




»» South Africa – major challenges in the education sector

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Economic situation

-  Real growth
-  Real public consumption expenditure (var. on prev. year)
-  Inflation rate

Lack of reforms and low commodity prices are hampering growth

Since the financial and economic crisis of 2007–2010, South Africa's economy has experienced relatively slow growth in comparison with large emerging economies. GDP rose at a rate of just under 1 % last year. Lagging reforms and corruption allegations against politicians were partly responsible, weighing on consumption and investment. External impulses have been few because of weak commodity prices. Inflation is relatively high compared with other large emerging market economies.




Growth financing

-  Budget balance to GDP
-  Gross government debt to GDP
-  External debt to GDP

Total debt is still growing

Weak growth is placing strain on the national budget. At the same time, South Africa is grappling with major structural challenges. But instead of solving them, the government is focusing on social transfers. As a result, public debt continues to rise. The backlog of reforms is also hampering long-term economic growth and putting pressure on future state finances. Corporate and household debt levels are also up.




Growth resources

-  Investment ratio
-  Share of services in GDP
-  Labour market participation

Low investment and labour market participation

In 2016 the investment-to-GDP ratio was just under 19.5 %, a low ratio compared with other emerging market economies. But this is not surprising, given the very large service sector and small share of manufacturing. The low level of labour market participation is due to the low female employment rate, which is typical of emerging economies, and the fact that a vast number of youths are no longer available to the labour market because of inadequate skills.

Economic relations with Germany

-  Germany's share of exports
-  Germany's share of imports
-  FDI inflows from Germany

Trade with Germany is an important pillar; FDI is all but insignificant

Germany is an important external market for South Africa. Goods imports and exports play a major role. Direct investment is currently of little relevance. The country's growth weakness and lack of trust in the government have made investors – including those from Germany – less willing to invest.

Legend (see p. 5 for detailed explanation of methodology)

 very good  good  neutral  poor  very poor

Investment climate – assessment by our local experts

South Africa is still scoring points with its very well-developed transport and telecommunications infrastructure. The problem of energy shortages is being gradually defused. The country also boasts a stable financial system and legal framework. However, high political uncertainty, weak economic development, high unemployment and corruption are significantly reducing the quality of the location. This is also preventing significant progress in addressing the sharp social inequalities. Continued on p. 2

Focal theme: major challenges in the education sector

South Africa invests more in education than emerging economies on average (6 % of GDP compared with 4 % (source: UNESCO 2017)). However, the additional expenditure is insufficient to adequately prepare all school leavers for the labour market. This deficit is preventing the country from harnessing the potential of a young population. Its growth weakness is also related to the problems of the education sector. Investors should be prepared to close educational gaps with investments of their own. Continued on p. 2

Investment climate – assessment by our local experts

South Africa still offers locational advantages that are unique to the region of Sub-Saharan Africa. These include, above all, its modern infrastructure. Spanning some 750,000 km, its road network is larger than that of Germany and, based on its surface area, denser than that of Turkey, China or Canada, for example (as at 2015). Mobile telecommunication networks are accessible nationwide. The supply of educational facilities and health services is competitive, although substantial differences remain between the public and private providers. Good public services are also available, for example, in tertiary education and intensive care medicine. The previous power supply bottlenecks are also being gradually resolved. Unfortunately, the momentum once achieved in expanding renewables has come to a standstill.

Other major advantages of South Africa as a business location: the legal system and banking sector. The former includes not just an independent justice system but also well trained lawyers – both are crucial conditions for succeeding as an investor. The banking sector can look back on a long tradition. It is considered to be stable and very well regulated. The Basel III rules have been implemented since 2013. The Tier 1 capital ratio is now 15.2%, according to the IMF (August 2017). The NPL ratio is a surprisingly moderate 2.8% despite the protracted cyclical weakness, which is indicative of the banks' effective risk management systems. The South African Reserve Bank as South Africa's central bank enjoys constitutionally guaranteed independence, which is not being questioned.

Yet South Africa is letting a significant portion of its potential go to waste. Frequent allegations of corruption and bickering across party lines have led to economic policy paralysis. This has caused increased uncertainty, discouraging businesses from investing and considerably

weighing on the business climate. As a result, economic growth is weak and labour productivity is falling. Although South Africa's economy more closely resembles that of an industrialised country than a classic emerging economy and therefore cannot be expected to consistently achieve typical emerging economy growth rates of 4% or higher, its shrinking per-capita GDP increases and even declining per capita incomes (in 2015, 2016 and probably also in 2017) speak volumes. Unemployment has reached alarming levels of 28% overall and 50% among young adults. This also has significant impacts on South Africa's social equilibrium, as social contradictions are mounting. The number of people living in poverty (upper bound poor limit) has been increasing again since 2011 and is around 30 million – more than half the population. Almost half of the 30 million live in extreme poverty (food poor limit).

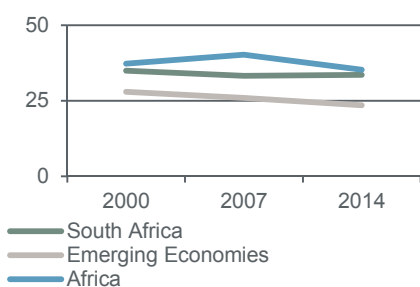
This political-economic situation has caused South Africa to lose international competitiveness as an investment location. On the World Bank's Doing Business Index, South Africa occupies only the 82nd rank after Botswana (of a total of 190, previously rank 74). Its current ranks on the Global Competitiveness Index (61 of 137) and the Corruption Perceptions Index (64 of 176) have also fallen compared with the previous ratings.

In conclusion, South Africa is generally a good location for investment in this region. An efficient political leadership that creates stable and reliable conditions and effectively fights poverty, crime and corruption would encourage more investors to recognise the country's potential and return to harness it. This applies not just to business in South Africa itself, but also with regard to its function as a hub for Sub-Saharan Africa.

Based on an interview conducted with Michael Fischer (DEG South Africa Office Director) on 23 November 2017. ■

Figure 1: Development of student/teacher ratio

Absolute figures



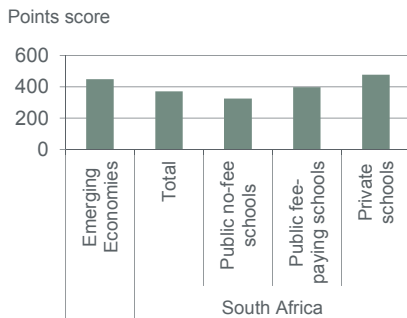
Source: UNESCO

Focal theme: Education sector is facing major challenges – more highly trained graduates are required

Investment in education is inadequate: The average student/teacher ratio in South Africa is worse than the average for emerging economies (see Figure 1). Because the number of students has grown, this situation has hardly improved since the year 2000. The ratio remains on a high level and is more similar to the African average than that of emerging countries. Investment in school infrastructure is too low to ensure that schools across the nation are well-equipped, at 3.3% of GDP in 2015, compared with Brazil (6.2%*), Thailand (5.7%*) and Turkey (10.8%*) (OECD 2017 – * figures for 2013). School experts deplore South African teachers' poor level of training (OECD 2013).

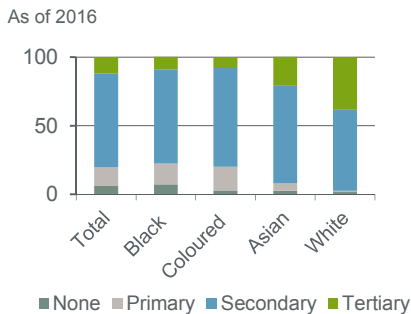
Only few students receive a good education: International comparative assessments such as TIMSS (Trends in Mathematics and Science Study) confirm the problems in the education sector. The basic mathematic

Figure 2: TIMSS (mathematics) 2015 assessment results



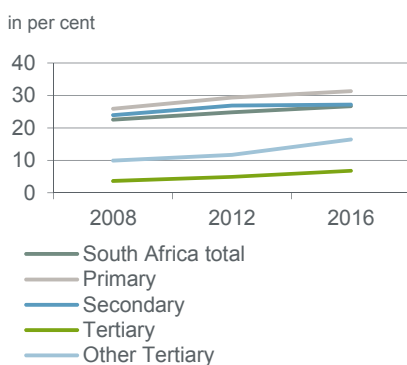
Source: TIMSS

Figure 3: Level of qualification by population group



Source: Statistics South Africa

Figure 4: Unemployment by level of education



Source: Statistics South Africa

knowledge measured in this assessment was below the average level of emerging countries for grade 5 and 9 students (see Figure 2). But the results of the assessment for South Africa also revealed that a portion of students is able to keep up with the international level: mathematic knowledge of students attending a private school or a public school that charges fees is above and just slightly below, respectively, the average level of emerging countries. However, more than 90% of students attend a free public school (Department of Basic Education 2015). These schools are particularly affected by the described lack of investment in education and the shortage of well-trained teachers. Their students' achievement levels are therefore even below the national average. This is particularly true of the black and coloured population. Poverty has become most firmly entrenched in these population groups through apartheid. Lack of economic opportunity and poor education reduce school success and cause students to drop out before they complete the regular 12 years of schooling. The levels of qualification in these population groups is therefore lower. The proportion with no or only primary school education exceeds 20%; among white South Africans that share is only around 2% (see Figure 3).

Share of graduates is too low for an emerging country. In 2015 the proportion of the population with a bachelor degree was around 5%. In Brazil, for example, it was around 13%, in Thailand approx. 12% and in Turkey 14.5% (OECD 2017). The low share of graduates in South Africa is due to the described problems in the education system and the discrimination of the poorer, i.e. primarily black population. Accordingly, this portion of the population is less qualified (see Figure 3). The share of individuals with tertiary education in this group is below that of the white and Asian population.

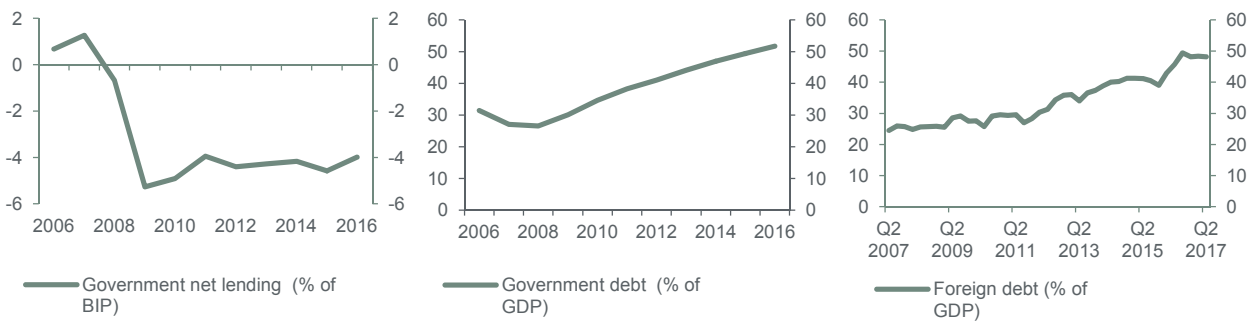
Weak education system contributes to weak growth: As a result of the deficiencies of the education system, individuals without a school leaving certificate or higher education are particularly susceptible to unemployment. Among those with merely primary or secondary school education, the unemployment rate is even higher than the already high national average (see Figure 4). The unemployment rate of graduates and persons with an upper-secondary school leaving certificate, in turn, is much lower. Much indicates that the country's low growth rates are also related to the problems of the education sector, particularly given the frequent reports lamenting the lack of skilled workers (OECD 2013). The ongoing brain drain is further exacerbating this skills shortage. South Africa's economic weakness is encouraging this trend. The deficiencies in the education sector are preventing the country from harnessing the potential of a young population. Enterprises looking to do business in South Africa should be aware of this bottleneck and be prepared to fill the educational gaps in the workforce with investments of their own where appropriate. ■

Figures

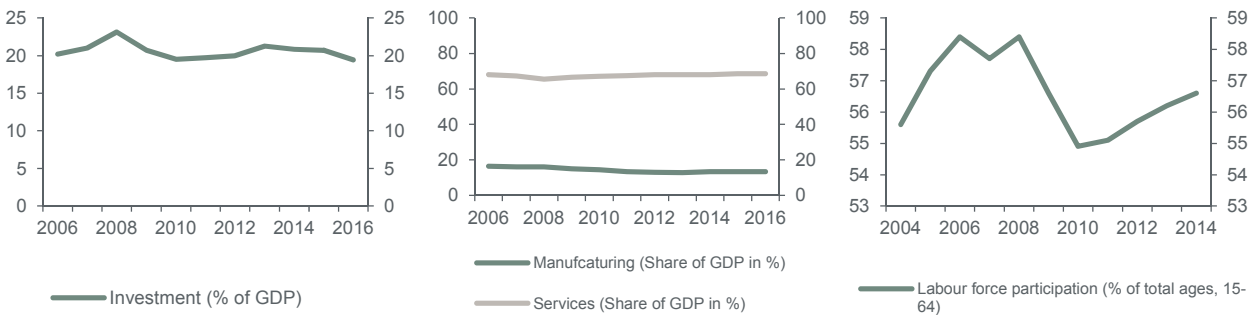
Economic situation



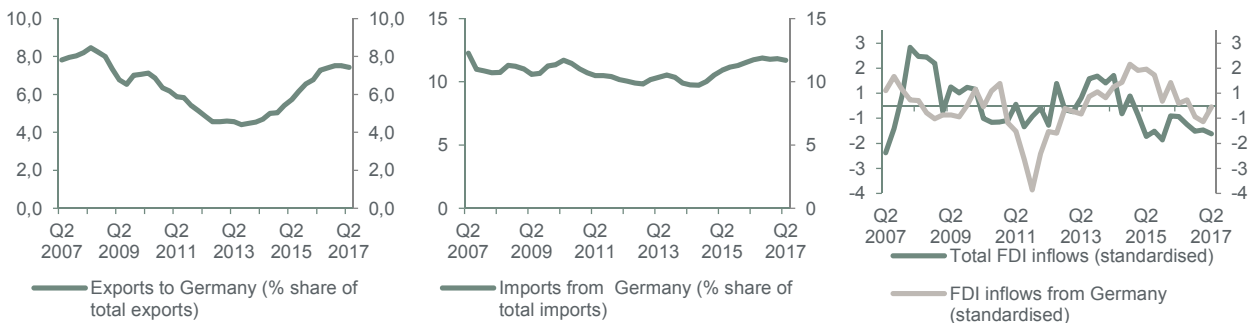
Growth financing



Growth resources



Economic relations with Germany








KfW Research

Emerging Markets Spotlight

Methodology

In the Emerging Markets Spotlight, a selected country is analysed based on various macroeconomic indicators. These indicators are grouped into four categories: economic situation, growth financing, growth resources and economic relations with Germany.

 Quintile 1	The indicators are used to compare the country's situation with its peers. The group comprises Brazil, China, India, Indonesia, Mexico, Russia, South Africa and Turkey. The comparison is based on a quintile ranking in five categories, which are labelled in different colours (see chart):
 Quintile 2	
 Quintile 3	The country is assigned to a quintile of the country group for each indicator analysed. The best quintile may be different for each indicator. For example, higher growth rates are better, so here the upper quintile is coloured dark green, but higher debt rates are a negative factor, so here the upper quintile is coloured dark red.
 Quintile 4	
 Quintile 5	

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