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Full Length Research Paper

Interest rate pass-through to bank mortgage and participation bond rates in South Africa: Evidence from ARDL and FMLS models

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Abstract

This paper examines the degree of pass-through and the adjustment speed of the bank rate and partB rate in response to changes in the repo and treasury bill rates in South Africa for the period 1998M4 to 2011M1. The repo rate is the policy rate while the treasury bill rate (TBR) represents money market rates. We employ the ARDL and FMLS estimators to test for co-integration over the whole sample period 1998M4 to 2011M1. From the ARDL model, long-run repo rates pass-through to bank rates range from 0.83 to 1.21. Estimates higher than unity indicate the overshooting of bank rates. Long-run TBR pass-through to participation mortgage bond rates lie between 1.00 and 1.29. A striking result is that both repo rates and TBR show overshooting in bankrates and partB rates. This phenomenon is akin to overshooting in exchange rates due to price increases. Our repo results to bankrates are similar to Aziakpono et al. (2007) and De Angelis et al. (2005). To the author's knowledge, there are no studies that have examined repo and TBR pass-through to participation mortgage bond rates in South Africa.

Key words: Interest rate pass-through, monetary policy, incomplete pass-through, ARDL, FMLS, bankrates, partB rates, overshooting, TBR, repo rates.

Abbreviation

JEL Classification: E43, F41, E52, E5

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