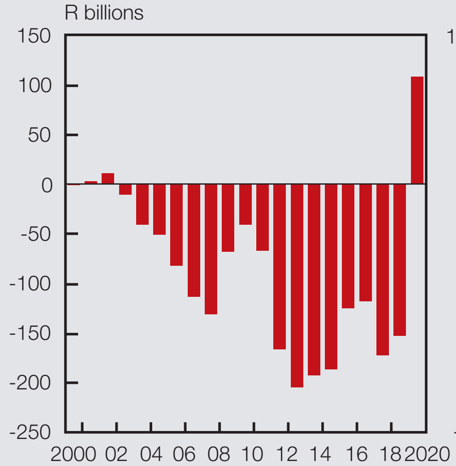
Box 2 The nexus between South Africa's balance on the current account of the balance of payments and saving and investment[1]

The balance on the current account of the balance of payments returned to an annual surplus in 2020, for the first time since 2002. Within the framework of the macroeconomic accounts, the difference between saving and investment is equal to the balance on the current account in an open economy. However, postulating the interrelationship between these variables in this manner is an oversimplification of the nuances and causalities between the main aggregates in the macroeconomic accounting framework, and in particular the balance on the current account in relation to gross saving and gross capital formation.

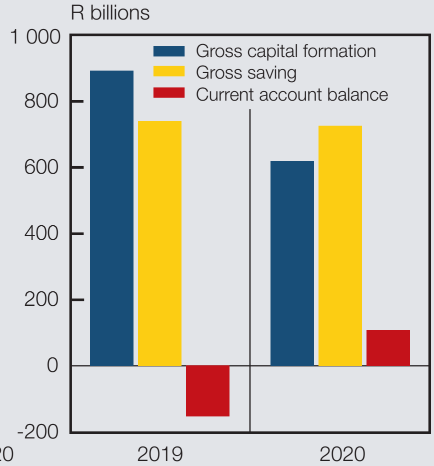
This box elucidates – at a high level – the macroeconomic accounting framework, to show how a current account deficit or surplus and the other aggregates relate to saving and investment, and how saving and investment relate to one another over the long term in the context of broader economic activity. From this nexus, it is evident that a current account surplus on its own does not necessarily support gross capital formation and that the pace of economic growth and its effect on income is a major driver of investment and saving. This is illustrated by the effect of the Coronavirus disease 2019 (COVID-19) on domestic economic growth, income generation as well as on saving and investment, despite the presence of a surplus on the current account.

Balance on the current account of the balance of payments



Source: SARB

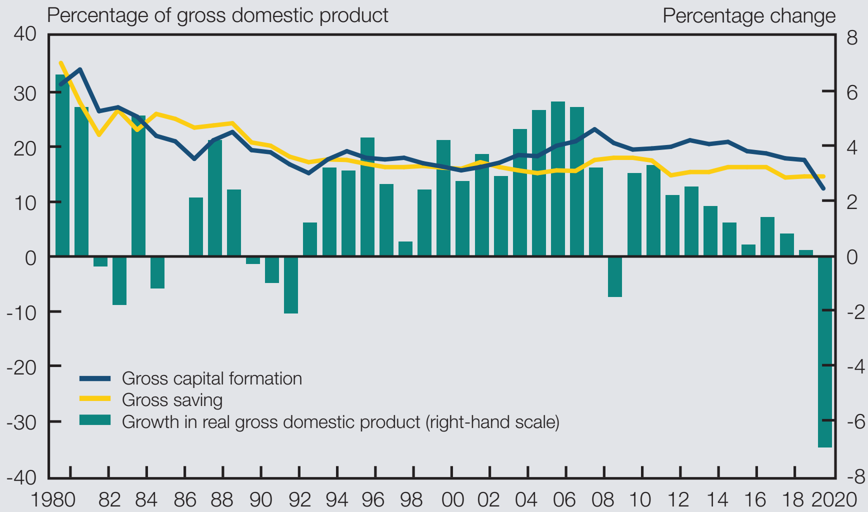
Balance on the current account, saving and investment



Sources: Stats SA and SARB

1 This box relates to the statistics published on pages S–82, S–84, S–112, S–116, S–137, S–138 and S–156 in this edition of the *Quarterly Bulletin*.

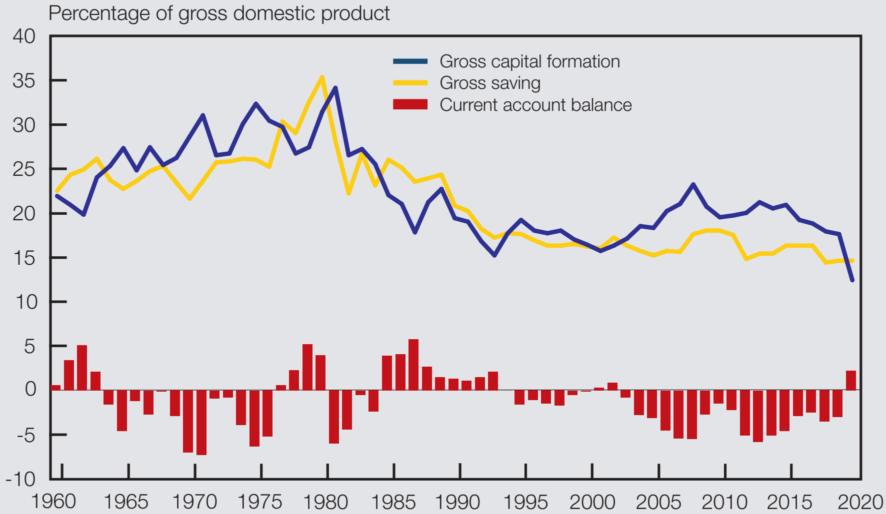
Economic activity in relation to saving and investment



Within the context of the macroeconomic accounting framework, the balance on the current account in an open economy is the difference between gross saving and gross capital formation, and when the current account is in a deficit (surplus) position, gross saving is less (more) than gross capital formation.[2] In this context, gross saving equals gross national disposable income less total final consumption expenditure, based on the notion that income not spent on final consumption expenditure will be saved.

Understanding the nexus between the balance on the current account, saving and investment, requires an appreciation of the fact that despite the necessity for the economic identity to hold,[3] it does not indicate causality. In practice, aggregate saving and investment are the outcomes of independent decisions and actions of a multitude of economic agents, implying the existence of a variety of causalities. For instance, a domestic institutional unit could first save from income generated and then embark on investment, or investment can be funded through banking sector credit extension, the financial markets through intermediation, or from non-residents. In all instances, the investment decisions will be informed by future prospects of economic activity and profits. A sizable portion of imported goods ultimately also find their way either directly or indirectly into consumption and investment expenditure, impacting both investment and the current account. Thus, investment spending on imported goods could contribute to a deficit or smaller surplus on the current account.

Balance on the current account relative to saving and investment



Sources: Stats SA and SARB

2 The gap between saving and investment not only relates to goods, but can for instance also be ascribed to an increase in dividend payments to the rest of the world, implying that when viewed in isolation, only saving would be affected.

3 An identity is a definition that always holds ex post, while an equation holds for specific values of the relevant aggregates.

South Africa's balance on the current account of the balance of payments within the context of the macroeconomic accounting framework

R millions

Calculations	High-level items	2019	2020
	Final consumption expenditure by households	3 058 619	2 978 356
Plus	Final consumption expenditure by general government	1 081 318	1 122 401
Plus	Gross fixed capital formation	908 878	783 620
Plus	Change in inventories	-15 773	-165 534
Plus	Residual	19 037	9 594
Equals	**Gross domestic expenditure (including residual)**	**5 052 077**	**4 728 437**
Plus	Exports of goods* and services**	1 515 866	1 515 419
Less	Imports of goods* and services**	1 490 318	1 269 881
Equals	**Gross domestic product**	**5 077 625**	**4 973 975**
Plus	Primary income and current transfers from the rest of the world**	143 540	154 604
Less	Primary income and current transfers to the rest of the world**	322 264	291 938
Equals	**Gross national disposable income**	**4 898 901**	**4 836 641**
Less	Gross domestic expenditure (including residual)	5 052 077	4 728 437
Equals	**Balance on current account**	**-153 176**	**108 204**
	Exports of goods* and services**	1 515 866	1 515 419
Less	Imports of goods* and services**	1 490 318	1 269 881
Plus	Primary income and current transfers from the rest of the world**	143 540	154 604
Less	Primary income and current transfers to the rest of the world**	322 264	291 938
Equals	**Balance on current account**	**-153 176**	**108 204**
	Gross national disposable income less the residual	4 879 864	4 827 047
Less	Total final consumption expenditure	4 139 937	4 100 757
Equals	**Gross saving**	**739 928**	**726 290**
Less	**Gross capital formation*** **	**893 104**	**618 086**
Equals	**Balance on current account**	**-153 176**	**108 204**

Components may not add up to totals due to rounding off.

* Collectively part of the trade account, and in turn, part of the current account
** Collectively part of the services, income and current transfer account, and in turn, part of the current account
*** Generally referred to as investment

Sources: Stats SA and SARB

From the macroeconomic accounting framework, it is evident that in aggregate, a higher level of saving in relation to investment requires a current account surplus, as in 2020 and in all other such occurrences in the past. In the case of South Africa, both annual saving and investment as a ratio of gross domestic product (GDP) have trended lower since the beginning of the 1980s, irrespective of current account surpluses or deficits. Despite a persistent and increasing current account deficit from 2003 to 2008, at the beginning of the longest period of uninterrupted consecutive annual current account deficits of 17 years, the gradual decline in the saving and investment ratios to GDP was temporarily reversed. The larger annual current account deficits and the upward trend in both saving and investment relative to GDP during the 6-year period from 2003 to 2008 were accompanied by an above average annual real economic growth rate of 4.5%. This compares with an average annual real economic growth rate of only 1.4% for the remainder of the 17-year deficit period, whereas the average annual real economic growth rate amounted to only 2.0% from 1980 to 2002.