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Page: 15

Reserve Bank stands its ground

Rand aligning to 'macroeconomic fundamentals'

Bloomberg, Wiseman Khuzwayo and Reuters

The rand is expected to tumble further as China's economy slows.

PHOTO: BLOOMBERG

THE SA Reserve Bank had no intention to defend the currency given the muted impact of a falling rand on inflation and the benefits it provided to Africa's second-largest economy, governor Lesetja Kganyago said.

The currency's decline was a result of the Chinese slowdown and expected monetary policy normalisation in the US, Kganyago said on Saturday on the sidelines of a Group of Twenty (G20) meeting of central bank governors and finance ministers in Turkey's capital, Ankara.

"There is no amount of central bank involvement that would do anything to stop a currency from aligning to what the macroeconomic fundamentals are," he said.

"We have had a shock to our commodity prices and the currency has depreciated. It just provided a cushion to our export sector."

The rand

The rand tumbled more than 8 percent over the past month on concern that prices for commodities, which account for more than half of the nation's exports, will plunge further as China's economy slows.

While the bank has repeatedly cited a weak currency as the biggest risk to consumer prices, Kganyago played down the feed-through impact, citing the decline in oil prices.

"What we have seen is that with every episode of the rand's depreciation, the pass-through from the depreciation of the currency into the inflation rate had been muted and had been lower," he said.

The rand's depreciation "is also accompanied by the decline in the oil price and the decline in the oil price is disinflationary".

The Reserve Bank raised its benchmark repurchase rate by 25 basis points to 6 percent in July, the first policy move in a year, to help fight inflation that accelerated to 5 percent in July. Kganyago said on August 11 that the current tightening cycle would be moderate.

The oil price decline "gives a fillip" to the economy through lower energy bills as South Africa imported about 70 percent of its crude oil requirements, the governor said.

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The bank might have to cut its economic growth forecast for this year after the economy contracted by an annualised 1.3 percent in the second quarter, he said. The monetary policy committee (MPC) said in July that the economy would grow 2 percent this year and 2.1 percent in 2016.

Meanwhile, the rand extended its decline against the dollar on Friday after US jobs data showed that the unemployment rate had dropped to a near seven-and-half-year low of 5.1 percent, the lowest since April 2008.

The Federal Reserve considers this level to be full employment, potentially bolstering the case for an interest rate increase next week.

In response, emerging market stocks and currencies headed for weekly declines and developing nations' assets extended losses on Friday.

"The option for a September rate hike remains on the table and emerging market assets will remain under pressure," Société Générale strategist Bernd Berg said.

"The unemployment rate at 5.1 percent puts a bit of pressure on the Fed to explain why they need to wait more with such a low number. I expect assets to sell off further ahead of the Fed meeting."

The rand weakened by 2.3 percent against the dollar to R13.8551 late on Friday, the second weakest performance for the local currency and compared with August 24 when it fell to a record low of R14.0682 against the dollar.

"The problem for emerging market currencies is that the Fed, if it does hike, will not be doing so against a backdrop of particularly impressive growth," Dominic Bunning, a senior foreign exchange strategist at HSBC Bank, said.

With a wide current account deficit, weak economic growth and a slowdown in China, South Africa's economy was more vulnerable to these volatile capital funding shifts, he said.

Lee Naisbitt, an analyst at Rand Merchant Bank (RMB), said the rand had convincingly broken out of its long-term upward trend channel and might target the highs seen close to R14 against the dollar.

Ion de Vleeschauwer, the chief dealer at Bidvest Bank, said the rand might breach the R14 per dollar this week.

Need higher rates

Even higher interest rates were needed to arrest the rand's decline, he said. "It's just constant demand for dollars. We need higher interest rates here, and by lots. You need at least 50 basis points or more."

The MPC of the Reserve Bank meets from 18 to 23 September to review interest rates, one week after the Fed.

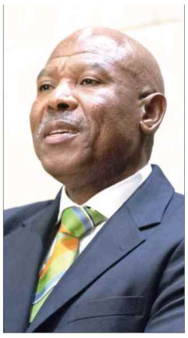
In the latest sign of strain on the local economy, the business confidence index released on Thursday by the SA Chamber of Commerce and Industry showed business sentiment fell to a 16-year low.

The rand fell as much as 1.5 percent against the dollar after the survey was released.

The Standard Bank South Africa purchasing managers' index remained below the 50 level for a third month in August, suggesting a manufacturing contraction.

Annabel Bishop, the chief economist at Investec in South Africa, said the rand remained at risk of further weakness as further first readings on the third quarter industrial production were due this week.

In its September forecast, RMB said the rand had continued to weaken amid deteriorating fundamentals and the risk-off global backdrop.



Reserve Bank Governor Lesetja Kganyago

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