NATIONAL COUNCIL OF PROVINCES

QUESTION FOR WRITTEN REPLY

QUESTION NUMBER 186

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Mr T D Harris (DA-WC) to ask the Minister of Finance:

(1) With reference to the Medium Term Budget Policy Statement (details furnished), what reforms will be required in South Africa in order to replicate such a reaction to future recessions;

(2) whether he will make a statement on the matter?

CW239E

REPLY

(1) The global economic crisis resulted in a very large negative demand shock that plunged many countries around the world into recession, including South Africa. Some countries have been in the fortunate position of avoiding recession through the crisis, such as Korea and Australia, the examples referred to in the Medium-term Budget Policy Statement.

An economy can adjust to a demand shock either through a fall in prices, or a decline in volumes or a combination of the two. If prices of goods and labour do not adjust to the fall in demand, volumes will bear the brunt of the adjustment leading to a decline in consumption and employment. This reality has been experienced in a very real way by almost a million South Africans who have lost their jobs over the past year, even as those with jobs have benefited from real wage increases close to 2%.

Countries like Australia and Korea have shown more resilience, in part because prices and wages adjusted quickly to the drop in demand, enabling them to maintain employment despite lower sales. Their policies were also strongly supportive of macroeconomic stability and export competitiveness. As a result, GDP growth bounced back swiftly after the dramatic contraction in the fourth quarter of 2008, which limited the impact on employment.

It takes time to establish a more flexible economy capable of reacting and responding to economic shocks. Australia embarked on a reform process in the 1980s that has lasted twenty years. Korea responded to the Asian crisis in 1998 with a determined effort to raise productivity. Such a process is a conscious decision to undertake policy reforms that transform product and labour markets such that they are competitive, efficient and able to adjust swiftly. While undertaking these changes, a solid and robust macroeconomic framework that supports low inflation and robust investment is also crucial.

While South Africa can draw many lessons from these countries, we need to acknowledge that each country is different. The economic adjustment that has taken place in South Africa was exacerbated by large imbalances, high debt and inflation, that were present in the economy before the financial crisis intensified. There are a range of policies that we can pursue to ensure that the economy becomes more labour absorbing and to ensure that we are more resilient for future recessions. Along with a focus on the delivery of better quality public services in education, health and crime prevention, there must also be renewed emphasis on microeconomic reforms to enhance competitiveness and the ability of firms and workers to adjust to economic adversity. This will include improving competition through a proactive competition policy, effective regulation, reducing the cost of doing business, investing in infrastructure to remove bottlenecks, and ensuring that real wage increases match productivity growth. Macroeconomic policies that are counter-cyclical and maintain a low and stable rate of inflation will remain vital to support sustainable growth.

(2) Not at this stage