South African Reserve Bank

ANNUAL REPORT 17/18

PROMOTING THE ECONOMIC WELL-BEING OF SOUTH AFRICANS

CONTENTS

FEEDBACK

The SARB welcomes feedback on its annual report to inform the continuous improvement of its communication to stakeholders. Your feedback, comments and/or questions can be sent to Sheenagh Reynolds, the Secretary of the SARB, at Sheenagh.Reynolds@resbank.co.za.

ONLINE

The annual report can be accessed at: https://www.resbank.co.za/Publications/Reports/Pages/Annual-Reports.aspx

ABOUT THE SARB

FOUNDED IN 1921, THE SOUTH AFRICAN RESERVE BANK (THE SARB) IS THE **OLDEST CENTRAL BANK IN AFRICA.**

FOLLOWING ITS FIRST ISSUE OF BANKNOTES TO THE PUBLIC ON 19 APRIL 1922, THE SARB SHORTLY THEREAFTER BECAME THE SOLE ISSUER OF BANKNOTES IN SOUTH AFRICA.

Today, the SARB has over 760 private shareholders who have limited rights, namely to consider the SARB's annual financial statements, elect seven of the eleven non-executive directors of the Board, and appoint the external auditors and approve their remuneration. The shareholders have no rights or involvement in the conduct of monetary policy, financial stability policy or banking regulation. SARB shares are transferred by way of an over-the-counter share-trading facility maintained by the SARB.

After allowing for certain provisions, payments of company tax on profits, transfers to reserves and prescribed dividend payments; any remaining surplus is paid to the South African Government. The SARB is, therefore, not driven by a profit motive but by serving the best interests of the people of South Africa.

The SARB's head office is in Pretoria, where it conducts its annual Ordinary General Meeting (AGM) of shareholders. It also operates cash centres in Cape Town, Durban and Johannesburg.

The SARB is regulated in terms of the South African Reserve Bank Act 90 of 1989, as amended (SARB Act), read with section 223 of the Constitution of the Republic of South Africa, Act 108 of 1996 (the Constitution). The SARB's primary mandate and independence are entrenched in sections 224 and 225 of the Constitution.

VISION

The SARB leads in serving the economic well-being of South Africans through maintaining price and financial stability.

MISSION

To protect the value of the currency in the interest of balanced and sustainable economic growth in South Africa.

VALUES

The SARB actively encourages and strives towards the following values:

- RESPECT AND TRUST
- OPEN COMMUNICATION
- INTEGRITY
- ACCOUNTABILITY
- EXCELLENCE

MANDATE

CONSTITUTIONAL

Achieve and maintain price stability.

STATUTORY

Protect and enhance financial stability.

ABOUT THIS REPORT

The SARB is pleased to present its annual report for the year ended 31 March 2018. This report forms part of the SARB's public accountability and responsibility to a broad range of stakeholders. It provides readers with a holistic account of the SARB's strategy, performance and impact on society. It therefore contains financial and non-financial information that is material to the SARB's ability to sustainably implement its mandate.

The intended readers of this report are principally the Members of Parliament of South Africa and specifically the Standing Committee on Finance, through which the SARB is accountable to the people of South Africa, as well as the SARB's shareholders. The report is also considered relevant to a broader readership interested in how the SARB implements its mandate.

SCOPE AND BOUNDARY

THE SARB GROUP

The SARB

THE SOUTH AFRICAN RESERVE BANK

Wholly owned subsidiaries

- The South African Mint Company (RF) Proprietary Limited (South African Mint), including its subsidiary Prestige Bullion (RF) Proprietary Limited
- The South African Bank Note Company (RF) Proprietary Limited (SABN)
- The Corporation for Public Deposits

Associate

- African Bank Holdings Limited (ABHL)

The SARB's relationships beyond this boundary contribute significantly towards its ability to create value through achieving its mandate. These relationships are discussed throughout the report.

REPORTING CHANGES ALIGNED TO STRATEGY

The SARB's strategy aims to ensure that it remains a relevant and forward-looking central bank. The strategy comprises clear and measurable strategic focus areas (SFAs), strategic objectives and strategic initiatives for the medium term. The structure of this year's annual report reflects the SARB's strategic plan to 2020. An overview of the strategic plan is included on page 7 and more detailed discussions on how the SARB manages its strategy and performance against its SFAs and strategic objectives start on page 14.

CHANGES TO GROUP OPERATIONS

The Financial Sector Regulation Act 9 of 2017 (FSRA) was enacted on 22 August 2017, marking a significant milestone in the implementation of the Twin Peaks framework of financial regulation and paving the way for the introduction of the Prudential Authority on 1 April 2018.

PRUDENTIAL AUTHORITY'S INITIAL REPORT
PG 45

REPORTING FRAMEWORKS

The following best reporting practice frameworks have been used to guide and prepare the report.

The King Report on Corporate Governance in South Africa 2016 (King IV)

International Financial Reporting Standards (IFRS): in compiling and presenting its annual financial statements, the SARB has elected to use IFRS as a guide, except where IFRS conflicts with the provisions of the SARB Act. In such instances, the SARB Act takes precedence. The SARB's summarised Group annual financial statements, starting on page 80 of this report, provide further detail.

The International Integrated Reporting Council's Integrated Reporting Framework

The principles of each framework are balanced against their practicality and relevance to a central bank, taking into account overriding legislation and confidentiality requirements.

ASSURANCE

The summarised Group annual financial statements presented in this report, and the full Group annual financial statements available on the SARB's website, have been independently audited by the SARB's external auditors – PricewaterhouseCoopers Inc. and SizweNtsalubaGobodo Inc.

APPROVAL

The determination of material matters for inclusion in this report is undertaken at executive level, with due consideration of stakeholders' information requirements, and with oversight provided by the Board of Directors (the Board).

The Audit Committee and the Board have reviewed this report. In the Board's opinion, the report provides a fair and balanced account of the Group's performance and material matters. The Group annual financial statements for the year ended 31 March 2018 were approved by the Board on 8 June 2018 and signed on its behalf by:

E L (LESETJA) KGANYAGO
GOVERNOR OF THE SARB

SERVING THE ECONOMIC WELL-BEING OF SOUTH AFRICANS

THE SARB'S MANDATE

CONSTITUTIONAL

The Constitution prescribes the primary mandate of the SARB, which is to protect the value of the currency in the interest of balanced and sustainable economic growth. **Achieving and maintaining price stability** contributes towards the stability of the entire financial system.

The SARB continually considers the inter-relationships between price and financial stability to ensure that decisions relating to one do not unduly negatively impact on the other.

STATUTORY

The FSRA formally mandates the SARB to **protect and enhance financial stability** in South Africa. Through the Prudential Authority, the Act expands the SARB's regulatory responsibility beyond licensed deposit-taking institutions.

KEY FUNCTIONS

- Formulating and implementing monetary policy
- Issuing and destroying notes and coin
- Promoting financial stability which includes acting as the lender of last resort in exceptional circumstances
- Managing the official gold and foreign-exchange reserves of the country
- Regulating and supervising financial institutions, including banks and insurance entities
- Undertaking economic data analysis and research
- Ensuring the effective functioning of the National Payment System (NPS)
- Administering the country's remaining exchange controls
- Acting as banker to the government

STRATEGIC PLAN

The SARB's four-year strategic plan sets out what the SARB intends to do to achieve its vision and mission and execute its mandate.

STRATEGIC PLAN
PG 7

STRATEGY AND RISK MANAGEMENT, AND GOVERNANCE underpin the SARB's ability to sustainably execute its mandate

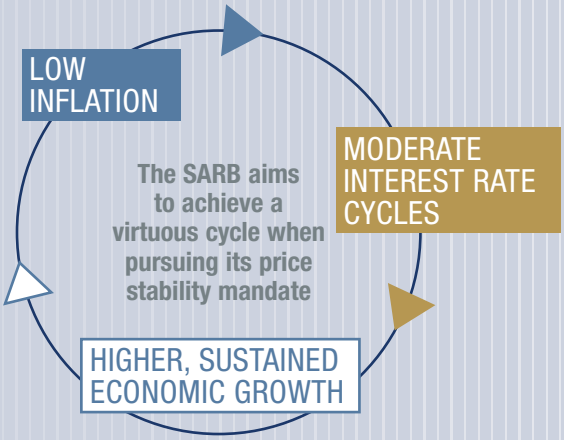
The SARB Act and associated regulations set the framework and structure of the SARB, the way in which it is managed and the actions it may take.

STRATEGY AND RISK MANAGEMENT, AND GOVERNANCE REPORTS PGs 14 and 66 respectively

MAINTAIN THE CONSUMER PRICE INDEX (CPI) WITHIN A TARGET OF

3–6%

The South African Government, in consultation with the SARB, sets an inflation target which serves as a yardstick against which price stability is measured. The SARB can independently use any instruments of monetary policy at its disposal to achieve this goal.



HOW PRICE STABILITY SERVES THE ECONOMIC WELL-BEING OF SOUTH AFRICANS

A MONETARY POLICY STANCE THAT PROVIDES A LOW AND STABLE INFLATION ENVIRONMENT:

> protects the purchasing power and living standards of all South Africans, particularly the poor;

> supports sustainable and balanced economic growth;

> contributes to South Africa's ability to create employment;

> facilitates general trust in the value of the rand and provides a favourable environment for investment in South Africa; and

> helps to maintain and improve South Africa's international competitiveness.

MONETARY POLICY PG 26

IN PROMOTING FINANCIAL STABILITY, THE SARB STRIVES TO:

01 Monitor the financial system

02 Mitigate risks to financial stability

03 Restore or maintain financial stability if a systemic event occurs or is imminent

HOW FINANCIAL STABILITY SERVES THE ECONOMIC WELL-BEING OF SOUTH AFRICANS

A STABLE AND SAFE FINANCIAL SYSTEM:

> is an important precondition for sustainable economic growth and development, and employment creation;

> contributes towards the system's resilience to vulnerabilities and shocks; and

> promotes efficient financial intermediation through sound financial institutions and market infrastructures.

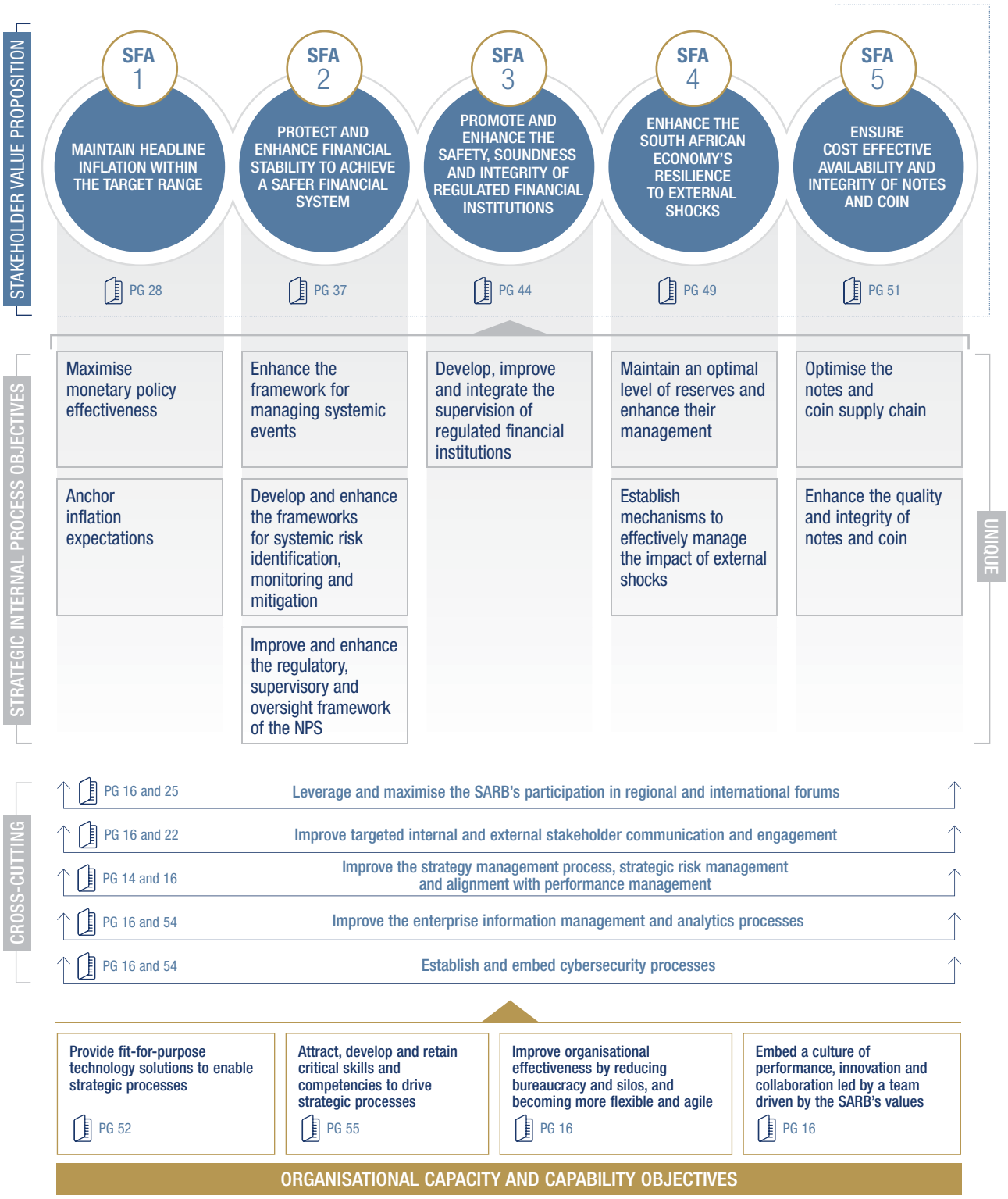
FINANCIAL STABILITY PG 34


BUSINESS PLAN

STRATEGIC PLAN

THE SARB STRATEGY MAP

The SARB's strategy map sets out its five strategic focus areas and supporting strategic objectives. These SFAs and objectives do not represent the entire work of the SARB. Instead, they create focus and a manageable strategic agenda, distilling the most important work required to deliver the SARB's mandate. The strategy map illustrates the relationships between the SFAs and strategic objectives across three interrelated perspectives, and provides a simple, standardised and visually-powerful way of communicating the strategy across the SARB.



PERFORMANCE OVERVIEW FOR THE YEAR ENDED 31 MARCH 2018

STRATEGY HIGHLIGHT

The SARB reviewed its strategy and found the design to be sufficiently robust in responding to internal and external environmental factors, however, more effective coordination and execution of the large, complex, enterprise-wide projects is needed. Greater focus will be placed on financial technology (fintech), exponential technologies, cybersecurity, data and information management, communication, stakeholder engagement and the changing world of work[1].

PG 14

SFA 1

MAINTAIN HEADLINE INFLATION WITHIN THE TARGET RANGE

Performance

Average inflation rate

4.7%

within the 3–6% target range.

Financial impact

The repurchase rate (repo rate) is the primary tool used by the SARB to maintain headline inflation within the target range. The SARB engages in various open market operations to give effect to the policy rate. These include repo and reverse-repo transactions, the issue of SARB debentures, the transfer of public sector funds between the SARB and the market and foreign-exchange swaps.

Other factors which impact liquidity management include market demand for notes and coin, the cash reserve balances that commercial banks must hold with the SARB and foreign-exchange spot transactions. The net effect of these factors is recorded on SARB's statement of financial position as accommodation to banks.

The implementation of the monetary policy was executed smoothly during the year through open market transactions to give effect to the decisions of the Monetary Policy Committee (MPC). These market and investment management operations impact the SARB's financial performance through interest earned on assets, primarily foreign reserves and outstanding repo transactions. Interest paid on liabilities, primarily local government deposits, call deposits and foreign deposits received, also impacts financial performance.

1. *Changes in the work environment include technology advances such as artificial intelligence, machine learning and robotics; and a multi-generational, connected, flexible and mobile workforce.*

SFA 2

PROTECT AND ENHANCE FINANCIAL STABILITY TO ACHIEVE A SAFER FINANCIAL SYSTEM

Performance

There were no systemic risk events in the financial system.

Financial impact

The SARB enhances protection provided to small retail depositors and is consulting with stakeholders on the structure and funding arrangements of the deposit insurance scheme. It is envisaged that the scheme will be a wholly owned subsidiary of the SARB. Initiatives are underway to ensure that the scheme has minimal cost impact on the industry and the SARB, while providing a public benefit.

SFA 3

PROMOTE AND ENHANCE THE SAFETY, SOUNDNESS AND INTEGRITY OF REGULATED FINANCIAL INSTITUTIONS

Performance

All significant financial institutions met or exceeded the quantitative prudential standards, having sound governance, compliance and risk management practices. Non-significant financial institutions that have not met the quantitative prudential standards, or which do not have sound governance or compliance and risk management practices, are under specific regulatory action.

Financial impact

Subsequent to year-end, the Prudential Authority was officially established as a juristic person operating within the SARB on 1 April 2018. The full financial effect of the Prudential Authority will commence in the new financial year and the costs attributable to the unit are expected to be fully recovered from levies in 2019/20.

SFA 4

ENHANCE THE SOUTH AFRICAN ECONOMY'S RESILIENCE TO EXTERNAL SHOCKS

Performance

Accumulated adequate levels of official gross gold and foreign-exchange reserves in accordance with adequacy guidelines.

Growth in foreign reserves

US$3.4 billion

(2017: US$0.2 billion decrease)

Financial impact

One of the ways in which countries can enhance their resilience to external shocks is to hold foreign reserves as financial buffers. The SARB has successfully grown gold and foreign-exchange reserves during the reporting period to just under US$50 billion. The year-on-year decline in the rand value of the official gross gold and foreign-exchange reserves of R25 billion (2017: R71 billion) was mostly due to the appreciation of the rand and a decrease in the statutory gold price.
The growth in the US dollar value of gold and foreign reserves was attributable to National Treasury foreign currency deposits, a valuation increase due to the depreciation of the US dollar against major currencies, an increase in the US dollar gold price and other reserve accumulation activities.

GOLD AND FOREIGN-EXCHANGE HOLDINGS

	2018 US$m	2017 US$m	**2018 Rm**	2017 Rm
Gold coin and bullion	**5 330**	4 999	**63 253**	66 338
Special drawing rights holdings	**2 600**	2 426	**30 855**	32 200
Foreign-exchange reserves	**42 049**	39 185	**498 961**	520 009
	49 979	46 610	**593 069**	618 547

SFA 5

ENSURE COST EFFECTIVE AVAILABILITY AND INTEGRITY OF NOTES AND COIN

Performance

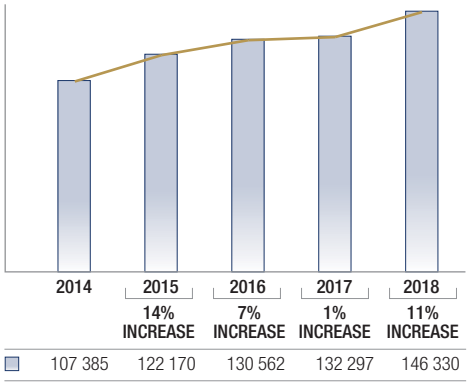
The SARB embarked on two major initiatives:

- The implementation of the cash management strategy, including a demand-driven cash replenishment model.
- The preparation for the Nelson Mandela commemorative coin and banknote series.

The SARB recorded a R378 million decrease in the cost of currency through reduced orders and the use of buffer stocks. It is anticipated that orders will increase significantly in the next financial year as the cash management strategy is executed.

The R14 billion year-on-year increase in notes and coin in circulation was mostly due to increased demand. Order fulfilment to the cash industry was 100%.

NOTES AND COINS IN CIRCULATION (Rm)



FINANCIAL HIGHLIGHTS

Group profit before tax
R3.2 billion
2017: R2.1 billion

The SARB recorded a profit before tax of R1.9 billion, a marginal increase of R43 million compared to the prior year.

The South African Mint had an excellent year, contributing profit before tax of R952 million (2017: R668 million) to the Group, primarily on the back of a successful 50-year anniversary campaign for the Krugerrand.

In line with the SARB Act **a dividend of R0.2 million was paid to SARB shareholders.**
(2017: R0.2 million)

The SARB transferred R1.4 billion from current year profits to the contingency reserve in terms of the SARB Act to rebuild the reserves.

The SABN made a minor loss before tax of R8 million (2017: R174 million profit), largely due to reduced production. **A return to profitability is expected in 2018/19.**

The SARB's 50% shareholding in ABHL, which came about as part of facilitating the resolution of African Bank Limited, **contributed R424 million** to the Group's profits, largely offsetting the prior year's loss of R556 million.

PG 81 and 82

IT HIGHLIGHTS

Completed a number of major IT initiatives that support the SARB's SFAs, including the successful upgrade of the data centre at the SARB's head office and a mobile application giving users access to current and historical Quarterly Bulletins.

Implemented the base infrastructure of Security Incident and Event Management technology to support effective monitoring of system security and guard against cybercrime.

PG 52

HUMAN RESOURCES HIGHLIGHTS

Conducted two employee surveys to gain insight on how the SARB can improve the employee experience.

Spent

R35 million

on training and development, reaching **80% of the workforce**.

Completed the alignment of the performance contracts of departmental heads to the SARB's strategy and cascaded performance objectives to all managers.

The coverage ratio of critical roles improved to

80%

(2016/17: 68%)

Regrettable turnover ratio improved to

1.17%

(2016/17: 1.46%)

PG 55

SOCIAL INITIATIVES

Granted external bursaries to tertiary students valued at

R5.9 million

(2016: R4.2 million)

Of the 58 students granted bursaries, 49 are black (African, Coloured and Indian) and 33 are women.

Extended the MPC Schools Challenge to seven provinces, with schools in the Eastern Cape, North West and Northern Cape provinces participating for the first time.
The challenge will be extended to KwaZulu-Natal and the Western Cape provinces during the 2018/19 financial year.

PG 60

GOVERNOR'S MESSAGE

E L (LESETJA) KGANYAGO

It gives me great pleasure to again present to South African citizens, shareholders and other stakeholders the annual report of the SARB for the financial year ended 31 March 2018. This report provides a comprehensive overview of the work of the SARB and its subsidiaries, as well as the summarised financial statements of the Group.

This past year was characterised by periods of heightened domestic political uncertainty. Nevertheless, the SARB remained focused on its primary objectives to achieve and maintain price and financial stability. During the reporting period, there was a marked improvement in inflation outcomes. Inflation was within the target range for the entire financial year, at an average of 4.7%, and it is expected to remain within the target range of 3–6% for the rest of the forecast period ending 2020. The more benign inflation performance is attributable in part to the stronger currency and the dissipation of the impact of the drought on food prices. Although inflation reached a low of 3.8% in March, this is expected to be the bottom of the current cycle, as the impact of the value-added tax (VAT) increase and higher petrol prices is likely to be felt soon.

An important focus of our activities was to get inflation expectations to decline and move closer to the mid-point of the target range. Inflation expectations are an important determinant of wage- and price-setting in the economy, and for a number of years these expectations have been stuck at the upper end of the target range. In the first quarter of 2018, we saw a marked moderation of these expectations in the various measures of expectations. While it is still too early to say that expectations have declined on a sustained basis, it is a promising development.

South Africa's gross domestic product (GDP) growth surprised on the upside during 2017, having recorded growth of 1.3%. This despite a contraction in the first quarter. Although a stronger performance of around 1.7% is expected during 2018, growth is expected to remain below potential, and insufficient to make inroads into the high unemployment rate.

The combination of the improved inflation outlook and below-potential growth gave the MPC some room to ease the stance of monetary policy and provide some support at the margin to economic growth. In July 2017 and March 2018, the MPC reduced the repo rate by 25 basis points on each occasion to its current level of 6.5% per annum. In line with its strategic objective, the committee will remain focused on ensuring the headline inflation remains close to the mid-point of the inflation target range on a sustained basis. A detailed report on monetary policy and the rationale for the policy stance can be found on pages 26 to 32.

The SARB's role in maintaining, promoting and enhancing financial stability has been given formal expression in the enactment of the FSRA in August 2017. The Act confers on the SARB an expanded regulatory role in the financial sector, at both the microprudential and macroprudential levels. In accordance with the Act, the Prudential Authority was officially established within the SARB on 1 April 2018.

While the banking system remains well capitalised and the financial system did not show significant signs of stress during the year, there were a number of well-publicised event risks, none of which were assessed to be systemic in nature. First, the announcement of an investigation into accounting irregularities at Steinhoff International Holding NV saw a collapse in its share price. While there may be some impact of a potential default on the company's debt exposure on South Africa's banking system, this exposure is relatively limited, and mainly concentrated in foreign banks. Second, a report on Capitec Bank and subsequent short-selling of the bank's shares caused some volatility in the share price. However, the SARB's view is that the bank is well capitalised and has ample liquidity.

Third, in March 2018, following signs of a severe liquidity crisis, the SARB placed VBS Mutual Bank under curatorship with the aim of protecting the interests of depositors. Subsequent to this step, the SARB has instituted a forensic investigation into possible fraud or material misstatements.

At the time of publication of this annual report, the curatorship and the investigations were still underway. Given the size of VBS Mutual Bank and its limited interconnectedness with the rest of the financial sector, it is not assessed to pose a systemic risk.

The SARB was unfortunately not immune to attempts to undermine and capture state institutions. During the past year, the SARB faced challenges to its independence as well as to its ownership structure. Often the two issues are confused in people's minds.

The challenge to the SARB's primary mandate and monetary policy independence, which is enshrined in the Constitution, came from an unexpected source. The Public Protector, in her ruling on the legality of the SARB 'lifeboat' to Bankorp over 30 years ago, argued that Absa, as the purchasing bank, was liable to repay the facility. However, her binding remedial action called for a change in the SARB mandate, from price stability to one of "ensuring that the socio-economic well-being of the citizens are protected". This would have required a Constitutional amendment. We challenged these findings and proposed remedial actions in court and the judgement went in our favour and the report was set aside. We will continue to vigorously defend challenges to our independence and Constitutional mandate, and we shall do so by drawing strength from fellow South Africans whose long-term interest inform our actions.

The proposed nationalisation of the SARB, by contrast, has little to do with our core mandate. Private shareholders currently have very limited rights, and have no role whatsoever in policymaking and execution. This is the preserve of the Governor and Deputy Governors, who are appointed by the President. While shareholders can vote for Board members, the majority of the Board is appointed by government. In any event, the Board itself is strictly a governance Board and plays no role in policy formulation. The SARB functions in the public interest; private shareholders and their representatives on the Board have no influence whatsoever on monetary policy, financial stability or banking regulation. Private shareholders do, however, represent an additional layer in the governance framework, and this helps strengthen accountability and transparency. Furthermore, shareholder-elected Board members add valuable expertise and inputs to the operations of the SARB.

Nationalising the SARB would also be expensive as its shares currently trade for much less than the price at which some existing shareholders are willing to sell their shares. The 'buying-out' of existing shareholders will therefore result in paying large sums of money to effect cosmetic changes that will have no bearing on the manner in which the SARB carries out its mandate or executes its policy responsibilities. Irrespective of shareholding structure, the primary mandate of the SARB and its independence will remain unchanged.

Despite these domestic challenges, the SARB has enjoyed some global recognition. I was honoured to be appointed as Chairperson of the International Monetary and Financial Committee, which is the policy advisory committee of the Board of Governors of the International Monetary Fund. Furthermore, I was named Central Bank Governor of the Year by Central Banking Publications. Although these honours were bestowed on me in person, they do not belong to me. They are a reflection of the people who stand behind me and a recognition of the SARB's institutional strength.

I am pleased to report that the SARB remained profitable for the fourth consecutive financial year. The Group recorded after-tax profit of R2.4 billion compared with R1.4 billion in the previous financial year. The SARB itself accounted for R1.4 billion of this total, while the remainder of this profit came from the South African Mint – mainly due to the successful 50-year anniversary campaign for the Krugerrand – and from ABHL. However, as we always note, the SARB does not have a profit-maximising objective, and our operations are conducted in pursuit of our mandate and objectives, in the interest of the country. We will, however, continue to strive for operational efficiency and good governance.

The SARB did not operate with a full Board for the past year. The terms of office of three government-appointed non-executive directors expired during 2017. Dr Terence Nombembe was re-appointed for a further term in July 2017. Dr Tania Ajam was not available for re-appointment and Ms Maureen Manyama resigned at the end of July. The latter two positions were still vacant at financial year-end. With respect to shareholder-elected non-executive directors, Mr Rob Barrow, Prof Rochelle le Roux and Mr Gary Ralfe were all re-elected at the 2017 AGM. The term of office of Mrs Venete Klein expires at the 2018 AGM and she has indicated that she is not available for re-election. A new Board member will therefore be elected by shareholders at the AGM from a shortlist compiled from nominations received by the Panel established in terms of the SARB Act.

This has once again been a difficult year, but the SARB has been able to contend with the challenges faced. This has been a strong team effort, and I would like to extend my sincere thanks and appreciation to the non-executive directors, the Deputy Governors and all employees for their hard work and commitment to this important institution. I have no doubt I can continue to rely on them for unwavering support and dedication in the execution of our mandate and objectives, in the interest of all South Africans.

E L (LESETJA) KGANYAGO
GOVERNOR

STRATEGY MANAGEMENT

The successful execution of the SARB's strategy will ensure that it continues to meaningfully contribute towards the economic well-being of all South Africans by achieving its mandate.

In 2016, the SARB adopted a new strategy management framework and four-year strategic plan. Two years into this journey, the design of the strategic plan has remained fairly consistent, however, a stronger focus has been placed on both executing and tracking the strategy. The SARB is on track to achieve its 2020 targets.

Through the continual development and improvement of its strategy management framework, and associated processes and systems, the SARB is working towards a strategy-focused organisation where:

- the strategic plan and strategy management framework are continually embedded into the everyday lives of its employees;
- its departments work together and within the broader external eco-system to execute the strategic focus areas (SFAs) and strategic initiatives; and
- change is driven and supported by the SARB's leadership team, culture and employees.

STRATEGY DESIGN

The 2020 strategic plan, summarised on page 7 drives the achievement of both price and financial stability. The five SFAs and their supporting strategic objectives prioritise key areas of work and provide a manageable strategic agenda against which performance can be measured.

SFA 1 — MAINTAIN HEADLINE INFLATION WITHIN THE TARGET RANGE

The objective is to achieve and maintain price stability in the interest of sustainable and balanced economic growth. Two strategic objectives support SFA 1. The first is to maximise monetary policy effectiveness by continuing to develop a policy-relevant and structured research programme, which focuses on SFA 1 and better understands the synergies between the SFAs, specifically SFAs 1, 2 and 4. The second objective is to anchor inflation expectations by continually building the SARB's stakeholder engagement programme through more effectively targeting sectors and groups that influence price setting.

SFA 2 — PROTECT AND ENHANCE FINANCIAL STABILITY TO ACHIEVE A SAFER FINANCIAL SYSTEM

This is the SARB's main responsibility in terms of its financial stability mandate. When financial stability risks are managed well, systemic financial crises are less likely to occur, and are more easily managed if they do occur, mitigating the spill-over effects on the broader economy and society. Three strategic objectives support SFA 2. The first is to establish and enhance frameworks to manage systemic events; the second is to develop and enhance frameworks for systemic risk identification, monitoring and mitigation; and the third to enhance the regulatory, supervisory and oversight framework of the National Payment System (NPS).

SFA 3 — PROMOTE AND ENHANCE THE SAFETY, SOUNDNESS AND INTEGRITY OF REGULATED FINANCIAL INSTITUTIONS

The Prudential Authority was established on 1 April 2018 in terms of the FSRA, which introduces the Twin Peaks approach to financial regulation. Twin Peaks has two main aims – to strengthen the safety and soundness of financial institutions and to better protect financial customers and ensure that they are treated fairly by financial institutions (market conduct). SFA 3's strategic objective is to further establish and embed the Prudential Authority, which will consolidate the prudential regulation and supervision of financial conglomerates, banks, insurers and financial market infrastructures (FMIs) in the SARB.

SFA 4 — ENHANCE THE SOUTH AFRICAN ECONOMY'S RESILIENCE TO EXTERNAL SHOCKS

Resilience to external shocks is the ability to maintain price and financial stability when adverse external events occur. Two strategic objectives support SFA 4. The first is to maintain an optimal level of reserves and enhance their management. This gives South Africa access to sufficient foreign exchange to meet its financial commitments. The second objective is to establish mechanisms to effectively manage the impact of external shocks. These mechanisms will strengthen the South African economy's ability to anticipate different types of shocks and respond to such scenarios through clear and executable plans.

SFA 5 — ENSURE COST EFFECTIVE AVAILABILITY AND INTEGRITY OF NOTES AND COIN

Banknotes and coin are used to buy and sell goods and services. These forms of legal tender must be readily available and in adequate supply to meet the public's demand and their integrity must be trusted. Two strategic objectives support SFA 5. The first is to optimise the notes and coin supply chain and the second is to enhance the quality and integrity of notes and coin.

While the achievement of the SARB's mandate through the SFAs is the intended outcome of the strategy, it is also imperative that the SARB builds internal enabling capability to ensure that it remains a relevant and high-performing organisation over the longer term. While not core to the SARB's mandate, these cross-cutting objectives support all five SFAs and enable step change in performance; namely:

CROSS-CUTTING OBJECTIVES

Leverage and maximise the SARB's participation in regional and international forums to advance South Africa's national interest.

Improve targeted internal and external stakeholder communication and engagement as an important tool to deliver the SARB's mandate, create greater transparency around the SARB and improve citizen education. A brand and corporate identity initiative is underway and will be complemented by the SARB's stakeholder strategy and engagement initiatives.

Improve strategy, risk and performance management to enable the SARB to respond to the rapidly changing environment, understand the risks associated with its strategy and continue to build a high-performing organisation. A strategic initiative has recently been launched to better understand the role of central banking post 2020 and the implications for the SARB. Factors such as financial technology (fintech), blockchain, smart payment methods, intelligent cybersecurity and other exponential technologies are covered by the initiative.

Improve enterprise information management to address the SARB's current and future information requirements and enable it to optimally collect, analyse and disseminate information in response to increasing financial system complexity and rapid technological developments.

Establish and embed cybersecurity processes given that cyber threats remain high and no organisation is completely immune to such risks.

The building blocks of the SARB strategy are the foundational capability and capacity elements that provide the backbone to ensure organisational effectiveness.

BUILDING BLOCKS

Provide fit-for-purpose technology solutions that deliver accurate and timeous information to inform decision making and enable the SARB's processes in a globalised and increasingly complex environment. The revised IT strategy is being implemented and the IT portfolio has been segmented into tier 1 and tier 2 projects, with tier 1 projects requiring increased focus given their significant impact on the SFAs.

Attract, develop and retain critical skills and competencies by maturing talent management, workforce planning and performance management, as well as fostering employee engagement and developing a new employee value proposition. This focus supports the SARB's response to the changing world of work, which includes technology advances (artificial intelligence, machine learning and robotics) and a multi-generational, connected, flexible and mobile workforce.

Improve organisational effectiveness by reducing bureaucracy and silos and becoming more flexible and agile to enable rapid response to the changing environment. A number of initiatives aim to improve the SARB's agility, including a review of governance structures and committees across the organisation.

Embed a culture of performance, innovation and collaboration led by a team driven by the SARB's values. The SARB is implementing a programme that aims to embed the desired culture and strengthen its leadership. This is a focal point of the SARB's enterprise-wide initiatives, as successful strategy execution depends on alignment between culture and strategy.

STRATEGY REVIEW

A targeted analysis of disruptive environmental forces and the SARB's internal performance was undertaken during the reporting year, and it was concluded that the SARB's strategy is sufficiently robust to respond to internal and external factors. The five SFAs remain in place for the medium term to 2020. One notable refinement is the inclusion of cybersecurity as a strategic internal cross-cutting objective in the strategic plan. This is in response to the increasing number of cybercrime incidents globally and the growing sophistication of cyberattacks.

The SARB recognises that a longer-term focus is required to ensure that it is future fit, relevant and able to respond to the megatrends that impact its work. For example, fintech is one factor that may shape the strategic focus in the longer term. Work is underway to test the relevance of the strategic plan beyond 2020.

Developments in financial technology

The rapid developments in fintech such as crypto-assets, initial coin offerings and crowdfunding means that the financial sector is potentially facing innovation- and technology-driven disruptions to its products and services. This has implications for the SARB's macro- and microprudential oversight responsibilities.

The SARB established the Fintech Programme in 2017 as part of its 'smart central bank of the future' strategic initiative. A dedicated unit staffed with full-time employees is tasked with strategically tracking and analysing fintech developments. The primary aim of the programme is to ensure efficient, appropriate and enabling fintech policy and/or regulatory frameworks for emerging financial services activities and innovations. The programme will facilitate the development of policy positions for the SARB across the fintech domain, taking into account the related benefits and risks of fintech. It will consider whether current policies and regulatory regimes are still appropriate for these innovations and, where required, assist policymakers in formulating new regulatory responses to these innovations.

The SARB has adopted a risk-based rather than a rules-based evaluation approach. For example, it does not evaluate the product, technologies used or the entity, which is usually a small technology company. Instead, it evaluates the underlying economic function or regulated activity which would typically include deposit taking, payments, lending, insurance and investments.

THE FINTECH PROGRAMME WILL FOCUS ON THE FOLLOWING THREE AREAS

Development of a policy and/or regulatory framework for crypto-assets: the SARB's review will cover issues such as clearing and settlement risks, exchange control impacts, monetary policy and financial stability and cybersecurity, among others.

Assess the appropriateness of innovation facilitators[1] for the SARB: clear and transparent eligibility and participation criteria will be developed to assist the selection of applicants for a regulatory sandbox. The data collected and interactions with innovation facilitators could inform policy positions.

Fintech data collection and analysis: to fast-track learning of exponential technologies such as blockchain.

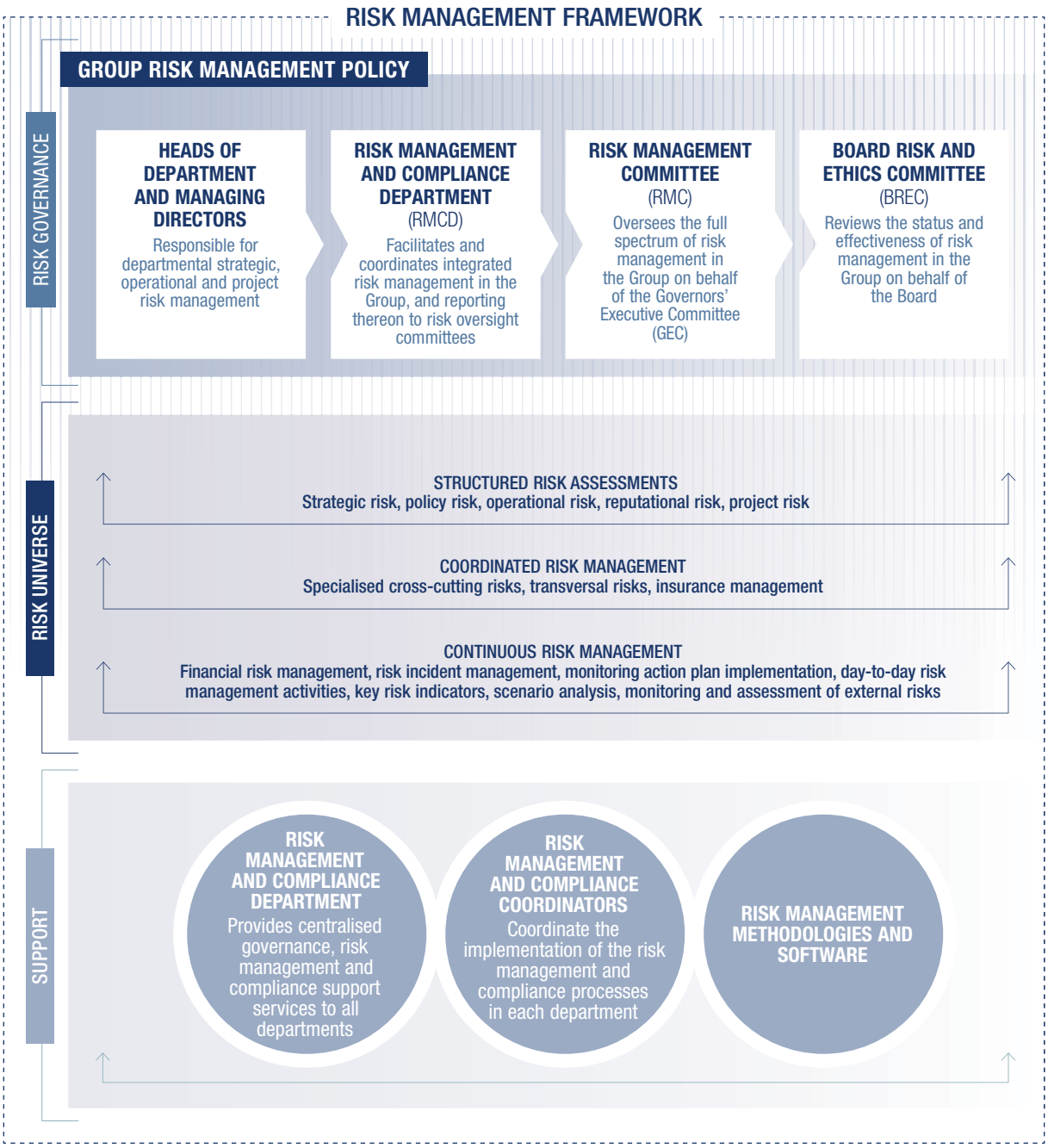
The SARB is committed to staying abreast of and contributing to global thought leadership on fintech. It collaborates with local and international regulatory and standard-setting bodies. Work undertaken by the various working groups at the Financial Stability Board and the Bank for International Settlements has been proactive in trying to understand fintech developments and robustly exploring benefits, risks and appropriate regulatory frameworks.

1. *Innovation facilitators is a collective term for innovation hubs, regulatory sandboxes and accelerators. A regulatory sandbox is a set of rules that allows innovators to test their products or business models in a live environment without following some or all legal requirements and subject to predefined restrictions.*

RISK MANAGEMENT

The SARB is exposed to significant inherent risks in many of its core functions. Given its unique role, the SARB's risk management and control objectives go beyond the risks that impact its operations to include public interest in line with its constitutional and statutory responsibilities.

The SARB's risk management framework ensures that the risks that may threaten the achievement of the SARB's strategic objectives are adequately and effectively managed at acceptable levels. The SARB's risk management approach includes monitoring and appropriately responding to potential and actual risks emanating from global and domestic political and economic environments. The framework governs the full spectrum of strategic, financial (including credit, market and liquidity), reputational and operational risk management and considers and, where appropriate, incorporates the risk management principles set out in the fourth King Report on Corporate Governance in South Africa (King IV).



COMBINED ASSURANCE APPROACH

The Group follows a combined assurance approach to risk management and control. This approach aims to integrate, coordinate and align the assurance processes within the Group and to optimise the level of risk, governance and control oversight.

1st LEVEL OF ASSURANCE PROVIDERS

DEPARTMENTAL MANAGEMENT

Risk management and internal control are an integral part of the Group's management and accountability functions. Management within each department is primarily responsible for the ongoing identification, assessment and management of their department's risks; including designing, implementing and maintaining an adequate and effective system of control.

2nd LEVEL OF ASSURANCE PROVIDERS

INTEGRATED RISK MANAGEMENT

The Group's risk management policy and framework, and the RMCD which performs a centralised, integrated risk management coordination function, together ensure that risks are managed in a way that is consistent with internationally accepted standards and guidelines.

The RMCD reports to the RMC and BREC on risk management activities and the status and effectiveness of risk management in the Group. In addition, it facilitates structured risk assessments conducted at various levels and covering all functions and business units. The coordinating role of the RMCD extends to the management of specialised, cross-cutting risks which include compliance and business continuity management.

The RMCD also coordinates and facilitates continual risk management activities, which include the reporting of risk incidents, monitoring the implementation of action plans to mitigate identified residual risks, and implementing and monitoring key risk indicators.

3rd LEVEL OF ASSURANCE PROVIDERS

INTERNAL AUDIT

The Internal Audit Department (IAD) provides objective, independent assurance on the adequacy and effectiveness of the Group's governance, risk management and control processes.

The Chief Internal Auditor (CIA) reports jointly to the Governor and to the Chairperson of the Audit Committee. All IAD activities are governed by an Internal Audit Charter approved by the Audit Committee. The Board reviews the Charter at least every three years to ensure its relevance.

The IAD's risk-based approach to auditing aligns to the International Professional Practice Framework as prescribed by the Institute of Internal Auditors (IIA). The IAD's audit methodology is based on the guidelines set out in the Committee of Sponsoring Organizations of the Treadway Commission (COSO) framework.

The external quality assurance (EQA) review undertaken during the reporting year, confirmed the IAD's general conformance to IIA standards. EQA reviews are undertaken periodically.

COMBINED ASSURANCE FORUM

The Combined Assurance Forum (CAF) coordinates work undertaken by the respective assurance providers and is accountable to the GEC and the Audit Committee. It comprises representatives from the various assurance service providers and the independent external auditors. In addition to CAF meetings, bilateral meetings are held between the respective assurance service providers to coordinate their respective assurance activities.

Independent external assurance service providers

The Group's annual financial statements are audited by independent external auditors, and where deemed necessary, other external assurance providers are used to obtain independent assurance on the adequacy and effectiveness of internal processes and practices, taking into account international best practice.

SPECIALISED CROSS-CUTTING RISKS

Compliance risk management

Specific efforts, applied Group-wide, to ensure that the Group meets its compliance obligations include:

> developing and maintaining an appropriate compliance policy and framework;

> identifying, assessing and monitoring compliance with applicable regulatory requirements;

> promoting a culture of compliance; and

> reporting on compliance risks to the RMC and BREC.

Business continuity management

The SARB has a business continuity management policy and framework in place. The RMCD provides centralised coordination and the appropriate backup infrastructure and facilities further strengthen the SARB's resilience. The RMCD facilitates business impact assessments and compiles business continuity plans for all departments. It also liaises closely with the Cyber and Information Security Unit, which is responsible for ensuring holistic governance and management of the Group's cyber and information security programme.

Enhancing integrated risk management

During the reporting year, the RMCD focused on enhancing integration across the various components of the risk management value chain.

The chief risk officers of two central banks conducted a peer review of the adequacy and effectiveness of the SARB's integrated risk management framework and processes. The results showed that the SARB's integrated framework and processes encompass the essential components of a strong risk management programme and include the core components of the operational risk management principles and practices used by other central banks and monetary and supervisory authorities.

Going forward, focus will be placed on strengthening the integration between the risk and strategy management processes, and the recommendations arising from the peer review will be implemented. These recommendations include streamlining the reporting process to the RMC and BREC and further automation of some of the supporting processes.

STAKEHOLDER ENGAGEMENT

Of critical importance to the SARB, particularly given the fast changing and challenging environment in which it operates, is to make the SARB's work more accessible to all South Africans. Targeted internal and external stakeholder engagement and communication has therefore been included in the SARB's strategic plan as a cross-cutting strategic objective that supports the realisation of the SARB's intended outcomes.

Historically, the SARB's engagement initiatives focused mostly on its primary mandate – monetary policy. Recent developments, including changes to the regulation of the financial services sector, have broadened the SARB's responsibilities. This has deepened the need for more communication on the SARB's strategy, analysis and policy conduct. The SARB is therefore rebalancing its communication and engagement efforts to facilitate better understanding of its role and responsibilities, particularly among the general public.

As more South Africans start to see the positive link between what the SARB does and their own economic well-being, the more favourably they will view the SARB and place their trust in it, enhancing the SARB's credibility and reputation.

PRIMARY STAKEHOLDERS

Parliament is a primary stakeholder as it is through parliament that the SARB accounts to the citizens of South Africa. The Governor and other SARB officials engage regularly with parliament and other special interest groups on the work that the SARB does. Work is underway to broaden the scope of these engagements to cover the specific goals articulated in the SFAs.

During the reporting year, the SARB conducted two surveys to gain employee insight. The Employee Value Proposition survey and the Employee Engagement survey. The results of both surveys will be used to improve organisational culture and employee experience.

PUBLIC ENGAGEMENTS

Each Monetary Policy Committee (MPC) meeting concludes with a press conference at which the Governor delivers a statement explaining the decision of the MPC. The statement is published on the SARB's website, together with documents detailing the key forecasts and assumptions used in the meeting, for variables such as headline inflation, economic growth and the future (model-determined) policy rate. The press conference also provides an opportunity for MPC members to answer questions from stakeholders on its deliberations and decision.

In addition, a more detailed review of monetary policy is presented to members of the public at various Monetary Policy Forums, held twice a year in major centres throughout the country.

In 2017, the SARB hosted two pilot forums in Soweto to reach new audiences. Lessons learnt are being used to redesign the SARB's approach to engaging with the general public and stakeholders outside the SARB's core group of stakeholders. For example, following the Soweto forums, the SARB hosted a workshop to explain the application process for a banking licence. Pleasingly, the workshop was attended by more than 250 people from various provinces, indicating a demand for engagement with the SARB.

Reputational survey

The Reputational Survey is undertaken every two years and assesses SARB's reputation based on familiarity, favourability, trust and advocacy. The survey provides the SARB's leadership with useful insight into how stakeholders view the organisation and the results are used to inform stakeholder communication and engagement initiatives.

The overall reputational scores among all three stakeholder groups were positive. However, informed stakeholders felt that the SARB's public visibility could be improved and employees indicated a need for better engagement from the SARB's leaders and managers. The awareness of the SARB by the general public remained low, but positive among those who were aware of the organisation.

Reputational scores achieved in the 2016 survey

INFORMED STAKEHOLDERS
80.9%
2014: 78.4%

EMPLOYEES
71%
2014: 75%

GENERAL PUBLIC
69.3%
2014: 69.3%

These communication efforts foster economic education and literacy, helping citizens understand their economic environment so that they are better able to make informed decisions with regards to lending, savings and investment which have a direct impact on their well-being. The engagements also help the private sector to better understand the impact of changes in short-term interest rates on macroeconomic variables. Finally, clear and transparent communication helps to build public support for the measures required to support prudent monetary policy.

OUTREACH PROGRAMMES

The SARB's outreach programmes include the national MPC Schools Challenge in partnership with the Department of Basic Education (discussed on page 61 of the corporate social investment report) and high school learner visits to the SARB or SARB representatives visiting schools and universities. During these visits, the SARB engages on monetary policy and the work that it does. It targets teachers, students and learners involved with commerce subjects.

The SARB views these engagements as an effective and sustainable way in which to achieve better understanding around its work, and to broaden its reach indirectly to a wider audience through knowledge sharing. Going forward, it will focus on reaching more schools, particularly those in small towns and rural areas.

SOCIAL MEDIA

The SARB operates Twitter, Facebook, LinkedIn and Instagram accounts, which provide a wide range of stakeholders with a mechanism to quickly reach the SARB when they need information. These platforms are gaining in importance and used to address a range of issues, particularly those relating to coin and banknotes.

REGIONAL AND INTERNATIONAL FORUMS

South Africa is committed to the development of an effective and efficient global financial regulatory architecture. The SARB is a member of and actively participates in relevant and strategic international forums, including the Group of Twenty (G-20) and the FSB. This enables it to influence the global financial reform agenda.

The SARB has signed Memoranda of Understanding with the European Central Bank and Deutsche Bundesbank, and agreed to a formal programme of collaboration with the Bank of England, on technical matters relating to central banking issues.

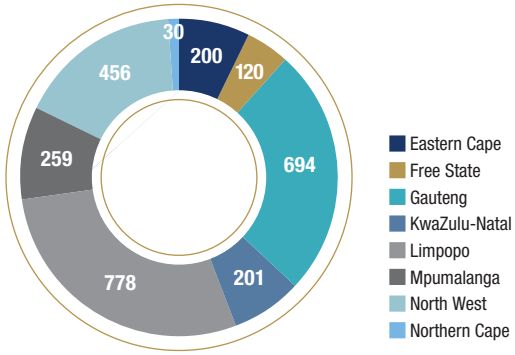
Monetary Policy Forums

2 626 people

attended Monetary Policy Forums or events in 2017. Since 2000, forums have been hosted in 10 cities and towns across South Africa, attracting a wide range of stakeholders, including business people and students.

Learner interactions

High school learner visits to the SARB's head office



Social media

SA Reserve Bank
February 26

Many South Africans wonder if the 10c and 20c pieces are still legal tender. They are and should be accepted as payment for any goods and services. However, there are limits to how many coins may be used per transaction.

SARB FOLLOWERS

March 2018

31 872
April 2017: 1 600

25 500
April 2017: 6 300

12 700
April 2017: 4 400

International engagements during the year

Association of African Central Banks (AACB): the SARB hosted the annual Assembly of Governors' meeting and the Governors' Symposium. Delegates from 42 member banks in Africa, as well as delegates from Asia, Europe and the United States of America (USA) attended. The SARB's Governor chairs the AACB, which drives the African Monetary Cooperation Programme of the African Union.

Africa Local Currency Bond Markets Conference: the SARB jointly hosted this conference to develop local currency bond markets with the Deutsche Bundesbank as part of the Compact with Africa Initiative, a G-20 Agenda initiative. The conference was attended by delegates from 20 African countries and eight G-20 countries.

BRICS[1]: the SARB is driving a number of initiatives to further the work of and lend greater credibility to the BRICS Contingent Reserve Arrangement. Work to finalise the legal structure of the BRICS Bond Fund (an initiative announced in 2017 under China's BRICS Presidency) is also progressing under the leadership of the SARB as the coordinating central bank.

International Monetary and Financial Committee (IMFC): in January 2018, Governor Lesetja Kganyago was appointed Chairperson of the IMFC and Deputy Governor, Daniel Mminele, as Chairperson for the IMFC's deputies. Both posts will be held for a three-year period. The IMFC deliberates policy issues facing the International Monetary Fund (IMF) and the IMF's agenda. This includes the global economic outlook and the IMF's operations, governance and resources, among others.

1. *An association of five major emerging national economies: Brazil, Russia, India, China and South Africa.*

MONETARY POLICY

OVERVIEW

Price stability reduces uncertainty in the economy, contributing to stronger economic growth and employment creation over time. Furthermore, a low and stable inflation rate protects the purchasing power of the rand. Hence the need for low inflation, particularly for the poor who have limited means of protecting themselves against continually rising prices.

ACHIEVING AND MAINTAINING PRICE STABILITY

WHAT IS MONETARY POLICY?

Monetary policy is the process through which the SARB influences interest rates in the economy to ensure price stability.

The interest rate is the main tool used to manage inflation. The SARB sets the repurchase (repo) rate, which is the rate at which banks borrow from the SARB. This in turn impacts the interest rates that banks charge their customers, as well as other interest rates in the economy.

Over the long run, central banks have a high degree of control over inflation in their economies. In the short run, shocks like droughts can cause inflation to rise, however, these effects tend to be temporary. For prices to keep increasing year after year, central banks have to create extra money. In turn, by controlling the supply of money, central banks have the capacity to manage inflation over time. Given this power, many central banks, including the SARB, have a primary mandate of controlling inflation. Low and predictable inflation provides several benefits. It protects the spending power of consumers, especially in poorer households which are often most vulnerable to inflation. It also permits lower interest rates, particularly for longer-term borrowing, as lenders can charge less to protect their investments from inflation.

Although these are the most important benefits a central bank can provide for a country, over the shorter run monetary policy can also influence the level of output and employment, albeit in a limited way. For instance, when an economy is operating below its potential, lower interest rates can help it recover. Accordingly, inflation-targeting central banks typically also consider how their decisions will affect variables like growth and unemployment. However, the central bank cannot permanently control real output in the same way it can control inflation. This is why inflation targeting is the SARB's core mission.

WHY AN INFLATION-TARGETING APPROACH?

This approach results in the target being clearly articulated, reducing uncertainty and supporting transparency and accountability. Successful implementation of inflation-targeting also helps to anchor inflation expectations.

HOW IS INFLATION MEASURED?

Inflation is measured by defining a basket of goods and services used by a 'typical' consumer and then keeping track of the changes in the cost of that basket. Statistics South Africa is the official compiler of the consumer price index (CPI) which is the measure of inflation.

WHAT DOES THE SARB CONSIDER WHEN MAKING INTEREST RATE DECISIONS?

The MPC decides the short-term interest rate appropriate for achieving the SARB's price stability mandate, defined as an inflation rate of 3–6%. Meetings take place once every two months, and provide an opportunity for the committee members to review economic data and discuss the appropriate monetary policy response.

The committee's decisions take into account the variable medium-term horizon for inflation and the time lags between policy adjustments and economic effects, which are between 12 to 24 months. The flexible inflation-targeting framework allows for temporary deviations from the target in response to shocks to inflation beyond the control of monetary policy.

PUBLIC ENGAGEMENT ON THE MPC DECISION
PG 23

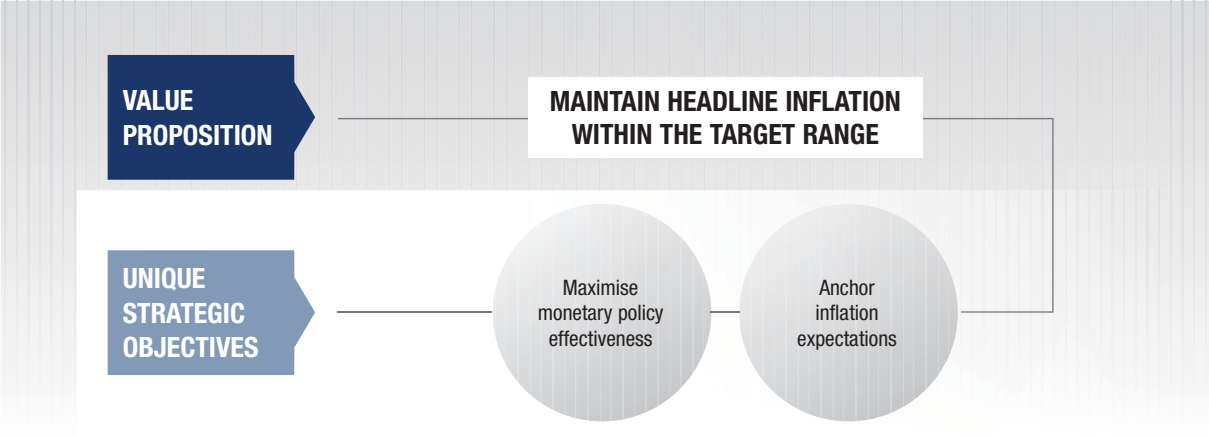
WHAT ARE THE RISKS TO MAINTAINING INFLATION WITHIN THE TARGET RANGE?

A weakening rand exchange rate could potentially accelerate inflation. For example, increasing uncertainty about future economic policy or further ratings downgrades could prompt capital outflows, pushing up borrowing costs and putting pressure on the rand.

External shocks such as increases in international oil prices or drought will make certain goods more expensive.

Remuneration increases in excess of inflation and productivity increases tend to push up prices.

SARB STRATEGIC PLAN: SFA 1



PERFORMANCE SCORECARD

		Target (annual)	2017/18 (annual)	2016/17 (annual)
STRATEGIC MEASURE	Headline inflation versus target	3–6%	Target met 4.7%	6.3%

The SARB achieved success for SFA 1. Since April 2017, inflation has been within the target range and is projected to remain within the range over the three-year forecast horizon. Inflation expectations, as measured through the Bureau for Economic Research (BER) survey, have also remained consistent with the target range. For most of the reporting year, expectations fluctuated around the upper end of the range, however in the first quarter of 2018 expectations for 2019 moderated, declining to 5.3%. The SARB would prefer to see inflation expectations anchored around the mid-point of the target range.

PROGRESS MADE

To maximise monetary policy effectiveness, the SARB:

Established the foundations of the cross-cutting policy-relevant research agenda. A key focus is to determine and establish how the research agenda will be delivered and a key outcome for the next financial year will be to embed and strengthen this capability. The research agenda will assist the SARB to better understand the synergies between the SFAs, particularly SFAs 1, 2 and 4.

Is reviewing the Economic Research and Statistics Department's modelling and forecasting process with completion expected around May 2018. The department achieved its research objectives in various thematic areas of the agenda.

To anchor inflation expectations, the SARB:

Continued to publish policy relevant economic analysis and provide the public with more information about the underlying assumptions that drive the SARB's two-year forecast of the economy. The government and other stakeholders were also provided with improved economic statistics relevant to the formulation and implementation of macroeconomic policy. To meet its objectives to anchor expectations closer to the mid-point of the target range, the SARB will continue to enhance its stakeholder engagement programme by more effectively targeting sectors and groups that influence price setting.

REPORT ON MONETARY POLICY PG 29

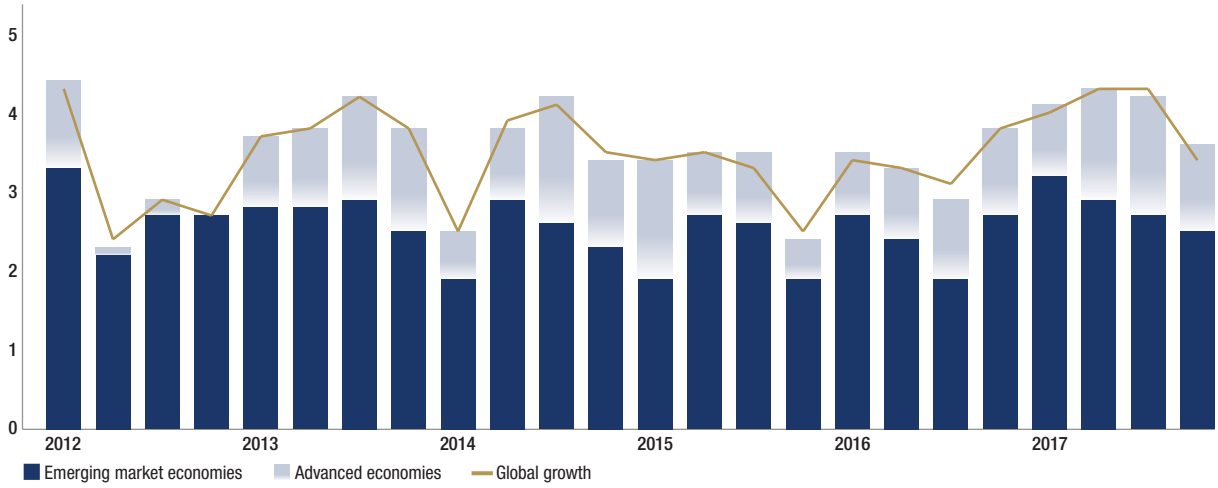
STAKEHOLDER ENGAGEMENT PG 22

REPORT ON MONETARY POLICY

OVERVIEW OF THE WORLD ECONOMY

The global economy has enjoyed a robust and synchronised recovery, making the current upswing the strongest and most sustained growth phase since the rebound from the global financial crisis in 2010. The improvement has been broad based with notable upswings in advanced economies, while key emerging markets such as Brazil and Russia exited protracted recessions. The current upswing, however, remains largely cyclical, with few signs in recent years of an increase in global potential output growth.

REAL GLOBAL OUTPUT GROWTH AND CONTRIBUTIONS FROM ADVANCED AND EMERGING MARKET ECONOMIES (%)



Source: IMF World Economic Outlook.

Advanced economies have maintained strong growth momentum. In the USA, recovery has been solid and is likely to remain supported by fiscal stimulus in 2018 and 2019. Unemployment has fallen to an 18-year low of 3.9%, while inflation has eluded the central bank's 2.0% inflation target, resulting in a modest monetary policy tightening cycle. However, some signs of wage acceleration at the start of 2018 raised fears that the Federal Reserve may have to increase interest rates faster than expected.

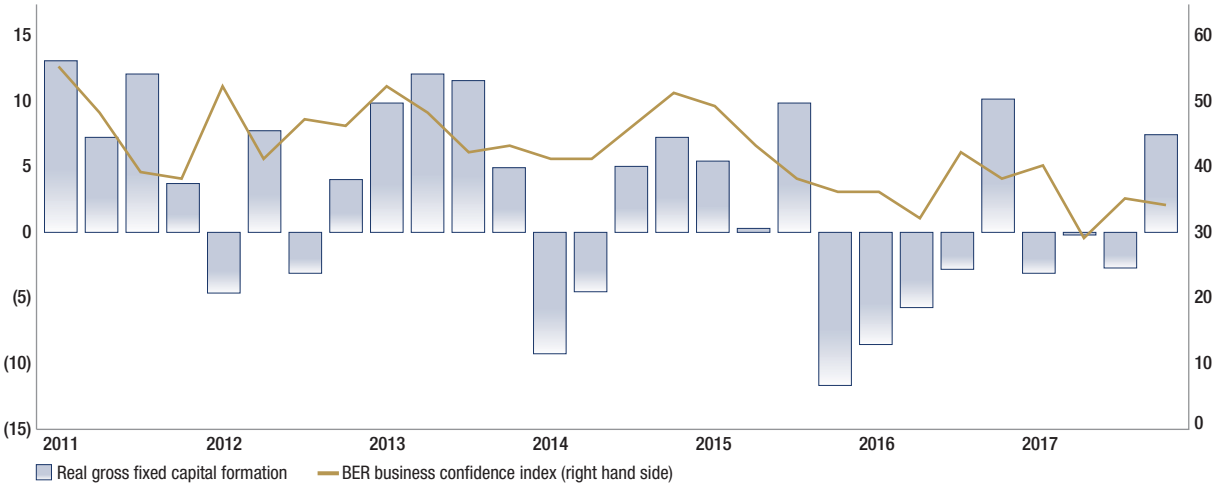
Economic activity in the euro area has also been on a solid footing driven mainly by domestic demand, including a pickup in investment. Many European economies have performed relatively strongly. By contrast, economic activity in the United Kingdom (UK) lost some momentum, as higher inflation eroded consumer demand and uncertainty over the economic implications of Brexit may have weighed on corporate investment.

Emerging markets have benefitted from higher commodity prices, stronger import demand in advanced economies and accommodative monetary policy. China has maintained relatively high levels of growth above 6%, driven mainly by robust net exports against a backdrop of improving global trade conditions. Meanwhile, China's services sector has grown steadily, offsetting a moderation in the secondary sector and signalling an ongoing re-balancing of the economy.

DOMESTIC REAL ECONOMY DEVELOPMENTS

South Africa's real gross domestic product (GDP) expanded by a moderate 1.3% in 2017, from a post-crisis low of 0.6% in 2016. The pickup in growth mainly reflected a rebound in the agriculture and mining sectors from particularly weak levels in 2016. Nonetheless, 1.3% growth remains weak both by historical and 'peer country' standards. The average emerging market growth rate in 2017, for instance, was 4.7%. Real per capita income has also been on the decline and unemployment has remained persistently high, reaching a peak of 27.7% in the third quarter of 2017, and settling at 26.7% in the first quarter of 2018.

REAL GROSS FIXED CAPITAL FORMATION (%) AND BUSINESS CONFIDENCE



Source: Statistics South Africa, SARB and BER.

Against the backdrop of persistently low domestic growth, government finances posted large and sustained fiscal deficits in recent years. As a consequence, government debt levels increased to 50.7% of GDP in 2017. South Africa is now rated sub-investment grade by Fitch and Standard & Poor's (S&P). While Fitch has a BB+ rating for both local and foreign currency debt, S&P has a split rating: the long-term foreign currency rating at BB and the local currency rating at BB+. Accordingly, the 2018 Budget Review proposed a number of measures to rebuild confidence and to return public finances to a sustainable path. These measures included a 1-percentage point hike in the value-added tax (VAT) rate to 15%, as well as a marginal reduction in the expenditure ceiling.

South Africa's external financing needs, on the other hand, have improved somewhat. The country's current account deficit has been declining substantially, reaching 2.5% of GDP in 2017, owing to improving terms of trade, as well as the more robust economic conditions of its trading partners. However, given South Africa's low savings rate, the country is likely to continue to run sizable twin deficits on the current account and the budget over the medium term.

The SARB's forecasts indicate some improvement over the medium term with growth anticipated to reach 2.0% in 2020. The recovery is mainly on account of stronger business confidence, which should allow for a recovery in investment. The continued upswing in the global economy should also provide additional spill-overs to South Africa in the form of firmer exports. The pickup in domestic growth also entails continued growth in household consumption in light of households' reduced debt burdens and continued gains in real disposable income, despite the rise in indirect taxes. Nonetheless, the improvement in growth is muted and expansion is projected to remain below long-term averages over the medium term.

INFLATION DYNAMICS

Domestic consumer price inflation decelerated rapidly throughout 2017 to below the mid-point of the 3–6% target range in January 2018. The moderation in consumer price inflation resulted largely from a reduction in supply side cost pressures amid relatively subdued domestic demand. Food and electricity prices slowed notably, while the appreciation in the rand exchange rate since 2016 lowered the price of imported goods significantly. Food inflation fell from 12.1% in December 2016 to 4.6% in January 2018 as drought conditions gave way to record harvests (except for the Western Cape). Underlying inflation has also declined, averaging 4.7% in 2017, versus a long-run average of 5.0% between 2003 and 2016. Core inflation receded to its lowest level in six years at the start of 2018 from a peak of 5.9% in December 2016.

The price of Brent crude oil increased by more than 70% between mid-2017 and May 2018, reaching levels over US$70 per barrel. In November 2017, the Organization of the Petroleum Exporting Countries (OPEC) and other non-OPEC producers agreed to extend production cuts of 1.8 million barrels per day until the end of 2018. Attempts to reduce supply have also benefitted from collapsing production in Venezuela – one of the world's largest oil exporters. While higher oil prices have led to increased USA shale production, the combination of solid growth in world oil consumption, OPEC compliance with its production targets and geo-political tensions have pushed crude prices over US$75 per barrel. Over the medium term, world oil prices are not forecast to increase significantly from current levels given the potential supply response from new producers, which have managed to reduce marginal costs significantly.

World food developments have been favourable over the past two years, with prices declining steadily in dollar terms from the high levels reached in early 2016. Bumper domestic crops, following a prolonged drought in the northern parts of South Africa in 2016, and positive exchange rate factors have further contributed to a steady decline in local food prices. South African food inflation averaged 6.9% in 2017, with a peak of 8.7% in the first quarter of 2017. Meat prices, however, have remained elevated, averaging 12.8% in 2017, thus limiting the deceleration in overall food price in 2017. Higher poultry prices contributed significantly to the acceleration in overall meat price inflation in 2017. Several factors, including import tariffs on certain poultry products, as well as the outbreak of avian flu in Europe and later in South Africa, severely affected domestic poultry and egg prices throughout most of 2017. Overall food price inflation is expected to accelerate somewhat in 2018, mainly on account of higher VAT rates.

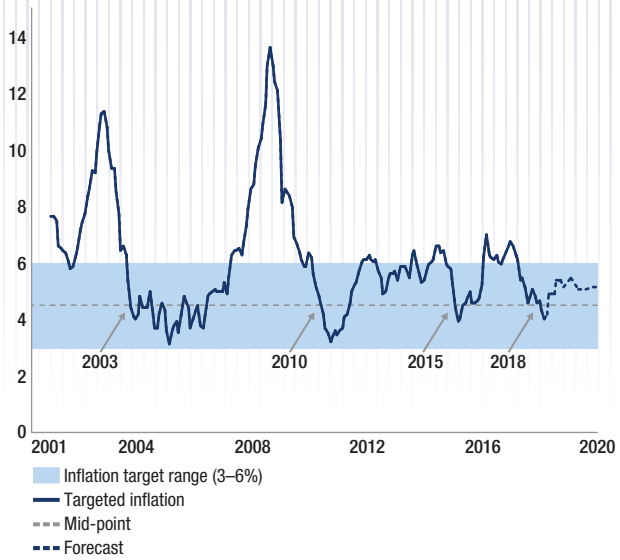
Food and petrol prices are volatile and mostly unresponsive to monetary policy. Policymakers therefore pay close attention to underlying inflation. The composition of SARB's preferred measure of core inflation is largely two thirds services and one third goods; and excludes food, non-alcoholic beverages, petrol and electricity prices.

The goods subcomponent averaged 3.3% in 2017 and is expected to increase slightly to 3.5% by 2019. Services inflation has been more rigid, reflecting the stronger influence of relatively sticky wage growth. Nonetheless, it moderated to 5.5% in 2017 from a post-global financial crisis average of 5.8%, as a slowdown in actual and owners' equivalent rents extended to some other sectors. The varying projections of these two subcomponents are mainly explained by the fluctuations in the exchange rate and inflation expectations.

The exchange rate is one of the key drivers of inflation in South Africa and its impact is transmitted through import prices. Changes in the exchange rate tend to pass through to consumer prices with a lag. The rand exchange rate has been on an appreciating trend since early 2016. By early March 2018, the rand was back at 2015 levels against the US dollar and in trade-weighted terms. The appreciation in the rand has had a clear impact on core inflation, with the core goods subcomponent – including items such as vehicles, household appliances and clothing – slowing more abruptly than the services subcomponent.

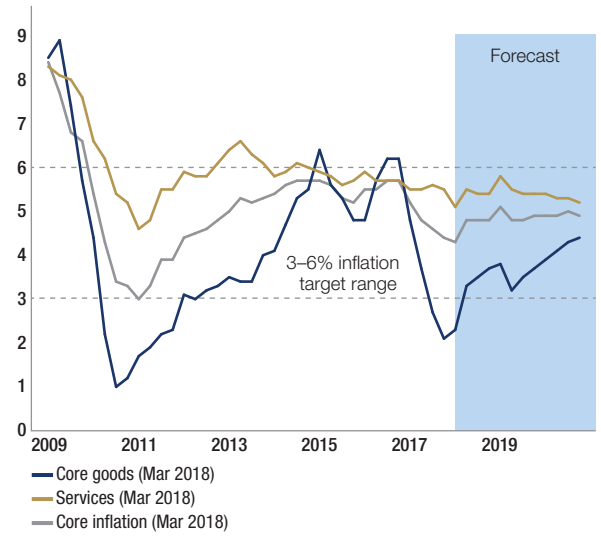
Longer-term inflation expectations, which have been fairly sticky at the upper end of the target range over the post-crisis period, have started to come down. In fact, short-term expectations have moved quite rapidly, while longer-term expectations have adjusted more slowly. This is an important monetary policy

SOUTH AFRICAN INFLATION (% change)



Source: SARB.

CORE INFLATION AND ITS COMPONENTS (% change over four quarters)

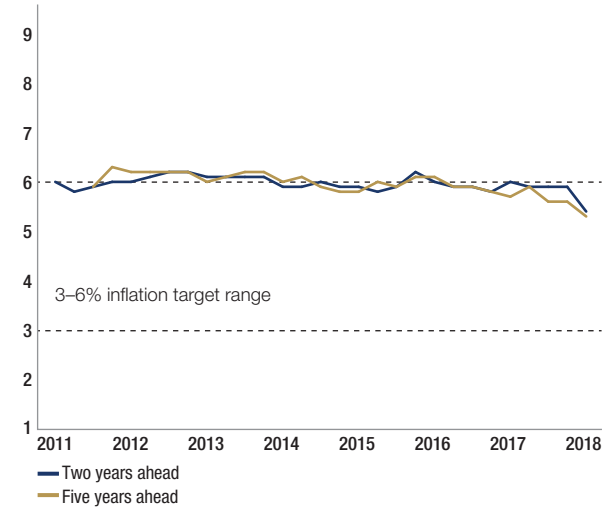


Source: Statistics South Africa and SARB.

REAL EFFECTIVE EXCHANGE RATE OF THE RAND (index)

Source: SARB.

LONGER-TERM INFLATION EXPECTATIONS (%)



Source: BER and SARB.

achievement as inflation expectations influence price- and wage-setting behaviour in the economy. With inflation expectations for the next two years having declined to 5.4% in the first quarter of 2018 – the lowest level since this question was added to the BER survey in 2011 – the prospects for inflation are encouraging.

MONETARY POLICY DECISIONS

Monetary policy decisions affect the economy with a lag of approximately one to two years. Headline inflation numbers, however, are sometimes distorted by temporary shocks such as large movements in oil prices. For this reason, policymakers aim to look through these shocks, and focus on underlying inflation trends. Moreover, policymakers also consult alternative measures of inflation designed to exclude volatile items.

Inflation has gradually declined to within the 3–6% target range, averaging 5.3% in 2017. The shocks that pushed headline inflation in early-2018 to below 4.5% (unusually low electricity and food price gains, and import price deflation from a stronger rand) are now fading, and higher taxes, particularly VAT, will raise inflation again in the near term. The SARB's inflation forecasts have also consistently projected a return to above the target mid-point. In recent years, the SARB has been emphatic that the 3–6% target should not be interpreted as a 6% target, and that policymakers would prefer to have inflation expectations anchored around the 4.5% mid-point.

Over the past few years, the mix of high political uncertainty, persistent fiscal deficits and credit rating downgrades have continued to present upside risks to the inflation outlook. In such a context, the MPC has been forced to maintain a cautious approach, even when confronted with weak domestic demand growth and a negative output gap, which typically curbs demand-driven price pressures. Consequently, the policy response has taken the form of moderate relaxation, with the repo rate declining 50 basis points from its starting point of 7% in January 2017. However, the SARB's own estimates of the neutral real interest rate suggests that policy remains marginally accommodative and hence, the room for additional rate cuts remains limited in the absence of a more durable improvement in the inflation outlook.

The growth forecast has improved steadily, but remains below long-run averages and potential growth. This is mainly due to a lack of structural reforms, which are largely outside the scope of monetary policy. Despite the higher levels of consumption expenditure by households in the latter part of 2017, overall demand remains weak; however, monetary policy is providing some support to the economic recovery as the level of real interest rates has remained slightly below long-run norms in recent quarters.

FINANCIAL STABILITY

OVERVIEW

The financial system in South Africa is important to every citizen as it either directly or indirectly touches the well-being of everyone living in the country. When financial stability risks are managed well, systemic financial crises are less likely to occur, and are more easily managed if they do occur, mitigating the spill-over effects on the broader economy and society. In addition, the SARB's prudential supervision of regulated financial institutions contributes towards an efficient financial system that provides financial services to all South Africans. Financial stability is not an end in itself but, like price stability, it is generally regarded as an important precondition for sustainable economic growth, development and employment creation.

PROTECTING AND ENHANCING FINANCIAL STABILITY

FINANCIAL SECTOR REGULATION ACT 9 OF 2017 (FSRA)

The FSRA was enacted on 22 August 2017, marking a significant milestone in the implementation of the Twin Peaks framework of financial regulation. The FSRA confers on the SARB an explicit, statutory mandate to protect and enhance financial stability in South Africa. This mandate will include efforts to prevent a systemic event and, should a crisis occur, assistance with restoring financial stability in the country. The FSRA also sets out the mechanisms to achieve the intended outcomes of the Twin Peaks framework. One of these mechanisms is the Prudential Authority, which is responsible for assisting the SARB with its financial stability mandate. The Prudential Authority became effective on 1 April 2018.

"It is important to acknowledge that the financial sector and the risks associated with it are constantly evolving. It therefore follows that regulatory frameworks need to evolve with the sector. Increased regulation should not be construed as a burden of over-regulation, but should rather be viewed as evidence of the evolution of the financial sector as well as the associated risks and the regulatory response to them."

Deputy Governor of the SARB
Francois Groepe

HOW DOES THE SARB MANAGE FINANCIAL STABILITY?

A framework to monitor financial stability

> Monitoring and mitigating against risks to financial stability.
> Stress testing the South African banking sector.
> Partnering with external research experts and promoting excellence in financial stability research.
> Evaluating the impact of regulatory reforms on the financial system and providing input into global regulatory, supervisory and financial sector standards.

A macroprudential policy framework

A calibrated toolkit of macroprudential instruments for the Financial Stability Committee (FSC) to apply in mitigating potential systemic risks.

A legal framework for resolving SIFIs[1]

> The draft Resolution Bill.
> A deposit insurance scheme to enhance depositor protection.

1. *A systemically important financial institution (SIFI) is an entity whose failure may trigger a systemic event. A systemic event is an event or circumstance that may reasonably be expected to have a substantial adverse effect on the financial system or on economic activity in South Africa, including an event or circumstance that leads to a loss of confidence in the ability of operators in the payment and settlement systems, financial institutions and financial markets to continue to provide financial services and products.*

RISKS TO FINANCIAL STABILITY DURING THE REPORTING YEAR PG 39

THE ROLE OF THE FINANCIAL STABILITY COMMITTEE

The SARB fulfils its responsibility to protect and enhance financial stability through the FSC. The committee comprises the Governor as Chairperson, the Deputy Governors, all members of the MPC and a maximum of seven other SARB officials.

The FSC met three times during the reporting year to monitor vulnerabilities in the global and domestic environments, assess their possible implications for domestic financial stability and decide whether any mitigating measures needed to be taken. The issues discussed by the FSC and any decisions taken are communicated in the biannual Financial Stability Review publications.

The FSRA makes provision for a Financial Stability Oversight Committee (FSOC) to support the SARB in protecting and enhancing financial stability. The FSOC will meet at least every six months and its membership comprises representatives from the SARB, National Treasury and all financial regulators. The Governor chairs the committee.

FSOC's primary objectives are to:

> coordinate appropriate plans, mechanisms and structures in the financial sector to mitigate financial stability risks and vulnerabilities and support the SARB when it performs its functions in relation to financial stability; and

> facilitate cooperation and collaboration, and coordination of action, between financial sector regulators and the SARB.

The FSOC, in its capacity as an advisory committee, works closely with the FSC, as the SARB's policymaking committee on financial stability.

SARB STRATEGIC PLAN: SFA 2

VALUE PROPOSITION

PROTECT AND ENHANCE FINANCIAL STABILITY TO ACHIEVE A SAFER FINANCIAL SYSTEM (MACRO)

UNIQUE STRATEGIC OBJECTIVES

- Enhance the framework for managing systemic events
- Develop and enhance the frameworks for systemic risk identification, monitoring and mitigation
- Improve and enhance the regulatory, supervisory and oversight framework of the NPS

PERFORMANCE SCORECARD

STRATEGIC MEASURES	Target (annual)	2017/18 (annual)
Policy action based on a set of macroprudential indicators (mitigation of vulnerabilities)	Complete research on key elements of the macroprudential toolkit	**Progress made but target not met** Policy papers on three instruments completed and presented to the FSC
Frameworks for identifying, monitoring and mitigating systemic risk	Introduce enhanced systemic risk measures (SRMs)	**Target met** Enhanced SRMs incorporated into the monitoring framework
Crisis management and resolution plans and a legal framework	Complete a simulation exercise and evaluate the results	**Target met** Simulation exercise completed and evaluated by the Financial Sector Contingency Forum[1] (FSCF)

No systemic risk events occurred in the financial system during the reporting year, and there was no need to resolve any SIFIs. The SARB is on track to meet its objectives (frameworks, toolkits, policy development and simulation exercises) set out in the scorecard.

PROGRESS MADE

To enhance the framework for managing systemic events, the SARB:

Conducted and completed the public consultation process on the resolution framework, paving the way for the approval of the draft Resolution Bill. The Bill includes proposals to establish a pre-funded deposit insurance scheme. Once approved, the process to submit the Bill to Parliament for promulgation into law will begin. This work is expected to continue into the next financial year.

To develop and enhance the frameworks for systemic risk identification, monitoring and mitigation, the SARB:

Completed the research paper on SRMs and presented it to the FSC for consideration and approval. Additional SRM research papers are in progress.

To improve and enhance the regulatory, supervisory and oversight framework of the NPS:

While the NPS oversight framework has been approved, further enhancements to the legislation have been delayed due to the extended deadline for inputs requested from external experts.

REPORT ON FINANCIAL STABILITY
PG 38

1. *The primary objective of the FSCF is to identify potential risks in the financial sector that may become systemic events and to coordinate appropriate plans, mechanisms and structures to mitigate these risks.*

REPORT ON FINANCIAL STABILITY

Financial stability refers to a condition where the financial system is resilient to systemic shocks, facilitates efficient financial intermediation and mitigates the macroeconomic costs of disruptions in such a way that confidence in the system is maintained.

The FSRA specifically refers to SARB's responsibility to monitor global and domestic environments, using quantitative and qualitative indicators to identify possible vulnerabilities. In ordinary circumstances, the SARB may advise financial regulators on what steps to take and information to provide to mitigate these vulnerabilities. Furthermore, the Governor may, after consultation with the Minister of Finance, declare that a systemic event has occurred or is imminent. The SARB is responsible for implementing the action required to prevent, mitigate and manage such an event, and is provided with certain additional directive powers. It may direct financial regulators to provide information and take action to increase the resilience of financial institutions, prevent the risk from spreading, and to restructure, resolve or wind-up a SIFI.

RISKS TO FINANCIAL STABILITY

The SARB regularly assesses the risks to financial stability and has developed a framework to identify vulnerabilities in South Africa's financial system and how they change over time. During the reporting year, the following key risks were identified and tracked:

> the deteriorating domestic fiscal position as a result of lower-than-expected revenue collection and the rising contingent liabilities of state-owned enterprises (SOEs);

> the continuing synchronised downward phases of the South African financial and business cycles, implying recessions could potentially be longer and deeper, and impact the banking sector in terms of higher impairments and lower asset quality;

> rising prospects of trade protectionist measures by the USA and potential retaliatory measures by other jurisdictions could have negative implications for global asset prices and potentially result in a trade war, impacting global trade;

> an abrupt repricing of risk premiums against a backdrop of global policy uncertainty opens channels of negative spill-overs and financial contagion, particularly for fragile and/or risky emerging markets; and

> China's rising corporate, non-corporate, government and shadow-banking debt may be larger than estimated.

The amplification mechanisms and contagion effects are key for the systemic risks identified, as well as for 'other' identified risks that have not featured that prominently. Some of these 'other' risks include global geo-political events that flare up from time to time (North Korea, Gulf States, Brexit) and political uncertainty in South Africa at the time. In addition, the banking sector in South Africa could be exposed to risk depending on how the proposed policy of land expropriation without compensation is implemented.

Another event risk that arose during the reporting period, was the announcement of an investigation of accounting irregularities and the subsequent resignation of the Chief Executive Officer (CEO) of Steinhoff International Holding NV. The conglomerate's share price declined more than 90%, resulting in a short-term liquidity crisis for the company. The Steinhoff group has taken various actions to stabilise the impact of the event on its finances and operations in the medium term. Potential financial stability implications arising from this event have been assessed by the SARB and to date, have proved not to be systemic. The impact of a potential default on the conglomerate's debt exposure, and impact of this default on the South African banking sector, are being monitored.

Furthermore, an increase in the volatility of some equities listed on the JSE Limited has been observed since December 2017. This could have been triggered by a 'short-selling' strategy which is not commonly used in South African financial markets. This type of short-selling strategy has the potential to create financial instability if the target company is a deposit-taking institution and the short-selling campaign results in a negative feedback loop between declining investor confidence (as reflected in a declining equity price) and a loss of depositor confidence in the institution (as reflected in a decline in deposits or a 'run' on the bank). Although banks are potentially systemically important in nature, a significant decline in their equity price is not necessarily regarded as a systemic risk.

DOMESTIC FINANCIAL STABILITY DEVELOPMENTS

Both S&P's and Fitch downgraded South Africa's sovereign credit rating to sub-investment grade in late 2017, while Moody's Investors Service kept South Africa's rating unchanged at investment grade. Political developments since the governing party's electoral conference in December 2017 have improved confidence levels and helped to

stabilise the domestic economic outlook, resulting in the risk of a ratings downgrade abating somewhat. In March 2018, Moody's Investors Service changed the outlook for South Africa from negative to stable, with positive macroeconomic indicators, institutional changes at some SOEs and a well-received budget, contributing to the decision.

The SARB's forecast for domestic economic growth for 2018 and 2019 has been revised upwards. This improved outlook is in line with the relatively high level of the SARB's composite leading business cycle indicator of economic activity in December 2017.

Government finances

South Africa's current fiscal position remains a key domestic challenge that could impact the stability of the financial system, and therefore continues to be a focus point for financial stability analysis. The sustainability of government finances is crucial for any economy as it directly impacts on the government's debtholders, which in South Africa's case, are mainly pension and provident funds and banks. Fiscal sustainability is also a key consideration for rating agencies when they assess sovereign credit ratings. Issues of particular relevance include higher debt levels, the budget deficit, and the size of liabilities underwritten by government. Although the containment of government debt remains an important focus area for the South African Government, debt continued to trend upwards during 2017, albeit at a less concerning rate. A fine balance between maintaining spending commitments and ensuring the long-term health of government finances is required.

Governance issues at SOEs, rising contingent liabilities of government and associated liquidity shortfalls could put additional pressure on government finances. Should SOEs fail to roll over debt, the government would be liable and most likely would have to take on further debt.

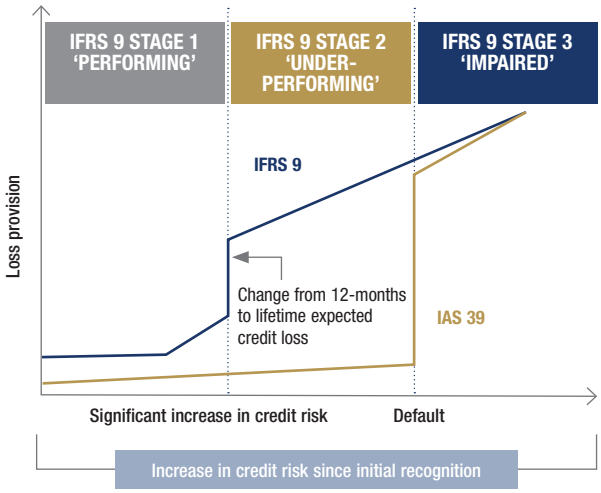
Banking sector

South African banks remained healthy and well capitalised during the reporting period, with the sector's capital adequacy ratio at 16.23%. However, credit defaults continued to increase in the first half of 2017, while the ratio of total impaired advances as a percentage of total gross loans and advances (a key indicator of credit risk), remained below 3% for most of 2017 before increasing to 3.24% in March 2018. Impaired advances increased by 16% for the quarter to March 2018, and total credit impairments increased by 25% over the same period.

IFRS 9 specifies how an entity should classify and measure financial assets, financial liabilities and some contracts to buy or sell non-financial items. Banks and other reporting entities must account for impairments on loans (financial assets or instruments) by applying the *expected credit loss model* as opposed to the *incurred loss model* used previously. IFRS 9 is forward-looking in its approach to expected credit losses and incorporates a broader range of factors such as past events, current conditions and supportable forecasts, including current macroeconomic conditions, to determine credit losses[1]. This results in a sharp increase in loss provisions and a step change in the manner and timing of calculating impairments.

The SARB conducted a quantitative impact survey on the South African banking sector during November 2017. The preliminary results indicate that although the changes in the treatment of credit impairments will impact the regulatory capital of the sector over the course of 2018, it is unlikely to result in financial instability. Further analysis will be conducted. The standard is effective for annual reporting periods beginning on or after 1 January 2018.

PROVISIONING UNDER IFRS 9



Source: Fykstrom, N and Li, J., IFRS – the new accounting standard for credit loss recognition.

1. *Novotny-Farkas, Z., The Significance of IFRS 9 for Financial Stability and Supervisory Rules, p12.*

Profitability in the banking sector, while remaining strong, has been decreasing since the first half of 2017. Measured by return on equity, the sector's profitability has declined from 17.4% in February 2017 to 16.0% in January 2018. The sector's cost-to-income ratio (also known as the efficiency ratio) has increased marginally from 55.2% in February 2017 to 56.7% in January 2018, mainly as a result of the average growth in operating expenses exceeding the average growth in operating income. Profitability has also been impacted by subdued economic activity. Lower profitability impacts a bank's ability to accumulate retained earnings, which forms part of its regulatory capital. An ongoing, sustained decline in banking sector regulatory capital could make the banking sector less resilient to shocks and result in financial instability.

The countercyclical capital buffer

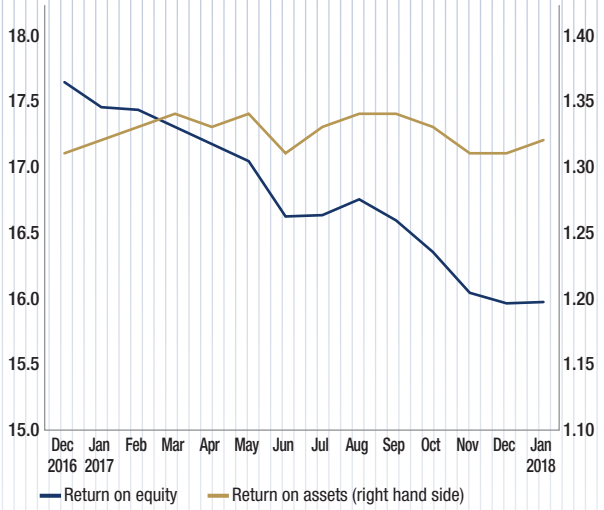
The countercyclical capital buffer (CCB) forms an integral part of the internationally agreed-upon standards for risk-based capital requirements, and is being phased in between January 2016 and January 2019. The CCB provides macroprudential supervisors with a tool to increase or decrease capital requirements for banks to protect the financial system from the boom and bust phases of the financial cycle. The Basel Committee on Banking Supervision (BCBS) has suggested in its guidance to national authorities that the credit-to-GDP gap be used as a guide for deploying Basel III CCBs, although most jurisdictions, including South Africa, supplement this with additional indicators.

The FSC is responsible for setting the CCB rate. During the reporting period, the committee decided not to activate the CCB add-on for banks, supported by developments in the credit-to-GDP gap and other indicators.

Stress testing

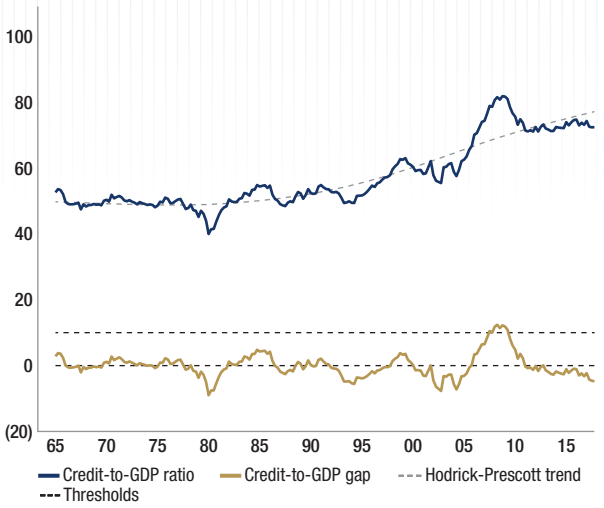
The SARB conducted a combined bottom-up and top-down common scenario stress-testing exercise during 2015/16. The exercise assessed the vulnerability of the South African banking system to adverse economic developments. To ensure the robustness of the procedures and future stress-testing exercises, the Deutsche Bundesbank and the IMF undertook peer reviews of the exercise. The outcomes have been used to refine the SARB's stress-testing models and framework, including the addition of liquidity risk. In line with the SARB's stress-testing governance framework, full stress-testing exercises are generally conducted once every two years. The SARB is preparing for the 2018 Common Scenario Stress Testing Exercise and will publish the results of the exercise in the second edition of the Financial Stability Review in 2018.

PROFITABILITY IN THE BANKING SECTOR (%)



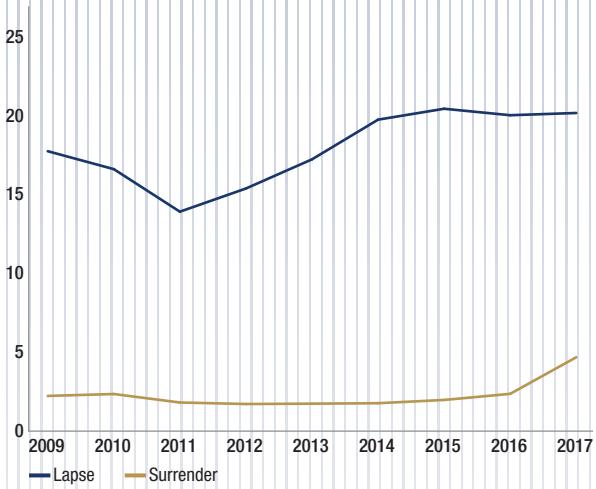
Source: SARB.

CREDIT-TO-GDP RATIO, GAP AND HODRICK-PRESCOTT TREND (%)



Source: SARB.

LAPSES AND SURRENDERS RATIOS (%)



Lapse ratio: number of policies lapsed as a percentage of the total number of policies in force.

Surrender ratio: number of policies surrendered as a percentage of the total number of policies in force.

Source: Financial Services Board.

Insurance sector

The Financial Services Board launched the SAM project in 2009 to establish a risk-based solvency regime for the prudential regulation of long- and short-term insurers. The risk-based framework, which emerged from the Twin Peaks model of financial regulation, is close to completion and is focusing on ensuring that both the industry and the Prudential Authority are ready for implementation in July 2018.

The South African insurance industry has been impacted by subdued economic activity. New business volumes and profit margins are under pressure and a strong increase in the number of surrenders and lapses indicates that many policyholders are not in a position to maintain their policies. This could negatively impact the profitability of long-term insurers as the costs associated with entering into a policy are incurred upfront and recovered over the lifetime of the policy. The growth in the gross written premiums of the short-term insurance industry has also slowed due to the subdued economic conditions.

DEVELOPMENTS IN FINANCIAL SERVICES TECHNOLOGY

The rapid adoption of technology-enabled innovation in financial services and the adoption of new business models has attracted the attention of financial authorities in a number of jurisdictions. The FSB's June 2017 report on the potential financial stability implications of fintech provides a framework to assess the fintech landscape. It defines the scope of fintech activities and explores the potential benefits and risks to financial stability. In addition, the report discusses the regulatory and supervisory issues related to fintech and identifies a number of issues that merit attention. The report prioritises managing operational risks from third-party service providers, mitigating cyber-risks and monitoring macrofinancial risks.

In 2017, the SARB established a Fintech Programme to develop its capacity to better understand the risks and benefits of fintech.

FINTECH PROGRAMME
PG 18

The potential impact of fintech on financial stability is considered to be low at this stage. However, as new alternative platforms expand and experience a full business cycle, regulators will need to remain vigilant to familiar micro- and macro-level financial services risks. These include financial risks (such as maturity mismatches) and operational risks. The interconnectedness of systems may result in other risks such as procyclicality and contagion risk.

PRUDENTIAL AUTHORITY

The Prudential Authority was established on 1 April 2018, in terms of the FSRA which introduces the Twin Peaks approach to financial regulation. Twin Peaks has two main aims: firstly, to strengthen the safety, soundness and integrity of financial institutions and secondly, to better protect financial customers and ensure that they are treated fairly by financial institutions (market conduct). Other objectives of the model include prevention of financial crime, financial inclusion, transformation of the financial sector and enhancing confidence in the financial system by ensuring its stability, efficiency and integrity.

SARB STRATEGIC PLAN: SFA 3

VALUE PROPOSITION

PROMOTE AND ENHANCE THE SAFETY, SOUNDNESS AND INTEGRITY OF REGULATED FINANCIAL INSTITUTIONS

UNIQUE STRATEGIC OBJECTIVES

Develop, improve and integrate the supervision of regulated financial institutions

PERFORMANCE SCORECARD

STRATEGIC MEASURES	Target (annual)	2017/18 (annual)	2016/17 (annual)
Percentage of financial institutions that meet or exceed the quantitative prudential standards for SIFIs	100% or specific regulatory action	Target met 100%	100%
Percentage of financial institutions that meet or exceed quantitative prudential standards for non-SIFIs	100% or under specific regulatory action	Progress made but target not met 90%[1]	100%
Financial institutions with sound governance compliance and risk management practices	All institutions fully compliant or under specific regulatory action	Progress made but target not met 90%[1]	100%

1. *All non-compliant institutions are under specific regulatory action.*

Assessments on compliance with the Principles for Financial Market Infrastructures were not conducted due to the delay in promulgating the FSRA, and the Financial Services Board remained responsible for this role during the reporting year. Going forward, the SARB will conduct these assessments.

PROGRESS MADE

To develop, improve and integrate the supervision of regulated financial institutions, the SARB:

Developed and distributed for consultation the supervisory approach for banking, insurance, cooperative financial institutions and conglomerates. The approach for FMIs is in the early stages of development.

Completed 50% of the overall integrated supervisory approach and framework.

Prudential standards are still to be developed. The Prudential Authority is preparing for the Financial Action Task Force (FATF) mutual evaluation in 2019, which will assess the compliance of South Africa's framework and laws for anti-money laundering and the combating of terrorist financing against international standards. The Solvency Asset Management (SAM) reforms are part of the overhaul of financial sector regulation in South Africa. The Insurance Bill, which is still being considered by Parliament, builds on the regulatory framework created through the FSRA and is expected to be implemented in July 2018.

REPORT OF THE PRUDENTIAL AUTHORITY
PG 45

REPORT OF THE PRUDENTIAL AUTHORITY

THE NEED FOR REGULATORY REFORM

During the most recent global financial crisis in 2008, the South African financial system proved its resilience with no major financial institutions having failed. However, the crisis highlighted the extent to which financial groups are embedded within economic and financial systems, as well as the high degree of interconnectedness. Regulators subsequently agreed that more could be done to improve the strength and adaptability of the system through the implementation of a more proactive model of financial sector regulation.

Historically, the regulatory architecture for the South African financial sector was fragmented. Different sectoral laws applied to different regulatory authorities overseeing individual institutions. For example, there were, and still are, separate pieces of legislation with differing standards and requirements for banks, insurance companies, pension funds, collective investment schemes and credit providers, among others.

The Twin Peaks reform represents a shift away from this siloed approach to reduce the possibility of regulatory arbitrage or 'forum shopping' in the financial system. The Prudential Authority's overarching objective is to harmonise and integrate the approach to prudential supervision across sectors, to the greatest extent possible.

REGULATORS

The Twin Peaks model of financial regulation places equal focus on prudential and market conduct regulation and supervision by creating dedicated authorities responsible for prudential and market conduct objectives.

The Prudential Authority, a juristic person within the SARB's administration, is the prudential regulator and supervisor of financial institutions[1] and FMIs[2] in South Africa. The Prudential Authority was established from the Financial Services Board Insurance Prudential team, the Bank Supervision Department of the SARB and the Supervisory Team of the Cooperative Banks Development Agency.

The FSRA also makes provision for a standalone Financial Sector Conduct Authority (FSCA), responsible for enhancing and supporting the integrity and efficiency of South Africa's financial markets and protecting financial customers.

Together with the FSCA, the Prudential Authority is responsible for licensing banks, mutual banks, cooperative banks, cooperative financial institutions, insurers and FMIs.

IMPLEMENTATION OF THE TWIN PEAKS MODEL

The transition to the Twin Peaks model of regulation will occur in a phased manner. The FSRA gives the new regulatory authorities additional powers, over and above those provided in existing industry-specific laws, to ensure that they have the required tools to perform effectively in the first phase of implementation, without being limited by gaps in existing legislation.

The respective legal frameworks for prudential and market conduct regulation will be developed, harmonised and strengthened in the second phase of implementation. Where required, industry-specific legislation will be repealed and new legislation or regulatory instruments introduced. Legislative developments relating to levies and the conduct of financial institutions and financial markets will be introduced in due course, solidly launching the Twin Peaks model of regulation into the second phase of implementation.

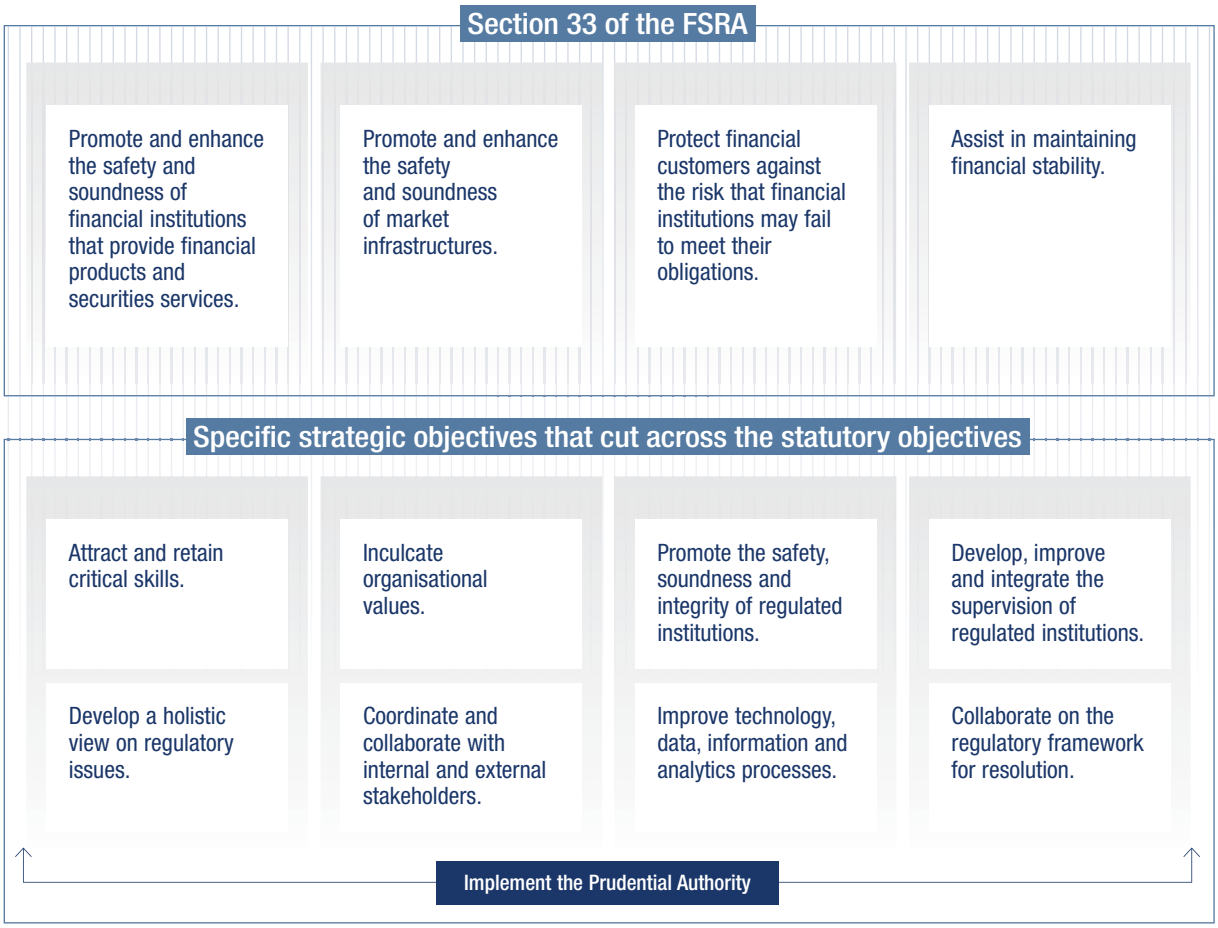
GOVERNANCE STRUCTURES

The governance structure, resources, financial management and reporting obligations of the Prudential Authority are prescribed by the FSRA. Furthermore, the Prudential Authority is required to submit a report on its activities to Parliament and to prepare financial accounts for each financial year which will be included in the SARB's annual report.

The Prudential Committee is responsible for the overall governance of the Prudential Authority. It is chaired by the Governor of the SARB and comprises the CEO of the Prudential Authority (who is also a Deputy Governor of the SARB) and the remaining Deputy Governors of the SARB.

1. *A financial institution refers to licensed, regulated and/or supervised banks and insurers, as well as institutions required to be licensed in terms of applicable financial sector legislation.*
2. *Section 1(1) of the Financial Markets Act 19 of 2012 (FMA) defines a market infrastructure as a central counterparty, a central securities depository, a clearing house, an exchange and a trade repository.*

OBJECTIVES OF THE PRUDENTIAL AUTHORITY



The Prudential Authority assesses its progress in executing its strategic objectives on a six monthly basis as part of the SARB's strategic plan. This ensures alignment between the Prudential Authority and other departments of the SARB.

FUNCTIONS OF THE PRUDENTIAL AUTHORITY

Prudential regulation and supervision

A healthy, sound, and properly functioning financial institution is able to meet its obligations to financial customers such as depositors and policyholders. Prudential regulation aims to ensure that financial institutions comply with minimum prudential requirements related to capital, liquidity, credit and other requirements, and that they are managed by suitably qualified and skilled individuals.

A number of new areas of regulatory and supervisory responsibilities have been placed on the Prudential Authority. Two of the most significant reforms to prudential oversight relate to financial conglomerates and FMIs.

The South African financial system is dominated by a few large financial institutions. As a result of this concentration and the high level of interconnectedness, the risk of contagion is high. The FSRA allows the Prudential Authority to designate members of a group of companies as a financial conglomerate. The more detailed regulatory and supervisory requirements, for example the designation criteria for financial conglomerates, will be released by the Prudential Authority in the coming months.

The Prudential Authority, together with the FSCA (the responsible authority for the FMA), will develop a supervisory framework for FMIs during 2018/19.

The FSRA requires the Prudential Authority to follow an integrated risk-based, forward-looking and outcomes-focused supervisory approach in its microprudential supervision. In addition, financial institutions need to be aware of the risks to their businesses and have adequate corporate governance frameworks and risk management processes in place to appropriately mitigate these risks. Therefore, the Prudential Authority may issue prudential standards in addition to sector legislation, as well as joint standards with the FSCA.

It is important to note that in its development of a comprehensive and consistent prudential regulatory and supervisory approach, the Prudential Authority is committed to the implementation of internationally agreed regulatory and supervisory standards in a manner that appropriately takes into account the context, realities and the capacity of South Africa's financial institutions. It participates in the processes of international standard setting bodies and after assessing the appropriateness of various international standards for South Africa, the Prudential Authority will adopt and adapt these standards into the South African regulatory frameworks.

Financial inclusion

By achieving its objectives, the Prudential Authority will support financial inclusion and sustainable competition in the provision of financial products and services. It will monitor fintech, particularly developments that have the potential to facilitate financial inclusion through affordable and appropriate financial services and the entrance of smaller players into the market. This work will be undertaken together with the SARB and the FSCA to develop appropriate actions that support innovation and fintech.

FINTECH PROGRAMME
PG 18

Cooperation and collaboration with other regulators

The Prudential Authority values transparency, collaboration and coordination in promoting the safety and soundness of financial institutions. It is required to enter into Memoranda of Understanding with, among others, the FSCA, the SARB in its macroprudential role, the National Credit Regulator and the Financial Intelligence Centre on a number of areas of common interest to ensure effective alignment and efficiencies in the supervisory approach.

Looking ahead

The Prudential Authority's Regulatory and Supervisory Strategy document will be published on its website by 1 October 2018, in line with the requirements of the FSRA. The document will provide general guidance and information to the public regarding the Prudential Authority's approach to regulation and supervision, the principles that will guide its decisions, the key priorities over the next three years and the key outcomes it intends to achieve. The Prudential Authority appreciates that the implementation of the Twin Peaks reform will involve significant changes to existing processes, practices, structures and operations. It is therefore committed to communicating timeously and in an open and transparent manner to assist the transition of the financial sector regulatory landscape.

In the coming months, the Prudential Authority intends to publish:

> the approach to licensing;

> the supervisory framework for financial conglomerate supervision;

> the supervisory framework for FMI supervision;

> the integrated supervision framework;

> the enforcement approach;

> Memoranda of Understanding with other regulators; and

> guidance on the regulation of significant owners.

RESILIENCE TO EXTERNAL SHOCKS

Resilience to external shocks is the ability to maintain price and financial stability when adverse external events occur. As a small open economy, South Africa is susceptible to global economic and financial market influences, which may have adverse effects on the economy. It is imperative that the SARB, together with other government agencies, have policies that maintain confidence in the economy and preserve macroeconomic stability during such episodes.

WHAT IS AN EXTERNAL SHOCK?

An external shock is an event that takes place outside South Africa and which has a negative impact on the South African economy and/or financial markets. A shock could, among others, disrupt international trade or the cross-border flow of capital, and may have a negative impact on the economic well-being of South Africans.

WHY DOES THE SARB HOLD FOREIGN-EXCHANGE RESERVES?

Gold and foreign-exchange reserves are typically held to enable the SARB to provide foreign exchange liquidity in times of financial market stress. This ensures that South Africa is able to meet all its foreign obligations, such as debt servicing or international trade, should the natural supply of foreign exchange diminish. Maintaining an adequate level of reserves boosts investor confidence, thereby helping to reduce the likelihood of capital outflows.

SARB STRATEGIC PLAN: SFA 4

VALUE PROPOSITION

ENHANCE THE SOUTH AFRICAN ECONOMY'S RESILIENCE TO EXTERNAL SHOCKS

UNIQUE STRATEGIC OBJECTIVES

- Maintain an optimal level of reserves and enhance their management
- Establish mechanisms to effectively manage the impact of external shocks

PERFORMANCE SCORECARD

		Target (annual)	2017/18 (annual)
STRATEGIC MEASURE	Official gross foreign-exchange reserves accumulation versus target	Accumulate adequate reserves	✓ Adequate levels of foreign-exchange reserves accumulated during the reporting period

PROGRESS MADE

To maintain an optimal level of reserves and enhance their management, the SARB:

- Implemented the Strategic Asset Allocation.
- Approved the concept framework for the Broker Counterparty Selection Approval and Monitoring framework and the Bank Credit Assessment Model framework.
- Completed a review of the External Fund Management Programme.

To establish mechanisms to effectively manage the impact of external shocks, the SARB:

- Developed a framework to identify and manage systemic events in terms of the FSRA. Simulation and stress testing of the framework will continue into the new financial year.

AVAILABILITY AND INTEGRITY OF NOTES AND COIN

Banknotes and coin are legal tender used to buy and sell goods, such as food, and services, such as transportation. These forms of legal tender must be readily available and in adequate supply to meet the public's demand and they must be trusted by the citizens of South Africa.

WHAT IS THE SARB'S RESPONSIBILITY IN TERMS OF NOTES AND COINS?

The SARB has the sole right to make, issue and destroy banknotes and coin in South Africa, and it is responsible for the wholesale distribution of banknotes and coin to commercial banks. The SARB also replaces soiled banknotes and settles claims for mutilated banknotes. The SARB, together with the South African Police Service and the commercial banks, work to combat the counterfeiting of banknotes and coin.

SARB STRATEGIC PLAN: SFA 5

VALUE PROPOSITION

ENSURE COST EFFECTIVE AVAILABILITY AND INTEGRITY OF NOTES AND COIN

UNIQUE STRATEGIC OBJECTIVES

- Optimise the notes and coin supply chain
- Enhance the quality and integrity of notes and coin

PERFORMANCE SCORECARD

STRATEGIC MEASURES	Target (annual)	2017/18 (annual)	2016/17 (annual)
On-time in-full fulfilment of orders from the cash industry	100% of orders fulfilled within agreed timelines	Target met 100%	100%
Incidence of counterfeiting measured in parts per million (ppm)	Less than 15 ppm	Target met 10.52 ppm	10 ppm

Note: while both targets have been met in terms of their parameters, both have been revised to partially achieved for the reasons outlined in the South African Bank Note Company (RF) Proprietary Limited on page 65.

PROGRESS MADE

To optimise the notes and coin supply chain, the SARB:

Fulfilled all orders from the cash industry on time.

Streamlined its physical footprint to improve efficiency and reduce risk, and ensure the long-term sustainability of the currency management function. As part of its cash management strategy, the SARB closed its branches in Bloemfontein, East London and Port Elizabeth, and converted its remaining branches to cash-handling centres.

To enhance the quality and integrity of notes and coin (measured by the percentage yield of fit notes in circulation, where the percentage yield should be above the target), the SARB:

Achieved a 92% yield against a target of 90%. However, the note quality assessment process has highlighted some concerns around the sample coverage.

SUBSIDIARY REPORTS
PG 62

INFORMATION TECHNOLOGY REPORT

To effectively execute its expanded mandate, the SARB depends on accurate and timeous information to inform its decision making. It therefore regards information technology (IT) as a strategic asset that enables its strategic plan.

One of the SARB's cross-cutting objectives is to improve the management of enterprise information as well as the analytics process. It aims to achieve this by providing fit-for-purpose technology solutions that enable the effectiveness of organisational capacity and capability. Setting this foundation will support the SARB's internal processes to achieve their respective responsibilities in terms of delivering the SARB's strategic objectives.

IT STRATEGY

IT is deeply entrenched in the way the SARB conducts its business. The IT strategy enables the SARB's strategy and sets the strategic direction of the SARB's IT function. It also recognises IT's role in conducting the SARB's business in a globalised and increasingly complex environment.

A strategic IT scorecard has been developed with agreed measurable key performance indicators. Progress against the scorecard is reported quarterly to the Information Technology Steering Committee (ITSC).

The key measures of the IT scorecard are:

- how IT enhances SARB's efficiency and effectiveness;
- internal processes that assist the IT function to deliver business value; and
- capabilities such as skills, technology requirements and culture that enable internal IT processes.

The SARB is pleased with the progress made against the IT scorecard's objectives for 2017/18 and remedial actions have been put in place to address gaps where performance has not met targets.

IT GOVERNANCE

The SARB's IT strategy covers alignment with good practice IT trends and standards, and process maturity against King IV's IT governance requirements is regularly assessed. The self-assessment during the reporting year confirmed the SARB's compliance with the IT requirements of King IV's Principle 12. While the opportunities presented by IT are clear, the rapid pace of technological change introduces risk. The appropriate governance, risk and control systems are in place to manage and mitigate information and IT system risks, which remain crucial focus areas for the IT function.

The IT governance framework and IT Charter were updated during the reporting year to align to the new IT strategy and are being reviewed for approval. The framework and charter assist the Board to discharge its IT responsibilities and ensure effective two-way communication between management and the Board on IT matters.

INFORMATION TECHNOLOGY STEERING COMMITTEE
PG 77

2017/18 PERFORMANCE

AVAILABILITY

Achieved an average availability of critical systems of 99.75%, above the target of 99% (2016/17: 99.93%).

MAJOR IT INITIATIVES COMPLETED AND WHICH SUPPORT THE SFAs

The SARB's information and communications technology (ICT) equipment was successfully migrated to its head office data centre with no impact to operations. The migration has attracted the interest of local and international sectors wanting to gain knowledge on the process.

Launched the SARB Mobile application (app), giving users access to current and historical Quarterly Bulletins. It also provides them with quick and easy access to related data and information. The app is available in major app stores.

In response to the findings of the IT strategy review and to ensure the IT function is aligned to the SARB's business imperatives, the capacity of the Business Relationship Management division within the IT function was enhanced and the SARB is maturing the demand management process.

IT OPERATIONS

Availability

In addition to the SARB's strategic IT objectives, focus is placed on ensuring that ICT environments and solutions are adequately maintained with high availability and reliability. During the reporting year, the average availability of critical systems was 99.75% and three business continuity IT recovery tests were conducted, with all three being successful.

Enterprise Information Management (EIM) Programme

The EIM strategy addresses the SARB's current and future information requirements and focuses on various data and IT initiatives that enable the SARB to optimally collect, analyse and disseminate information.

CYBERSECURITY

Cyber threats remain high and no organisation is completely immune to such risks. Cyber-risks are mitigated through continuous improvements to systems and processes to protect the SARB from cyberattacks. The SARB has chosen to implement Security Incident and Event Management technology to support effective monitoring of system security, and during the year it implemented the base infrastructure of this technology solution. During the year, cyber and information security risk, Swift compliance and attack path assessments for key systems were undertaken and the necessary action plans are in progress.

Looking ahead

The focus of this reporting period was project planning, including the sourcing of appropriate partners. Looking forward, the SARB's focus will be to implement and execute large-scale IT projects, particularly those that significantly impact the SFAs.

HUMAN RESOURCES REPORT

The successful execution of the SARB's strategy and mandate depends on the collective effort of its employees. Embedding a culture of performance, innovation and collaboration led by the SARB's values and delivering an attractive employee experience, will assist the SARB to attract, develop and retain the critical skills and competencies needed to drive strategic progress.

2017/18 PERFORMANCE

The SARB focused on the following four areas of its 2020 people strategy

Maturing talent management and workforce planning

> Talent reviews have helped to raise awareness around the talent management process, reinforced collective accountability and encouraged talent mobility.

> Approved a leadership development strategy and the architecture design for leader and manager development programmes.

Maturing performance management and aligning it to reward and recognition

> Completed the alignment of the performance contracts of departmental heads to the SARB's strategy and cascaded performance objectives to all managers.

> Implemented a new Remuneration Policy that aligns to the total reward strategy which promotes a flexible, balanced, integrated and cost-effective reward structure.

> Rolled out total reward statements which for the first time encompassed direct (fixed and variable pay and recognition) and indirect (benefits and development) reward elements.

Fostering employee engagement

> Conducted an Employee Value Proposition survey and Employee Engagement survey.

Developing an employee value proposition for the strategic future workforce

> Spent R35 million on training and development, reaching 80% of the workforce.

> The engagement surveys identified the attributes of an attractive employee value proposition for the SARB and the findings will be used to improve organisational culture and the employee experience.

STAFF TURNOVER

The closure of the SARB's branches in Bloemfontein, East London and Port Elizabeth, as part of its cash management strategy, contributed to the reduction in headcount and increased overall staff turnover. Employees impacted by this organisational restructure were able to apply for enhanced early retirement and voluntary severance packages.

Pleasingly, regrettable turnover improved.

NUMBER OF EMPLOYEES

1 967

2016/17: 2 186

OVERALL STAFF TURNOVER RATIO

20.9%

2016/17: 6.2%

REGRETTABLE TURNOVER RATIO

1.17%

2016/17: 1.46%

CRITICAL ROLES

The SARB experienced challenges in sourcing suitable candidates for critical roles that support the SFAs, resulting in an increased average time to fill a post. However, the successful sourcing and placing of the right candidates in critical roles has improved the SARB's coverage ratio of critical roles to 80%.

AVERAGE TIME TO FILL CRITICAL ROLES

114 days

2016/17: 96 days

DEPTH OF SUCCESSION OF CRITICAL ROLES

One

2016/17: One

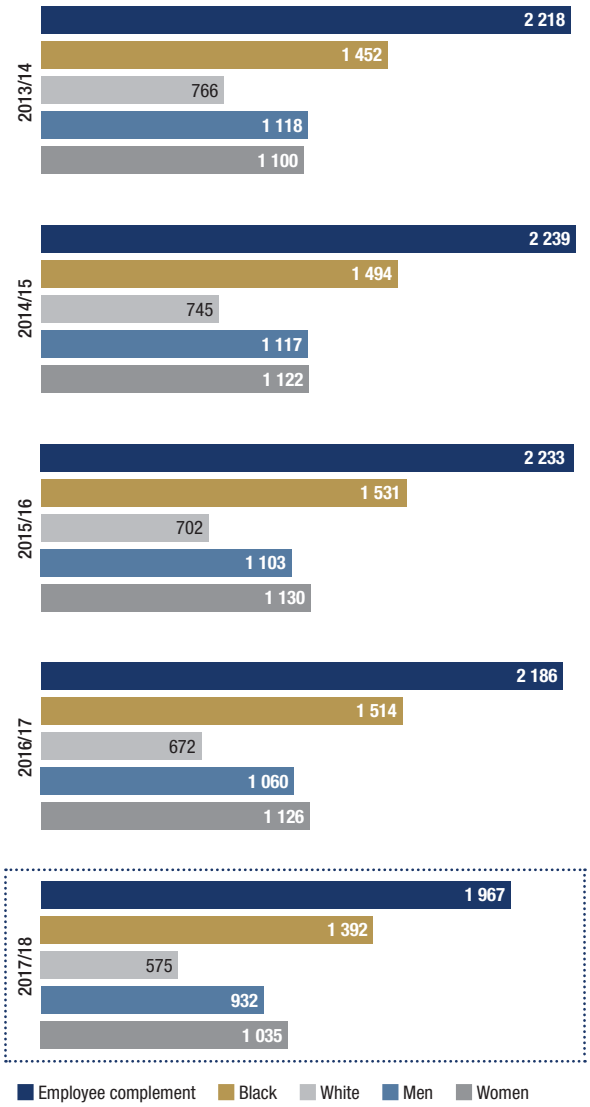
COVERAGE RATIO OF CRITICAL ROLES

80%

2016/17: 68%

WORKFORCE PROFILE

HEADCOUNT OVER FIVE YEARS (NUMBER OF EMPLOYEES)



Note: black includes African, Coloured and Indian.

AVERAGE AGE

42 years

(2016/17: 42 years)

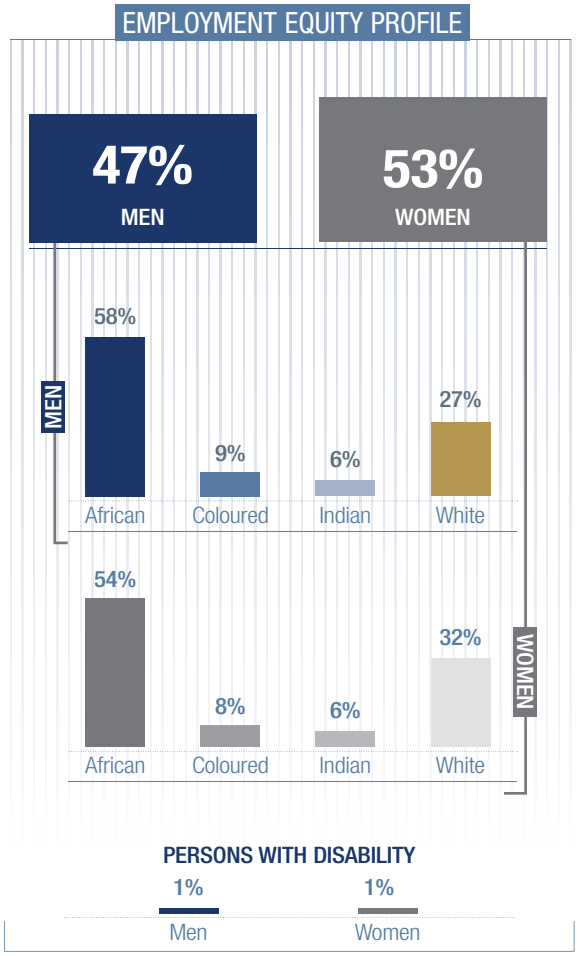
AVERAGE YEARS OF SERVICE

12 years

Years	Employees
0 – 1	229
2 – 4	287
5 – 10	557
11 – 20	451
21 – 30	329
Over 30	114
Total	1 967

EMPLOYMENT EQUITY

Transformation and employment equity are key focus areas and the SARB continues to build a sustainable workforce that reflects the demographics of the economically active population in South Africa. It complies with the Employment Equity Act of 1998, as amended. The SARB's 2017/18 employment equity report was accepted by the Department of Labour.



REMUNERATION

The SARB's total reward philosophy is to reward employees for their performance and contributions to its strategic objectives. The philosophy covers fixed pay, variable pay and recognition benefits, work-life balance, and career development and opportunities.

LEARNING AND DEVELOPMENT

The SARB believes that its employees should find working for the SARB a stimulating and personally enriching experience. It accepts co-responsibility for the development of each employee's full potential.

Training expenditure including study aid

R34.9 million

reaching **80%** of employees

2016/17: R47.3 million reaching 72% of employees

Training spend as a percentage of total payroll

2%

2016/17: 3%

Of the **1 608** employees trained

2016/17: 1 594

75% are Africans

2016/17: 80%

51% are women

2016/17: 52%

1% are people with a disability

2016/17: 1%

GRADUATE DEVELOPMENT PROGRAMME

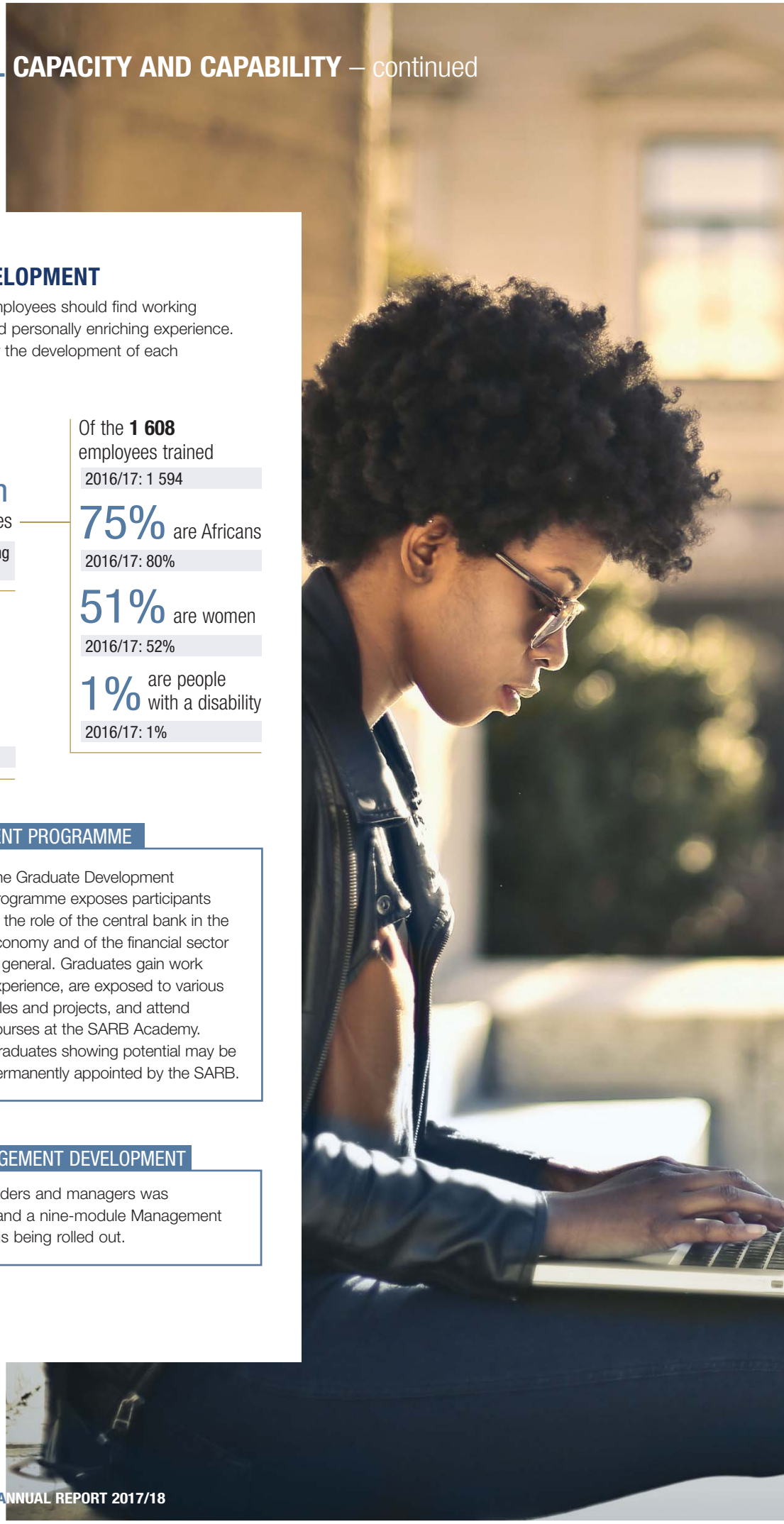
22 recruits

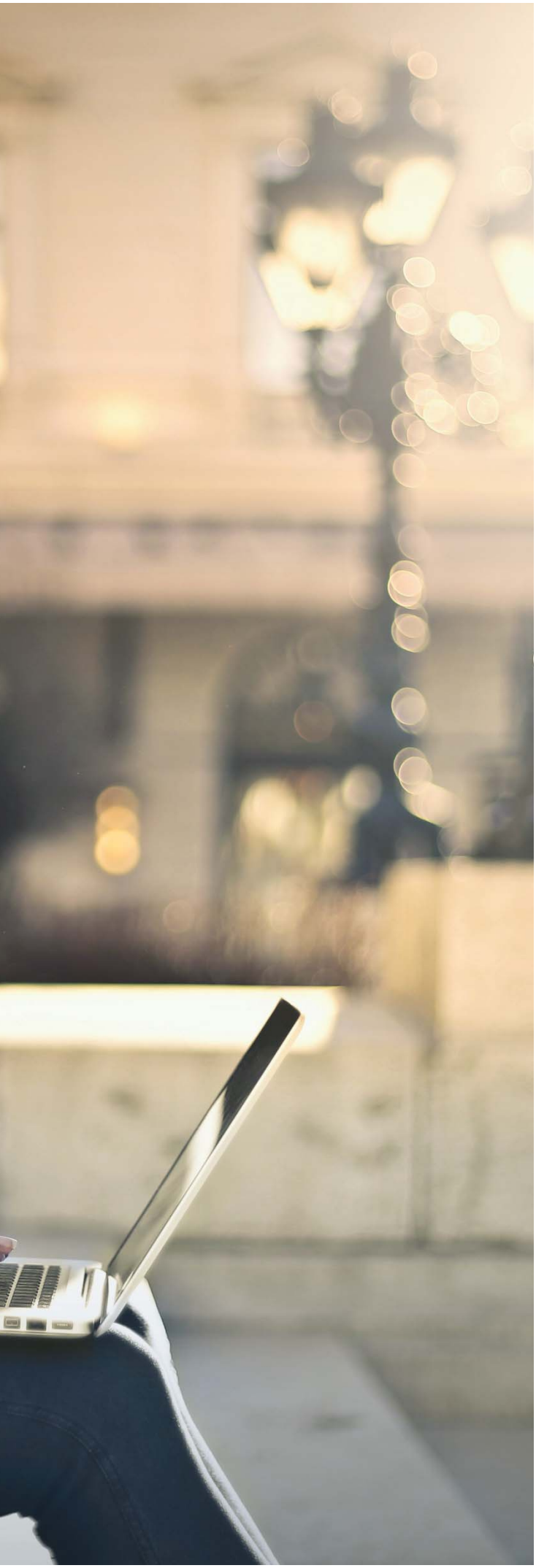
2016/17: seven

The Graduate Development Programme exposes participants to the role of the central bank in the economy and of the financial sector in general. Graduates gain work experience, are exposed to various roles and projects, and attend courses at the SARB Academy. Graduates showing potential may be permanently appointed by the SARB.

LEADERSHIP AND MANAGEMENT DEVELOPMENT

A framework to develop leaders and managers was developed during the year and a nine-module Management Fundamentals Programme is being rolled out.





SARB RETIREMENT FUND

The SARB Retirement Fund is a single scheme that provides a full spectrum of pension benefits to the employees of the SARB, South African Bank Note Company (RF) Proprietary Limited and South African Mint Company (RF) Proprietary Limited.

At 31 March 2018, the SARB Retirement Fund had 2 597 contributing members, 107 preserved members, 867 life annuitants, 233 life annuities (formerly the SARB Pension Fund), 52 living annuitants, and seven deferred retirees (members who have retired from the Group but not from the fund). The fund's total liability amounted to R6 151 million at year-end.

In addition to the statutory actuarial valuations performed every three years, interim actuarial valuations are conducted annually. The last statutory actuarial valuation was at 31 March 2015, and found the fund's financial position to be sound. The fund is finalising its 31 March 2018 statutory valuation.

The fund's assets are managed by an external asset manager with oversight by an Investment Committee. The Board of Trustees actively monitors changes in the retirement industry; including retirement legislation reform, the advent of Treating Customers Fairly legislation and the implementation of the Protection of Personal Information Act 4 of 2013. Members are kept informed of any changes through road shows, circulars and fund booklets. The operations of the fund are constantly reviewed to ensure compliance with legislative changes and leading retirement fund practice.

Looking ahead

People-related initiatives for 2018/19 are to:

> continue to drive a high level of engagement with employees;

> introduce initiatives to strengthen organisational culture;

> continue to develop leaders and managers; and

> embed talent management, performance management and reward processes.

CORPORATE SOCIAL INVESTMENT REPORT

The SARB aims to conduct its business practices in a transparent way based on ethical values, compliance with legal requirements and respect for people, communities and the environment. The SARB's social investment primarily focuses on initiatives that develop skill and support awareness of monetary policy and financial stability.

The objectives of the SARB's corporate social investment (CSI) strategy are to:

- develop human capital, particularly in the fields of monetary policy economics and financial stability;
- improve the quality of economic and financial journalism in South Africa and on the continent; and
- expand the understanding of monetary policy among high school learners.

CSI STRATEGY

EDUCATION

Access to education through funding

External bursaries
Offer bursaries to young people studying at tertiary institutions.

Academic research
- Support and fund the Chair of Monetary Economics at the University of Pretoria.
- Support and fund the Centre for Economic and Financial Journalism at Rhodes University.
- Support and fund the Chair of financial stability studies.
- Support and fund financial stability research grants.

MPC Schools Challenge
Competition for Grade 12 Economics learners.

EMPLOYEE VOLUNTEERISM

Employees who actively volunteer their personal time to community development

Mandela Day
Encourage employees to participate in the commemoration of Nelson Mandela.

ENTERPRISE DEVELOPMENT

Support small and micro enterprises with mentorship and incubation

Continued to mature inclusive procurement and work has started on enterprise acceleration.

EDUCATION

External bursaries

NUMBER OF STUDENTS SUPPORTED	TOTAL VALUE OF BURSARIES GRANTED	NUMBER OF STUDENTS THAT GRADUATED	DIVERSITY
58	R5.9 million	19	Of the **58 students** granted bursaries, **49 are black** and **33 are women**
2016: 50	2016: R4.2 million	2016: 9	2016: 25 black and 16 women

Academic research

BENEFICIARIES OF EDUCATION AND SKILLS DEVELOPMENT PROGRAMMES

	2017	2016	2015
University of Pretoria (postgraduate programme in Monetary Policy)	**60**[1]	39	59
Rhodes University[2] (Economic Journalism Programme)	**7**	10	9
External bursaries	**58**	50	42
Arts and culture bursaries	**2**	1	1
South African Institute of Chartered Accountants (bursary fund)	**5**	5	0
Sponsorship (matriculants)[3]	**0**	2	4
Total beneficiaries	**132**	107	115

1. *Seven of the 60 students are enrolled for a PhD.*
2. *Seven students graduated with either a Master's degree in Journalism or a postgraduate diploma in Economic Journalism.*
3. *Scholarship students were moved to the external bursary scheme.*

MPC Schools Challenge

Run in partnership with the Department of Basic Education, the MPC Schools Challenge provides an exciting opportunity for Grade 12 learners studying Economics to understand a few of the factors that the SARB needs to consider when it sets the country's repo rate. The challenge gives learners and their teachers the opportunity to step into the shoes of the MPC. In 2017, schools in the Eastern Cape, North West and Northern Cape provinces participated in the challenge for the first time and at the start of 2018, the challenge was rolled out to all nine provinces.

NUMBER OF SCHOOLS

	2017	2016	2015
Eastern Cape[1]	**12**	0	0
Free State	**22**	16	23
Gauteng	**39**	23	42
Limpopo	**42**	18	28
Mpumalanga	**13**	17	0
North West	**9**	0	0
Northern Cape	**4**	0	0
Total	**141**	74	93

1. *Learner briefing workshops were held in Port Elizabeth and East London.*

The operating model of the MPC Schools Challenge is under review, with a focus on the effectiveness of the programme in achieving its objectives. The review will aim to identify how the initiative can be made more cost effective through operational efficiencies and economies of scale.

EMPLOYEE VOLUNTEERISM

To commemorate Mandela Day on 18 July 2017, R1.5 million was allocated to 10 schools with special needs in seven provinces. Employee activities ranged from painting and tiling to electrical work and plumbing, as well as general repairs and cleaning, among others. The beneficiaries are public schools funded by the Department of Basic Education and which offer Mathematics and Economics subjects.

GOVERNANCE OF CSI

The SARB's CSI programme operates under the Executive Management Department with entrenched governance standards and structures. The Chief Operating Officer chairs the CSI Committee which is tasked with guiding, directing and overseeing the SARB's CSI initiatives and ensuring that fund allocation complies with the CSI Policy.

CSI SPEND (Rm)

	2017	2016	2015
University of Pretoria (postgraduate programme in Monetary Policy)	**2.5**	1.5	0.8
Rhodes University (Economic Journalism Programme)	**1.6**	1.6	1.6
External bursaries	**5.9**	4.3	2.6
Arts and culture bursaries	**0.1**	0.05	0.05
South African Institute of Chartered Accountants (bursary fund)	**0.7**	0.6	0.6
Sponsorship (matriculants)[1]	**0**	0.3	0.4
Employee volunteerism	**1.5**	2.5	0
MPC Schools Challenge[2]	**2.9**	1.1	1.0
Total expenditure	**15.2**	12.0	7.1

1. *Scholarship students were moved to the external bursary scheme.*
2. *The MPC Schools Challenge has been included in the CSI spend for the first time.*

SUBSIDIARY REPORTS

Each of the SARB's three subsidiaries has its own Board of Directors (Board) and Board members are appointed by the Governors' Executive Committee, except for the Corporation for Public Deposits whose Board members are appointed by the Minister of Finance. Each subsidiary's Board is ultimately accountable and responsible for the entity's performance and affairs.

SUBSIDIARY STRUCTURE

South African Reserve Bank

CURRENCY PRODUCING

SOUTH AFRICAN MINT COMPANY (RF) PROPRIETARY LIMITED (SOUTH AFRICAN MINT)	Produces coin and coin-related products for South Africa and the international export market.	**Board Chairperson** Deputy Governor F E (Francois) Groepe
SOUTH AFRICAN BANK NOTE COMPANY (RF) PROPRIETARY LIMITED (SABN)	Produces banknotes for South Africa and the international export market.	**Board Chairperson** Deputy Governor F E (Francois) Groepe

INVESTMENT SERVICES

CORPORATION FOR PUBLIC DEPOSITS (CPD)	Accepts call deposits from the public sector and invests these funds in deposits, short-term money-market instruments and special Treasury bills. The CPD may also accept call deposits from other depositors, if approved by the Minister of Finance.	**Board Chairperson** Deputy Governor A D (Daniel) Mminele

The work to more closely align the currency-producing subsidiaries, as well as their policies and procedures with those of the SARB, is ongoing. Functions such as risk management, internal audit, company secretariat, finance and security services are managed centrally, providing consistent management approaches and contributing to operating efficiencies. Both currency-producing subsidiaries made good progress against their strategic focus areas during the reporting period.

THE AUDITED FINANCIAL RESULTS OF THE SUBSIDIARIES ARE CONSOLIDATED WITH THOSE OF THE SARB IN THE SUMMARISED AND FULL GROUP ANNUAL FINANCIAL STATEMENTS.

SUMMARISED STATEMENTS
PG 80

THE SOUTH AFRICAN MINT COMPANY (RF) PROPRIETARY LIMITED

The South African Mint's business units

CIRCULATION COINS

Manufactures and supplies legal tender coins for circulation and transactional use in the economy.

COLLECTABLES

Produces premium products (primarily gold and silver) that cater for the collector, gift and investor markets.

PRESTIGE BULLION (RF) PROPRIETARY LIMITED (PRESTIGE BULLION)

A joint venture between the South African Mint and Rand Refinery Proprietary Limited (Rand Refinery). Prestige Bullion manufactures, sells and distributes bullion Krugerrand coins for local and international markets.

2017/18 PERFORMANCE OVERVIEW

The planned operationalisation of Prestige Bullion will better align the interests of shareholders, put in place dedicated personnel and resources, and enable a focused strategy that is more independent of Rand Refinery and the South African Mint. Both entities have agreed on the terms of the shareholder agreement extension.

The South African Mint successfully fulfilled its circulation coin order in South Africa, with good circulation coin export revenue which exceeded budget. Bullion Krugerrand coin sales achieved another record year, driven by buoyant domestic demand and solid international sales. The new anniversary Krugerrand products contributed to the profitability. Overall, the South African Mint contributed profit before tax of R952 million (2017: R668 million) to the Group.

The South African Mint is ISO 14001 certified and is applying for ISO 14001:2015 certification. Despite the presence of potentially hazardous substances and environmental processes, the site is recognised as a safe production facility. The lost time injury frequency rate (LTIFR) reached zero for the first time since 2011, and at financial year-end, the South African Mint achieved 1.25 million man hours worked without a lost-time injury.

Celebrating anniversaries was the prevailing theme for the reporting period.

FEBRUARY TO SEPTEMBER 2017

Celebrated the Krugerrand's 50th anniversary, with new fine silver and platinum coins, new sizes in the traditional gold coin range and the launch of limited edition Krugerrand fashion accessories.

OCTOBER 2017

Launched the 'Celebrating South Africa' theme to commemorate key milestones in South Africa's democracy. A product series commemorating former political leader, Mr Oliver Reginald Tambo's birth centenary was introduced. The R5 commemorative circulation coin was launched by the Governor of the SARB in the presence of Mr Tambo's family. The launch trended on Twitter and the entry-level base metal and sterling silver coins were very well received.

DECEMBER 2017

Produced a tickey and crown set to celebrate the 50th anniversary of the world's first successful human heart transplant at Groote Schuur Hospital, Cape Town.

Looking forward

During the 2018/19 financial year, the South African Mint will:

> Launch a silver bullion Krugerrand coin.

> Introduce a commemorative coin series to celebrate the 100th birth centenary of distinguished statesman and global icon, Nelson Mandela. The series will include three collectable coins (sterling silver, gold and uncirculated base metal) and a new bi-metallic R5 circulation coin, featuring new latent imaging technology, a security feature that will add to the coin's integrity.

> Launch a tickey and crown set focusing on South African inventions such as computed tomography (CT) scanning, and the first sample of the 2018 Natura product, which focuses on the rise of the dinosaurs.

THE SOUTH AFRICAN BANK NOTE COMPANY (RF) PROPRIETARY LIMITED

2017/18 PERFORMANCE OVERVIEW

The SABN achieved mixed results for the year under review, making a minor loss before tax of R8 million (2017: R174 million profit), largely due to a decline in production. A return to profitability is expected in 2018/19.

Quality concerns required the sourcing of alternative substrate, and resulted in production delays which required extensive overtime work to achieve production targets and complete the banknote order for 2017/18. Delays were also experienced on the production of the Mandela Centenary Series banknotes due to poor quality proofs and origination materials, and the order has been carried over to 2018/19.

In addition, 59 days of industrial action ended with organised labour accepting the original 6.6% salary increase offered by the SABN.

The overall manufacturing waste rate was 9.5% at 31 March 2018, above the target of 6.2%. The increased waste rate was due to the substrate quality which has subsequently been addressed.

The information and communications technology environment provided a stable, reliable and consistent level of service delivery, and the maturity of processes is improving. During the reporting year, the SABN worked with the SARB's Cyber and Information Security Unit to assess its cybersecurity exposure and enhancements are being implemented.

Other projects completed during the reporting year include the single campus for the SABN and the Pretoria North depot, and the installation of a seamless power solution. The depot was incorporated as part of the SABN as a finished goods warehouse, with no significant issues experienced. The power solution is fully operational, providing clean power seamlessly when municipal power is interrupted.

Pleasingly, the LTIFR was 0.23 against a tolerable level of 0.5. Training has been provided to manage a marked increase in first aid incidents. The safety, health and environmental management processes, including training and awareness, are continually reviewed to ensure that employees remain vigilant.

The SABN was re-certified for ISO 9001:2015 (quality management) and ISO 14001:2015 (environmental management) during the reporting year.

Chief Financial Officer, Mr A S (Ahmed) Haffejee, was appointed as the acting Managing Director following the retirement of Ms J (Joyce) Kumbirai with effect from 31 March 2017. The new Managing Director, Ms L (Liziwe) Mda, assumed her position on 2 May 2018.

THE CORPORATION FOR PUBLIC DEPOSITS

All funds invested with the CPD and the interest that is earned on these funds are repayable on demand.

The CPD is governed by the Corporation for Public Deposits Act 46 of 1984 and its Board meets four times a year. Board members, appointed by the Minister of Finance, comprise officials from the SARB and National Treasury. Given the CPD's scope and risk profile, the Board agrees that it is not necessary to appoint Board committees to support the CPD in the discharge of its responsibilities.

The CPD is accommodated at the SARB's head office and uses the SARB's accounting systems and infrastructure. The SARB's Financial Services Department is responsible for the administration and accounting of funds under the CPD's control, and the CPD's investment activities are performed by the SARB's Financial Markets Department.

GOVERNANCE AND ETHICS

The SARB strongly believes that its credibility and reputation are critical to its work and depends on excellent leadership. All leaders and employees of the SARB are required to maintain the highest level of ethics in ensuring that the practices of the SARB are conducted in a manner that is beyond reproach.

BOARD OF DIRECTORS

The SARB has a unitary board structure which functions in terms of the amended South African Reserve Bank Act 90 of 1989 (SARB Act) and a Board Charter. The Board of Directors (the Board) reviews the Board Charter and the terms of reference of all its committees every three years, unless otherwise required.

BOARD COMPOSITION

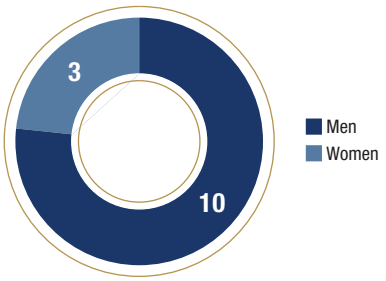
NUMBER OF BOARD MEMBERS

13 The SARB Act requires the Board to have 15 Board members. Non-executive directors for the two vacancies will be appointed by government in due course.

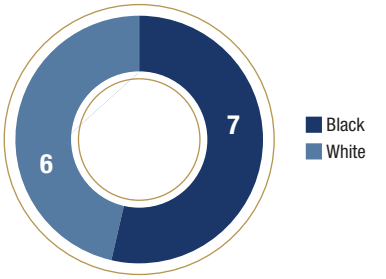
AVERAGE AGE OF BOARD MEMBERS

57.8 years

GENDER COMPOSITION



RACE COMPOSITION



DIRECTORS' CURRICULA VITAE PG 69

GOVERNOR

E L (Lesetja) Kganyago (52)
Governor

DEPUTY GOVERNORS

A D (Daniel) Mminele (53)
Deputy Governor

F E (Francois) Groepe (48)
Deputy Governor

K (Kuben) Naidoo (47)
Deputy Governor

NON-EXECUTIVE DIRECTORS

R J G (Rob) Barrow (71)
Chairperson of the
Audit Committee

T (Terence) Nombembe (56)

F (Firoz) Cachalia (59)
Chairperson of the Board
Risk and Ethics Committee

G M (Gary) Ralfe (73)
Chairperson of the Non-executive
Directors' Committee

C B (Charlotte) du Toit (52)

B W (Ben) Smit (67)

V J (Venete) Klein (59)
Chairperson of the
Remuneration Committee

N (Nicholas) Vink (62)

R (Rochelle) le Roux (53)

GOVERNANCE REPORT

"Nelson Mandela represented the best version of ourselves as South Africans. While preserving the value of money is our main mandate, our purpose is to be a bastion of institutional strength, contributing to a stable and prosperous economy that serves the well-being of all South Africans, and guided in part by Madiba's values."

Governor of the SARB | Lesetja Kganyago

BOARD OF DIRECTORS

The Governor and three Deputy Governors of the SARB are executive members of the Board. They are appointed by the President of the Republic of South Africa after consultation with the Minister of Finance and the Board. For their first term of office, the Governor and Deputy Governors are appointed for a period of five years. Thereafter, they may be reappointed for further terms of five years or less, per term.

In line with international practice, the Governor serves as both the Chief Executive Officer (CEO) of the SARB and Chairperson of the Board, with a casting and deliberative vote as stipulated in the SARB Act. This does not comply with the fourth King Report on Corporate Governance (King IV) which recommends that a chairperson be an independent non-executive director. The Chairperson of the Non-executive Directors' Committee fulfils the role of lead independent non-executive director and has unrestricted access to the Governor.

In consultation with the Minister of Finance, the President of the Republic of South Africa also appoints four non-executive directors to the Board and the remaining seven non-executive directors are elected by the SARB's shareholders. The non-executive directors may serve up to three terms of three years each, which is considered an appropriate period of service for SARB Board members.

At 31 March 2018, there were two vacancies on the Board for government-appointed non-executive directors.

CHANGES MADE TO THE BOARD IN THE CURRENT REPORTING YEAR
PG 82

Non-executive directors do not have service contracts with the SARB. The SARB Act sets the 'fit and proper' criterion for directorship and makes provision for a Panel to evaluate prospective non-executive directors. This ensures that the Board operates with integrity and a diversity of knowledge and skills to enable effective governance.

Advertisements calling for the nomination of candidates to fill shareholder-elected Board vacancies are placed in national newspapers, and on the websites of the Institute of Directors South Africa and the SARB. The Panel evaluates prospective non-executive directors, taking into account skill, knowledge and diversity, and recommends a maximum of three candidates for each vacancy. The SARB's shareholders consider the recommendations and elect the non-executive directors at the annual Ordinary General Meeting (AGM).

Board members perform annual self-assessments to evaluate the functioning of the Board and its committees. The Chairperson meets annually with all Board members individually to discuss various issues. Among other things, these discussions also inform recommendations for the nomination (or otherwise) of a Board member for re-election. Recommendations are made after the needs and skills of the Board, and the contribution of non-executive directors to the work of the Board, have been assessed.

The SARB Act stipulates the matters that the Board must consider and the Board Charter sets out the rules and procedures for the Board to ensure the proper discharge of its governance functions. The Board receives reports on governance and oversight matters from the Governors' Executive Committee (GEC) (which is responsible for the day-to-day management of the SARB) and the various Board committees (which are chaired by non-executive directors). The Board ordinarily meets five times a year.

CURRICULA VITAE

GOVERNOR

E L (Lesetja) Kganyago (52)

Appointed Governor:
9 November 2014.

Served as a Deputy Governor:
16 May 2011 to 8 November 2014.

Responsible for: Executive Management Department, SARB Secretariat, General Counsel, and Internal Audit and Economic Research and Statistics departments.

Before his appointment to the SARB, Mr Kganyago was Director General of National Treasury. He has represented South Africa in international organisations such as the World Bank, the International Monetary Fund (IMF), the Group of 20 (G-20) and the African Development Bank. Mr Kganyago holds a Master of Science (MSc) degree in Economics from London University's School for Oriental and African Studies and a Bachelor of Commerce (BCom) degree in Economics and Accounting from the University of South Africa (Unisa). He has received training in the fields of finance, economics and management.

Awards earned by Mr Kganyago during the past year include:

> Global Markets Awards – Governor of the Year for Sub-Saharan Africa (October 2017).

> The Association of Black Securities and Investment Professionals Lifetime Achiever Award (October 2017).

> Sunday Times – Companies Business Leader of the Year (November 2017).

> Central Banking – Governor of the Year Award (March 2018).

In January 2018, Mr Kganyago was appointed Chairperson of the International Monetary and Financial Committee (IMFC) for a term of three years. He is the first Southern African Development Community (SADC) Governor to be appointed to this position. The IMFC is the primary advisory body of the IMF Board of Governors and deliberates on the principal policy issues facing the IMF.

DEPUTY GOVERNORS

A D (Daniel) Mminele (53)

Deputy Governor appointment: first appointed on 1 July 2009 and reappointed for a second five-year term on 1 July 2014.

Responsible for: Financial Markets Department, International Economic Relations and Policy, Legal Services and Human Capital and Operations Cluster.

Mr Mminele is the G-20 central bank deputy for South Africa and the Chairperson for the IMFC's deputies. He holds a diploma in Banking (Bankkaufmann) awarded by the Chamber of Industry and Commerce (Bielefeld, Germany), and certificates from the Chartered Institute of Bankers in London. Mr Mminele has completed an Executive Leadership Programme at the Wharton School of Business and Goldman Sachs. His experience before joining the SARB includes credit-risk analysis, corporate banking, and project and structured finance at private banking institutions in Germany, the United Kingdom (UK) and South Africa.

In January 2018, Mr Mminele was awarded the Great Order of Merit by the President of the Federal Republic of Germany for his work in furthering German-South African relations. The Order of Merit is the highest tribute the Federal Republic of Germany can pay to individuals (both citizens and foreigners) for services to the nation.

F E (Francois) Groepe (48)

Appointed non-executive director: July 2004.

Deputy Governor appointment: first appointed on 1 January 2012 and reappointed for a second five-year term in 2017.

Responsible for: Financial Stability and Currency Management clusters.

Mr Groepe represents the SARB in various international forums and standard-setting bodies such as the Bank for International Settlements' Committee on Payments Market Infrastructures, the Financial Stability Board's Standing Committee on Standards Implementation, the Resolution Steering Group and the Regional Consultative Forum. Prior to joining the SARB, Mr Groepe was the Group Managing Director and CEO of Media24. He holds BCom (Hons) and Master of Business Administration (MBA) degrees from Stellenbosch University, Bachelor of Laws (LLB) and Masters of Laws (LLM) degrees from Unisa, a MSc Finance (Economic Policy) degree from London University's School for Oriental and African Studies and a postgraduate diploma in Tax Law from the University of Cape Town. He is a Chartered Management Accountant and an Advocate of the High Court of South Africa.

K (Kuben) Naidoo (47)

Appointed Deputy Governor and CEO of the Prudential Authority (previously Registrar of Banks):
1 April 2015.

Served as an Advisor to the Governor: from 1 April 2013.

Responsible for: Prudential Authority Cluster.

Mr Naidoo previously headed the Secretariat at the National Planning Commission in the Presidency, and the Budget Office at National Treasury. He holds an MBA from the University of Birmingham in the UK and a Bachelor of Science (BSc) degree and a postgraduate diploma in Public Management from the University of the Witwatersrand (Wits).

NON-EXECUTIVE DIRECTORS

	REPRESENTATION	COMMITTEE MEMBERSHIP	OTHER DIRECTORSHIPS
R J G (Rob) Barrow (71) QUALIFICATION: Chartered Accountant South Africa (CA(SA)) and has been actively involved in financial markets regulation and the setting of accounting standards in South Africa. Has knowledge and skills in commerce and finance.	**Shareholder elected:** July 2011, re-elected in July 2014 and again in 2017 for a final three-year term.	**Audit Committee (Chairperson)** **Board Risk and Ethics Committee** **Non-executive Directors' Committee**	*Non-executive director of the SARB's two currency producing subsidiaries and Strate (Pty) Limited (the South African central securities depository).*
F (Firoz) Cachalia (59) QUALIFICATION: LLB, LLM, Bachelor of Arts (BA) and BA (Hons) degrees, higher diploma in Company Law; admitted as an attorney.	**Government appointed:** July 2012 and re-appointed in 2015 for another three years.	**Audit Committee** **Board Risk and Ethics Committee (Chairperson)** **Non-executive Directors' Committee**	*Adjunct Professor at the Wits Law School and participates on the boards of various organisations.*
C B (Charlotte) du Toit (52) QUALIFICATION: Doctor of Philosophy (PhD) (Econometrics). Has knowledge and skills in industry.	**Shareholder elected:** July 2016.	**Board Risk and Ethics Committee** **Non-executive Directors' Committee**	*Plus Economics Advisory Pty (Ltd).*
V J (Venete) Klein (59) QUALIFICATION: Chartered Director South Africa (CD(SA)), business and financial qualifications from Harvard, Insead Business School, the Massachusetts Institute of Technology, the International Institute for Management Development and Wits. Has knowledge and skills in commerce and finance.	**Shareholder elected:** July 2015.	**Non-executive Directors' Committee** **Remuneration Committee (Chairperson)**	*Calgo M3 Holdings, PG Group, DB Schenker.*
R (Rochelle) le Roux (53) QUALIFICATION: Law degrees and diplomas from local and international universities, including a PhD. Has knowledge and skills in labour.	**Shareholder elected:** July 2011, re-elected in July 2014 and again in 2017 for a final three-year term.	**Non-executive Directors' Committee** **Remuneration Committee**	*Director of the Institute of Development and Labour Law and Head of Department of Commercial Law, Faculty of Law, University of Cape Town.*

T (Terence) Nombembe (56)	REPRESENTATION	COMMITTEE MEMBERSHIP	OTHER DIRECTORSHIPS
QUALIFICATION CA(SA), Bachelor of Accounting Science (BCompt) (Hons), BCom, conferred with an Honorary Doctorate in Accounting Science by the Walter Sisulu University.	**Government appointed:** July 2014 and re-appointed in July 2017.	**Audit Committee** **Board Risk and Ethics Committee** **Non-executive Directors' Committee**	*None.*

G M (Gary) Ralfe (73)			
QUALIFICATION BA (Hons) (Cantab) and Baccalaureus Procurationis (BProc) (Unisa) degrees. Has knowledge and skills in mining.	**Shareholder elected:** July 2011, re-elected in July 2014 and again in 2017 for a final three-year term.	**Audit Committee** **Non-executive Directors' Committee (Chairperson)** **Remuneration Committee**	*Chairperson or Director of four public benefit organisations involved in education, health and the promotion of constitutional democracy.*

B W (Ben) Smit (67)			
QUALIFICATION Doctor of Commerce (DCom) and Master of Commerce (MCom) degrees in Economics. Has knowledge and skills in industry.	**Shareholder elected:** December 2010, re-elected in July 2013 and again in 2016 for a final three-year term.	**Board Risk and Ethics Committee** **Non-executive Directors' Committee**	*None.*

N (Nicholas) Vink (62)			
QUALIFICATION PhD (Agriculture) in Agricultural Economics. Has knowledge and skills in agriculture.	**Shareholder elected:** July 2016.	**Non-executive Directors' Committee** **Remuneration Committee**	*Chair of the Department of Agricultural Economics at Stellenbosch University, non-executive director on the Board of Rooibos Ltd, Chairperson of the Board of Trustees for the Centre for Rural Legal Studies, President-elect of the International Association of Agricultural Economists.*

BOARD AND ITS COMMITTEES

Board committee structure at 31 March 2018

Meeting attendance (1 April 2017 to 31 March 2018)

	Appointment	Board 6 meetings	Audit 4 meetings	BREC 4 meetings	Nedcom 4 meetings	Remco 4 meetings
E L (Lesetja) Kganyago (^)	9/11/2014	**6/6**	**4/4**	**4/4**	**1/4**	**4/4**
A D (Daniel) Mminele (>*)	1/7/2009	**6/6**	**3/4**	n/a	n/a	**2/4**
F E (Francois) Groepe (°*)	1/1/2012	**5/6**	**3/4**	**3/4**	n/a	n/a
K (Kuben) Naidoo	1/4/2015	**6/6**	n/a	**4/4**	n/a	n/a
B W (Ben) Smit	8/12/2010	**6/6**	n/a	**4/4**	**4/4**	n/a
G M (Gary) Ralfe	1/7/2011	**6/6**	**4/4**	n/a	**4/4**	**4/4**
R J G (Rob) Barrow	1/7/2011	**6/6**	**4/4**	**4/4**	**4/4**	n/a
R (Rochelle) le Roux (*)	1/7/2011	**5/6**	n/a	n/a	**4/4**	**4/4**
M (Maureen) Manyama (†*)	6/10/2011	**3/6**	**1/4**	n/a	**1/4**	n/a
T (Tania) Ajam (#)	6/10/2011	**4/6**	n/a	**2/4**	**2/4**	n/a
F (Firoz) Cachalia	16/7/2012	**6/6**	**4/4**	**4/4**	**4/4**	n/a
T (Terence) Nombembe (*)	14/7/2014	**5/6**	**4/4**	**4/4**	**3/4**	n/a
V J (Venete) Klein	31/7/2015	**6/6**	n/a	n/a	**4/4**	**4/4**
C B (Charlotte) du Toit	30/7/2016	**6/6**	n/a	**4/4**	**4/4**	n/a
N (Nicholas) Vink (*)	30/7/2016	**5/6**	n/a	n/a	**3/4**	**3/4**

Chairperson of the Board or committee.
^ *Attends Audit Committee, Remco and Nedcom meetings by invitation.*
> *Attends Audit Committee and Remco meetings by invitation.*
° *Attends Audit Committee meetings by invitation.*
Term expired on 5 October 2017.
† *Resigned on 28 July 2017.*
* *Apologised for absence(s).*
n/a: not applicable.

AUDIT COMMITTEE

Chairperson: R J G (Rob) Barrow, an independent non-executive director, who is also a member of BREC.

Members: all four committee members are independent non-executive directors with financial expertise and two members are chartered accountants. At 31 March 2018, there was one vacancy on the committee.

By invitation: Governor E L (Lesetja) Kganyago, Deputy Governor A D (Daniel) Mminele, Deputy Governor F E (Francois) Groepe, the Chief Operating Officer (COO), the (acting) Head of the Financial Services Department (FSD) and (acting) Group Chief Financial Officer, the Chief Internal Auditor, the Head of the Risk Management and Compliance Department (RMCD).

Roles and responsibilities

In line with its terms of reference the Audit Committee has an objective, independent role and assists the Board in fulfilling its oversight responsibilities for financial reporting, the system of internal controls, the audit process and, as appropriate, the SARB's compliance with laws and regulations as they relate to financial reporting. The committee also reviews the deliberations and minutes of the audit committees of the SARB's currency-producing subsidiaries (the South African Mint Company (RF) Proprietary Limited and the South African Bank Note Company (RF) Proprietary Limited).

The Chairperson is a member of the audit committees of the currency-producing subsidiaries, ensuring the sharing of information and alignment with the Group's policies.

The internal and external auditors have unrestricted access to the committee's Chairperson, and the committee meets regularly with the heads of the Business Systems and Technology Department, the FSD, the RMCD, the Internal Audit Department and the external auditors.

Key activities in 2017/18

> Reviewed all significant internal audit findings and monitored management's responses to these findings.

> Received a combined assurance report in May 2018 at the same time that the draft 2017/18 Annual Report was considered. The committee was satisfied with the assurance that the SARB's control environment is sound.

> Reviewed and approved the annual fee limits for non-audit work by the statutory auditors for the SARB and the Group.

> Reviewed the scope of the internal and external statutory audits.

> Conducted its annual self-assessment, as well as assessments of the SARB's internal audit and financial functions, and the external auditors.

> Considered the implications of the IFRS 9 requirements, which apply to the SARB's financial reporting from 1 April 2018.

REPORT OF THE AUDIT COMMITTEE
PG 84

BOARD RISK AND ETHICS COMMITTEE

Chairperson: F (Firoz) Cachalia, an independent non-executive director, who is also a member of the Audit Committee.

Members: six non-executive directors, the Governor and two Deputy Governors, one being the Deputy Governor responsible for the RMCD. At 31 March 2018, there was one vacancy on the committee.

By invitation: the COO. In addition, the Chairperson of the Remuneration Committee attends meetings where ethical reports are considered.

Roles and responsibilities

The BREC assists the Board in discharging its responsibilities with regard to risk management and good corporate citizenship. The committee oversees and monitors all matters relating to risk management, including the status of risk management, the effectiveness of the Risk Management Policy and activities, the mitigating measures that address key risks and the Group's risk management disclosure. It also monitors the Group's activities to ensure responsible corporate citizenship, specifically those related to social and ethics responsibilities.

Key activities in 2017/18

> Considered Group-wide and departmental risk reports (including strategic, operational, financial, legal, compliance, reputational and security risk areas) and the results of the combined assurance model for the Group.

> Considered the SARB's Corporate Social Investment Policy and report.

> Monitored all matters reported to the whistle-blowing hotline.

NON-EXECUTIVE DIRECTORS' COMMITTEE

Chairperson: G M (Gary) Ralfe, an independent non-executive director.

Members: all members are non-executive directors. At 31 March 2018, there were two vacancies on the committee.

By invitation: executive directors and management, as required.

Roles and responsibilities

Nedcom's primary function is to assist the Board in fulfilling its legal and supervisory obligations and responsibilities, enhance corporate governance practices, ensure ongoing director training and development, and annually evaluate the performance of the Governor, Deputy Governors and the Secretary of the SARB.

Key activities in 2017/18

> Received presentations and discussed various topics on local and global economic environments, as well as specific areas of interest, as part of ongoing director training and development.

> Considered the performance of the Governor, Deputy Governors and the Secretary of the SARB.

> Considered the training needs of directors.

REMUNERATION COMMITTEE

Chairperson: V J (Venete) Klein, an independent non-executive director.

Members: three non-executive directors.

By invitation: Governor E L (Lesetja) Kganyago, Deputy Governor A D (Daniel) Mminele, the COO, Head of the Human Resources Department and Head of the SARB Academy.

Roles and responsibilities

Remco reviews the Bank-wide framework for human resources, as well as remuneration policies and practices. In line with its terms of reference, the committee recommends for the Board's consideration, the remuneration packages of the Governor and Deputy Governors, and the remuneration and incentives structures for employees. The executive directors, rather than Remco, recommend the remuneration of the Board's non-executive directors for confirmation by the Board. Recommendations take place after conducting relevant enquiries and benchmarking against similar organisations and surveys to determine an appropriate increase.

Key activities in 2017/18

> Monitored the implementation of various human resources initiatives, including talent management and the total reward strategy and wellness operating model.

> Reviewed the career path structures of various roles such as management and specialist, among others, and considered the findings of the Multiple Career Path review.

> Monitored the review of the SARB's human resources policies.

> Monitored the implementation of the cash management strategy, which impacted employees in the Currency Management and Group Security Management departments.

> Amended the Governors' Handbook, which covers the Board-approved rules relating to the benefits, privileges and conditions of service for the governors.

> Conducted an independent benchmark review of the non-executive directors' fees and the remuneration of the governors.

> Considered and approved the annual remuneration increases for employees and the budget for annual bonuses.

GENERAL MANAGEMENT

J (Johann) Bence (57)
Head: Currency Management Department

B (Bulelwa) Boqwana (50)
Chief of Staff – Executive Management

D E (Denzel) Bostander (45)
Head: Conglomerate Supervision Department

R (Rashad) Cassim (52)
Head: Economic Research and Statistics Department

J J (Johann) de Jager (63)
General Counsel

D P (David) Garnett (51)
Head: Group Security Management Department

G (Grant) Haarhoff (38)
Acting Head: Financial Services Department and Group Chief Financial Officer

M S (Saleem) Ismail (57)
Head: Business Systems and Technology Department

F (Faizel) Jeena (48)
appointed from 1 May 2018
Head: Specialist Risk Support Department

S B (Brian) Kahn (64)
Advisor to the Governor

W (Willie) Kamffer (56)
Head: Risk Management and Compliance Department

U (Unathi) Kamlana (38)
Head: Policy, Statistics and Support Department

H M (Ntebo) Kgoroba (52)
Head: Human Resources Department

G M (Gerdus) Lewis (44)
Head: Internal Audit Department and Chief Internal Auditor

C (Craig) Lister (43)
Head: Strategy Management Office

P (Pradeep) Maharaj (56)
Group Executive Currency Management

P M T (Tim) Masela (57)
Head: National Payment System Department

S E (Elijah) Mazibuko (54)
Head: Financial Surveillance Department

F S (Sandile) Mthiyane (44)
Head: Corporate Services Department

L R (Leon) Myburgh (51)
Head: Financial Markets Department

H F (Hendrik) Nel (57)
Head: Financial Stability Department

M (Mogam) Pillay (45)
Chief Operating Officer

L (Logan) Rangasamy (55)
Head: International Economic Relations and Policy Department

S L (Sheenagh) Reynolds (51)
Head: SARB Group Secretariat and Secretary of the SARB

J (Jabulani) Sikhakhane (53)
Head: Communications Division

N (Nomfundo) Tshazibana (41)
Advisor to the Governors

C J (Chris) van der Walt (55)
Head: Legal Services Department

S (Suzette) Vogelsang (50)
Head: Insurance, Banking and Financial Market Infrastructure Supervision

L (Lucy) Voss-Price (47)
Head: SARB Academy

EXECUTIVE MANAGEMENT

Governors' Executive Committee and its subcommittees

MONETARY POLICY COMMITTEE (MPC)

GOVERNORS' EXECUTIVE COMMITTEE (GEC)

FINANCIAL STABILITY COMMITTEE (FSC)

- **BUDGET COMMITTEE** (BC)
- **INFORMATION TECHNOLOGY STEERING COMMITTEE** (ITSC)
- **MANAGEMENT COMMITTEE** (Manco)
- **RESERVES MANAGEMENT COMMITTEE** (Resmanco)
- **RISK MANAGEMENT COMMITTEE** (RMC)

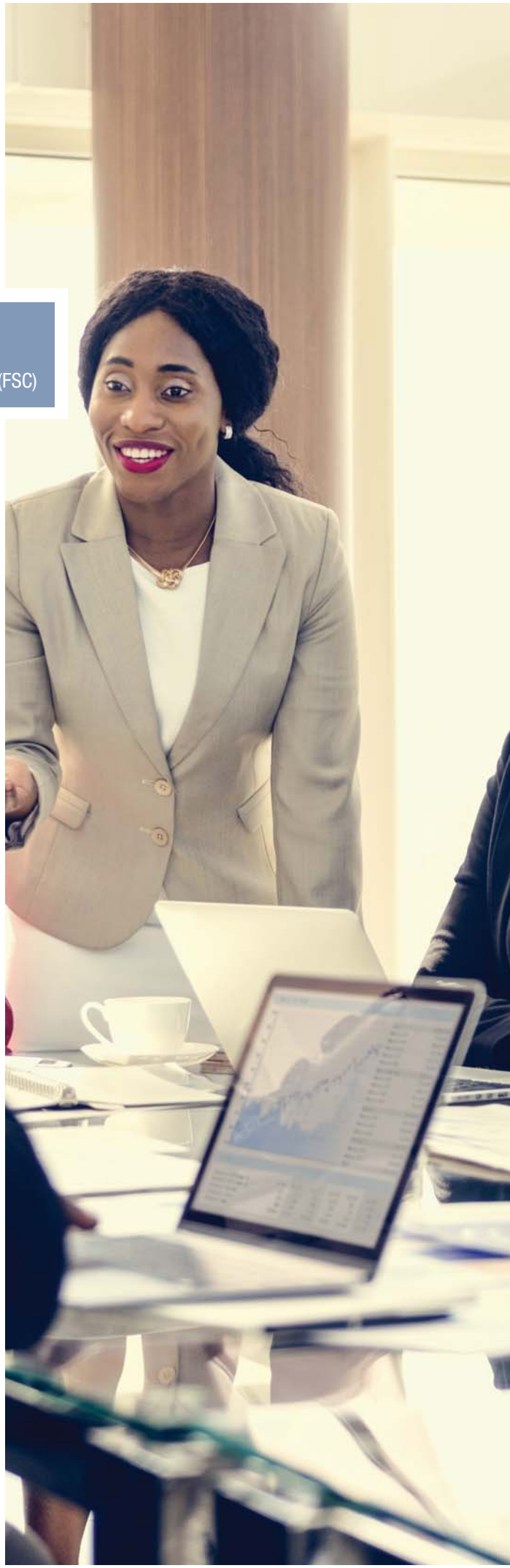
GOVERNORS' EXECUTIVE COMMITTEE

In their capacity as executive directors, the Governor and Deputy Governors are responsible for the day-to-day policy decisions and management of the SARB, except for those areas entrusted to the Board, MPC and FSC. The GEC meets every two weeks to consider policy issues and other executive management matters.

The members of the GEC are the Governor as Chairperson and the Deputy Governors. The COO, Group Executive Currency Management and General Counsel attend the meetings ex officio. The Secretary and Assistant Secretary of the SARB also attend the GEC meetings and maintain a record of the deliberations for dissemination to the Group, where applicable.

MONETARY POLICY COMMITTEE PG 27

FINANCIAL STABILITY COMMITTEE PG 36



BUDGET COMMITTEE

The BC is chaired by Deputy Governor K (Kuben) Naidoo, and is attended by eight senior employees of the SARB. The Procurement Committee, chaired by the COO, is a subcommittee of the BC and fulfils an important oversight role in the governance of the SARB's procurement processes.

The BC's responsibilities include:

> developing the SARB's budget guidelines and procedures;

> monitoring monthly budget variances;

> providing quarterly reviews to the GEC for submission to the Board;

> supervising, controlling and monitoring the process and compilation of annual departmental budgets and the SARB's consolidated budget; and

> facilitating the departmental annual budget proposal presentations to the BC and the GEC.

Once the GEC approves the budget – comprising operational, remuneration and capital budgets – it is tabled for Board approval.

The SARB'S budget for 2017/18 and 2018/19

	2018/19	2017/18		
	Board-approved budget R'000	Actual R'000	Revised budget R'000	Board-approved budget R'000
Personnel costs	**2 605 936**	2 481 008	2 467 675	2 365 541
Operational costs	**959 435**	771 130	851 876	915 918
Cost of new currency	**2 148 503**	1 041 854	1 381 336	1 562 832
Total operating expenditure	**5 713 874**	4 293 992	4 700 887	4 844 291
Capital expenditure	**814 284**	470 953	453 988	549 364
Overall expenditure	**6 528 158**	4 764 945	5 154 875	5 393 655

INFORMATION TECHNOLOGY STEERING COMMITTEE

The ITSC is chaired by Deputy Governor A D (Daniel) Mminele and is attended by 11 senior employees of the SARB. The committee's primary role is to provide strategic oversight to ensure alignment between the IT strategy and the SARB strategy. It is supported by its subcommittee, the Architecture Review Committee.

The key functions of the ITSC are to:

> ensure that all new IT initiatives align to the SARB's strategic objectives and architecture;

> prioritise IT projects and initiatives;

> ensure that IT delivers value through effective management and monitoring of IT project risks and IT resources; and

> approve IT investments.

MANAGEMENT COMMITTEE

Manco is chaired by Deputy Governor F E (Francois) Groepe; and all departmental heads, the Secretary of the SARB, the Group Executive Currency Management and the COO, are members. The Executive Management Chief of Staff, Executive Assistants to the Deputy Governors, Head of the Strategy Management Office and Head of the Communications Division attend by invitation.

The committee is responsible for monitoring progress on strategy implementation and the day-to-day operational management of the SARB, including:

> approving the cross-cutting procedures and organisational objectives for the internal operations of the SARB;

> developing and amending the SARB's administrative and operational policies; and

> providing assurance that the policies and operational systems of the SARB are aligned with best practice.

RISK MANAGEMENT COMMITTEE

The RMC is chaired by the Governor and its members are the Deputy Governors, the COO and five departmental heads. Its primary purpose is to assist the GEC by overseeing the risk management process in the Group and to report on this process to the GEC and BREC. Its main responsibilities are to monitor the implementation of the risk management strategy, policy and structure, and to assess and review the adequacy and effectiveness of the risk management process in the Group.

The RMC has three subcommittees: the Group Security Committee, the Business Continuity Management Committee and the Occupational Health and Safety Committee.

RISK MANAGEMENT
PG 19

RESERVES MANAGEMENT COMMITTEE

Resmanco is chaired by the Deputy Governor responsible for financial markets, A D (Daniel) Mminele, and comprises seven senior employees of the SARB. Its primary responsibilities are to oversee the implementation of the Gold and Foreign-Exchange Reserves Investment Policy and to facilitate the prudent investment of South Africa's official reserves.

In addition, Resmanco appoints external fund managers, financial custodians and securities lending agents, and determines the allocation of the risk budget, investment guidelines, and asset classes for tranches and portfolios. It recommends, for approval by the GEC, changes to the Gold and Foreign-Exchange Reserves Investment Policy, strategic asset allocation, the size of the Securities Lending Programme, the overall risk budget, tranche sizes and currency composition of tranches. Resmanco also monitors the parameters for the annual and periodic re-balancing of tranche sizes and currency composition, the management of the Securities Lending Programme and the implementation of the GEC resolutions in so far as they pertain to reserves management.

Resmanco reports its activities and risk and reserves management to the GEC quarterly, and to the Board annually. Two representatives from the National Treasury attend Resmanco meetings as observers.

KING IV

The SARB subscribes to King IV's principles of responsibility, accountability, fairness and transparency. The Board has implemented the principles where appropriate and where they do not contravene the legislation governing the SARB. To assure stakeholders that the SARB is ethically and sustainably managed within prudently determined risk parameters that comply with generally accepted corporate governance practices:

- the Board assesses the SARB's governance framework against best practice annually; and
- will regularly consider whether further application of the King IV principles can be implemented.

ETHICS

Given its role in society, the SARB must be, and must be seen to be, an institution of integrity that maintains the highest ethical standards.

The Group proactively ensures that the necessary policies, frameworks and procedures are in place to prevent and, if necessary, eradicate unethical behaviour or unlawful conduct. This is managed through the following policies and frameworks:

> Code of Ethics and Business Conduct;

> Outside Interests, Outside Occupations and Public Speaking Policy; and

> policies on commercial crime control, whistle-blowing, personal account trading and the receiving of gifts.

The BREC oversees the Group's ethics management programme, and the RMCD coordinates and facilitates the ethics management process, including the administration and analysis of annual employee declarations as prescribed by the above policies. Going forward, the SARB will work to raise ethics awareness within the organisation to support the consistent application of the Code of Ethics. Employee insight on ethics is gained through the employee engagement survey.

The integrated risk management process includes risk assessments on ethics management and commercial crime control. In addition, the internal audit process assists in identifying possible incidents of commercial crime and other irregularities.

An independent external hotline enables employees and the public to anonymously report dishonest or questionable practices and sensitive matters related to the business of the SARB. All allegations are treated seriously and investigated fully. The hotline is available 24/7 and callers can communicate with trained operators in English, Afrikaans, isiZulu and Sesotho.

SHAREHOLDING AND DIVIDEND

The SARB has private shareholders with limited rights, namely to consider the SARB's annual financial statements, elect seven of the non-executive directors of the Board, and appoint the external auditors and approve their remuneration. These activities take place at the SARB's AGM. The shareholders have no rights or involvement in the conduct of monetary policy, financial stability policy or regulation.

At 31 March 2018, the SARB had 765 shareholders. The SARB Act stipulates that shareholders are entitled to a 10 cents per share dividend on an annual basis paid from the accumulated reserves.

The SARB Act restricts shareholders to owning no more than 10 000 shares which include those shares held by associates. Only the shareholders who reside in South Africa are entitled to vote at the AGM and they hold one vote for every 200 shares.

REGULARISATION OF SHAREHOLDING IN THE SARB

On 4 November 2016, the Gauteng Division of the High Court in Pretoria (the High Court) issued an order to certain shareholders holding 149 200 SARB shares in contravention of section 22(1) of the SARB Act. The High Court directed these shareholders to dispose of their SARB shares, in aggregate with their associates, in excess of 10 000 shares. In addition, it appointed Investec Securities Proprietary Limited (ISL) to act as an independent broker to facilitate the disposal of the SARB shares over a two-year period from the date of the order and at a sale price of not less than R1.55 per share.

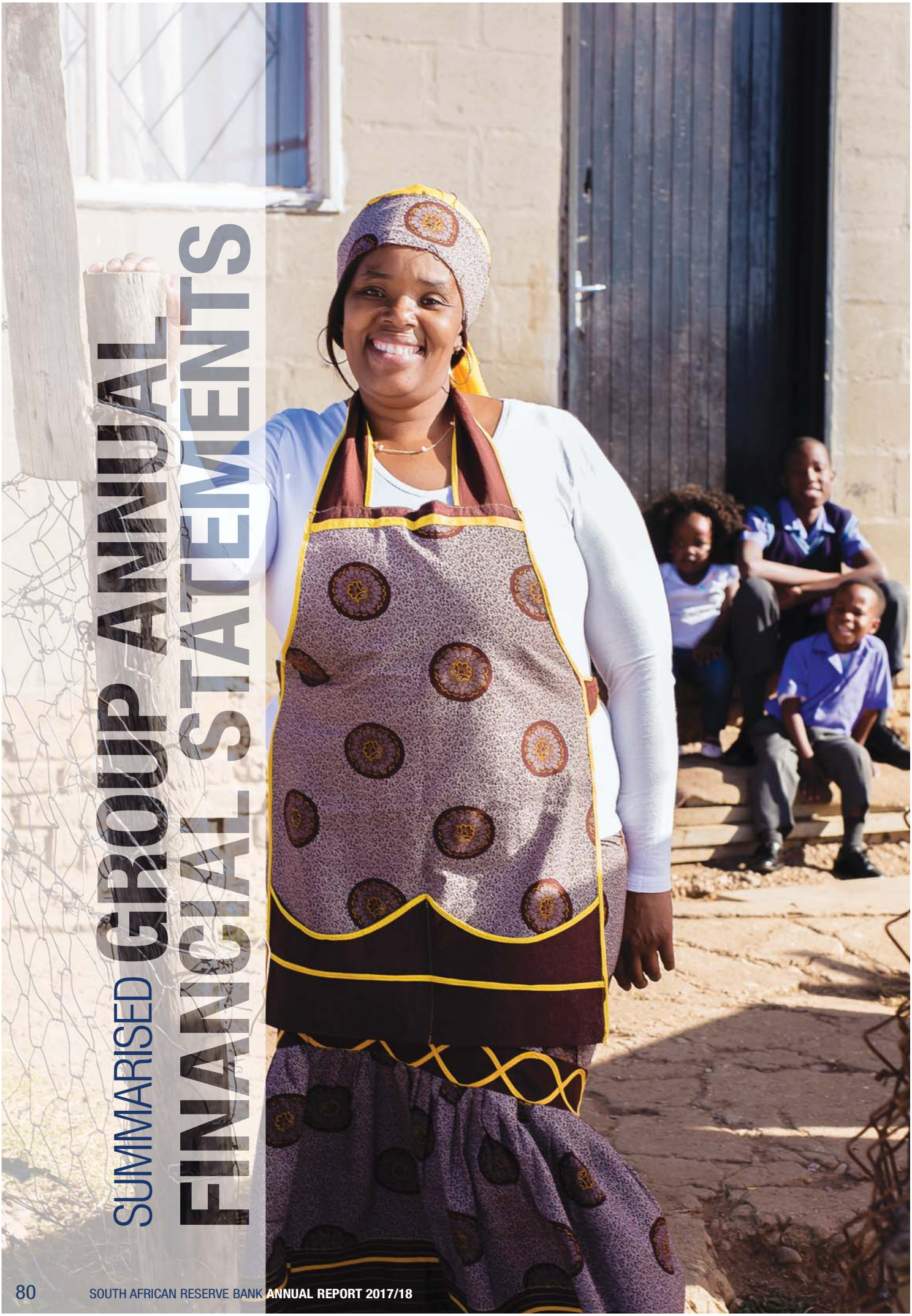
The High Court also directed the SARB's General Counsel to do all things necessary to enable the sale of the shares, including the signing of all necessary documentation and providing whatever assistance was required to ISL.

On 2 March 2017, the Governor announced the availability of these shares for purchase by eligible members of the general public. The response was overwhelming with the share offer being substantially oversubscribed.

The administrative process of matching the eligible buy offers with the available SARB shares was conducted in terms of the rules relating to SARB shares on the over-the-counter share transfer facility and in terms of section 35 of the SARB Act. The 149 200 SARB shares were subsequently sold to 58 new shareholders.

The requirements set by the High Court were finalised in January 2018 when the last proceeds were paid over to the affected shareholders who had held these SARB shares in contravention of the SARB Act.

SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS



DIRECTORS' REPORT

for the year ended 31 March 2018

INTRODUCTION

The directors are pleased to present to stakeholders this report on the activities and financial results of the South African Reserve Bank (SARB), including its subsidiaries and associate (Group), for the year under review.

This annual report, issued in terms of the South African Reserve Bank Act 90 of 1989 (SARB Act), as amended, and its regulations, addresses the performance of the Group and compliance with relevant statutory information requirements.

It is the responsibility of the directors to prepare the summarised Group annual financial statements and related financial information which present the Group's state of affairs.

These summarised Group annual financial statements were prepared on a going concern basis, taking cognisance of certain unique aspects relating to the SARB's ability to create, distribute and destroy domestic currency, its role as lender of last resort, its responsibilities in the areas of price and financial stability, and its relationship with the South African government (SA government) concerning foreign exchange and gold transactions.

The summarised Group annual financial statements include appropriate and responsible disclosure, and are based on accounting policies that have been consistently applied and which are supported by reasonable and prudent judgements and estimates.

The summarised Group annual financial statements were audited by the independent external auditors who were given unrestricted access to all financial records and related data, including minutes of all the meetings of the Board of Directors (Board) and its committees, as well as of executive management meetings.

The directors are responsible for governance, which is monitored on an ongoing basis. The SARB applies the principles and guidelines of the King Report on Corporate Governance in South Africa 2016 (King IV), where appropriate, and where they do not conflict with the SARB Act.

NATURE OF BUSINESS

The SARB is the central bank of South Africa and is regulated in terms of the SARB Act. Its primary objective is to protect the value of the currency in the interest of balanced and sustainable economic growth. In pursuit of price and financial stability, the SARB performs the key activities set out on page 4.

SUBSIDIARIES

The subsidiaries of the SARB are:

- The South African Mint Company (RF) Proprietary Limited (South African Mint), including its own subsidiary, Prestige Bullion (RF) Proprietary Limited (Prestige Bullion) which produces circulation, bullion and collectable coins.
- The South African Bank Note Company (RF) Proprietary Limited (SABN) which produces banknotes.
- The Corporation for Public Deposits (CPD) which receives and invests call deposits from the SA government and public entities.

Information on the SARB's financial interest in its subsidiaries is provided in note 18.

The subsidiaries did not pass any special resolutions that are material to the SARB's affairs in the year under review.

ASSOCIATE

African Bank Holdings Limited (ABHL) is the public holding company of African Insurance Group Limited (InsureCo) and African Bank Limited (ABL).

Information on the SARB's financial interest in its associate is provided in note 18.

ACHIEVEMENT OF OBJECTIVES

The annual report includes the SARB's achievements against its strategic objectives, which can be found on pages 8 to 10.

FINANCIAL RESULTS

The gradual normalisation of global interest rates has positively impacted the SARB's financial results and is likely to continue to do so for the short to medium term. Interest income of the SARB, derived mainly from foreign investments and accommodation to banks, increased by R0.5 billion (2017: R0.4 billion). Operating costs increased by R0.1 billion (2017: R0.2 billion), mainly attributable to once-off costs incurred as a result of the implementation of the Cash Management Strategy, offset by a reduction in the cost of new currency. The net result of these factors was a profit after taxation of R1.4 billion (2017: R1.4 billion) for the year ended 31 March 2018.

DIRECTORS' REPORT *continued*

for the year ended 31 March 2018

South African Mint (including Prestige Bullion) made a profit after taxation attributable to the parent of R0.4 billion (2017: R0.3 billion) and declared a dividend of R0.2 billion (2017: R0.2 billion) to the SARB. Refer to note 18 for further detail.

SABN incurred an after-taxation loss of R5.7 million (2017: R0.1 billion profit). The loss in the current year was mainly due to lower production volumes which are likely to reverse in the coming financial year. Refer to note 18 for further detail.

The CPD recorded a profit after taxation of R91.4 million (2017: R73.5 million), of which R91.2 million (2017: R73.3 million) was due to the SA government in accordance with the Corporation of Public Deposits Act 46 of 1984 (CPD Act). Refer to note 18 for further detail.

ABHL made a profit of R423.9 million before taxation (2017: R556.5 million loss) attributable to the Group. Refer to note 18 for further detail.

FINANCIAL POSITION

The Group's total assets decreased by R12.2 billion (2017: R68.6 billion), largely as a result of a decline in gold and foreign exchange reserves of R25.2 billion (2017: R70.6 billion), offset by an increase in cash and cash equivalents of R12.9 billion (2017: R19.7 billion).

Total liabilities of the Group decreased by R13.9 billion (2017: R69.7 billion) largely as a result of the Gold and Foreign Exchange Contingency Reserve Account (GFECRA) (used for the currency revaluation of foreign assets and liabilities which is for SA government's account) decreasing by R37.2 billion (2017: R73.5 billion), offset by increases in notes and coin in circulation of R14.0 billion (2017: 1.7 billion) and deposit accounts of R13.2 billion (2017: R2.9 billion decrease).

The decrease in both total assets and total liabilities was mainly as a result of a stronger rand and a lower South African rand (ZAR) gold price.

The contingency reserve increased by R1.8 billion (2017: R0.8 billion) due to the profit after taxation achieved for the year being transferred to the reserve.

Further details on the Group's financial information for the year, appear on page 87.

DIVIDENDS

The SARB Act permits the SARB to declare dividends from its accumulated profits (reserves). An interim dividend of five cents per share for the financial year was paid to shareholders on 20 October 2017; the final dividend, also of five cents per share, was paid on 11 May 2018. The total dividend paid for the financial year was R0.2 million (2017: R0.2 million).

DIRECTORS

The composition of the Board at 31 March 2018 is reported on pages 66 to 71.

The terms of office of R J G (Rob) Barrow (commerce or finance), R (Rochelle) le Roux (labour) and G M (Gary) Ralfe (mining) as shareholder-elected non-executive directors, expired the day after the 2017 annual Ordinary General Meeting (AGM).

All three non-executive directors were eligible for re-election and were re-elected at the AGM held on 28 July 2017 for their last term of three years.

The term of office of V J (Venete) Klein (commerce or finance), who is a shareholder-elected non-executive director, will expire the day after the 2018 AGM. Ms Klein has indicated that she will not be available for re-election.

The terms of office of T (Tania) Ajam, M (Maureen) Manyama and T (Terence) Nombembe, who are SA government appointed non-executive directors, expired during 2017. M (Maureen) Manyama resigned with effect from 28 July 2017 and T (Tania) Ajam was not available for re-appointment. Their positions were still vacant at financial year-end. The SA government has re-appointed T (Terence) Nombembe with effect from 14 July 2017 for a further term of three years.

The term of office of F (Firoz) Cachalia as a SA government appointed non-executive director will expire on 17 July 2018. He is eligible for re-appointment.

At 31 March 2018 and to date, none of the directors in office held any direct or indirect shareholding in the SARB.

Directors' fees for services rendered during the year under review are disclosed in the appendix on page 122.

EVENTS AFTER REPORTING DATE

Although not impacting the financial performance of the Group, we draw attention to the establishment of the Prudential Authority (PA), effective 1 April 2018. Refer to note 19 for more detail.

No other material events occurred between 31 March 2018 and 8 June 2018 requiring disclosure in, or adjustment to, the Summarised Group annual financial statements for the year ended 31 March 2018.

SECRETARY OF THE SARB

S L (Sheenagh) Reynolds

DIRECTORS' REPORT *continued*

for the year ended 31 March 2018

REGISTERED OFFICE

Business address:
370 Helen Joseph Street
(formerly Church Street)
Pretoria
0002

Postal address:
P O Box 427
Pretoria
0001

The summarised Group annual financial statements were approved by the Board on 8 June 2018 and signed on its behalf by:

E L (Lesetja) Kganyago
Governor

R J G (Rob) Barrow
Non-executive Director
and Chairperson of
the Audit Committee

G R (Grant) Haarhoff

Acting Group Chief
Financial Officer

S L (Sheenagh) Reynolds
Secretary of the SARB

STATEMENT BY THE SECRETARY OF THE SARB

In my capacity as Secretary of the SARB, I certify that all the returns required to be submitted, in terms of the SARB Act, for the year ended 31 March 2018, have been completed and are up to date.

S L (Sheenagh) Reynolds
Secretary of the SARB

8 June 2018

REPORT OF THE AUDIT COMMITTEE

for the year ended 31 March 2018

The Audit Committee is a committee of the Board. All its members, including the Chairperson, are independent non-executive directors. The responsibilities of the Audit Committee are set out in its terms of reference, which are approved by the Board and reviewed every three years or more frequently, if required.

The Audit Committee confirms that it carried out its functions responsibly and in compliance with its terms of reference, during the reporting year.

The SARB's executive management, internal auditors, external auditors and other assurance providers attend the Audit Committee's meetings in an ex officio capacity. Management and internal and external auditors meet independently with the committee, as appropriate.

ROLES AND RESPONSIBILITIES

The Audit Committee assists the Board in fulfilling its oversight responsibilities in terms of the SARB's financial reporting processes, risks and system of internal financial controls, as well as the SARB's processes for monitoring compliance with laws and regulations as they relate to financial reporting.

INTERNAL CONTROL (INCLUDING INTERNAL FINANCIAL CONTROLS)

The SARB's system of internal financial controls is designed to ensure:

- the integrity and reliability of financial information;
- compliance with all applicable laws and regulations;
- the accomplishment of objectives;
- economy and efficiency of operations; and
- the safeguarding of assets.

The Audit Committee is satisfied that this system of internal financial controls is adequately designed and operated effectively to form a sound basis for the preparation of reliable financial reports. This assessment is based on reports from management, risk management, internal auditors and external auditors.

The Audit Committee considered, and is satisfied with, the expertise and experience of the acting Group Chief Financial Officer (CFO). The finance function in the SARB has the expertise and adequate resources to support the acting Group CFO.

COMBINED ASSURANCE

The Group has adopted a combined assurance (CA) approach, in line with King IV, to increase the effectiveness of assurance activities by the functionaries within the three lines of assurance.

The Audit Committee considers the adopted CA approach to be adequate to achieve the said objectives of effective assurance activities across the Group.

SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS

The Audit Committee reviewed the summarised Group annual financial statements of the SARB and the external auditors' report thereon, and recommended their approval to the Board.

INTERNAL AUDIT

The Audit Committee reviewed and approved the Internal Audit Charter which defines the purpose, authority and responsibility of the internal audit function. The committee also approved the annual internal audit plan.

The Audit Committee reviewed the Internal Audit Department's (IAD) reports on control weaknesses and management's corrective actions.

The Audit Committee is satisfied that the IAD is independent and appropriately resourced to provide assurance on the adequacy and effectiveness of the internal control environment of the SARB. The Chief Internal Auditor (CIA) reports functionally to the Audit Committee and administratively to both the Chairperson of the Audit Committee and the Governor.

EXTERNAL AUDIT

The Audit Committee is satisfied with the independence of the external auditors of the SARB. This assessment was made after considering the independence letters from the external auditors, continuous monitoring and approval of non-audit services, and a formal partner rotation process.

In consultation with executive management, the Audit Committee reviewed the external auditors' proposed audit scope, approach and audit fees for the year under review.

The Audit Committee is satisfied with the formal procedures that govern the provision of non-audit services by the external auditors. This is monitored through reporting such activities to the committee.

COMPLIANCE

The Audit Committee is satisfied that the SARB has implemented appropriate processes and controls to ensure compliance with all applicable laws and regulations as they relate to financial reporting. This is based on the committee's review of reports received from both internal and external auditors, as well as from the executive management and relevant departments.

INFORMATION TECHNOLOGY

The Audit Committee is satisfied that the SARB is able to manage its information technology (IT) capability and that its IT controls are appropriate to support the integrity of financial reporting. This is based on the committee's continuous review of reports from IT management, as well as the internal and external auditors.

WHISTLE-BLOWING

Based on combined submissions from the Risk Management and Compliance Department and the IAD, the Audit Committee is satisfied that procedures have been established to receive, retain and resolve complaints regarding accounting, internal controls or auditing matters, including procedures for confidential and anonymous submissions in this regard.

R J G (Rob) Barrow
Chairperson of the Audit Committee

FINANCIAL REPORTING FRAMEWORK

REPORTING FRAMEWORK

The summarised Group annual financial statements have been prepared in accordance with the SARB Act and the accounting policies set out in note 1.

The SARB Act is not prescriptive regarding the accounting framework that the SARB should adopt, except for sections 25 to 28, which deal with the accounting treatment of gold and foreign exchange transactions. These sections are in conflict with the International Financial Reporting Standards (IFRS). The SARB has chosen to use IFRS as a guide in deciding on the most appropriate accounting policies to adopt, and as a model for the presentation and disclosure framework followed in its summarised Group annual financial statements.

The SARB Act, however, takes precedence over IFRS in the areas noted above and, as a result, the recognition and measurement criteria as set out in IFRS have not been followed in these circumstances. In addition, the SARB considers certain recognition and measurement principles as well as disclosures inappropriate to its functions. The SARB's summarised Group annual financial statements, therefore, disclose less detail than would be required under IFRS. The significant departures from IFRS as a consequence of the above are summarised as follows:

RECOGNITION AND MEASUREMENT

1. According to the SARB Act,
   a. realised and unrealised valuation gains and losses on gold, and realised and unrealised foreign exchange gains and losses on foreign denominated assets and liabilities are for the account of SA government, and have therefore not been accounted for in profit or loss, as required by *International Accounting Standard (IAS) 21 The Effects of Changes in Foreign Exchange Rates*; and
   b. gold is valued in terms of section 25 of the SARB Act at the statutory gold price. Gold has been recognised as a financial asset of the SARB.

2. Deferred taxation assets

   Deferred taxation assets are recognised for all deductible temporary differences, the carry forward of unused taxation losses and the carry forward of unused taxation credits. In the past, deferred taxation assets were not reduced to the extent that it was no longer probable in the foreseeable future that the related taxation benefits would be realised. This was a departure from IFRS. The standard requires that deferred taxation assets are reduced to the extent that it is no longer probable, in the foreseeable future, that the related taxation benefit will be realised.

   The principles of *IAS 12 Income Taxes* require an entity to demonstrate convincing evidence that future taxable profits will be available where the entity has unused taxation losses.

   Although the basis of preparation of the financial statements did not take into account the requirements of *IAS 12 Income Taxes* in the past, had the recognition and measurement principles of *IAS 12 Income Taxes* been applied, the deferred taxation asset raised would have been considered recoverable and would thus not have resulted in departure.

   The SARB has been profitable since the financial year ended 31 March 2016 and is projected to continue to generate profits in the foreseeable future. As a result of this profitability, previously carried forward taxation losses have been fully absorbed and at 31 March 2018 the SARB no longer has a deferred taxation asset relating to taxable losses. The SARB is mandated, as per the SARB Act, to operate as the sole central bank in South Africa and has been doing so for the past 97 years. The continuity of the SARB is therefore protected by statute and not dependent on market forces.

   It is therefore management's conclusion that the SARB has for the past two years complied with *IAS 12 Income Taxes* and that the departure is no longer applicable (refer to note 1). Furthermore management has assessed that retrospective application would not result in any adjustments to the current and prior two financial periods and thus no further disclosure is applicable.

PRESENTATION

In the summarised Group annual financial statements,

1. not all information as required by *IFRS 7 Financial Instruments Disclosures*, are disclosed. This relates specifically to:
   - Market risk: The sensitivity analysis for each type of market risk to which the SARB is exposed at the reporting date, showing how profit or loss and equity/other comprehensive income would have been affected by changes in the relevant risk variables that were reasonably possible at that date;
   - Credit risk: The credit quality per counterparty, the historical information about the counterparty default rates, the contractual maturity analysis of financial assets and the exposure to credit risk by class of financial instrument; and
   - Liquidity risk: the contractual maturity analysis of financial assets.
2. assets and liabilities relating to securities lending activities and financial derivative products used for portfolio management purposes have been disclosed, but offset in note 5 because it is considered inappropriate to gross up the foreign exchange reserves of the SARB.

INDEPENDENT AUDITOR'S REPORT ON THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS

OPINION

The summarised Group annual financial statements of South African Reserve Bank (SARB) set out on pages 87 to 121, which comprise the summarised Group statement of financial position as at 31 March 2018, the summarised Group statement of profit or loss and other comprehensive income, summarised Group statement of cash flows and summarised Group statement of changes in equity for the year then ended, and related notes, are derived from the audited Group annual financial statements of the SARB for the year ended 31 March 2018.

In our opinion, the accompanying summarised Group annual financial statements are consistent, in all material respects, with the audited Group annual financial statements, in accordance with the basis described in note 1 to the summarised Group annual financial statements.

EMPHASIS OF MATTER – BASIS OF ACCOUNTING

Our auditor's report on the audited Group annual financial statements includes an emphasis of matter paragraph highlighting note 1 to the Group annual financial statements, which describes the basis of accounting. The emphasis of matter further states that the Group annual financial statements are prepared for the purpose as described in the Group annual financial statements, and that as a result, the Group annual financial statements may not be suitable for any other purpose. As the summarised Group annual financial statements are derived from the Group annual financial statements, the summarised Group annual financial statements may also not be suitable for any other purpose.

SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS

The summarised Group annual financial statements do not contain all the disclosures required by the basis of accounting described in note 1 to the Group annual financial statements and the requirements of the South African Reserve Bank Act. Reading the summarised Group annual financial statements and the auditor's report thereon, therefore, is not a substitute for reading the audited Group annual financial statements and the auditor's report thereon.

THE AUDITED GROUP ANNUAL FINANCIAL STATEMENTS AND OUR REPORT THEREON

We expressed an unmodified audit opinion on the audited Group annual financial statements in our report dated 8 June 2018.

DIRECTOR'S RESPONSIBILITY FOR THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS

The directors are responsible for the preparation of the summarised Group annual financial statements in accordance with the basis described in note 1 to the summarised Group annual financial statements.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on whether the summarised Group annual financial statements are consistent, in all material respects, with the audited Group annual financial statements based on our procedures, which were conducted in accordance with *International Standard on Auditing (ISA) 810 (Revised), Engagements to Report on Summary Financial Statements*.

PricewaterhouseCoopers Inc.

PricewaterhouseCoopers Inc.
Director: Vincent Tshikhovhokhovho

Registered Auditor
4 Lisbon Lane
Waterfall City
2157

Johannesburg
8 June 2018

SizweNtsalubaGobodo Inc.

SizweNtsalubaGobodo Inc
Director: Agnes Dire

Registered Auditor
20 Morris Street East
Woodmead
2191

Johannesburg
8 June 2018

SUMMARISED GROUP STATEMENT OF FINANCIAL POSITION

at 31 March 2018

	Notes	**2018 R'm**	2017 R'm
Assets			
Cash and cash equivalents	2	**38 560**	25 676
Accommodation to banks	3	**66 850**	59 685
Investments	4	**5 833**	3 735
Gold and foreign exchange	5	**592 617**	617 783
Loans and advances	6	**17 570**	27 657
South African government bonds	7	**8 083**	8 153
Other assets		**12 192**	11 184
Total assets		**741 705**	753 873
Liabilities			
Notes and coin in circulation	8	**146 330**	132 297
Deposit accounts	9	**280 020**	266 821
Foreign deposits	10	**101 956**	106 655
South African Reserve Bank debentures	11	**340**	611
Gold and Foreign Exchange Contingency Reserve Account	12	**193 917**	231 158
Post-employment benefits	13	**3 451**	2 442
Other liabilities		**4 581**	4 481
Total liabilities		**730 595**	744 465
Capital and reserves[1]			
Share capital		**2**	2
Accumulated profit		**1 717**	1 459
Statutory reserve		**395**	395
Contingency reserve		**9 215**	7 400
Other reserves		**(283)**	101
Non-controlling interest		**64**	51
Total capital and reserves		**11 110**	9 408
Total liabilities, capital and reserves		**741 705**	753 873

(1) Further detail on capital and reserves is provided in the summarised Group statement of changes in equity.

SUMMARISED GROUP STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

for the year ended 31 March 2018

	Notes	**2018 R'm**	2017 R'm
Interest income		**13 575**	13 899
Interest expense		**(8 041)**	(8 317)
Net interest income		**5 534**	5 582
Dividend income		**47**	38
Operating income		**2 726**	2 046
Total income	14.1	**8 307**	7 666
Operating costs	14.2	**(5 487)**	(5 010)
Share of net profit/(loss) of associate accounted for using the equity method	18.2	**424**	(556)
Profit before taxation	14	**3 244**	2 100
Taxation		**(816)**	(717)
Profit for the year		**2 428**	1 383
Attributable to:			
The parent		**2 164**	1 202
Non-controlling interest		**264**	181
		2 428	1 383
Other comprehensive income (net of taxation)			
Items that will not be reclassified to profit or loss			
Remeasurement of post-employment benefits		**(564)**	(125)
Revaluation adjustments of property, plant and equipment		**(30)**	1
Items that may subsequently be reclassified to profit or loss			
Unrealised gain on available-for-sale financial assets		**211**	144
Realised gain on available-for-sale financial assets		**(1)**	–
Total comprehensive income for the year (net of taxation)		**2 044**	1 403
Attributable to:			
The parent		**1 780**	1 222
Non-controlling interest		**264**	181
Total comprehensive income		**2 044**	1 403

SUMMARISED GROUP STATEMENT OF CASH FLOWS

for the year ended 31 March 2018

	Notes	**2018 R'm**	2017 R'm
Cash flows from operating activities			
Cash generated from/(utilised by) operating activities	15	**16 276**	(2 613)
Taxation paid		**(270)**	(173)
Dividends paid		**(252)**	(210)
Transfer to SA government[1]		**(73)**	(73)
Net cash flows generated from/(utilised by) operating activities		**15 681**	(3 069)
Net cash flows generated from investing activities		**(2 797)**	22 797
Purchase of property, plant and equipment		**(565)**	(472)
Proceeds on disposal of property, plant and equipment		**3**	1
Purchase of intangible assets		**(134)**	(49)
Net (acquisition)/disposals of investments		**(2 101)**	23 317
Net increase in cash and cash equivalents		**12 884**	19 728
Cash and cash equivalents at the beginning of the year		**25 676**	5 948
Cash and cash equivalents at the end of the year		**38 560**	25 676

(1) Further detail on the transfer to SA government is provided in the summarised Group statement of changes in equity.

SUMMARISED GROUP STATEMENT OF CHANGES IN EQUITY

for the year ended 31 March 2018

	Share Capital R'm	Accu-mulated profit R'm	Statutory reserve R'm	Contin-gency reserve R'm	Other reserves R'm	Total R'm	Non-controlling interest R'm	Total R'm
Balance at 31 March 2016	**2**	**1 179**	**395**	**6 551**	**81**	**8 208**	**80**	**8 288**
Total comprehensive income for the year	–	1 202	–	–	20	1 222	181	1 403
Profit for the year	–	1 202	–	–	–	1 202	181	1 383
Remeasurement of post-employment benefits	–	–	–	–	(125)	(125)	–	(125)
Revaluation of property, plant and equipment	–	–	–	–	1	1	–	1
Unrealised gain on available-for-sale financial assets	–	–	–	–	144	144	–	144
Transfer to SA government	–	(73)	–	–	–	(73)	–	(73)
Transfer (from)/to reserves	–	(849)	–	849	–	–	–	–
Dividends paid	–	–	–	–	–	–	(210)	(210)
Balance at 31 March 2017	**2**	**1 459**	**395**	**7 400**	**101**	**9 357**	**51**	**9 408**
Total comprehensive income for the year	**–**	**2 164**	**–**	**–**	**(384)**	**1 780**	**264**	**2 044**
Profit for the year	**–**	**2 164**	**–**	**–**	**–**	**2 164**	**264**	**2 428**
Remeasurement of post-employment benefits	**–**	**–**	**–**	**–**	**(564)**	**(564)**	**–**	**(564)**
Revaluation of property, plant and equipment	**–**	**–**	**–**	**–**	**(30)**	**(30)**	**–**	**(30)**
Unrealised gain on available-for-sale financial assets	**–**	**–**	**–**	**–**	**211**	**211**	**–**	**211**
Realised gain on available-for-sale financial assets	**–**	**–**	**–**	**–**	**(1)**	**(1)**	**–**	**(1)**
Transfer to SA government	**–**	**(91)**	**–**	**–**	**–**	**(91)**	**–**	**(91)**
Transfer (from)/to reserves	**–**	**(1 815)**	**–**	**1 815**	**–**	**–**	**–**	**–**
Dividends paid	**–**	**–**	**–**	**–**	**–**	**–**	**(251)**	**(251)**
Balance at 31 March 2018	**2**	**1 717**	**395**	**9 215**	**(283)**	**11 046**	**64**	**11 110**

SUMMARISED GROUP STATEMENT OF CHANGES IN EQUITY *continued*

for the year ended 31 March 2018

EXPLANATORY NOTES

Statutory reserve

The statutory reserve is maintained in terms of section 24 of the SARB Act, which stipulates that one-tenth of the surplus of the SARB, after provisions normally provided for by bankers and payment of dividends, has to be credited to the statutory reserve.

Contingency reserve

In terms of section 24 of the SARB Act and section 15 of the CPD Act, contingency reserves are maintained to provide against risks to which the SARB and the CPD respectively are exposed.

Other reserves

Bond revaluation reserve

Gains and losses arising from a change in fair value of available-for-sale financial assets are recognised in other comprehensive income. When these financial assets are sold, collected or otherwise disposed of, the cumulative gain or loss previously recognised in other comprehensive income is recognised in profit or loss.

Property, plant and equipment revaluation reserve

Gains and losses arising from a change in fair value of artwork are recognised in other comprehensive income. When these assets are sold, collected or otherwise disposed of, the cumulative gain or loss previously recognised in other comprehensive income is recognised in accumulated profit.

Post-employment benefit remeasurement reserve

Actuarial gains and losses relating to the remeasurement of the post-employment benefits, and arising from experience adjustments and changes in actuarial assumptions, are charged or credited to equity in other comprehensive income in the period in which they arise. These gains and losses are not subsequently reclassified to profit or loss.

Transfer to SA government

In terms of section 24 of the SARB Act, nine-tenths of the surplus of the SARB, after provisions normally provided for by bankers and payment of dividends, has to be paid to SA government. No amount was transferred to SA government by the SARB in the current year as the SARB is rebuilding the contingency reserve.

In terms of section 15 of the CPD Act, the balance of net profits after transfers to reserves and payment of dividends has to be paid to SA government. For the year ended 31 March 2018 an amount of R91.2 million (2017: R73.3 million) was due to SA government by the CPD.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS

for the year ended 31 March 2018

1. ACCOUNTING POLICIES

1.1 Basis of presentation

The principal accounting policies adopted in the preparation of these summarised Group annual financial statements are set out below. These accounting policies should be read together with the financial reporting framework on page 85.

These summarised Group annual financial statements have been prepared on a going concern basis, in accordance with the SARB Act and the accounting policies set out in this note.

The preparation of the summarised Group annual financial statements requires the use of certain key accounting estimates. It also requires management to exercise judgement in the process of applying the accounting policies of the Group. The areas with a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the summarised Group annual financial statements, are disclosed in note 1.19 and the relevant notes.

The accounting policies have been applied consistently to all years presented, except for the change described below.

Change in accounting policy

In the current year, the Group elected to voluntarily change the Financial Reporting Framework by removing the deviation from IFRS relating to deferred taxation assets. Previously, the Group would recognise a deferred taxation asset in full and would not reduce it to the extent that it was no longer probable that in the foreseeable future there would be related taxation benefits.

The Group has been consistently making taxable profits and therefore the deferred taxation asset that was initially raised in terms of the deviation has been utilised. The Group is therefore of the view that based on the changes in the manner in which the Group makes taxable profits, it is highly unlikely that it would need to utilise the deviation going forward and therefore has voluntarily elected to change its basis of preparation by removing the deviation from the Financial Reporting Framework.

A voluntary change in accounting policy requires retrospective application with an adjustment to the opening accumulated profit for the earliest prior period presented, which is 1 April 2016. The Group has assessed that the impact of the change is immaterial in terms of the recognition and measurement of its deferred taxation asset as at 1 April 2016 and therefore no restatement is required for the voluntary change in accounting policy. Refer to the financial reporting framework on page 85.

1.2 New standards and interpretations

1.2.1 New and amended standards adopted by the Group

In the current year, the Group has adopted the following standards and interpretations that are effective for the current financial year and that are relevant to its operations:

» ***IAS 7 Statement of Cash Flows***

The IASB issued an amendment to *IAS 7 Statement of Cash Flows* introducing additional disclosure that will enable users of financial statements to evaluate changes in liabilities arising from financing activities.

The effective date of this amendment is for years commencing on or after 1 January 2017. The Group has adopted the amendment for the first time in the 2018 summarised Group annual financial statements. The amendment has no material impact on the summarised Group annual financial statements.

» ***IAS 12 Income taxes***

In January 2016, the IASB issued amendments to clarify the requirements for recognising deferred taxation assets on unrealised losses. The amendments clarify the accounting for deferred taxation where an asset is measured at fair value and that fair value is below the asset's taxation base. They also clarify certain other aspects of accounting for deferred taxation assets.

The effective date of this amendment is for years commencing on or after 1 January 2017. The Group has adopted the amendment for the first time in the 2018 summarised Group annual financial statements. The amendment has no material impact on the summarised Group annual financial statements.

There are no other new or amended standards applicable to the Group for the financial year ended 31 March 2018.

1.2.2 New standards, amendments and interpretations not yet adopted

A number of new standards, amendments and interpretations are effective for annual periods beginning after 1 April 2018, and have not been early adopted in preparing these summarised Group annual financial statements. None of these are expected to have a significant impact on the summarised Group annual financial statements, except for the following:

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.2 New standards and interpretations *continued*

1.2.2 New standards, amendments and interpretations not yet adopted *continued*

» ***IFRS 15 Revenue from Contracts from Customers***

New standard that requires entities to recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This core principle is achieved through a five step methodology that is required to be applied to all contracts with customers. The new standard will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively and improve guidance for multiple-element arrangements.

The effective date of the amendment is for years beginning on or after 1 January 2018. The Group expects to adopt the amendment for the first time in the first annual period after the effective date, commencing 1 April 2018. The amendment has no material impact on the summarised Group annual financial statements. The new standard supersedes:

– *IAS 11 Construction Contracts;*
– *IAS 18 Revenue;*
– *IFRIC 13 Customer Loyalty Programmes;*
– *IFRIC 15 Agreements for the Construction of Real Estate;*
– *IFRIC 18 Transfers of Assets from Customers; and*
– *SIC-31 Revenue – Barter Transactions Involving Advertising Services.*

» ***IFRS 9 Financial Instruments***

A final version of *IFRS 9 Financial Instruments* has been issued which replaces *IAS 39 Financial Instruments: Recognition and Measurement*. The completed standard comprises guidance on classification and measurement, impairment, hedge accounting and derecognition, and introduces a new approach to the classification of financial assets, which is driven by the business model in which the assets are held and their cash flow characteristics. A new business model was introduced in the standard which does allow certain financial assets to be categorised as "fair value through other comprehensive income" (FVOCI) in certain circumstances. The requirements for financial liabilities are mostly carried forward unchanged from *IAS 39 Financial Instruments: Recognition and Measurement*. However, some changes were made to the fair value option for financial liabilities to address the issue of own credit risk.

The new model introduces a single impairment model being applied to all financial instruments, as well as an "expected credit loss" (ECL) model for the measurement of financial assets. *IFRS 9 Financial Instruments* contains a new model for hedge accounting that aligns the accounting treatment with the risk management activities of an entity, it also requires enhanced disclosures that will provide better information about risk management and the effect of hedge accounting on the summarised Group annual financial statements. *IFRS 9 Financial Instruments* carries forward the derecognition requirements of financial assets and liabilities from *IAS 39 Financial Instruments: Recognition and Measurement*.

The mandatory effective date for implementation is for annual periods beginning on or after 1 January 2018. The Group expects to adopt the standard for the first time in the first annual financial period after the effective date, commencing 1 April 2018.

The Group has undertaken a detailed assessment of the impact of the application of *IFRS 9 Financial Instruments* on its summarised Group annual financial statements.

Classification and measurement

The classification and measurement of financial assets will depend on how these are managed (the entity's business model) and their contractual cash flow characteristics. These factors determine whether the financial assets are measured at amortised cost, FVOCI or fair value through profit or loss (FVPL). The combined effect of the application of the business model and the contractual cash flow characteristics tests may result in some differences in the population of financial assets measured at amortised cost or fair value compared with *IAS 39 Financial Instruments: Recognition and Measurement.* The Group expects the following reclassifications and remeasurements:

– SA government bonds currently classified as FVOCI will be classified as FVPL;
– Bank for International Settlements (BIS) shares currently classified as FVOCI and measured at cost will remain as FVOCI, but measured at fair value with the fair value movements recognised in the accounting records of the SARB;
– foreign deposits will be classified as FVPL and not amortised cost; and
– items measured at amortised cost (i.e. accommodation to banks, loans and advances, short term deposits and receivables) will be tested for impairment using the new ECL model.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.2 New standards and interpretations *continued*

1.2.2 New standards, amendments and interpretations not yet adopted *continued*

***Classification and measurement** continued*

The SARB will include a fourth classification category called "SARB Act" wherein all assets and liabilities affected by the SARB Act (where certain movements are posted to GFECRA), will be classified. The SARB deviates from IFRS due to the fact that the SARB Act takes precedence over IFRS (refer to the financial reporting framework on page 85). This category will allow for more accurate presentation and will give users of the SARB's summarised Group annual financial statements a clearer understanding of the impact of the SARB Act. The main items included in this category will be:

– Gold;

– Special Drawing Rights (SDRs);

– Forward exchange contract assets and liabilities; and

– GFECRA.

Impairment

The impairment requirements apply to financial assets measured at amortised cost and FVOCI, receivables, and certain loan commitments and financial guarantee contracts. At initial recognition, an impairment allowance (or provision in the case of commitments and guarantees) is required for expected credit losses (ECL) resulting from default events that are possible within the next 12 months (12-month ECL). In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument (lifetime ECL). Financial assets where 12-month ECL is recognised are in 'stage 1'; financial assets that are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment, so are considered to be in default or otherwise credit impaired, are in 'stage 3'. The assessment of credit risk and the estimation of ECL are required to be unbiased and probability-weighted, and should incorporate all available information relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money. As a result, the recognition and measurement of impairment is intended to be more forward-looking than under *IAS 39 Financial Instruments: Recognition and Measurement*, and the resulting impairment charge may be more volatile. *IFRS 9 Financial Instruments* may also result in an increase in the total level of impairment allowances, since all financial assets will be assessed for at least 12-month ECL and the population of financial assets to which lifetime ECL applies is likely to be larger than the population for which there is objective evidence of impairment in accordance with *IAS 39 Financial Instruments: Recognition and Measurement*. The Group has developed an impairment model which calculates an ECL allowance per counter party per instrument. The calculation itself essentially uses the closing balance (the exposure at default), multiplies it with a loss given default ratio (zero if the asset is fully collateralised and the collateral is highly liquid) and the probability of default. The probability of default is calculated using regression analysis. *IFRS 9 Financial Instruments* requires the use of forward looking information (such as macro-economic information) to adjust the probability of defaults of those entities at each reporting date. By using regression analysis, the impact of each macro-economic factor on the probability of default can be calculated. The assessment indicates that there are no major gaps in current impairment models due to the short nature of the financial assets and the fact that they are mostly over collateralised.

Transitional impact

The Group does not intend to restate comparatives.

For the SARB and Group, adoption is expected to increase net assets at 1 April 2018 by R2.3 billion, net of deferred taxation of R883.5 million. These estimates are based on accounting policies, assumptions, judgements and estimation techniques that remain subject to change until the Group finalises its financial statements for the year ending 31 March 2019.

» ***IAS 19 Employee Benefits***

These amendments require an entity to use updated assumptions to determine current service cost and net interest for the remainder of the period after a plan amendment, curtailment or settlement and recognise in profit or loss as part of past service cost, or a gain or loss on settlement, any reduction in a surplus, even if that surplus was not previously recognised because of the impact of the asset ceiling.

The effective date of the amendment is for years beginning on or after 1 January 2019. The Group expects to adopt the standard for the first time in the first annual financial period after the effective date, commencing 1 April 2019. The impact of this standard is currently being assessed.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.2 New standards and interpretations *continued*

1.2.2 New standards, amendments and interpretations not yet adopted *continued*

» ***IFRIC 22 Foreign Currency Transactions and Advance Consideration***

This IFRIC addresses foreign currency transactions or parts of transactions where there is consideration that is denominated or priced in a foreign currency. The interpretation provides guidance for when a single payment/receipt is made as well as for situations where multiple payments/receipts are made. The guidance aims to reduce diversity in practice.

The effective date of the amendment is for years beginning on or after 1 January 2018. The Group expects to adopt the standard for the first time in the first annual financial period after the effective date, commencing 1 April 2018. The impact of this standard is currently being assessed.

» ***IFRS 16 Leases***

This is a new standard that introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments. A lessee measures right-of-use assets similarly to other non-financial assets (such as property, plant and equipment) and lease liabilities similarly to other financial liabilities. As a consequence, a lessee recognises depreciation of the right-of-use asset and interest on the lease liability, and also classifies cash repayments of the lease liability into a principal portion and an interest portion and presents them in the statement of cash flows applying *IAS 7 Statement of Cash Flows. IFRS 16 Leases* contains expanded disclosure requirements for lessees. Lessees will need to apply judgement in deciding upon the information to disclose to meet the objective of providing a basis for users of financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of the lessee. *IFRS 16 Leases* substantially carries forward the lessor accounting requirements in *IAS 17 Leases*. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. *IFRS 16 Leases* also requires enhanced disclosures to be provided by lessors that will improve information disclosed about a lessor's risk exposure, particularly to residual value risk.

The effective date of the amendment is for years beginning on or after 1 January 2019. The Group expects to adopt the standard for the first time in the first annual financial period after the effective date, commencing 1 April 2019. The impact of this standard is currently being assessed.

The new standard supersedes:

- *IAS 17 Leases;*
- *IFRIC 4 Determining whether an Arrangement contains a Lease;*
- *SIC-15 Operating Leases – Incentives; and*
- *SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.*

There are no other IFRS or International Financial Reporting Interpretations Committee (IFRIC) interpretations that are not yet effective that would be expected to have a material impact on the Group.

1.3 Group accounting

1.3.1 Subsidiaries

Subsidiaries are all entities over which the SARB has control. The SARB controls an entity when the SARB is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the SARB.

The acquisition method of accounting is used to account for subsidiaries by the Group. Investments in subsidiaries are stated at cost less allowance for impairment losses where appropriate, and include loans to subsidiaries with no repayment terms where these are considered part of the investment in subsidiaries.

Intercompany transactions, balances and unrealised gains on transactions between the Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the transferred asset. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group, with the exception of the SARB's policy on foreign currency translation (refer to note 1.6). These foreign exchange profits or losses are for the account of SA government and are thus transferred to the GFECRA in terms of sections 25 to 28 of the SARB Act.

Non-controlling interests in the results and equity of subsidiaries are shown separately in the summarised Group statement of financial position, summarised Group statement of profit or loss and other comprehensive income and summarised Group statement of changes in equity respectively. Total comprehensive income of subsidiaries is attributed to the SARB and to the non-controlling interest, even if this results in the non-controlling interests having a deficit balance.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.3 Group accounting *continued*

1.3.2 Associate

An associate is an entity over which the Group has significant influence but not control or joint control. This is generally the case where the group holds between 20% and 50% of the voting rights.

An investment in associate is initially recognised at cost and adjusted thereafter to recognise the Group's share of the post-acquisition profits or losses of the investee in profit or loss, and the Group's share of movements in other comprehensive income of the investee in other comprehensive income. Dividends received or receivable from an associate are recognised as a reduction in the carrying amount of the investment.

When the Group's share of losses in an equity-accounted investment equals or exceeds its interest in the entity, including any other unsecured long-term receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the other entity.

Unrealised gains on transactions between the Group and its associate are eliminated to the extent of the Group's interest in this entity. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of the equity accounted investee have been changed where necessary to ensure consistency with the policies adopted by the Group, with the exception of the SARB's policy on foreign currency translation (refer note 1.6). These foreign exchange profits or losses are for the account of SA government and are thus transferred to the GFECRA in terms of sections 25 to 28 of the SARB Act.

The carrying amount of an equity-accounted investment is tested for impairment in accordance with the policy in note 1.9.

1.4 Financial instruments

Financial instruments include all financial assets and financial liabilities, including derivative instruments, but excluding investments in subsidiaries, investments in associates, post-employment benefit plans, provisions, property, plant and equipment, deferred taxation, intangible assets, inventories, surplus due to SA government and taxation payable or prepaid.

1.4.1 Financial assets

1.4.1.1 Classification

The Group classifies its financial assets into the following categories: financial assets at fair value through profit or loss (including held-for-trading), loans and receivables and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired.

Management determines the classification of financial assets at initial recognition.

Financial assets at fair value through profit or loss

This category comprises two subcategories: (i) financial assets held-for-trading, and (ii) those designated as fair value through profit or loss at inception.

A financial asset is classified as 'held-for-trading' if it is acquired principally for the purpose of selling in the short term, if it forms part of a portfolio of financial assets in which there is evidence of short-term profit-taking or if so designated by management. Derivatives are also classified as held-for-trading, unless they are designated as hedges at inception.

A financial asset is designated as 'fair value through profit or loss' when;

- either it eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring the asset, or recognising the gains or losses on it, on a different basis; or
- it forms part of a portfolio of financial assets that is managed and its performance is evaluated on a fair-value basis, in accordance with a documented risk management or investment strategy and information about the portfolio is provided internally on that basis to key management personnel; or
- it forms part of a contract containing one or more embedded derivatives and *IAS 39 Financial Instruments*: *Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as fair value through profit or loss.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. This category does not include those loans and receivables that the Group intends to sell in the short term or that it has designated as at fair value through profit or loss or available-for-sale.

Available-for-sale financial assets

Available-for-sale financial assets are those intended to be held for an indefinite period and may be sold in response to liquidity needs or changes in interest rates, exchange rates or equity prices. Financial assets that are either designated in this category or not classified in any of the other categories are classified as 'available-for-sale' financial assets. The main classes of financial assets classified as available-for-sale are South African government bonds and the equity investment in the BIS.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.4 Financial instruments *continued*

1.4.1 Financial assets *continued*

1.4.1.2 Reclassification

The Group may choose to reclassify a non-derivative trading financial asset out of the held-for-trading category if the financial asset is no longer held for the purpose of selling it in the near term. Financial assets other than loans and receivables are permitted to be reclassified out of the held-for-trading category only in rare circumstances arising from a single event that is unusual and highly unlikely to recur in the near term. In addition, the Group may choose to reclassify financial assets that would meet the definition of loans and receivables out of the held-for-trading or available-for-sale categories if the Group has the intention and ability to hold these financial assets for the foreseeable future or until maturity at the date of reclassification.

Reclassifications are made at fair value as at the reclassification date. Fair value becomes the new cost or amortised cost as applicable, and no reversals of fair value gains or losses recorded before reclassification date are subsequently made. Effective interest rates for financial assets reclassified to loans and receivables are determined at the reclassification date. Further increases in estimates of cash flows adjust effective interest rates prospectively.

1.4.1.3 Recognition and derecognition

Purchases and sales of financial assets that require delivery are recognised on trade date, being the date on which the Group commits itself to purchasing or selling the asset. From this date, any gains or losses arising from changes in the fair value of the assets and liabilities are recognised. Financial assets are derecognised when the rights to receive cash flows from the assets have expired, or where the Group has transferred substantially all risks and rewards of ownership.

When securities classified as available-for-sale are sold, the accumulated fair value adjustments recognised in other comprehensive income are reclassified to profit or loss as gains and losses in interest income.

1.4.1.4 Measurement

Initial measurement

Financial assets are initially recognised at fair value plus transaction costs, except those carried at fair value through profit or loss. Transaction costs of financial assets carried at fair value through profit or loss are expensed in profit or loss.

The best evidence of fair value on initial recognition is the transaction price, unless fair value is evidenced by comparison with other observable current market transactions in the same instrument or based on discounted cash-flow models and option-pricing valuation techniques whose variables include data from observable markets.

Subsequent measurement

Loans and receivables are subsequently carried at amortised cost using the effective interest method. The amortised cost of a financial asset is the amount at which the financial asset is measured on initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reductions for impairment of financial assets.

Available-for-sale financial assets are subsequently carried at fair value. Unrealised gains and losses arising from changes in fair value are recognised in other comprehensive income. When the financial assets are derecognised the cumulative gain or loss recognised in other comprehensive income is transferred to profit or loss as a reclassification adjustment. Interest income and dividend income received on available-for-sale financial assets are recognised in profit or loss.

Gains and losses arising from a change in the fair value (excluding changes in fair value due to foreign exchange movements as explained in note 1.6) of financial assets and liabilities designated at fair value through profit or loss are recognised in profit or loss.

1.4.1.5 Impairment of financial assets

The Group assesses whether financial assets need to be impaired at each reporting date. A financial asset is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (a loss event) and that loss event has an impact on the estimated future cash flows of the financial asset that can be estimated reliably.

Financial assets carried at amortised cost

If there is objective evidence that an impairment loss has been incurred on loans and receivables, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate of the financial asset.

Objective evidence that loans and receivables are impaired includes but is not limited to the observable data that comes to the attention of the Group about the following events:

- significant financial difficulty of the debtor;
- a breach of contract, such as default or delinquency in payment; and
- it becoming probable that the debtor will enter bankruptcy or other financial reorganisation.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.4 Financial instruments *continued*

1.4.1 Financial assets *continued*

The carrying amount of the asset is reduced and the amount of the loss is recognised in profit or loss. If a loan or receivable has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, such as improved credit rating, the previously recognised impairment loss is reversed and is recognised in profit or loss.

Financial assets classified as available-for-sale

If there is objective evidence of impairment for available-for-sale financial assets (excluding equity instruments), the cumulative loss, measured as the difference between the acquisition cost and current fair value, less any impairment loss on the financial asset previously recognised in profit or loss, is removed from other comprehensive income and recognised in profit or loss.

If, in a subsequent period, the fair value of a financial asset (excluding equity instruments classified as available-for-sale) increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss.

Any increase in fair value subsequent to an impairment loss is recognised in other comprehensive income.

Impairment losses recognised in profit or loss on equity instruments classified as available-for-sale are not subsequently reversed through profit or loss.

1.4.2 Financial liabilities

1.4.2.1 Classification

The Group classifies its financial liabilities into financial liabilities at fair value through profit or loss and financial liabilities at amortised cost.

The Group classifies a financial instrument that it issues as a financial liability in accordance with the substance of the contractual agreement. Management determines the classification of financial liabilities at initial recognition.

Financial liabilities at fair value through profit or loss

Derivatives with negative fair values and foreign deposits have been classified as financial liabilities at fair value through profit or loss.

Financial liabilities at amortised cost

The following liabilities have been classified as financial liabilities at amortised cost: notes and coin issued, South African Reserve Bank debentures, deposit accounts, amounts due to subsidiaries, the GFECRA and other liabilities.

1.4.2.2 Recognition and derecognition

The Group recognises financial liabilities when it becomes a party to the contractual provisions of the instrument.

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled, expire or are substantially modified. The difference between the carrying amount of the financial liability derecognised, and the consideration paid and payable is recognised in profit or loss.

1.4.2.3 Measurement

Initial measurement

Financial liabilities are initially recognised at fair value, generally being their issue proceeds net of transaction costs incurred, except for financial liabilities at fair value through profit or loss.

The best evidence of fair value on initial recognition is the transaction price, unless the fair value is evidenced by comparison with other observable current market transactions in the same instrument or based on discounted cash-flow models and option-pricing valuation techniques whose variables include only data from observable markets.

Subsequent measurement

Subsequent to initial recognition, financial liabilities are measured at fair value. All related, realised and unrealised gains and losses arising from changes in fair value, excluding changes in fair value due to foreign exchange movements as explained in note 1.6 are recognised in profit or loss.

Other liabilities are measured at amortised cost, which approximates fair value, and are remeasured for impairment losses, except as set out below:

- Non-interest-bearing deposit accounts and amounts due to subsidiaries are accounted for at cost, as these do not have fixed maturity dates and are repayable on demand.
- Notes and coin issued and the GFECRA are measured at cost as these liabilities do not have fixed maturity dates. The banknotes and coin in circulation represent the nominal value of all banknotes held by the public and banks, including recalled and still exchangeable banknotes from the previous series

Amortised cost is calculated using the effective interest method that discounts the estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or liability.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.4 Financial instruments *continued*

1.4.3 Effective interest method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument or, where appropriate, a shorter period to the net carrying amount of the financial asset or liability.

1.4.4 Offsetting of financial instruments

Financial assets and financial liabilities are offset, and the net amount reported in the summarised Group statement of financial position where there is a currently legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

In addition, as set out in note 5.2, financial assets and financial liabilities arising from derivatives and securities lending activities have been offset.

The fair value of all derivatives is recognised in the summarised Group statement of financial position and is only netted to the extent that a legal right of setting off exists and there is an intention to settle on a net basis.

1.5 Fair value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions (i.e. an exit price) regardless of whether that price is directly observable or estimated using another valuation technique.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

Fair values are determined according to the fair value hierarchy based on the requirements in *IFRS 13 Fair Value Measurement*. Refer to note 16 for further details.

1.5.1 Derivatives

A derivative is a financial instrument, the value of which changes in response to an underlying variable that requires little or no initial investment and is settled at a future date.

Fair values are obtained from quoted market prices (excluding transaction costs), dealer price quotations, discounted cash flow models and option-pricing models, which consider current market and contractual prices for the underlying instruments, as well as the time value of money.

1.5.2 Foreign marketable money market investments

The fair value of foreign marketable money market investments is based on quoted bid rates, excluding transaction costs.

1.5.3 Local and foreign portfolio investments including securities lending portfolio investments

The fair values of portfolio investments are valued using the quoted fair values as obtained from portfolio managers. Where these instruments are bank deposits, they are valued at nominal values plus accrued interest based on market rates. These values approximate fair values.

1.5.4 South African government bonds

Listed bonds are valued using quoted fair values at year-end as supplied by the JSE Limited.

1.5.5 Valuable art

The fair value of valuable art is determined based on the price at which an orderly transaction to sell the assets would take place between market participants at the measurement date under current market conditions.

Revaluations of valuable art shall be made every three years by an independent, reliable valuator to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. In the absence of an official fair value assessment by an independent valuator, the insured value will be used as an indicator of fair value.

If an asset's carrying amount is increased as a result of revaluation, the increase shall be recognised in other comprehensive income and accumulated in equity under the heading of other reserves. However, the increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss.

If an asset's carrying amount is decreased as a result of a revaluation, the decrease shall be recognised in profit or loss. However, the decrease shall be recognised in other comprehensive income to the extent of any credit balance existing in the revaluation reserve in respect of that asset. The decrease recognised in other comprehensive income reduces the amount accumulated in equity under the heading of other reserves.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

The revaluation reserve included in equity in respect of an item of valuable art may be transferred directly to accumulated profit when the asset is derecognised.

1.6 Foreign currency activities

Foreign currency translation

1.6.1 Functional and presentation currency

Items included in the financial statements of each of the Group entities are measured using the currency of the primary economic environment in which the Group operates (the functional currency). The summarised Group annual financial statements are presented in South African rand, which is the functional currency of the Group.

1.6.2 Foreign exchange gains and losses arising in entity accounts

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the date of the transactions.

Foreign exchange profits or losses of the SARB, insofar as they arise from changes in the value of the rand compared to other currencies, are for the account of SA government and consequently all these profits or losses are transferred to the GFECRA in terms of sections 25 to 28 of the SARB Act. Investment returns on foreign exchange reserves and interest paid on foreign loans are for the account of the SARB and are accounted for in profit or loss. Gains and losses on conversion to the functional currency are recognised in profit or loss for the subsidiaries and associate.

1.7 Property, plant and equipment

Property, plant and equipment is identifiable non-monetary assets which the Group holds for its own use and which are expected to be used for more than one year.

Property, plant and equipment is recognised when:

- it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and
- the cost of the asset can be measured reliably.

Property, plant and equipment is initially recognised at cost.

Freehold land and items under construction are subsequently carried at cost less accumulated impairment losses. Valuable art whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated impairment losses. Other items of property, plant and equipment are subsequently carried at cost less accumulated depreciation and accumulated impairment losses. Depreciation is determined separately for each significant part of an item of property, plant and equipment, and is charged so as to write off the cost of the assets (other than land, valuable art and items under construction) to their residual value over their estimated useful life, using the straight-line method. Land and valuable art have indefinite useful lives and are not depreciated. Items under construction are not used and thus not depreciated. The estimated average useful lives of the assets are as follows:

Item	Depreciation method	Average useful life
Buildings	Straight line	50
Furniture and equipment	Straight line	2 to 28
Land	Not depreciated	Indefinite
Valuable art	Not depreciated	Indefinite
Vehicles	Straight line	5 to 7
Work in progress	Not depreciated	

Work in progress consists of items under construction and is measured at cost. Work in progress is transferred to the related category of assets and depreciated accordingly when the asset is completed and available for use.

Subsequent costs are included in the carrying amount of the asset only when it is probable that future economic benefits associated with the items will flow to the Group and the cost of the item can be measured reliably. All repairs and maintenance costs are charged to profit or loss when incurred.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising from the derecognition of an item of property, plant and equipment is included in profit or loss.

The residual values and useful life of assets are reviewed at each reporting date and adjusted if appropriate.

1.8 Intangible assets

Intangible assets are identifiable non-monetary assets without physical substance which the Group holds for its own use and which are expected to be used for more than one year.

An intangible asset is recognised when:

- it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and
- the cost of the asset can be measured reliably.

Intangible assets are initially recognised at cost.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.8 Intangible assets *continued*

Research expenditure relating to gaining new technical knowledge and understanding is charged to profit or loss when incurred. An intangible asset arising from development (or from the development phase of an internal project) is recognised when:

- it is technically feasible to complete the asset so that it will be available for use or sale;
- there is an intention to complete and use or sell it;
- there is an ability to use or sell it;
- it will generate probable future economic benefits;
- there are available technical, financial and other resources to complete the development and to use or sell the asset; and
- the expenditure attributable to the asset during its development can be measured reliably.

Purchased software and the direct costs associated with the customisation and installation thereof are capitalised. Expenditure on internally-developed software is capitalised if it meets the criteria for capitalising development expenditure. Other software development expenditure is charged to profit or loss when incurred.

Amortisation is provided to write-down the intangible assets, on a straight line basis, to their residual values. The estimated average useful lives of the assets are as follows:

Item	Amortisation method	Average useful life
Computer software	Straight line	2 to 20
Work in progress	Not depreciated	

Work in progress consists of items under construction and is measured at cost. Work in progress is transferred to the related category of assets and amortised accordingly when the asset is completed and available for use.

Intangible assets are subsequently carried at cost less any accumulated amortisation and any impairment losses.

An item of intangible assets is derecognised upon disposal or when no future economic benefits are expected from use or disposal. Any gain or loss arising from the derecognition of an intangible asset is included in profit or loss.

The residual values, amortisation period and the amortisation method for intangible assets are reviewed at each reporting date and adjusted if appropriate.

1.9 Impairment of other non-financial assets

The carrying amounts of the Group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment, in which case their recoverable amount is estimated.

An impairment loss is recognised in profit or loss whenever the carrying amount of an asset exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. The discounted cash flow analysis is used to determine the fair value of the investment in subsidiary/associate and estimated future cash flows are based on management's best estimates. The assumptions used in the forecast are based on available historical information, taking management opinion and experience into consideration. Cash flow projections are approved by the subsidiary/associate's Boards and consists of cash flows from the associate and all its subsidiaries. A five-year forecasting period should be used for cash flow projections from the subsidiary/associate and where available forecasts fall short of the five-year forecasting period, nominal growth in line with inflation is assumed. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units).

Investments in subsidiaries and associate are tested for impairment when dividends are declared to the holding company.

An impairment loss is recognised in profit or loss whenever the subsidiary or associate declares dividends to the holding company and evidence is available that:

- the carrying amount of the investment in the separate financial statements of the holding company exceeds the carrying amount in the consolidated financial statements of the investee's net assets; or
- the dividend exceeds the total comprehensive income of the subsidiary or associate in the period the dividend is declared.

Non-financial assets that suffered an impairment loss are reviewed for possible reversal of the impairment at each reporting date.

A previously expensed impairment loss will be reversed if the recoverable amount increases as a result of a change in the estimates used previously to determine the recoverable amount, but not to an amount higher than the carrying amount that would have been determined had no impairment loss been recognised.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.10 Gold

Gold is held by the SARB as part of its foreign reserves. In terms of section 25 of the SARB Act, gold is initially recorded at the prevailing rates at initial recognition, including transaction costs. Subsequent to initial measurement, it is valued at the statutory price. The statutory price is the quoted price at the reporting date. Gold loans are measured at the quoted price at the reporting date. In terms of section 25 of the SARB Act, all gains and losses on gold, held by the SARB, are for the account of SA government, and transferred to the GFECRA.

1.11 Taxation

The taxation expense for the period comprises current and deferred taxation. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions, where appropriate, on the basis of amounts expected to be paid to the tax authorities.

The charge for current taxation is based on the results for the year as adjusted for items that are non-assessable or disallowed for taxation purposes. It is calculated using taxation rates that have been enacted or substantially enacted by the reporting date, and any adjustment of taxation payable for previous years.

Deferred taxation is provided using the liability method, based on temporary differences. However, deferred taxation liabilities are not recognised if they arise from the initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss. The amount of deferred taxation provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using taxation laws enacted or substantively enacted at the reporting date. Deferred taxation is charged to profit or loss, except to the extent that it relates to a transaction that is recognised in other comprehensive income or in equity. In this case, the taxation is also recognised in other comprehensive income or in equity. The effect on deferred taxation of any changes in taxation rates is recognised in profit or loss, except to the extent that it relates to items previously charged or credited directly to equity or other comprehensive income.

Deferred taxation assets are recognised for all deductible temporary differences, the carry forward of unused taxation losses and the carry forward of unused taxation credits.

Deferred taxation is provided on temporary differences arising on investments in subsidiaries and associate except for deferred taxation where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred taxation assets and liabilities are offset when there is a legally enforceable right to offset current taxation assets against current tax liabilities, and when the deferred taxation assets and liabilities relate to income taxation levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis. Refer to note 1 for the change in accounting policy.

1.12 Employee benefits

1.12.1 Pension and retirement funds

Group companies operate various pension schemes. The schemes are funded through employer and employee contributions to insurance companies or trustee-administered funds. All funds in which the Group participates are defined contribution funds, however, there is an element within the SARB retirement fund which is deemed to be defined benefit in nature. This element, as detailed in note 13.3, is treated according to the principles of a defined benefit plan.

1.12.1.1 Defined benefit plans

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors, such as age, years of service and compensation.

The expected costs of post-employment defined benefits are charged to profit or loss over the expected service life of the employees entitled to these benefits according to the projected unit credit method. Costs are actuarially assessed, and expense adjustments and past-service costs resulting from plan amendments are amortised over the expected average remaining service life of the employees.

The liability recognised in the statement of financial position in respect of defined benefit pension plans is the present value of the defined benefit obligation at the reporting date, together with adjustments for unrecognised actuarial gains or losses and past-service costs. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise. Remeasurements are not classified to profit or loss in subsequent periods. Past-service costs are recognised in profit or loss at the earlier of the following dates: (i) when the plan amendment or curtailment occurs or, (ii) when the entity recognises related restructuring costs or termination benefits.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.12 Employee benefits *continued*

1.12.1 Pension and retirement funds *continued*

1.12.1.2 Defined contribution plans

A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity or fund. The Group has no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employees' benefits relating to employee service in the current and prior periods.

For defined contribution plans, the Group pays contributions to publicly or privately administered pension plans on a mandatory, contractual or voluntary basis. The contributions are recognised as employee benefit expenses when they are due.

1.12.2 Post-employment benefits

The SARB provides post-employment medical and group life benefits to qualifying employees and retired personnel by subsidising a portion of their medical aid and group life contributions.

Entitlement to these benefits is based on employment prior to a certain date and is conditional on employees remaining in service up to retirement age. The expected costs of post-employment defined benefits are charged to profit or loss over the expected service life of the employees entitled to these benefits according to the projected unit credit method. Costs are actuarially assessed, and expense adjustments and past-service costs resulting from plan amendments are amortised over the expected average remaining service life of the employees.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise. Past-service costs are recognised immediately in profit or loss, to the extent that they relate to retired employees or past-service.

The liability is provided for in an actuarially determined provision.

1.12.3 Leave pay accrual

Employee entitlements to annual leave and long-service leave are recognised when they accrue to employees.

The leave pay accrual at the reporting date represents the present obligation to employees as a result of employees' services provided up to the reporting date. The accrual is measured as the amount that is expected to be paid as a result of the unutilised leave entitlement that has accumulated at the reporting date.

1.13 Sale and repurchase (repo) agreements

The SARB has entered into repo agreements as part of its monetary policy activities. Securities purchased under agreements to resell are recorded under accommodation to banks as loans and receivables. Securities sold under agreement to repurchase are disclosed as reverse repo agreements included in deposit accounts.

The underlying securities purchased under repo agreements are not recorded by the SARB. Likewise, underlying securities sold under repo agreements are not derecognised by the SARB.

The differences between the purchase and sale prices are treated as interest and accrued using the effective interest method.

The standing facilities are available daily on an automated basis in the form of a bilateral repo or reverse repo transactions maturing on the following business day. The respective interest rates are set at a spread of 100 basis points above or below the prevailing repo and reverse repo transactions, respectively. The SARB may change the spread from the repo rate any time at its discretion.

1.14 Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses.

Redundant and slow-moving inventories are identified and written down to their estimated economic or realisable values. Raw materials are valued at cost according to the first-in, first-out basis by subsidiaries. Some raw materials are valued at standard cost, which closely approximates actual cost on a first-in, first-out basis.

Consumables are valued at the weighted-average cost price. Maintenance spares are valued at average cost.

Finished goods and work in progress are valued at direct costs of conversion and production overheads on a first-in, first-out basis. Production overheads are included in the cost of manufactured goods, based on normal operating capacity.

Note-printing and coin-minting expenses include ordering, printing, minting, freight, insurance and handling costs. These costs are recorded as part of work in progress for the SABN and the South African Mint, and are released to profit or loss when the currency is sold to the SARB.

1.15 Cost of new currency

The SARB recognises the cost of new currency in profit or loss when the banknotes and coin are delivered, and the significant risks and rewards of ownership are transferred to the SARB.

1.16 Statement of cash flows

For the purpose of the statement of cash flows, cash and cash equivalents include all cash on hand, bank overdrafts of subsidiaries and short-term South African money market instruments. As far as the SARB is concerned, no cash and cash equivalents are shown because of the SARB's role as central bank in the creation of money.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

1.17 Provisions

Provisions are liabilities of uncertain timing or amount and are recognised when the Group has a present legal or constructive obligation as a result of past events for which it is probable that an outflow of economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are measured at management's estimate of the expenditure required to settle that obligation at the end of each reporting period, and are discounted (at a pre-taxation rate that reflects current market assessments of the time value of money and the risks specific to the liability) to present value where the effect is material. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

1.18 Total income

Interest income and interest expense are recognised on a time proportion basis, taking account of the principal outstanding and the effective interest rate over the period to maturity. Interest income and interest expense are recognised in profit or loss for all interest-bearing instruments on an accrual basis using the effective interest method. Interest income includes changes in the fair value of the SARB's financial assets. Where financial assets have been impaired, interest income continues to be recognised on the impaired value, based on the original effective interest rate. Interest income and interest expense include the amortisation of any discount or premium, or other differences between the initial carrying amount of an interest-bearing instrument and its amount at maturity calculated on an effective interest basis.

Dividends are recognised when the right to receive payment is established.

Other income arising from the provision of services to clients is recognised on the accrual basis in accordance with the substance of the relevant transaction. This consists mainly of commission on banking services.

1.19 Key accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

There were no significant changes to the Group's estimates and assumptions in the current or prior year.

1.20 Related parties

As per *IAS 24 Related Party Disclosures*, the summarised Group annual financial statements contain the disclosures necessary to draw attention to the possibility that the Group's financial position and profit or loss may have been affected by the existence of related parties and by transactions and outstanding balances with such parties.

Related parties include, but are not limited to subsidiaries, the associate, members of management who hold positions of responsibility within the Group including those charged with governance in accordance with legislation, and members of management that are responsible for the strategic direction and operational management of the Group and are entrusted with significant authority. Their remuneration may be established by statute or by another body independent of the Group. Their responsibilities however may enable them to influence the benefits of office that flow to them, their related parties or parties that they represent on the governing body.

1.21 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new ordinary shares are shown in equity as a deduction, net of taxation, from the proceeds.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

2. CASH AND CASH EQUIVALENTS

	2018 R'm	2017 R'm
Bank and cash balances	**31 274**	22 041
Short-term South African money market investments	**7 286**	3 635
Total cash and cash equivalents	**38 560**	25 676

Financial instruments with an original maturity of less than three months are reflected above.

Included in short-term South African money market investments are repurchase agreements, the following table represents details thereof:

Fair value of repurchase agreements	**4 599**	3 563
Fair value of collateral received	**4 753**	3 562
Fair value of collateral permitted to sell or repledge at the reporting date	**4 753**	3 562
Collateral cover	**103.34%**	99.98%
Maturity date	**5 April 2018**	6 April 2017

At the reporting date, none of the collateralised advances were past due or impaired. The counterparties are exposed to interest rate risk on the various securities pledged as collateral for the repurchase agreements. The Group has the ability to sell or repledge these securities in the event of default.

3. ACCOMMODATION TO BANKS

Repurchase agreements	**56 000**	56 000
Standing facility	**10 820**	3 674
Accrued interest	**30**	11
Total accommodation to banks	**66 850**	59 685

Accommodation to banks represents short-term lending to commercial banks.

Repurchase agreements

The repurchase agreements yield interest at the repurchase rate of the SARB	**6.50%**	7.00%

The following table presents details of collateral received for repurchase agreements (including accrued interest):

Fair value of collateral received	**56 228**	56 107
Fair value of collateral permitted to sell or repledge at the reporting date	**56 228**	56 107
Collateral cover	**100.35%**	100.17%

The collateral received consists of various South African government bonds and Treasury Bills with maturities ranging from days to years.

At the reporting date, none of the collateralised advances were past due or impaired. During the year under review, no defaults were experienced (2017: no defaults).

The counterparties are exposed to interest rate risk on the various securities pledged as collateral for the repurchase agreements. The SARB has the ability to sell or repledge these securities in the event of default.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

3. ACCOMMODATION TO BANKS *continued*

	2018 R'm	2017 R'm
Standing facility		
The standing facilities yield interest at the repurchase rate of the SARB less 1%	**5.50%**	6.00%

The following table presents details of collateral received for the standing facility (including accrued interest):

Fair value of collateral received	**21 664**	3 674
Fair value of collateral permitted to sell or repledge at the reporting date	**21 664**	3 674
Collateral cover	**200.22%**	100.00%

The collateral received consists of various South African government bonds and Treasury Bills with maturities ranging from days to years.

At the reporting date, none of the collateralised advances were past due or impaired. During the year under review, no defaults were experienced (2017: no defaults).

The counterparties are exposed to interest rate risk on the various securities pledged as collateral for the standing facility. The SARB has the ability to sell or repledge these securities in the event of default.

4. INVESTMENTS

Short-term South African money market investments	**5 833**	3 735
Maturity structure of financial assets		
Between 1 and 12 months	**5 833**	3 735

For investments that meet the definition of financial assets designated at fair value:

Maximum exposure to credit risk	**5 833**	3 735

In terms of investment guidelines, approved by the Boards of the respective subsidiaries, all investments are placed with reputable financial institutions. The CPD utilises banking institutions with a minimum credit rating of BBB- by at least two of the agencies: Standard and Poor's, Fitch or Moody's. The change in fair value due to changes in credit quality or spreads is not material and has therefore not been disclosed separately.

5. GOLD AND FOREIGN EXCHANGE

Gold coin and bullion	**63 253**	66 338
Money- and capital-market instruments and deposits	**107 610**	102 583
Medium-term instruments	**333 333**	367 629
Portfolio investments	**88 401**	81 229
Accrued interest	**20**	4
Total gold and foreign exchange	**592 617**	617 783

Gold coin and bullion consists of 4 028 618 fine ounces of gold at the statutory price of R15 700.90 per ounce (2017: 4 026 987 fine ounces at R16 473.31 per ounce).

The foreign exchange balances yield investment returns achievable in the various currencies in which they are invested. It is not practicable to calculate effective yields on the portfolios due to the volatility caused by exchange rate fluctuations.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

5. GOLD AND FOREIGN EXCHANGE *continued*

Included in the gold and foreign exchange holdings are the following items provided for additional information purposes:

5.1 Derivatives held-for-trading

The SARB utilises financial derivative products for portfolio management purposes, and seeks to minimise the effects of currency and interest rate risks by using such instruments to economically hedge the related risk exposures. The use of financial derivatives is governed by the SARB's policies approved by the Governor's Executive Committee (GEC), which provides written principles on the use of derivative financial instruments. Compliance with policies and exposure limits is reviewed by management on a continuous basis. Risk management practices also include regular reporting to the Risk Management Committee (RMC) and Board Risk and Ethics Committee (BREC). The SARB does not enter into or trade financial instruments, including derivative financial instruments, for proprietary trading purposes.

	Net fair value R'm	Fair value of assets R'm	Fair value of liabilities R'm	Contract/ notional amount[1] R'm
2018				
Forward exchange contracts	**45**	**103**	**(58)**	**46 562**
Futures contracts	**(30)**	**17**	**(47)**	**15 920**
Interest rate swaps	**45**	**55**	**(10)**	**6 794**
Total derivatives held-for-trading	**60**	**175**	**(115)**	**69 276**
2017				
Forward exchange contracts	(117)	93	(210)	22 055
Futures contracts	11	35	(24)	27 571
Interest rate swaps	(13)	12	(25)	24 382
Total derivatives held-for-trading	(119)	140	(259)	74 008

(1) The notional amount of a financial instrument is the nominal or face value that is used to calculate payments made on that instrument. The amount generally does not settle between counterparties.

5.2 Offsetting financial assets and financial liabilities relating to gold and foreign exchange

The SARB is subject to an enforceable master netting arrangement with its derivative counterparties. Under the terms of this agreement, offsetting of derivatives is permitted only in the event of bankruptcy or default of either party to the agreement. There is no intention to settle on a net basis or realise the asset and settle the liability simultaneously. The following table presents details of this:

	Gross amounts presented in the derivatives held-for-trading R'm	Offset R'm	Net amounts presented in the derivatives held-for-trading R'm	Related amounts not set off in derivatives held-for-trading		
				Instruments which offset on default R'm	Collateral amount received R'm	Net amount R'm
2018						
Forward exchange contract assets	**103**	**–**	**103**	**(11)**	**–**	**92**
Interest rate swap assets	**55**	**–**	**55**	**(9)**	**–**	**46**
Forward exchange contract liabilities	**(58)**	**–**	**(58)**	**11**	**–**	**(47)**
Interest rate swap liabilities	**(10)**	**–**	**(10)**	**9**	**–**	**(1)**
2017						
Forward exchange contract assets	93	–	93	(58)	–	35
Interest rate swap assets	12	–	12	(12)	–	–
Forward exchange contract liabilities	(210)	–	(210)	58	–	(152)
Interest rate swap liabilities	(25)	–	(25)	12	–	(13)

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

5. GOLD AND FOREIGN EXCHANGE *continued*

5.3 Special Drawing Rights

The Special Drawing Rights (SDRs) asset of R25.8 billion (2017: R26.9 billion) included in gold and foreign exchange carries interest at an effective rate of 0.85% (2017: 0.40%). National Treasury promissory notes have been pledged as collateral against the SDRs.

The following table presents details of collateral held:

	2018 R'm	2017 R'm
Fair value of collateral received	**47 588**	52 652
Collateral cover	**184.78%**	195.73%

At reporting date, none of the collateralised advances were past due or impaired (2017: none). During the year under review, no defaults were experienced (2017: no defaults).

6. LOANS AND ADVANCES

Secured foreign loans	**58**	60
Interest-bearing local loans	**17 512**	27 597
Total loans and advances	**17 570**	27 657

Secured foreign loan

The loan facility of R75.0 million (2017: R75.0 million) expires on 31 December 2018 if not renegotiated and carries interest at an effective rate of 6.94% (2017: 7.00%). Land Bank promissory notes have been pledged as collateral against the foreign loan.

The following table presents details of collateral held:

Fair value of collateral received	**82**	82
Fair value of collateral permitted to sell or repledge at the reporting date	**82**	82
Collateral cover	**140.31%**	135.57%
Maturity date	**29 May 2018**	4 May 2017

At the reporting date, none of the collateralised advances were past due or impaired (2017: none). During the year under review, no defaults were experienced (2017: no defaults).

The counterparties are exposed to interest rate risk on the various securities pledged as collateral for the foreign loan. The SARB has the ability to sell or repledge these securities in the event of default.

Interest-bearing local loans

The loans are advanced as part of the national government's Inter-Governmental Cash Co-ordination (IGCC) arrangement, in terms of which some state-owned entities and treasuries of provincial governments deposit excess funds with the CPD to form a pool of funds from the public sector. The national and the provincial treasuries are allowed to borrow money from the IGCC pool of funds. National Treasury guarantees that the deposits will be made available to depositors on demand.

The interest-bearing loans are unsecured, short-term in nature and callable on demand. The loans earn interest at a rate equal to the 91-day Treasury bill yield – the rate at the reporting date was 6.99% (2017: 7.40%).

At the reporting date, none of the collateralised advances were past due or impaired (2017: none). During the year under review, no defaults were experienced (2017: no defaults).

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

7. SOUTH AFRICAN GOVERNMENT BONDS

	2018 R'm	2017 R'm
Listed bonds: Interest-bearing	**8 029**	8 094
Accrued interest	**54**	59
Total South African government bonds	**8 083**	8 153
Effective interest rate	**8.40%**	8.19%
South African government bonds pledged as collateral for reverse repurchase agreements (note 9):		
Listed bonds pledged	**–**	1 271
Associated liability	**–**	1 256

The SARB is exposed to interest rate risk on the listed South African government bonds pledged as security. South African government bonds are pledged as collateral for reverse repurchase agreements. The counterparty has the ability to sell or repledge these bonds in the event of default.

8. NOTES AND COIN IN CIRCULATION

Notes	**140 414**	126 623
Coin	**5 916**	5 674
Total notes and coin in circulation	**146 330**	132 297

The liability for notes and coin issued is the net liability after offsetting notes and coin held by the SARB and not yet issued into circulation as cash held by the central bank does not represent currency in circulation.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

9. DEPOSIT ACCOUNTS

	2018 R'm	2017 R'm
Non-interest-bearing	**132 912**	126 545
Banks' reserve accounts	**98 504**	90 972
SA government accounts	**32 991**	34 410
Other current accounts	**1 417**	1 163
Interest-bearing	**147 108**	140 276
Reverse repurchase agreements	**–**	1 256
SA government special deposit	**67 157**	67 157
Banks' current accounts	**11 644**	6 708
Call deposits	**68 307**	65 155
Total deposit accounts	**280 020**	266 821
Maturity structure of deposit accounts		
On demand	**102 715**	100 728
Subject to negotiation with National Treasury	**67 157**	67 157
Within 1 month	**110 148**	98 936
	280 020	266 821

Banks' reserve accounts

Commercial banks are required to maintain a minimum cash reserves balance with the SARB into which they are able to deposit at least such amounts as may be necessary to comply with the SARB Act. The banks' reserve accounts do not accrue interest. The commercial banks can utilise the reserve accounts to either fund short positions or deposit surplus funds. As at year-end, the balance was below the required minimum reserve balance by an amount of R35.5 million (2017: R2.0 billion).

Reverse repurchase agreements

The reverse repurchase agreements are secured by collateral as presented below:

Market value of South African government bonds	**–**	1 271
Collateral cover	**–**	101.26%

The reverse repurchase agreements bear interest at market-related rates or below the repo rate of the SARB (note 7).

SA government special deposit

SA government's special deposit bears interest at a rate equivalent to the return earned on foreign exchange investments made by the SARB. The interest earned on the deposit was settled during the year under review.

Call deposits

In terms of the current interest rate policies approved by the CPD Board, call deposits earn interest at a rate of ten basis points less than the 91-day Treasury bills yield. The prevailing rate at year-end was 6.89% (2017: 7.32%).

10. FOREIGN DEPOSITS

Foreign deposits	**101 956**	106 655

Foreign deposits are placed by customers at market related rates.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

11. SOUTH AFRICAN RESERVE BANK DEBENTURES

	2018 R'm	2017 R'm
Capital	**340**	610
Accrued interest	**0**	1
Total South African Reserve Bank debentures	**340**	611

The debentures are issued to the market on tender normally on a 7-, 14-, 28- or 56-day term. The debentures are unsecured. Details of the debentures in issue at 31 March 2018 are as follows:

Maturity date	**Interest rate %**	**Capital R'm**
4 April 2018	**6.74**	**40**
25 April 2018	**6.75**	**200**
25 April 2018	**6.71**	**100**
		340

12. GOLD AND FOREIGN EXCHANGE CONTINGENCY RESERVE ACCOUNT

	2018 R'm	2017 R'm
Opening balance	**231 158**	304 653
Loss on gold price adjustment account	**(3 114)**	(6 851)
Profit on forward exchange contract adjustment account	**6 024**	9 683
Loss on foreign exchange adjustment account	**(40 445)**	(74 215)
Movement in unrealised gains/(losses) on forward exchange contracts	**69**	(2 298)
	193 692	230 972
Payments from National Treasury	**225**	186
Closing balance	**193 917**	231 158
Balance composition		
Balance currently due to SA government	**196 652**	233 962
Unrealised gains/(losses) on forward exchange contracts	**(2 735)**	(2 804)
	193 917	231 158

The GFECRA, which is operated in terms of section 28 of the SARB Act, represents net revaluation profits and losses incurred on gold and foreign exchange transactions, which are for the account of the SA government. Settlement of this account is subject to agreement, from time to time, between the SARB and SA government and consists mainly of the exchange margin. During the reporting year under review, a net amount of R224.6 million was settled by SA government (2017: R185.9 million).

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

13. POST-EMPLOYMENT BENEFITS

The SARB and its subsidiary provide the following post-employment benefits to its employees:

	Notes	**2018 R'm**	2017 R'm
Amounts recognised in the statement of financial position			
Post-employment medical benefits	13.1	**2 704**	2 243
Post-employment group life benefits	13.2	**58**	46
Post-employment retirement fund benefits	13.3	**689**	153
Total post-employment benefits		**3 451**	2 442

13.1 Post-employment medical benefits

Post-employment medical benefits are provided to retired staff in the form of subsidised medical aid premiums. This benefit has been closed to all new employees at the SARB since 1 September 2011 and the subsidiary since 2003. A provision for the liability has been raised; this covers the total liability, that is, the accumulated post-employment medical benefit liability at 31 March 2018.

13.2 Post-employment group life benefits

Post-employment group life benefits are provided to retired staff in the form of subsidised group life premiums. This covers the total liability, that is, the accumulated post-employment group life benefit liability at 31 March 2018.

13.3 Post-employment retirement fund benefits

The Group has made provision for pension and provident plans substantially covering all employees. All employees are members of the retirement fund administered by the Group or are members of funds within the various industries in which they are employed. The assets of these plans are held in administered trust funds separate from the Group's assets and the funds are governed by the Pension Funds Act 24 of 1956.

Statutory actuarial valuations are performed tri-annually with the 31 March 2018 valuation currently being conducted. Interim actuarial valuations are concluded annually (except in years where a statutory valuation is performed). Where a surplus in the fund is calculated, it is for the benefit of the members, and accordingly no asset is recognised in the financial statements of the SARB. The retirement fund is regulated by the Financial Services Board (FSB) and is a single scheme which caters for active members, pensioners on a living annuity, pensioners on a life annuity, and pensioners from the former defined benefit fund.

Active members participate on a defined contribution basis. The market risk lies fully with the active members until retirement. On retirement, former employees can commute up to one-third of their share of funds. They may use the remaining funds to buy either a living annuity or a life annuity (or a combination of both) from the fund. They may also choose to transfer their share of funds to another registered retirement annuity. The value of assets under management for active members as at 31 March 2018 was R4.0 billion (2017: R4.1 billion).

Living annuity pensioners bear the entire market risk on their funds; however, they also fully benefit from positive market returns.

The life pension quoted by the retirement fund is based on the amount of capital available to the employee, as well as marital status, gender and age. There are currently 867 life pensioners. Once quoted a life pension, the rules of the fund stipulate that it will not be reduced, and thus, although the pensioner bears the market risk with regard to the annual increase granted, the employer will contribute if there is a shortage in the pension account which supports maintaining pensions at their existing level. This is in effect the only uncovered 'defined benefit' element in the fund. The risk for the retirement fund, and ultimately the SARB, in meeting this defined benefit, is market risk and life expectancy.

Since inception in 1995, there has not been a shortage in the pension account for any given year. The most recent interim valuation at 31 March 2017 found the fund to be fully funded, with the actuarial liability of pensions to be R1.2 billion with plan assets of R1.4 billion. The trustees of the retirement fund and the management of the SARB do not foresee a statutory liability for the SARB in terms of these pensioners.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

14. PROFIT BEFORE TAXATION

14.1 Total income includes:

	2018 R'm	2017 R'm
Income from investments	**45**	42
Dividends received	**47**	38
Realised and unrealised (losses)/profits on investments	**(2)**	4
Commission on banking services	**994**	798

Realised and unrealised profits/losses on the SARB's investments are included in interest income in terms of the SARB's accounting policies.

14.2 Operating costs include:

Directors' remuneration	**27**	26
For services as non-executive directors	**5**	5
For services as executive directors	**22**	21
Depreciation, amortisation and impairment	**480**	399
Buildings	**96**	21
Plant, vehicles, furniture and equipment	**294**	284
Computer software	**90**	94
Net loss on disposal of land, plant, vehicles, furniture and equipment	**30**	4
Write-downs of inventories	**41**	8
Auditors' remuneration	**18**	40
Audit fees	**14**	17
Fees for other services	**4**	23
Consulting fees	**127**	92
Retirement benefit costs	**716**	582
Contributions to funds – Normal	**215**	206
Contributions to funds – Additional	**75**	9
Provision for post-employment medical benefits	**279**	258
Provision for post-employment group life benefits	**6**	5
Provision for post-employment retirement fund benefits	**34**	9
Premiums paid – Medical aid	**102**	91
Premiums paid – Group life	**5**	4
Remuneration and recurring staff costs	**2 193**	1 960
Cost of new currency	**213**	179
Other operating costs[1]	**1 642**	1 720

(1) Other operating costs comprise mainly business systems and technology costs, repairs and maintenance, building maintenance costs, travel and accommodation, and training expenses.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

15. CASH GENERATED FROM OPERATING ACTIVITIES

	2018 R'm	2017 R'm
Reconciliation of profit before taxation to cash generated from operating activities		
Profit before taxation for the year	**3 244**	2 100
Adjustments for:		
Depreciation, amortisation and impairment	**480**	399
Net loss on disposal of fixed assets	**30**	4
(Profit)/loss from associate	**(424)**	556
Unrealised foreign exchange loss/(gain)	**9**	(5)
Fair value adjustments on investments	**3**	(3)
Realised gains on available-for-sale financial assets	**(1)**	–
Post-employment benefits	**226**	189
Coupon interest accrued	**5**	(1)
Amortisation of coupon interest	**(32)**	(30)
Net cash generated from operating activities	**3 540**	3 209
Changes in working capital		
Accommodation to banks	**(7 165)**	(6 175)
Other assets	**(1 086)**	(1 055)
Gold and foreign exchange	**25 166**	70 620
Loans and advances	**10 087**	(298)
South African government bonds	**390**	–
Notes and coin in circulation	**14 033**	1 735
Deposit accounts	**13 200**	(2 869)
Other liabilities	**391**	1 410
Foreign deposits	**(4 699)**	4 572
South African Reserve Bank debentures	**(271)**	(2 565)
Gold and Foreign Exchange Contingency Reserve Account	**(37 310)**	(71 197)
Cash generated from/(utilised by) changes in working capital	**12 736**	(5 822)
Cash generated from/(utilised by) operating activities	**16 276**	(2 613)

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

16. FAIR VALUE HIERARCHY DISCLOSURES

The tables on page 116 analyse the assets and liabilities of the Group carried at fair value and amortised by the level of fair value hierarchy. The fair value hierarchy depends on the extent to which quoted prices are used in determining the fair value of the specific instruments. The different levels are defined as follows:

Level 1: Fair value is based on quoted prices (unadjusted) in active markets for identical assets or liabilities. These are readily available in the market and are normally obtainable from multiple sources.

Level 2: Fair value is based on input other than quoted prices included within Level 1 that is observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Fair value is based on input for the asset or liability that is not based on observable market data (i.e. unobservable inputs).

The Group's policy is to recognise transfers into and transfers out of the fair value hierarchy levels as at the date of the event or change in circumstances that caused the transfer. During the year under review, there have been no transfers between any of the levels (2017: none).

16.1 Valuation techniques used to derive Level 1 fair values

The fair value of financial instruments traded in active markets are based on quoted market prices as obtained from the custodians at the statement of financial position date. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer broker or pricing services, and those prices represent actual and regularly occurring market transactions on an arm's-length basis. The quoted market price used for financial assets held by the SARB is the current price as per the custodian's pricing hierarchy. These instruments are included in Level 1. Instruments included in Level 1 comprise primarily fixed income investments classified as trading securities or available for sale.

16.2 Valuation techniques used to derive Level 2 fair values

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity-specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in Level 2.

Specific valuation techniques used to value financial instruments include the following:

- quoted market prices or dealer quotes for similar instruments are used for gold and foreign exchange and investments;
- the fair value of interest rate swaps is calculated as the present value of the estimated future cash flows based on observable yield curves;
- the fair value of forward exchange contracts is determined using forward exchange rates at the statement of financial position date, with the resulting value discounted back to present value; and
- the fair value of all other instruments are derived with reference to yields.

16.3 Valuation techniques used to derive Level 3 fair values

Immaterial Level 3 items are detailed in the Group annual financial statements and have been excluded from this report.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

16. FAIR VALUE HIERARCHY DISCLOSURES *continued*

	Level 1 R'm	Level 2 R'm	Level 3 R'm	Total R'm
2018				
Items measured at fair value				
Financial assets				
South African government bonds	**8 083**	**–**	**–**	**8 083**
Investments	**–**	**5 833**	**–**	**5 833**
Gold and foreign exchange	**316 801**	**275 816**	**–**	**592 617**
Gold coin and bullion	**63 253**	**–**	**–**	**63 253**
Money- and capital-market instruments and deposits	**–**	**107 630**	**–**	**107 630**
Medium-term investments	**213 434**	**119 899**	**–**	**333 333**
Portfolio investments	**40 114**	**48 287**	**–**	**88 401**
Items measured at amortised cost				
Financial assets				
Cash and cash equivalents	**31 274**	**7 286**	**–**	**38 560**
Accommodation to banks	**–**	**66 850**	**–**	**66 850**
Loans and advances	**–**	**17 570**	**–**	**17 570**
Financial liabilities				
Notes and coin in circulation	**–**	**146 330**	**–**	**146 330**
Deposit accounts	**–**	**280 020**	**–**	**280 020**
Foreign deposits	**–**	**101 956**	**–**	**101 956**
South African Reserve Bank debentures	**–**	**340**	**–**	**340**
Gold and Foreign Exchange Contingency Reserve Account	**–**	**193 917**	**–**	**193 917**
2017				
Items measured at fair value				
Financial assets				
South African government bonds	8 153	–	–	8 153
Investments	–	3 735	–	3 735
Gold and foreign exchange	424 746	193 037	–	617 783
Gold coin and bullion	66 338	–	–	66 338
Money- and capital-market instruments and deposits	–	102 587	–	102 587
Medium-term investments	345 396	22 232	–	367 628
Portfolio investments	13 012	68 218	–	81 230
Items measured at amortised cost				
Financial assets				
Cash and cash equivalents	22 040	3 636	–	25 676
Accommodation to banks	–	59 685	–	59 685
Loans and advances	–	27 657	–	27 657
Financial liabilities				
Notes and coin in circulation	–	132 297	–	132 297
Deposit accounts	–	266 821	–	266 821
Foreign deposits	–	106 655	–	106 655
South African Reserve Bank debentures	–	611	–	611
Gold and Foreign Exchange Contingency Reserve Account	–	231 158	–	231 158

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

17. COMMITMENTS AND GUARANTEES

17.1 Guarantees

R3.0 billion (2017: R3.0 billion) has been guaranteed by the SARB to ABL undertaking to settle unrecoverable loans that the Residual Debt Services Limited could not settle i.t.o the indemnity agreement. By 31 March 2018 this facility had not been utilised.

In turn, R3.0 billion (2017: R3.0 billion) has been guaranteed by the National Treasury to the SARB with the same terms to assist with the above mentioned guarantee issued to ABL. A guarantee fee of 30 basis points is payable upon the utilisation of the guarantee facility. By 31 March 2018 this facility had not been utilised.

17.2 Committed liquidity facilities

The committed liquidity facilities (CLFs) are designed to allow local banks to meet Basel III rules that require financial institutions to hold high-quality liquid assets as a buffer during times of market stress. Subsequently, the SARB has approved the provision of a CLF available to banks to assist banks to meet the liquidity coverage ratio (LCR).

Although banks can contractually draw down on the CLF with immediate effect, such a draw down would signal a degree of liquidity pressure and banks are not expected to draw down except in circumstances of extraordinary liquidity needs. The SARB monitors the liquidity positions of all banks as part of its normal supervisory processes and should be aware of any deterioration in a bank's liquidity position that could possibly result in a draw down on the CLF.

On 31 March 2018 the total CLFs granted by the SARB for the period 1 January 2018 to 31 December 2018 amounted to R133.0 billion (2017: R89.6 billion), which have not yet been utilised. Commitment fees of R771.3 million (2017: R520.0 million) have been received for the period of 1 January 2018 to 31 December 2018 of which R192.8 million (2017: R130.0 million) is accounted for as income for the year ended 31 March 2018. The balance is reflected in other liabilities.

An interest rate of repo plus 1% is charged on draw down for the draw down period of up to 30 days.

The available facility is limited to the lower of the facilities entered into and the available collateral after the haircut is applied. To date, residential, commercial mortgages, auto loans and asset backed securities to the value of R143.8 billion (2017: R89.6 billion) (before the haircut is applied) have been ceded to the SARB as collateral as per the individual agreements. A haircut is applied to the collateral registered with the SARB as per the contractual agreement, based on the risk associated with each class of asset registered as collateral.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

18. RELATED PARTY INFORMATION

18.1 Investment in subsidiaries

	Number of shares 'm	% held	2018 R'm	2017 R'm
Corporation for Public Deposits[1]	2	100	**2**	2
South African Bank Note Company (RF) Proprietary Limited	61	100	**803**	803
Share capital	61	100	**61**	61
Subordinated loan	–	–	**742**	742
South African Mint Company (RF) Proprietary Limited	60	100	**206**	206
Total investment in subsidiaries			**1 011**	1 011

(1) The SARB provides key personnel services to the CPD.

The subordinated loan to the SABN of R0.7 billion (2017: R0.7 billion) bears no interest and has no fixed terms of repayment. No repayments were made during the year (2017: R0.3 billion). The SARB may demand repayment of the loan provided the subsidiary's assets exceed its liabilities. When recalled, the subsidiary has the option to convert the loan to share capital. The loan is included in the books of the subsidiary as a separate category of equity and is thus treated as an addition to the SARB's investment in subsidiary.

The contribution to the Group profit or loss attributable to the parent (pre elimination of intercompany transactions) is as follows:

Corporation for Public Deposits			**91**	74
South African Bank Note Company (RF) Proprietary Limited			**(6)**	130
South African Mint Company (RF) Proprietary Limited			**421**	299
Total contribution to Group profit or loss			**506**	503

18.2 Investment in associate

African Bank Holdings Limited (Carrying value)	500	50	**4 446**	5 002
Profit/(loss) attributable to Group profit			**424**	(556)
Carrying value of investment in associate			**4 870**	4 446

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

18. RELATED PARTY INFORMATION *continued*

18.3 Transactions with non-controlling interests

Prestige Bullion

The South African Mint holds a 60% interest in Prestige Bullion. Prestige Bullion distributes, and sells bullion Krugerrand coins to local and international markets. The South African Mint is responsible for the manufacturing while the marketing and distribution of the coins is done by Rand Refinery.

Rand Refinery has a 40% interest, and therefore holds a non-controlling interest in Prestige Bullion.

	2018 R'm	2017 R'm
Profit attributable to non-controlling interest	**264**	181
Accumulated non-controlling interest at year-end	**64**	51
Dividends paid to non-controlling interest	**251**	210

No significant restrictions exist on the SARB's ability to access or use the assets and settle the liabilities of the Group.

18.4 Amounts due by/to related parties

Amounts due by related parties		
Corporation for Public Deposits	**–**	3
South African Bank Note Company (RF) Proprietary Limited	**9**	–
SA government	**17 512**	27 597
South African Mint Company (RF) Proprietary Limited	**25**	–
Amounts due to related parties		
African Bank Limited (equity accounted, not consolidated)	**–**	388
Corporation for Public Deposits	**7 536**	8 761
SA government	**362 358**	397 881
GEFCRA	**193 917**	231 158
Deposits		
Corporation for Public Deposits	**68 366**	65 229
Non-interest-bearing	**32 918**	34 337
Interest-bearing	**67 157**	67 157

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

18. RELATED PARTY INFORMATION *continued*

18.5 Transactions between the SARB and its related parties

	2018 R'm	2017 R'm
Dividends received		
South African Mint Company (RF) Proprietary Limited	**150**	150
Interest received	**3 166**	3 789
African Bank Limited	**1**	77
SA government	**3 165**	3 712
Interest paid	**6 108**	6 541
African Bank Limited	**–**	5
Corporation for Public Deposits	**939**	736
SA government	**5 169**	5 800
Rent paid		
South African Bank Note Company (RF) Proprietary Limited	**3**	3
Coin management fees paid		
South African Mint Company (RF) Proprietary Limited	**3**	3
Management fees received	**7**	6
Corporation for Public Deposits	**3**	3
South African Reserve Bank Retirement Fund	**4**	3
Cost of new currency	**793**	1 415
South African Bank Note Company (RF) Proprietary Limited	**537**	945
South African Mint Company (RF) Proprietary Limited	**256**	470
Pension fund contributions		
South African Reserve Bank Retirement Fund	**261**	157
Administrative services	**4**	3
South African Bank Note Company (RF) Proprietary Limited	**1**	2
South African Mint Company (RF) Proprietary Limited	**3**	1
Recovery of foreign exchange gains		
South African Bank Note Company (RF) Proprietary Limited	**36**	49
Charges (other income)		
African Bank Limited	**–**	1

All other significant balances are shown in the statement of financial position under the appropriate headings.

18.6 Inventory held on behalf of the SARB by the South African Mint

At year-end, coin inventory to the value of R291.0 million (2017: R391.0 million) was held on behalf of the SARB.

NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 March 2018

19. EVENTS AFTER REPORTING DATE

The PA (as part of the Twin Peaks model of the financial sector regulation) was officially established as a juristic person operating within the administration of the SARB (as a division) on 1 April 2018. The PA is responsible for regulating banks, insurers, cooperative financial institutions, financial conglomerates and certain market infrastructures. The PA's objective will be to promote and enhance the safety and soundness of regulated financial institutions.

Certain staff from the Financial Services Board were moved across to the SARB effective 1 January 2018. The PA is fully operational and has its own budget. It will collect fees in the form of applications (effective 1 April 2018) and levies (effective 2019). While preparation and planning occurred during the financial year ended 31 March 2018, the full financial effect of this division will therefore only commence in the new financial year, with the costs attributed to the PA only to be fully recovered from the 2019/20 financial year onwards.

No other material events occurred between 31 March 2018 and the date of signing this report requiring disclosure in, or adjustment to, the financial statements for the year ended 31 March 2018.

APPENDIX TO THE NOTES TO THE SUMMARISED GROUP ANNUAL FINANCIAL STATEMENTS

DIRECTORS' REMUNERATION

	2018 R'000	2017 R'000
Paid by SARB		
Executive directors: Remuneration		
Governor E L Kganyago		
Remuneration and recurring fringe benefits	**6 994**	6 577
Other fringe benefits	**85**	227
	7 079	6 804
Deputy governor A D Mminele		
Remuneration and recurring fringe benefits	**5 036**	4 736
Other fringe benefits	**129**	216
	5 165	4 952
Deputy governor F E Groepe		
Remuneration and recurring fringe benefits	**5 036**	4 736
Other fringe benefits	**107**	158
	5 143	4 894
Deputy governor K Naidoo		
Remuneration and recurring fringe benefits	**4 998**	4 702
Other fringe benefits	**2**	–
	5 000	4 702
Total remuneration of executive directors	**22 387**	21 352
Non-executive directors: Remuneration for services		
B W Smit	**421**	353
C B du Toit (appointed 30 July 2016)	**421**	220
F Cachalia	**560**	444
G M Ralfe	**520**	425
J F van der Merwe (term ended 30 July 2016)	**–**	184
J V Klein	**487**	380
M M Manyama (resigned 28 July 2017)	**137**	325
N Vink (appointed 30 July 2016)	**389**	220
R J G Barrow	**571**	449
R le Roux	**407**	356
T Ajam (term ended 5 October 2017)	**227**	353
T N Mgoduso (term ended 30 July 2016)	**–**	170
T Nombembe	**474**	363
	4 614	4 242
Paid by subsidiaries		
Non-executive directors: Remuneration for services		
R J G Barrow	**552**	451
Total remuneration of non-executive directors	**5 166**	4 693
Total remuneration of directors	**27 553**	26 045

MINUTES OF THE 97TH ANNUAL ORDINARY GENERAL MEETING OF SHAREHOLDERS OF THE SARB

The ninety-seventh annual Ordinary General Meeting (AGM) of shareholders was held at the head office of the South African Reserve Bank (the SARB) in Pretoria on Friday, 28 July 2017 at 10:00.

The Chairperson, Governor Lesetja Kganyago, extended a warm welcome to all present and declared the meeting duly constituted in terms of the regulations framed under the South African Reserve Bank Act 90 of 1989, as amended (the SARB Act).

The Chairperson introduced Deputy Governors Daniel Mminele, Francois Groepe and Kuben Naidoo; Chairperson of the Audit Committee, Mr Rob Barrow; Chairperson of the Remuneration Committee, Ms Venete Klein; Chairperson of the Board Risk and Ethics Committee, Prof. Firoz Cachalia; Chairperson of the Non-executive Directors' Committee Mr Gary Ralfe; the SARB's General Counsel, Dr Johann de Jager; and the Secretary of the Bank, Ms Sheenagh Reynolds, who shared the podium with him.

The Chairperson then addressed the meeting; his full address is attached hereto for record purposes and marked Annexure A.

The Chairperson then turned to the formal business of the day and confirmed the agenda for the meeting as follows:

- To receive, discuss and note the minutes of the AGM held on 29 July 2016.
- To receive and discuss the financial statements for the financial year ended 31 March 2017, including the directors' report and independent external auditors' report.
- To approve the remuneration of the SARB's independent external auditors, PricewaterhouseCoopers Inc. and SizweNtsalubaGobodo Inc. (in terms of regulation 22.1(b), read with regulation 7.3(c) of the Regulations), for completing the audit for the 2016/17 financial year.
- To approve the appointment of PricewaterhouseCoopers Inc. and SizweNtsalubaGobodo Inc. as the SARB's independent external auditors for the 2017/18 financial year.
- To elect three non-executive directors to serve on the SARB's Board of Directors (Board).
- To consider any further business arising from the above items (in terms of regulation 7.3(e) of the Regulations).

The Chairperson confirmed that the Office of the Secretary of the Bank had not received any requests for special business to be placed on the agenda of this meeting. A shareholder, Mr Adrian Fondse, interjected and stated that the items which he had submitted for inclusion in the agenda of this meeting had not been included.

The Chairperson advised that the meeting would proceed according to the agenda items outlined and that any other matters of interest to the shareholders would be addressed after the formal business of the meeting had been transacted. At that stage, the General Counsel would be afforded an opportunity to respond to Mr Fondse's enquiry.

Ms Reynolds, the Secretary of the Bank confirmed the shareholder representation at this meeting as follows:

1. the total number of shares in the issued share capital of the SARB held by its shareholders was 2 000 000 (two million);
2. 17 shareholders were present in person;
3. 11 shareholders were represented by proxy; and
4. 574 votes were exercisable by shareholders present or holding duly certified proxy forms for this purpose.

Shareholders were advised that, as was the practice, the SARB would make use of electronic voting at this meeting, which would be facilitated by Lumi Technologies SA (Pty) Limited (Lumi).

The Chairperson called for a poll on each of the items to be considered at the AGM.

ACCEPTANCE OF THE MINUTES OF THE 2016 AGM

The Chairperson proposed that the minutes of the ninety-sixth AGM held on 29 July 2016, which had been distributed as part of the *Annual Report 2016/17,* be taken as read.

There were no objections to the minutes. On the basis of the results of the poll, the Chairperson declared that the minutes of the 2016 AGM had been accepted by 99.76% of the votes cast.

ACCEPTANCE OF THE ANNUAL FINANCIAL STATEMENTS FOR THE FINANCIAL YEAR ENDED 31 MARCH 2017, INCLUDING THE DIRECTORS' REPORT AND INDEPENDENT EXTERNAL AUDITORS' REPORT

The Chairperson formally moved that the annual financial statements for the year ended 31 March 2017, including the directors' report and the independent external auditors' report, which had been posted to shareholders on 26 June 2017, be accepted. The meeting was informed that the Annual Report 2016/17 contained the summarised Group annual financial statements. The full set of the 2016/17 annual financial statements had been made available on the SARB's website.

MINUTES OF THE 97TH ANNUAL ORDINARY GENERAL MEETING OF SHAREHOLDERS OF THE SARB *continued*

On the basis of the results of the poll, the Chairperson declared that the audited financial statements for the year ended 31 March 2017 had been accepted by 90.26% of the votes cast.

REMUNERATION OF THE SARB'S INDEPENDENT EXTERNAL AUDITORS

The Chairperson moved that the remuneration for the SARB's independent external auditors in respect of the general audit of the SARB for the financial year ended 31 March 2017, be confirmed and approved.

On the basis of the results of the poll, the Chairperson declared that the remuneration of the SARB's independent external auditors amounting to R11 791 448,00 (excluding VAT) for the general audit for the financial year ended 31 March 2017 had been approved by 90.1% of the votes cast.

APPOINTMENT OF INDEPENDENT EXTERNAL AUDITORS

The Chairperson turned to the appointment of the SARB's independent external auditors for the 2017/18 financial year.

It was reported that the Board had recommended that PricewaterhouseCoopers Inc. and SizweNtsalubaGobodo Inc. be reappointed as the SARB's independent external auditors for the 2017/18 financial year.

The Chairperson confirmed that the lead audit partners of both firms rotate every five years, which was in line with best practice.

The Chairperson moved that PricewaterhouseCoopers Inc. and SizweNtsalubaGobodo Inc. be appointed as the SARB's independent external auditors for the 2017/18 financial year.

Following the above, the shareholders present cast their votes, and on the basis of the results of the poll, the Chairperson declared that PricewaterhouseCoopers Inc. and SizweNtsalubaGobodo Inc. had been reappointed as the SARB's independent external auditors for the 2017/18 financial year by 89.31% of the votes cast. The auditors were congratulated on their reappointment.

ELECTION OF THREE NON-EXECUTIVE DIRECTORS

The Chairperson turned to the election of non-executive directors. He advised the meeting that there were three vacancies for shareholder-elected non-executive directors for persons with knowledge and skills in commerce or finance, mining and labour, respectively.

Messrs Rob Barrow and Gary Ralfe, and Prof. Rochelle le Roux's terms of office would be expiring the day after the AGM, being 29 July 2017, but all were available for re-election for another term of three years.

All the candidates to be considered for these positions had been confirmed by the Panel appointed in terms of section 4(1C) of the SARB Act. This Panel comprised the Governor, as well as retired Constitutional Court Judge, Ms Yvonne Mokgoro, and Mr Abel Sithole (both nominated by the Minister of Finance) and Mr Kaizer Moyane, Mr Dumisani Mthalane and Mr Bheki Ntshalintshali (all nominated by Nedlac).

The Panel had confirmed seven candidates in terms of section 4(1G) of the SARB Act for consideration for the three vacancies and was satisfied that all seven candidates were eligible, and fit and proper to stand for election as directors of the SARB. The curricula vitae for these seven candidates had been sent to shareholders together with the notice of this meeting.

Mr Rob Barrow and Mrs Simone Le Hane had been selected as candidates to stand for the position of non-executive director with knowledge and skills in commerce or finance.

The results of the poll showed that 71.78% of the votes were cast in favour of Mr Barrow and 18.64% in favour of Mrs Le Hane, 9.58% abstained from voting.

On the basis of the voting results, the Chairperson declared that Mr Rob Barrow had been re-elected as the non-executive director with knowledge and skills in commerce or finance. Mr Barrow's reappointment would be effective from 29 July 2017 until the day after the AGM in 2020.

The Chairperson congratulated Mr Barrow on his re-election and thanked him for his dedicated and valuable service as a director over his six-year term of office.

The Chairperson turned to the election of a non-executive director to fill the second vacancy for a person with knowledge and skills in mining. Messrs Gary Ralfe and Nape Mojapelo and Ms Lerato Molebatsi had been selected as candidates to stand for the aforesaid position.

The results of the poll showed that 52.09% of the votes were cast in favour of Mr Ralfe, 18.51% in favour of Mr Mojapelo and 19.34% in favour of Ms Molebatsi, 9.06% abstained from voting.

On the basis of the voting results, the Chairperson declared that Mr Gary Ralfe had been re-elected as the non-executive director with knowledge and skills in mining. Mr Ralfe's reappointment would be effective from 29 July 2017 until the day after the AGM in 2020.

The Chairperson congratulated Mr Ralfe on his re-election and thanked him for his dedicated and valuable service as a director over his six-year term of office.

The Chairperson then turned to the election of a non-executive director to fill the vacancy for a person with knowledge and skills in labour. Prof. Rochelle le Roux and Mr Fezile Dantile were available for election to fill this position.

MINUTES OF THE 97TH ANNUAL ORDINARY GENERAL MEETING OF SHAREHOLDERS OF THE SARB *continued*

The results of the poll showed that 90.24% of the votes were cast in favour of Prof. Le Roux and 1.05% in favour of Mr Dantile, 8.71 % abstained from voting.

On the basis of the voting results, the Chairperson declared that Prof. Rochelle le Roux had been re-elected as the non-executive director with knowledge and skills in labour. Prof. Le Roux's reappointment would be effective from 29 July 2017 until the day after the AGM in 2020.

The Chairperson congratulated Prof. Le Roux on her re-election and thanked her for her dedicated and valuable service as a director over her six-year term of office.

The Chairperson thanked all the candidates for being willing to stand for election to the Board and hoped that, whether successful or not, they would continue to take a keen interest in the work of the SARB.

SPECIAL BUSINESS TO BE CONSIDERED AT THE AGM

The Chairperson reiterated his earlier statement that the Office of the Secretary of the Bank had received no requests for special business to be placed on the agenda of this meeting.

In the absence of questions arising from the matters under consideration at this meeting, the Chairperson stated that for the benefit of the shareholders present, he would call upon the SARB's General Counsel, Dr De Jager, to respond in respect of the items which Mr Fondse had requested to be placed on the agenda of this meeting. The Chairperson asserted that the items proposed by Mr Fondse did not qualify as special business for consideration at the AGM and extended beyond the remit of the SARB's shareholders.

Dr de Jager first clarified the business of the AGM in terms of the SARB Act. He confirmed that the business of the AGM was to receive and discuss the minutes of the previous meeting, the financial statements for the preceding financial year, the report of the Board on the state of affairs and business of the SARB, the external auditors report, to attend to the election of directors, and to attend to the appointment of auditors and the approval of their remuneration (this being referred to as the ordinary business of a general meeting).

In addition, special business, of which proper notice had been given, may be transacted at the general meeting. Such special business would include resolutions proposed by shareholders and which relate to the ordinary business of a general meeting. He emphasised that special business did not constitute any business which shareholders wished to raise relating to the SARB and/or criticism of reports or documents presented at the general meeting. It must clearly relate to the ordinary business of a general meeting referred to above and must, more particularly, be framed as a resolution which was capable of being implemented, if adopted.

Dr de Jager shared with the shareholders feedback of his various engagements, either conducted in writing or in person, with Mr Fondse over a number of years. He mentioned that in the previous year, Mr Fondse had sought to place 15 issues on the agenda of the 2016 AGM. As these issued did not relate to the ordinary business of a general meeting as referred to above, they did not constitute special business. At the time, Dr de Jager had engaged Mr Fondse on various occasions in order to explain that these items were not related to the ordinary business of a general meeting. He then outlined those items in question to the meeting. Dr de Jager cited that Mr Fondse had again written to him insisting that his 15 items be placed on the agenda of the 2017 AGM, for discussion. Mr Fondse had again been advised in writing and verbally prior to the 2017 AGM that these items could not be placed on the agenda as they did not constitute special business.

Following the above, the Chairperson informed the meeting that the SARB had received a letter from a SARB shareholder, Mr Stephen Goodson, regarding the SARB's price and financial stability mandates, which he found appropriate to address at this meeting. He emphasised that these issues did not constitute special business, but responding to them was for the benefit of all shareholders present. In brief, Mr Goodson had asked whether it would be appropriate for the SARB to adopt the 1933 Chicago Plan introduced by Mr Irving Fischer, who had advocated that the state should create the nation's money supply and that private banks should operate as full reserve banks. Mr Fisher had argued that this would generate full employment, business cycles would no longer occur and inflation would be reduced and remain at zero.

The Chairperson stated that, as indicated by the question, this issue was not new and it was a highly contentious topic. Furthermore, it had spawned a relatively large body of literature, including numerous critiques of the plan and its more modern variants. Apart from the substantial transitional costs and economic disruptions, opponents of the plan showed that eliminating fractional reserve banking was unlikely to be beneficial, either in terms of price or financial stability. There would still be the creation of money under some sort of rule, and the degree of inflation would be closely related to this rule, as was the current practise.

He further explained that financial innovation was ongoing. Instead of a single, top-down revolutionary change, however, disruption was likely to come from many sources and take many different forms. For instance, the SARB had been actively involved in blockchain technology research. Similarly, the Bank of England had researched granting private access to its balance sheet via digital currency. The new peer-to-peer lenders connect savers directly with borrowers, breaking down chains of intermediation that had traditionally been the preserve of banks. No doubt, these and other innovations would transform financial sectors everywhere during the coming years.

MINUTES OF THE 97TH ANNUAL ORDINARY GENERAL MEETING OF SHAREHOLDERS OF THE SARB *continued*

In conclusion, the Chairperson stated that the SARB was always interested in discussing macroeconomics and economic innovations, but that this AGM was not the appropriate forum for such a discussion. The SARB would engage with Mr Goodson separately on this topic.

The Chairperson thanked President Zuma and the Presidency, the Government and Parliament for their continued support. The sound working relationship between the SARB and National Treasury had continued. He thanked the Minister of Finance, Malusi Gigaba, and his predecessor, Pravin Gordhan, Deputy Minister of Finance, Sfiso Buthelezi, and his predecessor, Mcebisi Jonas; the recently appointed Director General, Dondo Mogajane, and his predecessor, Lungisa Fuzile, and the staff of National Treasury for their ongoing support of the SARB.

Sincere thanks were also expressed to the members of the Board for their continued contributions and support, and for ensuring proper corporate governance in the SARB.

The Chairperson advised that a government-appointed non-executive director, Ms Maureen Manyama, had tendered her resignation from the SARB Board with effect from 29 July 2017, due to a conflict of interest which had arisen owing to her new place of employment. On behalf of the SARB, he thanked Ms Manyama for her contribution over the past six years on the Board and wished her all the best for her future endeavours.

Sincere appreciation was also expressed to Deputy Governors Mminele, Groepe and Naidoo as well as to the entire management and staff of the SARB for their continued dedication and commitment during what was once again a challenging year. He thanked them for their contributions in sharing the load and stated that he was confident that their efforts would ensure that 2017 would be even more successful.

The Chairperson then gave Mr Burger, the Chief Executive Officer of FirstRand Limited, an opportunity to propose a vote of thanks.

Mr Burger, on behalf of the shareholders and the banking industry, expressed gratitude to the Board, Governor, Deputy Governors and the staff of the SARB for the excellent work done in the 2016/17 financial year.

He stated that the sustainability and success of the banking sector was very dependent on the enabling environment created by the SARB through monetary policy and the supervision of the banking sector.

Mr Burger affirmed that the SARB had a major positive impact on global investor sentiment towards South Africa. He alluded to the fact that rarely had the integrity and stability that had come to define the SARB been more valued than in the current environment of heightened political and policy uncertainty. This appreciation had stretched beyond South Africa's border into the global investment community. Accordingly, the respect that foreign investors held for the SARB was noted at almost all meetings that the South African banking sector held with international investors.

Mr Burger went on to say that he appreciated the ongoing efforts of the SARB to communicate and protect its monetary policy framework, its integrity, independence and the soundness of the banking sector. These efforts were important for the stability of South Africa's monetary sector, especially at a time where certain elements were requesting a change of the SARB mandate, which could be ill afforded at this stage.

From a banking supervision perspective, the SARB's notable achievements and participation in the international standard-setting bodies, such as the Financial Stability Board, the Basel Committee on Banking Supervision and the Financial Action Task Force had ensured that South Africa was compliant with international standards, which were critical for access to foreign banking relationships and capital. He congratulated the SARB on the work done pertaining to the Financial Sector Regulation (FSR) Bill and the Financial Intelligence Centre Act (FICA).

Furthermore, Standard & Poor's (S&P) recent statement on the strength of the banking sector was attributable to the strength of the supervision and monitoring of the Bank Supervision Department in the Prudential Authority Cluster of the SARB.

Mr Burger concluded his vote of thanks by wishing the Governor and his team well as they journey through this challenging economic environment and asserted that the banking sector was committed to contributing positively towards the achievement of economic growth.

Following the vote of thanks by Mr Burger, the Chairperson confirmed that all business included in the agenda had been transacted.

The Chairperson then thanked the shareholders for their attendance and participation, and confirmed that the SARB would continue to count on the shareholders' support in future.

The Chairperson declared the proceedings closed.

E L Kganyago
Chairperson

ANNEXURE A: AN ADDRESS BY LESETJA KGANYAGO, GOVERNOR OF THE SOUTH AFRICAN RESERVE BANK (THE SARB)

to the ninety-seventh annual Ordinary General Meeting of the SARB shareholders held on Friday, 28 July 2017 *continued*

This past year has been extremely eventful, from both an economic and a political perspective. This has been the case both globally and domestically.

A number of themes dominated the global backdrop. First, there were major shifts in the political settings. Surprise outcomes in the UK referendum regarding its continued membership of the European Union and in the US presidential election coincided with increased concerns about the rise of political populism in a number of regions, a backlash against rising inequality blamed on globalisation, and a rise in nationalistic tendencies. The French political landscape changed dramatically, given the decimation of traditional parties, but a strong move to the extreme right did not transpire as feared.

Second, these developments threatened the sustainability of the global economic recovery which had shown signs of resilience after a few years of disappointing outcomes and false starts. But despite these uncertainties, there appear to be definite signs that most regions are on a path of sustained recovery from the most recent global economic crisis. It has taken almost 10 years to reach this point, which is indicative of how long it takes to recover from economic slowdowns following a financial crisis. Nevertheless, expectations are for a lower growth trend than in the pre-crisis period.

Third, most of the advanced economies saw a decline in unemployment rates, although they remain relatively high in the euro area on average. Despite tightening labour market conditions, wage growth in these economies has remained minimal. While some ascribe this trend in part to low productivity growth or the impact of technological change, the full explanation remains a subject of much debate. But this trend could contribute to the persistence in rising inequality and political instability.

The fourth global theme relates to inflation. Earlier concerns about deflation have abated. Inflation generally remains benign and below target in most of the advanced economies despite the improved growth outlook and lower unemployment. The volatility that was observed was driven primarily by oil price fluctuations. A notable exception is the UK where the inflation target has been exceeded following the Brexit-induced depreciation of the sterling. The subdued global inflation environment is ascribed in part to low wage growth.

Fifth, despite the absence of inflation pressures, monetary policies in the advanced economies have begun a slow retreat from their highly accommodative stances. The US Fed has led the way with three Fed Funds rate increases of 25 basis points each in the past year. The Fed has also communicated its intention to begin slowly shrinking its balance sheet – which was expanded significantly during the global financial crisis – this year. The ECB and the Bank of England have also recently signalled a possible end to their extremely accommodative monetary policy stances later this year, but rates are expected to remain low in Japan.

Sixth, capital flows to emerging markets have remained relatively robust but sensitive to changes in advanced economy policy signals. While changing expectations regarding ECB and US monetary policy in particular have impacted on a number of emerging market currencies and bond yields, the reaction has been relatively muted. Those economies that were most sensitive to the 2013 'taper tantrum' episode have much-improved macroeconomic balances, and their currencies are less vulnerable to possible spill-over effects from US monetary tightening.

Finally, international oil prices have also been fairly volatile. Attempts by OPEC and other producers to underpin falling prices through output restrictions were effective in the short run, with oil prices rising to around US$58 per barrel in December 2016 from earlier levels of around US$45-50, after they had fallen to below US$30 per barrel in early 2016. Since April we have seen this strategy being undermined by increased output from shale gas producers in the US in particular, and by non-compliance by parties to the agreement.

Turning closer to home: while global growth prospects have generally improved, South Africa is unfortunately an outlier. This past year has seen the worst domestic growth performance since the recession during the global financial crisis. The economy grew at a paltry 0.3% in 2016, and recently recorded two consecutive quarters of negative growth. The SARB had expected the fourth quarter of 2016 to be the low point in the cycle, but growth in the first quarter of this year surprised significantly on the downside at -0.7%. This contraction was broad-based, with only the primary sector recording positive growth.

Despite this, we believe that the worst is behind us – and that growth in the second quarter of this year will be positive. However, the SARB's growth forecast was revised down significantly, as communicated at the recent meeting of the MPC. Growth of just 0.5% is now forecast for this year, rising to 1.3% and 1.5% respectively in the next two years. This is clearly too low to make any meaningful inroads on unemployment.

For most of the past year, headline inflation was above the upper end of the target range of 3–6%, at an average of 6.3% and a peak of 6.8% in December. In the early months of 2017, inflation moderated considerably and returned to within the inflation target range in April.

ANNEXURE A: AN ADDRESS BY LESETJA KGANYAGO, GOVERNOR OF THE SOUTH AFRICAN RESERVE BANK (THE SARB)

to the ninety-seventh annual Ordinary General Meeting of the SARB shareholders held on Friday, 28 July 2017 *continued*

The inflation forecast presented to the MPC at its most recent meeting showed a marked improvement. While previous forecasts had suggested that the longer-term inflation trajectory would be uncomfortably close to the upper end of the target range over the forecast period, the new forecast showed a more benign path. Inflation is now expected to average 5.3% in 2017 and 4.9% and 5.2% respectively in the coming two years, with a low point of 4.6% in early 2018. The core inflation forecast is just below 5.0% for all three forecast years.

The drivers of these improved inflation outcomes over the past few months include:

- lower food price inflation, as the effects of the drought recede;
- lower international oil prices;
- lower electricity tariff increases;
- a more resilient exchange rate than had previously been expected, coupled with muted exchange rate pass-through; and
- weak domestic demand.

More recently, there have also been indications of some wage moderation.

Despite the improved outlook, the MPC is still concerned that inflation expectations remain sticky at the upper end of the target range. As indicated in our post-MPC statement, we would prefer expectations to be anchored closer to the midpoint of the range. Furthermore, we are aware that the inflation outlook can change quickly in the event of supply-side shocks. At this point, however, we view the risks to the inflation outlook to be broadly balanced.

The main risk to the inflation outlook has, for some time, been the exchange rate. During the past year, while volatile, the rand has been relatively resilient, considering the adverse shocks it has had to face. At current levels, it is still stronger than it was at this time last year. The local currency has been supported by the significant improvement of the current account of the balance of payments, favourable terms of trade, and the generally positive capital flow environment for emerging markets. The rand has been adversely affected by low growth, political and policy uncertainty, and the credit ratings downgrades. These factors, along with the possibility of advanced economy monetary tightening, continue to weigh on the rand.

For much of the past year, monetary policy has had to deal with the increasingly difficult scenario of accelerating inflation in the context of slowing domestic economic growth. With inflation expectations anchored at levels of around 6.0%, the monetary policy challenges were significant. Furthermore, most of the pressures on inflation emanated from the supply side, in particular food prices, and were not driven by excess demand.

Faced with this policy dilemma, the MPC accommodated the temporary breach of the upper end of the inflation target band and maintained an unchanged monetary policy stance since the 25 basis point increase of the repo rate to 7.0% in March 2016. In both March and May of this year, as the inflation outlook improved, the MPC indicated that the tightening cycle was likely to have ended but that a further improvement in the inflation outlook would be required before the policy rate could be reduced. At its most recent meeting, following the improved inflation forecast and deteriorating growth outlook, the MPC reduced the repo rate by 25 basis points, to 6.75% per annum. The MPC also noted that future policy decisions would be dependent on data outcomes and the assessment of the balance of risks. The MPC will remain vigilant and will not hesitate to reverse this decision should the inflation outlook and risks deteriorate.

The most recent global financial crisis saw increased financial stability responsibilities being given to central banks around the world. Although the SARB has had a role in ensuring financial stability for some time, our responsibilities in this area have expanded. The SARB's role in maintaining, promoting, and enhancing financial stability is formally mandated in the Financial Sector Regulation Bill (FSR Bill). Unfortunately, the parliamentary processes to promulgate the FSR Bill took longer than expected. This has delayed the establishment of the proposed Prudential Authority, which will expand the SARB's regulatory responsibilities in the financial sector. I am, however, pleased to be able to report that the FSR Bill has now been passed, and is awaiting the signature of the President. Implementation planning is nonetheless well advanced.

The delay in the promulgation of the FSR Bill has not detracted from our focus on those areas of responsibility that we currently have, both at macroprudential and at microprudential levels. As I alluded to earlier, the recovery in the advanced economies from the global financial crisis has taken 10 years and is still not completely assured. This underlines the importance of financial crisis prevention. We therefore need to ensure the stability of the banking sector through appropriate regulation and supervision, and to monitor the broader economy for excesses that could undermine financial stability.

As you are all no doubt aware, the SARB has been in the spotlight for the past few weeks, mainly for the wrong reasons. It is appropriate for me to make a few brief comments about some of these issues. The first relates to the remedial instruction by the Public Protector to Parliament to set in motion a process to change the constitutional mandate of the SARB. We have challenged this remedial action in the High Court on a number of grounds, and the matter will be heard in court next week, even though the Public Protector has chosen not to oppose our submissions. Apart from the issue of whether the Public Protector has overstepped her legal powers in this regard, or the issue that the remedial actions proposed were

ANNEXURE A: AN ADDRESS BY LESETJA KGANYAGO, GOVERNOR OF THE SOUTH AFRICAN RESERVE BANK (THE SARB)

to the ninety-seventh annual Ordinary General Meeting of the SARB shareholders held on Friday, 28 July 2017 *continued*

unrelated to the original complaint under investigation, these developments have opened the door to a debate about the appropriateness of our mandate and of the inflation-targeting mandate specifically.

Price stability, or the protection of the value of the currency, is a core function of central banks. I know of no central bank that does not have this mandate. These institutions are best equipped to carry out this function, and stripping them of this mandate would raise the question as to where the responsibility for price stability should lie. Our Constitution is very clear: this is, correctly, a SARB function, and we should protect the value of the currency in the interest of balanced and sustainable growth in the South African economy.

There is no virtue to high inflation, which ravages the incomes and savings of the poor in particular, but which has also wiped out the savings of the middle classes in a number of countries. We need not look further than our northern border to see the impact. The wealthy are more able to protect themselves through various hedging mechanisms, and in this respect inflation has a negative distributive effect. Low inflation, by contrast, protects the purchasing power of incomes and social pensions and savings, and provides a more conducive environment for investment and job creation by reducing uncertainty about future prices.

Any mandate given to a central bank should focus on what it can do and not on what we would like it to do. A socio-economic objective such as protecting the buying power of the money in the pockets of South African citizens is an important and attainable objective, and in the area of our core competency.

Apart from this objective, we also:

- ensure the availability of good-quality banknotes and coin;
- ensure the effective functioning of the national payment system;
- prudently manage the official gold and foreign-exchange reserves of the country;
- strive for a stable financial system; and
- regulate and supervise the banking system.

As we have seen from the global financial crisis, such crises have a devastating effect on the economy – and it takes many years to recover. It would be counterproductive to divert the SARB's policies away from these important socio-economic objectives in order to try and achieve outcomes over which the SARB has little or no influence.

The fact that we do not have an explicit employment or growth mandate does not imply that we have a narrow focus on inflation to the exclusion of these considerations. However, we must be clear about what a growth mandate means for central banks. Monetary policy cannot determine the longer-run growth potential of the economy. This is the domain of other policies, as potential growth is determined by structural policies (e.g. on education, infrastructure, and technology). South Africa's high unemployment rate is largely structural. The contribution that monetary policy can make to long-run growth is through ensuring price stability, which is more conducive to longer-term investment and expenditure decisions. The higher and more volatile inflation is, the higher the riskiness of investment.

Monetary policy can, however, impact on the real economy over the economic cycle, i.e. on the extent to which growth fluctuates around potential output. The extremely moderate nature of the tightening cycle since 2014 is an illustration of our concerns for cyclical growth. While it is true that excessively tight monetary policy conditions can undermine growth and employment, the low and at times negative policy rate prevailing in South Africa in recent years is indicative of an accommodative monetary policy stance.

The bottom line is this: we cannot solve a structural growth problem with monetary policy, irrespective of our monetary policy framework. Keeping interest rates artificially low may have short-term benefits, but it will result in higher inflation in the long run. We cannot 'buy' higher growth and employment through high inflation. In fact, high inflation inhibits growth. Low inflation, by contrast, allows for lower interest rates and higher growth.

Whether we operate in an inflation-targeting framework or not, our objective will still be the protection of the value of the currency. Inflation targeting is a framework within which to achieve this target. It makes our objective transparent and helps to anchor inflation expectations. We would not behave differently in the absence of an explicit target. Inflation targeting has been successfully adopted by many other emerging markets as well, and more recently by a number of developing economies, including Ghana and Uganda.

The issue of private shareholding in the SARB also needs addressing, particularly in this forum. Private shareholding in central banks is an historical legacy, as originally central banks were in fact privately owned. This changed over time, particularly since the 1930s. Apart from the SARB, there are nine other central banks that have some form of private shareholding. These include the US Federal Reserve System as well as the central banks of Belgium, Greece, Italy, Japan, and Switzerland.

ANNEXURE A: AN ADDRESS BY LESETJA KGANYAGO, GOVERNOR OF THE SOUTH AFRICAN RESERVE BANK (THE SARB)

to the ninety-seventh annual Ordinary General Meeting of the SARB shareholders held on Friday, 28 July 2017 *continued*

The critical issue is the role that private shareholders play and the potential for conflicts of interest. In the SARB, private shareholding does not impart the same rights and benefits that shareholders in private companies have. The notion of a central bank as a public policy institution, with the main goal of promoting monetary and financial stability in the interests of the general public, is remote from the traditional concept of a commercial company with a profit motive. The SARB is an independent legal person, a public institution that has no profit motive and is not owned by its shareholders or anyone else.

Accordingly, shareholders in the SARB:

- have very limited rights;
- have no role whatsoever in the setting of, or influencing, the key mandates of the SARB, i.e. monetary policy and financial stability policy;
- have no sway over the day-to-day management of the SARB;
- are restricted to a maximum of 10 000 shares per shareholder out of 2 million issued shares (including those of their associates);
- receive a fixed return on their shares of 10 cents per share from profits made. (This amounts to an overall divided payment by the SARB of R200 000 per year. In fact, 90% of the SARB's profits are transferred to government, and the remaining 10% are allocated to the SARB's reserves.);
- do not have any claim on the foreign exchange reserves of the SARB; and
- are unable, by means of a resolution or otherwise, to amend or change the SARB's affairs by deviating from the prescriptions of the SARB Act.
- in terms of the SARB Act, the most effective powers of the shareholders are:
- the approval of the appointment of auditors for the SARB and their remuneration; and
- the election, from a vetted list, of seven non-executive directors to the Board. (The other eight members are appointed by the President. These include the Governor and the three Deputy Governors.)

Furthermore, the Board itself is a corporate governance board, and has no input or say in policies related to the SARB's mandates and primary functions. The Board's functions are limited to corporate governance issues, internal controls (including auditing), staff policies, and staff remuneration.

The management of the business of the SARB, including the setting of monetary policy, vests in the Governor and Deputy Governors, who are appointed by the President after consultations with the Minister of Finance and the SARB Board. The Governor and Deputy Governors are clothed with decentralised original powers of management.

Private shareholding represents an additional layer in the governance framework, to strengthen accountability and transparency, and complements the mechanism of how we are accountable to South Africans through their representatives in Parliament.

While international experience does not suggest that the shareholding structure of a central bank meaningfully affects its performance, there is equally no obvious case for changing this structure at present. Any move towards 'nationalisation' would be largely symbolic and would have no impact whatsoever on the SARB's mandate. The view that the SARB is owned and run in the interest of the private sector is incorrect. Our independence and mandate are enshrined in the Constitution. Whether the SARB has private shareholders or whether all its shares are owned by government, its primary mandate remains.

A considerable number of legal considerations would have to be taken into account if private shareholding were to be removed. The potential purchase of all the SARB shares by government would require the introduction of suitable legislative measures, since the SARB Act does not currently provide for this. This legislation would also have to provide for measures such as the determination of the value of the shares, as determined by the Legislature.

On private shareholding, it should also be noted that the SARB embarked on a process of regularising its shareholder structure, which culminated in a judgement obtained from the Gauteng division of the High Court in November 2016. In terms of said court order, a total of 149 200 SARB shares held by 15 shareholders were disposed of, which resulted in 57 new shareholders spread across the general public. The interest in SARB shares is currently exceptionally high, with standing buy offers from 28 buyers wishing to purchase 90 109 shares.

ABBREVIATIONS

AACB
Association of African Central Banks

ABHL
African Bank Holdings Limited

ABL
African Bank Limited

AGM
annual Ordinary General Meeting

app
application

BA
Bachelor of Arts

BC
Budget Committee

BCBS
Basel Committee on Banking Supervision

BCom
Bachelor of Commerce

BCompt
Bachelor of Accounting Science

BER
Bureau for Economic Research

BIS
Bank for International Settlements

BProc
Baccalaureus Procurationis (law degree to qualify as an attorney in South Africa, phased out in 2001 and replaced by an LLB)

BREC
Board Risk and Ethics Committee

BRICS
An association of five major emerging national economies: Brazil, Russia, India, China and South Africa

BSc
Bachelor of Science

CAF
Combined Assurance Forum

CA(SA)
Chartered Accountant South Africa

CCB
countercyclical capital buffer

CD(SA)
Chartered Director South Africa

CEO
Chief Executive Officer

CFO
Chief Financial Officer

CIA
Chief Internal Auditor

CIO
Chief Information Officer

CLF
committed liquidity facility

Companies Act
Companies Act 73 of 2008

Constitution
Constitution of the Republic of South Africa Act 108 of 1996

COO
Chief Operating Officer

COSO
Committee of Sponsoring Organizations of the Treadway Commission

CPD
Corporation for Public Deposits

CPD Act
Corporation for Public Deposits Act 46 of 1984

CPI
consumer price index

CSI
corporate social investment

DCom
Doctor of Commerce

ECL
expected credit loss

EIM
Enterprise Information Management

EQA
external quality assurance

ex officio
by virtue of one's position or status (Latin)

FATF
Financial Action Task Force

fintech
financial technology

FMA
Financial Markets Act 19 of 2012

FMI
financial market infrastructure

FSB
Financial Services Board

FSC
Financial Stability Committee

FSCA
Financial Sector Conduct Authority

FSCF
Financial Sector Contingency Forum

FSD
Financial Services Department

FSOC
Financial Stability Oversight Committee

FSRA
Financial Sector Regulation Act 9 of 2017

G-20
Group of Twenty Finance Ministers and Central Bank Governors

GDP
gross domestic product

GEC
Governors' Executive Committee

GFECRA
Gold and Foreign-Exchange Contingency Reserve Account

Hons
Honours (degree)

IAD
Internal Audit Department

IAS
International Accounting Standard

IASB
International Accounting Standards Board

ICT
information and communications technology

i.e.
id est (that is to say) (Latin)

IFRIC
International Financial Reporting Interpretations Committee

IFRS
International Financial Reporting Standards

IGCC
Inter-Governmental Cash Coordination

IIA
Institute of Internal Auditors

IMF
International Monetary Fund

IMFC
International Monetary and Financial Committee

Inc.
Incorporated

Income Tax Act
Income Tax Act 58 of 1962

InsureCo
African Insurance Group Limited

ISL
Investec Securities Proprietary Limited

ABBREVIATIONS *continued*

ISO
International Organization for Standardization

IT
information technology

ITSC
Information Technology Steering Committee

JSE
Johannesburg Stock Exchange Limited

King IV
King Report on Corporate Governance in South Africa 2016

LCR
liquidity coverage ratio

LLB
Bachelor of Laws

LLM
Master of Laws

Ltd
Limited

LTIFR
lost time injury frequency rate

Manco
Management Committee

MBA
Master of Business Administration

MCom
Master of Commerce

MPC
Monetary Policy Committee

MSc
Master of Science

Nedcom
Non-executive Directors' Committee

NPS
National Payment System

OPEC
Organization of the Petroleum Exporting Countries

Pension Funds Act
Pension Funds Act 24 of 1956

PhD
Doctor of Philosophy

Prestige Bullion
Prestige Bullion (RF) Proprietary Limited

Pty
Proprietary

PwC
PricewaterhouseCoopers Inc.

Rand Refinery
Rand Refinery Proprietary Limited

Remco
Remuneration Committee

repo rate
repurchase rate

Resmanco
Reserves Management Committee

RF
ring fenced

RMC
Risk Management Committee

RMCD
Risk Management and Compliance Department

SA
South Africa(n)

SABN
South African Bank Note Company (RF) Proprietary Limited

SADC
Southern African Development Community

SAM
Solvency Asset Management

SARB
South African Reserve Bank

SARB Academy
South African Reserve Bank Academy

SARB Act
South African Reserve Bank Act 90 of 1989, as amended

SARB Amendment Act
South African Reserve Bank Amendment Act 4 of 2010

SARB debentures
South African Reserve Bank debentures

SFA
strategic focus area

SIFIs
systemically important financial institutions

SNG
SizweNtsalubaGobodo Inc.

SOEs
state-owned enterprises

South African Mint
South African Mint Company (RF) Proprietary Limited

SRM
systemic risk measure

S&P
Standard & Poor's Financial Services LLC

the Board
Board of Directors of the SARB

the Group
South African Reserve Bank Group, including its subsidiaries and associate, African Holdings Limited, referred to in the summarised annual financial statements

UK
United Kingdom

Unisa
University of South Africa

USA
United States of America

VAT
value-added tax

Wits
University of the Witwatersrand

CONTACT DETAILS

PHYSICAL ADDRESS

Head Office

370 Helen Joseph Street (formerly Church Street)
Pretoria 0002
Telephone: 012 313 3911/0861 12 7272

POSTAL ADDRESS

P O Box 427 Pretoria 0001

CASH CENTRES

Cape Town

25 Burg Street
Cape Town 8001
Telephone: 021 481 6700
P O Box 2533 Cape Town 8000

Durban

8 Dr A B Xuma Street
Durban 4001
Telephone: 031 310 9300
P O Box 980 Durban 4000

Johannesburg

57 Ntemi Piliso Street
Johannesburg 2001
Telephone: 011 240 0700
P O Box 1096 Johannesburg 2000

South African Reserve Bank

www.resbank.co.za