

MPC COMMENT | 30 JANUARY 2025

A hawkish cut by the SARB amid worries about global uncertainty

Author: Lisette IJssel de Schepper and Tracey-Lee Solomon

During the first meeting of 2025, the Monetary Policy Committee (MPC) of the South African Reserve Bank (SARB) decided to lower the repo rate for a third consecutive meeting by 25bps, to 7.5%. Even more than before, the SARB focused on the upside risks to inflation—especially over the medium term, which is deemed more uncertain than usual.

As we flagged ahead of the meeting, not all members voted for the reduction, and two of the six preferred that the policy rate remain unchanged—although the committee was ultimately in agreement that it was possible to reduce the degree of policy restrictiveness. The 25bps cut was in line with our expectations and the consensus forecast ahead of the meeting.

GLOBAL UNCERTAINTY IS A KEY CONCERN FOR THE SARB

Governor Lesetja Kganyago kicked off his statement by saying that some of the risks identified by the SARB have materialised since the previous meeting, especially on the global front. The SARB acknowledged limited space for the US Federal Reserve (Fed) to ease policy further and even warned that the Fed may hike its interest rate if inflation picks up once again. This would create volatility, and the SARB wants to avoid this scenario for SA. The SARB appears even more pessimistic about global monetary policy than the banks themselves. While an extended pause by the Fed is likely after the Fed kept its policy rate unchanged earlier this week, Fed Chair Jerome Powell did not highlight the risk of an interest rate hike. Instead, he noted that rates are already significantly restrictive and well above the neutral level. Additionally, the European Central Bank (ECB), which announced a 25bps rate cut at the same time as the SARB, signalled that further cuts are likely. The ECB acknowledged that monetary policy remains restrictive but omitted its usual commitment to keeping rates “sufficiently restrictive for as long as necessary.” Altogether, this underscores that the SARB is highly cautious relative to its global counterparts. Of course, in the EM space, one could refer to the Central Bank of Brazil, which hiked its policy rate aggressively this week – but the circumstances in Brazil are, at the moment, different to those in SA.

Listening to the statement, it seemed it was written by a member who wanted interest rates to be unchanged. While mentioning the usual uncertainties on the local front – administrative prices and the rand exchange rate – the focus was firmly on the potential impact of the global environment on the domestic inflation and growth outlook. When prompted about what these global uncertainties could be during the Q&A, Kganyago referred to trade measures. If major

central banks would slow – or hold, or even reverse – their pace of policy easing, global financial conditions would remain tighter for longer. This would have implications for capital flows to EMs, including SA, which would also impact the exchange rate. Over time, a (weaker) rand would affect economic activity and inflation. While the SARB would look through the shock, it would act on the second-round implications of these developments.

In terms of its forecast, the SARB sees headline inflation average at 3.9% in 2025 (down from 4% before), with the forecast for 2026 (4.6%) and 2027 (4.5%) unchanged. While our forecast is for slightly higher inflation this year, the pattern is similar, with low inflation during the first half and moving close to the midpoint of the target during the second half of the year. The SARB (and our) electricity price increase assumption is on the high side and suggests inflation turn out even lower. While the Governor was speaking, Nersa announced the following electricity tariff increases for the next three years: 12.7% for 2025/26, 5.35% for 2026/27, and 6.17% for 2027/28. This is lower than Eskom asked for. *We will reassess our CPI forecast following the release of the Income and Expenditure Survey (IES) earlier this week and the confirmation of the Eskom tariff increases. We will provide an update in the upcoming Economic Prospects release.*

The risks to the inflation outlook are assessed to be on the upside, especially over the medium term; the outlook is deemed more uncertain than usual. In September and November, the SARB saw the risks to the inflation outlook as balanced. The lower-than-expected electricity tariff increase arguably removes one of the SARB's upside risks to inflation. However, given its heavy focus on global uncertainties, it is likely that the SARB still deems the balance of risks to be tilted to the upside.

The SARB made a significant downward revision to its 2024 growth forecast, lowering it from 1.1% to 0.7%. This is a touch below our expectation for 0.8% growth in 2024. As the BER, the SARB sees a fairly strong Q4 due to a normalisation in agricultural production following the slump in Q3 and strong household consumption. The SARB sees real GDP growth accelerate to 1.8% next year and reach 2% by 2027. Importantly, this would mean that the output gap (roughly put the difference between the economy's potential growth rate and the economy's actual growth rate, or the 'speed limit' as Kganyago calls it) would be zero by 2027. This would be in line with the steady state. The risks to the growth forecast are assessed to be balanced.

Like in the previous meeting, the SARB highlighted two scenarios it explored during its deliberations. One focused on a universal 10%pt increase in US tariffs, with retaliatory measures by other countries. This resulted in higher global inflation and interest rates and greater risk aversion in financial markets. The model sees the rand weaken to R21/\$, with inflation reaching 5% and the policy rate half a percentage point higher, at its peak, relative to the baseline forecasts. A more optimistic scenario explored accelerated structural reform. Akin to results from similar analysis done by the BER, this showed how progress on the reform front could provide the SARB with the space to ease policy further.

UPSIDE RISKS TO THE INFLATION OUTLOOK SUGGEST THE SARB MAY (ALMOST) BE DONE WITH ITS CUTTING CYCLE

The SARB's own quarterly projection model (QPM) suggests that some further easing is warranted over the short term, with the repo rate settling at 7.25% (from 7.5% after this meeting). However, as usual (perhaps even more than usual), the governor said this was a mere guideline and that decisions would be made on a meeting-to-meeting basis. During the

Q&A, Kganyago said that when there was a “multiplicity of shocks”, looking through and waiting for second-round effects becomes more challenging, and the bank might be forced to act earlier.

For now, we think there is room for another 25bps rate cut in March. However, there is a plausible story to be told that a majority of MPC members would prefer the interest rate to remain on hold. The MPC seems particularly concerned about the uncertainties over the medium term, and we are unlikely to have much more certainty on that front soon. That said, should inflation expectations remain anchored at the target (the next BER Inflation Expectation Survey is due on 17 March – i.e. before the MPC decision), and we see some global windfalls (for example, a steady exchange rate or lower oil prices), a cut should be possible.

Economic Prospects, which is due to be released in the first weeks of February, will share more insights and forecast implications.

CONTACT US

Tel: +27 (21) 808 9777

Email: lisette@sun.ac.za

Click [here](#) for previous editions of this publication.

Please refer to the glossary on the [BER website](#) for explanations of technical terms.

Copyright & Disclaimer

This publication is confidential and only for the use of the intended recipient. Copyright for this publication is held by Stellenbosch University.



Although reasonable professional skill, care and diligence are exercised to record and interpret all information correctly, Stellenbosch University, its division BER and the author(s)/editor do not accept any liability for any direct or indirect loss whatsoever that might result from unintentional inaccurate data and interpretations provided by the BER as well as any interpretations by third parties. Stellenbosch University further accepts no liability for the consequences of any decisions or actions taken by any third party on the basis of information provided in this publication. The views, conclusions or opinions contained in this publication are those of the BER and do not necessarily reflect those of Stellenbosch University.