INSTITUTE FOR ECONOMIC JUSTICE
RESEARCH POLICY ADVOCACY

JOBS SUMMIT POLICY BRIEF SERIES

August 2018

STREAM 1, POLICY BRIEF 3

FINANCIAL SECTOR

Policy brief prepared for the Labour Caucus in the Jobs Summit Economic Sector Interventions working group by the Institute for Economic Justice (IEJ).

Stream: Economic Sector Interventions Stream, brief 3

IEJ Collaborator: Gilad Isaacs

Institute for Economic Justice

1. NATURE OF THE PROBLEM

The South African financial sector has seen significant expansion over the last two decades and finance has come to play a more important role in the economy and the lives of South Africans. This is witnessed in: the growth rate of the financial sector's GVA and capital stock that well exceeds GDP growth rates; the volume of debt in the economy; employment in the financial sector; the local and international trading of rand assets; large appreciation on the JSE; indebtedness of households; and the increasing role of non-financial corporates in financial markets, amongst other indicators.

Despite this, the extent to which the expansion of finance has had a beneficial jobs-enhancing impact on the South African economy is questionable.

Some potential reasons why include: the channelling of funds away from real fixed investment and into financial markets and financial products; the negative role of short-term capital flows; volatility and appreciation in asset prices; over-indebtedness; a funnelling of highly skilled individuals (such as engineers) into the financial sector; facilitating capital flight; and a reinforcing the existing growth path.

2. PREVIOUS AGREEMENTS BY SOCIAL PARTNERS TO ADDRESS THE ISSUE

Financialisation has not been adequately addressed by the social partners together or separately.

3. PROPOSALS

There is a growing body of international evidence (including from the IMF) that "too much finance" is bad for the economy. There is also strong evidence that the expansion of finance in the ways described above ("financialisation") reduces investment in the real economy, and exacerbates poverty and inequality.

Few of the measures below have been implemented in South Africa and less-binding approaches, such as via the Financial Services Charter, have failed. Many of these measures have however been experimented with internationally or were common practice in the post-war period.

The proposal includes:

1. Shift patterns of bank lending (we have witnessed a fall in lending – as a share of total loans and deposits – to non-financial corporations by the major banks)

   a) Impose lending requirements on the major banks

   b) Support a more diverse banking sector, including local and cooperative banks

   c) Cap user fees

   d) Further limit the financial market investment activities of commercial banks

2. Make finance cheaper

   a) Reduce the interest rate spread (which is very high in South Africa), if necessary via offering state-financed lending to create competition in the market

b) Reduce the cost of lending from quasi-state financing institutions such as the Industrial Development Corporation (IDC) and Development Bank of Southern Africa (DBSA) through government funding (or government-backed funding) and strengthen their developmental mandate (see Policy Brief 1.4: Reorienting DFIs to Play a Stronger Role in Job Creation)

3. Stabilise financial flows

a) Implement limited capital controls (such as minimum stay requirements) and reduce interest rates to reduce short-term speculative flows

i) Straightforward taxes or withholding taxes on transactions, foreign borrowing, and foreign investment in local bonds (for example, Brazil in 2009–12 and Thailand in 2010) – taxes on targeted types of capital flows

ii) One important tax is a "Tobin tax" – a tax imposed on financial transactions

iii) Controls on swap and forward-cover transactions (for example, Indonesia, Malaysia, and the Philippines in the early 1990s) – limits speculative trading of rand assets

iv) Minimum offshore borrowing or holding periods (for example, Indonesia in 2010 and Thailand in 1996) – limit short-term offshoring borrowing by banks that is often channelled into asset markets.

v) Unremunerated reserve requirements (URR) on investments of less than a minimum holding period and higher reserve requirements for foreign currency liabilities (for example, Chile in 1991–98 and Peru recently) – compulsory non-interest-bearing deposit in foreign currency to be lodged with the Central Bank for a set period (e.g. one year) in an amount proportional to the size of the inflow so that the additional cost discourages external financing entering through identified channels covered by the mechanism

vi) Limit use of "sterilisation" of capital flows as this bears significant fiscal costs and further encourages short-term capital inflows

b) Encourage greenfield FDI through various state incentives

c) Make South African government bonds lends less attractive as targets of carry trade by lowering interest rates

d) Curtail capital flight and tax evasion through stricter controls and oversight (see Policy Brief 2.3: Tax)

4. Reduce incentives for the focus on "shareholder value maximisation" to mean inflating stock prices and distributing dividends so that these funds can be used for long-term investment

a) Restrict the use of share (and other) incentives as components of executive pay

b) Provide tax incentives for spending on labour costs

c) Ban share buybacks

Increase capital gains and other wealth taxes, including by instituting a net wealth tax

d) Encourage shareholder activism, particularly via union investment funds and the Public Investment Fund (PIC) to ensure that decisions taken by firms channel funds towards long-term investment in the economy

4. JOBS IMPACT

The proposals above argue that through various regulatory means finance can play a pro-active role in expanding the economy, in particular sectors of the economy that can be labour absorbing.

The proposals could also have dynamic effects on the economy, stimulating GDP growth, and help shift the economy away from a highly concentrated, capital intensive, monopolistic, mineral and finance centric growth path.

5. FINANCING AND SOURCES

Most of the policies above would require changes to government legislation or regulations. Certain direct financing, for example capitalisation of the IDC, would require direct state support (see Policy Briefs 1.4: Reorienting DFIs to Play a Stronger Role in Job Creation; 2.3: Tax; 2.4: Macroeconomic; 2.4a: Monetary for financing options).

6. ROLE OF STATE INSTITUTIONS AND SOCIAL PARTNERS

The above approaches would need to be undertaken through government regulation. However, the business sector has a role to play in finding ways in which finance is channelled towards productive, growth-enhancing activities. Labour, and labour investment funds, can play an important role by exercising oversight over the decisions of companies within which they invest; such funds could also be used to start local and cooperative banks focused on affordable credit and productive investment. The PIC can also play an important role as an activist investor.