Statement on the Bank Rate

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Most of the financial aggregates used by the Reserve Bank as a basis for monetary policy decisions have moved in the right direction recently to justify a reduction in the Bank rate. In some instances, for example in the case of the money supply, the level of the rate of increase still exceeds what is regarded as prudent for sustainable financial stability, but recent declines in this level are nevertheless encouraging.

The **M3** money supply increased by 13,9 per cent over the twelve months up to August 1997, down from the 15,9 per cent registered in April this year, but still well outside of the Reserve Bank's guideline of an increase of 10 per cent for the current calendar year. However, in the recent past, more specifically from June to August 1997, the seasonally adjusted annualised rate of increase in **M3** was only 11,4 per cent.

The rate of increase in the amount of credit extended to the private sector measured over a period of twelve months likewise declined from 17,4 per cent in April 1997 to 14,6 per cent in August 1997. Over the three months' period from June to August 1997, the seasonally adjusted annualised rate of growth in the total amount of bank credit extended to the private sector indeed declined to the low level of 5,9 per cent.

The Reserve Bank is also encouraged by the turnaround since earlier this year in the rising trend in both consumer and producer price inflation. In the case of consumer prices, the rate of increase in the overall index peaked at 9,9 per cent in April, before declining to 8,7 per cent in August 1997. The rate of change in the production price index declined from 9,6 per cent in March 1997 to 5,9 per cent in August.

After the depreciation of 21,9 per cent last year, the exchange rate of the rand has stabilised again. On 16 October 1997, the effective nominal exchange rate of the rand was about 2½ per cent above its level of 31 December 1996. The total gross gold and foreign exchange reserves of the Reserve Bank also increased from R10,3 billion at the end of last year, to R26,5 billion at the end of last month.

South Africa has now successfully weathered the storms of last year in the foreign exchange market and has, to an important extent, succeeded in preventing an escalation in the adverse effects of the depreciation on domestic financial conditions. There are, nevertheless, good reasons for a cautious approach to the relaxation of monetary policy, particularly if account is taken of the continuing nervousness in the foreign currency markets of a number of East Asian countries. In many of these countries, problems were created by a prolonged period of excessive money and credit growth and unsustainable levels of interest and exchange rates.

Taking account of all these financial developments, the Reserve Bank is satisfied that a reduction of one percentage point in the Bank's lending rates to banking institutions can now be justified. As from Monday, 20 October 1997, the Bank rate will therefore be reduced from 17 to 16 per cent per annum. All related interest rates of the Reserve Bank will likewise be reduced by one percentage point.

Most of the more flexible market interest rates, such as the Treasury bill tender rate, rates on bankers' acceptances and negotiable certificates of deposit, and the yield on long-term Government bonds, have already discounted a decline of at least one percentage point in the Bank rate. It can be expected that the lending rates of banking institutions will now follow the decline in the Bank rate. Banking institutions are requested, however, to remain cautious with the extension of additional credit, and to continue to support the monetary authorities in their quest for eventual financial stability.

The progress made so far in establishing greater financial stability should contribute to the overall objective of South Africa to stimulate economic development and to create more employment opportunities to the advantage of all South Africans. The maintenance of a stable overall financial environment must be acknowledged as an important precondition for sustainable economic growth at a higher level, as envisaged in the Government's **Macroeconomic Strategy for Growth, Employment and Redistribution**.