



# Release of the *Financial Stability Review*

First Edition 2024

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Financial Stability Forum

5 June 2024

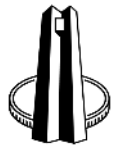
Dr Herco Steyn



SOUTH AFRICAN RESERVE BANK

# Defining financial stability

- ‘Financial stability’ refers to a financial system that **exudes and inspires confidence** through its **resilience to systemic risks and shocks**, and its ongoing ability to **efficiently intermediate funds**.
- **Without financial stability**, there is a heightened risk of the **financial system experiencing disruptions** in financial intermediation that could **adversely impact real economic activity**.
- Financial stability is **not an end in itself**, but is an important **precondition** for sustainable **economic growth**.

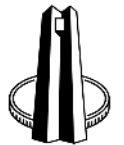


# Legal basis for the *Financial Stability Review (FSR)*

The **Financial Sector Regulation Act 9 of 2017** mandates the **SARB** to:

- assess the stability of the financial system during the six-month review period;
- identify and assess risks to financial stability in at least the next 12 months;
- provide an overview of the steps taken by the SARB and financial sector regulators to identify and manage identified risks and vulnerabilities in the financial system; and
- provide an overview of the recommendations made by the SARB and the Financial Stability Oversight Committee (FSOC) during the period under review and progress made in implementing those recommendations.

**FSR: not only about identifying risks;** also important to highlight **initiatives and factors that increase resilience.**

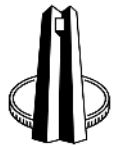


# Collaborating in pursuit of financial stability

- The FSR Act assigns a **lead role to the SARB** in protecting and enhancing financial stability in South Africa

## BUT

- The FSR Act also empowers **several other financial sector regulators to support the SARB** in pursuing this mandate, including NT, PA, FSCA, FIC and NCR.
- The *FSR* is **tabled in Parliament** and is **targeted at the Members of Parliament, participants in the financial sector, international central bank peers, ratings agencies, international financial institutions, standard-setting bodies and academia.**
- The *FSR* **aims to stimulate debate on pertinent issues related to financial stability** in South Africa.



# Global developments

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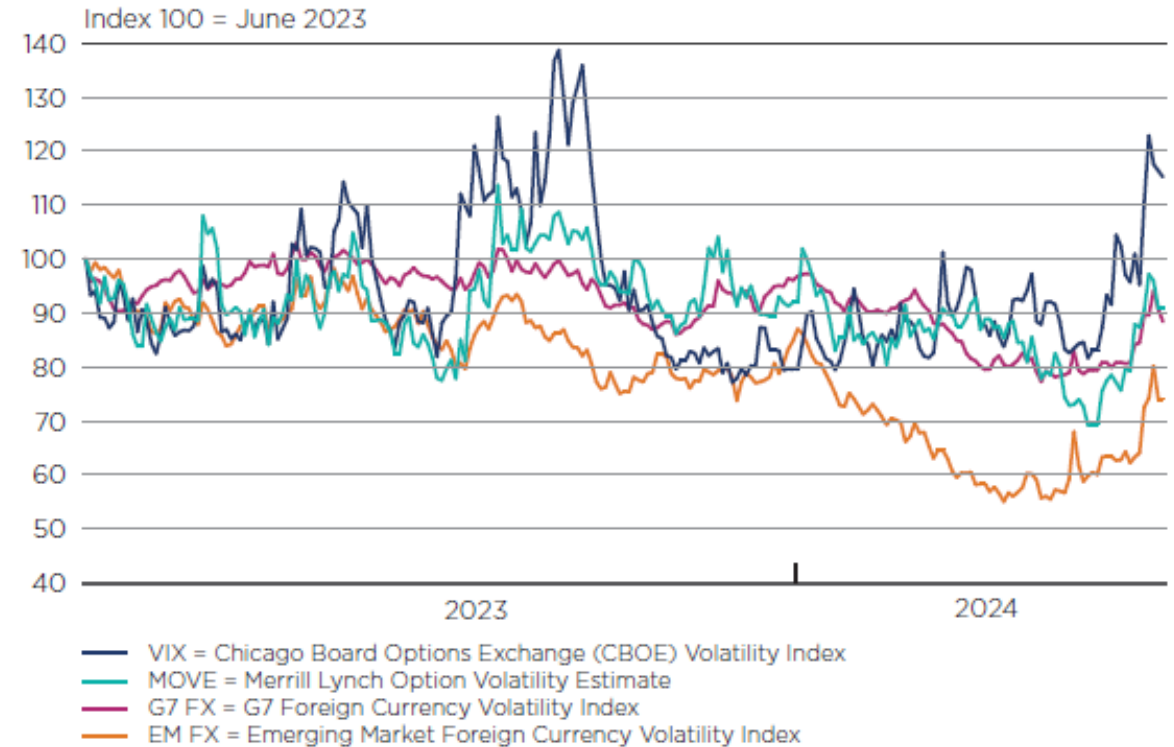


# Key global developments

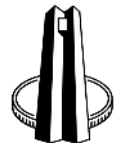
## Since November 2023 *FSR*:

- Global financial markets buoyed by **growing evidence that steady progress towards sustained disinflation is being made.**
- **Fiscal deficits** (i.e. shortfall in government income relative to government spending), **government debt** levels and **debt-service costs** remain elevated.
- **Factors that could impact market volatility: elections** in more than 70 countries; **geopolitical tensions** (Russia-Ukraine; Middle East; US-China); **policy rate divergence.**

## Selected volatility measures



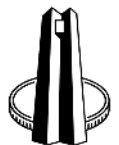
Source: Bloomberg



# Key global developments

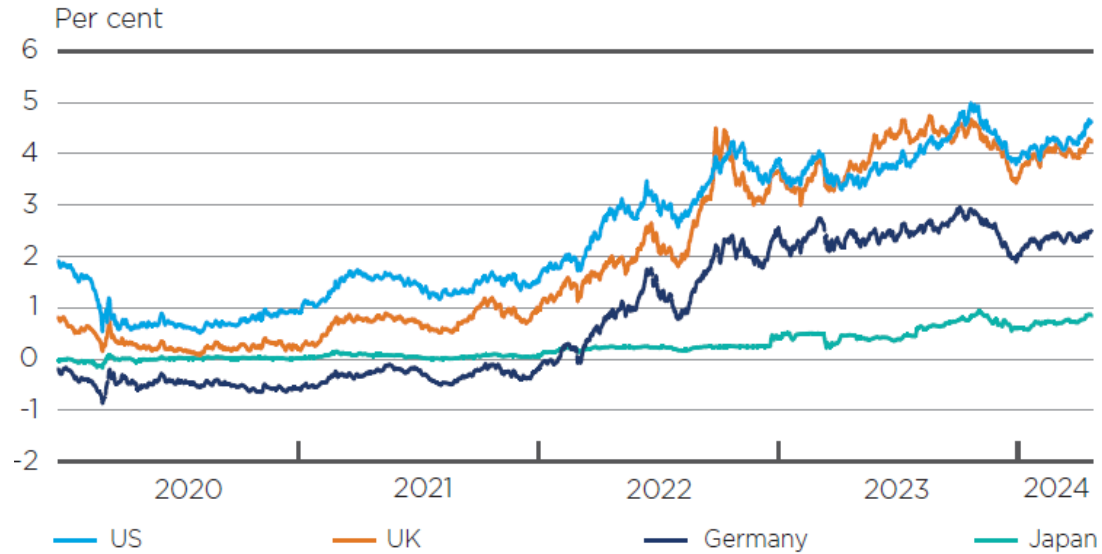
- **Inflation has proven stickier than anticipated** and expectations of **interest rate cuts** have been **pushed back to later in the year**.

Selected 10-year AE government bond yields



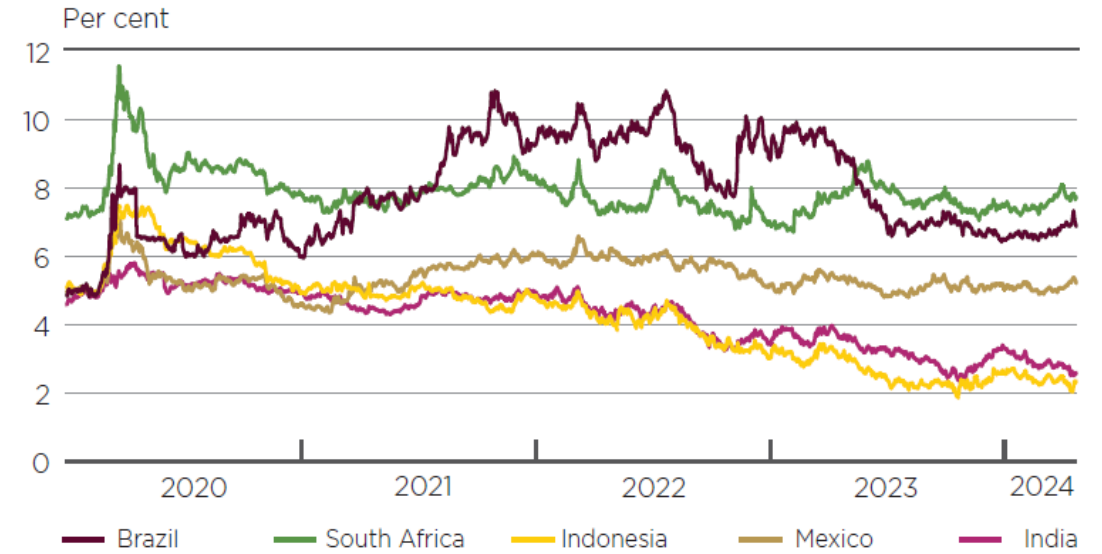
# Key global developments

## Selected 10-year AE government bond yields

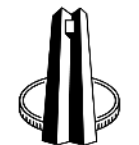


Source: Bloomberg

## Selected 10-year EM government bond yield spreads



Source: Bloomberg





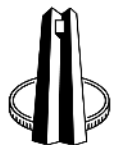
# Domestic developments and key risks to financial stability

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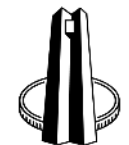
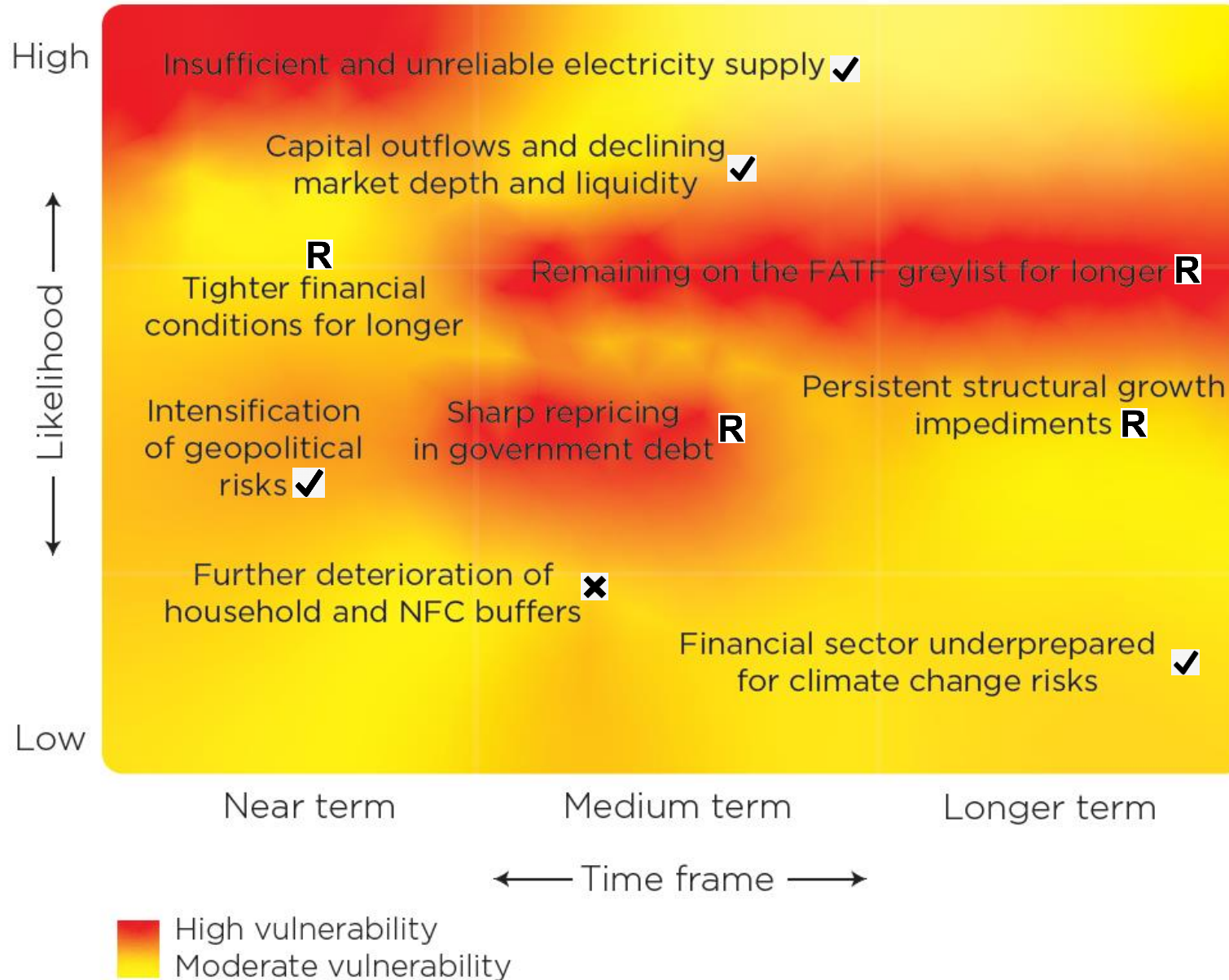


# Key risks to South African financial stability

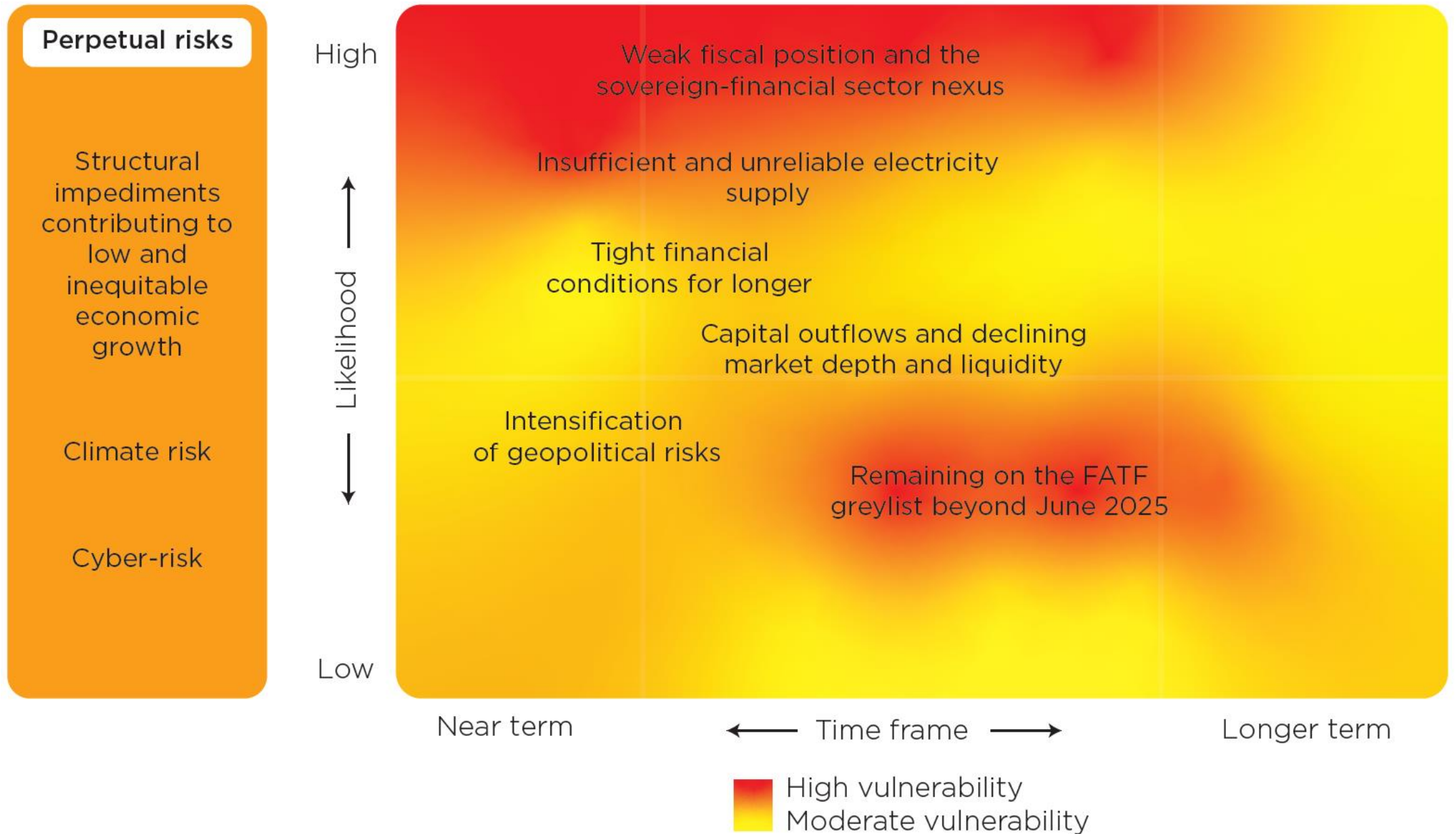
- Communicated via the SARB Risks and Vulnerabilities Matrix (RVM)
- RVM reflects the **residual vulnerability of the financial system**
- **Vulnerability:** A property of the financial system that:
  - reflects the existence or **accumulation of imbalances;**
  - may **increase the likelihood of a shock;** or
  - when impacted by a shock, **may lead to systemic disruption.**
- Residual vulnerability: **remaining or net vulnerability** of the financial system **after considering existing mitigating factors and actions**



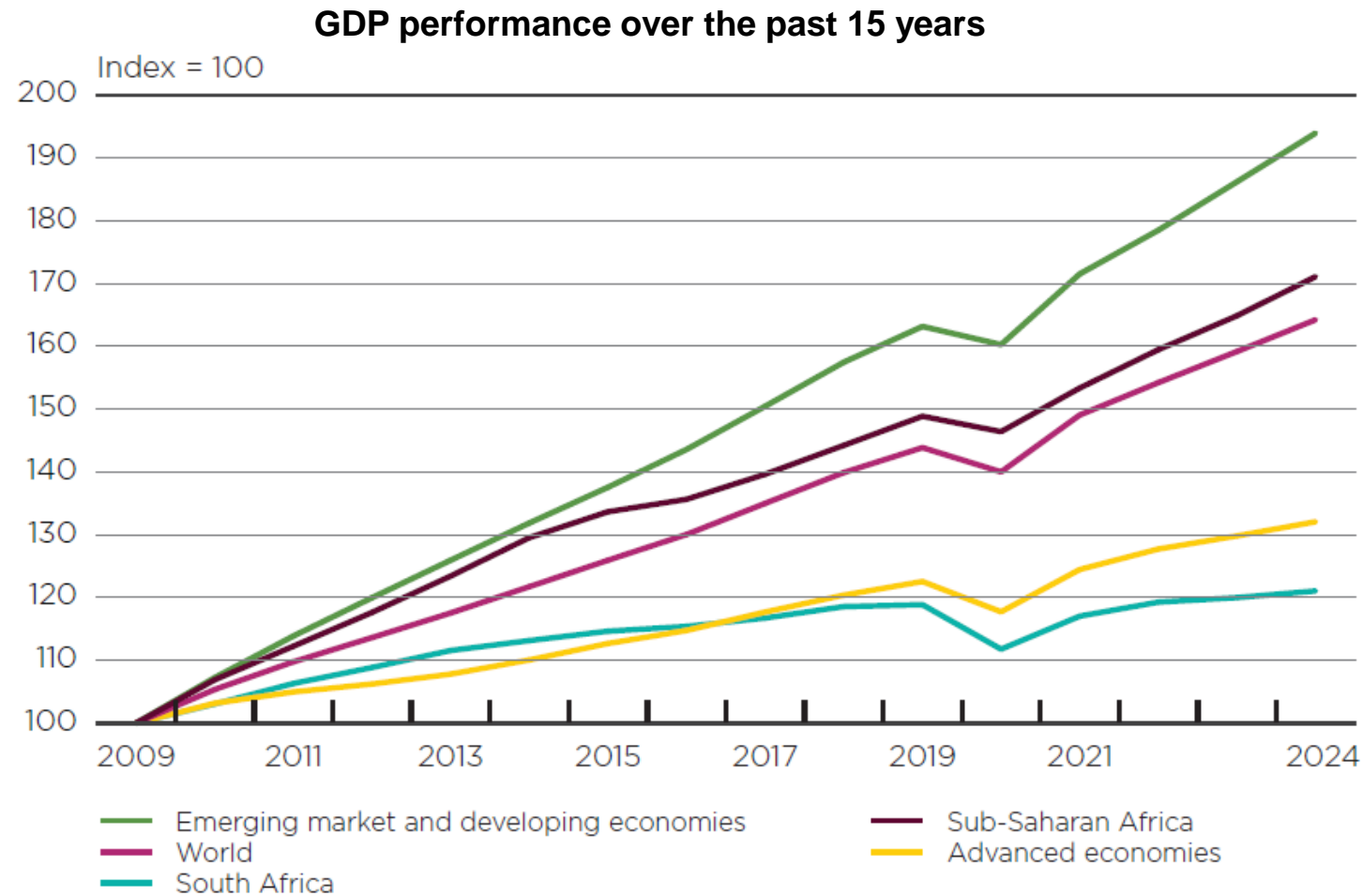
# SARB RVM: November 2023 FSR



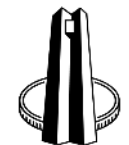
# SARB RVM



# Structural impediments contributing to low and inequitable economic growth

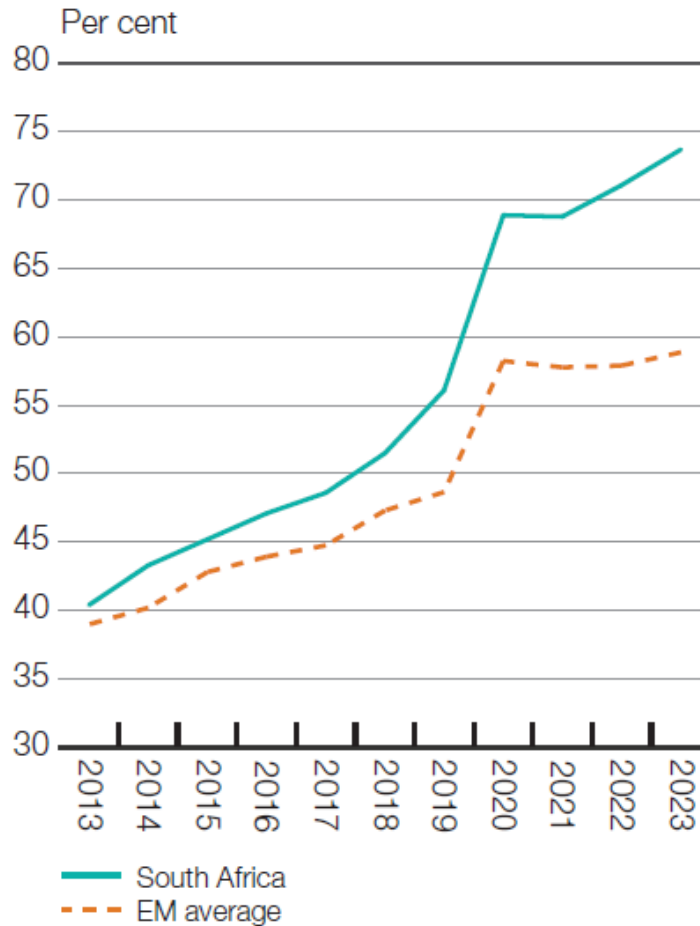


Source: IMF



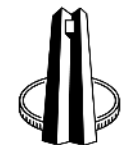
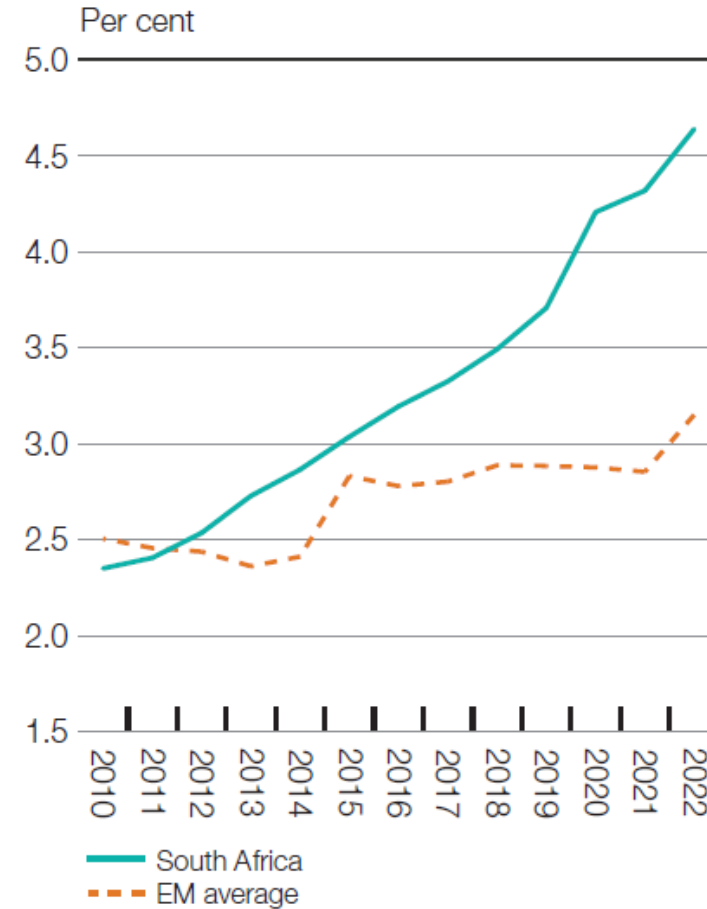
# Weak fiscal position and sovereign-financial sector nexus

## Debt-to-GDP ratios: South Africa vs EM average



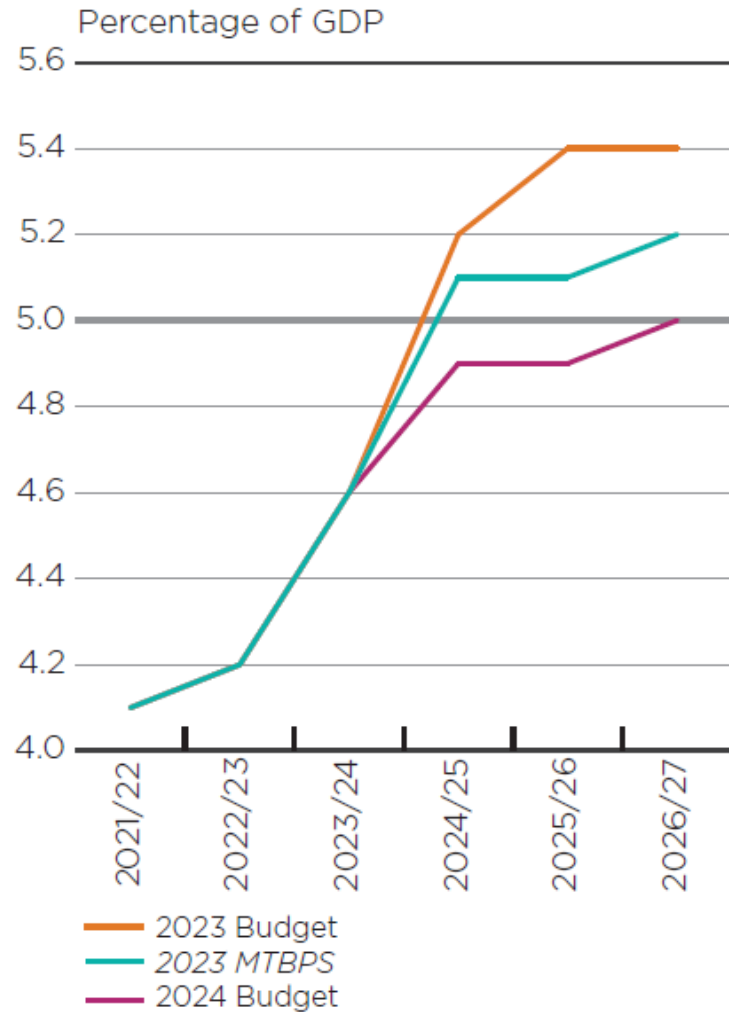
Source: SARB

## Interest-to-GDP ratio: South Africa vs EM average

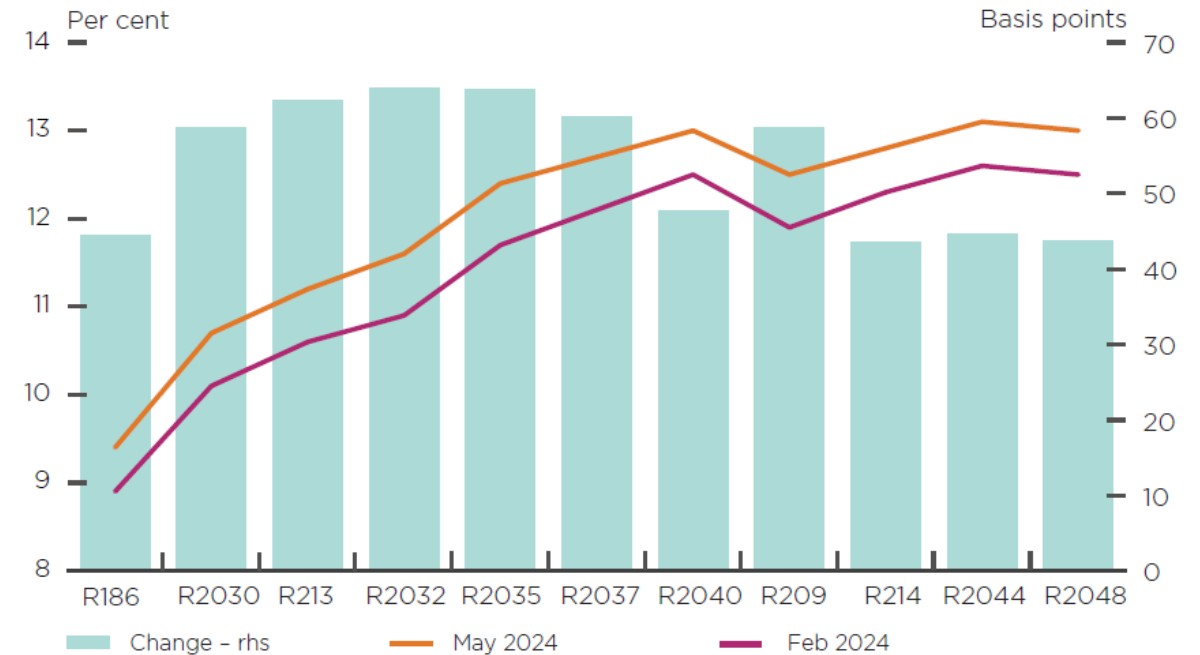


# Weak fiscal position and sovereign-financial sector nexus

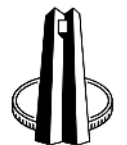
Projected government debt-service cost



SA government bond yield curve

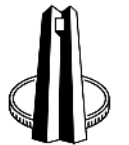


Source: SARB



# Weak fiscal position and sovereign-financial sector nexus

- The South African **financial system is highly exposed to government debt.**
- A high and growing proportion of financial institutions' balance sheets comprising government debt **hold the following potential implications:**
  - **crowding out** lending to or investing in the private sector;
  - **exposing the financial system to market risk** in the event of a **sharp repricing of government debt**; and
  - **undermining market resilience** as the financial system is increasingly **exposed to a common risk.**

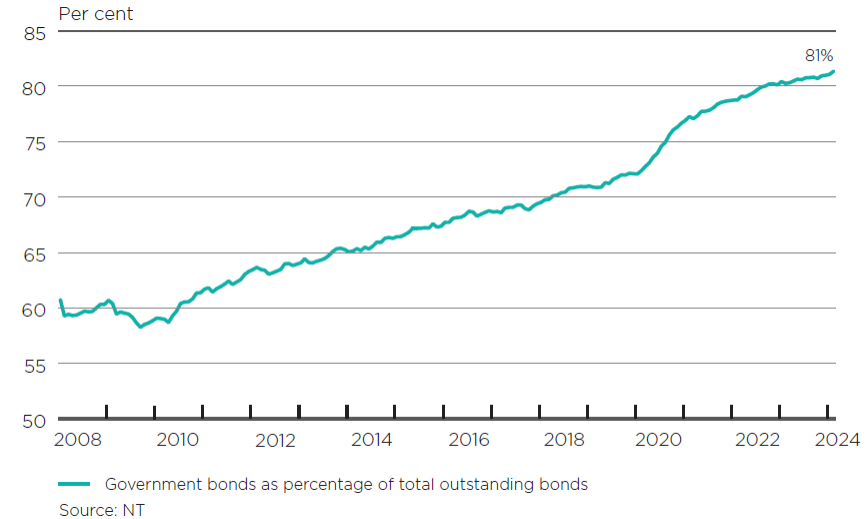




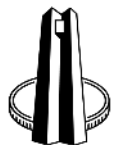
# Capital outflows and declining market depth and liquidity

- South Africa's **capital markets have become shallower and less liquid** over the past few years
- **Reduces diversification options** of both borrowers and investors
- On the JSE, there have been **net company delistings every year since 2016**

Government bonds as percentage of total outstanding bonds



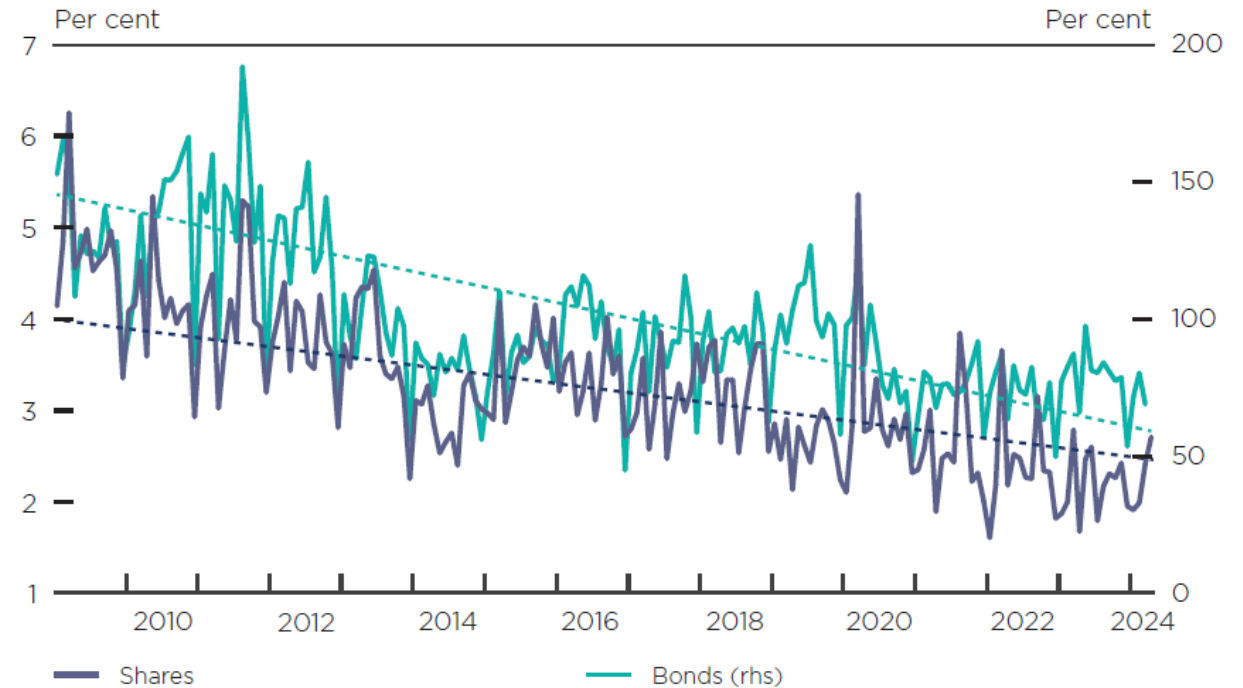
JSE listings and delistings



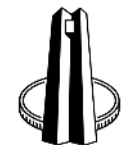
# Capital outflows and declining market depth and liquidity

- **Turnover in both the domestic bond and equity markets have also declined** in recent years.
- **Could affect efficient pricing, investor returns and the cost of funding.**

**Bond and equity turnover as percentage of total market capitalisation**

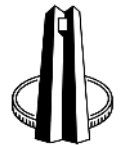
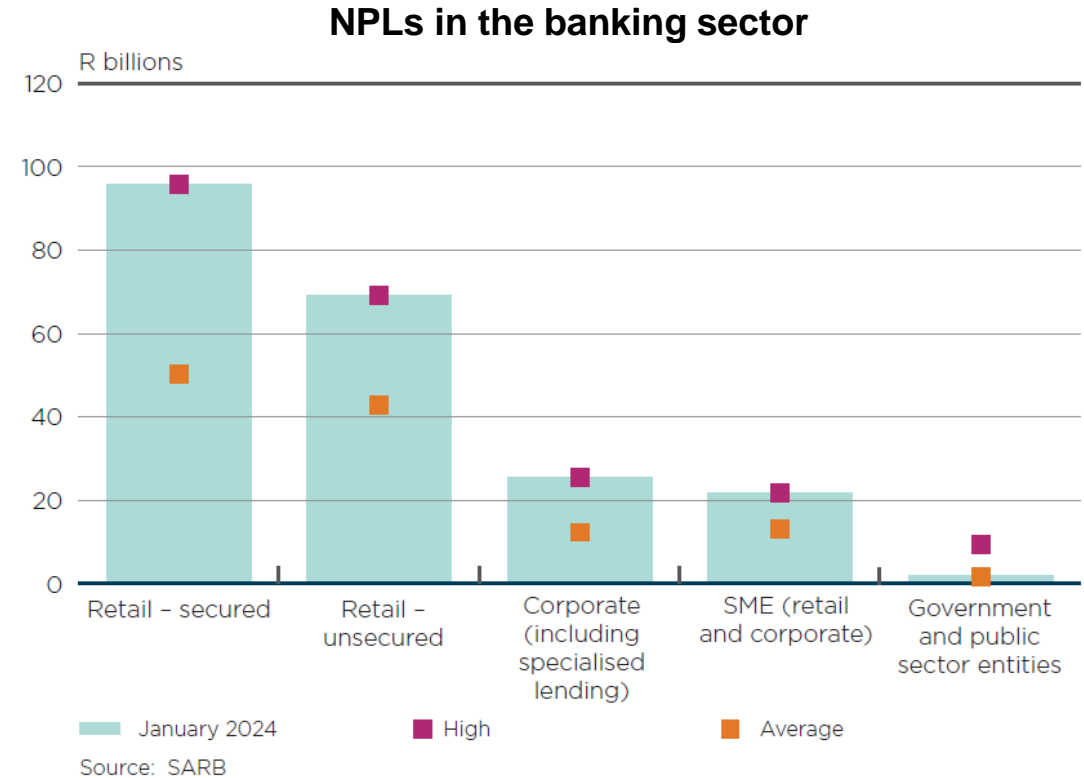


Source: Strate



# Tight financial conditions for longer

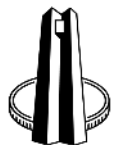
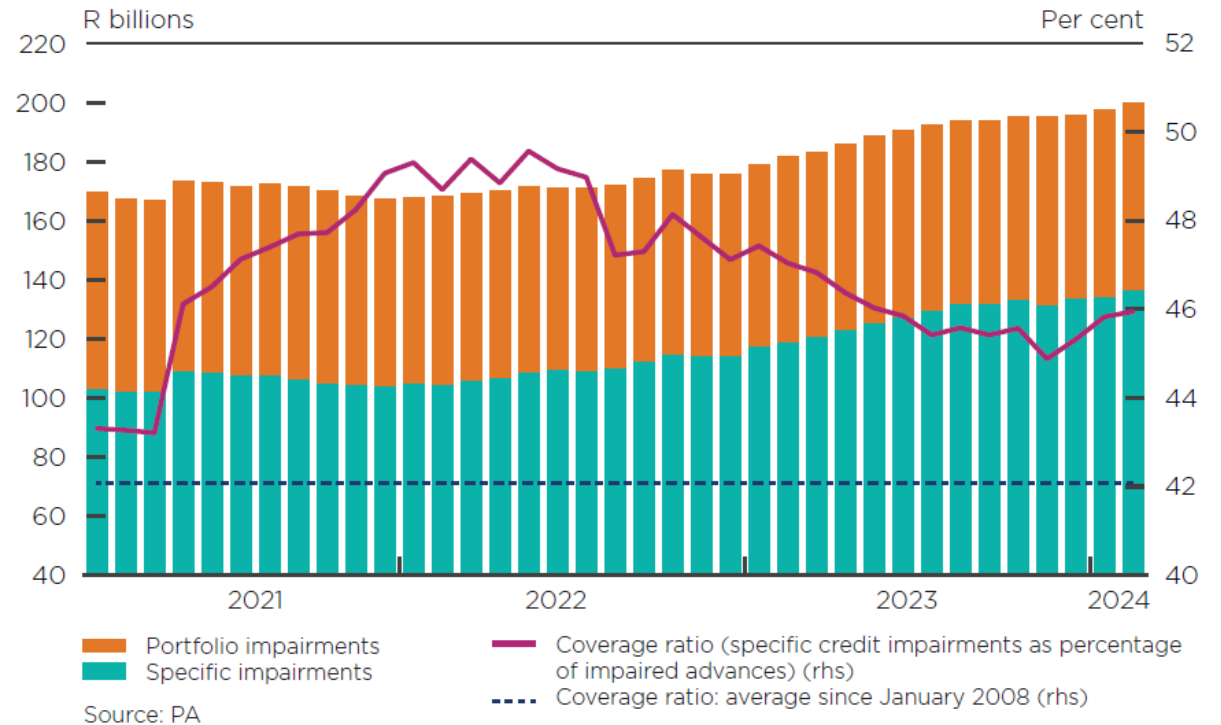
- **High policy rates** contribute to restrictive financial conditions, as **households, companies and governments find it more difficult and more expensive to access credit.**
- The banking sector's **non-performing loans (NPLs)** for the largest asset classes **are at their highest levels in a decade.**
- This could **result in rising credit losses, which could reduce bank capital and profitability.**



# Tight financial conditions for longer

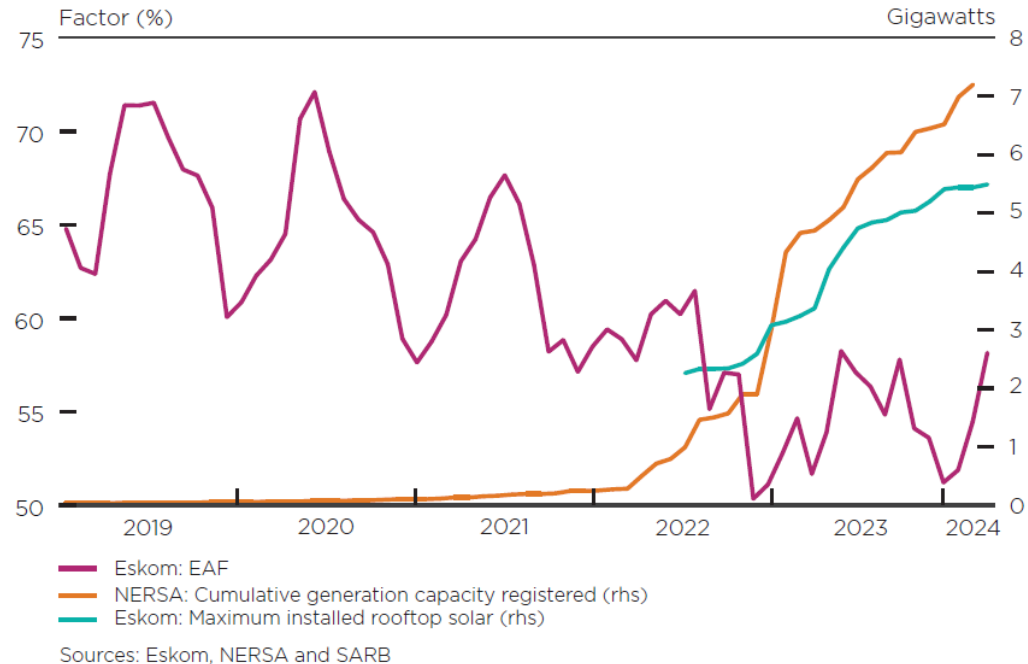
- To mitigate the uptick in NPLs, **banks have been increasing their provisions for potential credit losses**
- Banks have been **increasing their provisions faster than credit is being extended**, as reflected by the growing value of impairments raised
- Suggests that **banks should be able to absorb a further increase in defaults.**

Impairments and specific impairments as a percentage of impaired advances

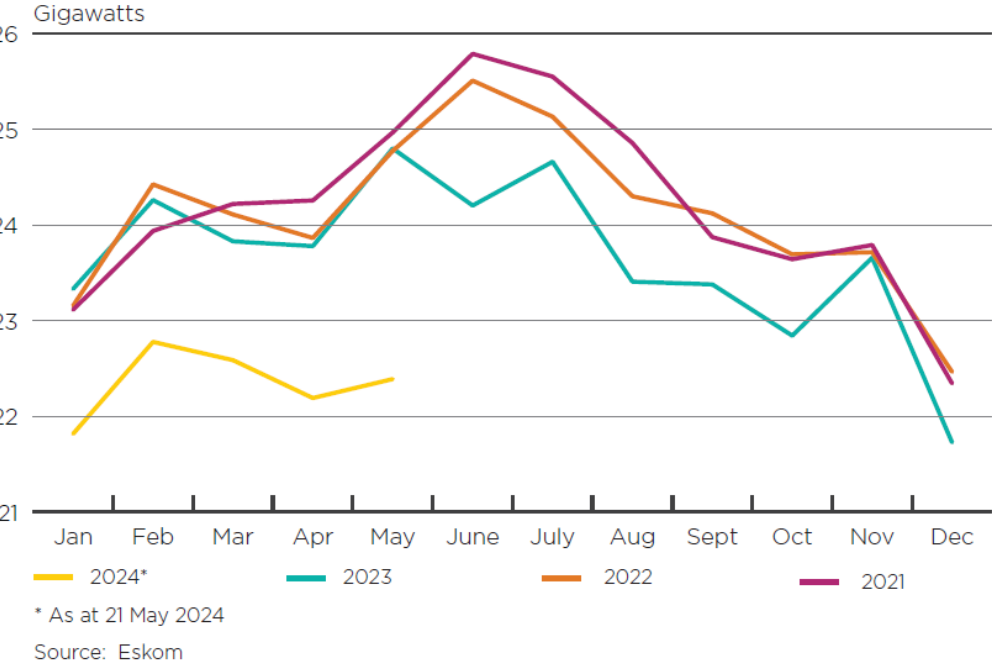


# Insufficient and unreliable electricity supply

**Eskom EAF and renewable generation registered and installed**

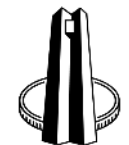


**Average monthly Eskom residual demand**



# Intensification of geopolitical risks and remaining on the FATF greylist beyond June 2025

- A small open economy such as **South Africa faces several risks arising from geopolitical tensions** e.g. changes in the **level and direction of existing trade and financial flows**, **volatility in the prices of both imported and exported commodities**, supply chain constraints and **disruptions in international transport systems**.
- **The ongoing uncertainty associated with simmering geopolitical tensions is also likely to weigh on investor sentiment, resulting in volatile capital flows and asset prices.**
- The European Union added South Africa to its **list of high-risk countries in June 2023**.
- In early December 2023, **the United Kingdom also classified South Africa as a high-risk third-party country.**
- Subsequently, the **European Securities and Markets Authority (ESMA) derecognised JSE Clear as a qualifying central counterparty (CCP)** with effect from 29 December 2023.



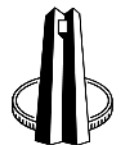
# Policy actions and initiatives

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# Policy actions and initiatives undertaken to enhance domestic financial stability

- Enhancing the financial safety net through the **operationalisation of the Corporation for Deposit Insurance**
- Ongoing progress with **resolution standards**
- Introducing a **positive cycle neutral countercyclical capital buffer**
- Mitigating the **sovereign-financial sector nexus**
- **Increasing the financial sector's resilience** to deal with a national **electricity grid shutdown**
- **Collaborating** with FSOC members
- **Enhancing** macroprudential **policy transparency**
- **Enhancing cyber-resilience** within the financial sector
- **Enhancing** the financial sector's **resilience against climate risk**





# Financial stability assessment

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# Financial stability assessment

- The South African financial system **faces several risks to financial stability**.
- However, **steady progress has been made to reduce the vulnerability of the domestic financial system against the key risks highlighted**, most notably by strengthening the domestic financial safety net and mitigating the impact of a potential systemic event.
- **Prudentially regulated domestic financial institutions**, in aggregate, **remained resilient**, as measured by their ability to maintain adequate capital and liquidity buffers to absorb the impact of shocks.
- Financial institutions have been able to **provide financial services uninterruptedly**.



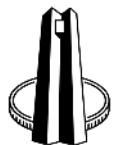
# 2023/24 Insurance Common Scenario Stress Test (ICSST)

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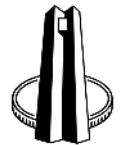
# 2023/24 Insurance Common Scenario Stress Test (ICSST)

- The ICSST subjected a **set of potentially systemic South African insurers** to a selection of **severe but plausible shocks and scenarios**.
- **November 2021 FSR:** the SARB presented results of an exploratory insurance stress-testing exercise and highlighted the **need for more advanced and comprehensive stress tests of the insurance industry**.
- The **2023/24 ICSST is the second macroprudential exercise** to be conducted on the South African insurance industry and is an enhancement of the 2020/21 exercise.

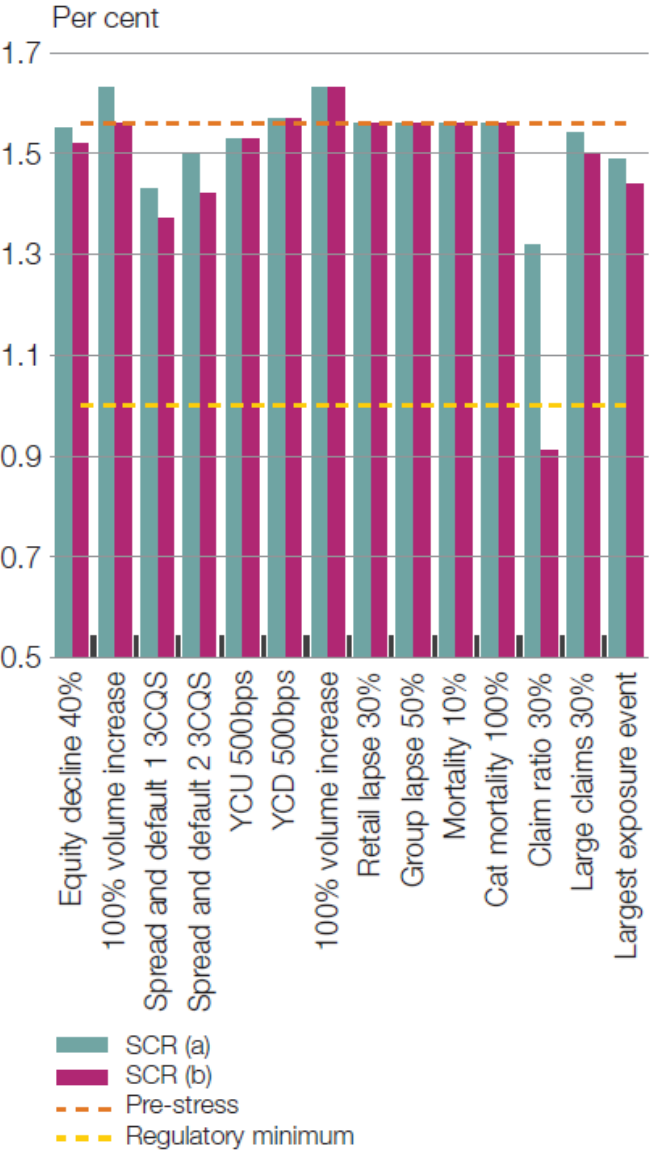
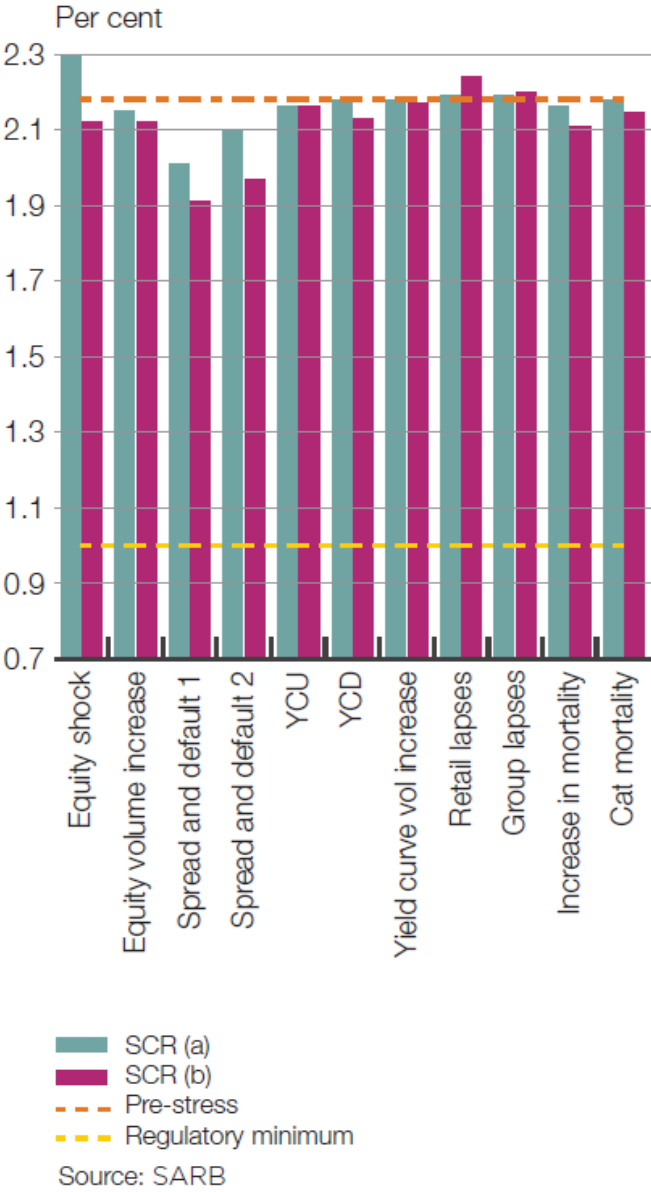


# ICSST participants

- **A total of 9 insurers were included** in the 2023/2024 exercise
- **5 participating life insurers:** Old Mutual Life Company of South Africa, Sanlam Life, Liberty Life, Momentum Metropolitan Life and Hollard Life
- Account for roughly **60% of the total assets of the life insurance segment**
- **4 participating non-life insurers:** Santam, GuardRisk, Hollard and Old Mutual Insure
- Account for more than **49% of total gross written premiums in the non-life segment**
- Number of participants may be reviewed again in future ICSSTs



# ICSST results





**THANK  
YOU**



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