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in the moment

Sanisha Packirisamy
Chief Economist

Tshiamo Masike
Economic Analyst

Rand gains and stable oil keep inflation muted at 2.8% in April

Headline inflation (CPI) lifted from 2.7% y/y in March to a still muted 2.8% y/y in April.

The acceleration was primarily due to food and non-alcoholic beverages (NAB) inflation rising by 4% y/y from 2.7% y/y.

Core inflation eased slightly to 3% y/y in April from 3.1% y/y in March.

This was mainly due to a deceleration in restaurant and accommodation services inflation (3% y/y from 4.2% y/y).

Oil prices subdued but fuel levy increase introduces upward pressure to fuel inflation.

Brent crude prices are expected to stay subdued as oil supply outpaces demand, while Budget 3.0 announced an inflation-linked fuel levy increase.

Price pressure emerges in food inflation.

Meat and cereal inflation are expected to rise due to stronger red meat demand and elevated white maize prices.

So what?

With lower oil prices, a stable rand, weak economic growth, and the scrapping of the value-added tax (VAT) hike, the South African Reserve Bank (SARB) is likely to revise its 2025 inflation forecast down from 3.6%. The Reuters consensus has shifted lower to 3.7% for 2025 to reflect these factors. We continue to expect at least one more interest rate cut to 7.25% in 2025 but the SARB is likely to proceed with caution thereafter given global risks.

Easing trade tensions between the United States (US) and China reduce global recession risks. Consequently, imported deflation from China may also lessen. Fixed income markets (as of 21 May) are pricing in just one cut by year-end, down from an expected two cuts in April which likely reflects shifting US policy expectations. A potential shift lower in SA's inflation target further limits the scope for interest rate cuts.

Consumer lens

Food inflation rose to 3.3% y/y in April (2.2% y/y in March).

The average cost of a household food basket* in April 2025 was R5 420.3, up by 1.6% y/y or R83.99.

Transport deflation deepened to 3.9% y/y in April from 2.4% y/y in March.

Petrol (ULP 95) users may pay R0.22/l less in June 2025 while diesel (0.05%) could cost R0.49/l less*.

* According to the Pietermaritzburg Household Affordability Index
The average food basket includes bread, frozen chicken portions, maize meal, sugar, beef, rice, cooking oil, potatoes, tinned pilchards, wors and other items.

** According to the Central Energy Fund (CEF) on 20 May.
The petrol cost of an average car (45 litres) is R963 in May 2025, R9.9 less than in April 2025.

Headline inflation remained below the lower limit of the inflation target band

According to Statistics (Stats) SA, headline inflation inched up slightly to 2.8% y/y in April 2025, from 2.7% y/y in March. This was against the Reuters median expectation for unchanged inflation. The rise was mainly due to higher inflation in the food and NAB category, while downward pressure came from the transport category.

On the other hand, core inflation eased marginally to 3% y/y in April from 3.1% y/y in March, defying Reuters median consensus expectations of an increase to 3.2% y/y. Restaurants and accommodation services, as well as clothing and footwear inflation, decelerated, contributing to the decline in core inflation.

Goods inflation fell to 1.7% y/y in April from 2% y/y in March, while services inflation rose to 3.8% y/y from 3.5% y/y over the same period. Within the services category, upward pressure stemmed from information and communication services (2.4% y/y from 0.7% y/y) and passenger transport services (negative 0.7% y/y from negative 1.7%). Moreover, package holidays inflation spiked to 6.5% y/y from 1% y/y.

> At these levels, all key measures of inflation (headline, core, goods and services) remain below the midpoint of the inflation target range.

Oil prices averaged below US$70/bbl in April for the first time since May 2021

Transport fell deeper into deflation territory at 3.9% y/y in April on the back of notable decreases in fuel prices (R0.72/l for petrol and R0.84/l for diesel). These large decreases were due to a stronger rand (R18.29/US$ in March from R18.48/US$ in February) and lower Brent crude oil prices (US$72.7/bbl in March from US$75.4/bbl in February).

The international oil market remained benign with average Brent crude prices declining for the third consecutive month and slipping below US$70/bbl in April (see chart 1).

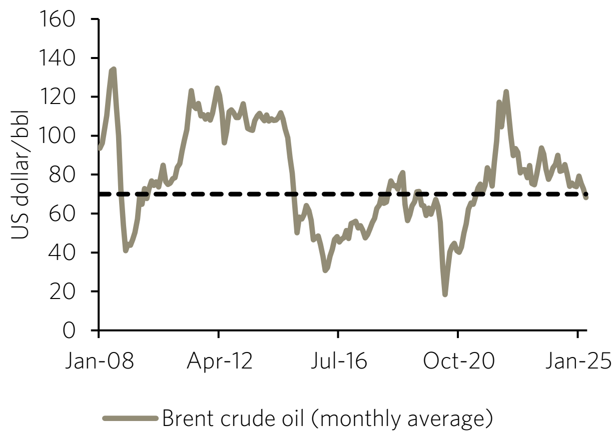
On the other hand, the rand weakened to an average of R18.91/US$ in April which caps the full oil price benefit to local petrol prices. As reported by the CEF, petrol prices decreased marginally by R0.22/l in May and R0.42/l for diesel. Given continued subdued oil prices in May and a stronger rand, the CEF is guiding to a further decrease in fuel prices in June.

For the first time in three years, the finance minister implemented an inflation-related increase in the fuel levy in Budget 3.0 to help offset the revenue shortfall from the reversal of the VAT increase.

> The fuel levy increase represents a R0.15c/l increase to R3.85/l for diesel and R0.16c/l increase to R4.01/l for petrol, effective from 4 June 2025.

This introduces upside pressure on fuel inflation and thus transport inflation.

Chart 1: Slip in oil prices continued



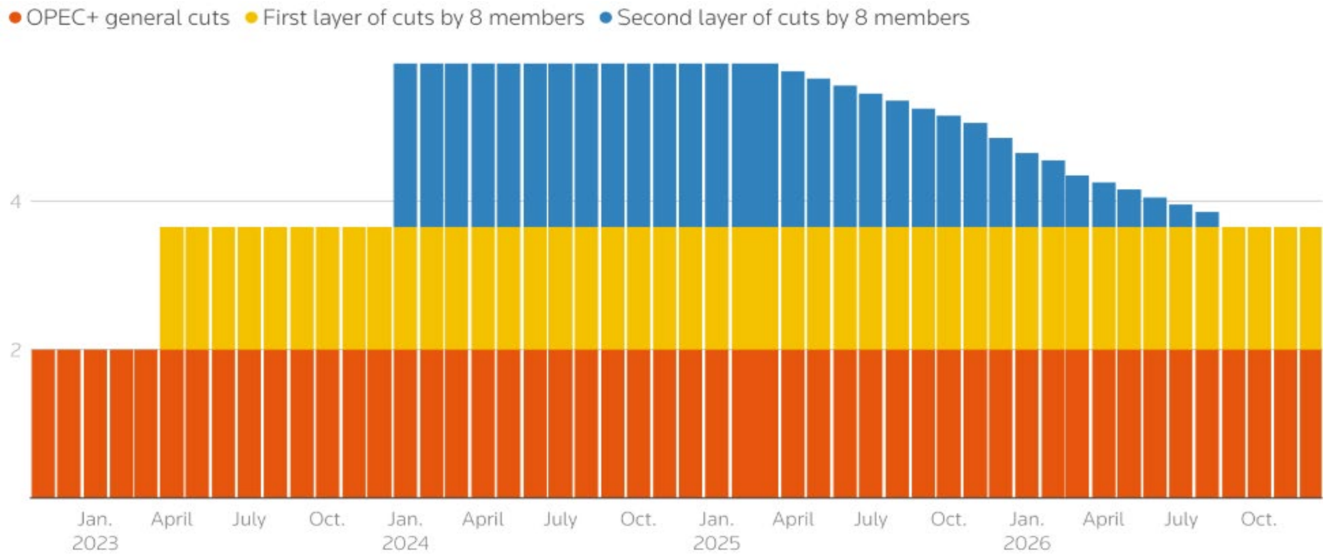
Source: Energy Information Administration, Momentum Investments

Signs of de-escalating trade tensions following the US lowering tariffs on Chinese goods from 145% to 30%, and China reducing tariffs from 125% to 10% on US goods for a 90-day period, alongside a trade deal between the US and United Kingdom, helped lift oil prices slightly in May.

> Nevertheless, the International Energy Agency (IEA) expects global oil supply growth to "considerably outpace demand growth" in 2025, suggesting oil prices will likely remain subdued.

The stronger oil supply outlook is driven by a faster-than-expected unwinding of OPEC+ (Organisation of the Petroleum Exporting Countries plus) production cuts (see chart 2), as well as rising output from non-OPEC+ producers. However, potential tighter sanctions on Venezuela, Iran and Russia could limit some of the expected increases from OPEC+. Meanwhile, lower oil prices are weighing on US shale production. In May, the IEA cut its forecast for US light oil output for the second consecutive month.

Chart 2: Eight members of OPEC+ unwinding production cuts faster than announced in February 2025



Source: Reuters

Note: Chart shows planned unwinding in February 2025 in millions of barrels

Pressure emerges in food inflation

Food and NAB inflation rose to 4% y/y in April from 2.7% y/y in March, driven by an increase in food inflation (3.3% y/y from 2.2% y/y), while NAB inflation eased to 7.6% y/y from 7.9% y/y. Five of the nine food categories saw faster inflation, with the main drivers being the two largest components: meat (3% y/y from 0.4% y/y) and cereal products (4.8% y/y from 4.3% y/y). Inflation in oils and fats also accelerated, rising to 4.8% y/y from 2.2% y/y.

The upward pressure on cereal product prices stems from elevated white maize prices. While these have come down from recent peaks, they have started trending upward again.

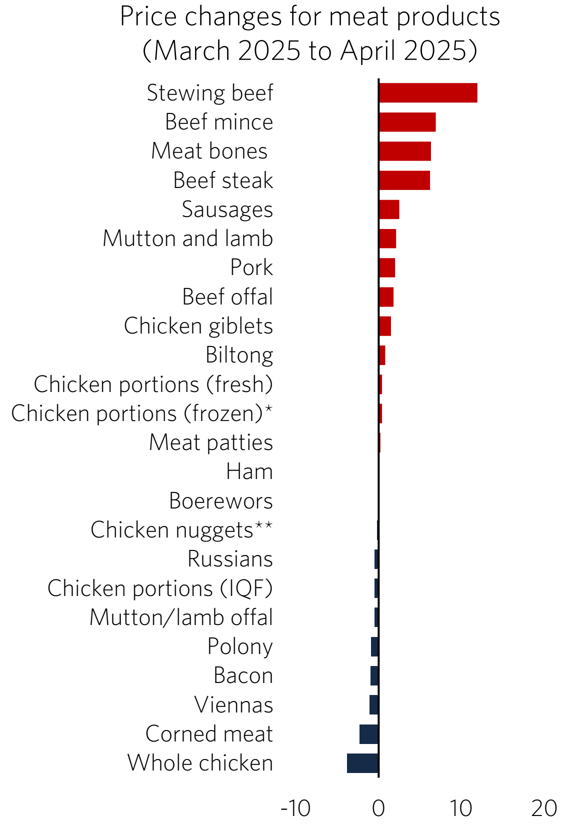
According to the United Nation’s Food and Agriculture Organisation, international maize prices rose in April due to “seasonally tighter stock levels in the US”, exchange rate movements and recent changes to US import tariff policies, including the exemption of Mexico and the suspension of tariffs above 10% for several other trade partners. These factors contributed to higher cereal prices, which—along with an increase in meat prices—more than offset declines in dairy and vegetable prices, resulting in a 1% month-on-month rise in the global food price index in April.

The SARB expects meat and cereal product inflation to rise to 2.6% and 5.2%, respectively, in 2025.

> Meat inflation is expected to rise as the impact of previous low base effects fades and demand for red meat strengthens. Meanwhile, elevated white maize spot prices are likely to keep cereal inflation high through mid-2025.

However, the expected return of La Niña weather conditions could help ease these pressures in the second half of the year.

Chart 3: Highest meat price increase recorded for red meat in April



** non-IQF*

*** Chicken nuggets, strips and fingers***

Source: Stats SA, Momentum Investments

Soft inflation outlook points to a higher likelihood of a cut at the May interest rate meeting

Headline inflation averaged 3% in the first quarter of 2025, in line with the SARB's March 2025 forecast. With inflation remaining subdued at the start of the second quarter and signs of a softer inflation outlook due to lower oil prices, a stable currency, weaker economic growth and the scrapping of a VAT hike which triggered Budget 3.0, the SARB is likely to revise its annual inflation forecast down from 3.6% for 2025. The median consensus inflation expectation by Reuters has fallen from 4.1% for 2025 at the start of the year to 3.7% in the April survey.

A softer inflation outlook points to an increased likelihood of an interest rate cut at the upcoming May interest-rate setting meeting. While the bias is for another cut thereafter, we note that the Monetary Policy Committee will likely maintain a cautious approach to easing monetary policy too far below the neutral level given ongoing global and local risks.

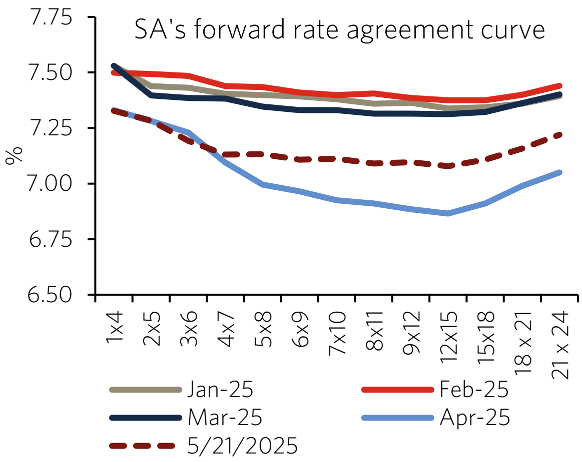
> While negotiations to reduce tariff rates between the world's largest economies (the US and China) bode better for global inflation and growth than previously anticipated, this also means the drag on China's inflation will be smaller.

With a less pronounced demand shock, the imported deflation from China to SA will likely be less.

The forward-rate agreement curve as of 21 May 2025 had fully priced in one 25 basis point rate cut by year-end but not in the May meeting. This represents a scaling back of expectations from two cuts priced in at the end of April (see chart 4), likely reflecting shifting expectations for US monetary policy, as recession fears eased.

Interest rates falling significantly below the SARB's estimated neutral level of 7.25% would likely require a global recession. However, the recent de-escalation in US-China trade tensions reduces the likelihood of such a scenario and in turn, the likelihood of the SARB cutting far below neutral, in our view. Global fund managers' expectations for a so-called hard landing in the next 12 months pulled back to 26% in Bank of America Merrill Lynch's Fund Manager Survey in May from 49% in April 2025. Furthermore, the comment from the deputy finance minister that an announcement on the inflation target will be made "soon" limits the scope for further interest rate cuts.

Chart 4: Fixed income market has scaled back interest rate cut expectations



Source: Bloomberg, Momentum Investments