

# Rand strength will help tame inflation

**S**USTAINED rand strength may be bad news for

exporters and miners, but it will bring relief on the inflation front, helping to ease price pressures in the next few months.

So far this year, inflation has stayed high, forcing the Reserve Bank to unexpectedly stop cutting interest rates at its policy meeting last month. But many analysts say consumer prices will now start to beat a hasty retreat, subdued by food prices and rand gains, which help curb import costs.

"There are reasons to believe that the sticky pace of decline in inflation is unlikely to continue," said Coronation Fund Managers fixed-income analyst Mark le Roux.

He cited sharp falls in grain prices — down more than 30% in the past year — and lower producer prices at mines, factories and

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farms. The third factor is the rand, which rose more than 23% against the dollar and 21% against the euro so far this year.

Inflation measured by the annual rise in SA's consumer price index has breached its official 3%-6% target range for 26 months in a row, peaking at 13,7% last year.

In May, it subsided to 8% from 8,4% in April — just a touch below its rise of 8,1% in January.

Part of the reason for the stickiness of inflation at these levels is revisions this year to the consumer price basket, which now includes more service costs.

Another reason is the rand's depreciation when the global crisis struck last year. It hit a 6½-year low at R11,87/\$ on October 22. The unit traded at R7,71/\$ late yesterday, not far off a 10½-month peak at

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R7,67/\$ scaled a couple of weeks ago. This trend alarmed many as it erodes both the competitiveness of local exports and the rand-denominated revenues of SA's miners.

But it should also help bring inflation back into its target range early next year, and keep it there, as the Bank forecast last

month. It may also persuade the Bank to trim interest rates at its policy meeting in the middle of next month, after 4,5 percentage points in cuts since December.

"Part of the reason why we've been surprised by the stickiness of inflation is by the delayed impact of last year's rand depreciation," said Barnard Jacobs Mellet economist Elna Moolman. "I now expect its appreci-

ation to put downward pressure on inflation next year."

It takes shifts in the rand's exchange rate nine to 10 months to feed into consumer prices, with the response much faster on the way up than down.

Moolman thinks interest rates have hit bottom, although further rate cuts cannot be ruled out if inflation proves benign.

Nedbank economist Carmen

Altenkirch thinks there is a good chance of the Bank cutting rates by another percentage point.

"The last half of the year should see inflation easing quite sharply to slightly above 6% ... the rand's sustained recovery should be a big part of this story," she said. Data next week may show that CPI slowed to 7,2% last month.

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