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REPUBLIC OF SOUTH AFRICA

SOUTH AFRICA RELEASES THE 2009 INTERNATIONAL MONETARY FUND ARTICLE IV STAFF REPORT

The International Monetary Fund (IMF) today released its 2009 Article IV Staff Report. This report is an annual assessment of South Africa's macroeconomic situation, including developments in the monetary, fiscal and financial sectors of the economy. The report was positively received by the IMF's Executive Board at its meeting of 5 August 2009, as noted in its Public Information Notice, which was also released today.

The Staff Report and the response of the IMF Board are broadly supportive of the fiscal, monetary and financial policies of the South African government. They note that the country's economy is weathering the effects of the financial crisis relatively well. The Report ascribes this to government's sound macroeconomic policies, underpinned by consistent and transparent policy frameworks, the floating exchange rate regime, and a well-supervised financial system. This, the Report notes, contributed to South Africa's strong economic growth, averaging 5 percent between 2004 and 2007, as well as to its single-digit inflation, steady employment growth, strengthened public finances and an improved external reserve position.

IMF forecasts

The Article IV Report projects a contraction in gross domestic product (GDP) of 2.1 percent in 2009 as a whole. This is slightly more pessimistic than the Reuters July consensus of a 1.9 percent contraction.

The IMF Report also projects that the current account deficit will narrow to 6 percent of GDP in 2009, before widening to 7-7½ percent of GDP over the medium term. The IMF view is that the deficit is manageable at this stage. In should also be noted that about half of the deficit is rand-denominated, substantially reducing South Africa's external vulnerability.

The IMF supports the current policy of the South African Reserve Bank and National Treasury to build up reserves when market conditions are favourable. The IMF also supports South Africa's flexible, floating exchange rate system, and shares the view that this system provides an important buffer against external risks. It notes that the rand is a volatile currency, reflecting the relatively high proportion of offshore trading. As such intervening to manage the currency would be counterproductive.

Global financial crisis

Last year, the IMF Report made a number of recommendations based on its Financial Sector Assessment Programme (FSAP) update, where it concluded that "South Africa's financial system is fundamentally sound". The reports for both last year and this year recommend consolidated supervision of financial conglomerates, imposing fit and proper requirements on pension fund trustees, and improving monitoring and early warning analysis of risks and emergency measures.

The Report observes that South Africa's money markets remained orderly and financial institutions stable when the financial crisis intensified in late 2008. It also notes that the financial system has shown remarkable resilience through the current global financial crisis. The healthy profitability, limited exposure to foreign assets and funding, and low leverage of South African banks allowed them to remain solvent with no need for extraordinary liquidity or state support.

The Report's overall assessment is that banks' insolvency risks are small due to strong capital positions and generally high profitability. It notes that the banking sector is sound, and that corporate and financial sector balance sheet exposures to exchange rate and interest rate shocks are limited. However, while the system is stable, banks are feeling the impact of the declining economic activity and rising unemployment.

The report also points out some downside risks to the economy as a result of the global economic decline, like reduced trade flows, further financial market turbulence, and deteriorating loan quality of banks.

View of the South African government

The South African government welcomes the generally positive report. However, government does not share all the views expressed in the report, particularly recommendations relating to trade, industrial policy and the labour market. With regard to labour market issues, it should be noted that there are some differences between the IMF, the Organisation for Economic Cooperation and Development (OECD) and the International Labour Organisation (ILO) on the labour market policy in South Africa.

The government will consider the recommendations made. There will be further discussions within government and with the IMF on the content of the report. Such discussion will also take into account various inputs on growth and development by the World Bank, OECD, ILO and various academic and research institutions.

Government has published two policy discussion papers on national strategic planning and performance, monitoring and evaluation. The implementation of these policies should assist in improving the quality of public services and this is in line with the recommendations of the report.

South African currently has a policy that encourages the private sector to invest in public infrastructure, including through the Public Private Partnerships arrangement (PPPs). Government will explore why take-up in PPPs has been lower than desired, while acknowledging the need to expand public infrastructure.

Government also initiated a process with financial regulators to give effect to the recommendations of the IMF, the Financial Stability Board and the G20 meetings. These include measures to strengthen consolidated supervision of financial conglomerates.

Government notes that the Report has recognised mitigating factors with regard to the current account deficit, including a relatively large portion of it being comprised of rand denominated factors. Government has also acknowledged the need for a pragmatic and disciplined fiscal policy, including a limit of 50 percent for debt to GDP, to alleviate risks to the medium-term fiscal position.

Government will update its macroeconomic forecasts in October 2009 when the Minister of Finance tables the Medium Term Budget Policy statement.

A copy of the full report is available on the International Monetary Fund website (www.imf.org) and on the National Treasury website (www.treasury.gov.za)

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