CDE
EXECUTIVE
SUMMARY

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POLICY GRIDLOCK?

Comparing the proposals made in three economic policy documents

Introduction

This report examines three major government strategy documents relating to the economy:

- The Industrial Policy Action Plan (IPAP) produced by the Department of Trade and Industry;
- The New Growth Path (NGP) produced by the Department of Economic Development; and
- The National Development Plan (NDP) produced by the National Planning Commission.

The report examines government's economic strategy as articulated in these documents, seeking to illuminate areas of agreement and of disagreement, as well as differences of emphasis. It assesses the extent to which the approach to economic policy articulated in the three documents coheres into a single approach.

This report is not intended as a critique of government policy. The objective is more limited: to define and delineate policy approaches current within government more sharply. The report must necessarily summarise and condense the arguments and proposals made in each document. However, in doing so, it seeks to represent fairly and objectively the core assumptions and arguments of the three documents. The advantage of this approach is that it helps readers to better understand the similarities and differences of the three policy documents, and to engage with what they propose. Obviously, full engagement with those documents requires reading the originals.

What are the policies' primary objectives?

Industrial Policy Action Plan

IPAP's objectives are premised on long-standing international thinking about industrial policy, and include expanding the industrial base and diversifying exports. Despite this, employment creation is the clear policy priority even though this is seldom the principal aim of industrial policies elsewhere. The clearest manifestation of this is that IPAP's policy proposals are evaluated against their potential to increase employment, resulting in an aggregate target of creating just under 2,5 million direct and indirect jobs.

New Growth Path

The NGP has a number of objectives including a reduction in income inequality, faster economic growth and the development of a green economy. As in IPAP, employment creation is the NGP's principal objective and is the only one to have clear quantitative performance metrics, promising to create 5 million jobs by 2020. This aggregate employment metric is built on a series of sectoral targets, including: infrastructure, 250 000 jobs per annum; getting 300 000 households into agricultural smallholder schemes; and 145 000 jobs in agro-processing by 2020, etc.

Despite being ostensibly a growth plan, the NGP does not specify a growth target, nor is there a discussion on what determines and constrains growth; when growth is considered at all it is only in the context of employment creation. The NGP starts with the desired employment number and then works back to the desired level of growth. In doing so, however, it only considers jobs that meet the criterion of being "decent work"—though it does not define the term.

National Development Plan

The NDP sets out a number of measures of economic success. These are not limited to employment creation and include:

- GDP growth of 5,4 per cent between 2010 and 2030;
- Annual employment growth of 3,3 per cent to 2030;
- Growth in investment at 15 per cent a year until 2030; and

- Average annual growth of 6 per cent in the volume of exports.

The NDP explicitly recognises that employment will be highly conditional on the rate of growth, but suggests that South Africa will need to create 11 million jobs by 2030 to reduce unemployment to 6 per cent.

With respect to "decent work", the NDP says that this should be achieved in the long term consequent upon an expanding economy with rising skill levels, while in the earlier phase of the plan emphasis will have to be placed on mass access to jobs while maintaining standards where decent jobs already exist.

Understanding the economy's constraints

Industrial Policy Action Plan

IPAP describes the South African economy, both prior to and after the recession, as consumption-driven, which, it says, is not sustainable. Growth in consumption-driven sectors (finance and insurance, real estate, transport and storage, communication, wholesale and retail, and catering and accommodation) is said to have occurred at the expense of the production-driven sectors (agriculture, mining, manufacturing, electricity and water, and construction).

Table 1: Defining objectives and characterising employment

	OBJECTIVES	QUANTIFIED OBJECTIVES	EMPLOYMENT OBJECTIVE	CHARACTERISING EMPLOYMENT
IPAP	• Exports • Technology • Skills • Employment	• Employment (Aggregate)	• 2 447 000 by 2020 (direct and indirect) • 350 000 by 2020 (direct)	• N/A
NGP	• Employment • Growth • Green economy • Reduction in inequality	• Employment (sectoral targets)	• 5 million jobs by 2020	• Decent work
NDP	• Output • Investment • Exports • Employment • Poverty and inequality	• Output • Investment • Exports • Employment • Poverty and inequality	• 11 million jobs by 2030	• Decent work over long term

IPAP identifies two key factors that underpin this trend:

- A mal-functioning financial sector in which, mainly due to an asset-liability mismatch, short-term investments that characterise the services sectors are preferred over longer-term and capital-intensive investments - which are required to fund manufacturing investments.
- An overvalued exchange rate which stimulates a booming consumption sector and increases imports, but which jeopardises exports, and, as a result, creates an adverse trade balance and makes South Africa increasingly reliant on short-term capital inflows.

To counter these, IPAP says South Africa needs a more competitive exchange rate and lower interest rates.

New Growth Path

The NGP offers a similar characterisation of South African growth as consumption-led, but it takes a different view on what underpins this, pointing to a dynamic where South African interest rates have fallen as a consequence of the higher nominal value of the Rand. Lower interest rates, it says, have fuelled consumer borrowing.

The NGP identifies what it terms "fundamental bottlenecks and imbalances in the economy":

- Over-dependence on the minerals value chain, leading to the high emissions-intensity of the economy;
- Weaknesses in the state's use of commodity-based revenue for economic diversification and skills development;
- Bottlenecks and backlogs in logistics, energy infrastructure and skills, which raise costs across the economy, and which are manifested most obviously in capacity constraints in the generation of electricity;
- Continued economic concentration in key sectors, permitting rent-seeking at the expense of consumers and industrial development; and
- A persistent balance-of-trade deficit funded with short-term capital inflows attracted largely by high interest rates.

National Development Plan

The NDP does not describe the country's economic trajectory as consumption-led, suggesting instead that South Africa is caught in a "middle income trap": it is unable to compete at the "bottom-end" with low-income countries but is also unable to break into, higher-value products and markets that are dominated by high-income countries. Four key constraints, which reinforce each other, impede attempts to grow faster:

The lack of competition in goods and services stifles innovation and the entry of new firms;

Uncompetitive labour markets keep new entrants out and skew the economy towards high-skill, high-productivity sectors;

Low savings mean that the country is reliant on foreign capital inflows; and

A scarcity of skills pushes up the premium for skilled labour and contributes to rising inequality.

The NDP regards the local financial sector as one of South Africa's key competitive advantages. Other strengths include natural endowments (especially minerals), a strong fiscal position, the country's location on the continent, quality universities, and a sophisticated services industry.

Where will new jobs be created?

Industrial Policy Action Plan

Apart from IPAP's aggregate target for direct employment growth in manufacturing at 350 000 additional jobs by 2020, there is no additional analysis of what sort of firms would allow for this growth (eg. whether these will be large or small, new or existing, export-oriented or focussed on the domestic market).

New Growth Path

The NGP sees the largest share of future employment growth happening in the productive sectors and infrastructure provision, in contrast to the service sector which it does not regard as a key area for growth. As with IPAP, nothing is said about the type of firms that will grow employment.

National Development Plan

With 5,9 million jobs by 2020 (and 5 million more by 2030), the NDP is the most ambitious strategy in terms of job creation.

In contrast with IPAP and the NGP, the NDP envisages most employment growth (90 per cent) will occur in small, labour-intensive service firms largely oriented to the domestic market. These are not high-technology firms, but are composed largely of semi-skilled and low-skilled workers.

Clearly the largest part of the projected employment growth cannot be achieved in existing firms, but will require a very large increase in new firm entry.

Policies proposed

Based on a different specification of objectives; characterisation of South Africa's key economic constraints, and differing perceptions as to where new jobs are likely to be created, the three strategy documents propose differing policies. Table 2 on page 6 provides a brief overview.

Concluding remarks

While there are significant differences in the central emphasis that they assign to employment creation—for IPAP and the NGP, employment growth is the sole quantified objective while for the NDP there are other quantified goals and employment is seen as dependent on economic growth—the three strategy documents are in broad agreement that employment creation is the key objective of economic policy.

There is some measure of overlap among the documents, but significant differences emerge between IPAP and the NGP, on the one hand, and the NDP, on the other, in their respective characterisations of the trajectory of the South African economy and in the identification of the binding constraints on further development. There are additional differences in the identification of the economic sectors and activities—and of the characteristics of firms—that have the potential to create new jobs. These differences underpin and inform the different policies proposed by the three documents.

Clearly, if government policy is to be coherent, choices will have to be made about which set of policies is most appropriate.

Table 2: Key Policy Interventions

POLICIES	IPAP	NGP	NDP
Exchange rate	• Unqualified support for depreciation	• More competitive • Requires - fiscal restraint - accord on wages and prices	• No nominal devaluation • Conditions for effective devaluation do not exist
Development finance institutions and capital subsidies	• Expanded DFIs • Investment subsidies	• Expanded DFIs • Investment subsidies • Development bond • State-owned bank for rural areas	• None advanced
Local procurement	• Unqualified support	• Unqualified support	• Caution on higher costs jeopardising growth
Sector support strategies	• Very wide ranging industrial policy, with an emphasis on beneficiation	• IPAP plus: - infrastructure - agriculture - mining - green economy - tourism - high level services	• Protect sectors with long-term prospects • Short-term support measures for industries affected by cyclical downturn • The financial sector • Retail and business services
Labour market	• No consideration	• Productivity accord • Tighten sub-contracting, labour broking, and outsourcing. • Support for workers in unorganised sectors to achieve greater organisation	• Youth Wage subsidy • Wage restraint • Regulation and subsidy to labour placement sector • Unfair dismissal not to apply for probation period • Simplify dismissal procedures • Migration policy reform to attract more foreign skills

This is the executive summary of a CDE Focus written by Professor David Kaplan of the University of Cape Town. The full-length publication is available from CDE. It can also be downloaded from www.cde.org.za.

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