

**Public finance and economic development
The South African case**

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"THE ROLE OF PBDs IN AFRICAN PARLIAMENTS FISCAL OVERSIGHT:
CONTRIBUTION TO THE AFRICAN DEVELOPMENT AGENDA"

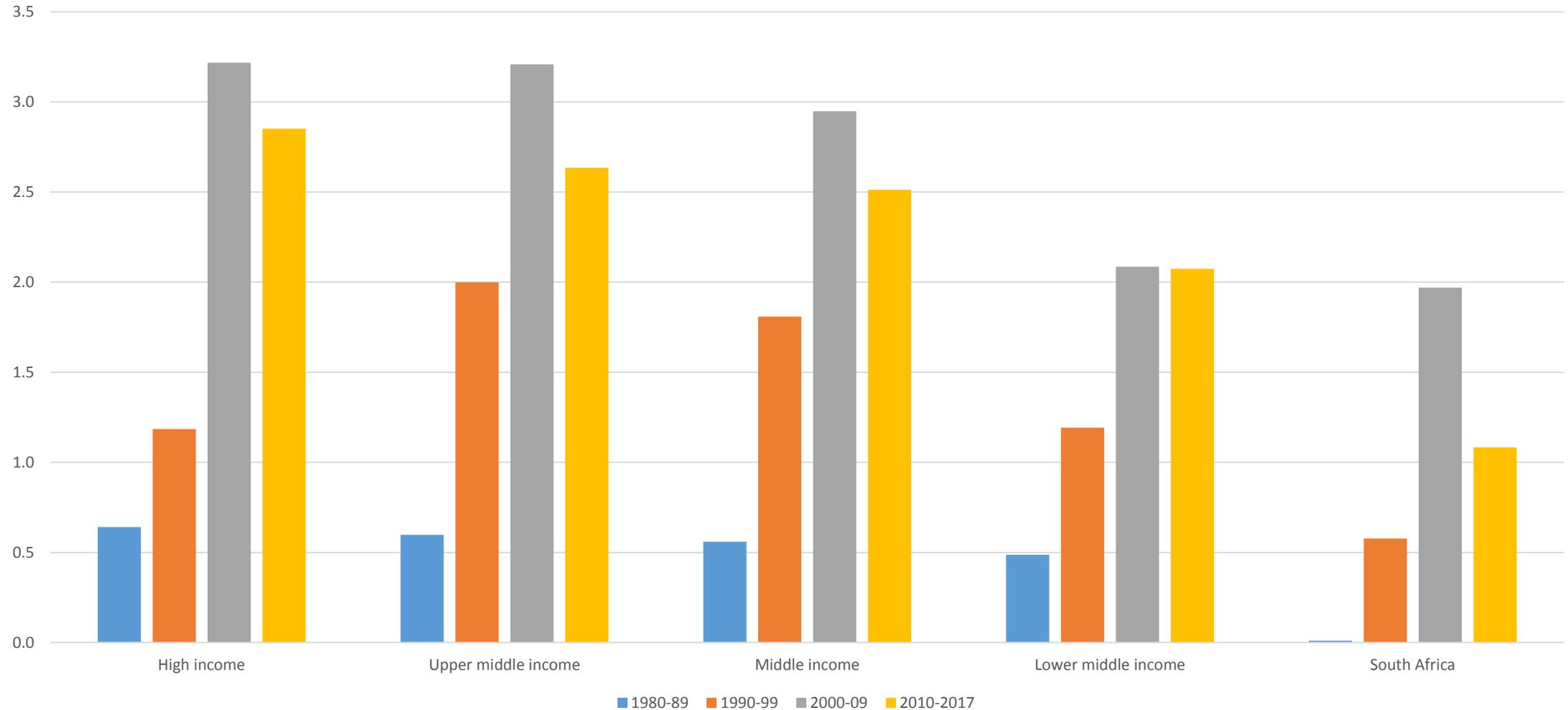
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Public finance and the developmental state

- The focus of the developmental state in this presentation is focused on deepening the industrialisation within countries and diversifying the productive base.
- Some of the role of developmental states:
 - Does not only fix market failures but is actively involved in market formation, and support innovation that can enhance productivity and growth
 - Manages rents and market concentration and control
 - The developmental state is directly and actively involved in economic sectors and markets alongside the private sector
 - Manages cross-border flows and protects the economy from contagion
- Therefore, the developmental state through its actions has the ability to support the growth of the economy
- Its economic activities, other than just revenue collection, can affect the sustainability of its budget activities

South African investment has been low compared to other countries

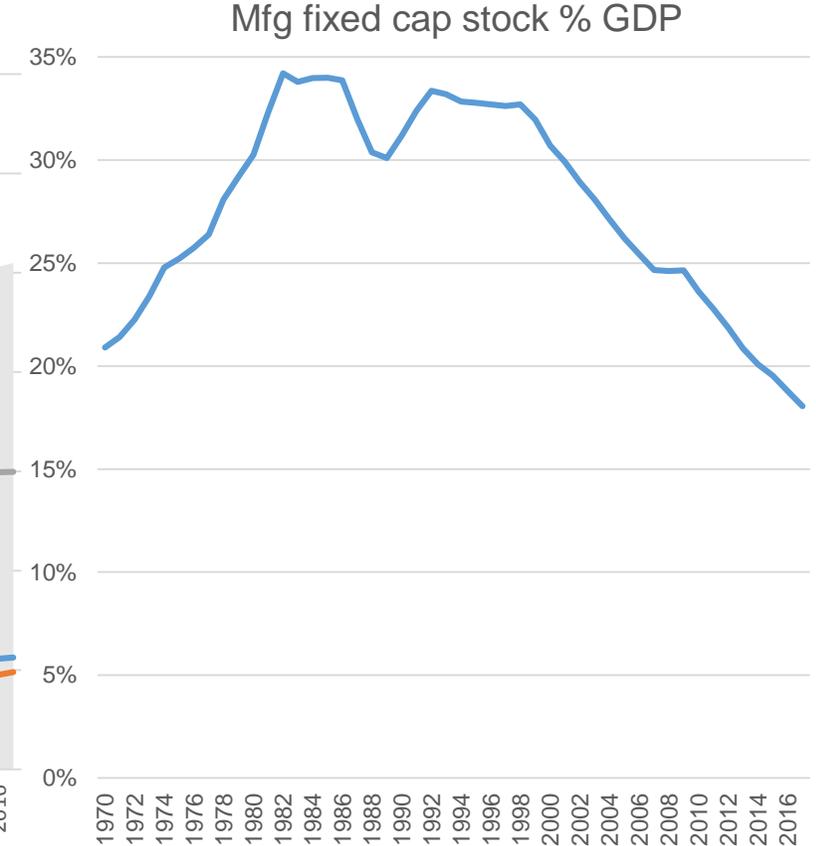
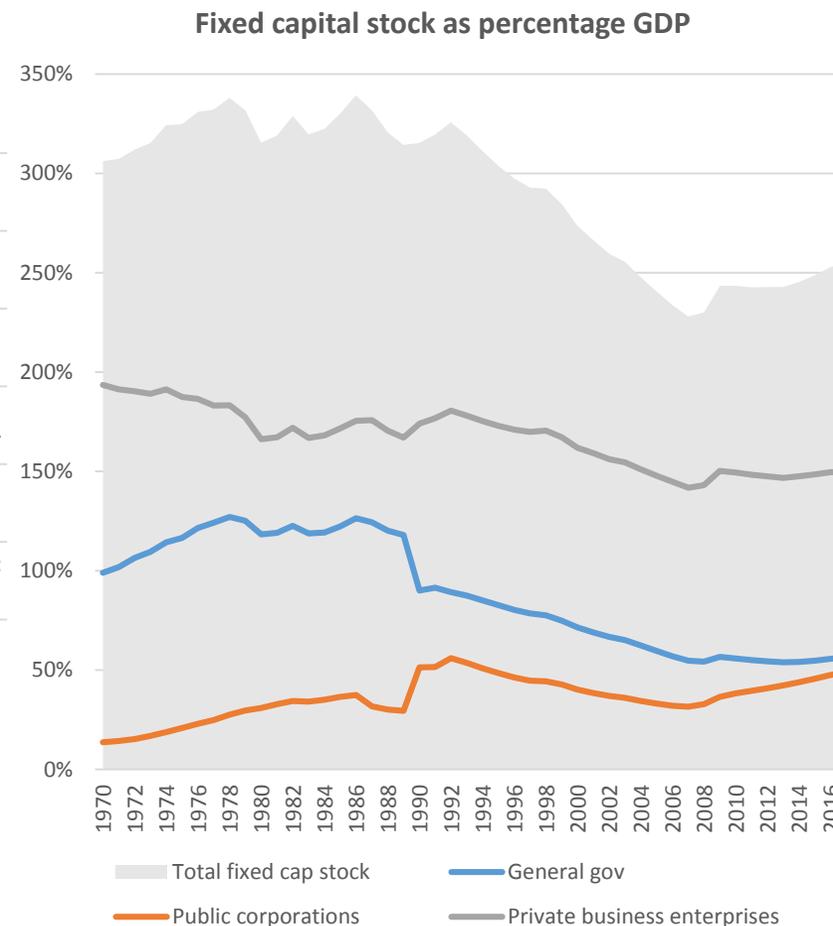
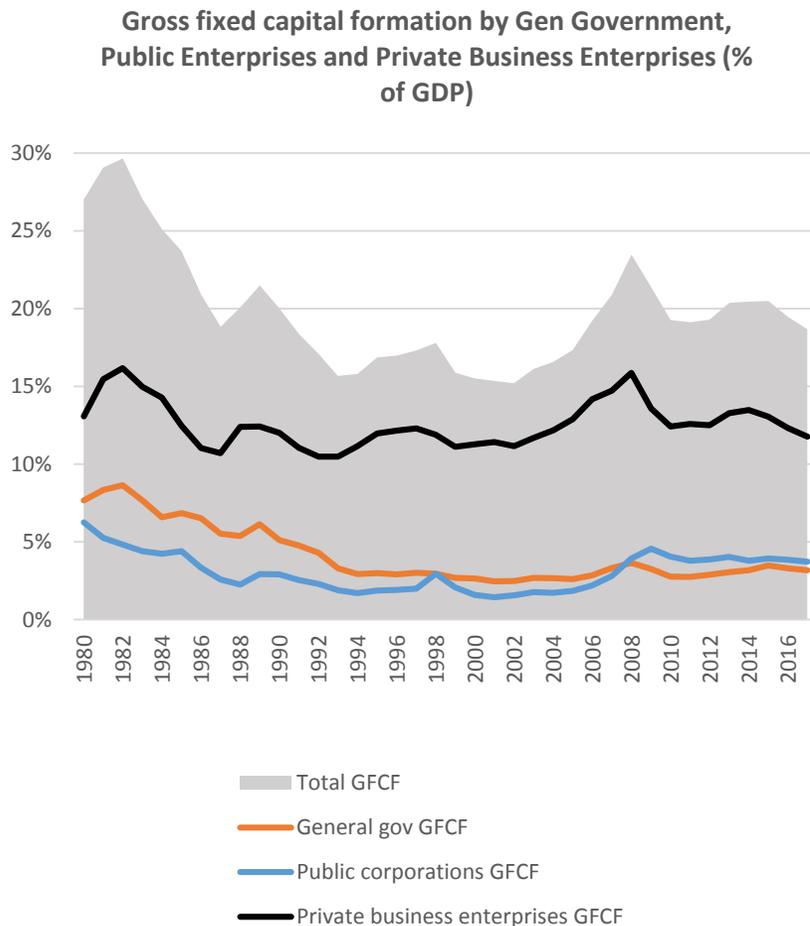
Investment (GFCF as percentages of GDP) comparing South Africa with average of country income groups



Source: WDI

Investment and accumulation in South Africa

- Public investment has been poor at under 5% each for gen government and public enterprises
- Private investment has returned to lows of the 1980s and 1990s
- Fixed capital stock as a percentage of GDP at lowest levels in decades

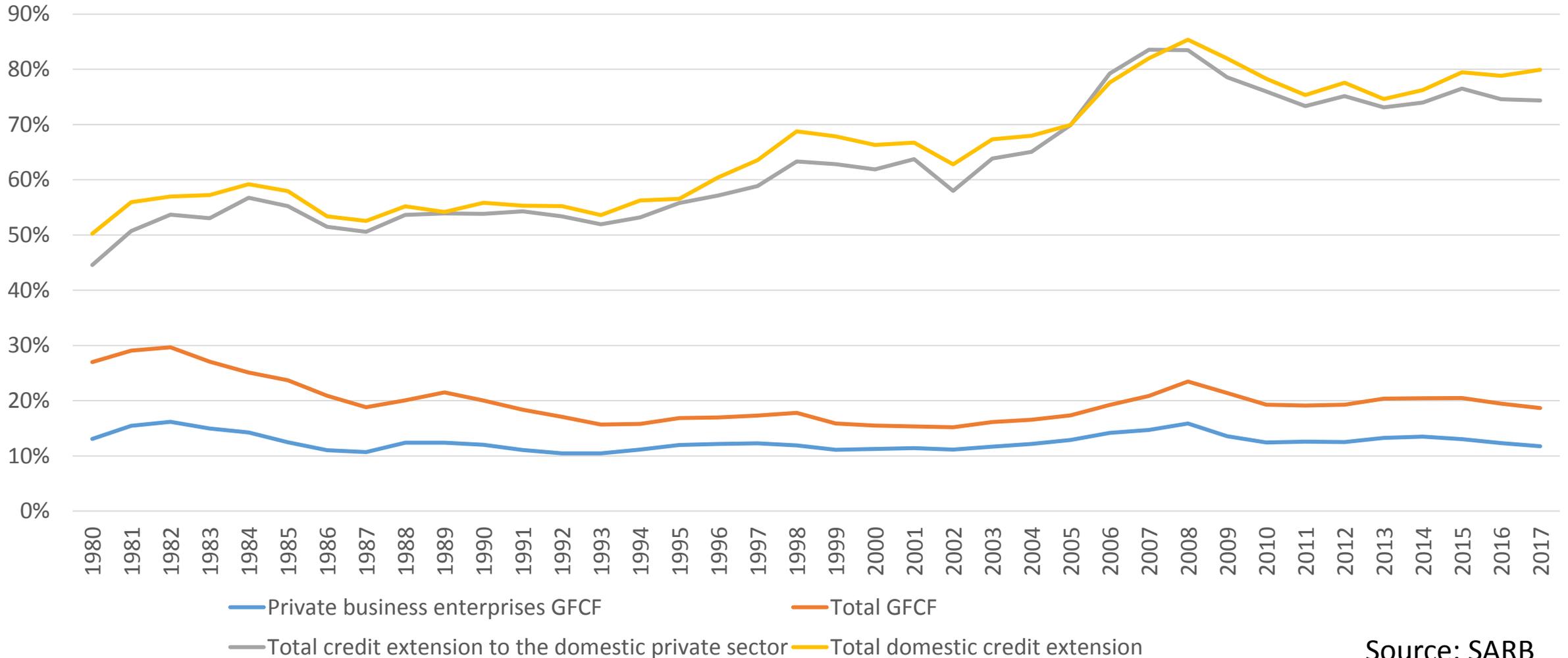


International debt and the current account deficit

- Many economists argue that investment is low because domestic savings is low, investment and link the current account deficit to this need for foreign capital inflows
- This understanding is often incorrect, and is wrong for South Africa:
 - South Africa has deep and sophisticated financial markets with internationally active financial institutions that are more than capable of financing domestic investment
 - What was referred to as foreign savings was actually foreign financial flows due to liquidity increases as a result of growing debt and quantitative easing
 - This liquidity searched for high, short-term returns in emerging markets and caused volatility and instability
 - The size of the current account deficit was significantly enlarged not because of the trade deficit but because of financial transfers associated with foreign capital inflows
- The foreign financial inflows to domestic currency bonds were not due to less domestic appetite but foreign funds searching for high returns
- Reduced quantitative easing and a credit rating downgrade will cause funds to flow out of South Africa
- But in low interest global environment appetite remains quite high

There has been large levels of credit extension to the private sector but low levels of investment

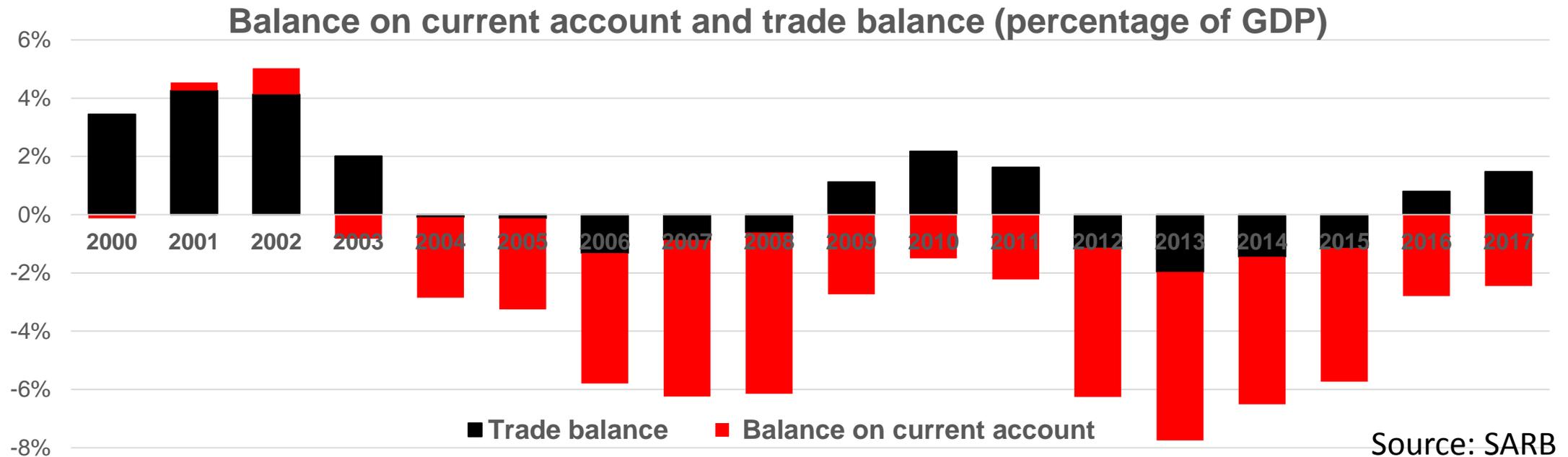
Comparing fixed investment to credit extension (percentages of GDP)



Source: SARB

Financial payments to foreign holders' of South African assets has been the main cause of large current account deficits not the trade deficit

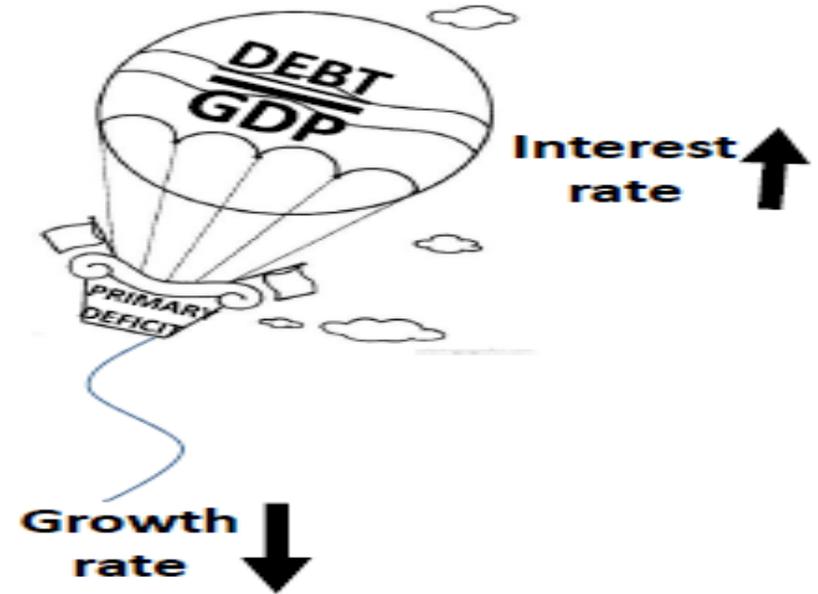
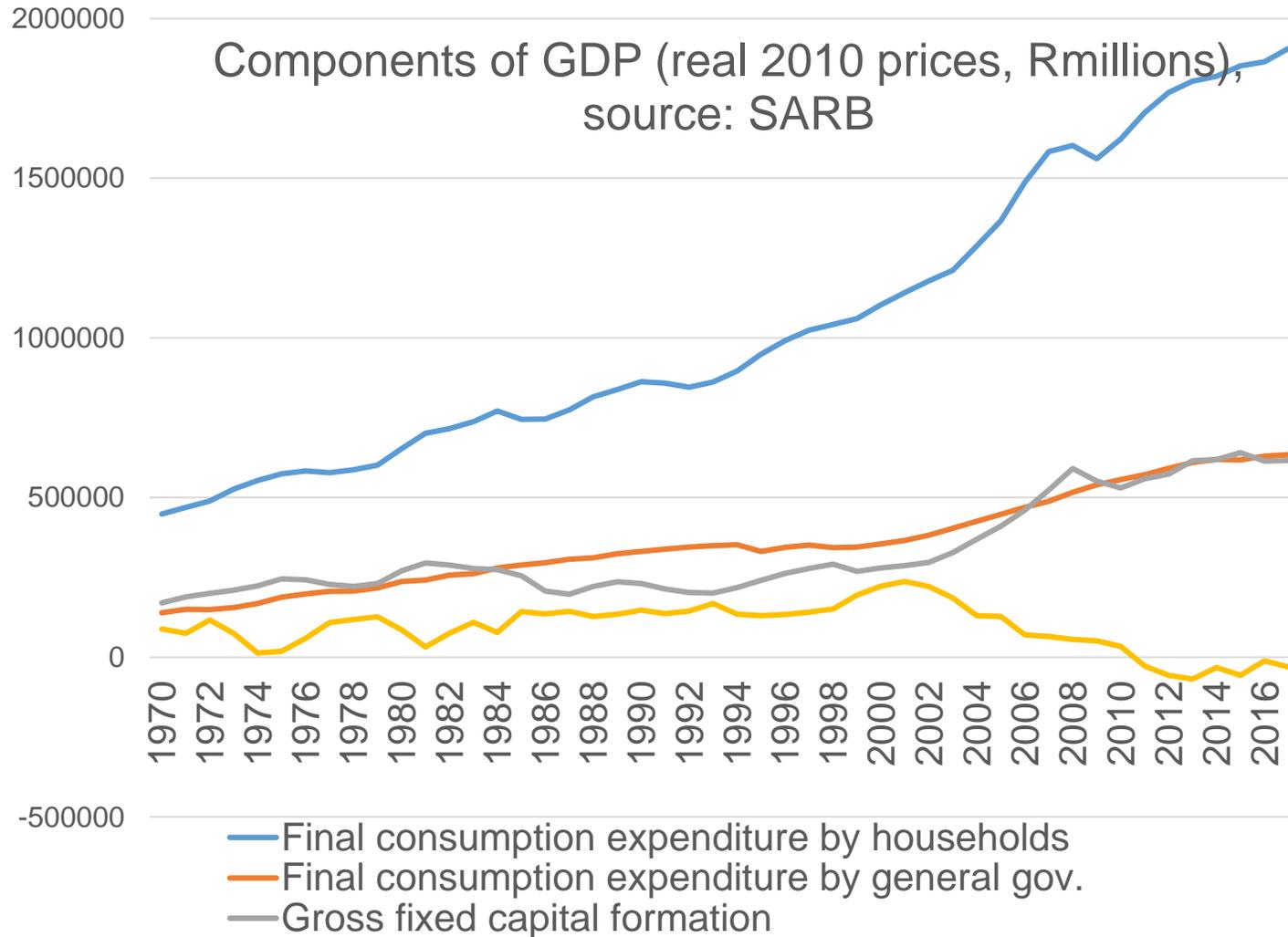
- The current account deficit was not due the need for financial flows into the country because South Africans do not save enough
- The flows were due to financial speculators looking for high short-term returns in South Africa at a time when there was increased liquidity in global financial markets



The current account consists of 2 parts:

- Imports (M) and exports (X) of goods and services (if $M > X$ then trade deficit & if $X > M$ then trade surplus)
- Financial transfers: payments to foreign holders of a country's investments and payments to holders' of foreign investments and other financial transfers (e.g., foreign aid and remittances)

Where will future growth come from



- Deficit to /GDP and Debt/GDP are ratios
- If the state can spend in a way that support market formation, innovation and productivity growth it will increase the denominator (GDP) over time

SA has not performed well in terms of GDP per capital growth since the crisis

Average annual growth in GDP per capital

