SOUTH AFRICAN STATE DEBT - FACT OR FICTION AND IS THE MAURITIAN ECONOMIC MIRACLE A DECLINING MYTH: IMPACT AND CONSEQUENCES ON THE ECONOMY, BUSINESS AND THE DEVELOPMENT ENVIRONMENT

Anis Mahomed Karodia

ABSTRACT

This paper looks at the issue of state debt and its consequences upon the economy of South Africa, given the world economic crisis. On the other hand the paper attempts to look at the island of Mauritius on the basis that, in spite of the fact, that it has made good use of the aid it receives, the paper posits that its current position is now similar to that of Spain, in that, Mauritius is not the 'miracle' it seems. In so doing the researcher will articulate his thought process to substantiate the arguments put forward in this paper.

INTRODUCTION

It is obvious when one analyzes the Reserve Bank's bulletins in the recent past it reveals a South African economy, plodding along the continuum of subdued growth which puts the economy under extreme pressure. The large current account deficit, the gap between what the country, is exporting and what it is importing, comes in higher than market expectations at 6, 5 percent for the last quarter of 2012. This large deficit would most certainly place continuing pressure on the Rand, as its currency of exchange. This will most certainly bring about the risk of rising inflation, as costs rise in almost all sectors, with particular reference to food rises that will impact drastically and negatively upon the poor. South Africa pursues a policy of attempting to keep inflation to within a target band of 3 to 6 percent. The upward pressure on inflation limits the Reserve Bank's maneuvering, ability and room to drop interest rates. The question is can this be maintained over a reasonable time horizon?

On the other hand Mauritius has been the success and miracle of World Bank types and the likes of the Nobel laureate Joseph Stiglitz, who for different reasons see Mauritius as a model that other small developing countries, ought to be emulating and increasingly copying. However, Africa's "miracle" economy which has undergone a transformation from dependence on sugar exports to export of services such as tourism, financial services and information technology in one generation is starting to look very vulnerable. In Port Louis, the capital of the island there is now a strong scent and odour of Spain in the air" (Grynberg, 2013:6). For those people who wonder and project and look at, what is behind the great economic success story, it is more complicated than the Mauritian political and academic elite would have us and the world believe.

THE SOUTH AFRICAN DEBT CASE AND EMERGING CRISIS

Wiseman Khuzwayo (2013:3) states "that the economy has been under severe and significant pressure due to external conditions and home grown factors, with goods – producing sectors particularly affected, according to the Industrial Development Corporation (IDC)". Its Economic Overview report says, production stoppages in mining, due to industrial action, adversely affected performance. This has affected and impacted negatively on export revenues. On the other hand the broad mass of economists believe that Finance Minister Pravin Gordhan provided a reasonably balanced budget under different circumstances, but some have warned that South Africa was moving decidedly in the wrong direction over its debt levels (Pressly, 2013:1). According to Pressly, "almost every debt trap has taken the borrower by surprise" (2013). Greece is a great example. Is the country (South Africa) being placed in a debt trap, associated with debt levels of 60 percent or more of gross domestic product (GDP)? Lamberti (2013:1) indicates that there are a number of issues that raised South Africa's risk profile. Among these are, foreigners own a third of government debt stock. This has risen from about 10 percent in 2008 to about 35 percent now. It is obvious that this raises the question as to when they don't like South Africa anymore for whatever reasons, we have or will be confronted with the all embracing reality of a currency under pressure and bond yields will start to rise drastically. This will force interest rates to rise even higher. According to Lamberti (2013:1) this "is the anatomy of a sovereign debt crisis – when the wheels start to fall off."

Manufacturing has also taken a great strain. The supply side of the economy is still facing surplus production capacity in various segments, not only due to weak demand conditions, but also due to cost pressures and other competitiveness issues (Khuzwayo, 2013: 1). On the other hand the demand – supply gap has widened because of the increased demand for crude oil and petroleum products. Owing to all of this business confidence remained at low levels. In terms of Foreign Direct Investment (FDI) South Africa outperformed other African countries (4, 8 percent increase). Consumer spending will be moderate but the public sector will increase its spending by rolling out capital expenditure. This analysis and, other issues in the report of the IDC remains hopeful, but then, it is in many ways a government institution playing to the government agenda and gallery. Another downside to the economy of South Africa is the rising welfare benefits being doled out by government and the ever increasing public sector wage bill. By any stretch of the imagination, these issues are serious and can have devastating effects upon the economy and development of the country, if not controlled.

A very serious problem that confronts South Africa is the question of the political environment, such as a perceived lack of a crackdown on corruption, nepotism, and cronyism and, in many quarters the lack of the rule of law. Another Marikana type incident would lead to South Africa being answerable to the foreign sector. The problems of Marikana are continuing even today and, may have resulted or contributed to the very high fluctuation of the South African Rand, which is having negative effects upon the economy. Should this unpleasant scenario and circumstance reoccur and play out in real terms, the Central Bank and the Treasury within the Department of Finance may attempt to control interest rates, but South Africa is a small player internationally and the pressure of a high global interest rate environment would likely and ultimately push up the rates. What then is the caveat of this bleak picture in respect to such a situation? That South Africa has been increasing its debt from 20 percent of GDP five years ago to more than 40 percent today, there are many countries in Europe and some in Africa that are financing growth through debt. However, in spite of the above scenario it must be acknowledged and finitely understood by South African politicians and its Ministry of Finance that it is living beyond its means. “The projected deficit stands at R163 Billion but some estimates place it at R183 Billion. New debt could and will be accrued in the years that lie ahead, and this is estimated to be about R500 Billion” (Pressly, 2013: 1).

There is some good news, only if government can achieve the restructuring of state owned enterprises. There has been some talk about the privatization of South African Airways (SAA), Denel, the SABC and the Post Office, but in reality this is not nearly enough. These are loss making enterprises, cushioned employment far above normal salary levels, coupled with ineffectiveness and inefficiency. Is there any difference in terms of bailouts being offered to these State enterprises when one extrapolates it to the debt crisis affecting enterprises in European countries? The Minister of Finance, in reality is a lame duck Minister in a Cabinet that does not listen nor take seriously his suggestions about fiscal prudence and its business as usual. This is exemplified by the Minister’s response, when asked within the context of the Budget Review, if privatization was being suggested, Gordhan said, “it was most definitely not the direction that policy was going. Instead there was a need for the private sector to be involved with the government in infrastructure projects.” A typical response of a Finance Minister that appears to be out of tune with the realities of crisis, covering his tracks and maintaining the status quo, in order to please his cabinet colleagues and government policy imperatives, to the detriment of the country, with a view of keeping his job by not upsetting the apple cart and thus maintaining the status quo.

Given the imperatives of the last budget, a purposeful analysis of the budget reflects that it was a half hearted budget, pandering to the elite and proves that Marikana burned in vain. It therefore leaves no doubt that Minister Gordhan has gone from hero to Nero (Reddy, (2013: 12). The rapidly accelerating economic and social crisis that confronts South Africa, called for a budget that would have enshrined, a massive state – led effort to redistribute wealth and to uplift the poor through social spending and direct job creation. However, it is obvious that, South Africa’s wealthy have become absolutely and better off since the end of apartheid, supported by business profits, thus allowing the freedom of capital and thus guarantees unprecedented power over social and economic policy. In this regard Reddy (2013: 12) rightly points out that, “if not beholden to those interests, Gordhan’s budget would have started with the repudiation of the 25 percent tax revenue to gross domestic product rule that, appears to have come out of the negotiated settlement of 1993 and that has ensured that the “social solidarity our history demands has never been forthcoming.” Instead Gordhan turns to the very market responsible for unemployment to create jobs by giving more away to business with a youth wage subsidy. The economy continues to hemorrhage jobs. In short, Gordhan’s budget in 2013 is the latest indication that political elites and the corporations with which they have allied have no intention of altering the current course. It must therefore be the time in South Africa for purposeful resistance and social change that was born in Marikana. It is time for South Africans to reject the economic imperatives of the government, reject increasing state debt, state corruption and press the state to bolster revenues and to find ways to fund a National Health Insurance that will provide for the millions locked out of South Africa's hyper - commercialized health system.

What Finance Minister Gordhan has misunderstood and not reflected upon in his budget is the all embracing fact and reality that macro policies would not solve the unemployment problem and the realization that, it takes more than economic growth to bring about social inclusion and human development, in a country like South Africa, given its apartheid history, in order to reduce and deal decisively with the scourge of poverty, unemployment, inequality and the increasing rises in food and fuel prices and energy tariffs. The budget should have reflected and dealt with issues such as possible economic assumptions, (for example, how the budget is targeting infrastructure development and so on), the human face of poverty and small solutions to big problems. The budget in reality is silent on these issues, yet the state is steadily increasing state debt.

Brian Kantor (2013) states that "the news of a much lower Eskom tariff hike, 8 percent instead of 16 percent over five years, comes with a debt servicing cost, and therefore, Eskom's debt is expected in real terms to rise from R330 Billion to R550 Billion. Without laboring the point, it is essential that South Africa grows its economy sufficiently, but it does not appear to have an implementable plan to achieve this and to hold Ministries and their Ministers accountable. If growth is not achieved in the short term, there will be no alternative for the government, but to increase taxes in the new financial year. This would be a precarious intervention strategy because there would be increased pressure on South Africa's debt levels, to spiral drastically out of control. The answer going forward is to stabilize the debt ratio, to get the economy growing by improving efficiency, productivity, holding people accountable, reducing drastically corruption, policy shifts, nepotism and the like. If these variables are not looked at seriously, the country is very close to a situation where things can go wrong. This is the reality. Any positive picture can change rapidly, if strikes, police brutality, crime, corruption, government mismanagement, uncontrolled government expenditure and inefficiency are allowed to reign supreme, it could trigger all sorts of trouble and gloom for the economy. This would negate growth which would remain too low and the costs of servicing debt will rise significantly. This is the real danger.

By the same token Rene Vollgraaff (2013: 130) states that "investment flows helping to finance South Africa's current account deficit are cause for concern, due to their unpredictable nature. There is the real risk to South Africa's credit rating. Standard and Poor, has warned that South Africa's credit rating could lower the country's rating again if funding for the current account deficit began to dry up. The issue is simple can South Africa sustain its appetite for assets? It also brings to the fore the fact that in terms of our overall indebtedness ratios, both for the public sector and for our external debt in total, South Africa is not actually a heavily indebted nation, "but Reserve Bank governor Gill Marcus warned that Foreign Direct Investment (FDI) flows had been volatile and the growing proportion of bonds owned by non – residents, could constrain the pace of inflows." (Marcus, 2013: 13). Michael Keenan 2013: 13) on the other hand posits that "it is not as good as it has been. It is evident when you look at the rand's poor performance, particularly against other emerging market currencies. Investors are showing a distinct preference for our peers." This is a tacit indication that we require more FDI in South Africa. It has also to be acknowledged that there has to be a distinction between FDI and portfolio flows which are often artificial in nature and that "South Africa has very liquid, well – regulated and integrated financial markets. The reason why a country like Mozambique has a much higher percentage of FDI is because it does not have the proper financial markets, which we do have. That is why we attract more of these liquid and portfolio flows" (Vollgraaff, 2013: 13). Given this data analysis, according to Keenan (2013), "it means the current account deficit was underestimated for much of last year." Is it a case given this scenario that the weaker rand reflects a deep economic flaw and contributes to state debt, when one considers that earnings from exports of goods, services fail to cover import costs? Does this indicate that something is seriously out of kilter in the way the economy works? Human nature suggests that long – term economic improvements can't be achieved by a weakening currency and, through cutting interest rates for that matter, and in so doing making the country less competitive due, to greater effective protection of inefficiency, along with potentially promoting a greater skills drain. In reality, the issues pointed out in this article, should concern all South African's and indeed the government. It appears that state debt is spiraling out of control in Africa's largest economy, and therefore, the question needs to be answered - as to whether South African debt is a question of myth or fiction.

THE MYTH OF THE DECLINING MAURITIAN ECONOMIC MIRACLE

It has to be understood and appreciated that the Mauritian economic miracle was due to the generosity that the international community has foisted on to Mauritius, which makes it unique among African countries. This was in past, as a result of the pessimistic assessment of another Nobel laureate, James Meade, who at independence, thought "Mauritius would be a hopeless basket case, but the European Union (EU) gave the country a huge sugar quota, which allowed Mauritius to export sugar at two to three times the world price" (Grynberg. 2013: 6). This was offered to several other countries, but not a single of these countries (Fiji, Jamaica and Guyana) received a quota as large as Mauritius, under the Lome Convention of 1975. This created huge profits for the country's largely white sugar barons or Grand Blanc as they are known in Mauritius. This was equivalent to 5 to 6 percent of the country's GDP every year. These benefits were accumulated by a few large farmers and allowed by government unchecked and invested in tourism and textile factories.

For years the European Union wanted to get rid of the Lome Convention, and the Cotonou Agreement, on the basis that they did not benefit Africa and be replaced by the infamous economic partnership agreements, which are free market / trade agreements. In fact and in reality is the all embracing fact that, Mauritius is the only African country were transformation occurred on the basis of European philanthropy and generosity coupled with (unlike South Africa) were the elite were not corrupt and did not squander the aid obtained and thus guaranteed viable business to thrive and succeed. Mauritius also benefitted from the United State's Agricultural Growth and Opportunity Act and, was permitted to export its textiles duty free. The Mauritian government was also able to create, to a limited extent an elite, of new settlers granted permanent residence which created an international and cosmopolitan business character. The 1990's saw the advent of export processing zones, allowing the Indian Ocean Island to move from an agricultural to an industrial exporter in less than a decade.

Roman Grynberg (2013: 6) points out that "what is less known is the crucial role that India is now playing in the transformation of Mauritius from an industrial to a service exporter. This is exemplified by the reality and fact that, about 42 percent of India's foreign direct investment in 2010 came from Mauritius, and strengthened by the double taxation agreement, which exempts Mauritian companies from Indian capital gains tax." In this regard Grynberg (2013) states that this agreement has cost the Indian government more than $600 million dollars and India wants to now bail out of this agreement". The Mauritian government is aware of this and when this happens Mauritius will be a big loser, impacting on its economic growth and on its economy, as a whole. Mauritius was thus able to create a tax haven for would be investors and this has served them well thus far. In this way it also empowered local businessmen by allowing them to hold board positions within the companies of foreign investors. According to 2010 statistics, financial intermediation grew to 12, 3 percent of GDP.

Realizing the all embracing reality of how vulnerable Mauritius is, the government has diversified its economy. The fastest growing diversity and probably the most risky has, been the sale and development of real estate to largely foreign takers / buyers of land. The question therefore arises, is this sustainable? The short answer is definitely not, on the basis that the Island will run out of good land or the prices will fall and bring about collapse. Does this in Mauritius now represent the Spanish real – estate bubble that plunged the country into a long and deep recession in 2007 – 2008, and from which it still has to recover. Grynberg (2013) states that "in Mauritius's transformation from a goods to a service exporter, its balance of payments is now starting to look very wobbly and has been worsening steadily as exports decline. The current account deficit was slightly less than 12 percent of GDP in 2011, well above what most economists consider to be sustainable in Africa.

Despite the development of new commodity exports, the economy has suffered a serious relative decline in its traditional exports of sugar and textiles, and imports, including oil have been rising rapidly and to this end Grynberg further points out that "the only thing keeping Mauritius afloat has been a capital account surplus and significant exchange reserves." It is on a shaky path because its economy now rests on land and property and the shaky trade agreement with India. Grynberg further points out that Mauritius "is on a shaky path and, although the devaluation of the Mauritian rupee is strongly opposed by some government economists, more and more government ministers are saying openly that it is living beyond its means" (No different to South Africa). The structural change in its economy from a goods exporter to that of a service exporter has also moved Mauritius from having a relatively balanced current account to unsustainable deficits (Similar to South Africa). It has converted itself into a manufacturing and service exporter in one generation, which no other African country has achieved. This achievement has been done because of the unprecedented levels of trade assistance from Brussels, Washington and Delhi.

In spite of this achievement and the pride of the Mauritian people of these achievements Grynberg states that "the miracle has given rise to an enormous amount of hubris in Port Louis. But what is needed now is more modesty as the assistance, given the world economic slump and meltdown, causes its own problems within the context of world economies, particularly upon the economies of developing nations, and probably as Mauritian luck and comfort runs out. The Mauritian so – called miracle is not what it is and in all probability the good times are coming to an end. The Mauritian government and its people need to understand this reality and phenomenon, and perhaps it is an ideal time to reevaluate its policies and economic realities as the world economic crisis takes its toll on most countries of the world, both developing and developed nations.

CONCLUSION

This paper outlined the emerging consequences and implications that could result from, the increasing state debt of South Africa and the declining miracle of the Island state of Mauritius. These issues have to be seriously considered by the South African and Mauritian governments in terms of development, business opportunities, employment and the reduction of poverty and inequality. The issues raised are frightening and must be seriously looked at in the immediate future. It's always important for governments to never plaster over the cracks, because the house can fall down. Increasing debt can destroy the fundamentals of economic recovery and usher in strife with devastating consequences and contribute to significant economic stagnation for any country, whilst the reliance on foreign aid can have long term negative consequences for the success of any growing economy, in terms of sustainability, people participation and development success. A reevaluation of policies is therefore required by both the governments of South Africa and Mauritius, in order to become winning nations.

- Anis Mahomed Karodia (PhD): Is the former Director General of the North West Department of Education. He is currently a senior faculty member of and researcher at the Regent Business School, 35 Samora Machel Street, Durban, Kwa Zulu Natal, South Africa.

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