

Putting flesh on the bones

In both August and September I wrote in this Newsletter that the only way out for the stalled SA economy is a social compact, an agreement of sorts, where the powerful stakeholders in society agree on the way forward. What would such an agreement look like? Is it a practical possibility or just pie in the sky?

Firstly, others have done it. The Netherlands and Ireland are classic cases of countries that forged compacts in the 1980s and 1990s respectively, which got them growing. Ireland then lost it again when hit by the Global Financial Crisis of the 2000s, but the Netherlands have done well, thank you. So theoretical stuff it is not. A compact that generates growth and reduces unemployment and poverty is very doable.

Taking the idea forward

Now Prof Ravi Kanbur from Cornell University in the US has made a powerful contribution to the social compact idea. He is also co-editor of the Oxford Companion to the Economics of SA – a must read for anybody interested in the SA economy beyond what a colleague calls “the four rates – growth rate, interest rate, inflation rate and exchange rate”. Prof Kanbur certainly delves much deeper than just the “four rates” and is well versed on SA. In a recent article he explored what he called “contours of a grand bargain” as a way to deal with unemployment and poverty in SA.

He makes the common sense but important observation that there is wide agreement on SA’s problems (unemployment, poverty, inequality) but very little agreement on which policies to pursue to address these problems. There is no lack of ideas; hundreds of proposals are floating around from nationalisation to Piketty’s wealth tax to unbridled free markets. But there is a complete lack of agreement on which ideas to follow. This he ascribes to a variety of reasons, ranging from technical analysis to political persuasion and ideology.

He suggests the way out may be a “grand bargain” – not so much a consensus, as a “package ... that balances opposing perspectives whose differences cannot be resolved through technical debate...”.

Competing perspectives underline the problem

The lack of agreement on what to do is beautifully illustrated by the arguments about labour and employment. The one school (classic labour economics) says all that has to happen is that wages must fall far and deep enough for the unemployed to be employed. The employment co-efficient of 0.7 is marshalled in evidence – that number simply means a 1% decline in wages will lead to 0.7% increase in employment. Or a 10% decline in wages will result in a 7% increase in employment.

No so easy, says the counter school. To halve unemployment would require wages to fall by between 20% and 30%. The resistance will be enormous. All the more so when the wage cut is only for the workers or people on already low incomes. Some get millions and others must cut wages. And what are the chances of higher-income people agreeing to have their wages cut? Nil. Just ask any group of people at the coffee station or over dinner whether they are willing to take a 25% cut in their income. Phone me if you find any volunteers.

When wage cuts are on the table, it is always “other people” that must cut – “management and fat cats” if you are a worker; and the “workers” if you are a manager or fat cat. Nobody is prepared to cut their **own** income, thus deadlock is inevitable.

A different way

So if the wages-must-fall approach is more wishful thinking than real policy, what then?

Here Prof Kanbur makes a useful suggestion. Focus on the non-labour cost of employment, he suggests. Use that as a contour for a “grand bargain”.

Non-labour cost would include items like infrastructure, both for enterprises (think electricity), but also for workers (think public transport that reduces the cost of travelling to work). It can also include steps to curb monopolies and concentration of pricing power, so that pay packets can stretch further whilst also allowing more production and thus more jobs. Another item could be to reduce regulations which hinder the development of small business.

A host of issues

Another important contour is fiscal rectitude. Set deficit and debt targets that keep the capital markets and ratings agencies calm. Prof Kanbur suggests it includes an agreement to curb the state’s salary bill. That will require some convincing, but if non-state workers are seen to share in the sacrifice, it will be hard for the civil servants not to agree. More so now that the ANC’s just concluded policy conference resolved that budgets should prioritise investment above consumption.

Another contour can be around education. Prof Kanbur quotes evidence that Brazil’s success in reducing inequality – the Gini declined from 0.63 to 0.54¹ – was partly due to reducing inequality in education.² He thus suggests a contour around bigger investment in human capital – employ more interns, train more artisans, leverage public and private spending. Perhaps link that with a push-back of SADTU’s power around school appointments and transfers....

NDP

None of these ideas is new. It is articulated in the NDP and by many others. The trick is to include known ideas in a “grand bargain” that can get implemented. The NDP stated the importance of a social compact to tackle the wide ranging problems of SA. Ex-minister Manuel reiterated the importance of a social compact at a Financial Times conference in London last week. A social compact is an important way of implementing the NDP.

Pro-active better than reactive

SA’s political-economic landscape is shifting. A wealth tax is gaining traction; pressure around land is rising; a minimum wage is on the table; confidence is sliding and growth is stuck around 1.5%. One option is to sit back and let things develop. The much better option would be for business and other leaders to take the initiative in constructing a package of measures that enhance growth and employment.

It will require a shared sacrifice and nobody will get just what they want (the many ideologues will have to take a backseat here), but a balanced package that spurs growth is preferably to stagnation.

¹ SA’s Gini is around 0.68

² The introduction of a minimum wage also played a role

So What?

- The idea of a social compact is not pie-in-the-sky at all. It has been done in other countries and it can be done in SA as well.
- SA's problem is not a lack of ideas, there are many; the problem is agreement on which ideas to implement.
- Agreement is difficult for reasons of politics, ideology, vested interest, a particular worldview and so on. Much more than just "the four rates" are at stake.
- A package that recognises these competing viewpoints and balances them creates a visible path forwards.
- The contours of such an agreement can focus on items like the non-labour costs of employment, specifically infrastructure, public transport and the like. It must also include macro-economic prudence and a special focus on education.
- The ground is shifting – now is the time for an initiative to construct a "grand bargain" for the way forward.