South africa's economy and fiscal objectives

Countries

Research Question: How appropriate is the recently announced fiscal policy in terms of the state of the economy since 2007, the outcomes of ASGISA and the economic growth path envisaged by government?

In measuring the appropriateness of the South African fiscal policy stipulated in the general budget for the 2011/2012 period, one must look not only at South Africa’s current economic position but rather the state of the economy over the last five years as well as the context of the ASGISA outcomes and the overall economic path of the government.

Before one can measure their appropriateness in relation to past years and other measures, one must first fully understand what these fiscal policies were. The fiscal policy stipulated in the recent general budget of South Africa for the 2011/2012 period included an increase in government expenditure and a decrease in taxes: “ The Budget expanded spending…For the business sector, it expanded investment” [1] (shown in Figure 3. 1). “ For the small business sector, there were… tax relief measures.” [1] (R8. 1 billion in personal income tax relief). This decrease in tax can be seen in Figure 3. 2.

Fiscal policy includes two main measures, government expenditure and taxation. One can see that a clear expansionary fiscal policy has been adopted in 2011. This is to counter the monetary restrictive policy that has simultaneously been announced, " Monetary policy, operated by the SA Reserve Bank, will continue to be focused on controlling inflation, and… fiscal policy is countercyclical." [1]

Once one has a clear understanding of the current fiscal policy, one is then enabled to measure it’s appropriateness in terms of the last five years and other measures. One must begin by comparing certain financial indicators over the last five years (2007 – 2011) in order to gain a greater picture of the economy and then a safe deduction in terms of the effectiveness of the fiscal policy can be made. These indicators include the real gross domestic product; final consumption by households; economic activity and employment

The first indicator to be analysed is the real gross domestic product of South Africa from 2007 until 2010. From Table 1. 1; Table 1. 2 and Table 1. 3 one can recognise that South Africa’s real gross domestic product has decreased from 5. 1 in 2007 (Table 1. 1) to 3. 9 in the first half of 2010 (Table 1. 3). The reasons for this decline in real GDP over the last five years vary from year to year, with one underlying recession as the main driving force. This decrease could be used to understand the expansionary fiscal policy of the government in 2011. Government expenditure stimulates the economy and helps the GDP to strengthen; a logical step when one looks at the GDP decline over these five years.

The second indicator to be analysed is the household’s real final consumption expenditure, this indicator too shows a strong decrease from 2007 to 2009 (shown in Figure 1. 1; Figure 1. 2 and Figure 1. 3), with a slight increase in 2010 due to the FIFASoccerWorld Cup in South Africa and the beginning of South Africa’s recovery from the global recession. Once again an expansionary fiscal policy is required in a situation like this, as the government needs to in some way encourage spending by households. This is done by decreasing tax, which was done in 2011, and is therefore an extremely appropriate measure.

The third and final indicator one must analyse is the economic activity along with employment. This indicator also shows a decrease over this five year period due to the recession and the economy slowing down and therefore unemployment rising and economic activity decreasing as a result. (This can be seen in Figure 2. 1; Figure 2. 2 and Figure 2. 3)

The decline of these three indicators over the past five years is due to both the recession that occurred in this period as well other factors.

In 2007 the beginning of the decline of these three indicators can be seen. The first signs of the global economic crisis could be seen through indicators such as: “ The increasing turbulence in financial markets because of the sub-prime loan crisis and associated liquidity crisis, weakening inflation prospects and political uncertainty because of the election of Jacob Zuma… weakened economic prospects by the end of the year.” [2] South Africa had enjoyed sustained growth for a long period of time but the second half of 2007 was a negative turning point for the economy as “ Simultaneously the strong global growth of the preceding four years started to peter out.” [3]

In Table 1. 1 one can see the real gross domestic product and economic activity decrease in 2007 compared to 2006. When looking at 2007 in isolation an expansionary fiscal policy may seem questionable but when one considers the forecasts that would have been made at this point (the second half of 2007) concerning the impending recession it begins to make more sense.

In 2008 South Africa felt the recession begin to take a greater effect and a decline in economic growth. The greater the effects of the recession becomes the more appropriate the 2010/2011 fiscal policy begins to seem.

One of the greatest downfalls for the South African economy in 2008 was the electricity crisis that occurred during this time due to the fact that Eskom, South Africa’s primary electricity provider began to realize that the population size had exceeded its electricity provision levels. “ Severe logistical and capacity problems with the generation and transmission of electricity were experienced in the beginning months of 2008. This severely hampered production… culminating in a significantly slower rate of economic growth…” [4]

In Table 1. 2 it is clear to see the South African economy and Gross Domestic Product begin to decline. The real GDP decreased from 5. 1 in 2007 to 3. 1 in 2008. These are all signs of a slowing down economy and therefore the appropriateness of an expansionary fiscal policy

The issue of real final consumption expenditure by households also starts becoming a problem in 2008 as can be seen in Figure 1. 1 and Figure 1. 2. It decreased from 7, 2 at the beginning of 2007 to 2, 9 in the first half of 2008. This reduction in expenditure calls desperately for an expansionary fiscal policy (as reduced taxes will increase expenditure and government expenditure will push up production and total expenditure in the economy).

Finally in Figure 2. 1 and Figure 2. 2 the economic activity clearly decreases in South Africa in 2008 and thus needs to be stimulated.

In 2009 “ the financial crisis disrupted credit extension and paralysed trade and income flows.” [5] The global economic crisis impacted South Africa as “ the synchronised downswing in global economic activity spilled over into the country.” [5] These factors led to a decline in real gross domestic product from 3. 7 in 2008 to -1. 8 in 2009 (Table 1. 3); a decline in real household consumption (Figure 1. 2 and Figure 1. 3) and a decline in economic activity and employment (Figure 2. 2).

2010 represented a period where South Africa and the world first began to recover from the recession of the last few years. It was, “ a period of somewhat uncertain and uneven recovery in the global economy. Strongly stimulatory… fiscal policy measures were adopted… in order to restore and nurture economic growth.” [5] South Africa’s successful bid for the FIFA World Cup 2010 helped to stimulate the economy in this time. “ The…2010 FIFA World Cup tournament and recovering world economy underpinned activity in the first half of 2010” [5] This recovery saw an increase in real GDP from -1. 8 in 2009 to 3. 9 in 2010 (Table 1. 3); an increase in real consumption expenditure by households (Figure 1. 3) and a slight positive turn in employment (Figure 2. 3).

The current growth path envisaged by the government is essentially that of stimulating the economy over the next few years. The government is looking to grow employment, GDP and exports over the next few years and keep the upward curve of the economy progressing into the next few years. “ Real GDP growth was projected to reach 3. 4 percent in 2011, 4. 1 percent in 2012 and 4. 4 percent in 2013. Steady employment gains – of about two percent a year… Real growth in exports was expected to average 6. 5

percent a year.” [1] An expansionary fiscal policy is appropriate for such a growth path as a decrease in tax and increase in government expenditure would lead to a real GDP growth, an increase in employment and growth in production and therefore exports.

The Accelerated and Shared Growth Initiative for South Africa (AsgiSA) is aimed at improving South Africa’s main issues, unemployment and skills shortage. “ The aim of AsgiSA is to halve unemployment…and to halve thepovertyrate.” [6] These two main aims are achieved through an expansionary fiscal policy. The increase in government expenditure and decrease in taxes will lead to an increase in production which will increase employment levels and an increased need for employees will lead to more skills training and a decrease in skills shortage. This increase in production, consumption, income and employment naturally then decreases the poverty rate in the country.

The fiscal policy’s objective is to stimulate the economy, increase production, employment and overall income. One can therefore conclude that the expansionary fiscal policy adopted by the South African government aimed at increasing government expenditure and decreasing the tax burden is, in fact, an appropriate one when one looks at the declining state of the economy over the last five years with the recovery process beginning in 2010 (due to the FIFA World Cup and the recession beginning to slow down), the outcomes of ASGISA and the growth path envisaged by the government for the future. An expansionary fiscal policy is a appropriate process for South Africa when one looks at all of the above aspects.