South African Reserve Bank

1973

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-third Ordinary General Meeting to be held on 21 August 1973.

Hierdie Verslag is ook in Afrikaans beskikbaar.

Contents

General observations

After almost two years of relatively slow economic growth, the South African economy is at present in an upward phase of the business cycle. From about the beginning of the fourth quarter of 1972 a moderate acceleration in economic activity has occurred, as indicated by the national accounts and other economic statistics. Despite this revival in economic activity the rate of increase in the real gross domestic product for the year that ended on 30 June 1973 as a whole did not show any significant acceleration compared with the preceding year. In fact, real gross domestic product increased by between 4 and 4½ per cent during the year under review — approximately the same growth rate as during the preceding year. Gross *national* product at constant prices recorded a growth rate of about 5½ per cent during the past year, compared with a rate of approximately 5 per cent during the preceding year. The real national product increased at a higher rate than the real domestic product owing to the more rapid rise in the prices of South Africa's export products (including gold) than in prices of imported goods. This favourable turn in its terms of trade enabled South Africa to obtain more goods from abroad for the same volume of exports during the year under review than during the preceding year and thereby increased the economic welfare of residents by more than the increase in domestic production.

At current prices the gross domestic product increased by 16 per cent during the year under review. Owing mainly to sharp increases in the price of gold, other mining and agricultural products, the contribution to the gross domestic product of the two primary sectors rose substantially, namely by 22 per cent in the case of agriculture and by 44 per cent in the case of mining. Higher rates of increase were also recorded by manufacturing, wholesale and retail trade and the sectors transport, storage and communication and community, social and personal services. The sharp and sustained rise in the price of gold on the private market from the beginning of 1972 (from December 1971 to June 1973 the average price on the London market rose by 148 per cent) not only brought new prosperity to the gold mining industry, but the higher incomes accruing to the gold mining companies have also been percolating through to the rest of the economy and should contribute to a higher growth rate in general. The value of non-gold mining production also rose substantially as a result of increases in both the volume of production and higher prices obtained, particularly on international commodity markets. In real terms, the main contributions to the increase in the gross domestic product were made by the manufacturing and non-gold mining sectors, which showed marked increases in the volume of production.

The revival of economic activity during the year under review, therefore, stemmed largely from higher export earnings (particularly those of agriculture and mining) and to a lesser extent from increased manufacturing production. Total domestic demand has not yet expanded materially, but individual components of domestic demand increased substantially, namely private consumption expenditure on durable goods (mainly motor cars) and capital outlays by public corporations (mainly Iscor), the South African Railways and the Post Office. Inventory investment remained low and this brought the ratio of inventories to sales to a very low level judged by past experience. Fixed investment by the private sector showed little change during the year under review, with actual declines recorded in the capital outlays of the sectors commerce and manufacturing. However, a stronger revival in total domestic demand seems possible in the near future in view of the following considerations: the secondary expansionary effects of the increased export earnings and net gold output, the relatively low level of inventories, the substantial increases in salaries and wages which may lead to higher consumption expenditure, the rise in manufacturing production which will sooner or later take up the existing unused capacity and lead to increased new capital outlays by the private manufacturing sector, the mining of lower grade ore by gold mining companies which may increase their capital outlays, the increased spending by the Government as provided for in the 1973/74 Budget, the large expansion programmes already announced by other public authorities and corporations, and the easier monetary and banking situation, with low interest rates which may facilitate spending in general. If the possibility of a faster rate of increase in aggregate domestic demand is viewed in conjunction with the greater availability of labour and capital resources, the present situation appears very conducive to a further acceleration in the overall growth rate of the economy.

The relatively low rate of increase in aggregate domestic demand, as measured by the increase in the gross domestic expenditure, coupled with a higher rate of increase in the gross national product, was reflected in a surplus on the current account of the balance of payments during 1972/73. The balance of payments on current account showed a marked improvement during the past three years and changed from a deficit of over R1100 million in 1970/71 to a deficit of over R400 million in 1971/72 and then to a surplus of nearly R270 million in 1972/73. The net inflow of capital declined during the same period from about R750 million in 1970/71 to about R235 million in 1972/73, mainly as a result of more favourable conditions for raising capital in the domestic market; large repayments of official loans; the switching from foreign to local financing of international trade induced by the lower interest rates obtaining in South Africa; and exchange control measures introduced by the United Kingdom. Despite the reduction in the net capital inflow, the total gold and other foreign reserves increased during the past two years to an all-time record of well over R1300 million at the end of June 1973. Sharp rises in merchandise exports and net gold output, which outweighed the increase in merchandise imports and net service payments, were mainly responsible for the improvement in the balance of payments during the year under review.

Against the background of increased exchange rate flexibility in the world as a whole, the improvement in the balance of payments and the revival in domestic economic activity naturally influenced South Africa's exchange rate policy. After depreciating effectively in relation to all other currencies to a level of about 15 per cent below that of 15 August 1971, the rand appreciated effectively by about 3 per cent on 25 October 1972 and further by about 6 per cent when the dollar devalued by 10 per cent on 12 February 1973. After allowing a depreciation of about 3 per cent with the downward floating dollar during April and May 1973, the authorities appreciated the rand by 5 per cent on 5 June 1973 and this brought the average effective exchange rate of the rand to about 5 per cent below the level of 15 August 1971, or to about the level of 31 October 1967.

Given the healthy balance of payments situation and with an acceleration in domestic production already under way, the most pressing remaining problem facing the authorities is the high rate of price increases. During the year under review, consumer and wholesale prices rose at exceedingly high rates by South African standards. This problem of inflation however, was not limited to South Africa, but was a world-wide phenomenon. Changes in exchange rates during the past two years contributed materially to the higher rate of increase in prices, but the largest contribution to the sharp rise in consumer prices during 1972/73 was made by the exceptionally high rate of increase in food prices. It is unlikely, however, that food prices will continue to rise at this rate during the coming months. In fact, the rate of increase in the consumer price index reached a peak in April 1973 before levelling off during May and June 1973. Another welcome development was the increase in output per man-hour in mining, manufacturing and construction recorded during recent months that may assist in reducing the high rate of inflation.

During the year under review, the money and banking situation was characterised by a considerable further easing of money market conditions, a marked fall in interest rates, particularly short-term rates and a sharp rise in the quantity of money and near-money caused by the increase in the gold and other foreign reserves and a substantial increase in bank credit to the private sector. The increase in bank credit can only partly be explained by the rise in consumer spending, but to a large extent it probably represents a shift from foreign to local financing of international trade induced by the considerable interest rate differential and a shift from inter-company lending to certain forms of bank lending, especially bankers' acceptances, at relatively low interest rates. Although the supply of money and near-money increased substantially during 1972/73, prices also rose more rapidly, with the result that the ratio of money and near-money to the gross domestic product at current market prices did not increase much and was still below its long-term trend.

Monetary and fiscal policy remained cautiously stimulative during the year under review. Credit ceilings were abolished and the new liquid asset requirements were fixed at levels which enabled the banks to extend additional credit to the private sector. Interest rates quoted by the official sector, including Bank rate, were reduced on several occasions and the 1973/74 Budget was aimed at a further moderate stimulation of economic growth.

During the year under review, the demand-supply relationship of loanable funds in the capital market was quite different than during the preceding years. Increased domestic saving and a substantial addition to domestic liquidity resulting from a favourable balance of payments and the large increase in bank credit contributed to a much larger supply of funds in the financial markets. At the same time, the demand for funds was relatively low because fixed investment increased slowly, with the result that interest rates declined significantly. The increased supply of loanable funds was also reflected in large inflows of funds to building societies and banks and well supported new issues in the market for fixed-interest securities. Share prices and turnover on the stock exchange continued to increase during the year under review, particularly until January 1973. Gold shares attracted strong interest and the prices showed exceptionally sharp increases, which was largely associated with the substantial rise in the price of gold on the private market.

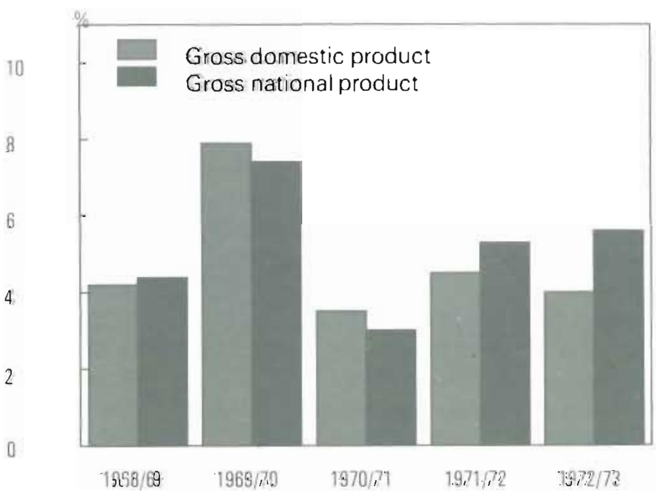
National accounts and other economic indicators

Revival in general economic activity

The rate of increase in the gross domestic product at current market prices accelerated appreciably from $11\frac{1}{2}$ per cent in 1971/72 to 16 per cent during the year that ended on 30 June 1973. Sharp rises in the gross operating surplus (mainly profits) during both years were mainly responsible for the relatively high growth rates in the gross domestic product, although the rate of increase in the remuneration of employees was also higher during 1972/73. The relative share of the operating surplus in the gross domestic product at factor cost consequently increased from the relatively low level of 39 per cent in 1970/71 to nearly 43 per cent in 1972/73. The latter percentage was still slightly lower than the average for the nineteen sixties.

In contrast to the pronounced acceleration in the growth rate of gross domestic product at *current market prices*, gross domestic product at *constant prices* increased at an approximate rate of between 4 and $4\frac{1}{2}$ per cent during both 1971/72 and 1972/73. However, a distinct change was observed in the rate of increase in the quarterly real gross domestic product during the course of 1972/73. Since the fourth quarter of 1972 the real gross domestic product increased at a moderately faster rate. Several sectors of the economy contributed to this acceleration, in particular the manufacturing sector, the non-gold mining sector and certain sections of commerce. The statistical evidence provided by the national accounts data of a significant but moderate revival in general economic activity from the fourth quarter of 1972, was also confirmed by a statistical analysis of a large number of monthly economic indicators, which indicated a lower turning point in the business cycle in October 1972.

Annual percentage change in gross domestic product and gross national product at constant 1963 prices



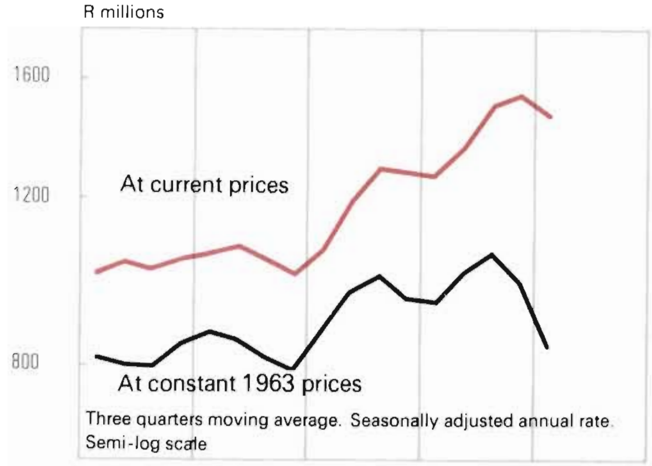
Sharp increase in real gross national product

In the present situation of sharp increases in prices of some of the country's most important export products, in particular gold, the rate of increase in the real gross domestic product to a certain extent gives a misleading picture. The real gross domestic product represents a measure of the volume of goods and services produced in the domestic territory during a particular period of time. All the goods and services produced domestically are not intended, however, for the domestic market because a certain portion is exchanged for goods and services from the rest of the world. If, therefore, the prices of South African export products increase faster than the prices of goods imported from the rest of the world in exchange for these products (i.e. when an improvement in the "terms of trade" occurs) the real purchasing power or the total volume of goods and services available for domestic consumption or investment by the residents of the country will increase at a faster rate than the real gross domestic product. Such a favourable development will be reflected in a higher rate of increase in the real gross *national* product than in the real gross *domestic* product.

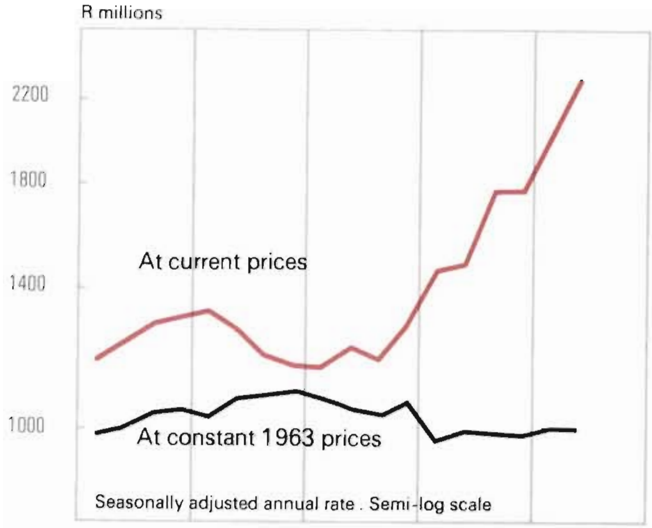
A very significant change in the terms of trade of South Africa became evident from the beginning of 1972. For most of the post-war period the prices of South Africa's imports rose at a faster rate than its export prices, but from the beginning of 1972 a reversal of this trend occurred. For both 1971/72 and 1972/73 the more favourable terms of trade led to a higher growth rate in the real gross *national* product than in the real gross *domestic* product. Whereas the real gross domestic product increased at an approximate rate of between 4 and $4\frac{1}{2}$ per cent during 1971/72 and 1972/73, the increase in the real gross national product was 5 per cent in 1971/72 and $5\frac{1}{2}$ per cent in 1972/73. The rate of increase in the economic welfare of the country, as measured by the real gross national product, was therefore, higher than the rate of increase in the domestic product and, moreover, showed an acceleration from 1971/72 to 1972/73. With the rate of increase in the prices of imported goods declining and with the further increase in the price of gold and other export commodities during 1973, the terms of trade may be even more favourable for the calendar year 1973, and the rate of increase in the real *national* product may be substantially higher for 1973 than that of the real *domestic* product.

Contribution to gross domestic product of

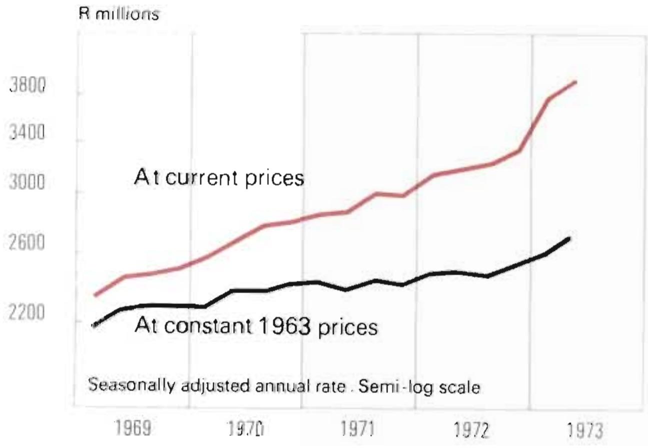
Agriculture



Mining



Manufacturing



Primary and secondary sectors contributed to higher growth rate

Notwithstanding drought conditions, the agricultural sector increased its contribution to the gross domestic product at current market prices by more than 22 per cent during 1972/73, mainly owing to the higher value of the maize and wheat crops during the second half of 1972, exceptionally good fish catches, and sharp rises in the prices of most other agricultural products. At constant prices, the value added by the agricultural sector showed almost no change during 1972/73.

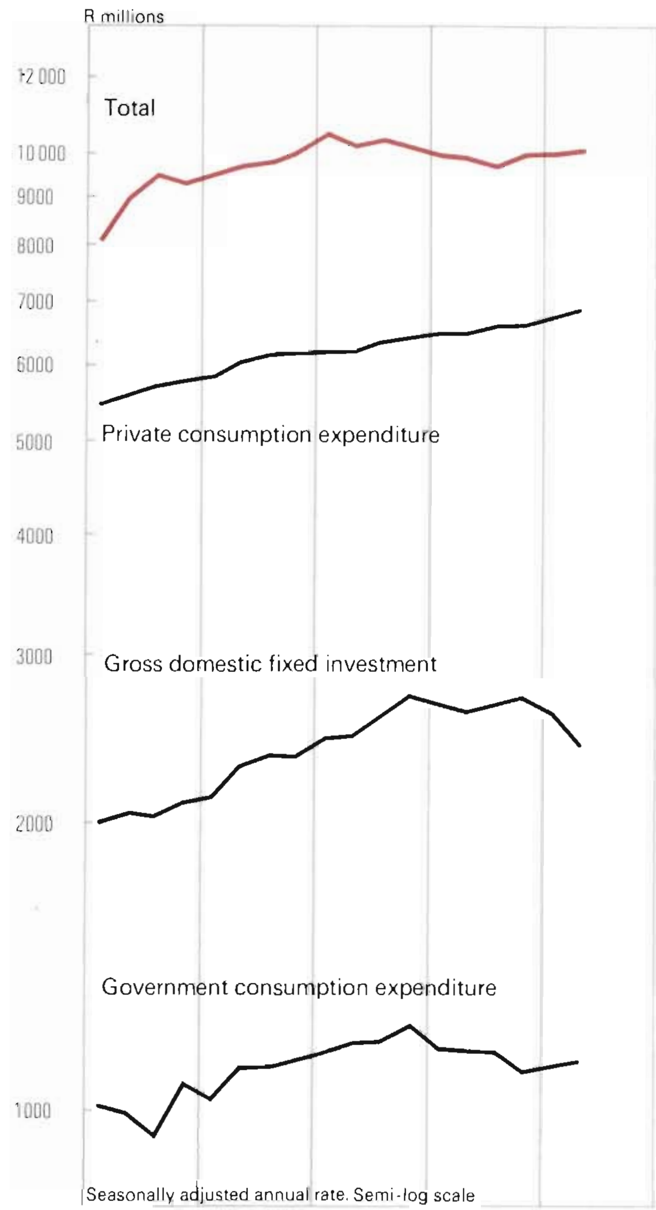
In the mining sector conditions were even more favourable during the year under review. As a result of the marked increase in the price of gold on the private market and the high prices obtained for diamonds and other metals and minerals on international markets, the contribution of the mining sector to the gross domestic product at *current* prices increased by no less than 44 per cent in 1972/73, compared with 15 per cent during the previous year. At constant prices, however, the value added by mining declined during both years mainly on account of a decline in gold production.

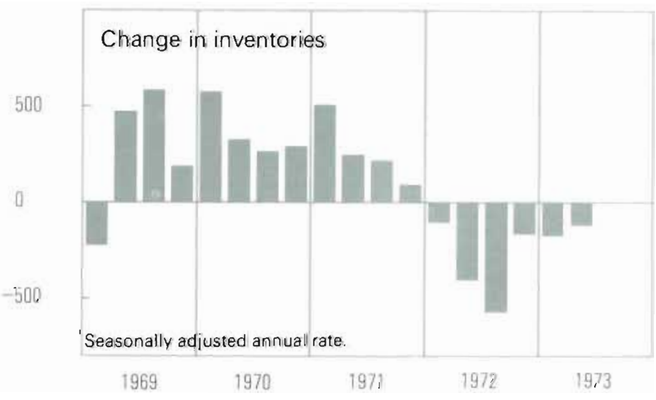
The contribution of the manufacturing sector to the gross domestic product also increased at a higher rate during 1972/73 than during 1971/72, mainly owing to a substantially faster rate of growth in profits. A welcome development during the year under review was the acceleration in the rate of increase in the volume of manufacturing production, particularly during the first half of 1973. In the primary sectors of the economy, however, the higher value added was almost exclusively attributable to higher prices, as shown in the accompanying graphs. The higher rates of growth in the value added by the wholesale and retail sector and the sectors transport, storage and communication and community, social and personal services were also largely attributable to higher prices and increases in salaries and wages granted to government employees.

Low rate of increase in aggregate domestic demand

During the year that ended on 30 June 1973, aggregate domestic demand at current prices, as measured by total gross domestic expenditure, rose by $10\frac{1}{2}$ per cent compared with an even lower rate of increase of $6\frac{1}{2}$ per cent during the preceding year. Although the rate of increase during the year under review was higher than during the preceding year, it was nevertheless still appreciably lower than the rates of $17\frac{1}{2}$ per cent and $12\frac{1}{2}$ per cent recorded during 1969/70 and 1970/71, respectively. The main cause of the relatively low rate of increase in total domestic spending during 1972/73 was the marked, running-down of inventories, although consumption expenditure by general government and gross domestic fixed investment also increased at slightly lower rates. Private consumption expenditure at current prices rose by about the same high rate as during the preceding year.

Gross domestic expenditure at constant 1963 prices





As gross national product increased at a much higher rate than gross domestic expenditure during the last two years, the gross national product exceeded gross domestic expenditure in 1972/73 for the first time since 1967/68. This was also reflected in a surplus on the current account of the balance of payments during 1972/73.

Moderate increase in private consumption expenditure

During both 1971/72 and 1972/73, private consumption expenditure at current prices increased by about 12 per cent but at constant prices by only approximately 4 per cent. This implies that the rate of increase in the price deflator for consumer expenditure remained almost unchanged, albeit at a high level, during the past two years.

Percentage change in private consumption expenditure at constant prices

	Year ended 30 June 1971	1972	1973
Durable goods: total	—1	4	5
Furniture and household appliances	—5	11	—
Personal transport equipment	4	—2	12
Semi-durable goods: total	9	4	4
Clothing and footwear	11	5	4
Non-durable goods:	6	4	4
Services:	5	4	4
Total private consumption expenditure	5½	4	4

As can be seen from the accompanying table, the rates of increase in expenditure at constant prices on semi-durable and non-durable goods and also on services remained unchanged over the last two years at a level below that of 1970/71. Expenditure on durable goods, however, increased substantially and significant changes occurred in the rates of increase in expenditure on major durable goods components. Expenditure on furniture and household appliances at constant prices increased sharply in 1971/72, but showed no change during 1972/73 whereas real expenditure on new personal transport equipment, mainly on new motor cars, increased by no less than 12 per cent in 1972/73, compared with a decline of 2 per cent in the preceding year. At current prices, the outlays on personal transport equipment increased by as much as 25 per cent during the year under review.

Although the rate of increase in private consumption expenditure showed little change during the past year, quarterly estimates at both current and constant prices revealed a marked acceleration in expenditure during the first half of 1973. Increased real consumer spending during this period was due to a substantial increase in the number of new motor cars sold, although noticeable volume increases were also recorded in the spending on clothing and footwear.

Small increase in consumption expenditure by general government

Current expenditure on goods and services by general government rose by only about 5 per cent during the year under review, as against 12 per cent during the preceding year. Although this was the second consecutive year in which the rate of increase in government consumption expenditure declined, quarterly estimates reveal a sharp acceleration during the first half of 1973. However, the higher level of government expenditure during the second quarter of 1973 was almost entirely attributable to salary and wage increases granted to public servants, effective from April 1973.

Lower rate of increase in gross domestic fixed investment

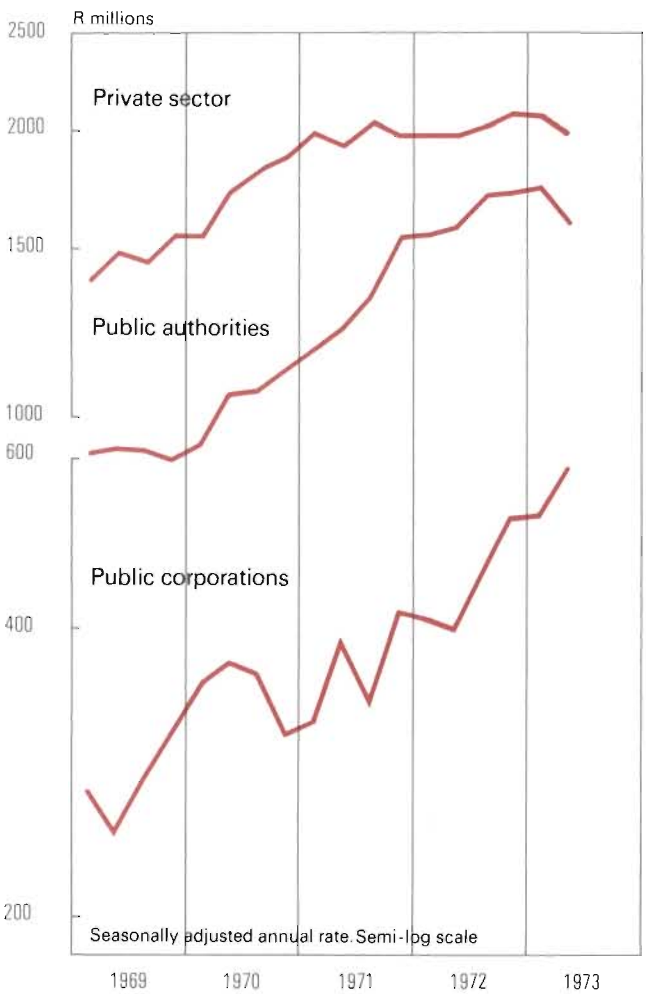
After increasing at relatively high rates during the preceding three years, gross domestic fixed investment at current prices showed a moderate rise of only 8 per cent during 1972/73. As the accompanying table shows, this low rate of increase resulted from no change in the capital outlays by the private sector and a substantial reduction in the rate of increase in fixed investment by public authorities. Capital expenditure by public corporations, which is substantially smaller in size than the aforementioned two categories, increased markedly during 1972/73, mainly on account of the extension and renewal programmes of Iscor.

Fixed investment by public authorities increased at a lower rate during 1972/73 because capital outlays on social and non-infrastructural development showed

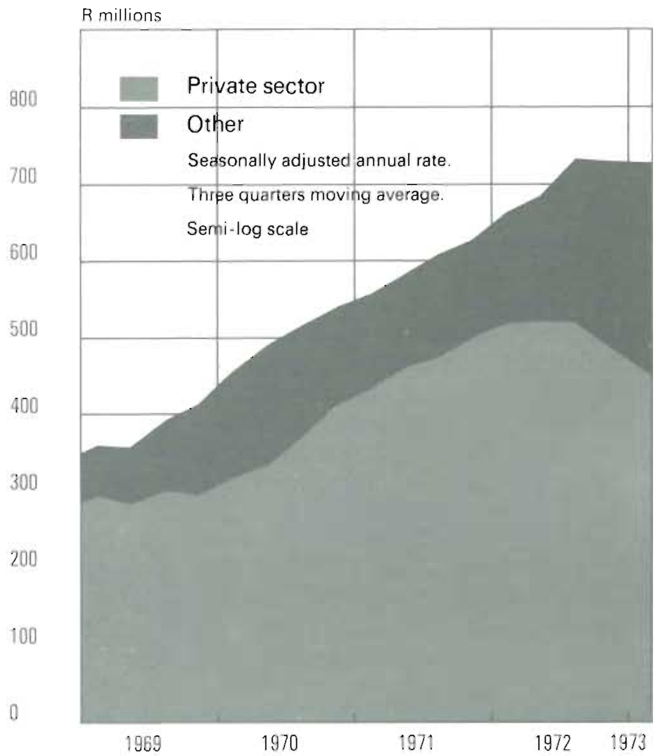
Percentage change in gross domestic fixed investment at current prices

	Year ended 30 June			
	1970	1971	1972	1973
Private sector	**14**	**21**	**5**	**—**
Agriculture and mining	—	6	—2	10
Manufacturing	5	37	18	—12
Commerce	31	28	2	—17
Private residential buildings	17	29	2	5
Public authorities	**11**	**20**	**35**	**13**
Economic infrastructural development:	9	20	41	17
S.A. Railways	— 9	23	70	24
Post Office	41	40	35	11
Other projects	16	20	16	—2
Public corporations	**29**	**3**	**18**	**39**
Manufacturing	123	— 2	23	91
Electricity, gas and water	2	7	17	6
Total fixed investment	**14**	**18**	**16**	**8**

Gross domestic fixed investment at current prices



Gross domestic fixed investment: manufacturing



an actual decline, whereas the rate of increase in investment by the S.A. Railways and the Post Office decreased. Nevertheless, investment by public authorities, and especially in respect of economic infrastructure, remained on a relatively high level.

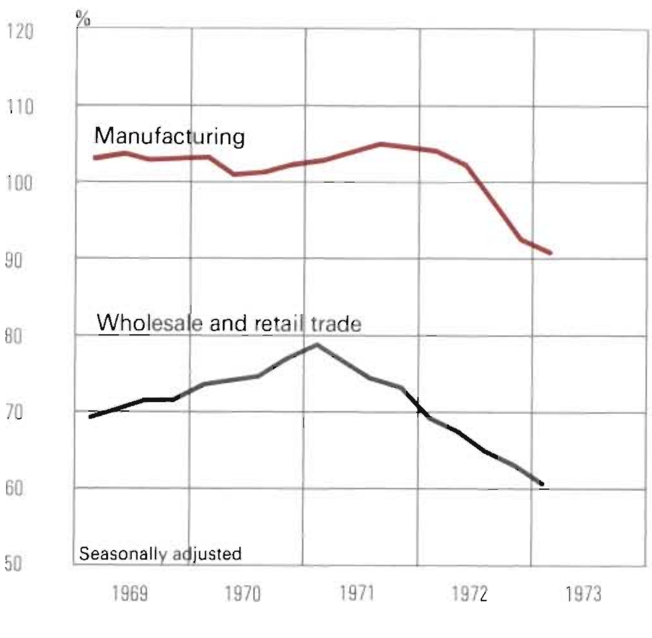
Capital outlays by the private sector showed little change during the past two years. During 1972/73 the low level of private fixed investment was noticeable in all the major sections, with manufacturing and commerce showing actual declines. However, if manufacturing projects of public corporations such as Iscor, Sasol, Natref and Alusaf, are included under capital outlays on manufacturing projects this total increased by a further 10 per cent during the year under review. The expansionary forces at work in the economy, such as higher consumer expenditure resulting from the increases in salaries and wages granted to employees in almost all spheres of the economy, higher incomes generated by the record export earnings of the mining and agricultural sectors, the current low level of stocks and the large capital expenditure programme announced by the government sector and public corporations, may be expected to lead to the fuller utilisation of productive capacity and eventually to an increase in new fixed investment.

Running-down of inventories

During the year under review the book value of inventories (excluding the value of livestock) increased by only about R150 million or $1\frac{1}{2}$ per cent, as against $12\frac{1}{2}$ per cent and $5\frac{1}{2}$ per cent during 1970/71 and 1971/72, respectively. If the value of inventories is adjusted for price increases in excess of the average price level during the year under review inventories actually decreased by approximately R250 million in 1972/73, as against an increase of only about R25 million in 1971/72. It is furthermore of importance that during the year under review practically no addition was made to industrial and commercial inventories. The increase of R150 million was accounted for mainly by agricultural stocks. With the gross domestic product at current prices rising at a relatively high rate, the ratio of the average book value of non-agricultural inventories to the gross domestic product declined to about 32 per cent for the year that ended on 30 June 1973, compared with nearly 37 per cent for the preceding year.

The present low level of inventories is clearly evident from the accompanying graph which shows the inventories-to-sales ratio of the manufacturing and trade sectors, excluding the motor trade. A sharply declining tendency in the ratio occurred since the first quarter of 1971. However, the current low level of inventories as well as the expected acceleration in sales may in due course lead to an inventory build-up which could provide a strong stimulus to manufacturing production and a faster rate of growth in overall economic activity.

Inventories as percentage of sales



Substantial further increase in gross domestic saving

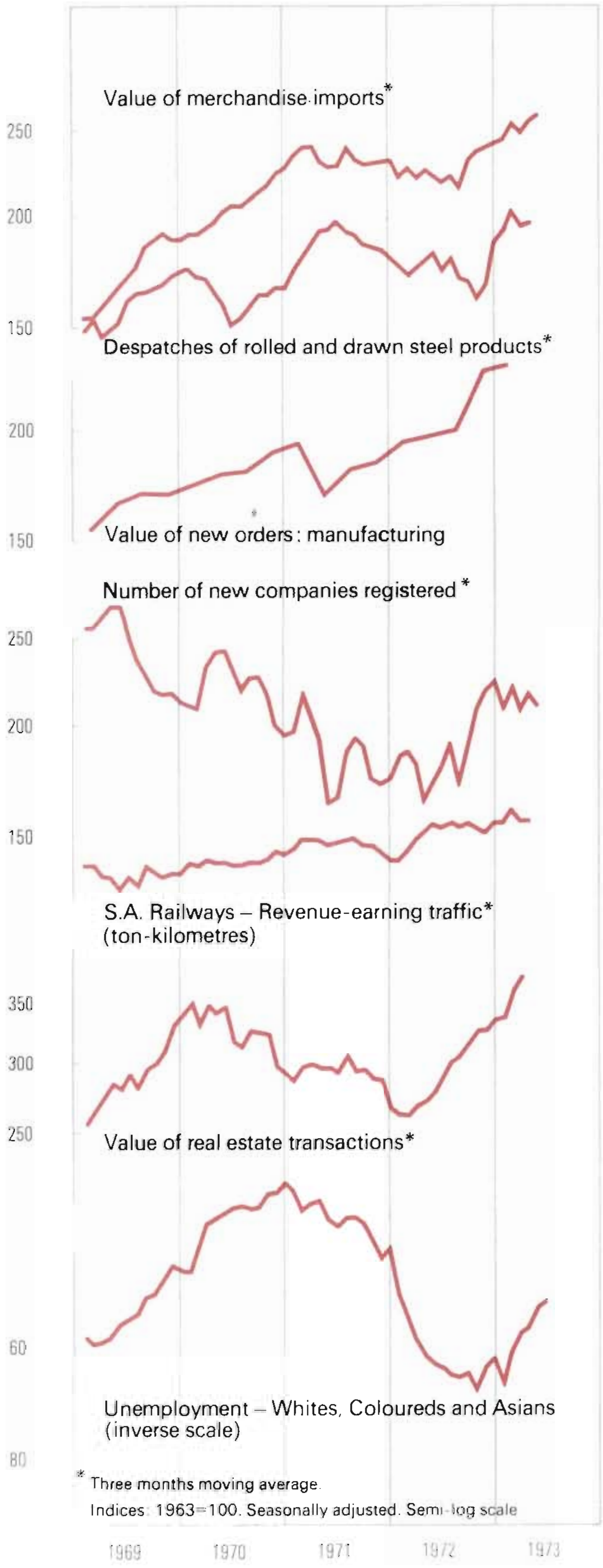
After having increased by no less than 32 per cent in the year that ended on 30 June 1972, gross domestic saving recorded a further pronounced rise of 22 per cent during 1972/73. The two main components that accounted for this increase were the current surplus of the general government and corporate saving. These increases can, in turn, to a large extent be ascribed to the marked rise in the profits of mining companies which, on the one hand, led to a substantial increase in tax receipts and therefore the current surplus of the government, and, on the other hand, to higher undistributed profits in the mining sector. Corporate saving originating in the mining sector consequently more than doubled during the past year. Provision for depreciation showed its normal increase but personal saving showed little change after it had increased by no less than R500 million during the preceding year.

The overall result of the substantial increase in gross domestic saving was that the ratio of gross domestic saving to gross domestic product rose to 25 per cent in 1972/73, which was one percentage point higher than the annual average for the previous ten years. In addition the sharp increase in gross domestic saving resulted in an excess of domestic saving over domestic investment in 1972/73 for the first time since 1968/69.

Revival in general business conditions

General economic indicators show that the South African economy was in a downward phase of the business cycle from early in 1971 until late in 1972. During the course of 1971 the lower growth rate was accompanied by the disappearance of excess domestic demand and a reduction in the rate of increase in prices. In such circumstances the balance of payments usually changes from a deficit to a surplus,

General indicators



* Three months moving average.
Indices: 1963=100. Seasonally adjusted. Semi-log scale

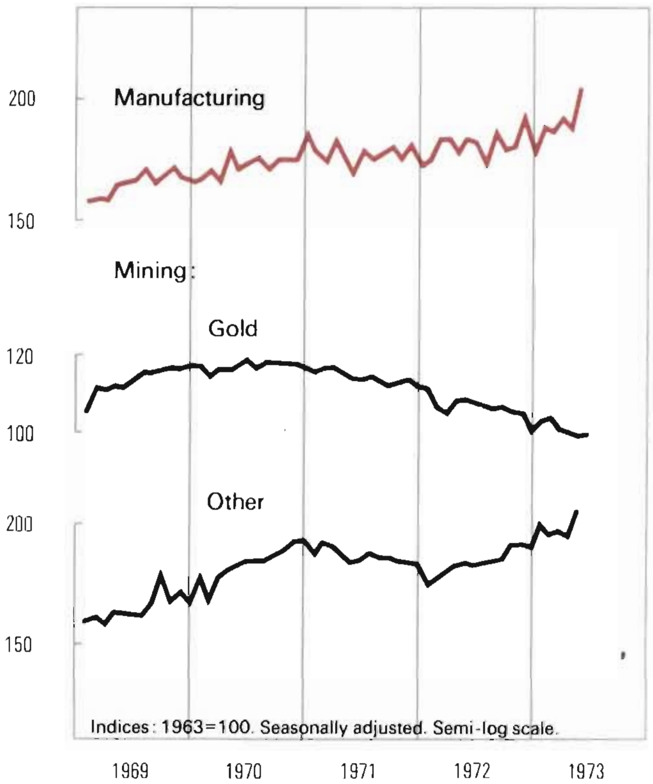
but in 1971 financial developments abroad prevented this from happening and the decline in the gold and other foreign reserves continued to restrain expansion until the end of 1971. The economy, therefore, needed stimulation without aggravating the balance of payments problem. In view of the general realignment of exchange rates in December 1971, the devaluation of the rand was the obvious way of attaining these two goals at the same time. Further moderately expansionary measures were introduced by the Government in both the 1972 and 1973 Budgets and a generally easy monetary policy was pursued during 1972 and the first half of 1973. Although the general revival of economic activity was slow to take effect, various general economic indicators began to turn upwards from the beginning of the fourth quarter of 1972.

A statistical analysis of a large number of business cycle indicators, published in the June 1973 *Quarterly Bulletin* of the Reserve Bank, reveals a lower turning point of the business cycle in October 1972. Until the second quarter of 1973 the revival was very moderate, but there are quite a number of expansionary forces at work that will stimulate the economy further. These include the healthy balance of payments situation with rising foreign reserves increasing the availability of funds and reducing interest rate levels, the increase in domestic incomes generated by higher earnings from gold production and other export commodities, the substantial increases in salaries and wages that may lead to a further rise in consumer spending, the low level of inventories which may reduce the time lag between increased demand and higher production, the easier labour situation, and the existence of unused capacity in certain sections of industry.

Revival in manufacturing production

A welcome development during the year under review was the revival in manufacturing production. In contrast to the decline in the growth rate during the preceding two years the growth rate in the volume of manufacturing production accelerated from 1,8 per cent in 1971/72 to about 5 per cent during 1972/73. This rate of increase is still lower, however, than the average growth rate of 6,4 per cent needed according to the Economic Development Programme to obtain an average overall growth rate in the economy of $5\frac{3}{4}$ per cent for the period 1971 to 1977. Nevertheless, the index of the physical volume of manufacturing production indicates a relatively sharp upturn from the fourth quarter of 1972 and this acceleration was continued during the first five months of 1973. In fact, the average level of the index in the first five months of 1973 was 6,9 per cent higher than the level for the corresponding period of the preceding year. It is also noteworthy that the production of durable goods, which had shown virtually no change during 1971 and the greater part of 1972, has recovered markedly since the fourth quarter of 1972. This, in turn, may be ascribed to relatively large increases in the output

Physical volume of production



of basic metals and metal products, transport equipment and non-metallic mineral products. The higher level of activity in the manufacturing sector was also reflected in a higher degree of capacity utilisation during the fourth quarter of 1972 and the first quarter of 1973. With the low level of inventories and with domestic and foreign demand for manufactured goods rising, the volume of manufacturing production is expected to increase further during 1973.

The revival in manufacturing output was also accompanied by an improvement in output per man-hour. As the accompanying table shows, production per man-hour either declined or increased at a very low rate during 1970/71 and 1971/72 as a result of under-utilisation of production capacity and a certain degree of labour hoarding. In 1972/73, the position changed and output per man-hour rose by about 2 per cent probably owing to the fuller utilisation of the available production capacity and the better use made of labour resources.

Manufacturing — output per man-hour

Percentage change

Year ended 30 June	Manufacturing production	Hours worked	Production per man-hour
1970	8,0	6,9	1,0
1971	4,0	4,1	—0,1
1972	1,8	1,4	0,5
1973*	3,8	1,8	2,0

*Figures up to April 1973 compared with figures for corresponding period during the preceding year.

New prosperity for the gold mining industry

For nearly a century, the gold mining industry contributed to the promotion of growth and stability in the domestic economy and has been by far the most important foreign exchange earner, supplying foreign exchange for the development of industry and commerce in South Africa. During the late nineteen fifties and nineteen sixties, the relative importance of the gold mining industry in its contribution to gross domestic product and to exports tended to diminish as a result of the fixed price of gold, which, together with the continued increase in costs, left large quantities of lower grade ore uneconomical to mine. Thus, the number of kilograms produced declined continuously since the middle of 1970, whereas the value of the gold production declined from middle-1969 to middle-1970 and then increased gradually until the end of 1971 before rising sharply during 1972 and the first half of 1973.

From the end of 1971 the sharp and sustained rise in the gold price on the private market as a result of the uncertainties on the international financial scene, brought new prosperity to the industry. After rising only slightly from R26,7 per fine ounce in 1969/70 to R27,0 in 1970/71, the average price of gold on the London market rose sharply to R34,6 in 1971/72 and to no less than R57,5 in 1972/73. The increase during the last eighteen months of 148 per cent was even more spectacular, as shown in the accompanying graph.

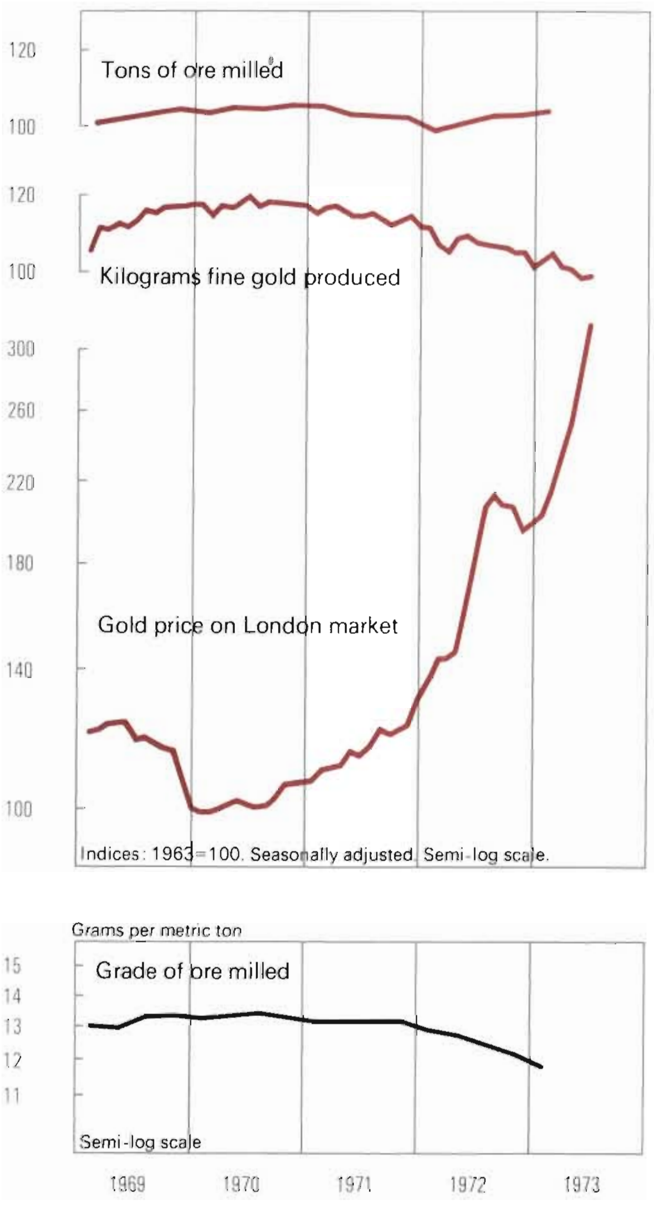
The buoyant conditions in the gold mining industry have already had and will continue to have effects throughout the economy. For the industry itself, profits increased by more than 70 per cent in 1972/73 and this enabled gold mines to increase salaries and wages to their employees, pay out higher dividends, make a substantially larger contribution to government income and still retain undistributed profits of more than double the amount of the preceding year. These higher cash flows exert an important expansionary influence on the economy as a whole.

Another important development is that substantial reserves of low grade goldbearing ore previously uneconomical to mine have now become profitable. In order to prolong the life of existing mines, the average grade of ore mined has been reduced substantially, especially since the beginning of 1972, as shown in the accompanying graph. Although the physical volume of gold ore milled increased somewhat since the beginning of 1972, the number of kilograms fine gold produced declined by 5,1 per cent in 1971/72 and by a further 6,6 per cent in 1972/73.

For the domestic economy as a whole, the new prosperity in the gold mining industry has had important effects. Gold mining's contribution to the gross domestic product at current prices rose by no less than 44 per cent in 1972/73, whereas the decline in the volume of gold production of 6,6 per cent was recorded as a reduction in the real *domestic* product. However, the large increase in the price of gold made a significant contribution to the improvement in the terms of trade and consequently to the much higher rate of increase in real gross *national* product, as already indicated above. Expansion programmes in the gold mining industry have already been reflected in increases in fixed investment. Moreover, higher dividend payments and increased salaries and wages, which have not as yet worked through fully to final demand, should also have an expansionary effect on economic activity.

The most outstanding direct effect of the increase in the price of gold is, of course, its influence on the balance of payments. Net gold output has always been the most stable component in South Africa's balance of payments, but has tended to decline in relative importance owing to the fixed price of gold. In 1971/72, however, the value of the net gold output, as reflected in the balance of payments, increased by 16,9 per cent and in 1972/73 rose by a further 41,1 per cent from R1 015 million in 1971/72 to no less than R1 432 million.

Gold mining



Sharp increase in non-gold mining production

Non-gold mining production, which had shown a declining tendency during calendar year 1971, increased sharply and almost uninterruptedly from the beginning of 1972. For the eleven months until May 1973 the index of the volume of non-gold mining production was on average 6,0 per cent higher than for the comparable period a year ago, but for the first five months of 1973 the average of the index was 11,6 per cent higher than during the same months in 1972. Major contributions to this increase were made by platinum, manganese, coal and asbestos. Substantial increases in the prices of metals and minerals, particularly on international markets, and a running-down of inventories led to an even higher increase in the proceeds from the sale of non-gold mining products. During the period July 1972 to April 1973, the value of sales were about 26 per cent higher than for the same period a year ago.

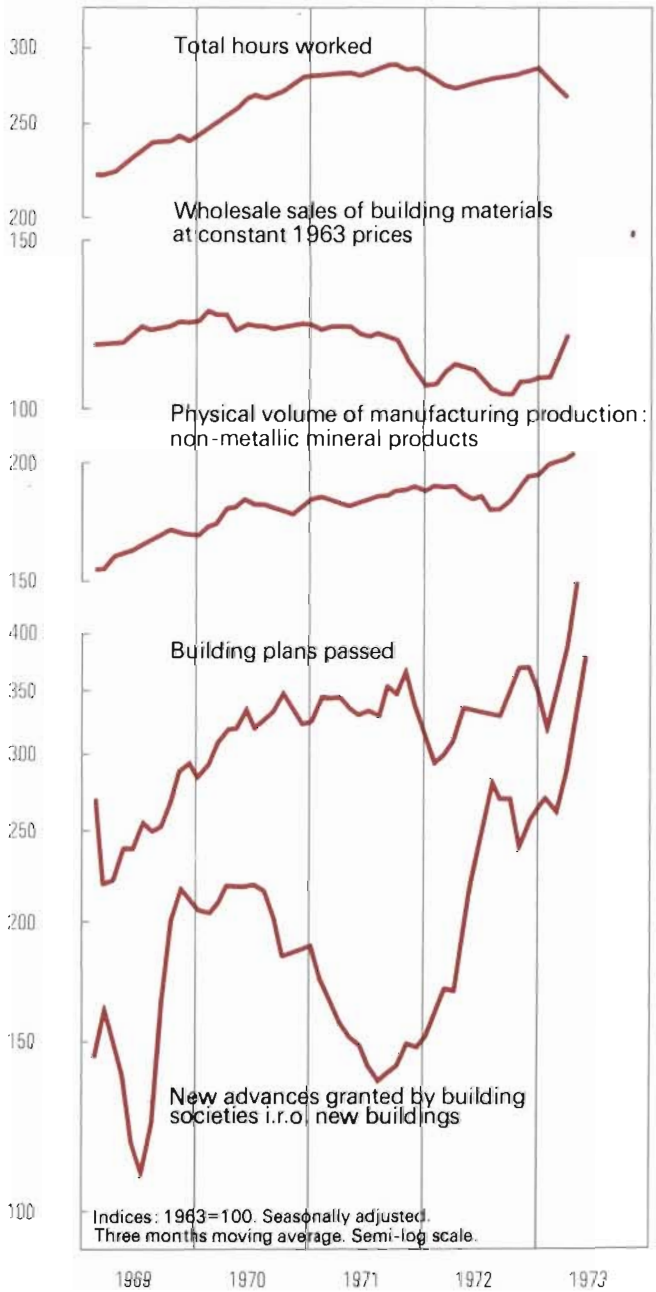
Increase in building and construction activity

During the fourth quarter of 1972 and the first four months of 1973 sharp and sustained increases were recorded in certain indicators of activity in the building and construction industry, such as wholesale sales of building materials, the physical volume of production of non-metallic mineral products (including building bricks and tiles, glass products, cement and cement products and composite boards and sheets), advances granted by building societies for new buildings and the total value of building plans approved. Total hours worked, however, showed a different tendency. After increasing during the last nine months of 1972, to a level still below that reached during the second half of 1971, total hours worked declined sharply during the first quarter of 1973. This may indicate a rise in building and construction activity associated with an increase in output per man-hour, a welcome development which may have been induced by the better utilisation of the existing labour force under competitive conditions and rising salaries and wages.

From official information on the value of building plans approved and buildings completed as well as certain general indicators it is evident that the bulk of building activity is presently directed to the construction of residential buildings, particularly private residential dwellings. Non-residential construction may take a little longer to revive owing to the existing surplus supply of office and shop space in certain centres and the existence of surplus production capacity in the manufacturing sector.

An alarming development in this sector is the sharp acceleration in the wholesale prices of building and construction materials during the year under review. After increasing at an average annual rate of 3,7 per cent from June 1967 to June 1972, these prices accelerated to an annual rate of no less than 11,2 per cent from June 1972 to June 1973. Until recently a major portion of the price increases was absorbed by the industry owing to the highly competitive conditions during approximately the last eighteen months.

Construction

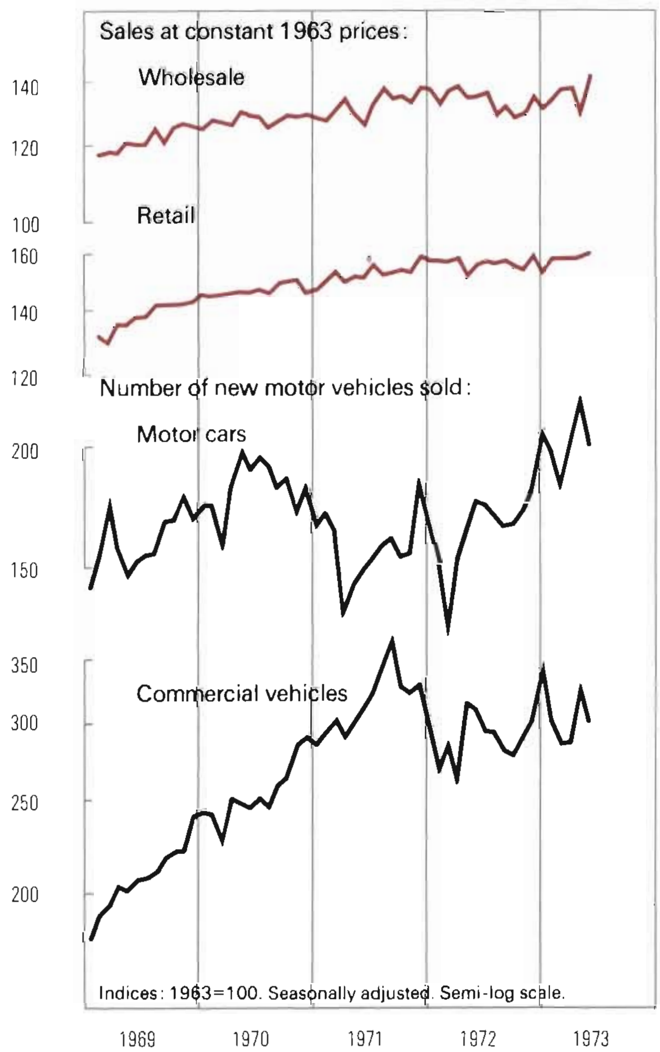


Improvement in trading conditions

As mentioned above, the general upward adjustments in salaries and wages of various labour groups and other expansionary forces currently at work in the economy have not as yet worked through fully to final consumer demand. Nevertheless, the average seasonally adjusted index of retail sales at constant prices, which had shown a declining tendency during the course of 1972, increased at an annual rate of 3,6 per cent from the second half of 1972 to the first five months of 1973. After showing a declining tendency during the first three quarters of 1972, wholesale sales at constant prices increased since the fourth quarter.

One branch of commerce which is experiencing buoyant conditions is the motor trade. The number of new motor cars sold during the first six months of 1973 was 18 per cent higher than in the second half of 1972 and no less than 29 per cent higher than during the first six months of 1972. Expenditure on new motor cars was almost exclusively responsible

Commerce



for the sharp increase in private consumption expenditure on durable goods during 1972/73. Sales of commercial vehicles did not increase to the same extent, a development reflecting the low growth rate in overall economic activity that has been experienced during the past two years. The number of such vehicles sold during the first half of 1973 was, nevertheless, 6 per cent higher than sales during the second half of 1972.

Labour situation

In conformity with economic developments as described above, total non-agricultural employment increased at higher rates in the fourth quarter of 1972 and the first quarter of 1973. During the nine months that ended on 31 March 1973, total non-agricultural employment was 1,8 per cent higher than during the same period of the preceding year. Noticeable increases in employment were recorded in the sectors gold and other mining, commerce and the Post Office.

The number of registered unemployed Whites, Coloureds and Asians showed similar changes. After increasing almost uninterruptedly from 7 624 in December 1970 to 13 326 in October 1972, it declined fairly sharply to 10 521 in June 1973. As a percentage of the comparable labour force in the non-agricultural sectors of the economy, the number of unemployed Whites, Coloureds and Asians declined from 0,72 per cent in the third quarter of 1972 to 0,6 per cent in the second quarter of 1973.

Notwithstanding relatively easy conditions in the labour market during approximately the past two years, increased demands for upward adjustments to salaries and wages continued on the ground of rises in the consumer price index. Substantial upward adjustments were made towards the end of 1972 and the first half of 1973. The accompanying table shows that real earnings per worker have been increasing steadily every year and that the average worker was about 17,3 per cent better off, in terms of real purchasing power, in 1972/73 than five years ago. Moreover, the average annual percentage increase of 3,2 per cent in the real remuneration of employees over the last five years is substantially higher than the annual average increase in the real national product per capita of 2,1 per cent.

Percentage change in consumer prices and remuneration per employee in the non-agricultural sectors

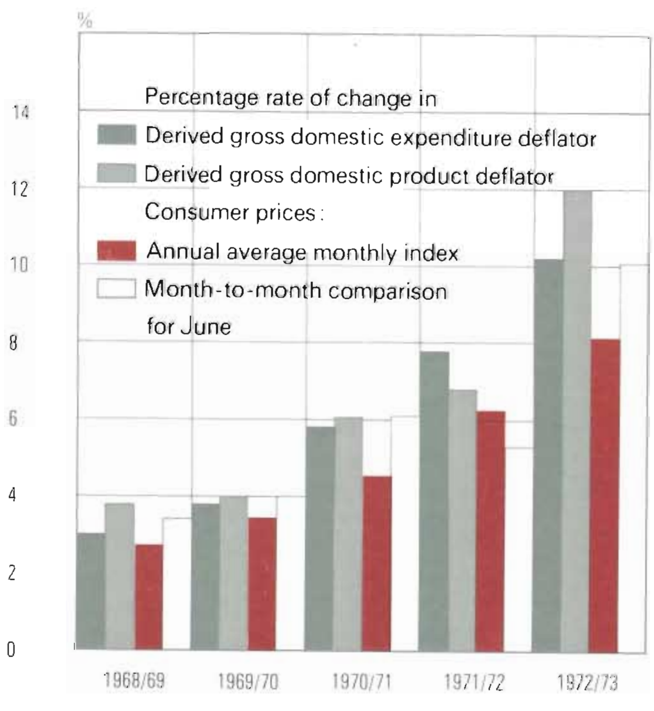
Year ended 30 June	Consumer prices	Remuneration per employee	Real purchasing power
1969	2,8	8,7	5,8
1970	3,5	8,0	4,3
1971	4,6	11,8	7,0
1972	6,3	9,2	2,8
1973	8,2	10,8	2,3
Average 1969 to 1973	4,5	7,9	3,2

Rapid rise in prices

The high rate of price increases is at present one of South Africa's, and for that matter one of the world's, most pressing problems. Because different statistical measures are often used to quantify the rate of inflation, it may perhaps be useful to identify the different measures of price increases and to indicate what each of them actually measures.

The gross domestic product deflator, as a measure of changes in prices of all goods and services produced in South Africa, rose by 12 per cent during 1972/73, compared with 7 per cent in 1971/72. Because a large proportion of goods produced in South Africa, including gold, is exported, the price rises of these export goods are incorporated in the gross domestic product deflator and during 1972/73, they contributed materially to the increase. It is, therefore, not surprising that during 1972/73 the gross domestic expenditure deflator, as a measure of the aggregate price rises of private consumption expenditure, government consumption expenditure and gross domestic investment increased at a substantially lower rate than the gross domestic product deflator, namely by 10½ per cent. Another well-known measure of price increases, namely the consumer price index rose by 8,2 per cent during 1972/73, when the average of the monthly indices for 1972/73 is compared with the average for the preceding year. From June 1972 to June 1973 consumer prices rose by 10,1 per cent. The former increase measures the change in the average level of prices between the two years, whereas the latter gives the change in the course of the year 1972/73, i.e. the more recent development.

Indicators of inflation



Consumer prices

Percentage rate of change in seasonally adjusted index

	June 1971—June 1972	June 1972—June 1973
Services	**6,0**	**9,5**
Housing	6,7	9,5
Other	4,9	9,5
Goods	**4,9**	**10,4**
Food	5,5	16,5
Furniture and equipment	5,0	6,9
Clothing and footwear	5,5	7,3
Vehicles	6,3	5,2
Other	3,1	6,4
Total	**5,3**	**10,1**

As shown in the accompanying table, the largest contribution to the sharp rise in consumer prices during the year under review was made by the exceptionally high rate of increase in food prices. Clothing and footwear and services also recorded large increases. The rapid rise in food prices may in the first place be ascribed to adverse weather conditions prevailing in large parts of the country, but also to significant upward adjustments in agricultural prices controlled by the government. These increases were granted on the basis of marked rises in production costs per unit. Domestic consumer prices were furthermore seriously affected by changes in exchange rates during the course of 1971/72 and 1972/73.

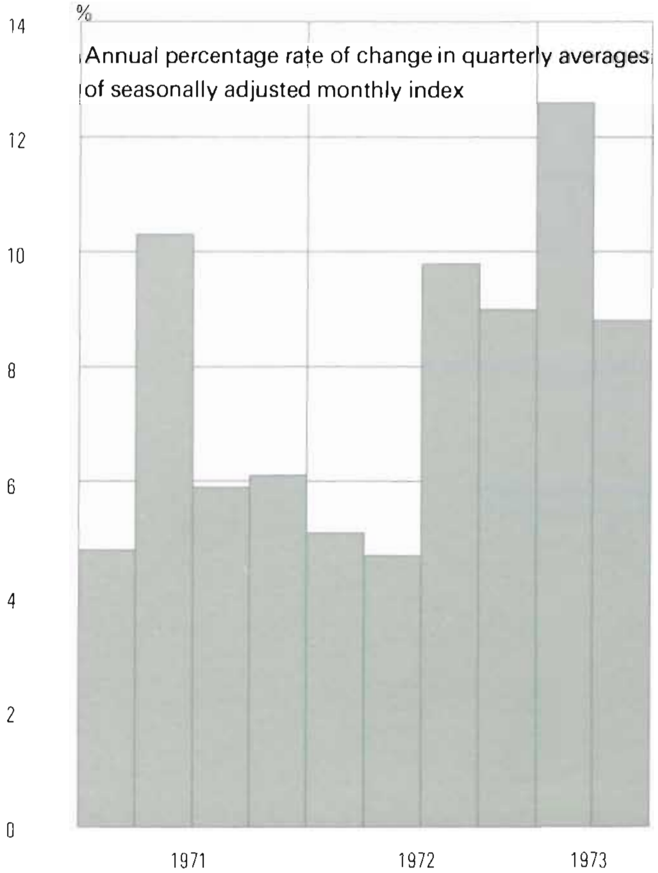
On the basis of average quarterly increases taken at an annual rate, as shown in the accompanying graph, it would appear that a peak was reached in the first quarter of 1973 and that the rate of increase in the second quarter of 1973 was noticeably lower.

Largely as a result of the same causal factors, the rate of increase in the wholesale prices of goods for domestic consumption accelerated from 7,3 per cent between June 1971 and June 1972 to as much as 13,3 per cent over the subsequent twelve months. The main contributory factor was an escalation in the prices of South African produced agricultural goods from 6,7 per cent to 23,7 per cent over the same period, while the rate of increase in prices of imported goods declined slightly from 11,8 per cent to 10,7 per cent over the comparable period.

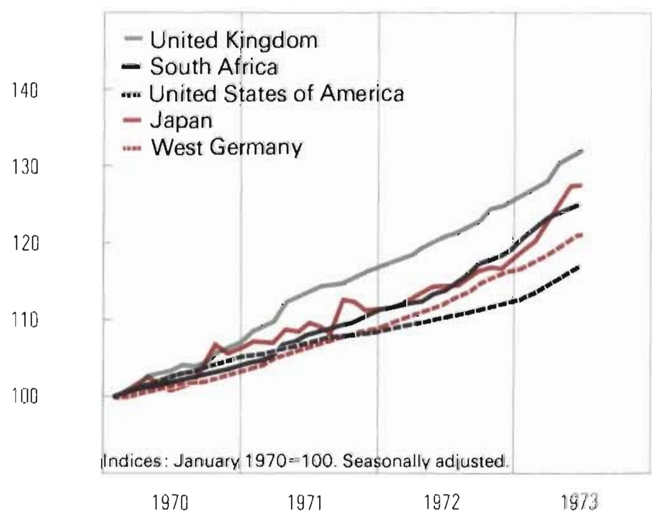
During the year under review, the trend in the prices of imported goods changed significantly. Following the realignment of currencies in December 1971, prices of imported goods increased sharply at an annual rate of 16,8 per cent up to October 1972. In the following months to June 1973, however, the annual rate of increase slowed down appreciably to 8,8 per cent.

A comparison of the rate of increase in the consumer price index for a number of countries reveals that the problem of inflation is not limited to South Africa, but has become more of a world-wide phenomenon. As the accompanying graph shows, the increase in the consumer price index during the past few years was lower in South Africa than in the United Kingdom and Japan, but higher than in Western Germany and the United States.

Consumer prices



International comparison of consumer prices



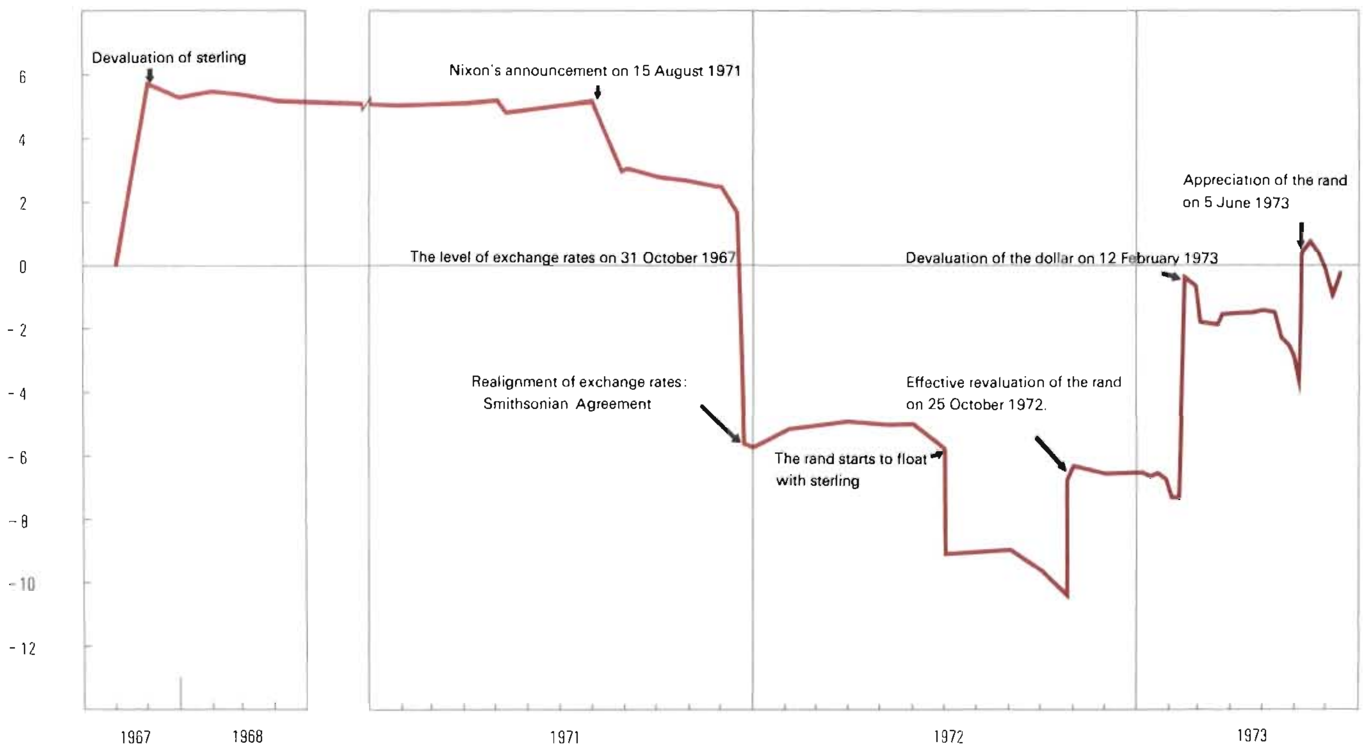
Balance of payments

International financial developments and South Africa's exchange rate policy

During recent years the South African economy and, in particular, the South African balance of payments has been influenced to a great extent by developments in the international monetary sphere. After a period of relative stability during the nineteen fifties and a large part of the nineteen sixties, foreign exchange markets have been characterised by unsettled conditions starting from the devaluation of sterling by 14,3 per cent in November 1967. This was followed by the introduction of the two-tier system for the marketing of gold in March 1968, the devaluation of the French franc in August 1969, the revaluation of the German mark in October 1969, the flotation of the Canadian dollar from the end of May 1970, and the revaluation of the Austrian schilling and Swiss franc and the flotation of the currencies of Germany and the Netherlands in May 1971.

The South African authorities maintained the gold parity of the rand during this period of uncertainty, because the balance of payments was fairly strong, the domestic economy was expanding satisfactorily and skilled labour and capital were in short supply. Although the parity of the rand was kept unchanged, changes in the exchange rates of some of South Africa's trading partners brought the rand at the beginning of 1971 to a weighted average value in terms of all other currencies which was about 5 per cent higher than its level before the 1967 devaluation of sterling (see accompanying graph). The announcement on 15 August 1971 that the United States was no longer prepared to convert officially held dollars into gold or other reserve assets, and the decision of the major industrial countries to let their currencies float, forced South Africa to reconsider its exchange rate policy. At that time it was expected that the value of the dollar would depreciate, and since it was considered undesirable for the rand to appreciate further, the authorities decided to quote buying and selling rates for the rand in dollars. On 18 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 to varying degrees. At that stage South Africa's total gold and other foreign reserves had declined from a peak of R1 235 million at the end of March 1969 to only R570 million at the end of November 1971. The domestic economic activity was sluggish and an expansionary policy was called for. Consequently on 21 December 1971 it

Effective depreciation (−) or appreciation (+) of the rand (Cumulative from 31 October 1967)



was decided to devalue the rand by 12,28 per cent and, at the same time, to quote buying and selling rates for the rand in sterling in stead of in U.S. dollars. This brought the effective exchange rate of the rand down to about 6 per cent below its level on 31 October 1967 and to about 11 per cent below its level on 15 August 1971.

This exchange rate policy, coupled with favourable prices for South African exports on international commodity markets, led to a marked improvement in the balance of payments. The overall deficit on South Africa's balance of payments of R239 million during 1971 thus changed to a surplus of R184 million during the first six months of 1972. Continued pressure on sterling compelled the United Kingdom to allow the pound to float as from 30 June 1972. At that time it was expected that sterling would depreciate and South Africa was faced with the problem whether to depreciate along with its main trading partner or to appreciate against it. It was decided to maintain the fixed exchange rate of the rand with sterling, because the balance of payments had just started to improve, the gold and other foreign reserves had not yet reached a satisfactory level and the achievement of a more rapid growth rate was a matter of high priority.

Consequently, at the beginning of the year under review, the rand depreciated with sterling to an average level about 10 per cent below its effective exchange rate at the end of October 1967 or approximately 15 per cent below its level on 15 August 1971, before it was decided that the circumstances had changed to such an extent that an appreciation of the rand was desirable. A new par value was established for the rand on 25 October 1972, which represented a devaluation of 4,2 per cent in terms of gold. By comparison with market exchange rates which prevailed on the previous day for the rand against all currencies except sterling, however, this decision in practice represented an effective appreciation of approximately 3 per cent.

After 25 October 1972 the rand was linked to the dollar and depreciated slightly until the announcement by the United States of another devaluation of the dollar by 10 per cent on 12 February 1973. South Africa decided to maintain the par value of the rand, because the gold and other foreign reserves had reached a level of R1 124 million at the end of January, the economic climate was much more conducive to faster economic growth and a deflationary effect would be gained by an effective appreciation of the rand. The average effective exchange rate of the rand, therefore, increased to approximately 1 per cent below the level attained before the devaluation of sterling in 1967 and to about 6 per cent below its level on 15 August 1971.

Subsequently, conditions in foreign exchange markets remained unsettled and on 19 March the EEC countries, with the exception of the United Kingdom, Ireland and Italy, decided to float together against all other currencies, while the German mark was revalued by 3 per cent to facilitate this step. After 19 March the dollar and the rand remained steady for several weeks, but then began to depreciate somewhat again. On 4 June 1973 the rand reached an effective exchange rate against all other currencies of about 4 per cent below its level on 31 October 1967 and approximately 9 per cent below its level on 15 August 1971.

A depreciation of the rand to that extent was not considered desirable, because the balance of payments had improved satisfactorily, the gold and other foreign reserves had reached a new record level, and a depreciation would aggravate the already high rate of inflation. Consequently the Government announced that from 5 June 1973 the Reserve Bank would quote new buying and selling rates for the US dollar which represented an appreciation of the rand against the dollar, and therefore against all other currencies, by about 5 per cent. The gold parity of the rand was, however, maintained unchanged and the rand price for gold remained at R29,75 per fine ounce. Taking into account changes in other exchange rates, this step amounted to an effective appreciation of the rand by about 5 per cent. Subsequently the rand again depreciated with the dollar. On 29 June the German mark was revalued by another 5,5 per cent.

Exchange rate policy during the larger part of the year under review was aimed at an effective appreciation of the rand particularly with the view to combat the high rate of inflation and taking into account the fact that an economic revival was already under way. The appreciation of the rand brought the average effective exchange rate of the rand to about the level of 31 October 1967, or to about 5 per cent *below* the level on 15 August 1971. Against the currencies of South Africa's main trading partners, the rand has naturally appreciated or depreciated in varying degrees. For example, against the US dollar the rand has appreciated by 6,4 per cent and against sterling by 17,3 per cent from 31 October 1967 to 13 July 1973, whereas it has depreciated vis-à-vis the German mark by 37,4 per cent, the Swiss franc by 29,6 per cent and the Japanese yen by 21,5 per cent over the same period.

Substantial improvement in overall balance

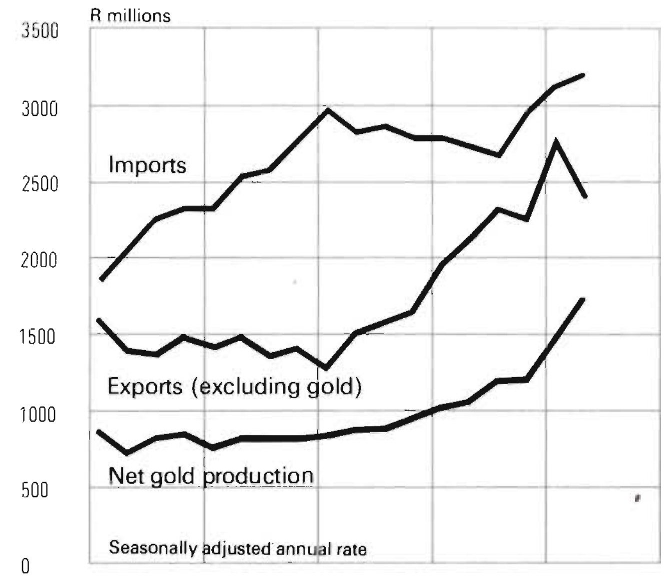
As indicated above, the overall balance of payments improved substantially over the past two years from a deficit of R359 million in 1970/71 to a surplus of R503 million in 1972/73. This marked improvement occurred in spite of a decline in the net inflow of capital and was the result of a change from a large

Overall balance on balance of payments
R millions

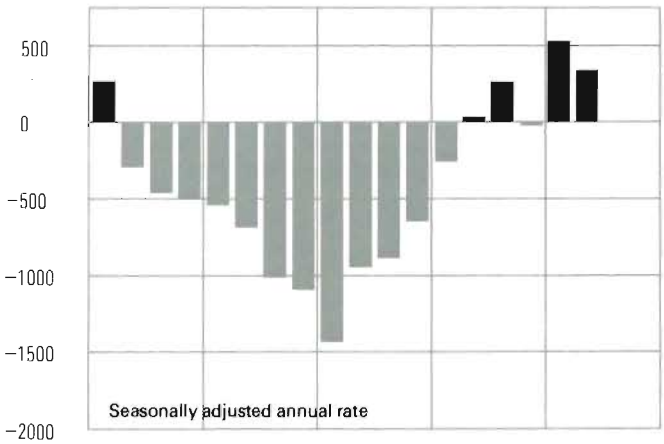
Year ended 30 June	Balance on current account	Net inflow of capital	Overall balance
1971	—1 111	752	—359
1972	—432	510	78
1973	268	235	503

deficit to a surplus on the current account of the balance of payments, owing to a sharp rise in merchandise exports and the net gold output, which outweighed the increase in the payments for merchandise imports and net services.

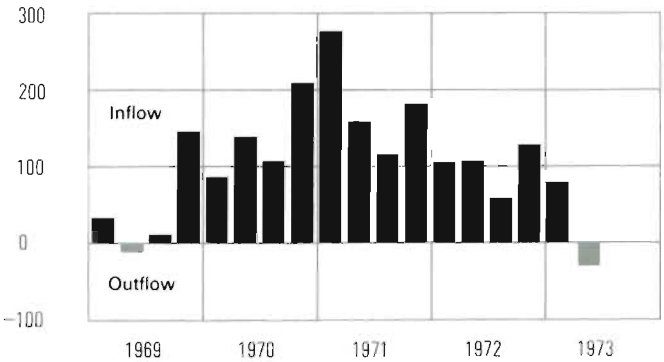
Balance of payments current account



Balance on current account



Total capital movements



Sharp increase in merchandise exports

After declining for two consecutive years, merchandise exports recovered remarkably during 1971/72 and 1972/73, when it increased by no less than 31 per cent and 33 per cent, respectively. Both the volume and the prices of merchandise exports rose, but the price rises contributed most to increases in the value of exports. The sharp increase in merchandise exports during 1972/73 is even more remarkable as poor agricultural crops led to reduced exports and the policy of exchange rate appreciation followed since October 1972 slightly lowered the rand proceeds of exported goods during the larger part of the year under review. Nevertheless, further substantial increases in prices on international commodity markets together with a higher volume of exports of mining and manufacturing products led to the substantial improvement.

Major contributions were made to the sharp increase in the value of merchandise exports during 1972/73 by diamonds, sugar, fruit, wool, base metals and, up to the end of April 1973, maize. A classification of exports by stage of production shows substantial increases in all the categories, with the exception of raw materials originating in mining which increased only moderately. It is indeed gratifying that the exports of manufactured goods increased in value and in volume and with all the export incentives granted by the authorities during the past two years, the prospects of higher exports of manufacturing products look promising.

Substantial rise in net gold output

As shown in the accompanying table, the net gold output increased phenomenally during the past year, owing to a rise of more than 50 per cent in the average price of gold on the private market. Although the volume of the net gold output declined during 1972/73, the value increased to such a high level that the balance of payments as a whole will be able to accommodate a higher domestic economic growth rate before the restraining effects of a balance of payments deficit will be felt. The increase in net gold output is even more remarkable when it is considered that up to April 1973, not all the newly-mined gold was sold. From April 1973, however, about all the newly produced gold has been sold on the private market.

Percentage increase and value of net gold output

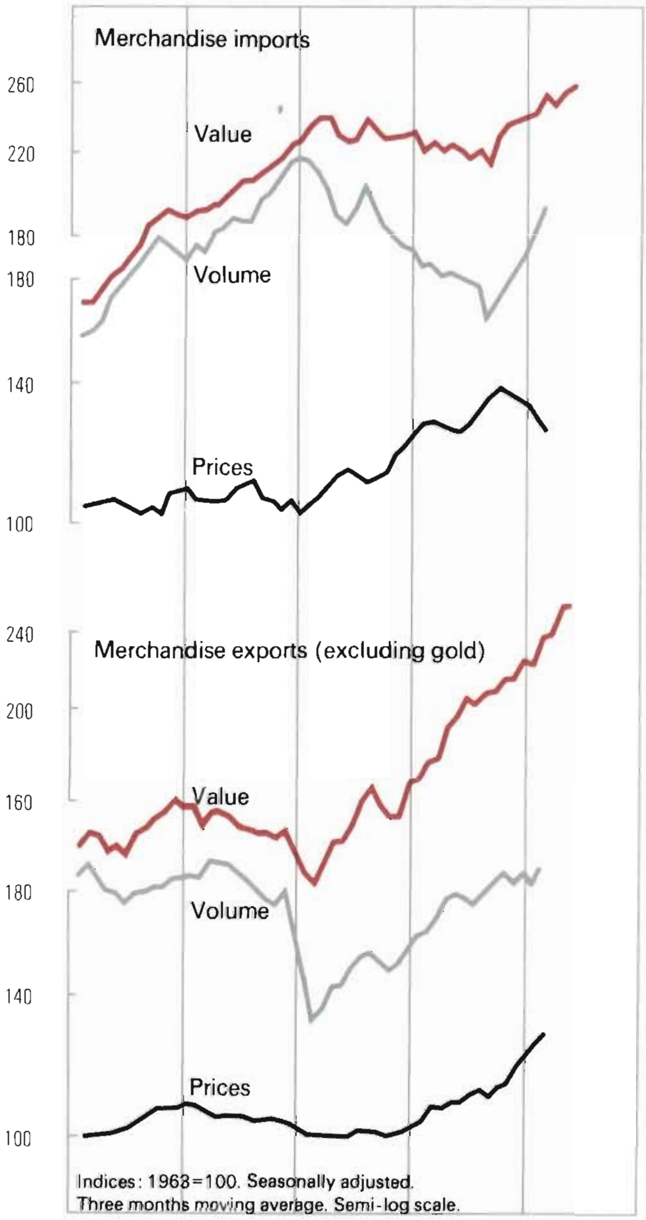
Year ended 30 June	Volume %	Price %	Value: Amount R m	Value: %
1971	—2,4	5,0	868	2,5
1972	—5,8	24,1	1 015	16,9
1973	—8,8	54,7	1 432	41,1

Moderate increase in merchandise imports

After increasing slightly by only 0,4 per cent in 1971/72, merchandise imports rose moderately by 7 per cent in the year that ended on 30 June 1973. The relatively slow rise in merchandise imports during the past two years can be attributed to a decline in the volume of imported goods during most of the period. This decline in the quantity of goods imported occurred under a relatively free import control system after the progressive relaxation of import control since July 1972 and is, therefore, related to the relatively low level of domestic demand for goods and services. Import prices, on the other hand, rose considerably from about the end of 1971 as a result of the depreciation of the rand and the high rate of inflation in most of South Africa's main trading partners.

As shown in the accompanying table, a reversal occurred in the declining trend in the value of merchandise imports from the fourth quarter of 1972. From about the same time the wholesale price index of imported goods increased at a lower rate. The volume of merchandise imports, therefore, started to rise during the last three quarters of the year under review in conformity with the revival in overall economic activity.

Merchandise imports and exports



Merchandise imports at a seasonally adjusted annual rate
R millions

1972:	1st quarter	2 820
	2nd quarter	2 766
	3rd quarter	2 692
	4th quarter	2 990
1973:	1st quarter	3 170
	2nd quarter	3 235

A classification of imports according to stage of use shows moderate increases in the imports of capital and consumer goods and a more pronounced increase in imports of intermediary goods during 1972/73. All the main types of products imported increased during 1972/73, except the imports of textiles, base metals, live animals and transport equipment. The largest contributions to the rise in merchandise imports were made by machinery and electrical equipment and chemical products.

Sharp rise in net invisible payments

Net invisible payments to the rest of the world increased by no less than 27 per cent during 1972/73, compared with a decline of 18 per cent in the previous year. This high rate of increase was the result of a substantial increase of R260 million in payments for services rendered by foreigners, which outweighed the moderate increase in service and net transfer receipts. Sharp increases occurred particularly in dividend and interest payments to foreigners, freight payments on merchandise imports and tourist expenditure abroad.

Smaller net inflow of capital

In contrast to the large net capital inflows of R752 million and R510 million recorded in 1970/71 and 1971/72, respectively, the net capital inflow in 1972/73 amounted to only R235 million. Various developments contributed to this significant decline in capital inflow. Firstly, exchange control measures were introduced in the United Kingdom on 23 June 1972 whereby transactions in securities of overseas Sterling Area countries are now 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 have to be

Net capital inflow
R millions

	Year ended 30 June		
	1971	1972	1973
Private sector	639	430	94
Net foreign purchases on Johannesburg Stock Exchange	91	161	1
Foreign long-term loans obtained by local authorities and public corporations	153	132	275
Other long-term capital	145	149	62
Short-term capital including errors and unrecorded transactions	250	— 12	—244
Central government and banking sector	113	80	141
Foreign long-term loans by central government	130	87	219
Other	—17	— 7	—78
Total net capital inflow	752	510	235

made with exchange obtained at a premium in the sterling securities market. As shown in the accompanying table, the net purchases by foreigners of securities quoted on the Johannesburg Stock Exchange consequently declined to a negligible amount.

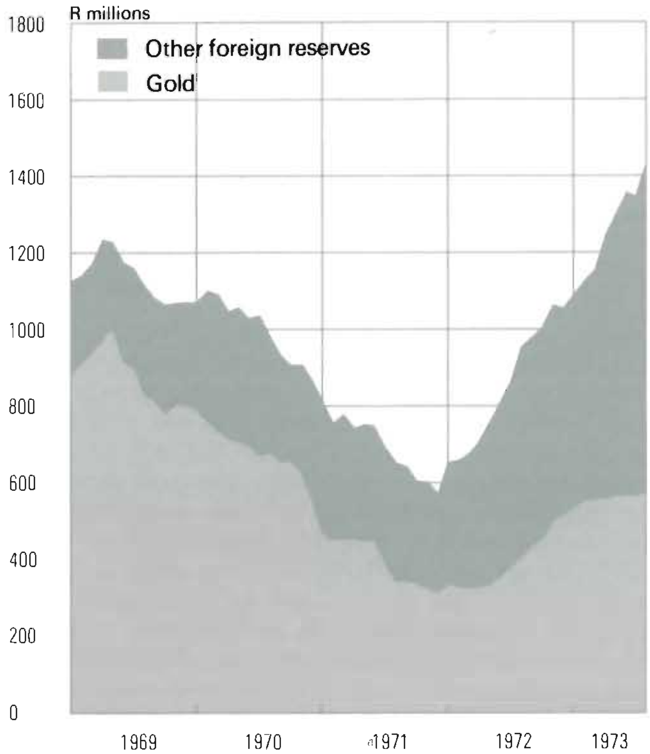
Secondly, more favourable conditions in the domestic capital market probably contributed to a large extent to the decline in the inflow of long-term capital to the private sector, other than loans of local authorities and public corporations. Thirdly, the central government and the Reserve Bank made large repayments on foreign loans owing to the favourable balance of payments position. Finally, the increased ability of domestic banks to extend credit at lower rates than those prevailing abroad and the continued uncertainty regarding exchange rates probably favoured domestic short-term financing of international trade.

Local authorities and public corporations, on the other hand, made increasingly more use of foreign borrowing in the financing of their development expenditure. The South African Railways and the Post Office also borrowed large amounts abroad.

Continued increase in gold and other foreign reserves

Balance of payments transactions accounted for an increase of R503 million in the gold and other foreign reserves during 1972/73. If valuation adjustments due to changes in exchange rates are taken into account, the total gold and other foreign reserves rose by R478 million during the year under review, compared with an increase of R172 million in 1971/72. From November 1971, the gold and other foreign reserves have increased almost continuously to a level of R1 341 million at the end of June 1973. During July 1973 the Reserve Bank's holdings of gold and other foreign reserves increased by R72 million to R1 268 million. The gold reserves of the Reserve Bank valued at the statutory price of R29,55 per fine ounce, amounted to R570 million at the end of July 1973 or about 45 per cent of its total gold and other foreign reserves.

Gold and other foreign reserves



Monetary and banking situation

During the year under review the main features of the monetary and banking situation were the considerable further easing of money market conditions as reflected in declining short-term interest rates and the rapid rise in the money and near-money supply, mainly as a result of the favourable balance of payments position and a substantial increase in domestic credit extension.

Monetary policy remained cautiously stimulative. Thus, the ceilings on bank credit were raised from 1 September 1972 and then abolished with effect from 1 November 1972, when the amended Banks Act of 1972 was implemented. The supplementary liquid asset requirements laid down under the amended Banks Act were fixed in such a manner that the banks were able to extend further credit to the private sector. Moreover, several reductions were made to interest rates quoted by the official sector, including Bank Rate, in conformity with the sharp drop in money market interest rates.

Large increase in the money and near-money supply

From June 1972 to June 1973 the money and near-money supply increased by a record amount of more than R1 000 million, or by 24 per cent, compared with much lower rates of increase during the preceding number of years. Moreover, the rate of increase accelerated considerably during the first half of 1973 compared with the second half of 1972, as the accompanying table shows.

Increases in money and near-money

Seasonally adjusted annual rates

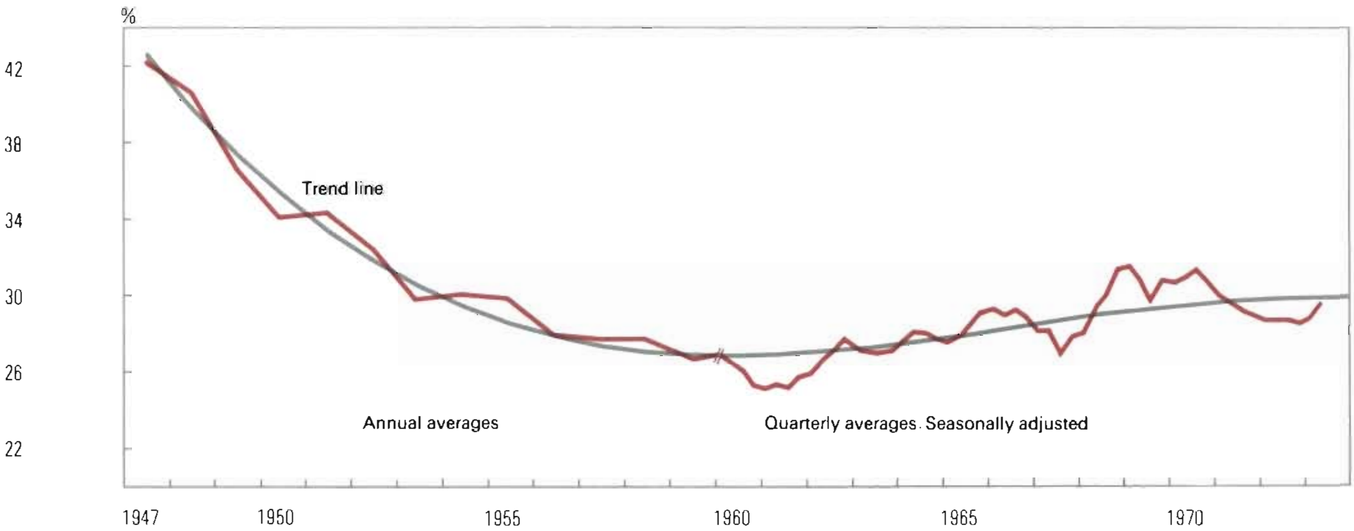
		%
1971:	2nd half	5
1972:	1st half	10
	2nd half	16
1973:	1st half	28

Ratio of money and near-money to gross domestic product

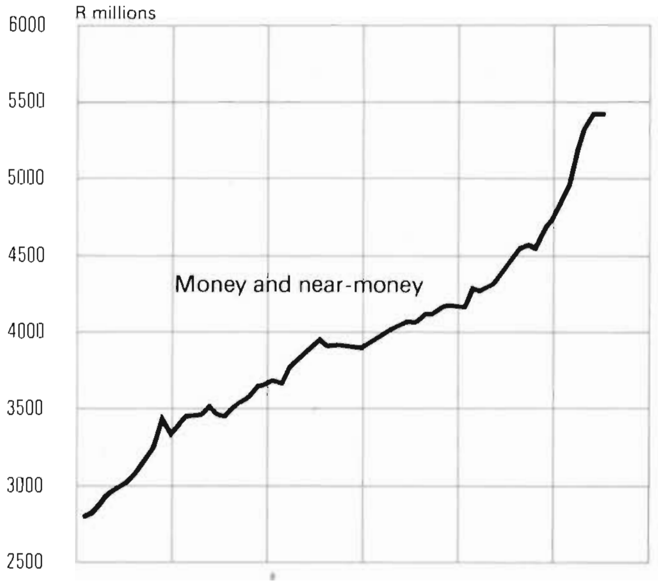
Although the supply of money and near-money increased at a substantially higher rate during 1972/73 than during preceding years, domestic and external prices also rose at a more rapid rate than before, with the result that the ratio of money and near-money to the gross domestic product at current market prices did not change significantly until the second quarter of 1973. The average ratio was 28,8 per cent during 1972/73, compared with 28,9 per cent for 1971/72.

To judge whether this ratio is high or low, it is useful to establish the long-term trend of the ratio by applying appropriate statistical techniques to the available historical data. The accompanying graph shows the ratio of money and near-money to the gross domestic product for the post-war period, together with a long-term trend line. The ratio declined from the very high figures recorded in the immediate post-war period, when private sector liquidity was

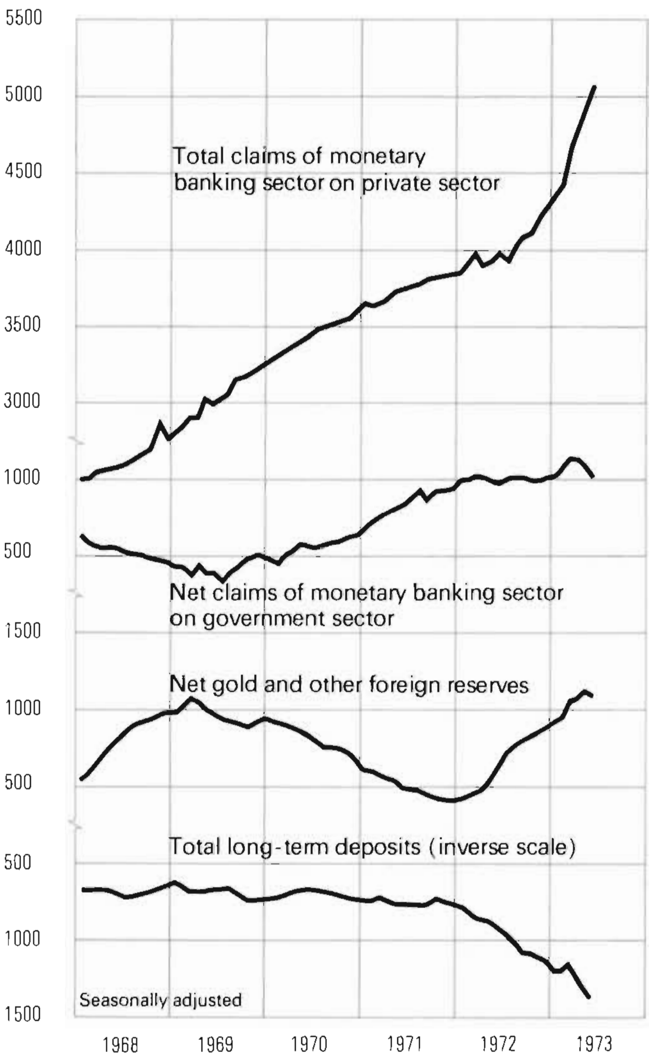
Ratio of money and near-money to the gross domestic product



Monetary analysis



Causes of changes in money and near-money



artificially high as a result of the war, to a very low level in 1961, before rising again to a new peak in 1969. Since then, the tendency of this ratio has been mostly downward. It is noteworthy that the ratio of money and near-money to the gross domestic product appears to have been below the long-term trend line since 1971. If the money supply alone (i.e. without near-money) is expressed as a ratio to the gross domestic product, the figure for the second quarter of 1973 does not deviate significantly from the long-term trend line.

Causes of changes in money and near-money

The sharp rise in the quantity of money and near-money during 1972/73 was caused mainly by the continuation of the rise in the gold and other foreign reserves which started from the end of 1971, and a large increase in bank credit to the private sector from August 1972. As might be expected in a period of strongly rising foreign reserves, the banking sector's net claims on the government sector did not increase significantly. At the same time long-term deposits of the private sector with the banking sector (which are excluded from the definition of money and near-money) rose markedly in conformity with the popularity of investments with building societies.

Causes of changes in money and near-money from 30 June 1972 to 30 June 1973
R' millions

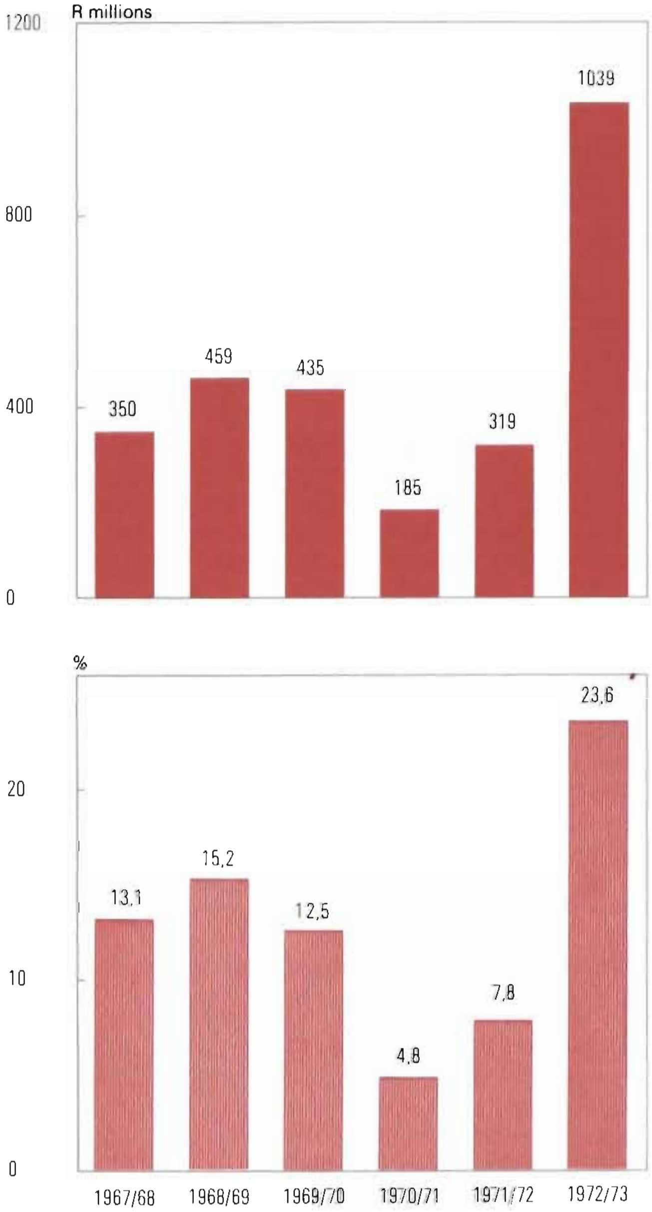
Net gold and other foreign reserves	+486
Claims on the government sector:	
Gross claims	+560
Government deposits*	—508
Net claims	+52
Claims on the private sector	+1 087
Long-term deposits*	—451
Net other assets	—134
Total money and near-money	**+1 039**

*Increase —, decrease +.

Large rise in domestic credit extension

Domestic credit extension, consisting of the change in bank credit to the private and government sectors, amounted to over R1 100 million during 1972/73, mainly as a result of a very large increase in bank credit to the private sector. Net bank credit to the government sector rose only very moderately during 1972/73, the third consecutive year in which the increase was smaller than during the preceding year. Bank credit to the private sector, on the other hand, showed a marked increase of over R1 000 million, or 28 per cent, during 1972/73. About two-thirds of this rise occurred during the first half of 1973, when the increase averaged well over R100 million per month. The strong revival in bank credit to the private sector from August 1972 stands in marked contrast to the

Changes in money and near-money

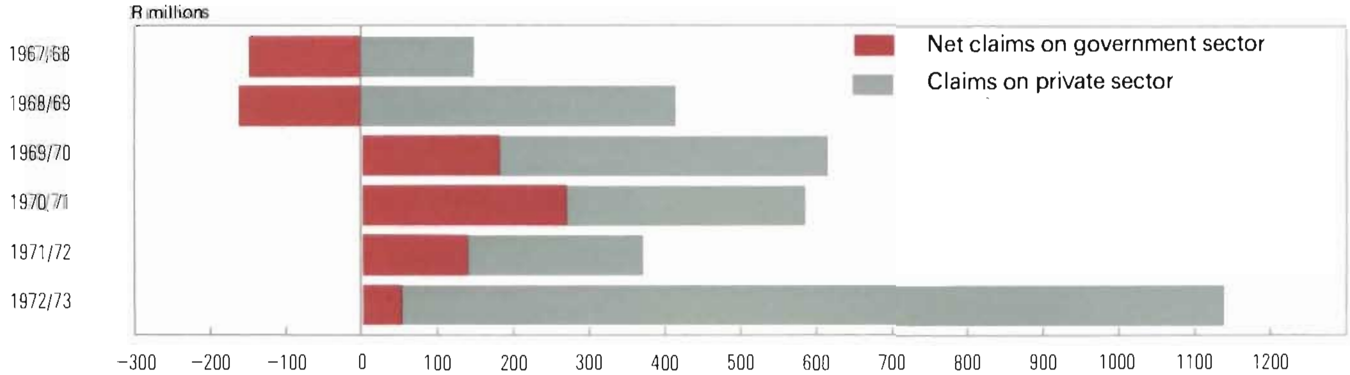


relatively mild increases of 9 and 6 per cent during 1970/71 and 1971/72, respectively, and with the almost stagnant level of commercial bank discounts and advances during most of these two years. Moreover, whereas about 40 per cent of the total increase in bank credit to the private sector during 1971/72 was accounted for by increased cash credit advances of the Land Bank, the latter's advances actually declined fairly markedly during 1972/73, in conformity with the change from bumper crops in 1971/72 to relatively poor crops in 1972/73. The other categories of banking institutions also contributed in different ways to the rise in bank credit to the private sector. Although the monetary hire-purchase and general banks' share of the total amount of outstanding discounts and advances as at the end of June 1972 was only about 16 per cent, this group contributed 33 per cent to the increase in the total discounts and advances to the private sector during 1972/73.

An analysis of the type of discounts and advances reveals that a significant portion of the increase (23 per cent) was in the form of hire-purchase discounts and advances and leasing, although these credits constituted only 11 per cent of the total amount of discounts and advances outstanding as at the end of June 1972. Moreover, if personal loans and open accounts are also taken into account, the total of consumer credit is estimated to have increased from slightly less than R1 500 million during 1971 to R1 634 million in 1972.

Another noteworthy feature of the extension of bank credit during the year under review was the marked increase in the use made of bill and acceptance finance. The banking sector's holdings of bankers' acceptances and trade and agricultural bills increased from R332 million to R550 million during 1972/73, i.e. by 66 per cent. This is in sharp contrast with a decrease of 13 per cent during the preceding year. This development was probably associated with the considerable widening of the margin between the cost of acceptance finance and the prime overdraft rate of commercial banks to 1 — $1\frac{3}{4}$ percentage points during the year under review. The discount rate on bankers' acceptances fell sharply in conformity

Changes in domestic credit extended by the monetary banking sector



with all the other money market rates, whereas the prime overdraft rate of commercial banks remained unchanged at 8½ per cent from 19 August 1972 to 16 April 1973, when it was reduced by ½ per cent. From 16 July this rate was lowered by a further ½ per cent to 7½ per cent.

Although the increase in hire-purchase discounts and advances and leasing can easily be explained by the rise in consumption expenditure on durable goods, mainly motor cars, the large increase in the other forms of bank credit cannot be related to other forms of domestic expenditure because the latter showed only moderate increases. A number of other factors may have caused the rise in bank credit. A shift may have occurred from foreign to domestic financing of imports and exports induced by the lower level of short-term interest rates in South Africa than abroad. Short-term interest rates in Britain moved in the opposite direction than those in South Africa during the larger part of the year under review, and the margin between comparable rates widened considerably, for example, the Treasury bill tender rate in Britain was 4,32 percentage points higher than the South African rate at the end of June 1973. The abolition of the ceilings on bank credit may have led to the extension of credit to certain clients which previously could not be accommodated by their banks under the then existing credit ceilings. With the lower level of interest rates, another factor that may have contributed to the rise in bank credit to the private sector may have been a shift towards credit extension by the banking system from inter-company lending outside the banking institutions.

The liquidity of banking institutions

The amount of surplus liquid assets of commercial banks, merchant banks and monetary hire-purchase and general banks was higher during 1972/73 than during the preceding year, namely at a monthly average ratio to liabilities to the public of 5,0 per cent compared with 3,8 per cent in 1971/72. At the end of June 1973 the surplus liquid assets of these banking institutions amounted to R239 million or 3,4 per cent of their liabilities to the public. The banks' liquidity situation was, therefore, such that they were able to extend further credit.

Supplementary cash and liquid asset requirements were laid down with the implementation of the amended Banks Act as from 1 November 1972. The minimum and supplementary cash and liquid asset requirements of all banking institutions were as follows:

(1) A minimum cash reserve balance at the South African Reserve Bank of 8 per cent of the banks' short-term liabilities to the public;

(2) A supplementary cash balance with the National Finance Corporation of 10 per cent of the banks' short-term liabilities to the public;

(3) Liquid assets (including cash reserves) amounting to the total of:

   (i) 45 per cent of the banks' short-term liabilities to the public,

(ii) 28 per cent of the banks' medium-term liabilities to the public,
(iii) 5 per cent of the banks' long-term liabilities to the public,
(iv) 10 per cent of the banks' acceptance liabilities.

The supplementary cash requirement with the National Finance Corporation was subsequently reduced to 7 per cent as from the date of certification of the banks' monthly return for March 1973.

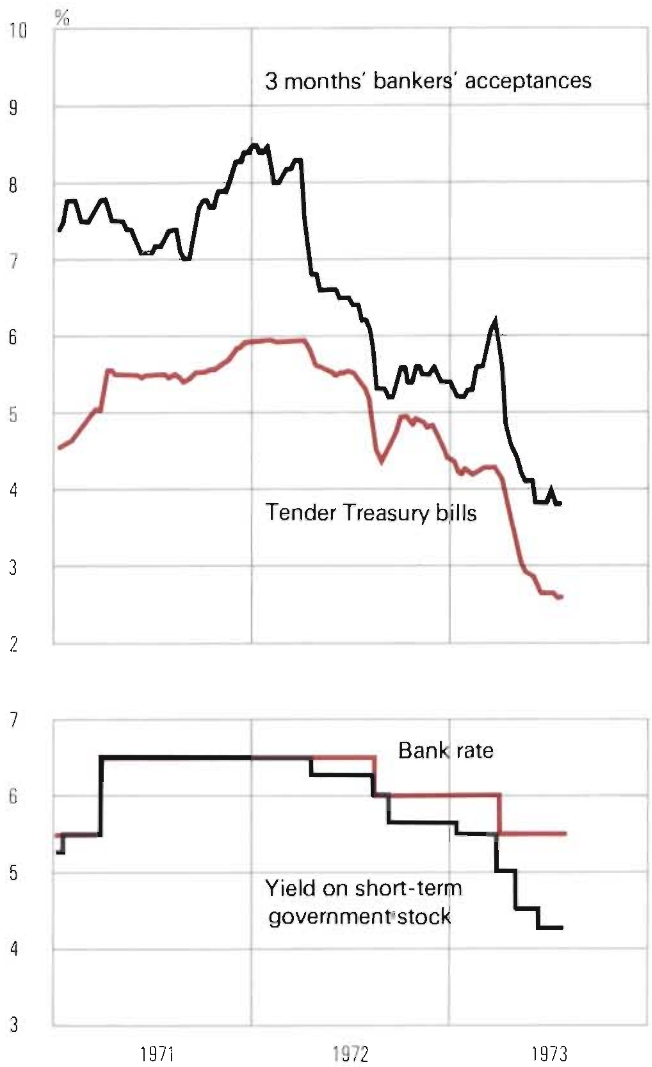
The amended Banks Act also imposed a 20 per cent limit on the extent to which liquid bankers' acceptances and trade and agricultural bills may be included to comply with the liquid asset requirements (other than the cash reserve requirement). At the end of June 1973 most banks held less liquid bills than 20 per cent of their required liquid assets. For the commercial banks and monetary hire-purchase and general banks the additional bankers' acceptances and other bills that may be included as liquid assets amounted to R53 million at the end of June 1973.

Easing of money market conditions

Money market conditions continued to ease further during the year under review, except for a short period between middle February and end March 1973 when a seasonal shift of funds to the government led to a temporary tightening of the market. Short-term interest rates continued the sharply downward trend which had become apparent from the end of the first quarter of 1972. In fact, the decline in short-term interest rates was more pronounced than for a long time and rates reached such low levels as were last recorded in the early nineteen sixties. This marked decline in interest rates was one of the outstanding features of the monetary and banking situation.

The Treasury bill tender rate, for example, declined from about 6 per cent at the end of 1971 to 4,38 per cent at the end of 1972 and to only 2,64 per cent at the end of June 1973. On 13 July 1973 the rate was 2,57 per cent, its lowest level since early March 1964. Other short-term interest rates showed even more marked declines; for example, the discount rate on 3-months' bankers' acceptances declined from $8\frac{1}{2}$ per cent at the end of 1971 to about $5\frac{1}{2}$ per cent at the end of 1972 and further to 3,8 per cent at the end of June 1973. Bank rate was also reduced from $6\frac{1}{2}$ to 6 per cent on 10 August 1972 and to $5\frac{1}{2}$ per cent on 28 March 1973. The rate quoted on government securities with an unexpired maturity of 3 to $3\frac{1}{2}$ years was reduced no fewer than six times during the year, from $6\frac{1}{4}$ per cent before 10 August 1972 to $4\frac{1}{4}$ per cent on 9 June 1973. Maximum deposit interest rates for banks and building societies, as prescribed in terms of the deposit interest rate control regulations of March 1972, were reduced voluntarily by $\frac{1}{2}$ per cent in August 1972. On 11 April 1973 this lower level of deposit interest rates was given legal effect. Towards the end of June some of the banking institutions reduced the interest rate paid on deposits of twelve months and longer by $\frac{1}{2}$ per cent to $6\frac{1}{2}$ per cent.

Money market and related interest rates



Government finance

Reduction of expenditure by public authorities

As in most countries, the demand by South Africa's public authorities for productive resources constitutes an important part of total demand. Thus, the combined consumption and investment expenditure of all public authorities in respect of the year under review represented 21,8 per cent of the gross domestic product. Largely as a result of the deliberate policy adopted in the 1972/73 central government budget to reduce substantially the rate of increase in government expenditure, particularly on consumption and non-infrastructural investment expenditure, this ratio was significantly smaller than the ratio of 23,6 per cent for 1971/72.

Small increase in current expenditure

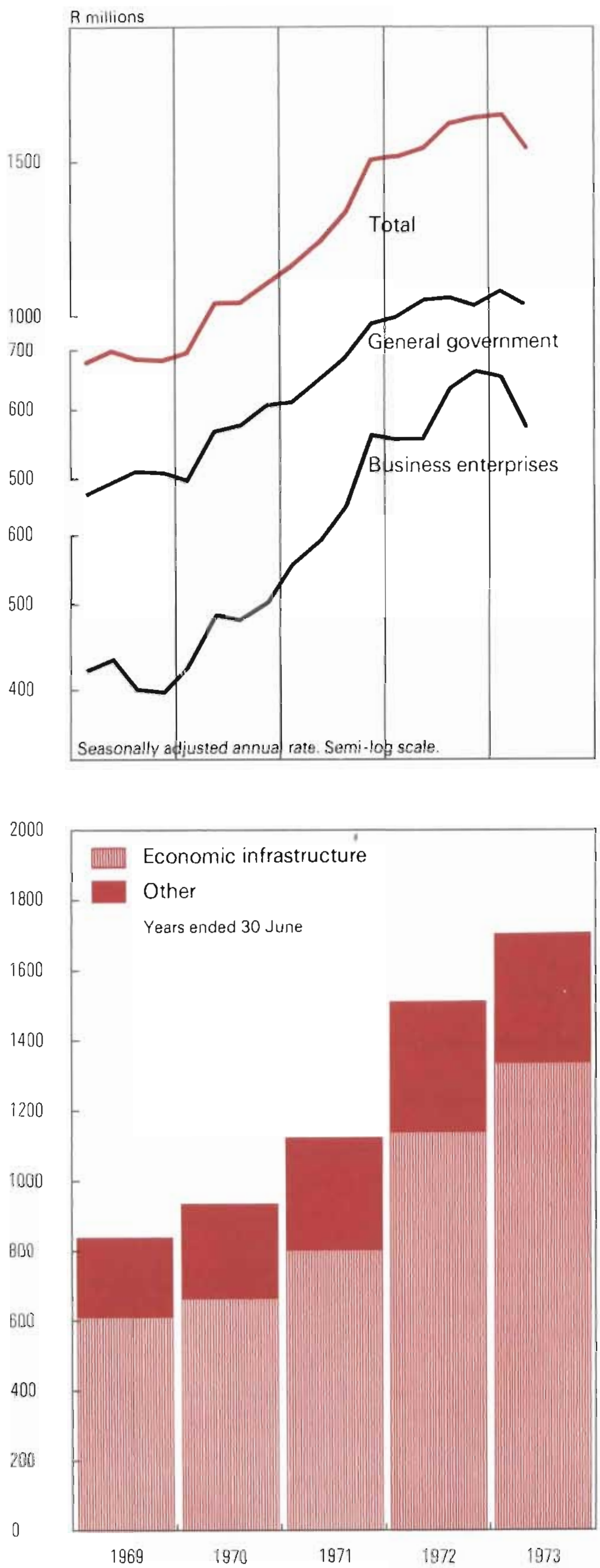
Consumption expenditure by public authorities rose by only about 5 per cent during the year under review, its lowest rise since 1966/67. This lower rate of increase occurred at all levels of government and in a variety of expenditure items, particularly salaries and wages of government employees which were kept virtually unchanged during 1972. The percentage increase observed during the period under review was, therefore, primarily the result of increases in consumption expenditure during the first half of 1973, following the upward adjustment of salaries and wages in the public sector in April 1973.

The other components of current expenditure of public authorities, namely subsidies and current transfers to households, also increased at a lower rate during 1972/73 than during the preceding year. Subsidies showed only minor changes, whereas current transfers to households, chiefly pensions, rose by 13 per cent during 1972/73, compared with 17 per cent in 1971/72. With current expenditure items rising at a lower rate during 1972/73 than during the preceding year, and with the substantially faster increase in current revenue during 1972/73, the current surplus reached a record amount of R678 million.

Priority for economic infrastructural fixed investment

The total fixed investment of public authorities rose by only 13 per cent during the year under review, compared with the increase of 34 per cent during the preceding year. The different components of expenditure, however, showed divergent trends. Whereas fixed investment by the non-trading departments levelled off during the year under review, capital outlays by the business enterprises (mainly the South African Railways) rose steeply during the second half of 1972, but declined notably during the first half of 1973, as shown in the accompanying graph. A functional classification shows that priority was given during the past two years to economic infrastructural investment, particularly in respect of transport and communication, roads and government water schemes. In fact, these types of expenditure

Gross fixed investment: public authorities



rose by no less than 41 per cent during 1971/72 and by a further 17 per cent during 1972/73. Although less than in the previous year, the rate of growth still remained at a high level compared with preceding years. This compares with a decline of 2 per cent in investment expenditure on other projects, mainly as a result of reduced expenditure on government buildings, including schools and hospitals.

Smaller Exchequer deficit

During 1972/73 total capital and current expenditure of the central government, as reflected in total issues from the Exchequer Account, exceeded total receipts, excluding borrowing, by only R426 million, compared with a deficit of more than double this amount during the preceding year.

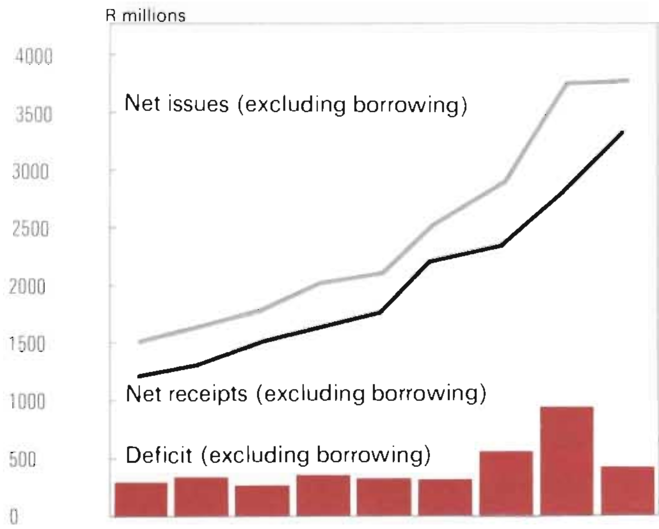
The accompanying table shows that the decline in the Exchequer's deficit was due to a substantial rise in receipts coupled with almost no change in issues. Higher income tax collections from various sources led to the increase in receipts. Data for the fiscal year that ended on 31 March 1973 reveal that taxes paid by persons rose by R175 million compared with the preceding fiscal year and their share of total income tax receipts therefore rose from 37 per cent in 1970/71 to 45 per cent during the past fiscal year. The relative importance of income tax paid by persons as a source of revenue accordingly exceeded that of income tax paid by non-mining companies (43 per cent) for the first time since 1967/68, notwithstanding the increase of R94 million in income tax receipts from these companies during the year. Higher premiums earned on private market gold sales led to higher profits and resulted in an increase of R64 million to R162 million in the income tax receipts from gold mining companies during 1972/73. These income tax receipts accounted for 9 per cent of total income tax collections during the year.

Exchequer account
R millions

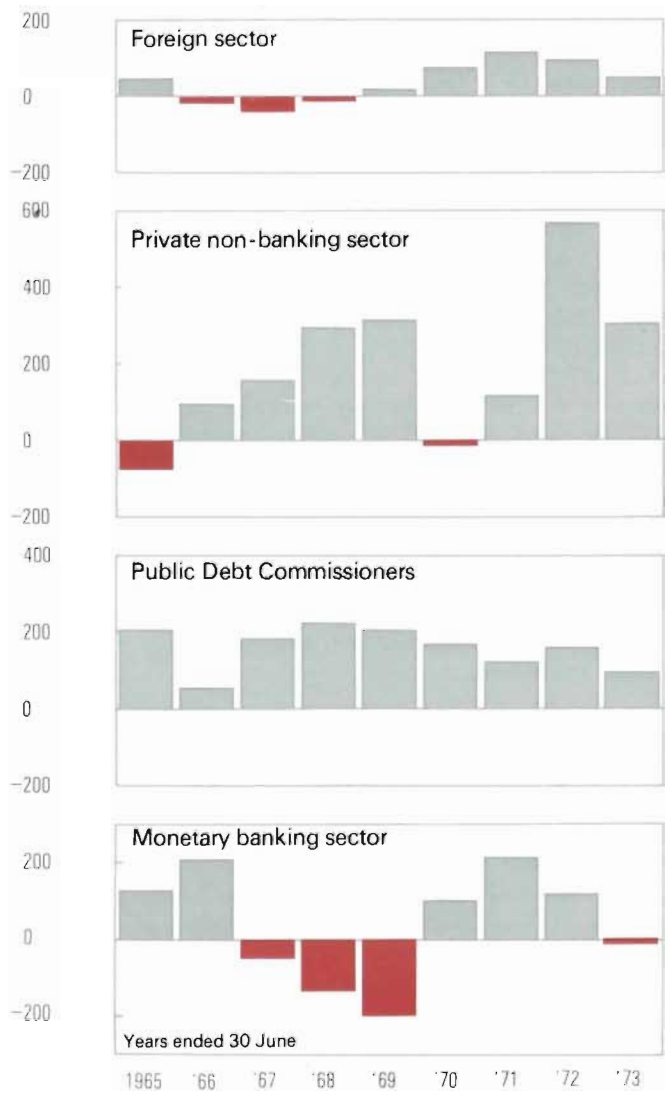
	Year ended 30 June		
	1971	1972	1973
Total net issues	2 904	3 743	3 769
Total net receipts	2 341	2 810	3 342
Total deficit (excluding borrowing)	563	933	426

The increased supply of loanable funds resulting from the increase in the gold and other foreign reserves and higher domestic saving, enabled the Treasury to finance its deficit in the year 1972/73 entirely from non-banking sources, particularly from the private non-banking sector. The Exchequer's net indebtedness to the monetary banking sector was

Exchequer account



Exchequer financing
Change in net debtedness to



actually reduced by about R21 million because the record increase of R453 million in the banks' government security holdings was more than neutralised by the large increase of R475 million in the Exchequer's available cash balances. The latter included an addition of R264 million to the Stabilization Account. The increase in Exchequer deposits was particularly notable during June 1973 when a favourable response to recent stock issues coincided with a seasonal inflow of income taxes. The upward movement in *total* Exchequer deposits has continued since then and these deposits actually exceeded the R1 milliard level early in July. Exchequer cash balances normally show a seasonal downward movement in the latter half of the calendar year and a similar development during 1973 could lead to a substantial increase in the liquidity of the banking and the private non-banking sector.

Holdings of government securities by the private non-banking sector rose by R305 million during the year or by about half the amount recorded in 1971/72. The increase nevertheless represented no less than 71 per cent of the smaller Exchequer Account deficit and exceeded the average contribution during the preceding ten years by a large margin. Because of the abolition of loan levies on individuals in the 1972/73 Budget, the increase in the private sector's holdings of government securities during the period under review was mainly accounted for by marketable government stock held by insurers and pension funds. Net receipts of foreign loans by the Treasury amounted to R47 million during the year, and net investments by the Public Debt Commissioners to R96 million. Both contributions were smaller than in 1971/72.

The 1973/74 Budget

The 1973/74 Budget was aimed at a further moderate stimulation of economic growth without aggravating inflationary pressures. Various taxes were reduced, incentives for fixed investments were raised and, to offset the effects of inflation on the lower income groups, social and civil pensions were increased. The Minister endeavoured to stimulate exports, particularly manufactured products, by accepting and implementing various proposals of the Commission of Inquiry into the Export Trade.

Expenditure from the Revenue and the Loan Account together was estimated at R4 447 million, or 19 per cent more than in 1972/73. The increase was mainly due to anticipated higher expenditure from Revenue Account, mostly of a current nature, and included salary adjustments totalling R180 million. Expenditure from that Account was estimated to increase by 22 per cent, whereas that from Loan Account, mainly of a capital nature, was expected to rise by 11 per cent. Capital expenditure was mainly directed at the improvement of the economic infrastructure.

After taking into account the various tax proposals, total revenue was estimated at R3 350 million, leaving a deficit of R1 097 million. The Minister proposed to finance a large part of the deficit from available cash balances, including R351 million from the Stabilization Account, thereby increasing the flow of funds to the private sector.

Capital market

Increased supply of loanable funds in the capital market

The demand-supply relationship in respect of loanable funds in the capital market was quite different during the year that ended on 30 June 1973 from that during most of the post-war period. The supply of funds was increased through a general rise in gross domestic saving, which actually exceeded gross domestic investment, a phenomenon that has occurred only occasionally during the post-war period. A higher level of liquidity in the economy brought about by the substantially improved balance of payments situation and an increase in bank credit to the private sector also contributed to the larger supply of funds in the financial markets. With fixed investment sluggish, the demand for loanable funds was relatively low, with the result that interest rates declined significantly.

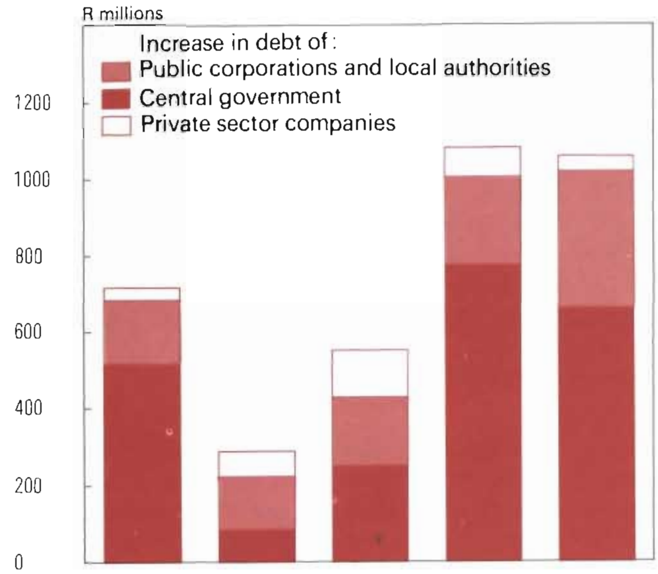
Easing of market for fixed-interest securities

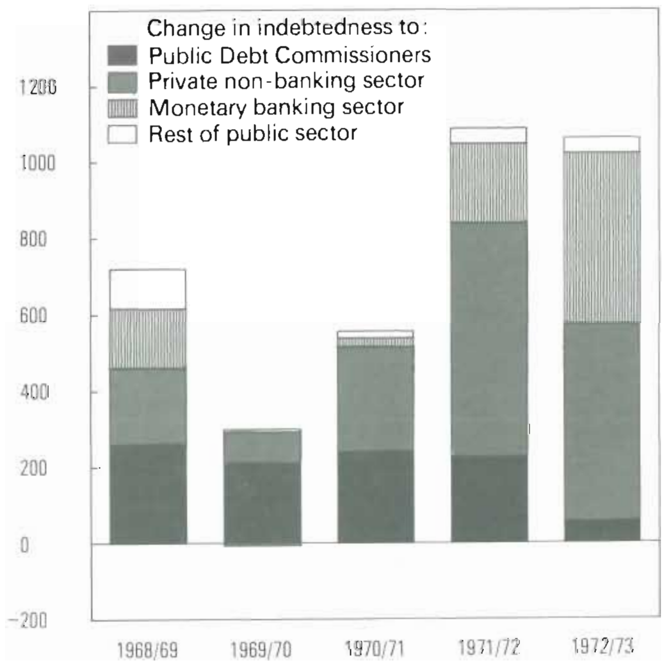
As from the second quarter of 1972 conditions in the market for fixed-interest securities have become easier, except for a temporary drain on the supply of funds in this market during the first quarter of 1973 caused by a heavy over-subscription of two share issues. A smaller demand for funds by the public as well as the private sector and a substantial increase in the supply of loanable funds both contributed to the easing of the market for fixed-interest securities. Owing to a cut-back of capital expenditure and the substantial foreign borrowing by the S.A. Railways and the Post Office during the 1972/73 fiscal year, the government's domestic borrowing requirements were substantially smaller during the year that ended on 30 June 1973 than during the preceding twelve months, and this reduction more than compensated for the increase in the demand for funds by public corporations. The latter was to a significant extent met by foreign borrowing. The amount of funds raised by the private sector in the domestic market for fixed-interest securities decreased during 1972/73 because of a lower level of private fixed investment generally and the more favourable conditions for raising capital in the share market.

The supply of funds in the domestic market came mainly from the monetary banking sector and the private non-banking sector. The contribution of the Public Debt Commissioners, who are usually a principal supplier of funds in this market, fell from R227 million during 1971/72 to only R59 million during 1972/73, mainly because the Commissioners invested a larger portion of their funds in the form of Treasury bills. The monetary banking sector's contribution increased significantly owing to the requirement in the amended Banks Act, effective from 1 November 1972, that banking institutions have to maintain prescribed investments equal to at least 10 per cent of their long-term liabilities to the public and that at least 50 per cent of these investments must consist of government securities.

The private non-banking sector (mainly insurers and private pension and provident funds) contributed most to the supply of funds in the fixed-interest securities market. During 1972/73 this sector's con-

Marketable domestic fixed-interest securities

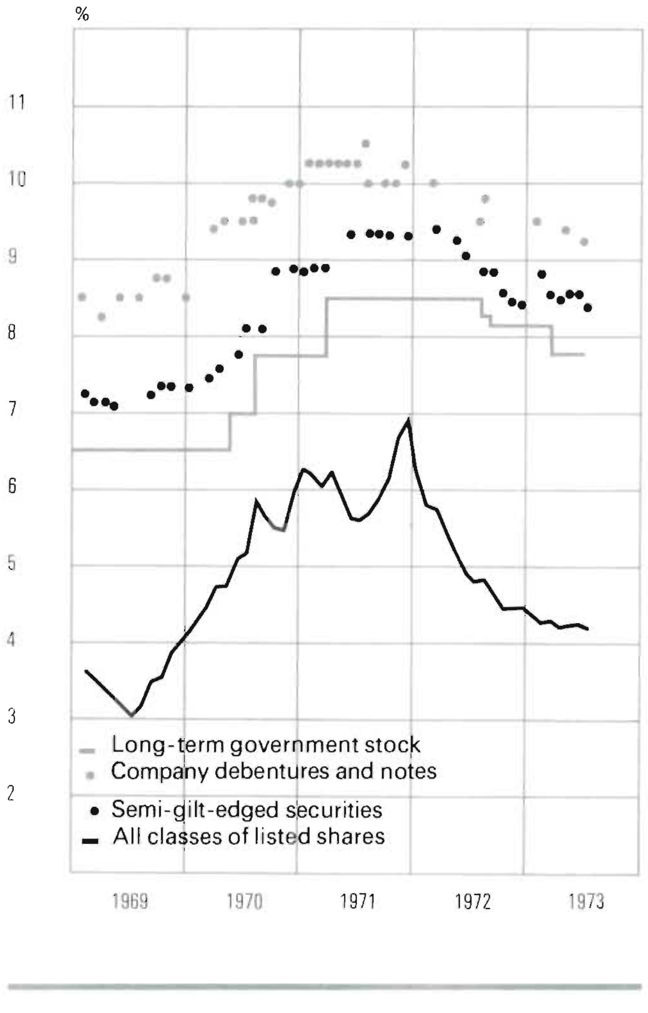




tribution declined to R512 million, compared with R633 million during 1971/72, i.e. more than the proportionate fall in the total demand which declined from R1 097 million in 1971/72 to R1 061 million in 1972/73. As during 1971/72, the emphasis in the investment policy of insurers and pension and provident funds was still on investing in gilt- and semi-gilt-edged securities because of the obligation to increase their holdings of such securities in terms of the new requirements introduced on 1 October 1971. The limited capital requirements of the private sector, related to the sluggishness of private fixed investment, also influenced the investment policy of the relevant institutions. During the year that ended on 30 June 1972, their net investment in gilt- and semi-gilt-edged securities amounted to 54 per cent of the increase in their assets, and for the nine-months' period up to the end of March 1973 (later figures are not available), the corresponding ratio amounted to 42 per cent.

The easing of conditions in the fixed-interest securities market during the year that ended on 30 June 1973 led to a continued decline in yields. The yield on long-term government stock was reduced from 8,50 to 8,25 per cent in August 1972 and further to 8,125 per cent in September 1972 and 7,75 per cent in March 1973. The predominant yield on new issues of long-term semi-gilt-edged securities, which began to move downwards during the second quarter of 1972, declined from about 9,35 per cent at the end of the first quarter of 1972 to about 8,30 per cent at the end of June 1973. During the same period the predominant yield on new issues of company debentures and notes decreased from about 10,25 to 9,25 per cent. Because of these adjustments, the margin between the yields on semi-gilt- and gilt-edged stock and that between the yields on company debentures and gilt-edged stock, both of which customarily widen during periods of rising interest rates and narrow during periods of decreasing interest rates, declined from 0,85 and 1,75 per cent, respectively, at the end of March 1972 to 0,55 and 1,50 per cent, respectively, at the end of June 1973.

Interest rates and yields



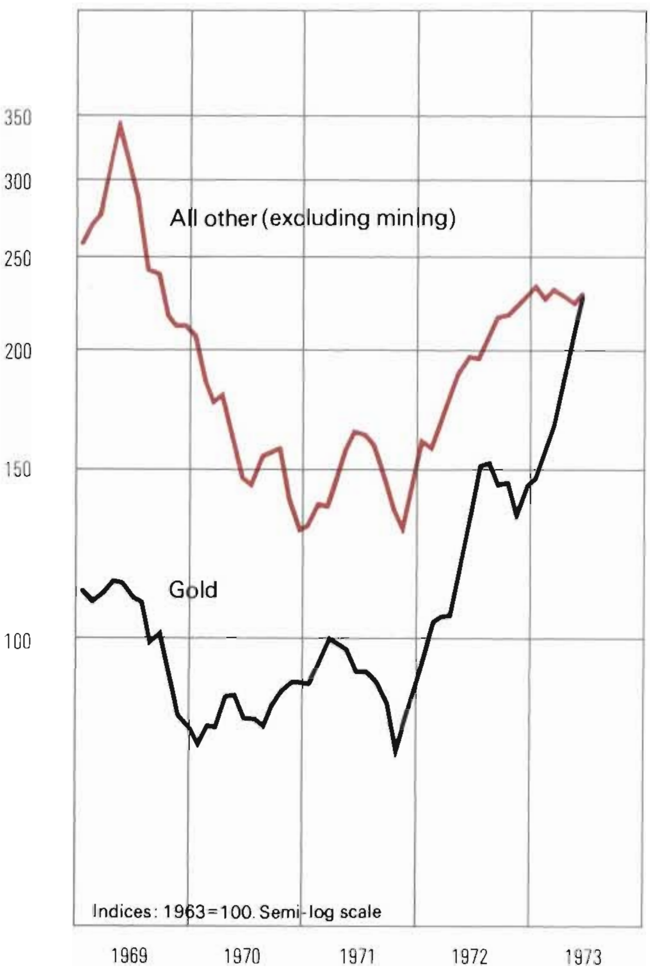
Share market

The rising trend in share prices as from the end of 1971 was maintained until January 1973, but thereafter only the prices of gold mining shares and to a lesser extent also industrial and commercial shares continued their upward movement. Prices of other mining shares and financial shares drifted downwards after January. Notwithstanding these divergent tendencies, the overall index of share prices, representing in terms of market values about 96 per cent of all shares listed on the stock exchange, continued its upward trend and showed an increase of 22 per cent during the year that ended on 30 June 1973. Corresponding price increases for the period as a whole within the major categories of shares were 43 per cent for mining shares, 9 per cent for financial shares and 25 per cent for industrial and commercial shares. Gold mining share prices increased sharply in accordance with the rise in the price of gold on the private market and increased by 69 per cent during the period under review. The downward drift in prices of mining shares, other than gold, and financial shares as well as the moderate increase in the prices of industrial and commercial shares after January 1973 were probably due to a shift of investment interest to the gold mining section. In total non-residents also contributed less to the market because their net purchases during 1972/73 amounted to only R1 million, compared with R161 million in 1971/72.

The generally weaker trend in share prices after January 1973 was not reflected in the stock exchange turnover as measured by the number of shares traded, and the average monthly turnover during the five-month period February to June 1973 was roughly equal to the monthly average for the first seven months of the period under review. The level of transactions during 1972/73 was on average 30 per cent higher than during 1971/72. Turnover figures, therefore, confirm that the weaker trend in some classes of share prices was not due to a lack of interest, but rather due to a shift of interest to one section of the market.

The increase in share prices during the review period

Share prices



led to a decline in share yields. The yield on all classes of shares decreased from 4,73 per cent in June 1972 to 4,13 per cent in June 1973. If mining shares are excluded, the average yield declined during the first seven months of 1972/73, but increased after January 1973. Notwithstanding the decline in share yields, the inverse yield gap between gilt-edged stock and ordinary shares narrowed from 3,77 to 3,62 per cent between June 1972 and June 1973.

Because of the increased activity and higher prices on the stock exchange, conditions became more favourable for raising new capital in the share market. Two new issues, totalling R23 million, in February and March 1973, for example, attracted subscriptions of R465 million. The influence of this temporary immobilisation of funds was felt not only in the share market, but also in other sections of the capital market. New issues of shares on the stock exchange were considerably higher during 1972/73 than during 1971/72, the relevant figures amounting to R176 million and R108 million respectively. A break-down of the amount of new capital raised on the stock exchange indicates that banking and insurance companies raised 36 per cent of the total, financial mining companies 20 per cent, financial industrial companies 12 per cent, industrial and commercial companies 23 per cent, and property and mining companies 9 per cent.

Notwithstanding the generally favourable conditions on the stock exchange during 1972/73, unit trusts continued to experience an outflow of funds in the form of net repurchases of units. These repurchases amounted to R17 million, compared with net sales of units amounting to R4 million in 1971/72. Because of the outflow of funds, the trusts made no net additions to their securities portfolios during the period under review. In order to meet the outflow of funds the trusts' cash and deposit holdings were reduced. The market value of the trusts' net assets increased by R62 million to a level of R500 million at the end of June 1973 on account of an increase in share as well as fixed-interest security prices. The selling prices of units, which are based on the market value of net assets, accordingly increased by 14 per cent between June 1972 and June 1973. This is less than the 22 per cent rise in share prices of all classes of shares listed on the stock exchange owing mainly to the fact the stronger rising mining shares do not feature predominantly in the trusts' portfolios. The yield on these units declined from 4,2 per cent in June 1972 to 3,6 per cent in June 1973.

Mortgage market

A significant change occurred in the demand-supply relationship of funds in the mortgage market. Owing to the slowing-down of private fixed investment and the over-supply of shop and office accommodation in relation to the demand in certain areas, the demand for industrial and commercial mortgages tended to level off. However, there was a substantial flow of funds to the residential mortgage market where a strong demand existed. The larger supply of and lower demand for funds in the mortgage market was reflected in a general decline in mortgage rates, the average rate on all classes of mortgage loans decreased from 9,08 per cent in June 1972 to 8,89 per cent in March 1973.

The ability of the mortgage market to meet the demand for funds was reflected in the net amount of new mortgage bonds registered, i.e. after deducting the amount of bonds cancelled. During the nine months from June 1972 to March 1973 (the latest period for which information is available), the monthly average of net mortgage bond registrations was 22 per cent higher than the monthly average for 1971/72 namely R91 million compared with R75 million.

The supply of funds to the mortgage market came mainly from the building societies, banking institutions and participation mortgage bond schemes. In terms of the net registration of mortgage bonds according to mortgagee, these institutions were responsible for about 86 per cent of the total for 1972. When the classification of the outstanding mortgage debt according to the most important financial institutions is reviewed over the five-year period 1968 to 1973, the proportionate share of building societies, banking

Mortgage loans outstanding

	31 March 1968		31 March 1973	
	Amount R m	%	Amount R m	%
Building societies	1 697	54	3 192	56
Participation mortgage bond schemes	334*	10	828	15
Banking institutions	339	11	561	10
Land Bank	228	7	421	7
Insurers	418	13	420	7
Private pension and provident funds	159	5	289	5
Total	3 175	100	5 711	100

*June 1968

institutions, the Land Bank and private pension and provident funds remained fairly constant, but that of participation mortgage bond schemes increased to compensate for a decline in the relative share of insurers. Insurers have shown more interest in direct property development as a substitute for providing mortgage loans and this gap in the supply of funds in the mortgage market was filled mainly by the participation mortgage bond schemes. These schemes specialise in industrial and commercial mortages, but also provide mortgage loans for residential purposes, mainly in the form of mortgages on flats.

Flow of long-term funds to financial institutions

The accompanying table shows the order of magnitude of the flow of long-term funds to the main groups of financial institutions. As may be expected, the flow of funds in the form of contractual savings to insurers and pension funds showed a steady annual rise. Banking institutions also experienced an increase in the inflow of longer-term funds, but the flow of funds to building societies and participation mortgage bond schemes tended to fluctuate. During 1972/73 building societies received a very large amount of funds, not only in relation to the other groups of financial institutions, but also compared with the inflows recorded during previous years. Participation mortgage bond schemes were the only institutional group which had a reduced inflow of funds during 1972/73 and the relevant amount was only about 70 per cent of the figure recorded in the previous year.

Flow of long-term funds to selected financial institutions

	Year ended 30 June					
	1971		1972		1973	
	R m	%	R m	%	R m	%
Building societies	410	31	350	24	744	37
Banking institutions.....	183	14	255	17	317*	16
Participation mortgage bond schemes	147	11	158	11	110*	5
Long-term insurers	220	16	260	18	290*	15
All pension and provident funds	374	28	442	30	531*	27
Total	1 334	100	1 465	100	1 992*	100

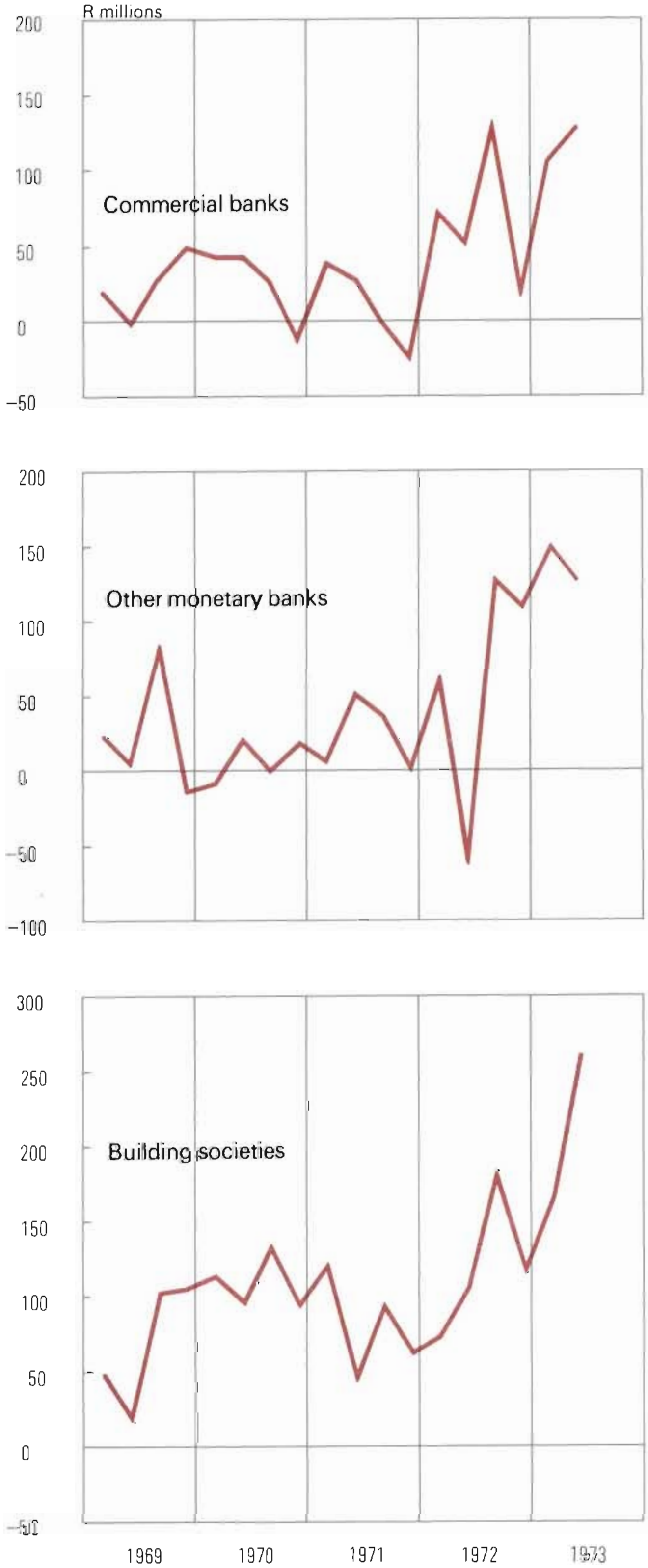
*Preliminary figures

Apart from the decline in the demand for industrial and commercial mortgages, a reason for the decline in the inflow of funds to the participation mortgage bond schemes and the larger inflow to building societies and banks was the deposit interest rate control introduced in March 1972. Interest rates on deposits and building society shares were fixed approximately at their then existing market levels, but in the case of participation mortgage bond schemes the maximum permissible interest payable to participants in mortgage schemes was reduced by 1 per cent from $9\frac{1}{2}$ per cent to $8\frac{1}{2}$ per cent.

The inflow of funds to building societies of R744 million during 1972/73 represented a 21 per cent increase in their total liabilities and is approximately double the increase during the previous year. This inflow of funds together with the return flow of funds from capital repayments on existing mortgages enabled the societies to grant new mortgage advances of R1 064 million during the period under review, or R429 million more than during 1971/72. The societies also added R266 million to their holdings of liquid assets and the suspended prescribed investments.

Because of the large inflow of funds experienced by the societies, they were able to reduce considerably the backlog in the demand for housing loans. They were also able to reduce the interest payable on mortgage loans. On 1 February 1973 the societies lowered the mortgage rate on dwellings from 9,0 to 8,75 per cent. In June 1973 the societies decided that they will reduce this rate further to $8\frac{1}{2}$ per cent and also the mortgage rate on flats and other buildings to $8\frac{3}{4}$ per cent during the period from 1 August to 1 October 1973. Maximum interest rates for deposits and shares were fixed in terms of the deposit interest rate control in March 1972. In August 1972 a new set of deposit and share rates were agreed upon by the societies and the monetary authorities, and legal effect was given to these rates in April 1973 under the existing deposit interest rate control. A further reduction in the maximum rate payable on paid-up indefinite period shares (excluding tax-free shares) was also effected in April and at the same time a new maximum rate was introduced for deposits of two years and longer. In June 1973 most of the building societies reduced some of their deposit rates below the permissible maxima; the rate on special savings deposits was lowered from a maximum of $5\frac{1}{2}$ to 5 per cent, that on deposits from 12 to 24 months from 7 to $6\frac{1}{2}$ per cent and that on deposits of 24 months and longer from $7\frac{1}{2}$ to $6\frac{1}{2}$ per cent. All other rates were kept unchanged, namely $6\frac{1}{2}$ per cent for deposits in terms of the government-sponsored home owners' sheme, subscription shares and tax-free indefinite period shares, 7 per cent for

Net investment in savings and time deposits and building society shares



other indefinite period shares and $7\frac{1}{2}$ per cent for fixed period shares with guaranteed dividends.

During the 1973 Parliamentary Session the Building Society Act was amended and the relevant changes included the following:

1. The maximum loan which a society may advance to any buyer of a house for repayment over 30 years is increased from R15 000 to R20 000.
2. The Minister of Finance is empowered to prescribe that the interest rates on existing and future housing loans which exceed R15 000, or any other amount fixed by the Minister, must be increased by a minimum amount above the basic lending rate of the building societies.
3. The Minister is also empowered to prescribe the percentage of total housing loans which may be advanced by societies for flats, buildings for commercial purposes and houses for which the loan would exceed an amount specified by him.
4. The proportion of the value of a house which a building society may advance as a loan, is reduced from $82\frac{1}{2}$ per cent to 80 per cent.
5. Building societies will be allowed to accept savings deposits from companies provided that the deposits are accepted subject to the conditions that only one withdrawal may be made per month, and each deposit or withdrawal shall amount to no less than R100, or that the monies so invested with societies represent lessees' deposits referred to in the Rents Act of 1950.
6. The definition of dwelling houses has been amended to include a "unit" as defined in the Sectional Titles Act of 1971, and used for residential purposes.