REPORT ON THE 1993 CONSULTATION WITH THE REPUBLIC OF SOUTH AFRICA

1. The Committee consulted with South Africa on 7 and 8 July 1993, in accordance with its terms of reference and the Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205). The consultation was held under the chairmanship of Mr. P Witt (Germany). The International Monetary Fund was invited to participate in the consultation, in accordance with Article XV of the General Agreement.

2. The Committee had the following documents before it:

- Basic document submitted by South Africa: BOP/316
- Background paper by the Secretariat: BOP/W/153
- International Monetary Fund, South Africa - Supplementary Background Material for the GATT, dated 9 June 1993.

Opening Statement by the representative of South Africa

3. The opening statement of the representative of South Africa is attached as Annex I.

Statement by the representative of the International Monetary Fund

4. The statement made by the representative of the International Monetary Fund is attached as Annex II.

(i) Balance-of-payments position and prospects; alternative measures to restore equilibrium

5. Members of the Committee recognized the special political and economic difficulties which had been experienced by South Africa since the mid-1980s and expressed their support for the comprehensive political, social and economic changes taking place in South Africa. The adjustment of the economy to the situation caused by economic and financial sanctions had required generation of current account surpluses to counterbalance the effects of a heavily negative capital account of the balance of payments and the denied access to international capital market. The economic growth of South Africa had been slow between 1986 and 1990 and negative since then, with increasing unemployment. International reserves had fallen to a level equivalent to only six weeks of imports. South Africa introduced the import surcharge under the pressure of these circumstances. The Committee noted that at present, the authorities’ room for policy manoeuvre was very limited and was expected to remain so.

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6. Members of the Committee recognized the steps made by South Africa towards trade liberalization, but noted that the country’s tariff structure was too complicated, tariff bindings were at a low level and a number of quantitative restrictions still remained in agriculture, fisheries and forestry. Therefore, they urged South Africa to continue the liberalization of the import regime, increase its transparency, promote competition and the integration of the country’s economy into the international economy.

(ii) System, methods and effects of import restrictions

7. Members noted that the level of import controls in South Africa varied widely by sectors as a result of different measures, maintained for other than balance-of-payments reasons. South Africa was asked to phase out its import permit system, or justify it under the GATT.

8. Committee members welcomed that the rates of the import surcharge introduced for balance-of-payments purposes had been reduced since its introduction. However, they expressed concern that the measure was implemented in a discriminatory way, inconsistently with the basic GATT principle of non-discrimination, as imports originating in certain contracting parties were exempted from it. One member of the Committee, representing a country which was exempted from the surcharge, noted that the objective of exempting his country was to restart trade flows from practically zero level; all exemptions affected only 0.3 per cent of South Africa’s imports. He expressed the hope that the discrimination would be eliminated through a phasing out of the surcharge.

9. The Committee expressed understanding that South Africa was not in a position to eliminate the surcharge at present. However, it requested South Africa to provide a time-table for its phase-out and to consult on any balance-of-payments measures still maintained in mid-1994. Some members noted that, in their view, South Africa should be consulting under Article XII of the General Agreement.

10. In reply, the representative of South Africa stressed that it was not possible for the present Government, nine months before the elections, to take a firm decision on a time-table leading to the elimination of the surcharge. It was expected that the new Government, in the context of the new budget, could address the issue of the surcharge in mid-1994. Thereafter, South Africa would be ready to consult on any outstanding balance-of-payments measure. In respect of the discriminatory implementation of the measure, he stated that it affected only a very small amount of trade. The special treatment given to Turkey would be abolished by the end of 1993, when the bilateral agreement between the two countries providing for the exemption would expire. The phasing out of the measure would solve the problem of remaining discrimination. As to the comments relating to other aspects of South Africa’s trade regime, he noted that these issues were examined in depth by the Council in the recent trade policy review exercise. Finally, he thanked the Committee for the understanding shown for the specific problems faced by South Africa in the present period.
(iii) Conclusions

11. The Committee welcomed South Africa’s readiness to consult on its import surcharge under the balance-of-payments provisions of the General Agreement. It expressed support for the socio-political and economic reform process presently taking place in South Africa.

12. The Committee recognized the political and economic difficulties which had led to the introduction, expansion and present form of the import surcharge. The Committee understood that adjustment to these difficulties had required generation of current account surpluses to deal with a heavily negative capital account of the balance of payments.

13. South Africa had experienced slow growth since 1986 and negative growth since 1990. In 1993, growth was expected to be slow with unemployment increasing further. The level of international reserves was very low, having fallen to around six weeks of imports, despite the recession. The Committee noted that, under the circumstances, and including recent steps towards fiscal consolidation, the authorities' room for policy manoeuvre was very limited and would continue to be so; especially, the need to obtain and maintain an adequate level of international reserves would remain a basic constraint on economic policy.

14. The Committee recognized that the normalization of South Africa’s external trade and financial relations would depend not only on confidence in the political developments, but also on its pursuit of sound macroeconomic and structural policies. In this context, the Committee stressed the need for simplification and greater transparency of South Africa’s complex import régime. It therefore welcomed South Africa’s determination to pursue domestic economic policies that, by accelerating the opening of the economy to internal and external competition, would promote its full integration into the international economy.

15. The Committee welcomed the progress made so far in reducing the rates of the import surcharge and the commitment of the South African authorities to propose its phase out as a priority.

16. Members of the Committee expressed concern that the surcharge was applied inconsistently with the principle of non-discrimination. The Committee urged South Africa to eliminate this discriminatory treatment and emphasized that an early abolition of the surcharge would be the best way to correct this inconsistency with South Africa’s GATT obligations.

17. The Committee urged South Africa to phase out the import surcharge and reiterated the need for a timeframe in this regard. It welcomed the readiness of the South African authorities to provide information on progress by mid-1994. Thereafter, the Committee will consult again on any balance-of-payments measure still maintained.
ANNEX 1

Opening Statement by the Representative
of the Republic of South Africa

In terms of the provision of the 1979 Declaration on Trade Measures taken for Balance of Payments Purposes, South Africa welcomes this opportunity to discuss its continued levying of import surcharge against the background of economic and political developments in the country.

A review of trade policy measures introduced in recent years by the South African Government should begin by taking cognisance of the background against which South African trade policies had to be formulated since the early eighties.

Over a number of years a number of contracting parties deemed it fit to introduce certain trade restricting measures against South Africa which distorted and complicated the environment in which trade policy had to be formulated. It should be recorded that these measures, with a few minor exceptions, have not been notified to the GATT by the contracting parties instituting them. Although many of the measures against South Africa were lifted over the last two years, certain important trade restrictive measures have remained in force. For example, South Africa still has no access to IMF loans, and more than 100 sub-national entities in the United States maintain such restrictive measures against South Africa.

The international political and trading attitude towards South Africa has improved steadily over the last twelve months and the complete normalization of trade relations is now foreseeable. In consequence, South African trade policy is under thorough review. Some contracting parties have already revoked all unilaterally imposed restricting measures against South Africa. However, the total abolition of such measures by all contracting parties clearly is a pre-condition for the complete normalization of trade relations in a wider context.

The import surcharge, which was notified to GATT, was one measure which South Africa was forced to take in order to safeguard its essential national interests. South Africa at that time faced the reality that virtually all of its major trading partners had introduced punitive measures against the country’s exports, while imports from the same countries could continue to expand with no interruption or any interference by the Government. Clearly, no government can let such an imbalance develop without taking some safeguard measures in order to protect the national interest. Of several measures that were at the disposal of the Government, the surcharge mechanism was judged to be the least disruptive to imports and the most transparent to the international trading community.

Regarding the surcharge as such, South Africa has already provided the Committee with details, highlighting its history, the current state of affairs and the prospects for its abolition. I shall return to some of these issues in a moment, updating certain figures in the process.

Let me state at the outset that it is my understanding that the issue before us appears to be the timing of the phasing out of the surcharge, rather than its immaculate design. The South African Government has already committed itself -through repeated statements by the Minister of Finance and by stepwise reductions - to the abolition of this impost. It would, however, be foolhardy to take the last steps before the right circumstances are firmly in place - and it is clearly not only our judgement that the time is not yet right!
In studying GATT documentation and the records of recent proceedings regarding other member countries' use of measures that restrict foreign trade in order to alleviate short-term balance-of-payments instability, the validity of an import surcharge in the GATT context does not appear to be at issue. What does seem to meet with apprehension is the fact that the surcharge is levied on some bound items, the long duration of what was envisaged as a temporary levy and differential rates.

If South Africa's surcharge were to be assessed in the normal way, GATT contracting parties will presumably find reason for dissatisfaction on account of these three factors. As indicated in my opening remarks, you cannot, however, in all fairness ignore the GATT-alien actions instituted by governments and institutions against my country. These actions, some of which are still in force, left my authorities no other alternative but to introduce this measure in 1985. This step reflected the inevitability of having to address problems experienced on the capital account of the balance of payments, through a measure that affected the current account.

In order to protect South Africa's creditworthiness and honour its loan commitments to ensure continued access to financial markets, South Africa - who certainly even then did not have an inordinately high foreign indebtedness - on 1 September 1985 was forced to close its foreign exchange markets and the Stock Exchange and introduce a temporary standstill in the repayment of certain categories of foreign debt, mainly short-term bank debt. The liquidity problem (in the form of short-term capital outflow) resulting from the unilateral and adverse actions by certain American banks, necessitated a range of measures to protect the country's foreign reserves and, in general, the balance of payments.

With effect from 23 September 1985 South Africa consequently introduced a surcharge of 10 per cent on all imported goods that were not bound in terms of GATT. In South Africa’s communication to GATT the reason was clearly stated, namely "... to forestall the imminent threat of a serious decline in South Africa’s monetary reserves".

The most important changes since 23 September 1985 were:

(a) As a result of a rapid rise in the import of goods, coupled to a sharp increase in the outflow of capital (mainly short-term) which placed the country’s reserves under exceptional pressure, certain goods bound under GATT became subject to import surcharge as from 15 August 1988. In value terms, these goods amounted to 27% of the imports under surcharge in 1992, the latter, in turn, comprising 50,4% of the total import of goods.

(b) The introduction of differentiated rates to approximate a balance between the need to reduce a sharply increased flow of imports for balance-of-payments reasons and the necessity of the various imports in domestic production. On this basis four basic categories, each with a different general rate, was introduced.

(c) As part of agreements with certain countries that had no formal trade agreements with South Africa and as a quid pro quo for their early lifting of trade sanctions against South Africa, exemption from surcharge was allowed on a country basis in respect of Hungary (10 August 1990), Poland (28 June 1991) Czechoslovakia (12 September 1991) and Romania (29 November 1990). The total value of imports from these countries amounted to only R250 million ($75 million) in 1992. A preferential trade arrangement concluded with Turkey, with effect from 1 January 1988 also provided for exemption from import surcharge in respect of certain specified products. This
arrangement expires on 31 December 1993. In addition, different types of exemptions have been given to a number of Southern African countries under preferential trade agreements or arrangements. These include Zimbabwe, Malawi, Mozambique and Mauritius. The benefit of surcharge exemption on a country basis will of course disappear when the surcharge is abolished.

(d) The South African Government has already progressed far in phasing out the surcharge. Since introduction, the different rates for the four categories have been reduced to the following levels:

- "luxury" goods: from 60% to 40%
- "household" goods\(^1\) from 20% to 15%
- capital goods: from 15% to 5%
- intermediary goods: from 10% to 5%

In the nature of the measure, it has a revenue effect. In 1992/93, the surcharge amounted to a gross figure of R1,5 billion, which was 2,0 per cent of central government revenue or 0,4 per cent of gross domestic product. The revenue for the exchequer related to goods bound under GATT amounted to R435 million in the financial year 1992/93.

Why was the surcharge retained for so long a period and why did we resort to such a differentiated structure? The first question had everything to do with the nature of our balance-of-payments and foreign exchange reserve predicament. In essence, the whole period from August 1985 to the present was on balance characterized by deliberate deflationary policies to preserve and build up desperately needed foreign reserves during a period of negotiated foreign debt repayment and other net capital outflows in the absence of a banker of last resort, i.e. the IMF, as the result of sanctions imposed by the United States of America. The South African balance-of-payment problem which precipitated the introduction of the import surcharge, as part of a policy package, was not conventional. It did not present itself as a current account deficit and it was not of a short-term (cyclical) nature. In fact, over the period 1985 to 1992, a cumulative current account surplus of R40,5 billion had to be realised. Such was the capital outflow that this resulted in the gross gold and foreign reserves increasing by only R5,8 billion over this period. Despite the fact that even this level is still very low, uncomfortably so, we are confident that the price, in terms of growth forfeited, was worth the better base which our much improved international debt ratios should present for future economic growth and foreign investor confidence, once a political settlement is reached. (Since August 1985, when South Africa's foreign debt ratio amounted to 42,9% of GDP, this ratio was reduced to 15,1% at the end of 1992). It should be clear, however, that measures such as the import surcharge were necessitated by circumstances that required South Africa to artificially "manufacture" a current account surplus for eight consecutive years and which regrettably had serious consequences on employment. Estimates are that approximate 40 per cent of the labour force is currently unable to find employment in the formal sector of the economy.

Unfortunately, the problem is not over yet. Recently a further adverse movement in foreign reserves appeared. Details about the reasons for this trend, which has not (yet) been very much influenced by recent gold price increases, are given in our background report. The continued drought, leads and lags in short-term capital flows and the adverse effect of political uncertainty and violence

\(^1\) E.g. consumer goods such as refrigerators, stoves and washing machines (so-called "white" goods)
on capital movements in general, are the main factors. The fact that virtually no current account surplus was recorded in the first quarter of 1993, accentuates the dilemma, especially in the absence of the facilities the IMF would normally provide.

As a consequence of the decline in the current account surplus and the considerable weakening of the capital account of the balance of payments, the country's net gold and foreign reserves dropped by R3,7 billion during the second half of 1992 and by a further R3,3 billion during the first quarter of 1993. This represents a clear turn-about, since reserves had been laboriously re-built by R6,1 billion from June 1989 to June 1992.

At the end of March 1993 the country's gross gold and foreign reserves (including the Reserve Bank's use of external credit facilities) amounted to R9,5 billion, compared to R13,2 billion at the end of August 1992. Over this period the import cover fell from an equivalent of 8 weeks' import of goods and services, to less than 7 weeks (still a very low level).

The need for continued caution regarding the balance of payments stems from three factors. Firstly, 1993 is the last year of South Africa's Third Interim Foreign Debt Arrangements with its foreign creditor banks. In terms of these arrangements an estimated R1,3 billion of foreign debt will have to be repaid during 1993. Together with debt repayment outside the "net", the total net capital outflow can amount to R5 billion in 1993. Although clarity should be obtained soon on the outcome of the current negotiations regarding the repayment of the estimated January 1994 foreign debt figure of about R16 billion in the "net", repayment in the absence of any significant capital inflow will continue to represent a particularly harsh balance-of-payments constraint. Of this amount, an estimated R2 billion will have to be repaid in 1994 alone. Secondly, as might be expected, the process of political transition and constitutional negotiations entails a regrettable degree of instability which, together with the occurrence of violence and very high unemployment, creates uncertainty that enhances the risk of capital outflows and delays the normalization of the country's international financial relations, which is a prerequisite for new foreign loans. Thirdly, an economic upswing that leads to an early rise in imports, will add to the vulnerability of the balance of payments, even if the current account remains in considerable surplus.

It is realised, of course, that the balance-of-payments question is a reflection of a multitude of deep-seated economic problems. The road to economic recovery and sustainable economic growth requires a comprehensive restructuring of the economy, important ingredients of which were envisaged by my colleague, the Director-General of Trade and Industry in his opening statement at the Trade Policy Review on South Africa on 1 and 2 June 1993. It is therefore of crucial importance that consensus be reached on a programme of economic restructuring amongst the various role players in the country. Contracting parties' attention has already been drawn to the Normative Economic Model released by the Minister of Finance and of Trade and Industry as a discussion document to facilitate this process. The National Economic Forum, the tripartite mechanism set up between Government, Business and Labour, is intent upon achieving such consensus in the next few months. This is very important from the point of view of ensuring strong policy leadership by the Transitional Executive Council likely to be established soon and for which the necessary legislation will be passed in October this year, as well as by the new Government of National Unity to be formed after the first non-racial democratic election scheduled for 27 April 1994.

Progress being made in seeking consensus on the nature of economic restructuring already shows very promising results in terms of the acceptability of a development path that recognizes, inter alia:
the importance of monetary and fiscal discipline to establish and maintain macro-

economic stability;

the need for increased investment in the social field, notably in appropriate and good
education and training;

efficient and flexible domestic goods and factor markets; and

an outward-orientated growth strategy, based on improved productivity and international
competitiveness through a gradual and systematic opening up of domestic markets to
international competition.

The rebuilding and reconstruction of the South African economy has to take place as part of
the process of normalizing its foreign trade and financial relations. The fact that we are considering
a revision of our original tariff offer to aim at meeting the Uruguay Round objectives, testifies to our
seriousness in this regard. We also realise that the abolition of import surcharge will facilitate matters
further. At the same time, we call upon members of this Committee to recognise the transitional stage
in which South Africa finds itself at the moment, both politically and economically. They should also
actively assist these processes so as not to impair the progress towards reform and, more importantly,
the economy as such. The need to reverse the capital outflow is an obvious first priority. Beyond
that, the New South Africa needs not only the world’s moral support and assistance, it needs to be
able to establish the right conditions for attracting foreign loans and equity investment. Hopefully,
a substantial flow of concessional and developmental finance will emanate in this process.

Before concluding with some remarks on future prospects, a brief word is needed regarding
the other question raised earlier, namely the differentiated nature of the surcharge. The different rates
for different categories of goods were obviously aimed at placing a lesser constraint on goods that were
more essential in the production process. The extension of the surcharge to some GATT-bound goods
should be viewed in the same context. The differentiation between countries reflected, for a large
part, the abnormal circumstances which the country faced during the height of sanctions. The sanctions
era was characterised by many unorthodox steps against and by South Africa. Country-differentiation
with regard to import surcharges was, in certain cases, part of all this. Clearly, the appropriate way
to “level the playing fields” is to abolish the import surcharge when circumstances permit, rather than
to do away with arrangements in respect to specific countries that already reflect a normalized situation.

In this regard, the important remaining question is the timing of the abolition of the surcharge.
I conclude, therefore, with a few remarks on the prospects for the economy and the phasing out of
the surcharge.

South Africa is in its fifth year of economic downswing, experiencing its longest recession
since 1908. Having had negative rates of growth for 1991 and 1992, prospects for 1993 look slightly
better and we may see the beginning of a long-awaited upswing. Assuming a relatively normal
agricultural crop, latest projections for 1993 - statistically at least - point to an overall economic growth
rate of, at best, 0,5 per cent in real terms. This will be accompanied by an estimated current account
surplus that could be less than the projected long-term capital outflow. Under these circumstances
there would be no room at all for any relaxation of the import surcharge - less so for as long as or
insofar as sanctions regarding foreign loans to and investment in South Africa remain in force in certain
countries and South Africa’s access to normal IMF facilities has not been resolved beyond any doubt.
On the contrary, much skill will actually be required to avoid further restrictive policy measures during
the course of 1993 to safeguard the balance of payments.
Given the fact that South Africa will have an election in April 1994, the earliest next opportunity for a full reappraisal of the prospects for an early reduction or even total phasing out of the surcharge would probably not be before the middle of 1994. By then there may be much greater clarity on the timing and strength of the country’s next economic upswing (to be substantially influenced by the extent of economic recovery in OECD countries), the precise arrangements with foreign creditor banks, the process of political development and the nature of economic restructuring. Should these developments hold the prospect of an amelioration of the balance-of-payments constraint, in support of a sustainable economic growth phase of some significance, the abolition of the surcharge may then become feasible. In quantitative terms, an economic growth rate of between 1 and 2 per cent for 1994, coupled with a current account surplus of at least R5 billion, are regarded as prudent reference figures, i.e. assuming that no net foreign capital inflow occurs.

It is unfortunately a fact that the South African Government would be failing in its obligations to its citizens - also the large number of unemployed South Africans - if it did not, for the time being, continue to levy the surcharge. We shall, of course, continue to notify the GATT of any changes in the application of this measure.
ANNEX II

Statement by the IMF Representative

During the past three years, considerable progress has been made in South Africa’s socio-political environment, particularly the repeal of most of the basic legislation that upheld apartheid. These legislative actions cleared the way for ongoing negotiations for an interim constitution and for a redress of the social inequities brought on by the previous system. Political uncertainty, however, has continued to exert a negative economic influence on an economy already weakened by trade and financial sanctions which have required rigorous adjustment since 1985.

The financial sanctions, in particular, resulted in a marked change in the country’s external accounts. After a long tradition of being a net user of external savings, South Africa was denied access to international capital markets, obliging it not only to depend on its own domestic savings but also to repay foreign capital on a significant scale. The South African authorities used both exchange rate policy and an intensified system of trade protection to bring about the required shift in the external current account balance. In addition, they reintroduced the financial rand system, which helped contain the depreciation of the commercial exchange rate, and negotiated a series of interim arrangements for the restructuring of a large portion of the external debt.

Consequently, since 1986, South Africa has generated a series of current account surpluses, averaging 2-3 percent of GDP per annum, compared with deficits of about the same magnitude previously. These surpluses allowed capital repayments of over 2 percent of GDP annually, as well as some build-up in reserves. The containment of the external disequilibrium, however, was at the expense of a slowdown in output growth, which was exacerbated by the investment-damping effect of political uncertainty. Real GDP growth averaged less than 1 percent per annum during 1986-92. Since 1990, output has declined continuously, with the downward trend aggravated by a severe drought in 1992. By 1992, real per capita income had fallen 15 percent below the level of the early 1980s, and the investment ratio had dropped by one-third to about 16 percent of GDP, barely sufficient to replace depreciating capital.

During 1986-89, efforts to sustain growth through relaxed financial policies contributed to a depreciation of the rand and higher inflation. Since 1990, the authorities have attempted to contain price pressures by shifting to a tighter monetary policy. At the same time, however, they have accepted a larger government deficit brought about by the recession and an increased commitment to social spending (education, health, and pensions). While tight money succeeded in bringing inflation down to a little below 10 percent in December 1992 for the first time in 15 years, the government deficit, estimated at over 8 1/2 percent of GDP in the year ending March 1993, did little to lift the economy out of the recession. Moreover, wage rates proved relatively unresponsive to unemployment, which reached a disturbingly high level. On the external front, the balance of payments turned into a large deficit beginning in mid-1992 on account of the impact of the drought on agricultural exports and imports, the fall in South Africa’s international terms of trade to their lowest level in two decades, and the net capital outflows prompted by the higher risk premia on foreign borrowing that accompanied domestic instability. By end-April 1993, gross reserves had fallen to a level equivalent to only about six weeks of imports.

Without an improvement in the terms of trade, the prospect for 1993 is for very little growth. The budget for the current fiscal year envisages a cut in real expenditure and a tax adjustment to raise the revenue/GDP ratio while increasing the incentives for corporate savings. These steps toward fiscal
consolidation are welcome. However, in the absence of a significant turnaround in the availability of foreign financing, the fiscal deficit, projected at 7 percent of GDP, would still crowd out any incipient rise in private investment. Also, the increase in the government debt, together with growing off-budget obligations, is likely to impose serious fiscal constraints on the policies of future governments. In this light, and in light of substantial prospective demands on the budget, a more restrictive stance on government spending is warranted.

In the circumstances, the monetary authorities' objective of containing inflationary pressures and preventing a further drop in reserves is in conflict with the desire to support a recovery. In particular, high real interest rates are holding back a turnaround in the inventory cycle. A reorientation of the policy mix—toward a tighter fiscal stance and some easing of monetary conditions—would bolster private sector activity and probably strengthen the trade balance. However, a sharp depreciation of the rand should be avoided for fear of exacerbating uncertainty or provoking an inflationary wage response.

The current account surplus of recent years is attributable not only to the macroeconomic stance, but also to active commercial policy. South Africa’s trade regime has traditionally been inward-looking, aimed largely at import substitution; sanctions entrenched this orientation. In addition to a complicated network of import licensing and high tariffs, a 10 percent import surcharge was introduced in 1985 to protect the balance of payments. In 1988-89, the surcharge was broadened and raised to a maximum of 60 percent on some items. The authorities began to reduce it in 1990, and in 1991 it reached its present level of between 5 percent (applicable to capital and intermediate goods) and 40 percent (luxury goods). The recent expansion in manufacturing exports reflected, in part, the weakness of domestic demand, but it also relied heavily on export subsidies. More generally, the South African economy is extensively controlled, resulting in a high degree of market inefficiencies. Besides the system of protective tariffs and subsidies, the key structural distortions include an interventionist industrial policy, restrictions on capital movements, and excessive government claims on scarce resources.

The Government recognizes the urgent need for structural transformation, including the priority of job creation for a growing labour force. The Government’s medium-term economic objectives and proposals (contained in the Normative Economic Model put forward in March 1993) envisage a significant revival of productive investment and a steady recovery of growth largely through progressive removal of the existing distortions. Central to this approach is the need for less direct government involvement in the economy and for policies aimed at improving competition in the domestic market, in part through a more open trade policy.

The medium-term strategy for structural change has yet to gain acceptance among the various groups that are likely to form the Government following the multi-racial elections planned for early 1994. In particular, issues such as the appropriateness of centralized wage bargaining and the degree of intervention to remedy the injustices of the apartheid economy remain unresolved. However, there seems to be an emerging consensus on the need to dismantle the trade control system—although not necessarily on the pace of change. Progress has been made on tariffication of quantitative restrictions, and relatively few of the latter remain. For the future, it is envisaged that the trade regime will become more export-oriented, with lower protection generally and with exporters having unrestricted access to imported inputs at international prices. The protection system will be simplified, with the import surcharge removed, formula duties replaced by antidumping measures, and the tariff structure rationalized. The Fund supports this stance, which is intended to allow the economy to develop along the lines of its comparative advantage.
Although the political environment is expected to permit an early lifting of sanctions, which could ease the pressure on financial flows, much uncertainty remains. If there are recurrences of domestic disturbances, the investment outlook will be weakened even further and risk premia for foreign capital inflows will remain high. On the other hand, even if the political transition stays on track, it will be some time before the beneficial impact of a reorientation of policies will be felt. In any event, increasing repayments are scheduled in connection with the external debt agreements. For these reasons, the authorities are implementing trade reform with caution and refraining from any action that could further weaken the balance of payments position in the short run. In this environment, and in light of the sharp decline in reserves since August 1992, the authorities thought it imprudent to carry out their earlier plan to remove the import surcharge in the 1993 budget.

In the immediate future, the need to maintain an adequate level of international reserves will remain a basic constraint on economic policy. Any sharp tightening of financial policies, however, would risk further depressing production, employment, and investment. Therefore, the management of aggregate demand and international reserves will require a delicate balance of all the available policy instruments: in particular, a steady reduction in the fiscal deficit, a careful relaxation of monetary conditions, and a supportive exchange rate will be important in the period ahead. At the same time, early and steady movement toward structural reforms, including a liberalization of the exchange and trade system, should help lessen supply constraints, restore trade flows, and strengthen the underlying balance of payments position. South Africa’s access to foreign markets in both products and capital will be crucial throughout this process.