1. The Committee has conducted the 1961 consultation with the Union of South Africa under the provisions of paragraph 4(b) of Article XII. The Committee had before it a basic document prepared by the secretariat in collaboration with the South African authorities (MT(61)10/Rev.1) and certain documents provided by the International Monetary Fund. In conducting the consultation the Committee followed the plan for such consultations recommended by the CONTRACTING PARTIES. The consultation was completed on 26 April 1961. The present report summarises the main points of discussion during the consultation.

Consultation with the International Monetary Fund

2. 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 agreed 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 International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision relating to the last consultation with the Union of South Africa under Article XIV of the Fund Agreement and the background material prepared in connection with that consultation. The Fund has also provided a supplementary paper, dated April 6, 1961, to supply background information on recent developments.

"With respect to Parts I and III of the Plan for Consultations the Fund draws the attention of the CONTRACTING PARTIES to the Executive Board decision of December 28, 1960\(^1\), taken at the conclusion of its recent consultation with the Union of South Africa, and particularly to paragraph 3, which deals with the balance of payments and reserve position, and to paragraph 4, which deals with the restrictive system of the Union of South Africa. On the same date, the International Monetary Fund agreed to a request by the Government of South Africa for the purchase of sterling and deutsche mark each to an amount equivalent to $18,750,000.

\(^1\) See Annex II.

Spec(61)143
"As will be noted from paragraph 3 of the Fund decision referred to above, reserves fell from £SA151.9 million at the end of 1959 to £SA85.6 million on December 2, 1960. On March 24, 1961, they amounted to £SA95.4 million. This figure included the Fund drawing of £SA13.4 million. The general level of restrictions of the Union of South Africa which are under reference does not go beyond the extent necessary at the present time to stop a serious decline in its monetary reserves.

"With respect to Part II of the Plan for Consultations, the Fund draws attention to the decision taken at the conclusion of its last consultation with the Union of South Africa. The Fund has no additional alternative measures to suggest at this time.

"Perhaps I should add, Mr. Chairman, that the foregoing statement was drafted and approved in the Fund in the light of the latest information then available to the Fund, including the information on page 5 of the supplementary paper, under the heading 'Restrictive System'. We have been informed by the delegation from South Africa that certain other changes have since taken place. Undoubtedly the delegation will supply the Committee with information on these later changes."

Balance-of-Payments Position and Prospects

3. The representative of the Union of South Africa opened the consultation with a statement on developments in the economic field in South Africa during 1960 and on certain modifications which his Government had recently introduced in the import control system. The complete text of this statement is attached as Annex I to this report.

4. The South African representative recalled that at the time of the last consultation in May 1960 the general economic recovery in South Africa which had begun about nine months earlier was reaching its height. Interest rates continued to fall and merchandise exports were expanding. Export prices ceased to decline further and there was a substantial increase in gold output. As a result there was at that time a steady rise in the country's gold and foreign exchange reserves.

5. Taking 1960 as a whole South African imports, however, increased substantially to a level approaching the record level of 1958. This increase had largely been due to the appreciable expansion of general economic activity in the country, but it also reflected the flexibility of the import control system and its liberal administration. To a certain extent the
rise in imports might be attributed to the replenishment of depleted inventories and speculative imports in anticipation of a possible intensification of the import restrictions. On the other hand, net exports increased only slightly in 1960. Excluding re-exports there was actually a slight decline in the exports of South African produce. This decline was mainly due to the somewhat depressed conditions which prevailed in the markets for certain primary commodities.

6. The substantial increase of R.133 million in merchandise imports and the slight increase of only R.6 million in merchandise exports resulted in an increase in the trade deficit by about R.127 million. This, combined with changes in current invisible payments and gold output, resulted in a reduction in the net current surplus of about R.128 million, i.e. from R.158 million in 1959 to R.30 million in 1960. A net out-flow of capital in all forms of R.162 million, therefore, caused South Africa's gold and foreign exchange reserves to decline by R.132 million in 1960. This substantial net out-flow of private capital occurred mainly during the first, second and third quarters of the year.

7. The gold and exchange reserves of South Africa stood at R.304 million at the end of 1959 and declined to R.171 million a year later. They continued to decline in the earlier months of 1961, and reached a level of R.177 million on 14 April 1961 only through the inclusion of drawings amounting to R.18 from the IMF. It was in the light of the present level of the country's foreign exchange reserves that the Ministry of Economic Affairs had recently announced that the policy of caution which had been followed since the end of last year in the issue of import permit allocations was being continued with slight modifications. Details of these modifications were being supplied to the contracting parties (see 1/1454).

8. Members of the Committee thanked the representative of South Africa for his clear and informative statement. The Committee then discussed with the South African representative various questions relating to the prospects for the country's principal exports, the expected level of imports, the trend in capital movements, and the general prospects for South Africa's balance of payments.

9. With regard to exports, a member of the Committee noted the decline in wool exports in 1960 and enquired about the future outlook. The representative of South Africa thought that recovery in export earnings from wool could be expected; the latest wool sales, in March this year, seemed to indicate a tendency of firming prices. As regards gold, which was the principal export of the Union, a member of the Committee observed that production and export of this commodity had been continuously rising since 1958 and enquired whether
this trend could be projected into the future. The South African representative replied that the rise in gold exports in the last few years had been due to increases in the volume of production, the price of gold being pegged with little likelihood of its being adjusted in the light of rising production costs. Expansion in production had been increasingly reliant upon deeper mining and further expansion has become technically more difficult.

10. As regards imports, some members of the Committee noted that there had been a substantial fall in total imports in 1959, which followed the tightening of restrictions in 1959. The representative of South Africa pointed out that the decline in imports in 1959 was due to factors other than the import restrictions as was evidenced by the large amount of unused import-permit allocations totalling £SA39.5 million in 1959 compared to £SA12.9 million in 1958. Referring to the statement by the South African representative that the increase in imports in 1960 might be partly attributed to the replenishment of depleted inventories and speculative over-importation, a member of the Committee considered that these might be a favourable factor in that they must have reduced the demand for imports in subsequent months. The representative of South Africa replied that so far there had been no discernible signs of a decline in imports; the returns for the first two months of 1961 had already exceeded those in the corresponding period in 1960. A member of the Committee commented that the best way of avoiding speculative importation would be the dismantling of all restrictions. It was suggested by another member that the recent decline in net capital in-flow might be accompanied by a corresponding decline in the imports of capital equipment and other investment goods. The South African representative stated that despite the net out-flow of capital in the past year and in the early months of 1961, there had been no falling off in the demand for capital goods; imports of such products were, in fact, higher in 1960 than in previous years.

11. Members of the Committee noted that the present balance-of-payments difficulties of South Africa and the decline in its gold and foreign exchange reserves was mainly due to a net out-flow of private capital since, even with the worsened trade balance, there remained a net current account surplus of R.30 million in 1960. Invited to comment on the prospects for a reversal of this situation, the representative of South Africa considered that the out-flow of private capital had reached a high point where it could be expected to stabilize and gradually to revert to the traditional net inflow. In any case, the net loss of reserves on capital account could not continue indefinitely. Some members of the Committee expressed the view that since the deterioration in the balance of payments was entirely due to private capital movements, South Africa should perhaps explore the possibility of redressing the situation through measures which were directly related to capital transactions rather than through the restriction of imports. The
South African representative stated that the recent net out-flow of private capital was regarded as a transient short-term problem, that the traditional policy of his Government was always to welcome foreign capital and that it would be detrimental to the country's position as a sound market for investment if any attempt were made to curb the free flow of foreign capital into or out of the country. Whether the decline in reserves was caused by capital movements or by unfavourable trends on current account, the Union of South Africa considered that the appropriate course to follow at present was to continue its cautious policy in maintaining the import restrictions. In this connexion the representative of the International Monetary Fund observed that discussions of measures directly affecting capital movements would be more suitably pursued in some other forum than meetings of the CONTRACTING PARTIES.

12. Members of the Committee commented that, considering that the Union's export prospects remained favourable, that gold production might continue to rise or at least maintain its present level, that the high level of imports in 1960 had been partly due to transient factors, and that the out-flow of private capital would not go on indefinitely but would eventually revert to a net in-flow, the South African Government should have greater confidence in its future balance-of-payments situation and should be in a position to exercise more restraint in the use of import restrictions. The representative of South Africa stated that it was the avowed policy of his Government to avoid the use of import restrictions as much as possible; for its experience had shown that such restrictions, while necessary for short-term financial reasons, had almost inevitably created readjustment problems for domestic industries which might take a long time to resolve. For several years consistent efforts had been made to create a situation in which the import restrictions could be finally removed and, by the early months of 1960, the expectation had been that the final step could be taken shortly. This expectation had, however, been upset by the unforeseen change in capital movements.

13. The South African representative stressed that in spite of the recent slight tightening of restrictions, contracting parties could remain confident that the Union of South Africa would not hesitate to remove all restrictions once it felt certain that such a step could be taken without the risk of having to take retrogressive action. Members of the Committee expressed the hope that when that opportunity presented itself the South African Government would not hesitate to take the decisive step of removing all the remaining restrictions.

**Alternative Measures to Restore Equilibrium**

14. The Committee noted the various measures in the fiscal and monetary field which, as described in the documents of the International Monetary
Fund, had been taken in recent years by the South African Government. Members of the Committee expressed gratification at these sound financial policies being pursued and expressed the hope that these would be continued where necessary. The representative of South Africa recalled that the last Budget again included a number of measures designed to encourage the expansion of local industries which were found to be economical. Two years ago the Board of Trade had instituted investigations on products which were being imported into the Union in substantial quantities with a view to ascertaining which of them could be produced locally on an economical basis. The report of the Board on textiles had been submitted recently and its reports on other products were being prepared. Efforts in this field were aimed at solving the Union's balance-of-payments problems on a lasting basis.

System and Methods of the Restrictions

15. The Committee discussed the system and methods of restrictions of South Africa on the basis of the GATT and IMF documents before the Committee. The representative of South Africa informed the Committee that subsequent to the preparation of the GATT "basic document", new decisions had been taken regarding import licensing in 1961. These decisions, taken on 17 April 1961, included the following:

(i) A supplementary allocation of 10 per cent for Group B goods (consumer goods, with domestically available supplies, referred to in paragraph 14(i) of the "basic document"), thus bringing the allocations so far made up to 60 per cent of individual importers' quotas for 1960.

(ii) A supplementary allocation of 25 per cent for Group A goods (other goods on the quota list, referred to in paragraph 14(ii) of the "basic document") thus bringing the allocations so far made up to 75 per cent of individual importers' quotas for 1960.

(iii) For raw materials and capital equipment, additional issues of permits henceforth to be made in the light of actual requirements and existing stocks.

These decisions had been taken in view of the further decline in reserves and in continuation of the policy of caution indicated by the Government in November 1961. Additional allocations would, however, be considered later in the year if the level of reserves made this practicable (see L/1454).

16. The South African representative added that these measures were expected to produce a saving on imports of about R.80 million, equivalent to approximately 7 per cent of the country's total imports in 1960. The
reduction in imports fell on the various categories of imports as follows:

<table>
<thead>
<tr>
<th>Category</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group B consumer goods</td>
<td>R.30 million</td>
</tr>
<tr>
<td>Group A goods</td>
<td>10</td>
</tr>
<tr>
<td>Raw materials</td>
<td>20</td>
</tr>
<tr>
<td>Motor vehicles</td>
<td>20</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>R.80 million</strong></td>
</tr>
</tbody>
</table>

17. Members of the Committee, noting that the reduction in motor vehicle imports had been achieved through the suspension of the system of replacement licensing to meet full requirements, requested information on the new method of restrictions used. The South African representative explained that, having found various disadvantages in the previous system under which passenger vehicle imports were licensed on the basis of monthly retail sales, the Government introduced a new system at the beginning of 1961 under which each importer was assigned a quantity for stocks and given quotas to meet six months' requirements estimated on the basis of sales in a previous representative period. The stocks allowed to all importers being equal, importers already holding large inventories were thus given less licences. This transitional adjustment in stocks had resulted in a reduction in total allocations for the year. This reduction met the incidental need for economy in view of the balance-of-payments situation, but it is not intended that this restriction would be repeated next year.

18. The Committee noted that according to the "basic document" raw materials and capital equipment (specified in Annex B to that document) previously licensed on a replacement basis without effective restriction had, from the beginning of 1961, been made subject to quota restriction, and that according to the policy statement of the Minister of Economic Affairs on 17 April 1961, additional import permits for raw materials and capital equipment would be made in the light of actual requirements and existing stocks. The South African representative agreed that both these steps represented an administrative tightening of the controls. The recent deterioration in the balance-of-payments position of South Africa warranted an intensification of restrictions and, mainly owing to a desire to avoid the use of quotas, the Government had decided to rely on a more strict interpretation of the regulations in order to achieve a slight saving in import payment. Although the issue of such licences henceforth would be influenced to a greater extent by considerations of existing stocks and the availability of local supplies, there was no intention to use the discretionary power severely to interfere with the normal flow of such imports or to afford additional protection to domestic industries. The saving in foreign exchange to be achieved through this action would amount to no more than 6 per cent of the total imports in this category. Some members of the Committee commented that, while the need for South Africa at present to reduce imports was undeniable, the transmutation of a control system known to be purely pro forma to one with distinctive restriction features was somewhat regrettable. The question was also raised as to what
would be the means for arbitration if there should be a difference of opinion between the licensing authorities and importers as to whether the conditions of local supply and stocks were or were not fulfilled in any particular case. The representative of South Africa assured the Committee that the controls and restrictions in South Africa were administered in the most flexible and liberal manner possible. The administrative action in question was considered to be a more liberal substitute for straight quota restrictions, and in no way detracted from the Government's general policy of progressing as far and as rapidly as possible towards the full liberalization of imports.

19. In answer to questions, the representative of South Africa stated that as noted in the report on the last consultation in L/1191, the agricultural marketing boards dealt with only a very limited range of products, which constituted a very small proportion of total imports, the most important item being wheat, imports of which in 1960 amounted to £SA 4 only.

20. A member of the Committee urged that South Africa consider the possibility of using the so-called "negative list" method of restrictions; with the greatly diminished scope of import restriction, it would be desirable from the point of view of traders if the control dealt only with a list of specified products.

Effects of the Restrictions

21. The Committee noted that the general policy of South Africa was manifestly to avoid the use of import restrictions for protective purposes. However, the restrictions applied for balance-of-payments purposes, as the South African authorities were clearly aware, did in many cases have an incidental protective effect creating subsequent problems of readjustment. Some members expressed concern at the fact that in certain sectors the method and administration of the restrictions seemed to be linked closely to considerations of domestic supply and industries. The representative of South Africa assured the Committee that his Government was fully aware of the dangers of protection being afforded to uneconomic industries. South Africa being primarily an exporter of agricultural and mining products, including gold whose price was fixed, the country clearly could not afford to have a cost structure based on protected, inefficient industries. Local supply and production was taken into account in allocating exchange resources for imports, predominantly because priority must be given to essential requirements of raw materials and capital equipment.
General

22. Members of the Committee noted that South Africa's current account remained favourable and that the recent decline in reserves was entirely due to the net out-flow of private capital. As regards imports, exports and other current account transactions there appeared to be no cause for concern. In as much as the out-flow of capital could not continue indefinitely there was every reason to believe that the reserves would recover in the near future. They expressed the hope that the South African Government would take advantage of any significant improvement in the monetary reserves to resume the policy of gradually removing import restrictions in which considerable progress had been made up to 1959. Members of the Committee also expressed satisfaction that the South African Government was fully aware of the importance of giving the closest possible attention to the avoidance of incidental protection being afforded domestic uneconomic industries by the import restrictions.

23. The representative of South Africa said that he had taken note of all the views expressed at the consultation and would convey them to the attention of his Government.

Annexes

I. Opening statement by the representative of South Africa.

II. IMF Board decision of 28 December 1961 (as in Spec(61)93).