



## BANK OF MAURITIUS

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### **Minutes of the 39<sup>th</sup> Monetary Policy Committee Meeting of 17 February 2016**

The 39<sup>th</sup> meeting of the Monetary Policy Committee (MPC) was held on Wednesday 17 February 2016 at 10:30 hours at the Bank of Mauritius and was chaired by Mr Rameswurlall Basant Roi G.C.S.K., Governor.

Members present: Mr Yandraduth Googoolye - First Deputy Governor; Mr Mahendra Vikramdass Punchoo - Second Deputy Governor; Mr Pierre Dinan, Mr Mohammad Mushtaq Namdarkhan, Mr Nishan Degnarain, Dr Streevarsen Narrainen and Mr Guy Wong So - External Members.

#### **Summary of Staff Report on Economic and Financial Developments**

The Bank's staff reported on economic and financial developments since the 38<sup>th</sup> MPC meeting held on 9 November 2015.

#### ***International economic environment***

1. **The MPC reviewed the latest 2016 global economic projections and noted that global growth remained modest, uneven and faced considerable headwinds.** The IMF's January 2016 World Economic Outlook (WEO) Update downgraded global growth forecast to 3.4 per cent for 2016, 0.2 percentage point lower compared to the projection made in October 2015, mainly on account of a weaker pick-up in emerging economies. Global growth was expected to edge up to 3.6 per cent in 2017. Downside risks to the global outlook would include the rebalancing of economic activity in China, lower commodity prices and interest rate normalisation in the United States.
2. **Average global inflation has remained benign amid sustained slack in the world economy, subdued demand, declining commodity prices and tepid wage growth.** Inflation rates in advanced economies have continued to undershoot inflation targets. Inflation outturns were rather diverse in emerging market economies, reflecting on the one hand, the effects of muted domestic demand and lower commodity prices and on the other, the substantial depreciation of currencies. In the near term, average global inflation was expected to remain subdued.
3. **Global commodity prices declined further on the back of persistent excess supply and relatively weak global demand and would face the same outlook in 2016.** Oil prices have plummeted amid expectations of higher production by members of the Organisation of the Petroleum Exporting Countries and the sustained global oil glut. The price per barrel of West Texas Intermediate crude oil fell to a low of US\$28.40 on 20 January 2016. The prices of other commodities, especially metals, have slumped as well. The Food and Agriculture Organisation (FAO) food price index dropped to 154.1 in December 2015, from 158.2 in October 2015.

4. **Global financial market volatility rose markedly against a backdrop of slowing activity in large emerging market economies, diverging monetary policies of major central banks, persistent declines in commodity prices, and vulnerable liquidity conditions.** Most major stock markets continued to sustain losses and, between 9 November 2015 and 10 February 2016, the MSCI World and MSCI Emerging Markets shed, on average, around 12 per cent and 13 per cent, respectively.

### *Domestic economic developments*

5. **Economic growth continued at a moderate and weaker-than-expected pace in 2015.** Statistics Mauritius (SM) downgraded its 2015 GDP growth estimate to 3.4 per cent, mainly due to lower sugar output, a persistent contraction in 'Construction' and weaker-than-expected performance of 'Textiles', partly offset by stronger activity in 'Accommodation and food service activities'. In terms of domestic demand, growth in 2015 continued to be supported by household consumption while investment remained lacklustre.
6. **In 2016, the economy is projected to register a higher growth compared to 2015.** SM expects GDP growth to accelerate to 3.9 per cent in 2016. A pick-up in activity in key export markets together with ongoing domestic efforts to diversify traditional export markets are expected to support external demand. On the domestic front, gross domestic fixed capital formation is expected to grow in 2016 after four consecutive years of decline due to stronger support from both private and public investment. Acceleration in growth is projected for several key sectors and the 'Accommodation and food service activities' sector is estimated to grow by 4.5 per cent in 2016, based on expected tourist arrivals of 1.2 million.
7. **Inflation has remained at low levels since the November 2015 MPC meeting.** Headline inflation dipped to its lowest value since June 1988 at 1.2 per cent in September 2015 and remained contained in the range of 1.2-1.3 per cent till January 2016. Year-on-year inflation subsided to 1.3 per cent in December 2015 and further to 0.4 per cent in January 2016. The various derived inflation indicators, including the core inflation measures, also remained at low levels. Inflation expectations (headline) assessed in November 2015 remained skewed to the downside.
8. **Input cost pressures remained at moderate levels, notwithstanding the rise in the wage rate index.** Domestically, input cost pressures remained contained, while the import price index dropped during 2015Q3. However, the wage rate index (WRI) increased by 0.6 per cent q-o-q to 128.4 in 2015Q3 and on a y-o-y basis by 5.2 per cent. In real terms, the WRI is estimated to have increased by 4.0 per cent in 2015Q3 relative to 2014Q3.
9. **Labour market conditions remained more or less unchanged since the last MPC meeting, with a slight uptick estimated in the unemployment rate for 2015.** Quarterly estimates have pointed to a lower unemployment rate at 7.4 per cent in 2015Q3 compared to 7.8 per cent in 2015Q2 and 7.6 per cent in 2014Q3.

10. **The current account deficit was lower in 2015Q3 compared to 2014Q3, reflecting a lower merchandise trade deficit and comfortable surpluses on the services and income accounts.** The deficit on the current account dropped to 5.3 per cent of GDP in 2015Q3, from 8.7 per cent of GDP in 2014Q3. Bank staff have projected a current account deficit of 5.0 per cent for both 2015 and FY15-16. The end-December 2015 level of gross official international reserves of the country represented 7.6 months of imports, up from 6.2 months as at end-December 2014.
11. **Excess liquidity in the domestic money market generally trended upwards since the last MPC meeting due to seasonal considerations and net redemption of Government securities, but the Bank implemented various measures to contain excess liquidity within tolerable levels.** The average cash reserve ratio maintained by banks declined from 10.77 per cent for the period ended 12 November 2015 to 10.52 per cent for the period ended 7 January 2016 before rising to 11.24 per cent for the period ended 4 February 2016. Outstanding BoM securities as on 26 January 2016 stood at Rs30.8 billion, while the outstanding amount of deposits placed by banks on account of sterilised foreign exchange intervention amounted to Rs7.9 billion.
12. **Interbank money market rates remained at low levels, while rising banks' excess reserves exerted downward pressures on money market yields for various maturities.** The weighted average overnight interbank interest rate edged up to 1.24 per cent in December 2015, from 1.09 per cent in October 2015. The weighted yields for the 91-Day, 182-Day and 364-Day GMTBs stood at 3.39 per cent, 3.60 per cent and 4.05 per cent, respectively, as at end-December 2015 compared to 2.23 per cent, 2.39 per cent and 3.20 per cent as at end-October 2015. However, with the rise in excess liquidity, the weighted yields on 91-Day, 182-Day and 364-Day GMTBs went down to 2.38 per cent, 2.62 per cent and 2.91 per cent, respectively, at the end of January 2016. Yields on medium- and long-term Government securities broadly followed the same path.
13. **Since the last MPC meeting, movements in the rupee exchange rate reflected developments in major currencies as well as in domestic demand and supply conditions.** In nominal effective terms, the rupee appreciated by 0.8 per cent between November 2015 and January 2016. However, between September 2015 and December 2015, the real effective exchange rate of the rupee, weighed by trading partner countries, depreciated by 1.3 per cent.
14. **Broad money liabilities (BML) as well as bank credit to the private sector annual growth rates slowed somewhat in December 2015.** BML annual growth rate declined from 11.7 per cent in September 2015 to 10.2 per cent in December 2015, while claims on other sectors dropped from 9.3 per cent to 8.1 per cent. The annual growth rate of banks' credit to the private sector (excluding credit to GBC entities) went down from 5.2 per cent to 4.2 per cent, with the annual growth rate in household credit falling from 5.2 per cent to 5.0 per cent and mortgage credit going down from 11.1 per cent to 9.4 per cent.
15. **The domestic banking sector remained sound and resilient.** The capital adequacy ratio maintained by the banking sector improved further from 17.2 per cent as at end-June 2015 to 17.6 per cent as at end-September 2015. The ratio of impaired credit to total credit worsened from 4.9 per cent as at end-June 2015 to 6.3 per cent as at end-September 2015, but the coverage ratio (ratio of specific provision to impaired credit) improved from 40.0 per cent as at end-June 2015 to 49.2 per cent at the end of September 2015.

## **Staff economic outlook**

16. **Bank staff have estimated that headline inflation would be contained at relatively low levels in the near term, conditional on both external and domestic assumptions.** Headline inflation has been projected at around 2.3 per cent for 2016. Subdued inflation in the economy reflect, among others, base effects arising from the previous cuts in energy prices, muted imported inflationary pressures and slackness in domestic demand.
17. **Bank staff have forecast a real GDP growth of 3.8 per cent for 2016.** The implementation of announced public infrastructure projects and the anticipated boost in private sector investment are projected to contribute to the pick-up in the domestic economy.

## **Monetary Policy Decision**

18. **Members discussed the recent international and domestic developments and projections.** The global economic environment was increasingly being subject to huge uncertainties and risks. China's economic growth rebalancing, diverging monetary policies across regions, including the adoption of negative interest rate policies, and geopolitical risks could heighten market volatility, which could harm global growth going forward. Commodity prices were projected to remain subdued in the near term and global inflationary pressures would remain benign. Whilst there have been signs of improved growth in some advanced economies, downside risks to the global growth outlook would persist.
19. **MPC members observed that the monetary policy stance was accommodative to growth, with inflation contained below 3 per cent.** They noted the decline in externally-generated inflationary pressures as well as in various inflation indicators. Inflation risks stemming from domestic demand remained relatively muted. They viewed that the inflation outlook was relatively moderate and that, at the current juncture, inflation did not pose any serious risk. In the absence of any major shock, they viewed that headline inflation would remain contained at relatively low levels.
20. **Members reviewed the growth performance of the economy in 2015, which was propped up by key export sectors.** The economy was still operating below its potential level. The sharper-than-projected contraction in private investment in 2015 underscored the presence of structural bottlenecks that have been a major drag on growth prospects. The economy would perform better in 2016 with gross domestic fixed capital formation expected to grow after four consecutive years of decline due to stronger support from both private and public investment. Domestic productivity levels and trends and wage developments in the economy were, however, diverging. Members commented on the banking sector's stability and soundness and reviewed latest trends in non-performing loans.
21. **Members took note of the evolution of excess reserves in the banking system, the Bank's sterilised interventions and active liquidity management since the last MPC meeting.** They took note of the ongoing work with regard to the new monetary policy operational framework. They also stressed on the need to further reduce the level of excess liquidity in order to enhance

the effectiveness of monetary policy. The MPC envisages the implementation of the new monetary policy framework at its next meeting.

22. **The Committee weighed the risks to the growth and inflation outlook and discussed alternative interest rate scenarios.** Views diverged about the monetary policy stance to be adopted. Two MPC members viewed that monetary policy could be further eased given the subdued global economic outlook and the need to lessen borrowing costs, especially for the SME sector. A majority of members judged that the monetary policy stance was broadly appropriate and that the reduction in the Key Repo Rate effected last November had yet to work through the economy.

#### ***Voting pattern***

23. **At the conclusion of the discussion, the Committee voted with a majority of 6-2 to keep the Key Repo Rate unchanged at 4.40 per cent per annum.** The two dissenting members voted to cut the Key Repo Rate by 25 basis points.
24. **The MPC would continue to monitor economic and financial developments.** The MPC would also stand ready to meet in between its regular meetings, if the need would arise.
25. **The next MPC meeting is scheduled on Wednesday 22 June 2016.**
26. **Voting for the MPC action:** Mr Rameswurlall Basant Roi G.C.S.K., Mr Yandraduth Googoolye, Mr Mahendra Vikramdass Punchoo; Mr Pierre Dinan, Mr Mohammad Mushtaq Namdarkhan and Mr Guy Wong So.
27. **Voting against the MPC action:** Mr Nishan Degnarain and Dr Streevarsen Narrainen.

## Editor's Note

According to the Bank of Mauritius Act 2004, the primary object of the Bank shall be to maintain price stability and to promote orderly and balanced economic development. The Act gives the Monetary Policy Committee (MPC) responsibility to formulate and determine the monetary policy to be conducted by the Bank. The MPC meets on a regular quarterly basis.

When the MPC met on 17 February 2016, the last available data on national accounts, employment and external trade were for 2015Q3. The last data available on CPI and inflation were for January 2016.

## Abbreviations and Definitions

**Headline inflation** is measured by the change in the average Consumer Price Index (CPI) over a twelve-month period compared with the corresponding previous twelve-month period.

**Y-o-y inflation** is measured by the change in the CPI for a given month compared with the corresponding month of the preceding year.

**CORE1 inflation** excludes food, beverages and tobacco and mortgage interest on housing loan from the CPI basket. Both headline and y-o-y CORE1 inflation measures are available.

**CORE2 inflation** excludes food, beverages and tobacco, mortgage interest, energy prices and administered prices from the CPI basket. Both headline and y-o-y CORE2 inflation measures are available.

**Y-o-y** refers to year-on-year changes.

**Q-o-q** refers to quarter-on-quarter changes.

**GMTBs** refer to Government of Mauritius Treasury Bills.