Statements regarding monetary policy

Issued by the South African Reserve Bank

25 March 1980

In my Chairman's Address delivered before the Annual General Meeting of the Reserve Bank on 21 August 1979, I indicated that the Reserve Bank is of opinion that the ceiling method of credit control should be abolished as soon as possible, but that it should be replaced by an indirect method which would yield better results than obtained in the past by directives relating to liquid assets. In pursuance of this line of thought, the Bank has now, after the usual consultation with the Minister of Finance, decided to take certain steps which are aimed at placing more emphasis on cash reserve requirements and supporting open market operations as instruments of credit control in future, with a view to abolishing in due course the direct method of control whereby quantitative limits are placed on the banking institutions' credit extension to the private sector.

In the gradual change-over to the new method of credit control, account will, of course, have to be taken of the underlying economic conditions and the general objectives of the current economic policy. The total quantity of money and near-money increased by the unacceptably high annual rate of 30 per cent during the latter two quarters of last year, while a large amount of surplus liquidity accumulated in both the banking and the private non-banking sectors. Three of the major factors which contribute to changes in the quantity of money, exercised an expansionary effect towards the end of 1979. The balance of payments as a whole showed a surplus, the banks' credit extension to the private sector increased and the banking sector's net claims on the government sector rose. At the same time, the private sector's long-term deposits with the banking sector, which had increased sharply during the first half of 1979 and thus had a negative impact on the quantity of money, rose at a much slower tempo.

In the light of these developments and the high rate of inflation, it will be necessary to ensure that the quantity of money and near-money does not continue to increase excessively. However, it would be consonant with the general economic policy of encouraging a higher economic growth rate, that the banks' credit extension to the private sector should not be restricted too much at present. Taking into account the favourable balance of payments position, it is therefore of particular importance how the Government will finance its expenditure in the coming year. Furthermore, the Reserve Bank will have to absorb a part of the surplus liquidity by means of open market operations.

Against this background the Bank has decided to effect the following adjustments to its monetary policy measures:

Liquid asset requirements

Big banks, that is banking institutions with total assets of more than R800 million, now have to invest 10 per cent of the increase in their short-term liabilities plus 4 per cent of the increase in their medium-term liabilities since 30 September 1975 as a supplementary requirement in liquid assets. This supplementary liquid asset requirement, which was already reduced in 1979 and abolished for other banks (with total assets of R800 million or less), is now also abolished for the big banks as from the date of certification of their monthly statements (B A Form No 7) for 31 March 1980.

Cash reserve requirements

All banking institutions now have to hold over and above the basic cash reserve requirement, whereby they have to keep 8 per cent of their short-term liabilities towards the public as an interest-free balance with the Reserve Bank, also a supplementary cash reserve equal to 7 per cent of their short-term liabilities with the National Finance Corporation of South Africa. In order to place more emphasis on cash reserve requirements and to utilise them more effectively as policy instrument, it has been decided to require that all banking institutions should, as from the date of certification of their monthly statements (B A Form No 7) for 31 March 1980, hold this supplementary cash reserve as an interest-free balance with the Reserve Bank, instead of with the National Finance Corporation.

The above-mentioned abolition of the supplementary liquid asset requirement in respect of the increases in the short- and medium-term liabilities of the big banks, will result in the release of a substantial amount of their liquid assets. In the light of the existing surplus liquidity in the economy and the possibility that further large accretions to liquidity may occur during the coming months, it has been decided to introduce an additional supplementary liquid asset requirement now for the big banks in the form of a cash reserve equal to 5 per cent of their outstanding medium-term liabilities to the public. Seeing that banks pay interest on all their medium-term deposits, it is deemed fair that this additional cash reserve should be held in the form of a balance with the National Finance Corporation so that it may earn the usual call deposit interest rate which the Corporation pays on deposits.

In order to carry through further the change in emphasis towards credit control by means of cash reserve requirements, it has been decided that banking institutions with total assets of R800 million or less, should in future also comply with a cash reserve requirement against their medium-term liabilities. These banks now have to invest 7 per cent of their medium-term liabilities as a supplementary requirement in liquid assets. It has been decided not to increase the total liquid asset requirements for these banks now, but to require that they should hold as from the date of certification of their monthly statements for 31 March 1980, 3 per cent of their medium-term liabilities as a supplementary cash reserve with the National Finance Corporation, and should from that date invest only 4 per cent of their medium-term liabilities as a supplementary requirement in other liquid assets.

The cash reserve and liquid asset requirements which will be applicable to the "big" and "other" banks respectively as from the date of certification of their monthly statements for 31 March 1980, are summarised in the appended table.

It must be stressed that the requirements relating to cash reserves and other liquid assets as now laid down, will be reconsidered during the coming months as the banks' new monthly statements become available and the effects of the modified requirements can be better evaluated.

Discount houses

In terms of a directive of the Reserve Bank, the discount houses may not invest more than 35 per cent of their total assets in bank acceptances and commercial bills, which qualify as liquid assets. In order to enable these institutions to channelise an increased share of their total funds to the private sector, it has been decided to allow the discount houses to invest up to a maximum of 37½ per cent of their total assets in liquid banking acceptances and commercial bills in future. This concession takes effect immediately.

Credit ceilings

The foregoing adjustments in the cash reserve and liquid asset requirements, should, together with supporting open market transactions by the Reserve Bank, make it possible to abolish the ceiling method of credit control in due course, but it would be unwise to do so now in this stage of transition.

Seeing that a number of banks are already experiencing problems with their credit ceilings, it has been decided to increase the ceilings applicable to all banking institutions' discounts, loans and advances to the private sector, and also to their investments in securities of the private sector, as from 31 March 1980 by 6 per cent of the basic figures as at 31 December 1975. This increase is additional to the existing increase of ½ per cent per month of the basic figures.

Banking institutions of which the total credit extension to the private sector does not amount to more than R25 million, are exempt from the credit ceilings at present. This limit is raised to R30 million as from 31 March 1980.

Liquid asset requirements for banking institutions as from date of certification of monthly return (B.A. Form No. 7) for March 1980

A. Banks with total assets of more than R800 million

Requirements	Liabilities to the public[1]			
	Short-term	Medium-term	Long-term	Liabilities under acceptances
	%	%	%	%
Basic:				
Reserve balances with South African Reserve Bank	8	—	—	—
Other	22	20	5	10
Supplementary:				
Reserve balances with South African Reserve Bank	7	—	—	—
Reserve balances with National Finance Corporation	—	5	—	—
Other	18	10	—	—
Total	**55**	**35**	**5**	**10**

B. Banks with total assets of R800 million or less

Requirements	Liabilities to the public[1]			
	Short-term	Medium-term	Long-term	Liabilities under acceptances
	%	%	%	%
Basic:				
Reserve balances with South African Reserve Bank	8	—	—	—
Other	22	20	5	10
Supplementary:				
Reserve balances with South African Reserve Bank	7	—	—	—
Reserve balances with National Finance Corporation	—	3	—	—
Other	13	4	—	—
Total	**50**	**27**	**5**	**10**

1. As reduced for purposes of the liquid asset requirements, where applicable.

Deposit rate control

Under the special powers which are conferred on the Reserve Bank in terms of the Currency and Exchanges Act (Act No 9 of 1933), maximum interest rates are at present prescribed which banking institutions and building societies may pay on deposits of the public. These maximum limits are now appreciably higher in general than the rates which are paid in practice on deposits, and in view thereof it has been decided to withdraw the existing directives in this regard immediately.

Open market operations

The Reserve Bank has been particularly active during the past few years in buying and selling assets in order to influence liquidity conditions in the money market and in the private non-banking sector. The effective control of credit extension by banking institutions by means of cash reserve requirements depends a great deal on an effective open market operations policy by the Reserve Bank, inclusive of its discount policy, and on firm discipline in the handling of government finance.

The Bank realises that considerable deficiencies still exist in the money and capital markets in South Africa which impair its ability to carry out open market operations effectively. At present the Bank is, for example, experiencing a serious shortage of the necessary assets which it could utilise for this purpose because its portfolio of government stock has already been fully sold during the past year. The Bank proposes, however, to start issuing special Reserve Bank debentures soon which are intended exclusively for open market operations. These debentures, which could be issued in various maturities, will qualify as liquid assets if they have an outstanding period to maturity of less than three years. The debentures will be issued at market rates, and will be transferable and negotiable. Application will also be made to the Johannesburg Stock Exchange for the listing of the debentures.

The Bank will further, as in the past, continue to sell and buy government stock and Treasury bills.

18 April 1980

The margin between short-term interest rates in South Africa and comparable interest rates abroad is at present so large that the switching of financing of South Africa's foreign trade from foreign to domestic sources increased to such an extent that the domestic money market tightened considerably. In order to avoid that this tendency continues unabatedly, the Reserve Bank finds it necessary to increase as from today its discount for dollar forward exchange transactions with a maximum maturity of one year from 2½ per cent to 12 per cent per annum. This credit for long periods to buyers of South African products, while at the same time importers should more readily make use of off-shore financing. This rate for dollar forward exchange cover will be adjusted from time to time in accordance with changes in interest rates and other economic conditions.