

29 September 2010

Economic Commentary

Consumer inflation

Consumer inflation at lowest level since February 2005

- Inflation slowed to 3,5% in August, slightly below market expectations and its lowest level since February 2005, helped by the strength of the rand, weak domestic demand and disinflationary pressures from abroad.
- The short-term outlook for inflation remains favourable, with some downside risk, particularly if the rand appreciates further.
- Although high wage demands do pose a concern, the greatest risk to the medium-term inflation outlook would come from a sudden sharp depreciation of the rand.
- The further moderation in inflation is good news, but it does not alter our view that rates are likely to remain unchanged at the next meeting.

Table 1 : Consumer inflation

	August Y-o-y%	August M-o-m%	July Y-o-y%	Nedbank Forecast Y- o-y%	Market Forecast Y-o-y%
Total	3,5	0,1	3,7	3,5	3,6

Source: StatsSA

Comment

Inflation eased to its lowest level since February 2005¹ in August, falling to 3,5% from 3,7% in July, due to declines in durable goods prices, particularly cars and household goods, as well as petrol.

Food inflation edged up slightly, increasing to 1,5% in August from 1,1% in July, mainly due to higher fruit and vegetable prices. Over the month, food prices rose by 0,5%, due to a 2,7% m-o-m and 1,1% m-o-m gain in fruit and vegetable prices respectively. Electricity prices also increased slightly over the month, rising by 1,5%, as Eskom's tariff increase was not fully reflected in the June number.

Prices of durable goods continued to decline, falling by 3,1% y-o-y (-0,3% m-o-m). In particular, vehicle prices fell by 0,1% m-o-m and 1,1% y-o-y. Prices of household furniture declined 4,9% y-o-y, following a 4% y-o-y decline in the previous month, while household appliances declined by 3,5% y-o-y, after falling by 3,2% y-o-y in July.

Petrol prices fell by 1,3% over the month, due to lower oil prices as well as a strong rand. On an annual basis, petrol prices continued to rise, increasing by 6,5%.

Group Economic Unit

Carmen Altenkirch

+27 11 295 9878

CarmenAI@nedbank.co.za

Dennis Dykes

+27 11 295 6435

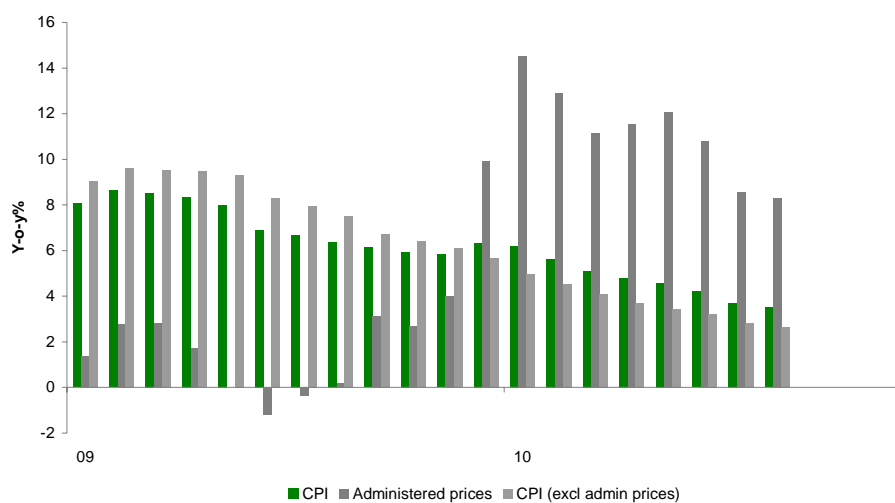
DennisD@nedbank.co.za

Corporate Place, 135 Rivonia Road,
Sandown, 2196, South Africa

<http://nedbankgroup.co.za>

Important disclosures can be found in the Disclosures Appendix.

¹ Based on CPIX

Chart 1 : Consumer inflation

Source: StatsSA

Outlook

Inflation has surprised on the downside over the past few months, helped by the strength of the rand, weak domestic demand and disinflationary pressures from abroad. The outlook for many of these drivers remains uncertain but inflation will probably start rising higher over the next few months, as some degree of opportunistic pricing re-emerges and food inflation picks up slightly. The two main risks to the relatively favourable medium-term inflation outlook come from above-inflation wage increases, which since not tied to gains in productivity, would put upward pressure on company costs and ultimately prices. The other risk comes from a possible depreciation of the rand. The government is currently looking at ways to weaken the currency in order to improve the country's export competitiveness. Although impossible at this stage to predict, there is a danger that efforts are too successful.

Implications

The improvement in the inflation outlook was one of the factors that contributed towards the MPC's decision to cut rates by 50 basis points on 9 September. Although the further moderation in inflation is good news, it does not alter our view that rates are likely to remain unchanged at the next meeting, as the short-term improvement in inflation has already been discounted by the Bank.

Although the Governor noted that the "scope for further downward movement is seen to be limited, but would be assessed on an ongoing basis", we still believe that given the uncertain nature of the recovery, a further rate cut remains a possibility, particularly in early 2011. The two key factors to watch over the coming months will be the likely inflation trajectory as well as any indication that growth is beginning to falter.

Table 2 : Inflation

	CPI							
	Weights	August 2010			July 2010			
		Month-on-month		Year-on-year	Average	Average	Month	Year
		%	%	%	m-o-m	y-o-y	%	%
	Base 2008	contribution		past 3 yrs		past 3 yrs		
CPI for all urban areas	100	0.1	0.1	3.5	0.3	6.91	0.6	3.7
Food and non-alcoholic beverages	15.68	0.5	0.1	1.7	0.7	8.36	0.3	1.4
Food	14.27	0.5	0.1	1.5	0.7		0.5	1.1
Bread and cereals	3.08	0.9	0.0	-2.1	1.1	10.50	-0.3	-3.4
Meat	4.59	0.2	0.0	0.6	-0.1	5.20	0.3	-0.1
Fish	0.66	-0.6	0.0	2.9	0.2	8.43	0.2	3.8
Milk, eggs and cheese	1.79	-0.1	0.0	0.9	0.9	9.07	-0.4	1.6
Oils and fats	0.53	0.2	0.0	-2.9	0.2	13.56	0.2	-4.2
Fruit	0.47	2.7	0.0	4.1	1.3	8.00	-1.4	2.2
Vegetables	1.63	1.1	0.0	8.4	1.9	10.10	3.8	9.1
Sugar, sweets and deserts	0.77	0.3	0.0	4.7	0.9	9.49	-0.4	4.9
Other	0.75	0.2	0.0	1.6	0.5	10.64	0.0	2.3
Non-alcoholic beverages	1.41	0.3	0.0	4.6	0.9	10.23	-0.2	5.1
Alcoholic beverages and tobacco	5.58	0.2	0.0	7.2	1.4	9.42	0.1	9.7
Alcoholic beverages	3.29	0.2	0.0	6.6	0.1	7.45	0.3	6.4
Tobacco	2.29	0.1	0.0	7.8	3.2	12.18	-0.1	14.1
Clothing and footwear	4.11	0.1	0.0	1.1	0.4	7.59	0.0	1.5
Clothing	2.9	0.1	0.0	1.1	0.4	7.65	0.0	1.4
Footwear	1.21	0.2	0.0	1.2	0.5	7.31	-0.1	1.5
Housing and utilities	22.56	0.3	0.1	6.3	0.4	8.21	3.0	6.4
Actual rentals for housing	3.49	0.0	0.0	4.5	0.0	5.88	0.0	4.5
Owners equivalent rent	12.21	0.0	0.0	3.9	0.0	2.89	0.0	3.9
Maintenance and repairs	1.68	0.3	0.0	3.2	2.0	7.66	0.3	3.7
Water and other services	3.31	0.5	0.0	0.0	0.4	0.00	8.8	0.0
Electricity and other fuels	1.87	1.5	0.0	18.3	2.5	23.51	16.3	19.4
Household contents and equipment	5.86	-0.2	0.0	-0.5	0.2	3.88	-0.1	-0.2
Furnishings, floor coverings and textiles	2.17	-0.7	0.0	-4.9	0.0	-2.13	0.0	-4.0
Appliances, tableware and equipment	1.05	-0.2	0.0	-3.5	0.7	4.08	-0.4	-3.2
Supplies and services	2.64	0.1	0.0	4.0	0.2	7.99	0.0	4.0
Domestic workers wages	1.99	0.0	0.0	5.8	0.0	7.58	0.0	5.8
Health	1.47	0.0	0.0	7.2	0.1	9.69	0.5	7.5
Transport	18.8	-0.2	0.0	1.1	-0.4	3.25	-0.4	1.1
Purchase of vehicles	11.25	-0.1	0.0	-1.1	0.0	0.53	-0.2	-0.6
Private transport operation	4.82	-0.9	0.0	6.1	-1.7	8.65	-1.2	4.9
Petrol	3.93	-1.3	-0.1	6.5	-2.2	9.41	-1.9	4.9
Other running costs	0.89	0.2	0.0	5.0	0.1	9.35	1.4	5.0
Public Transport	2.73	0.5	0.0	2.6	-0.2	6.85	0.0	2.0
Communication	3.22	0.2	0.0	-3.0	1.2	-0.48	-0.2	-1.3
Recreation and culture	4.19	0.6	0.0	-1.9	1.0	4.82	-0.5	-2.3
Education	2.19	0.0	0.0	9.2	0.0	8.92	0.0	9.2
Restaurants and hotels	2.78	-0.1	0.0	6.3			-3.9	6.4
Miscellaneous goods and services	13.56	0.0	0.0	5.7	0.2	8.66	0.3	5.8
Personal Care	2.20	-0.3	0.0	-0.2	0.7	7.30	-0.9	0.7
Insurance	7.71	0.0	0.0	7.5	0.0	8.99	-0.1	7.5
Financial Services	1.27	0.0	0.0	4.1	0.5	9.57	0.9	4.1
Other Services	2.38	0.0	0.0	6.0	0.0	8.71	1.9	6.0

Source: StatsSA

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