



## Encouraging drop in services inflation in April 2024

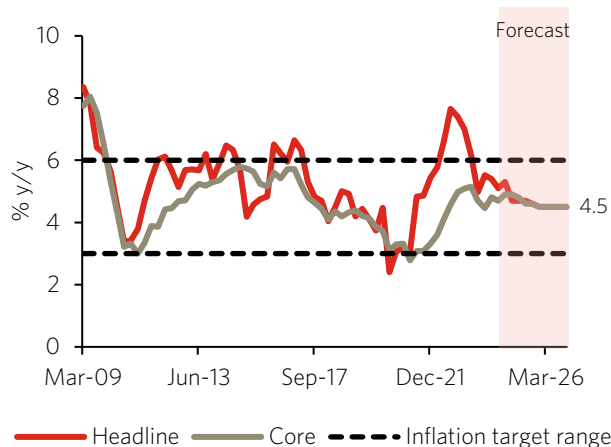
### Highlights

- As reported by Statistics South Africa (Stats SA), the consumer price index (CPI or headline inflation) dropped slightly from 5.3% year-on-year (y/y) in March 2024 to 5.2% y/y in April 2024. Core inflation eased more meaningfully to 4.6% y/y in April from 4.9% y/y in March.
- From an average of 5.4% in the first quarter of 2024, the SA Reserve Bank (SARB) expects inflation to ease in the second quarter to 5.1% before bumping up slightly to 5.3% in the third quarter.
- High services inflation was previously flagged as a concern by the SARB. The moderation of services inflation to 4.6% y/y in April will likely be welcomed by the SARB but medical insurance inflation (the second largest item in the services basket) remains high at 10.3% y/y in April.
- Food and non-alcoholic beverages inflation (NAB) continued to trend downward for the fifth consecutive month to 4.7% y/y in April. The expected upward pressure on food inflation from the past El Niño season is not significant and is expected to be short-lived.
- The Crop Estimates Committee (CEC) upwardly revised its third summer crop production forecast for 2024 by 1% compared to its second production forecast.
- During May 2024, there were cases of foot-and-mouth disease reported in the Eastern Cape. Measures have been put in place to try and prevent the spread of the disease.
- Transport inflation edged up to 5.7% y/y in April, from 5.3% y/y in March. The rise in transport inflation was due to fuel inflation. Based on early data from the Central Energy Fund (CEF), we can expect fuel price cuts of around R0.84/l for petrol (95 ULP) and R0.90/l for diesel (0.05%) in June 2024 which will translate to downward inflationary pressure and provide relief for consumers.
- Both major determinants of domestic fuel prices (international oil prices and the exchange rate) have unfolded positively. The price of Brent crude oil has retreated from a monthly average of US\$90/bbl in April to the lower US\$80/bbl range in the first three weeks of May.
- The rand has strengthened from around R18.80/US\$ in March and April to R18.41/US\$ month-to-date (1 to 20 May). Investec notes that the rand's strength in recent weeks could be attributed to subsiding political risk as more opinion poll results are being released.
- While the April inflation outcome is encouraging, we still expect the SARB to keep interest rates unchanged at 8.25% in May 2024. Considering that headline inflation is projected to continue to moderate, and that monetary policy is forward-looking in nature, we still see a possibility that the SARB may start cutting interest rates in the second half of 2024. We have, however, scaled back our expectation from 75 basis points worth of cuts in 2024 to 50 basis points, on persistent upside risks to inflation.

## Core inflation dropped closer to the mid-point of the inflation target in April

Headline inflation averaged 5.4% in the first quarter of 2024. This was in line with the SARB's March estimate and slightly better than the 5.5% average recorded in the fourth quarter of 2023. The average core inflation rate of 4.8% in the first quarter was also in line with the SARB's March estimate but worse than the 4.5% recorded in the fourth quarter of 2023 (see chart 1).

Chart 1: Average inflation expected to trend down



Source: SARB March Monetary Policy Committee (MPC), Momentum Investments  
Actuals until the first quarter of 2024. Forecasts until the fourth quarter of 2026

The second quarter started positively with headline inflation dropping slightly to 5.2% y/y in April from 5.3% y/y in March, better than the Reuters median consensus of 5.3% y/y. Lower food and NAB inflation as well as lower miscellaneous goods and services inflation in April offset higher transport inflation and restaurant and hotels inflation.

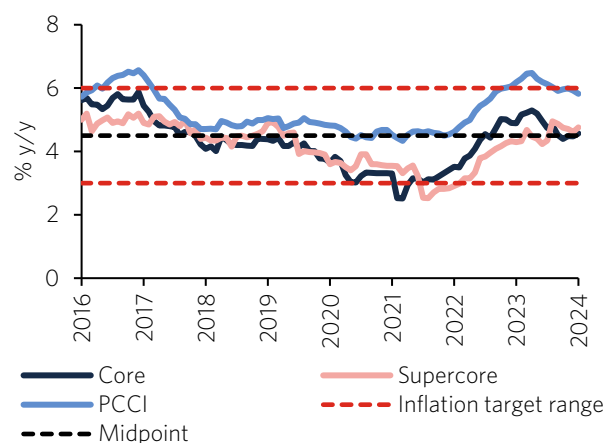
Core inflation eased from 4.9% y/y in March to 4.6% y/y in April (Reuters median consensus: 4.7% y/y). The moderation was mainly due to lower health insurance inflation (10.3% in April from 12.9% in March) and the big drop in package holiday inflation from 5.5% y/y in March to a negative 1.4% y/y in April. These two categories contributed to a lower services inflation rate of 4.6% y/y in April (5% y/y in March).

Persistent core inflation was flagged as a concern in the SARB's April 2024 Monetary Policy Review (MPR) mainly on account of services inflation. April's services inflation print may provide relief to the SARB especially

because the moderation was due to the biggest pressure point (medical insurance inflation). The only other services components recording high price increases were water and other services (7.9% y/y in April), maintenance and repairs (7.9% y/y), maintenance and repairs of dwellings (7.4% y/y), restaurants and hotels (7.5% y/y) and education (6.3% y/y) but these services combined make up only 16.5% of the services basket. The majority of items (13 out of 19) in the services basket (including the biggest item in the services basket - owners' equivalent rent) are either contained within the 3% to 6% inflation target range or are recording price increases below 3%.

The new core inflation measures developed by the SARB (supercore and PCCI (persistent and common component of inflation)) indicated elevated inflationary pressures. In particular, PCCI was tracking closer to the upper end of the inflation target range in January 2024 (see chart 2).

Chart 2: Supercore and PCCI above core inflation



Source: SARB, Momentum Investments  
Monthly data until January 2024

The SARB expects inflation to moderate in the second quarter of 2024 compared to the first quarter with headline inflation easing faster than core inflation. Headline inflation is expected to ease by three percentage points to 5.1% in the second quarter and core inflation is expected to ease by one percentage point to 4.7%.

Headline and core inflation are expected to tick up in the third quarter likely driven by higher municipal charges. Upward inflationary pressure in the third quarter may also stem from rental inflation and the expected impact of the drier and hotter weather conditions in February and March 2024. Thereafter,

headline inflation is expected to ease as the quarters progress but at a slower pace given the stickiness in core inflation. The SARB expects headline inflation to settle at 4.5% from the fourth quarter of 2025 onwards (see chart 1).

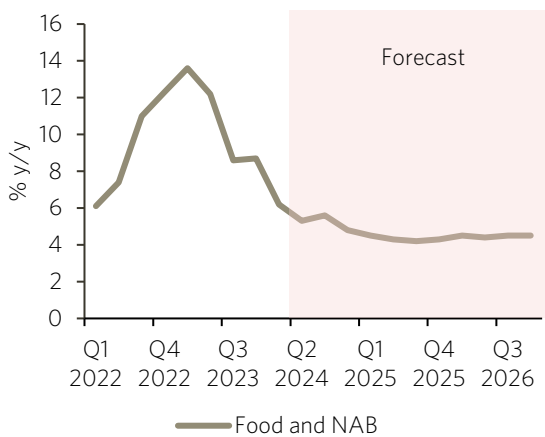
### Food inflation dipped below 4.5%

Food and NAB inflation dropped to 4.7% y/y in April from 5.1% y/y in March. This represents the fifth consecutive decrease in food and NAB inflation and it is the first time the category has dipped below 5% since September 2020. More encouragingly, food inflation decreased to 4.4% y/y in April from 4.9% y/y in March. The reduction was broad-based with seven of the nine food categories easing in April. Meat inflation decreased to 0.5% y/y in April from 0.8% y/y in March. Bread and cereals inflation also dropped to 4.3% y/y in April (5% y/y in March). Although still elevated, milk, eggs and cheese inflation moderated to 8.7% y/y in April from 10.1% y/y in March.

potential impact of El Niño weather conditions, but the expected inflationary pressure is not significant and it is seen to be short-lived. This is in line with crop estimates from the CEC and meat slaughtering rates.

The CEC revised its summer crop forecast (third forecast) for 2024 up by 1% in April 2024 compared to its second forecast. This follows an 8.9% downward revision from the initial 2024 forecast on the back of drier and hotter weather conditions in February and March. The latest upwardly revised figure (16.02 million tons) implies that the CEC expects the impact of the more intense El Niño at the beginning of the year to be milder than previously anticipated.

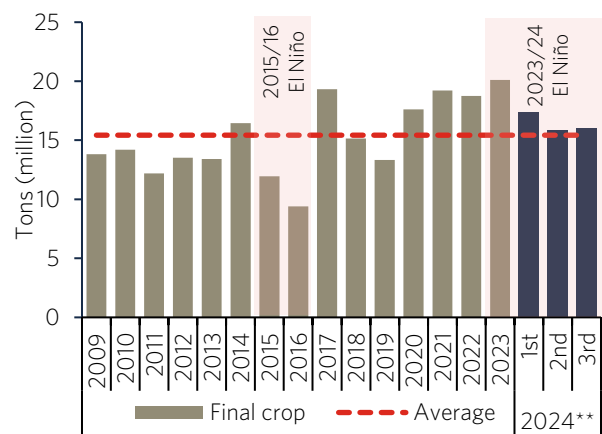
Chart 3: Food and NAB expected to continue easing



Source: SARB, Stats SA, Momentum Investments  
Forecasts until the fourth quarter of 2026

The SARB published its quarterly food and NAB inflation expectations for the first time in the March Monetary Policy Committee (MPC). Food and NAB inflation is expected to ease gradually over the quarters from 6.1% y/y in the first quarter of 2024 to around the midpoint of the inflation target range from the first quarter of 2025 onwards. The uptick pencilled in for the third quarter of 2024 (5.6% y/y) incorporates the

Chart 4: 2024 expected summer crops\* not in a dire state



Source: CEC, Momentum Investments  
\* Commercial summer crops  
\*\* Production forecasts

The latest summer crop forecast for 2024 (third forecast) remains below the initial forecast and the final crop of the past four years (see chart 4). Encouragingly, the expected final summer crop in 2024 is slightly above the average since 2009 and more importantly,

markedly above the realised summer crop during the 2015/2016 El Niño season. According to the SARB, the magnitude of the drought experienced in 2015/2016 added up to 10 percentage points to food inflation and three percentage points to headline inflation. Seeing as the summer crops estimates for this year are significantly above 2015/2016, the impact of the El Niño weather phenomenon on inflation will likely be far milder. Additionally, the Agriculture Business Chamber notes that El Niño is over which is a positive development for winter crops.

The broader Southern African region experienced much more severe El Niño conditions relative to SA. According to the Famine Early Warning Systems Network’s food security outlook report for February to September 2024, the region “is expected to have a supply gap for staple cereals”. The “combined maize exports from SA and Tanzania are unlikely to meet the regional demand” and some countries may need to import from East Africa and South America. The report further notes that SA will likely remain the main source of grain supply for Zimbabwe in the outlook period.

The outbreak of animal diseases in SA is largely contained but outbreaks are still occurring and therefore remain a risk to food inflation. In 2022, six of SA’s nine provinces reported an outbreak of the foot-and-mouth disease. Since then, significant progress has been made in containing the disease. The Department of Agriculture, Land Reform and Rural Development published an update report in March 2024 which indicated that the outbreaks have been resolved in three of the six provinces. Meat price inflation has moderated from the peak of 11.4% y/y in February 2023 to 0.5% y/y in April 2024. The unaffected provinces at the time were Eastern Cape, Western Cape and Northern Cape.

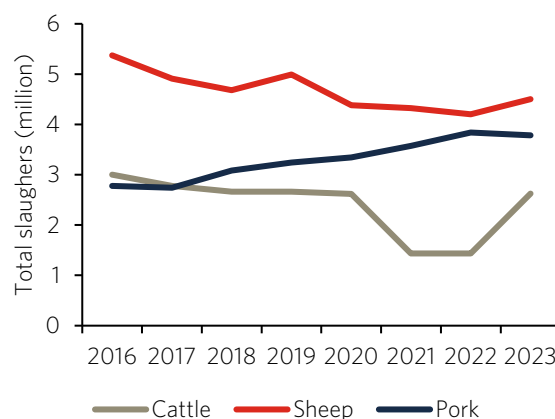
## Fuel inflation drove up transport inflation, but some relief is expected in June

Following the unexpected drop to 5.3% y/y in March, transport inflation edged back up to 5.7% y/y in April. The main culprit for this rise was private transport operation inflation (fuel) surging from 6.2% y/y in March to 9% y/y in April. On the other hand, public transport was in deflation territory for the second consecutive month at 0.6% y/y.

According to *Farmers Weekly*, Eastern Cape is no longer classified as foot-and-mouth disease free because the disease was detected in the province in May 2024 bringing the number of affected provinces to four. The department has put measures in place to prevent the spread of the disease in the Eastern Cape.

According to data from the Red Meat Levy Admin, the total number of cattle slaughtered in 2023 recovered to levels recorded before the 2021-2022 food-and-mouth disease outbreak (see chart 5) mostly boosted by increased slaughtering towards the end of 2023. The number of cattle slaughtered in February 2024 was 13.8% y/y higher than in February 2023. Sheep slaughtering surged by 23.1% y/y over the same period. The increase in slaughtering will likely keep meat price inflation (the biggest item in the food basket) contained. However, the producer price inflation of live animals jumped to 12.6% y/y in March from 7.2% y/y in February which signals upward meat price pressures in the near term.

**Chart 5: Cattle slaughtering has recovered from the foot-and-mouth disease outbreak**



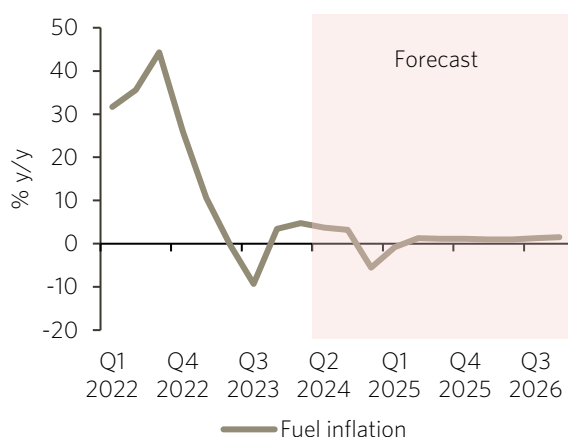
Source: Red Meat Levy Admin, Momentum Investments

The CEF announced a slight increase of R0.37/l in the price of petrol (both grades) in April while diesel (0.05%) decreased by R0.30/l. Early data from the CEF published on 20 May 2024 suggests fuel price cuts in June of around R0.84/l for petrol (95 ULP) and R0.90/l for diesel (0.05%). This will be a welcome relief for

consumers and introduces downside inflationary pressure for June.

As with food and NAB, the SARB published its quarterly fuel inflation outlook until the fourth quarter of 2026 for the first time in the March MPC. Fuel inflation is projected to remain low over the medium term with some months of disinflation over the forecast period (see chart 6). Fuel inflation is expected to average close to the lower end of the inflation target in the second and third quarters of 2024 at 3.7% and 3.2%, respectively, and drop to negative 5.5% in the fourth quarter of 2024. This means fuel inflation is not expected to place upward inflationary pressure during this year but oil price and exchange rate movements are key risk factors to fuel prices.

**Chart 6: Fuel inflation expected to remain below the mid-point of the inflation target range**



Source: SARB, Stats SA, Momentum Investments  
Forecasts until the fourth quarter of 2026

## Sticky inflation delaying interest rate cuts

Including the April inflation rate, headline inflation has remained above 5% for eight consecutive months following just two months of inflation dipping to the upper 4% range in July and August 2023. While it is positive that headline inflation is within the 3% to 6% target band, it has remained uncomfortably higher than the preferred 4.5% midpoint and some inflation risks have materialised over the past few months including hotter and drier weather conditions, high medical inflation costs and elevated administered price inflation.

The price of Brent crude oil has retreated from around US\$90/bbl and upper US\$80/bbl during the four weeks of April (the monthly average in April was US\$90/bbl) amid escalating tensions in the Middle East and Organisation of the Petroleum Exporting Countries (OPEC+) oil production cuts to the lower US\$80/bbl range in the first three weeks of May. According to the International Energy Agency (IEA), world oil demand growth is losing momentum. Oil demand growth in the first quarter of 2024 was below the IEA’s forecast and is estimated to be lower-than-expected in 2024 and 2025. The IEA attributes lower demand growth to the post-COVID rebound being largely complete as well as vehicle efficiencies and an expanding electronic vehicle fleet. On the supply side, the extension of OPEC+ voluntary production cuts through June will remain a drag on supply but “non-OPEC+ producers, led by the Americas, will continue to drive oil supply growth through 2025”. Overall, the balance of supply and demand is expected to be tight for the remainder of 2024.

The average exchange rate in April was largely unchanged at R18.88/US\$ compared to R18.83/US\$ in March. The rand has been moving in the positive direction during May. On a month-to-date basis (1 to 20 May), the rand is stronger at an average of R18.41/US\$ relative to R18.81/US\$ over the same period in April. Investec notes that rand strength in recent weeks could be attributed to subsiding political risk as more opinion poll results are being released.

These developments support the SARB’s decision to keep interest rates constant in the past five interest rate decisions since July 2023 as well as analysts’ receding projections of interest rate cuts and the expected magnitude of the rate cuts.

We expect the SARB to keep interest rates unchanged at 8.25% in May 2024. We base our expectation on lingering inflation risks and caution portrayed by major global central banks, especially the United States Federal Reserve. The interest rate decisions of major

global central banks are an important consideration for monetary policy domestically. This is from the aspect of interest rate differentials because differentials impact capital flows and this could result in a weaker rand and consequently lead to higher imported inflation.

Despite the upward inflationary pressure stemming from El Niño, headline inflation is expected to continue to decelerate and settle sustainably around the SARB's

preferred 4.5% mark from the second quarter of 2025. Considering the projected inflation path and that monetary policy is forward-looking in nature, we still see a possibility that the SARB may start cutting interest rates in the second half of 2024. We have, however, scaled back our expectation from 75 basis points worth of cuts in 2024 to 50 basis points, on persistent upside risks to inflation.

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