RETHINKING South Africa's macroeconomic policy approach

The need to respond to crises has driven momentous changes in macroeconomic thinking, said macroeconomics expert Dr Seeraj Mohamed at the first of a series of Macroeconomic Policy Dialogues hosted by the HSRC. Mohamed and fellow economists Gilad Isaacs and Alexis Habiyaremye argued that, contrary to the old, neoliberal view, pro-poor fiscal stimulus is critical for overcoming and preventing socioeconomic crises like that precipitated by the COVID-19 pandemic. South Africa's historical focus on economic stability should give way to structural macroeconomic policy goals centred on building an equitable society. By *Andrea Teagle*

Despite the global shift away from neoliberal macroeconomics, South Africa is still anchored in neoliberal economic thought, favouring macroeconomic stabilisation, fiscal austerity (constrained government spending to control debt) and minimal state intervention. This 'old view' is encapsulated by the Washington Consensus, according to macroeconomics expert Seeraj Mohamed at the HSRC's macroeconomic policy dialogue: 'Macroeconomics of reconstruction and recovery: Policy options beyond COVID-19?' The Washington Consensus reflected a 'one-size-fits-all' set of free-market policy reforms that the World Bank and the International Monetary Fund (IMF) promoted across developing countries in the 1980s.

A feeding scheme in Vrygrond, Cape Town, during the lockdown. Macroeconomics experts emphasise the need for pro-poor, targeted stimulus packages together with poverty-reduction programmes to build a more resilient economy.
Photo: *Andrea Teagle*

Mainstream economic organisations, including the IMF, have since recognised the shortcomings of a narrow focus on stability, said Gilad Isaacs, a director at the Institute for Economic Justice. By the late 90s, it was widely recognised that neoliberal policies had largely failed to alleviate poverty and inequality. In its 2006 interim report, the IMF-World Bank development committee stated that:

'In a developmental context, fiscal policy serves as both an instrument of macroeconomic stabilisation and as an instrument to achieve growth and poverty reduction objectives. In many developing countries, however, fiscal policy focus[ed] largely on the goal of stabilization. Correspondingly, growth and poverty reduction objectives were under-emphasized.'

In fact, according to Mohamed, the neoliberal push to privatise elements of the care economy – basic services, education and health – has caused deep inequalities in many developing countries.

"Now we're seeing the state, in many countries including our own, having to step in and deal with not only the problems of the pandemic and the economic consequences of the pandemic, but a cumulative range of problems that have developed over a long period of time."

Stimulation packages

Many countries, including South Africa, scrambled to keep their economies afloat during the pandemic through fiscal stimulation packages.

Fiscal packages aim to stimulate the economy by encouraging an uptick in consumption. In the medium term, prices will adjust to reflect the increase in money supply. However, proponents of fiscal stimulus argue the initial expansion of goods and services in response to the stimulated demand has its own long-term impacts, Alexis Habiyaremye, former senior research specialist at the HSRC, explained.

This approach is frowned upon by neoliberal theory. Neoliberalist thought holds that monetary policy should dominate fiscal policy, which should be used only in the short run, if at all, Mohamed said.

The neoliberal argument against fiscal stimulus is that people might not respond by consuming more goods and services. Anticipating tax hikes, they might choose to save instead, sending the economy into a deeper slump.

Habiyaremye said cash injections are most effective when targeted at low-income groups whose spending, even on basic goods and services, is constrained, and who do not pay taxes. However, the government has not invested in deliberately pro-poor macroeconomic stimulus packages.

In a newly published UNU-Merit discussion paper, Habiyaremye and colleagues examine the experiences of 10 developing countries who implemented stimulus packages after the 2007-2009 Great Global Recession. The team, which also included the HSRC's Dr Peter Jacobs, found that fears of sustained inflation did not play out. Except for Kenya, the countries (spanning Africa, East Asia and Latin America) experienced a relatively small increase in short-term inflation that settled in the medium range of their inflation targets.

However, during the virtual policy dialogue, Habiyaremye emphasised that injecting money into the economy does not necessarily reduce poverty if it is not accompanied by existing poverty-reduction programmes.

Even pro-poor, targeted stimulus packages are not enough; rather, they should form part of the foundation of an equitable post-COVID economy, responsive to the needs of local communities, write Habiyaremye and his colleagues.

Sustainable level of borrowing?

"What are some kinds of guidelines, rules of thumb or just sensible thinking as to what are sustainable levels of borrowing?" asked dialogue discussant Prof Fiona Tregenna, the DST/NRF South African Research Chair in Industrial Development.

Measuring the sustainability of borrowing extended beyond simply the resulting GDP growth minus the cost of borrowing. The speakers agreed that critical to the question of sustainable debt was how the government allocated its limited fiscal resources. Although categorised as consumption, expenditure on basic services such as education could be viewed as a socioeconomic investment towards a more equitable future. Money spent on infrastructure and public capital goods is more likely to have long-term impacts by changing the structure of the economy.

"We don't have [debt] levels that are outrageously high; what we have are costs that are higher than global averages," Isaacs said.

In the 2006 interim report, the IMF and World Bank note that 'there is no simple relationship between debt and growth... . Moreover, there is no single threshold for debt ratios that can delineate the "bad" from the "good"'.

Mohamed observed that developed countries were revisiting the assumption that the central bank should remain independent: since the 2007–2009 financial crisis, central banks were increasingly financing government spending directly. He charged that the South African government was hindered by an unwillingness to undertake real macroeconomic analyses, or to consider alternative perspectives to old mainstream economic thinking.

Drawing on results from the UNU-Merit discussion paper, Habiyaremye argued that the government should seek to reach an agreement with the private sector to jointly finance the stimulus, with a view to reducing enduring unemployment and restructuring the economy equitably.

New macroeconomic goal?

Isaacs argued that South Africa needs a new macroeconomic goal to replace that of stabilisation. "Macro policy should be about an overall vision for transforming the form of the economy as a whole, and not simply stabilising the existing economy."

Macroeconomic policy guided by stabilisation has resulted in pro-cyclical spending, alongside a restrained monetary policy regime characterised by inflation targeting, he said.

"What this has led to is a potential disconnect between the objectives being advanced in other policy areas, like industrial policy… and in labour market policy."

He said South Africa needed to align its macroeconomic policy with its other policy imperatives, and that possible future macroeconomic goals might be poverty alleviation, decent work and structural transformation.

Structural transformation

While the growth period of 2003–2007 before the recession has been upheld as a success of South Africa's macroeconomic policy, Mohamed argued that the type of growth that occurred was "hugely negative" for the people. The expansion of the financial sector relative to the economy as a whole – a process called financialisation – fuelled GDP growth, but also saw a contraction in employment.

"When we talk about the financial sector being advanced and developed in South Africa... advanced for what?" he challenged. "Developed for what? Does it actually increase our systemic risk [the risk that the financial sector collapses]? Has it helped us build an inclusive economy?"

Referring to efforts to respond to the economic impacts of COVID-19, Mohamed added that the same applies to business confidence. "What does … getting South African businesses to invest more in this current period actually mean? Is it going to solve unemployment problems?"

Shifts in the global economy, driven by the technological advancements of the fourth industrial revolution, required that South Africa examine its role within global value chains and the global division of labour, said Mohamed.

The speakers agreed that COVID-19 had demonstrated the need for South Africa to critically challenge its traditional macroeconomic thinking and create a blueprint for how to move towards a more resilient, inclusive, and sustainable economy.

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Note: *The webinar was part of an HSRC dialogue series promoting evidence-informed solutions to diverse macroeconomic puzzles hindering transformational development in South Africa, our continent and beyond. The dialogues also aim to strengthen cooperation with policy practitioners, academia and non-governmental stakeholders.*

Click here to watch the second Macroeconomic Policy Dialogue: 'The new macroeconoic paradigm: What does it mean for South Africa?"

LOOK OUT FOR THE UPCOMING DIALOGUES:

30 September 2021:
'South Africa's long-term economic policy options beyond 2021' with speaker, Prof Asghar Adelzadeh, and discussant, Dr Pali Lehohla

21 October 2021:
'How financialisation affects SA's macroeconomic policy options'

16 February 2022:
'Fiscal policy and industrialisation in SA: Macroeconomics of the infrastructure budget'

Further reading:

Macroeconomic stimulus packages and inequality in developing countries: Lessons from the 2007-2009 crisis for South Africa, by Alexis Habiyaremye, Peter Jacobs, Pelontle Lekomanyane and Olebogeng Molewa, *HSRC Review*, April 2020

Rethinking growth-unemployment puzzles in the COVID-19 recession: Contextualising SA's macroeconomic policy options, by Peter Jacobs, Pelontle Lekomanyane and Karabo Nyezi, *HSRC Review*, July 2020