THE RECENT SHIFT OF EMPHASIS IN SHORT-TERM ECONOMIC POLICY IN SOUTH AFRICA*

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Die Minister van Finansies het laat in 1977 'n klemverskuiwing in kort-termyn ekonomiese beleid aangekondig: 'n Geleidelike verskuiwing van die beperking van investering en verbruik, na die stimulasie van gesonde ekonomiese groei. Die grondslag van hierdie klemverskuiwing is die sukses bereik met die beperkende monetêre en fiskale beleid en die verbetering van die betalingsbalans. Aspekte van hierdie belangrike beleidstelling word bespreek. Die merkwaardige swaai van 'n groot betalingsbalanstekort na 'n groot oorskot dien as bewys van die inherente sterkte en aanpasbaarheid van Suid-Afrika se betalingsbalans, tenspyte daarvan dat die balans in die afgelope paar jaar etlike groot skokke moes absorbeer: Die wêreldresessie van 1973–75; die onbestendigheid van die goudprys sedert einde 1974; gebeure in Angola in 1975 en in swart stedelike gebiede in 1976; en voortgesette politieke onsekerheid in, en druk op Suider-Afrika. Die tyd is nou ryp vir 'n nuwe ekonomiese opswaai, onder meer weens 'n styging in uitvoere, voortgesette uitvoervervanging, toename in sekere vorms van staatsbesteding, en die noodsaaklikheid van heropbou van voorrade wat tydens die resessie afgebou is. Daar is steeds 'n tekort aan kapitaalinvloei, wat die regering sal noodsaak om bestendige ekonomiese groei te stimuleer. Dit sal egter versigtig beheer moet word, om te verseker dat die nuwe opswaai nie inflasionêr is nie.

In an important policy speech on 31 August 1977, the Minister of Finance, Senator Owen Horwood, announced a shift of emphasis in short-term economic policy in South Africa. The Minister stated: "I foresee in the months ahead a gradual shift of emphasis in monetary and fiscal policy from the present curbing of investment and consumption to the stimulation of sound economic growth. Such a shift of emphasis will serve as recognition of the success achieved by the restrictive monetary and fiscal policies in improving the underlying balance of payments situation and in creating scope for new expansion."

Some aspects of this important policy announcement will be discussed briefly.

First, a few remarks on the background to this recent policy change. The important point to emphasise here is that, although South Africa is still confronted by serious economic problems, our present economic situation is fundamentally different from that of a year or eighteen months ago. During the first half of 1976 we were still living beyond our income in the sense that we had a substantial current account deficit on the balance of payments and were financing this to a large extent by means of short-term foreign borrowing. Not surprisingly, this resulted in a decline in our net gold and other foreign reserves. At that stage our money supply was still rising much too rapidly, and this was also true of public sector spending in general.

The present position is totally different. Although the capital account of the balance of payments has deteriorated, the deficit on the current account has been transformed into a surplus, and both the public and private sectors have for months now been reducing their foreign indebtedness. In other words, instead of keeping our reserves *up* by short-term foreign borrowing, we have for some time now, in effect, been keeping them *down* by repaying foreign trade credits and other short-term loans. Moreover, during the past year, the money supply has been rising at a greatly reduced rate and most of the main components of gross domestic expenditure have been declining in real terms. In a nutshell, the underlying balance of payments position is now much stronger and the domestic economy much "colder" than a year ago.

The remarkable swing from large deficit to substantial surplus in the current account between the first half of 1976 and the first half of 1977, served as yet another illustration of the inherent strength and adaptability of South Africa's balance of payments. Experts have long known that the so-called "balance of payment adjustment process" works exceptionally well in South Africa. This expression is jargon used by international economists and bankers to describe the process by which balance of payments deficits are transformed into surpluses and vice versa. This process is to some extent an automatic one. But it can be assisted, as was the case in South Africa, by appropriate monetary and fiscal policy measures. And it can certainly be hampered or even prevented from operating by inappropriate policies, as has, in fact, happened in many countries during the past year.

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What makes our balance of payments performance during the past year all the more remarkable, is the fact that South Africa was one of the few countries in the world which succeeded, in the difficult international conditions of this period, in transforming a large deficit into a sizeable surplus. Moreover, apart from the rise in the price of gold, we did not receive much assistance from an improvement in the terms of trade during this period.

All of this confirms once again that South Africa has a balance of payments with inherent strength and adaptability. We must concede a few facts: We have an open economy; Our imports and exports are large in relation to our gross national product; There are wide cyclical and other fluctuations in our current account; There are considerable fluctuations in our capital account as a result of both political and economic factors; At times these various fluctuations can exert serious pressure on our gold and other foreign reserves. But there certainly is no chronic or "structural" disequilibrium or weakness in our balance of payments.

On the contrary, the experience of the entire post-war period, and particularly of recent years, has shown that basically we have a healthy balance of payments which is capable of withstanding serious setbacks and considerable buffeting, and which has the ability to adjust within a reasonable period to unfavourable cyclical as well as non-cyclical influences.

To appreciate this, one only has to list the various unexpected shocks which the South African balance of payments has had to absorb during recent years. The first was the severe world recession of 1973–75. The second was the fall in the gold price from a peak of $198 per ounce towards the end of 1974 to a low point of $103 in August 1976. Then, in the middle of this downward movement came the events in Angola towards the end of 1975. This was followed in the middle of 1976 by the disturbances in Soweto and other black townships. In addition, considerable attention came to be focused on the problems of Rhodesia and South West Africa. And more recently new domestic and international events have affected our economic relations with the outside world.

Among the major effects of these adverse developments on our economy and balance of payments were higher defence expenditures, the continued stockpiling of strategic commodities and unfavourable consequences for the capital account of the balance of payments.

Yet the facts now show that, given the restrictive monetary and fiscal policies of the past eighteen months and the 1975 devaluation, the South African balance of payments was able to cope with all these adverse developments. Moreover, looking ahead I can see no reason why it cannot continue to make whatever adjustments may prove to be necessary. If, for example, we have to do without a significant net inflow of foreign capital for some time, the current account should be able to adjust to this. Similarly, if we are affected by sanctions of any kind, the balance of payments as such should show the necessary adaptability. Of course, these adjustments will not be painless. The rate of economic growth, for example, will certainly be lower in the long run without foreign capital and with sanctions than it would have been under more normal conditions. I am not questioning for a moment that our standard of living would be adversely affected by unfavourable developments of this kind. But I do believe that the balance of payments as such could make the necessary adjustments.

It would, of course, be a mistake to expect the current account surplus to remain at the exceptionally high level of the second quarter of 1977. The very fact that there is a current surplus at the moment is in itself abnormal, since South Africa usually runs a deficit on current account financed by a net capital inflow from abroad. Moreover, quite apart from cyclical changes, the current account surplus or deficit can be expected to fluctuate considerably from quarter to quarter. When the figures become available, they will probably show, for example, that during the third quarter of this year the current surplus declined considerably, partly because of the inclusion in the import figure of two large ships purchased by South Africa during this period. During the fourth quarter, however, it is possible that the surplus might increase again owing partly to the recent rise in the price of gold. In any event, for the calender year 1977 the current account should show a comfortable surplus, as compared with the relatively large deficit of R1 711 million registered in 1976.

Another major reason for the recent shift of emphasis in policy was the domestic economic situation. The authorities had to ask themselves what would happen to private fixed investment, inventory investment, private consumption, manufacturing output, unemployment, etc. if the existing restrictive monetary and fiscal policies were kept unchanged.

What *is* going on in the domestic economy at present and what are the immediate prospects? On the one hand, there are already certain important influences at work which should in due course bring about a new economic upswing in South Africa, if indeed they have not already begun to do so. The most important of these is the exceptional increase during the past year in the value of merchandise exports and the gold output, which together with the decline in imports has brought about the surplus on current account. This surplus in itself means that additional income is being created in the domestic economy.

A second important expansionary influence is the continuing process of import replacement. This process has been encouraged by official policy measures such as the devaluation of September 1975 and the revenue duty on imports included in the latest Budget, as well as by recent efforts of the private sector itself to "buy South African", with special reference to capital goods and intermediate goods (in view of the limited scope for import replacement in the case of consumer goods).

A third expansionary factor is the increase in certain forms of current government expenditure and investment by public authorities and corporations, particularly since this increase is to some extent being financed by bank credit.

Fourthly, although the continued decline in inventories is for the present probably still a deflationary factor, a point must be reached sooner or later where inventories are considered to be too low in relation to expected demand. When this results in an increase in inventory investment, it will naturally stimulate the economy.

Against these expansionary factors, certain deflationary influences have continued to operate in the economy. Private investment is still declining and private consumption still moving more or less horizontally in real terms. The general business climate has not yet become conducive to new expansion in the private sector. Profit expectations are still not an adequate spur to investment. In many sections of manufacturing there remains considerable surplus capacity. In these circumstances many industrialists and other entrepreneurs are still adopting an attitude of wait and see.

Until recently the combined effect of these deflationary influences proved strong enough to neutralise the expansionary influences to which I have referred. Whether this is still the case, is difficult to assess. It is possible that we have already reached the lower turning point of the business cycle and that we may now be in the early stages of a new cyclical upswing. Whether this is so or not, will only become clear when the relevant statistics for both the third and fourth quarters of 1977 become available, which will not be until the first quarter of 1978. But even if we have turned the corner and economic activity generally is now rising, it is still at a relatively low level for the time being.

If political circumstances and the net inflow of foreign capital had been more normal at this stage, the surplus on the current account of the balance of payments would by now have resulted in a noticeable upward movement in the net gold and other foreign reserves and the creation of an expansionary monetary and financial climate. In conjunction with the other expansionary forces at work in the economy, this would in all probability already have brought about a strong new upswing. In addition, the monetary authorities would then have been in a position to encourage this natural process by means of expansionary policies.

The present situation, however, is that the net inflow of capital is *not* normal and that the traditional balance of payments pattern is not in evidence for the moment. This creates a dilemma for the authorities. If we now attempt to stimulate the economy in general by means of such classical methods as accelerating the rate of money creation and government spending, this might well facilitate and encourage the outflow of private short-term capital. On the other hand, if the economy is deflated still further, additional "recessionary liquidity" might be created, which in present circumstances might also tend to leave the country. If this were to happen, we could end up with a weaker, instead of a stronger, position, in the sense that our rate of economic growth might well be lower without the compensation of an increase in the net reserves.

It is against this background that the recent decision by the authorities to shift the emphasis in their short-term stabilisation policy in the direction of stimulating sound economic growth, must be viewed. There is no longer a question mark over South Africa's ability to maintain control over its money supply, government spending, and other related factors, and therefore over the current account of the balance of payments. Our successes in this field have been widely recognised. The danger now is rather that a question mark might be placed over South Africa's ability, in present circumstances, to attain a new cyclical upswing in domestic activity. If such an upswing does not materialise soon, confidence in the South African economy might be adversely affected for reasons totally different from those of a year ago.

It is true that foreign capital does not tend to flow into an economy which appears to be in danger of getting into financial difficulties because of excessively permissive monetary and fiscal policies. But capital is also not attracted to an economy which keeps on cooling down and which creates the impression of economic stagnation. Up to a point it was essential for the monetary authorities to cool down the economy. This has been done with great success. But further deflation can now become counterproductive and harm the balance of payments as a whole by weakening the capital account.

A further important reason for the recent shift in emphasis in short-term economic policy is to be found in the fact that the recessionary tendency in the economy has inevitably exerted an adverse effect on the tax base of the economy. Quite understandably, the revenue from income tax on companies and individuals, as well as from indirect taxes, has been reduced by the slowdown in the economy. Steps therefore have to be taken to prevent the emergence of a vicious circle in this respect, in the sense that low tax revenues might leave the authorities no choice but to reduce expenditures or use more bank credit, and that the latter in turn, might lead the Reserve Bank to restrict bank credit to the private sector still further. The result would be a further reduction in economic activity, and so the circular process would repeat itself.

It is important, however, to be clear about what the shift of emphasis means and what it does not mean. It does not mean throwing caution to the winds and "spending for prosperity". It does not mean showing the green light for all sorts of public and private sector expenditure or for large wage and salary increases. It does not mean general tax reductions. But it does mean gradually relaxing the restrictive monetary and fiscal measures to the extent necessary to reverse the downward tendency in real gross domestic expenditure, and to ensure an adequate but not excessive increase in the money supply.

The precise way in which the economy is to be stimulated, is still under discussion. But in his policy announcement in August 1977 the Minister did mention various possibilities, including the selective stimulation of expenditure on housing in non-white residential areas and on schemes such as the electrification of Soweto, even if this involved the creation of some additional bank credit in the form of bridging finance. The Minister also referred specifically to the possibility of further export promotion. Moreover, in view particularly of the existence of considerable surplus capacity in manufacturing industries, he expressed support for the recent efforts of the private sector to encourage import replacement in respect of capital goods and intermediate goods, provided this was done on a sound economic basis.

What about inflation? Of course, inflation remains a serious problem. And it goes without saying that it remains a primary objective of official economic policy to reduce the rate of inflation below its present level of about 11%. But our inflation in recent months has not been the result of excessive money creation or spending. Nor has it been the result of excessive wage and salary demands by irresponsible trade unions. The shift in policy emphasis should accordingly not be inflationary in any sense. On the contrary, although the price indices have not yet fully reflected this, considerable progress is being made in removing the basic causes of inflation in South Africa, and there are grounds for believing that the rate of inflation will decline gradually in the period ahead.

To sum up, it is largely a question of balancing policy objectives. We need to strengthen our overall balance of payments further and to rebuild our gold and foreign exchange reserves to a more satisfactory level. We also need to reduce the rate of inflation to well below the present figure. To this end we have applied restrictive monetary and fiscal policies, and these have produced exceptionally good results in the form of a substantial improvement in the balance of payments on current account. Against this, the net inflow of capital has declined. To deflate the economy further would tend to be counterproductive. It would probably weaken rather than strengthen the capital account and would tend to erode the tax base. For this reason the recently announced shift of emphasis in official economic policy is in South Africa's best interests. The objective of official stabilisation policy now is to move with caution, but also with determination, to ensure that the new economic upswing gets under way in a manner which is not inflationary and which will assist in improving the capital account of the balance of payments.

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Numerous other studies have similarly indicated important national differences affecting management. In a *Business Management* article in 1977, vol. 8:1, Cummings, Schmikl and Blackburn also reported on differences relating to risk-taking propensity and to conciliatory versus belligerent attitudes.

It is essential that South African managers realize (as many of course do) that managerial approaches and solutions which may work well in other countries should not be transferred to South Africa without thorough consideration of cultural aspects which are bound to determine feasibility and success (or lack of these) here. This does not rule out benefitting from new approaches and insights in other countries. South African managers could learn much from their counterparts in countries such as Japan, Germany, the United States and France — but adoption of such approaches must be analytical rather than imitative.

Much more important than the understanding of these cultural differences by South African managers is, however, that multinational corporations, foreign investors in South Africa, and particularly governments in other countries, realize that solutions which work (or frequently don't even work) in their own countries cannot simply be transferred to South Africa. Whether they relate to business management or to politics these foreign solutions could easily be counter-productive.

To this day, few people have understood and adapted their behaviour to Blaise Pascal's insight (in the 17th Century) into the relativity of cultural norms, expressed in his dictum "Truth on this side of the Pyrennees, error on the other side".

* Hofstede, Geert: "Lions' cultures and foxes' cultures and the feasibility of self-management". Working Paper 77–22, European Institute for Advanced Management Studies, Brussels, October 1977.