

Nedbank

Economic commentary

28 October 2009

CONSUMER INFLATION

Falling food inflation and a stronger rand drag inflation lower

- The latest figures is slightly below consensus but does not change the outlook noticeably
- Food inflation continued to moderate, while the price benefits of the stronger rand continued to be visible
- We still expect inflation to fall within the target range in the second quarter of 2010

Latest (September 2009)

Overall: 6,1% y-o-y, 0,4% m-o-m (6,4% y-o-y in August 2009)

Nedbank forecast: 6,3% y-o-y

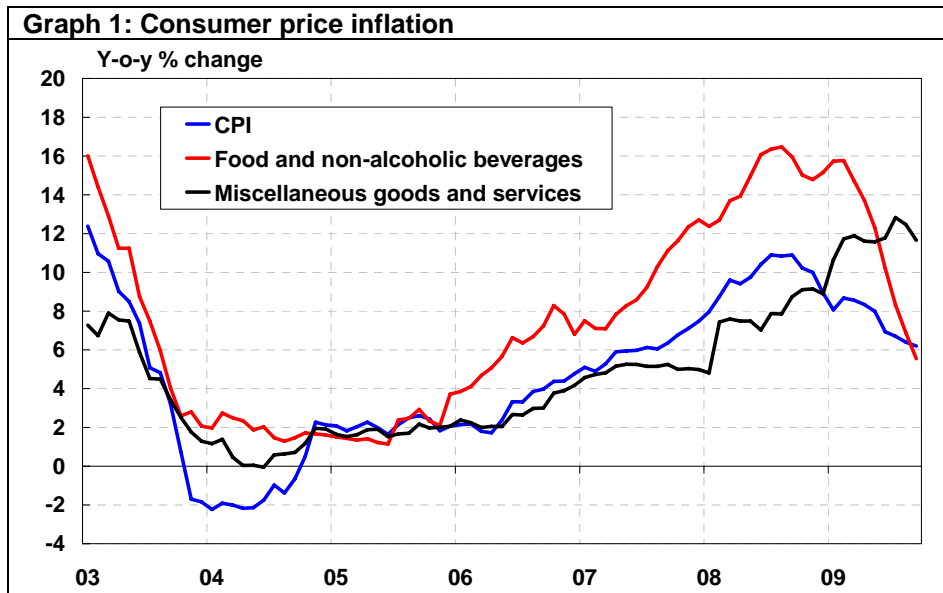
Market forecast: 6,2% y-o-y

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Comment

Headline inflation moderated further in September, coming in below market consensus and dropping to its lowest level since August 2007.

Food inflation continued to moderate as higher prices of vegetables (up 1,6% m-o-m), fruit (up 0,9% m-o-m) and other foods (up 0,3% m-o-m) were offset by price declines in most of the other food categories.

Weak demand conditions, coupled with the impact of the strong rand, helped to keep durable goods' price increases moderate. Prices of furnishings (down

0,8% m-o-m), appliances (down 0,4% m-o-m) and motor vehicles (down 0,3% m-o-m) eased during September.

Electricity prices were flat during the month after increasing sharply in the previous two months, but were up by 24,9% y-o-y, reflecting the impact of the 31,1% hike in electricity tariffs effective from 1 July.

The transport category rose by 0,7% m-o-m as the decline in vehicle prices was more than offset by higher petrol prices (the 36 cents/litre increase in September) and an increase in other running costs.

The items surveyed during September include actual rentals for housing (0,9% m-o-m and 5,4% y-o-y) and owner's equivalent rent (0,9% m-o-m and 4,7% y-o-y), which pushed the housing and utilities category up by 0,6% m-o-m and 7,6% y-o-y, while costs of private transportation operations increased by 3,8% m-o-m but were down by 11,8% y-o-y.

Outlook

The continued decline in headline inflation is encouraging and is in line with our forecasts that CPI will fall within the 3% to 6% target range in the second quarter of next year, as base effects, relatively weak demand and the rand's relative strength continue to drag it lower.

The proposed increases in electricity tariffs have once again emerged as an uncertainty regarding the outlook for inflation. Eskom's proposed 45% per annum hikes for the next three years would exert significant upward pressure on inflation and could well keep it above the target range depending on the extent to which inflation moderates in the early part of next year. In addition to the direct impact on inflation, second round effects are also likely, although the extent to which retailers can push through higher prices will be dependant on the health of household balance sheets. The Government's increased emphasis on weakening the rand to improve export competitiveness would also have negative implications for inflation, given the high import component of the basket.

The SARB still expects CPI to fall on a sustained basis to within the 3% to 6% target range in the second quarter of 2010 and remaining there until the end of 2011. The National Treasury's forecasts released in the Medium-Term Budget Policy Statement yesterday indicate that the government is less optimistic on the inflation trajectory, with inflation expected to return to the target band only in 2012.

Implication

Today's inflation data are encouraging, but we believe that they will not have a major influence on interest rates in the coming months. The market clearly now feels that the bottom of the cycle has been reached and is looking for a rise in rates in the first half of 2010 based on normal recovery patterns and the much-discussed Eskom tariff hikes. However, the former is unlikely and the latter has probably been overplayed. The tariff increases should be viewed as an exogenous shock that will have a depressing effect on consumer demand.

Given the severe dislocations in the global economy, local economic activity remains very vulnerable to further weakness and in our view there would be little downside to further relaxation sometime during the next few meetings.

	CPI							
	Weights	September 2009					August 2009	
		Base 2008	Month-on-month %	% contrib	Year-on-yea %	Average m-o-m past 3 yrs	Average y-o-y past 3 yrs	Month %
CPI for all urban areas	100	0.4	0.37	6.2	0.5	7.81	0.3	6.4
Food and non-alcoholic beverages	15.68	0.1	0.01	5.5	1.1	10.87	0.1	6.9
Food	14.27	0.1	0.01	4.9	1.1		0.1	6.2
Bread and cereals	3.08	-0.4	-0.01	-2.0	1.2	16.02	-0.5	0.4
Meat	4.59	-0.7	-0.03	4.2	0.2	7.14	-0.5	5.7
Fish	0.66	-0.4	0.00	7.2	1.0	9.48	0.2	10.6
Milk, eggs and cheese	1.79	0.3	0.00	7.5	1.8	14.49	0.6	9.8
Oils and fats	0.53	-0.1	0.00	-12.9	2.0	18.74	-1.2	-11.6
Fruit	0.47	0.9	0.00	12.9	-0.2	9.00	0.9	10.9
Vegetables	1.63	1.6	0.03	15.9	2.2	12.83	1.7	13.2
Sugar, sweets and deserts	0.77	0.4	0.00	9.5	1.0	9.84	0.4	10.3
Other	0.75	1.3	0.01	11.7	1.9	12.44	0.8	13.5
Non-alcoholic beverages	1.41	-0.1	0.00	11.7	1.0	10.05	0.9	13.9
Alcoholic beverages and tobacco	5.58	0.3	0.02	11.8	0.5	9.81	0.0	12.6
Alcoholic beverages	3.29	0.4	0.01	7.9	0.4	7.62	0.0	8.4
Tobacco	2.29	0.3	0.01	17.3	0.7	12.89	5.9	18.8
Clothing and footwear	4.11	0.2	0.01	5.0	-0.1	4.58	0.5	5.0
Clothing	2.9	0.3	0.01	5.3	-0.1	4.73	0.4	5.2
Footwear	1.21	0.2	0.00	4.3	0.0	4.18	0.5	4.4
Housing and utilities	22.56	0.6	0.14	7.6	0.4	10.21	0.4	7.8
Actual rentals for housing	3.49	0.9	0.03	5.3	1.0	7.39	0.0	5.6
Owners equivalent rent	12.21	0.9	0.12	0.0	0.7	0.00	0.0	0.0
Maintenance and repairs	1.68	0.2	0.00	7.3	0.4	9.63	0.7	8.3
Water and other services	3.31	0.0	0.00	0.0	0.0	0.00	0.5	0.0
Electricity and other fuels	1.87	0.0	0.00	24.9	7.5	21.05	2.5	25.9
Household contents and equipment	5.86	0.1	0.01	5.2	1.3	4.50	0.1	6.1
Furnishings, floor coverings and te	2.17	-0.8	-0.02	-0.9	-0.4	-1.37	0.2	0.1
Appliances, tableware and equipm	1.05	-0.4	0.00	9.5	0.2	5.83	0.2	11.2
Supplies and services	2.64	0.9	0.02	8.3	2.5	7.80	0.1	8.9
Domestic workers wages	1.99	1.2	0.02	6.4	3.0	6.90	0.0	6.4
Health	1.47	0.2	0.00	11.3	0.2	8.62	0.3	11.1
Transport	18.8	0.7	0.13	-1.3	-0.2	3.67	-0.2	-2.7
Purchase of vehicles	11.25	-0.3	-0.03	2.7	0.1	0.44	0.4	3.7
Private transport operation	4.82	3.6	0.18	-11.8	-1.0	8.42	-2.1	-19.9
Petrol	3.93	4.8	0.19	-17.0	-1.2	8.57	-2.7	-26.4
Other running costs	0.89	0.2	0.00	11.8	0.4	10.00	0.2	12.3
Public Transport	2.73	0.2	0.01	1.5	1.0	6.27	-0.2	4.2
Communication	3.22	-0.6	-0.02	0.9	-0.3	0.48	2.0	1.3
Recreation and culture	4.19	-0.1	0.00	11.3	0.0	5.56	0.3	11.7
Education	2.19	0.0	0.00	10.5	0.0	8.02	0.0	10.5
Restaurants and hotels	2.78	0.6	0.02	10.0			0.0	9.6
Miscellaneous goods and services	13.56	0.4	0.06	11.7	0.6	8.55	0.1	12.5
Personal Care	2.20	0.3	0.01	13.0	0.8	9.18	0.6	14.4
Insurance	7.71	0.7	0.06	11.2	0.3	8.10	0.0	10.5
Financial Services	1.27	0.0	0.00	7.8	2.6	10.92	0.0	16.1
Other Services	2.38	0.0	0.00	14.1	0.4	7.43	0.0	15.1

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