Reserve bank keeps repo rate unchanged

The Reserve Bank's Monetary Policy Committee [MPC] has kept the repo rate unchanged at 5% as expected by the market.

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"The MPC has therefore decided to leave the repurchase rate unchanged at 5% per annum. The MPC is ready to act appropriately in either direction in the event of material changes in the outlook," Governor Gill Marcus said on Thursday.

The MPC said it was increasingly concerned about the South African economy's deteriorating outlook including issues that are contributing to the vulnerability of the economy such as the fractious labour relations environment and the associated risks of protracted work stoppages and excessive wage increases and electricity supply constraints among others.

"These interrelated developments are reflected in the volatility and weakness in the exchange rate. There is an urgent imperative for all parties - government, business, labour and civil society - to interact and address these issues and vulnerabilities at a national level," said the governor.

Difficult labour relations environment continued to dominate the economic landscape thereby contributing to declining domestic and foreign investor confidence. This could be seen in the depreciating and volatile exchange rate.

Statistics South Africa (Stats SA) on Wednesday released data of the Consumer Price Index (CPI) for April that came in at 5.9% unchanged from the previous two months. The MPC said that its inflation forecast since its last meeting had remained relatively unchanged with a temporary breach of the upper end of the bank's target range expected in the third quarter but at a lower average of 6.1% from 6.3% previously. The bank targets inflation between 3 and 6%.

Inflation is expected to moderate to 4.9% in the fourth quarter of 2015. "The slight improvement is due to changed assumptions about international commodity prices, including oil, and lower global inflation."

The global economic environment continued to be challenging with different regions growing at varying rates. The exchange rate of the rand continues to be impacted by external developments and is also compounded by domestic factors.

"The increasingly fraught labour relations environment, and high wage demands in the mining sector in particular, are likely to continue to impact adversely on the volume of mining exports against a backdrop of falling international commodity prices and concerns about the widening of the current account deficit of the balance of payments," noted Marcus.

South Africa's credit ratings could be affected by these developments.

Since the previous meeting of the MPC, the rand has depreciated by around 4.6% against the US dollar.

The MPC further noted that the current level of the rand if sustained poses a significant upside risk to the inflation outlook.

The central bank revised down its growth forecast from 2.7% to 2.4% for 2013 and from 3.7% to 3.5% in 2014. Growth is expected to accelerate to 3.8% in 2015.

The central bank expressed concern about the prospect of wage settlements, this as a several sectors of the economy are entering into wage-bargaining rounds.

"The MPC is increasingly concerned about the prospect of settlements well above inflation and productivity growth and the risk of protracted and disruptive strike action, with negative implications for growth and exports. Furthermore, excessively high settlements will come at the expense of retention of employees, employment creation and could result in higher inflation. The risk of a wage-price spiral remains high."

In a research note on Wednesday, Nedbank economists said they believe rates will remain at the current levels for the rest of this year.

"The latest inflation numbers do not alter our interest rate view. We believe that rates will remain at current levels for the rest of this year. The MPC will need to strike a balance between high inflation and still poor economic growth outcomes, with the current policy stance likely to remain in place well into 2014," noted Nedbank.