South African Reserve Bank

The role of the SARB in financial stability

Presentation to SCOF

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Outline

- Expanded focus of central banks
- Financial stability as an objective of central banks
- Defining financial stability
- Development of financial stability in the SARB
- Structures and functional approach
- Financial Sector Regulation Bill
- Risk assessment matrix
- Challenges

Central bank mandates

- Traditional central bank objective: price stability
- Asian crisis (1998)
  - – price stability not a sufficient condition for financial system stability
- Strong interrelationship
- Implicit central bank objective
- Global financial crisis
- Explicit objective
- Expanded mandate

Financial stability mandate

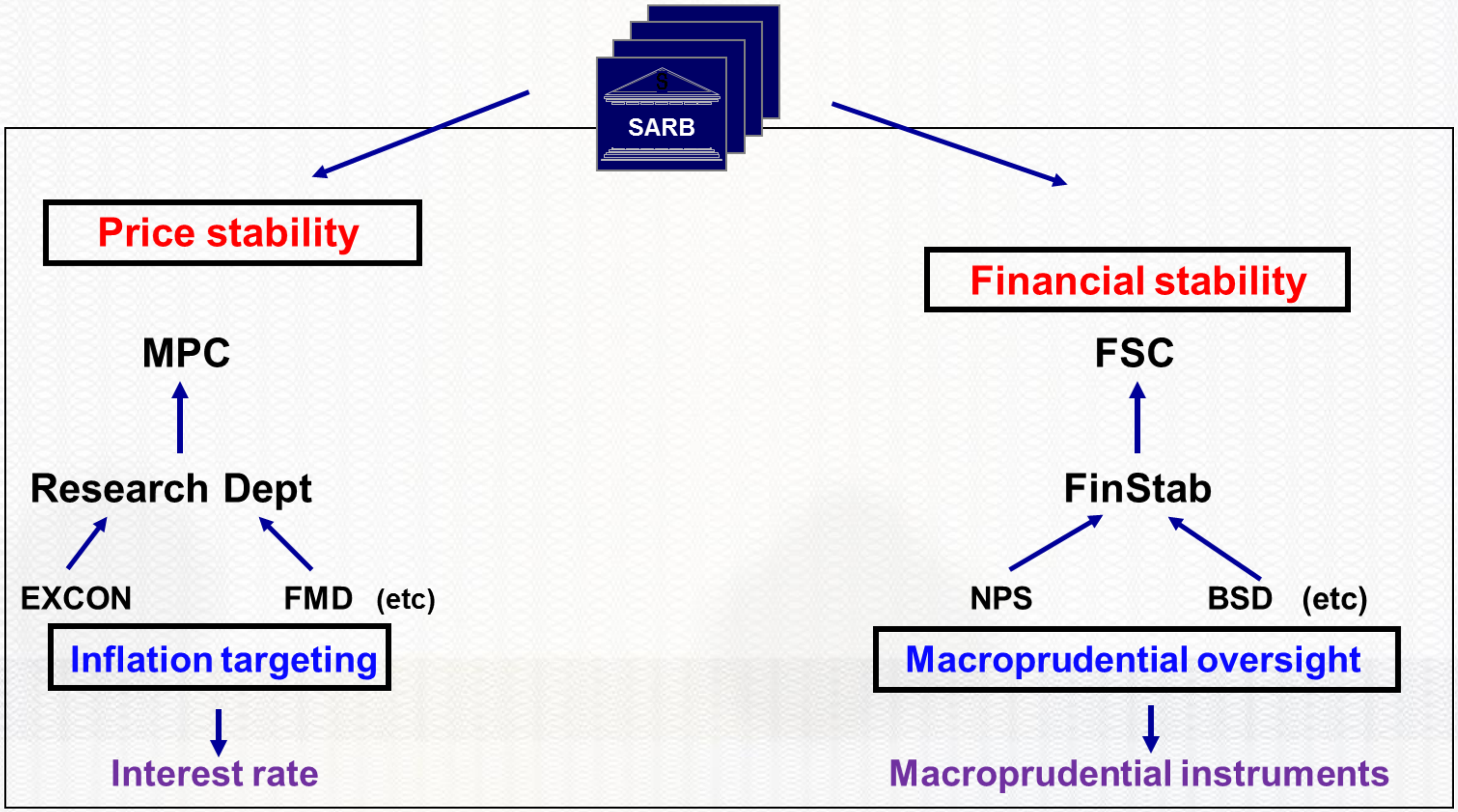
- Letter from the MoF to the Governor - "…and re-affirm the role that the Bank plays in overseeing and maintaining financial stability"
- 'A safer financial sector to serve South Africa better' (Red book) – "The Reserve Bank is best placed to play the role of a macroprudential supervisor"
- Twin peaks implementation document – "…the South African Reserve Bank is now explicitly mandated to oversee and maintain the South African financial system's stability"
- Legislation – included in the Financial Sector Regulation Act – "…protecting and enhancing financial stability"
- Shared responsibility with other stakeholders

FINANCIAL STABILITY: a possible definition…(cont)

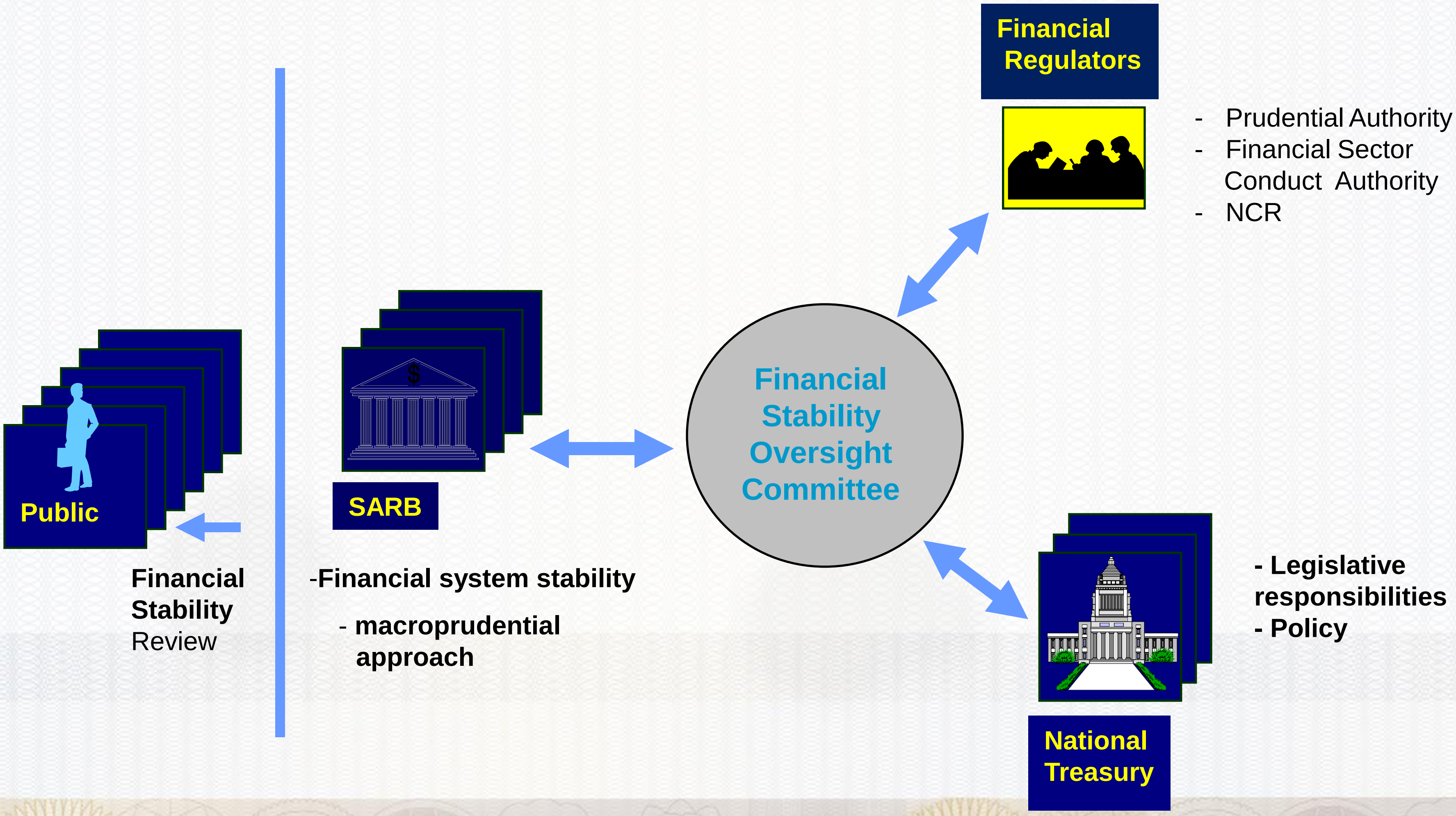
"… financial stability refers to a financial system that is resilient to systemic shocks, facilitates efficient financial intermediation and mitigates the macroeconomic costs of disruption in such a way that confidence in the system is maintained."

(SARB, Financial Stability Review)

SARB – pursuing its goals
(internal relationships)



External coordination



Financial regulatory reform

Financial Sector Regulation Act

- **Prudential Authority** (SARB)
- **Financial Sector** Conduct Authority **(FSCA)**
- Financial Stability **(SARB)**
  - **Financial Stability Committee**
  - Financial Stability Oversight Committee
  - Resolution Authority (SARB)
  - Financial Sector Contingency Forum

SARB financial stability responsibilities ito FSRB

- *"Protecting and enhancing financial stability"* (FSR Bill)
  - Monitor global and domestic environments through quantitative and qualitative indicators
  - Identify possible vulnerabilities
  - Mitigate through policy action (macroprudential policy)
    - *"…take steps to mitigate risks to financial stability…advising financial regulators of steps to take…"* (FSR Bill 12(b))
- "*Governor may declare a systemic event…*" (FSR Bill)
  - SARB to take steps to prevent, mitigate, manage … and may give directives to financial regulators to provide information…take certain actions

Financial stability functions

- Macroprudential analysis and mitigation of risks through policy actions
- Stress testing financial institutions and market infrastructures
- Assess and promote the robustness of the financial system architecture
- Monitor and coordinate systemic crisis prevention and resolution
- Research and disseminate information on financial stability issues

Risk Assessment Matrix: June 2017

Risk	Probability	Impact
Deteriorating economic, political and social conditions (weak growth, high unemployment, contingent liabilities linked to state-owned enterprises, avoidance of difficult structural reforms).	high	Further sovereign credit rating downgrades to sub-investment grade, resulting in capital outflows, higher cost of and reduced access to funding, spillovers to the banking sector (increasing impairments and reduced profitability and confidence). (high)
US policy uncertainty related to delayed implementation of policy reforms, trade protectionism, fiscal stimulus, and a possible rollback of financial regulation.	medium	Weaker confidence, a rise in foreign currency borrowing costs (if there is a policy mix of loose fiscal policy and tight monetary policy), higher funding costs (due to higher US bond yields and a stronger USD), capital outflows from emerging markets (medium)
Threats to the financial system in the UK and Europe (vulnerability of the EU banking sector, protracted Brexit process, nationalist political movements, Greece's bailout).	medium	Weaker confidence, higher financial market volatility and/or asset price losses (exchange rate, bond yields, equities), slower global and emerging market growth (due to a slowdown or reversal of fiscal and structural reform and trade from nationalist policies). (medium)
China's rising corporate and government debt could lead to a tightening in credit conditions in China which could dampen global GDP growth.	medium	Weaker sentiment, abrupt deleveraging, higher non-performing loans, slower Chinese and global GDP growth, higher volatility and asset price losses, lower commodity prices (medium)

Note: Risks are not mutually exclusive; they may interact and materialise jointly.

Challenges…

- Bank's expanded mandate
- Financial Sector Regulation Act
- Financial Stability Oversight Committee
- Toolkit of macroprudential instruments
- Coordination between macroprudential, microprudential and monetary policy
- Resolution Framework/Bill
- Deposit Insurance Scheme
- Develop stress testing capacity

The end