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KEYNOTE ADDRESS

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Accelerating growth and development in South Africa

Economic Society of South Africa, Conference Gala Dinner, 8 September 2005

I am delighted to have the privilege of joining you tonight, and to have the opportunity to congratulate the Economic Society of South Africa on this 80th anniversary.

I understand that the Economic Society was not only formed in 1925, but that was also the year of its first conference. The Society had its origins in a more modest earlier proposal by Dr JE Holloway to WH Clegg, the first Governor of the Reserve Bank. Holloway had written, in words that might have come from my mailbox last week: "It is a peculiarity, not only of world problems of the present day, involved as they are by a multiplicity of conflicting interests, but also of local South African problems, that the economic aspect is becoming increasingly important. Society wants guidance, now more than ever before, in its economic problems…" Holloway suggested a gathering of a "small circle … of men who, by virtue of their knowledge of the theory or practice of the body-economic, could provide one another with the essential atmosphere of stimulation and constructive criticism…" I am pleased to see that membership has not remained restricted to a small body of men, and I am sure that the atmosphere of stimulation and constructive criticism benefits from greater diversity these days – although perhaps not quite as much diversity yet as we would like.

The influence of this intellectual stimulation and criticism on South Africa's fiscal and financial affairs over the past eighty years has undoubtedly been immense, not least in that senior treasury officials and even a few of my predecessors owed at least part of their education to their membership of the Economic Society. An accounting as to whether the credits outweighed the debits in these various internships has not yet been published, but I am happy to accept that in this, as in many matters economic, the lines of causality and influence probably ran both ways.

My topic this evening is growth and development. I am confident this is a topic that will create "an atmosphere of stimulation and constructive criticism…", indeed it is safe to assume that there are as many views on economic growth and development in this room as the number of economists here. Or perhaps twice that number, for as we have known since Mr Keynes served as advisor to the Chancellor of the Exchequer, an economist worthy of the name offers at least two views on every subject.

Well, I am not constrained by the discipline of an economic training and I don't need to be restricted to just the economist's one hand and the other, and so I'd like to share with you five perspectives on the growth and development challenges facing us in South Africa.

How we accelerate growth, how we improve our economic performance, is one of the central questions we face as a nation and polity. I greatly welcome the foresight of your conference organisers in putting these issues on the agenda, and I look forward to learning from the research papers that the conference programme contains, and subsequent analysis and debate that will no doubt be provoked.

Economic growth is not just a matter of theory and empirical facts, but about unique policy challenges, values and competing priorities. There is no universal recipe to be applied to all countries, or that is relevant for all time. Just as each country and region has its own circumstances and customs and cuisine, so also we need to look closely at the particular economic and development challenges and choices we face. We, in South Africa, have to write our own unique recipe for growth, taking into account our history, our geography, our neighbours, the international economy and, most critically, our own vision and values.

The first perspective on our development challenge, I would suggest, is the divided nature of our economy. President Mbeki has spoken about the first and second economies – one that most of us here are familiar with, that operates on established principles of law, property, contract, and reciprocity, and the other on the interstices of regulated commerce: unincorporated, insecure, unprotected, unbankable, overtraded. This second economy is characterised by high levels of unemployment, poverty, limited access to essential services and limited opportunities for economic participation.

Within the mainstream economy, there are several challenges for growth, competitiveness and development – there is the rapid pace of technological change, the complexity and unpredictability of global markets, there are regulatory and market failures or institutional weaknesses. The high costs of doing business prevent small businesses from surpassing current growth levels and prevent more established business from expanding to other markets. This is coupled with inadequate economic infrastructure. There is inadequate competition within some industries, evidenced by high mark-up pricing, and slow dispersion of technical change and business opportunities.

We face infrastructure investment challenges and we need to improve urban and spatial development planning, and deal with inefficiencies in our freight transport systems and congestion on roads and commuter rail services. These are development issues for both the modern and the marginalized parts of the economy – they are partly about redressing the fragmentation and imbalances we inherit from the past and they are about building bridges between formal and informal networks of economic activity.

The growth and developmental challenges facing South Africa are partly about eliminating the duality in the economy and creating seamless markets and an integrated physical landscape.

More rapid growth is a critical pre-condition for broadening participation in the economy. Our growth performance has increased the past decade, to about 4 per cent a year currently from below 1% in the decade before 1994, and the volatility of income and output trends has also fallen. Several other positive indicators are worth noting:

- There has been a significant reduction in the level of government dissaving and a shift in budget allocations towards, education, health and welfare.
- We are working within a stable, low inflation macro-economic environment to lower unemployment.
- Inflation and interest rates are at historic lows.
- Business and consumer confidence is booming.
- And while unemployment remains a challenge, there are encouraging signs of a turnaround in job creation over the past four years.

But this is just the first phase in building a prosperous economy, broadening participation and reducing the wealth and income gaps that characterise the South African economy.

So let me suggest a second perspective on the growth challenge, one that focuses not on distributional issues, but on the investment environment. Improved economic performance is partly about building an environment within which investment decisions can be taken confidently, investors are rewarded for taking business risks and discovering new productive opportunities, and the regulatory context encourages business development.

This is about microeconomic and institutional arrangements, it is about the details of industrial and trade policies, it is about sound financial markets and effective corporate governance, it is about tariff-setting and competition policy, it is about the quality and effectiveness of public services. Macroeconomic and financial conditions are part of an enabling environment, but there is a great deal more that also needs careful economic appraisal and review.

One of the distinctive features of our investment environment is our commitment to seeking shared solutions to the challenge of broadening ownership and participation in the South African economy. We have put in place a broad statutory framework for black economic empowerment, that invites stakeholders to reach voluntary and cooperative agreements, to make forward-looking commitments and then jointly monitor progress against these targets. Many countries have adopted more interventionist approaches to redistribution, sometimes with decidedly damaging consequences.

The economics of this approach to improving the distribution of wealth and opportunities are not straightforward. There are benefits in a cooperative and negotiated framework, but there are risks associated with perceived regulatory uncertainty and the possible breakdown of financing arrangements or long-term partnerships. If cooperative agreements are not well-specified, then there may also be misunderstandings about expectations. Cooperation relies on trust, and trust rests on shared information and clear roles and responsibilities. There is a formidable research programme here, that can draw to some extent on international experience, but also needs to be firmly grounded in the particular challenges of empowerment in our own context.

A third perspective on growth and development focuses on the physical, rather than the institutional environment within which investment decisions are taken and economic activity takes root. We inherit a profoundly fragmented and distorted physical and spatial landscape, in which people live too far from where they work, low-income communities lack basic infrastructure and amenities and the social fabric of communities is weak, both in our walled gated suburbs and in vulnerable low-income neighbourhoods.

How do we ensure that we spend the money we budget for infrastructure in the right places, and spend it well? How do we ensure that we have the engineers, architects and project managers to complete our major infrastructure projects on time, and that spatial development is well planned, transport systems become more efficient and communication networks contribute effectively to growth and development?

These are not just issues of technical capacity, but also of better governance and accountability, both in the public and the private sectors. Once again, there are difficult and important research questions to ask – and there is also the challenge of improving the links between economic analysis and urban or regional planning, of getting economists and engineers or planners to talk to each other and work together. Partnership and cooperation has to be fostered not just between institutions, but also between the complementary disciplines that shape growth and development planning and programmes.

(Perhaps I should confess that as an engineer in an earlier phase of my career I have had to adapt to the ambiguities of the language of economic advisors, and so I have a particular interest in bridging this communication gap. First lesson: when you talk about “foundations” or “fundamentals”, it’s important to explain to an engineer that the cement price does not come into the calculations. And when the project manager shows you his bill of quantities, my advice is check that VAT has been added, you don't need to work out whether the supply curve is convex.)

Fourthly, we have to keep a clear focus on the human dimension of our growth and development.

Labour is abundant in South Africa, but we have not done well in mobilising the unemployed, nor in improving the pace of skills generation and their applicability to the particular needs associated with industrial and development opportunities. We need to understand far better the dynamics of South Africa's labour market, in particular industrial, occupational and regional settings.

General propositions about flexibility or productivity do not get us very far – we need dispassionate advice on specific trends and particular reform options. It is something of a puzzle that we record such high unemployment rates by international comparison, although work-seekers have an average of 9,5 years of schooling. Are the difficulties in the content and quality of schooling, in the management of entry-level employment at the workplace, or perhaps in the wider social support environment? In the context of renewal and substantial investment in our further education colleges and curricula, these are hugely important issues and the voice of economists needs to be heard, alongside educationists, employers and representatives of labour.

Finally, there is the all-important perspective of the residual item in the growth equation.

Perhaps the polite way to talk about what we don't know, is to pay appropriate respect to the frontiers of economic science, by which I mean the continuous search for greater clarity about the sources of technical change, the determinants of productivity and the dynamics underlying market movements in prices and incomes. There is a huge gap between what we can model and what we can observe, and so economic advice is incomplete and frequently contested. The gap is particularly large when it comes to explaining sources of growth and predicting future trends. I don't think mention this as a reason for discouragement, but rather as a reminder of the importance of asking the right questions.

So, for example, in thinking about our growth prospects we have to take into account that we have a comparatively low rate of saving. It is that much more important that we should ensure that investment is well targeted, well planned, and efficiently executed.

We have well-established higher education and research institutions, but its capacity is not unlimited and new research programmes can be hugely expensive. We have a particular need for clear and intelligent advice on priorities for research and technology spending.

The South African economy has important trade, financial and institutional links with the rest of the southern African region and the African continent. Our well-being relies in part on successful economic development strategies in our neighbouring countries. We need to understand these links better, and find ways of mediating international economic relations through better institutional arrangements.

In short, South Africa's future depends in no small measure on the intellectual power, innovation and creativity of the community of economists. And I am fully conscious that there will be competing views, there will be noisy debates, we need a varied menu and there will be many different tastes and preferences to accommodate.

I am pleased to be able to share with you advance notice of a new research programme to be supported by the National Treasury, aimed at strengthening cooperation between economic researchers and building on the standards of excellence which have been a hallmark of the Economic Society of South Africa over the past eighty years. The project will be administered through the School of Economics at the University of Cape Town, but it will fund research on a competitive basis throughout the economic community. The Treasury will participate in the project steering committee, but projects will be subject to independent academic peer review. It is also our intention to expand this research project to also include leading economists and experts from elsewhere in Southern Africa and the wider research community, and to promote research capacity building and opportunities for young economists. This is a venture in keeping, I think, with the spirit in which the Economic Society was founded, and I hope that this conference will provide an opportunity for a preliminary gathering of thoughts on some of the pressing research questions that might benefit from more rigorous analysis as part of this new research initiative.

Thank you