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INVESTING IN THE PROMISE OF SOUTH AFRICA: AN AMERICAN PERSPECTIVE

Dr. Howard C. Reed is
Special Counsel for Finance and Investment Policy
to the United States Trade Representative

On behalf of President Clinton and the United States Trade Representative, Ambassador Kantor, I welcome the opportunity to talk for a few minutes about the promise of South Africa and about how we can develop a partnership with you to assist in accomplishing your objectives, notably: a significantly better life for your citizens; a diversified and expanding economy; a more stable economic and social environment; and a full and complete participatory democracy for the people of South Africa. One year ago, President Mandela, in his inaugural address to your Parliament, underscored your Government's commitment to a people-centred society of liberty. He emphasized that this goal would be the meaning, justification and purpose of the Reconstruction and Development Programme (RDP) outlined in the White Paper last November.

We commend you on the tremendous start that you have made toward accomplishing your objectives. I know that you have been told that many times by many people and perhaps many times by the same people during the past year.

We do not think, however, that given what has transpired in South Africa since the election, that we can be too praiseworthy, especially since press reports on US trade actions may occasionally call our good intentions into question. Therefore, let me take a few moments to outline our thinking on the issues and obstacles that we face in building a strong and mutually beneficial partnership between the United States and South Africa.

As for the United States, we are faced with a mounting national debt that is approaching US\$5 trillion, annual budget deficits of US\$150-200 billion, runaway health care costs, continuing global economic and strategic responsibilities, and a balance-of-payments deficit exceeding US\$100 billion in eight of the last ten years. Now a restless American electorate is demanding greater fiscal responsibility from the government. We are now in the process of agonizing over what and how much to cut [a problem that is not unfamiliar to you]. One of the principal targets of our Congress over the past few years is US foreign aid expenditures. Quite candidly, pressure to

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reduce the foreign aid budget even more will continue - and traditional opposition to cutting foreign aid is likely to weaken not strengthen. The prevailing attitude among many government officials as well as private sector practitioners is to let the private sector and the markets provide the necessary and needed capital for developing countries.

Clearly there is considerable merit in the private sector (the markets) playing a significant role - actually all successful economic development experiences that I am familiar with were to a significant extent private sector (market) driven. Even so, the government was not a passive bystander. In successful economic development experiments, governments have provided complementing financial support and legislation. Without that support, it is doubtful whether the experiments would have been successful. The evidence will clearly show that the most successful instances have been when government and the private sector worked together, in concert, with common objectives. It is this approach that will be the most effective for living up to our global economic responsibilities.

As for South Africa, we recognise the magnitude and the complexity of the problems that must be resolved if South Africa is to be the country that you [and we] want it to be. The problems are:

- * providing jobs for the millions of unemployed;
- * bringing about racial diversity of employment in the private and public sectors;
- * providing adequate housing and infrastructure; and
- * completing the reintegration of South Africa into the world economy so that it can, perhaps,

act as a pole of growth for Southern Africa as a whole.

We understand the challenge that these problems pose for all South Africans, particularly for those of you in positions to effect change and progress. As a rule of thumb, some developing economies - the Asian Tigers, for example - invest each year the equivalent of 23%-25% of their GDP in capital stock, both housing and commercial activities. Your Minister of Labour has said that South Africa will need to invest like amounts if you are to achieve the required 8%-10% annual growth rate. That would mean that South Africa would have to find US\$40-60 billion to meet its annual investment needs. The United States wants to be helpful, in a way that complements your efforts.

Of particular note, many of the issues impacting on South Africa are the same issues as those facing the world's most advanced industrialised nations. These issues are:

- (1) providing jobs for the unemployed and the underemployed;
- (2) increasing global trading activity by pushing the agenda for market oriented economies and greater market access to those economies;
- (3) using regional structures and organisations to open markets and improve the terms of trade; and
- (4) establishing a financial framework and structure for relatively stable exchange rates, continued global liquidity, and efficient capital utilization.

South Africa has begun to tackle these problems through the RDP which sets out an ambitious programme for re-engineering government and establishing a

broad-based strategy for economic development. Since this is your means to an end, we will be supportive.

The Key Role of Foreign Investment

In recent years, portfolio investment has surpassed direct investment as the predominant element of cross-border capital flows. The increasingly mobile character of portfolio investments is at times devastating, particularly for host countries. For example, investors withdrew nearly US\$13 billion in one day (20 December 1994) after Mexican officials announced that the government would not support a fixed exchange rate. The result of this action led to further draining of Mexico's shrinking international reserves, and forced the government to float the peso the very next day, 21 December 1994. Some 'Monday morning quarterbacks' may question the wisdom of the Mexican government's announcement, but that is not the point. The point is that foreign portfolio investors have it in their power to cause crises and disaster almost instantaneously and without warning.

On the other hand, there can be significant benefits from portfolio investments. Such investment often results in efficient allocation, lower capital costs for the recipient country (and its firms) by increasing the supply of capital which typically increases the foreign exchange value of the recipient country's currency, and in turn reduces the cost of foreign sourcing by making imported inputs less expensive.

Ideally portfolio investment and direct investment should, to some extent, complement one another, because they are in fact partial substitutes. This is as it should be. Foreign direct investment capital should always be large enough to function as the core (or equity) capital of

a country's foreign investments. It is for these reasons that I am troubled by the present structure of investment flowing into South Africa. The US investment funds that have been chartered to invest in South Africa are all portfolio investment funds. Our policy development initiatives will be geared to bring this apparent imbalance into balance, on the principle that increased investments in 'real assets' is needed to balance the flow of portfolio funds. In addition, it is direct investment that will have the greatest impact on reducing South Africa's number one problem - unemployment.

Reducing unemployment, anywhere in the world today, is increasingly difficult given the predominant propensity to develop and market new technology at a dizzying pace. There is this unquestioned belief that investors and new technology are always beneficial to the economies and their workers. Industrialised economies preach the virtues of technology - efficiency, cost savings and higher productivity. Developing economies rail against technology exports to their countries that are less than state-of-the-art. Little, perhaps *no*, consideration is given to the real consequences of such investments.

These cutting-edge technologies, when introduced in developing countries, frequently create an underclass of illiterate and unskilled would-be-workers that are by-passed as their country's economy leapfrogs several stages of industrialisation straight into the advanced technology arena dominated by the most advanced industrialised countries. In the case of South Africa, we recognise clearly that there are sectors of your economy that are not only capable of absorbing state of the art technologies but will introduce advanced technology processes, products, etc. into the South African market and throughout the world. However, many of your sectors perhaps will benefit most from investments of 'appropriate

technology' that is more labour intensive - not outdated technology that suppresses worker growth and upward mobility - and provides value-added for the worker and the economy by significantly reducing unemployment.

We want to feel that if the time comes to actively engage in discussion about 'appropriate technology' investments in South Africa, that our intentions will not be misunderstood, misrepresented, and/or distorted.

Our recent implementing legislation for the Uruguay Round included a provision for the Clinton Administration to develop a Trade and Development Policy for sub-Saharan Africa. The United States Trade Representative has been tasked to develop the policy. It is my responsibility to marshal the resources, develop the policy, and draft a report to congress for the President and Ambassador Kantor. This initiative can do more for sub-Saharan Africa, particular South Africa, than any here-to-fore aid or aid-related package.

We are moving forward. The first phase report on the Trade and Development Policy will go to Congress in December of this year. We ask you to also move forward and commit to applying national treatment to foreign investors, which will soon lead to a US-South Africa Bilateral Investment Treaty. Such a treaty, together with an agreement between our two countries on effective protection of Intellectual Property Rights, will do much to assist the Clinton Administration's efforts to encourage further American investment here.

One of my country's great leaders commented, 'a good example is the best sermon'. In a favourable environment we, the United States, will put into practice what we are preaching.

This is an edited version of an address given by Dr. Reed when he visited Jan Smuts House on 24 May 1995.

STATEMENT OF PURPOSE

The South African Institute of International Affairs is an independent organisation which aims to promote a wider and more informed understanding of international issues among South Africans.

It seeks also to educate, inform and facilitate contact between people concerned with South Africa's place in an interdependent world, and to contribute to the public debate on foreign policy.