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All Signal, No Noise

MARKET ANALYSIS

MNI South African Reserve Bank Review: July 2025

Executive Summary:

- **The central bank delivered a unanimous decision to cut rates by 25bp.**
- **The SARB shifted its implicit inflation target lower to +3.0% Y/Y.**
- **Talks with the Treasury on the formal inflation target reform are ongoing.**

Key Links:

- **MPC Statement**
- **Press Conference**
- **Forecast Report**

Key Takeaways: Aiming Lower

The South African Reserve Bank (SARB) took the opportunity provided by dampened inflation and receding inflation expectations and delivered the expected 25bp cut to its policy rate, bringing it to 7%. Uncertainty remained a key theme of the statement as global risks abound. Alongside the rate decision, the central bank took another step in the ongoing overhaul of its inflation-targeting regime. Although the reform is still technically in the works, the Monetary Policy Committee (MPC) now explicitly declared that it will aim to keep inflation at the bottom of its official target range (+3.0-6.0% Y/Y) and said it would use forecasts assuming a +3% Y/Y target as a point of reference at future meetings.

The market was relatively unfazed by the SARB's decision to lower interest rates by 25bp, an outcome predicted by a clear majority of analysts. Governor Lesetja Kganyago said that the decision was unanimous amid a benign inflation outlook, with headline CPI expected to tick higher to +3.3% Y/Y in the coming months and then stabilise around the target through the rest of the forecast period. The unanimous vote fell on the dovish side of expectations, with consensus leaning towards a split vote. The risks to the growth and inflation projections were assessed as balanced. Uncertainty remained an important theme of the SARB's communications, as the spectre of an imminent US tariff hike hanged over the central bankers as they deliberated interest-rate action. However, Governor Kganyago emphasised during his press conference that tariffs are only relevant to monetary policy insofar as they have an impact on prices.

With the outcome of the vote priced in, progress on the inflation target reform was arguably the highlight of this MPC meeting. Governor Kganyago declared that from now on, the MPC will prefer to see inflation anchored at the lower end of the official +3.0-6.0% Y/Y target range rather than at the +4.5% mid-point. This follows from the SARB's decision to append an alternative forecast scenario assuming a +3.0% inflation target to the set of projections that informed its monetary policy meeting in May. The Governor clarified that the +3.0-6.0% target range remains in force the shift in the implicit target was akin to the informal yet meaningful move to the +4.5% mid-point in 2017. Following the meeting, Finance Minister Enoch Godongwana refused to comment on the matter and said that any formal steps will be announced 'through our normal meetings' and during the Medium-Term Budget Policy Statement (MTBPS).

It is now clear that the gradual implementation of the inflation target reform is effectively underway. While the forecasting exercise in May could have been interpreted as a technical rehearsal, the next step taken this week significantly increases the costs of reversing the process. Although the formal announcement will likely be made during the MTBPS in autumn, the SARB has taken early action and shifted its focus while inflation remains stable around the bottom of the target range. The decision to implicitly shift the inflation objective before the Treasury's announcement has two-way implications – on the one hand, it raises questions about policy coordination; on the other hand, it allows the SARB to demonstrate its determination to anchor inflation at lower levels. Looking ahead, the SARB's Quarterly Projection Model (QPM) implies five more cuts under the +3% Y/Y scenario. However, the SARB has repeatedly stated that the QPM is merely a policy guide.

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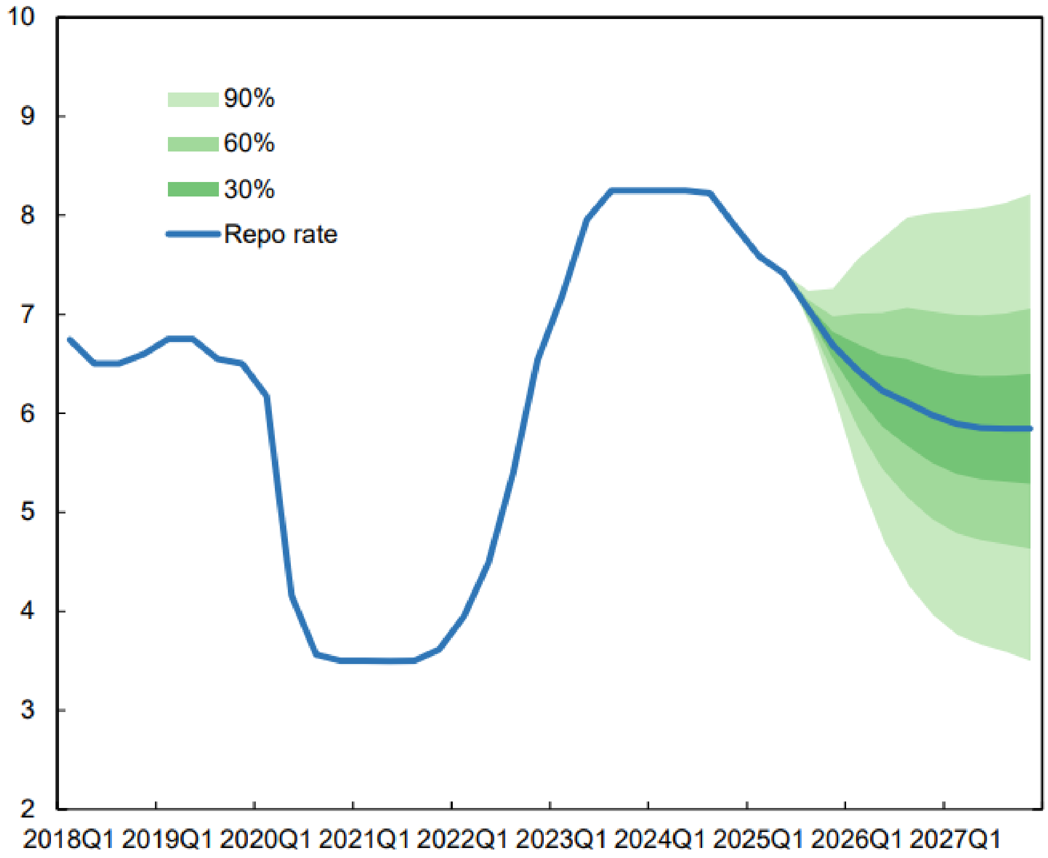
SARB Interest-Rate Forecast

Repurchase rate forecast*

Per cent



*The uncertainty bands for the repo rate are based on historical forecasting experience and stochastic simulations in the Quarterly Projection Model (QPM). The bands are symmetric, and therefore do not reflect any assessment of upside or downside risk. For details on the QPM see 'Enhancing the Quarterly Projection Model', South African Reserve Bank Working Paper Series No. WP/23/05, June 2023.

Source: SARB

Analyst Views (Alphabetical Order)

BER: SARB Signals Preference For Lower End Of Inflation Target

- In their view, the key takeaway from the MPC press conference was the announcement that future MPC decisions would be anchored around the lower bound of the +3-6% Y/Y target band.
- SARB Governor Lesetja Kganyago noted that this was not an official change in the target, as would mandate approval from National Treasury; it is rather the preference of the SARB, much as was the move to +4.5% Y/Y.
- June consumer inflation was in line with the preferred rate; however, the SARB expects inflation to pick up over the next few months.

- Looking ahead, the SARB's Quarterly Projection Model (based on the newly adopted +3% Y/Y target) suggests five more cuts over the medium term. However, the MPC is not beholden to the QPM.

Commerzbank: Trying To Anchor Inflation Close To +3% Y/Y

- They write that the SARB had a surprise up its sleeve: the inflation target will be lowered from +4.5% Y/Y to +3% in the future. The central bank admitted that discussions with the Ministry of Finance on a new (official) inflation target are still ongoing. The SARB also did not want to commit to what such a new target might look like. However, given that inflation has now been hovering around +3% for almost nine months, the SARB wants to seize the opportunity to anchor inflation expectations among South African stakeholders (households, businesses and market participants) at this level for the long term.
- The central bank is aware that there will be a transition phase during which the key interest rate will have to remain higher in order to anchor inflation at the new level, which in turn is likely to weigh on GDP growth. However, it believes that a lower inflation target is preferable in the long term, as it makes the economy more resilient to shocks and, with a lower inflation target, inflation and inflation expectations converge more quickly back towards the target.
- In addition, the central bank's forecasts indicate that a lower inflation target could pave the way for lower key interest rates in the medium term. The SARB expects the key interest rate to fall further as early as 2025 and to be lowered to 6% in 2026. This would be good news for the South African economy, which would certainly welcome structurally lower interest rates. All in all, the lowering of the inflation target is to be welcomed, although approval and an official statement from the Ministry of Finance would certainly give this change even more weight. The lower target should be positive for the ZAR in the long term. In the medium to short term, however, political risks remain imminent, making the rand prone to volatility.

Goldman Sachs: Expecting 50bp Of Further Cuts This Year & Further 150bp Afterwards

- The SARB has signalled a shift to an effective +3% Y/Y inflation target within its 3-6% target range. Meanwhile, National Treasury indicated that they will comment on the inflation target in the Medium Term Budget Policy Statement. SARB forecast revisions on the back of the policy announcement are substantial and assume a continued decline in inflation expectations, settling lower at the new 3% target during 2027.
- Goldman previously laid out macro scenarios for inflation and the policy rate under a potential reduction in the inflation target, with their analysis largely concurring with the SARB's: inflation is likely to remain anchored around +3% Y/Y, leaving space for front-loaded rate cuts provided that inflation expectations continue to fall. Relative to the market, Goldman's view on inflation is significantly more benign, on account of greater emphasis on a) weak demand holding back core; and b) downward pressure from declining inflation expectations. Given this more benign inflation outlook and falling inflation expectations, Goldman made the case for front-loaded policy easing to a lower terminal rate.
- Given the announcement from SARB, Goldman raise their 2025 forecast slightly from +3.1% Y/Y to +3.3% on recent food/supply factors but lower their 2026 forecast from +3.7% to +3.3% and their 2027 forecast from +4.0% to +3.1%. Their inflation forecast is aligned with the SARB's downward-revised outlook. With respect to growth, they leave their 2025 forecast unchanged at +1.0% and lower their 2026 forecast from +2.0% to +1.6%. With respect to the policy rate, they keep their forecast for 50bp of further cuts in the remaining two MPC meetings in 2025 unchanged (down to 6.50%) but build in a further 150bp of rate cuts down to a 5.0% terminal rate.

HSBC: Lower Implicit Inflation Target

- They note that in the latest press conference, the rate decision was not the focus. It was all about the adoption of a new inflation target. While technical discussions continue with the National Treasury, the SARB's Governor suggested an implicit change to the inflation target.
- Recall that in 2017, the central bank adopted a similar approach emphasising that its policy setting was designed to lower inflation to the mid-point of the range (i.e. +4.5%). This policy approach contributed to lower inflation expectations and hence has been pivotal in the recent inflation successes. It seems that the SARB wants to take a step further and adopt a new implicit target of +3.0%.
- Such an announcement may raise some questions about a lack of coordination with the government. However, it seems that the SARB does not want to miss the opportunity of having inflation already close to +3.0% to anchor inflation expectations at a lower level.

JP Morgan: Expecting Policy Rate Of 6.25-6.50% By End-2027

- JP Morgan note that the SARB's implicit inflation target has shifted, making it likely that the Finance Minister will formally adjust the inflation target, probably in October MTBPS. In an earlier significant move, the SARB had added a +3% Y/Y target scenario at its last MPC statement in May, stressing that a lower target would lead to lower interest rates (eventually).
- In their view, while a formal joint statement by the Governor and Finance Minister would have served as a more powerful commitment signal to a +3% Y/Y target, the target reform is now well underway and unlikely to be reversed. For the SARB, it seemed the benefits from locking-in currently low inflation outweighed concerns of going it alone.
- Key to the successful execution is the SARB's significant credibility and a likely steadfast affirmation of the new target. They think the MPC is unlikely to backtrack from here, having acknowledged that shocks will occur under any target, even as theoretically National Treasury could refuse to amend the target range. Of course, the SARB will closely monitor inflation expectations, but it articulated a relatively realistic time horizon of about three years before inflation expectations likely settle at the new lower level.
- JP Morgan largely differ with the SARB on the timing of downward drifting inflation expectations and inflation as they model inflation expectations on the pattern similar to the 2017-2019 implicit target shift from +6% Y/Y to +4.5%.
- In their view, given the need to entrench lower inflation expectations, a further cut in 4Q25 is unlikely (unless the growth outlook significantly deteriorates). In this light, the J.P. Morgan SARB Hawk-Dove indicator shows the latest statement as the least dovish since 3Q24 with a close-to-neutral tone. However, they now pencil in an additional repo rate cut in 4Q26 to 6.75% (with risks of 6.5%) and anticipate a policy rate of 6.25%-6.50% by end-27.

Nedbank: Another 25bp Cut, Inflation Target Lowered To +3% Y/Y

- Nedbank note that with the +4.5% Y/Y inflation target, the SARB's Quarterly Projection Model projects the repo rate bottoming out at 7%. However, at the lower target of 3%, the QPM predicts five more rate cuts over the medium term, taking the repo rate below 6%. The model reflects that interest rates have to decline as inflation eases in order to prevent the real interest rate from rising too much.
- A relatively calmer global environment than at the time of the May meeting, when the announcement of the reciprocal tariffs by the US weighed on sentiment and caused chaos in the markets, was a key factor in the MPC's decision to cut the repo rate. The rand has since recovered significant ground and is still resilient. Oil prices have also remained contained, reflecting ample global supply versus weak demand. As a result, the MPC believe that the inflation outlook is benign. Meanwhile, the growth trajectory remains weak, and therefore, there is no demand pressure on prices.
- Nedbank believe that the SARB's profound announcement of a lower inflation target paved the way for this week's interest rate cut. Future rate moves will, in addition to the usual economic developments, be influenced by progress in maintaining inflation around +3% Y/Y. Under the +4.5% inflation target scenario, they see no room for further cuts in this cycle as inflation would rise to +4.5% in 1Q2026.