Statement regarding anti-inflationary measures

*by the Honourable the Minister of Finance,
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Last year the authorities introduced various measures to counter the two dangers which threatened the South African economy, namely, inflation and the decline in our foreign reserves.

The second danger has been averted, at least for the present, and our total reserves now stand at the satisfactory level of approximately R585 million, thanks to an improvement in the balance of payments on current account as well as an inflow of foreign capital.

The measures taken against the first (and related) danger, namely inflation, have also had a measure of success, so that a reduction in the excessive rate of expansion of the economy set in after the middle of 1965. During the first quarter of 1966 gross domestic expenditure actually fell below the gross national product. General economic activity, however, remained unduly high, and the desired effect of the monetary and other measures was to a large extent offset by various factors, particularly the inflow of foreign capital, which sustained the liquidity of the economy at too high a level.

Although there is no reason for undue concern, the Government nevertheless feels that, because of the neutralising factors, the existing measures have worked too slowly, and that it is desirable to take effective steps to eradicate the inflationary danger more rapidly. In the short run these steps may cause a measure of inconvenience in, and even a pause in the growth of, certain sectors of the economy, but they are absolutely necessary in order to ensure the economic stability of the Republic and to create the conditions for further economic expansion at a sustainable rate.

The evils of inflation, especially for the salary and wage-earner, the pensioner and the gold mining and other export industries are well known. The Government is therefore determined to ensure the internal and external stability of the rand and to combat inflation effectively.

It is essential that the measures should penetrate to the heart of the problem, namely, the excessive monetary demand. In this connection the Government has in view a four-point attack on inflation.

The first group of measures are intended as a positive encouragement to saving. The South African Reserve Bank's pattern of rates for long-term Government securities (i.e. exceeding ten years) will be progressively increased so that the rate for stocks of 25 years and over will be $6\frac{1}{2}$ per cent. The restrictions on interest rates payable on deposits with financial institutions will be lifted immediately, so that these institutions can compete freely for the savings of the public. In addition, the conditions of investment in, *inter alia*, the Post Office Savings Bank and National Savings Certificates will be broadened and made more attractive – particulars will be announced shortly.

The second aim of the authorities is to slow down the excessive pace of capital and consumption expenditure. With this object in view the Reserve Bank has decided, after the customary consultation with the Treasury, to raise its discount rate from 5 per cent to 6 per cent. The general rise in interest rates, which will probably follow this step as well as the first group of measures, will also promote this second objective. In addition the Reserve Bank's request to the monetary banks to limit their discounts, loans and advances to the private sector to the total of these items as at 31st March, 1965 (plus a special increase of $2\frac{1}{2}$ per cent which must be used exclusively for the agricultural sector) will be extended for a further period of six months from 30th September, 1966. I wish to emphasise that the abovementioned increases in interest rates will, it is hoped, be of comparatively short duration; it will strengthen the anti-inflationary forces substantially if less urgent spending is postponed until the overheating of the economy has been eliminated and rates can again be reduced.

The third point of the authorities' attack on inflation consists of fiscal measures. These measures cannot be announced before my Budget Speech next month. I wish to state now, however, that the Government is determined to finance State expenditure as far as possible in a non-inflationary manner. This requires that State capital expenditures be met to a larger extent from long-term loans (i.e. genuine savings). The higher rates of interest for long-term Government loans, as well as the more attractive conditions offered to the individual saver, should help the Government to achieve this object. It will, however, also be necessary to take special steps to bring about a greater degree of investment in Government securities by life assurance companies, pension funds and perhaps certain other financial institutions. Proposals in this connection will be submitted to Parliament.

As a fourth measure against inflation my colleague, the Minister of Economic Affairs, has decided to relax import control in respect of certain types of goods on a selective basis. Dr. Diederichs will make an announcement in this connection shortly.

The measures which are now being applied may in some cases affect the lower and middle income groups in the short run, but it is precisely these groups who will suffer relatively the greatest loss in the long run if these steps are not taken. On the other hand, these income groups will reap relatively the greatest benefit in the long run from the steps the Government is taking to combat price increases. The Government will also act positively to protect the interests of these groups as far as possible in the period of adjustment. In particular, prices will be closely watched and the Government will not hesitate to act if unjustified price increases should occur. This applies of course to all price increases, but increases in food prices especially will be very carefully scrutinized.

The producers' prices for most food products, which – mainly because of drought conditions – had to be increased, have already been fixed for the current season and have therefore already come into force. The Government will of course continue to have close regard to the interests of farmers, but will at the same time ensure that consumers' prices of essential foodstuffs are kept within reasonable limits. The food processing industries and the distributive trade have already passed on the effect of the increased producers' prices to the consumer. The Government therefore appeals to commerce and industry to do their share in maintaining the stability of food prices, which play such a strategic role in our struggle against inflation.

Rents of dwellings and other buildings are, like food prices, another strategic factor in the cost of living, and the Government regards any further increases in rents at this stage as entirely undesirable. The Government will therefore keep this aspect also under close surveillance.

Furthermore, if rates of interest on mortgage bonds have to be increased, the Government appeals to building societies and other financial institutions to extend the duration of mortgage loans wherever possible rather than to raise the payments on the loans.

The struggle against inflation, which is a world-wide phenomenon, demands sacrifices from all sections of the community. It requires a high sense of responsibility and restraint among employees and traders in fixing wages, salaries and prices. It requires also strong and resolute action by the authorities in the directions set out above. If the Government should shrink from its responsibility, it would seriously jeopardize the future economic stability of the Republic. But I trust that, if we all stand together to win the war against inflation, we shall be able, after the necessary period of adjustment, to usher in a new phase of stable economic progress.