Board Meeting of March 23, 1999
Statement by Mr. Girmai Abraham

South African Country Assistance Strategy

We welcome the opportunity to comment on and clarify some of the issues presented to the Board today. South Africa is one of the founder-member states of the Bank and that membership encompasses the World Bank Group as a whole. For historical reasons the Bank ceased lending operations in 1967. The Bank’s re-engagement in South Africa began in 1990 culminating in a Memorandum of Understanding that deepened the country’s relationship with the World Bank Group in 1995. The relationship between South Africa and the Bank Group has matured considerably since then.

The South African CAS before you today is the product of extensive consultation between the Government of South African (GOSA) and the International Bank for Reconstruction and Development (IBRD) and aims to address the current reconstruction and development priorities of South Africa. Since 1994, the policies and programmes of the Government have been subject to extensive consultation, publication of discussion documents, White Papers and wide-ranging legislative reforms. The CAS document has already detailed some of these but we would like to emphasise a few. In 1996 the country adopted a macro-economic strategy, namely, the Growth, Employment and Redistribution (GEAR). The GEAR framework sets South Africa’s long term vision for development. Major elements in the strategy include the following:-

• A fast fiscal deficit reduction programme to contain debt service obligations, counter inflation and free resources for investment.
• Budget reform to strengthen the re-distributive thrust of expenditure.
• A reduction in tariffs to contain input prices and facilitate industrial restructuring, compensating partially for exchange rate depreciation.
• An exchange rate policy to keep the real effective rates stable at a competitive level.

The GEAR strategy was rapidly followed by the adoption of a Medium-Term Expenditure Framework (MTEF) in 1998. The MTEF sets out spending plans for three years at the time of the adoption of the budget. This has greatly facilitated democratic accountability and transparency. According to the MTEF process the government envisages to achieve the following objectives:

• Meeting the basic needs of the people;
• Accelerating the basis for sustained economic growth, development and job creation;
• Development of human resources; and,
• Ensuring the safety and security of the citizen and the state.

Job creation remains South Africa’s number one challenge. The Jobs Summit held on 30 October 1998 has focussed on a broad range of policy commitments, which include:

• Sustainable and stable macroeconomic policies;
• Industry policy measures and programmes that will directly address employment and encourage investment;
• New programmes to strengthen further the small, medium and micro enterprise sectors;
• Tourism promotion and enhancement of tourism capacity;
• Enhanced delivery of housing and new initiatives to expand the stock of rental housing;
• Human resource development, support for education and broader access to training; and
• Labour market policies dealing with job security, productivity and employment for youth, women and the disabled.

The South African government accords great importance to regional development. As a member of the Southern Africa Development Community (SADC) South Africa is charged with the responsibility of managing regional health issues, investment and financial integration. In this regard, South Africa has worked with the World Bank and an IDF grant was given to the South African Reserve bank to manage the project on the development of payment, clearing and settlement system in SADC countries. South Africa believes that there is ample scope for co-operation with the Bank Group on regional infrastructure, energy, environment and tourism sectors.
We would like to reflect on South Africa’s macro-economic situation and prospects. Economic prospects for 1999 are expected to be strongly affected by the turbulence in the international financial markets in 1998 as was economic performance in 1998. The reassessment of risk associated with investment in emerging markets caused interest rates in South Africa to move higher, the rand to depreciate and output growth to be decidedly weaker than what it would have been otherwise.

Fiscal policy was the stabilising factor throughout the global financial turmoil and the Central Government’s deficit before borrowing continued to narrow in spite of slack conditions in the economy. Strict controls over expenditure and improved tax collection contributed to the lower deficit, which is set to decline to 3.5 per cent of gross domestic product in the year starting on 1 April 1999. Provincial governments were also successful in turning financial shortfalls in fiscal 1997/98.

Developments regarding inflation have been even more encouraging. Although initially the depreciation of the rand accelerated the increase in the general price level, inflation had already started to abate by the end of 1998. Year-on-year consumer price inflation stayed below 10 percent per annum and started to slow down from December 1998, mainly because of tight monetary and fiscal policies, solid increases in labour productivity, some moderation of wage growth and the partial absorption of production costs by domestic producers.

Fixed investment has risen strongly from its low levels of the early 1990s and is still growing at a robust rate. The deficit on the current account of the balance of payments was well contained, registering a value of about 2 per cent of gross domestic product for 1998 as a whole. On a net basis, the South African economy has not been a major recipient of foreign direct investment capital. However gross flows have been substantial, signifying fuller integration into the global economy.

We therefore would like to emphasise that any impression of undue vulnerability is misplaced. The rand exchange rate depends largely upon current and expected economic policies and developments and the markets’ interpretation of these. This inherent flexibility of the exchange rate acts as an important shock absorber – exchange rate and interest rate adjustments help to restore macro-economic stability by allowing markets to move quickly to new equilibrium levels. Such rate adjustments should be seen as part of the natural reaction to sudden reversals of international capital flows and not as mechanisms for triggering domestic crises.

The sharp rise in interest rates in the second and third quarters of 1998 helped to stabilise the South African financial markets without undue delay. Apart from a brief period in January 1999 when emerging market problems threatened to unsettle domestic financial conditions, the downward trend persisted well
into the first quarter of 1999, thereby preparing the way for an economic recovery that is expected to get under way from by the middle of 1999.

Although the ratio of short-term to total foreign debt seems high, it should be kept in mind that South Africa imports more than R200 billion per annum in goods and services. Trade finance, provided by exporters and other parties who have a strong interest in exporting to South Africa, forms a substantial part of short-term external debt.

Notwithstanding some of the remarkable achievements that the country has recorded in the transformation period, the South African authorities remain cognizant of the many challenges still to be addressed. The CAS underlines some of the problems that need a collaborative approach in handling. The international community including the World Bank Group has been supportive of the authorities’ development program. We thus wish to commend the Bank for its pioneering role as a knowledge bank. The building of human and institutional capacity and the fight against poverty are among the goals that the South African peoples are committed to.

On the social front, the government’s development objectives and policies are clearly spelt out in the budget. South Africa already spends a high portion of its budget on social sector spending. The emphasis is therefore not on further budget allocation to the social sectors but to re-allocation of spending to address efficiency concerns and to improve service delivery. The South African authorities are appreciative of the Bank’s role on environmental issues. The Bank has been able to impart lessons from other parts of the world and to improve the quality of debate on biodiversity management issues. Also important has been the role of the Economic Development Institute (EDI) on capacity building within the government and the civil society. My authorities view further engagement of the EDI as a constructive development.

My authorities have raised with management a number of concerns about the tone of the document and the political analysis given in paragraph 54. It is our understanding that there will be further consultation before the document is made public.

In conclusion, South Africa looks forward to a partnership with the Bank Group in tackling the problems identified in the CAS document. On behalf of my South African authorities, let me express my deep appreciation for the Bank Group for the constructive dialogue and close co-operation in identifying priority areas.