Transformation of the financial sector

Presentation to the SCOF

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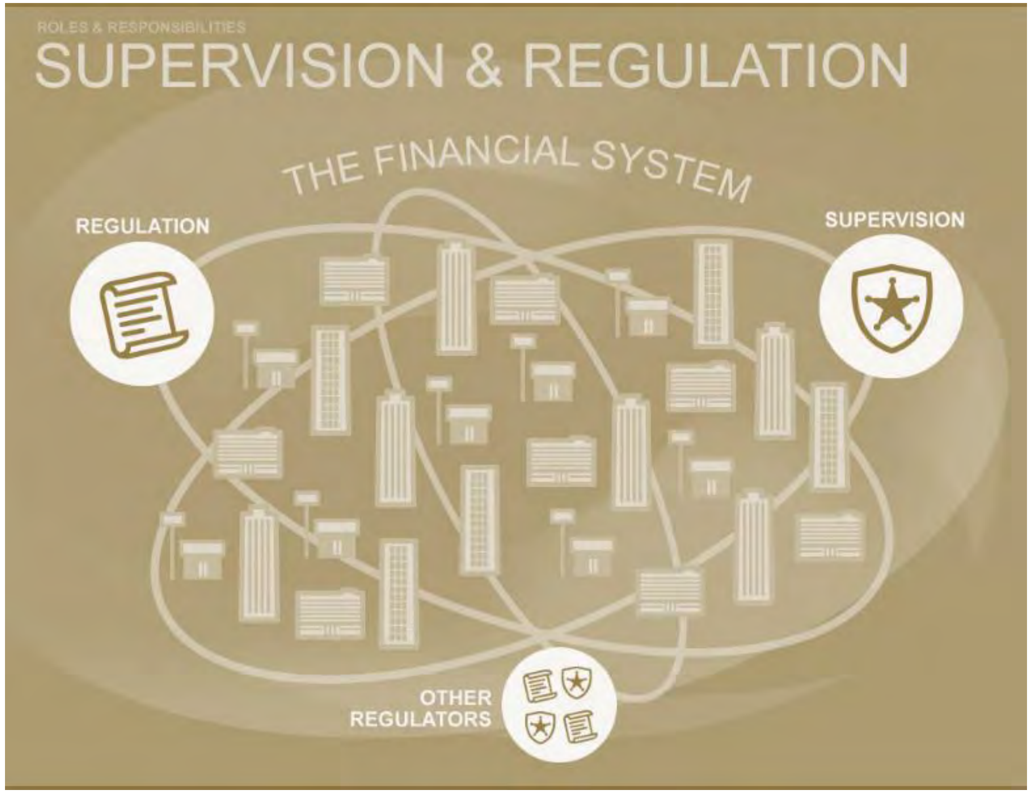
South African Reserve Bank

Prudential Authority

Overview of presentation

1. Overview of the mandate and objective of the PA
2. Overview of the PA Structure and Governance
3. Regulatory and supervisory strategy
4. The transformation agenda and the PA
5. Entities supervised by the PA
6. Update on the relevant sectors
7. Listing requirements for banks and insurers
8. What is the role of the prudential regulator in transformation
9. The Financial Sector Regulation Act, 2017
10. Transformation requirements of the Insurance Act
11. What is the model of transformation envisaged?
12. Understanding the role
13. Way forward



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Overview of the PA: Mandate and Objectives

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MANDATE

- **To promote and enhance the safety and soundness of financial institutions** (such as banks and insurers) and **Market Infrastructures** (such as central counterparties, central securities depositories, clearing houses, trade repositories and exchanges).
- **Responsible** for **protecting financial customers** against the risk of those institutions failing to meet their obligations.
- The **PA also assists the SARB** in maintaining **financial stability.**

OBJECTIVES

a	b	c	d
Safety and soundness	**Safety and Soundness**	**Protect**	**Assist SARB**
Promote and enhance the safety and soundness of financial institutions that provide financial products and securities services	Promote and enhance the safety and soundness of market infrastructures	Protect financial customers against the risk that those financial institutions may fail to meet their obligations	Assist in maintaining financial stability
Financial Institutions	**Market Infrastructures**	**Financial customers**	**Financial Stability**

- **Commercial Banks**
- **Mutual Banks**
- **Co-operative Banks**
- **Co-operative Financial Institutions**
- **Life-insurers**
- **Non-life insurers**
- **Exchanges**
- **Central Counterparties**
- **Trade Repositories**
- **Clearing Houses**
- **Central Securities Depository**

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Overview of the PA: Structure and Governance

Prudential Committee

- **Lesetja Kganyago**
  Governor & Chairperson of the Prudential Committee
  - **Kuben Naidoo**
    Deputy Governor and CEO of the Prudential Authority
  - **Fundi Tshazibana**
    Deputy Governor
    Markets and International
  - **Rashad Cassim**
    Deputy Governor
    Financial Stability

Prudential Authority Management

- **Suzette Vogelsang**
  Head: Banking, Insurance, Market Infrastructure and CFI Supervision
- **Faizel Jeena**
  Head: Risk Support
- **Denzel Bostander**
  Head: Financial Conglomerate Supervision
- **Unathi Kamlana**
  Head: Policy, Statistics and Industry Support

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Regulatory strategy and supervisory framework

- The PA's Regulatory Strategy 2018-2021, was adopted by the Prudential Committee and published on the SARB's website on 28 September 2018.
- The Regulatory Strategy deals with the PA's approach to regulation and supervision, the areas of immediate focus as well as areas of additional priorities

Approach to Regulation

give effect to the consultation requirements as stipulated in the FSR Act and ensure compliance with internationally agreed standards

Approach to Supervision

risk-based and proportional, forward-looking, outcomes-focused and integrated, underpinned by appropriate supervisory tools

Supervisory frameworks

Banks, insurers and MIs

To be developed – financial conglomerates, significant owners

Immediate Focus areas

1 – Strengthen the regulation and supervision of banking institutions

2 – Implement prudential regulation and supervision of financial conglomerates

3 – Prudentially regulate MIs

4 – Prudentially regulate and supervise insurers

5- Establish a framework for significant owners

6 – Conclude MoUs with the SARB and regulators

Additional priorities

- Supporting transformation
- Supporting sustainable competition in the provisions of financial services and
- supporting financial inclusion as well as development in financial technology (fintech)

Entities supervised by the Prudential Authority

Entities per sector	No. of entities
Banking sector	**34**
Registered banks	19
Local branches of foreign banks	15
Mutual bank sector	**4**
Co-operative sector	**26**
Co-operative banks	4
Co-operative financial institutions	22
Life insurance sector	**73**
Primary insurers	66
Cell captive entities	7
Non-life insurance sector	**86**
Primary insurers	73
Cell captive entities	5
Captive insurers	8
Reinsurers	**11**
Life reinsurers	3
Non-life reinsurers	3
Composite reinsurers	5
Total	**234**

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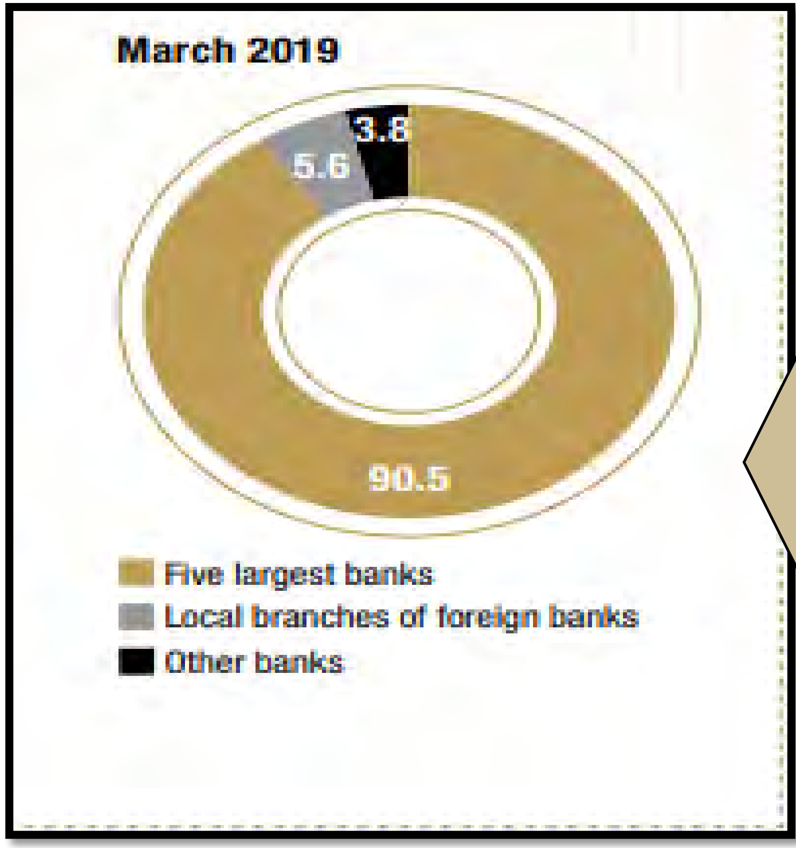
Banks

- 5 largest banks hold 90.5% of the total banking sector assets



<u>Designation of Systemically Important Banks (D-SIBs)</u>

- Quantitative methodology ranks the systemic relevance of banks in relation to each other.
- Use of supervisory judgement and discretion – to assess the level of significance
- Higher capital requirements for D-SIBS and intensified supervisory oversight
- Levels the playing field – comparing with smaller players
- Enhances competition

Total banking sector assets increased from **R5 201 billion** in March 2018 to **R5 654 billion in March 2019.**

The banking sector assets increased by **8.69%** in March 2019 from the previous year, mainly supported by the increase in gross loans and advances.

Member-based deposit taking institutions

Mutual Banks

The total mutual banking sector **assets** increased to

R3.136 million

in March 2019

(2018: R3.001 million).

The sector remained profitable during the period under review, although a declining trend in profitability was evident throughout the review period. Mutual banks remained adequately capitalised, with the total CAR well above the minimum statutory requirements.

Identifying the challenges being experienced under the current mutual banks framework, as well as the best approach to make supervision more relevant to the current ownership structures of mutual banks.

Co-operative banks and CFIs

Selected indicators for co-operative banks and CFIs

	Number		Members		Deposits R millions		Assets R millions	
February*	2018	2019	2018	2019	2018	2019	2018	2019
Co-operative banks	3	4	3 246	4 321	R128.8	R145.3	R153.5	R177.4
CFIs	23	22	24 618	23 170	R128.6	R149.1	R180.4	R192.1
Total	**26**	**26**	**27 864**	**27 491**	**R257.4**	**R294.4**	**R333.9**	**R369.5**

* *The financial year-end of all co-operative banks and CFIs is 28 February.*

Work being done on updating co-operative banks rules and development of prudential standards for CFIs

Insurers – Life, non-life and reinsurers

Selected indicators for the South African life insurance industry

R millions	Primary	Cell captives	Reinsurers	Total
Assets	2 993 436	10 768	7 256	3 011 459
Liabilities	2 630 845	3 602	3 900	2 638 348
Solvency capital requirement cover ratio (median)	1,9	1,1	1,5	**1,5**
Minimum capital requirement cover ratio (median)	4,3	4,1	5,3	**4,3**

Selected indicators for the South African non-life insurance industry

R millions	Primary	Cell captives	Captives	Reinsurers	Total
Assets	149 882	37 584	2 517	7 279	197 262
Liabilities	85 097	23 155	845	5 731	114 828
Solvency capital requirement cover ratio (median)	1,8	2,1	1,8	1,6	**1,8**
Minimum capital requirement cover ratio (median)	3,8	2,5	3,8	4,5	**3,8**

Composite reinsurers

Five reinsurers are currently classified as composite reinsurers, meaning that they write both life and non-life reinsurance businesses.

The gross premiums for the six months ending December 2018 in respect of the life and non-life businesses totalled R4.9 billion and R6.8 billion respectively.

Total assets

R34 billion

as at the end of December 2018.

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Financial market infrastructures

- The PA is responsible for the prudential supervision of market infrastructures.
- This category includes exchanges, central securities depositories, clearing houses, central counterparties (CCPs), and trade repositories.
- The reporting templates for market infrastructures' data submissions were published in January 2019, with the first set of data submissions to the PA being due by April 2019.
- The PA will report on market infrastructures' data in its 2019/20 Annual Report.

Licensed Prudential Authority-regulated market infrastructures

Exchanges	JSE Limited
	A2X (Pty) Ltd
	ZAR X (Pty) Ltd
	4 Africa Exchange (4AX) (Pty) Ltd)
	Equity Express Securities Exchange
Central securities depositories	Strate (Pty) Ltd
	Granite
Clearing houses	Strate (Pty) Ltd
	JSE Clear

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Financial Sector Regulation Act, 2017

- Promulgated on 22 August 2017
- Gave effect to the Twin Peaks Model

- Established the PA and the FSCA on 1 April 2018
- Formalised the financial stability mandate of the SARB

7. Object of Act

(1) The object of this Act is to achieve a stable financial system that works in the interests of financial customers and that supports balanced and sustainable economic growth in the Republic, by establishing, in conjunction with the specific financial sector laws, a regulatory and supervisory framework that promotes:-

(a) financial stability;

(b) the safety and soundness of financial institutions;

(c) the fair treatment and protection of financial customers;

(d) the efficiency and integrity of the financial system;

(e) the prevention of financial crime;

(f) financial inclusion;

(g) transformation of the financial sector; and

(h) confidence in the financial system.

(2) When seeking to achieve the object of this Act, the Reserve Bank and the financial sector regulators must not be constrained from achieving their objectives and responsibilities as set out in sections 11, 33 and 57.

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What is the role of the prudential regulator in transformation?

- Prudential regulators have a direct role to play:
  - Entrants into the sector – Licensing
  - Development of a financial institution - Promote and enhance safety Financial sector data - Supervision
  - Products offered to consumers - Supervision
  - Ensuring compliance - Enforcement
  - Exit from the sector – Resolution
- The role of the prudential regulatory in transformation can only unfold within the regulator's legislative mandate

Licensing:
Reduce barriers for entry and promote competition – risk based approach

Licensing:
Allow for a variety of types of financial institutions – microinsurers, co-ops, CFIs, mutual banks

Licensing:
Consider transformation targets when licensing – specifically provided for with regard to insurers

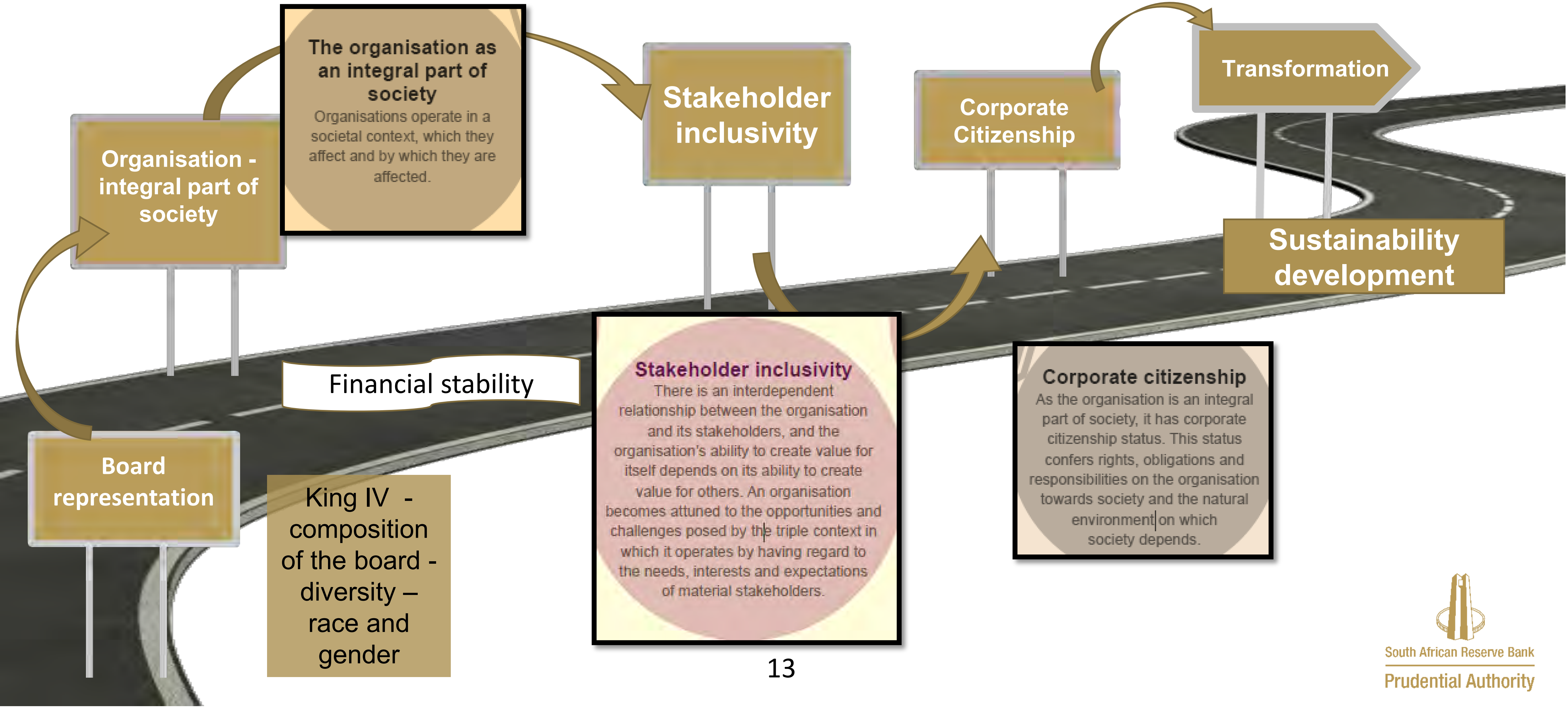
Supervision: Proportional and risk based
Progressive realisation of prudential requirements - insurers

Supervision: Obtain and analyse transformation data

Supervision:
Monitor transformation targets

Supervision: Products that promote access and financial inclusion

Listing requirements for banks and insurers



What is the model of transformation we envisage?

Licensing

- Engage with NT to consider a tiered approach to banking and insurance which will reduce capital requirements for simpler business models and allow more entrants into the sector
- More entrants will promote competition in the sector
- Competition will promote access to financial services

Supervision

- Proportional supervision – allows for growth in sector
- Monitor transformation targets - catered for in the insurance sector – extend to banking and FMIs

Developmental

- Allow financial institutions or fintech companies to experiment with financial technology dealing with the provision of financial products and financial services in a safe environment – allows for new methods to promote access to financial services (financial inclusion) and promote competition

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Transformation requirements of the Insurance Act, 2017

Definition of Transformation

IA defines "transformation of the insurance sector" as transformation as envisaged by the FSC issued in terms of section 9(1) of the BBBEEA.

The IA provides for transformation <u>in the objective of the Act, requirements for conversion of existing registrations and new licences variation of licencing conditions and exemptions.</u>

Licensing

Allowing for progressive compliance with the requirements of the IA.

This can be achieved by licensing conditions and exemptions that will consider the transformation plans submitted by the applicant

Supervision

Entrenching the principle of proportional supervision

The regulatory requirements are applied in a manner which is proportional to the nature, scale and complexity of the risks inherent in the business

Dedicated prudential standards

Understanding the role

- Through checks and balances

Role	Checks and balances
Reducing barriers to entry – based on simple business models – strengthen tiered financial system	Do not compromise on safety and soundness of financial institutions
More entrants – increased competition	Do not compromise on financial stability and safety and soundness of financial institutions.
Proportional supervision	Forward looking, risk and outcomes based
Encourage fintech in provision of financial products and services	Promote regulatory and supervisory objectives – work being done by the IFWG

Way forward

- Integrating regulatory and supervisory process to incorporate transformation
- Strengthen the CFIs, Mutual Banks and Co-operative Banks framework to ensure proportional supervision and attainable entrance to the sector
- Co-operate and collaborate with other regulators on transformation agendas
- Engage with National Treasury on tiered banking

Discussion