Moving from resource dependence

TIPS Seminar

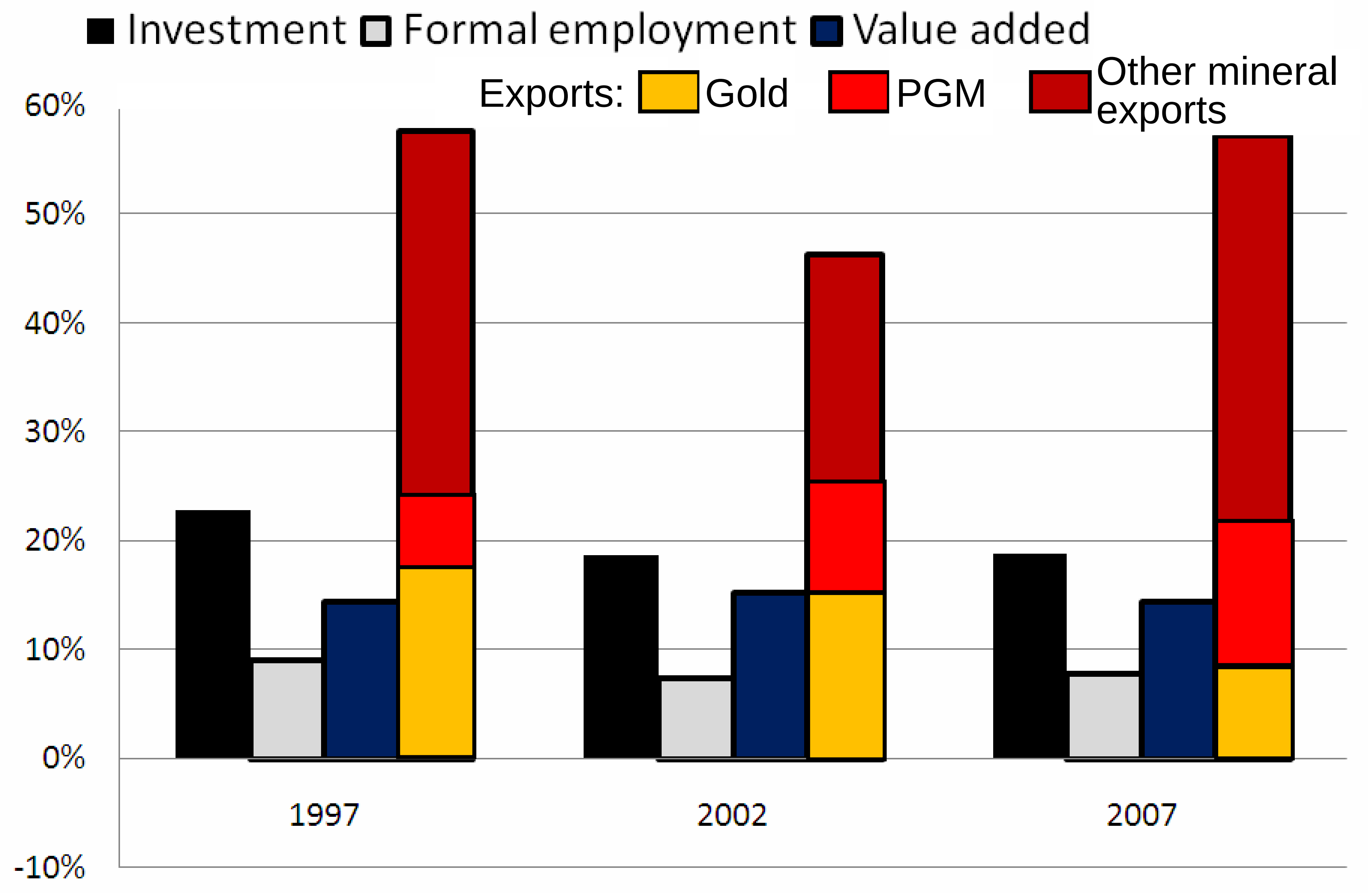
March 2009

Personal views only

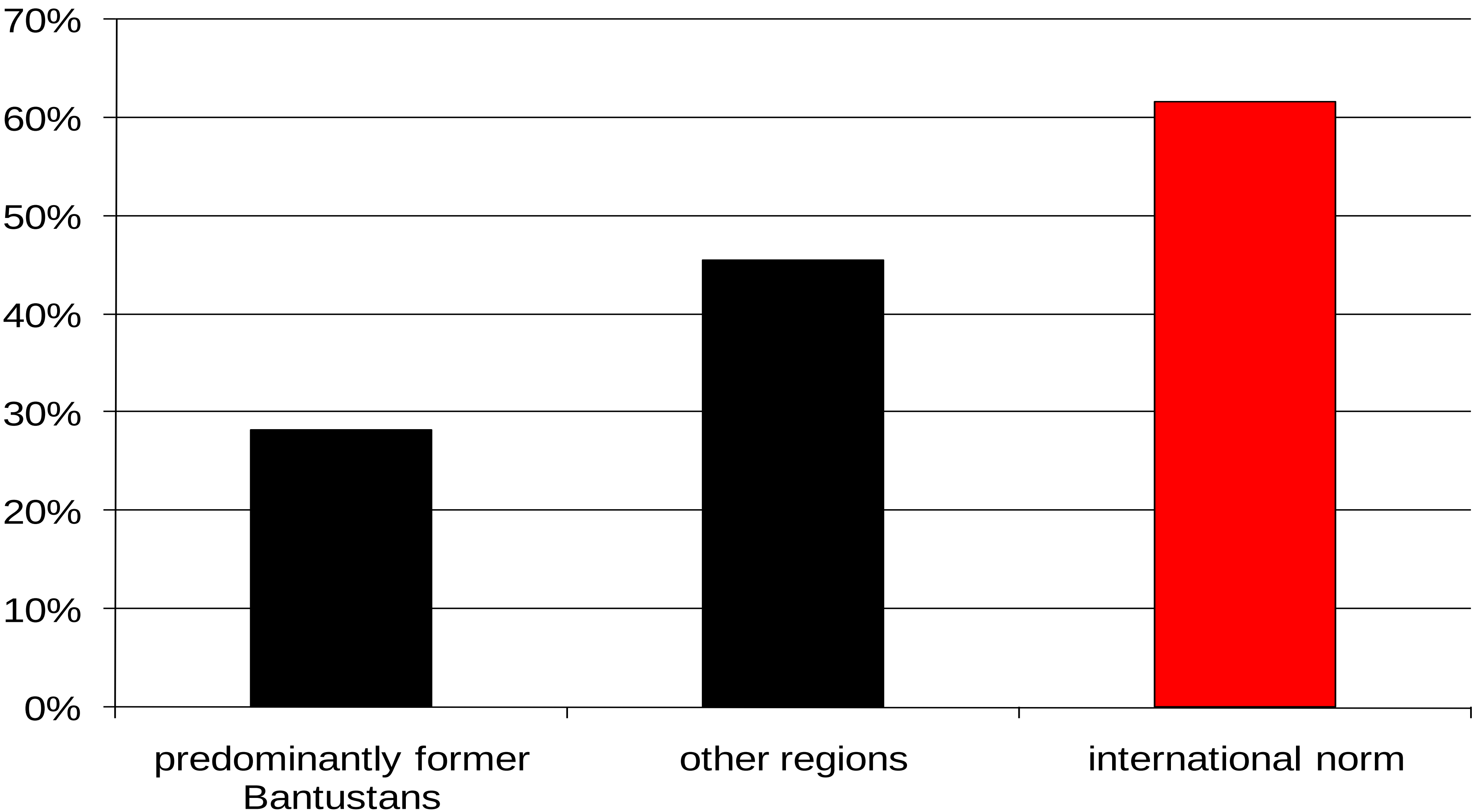
The context

- South African economy still shaped by exports from the mining value chain
- Combined with very low employment levels, despite improvements in recent years

Mining share in economy



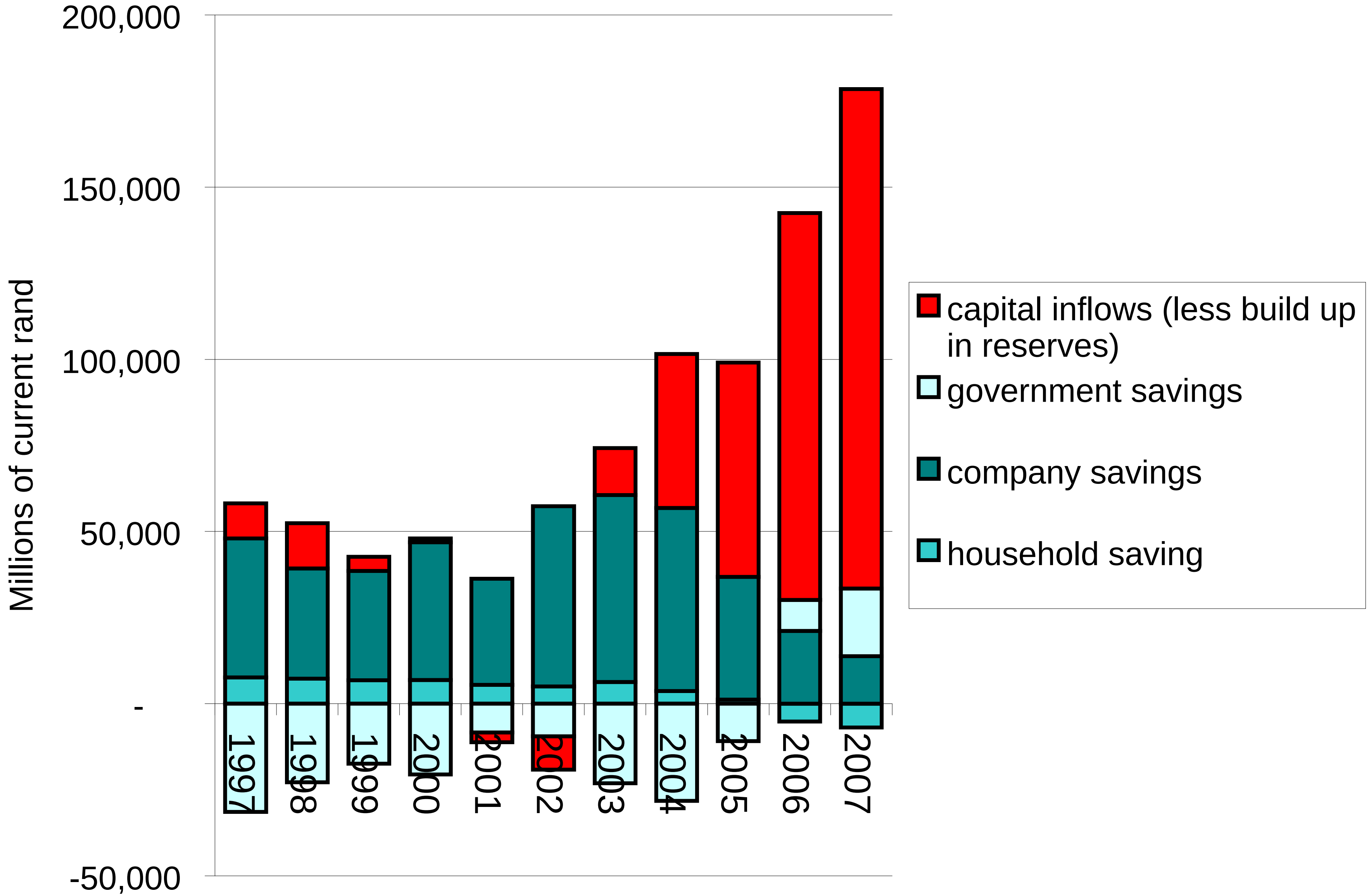
Share of working-age adults with employment



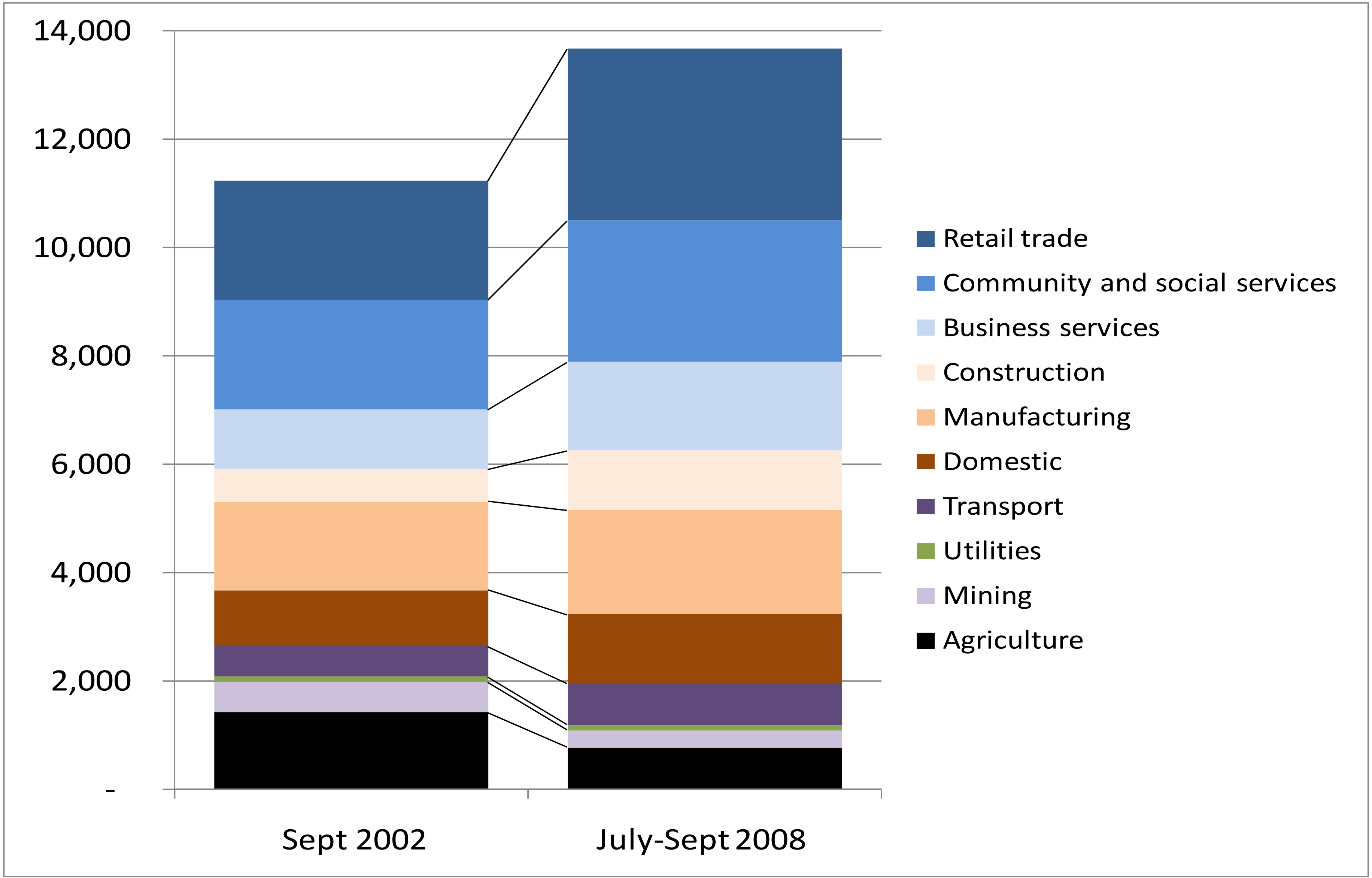
Concerns about continued resource dependence

- Contradiction:
  - High commodity prices bring high capital inflows into equity and bonds, resulting in appreciation – so hard to diversify exports
  - Appear to have squeezed out private domestic savings
- Implications for equity and poverty:
  - Employment creation in boom was rapid but focused on tertiary sectors
  - Poverty alleviation through creation of low level jobs plus redistribution through state

Financing of new investment



Employment by sector



Worldwide downturn...

- Both export revenues and capital inflows plummet
- Government revenues decline so hard to sustain redistribution
- Job losses expected in retail, housing construction and parts of private services – as well as mining value chain

Options for diversification

- Path dependence means new economic activities will require government support
- Essentially two options in discourse:
  - Dynamic exports
  - Employment intensive
- Proponents tend to emphasise potential benefits
- Here also look at requirements and risks – are they viable? what is the cost of failure?

1. Dynamic exports

- East Asian/Harvard group model, reflected in IPAP lead sectors
- Vision: Massive expansion in dynamic exports supports rapid industrialisation and expansion in decent work
- Sectors and markets
  - Growth in exports of cars, high-tech chemicals and electronic equipment, plus high-end foods, light industry and services
  - Rapid decline in share of mining products in exports
  - Low-tech manufactures increasingly imported (clothing, processed foods, plastics, appliances)

Outcomes if successful

- Rapid growth - comparable to India and China
- Relatively slow growth in employment – but good jobs in manufacturing
- New opportunities for higher-end, formal small and medium enterprise
- … and if not successful: Slowdown in growth as fail to support mining and agriculture without expanding new ones

Requirements

- Competitive rand combined with trade policy that supports infant industries while opening markets for new exports
- Robust international demand
- More efficient and low-cost infrastructure plus access to high-level professionals and artisans
- Substantially increased state support for new, dynamic industries, in the context of more consistent and constructive engagement with capital

Likelihood of success

- Contradictions:
  - If commodity markets boom, is it politically or socially possible to depreciate?
  - A prolonged global downturn would depress the rand but also constrain international demand
    - Does the current crisis signal a shift in the role of the US as "consumer of last resort?"
- Price of failure depends on how much put into new industries at the cost of traditional ones

2. Employment creation

- Vision: Government builds on current competitive advantage to ensure rapid employment creation with limited support for high-tech industries
- Sectors and markets
  - Encourage activities and markets that can create employment even if the rand is high or export markets are depressed
    - Relatively low-tech goods to meet domestic and regional needs (agriculture, light industry, low-end services) – protected by transport costs
    - Minerals continue to dominate overseas exports, but a rising share comes from higher-end agriculture and services
  - Knowledge-based manufacturing and services are sustained but not sole priority

Outcomes if successful

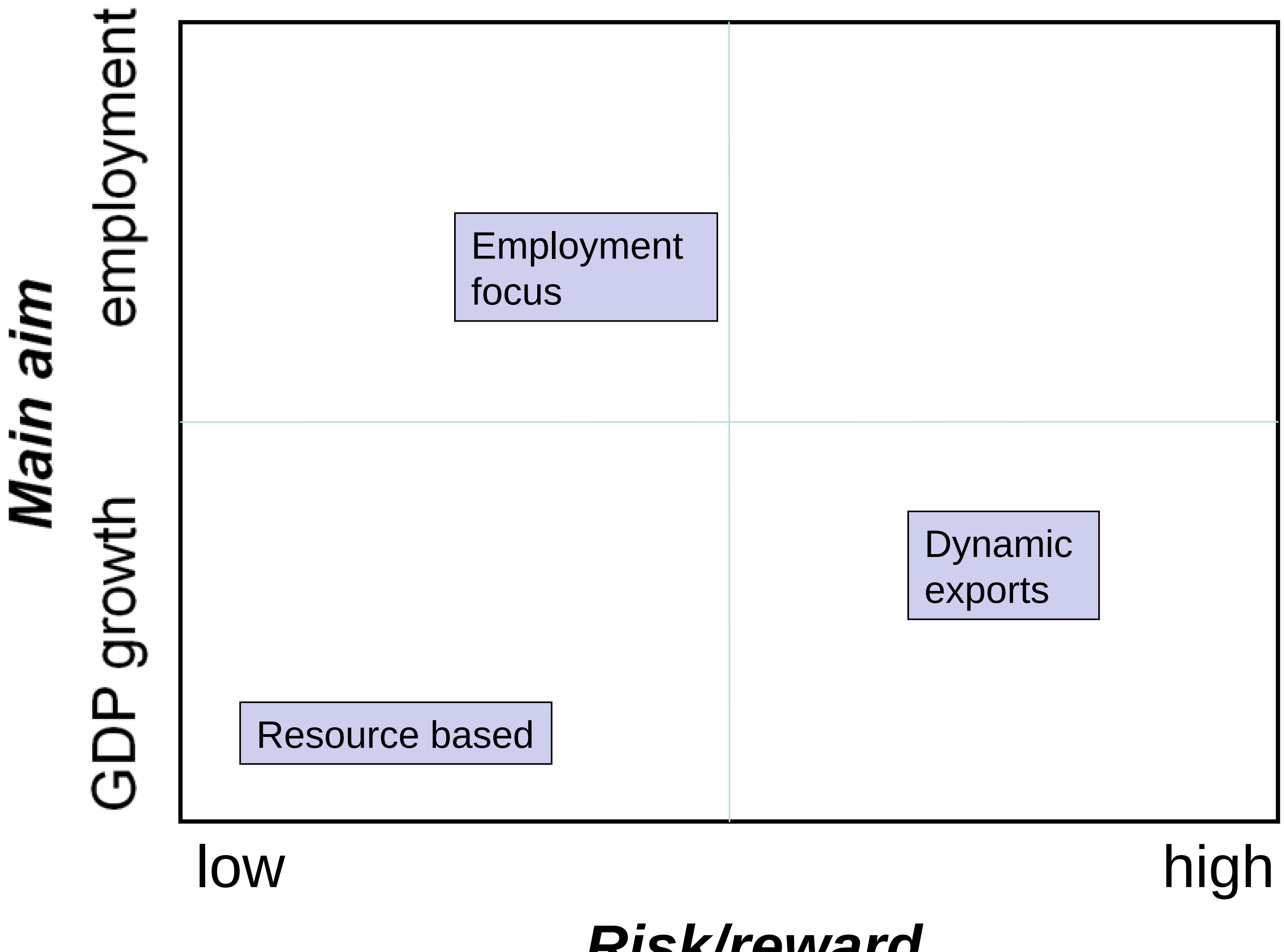
- Growth: Sustained but not outstanding initially
- Employment: Rapid growth in first five to ten years, then levelling off as achieve normal unemployment rates
- Growth in small and micro enterprise particularly in agriculture and services, but little change in core manufacturing and mining
- Rapid improvement in income and asset distribution as employment increases and working conditions improve
- … and if not successful:
  - Government wastes resources on non-competitive labour-intensive industries, while South Africa falls further behind in dynamic industries
  - Redistribution shifts from welfare to make-work

Requirements

- Willingness of state to provide major support to start up labour-intensive sectors and for agrarian reform
  - Relatively expansionary fiscal and monetary policy to support demand and resourcing for new industries , plus
  - State capacity and engagement: explicit mandate to focus on employment creation, and shift in resourcing, infrastructure and governance capacity toward employment-creating industries
- Closer engagement with SADC to ensure growing regional demand
- Consistent support for mining expansion, including review of narrow BEE and basic infrastructure provision and tariffs

Likelihood of success

- Relatively easy to aim for modest success in knowledge-intensive industries and new exports – since not very far ahead of the market
- Much less likely to succeed in large-scale employment-creating initiatives and agrarian reform, which require major transformation
- The price of failure
  - White elephants
  - Neglect of knowledge-intensive industries


Main aim
employment
GDP growth
Employment focus
Dynamic exports
Resource based
low
high
Risk/reward

Some conclusions

- Need to be clear about risks as well as rewards – what is viable?
- Different strategies address different problems (growth, employment, incomes for the employed) – but popular support requires an explicit commitment to employment creation
- Mass employment creation
  - Isn't possible in the best-paid industries
  - Higher employment levels should help improve pay in all industries in the long run

Some conclusions

- Need a much more strategic approach to capital, including around narrow BEE in mining and agriculture
- The value of the currency is a critical issue, which in turn depends on
  - Global commodity prices
  - Ability to push through depreciation if commodity prices are high
- Global warming and strategies to address it will likely affect exports
- Any strategy needs improved economic infrastructure – which will be more difficult to fund in light of the global economic crisis