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EBD/85/313

December 16, 1985

To: Members of the Executive Board
From: The Secretary
Subject: South Africa - Exchange Control Regulations

The Fund has received the following statement issued by the South African Minister of Finance on December 6, 1985:

The surplus on the current account of South Africa's balance of payments increased further during the third quarter of 1985 to a seasonally adjusted annual rate of R 6.9 billion. This is equivalent to 5.8 percent of gross domestic product--a very high ratio by historical and international standards. The latest foreign trade statistics indicate that this surplus was maintained, if not increased still further, during October. However, as a result of continued pressure on the capital account of the balance of payments the rand has remained around a level of between 36 and 39 U.S. cents during recent months.

To reduce this pressure a "standstill" in respect of certain foreign debt repayments was announced on 1 September 1985 and the existing exchange control over residents was supplemented by the reimposition of exchange control over non-residents (the financial rand system).

To supplement these measures it has now been decided to take certain steps to ensure the more effective application of existing exchange rate and exchange control procedures and to introduce certain exchange control restrictions:

1. Spot exchange market

The existing arrangements with regard to the spot foreign exchange market will remain unchanged. This includes the existing limits imposed by the Reserve Bank on the daily foreign exchange holdings of authorized dealers, on the total amount of foreign loans which a bank may enter into for its own account (10 percent of its total liabilities to the public), and on a bank's net open foreign exchange position (10 percent of its paid-up capital and reserves). Authorized dealers are reminded of the requirement to comply fully with these limits.

2. Forward exchange market

- 2.1 The mechanism regarding the "swap" market whereby authorized exchange dealers (banking institutions) may currently purchase U.S. dollars from and sell U.S. dollars within set limits to the South African Reserve Bank for further delivery also remains unchanged.
- 2.2 In order to limit the Treasury's risk arising from the provision of forward cover, the Reserve Bank will continue its policy, as announced in August 1983, of gradually reducing the maximum net amount that authorized dealers can buy from or sell forward to the Bank by means of swaps. For the year to 31 August 1983 the total amount of this exposure for all authorized dealers together was fixed at US\$10 billion. On 1 September 1984 it was reduced by one third. It will now be reduced by another third with immediate effect. As planned, the Reserve Bank's obligation to supply forward cover to authorized dealers will lapse on 31 August 1986. Should any problems arise in this regard as a result of the new arrangements relating to the forward cover of export proceeds as set out in paragraph 4.5 of this statement, the Reserve Bank will be prepared to consider individual applications on merit.
- 2.3 As in the past, the Reserve Bank will, in exceptional cases and at its sole discretion, also enter into outright forward exchange purchase and sale contracts with authorized dealers against documentary proof that the underlying transactions are customer-based. Such deals will be done for maximum amounts of US\$10 million per deal.

3. Payment to gold mines

With effect from 9 December 1985 the Reserve Bank will pay the gold mines in rand on the day of purchase for all gold bullion sold by them to the Bank, and not half in rand and half in U.S. dollars as in the past.

4. Exchange control

- 4.1 Transfer to Reserve Bank of Accounts paid to special restricted accounts

In terms of the Exchange Control Regulations, 1961, as amended, all authorized dealers shall forthwith transfer to and deposit with the Reserve Bank all amounts

paid to "special restricted accounts" (as defined in regulation 4 A of the aforesaid Regulations) held with them under the debt standstill arrangements.

4.2 Documentary evidence

Inspections undertaken by the Exchange Control Department of the Reserve Bank have revealed that in some instances authorized dealers have been entering into foreign exchange transactions with their customers in disregard of the requirement to call for documentary evidence in support of such transactions. Such negligence is viewed in a serious light, and authorized dealers should at all times comply fully with this existing requirement.

4.3 Proceeds of exports

In terms of the Exchange Control Regulations, South African exporters may grant extended payment terms to overseas buyers for a period of up to six months from date of shipment of the goods. In exceptional cases, authorized dealers may authorize their customers to grant export credit of up to a maximum of twelve months. While exporters may therefore grant credit to overseas buyers, they may not retain export proceeds abroad for the periods mentioned above, but are required in terms of the Exchange Control Regulations to sell to an authorized dealer such proceeds within a period of seven days from the date of receipt thereof. The evidence suggests that some exporters have been granting credit to foreign buyers beyond the normal permissible period of six months and that others have not been adhering to the prescribed period of seven days within which they have to account for their export proceeds.

It will be appreciated that such actions constitute a direct contravention of the Exchange Control Regulations which would render the parties involved liable to prosecution. The Control will in future monitor export credits and payments more closely and will shortly hold discussions with authorized dealers regarding the existing reporting procedures in this regard. In the meantime, authorized dealers will serve the best interests of their customers by bringing the obligation imposed on exporters by the Exchange Control Regulations pertinently to their notice.

4.5 Compulsory forward cover for exports

With effect from Monday, 9 December 1985, it will be mandatory for exporters who do not sell "spot," to cover forward their total export proceeds within a period not later than seven days after date of shipment.

Importers are not affected by this requirement.

4.6 Inter vivos trusts

The Exchange Control acknowledges that inter vivos trusts are established inter alia for estate planning purposes. It has come to the Control's notice, however, that such trusts are sometimes used as a channel to export capital from the Republic. With effect from 9 December 1985, therefore, income accruing to nonresidents, including former residents, from such trusts may only be transferred through the medium of financial rand.

Immediate steps will be taken to amplify the frequency and extent of inspections covering all aspects of exchange control. Transgressions of the exchange control regulations are already subject to severe penalties. The authorities will not hesitate to protect South Africa's interests with appropriate action where necessary.

The measure regarding transfers from inter vivos trusts appears to be a modification of an existing multiple currency practice and may involve Fund jurisdiction under Article VIII, Section 3 of the Articles of Agreement. The staff will seek clarification on these and other related matters during the next Article IV consultation discussions scheduled for around May 1986.

The staff understands that a proposal by South Africa for a longer-term arrangement for the repayment of its foreign debt is being submitted to major creditor banks. In his statement of December 10, 1985 the Chairman of the South African Standstill Coordinating Committee announced that:

In the meantime, it is necessary to extend the present standstill from 31 December 1985 to 31 March 1986. It is believed that this should give the Standstill Coordinating Committee, the Mediator, and the Foreign Creditors of South Africa sufficient time to come to an acceptable arrangement for the gradual withdrawal of the restrictions now in force on the redemption of the foreign debt.

Various submissions were recently made to the Standstill Coordinating Committee for the exemption of certain credits and certain creditors from the standstill restrictions. In particular, nonbank creditors of, and certain holders of very short-term deposits with, South African banks, now subject to the redemption restrictions, have appealed to the Standstill Coordinating Committee for special concessions. In view of the continuing pressure on the South African foreign exchange market and also of the stage now reached in the negotiations with foreign creditors, it has been decided to retain the standstill for the extended period more or less in its present form. In seeking a longer-term formula for the management of South Africa's foreign debt, special attention is, however, being given to these various groups of creditors and efforts are being made to find ways and means of accommodating at least some of their requests.

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