NATIONAL ASSEMBLY

QUESTION FOR ORAL REPLY

QUESTION NUMBER 95

14 MARCH 2007

MR I O DAVIDSON (DA) TO ASK THE MINISTER OF FINANCE;

Whether he will make a statement on the role and relationship between fiscal and monetary policy in providing stimulation to the supply-side of consumption-led economies in emerging markets with high growth and employment needs? ***N444E***

REPLY:

Fiscal and monetary policies have separate mandates. The mandate of the Reserve Bank is price stability, within the inflation target of 3 to 6 per cent. Fiscal policy meanwhile is concerned with providing government with the resources to achieve its social and economic objectives through a sustainable fiscal stance. Both the Treasury and Reserve Bank carry out their mandate in the interest of balanced and sustainable economic growth.

Fiscal and monetary policies are also interdependent, meaning that some level of coordination or consideration of each policy stance is useful in ensuring sustainable macroeconomic outcomes.

Real growth in targeted expenditure in support of government's economic and social objectives, including the strong emphasis on infrastructure development, helps to raise the productive growth rate of the economy. It indirectly supports productivity of factors of production, and thus contributes to lower inflation. For example in the last three years, investments in human capital through education has grown by 10,2 per cent a year, and health expenditure has grown by 13,3 per cent. Investments in a safer society have seen the budget for police grow by 12,8 per cent a year, while justice has grown by 11,5 per cent. These important priorities continue to receive significant increases in their resources from the 2007 Budget.

While non-interest expenditure has grown by over nine per cent in real terms over the past 3 years, inflation has been comfortably within the target range and interest rates are now significantly lower than they have been in many years.

This, combined with a strong fiscal position, has improved government saving significantly. Government is now contributing positively to the effort to bolster economic savings and investment, which serves to enhance the sustainability of the broader macroeconomic environment. Over the medium term government will contribute positively to the country's saving rate. This helps to lower the cost of capital, increase investment, and build the supply side of the economy.

Revenue growth has also remained strong, in line with a rapidly growing economy. This has enabled government to provide tax relief in successive budgets to offset the cost of inflation on the economy and strengthen economic activity when needed. Tax relief has also helped to balance the rise in tax revenues occasioned by changes in tax policy, administration, and the broadening of the tax base. In the 2007 Budget, government provided tax relief primarily to offset inflation and prevent a rise in unit labour costs and inflation.

Significant reductions in the corporate tax rate from 40 per cent in 1994 to 29 per cent will have increased the return to investment and bolstered the supply side of the economy.

While government priorities have continued to receive significant increases in resources in the 2007 Budget, the budget balance has been strengthened significantly. This not only serves to provide fiscal space for the future, but also signals government's commitment to managing the fiscal accounts in a manner that does not undermine the sustainability of the macroeconomic environment by placing undue pressure on inflation, interest rates and the current account deficit.

Alongside declining inflation over the years, Treasury's fiscal management and prudent approach to debt have resulted in increased resources for expenditure as debt service costs have come down. Low debt levels and the reinforcing effect of falling debt service costs on the sustainability of the fiscal position have contributed, with declining inflation, to low interest rates. A reduced cost of capital, in turn, has contributed to increased investment in productive capacity in the economy.

The fiscal stance thus provides support to the supply-side of the economy through growth in infrastructure related allocations, human capital development, improved government savings, and a lower cost of capital. This complements the monetary management of the economy by the South African Reserve Bank, which focuses on maintaining a low rate of inflation. A low and stable rate of inflation helps to maintain the competitiveness of the economy in world markets and contributes to stable growth in gross domestic product.

NATIONAL ASSEMBLY

QUESTION FOR WRITTEN REPLY

QUESTION NUMBER 105

DATE OF PUBLICATION: 9 FEBRUARY 2007

DUE TO PARLIAMENT: 22 FEBRUARY 2007

PRINCE N E ZULU (IFP) TO ASK THE MINISTER OF FINANCE:

(1) Whether inflation targeting has had positive benefits for the country since its inception; if not, why not; if so, what are the relevant details;

(2) whether he will make a statement on the matter? ***N110E***

REPLY:

(1) Inflation targeting has benefited the South African economy in a number of respects. The primary benefit has come from the anchoring of inflation expectations within the target band of 3-6 percent, which has facilitated the lowering of inflation and interest rates. The anchoring of inflation expectations has lessened the burden on monetary policy to use interest rates (monetary tightening) to achieve lower inflation. The nominal repurchase rate has declined from 13.5 percent in 2002 to 9 percent currently. Unit labour costs have also declined in line with inflation.

The combination of lower inflation, lower interest rates and lower unit labour costs has supported the strongest economic growth and job creation in decades, with estimates of over 1 million jobs created since 2001.

A second benefit arising out of this policy is improved domestic competitiveness. By keeping inflation low, sound monetary policy frameworks, such as our own, help keep goods and services exported abroad competitive relative to those of our trading partners. At the same time, credibility of the inflation targeting framework reduces the extent to which the inflationary effects of depreciation of the exchange rate pass through into domestic prices.

Keeping inflation low is also important to maintain the real income of poor households. Poor households are especially vulnerable to inflation, because they are least able to increase their income to offset the erosion of real income caused by high inflation. Over the course of 2006, for instance, poor households have been negatively affected by rising meat and other food prices. Low inflation is critical to maintaining and improving the living standards of our poorest households.

(2) No.

MINISTER OF FINANCE
MG
07 MAR 2007
FILE No: M2/1/1/10/2
MINISTER OF FINANCE
737-07

NATIONAL ASSEMBLY

QUESTION FOR WRITTEN REPLY

QUESTION NUMBER 224

DATE OF PUBLICATION: 23 FEBRUARY 2007

DUE TO PARLIAMENT: 8 MARCH 2007

DR S M VAN DYK (DA) TO ASK THE MINISTER OF FINANCE:

(1) Why, in the light of fiscal discipline, has the economic growth rate been adjusted upwards annually since 2000;

(2) whether incorrect growth estimates by the SA Statistics Service played a role in the successive review of the economic growth rate; if so, what are the relevant details;

(3) why, given the economic growth, is there no corresponding decrease in unemployment;

(4) whether economic growth estimates in the informal sector are factored into the total economic growth figure; if not, why not; if so, what percentage of the calculations does this contribution represent? ***N294E***

REPLY:

(1) Prior to 2000, prudent fiscal policy helped to lower debt service costs and the cost of capital in the economy as a whole, supporting growth across the economy as interest rates declined and freeing additional resources for productive expenditure. After 2000, government budgeted for stronger growth in non-interest expenditure and was able to enact annual reductions in tax rates. Economic growth was supported by allocating funds to key public service uses, increasing the social wage and raising financing of infrastructure priorities. Those broad allocations have helped to raise investment across the economy, supporting a renewal of property and its extension, inducing new investments in plant and machinery, and major infrastructure projects, such as roads. They have also supported growth by focusing on improvements to the skills base, the health care of the population,

and other social determinants of growth. Lower tax rates and rising social grants have helped to underpin growth in household expenditure. Investment and lower supply costs of labour have helped to increase employment, which directly feeds into rising household income.

In the past three years, gross fixed capital formation (investment) recorded the highest growth rate at 10,4 per cent , with household consumption growth recorded at 6,8 per cent and government consumption growth of 5,7 per cent. Investment growth is projected to increase to an annual average 10,9 per cent in this period, whereas export growth could rise to 6,7 per cent. Household consumption growth is expected to moderate to 5,2 per cent and government consumption growth could slow down to 4,6 per cent.

Forecasting economic growth is equal measure art and science. Past trends and economic relationships are statistically measured and extrapolated into the future, with adjustments made for expected changes to policies and key prices and volumes in the economy. So, in broad terms, our adjustments to economic growth reflect a continuous updating of our understanding of the economy and changes in the data itself – sustained upward adjustments reflect a rising potential and realized growth rate of the economy.

At the same time, our growth rates are adjusted in line with GDP data revisions that are undertaken annually in November by Statistics South Africa. These revisions incorporate more complete, detailed and accurate data sources that are not available when quarterly estimates of the national accounts are compiled. Since 2000, the November GDP revisions have on average added 0.6 of a percentage point to the annual GDP growth rate, yet it is still difficult to predict with accuracy changes in GDP that the revisions will cause.

(2) It is not correct to refer to "incorrect growth estimates". The preliminary quarterly GDP estimates are by their nature incomplete in their coverage at the time of release, and are therefore subject to revision. GDP revisions are part of the national accounts processes in most countries.

(3) Since March 2003, the official rate of unemployment has fallen by nearly 6 percentage points to 25.6 per cent and the broad unemployment rate has fallen by nearly 4 percentage points to 39 per cent. Strong and sustained economic growth and macroeconomic stability have contributed to an environment in which firms can operate and expand, helping to bring the unemployment rate down. Moderate real wage growth and rising levels of worker productivity have also assisted employment creation. Inflation targeting has anchored inflation expectations, bringing average wage settlements to 6,5 per cent in December 2006.

Of the 544,000 additional jobs created in the year to March 2006, 309,000 were in the non-agricultural formal sector. At the current rate of employment growth (4,5 per cent), the target of halving unemployment by 2014 will be met, with the majority of these jobs being created in the formal sector.

(4) The total economic growth estimate from Statistics South Africa includes gross value-added from both the formal and informal sectors of the South African economy. According to Stats SA, the informal sector accounts for about 6 per cent of total GDP and is largely concentrated in the construction and tertiary industries. Due to the difficulties in obtaining comprehensive information on informal sector activity and given anecdotal evidence on the strength of informal sector activity, the official estimate probably understates the size of the informal sector.