Business

Shake up economy, says think-tank

South Africa must develop its production capacity and cut its reliance on resource exports, a report says

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With the fourth industrial revolution taking place globally, South Africa cannot go on with business as usual, according to the Industrial Development Think-Tank (IDTT), which is calling on the government to restructure the economy.

The IDTT, which is housed at the Centre for Competition, Regulation and Economic Development at the University of Johannesburg, is an initiative of the department of trade and industry to assess policy on the structure of the economy.

"Countries develop by changing the structure of the economy to move from sectors of low to high productivity and complexity [sectorial transitioning] and within sectors through upgrading to higher value-added activities [sectoral deepening]", the IDTT said in a report released earlier this month.

The minister of trade and industry, Rob Davies, concurs. "The fourth industrial revolution, now upon us, makes it more critical that we focus single-mindedly on investing in our own productive capabilities."

He added the economy must be opened up to black entrepreneurs.

The think-tank, which has researched South Africa's industrial policy over the past 24 years, argues that the transition from consumption-driven sectors such as finance, insurance, real estate, transport and communication to production-driven sectors such as agriculture, mining and mainly manufacturing will have huge ramifications. This will not only mean an increase in the national income and taxation base but will also mean making possible a larger and more equitable provision of social services.

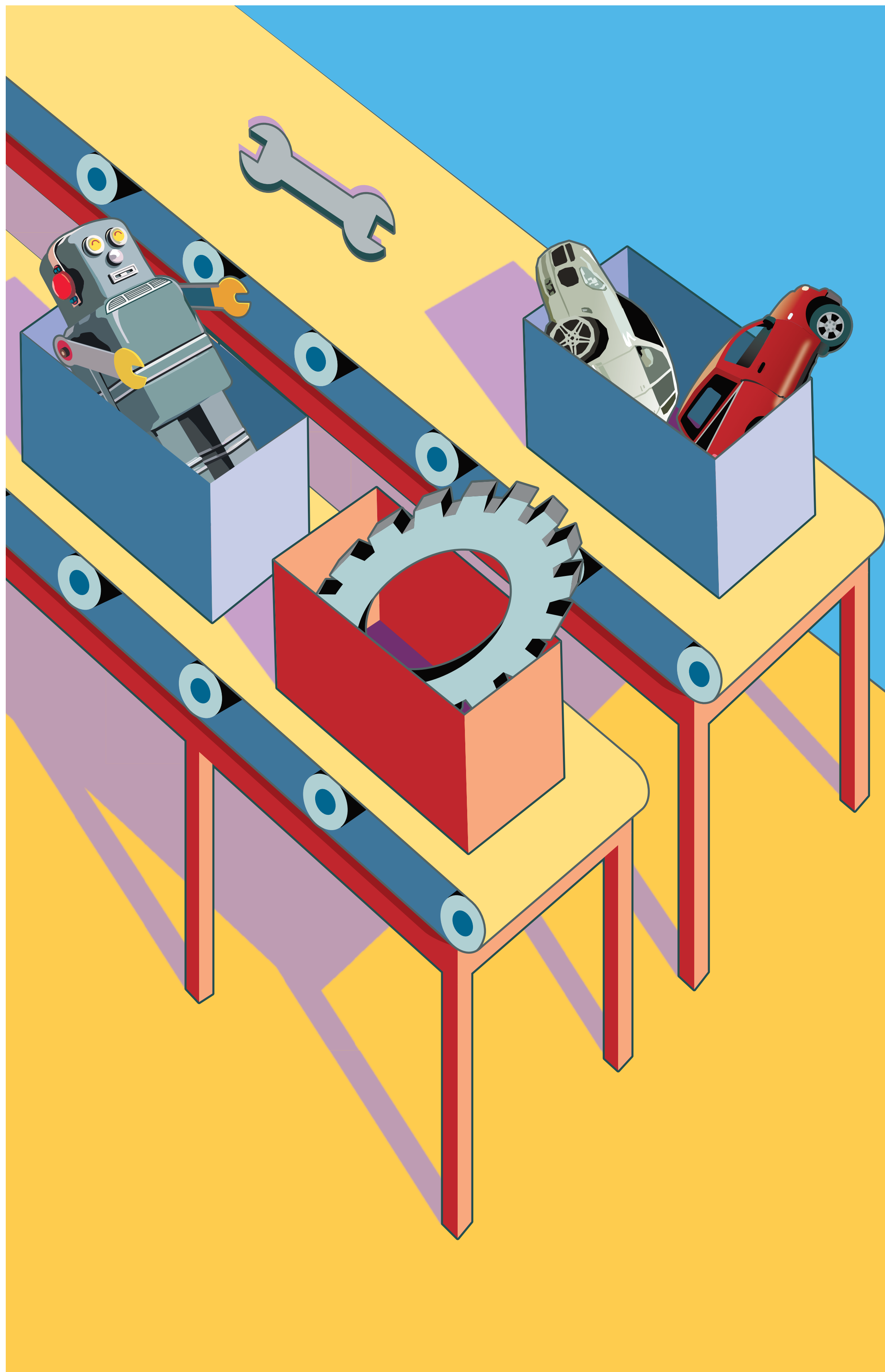
"Manufacturing means workers and firms learn and build capabilities with high productivity [and] higher levels of value-add, but manufacturing also has the ability to pull along growth due to linkages to other sectors such as services," said Pamela Mondliwa, an IDTT economist.

South Africa's value-added industry grew at an average annual rate of slightly less than 1.6% from 1994 to 2016 whereas gross domestic product (GDP) grew at 2.9%. Investment levels have been low and the improvement of skills has been limited, the report says.

It cautions that the country remains an exporter of basic metals and a growing net importer of machinery and equipment and, therefore, needs to restructure.

Mondliwa said the development of design and engineering services were particularly important in the fourth industrial revolution and were nothing out of the ordinary. She pointed to countries such as Thailand, Malaysia and Brazil that have built up clusters for key industries. In Thailand, for example, the automotive cluster had a strong local basis, with skills, technological support and supplier development.

"In South Africa, the clusters do not exist, including in auto, and need to be substantially ramped up. Malaysia had similar policies across a range of manufacturing sectors, while Brazil had concerted policies to develop agro-processings among other sectors," she said.



Graphic: JOHN McCANN

The report argues that, although some sectors have been highly incentivised, success has been limited. For example, the automotive industry has received support and protection for more than a century but, since 1994, it has been limited to fully assembled vehicles and a narrow range of components, and has not developed the characteristics of a real auto hub such as in Thailand and Mexico.

A lack of an overarching policy, as seen in the 1990s and 2000s, coupled with a lack of commitment by the government, will continue to undermine industrial policy interventions, despite the existence of the National Industrial Policy Framework, the IDTT says, and the department of trade and industry needs more support from the government.

South Africa has made some progress in transforming the structure of the economy but it has regressed overall. For instance, the contribution of the manufacturing sector to GDP declined from 21% to 13% between 1996 and 2013.

The commodities boom of the 2000s led to an overreliance on exporting commodities. There now needs to be a more effective management of natural resource earnings, including appropriate macroeconomic policies to avoid overvaluation of the rand.

South Africa's post-apartheid economic transformation has not generally delivered a "better life for all"

By delaying to address these issues, South Africa is missing out on benefits such as global integration, competitiveness and learning through exporting in diversified manufacturing industries, according to the IDTT.

"Export capabilities such as mining machinery have not been built upon," the report notes.

The mineral and resource sectors continue to dominate South Africa's export basket — up to 60% of the total — and exports have remained commodity intensive, with little added value.

"This has been further exacerbated by a generalised skills deficit and specific sectoral skills mismatches, which together pose a development problem with serious ramifications for the skills-intensive manufacturing sectors," the report says.

It argues that the economy continues to be highly concentrated, with some data showing that it is becoming worse, although the ownership has changed because of an increase in foreign and local institutional investors.

Mondliwa referred to a recent study by the Competition Commission, which found that there was often unilateral dominance, with a single firm holding up to a 45% market share, in sectors such as communication technologies, energy, financial services, food and agro-processing.

Statistics South Africa data shows that, in manufacturing, the proportion of subsectors in which the biggest five firms held 70% and more of market share has increased from 16 (in 2008) to 22 of 80 subsectors (in 2014).

The think-tank says South Africa's poor performance is a blind spot from the past. "The compromise reached in 1994 is reflected in the strength of established business groups. The government ought to discipline their rents by subjecting them to market competition, imports and through competition law enforcement."

South Africa's post-apartheid economic transformation has not generally delivered a "better life for all". The report argues that the political compromise merely reinforced the previous regime's status quo instead of changing it.

Even though there have been improvements in social services such as social grants for the poor and higher earnings for professionals, including for the growing number of public servants in a small middle class, ownership remains in the hands of the political elite and connected people.

Unemployment remained high at 26.7% in 2017, and at 36.3% in broader terms, and a large part of the population — 30.4-million (55.5%) — survives on less than R992 per person per month..

The picture is not all doom and gloom for industries such as the agriculture and agro-processing industries, where there has been a widespread liberalisation of markets, although the sugar industry is an exception. The fresh fruit sector has emerged as a strong exporter.

Although the downstream processing of sugar, dairy and fruit does not offer industrialisation opportunities, value-chain challenges remain. This includes continued support for the sugar industry, which raises the price of sugar for downstream producers. The dairy sector is concentrated, with the increasing presence of multinationals resulting in significant barriers for new entrants.

Mondliwa said the government needed to place reindustrialisation at the centre of its development strategy and to prioritise investment and support clusters and to open up the economy to small and medium business. For instance, a code of conduct for developing supermarket suppliers should be implemented.

"We need an economy that is more dynamic, competitive and sustainable, where innovation and productivity lead to better jobs, with high wages and where entry is supported," the report recommends. To do this, a new vision for reindustrialisation is needed as well as a political settlement that prioritises long-term investment in productive capacity and rewards effort and creativity rather than incumbency.

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