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The Role of Government

Re-purposing the Govt. of South Africa to focus on creative legislation

Despite the benefit of over two centuries of history to look back on when formulating economic policy, successive administrations of the new South Africa have eschewed human ingenuity in favour of state intervention. Today, the State looms so large over the economy that there is little room left for the individual to demonstrate ingenuity. A slate of Government policies (RDP, GEAR, ASGISA, NDP) have found strong expression in support of "leave it to me" and State-Owned-Enterprises. The problem is that SOEs operate in creative domains whose fundamental underlying ingredient of success is human productivity. In such domains, outcomes follow a Pareto Distribution where there is wide disparity between businesses that are successful and those that fail. Profits are distributed away from SOEs to their competitors (e.g. SAA vs. KLM) or other players in the value chain (Eskom vs. Exxaro). Winner-take-all outcomes are not what the State's redistributive ideology are trying to achieve. Incessant attempts to panel beat a Pareto Distribution into a Normal Distribution demonstrates that the Government does not appreciate the complexity of the problem it is trying to solve. Normal Distributions exist in factors such as intelligence, cognitive ability, motivation, and so on. The distribution of these factors does not follow race, gender, or religious traits as the Apartheid Government pretended for so long. Had the Government limited itself to creative legislation in Parliament to democratise and regulate these factors and allow human ingenuity to solve local problems, the country would not be on the cusp of systematic risk in energy, water, education, health care and the capital markets.

FIRST AVENUE
INVESTMENT MANAGEMENT
21 Fricker Road, Illovo, Jhb, 2196
+27 11 772 2480
info@firstavenue.co.za

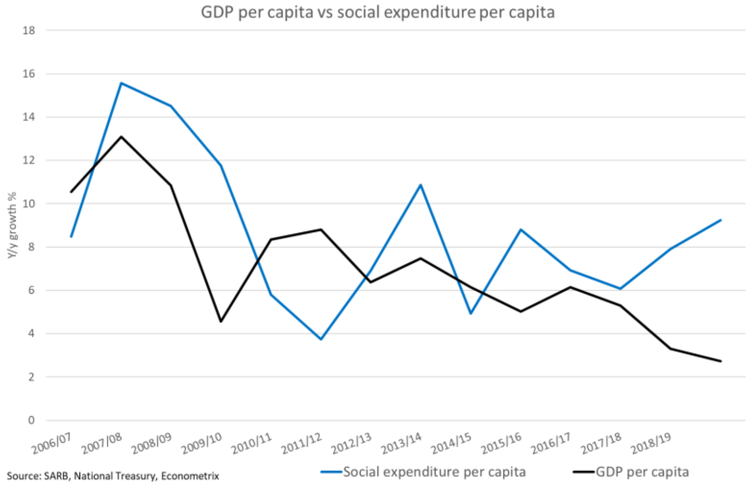
What is the purpose of a Government?

The COVID 19 pandemic has reminded all of us the world over of what the essence of the Government's role is; to anticipate and minimise, if not avoid, the risk of collapse of an entire system. Often this risk is associated with the financial system, but one may very well apply it to education, healthcare, safety and security, energy, water, and such whose malfunction could collapse an entire economy. The approach of the Government of South Africa, both pre- and post- independence, to managing systemic risk has been to build, own, and operate assets (State Owned Enterprises) as delivery mechanisms of their legislated policies.

Post-Apartheid administrations have, and continue to, use State Owned Enterprises (SOEs) to address the skew in two factors that combine to form economic development, namely, (i) access to economic opportunity to create wealth and (ii) protection from the vagaries of the economy in the event one fails to create wealth. Similarly, in the past, Apartheid Governments were remedying an ethnic skew against Afrikaners by the English. However, these SOEs also had another objective, namely, to deny non-Whites equal access to wealth creating opportunities as well as protection against economic calamity. In this, Apartheid Governments created (economic and social) systemic risk which ultimately bankrupted the country (financially and morally) and eventually undermined the very existence of SOEs. Having assumed Apartheid era debt at independence, the new Government privatised some SOEs in order to pay down the debt to a manageable level. However, post-Apartheid Governments kept a large swathe of SOEs with the intention of using them to reprise the goal of remedying racial skews suffered by Black, Indian, and Coloured people. Yet, here we are in 2020 and, for all intents and purposes, post-Apartheid SOEs have led to the financial ruin of the country.

The one thing post-Apartheid SOEs have in common with Apartheid era SOEs is that they both played a leading role in degrading and collapsing the financial and economic system. Notwithstanding the argument that Eskom, for instance, was in a better state then than it is now, SOEs were conduits of misallocation of capital. In other words, capital that should have been allocated to human ingenuity was issued to SOEs. Protection of the citizen against the vagaries of the economy has come at the expense of economic growth. The contrast is stark on a per capita basis:

Figure 1: Chart of GDP per capita vs. Social Grants Spend per Capita



Source: SARB, National Treasury, Econometrix

This is the unintended outcome of all the Government's economic policies since 1994: Reconstruction and Development Plan (RDP), Growth, Employment, and Redistribution (GEAR), Accelerated and Shared Growth Initiative for South Africa (ASGISA), and now, the National Development Plan (NDP). All these plans are cut from the same cloth.

In both pre-and post-independence, deep introspection by a wide variety of actors in society has offered up reasons for the failure of the Government and its entities. Corruption ranks high among them. Hand in hand with corruption is a lack of sound governance. Incapacity is another. Hand in hand with that is the question of the mandate of the SOE – is it the right mandate to pursue? Is it clear or ambiguous? And so on, and so on. The introspection, under Apartheid as it is now in the post-Apartheid era, tried to figure out why such a good thing went so horribly wrong. As the din of introspection rises, the truth hid then, as it does now, in plain sight.

SOEs are an ideological construct, a philosophical reaction to a previous deeply unjust economic order. Apartheid nationalism found economic expression in SOEs whose mandate was to address the devastating blows Afrikaners took from British mercantilism. The British amassed an empire of colonies from which they extracted raw materials and resources in exchange for finished goods of higher value. This led to a favourable balance of trade account which was thought to increase national wealth – the French, Spanish, and Portuguese competed with the British for colonies. Mercantilism though had no civility. It contained many acts of inhumanity and treated people in the colonies as possessions.

Naturally, people in the colonies waged rebellions, battles, and wars to repel the dominion sponsored or approved by mercantilists. The deep scars of the Anglo Boer wars left many Afrikaners vanquished, ravaged, and destitute. It is no wonder that Afrikaners embarked on centralised efforts to economically uplift the Afrikaner. You can clearly see the parallels between the condition of the Afrikaner in the mid-20th century (1948) and the African in 1994 at independence. African reaction to Afrikaner fascism was not only strong, but also found expression of economic liberation in State Owned Enterprises. Today, as a result of the Government's efforts to use SOEs to drive economic development, there are about 721 SOEs which are exempted from competition (monopolies) or exist solely on Government funding. The Government is now larger in all ways imaginable than it ever was before – as an employer, service provider, debtor, creditor and customer and so on.

Yet, the truth hiding in plain sight is that both the Afrikaner era Governments and post-Apartheid Governments both looked at civilisation through the lens of state intervention rather than human ingenuity. In other words, they both believed that State-owned and operated companies were far better at civilising, refining, and enlightening society than ingenuity demonstrated by individuals in their local communities. This oversight was remarkable because Afrikaners, as descendants of both the Dutch and French migrants to Holland, the Huguenots. They would have been, or should have been, aware of the arguments (and literature) raging through Europe regarding how wealth was created, distributed or destroyed. In fact, Cape Town was settled in 1652 by the Dutch as a result of it being a refreshment outpost for the Dutch East India Company.

The refreshment outpost was intended to supply Dutch ships (headed to Asia) with fresh fruits, vegetables and meat as well as to enable sailors to recuperate. Such companies (the British equivalent was the British East India company) added enormous wealth to their mother countries. By some estimates, the Dutch East India Company would have been worth US$7.8tr had it still been around today. Adjusted for inflation, the British East India Company would have been worth US$4.1tr today. The Dutch East India Company was more prolific because it had quasi Government powers – it could start and wage a war using Dutch soldiers. There was a French East India Company too! This was the heyday of mercantilism. Beyond the devastation mercantilism wrought on the colonies, it also created huge disparities in wealth inside the dominion (seat of the empire).

The great thinker Adam Smith, in his book "Wealth of Nations", published in 1776 argued that European countries were competing for the wrong thing. Wealth wasn't to be found in commodities like gold and silver. It resided in human ingenuity. The more ingenious human labour was, the more valuable the wealth it created. If the labour class could have the freedom to pick their job or enterprise, all the while knowing the Government would leave the money they made well alone, why wouldn't they work hard and imaginatively at it? They would produce goods and services of high enough quality to trade with other nations. Nations would not need to waste money on defence and wars. Shortly after Adam Smith published his book, Americans successfully revolted against British rule in what is known as the American War of Independence.

Descendants of the Dutch should have been familiar with this explosive datapoint, if not Adam Smith's arguments. The American War of Independence was the shot that rang across the world. The Netherlands, a prolific coloniser, reached the pinnacle of European commercial success between the sixteenth and seventeenth centuries. There is no way Adam Smith's own shot that rang across the world could not have been heard in the Netherlands. The Huguenots would have been aware of similar sentiments, encapsulated in the term, "Laissez Faire", in their former homeland of France. The term laissez-faire likely originated in a meeting that took place around 1681 between powerful French Controller-General of Finances, Jean-Baptiste Colbert, and a group of French businessmen headed by M. Le Gendre. When the eager mercantilist minister asked how the French state could be of service to the merchants and help promote their commerce, Le Gendre replied simply: "Laissez-nous faire" ("Leave it to us" or "Let us do [it]", the French verb not requiring an object). Even Karl Marx, who saw the capitalism as a progressive stage that would eventually stagnate and give way to socialism was awe struck by the prowess of human ingenuity. He just wondered why something so smart wasn't creative enough to fix its own internal contradictions.

By 1720, about 270 French Huguenots had settled in the Cape. Trade and travel between Europe and settlers in the outpost of South Africa continued apace even as great thinkers debated wealth, war, liberty, and human ingenuity. How is it that, in 1948, descendants of settlers didn't consider it (human ingenuity) as a viable option to develop South Africa? In 1994, the new Government had an even longer lead time on the idea of commerce. Africans were an integral part of enterprise in South Africa. It is easy to make the same point about Black South Africans as American author and playwright James Baldwin, makes about African Americans in the United States; neither would be what they are today without their Black populations. All spheres of the country were built on their back. Why then would the new Government, even with the benefit of binoculars to look as far back into history of both the country and the world, forsake centuries old intellectual capital in corporate South Africa for state intervention? The evidence for human ingenuity in South Africa was overwhelming and Black people were part of its engine.

At the infancy of the new South Africa, the country was the highest scoring developing country in the International Property Rights Index. The Index effectively ranks countries by the laws of commerce that underpin market-based contracts have not only taken hold but flourished. In 2007, South Africa, governed by Roman Dutch Law, ranked 20th globally (48th in 2019). In this, it had the distinction of punching at the same weight class as heavyweights such as the G7 countries. Roman Dutch Law is an uncodified, scholarship-driven and judge made legal system based on Roman Law as applied in the Netherlands in the 17th and 18th centuries. It has served as an active ingredient in the development of South Africa's economy. Thanks, in no small part, to idea diffusion by the Dutch Settlers in South Africa in the 17th century. When Afrikaners chose state intervention, they knew better than that. They had seen contract law work very well for private enterprise in The Netherlands, the world's first high income country. Today, South Africa outscores its fellow members in BRICS at protection of property rights and intellectual capital (South Africa generally follows English law in both criminal and civil procedure, company law and constitutional law. We are not so strong in some of these areas such as criminal and civil procedure).

Perhaps it is clear why, in 1948, Afrikaners would not double down on human ingenuity. They were more interested in making a racial case than a human case. Why would a people who know of the huge gains of human ingenuity seek to impose debilitating outcomes on others? One way to look at the moral failures of Apartheid (treating people and children as property, cheap labour, abusing the environment, and so on) is to see that they are perversions of the desire to own, produce, and consume more by any means necessary. Isn't that what colonialism, slavery, mercantilism, imperialism were – a desire to own, produce, and consume more by any means necessary? The Apartheid Government figured out that it could tilt the Pareto principle (more on this shortly) heavily in favour of White people if it not only gave White people a leg up through SOEs but also excluded an entire category of people (e.g. Blacks) from participating in iterative trading activities and creative endeavours.

If Afrikaners overlooked the obvious case for human ingenuity in individuals because they were more interested in making a racial case, what motivated post-Apartheid state intervention to encroach on the private sector and ultimately crowd out human ingenuity as it has since independence in 1994? It may very well be to avoid the perversion of ownership, production, and consumption that tend to rear their ugly heads in capitalism, as they did under Apartheid, from overrunning the system. It is fair to say policies of all administrations in post-Apartheid South Africa have one unifying quality, namely, redistribution of wealth. Given the history of the country, who could argue with the intention to markedly improve the lot of non-white peoples as evenly as possible? There is only one problem; not all distribution curves are equal.

What post-Apartheid Governments wanted to see was a normal distribution of wealth. Often that creates a large middle class and smaller disparity of wealth in society. Wealth and productivity, however, follow the Pareto distribution or Price's Law. A small number of people in any creative domain, where the fundamental underlying measure of success is human productivity, tend to produce over 50% of the output or outcomes in any industry. This can be observed in the number of goals scored in a league, number of novels or paintings sold, number of artists who get airplay on radio, actors who get to play the lead in blockbuster movies, or amount of GDP produced in the world, and so on. How small is this number of people? It is the square root of the number of people engaged in that creative domain. So, in a company of 100 people, 50% of the profits can be traced back to the efforts of 10 people. In a company of 100 000, 100 people account for 50% of the profits. The implication of the mathematics here is that incompetence grows exponentially while competence linearly.

Figure 2: The Difference in Outcomes Between A Normal (black) and Pareto (grey) Distributions

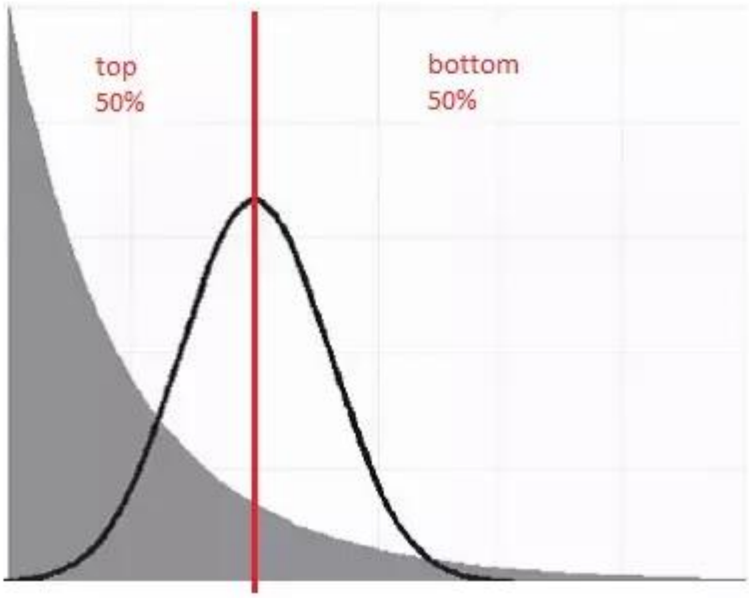
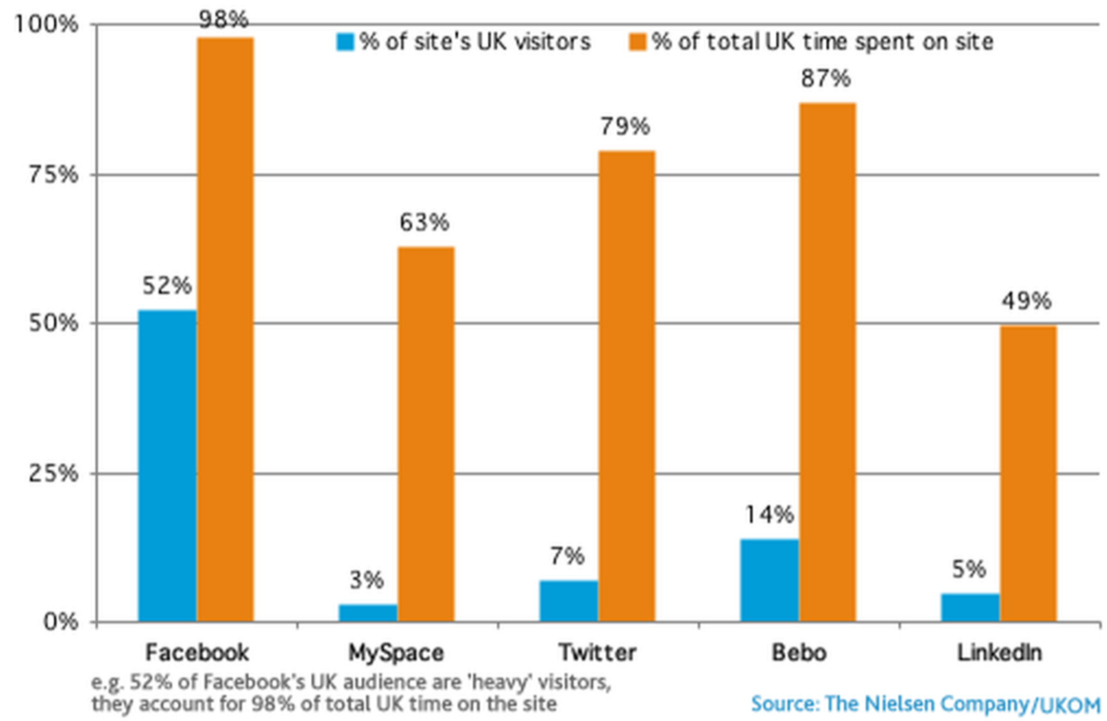


Figure 1: **A Normal Distribution (Black) Overlaying a Paretian Distribution (Grey).**

To use a very common sport, soccer, to illustrate, Ronaldo and Messi have won 9 of the last 16 FIFA World Football Player of the Year Award. Even if we consider the other 7 players who won when Ronaldo or Messi didn't win, what percentage of the total number of players in Europe are they? It is a vicious statistic. Another example: All the Grammy Award or Oscar Award winners are an absurdly tiny percentage of all musicians or actors who have ever recorded an album or acted in a movie. Engaging in an iterative trading activity, which is what a market-based economy is, often results in the average person making out with little income and literally no wealth while a few people end up with the lion's share of income and wealth.

Two out of two hundred countries, namely the US and China, produce 40% of global GDP. Following is a chart that perfectly illustrates how deadly the Pareto distribution is. We can all agree that social networks are incredible creative domains who compete for our need to communicate for social (Twitter) or professional (e.g. LinkedIn) purposes or both (e.g. Facebook). The chart below shows the various extremities of winner-take-all in highly creative industries. In a study of the use of social networks in the UK in 2010, the Nielsen Company found that only 7% of Twitter users drive 79% of the overall time spent on the app by all users (think Donald Trump). These are heavy users! Five percent of LinkedIn users spend 49% of the time spent by all its users. Look at MySpace; 3% of users spent 63% of all the time spent on the app.

Figure 3: Heavy Social Network Visitor Activity in the UK, January 2010



There is nothing normal about this distribution of numbers. Income and wealth follow similar patterns of distribution.

You have no doubt heard of how wealthy the top 1% (and the top 1% of the top 1%) are relative to all of us. If you thought the distribution pattern in social networks is devastating, the distribution of wealth on the stock market is nothing short of dispiriting. In a paper titled, "Do Stocks Outperform Treasury Bills?", Professor Hendrik Bessimbinder of the University of Arizona examines whether the stock is the wealth creating machine it is often known to be. In studying where most of the returns registered by the US stock markets between 1926 and 2015 originated, he found that only 4% of companies listed in the US generated the majority of wealth created in that period. In other words, in terms of lifetime dollar wealth creation, 1,040 out of 26,000 drove all the returns in the US over a 90-year period. By lifetime dollar wealth creation, we mean from the time a company is listed to when it ceases to exist either because of bankruptcy, merger, acquisitions, management or private equity buy-out, and so on. So, in the long term, unless you were invested in those 1,040 companies, you either lost money or made as little as the one month return on Treasury bills. The top 1% would have made their money from holding and riding out one or more (e.g. The Walton Family of the Walmart fame) of the 1,040 companies. Warren Buffett held more than one of these. The other side of this coin is that the average investor has lost money trying to build wealth by picking and choosing stocks to own on the stock market. Building wealth in competitive and creative domains is an absurdly low probability game!

This feature of creative productive systems is obviously problematic, and no one really knows what to do about it. It is such a powerful phenomenon that you ought to be incredibly and carefully thoughtful if you want to reallocate productive outcomes to normal distributions. To blame it on the oppressive nature of the system, as we have mostly done in South Africa, is to radically underestimate the complexity of the problem. No wonder Karl Marx thought the contradictions in a market-based economy (created by the Pareto Principle) would naturally lead to socialism. Wealth distribution is a conundrum that was aptly explained by Robin Marris, Prof. of Economics at Birkbeck, University of London, "People on the whole have normally distributed attributes, talents, and motivations, yet we finish up with wealth distributions that are much more unequal than that". Some countries tire of figuring out the problem and opt out of creative production (e.g. Zimbabwe, Venezuela). In so doing, they invited other problems.

In the context of the failure of South Africa to manufacture good news, despite an array of economic policies, it would not be out of place to hear calls for the country to throw the towel on what remains of our market- based system.

The Pareto Principle is what Nelson Mandela's Government, and subsequent administrations have been trying to solve through state ownership and operation of SOEs. Truly, a Black person is as equally talented as anybody so she should have access to the opportunity to run South African Airways, Eskom, Transnet, PRASA and so on. As true as that is, nothing says any one of those institutions, whose underlying fundamental measure of success is human productivity, should be successful. In fact, the Pareto Principle says profits in the global aviation industry could very easily be distributed away from SAA as they have! The Pareto Principle says profits in the energy industry could most likely be distributed away from Eskom, PRASA, and Denel to other players in the value chain.

The Government may want to give nurses, doctors, and teachers equal access to professional opportunity because talent, passion, intelligence, trust, transparency, desire, imagination, openness, energy and so on may be normally distributed. That's fair and square. But a word of caution from the Pareto Principle – good intentions are not outcomes. The profit motive, based on human productivity, will distribute outcomes in health care and education away from Government schools and hospitals to their peers in the private sector. So, the burning question to the Government of South Africa is, if you understand this, why not focus your entire efforts – through creative legislation - on inputs to human nature that are normally distributed in order to widen the starting line in life?

This conversation would be inadequate if we didn't show that we understand the political left better than it understands itself. The political left exists for the very reason of this paper – the unequal distribution of income and wealth that naturally arises out of iterative competitive duels that each of us wakes up in the morning to engage in throughout the day. By doing your job well, by working longer hours, not leaving problems unsolved, and so on, each of us who succeeds, and garners an increasingly larger share of the resources available for reward causes inequality. The left thinks that inequality is the problem and gets into the Government's head to conjure up all sort of schemes solve it. One of those schemes is an ever-increasing tax rate that subsidizes those left behind by the Paretian distribution. Yet, with an incredibly high tax rate, South Africa is as poor today as it was at the dawn of our young democracy! What could be causing the problem to persist?

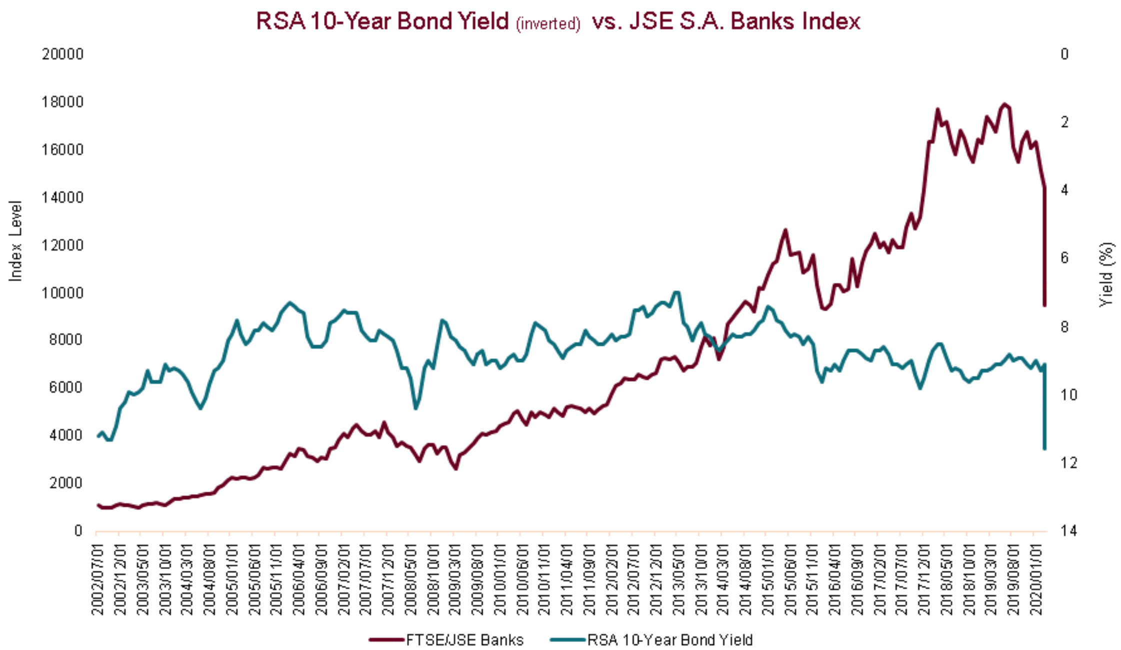
South Africa's woes are in social mobility, and the Government is at the centre of this problem. Social mobility is a term used to describe the ability to move up and down the economic ladder across generations regardless of biases known to man (race, gender, religion, and so on). To be sure, the left always used Nordic countries (Norway, Finland, Sweden, Iceland, Denmark) to justify ever rising tax rates and social spend. South Africa gives the Nordic a run for their money in social spend. And compared to Nordic countries, it spends the least on both safety, security and defence. So, here the left is getting what it wants. Yet Nordic countries lead the world in social mobility while South Africa ranks 77th out of 82 countries in the World Economic Forum's annual Global Social Mobility Index. What this means is that if you are poor in South Africa, the chances of you climbing up the economic ladder by converting access to opportunity into wealth over your lifetime and your child's lifetime are extremely low. On the other hand, if you are on the other side of the Pareto distribution (rich, that is), there is way more than a good chance that your children will stay rich relative to their fellow citizens. The starting point is everything in countries like South Africa whereas Nordic countries who rank in the top 5 in social mobility have pretty much erased the starting line. The big lesson here is that the only thing worse than inequality in one generation is the inability for the rich and poor to swap places as generations turn. No one wants to play a competitive game if it is rigged. Why give my all if I already know the result. I would rather engage in corruption as a means of flipping over the board game in the hope that when it lands, I am at the top. This is where we are.

How is the Government at the centre of this economic vortex? Time and time again, industry after industry, the Government has applied brakes to efforts by its own citizens to move up the economic ladder. Having inherited South African Airways, the Government is overcome by envy (a trait the Bible dedicates two of the ten commandments to) to start a budget airline (Mango) to compete with the private sector that had in fact spotted a market segment SAA wasn't catering to. You could fill the Kalahari Desert with dead bodies from budget airlines that went bankrupt due to Government interference (the last notable one being 1Time). Does the Government and the political left think that the owners, employees, and perhaps suppliers to all the defunct budget airlines moved up the economic ladder? Now go industry by industry and you'll see what havoc SOEs wreak throughout the economy. As good citizens, we have all gradually ceded control, bit by bit over 26 years to the Government's efforts to redistribute outcomes from the citizen to the State, and we are enduring economic tyranny.

Laden with ideology and devoid of pragmatism, the Government must be stunned that increased state intervention in the past two and half decades has resulted in a Pareto distribution worse than what the private sector typically produces. Who would have thought that with the Government pervasive in most of the lives of the South African citizen, we would have the second highest Gini coefficient (income inequality) in the world? Today, the State has created severe systemic risks in a range of industries including education, healthcare, mass transit, water and sanitation, banking and energy. Public finances have hit an immovable wall. Tax rates have hit an immovable ceiling. Interest expenditure from Government borrowings has hit a shatter proof glass roof. The Government now relies heavily on contributions from wealthy individuals and companies to fund efforts to combat the COVID 19 pandemic. Who would fund repairs to the water and sanitation infrastructure if the bottom fell out there? Talking of water, South Africa's geographical position makes it prone to droughts. Where is the budget appropriation for a desalination plant going to come from should coastal cities like Cape Town, East London, and Port Elizabeth suffer another drought?

As a consequence, to underestimating its real purpose, to reduce systemic risk though policy and regulation, and overestimating its ability to own and operate SOEs, all three major credit rating agencies have expelled South Africa from the family of highly credit worthy nations. Sovereign credit ratings implicate the banking industry because banks do not have to allocate a risk rating to the capital they invest in Government bonds (zero-risk weighting in their capital structure). The downside is that this contaminates credit ratings of banks if the sovereign credit rating falls. Because of this, market returns of banking shares are highly correlated with Government bond yields over time.

Figure 2: JSE S.A. Banking Index vs. 10Yr. RSA Government Bond Yield (inverted)



Source: Reuters, First Avenue

By suffering successive sovereign downgrades, the Government is progressively destroying the integrity of the banking system. Clearly, all attempts by the Government to raise economic growth have dismally failed to inspire confidence in credit rating agencies as well as domestic businesses and multi-nationals. It is likely that the banking industry will now face the twin evils of slow revenue growth and rising bad debts. Has the Government ever thought about what it would do if any one of the major banks goes the way of the flesh with Government deposits, private and corporate savings, counter-party liabilities to other local banks, and not to mention jobs in both the sector and downstream?

The intent to use SOEs to shovel money from the wealthy few to the (poor) masses has ironically made some of the politicians and bureaucrats involved in this benevolent activity very wealthy. Wealthy enough to be confused about either the outcome they're getting from something as uncreative as towing the party line in Parliament or the methods their party has employed over the years. In effect, this personalised policy making has resulted in vested interests that so far have proved impossible to resolve through conscientious actions or party-political processes (the governing party does have an Ethics Committee). That this impasse has lasted this long is symptomatic of the weakness of the criminal justice system to prosecute those who have pathologised public policy. Unable to resolve their own internal conflicts, some politicians are doubling down on sending the country further down the road to perdition – the nationalisation of the Reserve Bank. The intent is simple - to compel the Bank to print more money. The idea even simpler - to access more money, no matter how debased, to take further aim at the Pareto distribution.

Here is the real rub:

There is a reason why policies and Governments fail. Running a country competently is very difficult because of the very low probability of (i) conceptualizing great policies, (ii) orienting your actions to the concepts, and (iii) implementing policies conscientiously (as they say in boxing when you fight a good fight, "letting your hands go"). There is a reason why businesses and their managers fail. Running a company competently is very difficult because of the low probability of (i) conceptualizing great ideas, (ii) orienting your strategies to those ideas, and (iii) implementing those strategies conscientiously. Legislative and business creativity have an absurdly low probability of success. The Governments of South Africa took on both low probability events at the same time – passing laws in Parliament while owning and operating businesses (SOEs). Not maximizing its chance of succeeding at one, the Government failed miserably at both. Examples are too many to enumerate.

However, Moody's downgrade statement makes mention of the Government owned energy provider, Eskom. Even leading up to the first wave of load-shedding in 2008, Eskom's systemic risk had already been communicated to the Government. Twelve years after 2008, the slow pace of reform to introduce competition and better regulate pricing have left the country unable to support anaemic economic growth and vice versa. The litany of errors between Government policy and SOE operations all along the length and width of the economy have led to the grave situation we are in. The sheer breadth of systemic risk in the country will take your breath away, literally!

It is no longer political heresy or blasphemy to say that wherever the Government has gone in the past to seek political consensus, cover, and electoral wisdom ultimately purged the last ounce of confidence of those who lend to the Government - the bond market. This is how systemic risk works. The average person was roused from her sleep on Tuesday 24th March to go about her daily chores. She had not the slightest inkling of the danger that could have easily upended her life beyond recognition. The Government was struggling to issue a R4.5bn ten-year bond (R2030). Nobody wanted to lend the Government money anymore! How was the Government going to pay salaries, social grants, and so on? What would Government guarantees made to banks for lending to SOEs mean? What would banks do with worthless guarantees? Since 2009, the political industrial cluster feathered itself in Government operations, raising Government debt from 29% of GDP to 61% in 2020. If you include Government guarantees on further debts taken by SOEs to feed the political industrial cluster, govt debt to GDP is 72%. The implications of this would domino and reverberate through the economy like a gun shot in the night.

The yields (interest rate lenders charge the Government) on that bond shot up from 9% to 13.22%! At that rate, servicing debt costs would increase by well over 25% and push the Government toward default (as it clearly cannot cut expenditure elsewhere). The Reserve Bank, which has over the years been steadfast in warning that the impact of fiscal policy dwarfs that of monetary policy, was forced to step in to facilitate liquidity to the Government. It announced that it will be participating in the (secondary) bond market as a purchaser of Government bonds. This calmed the markets and strengthened bond yields down to 11.45%, much better than 13.22% but still a lot worse than 9%. Since then, the Reserve Bank's balance sheet has grown to over R9bn on account of buying Government bonds. If Government finances do not improve, the Reserve Bank will have to take a loss on the bonds when it sells them.

This rebuke surely has put paid to the Government's understanding of its role. The ignominy must be hard to live with. Like the US, South Africa is addicted to debt. Only, it does not have a robust tax base and a growing economy, let alone the world's reserve currency, to handle its obligations.

Out of money, the Government is also out of time.

South Africa does not lack the political will to implement structural reforms to the economy. It lacks the prosecutorial ability to criminally punish the political-industrial cohort that has pathologised public policy. Without this deterrent, personalised public policy will continue to run amok! It is also this cohort that is objecting to the next best solution to the country's problems, an IMF intervention. We have witnessed the visible hand of the political industrial cluster pushing the Government over the cliff. Now we need to witness a surgical operation intended to raise the country from a heap of ashes. A financial reset. A policy reset that is more respectful of phenomena that create and destroy wealth.

Certain of the political posturing that is sure to follow (leftist political parties outright oppose the Treasury approaching the IMF for funding and the Minister of Finance wants to limit the approach to IMF for assistance related to fighting the health scourge), bond vigilantes will light a fire under the Government's heavy feet every Tuesday and Friday, the days when the Government auctions its bonds. While the Reserve Bank had no option but to come to the aid of Treasury in the bond market, it will be keen to exercise its independence by not regularising unsustainable behaviour. It will be keen not to compound the problem by printing more money to support ruinous fiscal policy into perpetuity. The last thing South Africa needs, on top of all its woes, is inflation.

South Africa's salvation is in a creative legislature and a creative private sector.

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Lead Author: Hlelo Giyose, Chief Investment Officer

First Avenue Investment Management (Pty) Limited *which is approved as an Authorised Financial Service Provider in terms of the Financial Advisory and Intermediary Services Act, 2002. (FSP 42693)*

Registration Number 2008/027511/07

Registered Offices
Address: 21 Fricker Road, Illovo, 2196
Telephone: (+27-11) 772-2480