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in the moment



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# National Treasury growth strategy proposals
# Will there be political will to implement?

## Highlights

- National Treasury recently released an economic growth strategy discussion document highlighting the various reforms required to attain transformation in the South African economy through sustainable and inclusive growth, while maintaining global competitiveness.
- The document outlines the policy interventions required through short-, medium- and long-term reforms to improve growth in the economy by 2% to 3% in the next ten years, while creating a million jobs.
- This is merely a discussion paper and can only be implemented by all government departments once it becomes part of economic policy. As such, the political will to drive the successful implementation of the proposed reforms will be the ultimate judge of the relevance of the document.
- Nevertheless, the intention to release the document from Treasury without it going through Cabinet first can be seen as favourable as it eliminated lengthy consensus-seeking discussions before it was published and it could possibly draw public support against the anticipated labour union outcry on a number of proposals outlined in the document.
- The reforms proposed are not entirely new in nature, some arise from the National Development Plan and the Harvard recommendations, but are pragmatic and reasonable in Momentum Investments' view. While some of these reforms are inherently expected in our baseline growth forecasts, the achievement of the longer-term and more politically contentious reforms provide upside to our growth expectations, but will depend heavily on government's willingness to implement and drive these proposals.

## Background

The current low growth (decline in real gross domestic product per capita since 2015) and high unemployment trajectory requires sustainable interventions. Economic transformation without hindering long-term global competitiveness and labour-intensive growth should be key to reforms.

Not all the proposals are new and many have been mentioned in the National Development Plan (NDP), Ricardo Hausmann (Harvard) assessment and previous budget documents. The key themes are discussed below:

## Modernising network industries

. Electricity

- Integrated Resource Plan (IRP) updated to reflect economic conditions and technology
- Council for Scientific and Industrial Research (CSIR) found that by 2025 the renewables share of total energy should be 70% in an unconstrained and least-cost model, higher than the 30% estimation in the Department of Energy's base case
- CSIR also showed the least-cost energy mix is R70 billion less per annum
- Independent transmission company from Eskom unbundling
- Selling-off power stations with station specific obligations (staff contracts etc.), the sale of these assets could raise R450 billion assuming costs are reflective of tariffs (SBG Securities believes this amount is ambitious)
- State-owned transmission to purchase electricity transparently from independent power producers (IPPs)
- Reduce municipal reliance on electricity revenue
- Should allow consumers to sell excess electricity they generate
- Installing solar PV panels on social housing (providing free electricity for indigent households)

Telecommunications

- Spectrum should be released with state-controlled network being minimal
- Finalisation of rapid installation of telecommunication infrastructure
- Open access conditions to minimise infrastructure duplication
- Leverage private sector for broadband roll out
- By the third year the price of telecommunication will have declined by 25%
- 10 % rise in fixed broadband penetration raises growth by 1.35% in developing countries

Transport

- Introduction of Economic Regulation of Transport Bill contributes to competitive pricing and improved service quality in the freight rail and port system
- Third-party access to rail network (increase private sector participation)
- Introduce competition in rail and ports
- Rail freight is cheaper than road, but road still represents 70% of market share (shift from road to rail where practical and efficient)
- Green paper by Department of Transport suggests full cost recovery from freight operators (heavy goods vehicles currently subsidised)-global trend charges by distance and weight
- Consider reviewing fuel price regulation (in 2003 reviewed fuel price and petrol price dropped by 4 c/l)
- Formalise taxi industry and subsidise it

Water

- Investment strategy for water resource development, bulk water supply and wastewater management
- Independent water regulator can improve efficiency of water supply and pricing
- Implementation of national water conservation programme

## Lowering barriers to entry, increasing competition and small business growth

- Competition and market structure to be considered when drafting legislature
- More accessible development finance, such as small business and innovation fund underway
- One-stop shop for smaller firms, such as public procurement can help reduce red tape
- Relaxed regulation in network industries (telecommunications and banking) results in less onerous and more flexible support of mobile money
- Addressing exclusive leases lowers barriers to entry for retailers
- Reduce switching costs in banking and telecommunications (positive for consumers)
- Costs of compliance with red tape is the same across companies (more expensive for smaller companies)
- Address late payments from government to smaller business and draft tenders specifically for smaller businesses (subcontracting through larger firms)

- Revisit the previously rejected (procedural flaws) of the Red Tape Impact Assessment Bill which can reduce red tape by 25% over 5 years
- Full or partial exemptions for small businesses (extension of bargaining council agreements is onerous on small firms that cannot afford steep pay increases better absorbed by larger firms)

## Supporting labour-intensive growth in agriculture and tourism

- Improve access to financing to farmers
- Land Bank should broaden their insurance product offering (business continuity and food security) and allow for affordable agricultural insurance
- Extension of services to support smallholder and emerging farmers to transition to higher-value agricultural commodities
- Improve market access to water, markets and trade promotion in irrigated agriculture (apples, citrus, avocado, macadamia)
- Budgetary support for tourism agencies
- Relaxed visa regulations should support growth in tourism and uphold safety and security concerns, such as a Tourism Safety Initiative (visible policing in tourism hotspots)

## Promoting export competitiveness and harnessing regional growth opportunities

- Infrastructure access improved by competition promotion and private sector participation
- New and re-negotiated trade agreements with growing markets (Southern African Development Community [SADC])
- Improve intra-regional logistics
- Automation of licensing system for key export documents and review border control procedures
- SA product export awareness, Export Marketing and Investment Assistance Scheme

## Economic stance

- Economic growth should complement a reduction in inequality (which aggravates social fragmentation), although a growing economy should take precedence
- Low growth limits transformation, counter-cyclicality of fiscal and tax policy increasing state's inability to stimulate aggregate demand which threatens overall long-term potential growth
- Virtuous cycle between economic transformation with inclusive and sustainable growth while remaining globally competitive. Complementing each other and not mutually exclusive or competing
- Trade-offs, economies of scales, transition into new sectors remain important factors which could be planned for through reskilling people and ensuring welfare-neutral interventions
- Small, medium, and micro enterprises (SMMEs) are responsible for more than 50% of all employment opportunities in SA and the sector contributes more than 45% to GDP, but SA has the lowest successful SMMEs creation rates. In the first year 70% to 80% of them fail and about half of the survivors last for the next five years. Initiatives need to be outlined to reduce the regulatory burden for SMMEs
- Document mentions the importance of inflation targeting
- Land reform cannot be done with a one-size-fits-all approach
- Capable economic institutions represent collective choices ;security of property rights, market structure, barriers to entry and contractual agreements and its enforcement
- Improved government finances and fiscal trajectory will reduce borrowing costs across the economy and have important broader macroeconomic benefits

## Long-run growth fundamental building blocks

- Educational life cycle enhancement (linking it to labour market needs) and focusing on early childhood development (raise earnings by 25%)
- Continuously support youth employment interventions (cooperation between learning institutions and private sector, learnerships and apprenticeships)
- Addressing skills constraints, such as short-term easing of immigration regulations for tertiary qualified individuals
- Overcome spatial legacies (fast track provision of title deeds) and expand integrated public transport systems
- New compact between the government, private sector and other social partners to ensure state policies are unambiguously in the public's interest
- Stable macroeconomic policy framework will allow for flexible exchange rate, inflation targeting (low and stable inflation), credible and sustainable fiscal policy (will reduce uncertainty)

Table 1: Implementation of the above reforms suggests growth starts to ramp up in the short term and lays the foundation for growth in the medium to long term

| | Additional growth in expenditure components (% points) | | |
|---|---|---|---|
| | Short term (average over years 1–3) | Medium term (average over years 1–6) | Combined long term (average over years 1–10) |
| Absorption | 0.8 | 1.8 | 2.4 |
| *Private consumption* | *1.0* | *2.2* | *2.9* |
| *Fixed investment* | *0.7* | *1.7* | *2.2* |
| *Government consumption* | *0.5* | *0.7* | *0.9* |
| Exports | 0.8 | 0.9 | 1.6 |
| Imports | 0.8 | 0.9 | 1.8 |
| **Gross domestic product at market prices** | **0.8** | **1.8** | **2.3** |
| **Additional employment ('000, after 10 years)** | **142** | **929** | **1,011** |

Source: Based on estimates from the Modelling and Forecasting Unit's SAGE model.

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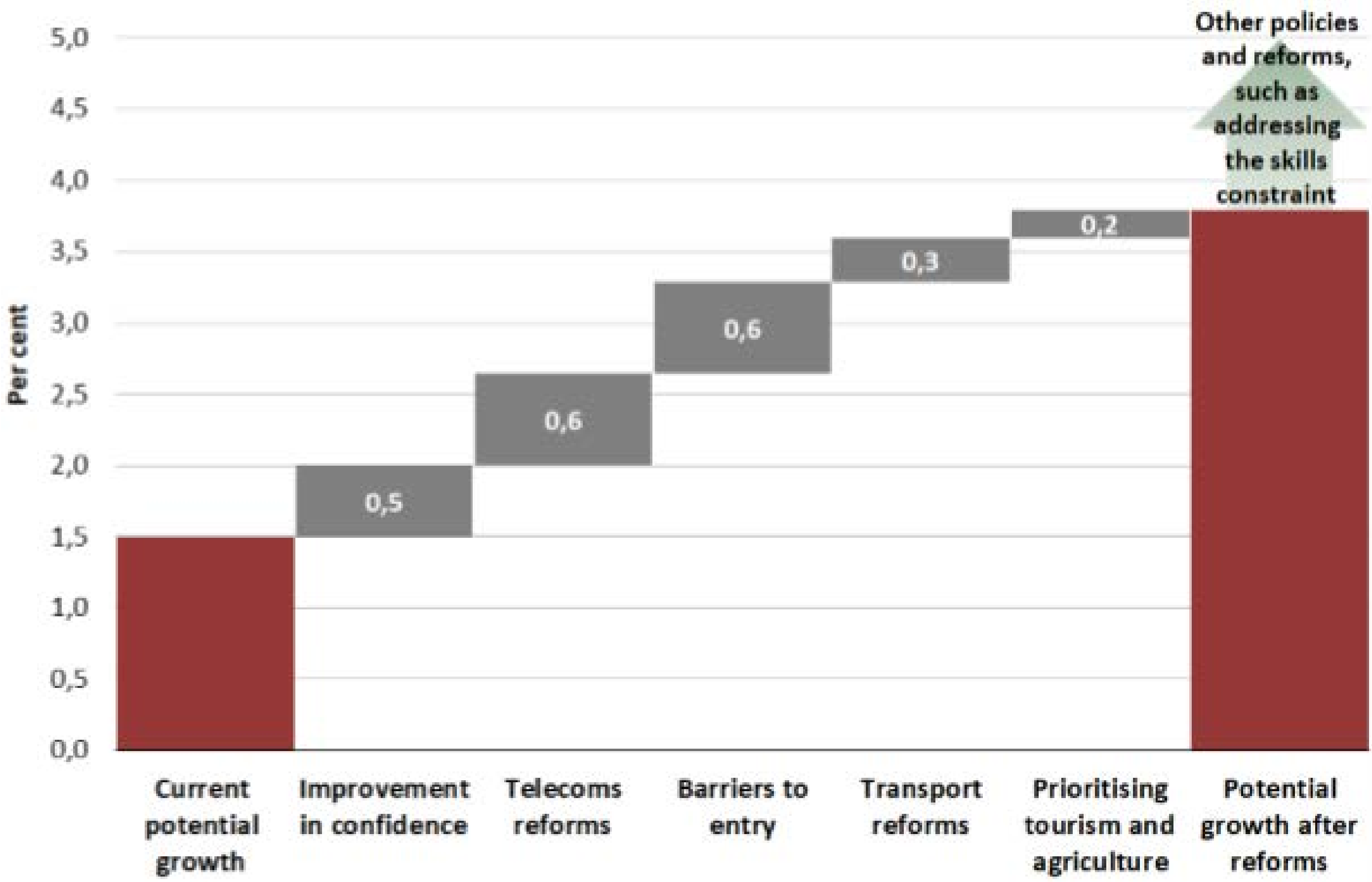
Figure 1: Execution of these interventions could raise growth potential by 2% to 3% and increase jobs by 1 million. The success of short-term reforms remains key (this chart was published in a previous Treasury budget document)




*Source: Based on estimates form the Modelling and Forecasting Units SAGE model*

## Education and labour

- Generational poverty and intergenerational inequality can be reduced through transformative education
- Comprehensive reading plan for primary learners likely to reduce reading deficits
- Investing in educational and health outcomes of the youth will render no return unless they find employment
- There has been a doubling of the wage premium for highly-skilled labour relative to the monotonic increase in the US over the last 35 years
- The cost of commuting has increased by more than inflation on an annual basis
- Low-income earners spend 40% of their income on transport
- 70% of discouraged workers cite their location as a constraint to looking for a job

Figure 2: Estimated growth impact of the above reforms by gross value add from the different sectors

| | | Deviation in growth of real value added (% points, average over 10 years) | | |
|---|---|---|---|---|
| ↓ Sector | Scenario → | Short term | Medium term | Combined long term |
| Agriculture, forestry, and fishing | | 3.8 | 5.0 | 5.0 |
| Mining and quarrying | | -4.0 | -4.9 | -5.0 |
| Manufacturing | | 3.9 | 4.1 | 4.0 |
| Electricity, gas, and water | | 1.8 | 2.7 | 2.8 |
| Construction | | 4.3 | 5.7 | 6.0 |
| Trade, catering, and accommodation | | 4.3 | 5.2 | 5.3 |
| Transport, storage, and communication | | 5.6 | 8.0 | 9.7 |
| Finance, insurance, real estate, and business services | | 5.0 | 8.3 | 8.4 |
| Community, social, and personal services | | 2.7 | 3.4 | 3.6 |

*Source: Based on estimates form the Modelling and Forecasting Units SAGE model*