PRESS RELEASE

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IMF Staff Completes Staff Visit to South Africa

FOR IMMEDIATE RELEASE

End-of-Mission press releases include statements of IMF staff teams that convey preliminary findings after a visit to a country. The views expressed in this statement are those of the IMF staff and do not necessarily represent the views of the IMF's Executive Board.

- *The economy's recovery from the pandemic should continue this year as lagging sectors (tourism, hospitality, and construction) gradually catch up. Mitigating the impact from COVID-19 and recent floods and preserving well-targeted social outlays are key priorities.*
- *South Africa needs to urgently remove obstacles to private investment and encourage competition to reignite economic growth in the medium term. Eskom and Transnet should transform their business models to contribute to the sustainability of the public finances.*
- *A continuation of the monetary-policy tightening, timely initiated by the South African Reserve Bank (SARB), is indispensable to keep inflation expectations anchored.*
- *Reining in unproductive fiscal spending and using the bulk of the temporary revenues to reduce borrowing needs are key steps to put the debt-to-GDP ratio on a declining path and boost confidence. Strengthening governance will help to ensure durable and inclusive growth.*

Washington, DC – June 7, 2022: A staff team from the International Monetary Fund (IMF), led by Ana Lucía Coronel, met with the South African economic authorities and several other counterparts during May 26–June 6, 2022, to discuss recent developments and the economic outlook in the context of its regular surveillance cycle. At the end of the visit, Ms. Coronel issued the following statement:

"As South Africa's economy emerges from the pandemic-induced contraction, it is benefiting from favorable commodity prices, which have raised exports and government revenue. However, a series of shocks is adversely affecting its outlook. The flooding in Durban, uncertainty about the war in Ukraine, tightening of global financial conditions, and China's slowdown pose challenges to growth and price stability. Policy action needs to focus on mitigating the impact of these shocks while addressing longstanding structural economic obstacles to growth. Frequent load shedding is an impediment to conducting business in South Africa. Similarly, failures in the transportation system limit the gains from the commodity price boom. Rising inflation hurts the purchasing power of low-income households and negatively affects the country's competitiveness and financing costs.

"While the IMF staff team expects medium-term inflation to remain near the mid-point of the targeted range, thanks to the SARB's vigilant monetary policy, Fund staff is increasingly concerned about the growth outlook and its implications on employment, poverty, and inequality. The team reaffirmed its finding that low growth in the last decade has been caused by binding structural constraints, rendering demand-side policies (whether fiscal or monetary) less effective in boosting economic activity. Despite some important progress in addressing the scarring effects of state capture on governance and institutions, sustained efforts are needed to improve procurement processes and deter corruption. It is more urgent than ever to transform the network industries and foster competition to attract private investment, create jobs, and reverse the slide in social conditions.

“The recent conclusion of the digital spectrum auction, and the changes in the licensing of generation capacity in the energy sector are welcome. These actions need to be complemented by broad-based removal of regulatory barriers to investment and competition, while resisting detrimental protectionist policies. There remains a large gap between encouraging policy statements and reform implementation, which undermines the confidence and growth impact of those statements. Improving the functioning of the labor market and the quality of education are also essential to tackle South Africa’s high structural unemployment.

“The operations, finances, and governance of Eskom and Transnet need to be improved decisively and quickly. Any solution to Eskom’s debt problem must be preceded and accompanied by concrete and credible actions to downsize the company’s balance sheet and restore its commercial viability. These include efforts to cut costs and collect arrears, as well as a more predictable tariff-setting mechanism. Otherwise, Eskom will continue relying on government support and remain a constraint to economic growth and a threat to the sustainability of the public finances. Transnet needs to restore the operational capacity of the freight rail system and improve the efficiency of its ports, including by accelerating reforms that attract private sector investment. These reforms will also contribute to the success of the country’s low-carbon transition and its financing.

“A growth-friendly fiscal consolidation is indispensable to restore policy space, put debt on a declining and sustainable path, and increase market confidence. This will require thoughtful streamlining and re-prioritization of unproductive outlays in favor of crucial ones—notably, promoting COVID-19 vaccination, addressing the damage from the floods, and continuing to support the most vulnerable groups. Efforts to contain compensation costs and streamline transfers to SOEs while they advance operational and governance reforms need to be stepped up. The financial condition of some municipalities is causing continued deterioration in service delivery and needs to be remedied. The bulk of the fiscal revenues resulting from the temporary commodity price boom should be used to reduce borrowing requirements, as the gains could easily fade away and would not sustain a permanent increase in expenditure.

“The SARB’s focus should continue to be on inflation expectations and ensuring low and stable inflation, while letting the rand absorb shocks. With the unwinding of temporary regulatory easing, banks’ financial indicators should be closely monitored, particularly in small institutions with vulnerabilities. Urgent actions are needed to address shortcomings identified by the Financial Action Task Force in the areas of anti-money laundering and combating the financing of terrorism, which would strengthen South Africa’s role as a financial hub.

“The IMF staff team would like to thank the authorities and all other counterparts for their warm hospitability and very productive discussions.”