AN EVALUATION OF MACROECONOMIC POLICY IN THE DEMOCRATIC ERA*

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The term "macroeconomy" is a relatively new term in the vocabulary of economists. It was "coined" as part and parcel of the Keynesian revolution in the 1930s ad 1940s. Before the Great Depression of 1929-1933, economists of the neoclassical school concentrated mainly on supply and demand on individual markets. In accordance with their dogmatic belief, the price mechanism operates in such a manner in competitive markets that all markets will be "cleared" and equilibrium prices will be established automatically. Consequently, they were convinced that the oversupply or undersupply – on both factor markets and on markets of final products –were temporary phenomenon and that equilibrium would be restored automatically on every single market and for that matter also in the economy at large.

The myth of neoclassical orthodoxy about the automatic trend towards market equilibrium was cruelly smashed during the Great Depression. Against all the predictions of the neoclassical economists, large-scale unemployment was experienced in all the great industrialised countries. In the early 1930s the unemployment rate in Germany was 40% of the labour force, in Britain and France 30% and in the USA 25%. To the discomfiture of the neoclassical economists, wage adaptations could not absorb the "oversupply" of labour. It was under these circumstances that J.M. Keynes published his *General Theory* in 1936. According to him the high levels of unemployment was the result of an "underemployment equilibrium" that has developed in the capitalist economies of the time. According to him the problem was of such a general or "macro" nature that it was futile to intervene in a single market (even the labour market) and that the problem could

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not be solved by price, wage or interest rate adaptations. (Many economists regarded Keynes after the publication of his book as a mad man. According to them it is completely impossible for an economy to experience "unemployment" and be in "equilibrium" at the same time. They regarded it as a *contradiction in terms*).

Keynes' explanation was that mass unemployment in the 1930s was not a labour market phenomenon but a *macroeconomic* phenomenon: i.e. a phenomenon that concerns the economy as a whole; i.e. as a "macro" or "comprehensive" entity. The word "macro" is often interchanging with "mega"[1]. According to Keynes an "underemployment equilibrium" exists when the Aggregate Demand (or the Total Spendings on consumption and investment in the economy as a whole) is too small to justify a Total Production (Aggregate Supply) large enough to employ the total labour force. In such circumstance the government must implement a macroeconomic policy (or a mega policy) to increase the Aggregate Demand (or the Total spendings on consumption and investment) to a level large enough to justify a Total Product (or an Aggregate Supply) large enough to employ the total labour force. His proposals were rather radical for his time. To emphasize the importance of increased public spending, he made the sarcastic proposal that the government should employ workers to dig trenches and to fill them up again as long as wages are paid to workers to increase Aggregate Demand. Keynes was someone who could think outside the "box". He broke away from the narrowness of neoclassical orthodoxy and from the myth that competitive markets are self-regulating mechanisms and that all markets will be cleared automatically.

It is important to remember that Keynes regarded the restoration of macroeconomic equilibrium (or stability) as a precondition to restore *full employment*. It is almost 70 years since the *General Theory* was published. The macroeconomic problems of today are very much different from the problems of

[1] *Macros* in Greek means great and *megas* means big.

the 1930s – especially in the developing countries. The unemployment problem of the 1930s was mainly a (temporary) cyclical problem, while the unemployment problem in developing countries is mainly a (rather permanent) structural problem in a situation of "underdevelopment", of balance of payment problems and of inflationary pressure. But in spite of these differences the restoration of macroeconomic stability in developing countries must also be to create conditions that will be – at least over the long run – conducive for job-creation and for a meaningful movement towards full employment.

Before we can evaluate the ANC's macroeconomic policy over the past 11 years, it is necessary to acknowledge the poor state of the modern sector of the South African economy in 1994 with special reference to the imbalances in the macroeconomic and fiscal situations. The period from 1974 to 1994 was a period of stagflation and creeping poverty. The average growth rate was only 1,7% annually and the per capita income declined by 0,7% annually. The level of unemployment (according to the broad definition) increased from ±20% in 1970 to ±30% of the potential labour force in 1994. During the tenure of the De Klerk government (1989-1994) the budget deficit increased from less the 3% of GDP to more than 9%! In this period total government debt increased from less than R100 billion to almost R250 billion (in current prices)[2]. In these circumstances it was, undoubtedly, necessary to implement measures to restore the macroeconomic fundamentals. The big question is whether the macroeconomic policy that was implemented, was the correct one. According to the proverb, there are more ways of killing a cat than drowning it in butter.

In 1993 the corporate sector and core ANC leaders reached a hugely important elite compromise. This happened before the transitional executive council (TEC) accepted a secret $850 million loan from the IMF to help tide the country over

[2] In mitigation to the De Klerk government we should acknowledge that part of the increase represented the debts to the Bantustan governments while a part of the increased social spending on black communities was financed by increased borrowing.

balance of payments difficulties in November 1993. Before the TEC signed the loan agreement, the corporate sector and NP government on the one hand and ANC leaders on the other signed a secret protocol on economic policy. In the "Statement on economic policies" agreed with the IMF, the TEC committed itself to a neo-liberal, export-oriented economic policy, and a "redistribution through growth" strategy[3].

The "Statement" of 1993 reads like the wish list of a corporate sector desperate to resolve its 20-year-long accumulation crisis. It also reads like a curtain raiser for the GEAR strategy announced two and a half years later. The social crisis of abject poverty, structural unemployment and violent criminality – in which a least 50% of the population was trapped – is euphemistically described as "social backlogs". The corporate sector's myth that economic growth would "trickle down" to the poor is accepted as a self-evident. Strangely enough "structural" policies, to which the "Statement" refers, were not implemented. The promise that "all can share equitably … in durable growth" was preposterous if we take into account the deeply entrenched inequalities in socio-economic power and property between the bourgeois elite and the impoverished majority.

By agreeing in the "Statement" to contain expenditure, not to increase taxes, to maintain fiscal balance, and to lower the government deficit in order to prevent the danger of macroeconomic populism and to attract FDI, the ANC committed itself – before the election of 1994 – to a macroeconomic and fiscal policy that clearly excluded a comprehensive redistribution policy for addressing the predicament of

[3] The "Statement" contains the following passage: "Monetary policy has carried much of the burden of SA's adjustment during the 1990s … An easing of [the strict] monetary policy would have risked a further undermining of [international] confidence and a resurgence of inflation … To redress social backlogs, SA's economic policies must be driven by the objective of durable [economic] growth *in which all can share equitably*. This will require political stability and a package of *macroeconomic* and *structural* policies that address the problems of high unemployment and weak investment, respect financial restraints, and promote [international] confidence in the country's economic management … There is widespread understanding that increases in the government deficit would jeopardise the economic future of the country … [and that] given the importance of maintaining a competitive tax structure … [fiscal policy] will emphasize *expenditure containment* rather than rising taxes … It is [also] recognised that unless social needs are addressed in a responsible manner socio-political stability would be difficult to sustain… Trade and industrial liberalisation will be an important part of the restructuring of the economy" (TEC, Statement on economic policies, reprinted in *Business Day*, 24 March 1994).

the poorest half of the population. Although no one could have favoured macroeconomic populism, it would have been possible to attain both fiscal balance and comprehensive redistribution by increasing both government spending and taxation. However, the sharp *inequalities* in the distribution of income and property were not acknowledged in the "Statement". But what is perhaps the most important omission, is that the sharp structural division between the "first" and the "second" economies was not acknowledged in the "Statement" at all. The policy framework that was accepted was to restore the "macroeconomic" fundamentals of the "first economy" with the implicit hope that "economic growth" in the "first economy" will automatically "trickle down" to the "second economy". When that "Statement" was accepted a "First World" mindset and the neoliberal ideology of the British-American world were shaped in the heads of the new powers to be. With the knowledge of hindsight we can allege that a "First World" mindset and the neoliberal approach were in fact "cast in stone" in the minds of the powers to be. It is 11 years later, but the cat is still killed by drowning it in the same butter.

When GEAR was announced in June 1996, the "First World" mindset and the "trickle down" myth became even more deeply ingrained in the policy approach of the ANC government. Over the past 11 years the package of fiscal and monetary constraints, of neo-liberalism and of a too quick globalisation process, succeeded to create macroeconomic stability in the modern sector of the economy. The promise that if we re-engage with the global capitalism it would create conditions conducive for the influx of foreign direct investment (FDI) equal to 5% of GDP did not materialise. The actual influx was equal to ±1% of GDP annually.

The macroeconomic stability attained was indeed conducive for considerable economic growth in the "First World" sector of the economy, but this "growth" did not "trickle down" to the poorer half of the population – i.e. to the inhabitants of the "second economy". The GEAR strategy dismally failed in its promise about the creation of job-opportunities and about redistribution to the poor via the private

sector. It is true that the economic growth rate of between 3% and 4% in 2004 created some additional job-opportunities in some sectors of the economy. But in a country in which unemployment (according to the broad definition) has increased from 30% tot 42% of the labour force, the gains attained in 2004 were far too little, too late and in all probability non sustainable.

Let us return to the macroeconomic policy over the past 11 years. If we looked at it in isolation the policy seems as if it was very successful. The rather serious fiscal and debt crisis of 1994 has been resolved; the balance of payments is now in a healthy state, while inflation has been brought under control. But we cannot look at the macroeconomic policy in isolation. In the economy of a country nothing happens in isolation. In the economy everything depends on everything else. A specific policy can have positive results, but there are always all kinds of hidden costs involved. To put the so-called macroeconomic fundamentals in place was by nature a painful process. The critical question is who carried the "pain" or the "costs" of restoring macroeconomic fundamentals? We can identify two "candidates".

Firstly, macroeconomic stability was attained by cutting back investment on infrastructural development. As a result huge infrastructural backlogs have developed that can hamper economic growth in the years ahead. There are, however, signs that the government realises the need for large-scale infrastructural investment. It would, however, not be easy to remove these backlogs – especially if the lack of capacity in the public sector is taken into account.

Secondly, a large part of the "pain" of the macroeconomic policy was shifted on the poorer half of the population. Although the government is not prepared to acknowledge it, the poor have had a rather raw deal since 1994. In an argument put forward regularly by the government or by the business community, it is claimed that it was necessary to restore government finances and macroeconomic stability *before* the government could spend greater amounts – or the highly needed amounts – on the poor. But while this argument is repeatedly used as an excuse for not spending *more* on the poor, the top third of the population became much richer, while the poverty of the poorer half of the population became deeper and even more entrenched. It is true that social spending as a percentage of non-interest spendings increased from 51% in 1992 to ±58% over the past five years. The question is, however, whether this increase in social spending was adequate to stop the process of pauperisation in the ranks of the poorer half of the population. The answer to this question is clear: the increased social spending was and is still inadequate - especially because the economic growth that was attained, turned out to be "jobless" and even "job-destroying" growth.

One of the most serious tactical mistakes made by the government over the past 11 years, is that it did not understand – or did not understand adequately – the *dynamic* character of the poverty problem in South Africa. Consequently they did not treat the poor with the necessary empathy and sympathy.

The poverty traps set during the apartheid period remain an important explanation for the persistence and for the worsening of the poverty situation in South Africa. But on top of this, the macroeconomic and other policies introduced by the ANC government created *additional* poverty traps for the poor. It is not possible to explain the deepening of poverty without taking these "new" traps into account. We can identify the following seven "new" poverty traps:

- Under the watch of the ANC, unemployment increased from 26% in 1994 to 30,5% in 2004 (in accordance with the official rate) and from 30% to 42% (according to the expanded definition); vulnerable workers lost their jobs because they were exposed to the cold winds of global competition after the government entered "globalism" "head over heals" instead of entering in a gradual and measured way; opportunities were created for exporters to make

huge profits by cutting back on their workforce and their labour account; "space" and "freedom" were granted to the corporate sector to change their production methods into a much more capital-intensive production method in which labour is replaced constantly by capital; the casualisation of many workers left them without the protection of the labour laws;
- Under the watch of the ANC, workers' share in the national income dropped from nearly 60% in 1992 to only 51% in 2002. (In a "normal" country workers' share is closer to 70%);
- Under the watch of the ANC, the HIV/AIDS problem escalated into a pandemic that is almost out of control – especially in the ranks of the poor.
- Under the watch of the ANC, crime and violence escalated to unprecedented levels and it is mainly the living patterns of the poor that are constantly disrupted by these high levels of crime and violence – especially because they are too poor to protect themselves against such predicaments;
- Under the watch of the ANC, a large part of the civil society (mainly in the ranks of the poor) have been demobilised to leave a large part of the poor without bargaining power at a time when pressure groups in the ranks of the (white and black) middle class are exceptionally well organised and in a position to influence government policy in their favour and to the detriment of the poor;
- Under the watch of the ANC, many services for the poor have been privatised in spite of the fact that the poor cannot afford to pay for these services. This alarming situation has been aggrevated by the many problems experienced in the delivery of services by the third tier of government;
- Under the watch of the ANC, the steps taken to close the huge educational and skills gaps have been rather unsuccessful.

In 1994 the poverty problem was already very serious. It was, undoubtedly the most awful part of the bad legacy that was bequeathed by the apartheid regime to democratic South Africa. Severe poverty in the ranks of the lower half of the population has already attained in 1994 an endogenous *dynamic* through which poverty was – and still is – spontaneously perpetuated and augmented. In 1994 poverty was already like a snowball rolling along a slope on its own momentum. The increased spending on social services led to a considerable increase in the "social wage" of a large part of the poor. This certainly delayed the rolling snowball in its downward track. But at the same time the "new" poverty traps to which the poor have been exposed over the past 11 years, have "quickened" the pace of the rolling snowball. On balance, the speed with which the snowball is rolling along the slope has accelerated. Consequently, poverty became deeper.

It is rather important to realise that the macroeconomic policy of the past 11 years was strictly speaking not a "macro" or a "mega" policy. It was a policy to restore the economic disparities in the "first economy", while neglecting the socio-economic disparities in the "second economy". Consequently, the economic situation in the "first economy" became rather healthy over the past 11 years, while the socio-economic disparities in the "second economy" became worse during the same period.

After 11 years of democracy the socio-economic destiny of the poorer half of the population – i.e. the inhabitants of the "second economy" – is still dependant on whether economic growth in the "first economy" will, *überhaupt,* have the alleged "trickle down" effect. We all know that it is dangerous to build a castle on sand. The ANC should have known better than to build its macroeconomic policy on the "trickle down" *myth.* Nobody ought to be surprised that the crisis of *poverty, unemployment and inequality* is presently more severe than 11 years ago in spite of the success the government attained in putting the macroeconomic fundamentals of

the "first economy" in place. Hoogenveen and Özler[4] are rather explicit in their conclusion that "[economic] growth has not been *pro-poor* in South Africa as a whole, and in the instances when poverty declined for certain sub-groups, the distributional shifts were still not pro-poor" (p15).

Trevor Manuel expressed last week doubt about the correctness of Statistics South Africa figures that the unemployment rate (according to the broad definition) is 40%. He said that if 40% are unemployed and without income there ought to be a revolution. The minister ought to be very careful not to deny the severity of the unemployment and the poverty problems. Both these problems have deteriorated over the past 10 years and if this downward trend is maintained for another 10 years, we can indeed experience social instability, class struggle and even a revolution. The fact that the socio-economic situation is still relatively stable in spite of severity of the socio-economic problems can, *inter alia,* be attributed to the role extended families are playing – in especially black communities – to make poverty more bearable for unemployed members of these families. Given that no safety net is available for millions that are unemployed, these able bodied individuals, between the ages of 14 and 60/65, survive on the grants of the children, the disabled and the elderly members of the extended family of which the unemployed are members. This is an unhealthy situation, because the grants are supposed to support the individuals to which they are paid.

The ANC promised the electorate in its Election Manifest (for the 2004 Election) to reduce the levels of both poverty and unemployment by half in 2014. It is, unfortunately, not clear what exactly is meant by this promise[5]. Charles Meth estimated that under the most optimistic conditions 5,8 million jobs would have to be created between 2004 and 2014, while under pessimistic assumptions 11 million

[4] Hoogenveen, J.G. and B. Özler, (2004), *Not Separate, Not Equal: Poverty and Inequality in Post-apartheid South Africa,* The World Bank. Unpublished Manuscript.

[5] The halving of the unemployment rate would depend, according to Charles Meth, on the behaviour of three variables: the rate of growth of the potential labour force, the rate of change of the participation rate and the rate of economic growth and employment creation. See the article of Charles Meth, *A pig with wings?The ANC's employment halving goal,* School of Development Studies, KwaZulu Natal University, December 2004.

jobs would have to be created to half the rate of unemployment according to the expanded definition. Under "average" assumptions 8,4 million jobs will have to be created. We can assert, with a high level of certainty, that if the corporate sector and global corporatism retain their influential position in economic policy-making and if the government continues with its present policy measures of neo-liberalism and globalism, the target of creating 8,4 million jobs from 2004 until 2014 will in all probability not be attained. If the government also were to remain unprepared to spend a higher percentage of GDP on social grants and poverty alleviations, then the socio-economic position of the poor will be – to say the least - extremely precarious in 2014.

The ANC seems to be quite content that the macroeconomic and other economic and social policies are the correct ones and that no new policy initiatives are necessary. In his speech in Parliament on 11 February 2005, President Thabo Mbeki expressed almost boundless optimism about the government's policy programmes and about the future of South Africa. According to him:

> "... our country, as a united nation, has never in its entire history enjoyed such a confluence of encouraging possibilities. On behalf of our government, we commend our programme to the country, confident that its implementation will help to place us on the high road towards ensuring that we become a winning nation and that we play our role towards the renewal of Africa and the creation of a better world.
>
> Acting together, we do have the capacity to realise these objectives. And sparing neither effort nor strength, we can and shall build a South Africa that truly belongs to all who live in it, united in our diversity!"

Trevor Manuel echoed this optimistic tone in his Budget Speech on 23 February 2005. He not only quoted the above phrase from the President's speech, but also described the government as one "that cares for its people, that makes socially just choices and that is committed to service delivery in the spirit of *batho pele*".

If we take account of the socio-economic crisis in the ranks of the poorer half of the population and also of the improbability that poverty and unemployment will be reduced by half in 2014, then the optimism expressed by Mbeki and Manuel must be rejected as unwarranted. It is indeed premature to allege that in a country in which 40% of the labour force is unemployed and in which 50% of the population is living in poverty, is on the high road to becoming a winning nation. Problems are not solved by this kind of optimistic rhetoric, but necessitate the acknowledgement of the true nature of these problems. An honest and profound analysis (or diagnosis) of the extent and core reasons for these problems are a *sine quo non* before a viable solution can be attained. Our problems of unemployment, poverty and inequality are severe enough to inspire us to think outside the "box" - as Keynes has done in the 1930s when challenged with the unemployment problems after the Great Depression. And like Keynes, I too realise that is would not be easy to change the mindset of the political and economic elite in South Africa and to cleansed them from the myths on which their approach is based. But given the severity of our social problems and the systemic nature of these problems, we have no choice but to think loudly – and outside the "box" – about the necessity of rather sweeping changes in the ideological, the policy and the systemic approach of the policy elite.

President Mbeki has acknowledged in October 1993 that there is no staircase between the "first economy" on the top floor and the "second economy" on the ground floor of South Africa's two-storey building. By acknowledging this, he in effect granted that the "trickle down" effect is nothing but a myth.

The government has promised on several occasions during the past 18 month, that special interventions into the "second economy" will be undertaken to rectify the alarming situation in the "second economy". The acknowledgment that the government will have to play an entrepreneurial role in the "second economy" is rather promising. Unfortunately, the government's ability to intervene in the "second economy" is very much hampered by the lack of capacity in the public sector. But what is perhaps of greater importance, is that it will be contra-productive to intervene in the "second economy" while the "structure", the macroeconomic policy and the neo-liberal privileges granted to the corporate sector remain intact in the "first economy". It is highly necessary to move towards a *truly developmental state system* in South Africa. But this system cannot be created in the "second economy" only. It will have to be created in the South African economy as an undivided entity. It is, therefore, necessary to award the highest priority possible to the building of capacity in the public sector and to think very deeply about the implications a genuine movement towards a *truly development state system,* will exert on our macroeconomic, our neo-liberal and our global-orientated policies.