9 Adopting proactive debt management policy strategies to forestall a debt crisis in South Africa

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9.1 Introduction

South Africa[1] could be heading towards a sovereign debt crisis of huge magnitude if certain decisive actions are not taken to manage rising debt levels. As a result of the national lockdown restrictions, aimed at containing the spread of the COVID-19 pandemic, gross domestic product (GDP) growth per capita[2] moved from 0,2 per cent in 2019 to – 8,3 per cent in 2020. However, it has increased to 1,6 per cent in 2021, owing to the ease of lockdown restrictions. Real GDP per capita (per cent change from previous period) is projected at 0,4 per cent in 2022.[3] In addition, the government's budget deficit and maturing loans increased from ZAR432,7 billion in 2019/2020 to ZAR670,3 billion in 2020/2021. Net government debt figures[4] expected to increase from ZAR3,66 trillion, about 74, 3 per cent of GDP, in 2020/2021 to ZAR5,09 trillion, about 84,9 per cent of GDP in 2023/2024.[5] This does not present a bright economic outlook. Minister Tito Mboweni aptly captures the situation in his supplementary budget speech:[6]

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1 'A borrowers' catch-22 African governments face a wall of debt repayments' *The Economist* (6 June 2020), https://www.economist.com/middle-east-and-africa/2020/04/11/africas-debt-crisis-hampers-its-fight-against-covid-19 (accessed 15 October 2020).

2 As percentage change from previous period. See https://data.imf.org/?sk=5778F645-51FB-4F37-A775-B8FECD6BC69B&sId=1461703256968 (accessed 9 June 2021).

3 As above.

4 Gross loan debt less cash balances.

5 Department of National Treasury Republic of South Africa Budget Review 2021 80.

6 Supplementary Budget Speech 2020, https://www.gov.za/speeches/minister-tito-mboweni-2020-supplementary-budget-speech-24-jun-2020-0000 (accessed 15 October 2020).

> We have many strengths. These include our young and ambitious people; our institutions, a robust and vibrant democracy, independent judiciary and our commitment to social justice progress; and our economic strengths: a diverse industrial base, a flexible exchange rate, stable inflation, and deep domestic capital markets that allow us to borrow mainly in rand. But debt is our weakness. We have accumulated far too much debt; this downturn will add more. This year, out of every rand that we pay in tax, 21 cents goes to paying the interest on our past debts. This indebtedness condemns us to ever higher interest rates. If we reduce debt, we will reduce interest rates for everyone, and we will unleash investment and growth. So today, with an eye on the future, we set out a strategy to build a bridge to recovery. Our Herculean task is to close the mouth of the hippopotamus! It is eating our children's inheritance. We need to stop it now! Our Herculean task is to stabilise debt.

Leaving this rising debt unattended may give rise to hyperinflation such as that experienced in other countries such as Zimbabwe in the early 2000s.[7] South Africa's budget deficit has already been revised to 14 per cent of GDP in 2020/21 in response to the spending demands and economic pressures of the COVID-19 pandemic.[8] Also, reduced tax revenue in the early parts of the pandemic contributed to a relatively high budget deficit arising from limited economic activities from which taxes are generated and a retraction of the previously-announced tax increases of ZAR40 billion.[9] A decline in government revenue and economic activities affects the unemployment rate. South Africa's unemployment rate is at 32,6 per cent in the first quarter of 2021 compared to 30,1 per cent in the first quarter of 2020, with a year-on-year percentage change of 2,5 per cent.[10]

The response to the crisis has been to access new sources of funding. The International Monetary Fund (IMF) in July 2020 approved over ZAR70 billion emergency loan[11] from the rapid financing instrument. In addition to this, the African Development Bank (AfDB)[12] and the

7 Zimbabwe's monthly inflation rate reached the 50% mark in February 1999 and gradually increased, reaching its peak at 2200,2% in March 2007. See A Makochekanwa 'A dynamic enquiry into the causes of hyperinflation in Zimbabwe' (2007) 10 University of Pretoria Department of Economics Working Paper 12 4.

8 Budget Review (n 5) 1-2. Tax revenue was R213,2 billion lower than projected in the 2020 budget.

9 As above.

10 Statistics South Africa Quarterly Labour Force Survey Report Quarter 1 2021 13.

11 SABC News 'IMF grants SA more than R70 billion loan to mitigate COVID-19 impact' (27 July 2020), https://www.sabcnews.com/sabcnews/imf-grants-sa-more-than-r70-billion-loan-to-mitigate-covid-19-impact/ (accessed 15 October 2020).

12 'South Africa: African Development Bank approves first ever crisis response budget support of R5 billion to fight COVID-19' *AfDB News* (22 July 2020).

New Development Bank approved emergency loans of US $1 billion to South Africa to tackle the socio-economic impacts of the COVID-19 pandemic.[13] Altogether, South Africa has borrowed over ZAR80 billion more to its already enormous debt and recessed economy.[14] There is scepticism from some political parties[15] such as the Democratic Alliance, who have expressed some reservation about government IMF COVID-19 relief funds. There is doubt that the emergency funds may end up being poorly managed, which could end up affecting South Africa's economic independence, especially if a default in payment occurs.[16] This fear is strongly held because of the IMF's previous track record of conditionalities that have resulted in restrictive monetary and fiscal policies especially in developing countries, with an accompanying negative impact on growth and social spending.[17]

9.2 The growth of sovereign debt post-1994 in South Africa

South Africa's government debt stands at 77 per cent of the nominal GDP in June 2020,[18] compared to about 62 per cent of its GDP in 2019.[19] It is expected to rise to 80 per cent and 84 per cent for 2021 and 2022 respectively.[20] At this stage, it is important to delve back to the post-

13 Reuters News 'New development bank provides South Africa with $1 billion COVID-19 loan' (June 2020), https://www.reuters.com/article/us-health-coronavirus-safrica-ndb-idUSKBN23R09I (accessed 15 October 2020).

14 Statistics for Business February 2020 report 3, http://www.statssa.gov.za/?p=13062 (accessed 15 October 2020).

15 N Mokobo 'Political parties concerned about impact of IMF loan on SA's sovereignty' *SABC News* (28 July 2020), https://www.sabcnews.com/sabcnews/political-parties-concerned-about-impact-of-imf-loan-on-sas-sovereignty/ (accessed 6 June 2021).

16 E Naki 'Fears over IMF loan conditions' *The Citizen Online* (7 August 2020), https://citizen.co.za/news/south-africa/government/2336932/fears-over-imf-loan-conditions/ (accessed 15 October 2020).

17 A Buira 'An analysis of IMF conditionality' (2002) 104 Oxford University Department of Economics Discussion Paper, https://ora.ox.ac.uk/objects/uuid:de9f4d70-c402-42aa-8031-032b89ec0a7b/download_file?file_format=pdf&safe_filename=JOURNAL&type_of_work=Working+paper (accessed 20 December 2020).

18 'South Africa government debt: % of GDP 1960 – 2020' Quarterly CEIC Quarterly Data (September 2020), https://www.ceicdata.com/en/indicator/south-africa/government-debt--of-nominal-gdp#:~:text=South%20Africa's%20Government%20debt%20accounted,63.3%20%25%20in%20the%20previous%20quarter (accessed 15 October 2020).

19 Budget Review of South Africa (2020) 10.

20 As above. Compare with projection at 91% of GDP including debt owed to state-owned enterprises. See 'Moody's downgrades South Africa's ratings to Ba1, maintains negative outlook' Moody Rating Action (27 March 2020), https://www.moodys.com/research/Moodys-downgrades-South-Africas-ratings-to-Ba1-maintains-negative-

democratic history to follow the evolution of South Africa's debt to its present figures, to finding a way out of this quagmire.

From the late apartheid era, it is believed that macro-economic policy and monetarism contributed to the debt build-up,[21] and continued into the post-apartheid era.[22] With the end of the former apartheid regime, the democratic government inherited a large public debt of over US $13 billion, mainly from widespread borrowing and a foreign debt standstill imposed against South Africa.[23] A tight monetary policy was adopted, premised on the belief that a coherent, strict, and effective monetary and fiscal policies will be a basis of the reconstruction and development programme (RDP).[24] Public debt rose to above 48 per cent in 1995. From 1996 the government took measures that prevented further increases in the debt level and by 2000 had reduced the debt level as a percentage of GDP to about 44 per cent.[25]

Debt repayments required under the 1986 plan continued. This is because economists believed that reneging on the debt by declaring it an odious debt[26] would affect the country's credit outlook,[27] especially by rating agencies such as Standards and Poors and Moody. South Africa

outlook--PR_420630 (accessed 17 October 2020). See also Statista 'South Africa: National debt in relation to gross domestic product (GDP) from 2016 to 2026' Data, https://www.statista.com/statistics/578887/national-debt-of-south-africa-in-relation-to-gross-domestic-product-gdp/ (accessed 14 June 2021).

21 A result of the high-interest, tight-money policies to maintain the value of the rand and keep interest rate low. See C Stals 'South African exchange rate policy: A Reserve Bank perspective' in PH Baker (ed) *South Africa and the World Economy in the 1990s* (1993) 148.

22 C Bassett 'The spectre of debt in South Africa' (2008) 41 *Labour, Capital and Society/ Travail, Capital Et Société* 70.

23 N Mhlaba & A Phiri 'Is public debt harmful towards economic growth? New evidence from South Africa' (2019) 7 *Cogent Economics and Finance* 3. See also 'Apartheid debt resettled' *Fin24 Online* (3 September 2001), https://www.news24.com/Fin24/ Apartheid-debt-settled-20010903 (accessed 12 June 2021).

24 G Gotz 'Shoot anything that flies, claim anything that falls' in G Adler & E Webster (eds) *Trade unions and democratisation in South Africa*, *1985-1997* (2000) 172-173.

25 By cutting on public spending. See South African Reserve Bank Statistical Tables, Public Finance 1997 69, https://www.resbank.co.za/content/dam/sarb/publications/ quarterly-bulletins/quarterly-bulletin-publications/1997/4752/Statistical-tables---Public-finance.pdf (accessed 13 June 2021). See also World Bank Central Government Debt Total (% of GDP) South Africa, https://data.worldbank.org/indicator/ GC.DOD.TOTL.GD.ZS?view=chart&locations= (accessed 13 June 2021).

26 Many activists suggested this route. See J Rubin 'Challenging apartheid's foreign debt', http://probeinternational.org/library/wp-content/uploads/2011/02/RUBIN.pdf (accessed 27 April 2021).

27 Fin 24 'Apartheid debt settled' (3 September 2001), https://www.news24.com/Fin24/ apartheid-debt-settled-20010903 (accessed 27 April 2021).

was also wary of a financial imbalance that could produce a debt crisis and compromise its sovereignty with an adverse effect on its economy.[28] Eventually, South Africa repaid the affected debt in full in August 2001 and the debt standstill regulations were repealed in November 2001.[29]

From 2002 to 2004, South Africa committed to a moderately expansionary fiscal regime, beginning roughly with the 2002-2003 government budget.[30] There was more spending on social and capital infrastructure and tax cuts, especially for small businesses.[31] The years 2002 to 2007 were good years.[32]

Arising from a period of prudent fiscal policy management, South Africa used the considerable fiscal space it had created from years of running a budget surplus to carry out strong government spending. Government surpluses and low deficits helped to bring the debt level down, to less than 24 per cent in 2008.[33] Sadly, the global financial crisis of 2008 to 2009 happened, and an economic recession soon followed. The recession led to a fall in tax collection from businesses, contributing to a reduction in government revenue. Spending continued,[34] however, and in time overtook revenue, causing the fiscal balance to turn to a deficit. The discrepancy between spending and revenue was financed by the accumulation of public debt from the capital markets causing South Africa's public debt level to escalate to 43,9 per cent of GDP by 2014.[35]

From 2014 onward, following the downgrading of South Africa's sovereign risk rating and the fiscal response it prompted, the fall in world

28 African National Congress 'Forward to a democratic economy' (1990) Discussion Document, Department of Economic Planning 13. See also Bassett (n 22) 77-79.

29 VB Shayanewako 'The impact of foreign debt on economic growth in South Africa' MComm dissertation, University of Fort Hare, 2013 10, 11.

30 AfDB/OECD 'African economic outlook' (2003) 283.

31 Bassett (n 22) 79. It was the Reserve Bank's policy commitments that kept the interest rates high to maintain the value of the rand that contributed substantially to the debt build-up.

32 L Kganyago 'Fiscal policy, public debt management and government bond markets: Issues for central banks' (2012) 67 BIS Paper 315. Until 2008 South Africa operated a budget surplus and prudent fiscal policy.

33 M Schoeman & K Creamer 'Public debt in post-crisis South Africa' (2015) 1-3, http://2015.essa.org.za/fullpaper/essa_2813.pdf (accessed 18 October 2020).

34 This continued because of the pre-recession spending obligations of the government related to the economic recovery plan. See Oxford Business Group South Africa Economy Outlook 'External factors challenge South Africa's record of strong economic growth', https://oxfordbusinessgroup.com/overview/mixed-review-external-factors-are-making-challenging-period (accessed 28 April 2021).

35 South African Reserve Bank 2014.

commodity prices, the severe recession hitting some of the country's trading partners, uncertain government policies, structural challenges, and the impact of state capture and corruption,[36] created negative GDP growth, causing massive job losses, and increasing the strain on public finances.[37] Deficit financing continued to increase moderately over the next few years, from 43, 9 per cent of GDP in 2014 to 62, 2 per cent of GDP in 2019.

In 2020 the COVID-19 pandemic forced the government to increase its debt with debt financing, to mitigate the effect of the COVID-19 pandemic control measures, such as the national lockdown on the economy. This is in addition to a tax revenue underperformance and an increasing expenditure from fund allocations for containing the COVID-19 effect. The result is a further increase in the debt to GDP figures. Moody estimates that the debt burden will reach 91 per cent of GDP by fiscal year 2023, inclusive of the guarantees to state-owned enterprises (SOEs).[38]

9.3 Implication of rising debt for South Africa

In a study investigating the dynamic relationship between accumulated public debt ratio and real GDP growth in the South African economy over the period from 1980 to 2014, it was concluded that the estimated threshold level that makes the positive correlation between public debt and growth turns negative at 31,37 per cent and above.[39] Against this backdrop, the implication of South Africa's rising debt profile is glaring.

9.3.1 Very high debt levels are accompanied by stiffer austerity budgets

Austerity measures are adopted when governments need to aggressively reduce their budget deficits. In emerging markets, it has been shown that the government starts implementing austerity measures when the debt to

36 J Rossouw & F Joubert 'Warnings about SA's push towards the fiscal cliff went unheeded for years' *Business Day online* (3 September 2020), https://www.businesslive.co.za/bd/opinion/2020-09-06-warnings-about-sas-push-towards-the-fiscal-cliff-went-unheeded-for-years/ (accessed 29 April 2021).

37 Schoeman & Creamer (n 33) 2.

38 M Mkhabela 'South African debt burden will reach 90% of GDP by 2021' IOL Business Report Opinion/ (27 April 2020), https://www.iol.co.za/business-report/opinion/south-african-debt-burden-will-reach-90-of-gdp-by-202 47236765#:~:text=South%20Africa%20recorded%20a%20government,the%20end%20of%20fiscal%202019. (accessed 18 October 2020).

39 Y Baaziz et al 'Does public debt matter for economic growth? Evidence from South Africa' (2015) 31 *Journal of Applied Business Research* 2187, 2194.

GDP ratio exceeds 64 per cent.[40] Austerity budgeting is commonly adopted to show fiscal discipline, especially when creditors become concerned that sovereign states are likely to default on their debts. Austerity measures are implemented through spending cuts, regressive tax increases, or both.

South Africa has gradually adopted austerity measures in response to rising debt levels over the years despite its commitment to the counter-cyclical policies in the 2014-2019 Medium Term Strategic Framework (MTSF). This is evidenced, for example, by the increase in the value-added tax (VAT) rate from 14 to 15 per cent as of April 2018[41] and the steady declining spending allocation per learner in real terms from ZAR17 822 in 2010 to ZAR16 435 in 2017.[42] The presence of austerity budgets has been justified by national treasury to curtail debt levels even though there is strong evidence that austerity fails to achieve this objective.[43] Given South Africa's historical economic injustices of the past and the widening global inequality trends, introducing austerity measures and social spending cuts may delay the emergence of a strong state, capable of meeting its developmental objectives. For example, in the education sector there have been reports on the declining quality of education from learner spending cuts.[44] In 2021 there is more allocation to economic development, but some of the key components of economic development have received cuts as well. For instance, industrialization and exports expenditure allocation is ZAR 36 billion.[45] This is about ZAR 3 billion less than the 2020 budget expenditure allocation of ZAR 39 billion. In contrast, debt service cost rose from ZAR 229 billion to ZAR 269 billion, with a ZAR 40 billion difference.[46] This implies that reducing productive spending in key sectors of the economy or key sub-divisions within a sector does not necessarily translate into reduced debt levels or debt servicing costs.

Studies on Greece show the negative effect from the imposition of austerity. Due to the austerity measures imposed in Greece, public employees' wages reduced by 17 per cent, followed by a reduction in

40 T Grennes 'Finding the tipping point: When sovereign debt turns bad' (2010) WBG Policy Research Working Papers.

41 National Treasury of the Republic of South Africa, Budget Review 2019.

42 B Sibeko 'The cost of austerity: Lessons for South Africa' (2019) 2 Institute for Economic Justice Working Paper Series 29.

43 As above.

44 National Treasury of the Republic of South Africa Budget Review 2019. Eg, learner spending fell by 8% in real terms from R17 822 in 2010 to R16 435 in 2017. See also Sibeko (n 42).

45 National Treasury of the Republic of South Africa Budget Review 2020 and National Treasury of the Republic of South Africa Budget Review 2021.

46 As above.

pension benefits. By 2012 Greece's debt-to-GDP ratio had increased to 175 per cent, one of the highest in the world.[47] Despite Greece implementing one of the most extensive fiscal consolidation programmes, Greece continued to experience a prolonged recession.

In the case of Zambia, austerity measures introduced in 1991 resulted in drastic cuts in Zambia's budget allocations for education, health and social welfare. This is because interest payments on debt accounted for over 50 per cent of government spending in 1991,[48] making it difficult for the Zambian government to spend on its citizens' welfare.

9.3.2 Unchecked rising debt profile affects credit ratings and consequently foreign investment levels

With increasing debt levels, the South African state stands to witness a further deterioration in its credit rating. Although most of South Africa's sovereign debt is denominated in Rands and protects the fiscus from currency exchange fluctuations, especially from trade imbalances, this does not reduce rising borrowing costs which increases debt level. This is because long-term domestic bonds attract higher interest rates on repayment and contributes to debt costs, in addition to a slow growing economy, as seen from the GDP projections and reduced tax income to buffer the rising debt cost. This is an unsustainable debt position to be in and presents a huge risk to South Africa's investment-grade credit ratings.

In January 2020 foreign holding of domestic bonds was at 37 per cent. However, owing to the Moody assessment downgrade from Baa3 to Ba1, foreign investors reacted to the downgrade by disinvesting out of the domestic bond market to the tune of ZAR 54 billion bringing foreign bond holding of domestic bonds to 30 per cent in July 2020.[49]

For 2021, the outlook on South Africa's rating is quite negative even though there are prospects for growth. While S&P maintains a stable outlook on South Africa, Fitch sovereign credit rating (SCR) outlook remains quite gloomy as Fitch bases its SCR at 'BB' status on South Africa's rising government debt, low economic growth and high level

47 Sibeko (n 42).

48 MS Grindle *Challenging the state: Crisis and innovation in Latin America and Africa* (1996) 25.

49 Bloomberg 'Foreign investors lose interest in South African bonds' *Business Tech* (4 August 2020), https://businesstech.co.za/news/finance/422616/foreign-investors-lose-interest-in-south-african-bonds/ (accessed 14 June 2021).

of inequality that could affect consolidation efforts.[50] This presents a challenge to the stabilisation of debt level because sovereign credit ratings influence foreign investors' investment decisions.[51] South Africa's reduced SCR could signal to investors the high-risk potential of investing in the domestic bond market, which could lead to reduced foreign investment inflow into South Africa and act as a setback to economic recovery in COVID-19 times.

Furthermore, unchecked debt levels may lure the government into seeking more foreign loans/credit than it can sustainably manage and gain positive returns on. According to Devarajan et al,[52] rising sovereign debt profiles may result in increased pressure from foreign creditors and international financial institutions (IFIs) on a debtor country to honour its debt repayments or carry out reforms to ensure reliable debt servicing. In addition, the promise of the provision of future credit on domestic structural reform could be used by IFIs and foreign investors to influence reforms that conflict with a country's developmental plans.

9.3.3 Increasing level of state capture, corruption, and interest rates

A high-level accumulation of public debt may provide fertile ground for increased corruption in a nation. This is due to a distortionary effect of the misallocation of resources in unproductive spending with little growth effect on the economy, such as national defence spending.[53] Increased corruption also increases public debt in a vicious cycle, creating a shadow economy that affects the ability of the government to raise taxes. This in turn leads to more borrowing to be used in financing bribes (in addition to tax revenues raised).[54] Poorly-managed debt levels in South Africa are likely to have a negative impact on the sincere fight against state capture and increase corruption levels, creating a vicious cycle of higher debts levels and undelivered developmental goals.

50 S Naidoo 'S&P and Fitch affirm SA's sovereign credit rating and outlooks' (21 May 2021) Money Web Budget, https://www.moneyweb.co.za/news/economy/sp-and-fitch-affirm-sas-sovereign-credit-rating-and-outlooks/ (accessed 14 June 2021).

51 G Kaminsky & SL Schmukler 'Emerging market instability: Do sovereign ratings affect country risk and stock returns?' (2002) 16 *The World Bank Economic Review* 171.

52 S Deverajan, D Dollar & T Holmgren *Aid and reform in Africa* (2001) 21.

53 E Kim, Y Ha & S Kim 'Public debt, corruption and sustainable economic growth' (2017) *MDPI Journal* 4, file:///C:/Users/Marie-Louise/Downloads/Public_Debt_Corruption_and_Sustainable_Economic_Gr.pdf (accessed 20 December 2020).

54 D Kaufmann, A Kraay & M Mastruzzi *World governance indicators project* (2013).

Unchecked government debt from large private sector borrowing for unproductive purposes poses another problem, especially when foreign debt holders decide to sell bonds. There might be difficulties in obtaining buyers willing to take a risk to hold government bonds when debt levels are very high. This could cause interest rates to rise sharply, push the government budget further into deficit and tilt the economy further into recession. An economy operating on a budget deficit causes interest rates to rise. This will be seen through a high inflation, and a stagnant local and regional market. The overall implication is that very high external debt levels may lead to economic inertia and growth depression, according to Schclarek,[55] especially in developing countries, due to a spill-over effect from the private sector hit by the high cost of debt. This in turn undermines foreign investor confidence and stalls the possibility of equity funds injection into the economy leading to more depression.

COVID-19 debt is a unique situation. This is because it comes from a sudden global pandemic, unlike the global financial crisis of 2008. The final part of this chapter provides some recommendations on the way forward.

9.4 Policy recommendations

The necessity of taking proactive steps and corrective policy measures to stabilise sovereign debt cannot be overemphasised. Debt, while useful in an economy, depends on prudent management to deliver its benefits. South Africa's rising debt profile, though disturbing, should not be used as a justification for hastily-reactive fiscal decisions. To this end, the debt management approaches adopted in this chapter would be centred on two major themes – closing the drainage channels and charting new courses.

9.4.1 Replace austerity budgeting with inclusive GDP growth spending

Austerity policies are expected to free up resources not only to meet debt obligations, but can be used to promote a growing economy. However, empirical evidence shows that this does not always happen. Instead, social services decline, employment and wages do not grow and, in the long run, austerity policies eventually harm the economy.[56] While imposing stiff austerity measures may reduce debt in the short term, it leaves a trail

55 A Schclarek *Debt and economic growth in developing and industrial countries* (2004).

56 OXFAM 'A cautionary tale: The true cost of austerity and inequality in Europe' (2013) 174 Oxfam Briefing Paper.

of long-term negative impacts,[57] such as a decline in wages, an increase in unemployment levels, and depressed growth, social unrest which could further exacerbate current sovereign debt levels,[58] as noticed in Greece.[59] This should be avoided. First, South Africa can look inward by adopting inclusive growth policies and mobilising domestic sources of finance that are sustainable, such as adopting policies geared towards a stronger reliance on domestic financial markets and domestic savings, to avoid relying heavily on short-term external finance.

Also, government spending budgets should be reasonable, purposeful, and aimed at productive sectors/activities of the economy that can pull in private sector investment such as digital trade, innovation in fin-tech, and agro-based SMEs. Also, there should be limited cuts to programmes and expenditure that do not harm essential services or economic activities, while channelling funds realised towards areas that have a direct and strong potential for positive impact on the GDP and spur economic growth. Funds so channelled should be constantly monitored and evaluated for performance. For example, government departments/parastatals performing similar functions could be merged, and over-bloated expenses such as 'foreign training expenses' could be trimmed. Funds realised from non-essential cuts could be channelled into strategic educational programmes such as investment in STEM and entrepreneurship. This would empower a generation of new economic growth drivers through continuous product and business innovation. As the GDP grows, debt levels would eventually reduce from a stable moving economy, investor confidence (for investment into the economy) would

57 IC Amakor & P Ndubuisi-Okolo *Austerity measures and its effect on net investment and export capacity of Tanzania (1986-2018)* (2019) 8 *Journal of Social Development* 6. Tanzania's government austerity measure toward export sustainability did not yield any positive result.

58 Notably, 'the interaction between the austerity measures and structural reforms generated a downward spiral of shrinking GDP and continued increases in sovereign debt'. See P Engler & M Klein 'Austerity measures amplified crisis in Spain, Portugal, and Italy' (2017) 7 *DIW Economic Bulletin*, DIW Berlin, German Institute for Economic Research 89-93, https://ideas.repec.org/a/diw/diwdeb/2017-8-1.html (accessed 27 October 2020).

59 FIDH/HLHR Report on downgrading rights: The cost of austerity in Greece 3, 9-12, https://www.fidh.org/IMG/pdf/downgrading_rights_the_cost_of_austerity_in_greece.pdf (accessed 29 April 2021).

be strengthened, producing a strong multiplying effect. In addition, GDP growth expenditure will fund itself over time, if properly managed.

9.4.2 Multilateral calls for partial debt forgiveness and renegotiated debt repayment to private creditors

Corrupt activities negatively impact a state's decision-making and service delivery processes that drive economic growth. It is recommended that the state impose strict consequences for deliberate fiscal corrupt activities.

According to the International Debt Statistics,[60] South Africa, like most other middle-income countries, owes a large chunk of its long-term (public and publicly-guaranteed) external debt stock to private creditors.[61] Private creditors own about 9 per cent of the external public debt of low-income countries, but 63 per cent of that of middle-income countries,[62] through their ownership of emerging market bonds, with interest payments made on these bonds. High debt figures may act as a constraint to more borrowing because of falling credit ratings.[63] This in turn affects creditors' desire to lend.

A policy recommendation would be for South Africa to reach an agreement with other middle-income countries such as Nigeria and Kenya, to multilaterally approach these private creditors (instead of unilaterally) and collectively renegotiate the terms of debt servicing. Also, in renegotiating debt terms, a proposal that balances partial debt servicing and partial debt forgiveness on grounds that funds released from 'partial debt interest payment' be channelled to economic recovery could be put forward. The proposal could rely on the unforeseen economic consequences of the COVID-19 pandemic as a '*force majeure* of sorts' that had upset the economic *status quo* and agreed payment plans.

Similarly, massive capital flight from large-scale tax evasion and accumulation of offshore wealth flow out of South Africa should be examined and addressed. This deprives the fiscus of necessary resources for development through reduced taxes from private sector investment, contributing to an underactive economy. An estimate of accumulated

60 World Bank Group International Debt Statistics (2021) 128.

61 As above. Total long-term (public and publicly guaranteed) external debt stock is about US $151 million with private creditor total figure share at US $78,523 million.

62 P Bolton et al 'Born out of necessity: A debt standstill for COVID-19' (2020) *CEPR Policy Insight* 103.

63 One of the reasons provided by Fitch in downgrading South Africa's SCR is its high debt levels. See Naidoo (n 50).

capital flight out of South Africa in 2017 amounted to over US $290 billion.[64] Capital flight of such magnitude will persist in delaying South Africa's development and adversely impact the economy through foregone private investment, tax revenue and potential funds for public investment. In addition, the use of cross-border tax planning and transfer pricing manipulations by businesses to reduce their local tax liabilities should be curbed. Although there are laws addressing illicit flows, proper execution remains a challenge especially because the effective tax collection abilities of the South African Revenue Service (SARS) have been steadily undermined by corruption.[65] Therefore, the government must focus on restoring capacity of revenue administration and encourage inter-departmental cooperation and swift communication as a short to long-term strategy to blocking this drainage channel.

9.4.3 More focus on resource mobilisation through minute taxing of domestic and cross-border digital transactions

Owing to the national lockdown imposed by the South African government in curbing the spread of the pandemic, businesses have had to find creative ways in adapting to the new situation. This has led to a growing preference for digital business platforms to physical business locations for transactions by consumers. On the other hand, businesses, including SMEs, are adapting to the new situation through integrating digital processes into their physical business model.[66] This is a catalyst for developing the digital economy alongside the physical economy through the creation of digital monetary value that can be taxed. The government could develop a policy in cooperation with the commercial banks to include a tiny digital platform levy on payment platforms, perhaps at 0,05 per cent of digital transaction cost. With regard to cross-border digital transactions, perhaps it is time for South Africa to cooperate with other Southern African countries on reviewing and reforming the Draft SADC Model Multilateral Tax Agreement, to capture cross-border digital transaction taxation, especially

64 Calculated and capitalised as the capital flight in present year plus the stock of wealth in the previous year capitalised at the Treasury bill rate. See L Ndikumana, K Naidoo & A Aboobaker 'Capital flight from South Africa: A case study' (2020) PERI Working Paper 11, https://www.peri.umass.edu/economists/leonce-ndikumana/item/1323-capital-flight-from-south-africa-a-case-study (accessed 14 June 2021).

65 S Gebrekidan & N Onishi 'Corruption gutted South Africa's tax agency. Now the nation is paying the price' *The New York Times* (10 June 2018), https://www.nytimes.com/2018/06/10/world/africa/south-africa-corruption-taxes.html (accessed 29 April 2021).

66 K Thompson Davy 'How COVID sped up SA's digital transformation' *Financial Mail Digital* (21 April 2021), https://www.businesslive.co.za/fm/fm-fox/digital/2021-04-08-how-covid-sped-up-sas-digital-transformation/ (accessed 8 June 2021).

by SMEs. This could be achieved by creating a nexus between the transaction parties and the income without the use of a physical presence or an effective place of management as is found in most tax treaties.[67] Furthermore, with regard to capturing cross-border digital transactions, there would be a need for stronger cooperation between SARS and other revenue administration authorities, starting regionally within the SADC for cross-border digital transaction information sharing before extending it to a continental and global level in time.

9.5 Conclusion

An unsustainably high debt level is fiscally unhealthy for an emerging market economy such as South Africa. Funds for development are unproductively channelled into debt servicing, contributing to a vicious debt cycle. Despite the challenges, a near sovereign debt crisis often provides a golden opportunity to 'never let a good crisis go to waste' while serving as a wake-up call for addressing weak policy decisions. There may not be a one-size-fits-all solution to forestalling a crisis, but one thing is clear: Fiscal resource drainage must be contained, while ensuring that a transparent, well-monitored GDP growth expenditure path is followed. It is hoped that the recommendations proposed in this study contribute to managing South Africa's rising sovereign debt.

67 Art 5 SADC Draft Model Multilateral Tax Agreement.

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