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INTERNATIONAL MONETARY FUND

SOUTH AFRICA

Selected Issues

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South Africa: Basic Data

Area	1.2 million square kilometers
Population (1996)	43.5 million
Population growth rate (1996)	2.0 percent
Employment in the nonagricultural sector	5.2 million

IMF Position (April 30, 1997)

Quota	SDR 1,365.4 million
Funding holdings of rand	SDR 1,902.94 million
Holdings of SDRs	SDR 0.68 million
Exchange rate	US\$ 1 = R 4.44

	1996	1992	1993	1994	1995	1996
	In millions of rand at current prices	(Percentage change at constant prices)				
<u>National accounts</u>						
Private consumption	330,476	-1.4	0.3	3.1	4.7	3.8
Public consumption	113,237	1.5	2.9	4.2	0.3	5.0
Gross fixed investment	92,557	-5.3	-2.8	8.7	10.3	6.8
Total domestic demand 1/	541,681	-1.4	1.5	5.8	5.5	3.3
Exports of goods and services	143,682	2.5	4.8	1.0	9.3	7.8
Imports of goods and services	139,647	5.3	7.0	16.1	16.6	7.5
Gross domestic product	543,014	-2.2	1.3	2.7	3.4	3.1
<u>Prices and wages</u>						
Consumer prices, annual average		13.9	9.7	9.0	8.6	7.4
GDP deflator		12.4	11.1	9.5	8.9	8.4
Remuneration per worker 2/		15.1	10.3	11.9	9.4	10.2
(In billions of U.S. dollars)						
<u>Balance of payments</u>						
Merchandise exports (non-gold)		17.2	17.3	18.3	22.4	23.0
Gold exports		6.8	6.9	6.7	6.2	6.1
Merchandise imports		18.2	18.3	21.5	27.0	27.1
Services and transfers, net		-4.0	-4.0	-3.8	-4.4	-4.0
Current account balance		1.7	1.9	-0.3	-2.8	-2.0
(In percent of GDP)		1.5	1.6	-0.3	-2.1	-1.6
Long-term capital, net		-0.5	-0.1	1.0	4.2	1.1
Short-term capital, net 3/		-1.1	-4.6	0.2	1.1	-0.2
Capital account balance		-1.7	-4.7	1.2	5.3	0.9
Gross official reserves		3.0	2.7	3.1	4.3	2.2
In months of imports		1.8	1.4	1.4	1.6	0.9
Net official reserves		2.7	0.3	0.9	3.5	1.6
In months of imports		1.6	0.2	0.4	1.3	0.7
(In billions of rand)						
<u>Government finances</u> 4/						
Revenue		82.8	96.9	112.2	125.9	146.1
Expenditures		111.4	122.1	137.0	151.7	177.4
Balance		-28.5	-25.2	-24.8	-25.8	-31.3
(In percent of GDP)		-8.2	-6.4	-5.5	-5.2	-5.6
(Annual percentage change)						
<u>Monetary aggregates</u> (end-period)						
Broad money		8.0	7.0	15.7	15.2	13.6
Bank credit to private sector		8.7	9.7	17.0	17.6	16.1

Sources: Data provided by the South African authorities; IMF, International Financial Statistics; and Fund staff estimates.

1/ Excludes statistical discrepancy.

2/ Nonagricultural sector.

3/ Includes errors and omissions of current as well as capital account.

4/ Fiscal year beginning April 1, cash basis, excluding special receipts and payments.

I. RECENT ECONOMIC DEVELOPMENTS

A. Introduction

1. Aided by the easing of political uncertainties after the national elections in early 1994 and by the cautious stance of policies adopted by the new administration,¹ economic performance and investor sentiment strengthened markedly. Nonagricultural value-added grew by 4 percent in 1995—led by a sharp increase in real gross private fixed investment—inflation, long-term yield differentials, and the net open forward position of the South African Reserve Bank (NOFP) fell considerably,² and the rand appreciated by 5 percent in real effective terms in the second half of the year. However, private nonagricultural employment plateaued in mid-year and fell thereafter (Figure 1).

2. In contrast, developments in 1996 were characterized by a shift in investor sentiment and unrest in the foreign exchange markets. These were brought about initially by unfounded rumors about the President's health and speculation regarding a wholesale removal of exchange controls on residents. It was subsequently reinforced by growing concerns about the course of financial and structural policies. The turnaround in investor sentiment was reflected in the depreciation of the rand—by some 21 percent in nominal effective terms and 15 percent in real effective terms over the twelve-month period to end-December 1996 (Box 1 and Figure 2). In this context, economic growth slowed, inflation rebounded, and the fall in private nonagricultural employment continued. In an effort to rebuild confidence, the authorities announced the Growth, Employment and Redistribution (GEAR) strategy in June 1996 (Box 2).

B. Real Sector Developments

3. Real GDP grew by 3.1 percent in 1996, buoyed in the main by a rebound in agricultural output (see below), moderately below the 3.4 percent growth in 1995. The expansion in real GDP exceeded the annual population growth rate, which is about 2 percent, for the third consecutive year. All components of domestic demand registered relatively robust

¹These policies consisted of phased reforms—based on social consensus and the constitutional independence of the Reserve Bank—including annual half-a-percentage point of GDP reductions in the fiscal deficit, an eight-year program of trade liberalization, step-by-step liberalization of foreign exchange controls, a four-year program to reform labor law and promote worker training, and public expenditure reprioritization towards the poor.

²The NOFP is the net oversold forward book of the Reserve Bank, less net international reserves.

FIGURE 1
SOUTH AFRICA

ECONOMIC INDICATORS, 1990-97

Source: South African Reserve Bank.

1/ Increase means appreciation.

2/ Consumer prices excluding VAT, food, and mortgage interest payments.

Box 1. The Depreciation of the Rand During 1996

The depreciation of the rand during 1996, after trading in a range of 3.60-3.65 per U.S. dollar for two years, was episodic, with periods of stability interspersed with sharp declines (Figure 2).

The perceived inconsistency between the real effective appreciation of the rand in the latter part of 1995 and the rapid growth of the monetary and credit aggregates, coupled with signs of a widening external current account deficit gave rise to concerns that the rand had become overvalued. A tightening of conditions in international financial markets and periodic speculation of accelerated exchange control liberalization on residents compounded these pressures both ahead of and following the initial depreciation. Political uncertainties also contributed to the initial fall, as well as the subsequent declines in April and early May: in mid-February, the President's health was (erroneously) thought to be in doubt; in late March, an ANC member was appointed Minister of Finance for the first time; this was rapidly followed by a sharply polarized debate about economic policy between representatives of labor and business; and in May, it emerged that the National Party would leave the Government coalition. But at each stage after these particular uncertainties were resolved, the rand failed to fully recover, suggesting that more fundamental factors may also have been at work.

Pressures on the rand were reinforced by growing market skepticism about the authorities' intention to halt the depreciation through a forceful tightening of financial policies. Although the bank rate was raised by 1 percentage point to 16 percent in late April, following a particularly sharp decline in the rand, the primary policy response was heavy official intervention in the forward and spot exchange markets.

The presentation of the Government's medium-term framework of "market-friendly" policies in mid-June, the Growth, Employment, and Redistribution strategy (GEAR), provided a brief respite. The rand fell again from mid-July, when apparent inactivity to implement the GEAR resuscitated doubts about policy, and it fell again in late October, when continued evidence of unexpectedly strong monetary and credit expansion overwhelmed the more positive evidence that the government budget deficit for 1996/97 remained on track. Neither further heavy intervention at that point, nor an additional 1 percentage point increase in the bank rate to 17 percent in November, were sufficient to stem or reverse these pressures decisively. By the end of 1996, the NOFP rose to US\$22 billion, about US\$15 billion higher than in mid-February 1996.

In early 1997, however, the rand recovered strongly as confidence in the authorities' fiscal and privatization plans rebounded, evidence of an improvement in the external current account deficit emerged, and capital flows to emerging markets strengthened.

FIGURE 2
SOUTH AFRICA
RAND PER U.S. DOLLAR, FEBRUARY 1996-APRIL 1997

Source: Reuters news service.

Box 2. The Growth, Employment, and Redistribution Strategy (GEAR)

The GEAR was presented to Parliament on June 14, 1996. It firmly reasserted the authorities' market-oriented and consensual approach to policy. Referring to projections reflecting current policy, it underscored the urgency of further action to raise labor-intensive economic growth to address inherited social inequities and the "unemployment crisis." It rejected the introduction of a national minimum wage and an expansionary fiscal policy to achieve these goals, and saw the real depreciation of the rand as growth-enhancing, if sustained by a firm anti-inflationary monetary policy. The GEAR targeted real GDP growth of 6 percent in 2000 and the creation of more than 400,000 jobs in that year, and offered five new sets of policy proposals—in addition to existing commitments to privatization and the reorientation of public spending to the poor—to achieve those goals:

- **Faster fiscal consolidation**, targeting a deficit of 4 percent of GDP in 1997/98, falling to 3 percent of GDP in 1999/2000—½ percentage point of GDP lower than previously targeted for each year;
- **A labor market policy of "regulated flexibility,"** strengthening regulatory protection for workers, scaling down wage floors for trainees and to reflect regional labor market conditions and firm size, broadening official powers to withhold the extension of wage agreements negotiated at sector level, and introducing a payroll levy to fund training;
- **Accelerated tariff reductions** to reduce imported input and consumption goods prices, while avoiding job losses in sensitive sectors;
- **An accelerated depreciation scheme** for new investments in manufacturing, and a tax holiday for new projects in approved areas and industries, based on the share of remuneration in value-added;
- **Further exchange control liberalization** in the context of a gradual process: the cap on foreign assets obtained through swaps was raised from 5 percent to 10 percent of total assets for eligible institutions, institutional investors were allowed to place 3 percent of net inflows during 1995 in foreign assets, and restrictions on foreign investor access to domestic credit were eased.

The GEAR's projections reflecting strengthened policies are as follows:

	1996	1997	1998	1999	2000
GDP growth	3.5	2.9	3.8	4.9	6.1
CPI inflation (period average)	8.0	9.7	8.1	7.7	7.6
Real bank rate (in percent)	7.0	5.0	4.0	3.0	3.0
Fiscal deficit / GDP	5.1	4.0	3.5	3.0	3.0
Non-agricultural employment growth	1.3	3.0	2.7	3.5	4.3
Private formal real wages growth	-0.5	1.0	1.0	1.0	1.0
External current account/GDP	-2.2	-2.0	-2.2	-2.5	-3.1
Real effective exchange rate	-8.5	-0.3	0.0	0.0	0.0

expansions, except for inventories which fell markedly (Appendix Table 1). Real public consumption grew by 5 percent in 1996, compared with 0.3 percent in 1995, reflecting increases in both public sector employment and wages. In contrast, the increase in real private consumption slowed to 3.8 percent in 1996, down from 4.7 percent in 1995, perhaps because the uncertainties that prevailed in the exchange market led to a more cautious attitude among consumers. In particular, real growth in consumption of services and non-durables slowed considerably in the second half of 1996, whereas consumption of durables remained robust throughout the year.

4. Real gross fixed investment increased by 6.8 percent in 1996, compared with 10.3 percent in 1995 (Appendix Table 2). Private investment grew by 6.7 percent—about half of the increase realized in 1995, as activity was adversely affected by economic uncertainty and slower growth in sales of manufactured goods. Investment by public corporations also moderated in 1996, largely owing to a scaling down of capital programs. However, investment activity by public authorities witnessed a strong recovery from a decline of 7.7 percent in 1995 to an increase of 4.4 percent in 1996, as expenditure on projects under the Reconstruction and Development Program (RDP) picked up (see Section I.C). With the exception of the agricultural sector, the buildup in inventories slackened markedly across all sectors, possibly reflecting the large accumulation that had taken place in previous years and higher interest rates. Meanwhile, as part of the GEAR, the authorities instituted measures with effect from July 1996, that are expected to boost private investment. These measures include an acceleration of depreciation allowances for income tax purposes on plant and equipment and on buildings intended for manufacturing activities, and a tax holiday of up to six years for new projects with assets in excess of R 3 million (see Section I.C).

5. Notwithstanding an improvement in government savings, gross domestic savings fell from 16.8 percent of GDP in 1995 to 16.5 percent in 1996, as the savings performance of both individuals and corporations deteriorated. Net foreign savings contracted from 2.1 percent of GDP in 1995 to 1.6 percent in 1996 (Appendix Table 3), reflecting in part a strong performance of the export sector, which benefited from the increased output of the “mega investment projects” (see Section I.E), the rebound in agricultural production, and the depreciation of the rand. At the same time, the slowdown in manufacturing activity resulted in a slower expansion in imports of intermediate goods.

6. On the supply side of the economy, the main source of growth in 1996 was the recovery in agricultural production. Real value added in this sector, which had contracted by 15 percent in 1995 on account of a severe drought, grew by 26 percent in 1996 aided by exceptionally good weather conditions (Appendix Table 5). Although the agricultural sector contributes only 5 percent of total value added, the sector accounted for nearly half of the growth in real GDP at factor cost.

7. The expansion of nonagricultural production registered a marked slowdown in 1996. Real output in the mining sector continued to fall, as the increase in diamond and coal production was more than offset by a decline in gold production, which was affected by

outbreaks of ethnic violence, underground fires, and seismic activities in some of the larger mines. Manufacturing output grew by only 0.4 percent in 1996, compared with 7.6 percent in 1995, owing in part to the slowdown in private consumption and cutbacks in inventory accumulation. The tertiary sector also expanded in 1996 at a slower pace than in 1995. In particular, growth of value added in the commerce sector slackened from 6.5 percent in 1995 to 3.7 percent in 1996, possibly reflecting the increased cost of credit, and growth weakened in the transportation and communication sector as well, notwithstanding increased demand for transportation services arising from the good agricultural season. However, the expansion in the financial services sector remained strong, boosted by the high activity in the foreign exchange, equity, and bond markets.

8. Notwithstanding the further expansion in economic activity in 1996, total employment in the formal nonagricultural sector declined in the first three quarters of the year, after a modest 0.7 percent advance in 1995 (Appendix Table 8). Formal nonagricultural employment fell by some 80,000 (1.7 percent) bringing the total loss in jobs since the peak in 1989 to more than 400,000.³ The loss in jobs in 1996 came entirely from the private sector, which registered a decline of more than 100,000 positions, despite a 2 percent gain in employment (about 6,700 positions) in the services sector. Manufacturing—which is the largest provider of private sector employment—lost some 55,000 positions, and the continued contraction of the mining industry led to a loss of about 19,500 jobs. The drop in employment in 1996 reflected in part the slowdown in growth of nonagricultural output and the persistent rise in real wages (see below). In contrast, public sector employment rose by some 22,000 positions, despite the separation of about 40,000 civil servants at the central and provincial government levels in the context of the three-year civil service rationalization program.

9. The new Labor Relations Act came into effect in November 1996, although the bill was passed by Parliament a year earlier. Its implementation was delayed by the need to put in place the supporting institutions. The Act establishes the basis for a centralized bargaining process on matters pertaining to conditions of service of employees, while protecting them from dismissal in the event of strike action. Under the Act, a Commission for Conciliation, Mediation and Arbitration (CCMA) and a Labor Council have been established. Since then, the CCMA has reportedly contributed significantly to a reduction in the number of man-hours lost through strikes. In the first two months of its existence, 601 disputes were referred to the body for conciliation; 401 of them were settled outright and the balance required additional review work. Meanwhile, the government released in early 1997 the Basic Conditions of Employment bill, which is intended to replace the current Basic Conditions of Employment Act. The bill also seeks to cover the conditions of service for nonunionized workers in the agriculture and domestic service sectors, and part-time workers, who are not effectively covered by the Labor Relations Act. The proposed basic conditions of employment include a reduction in the maximum hours worked per week from 46 hours to 45 hours, an increase in the overtime pay rate from 1½ to 1½ times the basic rate, and a three-weeks paid leave. The

³See Section II for a discussion on unemployment and employment issues.

bill will be discussed at the National Economic Development and Labor Council (NEDLAC) by representatives of labor, business, and government before its presentation to Parliament.

10. After moderating in 1995, the increase in nominal remuneration per worker accelerated in 1996, influenced by the pick up in inflationary pressures, an improvement in average labor productivity, and high gross operating surpluses of business enterprises. Average nominal wages in the nonagricultural sectors rose by 10.4 percent (on a 12-month basis) through September 1996, compared with a 9.4 percent increase for 1995 as a whole (Appendix Table 9), while real wages increased on an annual basis by about 1 percent in both 1995 and the first three quarters of 1996. Real wages in the public sector have fallen over the last 2 years, whereas real wages in the private sector increased by 2.4 percent in 1995 and by 1.2 percent (on a 12-month basis) through September 1996. Despite the increase in real remuneration per worker, real unit labor costs continued to fall during 1995 and the first three quarters of 1996, as the general upward trend in real wages was accompanied by higher labor productivity: the annual growth in real output per worker was 3.3 percent in 1995 and 2.3 percent in the first three quarters of 1996. The productivity growth has largely been the result of the continued shift to capital intensive technologies, and the attendant fall in employment.

11. Following annual inflation rates close to 10 percent a year during 1992-94, inflation fell markedly in 1995 and early 1996, declining to 5.4 percent by April 1996. However, consumer price increases accelerated again in the second half of 1996 and early in 1997, and the 12-month inflation rate rose to 9.4 percent by the end of 1996 and to 9.9 percent by April 1997. The upward trend in inflation over the last year can be attributed to a number of factors. First, the depreciation of the rand contributed to increases in the prices of imported goods, although the 9.7 percent rise in these prices during 1996 was significantly below the 21 percent nominal effective depreciation of the rand that took place during the period, as many importers shaved margins to protect their market share. Second, as indicated below, despite steps taken during the year to tighten credit conditions, broad money and bank credit to the private sector continued to expand strongly. Third, the surge in average nominal remuneration led to a resumption in the upward movement in nominal unit labor costs in the second half of 1995, which persisted in 1996.

C. Public Finance Developments

Developments through 1995/96

12. After peaking at 8.6 percent of GDP in 1992/93, the deficit of the central government declined to 6.7 percent in 1993/94, falling further to around 6 percent in 1994/95 and 1995/96 (Appendix Table 11).⁴ Government ordinary revenue increased by a cumulative 0.9 percent of

⁴The fiscal year begins April 1. Data prior to 1994/95 are not comparable with those thereafter
(continued...)

GDP during 1994/95 and 1995/96, to 25.3 percent in 1995/96 (Figure 3; Appendix Tables 12 and 13). Virtually all of this increase can be attributed to larger collections of personal and corporate income taxes, as customs receipts rose only marginally—offsetting the decline and eventual elimination of the import surcharge—and revenue from the VAT, excises, and the fuel levy remained relatively constant in terms of GDP. Over the same period, government expenditure fell by 0.4 percent of GDP to 30.5 percent of GDP in 1995/96. An increase in interest payments was more than offset by a large decline in capital expenditure to just 1 percent of GDP in 1995/96. This decline reflected in part a slow rate of expenditure under the Reconstruction and Development Program (RDP), and was the major reason for the increase in the stock of “rollovers” from R 1.5 billion at March 1993 (0.4 percent of GDP) to R 8.9 billion by March 1996 (1.8 percent of GDP; the latest date for which data are available).⁵ Transfers to the provinces were around 14½ percent of GDP, representing 60 percent of non-interest central government expenditure.

13. The RDP fund was designed to mobilize resources for special initiatives aimed at redressing inherited inequities. The fund was financed by a reduction of planned allocations to spending departments, and funding was to increase by R 2.5 billion annually from 1994/95 through 1998/99. In the event, significant capacity constraints led to large increases in rollovers. These constraints, which are being addressed, included weak management capacity, cumbersome tender procedures, lack of experience with private-public partnerships, and insufficient coordination. The RDP Office was abolished in mid-1996, and the various projects became part of the regular ministry budgets; the RDP fund is now used only for channeling international financial assistance to earmarked projects and programs.

14. Data on economic and functional classifications are only available for total expenditure of the national and provincial governments (Appendix Tables 14, 15, and 16), and include that

⁴(...continued)

because the 1994/95 budget changed the methodology concerning the treatment of four of the former homelands (Transkei, Bophuthatswana, Venda, Ciskei). Central government expenditure includes transfers to the provinces and the accrued rather than the cash interest charges; accrued interest data is around ½ percent of GDP higher than cash interest payments (this difference has been rising over time) owing to the sale of government bonds with a lower coupon rate than the prevailing market yield. The data here exclude extraordinary transfers to the Pension Fund and the Gold and Foreign Exchange Contingency Reserve Account, and revenue from the sale of strategic oil stocks.

⁵Rollovers result from underspending, mainly on capital projects, relative to the original budget allocations. The Minister of Finance approves the amounts that may be rolled over on a case by case basis. Generally, rollovers must be spent by the end of the following fiscal year, although rollovers associated with the RDP could in some circumstances be spent over several years (a provision that has now lapsed).

SOUTH AFRICA
GOVERNMENT FINANCES, 1989/90-1997/98 1/
(In percent of GDP)

Sources: Department of Finance; South African Reserve Bank; and Fund staff estimates.

1/ Fiscal year ending March 31. Data for 1996/97 are preliminary. Budget data for 1997/98.

2/ National expenditure including transfers to provinces, but excluding extraordinary transfers.

3/ Central government only: including revenue which is subsequently transferred to the provinces; excludes revenue from sale of strategic stocks of oil.

4/ Includes secondary tax on corporations and corporate tax on gold mining.

5/ Total expenditure by national and provincial governments, including stocks of rollover funds.

6/ Data before 1992/93 not available. Actual data to 1995/96, and budget data for 1996/97-1997/98.

7/ Excludes Wages, interest payments, and business subsidies.

financed by own revenue of the provincial governments (which is small and is mainly derived from motor vehicle and other licenses). While these data need to be interpreted with care,⁶ they indicate that total cash expenditure of the central and provincial governments declined by a cumulative 0.9 percent of GDP during 1994/95 and 1995/96 to 31.3 percent in 1995/96.

Developments in 1996/97

15. The "headline" deficit of the central government for 1996/97 rose to 5.3 percent of GDP from 4.9 percent in 1995/96. This was 0.2 percentage points of GDP above the budget target, as higher-than-projected revenue was more than offset by higher spending, which accelerated sharply toward the end of the fiscal year. When this "headline" estimate is adjusted to exclude extraordinary receipts such as the proceeds from the sales of strategic oil stocks, the deficit outturn for 1996/97 is 5.6 percent of GDP, and when accrued rather than cash interest payments are included, the deficit was 6.2 percent of GDP, compared with 5.8 percent in 1995/96. The higher-than-budgeted deficit largely reflected the much needed increase in RDP expenditure.

16. Central government ordinary revenue was 0.8 percent of GDP higher than in 1995/96 and 0.6 percent of GDP higher than budgeted. This increase was mainly due to a surge in corporate income taxes, reflecting the rise in corporate profitability and unanticipated higher receipts from the Secondary Tax on Corporations, following the halving of its rate to 12.5 percent. Personal income taxes were buoyed by collections under the third and final tax amnesty,⁷ while collections under the new 17 percent tax on retirement income were somewhat below target. Higher customs revenue from imports of motor vehicles was offset by lower VAT receipts because arrear collections were less than anticipated. However, the

⁶The data show the economic and functional classifications of the Budget plus the changes in the appropriations introduced in the Adjustments Budget, which is presented to Parliament the following February, and includes a distribution by spending ministry of the stock of rollovers from the previous fiscal year. Because the budget data do not include a provision for the expected expenditure of rollovers in the current fiscal year, the economic and functional data that are based on the Budget estimates are not strictly comparable to those based on the preliminary outcome presented in the Adjustments Budget. Further, the economic and functional data that are based on the Adjustments Budget include adjustments for the cash that was transferred to spending ministries, but which was subsequently not spent and was surrendered back to the exchequer account. Accordingly, the data in Appendix Tables 14, 15, and 16 have been adjusted for both surrenders and rollovers to derive the total cash expenditure of the central and provincial governments. Finally, at this time the economic and functional classifications of the 1996/97 budget are available, but not those for the 1996/97 Adjustments Budget.

⁷This amnesty, covering tax arrears prior to March 1994, netted around R 1 billion (0.2 percent of GDP) over the period November 1996 to February 1997.

overall target of 0.3 percent of GDP for collections of all types of tax arrears through improvements in tax administration was exceeded by a wide margin. Receipts were also boosted by nontax revenue, especially from interest earnings on government deposits, owing to higher interest rates than had been expected. Extraordinary revenue, resulting from the sale of the strategic oil stocks was in line with the budget.

17. Central government expenditure increased by 1.2 percent of GDP in 1996/97 to 31.7 percent of GDP, or 0.8 percent of GDP higher than budgeted. The increase in interest payments by 0.6 percent of GDP was in line with projections, and reflected in part the take over of the former debts of the four TBVC homelands by the central government. Other current expenditure fell by 0.9 percent of GDP compared with an anticipated fall in current expenditure of 1.5 percent of GDP in the budget; transfers to the provinces declined by 0.2 percent of GDP or half of what had been anticipated in the budget because some provinces overran their original allocations and were provided with additional transfers in the Adjustments Budget. Declines in the central government's own current expenditure made up the balance of the adjustment (a disaggregation by type of expenditure is not yet available). Capital expenditure rebounded—rising from 1.0 percent of GDP in 1995/96 to 2.6 percent in 1996/97—reflecting in part the pick up in RDP expenditure.

18. As noted above, the economic and functional classifications of the 1996/97 Adjustments Budget are not yet available. Comparing instead the 1996/97 budget with the 1995/96 budget, the data for the central and provincial governments indicate that outlays on wages and salaries increased sharply, with some offset in current transfers to businesses, households, and other units of government. The increase in wage and salary spending reflected the three-year agreement on civil service conditions that became effective in July 1996, which included a rise in wages of salaries of R 8.5 billion (1.5 percent of GDP) in the first year of the agreement and R 6.5 billion in each of the following two years. In addition, the agreement provided that any savings that arise from the "rightsizing" program would be used for further wage increases for those that remain in the civil service (see Section III).

19. Two tax incentive schemes were introduced during 1996 in the context of the GEAR. The accelerated depreciation allowance provides for straightline depreciation for new manufacturing plants and equipment over three years (rather than five) and for buildings over ten years (rather than 20) that are installed between July 1996 and September 1999. The income tax holiday can be granted for two years for each of three criteria that are met by new manufacturing investments valued at more than R 3 million starting from October 1996. The criteria are labor absorption (based on the value added devoted to wages and salaries), regional location (based on the assessment of regional potential and need for development, as determined by the Department of Trade and Industry), and industrial policy (based on priority industries that are determined by the DTI, using criteria such as labor intensity, industries with strong economic linkages, critical industries affected by the tariff reform, and global potential).

20. As in previous years, the 1996/97 deficit was in the main financed through the issue of long term bonds (Appendix Table 17). These bonds were sold with an average coupon rate of 12.83 percent, compared with a weighted average yield of 15.87 percent. The consequent discount on the sale of bonds amounted to R 6.7 billion.⁸

21. Total debt of the central government (at face value) has increased rapidly in recent years, rising from 39.5 percent of GDP in 1991/92 to 55 percent in 1996/97 (Appendix Table 18). Of this increase, 10.4 percentage points reflect the discount on the sale of government bonds, as described above (3.4 percent), the takeover of the overdraft debts of the former TBVC homelands that had been guaranteed by the central government and that are being gradually switched to Treasury bill debt (2.4 percent), the recapitalization of part of the actuarial underfunding of the public pension fund (1.7 percent),⁹ and the transfer to the South African Reserve Bank (SARB) to cover the losses in forward exchange operations (2.9 percent).¹⁰

22. As at March 31, 1996, contingent liabilities of the central government stood at R 134.8 billion (27 percent of GDP in 1995/96). The largest components were the underfunding of the government pension fund (R 54.4 billion) and the government guarantees (R 66.5 billion). Of the latter, R 55.5 billion were guarantees on public enterprise debts, mainly for the transport company Transnet (R 25.2 billion), the telephone company Telkom (R 10.0 billion), and the electricity company Eskom (R 6.2 billion). Revised guidelines for the issuance of new guarantees were implemented in October 1996; since then, the government is charging a fee to discourage the use of such guarantees.

⁸Given the practice of issuing bonds with a coupon rate that is lower than the market yield (which began in 1980), the interests bill is lower than the cash interest payment. Adjusting for this factor, the annual interest bill (and consequently the cash budget deficit) in 1996/97 would have been 0.6 percent of GDP higher than was recorded, similarly, adjusting the stock of government bonds for the corresponding discount, the debt to GDP ratio at March 1997 would have been 7 percentage points of GDP lower.

⁹As of March 31, 1996, actuarial underfunding of the state pension fund was estimated at around 40 percent of contingent government liabilities, or 10 percent of 1995/96 GDP.

¹⁰Following the realization of these losses, the balance of the Gold and Foreign Exchange Contingency Reserve Account held at the South African Reserve Bank is increased as is the total debt of the central government. Periodically, this obligation of the central government is regularized through the issue of zero coupon paper to the Bank. The Bank has the right to request conversion of this paper into central government coupon-bearing stock, should the latter be needed for monetary management purposes.

The 1997/98 budget

23. On March 12, 1997, the Minister of Finance presented to Parliament the budget for fiscal year 1997/98. In line with the government's commitments under the GEAR, the budget targets a decline in the overall deficit from 5.6 percent of GDP in 1996/97 to 4 percent in 1997/98 (excluding extraordinary revenue and the difference between accrued and cash interest payments in both years). The budget is based on the assumptions that real GDP growth will be 2.5 percent and that the GDP deflator will increase by 8.5 percent in 1997/98, compared with 3.7 percent and 9 percent, respectively, in 1996/97. Given that ordinary revenue has been held virtually constant at 26 percent of GDP, the whole adjustment effort is to come from a decrease in expenditure.

24. To achieve the revenue targets, the budget includes the following measures: (i) modifications to the personal income tax—including a change in the threshold rate, an increase in the nominal value of the tax bands, and a reduction in the number of tax bands from 8 to 7—which on balance avoid fiscal drag on low income earners (those below R 30,000 a year) but allows some drag on all other income earners; (ii) an increase in the taxation of fringe benefits such as company cars, travel allowances, and housing and holiday accommodation; (iii) the broadening of the coverage of the 17 percent tax on the gross interest and net rental income of retirement funds, which was introduced last year, to unit trusts and certain interest-bearing instruments; (iv) the unification of the taxation of lump sum payments from public and private sector pension funds (from March 1, 1998; acquired rights were grandfathered) and the reduction of the tax advantage of the transfer of public sector pension fund balances to provident funds; (v) the halving of the market securities tax to 0.25 percent, while removing the exemption for purchases by foreigners; and (vi) increases in specific excises (especially for tobacco and alcohol) and stamp duties, and a halving in the ad valorem excise rate of many commodities to a maximum of 15 percent.¹¹ In addition, further improvements in tax administration as a result of the merger in April 1996 of the Inland and Customs Revenue Services into the South African Revenue Service (SARS), the cash bonus scheme introduced at the SARS, and the forthcoming move to make the SARS autonomous from the civil service, are projected to yield R 2.5 billion (0.4 percent of GDP).

25. On the expenditure side, noninterest current expenditure of the central government is budgeted to decline by 1.3 percent of GDP—most of it as a result of a decrease in central government transfers to provincial governments—while capital expenditure of the central government is to decline by 0.5 percent of GDP. On an economic basis—where the data relate to all spending by the central and provincial governments and are subject to the caveats noted above—expenditure on goods and services is projected to decline by 0.5 percent of GDP to 15.8 percent, reflecting a slight decline in the wage bill, to 11.9 percent of GDP, and a reduction in transfers to business and other units of general government. On a functional basis, expenditure declines are forecast in the areas of defense, education (due to the rightsizing

¹¹For a description of the current tax system, see Annex I.

program; see Section III), and economic services, while increases are allocated to housing and welfare. With regard to business subsidies, recently the government shifted industrial promotion from the export subsidy scheme (GEIS) to various supply side measures, such as the promotion of industrial clusters and corridor developments, and the tax incentives program described above.

26. As previously, the deficit is to be financed almost wholly through the issue of government securities in the domestic market; the government will again issue debt at a discount with a coupon rate of some 2 percentage points below the expected yield. The lower deficit and the proceeds from privatization that accrue to the central government and those from the sale of strategic oil stocks will help keep the ratio of government debt to GDP at 55 percent, after including the planned takeover of old debts of Namibia to South Africa (0.2 percent of GDP).

27. The significant progress made by South Africa on a variety of structural reforms toward strengthening budgetary operations and tax administration is outlined in Section III and the new intergovernmental relations are outlined in Section IV.

D. Monetary Developments and Policies

28. Developments in the monetary area during 1995 were marked by an unprecedented volume of capital inflows to South Africa, which in turn presented the authorities with a new policy challenge. While they represented an increased external demand for South African assets arising from the strengthening of investor sentiment, they resulted in a large monetization which could lead to even higher inflationary pressures and a loss of competitiveness. The SARB firmed monetary policy in 1995, raising the bank rate from 12 percent to 15 percent in the course of the year, and sterilized a substantial fraction of the inflows. At the same time the SARB was able to reduce its net open forward position (NOFP) considerably. Nonetheless, the expansion of monetary and credit aggregates continued vigorously. The broadest money supply definition (M3) grew at rates exceeding 15 percent a year for most of 1995 (Appendix Table 19), well beyond the guideline range of 6–10 percent set by the SARB for the year, and the growth of bank credit to the private sector surpassed 18 percent on average for the year (Figure 4).

29. In contrast to the relatively stable environment in 1995, investor sentiment shifted markedly in early 1996 and monetary developments were dominated by unrest in the foreign exchange markets. As in other international episodes of currency weakness, adjustment in South Africa to an unsettled foreign exchange market came through a mix of exchange rate depreciation, loss of international reserves, and interest rate increases. The monetary authorities attempted to tighten the stance of monetary policy to support the exchange rate and contain the inflationary pressures arising from the currency depreciation, and reiterated their guidelines for growth of M3 in the 6–10 percent range for 1996 as a signal of their commitment to a firm monetary policy. The bank rate was increased twice in 1996 (April and

Figure 4
SOUTH AFRICA

MONETARY INDICATORS AND INTEREST RATES, 1990-97

Source: South African Reserve Bank.

November) to reach 17 percent, and liquidity in the money market was continuously squeezed. At the same time, the authorities intervened heavily in the spot and forward exchange markets, and thus the SARB's net holdings of gold and foreign exchange reserves dropped from US\$4.2 billion by end-1995 to US\$2.1 billion a year later, while the NOFP rose to about US\$22 billion by end-1996.

30. Notwithstanding the drain of liquidity implied by the loss of foreign assets and the increase in interest rates, the South African economy continued to monetize vigorously during 1996 and early 1997. The expansion of monetary and credit aggregates remained buoyant during most of 1996—with incipient evidence of tapering off by the end of the year before resuming their rapid pace in 1997. The 12-month growth rate of M3, which was 15.2 percent in December 1995, rose to 16 percent in October 1996, before declining to 13.6 percent by December 1996. Thus, the growth in M3 exceeded by far its guidelines and the fall in the income velocity of circulation—which started in 1993—continued in 1996 (Appendix Table 20). The expansion of narrow monetary aggregates was even more notorious (with M1 growing 30.9 percent in the year to December 1996) as the public in general, and institutional investors in particular, revealed an increased preference for liquid assets in the context of volatile financial and exchange markets. Furthermore, the demand for narrow aggregates was also stimulated by the attractive returns offered by banks on demand deposits in order to fund themselves in an environment of tight money market conditions.

31. As can be inferred from the above developments, the counterpart to the R 38.3 billion increase in M3 during 1996 was a contrasting behavior between its foreign and domestic sources (Appendix Table 20). While the net foreign asset position of the consolidated banking system declined by R 14.5 billion as a consequence of the unrest in foreign markets,¹² its net domestic asset position increased by R 52.8 billion in 1996. Given that most of the rise in domestic credit corresponded to an increase in the banking system's claims on the private sector, the 12-month rate of growth of bank credit to the private sector rose from 17.6 percent in December 1995 to a peak of 18.9 percent in October 1996, before moderating to 16.1 percent by the end of the year (Appendix Table 22). The increase in credit to the private sector during 1996 (R 41.2 billion) was more or less evenly distributed between households and corporations—56 percent and 44 percent respectively. Almost 36 percent of the total increase in credit to the private sector was in the form of mortgage advances to households.

32. Developments in foreign exchange markets and the increase in the inflation rate also impacted the level and structure of interest rates. The average yield on long-term government stock rose from 13.8 percent in January 1996 to 16.5 percent in May, and then declined to 16.2 percent by December 1996 (Appendix Table 21). A similar movement was registered in

¹²The fall in the consolidated banking system's net foreign assets reflected the loss of foreign assets of the SARB and the considerable accumulation of foreign liabilities by commercial banks.

interest rates prevailing in money markets. The representative rate on 3-month Treasury bills rose from 14 percent in January 1996 to 15.9 percent in May. This rate fell somewhat during the second half of the year, but rose again to that level by end-1996, as money market conditions tightened. The prime overdraft rate charged by banks followed closely the behavior of the bank rate, and increased to 20.25 percent in November 1996. It should be noted, however, that real interest rates prevailing at end-1996 were not significantly different from those at end-1995.

33. Conditions in the money market reflected the general tightness of the availability of liquidity. The “shortage” in the market (i.e. the amount the SARB accommodates) rose from an average daily value of R 4.9 billion in January 1996 to R 9.9 billion in December 1996, leading to an increased use of the second tier accommodation at the discount window in the last quarter of 1996. However, the SARB reduced its penalty rate for second tier accommodation from 1.5 percent above the bank rate to 0.75 percent in June 1996 to ease somewhat conditions in the money market.

34. Another marked change in investor sentiment occurred in early 1997, when confidence and stability returned to South African financial markets. The favorable sentiment in turn translated into capital flows returning to South Africa. These inflows—together with the proceeds (US\$1.3 billion) of the sale of 30 percent of the shares of Telkom to a foreign consortium—permitted the replenishment of the SARB’s net international reserves, which rose to US\$3.7 billion by May 1997, a strengthening of the rand, which appreciated almost 9 percent in nominal effective terms in the first quarter of 1997, and a decline of long-term yields to below 15 percent. However, the rate of growth of money and credit aggregates rose in 1997, and both M3 and bank credit to the private sector expanded again at rates exceeding 16 percent a year by March 1997, well above the renewed monetary growth guideline of 6–10 percent for 1997.

E. External Sector Developments

The Balance of Payments

35. The external current account registered a deficit of 0.3 percent of GDP in 1994—the first since 1984—owing to the rapid growth in imports, reflecting the pick up in economic activity, and a slowdown in exports. The deficit widened to 2.1 percent of GDP in 1995, as imports continued to grow at a fast pace (Appendix Table 23), and despite an increase in the volume of nongold exports and little change in the international terms of trade. Imports of capital goods were especially pronounced, suggesting that, as in 1994, investment was the most important factor behind the fast import growth. The current account deficit declined to 1.6 percent of GDP in 1996, with a similar improvement in the trade balance reflecting a continued strong export performance and a marked slowdown in import growth.

36. Exports picked up momentum in the second half of 1996 as a result of a number of factors, including the completion of some of the export-oriented “mega investment projects”

(Alusaf, Columbus Steel, and Namakwa Sands), which contributed significantly to the strong export performance of the manufacturing sector; the rebound in agricultural production owing to favorable weather conditions, which led to the rapid growth of agricultural exports; and the depreciation of the rand. Moreover, access to new markets, relatively strong growth in the main industrial countries, and high growth in the emerging economies also contributed to the firm demand for South African exports. While the volume of nongold exports increased by 11 percent, compared with 14 percent in 1995 (Appendix Table 26), the increase was a modest 2.6 percent in U.S. dollar terms, compared with 22.5 percent in 1995, reflecting lower export prices, as exporters seem to have used the depreciation of the rand to increase market shares. Accordingly, while the rand depreciated in nominal effective terms by 21 percent in 1996, the unit value of nongold exports only increased by 6 percent in rand terms.

37. The value of gold exports declined in U.S. dollar terms by 1.5 percent in 1996, owing to a fall in production that more than offset the increase in prices. The average U.S. dollar price of gold increased by less than 1 percent in 1996, as prices remained firm through the first half of the year but fell in the last quarter to US\$369.2 an ounce by December 1996 (US\$344.5 an ounce in May 1997), compared with a peak of US\$404.8 an ounce in February 1996. The share of gold in total merchandise exports declined from more than 28 percent in 1992 to 21 percent in 1996.

38. The growth of imports fluctuated markedly in 1996. It moderated in the first quarter, but picked up in the second and third quarter, reflecting some strengthening in aggregate domestic demand and in anticipation of a further depreciation of the rand, and turned negative in the fourth quarter largely owing to a decline in domestic demand. For the year as a whole, imports remained flat in 1996, after growing by 26 percent in 1995. Import growth in volume terms slowed to 7.6 percent in 1996, compared with about 16 percent in the previous two years. Intermediate goods and capital equipment continued to account for a large share in total imports. The pass-through of the depreciation of the rand on import prices was limited as the unit value of imports increased by 7.7 percent in 1996, at about the pace of increase in the previous two years, when the value of the rand remained broadly stable.

39. The deficit in the services account declined marginally from 3.3 percent of GDP in 1995 to 3.1 percent of GDP in 1996. This was the result of a marked further increase in tourist receipts, partially offset by higher payments for services associated with trade—mainly freight and insurance—and higher interest payments owing to the rise in South Africa's foreign debt.

40. Following the strong capital inflow that began in the second half of 1994, the surplus in the capital account declined from US\$5.3 billion in 1995 to US\$0.9 billion in 1996 (Appendix Table 28). This reflected a marked change in investor sentiment about South African assets. In particular, net inflows of long-term capital declined from US\$4.2 billion in 1995 to US\$1.1 billion in 1996, while net flows of short-term capital (net of errors and omissions) became slightly negative. The net inflow of long-term capital largely reflected an increase in borrowing by the public sector that exceeded the levels of 1995 and more than

offset the long-term outflows by the private sector. Government borrowing comprised the Euro-sterling issue of £100 million in January 1996, the Eurobond issue of DM 500 million—which was primarily aimed at refinancing a maturing bond issue—and a bond issue of US\$300 million in the U.S. market. Public corporations were also net borrowers. By contrast, private long-term capital inflows declined throughout the year and became substantially negative in the fourth quarter, reflecting the repayment of foreign debt obligations, net sales by non-residents of securities on the Johannesburg Stock Exchange, and an increase in assets held abroad by South African companies and nonbank financial institutions.

41. Total assets swaps (see Section V for a description of this mechanism) authorized since the inception amounted to the equivalent of US\$5.9 billion by end of 1996, but only US\$3.7 billion had been utilized; of this amount US\$2 billion was swapped in 1995 and US\$1.7 billion in 1996. Notwithstanding the increase in the ceiling in 1996 on swap operations, the rather low use of this mechanism indicates that the existing limits are not binding. This may reflect a limited interest by foreigners in such operations during 1996, perhaps owing to the volatility in the rand, as suggested by the decline in swap operations from US\$663 million in the first quarter of 1996 to an average of US\$342 million in the subsequent three quarters.

42. After a substantial drop in 1993, and a further decline in the first half of 1994, net international reserves recovered with the surge in capital inflows in the second half of 1994 and in 1995.¹³ Net international reserves peaked at US\$3.5 billion in the fourth quarter of 1995, or about 1.3 months of imports of goods and nonfactor services (Appendix Table 30), after having repaid US\$0.7 billion in reserve-related external liabilities. However, reserves came under pressure during 1996, declining by more than half by the third quarter of 1996, and were US\$1.6 billion by the end of the year. (Notwithstanding the pressures on reserves, the SARB did not make use of its external lines of credit through 1996.) In addition to intervening in the spot exchange market, the SARB intervened heavily in the forward foreign exchange market, raising the NOFP from nearly US\$7 billion in mid-February 1996 to about US\$22 billion in December 1996—an increase equivalent to some 6 months of merchandise imports in that period.

43. As indicated above, there was a marked strengthening of sentiment in early 1997, which resulted in large capital inflows and an increase in net international reserves to a record level (US\$3.7 billion) in May 1997. In a departure of previous policy, the SARB made use of the external lines of credit by the equivalent to R 2.5 billion through April 1997, but repaid R 0.7 billion in May. The NOFP has gradually declined to US\$17.8 billion in May 1997.

44. In line with the large capital inflow experienced in 1995, South Africa's total external debt (denominated in foreign currency) increased by nearly US\$4 billion to US\$22.3 billion, or 24 percent of GDP (Appendix Table 29). By end-June 1996, this stock had fallen to just

¹³The CCFF purchase from the Fund in December 1993 is considered a reserve liability.

below US\$21 billion as a result of the sharp reversal in capital flows and a reduction in long-term private debt—from US\$12.5 billion at end-1995 to US\$11.2 billion by June 1996; total private sector debt declined by US\$1.7 billion between 1995 and mid-1996, to about 57 percent of South Africa's external debt. At the same time, the share of short-term debt in total debt increased from less than 40 percent in 1994 to about 46 percent in June 1996, following the large short-term capital inflows in 1995.

Trade liberalization and trade agreements

45. Considerable progress has been made in rationalizing the external trade regime over the last few years. A trade reform initiative was launched in 1994 based on the government's application to the Uruguay Round of Trade Negotiations. The reform aims to eliminate quantitative import restrictions; standardize tariff rates at six levels; reduce the number of tariff lines to the six-digit Harmonized Code level by the end of 1999; reduce the maximum tariff rates to 30 percent for industrialized goods and 36 percent for agricultural goods, with "sensitive" industries—such as clothing, textiles, and motor vehicles—maintaining the higher tariff rates and longer adjustment periods.

46. Under the reform, South Africa replaced during 1994-95 most quantitative restrictions and formula duties with ad valorem tariffs for most manufactured products and a number of agricultural products, and adopted tariff bindings covering 98 percent of imports to become effective in 1999. Nominal rates of protection were reduced—even though most tariffs were already well below the agreed WTO tariff binding rates when the Uruguay Round negotiations were concluded. The tariff structure was simplified through the near halving of the number of tariff lines to about 5000 and through the reduction in the number of ad valorem rates. Reforms of the trade and marketing of agricultural products were accelerated in 1995, with the deregulation of prices, the abolition or reform of agricultural control boards, the conversion of import controls to ad valorem duties. Finally, the last remaining import surcharge, on luxury goods and household appliances, was abolished in October 1995.

47. During 1996, the schedules for the reduction of tariffs over 5-7 years were finalized, and a number of tariffs on commodities that were either not produced in South Africa or which were imported inputs were abolished. Overall, the import weighted average tariff rate fell from 11 percent in 1995 to 10 percent in 1996, but the reduction in tariffs on inputs ahead of those on final goods resulted in an increase in effective protection, which raised the existing biases against exports, labor absorption, and growth. Finally, the three-year process leading to the elimination of the primary export subsidy, GEIS, initiated in 1995, was brought to an end with the abolition of the export subsidy program to take effect from mid-1997, six months ahead of the original schedule.

48. Negotiations on regional free trade agreements with the South African Development Community (SADC)¹⁴ and the European Union (EU) continued during 1996. SADC was originally established in 1980; its agenda was refocused in 1992 toward deepening economic integration, including in monetary and fiscal policies, exchange rate and trade regime, and mobility of capital and labor. The Trade Facilitation Protocol, drafted in February 1996, envisages a Free Trade Agreement (FTA) among SADC member countries with reciprocal tariff reductions. The proposed FTA would be phased-in over an eight-year period, and South Africa was considering accelerating the elimination of tariffs on imports from SADC before the reciprocal SADC tariffs on South African exports were eliminated under the FTA. The review of the revenue-sharing formula for the Southern African Custom Union (SACU) is nearly completed;¹⁵ it aims at helping avoid sharp reductions in South Africa's transfers to the other members as a result of its unilateral tariff reduction.

49. The negotiations with the EU have proceeded slowly. After some delay, access by South Africa to the Lome convention, except for its trade preference provisions, was formalized in April 1997. The main benefits to South Africa are the right by South African companies to tender for contracts funded under the EU development fund and to participate in the joint bodies of the African Caribbean and Pacific (ACP) states and the EU—the joint assembly and ministerial meetings—where negotiations on the future of Lome are now taking place. Regarding the FTA proposed by the EU, which envisaged the asymmetrical phase-in of a free trade area over 10–12 years, the South African authorities are concerned that the EU offer has not adequately addressed South Africa's trading relations with the region and the fiscal implications for SACU, that it excludes 40 percent of South African agricultural exports to the EU, and that it would expose local farmers to subsidized European agricultural products by removing the current tariff protection.¹⁶ As a consequence, discussions have continued at a slow pace.

Capital controls liberalization

50. A major step in liberalizing exchange controls was taken with the elimination of the financial rand mechanism in March 1995, and hence the removal of all exchange restrictions on nonresidents. Progress was also made in relaxing controls on residents in various steps,

¹⁴The members are: Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Tanzania, Swaziland, Zambia, Zimbabwe, and South Africa.

¹⁵South Africa, together with Botswana, Lesotho, Namibia, and Swaziland, form SACU, which provides for the free movement of goods and the right of transit among member countries. Under SACU, South Africa administers duty collection and distributes shares of the common revenue pool to the four countries according to a revenue-sharing formula.

¹⁶Anti-dumping measures could not be applied against European subsidized exports under the Uruguay Round agreement.

underscoring the authorities' commitment to the gradual elimination of exchange controls on residents while ensuring that these steps were not disruptive to financial markets. For a description of these steps, see Section V.

51. It is important to note that the authorities' approach was not simply to liberalize controls in a sequence of steps that allowed different types of capital transactions one at a time, but to open a number of new windows for resident capital transactions, each subject to a cap. In this way, an increasing array of forms of resident capital transactions have been permitted, but the risks of major aggregate outflows were limited by the caps applied to each type of transaction. This feature of the step-by-step approach allowed the authorities to gradually increase the range of authorized capital transactions, as well as the scope of each of these transactions by raising the caps. The authorities intend to continue with this approach until all types of resident capital outflows are permitted and until the caps are no longer binding, and the risk of major capital outflows minimized.

The Eurorand market

52. Beginning in September 1995, a series of rand-denominated bonds were issued in the European market by non-South African entities, including Merrill Lynch, EBRD, and the Government of Sweden. Total issues amounted to the equivalent of US\$1.8 billion by mid-February 1996. The coupon rate fell from 15 percent on the initial issues to as low as 13 percent on issues in late January and the first half of February 1996. Activity in the Eurorand market slowed thereafter, but picked up markedly in early 1997, with total issues exceeding the equivalent of US\$10 billion by end-May 1997. In contrast to the previous issues, which had been short- or medium-term, a number of the issues in 1997 have carried maturities of 10 years or longer, with one issue by the EBRD having a maturity of 30 years. The coupon rate has generally been above 14 percent in 1997.

53. The development of the Eurorand market is an important step in the development of rand capital markets. Thus far, these issues appear to be largely held in the stable retail market, and there was no evidence of large sales during 1996. The market allows high credit quality international issuers to lower their borrowing cost in the Eurorand market vis-à-vis the sovereign issuer in the domestic rand market. Issuers swap the rand with a top-rated bank or investment bank in London, who then hedges the acquired rand exposure with the outright purchase of domestic rand gilts, frequently as part of an asset swap. The impact of these operations on reserves is generally thought to be positive or neutral.

II. UNEMPLOYMENT AND EMPLOYMENT ISSUES

54. The Growth, Employment and Redistribution strategy called attention to “the unemployment crisis in the labor market.” It cited official data for 1994 showing that open unemployment stood at one-third of the labor force and, on the basis of official macroeconomic projections, it concluded that the unemployment rate would rise further in the medium-term without enhanced policy actions. It noted that those worst affected by this would include the rural poor, the young, and the unskilled, and that even the enhanced policy environment proposed in the GEAR—including wage moderation and reforms to wage-setting institutions—would only achieve a reduction in the unemployment rate after the turn of the century. More recently, the South African Reserve Bank has reported that employment in the private nonagricultural sector continued to decline in 1996, compounding the fall of over 10 percent between 1990 and 1995.¹⁷ In addition, the authorities have indicated that even their projections for the unemployment rate in 2000 under the GEAR policy framework (nearly one-third of the labor force) could prove to be overly sanguine. This forms the background to the current preparations of a “jobs summit” aimed at discussing ways to tackle the unemployment problem in late 1997.

55. Given the authorities’ concern with unemployment and employment and the emphasis given by the authorities in the GEAR to wage determination practices for employment growth, this section discusses some aspects of current wage determination processes and their role in employment creation. The discussion also identifies some gaps in current knowledge about these issues that remain to be filled. The section goes on to assess the reliability of the underlying data on these matters, suggesting that the data do not appear to be subject to major measurement or construction errors, and hence that the authorities are right to use them in developing labor market policy.

A. Unemployment and Wage Determination

56. Open unemployment rates are extremely high and the authorities anticipate that they may continue to increase for some time, even on the basis of the enhanced policy framework presented in the GEAR. In this light, an assessment of the roots of unemployment is critical to the design of policy to address it.

57. As the Department of Labor correctly points out, there are many elements that should be considered in this context.¹⁷ Skills training has been inadequate—compounding a skilled labor shortage—trade policies have discouraged export-oriented growth and the associated stimulus to employment, and multiple economic distortions in the allocation of rural land due to the policies of the former regime have all played their part in generating large unemployment in South Africa. All of these issues need to be addressed in conjunction with those related to “labor market flexibility,” if the “unemployment crisis” is to be confronted

¹⁷See Mr. S. Pityana, quoted in *Business Day*, 24 January, 1997.

effectively. But even in this wider context, it is still appropriate to consider what contribution reform to wage setting practices might make to efforts to stimulate employment.

58. It should be noted at the outset that there is considerable “institutional flexibility” in South Africa. There is a great variety of institutional arrangements in its labor market, including (i) some sector level negotiating fora which sometimes exist alongside parallel plant-level fora for firms in the same sector; (ii) a wide range of labor contracts some of which are negotiated annually while others cover longer time periods including productivity-related clauses; (iii) a variety of different arrangements governing worker training; and (iv) many different trade union and employer organizations which interact with each other in diverse ways. In addition, there is no legal requirement forcing both employer and worker representatives to use any particular institution, procedure, or contractual arrangement.

59. However, there is little “wage flexibility” in South Africa, as it is heavily restricted by a multiplicity of floors on wage rates, many of which are enforceable in the courts. Although there is no national minimum wage—and the GEAR emphatically rejects the introduction of such a minimum wage—legally enforceable wage floors are set by Wage Boards and Labor Orders in sectors with limited trade union representation, and by Bargaining Council (BC)¹⁸ agreements between employer and labor representatives at sector level. Under the recent Labor Relations Act, these wage floors have been made applicable to all firms in the sector if the BC represents over half of the employees in the sector and if the representatives at the BC request this extension, whereas previously, this extension was at the discretion of the Minister of Labor. In addition, plant level negotiations, including in firms covered by sector level BC agreements, may set wage floors above the rates determined by the BC agreement, although these do not have the force of law. Finally, there are employer-employee negotiations outside any of these legal frameworks, which establish negotiated floors on remuneration and conditions of employment.

60. An assessment of wage flexibility thus must consider a variety of wage-floor mechanisms and the interaction between them. In this process, consideration should be given to the evidence that the Wage Boards and Labor Orders have a limited and somewhat arbitrary coverage, and that the wage floors they have set have been low and infrequently revised, despite inflation. Furthermore, there were only 19 wage floors in operation in mid-1995 applying to some 730,000 workers, with the bulk of these being covered by one determination. It is also important to consider that in 1993, only 86 BC agreements were in force covering about 10 percent of the total employed labor force, they were limited in their geographical coverage, and they provided exemptions for small firms.

61. In considering these issues and their implications for an assessment of how these institutions affect employment and unemployment, three issues are critical: whether the data cited above is appropriate to assess the coverage of the institutions, whether coverage is a

¹⁸These were known as Industrial Councils prior to the recent Labor Relations Act.

useful means of assessing the role of any wage setting mechanism in discouraging employment, and whether the wage setting institutions can sensibly be considered in isolation from the other institutions, rather than as a group.

62. First, consider the data cited. BC agreements may cover some 10 percent of the employed labor force. But it is not clear that comparing coverage to the entire employed labor force is helpful in assessing its effects on employment creation. It would be more useful to compare coverage with employment in the private, nonmining, nonagricultural sector; government employment should be excluded because the aim is to discern the role of wage flexibility in determining private employment. Similarly, employment in mining and agriculture should be excluded because wage floors in the mines have always been set in bilateral negotiations between unions and firms outside these structures, and because agriculture acts as one of the residual sectors for surplus labor. In a sample of 340 manufacturing firms in Gauteng, Cape Town, Durban and Port Elizabeth studied by the ILO,¹⁹ just under 60 percent of firms (and therefore a higher share of workers in firms covered by the survey) were subject to a BC agreement, and a little over 20 percent of those firms were non-parties to the agreement. It would also appear that the data cited from the Labor Department for coverage of BCs, which underlies the number of 10 percent coverage mentioned above, excludes workers in firms that are not represented on the BCs, and therefore understates coverage for this reason.

63. Furthermore, the concentration of unskilled and young people among the unemployed suggests that from the perspective of assessing the causes of unemployment, the relevant coverage that researchers should be attempting to measure is that of unskilled workers, possibly excluding unskilled but experienced workers. Coverage measured on this basis could be at a completely different level and could be evolving quite differently from coverage measured against either total employment or private nonmining employment.

64. Second, coverage itself may not be a useful means of assessing the role of these mechanisms in generating unemployment. If covered workers represent a small portion of all (relevant) workers, this could reflect two quite different circumstances: that the mechanism is setting wages below market-clearing rates and therefore covers few workers because few have any incentive to negotiate with employers within that apparatus; or alternatively, that the mechanism is setting wages above market-clearing wage rates, shrinking the affected sectors relative to others, and therefore inducing low coverage compared to total employment. In the first instance, the BCs are economically irrelevant, while in the second, they are critical to determining employment patterns, but in both cases, coverage is low.

65. Third, the above suggests that to assess the contribution of these wage-setting mechanisms to unemployment, other measures than coverage should be used. At the sector level, a relevant measure would be wage differentials across firms or sectors for similar

¹⁹Guy Standing, John Sender, and John Weeks (1996) p.361.

workers. If it could be shown that wage-setting institutions did not generate wage differentials compared to uncovered sectors, this would suggest that they had no harmful effects on employment, and could even be stimulating it if the institutions contributed to more harmonious industrial relations. However, evidence from many sources indicates that council wage structures set wages above those applied in firms outside council sectors, even allowing for factors such as firm size and unionization, and that they are certainly well above wage rates in the informal sector.²⁰

66. Additional insight would be gained into these issues by new research on cross section data on the distribution of wage rates relative to the applicable wage floors. This research would indicate whether the floors set in these institutional arrangements were binding, and in what circumstances. Therefore, it would be important to start collecting these data, as they could be highly revealing about the impact of the wage floors on actual wage rates.

67. Issues of geographical coverage and exemptions should also be considered with care. A BC may cover only part of the country, but may nevertheless cover the industry in the entire country. Given that the geographical coverage can be readily extended, BCs or any other legally binding wage floor mechanism may discourage potential entry by new firms, even in regions not currently covered by the arrangement. Furthermore, this reduces competition in the goods markets, and thus may generate monopoly rents while discouraging employment creation. At the same time, it may maintain the current geographical concentration of industry to the detriment of the high unemployment and peripheral regions. Therefore, reference to current geographic coverage of BC agreements will tend to understate their economic impact.

68. On a similar basis, the observation that small firms are often exempted cannot be interpreted to imply that these mechanisms are generally unimportant to the small firm sector. Exemptions involve considerable administrative effort on the part of the applicants to submit, which can explain why applications come disproportionately from larger firms that can afford to make the effort. Furthermore, the exemptions that are approved are overwhelmingly partial—often relating to matters which have no bearing on labor cost. In addition, exemptions may subsequently be withdrawn, or lapse after their usual term of one year. If entry by new firms involves any sunk costs, the fact that exemptions are required at all, at any stage of the prospective life cycle of the new firm, will discourage entry by new firms. This disincentive does not depend on the degree of discretion in granting exemptions because, even if exemptions were granted automatically for “small” firms defined in some clear way, the disincentive to entry would remain for those firms that could only operate efficiently above the size considered “small.” Moreover, these mechanisms would continue to discourage existing small firms from growing—which can explain the rather limited number of medium size enterprises in South Africa—as well as potential larger firms, including foreign direct investment.

²⁰Bruno Boccara and Peter Moll (1997).

69. The impact of these mechanisms—wage boards, labor orders, BCs, and business and trade union negotiations—on wage flexibility and on employment patterns cannot be determined by consideration of each wage-setting mechanism in isolation from the others. If one such mechanism set above market-clearing wage rates in one sector but all other sectors set market-clearing wage rates, it would lead to a reduction of employment in that sector. But this would not necessarily cause unemployment because workers shed by the sector with above market-clearing wage rates would shift into the other sectors at lower wage rates. However, if all major sectors are faced with above market-clearing wage rates, then the workers shed by them would have few sectors with market-clearing wage rates in which to find employment. Thus, the combined effect of these wage-setting mechanisms would be to generate very sharp wage inequality between the above market-clearing sectors and the market-clearing sectors, as is observed in the South African data, and it would lead to considerable unemployment if the market-clearing sectors were unable to absorb all the labor released by the other sectors.

70. In practice, it is probable that the relative importance of the different wage-setting mechanisms to the aggregate black unskilled labor market has evolved considerably in the last 20 years. ICs probably became more important to the determination of the wage rates of black South Africans in the early 1980s, and plant level negotiations probably increased in importance thereafter. But both may have induced unskilled labor to shift increasingly to the market-clearing “informal” and agricultural sectors.

71. A development that has taken place in recent years and that has attracted some attention has been the introduction of explicit productivity-related clauses in remuneration agreements. While these clauses have helped ease industrial tensions in the negotiating process, and have protected the share of profits in income—both of these are useful achievements—they may have had an unintended negative impact on employment creation by inducing layoffs on the grounds that average labor productivity—and hence the wages of the remaining workforce—can be raised by doing so. These contracts have not yet spread widely, but they could compound the process of rapid labor productivity growth stemming in part from the shift toward capital intensive technologies, which has been associated with large falls in employment since 1990.

72. Finally, and as described in previous occasions, poor training and an inward oriented trade regime have contributed to the anti-employment bias in the South African economy. However, these factors can only account for unemployment if accompanied by wage rigidities. Therefore, even though the authorities are right to emphasize initiatives in these broader areas to stimulate employment, increased wage flexibility would contribute significantly to the early impact of these efforts to stimulate the growth of employment.

B. Youth Unemployment

73. The heavy concentration of unemployment among young people is one of the more striking aspects of the composition of unemployment in South Africa, and this is increasingly

reflected in the discussion of unemployment issues. The causes and nature of youth unemployment thus require particular attention in labor market issues.

74. In a context of slow employment growth, employers might prefer to recruit older people, implicitly placing young people in a queue. But it seems improbable that this could account for the extremely high rates of youth unemployment observed in South Africa (see Figure 5). Even if employers were to prefer older workers, high involuntary youth unemployment would not occur if the differentials between youth and adult wages adjusted to offset this behavior of employers. One possible explanation is that the wage-setting institutions in South Africa are having a particularly marked effect on youth if they are impeding the necessary wage adjustment in response to the employers' behavior.

75. There are three indirect pieces of evidence consistent with this proposition. First, preliminary research undertaken by the University of Witwatersrand suggests that high reservation wages do not account for high youth unemployment. Second, the recent ILO survey finds "that employers' preferred age for recruits is unusually high—between 26 and 35—considerably higher than is the case in the Philippines or Malaysia, with very few indicating a preference for youth between the ages of 16 and 25."²¹ Third, the ILO survey also finds that many firms provide some training to new recruits, but only 7 percent of the firms provide industry-accredited training, and that training is overwhelmingly focussed on high-level workers. New recruits therefore do not receive anything like adequate training, despite the obvious need for it. In addition to simply impeding the employment of young people, wage floors may impede the provision of training in the private sector by preventing young recruits from accepting remuneration in the form of training.

76. Although firms do pay young workers less than adults with similar skills, the Department of Labor reports that such differentiation is limited, to at most 10 percent, which is considerably lower than in other countries. In view of its importance, it would be critical to collect evidence of the circumstances under which differentiation is applied.

C. The Unemployment Rate

77. The official estimate of unemployment is derived from the October Household Survey (OHS) that is conducted by the Central Statistical Service (CSS). These unemployment data for black South African people are shown in Figure 5. The household survey is conducted

²¹Guy Standing, John Sender, and John Weeks (1996) p.340.

Figure 5
SOUTH AFRICA

UNEMPLOYMENT OF BLACK SOUTH AFRICANS, 1995

Source: October Household Survey 1995; and staff estimates.
1/ Including those wanting work but not actively seeking it.
2/ Excluding those not actively seeking work.

annually, on the basis of direct interviews with a large sample of households, and the survey covers a range of issues in addition to unemployment. The survey is used for the official estimate of unemployment because few of the unemployed are entitled to unemployment insurance benefits, so an estimate based on the latter will not be an appropriate measure of unemployment.

78. The survey defines the employed as those over 15 years old who, during the week prior to the survey, worked for five or more hours for a wage, profit, or family gain in cash or kind. This is a very comprehensive definition, as it includes many underemployed people and those engaged in informal sector activities. The official measure of unemployment defines the labor force to include the unemployed who want work, even if they take no action to seek it. Measurement and definitional issues arise in the assessment of this measure of unemployment. A number of these problems were raised by South African commentators and by researchers from the ILO, and are considered below.

Measurement issues

- Some respondents that are absent from work, on leave, or on strike may have been misenumerated as unemployed.
- Mine workers in hostels, workers in defense force camps, hospitals, hotels, and those working in old age homes were excluded from the survey.
- Respondents may mistrust the enumerators and therefore under-declare employment.

79. The concern, and corresponding bias, that people on leave or sick-leave might have been included as unemployed seems unlikely to be serious because subsequent questions on the questionnaire about activities would have clarified their status.

80. The under-enumeration of those resident in mining hostels is a well-known feature of the OHS surveys, to which the CSS has drawn attention, but results in a very small bias. It arises because enumerators have faced considerable personal risks in working in the mining compounds. But CSS calculations using the employment data reported by the mines show that adjusting for this gap would at most reduce the rate of unemployment by 1 percentage point. Similarly, the under-enumeration of those employed in army bases, hospitals, and old-age homes introduce insignificantly small biases.

81. The third measurement concern, arising from mistrust of enumerators, again appears unlikely to be a major source of bias in the official estimate of the unemployment rate. There are a number of ways in which mistrust could affect the data which have different implications for the extent and even the direction of the bias in the measure of unemployment, including (i) employed mistrusters could report themselves as wanting work but unemployed—implying that the OHS *overstates* unemployment rates but *correctly* estimates participation rates; (ii) employed mistrusters could report themselves as outside the labor force

altogether—implying a less significant *overestimate* of the unemployment rate than under the circumstances noted above, and an *underestimate* of participation rates; and (iii) unemployed mistrusters might also report themselves as outside the labor force, (to avoid attracting official attention as job-seekers)—implying that the OHS *underestimates* both unemployment rates and participation rates.

82. Moreover, if mistrust were a major factor affecting the results, one would expect both nonsensical results and substantial inconsistencies when comparing the various surveys of unemployment. However, the detailed results of the unemployment surveys in 1993, 1994, and 1995 are consistent. For example, the broadly defined unemployment rate for South African black males was estimated at 32 percent in 1993, 34 percent in 1994, and 29 percent in 1995. These results are also consistent with the 1993 survey conducted by a consortium of independent institutions, which estimated the unemployment rate (defined in the same way as the OHS) at 34 percent. These surveys also consistently show higher unemployment rates among women, in rural areas, and among young poorly-educated people, and they indicate that unemployment rates are most severe in the Eastern Cape, Kwazulu Natal, and in Northern Province, corresponding correctly with anecdotal evidence from commentators with direct experience regarding conditions in rural areas and townships. Moreover, some of these commentators suggest that the unemployment rates in these areas are understated in the official data. Accordingly, it is not clear that mistrust fundamentally affects the official surveys, nor is it clear that it would necessarily introduce an upward bias in the unemployment rate. Finally, even if mistrust played a part in weakening survey results in the past, mistrust has likely eased since 1994, with the coming of the new political dispensation.

Definitional issues

- Only those readily available for work, meaning those able to take up employment within one week, should count as unemployed, but the OHS puts no time limit on this.
- Those not engaging in active job search should be regarded as outside the labor force, not as unemployed.

83. Although surveys of unemployment in OECD countries generally define the labor force to exclude those not available for work within one week, even if they express a desire to work and are seeking it, it is not clear that the OHS approach to this issue is incorrect. If it were too lax, it would tend to generate estimates of participation rates—the proportion of people of working age in the population who are in the labor force—that are implausibly high. But as discussed below, the estimated participation rates are, if anything, very low, and restricting the definition of availability for work would reduce the estimated participation rates even further.

84. In addition, the definition of availability for work should reflect the particular features of the labor market in which it is applied. In South Africa, the spatial dislocation brought about by past segregation policies means that many unemployed still live at considerable

distances from job opportunities. As a result, a greater proportion of the unemployed would have to move residence to take up such opportunities than would be the case in, for example, OECD countries. This suggests that it might be appropriate to define availability for work over a longer time period. However, the way that the data are currently collected does not allow a study of the impact on the participation and unemployment rates of different definitions of availability for work.

85. Three issues should be considered in determining the appropriate statistical treatment of those who declare a desire to work but who do not engage in active search for work: (i) the impact of different treatments of participation rates; (ii) the nature of the incentives for the unemployed (who are willing to work) to engage in job search; and (iii) evidence of recruitment practices of employers.

86. The current treatment of non-searchers—to include them in the labor force estimates—seems adequate. If non-searchers were to be excluded from the labor force estimates, then participation rates, estimated at a little over 60 percent for black African males of working age, would be even lower. Compared with international participation rates among males of over 80 percent, South Africa's rate is puzzlingly low. The high incidence of students repeating years in school could partly account for South Africa's low participation rates relative to OECD countries, but the relatively low South African enrollment rates in tertiary institutions would tend to offset this.

87. Consideration of the incentives for active job search suggests that unemployed South Africans are less likely to engage in active job-search than their OECD counterparts, even with an identical willingness to work. Unemployment benefits in OECD countries are often contingent on active job search, creating a direct incentive to do so, but there is no such an incentive in South Africa. In addition, active search is more likely to be successful and lead to employment in the OECD—and to be remunerated in that way also—simply because the ratio of applicants to vacancies is substantially lower in OECD countries than in South Africa. This suggests that definitions of the labor force in South Africa should include non-searchers to a greater extent than would be appropriate in the OECD, and this supports the OHS approach to this issue.

88. Finally, there is survey evidence that suggests that recruitment practices by South African firms rely heavily on informal methods, buttressing the case against a requirement for active job-search in the definition of the labor force. For example, most firms that recruit production level workers use informal means of doing so: over 40 percent relying on friends and relatives of existing workers and a further 13 percent calling on former workers.²²

89. These considerations suggest that the authorities are right to focus on the definition of unemployment including non-searchers. There is, nevertheless, an important gap in technical

²²Guy Standing, John Sender, and John Weeks (1996) p.338.

knowledge about search behavior in South Africa that needs to be closed, including through formal studies using available data sets. For instance, if non-search is correlated with the rate of unemployment defined excluding non-searchers, controlling for other factors, then this would corroborate the inclusion of the non-searchers in the labor force because it would imply that non-search behavior is caused by the low prospective returns to search activity.

90. In addition to the measurement and definitional issues considered above, there are other factors that suggest that the official OHS estimates of the unemployment rates are *understated*—apart from the anecdotal evidence to this effect.

91. First, as explained above, the OHS defines as employed all those who worked in any form for at least 5 hours in the preceding week, thereby including underemployed people in the employment estimate. This number of hours is below the floor that is implicit in OECD surveys of unemployment because the unemployed are unlikely to accept employment with limited work hours if the associated earnings do not compensate for the loss of unemployment benefits. This puts an implicit floor on the number of hours of work that they will accept, which will generally substantially exceed 5 hours per week. Given the way the data are currently collected in South Africa, it is not possible to assess the extent to which the estimated unemployment rate would change by raising the minimum number of hours of work per week, but it is clear that the official measure of unemployment rate understates actual unemployment.

92. Second, as the CSS staff has noted, informal settlements and squatter camps, in which unemployment rates are thought to be extremely high, are under-enumerated. This is because the sampling frames for the OHS surveys were based on the 1991 census, and many of the informal settlements mushroomed after that time. The CSS statisticians consider that this downward bias is thought to be about 1 percentage point, roughly equal the opposite bias from undercounting in the mines, army bases, etc.

93. On balance, therefore, taking into account the institutional characteristics of the South African labor market, the officially estimated unemployment rate does not appear to be subject to significant upward measurement biases. If anything, there are both measurement and definitional concerns which suggest that the official estimates of unemployment could be too low.

D. Formal Employment

94. The principal formal employment series published by the SARB, based on data collected by the CSS, are shown in Figure 6. As with the unemployment data discussed above, a number of concerns with these estimates have been raised, including:

- Adjustments to the data were not applied retroactively, rendering time series inconsistent.

FIGURE 6
SOUTH AFRICA
EMPLOYMENT, 1970-96

Source: South African Reserve Bank.

- The monthly data are drawn from firms that reported to the most recent industrial census, so new entrants are undercounted, the samples used for the industrial censuses have been updated irregularly, data from the TBVC states have been doubtful,²³ and the response rate to the census has been around 70 percent with “busy” firms least likely to respond.
- There are discrepancies between the sectoral decomposition of employment between the OHS and the CSS employment series, with the estimates of the latter being lower for all sectors than those of the former.
- Illegal immigrants are likely to be excluded from the employment series.

95. The SARB data exclude agriculture. This avoids a number of difficulties with the inconsistent adjustments to long time-series data on agricultural employment, particularly regarding female employment. However, this means that total employment is understated and that the overall employment growth trends may be under- or over-stated in the employment series, depending on whether employment in agriculture is rising more or less rapidly than employment elsewhere in the economy.

96. It is not clear that the sample of firms being used by the CSS to estimate employment is outdated. For the industrial censuses—which are conducted every three years—the CSS updates its sample of firms by using its own business register, the Registrar of businesses, VAT lists, telephone books, Industrial Councils (IC), and Federations, etc. For the inter-census data, the CSS continually updates the sample of firms surveyed on the basis of new information on company registrations. Non-respondents are pursued, ultimately through the courts, which normally yields the necessary returns. The comprehensive list of sources being used, and the continuous updating of the sample suggests that, at the least, the methodology underlying the data is not systematically liable to induce undercoverage of new firms.

97. There could still be concerns about the coverage of the so-called informal sector in the non-agricultural employment time series data. But this series understates overall employment growth only if employment in the unmeasured (informal) sector is rising faster than the measured sector or vice-versa. In the absence of compelling evidence concerning which of these biases prevails over any given time period, the nonagricultural employment series remains the best available measure of long-term overall employment trends. It is therefore important to support the CSS’s efforts to ensure that the coverage of firms is as comprehensive as possible.

98. Another important issue is related to the smaller unmeasured firms because they may have more marked pro-cyclical employment behavior, as international experience would

²³Under the former political dispensation, employment data in these states were excluded from CSS estimates of South African employment.

suggest. In these circumstances, even though the employment series correctly reflect the underlying secular trend in employment, the cyclicalities of employment could be understated by this series. On this basis, employment may have fallen even faster in the early 1990s than is suggested by the nonagricultural employment series, while employment growth may have been stronger than recorded since 1994.

99. The SARB has made considerable efforts to adjust the CSS employment series to include employment in the TBVC states (Transkei, Bophuthatswana, Venda, and Ciskei) on a consistent basis in their data. In contrast, employment in these areas has only been included in the CSS estimates of South African employment in recent periods (giving rise to a step jump in their employment series). Accordingly, using the employment series of the SARB to establish short-term trends in the growth of employment would seem more appropriate than using the data of the CSS because they avoid the step-jump generated by the CSS treatment of the TBVC states. Nevertheless, the very considerable weaknesses in the employment data for the former TBVC states make such adjustments by the SARB problematic, and it is unclear if the "ghost workers" in the public sector in these states offset the underenumeration of employment elsewhere in these states.

100. Finally, it would appear probable that the discrepancies between the stock of employment from the OHS data and those from the employment series of the SARB can largely be accounted for by so-called "informal" activities as opposed to unenumerated "formal" employment. These discrepancies can be large, however. So while it may be appropriate to identify overall employment growth rates from those employment series—on the basis that employment growth (or contraction) in the sectors excluded from the employment data does not deviate substantially from that in the included sector—the employment series should not be used to estimate unemployment rates at any point in time.²⁴ The latter would substantially overstate unemployment. As discussed above, the official measurement of unemployment rates derived from the OHS would be more appropriate for this purpose.

E. Summary and Conclusions

101. Many factors appear to explain the high rates of unemployment observed in South Africa, and wage inflexibilities appear to play a significant role. Further basic statistical research is required to clarify the role of wage inflexibilities more precisely, and the Department of Labor may be best placed to establish the necessary reporting mechanisms.

102. The particular role of wage inflexibilities in youth unemployment also requires further research, to better establish its importance. The available evidence—on reservation wages,

²⁴For this reason, an earlier study of employment issues in South Africa (SM/95/9) described the difference between formal employment and the labor force as the "formal employment gap," not as unemployment.

employer's hiring preferences, and the composition of training provision by the private sector—points in this direction, and the GEAR proposal to scale down trainee wages may be a useful means of addressing this particular cause of youth unemployment.

103. The suggestion that the official data on unemployment rates substantially overstate actual unemployment is hard to defend. Given the very high unemployment rate among black South Africans, the authorities have appropriately defined job-creation as a key goal of economic policy.

104. The methodology underlying the nonagricultural employment time series also appears sound, and it is widely recognized that they do not cover the informal sector. They therefore provide a meaningful indication of secular employment trends although they may understate the cyclicity of employment.

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III. STRUCTURAL FISCAL REFORMS

105. The Government of National Unity has been designing and implementing substantial structural reforms in the public finances area. Moreover, the pace of fiscal structural reform on a variety of fronts has accelerated, and the process has been reinforced with the announcement of the GEAR, which in the public finances areas aim at (i) reducing government dissaving by lowering the size of the budget deficit; (ii) reallocating expenditure in ways that enhance economic growth and improve income distribution; and (iii) improving efficiency of the public sector. This section outlines some of these reforms, focusing on developments during the last year.

A. Poverty Alleviation and Social Sectors

106. Poverty alleviation is one of the most pressing problems facing South Africa. A comprehensive survey on poverty undertaken in 1993 indicated that the poorest 40 percent of households (representing 53 percent of the population) spend less than R 385 per adult per month (1993 prices, equivalent to US\$118), with the poorest 20 percent of households spending less than R 225 a month. Further, poverty is concentrated in certain communities and groups: 95 percent of the poor in South Africa are black people, 75 percent live in the rural areas, 53 percent are unemployed, and 45 percent are children under 16 years. More than three-quarters of the poor have no access to electricity, running water in the household, or modern toilets, and 90 percent did not complete secondary school. Several initiatives have been launched in the areas of welfare and land reform, and an update on poverty and inequality will be released later this year by the Office of the Deputy President, drawing on assistance from the World Bank and UNDP.

107. Social security and other welfare assistance play an important role in South Africa. In 1996/97, some 2.7 million people received some form of assistance. Of these, 64 percent were elderly (who receive the old-age pension),²⁵ 26 percent were disabled, and the balance were children, war veterans, and families. Social security assistance (old-age and veterans pensions, disability, child and family maintenance, and foster parent grants) accounted for more than 85 percent of the 1996/97 social services budget, while welfare assistance (elderly care in homes, child and family welfare, probation services, drug rehabilitation, community centers, population development) and capital expenditure comprised the balance.

108. Progress in implementing reform in critical social sectors—health, education, and housing—has been slower than envisaged in 1994, mainly as a result of the wide-ranging consultation efforts initiated by the Government ahead of the design of reform agendas in these areas. Rapid progress has also been delayed by a variety of physical and management

²⁵The old-age pension pays R 470 per month, and is available to everyone over 65 years of age subject to a simple means test. These payments are often the sole source of income for extended families.

bottlenecks to establish and operate the new procedures. Nonetheless, these constraints are being addressed, and expenditure and reform in these areas are accelerating, financed in part through a decline in military expenditure.

Welfare reform

109. A White Paper on the Social Welfare Services was tabled in Parliament in February 1997. In this context, following the merging of the 14 previous administrations into a single system, the Department of Welfare is implementing a five-year plan that aims to combine public and private financing options to alleviate poverty and to reduce racial and gender discrimination in the provision of social services. During this period, the social welfare delivery system will be restructured, with a focus on community development and less emphasis on specialized service. At present, nongovernmental agencies do the bulk of the delivery of non-social security welfare services, but they often lack resources. The Department of Welfare also plans to reduce fraud with the establishment of a National Social Grants Registry, first by concentrating on new registrants and then incorporating the private and civil service pension funds into the Registry.

110. Major changes have been announced for the child maintenance grant. The grant is presently set at R 430 a month for parents plus R 135 a month per child for up to two children younger than 18. Given that only 350,000 children receive the current benefit, very few of them in black families, the system is about to change. The Report of the Lund Committee on Child and Family Support that was issued in August 1996 recommended, inter alia, that the current scheme be replaced with a flat-rate, means-tested child benefit to be phased in over five years. This recommendation has been accepted by Cabinet, and a phased transition is scheduled to commence in August 1997, replacing the present system with a benefit set at R 75 a month per child six years old or younger. The new scheme is expected to benefit 3 million children. The cost of the new scheme is expected to be some R 2 billion—nearly double the current scheme.

Housing

111. The housing needs of South Africa are considerable; the urban housing backlog is variously estimated at around 1.3 million units, and that for hostels and rural housing at up to 1.7 million units. In addition, given population growth, there is a need for 200,000 new housing units per year.

112. The housing subsidy program was initiated in 1994. It offers up to R 15,000 per household and is intended to benefit up to 300,000 families a year; the average subsidy to date has been R 13,400 per application. There are two types of housing subsidies. *Project-linked subsidies* provide housing to developers within projects that have been approved by Provincial Housing Boards, who then re-sell the house at below market prices to an individual household. Between March 1994 and December 1996, 352,100 such houses had been initiated, of which 90,500 had been transferred to the final owner. *Individual subsidies* enable

persons to acquire an existing property or a property not located in a project approved by a Provincial Housing Board; over the same period, 39,400 such subsidies had been provided. The delivery of housing has been slower than initially envisioned, owing to uncertainty over the initial nature of the program and administrative deficiencies, lack of technical and managerial capacity, a vague line of authority at provincial and local government levels, and slow delivery of the essential infrastructure and of the upgrading of services in disadvantaged areas. As these constraints are being addressed, the delivery of housing, electricity, and water is gaining momentum.

113. Several other special housing programs have been initiated at the national level. The Mortgage Indemnity Fund (MIF) was established in June 1995 to protect financial institutions against losses due to poor loan recovery and encourage them to lend to previous "red-lined" areas. Almost 52,000 new housing loans in such areas have been granted since the establishment of the MIF, with a combined value of more than R 6 billion; the first claims against the MIF (which has a reserve of R 450 million) are expected in 1997. The National Housing Finance Corporation was established in April 1996 to promote non-traditional sourced lending for housing, and its activities will commence in 1997. In addition, since June 1995, Servcon has assisted occupants that had fallen into arrears on servicing their housing debts by either buying the property at subsidized rates, or relocating to a more affordable property. By September 1996, 3,400 sales and 3,900 relocations had been concluded.

Health

114. About 11 percent of total government expenditure or 3.5 percent of GDP has been allocated to health services. Nevertheless, the accessibility and quality of health services within South Africa varies significantly, and basic health indicators such as infant mortality are poor. Expenditure had been weighted towards care in hospitals; in 1992/93, just 10 percent of total public expenditure was spent on non-hospital primary services. Several initiatives to address these problems have been implemented in recent years. From 1994, free health care was made available to pregnant women and to children under six years; partly as a result, the share of primary care in total expenditure had increased to 20 percent by 1995/96.

Implementation of a program designed to restructure the national health system and provide universal health care was initiated in 1996. To support this program, 126 new clinics had either been built or were under construction by February 1997, and for the year as a whole, a further 270 new clinics and the upgrade of 326 clinics are planned, as is the provision of a further 150 mobile clinics. To encourage the use of these facilities by all citizens, hospitals will charge users fees when patients bypass the free primary care facilities in favor of hospitals. From April 1996 all permanent residents have been granted free access to publicly funded primary care.

115. Given budget constraints, the shift in public resources to primary health implies a corresponding reduction in public resources provided to hospitals. Yet reconstruction of the hospital system is also needed; a recent audit of hospitals indicated the cost for rehabilitation or replacement program at R 8 billion over 5-10 years. Several supplementary financing

options are being considered, including withholding by hospitals of the user fees, and mandatory private insurance for formal sector employees and its retirees for a minimum package of hospital benefits. The fee for this insurance would be based on income and the number of dependents, and the insurance fund would not be allowed to exclude individuals on the basis of their health risk.

116. Finally, several programs have been launched to promote better nutritional standards. The National Nutrition and Social Development Program distributes around R 400 million annually to support small-scale, agricultural and income-generating projects, and to provide food assistance to pregnant women and young children. In addition, the Primary School Nutrition Program disburses around R 500 million annually to 12,300 schools; in 1996, the program provided food equivalent to 25 percent of the daily energy requirements to 3.2 million children.

Education

117. Education reform is a national imperative—illiteracy levels are around 20 percent—but rapid progress has been difficult. Expenditure on education has been more than 22 percent of the total and some 7 percent of GDP in recent years. The share devoted to primary and secondary schools (around 75 percent) is comparable to that in other countries. However, within sectors, spending has been highly inequitable and its return on the level of resources has been low. In 1991/92, one third of total spending was devoted to the education of white children (who represented 13 percent of the school-aged population) and one half for the education of black children (who were 75 percent of the school-aged population).²⁶ As a result, average teacher-pupil ratios vary between 1:38 to 1:47 in schools with predominantly black children depending on the region, compared with around 1:25 in schools with predominantly white children. In addition, the budget share devoted to personnel expenditure is high and growing (around 75 percent in 1991/92, and almost 90 percent in 1997/98) with the consequence that few resources are left for expenditure on quality-enhancing instructional materials and other needs, such as upgrading of school buildings. Relatively high wages are in part the consequence of a policy whereby teachers' remuneration is linked to academic and professional qualifications rather than to academic responsibility; the net effect is that one third of the teachers are actively in training for subjects that are often not related to their current responsibilities, and that around one-third of teachers are inadequately trained. The system is also overburdened by a rapid rise in enrollment, owing in part to the increase in the number of years of guaranteed free education from 9 to 10 and the continuing high repeater ratios (at up to 50 percent for grade 1 alone, and around 20 percent for the whole school system).

118. In an attempt to deal with some of these issues, the 15 former departments of education have now been merged into a single unit, and national norms for teacher-pupil ratios

²⁶Statistics that classify students by race are no longer collected.

of 1:40 for primary schools and 1:35 for secondary schools have been established. However, it has proven difficult to transfer teachers from areas where retrenchment is necessary to areas where teachers are needed. In addition, the South African Schools Act was passed in 1996, establishing a uniform framework for the organization, governance, and funding of schools, and a National Qualifications Framework has been established. A Green Paper on Higher Education Transformation was published in 1996 for comment, and a study on senior secondary schooling is in progress.

Social infrastructural development

119. Several major social investment programs are underway in the context of the restructuring of expenditure and the alleviation of poverty. The telephone connection program is on track (a further 2.8 million new connections in houses, schools and clinics will be installed in the next five years (see below) as is the electrification program—1.75 million new connections over the period 1994 to 2000). Community water supply and sanitation programs have accelerated, and by the end of 1996, 700 water projects which will eventually benefit more than 6 million people had been committed. Expenditure on municipal infrastructure and amenities increased during 1996 as part of the national grants program, which worked directly with low-income municipalities via the Municipal Infrastructure Program coordinated by the national government. Under this program, 1,089 projects have been identified, of which 115 were completed and 369 are under construction. Private-public partnerships for delivery of municipal services and infrastructure have been initiated.

Land reform

120. Land reform efforts include a land restitution and land redistribution program. Restitution for those dispossessed of their land under apartheid is being addressed by the Land Claims Court, which became operational in 1996; 11,000 claims have been lodged, and 25 cases are expected to be finalized during 1997 (affecting around 50,000 people). The land redistribution program aims to increase access to the land market by the poorest groups through a market-based reform. The program includes a flat-rate grant of R 15,000 per household to either acquire rural or urban land, secure tenure rights, provide basic infrastructure on land and improve it, and/or acquire equity in an existing agricultural enterprise. Taking up this subsidy makes the household ineligible for the housing subsidy described above; thus far, planning grants have been provided to 240 communities. Finally, the Extension of Security of Tenure Bill is expected to be tabled shortly and aims to protect rights of existing tenants from “unfair” evictions.

B. Other Reforms

Reform of the civil service conditions of service and pension reforms

121. On April 19, 1996 an agreement was reached within the Chamber of Public Service Bargaining Council on a three-year adjustment package for a unified set of conditions for the

civil service of the central and provincial governments.²⁷ The agreement addressed the rationalization and simplification of salary scales and grades, a "rightsizing" civil service employment program, and the restructuring of public pension benefits. The agreement stipulated an increase in the cost of improvements in the conditions of service of R 8.5 billion over the 12-month period starting July 1, 1996—of which R 1 billion was to be paid from departmental savings—and a further R 6.5 billion increase in the wage bill for each of the two subsequent years. Furthermore, the agreement established that any budgetary savings arising from a voluntary rightsizing program that began on May 1, 1996 be used to fund additional salary increases of up to R 4.7 billion a year in 1997/98 and 1998/99. The Minister of Finance also agreed to a moratorium on mandatory retrenchment, and government ministers announced the intention to reduce staff positions by 300,000 over three years (out of 1.3 million employees at the national and provincial levels).

122. The various civil service pension funds were unified into a single fund, with the initial pension based on the average salary of the last 24 months of service (rather than that of the last day of service), portability and a cash resignation benefit were enhanced, and the government's contribution was lowered from 18 percent of the wage bill to 17 percent. The net effect of these changes to the pension funds was to reduce the level of funding of the civil service pension fund by some 2 percent (R 2.7 billion), although the financial position of the pension fund is expected to improve gradually as the current limit on the total assets that the pension fund can invest in traded stocks is raised from 20 percent to 65 percent.

123. Between June 1996 and March 1997, the voluntary retrenchment program led to the departure of 39,800 employees out of 58,000 applicants, and 18,250 unfilled funded positions were cancelled. However, during the second half of 1996 (latest available data) total employment at the national government declined on a net basis by only 4,400 and at the provincial government by only 800, reflecting in part the need to replace several of the skilled workers that departed under the voluntary severance program. In March 1997, the Minister of Finance announced that the voluntary severance program needed to be reviewed because the current costs of retrenchment were prohibitive.

124. Other changes in the pension system have also been initiated. Following the recommendations of the Smith and Katz Commissions, the government established the National Retirement Consultative Forum, which met in January and February 1997. The Forum established several theme committees, and a Green Paper is expected to be released for public comment in October 1997. The theme committees recommended that (i) an old-age pension grant should be retained and financed from general revenues, methods of phasing out the means test should be considered, and the compilation of a national register of social grants should be accelerated; (ii) a common private sector retirement age for all retirement vehicles

²⁷The new Constitution specifies that conditions of service for national and provincial employees will be legislated at the national level, although provincial governments retain the right to hire and fire.

should be established, a system of tax deferment should be retained with tax relief on contributions, and short- and long-term strategies to promote saving for retirement should be formulated; (iii) equality of tax treatment for public and private funds should be introduced by March 1998 (including for local authorities and parastatal plans), the investment strategy of the Government Employees Pension Fund should be considered, as should alternative public pension arrangements; and (iv) the appropriateness of using pension funds as vehicles to fund post-retirement medical benefits should be investigated, and the actuarial position of such schemes should be supervised.

Medium-term expenditure framework

125. The national and local authorities are establishing a medium-term expenditure framework for the national and provincial governments. This framework will be an instrument to better assess and scrutinize the financial implications of current and alternative departmental policies and spending programs within budget constraints, enable spending ministries to improve planning and reduce the size of their rollovers, and encourage greater efficiency within spending ministries. The authorities intend to incorporate a three-year framework into the 1998/99 budget, which will establish expenditure by the national and provincial governments. Co-ordination between the different levels of government will be undertaken through the Budget Council, as well as between respective spending ministries at the national and provincial levels. At the same time, the authorities are developing a medium-term personnel framework, with assistance from the British Department for International Development (formerly the Overseas Development Administration), to rationalize employment in the areas of health, education, police, and defense.

The Katz Commission

126. In June 1994, an independent tax commission (the Katz Commission) was appointed to conduct a review of selected aspects of South Africa's tax structure and, in particular, to provide recommendations for tax changes, most of which have been adopted. A Tax Advisory Committee is also engaged in a detailed study of tax issues, providing input to the Katz Commission. To date, the Commission has released five interim reports (November 1994, June and December 1995, and April and May 1997). The first three recommended changes in (i) the personal income tax (by reducing the number of brackets from ten to five, instituting a flat rate of nine percent on annual taxable income up to R 30,000, and setting a maximum marginal rate of 45 percent on incomes above R 150,000); (ii) the corporate income tax (by reducing the Secondary Tax on Corporations and eventually replacing it with full or partial imputation system, and the implementation of a presumptive tax on company gross assets); (iii) the VAT (by broadening the base by narrowing zero-rating and eliminating exemptions); and (iv) the taxation of retirement income (by establishing equal treatment of discretionary and contractual savings and of public and private schemes, and raising the taxation of retirement income in the form of lump-sum withdrawals). They also recommend a strengthening of tax administration by modernizing computer facilities, improving tax assessment and audit

procedures, enhancing taxpayer education, and endowing the revenue service with more flexibility in respect of employment and wage policy.

127. The most recent two reports covered the taxation of capital transfers, and whether income taxes should be based on world wide income of residents regardless of source (the “residency” principle), or on the source of income regardless of residency of the recipient (the “source” principle). On the former, the Katz Commission recommended that donations and estate duty taxes be retained and not combined into a single tax, the exemption from estate taxes for bequests in favor of a surviving spouse be retained, an exemption for bequests to specified non-government organizations be allowed, a capital gains tax be periodically imposed on trusts that intend to skip generations, and distribution of capital from trusts be subject to a capital transfer tax. On the latter, the Katz Commission recommended that the taxation of active income continue to be based on the source concept, while passive income be taxed on a residency basis, procedures to prevent avoidance be tightened, greater recognition of foreign tax credits be undertaken, the tax exemption provided to interest flowing to foreign portfolio investors be continued, and a special tax dispensation be introduced to encourage the retention of international headquarters and holding companies.

128. Further interim reports are being drafted covering the introduction of a land tax at the local government level, the tax dispensation of medical aid schemes, friendly societies, and other benefit funds, the taxation of mineral rights, and the taxation of nongovernmental organizations. In addition, a holistic report on the tax system is to be prepared by November 1997. Finally, the government has announced its intention to simplify the Income Tax Act over the next several years, and make greater use of tax reference numbers to minimize tax evasion, including requiring a declaration of good standing to make tender applications for government contracts and to receive government assistance.

South African Revenue Service

129. To address revenue collection problems in recent years—including the build up in tax arrears—and the departure of 13 percent of senior and other staff from tax administration agencies in 1996 alone, in April 1996, the Inland and Customs Departments were merged to form the South African Revenue Service (SARS). The SARS is expected to be made autonomous, within the civil service, with the right to set its own wages and salaries and to finance itself by withholding 1-1½ percent of collections. Further, to rationalize the customs system, the number of international airports that can clear cargo will be reduced from 35 to 10, and the number of border posts will be reduced from 100 to 16; minimum import values are also being imposed.

Restructuring of state assets

130. Progress has been made toward the restructuring of state assets, in accordance with the National Framework Agreement signed between the government and organized labor in January 1996. The program aims at improving competitiveness in firms, promoting human

resource development, widening share ownership, and stimulating entrepreneurship within the black community. In late 1996, the government sold six radio stations, raising R 516 million; the proceeds were used to reduce domestic debt. In March 1997, 30 percent of the shares of Telkom was sold to a foreign consortium for R 5.6 billion; of this amount, R 4.4 billion will remain in the company to finance the above-mentioned 2.8 million new connections over the next five-year period in exchange for a five-year exclusivity (monopoly) period; the balance is to be used to reduce central government debt. A further 10 percent of equity of Telkom is expected to be sold to enhance black empowerment.

131. The government has announced that further sales this year will include Sun Air (a regional carrier) and Aventura (a tourist resort company). Various restructuring options include seeking a strategic partner for the Airports Company and for South African Airways; other plans for Safcol (a state forestry company) and Alexkor (a diamond mining company) are being considered, as is the restructuring of Transnet (a holding company for transportation and communication activities) after the problems associated with its large unfunded pension and medical liabilities are resolved. Finally, Eskom (the electricity company) is to be moved under government ownership (it currently has no shareholders, having been formed by an Act of Parliament), and consolidation of its distribution activities into a limited number of regional utilities is being considered.

Financial management

132. A reform of risk management philosophies and principles for government finances is being implemented so as to strengthen financial practices. All funding activities that are currently performed by the Reserve Bank on behalf of the government are being ring-fenced from its monetary operations, and the Department of Finance will become directly accountable for all management matters over its own debt. Primary dealers in government bonds will be appointed in a phased manner (the number is still to be determined), whereupon the functions of market-making and the selling of bonds will be shifted from the Reserve Bank. The present tap system to market government debt will be replaced with a tender or auction system, along with a variety of other structural reforms covering settlement periods, surveillance, risk management, and capital requirements.

133. In January 1996, the Cabinet endorsed the establishment of a formal cash management system within the Department of Finance to eventually remove overlaps between the Departments of Finance, State Expenditure, and the Reserve Bank in the management of the exchequer balances and other public sector cash reserves. In this context, the management of the tax and loan accounts and of the bank accounts of spending ministries would be transferred to the Department of Finance. Several reforms in cash management have already been implemented. Restrictions on cash-in-hand have been introduced, departmental disbursements are matched closer with actual spending, interest earned on statutory deposits such as the National Housing Fund are now credited to the Treasury instead of the relevant department, and the government is smoothing its debt funding peaks. Accounting standards are also to be improved, as is the management of domestic and foreign debt.

IV. THE NEW INTERGOVERNMENTAL STRUCTURE IN SOUTH AFRICA

134. South Africa has recently moved from an intergovernmental budget structure, which gave little effective discretion over revenue, expenditure, and borrowing to subnational levels, to one which provides considerable expenditure flexibility to the new nine provinces; local governments have not yet been incorporated into the arrangements. This section describes the new intergovernmental structures, assesses their features against a set of criteria, and notes their implications for other fiscal policies. The effects of the civil service wage agreement, and the financial situation of local governments are also described.

A. Intergovernmental Structures in South Africa

135. Until recently, there were three asymmetrical subnational government structures in South Africa. There were four states (Transvaal, Orange Free State, Natal, Cape), which were essentially administrative arms of the central government, with 95 percent of their financing arising from earmarked transfers from the national government; the state administrations had the right to reallocate expenditure within the same functional spending category, but not between functions, and were not allowed to borrow for any purpose.

136. There were 10 homelands: four TBVC "independent states" (Transkei, Bophuthatswana, Venda, and Ciskei), and six "self governing territories" (Gazankulu, Kangwane, Kwandebile, Kwazulu, Lebowa, Qwaqwa), each with their own government. The homelands had considerable discretion over their expenditure, and there was little accountability or transparency in their operations. These were financed by a limited own revenue base (10-20 percent of total resources), transfers from the central government, soft loans from the Development Bank of Southern Africa, and borrowing that was often guaranteed by the central government. Typically, the four states and ten homelands overspent—often by wide margins—and this was covered by further transfers from the central government. Finally, there were three "own administrations" associated with the tri-cameral parliamentary system covering the white, colored/mixed, and Indian populations.

137. The interim and final constitutions established three levels of government: national, provincial, and local. While the final Constitution became effective on February 3, 1997, legislation to support the new fiscal relations is expected to be passed later in 1997, and implemented from January 1998. The provinces and homelands were replaced in 1994 with nine provinces, each with its own government (ranked from smallest to largest in terms of budgeted expenditure in 1997/98: Northern Cape, Mpumalanga, Free State, North-West Province, Western Cape, Northern Province, Gauteng, Eastern Cape, and Kwazulu/Natal). The Constitution requires that the services provided by each province be of a similar standard.

138. Under the new intergovernmental relations, the national government will no longer compile expenditure and revenue estimates of the provincial governments, although it will be available to assist them to do so. Instead, with provincial governments responsible for determining their own budget process, the national government will focus on setting uniform

norms and standards for the country as a whole (see below), controlling the national spending departments, and enhancing financial management and training. Aspects that are still to be determined include establishing and enforcing national priorities over the medium-term, setting those norms and standards, determining equitable revenue shares given the regional disparities, and handling unforeseen expenditure.

139. The Constitution also specifies that the Financial and Fiscal Commission (FFC) will provide advice on the development and maintenance of the new intergovernmental financial and fiscal relations. In addition, a Budget Council has been established as a co-operative decision-making body consisting of the Minister and Deputy Minister of Finance, the nine provincial Ministers of Finance, and officials of the Department of Finance, State Expenditure, and Provincial Treasuries. The Budget Council is charged with recommending the revenue-sharing arrangements to the national government, taking into account the FFC recommendations. The national government reserves the right to accept or modify these recommendations.

Expenditure responsibilities

140. The Constitution specifies some exclusive areas of competency for the provincial and local governments, but there is joint responsibility between the national and provincial governments for the largest expenditure: non-tertiary level education, health, welfare, and to a lesser extent, housing. In 1997/98, almost two-thirds of provincial expenditure is expected to go to education and health, of which over three-quarters is for the payment of wages and salaries (Table 1).²⁸ The Constitution also specifies that conditions of service for national and provincial civil services will be legislated at the national level, although provinces retain the right to hire and fire. Major national concerns include defense and foreign affairs, most of police and economic services expenditure, and interest payments.

141. To implement these requirements, provinces maintain the major responsibility over education and health, subject to the norms and standards set by the national government. Housing is currently a responsibility of the national level, but may be shifted to the provincial

²⁸Specifically, around 40 percent of provincial government expenditure is for primary and secondary education, teachers and technical colleges, and special education; almost 90 percent of this expenditure is for personnel costs; 22 percent is for health services, although in provinces such as Gauteng that supply academic health facilities this share increases to 34 percent of total expenditure, with 55 percent of this expenditure for personnel costs; and 20 percent of their expenditure is for social security and welfare, where the provinces simply serve as a channel for payments made to individuals under national government norms.

Table 1: Indicators of Revenue Expenditure, and Social Diversity among Province

	Northern Cape	Mpuma- -langa	Free State	North- West	Western Cape	Northern Province	Gauteng	Eastern Cape	Kwazulu/ Natal
1997/98 provincial revenue (in percent):									
Revenue/GDP	0.3	0.8	1.0	1.1	1.5	1.7	2.2	2.3	2.6
National transfers/total provincial revenue	96.6	96.0	92.2	95.5	94.4	95.4	94.1	97.8	95.3
Share of transfer/total national transfer	2.5	6.0	6.9	8.4	10.9	12.9	16.1	17.1	19.3
1997/98 share of provincial expenditure for:									
Education	34.5	42.2	35.6	38.6	34.7	36.8	36.7	34.4	37.7
Health	15.9	21.1	23.3	16.7	26.0	15.5	34.3	18.8	22.8
Welfare 1/	27.0	...	14.9	15.4	23.8	14.4	17.1	20.2	20.6
Other functional categories	22.7	25.7	26.3	29.2	15.5	33.3	12.0	26.6	18.8
Wages and salaries	46.3	...	53.5	...	...	59.9	50.7	55.2	...
Social indicators (in percent):									
Provincial population/total population	1.8	7.3	6.7	8.1	9.0	13.1	17.1	15.7	21.1
Adult illiteracy rate (1991)	20	25	16	31	5	26	8	28	16
Rural population/provincial population (1995)	27	68	47	72	14	91	6	65	63
Poverty rate in province (1993)	57	52	66	57	23	57	19	78	53
Provincial poverty/total national poverty (1993)	1	9	9	9	4	18	6	24	21
Children aged 5-17 (1995)	26	29	26	28	26	36	23	31	31
Pensionable aged group (1995)	6	5	5	5	6	5	6	6	5
Personal income tax/national average 2/	110	99	88	57	163	28	221	44	75

Source: Financial and Fiscal Commission, May 1996; RDP, Indicators of Poverty, October 1995; 1997/98 Provincial Budgets; Budget Review 1997/98; and Fund staff estimates.

1/ Health and welfare combined for Mpumalanga, and shares refer to 1996/97 Budget.

2/ Per capita collections per province relative to national average in 1995/96 fiscal year.

level at a later stage. The establishment of civil service wages and salary rates for both the national and provincial governments is centralized. The level of government responsible for the provision of all or part of welfare services is to be determined.

Revenue responsibilities and distribution

142. While the Constitution is explicit concerning the assignment of expenditure responsibilities, it requires only that there be an "equitable" distribution of nationally raised revenue between the national, provincial, and local levels. Provinces may not charge taxes, levies, duties, or surcharges on corporate income, value added, property rates, or customs duties; they may charge a flat surcharge on the tax base of personal income or excises.

143. In May 1996, the FFC published recommendations on the distribution of nationally collected revenue between the national and provincial governments (the vertical share), and between the provinces themselves (the horizontal share). Regarding the vertical share, the FFC recommended that the current ratio of national to provincial government expenditure shares shift in favor of the provinces by 0.5 percentage points a year. This was based on the assumption that the demand for services from the provincial authority will grow with the population, while many services provided at the national level will not do so (e.g., defense).

144. Regarding the horizontal share, the FFC recommended that the inter-provincial allocation of resources be based on (i) a minimum standards component to ensure that the education and health standards in each province meet the national objectives; (ii) a spillover component for academic hospitals; (iii) a fiscal capacity equalization component to compensate provinces with small tax bases; (iv) an institutional grant set at a flat amount per province to defray the cost of basic legislative and administrative costs; and (v) a distributional factor based on the population of each province, with an added weight for the share of the rural population as a proxy for poverty. While the formula should remain unchanged for at least three years to provide for stability in planning at the provincial government level, the formula would be phased-in over six years to limit adjustment costs.

145. The national standards component is intended to ensure a minimum level of basic human capital in the form of primary and secondary education, and primary health care. The education component would ensure that there are sufficient funds to employ primary school teachers in the ratio of one teacher per 40 children with a secondary school teacher-student ratio of 1:35, as well as to fund average non-salary costs.²⁹ The formula is not intended to address backlogs in infrastructure in some provinces relative to others. The health component would be based on 0.5 trip a year to primary care facilities for those with private health care, and 2 trips a year for those without (rising gradually to 3.5 trips a year as the primary care

²⁹In 1996, the average salary of a teacher, including bonuses, was R 61,000 a year, and non-wage costs were around 40 percent of wage expenditure. This implied an average grant per child of R 2,250 a year.

system is expanded).³⁰ The small spillover component would finance training of doctors at academic hospitals which have externalities for other provinces (Gauteng and Western Cape have these facilities and thus have high shares of health in total expenditure).

146. The fiscal capacity equalization component is based on the principle that provinces should generate some revenue to cover part of their expenditure, particularly at the margin. As indicated in Table 1, provinces currently derive around 95 percent of their total revenue from transfers from the national government. The FFC notes that if virtually all revenue continues to come in the form of transfers on which the provinces have no discretion, there would "be an invitation to spend recklessly, because the provincial government would be absolved from having to justify its expenditure programme to its constituency, while the total obligation to raise taxes would rest on the national government."³¹ To address this potential problem, the FFC suggests that provinces be allowed to levy a flat surcharge of up to 12 percentage points on the personal income tax rate that is collected in their territory. Personal income taxes that accrue to the national government would then be reduced by a uniform 7 percent for all provinces, although the transfer from the national government to each province would be reduced by just half of the 7 percent (regardless of the rate the province chooses for the surcharge). Apart from the small "institutional capacity" grant, the remaining funds would be distributed on a per capita basis, with the portion of the rural population weighted by 1.25 times;³² after having subtracted the above items from the total pool of funds, this component would comprise around 45 percent of the total transfer.

Borrowing arrangements

147. The Provincial Governments Borrowing Act was passed in 1996 and defines the borrowing rights of the provincial governments as specified in the Constitution. The bill prevents provinces from borrowing to finance current expenditure (with the exception of bridge financing that is repaid within twelve months). Borrowing for capital expenditure must meet the approval of a loan coordinating committee, which the Minister of Finance chairs and who has veto power. Borrowing by a province (including borrowing through provincial enterprises or development corporations) is capped by a limit on the annual gross interest payments (including all forms of finance charges and deferred interest) relative to current revenue. The provision of a national guarantee on provincial borrowing requires an Act of Parliament.

³⁰The average cost was R 240 a visit in 1996.

³¹Financial and Fiscal Commission, *The Allocation of Financial Resources from the National and Provincial Governments for the 1997/98 Financial Year*, May 1996, page 14.

³²Rural shares of total provincial population vary from less than 15 percent in Gauteng and Western Cape, to more than 90 percent in Northern Province. Table 1 seems to indicate a positive correlation between poverty and rural population shares.

Arrangements for 1997/98

148. While the FFC's proposals are being considered, the Budget Council has recommended a somewhat different approach for 1997/98. Before sharing revenue between the national and provincial levels, a claim on nationally collected revenue was given to certain prior expenditure commitments, comprising: (i) interest on public debt (including debts of the former TBVC states); (ii) increases in civil service salaries; (iii) expenditure that had originally been initiated under the Reconstruction and Development Program (see Section I); and (iv) a contingency reserve and certain extraordinary items, while taking into account the projected budget deficit reduction.³³ After funding this "top slice," the balance of the revenue collected was divided between the national and provincial governments using the same share as in the 1996/97 budget after subtracting the same items, which yielded 77.4 percent of the remaining revenue accruing to provinces. The distribution to each province (the vertical distribution) was broadly in line with that recommended by the FFC.

B. Assessment of the New Intergovernmental Arrangements

149. International experience with intergovernmental relations suggest the critical factors that determine success includes the following areas :

(i) Expenditure issues, such as how allocative efficiency is reconciled with national priorities and standards, how national standards are enforced without resorting to unfunded mandates, and whether provinces have sufficient administrative capacity to operate effectively;

(ii) Revenue issues, such as how the national and provincial revenue assignments are specified, and how the revenue and expenditure assignments link responsibility with accountability; and

(iii) Borrowing and macroeconomic issues, such as whether the arrangements enable control over the deficit for general government; and whether the general government deficit can be adjusted for macroeconomic needs.

Expenditure assignments

150. Expenditure assignments are allocatively efficient when responsibility for each type of expenditure is assigned to the level of government that is closest to the final beneficiaries of these outlays. The new arrangements are consistent with this approach: the national

³³Since all borrowing accrues to the national government to pay for its expenditure, the total amount of revenue available for distribution between the national and provincial levels has to be reduced by the magnitude of the change in the programmed budget deficit so that the burden of adjustment is not borne only by the national government.

government maintains a strong role in the provision of public goods such as defense and foreign affairs, while responsibility for most of the other expenditure items is allocated to the provinces. The establishment of broad national norms and standards in important expenditure areas reflects an appropriate balance between allocative efficiency and equity goals.

151. Studies of fiscal relations in other countries suggest that it is also desirable for the national government to remain responsible for expenditure that has a strong aggregate demand impact that is subject to the business cycle (such as unemployment benefits, which are small in the case of South Africa), and where there is a need to pool risk. The latter concern suggests that it would be more efficient for the national government to be responsible for the provision of old-age and other pension benefits—it currently sets the statutory amounts and eligibility criteria—especially since enrollment in these programs has been increasing and the need varies by province.³⁴ A similar case could be made for the new nationally legislated child allowance (see Section III), where the take up rate is currently very uncertain. Further, the operating offices for the pension and child allowance benefits should remain under the national government to ensure proper vetting procedures. If responsibility for these programs were kept at the national level, total transfers to provinces would have to be reduced by around 12 percent. Other welfare assistance could be the concern of subnational levels, so that these programs are tailored toward the specific needs of the area.

152. It is important that the norms and standards set by the national government do not become unfunded mandates, and that the provincial priorities for their own expenditure are consistent with those for the country overall. In this regard, it is timely that the Department of Finance is developing a three-year medium-term expenditure framework, with close co-operation of the provinces, which together will set national and provincial priorities within a sustainable expenditure envelope (see Section III). The medium-term expenditure framework will also have another advantage; given that it is based on existing policies, it will indicate the cost to the provinces of conforming to the national standards, and the transparency of this approach will reduce any incentive for the national government to set unfunded mandates that the provinces will find hard to meet.

153. One aspect that is still to be determined is how the norms and standards set at the national level are to be monitored and enforced. To perform this function, an effective method to share provincial expenditure data needs to be established, as well as a system to centrally monitor the delivery of services (as opposed to just the expenditure) according to nationally set social objectives. Thus far, provinces are required to submit monthly cash plans at the start of the fiscal year, and to provide two budget updates during the year; it is possible that more frequent sharing of expenditure data will be required.

³⁴For example, the share of welfare in total expenditure in the Northern Cape is double that in some other provinces.

154. Realizing actual efficiency gains in expenditure can be undermined by institutional constraints on the administrative capacity of some provincial governments (including overstaffing, poor technical skills and training, inability to formulate and implement effective spending programs), and inability to develop modern and transparent expenditure management systems (including adequate financial control, reporting, accounting, and evaluation of expenditure programs). Improvements in a number of areas to achieve sound public expenditure management systems, especially for the provinces that have the weakest administrative capacity, have been identified (Box 3). Although the need is large, the process is likely to take time. It requires: (i) a clear definition of assignments to avoid duplication and waste; (ii) the establishment of clearly defined intergovernmental transfers that result from a formula-based approach; (iii) modern and comprehensive standardized budget classifications and accounting procedures; (iv) rolling plans that are exchanged between governments and regularly updated; (v) modern and computerized accounts-based systems to enable monitoring and control of all phases of government to help prevent arrears; and (vi) common audit and evaluation channels. The national government is also considering the possibility of centralizing wage payments to ensure that there are no wage arrears; in such an event, wage payments will be deducted from the transfers to each province. As explained below, however, provinces could influence the size of the wage bill through their employment policies.

Revenue responsibilities

155. The Constitution specifies that the national government should tax the bases that are mobile, sensitive to income changes, and are unevenly distributed across regions; this suggests a national focus on taxes on corporate income, natural resources, and foreign trade. Accordingly, the FFC's recommendations to provide limited taxing powers to the provincial governments are appropriate. As the FFC notes, arrangements which assign almost all taxing powers to the national government are undesirable since they separate spending authorities from revenue-raising responsibilities and obscure the link between benefits of public expenditures and the taxes needed to finance them.³⁵

156. The FCC recommends that the personal income tax is an appropriate base for a subnational surcharge since its base is typically less mobile than that for other taxes. To minimize distortions, the tax base—as opposed to the rate—should be the same country-wide. A surcharge on the personal income tax can, however, be difficult to administer. It requires knowledge of a taxpayer's residence (as opposed to the place of employment), creating

³⁵Nevertheless, not all taxing powers should be assigned to provincial or local areas because this deprives national government of a macroeconomic tool and has income inequality problems.

Box 3. Budget Features of the Nine Provinces

Northern Cape (population 0.9 million; received 2.5 percent of 1997/98 transfer):

- large distances with little economies of scale in spending
- low rate of job creation and high share of budget spent on welfare
- difficulties attracting skilled public staff; lack of co-ordination between ministries

Mpumalanga (population 3.0 million; received 6.0 percent of 1997/98 transfer)

- recent improvements in capacity to deliver and budget planning processes
- need for improved expenditure data by department

Free State (population 3.1 million; received 6.9 percent of 1997/98 transfer):

- second poorest province with large welfare needs
- need for improved budget planning and a strategic plan

North-West Province (population 3.9 million; received 8.4 percent of 1997/98 transfer):

- traditional sectors of mining and gambling in decline
- large rural population with high illiteracy and poverty rates
- difficulty attracting skilled civil staff

Western Cape (population 4.0 million; received 10.9 percent of 1997/98 transfer):

- relatively wealthy with potential for tourism and industrialization
- poverty levels are half the national average

Northern Province (population 5.7 million; received 12.9 percent of 1997/98 transfer):

- large rural share; high rate of poverty; poor basic infrastructure; low tax capacity
- large civil service with low productivity
- budget process and co-ordination among departments need strengthening

Gauteng (population 8.6 million; received 16.1 percent of 1997/98 transfer):

- relatively wealthy with strong tax capacity based in Johannesburg-Pretoria area
- produces half of direct taxation and poverty levels are one-third the national average
- planning and finance link strengthened via medium term expenditure framework
- large risk of underestimating welfare payments which are provincial responsibilities

Eastern Cape (population 7.5 million; received 17.1 percent of 1997/98 transfer):

- rural share at 65 percent; low job creation; high welfare needs; low tax capacity
- lack of administrative capacity and infrastructural development
- difficulties integrating former homeland states into an integrated civil service

Kwazulu-Natal (population 9.5 million; received 19.3 percent of 1997/98 transfer):

- large infrastructural backlogs
- low level of capacity in many departments, especially in local government
- need for better links between planning and finance

Sources: IDASA Budget Information Service, *Budget Watch*, March 1997; and Table 1.

problems for taxpayers that currently earn less than the income threshold where they would be required to submit a tax return (currently R 60,000 a year), and for individuals that earn income across several provinces. An alternative would be to set the personal income tax surcharge on the basis of the location of the employer, although, if employers were allowed to register in any province for tax purposes, there would be an element of tax competition between provinces. Nonetheless, given that the top marginal personal income tax rate is already fairly high in South Africa, an alternative to the surcharge would be to base the system on an indirect tax. While there would also be serious co-ordination problems for multi-stage taxes like the VAT, selected excise taxes are possible candidates. As these would encourage avoidance of such taxes by crossing provincial lines, these tax rates may also need to be fairly similar across provinces.

157. Several other issues arise in the context of the FFC's recommendations. The FFC recommends that the surcharge on the personal income tax be capped (at 12 percent). However, the link at the margin between additional expenditure and additional revenue will not be effective after this level is reached; should any further expenditure be undertaken, given that the provinces would not be allowed to augment their revenue through an increase in the surcharge, the national government will as now have to choose between declaring the province in default, or transferring additional resources. In addition, the flexibility that the link between different levels of expenditure and different levels of the surcharge provides to provinces depends in part on the overall degree to which provinces have meaningful discretion over their own expenditure. As noted above, much of their expenditure is already determined by the norms and standards set at the national government and by the centralized setting of civil service wages and conditions (see below). Finally, the independence granted to provinces in determining their tax revenue surcharges may come into conflict with the announced policy of the national government to maintain the tax to GDP share at about its current level. This suggests a need to adjust total revenue accruing to the national government to the extent that higher collections are made at the provincial level to maintain the overall tax share.

Aggregate borrowing and macroeconomic stability

158. The establishment of an institutional forum to consider macroeconomic coordination of budget policies within a multi-year setting is a sound principle. It is also appropriate for the central government to maintain strong control over borrowing and debt; on balance, the rules based approach that has been adopted is preferable to a discretionary approach because it is more transparent and stable. Any borrowing should be in the own name of the province, although this may be hard to enforce in practice.

159. One difficulty for macroeconomic stability arises as a result of the large level of resources that are allocated to provincial governments, which therefore may have to play an active part in fiscal management. This issue was highlighted in the 1997/98 Budget, where over half of the reduction in the projected deficit as a share in GDP came from a decrease in provincial transfers. In this context, an issue arises concerning how revenues are to be allocated as they vary over the business cycle. One approach could be to keep the level of

resources made available for recurrent expenditure—such as education and health—constant in real terms, while varying the level of provincial capital spending. Another approach, which is followed in some countries, where provincial revenues are based on a formula, is to have discretionary transfers of the national government during downturns which are financed by national government borrowing. The establishment of a contingency may be helpful in this regard.

C. The Civil Service Wage Agreement

160. The three-year wage bill agreement described in Section III raises a number of issues regarding several of the new intergovernmental arrangements. Civil service costs are the largest component of provincial expenditure, but wage levels are negotiated at the national level which limits provincial discretion over their own expenditure, which was one of the goals in establishing the new intergovernmental relations. While provincial governments have the right to hire and fire, the wage setting provisions are especially constraining because provinces also have to meet the national standards covering, for example, the teacher-pupil ratios at the primary and secondary education levels, and teacher salaries are the largest expenditure item for provinces.

161. Further, the interplay between the civil service agreement and the distribution of revenue on the basis of formula has several implications. Provinces receive allocations based on existing staff rather than current need. However, given that the civil service agreement essentially attempts to specify the total cost of provincial and national government salaries, savings from “right sizing” are to be used to fund further wage increases for those that remain. This implies that provinces that initially have either sufficient or too few civil servants in absolute terms will find their wage costs increased due to the savings that accrue to the provinces where there is currently an excess of personnel; this seems to disadvantage provinces that do not start with excessive civil services. This could be corrected by reallocating transfers among provinces in a discretionary fashion, but it would contradict the stable nature of the revenue sharing arrangements and would not provide an incentive for a province to downsize.

162. Finally, because the wage bill is set in nominal terms, shocks to GDP or the adoption of a more ambitious deficit reduction program affects the wage/nonwage split of each province. This was evident when the deficit target (excluding extraordinary revenue) was lowered—in accordance with the GEAR—from 5.6 percent of GDP in 1996/97 to 4 percent in 1997/98. In consequence, wages and salaries are now 49 percent of non-interest expenditure of the national and provincial governments, compared to 44 percent in 1995/96 (the year before the civil service agreement became effective). Table 1 shows the share of wages at the provincial government level is even higher and hence that the compression of the wage/nonwage split may have been more extreme.

D. Local Governments

163. Local governments play an important role in the fiscal system of South Africa, although they have not yet been incorporated into the new intergovernmental structure. Spending by the 835 municipal budgets was around 7.5 percent of GDP in 1996/97, including capital expenditure of 1.8 percent of GDP. Six metropolitan councils and their substructures account for half of total local government expenditure. Loans amounting to 55 percent of planned capital expenditure were budgeted in 1996/97. In principle, local governments have a substantial tax base compared with provincial governments, as own revenue accounts for 90 percent of their collections (charges on utility services electricity, water, and sewerage), which are bulk purchased from suppliers and sold to final users, property rates, and a turnover tax of 0.25 percent). In recent years, local governments have collectively had a deficit of just 0.2 percent of GDP; borrowing is restricted in the same way as for provincial governments.

164. Until recently, there were two groups of local governments. White local authorities (WLCs) which had significant revenue raising capacity and fiscal autonomy; revenue was mainly derived from local property taxes and the sale of electricity and water purchased from the utility companies; grants from the national government and the TVBC states were equivalent to just 3 percent of their total revenue. Black local authorities (BLCs), in contrast, lacked economic activity and hence a revenue base to be self-sufficient, and were therefore effectively wards of the state; their revenue from housing rents and utility charges was limited by payment boycotts, with the consequence that over 85 percent of the BLCs' revenue came from intergovernmental grants. Partly in response to this structure, debt to local governments, especially the BLCs, have recently increased due to nonpayment by households of the property rates and services provided to them by local governments. These debts have reached R 6.5 billion or 25 percent of annual property rates and service income, threatening the viability of several local governments. In turn, local governments owe R 26 billion.

165. The Constitution requires that local governments receive an "equitable" share of nationally raised revenue, which suggests that local governments will in future receive a higher share of their resources from the national government, with offsets from the provincial governments. In the interim period, the Local Government Transition Second Amendment Act of 1996 enables the national government to set limits on the rate of growth of local government expenditure. For each municipality, this rate of growth was set at 10 percent for 1996/97, and was reduced to 8 percent (for both current and capital expenditure) for 1997/98. The Act also envisioned monitoring at the provincial instead of the national level; this function is expected to be devolved in 1998/99. Finally, to start to alleviate the debt problems, "Project Liquidity" was launched in 1996, with teams from each province charged with visiting every municipality and reporting its cash flow problems, conducting detailed assessments, and making appropriate recommendations.

V. SOUTH AFRICA—CAPITAL LIBERALIZATION STRATEGY

166. The debate on the pace of liberalization of capital controls on residents in South Africa has been similar to discussions being held in many countries. The government has repeatedly indicated its intention to remove these controls, as part of its broader program to reduce inherited distortions in the economy, in a step-by-step manner. However, episodes of strong pressures on the rand, linked to rumors and speculation of an imminent removal of all capital restrictions, intensified the debate on this issue in 1996. This section provides a brief overview of capital controls in South Africa, describes the progress made in liberalizing these controls in recent years, reviews the arguments for and against faster liberalization, and concludes with an assessment of the current strategy.

A. Background

167. Comprehensive exchange controls were introduced in South Africa in 1961 to contain the large capital outflows that followed the "Sharpsville massacre." Nonresident capital transactions were restricted through the blocked rand mechanism, which insulated the capital account from movements of equity capital by permitting sales of blocked rand only to other nonresidents. This system remained in place until 1983 with some changes that widened the scope of blocked rand transactions, the introduction of the securities rand (1976) and, subsequently, the financial rand (1979). The introduction of the financial rand mechanism stimulated foreign direct investment by authorizing nonresidents to purchase local currency at the financial rand rate to finance investments in quoted securities and, with the specific approval of the Exchange Controls Department, in nonquoted shares. The various mechanisms governing nonresident transactions alongside comprehensive controls on residents severed the direct link between South African and international interest rates.

168. A comprehensive review of exchange controls was carried out under the auspices of the de Kock commission in the early 1980s. The commission recommended the eventual elimination of all exchange controls on nonresidents while retaining limited controls on residents. The financial rand mechanism was abolished, following these recommendations and the successful stabilization that followed the gold price boom in the early 1980s. Restrictions on residents were maintained, however, because of concern about the impact of a sudden removal of controls on the exchange rate and on the real estate and stock markets, although a more liberal attitude was adopted toward the applications by local firms to borrow abroad and toward certain types of investments overseas. Capital controls were reimposed in August 1985, as a consequence of a combination of adverse economic developments, an intensification of political pressures, and the imposition of international financial sanctions. At the same time, South Africa declared a debt moratorium ("standstill") on repayments of private debt to foreign commercial banks. These steps were part of a broader reversion to a more inward-oriented economic program, including additional trade protection.

169. This regime of controls remained broadly in place until the Government of National Unity took office in May 1994. An important element of the policy framework of the new

government was the removal of exchange controls. However, its room for maneuver in this area was restricted by a number of factors, most notably, the large size of potential capital outflows if institutional investors were to diversify their portfolios with foreign assets, the blocked emigrant funds, South Africa's low level of international reserves, the size of the net open forward position of the SARB, and the lack of a track record in implementing the macroeconomic policies necessary to support a capital liberalization program.

170. In these circumstances, the authorities adopted a "pragmatic" approach to exchange controls, indicating that controls would be gradually phased out when conditions were appropriate, while proceeding with a comprehensive economic program that would facilitate the eventual removal of all exchange controls. This program included the constitutional independence of the SARB, commitments to progressive reductions in the deficit of the central government and inflation, a program of trade liberalization under the auspices of the WTO, and a multi-year program of reform of labor market legislation and institutions, as well as preparation for benchmark sovereign issues and for ratings by the private international agencies.

B. Liberalization in the Last Three Years

171. The authorities made rapid progress in establishing appropriate conditions for their liberalization program. South Africa's position in the international financial market began to improve gradually in the early 1990s, with some South African private sector borrowers, the government, and public enterprises regaining access. International confidence greatly improved following the peaceful transition to majority rule in May 1994, the end of international financial and economic sanctions, and the strengthening of the domestic economy, and the authorities' commitment to cautious financial and structural policies. These developments were further reinforced by favorable ratings of the government's external debt by international credit rating agencies. As a result, following a decade of net outflows, the capital account turned positive in 1994, reflecting in part the government's successful placement of a global bond issue for US\$750 million in December 1994. By the end of 1994, net international reserves had increased to about half a month of imports, despite the emergence of a current account deficit in 1994.

172. The favorable shift in sentiment regarding the rand and the attendant strengthening of the capital account provided the backdrop for the first major step in eliminating capital restrictions—the abolition of the financial rand on March 13, 1995 and with it, all controls on nonresidents. This represented a major structural change, as it reestablished the direct link between international and South African interest rates by removing the buffer between them that was represented by the discount on the financial rand.

173. The SARB progressively tightened monetary policy in response to emerging inflationary pressures and the contagion effects of the Mexican crisis, and to support the planned exchange control liberalization. It raised the bank rate from 12 percent to 13 percent in September 1994, and to 14 percent in February 1995; doubled the reserve requirement on

banks' total nonreserve liabilities to 2 percent in February 1995; and set ambitious guidelines for the growth in M3, supplemented by bank-by-bank guidelines on growth of credit to the private sector. As a result of the tightening of monetary conditions and rumors of the eminent abolition of the financial rand, long-term bond rates increased from 14.5 percent in June 1994 to 16.9 percent by September 1994 and remained at about that level through the first half of 1995. This increase in interest rates suggests that the market expected that the abolition of the financial rand would result in future higher short-term interest rates. The exchange rates for the commercial and the financial rand began to converge, and the discount on the finrand fell below 10 percent for several weeks and then to 3.6 percent on the day of the abolition of the finrand. Thus, the successful abolition of the finrand, as reflected by the stability in the exchange rate following unification, was clearly a consequence of careful preparation and sound macroeconomic policies, and the establishment of credibility in the monetary stance.

174. The elimination of the finrand was followed by continued short-term capital inflows through the first half of 1995 and a substantial increase in international reserves. This facilitated progress in moving ahead with the relaxation of controls on residents. Consistent with the authorities commitment to the step-by-step approach to ensure that the reform was not disruptive to financial markets, the SARB eased controls on residents and partially withdrew from the forward market. The general approach underlying the strategy followed by the authorities with regard to the former, was not simply to liberalize controls in a sequence of steps that allowed different types of capital transactions one at a time, but to open a number of new windows, each subject to a cap, that would permit different types of capital transactions by residents. In this way, an increasing array of forms of resident capital transactions were permitted, but the risks of major aggregate outflows were limited by the caps applied to each type of transaction. This feature of the step-by-step approach allowed the authorities to gradually increase both the range of authorized capital transactions and the scope of each of these transactions by raising the caps. This process can be continued until all types of resident capital transactions are permitted and until the caps are no longer binding. Once the latter is achieved, the caps can be removed without risking further capital outflows.

175. Accordingly, in July 1995, the government authorized insurance companies, pension funds, and unit trusts to invest a portion of their assets abroad by way of swap arrangements with foreign investors interested in South African assets, thereby enabling these financial institutions to diversify their portfolios with foreign assets. To the extent that the inflows from nonresidents would have not occurred anyway, these swap operations would not affect South Africa's reserve position. Total swaps were subject to a cap of 5 percent of the total assets of these financial institutions. Subsequently, the government permitted these institutions to acquire up to 10 percent of the government's £100 million Euro-sterling issue launched in January 1996, and relaxed the conditions on direct investment by South African companies in countries in the Southern African region.

176. Also in July 1995, the SARB announced its intention to withdraw gradually from the forward market and encourage the development of a private market for forward transactions in which it might participate on its own initiative from time to time. In this context, it

abolished the requirement for exporters to obtain forward cover, limited its participation in short-term cover to financial transactions, and began to reduce progressively the subsidy on cover of short-term borrowing.

177. Notwithstanding the outflow of capital that began in mid-February 1996, the government made further progress in relaxing exchange controls on residents with the introduction of a number of measures in the context of the GEAR in June 1996 (Annex II). These measures included an increase in the limit on total swaps from 5 percent to 10 percent of total assets of the eligible institutions; permission for these institutions to place abroad in 1996 up to 3 percent of net asset inflow during 1995, subject to the overall 10 percent limit of assets; a further easing of conditions on residents to invest in the Southern African region; a more liberal access to domestic credit by nonresidents; more flexible exchange arrangements for exporters and importers; and substantial increases in the limits on various current account transactions.

178. With the strengthening of sentiment regarding the rand in early 1997, additional measures to relax exchange controls on residents were introduced in conjunction with the 1997/98 budget, with some of the corresponding limits expected to be announced by June 30, 1997. These measures include permission for individuals to make portfolio investment abroad and to hold foreign currency accounts in the domestic banking system; the elimination of, or further increases in, most limits on current account transactions; permission for corporations to raise foreign funding for investment abroad on the basis of their balance sheet; a broadening of the types of institutions eligible to enter into asset swap arrangements; permission for these institutions to transfer abroad in 1997 of up to 3 percent of the net asset inflow during 1996, and to invest an additional 2 percent of their assets in securities in the SADC region (subject to the overall 10 percent limit of the institutions' total assets); and a further relaxation on domestic borrowing by nonresidents.

C. Arguments for More Rapid Liberalization

179. The government has been urged to remove capital controls on residents at a faster pace, or what has generally been referred to as a "big bang" approach. Some have argued that capital controls are ineffective in stemming capital flight in any meaningful way, and that they are costly to maintain. Others, in contrast, have maintained that capital controls had been effective because of the general support that the previous regime enjoyed from the affected group, who viewed the controls as a necessary tool to isolate the country from internal and external pressures. Irrespective of which argument is an apt description of the behavior of individuals, the fact remains that a major stock of personal savings in South Africa is with financial institutions, which have been, and continue to be, effectively prevented from diversifying abroad by the existing controls. On this basis, the maintenance of limits on outward investment has led to a situation where domestic savings must be invested locally, thus inflating domestic asset and real estate prices and distorting investment decisions.

180. In this context, some have insisted that foreign direct investment was bridled by uncertainty about the timing of the removal of controls and its potential effect on the exchange rate, thereby delaying direct foreign investment decisions. Moreover, a number of analysts have stressed that the mere existence of exchange controls intensify the volatility of the exchange rate, as economic agents speculate on the timing and scope of the gradual steps.³⁶ They have maintained that the cost of uncertainty and volatility in the exchange rate may be even more damaging in the medium-term than that associated with a depreciation that may follow a rapid removal of controls. These analysts point to the episodic depreciation of the rand during 1996, arguing that the movements in the exchange rate were exacerbated by speculation that wholesale exchange control liberalization was imminent. In light of the political timetable of South Africa, they consider that further delays may increase uncertainty and thus increase pressure on the rand.

181. Another reason for a “big bang” is that the removal of capital controls will actually lead to an increase in net inflows, rather than to net outflows, and hence the concern of the government and others regarding its impact on the exchange rate and the economy are groundless. The experience shows that many countries enjoyed large capital inflows—including returning flight capital—following the removal of capital controls.

D. Arguments for Gradual Liberalization

182. A number of arguments for a gradual liberalization of capital controls in South Africa have been advanced on the basis of the special circumstances facing South Africa. First, the large visible stock of capital awaiting liberalization, including (i) the blocked funds that emigrants were forced to leave behind—which amount to R 15-20 billion—and are generally expected to exit quickly once granted permission; and (ii) the large stock of asset—estimated at more than R 600 billion in September 1996—held by financial institutions, such as pension funds and insurance companies, the managers of which have repeatedly expressed their desire to diversify their portfolio by investing abroad a significant portion of those assets. While this portion is difficult to forecast, even a modest one, say, about 10 percent, could have unsettling effects on the exchange rate and the domestic economy.³⁷ Second, it has been generally

³⁶The governor of the SARB, Dr. Stals, stated on February 20, 1996 that one of the disadvantages of exchange controls is that their sheer existence always leads to rumors and speculations about their removal.

³⁷Many of the advocates of a “big bang” approach acknowledge that this is a problem, but argue that the institutions are good “corporate citizens” and would not act in a manner that would damage the country by diversifying their asset base too rapidly and putting undue pressure on the exchange rate. Also, it is not in their own interest to do so. Others have suggested that these institutions could adopt voluntary restraints to prevent such an undesirable outcome. However, these arguments ignore the strong incentive for each

(continued...)

argued that capital controls in South Africa were more pervasive and more effective than in other countries, suggesting that capital flight was considerably lower than in other cases. This would imply that the pool of assets in South Africa awaiting to leave is relatively larger than was the case in other countries.

183. Third, returning capital flight may be less of a factor in South Africa than it has been in other cases because of the original motive for the capital flight. In many of the Latin American countries, for example, capital flight was motivated by policies that led to high and accelerating inflation in the context of controls on interest rates. In these countries, the removal of capital controls coincided with the implementation of major adjustment programs leading to high returns on capital, which attracted flight capital back to the country. In the case of South Africa, much of the capital flight may have been motivated by political concerns, and thus the removal of capital controls is not likely to induce a substantial return of capital, despite the peaceful transition to majority rule.

184. Finally, the removal of capital controls in South Africa may not have the same effect as in other liberalizing countries because their liberalization also applied to nonresidents who took advantage of the new investment opportunities, while these investors already face no restrictions in the case of South Africa.

185. On the more general issue that foreign direct investment is being hampered by the gradual relaxation approach because investors are expecting an imminent liberalization that could lead to a large depreciation, this would suggest that investors are ignoring the very strong signals and evidence provided by the authorities in this policy area. The authorities have repeatedly stated that they will liberalize gradually when conditions are appropriate to protect the external value of the rand, and they have provided ample proof in their actions of their commitment to their step-by-step approach; each step they take in this direction reduces the likelihood of a wholesale removal of controls. The elimination of the financial rand and the progressive reduction of capital restrictions on residents—which addressed some of the diversification needs—have been implemented successfully, without any evident impact on the rand. Moreover, as indicated above, the strategy itself allows for measured relaxation that reduces risk of a sizable depreciation. Finally, as the authorities have stated, the government has nothing to gain from not following the stated policy and surprising the market because this may destabilize the exchange rate and precipitate an even greater outflow.³⁸

³⁷(...continued)

institution to move ahead of the other, and invest abroad before its assets lose their value, and the probability that voluntary restraints in such times could easily unravel.

³⁸Dr. Stals made this point to a business group on March 7, 1996: "...The speculation that the next round of exchange control relaxations will lead to a major downward adjustment of the exchange rate of the rand, was presumptuous. If the Reserve Bank was of the opinion that
(continued...)

E. Conclusions

186. The issues raised by exchange control liberalization have changed fundamentally since the GNU began dismantling the inherited regime of controls in 1995. The government has now a track record of sound overall economic policies, and it has demonstrated its capacity to implement major step-by-step reforms without financial disturbances and without coming under pressure to reverse the steps that have been taken; and its commitment to the step-by-step process leading to full liberalization of exchange controls is now firmly established. The abolition of the finrand, which has reestablished the direct link between domestic and foreign interest rates, and the major steps to relax controls on residents that have already been taken represent substantial achievements compared with the prevailing situation in early 1994.

187. Notwithstanding the progress made thus far, the merits of persisting with the step-by-step approach remain persuasive. Perhaps most critically, markets continue to react negatively to rumors that the step-by-step process might be abandoned in favor of substantially more radical steps. Their concern focus in particular on the prospect that part of the large stock of personal savings held with financial institutions and the blocked emigrant funds might flow abroad, and that there is likely to be more pent-up demand for capital to exit abroad than capital that would be attracted in.

188. The above factors underscore the appropriateness of persisting with the step-by-step approach, but it is important to ensure that this approach remains credible and that it is properly sequenced relative to reforms in other areas. Uncertainty about the process could have discouraged foreign inflows due to the risk of a large unanticipated depreciation. However, the authorities successful track record in implementing this approach to date, their strong commitment to it, their revealed aversion to actions that might risk financial disturbances, and the use they are making of a gradual adjustment of the caps on resident capital transactions should all help to allay those concerns.

³⁸(...continued)

further relaxation could lead to a large outflow of capital, the Bank will not advise the Minister to proceed with the programme. This is indeed the main reason for the Reserve Bank's approach of gradualism in the phasing-out of exchange controls—each step must be carefully considered not to lead to unstable financial conditions in the country. This includes, of course, the objective of maintaining relative stability in the exchange rate of the rand.”

VI. THE VOLATILITY OF THE SOUTH AFRICAN RAND

A. Introduction

189. As described in Section I, the South African rand came repeatedly under pressure in foreign exchange markets during 1996, depreciating more than 28 percent against the U.S. dollar from mid-February to end-December. The instability of the exchange rate started with the large depreciation of February 16 (3.9 percent), and was followed, initially, by high volatility and, subsequently, by a phase of relative calm (Figure 7, top panel). Renewed bouts of instability appeared during the rest of the year, most notably in April, and to a lesser extent in July, October and December 1996. In each of these periods, exchange pressures were reflected in additional falls in the exchange value of the rand. These developments, and in particular the fact that turbulence was clustered around certain periods (and by implication so was tranquility) led to the impression among observers that the South African rand had been excessively unstable during 1996. The volatility of the rand is shown in the day-to-day percentage changes in the lower panel of Figure 7. The figure suggests that the variability of the rand during the first quarter of 1997 was similar to that in the second half of 1996, despite the strengthening of the rand vis-à-vis the U.S. dollar.

190. The issue of exchange rate volatility—as well as in other asset prices—has generated an extensive academic literature.³⁹ Among other empirical regularities of nominal exchange rates under floating regimes (such as the random walk property, the fat-tail phenomenon, etc.) a majority of studies indicate that nominal exchange rates are more volatile than most “fundamentals,” and that variability of the exchange rate seems to be time-varying, or more precisely, autocorrelated (i.e., the volatility clustering noted above for the rand). To our knowledge, no study on the volatility of the rand has been recently published, and this section is an attempt in bridging this gap.⁴⁰ In particular, this section addresses the issue of whether the rand had actually been excessively volatile in 1996.

191. The methodology used in this chapter is simple and it is based on the presentation of basic graphs and on the calculation of standard volatility measures. The analysis is eminently univariate, centered on the nominal exchange rate and, thus, it ignores other variables, such as money supplies, interest rates, incomes, market expectations, central bank interventions, etc., that could be potentially important (albeit in complex ways) to understand the determination of floating exchange rates. In order to address the question of the rand's volatility, two different benchmarks for comparison were used. First, an international benchmark—provided

³⁹The early literature is surveyed in Baillie and McMahon (1989), and more recently in Frankel and Rose (1995). An incomplete list of recent papers addressing the issue of exchange rate volatility would include Hodrick (1990) and Bartolini and Bodnar (1996).

⁴⁰The most recent studies on the properties of the floating rand in academic journals are those by Gidlow (1987, 1988).

Figure 7. South Africa--Exchange Rate, January 1, 1991 - March 31, 1997

Source: IMF Treasurer's Department, Rates Maintenance System

by the behavior of floating currencies from other countries—would give an indication to what extent the rand conforms to other floaters. Second, a historical benchmark—provided by the financial rand—was also looked into because it could shed some light on South Africa's own past experience with what was widely perceived as a volatile exchange rate.

B. International Comparisons

192. The analysis was conducted using the exchange rates of seven currencies (the German DM, the Japanese yen, the United Kingdom's pound sterling, the Canadian dollar, the Australian dollar, the New Zealand's dollar and the Mexican peso) against the U.S. dollar during 1991-97:Q1. These currencies cover a quite diverse group of countries, ranging from the large industrial to the smaller economies. With the exception of the peso, which had an exchange rate band until December 1994, all of the above currencies floated against the U.S. dollar for the entire period, although both the DM and the pound were participants of the Exchange Rate Mechanism of the European Monetary System (the pound's participation ended in September 1992).⁴¹ These exchange rates (in domestic currency units per U.S. dollar) and their daily percentage changes (with a common scale to ease cross-currency comparisons) are plotted in Figures 8-14.

193. To complement the graphical analysis, two simple statistics were calculated: the standard deviation of the daily percentage changes and the mean absolute daily percentage change (MADPC). Both statistics are widely used in the literature on exchange rate volatility,⁴² and the most important difference between them is that the standard deviation is more sensitive to outliers than the MADPC. In addition, with a view to appreciate the virulent movements that exchange rates can display, the maximum absolute daily percentage change is also reported. These statistics were calculated year by year for 1991-96 and for the first quarter of 1997 (Table 2).

194. Figures 7-14 and Table 2 confirm some stylized facts documented in the literature, and reveal some new features. First, nominal exchange rates are very volatile. An MADPC in the 0.2-0.5 percent range is common, and the maximum absolute percentage change in each

⁴¹Daily exchange rates were taken from the representative rates that are reported by these member countries to the Fund and are later published in the IFS, except for Mexico, where the Reuters daily ask rate was used.

⁴²See Mussa (1979, 1986, 1990), Baillie and McMahon (1989) and Isard (1993).

Figure 8. Germany--Exchange Rate, January 1, 1991 - March 31, 1997

Source: IMF Treasurer's Department, Rates Maintenance System

Figure 9. Japan--Exchange Rate, January 1, 1991 - March 31, 1997

Source: IMF Treasurer's Department, Rates Maintenance System

Figure 10. United Kingdom--Exchange Rate, January 1, 1991 - March 31, 1997

Source: IMF Treasurer's Department, Rates Maintenance System

Figure 11. Canada--Exchange Rate, January 1, 1991 - March 31, 1997

Source: IMF Treasurer's Department, Rates Maintenance System

Figure 12. Australia--Exchange Rate, January 1, 1991 - March 31, 1997

Source: IMF Treasurer's Department, Rates Maintenance System

Figure 13. New Zealand--Exchange Rate, January 1, 1991 - March 31, 1997

Source: IMF Treasurer's Department, Rates Maintenance System

Figure 14. Mexico--Exchange Rate, January 1, 1991 - March 31, 1997

Source: Reuter's Reuterlink. International Spot Currency Prices, Mexican Nuevo Peso (ask price).

Table 2. Volatility of Daily Exchange Rates

	South Africa Rand/US dollar	Germany DM/US dollar	Japan Yen/US dollar	United Kingdom Pound stg/US dollar	Canada Can dollar/US dollar	Australia Aus dollar/US dollar	New Zealand NZ dollar/ US dollar	Mexico Peso/US dollar
1991								
Number of observations	241	250	246	253	249	251	239	251
Standard deviation of percentage change	0.404	0.867	0.593	0.786	0.183	0.369	0.385	0.083
Mean absolute percentage change	0.295	0.626	0.453	0.579	0.132	0.273	0.271	0.051
Maximum absolute percentage change	1.473	4.144	2.766	2.829	0.916	1.958	2.322	0.490
1992								
Number of observations	247	253	251	255	252	253	231	251
Standard deviation of percentage change	0.392	0.905	0.571	0.961	0.302	0.424	0.375	0.166
Mean absolute percentage change	0.294	0.669	0.421	0.683	0.230	0.302	0.282	0.106
Maximum absolute percentage change	1.548	3.190	3.246	5.025	1.150	2.003	1.504	0.841
1993								
Number of observations	242	252	248	253	251	252	233	250
Standard deviation of percentage change	0.329	0.704	0.689	0.795	0.314	0.557	0.397	0.451
Mean absolute percentage change	0.241	0.551	0.505	0.596	0.244	0.424	0.294	0.164
Maximum absolute percentage change	1.755	2.121	3.457	3.032	1.041	2.246	1.960	4.061
1994								
Number of observations	248	251	246	252	249	221	247	256
Standard deviation of percentage change	0.418	0.611	0.635	0.426	0.269	0.491	0.309	1.987
Mean absolute percentage change	0.261	0.466	0.483	0.317	0.203	0.360	0.231	0.445
Maximum absolute percentage change	2.497	2.182	3.766	1.528	0.953	1.756	1.119	22.592
1995								
Number of observations	244	250	248	252	249	246	243	259
Standard deviation of percentage change	0.266	0.818	0.942	0.494	0.335	0.494	0.377	2.301
Mean absolute percentage change	0.168	0.567	0.659	0.353	0.240	0.376	0.284	1.314
Maximum absolute percentage change	1.262	4.413	5.072	2.438	1.623	1.714	1.751	15.894
1996								
Number of observations	248	250	244	254	251	249	248	260
Standard deviation of percentage change	0.641	0.438	0.470	0.360	0.196	0.413	0.359	0.346
Mean absolute percentage change	0.377	0.333	0.366	0.263	0.145	0.296	0.260	0.259
Maximum absolute percentage change	3.873	1.724	2.256	1.624	0.662	2.169	1.531	1.156
1997-Q1								
Number of observations	60	61	58	61	62	60	58	63
Standard deviation of percentage change	0.413	0.581	0.572	0.541	0.278	0.529	0.427	0.384
Mean absolute percentage change	0.320	0.469	0.471	0.444	0.219	0.417	0.339	0.233
Maximum absolute percentage change	1.133	1.603	1.377	1.304	0.811	1.408	1.283	2.127
1991-1997-Q1								
Number of observations	1530	1567	1541	1580	1563	1532	1499	1590
Standard deviation of percentage change	0.426	0.736	0.663	0.670	0.273	0.465	0.371	1.251
Mean absolute percentage change	0.275	0.533	0.481	0.465	0.200	0.341	0.272	0.388
Maximum absolute percentage change	3.873	4.413	5.072	5.025	1.623	2.246	2.322	22.592

year is often 1-2 percent.⁴³ Second, the phenomenon identified above as the time-varying variability of exchange rates is present and, hence, the volatility of all exchange rates appears to cluster (as does tranquility) around certain periods. For example, the volatility of the DM increased steadily during 1995, and then was rather limited in 1996 (Figure 8). Third, and less widely known, is the fact that the currencies of major industrial countries (Germany, Japan, and the U.K.) show larger volatility than those of smaller industrial countries (Canada, Australia and New Zealand). The MADPC of the yen, the DM, and the pound is about 0.5 percent for the entire 1991-97:Q1 period, while that for the currencies of the smaller industrial countries in the sample is closer to 0.3 percent. Exchange rates of the two developing countries in the sample (South Africa and Mexico) tend to behave like those of small industrial countries (MADPC of 0.28 percent and 0.39 percent respectively for 1991-97:Q1), except in periods when they face currency crises, in which case volatility increases substantially.

195. A comparison of episodes of exchange rate turbulence, namely, South Africa in 1996, United Kingdom in 1992, United States in 1995 (reflected in the DM and yen rates to the U.S. dollar), and Mexico in 1994-95 (all episodes represented by shaded cells in Table 2) shows that volatility in the rand was smaller than that in the other currencies. The MADPC was 0.38 percent for the rand compared with 0.68 percent for the pound, 0.57 percent for the DM, 0.46 percent for the yen, and 1.31 percent for the peso (in 1995). Differences in the maximum absolute percentage change are even more striking. While the rand depreciated 3.87 percent on February 16, 1996, the pound depreciated by 5.03 percent on September 17, 1992, the DM appreciated by 4.41 percent on May 26, 1995, the yen depreciated by 5.07 percent on August 16, 1995, and the peso depreciated by 22.59 percent on December 22, 1994. One caveat should be born in mind regarding the analysis of currency crisis episodes: there is a sample selection bias in this study because the episodes were selected with the benefit of hindsight. Nonetheless, these results show that the volatility of the rand in 1996 was not exceptionally high relative to other high turbulence cases.

C. Historical Comparisons: The Financial Rand

196. Another benchmark to which it is interesting to compare the recent volatility of the rand is the behavior of the financial rand. As an instrument of exchange control, the main objective of the finrand was to regulate nonresident investment into South Africa. With the abolition of the finrand, there was a concern that its instability could have been shifted to the unified foreign exchange market. Thus, to the extent that volatility in 1996 was associated to capital flows of nonresidents, the finrand could provide some clue of the instability that could be expected from such flows.

⁴³As an illustration, at the recent exchange rate of the rand of about R 4.47 to the dollar, the MADPC range implies variations of one to two cents per day. For the purposes of this section, qualitative inferences regarding exchange rate volatility are very similar using the standard deviation.

197. The analysis in this section parallels (in terms of the use of charts and statistics) the international comparisons in the previous section, but it is carried out using monthly data from the SARB's Quarterly Bulletin. Exchange rates for the comrand and the finrand are averages for the period. Figure 15 shows both exchange rates for the 1985-96 period and Table 3 displays the statistics.

198. Given that the period under consideration includes the aftermath of the balance of payments crisis and standstill of 1985, the period 1985-86 was excluded because the finrand was extremely volatile as the mean absolute monthly percentage change (MAMPC) was around 5.6 percent. The data reveals that the volatility of the rand in 1996 pales in comparison with the experience of the finrand: MAMPC of the rand was 2.38 percent in 1996, compared with 4.82 percent of the finrand during 1987-95.

D. Summary and Conclusions

199. This section is a first-pass attempt into addressing the issue of whether the rand had actually been excessively volatile in 1996. In order to address this question, two different yardsticks were used; namely, an international benchmark—provided by other floating currencies—and a historical benchmark—provided by the financial rand.

200. Evidence reviewed here confirms some of the stylized facts documented previously in the literature, but it also reveals some new features. Concretely, the data show that the variability of the South African rand tends to be similar to the variability displayed by the currencies of small industrial countries, except in periods when the rand has faced strong pressures, in which case the rand's volatility increases substantially. However, volatility in the rand was smaller during 1996 than in selected episodes of other currencies' exchange rate instability. In addition, the historical analysis shows that the volatility of the rand in 1996 was considerably lower than that recorded by the finrand in 1987/95.

Figure 15. South Africa
(Monthly, January 1985 - December 1996)

Exchange Rate (Rand/US dollar)

Month to Month % Change: Commercial Rand

Month to Month % Change: Financial Rand

Table 3. Volatility of Monthly Exchange Rates in South Africa

	Commercial Rand	Financial Rand
1985		
Number of observations	12	3
Standard deviation of percentage change	7.773	21.030
Mean absolute percentage change	5.577	19.331
Maximum absolute percentage change	20.256	24.418
1986		
Number of observations	12	12
Standard deviation of percentage change	7.906	13.153
Mean absolute percentage change	5.660	10.657
Maximum absolute percentage change	15.525	22.761
1987		
Number of observations	12	12
Standard deviation of percentage change	2.192	11.562
Mean absolute percentage change	1.694	8.944
Maximum absolute percentage change	6.010	28.726
1988		
Number of observations	12	12
Standard deviation of percentage change	2.499	8.555
Mean absolute percentage change	2.410	6.967
Maximum absolute percentage change	5.427	15.846
1989		
Number of observations	12	12
Standard deviation of percentage change	2.984	4.282
Mean absolute percentage change	2.659	3.287
Maximum absolute percentage change	6.197	8.961
1990		
Number of observations	12	12
Standard deviation of percentage change	1.312	5.678
Mean absolute percentage change	1.019	4.392
Maximum absolute percentage change	2.664	10.772
1991		
Number of observations	12	12
Standard deviation of percentage change	1.925	2.268
Mean absolute percentage change	1.584	2.025
Maximum absolute percentage change	4.290	3.650
1992		
Number of observations	12	12
Standard deviation of percentage change	1.771	6.060
Mean absolute percentage change	1.476	6.009
Maximum absolute percentage change	3.895	10.714
1993		
Number of observations	12	12
Standard deviation of percentage change	1.279	4.771
Mean absolute percentage change	1.223	3.605
Maximum absolute percentage change	3.596	11.022
1994		
Number of observations	12	12
Standard deviation of percentage change	1.465	4.207
Mean absolute percentage change	1.120	3.660
Maximum absolute percentage change	3.813	6.208
1995		
Number of observations	12	2
Standard deviation of percentage change	0.664	3.681
Mean absolute percentage change	0.510	2.603
Maximum absolute percentage change	1.694	4.671
1996		
Number of observations	12	
Standard deviation of percentage change	2.410	
Mean absolute percentage change	2.382	
Maximum absolute percentage change	7.064	
1987-95		
Number of observations	108	98
Standard deviation of percentage change	1.967	6.488
Mean absolute percentage change	1.522	4.815
Maximum absolute percentage change	6.010	28.726

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South Africa: Tax Summary as of April 1, 1997

Last revised = June 23, 1997

(All amounts in South African rand)

Tax	Nature of Tax	Exemptions and Deductions	Rates																											
1. Taxes on income, profits, and capital gains																														
1.1. <u>Individual income tax</u> Income Tax Act No. 58 of 1962 as amended	Central government tax charged on taxable income received by or accrued to a person from any source within or deemed to be within South Africa. Taxable income is assessed as gross income less exemptions and deductions. Receipts or accruals of a capital nature are generally excluded from gross income. Gains derived from asset transactions deemed to be made with the purpose of making a profit are included in gross income. Wage and salary earners are subject to withholding tax at source (PAYE) and may have to submit income tax returns at the end of the tax year. Persons whose income consists almost entirely of remuneration and of which the amount, after some deductions, does not exceed R 50,000 are subject to Standard Income Tax on Employees (SITE) under the PAYE system; SITE payers are not required to submit income tax returns. In the case of other individuals, tax is levied on taxable income in the tax year; provisional payments are effected in two half yearly installments. Certain provisional taxpayers may make a third "topping up" payment seven months after the end of their tax year. The tax year runs from the first day of March to the last day of February.	<u>Exemptions</u> include (i) the first R 2,000 of any taxable interest; (ii) dividends excluding dividends paid by fixed property companies or unit portfolios; (iii) benefits payable under the Unemployment Insurance Act, and (iv) leave gratuities on retirement/retranchment up to R 30,000. <u>Deductions</u> are allowed for (i) annual contributions to pension and retirement funds (the greater of R 1,750 or 7½ percent of pensionable income); (ii) retirement annuity fund contributions (the greater of R 1,750 or R 3,500 less allowable pension contributions or 15 percent of nonpensionable income), (iii) medical expenses (with deduction ceilings depending on age); and (iv) donations to certain educational institutions.	A single rate structure applies to all natural persons. The following rebates must be deducted from the normal tax determined on taxable income: Primary rebate R 3,215 Additional rebate R 2,500 (persons 65 years and older). Tax is calculated on the taxable income of any natural person under 65 years of age in accordance with the table below: <table><tr><th>Taxable annual income (In rand)</th><th>Marginal tax rates (In percent)</th><th>Average tax rates (In percent)</th></tr><tr><td>0- 16,921</td><td>0</td><td>0</td></tr><tr><td>16,922- 30,000</td><td>19</td><td>0.1 - 8.3</td></tr><tr><td>30,001- 35,000</td><td>30</td><td>8.3 - 11.4</td></tr><tr><td>35,001- 45,000</td><td>32</td><td>11.4 - 16.0</td></tr><tr><td>45,001- 60,000</td><td>41</td><td>16.0 - 22.2</td></tr><tr><td>60,001- 70,000</td><td>43</td><td>22.2 - 25.2</td></tr><tr><td>70,001-100,000</td><td>44</td><td>25.2 - 30.8</td></tr><tr><td>100,001+</td><td>45</td><td>30.8+</td></tr></table> A separate progressive rate structure applies to trusts.	Taxable annual income (In rand)	Marginal tax rates (In percent)	Average tax rates (In percent)	0- 16,921	0	0	16,922- 30,000	19	0.1 - 8.3	30,001- 35,000	30	8.3 - 11.4	35,001- 45,000	32	11.4 - 16.0	45,001- 60,000	41	16.0 - 22.2	60,001- 70,000	43	22.2 - 25.2	70,001-100,000	44	25.2 - 30.8	100,001+	45	30.8+
Taxable annual income (In rand)	Marginal tax rates (In percent)	Average tax rates (In percent)																												
0- 16,921	0	0																												
16,922- 30,000	19	0.1 - 8.3																												
30,001- 35,000	30	8.3 - 11.4																												
35,001- 45,000	32	11.4 - 16.0																												
45,001- 60,000	41	16.0 - 22.2																												
60,001- 70,000	43	22.2 - 25.2																												
70,001-100,000	44	25.2 - 30.8																												
100,001+	45	30.8+																												

Last revised = June 23, 1997

(All amounts in South African rand)

Tax	Nature of Tax	Exemptions and Deductions	Rates
<p>1.2. <u>Corporate taxes</u></p> <p>Income tax act No. 58 of 1962 as amended</p>	<p>Corporate income tax is a central government tax levied on the taxable income derived by all companies (whether local or foreign) from a source within South Africa. Taxable income is defined as gross income, other than capital receipts and exempt income, less allowable deductions and loss offsets.</p> <p>The tax year of assessment is the accounting year. Companies with taxable income in excess of R 20,000 are required to make three provisional tax payments in respect of each year of assessment, viz the first within six months after the commencement of the year of assessment, the second at the end of such year, and the third within a period of seven months from the close of such year for companies with a February year end. In all other cases the third payment will be due within six months after the close of the tax year.</p> <p>Comprehensive agreements for the avoidance of double taxation on the same income are in force with 29 countries.</p> <p>Limited agreements for the avoidance of double taxation on profits derived from sea or air transport are also in force with 8 countries.</p> <p>Gold mining companies are subject to special tax provisions.</p>	<p><u>Deductions</u> include normal operating costs, interest, and depreciation allowances but exclude dividends and capital expenditures.</p> <p>Depreciation allowances of non-mining companies vary according to type of asset, life expectancy, and intensity of use of assets. Generally, the straight-line method is used. Plant and machinery used in a process of manufacture, including aircraft and ships used by a taxpayer in the carrying on of his trade, may be written off on a straight line basis over 5 years. An initial allowance of 10 percent in respect of certain housing projects is also allowable. Farming machinery may be written off at 50 percent, 30 percent, and 20 percent over three years.</p> <p>A tax holiday scheme is in place for a period up to 6 years depending on the number of components certified by the Regional Industrial Development Board.</p> <p>An <u>assessed loss</u> can be carried forward indefinitely but cannot be carried backward.</p> <p>Capital expenditures by all types of mines are allowable as a deduction from income in the year of assessment in which they are incurred, limited, however, to the annual mining working profit.</p> <p>Unredeemed balance ranks for redemption against future mining working profit. Cost of land, mineral rights, mining rights, servitude, etc., are not deductible.</p>	<p>a. <u>Non-gold mining companies</u>: 35 percent of taxable income derived within South Africa.</p> <p>b. <u>Gold mining companies</u>: Formula-based tax rate according to:</p> <p>(a) Where the company is not exempt from the secondary tax on companies (STC):</p> $y = 43 - (215 \div x) \text{ or}$ <p>(b) where the company is exempt from the STC:</p> $y = 51 - (255 \div x)$ <p>In the formula y is the tax rate and x is the profit-to-revenue ratio.</p> <p>c. <u>Oil extraction companies</u>: 61 percent.</p> <p>d. <u>Long-term insurance companies</u>: If taxable income is determined under section 28, 45 percent. If taxable income is determined under section 29, 35 percent in respect to income derived from company policies and 30 percent in respect of income derived from policies held by individuals.</p> <p><u>Income of pension and retirement funds</u>: The net rental gross interest of pension, provident, and retirement annuity funds are taxed at a rate of 17 percent. Dividend payments received by the funds from unit trust schemes are also subject to the 17 percent tax.</p>

South Africa: Tax Summary as of April 1, 1997

Last revised = June 23, 1997

(All amounts in South African rand)

Tax	Nature of Tax	Exemptions and Deductions	Rates
<p>1.3. <u>Secondary tax on companies (STC)</u></p> <p>Income Tax Act No. 58 of 1962 as amended</p>	<p>A central government tax payable on the net amount of dividends, that is, the excess of dividends declared by the company over dividends accrued to the company during a dividend cycle.</p>	<p><u>Exemptions</u> include <u>inter alia</u></p> <ol style="list-style-type: none"> 1. Dividend payments of fixed property companies as defined in section 1 of the Unit Trust Control Act portfolios. These dividends are taxed in the hands of the recipient. 2. Dividends in specie in relation to approved unbundling transactions are also exempt from STC. 3. Dividends paid out by subsidiary companies to their holding company. 	<p>12½ percent on dividends declared on or after March 14, 1996.</p>
<p>2. <u>Social security contributions</u></p>			
<p>2.1. <u>Unemployment insurance contributions</u></p>	<p>A contribution collected by unemployment insurance funds.</p>	<p>Not payable for employees earning more than R 63,648 per year. Also excluded from unemployment insurance are domestic servants, homeworkers, and temporary workers who are employed for less than 8 hours or less than one full working day in any calendar year.</p>	<p>Employee and employer contributions of 1.0 percent of insured's earnings.</p>
<p>2.2. <u>Work injury insurance contributions</u></p>	<p>A compulsory insurance scheme.</p>	<p>Not payable by employees earning more than R 55,068 per year. Also excluded are domestic servants and casual workers.</p>	<p>Insurance premia vary with risk.</p>
<p>3. <u>Taxes on payroll and workforce</u></p>			
<p>3.1. <u>Payroll tax</u></p> <p>Regional Service Councils Act No. 109 of 1985</p> <p>KwaZulu and Natal Joint Services Act No. 84 of 1990</p>	<p>A tax levied by District and Joint Services Councils.</p>	<p>A tax levied by the Councils on remuneration paid by employer. Some Councils grant discounts of 15 percent, 20 percent, or 25 percent to farming enterprises.</p>	<p>Ranges from 0.25 percent to 0.38 percent depending on Council.</p>

South Africa: Tax Summary as of April 1, 1997

Last revised = June 23, 1997

(All amounts in South African rand)

Tax	Nature of Tax	Exemptions and Deductions	Rates
4. Taxes on property			
4.1. <u>Property tax</u>	A local tax payable on the capital value of land and improvements.	Method of valuation and rates differ across local governments. Rebates of up to 40 percent are provided for different classes of property.	Rates differ across local governments and depend on valuation methods.
4.2. <u>Estate duty</u> Estate Duty Act No. 45 of 1955	A central government tax payable on the estate of an individual. Property includes life insurance proceeds and lump-sum benefits received from pension or provident fund benefits.	Deductions include funeral and estate administration expenses, as well as outstanding debts of deceased. A single deduction of R 1,000,000 is applicable.	25 percent in respect of natural persons who died on or after March 14, 1996
4.3. <u>Donations tax</u> Income Tax Act No. 58 of 1962	A central government tax payable by the donor on the cumulative value of property donated by residents.	Donations by public companies and donations to charitable, educational, or ecclesiastical institutions are exempt. Annual exemption limits of R 5,000 and R 25,000 apply for legal and natural persons, respectively.	25 percent.
4.4. <u>Transfer duty</u> Transfer Duty Act No. 40 of 1949	A tax payable on the purchase consideration of fair value (whichever is the greater) of transfers of immovable property.	Exemption limits of R 24,000 for unimproved property and R 60,000 for property with dwelling.	For natural persons, 1 percent on the first R 60,000 plus 5 percent on the value in excess of R 60,000 but under R 250,000 plus 8 percent on amount in excess of R 250,000. For other persons, 10 percent of total value of property.
4.5. <u>Marketable securities tax</u> Marketable Securities Tax Act No. 32 of 1948	A tax payable on the purchase of marketable securities by a stockbroker on behalf of any person.		0.25 percent.

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Tax	Nature of Tax	Exemptions and Deductions	Rates
<p>5. Domestic taxes on goods and services</p>			
<p>5.1. <u>Value-added tax (VAT)</u></p> <p>Value-Added Tax Act No. 89 of 1991.</p>	<p>A central government tax levied on the supply of goods and services. VAT is collected at <u>single rate</u>, is <u>consumption-type</u> (allows full and immediate tax credit on capital goods), is based on <u>destination principle</u> (exports are zero-rated and imports are taxed), and uses an <u>invoice-based credit method</u> (VAT is calculated on sales and purchases separately, and tax is paid on difference between VAT on sales and VAT on purchases adequately supported by invoices.)</p>	<p>Main <u>zero-ratings</u> include (i) exports; (ii) several unprocessed food items including brown bread, maize meal, milk, eggs, fruit, and vegetables; (iii) petrol and diesel; (iv) several agricultural inputs including seeds, feed, and fertilizers; and (v) international transport services.</p> <p>Main <u>exemptions</u> include: (i) a limited number of financial services (mainly interest); (ii) residential rents; (iii) passenger transport; and (iv) educational services.</p>	<p>14 percent.</p>
<p>5.2. <u>Turnover tax</u></p> <p>Regional Service Councils Act No. 109 of 1985</p> <p>KwaZulu and Natal Joint Services Act No. 84 of 1990</p>	<p>A tax on turnover levied by District and Joint Service Councils.</p>	<p>Exemptions: (i) religious, charitable and educational institutions; (ii) nonprofit organizations engaged in nature conservation or animal protection; (iii) amateur sport clubs; and (iv) letting of accommodation to employees.</p>	<p>Ranges from 0.1 to 0.2 percent.</p>

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Tax	Nature of Tax	Exemptions and Deductions	Rates
<p>5.3. <u>Excise duties</u></p> <p>Customs and Excise Act No. 91 of 1964 as amended</p>	<p>Central government taxes payable by the manufacturer or importer of certain commodities. Most are specific, though some ad valorem rates exist.</p>	<p>A rebate is granted on dutiable goods that are used by government, provincial administrations, diplomatic representatives, etc., and on taxable goods used by producers in the manufacture of taxable goods for industrial or commercial purposes.</p>	<p>Beer (excluding sorghum beer): 72.5-118.3 cents per liter depending on alcohol content. Sorghum beer: 7.45 cents per liter. Sorghum powder: 33 cents per kilogram. Unfortified wine: 53.15 cents per liter. Fortified wine: 115.0 cents per liter. Sparkling wine: 147.5 cents per liter. Spirits: 2,376.87 cents per liter absolute alcohol. Other fermented drinks: 159.06 cents per liter. Cold drinks and mineral water: 14.83 cents per liter. Cigarettes: 79 cents per 10 cigarettes. Cigarette tobacco: 99 cents per 50 grams. Pipe tobacco and cigars: 672.5 cents per kilogram. Ad valorem rate lowered from 32.5-37.5 to a rate of 15 percent on essential oils; motorcycles with capacity less than 800 cm³ charged on excise of 7.5 percent; perfumes and toilet waters; beauty make-up preparations; preparations for use on the hair; shaving or bath preparations; photographic plates and film; articles of apparel and fur skin; microphones and stands; turntables, record-players and cassette-players; magnetic tape recorders; video recording or reproducing apparatus; prepared unrecorded media for sound; records, tapes, and other recorded media; reception apparatus for radio-telephony; motorcycles with capacity more than 800 cm³ charged on excise of 7.5 percent; motorcycles; lenses, prisms, mirrors, and other optical elements; spectacles, goggles, and the like; binoculars, monoculars, etc.; photographic cameras; cinematographic cameras and projectors; image projectors; wrist watches, pocket watches, and other watches</p>
<p>5.4. <u>Fuel levy</u></p> <p>Customs and Excise Act No. 91 of 1964 as amended</p>	<p>A central government levy on the sale of petrol, diesel, and kerosene mixtures.</p>		<p>Petrol: 69.4 cents per liter (unleaded); 75.6 cents per liter (leaded). Diesel: 65.1 cents per liter.</p>

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Tax	Nature of Tax	Exemptions and Deductions	Rates
<p>5.5. <u>Levy on financial services</u></p> <p>Income tax act No. 58 of 1962 as amended</p>	<p>A central government tax levied on interest which accrues to certain institutions.</p>	<p>Exemptions: (i) government pension funds; (ii) private pension funds where interest per quarter does not exceed R 125,000; (iii) stabilization account of SADF group life assurance scheme; (iv) interest received by pension fund from any other pension fund, insurer, or unit trust; and (v) the banking sector.</p>	<p>0.75 percent; to be abolished from January 1, 1998.</p>
<p>5.6. <u>Motor vehicle taxes</u></p> <p>Customs and Excise Act No. 91 of 1964 as amended</p>	<p>A tax levied on the value of imported components used in the manufacture of duty payable motor cars, station wagons and similar dual purpose motor vehicles, excluding heavy duty motor vehicles and motorcycles.</p>	<p>(1) A Customs driven program in terms of which the Customs value of components imported for the manufacture of motor vehicles are liable to customs duty. Provision is made that the value of the imported components can be reduced by a duty free allowance as well as the value of imported rebate credit certificates. Customs duty is only payable on the remaining customs value.</p> <p>(2) Ad valorem Customs and Excise duty which is applicable to imported as well as locally produced motor vehicles. Items (1) and (2) are applicable to motor cars, motor vehicles for the transport of ten or more persons of a vehicle mass not exceeding 1,600 kg., motor vehicles for the transport of goods of a vehicle mass not exceed 2,000 kg., or a GVM not exceeding 3,500 kg. or a mass not exceeding 1,600 kg. or a GVM not exceeding 3,500 kg. per chassis fitted with a cab and chassis fitted with engine of Heading No. 87.06 of a mass not exceeding 3,500 kg.</p> <p>(3) <u>Heavy duty vehicles</u>: certain components are liable to customs duty and the balance allowed under full rebate of customs duty.</p>	<p>49 percent with an annual reduction of 3 percent until it reaches 30 percent.</p> <p>(0.000035 x value for ad valorem duty purposes) less 0.5 percent.</p> <p>Compression ignition engine: 27.5 percent Driving axles: 27.5 percent Gear boxes: 27.5 percent Cabs/bodies: 17.5 percent Pneumatic tires: 27.5 percent</p>

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Tax	Nature of Tax	Exemptions and Deductions	Rates
<p>6. Taxes on international trade transactions</p>			
<p>6.1. <u>Customs duties</u> Customs and Excise Act No. 91 of 1964 as amended</p>	<p>A one-column tariff schedule based on the Brussels nomenclature with general, most favored nation, and preferential rates of duty. Preferential treatment is given to goods from the United Kingdom and in some cases, goods from Canada and Ireland. There is a Customs Union with Botswana, Lesotho, and Swaziland. Most duties are assessed ad valorem at c.i.f. value but there are a number of specific duties.</p>	<p>Rebates are allowed for certain goods used in manufacture by approved industries or by particular institutions and bodies.</p>	<p>There are 35 ad valorem rates, and 8,592 tariff lines with either formula, specific, or other types of duties. Import duties vary widely.</p>
<p>7. Other taxes</p>			
<p>7.1. <u>Stamp duties</u> Stamp Duties Act No. 77 of 1968</p>	<p>Ad valorem or specific taxes payable on a wide range of legal documents such bills of exchange, bonds, fixed deposit receipts, leases, marketable securities, etc.</p>	<p>Most securities issued by certain public corporations and public authorities are exempt from stamp duty on issue and transfers. Where marketable securities tax is chargeable, brokers' notes do not attract stamp duty.</p>	<p>Rates of stamp duty vary for different instruments and also for a particular instrument. Examples are: 5 cents per R 100 for bills of exchange; 10 cents per R 200 per annum on fixed deposit receipts; and 0.25 cents per R 100 on registration of share certificates.</p>

Exchange Control Liberalization in 1996 and 1997

Measures introduced in the GEAR

Relaxation of restrictions on nonresidents' access to domestic credit and on operations:

- the borrowing limit was doubled from 50 percent of shareholders' equity to 100 percent;
- the capital structure requirements on foreign-controlled South African resident organizations were relaxed by the removal of the requirement of the 1 to 3 ratio of shareholder's capital to loans; and
- these companies were authorized to extend loans to foreign shareholders in lieu of dividend transfers.

Further liberalization of restrictions on resident investment abroad:

- the limit on the total assets that insurance companies, pension funds, and unit trusts are authorized to swap with foreign investors was raised from 5 percent of total assets to 10 percent;
- the above institutional investors were authorized to transfer foreign currency abroad in 1996 by up to 3 percent of the net inflow of funds during 1995, subject to the overall limit of 10 percent of total assets;
- South African companies were authorized to invest abroad up to R 20 million per project for approved new investments from locally sourced capital—previously all financing had to be raised abroad; and
- companies were authorized to reinvest dividends earned abroad for the development of the company, subject to notification—previously all dividend earnings had to be repatriated within seven days, unless prior approval from exchange control had been obtained.

Relaxation of restriction relating to trade:

- exporters were authorized to retain export proceeds to cover the cost of imports, within 30 days of accrual.

Relaxation of constraints and substantial increases in the limits on various current account transactions, including:

- the annual travel allowances for tourism and business were raised, for adults from R 25,000 to R 60,000 and for children from R 12,500 to R 20,000;
- the export—without prior authorization—of yachts of up to R 750,000 a year was permitted;

- the limits on subscriptions and membership fees were increased; and
- the limits on technical service fees were increased from R 75,000 to R 150,000 per year.

Measures announced in conjunction with the 1997/98 budget¹:

Relaxation of restrictions on nonresidents' access to domestic credit and operations:

- the threshold on foreign share holding at which companies become subject to limits on local borrowing was increased from 25 percent to 50 percent; and
- nonresidents in the Common Monetary Area were permitted to maintain foreign currency denominated deposits with South African banks.

Further access for residents to invest and retain funds abroad:

- institutional investors were authorized to transfer foreign assets abroad in 1997 up to 3 percent of the net inflow of funds during 1996, and an additional 2 percent in securities listed on the stock exchanges in the SADC countries, ² subject to the overall limit of 10 percent of total assets;
- the definition of *institutions* eligible to engage in assets swaps was broadened to include regulated fund managers, and the flexibility of the unit trust management industry in applying the 10 percent limit of assets was increased;
- the limit on currency transfers for investment abroad was raised to R 30 million per project for approved new investments, and to R 50 million in the SADC countries;³
- Southern African subsidiary companies operating overseas were authorized to raise loans abroad against assets on the balance sheet of the parent company;
- companies were authorized to retain a percentage of their assets abroad for portfolio investments (limits not yet specified);
- companies were authorized to retain foreign currency earnings for up to thirty days of accrual instead of seven days;
- the prohibitions on individuals' capital investment abroad, in fixed property in SADC countries and in holding foreign currency deposits with authorized dealers were relaxed—individuals were authorized to maintain foreign currency denominated deposit accounts, subject to a prescribed ceilings (yet undefined), with South African banks and to retain foreign income earnings in foreign currency accounts; and
- individuals were granted full discretion in their use of foreign-earned income, with the exception of proceeds from merchandise exports.

¹Details on how some of these measures are to be implemented have not yet been finalized.

²Other than Namibia, Swaziland and Lesotho, where no restrictions apply.

³Other than Namibia, Swaziland and Lesotho where funds already flow freely.

Further development of the futures exchange in rand through the establishment of the South African Futures Exchange. Participation in the Exchange will initially be restricted to non-residents and to authorized dealers in foreign exchange. Residents, including corporations, will be permitted to deal in such contracts only via authorized dealers in foreign exchange, with further relaxation of these restrictions planned in the future.

Relaxation of restrictions and substantial increases in the limits in various current account transactions, including

- **the annual travel allowances were raised, for adults from R 60,000 to R 80,000 and for children from R 20,000 to R 25,000;**
- **the distinction between neighboring countries and other countries was eliminated, thereby raising travel allowances to neighboring countries;**
- **the restrictions on transfers of buying commissions, payment for specific services, and importation of newspapers, books and periodicals were eliminated; and.**
- **the need for prior approval for the payment for services rendered by non-residents, including directors' fees, subscriptions to clubs, memberships, and alimony payments were eliminated.**

Table 1. South Africa: Expenditure on GDP, 1992-96

	<u>1996</u>		1992	1993	1994	1995	1996	<u>1995</u>				<u>1996</u>			
	Millions of rand	Percent of GDP						I	II	III	IV	I	II	III	IV
	<u>(At current prices)</u>		<u>(Annual percentage change; at 1990 prices)</u>					<u>(Seasonally adjusted at annual rate)</u>							
Private consumption	330,476	60.9	-1.4	0.3	3.1	4.7	3.8	4.3	5.8	5.0	3.8	3.5	3.8	2.8	2.5
Public consumption	113,237	20.9	1.5	2.9	4.2	0.3	5.0	-2.0	0.4	2.0	2.1	6.4	9.2	5.7	4.7
Gross fixed investment	92,557	17.0	-5.3	-2.8	8.7	10.3	6.8	6.1	8.3	8.9	7.6	7.8	5.9	4.6	2.3
Final demand	536,270	98.8	-1.6	0.3	4.3	4.8	4.6	3.3	5.1	5.1	4.1	4.9	5.3	3.8	2.9
Inventory investment ^{1/}	5,411	1.0	0.2	1.2	1.5	0.7	-1.2	3.6	0.1	-7.6	-0.1	-2.8	7.4	-4.9	-3.6
Domestic demand	<u>541,681</u>	<u>99.8</u>	<u>-1.4</u>	<u>1.5</u>	<u>5.8</u>	<u>5.5</u>	<u>3.3</u>	<u>6.9</u>	<u>5.0</u>	<u>-2.8</u>	<u>4.0</u>	<u>1.9</u>	<u>13.0</u>	<u>-1.2</u>	<u>-0.8</u>
Exports of goods and nonfactor services	143,682	26.5	2.5	4.8	1.0	9.3	7.8	13.7	-10.0	48.0	-5.2	6.6	-8.7	36.7	8.1
Imports of goods and nonfactor services	139,647	25.7	5.3	7.0	16.1	16.6	7.5	28.3	-4.8	11.7	9.1	1.0	18.5	14.5	-8.9
Foreign balance ^{1/}	<u>4,035</u>	<u>0.7</u>	<u>-0.4</u>	<u>-0.2</u>	<u>-3.4</u>	<u>-1.7</u>	<u>0.1</u>	<u>-3.4</u>	<u>-1.5</u>	<u>8.5</u>	<u>-4.1</u>	<u>1.6</u>	<u>-7.6</u>	<u>5.3</u>	<u>5.4</u>
Statistical discrepancy ^{1/}	-2,702	-0.5	-0.4	0.0	0.6	-0.3	-0.3	-1.1	-1.0	-2.5	2.8	-0.3	-0.9	-0.8	-1.3
GDP at market prices	<u>543,014</u>	<u>100.0</u>	<u>-2.2</u>	<u>1.3</u>	<u>2.7</u>	<u>3.4</u>	<u>3.1</u>	<u>2.1</u>	<u>2.4</u>	<u>2.8</u>	<u>2.6</u>	<u>3.3</u>	<u>3.7</u>	<u>3.2</u>	<u>3.3</u>

Source: South African Reserve Bank, Quarterly Bulletin.^{1/} Contribution to GDP growth.

Table 2. South Africa: Gross Fixed Investment and Capital Stock, 1992-96

	<u>1996</u> Share of total	1992	1993	1994	1995	1996
(Annual percentage change; at 1990 prices)						
Total gross investment	<u>100.0</u>	<u>-5.3</u>	<u>-2.8</u>	<u>8.7</u>	<u>10.3</u>	<u>6.8</u>
By type of organization						
Private enterprises <u>1/</u>	74.4	-2.4	-1.6	13.3	13.0	6.7
Public corporations	13.7	-6.4	-13.4	-2.1	15.7	9.8
Public authorities	11.9	-15.4	2.6	-1.8	-7.7	4.4
By sector						
Mining	8.8	-18.7	-27.4	19.8	9.7	0.5
Manufacturing	28.7	-6.0	5.1	9.9	20.9	9.0
Financial services <u>1/ 2/</u>	22.3	-2.8	-0.1	10.7	7.8	2.9
Community, social, and personal services	10.6	6.2	1.8	-0.7	-9.2	3.9
Other sectors	29.5	-5.3	-3.8	7.5	12.2	10.9
By type of asset						
Residential building	9.7	4.9	-2.3	2.0	0.1	2.4
Nonresidential building	9.3	-17.7	-6.7	-1.1	-5.9	3.7
Construction works	13.2	-21.0	-10.6	-3.0	0.6	3.3
Transport equipment	13.2	-8.4	-7.0	6.1	13.0	4.1
Machinery and other equipment	51.2	7.7	3.2	18.4	20.4	10.3
Transfer costs	3.3	0.7	1.3	15.9	-2.4	2.7
Real fixed capital stock <u>3/</u>	<u>100.0</u>	<u>0.6</u>	<u>0.5</u>	<u>0.9</u>	<u>1.3</u>	<u>1.5</u>
Private enterprises <u>1/</u>	49.5	1.2	1.0	1.8	2.6	2.8
Public corporations	20.1	7.8	-2.3	-2.3	-1.7	-1.2
Public authorities <u>4/</u>	30.5	-5.0	1.7	1.6	1.4	1.5

Source: South African Reserve Bank, Quarterly Bulletin.

1/ Including transfer costs.

2/ Finance, insurance, real estate, and business services.

3/ End of period.

4/ General Government plus four departmental enterprises (Community Development Fund, Government Motor Transport Trading, Government Printing Works, National Housing Fund).

Table 3. South Africa: Financing of Domestic Investment, 1991-96

(In percent of GDP at market prices)

	1991	1992	1993	1994	1995	1996
Gross private saving <u>1/</u>	19.8	21.5	22.5	21.5	20.4	19.6
Less: Depreciation <u>2/</u>	14.5	14.1	13.5	13.1	13.0	12.7
Net private saving	5.4	7.4	9.0	8.4	7.5	6.9
Net personal saving	1.2	2.7	3.3	2.7	1.4	1.0
Net corporate saving	4.2	4.7	5.7	5.7	6.1	5.9
Gross general government saving <u>1/</u>	-0.9	-4.5	-5.3	-4.4	-3.6	-3.1
Less: Depreciation <u>2/</u>	0.6	0.6	0.6	0.6	0.6	0.6
Net general government saving	-1.5	-5.1	-5.9	-5.0	-4.2	-3.7
Net domestic saving	3.8	2.3	3.1	3.4	3.2	3.2
Net foreign saving (current account surplus -)	-2.0	-1.5	-1.6	0.3	2.1	1.6
Net domestic investment	1.8	0.9	1.5	3.7	5.3	4.8

Source: South African Reserve Bank, Quarterly Bulletin.

1/ Before inventory valuation adjustment.

2/ Provision for depreciation at replacement value.

Table 4. South Africa: Growth of Disposable Income of Households, 1992-96

	1996 Structure of disposable income	1992	1993	1994	1995	1996
	(In billions of rand)	(Percentage change from previous year)				
Net remuneration of employees <u>1/</u>	283.4	13.1	11.0	10.2	12.0	10.3
Net income from property	85.6	28.6	12.2	20.8	6.6	16.7
Transfers received	24.7	28.9	19.8	7.8	22.0	9.3
General government	23.7	30.5	19.1	8.6	22.4	9.1
Business enterprises	0.3	11.2	9.6	15.4	11.0	12.3
Abroad	0.7	-2.7	49.5	-15.2	15.2	14.6
Current income	393.7	16.7	11.7	12.2	11.4	11.6
Less: Direct taxes	56.7	17.1	10.5	20.1	11.3	13.2
Personal disposable income	337.0	16.7	11.9	11.0	11.4	11.3
Less: Private consumer expenditure	330.5	14.1	10.7	12.1	13.7	11.9
Less: Transfers to general government and abroad	...	-4.4	21.2	...	...	...
Personal saving	5.3	152.1	40.4	-10.4	-42.7	-19.3
Personal saving/Personal disposable income <u>2/</u>	1.6	4.2	5.2	4.2	2.2	1.6

Source: South African Reserve Bank, Quarterly Bulletin.

1/ After adjustment for net remuneration paid to the rest of the world.

2/ After provision for depreciation and inventory valuation adjustment.

Table 5. South Africa: Real Gross Domestic Product at Factor Cost, 1992-96

	<u>1996</u>		1992	1993	1994	1995	1996	<u>1995</u>			<u>1996</u>			
	Billions of rand	Percent of total						II	III	IV	I	II	III	IV
	<u>(At current prices)</u>		<u>(Annual percentage change; at 1990 prices)</u>					<u>(Seasonally adjusted at annual rates)</u>						
Primary sector	<u>61.7</u>	<u>12.8</u>	<u>-8.9</u>	<u>8.7</u>	<u>2.3</u>	<u>-7.5</u>	<u>7.8</u>	<u>-20.9</u>	<u>-6.0</u>	<u>0.7</u>	<u>23.0</u>	<u>13.2</u>	<u>15.0</u>	<u>5.7</u>
Agriculture, forestry, and fishing	22.5	4.7	-27.3	24.0	12.0	-14.9	25.8	-43.7	-23.1	-2.3	86.6	53.0	59.8	12.6
Mining and quarrying	39.1	8.1	1.7	2.3	-2.5	-3.1	-1.4	-4.9	3.7	2.2	-0.4	-5.0	-7.4	1.0
Industry sector	<u>148.2</u>	<u>30.7</u>	<u>-3.1</u>	<u>0.0</u>	<u>2.6</u>	<u>6.4</u>	<u>1.2</u>	<u>7.8</u>	<u>1.2</u>	<u>-1.9</u>	<u>0.5</u>	<u>3.1</u>	<u>0.4</u>	<u>2.5</u>
Manufacturing	114.9	23.8	-3.3	0.2	2.5	7.6	0.4	9.3	0.8	-3.4	-0.8	2.9	-0.9	2.2
Construction	14.3	3.0	-6.2	-6.8	1.2	1.7	1.8	1.8	1.6	2.0	2.2	1.7	1.0	1.2
Electricity, gas, and water	19.0	3.9	0.5	4.0	3.7	3.3	4.9	4.0	2.7	4.0	6.3	4.9	6.6	4.9
Service sector	<u>273.1</u>	<u>56.5</u>	<u>-0.1</u>	<u>0.6</u>	<u>2.5</u>	<u>3.7</u>	<u>2.8</u>	<u>5.0</u>	<u>4.4</u>	<u>4.0</u>	<u>0.9</u>	<u>3.0</u>	<u>2.2</u>	<u>2.8</u>
Wholesale and retail trade and catering	77.8	16.1	-2.3	0.5	3.9	6.5	3.7	9.0	8.3	9.2	-2.6	5.5	-0.1	2.8
Transport, storage, and communication	37.2	7.7	1.9	2.4	3.7	5.2	3.2	8.6	6.3	3.7	1.2	1.8	3.2	2.4
Finance, insurance, real estate, and business services	65.4	13.5	-0.2	0.1	2.6	3.6	3.2	4.2	4.0	2.5	3.0	2.5	3.9	3.5
General government and other services	92.8	19.2	1.1	0.4	0.9	1.0	1.7	0.7	0.7	0.7	2.5	1.6	2.7	2.5
GDP at factor cost	<u>483.0</u>	<u>100.0</u>	<u>-2.4</u>	<u>1.6</u>	<u>2.5</u>	<u>2.9</u>	<u>3.0</u>	<u>1.8</u>	<u>1.9</u>	<u>1.6</u>	<u>3.5</u>	<u>4.4</u>	<u>3.3</u>	<u>3.1</u>
<u>Memorandum item:</u>														
GDP less general government	409.5	84.8	-3.0	1.8	2.8	3.3	3.2	2.0	2.2	1.8	3.7	4.9	3.4	3.2

Source: South African Reserve Bank, Quarterly Bulletin.

Table 6. South Africa: Indicators of Mining and Quarrying Activity, 1989-96

	Weights <u>1/</u>	1989	1990	1991	1992	1993	1994	1995	1996
<u>(Annual percentage change)</u>									
Production volume	100.0	-2.4	-1.9	-0.9	0.4	3.0	-1.6	-1.6	...
Gold	45.8	-2.4	-1.2	-0.7	2.0	1.0	-6.5	-10.2	...
Nongold	54.2	-2.2	-2.7	-1.1	-0.9	4.7	2.6	5.0	...
Gross fixed investment									
at 1990 prices		3.2	-6.2	-6.8	-18.7	-27.4	19.8	9.7	0.5
Fixed capital stock									
at 1990 prices		4.3	3.1	2.1	0.1	-2.0	-1.0	-0.4	-0.5
<u>(In percent)</u>									
<u>Memorandum items:</u>									
Share in total capital									
stock at 1990 prices		8.4	8.5	8.6	8.6	8.4	8.2	8.1	7.9
Share in total nonagri-									
cultural employment		14.3	14.0	13.2	12.4	11.8	11.6	11.3	...
Share in real GDP at factor cost		9.7	9.7	9.6	10.0	10.1	9.6	9.0	8.6

Sources: South African Reserve Bank, Quarterly Bulletin; Central Statistical Service, Bulletin of Statistics.

1/ In 1990.

Table 7. South Africa: Indicators of Manufacturing Activity, 1991-96

	1991	1992	1993	1994	1995	1996	1995		1996			
							III	IV	I	II	III	IV
(Annual percentage change, at 1990 prices)												
Production volume	-3.6	-3.0	-0.2	2.7	7.5	0.4	1.9	1.6	-2.7	-2.3	-1.8	0.1
Durable goods	-5.1	-6.2	-1.7	3.5	10.5	0.9	2.9	3.0	-4.6	-2.9	-1.5	4.1
Nondurable goods	-2.5	-0.8	0.9	2.2	5.4	0.0	1.2	0.6	-1.3	-2.0	-2.0	-2.5
Sales	-3.5	-4.0	-0.8	2.4	7.1	1.5	4.0	3.9	-2.3	0.8	-2.0	1.9
New orders	-5.4	-4.2	-0.6	7.5	7.2	2.1	-2.1	-3.9	-2.1	1.0	0.8	3.7
Unfilled orders	-16.7	1.2	-0.9	12.6	4.4	-6.2	-7.4	-16.0	-10.1	-11.6	-0.5	1.9
Gross fixed investment	-11.7	-6.0	5.1	9.9	20.9	9.0	10.6	10.8	8.7	6.0	7.6	13.6
Unit labor costs	14.7	15.8	9.0	7.9	3.8	...	3.5	6.9	8.2	2.6	6.7	...
Production prices	11.3	8.2	6.7	8.2	9.6	6.9	7.8	8.8	5.9	6.0	7.8	8.6
Labor productivity	-1.4	-0.3	1.6	2.4	6.6	...	5.6	3.2	2.6	4.3	4.0	...
(In percent)												
Capacity utilization	81.0	78.5	77.9	80.0	83.2	...	83.2	82.3	81.1	81.5	81.4	...
Durable goods	78.2	75.1	74.8	78.5	82.8	...	82.8	81.4	80.9	81.0	80.7	...
Nondurable goods	93.0	81.0	80.3	81.5	83.5	...	83.4	83.3	81.1	81.8	82.0	...

Source: South African Reserve Bank, *Quarterly Bulletin*

Table 8. South Africa: Nonagricultural Employment, 1989-96
(1990 = 100)

	Public Authorities 1/ Business enterprises 2/			Private sector			Grand total
	General govt.	Total	Total	Mining	Manufacturing	Total 3/	
1989	98.6	102.2	99.0	102.4	100.1	100.8	100.3
1990	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1991	103.2	98.5	102.4	92.7	97.8	96.5	98.3
1992	105.3	94.5	103.6	85.3	95.1	93.1	96.3
1993	106.1	82.4	102.3	79.6	93.4	90.8	94.3
1994	107.7	76.8	102.9	78.0	93.6	89.7	93.7
1995	108.2	76.4	103.4	76.2	94.4	90.4	94.4
(End of quarter; seasonally adjusted)							
1991							
I	102.4	99.2	101.8	93.9	98.2	97.4	98.8
II	103.2	98.5	102.4	92.5	97.8	96.5	98.3
III	103.2	98.8	102.5	92.2	97.5	96.1	98.1
IV	103.9	97.6	103.0	91.0	96.8	95.8	98.0
1992							
I	104.0	96.6	102.8	87.7	96.0	94.4	97.0
II	104.7	95.5	103.3	85.2	95.3	93.7	96.6
III	105.8	94.0	104.0	83.8	94.3	92.4	96.0
IV	106.7	91.9	104.3	82.4	94.7	92.0	95.8
1993							
I	106.4	86.6	103.3	80.7	94.2	91.8	95.3
II	105.1	83.8	101.8	78.7	93.5	91.1	94.4
III	105.8	80.3	101.8	78.8	92.9	90.6	94.1
IV	106.9	79.0	102.5	77.9	91.6	89.8	93.7
1994							
I	107.0	77.6	102.4	78.2	93.1	89.5	93.5
II	107.1	76.5	102.3	78.3	93.4	89.5	93.4
III	108.0	75.8	103.0	77.4	94.1	89.8	93.8
IV	108.6	77.2	103.7	77.6	94.2	90.0	94.2
1995							
I	107.6	77.1	102.9	77.2	94.3	90.4	94.3
II	107.6	77.1	103.1	76.6	94.8	90.6	94.5
III	107.6	76.3	103.0	75.7	94.6	90.3	94.2
IV	109.8	75.0	104.6	74.8	93.6	90.1	94.6
1996							
I	109.4	75.0	104.6	72.9	91.6	88.8	93.6
II	110.3	75.7	105.6	71.9	90.8	88.0	93.4
III	110.6	76.0	105.9	72.3	90.1	87.4	93.0

Source: South African Reserve Bank, Quarterly Bulletin.

1/ Central Government, local authorities, provincial administrations, statutory bodies, and national and independent states (TVBC).

2/ Transnet and the Department of Posts and Telecommunications.

3/ Includes Electricity Supply Commission, Boards of Control, and universities.

Table 9. South Africa: Remuneration, Labor Productivity, and Unit Labor Costs in the Nonagricultural Sector, 1992-96

	1992	1993	1994	1995	1995 1/				1996 1/		
					I	II	III	IV	I	II	III
<u>(Annual percentage change)</u>											
Remuneration per worker											
At current prices											
Public authorities	14.8	9.1	15.0	6.5	14.1	-1.5	5.8	8.5	10.1	11.2	8.9
Private sector	14.9	11.0	10.0	11.1	10.3	12.7	10.8	11.1	12.5	10.5	11.0
Total	15.1	10.3	11.9	9.4	11.7	7.0	8.9	10.1	11.7	10.9	10.4
At constant 1990 prices 2/											
Public authorities	1.4	-1.5	6.0	-1.9	5.2	-8.9	-2.3	-0.6	1.1	1.5	-0.7
Private sector	1.5	0.1	1.5	2.4	1.6	4.2	2.4	1.7	3.2	0.8	1.2
Total	1.6	-0.4	3.1	0.9	2.9	-1.0	0.7	0.8	2.5	1.3	0.8
Labor productivity	1.1	2.7	2.7	3.3	2.8	3.3	3.9	3.2	3.2	2.9	2.3
Unit labor costs											
Nominal	13.8	7.4	9.0	6.0	8.7	3.7	4.7	6.7	8.2	7.7	8.0
Real 2/	0.5	-3.1	0.6	-2.4	0.2	-4.1	-3.2	-2.2	-0.7	-1.7	-1.6

Source: South African Reserve Bank, Quarterly Bulletin.

1/ Seasonally adjusted.

2/ At 1990 prices; deflated by nonagricultural deflator.

Table 10. South Africa: Price Developments, 1992-96

(Percentage change over the previous period; period average)

	Weight ^{1/}	1992	1993	1994	1995	1996	1995				1996			
							I	II	III	IV	I	II	III	IV
<u>(Seasonally adjusted at annual rate)</u>														
Consumer prices	100.0	13.9	9.7	9.0	8.6	7.4	9.5	9.9	2.2	5.3	8.9	7.8	9.0	11.5
Goods	57.9	16.3	10.4	9.4	7.4	6.2	8.0	8.5	-2.1	4.3	8.7	5.7	9.4	11.2
Of which:														
Food	19.3	24.5	7.1	13.6	8.7	6.2	7.4	7.8	-11.5	3.1	16.0	2.7	10.8	17.0
Services	42.1	11.1	8.7	8.9	10.7	9.5	10.0	12.9	11.6	4.3	10.1	10.4	9.7	11.2
Of which:														
Housing	21.4	1.0	-0.4	4.6	13.4	11.7	15.6	19.6	14.8	7.5	11.2	14.7	10.5	9.2
Producer prices	100.0	8.2	6.7	8.2	9.6	6.9	14.3	10.1	2.8	7.9	5.1	6.9	9.3	12.7
Goods produced in														
South Africa	80.5	9.1	6.9	8.9	9.9	7.5	13.5	10.0	3.7	9.8	4.8	6.8	11.4	11.4
Imported goods	19.5	4.1	4.9	5.5	7.6	5.3	15.5	10.5	-0.5	2.8	6.0	7.3	2.9	18.1
GDP deflator at														
market prices		12.4	11.1	9.5	8.9	8.4	13.9	6.9	9.3	4.2	10.9	9.9	11.2	1.4
<u>Memorandum items:</u>														
Twelve-month rate to end of period														
Consumer prices		9.5	9.7	10.0	7.0	9.4	10.3	10.0	6.4	7.0	6.3	6.7	8.4	9.4
Producer prices		6.9	6.3	10.3	8.5	8.8	10.9	10.5	7.6	8.5	5.9	6.1	7.6	8.8

Source: South African Reserve Bank, Quarterly Bulletin.^{1/} The consumer price series uses 1990 weights; the producer price series uses 1985 weights.

Table 11. South Africa: National Government Finances, 1992/93 - 1997/98 1/

	1992/93	1993/94	1994/95	1995/96	1996/97 Budget	1996/97 Prel.	1997/98 Budget
(In millions of rand)							
Total Revenue	83,864	98,108	112,189	127,285	144,687	147,727	163,059
Ordinary revenue 2/	82,759	96,673	112,173	125,926	142,791	146,116	161,801
Extraordinary Revenue 3/	1,105	1,435	16	1,359	1,896	1,611	1,258
of which: Sales of oil stocks	1,036	1,406	--	1,359	1,880	1,603	1,250
Expenditure 2/	111,359	122,052	136,956	151,699	173,490	177,381	186,580
Current expenditure	105,932	114,992	129,068	146,564	159,554	162,758	173,420
Interest payments 4/	17,050	20,828	24,233	29,337	36,071	36,443	39,643
Other current expenditure	88,883	94,165	104,834	117,227	123,483	126,315	133,777
of which: Transfers to provinces	...	...	64,097	72,572	79,630	80,783	84,129
Capital expenditure 5/	5,427	7,060	7,889	5,135	13,937	14,624	13,160
Overall Balance	-27,495	-23,944	-24,768	-24,414	-28,803	-29,654	-23,521
Excluding sales of oil stocks	-28,531	-25,350	-24,768	-25,774	-30,683	-31,257	-24,771
Excluding sales of oil stocks and including accrued interest	-29,800	-26,635	-26,728	-28,864	...	-34,749	...
(In percent of GDP)							
Total Revenue	24.1	24.8	25.1	25.6	25.8	26.4	26.2
Ordinary revenue 2/	23.8	24.4	25.1	25.3	25.5	26.1	26.0
Extraordinary Revenue 3/	0.3	0.4	--	0.3	0.3	0.3	0.2
of which: Sales of oil stocks	0.3	0.4	--	0.3	0.3	0.3	0.2
Expenditure 2/	32.0	30.9	30.7	30.5	30.9	31.7	30.0
Current expenditure	30.5	29.1	28.9	29.4	28.4	29.1	27.9
Interest payments 4/	4.9	5.3	5.4	5.9	6.4	6.5	6.4
Other current expenditure	25.6	23.8	23.5	23.5	22.0	22.6	21.5
Of which: Transfers to provinces	...	...	14.4	14.6	14.2	14.4	13.5
Capital expenditure 5/	1.6	1.8	1.8	1.0	2.5	2.6	2.1
Overall Balance	-7.9	-6.1	-5.5	-4.9	-5.1	-5.3	-3.8
Excluding sales of oil stocks	-8.2	-6.4	-5.5	-5.2	-5.5	-5.6	-4.0
Excluding sales of oil stocks and including accrued interest	-8.6	-6.7	-6.0	-5.8	...	-6.2	...
Memorandum items (in percent of GDP, unless otherwise indicated):							
Primary balance before borrowing	-3.0	-0.8	-0.1	1.0	1.3	1.2	2.6
Government debt 6/	44.5	48.6	54.8	56.2	55.6	55.0	54.8
Accrued interest	5.3	5.6	5.9	6.5	...	7.1	...
Adjusted debt/GDP ratio 7/	40.8	44.4	49.1	49.5	...	48.2	...
Extraordinary transf. (mill. rand)	3,777	14,840	--	3,073	--	--	--

Sources: Department of Finance; and Fund staff estimates.

1/ National budget, including transfers to provinces; fiscal year begins April 1.

2/ Repayment of budget lending classified as negative expenditure in line with GFS principles. Excludes extraordinary transfers to the Pension Fund and the Gold and Foreign Exchange Contingency Account.

3/ Excludes privatization receipts.

4/ Cash data; includes exchange losses on the amortization of foreign loans.

5/ Includes capital transfers to other units of government, except transfers to provinces which are included as current expenditure.

6/ At end of fiscal year. Includes extraordinary transfers to the Pension Fund and the Gold and Foreign Exchange Account.

7/ Subtracting accrued discount from face value of the debt stock.

Table 12. South Africa: National Government Revenue, 1992/93 - 1997/98 1/

(In millions of rand)

	1992/93	1993/94	1994/95	1995/96	1996/97 Budget	1996/97 Prel.	1997/98 Budget
Revenue	83,864	98,108	112,189	127,285	144,687	147,727	163,059
Inland Revenue	66,253	77,884	92,368	103,886	120,031	120,980	135,735
Income tax	46,956	50,172	59,868	68,109	77,579	79,427	89,623
Gold mines	422	623	1,173	894	865	605	800
Other mines	576	509	457	715	1,354	1,354	1,354
Nonmining companies	12,126	11,236	13,265	15,321	17,385	19,375	22,400
Individuals	33,833	37,805	44,973	51,179	57,975	58,093	65,069
Sales tax/VAT	17,506	25,449	29,288	32,768	36,930	36,150	40,280
Other	1,791	2,262	3,212	3,009	5,522	5,403	5,832
Customs and Excise	14,308	16,241	17,892	19,219	20,824	21,684	23,245
Customs duty	2,961	3,413	4,247	5,326	6,230	6,820	7,115
Surcharge	1,521	1,756	1,171	457	--	--	--
Excise duty	4,436	4,967	5,804	6,475	6,918	6,796	7,879
Fuel levy	7,083	7,860	8,352	8,928	10,360	10,500	11,595
Other	1,291	1,334	1,567	1,923	1,679	1,931	1,893
SACU payments	-2,984	-3,089	-3,249	-3,890	-4,363	-4,363	-5,237
Nontax Revenue	2,198	2,548	1,913	2,698	1,936	3,313	2,821
Grants	--	--	1	123	--	139	--
Extraordinary Revenue 2/	1,105	1,435	16	1,359	1,896	1,611	1,258
of which: Sales of oil stocks	1,036	1,406	--	1,359	1,880	1,603	1,250
Memorandum items:							
Direct taxes	47,559	50,933	61,005	68,884	81,054	82,477	93,023
Indirect taxes	33,002	43,192	49,255	54,221	59,801	60,187	65,957

Source: Department of Finance, GFS definition.

1/ Fiscal year begins April 1. Excludes repayment of budget lending.

2/ Excludes privatization receipts.

Table 13. South Africa: National Government Revenue, 1992/93 - 1997/98 1/

(In percent of GDP)

	1992/93	1993/94	1994/95	1995/96	1996/97 Budget	1996/97 Prel.	1997/98 Budget
Revenue	24.1	24.8	25.1	25.5	25.8	26.4	26.2
Inland Revenue	19.0	19.7	20.7	20.9	21.4	21.6	21.8
Income tax	13.5	12.7	13.4	13.7	13.8	14.2	14.4
Gold mines	0.1	0.2	0.3	0.2	0.2	0.1	0.1
Other mines	0.2	0.1	0.1	0.1	0.2	0.2	0.2
Nonmining companies	3.5	2.8	3.0	3.1	3.1	3.5	3.6
Individuals	9.7	9.6	10.1	10.3	10.3	10.4	10.5
Sales tax/VAT	5.0	6.4	6.6	6.6	6.6	6.5	6.5
Other	0.5	0.6	0.7	0.6	1.0	1.0	0.9
Customs and Excise	4.1	4.1	4.0	3.9	3.7	3.9	3.7
Customs duty	0.9	0.9	1.0	1.1	1.1	1.2	1.1
Surcharge	0.4	0.4	0.3	0.1	--	--	--
Excise duty	1.3	1.3	1.3	1.3	1.2	1.2	1.3
Fuel levy	2.0	2.0	1.9	1.8	1.8	1.9	1.9
Other	0.4	0.3	0.4	0.4	0.3	0.3	0.3
SACU payments	-0.9	-0.8	-0.7	-0.8	-0.8	-0.8	-0.8
Nontax Revenue	0.6	0.6	0.4	0.5	0.3	0.6	0.5
Grants	--	--	--	--	--	--	--
Extraordinary Revenue 2/	0.3	0.4	--	0.3	0.3	0.3	0.2
of which: Sales of stocks	0.3	0.4	--	0.3	0.3	0.3	0.2
Memorandum items:							
Direct taxes	13.7	12.9	13.7	13.8	14.4	14.7	15.0
Indirect taxes	9.5	10.9	11.0	10.9	10.7	10.7	10.6

Source: Department of Finance, GFS definition.

1/ Fiscal year begins April 1. Excludes repayment of budget lending.

2/ Excludes privatization receipts.

Table 14. South Africa: Economic Classification of National plus
Provincial Government Expenditure, 1992/93 - 1997/98 1/

	1992/93	1993/94	1994/95	1995/96	1996/97 Budget	1997/98 Budget
(In millions of rand)						
Goods and services	60,090	67,486	77,203	83,084	91,193	98,309
Remuneration of employees	42,417	47,734	56,461	58,993	67,614	73,773
Other	17,673	19,752	20,742	24,091	23,579	24,536
Interest 2/	17,530	22,150	24,863	30,321	34,628	38,550
Current transfers	32,707	31,625	34,818	38,998	37,055	37,226
Businesses	10,829	8,620	7,961	8,507	7,683	6,890
Households	10,677	11,360	14,904	16,617	16,297	17,560
Foreign	187	338	231	282	243	253
Other general government institutions and funds	11,014	11,307	11,723	13,592	12,832	12,523
Capital expenditure and transfers	7,771	10,150	11,347	16,652	14,229	14,839
Investment	5,155	6,843	7,935	11,726	10,134	9,396
Capital transfers	2,282	2,974	2,987	4,695	3,935	5,327
Businesses, households and foreign	353	840	508	735	527	1,377
Other general government institutions	1,929	2,135	2,479	3,961	3,408	3,950
Purchases of shares and loans	334	333	425	231	160	116
Unallocated	--	--	--	--	450	1,299
Less: Unspent funds 3/	1,893	4,153	8,024	13,029	--	--
Surrenders	433	746	1,584	4,113	--	--
Funds rolled over to new year	1,460	3,407	6,440	8,916	--	--
Total expenditure (cash)	116,204	127,257	140,207	156,026	177,555	190,223
(In percent of GDP)						
Goods and services	17.3	17.1	17.3	16.7	16.3	15.8
Remuneration of employees	12.2	12.1	12.7	11.8	12.1	11.9
Other	5.1	5.0	4.6	4.8	4.2	3.9
Interest 2/	5.0	5.6	5.6	6.1	6.2	6.2
Current transfers	9.4	8.0	7.8	7.8	6.6	6.0
Businesses	3.1	2.2	1.8	1.7	1.4	1.1
Households	3.1	2.9	3.3	3.3	2.9	2.8
Foreign	0.1	0.1	0.1	0.1	--	--
Other general government institutions and funds	3.2	2.9	2.6	2.7	2.3	2.0
Capital expenditure and transfers	2.2	2.6	2.5	3.3	2.5	2.4
Investment	1.5	1.7	1.8	2.4	1.8	1.5
Capital transfers	0.7	0.8	0.7	0.9	0.7	0.9
Businesses, households and foreign	0.1	0.2	0.1	0.1	0.1	0.2
Other general government institutions	0.6	0.5	0.6	0.8	0.6	0.6
Purchases of shares and loans	0.1	0.1	0.1	--	--	--
Unallocated	--	--	--	--	0.1	0.2
Less: Unspent funds 3/	0.5	1.0	1.8	2.6	--	--
Surrenders	0.1	0.2	0.4	0.8	--	--
Funds rolled over to new year	0.4	0.9	1.4	1.8	--	--
Total expenditure (cash)	33.4	32.2	31.4	31.3	31.6	30.6

Source: Department of Finance.

1/ Fiscal year begins April 1; includes transfers to local government, extrabudgetary funds, and social security funds (though not extraordinary transfers). Date for 1996/97 not available.

2/ Does not include exchange rate losses on amortized loans, as in Table 11.

3/ These comprise allocations that were unspent during the fiscal year. It is not possible to separate these funds from the allocations shown in the other lines. The amounts rolled over are shown within the allocations in the next fiscal year.

**Table 15. South Africa: Functional Classification of Central plus
Provincial Government Expenditure, 1992/93-1997/98 1/**

(In millions of rand)

	1992/93	1993/94	1994/95	1995/96	1996/97 Budget	1997/98 Budget
Protection services	21,165	23,076	27,065	27,657	28,125	29,621
Defence	10,803	10,683	12,908	12,800	11,831	10,716
Other 2/	10,362	12,393	14,157	14,857	16,294	18,904
Social services	51,759	57,983	65,371	79,555	81,368	88,601
Education	24,393	27,761	31,625	36,663	39,166	40,271
Non-tertiary	21,018	23,794	27,064	31,049	32,333	33,074
Tertiary	3,375	3,967	4,561	5,614	6,833	7,196
Health	12,709	13,969	15,565	17,659	18,464	20,223
Social security and welfare	10,031	10,794	13,672	15,655	16,426	18,433
Housing and related services	1,256	1,571	1,648	3,466	1,649	4,162
Other 3/	3,369	3,888	2,861	6,112	5,664	5,512
Economic services	18,419	18,259	17,777	20,181	19,519	18,885
Agriculture, forestry and fishing	6,059	3,719	3,645	4,263	4,366	4,519
Transport and communication	5,628	6,601	6,701	7,666	7,660	7,321
Other economic services 4/	6,732	7,939	7,431	8,252	7,493	7,045
of which: export trade promotion	2,684	2,528	2,248	2,314	1,948	1,428
Other noninterest 5/	9,224	9,943	13,156	12,402	13,465	13,266
Interest payments 6/	17,530	22,150	24,863	30,321	34,627	38,550
Unallocated funds	--	--	--	--	450	1,299
Less: Unspent funds 7/	1,893	4,153	8,024	14,089	--	--
Surrenders and suspensions 8/	433	746	1,584	5,173	--	--
Funds rolled over to new year	1,460	3,407	6,440	8,916	--	--
Total expenditure (cash)	116,204	127,257	140,207	156,027	177,555	190,222

Source: Department of Finance; and Fund staff estimates.

1/ Fiscal year begins April 1; general government comprises central and provincial governments, but excludes local governments, extrabudgetary funds, and social security funds. Data for actual 1996/97 not available.

2/ Police, prisons and law courts.

3/ Recreation and culture, community development, other community services and sewerage and sanitation.

4/ Including water, fuel and energy, mining, manufacturing and regional development.

5/ Including foreign affairs, general research, general administration, cost of raising loans, unallocable expenditure, and certain transfers to government enterprises.

6/ Does not include exchange rate losses on amortized loans, as in Table 11.

7/ Includes allocations that were unspent during the fiscal year. It is not possible to separate these funds from the allocations shown in the other lines. The amounts rolled over are shown within the allocations in the next fiscal year.

8/ In 1995/96, includes recovery from pension fund of R 1060 million, which can not be allocated in the categories above.

Table 16. South Africa: Functional Classification of Central plus
Provincial Government Expenditure, 1992/93-1997/98 1/

(In percent of GDP)

	1992/93	1993/94	1994/95	1995/96	1996/97 Budget	1997/98 Budget
Protection services	6.1	5.8	6.1	5.6	5.0	4.8
Defence	3.1	2.7	2.9	2.6	2.1	1.7
Other 2/	3.0	3.1	3.2	3.0	2.9	3.0
Social services	14.9	14.7	14.6	16.0	14.5	14.3
Education	7.0	7.0	7.1	7.4	7.0	6.5
Non-tertiary	6.0	6.0	6.1	6.2	5.8	5.3
Tertiary	1.0	1.0	1.0	1.1	1.2	1.2
Health	3.7	3.5	3.5	3.5	3.3	3.3
Social security and welfare	2.9	2.7	3.1	3.1	2.9	3.0
Housing and related services	0.4	0.4	0.4	0.7	0.3	0.7
Other 3/	1.0	1.0	0.6	1.2	1.0	0.9
Economic services	5.3	4.6	4.0	4.1	3.5	3.0
Agriculture, forestry and fishing	1.7	0.9	0.8	0.9	0.8	0.7
Transport and communication	1.6	1.7	1.5	1.5	1.4	1.2
Other economic services 4/	1.9	2.0	1.7	1.7	1.3	1.1
of which: export trade promotion	0.8	0.6	0.5	0.5	0.3	0.2
Other noninterest 5/	2.7	2.5	2.9	2.5	2.4	2.1
Interest payments 6/	5.0	5.6	5.6	6.1	6.2	6.2
Unallocated funds	--	--	--	--	0.1	0.2
Less: Unspent funds 7/	0.5	1.0	1.8	2.8	--	--
Surrenders and suspensions 8/	0.1	0.2	0.4	1.0	--	--
Funds rolled over to new year	0.4	0.9	1.4	1.8	--	--
Total expenditure (cash)	33.4	32.2	31.4	31.3	31.6	30.6

Source: Department of Finance; and Fund staff estimates.

1/ Fiscal year begins April 1. Date for actual 1996/97 not available.

2/ Police, prisons and law courts.

3/ Recreation and culture, community development, other community services and sewerage and sanitation.

4/ Including water, fuel and energy, mining, manufacturing and regional development.

5/ Including foreign affairs, general research, general administration, cost of raising loans, unallocable expenditure, and certain transfers to government enterprises.

6/ Does not include exchange rate losses on amortized loans, as in Table 11.

7/ Includes allocations that were unspent during the fiscal year. It is not possible to separate these funds from the allocations shown in the other lines. The amounts rolled over are shown within the allocations in the next fiscal year.

8/ In 1995/96, includes recovery from pension fund of R 1060 million, which can not be allocated in the categories above.

Table 17. South Africa: Financing of the Central Government Budget, 1992/93-1997/98 1/

(In millions of rand)

	1992/93	1993/94	1994/95	1995/96	1996/97 Budget	1996/97 Prel.	1997/98 Budget
Fiscal balance before borrowing 2/	-29,446	-26,819	-25,522	-30,707	-30,682	-30,262	-24,771
Government stock	28,180	38,755	24,990	32,536	27,855	20,644	19,074
Government stock issued	32,219	41,386	34,432	41,368	30,683	27,335	24,305
Discount on government stock	-4,039	-2,631	-9,442	-8,832	-2,828	-6,691	-5,231
Loan levy	--	--	-710	--	--	--	--
Money market instruments	--	--	-19	-4,215	--	--	--
Foreign loans	537	-140	2,604	1,745	947	1,277	3,931
Use of cash balances	5,286	1,537	-1,374	2,356	--	6,738	--
Unusual receipts	1,222	1,506	31	1,358	1,880	1,603	1,766
Privatization	108	--	--	--	--	--	516
Other 3/	1,114	1,506	31	1,358	1,880	1,603	1,250
Unusual transfers	-5,777	-14,840	--	-3,073	--	--	--
Gold and Foreign Exchange							
Contingency	-3,777	-7,500	--	-3,073	--	--	--
Government Pension Funds	-2,000	-7,340	--	--	--	--	--
Other	--	--	--	--	--	--	--
Total financing	29,448	26,818	25,522	30,707	30,682	30,262	24,771

Source: South African Reserve Bank, Quarterly Bulletin, and Fund staff estimates.

1/ Fiscal year begins April 1.

2/ Reserve Bank data for the central government deficit differ from Department of Finance data owing to differences of definition and timing.

3/ Includes National Supplies Procurement and Central Energy Funds.

Table 18. South Africa: Central Government Debt, 1992/93-1996/97

(In millions of rand)

	1992/93	1993/94	1994/95	1995/96	1996/97 Prel.
External debt 1/	2,348	5,201	8,784	10,944	11,523
Domestic debt	143,384	184,769	218,493	259,860	290,329
Marketable	138,681	181,890	216,476	258,892	288,090
Bonds	132,852	174,612	209,458	248,192	273,790
Bills	5,119	6,568	7,018	10,700	14,300
Loan levies	710	710	--	--	--
Nonmarketable	4,703	2,879	2,017	968	2,239
Bonds	334	279	174	60	...
Bills	4,366	2,597	1,840	905	...
Loan levies 2/	3	3	3	3	...
Gold and foreign exchange contingency reserve account 3/	8,934	2,190	4,147	--	2,169
Debt of former homelands 4/	...	...	13,191	8,124	4,003
Total government debt	154,666	192,160	244,615	278,928	308,024
(In percent of GDP)	44.5	48.6	54.8	56.0	55.0
Memorandum items (in percent of total debt):					
External government debt	1.5	2.7	3.6	3.9	3.7
Domestic government debt	92.7	96.2	89.3	93.2	94.3
Marketable	89.7	94.7	88.5	92.8	93.5
of which: Bonds	85.9	90.9	85.6	89.0	88.9
Nonmarketable	3.0	1.5	0.8	0.3	0.7
Other (from above)	5.8	1.1	7.1	2.9	2.0

Sources: South African Reserve Bank, Quarterly Bulletin; 1997/98 Budget Review and April Press statement; and Fund staff estimates.

1/ Adjusted for exchange rate changes.

2/ Including tax exemption certificates and personal saving.

3/ Includes losses on forward exchange cover provided by the Reserve Bank.

4/ This debt is being gradually regularized, mainly into marketable bills.

Table 19. South Africa: Growth Rates of Monetary Aggregates, 1984-96 ^{1/}

(In percent)

	M1A	M1	M2	M3
Changes in the year to the end of:				
1984	14.0	33.6	24.3	18.0
1985	19.8	-7.3	14.1	12.3
1986	20.5	12.8	4.3	9.3
1987	24.8	36.0	22.0	17.6
1988	25.0	23.1	35.2	27.3
1989	10.4	9.6	26.7	22.3
1990	14.3	15.1	12.8	12.0
1991 March	13.6	8.4	16.3	14.1
June	17.0	15.4	20.2	15.7
September	26.2	23.5	22.6	15.3
December	17.7	14.0	15.7	12.3
1992 March	25.2	13.5	11.5	9.0
June	18.6	10.5	11.5	7.2
September	23.6	23.2	12.8	8.7
December	16.2	17.5	10.8	8.0
1993 March	19.4	10.4	5.1	5.7
June	18.1	11.0	1.8	3.3
September	6.9	-0.0	1.3	4.3
December	16.6	6.7	3.9	7.0
1994 March	25.7	19.4	13.6	12.3
June	25.1	28.2	17.4	15.0
September	28.8	26.1	18.5	14.3
December	24.8	23.7	20.6	15.7
1995 March	6.6	10.4	12.6	12.2
June	17.0	7.8	15.6	16.8
September	12.9	12.7	11.5	16.1
December	16.8	19.3	13.9	15.2
1996 March	16.1	27.0	17.8	15.3
June	14.7	28.7	17.9	15.7
September	18.7	30.7	18.4	14.5
December	21.9	30.9	15.7	13.6
1997 March	25.7	30.1	18.8	16.5

Source: South African Reserve Bank, Quarterly Bulletin.

^{1/} M1A includes coins and bank notes in circulation and check and transmission deposits with banking institutions, building societies, and the Post Office Savings Bank. M1 is defined as M1A plus other demand deposits with banking institutions. M2 is defined as M1 plus other short-term deposits and medium-term deposits with banking institutions and building societies (including, for the latter, savings deposits and certain "share" investments), plus savings deposits with, and savings bank certificates of, the Post Office Savings Bank. M3 is defined as M2 plus all long-term deposits with banking institutions and building societies (including, for the latter, other "share" investments), plus investments in national savings certificates issued by the Post Office Savings Bank.

Table 20. South Africa: Monetary Survey, 1992-96

	1992	1993	1994	1995	1996
	December				
	(In billions of rand)				
Broad money (M3)	197.2	211.0	244.1	281.2	319.5
Coin and notes	9.5	10.5	12.2	14.3	15.9
Private deposits	187.6	200.5	231.9	266.8	303.5
Counterparts to broad money					
Net foreign assets	-1.8	-6.5	-7.4	-7.5	-22.0
Short-term	-3.5	-8.2	-9.0	-9.2	-23.9
Gross reserves	11.2	11.0	14.1	18.2	16.8
Reserve Bank	9.1	9.1	11.1	15.7	10.3
Commercial banks	2.1	2.0	3.0	2.5	6.5
Liabilities	-14.7	-19.3	-23.1	-27.4	-40.7
Reserve Bank	-0.9	-5.6	-5.2	-0.0	-0.0
Commercial banks	-13.7	-13.7	-18.0	-27.4	-40.6
Long-term	1.7	1.7	1.7	1.7	1.8
Net domestic assets	198.9	217.5	251.5	288.7	341.5
Government	7.2	7.5	15.5	5.8	10.1
Claims on Government	20.7	26.8	31.9	31.8	39.6
Government deposits	-13.5	-19.3	-16.4	-25.9	-29.5
Claims on private sector	209.5	229.8	268.9	316.2	367.0
Other items, net	-17.8	-19.8	-32.9	-33.3	-35.7
Other assets	49.0	47.9	46.5	56.6	74.9
Capital and reserves	-16.1	-20.2	-24.0	-29.6	-34.6
Other liabilities	-50.7	-47.5	-55.5	-60.4	-75.9
Contributions to growth of M3					
	(In percent)				
Net foreign assets	-1.6	-2.4	-0.4	-0.1	-5.2
Short-term	-2.0	-2.4	-0.4	-0.1	-5.2
Long-term	0.4	0.0	-0.0	0.0	0.0
Net domestic assets	9.5	9.4	16.1	15.2	18.8
Government	2.0	0.1	3.8	-4.0	1.5
Claims on Government	0.1	3.1	2.4	-0.0	2.8
Government deposits	1.9	-3.0	1.4	-3.9	-1.2
Claims on private sector	9.2	10.3	18.5	19.4	18.1
Other items, net	-1.7	-1.0	-6.2	-0.2	-0.8
Growth of broad money	8.0	7.0	15.7	15.2	13.6
Memorandum items:					
Income velocity of M3	1.80	1.88	1.90	1.85	1.81
Deposits at Reserve Bank (in billions of rand)	8.6	9.3	9.3	9.9	9.1

Source: South African Reserve Bank, Quarterly Bulletin.

Table 21. South Africa: Interest Rate Developments, 1992-96

(In percent per annum)

	Short-term rates					Long-term rates	
	Bank rate 1/	Clearing bank prime overdraft rate 2/	Rate on three-month deposits with commercial banks 3/	Rate on interbank deposits at call 3/	Treasury bill rate 4/	Government bond yield 5/	Predominant rate on new mortgages: participation bonds 2/
1992 March	16.0	20.2	15.5	15.5	15.5	16.4	18.9
June	15.0	19.2	13.5	13.8	14.0	16.0	18.9
September	15.0	18.2	12.2	13.0	12.1	14.2	18.4
December	14.0	17.2	12.1	12.0	12.0	14.9	15.9
1993 March	13.0	16.2	11.9	10.9	11.3	14.6	15.9
June	13.0	16.2	12.0	10.8	11.9	14.8	15.1
September	13.0	16.2	11.6	11.2	11.6	13.6	15.1
December	12.0	15.2	10.3	9.6	10.2	12.3	15.1
1994 March	12.0	15.2	10.3	9.6	10.1	13.0	14.0
June	12.0	15.2	10.5	10.4	10.8	14.5	14.0
September	13.0	16.2	11.5	9.8	10.8	16.9	14.0
December	13.0	16.2	12.6	11.6	12.5	16.8	15.1
1995 January	13.0	16.2	11.5	11.6	12.7	17.0	15.1
February	14.0	17.5	13.5	11.7	12.9	16.8	15.1
March	14.0	17.5	13.5	11.8	13.0	16.7	15.1
April	14.0	17.5	13.5	12.5	13.0	16.8	16.7
May	14.0	17.5	14.2	13.1	13.7	16.9	16.7
June	15.0	17.5	14.2	12.9	13.8	16.8	16.7
July	15.0	18.5	13.8	13.4	14.0	16.6	16.7
August	15.0	18.5	13.8	13.5	13.9	16.0	16.7
September	15.0	18.5	13.8	13.6	14.0	15.5	17.5
October	15.0	18.5	13.8	13.9	13.8	15.1	17.5
November	15.0	18.5	13.5	14.1	13.6	14.4	17.5
December	15.0	18.5	13.5	14.8	13.9	14.6	17.5
1996 January	15.0	18.5	13.8	14.3	14.0	13.8	17.5
February	15.0	18.5	13.8	14.2	13.9	14.1	17.5
March	15.0	18.5	13.8	14.1	14.1	15.0	17.5
April	16.0	19.5	14.2	14.6	14.3	15.8	17.5
May	16.0	20.5	14.8	16.0	15.9	16.5	17.5
June	16.0	20.5	15.5	16.0	15.8	15.8	19.5
July	16.0	19.5	15.2	15.3	15.0	15.4	19.0
August	16.0	19.5	15.5	16.2	15.9	15.8	19.0
September	16.0	19.5	15.1	15.4	15.3	15.4	18.2
October	16.0	19.2	15.5	15.7	15.0	15.8	18.2
November	17.0	20.2	15.8	16.9	15.3	16.2	18.2
December	17.0	20.2	16.0	17.7	15.9	16.2	18.6
1997 January	17.0	20.2	16.0	17.2	16.2	15.8	...
February	17.0	20.2	15.8	16.0	15.8	15.0	...
March	17.0	20.2	...	16.0	15.8	15.2	...

Sources: International Monetary Fund, International Financial Statistics; and South African Reserve Bank, Quarterly Bulletin.

1/ Until April 1993, Reserve Bank's discount rate for treasury bills. Thereafter, accommodation rate for overnight loans using government paper as collateral.

2/ End of period.

3/ Period average.

4/ Averages for each Friday of the month.

5/ Average yield on government bonds with a maturity of more than ten years.

Table 22. South Africa: Changes in Bank Credit, 1992-96 ^{1/}

	Credit to the private sector						Credit to Government, net	Total bank credit	Credit to the private sector	Total bank credit
	Bills discounted, deposits, and investments	Hire purchase credit	Leasing finance <u>2/</u>	Mortgage advances	Other loans and advances	Total				
<u>(Change from previous period; in millions of rand)</u>										
1992	2,463	293	1,266	12,160	632	16,815	3,606	20,421	8.7	10.4
1993	-4,976	3,510	993	14,619	6,173	20,317	245	20,563	9.7	9.5
1994	4,084	6,361	1,120	17,334	10,226	39,126	8,032	47,157	17.0	19.9
<u>(Percentage change from year ago)</u>										
1991 March	1,600	-84	169	2,487	4,630	8,801	-3,818	4,983	18.9	20.4
June	-1,924	334	381	2,736	2,526	4,054	935	4,990	16.7	17.6
September	1,660	284	846	2,837	964	6,591	-1,012	5,578	18.5	19.7
December	659	671	862	2,669	25	4,885	1,133	6,018	14.5	12.3
1992 March	-1,818	-894	630	2,819	1,352	2,090	-992	1,097	9.9	9.8
June	1,778	168	347	2,833	-1,260	3,866	-1,123	2,744	9.6	8.4
September	2,343	492	70	3,064	-645	5,322	1,049	6,372	8.6	8.5
December	160	527	219	3,444	1,185	5,537	4,672	10,208	8.7	10.4
1993 March	-1,505	-33	167	3,585	151	2,363	-1,327	1,036	8.8	10.3
June	-2,311	1,135	-141	3,217	-1,188	713	-3,962	-3,249	7.0	7.2
September	-742	1,087	608	4,154	3,790	8,895	2,898	11,793	8.6	9.6
December	-418	1,321	359	3,663	3,420	8,346	2,636	10,983	9.7	9.5
1994 March	-1,208	1,125	302	3,270	3,644	7,134	14,133	21,266	11.8	18.7
June	552	1,325	-43	3,909	-1,926	3,815	936	4,751	13.3	22.7
September	3,648	1,603	275	4,679	4,334	14,541	-1,401	13,140	15.3	22.2
December	1,092	2,308	586	5,476	4,174	13,636	-5,636	8,000	17.0	19.9
1995 March	-802	918	432	5,544	3,569	9,661	-2,046	7,615	17.6	13.0
June	-183	2,260	884	4,636	1,491	9,087	2,416	11,504	19.5	15.3
September	613	2,133	958	4,895	5,026	13,626	-6,743	6,882	18.0	12.3
December	2,447	2,708	488	5,150	4,078	14,871	-3,279	11,592	17.6	13.2
1996 March	403	1,648	651	5,318	6,223	14,242	-2,663	11,579	18.6	14.2
June	-1,316	2,256	915	5,146	3,926	10,927	8,923	19,851	18.7	16.4
September	-583	1,772	1,687	6,529	4,943	14,349	-2,054	12,294	18.1	17.8
December	-68	2,262	9	5,231	3,910	11,343	76	11,419	16.1	17.1
1997 March	674	789	263	5,231	9,167	16,125	4,560	20,685	16.0	19.3

Sources: South African Reserve Bank, *Quarterly Bulletin*.

^{1/} Credit extended by the banking sector, which comprises the Reserve Bank, the former National Finance Corporation, the Corporation for Public Deposits and the "pooled" funds of the former Public Debt Commissioners, the discount houses, the short term business of the Land Bank, the commercial and merchant banks, and other general banking institutions.

^{2/} Excluding unearned finance charges.

Table 23. South Africa: Balance of Payments, 1992-96

(In millions of U.S. dollars)

	1992	1993	1994	1995	1996
Current account balance	<u>1,745</u>	<u>1,852</u>	<u>-340</u>	<u>-2,800</u>	<u>-1,974</u>
Trade balance	5,793	5,844	3,485	1,617	2,045
Exports	23,987	24,171	24,966	28,626	29,120
Net nongold, f.o.b.	17,187	17,299	18,298	22,412	23,000
Gold ^{1/}	6,800	6,872	6,668	6,214	6,120
Imports, f.o.b.	-18,194	-18,327	-21,481	-27,009	-27,075
Nonfactor services	-946	-1,229	-1,282	-1,553	-1,106
Credits	3,754	3,757	4,078	4,575	4,322
Debits	-4,700	-4,985	-5,359	-6,128	-5,428
Factor services	-3,207	-2,895	-2,589	-2,897	-2,870
Credits	914	690	985	972	793
Debits	-4,121	-3,585	-3,574	-3,869	-3,663
Interest	-2,875	-2,659	-2,626	-2,919	...
Dividends and profits	-1,148	-825	-827	-830	...
Taxes	-98	-101	-120	-120	...
Transfers	105	131	45	33	...
Private	32	68	-29	-36	...
Official	73	64	74	69	...
Capital account balance	<u>-1,651</u>	<u>-4,666</u>	<u>1,219</u>	<u>5,303</u>	<u>897</u>
Long-term capital, net	-530	-83	987	4,170	1,137
Private	-1,632	800	-169	2,280	-472
Public	1,102	-883	1,156	1,890	1,609
Short-term capital, net	877	-1,556	1,393	1,782	1,397
Private	891	-1,725	860	2,161	1,346
Public	-14	169	533	-379	51
Errors and omissions	-1,999	-3,027	-1,160	-649	-1,639
Change in net reserves (on a transactions basis) ^{2/}	<u>94</u>	<u>-2,814</u>	<u>879</u>	<u>2,503</u>	<u>-1,076</u>
Change in liabilities relating to reserves ^{3/}	283	2,274	-116	-1,421	-1
SDR allocations and valuation adjustments	114	493	97	45	755
Change in gross reserves	491	-47	860	1,127	-322
Memorandum item:					
Current account/GDP (in percent)	1.5	1.6	-0.3	-2.1	-1.6

Source: South African Reserve Bank, *Quarterly Bulletin*; and Fund staff estimates.^{1/} Net foreign sales of gold plus changes in the gold holdings of the Reserve Bank and other banking institutions.^{2/} Gold and foreign exchange reserves of the Reserve Bank, the banking sector, and the Central Government.^{3/} Liabilities related to reserves include all foreign short-term liabilities of the Reserve Bank and other banking institutions and short-term foreign loans to the Central Government by foreign banks and authorities.

Table 24. South Africa: Quarterly Balance of Payments, 1994-96

(In millions of U.S. dollars)

	1994				1995				1996			
	I	II	III	IV	I	II	III	IV	I	II	III	IV
(Seasonally adjusted figures)												
Nongold exports, f.o.b.	4,364	4,258	4,613	5,063	5,342	5,280	5,753	6,029	5,868	5,403	5,737	5,989
Net gold exports ^{1/}	1,784	1,668	1,762	1,456	1,590	1,530	1,709	1,386	1,653	1,468	1,607	1,413
Imports, f.o.b.	4,830	4,908	5,674	6,057	6,642	6,701	6,713	6,950	6,905	6,622	6,834	6,731
Trade balance	<u>1,319</u>	<u>1,018</u>	<u>701</u>	<u>461</u>	<u>290</u>	<u>109</u>	<u>749</u>	<u>465</u>	<u>617</u>	<u>249</u>	<u>510</u>	<u>670</u>
Net services and transfers	-1,080	-842	-1,041	-866	-1,129	-1,015	-1,224	-1,050	-1,131	-999	-990	-921
Current account balance	<u>19</u>	<u>14</u>	<u>-27</u>	<u>-32</u>	<u>-67</u>	<u>-72</u>	<u>-38</u>	<u>-47</u>	<u>-41</u>	<u>-60</u>	<u>-38</u>	<u>-20</u>
(Actual data, not seasonally adjusted)												
Current account balance	283	50	-497	-160	-806	-1,008	-542	-448	-501	-831	-662	-11
Long-term capital, net	<u>-305</u>	<u>-362</u>	<u>330</u>	<u>1,318</u>	<u>276</u>	<u>1,247</u>	<u>801</u>	<u>1,827</u>	<u>1,143</u>	<u>449</u>	<u>-30</u>	<u>-265</u>
Public sector	-567	62	312	1,329	-132	465	374	1,167	596	255	-221	983
Private sector	262	-424	19	-10	408	782	428	660	548	195	191	-1,247
Short-term capital, net	<u>-252</u>	<u>-326</u>	<u>1,095</u>	<u>-306</u>	<u>1,410</u>	<u>49</u>	<u>-126</u>	<u>-175</u>	<u>-1,179</u>	<u>-104</u>	<u>-142</u>	<u>970</u>
Public sector	6	4	18	506	54	-499	48	21	1	29	-43	61
Monetary sector ^{2/}	699	386	732	-855	512	1,181	258	528	-996	1,456	-79	1,861
Other ^{3/}	-957	-715	345	43	844	-632	-431	-724	-184	-1,589	-19	-952
Total capital movements	<u>-557</u>	<u>-687</u>	<u>1,425</u>	<u>1,012</u>	<u>1,686</u>	<u>1,296</u>	<u>676</u>	<u>1,652</u>	<u>-36</u>	<u>345</u>	<u>-172</u>	<u>705</u>
Change in net reserves (on a transactions basis) ^{4/}	-273	-637	927	852	880	289	134	1,204	-537	-486	-834	695
Change in liabilities related to reserves ^{5/}	-69	440	-561	73	-395	-576	-86	-366	-1	7	130	-132
SDR allocations and valuation adjustments	125	20	8	-53	87	40	-70	-10	341	243	131	70
Change in gross reserves	<u>-217</u>	<u>-177</u>	<u>374</u>	<u>872</u>	<u>572</u>	<u>-246</u>	<u>-23</u>	<u>828</u>	<u>-197</u>	<u>-236</u>	<u>-572</u>	<u>632</u>

Source: South African Reserve Bank, Quarterly Bulletin; and Fund staff estimates.^{1/} Net foreign sales of gold plus changes in the gold holdings of the Reserve Bank and other banking institutions.^{2/} Excluding the Reserve Bank.^{3/} Private nonmonetary sector including unrecorded transactions.^{4/} Gold and foreign exchange reserves of the Reserve Bank, the banking sector, and the Central Government.^{5/} Liabilities related to reserves include all foreign short-term liabilities of the Reserve Bank and short-term foreign loans to the Central Government by foreign banks and authorities.

Table 25. South Africa: Quarterly Balance of Payments, 1994-96

(In millions of rand)

	1994				1995				1996			
	I	II	III	IV	I	II	III	IV	I	II	III	IV
(Seasonally adjusted figures)												
Nongold exports, f.o.b.	15,003	15,380	16,642	17,926	19,048	19,221	20,987	22,033	22,122	23,283	25,645	27,768
Net gold exports ^{1/}	6,134	6,023	6,359	5,155	5,670	5,569	6,234	5,064	6,233	6,325	7,184	6,552
Imports, f.o.b.	16,603	17,728	20,471	21,448	23,682	24,392	24,488	25,399	26,031	28,536	30,548	31,211
Trade balance	<u>4,534</u>	<u>3,675</u>	<u>2,530</u>	<u>1,633</u>	<u>1,036</u>	<u>397</u>	<u>2,733</u>	<u>1,698</u>	<u>2,324</u>	<u>1,072</u>	<u>2,281</u>	<u>3,109</u>
Net services and transfers	-3,713	-3,043	-3,758	-3,066	-4,026	-3,693	-4,466	-3,836	-4,264	-4,306	-4,424	-4,272
Current account balance	<u>821</u>	<u>632</u>	<u>-1,227</u>	<u>-1,433</u>	<u>-2,991</u>	<u>-3,296</u>	<u>-1,733</u>	<u>-2,137</u>	<u>-1,939</u>	<u>-3,234</u>	<u>-2,142</u>	<u>-1,163</u>
(Actual data, not seasonally adjusted)												
Current account balance	974	181	-1,794	-568	-2,873	-3,668	-1,978	-1,638	-1,889	-3,581	-2,959	-50
Long-term capital, net	<u>-1,049</u>	<u>-1,307</u>	<u>1,191</u>	<u>4,668</u>	<u>985</u>	<u>4,540</u>	<u>2,923</u>	<u>6,677</u>	<u>4,310</u>	<u>1,936</u>	<u>-134</u>	<u>-1,227</u>
Public sector	-1,950	223	1,124	4,705	-469	1,694	1,363	4,266	2,246	1,097	-987	4,557
Private sector	901	-1,530	67	-37	1,454	2,846	1,560	2,411	2,064	839	853	-5,784
Short-term capital, net	<u>-865</u>	<u>-1,176</u>	<u>3,949</u>	<u>-1,083</u>	<u>5,027</u>	<u>179</u>	<u>-458</u>	<u>-639</u>	<u>-4,446</u>	<u>-448</u>	<u>-633</u>	<u>4,498</u>
Public sector	22	14	64	1,791	192	-1,817	174	76	3	126	-194	282
Monetary sector ^{2/}	2,404	1,394	2,642	-3,026	1,826	4,298	940	1,930	-3,756	6,276	-353	8,629
Other ^{3/}	-3,291	-2,584	1,243	152	3,009	-2,302	-1,572	-2,645	-693	-6,850	-86	-4,413
Total capital movements	<u>-1,914</u>	<u>-2,483</u>	<u>5,140</u>	<u>3,585</u>	<u>6,012</u>	<u>4,719</u>	<u>2,465</u>	<u>6,038</u>	<u>-136</u>	<u>1,488</u>	<u>-767</u>	<u>3,271</u>
Change in net reserves (on a transactions basis) ^{3/}	-940	-2,302	3,346	3,017	3,139	1,051	487	4,400	-2,025	-2,093	-3,726	3,221
Change in liabilities related to reserves ^{4/}	-237	1,591	-2,025	258	-1,409	-2,095	-313	-1,337	-4	30	583	-613
SDR allocations and valuation adjustments	431	72	30	-189	311	147	-257	-38	1,287	1,047	586	323
Change in gross reserves	<u>-746</u>	<u>-639</u>	<u>1,351</u>	<u>3,086</u>	<u>2,041</u>	<u>-897</u>	<u>-83</u>	<u>3,025</u>	<u>-742</u>	<u>-1,016</u>	<u>-2,557</u>	<u>2,931</u>

Source: South African Reserve Bank, *Quarterly Bulletin*.^{1/} Net foreign sales of gold plus changes in the gold holdings of the Reserve Bank and other banking institutions.^{2/} Excluding the Reserve Bank.^{3/} Private nonmonetary sector including unrecorded transactions.^{4/} Gold and foreign exchange reserves of the Reserve Bank, the banking sector, and the Central Government.^{5/} Liabilities related to reserves include all foreign short-term liabilities of the Reserve Bank and short-term foreign loans to the Central Government by foreign banks and authorities.

Table 26. South Africa: Volume and Unit Value of Exports and Imports, 1991-95

(Percentage change from previous period)

	1992	1993	1994	1995	1996	1995 1/				1996 1/			
						I	II	III	IV	I	II	III	IV
Volume of exports													
Goods and nonfactor services	2.6	4.8	1.0	9.3	7.8	3.2	-2.5	10.2	-1.3	1.6	-2.3	8.1	2.0
Nongold goods and nonfactor services	2.7	6.7	4.0	14.3	10.7	2.0	0.2	7.7	4.1	-1.2	-0.3	7.7	4.6
Volume of imports													
Goods and nonfactor services	5.4	7.0	16.2	16.5	7.6	6.4	-1.2	2.8	2.2	0.2	4.4	3.5	-2.3
Unit value of exports 2/													
Goods and nonfactor services	4.2	9.6	12.0	6.6	10.0	3.4	2.3	0.2	-0.1	2.6	6.6	1.9	2.6
Nongold goods and nonfactor services	6.5	7.5	11.2	7.5	6.0	3.3	1.6	0.3	-0.2	--	5.0	1.8	3.6
Unit value of imports 2/													
Goods and nonfactor services	5.5	8.9	7.6	7.3	7.7	2.7	2.8	-0.4	-0.1	1.0	4.8	2.7	4.5
Terms of trade 3/													
Including gold													
Index 1990 = 100	97.4	98.1	102.0	101.3	103.6	101.4	100.9	101.6	101.5	103.1	104.9	104.1	102.2
Percentage change	-1.2	0.7	4.0	-0.7	2.3	0.6	-0.5	0.7	-0.1	1.6	1.7	-0.8	-1.8
Excluding gold													
Index 1990 = 100	99.4	98.1	101.5	101.5	100.0	102.2	100.9	101.6	101.5	100.5	100.7	99.9	99.0
Percentage change	1.0	-1.3	3.5	--	-1.5	0.6	-1.3	0.7	-0.1	-1.0	0.2	-0.8	-0.9
Memorandum items:													
Effective exchange rate (IFS)													
Nominal	-2.7	-3.6	-5.1	-7.5	-12.0	-2.1	-6.1	2.1	0.7	-1.1	-11.3	-4.3	-2.8
Real 4/	3.5	-1.8	-4.4	-3.1	-7.8	-0.8	-4.6	1.9	1.5	0.7	-10.8	-2.7	-0.2
Trading partners (GEE)													
Total domestic demand	0.4	0.6	-0.3	2.9	3.3	...	...	...	...	...	...	...	...
Non-oil import demand	4.6	6.0	1.6	9.7	5.8	...	...	...	...	...	...	...	...
Domestic demand (incl. exports) 5/	-0.6	2.3	4.7	6.3	4.3	2.0	0.4	1.6	0.5	0.7	1.9	1.6	0.3

Sources: South African Reserve Bank, Quarterly Bulletin; International Monetary Fund, International Financial Statistics; and Fund staff estimates.

1/ Seasonally adjusted quarterly data, except for memorandum items.

2/ In rand.

3/ Goods and nonfactor services.

4/ Relative consumer prices adjusted for exchange rate changes (depreciation -); period average.

5/ Quarterly data are seasonally adjusted.

Table 27. South Africa: Services and Transfers, 1991-95

(In millions of dollars)

	1991	1992	1993	1994	1995
Services					
Receipts	<u>4,486</u>	<u>4,668</u>	<u>4,446</u>	<u>5,062</u>	<u>5,547</u>
Freight	246	364	353	381	335
Other transportation	962	1,024	1,017	1,020	1,005
Travel	1,103	1,182	1,327	1,569	1,917
Investment income	775	838	716	891	883
Interest	165	147	129	188	268
Dividends and profits	518	598	501	602	509
Taxes	92	94	87	102	106
Other income <u>1/</u>	1,400	1,259	1,033	1,202	1,407
Payments	<u>8,444</u>	<u>8,821</u>	<u>8,570</u>	<u>8,933</u>	<u>9,997</u>
Freight	1,059	1,205	1,241	1,363	1,777
Other transportation	1,097	1,094	1,010	1,166	1,171
Travel	1,155	1,545	1,870	1,847	1,822
Investment income	3,281	3,136	2,831	2,824	3,150
Interest	2,078	1,890	1,905	1,877	2,200
Dividends and profits	1,084	1,148	825	827	830
Taxes	120	98	101	120	120
Other payments <u>2/</u>	1,851	1,840	1,619	1,731	2,077
Net	<u>-3,957</u>	<u>-4,153</u>	<u>-4,124</u>	<u>-3,870</u>	<u>-4,450</u>
Freight	-813	-841	-887	-983	-1,441
Other transportation	-134	-69	7	-146	-166
Travel	-53	-363	-543	-279	95
Investment income	-2,506	-2,298	-2,115	-1,933	-2,267
Interest	-1,913	-1,743	-1,777	-1,690	-1,932
Dividends and profit	-565	-551	-324	-226	-322
Taxes	-28	-4	-14	-18	-14
Other	-451	-581	-586	-529	-670
Net transfers	<u>73</u>	<u>105</u>	<u>131</u>	<u>45</u>	<u>33</u>
Private	-27	32	68	-29	-36
Central Government	100	73	64	74	69
Net invisibles	<u>-3,884</u>	<u>-4,048</u>	<u>-3,993</u>	<u>-3,825</u>	<u>-4,417</u>
(In percent of GDP)	(-3.5)	(-3.4)	(-3.4)	(-3.1)	(-3.3)

Sources: South African Reserve Bank, Quarterly Bulletin; and Fund staff estimates.

1/ Income from nonmerchandise insurance and other foreign earnings.

2/ Payments for nonmerchandise insurance and other foreign payments.

Table 28. South Africa: Net Capital Movements, 1992-96

(In millions of dollars)

	1992	1993	1994	1995	1996 prelim.
Long-term capital	-530	-83	987	4,170	1,137
Public sector	1,102	-883	1,156	1,890	1,609
General government	744	51	991	1,258	776
Public corporations	358	-935	165	631	833
Nonbank private sector	-1,390	819	218	1,778	-190
Direct investment, net	-613	-172	-100	-65	161
Nondirect investment, excluding net purchases of securities	19	131	208	498	-1,507
Net purchases of securities by nonresidents	-796	860	110	1,345	1,156
Banking sector	-242	-19	-387	503	-283
Short-term capital	878	-1,555	1,392	1,782	1,380
Public sector	-14	169	533	-379	51
General government	--	--	485	-474	0
Public corporations	-14	169	48	95	51
Nonbank private sector	-268	-712	-102	-319	-1,183
Direct investment	-191	-130	295	-170	44
Nondirect investment	-77	-582	-397	-149	-1,227
Banking sector	1,159	-1,013	962	2,480	2,513
Errors and omissions	-1,999	-3,027	-1,160	-649	-1,620
Net capital movements	-1,651	-4,666	1,219	5,303	897

Source: South African Reserve Bank; and Fund staff estimates.

Table 29. South Africa: External Debt 1/, 1989-96

	1989	1990	1991	1992	1993	1994	1995	1996 ^{4/}
<u>(In millions of U.S. dollars)</u>								
Debt outstanding (at year-end)								
Medium- and long-term <u>2/</u>	8,585	8,504	8,941	8,342	8,145	11,444	12,549	11,222
Public sector <u>3/</u>	5,347	5,248	5,735	5,260	5,481	6,197	7,319	6,840
Private sector	3,238	3,256	3,206	3,082	2,664	5,247	5,320	4,382
Short-term <u>2/</u>	12,012	10,879	9,188	8,959	8,545	7,203	9,765	9,693
Public sector <u>3/</u>	5,575	3,732	2,926	3,200	3,731	3,684	1,363	2,133
Private sector	6,437	7,147	6,262	5,759	4,814	4,519	8,402	7,560
Total external debt	<u>20,597</u>	<u>19,383</u>	<u>18,129</u>	<u>17,301</u>	<u>16,690</u>	<u>18,647</u>	<u>22,314</u>	<u>20,915</u>
Public sector	10,922	8,980	8,661	8,460	9,212	8,881	8,682	8,973
Private sector	9,675	10,403	9,468	8,841	7,478	9,766	13,632	11,942
<u>Memorandum items:</u>								
<u>(In percent)</u>								
Total external debt <u>5/</u> (in billions of rand)	63.5	67.0	70.2	83.2	86.7	98.8	116.9	...
Debt <u>5/</u> /GDP	27.3	24.5	22.8	22.7	21.6	22.9	24.0	...
Debt <u>5/</u> /Exports of goods and nonfactor services	96.2	94.7	94.6	104.8	94.5	95.7	97.4	...
Share of short-term debt in total debt	58.3	56.1	50.7	51.8	51.2	38.6	43.8	46.3
Interest payments/Exports of goods and nonfactor service	8.9	9.0	7.7	6.8	6.8	6.5	6.6	...

Sources: South African Reserve Bank, Quarterly Bulletin; data provided by the South African authorities; and Fund staff estimates.

1/ Foreign currency denominated debt.

2/ The distinction between short-term and long-term debt is not based on the original maturity structure, but on the schedule of repayments, i.e., short-term debt comprises all amortization payments due over the next year.

3/ Central Government, local authorities, public business enterprises, public corporations, and debt of the monetary sector that is not affected by the debt standstill.

4/ As of end-June 1996.

5/ Including rand denominated debt.

Table 30. South Africa: External Reserves, 1992-96

(In millions of U.S. dollars: end of period)

	1992	1993	1994	1995	1996	1995				1996			
						I	II	III	IV	I	II	III	IV
Gross external reserves	3,670	3,252	3,980	4,987	3,589	4,496	4,193	4,155	4,987	4,383	3,791	3,063	3,589
Gross official reserves ^{1/}	2,982	2,676	3,129	4,300	2,202	3,352	3,407	3,233	4,300	3,517	2,598	2,218	2,202
Gold, national valuation ^{2/}	1,992	1,658	1,445	1,481	1,261	1,518	1,619	1,569	1,481	1,693	1,529	1,323	1,261
SDRs	--	12	1	5	1	2	5	6	5	3	2	3	1
Other foreign exchange	990	1,006	1,683	2,815	940	1,833	1,782	1,658	2,815	1,822	1,067	892	940
External liabilities	4,806	5,678	6,531	7,517	8,684	6,636	7,176	7,106	7,517	6,094	7,413	7,183	8,684
Official liabilities relating to reserves ^{3/}	305	2,366	2,216	759	590	1,803	1,201	1,129	759	694	637	745	590
Net external reserves ^{4/}	3,366	887	1,764	4,228	2,999	2,693	2,992	3,026	4,228	3,689	3,154	2,318	2,999
Net official reserves ^{4/}	2,677	311	913	3,542	1,612	1,549	2,206	2,105	3,542	2,823	1,960	1,473	1,612
<u>Memorandum items:</u>													
Gross official reserves													
In millions of rand	9,104	9,092	11,087	15,680	10,305	12,030	12,382	11,793	15,680	13,993	11,254	10,042	10,305
In millions of SDRs	2,169	1,948	2,143	2,892	1,530	2,147	2,170	2,145	2,892	2,406	1,799	1,540	1,530
In millions of dollars, excluding gold	990	1,018	1,684	2,818	940	1,833	1,786	1,662	2,818	1,823	1,067	894	940
In months of imports ^{5/}													
Gross official reserves	1.7	1.4	1.4	1.5	0.8	1.3	1.3	1.1	1.5	1.4	1.0	0.8	0.8
Net official reserves ^{4/}	1.5	0.2	0.4	1.3	0.6	0.6	0.8	0.7	1.3	1.1	0.7	0.5	0.6

Sources: International Monetary Fund, International Financial Statistics; and South African Reserve Bank, Quarterly Bulletin.^{1/} Holdings of the Reserve Bank and Central Government.^{2/} Gold reserves are valued at 90 percent of the average of the last ten London fixing prices during the month.^{3/} Includes December 1993 CCFF drawing (SDR 614 million).^{4/} Gross reserves less official liabilities relating to reserves.^{5/} Imports of goods and nonfactor services.

Table 31. South Africa: Exchange Rate and Gold Price Developments, 1989-97

(Average data)

	U.S. dollar/ Rand	U.S. dollar/ Financial rand 1/		Effective exchange rate 3/		London gold price 5/ In U.S. dollars	
				Nominal	Real 4/	In rand	In U.S. dollars
	Level	Level	Discount	Index 1990=100		Level	
1989	0.381	0.279	28.9	103.3	95.4	998.9	381.5
1990	0.386	0.295	24.2	100.0	100.0	991.9	383.6
1991	0.362	0.315	13.5	94.0	103.0	999.5	362.2
1992	0.351	0.206	37.2	89.5	104.8	980.0	343.7
1993	0.306	0.233	20.9	81.2	100.2	1,176.7	359.7
1994	0.282	0.246	12.9	73.7	97.2	1,363.4	384.0
1995	0.276	...	...	69.5	97.4	1,393.5	384.2
1996	0.233	...	...	60.5	89.4	1,664.0	387.7
1994							
Jan.	0.293	0.225	23.1	79.1	100.4	1,319.5	387.0
Feb.	0.290	0.212	26.5	77.8	99.8	1,316.9	381.8
Mar.	0.290	0.204	29.2	77.1	98.6	1,326.9	384.1
Apr.	0.279	0.217	23.2	74.2	95.9	1,355.6	377.6
May	0.276	0.211	23.8	72.7	95.1	1,383.3	381.3
June	0.276	0.213	22.3	72.2	94.9	1,399.6	385.7
July	0.273	0.217	20.4	70.3	93.9	1,413.6	385.5
Aug.	0.278	0.222	20.2	71.8	96.9	1,368.8	380.4
Sep.	0.281	0.234	16.3	72.2	97.8	1,392.0	391.5
Oct.	0.283	0.249	12.8	71.8	96.8	1,379.3	390.0
Nov.	0.284	0.242	14.1	72.5	97.6	1,354.6	384.4
Dec.	0.281	0.246	12.9	72.6	98.1	1,351.0	379.6
1995							
Jan.	0.283	0.244	13.9	72.5	98.7	1,339.9	378.8
Feb.	0.281	0.256	7.7	71.7	98.4	1,341.1	376.7
Mar.	0.278	...	...	69.2	95.1	1,374.3	382.0
Apr.	0.278	...	...	68.3	95.0	1,409.8	391.2
May	0.273	...	...	67.7	94.7	1,409.8	385.2
June	0.273	...	...	67.7	94.8	1,418.3	387.6
July	0.275	...	...	68.4	96.2	1,405.5	386.2
Aug.	0.275	...	...	69.7	98.3	1,396.6	383.5
Sep.	0.273	...	...	69.9	98.7	1,402.6	383.0
Oct.	0.274	...	...	69.5	99.0	1,398.6	383.2
Nov.	0.274	...	...	69.8	99.7	1,405.8	385.3
Dec.	0.273	...	...	69.9	100.2	1,419.4	387.4
1996							
Jan.	0.275	...	...	70.8	101.6	1,453.2	399.1
Feb.	0.267	...	...	68.9	99.2	1,516.4	404.8
Mar.	0.255	...	...	65.7	94.4	1,556.9	396.4
Apr.	0.238	...	...	61.7	89.1	1,656.6	392.9
May	0.229	...	...	59.5	87.0	1,715.2	392.0
June	0.230	...	...	59.7	88.0	1,676.6	385.3
July	0.228	...	...	58.9	87.6	1,684.5	383.5
Aug.	0.221	...	...	56.9	85.5	1,752.9	387.4
Sep.	0.222	...	...	57.4	86.4	1,724.5	383.2
Oct.	0.219	...	...	56.5	86.0	1,743.7	381.0
Nov.	0.215	...	...	54.8	83.7	1,758.7	377.8
Dec.	0.214	...	...	54.8	84.0	1,729.1	369.2
1997							
Jan.	0.215	...	...	55.8	86.1	1,648.3	355.1
Feb.	0.225	...	...	59.1	91.8	1,544.0	346.5
Mar.	0.225	...	...	59.6	92.8	1,561.4	452.1
Apr.	0.225	...	...	59.6	...	1,532.2	344.6
May	0.225	...	...	58.8	...	1,537.9	344.5

Sources: South African Reserve Bank, Quarterly Bulletin; and International Monetary Fund, International Financial Statistics.

1/ End-of-period.

2/ The difference between the commercial and the financial rand as a percentage of the commercial rand.

3/ IMF estimates.

4/ Relative consumer prices, adjusted for exchange rate changes.

5/ Average daily fixing price per fine ounce.