

SA must raise its savings rate to foster economic growth

**TIME TO
TIGHTEN BELTS**

Nhlanhla Nene

SINCE the motto for this year's savings month is "Tighten Your Savings Belt", I thought it appropriate to share a joke with you: "What did the zero say to the eight? Your belt's a little tight, isn't it?"

The present downturn has meant considerable belt tightening. There are clear signs that economic realities have prompted businesses and households to address their balance sheets, by reducing consumption and saving more. South Africa's gross savings rate as a proportion of gross domestic product (GDP) rose to 17.1 percent in the first quarter, up from an average of 15.4 percent in 2008.

But even with the recent rise in South Africa's saving rate, our savings performance remains disappointing. Our savings rate is low by international standards and compares especially poorly with those developing countries with high rates of economic growth. In China, for example, the gross savings rate is over 40 percent.

Recent events remind us to expect reversals of fortune. The crisis has highlighted the danger of being overly dependent on others and the importance of making responsible decisions for the future, as individuals, representatives of firms and as an economy.

South Africa's aggregate savings have been on a declining trend because of the decline in corporate and household savings. Savings from the corporate sector represents the bulk of total savings, but the corporate savings ratio has fallen in net terms from 6.6 percent of GDP in the 1980s, to 5.6 percent in the 1990s and to only 3 percent between 2000 and 2008.

Household savings as a percentage of GDP have also declined sharply over the last 15 years, from 3.2 percent during the 1980s to 0.2 percent between 2000 and 2008.

As a percentage of disposable income, household savings have fallen from around 5.4 percent in the 1980s to 0.28 percent between 2000 and 2008. As a consequence,

household debt has risen steadily in recent years, and currently stands at 76.7 percent of disposable income.

South Africa is not alone in having experienced a declining household savings rate. Household savings rates have steadily declined in a number of Organisation for Economic Co-operation and Development countries where government benefits are high, the volatility of inflation and interest rates has declined, and financial innovation has increased access to credit.

Household saving rates tend to be higher in developing countries such as China because of limited social security nets and limited access to retail credit.

Fiscal prudence and strong growth in

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tax collections after 1994 contributed to a marked improvement in the government's savings performance. After dissaving on a net basis for 23 years, gross government savings as a percentage of GDP turned positive in 2001. However, the financial crisis and slowdown in domestic economic growth has seen government saving decline as revenue fell below budget estimates.

South Africa's low rate of saving is worrying for several reasons. Inadequate savings leave households vulnerable to shocks to income and rising prices. They constrain individuals' ability to put down deposits for large assets like houses, affecting wealth accumulation. Likewise, low levels of individual saving add to the burden on the government to provide retirement assistance.

Savings support capital accumulation and economic growth, as investment tends to raise productivity and global competitiveness. A higher savings rate can help smooth the business cycle because firms and individuals have a buffer during difficult times.

The more a country saves, the more investment can be funded from internal sources without requiring foreign capital in-

flows. Shortfalls between domestic savings and investment lead to current account deficits and the need for foreign capital inflows to finance the gap. Persistently high current account deficits can lead to macroeconomic instability if foreign liabilities rise too much and capital inflows dry up.

On the other hand, a higher savings rate and reduced spending is putting a brake on already sluggish aggregate demand.

Fortunately, fiscal policy has, over the past number of years, created space for increased spending by saving the windfall gains from above-potential growth.

The severity of present circumstance has compelled thriftier behaviour. But a more permanent shift requires policies that foster a savings culture. The government is contributing to this culture shift in several important ways.

Firstly, prudent macroeconomic policy creates an environment conducive to saving. Inflation targeting, for example, protects the purchasing power of savers and implies that savings are able to attract competitive real rates of interest. It must be noted, however, that low inflation itself may be a disincentive to save since households may be less inclined to hedge against future inflation by saving more.

Policy must therefore create conditions conducive to higher investment, economic growth and job creation because it is ultimately these factors that enhance the ability of corporates and individuals to save.

The government is committed to supporting economic growth and job creation in several ways, notably through its infrastructure development programme, labour-intensive employment programmes and through education and skills development. Income tax reform has also provided relief for savings through higher limits for interest earned on savings.

Creating an enabling environment also requires addressing barriers to saving, particularly those that are binding for poorer individuals.

The first of these barriers is affordable access to savings and transaction services. Several initiatives deserve mention:

- The Mzansi bank account, which has drawn in many first-time users of financial services. Uptake now exceeds 6 million.

- The retail savings bond initiative has attracted almost 33 000 investments, with an investment amount of over R4.2 billion.

- The National Credit Act has played an important role in reducing consumption-driven debt and ensures that the credit



Deputy Finance Minister Nhlanhla Nene says South Africa's savings rate has declined drastically since the 1980s, particularly for households and businesses. PHOTO: SIMPHWE MBOKAZI

market is accessible, efficient and non-discriminatory.

A second important barrier to saving is a lack of financial literacy. The Finscope 2008 survey revealed the extent of misunderstanding of financial terms and the lack of financial knowledge among South Africans. The need for financial education, and education more generally, is clear.

Postering a savings culture also requires making saving a "cool" and intelligent choice. The South African Savings Institute makes an important contribution

in this regard, by promoting a culture and an awareness of the importance of saving.

To conclude, South Africa's low savings rate puts the economy's ability to grow in a sustainable manner at risk. It is crucial to raise the level of our national saving in support of both short-term economic stability and long-term productivity growth and prosperity.

This is an edited version of a speech given yesterday by Deputy Finance Minister Nhlanhla Nene at the SA Savings Institute breakfast