# South Africa: Improving productivity and the efficiency of public spending to bolster living standards

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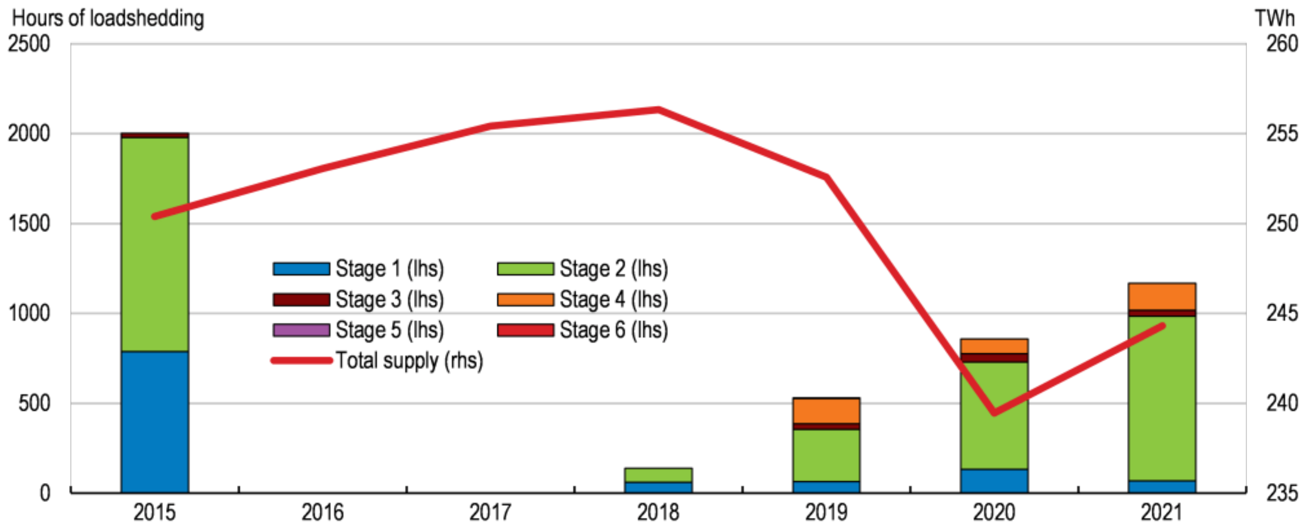
South Africa needs bold structural reforms to lift economic growth. The coronavirus crisis, flooding in Kwa-Zulu Natal and widespread electricity cuts have weakened an already fragile economy (Figure 1). GDP growth is projected to slow to 1.8% and 1.3% in 2022 and 2023, respectively. The war in Ukraine is creating additional risks: on the one hand, rising commodity prices are prolonging the commodity boom cycle, but, on the other hand, higher inflation is denting purchasing power. The social distress relief grant, put in place during the pandemic and covering up to 10.5 million individuals, has helped mitigate the effects of the crisis and inflation on poverty, but may not be sufficient if the economy does not grow faster: unemployment stood at 34.5% in the first quarter of 2022.

**Figure 1. Electricity availability has fallen dramatically**

Yearly hours of load shedding by stages and total annual supply in TWh




Note: Loadshedding is implemented in stages with more frequent power cuts at higher stages. At every stage of loadshedding, Eskom rations the country by a further 1 000MW of power. Stage 1 = 1 000 MW, Stage 2 = 2 000 MW, Stage 3 = 3 000 MW, Stage 4 = 4 000 MW, Stage 5 = 5 000 MW, Stage 6 = 6 000 MW.
Source: Eskom; Council for Scientific and Industrial Research, South Africa; Statistics South Africa; OECD calculations.
Weak growth performance has deep roots. South Africa’s growth underperformed during the past decade: GDP per capita was already lower in 2019 than in 2008, and over the period 2009–2019, GDP growth averaged only 1.1%. Weak economic growth is mostly explained by declining productivity due to deteriorating infrastructure, weak telecommunication networks and low investment. Failing electricity generation has become the main bottleneck to production and concern for investors. Skills shortages remain a constraint in several sectors. Adding to the issue, there is limited fiscal space to cope with high public spending pressures, notably for infrastructure projects, electricity generation, education and also social transfers. The debt-to-GDP ratio stands now at 70% of GDP.

The **2022 OECD Economic Survey of South Africa** highlights three areas to boost potential growth and improve medium-term fiscal sustainability. The government should:

- **Improve the efficiency of public spending and of the tax**

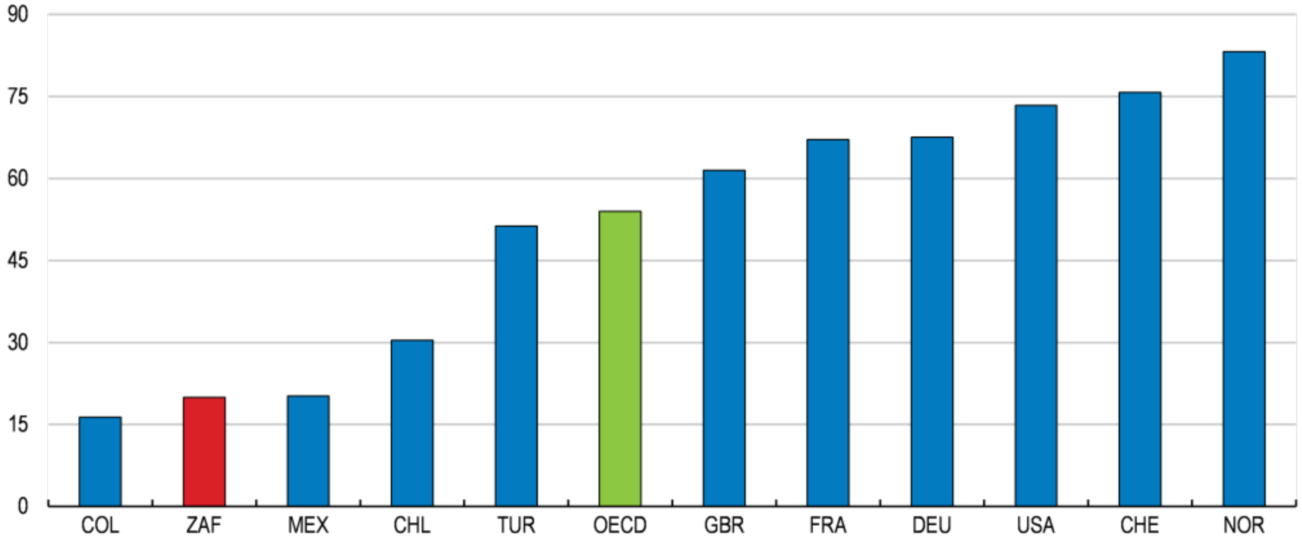
**system:** Government exposure to state-owned enterprises remains high and, in terms of state guarantees, amounts to around 16% of GDP. The financial performance of SOEs worsened with the pandemic, increasing the pressure on public finances. Restoring the finances of the main SOEs and privatising those intervening in competitive markets would reduce the fiscal burden. Better enforcement of sanctions for corruption offences is needed to restore public confidence and the proper functioning of public services. Reducing the size of the government's wage bill also remains essential. Finally, even though South Africa's tax-to-GDP ratio, standing at 26% of GDP, is higher than many emerging economies, there is room to increase tax revenues, while reducing inequality and making the tax system less distortive to growth. There is a wide range of tax provisions and exemptions that reduce effective tax rates significantly below statutory tax rates. The corporate income tax rate of 28%, for instance, is relatively high but tax liabilities are reduced by generous assessed losses.

- **Reduce labour market rigidities:** The pandemic has worsened labour market outcomes and further increased inequality. Unemployment is higher than the OECD average and peer countries, particularly for the youth. Wage bargaining remains confrontational and labour-employer relations have been ranked among the weakest by the World Economic Forum. The wage bargaining system suffers from a relatively high level of bargaining, at the industry level, declining representativeness of bargaining councils. Agreements are extended to non-members and often inadequate for SMEs. More wage negotiations at the firm level should be encouraged. For instance, agreements with representative unions at the firm level could be accepted as substitute to agreements at the sector level.

- **Boost productivity growth:** South Africa's productivity is comparatively low, and it has been falling over time (Figure 2). Improved infrastructure, enhanced competition and better skills are required to lift productivity, potential growth and living standards. Low and inefficient public investment, with insufficient cost-benefit analyses, are weighing on the quality of transport, telecommunications, and energy infrastructure. Maintenance is not conducted as regularly and early as needed. The funding of infrastructure projects from the general government budget should be augmented based on cost-benefit analysis. The economy suffers from lack of openness and competition. New broadband frequencies should be allocated rapidly to increase speed and lower subscription fees. Entry into professional services should be facilitated. Aligning competition policies of sectors regulators with the Competition Commission would open business opportunities and ease the entry and growth of SMEs. The country suffers from shortages of skilled workers and skills mismatches more generally. Efforts to increase the quality of education should continue and include increasing the quality of primary and secondary schools, further developing vocational training and adult learning. Changing the financing formula of universities would reduce the cost per student and allow enrolling more students in tertiary education.

**Figure 2. Productivity is lagging behind**

GDP per hour worked in constant USD PPPs, 2021 or latest



Source: OECD productivity database.

**Reference:**

OECD (2022), *OECD Economic Surveys: South Africa 2020*, OECD Publishing, Paris, https://doi.org/10.1787/d6a7301d-en