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GENERAL AGREEMENT ON TARIFFS AND TRADE

REPORT ON THE CONSULTATION UNDER ARTICLE XII:4(b) WITH THE REPUBLIC OF SOUTH AFRICA

1. The Committee has conducted the 1968 consultation with the Republic of South Africa under the provisions of paragraph 4(b) of Article XII. The Committee had before it a basic document prepared by the South African authorities (BOP/87) and documentation provided by the International Monetary Fund.

2. In conducting the consultation the Committee followed the plan for such consultations recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement, pages 97-98). The consultation was held on 1 November 1968. This report summarizes the discussion.

Consultation with the International Monetary Fund

3. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with South Africa. In accordance with the customary procedure the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of South Africa. The statement made was as follows:

> "The Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of October 16, 1968 taken at the conclusion of its most recent Article XIV consultation with South Africa and particularly to paragraphs 2, 3 and 4 which read as follows:
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> '2. Gross domestic product rose in 1967 by nearly 7 per cent, in real terms, in part because of an exceptionally large harvest. Gross domestic expenditure increased rapidly in the early part of 1967 but thereafter advanced at a more moderate pace. Consumer prices rose by about 1 per cent in the year ended June 1968, compared with an annual rate of increase of 3.4 per cent in the first half of 1967. The reduced pressure of domestic demand was also reflected in a decline in imports in the course of 1967; in the first half of 1968, imports were nearly 9 per cent lower than a year earlier. Merchandise exports, assisted by the considerable rise in agricultural output, rose sharply during 1967; in the first half of 1968 they were 28 per cent higher than a year earlier. The current account after registering large deficits in the first half of 1967 moved into surplus in the second half of 1967. The net inflow of private capital accelerated in the early months of 1968 and by the end of June 1968 total reserves amounted to R 941 million ($1,317 million), R 426 million higher than a year earlier.

'3. Since the last consultation, domestic policies have been aimed at eliminating excess demand and restraining increases in costs and prices. Budgetary policies have been tightened and there was a reduction in the year to March 1968 in banking sector claims on the public sector. The authorities have also continued their efforts to slow down the increase in bank credit to the private sector. The Government's stabilization efforts were greatly aided by stronger domestic financial policies, the large harvest, and reduced reliance on external restrictions.

'4. The Fund welcomes the further progress made in relaxing external restrictions and notes the intention of the South African authorities to continue to rely primarily on domestic financial policies in order to maintain internal and external balance. In view of the balance of payments and reserve position, the Fund urges the elimination of the remaining restrictions maintained for balance-of-payments reasons as rapidly as circumstances will permit'".

Opening statement of the representative of South Africa

4. The full text of the opening statement of the representative of South Africa is in the Annex to this report.

5. Following his opening statement the representative of South Africa stated that he wished also to bring to the Committee's attention certain further relaxations and simplifications of import control which had been announced by South Africa only a week before the consultation.[1] One item, namely offset duplicating master paper, had been transferred from the list of goods subject to general import permit to the permit-free list covered by paragraph 1 of the import control orders. In addition, the list of goods enumerated in Annex B, Part II(a) of BOP/87 (that is, 140 basic commodity groupings) had been completely deleted from the list of goods subject to permit under specific import quotas determined from time to time, which meant that the goods thus deleted from the relevant section of the import control orders (paragraph 4(a) of import control orders) were presently subject to the same licensing procedures as those applicable to general merchandise (vide section 4(d)(iii) of BOP/87 or paragrpah 4(a)(i) of import control orders). As specific permits were no longer required for the importation of the goods thus deleted from the lists of goods subject to such specific import permits, it meant that holders of general merchandise import permits could import the goods thus deleted freely under their existing import allocations for general merchandise. This gave them a wider choice of goods that may be imported under their general merchandise permits and there was also a considerable saving in administrative work for them since they no longer had to apply for specific permits for such goods.

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[1] In the following discussion references are made to paragraphs of the import control orders as they stood before the latest changes; these may be found in L/2969 and addenda. The new order will be issued as soon as possible as an L/- document.

6. Furthermore, sixteen basic commodity groupings had been deleted from the list of goods enumerated in Annex B, Part II(b) of BOP/87 (goods subject to permit under specific import quotas determined from time to time i.e. paragraph 4(c) of import control orders which now appear under 4(b)) which meant that these goods were at present also subject to the same licensing procedures as those applicable to general merchandise (vide section 4(d)(iii) of BOP/87 or paragraph 4(a)(i) of import control orders).

7. Finally, two basic commodity groupings (namely lace and radio receiving sets, including gram-radios) had been deleted from the list of goods subject to specific import permit under the system of conversion of general merchandise permits (Annex C of BOP/87 or paragraph 5 of import control orders) which meant that these goods were at present also subject to the same licensing procedures as those applicable to general merchandise (section 4(d)(iii) of BOP/87 or paragraph 4(a)(i) of import control orders).

8. The South African representative stated that the import control policy for 1969 had been announced by the South African Minister of Economic Affairs shortly before the consultation was due to take place and that he would like also to bring details of the Minister's announcement to the notice of the Committee.

9. In brief the policy announced for 1969 is as follows:

(a) Spares, consumable stores, raw materials and components for industry (paragraph 2 of import control orders)

Here a distinction is drawn between merchant importers and manufacturers.

Merchant importers will receive an initial allocation equal to 75 per cent of their total permit allocations for 1968 which were higher than those for 1967. The idea is that, according to customary practice, this initial allocation of import permits for 1969 will be followed by at least one further permit issue during 1969 to give them 100 per cent of their 1968 permit receipts.

Manufacturers will receive their full permit requirements on application in order to enable them to maintain six months' stocks on the basis of their current consumption.

(b) Capital plant and equipment (paragraph 2 of import control orders)

Here, again, a distinction is drawn between merchant importers and manufacturers.

Merchant importers will receive, in respect of capital plant and equipment of an f.o.b. unit cost not exceeding R 1,000 which they supply to manufacturers, permit issues on the same basis as that applicable to merchant importers under (a) above. In respect of capital plant and equipment with an f.o.b. unit cost exceeding R 1,000, merchant importers will receive permits on an end-user basis. This means that they may apply for permits on behalf of individual manufacturers and such permits are then granted freely to them for purposes of replacement of obsolete equipment and for the promotion of efficiency through the modernization of equipment.

Manufacturers will receive import facilities for capital plant and equipment on an individual application basis with due regard to the essential nature of the equipment required.

(c) General merchandise

An initial allocation equal to 75 per cent of the total permit issues made to individual importers in respect of their 1968 imports of goods under paragraphs 4(a) and 4(b) of import control orders will be granted to them immediately, while a further issue of permits to bring them up to the levels of their total permit receipts for 1968 will be made to them during 1969. The 1968 permit allocations were equal to 100 per cent of those for 1967 but were subsequently followed by an invitation to importers to apply for additional import facilities for 1968 if they felt that such additional facilities were necessary to enable them to meet the demand for imported general merchandise.

A large number of importers availed themselves of this facility with the result that their 1968 permit issues for general merchandise were raised above the 1967 levels. Since the 1968 permit issues constitute the basis for permit allocations for 1969, it means that those importers who applied for additional facilities for 1968 have correspondingly raised the basis on which they will receive permits for 1969. This represents a further relaxation of the restrictions on the importation of general merchandise.

(d) Motor vehicles

The policy for 1969 remains the same as that for 1968 - vide section 4(b) of BOP/87.

(e) Textile piece-goods (paragraph 4(a)(ii) of import control orders)

The policy for 1969 will be the same as that for 1968. This means that importers will receive immediately an initial allocation of 75 per cent of their total 1968 permit receipts while a further 25 per cent issue will be made to them during 1969, thus bringing their 1969 permit issues up to the levels of those for 1968.

Balance-of-payments position and prospects and alternative measures to restore equilibrium

10. Members of the Committee thanked the representative of South Africa for his statement and welcomed the new liberalization he had announced. It was recalled that there was a precedent for the announcement by South Africa of new liberalizations made just before a consultation. This could perhaps be interpreted as an indication of the value of the consultations.

11. The discussion then turned to an examination of South Africa's foreign exchange reserve position. Members of the Committee inquired, in the light of the decision of the Executive Board of the International Monetary Fund which had been communicated to them, as to how South Africa justified continued invocation of Article XII. One member mentioned that his country had reserves equal to only about two months' needs, though it had not invoked Article XII for some years past, and asked the representative of the Fund just how the Fund took account of a country's level of reserves in formulating its view on the restrictions. The Fund representative stated that there could not, of course, be a formula or ratio of reserves to imports or total foreign exchange payments of general application for the determination of a particular country's exchange reserve needs. Decisions by the Executive Board of the International Monetary Fund represent a carefully considered judgment taking account not only of all the components of a country's balance of payments and external financial situation, but also of the relevant aspects of its domestic economic situation. He confirmed, in answer to another question, that the Fund statement on South Africa did not include a reference to the effect that at the present time, the general level of South Africa's restrictions which are under reference "did not go beyond the extent necessary ...".

12. Members noted that the increase in foreign-exchange reserves was not the only evidence of the strength and prosperity of South Africa's economy. Exports had increased in the first eight months of 1968 by some 20 per cent over last year, the current account balance was more favourable and anti-inflationary policies had largely succeeded in bringing about price stability; it seemed though that more remained to be done to improve productivity. They emphasized the contribution which full liberalization of imports could make to supporting price stabilization and to helping the productivity programmes, and suggested that restrictions appeared to be maintained not so much on balance-of-payments grounds as for the protection of domestic industry.

13. In reply the representative of South Africa noted that many factors entered into the complex judgment required to determine whether a given situation warranted complacency about the balance of payments. This judgment had to take account of all relevant external and internal circumstances either affecting or likely to affect the present and future level of exchange reserves of each individual country. Referring to the statement of a member of the Committee that his country had reserves which were only sufficient to cover two months' normal imports, the South African representative stated that he could cite other

examples of countries with foreign exchange reserves sufficient to cover anything from six to twelve months' normal imports. He acknowledged that at R 1,020 million reserves were six times higher than they were at the end of 1960. In the judgment of his Government, however, the present reserve position was due entirely to a number of exceptional circumstances which were unlikely to continue to exert their beneficial influences on the balance of payments in the coming year. The general trend of fluctuations in South Africa's reserves during the past eight years, which could be regarded as a representative period, in itself clearly showed that the present high level of reserves could not be regarded as normal. South Africa generally enjoys one good agricultural crop year in seven, and the 1966-67 crop had been remarkably favourable, so much so that exports of a bumper harvest had been carried over into 1968; this factor was estimated to have brought in some R 200 million as a one-time foreign exchange gain. An abnormal capital inflow, much stimulated by uncertainties about key currencies, in the year ended in June 1968 had brought in at least R 340 million beyond what might normally have been expected. Reduced imports, due to anti-inflationary policies and restraint in Government purchasing, had certainly accounted for a saving of at least R 200 million over normal expenditures on imported goods. In addition, there were other special factors, such as the temporary increase in harbour receipts resulting from the closure of the Suez Canal. As regards the balance-of-payments prospects for 1969, it was expected that imports would rise reflecting the more liberal import policy and the requirements for capital goods to fill gaps created by postponements of capital expenditures and for other goods to rebuild inventories and stockpiles. Imports, excluding expected commercial and strategic stockpiling, were estimated to rise by R 200 million over the expected 1968 level. Exports of agricultural goods were estimated to fall by R 100 million, particularly because of prevailing drought conditions, and it was expected that there would be a capital outflow of an additional R 120 million due to the relaxation of exchange control. Taking all these factors together it was estimated by the South African Reserve Bank that reserves by the end of 1969 might be down to R 600 million, or the equivalent of only three months' foreign exchange needs at the present level of imports. This did not take into account the possibility that South Africa's largest goldmine might have to close down owing to its flooding, with the loss of an annual gold output in excess of R 60 million. These and other uncertainties, some peculiar to South Africa's internal and external situation, dictated a measure of caution in regard to the country's foreign reserves, although the South African Government had made real, substantial progress with the liberalization of its import policy as was evidenced by the five successive relaxations of import control that had been introduced during the past eighteen months. There were exceptional difficulties in eliminating immediately all import restrictions, particularly since the restrictions had been in force for twenty years, but South Africa was well aware of the benefits of increasing the competitive position of its industries through a relaxation of import control and through further efforts at making the best use of its labour and other resources. No restrictive measure was maintained solely for protective reasons. The Government's hope was to be able to continue to move ahead with liberalization. On the other hand, it would be premature to contemplate

the submission of a plan and schedule for the removal of the remaining restrictions as had been urged by some members of the Committee. The South African representative stated that comparisons between what other countries which had invoked Article XII have found themselves able to do by way of the submission of firm proposals for the removal of their import restrictions, and what was now being proposed for South Africa showed a certain lack of realism. Such comparisons failed to take account of the exceptional circumstances in which South Africa found itself - circumstances which in no way applied to the other countries concerned. Though only some 15 per cent of imports were still being effectively restricted even before the latest liberalization measures were announced, it would still be a major step for the South African Government to move from the present stage of a modest restriction of imports to complete liberalization and one that could not yet be planned for on any meaningful basis.

14. Members of the Committee expressed the view that since there was clearly no present balance-of-payments difficulty, the answer to questions concerning balance-of-payments prospects would appear to be of key importance. They enquired whether South Africa believed that a worsening of the balance-of-payments situation was considered likely on a scale such as might create the "imminent threat" of a serious decline in reserves which would appear to constitute the only possible basis for continued invocation of Article XII. Members of the Committee expressed interest in this connexion in the components of South Africa's capital inflow and queried whether this inflow was attributable to short-term factors as had been described; it must also reflect the strong earning capacity of some of South Africa's industries. Some funds which might have been transferred for speculative reasons might well remain invested, in gold mining for example. To the extent that the funds represented investment, there was less risk of a reverse flow. In that connexion the question also arose whether South Africa would permit an outflow of the order that had been suggested. If the possibility of a reverse flow were over-estimated, the overall situation, which always involved some uncertainty, might in fact be as favourable to liberalization as it would ever be.

15. The representative of South Africa indicated that the private capital inflow fell, apart from a balancing item on errors and omissions, into three categories. Increases in funds going to the stock exchange were very large, particularly during the first half of 1968 when the rate was double that for the whole of 1967, accounting for an estimated total inflow of some R 120 million over the two years 1967-1968. The second category, other long-term investments, hardly increased at all between the first and second half of 1967 and has in fact declined during the first half of this year. Short-term capital movements were very erratic, switching for example from an outflow of R 25 million during the first half of 1967 to an inflow of R 39 million during the second half and only R 11 million during the first half of this year. Errors and omissions cannot by their nature be analyzed. As to a possible reverse flow of capital, he stated that, in spite of exchange controls which could be employed to prevent certain capital outflows, there were various ways in which reserves would be adversely

affected. There was the possibility of physically exporting stocks and shares from South Africa resulting in an increased outflow of foreign exchange by means of dividend and interest payments; there could certainly be a turnaround in leads and lags of international payments which might cost South Africa as much as R 250 million; and relaxations of controls affecting been residents and blocked assets of non-residents would, after the most recent concessions, cost South Africa an estimated R 120 million per annum. Finally, some of the most profitable industries had been unable to transfer a large share of their earnings abroad due to the scarcity of capital brought about by the credit squeeze. All in all the time was judged less propitious for abandonment of import controls than might appear to outside observers. Individual countries' positions varied greatly as to reserve needs not only amongst themselves but also from time to time within the same country, and South Africa was not among those with minimum needs.

16. It was observed by members of the Committee that the sale of shares of South African companies outside the country would still remain a credit in South Africa's balance of payments. The main point which they noted in this connexion was, however, that South Africa's own estimated reserve needs seemed to increase even faster than her reserves. It was recalled that at the consultation in 1966 when reserves stood at R 583 million the Committee had strongly urged South Africa to draw up a plan and precise schedule that would indicate when trade partners might expect to see a progressive reduction and elimination of remaining import restrictions maintained on balance-of-payments grounds. However, South Africa had vigorously denied the possibility of doing so. At last year's consultation, when reserves stood at R 489 million the representative of South Africa had looked for no dramatic change in this level of reserves and had noted that reserves were equivalent to barely half of the six-month requirement which in its judgment was necessary and had again referred to the impossibility of drawing up a plan and schedule. Thus while the direction in which South Africa's trade policy had in the meantime been moving was welcome, now that reserves had strengthened to over R 1,000 million, it would be most encouraging if South Africa could come forward with a schedule for the elimination of the relatively small range of remaining effective restrictions. The fact that some import permit allocations were not being fully used by importers supported the view that liberalization would cause relatively little difficulty. From every point of view it seemed that South Africa could afford to make this move now and should do so.

17. In response to questions, the representative of South Africa reminded the Committee that the 15 per cent figure for imports under effective restriction should not be taken to mean more than had been claimed for it. Licensing extends to more than 15 per cent of trade and the area of unused licences was outside what his authorities considered to be under "effective restriction". Moreover, the failure to use unused licences was not being taken as a reason for reducing licences in the succeeding period. In response to a further question as to whether quantitative restrictions were being retained as an alternative to the tariff for protective reasons, the representative of South Africa stated that

the use of high tariffs as an alternative to quantitative restrictions was not being considered; it would hardly be in the GATT spirit to replace quantitative restrictions by high tariffs, not to mention that a substantial part of South Africa's tariffs was bound under GATT so that renegotiations would have to be gone through in order to obtain the necessary freedom in that area.

18. A number of questions were also put concerning measures especially in the monetary field which seemed inconsistent with the objective of limiting expenditures in order to avoid a threat of inflation. It was noted, for example, that permission seemed to be granted readily for the establishment of industries in "border areas" where the labour supply was plentiful. Another member commented on a reduction in the bank rate and the termination of a special 7½ per cent reduction in monetary banks' discounts and advances. It also appeared that the Government might itself have contributed to the capital inflow which had seemed to aggravate the excess liquidity problem. The contribution which liberalization could make to supporting other anti-inflationary policies was also noted.

19. In reply, the representative of South Africa stated that the apparent anomaly in the monetary relaxations was explained by the fact that the various credit restrictions and anti-inflationary measures in force had been judged to be somewhat in excess of what were needed at that particular point of time; the extra 7½ per cent credit ceiling measure had moreover been intended to be of a temporary nature only so that its lifting involved only a return to the status quo ante. Similarly as to the reduction of ½ per cent in the Bank rate, it should be borne in mind that the lending rates of the banks were increased fairly generally last year, not as a result of a further increase in Bank rate or at the insistence of the authorities, but with a view to meeting increased costs, including higher deposit rates. As for the share of government and banking in the capital inflow, the central government and banking sector account had moved from a credit position of R 36 million in the first half of 1968 to an estimated credit of only R 5 million in the second half; about half of these funds had been of a long-term character in the first period and nearly all in the second. As regards the subject of costs in industry, with one third of its export earnings coming from a commodity whose price was fixed and beyond South Africa's control, the South African Government was well aware of the need for keeping industrial costs as low as possible.

20. Members of the Committee continued to express reservations as to whether South Africa's remaining restrictions were appropriate under the terms of Article XII. It was noted in this connexion that as recently as August 1968 the value of liberalization as a tool of economic policy in effect had been denied by the Minister of Economic Affairs when he stated (L/2969/Add.4) that a further general relaxation of import control on a global basis would not at this stage have the desired effect, as it had come to his notice that numerous importers were unable to make full use of their permit allocations. The Minister had therefore felt that the granting of additional import facilities would not make

any notable contribution towards easing domestic liquidity problems. In another statement the Minister had made reference to the need to pay due regard to "existing domestic production" in deciding upon appropriate areas for import relaxation. Such views were naturally of concern to the Committee in spite of encouraging developments in South Africa's external trade, in capital inflows and in the movement of its reserves. It appeared to them that any further internal problems which South Africa might face could readily be handled by internal measures rather than by protection through restrictions on imports.

21. The representative of South Africa stated that the quotations drawn from certain Ministerial statements of his Government had been cited out of their proper context. He again assured the Committee that his Government fully appreciated the importance of a sustained forward movement and the important rôle which liberalization of imports had to play in the objective of containing inflation. Import controls were being kept under continuing review. The measures which he had announced to the Committee had been decided upon subsequent to the Minister's statement, which only recognized frankly the unavoidable protective incidence of restrictions long maintained. He stated that the Government had also issued a firm warning to all domestic industries not to rely on import controls and to apply for added tariff protection if they could not compete on the basis of the present tariff alone. Two strong moves had been made to reduce protection and only a small sector, which was to be reconsidered soon, still retained this shelter.

System and methods of the restrictions and effects of the restrictions

22. There was an exchange of views designed to clarify the nature of the new measures taken by the Government of South Africa on 25 October, which the representative of South Africa had announced at the outset. In this discussion it was established that one item had been freed from the requirement of licensing; that a number of items subject to quota restriction on which it had formerly been necessary to have licences specifically endorsed for importation of the particular product, could now be imported with any permit valid for general merchandise or spares, consumable stores, raw materials and components for industry; that another list of products still subject to quota and the specific licensing requirement had been modified and shortened; and that two items subject to specific permit under the system of conversion of general merchandise permits had been deleted from this most restrictive licensing procedure. The resulting relaxations and simplifications of import control were welcomed by the Committee, although the new measures still left all goods subject to one of five kinds of licensing procedure with the exception of the named items in the free list. Members of the Committee called attention in this connexion to the desirability of removing items from the restricted list which constituted the most severe part of the restrictive system.

23. The representative of South Africa pointed out that since the time of the last consultation there had been substantial additional liberalization moves, prior to the latest modifications of import control, the net result of which was to reduce the highly restricted list from some 200 items to twenty-two. He acknowledged that the restricted list was the most restrictive part of the system. He added, however, that there had also been a change in the conversion factor applicable to imports of these restricted items so that importers had to forfeit only R 2 of general merchandise permits instead of R 3, in order to obtain R 1 of permits for goods on the restricted list. In reply to a question as to the reasons for the discretion which had been left to the Minister of Economic Affairs to refuse applications for the conversion of general merchandise permits into specific permits for goods on the restricted list, or to authorize such conversion only on such conditions as the Minister may determine, the South African representative explained that many importers with liberal allocations of general merchandise permits had recently shown a tendency to concentrate all their applications for conversion facilities only on one or two items in the restricted list with a consequent disruption of normal trading patterns and an injudicious utilization of the total amount of foreign currency which could be set aside for the importation of all goods on the restricted list. The South African authorities felt that this tendency had to be curbed since it was still necessary to spread imports in this category over all commodities appearing on the restricted list in order to ensure that minimum commercial quantities of all the goods still subject to severe restriction would be admitted into the country, thereby also ensuring that there would not be discrimination against the trade of particular supplying countries.

24. Commenting on licensing policy as a whole, members noted that the maintenance of the previous year's level of licensing might be somewhat more restrictive than would appear because of inflation and price increases. The South African representative conceded that this was partially true, but pointed out that some prices had in fact declined as a result of the devaluation of certain currencies. Some members of the Committee expressed interest in knowing how quantities to be licensed were decided in those cases where no level of licensing is published, as for example in the case of the strategic goods mentioned in (B) at the top of page 4 of BOP/87 and the items referred to in the next paragraph (C), i.e. those recently transferred from the restrictive régime of paragraph 5 of the Import Control Orders. The level of licences issued for capital goods and consumer goods under the further import allocations which had been announced on 1 August on a selective basis (paragraph (e) on page 6, BOP/87), would also be of interest. One member had noted the reductions which had taken place in one group of textile materials imports during 1968, when import quotas had been reduced to about 20 per cent of their previous level. A member of the Committee noted that in some cases where applications were made for increased tariffs, goods sometimes stayed on quota even after a very high tariff had been accorded.

25. With respect to goods for which the specific levels of licensing are published, the South African representative stated that import facilities are granted on a selective basis on receipt of individual applications. This applied particularly to the large number of strategic commodities in Annex BII(b) of BOP/87 in respect of which it was considered necessary to restrict imports to particular importers participating in the stockpiling programmes. As regards the other goods (i.e. of a non-strategic nature) appearing in Annex BII(b) of BOP/87, the South African representative explained that the inclusion of these goods in that particular list should be seen as an interim stage between their removal from the restricted list and their licensing under the more liberal procedures applicable to general merchandise. The intention was to review the licensing régime in respect of these commodities during 1969 with a view to transferring some of them to the more liberal régime applicable to general merchandise. The South African representative stated that the licensing system applicable to individual categories of commodities would be clearer if reference was made to the import policy for 1969 which had been announced by the Minister of Economic Affairs and which was included in the opening statement made by the South African representative. In this statement a clear distinction was drawn between the licensing procedures applicable to spares, consumable stores, raw materials and components for industry; capital plant and equipment; general merchandise; motor vehicles and textile piece-goods. In respect of the first two categories of imports, viz. spares, consumable stores, raw materials and components for industry as well as capital plant and equipment, the licensing system clearly distinguished between imports by merchants and those by manufacturers themselves; the levels of import allocations received by each of these two groups of importers were set out in the policy statement for 1969 which was included in the South African representative's opening remarks.

General

26. The Committee recognized that progress had been made by South Africa towards liberalization and simplification of the import system, but considered that the level of restrictions maintained by South Africa was not warranted by the present balance-of-payments position and the level of foreign exchange reserves. They noted that there was uncertainty as to the balance-of-payments prospects and that this was relevant to the question of South Africa's continued recourse to the provisions of Article XII. They urged South Africa to review the need for continued invocation of Article XII in the light of the balance-of-payments prospects and to consider the possibility of submitting at an early date a plan and schedule for the elimination of remaining restrictions. The Committee agreed that next year's consultation with South Africa should take place as soon as practicable following the next consultation of the International Monetary Fund with South Africa. The Committee expressed the hope that in the light of information provided to it by the Government of South Africa and the International Monetary Fund, South Africa would then be able to give a further indication of the possibility of establishing a programme for the removal of its restrictions. The Committee thanked the representative of South Africa for his sincere effort to answer their many questions and appreciated the spirit of co-operation in which the consultation had been conducted.

Annex

OPENING STATEMENT BY THE REPRESENTATIVE OF SOUTH AFRICA

South Africa has once again experienced a year of high levels of employment and prosperous business conditions combined with a return to a relative stability of prices. I might add that this stability was achieved in spite of powerful influences beyond the control of the South African Government which, but for the vigilance of the South African authorities in applying appropriate measures, might easily have upset the country's internal equilibrium.

As members of the Committee will recall, particular emphasis was laid during the 1967 consultation on the monetary and fiscal measures that had been taken to bring inflationary tendencies under control.

On the whole, these measures proved to be effective. Price levels over the past year have risen only moderately; a surplus has emerged on the current account of the balance of payments; pressure on scarce resources, which was a feature of the inflationary uprising in 1966 and the early part of 1967, was relieved to some extent and apart from the excessive liquidity prevailing in the economy approximate balance was achieved between aggregate supply and demand.

These conditions of stability have, however, been threatened by various factors - chiefly speculation resulting from international currency uncertainties following the devaluation of sterling last November. This has led to a large and sustained capital inflow which, to the extent that it was invested in stocks and shares, has resulted in sharp increases in share prices and has also considerably increased the liquidity of the economy.

As far as the general economic situation is concerned, a very satisfactory real growth rate in the gross domestic product of 6 per cent was achieved for the year ended 30 June 1968. This high rate of increase was, however, largely due to an increase of no less than 23 per cent in the value added by agriculture which was, in turn, mainly a reflection of favourable weather conditions during the 1966/67 season.

Gross domestic expenditure continued its sharp upward trend in the third quarter of 1967, followed by a decline in the fourth quarter, relative stability in the first quarter of 1968, and a moderate rise in the second quarter. The slow rate of increase in the first half of 1968 can be ascribed mainly to a sharp decline in inventory investments.

Exports have continued to show an irregular upward trend, and have reached a record level in July 1968, after adjustment for seasonal fluctuations. The seasonally adjusted annual rate of exports for the first eight months of 1968 was R 1,570 million which was 21 per cent higher than for the corresponding period of 1967 mainly because of an increase in agricultural exports.

Net gold output, on the other hand, declined by about 3½ per cent between the first half of 1967 and the first half of 1968.

The level of imports, on a seasonally adjusted basis, was comparatively stable in the first half of 1967, but declined in the second half of the year and was followed by a modest recovery in the first half of 1968. For the first eight months of 1968 imports were at a seasonally adjusted annual rate of R 1,851 million, which was 8.7 per cent lower than for the corresponding period of 1967.

While service payments remained relatively stable, service receipts showed a marked increase from a seasonally adjusted annual rate of R 315 million to R 391 million. This increase was largely due to higher harbour receipts, including rising sales of bunker fuel and ships' stores as a result of the closure of the Suez Canal and the consequent diversion of shipping to the Cape route.

Recent trends in the balance of payments on current account provide mainly a reflection of the trends in exports, imports and service receipts to which I have already referred. This seasonally adjusted annual rate on current account improved from a deficit of R 386 million in the first half of 1967 to a surplus of R 15 million in the second half of 1967 and a surplus of R 198 million in the first half of 1968.

In the South African delegation's opening statement at the previous consultation reference was made to the strong inflow of private capital which had taken place during the preceding eighteen months. After the devaluation of sterling last November, the rate of this inflow increased sharply, as is evident from the fact that the net amount of private capital received in 1967 totalled R 235 million while the amount received in the first half of 1968 alone amounted to R 220 million. It is of some significance that a notable increase in the net inflow of private capital took place through the Johannesburg Stock Exchange during the first half of 1968. In fact, the South African Reserve Bank's index of prices of gold mining shares accordingly rose by 44 per cent between October 1967 and June 1968 while the official index of industrial and commercial shares increased by 39 per cent.

In the case of Government and banking capital, an outflow of R 66 million in 1967 was followed by an inflow of R 36 million in the first half of 1968.

As a result of the trends in the current account of the balance of payments and the capital movements to which I have referred, South Africa's gold and foreign exchange reserves rose at a moderate rate from a low point of R 462 million at the end of May 1967 to R 564 million at the end of 1967 but thereafter rose at a relatively sharp rate to R 1,020 million at the end of September 1968.

However, despite this sharp rise the reserves at the end of September were equivalent to only slightly more than six and a half months' imports on the basis of seasonally adjusted imports in the first eight months of 1968 and equal to no more than five months' total current payments.

The favourable balance of payments has also resulted in abnormally high levels of liquidity in the private sector as well as the banking sector. This excessive liquidity in the private sector has caused concern in view of the potential threat which it poses to the stability of the economy. It is felt that a renewed economic upsurge could well develop and that it would be very difficult for the monetary authorities to cope with the resultant inflationary pressures by means of monetary and fiscal measures.

For the present, however, the measures taken by the authorities to combat inflation appear to be adequate. The seasonally adjusted consumer price index rose at an annual rate of only 0.3 per cent from June to December 1967, and then increased at an annual rate of 2.4 per cent from January to July 1968. This change was largely attributable to the reversal of a downward trend in food prices. The seasonally adjusted wholesale price index on the other hand declined at an annual rate of 0.3 per cent in the latter half of 1967, whereafter it increased at an annual rate of 1 per cent during the first seven months of 1968.

The South African Government is aware of the rôle which adequate import facilities can play in dealing with the threat of inflation and, in this connexion, I should like to refer the members of the Committee to the relaxations of import control mentioned in the Basic Document.

An additional anti-inflationary measure, namely the further relaxation of exchange control has also been employed. On 31 July the Minister of Finance announced that more sympathetic consideration would be given to the following applications for foreign exchange: transfers abroad in foreign currency of the local proceeds of the sale of direct long-term investments in the equity of South African enterprises controlled by non-residents; direct investments abroad by South African residents; and redemptions prior to due date of loans owed to foreigners by South African residents. The Minister indicated that the possibility of further progress in this connexion would be considered if this should prove necessary.

The monetary and fiscal measures now being used to combat inflation are still mainly the same as those referred to during South Africa's consultations during the previous two years.

In his budget speech delivered on 27 March 1968, the Minister of Finance reiterated the Government's determination to continue the battle against inflation. The Minister budgeted for a surplus of R 5.1 million. With a view to reducing the liquidity of the private sector, the Treasury has persisted with and has even intensified its policy of sterilizing loan funds raised from the private sector by means of Government stock and Treasury bills issues in excess of its financing requirements.

During the nine months to the end of June 1968, the expansionary effects of the balance of payments were offset, to some extent, by a continued decline in the banking sector's net claims on the Government sector. On the other hand, despite

the ceiling on credit to the private sector, the total claims of the monetary banking sector on the private sector continued to rise until the end of March 1968. Since this rise has in part taken the form of an increase in investments, the South African Reserve Bank decided at the end of May 1968, to restrict the level of certain categories of these investments with the private sector to that obtaining at the end of March 1968.

The authorities were also concerned at the prospect of an inordinate easing of short-term interest rates. At the end of April 1968, the Reserve Bank accordingly instructed the monetary banks to maintain with it not only the normal minimum balance of 8 per cent of their short-term liabilities to the public, but also an additional amount equal to 12 per cent of the increase in these liabilities after the end of March 1968. A further 20 per cent of any increase in these liabilities has to be maintained with the National Finance Corporation. Further steps taken with the same end in view were the issue of Government stock and Treasury bills in excess of financing requirements, the sale of Land Bank bills to the discount houses and the placing of short-term funds abroad by the commercial banks under so-called "swap" arrangements.

In his annual address to stockholders on 27 August 1968, the Governor of the South African Reserve Bank stated that until the factors constituting a threat to the stability of the economy were effectively brought under control, there could be no question of a general relaxation of the Government's anti-inflationary fiscal and monetary policies. He added, however, that it was clear that the control of bank credit could not, without serious dislocation, play a major rôle during the coming year in combating inflation, and he accordingly announced the abolition, with effect from 1 September 1968, of the 7½ per cent reduction in the monetary banks' discounts and advances which was introduced last year, thus enabling the banks to extend additional credit up to the levels which prevailed at the end of March 1965. All the concessions in excess of the former ceiling previously granted had to be brought under the new ceiling. This abolition enables the monetary banks to create new credit to the extent of some R 40 million. However, the banks have been requested to ensure that preference is accorded to production credit for the agricultural and other sectors, and that credit is not extended purely for consumption or speculative purposes. As a special concession the monetary banks are additionally permitted to make available, in the form of discounts and advances to smaller business undertakings an amount equal to one per cent of their new ceiling. This could result in a further increase of R 20 million in their discounts and advances.

Furthermore, the Governor of the Reserve Bank announced a reduction of the Bank rate from 6 per cent to 5½ per cent, and explained that as long as the credit ceiling is maintained, a downward adjustment of ½ per cent in short-term interest rates under the present circumstances need not necessarily increase the potential danger of a new upsurge of inflationary pressures.

In conclusion, I should like to summarize that the principle being employed by the South African Government to avert the threat to the stability of the South African economy, posed by the existence of excessive liquidity, comprise both the full range of fiscal and monetary measures as well as relaxations in exchange and import controls. During the past twelve months no undue increases in price levels have occurred, although the potential danger of inflation still exists, and the authorities will not fail to take such further steps as may be necessary to avert this danger.