



**CO-OPERATIVE BANKS DEVELOPMENT AGENCY**

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**Market Risk Management guideline**  
**for**  
**Co-operative Financial Institutions**

## Background

CFI investments may suffer a loss if there is a fall in the market value of an investment. This is called 'market risk' or sometimes 'price risk'.

There are three major types of market risk:

- a) *Interest-rate risk*: - If interest rates rise the value of assets that promise a return at a fixed rate will fall. Typically, the interest rate used for reference is the market benchmark interest rate for the appropriate maturity. Prime lending rate is the commonly used benchmark for the Rand. CFIs that have investments in the CFI retail bond, might be affected by increasing or decreasing returns on their investments
- b) *Equity risk*: - If the price of equities listed and traded on the major stock exchanges changes, then the CFI balance sheet may be affected by a fall in the value of its equities or bonds. Even if equity investment assets carry a capital guarantee, there is still a risk. This is because if they don't increase in value as much as had been expected the overall financial performance of the CFI will be less than expected.
- c) *Currency risk*: - Changes in the exchange rate of currencies can lead to a loss in the value of investments denominated in foreign currencies.

CFIs are not expected to have significant equity and currency risk on their balance sheets without prior approval by the Supervisor.

This Guideline is issued by the Co-operative Banks Development Agency Supervision Unit ("the Supervisors") pursuant to section 45 of the Co-operative Banks Act No 40 of 2007 ("Act") and the Exemption Notice No 404 and comes into effect 1 April, 2014.

This Guideline establishes the standards of the Supervisors with respect to management by CFIs of market risk.

Each CFI is required to implement a policy that addresses the following:

**1. Authorized types, limits and concentration of investments, other financial instruments, and assets. These should include:**

1.1 Appropriate limits on:

1.1.1 Investments in a single financial institution and their connected institutions, with exceptions for deposits in banks registered under the Banks Act.

1.1.2 Concentration limits in a single financial institution e.g. in bonds, maximum cash and fix deposit

**2. Defined and prudent levels of decision-making authority. These should include:**

2.1 Delegated decision-making authority, including approval authority for:

2.1.1 The purchase and redemption of investments;

2.1.2 Large or complex transactions.

**3. Identifying, measuring, providing for and recording market impairments.**

**This should include:**

3.1 Process to monitor and report the value and yields of investments, the value or return of which can fluctuate, including:

3.1.1 Deteriorating investment positions;

3.1.2 Accounting for changes in aggregate market exposures

3.1.3 Procedure for responding to investments that exceed tolerance levels. This should tie into liquidity and other risk policies as have an impact and could be an indicator of trouble for a particular investment.