A Country in Crisis

First steps towards a growth strategy

Executive Summary

Introduction

In June 2023, CDE published an assessment of the reasons why economic growth has collapsed, arguing that the combination of bad policy, catastrophic governance and weak leadership amounted to what is effectively an anti-growth strategy. (Read CDE's report, South Africa's Anti-Growth Strategy: How poor policy and bad governance are wrecking growth.)

In this second report, we argue that policymakers need urgently to arrest our decline. There is no shortage of growth plans and strategies in South Africa today. There are two dominant but flawed approaches. One consists of a long laundry list of reforms and aspirations with little sense of what to prioritise and how the elements of the list all fit together. The second approach tries to prioritise immediate actions but fails to take into account state collapse or the country's devastating lack of leadership.

At no stage has the President or government provided a convincing or comprehensive diagnosis of why the country is in such deep trouble. Without such a diagnosis it is impossible to move forward. Specific challenges are framed as unexpected crises, a series of unfortunate, unpredictable accidents that might have happened to anyone. As a result, the county is in perpetual crisis response (not management) that never begins to address the root causes of our expanding polycrisis.

In order to stop the country falling apart, CDE is proposing a different approach. The focus of government needs to be on three core priorities: improving security and the rule of law, addressing the crises in energy and logistics, and stabilising public finances.

The country faces many other challenges, but these three priorities should dominate Cabinet meetings, the President's diary, government's budgets, and the substance of every government communication. Everything else is likely to be a distraction. Focusing on these three issues is not a recipe for rapid and sustained economic growth. But failing to address them guarantees that accelerated and sustained growth will never be achieved.

In implementing these priorities government should be guided by a few key principles of how to reform: hard-nosed realism about what the government can do now; stop fantasising about a capacitated state emerging in the near future; recognition that pro-market policies will work far better than policies that weaken markets; and acceptance that Master Plans are the wrong approach for South Africa's economy.

Improving security and the rule of law

No country can expect to grow with a security situation as bad as South Africa's, especially if there is deepening penetration of organised crime into a rising number of economic sectors. The two goals that should be prioritised to improve security are interlinked:

- Build state capacity to resist the mafias that are making economic growth increasingly impossible; and
- Build the state's capacity to protect itself from self-serving members of the political, bureaucratic and economic elites.

Law enforcement agencies should be making more aggressive use of terrorism and sabotage charges against people who use violence and the destruction of property to secure a policy change or some other concession from government. They should also explore the more aggressive use of charges relating to money laundering, which would make it possible to charge people who benefit from crimes that they did not themselves commit.

In relation to corruption cases, prosecutors seem determined to maximise the number of charges they put to every accused person, and, as a result, investigations take forever and are endlessly delayed. A more efficient approach would be to lay a narrower set of charges – even if these are not the most serious – so that cases can proceed more quickly. Prosecutors should also be open to plea bargains.

Addressing the energy and logistics crises

No economy can function, much less grow, without access to reliable and affordable energy, while the increasing dysfunction into which Transnet has fallen is further undermining growth. A key reason for these crises is that decades of cadre deployment in the state-owned companies has resulted in leadership that lack the knowhow to manage businesses that, because of misguided theories of development, are monopolies in their sectors. Resolving these crises requires two distinct but related activities:

- Government must recognise and address the technical, managerial and governance deficits in both Transnet and Eskom; and
- Government must unwind Eskom and Transnet's statutory monopolies and develop competitive markets for the generation of electricity and provision of logistics.

Freeing up businesses and households to generate energy has relieved pressure on Eskom's generating fleet and demonstrated how we can make progress. But to derive the full benefit of liberalisation we need to create competitive markets which requires the establishment of an independent systems operator buying electricity from lowest-cost producers on a continuous basis, proper feed-in tariffs and adjustable tariffs. Corresponding needs in a liberalised logistics market might include competing firms using the freight lines and providing port services so that users would be able to choose the best offering from more than one provider.

The need to create markets in these sectors is not satisfied through public-private partnerships and subcontracting arrangements. These might improve efficiency in the short term, but they are not a real departure from the basic model of a monopoly provider and could result in a new form of corruption and state capture.

Stabilising public finances

Although government's budgets articulate the need to reduce the deficit and stabilise the debt ratio, far too little has been achieved. The time has come to recognise that there is no option but actual spending cuts. A corollary of this is that government must roll back the commitments it has been making for higher levels of spending, whether in the form of faster-than-inflation increases in public sector salaries, unrealistic promises relating to a basic income grant, and the uncosted commitments being made to implement National Health Insurance.

There are no easy ways to cut government spending and doing so will provoke resistance from those affected, particularly public servants. Government's most important tasks are:

- Identify and implement a plausible strategy for fiscal retrenchment; and
- Start explaining to officials, public servants and the general public why spending cuts are both inevitable and necessary, and how they are going to be done.

In implementing spending cuts, it is important to recognise that it is undesirable to reduce spending on infrastructure, though infrastructure spending should be more focused on alleviating constraints to growth. In the context of state weakness and fiscal constraints, expanding the role of the private sector in infrastructure delivery must be a top priority. The response of citizens and the private sector as a whole to changes in the regulatory regime governing electricity generation shows how rapid a response might be expected to long-promised reforms to the public private partnership regime.

Cuts should be made where public spending offers the lowest returns. This might include subsidies provided to favoured sectors and businesses, and financial support provided to public entities that have reached a point of institutional failure. The specifics have to be carefully considered, and given the urgency of the situation, would require rapid review of private sector subsidies and public entities.

To achieve larger cuts we believe it is possible to consider shutting down whole departments, or components of departments, or reducing the size of bloated divisions like human resource management and communications, which tend to be highly inefficient and deliver little value. Candidates for cutting could be departments of Planning, Monitoring and Evaluation, Public Enterprises, Small Business Development, the Sector Education and Training Authorities, and significant parts of the department of Employment and Labour, Sports, Arts and Culture, and COGTA. The National Student Financial Aid Scheme could be converted into a student loan programme, with income-contingent repayment plans administered through the tax system (as recommended by the 2017 Heher Commission).

The vital importance of leadership

It is fair to say that we have doubts that any of what we have proposed above will happen. Certainly, it won't unless there are very significant changes in the way South Africa is led.

Replacing ineffective leaders and officials with more effective ones is, in fact, the first principle of reform. South Africa now needs leaders that place the interests of the country at the heart of its agenda, led by a President who is backed by a committed, credible and unified team that understands how to transform and bed down change in complex systems. As 'communicator-in-chief', the President must build a credible and hopeful narrative, and, as quickly as possible, a new consensus of where the country is going, how to change South Africa in the interests of all (not a well-connected elite), and the progress that is needed to do so.

The leadership team needs to understand the power of markets to drive prosperity and inclusion, and the essential role of the state in providing the foundations for market-driven solutions. It needs to be cognisant of the desperate poverty of nearly 60 percent of the population, and provide hope to all those excluded, while at the same time opening up the economy for more new firms. The team will need courage and legitimacy to drive change. It will need to build alliances with a broad range of constituencies and ensure the incremental inclusion of more and more South Africans, coupled with real improvement of public services.

Concluding remarks

The essential precondition of growth in South Africa today is that you can't start to rise until you have stopped falling.

To do this, we must stabilise our public finances by reducing expenditure; we must solve the crises in energy and logistics while putting in place the foundations of market-driven solutions that will replace the existing monopolies; and we must ensure that the justice system identifies and prosecutes the intertwined mafias and corrupt officials who have strengthened their hold on a growing number of sectors and activities.

There is no way to model the effect that achieving significant success in pursuit of these goals would have on growth, and it is even less possible to model what the effect would be of merely being seen to be pursuing them. What we do know is that failing to do these things essentially guarantees that South Africa's growth rate will continue to fall and will eventually turn negative, with dire consequences for poverty, inequality and stability.

To get to a point where we can expect these changes to be urgently and effectively implemented, we need not just a new leadership team, but a new way of leading.

Read the full report available on CDE's website (www.cde.org.za)

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