

The
Investment
Analysts
Journal

Number 30, November 1987

Die
Beleggings-
ontleiders
Tydskrif

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Inhoud

This issue in brief

Estimating the market risk premium on The Johannesburg Stock Exchange using ex post and ex ante models

This paper by Favish and Affleck-Graves examines the possibilities of developing quarterly risk premia forecasts through the use of logical statistical and mathematical procedures. However, it is also concerned with an evaluation of such forecasts in terms of their practical relevance to financial managers. Two main approaches to the calculation of risk premia can be identified: those based on "ex post" returns, and those based on "ex ante" estimated returns. The development by Sharpe of the CAPM had a major impact on the popularising of forward looking approaches to the matter and it is largely with the CAPM that the article deals. In discussing the results of research specifically concerned with South Africa, it provides much that is useful to managers in a local context.

Market timing and the JSE

The timing of investment or disinvestment action can be critical to portfolio management. But is it possible to identify major changes in share or stock price time series in an efficient market? This is an old question which has long been the centre of dispute. To it needs to be added an additional question concerning the identification of turning points even in a market where efficiency is sub-optimal or below average. Both these questions are considered in this article by Professor Colin Firer, Mike Ward and Frank Teeuwisse. Their conclusions will be of interest to academics and professionals alike.

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Anatomy of the financial rand

Controversy continues to surround the financial rand. The De Kock Commission recommended that it be abolished, and for a short while, between 1983 and 1985, it was. But the heavy capital outflows from South Africa prior to August of the latter year and the threat that this outflow would increase as a result of action taken by foreign banks to call in their maturing short-term credits, compelled the authorities to reintroduce the financial rand system. Has its reapplication been to SA's advantage? What are the possibilities of it finally being scrapped? How would its removal affect the flow of new capital to or from SA? These are some of the questions dealt with by Professor Hamblin in this useful analysis of SA's unique financial currency.

Investment basics XXI – Options trading in the gilt-market

Part 1 – A background to the market

This article by David Bullard is the first in a new Investment Basics series on options trading in the gilt-market. It sets the scene and will be followed by two further articles which will deal with the technicalities and arithmetic of such trading in the May and November 1988 issues of the Journal.

The Investment Analysts Journal

Thirtieth issue
November 1987

Last month's dramatic collapse of world stock markets has all the flavour of the crash that occurred fifty-nine years ago on Wall Street. Then, the stock market decline led to a general economic contraction and the concern now is that something similar could happen with grave consequences for South Africa. It is also worth recalling that the October 1929 stock market crash was not followed immediately by the Great Depression. It was necessary to wait for nearly a year for the banking crisis which really marked the depression's beginning. Indeed, as Milton Friedman has noted, had it not been for the banking crisis, the depression, as we recall it, might not have happened at all. And we know enough about the dynamics of modern industrial economics today to avoid falling into the trap policy-makers fell into in the early 1930s. Instead of easing monetary policy immediately to offset the recessionary effects of the share price drop and providing the liquidity the banking system needed to remain stable, the opposite was done with terrible consequences. Not only was a recession converted into a depression, but the ground was laid for the emergence to power of Hitler in Germany and thus, also, for World War II.

Although circumstances today are very different from what they were nearly sixty years ago, it might be too complacent for us to assume that our improved economic understanding is sufficient to ensure that another major world economic contraction will be avoided. Economists in the 1930s thought they were well equipped by the then prevailing theory to deal with practical problems, just as economists today think they too are equipped. It is of the nature of the problem that it is only *ex post facto* that it can become evident that a prevailing theory has lost its practical relevance as a result of structural change in the real world. As Keynes was to point out, the world of classical economic hypothesising had been left behind by the major industrial changes that had occurred as the nineteenth century drew to a close and the twentieth century got underway. By the end of the 1920s, the models of perfect competition on which too much of policy thinking still rested had almost completely lost their relevance. In the place of the competitive economy characterised by small operating units had emerged the economy of the modern industrial state and monopolistic competition.

There can be little doubt that major structural changes have occurred in the world economy since the Bretton Woods agreement of 1944 which set in place the present world financial system. And the system we have is still the system of Bretton Woods despite the scrapping of the dollar's gold convertibility in August 1971 and the eventual abandonment of fixed exchange rates. This is so because the central feature of Bretton Woods was not the gold exchange standard or even the fixing of currency relationships. It was the central role of the US as world banker. This continues and as long as it does, Bretton Woods will be with us.

At Bretton Woods, Keynes had proposed that a world central bank be established to provide the supply of the

Die Beleggingsontleders Tydskrif

Dertigste uitgawe
November 1987

Verlede maand se dramatiese ineenstorting van die wêreld-aandelemarkte het in 'n groot mate ooreengestem met die val wat nege-en-vyftig jaar gelede op Wallstraat plaasgevind het. Die aandelemark-afname het toe gelei tot 'n algemene ekonomiese inkrimping, en daar word nou gevrees dat iets soortgelyks met sombere gevolge vir Suid-Afrika kan gebeur. Dit is ook noemenswaardig dat die Groot Depressie nie onmiddellik op die Oktober 1929-aandelemark-ineenstorting gevolg het nie. Bykans 'n jaar het verstryk voordat die bankwesekrisis beleef is wat in werklikheid die begin van die depressie bestem het. Soos Milton Friedman trouens opgemerk het, as dit nie was vir die bankwesekrisis nie, sou die depressie soos ons dit onthou, dalk glad nie plaasgevind het nie. Ons weet ook genoeg van die bewegingsleer van hedendaagse industriële ekonomie om nie in dieselfde strik te beland as die beleidmakers in die vroeë 1930s nie. In plaas daarvan om monetêre beleid onmiddellik te verslap om die resessionalistiese uitwerking van die aandeleprys-daling te neutraliseer, en die likiditeit te verskaf wat die bankwesestelsel nodig gehad het om bestendig te bly, is die teenoorgestelde met vreesaanjaende gevolge gedoen. Die resessie is nie alleen in 'n depressie omskep nie, maar die grondslag is in Duitsland gelê vir Hitler se magsoorname, en derhalwe ook die Tweede Wêreldoorlog.

Alhoewel omstandighede vandag heelwat anders daar uitsien as bykans sestig jaar gelede, is dit dalk oorgerus van ons om te aanvaar dat ons verbeterde ekonomiese begrip toereikend is om nog 'n wêreld ekonomiese inkrimping te vermy. Ekonomie van die 1930s het gemeen dat hulle deur die toe heersende teorie goed toegerus was om praktiese probleme te hanteer, net soos ekonomie tans ook meen dat hulle toegerus is. Weens die aard van die probleem blyk dit slegs van agterna gesien, dat 'n heersende teorie sy praktiese verband verloor het as gevolg van strukturele veranderinge in 'n reële wêreld. Soos Keynes uitgewys het, is die wêreld van klassieke ekonomiese veronderstelling agterweë gelaat deur die grootskaalse nywerheidsveranderinge wat plaasgevind het namate die negentiende eeu ten einde geloop, en die twintigste eeu op dreef gekom het. Teen die einde van die 1920s, het die modelle van volmaakte mededinging waarop té veel van ons beleidsdenke steeds gerus het, bykans geheel en al hulle toepaslikheid verloor. In plaas van die mededingende ekonomie wat deur klein bedryfseenhede gekenmerk word, het die ekonomie van die moderne nywerheidsstaat en monopolistiese mededinging verrys.

Daar bestaan min twyfel dat grootskaalse strukturele veranderinge sedert die Bretton Woods-ooreenkoms van 1944 in die wêreld-ekonomie plaasgevind het wat die huidige wêreld-finansiële stelsel geskik het. Die stelsel wat ons het, is steeds die stelsel van Bretton Woods, ongeag die sloping van die dollar se goud-omsetbaarheid in Augustus 1971, en die uiteindelijke afstanddoening van vaste wisselkoerse. Dit is so aangesien die sentrale kenmerk van Bretton Woods nie die standaard van die goud-wisselkoers of selfs die vasstelling van valutaverhouding was nie. Dit was die sentrale rol van die VSA as wêreldbankier. Dit duur voort, en solank dit die geval is, sal Bretton Woods met ons wees.

world's monetary needs. This idea was rejected in favour of the plan put forward by Harry White, the American chief negotiator. White's plan led to the establishment of the IMF, but the IMF was never intended to be a central bank. The task of providing additional world liquidity was left to the US through the running by that country of a deficit on the current account of its balance of payments.

As long as the dollar was a scarce currency, and it continued to be so until the middle 1950s, all was well. Problems, however, began to emerge as soon as non-resident claims against the US gold reserve rose to equality with the reserve level at a given gold valuation. The problem today is that the gold price would have to be increased to around \$3 500 an ounce merely to equate the US gold reserve with the country's short-term foreign liabilities. Clearly, there can be no going back to the position that existed at the beginning of the post-war period even through the contrivance of a major increase in the official price of gold.

But if there is to be no going back, in what direction are we now headed? That is the critical question. And it is because even the G7 countries seem not to have an answer to it, that the markets cracked last month. It is going to require more than mere reassuring statements by the world's leading industrial nations to prevent another market crack either in 1988 or later. A US BoP adjustment would put off the evil day, but the fundamental problem, associated with the US's central banking role in a vastly changed world economic system, even then, would remain. It is this role which has to be changed if a new more enduring global financial order is to be established.

The editor

By Bretton Woods het Keynes aan die hand gedoen dat 'n wêreld sentrale bank gestig word om in die monetêre behoeftes van die wêreld te voldoen. Hierdie idee is verwerp ten gunste van die plan wat deur Harry White, die Amerikaanse hoofbedinger voorgestel is. White se plan het tot die stigting van die IMF gelei, maar dit was nooit die voornemen dat die IMF 'n sentrale bank moet wees nie. Die taak om bykomende wêreld-likiditeit te voorsien is aan die VSA oorgelaat deur dié land se bedryf van 'n tekort op die lopende rekening van sy betalingsbalans.

Vir solank as wat die dollar 'n skaars geldeenheid was, wat tot die middel van 1950 die geval was, was alles in orde. Probleme het egter begin ontstaan so gou as wat nie-inwonerseise teen die VSA-goudreserwe op voet van gelykheid met 'n gegewe goudwaardasie gestyg het. Die probleem tans, is dat die goudprys na ongeveer 3 500 dollars per ons verhoog moet word om die VSA-goudreserwe bloot met die land se korttermyn buitelandse laste gelyk te stel. Daar kan duidelik nie teruggekeer word na die posisie wat aan die begin van die vooroorlogse tydperk geheers het nie, selfs nie onder die dekmantel van 'n grootskeepse verhoging in die amptelike goudprys nie.

Maar as daar nie teruggekeer kan word nie, waarheen dan? Dit is die deurslaggewende vraag. Dit is juis omdat die G7-lande nie hierop 'n antwoord het nie, dat die markte verlede maand ineengestort het. Dit gaan meer as bloot gerusstellende verklarings deur die wêreld se leidende industriële volke verg om nog 'n mark-ineenstorting in 1988 óf later te verhoed. 'n VSA-betalingsbalansaanpassing sal die oordeelsdag uitstel, maar die grondliggende probleem, gepaard met die VSA se sentrale bankweserol in 'n grootliks veranderde wêreld-ekonomiese stelsel, sal selfs dan steeds bly staan. Dit is hierdie rol wat vernader moet word indien 'n blywender globale finansiële orde tot stand gebring wil word.

Die redakteur