SOUTH AFRICAN RESERVE BANK

**PRESS STATEMENT**

**23 November 2023**

## STATEMENT OF THE MONETARY POLICY COMMITTEE

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

As we approach the end of the year, easing headline inflation and modest economic growth remain the dominant global economic trends of this past year. Output in the Euro Area is poor, while the robust growth seen in North America is likely to moderate. China's growth performance is still weak, with few benefits for global commodity prices.[1] Across most regions, monetary policy will continue to focus on achieving inflation targets, while high debt levels will require fiscal consolidation efforts. In the developing world, financing conditions are expected to remain tight and growth moderate.

The longer-term economic outlook however, remains uncertain. Weaker household consumption and falling property prices may drag on growth for a sustained period. Climate change and geopolitical tensions threaten supply chains, output and prices.

[1] South Africa's commodity export index is forecast to *decline* by 27.9% this year, a further 11.5% in 2024, and an additional 5.0% in 2025. The index is forecast to fall by 1.7% in 2026.

With high interest rates and uncertainty, financial markets and asset prices are expected to remain volatile, dampening investor appetite and capital flows.

Taking these and other factors into account, the SARB's forecast for global growth in 2023 is broadly unchanged at 2.7% (from 2.6%), and 2.6% in 2024.[2]

While South Africa's electricity load-shedding has declined, domestic growth in the near term is likely to remain muted.  Energy and logistical constraints are still binding on economic activity and generally increase costs.[3]  We expect electricity supply to increase gradually over the medium-term however, helping to raise our forecast for output growth in 2024, 2025 and 2026.

Spending by firms, households, public corporations and general government remains positive in real terms, on an annual basis. Disposable income of households is expected to grow, albeit slowly. The investment forecast for the year was revised up to 7.7% in September. Credit growth to households and corporates has slowed in recent months, but remains positive. [4]

GDP growth for 2023 is revised slightly upward to 0.8% from the September figure of 0.7%.  Our GDP growth forecast for 2024 and 2025 is increased from the previous

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[2] Global growth in the QPM model is a trade-weighted average of South Africa's trading partners.

[3] The number of days of expected load-shedding is 300 in 2023, decreasing to 150 days and 100 days, respectively in 2024, and 2025.  Estimates of the average stages of load-shedding is multiplied by the number of days and then multiplied by the cost to GDP per stage-day.  The cost per stage was revised lower in the March 2023 MPC meeting. In nominal terms, these costs vary between R0-R1.2 million for stages 1 and 2 and up to R204-R899 million for stages 3 to 6, when continued on a 24 hour basis on weekdays. This will be assessed further as new data and information is received.

[4] Although growth in the claims on the domestic private sector has slowed from 8.4% y-o-y in January 2023, to only 4.6% yoy in September, real credit extension for the year to September is 0.3% above the average for calendar 2022.

meeting, to 1.2% and 1.3%, respectively, in large part due to an expected decrease in load-shedding.[5]

While households and firms exhibit some resilience, economic growth has been volatile and highly sensitive to new shocks. A sustained reduction in load-shedding, or greater energy supply from alternative sources, would significantly increase growth. The operation of ports and rail however have become a serious constraint.

At present, we assess the risks to the medium-term domestic growth outlook to be balanced, as demand continues to run ahead of the constrained supply environment. As a result, our current growth forecast leaves the output gap marginally positive.[6]

Turning to the inflation outlook, South Africa's headline inflation rate has increased more gradually than in many other emerging and advanced economies. Nonetheless, South Africa's inflation rate remains sensitive to shocks.

While volatile in recent weeks, oil prices have increased over the year and commodity export prices have moderated further. South Africa's external financing needs will increase as the current account deficit expands from a forecasted 1.3% of GDP this year (from 2.0%), to 2.6% of GDP in 2024 and to 3.5% of GDP in 2025.[7] The smaller deficit this year is the result of significantly better than expected trade outcomes in the third quarter.[8]

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[5] The growth forecast includes expected changes in the policy rate as given by the QPM.

[6] Potential growth is 0.1% in 2023 (up from 0.0%) and rising to 1.0% for 2024, 1.2% for 2025, and 1.6% in 2026.

[7] The current account deficit in 2026 is forecast to be -4.0% of GDP. Exports are forecast to grow in real terms by 4.8% this year (from 4.5%) and 2.9% in 2024. Our oil price forecast is higher than in September, averaging US$84 per barrel in 2023 and in 2024, before easing to US$82 for 2025 and US$80 for 2026.

[8] Agricultural exports and vehicle and parts exports were up, while there was a sharp drop in machinery and electrical goods imports.

The rand weakened over the past year, depreciating by about 9.5% against the US dollar. The lack of sustained economic growth and dependence on commodities is reflected in the high volatility of the currency in response to global risk-on and risk-off episodes. The implied starting point for the rand forecast is R18.76 to the US dollar, compared to R18.45 at the time of previous meeting.

Compared to September, fuel price inflation is broadly unchanged for 2023, but lowered from 5.8% to 3.2% in 2024.

Our food price inflation forecast for 2023 remains high at 10.6% (from 10.4%). The forecast for 2024 is slightly higher at 5.5%.

Better monthly outcomes have led to a marginal downward revision in our forecast for core inflation to 4.8% in 2023 (previously 4.9%) and to 4.6% in 2024 (from 4.7%). The core inflation forecast for 2025 remains at 4.5%. The new 2026 core forecast is also 4.5%. Services inflation in 2023 is now expected to come in at 4.3% (from 4.4%), before rising to 4.8% in 2024 (up from 4.6%). Core goods inflation remains elevated but is revised lower for this year to 6.0% (from 6.3%).[9] Growth in average salaries and unit labour costs is forecast to be somewhat lower than at the time of the September meeting.[10]

[9] Core goods refers to total CPI goods excluding food and NAB, fuel and electricity, whereas services include all surveyed services within the CPI basket. Core goods inflation is expected to be 4.5% in 2024, 4.4% in 2025, and 4.5% in 2026.

[10] Average salaries are expected to rise by 4.6% in 2023 (down from 5.4), 6.0% in 2024, and by 5.4% in 2025 and in 2026. Unit labour costs are forecast to rise by 4.6%, 4.5% and 4.4%, respectively, in 2023, 2024, and 2025. In 2026, unit labour costs are forecast to increase by 4.3%.

With few significant changes to underlying components, headline inflation for 2023 is revised down slightly to 5.8% (from 5.9%). The headline inflation forecast for 2024 is 5.0% (down from 5.1%), before stabilising at 4.5% in 2025 and 2026.

While our baseline inflation forecast has improved, risks to the inflation outlook are still assessed to the upside.

Even as global headline inflation moderates, oil markets are tight and core inflation is sticky. Despite recent easing in some food price components, domestic food price inflation remains volatile, and increased in October to 8.7%. El Niño conditions present longer-term concerns. Imported goods inflation has increased over the year, and despite some better recent outcomes, remains sensitive to currency weakness. Electricity prices continue to present clear inflation risks, and with logistics constraints, are likely to have broader effects on the cost of doing business and the cost of living. Given uncertain fuel and food price inflation, considerable risk still attaches to the forecast for average salaries.

Sticky inflation implies that average policy rates in G3 economies will remain high, at about 4.3% in 2024 compared to the 1.1% average rate seen in 2022.[11] These tighter global financial conditions will raise the risk profile of economies needing foreign capital. Sharply lower tax revenue, higher employee compensation and ongoing financing needs of state-owned enterprises are expected to keep South Africa’s long-term cost of borrowing elevated. Despite an expected moderation in inflation, long-term bond yields currently trade around 12%.

[11] G3 interest rates average 3.9% in 2023, 4.3% in 2024, and significantly higher at 3.4% in 2025 (up from 2.8%).

Higher inflation has generally resulted in elevated inflation expectations across markets, businesses and households. Market-based expectations for inflation in 2023 are currently 5.8%, while near-term break-even rates have dipped to 4.3%.[12] Medium and longer-term market expectations for inflation remain elevated. The September survey of the Bureau for Economic Research shows average inflation expectations lower at 6.1% for 2023. The Committee, however, would prefer to see expectations anchored at the mid-point of the inflation target band.[13]

Against this backdrop, the MPC decided to keep the repurchase rate at its current level of 8.25% per year. The decision was unanimous.

At the current repurchase rate level, policy is restrictive, consistent with the inflation outlook and elevated inflation expectations. Serious upside risks to the inflation outlook remain. In light of these risks, the Committee remains vigilant and stands ready to act should risks begin to materialise. Decisions will continue to be data dependent and sensitive to the balance of risks to the outlook. The inflation and repo rate projections from the updated QPM remain a broad policy guide, changing from meeting to meeting in response to new data and risks.

The policy stance aims to anchor inflation expectations more firmly around the mid-point of the target band and to increase confidence of attaining the inflation target sustainably over time.[14] The MPC will seek to look through temporary price shocks

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[12] At the median, market analysts (Reuters Econometer) in November expect inflation to average 5.8% in 2023, 4.9% in 2024 and 4.6% in 2025. Market-based rates are calculated from the break-even inflation rate, which is the yield differential between conventional and inflation-linked bonds. The 10-year breakeven now sits at about 6.1%. The 20-year break-even inflation rate sits at 7.2%.

[13] The BER Q3 2023 survey of inflation expectations indicated inflation at 6.1% in 2023 (from 6.5% in Q2) and 5.5% for 2024 (from 5.9% in Q2) and 5.3% in 2025. The Bureau's next release is the second week of December.

[14] The forecasted trajectory for the repurchase rate implies a rise in the inflation-adjusted repo rate from -1.3% in 2022, to 2.7% in 2023, and 3.2% in 2024. The real repo level for 2025 is expected to be 2.9%. The real

and focus on potential second round effects and the risks of de-anchoring inflation expectations.

Guiding inflation back towards the mid-point of the target band reduces the economic costs of high inflation and will achieve lower interest rates in the future. Since early 2020, the Committee has recommended additional means of lowering inflation that are within the reach of the public sector, including achieving a prudent public debt level, increasing the supply of energy, keeping administered price inflation low and real wage growth in line with productivity gains. Such steps would strengthen monetary policy effectiveness and its transmission to the broader economy.

Lesetja Kganyago
GOVERNOR
The next statement of the Monetary Policy Committee will be released on 25 January 2024.

The MPC dates for 2024 are:
25 January
27 March
30 May
18 July
19 September
21 November

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repurchase rates calculated here are based on the 3-quarter ahead inflation forecast and are annual average rates.