

The rand's sudden dive sparks fears of higher inflation

September 23 2011 at 12:50pm



REUTERS

A London trader watches stocks tumble.

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THE rand hit a more than two-year low against the dollar, sparking fears that the currency may go into freefall, with some economists saying anything could happen to it over the next few days.

The rand was one of the worst-performing currencies yesterday, recovering to R8.24 to the dollar in the afternoon after trading at R8.33 earlier. It was trading at R8.27 to the dollar at 6.45am today.

This was the lowest the currency had traded for in 26 months and was in line with other emerging markets whose currencies were sold off due to persistent anxiety over the euro zone debt crisis.

Bloomberg said the rand was among the worst-performing of 18 emerging-market currencies tracked against the dollar.

The Reserve Bank, which left the repo rate unchanged at 5.5 percent yesterday, said the weaker rand posed a threat to inflation.

Economists said the currency's slump was reminiscent of similar movement in 2001 and 2008.

Then, the rand remained weak for months and consumers were hit hard as the costs of manufacturing, production, imports and transport spiralled.

Yesterday's weakening was put down to the ripple effects of the euro zone crisis and the US Federal Reserve's announcement of a \$400 billion (R3.28 trillion) programme to skew its \$2.85 trillion balance sheet more heavily toward longer-term securities.

Investors started selling emerging market bonds this week, creating the turmoil – but the rand has been weakening against the dollar since the beginning of the month.

A weak rand means an increase in the cost of imported goods. This would hit consumers hard, with food inflation already at 7.5 percent, analysts said. South Africa is already importing maize, a staple food for humans and animals.

A weak rand would also put more pressure on inflation, which is at 5.3 percent and expected to reach 6.6 percent by the end of year. The Reserve Bank inflation target is between 3 percent and 6 percent.

Stanlib economist Xhanti Payi said the rand's weakening had begun last month. At the beginning of August it was trading at R6.70 to the dollar but by the end of the month it was at R6.99.

Payi said this was mainly because the entire world was at risk because of the euro zone debt crisis and the political situation in the US.

If the US went into a double-dip recession it could drag the entire world with it, Payi warned.

The Brazilian real had also suffered significant losses. "Investors are worried so they are selling off and taking their money back to the dollar," he said.

Previous slumps in world currencies were just after the 9/11 terrorist attacks in the US and in 2008, when most countries entered a recession.

Payi said that if Greece defaulted on its debt, there would be a run on banks that would have global consequences.

FNB economist Cees Bruggemans said the markets were adjusting their expectations in terms of growth.

"The Federal Reserve emphasised a significant downsize to growth which the markets had not factored in," Bruggemans said.

He was more cautious in his predictions, saying the rand sell-off might be an over-reaction.

He doubted the US faced a double-dip recession and was convinced the euro zone crisis would be resolved shortly.

Cadiz chief economist Adenaan Hardien said the rand had underperformed all year and been one of the most volatile currencies.

He said a range of currencies, not just the rand, had been sold off.

"No one knows how things will fall, no one will know how far the rand will fall," he said.

Hardien said investors had forgotten how notoriously volatile the rand was and had been lulled into a false sense of security by its recent strength.

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