

Money supply targets for 1986

Statement by Dr. Gerhard de Kock, Governor of the South African Reserve Bank

17 March 1986

In his Budget Speech today the Minister of Finance, Mr. B.J. du Plessis, announced that the Government has accepted the recommendation of the Commission of Inquiry into the Monetary System and Monetary Policy that the Reserve Bank should, with the concurrence of the Minister of Finance, set specific target rates of growth for one or more of the money supply aggregates.

The main reason for introducing monetary targeting is to assist the monetary authorities in their policy of controlling the money supply with a view to curbing inflation.

The targeting arrangements proposed by the Reserve Bank and accepted by the Government for 1986 are as follows:

- Following a comprehensive new statistical analysis of the relevant data as recommended by the Commission, the Reserve Bank has redefined the monetary aggregates M1, M2 and M3 and added a new concept M1(A). The new definitions are set out in detail in an appendix to this statement. While the money supply figures in the March issue of the Reserve Bank's *Quarterly Bulletin* will still be based on the old definitions, revised time series for all the monetary aggregates according to the new definitions will be published in the June issue, together with an explanatory article. Seasonally adjusted month-end figures for all the newly defined monetary aggregates will in future be released by the Reserve Bank each month.
- The money supply aggregate to be used for targeting purposes is the newly defined M3. This comprehensive aggregate consists of all bank notes and coins in circulation plus *all* deposits (including building society "shares") of the domestic private sector with banking institutions, building societies and the Post Office Savings Bank.
- The target for 1986 is set in the form of a tolerance range for the rate of increase in M3 of between 16 and 20 per cent between the fourth quarter of 1985 and the fourth quarter of 1986. Since the average amount of M3 during the fourth quarter of 1985 was R71,2 billion, according to the new definition, the lower limit set for the average M3 during the fourth quarter of 1986 is R82,6 billion and the upper limit R85,4 billion.
- In the prevailing circumstances, and taking into account the sharp decline during the course of 1985 in the rates of increase of all the monetary aggregates, the fourth quarter of 1985 may be judged to form a relatively low base from which to start a monetary targeting exercise. It is therefore relevant in the present case also to compare the target range for the fourth quarter of 1986 with the average of M3 during the fourth quarter of 1984. On this basis the target range set for the fourth quarter of 1986 provides for a growth rate for M3 of 14 to 16 per cent per year over this two-year period.
- In the accompanying table and graph, the target range for M3 is translated into seasonally adjusted upper and lower limits for each month-end during the targeting period in two forms - a "cone" and a "tunnel". This is in accordance with the practice employed in a number of other countries.

The adoption of a target for M3 naturally implies that interest and exchange rates must be reasonably flexible and able to adjust to changing circumstances. Interest rates and exchange rates cannot be determined independently of the money supply or of each other. If, therefore, the demand for credit were to rise strongly as the present economic upswing gains momentum, a rise in interest rates might well form an essential part of any package of monetary measures applied to prevent the money supply from "overshooting" the target. On the other hand, as the experience of the past ten months has shown, declining interest rates can be fully reconcilable with effective money supply control during periods of low aggregate demand.

Broad money supply M3 (new definition)

Target ranges for growth during 1986 (fourth quarter 1985 to fourth quarter 1986)

Upper and lower limits for M3 (seasonally adjusted), R millions

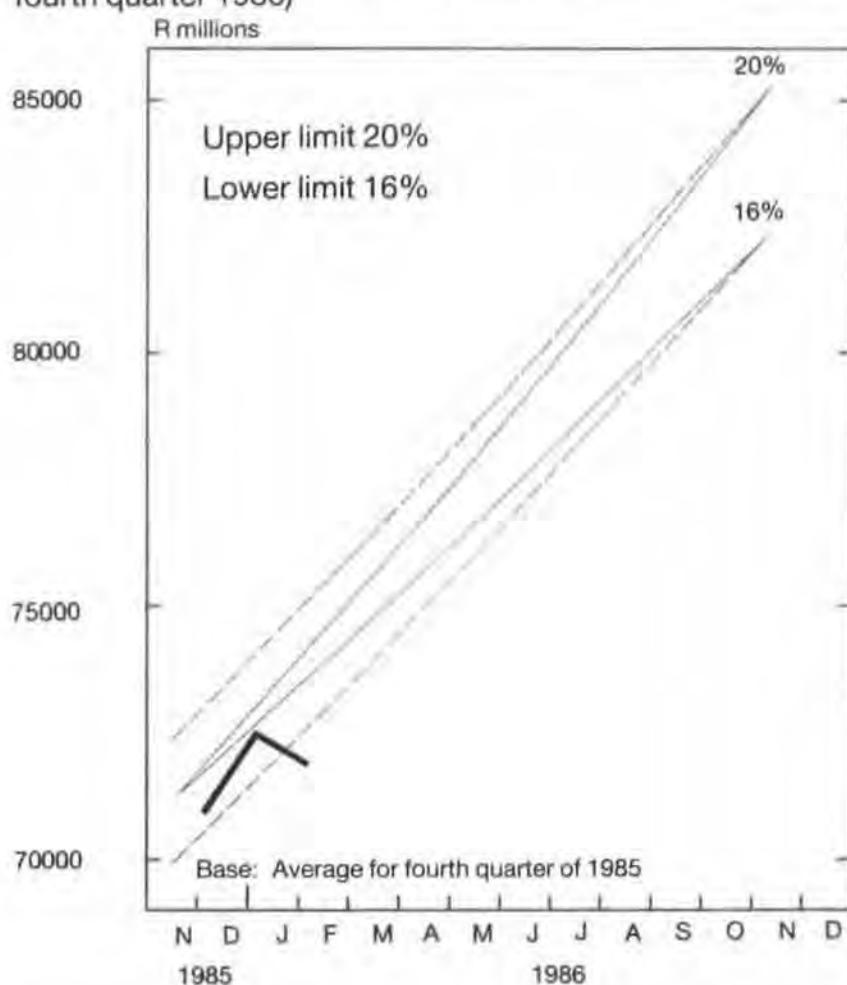
	Cone	Tunnel			
		Upper limit 20%	Lower limit 16%	Upper limit	Lower limit
1985: Average					
4th qr	71 174	71 174	72 380	69 968	
End of Nov	71 717	71 615	72 878	70 456	
Dec	72 815	72 507	73 890	71 434	
1986: End of Jan	73 930	73 409	74 916	72 426	
Feb	75 062	74 323	75 956	73 431	
Mar	76 211	75 248	77 012	74 452	
Apr	77 378	76 184	78 082	75 486	
May	78 562	77 132	79 196	76 534	
June	79 765	78 092	80 265	77 597	
July	80 986	79 064	81 380	78 676	
Aug	82 226	80 048	82 510	79 768	
Sept	83 485	81 044	83 656	80 875	
Oct	84 763	82 053	84 819	81 999	
Average					
4th qr	85 409	82 562	85 409	82 562	
End of Nov	86 061	83 074	85 997	83 138	
Dec	87 379	84 108	87 191	84 293	

R millions

$$\begin{array}{rcl} 1985 \text{ IV} & + & 20\% = 85 409 \\ & + & 16\% = 82 562 \end{array}$$

Broad money supply M3 (New definition)

Target ranges for growth during 1986 (fourth quarter 1985 to fourth quarter 1986)



As recommended by the Commission, the targeting exercise now being embarked upon will be applied with a fair measure of flexibility and a "low profile". What this means is that there will be no *rigid* and *overriding* "money rule" that implies leaving interest rates and exchange rates *completely* free to find their own levels at all times. Instead, the monetary authorities will continue to exercise discretionary judgment in deciding what combination of money supply, interest rates and exchange rates to aim at in any given set of circumstances. But this discretion will naturally be constrained by the need to avoid changing or breaching the M3 target so often that it loses its meaning.

It must also be emphasised from the outset that in framing and applying monetary policy the monetary authorities will not be influenced unduly by individual month-end figures. This is not only because month-end money supply statistics are notoriously volatile for technical reasons, but also because of the non-rigid approach being adopted to the targeting exercise in general. On the basis of past experience it is highly likely that individual month-end M3 figures will from time to time fall outside the limits set by the "cone" and the "tunnel". When this happens, the Reserve Bank will not necessarily feel constrained to tighten or ease its policy stance immediately. But, of course, if the monthly M3 figures *consistently* fall outside the target range, policy adjustments will have to be considered and/or the target range itself will have to be reviewed and possibly modified.

In accordance with the Commission's recommendations the main instruments of monetary policy to be used in order to maintain M3 growth within the target limits will be public debt management (including public borrowing policy), open-market operations, discount policy and Reserve Bank "intervention" in the foreign exchange market. Use of these market-oriented policy instruments may at times be supplemented by variations of the cash reserve requirements for banks and building societies.

As in many other countries, the rationale for introducing monetary targeting in South Africa is basically three-fold:

- It will make clear that the monetary authorities are determined to get to grips with what they themselves have consistently identified as a vital element in the process of inflation, namely an excessive rate of increase of the money supply.
- It will provide advance notification of the likely stance of monetary policy. This greater predictability should assist private sector enterprises in reaching business decisions and also be helpful to workers and employers in the formulation and negotiation of wage demands.
- It will provide a yardstick against which the actual performance of monetary policy may be judged.

From the point of view of curbing inflation, a lower target range for the rate of increase in M3 in 1986 than 16 to 20 per cent would obviously have been preferable. But apart from the problem of a relatively low base period already mentioned, the targeting exercise is being introduced under conditions of low growth and high inflation, and in the short term a balance has to be maintained between facilitating growth and curbing inflation.

In these circumstances a target range of between 16 and 20 per cent was chosen for 1986 because it meets two conditions: Firstly, it is high enough to accommodate a projected increase in real gross domestic product of more than 4 per cent between the fourth quarter of 1985 and the fourth quarter of 1986, which translates into an increase of about 3 per cent between calendar 1985 and calendar 1986. Secondly, it is low enough to ensure that the expected decline in the rate of inflation during the course of 1986 as a result of the recent appreciation of the exchange rate will not be aborted by the emergence of new demand inflationary pressure.

In other words, it is believed that attainment of the 16 to 20 per cent M3 target would be consistent with the simultaneous

achievement of a substantially higher real growth rate in 1986 than in 1985 and a marked decline in the rate of inflation during the course of 1986. If meaningful progress is made towards the latter end, the way will have been paved for the setting of a lower target range for M3 in 1987, as a prelude to a further reduction in the inflation rate.

APPENDIX

Definitions of monetary aggregates¹⁾

Monetary aggregate	Existing definition	New definition
M1(A)	-	Coin and banknotes in circulation, and cheque and transmission deposits with banking institutions ²⁾ , building societies and the Post Office Savings Bank
M1	Coin and banknotes in circulation, and demand deposits with monetary banking institutions. ³⁾	M1(A) <i>Plus:</i> Other demand deposits with banking institutions ²⁾
M2	M1 <i>Plus:</i> Other short-term deposits, and all medium-term deposits (including savings deposits) with monetary banking institutions ³⁾	M1 <i>Plus:</i> Other short-term deposits, and all medium-term deposits (including savings deposits) with banking institutions. ²⁾ <i>Plus:</i> Other short-term deposits, and all medium-term deposits (including savings deposits and certain "share" investments) with building societies. <i>Plus:</i> Savings deposits with and savings bank certificates of the Post Office Savings Bank.
M3	M2 <i>Plus:</i> All long-term deposits with monetary banking institutions. ³⁾	M2 <i>Plus:</i> All long-term deposits with banking institutions. ²⁾ <i>Plus:</i> All long-term deposits and other "share" investments with building societies. <i>Plus:</i> Investments in national savings certificates issued by the Post Office Savings Bank

1) Deposits included in these aggregates are those of the domestic private sector with the institutions concerned. Foreign deposits, government deposits and deposits of the institutions concerned with each other are excluded.

2) The South African Reserve Bank, the Corporation for Public Deposits, discount houses, all other registered banking institutions and the short-term business of the Land Bank.

3) The South African Reserve Bank, the commercial banks, merchant banks, the former National Finance Corporation, Corporation for Public Deposits, discount houses, the short-term business of the Land Bank, and other banking institutions of which the monthly average amount of demand deposit liabilities during the preceding calendar year amounted to at least R5 000 000 and of which the monthly average amount of short and medium-term deposit liabilities during the preceding calendar year collectively amounted to at least one-third of the total deposit liabilities of such an institution or at least R30 000 000.

Geldvoorraadmikpunte vir 1986

Verklaring deur dr. Gerhard de Kock, President van die Suid-Afrikaanse Reserwebank

17 Maart 1986

In sy Begrotingsrede vandag het die Minister van Finansies, mnr. B.J. du Plessis, die Regering se aanvaarding aangekondig van die aanbeveling van die Kommissie van Ondersoek na die Monetêre Stelsel en Monetêre Beleid dat die Reserwebank, met die instemming van die Minister van Finansies, spesifieke mikpuntgroeikoerse vir een of meer van die geldvoorraadtale moet stel.

Die belangrikste rede vir die instelling van monetêre mikpunte is om die monetêre owerhede by te staan in hul beleid om die geldvoorraad te beheer ten einde inflasie aan bande te lê.

Die mikpuntreeëlings wat vir 1986 deur die Reserwebank voorgestel en deur die Regering aanvaar is, is soos volg:

- Nà 'n omvattende nuwe statistiese ontleding van die betrokke gegewens, soos wat deur die Kommissie aanbeveel is, het die Reserwebank nuwe definisies vir die geldvoorraadtale M1, M2 en M3 opgestel en 'n nuwe begrip, M1(A), hieraan toegevoeg. Die nuwe definisies word in besonderhede in 'n bylaag tot hierdie verklaring uiteengesit. Terwyl die geldvoorraadsyfers in die Maart-uitgawe van die Reserwebank se *Kwartaalblad* nog op die ou definisies gegrond sal wees, sal hersiene tydreekse vir al die monetêre totale ooreenkomsdig die nuwe definisies, saam met 'n verduidelikende artikel, in die Junie-uitgawe gepubliseer word. Seisoensaangesuiwerde maandeind-syfers vir al die nuutgedefinieerde monetêre totale sal in die toekoms elke maand deur die Reserwebank vrygestel word.
- Die geldvoorraadtotaal wat vir mikpuntdoeleindes gebruik gaan word, is die nuut-gedefinieerde M3. Hierdie breë totaal bestaan uit alle banknote en munte in omloop plus *alle* deposito's (met inbegrip van bouvereniging-"*aandele*") van die binnelandse private sektor by bankinstellings, bouverenigings en die Posspaarbank.
- Die mikpunt vir 1986 word gestel in die vorm van 'n toelaatbare speelruimte vir die groeikoers in M3 van tussen 16 en 20 persent tussen die vierde kwartaal van 1985 en die vierde kwartaal van 1986. Omdat die gemiddelde bedrag van M3 gedurende die vierde kwartaal van 1985 volgens die nuwe definisie R71,2 miljard beloop het, is die onderste perk wat vir die gemiddelde van M3 gedurende die vierde kwartaal van 1986 vasgestel is, R82,6 miljard en die boonste perk R85,4 miljard.
- Onder die heersende omstandighede, en met inagneming van die skerp daling in die koers van toename in al die monetêre totale in die loop van 1985, kan die vierde kwartaal van 1985 beskou word as 'n betreklik lae basis om as die beginpunt vir 'n monetêre-mikpuntoefening te dien. Gevolglik is dit in hierdie geval ter sake om die mikpuntgrense vir die vierde kwartaal van 1986 ook met die gemiddelde van M3 gedurende die vierde kwartaal van 1984 te vergelyk. Op hierdie basis maak die mikpuntgrense wat vir die vierde kwartaal van 1986 gestel word, voorsiening vir 'n groeikoers vir M3 van 14 tot 16 persent *per jaar* oor hierdie tweejaartydperk.
- In die bygaande tabel en grafiek word die mikpuntgrense vir M3 op twee maniere na seisoensaangesuiwerde boonste en onderste perke vir elke maandeinde gedurende die mikpunttydperk omgerekken – 'n "kegel" en 'n "tonnel". Dit is in ooreenstemming met die praktyk wat in 'n aantal ander lande gevolg word.

Die aanvaarding van 'n mikpunt vir M3 beteken natuurlik dat rentekoerse en wisselkoerse betreklik buigsaam moet wees en in staat moet wees om by veranderende omstandighede aan te pas. Rentekoerse en wisselkoerse kan nie onafhanklik van die geldvoorraad, of van mekaar, bepaal word nie. Indien die vraag na krediet dus skerp sou styg narnate die huidige ekonomiese opswaai stukrag opbou, is dit goed moontlik dat 'n styging in rentekoerse 'n belangrike deel sal uitmaak van enige pakket van monetêre maatreëls wat toegepas sou kon word om te voorkom dat die geldvoorraad by die mikpunt "verbyskiet". Hierteenoor kan dalende rentekoerse, soos die ondervinding die afgelope tien maande geleer het, ten volle versoenbaar wees met effektiewe beheer oor die geldvoorraad gedurende tydperke waarin die totale vraag swak is.

Breë geldvoorraad M3 (nuwe definisie)

Mikpuntgrense vir groei gedurende 1986 (vierde kwartaal 1985 tot vierde kwartaal 1986)

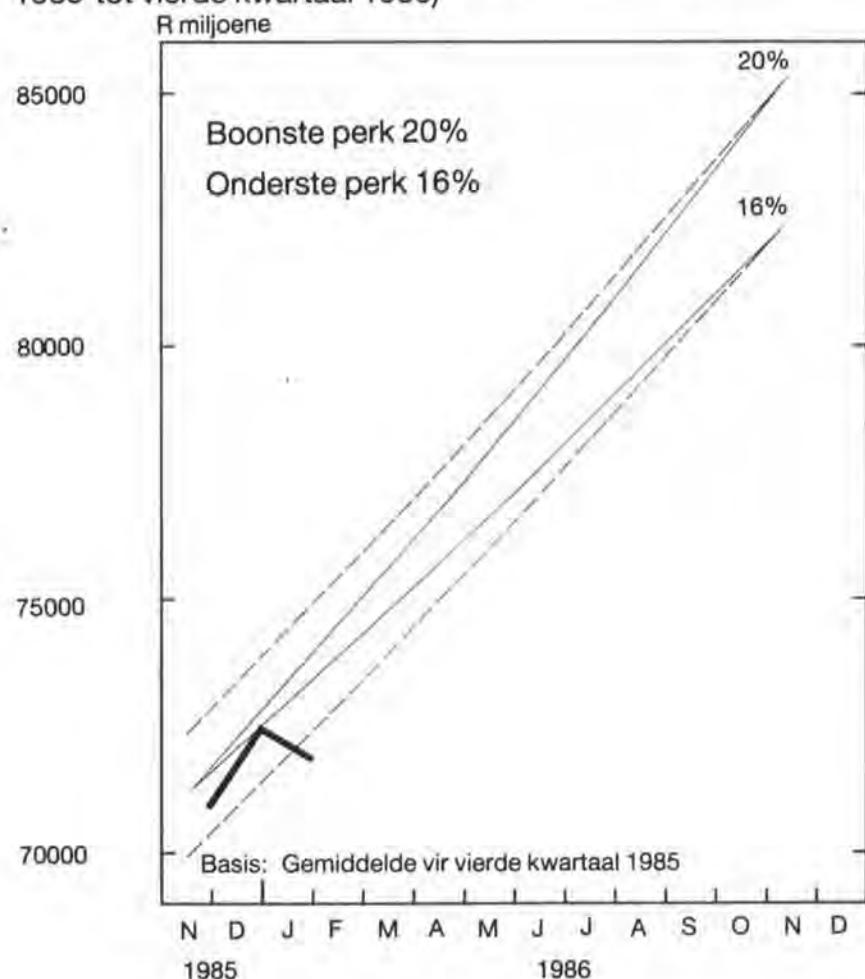
Boonste en onderste perke vir M3 (na seisoensaansuiwering), Rm

			Kegel		Tonnel	
			Boonste perk 20%	Onderste perk 16%	Boonste perk	Onderste perk
1985:	Gemiddeld					
	4de kw	71 174	71 174	72 380	69 968	
Einde	Nov	71 717	71 615	72 878	70 456	
	Des	72 815	72 507	73 890	71 434	
1986:	Einde	Jan	73 930	73 409	74 916	72 426
	Feb	75 062	74 323	75 956	73 431	
	Mrt	76 211	75 248	77 012	74 452	
	Apr	77 378	76 184	78 082	75 486	
	Mei	78 562	77 132	79 196	76 534	
	Jun	79 765	78 092	80 265	77 597	
	Jul	80 986	79 064	81 380	78 676	
	Aug	82 226	80 048	82 510	79 768	
	Sept	83 485	81 044	83 656	80 875	
	Okt	84 763	82 053	84 819	81 999	
	Gemiddeld					
	4de kw	85 409	82 562	85 409	82 562	
Einde	Nov	86 061	83 074	85 997	83 138	
	Des	87 379	84 108	87 191	84 293	

$$\begin{array}{rcccl} & & & \text{R miljoene} \\ 1985 \text{ IV} & + & 20\% & = & 85 409 \\ & + & 16\% & = & 82 562 \end{array}$$

Breë geldvoorraad M3 (Nuwe definisie)

Mikpuntgrense vir groei gedurende 1986 (vierde kwartaal 1985 tot vierde kwartaal 1986)



Soos deur die Kommissie aanbeveel is, sal die mikpuntoefening waarmee nou 'n begin gemaak word, met 'n redelike mate van buigsaamheid en 'n "lae profiel" uitgevoer word. Dit beteken dat daar geen *stram* en *oorheersende "geldreeël"* gaan wees waarvolgens rentekoerse en wisselkoerse *heettemal* vrygelaat word om te alle tye hul eie vlakte te vind nie. In plaas daarvan sal die monetêre owerhede voortgaan om hul diskresionêre oordeel uit te oefen wanneer hulle besluit na watter kombinasie van geldvoorraad, rentekoerse en wisselkoerse daar in enige gegewe stel omstandighede gestreef behoort te word. Hierdie diskresie sal natuurlik egter beperk word deur die noodsaak om te vermy dat die mikpunt vir M3 so dikwels verander of verbreek word dat dit geen betekenis meer het nie.

Dit moet ook vanuit die staanspoor beklemtoon word dat die monetêre owerhede by die formulering en toepassing van hul monetêre beleid nie oormatig deur maandeindsyfers beïnvloed sal word nie. Dit is so nie slegs omdat die geldvoorraadstatistiek soos op maandeindes om tegniese redes berugte wisselvaligheid toon nie, maar ook vanweë die buigsame benadering wat ten opsigte van die mikpuntoefening in die algemeen gevolg sal word. In die lig van vorige ondervinding is dit baie waarskynlik dat individuele syfers vir M3 soos op maandeindes van tyd tot tyd buite die perke sal val wat deur die "kegel" en die "tonnel" gestel word. Wanneer dit gebeur, sal die Reserwebank nie noodwendig verplig voel om sy beleid onmiddellik te verruim of te vernou nie. Maar as die maandelikse M3-syfers *aanhouwend* buite die mikpuntgrense val, sal beleidsaanpassings natuurlik oorweeg moet word en/of sal die mikpuntgrense self in hersiening geneem en moontlik gewysig moet word.

In ooreenstemming met die Kommissie se aanbevelings sal die belangrikste monetêre-beleidsinstrumente wat gebruik gaan word om die groei van M3 binne die mikpuntperke te hou, bestaan uit openbare-skuldbeheer (met inbegrip van die leningsbeleid van die openbare sektor), opemarktransaksies, herdiskonteringsbeleid en "intervensie" deur die Reserwebank in die buitelandsevalutemark. Die gebruik van hierdie markgerigte beleidsinstrumente mag by tye aangevul word deur wysigings van die kontantreserwevereistes vir banke en bouverenigings.

Soos in baie ander lande is die onderliggende redes vir die instelling van monetêre mikpunte in Suid-Afrika basies van drieërlei aard:

- Dit sal duidelik maak dat die monetêre owerhede vasbeslote is om 'n houvas te verkry op wat hulself konsekwent as 'n kernelement in die inflasieproses aangedui het, naamlik 'n oormatige koers van toename in die geldvoorraad.
- Dit sal dien as vooraf-kennisgewing van die waarskynlike ingesteldheid van monetêre beleid. Sodanige groter voorstelbaarheid behoort ondernemings in die private sektor te help om hul sakebesluite te neem en behoort ook vir werknemers en werkgewers van hulp te wees by die formulering van, en onderhandelings oor, looneise.
- Dit sal 'n maatstaf voorsien waarteen die werklike resultate van die monetêre beleid beoordeel kan word.

Vanuit die oogpunt van die beteueling van inflasie sou laer mikpuntgrense as 16 en 20 persent vir die groeikoers in M3 in 1986 vanselfsprekend verkieslik gewees het. Maar afgesien van die probleem van 'n relatief lae basistydperk waarna reeds verwys is, word daar onder toestande van lae groei en hoë inflasie met die mikpuntoefening begin, en op die kort termyn moet daar tussen die aanmoediging van groei en die beteueling van inflasie 'n sekere ewewig gehandhaaf word.

Onder hierdie omstandighede is daar vir 1986 mikpuntgrense van 16 en 20 persent gekies omdat dit aan twee vereistes voldoen: Eerstens is dit hoog genoeg om voldoende ruimte te laat vir 'n beraamde toename in die reële bruto binnelandse produk van meer as 4 persent tussen die vierde kwartaal van 1985 en die vierde kwartaal van 1986, wat na 'n toename van ongeveer 3 persent tussen die kalenderjaar 1985 en die kalenderjaar 1986 omgereken kan word. Tweedens is dit laag genoeg om te verseker dat die verwagte daling in die inflasiekoers in die loop van 1986 as gevolg van die onlangse appresiasie van die wisselkoers, nie as gevolg van die verskyning van nuwe vraaginflasiedruk op niks sal uitloop nie.

Daar word met ander woorde geglo dat bereiking van die groeimikpunt vir M3 van 16 tot 20 persent verenigbaar sou wees met die gelyktydige bewerkstelliging van 'n aansienlike hoë reële groeikoers in 1986 as in 1985 en van 'n aanmerklike daling in die inflasiekoers in die loop van 1986. Indien daar wel betekenisvolle vordering na laasgenoemde doel gemaak word, sal die pad ooggemaak wees om in 1987 laer mikpuntgrense vir M3 te stel, as voorspel tot 'n verdere verlaging van die inflasiekoers.

BYLAAG

Definisies van monetêre totale¹⁾

Mone-têre totaal	Huidige definisie	Nuwe definisie
M1(A)	-	Munte en banknote in omloop, en tjek- en transmissiedeposito's by bankinstellings, ²⁾ bouverenigings en die Posspaarbank.
M1	Munte en banknote in omloop en onmiddellik opeisbare deposito's by monetêre bankinstellings. ³⁾	M1(A) <i>Plus:</i> Ander onmiddellik opeisbare deposito's by bankinstellings. ²⁾
M2	M1 <i>Plus:</i> Ander korttermyndeposito's, en alle middeltermyndeposito's (met inbegrip van spaardeposito's) by monetêre bankinstellings ³⁾	M1 <i>Plus:</i> Ander korttermyndeposito's, en alle middeltermyndeposito's (met inbegrip van spaardeposito's) by bankinstellings. ²⁾ <i>Plus:</i> Ander korttermyndeposito's, en alle middeltermyndeposito's (met inbegrip van spaardeposito's en sekere "aandele"-beleggings). <i>Plus:</i> Spaardeposito's by en spaarbanksertifikate van die Posspaarbank.
M3	M2 <i>Plus:</i> Langtermyndeposito's by monetêre bankinstellings ³⁾	M2 <i>Plus:</i> Alle langtermyndeposito's by bankinstellings ²⁾ <i>Plus:</i> Alle langtermyndeposito's en ander "aandele"-beleggings by bouverenigings. <i>Plus:</i> Beleggings in nasionale spaarsertifikate uitgereik deur die Posspaarbank.

1) Die deposito's by hierdie totale ingesluit, is dié van die binnelandse private sektor by die betrokke instellings. Buitelandse deposito's, regeringsdeposito's en deposito's van die betrokke instellings by mekaar is uitgesluit.

2) Die Suid-Afrikaanse Reserwebank, die Korporasie vir Openbare Deposito's, diskontohuise, alle ander geregistreerde bankinstellings en die korttermynbesigheid van die Landbank.

3) Die Suid-Afrikaanse Reserwebank, handelsbanke, aksepbanke, die voormalige Nasionale Finansiëlekorporasie, Korporasie vir Openbare Deposito's, diskontohuise en die korttermynbesigheid van die Landbank, en ander bankinstellings waarvan die maandelikse gemiddelde bedrag aan onmiddellik opeisbare depositoverpligtigs gedurende die voorafgaande kalenderjaar minstens R5 000 000 bedra het en waarvan die maandelikse gemiddelde bedrag aan kort- en middeltermyndepositoverpligtigs gedurende die voorafgaande kalenderjaar gesamentlik of minstens een derde van so 'n instelling se totale depositoverpligtigs of minstens R30 000 000 bedra het.