



South African Reserve Bank (SARB) and Department of Basic Education (DBE)

2021 Monetary Policy Committee Schools Challenge



SOUTH AFRICAN RESERVE BANK

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Introduction: What the competition requires

- An understanding of **Economics = SA economy**
- An understanding of **monetary policy and inflation** in South Africa
- The ability to clearly **articulate thoughts and ideas** (in an essay with tables/graphs, etc.)
- The ability to present
 - **READ, READ, READ!!!**
 - **TALK, TALK, TALK!!!**
 - **SPEAK, SPEAK, SPEAK !!!**



Aggregate demand

Caused by

Economic participants

- households (C)
- firms (I)
- government (G)
- foreign sector (X-M)

AD

Aggregate supply

Determined by

Factors of production

- natural resources
- labour
- capital
- entrepreneurship

AS

Macroeconomic objectives

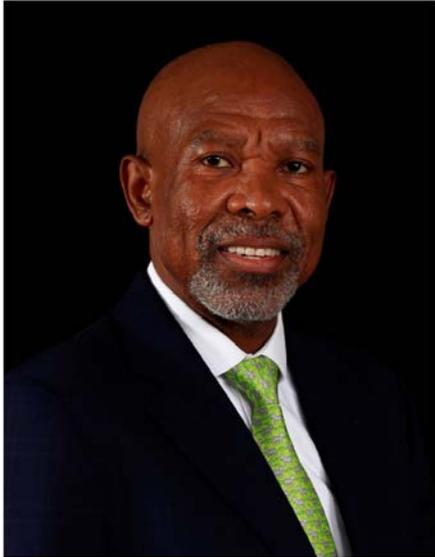
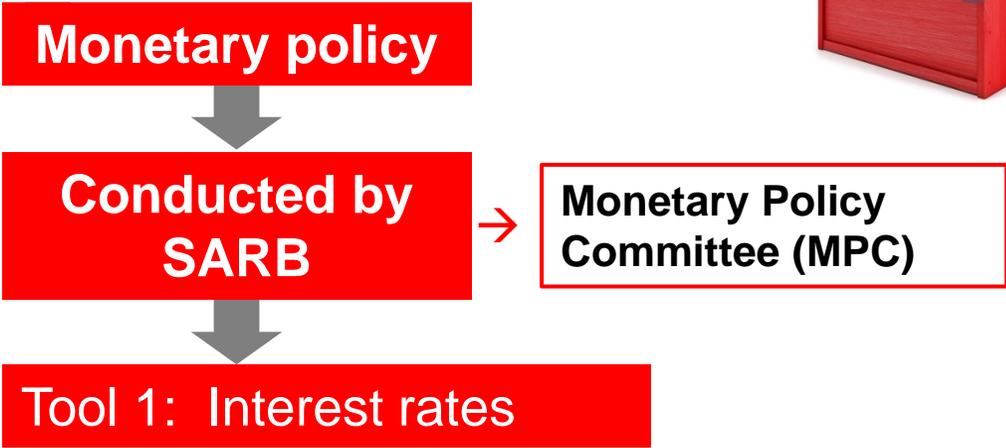
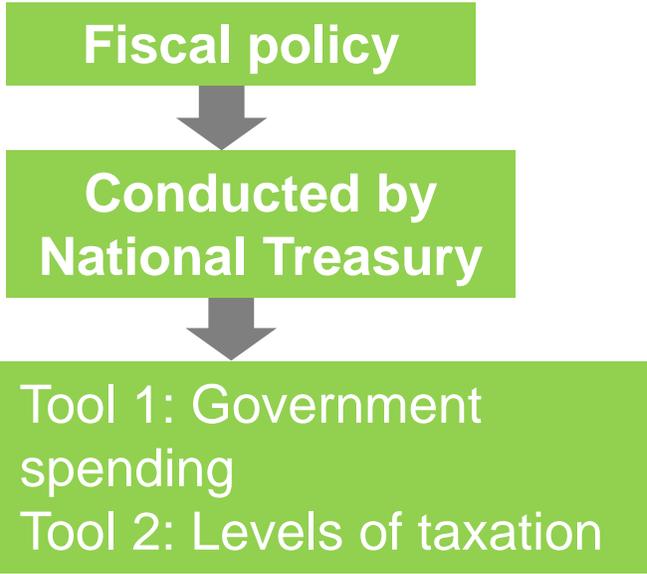
- economic growth
- unemployment
- inflation
- BOP stability
- Equitable Y

influenced by economic policy

Monetary policy

Fiscal policy

Government tries to stabilise the economy using macroeconomic policies/tools



The SARB's mandate

The Constitution of the Republic of South Africa prescribes the objective of the Bank as the **protection of the value of the currency** in the interest of balanced and sustainable economic growth and development



The primary mandate of the SARB is to achieve and maintain price stability in the interest of balanced and sustainable economic growth

The SARB has a complementary mandate to oversee and **maintain financial stability**



How does the SARB aim to achieve the mandate?

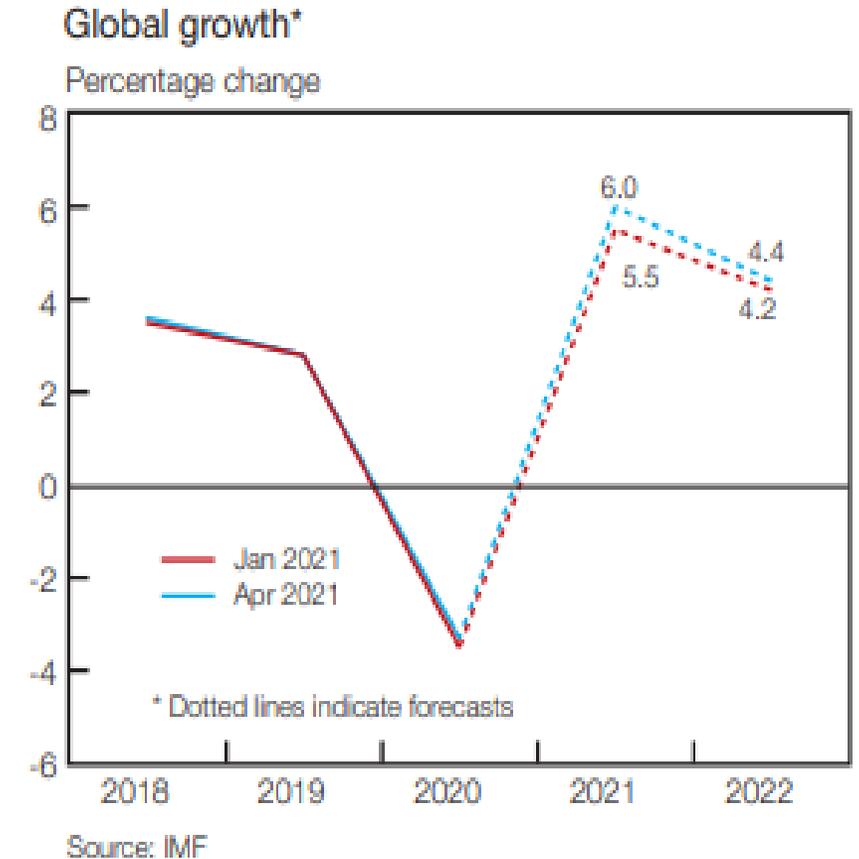
-  Maintain headline inflation within the 3–6% target range.
-  Protect and enhance financial stability
-  Promote and enhance the safety, soundness and integrity of regulated financial institutions and market infrastructure
-  Enhance South Africa's resilience to external shocks
-  Ensure the cost-effective availability and integrity of the currency

Factors affecting the economy and inflation



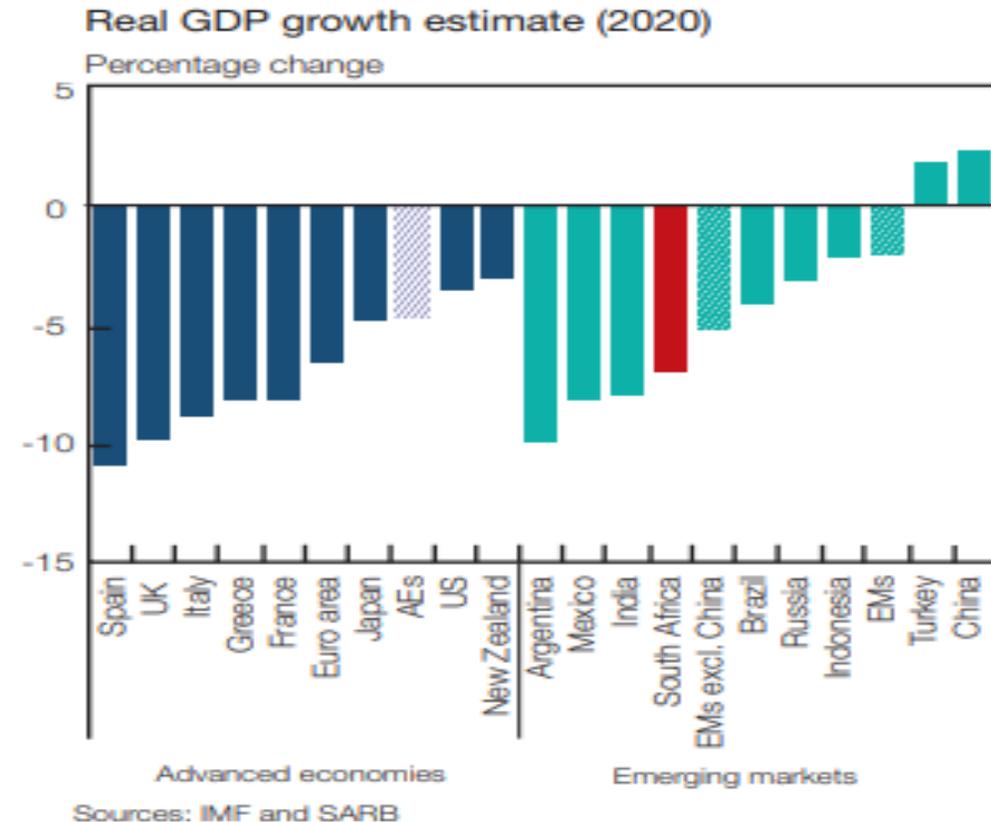
The global economy: Macroeconomic risks

- Macroeconomic risks
- **Global** recovery in GDP growth is underway post Covid-19 pandemic
 - Optimism about vaccination roll-out
 - Widespread fiscal and monetary support
 - Moderate rise in global inflation facilitated by stronger demand and supply constraints



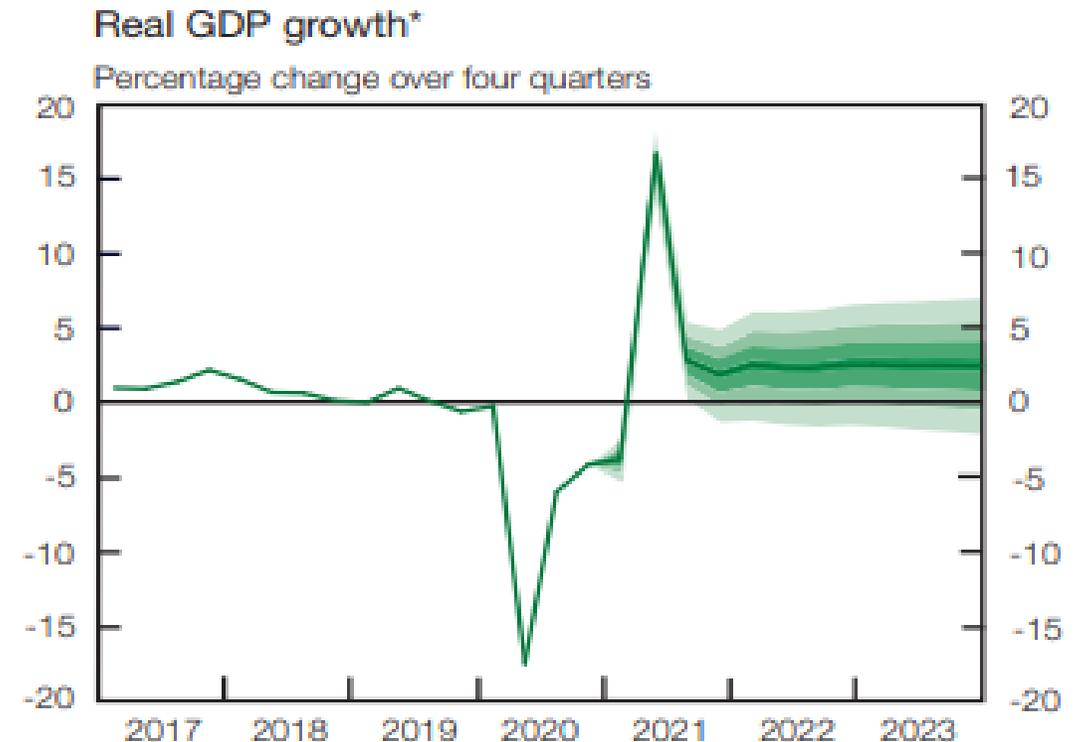
The global economy: Emerging markets

- Emerging market conditions largely negative in 2020
- Overwhelmed healthcare systems during Covid-19 pandemic
- Tourism industries affected
- Strained fiscal response
 - Excessive debt levels
- Winners
 - China
 - Turkey



The domestic economy: SA growth is forecast to stay low

- SA growth subdued
- Annual 2021 growth expected to be 3.8%
- 2022 = 2.4%
- 2023 = 2.5%
- COVID-19 uncertainties
 - Further lockdowns
 - Delays in vaccination roll-out
- Global developments
 - Rising commodity prices
 - Record-low interest rates
 - Easing of lockdown restrictions



* The bands around the central projection show confidence intervals of 10%, 30%, 50% and 70%.

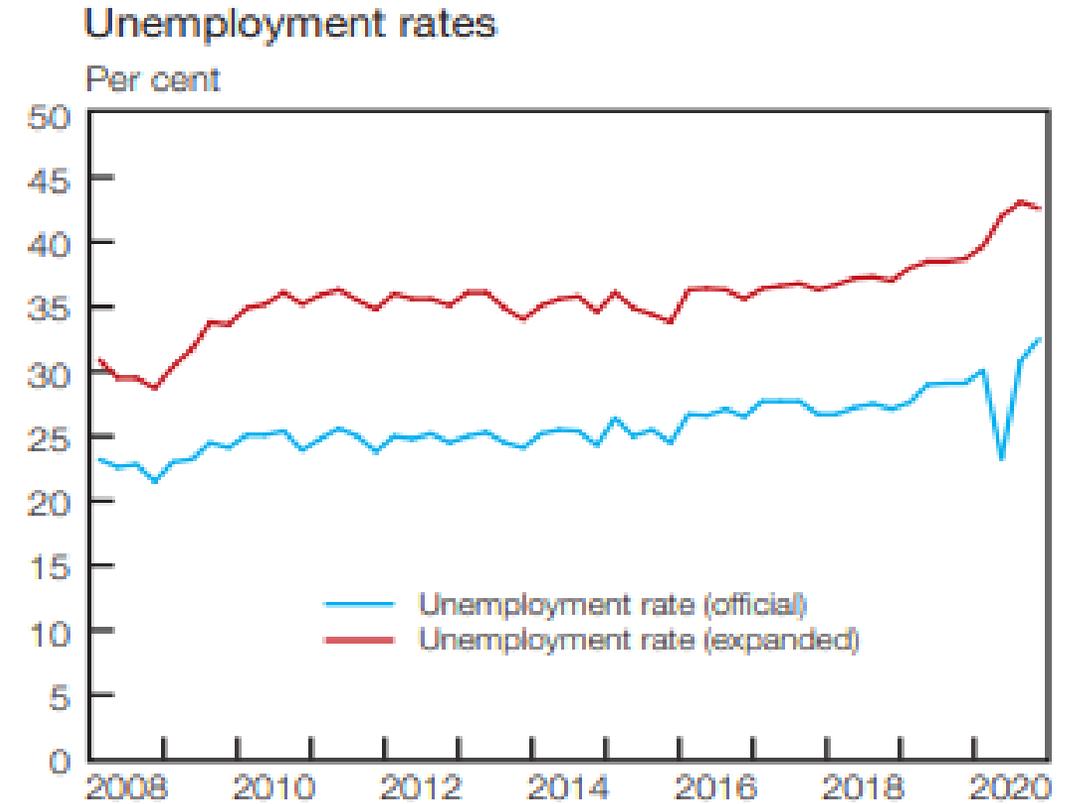
This chart shows seasonally-adjusted data, as used in the QPM.

Sources: Stats SA and SARB



The domestic economy: Unemployment

- Official unemployment rate: 32.5% Q4 2020
- Highest since 2008
- Expanded unemployment rate 42.6% Q4 2020

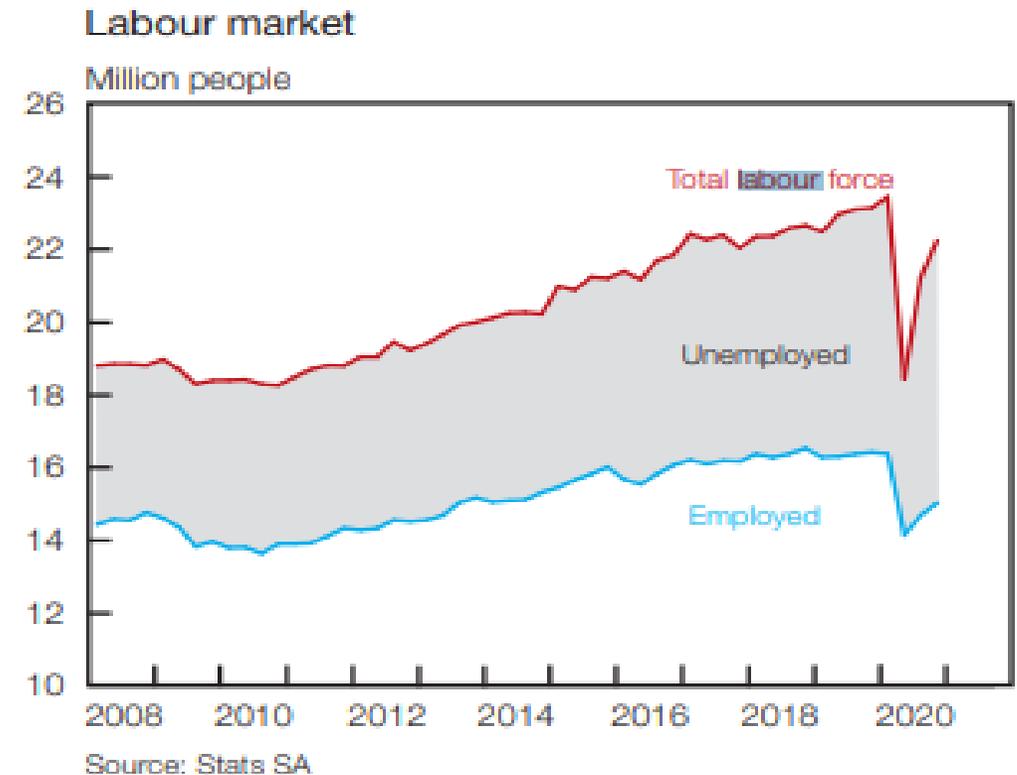


Source: Stats SA



The domestic economy: Labour market recovery since Covid-19 pandemic

- Roughly 2.2 million jobs lost in Q2:2020
- 900 000 jobs recovered by Q4:2020
- Net job losses = 1.4 million from Q2:2020 to Q4:2020
- Job losses skewed towards low-skilled jobs



Key economic indicators



Contributors

Demand factors

$$Y = C+I+G+ (X-M)$$

Real gross domestic expenditure

Quarter-to-quarter percentage change at seasonally adjusted annualised rates

Component	2019					2020				
	Q1	Q2	Q3	Q4	Year ¹	Q1	Q2	Q3	Q4	Year ¹
Final consumption expenditure										
Households.....	-0.9	2.5	0.3	1.4	1.0	0.0	-52.0	75.3	7.5	-5.4
General government.....	2.2	2.7	1.4	-0.2	1.5	1.8	-2.1	0.8	1.1	0.5
Gross fixed capital formation.....	-4.1	5.8	4.1	-10.0	-0.9	-18.7	-59.4	26.9	12.1	-17.5
Domestic final demand ²	-0.9	3.2	1.2	-1.2	0.8	-3.3	-45.4	46.7	6.8	-6.5
Change in inventories (R billions) ³	-11.7	29.4	-13.9	-40.3	-9.1	-70.7	-29.3	-144.1	-115.1	-89.8
Residual ⁴	0.1	0.2	0.1	0.0	0.1	0.0	0.4	0.3	0.2	0.2
Gross domestic expenditure ⁵	4.7	9.1	-4.5	-4.6	0.7	-7.1	-41.9	25.4	11.2	-8.9

1 Percentage change over one year

2 Comprises final consumption expenditure by households and general government as well as gross fixed capital formation

3 At constant 2010 prices

4 The residual as a percentage of GDP

5 Including the residual

Sources: Stats SA and SARB



Supply factors

- Electricity and water inflation –
 - moderated due to delayed implementation of the annual price increases in response to Covid-19 pandemic
- Agriculture prices increased
- Exchange rate – possible pass-through to consumer prices
 - Prices of imported products like petrol
 - Input costs



Inflation targets



Is inflation a good or a bad thing?

What happens if inflation is too **HIGH**?



What happens if inflation is too **LOW**?



What is the purpose of monetary policy?

- The main goal is *price stability*
- Responsibility rests with the central bank (SARB)
- South Africa adopted **inflation targeting** in February 2000 = where the central bank announces an **inflation target** and implements monetary policy to achieve this target directly



SFA 1

HEADLINE INFLATION
is **CORE INFLATION**
PLUS prices of food and
energy which change all
the time!

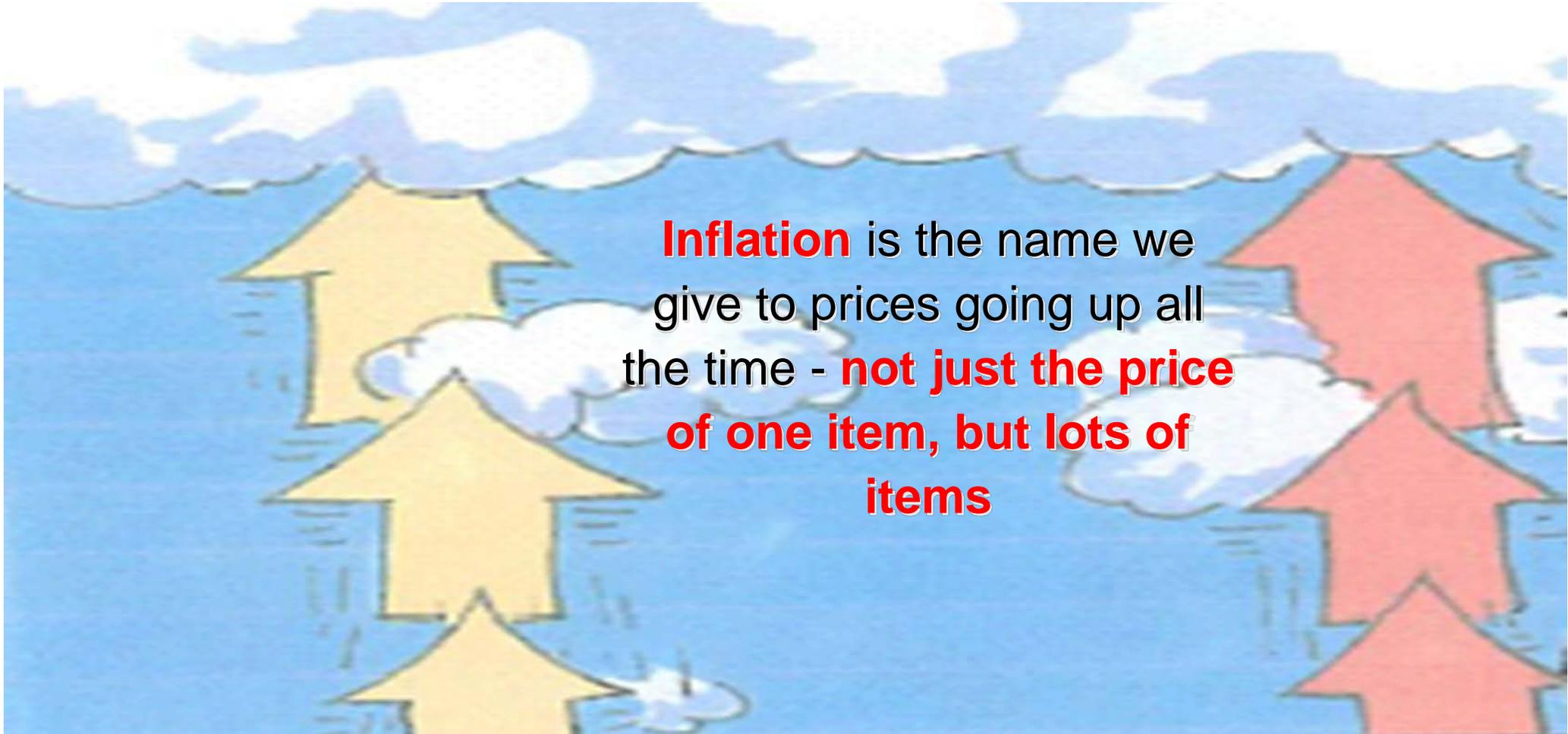
Maintain **headline
inflation** within the
target range



CORE INFLATION only
includes prices that do
not change frequently
(e.g. rent, labour etc.)



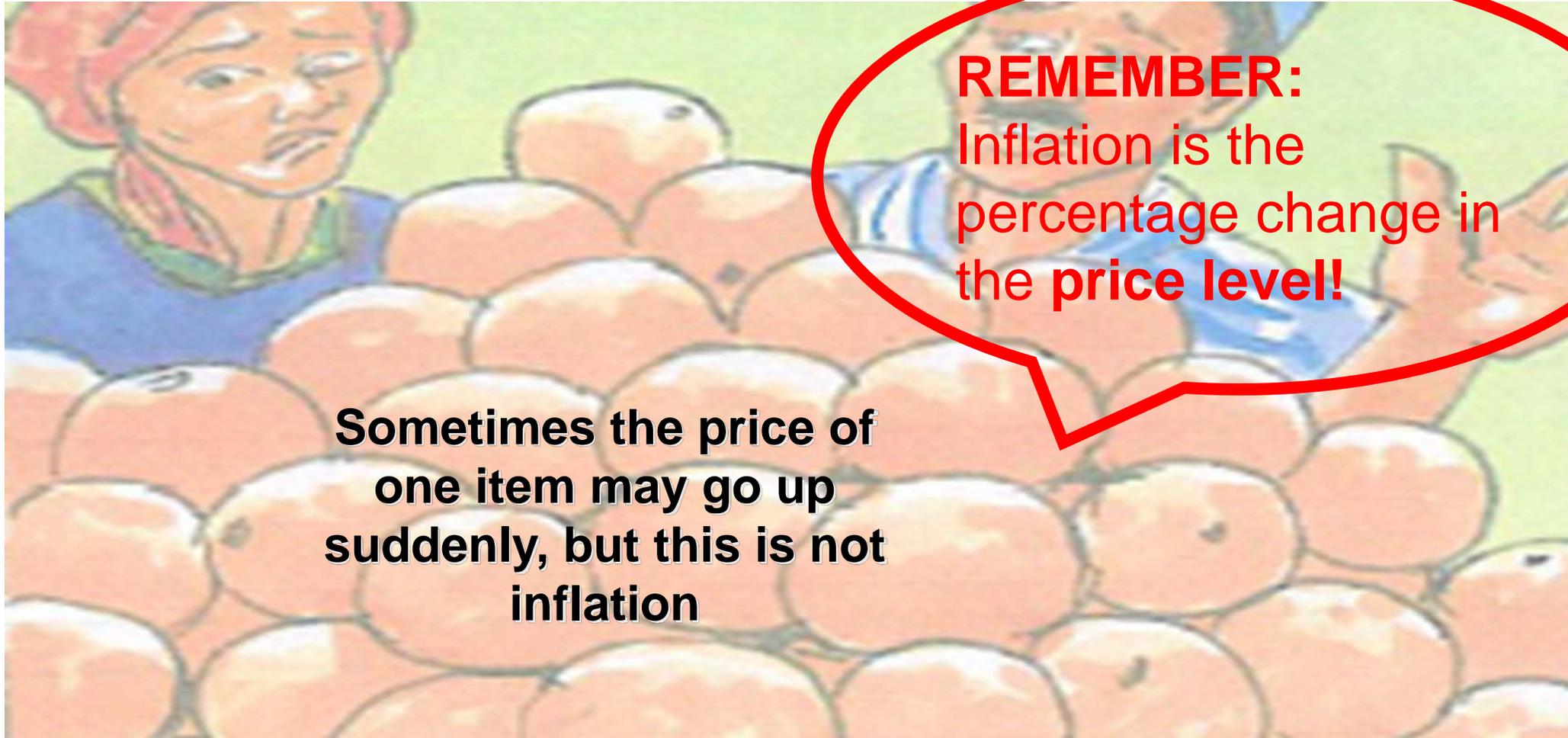
Definition



Inflation is the name we give to prices going up all the time - **not just the price of one item, but lots of items**



Definition



Weight of the different COICOP categories (100%)

- Food and non-alcoholic beverages (17.24%)
- Alcoholic beverages and tobacco (5.82%)
- Clothing and footwear (3.83%)
- Housing and utilities (24.62%)
- Household content, equipment and maintenance (4.35%)
- Health (1.40%)
- Transport (14.28%)
- Communication (2.63%)
- Recreation and culture (5.16%)
- Education (2.53%)
- Restaurants and hotels (3.09%)
- Miscellaneous goods and services (15.05%)





Sometimes a rise in the price of one item can cause a rise in the price of all other items



Causes of inflation

- **Demand-pull:**
 - Aggregate demand rises more rapidly than aggregate supply
- **Cost-push:**
 - Autonomous increase in production cost



Resource: <http://www.resbank.co.za/>

- Inflation rates

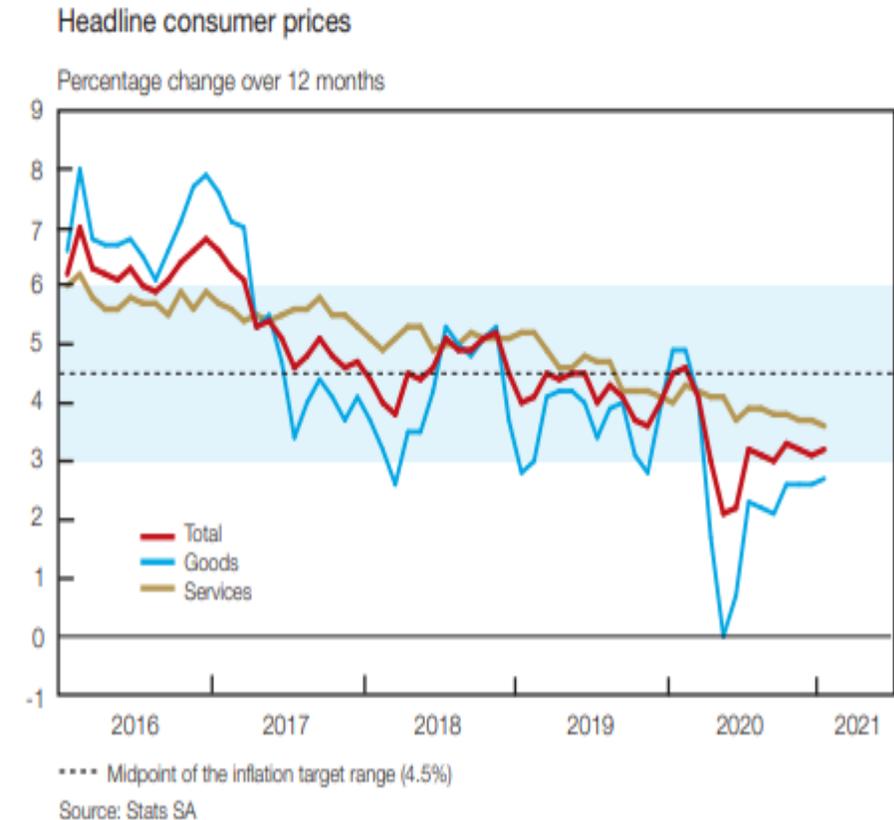


Inflation rates	
<u>CPI</u>	3.2
	Mar 2021



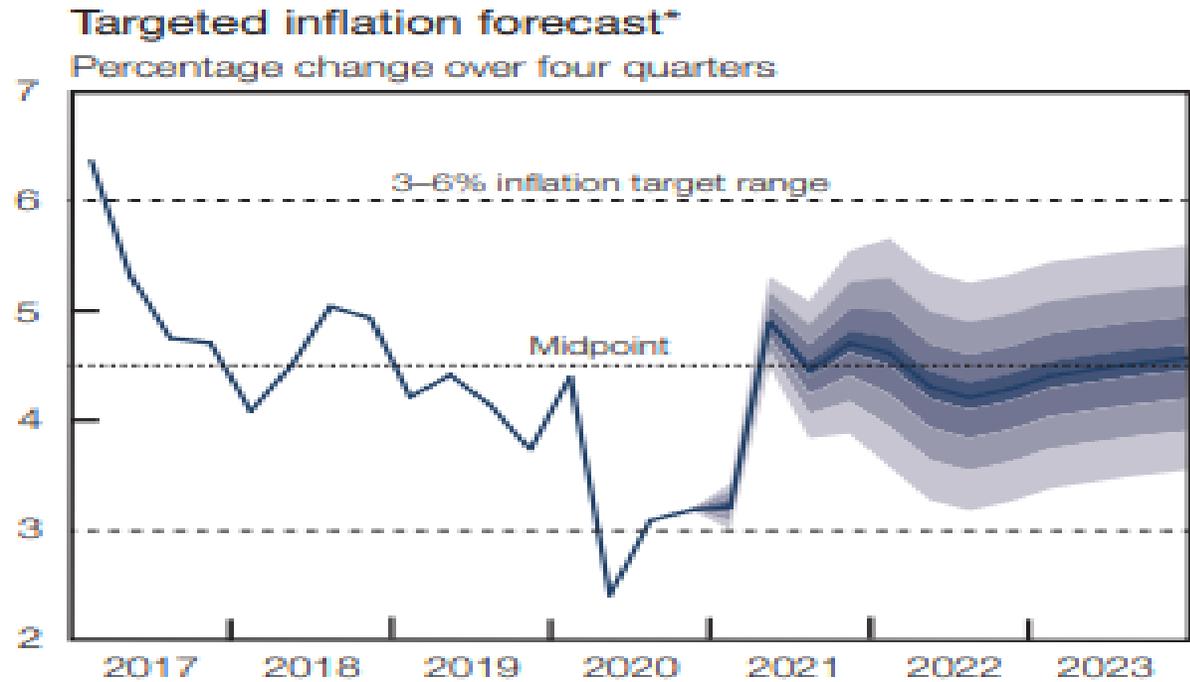
Inflation

- Headline CPI
 - Sharply declined from mid-point in Feb 2020 to below lower band (2.1%) in May 2020
 - Increased from below lower band in May 2020 to 3.2% in January 2021
- Deceleration in goods price inflation



Inflation outlook

- Inflation stabilises at 4.5% over the medium term



* The bands around the central projection show confidence intervals of 10%, 30%, 50% and 70%.

Sources: Stats SA and SARB

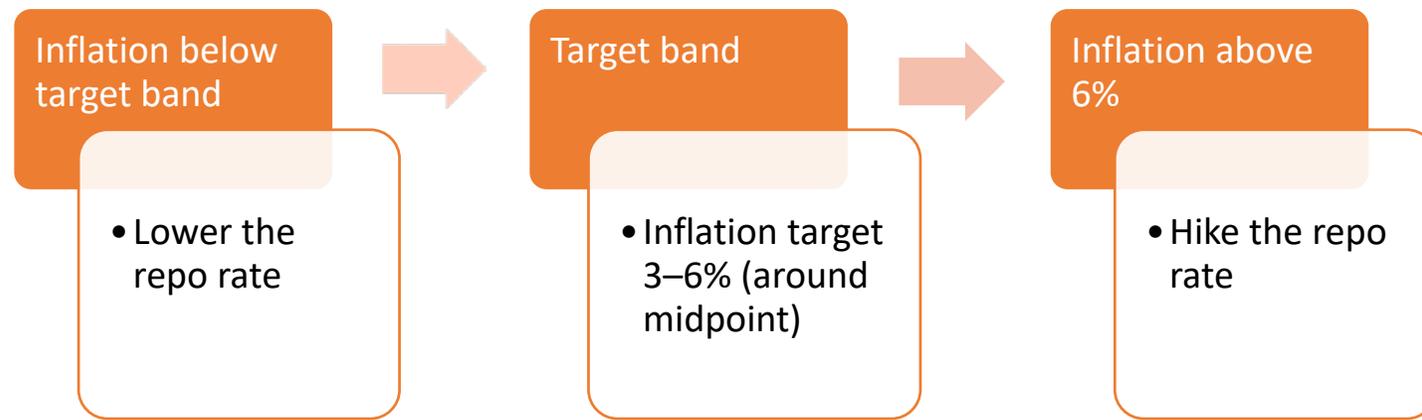


How would you form an inflation outlook?



1. Identify the *goal* of the model – methodology

- *1st step is to identify key drivers of inflation* (hint – see MPC statement for more info):
 - Demand-pull inflation:
 - Cost-push inflation:
- Then decide how to *change the repo rate*



2. Identify the *elements* of the model – the basic elements

Monetary policy

- The central bank's control of the financial conditions in a country in order to achieve an inflation target

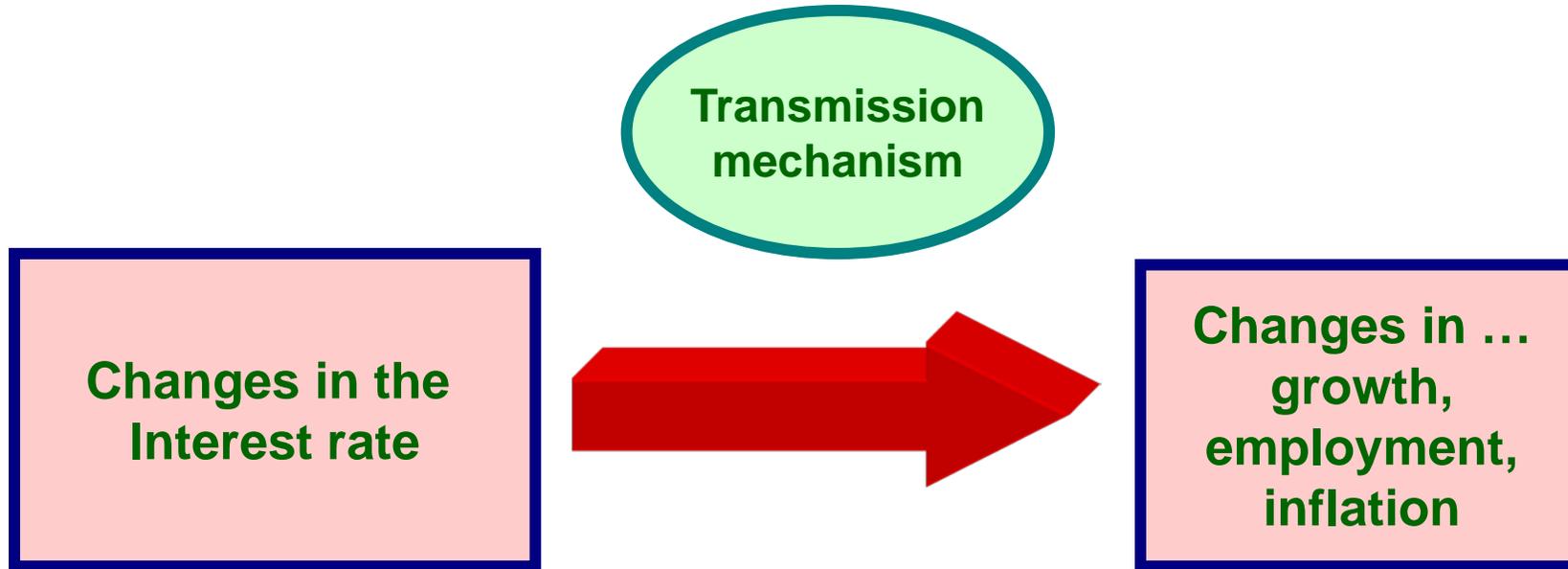
Instrument

= Repo rate

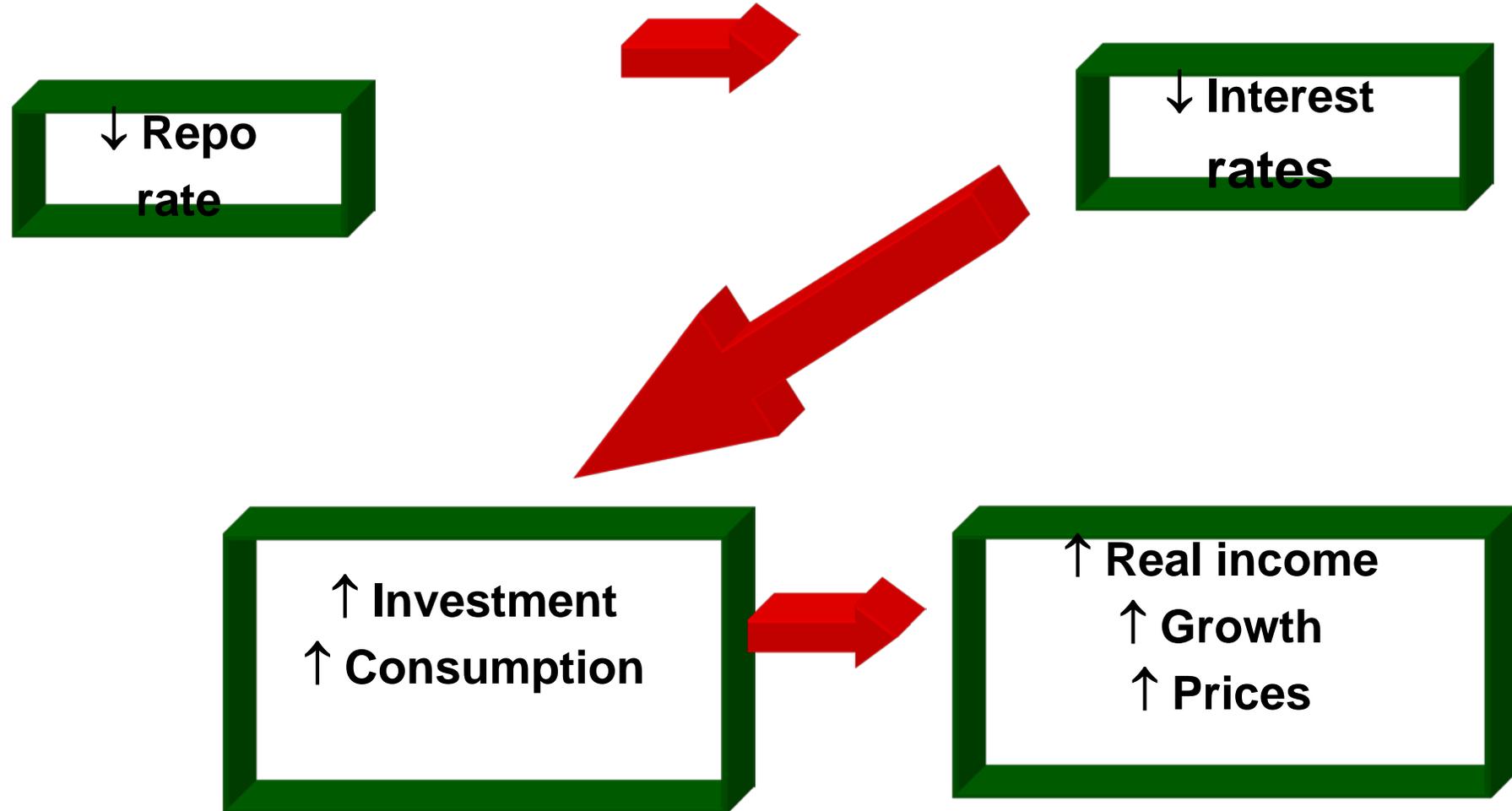
- The **rate at which commercial banks borrow money from the central bank** (the South African Reserve Bank)
- **Prime rate**
- The **rate at which a client with a normal risk can borrow money** from commercial banks



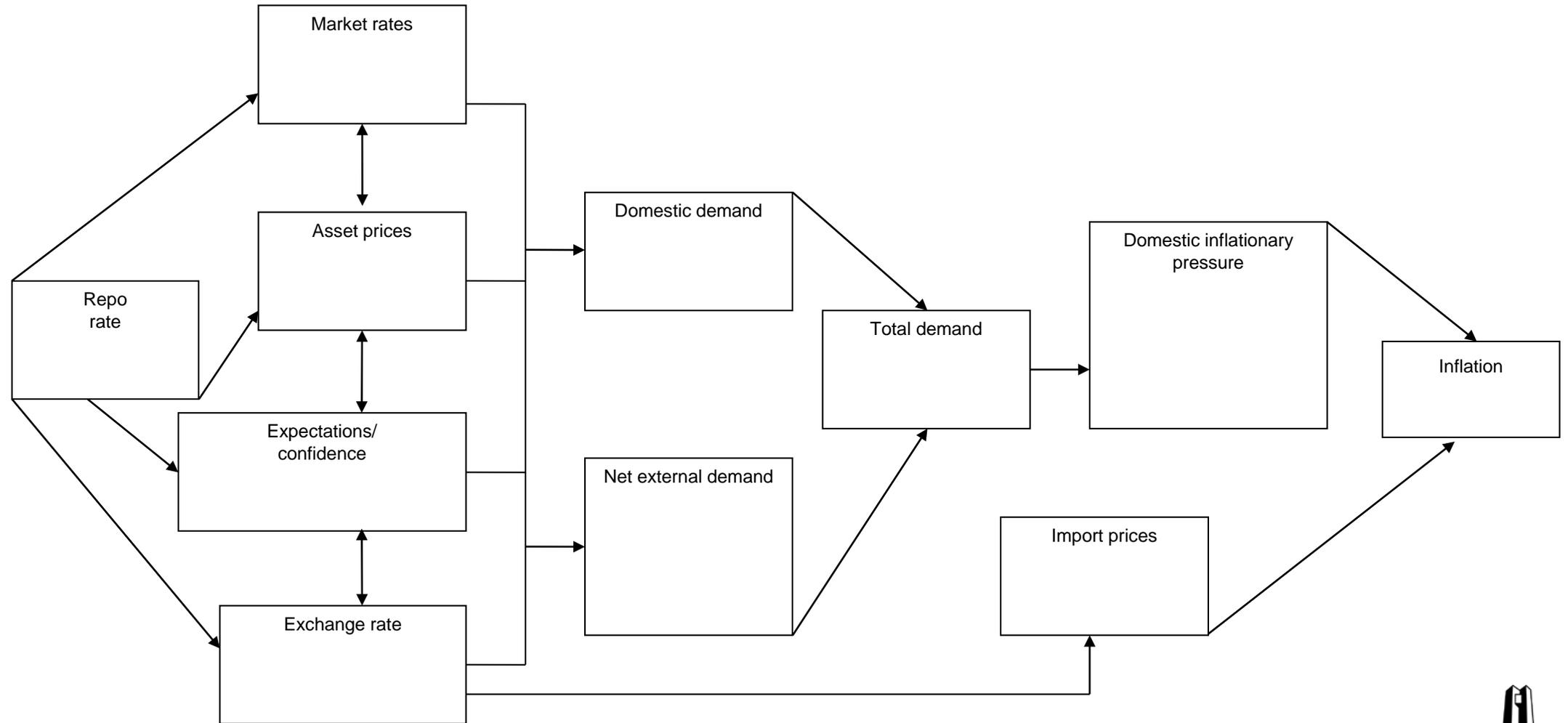
Transmission mechanism



Transmission mechanism – Interest rate channel



Transmission channels



MPC statement

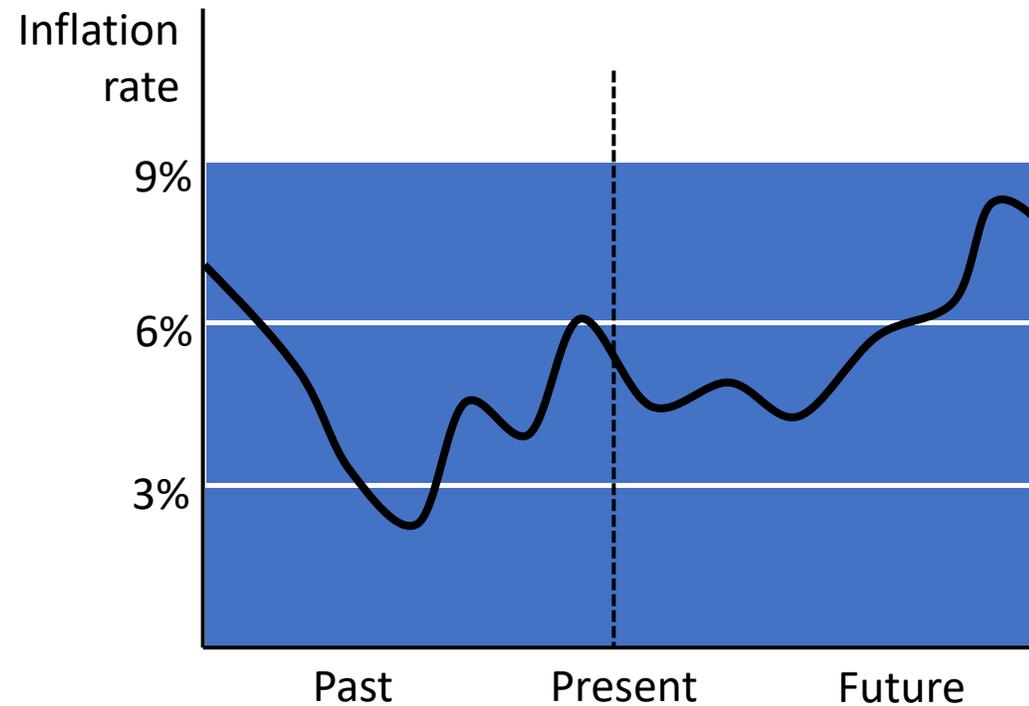


Statement structure



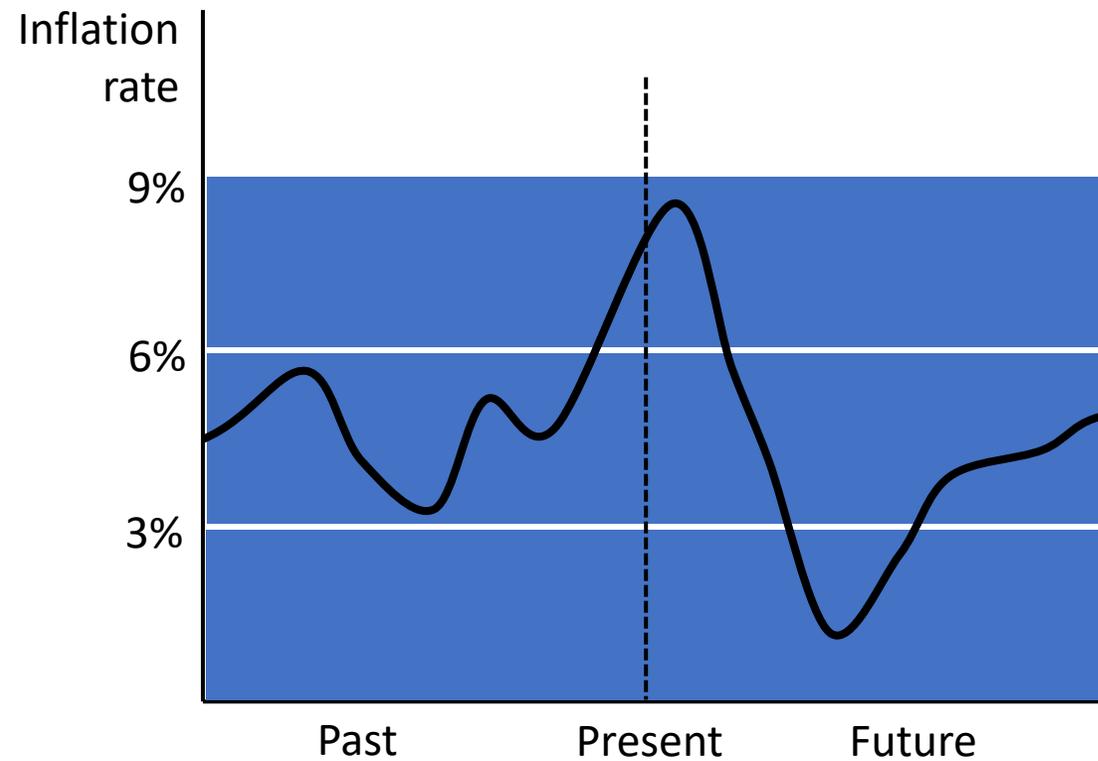
Your task for the statement is to decide whether to...

1. *Raise* the repo rate



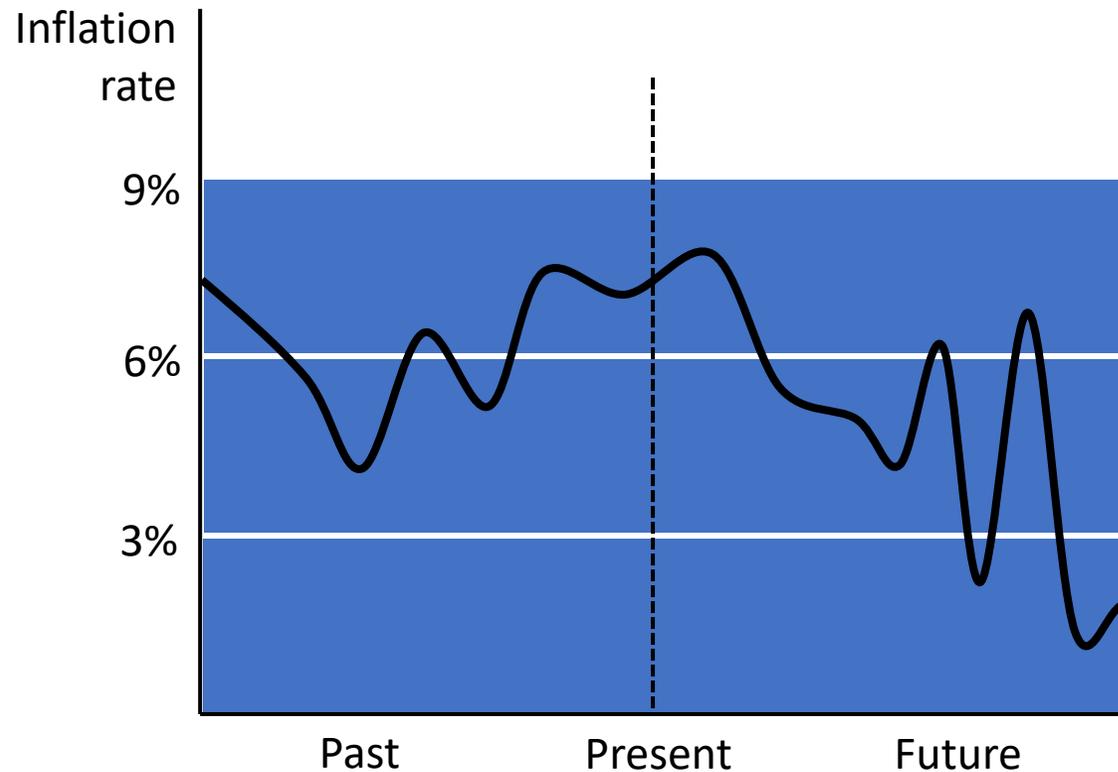
Your task for the statement is to decide whether to...

2. Keep the repo rate *constant* ⇔



Your task for the statement is to decide whether to...

3. *Decrease* the repo rate ↓



What makes a winning statement?

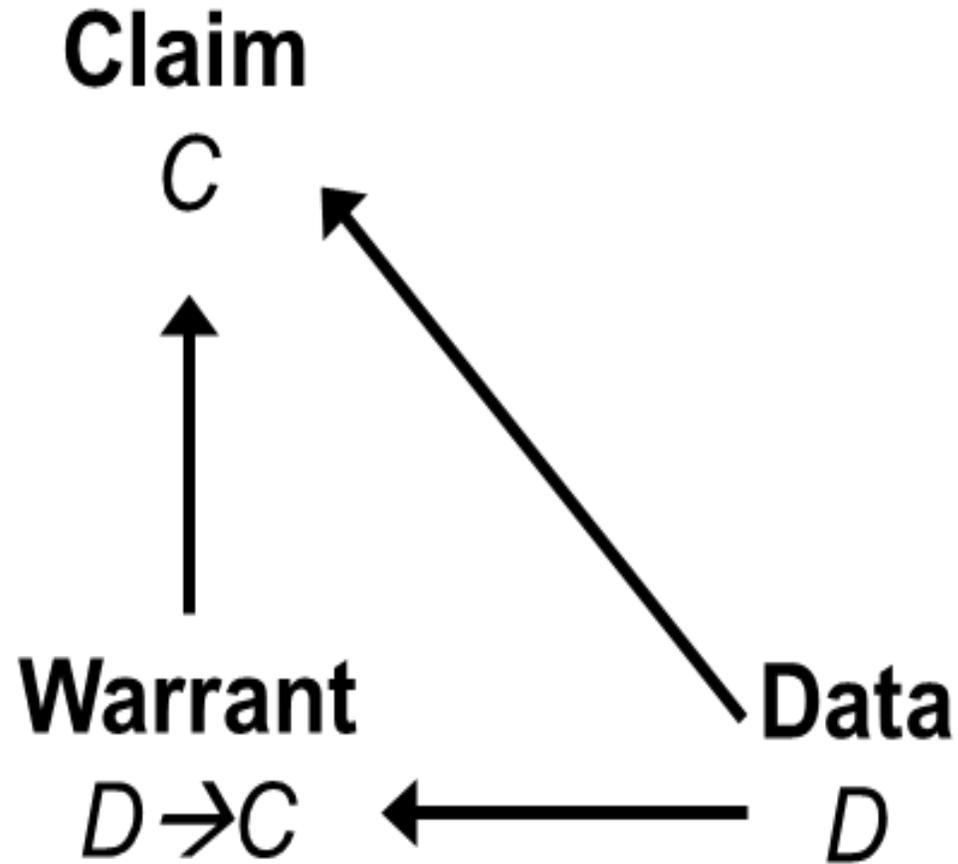
You need to make an *argument*

What is an argument?

- Saying something
- Story line
- **Evidence and fact**



What goes into an economic statement?



Data sources

- Various topics
 - <http://www.resbank.co.za/Research/Statistics/Pages/Statistics-Home.aspx>
- Specific data search
 - <http://www.resbank.co.za/Research/Statistics/Pages/OnlineDownloadFacility.aspx>
- *Monetary Policy Review*
 - <http://www.resbank.co.za/Publications/Reviews/Pages/Monetary-Policy-Review.aspx>
- MPC statements
 - <http://www.resbank.co.za/Publications/Statements/Pages/MonetaryPolicyStatements.aspx>



More data sources to consult

- South African Reserve Bank (SARB)
 - Quarterly Bulletin App [Quarterly Bulletins \(resbank.co.za\)](https://resbank.co.za)
- Statistics South Africa
- Bureau for Economic Research
- Big 4 banks - economic commentary section
- Business newspapers/websites



Technical aspects: Table – the wrong way ❌

	Utopia repo rate	Lemuria repo rate	Atlantis repo rate
2005	8.0%	2.0%	10.0%
2006	10.0%	3.0%	2.0%
2007	13.0%	2.0%	8.5%
2008	11.0%	4.0%	3.0%
2009	10.5%	3.0%	0.5%
2010	8.5%	2.5%	8.0%
2011	7.0%	2.0%	15.0%
2012	5.5%	1.5%	14.0%
2013	5.0%	2.0%	10.0%
2014	6.0%	1.5%	7.0%

- Utopia's interest rate was 8% in 2005, and Lemuria's rate was 2% and the rate in Atlantis was 10%. In 2006, Utopia's rate went up to 10% and Lemuria's rate also went up to 2%, while Atlantis's repo rate went down to 2%. Then in 2007...



Technical aspects: Table – the right way ✓

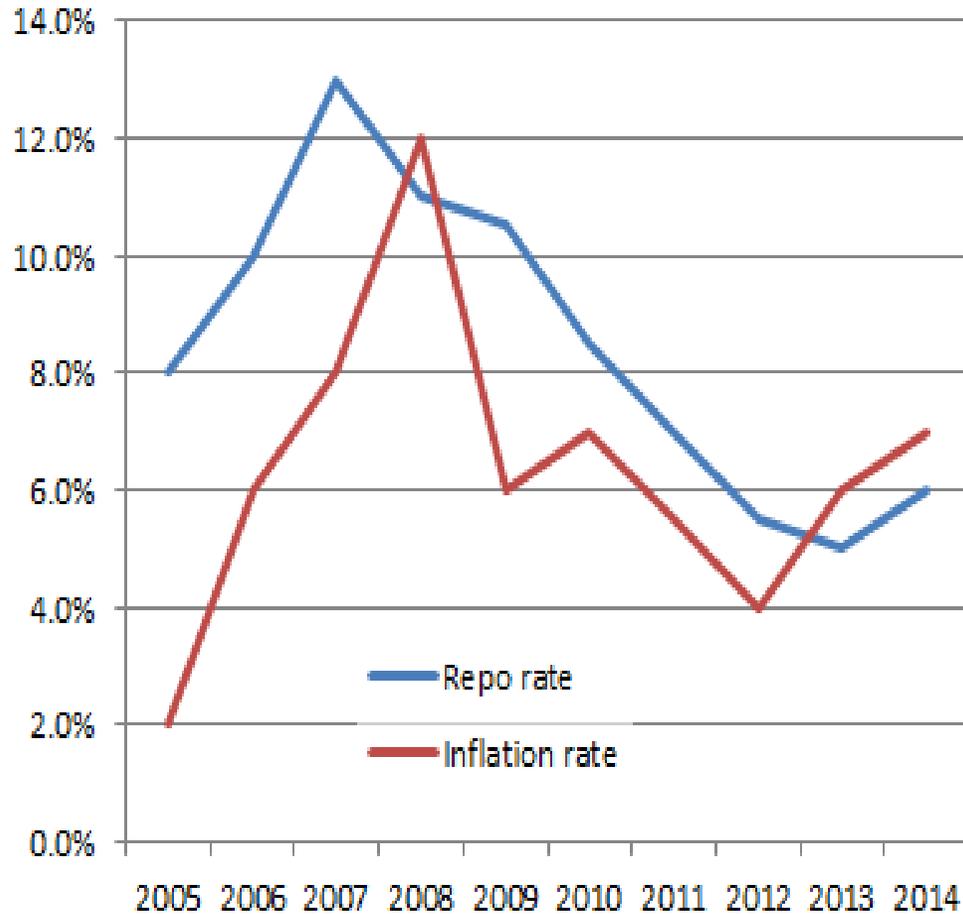
	Utopia repo rate	Lemuria repo rate	Atlantis repo rate
2005	8.0%	2.0%	10.0%
2006	10.0%	3.0%	2.0%
2007	13.0%	2.0%	8.5%
2008	11.0%	4.0%	3.0%
2009	10.5%	3.0%	0.5%
2010	8.5%	2.5%	8.0%
2011	7.0%	2.0%	15.0%
2012	5.5%	1.5%	14.0%
2013	5.0%	2.0%	10.0%
2014	6.0%	1.5%	7.0%

The interest rate in Atlantis was much more volatile compared to Utopia and Lemuria. This is partly due to the fact that Atlantis did not follow inflation targeting. Lemuria's effective monetary policy allowed it to keep inflation low, and therefore experienced the lowest interest rates...

Substantiate with a graph



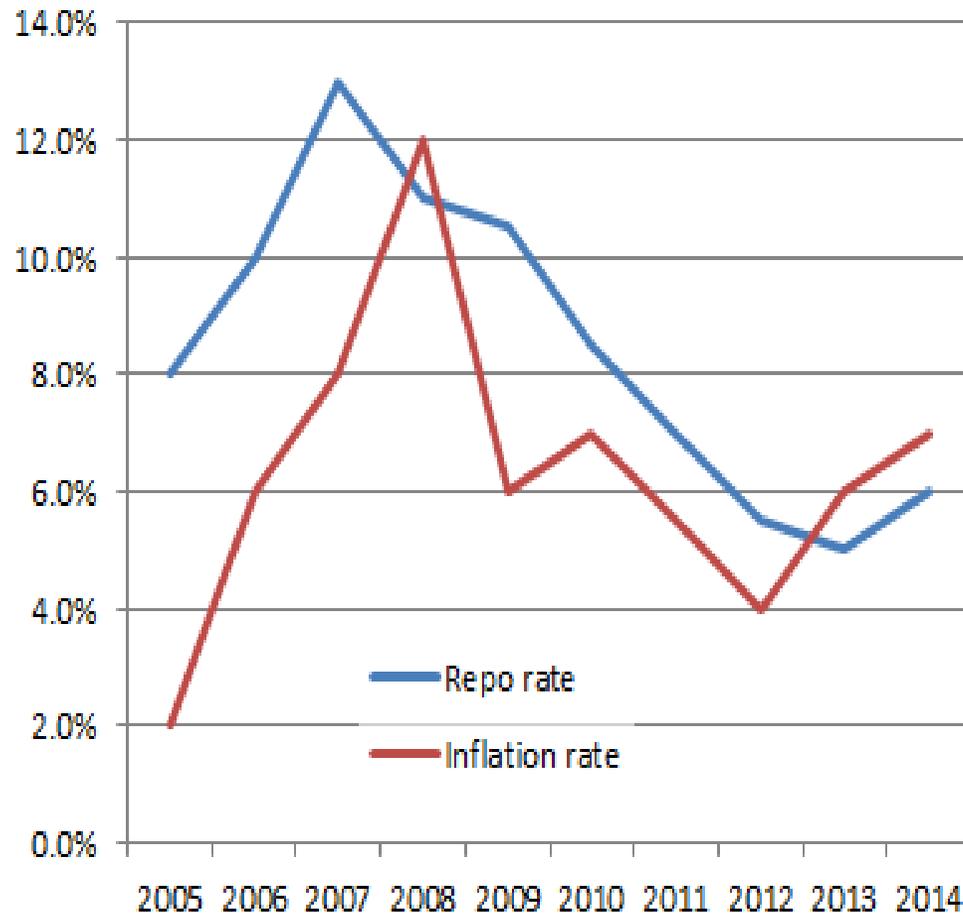
Technical aspects: Graph – the wrong way ❌



The repo rate went up to 13% in 2007, and then went down to 5% in 2013, and then it went up again. The inflation rate went up to 12% in 2008, went up and down to 4% in 2012, and then rose again to 7%...



Technical aspects: Graph – the right way



The central bank seems to respond to the inflation rate as is evident from the way the repo rate moves together with the inflation rate.

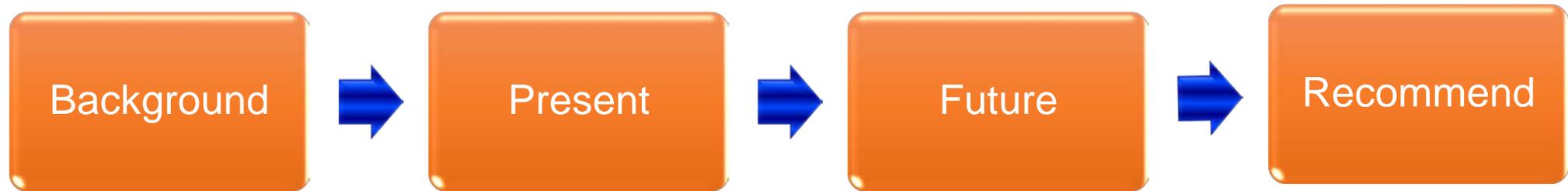


What was the difference?

- No simple repetition!
- Rather show the *meaning*:
 - Highlight what you want the reader to notice
 - Connect to how it supports your argument



The process



Recommendations – **VERY IMPORTANT**

- Does your inflation forecast suggest the need for:
 - **Rise** in the repo rate (↑)
 - **No** change in the repo rate (↔)
 - **Drop** in the repo rate (↓)
- Justify (as explained)
 - Consider target range over 12 to 24 months
 - Other variables?
- Forward-looking



3.5%



“The Monetary Policy Committee has decided to hold the repurchase rate at 3.5%. The implied policy rate path of the Quarterly Projection Model (QPM) indicates an increase of 25 basis points in each of the second and fourth quarters of 2021. Compared to the previous meeting, the shift in the rate path from the third to the fourth quarter is due to somewhat lower inflation in 2022.”

Governor Lesetja Kganyago

25 March 2021

#SARBMPCMAR21



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In conclusion...

- Know **what you will argue** about the repo rate
- Your argument should be derived from the future direction of **inflation**
- **Forward-looking**
- It should also be supported by **current developments**
- **Remember the final repo rate decision**



**THANK
YOU**



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