THE REAL ECONOMY BULLETIN

TRENDS, DEVELOPMENTS AND DATA

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Briefing Note: The President's investment drive

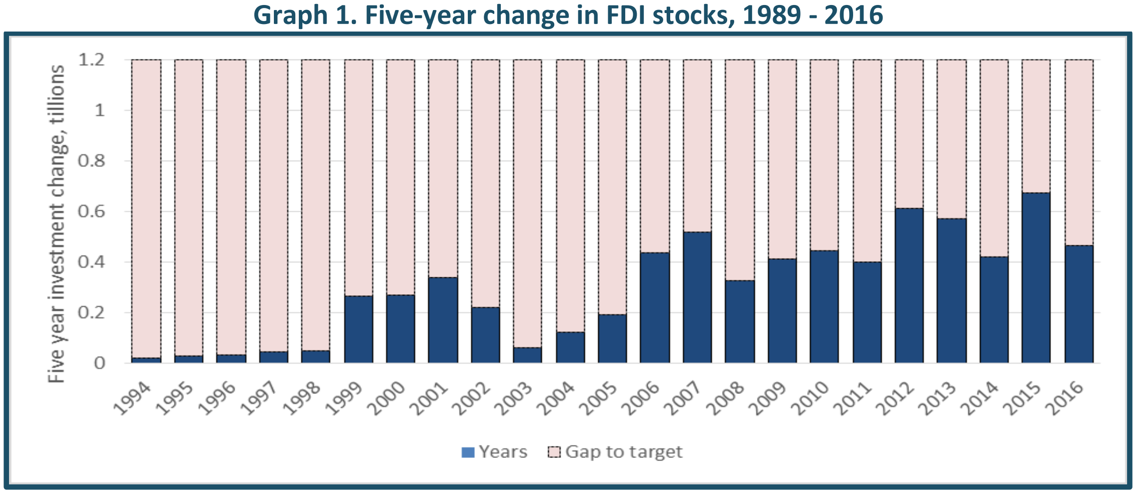
As part of the renewed push towards industrialisation, job creation and faster levels of economic growth, President Cyril Ramaphosa set an ambitious target of attracting US$100 billion in new investment within five years.

Adding between R1.2 trillion to R1.4 trillion in investment in the economy would make a significant contribution toward an economic turnaround. Key steps towards achieving that target including establishing a high-level team to identify opportunities, giving confidence to investors that the country is addressing long -term political stability, with the main facets of state capture being addressed, strategically targeted state visits with key trading partners and investor countries, and an investment conference planned to take place towards the end of the year.

Targeted state visits have led to grand pledges of investment into South Africa. These pledges boost to investor confidence and broader confidence in the country, but it is not clear how well they square with economic realities. Most investments require an underlying project logic. Caution is also important where the viability of these investments requires state off-take agreements or that government provide infrastructure on a large scale, such as water, electricity or new roads and rail.

The initiative was initially presented as focused on foreign direct investment (FDI), but quickly clarified as also targeting domestic investment. This clarification is important. When stacked up against existing FDI of R1.8 trillion, the target is over two-thirds of existing investment stocks. As can be seen in the graph below, no five-year period has come close to the new objective.

Graph 1. Five-year change in FDI stocks, 1989 - 2016



Source: TIPS calculations based on SARB 'Foreign liabilities: Total direct investment'

At the project level, a TIPS database of investment projects between 2016 and 2017 underscores the challenge of the target. The largest investments in the dataset – the construction of the Thabametsi and Khanyisa coal plants as independent power producers – together come to R40 billion. Thirty similar initiatives would be needed to hit the target. In practice, however, the vast majority of inward investment is a sprawl of much smaller projects. Most current projects are valued at less than R500 million, and prominently feature existing investors upgrading or expanding their facilities, a process that again is reliant on the context-specific identification of needs in existing productive structures.

The scale of the proposal can also be understood by comparing it to domestic investment. In 2017, total gross fixed capital formation in South Africa came to R870 billion; attracting R1.2 trillion, even if realised over a five-year period, would boost that amount by over 25% every year.

The President's initiative thus requires a new approach and strategy for government's investment promotion. Routes are being pursued to successfully unlock the level of investment targeted. In addition to recent state visits to and from China, the UK, Saudi Arabia, and the United Arab Emirates (all major trading partners), the President has ensured that key policy issues are being resolved. The most recent is the launch of the integrated energy plan and the resolution of the mining policy. The oil and gas framework is also close to being resolved. Reinvestment in the automotive sector, which has been the bedrock of manufacturing investment for the past few years, is also likely to continue; with recent steps toward finalisation of the new automotive incentive providing the policy continuity to maintain that sector's level of investment. Some of the proposed improvements to the incentive would likely see greater investment in the automotive supply chain, contributing to broader industrialisation efforts.

More effective efforts to leverage government procurement could deepen the impact of state investment, particularly if local content policies are revised to encourage sourcing both locally and from the surrounding region. However, caution needs to be given that the push to attracting new investment does not for example result in more expensive water[1] or electricity and the business case for these new investment projects are strong.

The target aside, greater clarity is required about the new administration's approach to investment. Debates in the past few years have been dominated by a shift away from trying to maximise investment levels in the abstract, to an effort to target investment to maximise the value derived from each project. That means trying to encourage investor pledges around key impact metrics such as employment, local procurement, and community development.

In this context, while investment in mining should be welcomed – both as a symbol of the return to profitability of commodity industries and a chance to extend the livelihood of mines on which many jobs rely – the pattern of the commodity boom, in which companies extract enormous profits without

[1] See recent TIPS research on the high cost of desalination: *Desalination in South Africa: Panacea or peril for industrial development?* Available at: http://www.tips.org.za/research-archive/sustainable-growth/item/3500-desalination-in-south-africa-panacea-or-peril-for-industrial-development.

appropriate investment in their long-term stability or in building a competitive domestic mining equipment industry, should not be repeated. Investment projects will also need to be considered with regard to geographic location, with highly centralised investment in the large metros likely to limit the impact on the most vulnerable in smaller cities and rural areas.

The President's emphasis on boosting investment is crucial, but getting commitments and projects is merely a first step. Assuring investments contribute to inclusive growth is a more complex challenge, but it is vitally important.