

Gill Marcus: South Africa's challenges at a difficult time for the global and domestic economy

Address by Ms Gill Marcus, Governor of the South African Reserve Bank, at the Noah Gala fund-raising dinner, Sandton, 21 August 2012.

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Distinguished Guests, thank you for the invitation to address you this evening.

The work that Noah does with orphans in our disadvantaged communities is admirable, and it is heartening to see the support that the organisation receives from the private sector at a very difficult time for our economy. It is estimated that the HIV/AIDS pandemic will leave more than 5 million children orphaned by 2015, which will add to the demands on the public sector and private sector organisations such as Noah. Helping to ensure a positive present and future for these children is not just a question of money. To achieve the aims and vision of Noah requires dedication and commitment to train and build capacity to foster stronger communities capable of caring and providing for children, whether these children have been orphaned by AIDS or any other cause. Noah's basic message is that every child must be allowed the possibility to dream and you provide that hope for the children and their communities.

It was stated in the Noah Annual Report 2012 "Looking ahead" that "the key to success lies in a collective effort". That "government ... has laid a foundation for change (through) grants and payments for caregivers that make the Noah approach sustainable" and that "getting to all needy children is the problem".

While there is much negative comment about government policies, it is important to recognise that at the core of health care there has been a critical shift that holds the potential to improve collaboration across all sectors involved in primary care, and to reach the adults and children who are presently underserved or excluded. When considering Community Oriented Primary Care I am aware that the ideas are very familiar to many of you in your practice. What is exciting is that they are now being integrated through the National Department of Health into the health care system. I will return to this in some detail later on.

Noah is undertaking this work at an extremely difficult time for the global and domestic economy. Let me first deal with the advanced economies, particularly the Eurozone and the United States. The crisis in the advanced economies persists, despite the temporary breather that global financial markets appear to be taking in the past few days. However, on the ground, growth outcomes and prospects have been deteriorating. Growth in the Eurozone was negative in the second quarter, having contracted by 0,4 per cent, and eight of the 17 members experienced negative growth. The engine of growth of the region, Germany, barely managed to register positive growth, and the short term indicators are not promising. The UK remains in recession, growth in Japan declined sharply to 0,3 per cent in the second quarter, and the prospect of a sharp fiscal cutback in the US early next year remains a dark cloud over the already slowing economy. To illustrate the depth of the very complex problems faced, Greece, which is at the forefront of the unfolding tragedy, is expected to have negative growth of some 6 per cent for 2012, with its GDP expected to have shrunk by around 20 per cent over the three-year period 2010–2012. Growth in the larger systemically important economies, notably China, India and Brazil, is also moderating under the strain of declining exports, illustrating the interdependent nature of the global economy.

Behind the growth numbers are the millions of people who have lost their jobs and their dreams. The unemployment rate in the Eurozone has now risen to 11,2 per cent, and youth unemployment to 22,4 per cent. This places enormous stress on the fabric of society which not only struggles to provide for those such as AIDS orphans, but now needs to deal with the demands of a growing number of people around the world who previously had jobs and

aspirations, many of them with skills and education, and who now find themselves in a situation where the chance of finding employment diminishes by the day. The demands on governments multiply under such circumstances, at a time when excessive fiscal austerity is the order of the day in the advanced economies, with large cutbacks in government spending and provision of basic social services. Unless governments can get growth going again, social and political disaffection is likely to spread, as we have already seen in a number of countries in Europe.

But not all of the challenges facing us are man-made. While growth in the developing economies is more positive, the global economy and developing economies in particular are facing new danger, and that is the sudden emergence of a possible food crisis which can only exacerbate the fragile social situation in many countries. The past few weeks have seen significant increases in several agricultural commodity futures prices, including grains, soya beans and cattle. Since the beginning of June, futures prices of maize and wheat traded on the Chicago Board of Trade (CBOT) have increased by around 60 per cent and 40 per cent respectively, and these increases are already having a global impact. On the South African Futures Exchange (SAFEX), for example, futures prices of wheat have increased by 20 per cent, and those of maize by 30 per cent since the beginning of June.

The main cause of these price increases has been severe drought conditions in the United States in particular, which is said to be facing its worst drought in 56 years, with 88 per cent of the maize crop facing these conditions, and parallels are being drawn with the “dust bowl” episode in the 1930s. Similar conditions are being faced by the soya bean crop in the US, and much of the damage to the crops has already been done. This outcome, and its severity, was quite unexpected, which illustrates our vulnerability to global weather shocks. As recently as June, the UN’s Food and Agriculture Organisation (FAO) was predicting an improved outlook for world cereal production in 2012, based on expectations of a much bigger maize crop in the United States. Furthermore, mild weather had led to early plantings of maize in the US which is now making the crop even more vulnerable to drought damage.

While the US drought is the main factor behind these latest agricultural price developments, other food producing regions are also experiencing adverse weather conditions. The Black Sea region, which is a major wheat producing area, has reported dramatically reduced crop yields; the monsoon in India has been below average; and the development of an El Nino pattern in the South Pacific is raising fears of crop damage later in the year in India, China, South-East Asia and Australia.

The food riots that were seen in a number of developing countries around the world at the time of the global food price spike in 2008 are a stark reminder and warning of how the current food crisis could unfold. A lot will depend on how sustained the adverse weather will be in various countries, particularly in the United States and India, but there is no doubt that as countries begin to restrict food exports, the potential is there for these developments to spread beyond one of food affordability to one of food availability. As food prices increase, diets deteriorate, malnutrition spreads and demands on public health services increase further.

The South African economy therefore finds itself in an extremely challenging environment, with the domestic economic growth outlook being dependent to an important degree on external developments. Given that the negative global growth outlook is likely to persist for some time, and we need to be mindful that the prevailing financial crisis has already lasted five years, with no end in sight, the challenges facing the domestic economy are daunting. But not all of our problems can be ascribed to these global factors. There are numerous underlying structural problems in the economy which are exacerbated, but not necessarily caused, by these global developments.

In line with the weak and deteriorating global outlook, the Bank has been progressively downgrading its economic growth forecasts over the past year. Growth in 2012 is expected to average around 2,7 per cent, down from 3,1 per cent in 2011. The most recent forecast for

2013 is a growth rate of 3,8 per cent, but the risks are seen to be on the downside. According to Reuters, the market consensus forecast for 2013 is 3,3 per cent.

Growth rates of this order of magnitude will not have an appreciable impact on South Africa's unemployment rate which currently stands at 24,9 per cent. It is instructive that during the high growth years between 2004–2007, when growth averaged around 5 per cent, unemployment declined to 21,9 per cent but this was quickly reversed following the crisis-induced recession in 2009. So if these patterns are to be repeated, we would need a number of years of significantly higher growth than we are currently expecting simply to get back to pre-crisis levels of unemployment.

However, the sustainable growth rate itself is constrained by the potential output of the economy, which, in turn, is determined by capacity and other structural constraints. At a simple level that implies that if we have unemployed resources or spare capacity in the economy, output can be increased in a non-inflationary manner. Research done in the Bank prior to the crisis showed that the potential output growth of the economy was between 4 and 4,5 per cent. Since the crisis, that has declined to around 3,5 per cent. This decline may have been due in part to some destruction of capacity and we also now know that growth will be constrained by the lack of adequate electricity provision until sometime next year at the earliest.

I should note that this does not imply that a growth rate in excess of 3,5 per cent would necessarily be inflationary. Currently the economy still has a negative output gap, which we estimate to be around 3,5 per cent, which is indicative of excess capacity in the economy. This means that the economy should be able to grow at rates in excess of potential without creating inflationary pressure until that output gap is closed.

South Africa's patterns of employment strongly suggest that the unemployment rate is not simply cyclical in nature, and is in fact structural. Even if we manage to grow at higher levels, it will be difficult to absorb such vast numbers of unemployed, especially in the short to medium term. In other words the natural rate of unemployment in South Africa appears to be in excess of 20 per cent, and significant structural changes will be required in order to make inroads into this. The structural nature of South Africa's unemployment and the structural constraints to growth are recognised in the various growth plans that have been published by government, the most recent being that of the National Planning Commission. It is generally accepted by growth theorists that sustained growth and structural change go hand in hand.

So the challenges are to close the output gap by getting growth to increase to be in line with potential, and to increase the potential output itself. Monetary policy can help with the former, but it cannot increase the potential output of the economy. This requires structural change, which includes a focus on investment and infrastructure spending to unclog some of the blockages in the economy.

Since the crisis, what growth we have had has been mainly driven by consumption expenditure. However, sustainable economic growth needs to be driven by investment. A reliance on consumption as a driver of growth is neither sustainable nor desirable: it implies a lack of savings and a build-up of imbalances, notably unsustainable and widening current account deficits. While the favourable pre-crisis growth rates were driven in part by strong consumption expenditure, they were also reinforced by strong growth in investment expenditure. Between 2003 and 2008, growth in fixed capital formation accelerated and averaged in excess of 12 per cent per annum. The ratio to GDP averaged around 20 per cent and peaked at 24,6 per cent in the final quarter of 2008. This compares favourably with the average of around 15,5 per cent of GDP in the previous 10 years.

Not surprisingly, investment expenditure was one of the casualties of the crisis, and has still not recovered fully. This is part of the explanation as to why South Africa's growth rates have lagged those of its peers. Investment expenditure contracted in both 2009 and 2010, but recovered somewhat in 2011 when it grew by 4,4 per cent. However, in the first quarter of 2012, while public corporation and general government fixed capital formation grew by

13,1 per cent and 9,3 per cent respectively, that of the private sector grew by a mere 1,8 per cent. This is a major source of concern should this trend continue, as private sector investment accounts for around 65 per cent of total fixed capital formation in the economy. The lagging private sector investment is consistent with the recent decline in business confidence that has been evident in the various indices. As a ratio to GDP, gross fixed capital formation had declined to 18,9 per cent in the first quarter of 2012. As a proportion of GDP, government and public sector investment now averages around 8 per cent, compared with 4,4 per cent between 1994 and 2007.

To achieve the desirable growth rate of 6 per cent will require an investment ratio of around 25 per cent. We are far from this and therefore require much higher rates of growth of investment from both the public and private sector over the next few years. To finance this in a sustainable manner will require more domestic savings, in other words a sacrifice of current consumption for higher future growth and employment.

While there are various and conflicting views on the role of government in the economy and in promoting growth, most people agree that an important job of government is to facilitate growth and investment by creating a positive investment environment as well as investing in infrastructure which enables growth directly and indirectly by freeing up logistical bottlenecks in the economy. But as important, if not more so, is investment in human capital, through provision of education and access to basic services, which has a growth support and a distributional element as well. This form of support includes the provision of public health.

So let me turn to the matter of Community-Oriented Primary Care or COPC, which I have become aware of and wish to share as an example of what can and is being done. In 2010 the Minister of Health, Dr Aaron Motsoaledi, initiated a proactive household and community-focused approach to promote healthy living, prevent, detect and treat disease early, and to manage, rehabilitate and palliate the ill. COPC in Tshwane District, for example, is being implemented and is designed around health posts. These are structures that are physically located in communities, with are health care practitioner teams, initially comprising professional nurses and community health workers. As teams, their responsibility is to interact in a proactive way with every household – as a collective as well as with individual members – in their jurisdiction. Their role is to promote health, prevent disease and detect disease early, and support treatment, rehabilitation and palliation; and to do this in a way that both develops capacity and shared responsibility for health care between service providers and service users.

Since 2010, Community Oriented Primary Care has been implemented in Tshwane in nine ward-based sites built on a partnership between the University of Pretoria (Family Medicine), the Department of Health and FPD (Foundation for Professional Development) in collaboration with private sector companies especially IT, health care providers and NPOs. The initiative involves inter-disciplinary and inter-professional practice. Schools and local NGOs are used as the premises for health posts and professional nurses head these PHC outreach teams and provide clinical and mentoring support. These health posts work very closely with health facilities within the geographic area and former home-based care givers are being trained to provide door-to-door services with each community health care worker being assigned 200 households.

Households are registered using mobile phone technology, giving the care workers a more accurate way to capture data and focus interventions. The GeoMed system currently registers households and has 8 modules to assess the health status of each family member. To date 14 745 households have been visited and registered and about 40,000 individuals have completed a health status assessment. Health posts have begun interventions, especially around TB and immediate health care needs. Fourth-year medical and other University of Pretoria students are attached to health posts, thereby learning on site and providing much-needed services, while community health workers are being trained on site and in a continuous way.

In this way the five principles that guide COPC, namely local situational analysis, comprehensive care, equity, practice with science, and service integration around users, are being given effect, building communities and partnerships, and making a real difference to people's lives.

This is an example of how, working together, we can make a real difference to the lives of our people and communities. To get things done we need to work together, and this requires trust and confidence which is essential for building a healthy and equitable society.

This evening you have all taken time out of your busy schedules to come here and contribute to Noah, an important initiative and example of the generosity of spirit and willingness to give both financially and personal time: one of the hallmarks of many South Africans. Noah's mission, values and objectives are helping build a resilient and resourceful society, which takes responsibility for those who are vulnerable, brings hope and a supportive environment. The character and strength of our democracy will be forged by, among other things, how we care for those who are vulnerable. Noah is an example of such commitment and care.

Thank you for inviting me to join you this evening, and I wish you well in the challenging times ahead.