

Spotlight on South Africa Conference Brief

By Richard Downie and Kaley Fulton

Introducing Spotlight on Africa

On September 28, the CSIS Africa Program hosted the inaugural event of *Spotlight on Africa*, a conference series profiling political and economic trends in some of the continent's largest and most dynamic economies. The series began by looking at South Africa; a key regional power, an important partner of the United States, and a country facing considerable political and economic turbulence. CSIS gave a platform to a diverse set of South African business leaders, academics, political analysts, and journalists. The event began with an address by the U.S. Ambassador to South Africa, Patrick Gaspard. (See annex for the full conference agenda). This report outlines some of the main themes to emerge from the discussions. It does not capture every opinion expressed but presents some of the main points of interest, convergence, and disagreement. The report ends by laying out some potential scenarios for South Africa watchers and U.S. investors to consider as the country proceeds along an uncertain path. The full conference can be viewed [here](#).

South Africa remains important

Recent political, economic, and social strife has prompted gloomy predictions about South Africa's trajectory yet there are good reasons to remain positive about the country's long term prospects. That was the message from the Ambassador Gaspard, who reminded the audience: "There's nothing wrong with South Africa that can't be repaired by all that's right in South Africa." Not only is South Africa responsible for approximately one-quarter of Africa's overall GDP, it is a magnet for Foreign Direct Investment (FDI), and a business gateway to the rest of the continent. Furthermore, South Africa's unique history and success in overcoming apartheid show that democratic consolidation, equality, and social justice are attainable objectives even in the most testing circumstances. South Africa's thriving civil society, vibrant media, and strong constitutional protections have given it a resilience that most other African nations do not enjoy.

However, the near-term challenges are cause for anxiety. On the political front, the August 2016 municipal elections confirmed voter disillusion with the ruling African National Congress (ANC). Intra-party tensions, political interference with state institutions, and chronic corruption suggest the ANC is deviating from the path of reform. Economic malaise and stagnant job growth, unless addressed, could cause the social contract to unravel.

At the heart of these challenges is the reality that South Africa's goal of transformation—economic, social, and racial—remains elusive. Indeed, it is the country's

“foundational challenge,” according to Ambassador Gaspard. Political transformation may have occurred in 1994 but economic transformation has yet to arrive, despite government programs like Broad-Based Black Economic Empowerment (BBBEE). The share of black CEOs in South Africa’s top companies has fallen from 15 percent to 10 percent. Youth in particular are being cut adrift from economic opportunities. Of the country’s 10.2 million youngsters aged 15-24, one-third are no longer in school, do not have a job, and have never received vocational training. The *Fees Must Fall* protests on university campuses are the most significant—and dangerous—manifestation of the mismatch between young peoples’ aspirations and the inability of the government to meet them.

Economic clouds

Paolo Mauro, the International Monetary Fund’s newly-appointed mission chief for South Africa, reminded the audience that South Africa’s long-term economic outlook is positive. South Africa has the most diverse economy in Africa and has the second largest GDP in the continent after Nigeria. However, South Africa recorded growth of only 1 percent last year and the near-term picture is decidedly uncertain.

Some of these economic headwinds are beyond South Africa’s ability to control. The decline in global commodity prices has dealt a serious blow to an economy that derives 75 percent of its export revenue from raw commodities. Of the main three minerals produced in South Africa, world prices have declined 76 percent for iron ore, 39 percent for gold, and 52 percent for platinum since the end of the commodity boom in 2011. In addition, South Africa has been hit by the most severe regional drought in living memory, leading to lower agricultural output and a rise in the cost of foodstuffs. Furthermore, FDI into South Africa has dropped to its lowest level for a decade, particularly as its largest trading partner, China, experiences its own economic slowdown.

These external pressures have combined with internal weaknesses to amplify the economic blow. Structural impediments have undermined South Africa’s economic performance and weakened its attractiveness as an investment destination. They include chronic social inequalities, rigid labor controls, poor industrial relations, problems with power production, failure to reform product and service markets and—most of all—policy uncertainty by the government. The power struggle between President Jacob Zuma and his Minister of Finance, Pravin Gordhan, creates an atmosphere of unpredictability. Furthermore, rule of law and property rights are coming under legislative strain. Peter Leon, Partner with Herbert Smith Freehills South Africa, LLP, offered some examples of current and potential laws that dampen the climate for foreign investment and perhaps explain why South Africa is only ranked 66 out of 109 global mineral producers in terms of its business attractiveness, according to research by Canada’s Fraser Institute. They include the Private Security Industry Regulation Amendment Bill, that indigenizes the private security sector; a Mineral Petroleum Resources Development Amendment Bill that would grant excessive powers to the Minister of Mineral Resources; and a Protection of Investment Bill that potentially domesticates investment protection.

This legislative activity, according to Hilary Joffe, editor at large of Business Day newspaper, is symptomatic of overregulation by a state that should be doing more to improve the enabling environment for the private sector. On top of this—as Ralph Mathekga, founding partner of Clear Content argued—is the specter of fiscal populism by an ANC that is desperate to shore up its political base. According to the panelists, these weaknesses make it virtually inevitable that ratings agencies will downgrade South Africa’s creditworthiness to junk status.

Some efforts are under way to stimulate the economy and lure investors back to South Africa. Hilary Joffe referenced the Small and Medium Scale Enterprise Fund as a positive step. Ambassador Gaspard cited President Zuma’s announcement of an employment scheme to train one million young people as a potentially valuable initiative, but warned that more effort is needed to align youth training programs with the skills demanded by employers.

Phuti Mahanyele, executive chairperson of Sigma Capital and a former *Forbes Woman Africa Business Woman of the Year*, acknowledged South Africa’s structural economic challenges but sounded an upbeat note, declaring that “We are moving forward.” She cited a McKinsey report highlighting five big areas of opportunity for growth: advanced manufacturing, infrastructure projects involving public and private partnerships; natural gas; service exports into the rest of Africa; and agricultural processing.

Political bumps on the road

South Africa’s current political upheavals stem from the fact that the ANC can no longer count on the “inherited legitimacy” it has hitherto enjoyed as the party of liberation, argued Mr. Mathekga. For the generation of South Africans born after 1994, the ANC’s epic history is less relevant than its current, poor, performance in office. The list of complaints includes cronyism, corruption, mismanagement of State-owned Enterprises (SOEs), the running down of national infrastructure, poor service delivery, and the erosion of state institutions. Ambassador Gaspard cited the “bizarre” criminal investigation into Minister Gordhan as only the latest example of political interference in supposedly independent institutions like the National Prosecuting Authority.

More broadly, the tectonic shifts that are in the process of remolding South Africa’s political landscape reflect the fact that while the 1994 transition may have transformed *who* governed the country it did not transform *how* the country was governed. Professor Steven Friedman of the University Johannesburg noted that a white elite was replaced by a multiracial elite which similarly failed to keep pace with the demands of its citizens for jobs, public services, and an end to social and economic inequities. The emergence of parties like the Economic Freedom Fighters (EFF) combined with the uptick in social protests that have increasingly turned violent and have made some of South Africa’s leading universities ungovernable, pose a direct challenge to an elite that is perceived to have failed to deliver on its promise of genuine transformation.

While the external challenges pile up, the ANC has been consumed by internal battles. Decision-making authority has eroded within the ANC as fissures open up, patronage networks

have taken hold, and serious policy differences—always a feature of the tripartite alliance—have become insurmountable. The party has turned inward and the question of President Zuma’s succession will dominate the near-term and distract the ANC from the task of governance.

The 2016 municipal elections confirmed the ANC’s waning popularity and saw it lose control of the major metropolitan areas of Tshwane (Pretoria), Johannesburg, and Nelson Mandela Bay. However, speakers offered different interpretations of what the result said about the profile of the ANC and the prospects for the opposition parties. While Mr. Mathekga observed that the ANC was becoming a predominantly rural party, Professor Friedman said that the ANC had lost a greater share of the vote in the countryside than in urban areas. Despite the ANC receiving its lowest share of the vote since taking power—53.9 percent—there was general agreement that the result was not, in the words of Jeffrey Herbst, president and CEO of the Newseum, a “decision-forcing moment” for the ANC. Dr. Herbst argued that President Zuma would likely see off any attempts to recall him before the party chooses its next leader in December 2017.

Observers of South Africa often lament the instability that characterizes present-day politics, but this volatile phase should not necessarily be portrayed in negative terms, according to Mr. Mathekga. He pointed out that people who yearn for the predictability of the recent past should remember that this was a period characterized by overwhelming ANC dominance and lack of competitiveness.

Furthermore, South Africa can draw on reserves of strength that better prepare it to weather political turbulence. The judiciary has been “messianic,” in the words of Peter Leon, in delivering independent judgements and standing up for institutions under threat, such as the Parliament and the Office of the Public Protector. He referenced the Constitutional Court ruling that President Zuma comply with the Public Protector’s order to pay back state funds used to improve his private homestead; and its striking down of the Restitution of Land Rights Amendment Bill.

Looking ahead

South Africa watchers should expect economic, political, and social volatility in the near-term. On the political front, the speakers concurred that the ANC would most likely retain power in the national elections of 2019 but that does not mean to say the path to victory will be easy. Much will depend upon who is chosen to lead the party into the next election. Two wings of the ANC appear to be jockeying for supremacy and each have their preferred candidates. A group loyal to President Zuma seeks to protect the prevailing patronage system and appears to favor the president’s former wife, Nkosasana Dlamini-Zuma. A pro-business, pro-market group champions the ever-cautious deputy president, Cyril Ramaphosa, who is well-regarded outside South Africa but—according to Dr. Herbst—garners less enthusiasm at home. However, there is plenty of time for other figures to emerge, or for the two factions to forge a compromise and agree on a unity candidate, such as ANC treasurer general, Zweli Mkhize.

As for the prospects of the leading opposition parties—the Democratic Alliance and the EFF—much will depend on the ability of these ideologically implausible bedfellows to work together. Professor Friedman observed that they have already demonstrated their ability to make life difficult for the ANC when they act in unison. In Johannesburg, their common stance against the ANC during the negotiations that followed the inconclusive outcome of municipal elections in the city propelled them to office at the head of a minority administration.

While the political forecast in the run-up to 2019 points toward considerable volatility, speakers warned against over-dramatizing the situation and rejected the suggestion that South Africa would descend into the kind of political dislocation and violence seen in neighboring Zimbabwe.

The economic outlook in the short-term will be closely linked to the political situation, in particular as the power struggle between President Zuma and Pravin Gordhan resolved itself and the charges against Gordhan were dropped; as well as the “political noise” that unsettles investors and suggests that long-promised structural reforms to the economy will be further postponed. GDP growth of 3.3 percent in the second quarter of 2016 points to better times ahead but a ratings downgrade could offset those gains.

Advancing U.S. interests

The United States has a multifaceted relationship with South Africa that includes—but is not confined to—the areas of diplomacy, business, cooperation on HIV/AIDS prevention and treatment; energy cooperation; law enforcement training; climate adaptation; and countering wildlife trafficking. While the bilateral relationship is sometimes tricky and historical suspicions can bleed into present day distrust, survey data from the Pew Research Center suggests that 72 percent of South Africans have a positive view of the United States.

The United States and South Africa enjoy a balanced and varied trade partnership worth \$21 billion a year. The African Growth and Opportunity Act (AGOA), renewed in 2015, remains the centerpiece of the bilateral trade relationship, enabling duty free access to the U.S. for South African agricultural products, automobiles, and wines, among other product lines. Ambassador Gaspard noted that U.S. companies like General Electric and Ford Motor Company have made a long-term bet on South Africa. He added that their investments in local training and skills development are valued by South African workers and strike a notable contrast with China’s engagement model.

U.S. policy objectives in South Africa are to advance inclusive growth and prosperity. Ambassador Gaspard emphasized the role of the private sector in achieving these goals but added that more could be done to foster a friendlier environment for U.S. investors. To illustrate the point, Ambassador Gaspard noted that new regulations have slowed down approval times for U.S. firms trying to move electrical goods into South Africa from 30 days to 500 days.

While an all-encompassing economic partnership agreement would help iron out these kinds of difficulties, Ambassador Gaspard conceded that such a deal was not a realistic prospect in the near term. As an alternative strategy, Ambassador Gaspard outlined a step-by-step

approach that would negotiate a series of smaller cooperation agreements governing intellectual property rights, labor rights, trade facilitation, bilateral investment, and trade in services.

While the U.S. government can play a role in advancing opportunities in South Africa, ultimately it is up to U.S. companies to take the plunge. Ambassador Gaspard noted that American firms already operating in South Africa are much more bullish about the environment they encounter than those that stand on the sidelines. He urged U.S. companies to focus on the broader landscape of opportunities rather than dwelling on government pronouncements or legislative developments that seem unfriendly to business. Ambassador Gaspard emphasized the collective power of the U.S. private sector to help craft a more enabling environment for business in South Africa, citing as an example the launch of an entrepreneur fund by the American Chamber of Commerce to invest in young South African businesses. The renewable energy sector is another area where collective advocacy for regulatory reform by U.S. business could open up opportunities for investment. Finally, South Africa's ongoing review of Intellectual Property Rights, including its patent system, provides an opportunity for U.S. companies—particularly in the pharmaceutical industry—to voice their support for sensible guidelines that will boost rather than stymie investment.

Spotlight on South Africa – Conference Agenda

Wednesday, September 28, 2016

2nd Floor Conference Center
Center for Strategic and International Studies
1616 Rhode Island Ave NW, Washington, D.C. 20036

Opening Keynote

- Ambassador Patrick Gaspard, U.S. Ambassador to South Africa

Panel I: South Africa's Shifting Political Landscape

- Jeffrey Herbst, President and CEO, Newseum
- Steven Friedman, Director, Centre for the Study of Democracy, University of Johannesburg
- Ralph Mathekga, Founding Partner, Clear Content
- *Moderator:* Jennifer Cooke, Director, CSIS Africa Program

Panel II: Outlook for Economic Growth and Investment

- Hilary Joffe, Editor at Large, Business Day
- Peter Leon, Partner, Herbert Smith Freehills South Africa LLP
- Phuti Mahanyele, Executive Chairperson, Sigma Capital
- Paolo Mauro, Mission Chief for South Africa, International Monetary Fund (IMF)
- *Moderator:* Simon Barber, Principal, Izwi Communications LLC