The Impact of Covid-19 on the Level of Productivity and Industrial Development in South Africa

by Thakaramahlaha Lehohla and Pule Kholopane

South Africa has identified the manufacturing sector as a key driver of the economy via the re-industrialisation drive, with incentive programmes such as the Manufacturing Competitive Enhancement Programme (MCEP), Cluster Development Programme (CDP), 12I Tax Allowance Incentive, and Special Economic Zones (SEZs). These include the development of black industrialists, with the purpose of growing the economy via manufacturing, growth in exports, revitalisation of industrial parks, and broad-based black economic empowerment (B-BBEE). Black industrialists must be directly involved in the strategic and operational leadership of the operation, and have the requisite expertise. They should take personal risk in the business, and be locked in for a reasonable time frame to the entity.

The Department of Trade and Industry (DTI) policy requires black industrialists to have a high level of ownership (>50%), and/or exercise control over the business. The DTI describes black industrialists as ‘black South Africans who own and, through significant shareholding, control an enterprise whose products are significantly used and have a considerable impact on decent employment and create broad-based economic opportunities’ (DTI, 2020).

The DTI has various incentive schemes for individuals who are planning to start their own businesses, as well as for those who have existing businesses. The Department seeks to broaden participation in entrepreneurial activity to all, with an emphasis on youth development, women, and B-BBEE, and developed the Industrial Policy Action Plan (IPAP) as a blueprint to realise this vision. In the midst of this plan, the country faces economic challenges, losing some of the advances made prior to the onset of the Covid-19 pandemic.

Covid-19 has caught the South African economy and industries off guard, as emergency approaches have had to be applied towards mitigating its spread. The greater focus has been on containing the virus by closing internal and external economic activities, with the exception of essential services. This comes as a double blow to an economy already bleeding from the consequences of state capture (poor management of state-owned entities, and corruption), a distressed steel sector, and the generally poor performance of its key sectors, such as the manufacturing industry. As a result, credit rating agencies have downgraded South Africa, reducing investor confidence and the possibility of positive growth. It is projected that manufacturing in South Africa will regress to 42.60 points by the end of this quarter, according to Trading Economics global macro models and analysts' expectations.

Further projections estimate that the Purchasing Managers' Index (PMI) (an indicator used to measure the level of productivity in industry) in South Africa will stand at 47.00 in 12 months' time. In the long term, South Africa's manufacturing PMI is projected to trend around 49.00 points in 2021 and 51.00 points in 2022, according to our econometric models (South African Manufacturing PMI – 1994–2019 Data). This raises an alarming question regarding what went wrong in terms of industrial development, as manufacturing's contribution to GDP was at 24% in the early 1980s, and regressed to less than 13% in 2017.

As seen in Figure 1, South Africa's GDP staggered between a 0% – 1.6% growth rate between 2017 and early 2019, then grew by 0.9% from mid-2019, followed by a 0.1% growth rate, then a drastic drop in January 2020 to a negative growth of 0.5% GDP.

This trend of minimal and negative growth in GDP can be attributed to Moody and Fitch's global credit rating downgrade of South Africa, due to poor governance and corruption precipitated in South Africa's state-owned entities (SOEs), resulting in load shedding (electricity), an increased unemployment rate (at 29%), negative growth in the financial year, expenditure of GDP at 62.5%, and a myriad of other economic deficiencies. The worst-case scenario is a further 5–7% contraction in economic growth, resulting from the Covid-19 pandemic.

Manufacturing

Over the past two decades, South Africa's manufacturing sector has been experiencing a

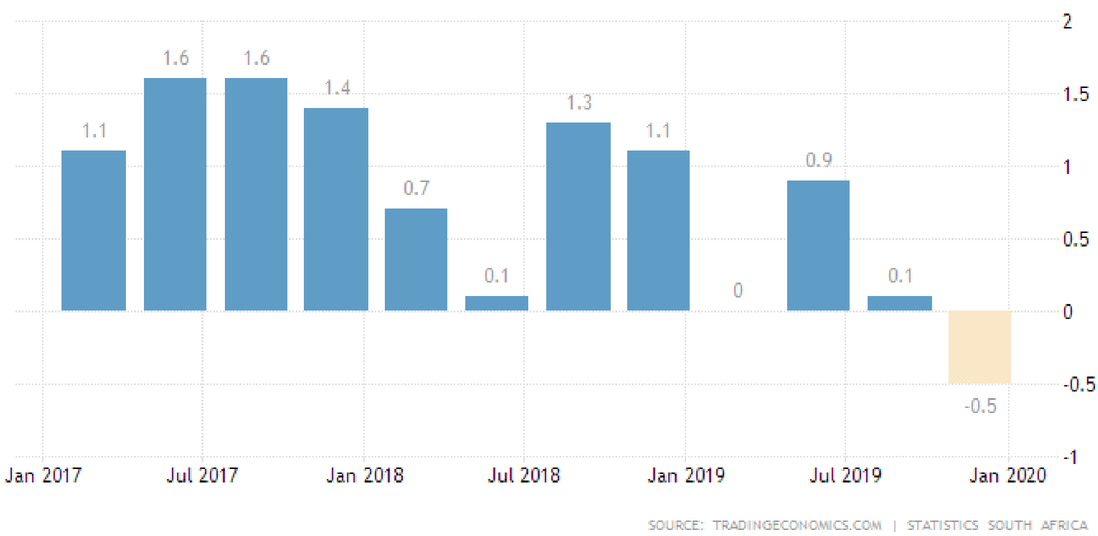

Figure 1: South Africa GDP Annual Growth Rate – 1994–2019 Data | 2020–2022 Forecast | (**Source:** Adapted from Trading Economics, 2020a).

significant revolution, including thorough shifts in management strategies, goods and process technologies, consumer expectations and supplier outlook, as well as competitive behaviour. Manufacturing and tourism are rated as the main job providers, followed by the mining industry. A collapse of these industries will deliver a significant blow to the South African economy.

According to the Manufacturing Circle (2020), South Africa requires a strong manufacturing sector in order to sustain the more than 1.6 million people it currently employs. It should also provide a platform for load and scale for key national infrastructure such as electricity, rail and municipal services. The manufacturing sector is among the top three multiplier sectors in terms of value addition, job creation, export earnings and revenue generation, as well as a driver of tertiary education and the absorption of people into the workforce.

Despite these great expectations for the manufacturing industry as a driver of productivity in the South African economy, the contrary is revealed in recent statistics. Since 2008, almost 400,000 South African manufacturing jobs have been lost, and manufacturing has declined from contributing more than 15% of GDP to just under 13% of GDP in 2016 (Manufacturing Circle, 2020). Key factors contributing to this decline include domestic electricity supply constraints, rapid increases in administered prices, labour instability, and competition from unfairly incentivised imported products.

Projected Impact During and Post-Covid-19

As a result of South Africa's nationwide lockdown in response to Covid-19, most manufacturing companies have closed, delivering a serious blow to the supply chain. Most stores and essential services have closed, and major projects intended to boost infrastructure and industrial development have been impacted. The DTI incentive programmes, such as the Critical Infrastructure Programme, as well as the 12I Tax Allowance Incentive – which focus on brownfield and greenfield projects at SEZs, attracting foreign and domestic direct investment, are non-operational as a result of the lockdown.

The author is involved in the incentivisation of industrial development projects, and can attest to the adverse impact on industrial development in terms of efficiency in the processing of applications and claims meant to finance industrial development projects. This particular value chain has become significantly inefficient, from the processing of claims, quality control, authorisation, and finally paying the claim. While a necessary precautionary measure to avoid the spread of a deadly virus, South Africa's lockdown will – in the long term – adversely impact industrialists and the economy.

A case in point is the Cluster Development in the

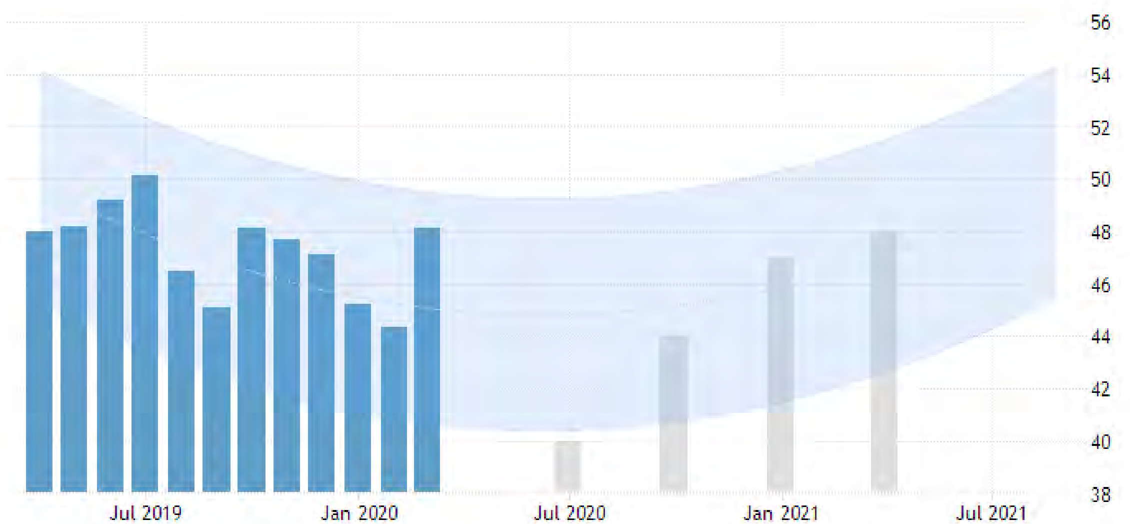

Figure 2: South Africa Manufacturing PMI – 1994–2019 Data|2020–2022 Forecast| (Source: Adapted from Trading Economics, 2020b).

DTI, where claims to the value of R10 million – which could have been processed and paid within three to four working days – may now be delayed until the end of the lockdown. This scourge could lead to the possible closure of the Cluster Development in the DTI, and the loss of many jobs. Additionally, on the industrialist side, the supply value chain is impacted adversely since there will be operational disturbances, and this will impact some industries' local and international markets.

Covid-19 has led to grim forecasts for the South African economy, from both a micro- and macro-economic perspective, with estimations that 75% of SMMEs will close down, and an additional 400,000 jobs could be lost. An additional provision of R150 billion is being sourced for economic sustenance, and there are currently conflicting views regarding sourcing a loan from the International Monetary Fund (IMF) to service the economy post-Covid-19. A 5-7% contraction is projected, and the economy is at negative growth as a result of Moody's downgrade (Boonzaier, 2020; De Lange, 2020).

According to Trading Economics (2020b), it is projected that the present lockdown will result in a further regression of the PMI – which has been on a downward slope for the past eight months.

Figure 2 explains the actual PMI manufacturing trend covering 2019 to early 2020, and provides projections for mid-2020, into 2021. It can be seen that the PMI rose by 48.1 in March 2020, whereas previously it was at 44.3. Prior to March 2020, there had been a downward slope since October 2019 as a result of contraction in industrial activity, which was due to slower delivery times. These delays are an indication that suppliers are busier under normal circumstances. This illustrates the clear adverse impact of the Covid-19 pandemic on global supply chains (Trading Economics, 2020b).

It is further projected that the Manufacturing PMI in South Africa will regress to 40.00 points by July 2020, as a result of credit rating downgrades and the slowing down of the production process due to Covid-19. Further projections estimate that Manufacturing PMI in South Africa will take an upswing to 47.00 points in January 2021 – which is a sign of recovery. As for the long term, the South African Manufacturing PMI is projected to trend around 49.00 points in 2021 and 51.00 points in 2022 (Trading Economics, 2020b).

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Recommended Solutions for Productivity Post-Covid-19

For a productive post-Covid-19 economy, Viegi (2020) suggests that expansion and diversification will be the key drivers of long-term growth. By engaging in an export strategy, exporting national firms can capitalise on becoming more productive, competitive and innovative. This is in line with the National Integrated Export Strategy, which aims to increase national export from the current 0.02% to 2% in 2030 (DTI, 2017).

On the industrial financing side, the DTI and Development Finance Institutions (DFIs) provide industrial development incentives in support of the country's IPAP. The industrial development incentive programmes are inclusive in the Master Plan, with the aim of supporting and developing the manufacturing sector, developing an export-driven economy which is globally competitive, as well as enhancing skills development in terms of contributing to product and process improvement. The positive effect of this is that productivity, wages and standard of living will increase, and generate resources for public services and redistribution. For long-term growth and resilience, there should be an incentive to boost public investment in health, education and infrastructure (Bloomberg, 2020).

Additionally, a limitation to monopoly power, promotion of innovation, and increase in accountability and transparency will result in a competitive environment. This scenario further reinforces the sentiments of Mwambari (2020), ascertaining that this pandemic could lead to the decolonisation of Africa, in terms of self-reliance, further economic reforms, prioritisation of African markets, innovation, and local manufacturing embracing the objective behind the establishment of the Africa Free Trade Agreement. Additionally, this initiative will gradually lead to African industrial development programmes diverting from foreign

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funding to national funding drawn from taxation, repatriated funds, and new, higher-value exports.

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Conclusion

This article has discussed the massive impact of Covid-19 on the economy in general, and its effect on the manufacturing sector in particular. What happens next will depend on how the Covid-19 crisis evolves. It is hoped that this virus will be contained, and that its transmission will be slowed down enough for production to resume, and for the economy to go back to normal. This would certainly bring relief to South Africans, and would help companies to bounce back relatively quickly with the help of tailored government measures. If the virus continues to spread, the government will be forced to extend the lockdown, further harming the economy and the supply chain. The global outbreak of the virus could possibly become an eye-opener for the African continent, in terms of realising the dream of self-reliance, and of utilising natural and intellectual resources to re-industrialise and develop the continent (Mwambari, 2020).

The new birth of industrial development in South Africa post-Covid-19 should focus on a 'lessons learned' path, and on an integrated industrial development strategy that involves the government, industry associations, industrialists (1st tier, 2nd tier, 3rd tier, 4th tier within supply value chains), and other relevant stakeholders. It should also assess the state of industry by means of a SWOT analysis (strengths, weaknesses, opportunities and threats), and develop a path for sustainable industrial development. The key competency will be operational efficiencies within Finance Development Institutions supporting manufacturing and industrial development, and accompanied by set targets per sector in terms of expected level of productivity, global competitiveness, contribution towards exports, and operational efficiencies within supply value chains. This requires enhanced strategic transformation processes within organisational value chains. It would also involve continuous improvement through industrial development systems' value chains within the state departments responsible for developing the country's industrial development policy and strategy.

Operations management approaches, such as business and operations strategy, market analysis, financial planning, master planning, demand management, master scheduling and order fulfilment processes, need to be integrated into the national industrial development strategy. This will result in filtering and feeding into the various sector and industry value chains, accompanied by projections and applied interventions in terms of the desired level of productivity in the South African economy, and in terms of manufacturing's contribution to PMI and South Africa's GDP. ■

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