Summary of macroeconomic research views:

- **Inflation:** Headline CPI remained unchanged at 2.8% y/y in May. While goods inflation increased in the month, fuel fell further into deflationary territory, with the latter likely to have bottomed out. While domestic inflation is likely to start rising in subsequent months (in part due to a 12.7% average electricity price hike, which takes effect on 1 July), the rebound should be gradual, barring a significant oil price shock amidst ongoing geopolitical tensions.

- **Repo rate:** The SARB resumed its monetary easing cycle in May, cutting the repo rate by 25 basis points to 7.25%. The SARB also revised its inflation forecasts lower, now projecting 3.2% for 2025 and 4.2%-4.4% through 2027, citing a stronger rand, lower oil prices, and the scrapping of VAT hikes. However, growth expectations were downgraded, with 2025 GDP now seen at just 1.2%.

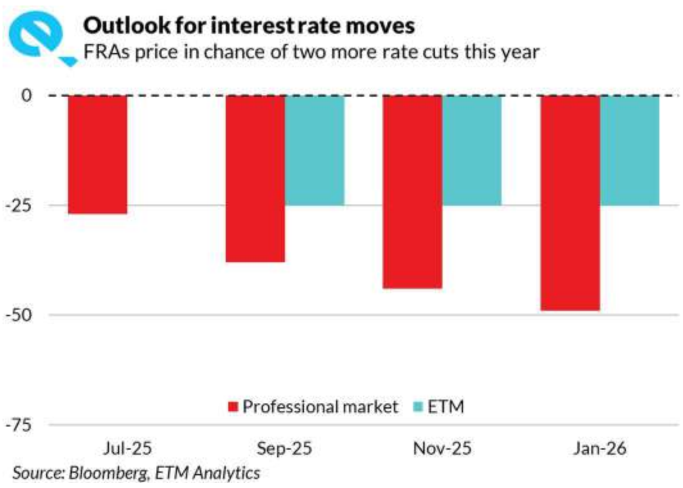
- **Government Finances:** The budget deficit contracted seasonally in May, to -R10.1bn from -R64.6bn in April. While it is early in the current fiscal year, from a year-to-date perspective, the -R74.7bn budget deficit marks a slight improvement from -R90.8bn in the corresponding period during the 2024/25 fiscal year. South Africa's public debt is expected to rise during the 2025/26 fiscal year, with weak growth expectations weighing on the revenue outlook, and meaningful expenditure cuts unlikely to be made.

- **GDP Growth:** SA's GDP grew by just 0.1% q/q in Q1, slowing from 0.4% in Q4. Y/y growth held steady at 0.8%. Without a second consecutive quarter of robust agricultural growth (+15.8%), overall GDP would have contracted. Particularly concerning is the significant decline across the productive sectors as mining output and manufacturing shrank by 4.1% and 2.0%, respectively.

- **Currency:** The ZAR closed June stronger against the USD, in line with a broad-based improvement in emerging market currencies. A fragile ceasefire between Iran and Israel led to improved risk sentiment. Domestically, GNU ructions towards the end of the month led to some temporary ZAR weakness.

- **Offshore conditions:** In the middle of the month, risk appetite soured sharply when the US bombed Iran. Oil prices rose sharply, and investors shifted to safe-haven assets such as the greenback. However, with a fragile ceasefire in place, the market has settled. USD weakness emerged towards the end of the month due to fiscal concerns about the debt impact of President Trump's $3.4 trillion tax and spending bill, which has passed through Congress. In the coming weeks, the market will need to weigh the stimulatory effects of this bill against its fiscal impact.

Interest rate indicators:

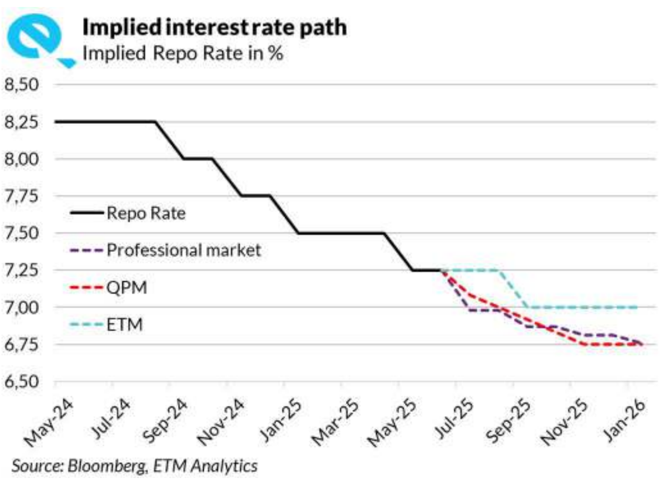


The SARB resumed its monetary policy easing cycle in May, cutting the Repo Rate by 25bps to 7.25%. The vote among MPC members was split 5-1, with the dissenting voice favouring a 50bp rate cut.

The case for further interest rate cuts remains, with the ZAR appreciating notably in recent weeks and inflation remaining below the lower end of the 3%-6% target band.

Global financial market conditions have also settled following the volatility seen during the peak of the Israel-Iran conflict. The VIX Index is trading well below the 20-mark once again to signal that risk-on conditions remain entrenched, while global oil prices have also receded with Brent below $70 per barrel once again.

Of course, one needs to factor in the high possibility that the SARB's inflation mandate will be adjusted in the coming months. As it stands, the revised target will likely be set at a fixed 3%. Achieving this target will require higher interest rates in the near term to keep inflation pressures contained.



However, until the change is formalised, the SARB will act under its current mandate, which keeps the door open to further rate reductions.

In the markets, FRA's are currently pricing in a rate cut at this month's MPC meeting, with a second rate cut largely expected by the January 2026 meeting.

This aligns with the path set forward by the SARB's own QPM model. ETM's expectations, however, are more conservative as we expect a 25bp rate cut in September.

By then, many uncertainties regarding the global backdrop will be clearer. If the inflation target is adjusted before the end of the year, there will need to be a reset of expectations, with interest rates then likely to be kept on hold until inflation expectations settle closer toward the new 3% target level.

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