Nedbank
Economic commentary

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## CONSUMER INFLATION


Research

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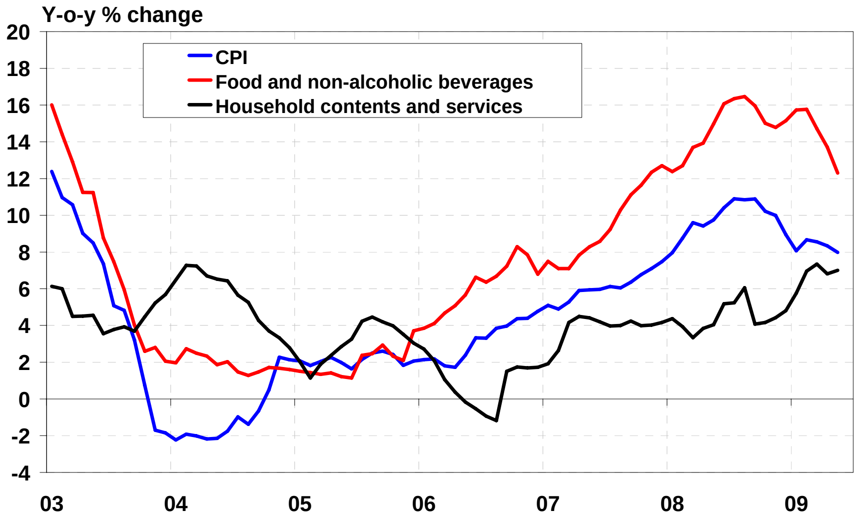
### *Inflation remains sticky*

**Latest (May 2009)**

Overall: 8% y-o-y, 0,4 % m-o-m (8,4% y-o-y in April 2009)
Nedbank forecast: 7,8% y-o-y
Market forecast: 7,9% y-o-y

Graph 1: Consumer price inflation




**Comment**

Consumer inflation is still proving to be very sticky, but, on the positive side inflation is now below where it was in January 2008. CPI fell less than expected in May, mainly due to increases in the prices of food, cars and household goods.

International food prices have continued to rise, which probably goes some way to explain the increase in food prices recorded over the past few months. Food prices increased by 0,5% m-o-m, following an increase of 0,4% in the previous month. Overall, higher food prices contributed 0,1 percentage points to the monthly rise. The increase was mainly due to higher prices for dairy products and eggs (1,4% m-o-m) as well as other foods, which rose by 2,1% m-o-m. Food inflation, however, continued to ease, dropping to 12,1% y-o-y, reflecting the high base established in 2008.

The price of vehicles, which makes up 11,3% of the total basket, rose by 1,4% m-o-m, taking the annual increase to 4,7% from 3,1% in the previous month. This reflects the impact of the rand's sharp decline late last year, which manufacturers are passing on to the consumer despite the collapse in demand for new vehicles.

The price of household contents and services also rose quite strongly over the month, increasing by 0,8% m-o-m, taking the annual increase to 7% from 6,8% in the previous month. This mainly reflects an increase in the price of household supplies as well as appliances and other electronic equipment.

**Outlook**

Our preliminary inflation forecast for June suggests further easing to around 7%. June is a survey-heavy month, with survey results being released for owner's equivalent rent, rent as well as public transport and vehicle insurance, which might result in a positive surprise. Fuel prices rose in June, which will contribute towards the month-on-month increase.

Inflation is expected to ease over the coming months due to base effects, following the sharp run up in commodity prices last year and their subsequent decline. However, inflation could remain sticky, particularly if retailers don't respond to weakening demand by cutting prices.

**The inflation outlook will depend largely on four factors.**

First, changes in **food prices** will remain crucial to the direction of inflation in the next few months. Excluding the modest decline in food prices in February, food prices have continued to rise every month, despite lower international food prices and much weaker demand for non-durable goods. More recently, international food prices have begun to march upwards again, making it unlikely that consumers will see lower food prices in the short term. Additionally, our monthly snap survey of prices points to continued price increases by the key retailers during June.

Second, **services inflation**, which tends to be backward looking, may still rise this year reflecting last year's higher inflation. However, the contraction in consumer spending suggests that insurers, hoteliers and restaurateurs may have to revise plans to increase prices much further this year.

The **rand** and **energy prices** will also remain key. The rand remained firmly below R8,50 to the dollar in recent months, and this will contribute to lower imported inflation. The extent of the recent increase in oil and food prices will also be muted by the rand's rally. However, should international commodity prices continue to rise, which does seem unlikely given still weak international demand, this could keep inflation above the target for longer.

**Implications**

Today's inflation figure, although disappointing, does not change our interest rate view. The Reserve Bank will continue to look beyond the next few months' inflation figures and focus on the medium-term inflation outlook as well as the severe contraction in domestic economic activity.

With the extent and duration of the global and local downturn remaining uncertain, the Monetary Policy Committee will continue to cut interest rates in order to provide the domestic economy with some support against the global recession. We therefore still forecast more interest rate cuts in the coming months, with the prime rate falling to 10,5% at this week's meeting and to around 10% by September.

| | CPI | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | May 2009 | | | | | April 2009 | |
| | Weights<br>Base 2008 | Month-on-month<br>% | %<br>contrib | Year-on-year<br>% | Average<br>m-o-m<br>past 3 yrs | Average<br>y-o-y<br>past 3 yrs | Month<br>% | Year<br>% |
| **CPI for all urban areas** | 100 | 0.4 | 0.38 | 8.0 | 0.5 | 7.89 | 0.5 | 8.3 |
| **Food and non-alcoholic beverages** | **15.68** | **0.5** | 0.09 | **12.3** | **1.1** | **11.85** | **0.5** | **13.7** |
| Food | 14.27 | 0.5 | 0.08 | 12.1 | 1.1 | | 0.4 | 13.7 |
| Bread and cereals | 3.08 | -0.1 | 0.00 | 10.8 | 2.6 | 16.78 | -0.3 | 17.9 |
| Meat | 4.59 | 0.7 | 0.03 | 10.3 | 0.9 | 9.79 | -0.1 | 10.4 |
| Fish | 0.66 | 0.3 | 0.00 | 14.1 | 0.7 | 10.79 | 0.2 | 16.2 |
| Milk, eggs and cheese | 1.79 | 1.4 | 0.02 | 13.1 | 1.6 | 14.20 | 1.6 | 12.2 |
| Oils and fats | 0.53 | -1.8 | -0.01 | -3.7 | 0.7 | 20.74 | -3.1 | 1.0 |
| Fruit | 0.47 | -1.9 | -0.01 | 14.8 | -3.4 | 10.61 | 2.6 | 12.2 |
| Vegetables | 1.63 | 0.3 | 0.01 | 17.6 | 0.4 | 12.23 | 1.0 | 17.9 |
| Sugar, sweets and deserts | 0.77 | 1.2 | 0.01 | 16.2 | 1.4 | 9.68 | 2.2 | 16.4 |
| Other | 0.75 | 2.1 | 0.02 | 17.9 | 1.4 | 12.71 | 1.3 | 17.3 |
| Non-alcoholic beverages | 1.41 | 1.0 | 0.01 | 14.9 | 0.7 | 9.53 | 1.4 | 14.2 |
| **Alcoholic beverages and tobacco** | **5.58** | **0.2** | 0.01 | **10.8** | **0.2** | **9.09** | **0.0** | **10.9** |
| Alcoholic beverages | 3.29 | 0.3 | 0.01 | 9.1 | 0.2 | 7.63 | 0.8 | 9.1 |
| Tobacco | 2.29 | 0.2 | 0.00 | 13.3 | 0.1 | 11.10 | 0.4 | 13.5 |
| **Clothing and footwear** | **4.11** | **0.1** | 0.00 | **5.0** | **0.0** | **2.28** | **0.4** | **5.1** |
| Clothing | 2.9 | 0.2 | 0.01 | 5.5 | 0.1 | 2.49 | 0.4 | 5.6 |
| Footwear | 1.21 | 0.1 | 0.00 | 3.9 | 0.0 | 1.85 | 0.4 | 4.0 |
| **Housing and utilities** | **22.56** | **0.0** | 0.00 | **8.0** | **0.1** | **10.56** | **0.1** | **8.1** |
| Actual rentals for housing | 3.49 | 0.0 | 0.00 | 6.4 | 0.6 | 8.79 | 0.0 | 6.4 |
| Owners equivalent rent | 12.21 | 0.0 | 0.00 | 0.0 | 0.0 | 0.00 | 0.0 | 0.0 |
| Maintenance and repairs | 1.68 | 0.4 | 0.01 | 15.0 | 0.8 | 11.27 | 0.7 | 16.9 |
| Water and other services | 3.31 | 0.0 | 0.00 | 0.0 | 0.0 | 0.00 | 0.0 | 0.0 |
| Electricity and other fuels | 1.87 | -0.1 | 0.00 | 29.5 | 0.0 | 14.81 | -0.1 | 29.4 |
| **Household contents and equipment** | **5.86** | **0.4** | 0.02 | **7.0** | **0.2** | **5.15** | **0.1** | **6.8** |
| Furnishings, floor coverings and textiles | 2.17 | 0.2 | 0.00 | 0.9 | -0.2 | -1.04 | -0.3 | 0.1 |
| Appliances, tableware and equipment | 1.05 | 0.3 | 0.00 | 16.1 | 0.4 | 6.69 | 0.7 | 16.6 |
| Supplies and services | 2.64 | 0.6 | 0.01 | 8.6 | 0.4 | 8.27 | 0.2 | 8.6 |
| Domestic workers wages | 1.99 | 0.0 | 0.00 | 6.2 | 0.0 | 7.45 | 0.0 | 6.2 |
| **Health** | **1.47** | **0.3** | 0.00 | **11.7** | **0.4** | **8.64** | **0.6** | **12.2** |
| **Transport** | **18.8** | **0.8** | 0.15 | **0.5** | **1.1** | **3.62** | **1.3** | **1.0** |
| Purchase of vehicles | 11.25 | 1.4 | 0.15 | 4.8 | 0.2 | 0.05 | 0.6 | 3.1 |
| Private transport operation | 4.82 | -0.3 | -0.02 | -16.2 | 2.8 | 8.25 | 4.2 | -11.5 |
| Petrol | 3.93 | -0.5 | -0.02 | -22.7 | 3.5 | 8.57 | 4.9 | -17.4 |
| Other running costs | 0.89 | 0.4 | 0.00 | 13.8 | 0.6 | 10.33 | 1.8 | 14.5 |
| Public Transport | 2.73 | 0.4 | 0.01 | 14.7 | 0.4 | 5.97 | -0.1 | 15.0 |
| **Communication** | **3.22** | **0.0** | 0.00 | **0.9** | **0.0** | **0.06** | **-0.1** | **1.0** |
| **Recreation and culture** | **4.19** | **0.5** | 0.02 | **13.7** | **0.8** | **5.58** | **1.1** | **14.9** |
| **Education** | **2.19** | **0.0** | 0.00 | **10.5** | **0.0** | **8.02** | **0.0** | **10.5** |
| **Restaurants and hotels** | **2.78** | **0.5** | 0.01 | **13.0** | | | **0.6** | **13.5** |
| **Miscellaneous goods and services** | **13.56** | **0.1** | 0.01 | **11.6** | **0.1** | **8.10** | **0.2** | **11.6** |
| Personal Care | 2.20 | 0.8 | 0.02 | 15.8 | 0.6 | 9.18 | 0.9 | 15.7 |
| Insurance | 7.71 | 0.0 | 0.00 | 7.5 | 0.0 | 6.97 | 0.0 | 7.5 |
| Financial Services | 1.27 | 0.0 | 0.00 | 19.6 | 0.0 | 11.92 | 0.0 | 19.6 |
| Other Services | 2.38 | 0.0 | 0.00 | 17.2 | 0.1 | 7.88 | 0.0 | 17.2 |

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