FUNDAMENTALS

SOUTH AFRICA MPC UPDATE: OUTLOOK DEPENDENCY FAVOURS CUT

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IN BRIEF

- As widely expected, the South African Reserve Bank (SARB) MPC meeting held in November 2024 lowered the repo rate by 25bps to 7.75%. The decision was the second consecutive unanimous outcome, but unlike the September 2024 MPC meeting, a 50bps rate cut was not considered.

- Refreshingly, the statement spoke of "outlook dependency", departing from the data dependency tone of previous statements. Aligned to this, the MPC painted three scenarios clouding inflation outlook.

- South Africa's risk premium has reduced somewhat following the formation of the Government of National Unity (GNU) mid this year, cementing the much-needed reform agenda. Relatedly, the S&P revised South Africa's ratings outlook from stable to positive.

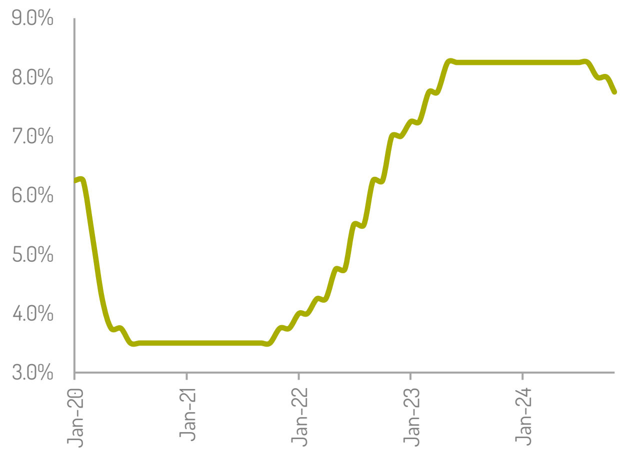
- Forecast for core inflation was revised marginally lower by 20bps to 3.9% in 2025. Broadly, the MPC expects headline inflation to remain steady at 4.0% in 2025, with electricity CPI and food inflation offering offsets to the softer core inflation.

- With the implementation of the two-pots pension withdrawals that started in September 2024, the authorities provided an update regarding the revised estimated withdrawals. Following the 2024 MTBPS statement and the revenue outturn during this FY25 to-date, SARB revised upwards the withdrawals in 2024 and 2025 by ZAR 11.0bn and ZAR 5.0bn, respectively.

Unanimity in the 25bps cut in the repo rate

As widely expected, the South African Reserve Bank (SARB) MPC meeting held in November 2024 lowered the repo rate by 25bps to 7.75%. The decision was the second consecutive unanimous outcome, but unlike the September 2024 MPC meeting, a 50bps rate cut was not considered. With an entrenched South African disinflation and mirroring the easing cycle employed by several central banks, the cut in the benchmark rate did not come as a surprise. Against the recency bias, specifically, the impact of US elections, our reading of the MPC decision is that of cautiousness by the policymakers to navigate an uncertain environment although the policymakers downplayed this single event.

REPO RATE TREND



SOURCE: SOUTH AFRICAN RESERVE BANK

Out goes the forward guidance; in comes scenarios

As has been the norm in recent post-MPC engagements, the policymakers downplayed any forward guidance arising from the Quarterly Projection Model (QPM). Refreshingly, the statement spoke of "outlook dependency", departing from the data dependency tone of previous statements. Aligned to this, the MPC painted three scenarios clouding the inflation outlook. Scenario 1 with higher administer prices of electricity and water is projected to result in a higher 2025 inflation of 4.2% from baseline of 4.0%. Scenario 2 with a more difficult environment with oil prices higher by 11.0% and South African Rand weakening to a low of 19.54 against the US dollar, is projected to result in a 4.7% inflation in 2025. Scenario 3 has a more favourable environment, oil prices declining marginally and USDZAR rate improving to 16.0 levels, has inflation forecasted at 3.7%. Nevertheless, SARB did not attach any probabilities to the scenarios under consideration.

Lower risk premium boosts ZAR steady outlook

South Africa's risk premium has reduced somewhat following the formation of the Government of National Unity (GNU) mid this year, cementing the much-needed reform agenda. Relatedly, the S&P revised South Africa's ratings outlook from stable to positive, citing better-than-expected growth prospects on receding logistics bottlenecks and debt stabilization efforts from the 2024 Medium Term Budget Policy Statement (MTBPS). The South African Rand has appreciated 1.3% YTD as of end last week, which has benefitted goods inflation. Nonetheless, the SARB's estimated FX passthrough was maintained at c. 10.0%.

COUNTRY RISK PREMIUM

SOURCE: BLOOMBERG

Softer core inflation offset by food inflation

The forecast for core inflation was revised marginally lower by 20bps to 3.9% in 2025. The downward revision was underpinned by weak Services inflation, softer core goods inflation and subdued wage inflation. Broadly, the MPC expects headline inflation to remain steady at 4.0% in 2025, with electricity CPI and food inflation offering offsets to the softer core inflation. Meat, with 33.4% weighting in food sub-index, has shown signs of picking up, pushing food inflation projections 20bps higher to 4.1% next year.

Trump 2.0 is a wild card, but there are other moving parts in other parts of the world

As expected, discussions on the impact of Trump presidency cropped up at the post-MPC engagements. On the surface, conventional wisdom views Trumps policies as inflationary, but from a trade perspective, the policymakers are much concerned with developments in its major trading partners, the European

Union's anemic growth prospects and recent developments in China. Chinese fiscal stimulus, in addition to the monetary stimulus measures, is likely to benefit South Africa, but the ongoing pivot from investment to household should dent the bilateral trading opportunity. The monetary authorities also sounded more agnostic towards the expected expiry of the African Growth and Opportunities Act (AGOA) under the Trump administration next year.

Muted inflationary impact on revised higher consumption off two-pots pension withdrawals

With the implementation of the two-pots pension withdrawals that started in September 2024, the authorities provided an update regarding the revised estimated withdrawals. Following the 2024 MTBPS statement and the revenue outturn during this FY25 to-date, SARB revised upwards the withdrawals in 2024 and 2025 by ZAR 11.0bn and ZAR 5.0bn, respectively. Furthermore, the authorities revised the spending split between consumption and debt repayments from 60:40 respectively, to 75:25. The authorities expect the higher revisions in the two-pot withdrawal and the anticipated higher household consumption to lift inflation by 8bps and 12bps in 2025 and 2026, respectively.

Open-ended wait to potential tweak in inflation target

From the press statement, the SARB seemed to suggest an imminent conclusion of the ongoing discussions around a potential change in its inflation target from the mid-point 4.5%. As per recent post-MPC meetings, the SARB stressed that any tweak to the inflation target will be communicated to stakeholders and our assessment is that the timeline for the conclusion of discussions between the National Treasury and the SARB appears open-ended.

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