

The Investment Analysts Journal

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Die Beleggings- Navorsers Tydskrif

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Inhoud

This issue in brief

An eclectic role for monetary policy

The justification of macro-economic stabilisation policies resides in the belief that governments can and, indeed, should intervene in the economy to smooth out business cycles and, thus, prevent the wastage of resources that results from booms and slumps. However, that belief, while still generally accepted by the conventional wisdom has come in for a good deal of criticism in recent years by neo-classical economists. Dr Johan Cloete, Chief Economist of Barclays National Bank, examines the role of monetary policy against this background with particular regard to its formulation and implementation in South Africa. He discusses, amongst other things, the difficulties of applying a constant money rule in this country and comes to a pessimistic conclusion regarding official efforts permanently to reduce inflation.

Trading in low priced shares: An empirical investigation 1968-1979

The view that low priced shares are more risky than high priced shares is held by many investors in many stock markets and this explains the resistance of some companies to stock splits and capitalisation issues. An investigation of such shares by Messrs Gilbertson, Affleck-Graves and Money suggests that while such a view might have a measure of validity it should not be allowed to obscure the fact that low priced shares often provide a relatively favourable return. Indeed, their research suggests that low priced shares are deserving of more attention than they receive on the JSE.

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A graphical solution to the lease evaluation problem

The growing popularity of lease finance, not least of all because of its tax advantages, has increased the need for effective evaluation techniques. This contribution from Australia develops a mathematical model which, through a graphical presentation, is easy to use. Presentations of the kind employed here are extremely valuable in sensitivity analysis and lend themselves to adaptations suited to the special requirements of particular users.

The puzzle of the two markets

Can two markets, both of which are efficient, react in different ways to the same information? This is an interesting question and is examined in this study of the comparative performance of gold share prices and the price of gold between March 1976 and August 1980. While there are factors that affect gold shares prices which have no direct bearing on the bullion market, one might expect such prices to reflect fairly accurately gold price changes from time to time. However, this has not always been so and Mr G. D. I. Barr of the Department of Mathematical Statistics at Cape Town University investigates why. He concludes that it has to do with the process through which expectations in the stock market are formulated.

The effect of taxation on earnings per share

The importance of taxation to the evaluation of ordinary shares can hardly be over-estimated for it is an expense of magnitude which has to be met before any payment of dividends can be made. To the extent, too, that taxation absorbs available cash resources these are diminished and may have to be supplemented if new capital projects are to be undertaken. Taxation also has a direct bearing on the cost of equity capital relative to that of loan capital and, therefore, is important to the determination of capital structure. This is the tenth article in our investment basics series and deals with essential tax issues. Mr I. J. Poluta is the tax consultant of JCI.

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Nineteenth issue

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*"We are determined to carry the policy of 'consolidation and adjustment' to its logical conclusion. This means exercising tight control over government spending, banking liquidity and the money supply. It also means permitting financial markets to tighten further if necessary and accepting **realistic*** interest rates. The lower average gold price and ... other adverse external developments ... are facts of life which cannot be ignored or neutralised by money creation or fiscal manipulation. We can argue about the appropriate **methods** of adjustment, weighing up their different costs and benefits. But the inevitability of adjustment must be accepted."*

Dr Gerhard de Kock
Governor of S.A. Reserve Bank
9 March 1982

*Our bold italics

The key word in the above statement is "realistic". For interest rates to be realistic they have to be politically acceptable, but equally, they cannot be realistic if they are not economically effective. Do we now have a level of interest rates in South Africa that will be effective in hastening the process of adjustment to which Dr De Kock refers? This is not a question that an editorial of this kind either can or should attempt to answer. Suffice it to observe that while short-term interest rates in South Africa at present are historically very high and in nominal terms are also higher than short-term interest rates in the US, Britain, Germany or Japan, they are neither extraordinarily high nor higher than the rates in these countries in real terms. To the extent to which it is real interest rates that govern the movement of physical resources, this must invite doubt as to whether interest rates here are yet high enough. However, it would be wrong to be dogmatic about that. What is real in the way of investment returns must depend, ultimately, on what happens to inflation, and investment decisions, therefore, inevitably hinge on expectations. In the final reckoning, the rate of interest is a price, and for any price to be effective in balancing the opposing forces of demand and supply, it must be left to find its own level. When prices of any kind, but especially interest rates, are ineffective in this regard, it is usually so because they have been interfered with. The merit of recent changes in South African financial markets is that they have taken us further along the road of deregulation though not far enough yet to attain the destination now generally acknowledged as being desirable by both the Government and the business community.

Although the prices of industrial shares have declined and are today about 17,5 per cent, on average, below their peak, they have not fallen quite to the extent that might have been expected considering the level to which nominal interest rates have risen or to which the gold price has fallen. In historical terms both the rise in interest rates and the fall in the gold price (two events not unrelated to one another), have been extraordinary and will inevitably have, in time, a material impact on the real economy. It is that impact to which Dr De Kock has referred. Clearly,

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Negentiende uitgawe

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*"Ons is vasberade om die beleid van 'konsolidasie en aanpassing' tot die logiese afloop daarvan deur te voer. Dit beteken dat streng beheer oor staatsbesteding, banklikwiditeit en die geldvoorraad uitgeoefen sal moet word. Dit beteken ook dat finansiële markte toegelaat sal moet word om nog meer gespanne te word as dit nodig is en om **realisties*** rentekoerse te aanvaar. Die laer gemiddelde goudprys en ... ander nadelige eksterne ontwikkelings ... is lewensfeite wat nie verontagsaam of deur geldskepping of fiskale manipulasie geneutraliseer kan word nie. Ons kan redeneer oor die toepaslike **aanpassingsmetodes**, en hulle onderskeie koste en voordele teen mekaar opweeg. Maar die onafwendbaarheid van aanpassing moet aanvaar word."*

Dr Gerhard de Kock
President van die S.A. Reserwebank
9 Maart 1982

*Ons vetkursivering

Die sleutelwoord in bostaande verklaring is "realisties". Vir rentekoerse om realisties te wees, moet dit polities aanvaarbaar wees, maar terselfdertyd kan dit nie realisties wees as dit nie ekonomies doeltreffend is nie. Het ons nou 'n rentekoersepeil in Suid-Afrika wat doeltreffend sal wees vir die bespoediging van die aanpassingsproses waarna dr De Kock verwys? Dit is nie 'n vraag wat 'n hoofartikel soos dié kan of moet poog om te beantwoord nie. Dit is voldoende om op te merk dat, hoewel korttermynrentekoerse in Suid-Afrika tans histories baie hoog is en nominaal gestel ook hoër is as korttermynrentekoerse in die VSA, Brittanje, Duitsland of Japan, dit nóg buitengewoon hoog nóg reël gesproke hoër is as die koerse in dié lande. Vir sover dit reële rentekoerse is wat die beweging van fisiese hulpmiddele reël, laat dit die twyfel ontstaan of ons rentekoerse inderdaad hoog genoeg is. Dit sal egter verkeerd wees om dogmaties te wees daaroor. Wat reël is in die sin van rendemente op beleggings moet uiteindelik afhang van wat met inflasie gebeur, en beleggingsbesluite staan dus noodwendig in verband met verwagtinge. Op slot van rekening is die rentekoers 'n prys, en vir enige prys om van die strydige magte van vraag en aanbod op doeltreffende wyse te balanseer, moet dit toegelaat word om sy eie plek te vind. Wanneer pryse van enige aard, maar veral rentekoerse, in dié verband nie doeltreffend is nie, is dit gewoonlik die geval omdat daar ingegryp is. Die verdienstelikheid van onlangse veranderinge in Suid-Afrikaanse finansiële markte is dat dit ons verder gevoer het op die pad weg van regulering, hoewel nog nie ver genoeg om die bestemming te bereik wat nou alom deur die Regering sowel as die sakegemeenskap as wenslik erken word nie.

Hoewel die pryse van nywerheidsaandele gedaal het en vandag gemiddeld ongeveer 17,5 persent laer as hulle hoogtepunt is, het hulle nie heeltemal soveel gedaal as wat verwag kon word as die peil waartoe nominale rentekoerse gestyg het of waartoe die goudprys gedaal het in ag geneem word nie. Histories gesproke was die styging in rentekoerse sowel as die daling in die goudprys (twee

what concerns him is that the level of economic activity in the domestic economy should be brought more into line with the level of economic activity in the world economy so as to avoid an aggravation of the country's already serious balance of payments problem. It is evident that the adjustment process is taking time, perhaps more time than is desirable, and has been delayed in part by the action the Reserve Bank has itself taken to ease the cash shortage that the external deficit has caused. Public officials, like Dr De Kock, cannot escape the political pressures that in any democratic country are brought to bear in the formulation of policy. Even in the US, where the Federal Reserve Board enjoys a greater degree of independence than does our Reserve Bank, that is so. They cannot, therefore, enjoy compromising what they know needs to be done when compromising may put at risk the attainment of objectives their office demands that they commit themselves to publically and unambiguously. It is a sad fact, but one for which Dr De Kock cannot be held personally responsible, that his term of office as Governor has coincided with one of the largest ever increases in the country's money supply and the largest ever decline in the external value of the rand. Who can doubt that in time this will feed back, and in an adverse way, to affect the rand's internal value. Inflation in South Africa is currently in excess of 15 per cent, and rising. In the US, West Germany and Japan it is closer to 5 per cent, and falling. Such a disparity in rates cannot persist for long without something happening. We have here all the unfortunate ingredients of a circle which is not only vicious but also unrelenting.

Our comments concerning the general desirability of a free determination of prices, particularly of interest rates and exchange rates, should not be read to mean that all attempts at macro-economic stabilization must needs be misguided. No doubt those occasions exist where changes of policy are necessary in order to alter the direction in which normal competitive forces are pushing the economy. However, given intervention, the onus must rest on governments to show that it has indeed been beneficial. There is a growing body of opinion in the US and Britain that intervention in these two countries in the post-war period has not been promoting of real growth in the long run but instead has directly contributed to the enigmatic coincidence of rising unemployment and inflation. If financial markets are efficient, as much of the evidence suggests, interventionist policies can never really succeed because the monetary and fiscal authorities do not have better information about the future than do private sector agents and cannot, therefore, prevent policy actions being anticipated and their effects neutralised. The corollary of this must be that it is only in a world of inefficient markets that such policies can be justified. Official efforts, thus, might better be spent promoting efficiency especially through the removal of controls, the encouragement of competition and the provision of information (including information about policy objectives and the means intended to be employed in their realisation), that such efficiency requires. Unfortunately, one of the factors which has worked against the efficient adjustment of the South African economy to a changed external situation over the past 15 to 18 months has been public confusion about official policy. While some of the actions of the authorities (e.g. encouraging off-shore borrowing, financing the public sector via Reserve Bank credit and devaluing the rand) have been easing of the liquidity shortage and encouraging of the business community, other actions (e.g. restricting current departmental spending, increasing taxes and raising interest rates) have been discouraging. Oscillation between conflicting policy actions is not helpful to public

gebeure wat nie onverwagt is nie) buitengewoon en sal dit onvermydelik mettertyd 'n wesentlike impak op die reële ekonomie hê. Dit is dié impak waarna dr De Kock verwys het. Dit is duidelik dat hy besorg is oor die feit dat die peil van ekonomiese bedrywigheid in die binnelandse ekonomie in nouer ooreenstemming gebring moet word met die peil van ekonomiese bedrywigheid in die wêreld ekonomie om 'n verergering van die land se reeds ernstige getalingsbalansprobleem te vermy. Die aanpassingsproses duur klaarblyklik lank, miskien langer as wat wenslik is, en is gedeeltelik vertraag deur die stappe wat die Reserwebank self gedoen het om die kontanttekort wat die buitelandse tekort meegebring het te verlig. Owerheidsamptenare, soos dr De Kock, kan nie die politieke druk vryspring wat in enige demokratiese land op beleidsformulering uitgeoefen word nie. Selfs in die VSA, waar die Federale Reserwebank 'n groter mate van onafhanklikheid as ons Reserwebank geniet, is dit die geval. Hulle kan dus nie die maklike uitweg van 'n kompromis kies nie, want dit kan die doelstellings waartoe hulle uit hoofde van hulle amp openlik en onomwonde verbonde is in gevaar stel. Dit is 'n ongelukkige feit, maar een waarvoor dr De Kock nie persoonlik verantwoordelik gehou kan word nie, dat sy ampstermyn as President saamgeval het met een van die grootste toenames ooit in die land se geldvoorraad en die grootste afname ooit in die buitewaarde van die rand. Niemand kan daaraan twyfel dat dit mettertyd 'n terugwerkende uitwerking op die binnewaarde van die rand sal hê nie, en wel op nadelige wyse. Inflasie in Suid-Afrika is tans meer as 15 persent, en dit styg steeds. In die VSA, Wes-Duitsland en Japan is dit nader aan 5 persent, en dit neem af. Dié verskil in koerse kan nie lank voortduur sonder dat iets gebeur nie. Ons het hier al die ongelukkige bestanddele van 'n kringloop wat nie net boos is nie, maar ook onverbidlik.

Ons opmerkings met betrekking tot die algemene wenslikheid van 'n vrye prysvasstelling, veral ten opsigte van rentekoerse en wisselkoerse, moet nie vertolk word as 'n uitspraak dat alle pogings om makro-ekonomiese stabiliteit te bewerkstellig noodwendig ombesone is nie. Daar bestaan ongetwyfeld wel geleenthede waar beleidsveranderinge nodig is om die rigting te wysig waarin normale mededingende magte die ekonomie dwing. As daar wel ingegryp word, moet die onus egter op regerings berus om aan te toon dat dit inderdaad voordelig was. In die VSA en Brittanje word die mening al hoe meer gehuldig dat ingryping in dié twee lande in die naoorlogse tydperk nie op die lang duur reële groei bevorder het nie, maar in plaas daarvan regstreeks bygedra het tot die raaiselagtige sameval van toenemende werkloosheid en stygende inflasie. As finansiële markte doeltreffend is, soos baie van die bewyse ook aandui, kan 'n beleid van ingryping nooit werklik slaag nie omdat die monetêre en belastingowerheid nie oor beter toekomsinligting as die privaatsektoragente beskik nie en dus nie kan voorkom dat beleidsoptrede voorsien en die uitwerkings daarvan geneutraliseer word nie. Die logiese afleiding is dat dit net in 'n wêreld van ondoeltreffende markte is dat dié soort beleid geregverdig kan word. Pogings van ampsweë moet dus eerder ingestel wees op die bevordering van doeltreffendheid, veral deur middel van die verwydering van beheer, die aanmoediging van mededinging en die verstrekking van inligting (met inbegrip van inligting oor beleidsdoelstellings en die middele wat aangewend gaan word om dit te realiseer), wat noodsaaklik is vir doeltreffendheid. Ongelukkig is een van die faktore wat die doeltreffende aanpassing van die Suid-Afrikaanse ekonomie by 'n veranderde buitelandse situasie oor die afgelope 15 tot 18 maande teëgewerk het, verwarring by die publiek aangaande amptelike beleid. Hoewel sommige

understanding or persuasive that the authorities know their own mind but suggestive rather of fine tuning techniques which elsewhere have been fairly thoroughly discredited.

The editor

van die owerheidstappe (bv. die aanmoediging van aflandige lening, die finansiering van die owerheidsektor deur middel van Reserwebankkrediet en die devaluasie van die rand) die verligting van die likwiditeitskort en die aansporing van die sakegemeenskap was, was ander stappe (bv. die inperking van huidige departementele besteding en die verhoging van belastings en rentekoerse) ontmoedigend. Weifeling tussen strydige beleidstappe gaan nie begrip aan die kant van die publiek bevorder nie en ook nie die publiek oorreed dat die owerheid doelgerig optree nie, maar skep eerder die indruk van fyn verstellingstegnieke wat elders geheel en al in onguns geraak het.

Die redakteur