

# Examining viable options for STATE PROCUREMENT of services

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The rise of the so-called 'tenderpreneur' has received much attention in the popular media with calls lamenting and questioning the advantages of the current system of public procurement. The alternative seems to suggest direct state procurement of services. Margaret Chitiga-Mabugu makes some suggestions in a new study.

There is increasing public awareness that tenders have created a class of rent seekers, the so-called 'tenderpreneurs'. These sentiments allude to some of the inherent weaknesses of the tender process to procure government services. These concerns can be framed into three arguments in favour of the direct provision of services by the state.

The first of these arguments relates to the perceived role of government; arguing that by calling for tenders the state has effectively abandoned its responsibility in the provision of basic services. The second argument asserts that tenders are responsible for corruption (rent seeking), whilst the third argument affirms that reducing every government service to a tender reduces the state's ability to create jobs.

Much has been written on the first two arguments, especially on corruption in public procurement and the mechanisms needed to prevent it from happening. However, very little has been done to test the validity of the third argument, particularly in a country like South Africa where the challenges of widespread unemployment demand the effective use of every rand spent.

To this end, the HSRC undertook a study to address the third argument. Specifically, it sought to assess the employment impact of shifting production from private providers to the state.

## The developmental aspect of public procurement

Although public procurement has come under the spotlight, in South Africa there is an argument that government procurement can be used to leverage employment and to create a more inclusive post-apartheid business landscape. This can be done by targeting and giving preference to suppliers

from previously disadvantaged groups and those companies that meet a range of black economic empowerment (BEE) objectives.

To this end, government procurement can be seen as taking a developmental role, a line of argument that is consistent with the notion of a developmental state. In such an instance, proponents of job creation through public procurement will caution that policymakers should be wary of claims about direct state provision creating 'more jobs' than procurement through tenders.

## Direct state provision vs. tender procurement

This dichotomy raises the possibility of different employment effects from the two methods of service provision. There is a perception, at least in the public debates in South Africa, that the mode of delivery itself can contribute to employment creation. We could characterise this view as microeconomic.

It is sometimes felt that different patterns of delivery modes of direct state service provision have different consequences for employment creation and that government should use its own machinery as a tool to tackle unemployment. Although this view is not widely found in the literature, partly because of a general scepticism among economists that the effects will be insignificant and that there are huge problems of government failure, it nevertheless merits consideration. Even if this option has relatively little impact on job creation, it will be an important finding, making clear the limits of microeconomic intervention.

There is prima facie plausibility in the argument as, while many of South Africa's economic problems emanate from the

size of the budget deficit, levels of unemployment cannot be explained simply by inadequate aggregate demand. From a macroeconomic point of view, an additional rand of domestic expenditure has the same impact regardless of where it is spent and by whom.

However, it is likely that a given amount of public money spent on, say, tenders will have a different impact on national employment than when spent on, say, education or agricultural extension directly. The difference will depend on the linkages between the receiving sector and the rest of the economy, the effects on demand and consumption patterns, the consequences for imports and exports and so on.

## Modelling public procurement

This study looked at the extent to which government could create more jobs by shifting from a system of public procurement to direct state provision of goods and services. A computable general equilibrium (CGE) model was used to simulate a shift from public procurement to direct state provision.

CGE models are well suited to analysing counterfactuals and provide a laboratory where impacts can be traced throughout the economy. While a partial equilibrium framework, such as a cost-benefit analysis, can give some insights into the impact of such a shift, it will not tell us what the net impact on the whole economy might be.

The central argument addressed by the study was the claim that arose from public debate which asserted that reducing every government service to a tender reduces the state's ability to create jobs and enriches a few. The study modelled the reduction in government procurement for a few services such as the construction of roads.



### Results

The results of the study showed that, given government's existing skills composition, there is a relatively larger increase in the demand for semi-skilled and high skilled labour with a corresponding increase in the income of the households that receive factor payments from these workers. Thus low income households do not benefit from the shift. The private sector demand for labour falls, for all skill categories, in road construction and the sectors that supply its intermediate inputs. In addition, due to broader economy-wide adjustments, the demand for low skilled labour also falls in gold, other mining, wood, metal products, machinery and equipment and electrical machinery sectors.

For the rest of the sectors, demand for labour increases relative to the base scenario. The results suggest that a shift away from

public procurement to direct state provision negatively affects employment in the private sectors where government used to procure its goods and services. However, this fall in labour demand in roads and its related sectors is outweighed by the increase in demand for labour in all the remaining sectors, stimulated by the increase in government activities, and the net effect is an increase in the aggregate demand for labour for the whole economy as seen in Table 1 below.

The employment impacts are driven by the fact that government is assumed to use its current labour skills composition. The effects of relaxing this assumption are not assessed in this study; allowing government to change its skills composition would probably alter the change in the pattern of demand for both skilled and unskilled labour.

### Policy implications

The results of the study indicate that there are some trade-offs. Due to broader economy-wide adjustments, employment is negatively affected in the private sectors that used to provide road construction services to government. Although the shift seems to create some positive impacts, the disproportionate impact on household income that benefits middle and high income households more than their low income counterparts, has serious implications for income inequality. This means that such a policy intervention would not be pro-poor unless the skills composition of government employment was to change.

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**Table 1: Change in total demand for labour, by skill level**

	Business as usual	No procurement (Roads)	% variation
Total			
High skilled labour	244 027	248 210	1.7
Semi-skilled labour	286 689	291 605	1.7
Low skilled labour	161 340	161 867	0.3
Informal skilled labour	36 039	36 039	No change

Source: Simulation results

The report *Direct State Provision of Goods and Services vs. Tender Procurement*, by Margaret Chitiga-Mabugu, M, Stewart Nanda, Ngandu and Vandyayi Mbanda is available on



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