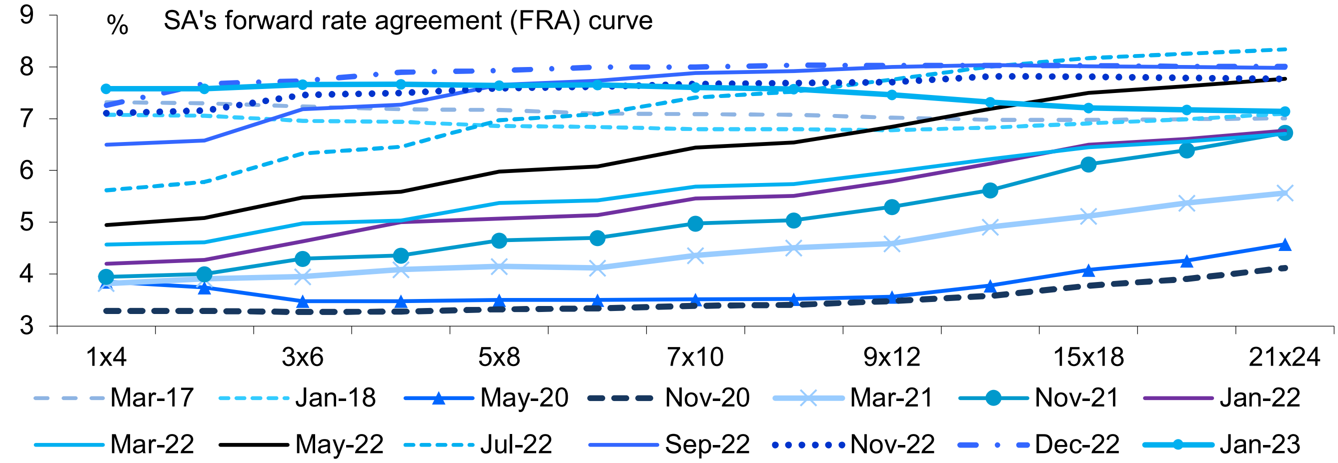
Investec

MPC preview: SARB to hike again

Friday 13th January 2023

Figure 1: Forward Rate Agreement (FRA) curve



Source: Bloomberg

South Africa's Monetary Policy Committee (MPC) will see its next interest rate decision on 26th January, while the FOMC's next rate decision will be announced on 1st February. This comes after the FOMC dropped its interest rate increase in December, from 75bp to 50bp, with SA potentially doing the same this month. However, market expectations for the next expected US rate hike (1st February) have now dropped to close to 25bp, after yesterday's release of its CPI inflation data. The US core CPI inflation measure fell to 5.7% y/y in December, from 6.0% y/y. This measure, CPI excluding food and energy, is still well above 2.0% y/y however and does not signal an end to US interest rate hikes, nor definitely a drop to hiking in 25bp instead of 50bp increments in the near term. The last time the core measure was at 5.7% was in 1982, and is still indicating that price increases are heady, despite dropping from July's peak of 6.6% y/y. US inflation data is nevertheless showing some signs of cooling, and the drop in the overall CPI, to 6.5% y/y from 7.1% y/y, also released yesterday and for December, was more marked. On a month on month basis, the index fell by 0.1%, the first drop since H1.22. Energy and goods prices accounted for the decline, while food and services (excluding food and energy) prices rose. In particular, the drop in motor vehicles and gasoline drove the moderation and hopes that inflation in the US will continue to drop lower (disinflation), aiding an even slower US rate hike cycle. US food prices showed their smallest increase since Q1.21, but rental costs remained elevated, while utilities costs rose more quickly. The US Labor Department also published a report on the labour market showing initial claims for state unemployment benefits dropped by 1 000 individuals, to 205 000 (seasonally adjusted) and concerns persist over the tight labour market.

In South Africa, CPI inflation is expected to fall to 7.2% y/y in December's publication due out next week Wednesday, dropping from 7.4% y/y, while core inflation could drop to 4.7% y/y from 5.0% y/y. With CPI inflation still well above the target, and risks to the outlook, the SARB is likely to hike the repo rate again this month, but we expect it could be by 50bp instead of the 75bp moves recently. Inflation is proving slow to subside in SA, but this should accelerate in H1.23 on base effects.

Figure 2: Forecasts

Period end rate %	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.24	Q4.23
Repo Rate	4.25	4.75	6.25	7.00	7.50	7.50	7.00	7.00
Prime Overdraft Rate	7.75	8.25	9.75	10.50	11.00	11.00	10.50	10.50

Source: Iress, Investec

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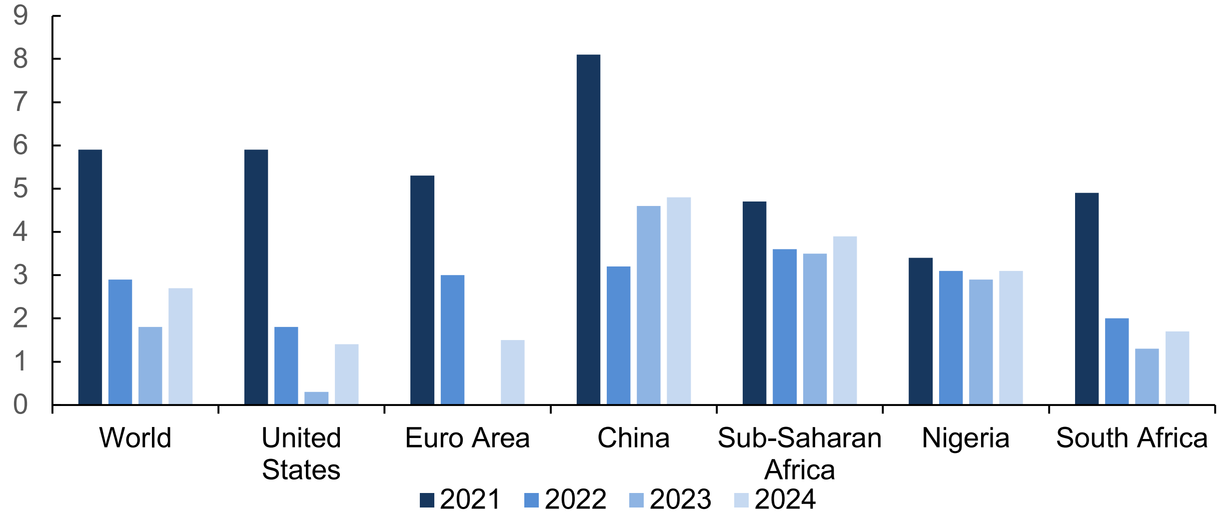
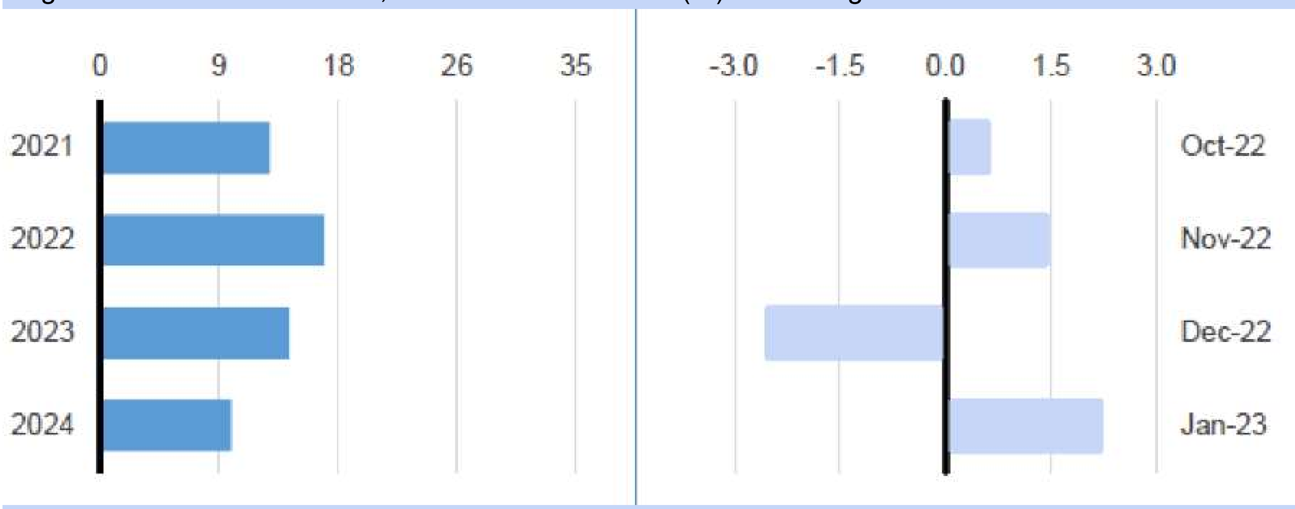
Figure 3: Major Economies and Sub-Saharan Africa, Real GDP, annual variation in %



Source: Focus Economics January 2023

Figure 4: Sub-Saharan Africa, 2023: 13.9% - inflation (%) and change in forecast



Source: Focus Economics January 2023

Figure 5: Reuters December 2022 forecasts: Repo rate %

Forecast period	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	2022	2023	2024
Repo rate %	7.50	7.50	7.50	7.25	7.00	7.00	7.25	6.75
Previous survey	7.25	7.25	7.25	7.00	7.00	7.00	7.00	6.75

Source: Reuters

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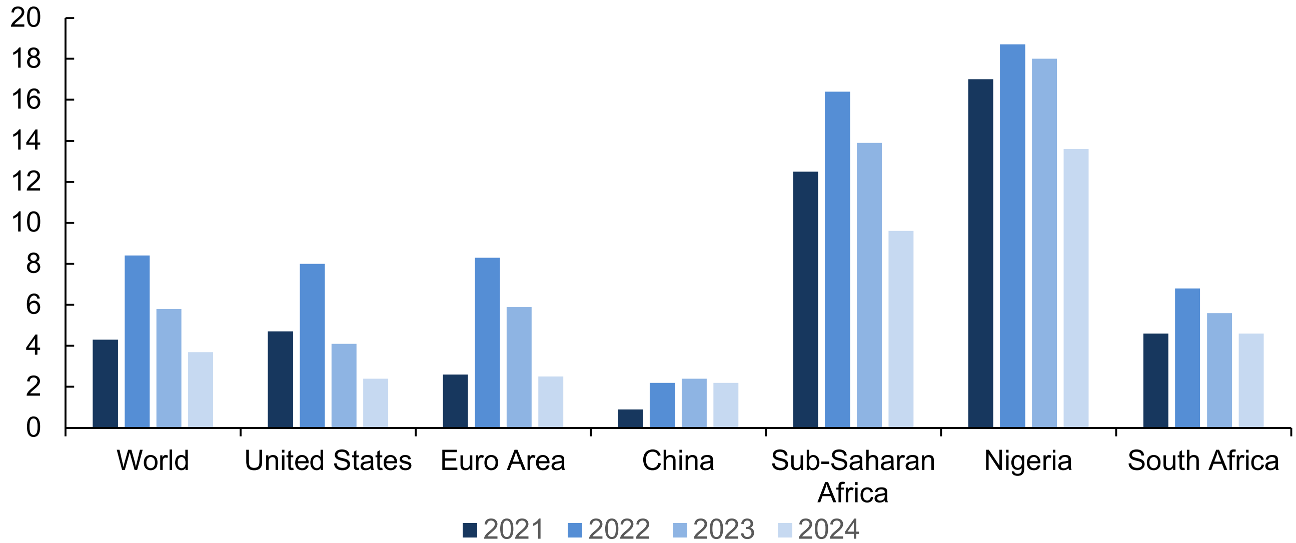
Figure 6: Major Economies and Sub-Saharan Africa consumer prices, annual variation in %



Source: Focus Economics January 2023

Looking forward, SA will see upwards pressure coming from the larger than expected increase in electricity prices announced late yesterday by NERSA, with an 18.65% rise "based on … (the) approved tariff of 146.48c/kWh in the 2022/23 financial year". With Stats SA typically capturing the annual electricity price increase for CPI inflation in July, it translates to around a 0.7% m/m contribution. Absent a very sharp rise in fuel prices in the month, or another shock, the CPI inflation outcome for the month of July 2023 could actually drop to 4.3% y/y, from 4.9% y/y in June, as base effects from H1.22's high fuel and food price increase will still have an effect. However, H2.23, if not the middle of 2023 already, risks seeing higher fuel prices on a reopening of the Chinese economy, while a significantly milder slowdown in economic activity than anticipated this year would also place additional pressure on prices.

For South Africa's monetary policy, much will depend on the rapidity of the decline in US inflation (particularly

Figure 7: Reuters December 2022 forecasts: CPI % y/y

Forecast period	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	2022	2023	2024
CPI % y/y	7.4	6.9	5.8	4.9	4.9	4.9	6.9	5.6	4.6
Previous survey	7.2	6.9	5.7	4.6	4.7	4.6	6.8	5.5	4.5

Source: Reuters

Figure 8: Inflation forecasts	2022	2023	2024	2025	2026	2027
Consumer Inflation (Av: %)	6.9	5.3	4.7	5.0	5.0	5.1
Producer Inflation (Av: %)	14.4	7.4	4.8	5.1	5.1	5.0
Salary & wage increases (%)	4.2	5.4	5.1	5.5	5.4	5.4

Source: Investec

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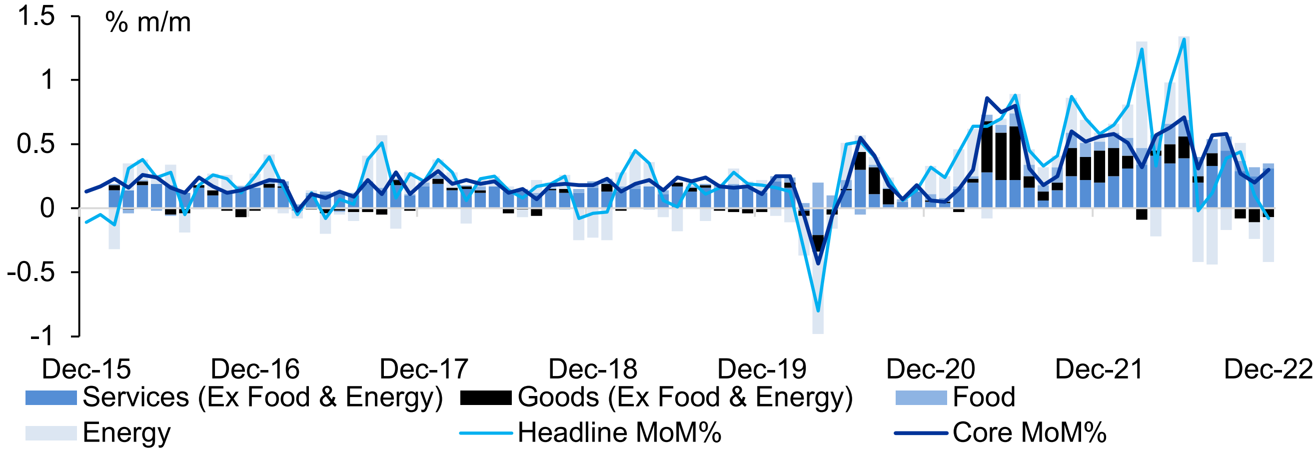
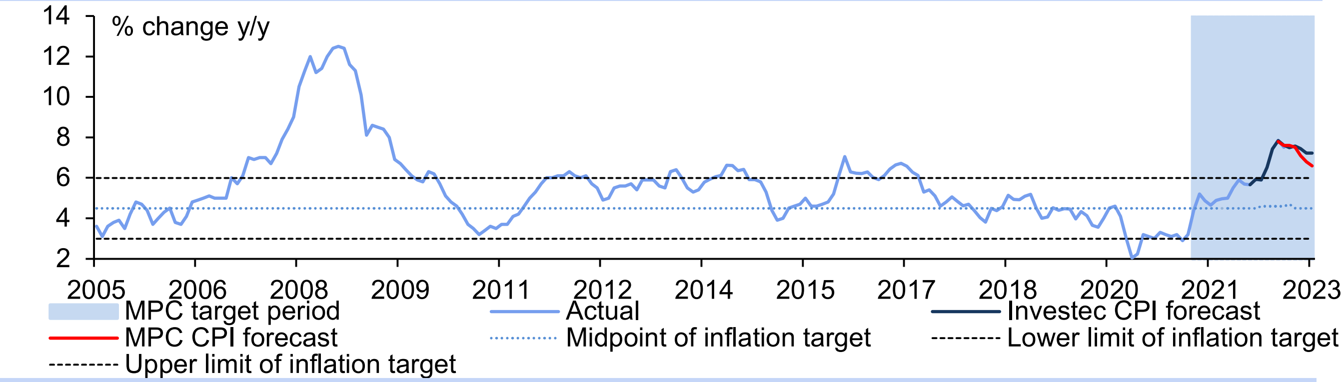
Figure 9: Top-Line contributions to US CPI mom % (sa), and core CPI



Source: Bloomberg

Figure10: SA Consumer Inflation: history and forecasts



Source: Stats SA, SARB, Investec

Figure 11: Reuters November 2022 Foreign exchange rates poll: USDZAR

	1M	3M	6M	1Y
Release/Effective Date	30 Nov 2022	31 Jan 2023	28 Apr 2023	31 Oct 2023
Median	18.2500	18.0000	17.8350	17.0950
High	18.7500	19.2500	19.6700	18.0000
Low	17.2000	15.9000	15.6300	15.3000
No. of forecasts	15	19	20	18

Source: Reuters

Figure 12: Reuters December 2022 forecasts: GDP

Forecast period	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	2022	2023	2024
GDP y/y %	0.9	0.9	1.1	1.2	1.2	1.1	2.1	1.2	1.7
Previous survey	1.0	1.2	1.6	1.6	1.8	0.7	1.9	1.4	1.8

Source: Reuters

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13: SA Monetary Policy Committee (MPC) meeting dates for 2023		
Month	Date	Forecast
January	24th – 26th January	7.50
March	28th March – 30th March	7.50
May	23rd May – 25th May	7.50
July	18th July – 20th July	7.00
September	19th – 21st September	7.00
November	21st -23rd November	7.00

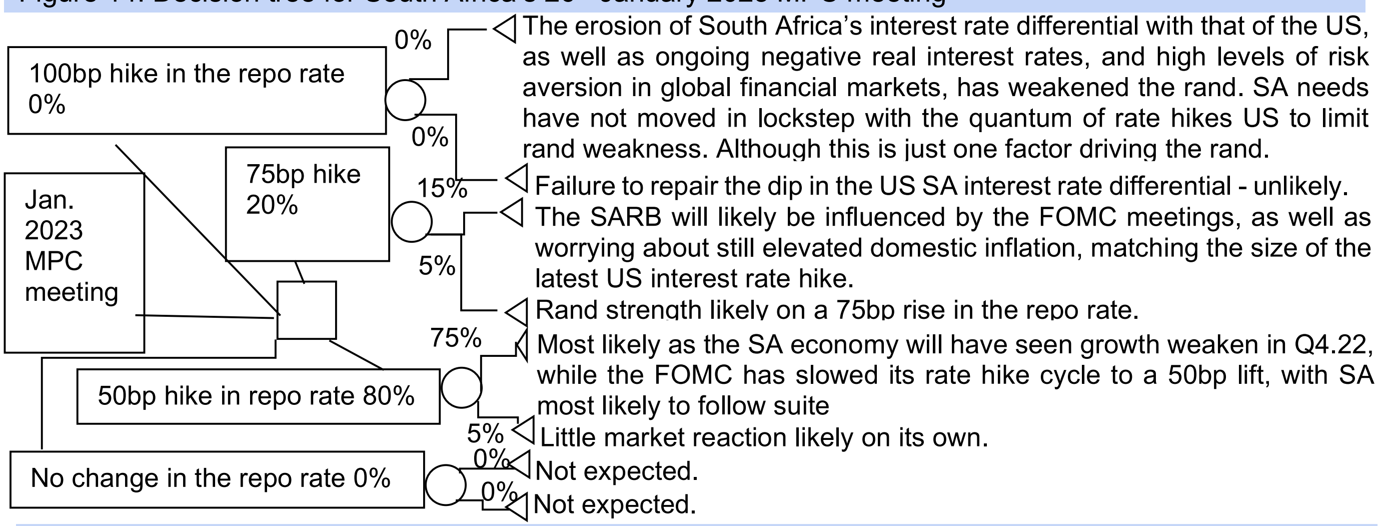
Source: SA Reserve Bank, Investec

Figure 14: Forecasts	2022	2023	2024	2025	2026	2027
Repo Rate	7.00	7.00	6.50	6.50	6.50	6.50
Prime Overdraft rate	10.50	10.50	10.00	10.00	10.00	10.00
SA rand bond	11.55	10.90	10.50	10.10	10.00	9.90
US Fed funds rate	4.50	4.25	2.75	2.50	2.50	2.50
UK Bank rate	3.50	3.25	2.25	2.50	2.50	2.50

Note: forecasts are *% year-end.* Source: Investec, SARB, IRESS

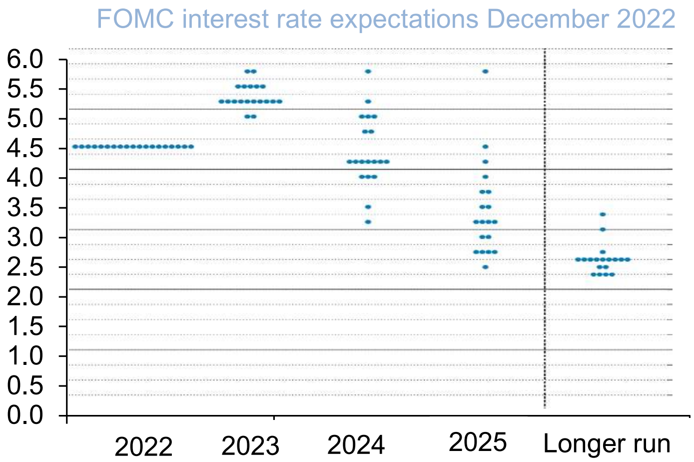
core PCE), and the pace of slowing in the US rate hike cycle, while the higher interest rates SA has already experienced will have a particularly negative impact on over-indebted consumers over Q1.23. If the FOMC slows its rate hike to 25bp in February, not currently indicated by the Fed's dot plot chart of its members interest rate forest for the year/s ahead, this would create space for SA to slow its interest rate increases as well. The SARB is not expected to hike rates by 75bp this month but narrowing the interest rate differential would be one reason it may consider doing so. South Africa's inflation rate at the retail level eased to 6.8% y/y from figures published by Stats SA for October, from 6.9% y/y in September, with the easing likely indicating some increased consumer financial vulnerability. Risks to the outlook also include a weaker than expected domestic growth rate as severe load shedding persist this year, and a further loss in investor sentiment.

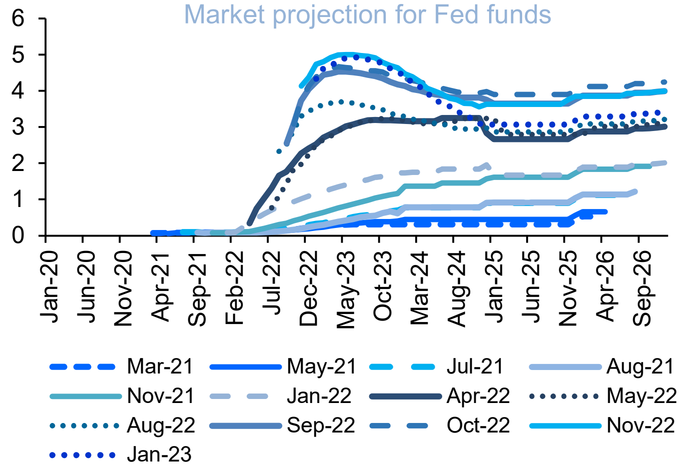
Figure 14: Decision tree for South Africa's 26th January 2023 MPC meeting



Key: squares are decision nodes; circles are chance nodes and triangles end nodes. Source: Investec

Figure 16: US interest rate projections





Source: FOMC, Bloomberg

Figure 17: FOMC /2023 Meeting Schedule

31st January–1st February 2023
21st-22nd March 2023
2nd-3rd May 2023
13th-14th June 2023
25th-26th July 2023
19th-20th September 2023
31st October-1st November 2023
12th-13th December 2023

Source: Federal Reserve Bank

Figure 18: Forecast of international interest rates (%, end quarter)

	US Fed funds	Euro zone Refi rate	Euro zone deposit rate	UK Bank Rate
Current	3.75-4.00	2.00	1.500	3.00
Q1.22	0.25-0.50	0.00	-0.50	0.75
Q2.22	1.50-1.75	0.00	-0.50	1.25
Q3.22	3.00-3.25	1.25	0.75	2.25
Q4.22	4.25-4.50	2.50	2.00	3.50
Q1.23	4.50-4.75	2.50	2.25	4.00
Q2.23	4.50-4.75	2.50	2.25	4.00
Q3.23	4.50-4.75	2.50	2.25	3.75
Q4.23	4.00-4.25	2.25	2.00	3.25

Source: Macrobond, Investec

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Figure 19: Interest rate forecast end rates

Date	Prime forecast	Prime less Inflation	Repo	Repo less Inflation
Jan 2020	9.75	5.2	6.25	1.7
Feb 2020	9.75	5.0	6.25	1.5
Mar 2020	8.75	4.6	5.25	1.1
Apr 2020	7.75	4.7	4.25	1.2
May 2020	7.25	5.3	3.75	1.8
Jun 2020	7.25	5.0	3.75	1.5
Jul 2020	7.00	3.8	3.50	0.3
Aug 2020	7.00	3.9	3.50	0.4
Sep 2020	7.00	4.0	3.50	0.5
Oct 2020	7.00	3.7	3.50	0.2
Nov 2020	7.00	3.8	3.50	0.3
Dec 2020	7.00	3.9	3.50	0.4
Jan 2021	7.00	3.8	3.50	0.3
Feb 2021	7.00	4.2	3.50	0.7
Mar 2021	7.00	3.8	3.50	0.3
Apr 2021	7.00	2.6	3.50	-0.9
May 2021	7.00	1.8	3.50	-1.7
Jun 2021	7.00	2.1	3.50	-1.4
Jul 2021	7.00	2.3	3.50	-1.2
Aug 2021	7.00	2.1	3.50	-1.4
Sep 2021	7.00	2.0	3.50	-1.5
Oct 2021	7.00	2.0	3.50	-1.5
Nov 2021	7.25	1.8	3.75	-1.7
Dec 2021	7.25	1.3	3.75	-2.2
Jan 2022	7.50	1.8	4.00	-1.7
Feb 2022	7.50	1.8	4.00	-1.7
Mar 2022	7.75	1.8	4.25	-1.7
Apr 2022	7.75	1.9	4.25	-1.6
May 2022	8.25	1.7	4.75	-1.8
Jun 2022	8.25	0.8	4.75	-2.7
Jul 2022	9.00	1.2	5.50	-2.3
Aug 2022	9.00	1.4	5.50	-2.1
Sep 2022	9.75	2.3	6.25	-1.2
Oct 2022	9.75	2.2	6.25	-1.3
Nov 2022	10.50	3.1	7.00	-0.4
Dec 2022	10.50	3.3	7.00	-0.2

Source: IRESS, Investec

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Figure 20: Interest rate forecast end rates (continued)

Date	Prime forecast	Prime less Inflation	Repo	Repo less Inflation
Jan 2023	11.00	3.8	7.50	0.3
Feb 2023	11.00	4.0	7.50	0.5
Mar 2023	11.00	4.5	7.50	1.0
Apr 2023	11.00	4.7	7.50	1.2
May 2023	11.00	5.2	7.50	1.7
Jun 2023	11.00	6.1	7.50	2.6
Jul 2023	10.50	6.2	7.00	2.7
Aug 2023	10.50	6.2	7.00	2.7
Sep 2023	10.50	6.0	7.00	2.5
Oct 2023	10.50	5.9	7.00	2.4
Nov 2023	10.50	5.9	7.00	2.4
Dec 2023	10.50	6.1	7.00	2.6
Jan 2024	10.00	5.3	6.50	1.8
Feb 2024	10.00	5.4	6.50	1.9
Mar 2024	10.00	5.2	6.50	1.7
Apr 2024	10.00	5.2	6.50	1.7
May 2024	10.00	5.1	6.50	1.6
Jun 2024	10.00	5.1	6.50	1.6
Jul 2024	10.00	5.3	6.50	1.8
Aug 2024	10.00	5.3	6.50	1.8
Sep 2024	10.00	5.3	6.50	1.8
Oct 2024	10.00	5.5	6.50	2.0
Nov 2024	10.00	5.5	6.50	2.0
Dec 2024	10.00	5.7	6.50	2.2
Jan 2025	10.00	5.6	6.50	2.1
Feb 2025	10.00	4.8	6.50	1.3
Mar 2025	10.00	4.6	6.50	1.1
Apr 2025	10.00	4.8	6.50	1.3
May 2025	10.00	5.0	6.50	1.5
Jun 2025	10.00	5.0	6.50	1.5
Jul 2025	10.00	5.0	6.50	1.5
Aug 2025	10.00	4.9	6.50	1.4
Sep 2025	10.00	4.9	6.50	1.4
Oct 2025	10.00	5.0	6.50	1.5
Nov 2025	10.00	5.1	6.50	1.6
Dec 2025	10.00	5.0	6.50	1.5

Source: IRESS, Investec

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Figure 21: CPI forecast averages

Date	Index Base 2016	Annual y/y	Monthly m/m	Quarterly y/y	Calendar year y/y	
Jan 2020	91.9	4.6	0.3			
Feb 2020	92.8	4.7	1.0			
Mar 2020	93.1	4.1	0.3	4.5		
Apr 2020	92.6	3.0	-0.5			
May 2020	92.0	2.0	-0.6			
Jun 2020	92.5	2.2	0.5	2.4		
Jul 2020	93.7	3.2	1.3			
Aug 2020	93.9	3.1	0.2			
Sep 2020	94.0	3.0	0.1	3.1		
Oct 2020	94.3	3.3	0.3			
Nov 2020	94.3	3.2	0.0			
Dec 2020	94.4	3.1	0.1	3.2	2020	3.3
Jan 2021	94.8	3.2	0.4			
Feb 2021	95.4	2.8	0.6			
Mar 2021	96.1	3.2	0.7	3.1		
Apr 2021	96.7	4.4	0.6			
May 2021	96.8	5.2	0.1			
Jun 2021	97.0	4.9	0.2	4.8		
Jul 2021	98.1	4.7	1.1			
Aug 2021	98.5	4.9	0.4			
Sep 2021	98.7	5.0	0.2	4.9		
Oct 2021	99.0	5.0	0.3			
Nov 2021	99.4	5.4	0.4			
Dec 2021	100.0	5.9	0.6	5.4	2021	4.6
Jan 2022	100.2	5.7	0.2			
Feb 2022	100.8	5.7	0.6			
Mar 2022	101.8	5.9	1.0	5.8		
Apr 2022	102.4	5.9	0.6			
May 2022	103.1	6.5	0.7			
Jun 2022	104.2	7.4	1.1	6.6		
Jul 2022	105.8	7.8	1.5			
Aug 2022	106.0	7.6	0.2			
Sep 2022	106.1	7.5	0.1	7.7		
Oct 2022	106.5	7.6	0.4			
Nov 2022	106.8	7.4	0.2			
Dec 2022	107.2	7.2	0.4	7.4	2022	6.9

Source: Stats SA, Investec

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Figure 22: CPI forecast averages (continued)

Date	Index Base 2016	Annual y/y	Monthly m/m	Quarterly y/y	Calendar year y/y	
Jan 2023	107.4	7.2	0.2			
Feb 2023	107.9	7.0	0.4			
Mar 2023	108.4	6.5	0.5	6.9		
Apr 2023	108.8	6.3	0.4			
May 2023	109.1	5.8	0.2			
Jun 2023	109.3	4.9	0.2	5.6		
Jul 2023	110.4	4.3	1.0			
Aug 2023	110.6	4.3	0.2			
Sep 2023	110.9	4.5	0.3	4.4		
Oct 2023	111.4	4.6	0.4			
Nov 2023	111.7	4.6	0.3			
Dec 2023	111.9	4.4	0.2	4.5	2023	5.6
Jan 2024	112.5	4.7	0.5			
Feb 2024	112.8	4.6	0.3			
Mar 2024	113.6	4.8	0.7	4.7		
Apr 2024	114.1	4.8	0.4			
May 2024	114.4	4.9	0.3			
Jun 2024	114.6	4.9	0.2	4.9		
Jul 2024	115.6	4.7	0.8			
Aug 2024	115.8	4.7	0.2			
Sep 2024	116.1	4.7	0.3	4.7		
Oct 2024	116.4	4.5	0.2			
Nov 2024	116.7	4.5	0.3			
Dec 2024	116.8	4.3	0.1	4.4	2024	4.7
Jan 2025	117.5	4.4	0.6			
Feb 2025	118.7	5.2	1.0			
Mar 2025	119.7	5.4	0.9	5.0		
Apr 2025	120.0	5.2	0.2			
May 2025	120.1	5.0	0.1			
Jun 2025	120.3	5.0	0.2	5.0		
Jul 2025	121.3	5.0	0.8			
Aug 2025	121.6	5.1	0.3			
Sep 2025	122.0	5.1	0.3	5.0		
Oct 2025	122.1	5.0	0.1			
Nov 2025	122.4	4.9	0.2			
Dec 2025	122.6	5.0	0.2	4.9	2025	5.0
Jan 2026	123.4	5.0	0.6			
Feb 2026	124.3	4.8	0.8			
Mar 2026	125.5	4.8	0.9	4.9		
Apr 2026	107.4	7.2	0.2			
May 2026	107.9	7.0	0.4			

Source: Stats SA, Investec

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Figure 23: Economic Scenarios: note updated probabilities

Extreme Up case **1%**

	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/Rand (average)	16.40	15.50	14.50	14.00	13.60	13.40	13.30	13.10
Repo rate (end rate)	6.50	6.25	6.00	5.75	5.50	5.25	4.75	4.75

SA economic growth very quickly rises to 3–5%, then 5-7%. Good governance, growth-creating reforms (structural constraints eradicated), strong property rights, no nationalisation or expropriation without compensation. High business confidence and fixed investment growth, substantial FDI, fiscal consolidation drives debt to low ratios of 2000s. Very subdued domestic inflation on extreme rand strength, very favourable weather conditions. Strong global growth, risk-on, commodity boom. Rapid upgrades of credit ratings to investment grade. No grey listing. Quick transition to renewable energy from fossil fuels.

Up case **4%**

	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/Rand (average)	16.60	15.90	15.50	15.00	14.70	14.60	14.50	14.90
Repo rate (end rate)	7.00	6.75	6.50	6.25	6.00	6.00	5.50	5.50

Economic growth averages 3.3% over five-year period, but lifts towards 5.0% y/y by period end, rising confidence and investment levels, structural constraints eroded, global growth strong, global financial markets risk-on. No nationalisation or expropriation without compensation. Low domestic inflation on favourable weather and global conditions, rand strength, lower state-controlled price inflation on increased privatisation. Credit rating upgrades on fiscal consolidation, markedly lower borrowings. Substantial transition to renewable energy away from fossil fuel usage, comprehensive measures to alleviate climate change impact on economy. No grey listing.

Base case **48%**

	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/Rand (average)	16.90	16.45	16.20	16.40	16.20	16.45	16.80	16.60
Repo rate (end rate)	7.50	7.50	7.00	7.00	6.50	6.50	6.50	6.50

Economic growth modest (1.9% average over 5 years) but lifts towards 3.0% y/y by end period on reforms, global financial market risk sentiment is neutral to positive. South Africa follows fiscal consolidation (debt to GDP stabilisation) leading to positive outlooks, then likely credit rating upgrades. The rand stabilises, then strengthens somewhat. Inflation is impacted by the course of weather patterns via food price inflation. A transition to renewable energy and slow move away from fossil fuel usage occurs and measures to alleviate the impact of climate change on the economy are modestly implemented. The Russian/Ukraine conflict eases and does not exacerbate. Little expropriation without compensation. Temporary grey listing.

Lite (domestic) Down case **36%**

	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/Rand (average)	18.30	18.50	18.00	18.20	17.90	18.10	18.20	18.30
Repo rate (end rate)	7.50	8.00	8.50	9.00	9.00	9.00	9.00	9.00

Weak GDP growth (0.9% average over 5-years), swing toward left leaning policies. Business confidence depressed, substantial electricity and water shedding, very weak rail capacity, civil and political unrest, very little investment growth, recession. Increased state borrowings, risk of credit rating downgrades rises, then occurs later in period. Some expropriation of private sector property without compensation with a negative impact on the economy. High inflation on unfavorable weather conditions, marked rand weakness. Little transition to renewable energy or measures to alleviate climate change. Grey listed..

Severe down case **11%**

	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/Rand (average)	18.70	19.30	19.50	19.70	19.90	19.90	20.00	20.50
Repo rate (end rate)	8.00	9.00	10.00	10.50	10.50	11.00	11.50	11.50

Lengthy global recession, global financial crisis – insufficient monetary and other support domestically and internationally. ANC/EFF coalition in 2024. Widespread, severe services load shedding, severe civil and political unrest. Government borrows from increasingly wider sources, SA rated single B from all three key agencies, eventually CCC grade, increased risk of default, sinks deeper into a debt trap. Failure to transition to renewable energy and to sufficient measures to alleviate the impact of climate change on the economy. Very high inflation on very adverse weather conditions, severe rand weakness. Expropriation of private property without compensation with a marked negative economic impact. Grey listed

Note: Event risk begins Q1.23. Source: Investec

Annabel Bishop • Investec Bank Limited • email: annabel.bishop@investec.co.za • Tel (2711) 286 7188

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Annabel Bishop • Investec Bank Limited • email: annabel.bishop@investec.co.za • Tel (2711) 286 7188

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Annabel Bishop • Investec Bank Limited • email: annabel.bishop@investec.co.za • Tel (2711) 286 7188