



SOUTH AFRICAN RESERVE BANK

**Keynote address by Rashad Cassim,
Deputy Governor of the South African Reserve Bank,
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Monetary policy, the yield curve and financial markets

The mandate of the South African Reserve Bank (SARB) is to protect the value of the currency, and we do it for a clear reason: to support balanced and sustainable growth. These are real economy considerations that firms and households can readily understand and support. At the same time, we pay a lot of attention to financial markets, as it is fundamentally through financial markets that policy is transmitted. After all, the SARB is a bank and our most important tool is the interest rate. In this light, I would like to talk to you today about how we look at financial markets in our monetary policy decision-making.

Let's start with our interest rate. About midway through the second half of the 20th century, it was fashionable to make monetary policy using many different tools, such as rules for how much credit could be extended to different sectors, or what reserve requirements banks had to hold for different kinds of liabilities. This has been called the 'Baroque age' of monetary policy because of its complexity.¹ This complexity made it difficult for everyone – even central bankers – to understand the true stance of monetary policy.

¹ U Bindseil, '[Evaluating monetary policy operational frameworks](#)', 2016.

Today, we have a more elegant and simpler approach, with most central banks relying on a single interest rate tool to achieve their monetary policy goals. There are a few cases where central banks target an exchange rate, and when interest rates are constrained by the zero lower bound, policymakers have experimented with other tools, such as quantitative easing. But these are the exceptions. In most cases, to make monetary policy means to set an interest rate, specifically a short-term rate.

In South Africa, we used to call this the repurchase, or repo, rate. We stopped using this term in our Monetary Policy Committee (MPC) statements a couple of years ago, and formally retired it this year. Nowadays, we refer to the SARB policy rate. The reason for this is that we changed our monetary policy implementation framework in 2022, and the new system relies on the SARB taking deposits from banks, rather than forcing banks to borrow from us. There is now hardly any demand by banks for repo borrowing from the SARB, so it is misleading to say that policy is transmitted through our repo auction.

For more expert users, however, it is important to understand what that rate represents and how it works. Under the surplus system, we provide banks with excess liquidity and then we pay the policy rate when they deposit it back with us overnight. A rand deposit with the SARB is the safest and most liquid rand asset imaginable. We are never going to default on rand obligations, as we can create rands, and we offer maximum liquidity because we keep these deposits in the payment system itself.

Every other asset can also be scored for its safety and liquidity, but none will match a SARB deposit exactly, and many will not come close. What we want financial markets to do is arbitrage – in other words, to price everything else against this one safe overnight rate. To do this, markets must think about safety, think about liquidity, and think about the future path of the overnight rate.

For example, a government Treasury bill is also very safe, but it is not quite as liquid as a SARB deposit, and it has a lifespan of three months or more, not overnight. This helps explain why a 91-day Treasury bill has a yield of 7.26%² against a policy rate of 7% currently.

² This pricing refers to the Treasury bill auction of 15 June 2026.

Similarly, a mortgage is less safe than a SARB deposit or a Treasury bill because people can default on mortgages, and even though you can take the house back, this entails costs and risks. A 20-year mortgage is also less liquid than an overnight deposit. It follows that mortgages to households have been costing around 9–10% lately, with the spread over the policy rate compensating for the extra risks.

These examples illustrate how we can affect the whole range of asset prices by moving our policy rate, and this is why it is such a powerful tool. At the same time, there are also many other factors that can move asset prices. We spend a lot of time in our monetary policy deliberations thinking about those shifts, about what is driving them and how they interact with our policy stance.

One of the most important topics in this discussion is the bond yield curve. This curve shows the interest rates on all the different government debt instruments, from the bond maturing this year all the way to the bond maturing in 2053.

Economists typically decompose long-term yields into a path for the expected short rate, which is the return you could get just for rolling over a short-dated safe asset and a term premium. The term premium then captures all the things that could happen over the life of a bond, which might require extra compensation.³

Given our control of short rates, we have an influence on the whole yield curve. We also have some influence on parts of the term premium. An important example is inflation risk: if investors feel unsure about the outlook for inflation, they will probably want higher yields to compensate. By contrast, if they see a clear and credible inflation-targeting framework, they can discount that risk and charge lower rates.

At the same time, there are many other factors affecting the term premium that are not in the domain of the central bank. For example, if government's debt trajectory is seen as unsustainable, markets will charge a risk premium. If too much debt is being issued, there could be strain on the balance sheets of the institutions that can buy it, which will also affect pricing.

³ In practice, this decomposition is central to how market developments are interpreted. If yields move because the expected policy path is shifting, that may reflect changing inflation dynamics. But if term premia move, this often reflects changes in fiscal risk, global conditions or investor sentiment.

Looking back over the decade to date, we can see the South African yield curve has changed significantly. On the one hand, the COVID-19 shock brought inflation down and we cut the policy rate to 3.5% – a record low. On the other hand, COVID-19 triggered large capital outflows from South Africa, we lost our last investment-grade credit rating and the fiscal deficit expanded dramatically, so long-term borrowing costs rose. This caused the yield curve to steepen: the long-term yield was well above the short-term yield. Indeed, based on the historical data in our *Quarterly Bulletin*, this was the steepest yield curve on record, with more than 5 percentage points between the front- and back-ends of the curve.

After COVID-19 came a global inflation surge and sharp monetary tightening. We moved the policy rate up to 8.25%. But this period also saw rising country risk and prolonged electricity load-shedding, which pushed up long rates too. The entire yield curve therefore shifted higher and remained very steep. In late 2023, for instance, 30-year rates were close to 13%, while short-term rates were around 9%, leaving the level of steepness still close to 4%. We interpreted this steep yield curve as chiefly a fiscal- and country-risk story.

More recently, South Africa experienced a remarkable turnaround. Both long and short rates fell substantially: at the start of 2026, short rates were under 7% and long rates were under 9%. Yield curve steepness compressed sharply, bringing that metric back close to its long-term average. The Middle East crisis disrupted this progress somewhat, but steepness actually moderated further, as the inflation shock pushed up short rates more than long rates.

Reflecting on these developments, it is striking how much South Africa's recent 'macro reset' has delivered. With a new inflation target, a strong fiscal commitment to stabilising debt now rather than later, plus reduced bond issuance, markets have priced in markedly lower yields on government debt. It is also striking that this has occurred despite no real growth turnaround to date.

It is hoped that we can make further progress. Anchoring inflation expectations close to 3% will allow us to set lower short-term rates, probably closer to 6% than 7%. Meanwhile, ongoing fiscal and structural reforms would justify more credit rating upgrades, such as those we have seen recently from both S&P and Fitch, and improve

demand for our bonds. We have already achieved a flatter and lower yield curve, and we should strive for further gains.

This phase of easing bond yields has broadly coincided with a stronger performance of South African assets more generally. You will all know how the JSE has gained, with the simple All-Share Index up nearly 60% from 2023.⁴ The exchange rate of the rand has also strengthened: back in 2023 we nearly reached R20 to the dollar, but the currency has since been closer to R16 to the dollar. Like various other emerging markets, we started seeing stronger capital flows, supported by investors looking to diversify away from the United States dollar. We also benefited from stronger terms of trade, mainly because of higher prices for gold and platinum group metals.

In our monetary policy setting, we do not target asset prices or the exchange rate. Instead, we think about how they affect our policy objectives.⁵ For instance, higher equity prices increase household wealth and ease financial conditions for firms, which supports consumption and investment. In turn, this feeds through to growth and inflation. However, the impact of asset prices on consumption is modest relative to changes in household disposable income.

During last year and early this year, our assessment was that financial conditions were broadly easing.⁶ This made it easier for us to proceed cautiously with rate cuts: we could move in increments of 25 basis points, and not at every meeting, reassured that the economy was also being supported by looser financial conditions. Fortunately, this cautious approach meant policy was not too far from where it needed to be when the latest Middle East crisis broke out in late February.

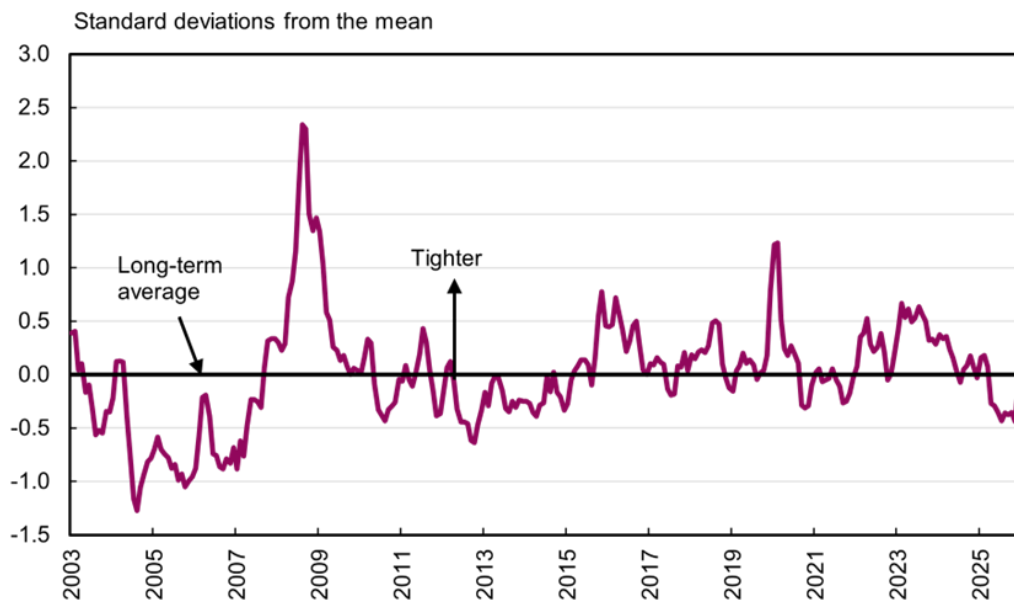
That shock generated a sharp tightening in financial conditions. At the same time, it only moved conditions from being somewhat easy to broadly neutral. In other words, financial conditions tightened but did not become tight. From a monetary policy perspective, it made a difference that markets immediately priced out all the interest

⁴ In SARB models, a 10% shock on the All-Share Index (lasting four quarters) results in household consumption increasing by an average of only 0.12% over the first year. Therefore, the approximately 23% increase that the All-Share Index experienced in 2025 would have contributed a modest 0.27 percentage points to the annual household consumption growth rate of 3.56%.

⁵ B Bernanke and M Gertler, '[Should central banks respond to movements in asset prices?](#)', *American Economic Review* 91(2), 2001, pp 252–257.

⁶ For more information on how these variables are derived, see SARB, '[Constructing a Financial Conditions Index for South Africa](#)', November 2024.

rate cuts that had previously been priced in. As a result, the short end of the yield curve shifted up, without us doing anything.⁷ This shift in financial conditions once again supported a cautious approach to policy, with rates left unchanged in March 2026 and then increased by a modest 25 basis points in May.



What all this implies is that our monetary policy stance has to be seen in the context of what happens in financial markets and how financial conditions affect credit availability and aggregate demand in the economy.

To conclude, as policymakers we are in quite a fortunate position, given that we work with a relatively large and sophisticated financial system and we have efficient passthrough. When we move our interest rate, borrowing costs change across the economy. Indeed, even the expectation of a change can drive widespread repricing. We therefore need to monitor market changes closely so that we understand what is driving the shifts and how they affect the monetary policy outlook. In turn, we can be confident that we have the tools to deliver on our constitutional mandate, which is to protect the value of the currency.

Thank you.

⁷ This illustrates how financial markets can transmit policy impulses ahead of MPC decisions.