1. The Committee has conducted the 1965 consultation with the Republic of South Africa under the provisions of paragraph 4(b) of Article XII. The Committee had before it (a) a basic document prepared by the South African authorities (BOP/46), and (b) documentation provided by the International Monetary Fund, as noted in paragraph 3 below.

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 completed on 10 May 1965. The present report summarizes the main points of discussion during the consultation.

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 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 and background material from the last consultation with the Republic of South Africa under Article XIV of the Fund Agreement.

"With respect to Part I of the Plan for Consultations, relating to balance of payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, the Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of May 5, 1965 taken at the conclusion of its recent consultation with the Republic of South Africa and particularly to paragraph 4 which reads as follows:
'Restrictions on imports were further relaxed in 1964 and there was some simplification of the restrictive system. The Fund welcomes these relaxations and urges the South African authorities to continue working toward the removal of the remaining restrictions, maintained for balance of payments reasons and to rely on internal financial policies.'

"With respect to Part II of the Plan for Consultations, relating to alternative measures to restore equilibrium, the Fund draws attention to the decision taken at the conclusion of its recent Article XIV consultation with South Africa and has no additional measures to suggest at this time."

**Opening statement by the representative of the Republic of South Africa**

In his opening statement, the full text of which is annexed to this report, the representative of South Africa reviewed developments in South Africa's balance of payments situation and in the economy in general. As predicted last year, foreign exchange reserves had declined appreciably and this decline is still in progress; reserves at the end of March 1965 were only about R442 million compared with the peak of R583 million reached in January 1964. The domestic economy continued to be buoyant and for the third successive year the real gross national product showed an increase of some 7 per cent per year. Investment continued high, especially in the private sector, and there was a substantial rise in consumer expenditures, including the sale of automobiles. Wholesale and consumer price indexes had moved upward 3-5 per cent, mainly in the second half of the year, largely as a result of rising food prices attributed to unfavourable weather conditions in certain agricultural regions. The increase in imports, which had helped to keep prices stable, was 23 per cent as compared with 1963, a figure considerably greater than the increase in gross national product. Exports increased less and net invisible expenditure increased so that there was a deficit on current account amounting to R78 million. To cope with these developments, South Africa was not at this stage tightening import controls; in fact additional products had been freed from control. Instead various internal measures had been adopted: an increase in the bank rate from 3.5 per cent early in 1964 by stages
to a present 5 per cent, increases in the ratio of liquid assets required to be held by commercial banks, tighter regulations by the Central Bank for extension of credit and other measures to restrain credit expansion. It was hoped in this way to slow down consumer buying with favourable effects on reserves, without a change in import policy.

**Balance of payments prospects and plan**

4. Members of the Committee thanked the representative of South Africa for his clear description of the development of the South African economy in 1964 and welcomed the steps taken in the further relaxation of restrictions. It was recalled that South Africa's present payments difficulties had been caused in 1960 mainly by an acute outflow of capital in 1960, which had reduced foreign exchange reserves to a low level. The situation seemed now to be evolving toward pressure on resources for implementation of development; shortages of manpower and of capital were developing, consumer demand was booming and as a result there was pressure on prices which seemed to be the major current symptom of disequilibrium. Reference was also made to the IMF decision in which South Africa was urged to continue working toward the removal of remaining import restrictions and to rely on internal financial policies. The question was raised whether it was not time for South Africa to take advantage of the moderating influence of unrestricted imports to help control price movements and whether South Africa might not better use fiscal and monetary measures to protect the balance of payments. Specifically, it was asked whether the measures now invoked by South Africa to relax import restrictions and to dampen inflation were part of a conscious and deliberate policy to build up reserves and to dismantle the restrictive import system. If so, what timetable was envisaged for accomplishing this purpose.

5. The representative of South Africa, in his replies, stressed the point that the total gold and foreign exchange reserves of his country had undergone a substantial decline during 1964 and that this downward trend, which had been beginning at the time of the last consultation, was even now continuing week by week. Total reserves had now dropped to some R390 million, or below the safe minimum for a relatively new country which pays for its imports on a current cash
basis; in fact reserves would now cover only about two and a half months total commitments. Notwithstanding this deterioration in its reserves of foreign exchange, the South African authorities had not taken any steps to intensify control on imports. Imports had increased during 1963 by 24 per cent over the preceding year, and during 1964 had shown a further increase of 23 per cent over 1965. It was acknowledged that the rise in imports had had a moderating and stabilizing effect on the country's price structure. The planned attack on this existing booming consumer demand had been by monetary and fiscal policies and if these were effective, as it was expected they would be, there would be a dampening down of demand with a consequent falling off in imports which in turn would allow the present unsatisfactory reserve position to correct itself. In conformity with this policy, and using monetary and fiscal policies to correct the position, the South African Minister of Economic Affairs had announced on 23 April 1965 that the 1964 level of import permits for the second 1965 issue would be maintained with only one modification designed to use up imported stocks of medium and low-quality poplin.

The representative of South Africa stressed that the announcement indicated the degree of reliance placed by the authorities on the new monetary and fiscal policies. The tightening of import control would only take place if these policies did not become effective and if time did not allow alternative measures to be introduced as it would not be in the interest of either South Africa or its trading partners to allow the reserves to run down to a very low level. The representative of South Africa pointed to the progressive steps which had been taken since 1961 to relax import control and again stated that once the reserves had reached a satisfactory level import control would be abandoned. In the past it had been found in practice that when the reserves were in the vicinity of six months total commitments, no balance of payments difficulties were encountered.
As for a timetable, plans had been made in 1959 and in 1963, but events made it impossible to move in accordance with such plans. One factor which made planning unusually difficult in South Africa was, for example, the uncertain weather which caused a great variation in the size of food crops and in the availability of staple agricultural exports. South Africa normally exports maize, wool and sugar and is self-sufficient in dairy products. But recently drought conditions had adversely affected these exports and had even led to a necessity to import certain foods. The resulting higher prices of agricultural products have in fact gone a long way to account for rises in price levels; such inflation as exists comes not from an increase in the amount of purchasing power available but from crop failures and shortage of skilled labour. It was pointed out that South Africa, traditionally a cheap money country, had increased its bank rate from 3 to 5 per cent and that banks now required to maintain higher liquidity than was theretofore the case; these measures are designed to make money and near money both more expensive and more difficult to obtain.

6. Referring back to the original capital outflow which had characterized South Africa's crisis in 1960, it was noted by members of the Committee that while South Africa's reserves are indeed deteriorating, this weakness does not appear to stem from the private capital account, which improved from a net outflow of the order of R85 million in the first half of 1964 to a net inflow of some R22 million in the second half of the year. This seemed to point to the fact that the decline in South Africa's gold and foreign exchange reserves, which amounted to some R51 million in the latter half of 1964, stemmed from the deficit on current account, which had resulted from import relaxations. In the view of some members of the Committee this simply pointed to demand inflation as the source of the trouble and for that purpose South Africa should adopt additional monetary and fiscal measures while moving further toward liberalization, as a guarantee against rising prices, and as a means of furthering competitive efficiency. The representative of South Africa pointed out however that on capital account in 1964 there was a net outflow of R51 million.
Alternative measures to restore equilibrium

7. Members of the Committee inquired what internal measures were being taken to curb consumer demand; specifically, they inquired what was being done about Government spending and whether, on balance, it was felt that the overall cash government budget would reduce, maintain or add to the amount of purchasing power in the economy. In particular, they asked whether the operation of the Loan Account was regarded as consistent with the Revenue Account, since the former might have an expansionary effect which offsets, or more than offsets, the contracting which might be effected through the Revenue Account.

8. The representative of South Africa agreed that something like a consumer spending was perhaps excessive and said the Government was well aware of the dangers involved. The volume of commercial bank discounts, loans and advances, had, for example, increased by 40 per cent in 1964. He stated that his Government had hoped that planned government expenditures on investment would be offset by stiffer current levies. He stated that the fiscal policies adopted included (i) a compulsory savings levy on certain tax payers, and (ii) a 5 per cent additional tax on company profits. He stated that the problem was a complex one in that the farming community was not as prosperous (because of drought conditions) as the business community, and legislation of this nature could not discriminate but was of general application.

System and methods of restriction

9. Members of the Committee expressed concern that the maintenance of import restrictions by South Africa might, while permitting the expansion of trade, distort the pattern of trade which would prevail if import restrictions could be removed; in particular they felt that there was danger that protection might be accorded to industries which were not viable in the long run. The representative of South Africa stated the principal aim of economic policy in South Africa is the achievement of the maximum rate of growth consistent with financial stability. There is some tendency to make the economy self-sufficient but such a policy is not pursued irrespective of cost, and the Government in general encourages only those industries
which give promise of developing efficiency. Moreover, the way in which import control works in practice allows for the importation of all types of goods even those on the restricted list of imports so that all goods manufactured in South Africa were subject to competition from similar imported goods. The importer himself was free to decide which goods should be imported and from which countries. He felt the fact that only some two-thirds of exporters of consumer goods did not bother to apply for their 1964 third round allocation of permits indicated there was no great feeling of frustration among importers themselves, and indicated also the high rate of permit issues granted for 1964.

10. Members of the Committee also expressed their view that, notwithstanding progress towards simplification of the import system, much of the complexity remained and surely operated as a disincentive to importation out of all proportion to any benefit to South Africa. The representative of South Africa drew attention to the favourable comment of the Executive Board of the International Monetary Fund on recent simplification of the system. He explained that there really are only three basic categories of goods for import licensing purposes: (1) those which may be imported without an import permit constituting about 31 per cent of South Africa's 1964 imports (this category was expanded for 1965); (2) those which may be imported under permit but for which annual quotas are granted to individual importers, making up about 64 per cent of South Africa's 1964 imports, including motor-vehicle components; and finally (3) those goods imported under permit but governed by specific quotas to individual importers, make up some 5 per cent of imports. These three categories together cover the entire range of commodity classification. Within certain commodity groups falling in the second and third categories there are particular goods which must be specifically described in the import permit in order to be imported, and this is the fourth licensing category described in BOP/46. Import permits are issued not on a commodity basis but in general terms and an importer requiring a specific import permit converts his normal issue on the basis of R2 of the general permit for every R1 specific import permit required, provided however, that in respect of the first R5,000 of an
importers general allocation, there was no loss in the face value of the permit. It was confirmed that even if goods were included in the restricted list of imports, any such goods which were imported under rebate of the general customs duty were automatically exempted from the restrictions of the list.

In response to a question, the representative of South Africa stated that the original basis of granting import allocations had been based on the value of 1948 imports by that firm. This in the course of time had been changed and import facilities were now calculated in the case of merchants on the volume of business done allied to the type of business. Individual importing firms received their allocations on this basis. The scheme did not therefore provide for the division of a block allocation by a trade organization to the individual members. Individual firms all receive their allocations direct from the Directorate of Imports and Exports.

The representative of South Africa stated that automobile imports consist of three categories, namely (i) those imported built-up, (ii) those cars which are assembled in South Africa and which did not aspire to group (iii), and (iii) those with a South African content by weight of 45 per cent rising to 55 per cent within three and a half years of the date the car was proclaimed a South African manufactured model. Importers were free to make their own decisions regarding the categories in which they fall. Category (ii) received more liberal treatment than Category (i) while Category (iii) had been freed from import control. The percentages of the market were Group (i) approximately 1 per cent, Group (ii) approximately 20 per cent and Group (iii) approximately 80 per cent. The representative of South Africa confirmed that apples are accorded token licences, to maintain traditional trade ties. Concerning the tyres mentioned, he stated that South Africa's manufacturing capacity for tyres exceeds present needs, as some countries for example, Rhodesia, to which South Africa formerly exported tyres, now make their own. Hence tyre imports are considered unessential.
12. A question was also asked concerning the extent to which South Africa has carried out the undertaking which the South African delegate had given in 1960 to the GATT Working Party on the Trade Agreement with the Federation of Rhodesia in which he had said that his Government was prepared to eliminate the preference given to products of the Federation through a general liberalization of South Africa's restrictions giving priority to products for which preferential treatment was meaningful to the trade of the Federation (L/1225, page 3, paragraph 6). The representative of South Africa stressed that Rhodesia's share in South Africa's imports is very small, being only 1.4 per cent of total in 1964. Also, some commodities included in the total were of sorts that would not in all likelihood be imported at all if they had to be brought from a great distance. It was also emphasized that the trade agreement with Rhodesia itself has built-in limits on the amounts of some commodities which South Africa will import duty free, or at preferential rates, even though Rhodesian goods are not subject to quantitative restriction under the general system; leaf tobacco and some items in the group which includes clothing textiles are examples of products subject to tariff quota.

Effects of the restrictions

Members of the Committee reverted to their concern that the restrictions may be serving mainly purposes other than those for which they were originally intended. This protective effect extends in some cases to goods of a kind not made in South Africa, merely because the imports are competitive with locally manufactured goods. The representative of South Africa recalled that the purpose of the restrictions is to save scarce foreign exchange and said that it was his Government's view that if, for example, heaters designed for use with electricity or propane were available from local sources, there was no need to admit heaters designed for use with other fuels, but provision existed for such heaters to be imported on the basis of the two-for-one exchange of foreign-exchange allocation, which remained as a guarantee against excessive local prices.
On the general question of the effect of the licensing system on the quantity of imports, the representative of South Africa also noted that the practice of announcing foreign-exchange allocations ahead of time helped importers to maintain a flow of supplies. So for example, the first 1965 allocation had been announced in November when a second was promised for April, and this had just now been made. Also he stressed, South Africa had never revoked an allocation once made and is proud of this record.

General

Members of the Committee urged South Africa to continue to work towards liberalization and felt that a definite time-table would be helpful in assuring that this objective was clearly kept in mind and would be achieved promptly. As a first step, South Africa was urged to return to the free list all items removed from it since 1961. High priority should be given to complete removal of the "fourth" or specific permit system and progress increase of quotas on general merchandise should be assured.

Goods not made in South Africa should not be restricted on the ground that they compete with local products. Also, in spite of simplification achieved, it was felt that the system was still too complex. The fact that importers had not fully utilized allocations late in 1964 could indicate that there were many goods, especially in the first licensing category, and including raw materials and capital equipment, which could well be freed entirely from any licensing requirement. If South Africa feels that any control must continue, certainly it is high time to establish a time-table for removal of the restrictions as a guarantee that the system established to deal with a temporary difficulty does not perpetuate itself for other purposes.

The representative of South Africa repeated the assurance given at previous consultations that as and when conditions allowed further steps would be taken to relax further the present restrictions. The restrictions were, however, maintained in the present circumstances in the interests not only of South Africa but also, of its trading partners and it was still very necessary to proceed with caution.