

Financial stability in South Africa

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South African Reserve Bank

Overview

- Financial stability as a central bank objective
- Regulatory reform in SA
- Recent financial stability developments
 - Globally
 - Domestically
- Concluding remarks



Financial stability as a central bank objective



Expanded focus

- Traditional central bank objective: price stability
- Asian crisis (1998)
 - price stability not a sufficient condition for financial system stability
- Strong interrelationship and interdependent
- Central bank objective (implicit)
- Global financial crisis
- Explicit objective
- Expanded mandate

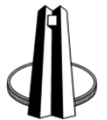


SARB's approach to financial stability

- Primary goal: “The achievement and maintenance of price stability”
- Implicit secondary objective: financial system stability
- Policies applied to prevent systemic instability
- Prudential regulation and supervision of banks
- Sound individual banks does not guarantee a stable system
- Emphasis on macroprudential analysis
- Create capacity: financial stability
- Financial stability mandate



Regulatory reform in South Africa



Regulatory reform and institutional arrangements in South Africa

- “A safer financial sector to serve South Africa better”
- Twin peaks approach
 - Prudential Authority
 - Market Conduct Authority
- Financial Sector Regulation Bill
 - SARB responsible for financial stability
 - Financial Stability Oversight Committee
 - Improved banking and financial crisis resolution frameworks



Framework for monitoring financial stability

- Systemically important financial institutions and markets
 - banks, non-bank financial institutions, FMIs
- Non-financial sector
 - excessive credit as indicator of buildup of systemic risk
 - households, non-financial corporates (wealth effects)
 - spillovers to banks
 - government finances
- Asset markets
 - overvalued, widely held, supported by excessive leverage
- Shadow banking
 - definition, size, risks, regulation?



Recent financial stability developments



WEF global risk report 2014

- Fiscal crises in key economies
- Structurally high unemployment
- Water crises
- Severe income disparity
- Failure of climate change mitigation and adaptation
- Greater incidence of extreme weather events
- Global governance failure
- Food crises
- Failure of a major financial institution
- Profound political and social instability

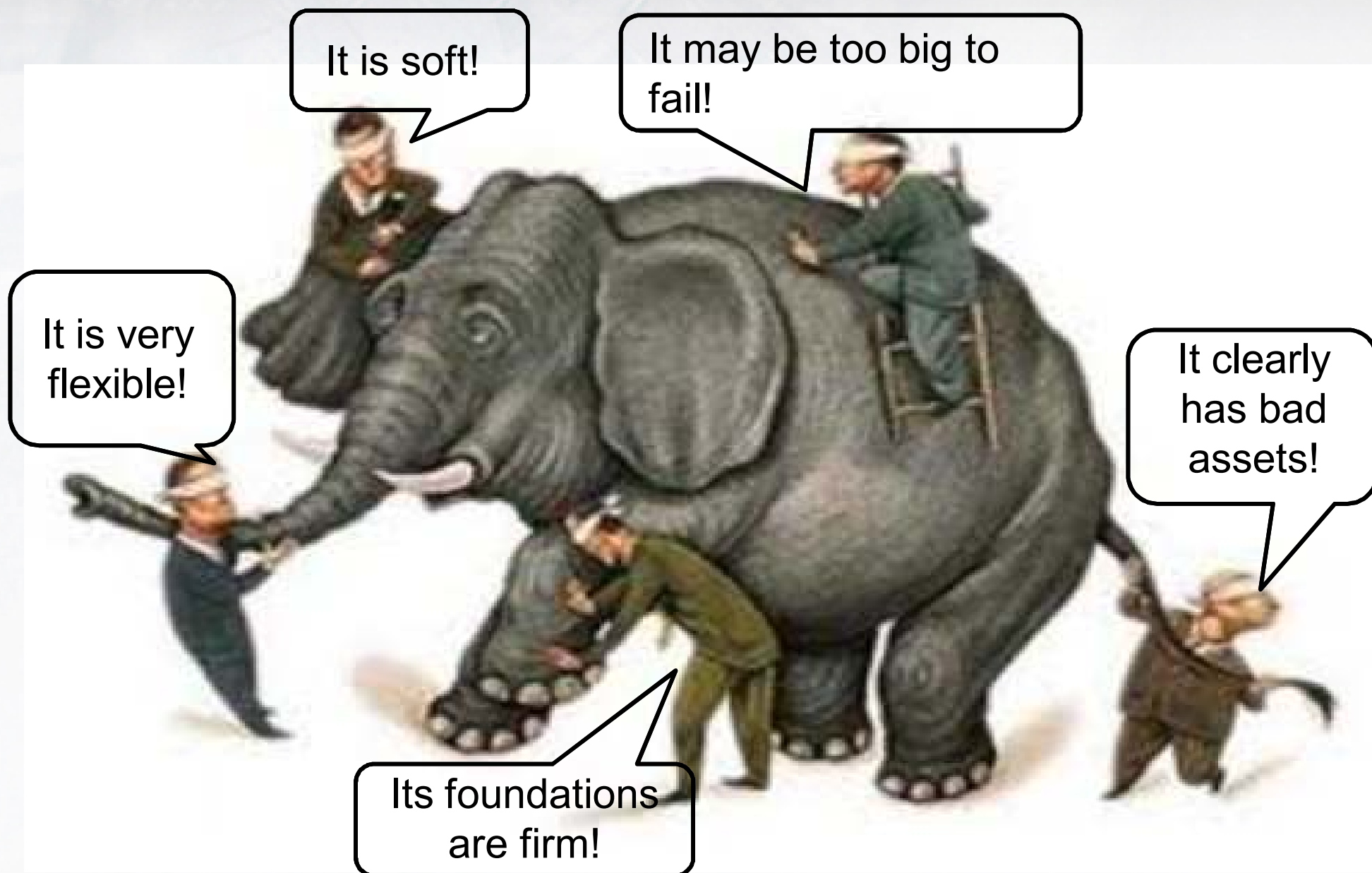


Risks to financial stability in SA

- Normalisation of monetary policy by the US Fed
- Household indebtedness
- Credit risk (unsecured lending)
- Unemployment
- Current account deficit
- Low domestic economic growth
- Mining sector contraction
- Sovereign credit rating downgrade
- Labour market disputes
- Geo-political developments



Systemic risk assessment



Risk assessment matrix

Source of main risks	Likelihood of severe realisation in the short term	Expected impact on financial stability if risk is realised
US monetary policy normalisation	High	Medium
Sovereign credit rating downgrade	Medium	High
Widening current account deficit	Medium	High
On-going labour market disputes	Medium	Medium
Low levels of growth in SA economy	Medium	High

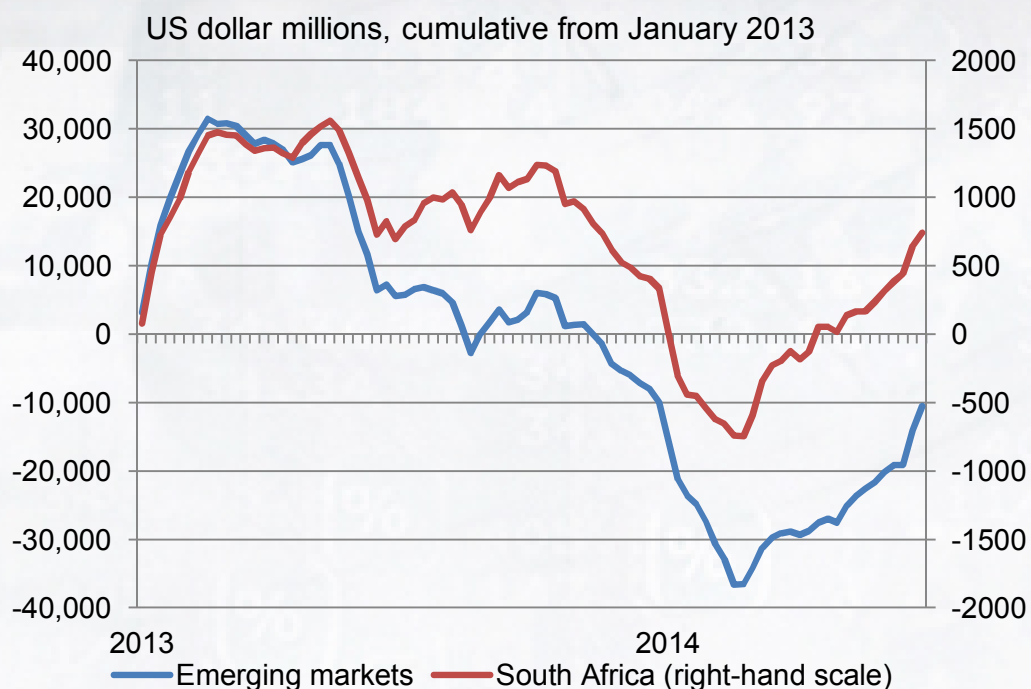


Impact of expected US monetary policy normalisation on SA

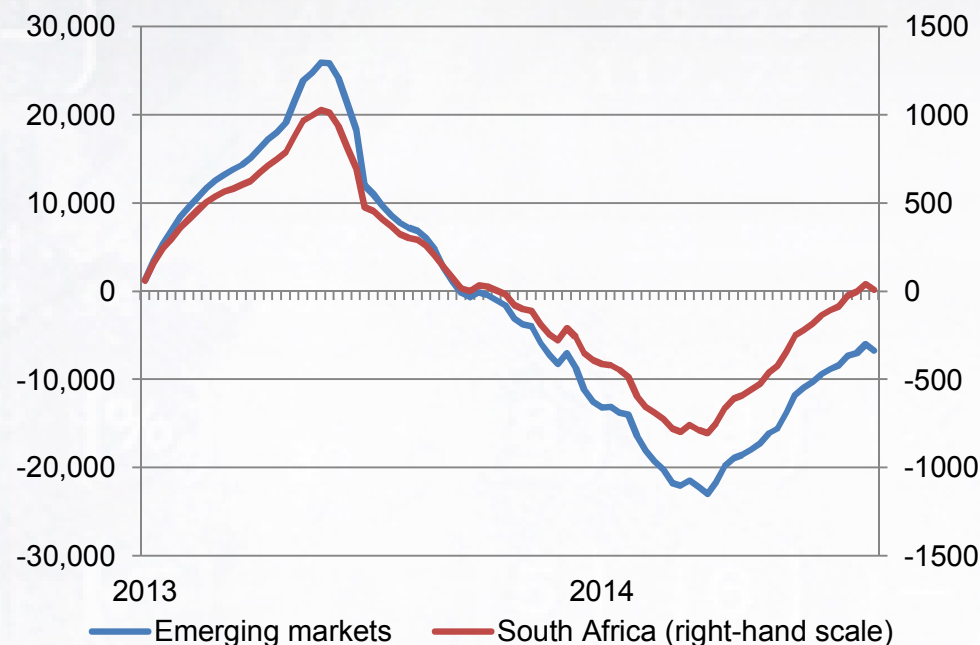


Portfolio outflows from bond and equity markets with some reversal recently...

Equity flows



Bond flows

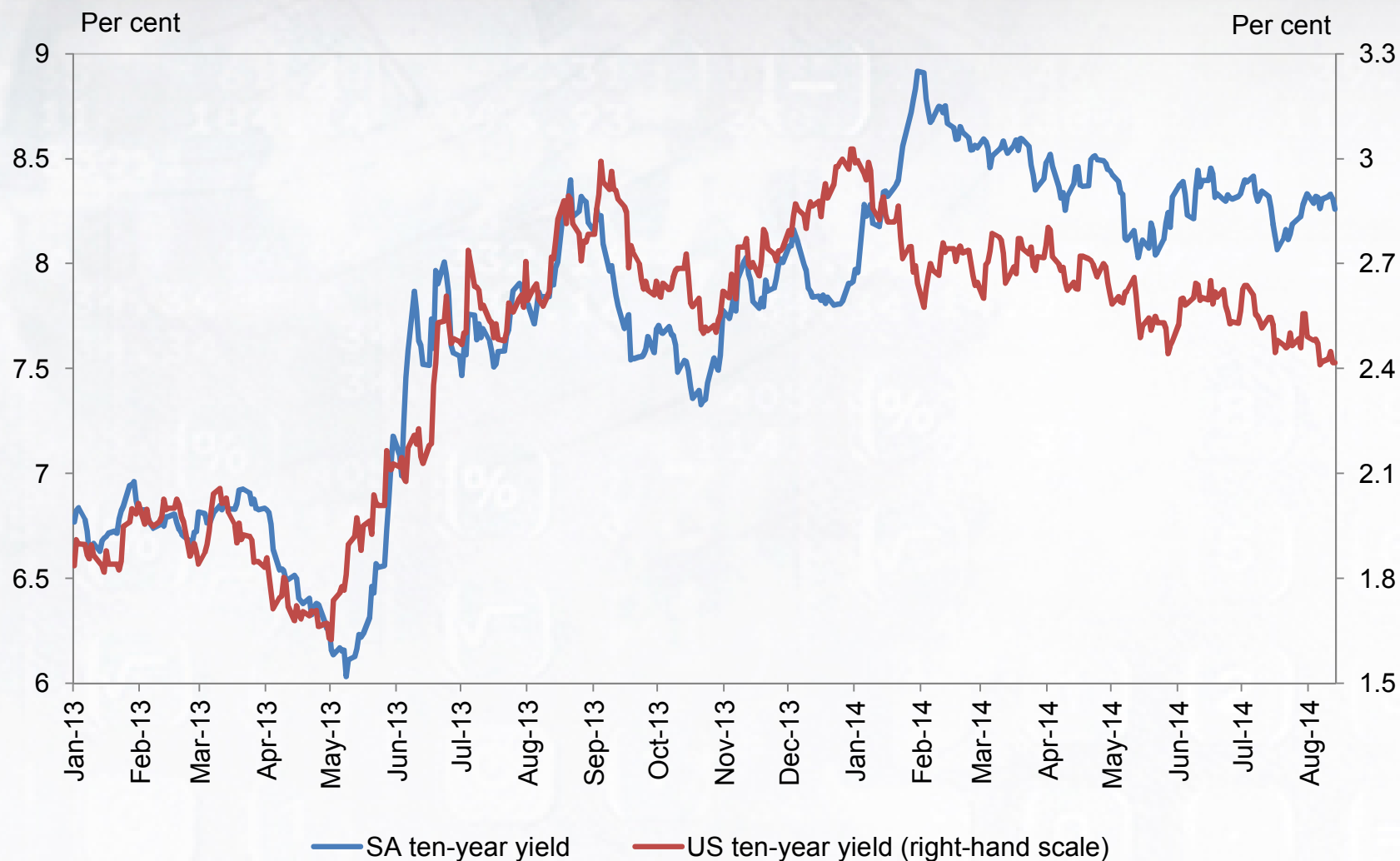


As at 13 August 2014

Non-resident transactions	Mtd (R'm)	Ytd (R'm)
Bonds	-8 022	-28 018
Equities	4 788	22 685



SA bond yields increased in close correlation with US yields...



Source: Bloomberg Finance LP



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Exchange rates against the US dollar

Indices, January 2013 = 100



Source: Bloomberg

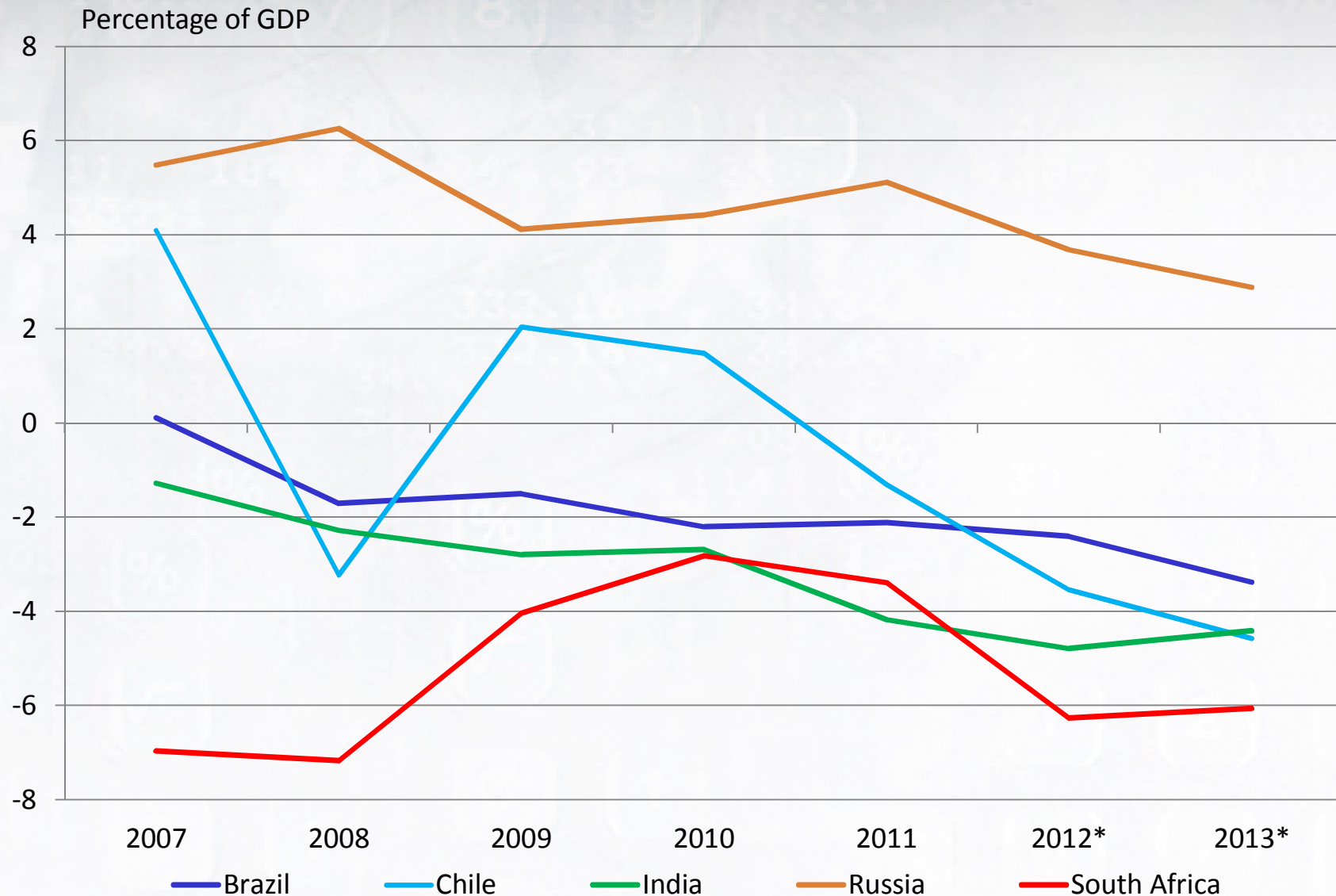


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Current account deficit



External position: Current account deficits



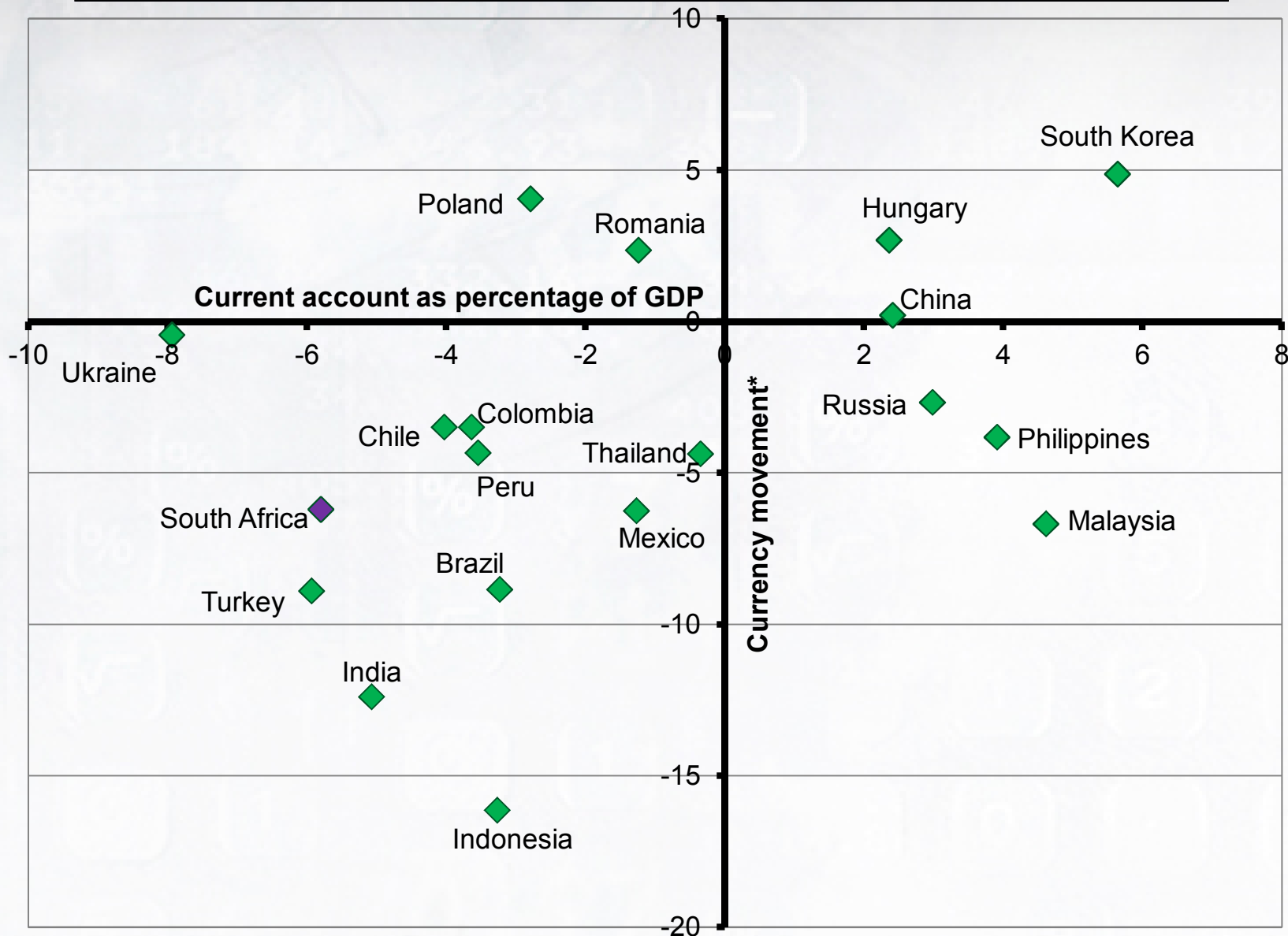
Source: IMF

* Estimates



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Current-account vulnerability a key exchange rate driver



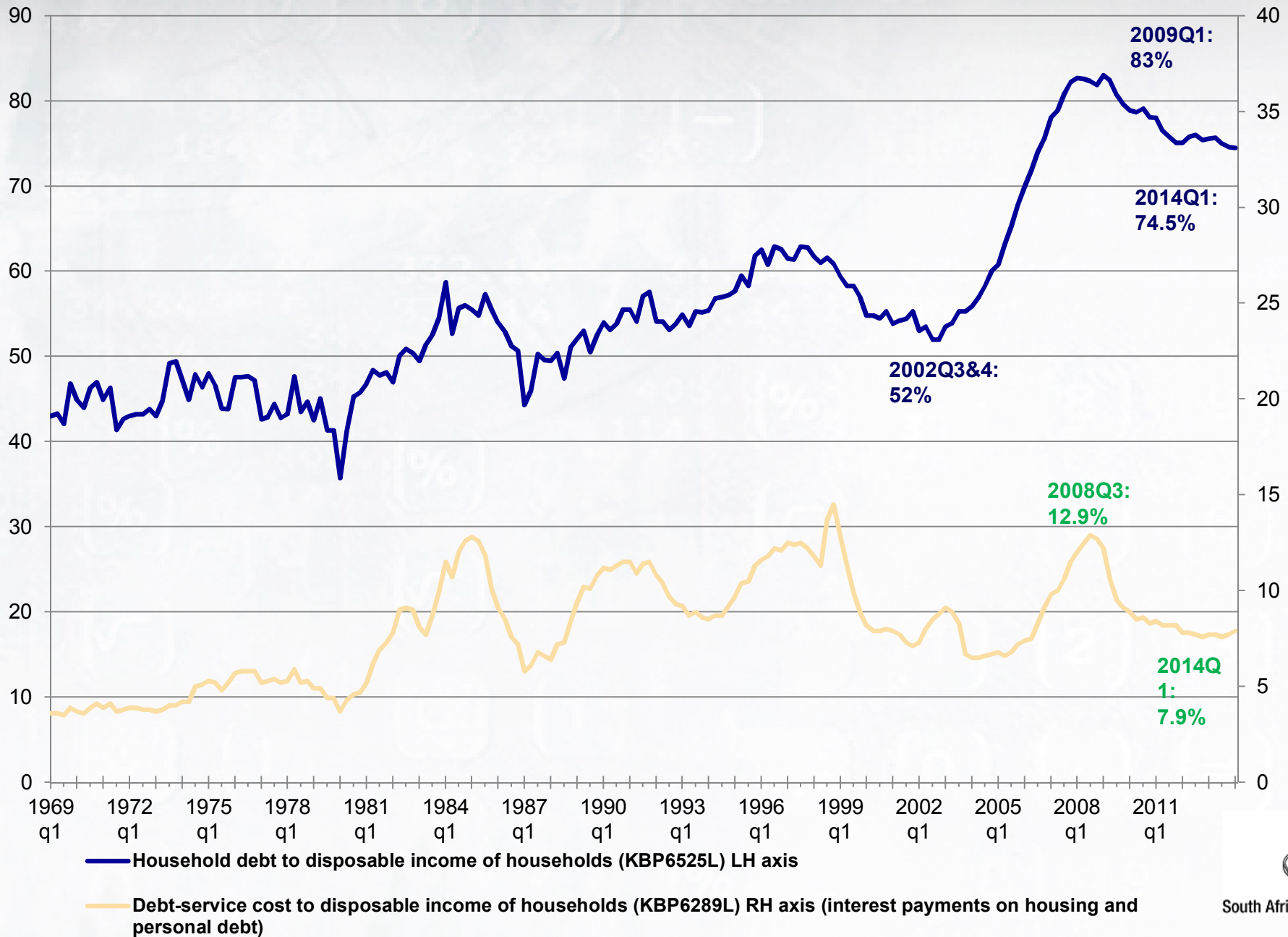
* Exchange rate movement from FOMC announcement in May – 1 October 2013. Negative indicates depreciation.

Household debt levels...

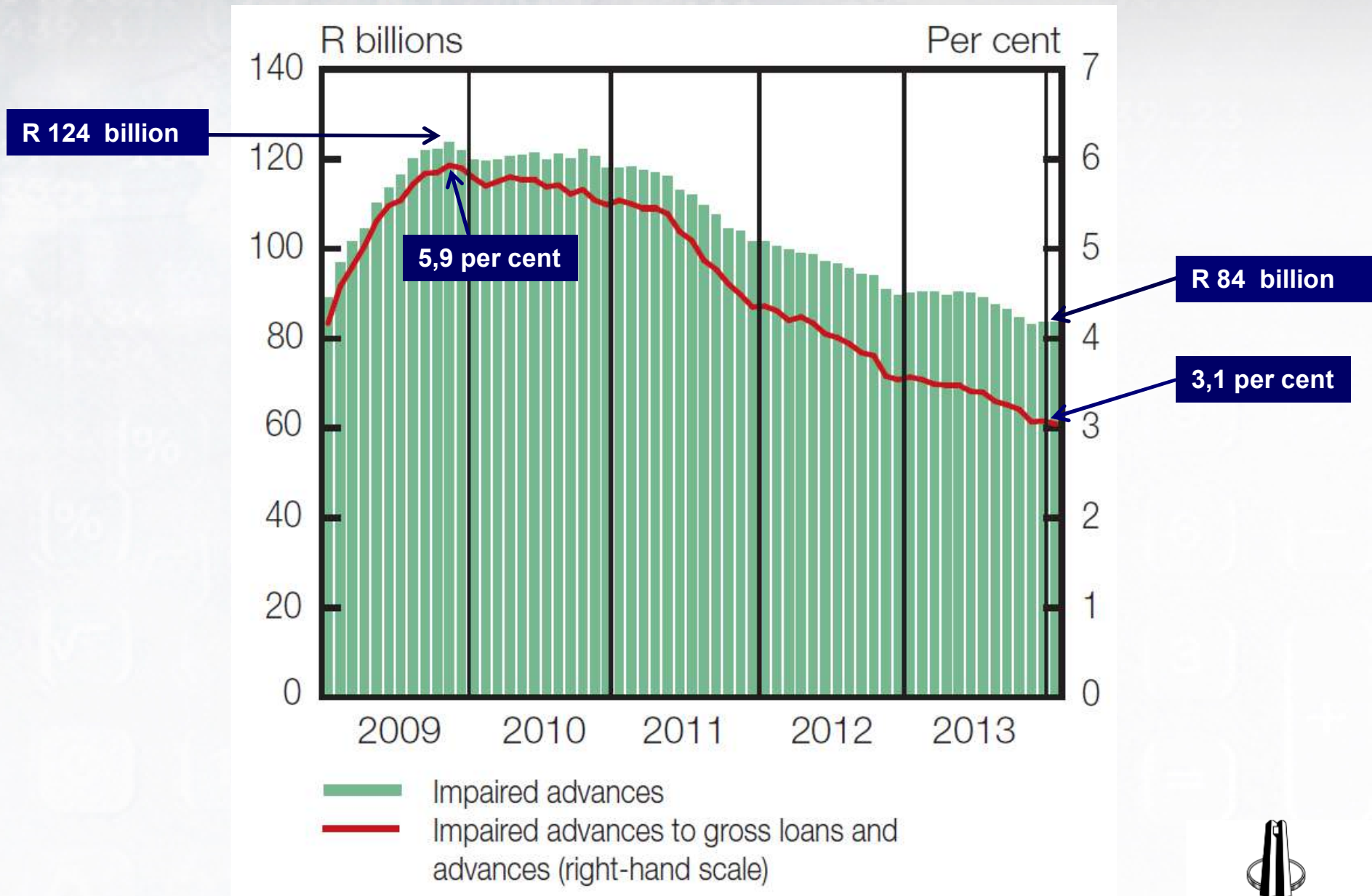
- Debt to disposable income decreasing (74,3%)
- Debt-service cost stable (7,7%), but...
 - higher cost of living
 - challenging labour markets
 - unemployment
 - servicing already high debt levels
- Impacting on loan quality at banks?



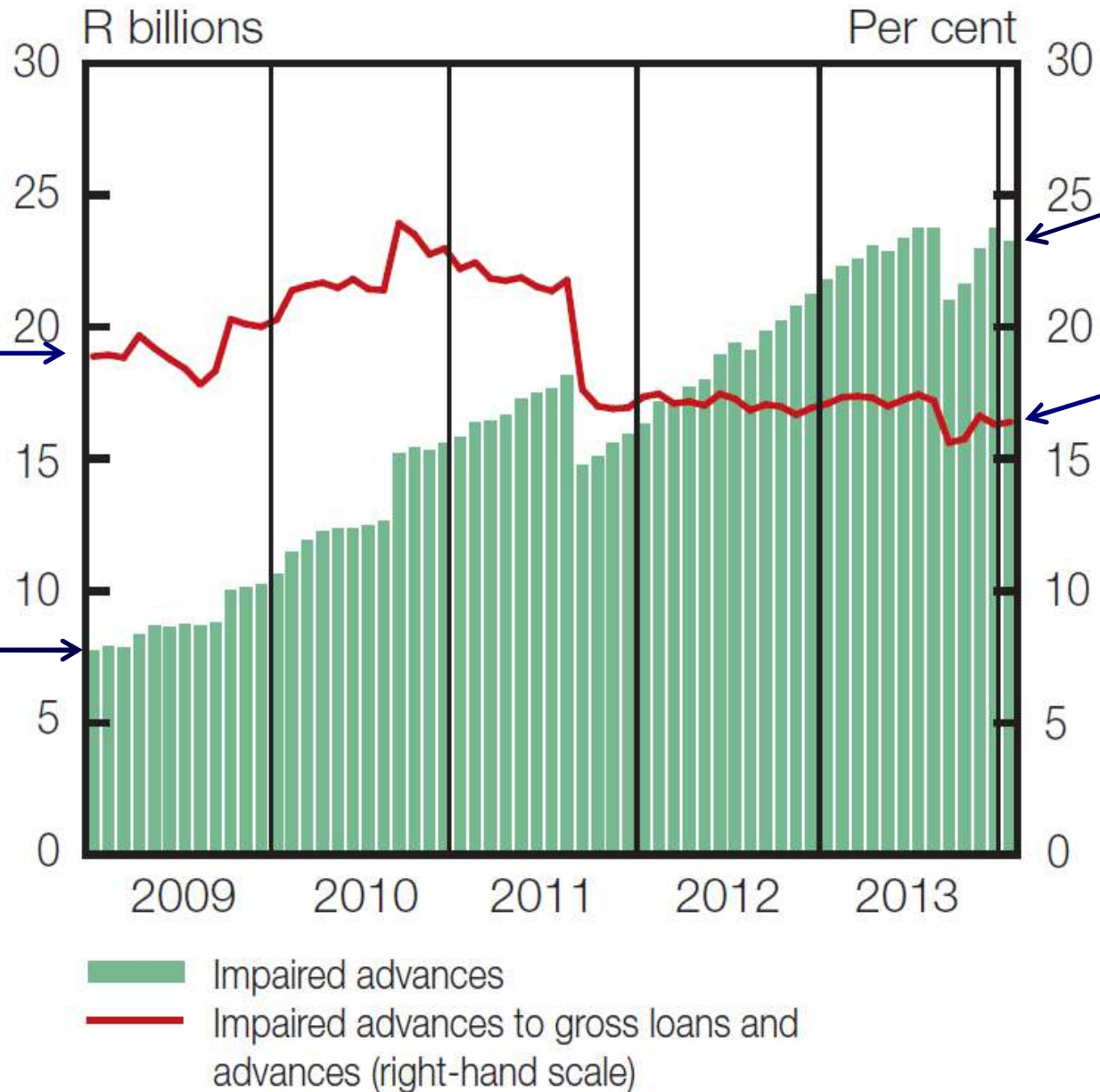
Household debt



Quality of credit at banks...impaired advances for the five largest banks



...loan quality for other banks



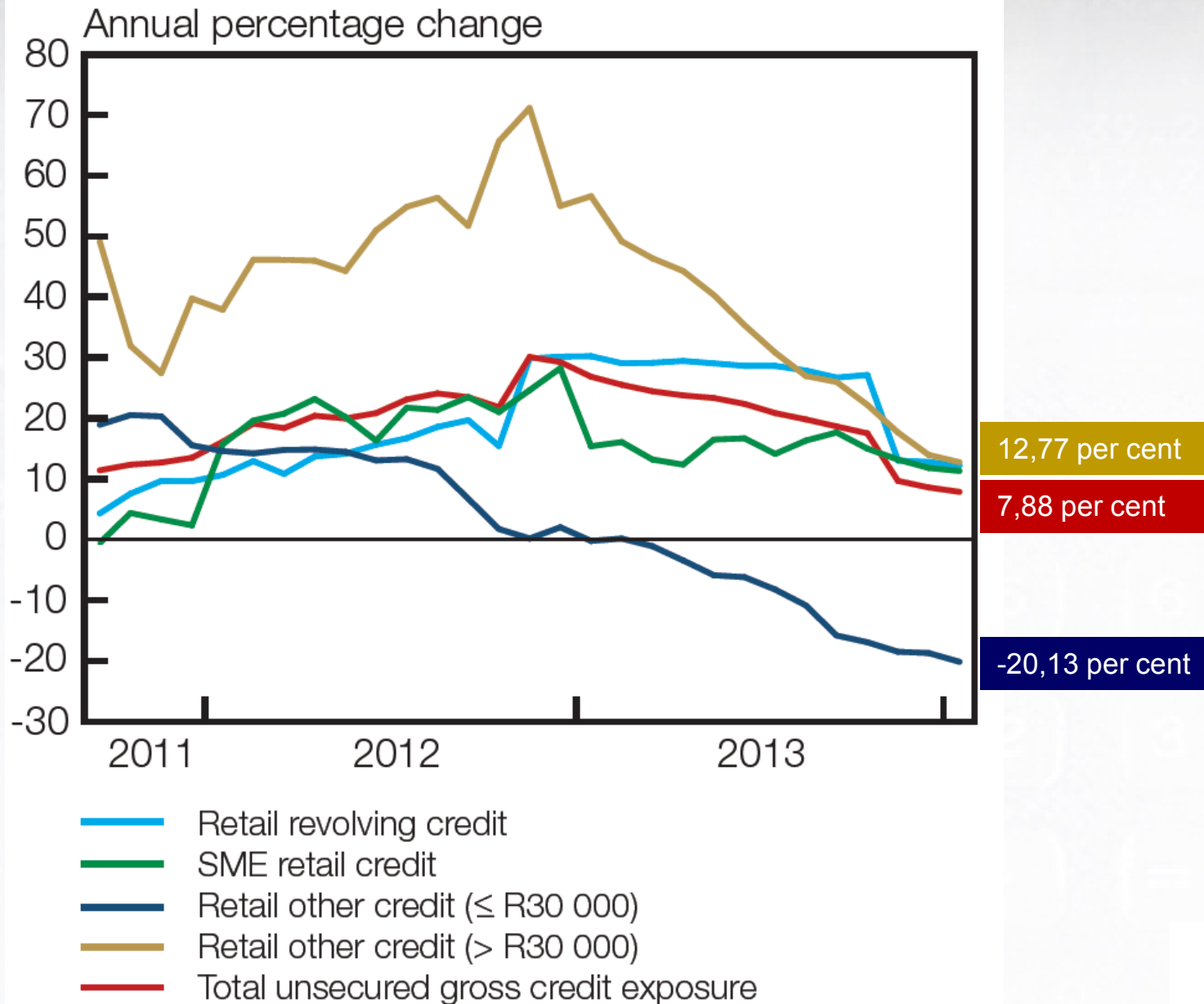
Source: South African Reserve Bank

Stress testing the financial sector

- Bottom-up stress tests done (2011/12)
- Peer review of methodology (IMF)
- Need to develop top-down approach/framework
- IMF Technical assistance programme (May 2014)
- IMF FSAP (June/July 2014)
 - comprehensive stress testing
 - main results
 - recommendations
 - further develop top-down framework
 - validate models and assumptions
 - develop macro stress test for insurance companies
 - monitoring framework to assess concentration risk of insurance sector towards large banks



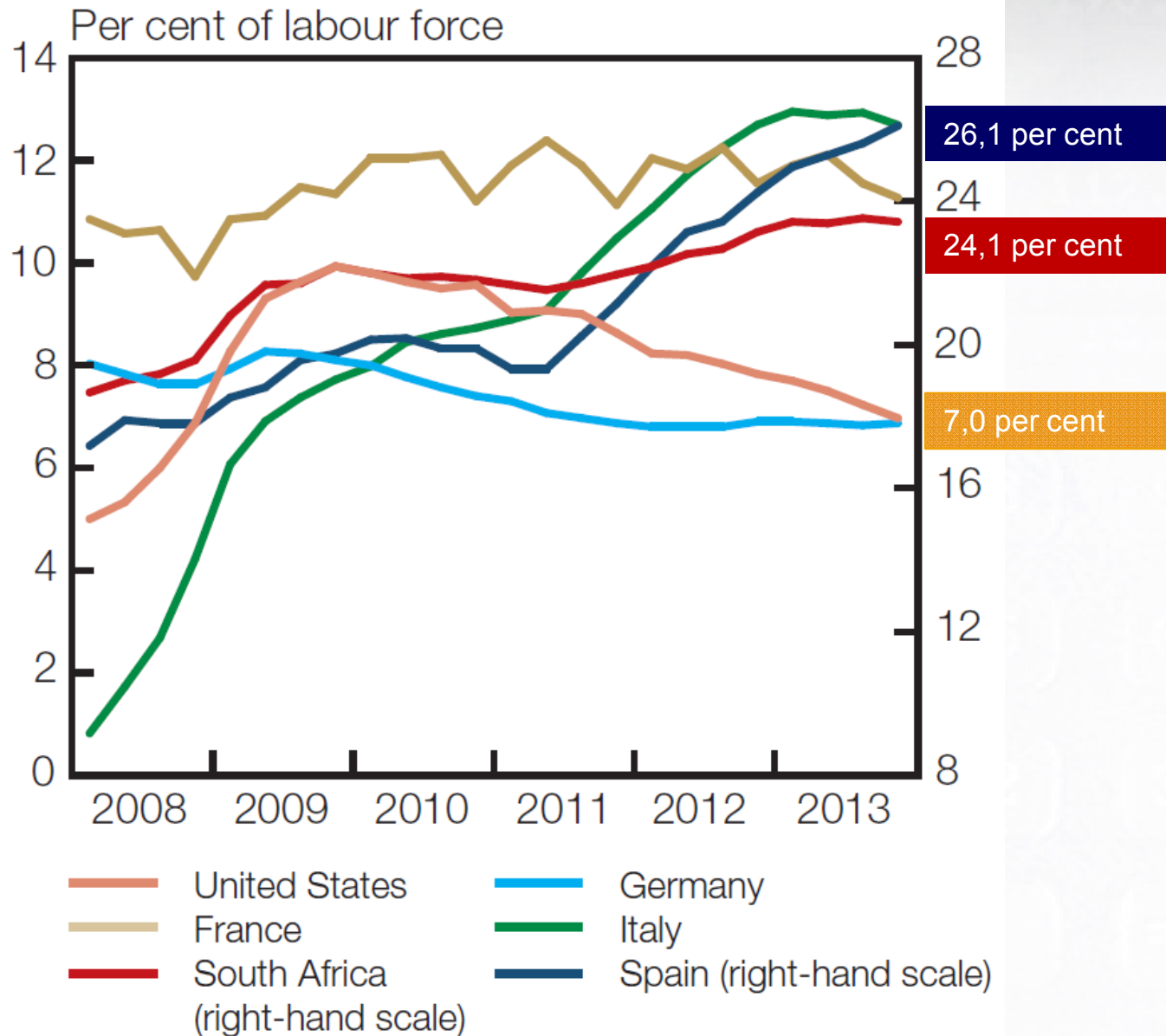
Moderation in unsecured credit exposure growth of 6 banks...



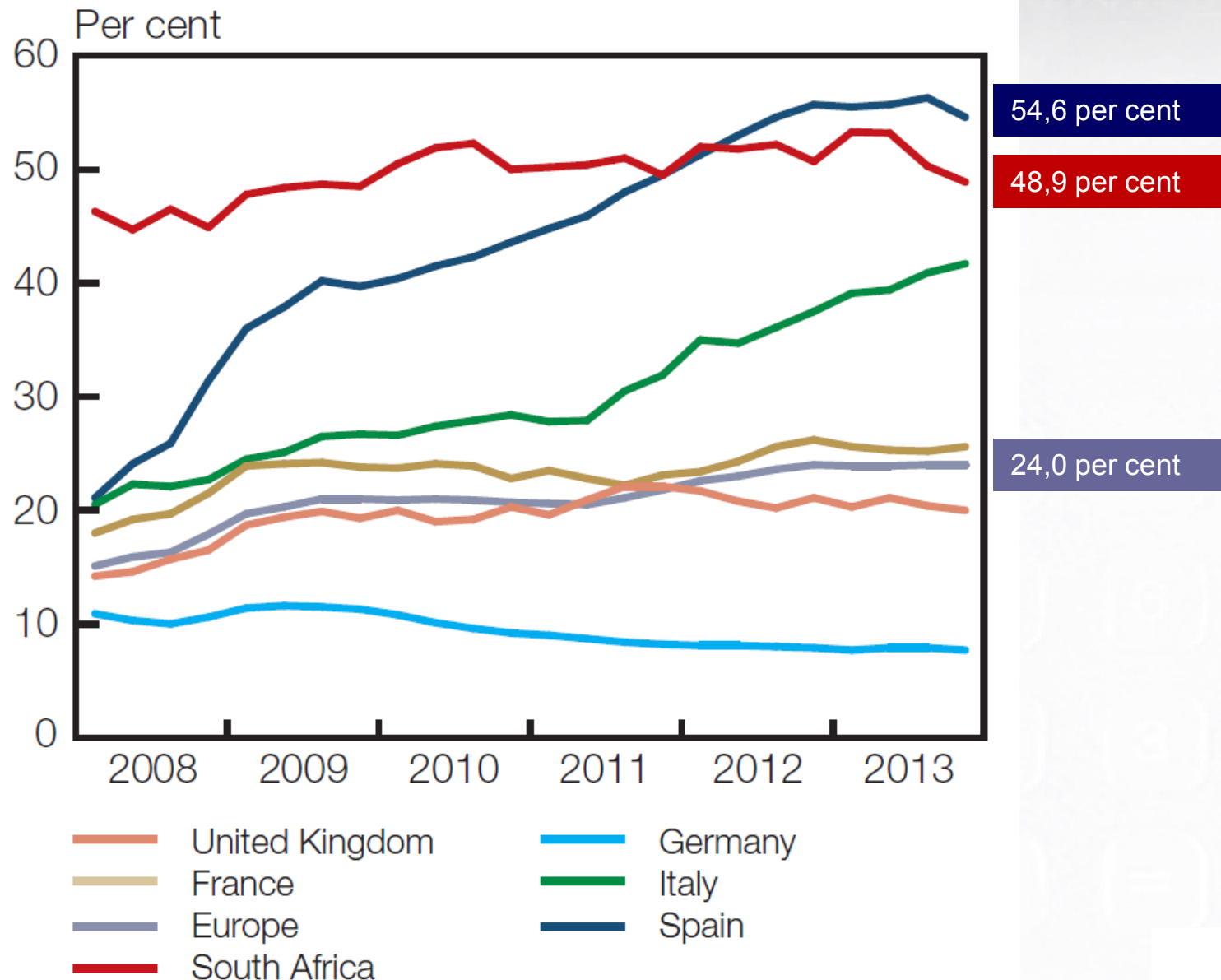
Unemployment and labour market disruptions



In the aftermath of the crisis unemployment increased globally...



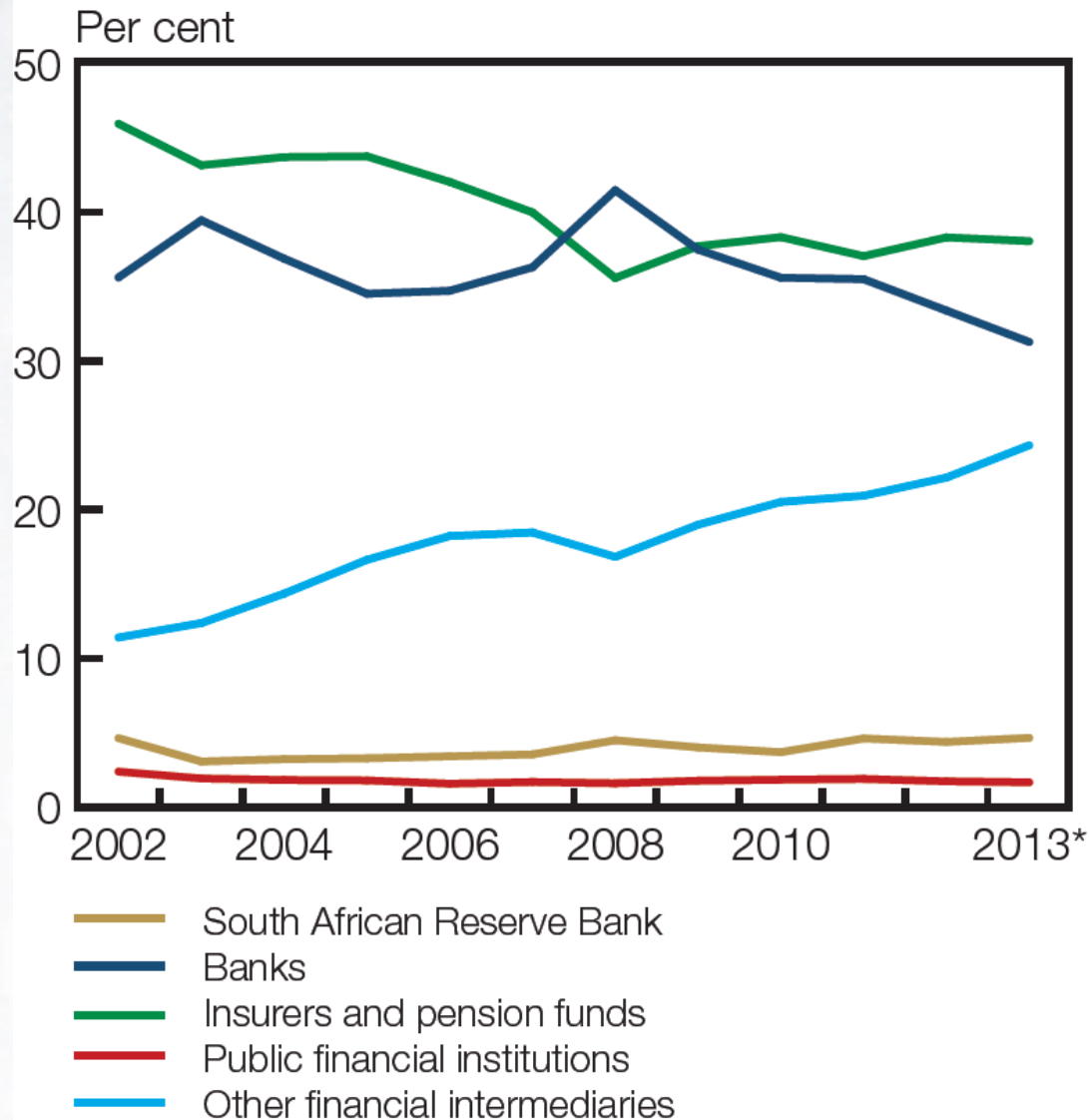
... with youth unemployment becoming a major concern in many countries



Shadow banking



Trends in the distribution of total assets between financial intermediaries in South Africa



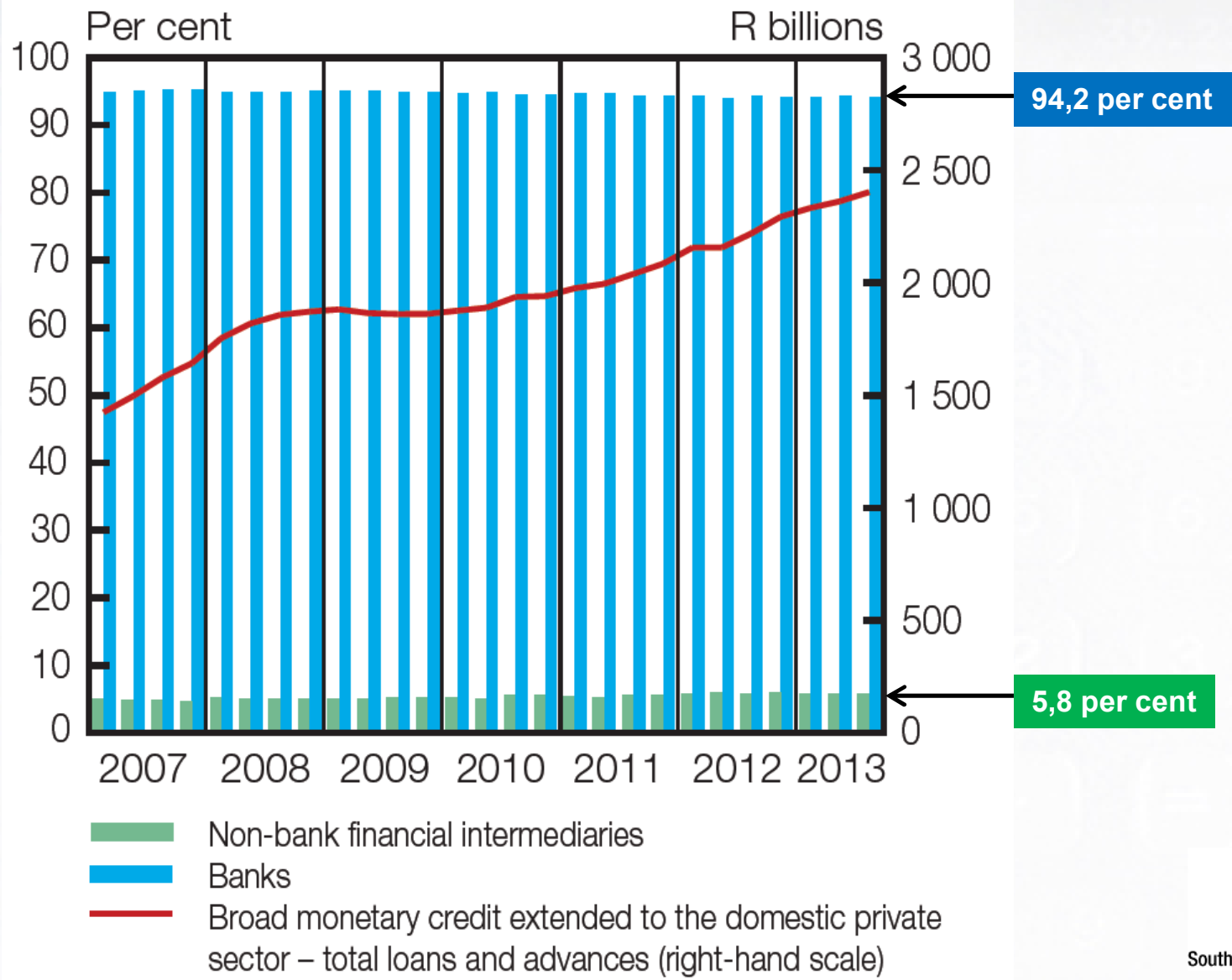
* Data for 2013 are preliminary

Sources: South African Reserve Bank and the Financial Services Board



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Credit extension by banks and non-bank financial intermediaries



Source: South African Reserve Bank

Concluding remarks

- Global financial conditions improved
- Consequences of global financial crisis still visible and impacting on SA financial system
- Some domestic financial, economic and social developments present challenges to financial system stability
- Robust financial infrastructure, open and liquid financial markets and a flexible exchange rate add to the resilience of SA financial system



The end

