

36 Dr Abedian's evidence was that there were "pure currency speculators" in the rand to an estimated volume of USD 200 to USD 300 million per day. He said: "I highlight here that there is no way by definition to quantify it, but my discussion with the trade both inside and outside the country is that this volume had grown by September last year to an estimated or guesstimated amount of possibly as high as 300 million dollars per day."¹¹⁵

The experts' conclusions¹¹⁶

(1) Gouws

37 Mr Gouws came to the conclusion that against the background of a steady depreciation of the rand during 2000 and the first half of 2001 most market participants came to the view that the currency was weak and it is likely that they took decisions to help protect themselves against further weakness. There was, therefore, already a weakening bias in the currency by the time the extraordinary confluence of factors and forces started to exert an influence from early September 2001 onwards. Some of those affected the currency via the influence on the current account; most affected the currency via the negative impact on confidence and on expectations about capital flows. The role of these factors became

¹¹⁴ Jammie Expert Bundle 343-345; Abedian, Expert Bundle 260-261

¹¹⁵ Abedian Record 422

magnified after mid October 2001 by a lower level of market liquidity following the Reserve Bank's announcement that foreign exchange control rulings were to be policed more rigorously. Some market participants may have taken advantage of the prevailing circumstances, but the sharp decline of the currency was the result of economic, political, policy and confidence factors and forces that had built up over a number of months. To attribute the fall in the rand to a number of specific transactions would be difficult and perhaps pointless in the light of the magnitude and complexity of developments since early September 2001.¹¹⁷

(2) Stals

38 Dr Stals summed up his views as follows:-

- (1) The South African exchange rate is determined by forces of demand and supply. The system of a managed float is by its nature unstable. Volatile movements in the exchange rate can be expected from time to time.
- (2) The nominal exchange rate of the rand against other currencies will over time depreciate more or less by the inflation differential between South Africa and its major trading partners.

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The evidence of the experts is dealt with in the order in which they gave evidence.

- (3) Globalisation led to an integration of financial markets on a worldwide basis. There has been a big increase in international capital flows. Turnovers in foreign currency markets assumed astronomical dimensions. South Africa participated in those developments and removed or relaxed exchange controls to an important extent. All those developments contributed to a more volatile exchange rate for the rand.
- (4) In the second half of 2001 various adverse external and domestic developments led to a deterioration in the South African balance of payments and therefore to a decline in the supply of foreign exchange.
- (5) Without any official support, shortages developed in the market for foreign exchange with a strong concurrent pressure on the rand to depreciate.
- (6) There was a growing perception in the market that the rand would continue to depreciate. Protective action by importers and expedient conduct by exporters squeezed the market even further. In December 2001 there were signs of panic in the market because of the shortage of liquidity.
- (7) The reduction in the NOFP may have contributed to the woes of the rand. The role of the NOFP in the depreciation of the rand

has, however, been exaggerated in the media and in the market. As long as the Reserve Bank enters into forward foreign exchange cover transactions for South African residents in respect of “firm, ascertained and documented” commitments, increased or declines in the NOFP will be neutral as far as supply and demand conditions are concerned in both the markets for foreign exchange and for domestic rand liquidity.¹¹⁸

(3) Abedian

39 Dr Abedian summed up the “bottom line impact” of the factors analysed in his report and evidence as follows:

- (1) Net demand for the rand had diminished substantially.
- (2) Policy uncertainty and an implicit policy re-think influenced the market.
- (3) A one-way bet on the currency had taken root.
- (4) No obvious defence for the currency was evident.
- (5) Liquidity in the market was diminishing from mid-year on and reached low levels during the fourth quarter of the year.
- (6) Global and environmental factors continued to weigh adversely on the currency.

(7) The market conditions were ripe for a run on the currency.

Dr Abedian identified three possible scenarios for the rapid depreciation of the rand in December 2001:-

- (1) A perfectly legitimate large transaction by one of the major market players might have led to the emergence of a herd mentality resulting in the run on the rand.
- (2) It is technically possible that one may execute a deal fully aware of the full-scale domino effects and one does so in order to benefit via a major deal already in contract. Such a situation was particularly more feasible when the pure speculators were driven out of the market by November 2001.
- (3) There were uncoordinated numerous market transactions that culminated in a self-fulfilling prophecy leading to a severe overshooting in valuation of the currency. Deals of this kind might well have had no motive other than well-considered business logic, yet the impact or outcome was identical to either of scenarios 1 and 2.¹¹⁹

(4) Bruce-Brand

40 Mr Bruce-Brand testified that he was not able to isolate any transactions

¹¹⁹ Abedian Expert Bundle 282, 283

which caused, contributed and/or gave rise to the rapid depreciation of the value of the rand. Furthermore the numerous economic and political factors mentioned by the various witnesses influenced the exchange rate of the rand – which would make the task even more difficult for him.¹²⁰

(5) The Governor

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41.1 The conclusion that the Governor came to was that the exchange rate obviously came under a great deal of pressure in the latter half of 2001. If developments in the balance of payments are taken into account, as well as the other issues mentioned by him, including the fact that market participants would tend to trade according to the view that the rand was vulnerable, thereby adding further pressures to the rand, the depreciation in the value of the rand was not altogether unexpected. Admittedly the severity and the speed of the decline were surprising and of great concern.

41.2 It is the view of the Reserve Bank that the best defence of a currency is prudent macro-economic policies accompanied by structural and micro-economic reforms, where appropriate.

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41.3 The Governor defended the Reserve Bank's role in 2001 by stating:

- given the inflation targeting monetary policy framework under which the Reserve Bank operates, it was not considered appropriate to hike interest rates in defence of the currency;
- it was not considered appropriate to intervene in the forex market to support the value of the rand by means of the forward book;
- on 14 October 2001 it was felt appropriate to enforce existing exchange controls on non-residents to ensure that only legitimate transactions took place in the forex market;
- contained in the statement of 14 October 2001 was a very positive announcement regarding future purchases of foreign exchange to reduce the NOFP;
- in a joint statement issued by the Governor and the Minister of Finance on 21 December 2001 the positive economic fundamentals were reiterated.¹²¹

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(6) Ramos

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42.1 Ms Ramos said that the Government has had to make policy choices in a complex and often unforgiving world. At the centre of the range of policy choices lies the principle that South Africa is an open economy. In that environment it is inevitable that from time to time there will be turbulence. The policy makers must be confident that the policy choices they have made and the good performance experience for the economy of the past five or six years will support the ongoing growth and sustainable development that the South African economy needs.

42.2 The Government has had to ensure that the appropriate macro-economic fundamentals are in place. Far-reaching reforms of the fiscal framework and management of public finances have been undertaken. Monetary policy has been consistent in tackling the distortionary impact of high inflation. Trade reform and financial market development have increased the flow of foreign currency to South Africa. Government's spending has been re-prioritised to

increase spending on social services, which promotes redistribution and provides a safety net against the potential social costs of globalisation.

- 42.3 In an environment of global integration, it is essential for a sound and well regulated financial system to be in place. Government has achieved this through an ongoing financial market reform aimed at keeping South African financial market standards consistent with international practice.
- 42.4 Government has chosen to follow a flexible exchange rate to act as a shock absorber against global developments. Exchange rate adjustments helped cushion the economy from external trade and capital flow shocks, and mitigate the impact of economic contraction, especially in respect of the poor.¹²²
- 42.5 There was no single or dominant cause for the depreciation of the rand. Ms Ramos said: “There were a number of variables at play at the same time and certainly in our attempts to try and understand what was going on, we have been unable to say what caused it was A and not B. It was a complex set of issues not least of which is the confidence that South Africans have in their own country and their own economy and so it has been difficult for us to say that there was one set of issues that led to the exchange rate depreciation that we saw last

¹²²Ramos, National Treasury Bundle, 58-59

year. There were lots of things happening at the same time.”¹²³

The Minister of Finance spoke of a complex set of factors which were at play.¹²⁴

¹²³ Ms Ramos Record 735-6

¹²⁴ Manuel Bundle National Treasury 87