How to Turn Crisis into Opportunity
After Covid-19 – Choices for a Better South African Future
The Brenthurst Foundation
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Introduction

On Tuesday 21 April 2020, President Cyril Ramaphosa, had this to say about South Africa’s fight against the Covid-19 pandemic.

We are resolved not merely to return our economy to where it was before the coronavirus, but to forge a new economy in a new global reality. Our economic strategy going forward will require a new social compact among all role players – business, labour, community and government – to restructure the economy and achieve inclusive growth. Building on the cooperation that is being forged among all social partners during this crisis, we will accelerate the structural reforms required to reduce the cost of doing business, to promote localisation and industrialisation, to overhaul state owned enterprises and to strengthen the informal sector.

The President was announcing the country’s largest-ever emergency spending plan to help South Africans cope with Covid-19 and its effects. Describing it as ‘our economic response to stabilise the economy, address the extreme decline in supply and demand and protect jobs’, Ramaphosa said government would spend some R500 billion – around 10% of GDP. Measures announced included R100 billion for the protection of jobs and for job creation; R40 billion for income support for workers whose employers could not pay them; and a R200 billion loan guarantee scheme in partnership with the major banks. The scheme intrinsically forecast the extent of the loss caused by Covid-19 in identifying the stimulus required.

In the context of a global downturn and significant stress across the African continent, the key question of the President’s plans is how he and his government might ensure the country is in a different, more prosperous place than it was before Covid-19. In the light of the history of state capture, and questions about the efficiency of the state agency, it is wise to ask if this money can be spent both quickly and prudently. To achieve the required efficiencies, the Presidency will have to lead an all-of-government approach.

It is also unclear where the money will be obtained and what this will do to the national balance sheet. The President indicated that R130 billion would come from reprioritisation of the current budget. The rest would come from sources such as the Unemployment Insurance Fund (UIF) and from ‘global partners and international finance institutions’ such as the World Bank, International Monetary Fund, the BRICS New Development Bank and the African Development Bank.

Many of these institutions are offering finance on good terms to fight the pandemic. However, while it might be low interest debt, it is still debt. South Africa will struggle to service it and its other obligations unless the economy is kicked into life to bolster declining government revenue. South Africa’s economy was already in trouble pre-Covid. Before the crisis, its 2020 economic growth was forecast at 0.8%, on the back of 0.7% growth in 2019.1 Under- and un-employment was effectively at 40%, and over 50% of young South Africans were out of work. Business confidence at the start of 2020 was at its lowest level in two decades.

Now the International Monetary Fund (IMF) predicts that South Africa’s economy will decline by as much as –5.8% during 2020, and rebound, all going to expectations, to 4% in 2021. This assumes that the government’s measures to manage the crisis and keep the economy ticking over are effective, and that the delivery of additional resources hits the intended mark. If not, and if revenue collapses along with GDP as spending ramps up, rather than the V-recovery predicted by the IMF, as below, South Africa might instead be looking at a deficit to GDP of as high as 20%. The effect would be compounded by the recurrent nature of the increased grants and other payouts announced by the President, which the government would find difficult to turn off in

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the midst of a recession despite his warning in his speech that ‘the day will come when these measures are no longer needed.’

Fundamentally, without the right sets of policy measures to reset the economy, South Africa could simply create a big increase in public debt with a limited domestic surplus.

The Covid-19 crisis might be a distraction, but it would be a dangerous illusion to assume that it sweeps away the serious problems that existed prior to the pandemic. What is needed is a strategy that faces South Africa’s problems head on and takes the country out of the low-growth, high-unemployment, high-crime, socially discordant dystopia that existed prior to Covid-19.

Yet crises, as Asia has routinely shown in its development path, can with single-minded leadership become the catalysts for much-needed reform.

Such a plan will have to include more than short-term mitigation focused on the extension of child support, food parcels or SMME bailouts – important though it is to confront the hunger and desperation that results from the lockdown. If resources ploughed into various non-essential services are not to be wasted, the plan must map out where and how deep, structural reform should take place to ensure the South African economy not only recovers, but is able to prosper.

This Discussion Paper considers the development of such a plan in three areas:

1. The likely global and continental scenarios, and their impact on South Africa. How might the pandemic change economies, change priorities and alter political trajectories?
2. The challenges that South Africa faces, and levers it has available to ensure a more positive economic future.
3. The recommendations for South Africa to turn this crisis into a high-growth opportunity in a post-Covid-19 world.

Rationalists, Populists and the International Context

The President has avoided populist traps such as raiding pension funds and imposing new taxes on businesses that are already reeling from the lockdown. But what are the prospects of obtaining cheap financing for South Africa, and for growth in a global and continental context?

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The IMF predicts the global economy will contract by 3% in 2020, making the ‘great lockdown the worst recession since the Great Depression, and far worse than the Global Financial Crisis.’

Assuming recovery in 2021, the Fund projects the ‘cumulative loss to global GDP over 2020 and 2021 from the pandemic crisis could be around US$9 trillion, greater than the economies of Japan and Germany combined.’ For the first time since the Great Depression ‘both advanced economies and emerging and developing economies are in recession’. Emerging market in developing economies face additional challenges, they face unprecedented reversals in capital flows, major currency pressures, while at the same time coping with weaker health systems and much lower fiscal space to support their economies.

Much depends on a continuation, indeed a surge, in government spending as part of the recovery. For example, the US – and other wealthy nations – have already committed to increase their deficits and pump up the spending. Amidst dozens of other initiatives, the US has approved a US$2 trillion stimulus. Before the outbreak, the US was expected to have a budget deficit of US$1.1 trillion – equivalent to 4.9% of GDP. After the passing of the stimulus measures, this is expected to be as high as 13%, entering uncharted territory, higher than the deficits incurred even during the years of a war economy.

How this assistance might be funded and where this will be spent presents a crisis of credibility to raise the money and, domestically, to make the political choices in picking the targets for funding and reform. The way to solve a crisis is the same as reform: there is a need to spend well and to keep the cost of financing as low as possible.

The economic impact of Covid-19 on Africa is expected to be large. McKinsey and Company, for example, finds that in the absence of significant fiscal stimulus, Africa will experience a three to eight percentage point cut to GDP growth, up to a US$200 billion decline, notwithstanding the effects of currency devaluations, inflationary pressure, or declining credit ratings, all of which could further worsen the economic outlook.3

As with South Africa, even before Covid-19, the rest of the African continent faced tremendous challenges, on the cusp of seismic demographic change; not just numbers, but also in distribution, as the world’s fastest urbanising region. To develop Africa’s economies at a rate quick enough to keep pace with its rapidly expanding population, projected to double by 2050, the continent requires large injections of foreign and local direct investment.

At current rates, in just 30 years Nigeria’s population will increase to over 400 million, while Tanzania’s, currently 53 million, will grow to the same size as that of Russia at 137 million. Kenya’s will more than double to 95 million, while Uganda will balloon from 43 million to 106 million, according to the United Nations.4 This is, to put things into perspective, the same amount of time as since the fall of the Berlin Wall. Over half of the population of sub-Saharan Africa is today under 25, half of whom are unemployed, accounting for 60% of all the continent’s jobless. This presents a politically explosive scenario.

Finding a way out of this situation was never going to be easy, and Covid-19 just made it much harder. Before the crisis the IMF, for instance, estimated that Africa needed to create nearly 20 million high-value jobs each year just to keep up with the number of young people coming into the African job market.5

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let alone deal with the backlog. Investment is needed for jobs, and jobs are needed for growth and political stability.

Yet, in 2018, FDI flows to Africa barely reached US$50 billion, or just 3.5% of the global total of US$1.3 trillion. Developing Asia on the other hand received US$512 billion in FDI in 2018, close to 40% of the total.\(^6\) Much of this money flows between companies, or their suppliers, which is likely to be negatively affected by Covid-19.

Remittances are now threatened by the Covid-19 pandemic as those paying them find their jobs in jeopardy and banks are off-limits in countries where severe lockdowns have been implemented.

Priorities around donor aid may need to be reconsidered to compensate for losses in remittance support. The use of Money Transfer services by humanitarian agencies means donors are familiar with such services.

Money transfer companies ought to reduce their transaction fees to help maintain its flows as a matter of national priority and business survival.

Data priorities should include diaspora data. Knowing and understanding transnational groups is vital to successfully engaging with them and crafting proper outreach strategies towards diaspora. Who are they, where are they and what do they do?

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\(^6\) See World Bank Development Indicators.

also does not add up, just as it is fallacious, as some propose that increased government spending improves debt to GDP ratios since government would have to increase debt (and the interest burden) to fund spending and improve efficiencies in government to levels hitherto not seen.

It is hard to see the shoots of recovery taking root in an autarkic world, especially for developing nations which are dependent on external borrowing for development and for foreign trade to drive growth. Several once relatively prosperous African countries look shaky, notably among the oil-producers, including Angola, Nigeria, Algeria, and Libya. Big oil projects look set to be further delayed, including in Mozambique. And some regimes that have been dependent on profiting from a premium on oil imports – including Zimbabwe – could run out of cash to pay off their constituents. Even if Africa does not fall to the pandemic, the catastrophe in commodities markets is going to wreak havoc on many African economies.

The IMF has, for instance, announced US$1 trillion in financial firepower to help the global response to Covid-19, US$100 billion of which is earmarked for low-income and emerging countries. Ten-year interest-free loans have already been announced for lower-income countries, including Rwanda, Senegal and Madagascar. The World Bank has also announced that US$160 billion will be available over the next 15 months. The African Development Bank (AfDB) is also providing substantial capital, including via a US$3 billion social bond.

No matter the schadenfreude of some over the globalisation reset, there is a clear connection between the health of global capital and other related flows and the ability of African countries to fund their way out of this crisis. There is, in this regard, a three tier typology of African countries, as portrayed below.

The Big Four (accounting for around 40% of Africa’s external debt); Frontier Debt Markets (19 countries accounting for some 46% of external borrowing), a number of which are highly stressed (Angola and Zambia, where the market has priced in default risks); and the Prudent or Poor grouping (the remaining 33 countries), together holding 14% of Africa’s external debt.  

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8 See, for example, https://theconversation.com/south-africa-is-bent-on-austerity-theres-a-strong-case-that-it-should-change-tack-135977.


10 With gratitude to Dr Greg Smith for this typology.
There are a number of possible threats to this funding scenario. The prospects of global recovery – and the normalisation of globalisation – depends on a range of political factors, centred on the US-China relationship. The possibility of a globalisation reset could be increased by a number of events: The use of an anti-China platform by President Trump during the 2020 election (a near certainty) or a more aggressive response by China, including over Taiwan, in the South China Sea, or in Hong Kong. There is a global, strategic aspect as relations take on a Cold War tone and temperature. Before Covid-19 there was an emerging consensus in the US that China was a strategic threat. Some 60% of Americans now have an unfavourable view of China, the highest number since Pew began polling on the question in 2005.\(^\text{11}\)

Any increase in tensions could dramatically negatively impact on the prospects for recovery. Most countries will, in this regard, have to try to avoid being caught up in a zero-sum geopolitical contest between the US and China and, as best as the situation allows, to keep their options open.

There are other potential global upsides for African countries. They could position themselves to benefit from the moderation of ‘one country risk’ (especially to China) in global supply chains and practice diversification. Despite increased continental trade openness overall, the level of integration in global value chains in Africa is one-third lower than other developing regions. Changing this requires diversification of investment types away from traditional concentration in extractive sectors to more light manufacturing and services which can create opportunities for value addition.

A drive for diversification is all the more imperative in Africa’s commodity-producing states post-Covid-19 as they seek to reduce export vulnerabilities and increase job opportunities.

Africa’s relative performers might also encourage greater aid flows through increased policy differentiation, in particular from the United States, already the largest donor to Africa, contributing US$11.2 billion of US$53 billion annually (with the European Union providing the second-largest volume of some US$7 billion) to ramp up economic growth and job creation.

China has already made headway with its ‘belt and road’ infrastructure initiative across developing and into developed markets. The pandemic has offers it the opportunity to present itself as a humanitarian ally, and Africa could also leverage its position including the treatment of its nationals in China, to improve terms of aid and trade. There have already been calls for Beijing to scrap the US$140 billion in debt that African countries have taken out with China since 2000 as ‘partial compensation to African countries for the impact that the coronavirus is already having on their economies and people.’

Finally, there may be an unexpected upside for Africa from the crisis. Younger populations might well come out of Covid-19 better than older ones. The Global South should, given the right conditions, be somewhere to invest. But much will depend on how Africa survives the crisis, the extent to which it is able to de-risk investments, and how it positions itself to profit from this new order.

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A global reset does not have to be a bad thing for Africa if it learns to own its problems and be their solution. The imperative for African leadership resolve, national resilience and a drive for competitiveness cannot be understated. But it is a situation of move quickly or be damned.

Six Key Global and Continental Insights

1. Global supply diversification will offer manufacturing opportunities to countries that can demonstrate the ability to react quickly and to operate according to Western standards.

2. Aid flows could be reduced as donors focus resources inward. There may also be pressure on aid organisations to reorient spending towards social goods such as healthcare along with a growing humanitarian imperative.

3. Insecure political elites could use the pandemic as cover for increased authoritarianism, the suspension of democratic processes such as elections and increased social control including through electronic surveillance of their population.

4. While advanced economies can currently borrow at exceptionally low interest rates for their stimulus, African countries do not have this luxury. There are only tough choices. Either borrow expensively with foreign currency risk from abroad. Or put further pressure on shallow domestic debt markets, risking a further crowding out of lending to credit-starved private business.

5. African countries will need to devise a suitable financing model for the post-Covid-19 world, whether public or private or both. The fact that the China’s (opaque) annual lending to Africa increased from less than US$1 billion in 2001 to over US$30 billion in 2016, illustrates this need even before Covid-19, as does their consequences for governance.

6. Covid-19 presents a big opportunity for Africa’s reformers, at the same time raising the costs of a failure to diversify.

South African Impacts

Taking our cue from President Ramaphosa’s observation about the imperative to forge a new economy, since 1994, South Africa’s share of global per capita GDP has fallen from 78% in 2008 to 68%, just as government consumption as a share of GDP has risen inexorably by 14% over the last ten years – growing at a rate equal to or greater than GDP growth for eight out of the last 10 years.13

And then there were the falling global ratings, an ever-ratcheting premium on borrowing. This situation is a result of a failure of growth; and that is a result of a clear failure of governance, profligate spending, state capture, looting and corruption which have particularly affected South Africa’s SOEs, and an inability to promote policies that could encourage investment and increase productivity.

Electricity provision – or the failure thereof – has also not helped. While the lower oil price will offer a temporary respite, the government must not lose sight of the importance of reforming the national power producer with minimal political interference.

In the automotive sector, as one illustration, February 2020 saw weak motor vehicle export sales at 30,832 vehicles, a decline of 8.4% compared to 2019.14 The industry, which contributes 6.9% to GDP, recorded an almost 30% decline in domestic vehicle sales for March 2020 compared to the same month
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FACING UP TO GLOBAL REALITIES:
1. The IMF predicts the global economy will contract by 3% in 2020, making the ‘great lockdown the worst recession since the Great Depression, and far worse than the Global Financial Crisis.’
2. Borrowing will increase substantially, with the US already expecting a 13% budget deficit, while the World Bank, IMF and AfDB are making substantial loans available.
3. Globalisation as we know it may be on the decline.

CHINA’S INFLUENCE ON THE AFRICAN CONTINENT COULD GROW
1. The pandemic offers China the opportunity to reset itself as a humanitarian ally, providing assistance with the health crisis which the US and Europe are unwilling or unable to do.
2. China’s influence in Africa will continue to be shaped by its role in providing infrastructure and its dominance in global trade.
3. China’s growing role will be helped by the US’ unwillingness to show leadership.

THE EFFECTS OF THE CRISIS ON THE AFRICAN CONTINENT:
1. There could be an increase in migration flows, exacerbating tensions in Africa and Europe.
2. National budgets will be strained beyond capacity by rising debt servicing costs, and the need to stock up on healthcare equipment.
3. Old financing models and sources of debt will have to be reconsidered.
4. Greater regional integration will be key for fast recovery post-Covid.
5. Some governments will find it hard to resist the opportunity to become police states, mining data for the purpose of political repression.

THIS GLOBAL RESET DOES NOT HAVE TO BE A BAD THING FOR AFRICA 
if it learns to own its problems and be their solution.

However, failure to act or act quickly will be a fatal mistake.
in 2019. While difficult to estimate future import/export sales, Covid-19 is continuing to disrupt supply chains and affect manufacturing operations around the world, including South Africa’s domestic manufacturing which also declined by 0.7% in February. The same negative downward pressures apply across other manufacturers, especially those affected by the export lockdown, from boat-building to wine-making.

That Covid-19 will push the economy firmly into recession is certain. It’s only the extent of the recession, which is arguable, for the moment most likely in the 5–7% margins, as per the IMF, in the process stressing the government’s revenue streams and thus ability to respond. This translates, according to some economists, to the loss of as many as 1.6 million formal sector jobs by the end of the second quarter following the extension of the lockdown.

The downward pressure cuts across sectors, manufacturing as well as services. The impact on South Africa’s tourism industry is likely to add further to these woes. This sector contributed 8.6% of the country’s GDP in 2018 and was responsible for 1.5 million jobs. The question remains whether tourism will recover fully, how long this recovery will take, particularly without government support to the sector, and what other factors – such as the re-instatement of travel insurance – might assist. There is a related continental perception question, too, with weak African health care systems unlikely to inspire leisure travel confidence. Africa has the lowest ratio of doctors of any region, at just 1 per 10 000 inhabitants.

The lockdown has highlighted differences in the vulnerability and resilience of poorer South African communities, and the opportunity for continued near-normality. While white-collar workers in the financial services sector have for instance been able to continue their jobs almost unhindered working from home, many low-wage workers and those in the SMME-sector have either lost their incomes, been forced to take leave, or face job cuts. This highlights the plight of the ‘missing middle’ – those with incomes that disqualify them from receiving social grants, but whose incomes are too low to enable savings. This is illustrated by the simple statistic that 49% of South Africans live below the poverty line, while only 27% qualify for social grants.

There are questions also of the long-term effect on education and human development. Disparities within the country’s school system have been amplified, with most former Model-C schools and private schools utilising the internet to continue their classes, while poor schools – which make up approximately 75% of all schools – have been left behind. Adding to the tragedy, tens of thousands of school children that benefit from school feeding schemes are going hungry as the classrooms remain closed. The Grade 12 results at the end of 2020 will no doubt reveal these differences to a greater extent than ever before.

The pandemic has also exposed the vulnerability of the small business sector, which depends on short-term cash-flows to fund operating expenses. A new regime of regulation, taxation and incentivisation will apparently be required to save these businesses and to allow them to become more resistant to exogenous shocks. The rapid

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18 Based on the Living Conditions Survey (LCS) part of Stats SA’s household survey programme.
How to turn crisis into opportunity

take-up of private sector SMME funding in South Africa in the wake of Covid-19 emphasises this need.\(^1\)

The growing ‘missing middle’ will rely on the government’s ability to enable job creation in the private sector – an imperative clearly distinct from that of the government being the one to create jobs. Politically, this crisis can only increase tension within the ranks of the ruling Alliance, which has maintained unity by growing public service jobs and salaries at a rate which does not match productivity gains. This tension is highlighted by the massive and rapid private sector response to the crisis.\(^2\)

In essence, South Africa faces a political choice between attempting to double-up on the state or on the private sector. It is a political decision inasmuch it is not economically possible to increase expenditure across government, no matter the extent to which the ‘entire balance sheet’ is mobilised.\(^3\) The cost of fudging the choice between the state and the private sector has suddenly increased with Covid-19. The epidemic has offered the opportunity for the private sector to become a partner in economic development for government, as epitomised by the Solidarity Fund. How this relationship develops and whether both parties can see the growth opportunities present offers exciting possibilities.

Reforms will have to consider carefully which areas – from education, to healthcare, to boosting specific sectors – require assistance given the likely dramatic reduction in government spending. This will invariably require tough political decision-making as there appears no way of doing this without alienating one or another major political constituency. There appears thus a fork in the Alliance’s economic future: one with the state at the centre, funded by a combination of international actors and increased domestic taxation, where the state plays an even more central role in production and distribution from retraining to establishing new infrastructure and financial architecture. The other route is of a state cut down to a size the country can afford, enabling lower tax-rates to stimulate growth and reform of the state-sector.

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\(^1\) In the first ten days of its operation, for example, the South African Future Trust established by the Oppenheimer family committed over half of its original R1 billion trust fund to 45 000 beneficiaries working in some 4 500 companies. It was reported, too, that the R1 billion Rupert family Sukuma Relief Fund was immediately overwhelmed by more than 10 000 applications and oversubscribed. At https://city-pressnews24.com/Business/doors-closed-for-applicants-seeking-relief-from-johann-ruperts-r1bn-fund-following-oversubscription-20200407.


Most importantly, given the socio-economic situation the country was in pre-Covid-19, any reforms undertaken in the aftermath of the crisis will have to aim to deliver the country to a different place than it was before the virus hit.

**Six Key South African Insights**

1. **This pandemic will exacerbate inequality.** A close watch will have to be kept on any potentially anti-poor policies and interventions which might drive inequality, such as taxation policies. Special attention needs to be paid to schools.

2. **The global order has changed.** Only the most robust aspects of globalisation will remain. This means that some industries – particularly tourism – might take a long time to rebound. Targeted government intervention will be required to kickstart hospitality and other contact-based services. The response of the insurance sector will be crucial to restarting tourism.

3. **The pandemic has also highlighted the pitfalls of fake news and disinformation.** Particularly in a country like South Africa, where connectivity is a luxury afforded to the relatively rich, government will have to address differential access to information, as this also affects government’s ability to gather crucial information.

4. **There will be fresh opportunities, for example in manufacturing and in services, in part facilitated by the cheaper Rand.** For South Africa, utilising this opportunity will hinge on better integration with African value chains and improved information on these markets.

5. **South Africa should keenly anticipate further similar (or different) crises.** Therefore, there cannot be too much analysis on the effects of the pandemic, the response by government and the success of specific policies. Data collection is key.

6. **When a financial bailout comes, there will be little to no scope for error.** Misuse of borrowed money will dig the economy into an even deeper hole. Government must not expect any special treatment or hand-outs and will have to ensure that the conditions of financing are favourable.

**South Africa’s Choices**

How should South Africa approach the array of crises it faces with a view to emerging from the Covid-19 pandemic in a stronger position to deal with its multiplying economic challenges?

Those on both the left and right – the ‘idiot ideologues’ – will see the pandemic as an opportunity for radical solutions: for higher taxation regimes and state bailouts writ large at the one extreme; on the other for mass privatisation and state sell-offs of land and other assets. No silver bullets exist, however, and no easy, simplistic solutions exist; rather the reform path as ever lies in between the radical offers, involving a series of difficult political trade-offs and tough resource choices.

These are the key choices that have to be made:

1. **Muddle Along or Make the Tough Macro-Economic Choices**

South Africa’s fiscal and financial room to manoeuvre had shrunk prior to Covid-19 crisis and has since worsened dramatically.

It is vitally important that strong signals are sent to domestic and foreign audiences that the government understands the magnitude of the crisis it faces, and is taking strong, well-targeted steps to reverse the dire economic outlook and reduce risks to the sustainability of the balance sheet.

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24 To use Rob Rose’s apt term. See https://www.businesslive.co.za/fm/opinion/2020-04-20-rob-rose-ramaphosas-roast-chicken-gestapo/.
AFTER THE VIRUS: 
CHOICES FOR A BETTER SOUTH AFRICAN FUTURE

KEY SOUTH AFRICAN REALITIES:
1. South Africa’s economy was in a perilous position even before the pandemic began.
2. The resulting recession could slash economic growth by as much as 7%, and shed 1.6 million jobs.
3. Cash-flow pressure on small businesses is immense, and the worst-hit segment is likely to be the ‘missing middle’: South Africans that don’t qualify for social grants, yet earn too little to save, and are vulnerable to unemployment.
4. In this way, the recession will exacerbate inequality.

THE KEY CHOICE IS BETWEEN THE STATE AND THE PRIVATE SECTOR, EITHER TO:
1. **Place the state at the centre**, by attempting to use government as a machine for growth and job creation will increase already-dangerous government spending, raise debt and worsen the situation: OR
2. Change the paradigm to one of private sector-led growth, **reigning in public spending** and stimulating business growth and investment will place the economy on a different growth path.

A COST-BENEFIT ANALYSIS TO ECLIPSE ALL OTHER
Reform will come at a great political cost. It requires the severing of the thousands of senior government jobs and tenders that have been wrongfully awarded to cadres who will not go down without a fight.

But the cost of not reforming will be greater. It will mean losing sovereignty and government’s ability to deliver social welfare, services and stability.
The approach of muddling along with the promise of future action – kicking the can down the road – is no longer effective. Moody’s, the last rating agency to have South Africa at investment grade status, has lost confidence and the country is now junk-rated by all agencies.

In the words of the economist Andrew Donaldson: ‘The government needs to implement the changes in programmes, public service remuneration, extra-budgetary commitments, state enterprise reforms and revenue strategies that will bring the deficit down to sustainable levels, alongside a recovery in economic growth. These may be three- to five-year adjustments, but there are steps along this path that have to be taken now.’

What is needed is a ‘credible medium-term fiscal adjustment strategy’. The reality is stark: If such adjustments are not made now, the government risks losing all credibility with the financial markets, leading, eventually to financial and fiscal collapse.

2. Rhetoric or Action on Small Businesses

Government has publicly supported small business growth, has a ministry dedicated to small enterprises and repeatedly says that small businesses are the engine of employment. But the reality does not match the rhetoric. The small business sector is smaller than it should be compared to peer countries and is highly cash-flow dependent and vulnerable. This is due to the onerous regulatory, tax and labour-regulation environment.

Immediate actions to be taken should include: the exemption of small businesses from collective bargaining agreements driven by large corporations and large trade unions; the swift implementation of subsidy schemes and incentives for start-ups, including tax holidays and labour-law exemption.

It is time to strengthen competition legislation to lower barrier to entry for new operators in banking, telecoms and other sectors where large companies dominate.

3. Bailouts or Dividends from State-Owned Enterprises

There is simply no new money available to bail-out State-Owned Enterprises such as Eskom, SA Airways and Transnet, which bear a large responsibility for the depth of the hole the economy is in.

The portfolio of state-owned enterprises must be urgently reviewed and non-core cost centres must be closed or sold off – if there are private buyers. The continued bailing-out of the dysfunctional SA Airways (on which the state has already expended R16.5 billion in the last decade, or R1 000 per household) must be stopped and it should be closed or sold off. Eskom must be overhauled to remove all the rents built into contracts over decades of corruption, to price coal correctly and to approve maintenance and builds that are based on competitive turn-key tenders.

The Covid-19 crisis has radically reduced demand and this provides Eskom with the opportunity to slash its fixed costs, getting rid of employees it did not need prior to the crisis and cutting contract costs.

The introduction of price competition into electricity generation is vital to ensuring an efficient grid.

Private partnerships are needed to inject new capital into rail and port operations, reducing the costs of importing and exporting and making South Africa a more desirable part of global supply chains.

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26 Ibid.


Plans need to be made with the 700-odd other SOEs – whether to sell off, merge or continue operations.

4. A Moribund State or One that Delivers Growth
The state is not fit-for-purpose and has become a supplier of patronage opportunities at the cost of efficiency and function. The first priority must be a radical overhaul of health provision systems, with a view to improving access by all to intensive care facilities and a boost to the country’s excellent laboratories, placing South Africa at the forefront of research into and finding solutions for external shocks from viruses.

South Africa funds health and education as a portion of GDP better than most developing nations, but its outcomes are often worse with most of the money soaked up in consumption expenditure when there is a dire need for new infrastructure.

An expanded infrastructure programme in partnership with the private sector aimed at addressing network costs and dealing with the maintenance backlog on roads, rail and ports must be instituted with the effect of opening up.

Beyond this, the state needs to become a partner in developing private sector growth with an emphasis on job creation.

South Africa needs to implement much talked-about (over three decades) reforms to its labour market to reduce the number of days lost to striking, and to link wage increases to improvements in productivity.

The need for a capable state is not, at its core, about spending more, but about spending better. Operational efficiency in fiscal expenditure is critical.

5. Open for Business or Cadres Only
South Africa must become an ‘open-for-business’ economy, where it is easy to invest and achieve a return that competes with other investment destinations. This calls for a sea-change in how government regulates the economy from an approach which seeks to extract rents for politically connected constituencies to one where obstacles to investment are actively minimised in partnership with the private sector.

It is simply not possible to turn all the well-meaning promises of investment into real businesses and jobs while there is high regulatory risk in comparison with South Africa’s peers.

A permanent investment agency – privately-run, but backed by government, perhaps taking a leaf out of the successful management of the Solidarity Fund – needs to be established to facilitate foreign capital inflows by actively removing obstacles.

The Costs and Benefits of Reform
Much debate on the various policy responses to date focused on the costs of bailing out the South African state, and where the money might come from and be spent.

The problems are deeper than Covid-19, as South Africa’s chronically poor economic performance over the last 12 years reminds. There is a danger that money without strings, IMF, ratings’ agency or otherwise, will simply be poured away into a bottomless pit of state wants and its personnel needs.

South Africa’s choice is a simple one: Sort out its policy and financial mess on its own or erode the government’s ability to deliver social welfare, services and stability, and lose policy sovereignty.

The ‘failure’ option, which has been pursued over the last two decades, has been to say the right things while ignoring the financial implications of insatiable borrowing and rampant spending to keep an oversized state and its enterprises afloat. The economy has

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29 See, for example, the IEJ proposals around a R400 billion rescue plan at https://www.groundup.org.za/article/economists-propose-r400-billion-relief-plan/.
structural problems, but they start with structural problems in South Africa’s politics. Large and powerful constituencies hold onto the belief that the state ought to be the primary driver in the economy and are deeply suspicious of the private sector. This notion has become entrenched within the ruling alliance as the state and SOEs have become patronage dispensing machines that absorb labour without improving productivity. The delivery of services has been patchy at best, but the cost of greasing the machine has been rising, nonetheless.

This statist view, South Africa’s development history shows, is financially unsustainable, and in a political culture shaped by entitlement, encourages state-capture. Unfettered further financing runs the very real risk of simply refuelling rent-seeking.

The ‘success’ option is to make the state and SOEs meritocracies, the kind that attract and reward highly skilled managers and workers who are able to more efficiently and effectively deliver on the state’s mandate. Such a development state would develop policy based primarily on its impact on economic growth and job creation, and would view the private sector as a vital partner to advance the country.

Of course, the political costs of the latter approach are significant. It requires the severing of the thousands upon thousands of senior jobs and tenders that have been wrongfully awarded to cadres who will not go down without a fight.

But the decision to humour the inefficient cadres at the expense of the country and those who desperately require jobs, service delivery and effective interventions by a functional state, is a deeply cynical one. It mortgages the country’s future for the sake of short-term political gains, and it will surely destroy the legacy of the leaders who cling to it because they would prefer to muddle through with the support of the hyenas than strike a bold new path.

There can be no debate about this choice. We have seen these two paths in action over the last three decades. In the years in which fiscal discipline and sound monetary management were at least partially implemented – the early to mid-2000s – South Africa’s economy grew, jobs expanded at the fastest rate post-apartheid, and it even produced a budget surplus.

Since then, through the years of state capture and enduring until the present, South Africa has experimented with the other path – growing the state, dispensing patronage rather than services and stoking spending through borrowing. The result of this experiment is there for all to see: a weakening currency, debt servicing costs, commercial stress, and the inevitable loss of sovereignty to one or another global lender.

The decision that must be taken now is one that will set this country’s trajectory for decades to come. Leveraging balance sheets, borrowing and spending absent good governance, and a policy setting – as outlined below – which encourages business can only take South Africa down the path of diminished delivery, lower investment, fewer jobs and greater instability. Structural reforms that contain spending, uproot cronism and tailor spending to the financial realities will produce a more effective, professional state that delivers – a sound financial platform to allocate resources to capital projects and investment, growth and jobs.
AFTER THE VIRUS:
AN ACTION AGENDA

15 Immediate actions that government could take to signal that it is intent on structural reforms:

1. Make access to 5G spectrum permanent and issue more spectrum to allow greater competition in telecommunications.
2. Implement cuts to the public service wage bill as indicated in the pre-Covid budget speech.
3. Pass legislation allowing government and state-owned enterprises to void contracts entered into during state capture.
4. Investigate the return on spending achieved in health and education and on general government running costs.
6. Issue RFI’s for a list of SOEs to be sold off in part or in full to raise money to fund the Covid-19 recovery.
7. Amend Municipal budgetary rules to reward delivery and discourage wastage and overspending.
8. Amend legislative and regulatory obstacles that discourage investment such as restrictions to foreign land ownership.
9. Re-energise the role of the private sector and reposition it as a partner, not enemy, in economic growth.
10. Establish a privately run and independently managed national investment promotion agency as a priority.
11. SETA levies should be retained by those businesses with a plan to put them into apprenticeship schemes.
12. Develop a joined-up, route development strategy to connect South Africa with the rest of the world.
13. Prioritise services exports to Africa and the rest of the world, from financial services and healthcare to retirement villages.
14. Unleash the digital economy, by upping the venture capital tax benefit.
15. Remove work-permit requirements on all African nationals with a post-graduate or higher university qualification.
Conclusion: Turning Crisis Into Opportunity

On Tuesday 21 April 2020 President Cyril Ramaphosa offered a plan to mitigate the worst effects of the Covid-19 crisis.

Still South Africa urgently needs a plan to ensure a high-growth future, one where the private sector can grow faster to provide the jobs that South Africans desperately seek. The loosening of interest rates by the SA Reserve Bank is an example of a step in the right direction in increasing private credit growth, but the economy requires also a fillip from the types of policy choices outlined above.

The manner and speed whereby the country can access an offramp from the lockdown will indubitably assist in any reset of the country’s longer-term economic trajectory, but there is no escape from the harsh realities that face Ramaphosa’s government. If anything, the crisis has shown exactly how stressed the contemporary circumstances of South Africa’s economy, many of its businesses and its citizenry are. But it also provides an opportunity to make far-reaching changes. Crises, to paraphrase Denis Healey, may come and go, but for governments like economies, the rules of arithmetic and geography remain the same. Covid-19 substantially raises the costs of government inaction and of misguided policy direction. To turn this crisis into an opportunity, South Africa’s leadership will have to act with decisiveness and implement much-needed economic policy reforms which put jobs and growth before ideology and vested interests. This better future, one of progressive capitalism, is not about less state or more state, but about a capable, efficient, corruption-free state.