Chapter 1: Registrar of Banks' review

1.1 Introduction

Financial stability, a safe and sound banking system, and sustainable economic growth can be achieved only when the legal and regulatory framework in terms of which banks and banking groups are regulated and supervised creates an environment that promotes, among other things, sound corporate governance, effective risk management, well-functioning markets and well-informed investors.

The South African banking sector continued to be adequately capitalised at 15,6 per cent at the end of December 2013, despite the implementation of the higher capital requirements of the Basel III framework[1] from January 2013. The banking sector's common equity tier 1 (CET1) and tier 1 capital-adequacy ratios reflect that regulatory capital increased by means of a combination of share capital and reserve funds, the most loss-absorbent type of capital.

In accordance with the agreed post-financial crisis reform agenda of international standard-setting bodies such as the Group of Twenty (G-20) Forum, the Financial Stability Board (FSB) and the Basel Committee on Banking Supervision (Basel Committee), the process of strengthening the South African regulatory and supervisory framework to promote and enhance financial stability and the safety and soundness of banks and banking groups continued during 2013.

In this regard, on 1 January 2013 South Africa implemented amended Regulations relating to Banks (the Regulations) to ensure that its domestic regulatory and supervisory framework remains in line with internationally agreed regulatory and supervisory frameworks, requirements and standards. These include the Basel III framework that was originally issued during December 2010 and subsequently refined by the Basel Committee. South Africa was one of only eleven jurisdictions that published finalised Basel III regulations effective from 1 January 2013, along with Australia, Canada, China, Hong Kong SAR, India, Japan, Mexico, Saudi Arabia, Singapore and Switzerland.

This chapter describes in greater detail the key international regulatory developments in the year under review, including complementary matters related to the implementation of the Basel III framework with effect from 1 January 2013.

1. The Basel III framework essentially comprises two documents issued by the Basel Committee on 16 December 2010, namely "*Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems*" and "*Basel III: International Framework for Liquidity Risk Management, Standards and Monitoring*".

1.2 Key international developments, recommendations and focus areas

1.2.1 Introduction

In its annual reports of the past few years, the Bank Supervision Department (the Department) of the South African Reserve Bank (the Bank) focused on, among other things, the aftermath of the global financial crisis and the comprehensive regulatory reforms announced to address the causes thereof.

Essentially, the Basel III framework presents the details of global regulatory standards on banks' capital adequacy and liquidity as agreed by the Governors and Heads of Supervision, which is the oversight body of the Basel Committee, and endorsed by the G-20 Leaders. Based on the key lessons learnt from the global financial crisis, the Basel III framework sets out requirements for higher and better-quality capital, improved risk coverage, the introduction of a leverage ratio as a backstop to the risk-based requirement, measures to promote the build-up of capital that can be drawn down in periods of stress, and the introduction of two global liquidity standards, namely (i) the liquidity coverage ratio (LCR), and (ii) the net stable funding ratio (NSFR).

As a member of the Basel Committee, and in order to ensure a level playing field between South African banks and other internationally active competitive banks, the Department regards the full, timely and consistent implementation of internationally agreed frameworks, requirements and standards as critical. In order to ensure the implementation of these internationally agreed frameworks, the Department introduced substantial revisions to its processes of monitoring, evaluating and analysing banks and banking groups' capital adequacy, risk exposures, corporate governance, public disclosure and other relevant information.

During 2013 the Basel Committee issued various documents and further requirements that materially impact on the regulation and supervision of banks and banking groups on matters such as:

- a revised version of the LCR;
- principles for effective risk data aggregation and risk reporting;
- guidance to supervisors and banks for managing risks associated with the settlement of foreign-exchange (FX) transactions;
- a framework for monitoring tools for intraday liquidity management;
- a framework for margin requirements for non-centrally cleared derivatives; and
- a revised policy framework for banks' equity investments in funds.

The key matters communicated by the Basel Committee in respect of the aforesaid documents and requirements are summarised below:

1.2.2 Liquidity coverage ratio

On 7 January 2013 the Basel Committee published a revised version of its document on the LCR.[2]

2. Available at http://www.bis.org/publ/bcbs238.htm.

The LCR forms an integral part of the Basel III framework and is one of the Basel Committee's key reforms in strengthening global capital and liquidity regulations with the goal of promoting a more resilient banking sector.

The LCR promotes the short-term resilience of a bank's liquidity risk profile by ensuring that it has sufficient unencumbered high-quality liquid assets (HQLA) that can be converted into cash easily and immediately in private markets to meet its liquidity needs for a 30 calendar day liquidity stress scenario.

Implementation of the LCR will also improve the South African banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source, thus reducing the risk of spillover effects from the financial sector making their way into the real economy. The revisions to the LCR include an expansion in the range of assets eligible as HQLA and some refinements to the assumed in- and outflow rates to reflect better actual experience in times of stress. In addition, the Basel Committee has agreed on a revised timetable for the phasing in of the LCR and additional requirements to give effect to its intention for the stock of liquid assets to be used in times of stress.

1.2.3 Effective risk data aggregation and risk reporting

On 9 January 2013 the Basel Committee issued principles for effective risk data aggregation and risk reporting.[3]

3. Available at http://www.bis.org/publ/bcbs239.htm.

The global financial crisis that commenced in 2007 revealed that many banks were unable to aggregate risk exposures and identify concentrations fully, quickly and accurately. This meant that banks' ability to make timely risk decisions was seriously impaired with wide-ranging consequences both for the banks themselves and for the stability of the financial system as a whole.

The principles that were published by the Basel Committee are intended to strengthen banks' risk data aggregation capabilities and internal risk reporting practices. Implementation of the above-mentioned principles will also strengthen banks' risk management, thereby enhancing their ability to manage stress and crises.

1.2.4 Managing risks associated with the settlement of foreign-exchange transactions

On 15 February 2013 the Basel Committee issued a document that provides guidance to supervisors and banks for managing risks associated with the settlement of FX transactions.[4]

The document provides comprehensive and detailed direction on governance arrangements and the management of principal risk, replacement cost risk and all other FX settlement-related risks. In addition, the document promotes the use of payment-versus-payment (PVP) arrangements, where practicable, to reduce principal risk.

In particular, the document stipulates seven guidelines that address governance, principal risk, replacement cost risk, liquidity risk, operational risk, legal risk and capital for FX transactions. The key recommendations made in the document emphasise that a bank should:

- ensure that all FX settlement-related risks are effectively managed and that its practices are consistent with those used for managing other counterparty exposures of similar size and duration;
- reduce its principal risk as much as possible by settling FX transactions through the use of financial market infrastructures that provide PVP arrangements. Where PVP settlement is not practical, the bank should properly identify, measure, control and reduce the size and duration of its remaining principal risk;
- ensure that when analysing its capital needs, all FX settlement-related risks should be considered, including principal risk and replacement cost risk, and that sufficient capital is held against these potential exposures, as appropriate; and
- use netting and collateral arrangements to reduce its replacement cost risk and fully collateralise its mark-to-market exposure on physically settling FX swaps and forward contracts with counterparties that are financial institutions and systemically important non-financial entities.

4. Available at http://www.bis.org/publ/bcbs241.htm.

1.2.5 Monitoring tools for intraday liquidity management

On 11 April 2013 the Basel Committee, in consultation with the Committee on Payment and Settlement Systems, issued a framework on monitoring tools for intraday liquidity management.[5] The framework enables banking supervisors to better monitor a bank's management of intraday liquidity risk and its ability to meet payment and settlement obligations on a timely basis.

Management of intraday liquidity risk forms a key element of a bank's overall liquidity risk management framework. The set of seven quantitative monitoring tools prescribed in the framework complements the qualitative guidance on intraday liquidity management as set out in the Basel Committee's 2008 paper titled *Principles for Sound Liquidity Risk Management and Supervision*.

The framework covers, among other things, matters related to:

- the detailed design of the tools for monitoring a bank's intraday liquidity risk;
- stress scenarios;
- key application; and
- the reporting regime.

5. Available at http://www.bis.org/publ/bcbs248.htm.

1.2.6 Margin requirements for non-centrally cleared derivatives

On 2 September 2013 the Basel Committee and the International Organization of Securities Commissions released the final framework for margin requirements for non-centrally cleared derivatives.[6]

6. Available at http://www.bis.org/publ/bcbs261.htm.

The framework has been designed to reduce systemic risks related to over-the-counter (OTC) derivatives markets, as well as to provide firms with appropriate incentives for central clearing while managing the overall liquidity impact of the requirements.

In terms of the globally agreed final framework, all financial firms and systemically important non-financial entities that engage in non-centrally cleared derivatives will have to exchange initial and variation margins commensurate with the counterparty risks arising from such transactions.

In order to manage the liquidity impact of the margin requirements on financial market participants, the framework allows for a broad array of eligible collateral to satisfy initial margin requirements and it makes provision for the introduction of an initial margin threshold below which a firm would have the option of not collecting initial margins.

The framework also makes provision for a gradual phase-in period to provide market participants with sufficient time to adjust to the requirements. The requirement to collect and post initial margins on non-centrally cleared trades will be phased in over a four-year period, beginning in December 2015 with the largest, most active and systemically most important derivatives market participants.

1.2.7 Banks' equity investments in funds

On 13 December 2013 the Basel Committee issued a revised policy framework for banks' equity investments in funds.[7]

7. Available at http:/www.bis.org/publ/bcbs266.htm.

The revised policy framework is scheduled to take effect on 1 January 2017 and will apply to banks' equity investments in all funds that are not held for trading purposes, including hedge funds, managed funds and investment funds.

The framework will be applicable to all banks, irrespective of whether they apply the standardised approach (STA) or an internal ratings-based (IRB) approach for credit risk as set out in the Basel framework.

The revised framework includes three approaches varying in sophistication for setting capital requirements for banks' equity investments in funds. These approaches provide varying degrees of risk sensitivity and have been adopted by the Basel Committee to incentivise due diligence by banks and transparent reporting by the funds in which they invest.

The revised framework will also help address risks associated with banks' interactions with shadow-banking entities by ensuring that exposures to funds engaging in shadow-banking activities are supported by adequate capital.

1.2.8 Ongoing development of regulatory reforms

The work of the Basel Committee in respect of the implementation of some of the components of the agreed post-crisis reform agenda, which includes a range of initiatives to promote the resilience and stability of financial markets, banks and banking groups, is still continuing.

As a member of the Basel Committee, South Africa, through the Department, endorses the initiatives, strategies and new or amended requirements or standards to address comprehensively the fundamental weaknesses revealed by the global financial crisis. The Department is also actively involved in developing regulatory reforms that promote the safety and soundness of the banking system, and that continue to support long-term economic growth.

1.3 High-level overview of key banking-sector trends

1.3.1 Banking entities registered in South Africa

As at the end of December 2013, 31 banking institutions reported data to the Department (excluding three mutual banks, but including one institution conducting banking business under an exemption notice issued by the Minister of Finance in terms of the provisions of the Banks Act, 1990 (Act No. 94 of 1990) (the Banks Act), namely Ithala Limited) and 43 international banks with authorised representative offices in South Africa (refer to Table 1.1).

Table 1.1 South African banking sector: Number of entities registered or licensed

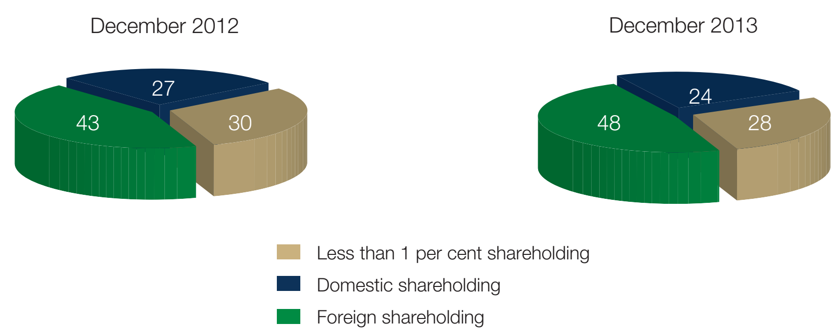
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Banks*................................	20	19	19	19	19	18	17	17	17	17
Mutual banks......................	2	2	2	2	2	2	2	2	3	3
Branches of international banks in the Republic of South Africa........................	15	15	14	14	14	13	13	12	14	14
Representative offices..........	43	47	43	46	43	42	41	43	41	43
Controlling companies.........	16	15	15	15	15	15	15	15	15	15
Banks under curatorship	0	0	0	0	0	0	0	0	0	0
Banks in receivership...........	0	0	0	0	0	0	0	0	0	0
Banks in final liquidation	2	2	2	2	2	2	2	2	2	2

* Includes active banks and banks exempted by the Registrar of Banks (with effect from 1 July 1996) in terms of the Supervision of Financial Institutions Rationalisation Act, 1996 (Act No. 32 of 1996) and section 1(cc) of the Banks Act, 1990

1.3.2 Shareholding structure

Figure 1.1 depicts the shareholding structure of South African banks. Of the nominal value of the total South African banking sector's shares in issue at the end of December 2013, foreign shareholders held 47,7 per cent, domestic shareholders 24,3 per cent and minority shareholders 28,0 per cent.

Figure 1.1 Shareholding structure of the South African banking sector (nominal value of shares) (per cent)



1.3.3 Approval of local and foreign expansions by South African banking groups

Table 1.2 presents the number of applications the Department has approved in terms of section 52 of the Banks Act since 2004. The majority of the applications received in 2013 were submitted by the five largest banking groups (refer to Appendix 8 for more information in this regard).

Table 1.2 South African banking sector: Number of approvals for local and international expansions granted in terms of section 52 of the Banks Act, 1990

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Local	16	29	16	12	15	10	16	19	12	19
Foreign*	20	17	8	25	19	26	22	27	14	21
Total	36	46	24	37	34	36	38	46	26	40

* Excludes transactions undertaken by Investec plc

1.3.4 Key banking-sector trends

Table 1.3 Selected indicators for the South African banking sector

	Dec 2012	Mar 2013	Jun 2013	Sep 2013	Dec 2013
Balance sheet					
Total assets (R billions)	3 653	3 701	3 787	3 767	3 843
Total assets: Year-on-year growth (per cent)	6,92	8,86	7,92	5,01	5,22
Gross loans and advances (R billions)	2 753	2 831	2 893	2 914	2 970
Gross loans and advances: Year-on-year growth (per cent)	9,16	10,24	10,63	8,74	7,89
Total equity (R billions)	286	295	297	290	306
Profitability					
Cost-to-income (smoothed) (per cent)	52,86	52,77	52,26	52,25	53,64
Return on equity (smoothed) (per cent)	17,74	16,87	16,64	16,42	14,74
Return on assets (smoothed) (per cent)	1,27	1,23	1,24	1,23	1,11
Capital adequacy					
Common equity tier 1 capital-adequacy ratio (per cent)		11,33	11,33	11,12	11,76
Tier 1 capital-adequacy ratio (per cent)	12,60	11,99	11,99	11,77	12,40
Capital adequacy ratio (per cent)	15,90	15,03	14,92	14,86	15,56
Credit risk					
Impaired advances (R billions)	111	113	114	108	108
Impaired advances as a percentage of total advances (per cent)	4,04	4,01	3,94	3,71	3,65
Specific credit impairments as a percentage of impaired advances (per cent)	40,25	40,67	42,09	44,58	45,74
Specific credit impairments as a percentage of gross loans and advances (per cent)	1,63	1,63	1,66	1,65	1,67

Note:

This table presents an overview of the financial and risk information, compiled by means of the aggregation of data submitted during 2012 and 2013 from individual South African-registered banks (including domestic branches of international banks but excluding offshore branches and subsidiaries of South African banks, mutual banks and cooperative banks). Information represents aggregated banks-solo information. Smoothed refers to calculations based on a 12-month moving average.

Total banking-sector assets amounted to R3 843 billion at the end of December 2013 (December 2012: R3 767 billion), representing a moderate year-on-year increase of 5,2 per cent. The four largest banks in South Africa contributed 83,4 per cent to the balance-sheet size of the total banking sector, similar to the level recorded in 2012. Gross loans and advances, which on average represented 76,6 per cent of banking-sector assets during 2013, increased almost 8 per cent to R2 970 billion at the end of December 2013, mainly due to increases in foreign currency-denominated loans, specialised lending, and lease and instalment debtors.

Home loans and term loans, accounting for 28,5 per cent and 18,2 per cent respectively of gross loans and advances, remained the single largest components of gross loans and advances at the end of December 2013. Other loans, leasing and instalment debtors, and commercial mortgages represented 17,7 per cent, 11,2 per cent and 8,8 per cent respectively of gross loans and advances.

The composition of banking-sector liabilities, which comprised predominantly deposits (on average representing 87,6 per cent of liabilities during 2013, marginally higher from the 2012 average of 85,5 per cent), remained largely unchanged when compared to 2012. In December 2013 banking-sector deposits comprised fixed and notice deposits (29,7 per cent), current accounts (20,4 per cent), call deposits (17,2 per cent), other deposits (12,4 per cent) and negotiable certificates of deposit (12 per cent).

Corporate and retail customers were the main source of banking-sector deposits throughout 2013, and on average accounted for 45,2 per cent and 22,6 per cent respectively of total deposits. On average deposits from banks represented 9,8 per cent of banking-sector deposits in 2013. Other sources of deposits included deposits from securities firms (averaging 7,3 per cent), the public sector and local authorities (averaging 6,8 per cent), and sovereigns (averaging 5,0 per cent) during 2013.

Off-balance-sheet items expressed as a percentage of total assets increased marginally from 28,8 per cent in January 2013 to 29,2 per cent in December 2013, mainly due to a 26,3 per cent year-on-year increase in guarantees issued on behalf of clients.

The banking sector continued to be adequately capitalised at 15,6 per cent at the end of December 2013, despite the implementation of the higher capital requirements of the Basel III framework from January 2013. The sector's CET1 capital-adequacy ratio was 11,8 per cent as at 31 December 2013, with common equity capital and reserves on average accounting for 75,2 per cent of total regulatory capital and reserves during 2013. The financial leverage multiple[8] of the banking sector declined marginally during 2013, amounting to 13,2 times as at 31 December 2013 compared with 13,3 times as at 31 December 2012.

Banks remained profitable during 2013. However, the banking sector's 12-month cumulative gross operating profit decreased year on year by 1,9 per cent as at 31 December 2013, mainly due to a decline in dividend income received from subsidiary companies (there was a large, once-off dividend paid by a subsidiary of a large banking group in December 2012 that did not recur in December 2013). Total banking-sector return on equity was 14,7 per cent, and the return on assets approximately 1,1 per cent as at 31 December 2013 (based on a 12-month moving average calculation). Staff expenses remained the single largest cost component and accounted for 55,8 per cent of the banking sector's total operating expenses during 2013. The 12-month moving average cost-to-income ratio of the sector deteriorated during 2013 and was 53,6 per cent as at 31 December 2013 compared to 52,9 per cent as at 31 December 2012.

Statutory liquid assets held by banks during 2013 on average exceeded those required throughout 2013. The average liquid assets held by the banking sector expressed as a percentage of liquid assets required to be held increased from 195,5 per cent at the end of December 2012 to 198,8 per cent at the end of December 2013.

Impaired advances[9] declined by 2,7 per cent year on year to R108,3 billion as at the end of December 2013. Impaired advances expressed as a percentage of gross loans and advances decreased to 3,7 per cent at the end of December 2013, a level last reported in the last quarter of 2008. Specific impairments covering impaired advances continued to increase during 2013, from 40,3 per cent in December 2012 to 45,7 per cent in December 2013.

8. The financial leverage multiple is calculated by dividing total banking-sector assets by total banking-sector equity attributable to equity holders (this ratio is not part of the Basel III framework).

9. Impaired advances are advances in respect of which a bank has raised a specific impairment and include any advance or restructured credit exposures subject to amended terms, conditions or concessions that are not formalised in writing.

1.4 Flavour-of-the-year topics for 2013

1.4.1 Introduction

Each year the Department identifies certain flavour-of-the-year topics to be discussed with banks' boards of directors (boards) during supervisory meetings held with banks. Accordingly, Guidance Note 10/2012[10] identified the following three flavour-of-the-year topics for 2013:

i. Impact of Basel 2.5 and Basel III on banks' business models and strategy
ii. Recovery planning – Phase 2
iii. Anti-money laundering (AML)/combating the financing of terrorism (CFT) controls of locally registered banks, inclusive of the foreign operations of such banks.

Banks' boards were requested to make presentations to the Department regarding each of the three topics. These three topics are discussed in greater detail below.

10. Available at http://www.resbank.co.za/Publications/Pages/BanksActGuidance.aspx.

1.4.2 Impact of Basel 2.5 and Basel III on banks' business models and strategy

Following the implementation of the Basel III framework in South Africa on 1 January 2013, a key focus area remained the impact of the Basel III framework on the business models and strategies of banks, as well as capital targets, sources of capital and the impact of the new loss-absorbency requirements.

In general, banks were already well prepared for the impact of the Basel III framework due to their interaction with the Department and as a result of the quantitative impact studies performed by them during 2012. Following the recent global financial crisis, banks had become more focused on how capital intensive some business models and strategies were, and where they had to refocus strategies or amend pricing due to increased capital and liquidity requirements. During 2013 banks accordingly focused on balance-sheet efficiencies, restructuring and capital redeployment within the consolidated groups, as well as on enhancing areas such as liquidity management systems and a revised outlook on trading business. Capital and funding plans also continued to receive a significant amount of attention during 2013. A number of banks were also reconsidering their return-on-equity targets under the Basel III framework, taking into account the higher capital requirements.

As expected, banks had reassessed their internal capital targets or buffers, given the release of the Basel III capital framework for South Africa, and it was evident that in general banks had increased their capital-adequacy targets and were focusing not only on total capital levels, but also specifically on CET1 capital. It was observed that banks had remained well capitalised, had already exceeded their capital targets and were well prepared for the stricter capital requirements that were phased in from 2013.

Many banks were still investigating the capital-raising structure within their groups given the new requirements under the Basel III framework. It is expected that this trend will continue to develop as banks and investors become more familiar with the new Basel III requirements.

The new loss-absorbency requirement under the Basel III framework drew considerable attention from banks and investors. Banks were more comfortable with the detailed requirements after the Department had released its guidance on loss absorbency at the point of non-viability.

1.4.3 Recovery planning – Phase 2

The FSB's key attributes of effective resolution regimes for financial institutions recommend that all systemically significant financial institutions have recovery and resolution plans in place. The Department first requested banks to start developing recovery plans in 2012.

During 2013 individual workshops were held with the five large South African banks to discuss their draft recovery plans, in which they had set out detailed plans on how they would deal with periods of severe stress. The recovery plans of the banks were benchmarked against the FSB document and feedback was given to the banks relating to the gaps identified by the Department. The banks were given until the end of 2013 to have a board-approved, integrated recovery plan. Significant progress was made by the banks with their recovery plans as evidenced by the presentations made by their boards during the last quarter of 2013. Future development of recovery plans by the large banks is expected to focus on the refinement of these plans.

1.4.4 Anti-money laundering/combating the financing of terrorism controls of locally registered banks, inclusive of the foreign operations of such banks

Banks' boards made presentations on the above flavour-of-the-year topic, and the domestic banking industry overall demonstrated a concerted effort and commitment to placing AML/CFT controls at the top of their agenda by identifying weaknesses within their respective organisations and presenting plans on how those weaknesses would be mitigated and resolved.

During 2013 banks demonstrated the responsibilities and commitment of their boards and senior management in their roles of ensuring that the risks associated with AML/CFT controls were being considered and addressed appropriately. This flavour-of-the-year topic raised the necessary awareness about the subject matter and the risks associated with AML/CFT in the banking industry.

1.5 Forward-looking approach to supervision

Principle 8 of the Core Principles for Effective Banking Supervision (the Core Principles), issued by the Basel Committee in September 2012,[11] emphasises that "adopting a forward-looking approach to supervision through early intervention can prevent an identified weakness from developing into a threat to safety and soundness".

11. Available at http://www.bis.org/publ/bcbs230.htm.

The Department, as in the past, continued to adopt and implement the Core Principles prescribed by the Basel Committee in 2013, and accordingly placed specific focus on assuming a forward-looking supervisory approach.

To this end, the Department's interaction with the chairpersons of the banks' boards, chief executive officers and management shifted during 2013 to focus more on the discussion of their banks' future strategies, risk appetite, and capital and funding projections in order to assess the adequacy and sustainability thereof. Banks' targeted return-on-equity levels and projected dividend covers over the next few years were also focused on in terms of the forward-looking approach assumed by the Department.

Other specific focus areas in 2013 were the setting of capital buffers and targets in meeting the new Basel III capital requirements; capital-raising initiatives as part of the banks' forward-looking capital plans; further discussions on the recovery plans developed by banks for scenarios that could lead to them reaching the point of non-viability; and the relevant actions to be taken should predefined indicators be breached. A crucial theme was the review of banks' internal macroeconomic stress-testing frameworks and models in order to understand the impact of plausible stress scenarios of varying severity.

For systemically important banks the Department is now collecting information on a more frequent basis in order to monitor and identify emerging risks timeously by considering their capital projections, and their demand and supply in respect of both regulatory and economic capital. This enables the Department to identify and monitor trends both across the large banks and on a bank-specific basis.

The Department will continue to focus its resources to enhance its forward-looking supervisory approach to allow the early detection, identification and mitigation of emerging risks faced by banks both individually and collectively.

1.6 Update on the implementation of a twin peaks model of financial regulation in South Africa

As explained in the Department's 2012 *Annual Report*,[12] South Africa is in the process of reforming its financial sector regulatory framework by moving towards a twin peaks model of financial regulation. Under the planned twin peaks approach, there will be opportunity to streamline the supervision of the financial system. Under a twin peaks model of financial regulation, the Bank will take responsibility for oversight of the safety and soundness of banks, insurers and financial conglomerates and macro-financial stability, and the Financial Services Board will take responsibility for market conduct supervision. There will be a phased approach to the implementation of a twin peaks model of financial regulation in South Africa, starting with the enactment of relevant legislation to establish the relevant regulators. In December 2013 the National Treasury (NT) released for public comment the cabinet-approved Financial Sector Regulation Bill, 2013 (the Bill)[13] to give effect to the establishment of the necessary regulators, their powers and responsibilities.

12. Section 1.4.

13. Available at http://www.treasury.gov.za.

The Bill not only addresses the establishment of regulators, but also covers broader matters, including balancing operational independence and accountability of regulators; creating a Financial Services Tribunal; strengthening enforcement and the ombud schemes; enhancing co-ordination and co-operation between financial regulators and establishing a crisis management and resolution framework. With respect to the last two points and the role of the Bank, the Bill gives the Bank primary responsibility to oversee financial stability, provides for resolution powers and identifies the Bank as the resolution authority in South Africa. In addition, the Bill creates a statutory inter-agency Financial Stability Oversight Committee, chaired by the Governor of the Bank, with appropriate financial stability powers.

In preparation for its responsibilities outlined in the Bill, the Bank set up working groups in 2013 to further the twin peaks process. These working groups address details such as implementation, information, funding and resource requirements. In the interim, the Bank, together with the NT, will drive issues related to its role of the prudential authority and financial stability, including the supervision of financial market infrastructures and resolution, while the Financial Services Board, together with the NT, will drive issues related to its role as market conduct authority. It is envisaged that once the Bill is passed into law, the prudential authority and the other related structures highlighted above will come into operation at the Bank relatively quickly. The deadline for public comments on the Bill was extended to 7 March 2014.

1.7 Financial stability developments and trends

Global and domestic financial stability risks that had been identified in early 2013 as a possible cause for concern were communicated in the Bank's March 2013 and September 2013 editions of the *Financial Stability Review*.[14] In a global context, the risks to the domestic financial system of a global recovery intensified during 2013. The unwinding of unconventional monetary policy actions in advanced economies and the resulting capital outflows and financial market volatility were the main concerns identified.

14. Available at http://www.resbank.co.za/Publications/Reviews/Pages/FinancialStabilityReview.aspx.

Financial stability risks that emerged during the course of 2013 included (i) domestic households' vulnerability to interest rate increases given their relatively high debt levels; (ii) disintermediation due to tighter regulation of banks (domestically and globally); and (iii) the possible unwinding of the United States' (US) quantitative easing (QE) programme, which dominated global and domestic financial markets during 2013. The impact of QE tapering in the US on capital flows and bond, equity and FX markets of emerging-market economies (EMEs), including South Africa, was severe.

An important macroprudential instrument that has already been agreed upon for implementation in terms of Basel III compliance is the countercyclical capital buffer (CCB). The CCB is designed to protect the banking sector from the build-up of systemic risks associated with periods of excessive credit growth by ensuring that there is a capital buffer that takes into account the macrofinancial environment in which banks operate. An exercise conducted by the Bank in this regard in 2013 indicated that there was no need yet to consider a CCB add-on for banks.

Globally, non-bank financial intermediation, or shadow banking, has become a vital part of the financial system as it provides an alternative to customers for gaining access to credit and other financial services in support of economic activity. However, a large non-bank financial sector also poses potential systemic risks to the financial system. From a systemic perspective, it is important that bank-like activities outside the banking sector are regulated commensurate with the risk that they introduce into the financial system and to promote a level playing field. Although this is not currently an area of serious concern, the Bank is in the process of investigating the refinement of the instrument revaluation methodology and to collect more granular data on the domestic shadow-banking system.

As a member of the FSB, South Africa underwent a country peer review in late 2012, the results of which were published in early 2013. The peer review covered interagency co-ordination and its regulatory structure, as well as the regulation of the OTC derivatives markets. The report issued in this regard noted the steps that the South African financial authorities had taken to address the enhancement of co-ordination and exchange of information, and the approach to the implementation of regulatory reform in terms of OTC derivatives. Proposed reforms will be implemented in a manner that is appropriate for the South African context and conducive to enhancing domestic financial stability.

1.8 Participation in international surveys

1.8.1 The Southern African Development Community Protocol on Finance and Investment follow-up survey

The Protocol on Finance and Investment (the Protocol) is one of the protocols entered into by the Southern African Development Community (SADC) member states to give effect to their commitments under the SADC treaty. The Department participated in a follow-up exercise on the survey that was discussed in the Department's 2012 *Annual Report*.[15] This ongoing survey formed part of the SADC secretariat's measurement matrix to track member states' progress in implementing the Protocol. The survey addressed a wide range of topics relating to legal and operational frameworks for investment and finance in South Africa, and specifically addressed co-operation and co-ordination in banking regulation and supervision.

15. Section 1.7.2.

1.8.2 Organisation for Economic Co-operation and Development Survey on Implicit Government Guarantees of Bank Debt

The Organisation for Economic Co-operation and Development's (OECD) Committee on Financial Markets (CMF) has been reviewing the effects of the policy responses by certain countries following the recent global financial crisis in entrenching perceptions that governments will always make guarantees available for bank liabilities and assets during crisis situations. Some market participants believe that the debt of banks, in particular systemically significant institutions, benefit from an implicit guarantee provided by governments. The survey explored this issue, with emphasis on work done by jurisdictions to estimate implicit bank debt guarantees, and considered policy responses relating to reducing the value of implicit guarantees of bank debt, including implementation of relevant reforms contained in the Basel III capital framework. The purpose of the survey was for CMF members to learn from work performed by other members, including how to best estimate and analyse the value of implicit bank debt guarantees and how to limit that value.

1.8.3 Basel Committee on Banking Supervision survey on financial inclusion

The Basel Consultative Group, a subcommittee of the Basel Committee, conducted a 'range of practice' survey on financial inclusion. The purpose of the survey was to review financial inclusion initiatives in different countries and to understand the risks to banking supervision that arose from increasing financial inclusion. This wide-ranging survey touched on various areas, including relevant jurisdictions' financial landscapes, the responsibilities, powers and functions of different supervisors, developments in financial inclusion in each jurisdiction, co-operation and collaboration between domestic and foreign supervisory authorities, licensing criteria for supervised entities and supervisory approaches adopted.

1.9 Participation in international regulatory and supervisory forums

1.9.1 Basel Committee on Banking Supervision

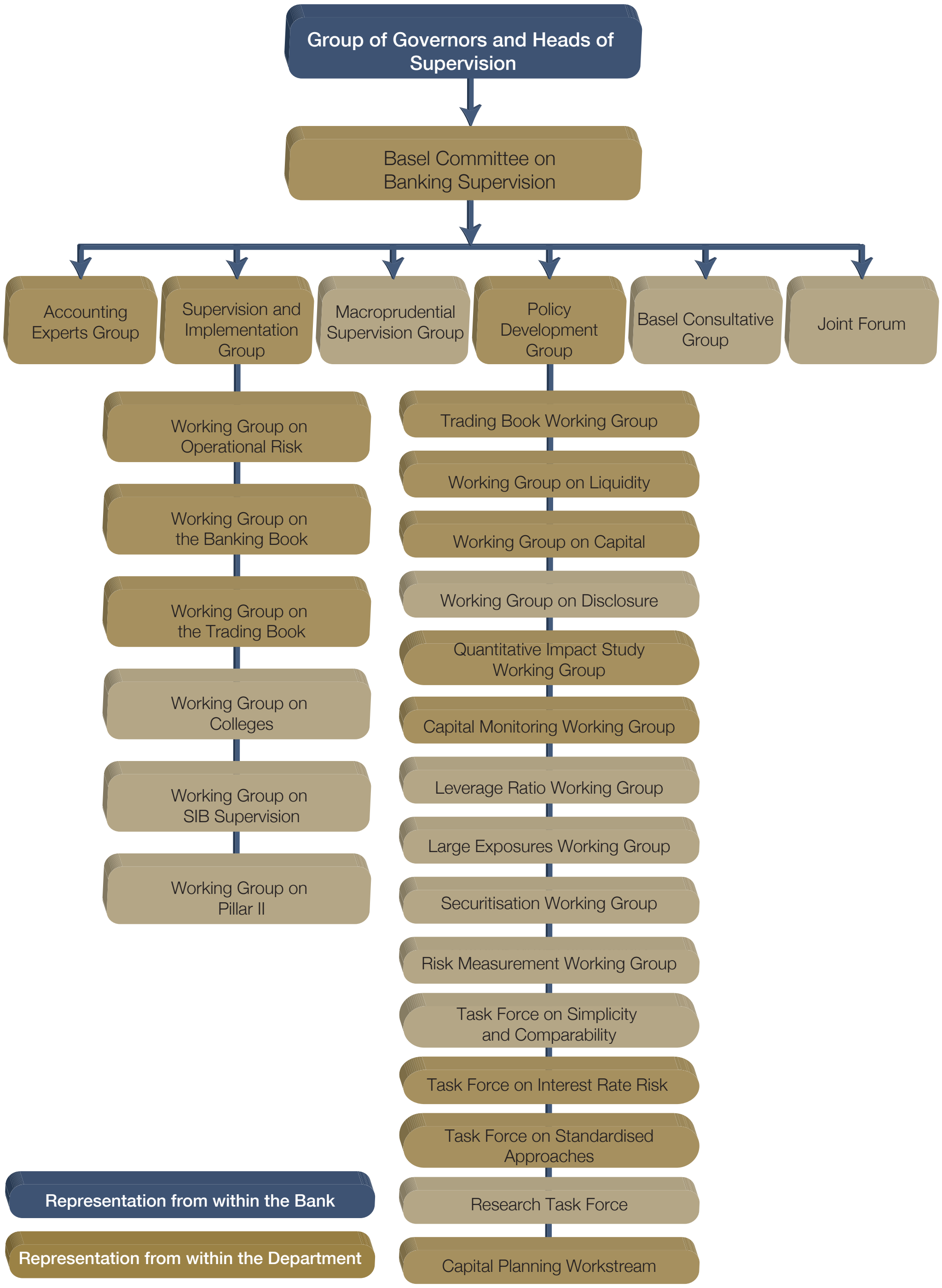
The Department represents South Africa on several committees within the structure of the Basel Committee. Representation is aimed at influencing the formulation of policy and elevating the profile of South Africa as a jurisdiction with sound banking supervision practices.

Policy development undertaken by committees reporting through the Policy Development Group (PDG) to the main committee is focused on specific regulatory areas where the committees are mandated to develop or maintain rules approved at Basel Committee level for inclusion in the Basel framework. Other committees in the Basel Committee's structure under the Supervision and Implementation Group (SIG) review the impact of changing regulations, the effectiveness and consistency of implementation of the Basel framework among jurisdictions and banks, implementation within regulatory risk areas and the convergence between banking and other standard-setting regimes.

The structure of the Basel Committee illustrated in Figure 1.2 was established in 2013. Participation in the groups is generally by invitation, although the Department requests inclusion in committees when the subject matter gains sufficient importance in the South African banking context.

The objectives of these groups are explained hereunder for groups in which the Department represented South Africa in 2013. Focal issues are also discussed where public knowledge of these issues permits it.

Figure 1.2 Structure of the Basel Committee on Banking Supervision (2013)



1.9.2 Accounting Experts Group

The function of the Accounting Experts Group (AEG) is to promote alignment between international accounting and auditing standards and practices, and risk management at banks. Areas of attention include the way in which market discipline is addressed through transparency of banks' public disclosure of financial and risk information. The AEG plays an active role in the development of international accounting and auditing standards. The Registrar chairs the AEG.

The audit subgroup of the AEG oversees auditing issues affecting banking supervision. International auditing standard-setting developments come under its attention, as well as any other documents emanating from the International Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants.

1.9.3 Supervision and Implementation Group

The SIG is the peer review committee of the Basel Committee. Its mandate is to help foster financial stability by supporting strong national and international supervision and regulation of banks. It has two primary objectives, namely (i) to foster the timely, consistent and effective implementation of the Basel Committee's standards and guidelines, and (ii) to advance improvements in practices in banking supervision, particularly across Basel Committee member countries.

The results of Level 2 Regulatory Consistency Assessment Programme (RCAP) studies that are commissioned by the Basel Committee are discussed at the SIG meeting prior to publication. Assessment on South Africa is scheduled to take place in the second half of 2014. Meetings of the SIG in 2014 will review reports on country RCAPs and further surveys on variations in risk-weighted assets (RWA) with specific focus on market risk RWA in the forthcoming survey.

1.9.4 Working Group on Operational Risk

The Basel Committee established the Working Group on Operational Risk (WGOR), previously known as the Standards Implementation Group Operational Risk Subgroup, as a permanent working group addressing operational risk policy and implementation issues. It reports to both the PDG and the SIG.

The principal focus of WGOR is the development of policy and the practical challenges associated with the successful development, implementation and maintenance of an operational risk framework addressing the requirements and expectations of the Basel Committee's allowed approaches, with a specific focus on the advanced measurement approach (AMA). Members assist with the drafting of policies, discuss operational risk implementation issues in their jurisdictions and participate in developing resolution plans.

Work continued in 2013 in terms of the fundamental review of the simpler approaches and the streamlining of AMA practices.

In addition, new work undertaken during 2013 by WGOR includes:

- sound principles peer review: The focus of the peer review was on the implementation of the sound principles for the management of operational risk at all three lines of defence in banks as well as practices of supervisory agency practices; and
- simplification of the AMA: The group had been tasked to consider options to refine the 'use test' with a view to increasing supervisory effectiveness of the AMA.

The Department continued to participate actively not only in WGOR, but also in some of the sub-workstreams during the period under review and will continue to do so during 2014.

1.9.5 Working Group on the Banking Book

The SIG Banking Book (SIG-BB) subgroup is a workstream of the SIG that was initially established to evaluate differences in RWA across banks using the IRB approach for credit risk, assess their compliance with RWA calculations according to the Basel framework's standards and develop recommendations to encourage the convergence of practices. The SIG-BB met these objectives by performing an in-depth hypothetical portfolio exercise whereby IRB parameter estimates of 32 large international banks were benchmarked for a set of common wholesale obligors. The work included questionnaires that were sent to the banks and having meetings with the banks. The work culminated in a public report titled *Regulatory Consistency Assessment Programme: Analysis of Risk-weighted Assets for Credit Risk in the Banking Book*.[16] The Department ensured active participation of South Africa in the studies where the scope of participation could be

16. Available at http://www.bis.org/publ/bcbs256.htm.

addressed using credit exposures of South African banks. Alternatively, the methods applied in the studies were applied on a purely domestic sample for the purposes of investigating consistent application of risk weights among domestic banks. Banks that showed significant differences in practice were dealt with accordingly.

At its September 2013 meeting, the Basel Committee requested the SIG-BB to prepare a programme for further analytical work. The programme consists of additional analysis of core portfolios not yet subject to in-depth studies and work on formulating guidance on specific issues to improve regulatory and supervisory practices influencing the consistency of RWA calculations. The SIG-BB is in the beginning phases of carrying out this work, which should be completed by end of the first quarter of 2015.

1.9.6 Working Group on the Trading Book

The SIG Trading Book (SIG-TB) subgroup is a workstream of the SIG established in 2012 to analyse reasons for differences in RWA in the trading book across different jurisdictions. This analysis is part of a wider RCAP initiated by the Basel Committee in 2012. The aim of the RCAP is to ensure consistent implementation of the Basel III framework, help strengthen the resilience of the global banking system, maintain market confidence in regulatory ratios and provide a level playing field for banks operating globally.

During the period under review, the SIG-TB extended its analysis conducted in 2012 to more representative and complex trading positions. Consistent with the findings in the first report *Regulatory Consistency Assessment Programme (RCAP) – Analysis of Risk-weighted Assets for Market Risk*,[17] the results showed significant variation in the outputs of market risk internal models used to calculate regulatory capital. In addition, the results showed that variability typically increased for more complex trading positions. The work of the SIG-TB in 2013 culminated in the latest report entitled *Regulatory Consistency Assessment Programme (RCAP) – Second Report on Risk-weighted Assets for Market Risk in the Trading Book*,[18] which was published by the Basel Committee in December 2013.

17. Available at http://www.bis.org/publ/bcbs240.htm.

18. Available at http://www.bis.org/publ/bcbs267.htm.

The Department's representative on the SIG-TB contributed to the finalisation of the studies undertaken; however, while coverage of South African banks could not be incorporated in the studies, the outcome of the study provided a perspective that affected the active supervision of market risk. The SIG-TB was also mandated in 2013 to investigate differences in RWAs across jurisdictions relating specifically to counterparty credit risk and credit valuation adjustments. Where applicable, South African banks will contribute to these studies, while aspects of planned work will be undertaken domestically by the Department.

1.9.7 Policy Development Group

The PDG assesses changes to banking regulation that are proposed by its subgroups and other streams under the Basel Committee structure. It serves the Basel Committee by identifying issues, commissioning research, overseeing quantitative analysis and making recommendations on policy which the Basel Committee has the discretion to adopt. It also reviews emerging supervisory issues aimed at promoting a sound banking system and high supervisory standards. The PDG has several executive subgroups and workgroups reporting to it on a wide range of risk and capital issues. The Department is represented on the PDG and many of its subgroups where the focal subject matter is relevant to South Africa.

Subjects receiving the attention of the PDG in 2013 that have an impact on the South Africa economy and the domestic banking system included the fundamental review of the trading book, developments related to the LCR and NSFR, revisions to the securitisation framework, capital requirements for OTC derivatives cleared through central counterparties (CCPs) and margin requirements for non-centrally-cleared derivatives. South Africa's stance on the considerable range of rules under formulation and several issues pertinent to South Africa's ability to comply with proposed or impending rules was asserted through representation on the PDG.

1.9.8 Trading Book Working Group

South Africa has been a member of the Trading Book Group (TBG) since 2007. The TBG deals with market risk in its various forms, including the trading book.

The TBG is currently concerned with addressing issues emanating from the market risk capital charges introduced in the Basel 2.5 framework, which significantly altered the amount of capital required to be held for market risk and led to a profound alteration in the way South African banks participate in trading. The TBG continues to concentrate on a fundamental review of the market risk capital framework. Part of the review is focused on the definition that distinguishes the so-called trading book from the banking book, how trading activities are defined and how risks in trading books (both market risk and counterparty credit risk) should be addressed by appropriate levels of regulatory capital.

Discrepancies between the standardised and internal model approaches for reporting market risk are also being dealt with by the TBG. The Department welcomes this review with caution against replacing the current STA with a framework that is comparable in complexity with the internal models approach. Small banks that are exposed to market risk through minor FX dealings and participation in straight-forward bond markets should be recognised and dealt with through appropriate regulation. Regulators and banks operating in the rest of Africa rely on the existing STA that the TBG intends to phase out. With minor adjustments weaknesses in the existing approach can be corrected.

The methods for calculating capital under both the standardised and internal model approaches are currently receiving attention to reduce the effects of inappropriate diversification recognition and double counting. Market liquidity as a limitation to banks' ability to trade is also being assessed in the review.

During 2013 the TBG issued a second consultative paper on the fundamental review[19] to which many organisations responded with valuable comments. The comments received in this regard are being considered by the TBG and will be used to further refine the fundamental review.

19. Available at http://www.bis.org/publ/bcbs265.htm.

1.9.9 Working Group on Liquidity

The Working Group on Liquidity deals with the two main standards relating to liquidity and funding, namely the LCR and the NSFR.

The Department was actively involved in the design of the revised NSFR through its involvement in various Basel Committee subcommittees. This culminated in the release of a consultative document on the proposed framework for the NSFR.[20] Significant attention will be paid by representatives of the Department at various committees to contribute to the finalisation of the framework due to the suitability of the current framework on banking systems and economies of other jurisdictions.

20. Available at http://www.bis.org/publ/bcbs271.htm.

The NSFR aims to limit over-reliance on short-term wholesale funding, encourages better assessment of funding risk across all on- and off-balance-sheet items, and promotes funding stability over a longer-term time horizon. The NSFR is defined as the amount of available stable funding relative to the amount of required stable funding, with 'available stable funding' being defined as the portion of capital and liabilities expected to be reliable over the one-year time horizon considered by the NSFR. This ratio should be equal to at least 100 per cent on an ongoing basis. The amount of such stable funding required from a specific institution is a function of the liquidity characteristics and residual maturities of the assets held by that institution as well as those of its off-balance-sheet exposures.

The LCR and NSFR are both subject to monitoring periods before becoming statutory requirements. Formal monitoring in South Africa of both ratios commenced on 1 January 2013, while the LCR will become effective as a compliance standard at 60 per cent from 1 January 2015 with a phase-in period up to 1 January 2019 when 100 per cent compliance will be required. The NSFR will be a compliance standard from 1 January 2018.

1.9.10 Working Group on Capital

The Working Group on Capital (WGC) was established early in 2013 by combining two groups that dealt with issues related to capital, namely the Definition of Capital Subgroup and the Contingent Capital Working Group. The WGC takes responsibility for handling all policy issues associated with the definition of capital under the Basel III framework and issues associated with capital-like instruments.

The WGC formulates policy responses to frequently asked questions related to capital submitted to the Basel Committee by regulators and banks to ensure consistent and clear interpretation of the definition of capital. The WGC also monitors developments around capital instruments, specifically bail-in instruments, loss absorbency and point of non-viability aspects that were introduced under the Basel III framework. South Africa participated in these surveys and will continue to participate actively in this group in 2014. Discussions arising from the studies have assisted the supervision of capital structures in South African banks, and have guided the development of domestic recovery and resolution plans.

1.9.11 Quantitative Impact Study Working Group

The Basel Committee established the Quantitative Impact Study (QIS) Working Group to calibrate the Basel III rules and to assess their impact on participating banking groups in member countries. Although a number of Basel Committee member countries implemented the Basel III framework during 2013, the QIS exercise continues to take place semi-annually with end-June and end-December reporting dates. The Department will continue to participate in the activities of the QIS Working Group in 2014.

The QIS exercise that is currently being conducted measures the amount of capital required by participating institutions and countries to reach the fully phased-in capital requirements of the Basel III framework based on balance-sheet information at the reporting date. Compliance with the LCR, NSFR and the leverage ratio has not yet been incorporated into the exercise.

While the QIS Working Group's responsibilities include developing and implementing the QIS and computational analysis of reported data, the group supports other Basel Committee work streams by developing QIS templates and the software needed to translate and check data submissions for use in the impact studies of these groups.

The scope of the QIS exercises started in 2013 includes:

- changes to the definition of capital;
- enhancements to risk coverage (including the revisions to the market risk framework, revisions to counterparty credit risk measurement and to the capital requirements for securitisations held in the banking book);
- the leverage ratio; and
- standards developed by the Working Group on Liquidity.

The future scope of the QIS exercises will expand to include further initiatives by the Basel Committee.

South Africa's participation in the QIS studies is essential to illustrate the wide-ranging impact of forthcoming rule changes, particularly from an emerging-market perspective.

1.9.12 Capital Monitoring Working Group

The Department contributes to the work of the Capital Monitoring Group (CMG), which monitors the level and cyclicality of minimum required capital (MRC) produced under the Basel 2.5 and Basel III frameworks. At present data from 105 banks that have adopted one of the advanced approaches to calculate their MRC are collected and analysed for inclusion in the CMG report submitted to the Basel Committee.

Data from banks across 15 countries are analysed in reports produced by the CMG every 6 months. Their analysis covers areas including MRC, capital ratios and buffers, RWAs, portfolio-level exposures, risk parameters and transitional capital floors. Members of the CMG share their experiences in monitoring capital requirements and the levels of capital on a national basis. The impact of participation has been pronounced in the Department's capital supervision and its assessments of banks' internal capital adequacy assessment process (ICAAPs).

1.9.13 Task Force on Interest Rate Risk

Following on from the work done on the fundamental review of the trading book by the TBG, the Basel Committee formed the Task Force on Interest Rate Risk to examine options for capturing interest rate risk and credit-spread risk in the banking book in the capital framework. The Department has identified this as an important area of development and will be represented on this working group to guide its rule-making developments and to assess the potential on the domestic banking sector through the work programme for 2014.

1.9.14 Task Force on Standardised Approaches

The vast majority of banks around the world and in South Africa make use of the standardised approaches for credit and operational risk to assess capital adequacy. To ensure that the standardised approaches remain robust and appropriately calibrated, the Basel Committee established the Task Force on Standardised Approaches (TFSA) to consider enhancing the standardised approaches for credit and operational risk. The TFSA is focusing on the STA to measure credit risk while the WGOR focuses on the redesign of the standardised operational risk framework.

The key objectives of the TFSA are to:

1. ensure the standardised approaches continue to be suitable for assessing the capital adequacy of internationally active banks, as well as other banks that are not using the advanced approaches for credit and operational risk;
2. ensure that the calibration of capital requirements under the standardised approaches reflects, to a reasonable degree, the inherent riskiness of positions for all main categories of exposures;
3. seek to strengthen the link between the standardised approaches and measures of risk based on banks' internal models; and
4. seek to reduce or remove, where possible, the reliance on external ratings, including developing supplementary measures for risk classification and encouraging stronger supervisory practices to promote alternative measures for risk assessment.

The TFSA's focus during 2013 was to identify the weaknesses in the existing STA for credit risk and to propose alternative ways forward. During 2013 South Africa was a corresponding member of the TFSA. Owing to the impact the revised STA will have on the South African banking sector, it is imperative for a departmental representative to attend meetings in 2014. Membership on the committee has therefore been established.

1.9.15 Capital Planning Workstream

During 2013 the Capital Planning Workstream finalised a capital planning survey that commenced earlier in 2013. The objective of the survey was to collect information on banks' capital planning practices and analyse it to identify the range of practices across different segments of capital planning processes and across multiple jurisdictions. The survey focused on gathering information on processes in six key areas of capital planning practices, namely general practices, governance, policy setting, risk management, stress testing and capital actions. Selected banks in South Africa were requested to participate in the survey. The Basel Committee subsequently released a document titled *A Sound Capital Planning Process: Fundamental Elements* in January 2014.[21]

21. Available at http://www.bis.org/publ/bcbs277.htm.

1.9.16 Anti-money Laundering/Combating the Financing of Terrorism Expert Group

The Basel Committee's AML/CFT Expert Group helps both supervisors and financial institutions to implement AML/CFT elements of the Core Principles in accordance with the Financial Action Task Force's (FATF) standards by producing practical and technical guidance that are applicable to national and international banks and banking groups.

As a result of FATF issuing the revised FATF Recommendations in 2012, the Basel Committee updated its AML/CFT guidelines to be aligned to the FATF Recommendations and to show the banks and banking groups how they should include money laundering (ML) and terrorism financing (TF) risk management within their overall approach to risk management.

1.9.17 Eastern and Southern Africa Anti-Money Laundering Group

The Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) held two meetings in April and September 2013. The ESAAMLG meeting held in September 2013 was followed by a private-/public-sector dialogue arranged under the United Kingdom Presidency of the Group of Eight (commonly referred to as the 'G8'). The main points of discussions related to the challenges faced by banks in promoting financial inclusion, the implications of ML and TF legislation and sanctions on money services business, as well as difficulties experienced in terms of establishing and maintaining correspondent banking relationships with banks in developed markets.

1.9.18 Financial Action Task Force meetings

A representative of the Department was part of the delegation that represented South Africa during the 2013 FATF meetings.

The FATF working group and plenary meetings for 2013 focused on the following that was of importance to the Department:

- How financial supervisors would be assessed during the next round of FATF mutual evaluations. It was concluded that in addition to countries' compliance with Core Principle 29 of the Core Principles dealing with the abuse of financial services, the assessment methodology specifically included other additional 13 Core Principles which should also be applied to the area of AML/CFT supervision. Compliance with the additional 13 Core Principles will also be assessed during the next round of mutual evaluations. The assessors will look at the application of a risk-based approach by financial supervisors in its supervision of financial institutions compliance with AML/CFT requirements, as well as the impact of supervisory actions on AML/CFT compliance in financial institutions.
- The fourth round of assessments will commence with Spain and Norway, with a target date of October 2014 set to discuss the mutual evaluation reports for the aforementioned countries. A final date for South Africa's next mutual evaluation has not yet been finalised. It is anticipated that South Africa will only be assessed during the fourth quarter of 2016 or early 2017.

1.9.19 Community of African Bank Supervisors of the Association of African Central Banks

The Community of African Bank Supervisors (CABS) is a newly established body and its first meeting is expected to take place in November 2014. In 2013, the chair of CABS (Mauritius) convened an initial meeting of selected countries to prepare for the first CABS meeting. The initial meeting was used to discuss issues to be included in the agenda of the CABS, namely a peer review mechanism, subcommittees to be established, co-ordination and collaboration processes, a work programme for the next three years and the proposed budget. These will be presented for approval at the next CABS meeting and for approval by the Association of African Central Banks assembly, also scheduled to convene in November 2014.

South Africa was identified to contribute to the CABS's future work which focuses on areas such as the work programme, colleges and peer reviews.

1.9.20 Aggregation Feasibility Study Group

The Aggregation Feasibility Study Group (AFSG) aims to explore solutions to international data aggregation for OTC derivatives monitoring. The work of the group entails the review of options to produce and distribute global aggregated trade repository (TR) data, taking into account legal and technical issues. Financial authorities need TR data to fulfil their mandates and to monitor financial stability.

In 2013 the AFSG drafted a report outlining its analysis of the options being considered which included a physically centralised model of aggregation, a logically centralised model of aggregation and the collection of raw data from local TR databases by individual authorities that aggregate the data themselves. The report summarises the authorities' requirements for aggregated OTC derivatives data, focusing on minimum prerequisites for useable data that fulfil authorities' mandates. It also addresses legal and policy considerations concerning data submission and access to data, and governance of the aggregation mechanism. The report discusses data and technology considerations associated with meeting authorities' requirements for aggregated data.

The Department's contribution to AFSG included input to the report through participation in its surveys. The Department raised domestic concerns over the framework at AFSG meetings, and also contributed to focused research by the AFSG on the protection of data and suggested governance structures. The AFSG's study facilitated valuable interaction with other macroprudential regulators, policy analysts and legal experts on regulatory developments which assisted the Department's role in drafting prudential regulations for financial market infrastructures such as TRs and CCP.

1.10 Participation in domestic regulatory and supervisory forums

The Department continues to serve on, and participate in, various domestic committees, tasks groups and working teams to consult with banking industry participants and bodies, audit firms, government departments and other financial regulatory authorities. Some of the these bodies include the NT's committees and initiatives, the Banking Association of South Africa (BASA), the South African Institute for Chartered Accountants (SAICA), the Committee for Audit Standards, the Financial Services Board, the National Credit Regulator, the Financial Intelligence Centre (FIC) and the Independent Regulatory Board for Auditors.

The objective of these interactions is topical and ranges from ongoing consultation on detailed complexities in the regulatory environment to operational and systemic concerns arising from economic developments or developments in the regulatory environment. These interactions enable the Department to stay abreast of developments across a wide spectrum and potential impacts on the banking industry.

The Department, together with inputs obtained from the banks via BASA, was able to develop and provide more detailed guidance on the Basel III framework's new higher loss-absorbency requirements for capital instruments at the point of non-viability. The guidance provided was based on the minimum requirements from the Basel Committee and took into account international best practice as used by other supervisory bodies and from various discussions with global financial intermediaries on how these new capital instruments should be structured. The guidance enabled domestic banks to gain a better understanding of the requirements to enable them to liaise and raise awareness with potential investors, which will enable them to issue these new capital instruments as part of their capital base.

1.11 Regional co-operation and interaction

1.11.1 Financial Stability Institute: High-level meeting for African banking supervisors

The eighth Financial Stability Institute (FSI) high-level meeting for African banking supervisors was held in Cape Town, South Africa, in January 2013. As in previous years, the meeting was hosted jointly by the FSI and the Department.

The theme for the 2013 meeting was "Strengthening Financial Sector Supervision and Current Regulatory Priorities".

1.11.2 Southern African Development Community Committee on Banking Supervision

The Department is a member of the SADC Committee of Banking Supervisors (SSBS). Established by the SADC Committee of Central Bank Governors, the principal aim of the SSBS is to implement the memorandum of understanding (MoU) that was concluded on 28 July 2006 between the central banks of the SADC member states on co-operation and co-ordination in the area of banking, regulatory and supervisory matters. The MoU aims to establish a framework for co-operation and co-ordination between SADC central banks in order to promote harmonisation of banking regulatory and supervisory matters. One of the main tasks of the SSBS is to oversee the drafting of a model banking law for SADC member states. To this end, a five-member working group was formed to focus only on the drafting of the SADC model banking law. The working group comprises members of the central banks of South Africa, Zambia, Malawi and Zimbabwe.

1.11.3 Toronto Centre Crisis Preparedness Programme for SADC

The Bank hosted, for the third time, a joint programme with the Toronto Centre on macro prudential surveillance. The workshop, which took place from 5 to 8 August 2013, was a regional training programme for senior officials from central banks and supervisory agencies from SADC member countries.

1.12 Expression of gratitude

I wish to express my appreciation to the Minister of Finance, Mr Pravin Gordhan, for his input on requests in terms of statutory requirements. To the Governor of the Bank, Ms Gill Marcus, and Deputy Governor Lesetja Kganyago: thank you for your ongoing co-operation, guidance and support during 2013.

My sincere appreciation also goes to the staff members of the Department for their continued efforts and willingness to repeatedly go beyond the call of duty to meet the challenges and demands of an ever-changing supervisory and regulatory landscape.

René van Wyk
Registrar of Banks