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**STRUCTURAL REFORM OF THE
SOUTH AFRICAN ECONOMY**

by

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Abstract

Economic growth in South Africa has been low and falling for several decades and the political stability of the country may well depend on achieving substantially higher living standards. After abandoning its earlier Reconstruction and Development Program (RDP), the present Government of National Unity (GNU) has embarked on a policy of macroeconomic restraint under its Growth, Employment and Redistribution (GEAR) initiative as the chief means of increasing economic growth. Despite the undoubted importance of macroeconomic stability, higher economic growth rates also require significant structural or microeconomic reform in order to enhance the adaptability and flexibility of the South African economy and so stimulate economic growth. Drawing extensively on the literature on economic and political reform in transitional and developing countries this paper examines the capacity of the GNU to implement far-reaching microeconomic reform in South Africa.

Key Words: South Africa, microeconomic reform, administrative capacity

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STRUCTURAL REFORM OF THE SOUTH AFRICAN ECONOMY

The historic elections held in April, 1994 heralded a dramatic transformation of South African society from a white oligarchy to a non-racial democracy. The success or failure of this fledgling democracy will depend crucially on whether the Government of National Unity (GNU) under President Mandela (and his successor Deputy President Tabo Mbeki) can deliver substantial increases in material well-being to its predominantly poor black constituency. Given the dismal growth rates achieved by the South African economy over the past two decades it is unlikely that these expectations can be met unless decisive action is taken to enhance economic growth. Following Rodrik's (1996, p. 11) taxonomy, at least two broad policy measures are necessary. In the first instance monetary and fiscal policy must ensure macroeconomic stability to generate domestic and international confidence in the South African economy. Notwithstanding current levels of deficit financing of the fiscus and some currency instability, budgetary policy, the behaviour of the Reserve Bank, and the Growth, Employment and Redistribution (GEAR) strategy provide solid grounds for believing that sound macroeconomic measures will be maintained. Secondly, it is widely recognised that the South African economy has severe structural problems which will have to be addressed if economic growth rates are to be raised. In contrast to macroeconomic policymaking, very little has been achieved in this arena. The problem of structural or microeconomic reform forms the subject matter of the present paper.

Considerable confusion exists surrounding the meaning which can be attached to the terms economic reform, reconstruction, restructuring, and transformation, and it is clear that these concepts are not necessarily synonymous. Mohr (1994, p.14) examines 23 examples of the use of these terms in a specifically South African policy context which can be grouped under "... five different definitions of restructuring"; he observes that "... the term is frequently used in such vague terms that it is rendered meaningless". Bates and Krueger (1993, p. 5) provide a useful generic definition of economic reform in the sense in which it is employed in the present context: "...[T]he term used to describe significant changes in a sizable number of economic policies as part of a package of policy changes. As will become evident as we proceed, the package of policy changes can vary significantly between countries, but usually involves a major adjustment of the extent to which the state interferes with market forces, which in turn entails institutional and administrative change, stabilization efforts, and removal or relaxation of controls and greater reliance on market mechanisms for allocation of resources".

However, we wish to qualify this definition by emphasising that economic reform should

be viewed as a means toward a specific end, which we designate as the creation of an "adaptive economy" (Killick, 1989a: 1989b) in the belief that economic adaptability can enhance economic development. Adaptive in this sense refers to "economic flexibility" which is assumed but never specified in neoclassical microeconomics (Basu, 1995, pp 64-67). We employ Killick's (1995, p. 17118) definition of economic flexibility: "We can define a flexible economy as one in which individuals, organisations and institutions efficiently adjust their goals and resources to changing constraints and opportunities".

The paper itself is divided into five main parts. The first section provides a synopsis of the growth performance of the South African economy over the recent past. The policy milieu within which microeconomic reform must be formulated is then summarised in section two, with the characteristics of desirable microeconomic reform set out in the third section. Part four focusses on microeconomic or structural reform in South Africa by examining the literature on reform in developing economies which have made the transition to democracy and by evaluating the bureaucratic capacity to implement reform which is available to the GNU. The paper ends with some brief concluding comments in section five.

ECONOMIC GROWTH IN SOUTH AFRICA

Economic policymaking in the New South Africa takes place against a bleak background where economic growth rates have been low and falling relative to growth capacity for more than two decades. As Kraftchik (1990, p. 62) has observed "economically the situation is marked by negative real rates of growth in manufacturing output and employment in the 1980's, and a steady decline in the overall rate of growth in gross domestic product since the late 1960's". Moreover, the widespread perception that the growth performance of the South African economy in the 1950's and 1960's was satisfactory now appears misplaced in the light of new evidence (Moll, 1990). Moll (1991, p. 19) has persuasively argued that "economic growth after 1948 was only fractionally faster than before despite highly favourable economic conditions. South Africa's comparative output-growth record is poor, and its record in terms of the growth of manufactured exports and total factor productivity verges on the disastrous". Table 1 below serves to highlight South Africa's poor economic performance in an international context:

TABLE 1. Economic Growth Rates, 1969-1989

	1969-1973	1974-1982	1983-1989
Industrial countries	4,3	2,1	3,6
Developing countries	7,2	4,3	3,6
Africa	7,5	2,8	1,8
Asia	5,2	5,9	7,4
Europe	5,9	3,9	2,6
Middle East	11,9	3,5	1,0
Western Hemisphere	6,9	3,8	1,7
Countries with recent debt-servicing problems	6,6	3,5	1,9
Countries without debt-servicing problems	5,7	5,4	6,7
South Africa	4,1	3,1	1,5

Source: Central Economic Advisory Service (1993).

Whilst it is clear from Table 1 that the South African economy performed badly against virtually all other identifiable international groups for most of the three time periods, it is also evident that South Africa mirrored international trends. If demographic and other macroeconomic factors are included, then the scale of the economic crisis in South Africa becomes obvious.

Table 2 below serves to emphasise the magnitude of this crisis. This table paints a gloomy picture of the performance of the South African economy over the recent past underscoring the immensity of the task confronting policymakers. For instance,

**TABLE 2. Recent Economic Performance
in South Africa, 1984–1994**

Calendar Year	Real GDP	Percentage change	Real GDP		Consumer price index	Percentage change	Balance of payments: current account R million
	R Million		Percentage per capita change	R			
1984	257 2925.1		7 987	2.5	42.2	11.5	–2 517
1985	254 175–1.2		7 700	3.6	49.1	16.3	5 208
1986	254 2210.0		7 517	–2.4	58.2	18.6	6 328
1987	259 5612.1		7 495	–0.3	67.6	16.1	6 708
1988	270 4634.2		7 631	1.8	76.2	12.8	3 383
1989	276 9402.4		7 633	0.0	87.4	14.7	3 467
1990	276 060–0.3		7 434	–2.6	100.0	14.4	5 324
1991	273 249–1.0		7 192	–3.3	115.3	15.3	6 187
1992	267 257–2.2		6 879	–4.4	131.3	13.9	3 940
1993	270 1811.1		6 803	–1.1	144.1	9.7	5 829
1994	276 4642.3		6 813	0.1	157.0	9.0	–2 089
Average 1984-94		0.7		–1.6		13.8	

Source: Department of Finance (1995).

with growth in real annual GDP only 0.7 per cent over the period 1984 to 1994, and South Africa's high population growth rate, this meant a decline in real GDP per capita of almost 15 per cent. The policy problems involved in drastically increasing the rate of economic growth are compounded by at least three other factors. Firstly, it is apparent from Table 2 that South Africa has an ongoing problem with inflation which averaged over 13 per cent between 1984 and 1994. Efforts aimed at boosting growth through the stimulation of aggregate demand may thus ignite existing inflationary pressures. Secondly, external constraints on the growth rate of the South African economy are also evident: whenever domestic economic growth occurs, the effects are soon felt in the balance of payments. And finally, although it is not even shown in Table 2 owing to a lack of reliable statistics, unemployment is undoubtedly a major source of concern. Barker (1992) has estimated that some 40 per cent of the labour force cannot obtain employment in the formal sector of the economy, half of whom may hold informal sector jobs. Even assuming an economic growth rate of 5 per cent per annum, Fallon and de Silva (1994) have calculated that formal sector unemployment will be around 37 per cent by 1998/2001 and 26 per cent by 200215. The political implications of these high levels

of unemployment are alarming.

The success or otherwise of policies aimed at increasing the rate of economic growth in South Africa depend in part on the causes of the present economic malaise. Various diagnoses have been attempted. For example, Mohr (1994, p. 47) adopts a long-run perspective: "... [S]ome of the major growth focus in the South African economy during the period 1946 to 1974 will be listed, and it will be indicated what happened to each of these forces from 1975 onwards". In this analysis, Mohr (1994) focuses on changes in world economic growth, world trade growth, technological progress, gold production, import substitution, foreign capital flows, and labour costs and argues that these changes depressed growth rates in South Africa. Similarly, Fallon and de Silva (1994) identify five sources of the poor performance of the South African economy since 1965. In the first instance, they argue that the investment to GDP ratio has steadily fallen from a peak of about 26 per cent in 1971/76. Secondly, the nature of investment has changed with an increasing proportion of the capital stock invested in the relatively low productivity public sector. Thirdly, from 1965 onwards macroeconomic policy has encouraged capital intensive production techniques, a trend which has been amplified by rising real wage rates for black labour. Fourthly, "... skill accumulation has been inadequate, and there has been a growing imbalance between the nation's stocks of physical and human capital" (Fallon and de Silva, 1994, p.65). And finally, they argue that the South African economy has exhibited a more pronounced business cycle which has meant the periodic under-utilisation of productive resources. Natrass (1995) has postulated that the decline of the gold mining industry in South Africa constitutes a significant factor in the poor growth performance of the South African economy. Noting that goldmining has experienced rising production costs, falling ore grades and a weak gold price, Natrass (1995) observes that South Africa's annual gold production as a percentage of world output fell from 66.6 per cent in 1981 to only 32.8 per cent by 1993, which meant a loss of some 166,000 jobs since 1987, or around a third of total direct employment in the industry. Finally, Bethlehem (1994) has argued that "socio-political turbulence" and falling economic growth have been strongly correlated in the post-war South African economy.

A REVIEW OF THE POLICY DEBATE IN SOUTH AFRICA

It has long been recognised by virtually all participants in South African policy debates that the South African economy is in urgent need of reform. Eckert and van Niekerk (1993) note that the first official proposal aimed at comprehensive economic reform, the 1987 *Economic Development Programme, 1978-1987* (later amended to form the 1991 *Revised Long-Term Strategy*), had its genesis in the then Prime Minister's Economic

Advisory Council as far back as 1979. The essence of this document was a proposal to reduce the role of the public sector in the South African economy so as to "... afford the private sector more opportunity to conduct business on a profit basis. It is hoped that in the process the natural operation of market forces will bring about a healthy competitive economic structure that will, among other things, create more job opportunities" (Economic Advisory Council of the State President, 1991, p. 12). Mohr (1994) also points to a parallel confidential official document with much the same message entitled *Ekonomiese Herstruktureering in Suid-Afrika*. Although the essence of this official policy stance was retained and set out in some detail in the 1993 *Normative Economic Model*, it is now clear that the impetus for economic reform under the previous minority National Party government had already evaporated. Qadir (1994, p. 183) has described the stalling of reform initiatives as follows: "The former white minority NP government came only belatedly to free market economics, as this conflicted so markedly with the heavily state interventionist economic approach of apartheid. A key turning point was the publication in 1987 of the *White Paper on Privatisation and Deregulation in the Republic of South Africa* and subsequent implementation efforts. The privatisation initiative soon stalled, however, when negotiations over the transition began in earnest after 1990. The new National Party policy of deregulation and growth has been tempered latterly by electoral expediency, as nonwhite voters need to be won by some promise of redistribution". The historic announcement by the De Klerk administration on 2 February 1990 unbanning the African National Congress and other political organisations included a commitment to freeze any further economic restructuring initiatives.

This is not to suggest that no economic reform had taken place. A privatisation program involving ISCOR, the South African Mint and a sorghum beer brewer had already been completed. Moreover, as part of a commercialisation initiative by the Office of State Enterprises, many public enterprises were reclassified as public corporations, including the giant Transnet, formerly South African Transport Services, which are now obliged to trade at prices which cover production costs. Similarly, various deregulatory reforms were introduced aimed at the promotion of effective competition in the South African economy. Perhaps the most significant reform to date has occurred in international economic relations. Various proposals for the reform of protection policy developed by the Industrial Development Corporation (1990) were accepted in the GATT negotiations in 1993 and became effective at the beginning of 1995. Subsequently, South Africa "... has embarked on a substantial revision of its tariff structures, protectionist measures and the phasing out of its controversial export subsidisation, the General Export Incentive Scheme (GEIS)" (Strydom, 1995, p.557). The liberalisation of international trade obviously intensifies the need for domestic economic reform (Blumberg, 1995).

However, virtually no progress has been made in other areas, like reducing the share of direct taxation in total government receipts, the removal of fiscal drag, government dissaving, and the overall reduction of government expenditure.

These official policy proposals were accompanied by numerous programs emanating from the private sector, various think-tanks, and some political parties¹. For example, Sunter (1987) produced his well-known "high road-low road" scenario alternatives, whereas Nedcor-Old Mutual brought out their *Change of Gears* strategy (Tucker and Scott, 1992). Similarly, the Democratic Party developed its own economic plan embracing tax cuts, deregulation, privatisation, labour intensive production, and export enhancement. Moreover, several quantitative analyses were conducted, not least the Macro Economic Research Group, the World Bank computable general equilibrium model, and the Development Bank of Southern Africa's social accounting matrix (Eckert and van Niekerk, 1993).

Whilst virtually all proposals envisaged some degree of microeconomic reform, Mohr (1994, p. 45) has argued that most "establishment" policy packages shared many common features: "For the government, the Reserve Bank and some other establishment groups, economic instability in the form of a declining domestic and international value of the rand seems to be the major issue. Restructuring is aimed at achieving or maintaining greater macro-economic stability in the narrow sense, which is regarded as a prerequisite for renewed economic growth".

The official centrepiece of the economic policy of the new GNU was contained in the RDP. Nolan (1995, p. 161) described the RDP as a bold plan which aimed "... to provide a comprehensive approach to harnessing the country's resources to reverse the effects of apartheid and to attack poverty and deprivation over a fiveyear period, setting out the framework for economic and social policy (as well as for developing the political institutions of the new democracy)". The RDP was overseen by the Ministry in the Office of the President and funded through an RDP Fund, financed via normal budgetary processes.

The RDP was based on "six principles" set out in an RDP *White Paper* published in September 1994. These broad guidelines were: specific RDP programs must be "integrated and sustainable"; initiatives must be " people-driven and people-centred"; programs must "promote peace and security for all"; RDP developments must foster "nation-building"; initiatives must "link reconstruction and development"; and finally, initiatives must "democratize South African society". On a somewhat less esoteric level, actual projects subsumed under the RDP were in fact launched. In his "state of the

nation" address on 24 May 1994, President Mandela announced a series of key programs, or Presidential Lead Projects to inaugurate the first year of the RDP. Delivered through the national, provincial and local government structures, these projects ".. were selected on the basis of a set of explicit criteria which included their potential high impact on communities, job creation, community empowerment, provision of basic needs, training and capacity development, transparency, potential to leverage existing funds, and economic and political sustainability" (Department of Finance, Section 2.1.3. 1). In total, some 21 projects had been initiated by early 1995 with an additional 4 programs launched at the end of the 1994/95 financial year.

Whilst there was undoubtedly a need for the RDP or some similar growth-orientated redistribution scheme to capture the imagination of the South African electorate in the historic April 1994 elections, as much as to actually solve economic and social problems, questions nevertheless arose as to the likely effectiveness of the RDP.² In general, even at its inception informed opinion appeared sceptical of the RDP having a decisive impact on living standards in South Africa. Some commentators highlighted weaknesses in the RDP itself. For example, Nolan (1995, p. 163) argued that "the RDP has generated considerable confusion, because in so many areas it advances general rather than specific goals, leaving open how its objectives are to be achieved, and with little clarification on its costing and financing". It was also observed that despite the ambitious aims of the RDP, which made its success critically dependent on appropriate macroeconomic policy settings over the life of the plan, the RDP was virtually devoid of discussion on appropriate macroeconomic policymaking. Turok (1995, p. 316) argued that "the 'people-driven' process envisaged by the RDP is unlikely to be smooth or harmonious" since attempts by the RDP to mobilise the whole of South African society necessarily meant that conflicts in society at large were mirrored in the RDP and its projects. Serious questions were raised about the financial underpinnings of the RDP. For instance, although R39 billion was touted as the total cost of the RDP during the election campaign prior to April 1994, it later transpired that R39 billion may have represented only annual expenditure on the RDP in its 1998 final year, with the cost of the entire program estimated at R135 billion (Nolan, 1995, p. 163).

Other observers questioned the ability of the South African bureaucracy to implement the RDP successfully. Simkins (1996, p. 85) pointed to the inauspicious beginnings of the RDP and laid the blame on bureaucratic failure: "What progress has been made? The RDP *Monitor* of August 1995 reported that more than R1.7 billion of the \$2.5 billion allocated to the Reconstruction and Development Fund in 1994-95 had not been spent in that fiscal year, and estimated that at least 20 percent of the 1995-96 allocation would not be spent. The major reason is lack of state capacity". Simkins (1996)

identified three dimensions of this "state incapacity". Firstly, there existed "program incapacity" which refers to the difficulties involved in implementing specific programs in a complex, evolving and uncertain policy environment. Secondly, the reconstruction of the South African civil administration at the provincial and local levels from the former provincial and homeland bureaucracies had not yet been completed, leaving the present structure incapable of efficient policy implementation. And thirdly, "... the establishment of the controls essential to good government takes time and is not always adequate ..." (Simkins, 1996, p. 86). In order to overcome bureaucratic failure, Simkins (1996) suggested the RDP utilised the existing nongovernmental organisations in South Africa and enlisted the assistance of the private sector. Moreover, he argued that Parliamentary appropriations would never be sufficient to fund the RDP adequately, and so alternative arrangements like privatisation, would have to be employed: "... [T]he state will have to alter its portfolio of assets; urban infrastructural development will inevitably be linked with privatisation" (Simkins, 1996, p. 86).

Some commentators were even less charitable about the prospects for the success of the RDP. For example, Bethlehem (1994, p. 297) was not optimistic: "What kind of state is required in South Africa if the right balance between delivery and efficiency is to be achieved? The RDP provides an answer when it envisages a small, efficient, enabling state, but its commitment is put in doubt by its subsequent elaboration of a bureaucratic framework required to meet its basic needs objectives. Being dealt with here is a new South Africa with ten separate governments - a central one and nine provincial - each with its own paraphernalia of administration. In the end, perhaps, the government will be saved by the macroeconomic constraints discussed earlier. Unless it is going to violate the commitment to fiscal balance and monetary restraint already made, it is going to have to cut its bureaucratic coat to fit its revenue cloth". Similarly, Natrass went on record to say that the entire RDP was simply "... a costly and ultimately unnecessary piece of bureaucratic musical chairs" (*Weekly Mail*, 1995).

In hindsight, the RDP represented a highly interventionist microeconomically-orientated policy of physical and social infrastructure development targetted at the poorer sections of South African society. It required a sophisticated state bureaucracy to succeed and appears to have failed because the South African state did not possess the requisite administrative capacities (Simkins, 1996). Subsequent policy formulation looks much more promising. Current official attempts to enhance economic growth centre on the (GEAR) policy initiative. In contrast to the microeconomic focus of the RDP, GEAR is intrinsically a macroeconomic strategy based on "... the premise that job creation is the way to address poverty and and that to increase employment opportunities higher economic growth is required" (Nomvete, Maasdorp and Thomas, 1997, p. 3). Key

elements of GEAR include a deficit reduction scheme, tariff reductions, stable real exchange rates, conservative monetary policies, and "moderate wage demands" (Biggs, 1997, pp. 48/49). Given its adherence to the so-called "Washington consensus" (Lal, 1995) and its low demands on the bureaucratic machinery of government, GEAR appears to have a reasonable chance of achieving at least some of its objectives.

CHARACTERISTICS OF DESIRABLE MICROECONOMIC REFORM

If economic development is defined in terms of increasing the material well-being of a target population, then it can be conceptualised as the outcome of three interrelated factors. Firstly, the economic efficiency of current resource usage. Secondly, the rate of growth of productive resources through time. And thirdly, the manner in which the resultant output is distributed amongst the target population. Underlying these factors is the basic economic and social structure which has a decisive influence on their performance. At its most fundamental level, microeconomic reform seeks to modify this institutional structure so as to enhance the operation of these factors and accelerate economic development.

A surprising degree of unanimity exists on the most appropriate means of conducting microeconomic reform. Thus Rodrik (1996, p. 9) has observed that "what is remarkable about current fashions in economic development policy (as applied to both transitional and developing economies), however, is the extent of convergence that has developed on the broad outlines of what constitutes an appropriate economic strategy. This strategy emphasises fiscal rectitude, competitive exchange rates, free trade, privatisation, undistorted market prices, and limited intervention (save for encouraging exports, education, and infrastructure)". Similarly, Deepak Lal (1995, p. 489) has identified a "consensual economic policy package" whose roots can readily be traced back to John Stuart Mill's *Principles of Political Economy*. Describing these policy prescriptions as the "Washington consensus", Lal (1995) cites Williamson's (1994) taxonomy of policy reforms as representative of the current prevailing orthodoxy amongst development economists. Williamson (1994) argues that an ideal microeconomic reform strategy should focus on ten main issues. These are as follows:

- Fiscal discipline, which implies that real budget deficits should never exceed 2 per cent of national income except in dire circumstances, since budget deficits usually crowd out private investment;
- Public expenditure constraints, which emphasise expenditure reductions rather than tax revenue increases to reduce budget deficits;

- Tax reform, which means relying on simple broad-based tax systems with only moderate marginal tax rates;
- Financial liberalisation, which implies market determined interest rates, no exchange controls, no other impediments to capital flows, and no subsidised credit;
- Market determined exchange rates, which mean the introduction of a unified and competitive exchange rate;
- Trade liberalisation, which involves a gradual movement towards free trade by the removal of tariffs, quotas, etc.;
- Encouraging foreign direct investment;
- Privatising public enterprises;
- Deregulating markets; and
- Establishing an efficient and well-defined system of property rights.

The thrust of this consensual view has been aptly described by Killick (1995, p.385-386) as follows:

"Overall, then, we see a case for a combination of pro-active interventions and strategic withdrawals, in promotion of the well-functioning market system which is the chief vehicle for national economic flexibility: safeguarding the national interest, minimising adjustment costs, responding to market failures and getting rid of regulations and other policy instruments which hamper the efficient working of markets".

There appear to be no compelling reasons why microeconomic reform in South Africa should not conform to this consensus, provided merit good provision seeks to ameliorate past injustice in the racial allocation of these goods and land reforms deal with need for restitution in the case of forced removals under apartheid.

MICROECONOMIC REFORM IN SOUTH AFRICA?

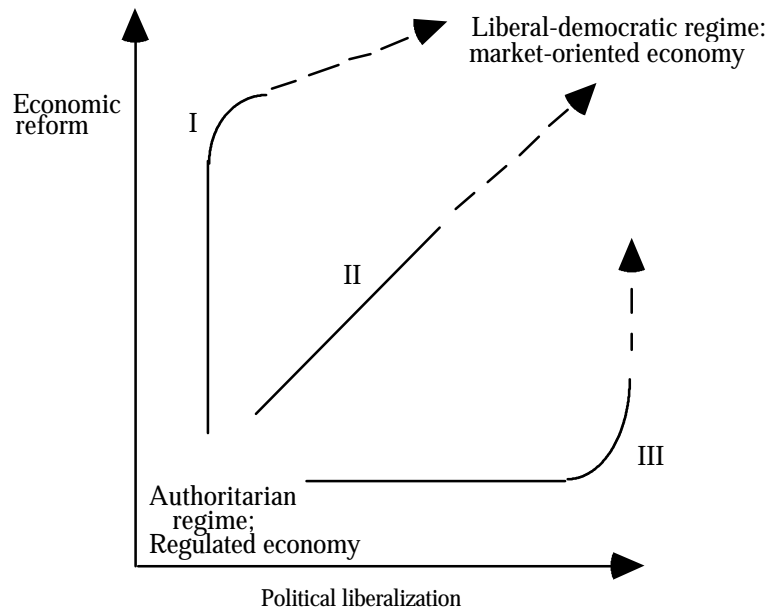
Although the general nature of the microeconomic reforms necessary in South Africa are thus easy to identify, the real question resides in whether or not the GNU will in fact embark on a substantial program of reform along these lines. A large and growing body of international literature has accumulated over questions of this kind which includes Bates and Krueger (1993), Rodrik (1996), Dornbusch and Edwards (1993), Grindle and Thomas (1991), Haggard and Kaufman (1992), Haggard and Webb (1994), Krueger

(1993), Bresser, Pereira, Maravall and Przeworski (1993), Przeworski (1991), Ranis and Mahmood (1992), Taylor (1994) and Williamson (1994). The question is made more difficult in the actual historical circumstances of South Africa where the transition to democratic government has barely been completed. The question itself has two dimensions: in the first place, will the Mandela administration (and its Mbeki successor) actually wish to engage in fundamental microeconomic reform, and secondly, does it possess the requisite bureaucratic and other capacities to achieve microeconomic reform?

1. The Political Will to Reform

One way of conceptualising this issue is in terms of the analysis of Haggard and Kaufman (1992). Haggard and Kaufman (1992, p.332) argue that "... the political effects of these [microeconomic] reforms are likely to be contingent on the *sequencing* of economic and political liberalisation" (original emphasis). Figure 1 below allows us to distinguish clearly between the three possible options identified by Haggard and Kaufman (1992); namely, economic reform implemented before, during, or after political transition. Sequence III in Figure 1 illustrates the case where authoritarian regimes yield to democratic governments without having introduced significant economic reform as with the previous National Party administration in South Africa. Haggard and Kaufman (1992, p.332) examine historical examples of sequences I, II and III and argue that "... each sequence has predictable consequences both for the nature of the democratic transition and for political alignments and conflicts in the post-transition period". In their analysis of sequence III Haggard and Kaufman (1992, p.339) examine developments in Argentina, Bolivia, Brazil, Peru, the Philippines, Uruguay and Eastern Europe as examples of this genre and contend that uncertainty characterises transitions of this kind since "... it can be expected that there will be considerable uncertainty with respect to new decision-making structures and the stance of key interest groups and political parties". Once a "routinisation of politics" comes into existence to reduce

Figure 1. Economic and Political Reform



Source: Adapted from Haggard and Kaufman (1992, p.333). Note that dashed lines indicate that sustainability of the path is problematic.

the level of uncertainty associated with transition then the consolidation of democratic rule will also demand a downward adjustment of expectations concerning the ability of the state to respond to distributive claims carried into the political arena" (Haggard and Kaufman, 1992, p.340). Haggard and Kaufman (1992, p.339) are pessimistic on whether governments in sequence III will actually pursue a reform agenda with vigour and observe that "although some regimes have begun projects of economic reform, few, if any, have yet seen sustained economic results from these efforts".

Bates and Krueger (1993) are also less than sanguine about the prospects for timeous economic reform in sequence III countries. On the basis of their analysis of an extensive range of case studies they postulate the following generalisation (Bates and Krueger, 1993, p.454):

"In all circumstances, of course, reforms have been undertaken in circumstances in which economic conditions were deteriorating. There is no recorded instance of the beginning of a reform program at a time when economic growth was satisfactory and when the price level and balance of payments situations were stable. Conditions of economic stagnation (and the recognition that it is likely to continue) or continued deterioration are evidently prerequisites for reform efforts".

This naturally raises the question of what constitutes a perceived "crisis" of sufficient magnitude to induce decisive action on the part of governments.³ According to Krueger (1993, p.124) "no satisfactory answer has yet been given". However, she does note that

"when a governing coalition is fairly cohesive and commands a reasonable majority, policy reform may come at an early stage in the process of economic deterioration" (Krueger, 1993, p.125). This may indicate that the prospects for economic reform at the level of policy making in South Africa are reasonably good. After all, the dominant African National Congress enjoys a substantial majority and discernible "crises" in the form of sharp devaluations of the rand occurred between February and May of 1996 and then again in June and July of 1998. The proximate causes of the first of these devaluations lay in the doubts surrounding President Mandela's health after his hospitalisation on 15 February 1996, the resignation of Finance Minister Liebenberg on 28 March 1996, exchange control uncertainty in early April 1996, and the National Party's withdrawal from the GNU on 8 May 1996, whereas the ostensible source of the 1998 devaluation appears to reside in the appointment of Tito Mboweni as Governor of the South African Reserve Bank. Nevertheless, good reasons exist for believing that policy paralysis on the part of the South African government, especially on the question of exchange controls and the overly tentative privatisation of various large parastatals, played a pivotal role in the significant loss of confidence in the South African rand in international currency markets on both occasions. However, set against the need to reform in the face of these "crises" is the GNU's populist support and its manifest caution in opposing the trade union movement in South Africa, especially the Congress of South African Trade Unions (COSATU). Evidence exists which suggests that this may be a feature of sequence III countries. For instance, Haggard and Webb (1993, p.147) observe that "democratisation is often accompanied by an increased level of political activity, which provides the opportunity for previously repressed groups, such as labour, to press their demands".

The key role played by governmental elites and state institutions in economic reform should also not be overlooked. Haggard and Kaufman (1992, p.18) have identified three ways in which this may occur. Firstly, "... government officials play a crucial mediating role between the international and domestic arena, and thus are directly exposed to pressures that emanate from the world economy, creditor governments, foreign firms and banks, and multilateral financial institutions" (Haggard and Kaufman, 1992, p.18). Given the openness of the South African economy and the exposure of many policymakers in the GNU to international influences during their enforced expatriation during the apartheid era, this factor is likely to be especially important in the South African case. Secondly, governmental elites and official institutions often play a decisive role in setting the policy agenda and guiding the policy process. And thirdly, "... the structure of political institutions, including the state itself, will influence both the capacity of the government to act and the range of societal interests that are represented" (Haggard and Kaufman, 1992, p.18).

It is possible to postulate some additional dimensions along which to evaluate the probability of significant microeconomic reform occurring in South Africa. For instance, the strength and independence of the judicial system is likely to affect the path to reform. In this respect South Africa possesses a distinct comparative advantage over most other developing and transitional economies falling into the sequence III category. Similarly, the cohesiveness and stability of government may also prove decisive. With the foundations of an orthodox two-party system already in place in South Africa and the GNU holding firm despite its ANC/SACP/IFP makeup, South Africa compares well with many other sequence III countries. In addition, policy leadership from the international community may be significant. However, given the decline of western interest in southern Africa, this is unlikely to be especially advantageous in the South African case.

In sum, the literature on economic reform in sequence III countries does not provide any clear-cut arguments for believing that substantial structural economic reform will be undertaken in South Africa. Actual events after the historic 1994 election reinforce this pessimism. At the level of microeconomic reform it is hard to escape the impression that the GNU has been in the grip of policy paralysis. Whether the rand devaluations in 1996 and 1998 will be sufficient to overcome this paralysis remains to be seen.

2. The Administrative Capacity to Reform

If the GNU (without the National Party) does indeed initiate a program of substantive structural reform along the lines of the Washington consensus outlined earlier, then the question arises as to whether the South African state possesses the requisite administrative capacity to actually implement the program. This is by no means a settled issue. We have already seen that the RDP has foundered due to what Sirkins (1996) termed "state incapacity" and there is little *a priori* reason to believe that matters will improve in the foreseeable future. Moreover, the inability of the state to successfully undertake market-orientated structural reforms is a generic problem faced by many developing countries which has been referred to by Kahler (1990) as the "orthodox paradox". The orthodox paradox hinges on the observed fact that the expansion of the role of markets in highly regulated developing economies ironically requires a strengthening of the state, and especially its economic bureaucracy, in order to work. Haggard and Webb (1993, p. 151) make a similar point:

"The wide variation in the quality of economic policy within both democratic and authoritarian governments suggests that the prospects for policy reform also depend on the characteristics of the state itself, particularly the discipline and competence of the

bureaucracy. Consequently, many structural adjustment programs require a selective strengthening of the governments role in the economy rather than a simple reduction in government intervention".

Leftwich (1995) also stresses the competence of the economic bureaucracy in the success or otherwise of economic reform in his model of the developmental state based on the performance of the East Asian capitalist economies.

Cogent reasons exist to support the view that the South African state has lost rather than gained bureaucratic expertise since its transition to democracy. Numerous senior civil servants have left the bureaucracy since 1994, including experts in economic policy formulation and implementation, like Estian Calitz, former Director General of the Department of Finance. In many instances these bureaucrats have been replaced by the beneficiaries of political patronage often with no obvious technical expertise. Similarly, 1994 election promises by the ANC/SACP alliance to the effect that no civil servant would lose their job under a new government have largely been honoured. This has meant a bureaucratic structure comprised of former South African national government bureaucrats, provincial administration employees, and members of all the old homeland government bureaucracies. The result is an unwieldy amalgam of people possessing widely differing degrees of technical competence and political allegiance.

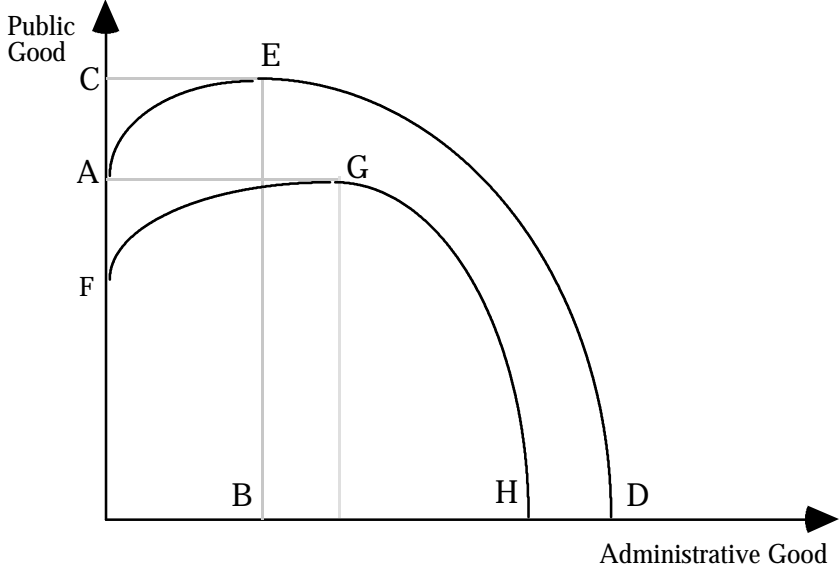
Three examples will suffice to highlight the limited administrative capacity of the South African state. Firstly, we have already discussed the deleterious impact of bureaucratic failure on the implementation of the RDP. However, it is worth emphasising that many of the administrative structures intended to deliver various RDP initiatives were set up in parallel to the existing formal bureaucracy. Their inability to function efficiently surely serves to demonstrate that the South African state is severely constrained in its capacity to create new efficient bureaucratic structures, at least in the short term. This would appear to have significant implications for any further bureaucratically-intensive policy interventions. Secondly, the apparently ongoing crisis in the administration and collection of import duties also underlines the weak bureaucratic capacity available to South African policymakers. Mounting anecdotal evidence appears to suggest that although extensive and longstanding tariffs apply to most imported goods coming into South African ports, customs officers often no longer impose these duties on billions of rands worth of goods (Old Mutual Economic Research Unit, 1996, p.5). Whether this is due to corruption or simple incompetence is not clear. Notwithstanding South Africa's obligation under the 1993 GATT agreement to progressively lower tariff barriers, it is apparent that administrative incapacity has rendered trade policy largely inoperative. In

effect, South Africa has adopted free trade by default. Once again this should counsel caution against relying on bureaucratic structures. Finally, although anecdotal evidence on the problem of state incapacity in South Africa has been accumulating for some time, until recently evidence of this kind has been met by either outright official denials or claims that any problems experienced are only transitory. However, the release of the *Provincial Review Report* (widely known as the Ncholo Report) by Public Service and Administration Minister Zola Skweyiya in September 1997 provided a devastatingly frank analysis widespread state incapacity in South Africa (Dollery and Wallis, 1998).

Black (1995, p.552) has developed a useful way of conceptualising the trade-off involved in public budgets between the public goods they are supposed to deliver and the resource consuming "administrative good" involved in producing and administering this public good. Figure 2 illustrates the production frontier between public goods and administrative goods.

In Figure 2 the initial production frontier is given by curve AED. If no resources are devoted to administration, then OA of the public good will result. By contrast, if OB administration takes place, then the amount of the public good will rise to a maximum

Figure 2. Public and Administrative Good Production Frontier



Source: Adapted from Black (1995, p. 552).

of OC. Thereafter additional resources allocated to administration will begin to incrementally lower the output of the public good. However, if some exogenous event were to reduce the efficacy of administration, then production frontier AED would shift inwards to form a curve like FGH. It is also likely that the maximum feasible amount of

the public good would occur under a somewhat higher level of administration, with point G lying to the south east of point E.

If the shift from AED in Figure 2 to FGH is indeed illustrative of the change in administrative capacity in South Africa, then the question arises as to the policy implications of this change. Postwar development economics has generated at least three different perspectives on the role of the state in the process of wealth creation. In the 1950s and 1960s it was widely believed that the bureaucratic apparatus of the state played a positive role in economic development. However, the subsequent poor performance of the state in many developing countries led to the opposing view of the state bureaucracy as a major obstacle to economic development with the attendant policy prescription for minimising the role of the state. But by the late 1980s this minimalist view was itself being challenged by the perception that the state was central to the achievement of satisfactory structural change (Kahler, 1990). As Evans (1992, p.141) has observed "dismantling the state is not the answer. It must be reconstructed". More recent support for this line of argument has been provided by the 1997 *World Bank Report* with its emphasis on the "enabling state" in the process of economic development.

Whether the South African bureaucracy represents a Leviathan predatory state or has the potential to become a developmental state matters little in the short run. As we have sought to show, in its present circumstances the administrative capacity of the South African state is severely constrained. Moreover, "reconstructing the state is an amorphous and frustrating task, a project of decades if not generations" (Evans, 1992, p.181). Thus, current policy formulation should be premised on two interrelated observations. Firstly, bureaucratic capacity is under-supplied in South Africa. And secondly, "the state's ability to perform administrative and other functions must be treated as a scarce good" (Evans, 1992, p.177). Irrespective of whether one accepts a developmental role for the state in the long run, acceptance of these characteristics of state capacity has some obvious short run policy implications for the GNU. In the first instance, scarce administrative skills must be rationed to ensure they are applied to those areas where markets do not usually perform adequately, like the maintenance of law and order and the provision (not production) of infrastructure as well as the generation of merit goods, such as basic education. Secondly, the public sector should withdraw its scarce bureaucratic capacity from areas where markets enjoy a comparative advantage by means of privatisation, especially in the case of Transnet, Escom, Telkom, and the South African Post Office. Thirdly, NGOs should be encouraged to take over from government departments in the provision of social welfare services, including NGOs from OECD countries which are likely to possess the requisite skills. And finally, consideration should be given to increasing the longer run capacity of the South African state.

CONCLUDING REMARKS

At least three features of current political economy in South Africa appear fairly settled. In the first instance, it is plain that the growth performance of the South African economy has been most unsatisfactory over the past few decades and will not improve unless a substantial program of microeconomic structural reform is instituted to remove severe structural constraints on economic activity. Secondly, at the macroeconomic level the GEAR policy initiative has performed tolerably well and embodies contemporary wisdom on appropriate macroeconomic policymaking. Not much more can be achieved by macroeconomic policies alone. Thirdly, and notwithstanding hostile rhetoric to the contrary from COSATU and some other significant interest groups, the nature of the requisite structural reform program is not controversial and can be summarised in terms of the so-called Washington consensus outlined earlier.

Much less clear is the question of whether the GNU will indeed formulate and seek to implement a structural reform program along these lines. Doubt exists at two levels. Firstly, international evidence drawn from developing economies which have made the transition to democracy appears suggestive of the view that sequence III countries do not embark on economic reform programs until and unless they are faced with some kind of "crisis". Whether the sharp devaluations of the South African rand in 1996 and 1998 are perceived as examples of such crises by the GNU and whether it acts as a catalyst for decisive policy action remains to be seen. And secondly, even if policymakers do prescribe a structural reform policy package which conforms to the Washington consensus, it is questionable whether the South African state has the administrative capacity to implement the package. It would thus not seem unreasonable to adopt a pessimistic view of the prospects for substantial microeconomic reform in South Africa in the foreseeable future.

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FOOTNOTES

¹ See Eckert and van Niekerk (1993, pp. 3-5) and Mohr (1994, pp. 42-45) for a detailed account of these proposals.

² Looking back on the broad sweep of South African development, Simkins (1996, p.92) has raised the intriguing argument that "the RDP appears as one initiative in a long chain of developmental efforts, rather than as a radically new approach". Citing precedents in the form of the Smuts administration's Second World War Social and Economic Planning Council, black education, industrial relations, occupational and income redistribution, and Regional Service Councils, Simkins (1996) argues that South African society has been characterised by evolutionary change, rather than revolutionary change.

³ The notion of crises acting as a trigger for reform is analytically problematic. Rodrik (1996, p.27) has set out two main criticisms as follows:

"First, note that there is a strong element of tautology in the association of reform with crisis. Reform naturally becomes an issue only when current policies are perceived to be not working. A crisis is just an extreme instance of policy failure. That policy reform should follow crisis, then, is no more surprising than smoke following fire. Furthermore, the hypothesis is virtually nonfalsifiable: if an economy in crisis has not yet reformed, the frequently proffered explanation is that the crisis has not yet become 'severe enough'."

