On the mandate, ownership and independence of the South African Reserve Bank

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It has been suggested that the South African Reserve Bank (SARB) is not doing enough to support economic growth and employment creation. There is confusion in the public debate, however, as three distinct concepts – the SARB's mandate, ownership and independence – are often inaccurately lumped together and misinterpreted. This clouds the debate, and hinders progress. This article attempts to focus and stimulate the academic debate by distinguishing between these three distinct, yet interrelated, concepts, and to clarify misunderstandings and misinterpretation. It also suggests some avenues through which each could be investigated further, and how different dimensions to the problem could be considered independently.

Keywords: Central bank; mandate; independence; nationalisation; private shareholders.

Introduction

Against the backdrop of a poorly performing economy, high unemployment and pervasive poverty, as well as a growing international discontent with the conduct and approach of central banks, the role of the South African Reserve Bank (SARB) in the South African economic policy debate has been questioned. The SARB's main policy instrument[1] is the repo rate, which is the interest rate at which the SARB lends to commercial banks, and which anchors domestic interest rates, including the prime lending rate, as well as longer-term rates. The repo rate is therefore the main determinant of the cost of credit, and thereby the SARB's main tool in combating inflation: by increasing the cost of credit, it can cool down an overheating economy, slowing down inflation. A higher repo rate makes it more expensive to borrow, which would have the effect of slowing down consumption and investment spending, and ultimately aggregate demand and economic growth. It is for this reason that a tight monetary policy stance – that is a 'too high' repo rate – is often criticised as harming economic growth. For example, Padayachee (2015) suggests that, in order to suppress inflationary expectations, the SARB has too often raised the repo rate in response to mainly exogenous price pressure (rising petrol, energy and food prices) under conditions of slow and low domestic economic growth. This has had 'negative consequences for consumption itself as well as investment, growth, small business development and employment' (2015:7). Among others, Rochon and Rossi (2006) question the perceived superiority of inflation targeting above prioritising economic growth and employment, while Epstein (2008) argues for an 'employment targeting' monetary policy framework for South Africa.

At the core of the criticism lies the belief that the SARB's insistence on maintaining price stability constrains economic growth and job creation, and that it simply does not support the government's broader economic strategy and goals. In perhaps the highest profile criticism to date, the Public Protector (PP) in a 2017 report suggested that the SARB's activities, which 'involves vast amounts of public money does not improve the socio-economic conditions of ordinary citizens' (Public Protector [PP] 2017:5.3.23). The report further suggested that:

> Once the state takes control of creating money and credit, numerous benefits aimed at alleviating economic ails of ordinary economically disadvantaged people may be achieved, unlike our current purely commercial transaction system which only seeks to improve a particular financial sector. (PP 2017:5.3.25).

The report then concluded with the instruction that the Constitution be amended and the SARB's mandate changed to include the protection of 'socio-economic well-being of the citizens', and that the SARB should ensure the achievement of 'meaningful socio-economic transformation' (PP 2017:7.2.1). The PP suggested, in short, that the independence of the SARB should be curtailed and its mandate expanded, as its current approach favours only the financial sector and does not

1.The operational approach to monetary policy and the SARB's accommodation system are explained in SARB (2007).

sufficiently address developmental goals. This evoked a backlash from several analysts, academic and private economists, and the SARB itself, by way of legal proceedings instigated by both the SARB and National Treasury (Treasury 2017). In 2018, the High Court ruled in favour of the SARB, and the PP's report was set aside.

Nonetheless, the controversy around this report ignited the debate on not only the mandate of the SARB, but also its ownership and independent operation. The PP's report, which suggests that the SARB favours the financial sector, has given rise to a narrative that the SARB's private shareholders are manipulating monetary policy to their own narrow advances. The fact that the vast majority of central banks around the world are not owned by private individuals, but rather by their respective national governments, makes the SARB an anomaly, and adds fuel to this fire. Politicians and analysts are falling over themselves to make statements and pronunciations, or to contradict and contest statements made by others.[2] In the meantime, South African debt has been downgraded to sub-investment grade by two of the three notable international ratings agencies – Standard and Poor's and Fitch. The third – Moody's – was instead optimistically waiting for signs of economic policy certainty and an improved economic outlook. Disconcertingly, the conflicting utterances by politicians create an atmosphere of policy *un*certainty, which is certainly not conducive to the South African economy escaping the quagmire. Moody's eventually also downgraded South African debt to sub-investment grade in March 2020.

However, given stubbornly high unemployment, slow growth and pervasive poverty, the essence of the question remains important: is the SARB failing 'ordinary citizens'? This question begets several deeper questions: Is the SARB's mandate appropriate, given the South African socio-economic structure? Is the SARB *too* independent, and therefore indifferent to socio-economic issues? Can the SARB play a more active role in boosting growth and employment? Would nationalising the SARB solve these problems? These are loaded questions, and the purpose of this article is not to exhaustively address them all. Instead, this article aims to disentangle the debate by clarifying misconceptions about three key concepts, which are often misinterpreted and conflated in the greater debate, namely the SARB's *mandate*, its *ownership* and its *independence*. It has been suggested that the SARB is compromised by its private shareholders' nefarious intentions, whereas, if it was owned by the state (i.e. nationalised), these concerns would disappear. Others are concerned that a nationalised SARB would lose its independence and consequently see its inflation-combating ability curtailed, that nationalisation is but a step towards interfering with the mandate, and that expanding the mandate to explicitly include economic growth and employment creation could in itself be inflationary and ultimately ineffective. Careful consideration and understanding of these key concepts – distinct, yet interrelated – is imperative to driving the debate and research in the field forward.

This article is organised as follows: Section 2 considers the legal framework which governs the SARB and its current inflation targeting strategy. Section 3 separates the three key concepts highlighted earlier, namely the SARB's *mandate*, *ownership* and *independence*, in an attempt to eliminate ambiguity around these issues. This section further investigates possible overlaps between these three concepts. Section 4 considers some of the burning questions in the debate, and suggests areas for further research within each subject. Section 5 concludes.

A brief history of the South African Reserve Bank

Establishment of the South African Reserve Bank

The SARB was established in 1921 through the Currency and Banking Act (No. 31 of 1920). Some of the early functions of the SARB were to act as sole issuer of banknotes, hold reserves of commercial banks, discount short-term paper, and make advances against said paper, gold or government securities (Gelb 1989).

At the time, virtually all central banks around the world were privately owned. In South Africa 'commercial banks were required by law to subscribe … a part of the capital of the central bank' (De Kock 1974:306) to contribute to its establishment. Specifically, any bank that did business in South Africa was required 'to hold stock of the Reserve Bank to a nominal value of not less than 5 per cent of its own paid-up capital' (De Kock 1954:24), although this requirement was subsequently dropped, as is explained below. The SARB issued share capital of £1 million[3], represented by 2 million shares. Only £280 420 was subscribed by commercial banks, and the remaining £719 580 was offered to the public (De Kock 1954:48). The share capital was fully subscribed by 06 March 1922 (Rossouw 2018). The SARB was therefore established with stockholders (as they were called at the time), consisting of commercial banks and private individuals.

Contemporary legal framework

The SARB is ultimately governed by the South African Constitution, which reads:

> The primary object of the South African Reserve Bank is to protect the value of the currency in the interest of balanced and sustainable economic growth in the Republic. (RSA 1996:224[1])

This is the SARB's *mandate*. 'Protecting the value of the currency' is interpreted as maintaining price stability, 'quantified by the setting of an inflation target by Government that serves as a yardstick against which price stability is measured' (SARB n.d.a). Growth and employment objectives are therefore not explicitly part of the SARB's

2. See, for example, Fin24 (2019b).

3. The share capital was converted to R2 million at decimalisation in 1961 (Rossouw 2018).

mandate, while price stability – protecting the value of the currency – is. The *independence* of the SARB is also enshrined in the Constitution:

> The South African Reserve Bank, in pursuit of its primary object, must perform its functions independently and without fear, favour or prejudice, but there must be regular consultation between the Bank and the Cabinet member responsible for national financial matters. (RSA 1996:224[2])

Reading these two paragraphs in conjunction, 'an independent SARB would be constitutionally bound to consult the finance minister in conducting monetary policy, and … the Bank should act in support of the general economic policy of government' (Padayachee 2015:5). Indeed, the SARB governor regularly meets with the Minister of Finance, as well as provides briefings to Parliament. This sets up the relationship between the SARB and the government as the SARB simply an arm or functionary of government, under the umbrella of the Ministry of Finance (National Treasury). Moreover, the SARB is not narrowly focused on the inflation target only, but also considers economic growth and broader goals when setting policy.[4] The SARB is further governed by the *South African Reserve Bank Act* (No. 90 of 1989), which has since been amended by, among others, the *South African Reserve Bank Act* (No. 39 of 1997) and the *South African Reserve Bank Amendment Acts* (No. 10 of 1993, No. 2 of 1996, No. 57 of 2000 and No. 4 of 2010).

The final mention of the SARB in the Constitution refers to its functions:

> The powers and functions of the South African Reserve Bank are those customarily exercised and performed by central banks, which powers and functions must be determined by an Act of Parliament and must be exercised or performed subject to the conditions prescribed in terms of that Act. (RSA 1996:225)

The SARB formulates and implements monetary policy, acts as a banker for the government, manages and supports the national payment system, acts as the custodian for South Africa's gold and foreign exchange reserves, and oversees several aspects of financial stability and macro- and micro-prudential regulation, among others (SARB 2007). However, since the debate around the role of the SARB is mostly concerned with the monetary policy stance, through the SARB's control over the policy (repo) interest rate, the remainder of the article considers only the SARB's monetary policy role.

These constitutional clauses – indeed the Constitution in its entirety – were the result of the Convention for a Democratic South Africa (Codesa) and Multiparty Negotiating Forum (MPNF) negotiations during the early 1990s. At the time, South Africa had just emerged from years of oppressive minority rule under the apartheid government and strict economic sanctions imposed on them during the 1980s which led to disinvestment, debt crises and a crippled economy. The negotiators and decision-makers at the time were faced with a difficult decision: the juxtaposition of the 'world-wide accepted increase in the importance of central bank independence' against the dominant 'political grouping (the African National Congress [ANC]) with an initial inclination towards socialism … also involving many jobless and disadvantaged stakeholders' (Wessels 2004:132). Ultimately, the decision was taken that the SARB should be empowered through independence to protect the value of the currency. While the choice at the time was not between choosing either employment or price stability, the expectation was presumably that an independent central bank would be first and foremost concerned with price stability, which would hopefully foster balanced and sustainable economic growth in the long run, leading to employment creation. It is quite likely that the fragile state of the economy at the time, and resultant urgent desire to attract foreign investment[5] and reintegrate in global markets, inspired these sections of the Constitution to be drafted in such a manner as would ensure access to the increasingly integrated world financial markets.

Inflation targeting

The government, through the Minister of Finance, announced the adoption of a formal inflation targeting framework in 2000 (Treasury 2000). This framework involves maintaining inflation – as measured by the Consumer Price Index (CPIX),[6] excluding interest costs, within a target band of 3% – 6%. This target was chosen in consultation between the National Treasury and the SARB (Treasury 2000) and became the benchmark by which the SARB exercises its mandate of the achievement of price stability.

The importance attached to price stability (i.e. low and stable inflation) is twofold: firstly, inflation reduces purchasing power, and erodes living standards. Some individuals are able to hedge or protect themselves against inflation: salaries can adjust in line with inflation, while growth in savings or investments could outperform inflation, thus protecting purchasing power. However, the poor and unemployed are unable to protect themselves against inflation. These citizens are often reliant upon nominal earnings, such as social grants or daily or seasonal wages, if they earn anything at all. They are more vulnerable to price increases, and their incomes are too small to even consider investing in inflation-hedging products. Easterly and Fischer (2001:161) find that 'inflation reduces the relative income of the poor', while StatsSA (2016) suggests that 'volatile inflation hurts the poorest'. Secondly, Treasury reasoned that 'stability in the value of money … enhances growth prospects' (Treasury 2000:6). The setting of an inflation target is suggested to anchor inflation expectations while creating 'certainty and transparency with regard to the bank's policy intentions' (Wessels 2004:144). Anchored

4. The SARB applies a 'flexible' inflation targeting framework (Kahn & De Jager 2011), favouring a pragmatic, instead of draconian, approach to interest rate setting. This should prevent a knee-jerk reaction in response to exogenous price shocks.

5. According to Maxfield (1997:4), governments hoping to attract foreign investment 'use central bank independence to try to signal their nation's creditworthiness to potential investors'.

6. The CPIX was replaced by the re-weighted CPI in January 2009.

expectations, in turn, make it easier for a central bank to manage and combat inflation. This creates an environment conducive to sustainable long-term economic growth. The government thus prioritised price stability specifically to 'counter the erosion of people's incomes and living standards that comes with rising prices and to remove the fear of future inflation that undermines investment and savings decisions' (Treasury 2000:5).

Demarcating the debate

The preceding section presented the legal framework and relationship to the government within which the SARB operates, while highlighting the importance the government and decision-makers of the time attached to price stability. This provides the context within which the SARB's *mandate*, *ownership* and *independence* can be examined further.

Mandate

The SARB's mandate is given by P.224 of the Constitution as *to protect the value of the currency in the interest of balanced and sustainable economic growth in the Republic.* To *protect the value of the currency* is interpreted as maintaining price stability, in the form of maintaining inflation within the 3% – 6% target band. However, the SARB's mandate was not always this well defined. During the second half of the 1980s, monetary policy objectives were stated as 'promoting economic growth, price level stability, balance of payments equilibrium, and enhancing employment' (Wessels 2004). In practice, however, 'different monetary policy objectives got prioritised at different times' (Wessels 2004:137). Wessels (2004:135), however, argues that it is 'imperative for a central bank to have a clear, single or primary objective', as the setting of multiple objectives might 'compromise the bank and invite political interference'. A single and clearly defined objective also enhances transparency and accountability. Wessels (2004) further argues that the SARB was strongly influenced by political matters in the mid-1980s, due to, among others, disastrous international sanctions imposed on South Africa. This pressure, including the Primrose prime incident of 1984,[7] 'resulted in the non-attainment of price stability, due to a more accommodating policy stance than was warranted' (2004:138).

During the early 1990s, as South Africa was transitioning to a democratic state, the central bank's mandate needed to be reconsidered. A clear single mandate for the SARB was adopted, in line with international best practice of the time. However, just over 25 years later, the SARB's mandate is back in the spotlight. While the attainment of relative price stability during the 1990s and 2000s is praiseworthy, economic growth and especially employment creation has lagged behind. Inflation has been reigned in from around 15% to under 6%, but growth has been lethargic and the unemployment rate has steadily increased. The price stability mandate, which did not translate into the employment creation envisaged, is therefore being questioned. The ruling African National Congress (ANC), at its 54th National Conference, consequently revisited the mandate of the SARB, and concluded that:

> Without sacrificing price stability, monetary policy should also take account of other objectives such as employment creation and economic growth. (ANC 2017:32)

Price stability was affirmed again to be the primary object of the SARB, despite the fact that price stability has not resulted in satisfactory employment creation. Some analysts believe that the bleak employment numbers are the result of other factors which are not sensitive to monetary policy, while others suggest that these numbers are proof that the government's faith in price stability is misguided. The controversial PP's report, alluded to earlier, instructed that Section 224 of the Constitution, pertaining to the mandate of the SARB, be changed to read:

> The primary object of the South African Reserve Bank is to promote balanced and sustainable economic growth. (PP 2017:7.2.1)

This order was met with outrage, no less than from the SARB itself, who challenged the authority of the PP to order changes to the Constitution. The PP's report was set aside by the High Court in 2018 (High Court of South Africa 2018), thus leaving the SARB's mandate unchanged for the time being. In actual fact, the SARB's mandate can *only* be changed by Parliament through a Constitutional Amendment Bill to amend Section 224, with such a bill requiring the support of at least two-thirds (267 out of 400) of the members of the National Assembly (RSA 1996:74[3]).

Ownership and nationalisation

Origin of the South African Reserve Bank's private shareholders

By the early 20th century most central banks were quasi-governmental bodies, despite the fact that at that time 'only a tiny number of central banks … were state-owned institutions. The majority had total or majority or significant private shareholders' (Padayachee 2015:11), including the SARB. Indeed, at the time 'it was exceptional for central banks not to have private shareholders' (Rossouw & Rossouw 2017:6). SARB stock (as the shares was known until 1989, with shareholders known as *stockholders*) was originally owned by both commercial banks and private individuals. This changed when banks were 'relieved[8] of the obligation to hold a certain amount of Reserve Bank stock' (De Kock 1974:306). Some of the stock in the hands of banks was subsequently sold to the public with some South African banks at the same time retaining some of their stock (currently known as *shares*).

Ownership structures of central banks started changing after 1936 and gained momentum after the Second World War (WWII) (Rossouw & Breytenbach 2011). In contrast to

7. In 1984, the SARB dropped interest rates shortly before an important by-election in the Primrose constituency. This 'placed in serious jeopardy the ability of the Bank to conduct autonomous monetary policy' (Rossouw & Padayachee 2008:17).

8. The Currency and Banking Act Amendment Act (No. 22 of 1923) allowed banks to 'dispose of the whole or part of their holding of Reserve Bank stocks' (De Kock 1954:61).

the early central banks, central banks established during and after WWII had no private shareholders, and 'were founded as State institutions' (De Kock 1974:304), by way of national governments subscribing the new central banks' full capital. The majority of older central banks were also nationalised during this time, with governments effectively buying out shareholders. For example, the Bank of England was owned by private shareholders from its inception in 1694, until it was nationalised in 1946 by way of the Bank's capital stock wholly transferred to the Treasury (BoE 1946).

As of 2019, there are only nine remaining central banks with private shareholders in the narrow sense of the word, namely: Belgium, Greece, Italy, Japan, San Marino, South Africa, Switzerland and Turkey. The Federal Reserve Banks in the United States have banks in their regions as 'shareholders' in the overall Federal Reserve System, but this shareholding is akin to reserve holding deposits with central banks in other countries.

Current shareholders and shareholder rights

The question of who the SARB's shareholders are, and what interests they represent, is often raised. The SARB currently has about 750 private shareholders who own the 2 million shares issued (SARB n.d.c). No associated shareholders are allowed to own more than 10 000 shares,[9] while shareholders have one vote for every 200 shares held. The objective of capping the voting rights of shareholders gives effect to par. 224(2) of the Constitution to not allow prejudice or undue influence over the SARB by its shareholders, although this was in existence long before the adoption of the Constitution. Dividends are statutorily limited to 10c per share (SARB n.d.c) and are subject to dividend withholding tax. Surpluses after payment of tax and allocation to reserves are transferred to government, which indicates that the SARB's operations are not driven by a profit motive.

The SARB's board of directors can consist of up to 15 directors. Eight directors, including the governor and three deputy governors, are appointed by the president of South Africa, after consultation with the Minister of Finance and the board. The SARB's shareholders can elect a maximum of seven non-executive directors from a list of candidates approved by a panel chaired by the governor (RSA 2010:2). Such candidates shall be deemed 'a fit and proper person with appropriate skills and experience' in fields such as commerce or finance, agriculture, industry, labour and mining (RSA 2010:2(e)–(f)). Non-executive directors serve terms of three years. The four executive directors – the governor and three deputy governors – are appointed for initial terms of five-year terms, while reappointment for second and consecutive terms can be for any period up to five years.

The powers and functions of the board are spelled out in the *SARB Amendment Act* (No. 4 of 2010) (RSA 2010:4A), and comprise various aspects of corporate governance of the Bank. The Act also explicitly states that 'all other powers and duties of the Bank under this Act shall vest in and be exercised by the Governor and Deputy Governors' (RSA 2010:4A). The power of shareholders is thus strictly limited to decisions impacting on governance decisions, such as the election of non-executive directors and the appointment of auditors. This governance structure is argued to 'enhance the independence, transparency and accountability' of the central bank (Rossouw 2018:7).

Independence

Walsh (2010:21) defines central bank independence as 'the freedom of monetary policymakers from direct political or governmental influence in the conduct of policy'. The importance of independence stems from the argument that 'the power to spend money should in some way be separated from the power to create money' (Mboweni 2000:1). Governments and politicians naturally carry an inflationary bias, as they can be tempted to spend money to 'create favourable economic and political environments just before elections' (Wessels 2004:133). A government concerned with its immediate popularity might strive for short-term gains from lower interest rates, even at the risk of promoting somewhat higher inflation further down the road (Mboweni 2000). An independent central bank would, in contrast, theoretically be free from political interference and have greater commitment to long-term objectives such as promoting a more stable price level (Polillo & Guillen 2005:1770). An independent central bank can pursue policies that are in the interest of the public, even if they might be politically unpopular.[10] The motivation for independence to be granted to central banks is thus exactly to shield or insulate them from short-term political influence or partisan political goals, and allow them to fulfil their mandate of long-term price stability as part of the country's overall economic strategy.

Another consideration is the danger of fiscal dominance. In emerging-market economies, there will always be added pressure for greater social expenditure that is funded via government spending, but against a narrower tax base (Kahn 2008:131). Under such conditions, the central bank could be forced – or at least expected – to create money to finance fiscal deficits or service the government's debts, which could ultimately enable a government to spend with reckless abandon. Even well-meaning governments can be tempted to simply create their own money through the central bank in order to finance deficit spending.[11] However, the inflationary impact of such behaviour has often been disastrous. Indeed,

9. A small handful of current shareholders opposed this limit, and legal action against delinquent shareholders was instituted by the SARB (Rossouw & Rossouw 2017).

10. An independent central bank can be a convenient scapegoat for failure of economic policy (Kane 1980). Governments cede monetary policy to a central bank since 'politicians want to be able to deny responsibility for unpopular monetary policy' (Maxfield 1997:12). Kganyago (2019)'s conviction that this 'obsession' with the SARB is a distraction from the real, hard economic questions that need to be asked perhaps gives credence to the scapegoating theory.

11. It should be noted that the Reserve Bank Act does make allowance for a limited amount of government stock to be held by the SARB. The SARB cannot, however, make 'excessive direct purchases of government stock' (Mboweni 2000:6). This does not rule out the central bank granting credit to the government, but it does restrict the direct financing of government deficits by the central bank.

'there is ample historical evidence of countries experiencing runaway inflation stemming from the malpractice of central banks being pressurised by governments into financing their fiscal deficits' (Wessels 2004:153), evident recently right on our doorstep in the case of Zimbabwean hyperinflation. Printing money to finance government spending has the effect of lowering the value – and therefore purchasing power – of existing money, leading to the need to print even more money to finance the same level of real spending, further eroding purchasing power, and so forth in a vicious cycle. It is for this exact reason that governments choose to delegate the functions of monetary policy and money creation to an independent, technocratic institution concerned first and foremost with price stability. This is also why the PP's suggestion that the state should directly take 'control of creating money and credit' (PP 2017:5.3.25) was met with outrage and consternation from several directions.

Independence is desirable for a central bank focused on price stability. An independent central bank is less vulnerable to the time-inconsistency problem (Kydland & Prescott 1977), where a policymaker might be tempted to pursue short-term gains at the expense of its long-term objectives. Moreover, a central bank that successfully pursues its mandate will have its credibility enhanced. This sets in motion a virtuous cycle, where higher credibility further anchors inflation expectations, ultimately improving the central bank's ability to meet its objectives. Credibility thus results in more effective combating of inflation. This is supported by many empirical studies which found that lower inflation is often realised in economies with more independent central banks (see e.g. Bodea & Hicks 2015; Walsh 2003). Finally, and perhaps most importantly an independent central bank is better equipped to withstand fiscal dominance.

There are also arguments against central bank independence. Forder (2005:854) questions central banks' motives by arguing that they are 'organisations with a very clear political interest, namely the enhancement or protection of their own position', while disputing 'the presumption of economists' moral superiority and the superiority of policy making by economists over politicians and democratic policy' (2005:856).[12] An independent central bank could also result in poor coordination of monetary and fiscal policies (Maxfield 1997).[13] Caruana (2013) warns against 'financial dominance', arguing that central banks should be insulated not only against political pressures (fiscal dominance), but also against financial market pressures.[14] The political argument is that turning over control of monetary policy, which affects every person in the country, 'to a body of unelected officials, is simply "undemocratic"' (Mboweni 2000:3). Such independent officials could have limited accountability, and be insensitive to the broader goals of government and society. Forder (2005:852) argues that 'unrestrained authority cannot be presumed to serve the public interest'. Walsh (2010:25) warns against the 'danger that a central bank that is independent will not be accountable'. Maxfield (1997:16) concedes that 'central banks are accountable to voters only indirectly', through their accountability to the government.

Notwithstanding these criticisms, the global trend has seen the autonomy of central banks gradually increasing since the 1980s (Padayachee 2015). Independence insulates central banks from the time-inconsistency problem and partisan political pressures, which improves the central bank's credibility. Specifically:

> If the public believes that the central bank is free from interference … it will also lower inflationary expectations, leading to price stability above and beyond the control of the money supply. (Bodea & Hicks 2015:54)

However, unrestrained independence is also not desirable, with the ideal scenario seeing 'a role for the elected government in establishing the goals of policy and in monitoring the central bank's performance in achieving these goals' (Walsh 2010:25).

Relationship between these concepts

Independence and mandate

The SARB receives its price stability mandate – the inflation target – from the government. This means that the SARB does not have the freedom to select its own goals or objectives, and it is therefore nothing more than an agent or representative of the government tasked with a certain set of delegated goals. However, the government does not dictate to the SARB *how* it should go about to achieve said goals. Instead, the 'setting of monetary policy instrument values … is entirely up to the Reserve Bank' (Mboweni 2000:4–5). Therefore, the SARB is viewed as *goal dependent* but functionally or *instrument independent*. That is, the SARB can autonomously utilise any tools it deems necessary to achieve its government-directed goals, and it enjoys 'full independence to apply its range or mix of policy instruments to pursue the target in an unconstrained way' (Wessels 2004:155). The SARB thus falls within Walsh (2010)'s standard, where government sets the goals of policy and monitors the SARB's performance in achieving these goals.

Ownership and mandate

Normally, shareholders have a substantial say in a company's strategic objectives such as profit maximisation, maximising shareholder value through dividends or the appointment of executives. However, current legislation prevents shareholders from exercising the same influence over the SARB. The SARB is not a profit-maximising corporation, surplus earnings are transferred to the government and dividends are capped by law. While shareholders can appoint non-executive directors,

12. It is this perceived arrogance and disconnect of economists and technocrats to think themselves more equipped than the elected government to act in the public interest which grates. The misunderstanding is, however, that they are arguably simply performing the tasks delegated to them by democratically elected politicians.

13. However, Maxfield (1997:15) argues that 'lack of policy coordination can stem from a variety of factors other than central bank independence'.

14. Interestingly, the SARB's first board of directors included three representatives of the commercial banks of the time. However, the Currency and Banking Act Amendment Act (No. 22 of 1923) excluded these banking representatives from the board, specifically to increase its independence from the banking sector (De Kock, 1954).

executive directors are appointed only by the government. Therefore, the SARB's shareholders cannot set the SARB's goals or objectives, nor can they flaunt or change the SARB's Constitutional mandate.

Just as private shareholding of the SARB does not give private individuals the power to dictate the SARB's mandate, so government ownership of the SARB will not give government or Treasury – who would be the new sole shareholder if the SARB was nationalised – or the ruling party the power to simply change the mandate. The mandate can only be changed through a Constitutional Amendment Bill, as was described earlier.

Independence and ownership

There are suggestions that the independence of the SARB is supported by the presumed more effective governance instilled by its private shareholders (Rossouw 2018), as well as the expertise they bring to the board. However, the fact that several independently operating central banks around the world are fully owned by their respective governments, suggests that private ownership is not a prerequisite for a credible and independent central bank. A nationalised central bank can also be independent in this context. Independence simply means that the central bank has the autonomy to pursue its goals, without its notional 'owners' (be they private individuals, the government or some combination) dictating how it should go about things.

Focusing the debate

Having separated these concepts, key questions or areas of debate can now be teased out, and each addressed within its own paradigm. This allows the debate to be broken down into manageable research agendas.

Could, and should, the South African Reserve Bank's mandate be changed?

The SARB's mandate is determined by the Constitution, and it can only be changed through Parliament by a Constitutional Amendment Act (see Section 1). The ANC reaffirmed that the mandate of the SARB should be the maintenance of price stability, while also calling for the nationalisation of the SARB (see Section 3). Price stability therefore remains the primary object. Nationalisation, or full state ownership, of the SARB, however, does not in and of itself broaden the SARB's mandate to explicitly include growth or employment creation. Therefore, nationalising the SARB would not translate to a change in its mandate.[15]

However, there are still calls from various directions that the mandate should be formally changed to include growth and employment. But to what extent can monetary policy affect growth and employment? What does existing empirical evidence suggest? For the purpose of the current national conversation, it is important to acknowledge the influence of monetary factors on the economy, and the role that monetary policy can – and cannot – play.[16]

During the 1950s and 1960s, the dominant academic view, supported by empirical evidence from various countries, was that there existed a trade-off between inflation and unemployment. This relationship was known as the Phillips curve, after Phillips's (1958) seminal paper, which detected a negative relationship between wage inflation and the UK unemployment rate and gave rise to the ultimately misconstrued idea that monetary policy could essentially 'buy' lower unemployment by tolerating higher inflation.[17] However, the relationship broke down in the 1970s, with the result that 'monetary policy was [is] no longer an effective tool for determining national employment levels' (Maxfield 1997:7). Vermeulen (2017) recently confirmed that such a long-term Phillips curve trade-off has not existed for South Africa since at least 2000. Empirical evidence further suggests that domestic economic growth and employment creation are relatively unresponsive to changes in interest rates and inflation (Hodge 2002; Vermeulen 2017). In fact, Hodge (2006:30) finds that 'inflation drags down growth in South Africa over the longer term'. The SARB's own models suggest that the growth effect of an interest rate reduction is quite small: a 100-basis-point rate cut would lead to a 0.5 percentage point increase in growth (Kganyago 2019). Tolerating more inflation for the sake of higher aggregate demand, through a looser policy stance, could potentially boost growth in the short term, but this boost would be quite small. However, this would raise inflation expectations and core inflation in the longer term, growth will slow down again, and there will be 'no permanent increase in output' (Kganyago 2019:10). In addition, permanently higher interest rates would be required to combat the higher inflation (Kganyago 2019), which is likely to further erode any gains made in the first place. This view is consistent with the main criticism of the Phillips curve hypothesis in the academic literature, which states that 'expansionary monetary policy would eventually raise expected inflation, resulting in higher inflation with *no output stimulus*' (Erceg 2010:176, own emphasis). Moreover, the brunt of the higher inflation will be felt by the poor and unemployed (Easterly & Fischer 2001). Therefore, striving for a short-term growth boost through rate cuts is likely to perversely *slow* growth in the long term, while imparting unnecessary inflationary pressure.

There are, of course, studies that make the opposite case. These include Epstein (2008) and Rochon and Rossi (2006), who argue that the opportunity cost of maintaining price stability is lost growth and employment. Stiglitz (2008:3)

15. This point has also been made and emphasised by president Ramaphosa (Fin24 2019a).

16. The literature on the impact of monetary variables (money supply and interest rates) on real variables (employment, economic growth and development) is immense. An exhaustive treatment of this topic falls beyond the scope of this article, but the debate can be traced back as far as Keynes and Hayek in the 1930s.

17. A significant empirical literature also interprets the Phillips curve as the relationship between inflation and output. In this view, higher output could be achieved by tolerating higher inflation.

contends that inflation targeting leads to a 'weaker economy and higher unemployment'. There is also a strand of literature that suggests that mildly high inflation would not adversely affect output. For example, Pollin and Zhu (2006:593) find that 'higher inflation is associated with moderate gains in gross domestic product growth' across a sample of middle-income and low-income countries. In such an environment, a looser monetary policy stance could potentially be pursued to attempt to boost economic growth.

As there seems to exist a fundamental disagreement over the degree to which monetary variables could influence real variables, this area warrants further empirical research in the South African context. Considering the two sides though, it is unclear how changing the SARB's mandate could contribute to growth and employment creation. As it stands, the evidence favours the conclusion that monetary policy *cannot* permanently support economic growth. If a looser policy stance, due to chasing growth and employment, causes higher inflation, growth would surely be harmed in the long run. Would the small short-term gains then be worthwhile? What about the impact of higher inflation on the poor? This debate is likely to rage on, as there are different motives and ideologies at play. But clearly, these questions need to be unequivocally answered first, before improper responsibilities and expectations are foisted upon the SARB. Empirical evidence suggests that looser monetary policy would have a very small impact on real variables, and could cause the SARB to lose its grip on inflation. Higher inflation would erode the living standards of all, especially our 9.4 million unemployed and discouraged work-seekers (StatsSA 2019), while its expansionary effect would be limited. Therefore, the current price stability mandate is arguably the mandate which best protects the socio-economic well-being of citizens.

Are the South African Reserve Bank's private shareholders exerting undue influence over monetary policy?

The governance of the SARB rests in the hands of its board of directors. The shareholders can elect up to seven (a strict minority) non-executive directors to the board, but – crucially – these directors have 'no power over monetary policy decisions or implementation' (Rossouw 2018:11). The remaining four non-executive directors and the four executive directors are appointed by the president. The monetary policy stance (i.e. the level of the repo rate) is not determined by the SARB's directors, board or shareholders, but by the Monetary Policy Committee (MPC).[18] The MPC consists of the governor, three deputy governors, and up to three senior officials (SARB n.d.b). The MPC is thus clearly a separate entity from the board, with only the four executive directors present on both panels. Shareholders are therefore not represented on the MPC. Moreover, 'at no time have private shareholders [*been able*] to affect the conduct of monetary policy' (Padayachee 2015:12). In addition:

> The Governor of the Bank has a deciding vote on the Board, giving control of the bank to those appointed by the President. Shareholders cannot remove the governor or the other members of the Board and have very little power over the Bank. (De Vos 2010:1).

Finally, the Reserve Bank Act makes provision for the Minister of Finance to make regulations regarding, among others, the election of directors by shareholders and shareholders' meetings in general (RSA 1989:S36). This reveals the 'considerable influence government has on the appointment of these officials' (Wessels 2004:146). Even though the SARB is not notionally 'owned' by the government, its key executive officers are appointed by the president. These executive officers currently occupy four out of the five seats on the MPC, while no director elected by the shareholders is present on the MPC. Control of the bank – and indeed over monetary policy – therefore effectively rests mainly with the government through the appointment of the executive directors. Shareholders' influence is limited to matters of corporate governance, and they are unable to dictate the monetary policy stance: *ownership is therefore completely removed from control* of the SARB and its policy objectives.

Should the South African Reserve Bank be nationalised?

The ruling ANC recently resolved that the SARB should be nationalised, that is '100% owned by the state' (ANC 2017:32). This would be consistent with the global standard where shares in the majority of central banks are, in fact, owned by their respective governments. This creates the expectation – and implication – that the *government should buy out private shareholders*, thus taking the SARB into national ownership. The political pressure to act on this resolution, as well as widespread disagreement over the SARB's mandate and independence, has, however, created a volatile situation. *Owning* SARB shares is not particularly profitable; however, *selling* the shares could potentially be lucrative. A government instructed by its ruling party to buy out these shareholders could potentially be forced to pay an exorbitant price in order to enact this resolution. Indeed, it would be in the interest of current shareholders to value their shares as high as possible, in the hope that the political pressure would force Treasury to meet their valuation when determining the price per share. As there is currently no mechanism in place to force shareholders to relinquish their shares, the predicament is thus that some current shareholders could simply refuse to sell their shares if the government is not willing to meet their valuation. This impasse creates the impression of the tail wagging the dog, and is likely contributing to the polarisation of the debate.

Recently, SARB shares have been separately valued at R1.55 and R1.38 per share (Rossouw & Rossouw 2017). The shares

18. Interestingly, 'during the pre-democratisation era monetary policy decisions were made predominantly by the person of the governor of the bank' (Wessels 2004:149). The MPC was only created in 1999.

have also been argued to be worth an exorbitant R4700[19] each (Mail & Guardian 2017), suggesting that some shareholders are indeed trying to profit from the political situation. However, the ANC also resolved that full public ownership of the SARB must be ensured 'in a manner that does not benefit private shareholder speculators' (ANC 2017:32). So the question of how the shares should be valued, to ensure that a just and equitable price can be reached, remains a potential area for further research. However, given that ownership of the SARB is so far removed from control over policy, nationalisation would really just change the name on the door, with precious little effect on policy.

Is the South African Reserve Bank 'too' independent?

The SARB receives its price stability goal from the government, and is free to pursue this utilising any tools it deems appropriate. However, the MPC also takes account of economic growth and other macro-economic considerations, and not just inflation, when choosing the policy stance, as a cursory reading of many MPC statements would confirm. SARB officials report to, and are held accountable by, the government, both in terms of the governance of the central bank, as well as the conduct of monetary policy within the framework of Government's broader economic policy. Indeed:

> … even the most autonomous central bank has to report in some form or another to the legislature, which in any case also has the ultimate power to change the laws governing the central bank (Mboweni 2000:3).

Central banks are ultimately 'creations of their respective governments and can therefore never function in complete isolation from Parliament' (Wessels 2004:151).

Independence does not imply a relentless focus on inflation at the expense of growth. According to Maxfield (1997), a weak empirical relationship between independence and employment and growth is observed for Organisation for Economic Co-operation and Development countries, which 'suggests that fears that central bank independence will strangle social democracy may be misplaced for the present' (p. 17). However, the fact that very little evidence on this relationship is available – particularly for developing economies – suggests a need for further empirical investigation.

Conclusion

It has been suggested that the SARB's mandate should be expanded to formally include economic growth and employment. To some, the SARB's 'soft' stance on these factors is unacceptable: growth and employment should not be subordinate to price stability. On the other hand, the orthodox academic view, shared by many central bankers around the world, is that price stability is an important precondition for sustainable long-term economic growth, and that employment creation should follow from such growth. Higher inflation, resulting from the rejection of the price stability goal and a subsequent looser policy stance, would harm growth and stifle employment creation. Moreover, higher inflation erodes the purchasing power and living standards of everyone, especially the poor and unemployed. Reckless and populist monetary policy could easily result in hyperinflation, the debilitating effects of which are currently visible in Zimbabwe and Venezuela.

Short-termism by politicians cannot be reconciled with the long view central bankers hold. Thus, to protect themselves from temptation, governments around the world have generally delegated monetary policy matters to an independent central bank, while legally or politically empowering central banks to pursue such matters at their own discretion. Nonetheless, the central bank is only one pillar of broader economic policy, and 'monetary policy … accordingly has to serve the overriding objective of macroeconomic policy' (Wessels 2004:141). However, the cost of a central bank artificially boosting demand by lowering interest rates, increasing the money supply, or generously monetising government debt is likely to outweigh any potential short-term gains. By taking the long view and focusing on price stability, the central bank creates 'a financial environment conducive to economic growth' (Wessels 2004:142), thus ensuring fertile soil for sustainable and inclusive long-term economic growth. While the central bank 'has the machinery and the expertise to carry out the monetary policy' (De Kock 1974:318), it remains but an agent of the government which dictates the overall direction of policy. The government therefore has the full right to change the direction of policy, and thereby the directive of the central bank, if it deems necessary.

Nationalising the SARB would eliminate perceived conflicts of interest between the private shareholders and the government's policy goals. However, given that monetary policy is already fully insulated from shareholder interests, such an approach would be largely symbolic. This would not change the way the SARB operates, nor change its mandate or priorities, all at an added cost to an already-stretched fiscus.

Independence does not make the SARB unaccountable or insensitive to growth and employment. The SARB reports to Parliament, and is held accountable by the Minister of Finance. Moreover, according to Padayachee (2015:2), 'most independent central banks are also state-owned entities'. There is thus no reason for a nationalised SARB to be any less independent than it is under its current private ownership. Fears that a nationalised SARB would lose its independence and credibility are perhaps misplaced.

19. There seems to exist a misconception that the SARB's shareholders have access to gold and foreign exchange reserves held by the central bank on behalf of the government. Crucially, however, the SARB is not the *owner* of the country's gold and foreign exchange reserves, but merely the *custodian*. Gold and foreign exchange belongs to the government, while the SARB is only responsible for the management thereof. Therefore, no SARB shareholder can lay claim to a share of the country's gold or foreign exchange reserves, as these assets do not belong to the SARB and, by extension, also not to its shareholders.

In conclusion, the debate about nationalising the SARB is much ado about semantics. The 'owners' of the central bank have no say in matters of monetary policy. Moreover, given current legislation, changing the name on the door will make no difference to the SARB's mandate, nor to growth or employment creation. In the words of Governor Kganyago, 'the growth problem in South Africa is mainly structural, … beyond the reach of monetary policy alone' (2019:2). We should stop pretending that 'if the SARB could just cut rates … all will be well' (Kganyago 2019:13). In short, the nationalising debate is the wrong debate to have. Instead of foisting unrealistic expectations on the SARB, we would be better served to let the central bank get on with what it is designed to do: maintain price stability. On the balance of current evidence, monetary policy is unfortunately not the silver bullet that would cure our growth and employment problems.

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Author's contributions

I declare that I am the sole author of this research article.

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