SOUTH AFRICAN RESERVE BANK

PRESS STATEMENT

30 January 2025

STATEMENT OF THE MONETARY POLICY COMMITTEE

Issued by Lesetja Kganyago, Governor of the South African Reserve Bank

Good day

At our last meeting, we warned about a more challenging global environment. Some of the risks we saw then have since materialised. In particular, the outlook for monetary policy in the United States has changed. The space for rate cuts by the Federal Reserve now looks limited, with core inflation still elevated[1] and new inflation risks emerging, such as rising tariffs on trade. It is even possible that US rates could go up again, to stabilise inflation.

Growth outside of the United States is generally more subdued. The largest economies in Europe have had weak economic performance. Germany has had two years of contraction, and both France and the UK have slow growth. At the same time, core inflation remains elevated, and rate-cut expectations have been pared back, although less than in the United States. Meanwhile, China's economy has been decelerating, with very low inflation and a marked decline in interest rates.

In these circumstances, the US dollar has appreciated strongly, and according to some measures has reached an all-time high.[2]

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[1] US core CPI inflation was 3.2% in December 2024

[2] For instance, the Fed's broad, nominal dollar index reached 127.8 index points in December 2024, above the previous peak of 127.5 reached in October 2022.

Turning to South Africa, the economy contracted in the third quarter. However, this was mostly due to an unusually large drop in agricultural production, which has limited implications for how we interpret the economy's underlying growth trend.

For the fourth quarter, we anticipate a rebound.[3] This will be supported by more normal agricultural production, as well as strong household spending, given tailwinds including lower inflation and Two-Pot pension withdrawals. We think this expected rebound in growth will close the output gap, leaving the economy to operate in line with its potential from the current quarter onwards.[4]

We expect potential growth to trend higher over the next few years. This gets growth to about 2% by 2027.

Looking at the composition of output, since the onset of Covid mining and manufacturing have underperformed, with output still below pre-pandemic levels. It is only due to growth in the tertiary sector that the economy is bigger now, than it was five years ago.

Similarly, on the demand side, investment has been depressed since Covid, while household and government spending have been more resilient.

As growth picks up, we expect some rebalancing, with a recovery in investment, as well as improvements in the primary and secondary sectors. We will be monitoring the data carefully to assess how closely the economy tracks these projections.

The risks to the growth forecast are assessed as balanced.

Moving to consumer prices, headline inflation averaged 4.4% last year, near the middle of our target range. Inflation slowed to 3% in December, having started the year above 5%. This was mainly due to favourable goods-price developments, including food inflation reaching 15-year lows, as well as lower fuel costs.[5]

Because of these transitory factors, inflation is likely to remain in the bottom half of our target range through the first half of this year. But headline inflation should revert to

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[3] Growth for 2024Q4 is projected at 1.3%, q/q and seasonally adjusted. 2025Q1 is 0.4%, also q/q sa.
[4] The estimated output gap is 0% for 2025Q1, from -0.6% of potential GDP for 2024Q3. In the forecast it averages -0.1% for 2025 and 2026, and 0% for 2027.
[5] Fuel prices fell by 10.2% in December 2024, year-on-year. Food inflation was 1.7%, slightly up from 1.6% for November, which was the lowest rate of food inflation since 2010. Overall goods inflation was 1.9%, compared with 4.2% for services.

around 4.5% thereafter, aided by core inflation which remains at or below the midpoint over the forecast horizon.

While our exchange rate assumptions have shifted towards a weaker rand[6], the effects on the inflation forecast have been limited. This is mainly because other components of inflation have come in below previous projections, lowering the starting point of the forecast.

Inflation expectations have also now largely aligned with our midpoint objective, according to the most recent survey.[7]

The risks to the inflation outlook are assessed to the upside.

In the near term, inflation appears well contained. However, the medium-term outlook is more uncertain than usual, with material risks from the external environment. Domestic factors such as administered prices are also problematic.

Against this backdrop, the MPC decided to reduce the policy rate by 25 basis points, with effect from 31 January 2025. Four members preferred this action, while two supported an unchanged stance.

The committee ultimately agreed that it was possible to reduce the degree of policy restrictiveness, making the stance somewhat more neutral. However, all members were concerned about the uncertain global outlook.

The forecast sees rates drifting slightly lower over the next few years, stabilising near 7.25%. But this rate path from the Quarterly Projection Model remains a broad policy guide. The MPC would like to emphasise that its decisions will be made on a meeting-by-meeting basis, with no forward guidance and no pre-commitment to any specific rate path. Such decisions will continue to be outlook dependent, responsive to data developments, and sensitive to the balance of risks to the forecast.

Given the challenging global environment, the MPC spent some time during this meeting reviewing a trade war scenario. This featured a universal increase of 10

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[6] The implied starting point for the forecast is R18.45 per USD, for 2025Q1, from R17.96 as of the November 2024 forecast. The average for 2025 is now R18.62, from R18.09 previously.

[7] This survey, conducted by the Bureau for Economic Research at Stellenbosch University, shows average expectations for 2025 at 4.5%, as of the fourth quarter of 2024, from 4.8% previously. Similarly, two-year ahead expectations declined from 4.8% to 4.6%. Expectations for the coming five years were also at 4.6%, from 4.8% in the third-quarter survey.

percentage points in US tariffs, with retaliatory measures by other countries. The scenario showed higher inflation and interest rates globally, as well as greater risk aversion in financial markets. In response, our model projected the rand depreciating to nearly R21 to the dollar, with domestic inflation reaching 5% and the policy rate half a percentage point higher, at its peak, relative to the baseline forecasts.[8]

We also looked at a scenario of accelerated structural reforms, domestically. This showed growth picking up gradually, getting to 3% in 2027.[9] Importantly, this scenario also showed lower inflation and lower interest rates in South Africa, demonstrating how structural reforms can reduce the country risk premium and create more monetary policy space.

Considering the difficulties of the external environment, it remains crucial to sustain domestic reform momentum while protecting macroeconomic stability.

The MPC's main contribution is to deliver low and stable inflation, with well-anchored inflation expectations. The committee remains vigilant, and ready to recalibrate policy as needed.

Additional measures that would improve economic conditions include reaching a prudent public debt level, further repairing and strengthening network industries, lowering administered price inflation, and keeping real wage growth in line with productivity gains.

Lesetja Kganyago

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[8] In this scenario, the SA policy rate peaks about 50bps above the baseline path (ending 2025 at 7.87% instead of 7.39%) while inflation is around 50bps higher (4.4% in 2025 rather than 3.9%, and 5% in 2026 rather than 4.6%). Global short-term rates are 50bps higher, at their peak, relative to the baseline.

[9] The scenario assumed faster implementation of structural reforms than in the baseline forecast. In the initial years of the scenario, inflation is 10-20bps lower than in the baseline, and the policy rate moves about 25bps lower. Growth is higher by 0.1pp and 0.2pp in 2025 and 2026, respectively, and accelerates over time, reaching 1.9% higher than the baseline in 2029, and 2.4% higher in 2032 (implying that growth more than doubles). This reflects higher investment, more exports and a reduced risk premium.

The next statement of the Monetary Policy Committee will be released on 20 March 2025.

Contact person:

Thoraya Pandy

0824168416

media@resbank.co.za