South African Reserve Bank

Remarks by Lesetja Kganyago,
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at the annual dinner in honour of
the Ambassadors and High Commissioners
to the Republic of South Africa

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Introduction

Dean of the Diplomatic Corps, Ambassadors, High Commissioners, Counsellors and Diplomats, ladies and gentlemen – a very good evening and a warm welcome to the South African Reserve Bank (SARB). I would like to extend my heartfelt gratitude to you for accepting our invitation to this annual event.

This year, we celebrate the 100th anniversary of the birth of Nelson Mandela. Earlier this month, for the first time in the nearly 100-year history of the SARB, we issued a commemorative banknote series as well as a third commemorative R5 circulation coin in honour of the life of former President Mandela. Tonight, I would like to briefly reflect on what we can learn from Tata Madiba's legacy, both as a statesman and as a champion of institutions.

After all, it was under Nelson Mandela's presidency that the defining characteristics of South Africa's foreign policy and trade policy, as well as our interaction with foreign investors, were established.
Madiba had a vision that South Africa should be 'ready to play a role in fostering peace and prosperity in the world that we share with the community of nations'.

In 1993, a year before he became president, Nelson Mandela highlighted that 'our foreign policy will rest on the belief that economic development depends on growing regional and international economic cooperation in an interdependent world'.[1] Since Madiba's presidency, the foundation of all of South Africa's interactions with the rest of the world has always been strong domestic institutions and a robust macroeconomic framework that provides policy certainty, supported by our participation in multilateral institutions and forums that are transparent and fair.

Looking at the state of the global and domestic economies today, it is worth reflecting on the importance of institutions in managing risks and dealing with crises.

Reflecting on the global economy

The global economy today looks very different from a year ago. Last year, the backdrop for South Africa and other emerging markets was generally constructive, as the recovery of the advanced economies continued on a steady path. The stronger demand supported higher commodity prices, while expectations of a moderate withdrawal of monetary stimulus in the advanced economies were supportive of strong capital flows to the emerging markets.

However, this favourable setting did not last long. A number of key risks have since emerged that threaten to unsettle the global economy. During the early part of 2018, growing expectations of a faster pace of monetary tightening began to emerge, as the stronger pace of United States (US) growth was sustained and fiscal policy became more expansionary. Growth in Europe and Japan has slowed, while the strengthening of the dollar has resulted in a reversal of capital flows from the emerging markets.

In addition, concerns about the rise in protectionism have materialised, thus contributing to an escalation in trade tensions. Concerns about a possible trade war have contributed to uncertainty about world trade, which could derail the global economic recovery that policymakers have been working hard at since the global financial crisis. We are already witnessing the adverse effects. In April, for example, we saw the largest decline in world trade since May 2015.

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[1] 'South Africa's future foreign policy', an article by Nelson Mandela in *Foreign Affairs*, Vol. 72, No. 5, November / December 1993, African National Congress

Trade wars are, in effect, a 'zero sum' game. Small open economies suffer the most, as they rely on trade with the advanced economies and large economies - who are the price setters. Addressing these risks at both country and global level requires strong institutional frameworks and a commitment to cooperation and coordination.

The rising interconnectedness has widened the set of shared problems that are more effectively addressed through a global agenda. In this respect, collaboration is essential. This includes, among other things:

- reaffirming the open and rules-based multilateral trade system;
- strengthening the global financial safety net;
- addressing the excess external imbalances;
- completing the financial regulatory reform agenda; and
- reaching the 2030 Sustainable Development Goals.

These issues are central to the agendas of the Group of Twenty (G20), the Financial Stability Board, the Bank for International Settlements, the International Monetary Fund, and the World Bank. South Africa is an active participant in all these institutions.

As you may be aware, the 10th BRICS[2] Summit, this time under South Africa's presidency, concluded a few days ago. Its theme was 'BRICS in Africa: collaboration for inclusive growth and shared prosperity in the Fourth Industrial Revolution'. Since the beginning of 2018, the SARB has actively driven a number of initiatives among the BRICS central banks. This has included initiatives directed at enhancing the research capacity of the Contingency Reserve Arrangement (CRA), further work on the establishment of the BRICS Bond Fund to support the development of local-currency bond markets in the other BRICS countries, and a stocktake exercise on financial technology as it relates to crypto-assets and the regulation thereof. Finally, and very significantly, the BRICS central banks have, for the first time, conducted a test run of the CRA with an actual transfer of funds. This exercise commenced on 3 July and was completed successfully today.

[2] Brazil, Russia, India, China, South Africa

Building strong institutions on the African continent is also very important to support development and improve the continent's resilience to shocks. The SARB – through its chairing of the Association of African Central Banks and as the Chair of the Committee of Central Bank Governors in the Southern African Development Community – has been involved in a number of activities in support of economic and financial integration on the continent. These initiatives have spanned, among other things, the areas of banking supervision, strengthening central-bank independence, regional payment systems, financial-market deepening, financial stability, and financial inclusion. Other issues that require urgent attention include the negative impact of the withdrawal of correspondent banking relationships on trade flows and remittances, as well as the limits to domestic revenue mobilisation due to illicit flows.

The South African economy

South Africa's growth outlook remains challenging. At the most recent meeting of the SARB's Monetary Policy Committee earlier this month, the growth forecast for 2018 was revised downwards to 1.2% from 1.7% in May. The growth forecast for 2019 is 1.9% and 2.0% for 2020, both of which are significantly lower than the levels required to generate employment and to reduce inequality and poverty rates. While we consider the current monetary policy stance to be broadly supportive of the economy, inflation risks are to the upside, and our fiscal framework is vulnerable.

Faced with similar conditions back in 1996 under Nelson Mandela's leadership, the South African government had to make some really difficult decisions. It was resolved to make the required policy choices and strengthen macroeconomic institutions. This garnered investor confidence and placed South Africa on a strong economic footing in the early 2000s.

Recent research conducted by the SARB[3] suggests that the collapse in the levels of confidence over the past few years had shaved off around 1 percentage point from

[3] Theo Janse van Rensburg and Erik Visser, 2017, 'Decoupling from global growth – is confidence becoming a scarce commodity?', *South African Reserve Bank Occasional Bulletin of Economic Notes*, October

growth in both 2015 and 2016. In the months since December 2017, we have seen a rebound in business and consumer confidence. However, a cyclical recovery based on a rebound in confidence will not be enough to grow the economy lower levels of poverty, reduce inequality, generate much-needed employment, and boost government revenues. Given the weak medium-term growth prospects, structural reforms and appropriate fiscal policies are critical to boosting potential growth and sustaining confidence levels, by raising productivity and promoting human and physical capital, and enhancing inclusiveness.

Underlying the subdued growth performance of the South African economy has been the weak trend in gross fixed capital formation, particularly by the private sector. We need to reverse the downward trend in the ratio of gross fixed capital formation to gross domestic product, which had declined to 18.7% in 2017, down from a peak of 23.5% in 2008. This is some way off the 25% target set in the National Development Plan.

The role of the South African Reserve Bank

Achieving higher potential output growth is not within the power of the central bank. The SARB can, however, contribute to an improved environment in a number of ways. For some time, ratings agencies and investors had identified South Africa's institutional strength as one of the stand-out features of its economy. Unfortunately, the past few years have seen a steady erosion of some of our key institutions. Fortunately, there is now a renewed focus on reversing this negative trend. In fact, this renewed focus is part of the reason forwarded by Moody's for retaining the country's investment grade rating.

The SARB, specifically its independence coupled with its mandate on price stability and financial stability, is seen as an important part of the institutional strength of the country. We have vigorously and successfully defended attempts to undermine our independence and integrity, and we will continue to do so.

Conclusion

To sum up, here is what I have learnt from Madiba's legacy:

- To occupy its rightful place in the global economy, South Africa must first get its own house in order.

- We must start by implementing those policies that we have identified for growth and the development of our people.

- To protect ourselves from external shocks, we must build buffers by allowing our institutions to work as they were intended to work.

- As a small open economy, securing future growth requires us to work with our neighbours and trading partners, directly and through multilateral institutions.

Let me conclude by quoting from a speech that Nelson Mandela delivered to the diplomatic corps in 1999:

> "I do need to say to each and every diplomatic representative this evening that whilst our achievements – like our hope for the future – would not be possible without the patience, sacrifice, commitment and determination of all our people. Our task has been made easier because we have been blessed and sustained by the goodwill and support of our subregion, our continent and the global community. For this we are very grateful to you all.[4]

Thank you, and enjoy the evening.

[4] http://www.mandela.gov.za/mandela_speeches/1999/990205_diplomat.htm