Financial Stability Review

Second edition
2024

South African Reserve Bank

Contents

The SARB's financial stability mandate

- Financial Sector Regulation Act: Legal mandate of SARB to protect and enhance financial stability in South Africa

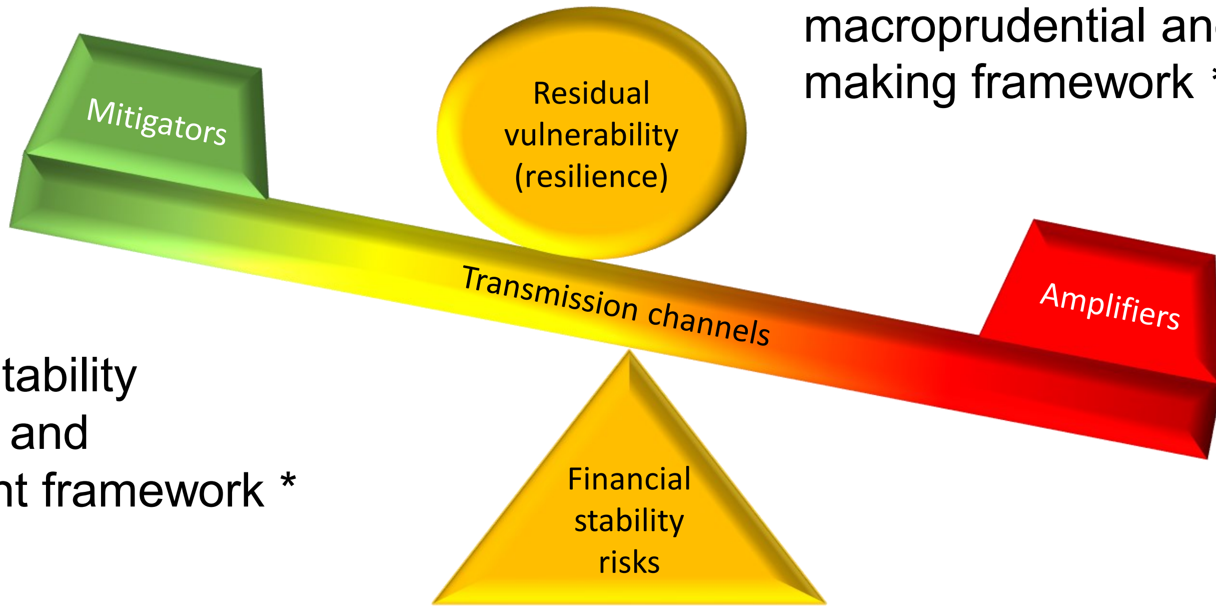
- Financial sector should be capable to perform its functions without interruption, despite changes in economic circumstances

  - Resilient to shocks
  - Efficiently intermediate funds
  - Even in adverse conditions
  - Public confidence in the financial system and institutions

- Precondition for balanced and sustainable economic growth

How the SARB executes its financial stability mandate

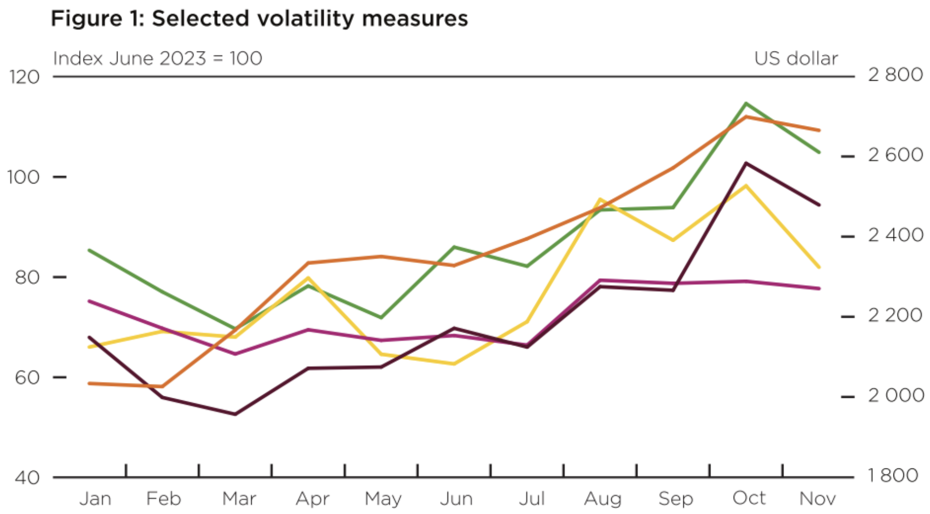
Financial stability macroprudential and decision-making framework *

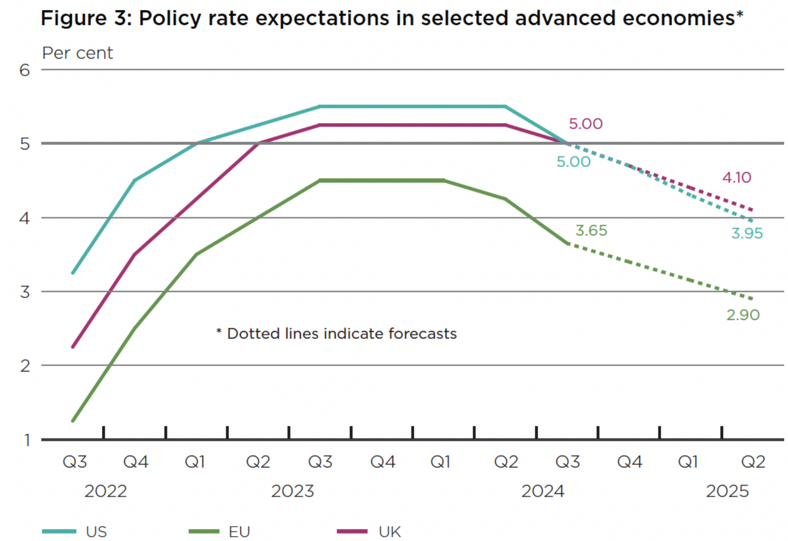


Financial stability monitoring and assessment framework *

* Documented frameworks available at https://www.resbank.co.za/en/home/what-we-do/financial-stability/macroprudential-policy

Global developments and risks





Domestic developments and risks

Improved sentiment after the formation of the GNU

Figure 4: South African versus emerging market sovereign bond spreads in 2024

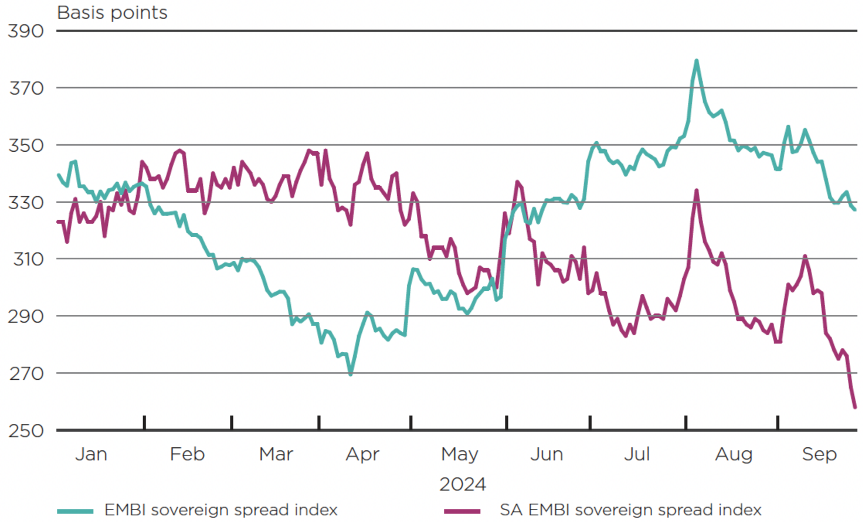
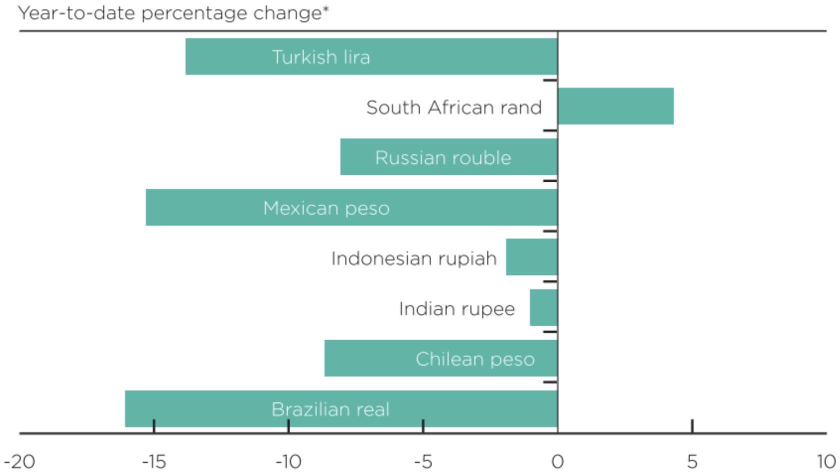
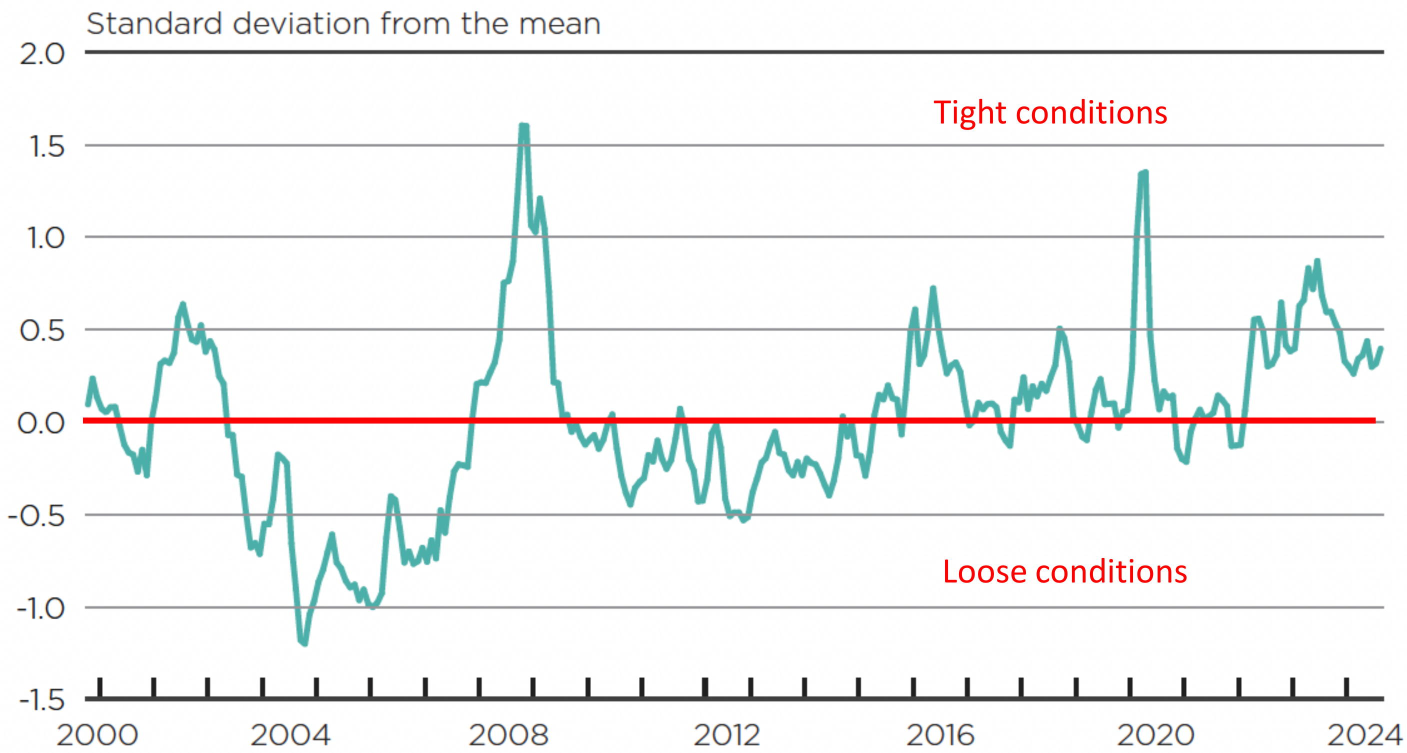


Figure 7: Performance of selected EM currencies against the US dollar in 2024

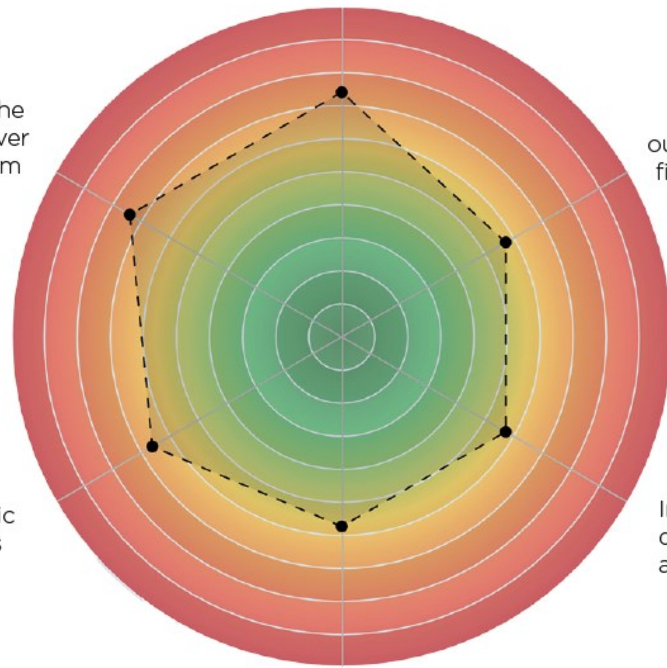


* From 1 January 2024 to 15 November 2024

Financial conditions remain tight



Key financial stability risks



Residual risk = Risk + Amplifiers - Mitigants

(The risk of ...)

Escalating global conflicts

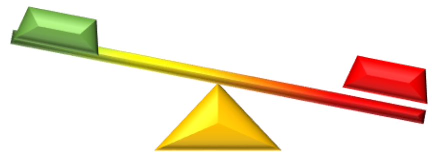
- Flight to safety, market volatility, capital outflows, currency depreciation
- Trade bottlenecks and rising commodity prices could reignite inflation and slow the decline in global interest rates
- Economic impact of trade restrictions, nearshoring and friendshoring
- Reduced access to and higher cost of foreign funding
- Increased risk of cyber attacks

(The risk of ...)

Deteriorating public sector debt ratios

Potential transmission channels to financial stability:

Market risk, liquidity risk, credit risk and concentration risk



Mitigants:

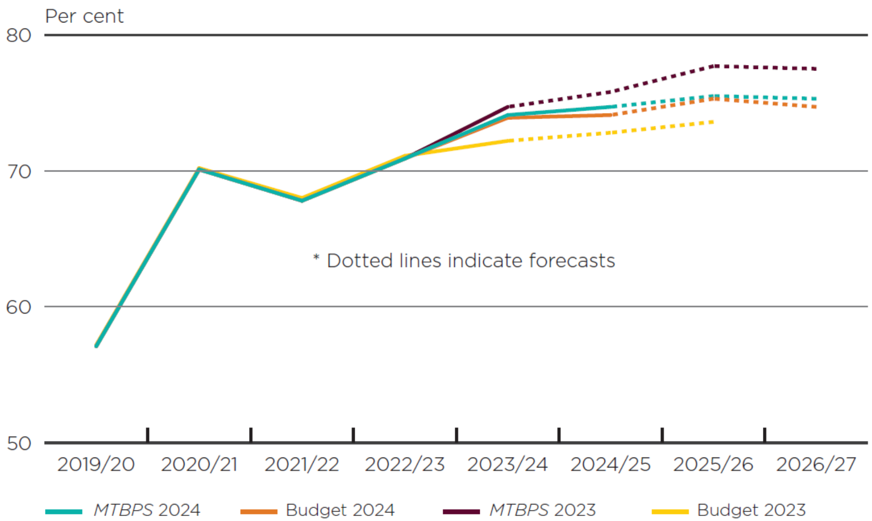
- First primary fiscal surplus since 2009
- Reduced funding needs (GFECRA, tax revenues from initial two-pot withdrawals)
- Lower yields on improved sentiment
- Declining policy rates

Amplifiers:

- Growing debt levels as debt
- Above inflation wage increases
- Weak SOEs
- High and rising exposure of financial sector to government debt
- No capital required against government debt exposures for banks on the standardised approach
- Possible overvaluations

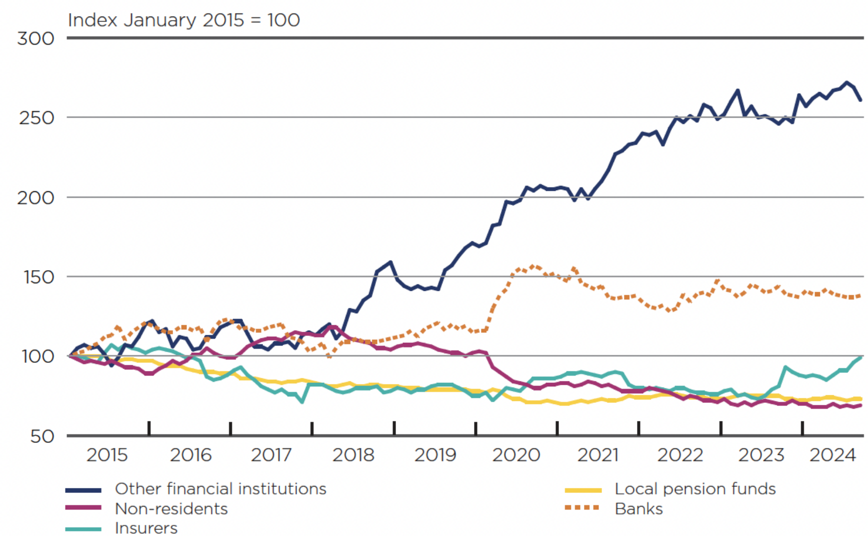
Financial sector remains the main funder of government

Figure 10: Government debt-to-GDP ratio*



Source: National Treasury

Figure 13: Holdings of SAGBs

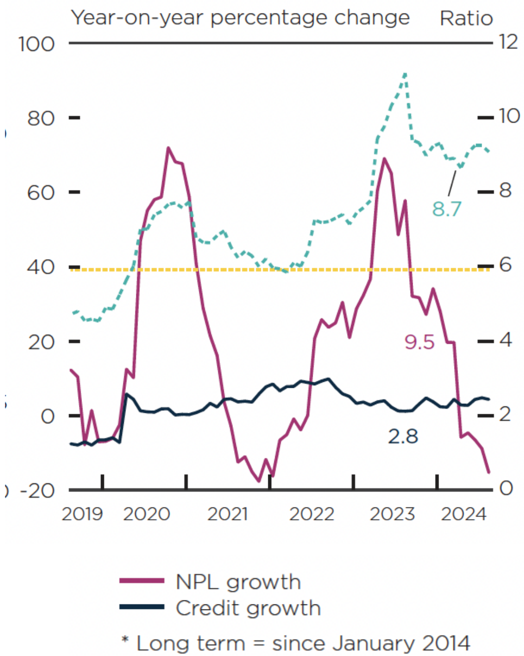


SOUTH AFRICAN RESERVE BANK

(The risk of ...)

Increased financial distress in households and SMEs

SME (retail and corporate)



Retail unsecured

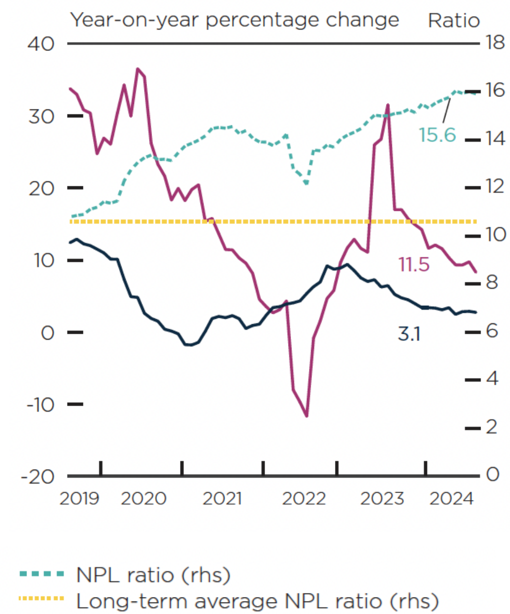
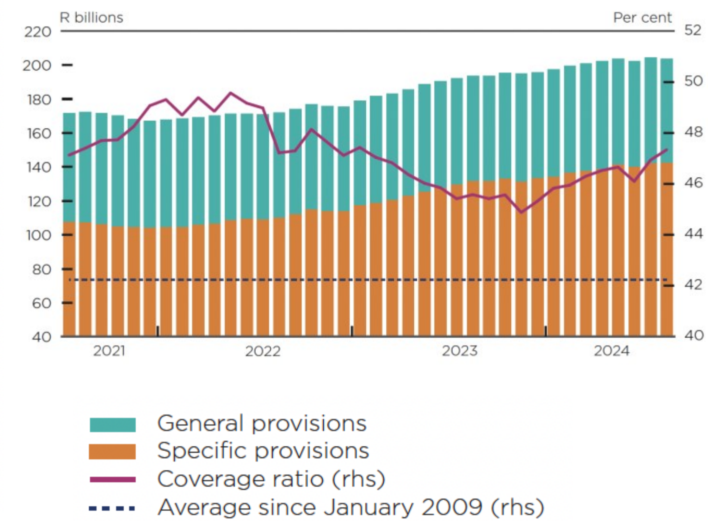


Figure 21: Bank provisions and coverage ratio

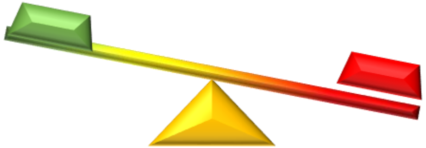


(The risk of ...)

Rapid capital outflows amid declining financial market depth

<u>Potential transmission channels :</u>

Severe exchange rate depreciation, valuation changes and market malfunctioning



Mitigators:

- Signs of improved investor sentiment towards South Africa
- Lower interest rates in advanced economies

Amplifiers:

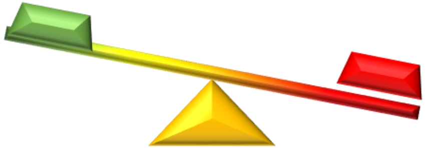
- Reduced diversification opportunities in domestic markets
- Lower market liquidity affects price discovery and valuations
- High volatility and a disproportionate impact of shocks
- Credit rating downgrades and exclusion from global indices

(The risk of ...)

Critical infrastructure failure

Potential transmission channels :

Direct (operational) and indirect (macroeconomic) impact on the financial system



Mitigants:
- Load shedding has subsided, mainly due to an increase in alternative energy sources
- Risk of a blackout has receded
- Increased focus of the Financial Sector Contingency Forum (FSCF) on business continuity, crisis preparedness and alternative connectivity

Amplifiers:
- Deterioration in other infrastructure (roads, railways, ports, water quantity and quality)
- Impact of precarious financial position and service deliver of municipalities on financial sector

(The risk of ...)

Remaining on the FATF greylist over the medium term

- 16 of 22 findings in SA Action plan now largely or fully addressed
- Six findings still to be addressed by last reporting cycle (February 2025) before the FATF Plenary session in June 2025
- If mid-2025 review does not result in a removal from the greylist, the adverse impacts will escalate:
  - Increasing compliance cost
  - Difficulty of accessing and retaining foreign counterparties
  - Higher funding costs
  - Less and more expensive hedging opportunities
  - Loss of regulatory equivalence status

Perpetual risks

- Low and inequitable growth
- The impact of climate change on the financial sector
- The risk of a cyber attack with systemic impact

Policy actions and initiatives

Initiative	Purpose
Introduce a positive neutral level of 1% for the countercyclical capital buffer (CCyB)	A positive neutral level for the CCyB gives the Reserve Bank policy space to provide to banks capital relief during a period of financial stress
Monitor the sovereign-financial sector nexus	Supervisory oversight and moral suasion; policy intervention remains an option if the risk escalates
Increase the financial sector's resilience to deal with an operational disruption with systemic impact	Financial sector can continue to provide a minimum level of payment, clearing and settlement services
Collaborate with members of the Financial Sector Oversight Committee (FSOC)	Coordinated actions among SARB, NT and financial regulators on risk mitigation
Enhance cyber-resilience in the financial sector through the FSCF	Collective and coordinated response to a systemic cyber attack in the financial sector

Briefings on selected topics

18

The economic impact of a 1% PCN CCyB

- Forthcoming working paper
- Marginal and temporary impact on credit extension and the economy
- Benefits outweigh costs

The changing composition of HQLA in South Africa

- Larger proportion central bank reserves following the introduction of the SARB's new monetary policy implementation framework in 2022

Vulnerabilities in the SA commercial real estate (CRE) sector and financial stability implications

- Pressure on CRE sector both from income and cost sides
- Structural and cyclical factors
- Available on the SARB website under financial stability

Conclusions

20

Financial stability assessment

- Financial stability prevailed over the review period despite global and idiosyncratic disruptions and risks.

- The outlook for financial stability improved since the June 2024 FSR on the back of a better fiscal outlook, decline in load shedding, lower interest rates and more optimistic investor sentiment.

- However, perpetual and structural risks remain relevant, while new risks have been added (pressure on households and SMME’s, deterioration in critical infrastructure other than electricity).

THANK YOU

SOUTH AFRICAN RESERVE BANK