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ECONOMIC TRANSFORMATION FOR SOCIAL CHANGE

Speech by Deputy Minister of Finance
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President and the Executive leadership of ABSIP

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Ladies and gentlemen, Good morning

Before I begin with my opening remarks, I would like to acknowledge the sterling work that the Association of Black Securities and Investment Professionals (ABSIP) has been doing during the last four years under the strong leadership of Ms Tryphosa Ramona. I am told that her term of office as President is coming to an end this year. Thank you for providing guidance to the organisation during difficult and challenging times. The new leadership must protect the gains made during your term in office and continue to move the transformation agenda forward in the financial and asset management sector.

We hope that the transition and the process of electing a new President and the executive will be managed efficiently with outcomes consistent with the best and proud traditions of ABSIP, Well done Ms Ramona and good luck to ABSIP on its future endeavours.

Global growth slowed to a six-year low in 2015, and the outlook for 2016 and 2017 remains subdued. Economic pressures have been most hard-felt in emerging markets, especially Brazil, Russia, and South Africa. This is a result of slowing growth in China, weak commodity prices, lower and more volatile capital flows, higher interest rates in US, and less space for counter-cyclical fiscal policy and monetary policy support.

South Africa is often described as a fragile economy. Fragile economies are those that have become too dependent on unreliable sources of foreign investment to finance their own growth ambitions, and in South Africa’s case, even their infrastructure and social investments. What countries such as Brazil, Turkey, and South Africa have in common is their extreme vulnerability to external shocks, with susceptibility to large-scale financial crises caused by even relatively small economic shocks.

The reason for this has to do with the structure of the economy, and the failure to implement the necessary economic reforms. When one compares economies such as Brazil, Turkey and South Africa with more resilient economies such as South Korea, Malaysia, and even China, a number of core differences are evident.

Firstly, fragile economies have very low levels of gross domestic savings as a percentage of GDP (14% for Turkey, 16% for SA compared to 34% for South Korea and 35% for Malaysia). Both government and citizens in South Africa are heavily indebted, which makes us extremely vulnerable. Debt servicing has become the fastest growing budget item, again both of government and private households. To put it into perspective, we could fund the annual budget of an additional two provinces, or provide the additional costs for free higher education for the next five years, on what we spend on debt servicing in one year. Reigning in rampant government spending, addressing the contingent liability concerns in our SOEs, and terminating/deferring spending on unviable projects is non-negotiable.

Secondly, the more resilient economies have far higher levels of fixed capital investment. For example South Africa's fixed capital investment as a percentage of GDP stands at 19%, Brazil at 18% and Turkey at 20%, compared to China at 47% and South Korea at 30%. We have to increase both public and private sector levels of investment in fixed capital.

Continued Government investment in infrastructure will not in itself enable us to escape our low growth trap. We need to urgently increase levels of private sector investment in our economy. To do this, we require economic policy certainty and more deliberate efforts to reduce the costs and ease of doing business in South Africa. I will pay more attention to this shortly.

The third area that sets fragile economies apart from more resilient ones, relates to the structure of the economy. Again the hard facts speak for themselves. Countries that are locked-in to global markets as primary commodity exporters find themselves extremely vulnerable in times of lower commodities demand and prices. This accounts for the poor performance of economies such as Russia, Brazil, Nigeria and of course South Africa.

Economies that have enjoyed higher and more equitable growth, and have proved far more resilient in the recent global downturn, are those with more diversified economies and higher levels of manufacturing value added. South Africa's manufacturing value added as a percentage of GDP is around 12%, Turkey's around 13% and Brazil's 17%, compared to China (32%), South Korea (31%) and Thailand (33%). It is especially in the high technology exports that the real differences are exposed. As a percentage of manufactured exports, high technology goods make up only 4.5% in SA and 2% in Turkey, compared to 43% in Malaysia, and 26% in both China and South Korea. This is directly attributed to government support in areas of R&D, technology development, industrial policy, export incentives and logistics efficiencies.

Many economists describe the South African economy as being caught in a low growth trap since the 1970s. Growth in South Africa has been slowing since 2011, and despite the 3.3% growth recorded in the second quarter, we remain in a downward phase of the business cycle. Growth in the primary (extractive) sector has been volatile. A rebound in mining in 2015 following normalisation of strike affected PGM output was offset by a contracting agricultural sector beset by the worst drought in decades. The manufacturing sector has also remained flat since 2014, and even the services sector has been slowing since 2011. And our bad politics is not helping.

As the Finance Minister noted in the MTBPS, the country is at cross-roads. Continuation of our existing growth model, with its low growth and inherent structured inequalities, will increase spending pressures on welfare, social security and debt servicing. This is a scenario we cannot entertain.

Since 1994 we have reduced the number of people living in extreme poverty from 41.1 per cent to 21.5 per cent. This is a huge achievement, this was the cornerstone of our "post-94 social bargain" – what we could call "redistribution through welfare" – this however is on a dangerous path of becoming unviable and is unravelling, due to low rates of economic growth, particularly since 2008 and limits to fiscal income that can be redistributed.

There is no doubt that the social bargain –especially the welfare spending component - brought significant social returns in reducing extreme poverty and vulnerability, and extending access to basic services. School enrolment and access to services such as sanitation and electricity have increased dramatically.

Another major transformational outcome has been the creation of a black middle class, but this was mostly through state employment and we have been less successful in creating an entrepreneurial black middle class.

But social inequality has not reduced. We have not deracialized ownership of the economy, and our ambitious project of creating a developmental state has been hamstrung by patronage and corruption. Higher social returns have accrued to those already endowed with capital and skills. Our poor education and training outcomes have not helped.

According to the Department of Labour's Commission for Employment Equity (CEE) Annual Report for 2015-2016, the white population group comprise 68.9 per cent of top management and 58.1 per cent of senior management in 2015, compared to their share of the economically active population of just under 10 per cent. By comparison, the black African population group comprise 14.3 per cent of top management and 21.2 per cent of senior management in 2015, despite comprising 77.4 per cent of the economically active population.

It is increasingly evident that we need a new social bargain – a new consensus – to build a faster growing and more inclusive economy.

This new social bargain should build on the great strengths we have as a country. We have strong institutions and a robust legal framework; we have well developed and deep capital markets; our share of GDP spending on infrastructure exceeds that of most other economies; we still have a good environment for business compared to many of our peers; and we are witnessing a renewed vigor from government, business and civil society for economic reforms.

At the heart of this new consensus for inclusive growth, we need to cultivate three new national obsessions that will re-inforce each other:
1. A national obsession with **renewed growth** and **vigorous industrialization**, based on reducing growth constraints and fostering new technological capabilities that will grow employment, incomes and exports.
2. A national obsession with constructing a government that is stronger, more capable and less corrupt.
3. A national obsession with education and skills development, to achieve the first two.

Exceptional leadership within government, business, labour and civil society will be necessary to re-mobilize society as a whole behind this national project, and to extract the kind of concessions and compromises necessary. New institutional mechanisms for collective socio-economic governance and accountability will have to be developed as a matter of urgency.

The first and important task of this collective leadership is to unite to preserve our sovereign credit rating. We have no choice but to remain optimistic.

Secondly, we need deliberate and urgent actions among relevant ministries and SOEs to remove constraints to growth. Already many of these actions have commenced, including reducing high cross border costs (including port tariffs); addressing electricity supply issues; as well as addressing regulatory bottlenecks and labour market constraints, especially labour unrests. We are alleviating infrastructure constraints and bottle necks through allocating R865 billion over MTEF to improve infrastructure. We are also working with municipalities to improve the ease of doing business, and have established a one –stop-shop (Invest SA) to coordinate investment promotion, facilitation and after-care at the national level. Invest SA will also ease delays for investors in obtaining visas, licences, permits, registration and approvals. We are also easing certain immigration regulations, including business visa-waiver for India, China, Brazil, Russia and other countries.

Thirdly, we must address barriers to entry and deliberately enable increased black ownership of the economy. But this must be done through enhancing productivity and competitiveness, so that as we address anti-competitive behaviour among cartels, we do not negatively affect output, jobs and exports.

Key initiatives we are driving to enable black ownership includes using the PIC to inject R70bn into agriculture, mining, manufacturing, infrastructure and energy. We are also prioritizing SME support through our Gazelles programme, and have also just established an SME public-private Venture Capital Fund.

Platforms such as ABSIP are critical for providing substance and leadership in our society.

ABSIP is a thought leader in the financial services industry – which is not only a critical element of the economy, given its size, but also in the role that it plays in directing investments – in other words, directing the course of the shape of our economy.

My thoughts are that we have made significant progress in transforming the financial sector, or at least putting the mechanisms for transformation in place, with regard to consumer protection, financial stability and BBBEE.

But I would want to challenge ABSIP to assess whether our financial sector is doing enough to grow a competitive economy. Are we directing sufficient financial resources into the productive economy and into economic infrastructure? Is the financial sector, to paraphrase my earlier remarks, obsessed with the country's industrialization? Is the financial sector contributing sufficiently to the country's growth and development, and if not, what can be done to improve this? Is our financial services sector sufficiently patriotic? What role can our domestic financial sector play in making us less fragile?

I have no doubt that ABSIP is the correct organization to take up these issues and be a central cog in the new growth coalition we need to build.

I thank you.