South African Reserve Bank

1972

Annual Economic Report

A review of economic and financial conditions in the Republic of South Africa presented as background to the Chairman's Address to Stockholders at the Fifty-second Ordinary General Meeting to be held on 22nd August 1972.

Hierdie Verslag is ook in Afrikaans beskikbaar.

Contents

General observations

During the year that ended in June 1972, the outstanding features of the South African economy were the dominant influence on the domestic economy of international financial and trade developments, the reduction of the pressure on various factors of production and a consequent change in the emphasis of fiscal and monetary policy. In addition, several other favourable and unfavourable developments occurred during the year under review.

International financial developments and changes in international commodity markets significantly influenced the South African economy and especially the balance of payments during the year under review. During the second half of 1971 the uncertainties about exchange rates detrimentally affected the South African economy. It was indeed unfortunate that South Africa was adversely affected by international exchange rate uncertainties during 1971 at the time when the fiscal and monetary measures taken by the authorities had begun to reduce the excessive spending in the economy. The rate of increase in aggregate demand slowed down considerably during 1971 with a consequent reduction in the deficit on the balance of payments on current account throughout the year. The international currency uncertainties, however, not only slowed down the improvement of the current account during the course of 1971, but also caused the leads and lags in capital movements to turn against South Africa, particularly in the fourth quarter of 1971. This led to a substantial further decline in the gold and other foreign reserves. Under these circumstances the authorities resorted to the tightening of import control in November 1971 when no certainty existed about the realignment of exchange rates.

After the tightening of import control and the realignment of exchange rates in December 1971, including the devaluation of the dollar by 7,89 per cent and the South African rand by 12,28 per cent, an improvement occurred in the South African balance of payments during the first half of 1972. The detrimental leads and lags in foreign payments and receipts largely disappeared or actually turned in South Africa's favour while at the same time the capital inflow in other forms increased faster. Moreover, the dificit on the current account was substantially reduced during the first half of 1972. These developments resulted in a rapid and sustained rise in the gold and other foreign reserves. In addition to the factors already mentioned, other international and domestic developments, such as the exceptionally sharp rise in the price of gold on the private market, the considerable improvement in the international commodity markets and the excellent agricultural season in South Africa, contributed further to the improvement of the balance of payments. Thus, the value of exports and the net gold output rose substantially, while that of imports continued to decrease moderately.

The improved balance of payments situation, in particular the rise in the gold and other foreign reserves, in turn, affected the domestic economy favourably. Not only did the stock exchange recover, but the general business mood changed from pessimism to optimism. Moreover, the general liquidity of the banks and the private sector was augmented by the rise in the gold and other foreign reserves and this led to a decline in short-term interest rates and a softening of long-term interest rates.

Apart from the marked changes in the South African economy brought about by international developments, another outstanding feature of the economic situation in the year under review was the reduced pressure on the factors of production and a consequent change in the emphasis of fiscal and monetary policy. During most of 1971 the authorities continued to pursue a fairly restrictive economic policy aimed at reducing the pressure on production resources. In particular, the policy was directed at curbing excessive rises in demand originating from spending on consumer goods and certain types of capital outlays in order to provide elbow room for investment on infrastructural development and expansion of production capacity in manufacturing. This policy achieved its objective in that the rate of increase in government spending, private consumption expenditure and certain types of capital investment declined and the pressure on the labour and capital resources eased. Towards the end of 1971 the economy had, therefore, cooled off to such an extent that the authorities were enabled to change to a more expansionary policy. Apart from the stimulative effects of the devaluation in December, the 1972/73 Budget contained various measures to promote faster economic growth without causing a new build-up of pressures on the factors of production and thus leading to more inflation. The Reserve Bank also announced fairly substantial increases in the ceilings on bank credit as from the 1st April 1972. The decision of the authorities on 30th June 1972 to maintain the existing exchange rate relationship between the rand and sterling after the British authorities' decision to allow the pound to float, is further evidence of the government's intention not to do anything that may hamper economic growth. On 10th August 1972 the Reserve Bank also reduced the Bank rate by $\frac{1}{2}$ per cent and adjusted its pattern of rates quoted for transactions in government stock, downwards by $\frac{1}{4}$ per cent. However, the authorities' approach was to stimulate the economy moderately and to avoid a further increase in prices. Moreover, a relaxation of import restrictions was also announced on 24th July 1972, in order to ensure that shortages of certain goods do not aggravate the problem of inflation.

Against these favourable tendencies have to be set some unfavourable developments which occurred during the year under review. The growth in manufacturing output remained low, despite the existence of some surplus plant and machine capacity, and productivity generally deteriorated. Consequently, the overall growth rate of the economy was unsatisfactory, although a slight acceleration occurred in the second quarter of 1972. Exports of manufactured and mining products did not yet show any significant rise and the higher export figure was mainly attributable to the price effects of devaluation, improved international commodity markets and a good agricultural year in South Africa.

The economic situation during the year under review, however, also showed several other welcome developments apart from the favourable influences of international financial developments and changes in international commodity markets on the domestic economy. Thus, gross domestic saving increased significantly, the government succeeded in reducing certain types of expenditure and was successful in its borrowing operations, salaries and wages generally rose at a lower rate than profits and thus reduced the relative share of salaries and wages to the total gross domestic product to a lower level and real activity would appear to have started to revive in the second quarter of 1972 in an atmosphere that was generally conducive to higher economic growth.

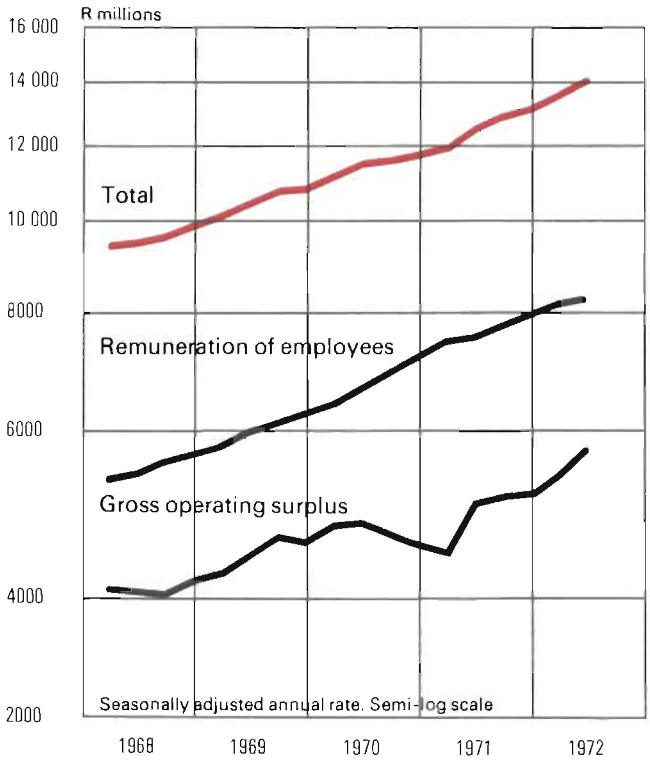
National accounts and other economic indicators

Acceleration in rate of increase in gross domestic product at current prices

During the year that ended in June 1972 the gross domestic product at current market prices increased by 12 per cent, compared with an increase of 8 per cent in 1970/71. This higher rate of increase was attributable to a favourable agricultural year, the high gold price ruling on the private market, the recovery of metal and mineral prices on international markets, higher export prices obtained for important agricultural products and the effects of the general realignment of currencies during the past twelve months.

The main contribution to the higher rate of increase in the gross domestic product during 1971/72 came from the primary sectors of the economy, namely agriculture and mining. Owing to favourable climatic conditions, record maize and wheat crops were produced. With wool prices increasing by about 60 per cent during the past marketing season and with higher export prices realised for sugar and fruit, agriculture's contribution to the gross domestic product increased by 17 per cent during 1971/72, compared with an increase of only 1 per cent in 1970/71. The mining sector experienced an even more pronounced improvement. During the year that ended in June 1971, mining's contribution to the gross domestic product at current prices *declined* by nearly 8 per cent, whereas it increased by more than 14 per cent in 1971/72. This increase, reflecting a higher operating surplus, was a direct result of the higher average price obtained for gold sold on the private market and the recovery of metal and mineral prices on international markets.

Gross domestic product



Notwithstanding further price rises, the contribution of the secondary sector to the gross domestic product showed a lower rate of increase during the year that ended in June 1972 than during the previous year. This lower rate was reflected in a decline in the rate of increase in salaries and wages. The value added by the tertiary sector increased at a slightly higher rate during 1971/72 than during the previous year mainly as a result of an increased growth in the profits of wholesalers and retailers earned on higher turnovers.

As the accompanying table shows, salaries and wages rose at a lower rate during the year under review than during the preceding year, whereas the operating surplus (mainly profits of the sectors agriculture, mining and commerce) showed a marked rise, in contrast to no change in the preceding year. The lower rate of increase in salaries and wages made a significant contribution to the reduction of inflationary pressures during the year that ended in June 1972. It is also noteworthy that the improvement in operating surplus led to an increase in the relative importance of the operating surplus in the gross domestic product. This represents a reversal of the downward trend observed during the preceding three years.

Percentage increases in components of gross domestic product

	Year ended June	
	1971	1972
Remuneration of employees	15	10
Operating surplus.................	—	14

During the year under review domestic and, more particularly, international price changes materially influenced South Africa's economy and made the trends of certain economic magnitudes at current prices quite different from those in real terms, i.e. after excluding price changes. Thus, although the gross domestic product at current prices rose much faster during the year that ended in June 1972 than during the previous year, the real gross domestic product increased at about the same relatively low rate of 4 per cent. Moreover, if the contribution of agriculture is excluded the real growth rate of all the other sectors of the economy together was reduced to approximately 2½ per cent, as against about 4½ per cent during the previous year. If the value added by mining, which showed a decline of 4 per cent, is also excluded, the real growth rate in the secondary and tertiary sectors together was 3½ per cent in 1971/72, compared with 4½ per cent in 1970/71. Apart from the large contribution by the agricultural sector and the decline in that of mining, the overall growth comprised of little growth in the sectors manufacturing and transport storage and communication, and a lower rate of growth than the previous year in the sectors construction, electricity, gas and water, and community, social and personal services.

The gross domestic product deflator, which is used to measure overall price increases in the economy, rose by more than 7 per cent during the year that ended in June 1972, compared with about 4 per cent the previous year. Although the rise in indirect taxes and government administered prices in the second quarter of 1971 contributed to the higher gross domestic product deflator, international price increases and the realignment of exchange rates, made a major contribution to the overall increase in prices.

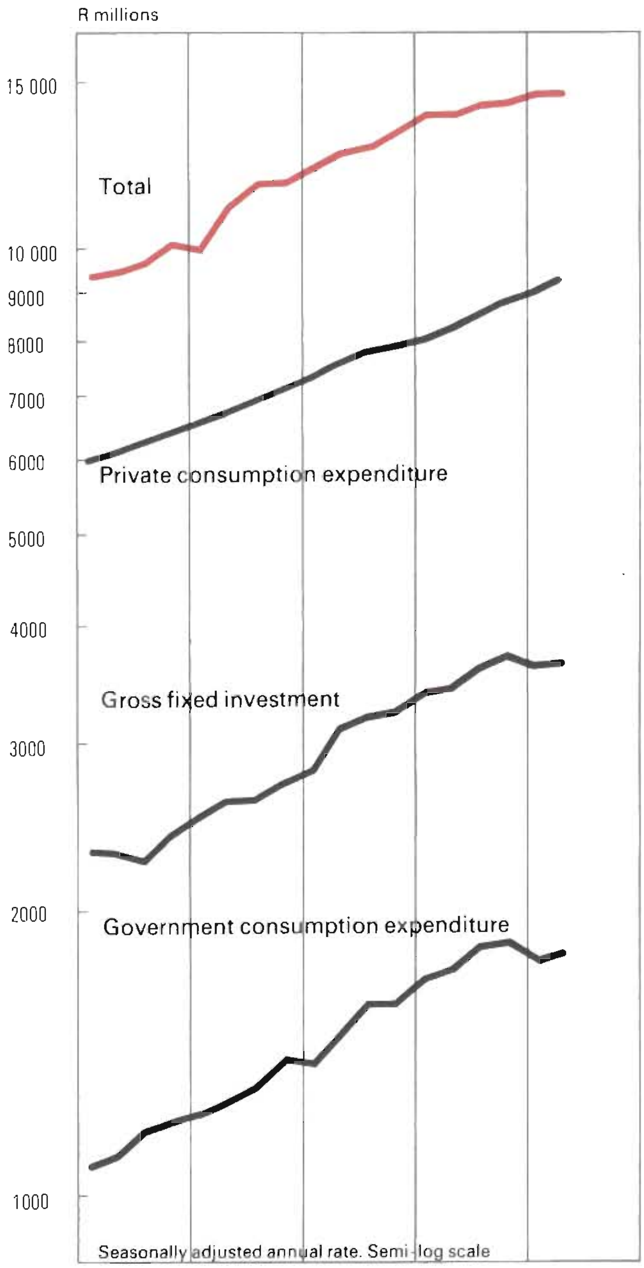
Quarterly estimates show that the gross domestic product at current market prices rose faster during the first half of 1972 than during the second half of 1971, mainly owing to the good maize crop and higher profits of gold and non-gold mining companies resulting from higher prices obtained abroad. As the business mood changed from a pessimistic outlook in the second half of 1971 to a more optimistic assessment of future economic prospects in the first half of 1972, manufacturers and traders were also enabled to increase their turnovers and profits.

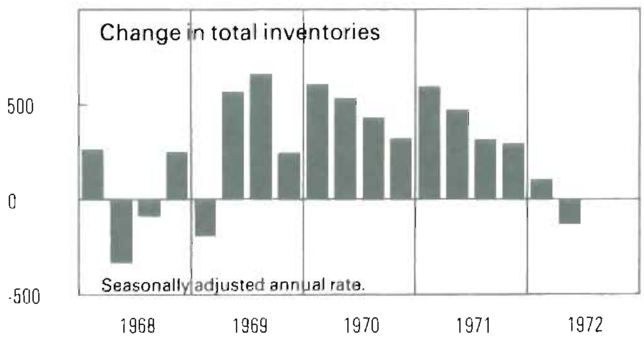
According to quarterly estimates of changes in the real gross domestic product during the course of the year under review, it would appear that the real growth rate remained low during 1971 and the first quarter of 1972, but showed a slight acceleration during the second quarter. This welcome upturn in the growth rate during the second quarter of 1972 was caused not only by higher agricultural production, but also by a rise in the value added by most of the non-agricultural sectors of the economy. The expansionary measures introduced by the authorities and the stimulative effects of the devaluation of the rand and the general realignment of exchange rates in December, therefore, appear to have produced an acceleration in the volume of economic activity during the second quarter of 1972.

Lower rate of increase in domestic expenditure

As the accompanying table shows, the rate of increase in total domestic expenditure declined significantly during the past two years. Both fixed investment and government consumption expenditure increased at a lower rate during the year that ended in June 1972 than during the previous year, whereas

Gross domestic expenditure





Percentage increase in gross domestic expenditure

	Year ended June		
	1970	1971	1972
Private consumption expenditure	11	10½	11
Government consumption expenditure	14	20	9
Gross domestic fixed investment	15	18	11
Gross domestic expenditure	17½	12	7

private consumption expenditure rose at a slightly higher rate. However, if price increases are excluded, private consumption expenditure also increased at a lower rate during the past year than during the previous year.

This significant reduction in the rate of increase of aggregate monetary demand, as measured by the total gross domestic expenditure, was reflected in a substantial reduction in the excess of gross domestic expenditure over the national product. The improvement in the balance of payments on current account was, therefore, to a significant extent attributable to the reduced rate of increase in aggregate monetary demand.

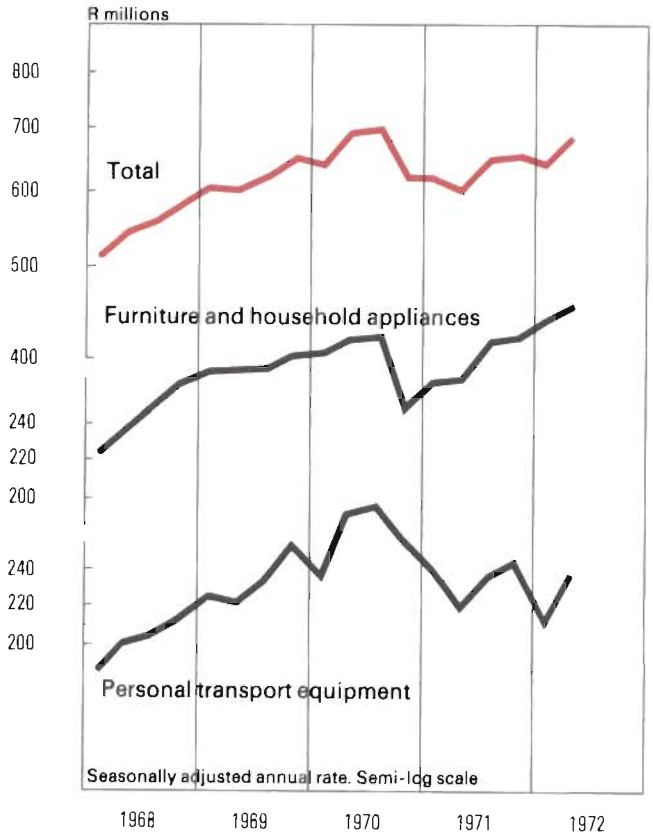
Smaller growth in real consumption expenditure

During 1970/71 the fiscal and monetary measures directed at reducing the rate of increase in private consumption expenditure on durable goods were so effective that, in real terms, an actual decline was recorded. In 1971/72 expenditure on durable goods at constant prices increased again by 3 per cent. It is also significant that the volume of expenditure on all other goods and services, i.e. semi-durable goods, non-durable goods and services, increased at a reduced rate during 1971/72. As these categories also showed the most rapid price rises, it would appear that some measure of price resistance has developed among consumers. It also indicates that the demand for many products and services is relatively elastic to price changes. Quarterly figures at current and constant prices indicate that private consumption expenditure, after it had increased at an exceptionally high rate in the third quarter of 1971, rose at a lower rate during the subsequent three quarters.

Growth rate in private consumption expenditure

Year ended June	At current prices	At constant prices		
		All goods and services	Durable goods	Other goods and services
	%	%	%	%
1970	11	7½	11	7
1971	10½	5	— 2	6
1972	11	4½	3	4½

Private consumption expenditure on durable goods at constant 1963 prices



In addition to reducing the excessive rate of increase in real private consumption expenditure, the government was also very successful in considerably reducing the rate of increase in its own consumption expenditure, namely from 20 per cent in 1970/71 to only 9 per cent during the year that ended in June 1972. During the first half of 1972, government consumption expenditure actually declined.

Slow-down in gross domestic fixed investment

From the accompanying table showing the most important changes in the growth rate of certain components of fixed investment, it is clear that total gross fixed investment rose at a considerably lower rate during the year that ended in June 1972 than during the preceding year. This decline resulted from declines in the capital outlays by mining and commerce and on residential building and a substantially lower rate of growth in fixed investment by private manufacturing. Fixed investment by public corporations rose more rapidly and capital outlays by the S.A. Railways and the Post Office continued to increase at very high rates.

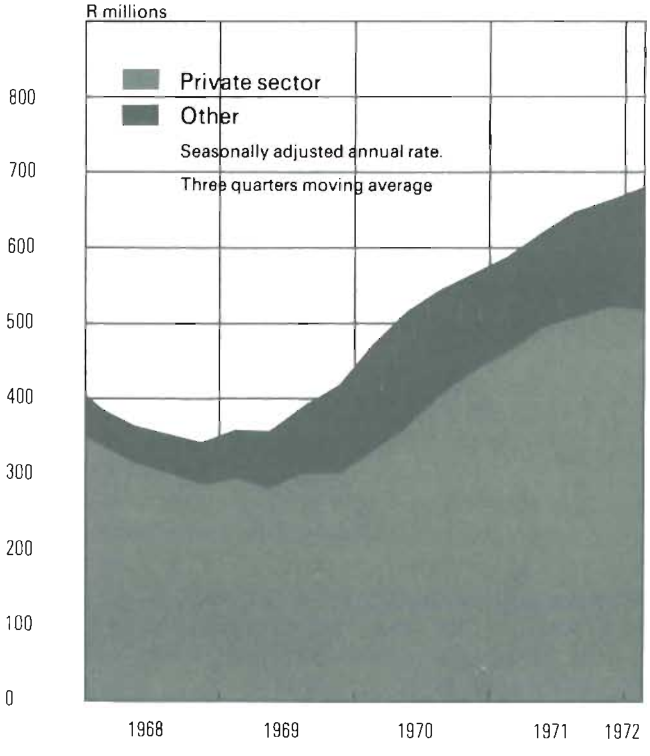
Notwithstanding substantial price increases, the value of real fixed assets of private manufacturing, nevertheless, increased by 9 per cent over the past two years together and that of total manufacturing by 15 per cent. This increase, therefore, represented an addition to the production capacity of manufacturing and, with actual production rising only moderately, implied that there was some measure of surplus plant capacity.

Quarterly estimates reveal that, after total gross fixed investment had risen at a relatively high rate up to the fourth quarter of 1971, it declined slightly during the first half of 1972. Fixed investment by the private sector, which had increased up to the third quarter of 1971, remained almost unchanged on a slightly lower level during the subsequent three quarters, whereas fixed investment by private manufacturing showed little change over the past twelve months.

Percentage change in components of gross domestic fixed investment

	Year ended June	
	1971	1972
Private enterprises:	21	2
Manufacturing	41	10
Mining	4	—12
Commerce	30	—1
Residential building	29	—2
Public authorities:	19	24
S.A. Railways	24	51
Post Office	40	26
Public corporations	1	17
Total fixed investment	18	11

Gross fixed investment: manufacturing

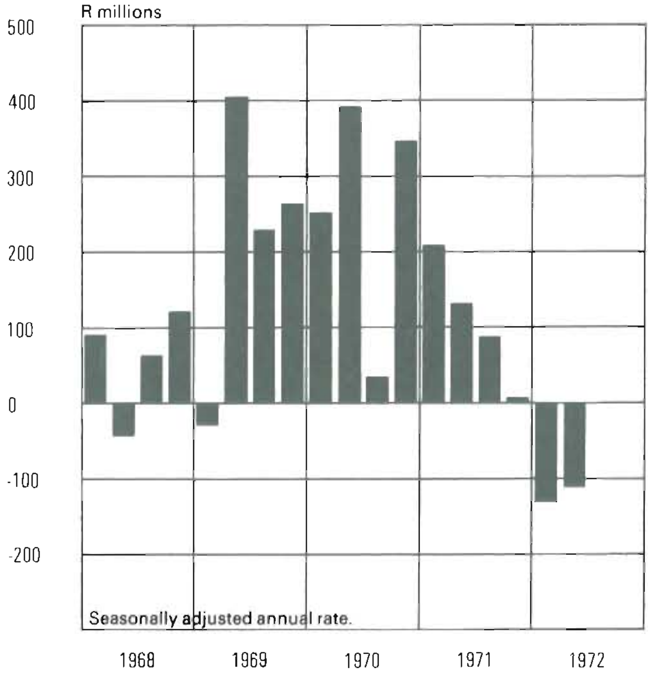


Smaller net addition to inventories

An outstanding feature of economic developments during the past three years was the large and sustained inventory build-up. In 1969/70 and 1970/71 additions to inventories at book value amounted to more than R550 million and more than R450 million, respectively. Although a slow-down in inventory accumulation occurred during the year that ended in June 1972, net additions to inventories at book value, nevertheless, still amounted to about R350 million. Owing to the rapid rise in prices during the year under review, however, the smaller addition to inventories at constant prices was much more pronounced.

The slow-down in inventory accumulation during the past year can largely be ascribed to smaller additions to commercial and industrial stocks. This was particularly evident during the first half of 1972, when the total value of industrial and commercial inventories, after adjustment for seasonal variations, actually declined. The running-down of industrial and commercial inventories during the first half of 1972 alleviated the pressure on the balance of payments and contributed materially to the substantial further improvement of the balance of payments on current account.

Change in industrial and commercial inventories



Welcome increase in domestic saving

After it had increased at an average annual rate of only 1½ per cent during the period from 1967/68 to 1970/71, gross domestic saving increased markedly by 25 per cent during the year that ended in June 1972. Substantial increases were recorded in corporate saving, personal saving and the current surplus of the government. This rise resulted in an increase in the ratio of domestic saving to the gross domestic product, namely from 21 per cent in 1970/71 to 23 per cent in 1971/72.

The increase in personal saving is notable in view of the various efforts of the authorities to encourage saving and to reduce the propensity to spend. The increase in the ratio of personal saving to disposable income from 9 per cent in 1970/71 to nearly 10 per cent in 1971/72 must, however, to a large extent be ascribed to the large rise in agricultural income, which contributed materially to both disposable income and personal saving.

Notwithstanding the increase of R675 million in gross domestic saving, it was still insufficient to finance gross fixed and inventory investment and a substantial amount of R499 million had to be financed from foreign sources.

Manufacturing and mining production sluggish

The most disappointing feature of the South African economy during the year under review was the sluggishness of manufacturing and mining production. The progressive decline during the past two years in the rate of increase in manufacturing production is shown by the changes in the average monthly index of the physical volume of manufacturing production given in the accompanying table. The levelling-off in manufacturing output during 1971/72 was also reflected in a decline in the value of unfilled orders between March 1971 and April 1972. The inadequacy of the growth rate in manufacturing production over the past two years is obvious, if these rates are compared with the target growth rate of 6,4 per cent of the Economic Development Programme for the period 1969 to 1975. There are, however, a number of expansionary forces at work which are conducive to an increase of production.

Divergent tendencies occurred in the production of different classes of products. Whereas the production of durable goods declined by 2,2 per cent during the ten months that ended in April 1972 compared with the corresponding period in the previous year, the production of non-durable goods rose by 3,5 per cent. Further important changes over this period in the production of individual categories of goods are shown in the accompanying table.

Apart from the low rate of growth of 1,2 per cent in manufacturing production during the ten-month period that ended in April 1972, the output per man-hour declined by about 0,2 per cent because hours worked by production workers increased by 1,4 per cent during the corresponding period.

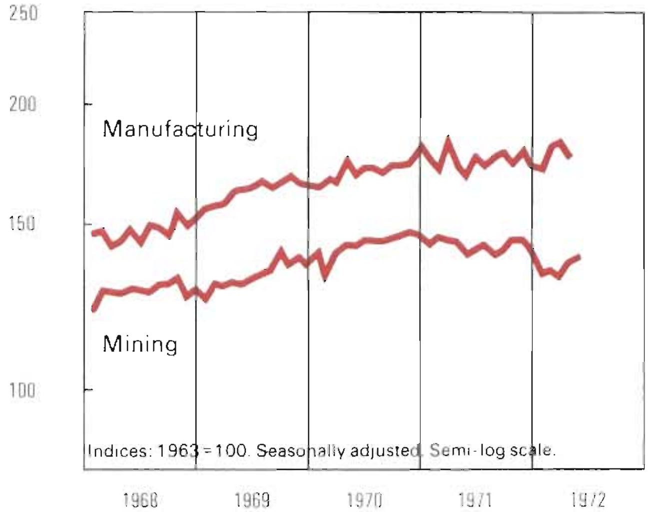
The growth rate of mining production was even more disappointing than that of manufacturing production. The index of the volume of gold production actually declined by 5,2 per cent during the year that ended in June 1972, compared with the previous year. This decline in gold production resulted from a decline of more than 3 per cent in the tons of ore milled and a slight decline in the grade of gold ore mined, made possible by the higher average price of gold obtained on the private market. It is clear, therefore, that total activity in the gold mining industry did not decline to the same extent as the number of kilograms of fine gold produced. In fact, the higher income generated by the gold mining industry, notwithstanding the decline in the number of kilograms produced, represented an important expansionary factor and helped to improve the balance of payments and the general business mood.

Growth in manufacturing production

Year ended June	%
1970	8,0
1971	4,1
1972*	1,2

*Latest available figure up to April 1972 compared with figure for corresponding period during previous year.

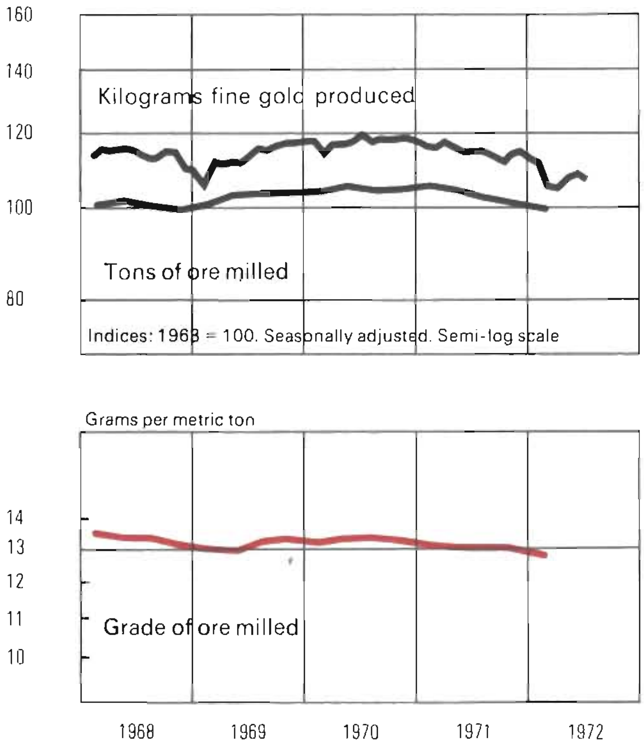
Production



Changes in production

Commodity	%
Food	6,3
Chemical products	6,1
Non-metallic mineral products	2,8
Basic metals and metal products	—3,4

Gold mining



Non-gold mining production also declined and during the eleven months that ended in May 1972 it was about $2\frac{1}{2}$ per cent lower than during the corresponding period of the previous year. Mining production in total consequently declined by 4 per cent over this period, and contributed much to the disappointing overall growth rate in the economy during the year that ended in June 1972.

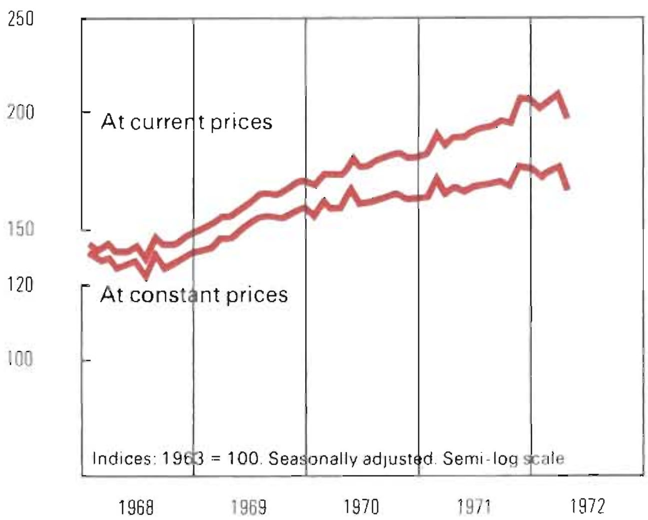
Levelling-off in building and construction activity

After it had increased sharply from 1968 to 1970, building and construction activity levelled off significantly during 1971 and the first quarter of 1972. The levelling-off tendency is indicated by various series such as the physical volume of production of cement, bricks, glass and allied products, the value of wholesale sales of building materials, the value of building plans approved, total hours worked and employment in construction. Advances granted by building societies for the construction of new buildings, which had declined for about two years until August 1971, increased sharply up to June 1972. More funds have, therefore, become available for the financing of residential buildings thus providing scope for more activity in this field. The levelling-off in building and construction activity was partly attributable to the official policy measures directed at curbing the excessive spending on buildings and construction and partly to the oversupply of office space and shops in certain of the larger cities. According to the value of real estate transactions, conditions in the property market as such remained less buoyant during the past two years than during the 1968 to 1970 boom period.

Slightly improved trading activities

The turnover at current prices of the retail and wholesale trade rose at a substantially faster rate during 1971/72 than during the previous year, but if price increases are excluded, the volume of trade increased only moderately. The value of retail sales rose by more than 10 per cent during the ten-month period that ended in April 1972, compared with a slower increase of 8 per cent during the previous year. The volume of retail sales, however, showed only a slight increase namely from 3.8 per cent in 1970/71 to 4.0 per cent in 1971/72. Sales of furniture and household appliances contributed substantially to the overall acceleration in the turnover figures. Apart from substantial short-term fluctuations in the course of the past two years, total motor trade figures showed little change between 1970/71 and 1971/72.

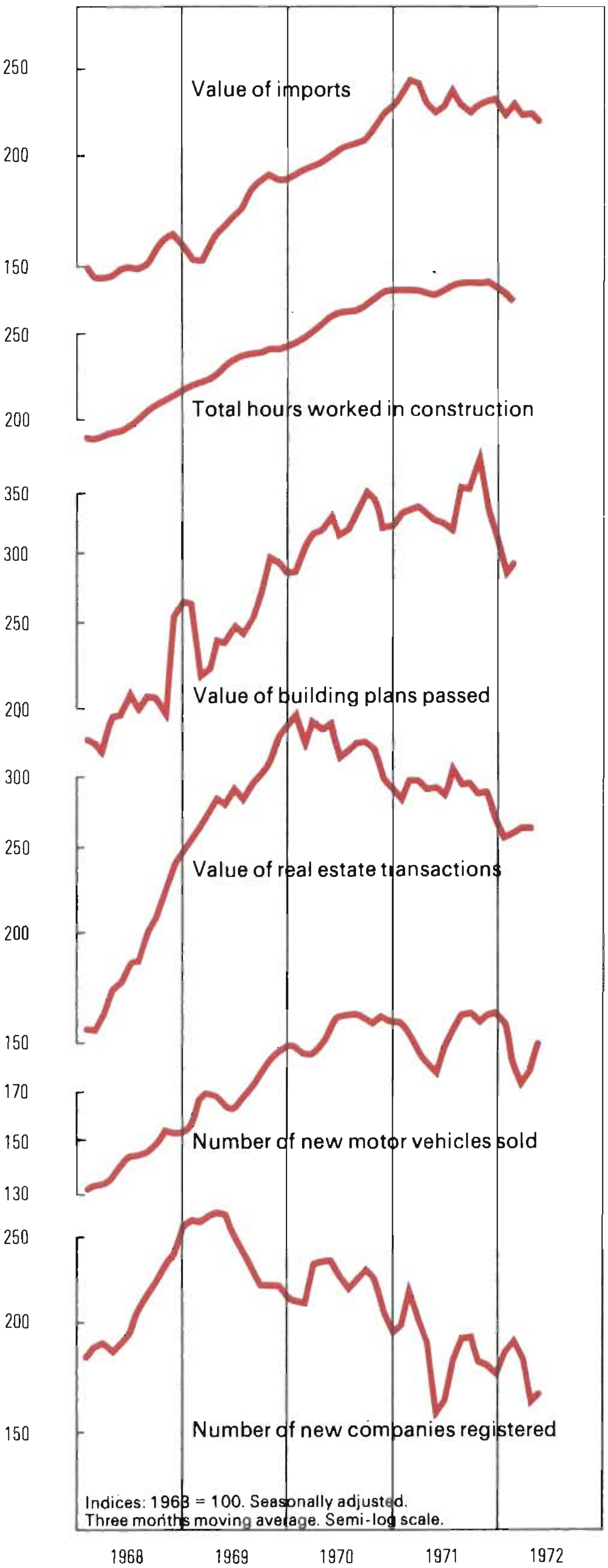
Retail sales



Levelling-off of other economic indicators

In addition to the slowing-down of manufacturing and mining production and construction activity, various other economic indicators levelled off during the year under review and confirmed the diagnosis of a downward phase of the business cycle. Consumption of rolled and drawn steel products, for example, declined appreciably in the second half of 1971 and despatches of these products to the local market continued to decline from May 1971 to April 1972. The number of additional Bantu em-

General economic indicators

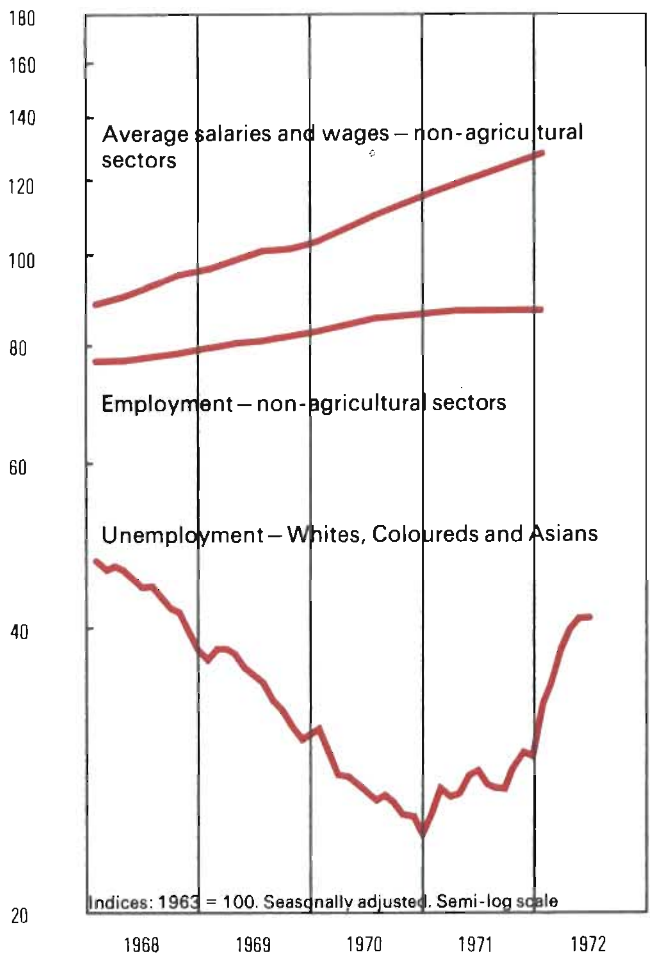


ployees approved under the Physical Planning Act levelled off throughout 1971/72. The number of new companies registered declined continuously for three years up to June 1972, whereas the number of companies liquidated increased sharply throughout 1971/72. Although the value of merchandise imports declined only moderately, the volume of imports declined substantially throughout the year that ended in June 1972.

Easing of labour situation

The lower rate of economic growth experienced during 1971 and the first half of 1972 resulted in an easing of the overall labour situation. The seasonally adjusted number of registered unemployed Whites, Coloureds and Asians, for example, increased almost uninterruptedly from 7 541 in December 1970 to 12 771 in June 1972. The increase in registered unemployed was particularly sharp during the first half of 1972. Notwithstanding the marked increase in unemployment, the figure was still relatively low and represented only about ¾ per cent of the total

Labour



number of Whites, Coloureds and Asians employed in the second quarter of 1972.

The slowing-down of economic activity was also reflected in a much lower rate of increase in the total employment in the non-agricultural sectors of the economy during 1971 and the first quarter of 1972. In the mining sector, total employment declined substantially throughout 1971 and the first five months of 1972, and in the construction sector the rate of increase in employment was much lower in 1971 than the exceptionally high rate of increase during the preceding four years. During the first few months of 1972 the employment in the construction sector actually declined. Lower rates of growth were also shown by employment by the Post Office, the public authorities, the S.A. Railways and the manufacturing sector. Apart from the slower increase in non-agricultural employment, divergent tendencies were recorded in the rate of increase in White as against Non-White employment in certain major sectors of the economy, as shown in the accompanying table.

Percentage change in employment

	1969/70 to 1970/71	Jul. 1970 — March 1971 to Jul. 1971 — March 1972
Manufacturing:	4,8	2,9
Whites	1,5	0,9
Non-Whites	5,9	3,4
Construction:	12,2	4,6
Whites	6,5	—1,7
Non-Whites	13,4	5,7

During the year that ended in June 1972, the output per worker in all non-agricultural sectors of the economy increased by only about 1 per cent, compared with an average annual rate of increase of about 2 per cent during the past decade. Major contributions to this decline were made by mining, manufacturing and construction. The mining industry experienced a difficult situation with a cutback in the production of certain types of minerals and the mining of lower grade gold ore, with the result that the increase in output per worker declined from an average annual rate of 4 per cent during the past decade to only about 1½ per cent in 1971/72. The output per worker in manufacturing declined by nearly 2 per cent during the nine months that ended in March 1972, compared with the corresponding period of the previous year. Although it is difficult to measure the real output per worker in the construction sector, it would appear that a decline of about 2 per cent was recorded for the year that ended in June 1972.

In conformity with the easing of the labour situation, the rate of increase in average wages and salaries also declined slightly. After having risen by 11 per cent during 1970/71, the average wages and salaries in the non-agricultural sectors of the economy rose by about 9 per cent in the year that ended in June 1972. Nevertheless, this increase in average wages and salaries together with an increase of only about 1 per cent in output per worker would suggest a substantial increase in the labour cost per unit of output during the past year.

Prices

A notable feature of the economy during the year that ended in June 1972 was the decline in the rate of increase in consumer prices, despite the adverse effects on consumer prices of the devaluation of the rand and the revaluation of the currencies of some of South Africa's main trading partners. The accompanying table shows that the rate of increase in the seasonally adjusted consumer price index was 1 per cent lower between June 1971 and June 1972 than during the preceding twelve months. This decline in the rate of increase is, however, to a certain extent attributable to the relatively sharp rise in consumer prices in April 1971 which contributed significantly to the high rate of increase from June 1970 to June 1971. However, the rise of 5,2 per cent in the cost of living during 1971/72 is still unduly high for South Africa. It is also a fact that imported inflation as a result of the realignment of exchange rates has as yet probably not had its full effect on the consumer price index. It is significant, however, that the annual rate of increase in the seasonally adjusted consumer price index actually declined from 5,5 per cent during the second half of 1971 to 4,9 per cent during the first half of 1972.

Consumer prices

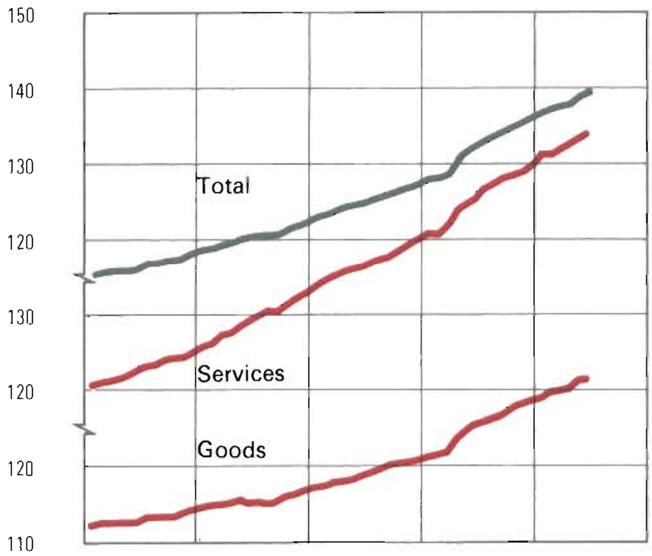
Annual percentage rates of increase in seasonally adjusted indices

	June 1970 to June 1971	June 1971 to June 1972	Dec. 1971 to June 1972
Services:	6,7	6,0	5,7
Housing	5,9	6 6	6,6
Other	8,2	4,8	4,1
Goods:	5,7	4,8	4,5
Food	4,7	5,5	4,2
Furniture and equipment	5,2	5,0	4,0
Clothing and footwear	2,0	5,5	5,8
Vehicles	7,8	6,3	6,5
Other	8,2	3,2	3,8
Total	6,2	5,2	4,9

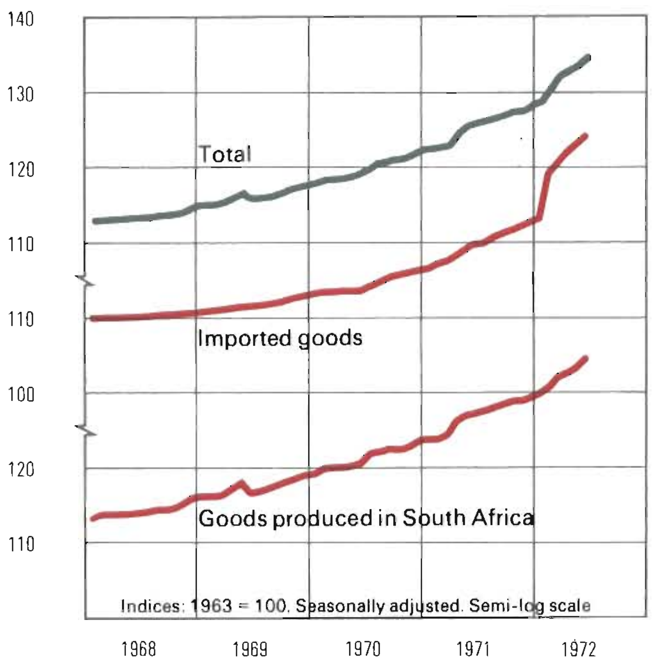
Increases in the prices of services once again made the major contribution to the rise in consumer prices during 1971/72. Various items of the consumer price index recorded pronounced increases, but those mainly responsible for the overall rise in the index, also taking account of their relative importance in consumer spending, were rent, home-owners' costs, meat, vegetables, furniture and appliances, clothing and footwear and vehicle prices.

The rate of increase in wholesale prices also accelerated during recent years, partly owing to the same factors that caused the rate of increase in consumer prices to accelerate. Whereas wholesale prices increased at an average annual rate of 3,2 per cent from June 1962 to June 1972, they rose by 5,3 per cent between June 1970 and June 1971, by 7,3 per cent from June 1971 to June 1972, and at an annual rate of no less than 10,7 per cent during the first half of 1972. The latter acceleration was largely caused by the influence of the devaluation of the rand and the general realignment of exchange rates in December 1971. Wholesale prices of imported goods and of agricultural, forestry and fishing products, for example, rose at annual rates of 19,0 and 13,4 per cent respectively, during the first half of 1972. The latter increase was mainly the result of increases in the prices of wool, hides and skins, and was also partly due to the effect of the devaluation.

Consumer prices



Wholesale prices



Wholesale prices

Annual percentage rates of increase in seasonally adjusted indices

	June 1971 to June 1972	December 1971 to June 1972
Goods produced in South Africa:	6,0	8,5
Agriculture, forestry and fishing	6,6	13,4
Manufacturing	5,7	7,1
Other	9,9	13,9
Imported goods:	11,9	19,0
Total	7,3	10,7

Balance of payments

International economic developments

During the year that ended in June 1972, the South African economy and, in particular, the South African balance of payments was influenced significantly by developments in the international monetary field. The international currency crisis in May 1971 was followed by President Nixon's announcement in August 1971 of a new package deal to further economic stability and prosperity in the United States. These measures included, *inter alia,* the suspension of the convertibility of dollars into gold or other reserve assets and the imposition of a temporary surcharge of 10 per cent on all dutiable imports not subject to quantitative restrictions. In response to the steps taken by the United States, South Africa's major trading partners allowed their currencies to float, and the expectation that these currencies would appreciate in relation to the dollar and the South African rand created more uncertainties affecting the balance of payments. These uncertainties considerably slowed down the progress already made during 1971 in reducing the balance of payments deficit, because they gave rise to leads in import and other foreign payments, lags in export and other foreign receipts, and the withholding of foreign capital. Under these circumstances, and because there was at that time no assurance that an international agreement on the realignment of exchange rates would be reached soon, the South African Government, on 24th November 1971, announced a considerable tightening of import control as a balance of payments measure.

On 18th December 1971 the Group of Ten reached the so-called Smithsonian agreement, in terms of which the US dollar was devalued by 7,89 per cent and certain other currencies were revalued in varying degrees. The official dollar price of gold was, therefore raised from \$35 to \$38 per fine ounce. It was also agreed that the maximum margin of fluctuation around the new central selling rates would be $2\frac{1}{4}$ per cent on either side, as against the IMF's previous margin of deviation from parity of 1 per cent. On the 21st December the South African Government decided to devalue the rand by 12,28 per cent and thus increased the official rand price of gold from R25 to R28,50 per fine ounce. This step was partly an adjustment necessitated by the general realignment of exchange rates and partly a policy measure designed to improve the overall balance of payments and, at the same time, to stimulate economic growth. After the tightening of import control and the devaluation of the rand South Africa's balance of payments did indeed improve considerably.

Exchange speculation continued, however, while discussions went on regarding proposals for an international monetary reform, including the finding of a solution to the problem of the inconvertibility of the dollar and the general improvement of the balance of payments adjustment process. In this atmosphere of continued uncertainty, successive waves of speculation from time to time caused pressure on certain currencies and, at the same time, contributed to the sharp rise in the price of gold on the private market. Heavy speculation against sterling in June 1972 and the resultant outflow of capital forced the U.K. authorities to take a number of temporary emergency measures. On 23rd June 1972 it was decided to allow the pound to float. The Bank of England also raised its Bank rate from 5 to 6 per cent and instituted exchange control on transactions between the United Kingdom and most of the other countries of the Sterling Area. The most important effect of the exchange control measures from South Africa's point of view is that transactions in securities of overseas Sterling Area countries will be treated in a similar way as securities of countries outside the Sterling Area. This means that purchases of South African securities by United Kingdom residents will have to be made with currency obtained at a premium in the sterling securities market.

After the announcement by the United Kingdom to float the pound, the S.A. Reserve Bank and various other central banks temporarily suspended foreign exchange dealings. South Africa's exchange rate policy decision was naturally dependent on the extent of the sterling depreciation and the action taken by the EEC countries. After considering all the information available, the government decided on 30th June to maintain the link with sterling. Consequently, the value of the rand has remained unchanged in terms of sterling and that of other exchange rates have been based on sterling rates. The main reasons for this decision of the government were the following:

1. The balance of payments had only started to improve and the gold and other foreign reserves had not yet attained a satisfactory level.
2. It was desirable that nothing should be done which could hamper exports, particularly in view of Britain's entry into the European Economic Community.
3. A stable relationship between the rand and the British pound has considerable value for South African business organisations, as Britain is still our largest single trading partner.
4. If the link with sterling had not been maintained, there would also have been the danger that speculative capital movements could occur which could affect the balance of payments adversely.
5. Finally, it was very important that nothing should be done which could put a damper on an upswing in the domestic economy.

The immediate effect of this decision was a slight depreciation of the rand against currencies other than sterling. The selling rate of sterling for dollars went down by as much as 7,6 per cent below par on 4th July, but recovered again and fluctuated between 5,9 and 6,8 per cent during the rest of July and closed on 6,0 per cent below par on 31st July.

Substantial improvement in overall balance of payments

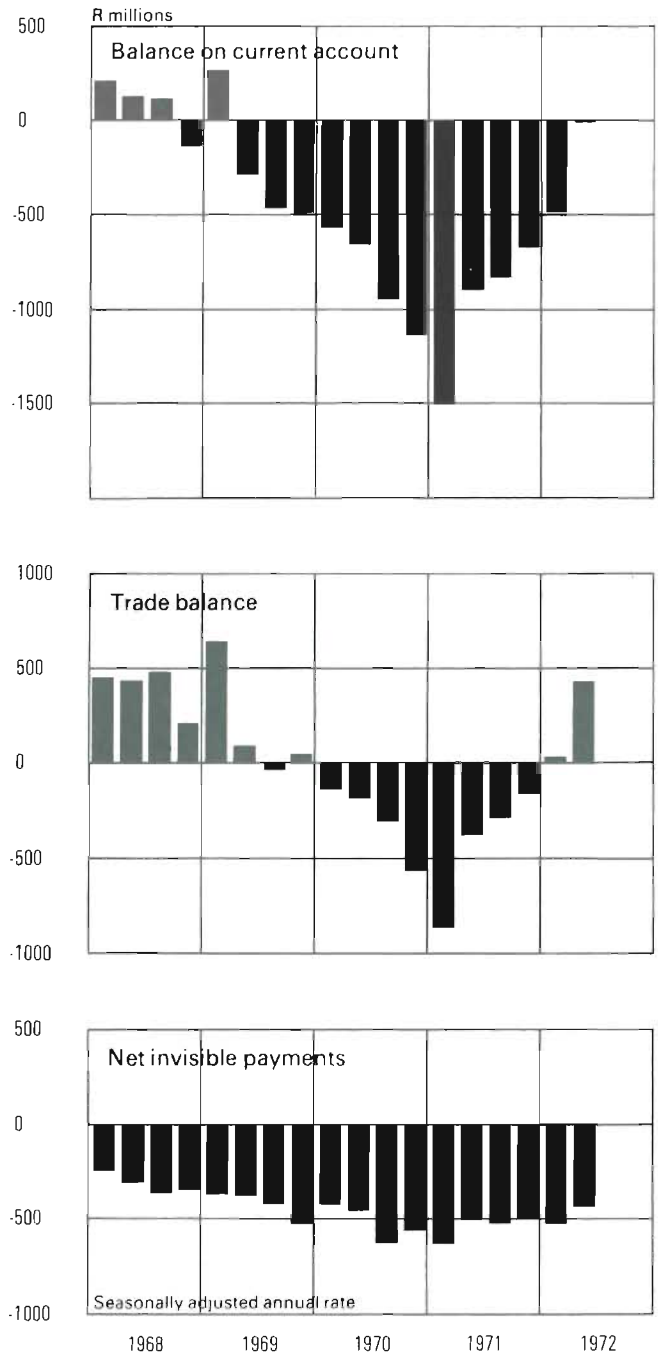
Although the deficit on the balance of payments current account improved during the course of 1971 as a result of the monetary and fiscal policies pursued by the authorities to reduce excessive demand, international currency uncertainties caused the leads and lags to turn against South Africa, particularly on the capital account, and led to a sharp decline in the gold and other foreign reserves. After the devaluation of the rand in December 1971, the current and capital accounts of the balance of payments both improved considerably and led to a reversal of the downward trend in the gold and other foreign reserves. Apart from the favourable effects of the realignment of exchange rates, other international and domestic developments contributing to the further improvement of the balance of payments were (1) the exceptionally sharp rise in the price of gold on the private market, (2) the significant improvement in the world market for some of our major export products, such as diamonds, wool, sugar and platinum, and (3) excellent agricultural crops.

As a result of the realignment of exchange rates, the rand value of imports did not decline exceptionally, but for the same reason, the export earnings in rand increased to new record levels, with the result that the trade balance showed a marked improvement and, with the capital inflow increasing, led to a substantial rise in the gold and other foreign reserves.

Improvement in current account

Although the deficit on the current account declined for five consecutive quarters, namely from the first quarter of 1971 to the second quarter of 1972, it still amounted to a relatively high figure of R499 million for the year that ended in June 1972. This deficit was, however, less than half the figure of R1 117 million for 1970/71. As the accompanying table shows, the progressive decline in the deficit over eighteen months was quite striking. The decline in the deficit resulted from lower imports, higher proceeds from both exports and net gold output and lower net invisible payments.

Balance of payments current account



Deficit on balance of payments current account
Seasonally adjusted annual rate — R millions

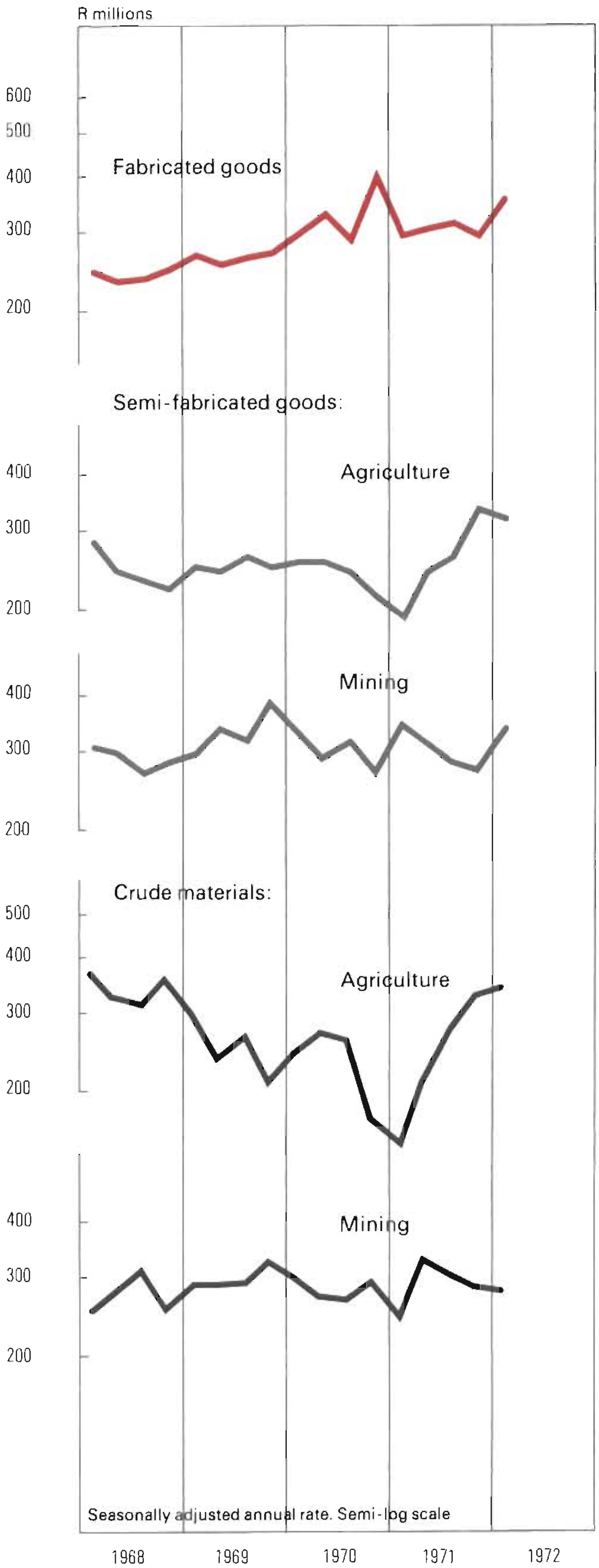
1971	1st qtr.	1 505
	2nd qtr.	897
	3rd qtr.	826
	4th qtr.	676
1972	1st qtr.	493
	2nd qtr.	8

It is important to note that an improvement in the current account had already occurred before the tightening of import control in November 1971 and the devaluation of the rand in December 1971.

Recovery of merchandise exports

As the accompanying table shows, exports recovered exceptionally well during the year that ended in June 1972, after declines had been registered

Merchandise exports according to stage of manufacturing



Merchandise exports

Year ended June	Amount R m	Percentage change
1970	1 465	— 2
1971	1 408	— 4
1972	1 804	+ 28

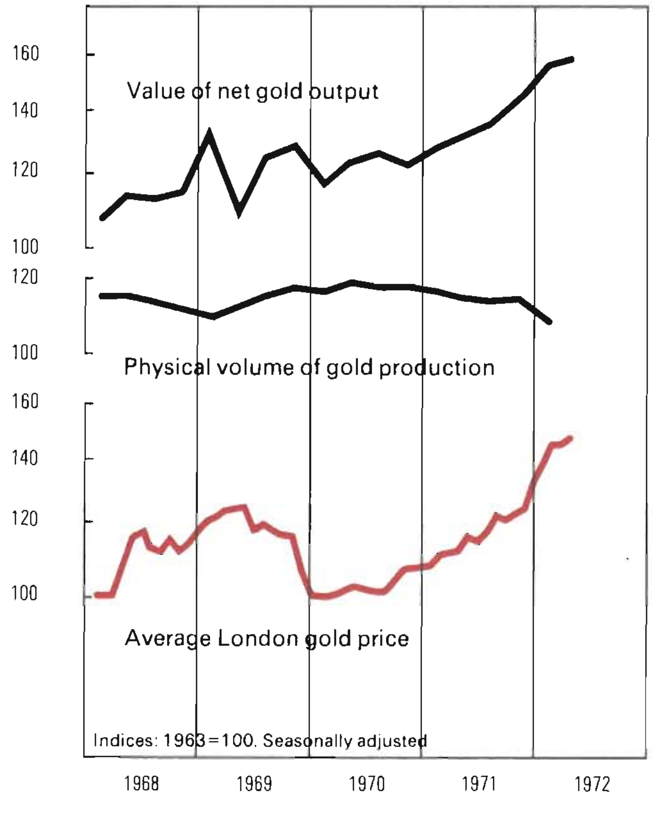
during the preceding two years. This sharp rise in exports was attributable *inter alia* to the realignment of exchange rates giving South Africa a higher rand value for some of its main export products, even in the cases where market prices remained unchanged. In addition to the gain from devaluation, the average world prices of some of the main export products showed a considerable improvement during the year under review. Examples of the improvement in export prices are given in the accompanying table. Apart from the marked increase in the prices of wool, copper and sugar, the prices of diamonds and fresh fruit also improved significantly.

Percentage change in export prices

	March 1970 to March 1971	March 1971 to March 1972
Wool	—21	+19
Copper....................	—24	+12
Sugar	—18	+57

With the exception of mineral products, increases were recorded in the value of almost all the main classes of goods exported during the year that ended in June 1972, but exceptionally large increases were shown in the exports of maize, sugar, diamonds, wool and base metals. If exports are classified by stage of production, raw materials and semi-manufactured goods originating from agriculture were mainly responsible for the sharp rise in merchandise exports during the year that ended in March 1972, although the exports of manufactured goods also showed a further increase. Raw materials and semi-manufactured goods originating from mining, on the other hand, did not increase during the year as a whole, but the latter rose sharply during the first quarter of 1972.

Net gold output



Substantial increase in net gold output

Owing to the sharp increase in the price of gold on the private market, the net gold output increased markedly and made a significant contribution to the improvement in the current account of the balance of payments, notwithstanding the fact that the physical volume of gold production declined by 5 per cent during the year that ended in June 1972.

Net gold output and change in average gold price

Year ended June	Net gold output: Amount, Kilograms '000	Net gold output: Amount, R m	Net gold output: Percentage change	Percentage increase in average gold price on London market
1971	104	868	3	1
1972	98	1 016	17	28

Declining tendency in merchandise imports

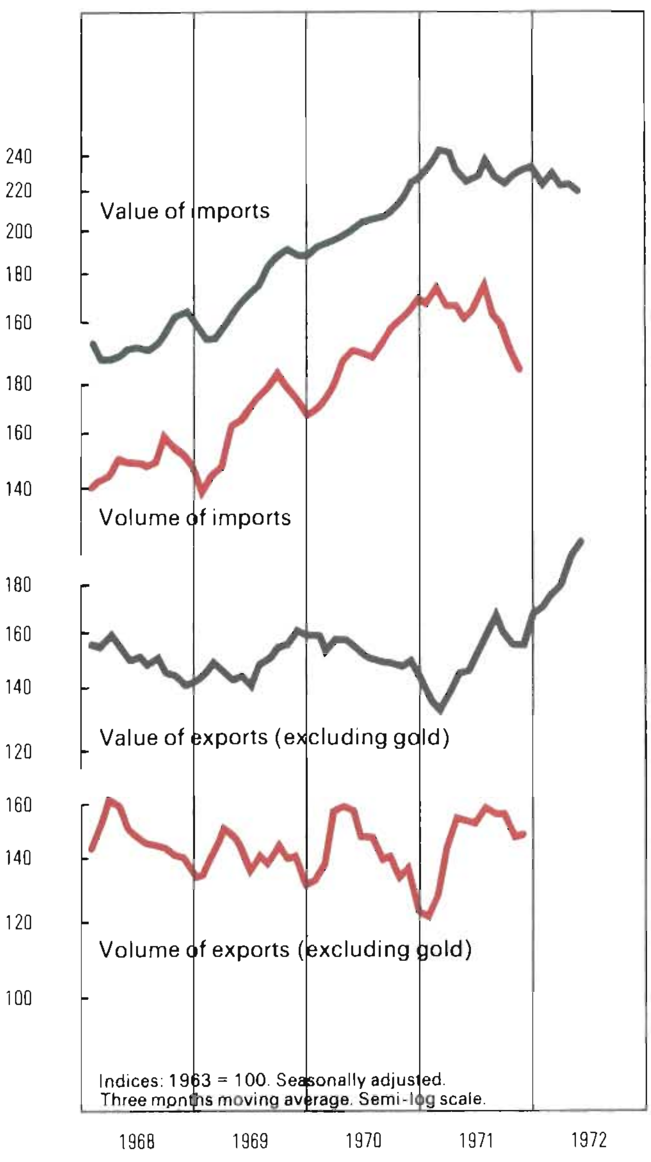
After rising sharply during 1969 and 1970 as a result of the strong upsurge in domestic expenditure, merchandise imports showed a moderate declining tendency from the beginning of 1971, i.e. for the eighteen months that ended in June 1972. As import control was only tightened in November 1971, it is clear that the change in the trend of imports did not come about solely as a result of import control, but rather coincided with the decline in the rate of increase in domestic spending. The strong upsurge in imports during 1969 and 1970 also came long after the substantial relaxation of import control in 1967. In July 1972 import control was relaxed and South Africa again, as in December 1969, decided to disinvoke Article XII of the General Agreement on Tariffs and Trade.

It is important to note that these tendencies in imports do not emerge clearly from comparisons of the years 1970/71 and 1971/72 as a whole. In fact, the import figures for the past two years were about the same, namely R2 807 million in 1970/71 and R2 820 million in 1971/72. This is clearly illustrated by the graph of imports which shows that during the first half of 1970/71 imports were still rising strongly, but a change of trend occurred from the beginning of 1971.

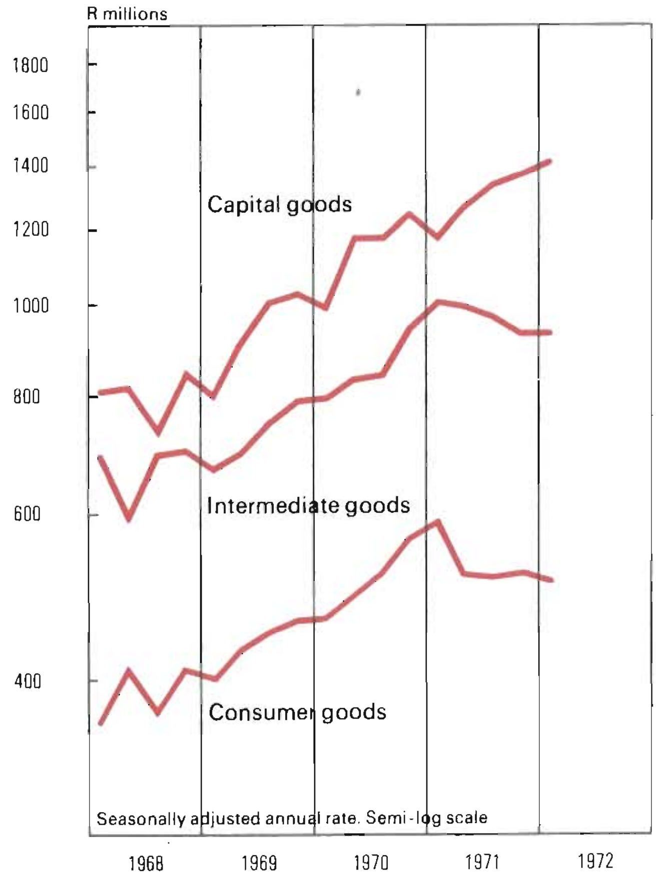
Another important feature not disclosed by the value of imports, is that imports measured in terms of rand did not show the same marked decline as the volume of imports. During the first half of 1972 this difference was much more pronounced because imports were measured in rand values, which had increased substantially as a result of the realignment of exchange rates. Although no figures are available for the volume and prices of imports after December 1971, the seasonally adjusted wholesale price index of imported goods rose by as much as 19 per cent at an annual rate during the six months that ended in June 1972.

The components of imports classified according to stage of use showed different tendencies during the year under review. The value of intermediate and consumer goods, constituting about 53 per cent of total imports, declined sharply from the end of the first quarter of 1971, but the value of capital goods continued to increase at a relatively high rate.

Merchandise imports and exports



Merchandise imports



Decline in net invisible payments

Net invisible payments to the rest of the world declined from R586 million in 1970/71 to R499 million in 1971/72, or by about 15 per cent. This net decline was brought about by a substantial decline in freight and merchandise insurance, associated with the lower volume of imports, and a smaller amount of dividends paid to foreigners. These two items declined more than the increases in interest payments resulting from the large capital inflow during recent years, larger tourist and transportation expenditure by South Africans abroad. Service and transfer receipts increased moderately.

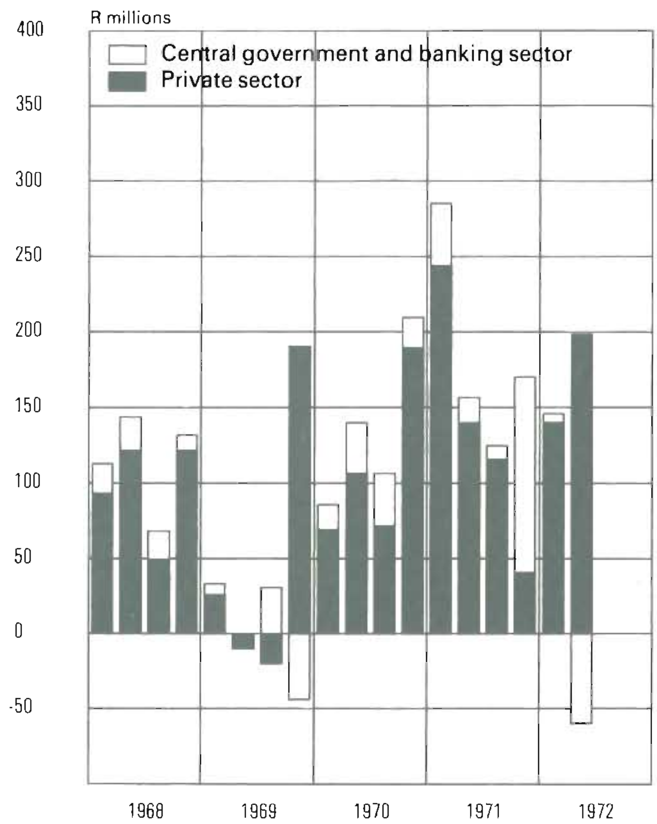
Further large net inflow of capital

From the end of June 1971 to the end of June 1972 a net inflow of capital of R578 million was recorded. Although this inflow was smaller than the record inflow of the previous year, it nevertheless contributed materially to the rise in the gold and other foreign reserves during the year under review. This was the seventh consecutive year that South Africa recorded a net inflow of capital.

The accompanying table shows, however, that the composition of the capital inflow changed considerably during the eighteen months that ended in June 1972. During the second half of 1971, the net inflow of capital to the private sector dropped substantially mainly as a result of the uncertainty about the ultimate level of the exchange rate of the rand, after it had been linked to the dollar in August 1971. The upward floating of the currencies of some of South Africa's important trading partners brought about leads in foreign capital payments and lags in foreign capital receipts and, therefore, caused a decline in the net inflow of capital. After the devaluation of the rand and the realignment of other exchange rates in terms of the Smithsonian agreement, these uncertainties disappeared and the net inflow of capital to the private sector increased again during the first half of 1972.

The sharp increase in the price of gold during the first half of 1972 coupled with the relaxation of the curbs on foreign investment by the United Kingdom in March 1972, contributed to a substantial rise in the net purchases by foreigners of securities listed on the Johannesburg Stock Exchange. These net purchases increased from R36 million in the second half of 1971 to no less than R121 million in the first half of 1972. On 23rd June 1972, however, the British Treasury introduced additional exchange control measures, including the requirement that purchases by U.K. residents of securities of Sterling Area countries would have to be made with exchange obtained at a premium from the so-called investment currency market.

Total capital movements



Net capital inflow
R millions

	1970 2nd half	1971 1st half	1971 2nd half	1972 1st half
Private sector	261	383	157	337
Net foreign purchases on the Johannesburg Stock Exchange	38	54	36	121
Long-term loans of public corporations and local authorities	77	75	78	54
Other, including errors and unrecorded transactions	146	254	43	162
Central government and banking sector	55	59	138	—54
Long-term loans of the central government	81	49	100	—21
Other	—26	10	38	—33
Total	316	442	295	283

Changes in the conditions prevailing in the domestic capital market also contributed to the change in the composition of the capital inflow. The tight conditions in the domestic capital market, together with the deterioration in the overall balance of payments, led to the relatively large inflow of capital to the central government and banking sector as well as to local authorities and public corporations during 1970 and 1971. In the first six months of 1972 the domestic market for fixed-interest securities eased significantly, with the result that the government was able to make net repayments of R21 million on its foreign loan commitments during this period. A corresponding decline in the amount of net foreign long-term loans obtained by public corporations and local authorities was also noticeable during the first six months of 1972.

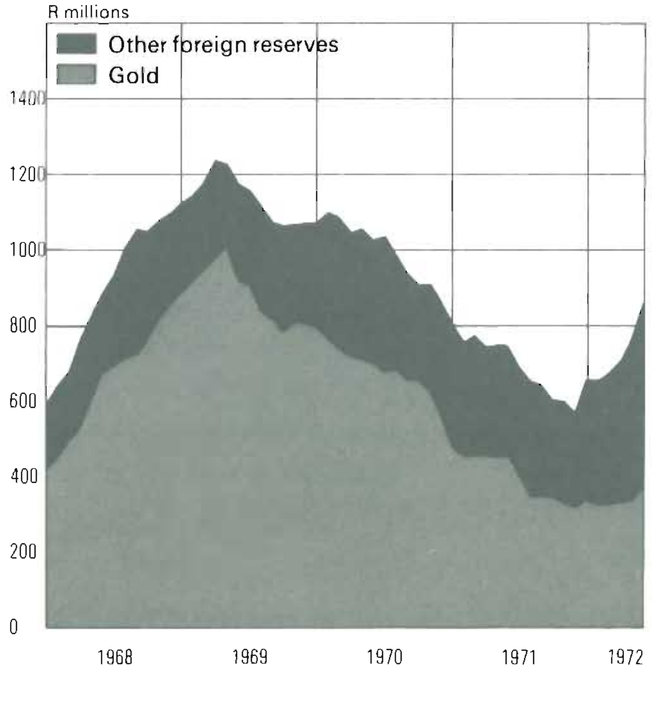
Sharp upturn in gold and other foreign reserves

The substantial improvement in the deficit on the current account and the large net capital inflow from abroad, resulted in an increase of R79 million in the gold and other foreign reserves during 1971/72, compared with a decline of R359 million in 1970/71. The reserves were further augmented by South Africa's share in the third allocation of special drawing rights in January amounting to R28 million, and by an exchange profit of R66 million in December owing to the realignment of exchange rates. During the year that ended in June 1972 the gold and other foreign reserves, therefore, increased by R173 million to a level of R864 million. In July the gold and other foreign reserve holdings of the Reserve Bank increased by a further R91 million to reach a figure of R823 million.

According to the month-end figures on the accompanying graph the gold and other foreign reserves showed an uninterrupted downward trend from March 1969 to November 1971, followed by a sustained rise during each of the subsequent months. In the months immediately before the realignment of exchange rates in December 1971, the gold and other foreign reserves would have declined more sharply if the net inflow of capital to the central government and banking sector had not risen so rapidly. However, during the first six months of 1972 the central government and banking sector was able to make net repayments on foreign loans and the foreign borrowing by public corporations declined, but at the same time the gold and other foreign reserves still increased substantially.

During 1971/72 the gold and other foreign reserve holdings of the Reserve Bank increased by R162 million, and that of the central government by R31 million. The monetary banking institutions' foreign exchange holdings, on the other hand, declined slightly over the relevant period. From the end of February 1972 the gold holdings of the Reserve Bank have increased progressively because the sharp rise in the total reserves made it unnecessary for the Bank to sell the total gold production on the private market. At the end of July 1972 the gold holdings amounted to 49 per cent of the total gold and other foreign reserves of the Reserve Bank.

Gold and other foreign reserves



Monetary and banking situation

Easier monetary and banking conditions

Although the quantity of money and near-money increased at only a fairly moderate rate during the year that ended in June 1972, the rate of increase accelerated significantly during the first half of 1972, mainly as a result of the substantial increase in the gold and other foreign reserves after the devaluation of the rand in December 1971. Money market interest rates, which had increased to very high levels during the second half of 1971, declined sharply during the first half of 1972, particularly after March 1972. In view of the relatively high rate of inflation, the authorities continued to pursue a cautious monetary policy which included relaxations of the credit ceilings at the end of March 1972 and a reduction of $\frac{1}{2}$ per cent in the Bank rate and of $\frac{1}{4}$ per cent in the pattern of rates quoted for transactions in government stock, as from 10th August 1972.

Ratio of money and near-money to gross domestic product

Fairly moderate rate of increase in money and near-money

During the twelve months that ended in June 1972, the quantity of money and near-money increased at a higher rate than during the previous year, but, as the accompanying table shows, the rates of increase during the past two years were still substantially lower than during the three-year period from 1967/68 to 1969/70. However, a marked acceleration in the rate of increase was noticeable in the course of the year 1971/72. Whereas the seasonally adjusted annual rate of increase was somewhat less than 5 per cent during the second half of 1971, it rose to almost 11 per cent during the first half of 1972. On balance, the monthly average quantity of money and near-money for the twelve months that ended in June 1972 exceeded the 1970/71 figure by approximately 6,5 per cent.

At these rates, the increase in money and near-money was, however, still significantly less than the rate of growth in the gross domestic product at current prices. The ratio of the average quantity of money and near-money to the gross domestic product accordingly decreased further from 30,6 per cent in 1970/71 to 29,2 per cent in 1971/72. Seasonally adjusted, the ratio declined from 29,6 per cent in the third quarter of 1971 to 28,5 per cent in the second quarter of 1972, the lowest level since the first quarter of 1968. Over a somewhat longer term, this ratio has shown a generally downward trend from the record level of about 32 per cent that had been reached in the first quarter of 1969.

Increases in money and near-money

Year ended June	%
1967	6
1968	13
1969	15
1970	13
1971	5
1972	8

Causes of changes in money and near-money

The rather higher rate of increase of money and near-money during 1971/72, as compared with 1970/71, was largely the result of the drastic reversal of the trend in the net gold and other foreign reserves subsequent to the devaluation of the rand. The net gold and other foreign reserves contributed R137 million to the money and near-money supply, as against their decline of R360 million during the preceding year. During 1971/72 the rise in domestic credit extension, i.e. the monetary banking sector's

Causes of changes in money and near-money

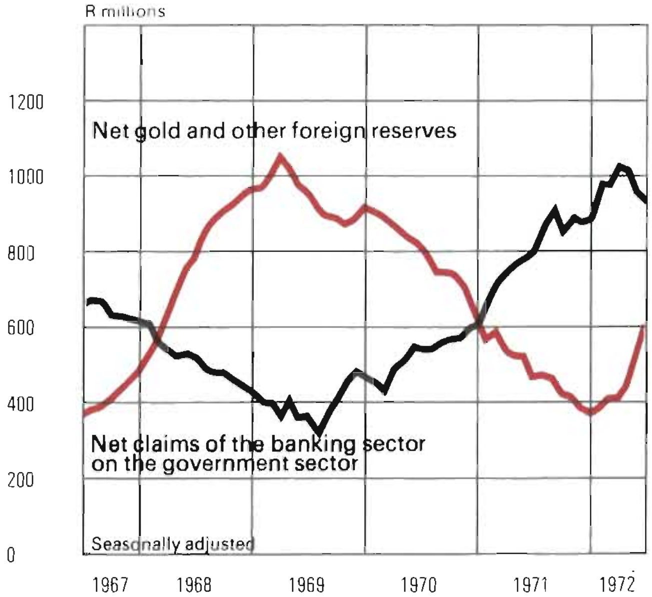
Not seasonally adjusted – R millions

	Year ended June 1971	1972
Net gold and foreign reserves	—360	137
Claims on government:		
Claims	96	234
Deposits (Increase—, decrease+)	174	—101
Net claims	270	133
Claims on private sector	314	243
Long-term private deposits (Increase—, decrease +)	—90	—159
Net other liabilities and assets	51	—25
Total money and near-money	**185**	**329**

credit to the private sector plus its net credit to the government sector, was over R200 million less than during the previous year. At the same time, the increase in long-term deposits of the private sector with the banking sector reduced the money supply during 1971/72 by substantially more than during 1970/71.

The figures for the year 1971/72 as a whole, however, do not clearly reveal the marked shifts that occurred in the pattern of the causes of changes in money and near-money in the course of the year. The continuing rapid decline in the net gold and other foreign reserves during the second half of 1971 was reversed into a sharp rise during the first half of 1972. Long-term deposits of the private sector with the banking sector, which had shown little change during the last six months of 1971, increased substantially during the first six months of 1972, thereby slowing down the rate of increase in money and near-money. Total bank credit to the private and government sectors continued to rise rapidly during the first nine months of the year under review. During the second quarter of 1972, however, the net claims of the banking sector on the government sector, seasonally adjusted, decreased by nearly R100 million, while claims on the private sector showed only a small further increase.

Relationship between foreign reserves and bank credit to government sector



Inverse relationship between changes in net foreign reserves and net claims of the banking sector on the government sector

There was further evidence during the year under review of the rather close negative correlation which in recent years would appear to have existed in the South African economy between changes in the net gold and other foreign reserves, on the one hand, and in net banking sector claims on the government sector, on the other. This apparent inverse correlation has been particularly marked since approximately the middle of 1967. In terms of this relationship, a change in direction of the movement in the net gold and other foreign reserves tends to be followed, with a lag of several months, by an opposite change in net bank credit to the government sector. Thus, the decline in the net foreign reserves from April 1969 preceded a rise in the level of net banking sector claims on the government sector from August 1969. Changes in the opposite directions have since occurred in both quantities, the rise in the net foreign reserves after devaluation having been followed by a decline in net claims on the government sector since April 1972.

Although this inverse relationship cannot be expected to exist under all circumstances, there are a number of economic forces that will normally tend to work in the direction of establishing such an inverse relationship. When a rise in the foreign reserves leads to an increase in the money supply, this facilitates borrowing by the government from the private non-banking sector and therefore helps the government to reduce its net indebtedness to the banking sector. This will be even more true when an increase in the net foreign reserves also gives rise, as it did during the second quarter of 1972, to expectations of a future decline in interest rates. Another reason for the above-mentioned negative correlation between changes in the net foreign reserves and in bank credit to the government sector is the relationship between government spending and imports. A reduction in total government spending, and therefore in its borrowing requirements, naturally results in lower imports by the government and may lead to an improvement in the balance of payments that may help to increase the net foreign reserves.

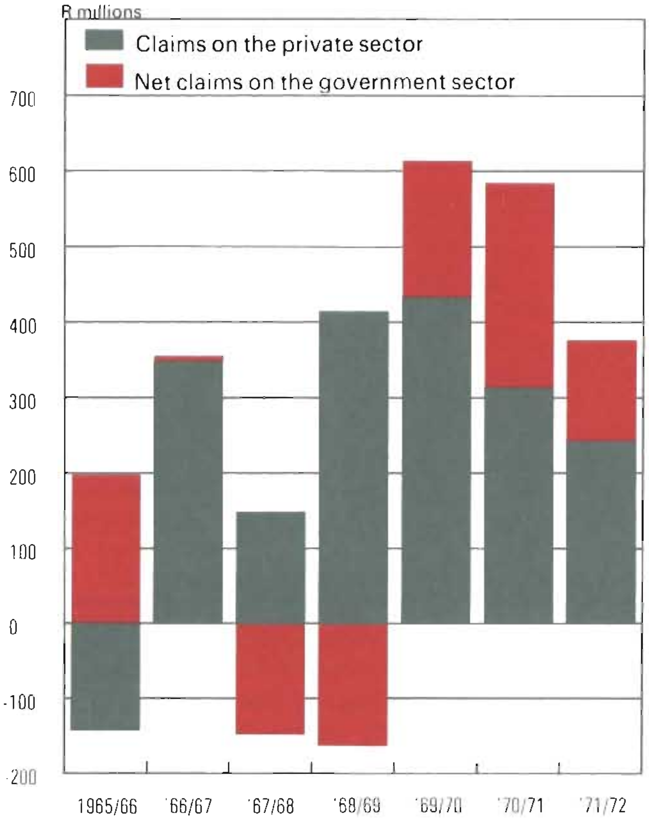
Reduced increase in total bank credit extension

As the accompanying table shows, total domestic credit extension increased at progressively lower rates during the past three years. During 1970/71 credit to the private and the government sector made roughly equal contributions to the total increase in domestic credit extension, but during 1971/72 the marked decline in net bank credit to the government sector from April 1972 onwards, made the government's contribution to the total increase in bank credit considerably smaller than that of the

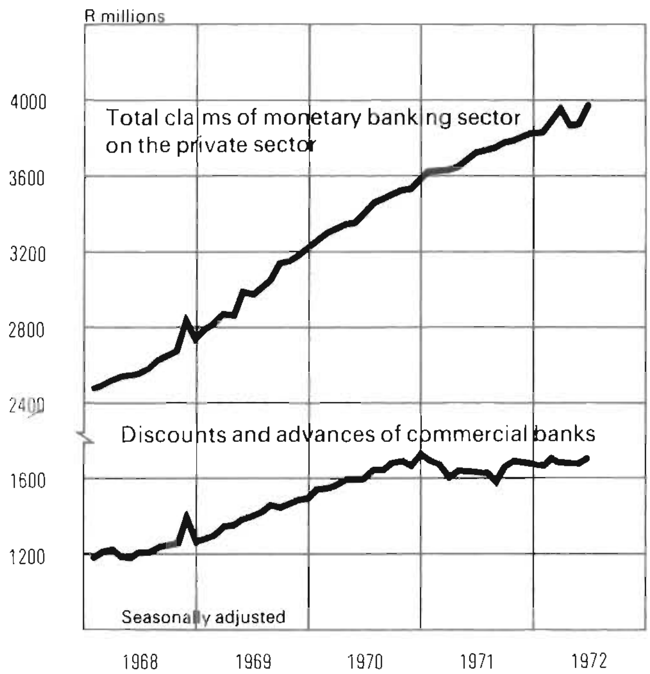
Changes in bank credit extension

Year ended June	To private sector	To government sector	Total Amount	Total Percentage increase
	R m	R m	R m	
1970	432	182	614	18,3
1971	314	270	584	14,7
1972	243	133	376	8,2

Changes in domestic credit extended by the monetary banking sector



Bank credit to the private sector



private sector. In both cases, the increase in credit extended was notably smaller than during 1970/71.

The increase in the net claims on the government sector (net bank credit to the government sector) during 1971/72 was more than fully accounted for by the substantially increased holdings of government securities by the banking sector, in particular the commercial banks, merchant banks and monetary hire-purchase and general banks. This was in contrast to the preceding two years, during which the increase in bank credit to the government sector consisted largely of a decline in government deposits. During 1971/72 the banking sector's holdings of government securities and other forms of lending to the government increased by R234 million and this more than offset the increase of R101 million in government deposits, resulting in an increase in the *net* claims on the government sector of R133 million.

Change in bank credit to the private sector

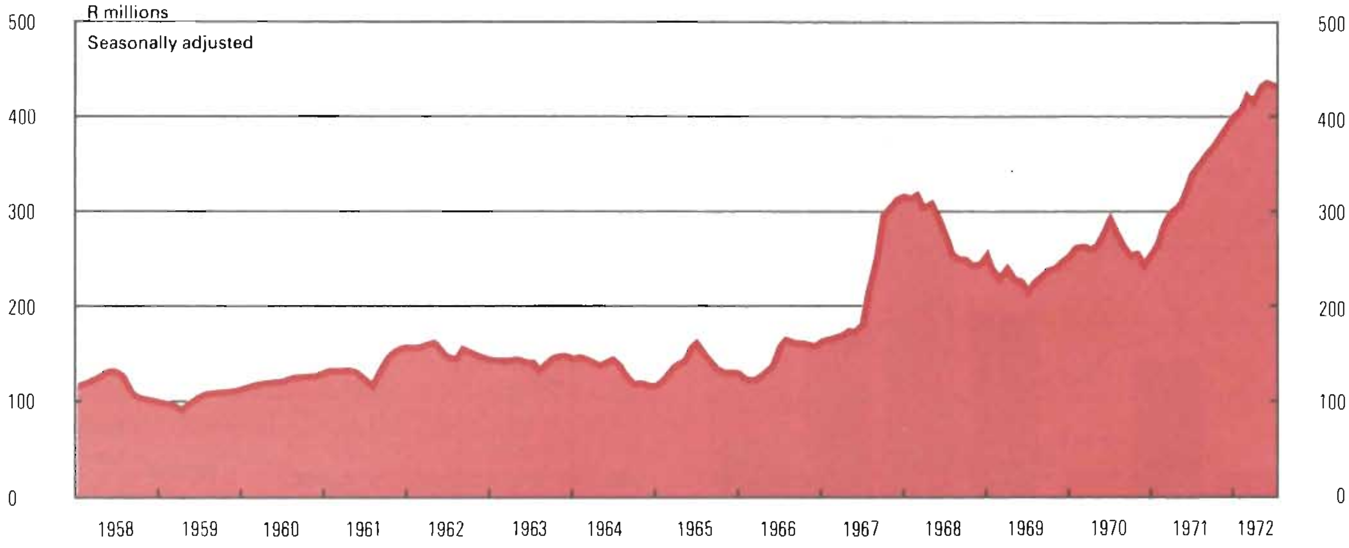
Year ended June	Percentage increase
1969	16
1970	15
1971	9
1972	7

The other, and in quantitative terms by far the more important component of domestic credit extension, namely bank credit to the private sector, increased substantially less during 1971/72 than during the preceding year. It has, in fact, increased at much lower rates during the past two years than during the preceding two years.

A relatively large part of the rise in bank credit to the private sector during 1971/72 was in the form of short-term credit extended by the Land Bank to agricultural co-operatives, control boards and farmers. This credit item contributed 40 per cent to the total increase in bank credit to the private sector. Moreover, as the accompanying graph shows, Land Bank cash credit advances increased substantially from 1967 and, apart from seasonal fluctuations, showed a marked upward trend. There are a number of reasons for this development, such as (1) the faster growth in agricultural production in recent years, (2) higher ratios of agricultural stocks to agricultural production, and (3) the extension of short-term credit by the Land Bank to borrowers previously accommodated elsewhere.

When the rise in cash credit advances of the Land Bank is excluded, total claims on the private sector during 1971/72 increased by only R145 million, i.e. by little more than half the amount of the increase in these claims during 1970/71. A substantial proportion of the increase during 1971/72 was, moreover, accounted for by increased investments in securities of the private sector by the commercial banks and, more particularly, by the merchant banks and monetary hire-purchase and general banks, rather than

Cash credit advances of the Land Bank



by a higher level of the banks' discounts and advances. The discount houses actually reduced their total claims on the private sector, mainly in the form of their holdings of bankers' acceptances, by over R50 million. This was partly the result of a deliberate attempt by the houses to reduce their total asset portfolios, in order to decrease their borrowing from the Reserve Bank as an almost permanent source of funds.

The discounts and advances of the commercial banks, not adjusted for a slight increase in net remittances in transit, rose by the fairly modest amount of R75 million during the year. This relatively small increase may be attributed partly to the limited scope available for the extension of credit under the ceilings during the larger part of the year under review. Not only were the credit ceilings applied more strictly and effectively from March 1971 by subjecting any excess over the ceiling to a penalty in the form of additional cash balances with the Reserve Bank, but they were kept unchanged during the year until the end of March 1972. However, fairly substantial increases in the ceilings applicable to all banking institutions were announced on 29th March 1972, in conjunction with other expansionary measures contained in the 1972/73 Budget. All banking institutions were given a concession to exceed the ceilings on their discounts and advances by 5 per cent and that on their investments by 10 per cent, both concessions to be used for the purpose of extending new credit for production and exports. The banks were also allowed to combine the two concessions, that is, to use them interchangeably. Even after these concessions had been granted, however, bank credit did not increase sharply, probably because of a lack of demand for credit associated with the reduced rate of economic activity and the high level of interest rates and the apparent shift to foreign sources for the financing of foreign trade.

Bank liquidity

During the twelve months that ended in June 1972 the monetary banks' excess liquid asset ratio increased slightly from the relatively low level that had been reached in 1970/71. As the accompanying table shows, the average monthly ratio of excess liquid assets to liabilities to the public remained between 3 and 4 per cent during the past three years, but this ratio was considerably lower than that attained in 1968/69.

Although the excess liquid asset ratio increased only slightly during the period under review, the average actual liquid asset holdings of the monetary banks as at month-ends exceeded the 1970/71 figure by well over R100 million. The largely offsetting influences of declines in government deposits and net gold and other foreign reserves helped to ensure a fairly stable level of the banks' liquid asset holdings during the second half of 1971. In the same way, the substantial increase in the gold and other

Average surplus liquid asset ratio of commercial banks, merchant banks and monetary hire-purchase and general banks

Year ended June	%
1969	8,3
1970	4,0
1971	3,2
1972	3,8

foreign reserves after devaluation tended to ease the normal tightening of bank liquidity during the first three months of 1972 and helped to increase the average excess ratio for the year as a whole.

Marked changes in short-term interest rates

The reversal in the trend of the gold and other foreign reserves in December 1971 also led to a pronounced change in money market conditions and to marked changes in short-term interest rates. During the second half of 1971, and more specifically from the end of August 1971, money market conditions tightened considerably and short-term interest rates increased sharply, mainly owing to the decline in the gold and other foreign reserves and the lower level of call deposits of commercial banks with the discount houses. Rates quoted on 90-day NCDs, for example, rose by about 2 per cent during this period, to reach a level of 8,7 per cent at the end of 1971. The Treasury bill tender rate also moved upwards from 5,42 per cent at the end of August to 5,96 per cent at the end of 1971.

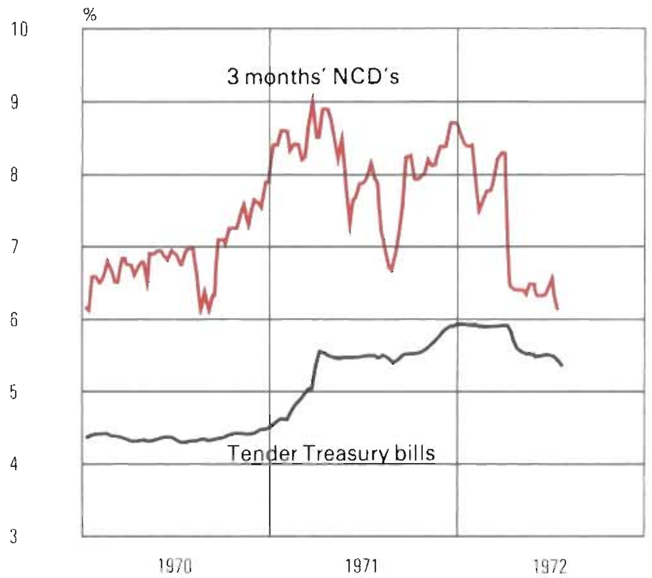
After the devaluation, money market conditions eased considerably and short-term interest rates dropped sharply as a result of the rapid and sustained rise in the gold and other foreign reserves. The decline in short-term interest rates was the most pronounced in the six-week period from the end of March to the middle of May 1972, when the easing effect of a decline in government deposits was added to the effect of the sharp rise in the gold and other foreign reserves. From the middle of May 1972, money market conditions became more stable as a result of a return flow of funds from the private sector to the government sector, mainly as a result of the very successful flotation of two government stock issues.

The drop in short-term interest rates during the first half of 1972 was even more pronounced than the increase during the second half of 1971. The rate on 90-day NCDs in the secondary market, for example, declined by just over 2 per cent to a level of 6,65 per cent on 30th June 1972. The Treasury bill tender rate also moved downwards during the first six months of 1972 by nearly $\frac{1}{2}$ per cent to 5,53 per cent at the end of June 1972. The yield on 3-year maturity government stock issued during May and June 1972 was lowered from $6\frac{1}{2}$ per cent to $6\frac{1}{4}$ per cent. On 10th August 1972 the Reserve Bank reduced the Bank rate by $\frac{1}{2}$ per cent to 6 per cent and adjusted the pattern of rates quoted for transactions in government stock, downwards by $\frac{1}{4}$ per cent.

Imposition of deposit interest rate control

Contrary to the marked changes in money market rates, deposit interest rates were relatively stable throughout the year under review. However, when a relaxation of the credit ceilings was announced on 29th March 1972 as part of a package of measures directed at stimulating economic growth, the Reserve Bank as from 30th March also instituted interest rate control in respect of the rates quoted on deposits by banks and building societies. The reasons for the introduction of this control are given below. The maximum rates laid down by the Bank were fixed at 6 per cent in respect of deposits of less than six months (including savings deposits and call loans), $6\frac{3}{4}$ per cent on deposits of six months or longer but less than twelve months, and $7\frac{1}{2}$ per cent on deposits of twelve months or longer. These maximum rates corresponded closely to the rates that had been quoted by the banks and the building societies at the time.

Short-term interest rates



Government finance

Smaller increase in government expenditure and larger current surplus

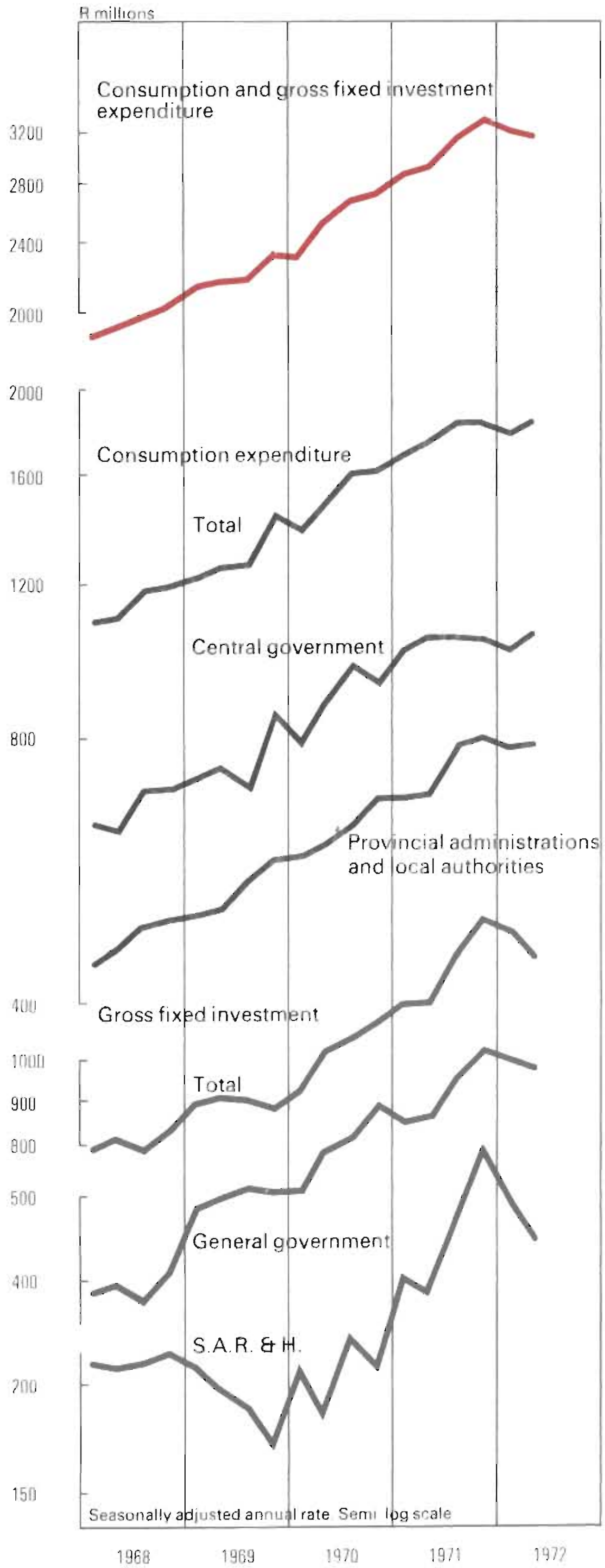
The public authorities, i.e. the central, provincial and local authorities, succeeded in changing considerably the trend in their current as well as capital expenditure during the year that ended in June 1972, particularly during the first six months of 1972. Although the total of these authorities' current and capital expenditure continued to increase sharply during the second half of 1971, actual reductions were recorded during the first two quarters of 1972. The result was that the increase in the total expenditure was well below the level attained during 1970/71.

A breakdown of expenditure by these authorities reveals that consumption expenditure contributed most to the lower rate of increase during 1971/72. This component of the expenditure of public authorities rose by only 9 per cent during the year that ended in June 1972, as against a rise of 20 per cent during the preceding year. Considering only the central government, the rate of increase in expenditure declined from 22 per cent in 1970/71 to only 5 per cent in 1971/72. An important reason for this reduction was the fact that salary and wage scales of the civil service were kept virtually unchanged during the past year. This not only contributed much to the reduction in aggregate demand, but also to avoiding a strong upward movement in salaries and wages generally, a development which would have aggravated substantially the inflationary pressures during the past year. Fixed investment also declined markedly during the first half of 1972, but the very high rate of increase recorded during the second half of 1971 resulted in an increase of 24 per cent in this type of expenditure for the year as a whole. About 60 per cent of the fixed capital outlays was on infrastructural development, a large part of which represented capital outlays by the S.A. Railways.

Although subsidies and current transfers to households are relatively smaller than consumption and investment expenditure, they also have an indirect influence on aggregate demand. Subsidies, of which those in respect of agricultural products accounted for about 60 per cent, increased by about 7 per cent during the year under review or substantially less than the increase of more than 32 per cent during 1970/71. Current transfers to households, on the other hand, accelerated their upward trend and rose by a further 17 per cent.

In addition to the smaller rate of increase in the current expenditure of public authorities, current revenue, largely in the form of tax receipts, rose at a higher rate. Consequently, the surplus of current income over current expenditure increased markedly, namely from R353 million in 1970/71 to R427 million in 1971/72, or by 21 per cent. Although a larger surplus was, therefore, available for the financing of capital expenditure, a substantial overall deficit remained to be financed through borrowing. As the central government also borrows on behalf of government enterprises, notably the S.A. Railways

Public authorities



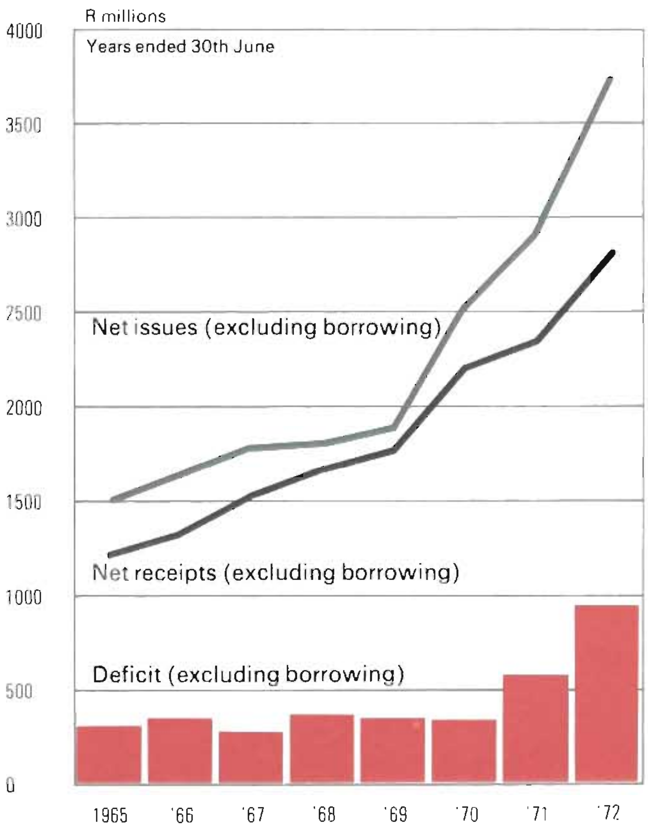
and the Post Office, and the provincial administrations, the borrowing operations of the public authorities are to a large extent reflected in the Exchequer Account.

Large Exchequer deficit, but improved financing operations

Total Exchequer issues (excluding redemptions of stock) exceeded total receipts (excluding borrowing) by a substantial amount during the year that ended in June 1972, namely by R933 million, compared with R563 million for the preceding twelve months.

In the tight capital market situation, which had prevailed during the first nine months of the period under review, the government found it extremely difficult to borrow on a voluntary basis from sources outside the banking system. Various steps were taken, therefore, to limit the extent to which bank credit had to be used to finance the Exchequer's large deficit. Loan levies were increased, attractive tax-free bonds were made available to individuals, the yield on government stock was raised and the compulsory amount to be invested by insurers and pension funds in government securities was increased. From about April 1972, however, the market for fixed interest securities in general improved and expectations of a decline in long-term interest rates arose. Under these circumstances, the government

Exchequer account



succeeded in converting stock maturing in May 1972 as well as in raising new money through the issuing of stock offered for subscription from 15th May to 15th June 1972. Two stocks were issued, a 3-year maturity at a yield of $6\frac{1}{4}$ per cent ($\frac{1}{4}$ per cent lower than that on the previous issue), and a 25-year maturity at a yield of $8\frac{1}{2}$ per cent (unchanged since 31st March 1971).

As the accompanying table shows, the two new issues not only attracted applications of a substantial amount, but the issues were also well supported by insurers and pension funds and other private non-banking investors. The R183 million contributed by the private non-banking sector exceeded the amount that had to be borrowed, in accordance with the Budget proposals, through stock issues during the whole fiscal year 1972/73.

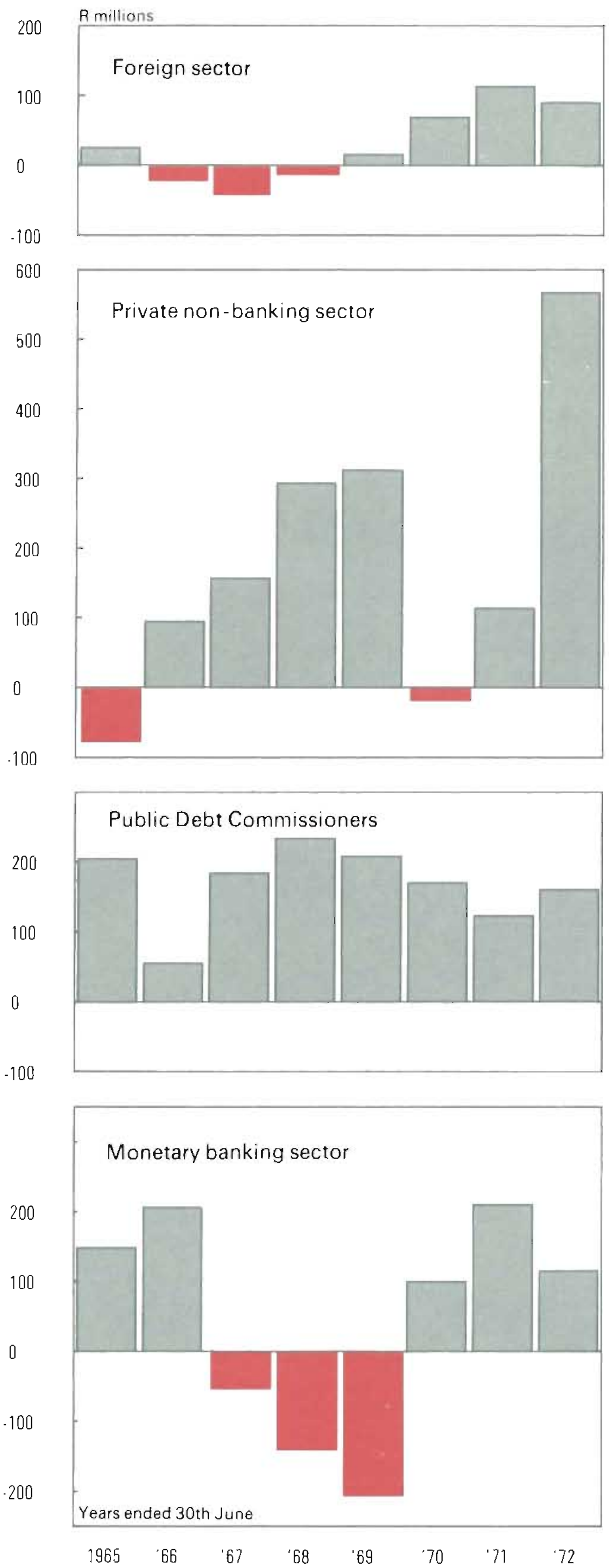
Cash applications for new stock issues, May/June 1972
R millions

	$6\frac{1}{4}$% 1975	$8\frac{1}{2}$% 1997	Total
Public Debt Commissioners	—	80	80
Monetary banking sector	124	102	226
Insurers, pension and provident funds	—	108	108
Others	29	46	75
Total	153	336	489

With the improved market situation and taking into account the various forms of compulsory loans, the government succeeded in borrowing a net amount of R567 million from the private non-banking sector during the twelve months that ended in June 1972, compared with a net amount of only R115 million during the preceding twelve months. The largest part of the former figure was raised through the stock issues in May and June, but R142 million was also borrowed in the form of loan levies and R63 million through issues of tax-free Premium Bonds.

During 1971/72 the Exchequer also borrowed a substantial amount abroad, namely R90 million, compared with an even higher amount of R114 million during the preceding twelve months. Foreign borrowing relieves the pressure on domestic financial markets and at the same time assists the balance of payments, but may, of course, also increase the money supply through an increase in foreign reserves and in this way increase the liquidity of the private sector. During the past three years the Treasury financed on average about 15 per cent of the Exchequer deficit through foreign borrowing. Nevertheless, at the end of June 1972 the total foreign debt accounted for less than 6 per cent of South Africa's total government debt, after taking into account the higher repayment values of foreign debt in rand as a result of realignments of exchange rates in December 1971. This percentage is still well below the levels in countries with which South Africa may reasonably be compared.

Exchequer financing
Change in net debtedness to



The Public Debt Commissioners, an important source of funds for the Exchequer, contributed less to the financing of the Exchequer deficit during recent years, mainly because of the withdrawal of funds by the S.A. Railways, the Post Office and the provincial administrations. During the year that ended in June 1972 the Public Debt Commissioner's net investment in government securities amounted to R160 million, whereas comparable figures for 1969/70 and 1970/71 were R170 million and R123 million, respectively. When institutions such as the S.A. Railways use their accrued internal funds to finance capital outlays, they do not necessarily help to reduce the Exchequer's borrowing requirements because the utilisation of internal funds, usually deposited with the Public Debt Commissioners, will lead to a corresponding reduction in the contribution of the Public Debt Commissioners to Exchequer financing.

Borrowing by the Treasury from the Public Debt Commissioners, the foreign sector and other non-banking sources together amounted to R817 million, or nearly 88 per cent of the Exchequer deficit. Hence the Treasury was obliged, as during the preceding two years, to make use of bank credit to finance the shortfall. The Exchequer's net indebtedness to the banking sector accordingly increased by R116 million during the period under review. However, the figure was R94 million lower than the increase in 1970/71, and if, in addition, account is taken of the substantial increase in the Exchequer deficit, it means that the relative importance of the monetary banking sector as a source of finance declined markedly, namely from 37 per cent in 1970/71 to only 12 per cent during the period under review.

It is also of interest to note that, whereas the increased net indebtedness during the preceding two years was mainly in the form of a decline in deposits, deposits rose by R132 million during the past year and was accompanied by a substantial increase of R248 million in the banking sector's holdings of government securities. After reaching a record level of R717 million at the end of July 1969, the Exchequer balance declined to R319 million on 30th June 1971 and then rose to R450 million on 30th June 1972, including R161 million on the Stabilization Account. This rise was largely the result of the substantial investment in government securities during May and June 1972. The Exchequer's cash balance actually declined during the larger part of the period under review, but the decrease was more than neutralised by the rise of R224 million in deposits during May and June 1972. Investments in government securities by the banking sector likewise rose by only R58 million between 30th June 1971 and 30th April 1972, but by a further R190 million during May and June 1972.

The 1972/73 Budget

In the 1972/73 Budget, which was presented to Parliament on 29th March 1972, the Minister of Finance attempted by various budget proposals to attain certain objectives, namely the improvement of the balance of payments, a more rapid rate of economic growth and the curbing of inflation. Under existing conditions and in the short run, these objectives were to some extent inevitably of a conflicting nature, but it was hoped that the measures proposed would furnish a sound basis for stable economic growth.

The Minister pointed out that it is of the utmost importance that growth should not be stimulated to such an extent that it would cause undue pressure on labour and capital resources. He also stressed that with only a moderate easing of the labour and capital markets and with limited excess plant capacity, "a hasty, reckless dash for growth at any cost" could lead to price increases that exceed those of South Africa's trading partners, a development that would reduce or eliminate the advantages to be gained from the realignment of exchange rates. A co-ordinated and balanced programme of action was necessary. The measures announced by the Minister were, therefore, aimed at a *moderate* stimulation of the economy, a reduction in the high rate of increase in state spending and the soundest possible financing of the Exchequer's overall deficit.

At the same time the tax system had to be revised so as to remove unnecessary disincentives to productivity and to promote production and exports wherever possible. In this regard tax incentives for exporters were increased and investment allowances in respect of machinery, plant and factory buildings were extended to 1975. The Minister also announced the relaxation of building control and credit restrictions on the sale of motor cars. In addition, savings were promoted, *inter alia,* by the introduction of a new home-owners saving scheme as well as by the reduction in the combined maximum marginal income tax and loan levy rate for individuals. Loan levies on individuals were in fact abolished and replaced by an additional surcharge on income tax. Sales duties on certain items were reduced and the cash position of companies was improved through a reduction in the loan levy on dividends received. The Minister also increased social pensions and granted further concessions in respect of earnings of married women.

The Minister succeeded in reducing substantially the proposed rate of growth in government expenditure, particularly on services which do not contribute directly to the economic infrastructure, and the Budget actually provided for an increase of only 6 per cent in total expenditure, compared with the fiscal year 1971/72. During the latter year expenditure rose by about 19 per cent. Total revenue was expected to increase by about 7 per cent and the Budget deficit was estimated at R798 million, or marginally below the Exchequer deficit during the fiscal year 1971/72. It was not expected that this shortfall could be covered completely by domestic and foreign borrowing and the Minister proposed to make use of R161 million still available on the Stabilization Account and to employ a further R18 million of the cash balances available on the Exchequer Account.

The emphasis of the Budget was, therefore, on stimulating growth to the extent that the available labour and capital resources could be put to optimum use without undue pressure being exerted on these resources. A too strong expansionary programme would soon have led to more inflation and thus to the disappearance of any advantages to be gained from the realignment of exchange rates.

Capital market

Significant changes in the capital market

During the course of the twelve months that ended in June 1972, significant changes occurred in the capital market. In November 1971 prices and activity in the share market reached the lowest levels recorded after the 1969 boom, but showed a sharp upturn from December, particularly as far as activity is concerned. The market for fixed-interest securities also eased somewhat during the second quarter of 1972, after it had been particularly tight for more than two years. Deposit-receiving institutions in general received more longer-term funds and in the case of building societies the inflow of funds improved substantially during the second quarter of 1972. The property market, however, remained less buoyant than during the boom of 1968 to 1970.

Interest rate control

On 30th March 1972 the Reserve Bank instituted interest rate control on deposits and building society shares. The purpose of the control was to avoid unjustified increases in deposit interest rates that might have resulted from keener competition created among banking institutions as a result of the relaxation of credit control. It was also taken into account that such competition might either leave the building societies unduly short of funds or have the equally undesirable effect, under the prevailing circumstances, of inducing them to increase their mortgage rates so as to be able to offer more competitive rates on deposits and shares. It was felt at the time that any downward tendency in interest rates which could develop, particularly if the balance of payments should continue to show a surplus, should not be counteracted by a contrary movement in deposit interest rates.

In addition to the maximum rates referred to earlier, the following maximum rates were fixed for building society shares:

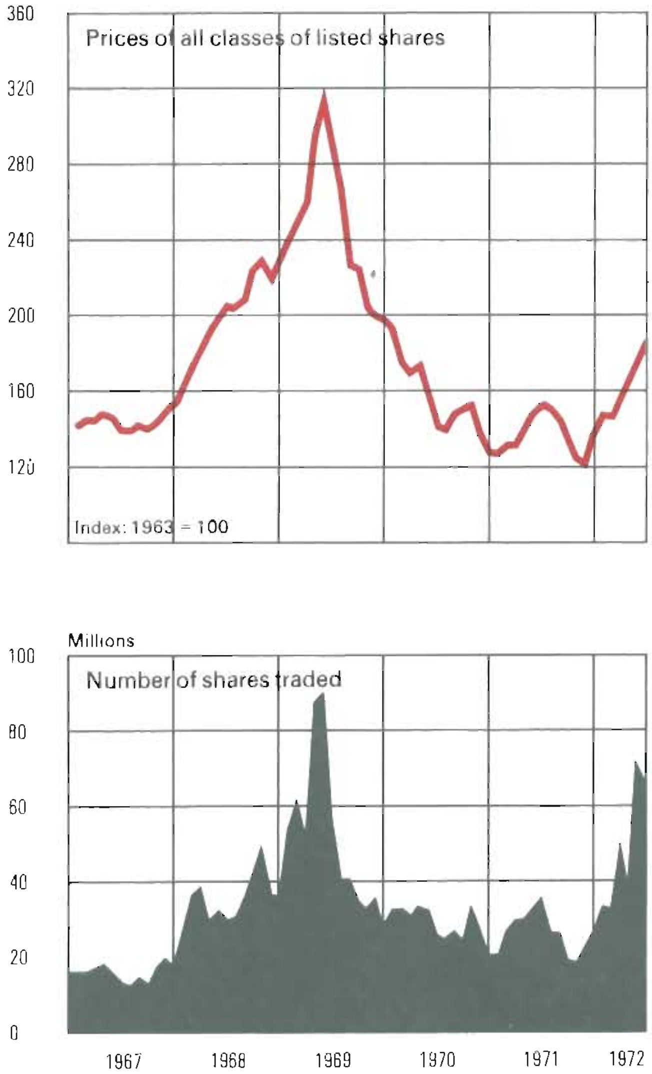
Subscription shares:	$6\frac{1}{2}$ per cent
Paid-up indefinite-period shares (excluding tax-free shares) and fixed-period shares:	$7\frac{3}{4}$ per cent
Fixed-period shares with a guaranteed dividend in terms of Section 37 (5A) of the Building Societies Act:	8 per cent

Accompanying the introduction of maximum interest rates for deposits and building society shares, certain related interest rates were also subjected to a maximum by the Registrar of Financial Institutions, in terms of a Proclamation issued under the Currency and Exchanges Act of 1933. A maximum interest rate of $8\frac{1}{2}$ per cent was imposed on funds raised under participation mortgage bond schemes and this maximum was also made applicable to money raised in the form of deposits, loans or debentures by "financial intermediaries" other than banks and building societies.

Strong upswing in share market

Significant fluctuations in prices and turnover on the stock exchange occurred during the period under review. Following a recovery in the first half of 1971, share prices and turnover resumed a downward course until November 1971 and reached the lowest levels recorded after the 1969 boom. On average the prices of listed shares declined by 21 per cent during the five months to November 1971. A decline in purchases by foreigners and a pessimistic assessment of domestic economic prospects were largely responsible for the renewed downward movement. From December 1971, however, prices and turnover have risen sharply. In June 1972 the prices of all listed shares were on average 54 per cent higher

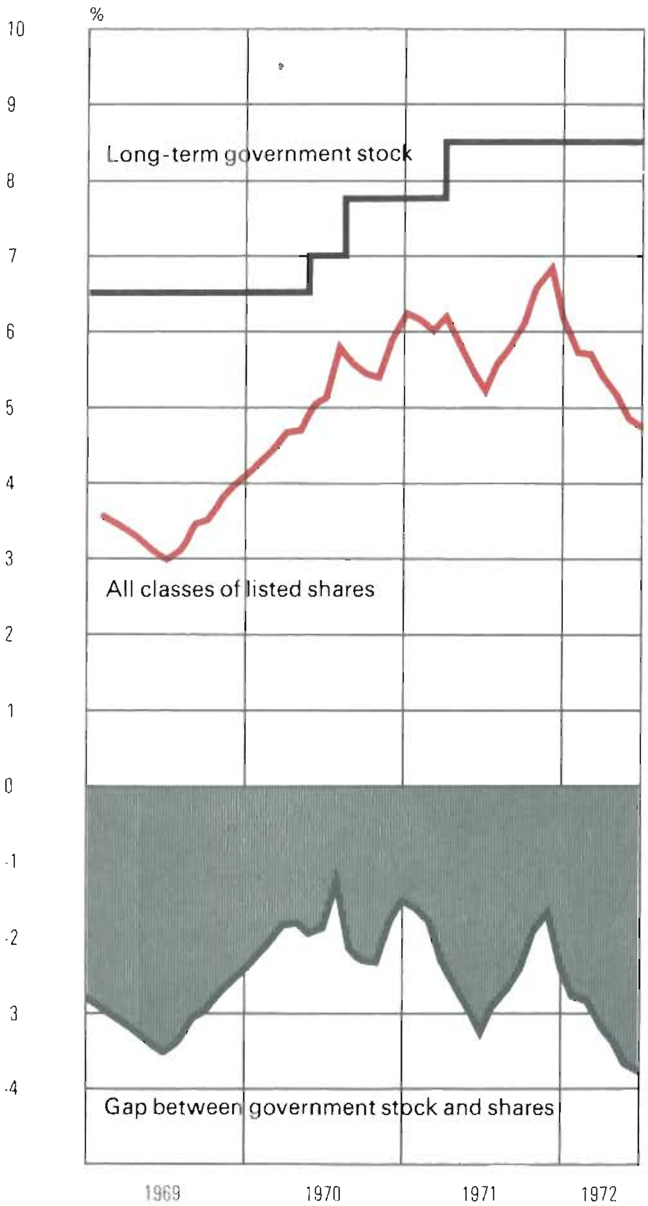
Johannesburg Stock Exchange



than in November the previous year and were roughly at the same level as in early 1968 when prices were rising or early 1970 when prices were declining. In the second quarter of 1972 stock exchange turnover, as measured by the number of shares purchased, reached a level that was only exceeded by the boom level recorded in the second quarter of 1969.

A major reason for the recovery of the share market was the renewed and substantial interest of foreigners in securities listed on the Johannesburg Stock Exchange. Net purchases of such securities by foreigners during the first six months of 1972 amounted to R121 million and exceeded the record annual figure of R101 million recorded in 1968. The uncertainty regarding international monetary arrangements and the sharp rise of the price of gold on the private market together with the relatively high level of South African share yields, stimulated the inflow of foreign capital through the stock exchange. On the domestic side, the imposition of import control in November and the devaluation of the rand in December 1971, followed by an increase in the country's gold and other foreign reserves and expectations of a decline in long-term interest rates, led to a more optimistic view of economic propects. The 1972/73 Budget presented at the end of March, was aimed, *inter alia*, at a more rapid rate of economic growth and served to improve such prospects even further. The change in the business mood provided a major inducement to local investors to invest in the share market.

Yields



The sharp rise in share prices from December 1971 to June 1972, however, was not evenly distributed among the various classes of shares. Whereas the prices of gold mining shares rose on average by 67 per cent and the increases in the prices of other mining (excluding coal mining) and financial shares ranged from 64 to 89 per cent, industrial and commercial share prices increased by about 32 per cent.

In conformity with share price movements, the average yield on all classes of shares increased from 5,5 per cent in June 1971 to 6,8 per cent in November 1971 and then declined to 4,7 per cent in June 1972. If this yield is compared with that on long-term government stock, the inverse yield gap widened from 1,7 per cent in November last year to 3,8 per cent in June 1972. This margin was even larger than the corresponding figure of 3,4 per cent recorded in May 1969.

Flow of funds to unit trusts not materially affected by the improvement of the share market

Notwithstanding the marked improvement of the share market during the last seven months of the period under review, the flow of funds to unit trusts increased only moderately, namely by R4 million, during the twelve months to June 1972. The relatively small inflow, nevertheless, represented a considerable improvement in relation to the preceding year, when an outflow of funds through net repurchases of units, amounting to R34 million, was experienced. Although the investment in units was not materially influenced by the improvement of the share market, the rise in share prices had the effect of increasing the market value of the trusts' net assets from R312 million at the end of October 1971 to R439 million at the end of June 1972, i.e. R57 million higher than the corresponding figure at the end of June 1971.

Easing of the market for fixed-interest securities

The market for fixed-interest securities eased during the first half of 1972, notwithstanding the very substantial amount of new funds raised through issues of marketable stock by the public sector.

This development was reflected in a better support for the long-term government stock issue in January 1972 and the exceptional success of the latest government stock issues in May and June this year. In addition, new issues of semi-gilt-edged securities during the second quarter of 1972 were over-subscribed, even after yields had been lowered. The main reasons for the easier trend of market conditions were (1) a smaller demand for equity as well as loanable funds by the private sector, (2) an increased supply of funds, particularly that at lower interest rates from abroad, (3) expectations of a decline in interest rates, and (4) higher investment requirements for the main suppliers of funds to the fixed-interest security market, namely insurers and private pension funds.

After the yield on long-term government stock had been increased from $7\frac{3}{4}$ to $8\frac{1}{2}$ per cent in March 1971, it remained unchanged until 10th August 1972 when it was lowered by $\frac{1}{4}$ per cent. The yield on new issues of long-term semi-gilt-edged securities was maintained at a level of about 9,3 per cent during the first nine months of the review period and was lowered to 9,2 per cent in April and 9,0 per cent in May 1972. Yields quoted for secondary transactions in long-term semi-gilt-edged securities declined to 8,75 per cent towards the middle of 1972. The yield on new issues of company debentures fluctuated between 10 and $10\frac{1}{4}$ per cent during the first eight months of 1971/72 and as no new issues were made thereafter, the effect of the easier market conditions on the yields on new issues cannot be determined at the present time.

The amount of new funds raised by the public sector through issues of marketable stock increased sharply during the year under review and amounted to about R1 025 million, compared with about R460 million in 1970/71. New issues of company debentures and notes, however, declined from about R120 million in 1970/71 to approximately R77 million in 1971/72. Of the net amount raised by the public sector, R248 million was contributed by the monetary banking sector, R227 million by the Public Debt Commissioners, R50 million by the redemption and other funds of public corporations and local authorities and R500 million by the private non-banking sector. The net investment in gilt- and semi-gilt-edged securities by the private non-banking sector was substantially higher than the corresponding figure of R154 million in 1970/71 and was largely accounted for by the very substantial subscriptions to the government stock issues in May and June this year. Investors were especially attracted to the long-term stock because the yield was maintained unchanged at $8\frac{1}{2}$ per cent at a time when long-term yields were generally expected to decline, particularly in view of the decrease of about 0,3 per cent in the yield on long-term semi-gilt-edged stock. The statutory obligation of insurers and private pension funds to increase their holdings of government stock at a time when the yield on such stock was considered to have reached a peak also contributed significantly to the demand for these securities.

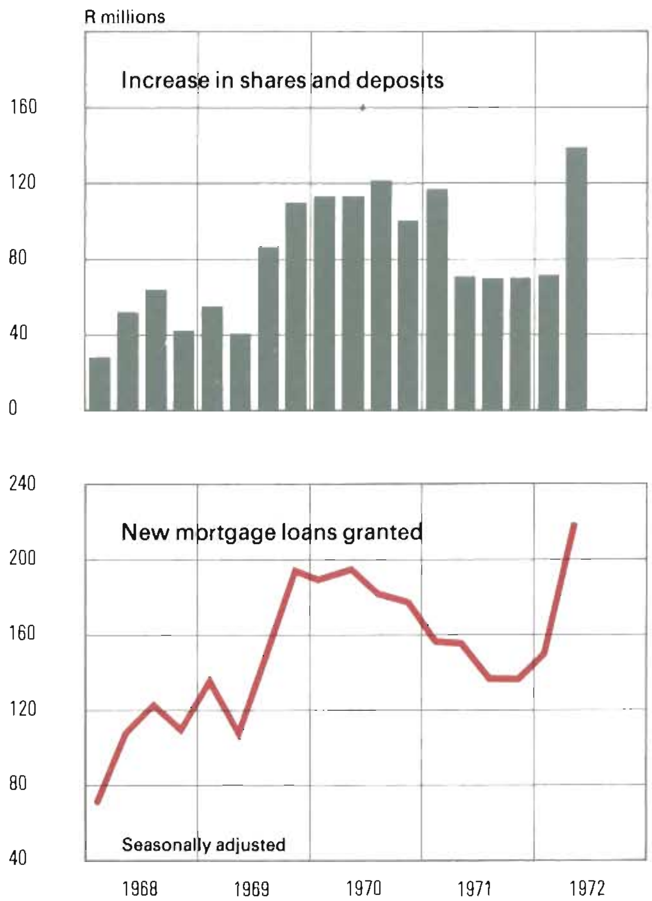
Smaller flow of funds to building societies

The flow of funds to building societies, in the form of an increase in shares and deposits, during the year that ended in June 1972 amounted to R350 million, representing an increase of 11 per cent, as against an increase of R410 million during the previous year. The increase of 11 per cent, nevertheless, still exceeded the average of 10 per cent for the ten-year period between June 1961 and June 1971. The smaller flow of funds to building societies had been experienced from the second quarter of 1971 and, if seasonal influences are eliminated, the increase in shares and deposits remained at the same level from the second quarter of 1971 to the first quarter of 1972, but then increased markedly during the second quarter of 1972.

To encourage the flow of funds to the societies, the Minister of Finance announced the following concessions on 19th August 1971:

1. Dividends on indefinite-period and fixed-period shares would henceforth be taxed on the same basis as dividends on ordinary company shares.
2. The limit on individual savings accounts was raised from R10 000 to R15 000.
3. The requirement under Section 32 of the

Building societies

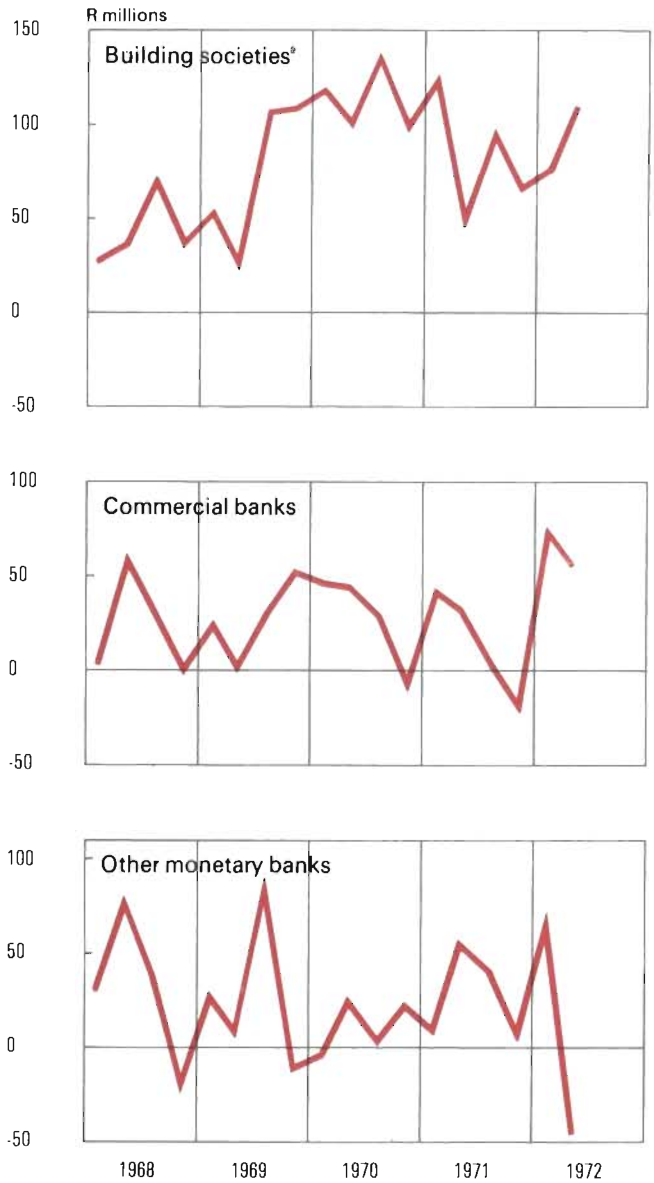


Building Societies Act, in terms of which additional prescribed investments other than liquid assets had to be maintained, was suspended until further notice.

4. The investment period for fixed deposits could be extended for periods of less than twelve months.
5. Normal agents' commission could be paid in respect of tax-free indefinite-period shares.

Further assistance came in March 1972 when deposit interest rate control was introduced. The 1972/73 Budget also provided for a government sponsored home-ownership savings scheme in terms of which the government will pay additional interest to prospective home-owners on savings with building societies. As the accompanying table shows, the tax concessions applicable to dividend earnings on building society shares led to a noticeable shift from fixed deposits to shares.

Net investment in savings and time deposits and building society shares



Changes in building society shares and deposits
R millions

	Year ended June 1971	1972
Shares	+209	+359
Fixed deposits	+138	— 85
Savings deposits	+ 63	+ 76
Total funds	+410	+350

New mortgage loans granted and paid out by building societies were less during 1971/72 than during the preceding twelve months, and the amount of mortgage and other loans outstanding increased by a smaller yet still sizeable amount, as the accompanying table shows. Although the societies were released from their obligation to maintain prescribed investments other than liquid assets, such investments nevertheless increased, and included an increase of R16 million in their holdings of gilt- and semi-gilt-edged stock not ranking as liquid assets.

Investments of building societies
R millions

	Year ended June 1971	1972
New mortgage loans granted	669	635
Mortgage loans paid out	733	621
Increase in loans outstanding	388	294
Net investment in liquid assets	22	24
Net investment in other prescribed investments	—6	38

Substantial investment in gilt- and semi-gilt-edged securities by insurers and private pension funds

During the year that ended in March 1972, the flow of funds to insurers and private pension funds amounted to approximately R580 million, representing an increase of 12 per cent in the assets of these institutions. As during 1970/71, the investment policies of the relevant institutions were still characterised by a preference for fixed-interest securities as opposed to ordinary shares. A very substantial part of their new funds, namely 48 per cent, was invested in gilt- and semi-gilt-edged securities and a further 8 per cent of such funds was directed to fixed-interest company securities. The institutions, therefore, significantly increased the supply of new funds in the market for fixed-interest securities and in total their net investment in this market amounted to about R330 million, compared with about R249 million in 1970/71.

Almost half of the increase in government stock holdings occurred during the first quarter of 1972 and may to a certain extent be ascribed to the higher investment requirements for insurers and pension funds announced by the Minister of Finance in September last year. In terms of this announcement the minimum amount of prescribed assets to be held by registered pension and provident funds was increased as from 1st October 1971 from 40 to 50 per cent of total assets and the minimum portion of these assets to be invested in government securities was raised from 10 to 20 per cent of total assets. In the case of insurers, the minimum amount of prescribed assets to be held was maintained at 30 per cent of net liabilities, but the minimum amount of government securities to be included in these assets was increased as from 1st October from 10 to 15 per cent.

Apart from the higher investment requirements which induced insurers and pension funds to invest more in gilt- and semi-gilt-edged securities, the easing of the upward pressure on long-term interest rates led to expectations of a downward movement in these rates, as in fact occurred in the case of secondary transactions in semi-gilt-edged securities. Insurers and pension funds, therefore, in some cases invested more than the required minimum in these securities so that they will for some time in future not have to invest in these securities if rates should decline. Other insurers and pension funds actually took a position as dealers in these securities and invested heavily on the expectation of rates declining in future, thus affording them the opportunity to realise a capital gain by selling the securities at higher prices.

Despite the shift in the investment preference of insurers and pension funds to fixed interest securities, they still invested a significant part of their available funds in ordinary shares, mainly during 1971. Equity investment at the existing yields and the growth potential of certain blue chips remained attractive. Insurers and pension funds also increased their investment in fixed property and mortgages moderately and allowed their cash and deposit holdings to decline, as against a substantial increase during the preceding twelve months.

Changes in assets of insurers and private pension funds
R millions

	Year ended March 1971	1972
Government stock	56	155
Public corporation and municipal stock	66	126
Company debentures	127	49
Total fixed-interest securities	**249**	**330**
Ordinary shares and unit trust units	29	87
Fixed property	38	46
Mortgage loans	23	47
Other loans	26	56
Cash and deposits	50	—9
Other assets	57	23
Total increase in assets	**472**	**580**