COVID-19 : South Africa, an Economy on its knees

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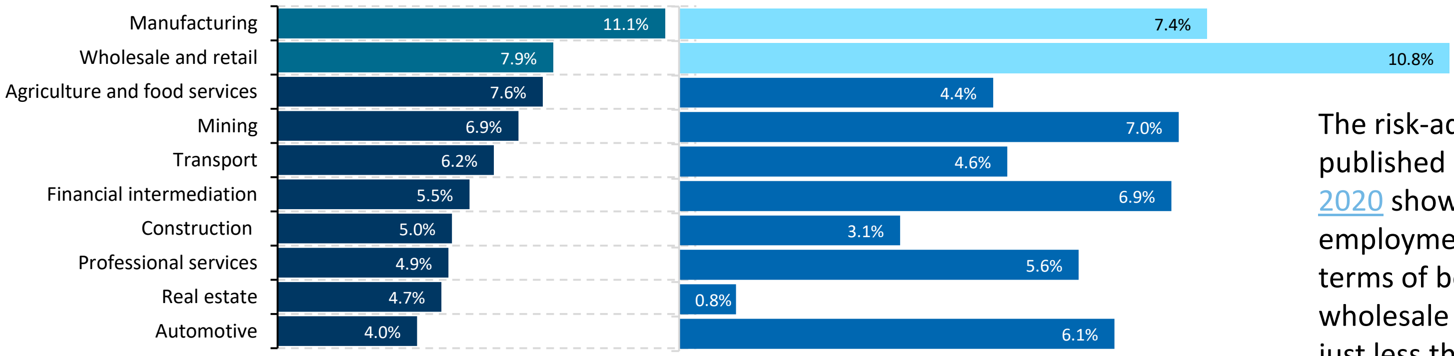
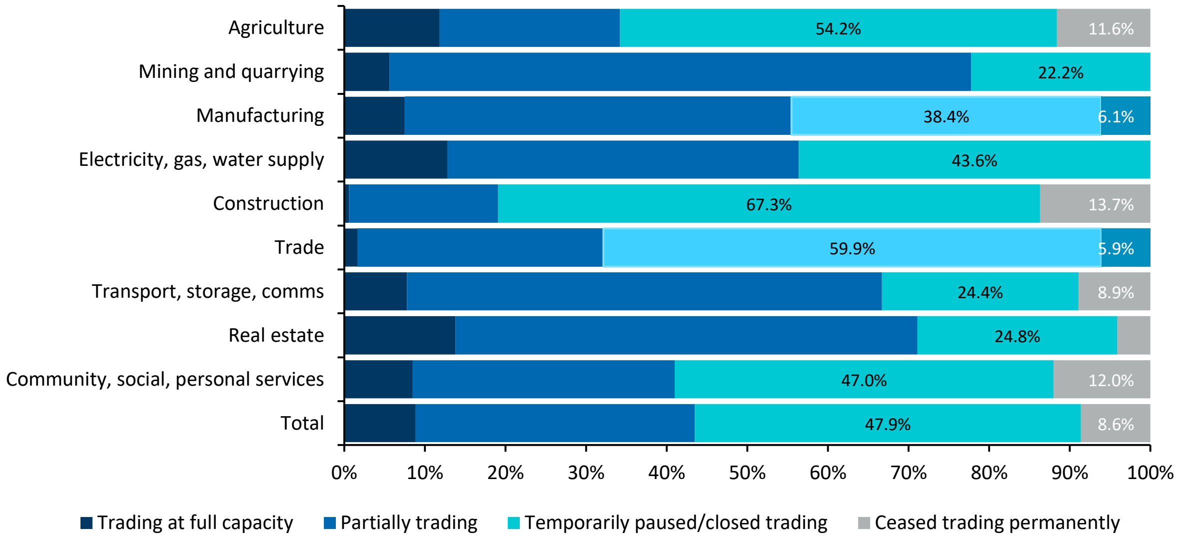
Economic restrictions have kept large employment sectors closed

Contribution to GDP (%) **Contribution to employment (%)**



Source: National Department of Health, Risk-adjusted strategy for economic activity, 26 April 2020

Trading status of businesses, 14 – 30 April 2020



Source: StatsSA second business impact survey, May 2020

The restrictions on economic activity implemented with the nationwide lockdown imposed on 27 March had a significant impact on different sectors of the economy.

The risk-adjusted strategy to re-opening the economy, published by the National Department of Health on 26 April 2020 shows the contribution of various sectors to GDP and employment. The sectors with the highest contribution in terms of both GDP and employment are manufacturing, and wholesale and retail trade. Combined, these sectors contribute just less than 20% of GDP and employment in the South African economy.

The second business impact survey conducted by Statistics South Africa between the 14th and 30th of April 2020 indicated that by the second half of April, approximately 45% of manufacturing businesses and 65% of retail and wholesale trade businesses were either temporarily closed or had ceased trading permanently. Other sectors that have been particularly hard hit by the economic restrictions imposed during alert Level 5 and Level 4 of South Africa's public health response to COVID-19 include agriculture and construction. These sectors contribute respectively 4.4% and 3.1% to overall employment in South Africa. By the second half of April, more than 65% of businesses in the agriculture sector and more than 80% of businesses in the construction sector were not trading.

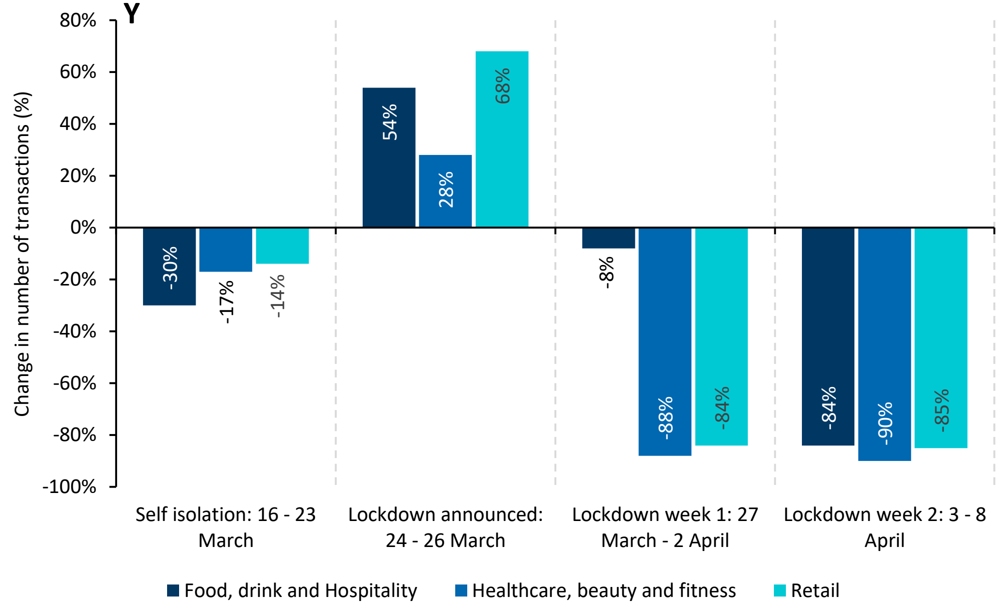
Importantly, all of these sectors contribute towards employment for low skilled workers. These are relatively low paid workers who form part of the "working poor". Loss of employment or decreased wages have significant consequences for this part of the labour force, and leave them particularly vulnerable to poverty.

Small businesses are disproportionately affected by restrictions

Small businesses are particularly hard hit the restrictions placed on economic activity during lockdown and alert level 4. SMMEs simply do not have the cash reserves to withstand protracted lockdown and periods of no revenue. Research based on small businesses in the US show that the median number of cash buffer days for small businesses is 27. Cash buffer days are the number of days of cash outflows that a business is able to pay without any cash inflows. While 27 days is the median for small businesses, this is shorter for businesses such as restaurants (16 days), retailers (19 days), and construction businesses (20 days). This creates significant pressure for SMMEs.

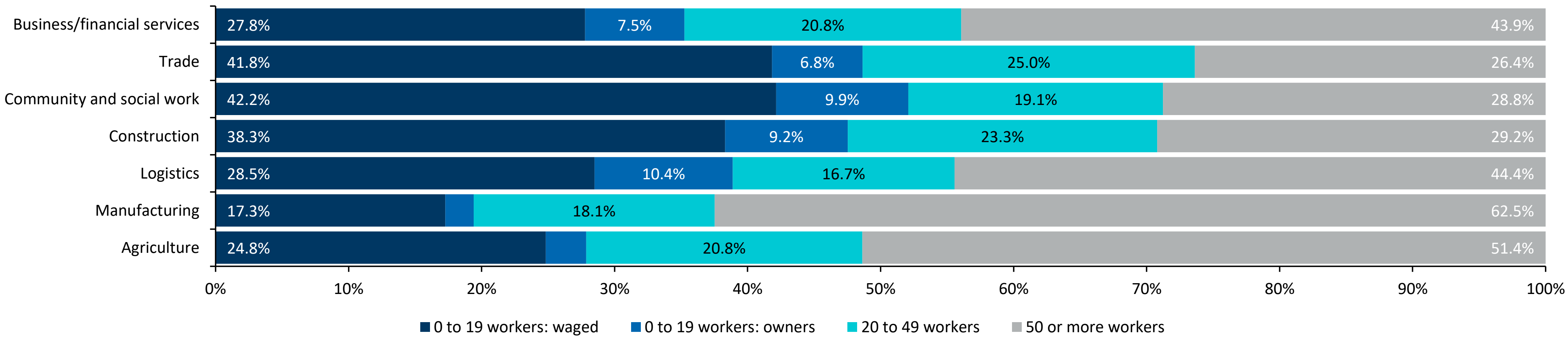
Small businesses are also important employers in the economy. A significant proportion of workers are employed in small enterprises. More than 40% of employees in the retail and wholesale (trade sector) work in enterprises of less than 20 people. Similar proportions of workers in the construction and community and social work sectors are employed in small firms. The impact of COVID-19 for employment in small businesses overall employment in South Africa will be profound.

Change in number of transactions, Y-o-Y



Source: Yoco, 2020

Enterprise size by sector, formal and informal (2019Q4)



Source: Statistics South Africa Quarterly Labour Force Survey, 2019Q4

Macroeconomic impact of COVID exacerbated by tax revenue shortfall

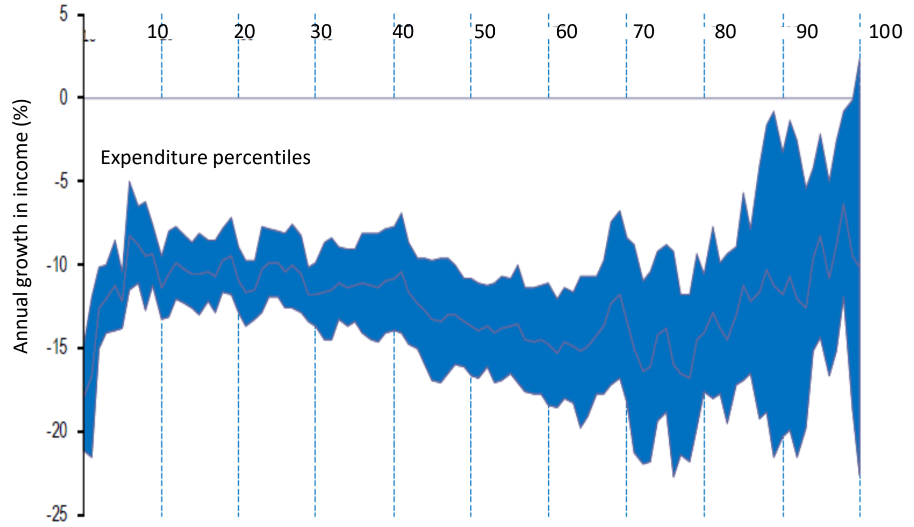
The long term health of the South African economy looks precarious. Estimates of the size of the contraction in GDP in 2020 range from -5.8% (IMF) to -9.5% (Bureau of Economic Research). This is a blow to South Africa's flailing economy and will have significant ramifications both for income of people living and working South Africa, and for the deployment of fiscal resources. Households will become increasingly cash-strapped in a brutal economic climate, which may erode tax compliance, even in instances where tax relief has been granted.

South Africa's fiscal debt currently stands at around 6.83% of GDP. The Development Policy Research Unit (DPRU) at the University of Cape estimates the impact on fiscal debt under different levels of shortfall in tax revenue collection, assuming a 6% contraction in GDP.

Assuming no reduction in revenue collection, fiscal debt is expected to increase to more than 13% of GDP as a result of a 6% contraction in GDP.

SARS Commissioner Edward Kieswetter indicated in May that *"whilst it is early days, our initial view is that revenue performance will be lower than the February [2020] Budget announcement by between 15% - 20%"*. According to DPRU estimates, assuming a 6% contraction in GDP, **this may increase fiscal debt to around 20% of GDP**. This means that an increasing proportion of dwindling tax revenue will need to be allocated to interest payment, leaving fewer resources available to be directed towards social and economic priorities.

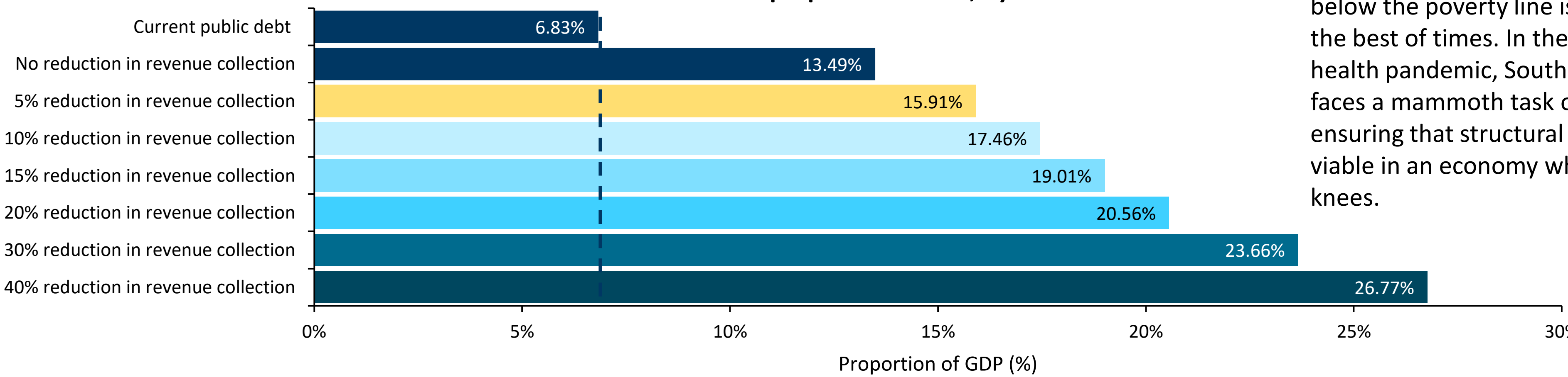
Loss of income by expenditure percentiles



Source: Sulla et al. (April 2020). World Bank

The prospect of rebuilding in a country where more than half of the population lives below the poverty line is overwhelming at the best of times. In the face of a global health pandemic, South African economy faces a mammoth task of rebuilding and ensuring that structural change remains viable in an economy which is already on its knees.

Fiscal debt as a proportion of GDP, by tax revenue shortfall*



*Source: Bhorat et al. (2020); *Assumes contraction in GDP of 6%*

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