



SA Rand Volatility

July 2006

INTRODUCTION

The Rand recently broke the psychological level of R7 to the US Dollar, and subsequently extended its losses falling to a new two-and-a-half year low of about R7.52 to the Dollar. The Rand is currently at levels of between approximately R7 to R7.30 to the Dollar but is, however, still expected to come under some pressure on concerns about SA's widening current account deficit, which widened to 6.4% of GDP in the first quarter of this year.

PURCHASING POWER PARITY (PPP) VALUATION APPROACH

The PPP valuation approach is arguably the most reliable predictor of currencies over the longer-term (the Rand included). It must be borne in mind, however, that this approach is merely an indication and not a precision tool. In the shorter-term there are a number of factors which have a bearing on the relative value of currencies. The recent sharp sell-off in the Rand against the US Dollar should be viewed in the context of a Rand that was expensive to begin with (at around R6 to the Dollar).



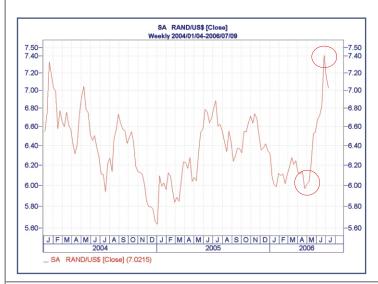
Short-term factors that have undeniably had an impact would include:

- A sharp sell-off in emerging market risk assets on concerns of higher global interest rates;
- Alarger than anticipated current account deficit in SA.

The Rand/Dollar exchange rate has seen a movement of 20%+ in a short time frame. It is quite possible that this is overdone and some consolidation/appreciation follows. However, it is probably fair to say that the favourable factors that drove the currency to overvalued levels have largely played out and a weakening Rand bias is anticipated (relative to PPP) over the medium-term.

OUTLOOK

Assuming the global economy and the commodity cycle remains buoyant over the next 6 months, we would expect the Rand to stabilise at current levels. In the long run, we would expect depreciation of the currency to be roughly in line with inflation differentials which, in essence, is the theoretical underpinning of the PPP approach.



- The Rand reached a two-year high on 23 June 2006, with a closing level of R7.4076 to the US Dollar.
- The Rand was last below R6/\$ on 21 April 2006 at a Level of R5.97/\$.
- The Rand has lost 11.14% for the current year to date.
- The Rand would be the first to suffer if SA was unable to finance the burgeoning current account deficit.

Additional Factors Driving the Rand:

- Surging Oil Price
- Strong Consumer Spending (high propensity to import)
- Inflation

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