upper bound for inflation to 4%.
- The localisation policy is abandoned and subsidies on products and production are cut by 5%.

Under this scenario, the model results show that over the coming decade:

- GDP growth will average 1.8% per annum to 2030.
- The unemployment rate stays high at 29% by 2030.
- The poverty rate initially declines but stays high at 37%.

Overall, the austerity scenario will make things worse for everyone – but the burden is felt the most by the poor.

Scenario 3: Six-Pillar Policy Framework – Nayi Le Walk, a nation in step with itself

The third scenario postulates what could happen if the government reconsiders the post-1994 economic policy framework. It proposes a "six-pillar" policy roadmap to put the economy on an inclusive path? This involves co-ordinating:

- macro-economic policy reform;
- social policy reform;
- micro-economic policy reform;
- trade and industrial policy reform;
- private sector international support; and
- provincial growth and development plans.

Pillar one: Macroeconomic policy reforms

The key features of pillar one would be:

- Government and public corporations increase their investment in economic infrastructure, social infrastructure and economic services by 10% annually over the next 10 years (this is 4% above the Business As Usual scenario).
- The Reserve Bank's solitary mandate of targeting inflation is upgraded to a dual mandate of both targeting inflation and also targeting 6% economic growth.
- Government spending on goods and services increases annually by 10.5% to provide necessary funding to expand the delivery of individual and collective social services.
- Monetary authorities adopt the necessary measures to raise the annual growth of credit extension to the private sector to 15%.

Pillar two: Social policy reforms

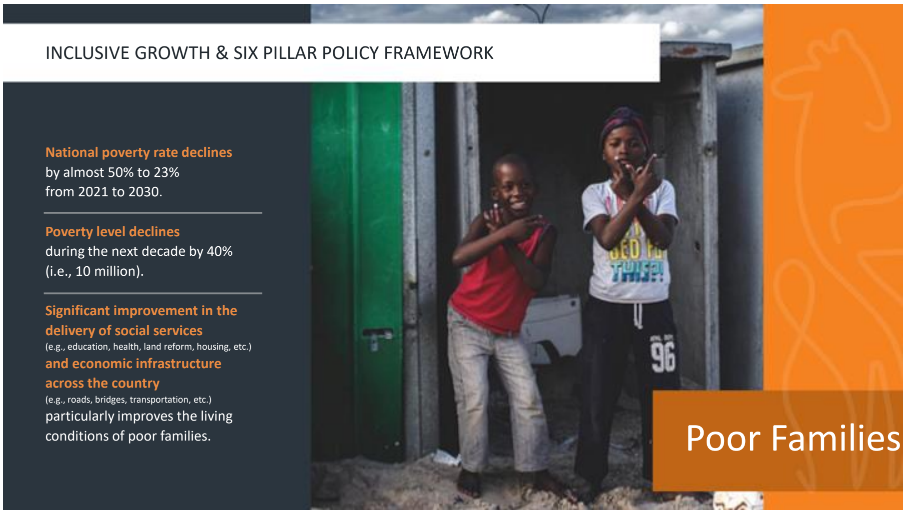
Interventions to build the social policy reform pillar require that:

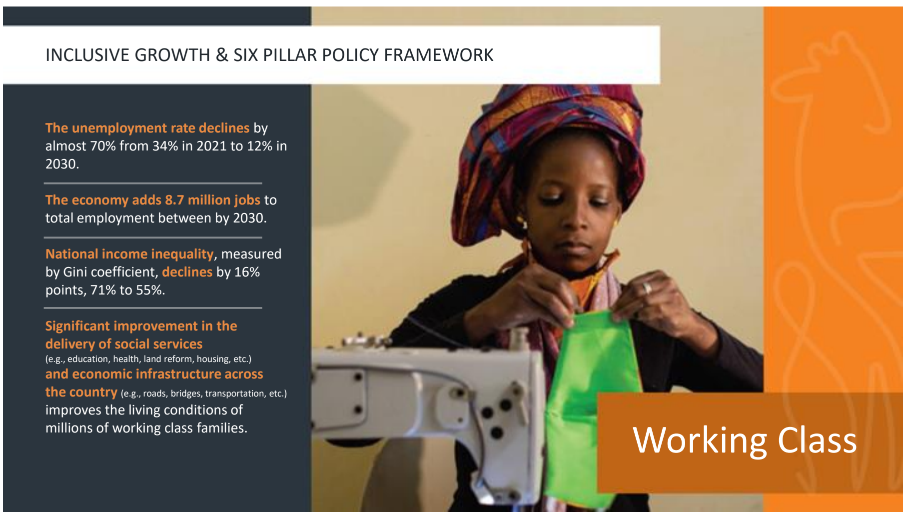
- Government begins to make Public Works the employer of last resort for the *unskilled* unemployed workers – with a daily pay rate of at least R160. The Expanded Public Works Programme expands to cover about 75% of the unskilled unemployed, with coverage growing by an additional 3% every year after 2021.
- Government immediately introduces an unemployment grant for *skilled* unemployed and for all who have become unemployed due to Covid-19 disruptions. The eligible unemployed workers will be entitled to R1000 a month, which increases by 6% annually.
- In light of the Covid crisis, government introduces a caregiver grant of R500 for a family member who takes care of a child who receives either a child support grant or a care dependency grant.
- The initial amount of the grants should increase by 6% annually.

Pillar three: Microeconomic policy reforms

Micro-economic policy reform measures for the next 10 years should include:

- Support policies that help exports from the agriculture





sector to grow by an additional 1% in 2021 and by an additional 0.5% every year thereafter. Thus, by 2030, exports from the agriculture sector are expected to be 6% higher.

- Lowering the price of the Transport, Storage and Communication Sector over the next 10 years by 5% to 10% initially (between 2021 and 2023) and then by an additional 5% annually.
- Direct boosts for labour productivity (an annual positive shock of 1%) in the following sectors: Transport, Storage and Communication; Agriculture; Food; Basic Chemicals; Iron and Steel; Trade; Catering and Accommodation.
- Improving competitiveness in the following sectors: Trade; Catering and Accommodation; Transport, Storage and Communication; Financial Intermediation; Insurance; Real Estate; Business Services – so that there is a gradual lowering of their mark-up, by two percentage points initially and by an additional one percentage point each subsequent year.

Pillar four: Trade and industry policy reforms

Trade and industrial policy measures include:

- Industrial financing incentives that will directly and indirectly increase total annual investment in the manufacturing sector by R10 billion (in 2010 prices) during the next 10 years.
- Special Economic Zone (SEZ) and African integration programmes to increase total exports by an additional 1.5% after 2021. »

> **[In] the six-pillar scenario, the future outlook will trend more towards an inclusive pro-poor path scenario.**

- Proudly SA and localisation policies to gradually reduce import dependency ratios of some sectors by 20% over the next 10 years.
- Public sector and public/private sector investment practices that gradually increase the employment intensity of economic growth in South Africa.

Pillar five: Private and international support

Private and international support should include:

- The Public Private Growth Initiative (PPGI) increasing investment in the South African economy by R500 billion over the next 10 years.
- The Public Investment Corporation (PIC) increasing its investment in the South African manufacturing sector by R100 billion between 2021 and 2025 (five years).
- The level of foreign direct investment in South Africa gradually increasing from 1% to 2.5% of GDP between 2021 and 2030.
- In the wake of the recovery from Covid-19, the nominal value of total world imports grows annually by 8%.

Pillar six: Provincial growth and development plans

Provincial growth and development plans need to complement national government interventions. Taking Gauteng as an example,

- The Growing Gauteng Together (GGT2030) industrial measures should increase Gauteng's total real output by 0.5% in 2021 and by an additional 0.5% each year thereafter.
- Provincial measures to promote African regional trade should increase Gauteng's exports to Africa by an extra 0.5% annually.
- Extensive provincial sector strategies and support measures should lead to an additional 0.5% annual investment increase in Gauteng's Agriculture, Food, Electricity, Water, Construction, and Transportation, Storage and Communication sectors.

Under the six-pillar policy scenario, the model projections show:

- GDP grows at an average of 6.2% per year over the period of 2021-2030.
- The unemployment rate drops to 12%, with 8.7 million additional jobs created by 2030.
- The poverty rate is cut by almost 50% to 23%.
- Income inequality is reduced by 16% points.

At the same time, the six-pillar policy option:

- Produces balanced growth, reflected in the simultaneous expansion of both aggregate demand and aggregate supply over the next 10 years.
- Generates the funds needed to pay for the scenario's expected increase in government expenditure, because government revenue will grow concurrently with the projected GDP growth.
- Produces, relative to the Business As Usual scenario, declining annual debt-GDP ratios due to the scenario's higher economic growth rates, lower real interest rates and better primary balance rates.
- Initially, during the pandemic, increases the cost of social grants relative to GDP, but the ratio will gradually fall during the rest of the decade because of the scenario's high economic growth outlook. By 2030, the cost of social grants relative to GDP will be 3.1% compared to 4% under the Business As Usual scenario.

Six-pillar policy scenario impact on the poor and the working class

The six-pillar policy framework will benefit the poor and the working class because:

- The national poverty rate declines by almost half between 2021 and 2030 as 10 million people are lifted out of poverty and the poverty level falls in the next decade by 40%.
- The unemployment rate declines from 34% in 2021 to 12% in 2030.
- The economy adds 8.7 million jobs to total employment by 2030.
- National income inequality, measured by the Gini coefficient, declines by 16% points, from 71% to 55%.
- Significant improvement in the delivery of social services (e.g., education, health, land reform, housing, etc.) and economic infrastructure across the country (e.g., roads, bridges, transportation, etc.) particularly improves the living conditions of poor and working class families.

Six-pillar policy scenario impact on the business class and the non-poor

For the rich and the business class:

- Real GDP will almost double over the next decade, which implies a significant expansion of the domestic market.
- Average profit rate remains above 16%.
- Improvements in the economy and overall well-being of the population improve average labour productivity growth.
- Government debt-GDP ratio will gradually decline, due to the high average annual growth rate, to less than 50%.
- Average investment-GDP increases to about 27%.
- Increase in social cohesion enables stable capital accumulation.

CONCLUSION

The ADRS modelling work highlights three possible scenarios for South Africa after taking the Covid-19 shocks into account:

iSbhujwa: Trickle-down outlook

If the recovery plan continues with the post-1994 policy status quo, i.e., the Business as Usual scenario, the past trickle-down path will resume after the pandemic with the economy stuck in low growth and high rates of unemployment, poverty and inequality during the next decade.

Gwara Gwara: Immiserising outlook

If the recovery plan implements even more conservative policies than those of the post-1994 status quo policies, the future outlook will trend more towards an immiserising growth path.

Nayi Le Walk: Pro-poor outlook

If the recovery plan policy framework reflects a shift from the post-1994 policy status quo and embraces a policy framework similar to the six-pillar scenario, the future outlook will trend more towards an inclusive pro-poor path scenario, enabling South Africa to recover from its chronic economic and development crisis.

South Africa was hit by the Covid-19 pandemic at a time when the country was already in the midst of an economic crisis. Since returning to the pre-coronavirus economic recession is not the most desirable recovery option, current policy challenges go beyond short-term Covid-19 mitigation measures. To help identify actionable recovery options, Dr Adelzadeh proposes a six-pillar policy framework that is promising but requires breaking away from the post-1994 economic policy framework that has consistently exacerbated South Africa's growth and development challenges.

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ENDNOTES

1. Indlulamithi Scenario 2030 developed and published the three scenarios. The names of the three scenarios discussed in this article come from the Indlulamithi Scenarios 2030. NA

Indlulamithi uses the "Indlulamithi Barometer" to collect information about the country's socio-economic and political progress. They report annually which scenario the country has been moving towards, or best represents the current path. In its latest presentation, in July 2021, it found that the evidence during the past year points to the Gwara Gwara scenario as South Africa's current actual scenario.