EFFICIENT GROUP

ECONOMIC COMMENTARY

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YOUR WEEKLY ECONOMIC UPDATE

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INFLATION AND THE UNLAWFULNESS OF CADRE DEPLOYMENT

Statistics South Africa (Stats SA) reported last week that, during the month of May, household prices increased by roughly 6.5% year-on-year. Higher inflation was partly driven by a low base effect, but more so by higher fuel prices, which have been increasing owing to the ongoing war in Ukraine as well as the sanctions imposed by the West. Fuel prices in May of this year are 32.5% higher than they were a year ago. Electricity prices are up 14.4%, public transport is up 12.5%, and different foodstuffs are up by roughly 8%. Core inflation, a reading that excludes the more volatile items, such as energy, fuel, and foodstuffs, from the (headline) inflation reading, only increased by 4.5% on a year-on-year basis. This reading helps to show that inflation in South Africa (SA) is a supply and not a demand issue. For this reason, interest rate decisions made by the South African Reserve Bank (SARB) cannot do much to reign inflation in, as higher interest rates cannot do anything to bring down fuel prices, electricity prices, or food prices. Also, if you strip out these volatile prices, it becomes quite clear that we do not have an inflation problem in SA, even though headline inflation breached the SARB's target of between 4% and 6%. The United States (US), like many other developed countries, has an inflation problem. There, demand has been stimulated by more than a decade of easy monetary policy, which has now resulted in prices going up to levels four times higher than their long-term average rate: 8.6% relative to their long-term average rate of around 2%. The SARB is simply increasing interest rates because they must. If they do not, our markets will not be competitive enough to attract short-term capital, which will put too much strain on our local currency.

Many still believe that the SARB will increase interest rates by another 1% to 1.5% in 2022, and then by another 1% to 1.5% in 2023, or maybe even more. But the SARB might not have to increase interest rates for too long. Amidst fears of a potential recession, international investors last week started to price in a potential slowdown in the tempo of interest rate increases in the US. In his two-day testimony to Congress, US Federal Reserve (Fed) Chairman, Jerome Powell, explained that a recession was "certainly possible". Global concerns about a slowdown in demand also helped to bring down oil prices to less than $110 a barrel. We expect that this trend will continue and that we might even see oil back to $95 a barrel by the end of the year. This, together with our expectation that the rand will strengthen back to levels between R15.00 and R15.50 against the US dollar, would mean that fuel prices should recover considerably towards the end of the year.

In other welcome news, Chief Justice Raymond Zondo found that the cadre deployment policies implemented by the ruling African National Congress (ANC) are both unlawful and unconstitutional. We have shared a similar view for a long time. High-ranking positions in all spheres of government should be filled based on 'best for the job' and 'best for the country', not based on 'best for the party' or 'best for my pocket'. Zondo's report explained that cadre deployment could be abused and lead to corruption and state capture, something that we are all too aware of. By President Cyril Ramaphosa's own admission, the Deployment Committee previously appointed unfit or corrupt individuals to positions of power. Ramaphosa's statement undermines evidence that he previously gave regarding the general integrity of the Deployment Committee and its actions. The fact that the committee did not prevent the appointment of unfit or corrupt individuals is an indictment of either its integrity, its ability, or both.