UMRABULO

Issue No.2, 2nd Quarter 1997

UNDERSTANDING GEAR

Growth, Employment and Redistribution: The Government`s new economic strategy

PREFACE

This workbook outlines the government`s macro-economic strategy, as spelt out in the "Growth, Employment and Redistribution" (GEAR) document. It explains the strategy within the broad context of how South Africa`s economy works, and the major problems and challenges facing the economy today.

The first chapter looks at the history of the South African economy and how the different parts of it fit together. Chapter two discusses the major problems, challenges and opportunities facing the South African economy at present. It explains the pressures placed on government to deal with our low growth and rapidly increasing population rates, our enormous debt, and the huge unemployment crisis. In chapter three the key elements and arguments of the GEAR strategy, as set out by government, are presented.

Whilst the document offers some critical insight, its main aim is to provide the reader with a clear understanding of the strategy and the context in which is was developed. This workbook should be used by branches as a tool to analyse, discuss and debate the economic strategy. The Department of Political Education and Training has made some of the critiques of GEAR available to ANC regional offices. They are useful papers to stimulate debate.

CONTENTS

Chapter One

1. Understanding Basic Economics

1.1 People and the Economy

The economy is about how a country earns and spends its money. It is about what is produced, how natural resources are used, employment, the buying and selling of goods and services, importing and exporting goods, the value of our money compared to other countries, and much much more.

Every person living in a country affects the economy in some way, and in turn the economy affects everybody. However, this differs for different people. For example, the owner of a large company who employs workers and makes a lot of profit which s/he then invests or spends, is affected by the economy very differently from an unemployed person who earns no money and has no money to spend.

Whether we are the rich business person or the unemployed person we all have interests in the economy. But our interests are different:

- The rich employer worries about things like, keeping production costs low, not being taxed too much and making profit.
- The unemployed person is more concerned about getting a job that pays decent wages, housing, food and good health care or perhaps transforming the economy into something radically different.

1.2 Different Types of Economies

There are two main types of economies that exist in the world. These are capitalist economies and communist economies which both have different forms and have emerged in different ways.

Capitalism

There are three main types of capitalist economies in the world today. They are: social democracies, command capitalism and free market capitalism.

1. Free Market capitalism developed in countries like America under Reagan and Britain under Thatcher in the 1980s. Free market capitalism looks at deregulating the labour market which means that there would be very few laws protecting workers from exploitation. These economies look more towards casual labour than full-time employment. Unions were smashed through this process. This idea led to emplyment increasing, but

wages were much lower and workers had few benefits if any at all. There was a shift in these economies to removing the welfare state through privatisation. The state sold off its assets (the things that it owned) to private businesses and cut social spending. These economies redefined the role of the state in the economy to allow for a situation in which business could grow.

2. Commandist capitalism exists mainly in the Pacific Rim countries like South Korea, Malaysia, Thailand and Hong Kong (also known as the "Asian Tigers"). In these economies, the state has policed both labour and capital. This has meant that basic labour rights have been removed. The state has tried to direct the process of industrialising the economy. These economies were helped in their industrialisation programme by the United States of America so that communism would not spread through Asia. Commandist capitalist economies are export-led which means that there is an emphasis put on developing goods and services for export purposes. Another feature of these economies is that the state nationalised the banks to redirect savings into developing industry.

3. Social democratic forms of capitalism emerged in countries in Western Europe after the Second World War. These economies had a large welfare state which spent a lot on education, health care and social security, particularly unemployement benefits. To do this, there had to be high taxation. In these economies, there was an attempt to develop an agreement between organised labour and capitalists to ensure prices and wages did not make inflation go higher. There are debates about whether these systems are in fact capitalism or a form of socialism.

Communism

Communism also developed in different forms. There were three main forms of communist economies. There was the Soviet model, the Chinese model and the Yugoslavian model.

In the Soviet Union there was centralised planning of all parts of the economy like production, exchange and consumption. Centralised planning meant that the economy was planned at a state level. A bureaucracy of planners decided on these basic questions of investments. Workers could not choose where to work. What they earned was also decided by these planners. The state owned everything in this model.

Under Chinese communism, the state owns the majority of the economy, but there has been an attempt to include the market alongside state ownership. In some areas in China, the labour market has been deregulated. To some degree production has been decentralised to villages.

In Yugoslavia there was an attempt to find a balance between the ownership of the state and the market. We can refer to this type of economy as a kind of "market socialism". There was an attempt to put in place `autonomous worker self-management` in companies. Workers, both skilled and unskilled, would manage the company, decide on how work would be divided and money spent. In other words, workers would equally share with each other the running of the company.

At the moment the South African economy is a capitalist economy with a few big companies (monopolies) controlling most of the wealth and resources of the country.

Because of the inequalities created by apartheid our government has to play a very important role in the economy. It is up to government to decide how the money which it has, is going to be used to meet the needs of all the people of this country. No government ever has enough money to satisfy everybody. The government has to make decisions and choices about the type of economy we want. This is what the macro economic strategy is all about.

To give us a full picture of the economy we must first look at the history of the economy in South Africa.

2. How the South African Economy Developed

2.1 Early Economy

From the arrival of the colonialists to the discovery of gold and diamonds in the late 1800`s, South Africa`s economy was based on farming. There was almost no industry. The development of big mines led to the growth of big business which needed lots of cheap labour.

2.2 Early Development 1880s - 1940s

The government introduced land and tax laws which limited the African people to the reserves and forced them to earn a money wage. Cheap black labour was directed to the mines and farms which were owned by white capitalists. Mining was key to generating a modern economy. The profits from mining were used to set up finance houses which set up factories. The government budget was used to favour the white minority and the capitalists. The African people suffered a great deal.

2.3 Rapid Growth 1950s 1970s

From the 1950s onwards, the South African economy grew much faster than the population. South Africans began to produce goods which previously could only be obtained from abroad through imports. This model that guided South Africa through its boom years was called Import Substitution and Industrialisation (ISI). In order to produce these goods machinery was imported from other countries. Gold was sold at an internationally fixed price so that South Africa had a stable income (foreign exchange money that we received from foreign countries buying our gold).

As a result of these policies rapid growth did occur, but this growth did not benefit people equally. White people, in general, became richer while the black working class in particular continued to be exploited. Capitalists produced more and more luxury goods that only the white and rich sections of society could afford. Huge profits were made as the government`s policies at the time ensured a supply of cheap labour. This model relied on three factors for its success: the fixed gold price, the cheap import of machinery and a cheap and stable workforce.

2.4 Economic Crisis 1970s 1990s

From 1970 onward the rapid growth rate began to decline. This was because the ISI model broke down. It did so for three reasons:

1. In 1971, the gold price was no longer fixed and started going up and down according to how much people in the world markets wanted to buy and how much was available to be sold. This meant that South Africa no longer had a stable income of foreign exchange.

2. An international oil crisis hit the world economy in 1973 and the oil price shot up. One of the results of this crisis was that South Africa had to pay much higher prices for oil and all other imports. So while we got less income from our gold, we had more expenses.

3. From 1973 stronger union organisations were built and there was a huge increase in strikes and other labour action. This meant that employers could no longer get away with paying such low wages. Mass political activity such as the Soweto Uprising of 1976 also led to increased instability. Sanctions meant that many foreign capitalists took their investments out of South Africa. Many big South African businesses also took a lot of their money to other countries.

4. The issue of racial fordism is also linked to the failures of ISI. Racial fordism means that the domestic South African market was divided upon racial lines with black people not having the same access to the economy as white people. This meant that the domestic market for goods and services was limited and quite small.

We started spending more than we were earning. In the 1980s and 1990s the downward movement of the economy continued and South Africa faced a recession. A recession occurs when the population is growing faster than the economy. This is called negative growth.

Economic growth is measured by comparing the increase in everything that is produced (Gross Domestic Product or GDP) to the growth in population. A country`s economy is said to be healthy when the GDP is greater than the population growth. However, the GDP is a limited tool in that it cannot measure people`s wellbeing. In this period the sectors of the economy which contributed most toward the GDP namely mining, manufacturing and agriculture began to contribute much less than they had in the past. When a recession occurs unemployment increases, services are more limited and most people become poorer.

3. Four key factors that influence the economy

Now that we have a broad overview of the history of the economy, we will turn to look at some key factors that influence the economy.

3.1 The size of the economy

The size of the economy is the first important factor. We measure the size of an economy by its Gross Domestic Product (GDP). The GDP is the sum of all the goods and services produced and sold by a country`s economy in one year. The problem with the GDP is it does not include goods and services that are produced and are not sold. Such goods and services include housework and subsistence farming. South Africa has a fairly high GDP compared to other African countries, but not compared to the rest of the world.

When we look at the size of the South African economy it is important to remember that we have some very rich provinces such as Gauteng where 40% of the GDP is produced, and some very poor provinces such as the Northern Province which only produces 3.1% of the total GDP. Determining the size of the economy by the GDP does not give a clear picture of poverty in the country. Although we may have one of the largest economies in Africa, we also have one of the largest gaps between rich and poor people.

3.2 The structure of the economy

The economy is made up of different sectors. The weakness and strength of each sector is a key influence on the economy. The main sectors are:

- **Manufacturing** the production of goods in factories
- **Finance** savings held in banks and building societies that are used for investment in the economy
- **Retail** the selling of goods in shops

- **Government** spending of taxes and other government income on things like education health, housing, welfare, and policing
- **Mining** of our natural mineral resources such as gold, coal, iron, and diamonds
- **Transport** moving goods and people across the country
- **Agriculture** Farming to produce food like maize, wheat, meat, fruit and vegetables
- **Elecricity, Gas & Water** providing these services for people and industries
- **Construction** building of houses, roads, factories etc.
- **Social Services** things like private health care, and old age homes.

When people talk about the **service sector** they usually combine the following five sectors: finance, retail, transport, electricity, social and government services.

> ***What are shares***
>
> Shares are small parts of a company`s total worth. They are sold on the stock market. The value of the shares change as the profits and worth of the company changes. Anyone can buy shares that are put up for sale on the stock market. Shareholders make profits by being paid a percentage of the company profit every year. This is called the dividend. They can also make profits by selling off their shares when the value is high. Small shareholders have little influence on how these companies are run. In most companies more than half of the shares are owned by one group. They are called the controlling shareholders

3.3 Economic Growth

The third key influence on the economy is economic growth. Growth in the economy is measured by the increase in GDP compared to population growth. As the population grows, it means that there are more people who have needs and wants and the GDP has to grow to cope with this. If the GDP does not do this, as explained earlier, a recession occurs.

As the population grows each year, more people need jobs. Without a high growth rate it is difficult to create new jobs but high growth does not automatically mean that new jobs will be created. For example, the growth in the South African economy was 3.5% in 1995, but only 55 000 new jobs were created in the formal economy by the middle of that year which is much lower than the number of people seeking employment in the economy.

3.4 The population of South Africa

The size and age of the population is the fourth important influence on the economy. There are about 40 million people living in South Africa. Racially

broken down, the numbers are as follows:
African 75.8%
White 13%
Coloured 8.6%
Indian 2.6%

People classified as African form the overwhelming majority of the population. In the past most of these people were dumped in bantustans and not regarded as South African citizens who were entitled to benefit from the South African economy.

4. Important Facts about the South African Economy

4.1 Investment Crisis

Fixed investment is the money spent by businesses (the private sector) on building new factories or buying new machines. This obviously leads to new jobs being created.

Speculative investment is money spent on buying shares in existing companies. This can make profit for the companies, but no new jobs are created.

Over the past ten years less money has been spent on fixed investment. In 1988 investment was R39 billion. This is R10 billion less than it was in 1981. This means that fewer jobs are being created while the population is increasing.

In some cases people have lost jobs when factories have had to close down because worn out machines are not replaced. Bosses prefer to use their money to buy shares or other companies. This does not create jobs.

4.2 The Monopolisation of the economy

In South Africa few companies control most of the economy. The mining companies used their profits to set up finance houses. The finance houses used their money to set up the manufacturing sector or to buy out existing companies. In other words, there were very few people who owned most of the economy. This situation still exists today.

In the years when the economy was growing, these monopolies had lots of spare money (reserve capital). During the economic crisis, these companies made profits by buying shares in other companies that were affected by the recession.

Today there are seven major companies in South Africa that control over 80% of the shares on the stock exchange. This concentration of power allows them to have great influence over the economy. They have the power to cripple the economy by not investing, by setting high prices, or by deciding what will be produced, how it will be produced and who will benefit. They are motivated by the need to make profit and do not need to work in the interests of the people.

4.3 Uneven development and distribution

The South African economy is not equally distributed and developed. Monopolies are a good example of uneven development. Another striking example is the distribution of land. Under the apartheid government 85% of the land was owned by white people, while only 15% was owned by black people. The best land for farming was owned by whites.

South Africa has one of the biggest gaps in the world between what rich and poor people earn.

- The poorest half of South African households earn less than 10% of the total income earned by South Africans.
- The richest 10% earn more than half of the total income.

4.4 Trade International Relations

International trade is about importing goods and services to South Africa and exporting goods and services from South Africa. Many countries buy goods and services from each other. From its early development South Africa relied on the export of raw materials such as coal, gold and diamonds. It also depended on the import of manufactured products, machinery and technology. The table and picture below show the total value of exports and imports from 1989 to 1993. Over the years the costs of raw materials has decreased whilst the cost of manufactured goods has increased. This is a problem for South Africa because we now have to pay more for imports but we get less money from our exports. It also means that we are not earning enough foreign exchange. This makes it more difficult for us to buy expensive machinery from overseas that could make our economy grow and create more jobs.

Year	Import Rbillion	Export Rbillion
1989	58.7	44.4
1990	60.9	44.1
1991	64.4	48.2
1992	66.8	52.9
1993	78.5	59.7

R1 billion is one thousand times R1 million.

5. The role of the government

Government has a major role to play in the economy. It has to address the needs and wants of the various sectors of the population. The government contributes about 15% of the economy`s GDP. The major source of income for the government is tax. Companies and individuals pay taxes to the government. Under the old system there was a very uneven way of taxing with ordinary people paying most of the tax rather than the big companies.

What is a budget?

A budget is not a very difficult thing to work out. It is perceived by many as an inaccessible document that only special experts can organise. However, everyone has their own personal budget. This means that if you work and receive R1000 a month, you have to see what your expenses are and what you are going to spend the money on every month. For example:

Stella earns R1200 a month. Her rent is R250. She has to spend R300 on food for herself and her daughter. Lights and water costs R50. Her transport costs to and from work each month is R75. Her daughter`s school fees are R150 a month. She has to pay the interest on the money that she owes on her Truworths account which is R20. The total expenses therefore are: R840. This means that Stella has R160 left over after all her expenses are paid. Stella must then decide what she wants to do with the left over money. She can buy clothes with it, furniture for her house, put a down payment on a TV etc. or she can open a bank account and save the money.

The budget for a town or city, province or country works on a similar principle. There are certain expenses that a government has to pay. Those expenses include labour costs, running the offices, paying their debts, providing services to people etc. The way in which a government makes money is through taxes from companies and individuals, investments that the government may have made and through parastatals. From the government budget, a decision must be made as to what to spend extra money on. Should it be spent on building houses? Should it be spent on education? Should it be spent on health care? There are many things that the government can spend money on. But the budget for government is limited, just like Stella`s budget is limited. So choices must be made. Money and resources must be spread to provide as much as possible, the best quality that is possible to as many people as possible.

What	**Budget (R million)**	**Percent (%) of total**	**Percent (%) of GDP**
Social Services	***88600.9***	***46.9%***	***14.2%***
Education	40 270.5	21.3%	6.5%
Health	20 223.4	10.7%	3.3%
Social security and welfare	18 433.2	9.8%	3.0%
Housing	4161.9	2.2%	0.7%
Other (recreation & culture, sewerage & sanitation, community development)	5512.0	2.9%	0.9%
Protection Services	***29 620.5***	***15.7%***	***4.8%***
Defence	10 716.4	5.7%	1.7%
Police	13 085.8	6.9%	2.1%
Prisons	3 866.8	2.0%	0.6%

Courts of Law	1978.6	1.0%	0.3%
Economic Services Transport & Communication Agriculture Water and related services Export trade promotion Other (Manufacturing, regional development, tourism, labour services, multi-purpose projects)	***18 885.2*** 7 320.8 4 519.1 1 863.1 1 427.8 3 754.4	***10.0%*** 3.9% 2.4% 1.0% 0.8% 2.0%	***3.0%*** 1.2% 0.7% 0.3% 0.2% 0.6%
General government Services (foreign affairs, general research & other government services)	***13 217.6***	***7.0%***	***2.1%***
Interest	***38 549.8***	***20.4%***	***6.2%***
Government Enterprises	***48.5***	***0.0%***	***0.0%***
Subtotal Plus: Expenditure not yet classified	***188 922.6*** 1 229.4	***100.0%***	***30.4%*** 0.2%
Total estimated expenditure	**190 222.0**		**30.6%**

Source: Central Statistical Services

5.1 A Summary of the South African Budget for 1996/1997

Both national and provincial budgets are worked out by government each year. Below is a table that shows what national and provincial government expenditure together was in each sector for 1996/97. The government`s total estimated expenditure for this period is R190 222 million. The table shows how much is spent on different sectors.

Government also receives money or revenue from it parastatals. A parastatal is a company in which government is the major shareholder (the largest owner). Examples of the major South African parastatals are Denel, Telkom, Transnet and Eskom. Government gets money from these parastatals through taxes and dividends. For example in 1996 the government got R900 million from Telkom. The government decided not to take money through taxes from Eskom as this would make the delivery of electricity to local communities much slower. In this instance National Government decided it would be better to leave that money with Eskom so that it could spend it on its electrification programme.

It is up to those in government to decide how its money is spent. The government prepares a budget for a year to show how it will spend this money. The way that the government chooses to spend money is a clear sign of where its priorities lie. Under the apartheid government a huge part of the budget was spent on defence and the bantustans. The priorities of our government are very different now and most of the spending is on social services such as education, health, social security and welfare, and housing.

The next section of this manual considers the problems and challenges of our present government as it tries to address these priorities.

Chapter Two

Problems and opportunities in the South African economy

1. Introduction

In the first chapter we looked broadly at what an economy is and the history of the South African economy. This chapter develops upon the last chapter by looking at what problems we face in the South African economy and what opportunities there are for the growth and development of our economy.

2. Problems

The ANC-led government has to look at all the problems in the country and come up with a coherent plan to solve them. We have to look at many factors when considering the problems in the economy that do not allow growth to occur, do not create jobs and do not allow the redistribution of resources around the country. Some of the problems can be solved by government and others cannot. But our government can try to create the conditions that are necessary to help solve the problems that we face.

The problems in the economy that we face relate to: development and growth; the debt and the deficit; the size of the civil service; growth; the currency; foreign and domestic investment; job creation; exports, imports and the balance of payments; research and development; productivity; lack of skills; and small production runs.

These problems will be briefly and broadly discussed below.

2.1 Development and growth

Development is very unequal in South Africa because of the apartheid policies of the past. The budget drawn up by the government has to address this and spend more money on the poorer sections of our population. Since there is not more money available than in the past, we have to reprioritise spending. This means cutting money from some existing programmes and spending it on new ones.

Our population is growing faster than the economy. This means that hundreds of thousands of young people who are new to the job market each year will not find jobs. At the moment, half the people in South Africa are under the age of 25 and the problem of unemployment will grow. Growing unemployment exists in the context of an already very high rate of unemployment in the country. The unemployment rate in South Africa today is estimated at being between 38 to 40%.

The less employed people there are, the less money the government receives through taxes. At the same time, more money has to be spent by the government to look after the poor. This puts more pressure on the budget to provide for education, health, welfare and housing.

2.2 The debt and the deficit

In their desperate efforts to cling to power, the previous National Party government went on a mad spending spree in their last few years in office.

They did not have enough money, so they overspent on their budget and had to borrow billions of rands from the banks. The new government has to pay back those apartheid debts. If we do not pay back those debts, no-one will ever trust us again if we want to borrow money in the future for development. Also, most of our debt is internal which means that money was borrowed from South African banks. The money that they lent to the government belongs to ordinary people. It is their savings, pension funds and insurance policies. If the government decides not to pay back the debt, many banks will collapse and people will never get their money back. However, there have been negotiations and campaigns to cancel the debt. For example, President Mandela has cut a large portion of the Namibian debt to South Africa on a moral and political standpoint because this debt was apartheid and colonial debt.

At the moment we are just paying back the interest on the debt. The actual debt is staying the same. In the table on the government`s budget we saw that R34,4 billion was spent in the 1996/97 financial year out of a total budget of R173 billion to just pay off the interest on the debt. Paying the interest on the debt is called "servicing the debt". If we can make the debt smaller by paying off some of it, the interest will be lower and we will have more money to spend on development and transformation. At present, millions of rands are diverted from social programmes to service the debt.

It is very tempting for the government to borrow more money in order that we deliver faster. We have been offered many loans. However, for every R1 billion that is borrowed, R120 million has to be paid in interest every year.

Because of our huge debt, we do not have enough income in our national budget to cover the expenses that we have.

We will have to spend more than we have. The difference between what we have and what we spend is called the deficit. In the budget year 1996/1997 the government expects to earn about R145 billion and spend R173. This means that its deficit will be about R28 billion we will have to borrow that to survive. The new government has started trying to make this deficit less. If it manages to meet its aims for 1996/1997 it will have reduced the deficit by nearly 1% in a year. Part of the government`s new economic strategy is to reduce that deficit to 3% of the GDP by 1999.

Borrowing leads to more debt and more interest for the next year. If we had no debt we would not have a deficit, no money would be wasted on paying the interest on the debt and could instead be spent on the people.

2.3 Size of the civil service

The biggest expense of the government is to pay salaries to civil servants. The government employs about 1.3 million people. Most of these people work as teachers, nurses and police. We have too many civil servants because of the bantustan policies of the previous government and the number of departments that had to be duplicated to run the Apartheid system.

If we can cut the salary bill of civil servants we will have much more money to spend on development and delivery. We can afford to have only 1 million civil servants which means we have to cut the civil service by 300 000. The process of creating a leaner civil service is called "rightsizing".

The process of rightsizing is difficult because some parts of the civil service cannot be reduced at all. At the moment 700 000 out of the total number of civil servants are teachers, health workers and police. We cannot cut their numbers. So we have to cut the other parts of the civil service and cut 300 000 jobs out of the remaining 600 000 that exist.

2.4 Growth

The only way for the government to get more money is through growth in the economy. If more jobs are created there are more people paying taxes to the government. More people also have money to look after their own needs. This means that less people are dependent on free services and support from the government.

If there is greater production then companies make more money and pay more tax, which again represents increased revenue for the government.

Manufacturing more local goods will mean that the country has to import less. In addition, if we can produce goods locally for South Africa to export, the country will earn more money.

2.5 Currency

Our country`s unit of money, the rand, is called our currency. The value of our currency is set by comparing its buying power with other countries` currencies on the international markets. We usually compare our currency to the United States dollar.

For the first half of 1996 we had a currency crisis. The value of the rand fell fast against the dollar. This affects our imports very badly. In January a farmer could import 4 tractors for R1 million. By June, a farmer could buy 3 tractors for the same R1 million. Government expenses were also badly affected. For example, if we had to pay R30 million interest on a foreign loan in January, in June we would have to pay R38 million for the same loan.

There were a number of reasons for the currency crisis:

- Rumours about Madiba`s health made people who buy shares on international markets nervous about future stability in South African politics;
- The Minister of Finance, Chris Liebenberg, resigned and was replaced by the first black ANC finance minister, Trevor Manual. This made them even more nervous;
- The South African Rand was actually valued at more than it should have been through government policy controls;

The government had no clear economic plan. Business and the union federations (Cosatu, Nactu and Fedsal now Fedusa) had published two different documents on the economic strategy that government should follow. Nobody was certain about which path the government would take.

All these factors led to a currency crisis. Our own business people lack confidence in the government and panic easily. The people who buy and sell shares on international markets also panic easily. When the rand started falling in value, they became nervous and sold their shares. The more people sold, the lower the value dropped. In other words, there were more people who wanted to get rid of their shares than people who wanted to buy them. The Reserve Bank stepped in and began buying rands. This slows down the fall of the rand. But the Reserve Bank had to use some of our foreign currency reserves to do so and could not spend more than we had.

The only real thing that the government could do was to come up with a clear plan for the economy as soon as possible. That is one of the reasons for the fast development of the Macro-Economic Strategy.

2.6 Foreign and Domestic Investment

An economy can only grow when more goods are manufactured. Money has to be invested in new factories, better machinery, research and development of new products. As we saw in the budget section, the government has no money to spare and cannot invest much with the money available.

Investment has to come from two main sources:

- Banks and finance companies that hold other people`s money such as pension funds and insurance money. They must look for a way of investing the money that will make good profit for their customers; and
- Businesses that make profits and can invest these profits in making their business bigger.

Both the banks and the businesses can be local or foreign. We have seen in the previous chapter that the biggest problem with current investment is that most investment is "speculative". This investment can leave the country very easily. When there is panic, investors just sell their shares and take their cash out of the country. This type of investment also does not directly influence job creation.

The type of investment that we need for long-term economic growth is investment in expanding production and creating jobs which can happen if we develop new factories and new small businesses. The total of such investments is called Gross Domestic Fixed Investment. The people who invest this money cannot just take the cash and run when they are concerned about the economy.

There is lots of local money inside South Africa. Hundreds of billions of rands are invested by the people in insurance houses, pension funds and banks. In the end we must try to get this money invested in ways that will grow the economy.

2.7 Job creation

For the economy to grow in a way that really improves the lives of people, new jobs must be created.

It costs a lot of money to create jobs in high-tech industries such as chemical and electronics industries. These are the types of industries that we have to develop to become internationally competitive. The costs that go into creating jobs include things like buildings for factories, machinery, research and training of staff. The more sophisticated the industry, the higher the costs of setting up a new factory. Jobs cannot be created in this sector without huge investments from local and foreign business.

It is much cheaper to create jobs in sectors like clothing where the training and technology costs are low. However, clothing is not a competitive industry. At the moment we can import cheaper clothes from overseas and our own clothing industry is shrinking. Farming is another sector where it is cheap to create jobs, but farmers are generally employing less people and using more machinery. At the moment, the informal sector is the biggest provider of new jobs in our economy.

2.8 Exports, imports and balance of payments

The balance of payments is the difference between what you import and what you export on the international market. If we import more than we export we have a bad balance of payments because we are spending more than we are making.

Most of our exports are:

- raw materials like steel, coal and precious metals.
- agricultural products often in their raw form like fruit and wool

We export huge sums of raw materials at a cheap price. Often these raw materials go to other countries where through manufacturing they are turned into expensive products that they then sell back to us at a very high cost. For example, we export gold which is then made into fine jewelry which we import back into the country. Why do we not just manufacture the jewelry ourselves? The same goes for steel that we export and then import back in the form of costly machinery.

Most of our imports are:

- machine parts
- electronics goods (computers, television, microwaves, etc.)

We have to take our raw materials and add value to them before exporting them. An example of this would be to cut the diamonds that we mine before we export them so that we can sell it for more money at the same time as creating jobs. This is called beneficiation which will require that factories are built, workers are trained and jobs are created.

2.9 Research and Development

Compared to other countries we spend too little on developing new products and methods. During the time of sanctions South Africa was a closed economy without much competition. Business was not forced to come up with better and more efficient ways of producing goods and services.

If we want to develop our manufacturing sector and compete with other countries, we have to spend more money on research. Some of this work can be supported by government. Universities and technikons have to be used and the business sector must also do its own research and development.

2.10 Productivity

Compared to other successful countries, South Africa has a low productivity level. Productivity is measured by comparing the cost and the time it takes to produce the same thing in a particular industry.

Low productivity is not just caused by people not working hard enough. Skilled management is needed to make a workplace more productive. Development and training programmes for workers must be used to increase their skills and efficiency. Worker participation in setting targets and standards will help to transform a workplace. In many countries rewards are also used so that increased productivity has clear benefits for workers.

2.11 Lack of skilled workforce

The vast majority of employed people in South Africa are unskilled or semi-skilled workers. We have a serious shortage of skilled technicians and managers. Under the apartheid system the full potential of only a small part of our population was developed and we inherited a white and male dominated management sector. Many managers of companies have MBA degrees or are chartered accountants. At the moment there are 16500 chartered accountants in South Africa, 79 of them are black and of these only 20 are African.

Every business needs technical people, people like electricians, mechanics, computer operators, accountants, etc. They usually have diplomas from technikons rather than degrees from universities. A few technical people are needed to back up any professionals. For example, an engineer (with a university degree) in Europe is usually backed up by 6 technicians. This means that engineers can concentrate on design and planning which the technicians can implement under their supervision. In South Africa the rate is one engineer to one technician. This means the highly skilled engineer has to spend time doing simple tasks that could have been done by a technician. Part of the reason for this imbalance is that most people go to university for further study rather than to technikons.

The workers of South Africa lack skills compared to more developed countries. This problem must be addressed through in-service training and skills upgrading of the existing workforce as well as through Adult Basic Education and Training (ABET) programmes. We also have to invest in the education of the next generation. At the moment only 40% of people who start school, matriculate. Almost all forms of technical or professional education need a matric certificate. This means that at least 60% of the new people looking for jobs each year do not have any qualifications.

By international standards the government is spending a big enough part of the budget on education. Ways must be found for the money to be used more efficiently so that our citizens end up with the type of education that will make the biggest possible contribution to a better society and a strong economy.

The vast majority of unskilled and unemployed workers are women. This means that women are marginalised in the economy and will remain the poorest of the poor. Equal rights in our Constitution will not change the lives of women unless something is done to change their economic position.

2.12 Small production runs

For many years South Africa was a closed economy where most of the manufacturing was aimed only at a local market and at making products which we could not get because of sanctions. Local companies survived because the previous government protected them from international competition. But it is very expensive to produce a small amount of any product, for example to produce one model of a car.

We have many different types of cars produced here and each type has many different models. For each model you need a whole production line where all the machinery is adapted and changed for that model. This costs a lot and adds to the price of each car.

3. Opportunities

3.1 Global Position

Our place on the world map puts us very far away from the big markets of the United States, Asia and Europe. In spite of this we are in quite a good position in the world economy.

Since the peaceful elections of a democratic government in 1994, the whole world has had a very positive attitude towards South Africa. We proved that negotiations can work and it is important for international politics that things work out in South Africa. We will get a lot of help from other governments and they will encourage investment here.

We also have a real democracy with a strong constitution. This makes us a politically stable country. Our well developed rail and harbour system makes it easy for us to transport goods for export.

We also have very good access to the rest of Southern Africa through roads and railways. Countries like Botswana, Lesotho and Zimbabwe have no access to the sea. The rest of the world needs to use our harbours to get access to a Southern African market.

3.2 State Assets

Our state assets are worth billions, but are stuck in enterprises that do not make a profit for the state. It often costs the state money to maintain its assets such as Telkom, Eskom and Transnet. These assets are often badly run and are not profitable. Our government needs to decide which assets it should be running and whether it needs to restructure or privatise some of these assets. The GEAR strategy looks at this question.

3.3 Huge Informal Sector

The informal sector is part of the economy that is not governed nor supported by formal regulations, structures or laws. Very small businesses like street hawkers and corner hairdressers, backyard mechanics, shebeens and spaza shops are all part of this sector. In some informal settlements you can get everything from bank loans to funerals through the informal sector.

The informal sector provides about 1.7 million jobs in our economy and is the only part of the economy that has really grown in the last ten years. It has grown more than all the other sectors put together. Conservative estimates state that goods and services from the informal sector contribute about 5.5% to South Africa`s overall GDP. More recent estimates from a household survey, however, say that the contribution is actually as much as 15%. Because of the nature of the sector, it is difficult to get an accurate figure.

Although this sector forms such a large part of the economy in terms of the money that it generates, almost nothing is paid to the government in tax. Because the informal sector is not regulated and controlled like other parts of the economy, the government cannot easily get tax from this sector or subtract tax from the wages that they pay.

This sector must be brought into the formal tax system by better indirect taxation, for example through value added tax (VAT) and petrol tax, which informal traders pay for buying and transporting goods. More support must also be given to the informal sector through advice services, training and loans.

3.4 Raw Materials

South Africa is the world`s richest nation in terms of the amount of different minerals and raw materials we have. We also have a good variety of agricultural products and if our farms become more productive we can export much more.

Our natural environment is unspoiled and our beaches, game and nature reserves and mountains are a big national asset. If we can protect the environment and use it wisely we can increase tourism to South Africa.

In some parts of the country, eco-tourism can be developed as an industry and create many new jobs. Tourism is also a great source of foreign currency for the country and leads to job creation in other sectors like the service sector and the transport sector.

3.5 Service sector and communications

Compared to the rest of the continent we have a very well developed service and communications network. Both of these are very important for economic growth.

3.6 Transport network

This is well developed and is crucial as it allows us to move essential goods. South Africa has a good road, rail and port infrastructure. It is also currently creating much development through the expansion of corridors, such as the Maputo Corridor.

3.7 Electricity and Water

Industry and agriculture are the biggest users of electricity and water. Reliable and adequate supplies are essential for economic growth. South Africa can generate enough electricity to provide for a much bigger economy. In the last few years electricity has been brought to most parts of the country which makes economic development in rural areas much easier.

Water is more difficult to provide since it cannot be produced. It can only be stored in times of rain and saved in times of drought. The government has now introduced new policies and laws to make sure our water resources are managed better.

Chapter Three

The GEAR strategy

1. Introduction

In the last two sections we looked broadly at how the economy works and what the problems and opportunities are for the South African economy. It is in the context of an analysis of these factors that the government produced a Macro-Economic Strategy (MES) for South Africa called Growth, Employment and Redistribution (GEAR), which are the key components needed to make our country succeed.

Towards the end of 1995, it became apparent that if the economy continued to grow at around 3%, as it was likely to do if no changes were made to the way it was working, government would not be able to deliver what it said it would in the Reconstruction and Development Programme (RDP).

Two alternatives for South Africa have been described as the "Low Road" and the " High Road". The "Low Road" suggests that if the new government maintained the old economic system, with a continuing trend of about 3% growth rate per year, the long term outcome would be rising unemployment, limited scope for social spending and at the end of the day, increasing social discontent. The "High Road" suggests a strategy for economic growth and development which targets 6% economic growth and the creation of 400 000 new jobs per year. For the government to deliver on its promises to the people, it needed to implement a strategy that would take South Africa along the "High Road" of economic growth and development.

It is within this context that the Minister of Finance, Trevor Manuel, presented a macro-economic framework, "Growth Employment and Redistribution" (GEAR) to Parliament on 14 June 1996. The strategy seeks to get the South African economy onto a new path, one that will ensure:

- a competitive and fast-growing economy which creates enough jobs for all work-seekers;
- a redistribution of income and opportunities in favour of the poor;
- a society in which sound health, education and other services are available to all;
- an environment in which homes are secure and places of work are productive

These are the same goals which underlie the RDP. What GEAR does, is to set out clearly the key economic plans for achieving these goals.

2. The Macro-Economic Strategy

At the heart of GEAR are two core strategies. Firstly, the framework looks at promoting growth through exports and investments. Secondly, it intends to promote redistribution by creating jobs and reallocating resources through the budget.

Growth through exports and investments

This core strategy strives to create the desired growth by changing the economy to increase the amount of goods and services that are exported, particularly in the non-gold sector. This involves the creation of a good and stable domestic environment to encourage domestic and foreign investments in South Africa.

Redistribution through jobs and the budget

This core strategy strives to redistribute the wealth of South Africa by ensuring that more and more people have access to jobs and are able to participate in economic activity. This strategy also places an important responsibility on government to redistribute wealth by reforming the budget thereby making adequate provision for essential services like water, housing, education, social services and health. These two core strategies are dependent on one another. The country needs economic growth to increase the amount of resources available for the development of its human potential. The core strategies are also interrelated, because investment in South Africa will promote jobs, and jobs will mean that people have more money to spend on goods and services, which will in turn promote further investment.

2.1 Some Features of the two core strategies

2.1.1 Fiscal Policy

Fiscal policy refers to the tools, instruments or methods that government can use to influence economic activity. It relates to how government collects its revenue and how it spends this money. GEAR looks at three factors of fiscal policy:

Sharpened focus on budget reform

The budget is the main tool that is available to government to focus the spending of departments, and for government to redistribute wealth. In the past the whole budget was focused towards satisfying the interests of a small minority of people in the country. To correct the inequalities of the past, the new government has refocused the budget to spread the resources in a more equitable or fair way.

A faster reduction in the fiscal deficit

As we saw in section 2, a fiscal deficit means that the government spends more money than it receives. This then means that it has to borrow money to pay for the extra spending. It borrows either locally, or from international sources. This is bad for the country because the government will have to repay the loan amount as well as the interest on that loan. This means that less money is available to government for housing, social services and education. At present, government borrows money at an interest rate of 16%. We saw in the last section how much it costs just to pay back the interest on the debt. Government borrowing in the domestic market is bad because it means that less money is available for private individuals or companies for investments which will be able to create jobs. Another negative aspect of government borrowing too much is that the demand for credit increases, meaning that the interest rate increases.

For these reasons government has decided to reduce the fiscal deficit to 4% of the GDP in the 1997/98 budget and to 3% by the year 2000. This means that the government will have to be more disciplined and spend less. However, government has stated that it will not cut down on spending for essential services, but it will cut down on wasteful expenditure.

Public Service Restructuring

In the last section we discussed that the previous government needed a huge bureaucracy to maintain apartheid. This led to huge wastage and inefficiency. The new government has therefore decided to restructure the public service. This means not only reducing the size of the public service, but changing it so that it meets the needs of all the people. By reducing the size of the bureaucracy, less money will be spent by government on salaries, which will help reduce the budget deficit and make more money available for housing, education, social services and health.

In this regard it is important to look at a recent report of the Attorney-General which stated that in KwaZulu/Natal alone, R1.36 billion per year has been spent in paying "ghost" employees. It is instances of waste such as this that government is committed to removing.

2.1.2 Monetary Policy

Monetary policy relates to the instruments, tools or methods that government uses to influence the value of the currency and prices. The government does this so as to ensure stability in the financial markets. The two main objectives of monetary policy are to reduce the rate at which prices increase (inflation), and to maintain a stable exchange rate. The objective of maintaining a stable exchange rate wants to ensure that the value of the rand in relation to other currencies (for example the American dollar) is kept at a fairly constant rate.

Inflation

Inflation is the rate at which prices increase. GEAR strives to keep the inflation rate low. A low and stable inflation rate is important because it provides stability in the financial markets, which will encourage investments and will promote the creation of more employment opportunities.

Stable competitive exchange rate

The exchange rate, managed by the South African Reserve Bank, is the value of the rand in relation to other currencies. For example, if a South African citizen wants one American dollar, s/he must pay more than four and a half South African rands (R4,50). GEAR strives to maintain a stable and competitive exchange rate which is important for South African importers and exporters because it provides stability when dealing with foreign consumers.

The gradual relaxation of exchange controls

Exchange controls are measures that prevent people from taking their money out of the country. Since the 1970s there has been a general relaxation of exchange controls in most countries. Presently there are only about 10 countries with exchange control measures. In South Africa, exchange controls were introduced in the previous regime. However, these controls are expensive to administer and have not been effective in preventing money from leaving the country. Exchange controls also prevent currencies from getting their true value in relation to other currencies. When a country is unable to maintain a stable and competitive exchange rate, this is negative implications for export-led growth. GEAR therefore sets as its target the gradual relaxation of exchange controls.

2.1.3 Trade and Industrial Policy

Trade policies are measures that are available to government to either help or limit trade between countries. For example, a government may impose a tariff (a tax) on foreign imports which then favours domestic producers over their foreign competitors. This means that foreign goods will become more expensive and will inhibit trade. In the past, the apartheid regime added tariffs to increase the costs of imported goods that were the same as goods produced in South Africa. Industrial policies are measures that government uses to promote the development of factories, new production methods and technological improvements.

Trade Policies

GEAR strives to provide a healthy environment for trade by gradually removing the barriers that inhibit trade between South Africa and other countries. Removing these barriers encourages efficiency of domestic producers because they will compete to produce cheaper goods, which ultimately benefits all of us, the consumers.

Industrial Support Measures

GEAR provides for measures that will support the development of industries, for example, the introduction of a tax holiday scheme which will encourage new investments in manufacturing. Moreover, GEAR seeks to encourage the production of non-gold exports, so that these might represent over 10% of GDP by the year 2000. Small and Medium-size enterprise development

The government sees the small and medium-size sector as an important sector that will promote the creation of jobs. GEAR strives to provide incentives to encourage the development of this sector. For example, government wants to develop institutions to provide financial and other assistance (advice, training etc.) for small and micro-enterprises.

2.1.4 Public Investment and Asset Restructuring

Public investment deals with government investments in land, buildings and infrastructure. Asset restructuring is about the way government companies or corporations (parastatals) are managed, controlled, regulated and owned. In the South African case, GEAR proposes a growth in public investment.

Public investment in infrastructure

An important component of GEAR is to accelerate investment in infrastructure. Investment in infrastructure will involve the construction of roads, grid electricity, sanitary facilities, hospitals, schools, water, pipelines, railways and harbours. Public investments in infrastructure improves the quality of life of people and also contributes towards economic growth.

A backlog refers to what is lacking and still needs to be developed. The backlog in infrastructure is estimated at R170 billion. The government recognises that it will have to co-operate closely with the private sector in meeting these demands.

Asset restructuring

GEAR recognises that asset restructuring will have to take place within the context of the National Framework Agreement that government entered into with labour. Asset restructuring may involve the total sale of the assets, a partial sale of the assets or sale of the asset while government still holds a small but strategic share. Asset restructuring also deals with the way assets are managed, controlled and regulated. For example, the proposed sale of a part of Telkom to an equity partner has been made conditional on a proportion of these shares going to the disadvantaged. Money raised from the sale could also be used to get rid of state debt, to invest back into the asset itself, or to finance other infrastructure. The restructuring of state assets should not be interpreted as an issue of the state withdrawing from participation in the economy.

2.1.5 Labour Market Reform

Labour market reform is concerned with such issues as relations between employers and employees, wages and training.

Structured flexibility in the labour market

GEAR states the need for structured flexibility within the labour market. In a recent report the International Labour Organisation stated that there was already a large measure of flexibility in the South African labour market. In this context a labour market policy supporting a growth path that will create jobs for the unemployed is under discussion. These matters still have to be discussed with the government, labour and business with the final discretion laying with the Minister of Labour.

Training

Training, the development of skills and improving productivity, is an important component of GEAR. The government is currently investigating the possibility of introducing a levy system that will make it compulsory for businesses to provide training to workers.

2.1.6 National Social Agreement

The activities of government, business and labour impact heavily on economic development. For example, if government spends more money than it receives, the deficit will increase, more money will be paid towards interest repayments and less money will be available to government for social spending. If business, for example, pays workers too low wages, then families will have less money to provide for their children with adequate schooling, clothing and food. If labour demands excessive wage increases, then this could cause higher inflation and the average person will be able to buy less with his or her money. The activities of government, labour and business are thus very important, and it is within this context that GEAR strives to encourage closer co-operation between these sectors. Closer co-operation between government, labour and business is not easy because this requires sacrifices from all sectors. However, closer co-operation is an absolute necessity for long term economic growth and development.

Conclusion

GEAR is a broad macro-economic policy framework which sets targets for government, for example, a 6% sustainable growth rate and the creation of 400 000 jobs per year by the year 2000. Its main objective is to create a new economic system that will ensure the rapid economic growth and development of the people of South Africa. The government is sure that GEAR will change the path that the South African economy is on from a slow growing and non job-creating economy, to a dynamic, fast growing, job-creating and development-orientated economy.

Critiques of GEAR

The purpose of this workbook is to provide a broad understanding of the historical context of the South African economy within which GEAR was developed. Many critiques have been leveled against GEAR since its release. A general indication of what these critiques are, are outlined below. For further reading ANC regional offices will be supplied with additional documentation.

Redistribution is a secondary outcome of growth and employment generation. The document relies on market oriented policies which assumes that everybody has equal access to the market. This is not the case in a capitalist economy like South Africa.

The document relies on a trickle down approach to the economy. Trickle down means that in a capitalist system the accumulation of resources will eventually reach most people in the country, or will slowly trickle down to most people who will benefit from increased production and growth. This has not been the case.

The document does not fully deal with the fact that in world trade competition is neither free nor fair.

The strategy looks at deficit reduction as primary accepting current political and economic constraints. The document seeks to reduce taxes rather than setting a framework for taxation that will increase the amount of money that government makes.

Existing structures of production and ownership are accepted with middle and upper income earners benefiting from tax reductions while the working class have to accept wage restraint.

The document says that the South African debt is too high when in fact it is low in comparison with advanced capitalist economies.

Financial and exchange control liberalisation is assumed to create private sector investment. Examples from China show that government intervention is very important in creating the foundation for profitable industries rather than having a completely open market.

Liberalising exchange controls makes South Africa more vulnerable to foreign capital flows.

If industrial development can only happen through investments by private companies, then the government can be held to ransom in the economy.

GEAR proposes a social accord. Central to this social accord is wage restraint by the working class while middle and upper income earners continue to increase their income. The result will be a bigger gap between what the working class earns (the majority of people in this country) and what the professionals, managers and bosses earn. This contradicts the RDP objectives.

- Export led growth strategy will benefit capital intensive and high skill industries, while in labour intensive industries workers are being retrenched and factories are closing.
- Liberalising trade lowers inflation but it makes imports cheaper than domestically produced products. This leads to the closure of factories and/or job losses.

SOURCES

Our Political Economy: Understanding the Problems A handbook for COSATU shop stewards (COSATU: JHB, 1992)

A User`s Guide to the South African Economy - Compiled by TURP (Y Press: Durban, 1994)