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YOUR WEEKLY ECONOMIC UPDATE

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ECONOMIC COMMENTARY - DR. FRANCOIS STOFBERG

Has monetary policy become too blunt? Lessons for South Africa

Central banks have long warned that setting interest rates is a "blunt tool" for steering economies and inflation. However, this tool is becoming more blunt. As economies evolve structurally, conventional monetary policy is struggling to shape behaviour as it once did. As a result, South Africa (SA) must adapt its expectations and instruments.

In advanced economies, the problem is clear: Consumers and businesses have shifted from floating-rate to fixed-rate debt. This means that, when central banks adjust policy rates, the impact on borrowing costs takes longer to be felt. The result is a weaker, slower transmission. At the same time, the global economy has shifted from goods to services. Manufacturing and construction (historically sensitive to interest rates) now represent a smaller share of activity. Services that dominate today's economies are more labour-intensive and less dependent on credit. And many new investments, particularly in artificial intelligence and digital infrastructure, are self-financed from cash flow, not debt. Monetary tightening, therefore, affects a smaller slice of the economy. The consequence is that central banks must move rates further and wait longer to achieve the same result. The mechanism is not broken but it has become much less predictable.

Implications for SA

The South African Reserve Bank (SARB) also relies heavily on the repo rate to control inflation and to support the rand. But its transmission mechanism has weakened. Studies show that commercial lending and deposit rates adjust slowly to policy moves; a form of "stickiness" that blunts monetary impact.

Recent research conducted by the SARB reveals that how banks react to policy changes plays a crucial role in how interest-rate decisions affect the wider economy. When the SARB raises or cuts rates, the response depends on how quickly and confidently banks adjust their own lending and deposit rates, or expand credit to households and businesses. In practice, when banks hold back on new lending or keep loan rates high, even large repo-rate changes take longer to filter through. This weakens the transmission mechanism of monetary policy, meaning that rate moves have less impact and more uneven effects across sectors. This creates several risks.

The first risk is that rate changes now have slower and smaller effects, forcing policymakers to act more forcefully or to hold rates steady for longer. Second, the impact is concentrated in credit-dependent households and small businesses, while larger firms remain insulated. Third, weaker transmission raises the risk of policy overshoot, either tightening too much or stimulating too little. Finally, it increases vulnerability to external shocks, such as commodity swings, fiscal slippage, or exchange-rate volatility.

A broader policy playbook

If the interest-rate lever is losing power, SA must rely on a wider toolkit:

+ **Strengthen structural and fiscal levers:** Fiscal and supply-side policies, from infrastructure investment and tax incentives to energy and logistics reform, can stimulate growth directly where monetary policy cannot.
+ **Deepen financial markets:** Improving competition among banks, reducing lending rigidity, and expanding access to alternative credit sources can help speed up monetary transmission.
+ **Use additional macro tools:** Beyond the repo rate, macroprudential instruments, forward guidance, and selective credit measures can target specific sectors more precisely.
+ **Anchor expectations through communication:** With slower transmission, the credibility of the SARB's messaging becomes critical. When inflation expectations are well-anchored, even small policy moves can have larger psychological and financial effects.

A new era of monetary management

The bluntness of monetary policy is not a crisis but it does demand humility. Rate changes alone cannot fix structural weaknesses, nor can they generate sustainable growth. For SA, where unemployment is high and confidence fragile, relying solely on interest-rate adjustments risks dulling both the economy and public trust. The challenge for the SARB and government is to combine disciplined monetary policy with more agile fiscal and structural reforms. In a world where the interest-rate hammer strikes with less force, it is time to pick up sharper tools and craft a more precise form of economic management.

Kind regards
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