

X P Guma: The Institute of Bankers in South Africa

Keynote speech by Dr X P Guma, Deputy Governor of the South African Reserve Bank, at the Institute of Bankers in South Africa's Annual Dinner, Johannesburg, 1 June 2006.

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Mr Chairman, Lawrence Mlotshwa; Mr President, Tom Boardman; Chief Executive Officer, Mr Mnisi; fellows of the Institute of Bankers, ladies and gentlemen, I wish to start my address by thanking the Institute for its invitation to me to be the keynote speaker tonight. Having last been invited to attend, let alone to speak on this occasion, almost ten years ago, I am somewhat anxious: for I am not sure about, I don't know with any certainty, the reasons for your gracious invitation. That said, I must also indicate that I assume that I have not breached the order of precedence of your organisation and hasten to declare that I proceed on the basis that all protocol has been observed.

The Institute of Bankers (IOB) in South Africa (SA)

The IOB is, I have been told, a world-wide association of bankers which meets biennially with the objective of providing education to the industry. In South Africa, this association has a history which dates back to 1904 and, through its use of heraldry establishes a link between past and present notions of precedence, excellence, discipline and service. "Finis coronat opus" states the logotype – in free translation, "the end crowns the work".

Two stories may, I think, usefully be told in support of my assertion: the link between past and present. The first goes as follows:

Once upon a time, in the 1970's, a young man secured a holiday job with a branch of a major banking institution in a small country. In that country, most people knew or knew of each other.

Being known to be bright, keen and energetic, the young man received neither training nor education from the managers of this branch of the major banking institution. Instead, they directed him to the "Waste Department" of the branch and advised him to "work hard".

On his first day on the job the young man – who was known to be bright, keen and energetic – watched in wonder as clients conducted their banking business; deposits, withdrawals, investments. And keenly observed the flow of vouchers and chits: pink or red for debits; green or blue for credits.

As the banking day drew to a close, a veritable flood of vouchers descended on the "Waste Department". And our hero – who was known to be bright, keen and energetic set to work. Shred the red ones he thought; save the green ones. This, after all, is the "Waste Department" of a major banking institution.

At approximately 2:45 p.m. that day, Nelly, the mentor arrived to assist our hero: he who was known to be bright, keen and energetic. She said: "We must now balance the total of the debits and the total of the credits in the accounts of the depositors ... And the investors"

He looked, with horror, at the pile of shredded pink chits in the waste-bin:

"file 13"; Nelly had said before leaving. He looked again at the sign above him: it still read "Waste Department"; and he left – never to return.

Now, had I been trained as a banker, this would never have happened. I would have known what was expected of the "Waste Department", independently of Nelly who wouldn't have mattered.

But I would not have been able to laugh as loudly as I did when, thirty something years later, I received a letter from the said bank stating that: We must conclude that your account was closed in the ordinary course of business..." They don't know what I know!

The South African banking industry needs an Institute of Bankers to protect its depositors and its young from Nelly – the mentor; and from young people who are bright, keen and energetic but prone to improvisation when bored and unrestrained.

The story of John Law: A second story

The story about John Law, as told by Professor J.K. Galbraith¹ runs thus:

Law, a Scotsman, arrived in France in 1716, in flight from a murder charge in England where he had been unduly successful in a duel. Having run through a considerable inheritance he had for some years made his living from gambling.

In France, however, he was able to persuade the authorities to grant him – and his brother – the right to establish a bank with capital of 6 million livres or about 250 000 English pounds: banking being then virtually unknown in France.

The bank was authorised to issue notes and did so – granting loans to the state. The government then used the notes to pay its expenses and pay off its creditors, whilst the banker – Law and brother – promised redemption in the currency of the weight of metal it contained at the date of issue of the paper. In other words, a classical fractional reserve bank.

All went well for some time. The financial position of the government was eased; prices began to rise; business and business confidence improved. The Banque Royale flourished.

Trouble arrived in 1719 when Law decided to found a company, the Mississippi Company, to exploit and bring to France the very large gold deposits which America was said to have in abundance.

To this end, he sold stock and shares to the general public, the intention being to use the proceeds to finance gold mining in America. The gold was to be added to the reserves of the Banque Royale to support an increased issue of notes – which notes had by now become a generalised means of exchange.

The problem lay with the French authorities. For the proceeds of the sale of stock went to them; not to the fictitious gold mines in America. Only the interest on the loans made to the authorities on the basis of the share issue was available to finance the said gold mines.

As Galbraith (p.35) notes:

“That the government of France was an even more unappealing investment than gold mining in the Louisiana swamps, or even that it and not Louisiana was the object of the investment went unnoticed – at least initially.” And Law, whose name was converted in French speech to the better-sounding Lass, became the most highly regarded man in France; on 5 January 1720, he was made Comptroller General of France, in recognition, it was said, of his financial genius.

Then the bubble burst. One prince, early in 1720, offended by his inability to buy stock at what he considered a fair price sent a pile of notes to the Banque Royale to be redeemed in hard currency. It was quite a pile, needing three donkey-carts for the journey. But, to cut a long story short, there was not enough hard money on hand at Banque Royale to redeem the notes.

Chaos ensued. Law's reputation was ruined; business became depressed; prices fell and a general depression ensued.

And what became of our financial genius, the Comptroller General of France? Why – he went to Venice and, having for a decade lived in decent poverty, a quiet and virtuous life, died there in the Catholic faith, piously receiving the Sacraments of the Church.

And the moral of this story is this:

The miracle of money creation by a bank may stimulate industry and trade – the upward phase of a business cycle in modern language – and give almost everyone a warm feeling of well being. But taken to excess, this miracle may result in a terrible day of reckoning. How to have the wonder without the reckoning? That is the question.

Mankind has progressed somewhat from the times of the 1720's with the creation of modern central banks whose functions typically include an element of oversight over the banking system. But the cupidity of certain people is eternal; and requires eternal vigilance. Beware of financial geniuses.

This, I would like to suggest to you, provides the best firm reason for the continued existence of the IOB. It must equip all those who are going to work in the banking system with the requisite set of

¹ *J.K. Galbraith (1975) Money: Whence it came, where it went, Penguin Books*

ethics with which to restrain people's greed and cupidity: and protect bright, keen and energetic young men – and women – from the ways of Nelly, the mentor, by providing them with the requisite training.

That done, we will all proudly be able to assert as we look back on our contributions to a safe and sound banking system, "Finis coronat opus".

Thank you for your attention. Ndi gqibile.