Mr Mboweni speaks on the role of the South African Reserve Bank in developing the economy

Speech given by Mr Tito Mboweni, Governor of the South African Reserve Bank at the Western Cape Exporter of the year awards dinner on 1 September 1999.

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Many central bank governors fight a constant battle against public misconceptions about the central bank's role in the economy. After only a short period in the job, I have realised that I, too, will have my work cut out for me in explaining the South African Reserve Bank's responsibilities.

As I discovered last week when I took part in a phone-in programme on SABC radio, there are people who mistakenly believe the Bank can provide them with personal loans, or loans for their businesses. I had to explain that I am not a personal banker with a limitless cheque book.

I was also worried to find that some of the callers did not have a good understanding of the relationship between interest rates and inflation. Once again, I realised the need for education and for continued emphasis on the Bank's main task – the achievement and maintenance of financial stability.

There might be people who are getting bored with my message. But I think it is well worth repeating, as even people with a good understanding of the economy sometimes expect us to be miracle-workers who will bring new life to the economy.

When I was invited to speak here tonight, my hosts asked me to talk about the role of the central bank in developing the economy, with a particular focus on exports. As was highlighted in the Governor's Address last week, the central bank's main contribution to economic development and export growth is to achieve price stability.

That must come as a disappointment to those exporters here tonight who hoped I would say something about the rand's exchange rate against the currencies of SA's major trading partners.

The best that I can do on the topic of the exchange rate is to recount a story about the euro, which has recovered somewhat from its weakness against the dollar. Please bear in mind that I tell the story with my tongue firmly in my cheek.

Research published last week by 4Cast, a London-based economic consultancy, suggests that an inverse relationship has developed between the performance of the euro and the frequency of statements by European Central Bank officials about the currency. The periods during which central bank officials kept quiet about the euro coincided with relative stability or appreciation of the euro against the dollar. The researchers were worried that when the ECB officials return from their summer holidays and start talking again, the currency could resume its slide to parity with the dollar.

I know there are people who might try to read some deeper meaning into that story. I tell this story simply to illustrate that I believe "less is more" when it comes to comments on the rand.

The only comment I will make is to reaffirm that we will not set targets, formal or informal, for the exchange rate. As you know, we have started making preparations for implementing inflation targeting as our monetary policy framework. We believe the inflation targeting route is incompatible with trying to force the currency into a straightjacket. And, in any case, fixed exchange rates are globally becoming a thing of the past as more and more countries move towards flexible exchange rate systems.

In the Governor's Address last week, we outlined our approach to inflation targeting and we reported on the organisational changes being made to the monetary policy decision-making process.

We also noted that the South African economy had recovered remarkably well from the effects of financial turbulence in Asia and Russia. Many tentative signs of a return to financial stability had appeared in the economy.

This was again confirmed by July's money supply and bank credit figures which became available yesterday. These figures show that for the first time since 1993, total bank credit extension increased at a rate of below 10%. This is good news indeed.

The markets have by now digested last week's Address. We have noted that analysts and commentators welcomed the decision to formalise monetary policy decisions by establishing a Monetary Policy Committee, or MPC, which will comprise the governor, the deputy governors and senior bank officials.

However, market participants are apparently disappointed by our decision not to publish the minutes of the MPC meetings.

There are costs and benefits for the Reserve Bank to publish the minutes of internal meetings. In the interests of greater policy transparency, we will issue brief statements to the public at regular intervals to provide information on overall economic conditions and the monetary policy stance. These statements will usually follow MPC meetings, which will take place every six weeks.

Frequent and predictable communication with the financial markets is not the only way in which we hope to achieve better public understanding of monetary policy. Regular reporting to Parliament's finance portfolio committee meetings, which are open to the media and the public, is another important component of getting our message across. That is why I was pleased to accept the portfolio committee's invitation to brief its members in Parliament and take questions on the Governor's Address later this month.

The release last week of the Governor's Address and the Annual Economic Report was a good opportunity to take stock of the economy after a particularly difficult time.

As exporters, you will know that global demand for South Africa's exports suffered a severe setback in the second half of last year as a result of the turmoil in international financial markets.

As a result of the crisis in Asia, the share of South African exports destined for Asian countries, including Japan, declined from more than 21% of total exports in the third quarter of 1997 to about 15% in the fourth quarter of last year. African economies were also experiencing hard times, and the contribution of exports to Africa fell slightly to below 14% of total exports over the same period.

South African exporters did, to some extent, offset the effects of the recession in these economies by redirecting trade flows to markets less affected by the crisis. Exports to the United States, for example, increased by about 30% in rand terms between 1997 and 1998.

But the effects of the global crisis and continued buoyancy in imports were such that the annualised current account deficit swelled to 2.6% of gross domestic product in the second half of last year. Although the deficit was not large by international standards, it nevertheless raised concerns that the level of spending, especially on public sector capital formation, could not be sustained.

Last year's tightening in monetary policy, and the improvement in international economic conditions as the turmoil in financial markets subsided, caused a marked recovery in the current account this year. The improvement in the current account reflected a revival in international demand for South African exports and a significant contraction in local demand for imports.

Export volumes rebounded satisfactorily in the first quarter of this year, but lost some momentum in the second quarter, when the current account slipped into deficit again.

It seems that the current account may remain in deficit for the remainder of the year, although exports should still benefit from the lagged effects of the rand's depreciation, the resurgence of foreign demand and an increase in international commodity prices.

As the lagged effects of interest rate cuts continue feeding through to economic activity and the recovery gains momentum, the demand for imports can be expected to strengthen. The turnaround in the inventory cycle, which appears to have begun in the second quarter of this year, will heighten local demand for imports.

The deficit on the current account should be financed comfortably by net capital inflows. Barring any unforeseen shocks on the international front, the South African economy has entered a period of more rapid growth coupled with a fairly comfortable balance of payments situation.

But the expected increase in the economic growth rate from last year's paltry half-a-percent will fall far short of the levels needed to make inroads into South Africa's high unemployment rate. Many of our people remain poverty-stricken, living below the breadline in makeshift shacks that do little to keep out the winter cold. To them, the concept of financial stability might be remote, but the only way in which their lot can be improved on a sustainable basis is if the Reserve Bank does not deviate from its course.

Globalisation of financial markets means that countries that are out of step with the rest of the world will be punished swiftly and severely. For our part, we must continue policies and programmes to contain inflation. We must also maintain sound and efficient financial institutions and markets.

In other words, the main thrust of monetary policy has to be the maintenance of financial stability – that is, stability of prices, financial institutions and financial markets. Ladies and gentlemen, every time you invite me to occasions such as these, expect to hear the same thing.

Thank you.