FREE MARKET FOUNDATION

PO Box 4056 | Cramerview 2060
011 884 0270 | gailday@fmfsa.org

Free Market Foundation Submission on Exchange Control Regulations

To: Committee 1 (Triple Challenges of Inequality, Poverty and Unemployment)
High Level Panel on the Assessment of Key Legislation

By: Free Market Foundation

1. The Free Market Foundation

The Free Market Foundation (FMF) is an independent non-profit public benefit organisation founded in 1975 to promote and foster an open society, the rule of law, personal liberty, and economic and press freedom as fundamental components of its advocacy of human rights and democracy based on classical liberal principles. It is financed by membership subscriptions, donations and sponsorships.

2. Introduction

Economic freedom is central to South Africa being emancipated from the triple challenges of poverty, inequality, and unemployment. However, when the ability of individuals to take the money they have earned through hard work and persistence, with them when they leave South Africa is robbed of them, foreign investors will think twice about bringing money in in the first place.

Exchange control in South Africa takes place by way of the Exchange Control Regulations (1961), as promulgated by Government Notice R.1111 of 1 December 1961 and amended up to Government Notice R445 in Gazette 35430 of 8 June 2012. These regulations are imposed in terms of section 9 of the Currency and Exchanges Act (9 of 1933). That Act was repealed by the Reserve Bank Act (29 of 1944), however, the Regulations remain in force.

3. History of exchange control

Exchange controls were introduced in 1961, less than one year after the horrific Sharpeville massacre which shocked the world and set the tone for the next four decades of civil strife in South Africa. In response to the sudden loss of foreign investment and an outflow of foreign exchange, the Apartheid government acted quickly to attempt to mitigate the effects on the local economy.

The controls were eased after the recommendations of the Commission on Exchange Controls in 1978 but were once again strengthened during the 1980s when heavy international sanctions were imposed on South Africa in solidarity with the anti-Apartheid movement.

The system of exchange control is based entirely in the Apartheid government's bid for survival. In a democratic country which engages in peaceful and open trade with the rest of the world, the system is an unnecessary limit on the economic freedom of all South Africans.

4. Abolish all exchange controls

Tito Mboweni, former Governor of the Reserve Bank, acknowledged in 2005 that the time had come for exchange controls to be dismantled. "For all intents and purposes", said Mboweni, "exchange controls have become purposeless." Indeed, in light of South Africa's democratic dispensation and open trade with other nations, and the lack of an authoritarian regime fighting for its survival, these measures have become redundant and are now simply a costly administrative exercise which unduly limits economic freedom.

South Africa's low saving rates and, recently, its stunning lack of economic growth, necessitates a welcoming environment for foreign investment. As FMF director Jasson Urbach asks, however: "Why would a foreigner want to invest in any country if they knew that they could not easily get their dividends out of it? Instead, they will simply invest in economies that welcome their money and do not impose [foreign exchange] controls."

Moreover, exchange controls also stand to scare off local investment. It signals, first and foremost, an unfortunate lack of confidence from the government. If the State is hopeful for South Africa's future, and believes its economic policies are working, why would it seek to forcefully limit the money that entrepreneurs can take out of the country? Indeed, strict exchange controls have a counter-intuitive effect: they lead to capital flight and local investors taking their money elsewhere. In the face of economic uncertainty a successful individual will bear the minor cost of getting the wealth out of the country to ensure it will survive elsewhere. If the government is confident in its own policies then it should not fear excessive amounts of capital leaving South Africa.

The history of exchange controls are tainted by the bloody hands of the Apartheid government in the wake of Sharpeville. The exchange controls are illogical and counter-intuitive. Finally, they limit the economic freedom of all South Africans without justification in terms of section 36 of the democratic Constitution.

5. Conclusion

In light of the above, the FMF proposes the abolition of all exchange control measures, including the repeal of section 9 of the Currency and Exchanges Act, and the repeal of the Exchange Control Regulations.

Attachment

1. Article: Exchange controls are an apartheid relic and should be abolished

Attachment to FMF submission on exchange controls

Exchange controls are an apartheid relic and should be abolished

In November 2005 the Reserve Bank Governor at the time, Tito Mboweni said, "For all intents and purposes exchange controls have become purposeless ... the cost of exchange control administration and the inconvenience that goes with managing (it) might not be worth the exercise". New calls to scrap the last remaining remnants of this apartheid legislation are now being made. Calls which should receive the hearty support of every South African who wants to see our country grow.

Although Mr. Mboweni's comments could not have made him popular amongst some of his peers, he recognised that exchange controls create endless hassles for investors wishing to enter into transactions with foreigners and that these costs far outweigh those of 'lost' employment at the Reserve Bank in the forex control sectors. Indeed, the much greater costs of forex controls are the lost investment opportunities, by both foreign and local investors, that are seldom visible or measurable.

Because of the relatively low savings levels of its citizens, SA desperately needs foreign investment to fund capital expansion programmes vital for future growth and employment opportunities. Why would a foreigner want to invest in any country if they knew that they could not easily get their dividends out of it? Instead, they will simply invest in economies that welcome their money and do not impose forex controls.

Moreover, what message do forex controls send to local investors? One factor frequently under-appreciated is that domestic investor's base their decisions on future prospects and are rightly sceptical of the motivations behind forex controls. Forex controls are counter-intuitive. They push domestic investors away from trying to keep their money within the country's borders, to seeking out any suitable foreign investment to hedge against future uncertainty in the local economy. With no forex controls in place, there would be peace-of-mind that the government is confident in its country's future and a lot of this 'insurance' investment would not be necessary. Removing exchange controls would increase the level of freedom for citizens. In any country where individual freedoms and rights are valued, the threat that its citizens may vote with their assets by investing them elsewhere, will keep the government in check, responsive and accountable to its people.

It is important to note that Rands never really 'leave' SA through the foreign exchange mechanism. All that happens is that they are exchanged for other currencies and remain for use in SA. After all, this is the only place where they are useful! For example, when a South African travels to the US, he cannot exchange Rands for goods and services while he is in the US – what on earth will the Americans do with those pieces of paper with pictures of the 'big five' on them? When a South African and an American exchange Rands for Dollars, no wealth leaves the country and none enters it. Neither country is made richer or poorer by exchanging currency. A country's wealth is derived from its production of goods and services, not the ratio of foreign to local currency owned by its citizens, government or foreigners.

High growth countries deliberately set out to create the kind of environment that will attract risk-taking entrepreneurs and investors. They do this by producing goods and services that other people actually want. They cut down on taxes and red tape, and, most importantly, refrain from attempting to prescribe to law-abiding local and foreign firms what they may and may not do with their own money.

SA is in a position to send a strong signal to the rest of the world that our economy is open to business. Eliminating these remaining vestiges from the apartheid regime will ensure that to the extent that the Rand may be unduly affected by these controls, our currency will return to its true value.

A common feature of all economically successful nations is that their citizens are not constrained by laws that undermine individual rights and liberties. Advanced economies achieve higher levels of economic growth through higher levels of individual rights and economic freedom – no country has ever grown appreciably by being closed off to the rest of the world. Innovation and competition – the real drivers of economic growth – are stifled when governments seek to control their citizens at every turn. There is nothing to wait for and everything to gain and the ideal opportunity to abandon this failed apartheid policy neatly presents itself on 27 October at the medium-term budget speech. For SA to grow, it can and should abolish exchange controls now.

Jasson Urbach
Director, FMF