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A bumpier road to 3% inflation - and it may start with a hike

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The SA economy is not in an Iran-induced crisis, but our fragile recovery has stalled and rate hikes are back on the table; only this time, the margin for error is smaller and the policy trade-offs, sharper.

At the start of the year, South Africa's road ahead was looking smoother: inflation was easing, interest rates were expected to fall, and the global economy seemed to be digesting all the tariff and trade drama. That meant a modest domestic growth recovery could finally start to gain some traction.

That encouraging story has now become more complicated. The world has changed again, and with it the assumptions underpinning that relatively neat outlook, especially when it comes to interest rates.

A few months ago, the question was how quickly interest rates would fall. Now it is whether they may rise again.

The trigger is familiar by now. The disruption to global energy markets has pushed oil prices higher, lifted fuel costs, and introduced a renewed inflation hump just when we thought the path to 3% was going to be swift and painless. For a small, open economy like South Africa, that feeds through the economy quickly - via the fuel pump, the exchange rate, and ultimately, into broader prices.

To be fair, policymakers have not been standing still. As my colleague **Roy Havemann** **pointed out in his column in April**, the temporary fuel levy relief does matter. It does not remove the shock, but it takes some of the sting out of it and helps to contain the immediate inflationary impulse. That buys us a bit of time.

But it does not fundamentally change the direction of the story.

Even with some cushioning, inflation is now set to move higher in the near term. A forecast of around 4% for headline inflation in 2026, with some months edging closer to 5%, looks reasonable even if the Iran conflict is resolved relatively quickly, with higher outcomes increasingly likely the longer it drags on.

That complicates the job of a central bank that has spent the past few years working hard to anchor expectations and build credibility around a lower inflation target.

The South African Reserve Bank (SARB) has earned a reputation for acting decisively when inflation threatens to drift. That credibility is valuable - it allows the Bank to look through temporary shocks - but it also means it cannot afford to ignore signs that inflation pressures may become more persistent.

Initially, the expectation was that the Bank could look through this shock. But several weeks in, with oil prices still elevated and disruption in the Strait of Hormuz ongoing, that window is closing quickly.

Which is why the prospect of a rate hike at the May MPC meeting suddenly feels very real.

BER CONFERENCE 2 JUNE

Governor Lesetja Kganyago is set to deliver the keynote address at the BER's annual conference – less than a week after the May MPC decision. Keen to ask him why he did or did not hike? Join us in Sandton on 2 June.

More information about the conference programme and links to register are available on our website.

If the SARB does feel compelled to respond, the logic is fairly clear: do as little as possible but do it quickly. A small, early adjustment of 25bps, followed by more only if needed, would be aimed less at the current fuel shock, which higher interest rates cannot fix, and more at preventing second-round effects from taking hold.

That distinction matters. This is not a demand-driven inflation story that can be neatly cooled by tighter policy. It is a supply shock, imported and largely beyond our control. Raising rates will not lower oil prices or reopen shipping routes. But it can help ensure that a temporary shock does not become a more persistent inflation problem.

That does not make it any less painful. Higher interest rates, even modest ones, will add pressure to already stretched households and raise borrowing costs for firms at a time when demand is still fragile. The trade-off is an uncomfortable one: short-term pain to avoid a more entrenched inflation problem later.

Another uncomfortable reality is that much of this now depends on decisions made far from our shores and, to a large extent, on what US President Donald Trump decides to do next.

Supply shocks, by their nature, often carry the seeds of their own reversal. Higher oil prices act as a tax on global demand, eroding purchasing power and eventually weighing on growth, which in turn helps bring inflation back down. If the current disruption proves temporary and second-round effects remain contained, the underlying disinflationary trend should reassert itself. In that case, the SARB would already have room to reverse course and resume cutting rates early next year.

Still, what was shaping up to be a relatively smooth path to 3% inflation now looks more like a bumpy road.

Which brings us back to the broader economic story. The past year did show signs of improvement: growth accelerated, inflation moderated, and confidence began to lift. But it was always a fragile recovery, supported by a handful of favourable factors rather than strong, self-sustaining momentum. The consumer did much of the heavy lifting but is now set to come under renewed pressure as inflation rises and higher borrowing costs bite into disposable income. Private investment, meanwhile, had only just begun to lift its head. It would not take much for it to turn down again.

ECONOMIC OUTLOOK, MAY 2026

We have revised our near-term growth outlook to reflect a more challenging global and domestic environment, while our medium-term trajectory remains broadly unchanged. **Economic Outlook** – exclusive to BER Premium Insights clients - outlines the key drivers shaping the forecast, including elevated geopolitical risk, renewed inflation pressures, and constrained policy space. South Africa's recovery has lost momentum amid higher fuel costs, weaker consumer demand, and ongoing structural constraints. As a result, growth is expected to remain subdued, with risks to the outlook increasingly skewed to the downside.

Indeed, fragile recoveries do not easily absorb shocks. They stall. They hesitate. They become more dependent on the external environment behaving itself, which is not a comfortable position to be in when global sentiment can swing on a late-night social media post.

But that is where we find ourselves. Not in crisis, but in a more constrained, more uncertain space where the margin for error is smaller and the policy trade-offs, sharper.

Granted, next year could still be better. Or at least, the road may become a little less bumpy - though I do realise that this is exactly what I said last year.

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