NATIONAL ASSEMBLY

QUESTION FOR WRITTEN REPLY

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DR P J RABIE (DA) TO ASK THE MINISTER OF FINANCE:

Whether the Government will abandon the official rate of inflation targeting; if not, what is the position in this regard; if so, what are the relevant details? **NW183E**

REPLY:

1. Inflation targeting will remain the framework for monetary policy in South Africa. As with all areas of policy we encourage an active debate on the merits and shortcomings of current policies in the interests of achieving higher sustainable rates of growth and employment for South Africa.

2. Permanently higher inflation carries a range of serious economic costs. It drives up interest rates, reduces competitiveness, and lowers actual and potential economic growth. It also reduces the living standards of groups with less ability to protect their incomes from rising prices, including the poor, workers, and those living off of fixed incomes (pensions).

3. Inflation targeting provides a clear nominal anchor for monetary policy and requires the Reserve Bank to be transparent about its goals and actions. These issues are extremely important for policy credibility and for managing inflation expectations effectively. If inflation is rising and inflation expectations are not anchored, then the cost of lowering inflation becomes much higher in terms of lost investment, lost exports and lost employment.

4. Inflation targeting allows the Reserve Bank's Monetary Policy Committee (MPC) to consider a range of factors that might impact on future inflation outcomes, including international economic developments, the size of the

output gap, domestic imbalances, inflation expectations, growth in unit labour costs, and movements in exchange rates and commodity prices. The effect of all of these factors on *future* inflation is what drives the monetary policy stance.

5. Since inflation targeting was adopted in 2000, both the level and volatility of inflation has declined, while GDP growth has also been stronger and less volatile than under previous monetary policy regimes. In recent years, external shocks to food and oil prices have driven South Africa's inflation rate above the 3-6% target range. Guided by the impact of current economic developments on future inflation prospects, the Reserve Bank remains focused on gradually reducing inflation back within the target range.