Note on the measurement and presentation of South Africa's net gold exports

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Introduction

South Africa's reintegration into global financial markets in the second half of the 1990s together with the gradual relaxation of exchange controls paved the way for changes to the country's gold-trading arrangements. The key role that the South African Reserve Bank had played in the marketing of gold changed significantly when the South African government liberalised the procedures for trading gold at the end of 1997.

Although gold still plays an important role in the South African economy, the contribution of gold exports relative to total exports of merchandise and gold declined from roughly 50 per cent in 1980 to 12 per cent in 2003. Over the same period, the country's production of gold as a percentage of Western World gold production contracted from 70 per cent to 14½ per cent – an indication that the influence of the country in the international gold market has dissipated over time. Largely due to the successful development of a foreign exchange market in South Africa and the much reduced need for a centralised system for marketing the country's gold production, the then Minister of Finance announced in December 1997 that South African gold mines would no longer be required to sell all newly produced gold bullion to the South African Reserve Bank, but would be allowed to do their own marketing subject to the exchange controls over South African residents.

The calculation of South Africa's net gold exports

For many decades the value of South Africa's net gold exports, which is shown as a separate item on the balance of payments, has been calculated according to a directive in early versions of the United Nations' *System of National Accounts* and not in accordance with the guidelines provided by the International Monetary Fund's *Balance of Payments Manual.* The item *net gold exports* in the current account of the balance of payments accordingly reflected the value of gold exports (including gold coins) minus gold imports plus any change in the gold holdings of the South African Reserve Bank and private banking institutions during a given period. With the exception of small quantities of gold that were sold to domestic investors in the form of Krugerrands, to the domestic jewellery industry and the dental profession, the volume of net gold exports was virtually equal to the domestic production of gold.

The fifth edition of the *Balance of Payments Manual* of the International Monetary Fund (IMF) proposes that a distinction be drawn between monetary gold and non-monetary or commodity gold and that transactions in monetary and non-monetary gold be treated differently in balance-of-payments statistics. In addition, the reclassification of gold, from non-monetary to monetary or *vice versa* (i.e. the monetisation and demonetisation of gold) should not be recorded as part of balance-of-payments statements.

Monetary gold may be defined as gold owned by monetary authorities (or by other institutions subject to the effective control of the authorities) and held as an international reserve asset. To qualify as a reserve asset, monetary gold should be available for use on demand. Transactions in monetary gold occur only between monetary authorities (essentially central banks) and their counterparts in other economies or between monetary authorities and international monetary institutions such as the IMF. As transactions in monetary gold only reflect changes in the composition of international reserve assets of the respective monetary authority – i.e. an exchange of gold for foreign exchange or vice versa – these transactions are not recorded in the balance of payments of South Africa.

Non-monetary gold, by contrast, covers gold not held as part of international reserve assets. It is treated like any other commodity and holdings thereof by mines, jewellers and other non-central bank entities are classified as stock-in-trade. International transactions in non-monetary gold are recorded in the trade account of the balance of payments.

When central banks increase their holdings of monetary gold by acquiring commodity gold (i.e. newly mined gold or existing gold offered in the private market), they are seen to have monetised gold. Similarly, when central banks release monetary gold from their holdings for non-monetary purposes (i.e. for sale to private holders or users), they are seen to have demonetised gold. Monetisation could therefore be defined as the reclassification of non-monetary gold to monetary gold and demonetisation as the reclassification of monetary gold to non-monetary or commodity gold. In order to identify the monetisation and demonetisation of gold, a separate item was created in the the balance of payments of South Africa titled "net monetisation (credit) or demonetisation (debit) of gold". Value changes resulting from the creation of reserve assets do not affect the net international reserve position owing to balance-of-payments transactions. In the international investment position of South Africa, value changes of this nature will be recorded as valuation adjustments.

Treatment of typical South African Reserve Bank transactions

In a nutshell, if the South African Reserve Bank purchases gold from a gold mine in one period and then sells it to a foreign jeweller in the next period at the same price, it would previously have been shown in the first period as net gold exports in the trade account with a corresponding increase in the net gold and other foreign reserves owing to balance-of-payments transactions and an increase in gross gold and other foreign reserves. In the second period no transaction flows would have been recorded, only a composition change with less gold and more foreign exchange in the gross gold and other foreign reserve holdings.

The new approach would show gold being monetised and an increase in gross gold and other foreign reserves in the first period. In the second period gold would be demonetised, the net gold exports in the trade account would increase, and the net gold and other foreign reserves owing to balance-of-payments transactions would also increase. The gross gold and other foreign reserves would remain unchanged.

In this issue of the *Quarterly Bulletin*, the calculation of South Africa's gold exports has been revised from 1981 onwards to conform to the guidelines of the fifth edition of the *Balance of Payments Manual* of the IMF.

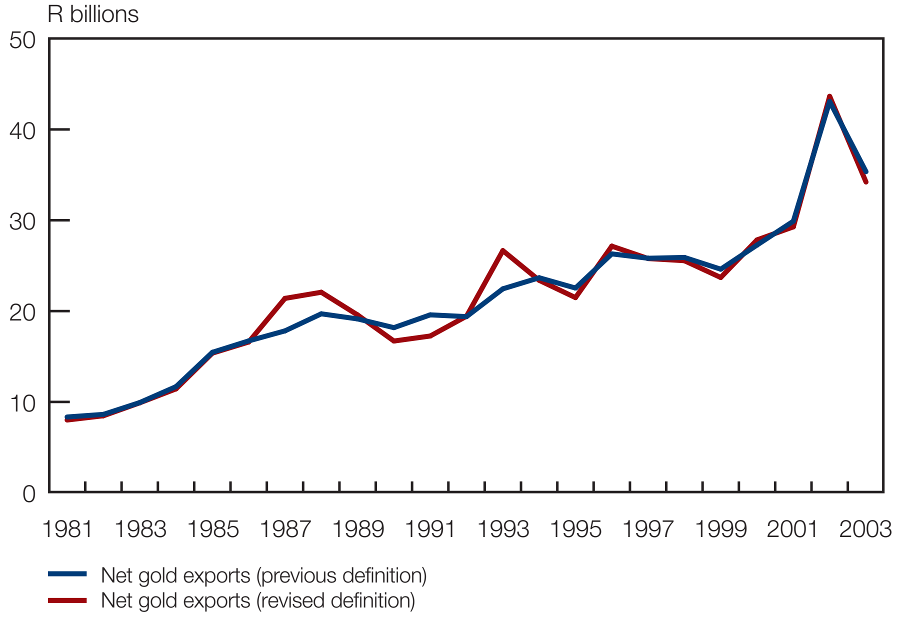
Impact of the revised treatment of gold on macroeconomic statistics

The revision of the country's gold exports impacts on the following economic aggregates:

- South Africa's *net gold exports* (pages S-86 to S-89) were revised to reflect transactions in non-monetary or commodity gold. Transactions in monetary gold between the South African Reserve Bank and other central banks or international monetary institutions were excluded from net gold exports. The item "net gold exports" in the trade account of the balance of payments no longer reflects the change in the gold holdings of the Reserve Bank and private banking institutions.

Such changes are now shown against a newly created item titled "*net monetisation and demonetisation of gold*" in the presentation of the balance of payments.

Net gold exports according to previous and revised definitions



- Changes in the country's *net gold and other foreign reserves owing to balance-of-payments transactions* (pages S-86 to S-87 and S-108) were revised to exclude the net monetisation or demonetisation of gold as well as transactions in monetary gold.

- South Africa's *overall terms of trade* on page S-89 was revised to reflect the adjustments made to gold export proceeds.

- The item *net foreign assets* in the monetary analysis (page S-24) was revised to exclude the net effect of the monetisation or demonetisation of gold.

- The *financing of gross capital formation* (page S-132) was amended to reflect the reclassification of gold from non-monetary to monetary gold, and vice versa.