

**MISHAP OR CRISIS?
THE APARTHEID ECONOMY'S RECENT RECORD IN HISTORICAL PERSPECTIVE**

by

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"The last few years were among the most difficult we have experienced and called for sacrifices by one and all. But that those sacrifices were worth it is clear now: the economic tide has turned towards growth and development and we can justifiably look ahead with new confidence."¹

"... overpowering economic and political forces (have) combined to produce a comprehensive structural crisis for the apartheid economy ... That there is no hope for the apartheid economy is now no longer in question."²

Introduction

The South African economy has performed poorly in recent years. One line of interpretation views this poor performance as a severe and unfortunate cyclical down-swing, from which the economy is slowly recovering. Another, by contrast, regards it as symptomatic of an economic crisis; many variations between these views can be found. This is, of course, an ideologically loaded issue, since the "mishap" position is associated with the South African government, and the "crisis" view with its left-wing opponents, who foresee national economic recovery only once significant economic and political restructuring of society has taken place.

I shall begin by describing the recent economic record of South Africa, put it into a post-War context, and draw out some causes of the current decline. I will then consider whether the causes of decline are temporary/cyclical, or long-term, whether they are likely to weaken or worsen, and how the decline as a whole should be characterized.

The South African Economy Since World War II

To understand the economic prospects of South Africa, it is useful to examine its overall record since the Second World War.⁴ From the 1940s until 1974, an increasingly open and buoyant world economy, with high demand for South African raw materials, created ideal conditions for steady growth in the real Gross Domestic Product (see Graph 1). Foreign exchange earned was used to import capital equipment, and build up local manufacturing and technology behind tariff barriers. In the social sphere, vigorous state policies were designed to disorganize African workers and keep African wage levels low. While all sectors of the South African economy grew over this period, three overall tendencies were particularly significant:

Firstly, agriculture and mining, the foreign exchange-earning sectors of the economy, grew relatively slowly. Their shares of real output fell slightly, and of employment more quickly (with an absolute fall in agricultural employment). Secondly, the other goods-producing sectors (manufacturing, electricity, and construction) grew more rapidly than the economy as a whole, and their shares of

employment also grew steadily. Thirdly, output and employment in the tertiary sectors (especially government) grew steadily, with employment probably contracting only in the personal services sector (led by domestic service).

Since the early 1970s the situation has changed markedly. Whereas in the 1960s the Gross Domestic Product of South Africa grew faster than that of the average middle-income developing country, it has failed to keep pace with the rest since then.⁵ There has been a steady slow-down in rates of economic growth since 1974: real GDP growth rates have fallen to 1.5 per cent in the 1980s. Growth rates have diminished unevenly through the economy, however. Owing to rising and erratic world gold prices, mining earnings have boomed, while agriculture and manufacturing have struggled; since 1982, real manufacturing output and employment have been growing more slowly than the economy as a whole. The tertiary sector has continued growing, led chiefly by government. Growth rates of formal jobs over the business cycle peaked in the 1960s and have been falling since (see below).

Three Determinants of Economic Development in South Africa

Three central determinants of South Africa's economic record can be identified: the balance of payments, the performance of the manufacturing sector, and the employment situation. **Firstly**, the balance of payments has always been a potential constraint on growth in South Africa. Compared to most developing countries, however, South Africa has an unusually strong balance of payments situation. The usual pattern is of a trade surplus produced by raw materials (agriculture and mining) exports, much of which is "consumed" by industrial sectors being net users of foreign exchange, and large invisibles deficits (interest payments, royalties, etc). Capital inflows attracted by high profit rates have also been an intermittent source of savings and foreign exchange.

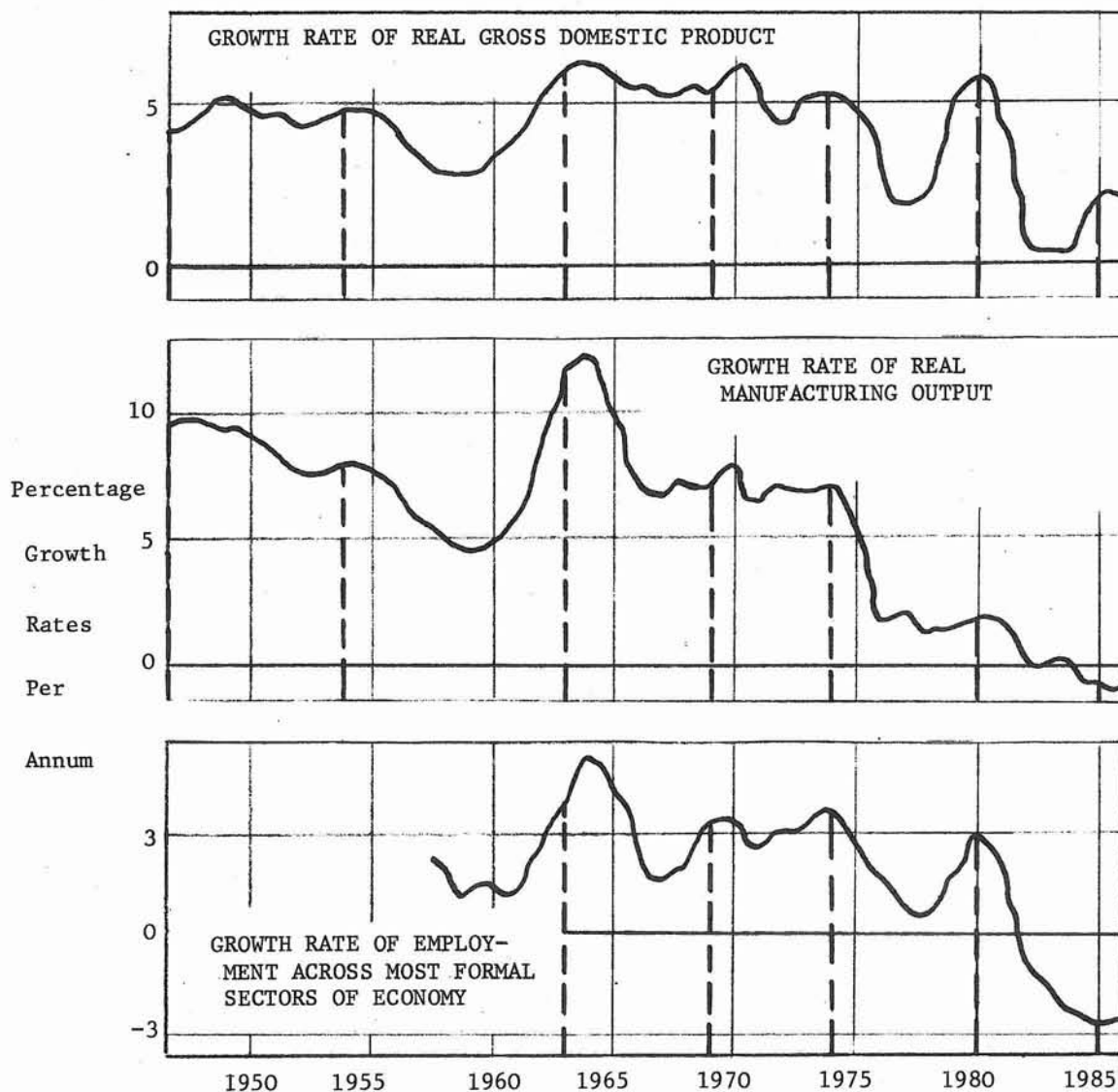
On the exports side, South Africa's position has not changed much post-War. South African exports have always comprised mainly raw materials, a small number of which come to a high share of total exports; the mining share in merchandise exports has averaged over 60 per cent. In imports terms, South Africa has been largely self-sufficient in consumer goods since the 1950s. The share of imported capital goods has risen since 1945, however, with machinery and transport equipment, for example, reaching 49 per cent of the imports total in 1985. Hence, although South Africa has built up a capital-goods industry, the strong historical value of the rand has permitted imported machinery to form a high proportion of capital goods used. As a result, balance of payments deficits have always tended to bite during boom periods in South Africa, with imports rising sharply, necessitating an eventual economic clamp-down and monetary contraction.

After 1971, the international gold price (which had been nominally constant in US dollars and falling in real terms since 1949) began rising, albeit erratically. This boosted mining revenues, eased South Africa's balance of payments constraint, and implied potentially higher domestic output growth rates if the extra income were to be used productively. The gold "bonanza" was squandered, however, and not used to extend South Africa's productive capacity significantly. So, when the gold price fell in the 1980s, the economy was suddenly weakened, with an exchange rate under pressure, a weakened manufacturing sector, and high foreign debts.

The vulnerability of South Africa's balance of payments is revealed in two main areas. Firstly, her current account is reliant on raw material exports and imports of manufactures. Non-gold net barter terms of trade - the ratio of export prices to import prices - remain stable during international booms but deteriorate during slumps. Further, her export earnings tend to be erratic, dependent on variable international raw material prices and agricultural fluctuations. Gold was a stabilizing factor until the early 1970s, but real gold earnings have fluctuated wildly since - though on a strongly upward long-run trend.

Secondly, the trade and capital accounts of the South African balance of payments have been opened up since the later 1970s, with state moves towards a "market-oriented monetary strategy", including financial deregulation, more variable

Graphs

Three Growth Indicators for South Africa,
1947-1986

Peak years of business cycles are indicated using dashed lines.

Note

Graphs are 3-year moving averages, data calculated from South African Reserve Bank sources, reworked as described in Moll, 'Best Lager'. Exponential growth rates between business cycle peaks are used. Sectors covered for employment are mining, manufacturing, electricity, commerce, transport and government services; this data is quite unreliable before the 1960s. Important omissions are agriculture, construction, and most business and private services.

and erratic interest rates, a more open balance of payments designed to encourage international trade and capital flows, and a floating and fluctuating exchange rate. This had two important effects: South African banks and the state raised foreign loans at (then) low real interest rates, which are now being repaid at much higher real rates, and allowed an important role for destabilizing short-term capital flows. These have rendered the South African economy, balance of payments and foreign exchange situation far more vulnerable to vicissitudes in the international economy in the 1980s, and also make it an easier target for sanctions.

A second important determinant of the long-run prosperity of the South African economy is the vitality of her manufacturing sector.⁶ South African real manufacturing output grew rapidly in the 1950s and 1960s, growth rates averaging over seven per cent per annum (see Graph 2 above). There were several reasons for these high growth rates: buoyant international demand and stable terms of trade, an active state import-substitution policy, and intervention in strategic economic sectors, cheap raw material and electricity inputs, capital controls compelling higher levels of local investment, and low black wages.

The record has negative aspects, however. The import-substitution programme combined with the strong currency led to a failure to export. International non-competitiveness of local production was accordingly entrenched via failure to achieve economies of scale and compete on international markets. Likewise, the industrial sector came to rely on protection and ever more advanced machinery imports, without the achievement of the full learning effects of producing a variety of capital goods for local use and for export.

Real manufacturing import levels as percentage of GDP failed to fall over the years, as South Africa moved "up" the imports scale, requiring increased inputs of imported machinery, transport equipment and technology to keep industry going. The "easy" stage of import substitution in local consumer goods, some durables and simpler machinery was basically complete by the early 1970s, with further scope for import-replacement limited to capital and intermediate goods and high-technology sectors.

In the 1970s, manufacturing growth began to slow, and rather half-hearted government efforts at stimulating exports and the processing of primary products have not been effective. The recent record has been particularly poor; according to the South African Reserve Bank, manufacturing volume of production in 1986 was 10.3 per cent below its 1981 peak. The manufacturing sector has begun to contract relative to other sectors (its share of real GDP had fallen from a high of 25.5 per cent in 1981 to 22.3 per cent in 1985), with inefficiencies and a limited internal market restricting local sales, and a strong exchange rate of the rand (until 1984) and trade sanctions limiting export growth. This is particularly unfortunate for an economy at South Africa's stage of development, as it implies slower future growth rates for the economy as a whole.

Thirdly, a major indicator of the health of any economy is the extent to which it can provide employment and incomes to its labour force. In these terms, South Africa's performance was impressive until the early 1970s. Employment in most of the formal, high productivity sectors of the economy grew steadily, with employment growth rates of 3.3 per cent per annum between 1964 and 1974 in those sectors for which more reliable official data is available (see Graph 3). African open unemployment rates seem not to have risen in the 1960s. Since then, the position has deteriorated drastically. Employment growth rates have fallen sharply in the past ten years, averaging only about one per cent per annum over the 1980-1984 cycle. At the same time, African population and labour-force growth rates have remained high, leading to a large and continually expanding pool of labour which is "surplus" to the needs of the modern sector of the economy.

To make the situation worse, the tendency since 1974 has been for industrial firms to increase capital use and labour productivity levels, rather than employment. This tendency is particularly noticeable in manufacturing, where output and employment growth rates averaged 2.9 per cent per annum and only 0.8 per cent per annum, respectively, over the 1974-1984 period. Commercial agriculture has been mechanizing and shedding labour since the 1960s, the mining sector cannot be relied

on to expand employment greatly, and construction employment seems unlikely to grow quickly. Commerce and private services not driven by a dynamic goods sector of the economy are unlikely to grow rapidly and raise worker incomes much. Rising government employment, on the other hand, is often of entirely unproductive bureaucrats, and constrained by a weak state fiscal position. In short, the employment outlook is bleak, and government efforts at stimulating the informal sector and labour-intensive employment are not likely to reverse employment trends.

Together, these employment trends have important implications. Unemployment and underemployment are likely to rise rapidly in the foreseeable future, as a rapidly growing labour force encounters a stagnant employment position in the economy. Increasing economic and social differentiation may emerge within the labour force, between people in high productivity, higher income jobs and the unemployed or underemployed. The services will be the main source of employment growth, led by petty trade and personal services, and the share in total employment of low productivity, low income casual workers and the self-employed will probably rise further.

Mishap or Crisis?

Various causes of South Africa's economic decline, since about 1974, and especially in the last six years, have been discussed above. Some are of a temporary or cyclical nature, most importantly those induced by vicissitudes in the world economy. These have forced many developing economies with structural similarities to South Africa to adjust to factors like falling raw materials prices, high interest payments on foreign debt, and short-term capital outflows. Some Latin American countries, for example, suffered far more from these adjustments than South Africa; over the crucial 1981-1985 period, South Africa grew at around one per cent per annum, compared to disaster in countries like Argentina (-2.1 per cent) and Venezuela (-1.3 per cent).

The South African economy has, in fact, adjusted relatively quickly to these "external" constraints, and most of its short-run weaknesses are being brought under control. As of early 1988, inflation rates were falling, the real exchange rate of the rand had recovered somewhat from its 1984-85 slump, foreign debts were steadily being paid off (using large current account surpluses of the balance of payments), and in some sectors signs of recovery were evident. Further, state macro-economic policy has begun turning away from the suicidal monetarist (high interest rates, free financial and other markets) policies of 1984-85, and the economy has begun making structural adaptations such that it should in the future be less vulnerable to changes in world economic conditions.

The most immediate danger is still the vulnerability of the balance of payments, but gold, uranium and coal exports will continue to provide valuable foreign exchange, and more cunning state balance of payments policy could enable the economy to benefit more from these earnings than in the recent past. This would be the case especially when the bulk of foreign debts have been paid off, reducing the necessity for large balance of payments surpluses, and inflation is seen as being under control.

To a significant extent, then, the poor economic performance of 1981-86 can be seen as a "mishap", as induced by an unfortunate coincidence of events which is unlikely to be repeated. But this is not the whole story. While the magnitude of the recent slump was magnified by external factors, the South African economy has been on a low-growth development path since the mid-1970s. Further, there are indications that the current political situation is having a particularly negative effect on the South African economy, on a scale not hitherto experienced.

Two major political-economic connections can be hypothesized in South Africa. Firstly, political "unrest" tends to lower investment levels and induce capital flight and balance of payments crises, leading to deflationary macro-economic policies, and slower economic growth. The logic seems simple: investors fear profits will be undermined by continual political struggle, with the added danger of possible eventual expropriation or nationalization of their investment.

under a radical government. To this can be added pressures on foreign firms operating in South Africa, owing to increasing anti-apartheid feeling in the West. Thus, real economy-wide growth rates of fixed capital stock of around 6.8 per cent per annum 1969-1974 have slowed down to 4.6 per cent 1980-84 - a period in which the capital:output ratio rose by around two per cent per annum and is likely to increase in the future. This decline is even more noticeable in manufacturing, with a comparable drop from 8.3 per cent to 4 per cent.

These patterns have been particularly noticeable in South Africa since the 1984/85 stage of Black resistance. The balance of payments suffered first, and real gross domestic fixed investment has fallen steadily since a peak in 1981 (halving in manufacturing by 1986), and real net domestic investment by private firms in 1985 and 1986 was negative, for the first time in South Africa's history!¹⁰

Secondly, in the early post-War period, the apartheid system may have aided economic growth in South Africa. Its fiscal costs were low and it encouraged rapid capital accumulation by ensuring a cheap, unskilled labour supply for White firms. By the late 1960s, this position had begun changing. The production pattern in the economy as a whole was moving increasingly towards higher-wage skill and capital-intensive sectors which are less dependent for survival on cheap, unskilled Black labour, and the labour controls they suffered prevented the dissemination of skills and hampered productivity growth.

At the same time, the recent fiscal costs of apartheid have soared in areas like defence, homelands, administration, and black education.¹¹ The net effect of these processes is that the total financial costs of apartheid are rising steadily in a period when the state can ill afford them, thus compelling it to raise taxes or loans to cover spending, or reduce expenditure in other areas. This, perhaps irreversible, combination of falling benefits and rising costs of apartheid over an extended period of time is unique to the current phase of South African history.

The South African economy has endured such a severe slump recently that any increase in demand is likely to raise output and employment, and investment levels will partially recover from the doldrums. However, such expansion is likely to be cut short owing to the slow growth of aggregate productive capacity in the 1980s, and the inflexibilities and costs associated with the apartheid economy can only rise further. Extrapolating recent economic trends in South Africa, it seems unlikely that total output will grow faster than perhaps two per cent per annum over the next decade, and real incomes per capita are likely to fall steadily.¹² Growth projections for the 1986-1990 period of 3.2 or 3.3 per cent per annum¹² seem unrealistically high.

The long-term prospects of the South African economy under the present regime are also unpromising. For a developing country, the structure of the economy is not healthy - most noticeable in the weak manufacturing sector, in South Africa's appalling recent job-creation record, in a weak state finance position (affecting investment in infrastructure and parastatals), and in the relatively poor performance of employment-creating, small-scale manufacturing and services over the past few years. Meanwhile, the world economy is growing only slowly, and has begun moving away from some of South Africa's raw material exports. South Africa will attempt to export manufactures, but faces stiff competition from other newly industrializing countries, and may be hamstrung by looming trade sanctions. Further, foreign capital and finance are increasingly suspicious of the South African situation, and South Africa will be forced to survive largely without new inflows of foreign capital. This is likely to reduce the long-run growth rate by at least two per cent per annum, especially if accompanied by diminished access to foreign technology and skills.¹³

In short, then, neither of the extreme positions quoted initially seems correct. The South African economy is in a bad way - suffering what may be termed a secular recession. None the less, this need not imply economic "crisis" and a forthcoming restructuring of accumulation processes in South Africa. The economic basis of white rule, while undergoing long-term decline, will certainly be able to provide comfortable incomes for most whites, and support a huge military-apartheid

apparatus for a long time yet. The economy has certain strengths - a strong food-producing sector, valuable mineral resources, a limited dependence on oil, a fairly developed manufacturing sector, some local technological know-how, and fair levels of local savings - which will enable it certainly to survive, and perhaps grow slowly, as long as effective large-scale trade sanctions are not applied.

Likewise, in broad political terms, the South African state's capacity to spend its way out of trouble in order to stabilize itself has become increasingly constrained by the poor overall economic climate, and its weak fiscal position. However, the argument that a "weaker" and more isolated economy will undermine the government's fiscal position, thus creating space for mass resistance, is questionable as it stands. Compared to countries like South Korea, Peru, and Zimbabwe, a relatively low proportion of government spending in South Africa is on the police and army.¹⁴ In times of real crisis, the state response to declining revenues would more likely be to lower spending on education, health, and welfare, followed by reducing infrastructural and homelands spending, while raising expenditure on the military and police - suicidal in the long run, perhaps, but a strategy quite capable of overcoming any short-run military and civil threat.

Towards a Laager Economy?

The South African economy is weakening slowly, but its resilience and capacity to adjust to changed circumstances should not be underestimated. Indeed, this could be put to the test over the next few years. Under the impact of sanctions and external vulnerability, there have been moves amongst South African economic policy-makers towards a "laager economy": reducing economic links with the outside world and attempting to become economically more self-sufficient - and hence freer from outside political pressures.¹⁵ This makes a virtue of necessity, for South Africa can no longer rely on foreign capital inflows, and some trade links are threatened. Instead, the local manufacturing sector will be relied on to provide the necessary machinery, capital goods and technology to keep the economy and military establishment functioning, perhaps with higher parastatal spending or vigorous investment incentives to raise investment in vital manufacturing sub-sectors.

The laager direction would further entrench economic decline in South Africa. Most obviously, inefficiency and clumsy government intervention in the economy would be perpetuated, raising production costs and lowering output growth rates in many economic sectors. In some industrial sectors, capital-intensive methods of production would be further entrenched, and dependence on erratic mining revenues would remain. Corresponding to this would be low rates of formal job-creation and steadily rising unemployment in all sectors and regions of South Africa, and generally falling real incomes.

This "backs-to-the-wall" option could have ominous political implications. Among Whites, a lengthy period of economic decline, with White morale bolstered by nationalism, anti-Communist feeling and state propaganda, might strengthen conservative groups and weaken the position of those who want to see an end to the system of White political supremacy. Such an economic and political environment would render progressive political organization among Blacks even more difficult than at present. In the absence of major new political initiatives, however, the resilience of the South African economy could allow such a situation to be perpetuated for many years.

- 1 Barend du Plessis, South African Minister of Finance, in 1987/88 Budget Speech, reported in South African Digest, 12.6.87.
- 2 Vella Pillay, "Rising Cost of Apartheid: the economic crisis", in Southern African research and Documentation Centre (ed), Destructive Engagement (Harare: Zimbabwe Publishing House, 1986), pp 223, 243.
- 3 This, often-used concept is rarely defined in the South African context. I follow Wright who suggests economic crisis "implies that in order for accumulation to continue some sort of restructuring of the accumulation process is necessary". Eric Olin Wright, Class, Crisis and the State (London: New Left Books, 1978), p 125.
- 4 Space limits reporting of data, methodology and references in the text. These are discussed in my "'Probably the Best Lager in the World': the record and prospects of the South African economy", in John Brewer (ed), Five Minutes to Midnight: How long will South Africa Survive? (Macmillan, forthcoming); and "Growth Without Development: the South African economy in the 1950s", delivered at a Conference on South Africa in the 1950s, Queen Elizabeth House, Oxford, 25-26 September 1987.
- 5 See World Bank, World Development Report 1982 (Oxford, 1982) p 112.
- 6 See Martin Fransman, "Capital Accumulation in South Africa", in Fransman (ed), Industry and Accumulation in Africa (London: Heinemann, 1982), pp 243-59; also Fransman, "The South African Manufacturing Sector and Economic Sanctions" (Geneva: International University Exchange Fund, 1980), pp 23-30.
- 7 See Trevor Bell and Vishnu Padayachee, "Unemployment in South Africa: trends, causes and cures", Development Southern Africa, 1.3/4, 1984; Trevor Bell, "Issues in South African Unemployment", South African Journal of Economics, 53.1, 1985, pp 24-25.
- 8 The post-1981 economic record of South Africa is analysed by Jesmond Blumenfeld, "Economy Under Siege", in Blumenfeld (ed), South Africa in Crisis (London: Croom Helm, 1987), pp 30-32.
- 9 Calculated from Inter-American Development Bank, Economic and Social Progress in Latin America (Washington, 1987), p 17.
- 10 South African Reserve Bank, Quarterly Bulletin, June 1987. Real fixed capital stock growth rates for 1984-86 were 1.8 per cent per annum for the whole economy, and -2.1 per cent per annum for manufacturing.
- 11 See Michael Savage, "The Cost of Apartheid", Inaugural Lecture (Sociology), University of Cape Town, 1986.
- 12 Pamela Freer, South Africa to 1990, update (London: The Economist Intelligence Unit, 1986), p 93. N J Barnardt and J du Toit, Macroeconomic Forecast for South Africa 1986-1991 (Stellenbosch: Bureau for Economic research, 1986), p 28.
- 13 T Malan, "Economic Sanctions as Policy Instrument to Effect Change - the case of South Africa", Finance and Trade Review (Volkskas, Pretoria, 14.3.1981), pp 95-98.
- 14 See broad comparisons in World Bank, World Development Report 1986, pp 222-23. In South Africa, this proportion reached a peak of 20.6 per cent in 1977/78 and fell thereafter, but has begun rising again.
- 15 See Pieter le Roux, "The State as Economic Actor: a review of the divergent perceptions of economic issues", presented at the Southern African Economy After Apartheid Conference, University of York, Centre for Southern African Studies, 29 September - 2 October 1986. Also Blumenfeld, loc. cit., pp 30-32.