

November 1, 1982 - 82/195

Statement by Mr. Brand on South Africa
Executive Board Meeting 82/140
November 3, 1982

The South African economy has been experiencing a large deficit in its external accounts since the early part of 1981. In order to finance this deficit the foreign exchange reserves were allowed to fall to a relatively low level and extensive foreign borrowing was undertaken, mostly on a short-term basis. When it became clear that the external environment was likely to remain unfavorable for some considerable time yet, my authorities progressively introduced strong corrective measures which to a large extent have been formulated with the benefit of very useful consultations with the Fund staff.

However, the large external imbalances have persisted and in view of the rapid accumulation of short-term external indebtedness, my authorities have decided recently to strengthen their adjustment efforts further while at the same time applying for use of the Fund's resources.

In his letter to the Managing Director, my Minister of Finance has indicated the reasons which have led to the severe deterioration in South Africa's balance of payments position over the last two years and has outlined the adjustment program which my authorities are implementing in order to restore equilibrium in the external accounts. The adjustment program is fully detailed in the memorandum on South Africa's economic policies and analyzed carefully and objectively by the staff in the excellent papers they have submitted to the Board. I, therefore, do not consider it necessary to dwell on this program at any length. I propose instead to limit myself to informing Directors of the latest developments in the South African economy and also to briefly report on recent policy measures not covered in the staff papers.

However, I would like to take the opportunity to make a few remarks about the severity of the adjustment program which my authorities have put in place, as well as the conditions which will apply if South Africa's requests for use of Fund resources are approved. These adjustments and conditions, one and all, are by any standards very onerous and will no doubt require important sacrifices from all the sectors of the South African economy. My authorities are, nevertheless, fully prepared to abide by them because of their serious determination to redress as soon as possible the undesirable developments which have occurred in the balance of payments and reserve position in the economy over the past two years. Moreover, my authorities have asked me to state to the Board their readiness to take immediate further steps should developments beyond their control indicate a need for further action.

Recent developments

Money and banking: At a seasonally adjusted annual rate M1, M2, and M3 increased by 24.1, 19.1, and 14.6 per cent, respectively in the period January to the end of August 1982, compared with increases of 34.1, 25.1, and 20.2 per cent for calendar year 1981 as a whole. The satisfactory outturn in respect of broad money (M3) must largely be attributed to the successful application of market-oriented methods of monetary policy, including the sale of large amounts of government stock to the nonbank private sector both through a new tender system and through sales by the Reserve Bank of stock obtained on "tap" from the Treasury. Bank credit to the private sector at a seasonally adjusted annual rate showed a 21.0 per cent increase in the same period, i.e., January to end-August 1982, compared with a 35.1 per cent increase for 1981 as a whole.

Government finance: Issues from the Exchequer account (adjusted for changes in the balance on the Paymaster-General Account) increased by 16.6 per cent in the first half of the 1982/83 fiscal year compared with the corresponding period in the preceding year. The main budget provided for an increase of 11.5 per cent in expenditure for the 1982/83 fiscal year as a whole. This compares with an increase of 17 per cent in Exchequer receipts in the first half of the 1982/83 fiscal year (compared with the corresponding period in the preceding year) and an increase of 11 per cent foreseen in the budget for the fiscal year as a whole. The relatively high rate of increase in Exchequer issues early in the fiscal year is, however, not a cause for concern since experience in previous years has shown a sharp decline in the rate of expenditure in the latter part of any fiscal year. The deficit of R 1394 million during the first five months of the 1982/83 fiscal year was financed as follows:

Public Debt Commissioners:	R 348 million
Nonbank private sector:	R 1,449 million
Monetary banking sector:	R -530 million
and foreign sector:	R 127 million

Selected interest rates: The rate on three-month bankers' acceptances, which on September 3, 1982 stood at 17.00 per cent, increased to 17.35 per cent on September 24, before easing to 16.00 per cent on October 29. The Treasury Bill rate also reached a peak of 16.35 per cent on September 24 before showing a slight decline to 15.44 per cent on October 29. The secondary market yields on long-term government stock showed averages of 14.09 per cent and 12.72 per cent in August and September, respectively. The moderate declining trend in interest rates does not reflect a relaxation in monetary restraint, but is rather an indication of a decline in the demand for funds as a result of the slowdown in domestic economic activity.

Price changes: At the end of September 1982 the year-on-year rate of increase in consumer prices was 14.1 per cent compared with 13.9, 14.4, and 16.0 per cent in the 12-month period ending August, July, and June

1982, respectively. Although the increase in the general sales tax from September 1 has increased the rate of inflation slightly, it is not expected that this development will make a revision of the projected rate in the staff report necessary.

Output and demand: Reflecting the present economic downswing, the increase in real gross domestic product slowed down progressively during the first half of 1982. Available information for the third quarter indicates that real output in important sectors of the economy, such as manufacturing and mining, fell below the corresponding levels in 1981. Compared with the corresponding period of 1981 real gross domestic expenditure showed a decline in the second quarter. On the same basis decreases were recorded in the third quarter in important expenditure components such as wholesale and retail sales and the number of new motor vehicles sold.

Recent policy changes

The South African Reserve Bank announced on September 27, 1982 that the supplementary minimum reserve balances which banks in South Africa are required to hold with the Reserve Bank against their short- and medium-term liabilities to the public had been reduced, and that a reduction had also been made in respect of required liquid asset holdings or required balances with the National Finance Corporation.

Based on the figures for the end of August 1982 the total reduction in minimum reserve balances with the Reserve Bank stemming from the aforementioned changes, was expected to amount to approximately R 422 million at the end of September 1982. The main objective of these changes, which did not signify any relaxation of the bank's present restrictive monetary policy, was to prevent an undue further tightening of monetary conditions. Such a tightening of monetary conditions has already been achieved through the considerable success which the authorities had in selling marketable government stock at market determined interest rates, both through the new tender system and through open market sales by the Reserve Bank of government stock obtained on "tap" from the Treasury. For instance, in the period August 1 to October 15 net sales of government stock by the Reserve Bank amounted to R 1,013 million, which was more than the amount of R 750 million taken up on "tap" from the Treasury. Of these sales R 882 million represented sales of long-term stock and the balance of R 136 million, short-term paper. In addition, the Treasury made a successful issue of long-term government stock for R 200 million on October 12, payment for which will be made in November. The large new issues and net sales of government stock will enable the authorities to finance the budget deficit projected for 1982/83 entirely outside the banking system. In fact, during the first half of the fiscal year not only the full amount of R 800 million provided for in the budget to be financed from new government stock was obtained, but additional net issues of government stock amounted to about R 960 million. In this way it has made a very important contribution to the progress that has been achieved

in bringing the money supply under proper control. I should also like to add that the heavier reliance on open-market operations as an instrument to control the money supply and the corresponding lesser emphasis on direct control measures are fully in line with the more market-related approach to monetary control which the De Kock Commission is expected to recommend when it submits its report early in 1983.

It may also be mentioned that the Reserve Bank at the end of August 1982 introduced a new pattern of rates for forward cover which no longer provide any special incentive for capital imports. This change encouraged exporters to increase their cover and importers to take less cover than had previously been the case and has already resulted in a substantial decline in the open position in the Reserve Bank's forward cover book.

Balance of payments

The balance of payments situation has begun to improve partly in response to the measures that my authorities have taken with a view to eliminating excess demand pressures. The deficit on the current account of the balance of payments at a seasonally adjusted annual rate declined from R 6,890 million in the first quarter of 1982 to R 5,400 million in the second quarter. A further decline is expected in the third quarter on the basis of preliminary results which are available, inter alia, in respect of imports and exports in July and August of 1982. Although the balance on current account is expected to improve further after the third quarter, the overall payments deficit is likely to remain sizable at least through the middle of 1983.