Sunday Times, 7 December

The road to prosperity

Government and business have realised that to eradicate poverty within one generation, they must be open to discussing a bolder set of proposals

By Ebrahim-Khalil Hassen

Jabu and Mariam are South Africans who experience the economy in very different ways.

Jabu has established a cellular phone kiosk at Johannesburg's new market for hawkers, built through a partnership between Joburg's council and business.

After raising finances through Khula Enterprises, he managed to buy start-up stock and pay a deposit to rent the premises.

His bank provided online services, which he is still learning to use. Jabu is excited about his future but worries whether he will make enough money to meet his monthly operating costs, pay his two employees and still turn a profit.

Jabu is on the fringes of the formal economy. He wants to establish himself as an entrepreneur and become wealthy through his business.

Since 1996 much of government's policy has been focus ed on getting success stories like Jabu off the ground.

The premise is that the formal sector will create jobs and boost economic growth and that historically disadvantaged groups will therefore share the fruits of economic growth.

President Thabo Mbeki referred to this as the "first economy" in a recent speech to Parliament and indicated that this economy has been government's traditional focus.

He argues that the first economy is modern, produces most of our wealth, and is integrated with the global economy.
Mariam, meanwhile, lives in a rural area.

She collects the monthly child support grant for her child and helps her father collect his old age pension. She is not eligible for a grant, even though she is unemployed.

After receiving her household money , she first exchanges the big notes for smaller notes at the illegal moneychangers, as it is cheaper to lose R20 than a "pinkie" (R50).

Together with a group of women, she participates in a stokvel. Under the scheme they all get a bulk amount once a year, which they use for buying goods, often in the city, and maybe even from

Jabu's store.

Government has provided her village with water and electricity, but she struggles to pay for these services.

Moreover, the supply of electricity is too small to run a sewing machine and not enough water is supplied to engage in small-scale farming.

She has tried to get a job, but the farmers employ only for a few weeks a year and other potential employers expect a qualification or work experience.

The likelihood of a healthy 30-year-old getting a government grant is remote - and Mariam realises she needs to find ways of making money.

Mariam's is the reality of the so-called "second" or "marginalised" economy, which draws its ranks from the rural and urban poor and is characterised by its small contribution to gross domestic product.

Mbeki recently stated that government needs to focus more strongly on the s econd e conomy because of its inability to generate its own growth and development and its disconnect ion from the first economy.

Government attempted to respond to the challenges faced by people like Jabu and Mariam and the problems in the wider economy in its recent Medium-Term Budget Policy Statement (2003), also called the "mini-budget".

The state has finally put taxpayers' money where its mouth is and presented a modestly expansionary model to accelerate shared economic growth.

The mini-budget marks a shift in the way government will use fiscal policy to stimulate shared economic growth and eradicate poverty.

It signifies a change both in the way government will spend money and how it will raise the resources for spending.

An expansionary set of programmes has now been unveiled.

Overall, the proposal is for a 4.4% real increase in non-interest spending over the next three years.

The big-ticket item in the mini-budget is the Expanded Public Works Programme.

This is a R15-billion commitment to create a million job opportunities. It is a substantive move to address unemployment in the short term.

Other second-economy measures that have been mooted include:
* Nodal developments in rural and urban areas;
* Access to credit;

* Women's economic development;
* Incorporating the needs of the poor into skills development legislation;
* Increasing spending on antiretroviral drugs provision;
* Extending the child support grant; and
* Rolling out free basic services in municipalities.

In addition to spending on social goods, government has committed itself to invest significantly more on infrastructure.

The mini-budget states that investment levels are to increase by between 6% and 7% a year between 2003 and 2006.

This will put investment at around 16% of GDP but the budget will have to grow much more quickly to reach the target of 25%. State enterprises are to play a more developmental role, attempting to link key infrastructure needs to job-creation problems.

On the revenue side, the proposals are equally remarkable - to raise an additional R37-billion over the next three years.

The deficit will be increased to 3.2 % of GDP in the next financial year to accommodate the additional spending.

These "counter-cyclical" measures aim to boost growth and ensure that the second economy benefits from government spending. Counter-cyclical approaches utilise fiscal policy to boost demand at times of economic downturns.

Part of the response from government fits this definition since it is attempting to boost demand in almost a traditionally Keynesian manner.

The change in orientation within government is astonishing.

From 1996 until 2000, officials scoffed at expansionary budgets, insisting that South Africa needed "short-term pain, for long-term gain". This philosophy guided fiscal policy. Deficits and taxes were reduced, as was social spending .

Government and business argued that through these tough measures, economic growth and job creation would flow.

When faced with challenges to the policy, government argued that - rather than a change in policy - the Growth Employment and Redistribution Strategy needed to be more fully implemented.

But there has been a weakening of faith since 2000, as trends in employment, investment and economic growth have been mostly negative.

Government today is far more confident about its leadership role in the economy.

The new stance marks a major change from when it argued that "the fundamentals were in place".

The "fundamentals" have not delivered the desired results.

During the Growth and Development Summit earlier this year, agreement was reached between the major economic players on many issues regarding South Africa' s economic future .

The agreement has soothed market anxieties on the matter of expansionary fiscal policy.

Government is thus beginning to exercise economic leadership through consensus-building.

This has given government the confidence to increase spending without risking a backlash from the markets or progressive civil society.

The government has demonstrated its ability to deliver. It has built a million houses and made six million water connections.

Yet failing to spend about R1.8-billion in budgeted money over the last two years remains a worry, as does the sustainability of many government projects.

Developing the capacity to project-manage the flow of funds and monitor the utilisation of funds will be crucial in the medium term, if

government's expansionary intentions are to turn into actions.

The need for a more hands-on government role stems directly from the worrying situation on the economic growth and unemployment fronts.

South Africa has experienced only modest economic growth since liberation and there has been a sharp rise in the number of people without jobs.

The consequence is an economic trajectory that leads only to greater impoverishment.

The problem is being compounded by rand volatility, reduced profits for companies and limited foreign direct investment.

Under such circumstances, governments need to act.

The South African Revenue Services is not immune to changes in the wider economy.

Revenue collection seems to be flattening as companies report lower profits. This is evident from government' s choice of increasing the deficit as opposed to simply raising more revenue.

So government must develop mechanisms for stimulating growth to regain some of the money it intends to spend.

However, the question can still be asked whether government can do more to improve the lives of the poor.

Taxes, for example, could be raised to increase spending on social services.

The medium-term proposal is that the tax:GDP ratio remains stable at 24.8%.

But proposals endorsed by the major unions and non-governmental organisations advocate raising R30-billion over three years by increasing the tax:GDP ratio to around 27%.

An even more direct way to redistribute incomes would be to have a tax cut that benefits the poor.

So instead of cutting personal income taxes, VAT could be reduced.

As poor people pay a higher percentage of their income on VAT in comparison with rich people, they would benefit more from a cut in VAT.

A bolder vision to fully fund education and healthcare over the longer term could result in the most substantial returns.

Similarly, proposals for more rapid land redistribution and the introduction of a basic income grant are further means to facilitate growth that benefits the poor.

Government and business have realised that if they are to eradicate poverty within one generation, they must be open to discussing a bolder set of proposals.

To a large extent the new budget has shifted the debate on public spending.

The traditional divide between those who support Gear and those calling for a return to the Reconstruction and Development Programme is being replaced with a pragmatic consensus that government has shifted its policies more in line with the latter option.

Mbeki and his team have undertaken something of a renaissance - making government spending more expansionary and giving the ANC budget a more social democratic flavour.

South Africans must engage these proposals with the goal of making public spending a more effective redistributive mechanism.

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