



South African Reserve Bank

Financial Markets Department

Record of proceedings of the Financial Markets Liaison Group meeting held via Webex on 2 June 2020

1. Overview

1.1 The Financial Markets Liaison Group (FMLG) meeting discussed the following key issues:

- The outcome of a survey commissioned by the National Treasury and the World Bank on factors that led to financial market liquidity pressures experienced in South Africa during March and April 2020;
- The systemic risk arising from COVID-19 and implications of further sovereign rating downgrades on South Africa's financial markets; and
- Progress reports from the FMLG subcommittees and the South African Foreign Exchange Committee (SAFXC).

2. Summary of discussions

2.1 **Presentation on the outcome of a survey commissioned by the National Treasury and the World Bank on factors that led to financial markets liquidity pressures experienced in South Africa during March/April 2020.**

2.1.1 The survey highlighted the main causes of liquidity pressures experienced in South Africa's financial markets during March 2020, the subsequent market interventions implemented by the SARB, and presented some policy proposals.

2.1.2 Most respondents to the survey were of the view that the SARB interventions were effective in addressing liquidity strains in the domestic financial markets at the time.

2.2 The systemic risk arising from Covid-19 (FirstRand) and implications of a sovereign rating downgrade on domestic financial markets (ABSA).

2.2.1 South Africa's debt to GDP and debt service costs were expected to deteriorate further owing to Covid-19. This would likely worsen the medium term sovereign credit ratings outlook.

2.2.2 The deterioration in South Africa's sovereign risk, subsequent credit rating downgrades and exclusion from global indices have the following implications:

- i. South Africa is likely to attract speculative investors, resulting in increased volatility in domestic bond market flows.
- ii. Local investors may have to hold a larger proportion of government debt owing to a decline in non-resident holdings of domestic government bonds.
- iii. The banking system may weaken owing to the deterioration in sovereign risk transferred into the banking system through sovereign debt held by banks, the cost and availability of funding to the banking sector and the potential inability of the sovereign to support local banks.
- iv. A decline in the banking industry's risk capacity which may negatively weigh on the financing of product innovation to enable GDP growth.
- v. The persistent depreciation of the ZAR weighed on local banks' foreign currency risk limits relative to international banks.
- vi. An increase in the cost of cross border business.

2.2.3 Others factors that negatively impacted the banking system included;

- i. Shadow banking entities, which also contributed to the liquidity pressures experienced during the Covid-19 crisis, were not subjected to the same regulatory framework and costs as applied to banks;
- ii. Money market funds held a larger portion of their assets in bank paper and banks held a notable share of their assets in sovereign debt posing a high concentration of risk in the financial system;
- iii. The banking system may be exposed to a liquidity mismatch;
- iv. It was recommended that work needed to be done in order to enhance the banking industry's capacity to take risk and cushion the cost pressures.

2.2.4 The SARB indicated that it did not intend, at this time, to expand the list of eligible collateral accepted at the SARB refinancing operations. Market participants also need to prepare themselves for the post crisis period where the central bank would begin unwinding the interventions made during the Covid-19 crisis.

2.3 **Feedback from the Money Market Subcommittee (MMS) and Reference Rate Working Group**

2.3.1 The SARB's Technical Specification Paper on South Africa's proposed reference rates would be published before the end of June 2020 for public comments.

2.3.2 The SARB's collateral substitution, barring any hiccups experienced in testing, would go live on 8 June 2020.

2.3.3 The commencement of work on improving the liquidity in the Treasury Bill market was delayed due to Covid-19. This project would commence once the workstreams were finalised. The workstreams had been identified, and feedback

had been received on the recommendations made with respect to improving liquidity in the TB market.

- 2.3.4 The SARB would provide feedback on the survey conducted on the tri-party collateral management framework at the next MMS meeting and agree on a way forward.

2.4 **Feedback from the Fixed Income and Derivatives Subcommittee (FI&DS)**

- 2.4.1 The FI&DS discussed the financial stability risk posed by the bond futures market following its surge to approximately R240 billion. This market came under significant pressure during the Covid-19 related liquidity crisis.

2.5 **Feedback from the Bond Market Development Committee (BDMC)**

- 2.5.1 The BDMC will focus on Central Counterparty Clearing, since the Electronic Trading Platform was functional and responsibility thereof had been handed over to the Markets Committee.

2.6 **Feedback from South Africa's Foreign Exchange Committee (SAFXC)**

- 2.6.1 The SAFXC, as with its global counterparts, continued to engage the buy-side to endorse the Global FX Code.
- 2.6.2 The SAFXC would participate in the annual meeting of the Global Foreign Exchange Committee scheduled for June 2020.

Enquiries:

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Secretariat of the FMLG

Attendance of the FMLG meeting 2 June 2020

Members in attendance	
Fundi Tshazibana, (FMLG Chairperson), SARB Edwin Makgopa, (Secretariat), SARB Khethiwe Mavundla, (Secretariat), SARB Zafar Parker, SARB (SAFXC) Samantha Springfield, SARB (MMS) Mukelani Nkuna, SARB Tim Masela, SARB Garth Klintworth, ABSA Capital Deon Raju, ABSA Capital Andries du Toit, FirstRand Denvin Naidoo, (FI&DS) Clive Sindelman, Investec Lourens van Rensburg, Investec George Kerby, Nedbank James Glover, Nedbank Tshepiso Moahloli, NT Roy Havemann, NT Theo Thomas, RMB Richard de Roos, (SAFXC) Randall Habana, IBA Vikas Khandelwal, IBA Andrew Hall, Standard Bank Paul Burgoyne, Standard Bank <u>By Invitation</u> Gavin Jones, Consultant – NT	<u>Apologies from members</u> Douglas Hendry, Standard Bank Bafundi Maronoti, SARB