Reserve Bank hikes repo rate

PRETORIA: The Reserve Bank has decided to raise the repo rate by 25 basis points, taking it to 5.75%, Governor Gill Marcus said on Thursday, 17 July.

Image source: www.enca.com

"The Monetary Policy Committee (MPC) has decided to continue on its gradual normalisation path and raise the repurchase rate by 25 basis points to 5.75% per annum, effective from Friday, 18 July," said Marcus.

The governor said given the expected inflation trajectory, the real repurchase rate remains slightly negative and well below its longer term neutral level.

She said the monetary policy stance remains supportive of the domestic economy and that any future moves will be gradual and highly data dependent.

At its last MPC sitting in May, the bank continued to hold the view that it is in a rising interest rate cycle.

Marcus reiterated that monetary policy should not be seen as the growth engine of the economy.

"The sources of the below par growth performance are largely outside the realms of monetary policy. In the short term, an improvement in the interaction and relationships between management and labour is essential to foster a climate of trust and confidence, and get South Africa back to work," she said.

Prior to the MPC's announcement, analysts had been divided about whether the repo rate would remain unchanged or not.

In an earlier research note today, Standard Bank said it expected the bank to hike rates by 25 basis points, largely premised on concerns the central bank might have regarding perceived credibility, especially with inflation above the target range.

The Consumer Price Index (CPI) rose to 6.6% year-on-year in May.

The Reserve Bank targets inflation between 3% and 6%.

Meanwhile, Nedbank said it was likely that the bank would keep the repo rate unchanged at 5.5% in an attempt to balance weak economic growth and high inflation.

In January, the bank hiked the repo by 50 basis points. At the time the repo rate -- which is the scale at which the bank lends money to commercial banks - had up until January 2014 left the repo rate unchanged at 5% since July 2012.

Balancing act

On Thursday, Marcus said the MPC faces an increasingly difficult dilemma of rising inflation and slowing growth. At the same time, the core mandate of the bank remains price stability but that it has to be mindful of the impact that its actions have on economic growth.

The marginal improvement in the bank's forecast of headline inflation at the last meeting have been reversed as recent food price developments surprised on the upside. The bank now expects inflation to average 6.3% in 2014, compared with the previous 6.2%.

The forecast average inflation for 2015 increased to 5.9% from 5.8%.

"Inflation is still expected to return to within the target band during the second quarter of 2015, provided that there are no further shocks to the system," Marcus said.

The forecast for core inflation is unchanged and is expected to average 5.6% per cent and 5.7% in 2014 and 2015 respectively, moderating to 5.5% in 2016.

"As before, the MPC sees the risks to the headline inflation forecast to be skewed to the upside," Marcus said.

The MPC further added the rand continues to pose an upside risk to the inflation outlook, with the currency having depreciated by 2.6% on a trade-weighted basis since the last meeting in May.

Since its last meeting, the country's growth outlook has deteriorated, compounded by continued labour disruptions.

"Following a contraction of 0.6% in the first quarter, the outlook for the second quarter is expected to be positive, but subdued, particularly in light of weak mining and manufacturing data in May," explained Marcus.

The bank's latest forecast, which assumes a speedy resolution of the metal workers' strike, sees growth in 2014 at 1.7% compared to 2.1% previously.

The growth forecast for the coming two calendar years have been reduced to 2.9% and 3.2% from 3.1% and 3.4% respectively.

The bank said that the trend in wage settlements poses an upside risk to the inflation outlook.

"These pressures are likely to intensify in the current difficult labour relations environment," she said.