POLICY BRIEF * COVID19 ECONOMY GROUP

Top Covid-19 policy priorities for protecting employment

Executive Summary

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South Africa entered the Covid-19 pandemic with 29% unemployment, over 40% living in poverty and the highest rate of inequality in the world, all now set to rise.

It is within our power to limit the damage. A balance can be found between containing the virus and other health, social and economic imperatives in a way that is mutually reinforcing.

This paper argues that a centrally regulated approach that controls activity should now give way to *enabling* communities and businesses to adhere to the protocols required to contain the virus. This approach is consistent with the President's May 24th announcement pivoting the country to a level 3 lockdown by June 1st.

Significant focus must now be trained on three top priorities to ensure that the return to work is sustained and employment protected:

- The first priority is to craft and implement "risk-adjusted strategies" that act like dynamic early warning systems and virus containment measures. This is a combination of information systems, testing, contact tracing and isolation, along with physical distancing, wearing of masks and sanitising[2].
- The second priority is to engage far more deeply with communities to identify strategies that can be sustained in a variety of living conditions.
- The third priority is widespread financial support to all affected business and workers to limit the extent of permanent damage. Returning to work is going to need special support and monitoring to ensure compliance with health protocols. The foundations to drive big-employment-growth-game-changers must be lain now.

Neither a lockdown nor an economic opening will be successful without the first two priorities. And they are amongst the few Covid-19 interventions that constitute long term investments for many other imperatives from controlling TB to community safety. The third priority is essential to the success of an economic rebound.

Four employment scenarios to 2023 demonstrate the imperative. The scenarios revolve around the effective implementation of these three priorities, as well as the policy reforms that stimulate a new wave of economic dynamism. The scenarios consider impact on GDP, employment, tax collection and public finances available to fuel recovery and economic development going forward.

[1] This paper draws on input and comment from the Covid19 Economists Group, convened by Miriam Altman (Professor of 4IR Practice, School of Economics, University of Johannesburg) and including Imraan Valodia, Stuart Theobald, Peter Attard Montalto, Michael Sachs, Mzukisi Qobo, Andrew Donaldson, David Francis, Tania Ajam, Alex van den Heever, and Wandile Sihlobo. Peter Attard Montalto prepared the macro-modelling used in this paper. Comment was also received from Prof Rob Davies, Caroline Skinner, Carol Paton, and Neva Makgetla. The paper also benefited from advice and data from Neva Makgetla at TIPS. The result is the responsibility of Miriam Altman alone.

[2] A fuller explanation of risk-adjusted strategies can be found in Fuest and Lohse 2020 and van den Heever 2020. The measures discussed in this paper are relevant to the immediate actions being recommended.

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South Africa is at a Covid-19 cross-roads. There is intense pressure to lift the lockdown and open the economy. Some say the lockdown no longer serves a public health purpose and the economy is being ravaged. The National Command Council that leads the government's response is concerned that opening will lead to uncontrolled spread of the virus. Sustainably lifting out of the lockdown is critical, and there is no roadmap. The stakes are high and there are no right answers, just ones that juggle uncertain probabilities.

Extremely high open unemployment, extensive and deep poverty and the highest rates of inequality in the world require that the top priority be focused on economic growth that stimulates employment and lifts communities out of poverty. Diminishing growth over the past decade has weakened industry, slowed job creation, while state capture damaged state capacity. Efforts to get the economy moving have been thrown off-course by the global Covid-19 pandemic.

There is little doubt that a better balance between health and economic imperatives must be found. This will require a different way of thinking about and prioritising these twin imperatives.

The dichotomy between arguing to 'open up now' versus 'lockdown and open up step-by-step' really needs to be mediated differently. The emphasis in managing the pandemic should now shift from a centrally regulated approach that controls activity to one that is *enabling* of participation and compliance in health solutions, which in turn is the foundation for reducing risk in opening the economy.

Risk-adjusted strategies are essential to the success of a lockdown ***and*** they are essential for the opening of the economy. They are required in both instances.

Risk-adjusted strategies act like dynamic early warning systems and virus containment measures. They include information systems that enable effective collection and provision of information, testing that offers results within 24 hours, contact tracing involving technology and human interface, places to isolate those infected, physical distancing strategies, and the widespread use of masks and disinfection (for example see vd Heever 2020 and Fuest and Lohse 2020[3]).

The WHO (2020) guidelines say this, and they also emphasize the need for community engagement.

Far more weight needs to be put on appropriate design of risk-adjusted and physical distancing strategies that can be reasonably implemented in a variety of living conditions, workplaces and transport modes.

The design and implementation of these elements should dominate Covid-19 response work. They are amongst the only tools we will have to manage the virus spread and restore economic activity.

And they are amongst the only Covid-19 expenditures that are long term investments: unlike ventilators, PPE or field hospitals, the strengthening of information systems, lab capacity, and community engagement will be instrumental in managing other issues from TB to community safety.

Four employment scenarios to 2023 demonstrate the imperative and are presented in the table below. The scenarios revolve around:

[3] Risk-adjusted strategies is a term used to explain actions that combine a relaxation of restrictions in the social and economic environment with continued effective health protection. They are aimed at:

- preventing the virus from spreading again rapidly
- strengthening the health care system to ensure the best possible treatment for as many patients as possible - with COVID-19 as well as with other serious diseases
- protecting groups at high risk for severe COVID-19 diseases
- avoiding social and psychological hardship in the fight against the pandemic as far as possible;
- making economic activities possible without taking unnecessary health risks
- limiting restrictions of fundamental rights to the minimum and in accordance with the principle of proportionality.

- the extent of reliance on lockdown versus risk-adjusted strategies
- the efficacy of township physical distancing and sanitising strategies
- the pace and extent of business and wage support that enable continuity of economic activity
- meaningful steps taken to address significant policy reforms that stimulate a new wave of economic activity and dynamism.

Scenario 1 shows a possible outcome where the central response to containing the spread of the corona virus relies on lockdowns. The modelling is based on at least some level of the lockdown being in place for most of the period between April and September 2020 and then scaling down to December. Risk-adjusted strategies are not sufficient to contain the spread. Although there is a lockdown, it is not effective in townships as appropriate community-engaged models have not been pursued, so residents largely ignore physical distancing guidelines. Business support comes too late and many firms retrench and close over the course of 2020 and 2021.

In this scenario, GDP falls by 20% in 2020 and 3,2 million workers lose their jobs. By 2023, it is clear that even after some rebound, 1,8 jobs are permanently lost, the new normal for the unemployment rate is around 37% and the economy is stagnating. Over the period from 2020/1 to 2022/3, tax collection is R 1,5 trillion less than that envisaged in the 2020 Budget. Interest now swallows 29% of revenue collected.

Many more people are thrown into deep poverty including those that had been working all their adult life. Child malnutrition becomes more commonplace. Gangs and criminal networks take the gap where the state has stepped out. Social instability and political contests make it politically impossible to scale back grants and public employment, leaving very little for economic recovery and drivers of future growth such as agriculture, infrastructure, R&D, or renewable energy. This leads to a dark decade.

Scenario 2 also has a reliance on lockdowns but has introduced a bit more risk-adjusted strategies and business support. Too few firms get support and there is significant retrenchment and business failure. There is no material progress in township physical distancing strategies. Two fewer weeks in lockdown relative to Scenario 1 has a big impact. In this scenario, GDP falls by 15% in 2020 and 2,5 million jobs are lost. By 2023, it becomes clear that about 0,9 million jobs have been permanently lost, the unemployment rate sits at 33% as the new normal and the economy is stagnating. Tax revenue falls by R 1 trillion over 2020/1 and 2022/3. Around 23% of tax revenue goes to making interest payments.

Scenario 3 sees commitment to risk-adjusted strategies that enable freer movement of people. Significant effort is put to engaging communities to find sustainable approaches to physical distancing. The level 5 and 4 lockdowns last 65 days, and then the extent of control falls from level 3 to 1 over the course of 2020. Widespread support gets to firms that need it, and that stops many firms from retrenching or closing. GDP falls by 10% in 2020 and 1,6 million jobs are lost. By 2023, it becomes clear that around 225,000 jobs are permanently lost and unemployment sits around 30%. There is a shortfall in tax revenue over the three years from 2020/1 to 2022/3 of R 686 billion as compared to the 2020 Budget. The economy reverts to a weakened pre-Covid-19 state, still stagnating as structural reforms are not introduced, nor is the drive for new economic activity pursued with enough vigour.

Scenario 4 pivots from Scenario 3 with the further addition of important structural reforms being implemented. There is great effort invested in building a professionalised state capacity and this, in turn, creates more certainty for investments that drive growth and employment. Progress is made on energy IPP investments and supplier industries, infrastructure spending (especially in housing, public building refurbishment and maintenance and supplier industries), agro-processing and associated exports, and similar. Digital migration takes place and spectrum is released. Broadband access is made more affordable and government services go online, saving significant costs for low-income households.

Scenario 3 and 4 have similar outcomes in 2020. It is the subsequent years where the difference is seen. By 2023, GDP is growing by 2,5% pa. Employment has restored to pre-lockdown levels and is by then expanding by around 200,000 annually. There is a shortfall in tax earnings of R370 billion over the three years to 2022/3. Public finances are strained but there is a path back to sustainability. Economic capacity is being strengthened and there are signs of upward movement.

The best case scenario presented in this paper really is the best case and will require significant commitment and course correction in Covid-19 policies and in demonstrating commitment to required structural change.

The worst case scenario is not the worst that can happen. There could be domestic reverberations into the banking sector or more dramatic shifting to reduce labour ratios or political cleavages that deepen as resources become ever more scarce.

These scenarios focus on the domestic picture. Further thinking is needed about what might happen globally and how this might affect South Africa.

Four Employment Scenarios linked to Four Covid-19 Policy Responses

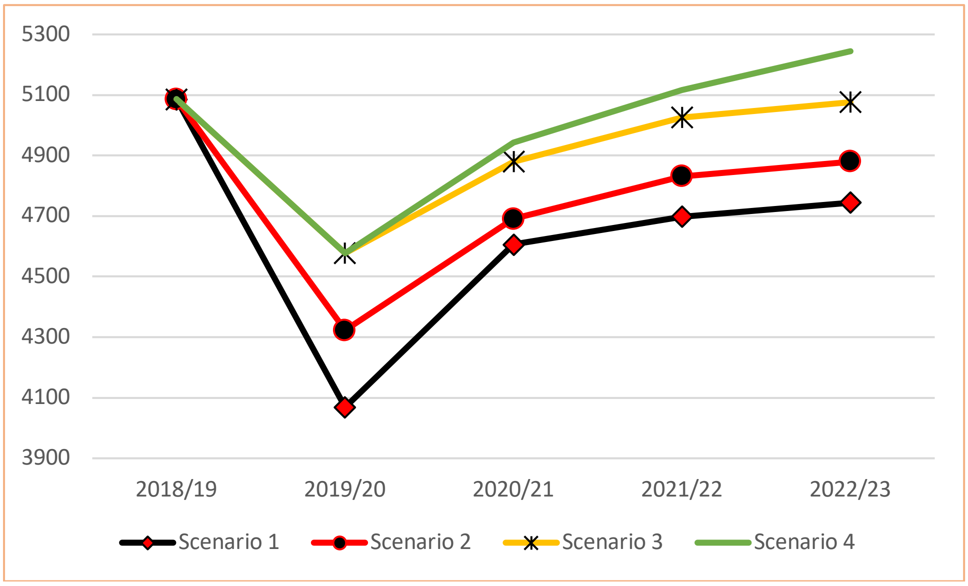
	Scenario 1	**Scenario 2**	**Scenario 3**	**Scenario 4**
GDP change in 2020	-20 %	-15 %	-10 %	-10 %
Employment change in 2020	-3.2 m	-2.5 m	-1.6 m	-1.6 m
Unemployment rate 2020	43 %	40 %	36 %	36 %
Permanent job losses by 2023	-1.8 m	-0,9 m	-0,2 m	+0,2 m
Change in real GDP in 2018/19 to 2022/23 (Rbn)	-341	-206	-9,8	+158
Unemployment rate by 2023	37 %	33 %	30 %	28 %
Tax revenue shortfall in 2020	R 400 bn	R 350 bn	R 225 bn	R 225 bn
3-year tax revenue shortfall relative to 2020 Budget	R 1 562 bn	1 064 bn	R 686 bn	R370 bn
% of tax revenue accruing to interest payments by 2023	29%	23%	19%	17%
Policy response element				
Risk-adjusted strategy effectively implemented	🔴	🟡	🟢	🟢
Township community engagement in physical distancing	🔴	🔴	🟢	🟢
Economic interventions create bridge for firms and employees to other side. Enables rebound	🔴	🟡	🟢	🟢
Significant structural improvements lead to lifting potential growth rate	🔴	🔴	🔴	🟢

Red means poorly implemented, amber means partially, green means impactful implementation

The likely shape of the recovery is a distorted square root and very likely not a "V". Further reverberations domestically or globally could see a distorted square root shape transformed into a W that veers downwards. This can particularly happen where the economic foundations no longer support a meaningful economic rebound.

Re-opening the economy is *essential* to veering closer to Scenario 3 and lays the foundation for achieving Scenario 4. There is significant pressure to do so as fast as possible. Having risk-adjusted strategies in place will enable that to happen.

Real GDP (Rbn) in Four Scenarios – 2019/20 to 2022/23



In a context of great uncertainty and evolving events, knowledge about the Coronavirus and how to respond to it is progressing fast. Any set of recommendations today could be overtaken by events tomorrow.

Even within this state of flux, there are three certainties, no matter how the Coronavirus evolves or our emerging understanding of policy responses:

- A risk-adjusted strategy and a sustainable physical distancing strategy should sit centre stage of any programme to manage the virus. They should be within our immediate capability to implement, set up to be flexible and adaptable to learning and feedback.
- The risk-adjusted strategies must be suited to different living conditions and involve communities, so that they effectively promote the required behaviour change.
- Effort must be focused on sustaining economic activity and ensuring economic capacity is not unnecessarily lost. Then look to the future.
  - The fastest route back to economic activity, charted in a way that enables physical distancing, will always be the best one. It is always better to generate revenue, in companies and through tax, than it is to save companies or borrow for the shortfall. And every day counts.
  - Success in opening up will depend on the effective implementation of health and safety protocols. Firms will need substantial support and guidance to comply with new ways of working. Compliance monitoring will have to be significantly ramped up.
  - The economic rebound will be stronger, the fuller and faster business support is delivered to slow down retrenchment and closures. It will still be needed even as the economy re-opens
  - Informal traders could thrive in this period. Let them operate subject to health guidelines, support their supply chains and get them online.
  - Those losing their jobs due to the lockdown should be actively channelled back into work opportunities, so that they don't join the long-term unemployed.
  - The economy will need new sources of growth and employment. We need to get the foundations in place to enable quick movement on these

The highest priorities in lifting out of a lockdown must be to dramatically strengthen risk-adjusted and physical distancing strategies and to enable the fastest route back to economic activity by supporting workplace readiness. This will give SA a chance of pulling through to a sustainable future.

That future will require big-growth-game-changers that could give a dynamic boost. Some criteria are needed – for example, one does not foresee much international movement of people for some time. Dynamic activities have the character of being job creating and having significant linkages especially into supply networks. Some examples include: pumped up social housing construction, maintenance and refurbishment of public buildings, public transport systems construction, implementation of the IRP and associated IPP energy investments such as battery storage, and much more meaningful expansion of agriculture and related industries. Eventually we will want to think about a more ambitious domestic tourism drive. A faster rollout of ubiquitous affordable broadband, combined with allowing online sales of anything and the stimulation of fintech would be transformative of the South African business landscape. Enabling informal traders to order online and warehouse could also be transformative of township enterprise.

Special approaches will be needed for industries that may take time to open such as tourism, hospitality, restaurants, beauty services and the arts. These sectors account for a large proportion of employment, and especially of women and youth. Innovative strategies must be found to figure out how to open sooner-than-later. For example, the Chinese have introduced 'COVID passporting' that allow free movement of those who are indicated as "green". There should be an opportunity for controlled tourism – for example of green passport Chinese tourists visiting controlled destinations in SA. In the meantime, special financial support may be needed to maintain infrastructure and hotels so that core capacity is not lost.