



Figure 1: SA consumer inflation: history and forecasts

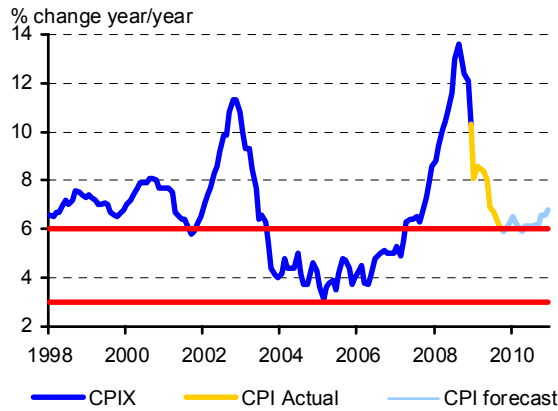


Figure 2: Year/year inflation (%)

	Nov 2009	Oct 2009	Nov 2008	Investec Forecast	Consensus Estimate
CPI	5.8	5.9	12.1	5.9	5.9

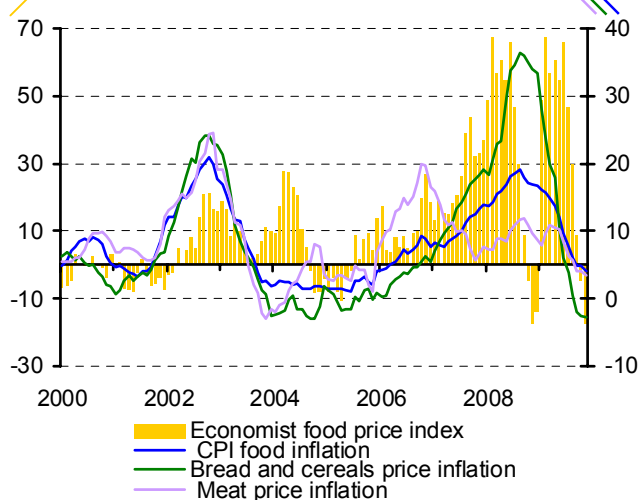
Note: *2008 CPIX

Figure 3: CPI month/month inflation (%)

	Nov 2009	Oct 2009
Food and alcoholic beverages		0.1
Miscellaneous goods and services		
Housing and utilities		
Transport		-0.2
Residual		0.1
Total	0.0	0.0

CPI: Consumer Price Index.

Figure 4: Change in domestic and international food prices, y/y, %



Sources: Statistics SA

Executive summary:

- CPI inflation remained in the target range in November, at 5.8% y/y (5.9% y/y previously). However, it is unlikely to remain below 6% over the next six months due to base and seasonal effects – December’s outcome is expected at 6.2% y/y;
- The rand has remained relatively stable around R7.40/USD, which we continue to believe will be the average outcome for Q4.09 and its trade-weighted strength has contributed to the inflation target being attained. We believe that the domestic currency will average R7.20/USD in Q1.10, strengthening further on an effective basis – which will push CPI inflation back within target in March 2010;
- Food price deflation continues at the global commodities level, which along with weak demand in SA, has caused retail price increases to moderate, a key reason for the headline figure re-entering the target band. We expect an increase in food price inflation over the festive season, but then the downward trend should continue, if not sharpen in Q1.10;
- With well over a million jobs lost in the 2008/2009 recession, a downward trend in CPI inflation is only to be expected, indeed what little inflationary pressure there is is emanating from administered prices. This situation will only be exacerbated when Eskom institutes its still hefty tariff hike in the middle of next year, should the 35% be approved;
- We continue to believe there will be no more interest rate cuts in the current cycle, unless the SA economy’s performance deteriorates significantly. With global recovery seemingly under way, this should drive the domestic performance with the demand side and job creation lagging behind.

Analysis of mooted 35% electricity tariff increase in 2010:

Eskom’s application for a 35% tariff increase, if approved, will add 0.65% to the monthly inflation rate in July 2010, or push CPI inflation up from (our estimated) 5.3% y/y to 6.0% y/y in one go. Once inflation is back at the 6.0% mark, second and third round effects will keep it out of the inflation target as long as increases as large as 35% per year occur, and in the absence of strong external deflationary/ disinflationary pressures. The second round effects on the manufacture and sale of goods due to a 250% increase in electricity tariffs (the cumulative impact of 35% per annum increases in tariffs over three years) will clearly result in both significantly higher costs of doing business and living, and make SA’s exports less competitive. Third round effects occur when the higher cost of living/doing business becomes entrenched, resulting in rising salary and wage increases (the first round effect is the electricity tariff increase’s impact on inflation alone, the second round effect the higher cost of production and living).

Outlook

Today’s outcome does not change our view either in terms of the future path of interest rates or inflation. With the demand side of the economy still in recession and only likely to emerge from it in early 2010, there is little chance of any interest rate hikes before Q4.10. Even this monetary tightening at the end of next year will be heavily dependent on economic performance and may well be delayed until 2011. With job losses still likely in Q4.09, and not much job creation in 2010, any decision to hike rates will be very unpopular. The move forecast in Q4.10 is based on the belief that monetary policy will be returned to a more neutral stance, should the strengthening economy warrant it. Electricity tariff increases of even 35% will keep inflation CPI inflation out of target in 2011 from when the tariff hikes are instituted, particularly due to second and third round effects.



SA Economic Research CPI Update

Disclaimer

The information and materials presented in this report are provided to you for information purposes only and are not to be considered as an offer or solicitation of an offer to sell, buy or subscribe to any financial instruments. This report is intended for use by professional and business investors only. This report may not be reproduced in whole or in part or otherwise, without the consent of Investec.

The information and opinions expressed in this report have been compiled from sources believed to be reliable, but neither Investec, nor any of its directors, officers, or employees accepts liability for any loss arising from the use hereof or makes any representation as to its accuracy and completeness.

Investec, and any company or individual connected to it including its directors and employees may to the extent permitted by law, have a position or interest in any investment or service recommended in this report. Investec may, to the extent permitted by law, act upon or use the information or opinions presented herein, or research or analysis on which they are based before the material is published.

Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied is made regarding future performance. Information, opinions and estimates contained in this report reflect a judgement at its original date of publication by Investec and are subject to change.

Investec is not agreeing to nor required to update research commentary and data. Therefore, information may not reflect events occurring after the date of publication. The value of any securities or financial instruments mentioned in this report can fall as well as rise. Foreign currency denominated securities and financial instruments are subject to fluctuations in exchange rates that may have a positive or adverse effect on the value, price or income of such securities or financial instruments. Certain transactions, including those involving futures and options, can give rise to substantial risk and are not suitable for all investors.

Investec may have issued other reports that are inconsistent with, and reach different conclusions from, the information presented in this report. Those reports reflect the different assumptions, views and analytical methods of the analysts who prepared them.

To our readers in Australia this does not constitute and is not intended to constitute financial product advice for the purposes of the Corporations Act.

To our readers in the United Kingdom: This report has been issued and approved by Investec Bank (UK) Limited, a firm regulated by the Financial Services Authority Limited and is not for distribution in the United Kingdom to private customers as defined by the rules of the Financial Services Authority Limited.

To our readers in the Republic of Ireland, this report is issued in the Republic of Ireland by Investec Bank (UK) Limited (Irish Branch), a firm regulated by the Financial Services Authority.

This report is disseminated in South Africa by Investec Bank Limited, a firm regulated by the South African Reserve Bank and in Switzerland by Investec Bank (Switzerland) AG.

This report is not intended for use or distribution in the United States or for use by any citizen or resident of the United States.