SOUTH AFRICAN RESERVE BANK

PRESS STATEMENT

18 July 2024

STATEMENT OF THE MONETARY POLICY COMMITTEE

Issued by Lesetja Kganyago, Governor of the South African Reserve Bank

As we move into the second half of the year, global inflation continues to ease. The very rapid price increases of 2022 and 2023 have receded. However, inflation in most economies has yet to stabilise in line with targets. For example, in June, consumer price inflation was 3% in the United States, and 2.5% in the euro area, still above those economies' 2% targets. Services and wage price inflation has proven stubborn, underpinned by resilient economic activity and low unemployment rates across major economies.

Clearly, the battle against inflation is not yet won, and for this reason, global interest rates remain elevated.

At the same time, there has been some policy divergence, which reflects different country circumstances.

Since our last meeting, policy rates were lowered in Canada, Switzerland and the euro area, but kept unchanged in the United States, the United Kingdom, and Japan. Among emerging markets, countries that have lowered inflation more, especially in Latin America, have been able to cut policy rates more. A concern for central banks, however, is that lower inflation outcomes have not always been sustained.[1]

Turning to South Africa, economic performance in the first half of the year was disappointing. The economy contracted slightly in the first quarter, by 0.1%, and recent

[1] For example, between April and May, Euro area inflation rose to 2.6% from 2.5%. In Brazil, inflation increased to 4.2% in June from 3.9% in May.

data, including last week's mining and manufacturing numbers, have caused us to trim our second quarter growth estimate modestly, to 0.6%.[2] Over the medium term, we expect somewhat faster growth, supported by a more reliable electricity supply and improving logistics, among other factors.[3] Our revised growth projections nonetheless remain below longer-run historical averages, of about 2%. The risks to this forecast are assessed as broadly balanced, with ample scope for structural reforms to lift growth further over the medium term.

On the inflation front, the most recent headline print, for May, was 5.2%, unchanged from April and still in the top half of our target range. The outlook, however, has improved somewhat. Headline consumer price inflation for this year is now projected at 4.9%, compared to 5.1% at the previous meeting.[4] Over the next few quarters, headline is expected to dip below the 4.5% midpoint, mainly because of fuel and food prices. This outlook is supported by the stronger rand.[5] The implied starting point for our forecast is now at R18.35 to the US dollar. Over the medium term, we continue to see inflation stabilising at 4.5%, with core inflation remaining close to this midpoint objective throughout.[6]

For inflation expectations, the latest survey results show average expectations at 5% next year and 4.9% two years ahead, still uncomfortably above the SARB's 4.5% objective, and above our own inflation forecasts. However, all categories of respondents lowered their inflation expectations from the previous survey.[7] We anticipate further progress as inflation slows, helping to re-anchor expectations firmly at 4.5%.[8]

While the forecast has improved, the balance of risks is assessed to the upside.

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[2] The previous projection was for growth of 0.7%

[3] The GDP impact of loadshedding has been reduced to -0.2pp, from an estimated -0.5pp in the May forecast. It is -0.1pp for 2025 (compared with -0.2 previously), and 0pp for 2026 (-0.04pp previously). This contrasts with an estimated -1.5pp for 2023.

[4] Headline is expected to average 4.8% in 2024Q3 and 4.3% in 2024Q4

[5] The implied starting point was R18.60 in the May forecast.

[6] Core averages 4.6% for 2024, 4.4% for 2025 and 4.5% for 2026

[7] Market-based measures of inflation expectations have similar dynamics. These break-even rates have declined recently, but remain generally above the midpoint. Shorter-term expectations (5 years) are at 4.6%; longer-term (10 year) expectations are at 5.7%

[8] The QPM projection for 2-year ahead inflation expectations stabilizes at 4.5% by 2025Q1.

Against this backdrop, the MPC decided to keep the repo rate unchanged at 8.25%. Four members preferred an unchanged stance, and two preferred a reduction of 25 basis points.

In discussing the stance, MPC members agreed that restrictive policy remains appropriate to stabilise inflation at 4.5%. The committee assessed that an unchanged stance remained appropriate, given the inflation risks. Some members, however, were of the view that the inflation outlook had improved enough to reduce the degree of restrictiveness.

Global interest rates remain high, especially in the United States, and rates may stay higher for even longer than markets currently anticipate. This presents risks to the currency outlook.

Domestically, inflation expectations do not yet reflect the 4.5% midpoint objective over the medium term. While expectations are moving in the right direction, they continue to show the impact of the recent inflation surge.

We remain concerned about administered prices. We have had to mark up electricity inflation for this forecast round, even as other categories shifted lower.

Services price inflation also remains uncomfortably above the mid-point.

The forecast continues to see rates easing into more neutral territory by next year. As before, the rate path from the Quarterly Projection Model remains a broad policy guide, changing from meeting to meeting.

Decisions of the MPC will continue to be data dependent, and sensitive to the balance of risks to the outlook.

We are committed to stabilising inflation at the mid-point of the target band. Achieving this outcome will improve the economic outlook and reduce borrowing costs.

Finally, we reiterate the views of the Committee on additional measures that would improve economic conditions. These include reaching a prudent public debt level, improving the functioning of network industries, lowering administered price inflation, and keeping real wage growth in line with productivity gains.

Lesetja Kganyago

GOVERNOR

The next statement of the Monetary Policy Committee will be released on 19 September 2024.

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