South African Reserve Bank

Date: 25 March 2020

The South African Reserve Bank (SARB) will commence purchasing government bonds. Since the introduction of this measure, announced in a media statement issued by the SARB on 25 March 2020, the SARB has received numerous media queries. This ‘frequently asked questions’ page aims to help explain some of the issues raised.

1. In layman’s terms, what has the SARB done and why?

The SARB has entered short-term funding markets, providing additional liquidity in exchange for repurchase agreements for maturities of up to 12 months. This will assist with the continuous flow of funding to institutions over different time frames. In normal market conditions, such funding is readily available. It has become less abundant in recent days due to high risk aversion.

The SARB will also commence buying government bonds in what is called the secondary market. The SARB will not buy bonds directly from government, that is, in the primary market. The purchasing of government bonds in the primary market is prohibited by section 13 of the SARB Act 90 of 1989, as amended.

These purchases should help to reduce excessive volatility in the price of government bonds. The bond purchases will be held by the SARB in the Monetary Policy Portfolio (MPP). The MPP is a liquidity management tool of the SARB, and can be used for both injecting and draining liquidity. These purchases support ‘price discovery’ – when buyers and sellers easily reach an agreed price for their transactions.

Each of these operations is done in accordance with the SARB’s responsibility to ensure the smooth functioning of our financial markets and that prices are set in an orderly manner.

2. Why has the SARB done this?

Since the outbreak of COVID-19, financial markets, such as the money, bond, equity and foreign exchange markets have seen extraordinary levels of volatility and extreme price movements. Among its functions, the SARB has the responsibility to ensure that its monetary policy decisions are effective and that these decisions have an impact, even if it is an indirect effect, on the cost of borrowing in the economy.

In addition, the SARB has a responsibility to ensure that financial markets operate smoothly and efficiently. Owing to the volatility and the sudden movement of many prices over the past two weeks, the SARB has implemented several measures to provide liquidity into the market, to stabilise markets and to ensure their orderly functioning. Orderly functioning in the market for government bonds is important for financial stability, and indirectly ensures the effectiveness of monetary policy by keeping market prices for assets consistent with the repurchase rate.

3. What does the SARB aim to achieve?

Orderly functioning in the market for government bonds is important for the sustained financing of government, for financial stability and for monetary policy. This ‘price discovery’ – the easy matching of buyers and sellers of bonds – can be upset by sharp spikes in risk aversion in local and overseas financial markets. The SARB’s action seeks to ensure that buyers and sellers conclude transactions more easily.

4. Is this a form of quantitative easing?

No, it is not quantitative easing. The SARB is seeking to reduce dysfunctionality in the market rather than determining prices. This may, however, result in price movements as demand and supply come into alignment. This is, however, not the primary objective.

Quantitative easing is generally applied where interest rates are zero or close to zero, and inflation is far below the central bank's target or even threatening to turn negative. In advanced economies where interest rates are at or close to zero, quantitative easing has been implemented through the purchase of a range of assets to support growth and investment. In general, these countries have used quantitative easing to raise the level of inflation. The SARB is not seeking to do this. South Africa does not have interest rates at or close to zero and the SARB is therefore not using this tool as a means to stimulate demand. The SARB's intervention is a financial market tool aimed at injecting liquidity into the market and ensuring a smoothly functioning market, rather than for economic stimulus purposes.

5. Is the SARB monetising the government deficit?

No, we are not monetising the government debt. The SARB is not giving money directly to government and is not buying bonds from government. In terms of the SARB's legal framework, it is not permissible for the SARB to lend directly to government or to print money to finance the government deficit. The SARB is injecting liquidity into the market and smoothing the market by buying bonds from banks, asset managers or other participants who hold them.

6. Where does the SARB get the money from to buy these government bonds?

For purposes of implementing monetary policy in the market, the SARB can create money to buy assets, thereby injecting money into the market, easing financial conditions. It can also drain liquidity from the market by selling the bonds and thus tighten financial conditions.

7. Is this akin to printing money and will it cause inflation?

When risk aversion increases and economic actors sell assets for cash, this generally takes cash out of the markets. This can have negative effects on the economy and also lead to further declines in asset prices. The SARB's action supports demand for those assets by being a buyer for some of those assets and, in the process, injecting cash into the markets. Under these circumstances, the SARB's actions are not likely to lead to higher inflation.

It should be noted that the Constitutional mandate of the SARB is to maintain price stability in the interest of balanced and sustainable growth. The measures taken in the market are aimed at both: maintaining price stability and ensuring balanced growth.

8. What is the scope and time horizon over which the SARB intends to purchase government bonds?

The SARB has not announced the amount of bond purchases it will undertake nor has it announced the time horizon over which it will conduct these purchases. This will be at the discretion of the SARB and dependent on market conditions.

9. What are the mechanics around the bond purchases and how will the SARB conduct these?

The SARB will be conducting the purchases on a bilateral basis, with a variety of market players. There will be no pre-announcements of dates when the purchases will be undertaken or of the sizes of intended purchases.