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SOUTH AFRICAN RESERVE BANK

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Financial Markets Department

Record of proceedings of the Financial Markets Liaison Group meeting held via Microsoft Teams on 2 June 2022

1. Overview

1.1. The Financial Markets Liaison Group (FMLG) meeting discussed the following key issues:

1.1.1. the South African Reserve Bank's (SARB) proposed directive on the liquidity coverage ratio (LCR);

1.1.2. the risk of greylisting of South Africa by the Financial Action Task Force (FATF) and the implications thereof for the South African government bond yield curve;

1.1.3. the decline in financial markets depth and liquidity in South Africa;

1.1.4. the SARB's new Monetary Policy Implementation Framework (MPIF); and

1.1.5. progress reports from the FMLG subcommittees and the South African Foreign Exchange Committee (SAFXC).

2. Summary of discussions

2.1. The SARB's proposed directive on the LCR

2.1.1. The Prudential Authority (PA) proposed a new directive that 5.0% of the South African rand high-quality liquid assets (HQLA) should no longer be derived from foreign HQLA. Members of the FMLG reflected on the proposed directive and resolved to establish a working group which would study the economic impact of the directive.

2.2. **The risk of greylisting of South Africa by the FATF and the implications thereof for the South African government bond yield curve**

2.2.1. The FMLG noted a presentation on the risk of South Africa's greylisting by the FATF and its implications. The FATF would decide in February 2023 whether to place South Africa on the greylist, and there was a high risk that South Africa would be greylisted. The implications noted included, but were not limited to:

i. Other countries would apply increased due diligence in financial transactions, and this would raise compliance costs.

ii. Some investment mandates might rely on the FATF greylist in assessing the risks of doing business in the country.

iii. Cross-border services such as correspondent banks, Society for Worldwide Interbank Financial Telecommunications (SWIFT), the London Clearing House and continuous linked settlement (CLS) might increase due diligence during the surveillance of cross-border flows, reduce the provision of services and/or increase costs.

2.2.2. An International Monetary Fund (IMF) study was considered, which suggested that when a country is greylisted, it could incur capital outflows of between 4.6% and 10.5% of gross domestic product (GDP). Unlike the countries observed in the IMF study, South Africa would likely be cushioned by:

i. improved macroeconomic imbalances;
ii. the less-dollarised banking system;
iii. the perception that the sub-investment grade credit rating and the associated high-risk premium already reflect greylisting;
iv. the regulatory and structural buffers (e.g. capital controls) as well as the large domestic asset management industry which all reduce the country's vulnerability; and
v. the fact that South Africa was a net foreign creditor while the emerging markets

considered in the IMF study were almost all net foreign debtors.

2.3. **The decline in financial markets depth and liquidity in South Africa**

2.3.1. The FMLG discussed the recent trends of a decline in the depth and liquidity of South Africa's financial markets. This was evidenced by increased de-listings on the Johannesburg Stock Exchange (JSE Limited), a decline in non-resident investor participation and a decline in liquidity in both money and capital markets.

2.3.2. The decline in depth and liquidity was generally attributed to structural and cyclical factors which included, among other things, regulation, sovereign rating downgrades, the recent increase in offshore limits for South African investors and tightening global financial conditions.

2.4. **The SARB's new MPIF**

2.4.1. The FMLG received an update on the SARB's new MPIF.

The SARB would follow a 12-week transition plan, from 8 June 2022 to 24 August 2022, with the aim of achieving the liquidity requirement of a R50 billion surplus compared to the current shortage of around R30 billion. The SARB had previously, in a consultation paper, envisaged fixed-rate, full-allotment refinancing auctions, but public comments had highlighted that the approach would have the following consequences:

i. The approach would place the SARB at the risk of becoming a lender of *first* resort instead of remaining a lender of *last* resort.

ii. Banks would rely on the SARB's repo system for funding instead of the interbank market, thus blunting the quota system.

iii. Banks would overfund and negatively impact short-term interest rates.

2.4.2. As a result, the SARB had resolved to retain the fixed-rate, fixed-quantity auction.

2.5. **Feedback from the Fixed Income and Derivatives Subcommittee**

2.5.1. The Fixed Income and Derivatives Subcommittee (FI&Ds) was collaborating with the Banking Association South Africa (BASA) to write a paper on how to improve secondary market liquidity for South Africa's corporate bond market.

2.6. **Feedback from the Money Market Subcommittee**

2.6.1. The tri-party collateral management framework

i. The concept paper had been approved by the Governors' Executive Committee (GEC) at the SARB, and the project had proceeded to the implementation phase.

2.6.2. Money market liquidity conditions

i. The Money Market Subcommittee (MMS) discussed the funding conditions in the foreign exchange (FX) forward market as well as the trends observed in the money market shortage since November 2021.

2.6.3. Feedback on the SARB's crisis response toolkit

i. The MMS considered the results of the SARB survey on the crisis response toolkit that had been used during the COVID-19 crisis in 2020. Feedback from market participants had been that the SARB had acted decisively in response to the COVID-19 crisis, and a few suggestions for future consideration had also been made.

2.6.4. Reference rate reform project

i. The SARB had published feedback on the draft statement of methodology and policies governing the SARB-administered interest rate benchmarks.

ii. Work was underway to enable the daily observation of South African Overnight Index Average (ZARONIA). The SARB was aiming to start publishing the ZARONIA rate daily from the beginning of June 2022 so that market participants could observe the rate for a period of six to nine months before adoption.

iii. The Market Practitioners Group (MPG) had expanded its workstreams to include the Derivatives, Tax and Accounting as well as Legal workstreams, while the Risk-free Reference Rate workstream had been reinstated with a new mandate to determine the need for forward-looking term rates.

iv. The SARB would soon commence with the process of reviewing the Johannesburg Interbank Average Rate (Jibar) Code of Conduct and Operating Rules.

2.7. **Feedback from the SAFXC** *(Zafar Parker and Richard de Roos)*

2.7.1. Outreach programme

i. The SAFXC had started with bilateral meetings with local asset managers to promote the Global FX Code (Code).

Enquiries:

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Secretariat of the FMLG

Attendance of the FMLG meeting 02 June 2022

Members in attendance	
Dr Rashad Cassim, (FMLG Chairperson), SARB	By Invitation
Edwin Makgopa, (Secretariat), SARB	Dr David Fowkes, SARB
Mpumi Ngwenya, (Secretariat), SARB	Henk JansevanVuuren, SARB
Zafar Parker, SARB	Philadelphia Makhanya, SARB
Samantha Springfield, SARB	Vukile Davidson, NT
Nicola Brink, SARB	Peter Taylor, IBA
Tim Masela, SARB	Niven Mangrey, Nedbank
Garth Klintworth, ABSA Capital	Faizel Jeena, PA
Parin Gokaldas, ABSA Capital	Pierre Mananga, PA
Andries du Toit, FirstRand	Wessel Mostert, PA
Heath Beckley, FI&DS	Cristel Bakker, PA
Lourens van Rensburg, Investec	Thabo Mbeleki, SARB
Clive Sindelman, Investec	Eddie Musasiwa, SARB
James Glover, Nedbank	Shivum Patel, RMB
Duncan Pieterse, NT	Kim Silberman, RMB
Theo Thomas, RMB	
Douglas Hendry, Standard Bank	Apologies from members
Paul Burgoyne, Standard Bank	Kweku Bedu-Addo, IBA
	George Kerby, Nedbank