

Postulations for increasing South Africa's savings rate

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Abstract

The decline of savings rates in Africa as a whole is something which has attracted attention worldwide. This problem is something which includes South Africa, despite the strong development that has occurred within South Africa's economy over the past decade. This essay thus examines the issues constraining personal savings, some of which occur worldwide, as well as the attempts being made by the Government to increase savings through its offering of Retail Bonds as well as the private 'Mzansi' banking account and its investigating the reformation of its social security system. The essay concludes that policies focusing on furthering the financial knowledge of the poor and developing the local banking system may hold more importance than reforming the social security system, based on varying literature regarding the investigated behaviour of the poor both in South Africa and America as well as various commentaries on social security systems.

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1. Introduction

South Africa's poor national saving rate of only 13.8% is of much interest due to the implications that a low savings rate has on economic growth. A large portion of the South African population has descended from those with little/no experience in formal savings, causing a similar pattern of living and perhaps a further future decrease in savings, if no remedy is discovered. This essay will thus examine factors contributing to the low private savings rate, current initiatives in place to increase savings as well as possible alternative solutions with the focus being placed on low-income earners in the economy, as these constitute the majority of those not formally saving in the economy.

2. Personal Saving Constraints

The poor personal savings rate of 1.5% of GDP (South African Reserve Bank, 2006:13) can be attributed to various factors. Some of these are faced internationally while others seem to be particular to South Africa. Before adequate solutions to the savings problem in South Africa can be formulated these factors must be explored. Let it be noted, however, that although these factors are categorised separately below, they overlap and effects overflow into each other.

Consumption and Saving

South African household savings has decreased with the increased expenditure and debt patterns – 2006 saw household expenditure increase by a further 7% (Manuel, 2007:6) with the debt to income ratio rising to 73% in the third quarter of 2006 (South African Reserve Bank, 2006:13). From the latter figures it is evident that much of household spending is financed through debt, decreasing disposable income further with debt service costs and further decreasing any residual amount of disposable income which could otherwise be saved (Mohr and Fourie, 2005:468). The problem that occurs with low income earners, however, is that any residual is scarce. The following paradox in South Africa thus emerges: financial liberalisation, which marks a developing economy, is also a contributing factor to the economy's poor saving rate. A study by the World Bank showed this and stated that South Africa's decrease in personal savings has been caused by financial liberalisation, but the increase in corporate savings has been due to the development (Loayza et al, 2000:408). Hence, the greater availability of credit has been helpful in developing the corporate sector of South Africa (thus generating greater savings), whilst the decrease in liquidity constraints has also been detrimental to household savings as it has made increasing consumption beyond one's means possible.

A further issue affecting savings is the cost of saving. The first of such costs are the actual bank charges attached with holding an account. These amounts consume a substantial portion of the poor's income. Costs such as withdrawal and deposit fees make it even more unattractive for those earning a

small amount to make use of the formal banking sector and hence most only hold bank accounts in order to receive their salaries and summarily withdraw the entire amount at once to minimise costs (Collins and Taljaard, 2005e:2). A further cost which causes the poor to keep their money on hand is the cost and inconvenience of travelling to an ATM in order to make a withdrawal by those living where there are no ATMs or bank branches (Collins and Taljaard, 2005e:2). The issue of high costs affecting low income earners has been recognised nationally and is mentioned by the National Treasury that low income earners are in fact “penalised” for saving (National Treasury, 2007:para10).

Public Saving vs. Private Saving

In his national budget speech, Minister Trevor Manuel described his elation at South Africa’s attaining its first budget surplus and commented further that this surplus was to signal private saving (Manuel, 2007:10). Despite this being a great achievement for the fiscus, it is submitted that high public savings actually decreases private savings through mathematically showing that an increase in public saving by 1% may decrease private saving by up to 0.6%, whilst policies implementing higher government spending have a positive effect on private saving (Elbadawi et al, 2000:15). A similar fact is stated in Green et al (2005:37) where the authors declare that public saving crowds out private saving.

Lack of Formal Incentives

A common fallacy is that the poor do not save, but it has been found that saving is rife among the poorest rural areas with saving occurring in an informal manner (Green et al, 2005:32). Low-income South African households have been found to have up to seventeen financial instruments where on average four of the seventeen are for saving, but only 30% of the seventeen are formal instruments (Collins and Taljaard, 2005b:2). Hence, the lack of formal saving among the poor must be partly due to a lack of incentives offered by formal institutions. Green et al (2005:47) observe that the lack of a real interest rate offered by saving institutions means that the poor will borrow and lend from each other – something common to South Africa.

In order to offer a real interest rate, banks must offer interest rates exceeding the inflation rate of approximately 5% (South African Reserve Bank, 2006:19). Savings and transaction accounts from Nedbank, Standard Bank, First National Bank and Capitec Bank were investigated to determine how many accounts offer a real interest rate with the lowest minimum required amount. Nedbank offers two investment accounts, the first with a minimum deposit of R1000 attracting an interest rate of 5.7% and the second with a minimum investment of R1000 with a month’s investment term and an interest rate of 7.35%. Standard Bank only offers its ‘PureSave’ account with an interest rate of 5%

and a minimum deposit of R1000. First National Bank offer a '32 day' account which offers 5.6% to minimum amounts of R1000 as well as a 'Flexi-Fixed' account which offers 7.75% to amounts greater than R100, but with a minimum term of twelve months. There is also a 'Fixed Deposit' account which allows minimum deposits of R100 with monthly investment terms available and interest rates beginning at 6%. Of the three banks, Standard Bank offers the best interest rate to the 'Mzansi' account, which is 1.75% for amounts less than R500. The most beneficial account found was one offered by Capitec where the minimum amount is R10 and an interest rate of 10% p.a. is offered. As is visible, however, there are not many accounts offering real interest rates to small amounts. When the various and numerous charges are considered as well as the inconvenience many experience in gaining access to a bank and the effect of inflation on one's money, it is no surprise that the poor choose informal means by which to save.

Lack of Precautionary Attitude and Adequate Knowledge

If savings is defined as an expression of the importance placed on present consumption versus future consumption (Cashwell, 2005:4), then it can be said that South Africans apparently lack adequate foresight and planning. This opinion is confirmed when one compares low-income earners of South Africa with those in America. In the 'Financial Diaries' study (Collins and Taljaard, 2005e:3) it was found that the studied South African households held little/no precautionary savings. Any savings, other than 'in-house', were often accumulated in stokvels or savings clubs for a specific purpose (Collins and Taljaard, 2005e:5). By contrast, a study done in America on low-income households found that individuals thought it wise and responsible to hold preventative amounts of savings (Sherraden et al, 2006:90). The subjects of the American study were given savings accounts wherein the individuals received financial education. Thereafter, the subjects commented that they were able to increase their savings as a result of the training received, which led to more efficient consumption as well as a more precautionary outlook to their money (Sherraden et al, 2006:91).

3. Current Savings Initiatives

In an effort to encourage the personal savings rate in South Africa, the following attempts have been made: the 'Mzansi' bank account; the government Retail Bond; and the Social Security Reform. Although this is not an exhaustive list, they are current government-driven efforts at increasing a rather dismal private savings rate.

The 'Mzansi' Account

The 'Mzansi' account is designed to be a low-cost account which is purposed at attracting those previously unbanked into using it. In a little over a year of its being implemented, it attracted approximately 1.5 million new users of which 90% were believed to be previously unbanked

(SouthAfrica.info, 2005:3). Although no management fees on the account are charged, only one free deposit per month allowed, any other transactions are charged and, as stated above, the best interest rate available is a meagre 1.75%. Hence, there is little motivation to hold their money therein as the small interest income which their capital would attract would hardly cover the cost of making more than one withdrawal, let alone the cost of getting to an ATM or bank branch.

The Government Retail Bond

The Government has gone a long way to make the Retail Bond an attractive option by making it very easily accessible (through purchasing online, at a Post Office or through posting the relevant documents to the National Treasury head office (National Treasury, unknown:3)) as well as by making the interest rate market-related. Despite these attractions, the bond has the following drawbacks – a) the minimum investment term is two years. Although this is relatively short in terms of investments, lower-income earners require the ability to liquidate their savings quickly and easily due to shocks that are experienced (Loayza et al, 2000:402), making the bond quite restrictive; and b) the bond prices are in R1000 increments. Since the majority of the population earn below R800 per month (Table 1, below) this means that one in such a position would have to save for a considerable amount of time before being able to purchase a bond, and then wait further for their return.

Social Security Reform

The current social security system is funded by government revenue, but suggested international practice is to fund the system through mandatory, income-based payments by citizens in order to make the system more beneficial (National Treasury, 2007:para23). If this is to happen, and be effective, individuals will have to contribute between 13%-25% of their income, depending on the reformed system's details (National Treasury, 2007:paras67 and 68). This is evidently a large portion of individual income in a country where real per capita income is quite low (UNICEF, 2004:5). Furthermore, there are many American authors who are overtly opposed to social security systems as a means to improve national saving rates and who state that social security welfare actually decreases savings (Feldstein, 1996:162) for the following reasons: a) social security reform may decrease national saving due to the fact that collected revenue is directly paid to the beneficiaries, thus increasing government expenditure (Page, 1998:2); b) it was measured that each dollar of social security wealth acquired would reduce private saving by between zero and fifty cents (Page, 1998:3); c) the benefits that will become due to those making payments now will not necessarily depend on their faithfulness in contributing, but on the future generation's willingness to contribute (Shipman, 1995:2); and d) that amount of income, which is legally required, could be put to better use into investments that would yield better returns (Shipman, 1995:2). Much of this thinking is based on

empirical evidence as well as the theory that individuals expecting to receive income later from the government will not necessarily make their own provisions now (Loayza et al, 2000:399). Despite these opinions, there are countries which have successfully implemented social security reforms and seen an increase in their savings rates.

4. Possible Solutions

Based on the above discussions concerning constraints on private savings as well as flaws with the contemporary implemented initiatives surrounding saving encouragement the following suggestions are made.

Credit Restrictions

Although a growing economy is partly characterised by the relaxing of liquidity constraints and financial liberalisation, it has been noted above that this has actually contributed to the decline in private saving. Hence, it is suggested that credit restrictions on goods which can not be considered as capital goods be implemented. The implication being that individuals should not be able to attain credit, in-store or otherwise, for leisure-based goods and clothing or for food bought for private consumption. The impact that this will have is a slight slowing of economic growth in the short term (Aron and Muellbauer, 2000:37) as consumers adjust their consumption patterns in such a way that forces them to save rather than pay off goods. If implemented correctly, this will also make more of individuals' income available to them through the diminishing of debt service costs. This would also go far to help satisfy Minister Manuel's request for consumers to save or settle their debts in light of the generous tax relief (Manuel, 2007:23).

Reformation of the Banking Sector

Despite South Africa having one of the most developed banking sectors in the world, there are three areas in which further development is suggested:

a) extending banks into rural areas. South African banks seem eager to integrate rural South Africans into their banks, but not eager to integrate themselves into rural areas. The opening of banks into rural areas is mentioned as a policy necessary for increasing private saving in Green et al (2005:55) as it expands access to formal institutions. In doing so, banks would be able to better understand their clients and perhaps adjust their services to accommodate them. Low-income earning South Africans seem to actually be quite good at saving in groups (Collins and Taljaard, 2005) through stokvels and the like and hence perhaps banks would be able to develop products similar to these, thereby assisting those in need of better returns for their money whilst extending their own client-base;

b) developing accounts for low-income earners which offer higher interest rates for smaller amounts. Banks need to develop products which target low-income earning clients through offering much higher interest rates with fewer restrictions and charges. This is needed because low-income earners often do not have large amounts in their accounts and current interest rates offer such negligible income, even for them. Perhaps new accounts could be income-based with those above a certain bracket being denied access to such accounts. This is suggested because, as mentioned above, the vast amount of the population earns less than R800 per month, making it possible for banks to offer interest rates well above 10% to this bracket of persons due to the small deposits that can be expected. Formal institutions need to make formal banking as attractive as possible. Such a policy may require subsidisation by the government for banks to cover extra administrative expenses and to keep costs for the clients low; and

c) diminishing financial restrictions to low-income earning clients. Bank Rakyat Indonesia performed a survey whereby it was found that, in terms of credit, prompt availability and access were more important than the interest rate thereof (Bank Rakyat Indonesia, 2004:1). Hence, the same can be assumed to be true for the poor's savings – it will be held where it can be accessed quickly and conveniently, irrespective of the interest rate; most often this in their house or with a family member or friend. Hence, the South African banking system needs to create very flexible and convenient banking services for them. This would partly be taken care of by point a), but perhaps banks could also offer ATMs with facilities that allow the poor to draw coins so that they are not forced to overdraw. Banks to discover what exactly would make banking easier for those who are previously and currently 'unbanked' as "what developing countries often lack is an appropriate financial sector, which could provide incentives for individuals to save, and acts as an efficient intermediary to convert these savings into credit for borrowers" (Green et al, 2005:29).

Training to Save

In the above-mentioned study of low-income households held in America, most commented that they found it easier to save when those running the program assisted them in doing so and created goals for their savings and spending (Sherraden et al, 2006:91). Thus, to assist in developing a culture that promotes saving over the use of credit (National Treasury, unknown:2) it is necessary to institute programs which can teach low-income earners how to better allocate and spend the little income which they do receive, as well as skills such as interest calculations etc. This may be more important than providing better products as some who do hold provident funds comment that they do not know how it works or how much they have and "are too afraid to ask too much about these funds for fear of losing their jobs" (Collins and Taljaard, 2005:2).

5. Conclusion

It is concluded that there is indeed a multi-faceted problem with private saving in South Africa, requiring a multi-faceted solution. It is submitted that things such as financial education and banking sector development should take priority over social security reform due to the uncertainty that the latter will in fact be effective in South Africa, particularly amongst low-income earning individuals, and the positive effects of the former.

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Appendix

Table 1

Geography by Income category for Person weighted

	No income	R1 - R400	R401 - R800	R801 - R1600	R1601 - R3200	R3201 - R6400	R6401 - R12800	R12801 - R25600
Eastern Cape	4836199	348320	706771	182394	156364	123459	55585	14865
Free State	1842144	249351	277253	117381	103533	69140	32967	8769
Gauteng	5282118	317838	692445	781247	669169	514375	330887	155304
KwaZulu-Natal	6868822	540327	838074	392209	345674	253010	122803	39314
Limpopo	3958868	410959	525404	123398	117449	89521	32952	7574
Mpumalanga	2204248	235998	306970	144356	109676	69311	35069	10640
Northern Cape	508847	64682	122126	38654	37814	29610	14177	3972
North West	2557504	220410	365938	198625	177222	91970	39006	11008
Western Cape	2543739	181106	517133	431522	353217	266294	143121	56891

	R25601 - R51200	R51201 - R102400	R102401 - R204800	R204801 or more
Eastern Cape	4914	3007	4232	654
Free State	2790	1798	1253	396
Gauteng	56072	19571	12333	5820
KwaZulu-Natal	12573	6260	5368	1582
Limpopo	3017	2187	1828	483
Mpumalanga	3162	1699	1418	442
Northern Cape	1250	747	671	176
North West	3400	1818	2036	413
Western Cape	17929	6801	4667	1914

Source: Space-Time Research, 2001