POLICY PAPER

Financial Stability Department

May 2024

The South African Reserve Bank

Macroprudential Policy Framework and

Decision-making Process

Key terms

Drawing on the definitions used by the Financial Stability Board (2021), key terms in this document are defined as follows:

Financial sector regulators: As per the Financial Sector Regulation Act 9 of 2017 (FSR Act), (i) the Prudential Authority; (ii) the Financial Sector Conduct Authority; (iii) the National Credit Regulator; and (iv) the Financial Intelligence Centre.

Financial stability: According to section 4 of the FSR Act, financial stability means (i) financial institutions and market infrastructures are capable of providing financial products and financial services and performing their functions and duties in terms of financial sector laws without interruption and despite changes in economic circumstances; and (ii) there is general confidence in the ability of financial institutions and market infrastructures to keep providing the said products and services, and to keep performing their functions and duties. Phrased differently, 'financial stability' refers to a financial system that is resilient to systemic risks and shocks and that can efficiently intermediate funds, even in adverse conditions, thereby bolstering confidence in the financial system and financial institutions. Financial stability is not an end in itself, but a precondition for balanced and sustainable economic growth.

Financial system: The system of institutions and markets through which financial products, financial instruments and financial services are provided and traded, and includes the operation of a market infrastructure and a payment system.

Macroprudential instrument: Any policy instrument, regardless of the institutional authority with whom it vests, that is explicitly applied to (i) mitigate vulnerabilities in the financial system and reduce systemic risk; thereby (ii) improving the resilience of the financial system; in turn ultimately (iii) protecting and enhancing financial stability in South Africa.

Residual/net vulnerability: The remaining vulnerability after considering the identified mitigating factors and actions.

Resilience: The ability of a financial system to deal with shocks without leading to financial instability.

Risk: The possibility of an adverse or undesirable event or outcome materialising. Risks may have materialised already or could still materialise in future. The materialisation of risks can often not be prevented completely, but the impact of a risk materialising may be mitigated to a greater or lesser extent.

Risk and Vulnerability Matrix (RVM): The RVM shows the residual vulnerability of the financial system after considering existing mitigating factors and policy actions.

Shock: An event that may cause disruption to, or the partial failure of, the financial system.

Systemic event: According to the FSR Act, 'an event or circumstance, including one that occurs or arises outside [of] the Republic [of South Africa], that may reasonably be expected to have a substantial adverse effect on the financial system or on economic activity in the Republic, including an event or circumstance that leads to a loss of confidence that operators of, or participants in, payment systems, settlement systems or financial markets, or financial institutions, are able to continue to provide financial products or financial services, or services provided by a market infrastructure'.

Systemic risk: According to the Financial Market Act 19 of 2012, 'the danger of a failure or disruption of the whole or significant part of [South Africa's] financial system'.

Transmission channels or mechanisms: The channels through which vulnerabilities may lead to the actual disruption of the financial system, should a shock occur.

Vulnerability: A property of the financial system that (i) reflects the existence or accumulation of imbalances; (ii) may increase the likelihood of a shock; or (iii) when impacted by a shock, may lead to systemic disruption.

1. Background and purpose of the document

The SARB last published its macroprudential policy and financial stability monitoring framework in 2021 (available here). In April 2024, the SARB's Financial Stability Committee (FSC) endorsed the updated SARB macroprudential policy and financial stability monitoring frameworks. This document sets out the SARB's macroprudential policy framework and decision-making process, and should be read in conjunction with the SARB's financial stability monitoring and assessment framework (available here). Its publication aims to increase transparency on how the SARB pursues its financial stability mandate in line with international best practice.

2. Macroprudential policy, objectives and design

Macroprudential policy refers to a set of policy options aimed at limiting the build-up of vulnerabilities in the financial system and strengthening financial system resilience, thereby protecting and promoting financial stability (Gadanecz and Jayaram, 2015). Macroprudential policy can be directed at reducing vulnerabilities across three dimensions (BIS-FSB-IMF, 2016; ECB, 2024):

a. **Time dimension:** Prevent or contain the gradual build-up of systemic vulnerabilities.
b. **Cross-sectoral dimension:** Increase the overall resilience of the financial system to shocks and limit contagion effects.
c. **Structural dimension:** Mitigate, to the extent possible, structural vulnerabilities within the financial system and encourage a system-wide perspective of financial regulation.

Drawing on a Bank for International Settlements (BIS) survey, Villar (2017) identifies the following five desirable features of macroprudential policy frameworks:

a. A clearly specified objective and usable instruments.
b. A common understanding and close alignment of decision-making powers over the available instruments that could be deployed for macroprudential purposes (Borio, 2014). Otherwise, central banks may be forced to use existing instruments (e.g. monetary policy ones) for purposes for which they were not specifically designed.
c. A clear relationship between the various institutions mandated with financial stability and other policy objectives, combined with a deep understanding of the

policy trade-offs and potential side effects of macroprudential measures are crucial.

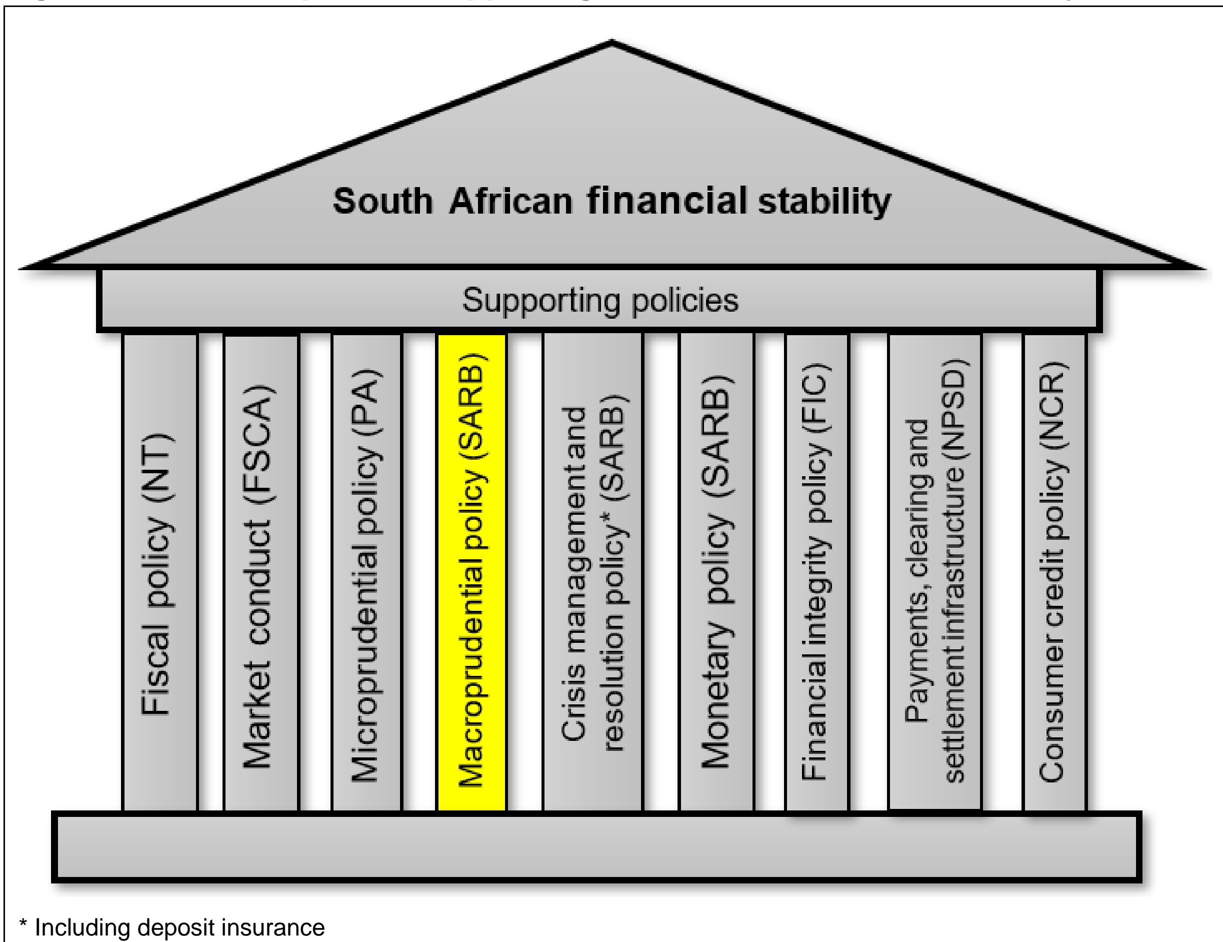
d. Arrangements to avoid mission creep, so that policies do not drift from ensuring financial stability towards other objectives (e.g. managing the business cycle).

e. Insulation from political cycles. This is critical as systemic risk often builds up over prolonged periods, implying that appropriate measures have to be taken at times when they may be unpopular.

3. Financial stability and macroprudential policy in South Africa

In South Africa, macroprudential policy aims to protect and enhance financial stability as defined in the Financial Sector Regulation Act 9 of 2017 (FSR Act). However, macroprudential policy is not the only policy that increases the resilience of the financial system and protects and promotes financial stability. Rather, financial stability is supported by various domestic policies as illustrated in Figure 1.

Figure 1: Domestic policies supporting South African financial stability



* Including deposit insurance

4. Macroprudential instruments

The purpose of a macroprudential instrument is (i) to mitigate vulnerabilities in the financial system and reduce systemic risk; thereby (ii) improving the resilience of the financial system; in turn ultimately (iii) protecting and enhancing financial stability. However, defining what exactly constitutes a macroprudential instrument is difficult as central banks use various tools to improve the resilience of the financial system, but this does not necessarily make them macroprudential (Villar, 2017).

There may be times when policy instruments that had originally been designed for other purposes, such as microprudential or market conduct regulation or central bank balance sheet management, could be employed for macroprudential purposes. They should, however, (i) explicitly target reducing systemic risk; and (ii) be underpinned by the necessary governance arrangements (FSB, 2011). There may be instances where an instrument could be deployed to mitigate a financial system vulnerability and/or improve the resilience of the financial system, but it may not necessarily be a prudential tool that vests with the SARB or the PA (e.g. market conduct instruments or instruments aimed at promoting financial system integrity).

In view of the above, the South African definition of a macroprudential instrument is as follows:

> Any policy instrument, regardless of the institutional authority with whom it vests, that at the direction of the SARB is explicitly applied to (i) mitigate vulnerabilities in the financial system and/or reduce systemic risk; thereby (ii) improving the resilience of the financial system; in turn (iii) protecting and enhancing financial stability in South Africa.

5. SARB macroprudential policy framework and decision-making process

5.1 The SARB's role in coordinating macroprudential policy

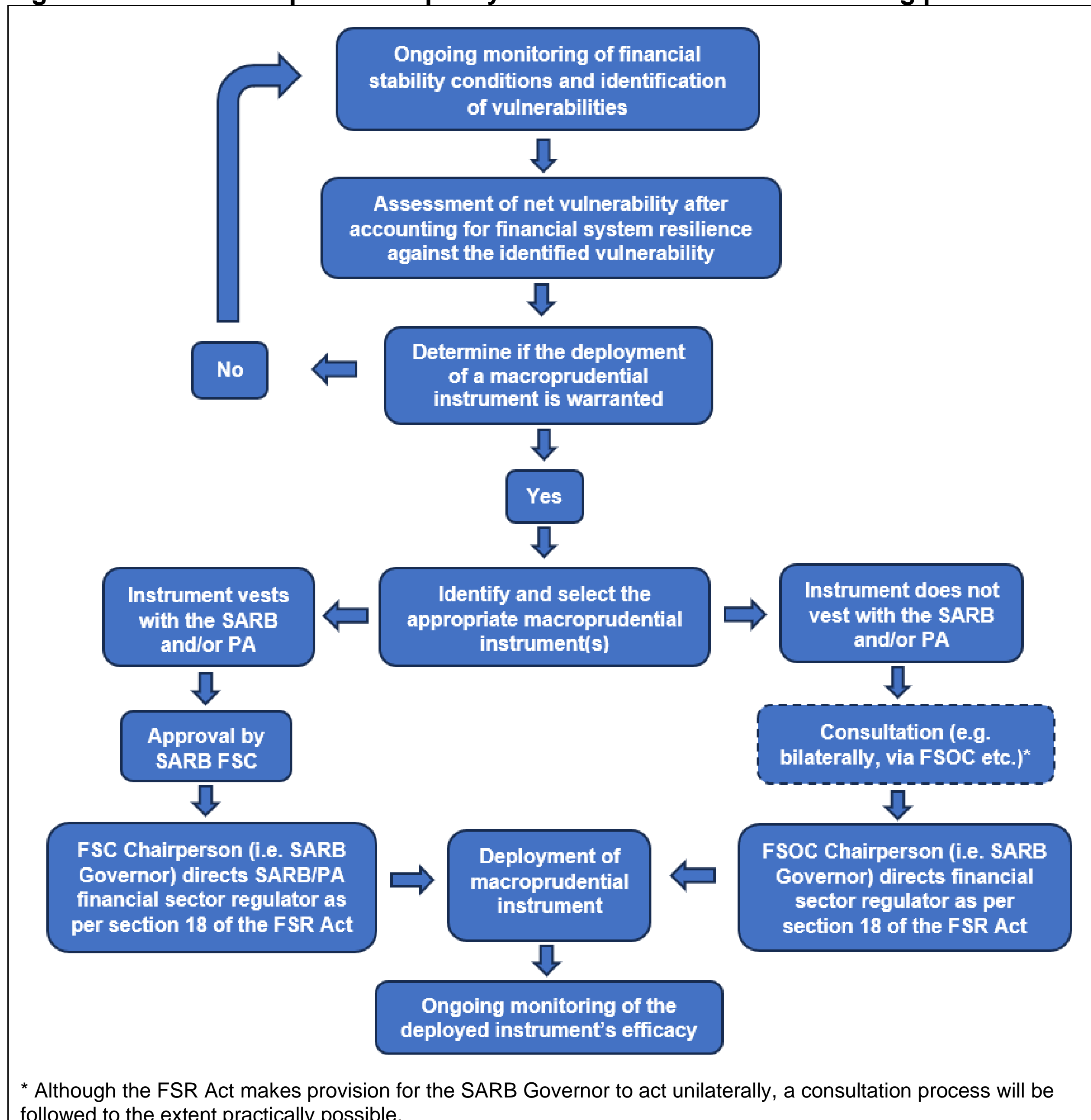
Although the FSR Act assigns the main legal responsibility for protecting and enhancing financial stability to the SARB, it also recognises the fact that it is not a mandate that can be achieved by one authority alone. Section 26 of the FSR Act directs that financial sector regulators[1] must co-operate and collaborate both with the SARB and each other to maintain, protect and enhance domestic financial stability. Financial sector regulators are also obliged to provide the necessary assistance and information to the SARB to maintain or restore financial stability, and to promptly report to the SARB any matter of which they become aware that may pose a risk to financial stability. The Financial Sector Oversight Committee (FSOC) has been established in terms of the FSR Act as a supporting mechanism for such information sharing.

The SARB is mandated to take steps to mitigate risks to financial stability, including advising other financial sector regulators, and any other organs of state, of the steps to take to mitigate those risks. South African macroprudential instruments may therefore be categorised into two broad categories: those that vest with the SARB (including the PA), and those that do not. Figure 2 depicts the SARB's macroprudential policy framework and decision-making process for instruments that vest (a) with the SARB and the PA; and (b) with other financial sector regulators.

[1] The Prudential Authority (PA), Financial Sector Conduct Authority (FSCA), Financial Intelligence Centre (FIC) and National Credit Regulator (NCR).

5.2 Steps in the SARB's macroprudential policy framework and decision-making process

Figure 2: SARB macroprudential policy framework and decision-making process



* Although the FSR Act makes provision for the SARB Governor to act unilaterally, a consultation process will be followed to the extent practically possible.

1. **Step 1: Ongoing monitoring of financial stability conditions and identification of vulnerabilities:** The SARB's Financial Stability Monitoring and Assessment Framework[2] details the indicators and instruments employed to monitor financial stability conditions and identify vulnerabilities in the South African financial system.
2. **Step 2: Assessment of net vulnerability after accounting for financial system resilience against the identified vulnerability:** A financial system's resilience reflects its ability to deal with shocks without becoming unstable. Once a vulnerability is identified, the net (or residual) vulnerability is determined by identifying and considering the mitigating factors and actions against the identified vulnerability (i.e. the financial sector's resilience given a particular vulnerability).
3. **Step 3: Determine if the deployment of a macroprudential instrument is warranted:** If the net vulnerability is still considered to pose a risk to domestic financial stability, the deployment of a macroprudential instrument may be warranted. Key considerations in this step are to determine the potential policy trade-offs and any possible unintended consequences the deployment of a macroprudential instrument might have.
4. **Step 4: Identify and select the appropriate macroprudential instrument(s):**
    a. **For instruments that vest with the SARB/PA:** The non-statutory, internal SARB committee that advises the Governor on macroprudential policy decisions in support of discharging the SARB's financial stability responsibilities is the Financial Stability Committee (FSC). In terms of the policy framework agreed between the Governor and the Minister of Finance on how the SARB will fulfil its financial stability mandate,[3] all policy recommendations related to the SARB's responsibilities set out in the FSR Act will be considered by the FSC before being approved by the Governor for implementation. If agreement is reached by the FSC on the deployment of a macroprudential instrument that vests with the SARB/PA, the FSC Chairperson (i.e. the SARB Governor) will subsequently direct the SARB/PA financial sector regulator as per section 18 of the FSR Act to deploy or amend the use of a macroprudential instrument.
    b. **For instruments that do not vest with the SARB/PA:** The SARB's macroprudential policy framework and decision-making process allows it to consult (e.g. bilaterally or through FSOC) on matters relevant to financial stability, but which are not directly under its direction. The FSR Act affords the

[2] Available at Macroprudential policy (resbank.co.za).
[3] This document is not publicly available.

SARB the explicit, unilateral power to direct a financial sector regulator to assist it in preventing systemic events from occurring and/or mitigating the adverse effects should a systemic event have occurred. However, a consultation process will be followed to the extent practically possible. If the deployment of a macroprudential instrument that does not vest with the SARB/PA is warranted, the FSOC Chairperson (i.e. the SARB Governor) directs the relevant financial sector regulator as per section 18 of the FSR Act to deploy or amend the use of a macroprudential instrument.

Similar to Step 3, determining the policy trade-offs and potential unintended consequences the deployment of a macroprudential instrument might have is crucial. Communication on directives on the deployment of macroprudential instruments will be effected in writing via the office of the SARB Governor.

5. **Step 5: Deployment of macroprudential instrument:** After the SARB Governor has directed the deployment of a macroprudential instrument, the relevant financial sector regulator will give effect to the decision communicated in writing, as well as with any provisions set out therein (e.g. timelines).
6. **Step 6: Ongoing monitoring of the deployed instrument's efficacy:** This step is critical to ensure that any unintended consequences are identified and that the instrument continues to function as intended.

A summary of the objectives, composition and functions of the FSC is provided in Annexure A, while Annexure B sets out the instruments under the direction of the SARB and the PA that the FSC could recommend to the SARB Governor to deploy. Annexure C provides a summary of the objectives, composition and functions of FSOC.

6. Conclusion

The SARB's macroprudential policy framework and decision-making process, read with the SARB's financial stability monitoring and assessment framework, describes the overarching framework the SARB uses to pursue its financial stability mandate. It is published as a reference document which supports transparency on how the SARB pursues its financial stability mandate.

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Annexure A

Table A.1: FSC overview

Description and objectives	Membership composition	Functions
• The FSC is an internal non-statutory policy committee of the SARB. • The purpose of the FSC is to formulate financial stability policy of the SARB in support of its financial stability mandate. • The FSC currently meets four times a year, but the Governor can convene a meeting at any time if required.	The FSC consists of: • the Governor as Chairperson; • the SARB deputy governors; • the heads of the SARB's line departments;[4] and • Members of the MPC who are neither deputy governors nor heads of department.	• Through the FSC, the SARB fulfils its responsibility to monitor and review the strengths and weaknesses of the financial system and any risks to financial stability. • The FSC assesses policy proposals to address systemic risks and decides whether any macroprudential policy measures need to be selected and implemented. • The FSC plays an active role to support the Governor in the management of systemic events or the resolution of designated institutions. • The FSC oversees the work of two subcommittees: - the Resolution Policy Panel, which oversees resolution policies, resolution plans and resolvability assessments; and - the Crisis Preparedness Committee, which focuses on increasing the SARB's ability to manage and respond to systemic events.

[4] These are the Financial Stability Department; the four departments comprising the Prudential Authority, the Financial Markets Department, the Financial Surveillance Department, the National Payment System Department, the Economic Statistics Department and the Economic Research Department.

Annexure B

The macroprudential instruments under the direction of the SARB and PA are listed in Table B.1 below.

Table B.1: SARB and PA macroprudential toolkit

Available instruments
• Adjustment to margins, haircuts or eligible collateral • Capital requirements, including sectoral capital requirements • Changes to individual foreign capital allowances • Changes to monetary operations and quotas • Changes to prudential limits of institutional investors' foreign exposure • Concentration risk/large exposure limits • Countercyclical capital buffer • Debt-to-income (DTI) ratio • Dynamic provisions • Expected loss provisioning • Foreign reserves accumulation • Foreign-exchange limits/effective net open foreign-currency position • Intervention in money, capital or FX markets (outright transactions, repos or swaps) • Leverage ratio • Liquidity facilities for systemic liquidity shortages or blockages (currently with banks only but potentially with key NBFIs in the near future) • Liquidity requirements (liquidity coverage ratio (LCR), cash reserve requirement (CRR), net stable funding ratio (NSFR)) • Loan-to-value (LTV) ratio • Macroprudential limit for Authorised Dealers • Recovery and resolution planning • Single remittance transactions

Annexure C

Table C.1: FSOC overview

Description and objectives	Membership composition	Functions
• The FSOC was established on 1 April 2018 as a statutory committee in terms of the FSR Act. • The primary objectives of the committee are to (i) support the SARB when it performs its functions in relation to financial stability; and (ii) facilitate cooperation and collaboration between the SARB and other financial sector regulators. • The FSOC meets at least twice a year, but the Governor may convene a meeting of the FSOC at any time when deemed necessary, and must convene a meeting if requested to do so by any one of the financial sector regulators.	The FSOC consists of: • the Governor as Chairperson; • the Deputy Governor responsible for financial stability matters; • the Chief Executive Officer (CEO) of the Prudential Authority; • the Commissioner of the FSCA; • the CEO of the National Credit Regulator (NCR), • the Director-General of National Treasury, • the Director of the Financial Intelligence Centre (FIC); and • up to three additional officials of the SARB appointed by the Governor (currently the Head of the Financial Markets Department, Head of the National Payment System Department and Head of the Financial Surveillance Department).	• Serve as a forum for SARB representatives and financial sector regulators and NT to be informed, and to exchange views on issues surrounding financial stability. • Make recommendations to the Governor on the designation of systemically important financial institutions. • Advise the Minister of Finance and the SARB on (i) steps to be taken to promote, protect or maintain, or to manage or prevent risks to, financial stability; and (ii) matters relating to crisis management and prevention. • Make recommendations to other organs of state regarding steps that are appropriate for them to take to promote financial stability and mitigating risks to financial stability. • The FSOC has a subcommittee, namely the Financial Sector Contingency Forum (FSCF), which was established as an informal industry body in 2002 and elevated to a statutory committee in the FSR Act in 2017 to ensure broad participation and engagement of stakeholder groups in defining and coordinating approaches to crisis management. • The FSCF's primary objective is to assist the FSOC with the identification of risks that could result in potential systemic events; and the coordination of appropriate plans, mechanisms and structures to mitigate those risks.

Instruments under the direction of FSOC members that may be used to protect and enhance financial stability could, for example, include financial system integrity (AML/CFT), minimum cash and terms to maturity requirements for money market funds, asset limits for pension funds etc.