Reforming monetary policy implementation in South Africa

Standard Bank-SARB webinar

Dr David Fowkes

9 June 2022

SOUTH AFRICAN RESERVE BANK

Overview

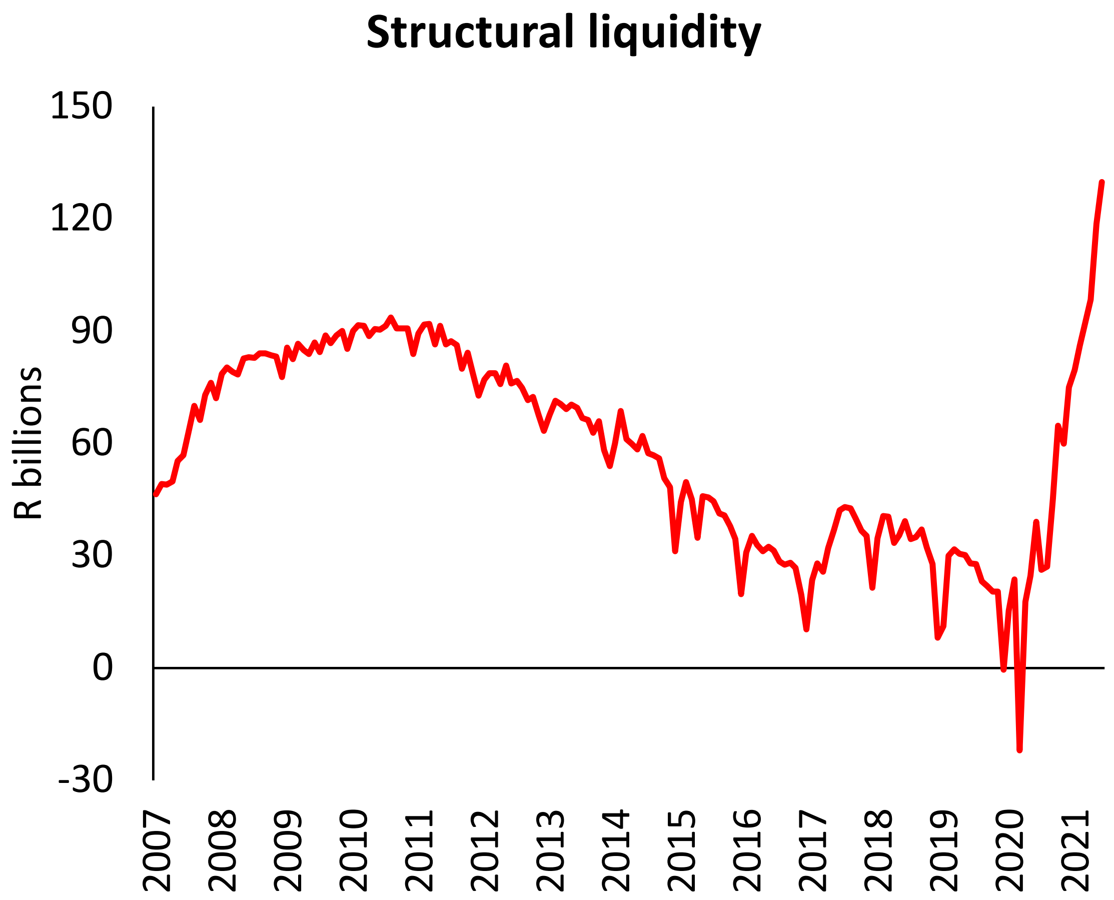
- Introduction to the new framework
  - What is a tiered floor?
  - Why makes this change?
  - Why tiers?
- Transition plan
- Implications
  - Financial markets
  - Non-bank financial institutions

Overview of a tiered floor

- A surplus not a shortage
- Abundant liquidity pushes rates down…
- But paying interest on reserves at repo puts a floor under rates
- Banks face quotas on deposits to keep the interbank market alive

Short overview of the reform rationale (1)

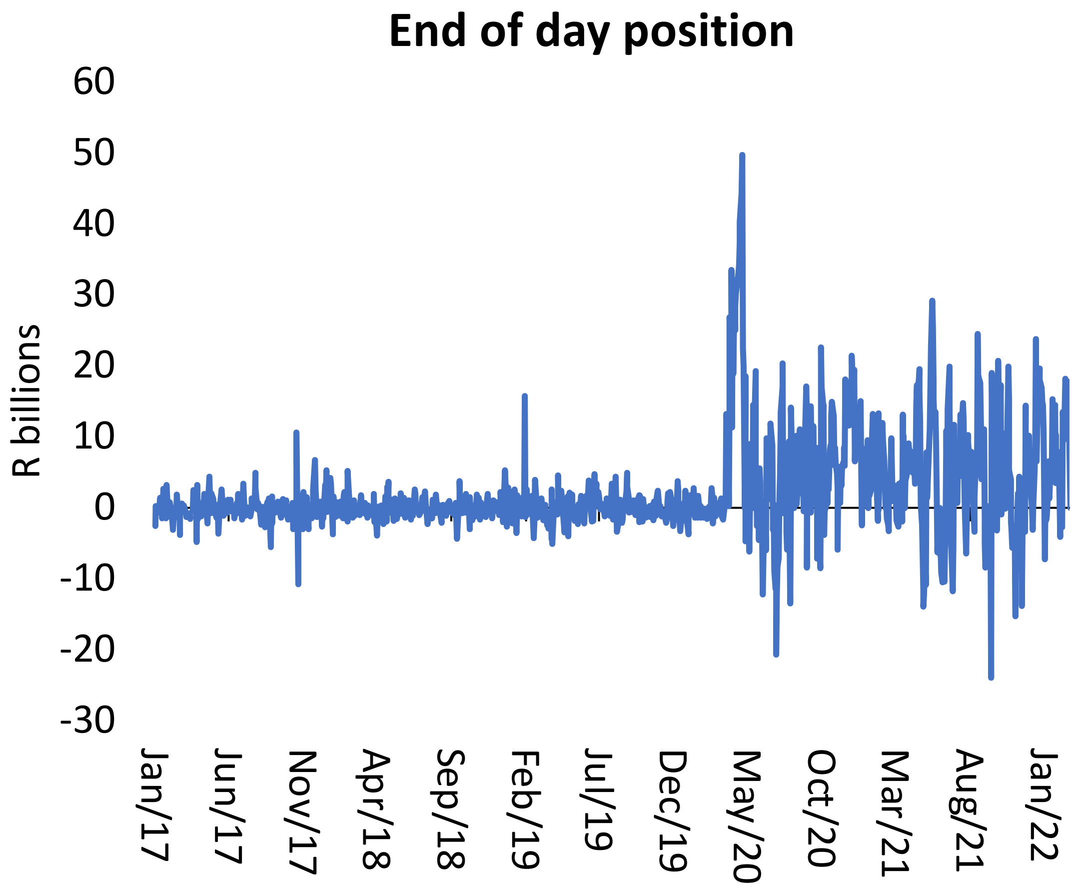
- The interest-on-reserves tool is a superior technology for controlling interest rates in the context of a structural liquidity surplus (more resilient to future liquidity shocks, less distortionary, cheaper)



SOUTH AFRICAN RESERVE BANK

Short overview of the reform rationale (2)

- Better flexibility to conduct balance sheet policies, if needed
- Better fit with regulatory developments, weakened interbank market
- Simpler and cheaper for users



South African Reserve Bank

Why quotas?

- Pure floors work with super-abundant liquidity
- But with merely ample liquidity, much of the supply can become stuck in a subset of banks (why lend when you can just deposit with the central bank at no penalty?)
- This leaves other banks short, and so they bid up rates to extract funds from surplus banks
- The central bank reacts to high rates by injecting more liquidity
- This forces a persistent balance sheet expansion (the ‘ratchet effect’)

Quotas + quota design rules will be public

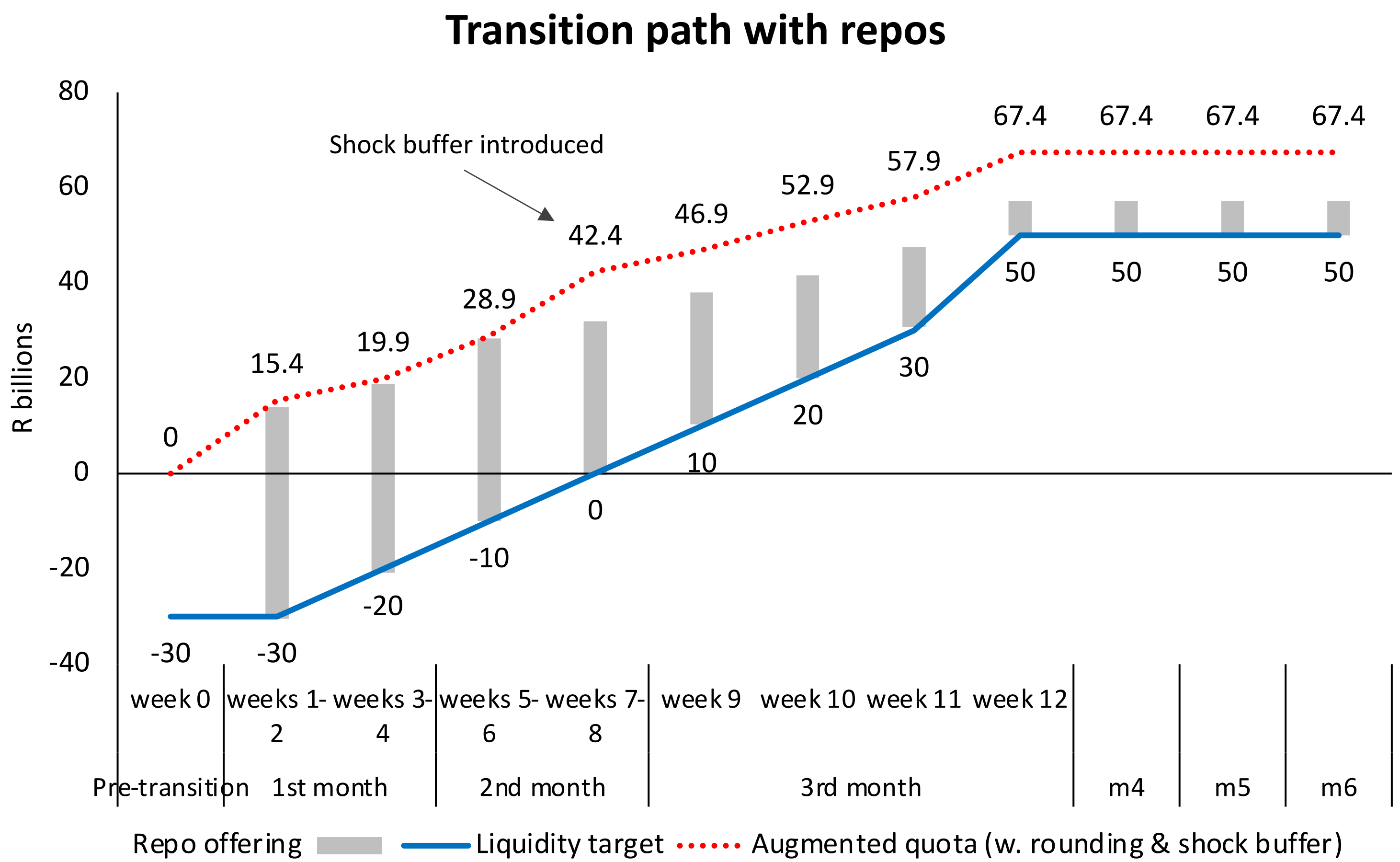
All rand millions **Bank**	Liquidity target plus shock buffer **Raw share of liabilities**	50 000 60 000 **Bank quotas**	100 000 110 000 **Bank quotas**	Rounding principle
STANDARD BANK OF SA	24.653%	15 000	28 000	Large banks, >10% of total liabilities. Round to nearest R1 billion
FIRSTRAND BANK	21.658%	13 000	24 000	
ABSA BANK	20.315%	13 000	23 000	
NEDBANK	16.806%	11 000	19 000	
INVESTEC BANK	7.678%	5 000	8 500	Medium banks, 0.2-10% of total liabilities. Round to nearest R500 million
CAPITEC BANK	2.333%	1 500	3 000	
CITIBANK	1.223%	1 000	1 500	
HSBC BANK - JHB	1.082%	1 000	1 500	
JPMORGAN CHASE BANK - JHB	0.837%	1 000	1 000	
STANDARD CHARTERED BANK	0.646%	500	1 000	
CHINA CONSTRUCTION BANK - JHB	0.537%	500	1 000	
BANK OF CHINA - JHB	0.493%	500	1 000	
AFRICAN BANK	0.282%	500	500	
GRINDROD BANK	0.201%	500	500	
BNP PARIBAS SOUTH AFRICA	0.199%	500	500	
DISCOVERY BANK	0.175%	500	500	
BIDVEST BANK	0.148%	200	200	Small banks, <0.2% of total liabilities. Round to nearest R200 million
SASFIN BANK	0.143%	200	200	
ALBARAKA BANK	0.128%	200	200	
STATE BANK OF INDIA	0.115%	200	200	
HBZ BANK	0.115%	200	200	
UBANK L	0.079%	200	200	
ACCESS BANK	0.069%	200	200	
TYME BANK	0.049%	200	200	
HABIB OVERSEAS BANK	0.015%	200	200	
FINBOND MUTUAL BANK	0.015%	200	200	
ICICI BANK	0.004%	200	200	
BANK ZERO	0.001%	200	200	
VBS MUTUAL BANK	0.000%	0	0	Inactive, 0% of all liabilities
Total Quota	**100.0%**	**67 400**	**116 900**	

Transition plans

- Gradual transition, 12 weeks – slow enough to familiarize users with new system & deal with technical problems, fast enough to avoid a long period without a meaningful shortage or surplus

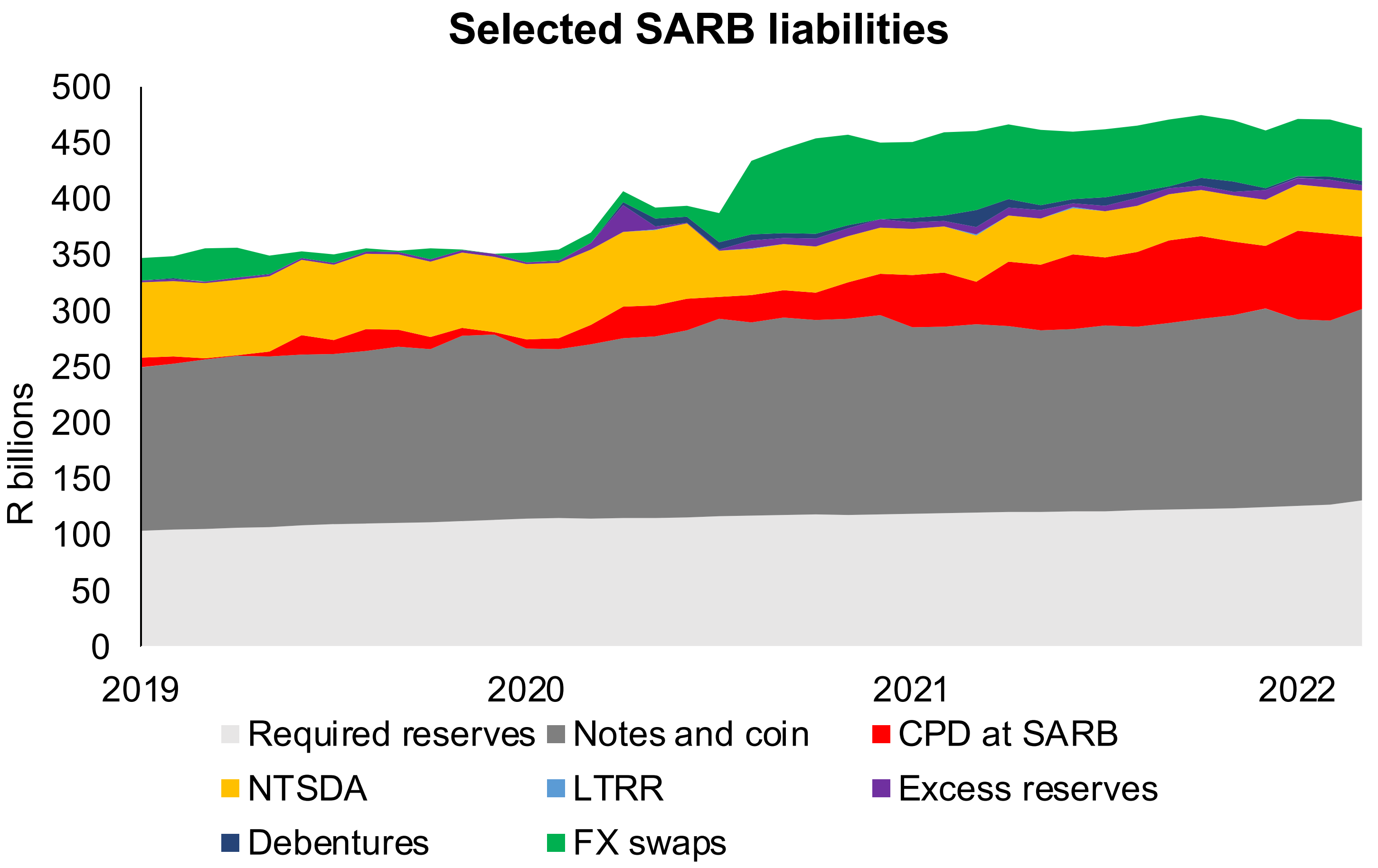
8 June	Start of transition, introduction of quotas, everything else unchanged	2 weeks
22 June	First reduction of the shortage, to R20bn	2 weeks
6 July	Second reduction of the shortage, to R10bn	2 weeks
20 July	Elimination of the shortage	2 weeks
3 August	Surplus of R10bn	1 week
10 August	Surplus of R20bn	1 week
17 August	Surplus of R30bn	1 week
24 August	Surplus of R50bn	1 week

Transition concept:
phase in quotas at low levels to start, maintain a shortage, use repos to fill the gap



SOUTH AFRICAN RESERVE BANK

New excess reserves will come from maturing existing liabilities



SOUTH AFRICAN RESERVE BANK

Market implications

- Not meant to change the monetary policy stance
- We expect somewhat better transmission of repo decisions
  - Smaller distortions in the forward market
  - Easier to do arbitrage – less liquidity scarcity
- Fundamental theory of transmission: would you rather hold money? Or use your money to buy something else? Assets trade until everyone is happy with their portfolio, given the interest rate

Implications for non-banks

- Interesting global debate on non-bank access to central bank lending during crises
- We are not offering such access currently
- In the next crisis, banks will have ample liquidity to start…
- And the SARB will have a powerful tool for injecting more, if needed
- But does it get through, appropriately?

Conclusions

- The new framework upgrades a 24-year-old system
- It gives South Africa a modern, resilient, more efficient MPIF
- Gradual transition goal is a R50bn surplus after 12 weeks
- Near-term impacts should be modest, enhancing MP transmission

THANK YOU

SOUTH AFRICAN RESERVE BANK