

# Development held to ransom?

Economics has been placed fairly low on the agenda of political negotiations. Debate on development is often reduced to issues of timing and priorities, with a substantial lobby for the "politics first" approach. Idasa's economics specialist WARREN KRAFCHIK argues that without economic restructuring a political settlement may be jeopardised.

**I**N THE negotiations over South Africa's future, economic development has often been relegated to a secondary role. Where important development forums or projects have been initiated they have often been scuttled or delayed by dominating political objectives. Yet, very few people across the political spectrum would deny that if we do not go a significant way to materially enriching the popular expectations of the disadvantaged the stability of the transition will be seriously threatened.

On one level South Africa enters the 1990s in a reasonable macro-economic position. It has substantial advantages, some of them earned at considerable cost over the past 10 years. Levels of foreign debt have been lowered considerably by the standards of any developing country. Debt repayments are no longer a drain on economic activity and the country has the potential to become a first-class borrower, if need be. The country has also shown itself able to run and sustain a positive trade balance, despite persistent low gold prices. In addition to this one can add the possibility of a small post-sanctions dividend in the form of increased exports and cheaper imports. This possibility is enhanced by the "locomotive" effect of expected increased growth in the industrial economy over the next 12 months. However, these positive, short-term indicators represent fragile advantages and are easily squandered. It must be stressed that the South African economy is not equipped to take advantage of this potential. The three major problem areas that continue to face the country are poverty, growth and inflation.

## POVERTY

Absolute poverty is endemic in South Africa. In 1990, 42% (17 million) of South Africans lived below the minimum living level. This stringent measure of poverty covers only subsistence needs and makes no allowance

for discretionary, savings or health expenditures. In addition, levels of inequality, or relative poverty, exceed those in most middle income countries. Serious disparities are particularly obvious along racial lines and are reinforced by geographical disparities; of those living below the Minimum Living Level, 94% (16 million) are black, while 65% (11 million) reside in rural areas.

## ECONOMIC GROWTH

The basic historical indicator of economic growth, the real gross domestic product (GDP), shows the value of output produced after correcting for inflation. Although the GDP has a number of flaws - in particular it omits income distribution - it remains the most widely used indicator of economic progress. What does the GDP show for South Africa?

Essentially the country has been following the worldwide trend to economic slowdown, with rates of growth declining from an average of 6% in the 1960s to 3.5% in the 1970s. During the 1980s the growth rate averaged only 1.5% per annum, while during 1991 and 1992 it has been strongly negative.

In the context of a population growth rate of 2.5% p.a., this poor growth record has ensured an average fall in per capita income of more than 1% per annum over the past twelve years!

The economy's failure to grow has had severe effects on employment. During the 1980s only a meagre 14.6% of new labour market entrants were able to find formal sector employment. Current estimates are that at least 30% of the potential labour force are unemployed, although there are stark regional differences, with some areas of the Eastern Cape, for example, experiencing up to 50% unemployment.

## INFLATION

Unexpected and high levels of inflation are socially and economically disruptive.



Although South Africa has till now been spared this problem, domestic inflation rates in the last seven years have diverged increasingly from those of her major trading partners. Thus the current South African rate of price increase is officially 15%, whilst most of Western Europe has rates currently below 5%. This has implications for South Africa's exchange rate and for the competitiveness of export and import substituting sectors.

## *'Positive, short-term indicators are fragile advantages and easily squandered'*

Unfortunately, the current inflation coexists with a substantial economic recession hence the normal tools used in the control of prices increases are unavailable to the authorities.

## MACRO-ECONOMIC MANAGEMENT

What macro-economic tools can we use to extricate ourselves from this low growth, high poverty, persistent inflation problem? Conventional economists refer to monetary and fiscal policy. In South Africa the dominant monetary tool over the past few years has been the interest rate (and not direct control over the money supply as many would think). A glance at interest rates over the last few years will show the hard line the South African Reserve Bank has taken in attempting to control inflation. High interest rates were set to dampen especially import expenditures in order to generate a trade surplus to repay foreign debt. Such a policy shows that the Reserve Bank views inflation as a



more significant problem than unemployment and poverty. What must be recognised is that even a reorganisation of priorities would not necessarily lead to a lowering of interest rates. Although in theory there is substantial excess capacity in certain sectors of the economy, there are bottlenecks in others caused by ageing capital, skill shortages and lack of management expertise. A policy of cheap credit in such an environment would simply drive prices up.

From the point of view of fiscal policy (ie government management of the economy through tax and government spending), the two basic indicators of South African policy options are tax rates and the deficit before borrowing (the difference between tax and government expenditure in the budget). Unfortunately, neither of these policy instruments currently offers sufficient scope for correcting the economic malaise.

As comparative research by Lieb Loots at the University of the Western Cape shows, South Africans are already highly taxed relative to other middle-income countries. While middle-income countries generate between 20% and 30% of their GDP in tax revenue, in South Africa the ratio is presently at 30%. Loots argues that given the limited tax base, steeper tax burdens are likely to incur costs, both on growth forgone and as allocative costs, by restricting investment. Tax increases are therefore largely limited to increases in the economic growth rate which will expand the tax base.

Spending not financed by taxation has to be financed by borrowing. South African budget deficits in the 1980s have been rela-

tively modest at an average of 3-4% of GDP, however, government overspending this year is expected to push the deficit closer to 7% of GDP. While there are no precise limits to the size of an acceptable deficit, deficits in excess of 7% are likely to exacerbate inflation and lead to unsustainable foreign debt burdens.

### CONCLUSIONS

The only hope for the future lies in the recognition that economic restructuring is as necessary as political restructuring. Any growth generated on the current economic base would entrench inequality, exacerbate inflation and, in any case, be stifled by balance of payments limitations and the continued lack of investor confidence. Clearly the South African economy is not faced with an aggregate growth problem that can be solved by the application of additional resources. Nor will the removal of economic and political distortions imposed by apartheid miraculously restore us to growth rates of the 1960s. Stagnation reflects long-term structural problems and only a restructured growth path can ensure sustained rising levels of per-capita incomes and social services.

### *'Only a restructured growth path can ensure sustained rising levels of per-capita incomes and social services'*

The challenge to future economic policy is to devise such a growth path which tackles both the issues of economic growth and redistribution without exacerbating inflation. The difficulty is that given constrained resources tough choices must be made and tradeoffs faced between these often contradictory goals. The debate between political parties over economic policy is therefore often reduced to the priority and timing each attaches to growth and redistribution objectives within its economic proposals.

Parallel to the debate over the nature of economic restructuring, however, a separate debate is emerging over the timing of this economic process relative to political democratisation. This debate places South Africa at the cutting edge of development theory and practice, where there are no appropriate guiding examples. There are no successful cases of countries which were compelled to tackle political and economic democratisation simultaneously. This is the challenge that South Africa has in common with Eastern Europe, and the verdict on the transition in Eastern Europe is still pending.

One tendency in South Africa stresses that

even though development is needed to create a stable democracy, a political settlement must precede a development settlement. On these grounds numerous development initiatives have been postponed or aborted. The argument is that at present we do not have a legitimate government nor any other sufficiently inclusive, participatory organisation that is able to plan and implement economic development. This places South African development in a Catch-22 situation. The government is unable to implement development initiatives as these will be rejected as unilateral restructuring; however, without political power, neither can any of the opposition groups negotiate development. In effect the political process is holding the development process to ransom.

While this tendency undoubtedly voices the real constraints many practitioners have encountered in development practice, it underplays a number of more important factors:

- The obvious point is that the stability of the transition depends on halting the violence which, in turn, depends on the amount of unemployment, poverty and inequality in the system. There cannot be a political solution to an economic problem and economics has been a central catalyst in the post-1980s violence. In addition, for the disadvantaged, the success of democracy will first be measured by material increases in the quality of life. To postpone delivery is to seriously risk undermining the best case political settlement.

- If South Africa is to overcome present economic stagnation, it must undertake an economic transformation process that is at least as fundamental and deep as political restructuring. What proponents of the "politics first" viewpoint underestimate is the long gestation period, between implementation and visible benefits.

- In the context of our already stretched resources, it is important to stress the preconditions for a resumption of investment. Economists traditionally distinguish between risk and uncertainty by saying that uncertainty has no probability attached, whilst with risk one knows the odds. The essence of commerce has always been decision-making in the face of risk. In the face of uncertainty, however, no businessperson can make a rational decision and is likely to do nothing. The South African political and economic policy situation at the moment is engendering precisely this sort of uncertainty. Unless the political affairs of the country are resolved speedily and clear guidelines for economic activity are established, there will not be an economy to support

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whatever administration eventually emerges.

• Finally, there is a danger that an interim government will not constitute a sufficiently legitimate structure to negotiate development policy. For practical reasons, it is possible that during this period most economic functions will continue to rest with the current government. Thus, the condition of legitimacy may only be met once a new democratic government takes power. To suspend development initiatives (or even to reduce the proportion of resources devoted towards such initiatives) until such a state of affairs exists is courting sure disaster.

For these reasons we must create sufficiently credible structures to, at least, map development options and initiate pilot development projects during an interim government period. One possibility is to use the various national, regional and issue-specific development forums that are currently mushrooming throughout the country. Although not perfect, these institutions represent the most inclusive, participative institutions currently available. To enable these bodies to perform this function, however, two conditions will have to be met: first, the investment of substantial resources to overcome present capacity and skill constraints and ineffective national co-ordination; second, all stakeholders must unconditionally commit themselves to the forums and the state must find mechanisms to give these forums direct access to and influence over legislative decisions.

Of course development forums cannot plan, guide and implement an entire economic restructuring process; they may however, serve to establish a solid base for future development in a number of ways. They may help to generate a culture of participative development which will stand us in good stead in the future. Pilot projects will provide important guidelines and positive examples for future initiatives. Active engagement in development will help expose future practitioners to the practicalities, management and institutional requirements of project management. Clear guidelines as to future economic policy will begin to coax investment to return. At the very least negotiations in development forums may instill a sense of urgency which will help the economic settlement keep pace with and support a political settlement.

*(An expanded version of this paper is available from Idasa, 1 Penzance Rd, Mowbray 7700.)*

# Confusion of options

**The federalism/regionalism debate has become something of a political football. RICHARD HUMPHRIES argues that the discussion is too simplistic and calls for a closer look at the implications of these options.**

**T**HE average South African might be forgiven for being confused about the meaning and interpretation of regionalism and federalism, especially since these concepts seem to have surfaced from nowhere in the last year or so to dominate political debate.

This confusion must be all the greater since the deadlocked Codesa 2 convention. Before the convention it was widely, if uncritically, argued that the National Party and the ANC were moving closer to one another on regionalism, even if they disagreed on federalism.

Now in the wake of Codesa 2 the media bombard their audiences with analyses pointing out the major differences between regionalism and federalism and how the major political parties and movements stand on these issues.

In its most simple form their positions could be captured in the following way. The Democratic Party is probably the only unqualified, and long-standing advocate of federalism; the National Party is a little more coy, arguing for "regionalism based on sound federal principles"; The IFP seems to be approaching the stage where it will die defending federalism (perhaps even confederalism) for KwaZulu while the ANC accepts the existence of regions but it is still not certain how much political power should be vested in regional authorities.

The differences between regionalism and federalism are important in their own right. Yet the debate takes on an added significance at this stage of the negotiations process since fundamental constitutional questions about the distribution of political power between contending tiers of government are involved. Thus a choice, either way, between regionalism or federalism will have long term consequences for the way South Africa is to be governed.

Put another way, the differences between the ANC and the NP cannot be equated, at this stage, with the policy differences between, say the Tories and Labour in the United Kingdom. There, both parties accept the constitutional parameters within which politics takes place; what is at issue is policy differences and emphasis within an accepted overarching constitutional order.

Here we have still to decide on the shape of our constitution. This explains why President De Klerk, at the opening of the recent short session of parliament reiterated the NP's determination to bind a future constitutional drafting body to principles which would guarantee regional authorities substantial political power.

The ANC rejects this because it, in effect, gives the present minority-based government and the interests it represents undue power over a constitution-drafting body elected by all South Africans.

**I**N a sense the NP refuses to countenance suggestions that one way out of the regionalism/federalism deadlock would be to let the issue play itself out through process politics over a defined period. If a majority of voters came to accept that regional powers were important to their daily existence then this ought to be sufficient to ensure that authorities would be instituted.

For the NP the problem or dilemma is that the regional fissures or pressures which it thinks exist might be contained by other dynamics during such a period. The ANC might also be uncomfortable about such a suggestion given its historic opposition to homeland balkanisation.

It might be argued that both regionalism and federalism share a common point of departure - that power should be vested in the regions - which makes the differences between them rather irrelevant. This is not