

1951

SOUTH AFRICAN RESERVE BANK

REPORT OF THE
'THIRTY-FIRST
ORDINARY GENERAL MEETING

25th July, 1951

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McGILL UNIVERSITY

SOUTH AFRICAN RESERVE BANK

Established under the Currency and Banking Act, 1920

BOARD OF DIRECTORS.

MICHEL HENDRIK DE KOCK GOVERNOR.
ERNST HEINRICH DANIEL ARNDT DEPUTY-GOVERNOR.

WILLIAM DUNCAN BAXTER
CHARLES EDWARD JAMES
WILLIAM HENRY ARTHUR LAWRENCE
REGINALD HEINRICH PARKER
ROBERT PYOTT
GIDEON JOUBERT ROSSOUW

} COMMERCIAL,
AGRICULTURAL AND
INDUSTRIAL
REPRESENTATIVES.

EDWIN WINTER CATTELL
GERRIT PETRUS JOHANNES LOTZ
EUGENE O'CONNELL MAGGS

} GOVERNMENT
REPRESENTATIVES.

HEAD OFFICE—PRETORIA.

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L. J. COCKHEAD.

SECRETARY AND CHIEF
ACCOUNTANT
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DEPUTY CHIEF CASHIERS
R. F. A. LOUW.
S. F. T. GREAVES.

ASSISTANT TO THE GOVERNORS
J. B. DE K. WILMOT.

PRO. DEPUTY CHIEF CASHIERS
B. C. J. RICHARDS.
J. E. SPOTSWOOD.

ASSISTANT SECRETARY
H. E. MOGGGRIDGE.
ASSISTANT CHIEF ACCOUNTANT
A. P. MCLOUGHLIN.

STATISTICIAN
T. W. DE JONGH.

INSPECTOR
E. W. WARREN.

SOUTH AFRICAN RESERVE BANK

Thirty-First Ordinary General Meeting of Stockholders

MINUTES OF PROCEEDINGS

The Thirty-first Ordinary General Meeting of Stockholders was held at the Head Office of the Bank, Pretoria, on Wednesday, 25th July, 1951, at 11.30 a.m., the Governor presiding.

The Governor declared the Meeting duly convened in terms of the Regulations framed under the South African Reserve Bank Act.

The Minutes of the previous Meeting were taken as read and confirmed.

The Reports of the Board and of the Auditors for the year ended 31st March, 1951, were presented and taken as read.

The Governor then addressed the Meeting and said:

In presenting to you the Balance Sheet and Accounts and the Reports of the Board and the Auditors, I have pleasure in explaining the changes which have taken place during the year ended the 31st March, 1951.

RESERVE FUND : £2,419,000.

In accordance with the provisions of Section 16(3) of the Reserve Bank Act, a further sum of £84,000 was allocated to the Reserve Fund out of the surplus profit for the past year.

NOTES IN CIRCULATION : £75,654,000.

Our note issue, which had remained relatively stable during the financial years 1945-50, after allowing for the usual monthly and seasonal fluctuations, experienced a sharp increase of about £9,300,000 during the past year. Since the commercial banks, however, increased their holdings of our notes by £2,600,000, the amount of notes actually in the hands of the public showed a net increase of about £6,700,000. This increase of 11% over a period of only one year is, no doubt, associated with the substantial further rise in the general price level as well as with an expansion of economic activity in the Union.

DEPOSITS : £116,311,000.

There was an increase of almost £20,000,000 in our total deposits, notwithstanding the increase of over £9,000,000 in our note liabilities and also a decrease of almost £8,000,000 in our advances, discounts and investments in the Union.

Bankers' deposits showed a net decrease of £6,580,000. While there was an increase of £4,151,000 in the minimum reserve balances which the commercial banks were by law required to maintain with the Reserve Bank, due to an increase in their deposit liabilities in the Union, their current account balances with the Bank reflected a decline of £10,731,000.

On Government and Provincial accounts, however, there was a further increase of £29,312,000, namely, from £24,241,000 to a record total of £53,553,000.

In the case of the remaining deposit accounts, a net decrease of £2,764,000 took place during the year.

FOREIGN CURRENCY LIABILITIES INCURRED AS AGENT FOR UNION GOVERNMENT.

United States Dollars	£3,571,000
Swiss Francs	£2,993,000

While the respective amounts were the same as those shown in the previous balance sheet, a change occurred in the nature of our liability in United States dollars.

Last year I explained that a loan of 36,500,000 Swiss francs and a revolving credit of \$20,000,000 had been granted to the Union Government by groups of Swiss and American banks, respectively; that the Bank had agreed to act as the Government's agent and in exchange for the foreign currencies concerned had paid the Government the equivalent in Union currency of the proceeds of the Swiss loan and of the total line of credit granted by the American banks; that, for taking over the actual or potential liability to the Swiss and American banks, the Bank had received special stock certificates from the Government for the total amounts involved and with maturities and interest rates corresponding to those laid down in the respective agreements with the banks concerned; and that our actual liability to the American banks at the 31st March, 1950, had amounted to £3,571,000, as only half of the credit had been drawn at that date.

In January, 1951, virtually the same group of American banks, acting in co-operation with the International Bank for Reconstruction and Development, made a loan of \$10,000,000 to the Union Government against 4 and 5-year promissory notes bearing interest at the rates of $3\frac{1}{4}$ and $3\frac{1}{2}$ % per annum respectively, and also granted a new revolving credit of \$20,000,000 for 3 years, in the place of the previous one, at a lower rate of interest (namely $2\frac{3}{4}$ instead of 3% per annum on the amount actually drawn, plus the same annual commitment fee of $\frac{1}{2}$ % on the total amount of the credit). In respect of both the loan and the new revolving credit, the Government entered into a similar arrangement with the Bank as that mentioned above, and as it suited the Bank at the time to do so, it used the proceeds of the loan to repay the \$10,000,000 which it had drawn under the previous credit.

Accordingly, the Bank's liability of £3,571,000 in United States dollars at the 31st March, 1951, referred to the loan of \$10,000,000 and not to the revolving credit granted by the American banks, as in the previous balance sheet. (Since the end of the year, however, the Bank has had occasion to draw \$10,000,000 under the new credit.)

GOLD COIN AND BULLION : £72,704,000.

Our gold reserve, valued at the statutory price of 248s. per fine ounce, showed an increase of almost £14,000,000

during the year, i.e. an increase of over 1,100,000 fine ounces. Furthermore, as a result of a proportionately larger increase in the gold reserve than in our net liabilities to the public (i.e. after deduction of our foreign assets), the reserve ratio rose from 69.1 to 77.4%.

BALANCES WITH OVERSEAS BANKS: £2,084,000.
BALANCE EMPLOYED IN LONDON MARKET:
£1,950,000.

FOREIGN BILLS : £95,077,000.

Our total holdings of foreign exchange reflected an increase of £17,932,000 which, together with the increase of £14,000,000 in our gold reserve, reflects approximately the extent of the Union's favourable balance of payments over the year ended the 31st March, 1951.

The total of our foreign assets at the end of the year amounted to £99,111,000, consisting of £94,349,000 sterling, £4,588,000 U.S. dollars, £105,000 Canadian dollars and £69,000 Swiss francs.

DOMESTIC BILLS : £1,282,000.

This item refers to discounts of domestic bills for one of the commercial banks which required temporary accommodation in connection with the financing of wool exports. The amount of £1,282,000 outstanding at the end of the year comprised £1,032,000 in trade bills and £250,000 in Treasury bills.

LOANS AND ADVANCES : £5,810,000.

There was a decrease of £3,962,000 in this item, which consisted entirely of advances to Government or quasi-Government bodies for the importation and storage of bags and essential foodstuffs.

GOVERNMENT SECURITIES : £18,750,000.

Our portfolio of Union Government securities showed a net decline of £5,253,000 during the year.

On the one hand, there was an increase of £3,571,000 in our holding of special stock certificates as a result of the additional amount issued to the Bank in connection with the \$10,000,000 loan to which reference has already been made. On the other hand, there was a decrease of

£8,824,000 in the net book value of our holding of ordinary Government stock. This decrease represented the net result of our open-market operations, i.e. the excess of sales over purchases of Government stock by the Bank during the past year, as compared with net purchases of more than £6,000,000 during the previous year.

PROFIT AND LOSS ACCOUNT.

Our gross revenue, after making provision for taxation, rebate on bills not yet due, and sundry liabilities, was £33,000 higher than last year. Our general expenditure, however, also showed a substantial increase, namely, £53,000, of which £40,000 represented increased provision for bank note expenses due to the substantial increase in the note circulation and the higher costs of paper and printing. Furthermore, there was an increase of £33,000 in provisions charged against profits, such as the expenditure on fixed property, furniture and fittings during the year and the requisite annual contribution to the pension fund.

The net profit, therefore, decreased from £997,000 to £943,000, out of which a dividend of 10% was paid to stockholders and £84,000 was allocated to the Reserve Fund, leaving £759,000 to be paid to the Government compared with £807,000 for the previous year.

GOLD TRANSACTIONS.

Apart from £54,000 acquired from other sources during the past financial year, the Bank purchased gold to the amount of £94,918,000 from producers in the Union at the fixed price of 248s. 3d. per fine ounce.

The remainder of the gold output was sold by the producers themselves at a premium for industrial, artistic and professional purposes and subject to conditions laid down by the Union Government after consultation with the International Monetary Fund. These sales realised approximately £51,500,000, the net premium amounting to about £3,600,000, or an average of $7\frac{1}{2}\%$ over the monetary price of gold. In accordance with the Government's requirements, the bulk of the proceeds from these premium sales was received in U.S. dollars.

The Bank's own sales of gold amounted to £81,134,000, namely, £74,018,000 to the Bank of England, £3,260,000

to the United States Assay Office in New York, and £3,856,000 for miscellaneous purposes.

The sales to the Bank of England included gold settlements to the amount of £5,480,000 in respect of net payments made through London on South African account to hard-currency countries, the balance of £68,538,000 representing gold sold under the financial agreement between the Union and the United Kingdom to which I referred last year. The latter amount accounted for over 47% of the local gold output during the period under review and was substantially in excess of the minimum quantity stipulated in that agreement.

The relatively negligible amount of our direct sales of gold in New York was due, on the one hand, to the considerable decline in the Union's net expenditure in the dollar area, and, on the other, to the increased dollar proceeds of gold sold for industrial purposes as well as appreciable capital receipts in dollars.

As regards the remainder of our gold sales, an amount of £2,398,000 was sold to the Bank for International Settlements against U.S. dollars; £1,136,000 to the Government of Mozambique in respect of deferred pay due to natives from that territory employed on the mines in the Union; and £219,000 to jewellers, dentists, etc. in the Union, through the South African Mint.

BALANCE OF PAYMENTS.

The Union (including South-West Africa) enjoyed a favourable balance of payments throughout the calendar year 1950, the net surplus amounting to £48,000,000 in the first half and £23,000,000 in the second, i.e. £71,000,000 for the year.

Excluding exports of gold and gold products, the estimated deficit on current account amounted to £154,000,000 in 1950 as compared with £228,000,000 in 1949. The reduction of £74,000,000 in this deficit was brought about by a decrease of £9,000,000 in imports and an increase of £65,000,000 in exports other than gold.

The total value of the net gold production (i.e. excluding domestic consumption but including the premium received from sales for semi-processing or fabrication of gold for export) increased from £114,000,000 in 1949 to £147,000,000 in 1950. There was actually a slight decrease

in the quantity of gold produced in the Union, but due to a higher average price the value of the gold output increased appreciably.

Taking into account, therefore, the net gold production which was either exported or available for export, the estimated current deficit for 1950 amounted to only £7,000,000 as compared with £114,000,000 in 1949. In 1950, moreover, there was an estimated net capital inflow of £78,000,000, giving a net surplus of £71,000,000 for that year as against a net deficit of £63,000,000 in the previous year.

ANALYSIS OF FOREIGN TRADE.

As far as the decline of £9,000,000 in imports is concerned, those from the United Kingdom decreased by £5,000,000 in 1950 from the record level of £131,000,000 which had been established in 1949, and which had been associated with abnormal imports in anticipation of the extension of import control to goods from the sterling area as well as from non-sterling countries. In the case of imports from the United States, Canada, Belgium and Switzerland, however, there was a decline of as much as £46,000,000, while imports from other countries showed an increase of £42,000,000. This significant diversion of trade is attributable, firstly, to the automatic adverse effect of the devaluation of Union currency on imports from countries which had either not devalued their currencies at all or had not done so to the same extent as the Union; secondly, to the more rigorous restriction of imports from hard-currency countries under the new system of import control, which came into effect as from the 1st January, 1950; and, thirdly, to the revival of trade with countries like Germany, Japan, Italy and Indonesia, which alone accounted for over £20,000,000 of the increase.

With regard to the new system of import control, however, it should be mentioned that the basis of allocation of permits was revised, as from the 1st January, 1951, in order to make a proportionately larger issue of general permits available for imports from any country as against the issue of restricted permits applicable only to goods from soft-currency countries, and thus to widen the field of competition for the Union's import trade. It should also be pointed out that, as a result of their having joined the European Payments Union, Belgium and Switzerland were transferred from the category of hard-currency coun-

tries to that of soft-currency countries during the course of 1950.

While total imports into the Union showed a decrease of only 3% in value between 1949 and 1950, there was, of course, a substantially larger reduction in volume owing to higher prices for imported goods, whose average monthly index rose from 217.5 to 240.3, i.e. by more than 10%. Nevertheless, the volume of imports must have been higher than in any year prior to 1947.

As regards exports other than gold and gold products, the increase of £65,000,000 between 1949 and 1950 was spread over a large number and variety of countries, including both hard and soft-currency countries. Although there was also an increase in the volume of such exports, the increase of 46% in value was primarily the outcome of the spectacular rise in the prices of wool and certain other commodities.

MONETARY AND BANKING SITUATION.

Last year I pointed out that, after a sharp decline from £455,700,000 in March, 1948, to £348,100,000 in September, 1949, the money supply in the Union suddenly reversed its trend, as a result of the favourable turn in the balance of payments, and rose steadily to £393,700,000 by the 31st March, 1950. Between the last-mentioned date and the 31st March, 1951, there was a further increase of £70,000,000 to a new record level of almost £464,000,000, due not only to the continuance of a favourable balance of payments but also to a net creation of bank credit which amounted to about £43,000,000 during the period concerned.

With regard to bank credit, there was an increase of almost £51,000,000 on the part of the commercial banks as against a decrease of £8,000,000 in the case of the Reserve Bank. The commercial banks' discounts and advances in the Union showed an increase of £43,700,000, while their investments in the Union increased by £7,000,000 and deposits with the National Finance Corporation by £150,000.

After having reached a high point of £156,000,000 in December, 1948, the commercial banks' advances and discounts in the Union dropped to about £109,000,000 in April, 1950, due both to the considerable reduction in imports during that period and to the contraction of bank

credit for non-productive purposes, in accordance with the request made to the banks by the Reserve Bank towards the end of 1948. The subsequent rapid rise to £154,000,000 by March, 1951, was associated with the renewed increase in the rate of imports since April, 1950, and with an increased volume of production as well as the substantial rise in prices which automatically caused a greater demand for working capital from industry and trade generally.

Notwithstanding the favourable balance of payments, the commercial banks' cash reserves in the Union declined by almost £4,000,000, due mainly to the increase in Government deposits with the Reserve Bank and in the amount of currency in the hands of the public. This decrease in their cash reserves occurred simultaneously with an increase of £44,000,000 in their deposit liabilities in the Union, as a result of which their cash-reserve ratio dropped from 26.5% at the 31st March, 1950, to 22.3% at the 31st March, 1951.

The increase of £44,000,000 in their deposits was, of course, the counterpart of the net increase in their assets referred to above. Of this amount, £7,000,000 represented the increase in their fixed and savings deposits, which was probably connected with the rise of $\frac{1}{2}$ % in the rates offered by the banks for such deposits since October, 1949, and with the re-introduction of a rate for 3 months' deposits in August, 1950.

Money rates, in general, showed relative stability at the higher levels which had been reached in various sectors of the money market during the previous year. The only noteworthy change was a reduction of about $\frac{1}{8}$ % in the market yields of Government, municipal and public-utility securities with maturities not exceeding 5 years. Thus, in November, 1950, the Government succeeded in raising a loan for 5 years, in conjunction with a longer-term issue and primarily for the conversion of a maturing loan, at a rate of $2\frac{3}{8}$ % compared with a rate of 3% in respect of a similar issue in January, 1950. This reduction in the rates for the shorter maturities was mainly the result of a further accumulation of idle funds, as reflected in the increase in deposits with the National Finance Corporation from £49,465,000 on the 31st March, 1950, to £74,155,000 on the 31st March, 1951.

In spite of the large increase in short-term funds, however, no alteration was made in the rates at which Treasury

bills were issued or in the rate offered for call money by the National Finance Corporation. These rates were maintained at the higher levels established in October, 1949, because there was reason to believe that the plethora of short-term money was a temporary phenomenon, and because it was considered to be sound policy, in the circumstances, not to disturb the rates which constitute the foundation of the general structure of money rates, but rather to continue absorbing the surplus funds and sterilising them for the time being. Thus, at the end of December, 1950, March, 1951, and June, 1951, the Treasury accounts with the Reserve Bank showed credit balances of £29,470,000, £44,400,000 and £40,000,000 respectively, while the credit balances of the National Finance Corporation with the Bank amounted to £7,750,000, £1,800,000 and £6,200,000 respectively.

FACTORS GOVERNING RECENT TRENDS IN MONETARY RESERVES.

After the sharp rise from £52,200,000 on the 16th September, 1949, to £139,900,000 on the 31st March, 1950, due to the revaluation of the gold reserve and the highly favourable initial effects of devaluation on the Union's balance of payments, which I explained in my address last year, the Reserve Bank's holdings of gold and foreign exchange experienced a further substantial increase to £171,800,000 on the 31st March, 1951.

An appreciable addition to the reserves during the first half of 1950 had indeed been anticipated on account of unavoidable delays both in the issue of permits under the new system of import control and in the execution of orders for capital equipment, but there had also been reason to believe that at least a large part of this addition would disappear again in the second half when imports were bound to take place at a higher rate than the average for the whole year. Imports for the second half of 1950 did indeed reach a much higher level than during the first half, namely, £178,000,000 as compared with £127,000,000; and the reserves did begin to fall after the middle of the year, namely, from £153,200,000 on the 30th June to £141,500,000 on the 31st August, 1950. But contrary to expectations the increase was then resumed and continued until the end of March, 1951, notwithstanding the fact that, in the meantime, import control had been relaxed on several occasions

and in various ways, and that the Union Government had voluntarily repaid the \$10,000,000 which it had drawn from the International Monetary Fund at the end of 1948.

The main reason for the unexpected improvement in the monetary reserves after August, 1950, was the exceptional rise in the value of the Union's exports other than gold and gold products. These exports increased from £90,000,000 for the six months ended March, 1950 (i.e. already after devaluation), to £146,000,000 for the six months ended March, 1951. This increase of over 60% was primarily the outcome of the sharp increase in the demand for primary products after the outbreak of war in Korea in the middle of 1950 and the consequent adoption of extensive rearmament and stockpiling programmes by the United States, in particular, and by several other countries on a smaller scale.

A second cause was the net inflow of capital estimated at £78,000,000 for 1950, which exceeded official expectations. This factor was attributable to confidence and interest abroad in the inherent economic potentialities or the strategic importance of the Union; and although there was evidence of money having been transferred to the Union under the stress of international political tension, it was almost invariably invested in one way or another instead of being kept in the highly liquid state associated with "hot" money. The receipt of more than £21,000,000 from non-sterling countries, mainly the United States and Switzerland, which was by far the largest amount of capital obtained in any one year from outside the sterling area, is a welcome sign of the widening interest and participation in the development of our country. Furthermore, early in 1951 the Government concluded an agreement with the International Bank for Reconstruction and Development for a loan of \$50,000,000 in respect of overseas capital expenditure to be incurred by the Electricity Supply Commission and the Railways and Harbours Administration, in addition to the loan of \$10,000,000 and the new revolving credit of \$20,000,000 to which I have already referred. Of this aggregate amount of \$80,000,000, however, an amount of only \$10,000,000 had been drawn at the 31st March, 1951.

Another reason for the appreciable increase in the monetary reserves during the year ended 31st March, 1951, despite the extensive relaxation of import control,

was the fact that overseas supply difficulties were encountered in certain lines of commodities, due, *inter alia*, to the effects of the rearmament and stock-piling programmes. Nevertheless, the actual amount of imports in 1950 (namely, £305,000,000 f.o.b.) was substantially larger than it was at first thought the country would be able to afford; and in the first quarter of 1951 a much higher level was reached, namely, £97,700,000, or at a rate of almost £391,000,000 per annum.

The fundamental point is that, whereas the Union had for some years suffered from adverse terms of trade with its principal overseas suppliers, the tide began to turn in its favour after September, 1949. In the first instance, the widespread devaluation brought relief to the Union through an immediate and appreciable increase in the price of its main export product, gold, in terms of sterling and many other currencies. It is true that devaluation also brought about an increase in the general level of prices in the countries which resorted thereto, and, thus, in the average cost of our imports from such countries, but this increase was much less than the rise in the gold price. At the same time, as explained previously, the Union was able to increase considerably the proportion of its imports from those countries. After the middle of 1950, a further source of improvement in our terms of trade was provided by the exceptional rise in the world prices of wool and other primary products. Thus, while there was also a further increase in the cost of imported goods, it was less than the rise in the yield of our exports.

The net outcome of all the aforementioned factors was that the Bank's holdings of gold and foreign exchange increased to a total amount of almost £172,000,000 at the end of March, 1951. Since that time, however, there has been a substantial decline, namely, to £153,000,000 on the 20th July. This decrease is attributable not only to a seasonal decline in exports and to half-yearly dividend remittances, but also to heavy imports as a result of liberal issues of permits. The monthly average of imports for April and May, for example, amounted to £41,000,000 as compared with an average of £33,000,000 for the first quarter of this year and £30,000,000 for the second half of 1950.

Although the reduced reserves of £153,000,000 still represent a relatively favourable position and are, moreover,

higher than was anticipated at the beginning of the year, it must be borne in mind that there is a considerable carry-over of unexecuted orders from previous years as well as under new permits issued in respect of the current year. In this connection, however, it may be submitted that there is always some lag both in deliveries of goods ordered and in payments for goods actually imported, and that the factor to be taken into account for reserve purposes is not the total carry-over of unexecuted orders or unpaid imports at any particular time, but only that part which is in excess of the normal lag. Nevertheless, after allowance is made for what may be regarded as a normal lag in respect of imports, a substantial excess carry-over is left as a prospective charge against the reserves.

In considering the adequacy of existing reserves, other qualifications have also to be made. In the first place, the rising cost of imports has steadily been reducing the net advantage which the Union came to enjoy in its terms of trade with most countries after devaluation, and again after the outbreak of war in Korea. As far as the present situation can be judged, there is still an appreciable net benefit in favour of the Union compared with the position prior to devaluation, but it must be recalled that at that time we had reason to complain about adverse terms of trade. There is now a possibility that, temporarily at any rate, we might have to face a further substantial shrinkage of the post-devaluation benefit. This danger might arise either from the continuation of the rise in the cost of imported goods without an upward adjustment of the world monetary price of gold, or from a decline in the prices for our exports (other than gold) while the cost of imported goods remained at a relatively high level for some time. Secondly, a contraction of the capital inflow might occur on account of the growing world shortage of capital for development purposes. Furthermore, unless the increase in the cost of imported goods is arrested, the same capital inflow will command an even smaller purchasing power abroad than has been the case during the past year. Finally, although considerable progress has been made with the various programmes of economic expansion and development in the Union, it is likely that, provided the requisite supplies can be obtained from abroad, the Union's imports of capital equipment and other producer goods, as well as more or less essential consumer goods, will

still tax severely our available exchange resources during the next two years.

In view of all these qualifications, therefore, it would appear to be advisable to retain the existing machinery of import control for the time being at least in order to ensure that the plans in hand for both mining and industrial development will not be held up merely because of a shortage of foreign exchange.

RENEWED INFLATIONARY TREND.

Like every other country in the world, the Union experienced a considerable further inflation of prices and costs during the past year. For example, the wholesale price index rose from 195.1 in May, 1950, to 223.3 in May, 1951, and the retail index from 159.2 to 170.4, i.e. by 14½ and 7% respectively.

The renewed world-wide inflationary trend, which was reflected in the Union through both the higher cost of imported goods and the marked increase in the prices for many of its exports, was also accompanied by an appreciable increase in the quantity of money in the Union, as well as in the rate of money turnover; and, as already mentioned, the increase in the money supply was derived, on the one hand, from an internal expansion of bank credit, and on the other, from an external surplus on capital account. The continuation of inflation in the Union was, therefore, the resultant of the combined operation of internal and external factors.

While it is difficult to assess precisely the respective contributions of the internal and external factors to the existing inflation in the Union, due to their continuous interaction and their varying reactions upon one another, there is little doubt that the rising cost of imports has for years been the major source of inflation in the Union. Internal contributory factors have operated with varying effects at different times, but after due allowance has been made for the counteracting or restraining influence of increased production, food subsidies and certain control measures, it can be submitted that the net inflationary effects of internal factors have, on the whole, played a small part as compared with the impact of imported inflation on our general level of prices and costs.

The reason for the predominance of the latter is that the Union is largely dependent on imported goods in vital sectors of its economy and, therefore, at all times tends to suffer automatically from world inflation. While it is true that, as a result of the great increase in the output of our secondary industries, we are less dependent than formerly on overseas supplies, we still have to import large quantities of raw or semi-finished materials for manufacturing purposes as well as finished producer and consumer goods, either because we cannot produce the goods concerned or because we cannot do so in sufficient quantities, particularly in view of the unusually rapid development which is still taking place in our country. In these circumstances it is evident that the rising cost of imports has been affecting our price and cost structure at many different points and in various ways, both directly and indirectly.

It is also clear, however, that the considerable increase in the total volume of public and private expenditures in recent years has played a not insignificant part in the progress of inflation in the Union. This increase in expenditures has manifested itself in large capital outlays on new development and expansion of productive facilities, housing and other building accommodation, and transport, power and other services, as well as in a rapid growth of the current expenditures of the Government and public authorities generally and of all branches of private enterprise, due, *inter alia*, to upward readjustments of salaries, wages and cost-of-living allowances. Although the final result has been a noteworthy and welcome increase in net real investment, both public and private, it has nevertheless provided an additional inflationary influence.

The Union has fortunately been able, in one way or another, to offer substantial resistance to imported inflation. Thus, for example, while the wholesale index for imported goods rose from 100 in 1938 to 230.8 in March, 1950, and 270.1 in March, 1951, that for locally produced goods increased to only 165.3 and 181.1 respectively, in spite of the fact that the higher cost of imported materials and equipment was, to no small extent, also reflected in the prices of goods produced in the Union.

There is, however, no doubt that the recent considerable rise in export incomes and the increasing cost of imported goods have seriously extended and intensified inflationary pressures in the Union and have created favourable condi-

tions for a further general inflation of prices and costs which would, of course, aggravate the existing inequalities and disruptions. Inflation has already caused severe and harmful disturbances in the economic and social relationships between different sections of our community. Furthermore, the obvious deterrent to thrift resulting from a continuous decline in the purchasing power of money, is a matter that must cause grave anxiety in a developing country like the Union, which particularly requires the largest possible proportion of its national income to be saved with a view to ensuring not only that its capital needs will be met, but also that it will derive the maximum benefit from the exploitation of its resources. Moreover, serious complications and disabilities have already been experienced as a result of the extremely high cost of capital equipment for replacements and renewals as well as for expansion and new development, and of construction for productive purposes or the provision of additional housing accommodation.

Thus, the inflationary situation in the Union, as in the rest of the world, has reached alarming dimensions and has created serious problems; and we must face the fact that we shall continue to suffer from external inflationary pressures in a greater or lesser degree as long as inflation prevails in the areas from which we derive the bulk of our needed imports, namely, Europe and North America. For this reason it is gratifying to note that the leading countries concerned now realise more fully the need to take more stringent monetary and fiscal measures, in addition to direct controls, in order to stop the inflationary trend, despite the cost of the Korean war and of the extensive rearmament programmes.

Nevertheless, although we cannot avoid being affected by inflation in Europe and North America, it is within our power to mitigate the impact of imported inflation by restraining purely internal inflationary pressures. While I have already mentioned the fact that the Union has had some success in offering resistance to imported inflation, the question is whether more cannot be done in that direction.

INTERNAL ANTI-INFLATIONARY MEASURES.

Various measures have been adopted as anti-inflationary instruments in the Union. Some of these, such as price

control, rent control and food subsidies, have been criticised in the Union, as elsewhere, on the ground that they deal with the symptoms rather than the causes of inflation and cannot serve as remedies for the disease because they do not attack the root of the trouble. Whether or not they represent only subsidiary and supplementary instruments, it must be admitted that they have proved to be of substantial assistance in the fight against inflation and can be tightened or relaxed as the circumstances require. On the other hand, it is apparent that the principal sources of inflation in the world have been an excessive increase in the volume of total expenditures, i.e. excessive in relation to the increase in production and population, and a rapid expansion of the money supply which provided the essential condition or the necessary setting for the continued growth of expenditures.

In the Union, however, it can at least be said that the increase in the quantity of money in circulation did not emanate mainly from the so-called monetisation of unproductive Government debt, as in many other countries. Between the end of 1938 and that of 1950 there was an increase of £346,000,000 in the money supply of the Union, and also an increase of £16,000,000 in the fixed and savings deposits of the commercial banks, i.e. £362,000,000 altogether. Of this total, the increase in the holdings of Union Government securities by the commercial banks and the Reserve Bank accounted for only £136,000,000 or under 38%; and it must further be borne in mind that a large part of the increase in the internal debt of the Government during that period represented either the counterpart of the net reduction of £67,000,000 in the external debt or productive capital expenditure incurred on the expansion of the railways and harbours, telegraph and telephone services, iron and steel works, irrigation and water conservation projects, Land Bank, Industrial Development Corporation, Fisheries Development Corporation, Klipfontein Organic Products Corporation, etc. The remainder of the increase in the money supply was derived from the increase of £115,000,000 in the advances, discounts and other earning assets of the commercial banks and the Reserve Bank in the Union, the greater part of which was also associated with increased production and trade, and from the increase of £113,000,000 in the net book value of the Reserve Bank's gold and exchange holdings, which was attributable partly to the revaluation of the gold reserve,

but mainly to a net favourable balance of payments over the period concerned.

At the end of 1950, the Reserve Bank's gold and exchange holdings constituted 90% of its note and deposit liabilities and 37% of the total quantity of money in circulation. Although this represents a relatively sound monetary position as compared with many other countries, the fact nevertheless remains that within a period of 12 years the money supply of the Union increased more than four-fold and the national income almost three-fold. It is true that during this period there was also a considerable increase in production and imports, i.e. in the quantity of goods available in the Union. In the absence of complete statistics of the volume of production in the Union, the increase in production between 1938 and 1950 can at least be gauged from the increases of 100% in the total revenue-earning traffic on the railways (in terms of ton miles), 80% in the index of employment in manufacturing industries, and over 70% in the index of electric current generated. Furthermore, after due allowance is made for the rise in the index of prices of imported goods, imports for the four years 1947-50 showed an average increase of 60% over the figure for 1938. The increase in the flow of locally produced and imported goods, however, lagged far behind the increase in total current and capital outlays in the Union.

The obvious remedy would, therefore, appear to be that of tackling the problem at its source, namely, to stop the process of increasing overall expenditures and the money supply and even to reverse the process in order to reduce the evil effects of inflation which have already manifested themselves. Measures to step up production and eliminate waste in consumption would, of course, also contribute toward the stopping of inflation to the extent that they could be applied promptly and effectively.

With regard to the former, however, mention must again be made of the decisive influence on the local situation of the inflated prices for both our imports and our exports and of the inflow of capital from abroad. Notwithstanding this qualification, there would seem to be scope for more positive internal action, and the danger inherent in the current inflationary situation demands whatever can be achieved by anti-inflationary monetary and fiscal policies.

As explained previously, the contraction of bank credit for non-productive purposes and the raising of bank

rates by $\frac{1}{2}\%$ helped to bring about a considerable reduction in bank advances and discounts between the end of 1948 and April, 1950, but did not prevent their subsequent rise to the previous high level within a year. While it is admitted that the renewed expansion of bank credit was associated with an increase in the value and volume of imports and production, it also deserves to be emphasised that the additional bank credit served to increase the available money supply which had already been augmented by a surplus inflow of capital. Prevailing conditions, therefore, require a restrictive policy on the part of the banks with a view to effecting a gradual reduction in the total of their advances, discounts and investments in the Union, at least until the general inflationary process has definitely been checked. The circumstances would appear to call, in particular, for restrictions on the use of bank advances for the direct or indirect financing of consumer credit or of speculative transactions of any kind, or for the provision of fixed capital for productive or distributive purposes, whether against real estate or other collateral.

In this connection, however, it should be added that, for the time being at any rate, the recent expansion of bank credit has largely been neutralised by the high level of Government deposits with the Reserve Bank and the consequent sterilisation of a substantial part of the money supply. Furthermore, since March last there has been a substantial decline in the cash reserves of the commercial banks, due primarily to the unfavourable turn in the balance of payments, which caused their cash-reserve ratio to drop from 22.3% at the end of March to 17% at the end of May. This sudden contraction of the credit-creating capacity of the banks can, therefore, be relied upon to work automatically in the direction of curbing the creation of bank credit.

As far as fiscal policy is concerned, relief from inflationary pressures could also be afforded by reversing the sharp upward trend of Government and other public expenditures or at least by stopping the increase in the total of such expenditures, and also by widening the range of taxes on consumption in order to reduce the effective demand for goods.

The increase in ordinary Government expenditure (i.e. on revenue account) has taken place at an alarming rate during the past twelve years, namely, from £42,000,000

in 1938-39 to £131,000,000 in 1945-46, £156,500,000 in 1950-51 and an estimated amount of over £180,000,000 for 1951-52, while the ordinary expenditure of the Provinces similarly increased from £16,000,000 in 1938-39 to over £57,000,000 in 1950-51. The capital expenditure of the Government, Provinces, municipalities and public-utility undertakings has also reached very high levels in recent years. With regard to such capital expenditure, however, it must be borne in mind that there was not only a heavy backlog to make up in respect of the basic services and facilities demanded by the considerable economic expansion in the Union since the war, but that provision has also to be made for the services required for new development. From the viewpoint of current inflation, on the other hand, it is imperative that the aggregate public expenditures, on ordinary as well as capital accounts, be met without the direct or indirect creation of additional bank credit in the Union. In present circumstances, therefore, it would appear to be necessary to keep public expenditures within the limits of available taxation and of loans capable of being raised from current savings in the Union or from overseas sources for purposes of overseas expenditures.

In this connection, it is interesting to recall that, in his Budget Speech of March, 1950, the Minister of Finance had found it necessary to utter a serious warning against the relentless growth of Government expenditure, particularly on social services and subsidies to the Provinces, of which an appreciable part is also destined for social services, and against the increasing tendency of Parliament to exercise pressure in favour of increased public expenditure. It is clear, however, that the avoidance of any further net increase in Government expenditure would require both a firm stand on the part of the Government and the full co-operation of Parliament.

With reference to increased taxation on consumption, the Budget Speech of March, 1951, revealed that attention had also been devoted to "the possibility of increasing taxes which, apart from yielding additional revenue, (would) have the effect of curtailing consumption and thus alleviate the inflationary pressure". On account, however, of the fact that there were some practical difficulties connected with the introduction of a system of sales or purchase taxes on certain types of consumer goods in the Union, as in the United States, Great Britain, Canada, etc., further

study would have to be devoted to the matter during the recess.

Finally, the fight against inflation demands the whole-hearted co-operation not only of the Government and Parliament, but also of employers and employees and of producers and consumers with a view to increasing productivity and production and also restraining consumption.

GENERAL REVIEW.

The past year has been a period of unprecedented economic activity in the Union, despite the operation of some disturbing factors. As an overall index of economic activity in terms of money transactions, bank debits, for example, increased from a monthly average of £550,000,000 in the first five months of 1950 to £700,000,000 in the corresponding period of 1951, i.e. an increase of $27\frac{1}{2}\%$. There was, however, also a substantial rise in the general price level during that interval. The indexes of wholesale and retail prices, for example, showed comparable increases of $12\frac{3}{4}\%$ and 7% respectively. Nevertheless, after due allowance is made for the rise in prices, an appreciable expansion of the volume of general economic activity is clearly indicated.

A large part of the increased activity in the Union during the past year is to be attributed to the expansion of the output of secondary industries. Apart from an increase in the productive capacity of various existing industrial enterprises, a large number of new factories were brought into operation, many of which represented subsidiaries or affiliates of overseas manufacturing concerns. An important event was the starting-up of the new iron and steel works at Vanderbyl Park, which should make a notable contribution towards relieving the current steel shortage in the Union. Several projects for the manufacture of finished goods wholly or mainly from local raw materials, or for the processing of local materials for use in other industries which formerly were entirely dependent upon imported semi-finished materials, also reached the production stage. In the meantime, new plans have been adopted with the same object in view, the principal one being the oil from coal project.

Although the gold output remained at approximately the same level as in the previous two years, considerable

progress was made with the development of the new gold-fields in the Orange Free State and of new mines in the Western Transvaal, and with the provision of the various ancillary services and amenities. One of the mines concerned recently commenced production and one or two more are expected to do so before the end of the year, while several others should be ready for production next year and the year thereafter. Furthermore, the output of diamonds, platinum and base minerals was increased and in several instances steps were taken either to expand the existing capacity or to develop or explore promising new areas. Arrangements were, moreover, concluded with the United States and Great Britain for the erection of the necessary plant to recover uranium as a by-product of certain gold mines and for the financing of all the capital expenditure involved therein.

There was also a substantial increase in agricultural and pastoral production, due to both relatively favourable weather conditions and higher prices. This applied to foodstuffs and other products which are entirely or principally consumed in the Union as well as to commodities which are produced mainly for export. The result was a net increase in exports of farm products at prices which, in most cases, were appreciably higher than those fixed under the respective controls for consumption in the Union.

The rapid industrial and mining development and the general expansion of productive and distributive activities have, however, created some difficult problems. Last year I had occasion to emphasise the prospects of a serious labour shortage, more particularly in respect of skilled labour. The manpower problem has since become more acute, causing the Government to take steps to speed up immigration and the local training of artisans and also to promote the adoption of wage incentive schemes with a view to increasing productivity. In the meantime other important bottlenecks have begun to manifest themselves, namely, in the fields of power and transport where difficulties are being encountered during periods of peak loads. Moreover, while the existing scarcity of certain essential materials and the delays in deliveries of capital equipment required from abroad have already caused some local repercussions, these factors would undoubtedly have the effect of disrupting several branches of economic activity in the Union if they were to continue for some time.

Apart from such intermittent bottlenecks and shortages, the most disquieting feature of the economic situation in the Union has been the continued increase in inflationary pressures and the consequent further rises in prices and costs. While some relief from both external and purely internal inflationary pressures can be derived from an extension or intensification of local anti-inflationary measures, we must accept the fact that we cannot effectively stop or reverse the inflationary trend until our principal suppliers succeed in doing so. Fortunately, there is now an encouraging prospect of the inflationary process being stopped at the primary source, namely, the United States, where more drastic anti-inflationary measures have been brought into operation. This prospect makes it all the more necessary for us to follow more or less similar disinflationary monetary and fiscal policies in order to prepare our economy for the consequences of a possible turn of the tide abroad. If, on the other hand, inflationary forces once more gain the upper hand in the United States and Europe, we shall not have lost by trying to restrain internal inflation in the meantime and to consolidate the tremendous economic progress which we have made during the past decade.

Finally, it is gratifying and reassuring that the considerable expansion of economic activity in the Union during the past year was achieved concurrently with a net increase in the monetary reserves, despite the appreciable relaxation of import control and, with some exceptions, the maintenance of adequate stocks of goods in the country. Our present gold and exchange reserves, although substantially below the peak of March last, still afford a valuable buffer against adverse influences on our balance of payments and, thus, against sudden disruption of our economy. In view of possible overseas developments, however, it is apparent that the circumstances demand the continuance of a policy of caution in both our external and internal financial affairs.

CONCLUSION.

I would like to take this opportunity of expressing our high appreciation of the valuable services rendered to the Bank by Mr. J. T. Jurgens who retired at the end of last month after holding the position of Deputy Governor for 6 years. On behalf of the Board of Directors and the staff I wish him good health and happiness in retirement.

On the other hand, I have great pleasure in welcoming Dr. E. H. D. Arndt as our new Deputy Governor. As Registrar of Banks during the past 9 years, he frequently came into contact with the Reserve Bank as well as with the commercial banks, and is, therefore, no stranger in the midst of the banking community.

In conclusion, I wish to add a word of thanks and appreciation to our staff for the efficient and expeditious manner in which they continued to handle the increasing volume of work.

At the conclusion of his address the Governor moved "That the Report and Accounts be adopted".

Mr. L. L. French seconded the motion which was then put to the meeting and was carried unanimously.

On the motion of the Governor, seconded by Mr. S. R. Barnes, it was unanimously resolved—

That Mr. W. Duncan Baxter and Mr. W. H. A. Lawrence whose period of office expired on the 1st July, in accordance with the terms of the South African Reserve Bank Act, be re-elected as Stockholders' Representatives on the Board of Directors.

The Governor then moved—

1. That Messrs. Deloitte, Plender, Griffiths, Annan and Company and Messrs. Whiteley Brothers be paid the sum of Two Thousand guineas each, in accordance with the recommendation of the Board, for auditing the accounts of the Bank for the year ended 31st March, 1951.
2. That Messrs. Whiteley Brothers and Messrs. Deloitte, Plender, Griffiths, Annan and Company be appointed Auditors of the Bank's accounts for the current year.

The Resolutions were seconded by Mr. D. J. Tredoux and having been put to the Meeting separately were carried unanimously.

Mr. C. E. James said that on behalf of those present at the meeting and the stockholders generally he wished to thank the Governor for his interesting address. The speech, which would be read by a very much wider public through the medium of the press, would, he felt sure, appeal

not only to financiers and business men, but, because of its clear and simple exposition of economic conditions and tendencies in the Union, would also be of the greatest interest to the man-in-the-street.

After the Governor had suitably thanked Mr. James the proceedings terminated.

1951

South African Reserve Bank

REPORT OF THE GOVERNOR AND DIRECTORS
TO BE PRESENTED TO STOCKHOLDERS AT THE
THIRTY-FIRST ORDINARY GENERAL MEETING TO
BE HELD AT PRETORIA ON THE 25TH JULY, 1951.

The accompanying copies of the Annual Accounts of the Bank and of the Auditors' Report are presented to Stockholders in compliance with the Regulations framed under Section 23 of the South African Reserve Bank Act.

After all expenses had been paid and full provision had been made for Income Tax and other liabilities and contingencies, and after writing off, as shown in Profit and Loss Account, from:—

	£	s.	d.
Fixed Property Account.....	29,237	11	11
Furniture and Fittings Account.....	3,774	17	9
and after contributing to the Pension Fund.	36,500	0	0
	<u>£69,512</u>	<u>9</u>	<u>8</u>
there was left a net profit of.....	£ 943,135	6	3

which was allocated in terms of Section 16
of the South African Reserve Bank Act,
1944, as follows:—

	£	s.	d.
Dividend to Stockholders of 10% per annum.....	100,000	0	0
Reserve Fund—1/10th of remaining surplus.....	84,313	10	
Balance payable to the Government.....	758,821	15	7
	<u>£943,135</u>	<u>6</u>	<u>3</u>

FIXED PROPERTY ACCOUNT.—After application of the provision of £29,237 11s. 11d. shown above, this account is written down to £1 0s. 0d. against which is held fixed property in Bloemfontein, Cape Town, Durban, East London, Johannesburg, Pietermaritzburg, Port Elizabeth and Pretoria.

FURNITURE AND FITTINGS ACCOUNT.—After application of the provision of £3,774 17s. 9d. shown above, this account is written down to £1 0s. 0d. against which is held all the furniture and fittings of the Bank, including Strong Room Equipment and Safes.

DIVIDENDS.—The Directors have declared the following dividends for the past year:—

- (1) an interim dividend of 5% for the half-year ended 30th September, 1950;
- (2) a final dividend of 5% for the half-year ended 31st March, 1951; making a total dividend of 10% for the year ended 31st March, 1951.

CAPITAL STOCK.—Holders of the Capital Stock of the Bank at the 31st March, 1951, numbered 980 of whom 50.5% held less than £500 stock each.

DIRECTORS.—In accordance with the Act, Mr. W. Duncan Baxter and Mr. W. H. A. Lawrence retire by rotation, but, being eligible, offer themselves for re-election.

AUDITORS.—Messrs. Deloitte, Plender, Griffiths, Annan and Company and Messrs. Whiteley Brothers were appointed at the last Ordinary General Meeting to examine the accounts of the Bank for the past year. The Stockholders will be requested at the forthcoming Ordinary General Meeting to determine, upon the recommendation of the Board, the remuneration of the Auditors for the recent audit, and to appoint Auditors for the current year.

Messrs. Deloitte, Plender, Griffiths, Annan and Company and Messrs. Whiteley Brothers offer themselves for re-election.

M. H. DE KOCK, Governor.

J. T. JURGENS	} Directors.
EUGENE O'C. MAGGS	
W. H. A. LAWRENCE	

G. RISSIK, Secretary.

Pretoria, 12th June, 1951.

BALANCE SHEET 31st MARCH, 1951.

	£	s.	d.
Capital	1,000,000	0	0
Reserve	2,419,577	17	3
Notes in Circulation	75,654,002	10	0
Notes of other Banks in Circulation	150,310	15	0
Deposits—			
Bankers' Reserve	36,572,289	0	0
Bankers' Current	22,746,466	17	1
Accounts	53,552,780	14	6
Other Accounts	3,439,307	18	8
Rebate on Bills not yet due	70,786	2	10
Foreign Currency Liabilities incurred as agent for the Union Government—			
United States	3,571,428	11	5
Dollars	2,993,033	4	8
Swiss Francs			
Other Liabilities			
Stockholders—for Final Dividend			
Government—for Remainder of Surplus			
	£206,355,418	14	0

PROFIT AND LOSS ACCOUNT
for the year ended 31st March, 1951.

General Expenditure— (Including Rates, Salaries, Directors' Fees, etc.)	£	s.	d.
Written off—			
Fixed Property ..	29,237	11	11
Furniture and Fittings	3,774	17	9
Pension Fund Contribution			
Profit for the Year—			
Allocated as under:			
(Vide Report of Governor and Directors)			
Stockholders ..	100,000	0	0
Reserve ..	84,313	10	8
Government ..	758,821	15	7
	943,135	6	3
	£1,494,378	2	5

Gross Revenue— after making provision for Income Tax, Rebate on Bills not yet due, Sundry Liabilities, etc.	£	s.	d.
	1,494,378	2	5
	£1,494,378	2	5

G. RISSIK, Secretary.

M. H. DE KOCK, Governor.

PRETORIA,
12th June, 1951.

J. T. JURGENS
EUGÈNE O'C. MAGGS
W. H. A. LAWRENCE

To the Stockholders of the
South African Reserve Bank.

We have audited the Balance Sheet dated 31st March, 1951, above set forth and report that, in our opinion, the Balance Sheet is a full and fair Balance Sheet and is properly drawn up so as to exhibit a true and correct view of the whole of the Bank's affairs according to the best of our knowledge and the explanations given to us and as shown by the books of the Bank as at 31st March, 1951. We also report that, in our opinion, the affairs of the Bank have been conducted in accordance with the provisions of the South African Reserve Bank Act, 1944, and the Regulations thereunder, so far as they affect the Balance Sheet and Accounts.

DELOITTE, PLENDER, GRIFFITHS, ANNAN & Co.,
WHITELEY BROTHERS,

Auditors.

Pretoria, 5th June, 1951.

BRANCH OFFICES.

BRANCH:	AGENT:
BLOEMFONTEIN	E. MOORE.
CAPE TOWN	H. J. ALSTON.
SUB AGENT	C. J. G. VAN HOOGBURDEN.
DURBAN	A. F. HALLIDAY.
EAST LONDON	R. H. MILLS.
JOHANNESBURG	A. F. CELLIERS.
SUB AGENT	R. E. SPENCE.
PIETERMARITZBURG	N. K. SPRADBURY.
PORT ELIZABETH.	A. J. VAN ZYL.
PRETORIA	C. T. VORSTER.
SUB. AGENT	G. LUSCOMBE.

