South African Reserve Bank

Opening remarks by Ms Fundi Tshazibana, Deputy Governor of the South African Reserve Bank at the Market Practitioners Group Forum
6 November 2020

Ladies and gentlemen, good morning and welcome to the Market Practitioners Group (MPG) Forum.

The MPG is a joint public and private sector body that was established by the South African Reserve Bank (SARB) to facilitate decision-making on matters relating to the reform of interest rate benchmarks in our country. Since its establishment in October 2018, the MPG has had various interactions with industry stakeholders and has set up substructures to craft the design of alternative interest rates in South Africa. The MPG also leads South Africa’s transition to a new and more robust interest rate dispensation. Importantly, the work of the MPG and its substructures, which I will allude to and contextualise shortly, forms part of a global agenda to strengthen existing interest rate benchmarks and identify alternative near risk-free rates.

Let me now briefly provide some context for those who may not be aware of the origins of the work on the reform of interest rates. In the major financial markets, reference rates, such as the London Interbank Offered Rate (Libor) and Euro Interbank Offered Rate (Euribor), are widely used as benchmarks for a large volume and broad range of financial products and contracts. These rates encountered episodes of attempted market manipulation and false reporting. This, together with the decline in liquidity in interbank unsecured funding markets after the global financial crisis (GFC), undermined confidence in the reliability and robustness of existing interbank benchmark interest rates.

These developments meant that the lack of integrity in the determination processes of some critical reference rates represented a serious source of vulnerability and systemic risk. As such, the Financial Stability Board undertook a fundamental review of major interest rate benchmarks.

In line with global developments, the SARB established the MPG following the publication of the 'Consultation paper on interest rate benchmarks in South Africa'. The consultation paper, among other things, considered whether there was a case for the reform of the Johannesburg Interbank Average Rate (Jibar) and explored the development of new benchmarks. The case for reforming the Jibar, which is the most widely used reference rate in South Africa and is therefore of systemic importance, was informed by a number of concerns, including that:

i. the Jibar is currently not underpinned by a large number transactions, which is a desirable and an essential characteristic of a benchmark interest rate according to the principles for financial benchmarks developed by the International Organization of Securities Commissions (IOSCO);
ii. market activity in three-month negotiable certificates of deposit (NCDs), which forms the basis of the most widely referenced three-month Jibar, has declined both in nominal terms and as a share of wholesale bank funding − currently, three-month NCD volumes make up less than 5% of NCD issuance; and
iii. the current calculation methodology for the Jibar is vulnerable to potential manipulation.

In addition to strengthening benchmarks to guard against potential malpractice, the SARB has also been cognisant of the role interest rate benchmarks play insofar as they serve as reference rates for a large number of financial contracts. This implies that they have a key role to play in the transmission of monetary policy decisions and the cost of (and remuneration of) capital in the broader economy.

While the SARB was initially at the forefront of the development of proposals on how this reform could be achieved, the mandate for determining a market-preferred choice of a reference rate to replace the Jibar was given to the MPG. The MPG was then organised in such a way that it comprises users of reference rates from different pockets of the market, including members of the savings industry, corporate treasuries, the banking sector and the official sector.

The MPG established five work streams, focusing on the different aspects of the project. These work streams include:

i. the Unsecured Reference Rate Work Stream, chaired by Mr Deon Raju from Absa;
ii. the Risk-Free Reference Rate Work Stream, chaired by Mr Andries du Toit from FirstRand;
iii. the Data Collection and Infrastructure Work Stream, chaired by Mr Ruan Roux from the SARB;
iv. the Transition Work Stream, chaired by Mr Paul Burgoyne from Standard Bank;
v. the Governance Work Stream, chaired by Ms Elmarie Hamman from the Financial Sector Conduct Authority; and recently
vi. the Communications Work Stream, chaired by Mr Zafar Parker from the SARB.

Collectively, the effort of these work streams and the Financial Markets Department of the SARB has culminated in an important body of work that will underpin South Africa's transition to alternative reference rates. We see this transition process as one which entails multiple and carefully sequenced steps, beginning with the stabilisation of the Jibar to secure the transition period. This is followed by the establishment of new rates and foundations for new markets, and then by the adoption of those rates before full transition takes place.

Thus far, the work of the MPG has largely focused on strengthening the current Jibar framework in line with the first step, as well as on finding new alternatives. This work has now been completed and the project is proceeding to the next phase which entails thinking about the most suitable transition approach to be adopted by South Africa. As its work is advancing, the MPG intends to keep all stakeholders informed of its progress and the next steps, and this is why we are here today. Thus, the purpose of today's MPG Forum is twofold:

- first, to report on and inform stakeholders of key decisions, considerations and recommendations made by the MPG in relation to the reform of the Jibar and the choice of an alternative overnight reference rate for South Africa; and
- second, to outline the envisioned transition process to an overnight rate as a key reference rate for the South African financial market.

As we engage in this conversation, I wish to reiterate the position the SARB has taken regarding the future of the Jibar. Earlier, I alluded to deficiencies in the current Jibar framework, which have led to the SARB taking a decision to reform the Jibar. The Unsecured Reference Rate Work Stream and later the Jibar Task Team have done commendable work in this regard, to ensure that the Jibar framework is strengthened to enhance its robustness. However, changes to the Jibar framework should not be understood as implying that the Jibar will continue indefinitely.

The SARB, as the benchmark administrator of the Jibar, has decided that the Jibar will cease at some future point. The enhanced framework will remain in place for a limited time, after which South Africa will transition to alternative reference rates. In the new interest rate dispensation, we expect that the key reference rate will be an overnight near risk-free rate, which may or may not co-exist alongside a risk-based term rate.

At this point I would like to hand over to my colleagues to share with you the decisions that have been taken thus far, their motivations as well as the trade-offs we have had to manage leading up to those decisions being taken.

Thank you.