New wine into new wineskins

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An alternative economic strategy for South Africa's economic reconstruction

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1. Introduction

An alternative economic framework is urgently required in South Africa. Conventional approaches have not yielded the results necessary for transforming a deeply unequal and highly corporatized economy. Over the last three decades South Africa has been unable to see sustained economic development to push the majority of South Africans into improved economic livelihoods so that they can realize their full human potential. South Africa's growth experience has been lacklustre, resulting in high levels of unemployment and stubbornly widening levels of inequality. The crisis of poverty, inequality and unemployment is worsening amidst a declining growth trajectory[1].

Post-apartheid economic policies have not led to a change in the control and production of key natural resources. The ruling elite has maintained control of resources to the detriment of the majority. South Africa's economic history has been one of ruling elites who controlled the mineral wealth, especially diamonds, gold, iron ore and platinum. Since the 1890s until the 1990s this wealth was shared between white English and Afrikaner capital who have ruled the economic landscape for the bulk of South Africa's modern economic history. Since the 1990s wealth accumulation followed the same path dependency of elite accumulation, albeit now slightly deracialised.

A handful of black tycoons were created under the banner of Black Economic Empowerment. The Mandela, Mbeki and Zuma governments identified a handful of beneficiaries who became the new black elite. There was no comprehensive plan to ensure redistribution of the economic gains for the benefit of the majority. The continuation of neo-liberal economic policies has yielded poor outcomes with respect to enhancing both economic growth and productivity. We thus see an unsurprisingly high concentration of wealth, with persistent poverty amongst the lowest income deciles, driven largely by income inequality[2].

There has been little effort to expand our conception of economic development during the post-apartheid era by drawing on the kind of development economics that considers the successes of the Asian tigers, some African lions and some Latin

[1] Statistics South Africa (Stats SA). 20219Labour Force Survey.
[2] Hunderborn, Leibbradnt & Woolard. 2016. Drivers of inequality in South Africa.

American jaguars. Instead, we emulate policies applied in first world economies whose models have shown to have little relevance for South Africa's unique problems.

The National Treasury estimates are dire. Their growth estimates prior to the COVID-19 pandemic for the next 3 years were less than 1% to 2% growth in the outer years of the Medium-Term Expenditure Framework (MTEF)[3]. The COVID-19 crisis will further deteriorate the growth outlook and the severity and length of the contraction will depend on our responsiveness. Even without the COVID-19 crisis, the outcomes of 2019 "Toward's an Economic Strategy for SA" are far worse than those of former economic policies such as the Growth Employment and Redistribution (GEAR) strategy and the National Development Plan (NDP). Growth estimates are consistently revised downwards. Irrespective of proposals and plans put forward by the National Treasury, estimates before the COVID-19 crisis of 0.9% growth were projected for 2020 by the IMF[4]. Investment conferences led by the Presidency, policy proposals done singlehandedly by the National Treasury and other government efforts have not managed to convince the international and local investment community about the positive effects such measures will have on the total growth story. The National Treasury's Economic Strategy envisaged minimal gains with only a 2.3% growth rate and a projected 1 million jobs. This strategy is premised on assumptions about microeconomic reforms that prior to implementation offer no solution to the more than 10 million unemployed South Africans.

Unless we acknowledge the inadequacy of the economic approach offered in the micro- and macro-economic proposals of the National Treasury and government as a whole, we are unlikely to see different outcomes in the next few years and decades. This paper proceeds from the view that micro-economic solutions offered for the next decade, on the back of the existing macroeconomic policy environment, will yield the same persistent outcomes. This will be discussed further in Section 5. South African economic policy has failed to craft and adopt a new generation of ideas about economic development. It continues to rely on classical mainstream economic thinking which many developed and emerging economies have abandoned for building their

[3] National Treasury. 2019. Economic transformation, inclusive growth and competitiveness: Towards an Economic strategy for South Africa.
[4] International Monetary Fund. 2020. 2019 Article IV Consultation with South Africa.

societies. The responses to the COVID-19 crisis have departed fundamentally from this framework. It is clear that a different development approach is required for us to reach our growth targets and rebuild South African society. Mainstream economists have not addressed the problem of under-development over more than two decades, yet we continue to adhere to growth models that result in the same processes of under-development.

We must accept that the vehicles that have been used have resulted in dismal failures economically, and that long-term economic gains will require a completely new approach that is underpinned with clear targets and the development of parallel planning capabilities. There is little or no mention beyond the improved financial performance of State Owned Enterprises (SOEs) by reducing their reliance on the fiscus, yet the vehicle through which governments influence economic outcomes beyond the budget is through the integration and co-ordination of government institutions. The functioning of state organs and alignment of government activities will have a further enabling effect on the growth potential of any country. The fiscal policy muscle and associated institutional instruments should not be ignored as the catalysts for invigorating economies.

Productivity enhancing structural change is needed in Sub-Saharan Africa (Nissanke 2019). This must be matched by investment in productivity-enhancing sectors coupled to the development of the necessary skills and technological knowledge. A fresh approach to transforming the economic framework requires structural transformation that is linked to growth enhancing changes. Furthermore, such growth enhancing structural change requires a shift in the allocation of resources to the most productive sectors via both public and private sector investments. Secondly, it will be necessary to target sectors with the highest and most dynamic growth potential. The reasons for the successes of the Asian tigers was the ability to successfully manage the macro economy for the purposes of structural transformation.

South Africa is currently faced with increasing energy costs and an unsustainable monopoly energy supplier that has massive debt and unstable energy supply. All projected economic growth requires a sustainable source of energy. To grow there will be further increased demands for energy supply, to about three times current capacity by 2050. However, as per approved government policy (Integrated Resource Plan), the coal-fired power stations that have been the backbone of the South African economy have to be decommissioned. Due to the economic responses to global climate change, investors are withdrawing from fossil fuels and renewables have become the cheapest source of energy. The just energy transition that is required can be a key driver of inclusive growth. The potential growth and scale of the new low carbon energy industry can catalyse the largest industrialisation programme since 1994. Upstream manufacturing and the development of local capabilities and product development to support the construction of renewables will introduce multiplier effects within manufacturing as new local markets are created.

South Africa does not have a debt crisis, but rather a GDP growth problem. Comparatively speaking our debt-to-GDP ratio reveals that in comparison to major economies our debt levels are nowhere near the impending crisis levels purported by those who insist we have debt crisis. Global debt levels have fallen from 245 percent of GDP in 2016, to 238 percent in 2019[5]. South African debt during the past decade has risen sharply. Before COVID 19 it was projected at worst to climb to 71.3 percentage points in 2022/23, from the 60.8 percentage points (2019/20) and estimated 65.6%(2021). The continued downward adjustments of tax revenue over the past few years has resulted in an expected under collection in future years. Rising public debt since the COVID 19 pandemic has shifted gross national debt expectations to 81.8% of GDP with long run implications estimation South Africa crossing the 100% mark in 2023/24 due to spiralling debt servicing costs. None of this means that the rising debt to GDP ratios cannot be sustained if the necessary growth rates can be achieved. The issue is whether the high levels of debt can be serviced, and future budgets balanced more efficiently. Government debt is not equal to household indebtedness; rather it is what function the debt plays in stimulating aggregate demand so as to boost economic growth. The economic posture speaks to preservation of the current economic framework and little effort to reconfigure the structure of South Africa’s low growth and low unemployment growth trap.

We argue that South Africa needs a fresh perspective, coupled with systemic changes in our government and planning agencies that monitor and measure the impact of interventions. There can be no sustained economic growth if townships, rural areas

[5] Estenssoro, A. 2019. A Decade after the Crisis, Has the Global Debt Burden Stabilised?

and regions that do not constitute the economic hubs of the future and remain ignored in the structural transformation project of our economy. Austerity measures without a decisive economic plan and strategy will not provide the much needed economic growth and transformation our economy requires. There is currently no consensus on the use of fiscal and monetary policy due to the influence of vested interests. Without a united approach providing fresh alternatives South Africa risks repeating the same mistakes with the same outcomes.

Although the pandemic has been projected to lead to further contraction of growth by 7.2%[6], massive closure of SMMEs with the business impact leading to 47,9% business temporarily closing with business turnover contracting by 90%[7]. The results show that 42% of business would not be able to continue to operate without turnover due to stringent COVID closure regulations. The resultant loss of turnover has had significant effects on the workforce whose work hours and have been directly impacted. The likely decrease in incomes will be felt in the medium term as spending will contract substantially across households. The downward trend is also matched by underperformance in tax revenue collections of almost 304 billion in the current fiscal year, leading to an estimated move from the 6.8% deficit of the February budget, to the now revised 14.6% deficit.

The entire globe is faced with unprecented economic shocks with fiscal expenditure increasing from between 3%-20% of GDP to stimulate economic activity. The reaction to this pandemic will no doubt determine our economic trajectory for the immediate and long-term future. We hold the view, however, that this is an opportunity to reconfigure, restructure and rebuild the South African economy.

The National Treasury projections estimate a bleak outlook with growth estimates of -7.2% (2020), 2.6% (2021) and 1.5% (2022). The proposed support and approach to the economic challenges will worsen South Africa’s structural economic problems. By securing IMF loan funding conditional on the enforcesment of free market policies, South Africa is effectively formalising what is has been implementing without multilateral agency conditionalities. Average growth in the last decade with these self-

[6] National Treasury Supplementary Budget Review. 2020.
[7] Statistics South Africa. 2020. Business Impact survey

same economic policies has been a dismal 1.9% resulting in an economic crisis that began way before the pandemic crisis.

This paper offers a compelling argument and is structured as follows: Section 2 presents the vision and timeframes, followed by the diagnostic assessment of the current economic status quo in Section 3. Section 4 discusses the challenges that need to be faced with respect to the economic fundamentals. Section 5 outlines the economic theory we apply to grasp the necessary fundamentals for the alternative economic framework. Sections 7,8 and 9 propose the necessary programs of delivery and related interventions.

This paper emerges from two workshops held in Stellenbosch by a group of economists working within a diverse set of public, private and research institutions (see Appendix for the names and affiliations.) These workshops were hosted under the auspices of the M-Plan initiative convened by Prof Thuli Madonsela, Chair of Social Justice, Stellenbosch University.

2. Vision and Time Frame

To realize the vision of a socially just South Africa, we need a well-being economy that is economically, socially and ecologically sustainable over the long run.

The vision of a socially just South African society is embedded within the South African Constitution. According to Professor Thuli Madonsela social justice is about "just and fair access to and equitable distribution of opportunities, resources, privileges and burdens in a group or between groups. … It is ultimately about equal enjoyment of all rights and freedoms by all regardless of human diversity and historical injustices." This interpretation of the Constitution stems from the values and human entitlements expressed in the Constitution. The key values are the achievement of equality, human dignity and freedom for all. The basic human entitlements this gives rise to in the Bill of Rights are civil and political rights, social and economic rights, cultural rights and environmental and development rights.

It is this vision that is contradicted by the harsh reality that 25 years after democracy, over 90% of all asset wealth is still in the hands of 10% of the population (most of whom are white). The top 1% of the population experienced the most significant increases in wealth since 1994 compared to all the other sectors of society. Economic growth on its own has been insufficient to ensure greater inclusion.

The translation of the Constitutional vision of social justice into economic policy will mean going beyond a narrow focus on economic growth as the necessary and sufficient condition for "equal *enjoyment* of all rights and freedoms by all regardless of human diversity and historical injustices." From this perspective, it makes more sense to refer to a commitment to a *well-being economy*. The Sustainable Development Goals adopted by the UN in 2015 establishes the indicators for a well-being economy. This is because they go well beyond GDP growth as the only significant indicator of progress. When progress is no longer measured in terms of the quantum of marketed goods and services (GDP) but also with reference to eliminating hunger and poverty, reducing gender and overall inequality, sustainable production and consumption, clean energy, urgent action on climate change, and restoring marine and terrestrial ecosystems, then it is a well-being economy that is envisaged.

To achieve a wellbeing economy, the overall goal needs to be sustainable wellbeing with dignity and fairness for humans and the rest of nature. Wellbeing is achieved when humans are mentally and physically healthy, there is greater equity and fairness, everyone has a sense of place because they are embedded in sound social relationships and the natural environment is flourishing.

For Costanza et. al., to "achieve a wellbeing economy, a major transformation of our world view, society and economy are needed to:

a. Stay within planetary biophysical boundaries – a sustainable size of the economy within our ecological life support system.
b. Meet all fundamental human needs, including food, shelter, dignity, respect, education, health, security, voice, and purpose, among others.
c. Create and maintain a fair distribution of resources, income, and wealth – within and between nations, current and future generations of humans and other species.
d. Have an efficient allocation of resources, including common natural and social capital assets, to allow inclusive prosperity, human development and flourishing. A wellbeing economy recognizes that happiness, meaning, and thriving depend on far more than material consumption.
e. Create governance systems that are fair, responsive, just and accountable."

3. Diagnostic Assessment: Economic Status Quo

An analysis of the South African economic indicators points to a worsening economic crisis with poor performance during most of the last five decades. Pre-1994, the exclusion of the large majority of the population resulted in economic gains benefiting the white elite. The state, finance and industry worked together to build a highly concentrated economy. A dozen people controlled the large bulk of the South African economy by the time negotiations with the ANC began from the late 1990s onwards. Commercial banks and finance capital supported the growth and expansion of the mining sector, with infrastructure development and labour market policies developed to support a strong mineral export capability. Four key institutions were developed during the first half of the c.20th that drove the industrial growth of the country, two private entities Barclays Bank and The Sanlam Group, and two state entities, the Industrial Development Corporation and National Finance Corporation. These institutions played a pivotal role in the state-led industrialisation machinery, as well as mining growth. It was during this time that the state would finance the establishment of institutions that drove economic expansion of these primary sectors, such as Eskom and Iscor.

The differences in economic realities experienced by South Africans is determined largely by race, and since 1994 by education (which, of course, is an apartheid legacy). South Africa's failure to build a fully industrialised national economy is due to the fact that growth for more than five decades was premised on low wages and unskilled black labour[8]. Without higher wages, a small domestic market could not sustain a fully industrialised economy. The gains generated from an export growth model based on minerals extraction could have catalysed a fully modernised industrialised economy. However, the perennial challenge facing the South African economy during the pre- and post-1994 era has been the limited purchasing power enjoyed by the large working population. International sanctions fundamentally harmed the South African economy, paving the way for a negotiated settlement. Racially exclusive capitalism has not been replaced by a radically different model after 1994. The phenomenon of

[8] Hart, K., Padayachee, V. 2013. *A history of South African capitalism in national and global perspective.* Transformation 81/82.

corporate dominance over a large portion of the economy plus high levels of concentration has resulted in the continued movement of capital towards the growth of these sectors. The growth path of finance and capital and the strategic role of state-owned enterprises has reinforced the dominance of the mineral-energy complex during the post-1994 period. The question to ask post 1994 is whether finance has changed its investment portfolio. To what extent have state entities been used to grow exports and the development of related or linked manufacturing sectors that absorb the majority of those previously excluded? If they have not changed, what policy mechanisms should be employed to change the financial flows? How should key institutions within the fiscal and monetary policy sphere be used to reverse this minerals-energy complex?

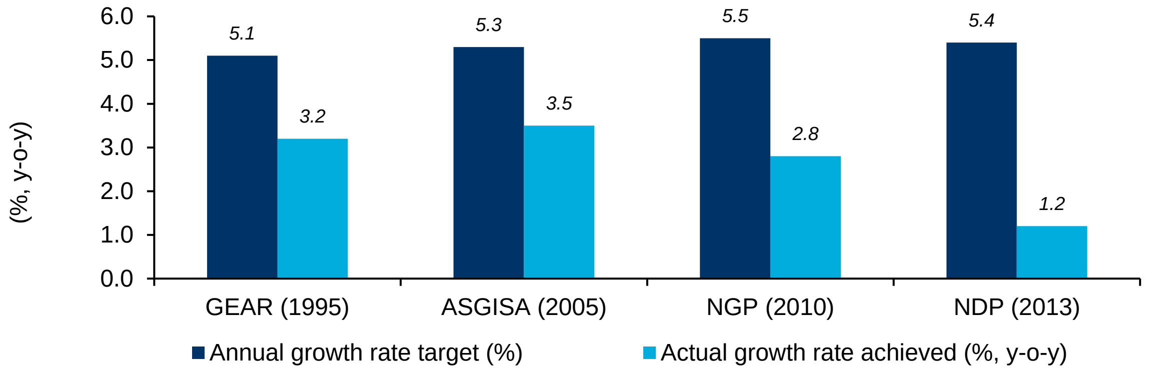
Recent trends confirm the argument that South Africa's economy is locked into a particular path dependency that is challenging to break out of.

Economic growth

During 1960-1980, the economy grew at an annual rate of 4.5%[9], supported by abundant natural resources. Despite an impressive growth record in the post-1994 period, the reliance on natural resources coupled with stringent economic sanctions ushered the country into subdued economic growth. The onset of democratic governance was marked most notably by South Africa's process of trade liberalization and access to global export markets. The reduced political turmoil and a boost in aggregate demand and consumption by government services are some of the factors which saw the economy recover from an average annual growth rate of 1.0% (1984-1993) to 3.0% (1994-2003)[10]. It is during this period that a series of economic policy packages were introduced to balance out apartheid-related inequities through job creation, proper housing incentives and overall socio-economic development. Some of these policies include GEAR, ASGISA, RDP, NGP, and the most current NDP.

Figure 1: Actual annual economic growth rates versus policy rates targets[11]

[9] SARB. 2019. Resbank Statistics. (Real GDP figures expressed in constant prices)
[10] SARB. 2019. Resbank Statistics.
[11] Investec. 2015. Investec GIBS Savings Index: The real facts about saving.



Sources: (SARB (2020) and Investec (2015))

Figure 1 shows how the economy underperformed despite the strategic policies that were put in place. Furthermore, South Africa's high integration with international markets and vulnerabilities to external shocks also affected economic growth over the analysed period. The 2008 financial crisis (which saw the economy contract by 1.5% y-o-y in 2009) exposed the country's vulnerabilities. Economic growth reached its highest peak of 5.6% y-o-y in 2006. Since then, however, economic growth moderated, but failed to recover from low growth rates post the 2009 global recession. GDP growth plunged to 0.2% y-o-y in 2019, partially due to persistent electricity supply deficits, limited investments in the real economy, failure to industrialize and inability to improve income levels. Despite high levels of financialisation and strong links to global markets the nation experienced a technical recession in the first quarter of 2019. This is expected to contract even further this year due to sudden economic and financial shocks triggered by the ongoing COVID-19 pandemic. As such, what seemed to be Africa's most prominent powerhouse, is now an economy that has effectively reversed to pre-1994 levels of economic growth.

Per Capita GDP

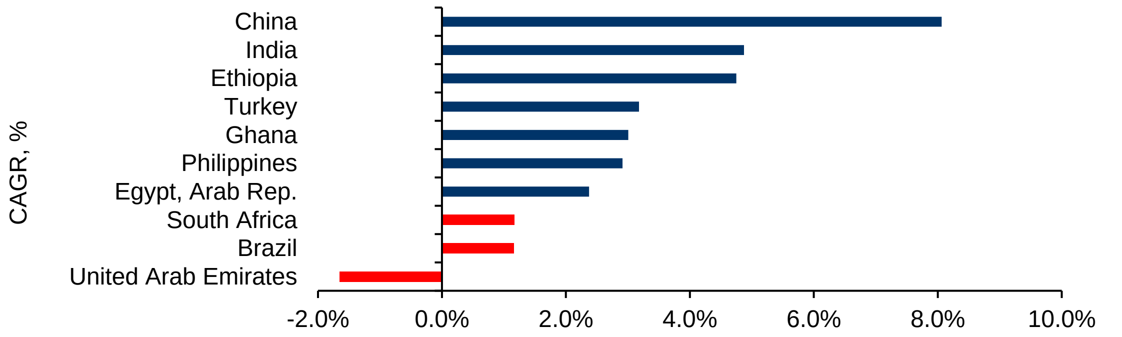
There is a widening gap between GDP per capita growth rates in South Africa compared to those in emerging markets. The differences were largely on the back of the GEAR and ASGISA growth policies. In the 25 years since 1994, the South African economy has achieved an average annual growth rate of 2.7% p.a.[12] (compared to 5.7%[13] for the selected emerging markets). This is higher than the average population

[12] SARB. 2020. Resbank Statistics.
[13] IMF. 2019. World Economic Outlook database.

rate of 1.8% (compared to an average population growth rate of 2.3% for selected emerging markets) during 1994-2018. This shows that despite economic growth accelerating at a faster pace than the population growth, GDP per capita in South Africa remained relatively low, growing at a compound annual growth rate of 1.2% p.a. during 1994-2018[14]. This is confirmed in

Figure 2 below which clearly shows that Brazil and South Africa have experienced muted GDP per capita growth over the past 25 years. Descriptive evidence shows that South Africa's GDP per capita in 1994 registered at $9,090 reached its peak of $12,381 in 2014 and contracted to $11,954 in 2019[15]. This further heightens the deep-rooted issue of a widening inequality gap which is caused by discrepancies in the allocation of economic benefits among the population.

Figure 2: GDP per capita of South Africa and selected emerging markets (1994-2018)[16]

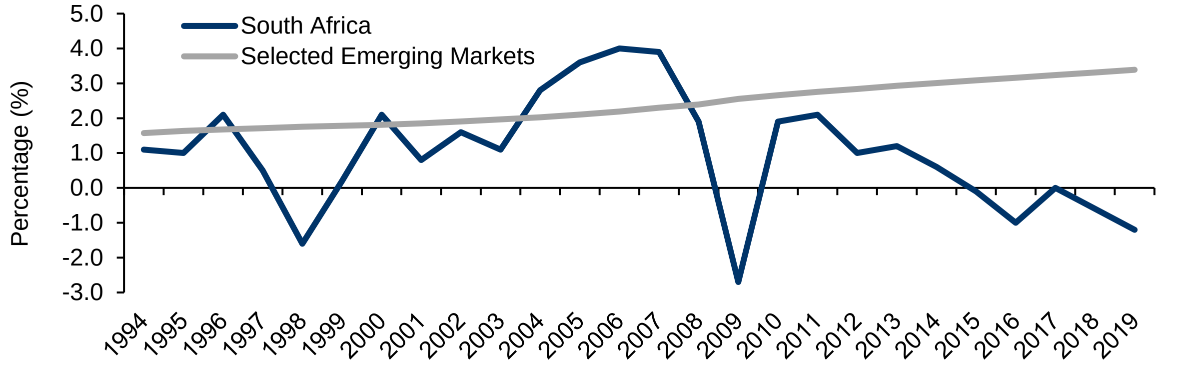


Source: (World Bank, 2019)
Note: GDP Per capita (constant 2010 US$) is expressed using the compound annual growth rate from 1994 to

Further evidence on South Africa shown in Figure 3 indicates a volatile GDP per capita, which is vulnerable to global economic shocks. However, it is crucial to note that despite the dire impact that various global economic crisis have had on the respective economies, their GDP per capita continued to rise as their economies recovered, while South Africa's GDP per capita continued on a downward trend. The deterioration of the growth rates after 2009 shows the inability of the economic gains to improve the standard of living.

[14] World bank. 2019. DataBank: World Development Indicators.
[15] IMF.2019. World Economic Outlook database.
[16] World Bank.2020. DataBank: World Development Indicators.

Figure 3: GDP Per Capita [17]



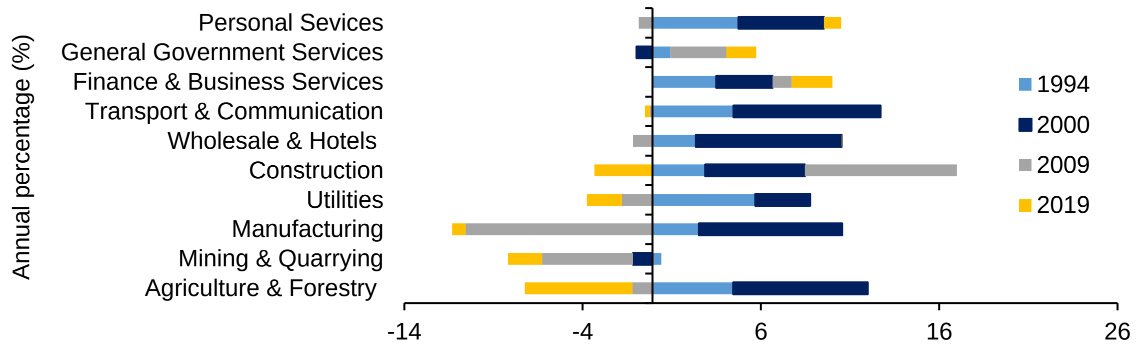
Sources: (SARB and IMF, 2019)
Notes: The Emerging Markets GDP Per capita is estimated using IMF's GDP on purchasing-power-parity (PPP) share of world total (Percent)

Sub-sector analysis

The South African economy was traditionally rooted in the primary and secondary sector. The key growth drivers during the 2000s stemmed largely from the expansion of household consumption underpinned by significant increases in household debt to income levels. With regard to historical sub-sectors performance over the 1994-2000 period, the manufacturing, agricultural, wholesale and retail, utilities and transport & communication significantly contributed to overall economic growth. However, South Africa's exposure to global shocks weighed on its overall economic performance. This was evident in 2009 (a year after the devasting global financial crisis) where these key sub-sectors contracted significantly. Data shows that despite various economic policy interventions, the country is still much exposed to the volatile global commodity market.

Figure 4: Historical Sub-Sector Analysis

[17] Selected emerging markets : Brazil, China, Ethiopia, Ghana, United Arab Emirates, Turkey, Philippines, India, Rwanda and Egypt. The use of these emerging markets was driven by the historical economic performance of the respective countries in light of historical economic policy changes, as well as comparing the performance of various macroeconomic indicators over time with same-like economies. These EMEs will be used in all EME comparisons in the paper except otherwise stated.



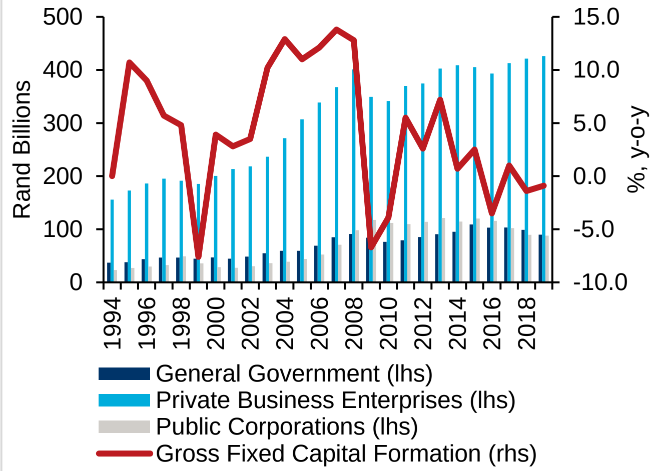
Source: (Statistics South Africa, 2019)

Gross Fixed Capital Formation

The level of investment in land, equipment and machinery is an indicator of re-investment and growth in the real economy. In terms of year on year changes, gross fixed capital formation (GFCF) in South Africa has declined substantially after the country declared its democracy in 1994 (Figure 5), recording its largest drop in 1999 during the Asian crisis (-7.6 % y-o-y) and post the financial crisis in 2009 (-6.7% y-o-y). Investment peaked between 2003–2008 and has since experienced feeble growth. Figure 6 further indicates that South Africa's GFCF is growing at a slower pace than two of the selected emerging markets, recording a compound annual growth rate of 0.05% p.a, compared to 1.32% and 0.29% for China and Turkey.

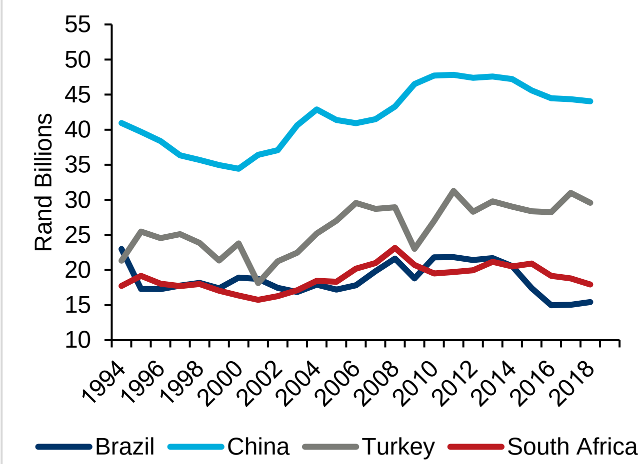
Furthermore, amongst the analysed key contributors to GFCF (Figure 5), private business enterprises outperformed the other analysed contributors in terms of investment, accounting for an annual investment average growth rate of 71.1% (during periods 1994-2003) and 66.0% (during periods and 2009-2019), respectively. But these trends in comparison to our global emerging competitors fare quite low and are deteriorating as Figure 6 outlines. Against this backdrop, private business enterprises need to play a more influential role in attracting investment in the South African business environment whilst also re-investing into the economy. Therefore, policies aimed at improving the business environment and private sector growth should be prioritised as this has the potential to attract further investment inflow, as well as unlock additional revenue for the government.

Figure 5: South Africa's GFCF contribution breakdown



Source: (SARB, 2019)

Figure 6: SA's GFCF comparison with selected emerging markets



Source: (World Bank, 2019)

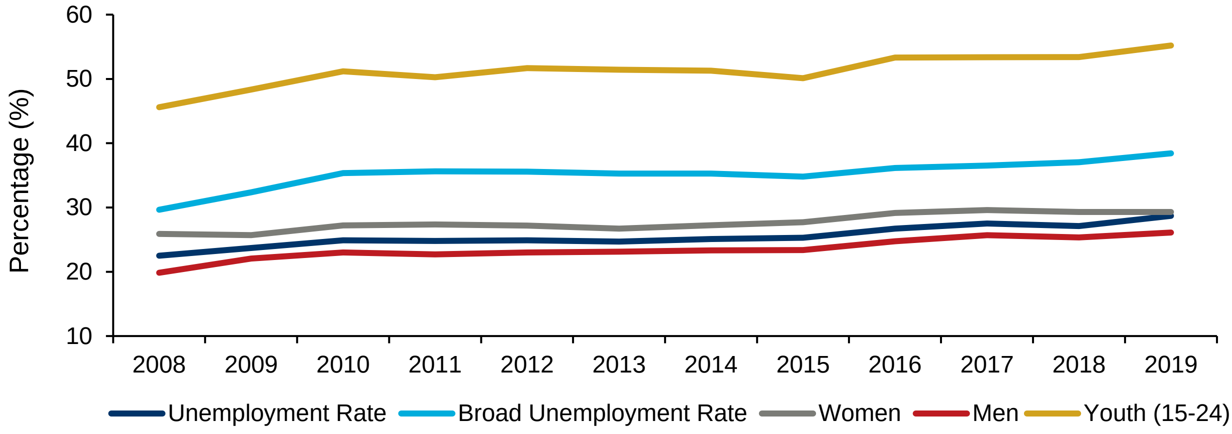
Unemployment rate

The unemployment rate remains the most fundamental indicator of the health of the economy. At 29.1% in 2019 (quarter three estimate), South Africa clearly has a jobs crisis. Unemployment has remained stubbornly above the 21% level since 1994, with worsening outcomes based on age, level of qualifications, gender or region. To put this into context, the unemployment rate for women between the ages of 15-64 stands at 31%, while its male counterpart registers a lower rate of 27.7%[18]. Furthermore, economic policies reduced unemployment between 2000-2008, but levels of unemployment remained unchanged for black youth, and more so for women. Failure to absorb the 15-24-year-old cohort into the labour market has led to heightened levels of youth unemployment of 58.2% (in the third quarter of 2019) - this number is even higher (61.7%) among the youth without a matric qualification[19]. Furthermore, weak economic growth, de-industrialisation and contracting primary sectors, coupled with a stressed fiscal balance, has put additional pressure on the South African labour market. The number of discouraged work seekers is a staggering 2,8 million because the labour market fails to absorb youth into the world of work. Women discouraged work seekers (between ages 15-64 years) in quarter three of 2019, registered at 1.5 million, compared to 1.3 million for men. This shows the widening of the inequality gap,

[18] Statistics South Africa. Quarterly Labour Force Survey. Quarter 3: 2019.
[19] Statistics South Africa. Quarterly Labour Force Survey. Quarter 3: 2019.

particularly amongst women and the youth, as well as the continued exclusion of women in the formal labour market.

Figure 5: Overview of South Africa's unemployment rates

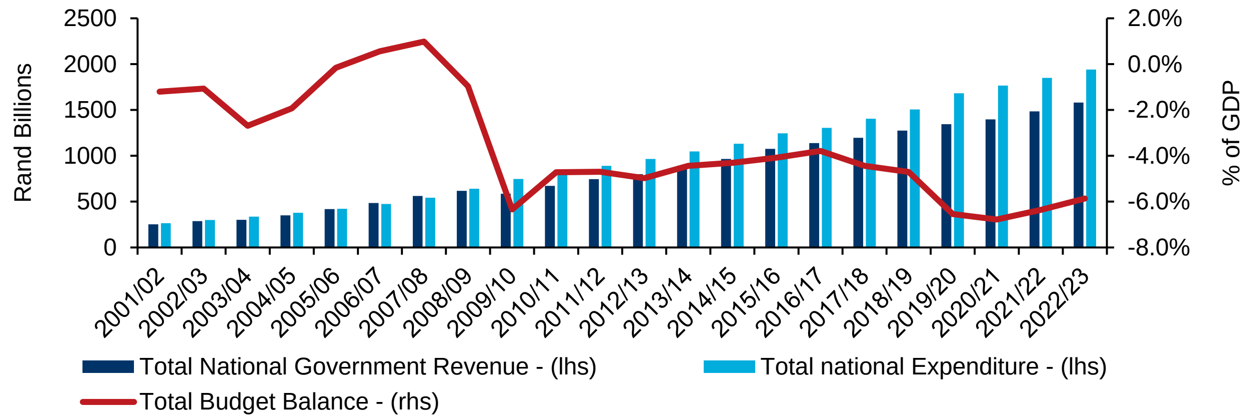


Source: (SARB and Statistics South Africa, 2019)

Fiscal Position

In 1994, the democratic South African government inherited significant socio-economic backlogs due to systemic exclusion by apartheid policies. The government adopted a Reconstruction and Development (RDP) programme which aimed at addressing developmental challenges. However, this was quickly overtaken by GEAR in 1996. The aim of the RDP was to ensure growth through redistribution, whereas GEAR's main emphasis was to foster economic stability with a focus on macroeconomic policy. Fiscal frameworks narrowed the significant fiscal deficit. However, the economy failed to recover post the 2009 financial crisis. In order to respond to the financial shock increased social and investment spending occurred to facilitate economic growth, widening the deficit in a weakening growth scenario. Over the last five years, however, the country's fiscal position weakened significantly due to continued weak growth and reduced collected tax revenues. Further pressure on state expenditure is worsened by ailing state efficiency and significant financial leakages from state institutions due to state capture. South Africa's budget shortfall worsened to 6.5% of GDP in FY 2019/20, from a smaller 1.1% of GDP deficit recorded in FY 2002/3. Economic policies have been aimed at ensuring fiscal sustainability whilst rebuilding ailing sectors. Since 2009 we have experienced a structural deficit, with the fastest growth being costs of servicing debt. Adjustment policies must improve the composition of spending, reprioritising the expenditure to support long-term economic growth, while managing existing risks, erasing socio-economic inequalities created under the apartheid regime and fostering sustainable use of resources.

Figure 8: South Africa's Fiscal State

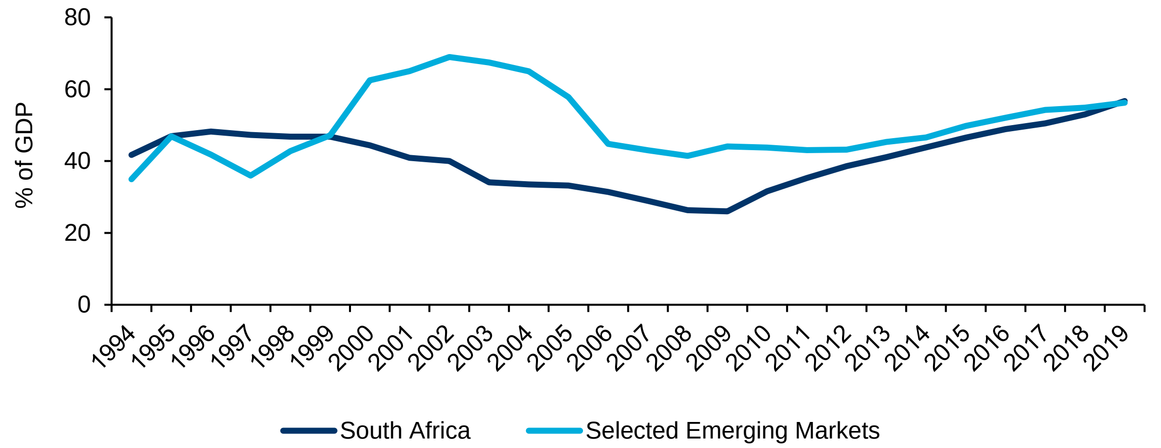


Source: (Statistics South Africa, 2019)

Government Debt

The accumulation of debt in South Africa has primarily been driven by persistently feeble economic growth, exacerbated by the poor performance of SOEs. Over the 1994-2019 period, government debt has expanded by a compound annual growth rate (CAGR) of 11.3%. Global economic events over the years have exposed the country's vulnerabilities and lack of external buffers. Government debt significantly increased post the global financial crisis and has since been on an upward trend. Stimulating the economy back to normality after any economic crisis will inevitably trigger debt. In comparison with Brazil, South Africa's gross debt as a percentage of GDP over 1994-2019 is relatively lower than that of Brazil. Despite differing magnitudes, South Africa and Brazil's large debt stocks are mainly due to their precarious fiscal position and feeble economic growth. Therefore, the government needs to focus on the feasibility of various public enterprises and prioritise expenditure for businesses that contribute to the alleviation of the country's know triple threat of poverty, inequality and unemployment. Furthermore, expansionary monetary policy should be applied, with intentions of developing fiscal plans and expenditure controls that will prioritise funding of sectors and industries that will create more job opportunities and stimulate the business environment.

Figure 9: Government Debt Comparisons

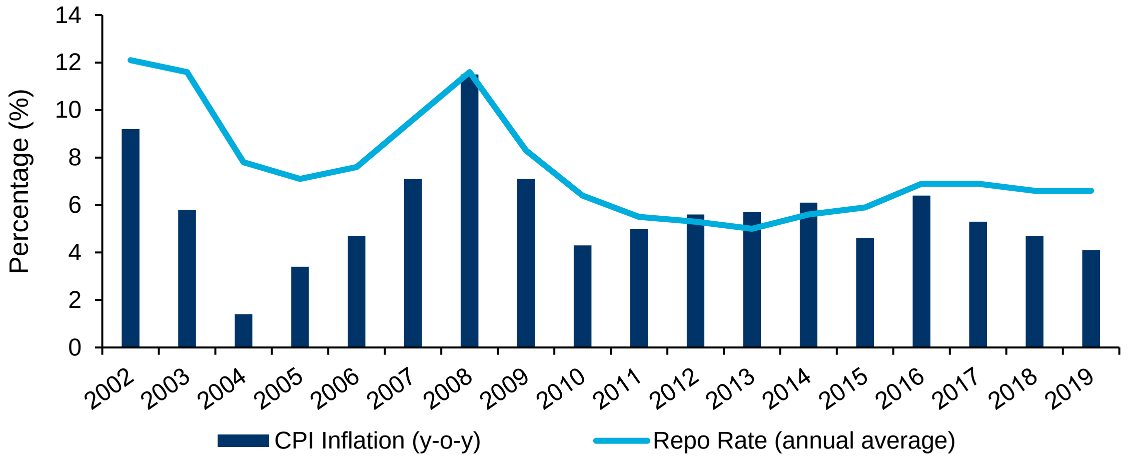


Source: (IMF and SARB, 2019)

Inflation and the Repo Rate

Inflation trends in South Africa were high during the 1980s and 1990s, averaging around 14% p.a, but monetary policy focussed on inflation targeting decreased it to 7% p.a over the 1994-2002 period. This has been the most effective instrument for yielding price stability, and inflation levels have stabilised within the targeted 3-6% range in recent years. Interest rate hikes, such as in 2002 and 2008, effectively quelled inflation levels of double-digits. Adverse effects include the high costs of servicing debt as the costs of borrowing continues to rise.

Figure 10: Inflation and Repo Rate



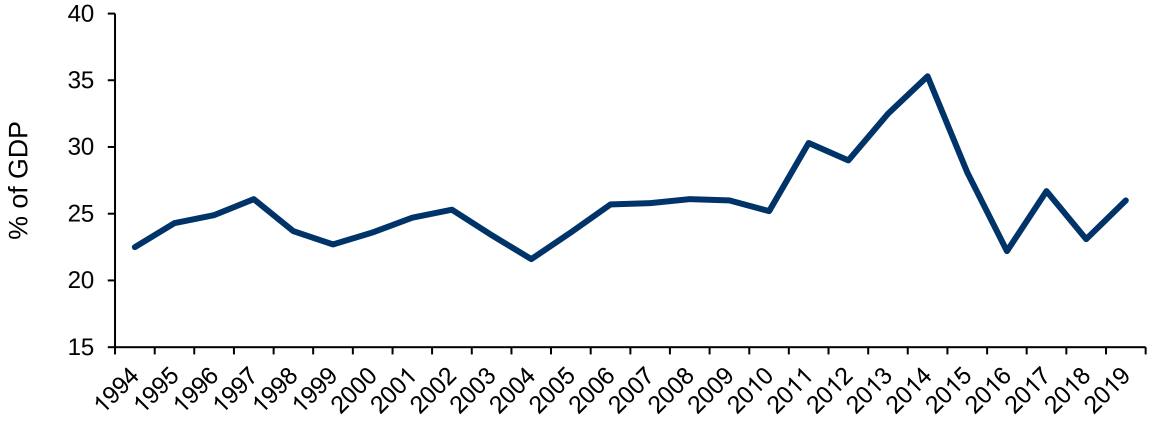
Source: (Statistics South Africa and SARB, 2019)

Savings Rate

South Africa has predominantly been a consumption-driven economy. Limited personal savings means that the poor in particular are not protected against unforeseen shocks. Moreover, if savings levels were higher this could be used to fund long term investments in human and economic development. According to the Investec GIBS Savings Index[20] report, inadequate savings diminishes investment and has negative spill overs on economic growth and employment. The index further shows that South Africa's savings levels are at their worst level since 1990. The South African Reserve Bank shows that South Africa's ratio of gross savings as a percentage of GDP only grew by a CAGR of 0.6% over the 1994-2019 period. Furthermore, the lack of financial inclusion for small businesses and poorer income groups further weighs on the already subdued savings rate. The country's lacklustre economic performance undermines government efforts to encourage saving behaviour (through the tax-free savings account among many).

20 Investec.2015. Investec GIBS Savings Index: The real facts about saving.

Figure 11: Ratio of Gross Savings



Source: (SARB, 2019)

Investment (as %GDP)

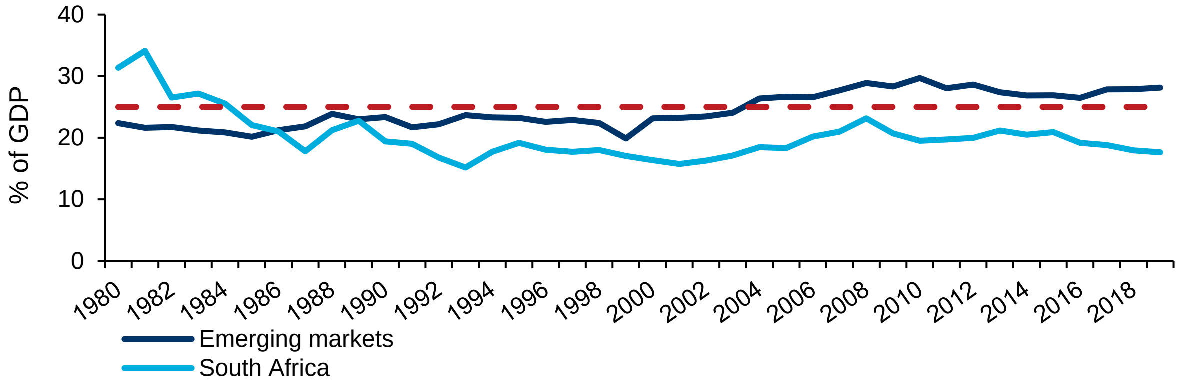
The pivotal role that investment plays in fuelling sustained economic growth has been well documented in economic literature[21]. Figure 12 shows that South Africa's total investment as a percentage of GDP is growing at a lower rate than that of the selected emerging markets over the 1994-2003 period. The International Monetary Fund's most recent data release shows that South Africa's total investment in 2019 registered at 17.6% of GDP, which is lower than the investment rate recorded in 1994 of 17.7%[22]. Furthermore, the Fund shows that total investment for the selected emerging markets registered a CAGR of 0.76% p.a over the 1994-2019 period, while South Africa's total investment rate contracted by 0.02% p.a over the same analysed period. The government's efforts to encourage investment inflows into the country have been counterweighted by feeble economic growth, political instability, weak savings rates, dysfunctional SOEs and high government debt. Among the aforementioned contributors to lack of investment, the underlining factor is that the South African economy is not growing, and this causes negative spill over effects on other key macroeconomic indicators, which in turn discourages investment activity. Overall fixed investment growth rates have been below GDP growth, suggesting that the private

21 Roy Harrod (1939) and Evsey Domar (1946), which later received a strong endorsement from Robert Solow (1956) and TW Swan (1956), among others.

22 IMF. 2019. World Economic Outlook Databases.

sector remains hesitant to expand capacity despite economic policies geared towards encouraging fixed investment as a % of GDP.

Figure 12: Total Investment

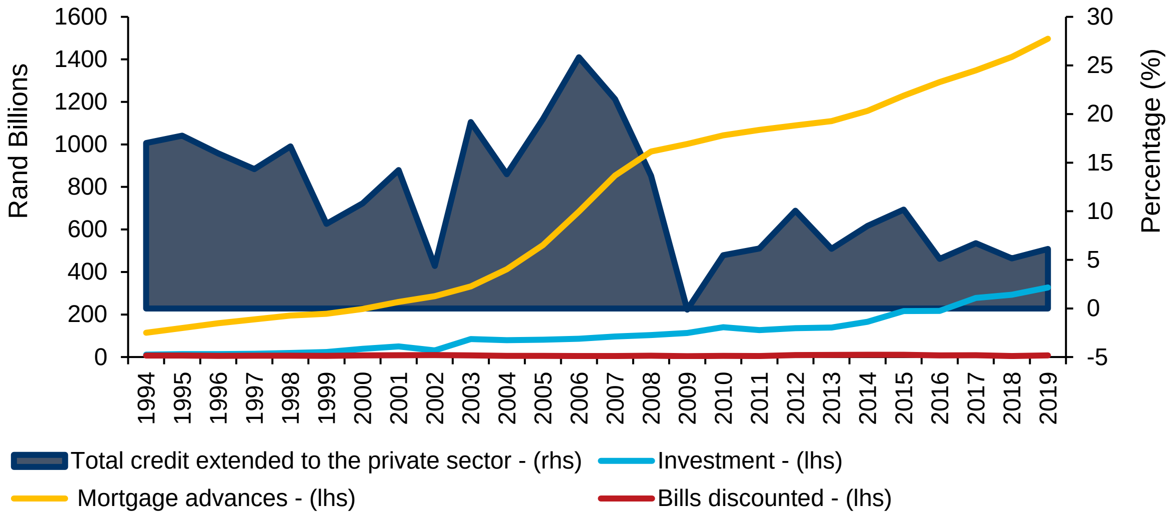


Source: (IMF, 2019)
Note: The red line represents the targeted benchmark for total investment for this study

Private Sector Credit

The public's demand for bank credit remained resilient. Private sector-led development in the 1990s to 2004 was a key tenet of GEAR, with the expansion of private sector credit extension (PSCE) as one of its key objectives. This reinforced the balance sheets of the five major banks who together control 85% of all financial assets. Rapid internationalisation, opening of trade barriers, and the loosening of capital controls in South Africa have supported PSCE the position of the banks within an increasingly financialised economy. However, total credit extended to the private sector declined from 14.2% y-o-y in 2001 to 6.1% y-o-y in 2019. The bank's total credit to the private sector is mainly comprised of mortgage advances, with a widening gap showing that a minute proportion is allocated to actual investment which barely rose beyond R293 billion in 2018.

Figure 13: Total Credit Extended to the Private Sector



Source: (SARB, 2019)

Increased levels of access by households to bank credit during this period is linked to the rising household income to debt ratios, which was the main driver of economic growth in the late 2000s. Post 2009 the continued resilience in demand for bank credit by the private sector was supported by relatively low debt levels, expectations of a decline in interest rates and ongoing increases in the price of mortgages. However, in the past five years, private sector credit has decreased, mainly due to bills discounted and mortgage advances. Subdued economic growth as well as exchange rate differentials and volatility pose upside risk for the private sector credit. Expansionary monetary policy may alleviate this problem, but only if it succeeds in stimulating the economy and providing inclusive financial support to small- and large-scale firms within the private sector.

Latest data shows that despite a resilient banking sector, only 80% of the adult population have formal bank accounts, while those using non-banking services increased from 72% to 74% in 2017[23]. Furthermore, financial inclusion in urban areas (90%) is greater than that in townships/rural areas (81%). While racial inequality continues to widen in the financial industry, with 97% financial inclusion for whites, compared 86% for black South Africans. This shows that despite a stable financial

[23] South African Institute of International Affairs (SAIIA). 2019. Digitising Financial Services: A Tool for Financial Inclusion in South Africa?

sector, inequality with regards to geographical placement and racial disparities continues to be a core issue. It is therefore imperative to consider broadening the scope of the South African financial sector.

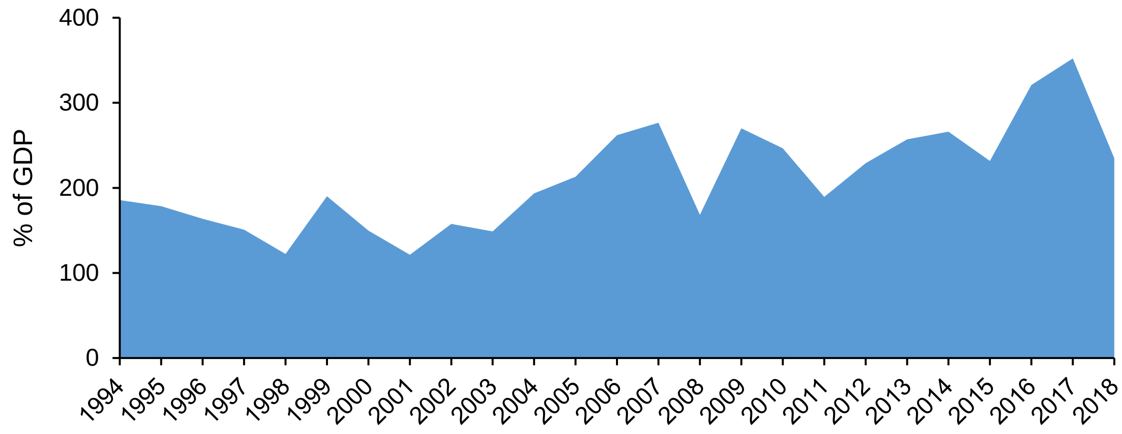
MARKET CAPITALISATION

Historically, South Africa was part of the group of fast developing countries in Africa. It has since been surpassed by some Eastern and Central African counterparts, despite smaller concentrations of capital assets. The country's gross domestic product (GDP) is largely accounted for by its stock market, which far exceeds that of other growing developing economies such as Mexico and Indonesia[24]. The JSE's significance in the national economy, measured by the ratio of market capitalization to GDP has remained stable, performing efficiently over the years, increasing to 235% of GDP in 2018, reaching a peak of 352% in 2017, up from 185.7% of GDP in 1994[25]. The stock market capitalization of more than three times the national GDP is significant, with equity markets and bond issuances surpassing most countries in the region. Capital markets remain volatile and unpredictable, though they exhibit potential to accelerate economic growth. But in times of financial crisis they are highly volatile. South Africa's high exposure to international markets poses downside risk for the economy, as the unpredictable fluctuations in the capital market can undermine the effectiveness of economic policy. Despite the downside, a well-developed and inclusive financial sector has the potential to grow domestic savings and allocate capital for productive projects that encourage economic growth.

The ability to use domestic capital markets for the advancement and growth of the real economy remains essential for furthering national growth initiatives. In order to reduce alternative sources of finance and debt, domestic capital flows remain under-utilized and efforts to increase allocation of domestic capital markets for funding investment remains crucial for national growth and development agendas. This will be furthered in detail in section 7 of the paper.

Figure 14: Stock Market Capitalisation

[24] Hassan, S. (2013). South African Reserve Bank Working Paper Series WP/13/04. South African Capital Markets: An overview.
[25] The Global Economy. 2019. South Africa: Stock market capitalization, percent of GDP.



Source: The Global Economy, 2019

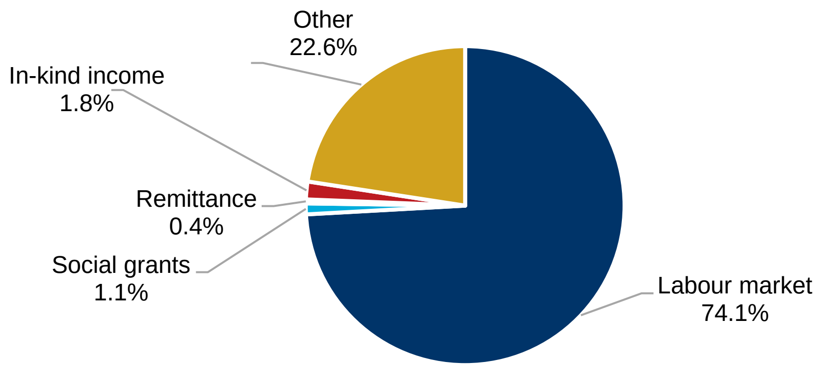
Poverty and income inequality

Poverty and inequality in South Africa have long been recognised as one of the most salient features of our society. South Africa is consistently ranked as one of the most unequal countries in the world, an empirical fact that has its roots in the history of colonisation and apartheid. To confront the challenge of addressing South Africa's triple threat (poverty, unemployment and inequality), higher rates of economic growth underpinned by redistribution and job creation are crucial. The importance of triggering robust economic growth matched by improved productivity and expansion of the real economy is highly emphasised in this study. Although the government of South Africa has repeatedly included growth imperatives in their various national policy proposals (GEAR, ASGISA, NGP, NDP), it has failed to adequately reduce the number of people living in poverty and who rely heavily on government cash transfers. The main drivers of poverty and inequality include continuous weak economic growth, deteriorating manufacturing sectors, ineffective income redistribution policies, lack of investment inflows, underdeveloped informal sector, inadequate educational infrastructure and services, deteriorating healthcare system and lack of financial inclusion for poorer households. Latest data shows that the top 10% of the population spent 8,6 times more than the bottom 40% in 2006, dropping to 7,9 in 2015[26]. Despite South Africa's high Gini coefficient, overall poverty, measured at a national level, has declined between 2006 and 2015 but it remains stubbornly high at over 30 million falling below the poverty line[27]. However, the country's labour market has severe gender and race

26 Statistics South Africa. 2019. Inequality Trends in South Africa: A multidimensional diagnostic of inequality.
[27] Statistics South Africa. 2019. Inequality Trends in South Africa: A multidimensional diagnostic of inequality.

biases, with female workers earning approximately 30% less than male workers for similar jobs. With regards to race, the mean real earnings between 2011 and 2015 amongst employed black Africans was R6 899 per month, for coloureds and Indians/Asians this was between R9 339-R14 235 per month, and for whites, it was R24 646 per month. The income discrepancies between blacks and whites has over the years widened, despite policy interventions such as BBBEE. The data suggests that poverty is concentrated amongst black females, thus policy responses need to have a gendered response to effectively deal with the labour market discrimination.

Figure 15: Relative Contributions to Inequality by Income Sources based on the Gini Coefficient



Source: (Statistics SA,2015)

Data from Statistics South Africa further shows that from 2006 to date, lower or bottom deciles are increasingly more dependent on social grants than on income from the labour market. This poses significant risk for the government as such dependency has the potential of increasing the likelihood of generational poverty. Therefore, regulations to deal with formal and informal sector labour market practices need to re-evaluate to ensure that the bottom deciles are not exploited to the extent that social services become more favourable than seeking employment.

SMME Growth

SMMEs can be a dynamic transformational force since, in the words of the World Bank, 'relative to larger firms'. SMEs enhance competition, entrepreneurship, job growth and spur economy-wide efficiency, innovation and economic growth. However, a lack of credible data makes it hard to estimate the full impact of these businesses on the domestic economy. The Small Enterprise Development Agency[28] provides some insights into this business environment, which include:

- The number of SMME enterprises has been on an upward trajectory from over the 2017-2019 period, increasing from 2.4 million in 2017 (Q1) to the current 2.6 million in 2019 (Q1).
- Number of formal SMMEs increased by 11.8% y-o-y in 2019 (Q1) compared to the same quarter in 2018, while informal SMMEs moderately increased by 2.3% y-o-y.
- In 2019 (Q1) SMMEs mostly operated in the trade & accommodation industry (41.3% of total SMME's), as well as construction (13.9% of total SMMEs).
- The share of SMMEs less than three years in business has gradually declined from 35% in 2008 to 26% in 2019 (Q1).

Behind this backdrop, it is clear that SMMEs can play a vital role in the provision of goods and services, and this requires a rethinking of value chains and point of sales within local markets. A high concentration index of oligopolies currently controls these at a retail level, constraining the ability for local businesses to meet demand. Despite the growth in the number of SMMEs to date, the lack of infrastructure support and funding creates additional market entry barriers and encourages oligopoly practices in South Africa.

South Africa has experienced sluggish economic growth over the past few years. The country's exposure to global shocks is also larger given the high degree of integration with international markets. Despite overcoming various global economic crisis, the country's inability to generate more jobs during periods of improved economic growth has worsened the socio-economic conditions that the country inherited in 1994. Moreover, a series of economic policy packages have failed to address the underlining

[28]Small Enterprise Development Agency. 2019. Annual Report 2018/19.

issues of inequality, unemployment and poverty. Subdued investment growth and private sector development further weigh on the already depressed business environment. One thing is clear, South Africa's considerable economic potential can be achieved only if the right policy mix is conceptualized at the very outset of this new era. Restructuring government expenditure by raising investment to mainly target the poor and underprivileged could assist in narrowing income inequality and encouraging sustainable job creation. As discussed in more detail below, expenditures need to be targeted at the building of productive capabilities and the strengthening of new economic entrants.

In summary, all these indices in section 3 point to the economic performance and health of the economy. Covid-19 will worsen some of these conditions. The next section discusses the underlying drivers of the economic crisis and challenges that will continue to impede economic performance in the post-COVID-19 health pandemic if nothing changes.

4. The core challenges that need to be faced

The economic impact of the COVID-19 pandemic and the subsequent lockdowns emanating from governments to safeguard the lives of their citizens has the potential to cause economic disaster worse than the global financial crisis of 2008. Unlike historical disasters such as wars where nations suffered based on their proximity to Western Europe, this pandemic has left no economy unaffected. It is reported that the military conflicts of the 20th century accounted for 150 million deaths. These political decisions had far reaching economic effects. Western European economies after WW1 experienced economic output contracting by 11%, whilst Asian and Latin America real GDP rose by 13% and 4% respectively[29]. The projected global magnitude of economic disturbance will result in a 3%[30] GDP contraction in 2020, whilst domestic GDP is also expected to contract by 7.2%[31]. This section will look at the core challenges that must be addressed in the economic strategy such as the pandemic,

[29] Olivier, M.J., Aldcroft, D.H. 2007. Economic Disasters of the Twentieth Century. Edward Elgar Publishing Limited. USA: Massachusetts.
[30] IMF.2020. Chapter 1: Global prospects and policies.
[31] National Treasury. 2020. Supplementary Budget Review.

widening inequality, unacceptably high poverty levels, with a current economic strategy that fails to adequately respond to the fundamental growth challenges.

The most imminent challenge all economies will face is beyond estimating the economic impacts and effects of the COVID-19 pandemic, but more so the measures that should be taken to directly mitigate the direct and indirect impacts of production shutdowns. These measures would need to be in response to the estimated economic losses once the true costs of COVID-19 are assessed. In this post COVID-19 recovery the economic losses do not incorporate loss of fixed capital value that is usually eroded with economic crisis. The data on the full impact of COVID-19 is constantly changing, but some work has been cited prior to the release of this paper. Some studies have estimated sectoral effects using Social Accounting Matrix and econometric modelling in a combination of sectors and activities[32]. Shocks will be expected in the supply of goods and services, with disruptions in supply due to reduced activity in various economic sectors. Non-essential business operations will suffer the most. Movement restrictions will reinforce this contration. Severe travel and movement restrictions also affect the movement of South African exports whilst the combined global supply chain disruptions have severely reduced production on the entire global value chain. The following impacts of the economic crisis can be anticipated:

- global shocks and lower commodity demands are estimated to cause exports to fall by 40-75% - the decline in agricultural exports will be less drastic;
- household demand will decline substantially both during and post-pandemic due to reduced movement, loss of income as companies reduce wages and reduced workforce adversely affect employment;
- wage earnings will be disrupted by an estimated 30%, with variations ranging between 25-40% reduction - lower income households will be hardest hit by loss of wages;
- the disruption of the production of consumer goods and services will lead to contractions of up to 60% (or more) across various sectors, including construction, catering and accommodation, machinery and equipment, tyres

[32] Arndt, C., Davies, Rl, Gabrie,S., Harris, L;, Makrelov, K;, Modise, B., Robinson, S., Simbanegavi, W., van Seventer, D., Anderson, L. 2020. Impact of Covid-19 on the South African Economy: An initial analysis. SA-TIED Working Paper 111. And PWC. 2020. Thinking through the possible Economic consequences of COVID19 for South Africa.

and rubber production, non-metallic minerals and products (cement and concrete), wood and wood products and alcoholic beverages and tobacco;

- large declines in manufacturing output estimated to be 30-60% for sectors such as basic chemicals, fertilizers, paints, paper and paper products, textiles and clothing, transport and storage, plus similar contractioins in mining and quarrying, will have knock-on effects for other sectors such as business services, research, rentals, wholesale, retail trade and education services;
- moderate declines of 10-30% are expected for petroleum, plastic, glass, food and non-alcoholic sectors, similarly for real estate, legal and accounting services, while declines of less than 10% are expected for agriculture, forestry and fishing sector, pharmaceuticals, hygiene and cleaning, electricity, gas and water, financial and health services
- Tax revenue and tax collections will be adversely affected with a decrease in collections of R304 billion as estimated by National Treasury for 2021 as import tax, direct taxes on households and enterprises and production taxes fall.

Source: (Arndt et al, 2020)

Actions taken in response to the economic impact of lockdown will determine the effects of COVID-19 and the pace at which the economy of South Africa will be restored. The economic recovery will largely depend on the balance of political forces and the type of economic policies adopted for reconstruction and recovery, and a class war may be detrimental to interest of national good. Based on the estimated impact of COVID-19 the fiscal stimulus package of R500 billion[33] was announced and allocated within the existing economic framework. This allocation included an increased allocation for job protection and creation of R100 billion, R50 billion for social security cash transfers, R21.5 billion for healthcare, R40 billion in wage support from the UIF, R20 billion to municipalities and R70 billion in tax relief. The biggest component of the fiscal stimulus package is the R200 billion credit guarantee scheme which had an uptake of only R10 billion (5%) by July 2020. . The allocated R50 billion for social

[33] South African Government. 2020. President Cyril Ramaphosa: Additional Coronavirus COVID-19 economic and social relief measures.

security and increased welfare subsidy to the most poor and vulnerable includes the COVID 19 R350 grant which is targeting 8 million South Africans. .

There was a clarion call by academics, civil society and several movements[34] for a moratorium on all debt servicing and vociferous opposition to accessing IMF funding announced by the National Treasury. Despite these concerns, the National Treasury intends to borrow US$7 billion from multilateral finance institutions for the pandemic response, and $1 billion has already been approved by the New Development Bank. An additional US$4.2 billion will be borrowed through the IMF's financing facilities[35]. National Treasury's intentions are the strengthening of public finances whilst restoring economic activity and providing the necessary measures to buffer the COVID pandemic shocks. Public consternation about the rising public debt levels and falling revenue, increased national expenditure and the widening budget deficits are used to justify harsh fiscal stabilisation measures. The budget allocated R145 billion for non-interest expenditure increases for a COVID 19 relief package[36], of which only R36 billion was an actual net overall increase rather than a re-allocation from other budgets.

The sub-investment credit ratings seem to have done little to lower the appetite for borrowing as the increased risk premium will certainly increase the costs of borrowing. The further 40% depreciation of the currency and related volatility will put significant pressure on repayments of dollar denominated debt. During the first half of 2020, interest rates declined by 275 due to the collaboration between National Treasury and the SARB. Temporary payment holidays have been introduced by commercial banks for households and businesses, and financial sector regulations have been eased to support credit flow[37]. . The stimulus response will have a lagged effect, but it certainly will have macroeconomic impacts. Our economic modelling in Section 9 will show the economic scenarios that measure the magnitude of output losses and the effects of growth gains from COVID-19 shocks.

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[34] Alexander Winning. 2020. South Africa should not approach IMF for help, ANC and allies say.

[35] National Treasury. 2020. Supplementary Budget.

[36] The allocation of the increased non-interest expenditure is as follows: Support for vulnerable households R40.8 billion, Health R21.5 billion, Municipalities R20 billion, Frontline services R13.6 billion, Basic and Higher education R12.5 billion, SMMEs, business support and job creation R6 billion, Public entities support R5.9 billion, Provincial allocations R19.6 billion

[37] South African Reserve Bank. 2020. Statement of the monetary policy committee.

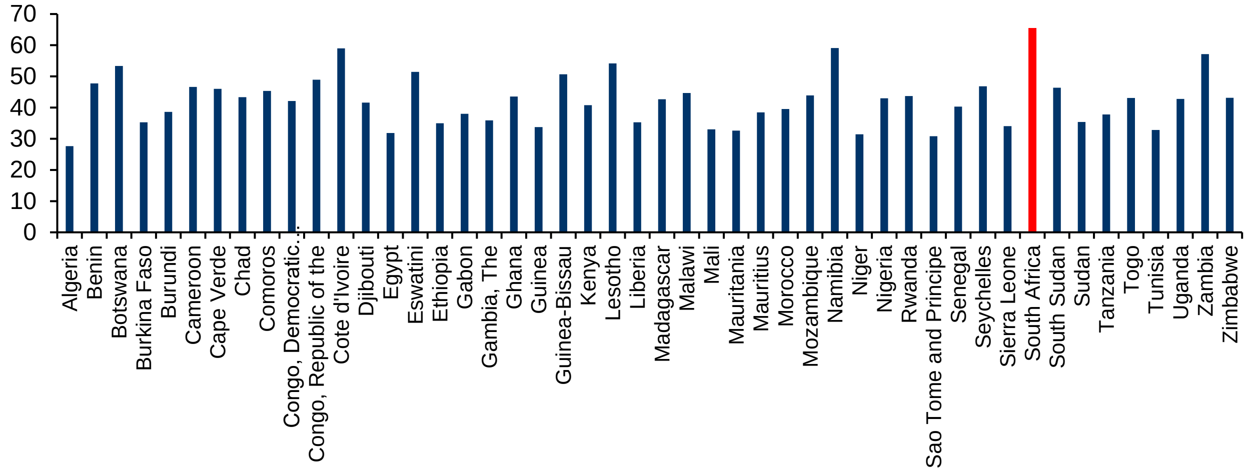
A significant proportion of the state budget will be reprioritised towards the urgent and immediate healthcare needs of state institutions and healthcare facilities. It remains unclear what proportion of resources dedicated to responding to COVID-19 emanates from local manufacturers. This expenditure on healthcare related goods and services may not be sufficient to impact the national economy but it may be crucial in boosting the chemical and equipment manufacturing sub-sectors whose ability to retain jobs and absorb the unemployed is crucial for stabilising manufacturing from further job losses. It is critical that during this time we are careful not to worsen the effects of the pandemic due to ineffective economic policies and failure to co-ordinate policy to prevent further wreckage on the currency, welfare and production of output. Economies during times of disaster employ expansionary fiscal and monetary policy, and this is an opportunity to industrialize and develop the agricultural sector. The reconstruction of the economy from pre-COVID-19 recession and post COVID-19 contractions requires co-ordinated effects towards national reconstruction and the survival of the South African economy using policy instruments outlined in Section 7.

In addition to COVID-19 a challenge is that growth will not yield the intended outcomes in South Africa and has a limited impact due to the high levels of inequality that persist in our country. Evidence from countries with similar growth and poverty rates experienced far greater reductions in poverty levels than Sub Saharan Africa counterparts. The effects of inequality and its pro-poor impact is reduced due to what is known as the low growth to poverty elasticity that Africa, including South Africa suffers. The low elasticity is shown by results on the effect of growth on poverty which show a 1% increase in GDP per annum, which results in a 0.53 percentage point decline in poverty in non-African developing countries. When compared in Africa, the same 1% increase is GDP per annum, the incidence of poverty is reduced by 0.16 percentage points[38]. This suggests any growth strategy that does not look at the restructuring of economic gains in order to reduce inequality will yield little positive outcomes for the large masses of the population. Furthermore, the distributional changes mainly in income distribution that improve growth outcomes elsewhere, are

[38] Clementi, F., Fabiani, M., & Molini. 2019. The Devil is in the detail: growth, inequality and poverty reduction in Africa in the last two decades. *Journal of African Economies*, 28(4), 408-434.

not experienced in South Africa as one proceeds towards the poorer percentiles of the population. Income groups need to benefit proportionally from increases in economic growth for poverty reduction to occur at a rapid pace, but inequality thwarts the proportional distribution of growth gains. Inequality thus minimises the poverty reducing effects of economic growth. Economic strategy that does not propose a growth path that causes a systemic movement of income distribution will not serve South Africa any differently to other post-apartheid policy outcomes.

Figure 6: Distribution of Gini coefficients in Africa



Source: (United Nations University, 2017)
Notes: Data varies between 2010 and 2017

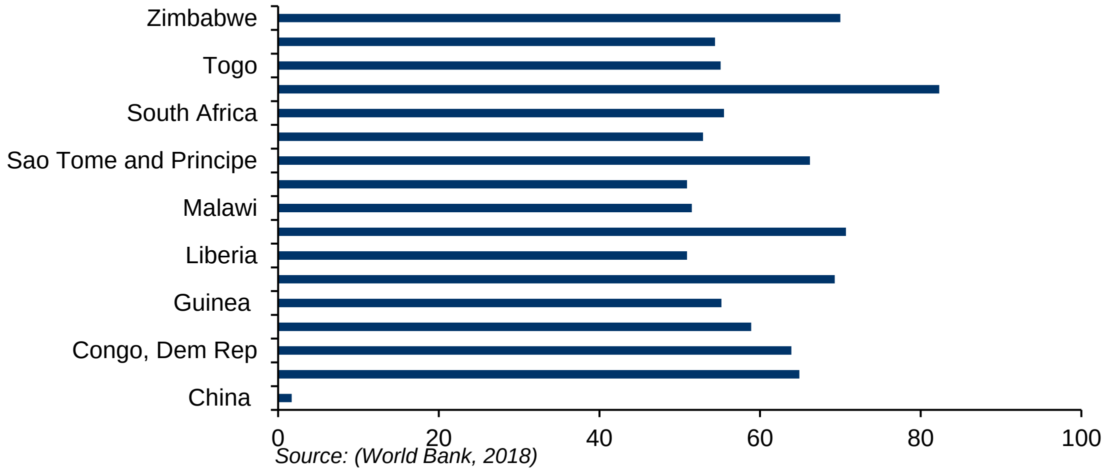
An additional challenge is that the full-scale eradication of poverty has to be one of the main tenets and outcomes of proposed economic strategies. The Chinese were able to reduce poverty to current levels of less than 2% by a sustained and continuous decline of poverty of 2.4 percentage points per annum over three decades. South Africa will need a poverty reduction of target of 2.7 percentage points with a 1 percentage point increase in population growth rates[39]. Sub Saharan Africa poverty is falling at half the required rate. We need to set clear tangible targets that can be measured and monitored.

The question then becomes: what is the required framework for an economy that sustains poverty alleviation? The answer would be clear structural economic transformation, movement towards greater labour productivity and a simultaneous

[39] Frankema, E., van Waijenburg. 2018. Africa Rising? A historical perspective. *African Affairs,* 117 (469), 543-568.

movement of capital and labour into high productivity sectors. The importance of driving labour productive growth is so that all income strata benefit from the gains of productivity and growth equally. The South African growth model is not underpinned by high levels of labour productivity, but rather a movement toward capital intensivity that completely negates the strategy pursued by the Asian tigers we seek to emulate. The historically resource extractive industries coupled with dwindling and stunted manufacturing growth, has meant South Africa remains stuck in the typical African growth path. It is thus no surprise to see the outcomes laid out in the diagnostic assessment. If we continue to repeat the growth model which has not yielded improved incomes, nor driven industrialisation and while enabling capital intensive growth we will manifest the same poor outcomes.

Figure 7: Poverty headcount ratio at national poverty lines (% of population)



Source: (World Bank, 2018)
Notes: Data varies from 2002-2018

The important factor policymakers have to accept is that the outcomes of economic policy have to result in the employment of our youth, the masses of unemployed with an improvement in incomes and productivity. The economic status quo shows us that growth has occurred as a result of an expanding services sector. This is contrary to what is necessary for a structurally transformed South African economy. Evidence has shown us that high productivity is derived largely from the manufacturing sector. Furthermore, labour intensivity coupled with exports orientation is also derived from a growing manufacturing sector. According to Bhorat, Steenkamp & Rooney (2018) the Sub Saharan Africa's ability to create employment is severely thwarted by the structure of our economies, and South Africa is not exempt. Despite growing 5 percentage points per annum between 2000 – 2008, the rate at which we have created jobs for the working age population has barely matched the needs. The growth of the working age population has expanded from 443 to 550 million, an increase of 107 million people. However, the economy has only created 73 million jobs, of these only 22% are allocated to the youth between 15-24 years of age. The result is with more than half of the population under the age of 25, a significant proportion are unemployed, leaving us with a continental unemployment level of 60%. South Africa is no better with 61% unemployment, differing from province to province and by level of qualification. The resounding outcome of a failed restructuring and reliance on services sector growth for expansion is that we have a parallel inability to produce jobs in our economy.

For long run economic development and growth, the performance of the manufacturing sector requires focus and intervention. This would be necessary to unlock the growth of the sector and raise the importance and economic contribution of the sub-sector in an effort to change economic outcomes. What is therefore necessary is changing the current productive structure of our economy to enhance structural reform that will have spinoffs for further productive capabilities. Hausman and Hidalgo (2009) argue most African economies suffer low levels of economic complexity, which is the opposite pre-requisite for producing more diverse and complex products. The capabilities of a country enable the production of more complex products and this sets them apart on global product markets. Economic and productive complexity directly influence levels of exports and competitiveness of products in the global markets. The enhancement of the export portfolio and the building of the requisite productive capabilities of a diversified portfolio is what should be prominent in our growth-related policy discussion for policy makers. South Africa must identify industries where there are already productive capabilities that provide opportunities for expansion. The public sector would then support this development agenda by using incentives and subsidies to finance the entry and expansion of the private sector in these sectors for the growth and expansion of the economy, with the solid intent of ensuring a growing manufacturing base. This would be both export orientated and labour intensive, so as to drive growth outcomes that result in job creation, as well as true structural reform which we have not yet seen.

The role of the state in driving development and its importance using both monetary and fiscal policy is understated and not seen as key in the current National Treasury economic strategy. The COVID-19 crisis has forced changes that will result in more interventionist approaches. Before the crisis, there was no clear stimulus provided for in the National Treasury paper which instead emphasized austerity and fiscal consolidation as key tenets of the economic solution. This despite significant evidence proving the economic multiplier effects of cutting state expenditure has negative outcomes. Furthermore, with global growth projected to diminish and further contract and an already low level of private sector led investment, the reduction of state expenditure will further constrain demand and lessen growth.

The current proposed economic strategy does not acknowledge the magnitude of the problem, as it says little about poverty nor inequality. National Treasury's economic strategy that is being implemented will have dire consequences for the economy. The proposed restructuring even if successful will only yield a 2.3 percentage point growth increase at most and contribute an additional 1 million jobs in the next decade. To implement the Treasury project would be irrational in the context of the much greater challenges that need to be faced. This proposal focuses on micro-economic reforms which are necessary to improve competitiveness and reduce government expenditure, but beyond those reforms there is little in the decisive action that needs to be taken if we are to boost growth and restructure the economy in ways that redistribute wealth to reduce poverty and inequality.

Moreover, the National Treasury document does mention regional economic integration, however, this is a key opportunity for promoting how regional and continental trade flows can be vastly improved. Intra-Africa trade is a mere 17 percentage points of total continental trade versus the European Union's 70%, yet there are great gains to strengthening continental linkages[40]. The economic strategy does not give reference to how the economic outcomes we currently possess were derived and the learnings from the failures of the past fiscal and monetary policy positions are merely noted. The replication of failures of the last three decades must surely lead to questions about the policy and underlying economic theory.

It is clear that we need a new approach, premised on a fiscal stimulus which is a prerequisite for growth. This all requires a new model of how the state functions, with focused state co-ordination for greater impact. This must be supported by domestic

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[40] UNCTAD. 2008. Economic development in Africa. Export performance following trade liberalization: Some patterns and policy perspectives.

capital mobilisation and a reduced reliance on external capital markets and financial flows.

5. The Necessary Fundamentals for Long-Term Wellbeing, Social Justice and Sustainability

ENABLERS

- Investment – private, DFIs, pension funds, etc
- Institutions – overview of governance, how corruption of both public and private sectors is the challenge, special case of the SOEs
- Policy - policy processes and how they work and don't work
- Learning – why learning curves matter
- Networks – the importance of networks, both problematic ones and healthy ones

The reality is that South Africa's current economic trajectory is unsustainable; economic growth has deteriorated, unemployment is rising, while poverty and inequality remain relatively high. COVID-19 will further exacerbate the market failures and widen the poverty gaps thus the government needs to urgently address and implement economic reforms that will not only stimulate economic growth but will also promote income equality and ensure that poor households are not left behind during the process of economic transformation.

6.1 South Africa needs a decisive economic strategy with a clear vision on how to generate labour demand whilst stimulating productivity

This requires clear targets that will be used to measure the success of the implementation of that strategy, with a clear process

Poverty reduction in South Africa requires economic growth that creates more job opportunities using labour absorptive sectors and growing high value-added manufacturing. Poverty and inequality reduce the positive effects of economic growth due to the unequal distribution of income and economic benefits. Research from the World Bank accentuates that during an economic boom, incomes of people in the lower quartile of the income distribution spectrum grow at a slower pace than those of people in higher quartiles[41].

Figure here is employment by sector over last two decades [or over ten-year trajectory] – Labour Force survey

6.2. Mechanisms on how the structure of the economy must be changed to enhance productivity, this will translate to growth.

Here we must insert the structural change and contribution by sectors over the last 50 years – data is available.

Countries that improved Human Development Index are those whose share of Manufacturing Value added (MVA) as a % of GDP and % of exports to the world increased

Figure here to display is actual output of primary, secondary and tertiary – with focus on secondary (manufacturing, utilities and construction)

6.3 Value chain and distribution that encourages new economic entrants

Changing monopoly and oligopoly type structures with cottage industry's and small scale manufacturing is key.

[41] The World Bank. 2013. African Pulse: An analysis of issues shaping Africa's economic future.

6.4 Economic transformation with aggressive transfer of factors of production to black South Africans

Access to factors of production such as land, capital and sufficient human capital development to strengthen labour capabilities remains constrained and distributed along historical racial lines.

Land reform and restitution processes have been delayed by the government, which has caused considerable uncertainty and social tension. The rapid response to the finalisation of land redistribution has the potential to assist the government in addressing the deteriorating social issues faced by the country. However, the complexities surrounding the process and sustainability of land redistribution need to take into consideration the impacts associated with industry supply chains and market access, while further examining to what extent beneficiaries will receive state support. Despite the many questions surrounding land redistribution, the key motivating factor is that this will create a more inclusive approach to addressing poverty, unemployment and inequality, which in turn will have a more significant impact on economic growth.

6.5 Optimisation of public goods and ownerships

Coordination of all state entities and arms of the state towards this economic strategy

What is seeks to achieve and the instruments it will use to achieve these have largely been ineffective with poor outcomes in most instances.

There also remains a lack of a clear process on what the different economic interests of the working class, vs owners of capital (the rich) vs the lowest income deciles.

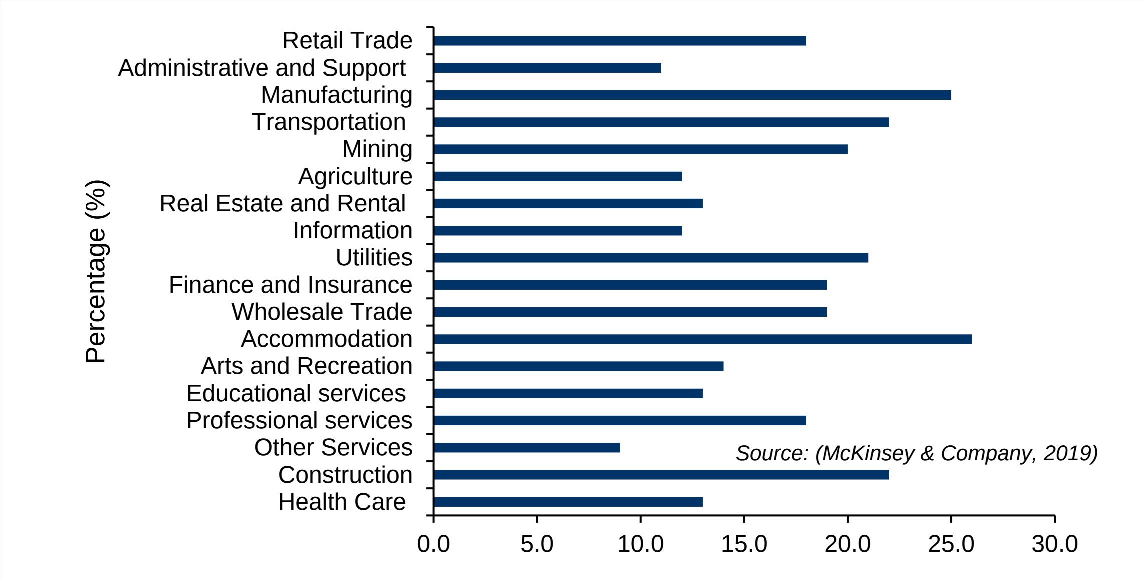
6.6 Digital technology and adoption of technology to advance growth

Technology applied in the production process will affect economic growth, South Africa should have an industrial growth path that is led by labour intensive goods but later replaced by capital intensive goods and production process. Asian economies transitioned and developed capabilities after mastering technology with heavy reliance on technology imports. Moreover, the enhancement of technological innovation and the increase in foreign investor interest in local industries has the potential to stimulate SMME growth and in turn, bolstering overall economic output. Despite the many benefits of automation, it could also potentially suppress labour demand, as automation in production activities along with improved best-practice methodologies for industry efficiency could cause permanent job losses, especially low-skilled jobs. For instance, the finance, insurance, real estate & business services industry (one of South Africa's biggest industries) in 2019 underwent a transition from walk-in banking services to online digital banking. This transition led to the banking industry shedding an approximate 4,722 jobs[42].

Although a study conducted by McKinsey & Company[43] shows that the adoption of automation technologies by South African industries has the potential to boost job creation and productivity, it also warns that automation could lead to significant job displacements, particularly in the manufacturing and retail sectors. The study further elaborates on how automation will cause the demand for employees without matric to fall substantially, while educated (skilled and high skilled) labourers will be deemed more favourable. This shows that despite the many benefits associated with technology, more impoverished citizens are more likely to be excluded from participating and benefiting from increased economic growth. Therefore, technologically infused growth should be complemented by investment in human capital as well as a strategy to protect and develop labour-intensive industries for workers whose skills are not required in high-tech environments.

Figure 8: Automation Adoption by 2030

[42] Mail & Guardian. 2019. Swings and roundabouts for jobs in banks.
[43] McKinsey & Company. 2019. The future of work in South Africa: Digitisation, productivity and job creation.



6.7 All South Africans working

Self-sufficiency vs dependency.

Human dignity and the full potential of all people realised and utilised.

South Africa is becoming a society where individuals take responsibility for themselves and and their families, while redistribution is realised via cash transfers and social programs organised by state institutions. The state has become the sole provider for poor households needs who have become dependent on these handouts. More people receive welfare than the number of people with jobs. The resulting increased welfare costs will be unsustainable if we do not bring the large proportion of South Africans into local economies that promote self-sufficiency, human dignity and the realisation of full human potential.

6.8 Agricultural productivity

The fastest growing economies in the world from 2015 to 2018 were smaller, non-resource intensive African economies who were largely agricultural exporters.

6. Interventions (6 to prioritise)

Towards a Diversified Economy in a Twenty-First Century World

To build a diversified economy that mobilises the abundant natural resources available in an ecologically sustainable way, South African policy makers must rethink the current developmental strategies and introduce policies that promote economic transformation, support labour-intensive growth, restore the environment and create a globally competitive economy. The key success factor will be whether the capabilities and knowledge base of all South Africans is significantly improved. As the productive capabilities of society as a whole increases, it becomes possible to produce sophisticated goods within a diversified economy. Hausmann, Hidalgo, Bustos et al. (2011) refer to this process of improving the productive capabilities of society as building 'economic complexity'. Building on this approach, Bhorat et al. (2019) suggest that "economic growth and development can be thought of as being about the accumulation of productive capabilities". This approach requires government, the private sector, and other stakeholders to collaborate in creating, combining and, ultimately, utilising the diverse productive capabilities within society. In this section of the report, we present interventions that can assist policymakers to enhance and deepen the economic complexity of the South African economy. This, in turn, will result in the much-desired economic diversification that is needed for inclusive sustainable economic growth.

6.1 Industrialisation, Requisite Macro-policy Instruments

Despite industrial strategies and the resolutions adopted at Job and Growth Summits, the industrial sector is still contracting. The merging of the Departments of Trade and Industry (DTI) and Economic Development (EDD) under one Ministry presents an opportunity for driving a co-ordinated approach to a restructured economy. This new Ministry is responsible for the current mix of industrial policies and downstream sector programmes, as well as trade policy and negotiations. Since the merger, both competitiveness instruments and finance mechanisms have been merged. Before the merger, both were previously run by EDD. This means that the Industrial Development Corporation (IDC), Small Enterprise Finance Agency (SEFA) and the National Empowerment Fund (NEF) jointly fall within the same Ministry including the International Trade Administration Commission (ITAC), Competition Commission and the Competition Tribunal.

Each of these institutions make available different incentives for driving industrial policy. These institutions, in turn, have unique policy instruments to stimulate particular industrialisation programmes and projects. There is, however, a widespread via across the Boards and EXCOs of these institutions that economic planning is fragmented and ineffective. We propose that an Industrial Council (IC) gets established that can put in place a coherent industrial planning framework that will knit this array of institutions together into a set of mutually reinforcing institutional entities. The IC would determine industrial policy, drive research and advance the use of appropriate mechanism and policy instruments to advance the newly developed economic strategy.

The South African industrial sector is characterised by the following:

- a centralised (oligopolistic) industrial complex that is effectively owned by a relatively small group of shareholders;
- a labour force that is vulnerable to the inefficiencies of this concentrated operating structure;
- a set of technological disruptions and the ‘global climate emergency" are driving a global transition away from fossil fuels to cleaner, cheaper forms of energy for industrial growth.

Based on these characteristics, we further identified the following challenges within the industrial cluster:

- Traditional industrial corporations have lost substantial market share due to limited investment in new technology within their operations, which has made them less competitive in the global market.
- Inefficiencies within operations have seen organisations like Arcelor Mittal affect the productivity and competitive ability of downstream industries, e.g. foundries. As a result, these organisations ‘look to China’ for wider production options at a better price.

- R&D investment has declined over time, thus making the key industrial sectors increasingly less competitive.
- The high levels of concentration within the industrial sector has created a barrier to entry for new entrants. This is especially critical at the point-of-sale where market access is critical.
- Development finance packages tend to exclude small and medium industrialists from being able to access. This has limited the ability of these smaller industrial organisations to commercialise ideas.
- Labour unions are inadequately mobilised within most industrial clusters which, in turn, means that workers do not have an effective means for bargaining effective alignment between wage demands and productivity improvements via skills development and technology improvement.
- Given the importance of the DTI and DED in supporting industrialisation, it is clear that the Public Finance Management Act (PFMA) is an inappropriate governance framework for the kinds of public-private partnerships that are required if state-enablement of industrialisation is required.
- The current regional economic integration strategy is vague, with unlcear political commitments and mandates when it comes to industrialisation.
- Oligopolies tend to dominate the value chain with respect to the supply of essential household goods and services, thus constraining entry by SMMEs from entering the mass markets (reinforced by exclusive lease agreements at malls and retail locations).

6.1.1 Existing Mechanisms

It is acknowledged that there have been a variety of incentives and measures that have been implemented during the last 26 years ranging from tax concessions, infrastructure support, trade and tariff support, competitiveness and training grants, various production and regional subsidies, R&D support and non-tariff government support. The table below details the existing mechanisms employed, followed by the shortcomings in the section below.

Table 1:Incentives

Tax Concessions	Incentive Details
Income Tax [S12, S37]	Companies are offered tax allowances for industrial policy projects. Both greenfield and brownfield projects qualify as long as they improve energy efficiency, located in an IDZ, target employment creation, train employees and target SMME procurement (10%)
Infrastructure support	
Green Fund Manufacturing Investment Grant (MIG) Critical Infrastructure Programme (CIP) Foreign Investment Grant (FIG)	The MIG was a manufacturing investment offering a grant between 15-30% of the value of machinery, equipment land and buildings and commercial vehicles related costs available between 2008 - 2014. The CIP was a cash grant that covers up to 30% of the costs of qualifying infrastructure to attract investment in manufacturing. The FIG covers costs firms importing machinery and equipment of up to 15% of the value or to a maximum of R10 million.
Enterprise Development support	
MIDP/APDP EIP/MIP BPO NIPP S12I Green Fund	Between 2012 – present, approximately R20 billion is allocated for manufacturing-related tax incentives. As of December 2019, the Jobs Fund had R8.1 billion in grant funding and

Jobs Fund	further R12 billion leveraged from its partners. [44] The DTI increased its allocation towards enterprise development support incentives from R3.3 billion in 2012 to R7 billion in 2015.
Trade and Tariff support	
MIDP DCCS, drawbacks and rebates	In recent years, the most popular incentive was aimed at improving competitiveness and promoting the productivity of vehicle manufacturing in the local markets with the intent to promote the expansion of vehicle exports and encouraging investment inflows. Manufacturers who produce more than 50,000 vehicles locally are allowed to import vehicle components duty-free. This allowance falls under the Automotive Investment Scheme (AIS). Under the scheme, manufacturers linked to productive assets of 50 000 vehicles, also receive a cash grant.
Competitiveness and training grants	
Jobs Fund, SSP, SDL, CF, Manufacturing Competitiveness Enhancement Programme (MCEP)	Existing businesses can apply for production incentives to further capital investment; green technology, improve competitiveness, feasibility studies and the improvement of cluster competitiveness. Production incentives

[44] National Treasury. 2020. The Jobs Fund Newsletter, March 2020.

	range from 7-15%, with local MVA offering higher ranges at 10 – 25% in industrial financing loan facilities for targeted industries. Firms can access up to R50 million subject to MVA limits. Furthermore, production incentives for green technology. Assets worth R5 million receive incentives of up to 70% of cost, those between R30 million and R200 million received 60%, while those above R200 million receive about 50% in incentives.
Regional subsidies	
RIDP, IDZs	
R&D Support	
Innovation Fund, SPII, S11D	In order to promote Research and Development (R&D) activities in South Africa, the Income Tax Act Section 11D enabled tax credits even if intellectual property (IP) resides outside the country. The Act also has no cap and several exclusions to disallow non-R&D related activities.

Source: (DTI, 2020; Newman, nd)

South Africa's existing industrial mechanisms focus on supply-side constraints to restructure the production of the economy in order to deal with increased global competition in the wake of trade liberalisation. The summary of the key programmes occurred at a time when South Africa joined the World Trade Organisation (WTO). Unlike East Asian economies who joined the WTO when the industrial sector was strong enough to benefit from opening up to foreign competition, South Africa's industrial sector remains below potential and, therefore, is severely constrained by foreign competition.

6.1.2 Inadequacies

Trade liberalization has contributed to the weakening of South Africa's industrial capability. Two key examples of are the effects of AGOA on the poultry market and the bilateral trade concessions made with the Chinese textile sector that decimated the South African textile industry. These two examples suggest that trade policy is not used effectively to grow South Africa's Manufacturing Value Added (MVA) per capita. South Africa has a much lower MVA compared to most emerging markets. South Africa's MVA growth is estimated at 2% per annum, much lower than China's 6%, Korea's 6% and India's 5% annual MVA growth[45].

The Jobs Fund was designed to address job creation and respond to the mismatch between the labour market supply and demand, especially in the areas of unemployed work seekers. It is aimed at also fostering partnerships between stakeholders and providing low-cost infrastructure for SMMEs. This includes better shelter and trading facilities for informal enterprises as well as improvements in market access. The fund is perhaps the largest intervention in response to labour market anomalies. However, it focuses only on existing companies whose initiatives create more employment opportunities. A mandatory requirement was matched funding of at least R10 million for each project, rising to higher levels for the different windows and calls for applicants. As of December 2019, the Jobs Fund created 254,618 permanent jobs, including seasonal jobs, as well as job placements. These jobs, however, were supported by R8.1 billion in grant funding and a further R12 billion leveraged from partners[46].

Between March 2011 and January 2018, the DTI spent R61 billion on various incentives to support enterprises, supporting only 14,226 over this period. This translate to roughly R871million per annum, which is nearly not enough to fully develop the country's industrial capacity. Over the same period, incentive approvals resulted in projected investments of R326 billion. Despite these investments, industrialisation

[45] Weiss,J. 2010. The Economics of Industrial Development. ISBN 9780415473729. Published by Routledge. Pages 272-16B/W Illustrations

[46] National Treasury. 2020. The Jobs Fund Newsletter, March 2020.

remains well below its potential, and this is compounded by the fact that the government's expenditure on industrialisation incentives remains relatively low.

SOEs are increasingly failing to contribute to the building of skills and supporting of secondary industries which manufacture the inputs in their production process.

There is a lack of coordination between institutions that are developing innovative technologies and products (CSIR, HSRC and Universities) and institutions that can finance such innovations. The has constrained the export-oriented innovative technologies and products for the global market.

Municipal by-laws are not used to enforce localisation and despite rhetoric to the contract, they do little to provide accessible spaces for local SMMEs within food and household goods markets, which is dominated by oligopolies. A Shoprite Checkers in Butterworth, for example, will extract far more from the local economy than a string of local SMMEs.

Preferential procurement policies remain stand-alone affairs. They are not integrated and co-ordinated in a fashion that supports local industries.

Public policies are ineffective due to their poor design and lengthy government bureaucracy processes. Feedback on business support policies is not well utilised due to the state's inflexibility to make amendments to policies as soon as feedback is received. Furthermore, the response by different government agencies and ministries to policy inadequacies - as well as the implementation of incentives - lacked the appropriate response times due to the government's lengthy bureaucratic processes.

The monitoring of the effectiveness of these programmes was lack in many respects. Whether firms were actually expanding as planned and creating the employment targeted required within budget and on time was not fed back into a well-structured learning loop. Cost-benefit analysis studies on these programmes are scarce, and there are very few public reports on the success of these instruments and programs. Whether or not they increased exports, jobs and competitiveness remains uncertain. Even if this was reliably quantified, it is difficult to ascertain to what extent can these incentives be attributed with the actual outcomes.

6.1.3 Alternative Industrialisation Strategies

Given the inadequacies of current industrialisation policies, we propose the following alternative strategies to address them:

a. Evidence-based industrialisation strategies that comprise of a mix of proven incentives and instruments whose use will have high employment generation but also grow existing and new sub-sectors while developing our industrial capabilities. There is a need for concise and legible planning for a 10 – 20-year trajectory which will be overseen and coordinated by the ministries. It is proposed that an Industrial Council oversee targeted sectors while putting state assets and instruments to optimal use. This Council should incorporate both government and business, providing real-time solutions to constraints and bottlenecks. The effective coordination of productive activities will underpin the success of these initiatives.
b. Economic restructuring should mean that the share of South Africa's MVA contribution to GDP should be doubled. The sectoral composition should show a shift away from primary sector activities towards the production of high value-added goods and processed agricultural products. The target of our economic strategy should be to double manufacturing in order to improve economic prosperity and increase the country's per capita GDP, moving from poor to rich in three decades.
c. South African frontier products and manufactured goods must be driven through the mobilisation of finance and capital for productive investments into differentiated products, particularly those where firms set prices.

Table 2: List of Suggested Frontier Products

Product	Description
Stone Wool	Slag, rock wool, mineral fibre and similar mineral wools
Vehicle Parts	Part and accessories (e.g. bumpers, safety seat belts, gearboxes, drive axles, exhaust pipes, radiators, suspension system)
Pig and Poultry Fat	Pig fat (including lard) and poultry fat
Lifting Machinery	Lifting, handling, loading or unloading machinery (e.g. lifts, escalators, conveyors, hoists, elevators)

Traffic Signals	Signalling, safety or traffic control equipment; for railways, tramways, roads, inland waterways, parking facilities, port installations, airfields
Aldehydes	Aldehydes, whether or not with other oxygen function; cyclic polymers of aldehydes; paraformaldehyde
Other Engines	Engines and motors (e.g. reaction engines, hydraulic power engines, pneumatic power engines)
Rubber Sheets	Plates, sheets, strip, rods and profile shapes, of vulcanised rubber other than hard rubber
Engine Parts	Parts for engines (spark-ignition reciprocating or rotary internal combustion piston engines, diesel or semi-diesel engines)
Vinyl Chloride Polymers	Polymers of vinyl chloride or other halogenated olefins, in primary forms
Large Flat-Rolled Iron	Iron or non-alloy steel; flat-rolled products, width less than 600mm, not clad, plated or coated
Nitrile Compounds	Nitrile-function compounds
Refractory Cements	Refractory cements, mortars, concretes and similar compositions
Fire Extinguishers Preparations	Preparations and charges for fire-extinguishers; charged fire extinguishing
Other Agricultural Machinery	Agricultural, horticultural, forestry, poultry-keeping, bee-keeping machinery; poultry incubators and brooders
Dairy Machinery	Milking machines and dairy machinery
Iron Radiators	Radiators for central heating, not electrically heated and parts thereof, of iron or steel; air heaters
Harvesting Machinery	Harvesting and threshing machinery, straw and fodder balers, grass or hay mowers; machines for

	cleaning, sorting or grading eggs, fruit or other agricultural produce
Large Construction Vehicles	Bulldozers, graders, levellers, scrapers, angledozers, mechanical shovels, excavators, shovel loaders, tamping machines and road rollers, self-propelled
Prints	Engraving, prints and lithographs

Source: Adapted from Bhorat et al. (2018)

d. A multi-pronged approach that also increases the production of non-traded goods and services, with low skill but high labour absorptive workforce in manufacturing and primary sector. It is accepted that there already exists high capital and skills intensive manufacturing sectors; a mixed approach must be adopted.
e. Policy misalignment must be rectified. Current policies tend to under-emphasize downstream production in favour of the upstream industry focus. The processing of steel into manufactured products such as equipment and machinery hold opportunities for job creation. The linkages between agriculture and advanced manufacturing industries hold strong growth potential as primary sector activities require machinery and equipment. Revisiting industrial trade policy (in a way that groups products where there exists the potential to produce domestically), coupled to appropriate developmental tariff regimes and duty-free schedules will be a key dimension of the economic strategy.
f. Government intervention will be required to broaden participation in large brownfield industrial sectors and their respective value chains. Government must restructure policies to widen access to the point of sales within the retail sector. This would ease the barrier to entry faced by smaller businesses. Small scale manufacturing and cottage industries should be expanded to grow employment in rural and peri-urban areas. A targeted 30-40% of employment should stem from such cottage industries. These include bakeries, woodworking, building materials, metalworking, dressmaking, hairdressing and soap making. Thus, developing capabilities of production in a de-centralised operating model is crucial while responding to constraints of rural

manufacturing such as lack of energy, difficulty accessing credit, poor quality infrastructure and lack of demand for small firm products. Thus, the state must focus its efforts on micro-credit and micro-finance as these firms will not access finance from traditional banks and financial institutions. This could include artisanal mining in the industrial minerals drive.

g. The focus must shift to developing a regional production partnership model to leverage strengths within the SADC region, intra-Africa and other global markets. The government should develop a cohesive industrialisation strategy that addresses impediments to trade in SSA countries, export promotion support and trade facilitation to finding new markets. Export finance credit to small firms should be provided and used to gain competitive advantage similar to what most OECD governments have done. Non-trade barriers can limit access to the markets of developed economies. This may require support from state entities to enable quality and safety standard bodies to provide the necessary support to small firms and new entrants.
h. The government should revise and strengthen the commitment to local procurement and sourcing by redeveloping incentive structures for international businesses whose use locally sourced inputs. The DTIC and National Treasury should strengthen their cooperation to ensure that local manufacturing is embedded in the state expenditure framework with clear targets and goals.
i. The government should develop a framework for expanded industrial funding. Existing financing institutions have not adequately addressed market failures. They must provide more targeted support to improve the global competitiveness of local firms. Financing new economic participants in regional and global trade requires broadening the mandate of DFIs to incorporate trade finance or the establishment of an entirely new export-import bank that finances and facilitates trade finance. This may be particularly important for advancing intra-Africa trade and for leveraging new markets from the African Continental Free Trade Area (AfCTA) agreement.
j. State capacity for disbursing funds timeously and in more innovative ways must be improved. Programmes could be devised that take advantage of all incentives across all agencies in order to achieve more impactful blended finance outcomes. It will be necessary to developing a team, nationally and in every province, of trade facilitation experts.

k. South Africa should employ a phased approach whereby high labour-intensive sectors should be further developed using the policy instruments that have already been discussed. Over the long run, however, a more capital-intensive growth path may be needed which targets comparative advantages that enable South Africa to transition into technology-based industrialisation pathway. National firms must be supported by improving their access to technology, and R&D should be used to generate technological rents. A research-driven industrialisation strategy is too risky for the private sector because the returns accrue to society as a whole, not just to the investor. Hence, government must derisk innovations by investing in R&D via entities such as the NRF as a core pillar of its national industrial strategy. Derisking can also take place via SOE investments (directly or via procurement) that support risk-taking firms during the early states of the innovation cycle. Knowledge-driven expansion should be used not only to respond to bottlenecks and shortcomings but it should be the strategic focus of industrial policy. Hence the proposed Industrial Council to coordinate policy, but also to ensure that the existing CSIR explores industrial policy-related R&D. Clear metrics of what proportion of public expenditure will be allocated to R&D as a part of the industrial strategy are required.

I. A key enabler of expanded trade in manufactured goods would be the accreditation bodies and institutions of the state that approve the standard of the goods produced by firms. Various sectors require certification from the South African Bureau of Standards (SABS). Capital and finance are required to ensure that these verification bodies can meet the demand for certification services as the country's export capacity improves.

CASE STUDY: In the Mid 1960s the Norwegians reorganised their existing research institutions such as the Technical industrial research council (NTNF) to establish a collective fund for industrial research. One of these was the Norwegian Defence Research Establishment (FFI) that developed technologies for products like seas detection systems for submarines, telecoms equipment, electronic intelligence, nuclear weapon detection tests. These institutions set the industrial policy using industrial research and establishing sector programmes that were evidence based. Longevity of those leading these institutions was crucial and many of the strategists were drivers of policy and research from 1957 up until 1980s. The research was also used to diffuse gains to all parts of the economy and this was done through fusion and close workings of the Ministry of Industry and the research council which was not isolated as there were direct policy recommendations of scientific infrastructure emanating from research directives across economic and social sectors.

Research Councils supported technological development within small scale primary industries and those included fisheries and agriculture. Bigger industries like construction and shipbuilding were supported with elaborates and companies also informed the research agenda of councils with public resources directed towards company R&D. The commercialization of new technologies was an imperative outcome of the Council. The fund identified its main impediments and responded to those ensuring that strong Norwegian companies were built using domestic resources. A sector was selected with shipbuilding chosen as part of the strategy of developing the large cable organisation and the company Verksted becoming a national champion. The selection of companies was aligned to clusters and up to 284 companies were the main beneficiaries. It must be pointed out that there were national champions that received the majority of the funding, with 24 companies receiving 8% and one company Det Noske Veritas (DnV) receiving 17% of monies distributed. This was clear state led driven industrial process which supported private enterprises.

6.2 Labour Absorptive Strategies

The National Human Resource Development Strategy requires that state institutions ensure that school leavers transition from school to post-schooling opportunities in a way that maximises their potential. This should include improved support for first-time entrants into the labour market. Coordination between agencies in this sector is inadequate. Improved connectivity between these agencies is particularly urgent during this time of continued contraction and in a post COVID-19 economy. Unemployment is at its worst, peaking at 29.1% in the last two quarters of 2019, worsening to 30.1% in the last quarter. Over the years, the services sector has absorbed the masses of South Africa's unskilled labour. A protracted slowdown of the sector could lead to more job losses. It is therefore crucial that the proposed labour absorption strategies must not only address unemployment in general but should also address this issue of unemployment among South Africa's youth.

The Presidential Job Summits began in 1998 with the former President Nelson Mandela addressing then what was considered the biggest problem in South Africa, namely unemployment. This problem remains unresolved. During the last Presidential Summit the current President went further by identifying inequality as the root cause of the problem: "*The structure of the economy, which was built on the extraction of minerals, where ownership and control are highly concentrated, remains largely untransformed. The jobs that have been created over the past few years have not kept pace with the growth of the population or the expansion of the workforce".*[47]

Although labour policy cannot address the structural persistence of inequality, it can address the problem of a mismatch between education/skills development and the world of work, including the national demand for skilled and semi-skilled labour. Policymakers, educational institutions and the Department of Labour have attempted to implement several approaches to address this challenge since 1994, yielding minimal improvements. Moreover, a large portion of learners increasingly prefer less

[47] South African Government. 2018. Address by President Cyril Ramaphosa at the Opening of the Presidential Jobs Summit, Gallagher Convention Centre, Johannesburg

technical subjects with fewer learners enrolling for mathematics, science and other technical subjects (even at technical and vocational training institutions). This has affected the youth's skills capacity and requires a shift if the productive economy is to drive economic reform.

Building a strong national knowledge infrastructure is critical for labour absorptive growth and for improving productivity. Although high tech products can readily be imported, developing technological capabilities and associated knowledge bases would improve South Africa's comparative advantage. However, this takes time and requires a skilled and competent workforce. Countries that supply the global value chain and are critical for the global production network focus on supply-side outflows in the labour market. Human resource development underpinned by improving science and technology is critical for economic transformation. This builds human capital which strengthens the growth of productive activities and capabilities.

A good example of how to do this emerges from the work of Bhorat et. al (2017). Using an "economic complexity' approach that identifies adjacent capabilities, it becomes possible to identify key high potential opportunities ('frontier products') that cross-cut traditional sectors. This means comparing how a percentage change in production for various frontier products results in the highest potential job opportunities.

6.2.1 Existing Mechanisms

The government has implemented several job creation programmes, including the Expanded Public Works Programme (EPWP), the Community Work Programme (CWP) and the Jobs Fund. Public institutions that provide educational opportunities for technical and vocational training are covered in the Technical and Vocational Education and Training (TVET) sector. In recent years, the TVET sector has been the focus of job creation policy due to the crucial role the sector is supposed to play in the provision of critical technical skills. The sector's funding allocation has increased notably since the advent of democracy, in line with the NDP's target of 2.5 million TVET enrolments by 2030. In this section, we focus on SETAs, EPWP and TVET colleges.

Sectoral Education and Training Authorities

In response to the lack of skills and high unemployment, South Africa established Sector Education and Training Authorities (SETAs). Currently, there are 21 SETAs, each providing skills development across various economic sectors. SETAs are tasked with developing the appropriate skills, developing and registering learning programmes and distributing Skills Development Levy (SDL) funds.

The SDL is a mandatory levy imposed to encourage learning and development in South Africa and is determined by an employer's salary bill. The funds are paid to the South African Revenue Services (SARS) and are to be used to develop and improve the skills of employees. The SDL collected by SARS is put in a fund and is then divided between the SETAs and the National Skills Fund (NSF). 80% is distributed to the different SETAs while the remaining 20% is allocated to the NSF. In FY 2018/19 the SETAs were allocated about R17.5 million, 6.9% larger than the previous year's allocation[48].

A total of 142,730 workers were funded for learnerships, bursaries and skill programmes under their respective SETA's, of which 122,023 (85.5%) completed the programmes in FY 2018/19. At the same time, about 180,921 workers were funded for artisanal programmes, and 111,275 (61.5%) workers completed the programme.

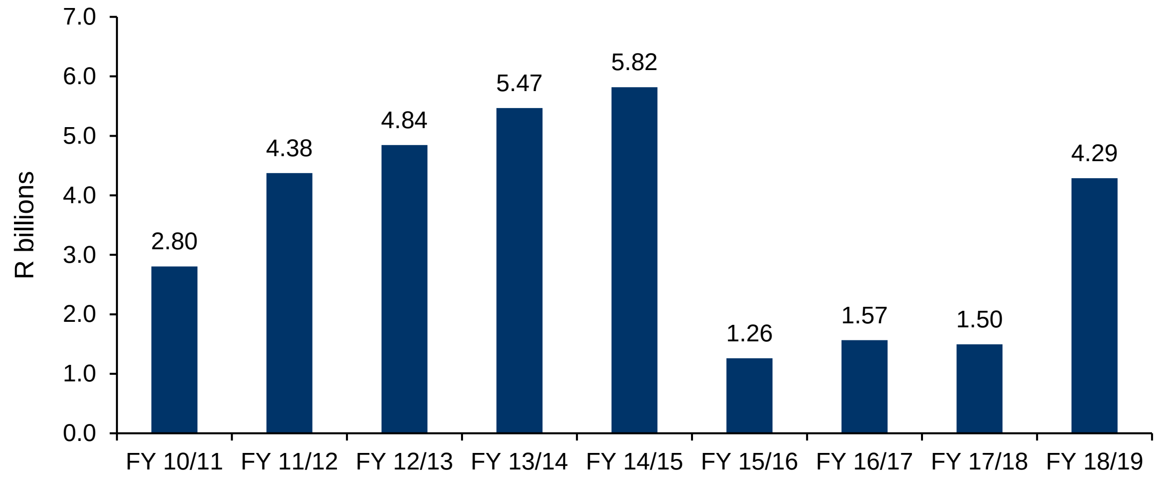
Technical and Vocational Education and Training (TVET) Colleges

Focussed on equipping the unemployed with the necessary job-specific vocational skills and practical work (e.g. internships, on-the-job training, and apprenticeships), the government introduced TVET in 2012. TVET forms part of the Post-School Education and Training cohort of South Africa's education system alongside Universities. Programmes offered by the TVET sector comprise of a mix of the National Certificate Vocational (NCV), occupational and artisan education and N-rated programmes. Following the mergers of 152 technical colleges, there are currently 50 TVET colleges in South Africa. Nevertheless, a significant allocation of capital, both public and private, is directed towards these institutions. In recent years, significant resources have been allocated to refurbish and build new campuses. In FY2018/19, the TVET college system received R1.3 billion for infrastructure maintenance through the Capital Infrastructure and Efficiency Grant (CIEG). Moreover, between FY 2010/11

[48] Department of Education 2018. Annual Report 2018/19.

and FY 2018/19, government expenditure on the TVET colleges amounted to R31.2 billion. Figure 19 below shows the total government expenditure on TVET over the 2011-2018 period.

Figure 19: Government Expenditure on TVET Colleges, FY 2010/11 – FY 2018/19



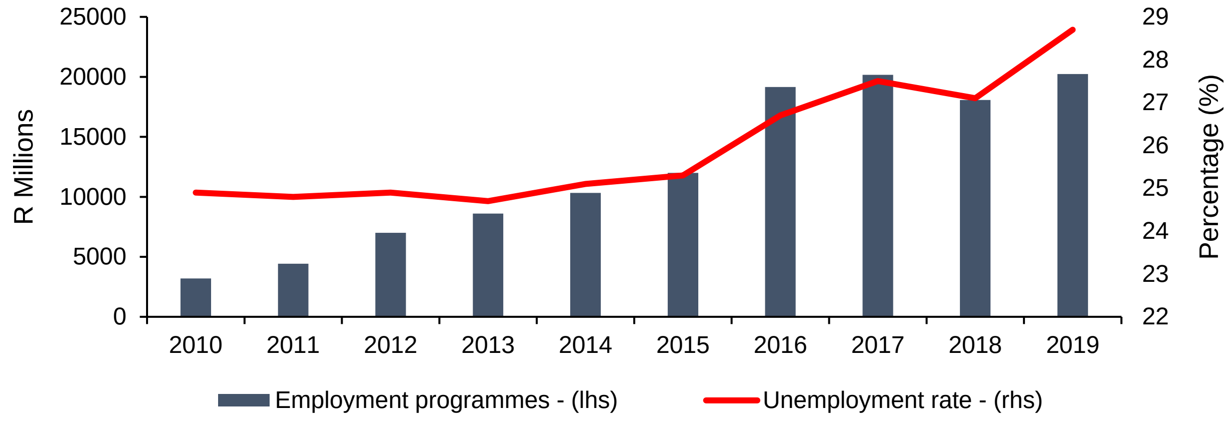
Source: (Department of Higher Education and Training (DHET), 2019)

Expanded Public Works Programmes

According to the FY 2019/20 budget, the government has allocated about R20.75 billion towards employment programmes, including the EPWP, CWP and the Jobs Fund, which is much larger than the R3.1 billion allocated in 2010. However, as Figure 12 shows, the increase in the total allocation to these employment programmes has not reduced South Africa's unemployment rate. This highlights the fact that South Africa's unemployment problem is not due to the lack of funding but is a result of ineffective implementation of interventions.

Figure 90: Overview of funding allocated to employment programmes[49]

[49] Employment programmes includes the Expanded Public Works Programme, the Community Works Programme and the Jobs Fund amongst many.



Source: (National Treasury, 2019)

The Expanded Public Works Programme (EPWP) aims at drawing a significant number of unemployed South Africans into productive work in the manner that will enable them to gain skills and increase their capacity to earn income and develop their community. The EPWP has had a notable impact on job creation for non-skilled and semi-skilled citizens. Since its inception in 2004, EPWP has created 10.9 million work opportunities, of which 66% of EPWP participants were women, 47% were youth, and 1% were people with disabilities[50]. The programme also assists participants to establish their own business or find permanent employment.

6.2.2 Inadequacies

The fundamental flaw in the labour market is "*its inability to facilitate the progression of young people from school to other learning or employment activities".[51]* While South Africa's school attainment at primary school level has improved notably, with completion rates rising from 85% in 2002 to 95% in 2017, secondary school completion rates remain low[52]. The secondary school completion rate increased from about 40% in 2002 to 50.7% in 2017. Moreover, according to the latest General Household Survey (GHS), of the individuals aged 19 – 23 years (i.e. either school-going age or HEI students)), 67% were not attending any educational institution, 7.1% were enrolled at universities, and about 6.4% were enrolled at TVET colleges in 2018[53]. There is a crisis if more than half of learners exiting school fall straight into

[50] Department of Public Works. 2019. EPWP Quarterly Report 1 April – 30 June FY 2019/20.
[51] Kraak, A. 2003. HRD and Joined up policy. Chapter 1 of HSRC (2003)
[52] Department of Basic Education. 2019. A 25 Year Review of progress in the basic education sector, 2019.
[53] Department of Education. 2018. General Household Survey (GHS): Focus on Schooling 2018

unemployment, and others into chronic unemployment. The failure of the education and training institutions to effectively channel first time entrants into economic opportunities remains the biggest shortcoming. Large scale public works initiatives are ineffective at absorbing all these learners.

Despite increasing expenditure in basic education, South Africa still lags in Maths and Science competencies compared to international standards. The Trends in International Mathematics and Science Study (TIMSS) – an assessment of the mathematics and science knowledge of fourth grade and eighth-grade learners around the world – is the best available benchmark to assess the country's quality of maths and science education. In South Africa, the 2015 TIMSS was conducted at grade 5 and grade 9 levels. The findings of this study show that for the grade 9 cohort, South Africa was ranked last out of the 39 participating countries in science and 38th in mathematics[54]. The TIMSS 2015 results also show the same trend for the grade 5 learners, with the country ranked 47th out of the 49 participating countries in the study[55]. This trend should be assessed and dealt with effectively as maths and science are the backbone of innovation and, in turn, production capacity. Nevertheless, South Africa's TIMMS scores in 2015 improved compared to the 2011 version of the study, particularly for the grade 9 learners, reflecting some improvements in the country's maths and science education.

The TVET sector has been unable to increase employment rates from TVET college graduates in part due to poorly designed programs and the poor performance of enrolled students. The HRDCSA (2014) accentuated that the low employment outcomes in the TVET sector are due to the lack of partnerships between industry and the TVET sector and the perception that TVET colleges are institutions of last resort.

There are concerns about the employment opportunities offered by EPWP, with critics suggesting the programme treats the symptom of the problem and not the cause. Nevertheless, even on its own terms the critics points to the following:

- Only 12.4% of EPWP participants found permanent employment, while 47.8% were granted other temporary contracts. Furthermore, only 14% received

[54] Department of Education 2015. TIMSS 2015 – Highlights of Mathematics and Science Achievement of Grade 9 South African Learners

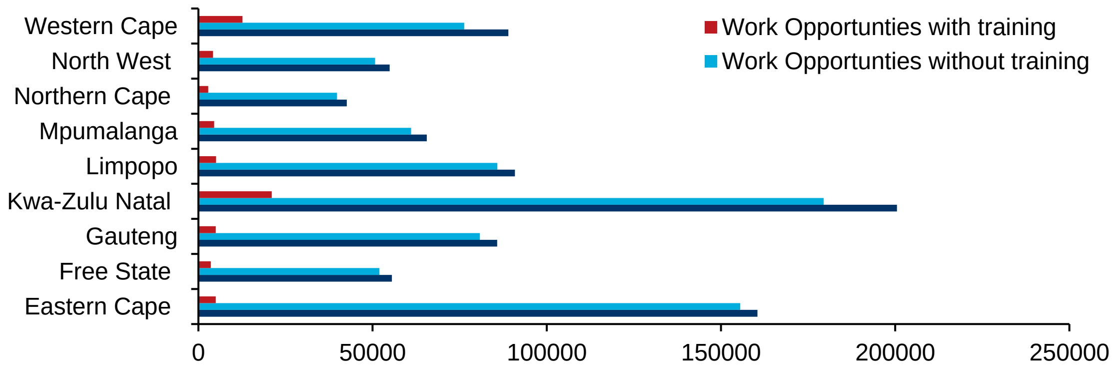
[55] Department of Education 2015. TIMSS 2015 – Highlights of Mathematics and Science Achievement of Grade 9 South African Learners

further training and education during employment[56]. This means almost half of the participants already on short term contracts would be compelled to sign another one at the end of the current one.

- Out of 845 162 work opportunities created by EPWP at the end of the third quarter of phase three, only 42,761 participants had formal training[57].

Figure 21 below shows that across all provinces, the proportion of work opportunities without training is greater than that of working opportunities with training. This indicates that youth who find working opportunities without training are more likely to be absorbed into the informal sector or go back to being unemployed. The lack of skills development within EPWP is alarming, given the high-level entry requirements for decent employment in the labour market. Broadening of employment programmes to encourage industrial related skills and training could encourage displaced youth to create employment opportunities for themselves. The large number of displaced youths from the short-term formal employment will continue driving up the country's already high unemployment rate, and further worsen the vicious cycle of poverty.

Figure 21: Training across the different provinces up to Q3 of FY 2018/19



Source: (Department of Public Works, 2018)

It is vital that the policy and implementation focus must be on equipping the unemployed with the necessary job-specific vocational skills and practical work (e.g. internships, on-the-job training, and apprenticeships) that will assist them in seeking decent employment. South Africa’s artisanal base among previously disadvantaged groups remains poor. An artisanal class could, ideally, be produced through the institutional capacity of the TVET system. Industrialisation requires a parallel human

[56] Department of Public Works. 2019. EPWP Quarterly Report 1 April- 30 June FY 2019/20.
[57] Department of Public Works. 2019. EPWP Quarterly Report 1 April- 30 June FY 2019/20.

resource development strategy to address the need for technical vocational training by young people and the demand for these skills in the labour market. Hence, both the inadequate capacity and poor quality of the country's vocational education are significant bottlenecks to labour absorption.

6.2.3 Alternative Labour Absorption Strategies

Given the inadequacies of current labour absorption policies, we propose the prioritisation of sectors that have the potential to absorb the unemployed. According to Bhorat et al. (2018), the sectors that hold the greatest potential for employment are agro-processing, metal products, plastics, and construction machinery. Further alignment of these high-potential sectors with the programmes offered by public education institutions is necessary to address the projected and current shortages of skilled workers in these sectors.

a. Several sectors have increased production levels, yet the unemployment rate remains high. This suggests that these sectors do not hold the potential to create significant increases in employment; some of these are chemicals, machinery & equipment, agricultural machinery and transport equipment. That said, these sectors play an essential role in the value chain of the economy and currently offer employment to many people. Thus, they should also be supported and stabilised using local procurement with the conditionality of employment generation in state procurement programs.
b. Research shows that capital intensive sectors tend to cut employment as they replace labour with technologies. The analysis further shows a worrying trend of declining employment in the automotive sector, despite the high levels of incentives through the MIDP and APDP subsidies. This warrants a dual focus on both high labour absorptive sectors and those that are non-traded with a domestic concentration, as the latter bolsters domestic distribution.
c. We have previously stated that unemployment adversely affects women and youth, thus we propose that those industries that would absorb a large proportion of women and youth be given priority. Industries that employ greater proportions of women are agro-processing, plastics and chemicals. Using career guidance to raise awareness about opportunities in manufacturing for women, labour legislation to equip workplaces for the employment of women

and ensuring effective sexual harassment policies are in place to mitigate unacceptable behaviour, it is likely that these highly absorptive sectors would offer opportunities for women in the production line.

d. Youth employment in manufacturing is low and has been declining with a 2.7% contraction in the per cent share of employment in manufacturing. Only a few sectors experienced a rise in the share of youth employment[58]. Rubber, machinery and equipment and meat products showed positive growth in youth employed compared to other sub-sectors, the largest being vehicle parts, transport equipment, glass products and chemicals. To increase their absorption in manufacturing, technical qualifications linked to sub-sectors and the completion of secondary school education with mathematics will be requirements.
e. We propose that the military apparatus and SOEs be mobilised to introduce a youth conscription or community service. Besides life skills, the focus would be the development of a black artisanal class with much sought-after skills such as artisans, plumbers, boilermakers, electricians, aircraft engineers, shipbuilders, and engineers.
f. Government should provide unemployed people with livelihood/employment opportunities by using the public employment schemes which, in turn, will reduce pressure on the social welfare systems. This could be a further extension of the EPWP program or the introduction of a grant for community health care workers.
g. The state procurement framework should be revised with certain services returning to more secure full-time employment practices, such as cleaning and security. We propose the banning of outsourcing in certain identified sectors. Some private -sub-sectors promote the casualisation and exploitation of workers by persistently relying on labour brokers. These workers should be employed with full benefits
h. The procurement framework should be revised to promote local context programmes (similar to what is applicable in the Renewable Energy Independent Power Producers Procurement Programme). SOEs have the internal capacity to produce equipment with local manufacturers, which would

[58] Bhorat et al 2017

create significant local jobs. However, procurement bills are not favourable to localisation even though this is a national development priority. Since localisation is deemed a national priority, it requires other factors beyond pricing to be considered in the procurement of goods and services.

i. Higher Education Institutions (HEIs) should be mandated to organise skills-employment matching. Students and learners who exit the training and education sector after being in the university, a TVET or any other higher education institution should be channelled into employment/livelihood activities.

j. Urgent attention must be given to the TVET sector with monitoring of performance indicators such as throughput rates, certification rates, number of artisans, placements of learners and the low performance of learners in engineering and information technology programmes within the NCV. There must be capacity to measure programme output and pass rate. This could enhance performance targets of the sector by ensuring that output meaningfully responds to the strategic role they are envisaged to play. High levels of dropouts and low certification rates must be addressed[59].

6.3 Domestic food production and Rural Development

The radical land reform promised post-apartheid has failed to transform rural livelihoods and historically entrenched agricultural food production value chains. The intent of improving land restitution, with complementary rural and land reform programs which sought to reform the use of productive agricultural land, including securing rights to those in rural areas has not progressed adequately. Contrary to improving rural livelihoods rural areas remain enclaves of inactivity, poverty, high levels of food insecurity despite large tracts of arable land, and high levels of youth unemployment. What must be pointed out is that the significant potential of transforming rural land to cultivating a historic culture of farming and improving food

[59] DNA (2016) reported that for half the colleges average certification rate is below 300.5% This increases the costs per graduate thus improved certification ensures costs are decreased overall. The NCV programme the cost can be reduced from R454 00 to R233 000 per enrolment if throughput rates are increased from the current 10.6% to 30% in NCVs.

production to reduce the incidence hunger poverty and under nutrition prevalent in rural areas still exists. The post-apartheid dream of formal sector jobs in urban areas absorbing the masses of unemployed has not been realised. Rural areas hold the potential for diverse economic opportunities that are non-farm related with diverse income streams a possibility, with the ability to produce food hold higher potential than in urban areas. Opportunities in non-farming related industries possible, but the land in rural areas remains under-utilised and the critical issue of the necessary conditions to improve productivity in rural areas crucial for poverty alleviation and job creation. Several initiatives that sought to provide capital, infrastructure, implements, and land reform have been incapable in securing improved livelihoods with heavy reliance on grants within rural economies.

The rising levels of unemployment and the severity of poverty is widespread in rural areas, this is largely due to the legacy of apartheid which ensured concentration of infrastructure, services and economic activity in the urban areas far from the rural nodes where large proportions of the population reside. It has been well established that the majority of the poor in South Africa reside in rural areas, and a stark majority of households are heavily reliant on the state social protection systems for sustenance. Self-provision in rural areas was the historical norm with most households producing their own food, with low reliance on market purchases but in the post democratic transition this has changed significantly. Economic justice requires that inequality within rural areas and the stark differences in the ownership of the factors of production and productive assets be addressed within any economic strategy. This would enable rural communities to derive benefits from them and to produce local solutions incorporating the rural youth to transform the widespread poverty in rural areas. Subsistence farming, small holder food production must be revisited in the agricultural food value chain. The trickle down economics and hope that the inclusion of rural economies in the current oligopoly controlled food production value chain will require a different set of economic instruments and policy mechanisms, with reviewed institutional support.

Statistics SA (2017) published a report on the poverty trends showing the Eastern Cape and Limpopo experienced the most severe cases, and black African females seeing greater proportions of poverty. The 30.4 million South Africans living in poverty revealed households exhibiting income below the poverty line of R992 per person per month60. The number of South Africans living below the food poverty line was at 13.8 million in 2015, which showed a stark improvement from 1 in 4 to 1 in 3 living with between 2009 and 2015. Even with these improvements it is still unacceptably high. This is an important factor in improving livelihoods as between 60-80% of total household income in low income households is spent on food61. If we are to reach the NDP targets of those living within poverty to zero by 2030, a more radical approach to the economic interventions of those living within the rural areas is required.

South Africa’s Multidimension Poverty Index shows that the poverty measures by province in South Africa by headcount are more intense in the Eastern Cape and Limpopo, followed by North West, Mpumalanga, Kwazulu Natal and the Northern Cape. These provinces have a greater proportion of their population living in rural areas, secondly those who are multidimensionally poor experience the challenges of inadequate infrastructure development, poor access to good quality basic education and health care using government facilities restraining the improvement of living standards. Provinces with economic hubs experience far better poverty outcomes, and the poorer provinces consistently poor with limited economic opportunities. It was thus not surprising when the Eastern Cape and Limpopo showed 95.4% and 93.5% of the elderly receive old age grants with heavy reliance on the social protection in the form of pension and child grants which nationally were more than 17 and 12 million respectively disproportionately skewed to rural economies (Stats SA, 2017). This points to the exclusion of the rural black population in the economy and this underpins the phenomena of rural poverty.

Du Toit (2014) argues that the disconnect between rural urban economic linkages should not be at the forefront of the growth deficit in rural areas, nor the strength of market and infrastructural linkages, but rather greater focus placed on the exclusionary form of development that South Africa has followed. The heavy reliance of rural black populations on wage labour for food and income security was designed by government policy that forced black Africans into cheap labour to advance the industrialisation and mining interests of South Africa, which was designed to benefit only whites. The rural

[60] Statistics South Africa. 2017. Poverty Trends in South Africa. The report calculates an upper bound poverty line of R992 per person per month (pppm) in 2015 prices. The report also applied a Food Poverty Line of R441 pppm
[61] Baiphethi, M. 2009. Contribution of Subsistence farming to food security in SA.

agriculture and African farming was destroyed to ensure that cheap rural labour would service urban mining interests and return to the rural homesteads when no longer needed in urban areas. Rural land was unproductive with the resettlement of many African farmers in mining providing cheap labour, and those who remained in rural areas were largely unemployed migrants, farm workers or black subsistence farmers whose access to the urban economy remained the preserve of the largely white elites. The transformation of the urban economy and the redistribution of the gains of the colonial patterns of profits were still centred and focused on urban and metropolitan areas. A systemic shift is required in this respect.

The South African agricultural sector is dualistic with a highly resourced and capital intensive largely white owned commercial farming versus a low resourced and developing black owned agricultural farming sector. The constraints separating the two should be quelled so as to respond to the national growth imperatives of industrialisation and specialisation within manufacturing. Agricultural productivity is interrelated to the growth of output, this is further multiplied when the linkages to a dynamic agricultural processing sector is developed. Agricultural sector hold the potential to provide inputs to a growing agro-processing sector that will provide not only goods and services, but provide wages and products for workers and households. Thus a stagnating agricultural sector can hold back industrialisation, directly linked to the loss of incomes rising which would also demand a higher quantity of manufactured goods. Some of the challenges facing new entrants are high capital requirements to entry, lack of financial products to meet farmer needs and massive logistical and agricultural support required upon entry, these are significant impediments and remain barriers to entry in the sector. COVID 19 has affected markets with deteriorating markets and the additional constraints posed by the pandemic may cause a deterioration of the gains made of the small number of black farmers who have now entered the agriculture value chain. The integration of primary sector production targeting new entrants will enhance the agricultural participation of black farmers and their participation in the sector, however markets have not successfully broadened access to women and youth, thus market led interventions need to be replaced with well designed and effective state interventions. to access to markets and broadening black farmer participation in markets.

6.3.1 Existing Mechanisms

The post apartheid policy terrain should have seen a more radical approach to the economic integration of the rural population and areas that were systemically excluded from any possibility of improving the economic trajectory of rural households. The draconian apartheid policies and nationalist agenda of both white English and Afrikaner policies ensured that the benefits of economic growth were specifically designed to exclude the benefits of such to the rural citizens, thus the policy frameworks of post-apartheid SA failed to deal with the colonial patterns of development. South Africa's growth in the post 1994 economic transformation did not ensure economic growth of rural areas, but the rather disorganised and narrow economic strategies to improve rural capabilities were left unattended. The economic position of neo-liberalism facilitated to a greater extent the entrance of global capital that enhanced existing white businesses with the remained inability of local black Africans to enter their own economy. This would certainly put pressure and inhibit the redistribution of productive gains and growth within rural areas. As only those who had historical access to the factors of production could gain ground in global markets, furthermore emerging black farmers who did not have the benefits of the protected white agricultural famers over the last 50 years were simply unable to gain traction needed to change market structure.

The effect of the agricultural liberalisation has been the development oligopolies and high levels of commercial sector concentration within farming. Du Toit (2019) reports that agrochemicals, fertilisers, agricultural services and agro-food processing is now dominated by a small number of big farms and food processors. In the last two decades an estimated 20% of farms produce 80% of the food in the retail sector, with the number of farming units dropping from 60 000 to 35 000. Rural farming economies remain excluded from most upward and downstream value chains, with the spatial pattens of agriculture bypassing local markets with regards to investment and production expenditure. The impact of food concentration and value chain concentration has led to forced evictions from commercial farmland, reduction of employment creation, inability of local markets and markets to enter supply chains and a farming economy that is largely delinked from rural nodes and rural supplier inputs[62].

The land restitution programmes have experienced a total number of xx claims, and yy have been settled which has improved the livelihood of xx households. The associated cost of land restitution programme has been at Rxx xxx with the land cost estimated at….. Land claimants are usually given financial compensation with minimal numbers re-entering the economy using the increased access to asset ownership. The transfer of approximately xx ha translated to x% of commercial agricultural land and x% of the total land in South Africa. Food productivity and provision of sustainable livelihoods post-apartheid have not yielded results.

6.3.2 Inadequacies

The patterns of poverty show that the bottom 40% of the population who are largely rural earn only 8.3% of the total national income. This points to the inability to change the income distribution amongst the apartheid spatial pattens and households for those who are not in the urban nodes. Farming and agriculture have experienced a decline in their contribution of employment by sub-sector and this is explained by the formation of large-scale commercial interests. The contribution agriculture can play in employment is depressed due to the type of agricultural model that South Africa has adopted.

Existing agricultural policy points to inability to penetrate the centralised distribution networks that exclude local markets and rural areas, in favour of large-scale commercial farmers. Retailers both domestic and international have let to these supply chains overlooking local producers with the systemic exclusion of smaller farmers and subsistence farmers overlooked and excluded.

This paper does not inform land reform policy however the issue of rural development and agricultural productivity must form part of the economic development strategy of the country. The type of economic policies pertaining to agricultural development has

[62] An estimated 2.3 million farm dwellers displaced with 940 000 eviction in the period 1994 – 2004

been positioned to pro-big business and large-scale industrial farming in opposition to the growth of smallholder farmers whose potential remains under-utilised. The supply networks and value chains have excluded small farmers, mainly black emerging farmers for a predominantly white large-scale commercial farm that has little regard for economic empowerment and worker rights and labour wages.

The rural nodes have no economic activity with the largely “Bantustans” and former homeland reserves enclaves for remittances and pension grants that are received as cash transfers from the state. Farmers inability to access water infrastructure, agricultural support, access to local markets and security of tenure has led to these areas remaining poverty reserves. State capacity in transferring claims in restitution programmes, or the implementation of the process of agricultural development by the ministry has done little for the rural poor, but has created a small class of larger scale African farmers.

The economic policy trajectory has failed to make an impact on the extent of poverty and unemployment of those in the small scale and subsistence agricultural sector, this portion of the population are those who reside in the rural areas with increased reliance on social protection means of grants and old age pension payouts. The upward mobility has largely been in higher income deciles of those in urban areas, with the widening inequality a sign of the high levels of income inequality locally. Evidence reveals that in farm areas whites are 143% better off, in tribal areas 30% better off than black Africans. Coloureds remain 10% better off women facing more exposed to poverty than males[63].

Rural communities could offer a base where people would be able to launch new initiatives that enable income generating activities n such areas. It must be stated that not all economic migrants move to urban areas, and there in fact movement from the urban to rural areas. The development model of highly dense cities and preparation of ghost villages should be questioned as urban nodes have not sufficiently improved the lives of economic migrants. In the absence of employment opportunities unemployment is simply displaced from the rural to urban areas.

[63] Cheteni, P., Khamfula, Y., & Mah, G. 2019. , C., Gender and poverty in South African rural areas.

State intervention has not see the change in the structure of production and boosting of manufactured exports by black farmers, thus the economic strategy should have a targeted process through which new and appropriate instruments that will increase the share of black farmers in agricultural sector output and increase the share of black farmers contribution to exports

6.3.3 Alternative rural development and domestic food production strategies

a. There must be an acceptance that there must be a distinction between economic strategies in the urban versus those in the rural nodes. Though all face poverty, the interventions and approaches for reducing the incidence of poverty of those in rural nodes requires a different approach. People in rural areas remain poor due to the inability to translate asset endowments to income generating products. In addition the lack of resource use within the assets amongst communities is coupled with limited access to product markets. There were winners and losers from apartheid which generated inequalities, these remain in the farming value chain and agricultural processing of goods.
b. The important issue is to have development vision of rural nodes whose development is not dependant on the urban development patterns, but rather even if inter linked experience an independent growth trajectory that will lead to rural population prosperity and the ownership of key economic markets to black South Africans. Secondly the focus on developing food production competencies and capabilities is crucial in both rural and urban nodes.
c. It is proposed that dwellers in the rural areas should be enabled to enter the value chains and distribution networks of food production within their local areas. This requires access to local markets being afforded to local farmers who would be given a portion of the distribution networks from existing markets and economies. A proposed intervention is using the state grants as an enabler to create local markets and use of the vouchers in a payment system to local farmers and distributers. This would enable smallholder farmers and subsistence farmers a ready market, however in the medium term allowing farmers the opportunity to improve their scale and potential to connect to urban and rural value chains.

d. The land reform model should encourage the integration of small and informal farmers into the local value chains and the breaking up of oligopoly style farming models that are managed by global and largely large scale farmers.
e. Provision of cheap credit to small scale farmers that is subsidised by the state is a critical enabler.
f. The instruments and mechanism of land and agrarian reform must benefit the poor and marginalised. The economic patterns show that the well connected and rich or politically elite remain the beneficiaries of asset allocation, resources and even rights to purchase land in certain areas. Francis (2006) outlines the North West and former Bophutatswana as an example where leases that were given to landholders who were largely white were then lobbied by NAMPO to acquire land post 1994, ahead of the local communities. The Geysdorp, Madibogo enabled landholders to purchase land after successful lobbying of the Department of Land Affairs, but the local residents residing in the rural settlements in the province have no such rights over arable land.
g. Churches, civil society and traditional authorities with access to large portions of lands must reorganise themselves using different models and mobilisation of resources. Reliance on the state for significant transformation of the performance of rural agricultural programs is key, but complementary measures that enhance the productive use of land in these areas must be prioritised. Local indigenous knowledge and practises such as “Illima” should be reignited and restructured to complement poverty reduction efforts of government.
h. Several papers have shown that poverty in South Africa is exacerbated in South Africa on women due to labour market failures and discrimination. These market failures point to the need to have poverty reduction strategies that target those largely excluded and on the peripheries on the labour market. South Africa’s patriarchal society is also reflected in the labour market with gender wage gap and worsened levels of poverty by gender, black rural women in particular. In rural areas access to property rights, enforcing equal wages and entry of women in traditionally male sectors is necessary where patriarchal norms persist that lead to generational poverty.
i. If the economy is to tackle the endemic poverty, social reforms that encourage increased reliance on the state which do not change the current distributional regime of assets and income, they will merely make poverty temporarily bearable.

But not change the level of inequality and impoverished levels of those in rural areas, what rural areas need is not increased social safety nets but rather a change in the distribution of assets and linkages to their own economic domains to change the current economic structure of exclusion and dependence, to another of redistribution and production.

j. Improvement of linkages between firms and agricultural sector, with targeted approach for new entrants, namely black farmers who are small scale or larger scale commercial sized farmers

Farmers in the deciduous fruit sector CASE STUDY

Dualistic farming production in SA requires a focused approach to farmers, with targeted i
and medium sized farmers who sill suffer harsh economic consequences due to COVID 1
farmers will not be simply in this 2020 period, but consequences will be experience in sub
sectors such as the deciduous farmers market due to missing this years season. The effe
with some demand coming to a halt leading to produce ordinarily targing export markets c
been: Local market sales seeing depressed fruit market prices, slow movement of excess
continent ground to a halt, fluctuating Rand increasing input costs furthering unsustainabil
season. The DAFF and Rural Development and Land Reform grant and voucher system o
preparing their winter crop is targeted at small holder and commercial farmers whose turn
– R1 million. The Land bank facility is targeted at existing land bank clients whose turnove
million. Due to the conditionality of the farming assistance offered by the state, several far
would not be able to access a portion of the funding due to the timeframes of funding seas

There appears to be no targeted funding mechanisms and initiatives aimed at the sector, t
income, turnover and reduced liquidity of farmers who have bit hit by large losses in the C
impede the ability of farmers in this sector to absorb farmworkers in the next season. Thes
who employ up to 30 people with average turnover of R3 million have suffered devastatin
affecting turnover and labour. Productivity has been severely impacted with the limited lab
number of new trees planted reduced. Nurseries tree orders have been reduced affecting
2021. The additional increased cost of doing business and safety concerns requires small
workers due to restrictions and adherence to strict safety regulations on farms. Downward
most fruit farmers is guaranteed, the extent to which will be determined by how much fruit
was exported, fruit in local markets or storage is currently being sold at low selling prices.
specific interventions that are tailored for each sub-sector. A mix of subsidies, preferential
farming units, emergency funding for small scale farmers, support for the prevention of la
highly labour absorption sub-sector. Emergency funding should look at both the immediat
making access to funding devoid of bureaucratic red tape. Soft loans, bridging finance an
holidays should be offered as effective funding instruments in this regard.

S

6.4 Investments, Domestic Resource Mobilisation & Private Sector Participation

Capital inflows of $5.3 billion into the South African economy resulted in weak and low growth in 2018[64]. This was despite a buoyant recovery after capital inflows more than doubled previous period divestment of $925 million in international capital flows. The robust investment drive initiated by President Ramaphosa set a target of $100 billion over a five year period. However, this will more than likely be further under-mined by the sharp global economic slowdown in 2020. South African Reserve Bank (SARB) figures show that for the year ???? capital inflows have fallen to $3.78 billion, which puts pressure on as investment-led growth strategy that relies heavily on attracting foreign capital.

Rapid capital accumulation plays a vital role in advancing economic growth and improving total country productivity. Although South Africa receives significant allocations of the FDI allocated to Sub-Saharan Africa, the concern is about the sectoral composition of the capital flows. According to IFC (2018), FDI inflows into South Africa are largely concentrated in the natural resources and financial services sectors. This is inconsistent with a commitment to a development pathway that emphasizes the expansion of manufacturing sectors.

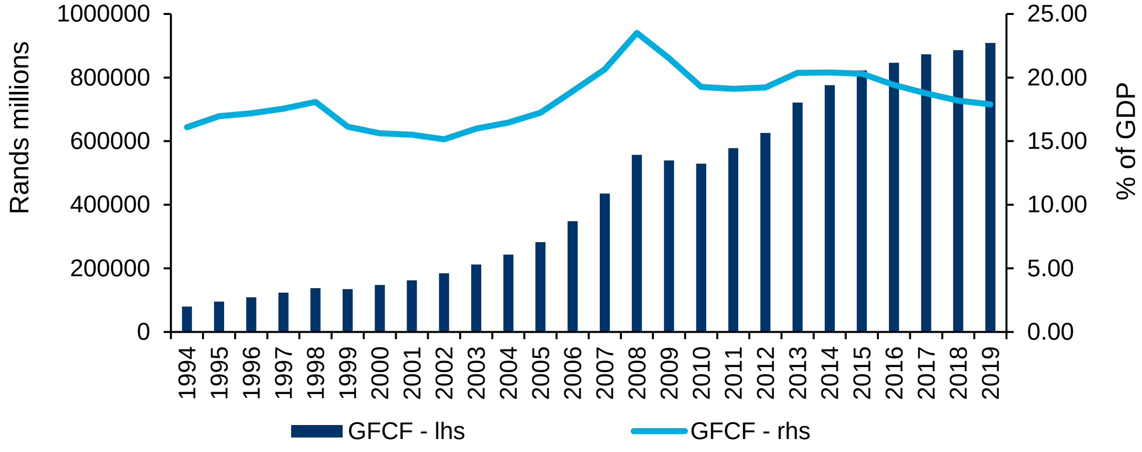
UNCTAD (2019) reported that investment in South Africa is largely focussed on mergers and acquisitions in business services, intra-company transfers and concentrated in the petroleum refining and mining sectors.

The pattern of growth and the sectoral composition of historical FDI inflows have not successfully stimulated economic growth over a prolonged period of time. Despite the fact that South Africa's financial infrastructure favours the efficient facilitation of external inflows, global investment sentiment has been more favourable towards other African economies and emerging markets. South Africa's growth has relied heavily on commodities with at best limited investments in the diversification of productivity.

[64] UNCTAD. 2019. World Investment Report. Washington.

Gross fixed capital formation (GFCF) has remained weak. It has risen from 16.1% of GDP in 1994 to 17.9% of GDP in 2019. GFCF remains well below potential private sector investment in the economy. This effectively means that investment in the real economy is insufficient and domestic capital mobilisation strategies are inadequate. Policies may prioritize the stimulation of reinvestment in the economy, but in practice this is not happening.

Figure 2210: South Africa's Gross Fixed Capital Formation (GFCF)



Source: (Statistics South Africa, 2019)

The Centre for Competition Regulation and Economic Development (CCRED) argue that one of the significant shortfalls of the economy is the high levels of market concentration[65] resulting in relatively low levels of competition between major firms and lower investment levels. . Concentration allows these large firms to earn higher returns and then hoard cash instead of re-invest in firm expansion. The top 50 JSE firms increased cash reserves from R242 billion to R1,4 trillion between 2005 – 2016.

[65] Bosiu, T., Goga, S., Robers, S. 2017. Concentration, profits and investment: Let's focus on the structure of the economy, not "cash hoarding". Centre for Competition Regulation and Economic Development Policy Brief. Industrial Development Think Tank: Policy Briefing Paper 1.

The CCRED policy brief confirms that market dominance by a few firms in critical economic sectors has worsened over the last two decades. It is reported that in the manufacturing sector market concentration by a few dominant firms has increased by 8% to 28%. Market concentration is measured by the top 5 biggest firms in sectors holding over a 70% market share in that sector. This has major implications for for both re-investment and a commitment to tax payments (given that such companies are more likely to engage in tax avoidance via their global linkages).

CCRED also found that institutional investors (both foreign and domenstic) force the companies they invest in to focus on short term returns because these investors tend to be high frequency traders who demand a continuous flow of profits and related dividend extraction. . Institutional investors have significantly increased their assets during the period 2000 – 2016. During the period 1995-2000, institutional investors accounted for on average 4% of JSE-listed shares. However, by 2016 domestic institutional investors accounted for 18% of JSE-listed shares and institutional investors accounted for 42%. Domestic investors have increased their assets 4% to 18% (domestic) and 42% (foreign) institutional investment ownership levels. In a sectoral focus the food production sector instead of expanding through productive capabilities has grown through mergers and acquisitions further entrenching high levels of market concentration.

Thirteen listed food companies controlled the food sector by 2016. SUsing the Hirschman Herfindahl Index (HHI), some firms held over 45% of market share using the HirschmannHerfindahl Index (HHI). Because cartelisation limits competition, consistently high profitability is enable, exceeding profit margins in most emerging market economies. Despite this, reinvestment by these same firms is lower than expected when such conditions prevail.

It is important to understand the drivers and enablers of this reinforcement of market concentration by a few dominating companies. It also is important to understand how the behavious of large firms affects small producers and consumer who suffer the consequences of price inflation. The direct effects of anti-competitive business practices impedes development prospects by raising the barriers to entry for smaller firms.. The biggest losers are consumers who face higher product prices and are offered fewer choices with fewer incentives differentiate between products with respect to and quality. [66].

To achieve rapid economic growth in the next decade, alternative policies must be adopted to catalyse large-scale investments. Domestic savings and pooling of domestic resources is what will bolster capital accumulation for this aggressive growth drive and facilitate the allocation of resources to productive sectors that will drive industrialisation. Capital markets can play a pivotal role in offering liquidity and acting as a buffer in responding to the constraints and after-shocks of the global COVID 19 pandemic. Life insurance companies, pension funds, development finance institutions and the wider financial sector should play a greater role in the provision of capital to drive national growth, especially in times of national economic crisis. A new generation of blended finance vehicles will be required

6.4.1 Existing Mechanisms

Domestic financial assets including non-banking financial assets can act as an economic enabler where international capital flows reverse or slow down. Pension funds in South Africa have experienced compounded annual growth rates of 14% in recent years exceeding the growth rates of similar assets in Australia, United Kingdom and Hong Kong. The world average growth of pension fund assets was 7% in the same period[67]. Domestic pension funds have experienced a massive increase of members, rising to over 15 million members post 2014, with an increase of total assets under management growing to R2.7 trillion in the two decades post democracy. In 2018 the combined assets under management of privately administered, underwritten funds, plus GEPF funds, rose to over R4 trillion. When combined with mutual funds this goes up to R8 trillion. The size of the banking sector has shrunk relative to total

[66] Qaqaya, H. Lipimile, G. 2008. The effects of anti-competitive business practices on developoing countries and their development prospects. United Nations Conference on Trade and Development. UNCTAD/DITC/CLP/2008/2

[67] Moleko, N., Ikhide, S. 2017. Pension funds evolution, reforms and trends in South Africa. International Journal of Economics and Finance Studies, 9 (2).

financial assets with the value of institutional assets rising faster than the value of banking assets.

Pension fund asset growth has led to a variety of positive spill-overs for capital markets, including improving the regulatory framework of the sector, modernisation of infrastructure, increased assets for bond and equities (particularly over the long run) and lowering of transaction costs. The asset allocation is large exposure to domestic equities and bonds, with government securities. A very small component is allocated to alternative investments which include investments in infrastructure as an asset class. There remains potential for use of pension funds for growth and development, ensuring capital is used to drive national priorities. Government regulations and the maintenance of good governance discourages rent seeking and misuse of pension assets. What requires more attention is how pension funds can target their investments in ways that contribute more directly to improved economic growth. The regulatory environment permits pension fund allocations to alternative investments (such as ???). However, there is need for greater understanding of and therefore allocation of funds to unlisted investments, whilst ensuring good corporate governance is maintained.

Minimal attention has been paid to the need to broaden the investment portfolios of institutional investors beyond the traditional set of listed companies and fixed income instruments. With the looming economic crisis and impending fiscal constraints, pension funds should be encouraged within the existing regulatory framework to consider infrastructure asset allocation as an asset class. This would mean capital markets acting as enablers for propelling economic development in two ways: infrastructure investments and aggressive industrialisation.

A new generation of blended finance vehicles are required. They should enable public sector investments (as subordinated debt and/or grant/concessionary funding) to crowd in private sector investments (as senior debt). A good example is the Infrastructure Fund managed by the DBSA that aims to generate R1 trillion in public and private investments.

6.4.2 Inadequacies

The critical question is to understand what is available from South African pension funds to support national development, and how much of this has been mobilised and allocated for playing a catalytic role in the South African economic reform trajectory. Identifying barriers to greater participation of pension funds and ensuring that the performance of this proposed asset class matches or outperforms other asset classes is key. To achieve this, the following issues will need to be addressed.

The maturity and size of the South African pension fund market equal, and often exceeds, the size of many OECD country pension markets. However, when assessing the exposure to alternative investments and to infrastructure via bonds, South African pension funds do not match to these OECD markets. In light of South Africa's massive development challenges and infrastructure backlogs, the allocation of capital by South African pension funds is mismatched with this reality. Major pension funds like OMERS (Canada), Australian Super (Australia), ABP (Netherlands), USS (UK) have targeted asset allocations of 47%, 30%, 25% and 26% respectively of their total investments for infrastructure investments[68]. The GEPF, which is comparable in total assets under management, allocates the lowest amount into alternative investments by targeting only 5% of their total portfolio for infrastructure investments. GEPF has the lowest percentage of actual investments infrastructure amongst those listed in Table 1.

Table 1: Infrastructure investments as % of total assets

			Infrastructure investment % of total assets			
Name of Fund	Country	Total AuM USD million	Unlisted equity	Listed equity	Fixed income	Total
CPPIB	Canada	136,039	6.0	0.8	Na	6.8
PFZW	Netherlands	131,780	2.0	0.0	0.0	2.0
OTTP	Canada	101,655	7.0	0.7	1.6	9.3
Future fund	Australia	65,825	4.1	Na	Na	4.1
AP-4	Sweden	29,560	0.0	9.0	0.0	9.0

[68] Della Croce, R. 2012. Trends in Large Pension Fund Investment in Infrastructure. OECD Working Papers on Finance, Insurance and Private Pensions No 29. OECD Publishing.

Endesa	Spain	2,082	0.0	8.7	4.7	13.4
Banco BPI	Portugal	3,114	0.0	10.2	10.6	20.8
AFP Horizonte-Col	Peru	7,162	0.3	3.0	7.4	10.7
Superannuation Fund	New Zealand	11,162	3.3	6.6	Na	9.9
Afore Bancome	Mexico	16,430	0.0	2.1	0.5	2.6
Australian Super	Australia	33,800	11.5	0.2	0.1	11.8
OMERS	Canada	52,385	15.5	0.0	0.0	15.5
Previ	Brazil	88,847	0.0	13.5	Na	13.5
GEPF	South Africa	138,572	0.1	Na	0.2	0.3

Source: Della Croce (2010)

South Africa's pension funds within the existing regulatory framework could potentially invest up to 10% of their funds in the infrastructure asset class and enterprise development facilities that would support the national growth agenda more aggressively. Development Finance Institutions (DFIs) whose mandate is financing targeted sectors of economy would act as the bridge to catalyze national investments and be capitalised using domestic capital inflows. The DBSA and NEF could advance the diversification of the pension fund portfolio.

Financial intermediaries and the state do not focus on pension funds as source of capital. Other than the Infrastructure Fund, there exists no coordinated response by the government to reconsider the financing of infrastructure and industrialisation initiatives. Like many other developing countries South Africa is competing to attract FDI. Despite our efforts we have not seen significant inflows of FDI into productive sectors. It therefore makes sense that stronger linkages are forged between pension funds and DFIs. It would help if the investment returns of these alternative asset classes are assessed and monitored to help reinforce the case that they are a sound long-term investment.

The sole purpose of pension regulators is to ensure that there is a conducive environment for investments while limiting risky and reckless investments of pension funds. The fears of weak state capacity, poor planning and weak governance of institutions and political meddling hinder FDI and domestic investment inflows into infrastructure. Pension fund regulators and oversight bodies that must now deal with these alternative investments globally cannot be seen to be deviating from well-established obligations.

Infrastructure projects such as toll roads, power distribution and transmission facilities can generate the required returns to attract a range of investors. In order to stimulate changes in investment behaviour, contract law coupled to a strong regulatory capacity for infrastructure development will be required. The South African regulatory regime does not restrict investment. However, governance concerns will have to be addressed, including ensuring there are no restrictions on the ability to collect payments for infrastructure services.

State institutions must drive national development with respect to both infrastructure and industrialisation. In countries such as Canada, USA and Australia, up to 15% of total public pension assets have been invested in infrastructure investments. These investments often involve non-traditional financing mechanisms with significant returns (Harith & Preqin). There is no reason why this will not apply in South Africa.

Inadequate emphasis is placed on recovering illicit financial flows, and this is private sector driven behaviour.

Large corporations have stockpiles of idle capital that would have been instead invested in the real economy to drive sustainable growth.

6.4.3 Alternative Domestic Resource Mobilisation Strategies

Given the inadequacies of current domestic resource mobilisation policies, we propose the following alternative strategies to address them:

a. We propose that pension funds actively pursue targeted allocations in alternative assets, including a separate allocation for an infrastructure asset class. This can be done without prescribed asset allocation with industry discretion. Alternative investments can offer acceptable returns and match other asset classes. Much of the infrastructure finance gap of around R1.5 trillion can be financed by significant investments by the pension and mutual funds. The proposed Infrastructure Fund is a blended finance vehicle being set up for this purpose, and the proposed Green Bond could effectively raise the necessary capital.

b. Trustees of pension funds, as well as institutional investment capital must be educated about the positive benefits of infrastructure investments and alternative investments that catalyse industrialisation. The notion that they do not yield returns or hold greater risk has shown not to be the case across a variety of global contexts. Infrastructure investment can stimulate diversification, protection against inflation and market volatility, whilst offering asset-liability matching for pension funds. Trustees must require that funds target national development priorities through these asset classes.

c. The GEPF, which accounts for between 88-94% of the PIC's total AuM, must lead the market with a balance between efficiency and equity/redistribution. The GEPF benchmarks and investment strategy must reflect this change. If the GEPF requires the PIC to participate in this broader investment vision, this would crowd the other private entities into this asset class. We therefore propose a review of the Investment Policy and Strategy of these institutions, and the instruments through which such assets are allocated. Greater resources must be allocated to the Isibaya Fund, the DBSA's Infrastructure Funds and other funds to initiate and drive a new generation of blended public and private sector investment strategies.

d. Information asymmetries and high transaction costs of negotiating and enforcing infrastructure agreements must be addressed. There is political and project risk associated with infrastructure planning and financing. However regulatory instability, technical and management incapacity, and fragmentation between various tiers of government requires a review of institutional arrangements. In addition, governance concerns over agencies that collect payments and pension funds ability to package viable projects whilst offering acceptable returns to clients must be addressed. These risks do not eliminate normal market and investment risks faced by other asset classes, but if not addressed will remain a barrier to investment.

e. We propose that the government enables debt instruments that will advance industrial capacity, particularly in labour-intensive sectors. In making these investments, policymakers must ensure there is a positive synergy between social outcomes and increases in productive capacity.
f. We call for the reconfiguration of the role of the PIC, Developmental Finance Institutions (DFI), and pension funds (both private and public) in domestic resource mobilisation. This can be achieved be recapitalising the NEF and the other DFIs to drive growth through redistribution and structural reform. To enable the setting higher asset allocation levels in alternative investments, Regulation 28 will have to be reformed. In addition the PIC can finance the building of industrial capacity by strengthening linkages with the NEF, DBSA and IDC whose models for project and development finance can act as a basis for furthering national development goals.
g. Illicit capital flows must be addressed
h. Tax on idle capital to discourage stockpiling of capital by large corporations that do not reinvest into the South African economy.

6.5 Fiscal Stimulus

Fiscal policy plays an important role in stimulating aggregate demand in the South African economy. It is an important determinant of growth. There are a variety of fiscal policy tools that advance growth and the economic outlook should determine the choice of fiscal policy instruments. Historically the South African government has used public finances to drive growth, since the 1960s a negative budget deficit between 1-6% of GDP is reported[69]. In the outer years the deficit has not sufficiently recovered from the post financial crisis shocks and weakened growth. The high levels of inequality, unequal development and stagnant economy crippled with high levels of unemployment has remained a persistent feature of the economy, stubborn even post 1994. Fiscal policy an important tool for redistribution of income and in the elimination of poverty. Expansionary policy has thus seen increasing allocations of government

[69] Roux, A. 2020. Everyone's Guide to the South African Economy.

spending to socio-economic development, welfare spending on social development, health and education and infrastructure spending. Several essential services that are a public good such as national defence, community and municipal services and public order and safety in society that are provided by various ministries and portfolios of government.

The national budget of government is financed by revenue that is sourced from direct and indirect taxes. This makes households considerably different from government as tax revenue is a direct function of the fiscal policies which can be changed. The progressive tax system adopted increases the allocation of tax as your income rises, and this is also an efficient way of reducing inequality. It is argued that tax contributes to levelling the playing field, before taxes and social spending the richest 10% incomes is more than 1000 times bigger than the poorest 10%, at a Gini coefficient of 0.77[70]. The effect of taxation and social spending reduces the gap in incomes to the richest 10% earning 66 times more than the poorest 10%. This improves the Gini coefficient to 0.59. Government expenditure is but one of the tools and instruments used by the state to stimulate economic activity whilst boosting growth.

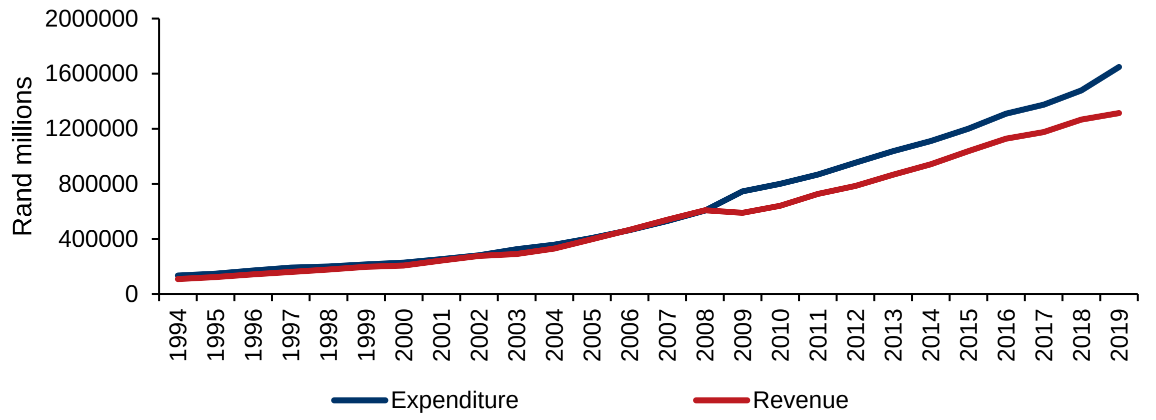
Fiscal injections boost output and consumption in both the long and short run, this helps the recovery of an economy more so in times of crisis. However, deficits induced in times of crisis should be reversed with coordinated fiscal and monetary policy changes once the gains of such fulfil their objectives. The type of expenditure must be growth enhancing. Purported long term gains emanating from public indebtedness in time of crisis rises must be monitored, balancing future tax increases and monetary policy actions should not reverse the growth gains made in the short run. It is argued that growth enhancing expenditure can be reversed by growth retarding tax policies (Gemmell, 2011). This however is dependant on the tax base and tax policies that immediately improve long run growth and aid economic recovery would include the improvement of tax instruments moving the tax base to consumption and immovable property. Lower taxes on low incomes further stimulates demand and improved taxes that reduce income inequality whilst meeting longer term economic objectives key.

[70] World Bank. 2014. South Africa Economic Update: Focus on Fiscal Policy and Redistribution in an Unequal Society. Washington DC. Accessed online https://www.worldbank.org/en/country/southafrica/publication/south-africa-economic-update-fiscal-policy-redistribution-unequal-society

Current COVID 19 responses include additional tax deferrals, payment holidays of up to 90 days, tax postponements and tax incentives.

Figure 23 below shows that since the global financial crisis in 2008/9, government expenditure growth has outpaced revenue accumulation. This has forced the government to turn to external borrowing to fund its widening budget deficit.

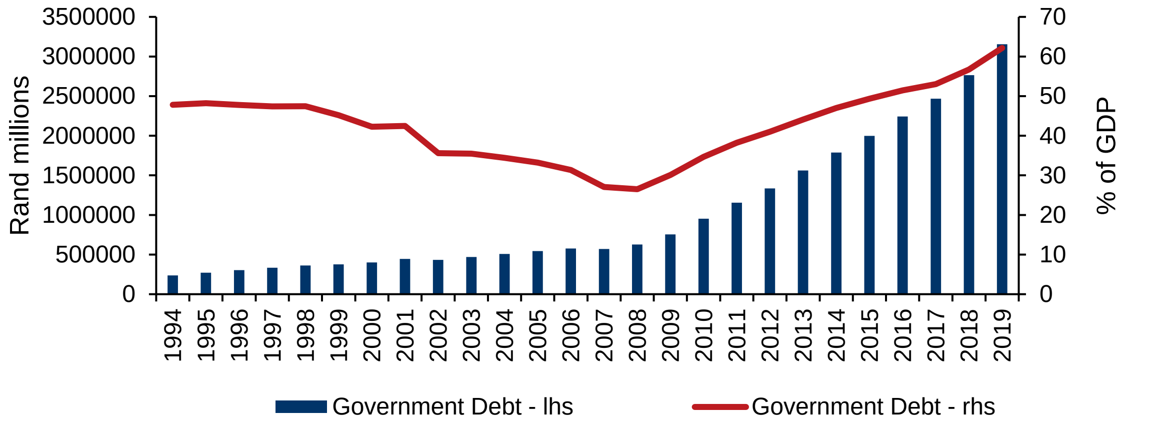
Figure 23: South Africa's Government Expenditure and Revenue



Source: (Statistics South Africa, 2019)

However, considering debt on its own is meaningless. What matters is the debt to GDP ratio. A country can raise debt as long as the economy is growing at rates that make it possible to service the debt. South Africa's debt levels before 2020 may not be high by international standards, but with low growth rates these debt levels are not sustainable with the high debt servicing costs expanding as a share of the fiscus. Figure 24 below shows South Africa's rising debt to GDP ratio, recorded at 62.2% in 2019. There are other ways to fund fiscal needs either than accumulating debt.

Figure 2411: South Africa's Government Debt to GDP Ratio



Source: (Statistics South Africa, 2019)

6.5.1 Existing Mechanism

The current fiscal injection of a proposed R500 billion into the economy to quell the post COVID 19 economic recession will positively impact output and employment. The stimulus package announced in May 2020 and adopted by Parliament in July 2020 has received mixed reviews on the impact of the interventions. There appears to be mixed consensus on the appropriateness of the interventions and more so whether the injections are sufficient to deal with the magnitude of the economic crisis South Africa finds itself in the midst of. South Africa was in an economic crisis before the COVID related economic pandemic effects, suffering two recessions in the last 6 months we were already in a recession. This will be worsened by the COVID shocks and the scale of the shocks has received an estimated 10% of GDP with unclear estimated impact on output and employment. Thus, fiscal stimulus must look at a robust recovery of an already ailing economy. How much will this R36 billion non-interest expenditure boost GDP in the short and long run, with the additional loan guarantee scheme? Evidence is necessary to measure the effects of the fiscal stimulus. Section 8 will provide evidence-based predictions on the different fiscal policy interventions that can be adopted, and the outcomes of current changes in public expenditures in the face of an economic crisis. This existing fiscal injection is factored in within this paper, our evidence will also look at alternatives that will move towards improving recovery and shortening the length of recovery.

Monetary and Fiscal Policy interventions include a 275 basis point cut in interest rates to boost aggregate demand, but additional liquidity programs in 10-year bond yields leading to drops from 12.4% to 9%. The key policy proposal from National Treasury on the back of already weakened fiscal policy measures are the targeting of a primary surplus to strengthen fiscal consolidation in the wake of rising public debt levels.

The composition of the fiscal package is made up of loan guarantees of approximately 4% of GDP, with the remaining R300 billion directed to revenue and expenditure measures[71]. The deterioration of public finances due to the pandemic has led to a revised budget deficit of -14.6% of R709.7 billion. National Treasury argues this is happening in the context of an already weakened fiscal position. The tax shortfalls are estimated at R300.4 billion with the result of the revenue deterioration a higher public debt allocation with debt to GDP rising from 65.6% (2019/20) to 81.8% (2020/21). The contracting of GDP by an estimated -7.2% and tax revenue underperformance elevated in the discourse as the key driver to managing a looming fiscal crisis and unsustainable debt levels. But there is little emphasis on how to boost tax revenue in an ailing economy with stimulus package founded on assumptions of low growth and declining nominal GDP.

Table 2: Main budget non-interest expenditure increases 2020/21

Budget Items	R million	
Support to vulnerable households	40 891	
Health	21 544	
Municipal support	20 034	
Frontline services	13 623	
Basic and higher education	12 541	
SMME and job creation	6 061	
Public entities	5 964	
Land Bank equity	3 000	
Provisional allocation for COVID 19 fiscal relief	19 575	

[71] National Treasury. 2020. Supplementary Budget Review.

Total	145 000	

Source: (National Treasury, 2020)

The allocation of R145 billion is shown in Table 2. Above is immediate expenditure, the additional R45 billion is in the next budget cycle, R70 billion is tax policy measures. The allocation R200 billion in loan guarantee schemes has a low take with an estimated 5% allocated to small businesses.[72] The economic relief efforts offered by the state are also in the form of SMME support through the economic cluster, when lockdown commenced and shutdown limited the operational capacity of most non-essential businesses economic cluster responded with various debt relief schemes from Department of Small Business Development (R200 million), National Empowerment Fund (R300 million), Industrial Development Corporation (R200 million), Tourism Relief Fund (R200 million), these are all directed at formal sector support. Total allocation being R6 billion to support small and informal businesses, and a further R5.9 billion for supporting public entities. The informal sector will be hardest hit but the nature of grants and support not yet to the scale of formal sector support despite that more than 3.6 million South Africans employed in this sector. The Temporary Employment Relief Scheme (TERS) of R40 billion has seen an uptake of R23 billion relieving 4.7 million workers.

Major revisions to the non-interest expenditure show suspended allocations of R100.8 billion that has been adjusted from several departments[73]. This reduction of R100 billion emanates from suspended national departments allocations (R54 billion), suspension of provincial conditional grants (R13.8 billion), Repurposing of provincial equitable share (R20 billion), Suspension of local government grants (R12.6 billion). This leads to a total change of non-interest expenditure of R36 billion. These downward expenditure adjustments would likely offset the repurposing fiscal allocation gains, which are largely non-infrastructure related and form part of the fiscal response to the pandemic. Thus we must assess the government responsiveness in respect to the magnitude of the response, but also the timeliness of the spending. The question

[72] National Treasury. 2020. Supplementary Budget.
[73] Supplementary Budget Review reductions to non-interest spending plans is as follows by economic classification: Transfers and subsidies reduced by R87.6 billion [Provinces and municipalities R46.4, Departmental agencies and accounts R12.6, Higher education institutions R3.2, Public corporations and private enterprises R6.4, Households R17, Non profits R1.7, Foreign govts R109 million]; Current payment reduction of R10.7billion [Goods and services R9.3, Compensation of Employees R1.4]; and Payment for capital assets R2.4 billion

that must be responded to in fiscal stimulus is in the weakening exports scenarios and lower household and business aggregate demand, to what extent will the government boost spending in the face of external shocks? South Africa's heavy reliance on global markets and advanced economies will continue in the short to medium term, however fiscal stimulus going forward should seek to aid us to restructure and re-ignite a new growth path that will boost our ability to recover from the health and economic pandemic.

6.5.2 Inadequacies

Governments including our own need to be commended for taking steps to mitigate and prevent the negative economic impact of COVID – 19. Though exercised in good faith, the provisions of additional welfare for the poor and stimulus packages for business will do little to resolve the structural inequalities that existed before the pandemic. These highly racialized and gendered structural inequalities have been exacerbated by the countries downgrade to sub investment grade (junk status) and the deep economic impact of COVID – 19.

Fiscal and Monetary policy instruments must be used in a coordinated manner to relive pressure on the markets and boost aggregate demand. The South African Reserve Bank (SARB) must follow the lead of developed economies and lower the interest rate aggressively, some developed economies have lowered interest rate levels to 0% to increase consumption in the economy. Our SARB needs to be more aggressive and offer interest free loans to government, or issue government bonds at zero or low rates as an immediate refinance mechanism.

It must be accepted that increased government expenditure is accompanied by either widening deficits which must be financed or recovered later through higher taxes or increased servicing of borrowed debt. The selection of policy instruments must be projected in both the short and long run, with planning and policy responsiveness working in tandem. The complexity of financing government deficits whilst boosting consumption in national economies is usually a short run mechanism which may be replaced by other tax related and lowered expenditure in the long run, but timing is important. The current National Treasury model does not appear to measure the detrimental effect that austerity will have on the already negative growth rate, particularly in a time of global recession. This may further the severity of the shock and lengthen the contracting effect in the South African context. Holding all things constant, had the supplementary budget been announced without COVID 19 what would the implications of the fiscal reprioritisation have been on all the departments and reduction of transfers. The fragility of the South African economy requires an appropriate and measurable fiscal policy response, that targets a higher growth rate than the continued stagnation targeted by National Treasury growth estimates.

The informal sector will be hardest hit but the nature of grants and support not yet to the scale of formal sector support despite that more than 3.6 million South Africans employed in this sector. The existing government support framework inadequately responds to the informal sector and the business support and job creation. The current tax framework and the debt relief and loan guarantee schemes is not targeted at the informal sector, with inadequate support offered through existing support mechanisms. To limit the extent of the pandemic shocks it is recommended that this be strengthened in a developing economy context.

The current suite of fiscal policies does not deliver the kind of economic development that South Africa needs, and there is not much evidence of a reduction in wasteful public expenditure through leakages and public sector inefficiencies. This exacerbates the ineffectiveness of fiscal interventions and lowers the impact of any fiscal stimulus.

The weak fiscal position due to increased debt to GDP ratios, is due to tax underperformance. This a short run decline that would improve in the medium term, yet government has prioritised raising debt from international finance institutions to meet the shortfalls and gap between revenue and expenditure. Section 6.4 has pointed to alternative domestic resource mobilisation strategies that do not hamper economic sovereignty nor subject us to the volatility of global currency fluctuations and the rising costs of borrowings. The increased risk premium on the back of two credit rating downgrades by S&P and Fitch ratings agency will significantly increase the already high allocations of servicing existing government debt. Cheaper financing mechanisms that will have limited negative long run impacts on government economic policy and lower the debt servicing allocation should be prioritised.

The actual increased fiscal allocation is not the reported 10% of GDP, but after the reprioritisation and adjustments, the true fiscal stimulus is ….?

The proposed fiscal consolidation of National Treasury that aims to drive a budget surplus within the next three years, this aims to reduce public expenditure with the aim of reducing debt to GDP ratios may have the alternate effect, due to the harmful effect of reducing growth and not sufficiently taking into account the fiscal multiplier effect could lead to worse than pre-COVID outcomes on unemployment, output due to the short run fiscal multiplier effects. It was found that European economies that implemented austerity underestimated the effect and fiscal consolidation efforts and hysteresis effects post recession[74]. These effects may be permanent and harmful even in the long term, thus timing of fiscal consolidation should not coincide with economic shocks and periods of recession which we are currently in.

The planning cycle of government should include in its planning the projected impact of its interventions of key variables such as poverty, inequality, employment and debt to GDP ratios as a measure of the performance of fiscal and monetary policy interventions. The emphasis on debt to GDP ratio as a measure of the health and performance of the budget and its interventions is insufficient, it should not be stand alone but rather the broad measures of economic health and performance captured in planning and budgetary cycles. All should be given equal weighting and importance, with fiscal and monetary policy responses showing how their instruments lead to improvements in these indices. The elasticity of government expenditure to economic output and impact on the aforementioned variables should form part of fiscal control planning procedures measured and monitored.

In the first quarter of 2020 South Africa's economy contracted for the second consecutive quarter by -2%, after contracting by -1.4% and -0.6% in the previous quarters. This is driven by a contracting manufacturing, mining and quarrying and construction industry, trade, electricity, gas and water. The last two years have seen a growth of 0.8% and 0.2% growth. South Africa's slowdown and collapse of key economic sectors began last year, continues to deteriorate, but with COVID 19 looks to completely meltdown unless decisive action is taken to stave off the unprecedented

[74] Gechert, S., Horn, G., Paetz, C. 2019. Long term effects of Fiscal Stimulus and Austerity in Europe.

downfall. The appropriate countercyclical fiscal policy must be pursued to support targeted aggregate demand from households and enterprises.

6.5.3 Alternative Fiscal Stimulus Strategies

Given the inadequacies of current fiscal policies, we propose the following alternative strategies to address them:

a. The elasticity of government expenditure to economic output and impact on the economic output, poverty levels, inequality and incidence of unemployment, and macro-economic variables including debt to GDP levels should form part of fiscal control planning procedures measured and monitored. Strengthening of planning systems and processes within the State will increase the effectiveness of the response of government.
b. The current Fiscal stimulus package is largely demand side oriented and should seek to not only stimulate aggregate demand but also revive supply side sectors and boost industry and drive competitiveness. We have severely limited supply side policies in a time of crisis, in contrast to East Asian stimulus packages we opted to boost domestic consumption similar to the US and European economies.
c. Monetary policy tools should not be under-estimated in a time of crisis and advancing economic recovery. The case of Asian economies found that quantitative monetary easing and lower interest rates had a larger effect on recovery than increased public expenditure and tax cuts[75]. In addition to inflation targeting, the SARB should target full employment given the crisis of 10 million unemployed South Africans and employ the appropriate tools and policy instruments to target full employment.
d. Decisive fiscal action must be implemented at provincial and district level to boost aggregate demand, with provincial stimulus playing an important role in contributing to local demand in a time of crisis, offering relieve particularly in the face of complete shut down of economic activity due to lockdown.

[75] Hur, S,K and Park, D. 2018. Did Fiscal Stimulus Lift Developing Asia Out of the Global Crisis? An Empirical Investigation.

e. The current weak position of South Africa's fiscal position, worsened by levels of leakages, corruption and inefficiencies cannot be ignored. However this should not be used to advance austerity in the face of an economic crisis whose full effects will be felt in the next two quarters, and these will worsen the severity of the crisis we are in.
f. Lastly reducing capital flight by putting in place capital controls to stabilize current account deficits that emanate largely from the outflow of profits, dividends and interest on current account balance of income. During such times domestic capital should be retained and the slowing down of profits through repatriation must be immediately halted.
g. In addition to inflation targeting, the SARB should target full employment given the crisis of 10 million unemployed South Africans.

h. Fiscal stimulus is required to propel the country towards a diversified economy. It can either be: i) debt-funded (borrowing) or ii) non-debt funded (redirecting existing resources, reducing wasted funds, reprioritisation and restructuring), or iii) an appropriate mix of both.
i. However, weak institutions can compromise fiscal stimulus, so it is crucial to establish special purpose vehicles (SPVs) or to use existing institutions to ring-fence the expenditure.
j. The state has the capacity to create new markets that can develop new funding flows, for example the Infrastructure Fund, the restructuring of the electricity industry.
k. To stimulate investment, the government should ensure that the correct multipliers apply, i.e. pick projects with the greatest socio-economic impacts in the short- and long-term.
l. Innovation is very dependent on public sector investment which is a form of stimulus. Innovation in a country is often facilitated by the research and development (R&D) activities of higher institutions of learning, plus well-targeted public sector investments/guarantees during the early phases of the innovation cycle (e.g. the sovereign guarantees for renewable energy projects that launched the REIPPPP).
m. Fiscal stimulus should be on focused specific sectors, e.g. energy.

n. Fiscal stimulus should not only be focused on the growth multiplier, but it must also focus on poverty alleviation as growth with no poverty reduction results in increased inequality.
o. The government should use non-debt fiscal stimulus interventions, including redirecting the investments of the PIC and DFIs, zero-rating certain items, increasing grants, and restructuring the tax system (addressing the inefficiencies in the tax system and higher taxes for the top 1%).

6.6 State Capacity

The Constitution defines the post-1994 South African state as a 'developmental state'. The developmental state depends on two fundamental pillars:

- 'cooperative governance', which refers primarily to the cooperative relations between government departments and the three 'tiers' of government; and
- 'participatory governance', which refers primarily to the relations between government and non-state actors such as business, civil society and the research and education sectors.

In short, the South African developmental state is a *relational developmental state.*

Published in 2011, Chapter 13 of the National Development Plan Vision 2030 contained the best summary overview to date of state capacity since 1994, and what needed to happen going forward. Needless to say, very few of the recommendations for "building a capable state" were implemented over the six-year period that followed. Indeed, by the end of the Zuma Presidency in early 2018, state capture had effectively hollowed out what state capacity there was by the time the NPC began its work.

To build a capable state it is necessary to focus on two key dimensions: the role of the state in the economy, and the organization of state institutions. The role of state institutions in the economy is largely defined by macro-economic policy: degree of state ownership versus private ownership, debt:GDP ratios which determines capacity to spend, inflation targets which determines interest rates, fiscal priorities, exchange rates and roles of key institutions like the SARB, SOEs and National Treasury. Chapter 13 does not focus on the *role* of state institutions. Instead, it lays out a clear diagnosis of the organizational problems and what needed to happen to build the state's *organizational* capacities. This distinction is important, because enhancing the role of state institutions as proposed in this report will be pointless if the organizational capacity of the state continues to deteriorate.

According to the NDP, the poor performance of the public service is caused by the "interplay between a complex set of factors, including tensions in the political-administrative interface, instability of the administrative leadership, skills deficits, the erosion of accountability and authority, poor organizational design, inappropriate staffing and low staff morale". (p.364)

The NDP's vision of a capable state refers explicitly to a state that addresses the twin challenges of poverty and inequality by "playing a transformative and developmental role". In order to be effective and enjoy the confidence of society, the NDP envisages state institutions that are well-coordinated, staffed by "skilled public servants who are committed to the public good and capable of delivering consistently high-quality services for all South Africans."

6.6.1 Existing Mechanisms

The NDP recognises that South Africa is a long way from the "desired end-state" expressed in the vision statement. The NDP recommends five targeted actions to improve state organizational capacity:

- stabilise the political-administrative interface;
- make the public service and local government careers of choice;
- develop technical and specialist professional skills;
- improve relations between the three spheres of government;
- clarify the public interest mandates and improve the governance structures of the state-owned enterprises.

The NDP recommended a number of mechanisms to achieve these targeted actions, none of which have been effectively implemented, namely:

- to stabilise the political-administrative interface, the NDP recommended the strengthening of the Public Service Commission, the creation of an 'administrative head' of the public service to whom Directors-General will report; and reduced political interference in appointing public servants;
- to build public service and local government as a career, the NDP recommended a graduate recruitment scheme, a career pathing strategy for local government, defining experience as a prerequisite for senior posts, and establishing a long-term management training capacity.
- to develop technical and specialist professional skills, the NDP recommends that a much clearer strategy to develop internal technical skills is needed, starting at junior levels, and clear career paths are created for technical specialists.
- to improve relations between the three spheres of government, the NDP recommends improved clarity of roles within a differentiated system to avoid overlap, resource sharing via regionalisation, a coherent set of powers and functions for metros, a narrower and clearer focus for Provincial Governments, and a new problem solving culture.
- to clarify the public interest mandates and improve the governance structures of the state-owned enterprises, the NDP envisages that by 2030 South Africa must be served by "financially sound and well governed SOEs that address the country's developmental objectives". The NDP's recommendations to achieve this were ignored, namely define a clear public interest and developmental mandate, streamline and simplify governance structures, and remedy the capacity constraints. As is now well-known, mandates were hijacked by state capture networks, governance was repurposed for corrupt purposes, and capacity was hollowed out. The economic consequences have been devastating, not simply in terms of looted funds, but also in terms of lost development opportunities.

6.6.2 Inadequacies

A developmental state depends on a continuous flow of innovations, initiated by frontline workers and top leadership within a 'learning organization' framework. Unfortunately, a compliance culture has evolved since 1994 that has all but killed off the developmental state. The compliance culture can be summed up as follows: deeply fearful of making mistakes in a regulatory environment where it is impossible not to make mistakes, officials minimise risk and maximise compliance.

Co-operation across departments/tiers (‘cooperative governance’) and participation with society (‘participatory governance’) becomes a risk worth avoiding when initiatives are not aligned to mandate. If they can just tick the boxes, public servants will feel safe. The result clear: minimal experimentation and innovation. And without innovation, navigating the complexities of development is impossible.

To make matters worse, the response to State Capture since Ramaphosa became president has been increased vigilance, tightening of the screws and more regulations. Protests happen every day, but officials worry more about what the Auditor-General will say, or whether politicians will throw them under the bus, than what the people think of them or want. The result is clear: deepening of the compliance culture and therefore, even more fear and less innovation.

At least during the State Capture years, we had firm evidence that some officials can be innovative: they found ingenious high-risk ways of looting state coffers. Can they now use these skills for good?

We also know of inspiring innovative cross-departmental, inter-governmental, non-corrupt and inclusionary alternatives across many sectors. So, we know officials can do it. The question is, can environments be created that allow officials to take the risk of being innovative for good without the fear of being punished?

In a culture of compliance (reinforced now by an anti-state capture narrative) officials tend to look inwards and upwards: inwards at those who can catch them out, and upwards to those who might not like what they do. Instead of including stretch targets into their KPIs, they do all they can to aim for less than what they are capable of.

Multiply this across the entire public service and you get institutional paralysis. This works for those who see public service as job, not a calling. But it works for no one else.

Underlying institutional paralysis is the technocratic image of the state as a service delivery “machine” rather than an enabler of development. A machine is operated by technical specialists. Consultation with and participation by real people and communities is thus viewed as a barrier. Sustaining development through building trust-based relationships, which requires “soft” skills, is not seen as adding value as it is difficult to measure.

Instead, the core business is “effective service delivery” via a vast array of so-called “mechanisms” — “stock-taking”, “performance dashboards”, “real-time reporting”, “outputs” and “audits”. In this self-perpetuating autocracy, every meeting is an echo-chamber. And management consultants write the meaningless scripts.

Even if you did want inter-departmental or inter-governmental co-operation, auditors prefer functions that do not overlap and budgets that are not pooled. As a result, officials must deliver on their mandates via their silos and segregated budgets. But to address complex system problems with multiple parts, they need at the very least to blend mandates and collaborate with other departments. And so, ironically, we have a developmental state driven by a nominal service-delivery culture, but where actual implementation is deemed to be high risk by the public servants who should feel safe enough to take risks every day.

Where co-operative governance happens, it is hollowed out. People arrive at coordination meetings to defend departmental mandates and protect budgets, not engage.Inter-governmental forums tend to be formalistic, non-discursive, non-learning and non-reflective soulless events. In these fora, a particular mode of leadership is replicated: the “higher” you are, the less you are expected to listen and the more you are expected to speak. As a result, leadership is about positions and the gradual accumulation of ignorance as you rise through the ranks.

> The alternative to all this starts by getting rid of the notion that “the state” exists. It exists only as an idea, a political project. But in reality, it is a vast ramshackle affair comprising a loosely coupled set of institutional assemblages. The best way to “see” the state is to see relationships and then lead accordingly.
>
> If leadership abuses relationships (by, for example, deploying fear or patriarchal power), performance will drop; if relationships are generative, empathetic and enabling, performance will improve. It is as simple as that (albeit easier for women to grasp than it is for men who have been socialised into cultures of control).

6.6.3 Alternative State Capacity Building Strategies

Public servants should discard what they have learnt about strategy which usually means starting with a vision statement and reverse engineering to the present. Instead, they should start with “what is” rather than “what it should be”, that is, start with ‘state-as-reality’ rather than ‘state-as-ideal’. The key questions then become: What do I have at my disposal to work with? Who should I work with to achieve the goal? What is beyond my direct control that I need to influence?

There are two types of governance environments that are misunderstood and conflated.

The first is the necessary ‘top-down’ *Authorising Environment* – this is, of necessity, a ‘command-and-control’ environment: it is regulatory and policy-driven, subject to budgetary and electoral governance cycles, rules-based, upwardly accountable, rigid and compliance-oriented.

The second is the equally necessary ‘bottom-up’ *Mobilising Environment* – in this potentially ‘safe-to-fail’ environment, experimentation, complexity, flexibility and learning are prevalent. It is where institutional agility in required, manifested in partnerships with stakeholders — businesses, social movements, faith institutions and research institutions (although when institutions in this environment fail to connect and communicate, their impact is muted).

In general, the Authorising Environment tries to suppress the Mobilising Environment. The latter then goes into resistance mode, as we have seen in our protests, or takes the government to court; while the former turns inward, hollows out and eventually disconnects from society.

To re-establish a balance between the Authorising and Mobilising Environments, effective partnerships are required. The mistake is to think that each can do what the other must do: the Authorising Environment cannot mobilise society on its own; and the Mobilising Environment needs access to the statutory power and resources of the Authorising Environment.

Both environments need each other, and both need to find better ways to connect and communicate with each other.

The change in mindset proposed here is in reality as paradigm shift from the traditional “good governance” approach to what could be called a “good enough governance” approach. Officials need to become adaptive managers of complex realities that defy linear thinking, planning and measuring. More importantly, public servants need guidance and support as they explore and navigate this kind of adaptive management. This is best illustrated by comparing two strategic management approaches.

The traditional model is a low-risk three-year cycle strategic management approach: year one, investigate; year two, strategise and plan; and year three, budget and implement. This is incredibly slow.

The alternative is very different: start something with others now (which contributes immediately to building trust in action); evaluate early (within a month or two which implies unrestricted information flows); learn-by-doing (which is about creating safe-to-fail spaces); incrementally budgeting as the project expands over time (no “big bangery” thinking); and continuously make small adjustments (which is about responsiveness and agility).

If the starting point is “state-as-reality” then the next logical step is to accept that the state cannot do everything. Instead, a ‘whole-of-society’ approach is needed that rebalances the Authorising and Mobilising Environments. This means enabling officials to empower and work with people, communities and businesses to engage and partner. It is all about enabling: encourage simple protocols rather than complex rules, substitute plain language for public sector acronyms and techno-speak, and be a good listener!

There is a common South African relational way of thinking that says: “Let’s bring all the stakeholders together in a consultative workshop to address the challenge.”

To put it bluntly, this does not work anymore. Higher-level people arrive at the first meeting, but never again. The energy peters out as attendance drops. Discussions seldom result in action or implementation. No-one is assigned to sustain the activities in between meetings. The end-result is a waste of time and money. Dialogue as an end-in-itself does not work.

The alternative is to establish the terms of engagement in advance, including the goal, who needs to be in the room, capacities, seniority (authorising and technical) level. Trust gets built by negotiating the terms of engagement and then collaborating. The result is fear reduction because participants can say: “If I have got to know someone by working with them, I will be prepared to take risks.” In this way, influence and implementation get expanded beyond the limits of the mandate of each and every single department.

Shifting to ‘good enough governance’ and relational modes of innovation-oriented fear reduction will mean cultivating a body of officials with multiple intelligences. This includes emotional intelligence (understanding myself to understand others), social intelligence (understanding how differences catalyse creativity) and relational intelligence (understanding the extent and quality of the relationships between the parts of the system).

For co-operative governance and participatory governance to regain their place as the foundation stones of the developmental state, it will be necessary to bring adaptive management capacities into the governance processes. Traditionally, the core governance competencies were policymaking, regulation, compliance, administration and monitoring/evaluation. What was missing was facilitation, and facilitation is the cornerstone of adaptive management. Adaptive management is a new skill for a time of complexity and transition. Without collaborative leadership, adaptation and learning capabilities, the chances of building a capable developmental state are close to zero.

6.7 Growth through Redistribution

Economic policies of ASGISA, GEAR and the NDP has driven a growth agenda with the hope of redistribution, with an alternate posture of growth needing to occur through redistribution. This paper has seen evidence that after almost three decades of lacklustre growth, that has not yielded redistribution, a new approach of aggressive industrialisation is necessary. Economic transformation in a low growth low employment environment diminishes the likelihood of empowerment of previously disadvantaged individuals and communities.

The extreme concentration of ownership and control in the South African economy - with a small number of large firms dominating most sectors - remains one of the country's greatest economic challenges. Companies with market power stifle broad-based inclusion and participation of new entrants in key sectors. The opening up of the economy to a diversity of participants has not happened while concentration and vertical integration within sectors have increased, reinforced by high barriers to entry weakening and displacing SMMEs and new entrants even in rural areas and townships.

6.7.1 Existing Mechanisms

To redress the systematic exclusion of black South Africans' participation in the economy, the government introduced the Broad-Based Black Economic Empowerment (B-BBEE) Act. B-BBEE is *an "integrated and coherent socio-economic process that directly contributes to the economic transformation of South Africa and brings about significant increases in the numbers of black people that manage, own* *and control the country's economy, as well as significant decreases in income inequalities".*[76] The overarching goal of B-BBEE was to empower previously disadvantaged South Africans through the redistribution of wealth and equitable participation in the economy. The B-BBEE strategy has not had desired results with wealth still in the hands of a select few 25 years after democracy and over 15 years since the strategy was put in place.

South Africa's existing industrial mechanisms focus on supply-side constraints to restructure the production of the economy in order to deal with increased global competition in the wake of trade liberalisation. One of the key programmes under this approach is the National Industrial Participation Programme (NIPP), which was designed to ensure that large foreign purchases by state entities secure offsetting investment and technology transfer obligations in the domestic economy. The implementation of the NIPF is set out in Industrial Policy Action Plans (IPAPs), with the latest being IPAP 2018/19 – 2020/21.

Nevertheless, there is no fiscal stimulus in place to support the growth of SMME's to assist them to enter the market for essential food items such as bread and milk.

6.7.2 Inadequacies

Despite the B-BBEE Act, South Africa remains one of the most unequal societies in the world, with blacks the majority in the poorest quintile. Disappointingly, 25 years after democracy, about 90% of all asset wealth is still in the hands of 10% of the population (most of whom are white). The top 1% of the population experienced the most significant increases in wealth since 1994 compared to all the other groups of society. Moreover, according to data from StatsSA, the average black South African earn less than 20% of white South Africans' average earnings. According to Stats SA (2017) the share of income going to the bottom 40% of income earners was only 8.3% with excessively high share of wealth concentrated with the topic 10% income earners.

Inadequate use of the R800 billion government procurement on goods and services at both national and provincial level to drive transformation. The consolidation of public procurement using the Public Procurement Bill must address the current shortcomings

[76] South Africa's Economic Transformation: A Strategy for Broad-Based Black Economic Empowerment

of using public procurement to improve economic opportunities for previously disadvantaged groups. The existing Preferential Procurement Regulations whose targeted 30% of SMMEs, cooperatives, township, and rural enterprises are unlikely to have fully achieved those outcomes.

Historically skewed patterns of ownership of the factors of productions and ownership of land, capital and entrepreneurial capital (such as processing facilities, buildings, machinery, plant and equipment) have changed minimally.

Municipal by-laws are not used to enforce localisation and to provide space for local SMMEs within food and household goods markets, which is dominated by monopolies and oligopolies. The low levels of locally owned small and micro-enterprises in townships and villages points to poor business regulation for citizens. Thus, local economies, inner cities and township economy should foster South African participation which has been severely neglected.

Serious constraints in value chain participation due to the lack of integration of locally produced goods and barriers to entry mainstream supply chains. This is more so in the retail sectors and agricultural value chains that have a handful of vertically integrated businesses that stifle broad-based inclusion and participation. Competition laws must address the high levels of concentration in the retail sector and break oligopolies to broaden entry of new economic participations.

Existing mechanisms cannot ensure that the economic system incorporates new entrants, and there are no instruments to deregulate and manage cartel-like behaviour. Measures that are currently in place to set aside the allocation of contracts to promote township, rural, local goods owned by women youth and people with disabilities must be used to drive the economic strategy of industrialisation and job creation.

Infrastructure delivery programmes and state procurement have primarily gone to a handful of firms whose use of locally manufactured materials and inputs would have a multiplier effect on inputs for roads, houses, buildings if locally sourced. However, few dominant players control the construction sector and equipment hire for entry into these key sectors is expensive. There exist massive investments into Special Economic Zones (SEZs), Industrial Development Zones (IDZs) and a few incubation hubs in some provinces. Yet these are poorly connected to local businesses, and there remains lack of integration by these IDZs and SEZs using township and rural enterprises for inputs. Poor backward and forward linkages using local firms, even lower use of emerging local firms as firms prefer distributors or suppliers meeting minimum requirements with little effects of structural transformation emanating from the investments[77].

It must be accepted that the various small business initiatives by the DTI and the Department of Small Business Development (DSBD) have remained poorly designed, fragmented and poor co-ordination limits the gains SMMEs would experience.

6.7.3 Alternative Growth Redistribution Strategies

Given the inadequacies of current growth redistribution policies, we propose the following alternative strategies to address them:

a. An empowerment model that realise rural enterprises and township enterprise participation in provincial and national departments' procurement must be established. This must be done in infrastructure projects, inputs for housing projects, the Departments of Education and Correctional Services' feeding and malnutrition programmes and use of Social Development vouchers. The government should allocate resources, either through fiscal stimulus for SMMEs to enter the essential goods market currently dominated by oligopolies. The Public Procurement Bill should advance this model and system to benefit black business owners and new economic entrants.
b. In order to fast track industrialisation, the Public Procurement Bill should enable offtake agreements for businesses that will supply materials and inputs using state procurement. This is for the sole purposes of securing finance and capital for business establishment and expansion for previously disadvantaged individuals.
c. The government must limit the operation of oligopolies in the retail sector within townships, villages, small towns, and the like to ensure the proportion is for local ownership. Local production cannot occur if retailers continue to crowd out local participants using malls and the like. Policies setting the minimum proportion of

[77] Ncane, M. 2017. Exploring Special Economic Zone linkages with emerging local firms, local employment and local skills development: Firm level evidence from Dube Trade Port and Richards Bay Industrial Zone. Master's Thesis. Stellenbosch University.

local shops and goods in malls and retailers must be enacted in order to open up the point of sales within the retail sector. This would ease the barriers to entry faced by smaller businesses. Thus the government should fast-track the amendment of the Competition Act, which intends to introduce measures to address barriers to entry, improved regulation and targeted industrial policies to support rivalry and open up markets.

d. The finalisation of land transfer for both agricultural and manufacturing use bust be fast-tracked. Property ownership, warehousing and access to land for productive use remain an impediment to growing a new class of previously disadvantaged farmers and industrialists.
e. The direct and indirect impacts of SEZs on structural transformation and local industry spillovers must be given more attention by the proposed Research Council and the shareholders of these industrial parks. The integration of emerging local firms into the value chain and industrialisation growth path must be a key outcome that is monitored by SEZs. SEZs in South Africa have been established to drive economic transformation and industrialization, and this inclusive approach requires local firms' capacity to meet quality standards be supported with the state using its finance, subsidy and incubation instruments to link the expectation of SEZ firms and emerging local firms output.
f. The frontier products proposed in Section 7.1 and the alternatives must be prioritized in townships, peri-urban areas and rural towns to stimulate economic activity and drive investment into these underdeveloped and historically overlooked areas for small scale manufacturing and industrialisation. Setting measurable targets with timebound goals should be inculcated with driving transformation.

7 Strategic Proposed Programmes

Here the focus will be on strategic interventions that:

- Realize our normative vision of a wellbeing, socially justice and sustainable economy

- Build the fundamentals over the long term
- Contribute to diversification
- Supported by the enablers

Note: the strategic interventions can be quite wide ranging, e.g. could relate to macro-issues like fiscal policy (Debt:GDP ratio) and/or monetary policy (interest rates), or sectoral interventions like energy or agriculture or manufacturing, but also social issues like GBV and social cohesion. Whatever they are, they must be formulated in terms of the logic of our argument, i.e. consistent with our normative vision, fundamentals building, contributes to diversification, and supported by enablers (which, in turn, may be weak and so cannot be assumed).

The intention of these programmes is to stimulate, stabilise and strengthen the economic framework, thus they can be done in stages.

1. STIMULATE

E.G. of USA Fiscal stimulus post 2009 recession and failed effects of austerity in Portugal and Greece recently.

E.G. of USA Fiscal stimulus post 2009 recession and failed effects of austerity in Portugal and Greece recently.

2. STABILISE

E.G. of China use of interest rate differential to stimulate and change structure of demand

-Also China printed money to reset Banks with China Dev Banks and others

Monetary, Fiscal AND Trade policy must be used to advance NATIONAL economic interests in the context of a globalised economy within which SA is linked and cannot extricate itself.

3. RESTRUCTURE

E.G. of China

8 Scenarios

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