



## **Is A Strong Rand Good?**

A strong Rand creates a general good feeling about ourselves, which might just be cloud cuckoo land if we analyse the effect of the strong currency on our economy.

The Rand weakened against the US Dollar and the British Pound Sterling by approximately 80% for the ten years from 1986 to 1996. To be very unscientific we could say in the region of 8 percent per year. From 1996 to 2001 it weakened against these same currencies at approximately 100% over five years. That means that the trend has more than doubled over the next five years. In 2001 it crashed in six months by 72%! It took the next sixteen months up till now to recover fully from the crash of 2001.

Everybody accepted the trend of the eighties to early nineties as fate. Everybody accepted the accelerated trend of the late nineties as the effect of the new South Africa incorporating the developing component for the first time in the country's active economy. But doom and gloom hit us when our currency fell out of bed in 2001 just as euphoria has set in now that the Rand has recovered.

What keeps the Rand up there at the moment? Two factors. The one is a technical recovery. Whenever the market crash it always recover technically and consolidate to fall back on the previous trend. The second is the Reserve Bank's remedy to increase interest rates.

The effect of the higher interest rate on the currency is that it attracts foreign investors from their low interest rate environments. But the foreigners do not make fixed long term investments. They invest in short term interest bearing investments from which they can flee overnight when interest rates drop.

So what does the Reserve Bank do? They keep the repo rate artificially high. How do we know it is artificial? By looking at the long term bond market which is determined by market forces and not the whims of politicians. To keep the interest rate high it artificially support the currency which create the impression that foreigners have faith in the country and therefore invest here. This makes for cloud cuckoo land.

What is the effect on the economy? Our exporters bleed to death! It stimulates inflation because South Africans are borrowers not investors. And cloud cuckoo land is cloud cuckoo land because foreign investors do not invest in factories to create jobs and to stimulate the economy. They invest in short term liquid interest bearing investments and will flee as soon as interest rates drop.

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