national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

The International Monetary Fund (IMF) has given the South African economy the thumbs up in its 2006 Article IV Staff report, inspite of global volatility. The report, released today, is conducted annually for each of the Fund's member countries. South Africa was assessed on its macroeconomic situation, including developments in the monetary, fiscal and financial sectors of the economy. Article IV consultations are conducted annually for each of the Fund's member countries.

Growth is projected at 4.2 percent for 2006 and 4 percent for 2007. The major risks to the forecast are external – a disorderly adjustment of global imbalances, price of oil, falling commodity prices, and a continuation of a slowdown in capital flows to emerging markets. On the domestic front, the widening current account deficit is raised as a concern by the Report. The Report does mention, however, that SA's good fundamentals would mitigate the impact of any adverse external shocks on the economy.

The Report contains some analysis of the sharp depreciation of the rand experienced in May/June this year. Four factors are mentioned as contributing to the depreciation, namely, the current account deficit, the drop in price of some of SA's key export commodities, a slowing down of portfolio flows to emerging markets, and the liquidity of the rand. With regard to this last factor, it is mentioned that when there is capital flight away from emerging markets, investors tend to sell the rand short to cover their exposure to other less liquid, emerging market currencies.

The IMF is broadly supportive of the financial policies of the South African Government. However, the Report makes a number of suggestions for further improving our policies, including:

Targeting the mid-point of the inflation band: The IMF praises SA's inflation targeting framework, but suggests that the mid-point of the band should be explicitly targeted, in order to further anchor inflation expectations.

Relaxing labour market legislation: The IMF reiterates its long-held view that South Africa's labour regulations are too restrictive and discourage job creation. The Fund singles out centralised collective bargaining and dismissal procedures for criticism, and also notes that there should be more consideration for the impact of labour regulations on small and medium enterprises (SMEs).

The IMF is supportive of ASGISA. However, the IMF staff do not agree that the level and volatility of the exchange rate is a constraint on South Africa's growth, stating that there is "no compelling evidence" to this effect.

The IMF regards South Africa’s financial sector as sound and well-capitalised. The Report does not view current levels of household indebtedness as posing a threat to financial stability, but points out that they could have wider macroeconomic implications, especially in the current environment of rising interest rates.

The Report contains some discussion of regional spillovers – areas where South Africa’s policies might impact on our neighbours. Two areas in particular were highlighted – the effect of further trade liberalisation (which the IMF supports) on SACU revenue and the stability and regulatory implications of the presence of South Africa’s financial conglomerates in the region.

The South African Government welcomes the report. We do not believe the concerns would undermine the current strong economic growth trajectory, which is underpinned by strong economic fundamentals and prudent macroeconomic policies

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