The MPC's decision: Another blow to consumers' wallets

By Katja Hamilton

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The South African Reserve Bank has hit the country with yet another interest-rate hike, this time 50 basis points which was a unanimous MPC decision.

Source: Pexels

This makes it the 10th interest rate hike since November 2021, with the previous 50 basis points hike - which came into effect from 31 March 2023 - having already escalated the repo rate to a 2009-high.

The decision came on the back of a Monetary Policy Committee (MPC) meeting today, 25 May, following which the South African Reserve Bank governor, Lesetja Kganyago, made his public announcement.

The 50bps hike to the repo rate means it will increase to 8.25%, the prime lending rate to 11.75% and that short term interest rates have now increased by 4.75% since the low of 3.5%.

The MPC's determination runs parallel to a convergence of global and domestic shocks that has created a complex web of inflationary pressures in South Africa, resulting in a longer-than-anticipated rate-hiking cycle.

"The rise in South Africa’s headline inflation rate has been shaped primarily by fuel, electricity and food price inflation," Kganyago said. "Food price inflation is now expected to be 10.8% in 2023 (up from 9.9%) and 5% in 2024 (up from 4.5%).

Risks to the inflation outlook are assessed to the upside. Despite easing of producer price and food inflation, global price inflation remains high."

Luigi Marinus, portfolio manager at PPS Investments, says part of the reason that the MPC has targeted a 4.5% level of inflation has been to bring about a moderation in inflation expectations.

"Inflation being sticky at around 7% and the forecast that the 4.5% level is only going to be achieved in the second quarter of 2025, has raised concerns that inflation expectations are not moderating," he said. "The direct practical implications are the effect on wage demands and continued rand weakness. The MPC has remained hawkish in the face of these concerns, possibly at the expense of GDP growth."

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Harry Scherzer, chief executive officer at Future Forex noted, "Interest rate hikes cause borrowing to become more expensive, resulting in less spending, lower economic growth and decreased employment. Nonetheless, Sarb has opted for long-term gain over short-term pain.

"With inflation running at around 7% (above Sarb's target of 3% to 6%), Sarb is trying to bring this down in line with its targets. The interest rate increase will help combat the latest bout of rand weakness, which otherwise could result in further inflation (due to increased prices in importing things like fuel)."

However, Sarb's hands are somewhat tied as the country faces low economic growth, high unemployment and fears around rising indebtedness among consumers (at the end of last year, the rate of new defaults on credit cards rose 20% year-on-year). Future rate decisions will hinge on global inflation, interest rates, and local matters (such as load shedding) that drive the price of goods and services.

The scathing cost of load shedding

"The regular and extended hours of load shedding pose an enormous risk to South Africa's outlook, despite the fact that many households and businesses continue to make commendable efforts to diversify their energy sources. At this time, it is crucial for consumers and businesses to continue being proactive in managing their finances to navigate this difficult economic cycle," said FNB chief executive officer, Jacques Celliers.

Subsequent to Sarb's decision to increase its repo rate by 0.50%, he confirmed FNB will lift its prime lending rate by 0.50% with effect from Friday, 26 May 2023.

FNB chief economist, Mamello Matikinca-Ngwenya posited, “The MPC's decision was expected by some market analysts. This reflects the MPC’s endeavour to remove the accommodation provided during the lockdowns, cater for sticky inflation and the upside risk presented by a weaker exchange rate."

The Russian-Ukraine conflict

Matikinca-Ngwenya added that escalated geopolitical tensions only serve to compound inflationary pressures, increasing frictions in global production as “reshoring” takes shape, threatening existing trade agreements and weighing on currencies as diplomatic fallouts occur, as we have experienced in SA.

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"Furthermore, while the prevailing local supply-side issues around energy and logistics are not considered to be within the ambit of monetary policy, they do adversely impact inflation and demand, by lifting the cost of living and operations. Therefore, further intensification of load shedding this winter exacerbates upside risk to inflation, and the upward pressure on interest rates is not fully neutralised.

"We still believe the MPC has reason to pause, to reflect on the delayed impact of the cumulative rate increase, but also to remain cautious about the road ahead."

For a second consecutive meeting, global GDP growth in SA is forecast to improve in 2023, from 2.0% to 2.4%, and in 2024 from 2.5% to 2.7%.

"This is compared to the forecast in South Africa where GDP growth is expected to be marginally higher in 2023 at 0.3% from the 0.2% expectation in the previous meeting. This takes into account the estimated 2% negative impact on South African GDP growth due to load shedding," Marinus of PPS Investments, said.

The GDP forecasts for 2024 and 2025 were unchanged at 1.0% and 1.1% respectively. The governor highlighted that GDP growth has been volatile and that a sustained reduction in load shedding or an increased supply from alternative sources would be required to raise growth.

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Unfortunately, geopolitics has very quickly become a significant economic issue in South Africa – second to only load shedding, says Angelika Goliger, EY Africa's chief economist.

"There is going to be a lot of uncertainty in the lead up to the Brics Summit, which is to be held in South Africa from 22 - 24 August. Our key trading partners, the US and EU, and the world, will be watching how the government engages with Russia preceding and during the summit.

"In the coming weeks, we could see measures against entities based in third countries for allegedly helping Russia evade sanctions, as the EU wraps up its efforts to monitor the impact of current sanctions against Russia. The Sarb can only do so much to support the economy in this context.

"The rand, which has previously reflected confidence towards emerging markets, has now become a measure of RSA-specific investor sentiment. With our import basket growing and our exports declining, the weaker rand and resultant inflation is something that the Sarb has no choice but address.

"While there is a lot of uncertainty around the rate path going forward, I would not discount another 25bps point hike at the next meeting."

ABOUT KATJA HAMILTON

Katja is the Finance, Property and Healthcare Editor at Bizcommunity.

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