Experts see repo rate increase as the start of more gradual increases

Yesterday's repo rate increase of 25 basis points by the South African Reserve Bank's (SARB) Monetary Policy Committee (MPC) shows a dovish outlook by the SARB and this appears to have disappointed markets, which, along with the contagion from the rate cut in Turkey, saw the rand come under pressure. The local currency touched R15.75 at one point before recovering at the close as exporters took advantage of the weaker rand.

Source: © fotogestoeber 123rf

Reza Hendrickse, portfolio manager at PPS Investments says the decision is in keeping with the trend across emerging market countries, many of which have already begun to hike interest rates.

“The decision to increase rates reflects the Committee’s view that although inflation should remain near the mid-point of the target band, inflation risks have increased,” he adds.

FNB chief economist, Mamello Matikinca-Ngwenya, says that the decision by the SARB to lift interest rates by 25bps is in line with the bank’s expectations.

“We project headline inflation to normalise from an average of 3.3% in 2020 to 4.5% in 2021.

“Over the next two years, we expect inflation to remain broadly contained around the 4.5% target, averaging 4.3% and

4.5% in 2022 and 2023, respectively," he says.

"This should allow for a gradual hiking cycle by the SARB - we currently expect a further 125bps cumulative increase in the repo rate by 2023.

"Notably, however, risks to our inflation outlook are biased to the upside," he adds.

Further gradual interest rate hikes

Hendricks also anticipates that further interest rate hikes are on the cards through a gradual hiking cycle.

"The Reserve Bank's Quarterly Projection Model currently expects interest rate hikes during every quarter for the next three years, which seems somewhat aggressive at this stage, but we recognise this will be sensitive to global inflation dynamics and policy settings," he says.

Thalia Petousis, portfolio manager at Allan Gray says that although the MPC's quarterly projection model suggests a rate hike at every meeting next year, Reverse Bank Governor Lesetja Kganyago attempted to temper this suggestion by asserting that further increases in the repo rate will be "gradual" – presumably with a weak consumer in mind.

"This narrative may not have been well received by foreign exchange traders who are keen to see a more hard line being taken, given the risks of emerging markets falling behind the curve should global central banks finally begin to raise dollar and euro interest rates," she says.

"The rand's depreciation to R15.75 to the dollar during the MPC meeting is also a classic case of our currency being thrown out with the Turkish bathwater given the lira's sell-off as CPI flies to 19.9% year-on-year, while their central bank continues to inappropriately cut rates," she adds.

She asks that while the quarterly projection model suggests that the repo rate should rise to 6.75% in 2024, which is still some time away, will the actual path of interest rate normalisation be gradual or rapid? "The MPC prefers the former, but they are, as ever, dependent on the data," she says.

A sign of economic recovery

FNB CEO Jacques Celliers believes that the rate hike is a sign that recovery is underway and that the rate adjustment should be read in the context of improving domestic demand, rising global inflation, and normalising global interest rates.

"Despite a few setbacks along the way, domestic economic recovery continues, spearheaded by better-than-expected household consumption expenditure and strong demand for our export products," he says.

He adds that improved consumer mobility, combined with the swift recovery in non-labour income, including strong dividend pay-outs as well as continued income support grants to economically vulnerable households, has inspired greater economic participation by consumers.