



## **SARB delivered the first highly anticipated repo rate cut to 8%**

### Highlights

- The United States (US) Federal Reserve (Fed) pivoted in September 2024 by reducing the Federal funds rate by 50 basis points to a range of between 4.75% and 5%. This follows eight consecutive meetings of keeping interest rates steady in light of inflation concerns.
- Domestic economic growth in the first half of 2024 was weak but growth prospects for the second half of 2024 are cautiously optimistic. This is on the back of improving confidence, easing structural constraints, particularly energy, and the two-pot retirement reform (the impact of the pension reform is built into the South African Reserve Bank's (SARB) growth and inflation forecasts).
- The SARB left its economic growth estimate for 2024 unchanged at 1.1% and revised growth for the next two years up to 1.6% in 2025 (previously 1.5%) and 1.8% in 2026 (previously 1.7%).
- Risks to the economic growth trajectory were assessed as balanced (unchanged assessment) but the assessment of inflation risks was improved to balanced (previously assessed risks as being to the upside).
- Inflation forecasts have once again improved. Headline inflation is expected to remain around the mid-point of the inflation target (4.5%) over the forecast period at 4.6% in 2024 (previously 4.9%), 4% in 2025 (previously 4.4%) and 4.4% in 2026 (previously 4.5%).
- Core inflation is estimated to remain slightly below the mid-point at 4.4% in 2024 (previously 4.6%), 4.1% in 2025 (previously 4.4%) and 4.3% in 2026 (previously 4.5%).
- On the back of lower international oil prices and a stronger rand, the SARB revised its fuel inflation forecasts lower. Food inflation was also revised lower and is expected to undershoot 4.5% in most quarters going forward.
- In comparison to our estimates and the Reuters median consensus, the SARB is more pessimistic about growth in 2025 and 2026 but they are more optimistic about the trajectory of headline inflation.
- The decision to reduce the repo rate by 25 basis points to 8% was unanimous and in line with the Reuters median consensus. However, it was revealed that the Monetary Policy Committee members (MPC) had debates about keeping interest rates constant at 8.25% or implementing a larger cut of 50 basis points which would have taken the repo rate down to 7.75%.
- It is widely anticipated that the SARB will continue to reduce interest rates this year and next year as it moves from the current restrictive stance to a more neutral monetary policy stance. The speculation now is centred around the magnitude of the interest rate cuts. In our view, the SARB will deliver another 75 basis points of cuts, in 25 basis points adjustments, by the end of 2025. Our projection is slightly less aggressive than the additional 100 basis points pencilled in by the Reuters median consensus and the forward-rate agreement (FRA) curve. The FRA is also leaning toward a more aggressive 125 basis points additional cuts.

## The Fed kicked off monetary policy easing with a larger-than-expected move

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The US Fed pivoted in 2024 by cutting the Federal funds rate by 50 basis points, leaving it in a range of 4.75% to 5%. This comes after eight consecutive meetings of keeping interest rates constant at a 23-year high since its last interest rate hike in July 2023. The decision to cut interest rates comes as the US Fed has become more comfortable about the decelerating inflation profile. They also signalled that they are not overly concerned about the resilience of the economy.

The Fed's first interest rate cut follows some of the other major central banks which had moved first, but as reported by the *Financial Times*, the Fed does not think that they are behind the curve and this larger-than-expected cut can be viewed as a "commitment to not get behind" the curve. The dot plot suggests further interest rate cuts in the US to a range of between 4.25% and 4.5% by the end of 2024.

In the week before the US Fed's decision, the European Central Bank (ECB) cut interest rates by 25 basis points to 3.5%. This was the second interest rate cut since the ECB started cutting rates in June 2024 (interest rates were kept constant in July) and brings the total cuts to 50 basis points, so far. According to *Reuters*, the ECB is unlikely to implement larger-sized cuts unless the economy deteriorates sharply from here.

The Bank of England (BOE) and Bank of Japan (BOJ) are scheduled to announce their decisions by the end of this week (20 September). The BOE started monetary policy easing in August by reducing the interest rate by 25 basis points from a 16-year high (5.25%) to 5%. On the other hand, the BOJ is one of the few central banks moving in contrast to global monetary policy easing trends. The BOJ has raised interest rates for the second time in 2024 but is expected to keep rates unchanged in September.

## Cautious optimism about economic growth in the second half of 2024

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Following a disappointing start to the year where the economy failed to grow in the first quarter of 2024, the second quarter was slightly better with the economy growing by 0.4% quarter-on-quarter (q/q). Nonetheless, overall, the first half of the year experienced weak economic growth.

The economic growth prospects for the second half of 2024 are cautiously optimistic because while some parts of the economy are improving, there are still factors that weigh on economic activity. Firstly, the economy is in a better position in terms of operational efficiency given the five-month, going on six, gap in loadshedding and easing logistics constraints. However, there are still issues in the logistics sector and this continues to affect production and export volumes. Secondly, benign inflation, especially in food and transport, is good for consumers and consumers will get further reprieve from lower interest rates as the SARB continues to cut interest rates. Moreover, the two-pot retirement reform is expected to boost consumers' short-term financial position. However, consumers' debt levels are high (reduces spending ability) and the

impact of lower interest rates and early pension withdrawals will likely have more of an impact from 2025. Lastly, it is encouraging that business and consumer sentiment is trending upward despite the indices still being in negative territory.

In July (the first month of the third quarter), manufacturing production increased by 1.7 year-on-year (y/y) following a significant contraction of 5.5% y/y in June. The manufacturing divisions that contributed the most to production growth in July were food and beverages which grew by 9.5% y/y and contributed 2.0 percentage points as well as basic iron and steel, non-ferrous metal products, metal products and machinery (5.2% y/y, contributing 1.1 percentage points).

Other sectors that grew in July were motor trade sales (0.3% y/y from negative 9.5% y/y in June) and retail trade sales (2.0% y/y from 4.1% y/y in June). The increase in retail trade sales was broad-based with five of the seven retailers recording higher sales. On the other hand, mining production contracted by 1.4% y/y in July and the decrease was largely broad-based with

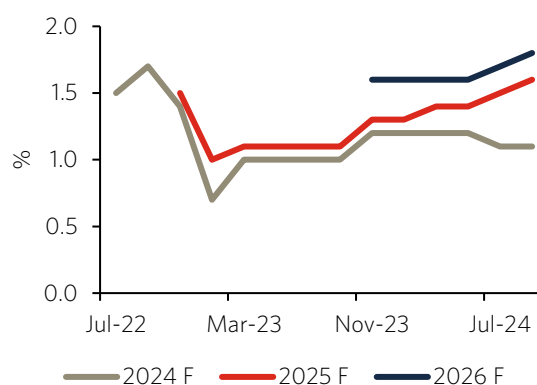
seven of the 12 mineral groups recording lower production. Wholesale trade sales also contracted by 3.2% y/y in July, lower than negative 10.2% y/y in June.

The SARB expects the economy to grow by 0.6% in the third and fourth quarters of 2024. The economic growth estimate for 2024 was left unchanged at 1.1%, in line with our estimate but slightly below the Reuters median consensus of 1%.

Economic growth estimates for 2025 and 2026 were revised higher by a 0.1 percentage point each to 1.6% and 1.8%, respectively (see chart 1). Despite the upward revisions, we and other analysts surveyed in the Reuters Econometer poll are more optimistic about economic growth than the SARB with an estimate of 1.8% in 2025 and 2.1% in 2026.

Risks to the economic growth outlook were assessed as balanced. The SARB raised concerns about investments and indicated that “a stronger investment performance is a pre-requisite for sustained higher growth”.

Chart 1: SARB’s real economic growth revisions



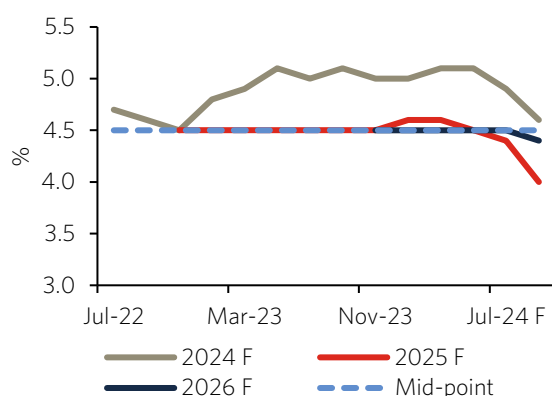
Source: SARB, Momentum Investments  
Data until September 2024

## Inflation comfortably around the 4.5% mid-point over the forecast horizon

The SARB revised its inflation forecast lower in the September meeting on the back of the unexpected sharp drop in the July inflation rate (4.6% y/y from 5.1% y/y in June), lower international oil prices, a stronger rand and the improved outlook on fuel and food inflation. Risks to the inflation outlook were assessed as balanced (previously to the upside).

(previously 4.5%) as illustrated in chart 2. Despite the SARB seeing inflation falling quicker than our estimates and the Reuters median consensus (see table 1), they still decided to cut by a smaller increment.

Chart 2: SARB’s headline inflation revisions



Source: SARB, Momentum Investments  
Data until September 2024

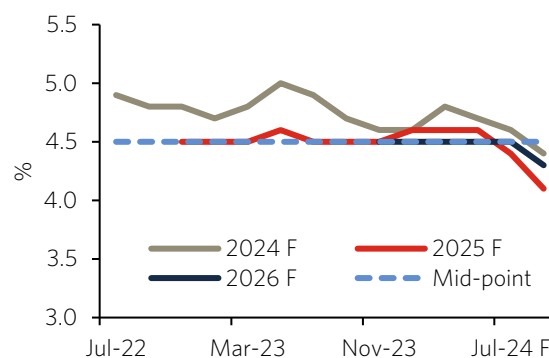
In the new forecasts, the SARB has inflation coming down to an average of 4.6% in 2024 (previously 4.9%), 4% in 2025 (previously 4.4%) and 4.4% in 2026

Table 1: Headline inflation forecast comparison

%	SARB	Momentum	Reuters
2024	4.6	4.7	4.7
2025	4	4.3	4.3
2026	4.4	5	4.5

Source: SARB, Momentum Investments, Reuters

Chart 3: SARB’s core inflation revisions

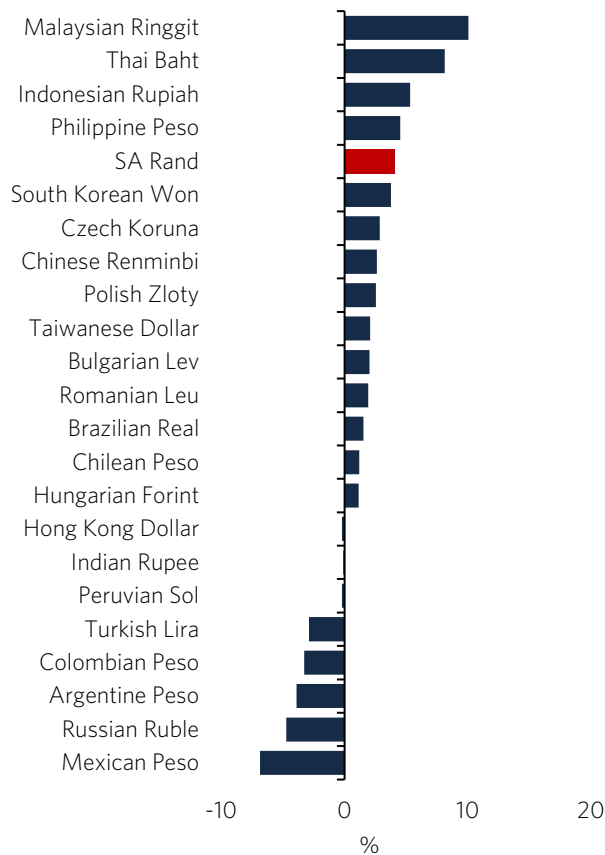


Source: SARB, Momentum Investments  
Data until September 2024

Core inflation was revised lower and is estimated to remain slightly below 4.5% over the medium-term at 4.4% in 2024 (previously 4.6%), 4.1% in 2025 (previously 4.4%) and 4.3% in 2026 (previously 4.5%) (see chart 3). These estimates are broadly in line with our projection of 4.4% in 2024, 3.9% in 2025 and 4.2% in 2026.

The rand has maintained its relative strength over the past few months and this has been beneficial for the local inflation profile. Since the July 2024 MPC meeting, the rand was the fifth best-performing currency against the US dollar, strengthening by 4.1% (see chart 4). The 50-basis point interest rate cut implemented by the US Fed in its September meeting bodes well for emerging market currencies. This is because lower interest rates in the US will likely trigger investors' risk appetite and lead to capital flows into emerging markets, SA included.

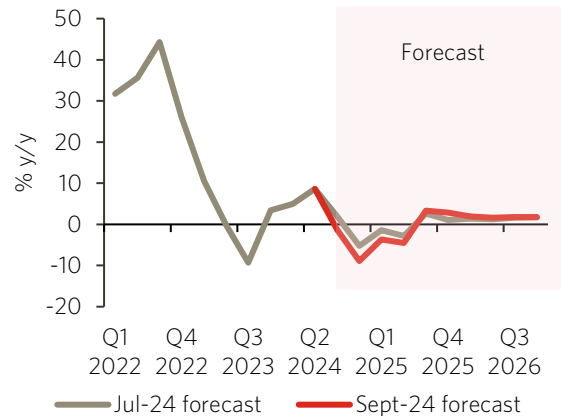
**Chart 4: SA in top five best performing EM currencies against the US dollar since the July 2024 meeting\***



Source: Bloomberg, Momentum Investments  
\* 18 July to 18 September 2024

The SARB emphasised the benefits of the stronger rand and lower international oil prices on the fuel inflation outlook. Fuel deflation is estimated to be more pronounced between the third quarter of 2024 until the second quarter of 2025 (see chart 5).

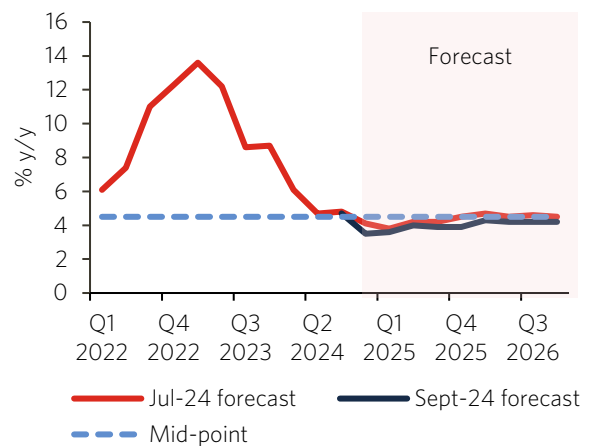
**Chart 5: SARB's fuel inflation forecast revisions**



Source: SARB, Momentum Investments  
Actual data until the second quarter of 2024. Forecasts until the fourth quarter of 2026

The food inflation outlook has also improved. Food inflation is expected to undershoot the 4.5% mid-point in every quarter from the fourth quarter of 2024 until the end of 2026 (see chart 6).

**Chart 6: SARB's food inflation forecast revisions**



Source: SARB, Momentum Investments  
Actual data until the second quarter of 2024. Forecasts until the fourth quarter of 2026

Inflation expectations, surveyed by the Bureau for Economic Research (BER), trended lower in the third quarter of 2024. Inflation expectations eased to 5.1% in

2024 (previously 5.3%) and will likely continue to moderate further in the fourth quarter survey. More encouraging was that businesses and trade unions adjusted their inflation expectations lower for 2025, 2026 and their expected five-year average in five years' time. The average inflation expectation for these three time horizons came down to 4.8%. This means that price setters are internalising the lower inflation

trajectory and this is positive for conducting monetary policy.

The SARB noted a few inflation concerns, including housing prices, electricity costs, wage growth, geopolitical risks and trade tensions. Despite the improved food inflation outlook, food inflation was noted as a source of uncertainty.

## Unanimous decision for the 25 basis point cut but other options were considered

As we and other analysts had anticipated, the SARB announced the first 25 basis point interest rate cut at the September meeting. The decision was unanimous (see table 2) but it was revealed that the MPC members debated about keeping interest rates constant at 8.25% or implementing a larger cut of 50 basis points. In the question-and-answer session, the governor indicated that the SARB is not behind the curve and does not intend to be ahead of the curve. This

implies that the bank is confident about the timing of the first interest rate cut and suggests that we may not see big interest rate cuts (e.g. 50 basis points) despite having debated about this.

Of the 21 surveyed analysts in the Reuters Econometer poll, 19 analysts expected the 25 basis point cut (ourselves included) and the remaining two analysts expected rates to be kept constant at 8.25%.

Table 2: Shift in MPC member preferences at the scheduled September 2024 meeting

Number of committee members	Favoured a 25-basis point cut	Favoured no move	Favoured a 25-basis point hike	Favoured a 50-basis point hike	Favoured a 75-basis point hike	Favoured a 100-basis point hike
24 November 2022	-	-	-	2	3	-
26 January 2023	-	-	3	2	-	-
30 March 2023	-	-	2	3	-	-
25 May 2023	-	-	-	5	-	-
20 July 2023	-	3	2	-	-	-
21 September 2023	-	3	2	-	-	-
23 November 2023	-	5	-	-	-	-
25 January 2024	-	5	-	-	-	-
27 March 2024	-	5	-	-	-	-
30 May 2024	-	6	-	-	-	-
18 July 2024	2	4	-	-	-	-
19 September 2024	6	-	-	-	-	-

Source: SARB, Momentum Investments

## More interest rate cuts anticipated

Following the SARB's interest cut in September and the improved inflation trajectory, we can expect the MPC to deliver another 25 basis point cut in November (the last interest rate setting meeting for 2024). This is in line with the Reuters median consensus. We expect that the interest rate cutting cycle will continue in the new year and we pencil in two more 25 basis point cuts in 2025,

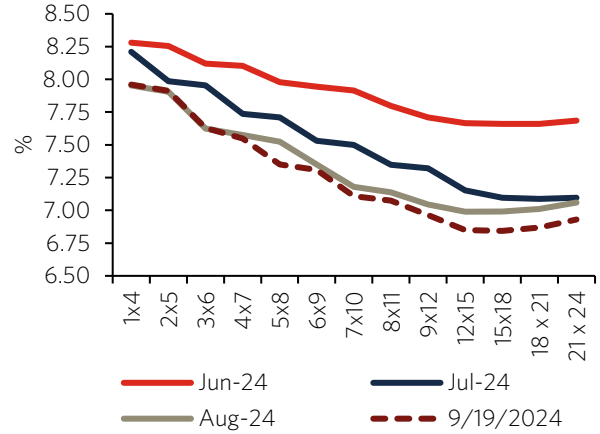
ending the year at 7.25%, slightly higher than the Reuters consensus of 7% and the FRA market (7%).

Over the past three months, the market has adjusted its outlook for interest rates notably lower (see chart 7) in line with domestic inflation trends and global interest rate trends. Similar to our view, the FRA curve (on 19

September) had priced in a cumulative 50 basis point cut by the end of 2024. The market is, however, expecting a slightly more aggressive cycle from here onwards with an additional 100 basis points fully factored in by the end of 2025 and there is a very high probability (above 90%) priced in for an additional 125 basis points of cuts.

The SARB’s quarterly projection model (QPM) is guiding toward a repo rate of 7.86% by the end of this year, which means no more interest rate cuts this year (contrary to our, Reuters and the FRA’s expectation). The model suggests a terminal rate of 7.17% in 2025, which would require 75 basis points of cuts in the year. The total interest rate cuts by the end of 2025 would be 100 basis points, in line with our projection.

**Chart 7: FRA curve is pricing in 125 basis points cuts by end-2025 with high potential for 150 basis points**



Source: Bloomberg, Momentum Investments

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