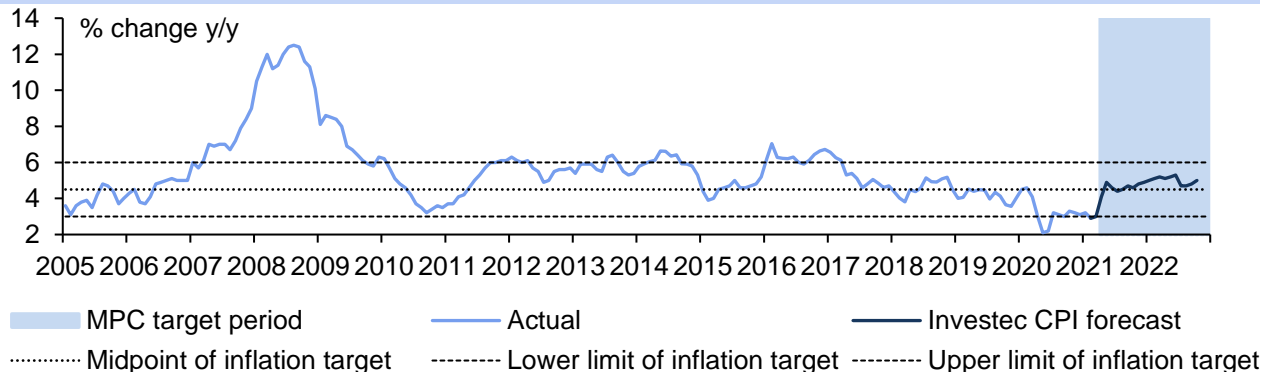




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Figure 1: SA Consumer Inflation: history and forecasts



Source: Stats SA, SARB, Investec

- The SARB’s monetary policy committee (MPC) unanimously decided to keep the repo rate unchanged at 3.50%. The implied policy rate path of the SARB’s Quarterly Projection Model (QPM) now indicates two increases of 25 basis points each in the second and fourth quarters of 2021, as opposed to the second and third quarters as indicated in the previous meeting. This shift in the rate path “is due to somewhat lower inflation in 2022”, according to the SARB. However, the SARB continuously reiterates that the repo rate estimate derived from the QPM “(r)emains a broad policy guide, changing from meeting to meeting in response to new data and risks,” particularly in this highly volatile environment.
- Following a subdued average CPI inflation rate of 3.3%, the SARB’s inflation expectations for this year have increased, but continue to remain below the mid-point of the inflation targeting band for 2021 at 4.3% (the forecast for 2021 was 4.0% previously). Its 2022 and 2023 projections have been lowered slightly to 4.4% (from 4.5% previously) and 4.5% (from 4.6%).
- Overall risks to the inflation trajectory continue to be perceived as balanced. Specifically, domestic food price inflation is “slightly lower than previously expected”, according to the SARB and is likely to remain relatively contained, with another bumper harvest anticipated. Indeed, the “favourable weather conditions that underpinned higher agricultural output in 2020 have continued into 2021”, according to Agbiz.
- Furthermore, the marked but temporary decline in medical insurance price inflation this year will have a moderating affect on the headline reading.
- The domestic currency has appreciated by 1.3% against the greenback on a trade weighted basis since the January MPC meeting and the implied starting point for the rand forecast has thus been adjusted to R14.96/USD (from R15.70/USD). Accommodative conditions in advanced economies and the more favourable global economic view should continue to “(s)upport global financial markets and strengthen international capital flows.”

Figure 2: SARB CPI inflation forecasts (% y/y)

	2019	2020	2021	2022
SARB 25 th March 2021	4.1	3.3	4.3	4.4
SARB 21 st January 2021	4.1	3.3	4.0	4.5
SARB 19 th November 2020	4.1	3.2	3.9	4.4
SARB 17 th September 2020	4.1	3.3	4.0	4.4
SARB 23 rd July 2020	4.1	3.4	4.3	4.3
SARB 21 st May 2020	4.1	3.4	4.4	4.4
SARB 14 th April 2020	4.1	3.6	4.5	4.4

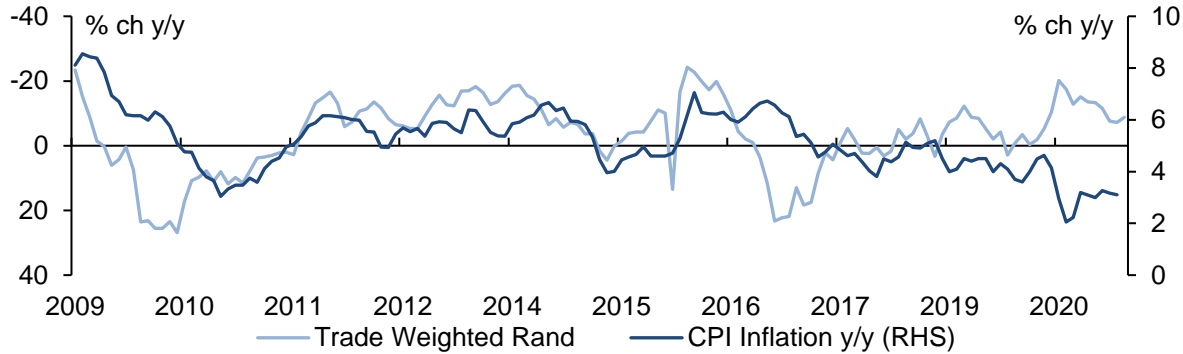
Source: SA Reserve Bank



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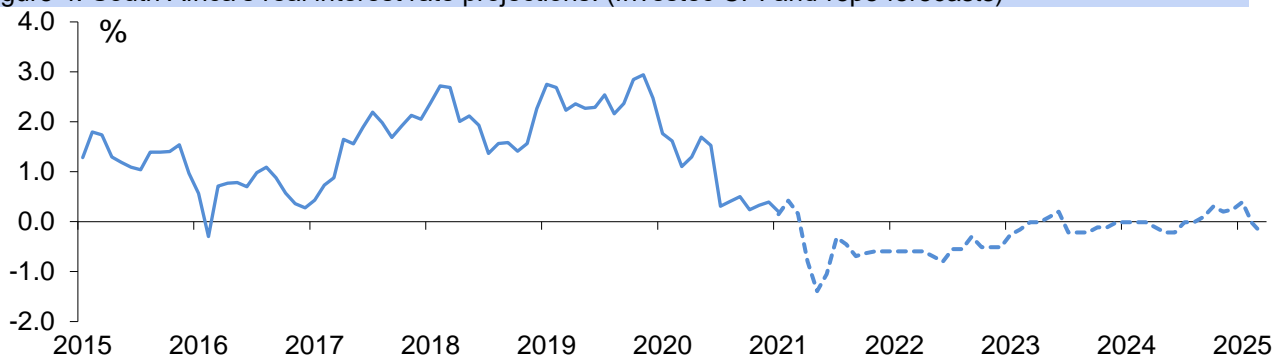
Figure 3: Trade weighted rand movements vs CPI inflation (both % change y/y)



Source: Stats SA, Iress

- Conversely, fuel, electricity and other administered price increases continue to remain upside risks to the inflation trajectory. Indeed, oil prices have climbed markedly this year and are expected to remain elevated over the SARB’s “forecast horizon”. Oil prices have thus been amended in the forecast, “resulting in higher petrol price inflation, at 12.7% for 2021, compared to 4.4% at the time of the January meeting.”
- While the country’s vaccine rollout, although slower than anticipated, has provided a degree of optimism, risks of further spikes in infection rates remain, with a third wave likely as we head into winter. Additionally, electricity supply constraints continue to hinder economic activity, with heightened rotational loadshedding experienced in March.
- Following 2020’s -7.0% decline, GDP is forecast to lift by 3.8% this year, a slight increase from 3.6% projected at the January MPC meeting. However, “(s)harply lower public and private investment last year and continued weakness in 2021 will weigh on growth prospects”. Growth is thus projected to moderate to 2.4% and 2.5% in 2022 and 2023 respectively (unchanged from January’s meeting). The SARB continues to evaluate the risks to the domestic growth outlook to be balanced.
- “Monetary policy continues to be accommodative, keeping financial conditions supportive of credit demand as the economy recovers from the pandemic and associated lockdowns,” however the implementation of “prudent macroeconomic policies and structural reforms,” remains critical to long term, sustainable growth.

Figure 4: South Africa’s real interest rate projections: (Investec CPI and repo forecasts)



Source: Investec, Iress

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Figure 5: Foreign sector assumptions

Percentage changes (unless otherwise indicated)	2018	Actual 2019	2020	2021	Forecast 2022	2023
1. Real GDP growth in South Africa's major trading partner countries	3.3% (3.3%)	2.2% (2.2%)	-3.1% (-3.6%)	5.8% (5.0%)	3.7% (3.8%)	3.3% (3.4%)
2. Output gap in South Africa's major trading partner countries	0.6% (0.2%)	0.4% (-0.1%)	-2.7% (-2.8%)	-1.6% (-2.5%)	-0.4% (-0.1%)	0.3% (0.1%)
3. International commodity prices in US\$ (excluding oil)	11.5% (11.5%)	-1.1% (-1.1%)	25.5% (25.4%)	23.3% (14.8%)	-13.0% (-13.0%)	0.0% (-0.5%)
4. Brent crude (US\$/Barrel)	\$71.0 (\$71.0)	\$64.4 (\$64.4)	\$41.8 (\$41.8)	\$62.0 (\$50.0)	\$60.0 (\$55.0)	\$60.0 (\$57.0)
5. World food prices (US\$)	-2.2% (-2.2%)	-0.8% (-0.8%)	3.1% (2.5%)	4.5% (2.9%)	1.7% (1.5%)	1.4% (1.5%)
6. International consumer prices	2.0% (2.0%)	1.4% (1.4%)	0.8% (0.8%)	1.6% (1.5%)	1.6% (1.5%)	1.8% (1.7%)
7. International policy interest rate	0.9% (0.9%)	1.1% (1.1%)	0.2% (0.2%)	0.0% (0.0%)	0.0% (0.0%)	0.0% (0.0%)

Figures in blue represents the previous MPC assumption

Foreign Sector Assumptions

- Trading partner GDP growth:** is broadly determined via the Global Projection Model "GPM" which is adjusted to aggregate the GDP growth rates of South Africa's major trading partners on a trade weighted basis. Individual projections are done for the four largest trading partners (euro area, China, United States and Japan), while the remaining trading partners are grouped into three regions: Emerging Asia (excluding China), Latin America and the Rest of Countries bloc. The assumption takes account of country specific "consensus" forecasts as well as regional growth prospects.
- Output gap:** as with GDP growth the output gap is determined via the GPM and is similarly adjusted. The output gap is driven by a combination of country-specific domestic factors, external factors, and financial-real linkages (beyond interest rate and exchange rate effects). Domestic factors include expectations of future demand and medium-term interest rates. External factors include exchange rate impacts on demand, direct spillovers through trade with trading partner countries, and foreign demand.
- International consumer prices:** are also broadly determined via the GPM, the index is an aggregate of the consumer price indices of the G3 countries (euro area, United States and Japan) weighted by their relative trade weights. Consumer prices are determined for each region discussed above by accounting for expected future price inflation, demand pressures, and pass-through from changes in the relevant exchange rate. Other institutional forecasts for international consumer prices are also considered.
- Commodity price index:** is a weighted aggregate price index of the major South African export commodities based on 2010 prices. The composite index represents the total of the individual commodity prices multiplied by their smoothed export weights. Commodity price prospects generally remain commensurate with global liquidity as well as commodity demand/supply pressures as reflected by the pace of growth in the trading partner countries.
- Brent crude oil price:** is expressed in US Dollars per barrel. The assumption incorporates the analysis of factors of supply, demand (using global growth expectations) and inventories of oil (of all grades), as well as the expectations of the US Energy Information Administration (EIA), OPEC and Reuters.
- World food prices:** is the composite food price index of the Food and Agriculture Organization of the United Nations (FAO) in US dollars. It is weighted via average export shares, and represents the monthly change in the international prices of a basket of five food commodity price indices (cereals, vegetable oil, dairy, meat and sugar). World food price prospects incorporate selected global institution forecasts for food prices as well as imbalances from the anticipated trend in international food supplies relative to expected food demand pressures.

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7. **International policy interest rate:** is again broadly determined via the GPM. Interest rates are an aggregate of the policy rates of the G3 countries (euro area, United States and Japan). They are individually determined by a "Taylor-type" monetary policy rule. The communications of the relevant central banks and other institutional forecasts are also considered.

Figure 6: Domestic sector assumptions

Percentage changes (unless otherwise indicated)	2018	Actual 2019	2020	2021	Forecast 2022	2023
1. Electricity price	5.2% (5.2%)	9.6% (9.6%)	9.1% (9.1%)	9.7% (8.2%)	11.4% (10.0%)	10.0% (10.0%)
2. Fuel taxes and levies	8.9% (8.9%)	5.8% (5.8%)	5.7% (5.7%)	5.1% (5.5%)	4.9% (5.0%)	4.7% (4.7%)
3. Potential growth	0.7% (0.7%)	0.3% (0.3%)	-2.5% (-2.5%)	1.6% (1.6%)	0.9% (0.9%)	0.9% (0.9%)
4. Inflation target midpoint	4.5% (4.5%)	4.5% (4.5%)	4.5% (4.5%)	4.5% (4.5%)	4.5% (4.5%)	4.5% (4.5%)
5. Neutral real interest rate	1.9% (1.9%)	2.1% (2.1%)	2.0% (2.0%)	2.1% (2.1%)	2.3% (2.3%)	2.3% (2.3%)

Source: SA Reserve Bank

Figures below the assumption in parentheses represents the previous MPC assumption

Domestic Sector Assumptions

- Fuel taxes and levies:** are the total domestic taxes and costs included in the price of fuel paid at the pump. They include the Road Accident Fund (RAF), the fuel levy, retail and wholesale margins, slate levy, and other minor levies. The two major taxes, which are set by the Minister of Finance in the annual budget, are the RAF and fuel levy. Income generated by the RAF levy is utilised to compensate third party victims of motor vehicle accidents while the fuel levy is used to provide funding for road infrastructure.
- Electricity price:** is an administered price measured at the municipal level with a weight of 3.75 per cent in the headline CPI basket. Electricity price adjustments generally take place in the months of July and August of each year, and the assumed pace of increase over the forecast period reflects the multi-year price determination (MYPD) agreement between Eskom and NERSA with a slight adjustment for measurement at the municipal level.
- Potential growth:** the pace of potential growth is derived from the SARB's semi-structural potential output model. The measurement accounts for the impact of the financial cycle on real economic activity and introduces economic structure via the relationship between potential output and capacity utilisation in the manufacturing sector (South African Reserve Bank, Working Paper Series, WP/14/08).
- Inflation target midpoint:** is the middle of the official target range of 3 to 6 percent.
- Neutral real interest rate:** The neutral real interest rate is the rate at which inflation is stable at the inflation target midpoint and output is operating at its potential. It is a key variable to determine the appropriate stance of monetary policy. The neutral real interest rate is a function of the model consistent real interest rate.

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