MONETARY POLICY AND FINANCIAL STABILITY REPORT

May 2017

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MAY 2017

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Monetary Policy and Financial Stability Report May 2017

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Foreword

The primary object of the Bank of Mauritius is to maintain price stability and to promote orderly and balanced economic development. Price stability provides a strong foundation for sustained and long-term economic development by enhancing the efficiency of the allocation of funds. The Bank conducts monetary policy and manages the exchange rate of the rupee, having regard to the best interests of the economic development of Mauritius. The Monetary Policy Committee of the Bank determines the appropriate monetary policy stance through changes in the Key Repo Rate. Concurrently, the Bank intervenes regularly on the domestic interbank foreign exchange market with a view to removing excessive volatility in the rupee exchange rate, and ensuring that the local currency reflects domestic economic fundamentals.

Another key object of the Bank is to ensure the stability and soundness of the financial system of Mauritius. A stable, safe and sound financial system is conducive to the proper intermediation of funds in the economy, thereby promoting financial development, and supports the domestic growth agenda. The Bank constantly monitors factors that may impact on the financial soundness of institutions falling under its purview.

The Report presents an evaluation of price and financial stability, recent and expected inflation trends as well as the risks to price and financial stability. It aims to enhance the public's understanding of the policies applied to achieve the mandates of the Bank. This Report uses information and financial data available up to end-April 2017, unless otherwise stated.

1. Executive Summary

Global economic recovery is set to gain momentum during 2017, mainly on the premise of an improved performance of advanced economies while macroeconomic fundamentals are expected to gradually revert to normal conditions, leading to a rise in real activity in several emerging market and developing economies. The rebound in commodity prices during 2016 provided relief to a majority of commodity exporter countries, while indications of rising global demand boosted both manufacturing and trade activities in advanced and emerging market economies. Nonetheless, downside risks to a sustained global recovery remain present, namely, inward-looking and protectionist policies, a tightening of global financial conditions in the case of faster-than-expected interest rate hikes and US dollar appreciation, a rollback of financial regulation, and rising geopolitical tensions in different parts of the world. In its April 2017 World Economic Outlook, the International Monetary Fund projects global growth to accelerate to 3.5 per cent in 2017 and further to 3.6 per cent in 2018.

The domestic economy recovered during 2016H2, underpinned by buoyant activity in key service sectors, enhanced performance of the manufacturing sector, and a rebound in the construction sector. Output growth also remained supported by strong domestic demand, favourable monetary conditions and improving business sentiment. Measures announced in the 2017-18 Budget Speech, including major infrastructure projects are expected to raise both public and private investment, and lend support to stronger domestic growth in 2017. Statistics Mauritius has projected real GDP to grow by 3.8 per cent in 2017. The Bank of Mauritius projects real GDP growth for 2017 to be in the range of 3.8-4.0 per cent. Notwithstanding domestic demand and supply conditions, the rupee remained somewhat stable on a nominal effective exchange rate basis. Excluding government securities issued for liquidity management purposes, public sector debt as a ratio to GDP increased from 55.4 per cent as at end-December 2016 to 55.6 per cent as at end-March 2017. The current account deficit is estimated to have narrowed to 4.3 per cent for the year 2016, reflecting a better performance of the services sector and a lower deficit in the goods account.

The Bank's monetary policy stance has remained broadly accommodative amid subdued inflationary pressures and anchored inflation expectations. A combination of mild domestic food price increases, relatively weak external demand conditions, and broadly stable nominal exchange rate have led to fairly low inflationary impulses during 2016H2. Headline inflation hovered within a narrow range of just under 1.0 per cent until November 2016, before increasing to 1.5 per cent in April 2017. In view of these developments, the Monetary Policy Committee kept the Key Repo Rate unchanged at 4.0 per cent at its meetings held in November 2016, February 2017 and May 2017.

Indebtedness of households declined during 2016H2 as a result of a slowdown in credit extended by banks to households, coupled with relatively higher increase in household disposable income. Likewise, debt servicing cost being borne by households has declined, having been favoured by the cut effected in July 2016 to the Key Repo Rate that trickled into lower prime lending rates charged by banks and other financial intermediaries. Notwithstanding the decline, household debt-to-disposable income ratio continues to remain elevated and requires monitoring.

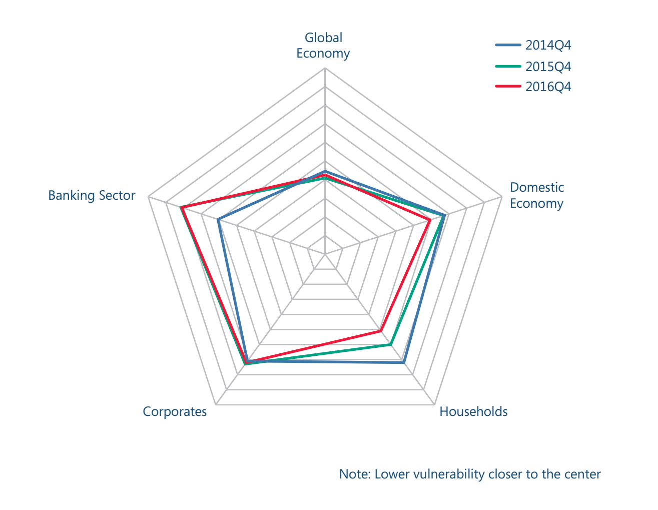
The evolution of corporate indebtedness remains paramount in the assessment of credit risk in the banking sector. Ongoing deleveraging among some large corporates in Mauritius has contributed to the slowdown in growth of private sector credit during 2016H2. Notwithstanding the fact that several major entities still operate with relatively high leverage ratios, it is expected that an improvement in domestic economic activity should provide a boost to corporate financials in Mauritius over the near-to-medium term. Going forward, the outlook for corporate performance remains closely related to both domestic and international economic prospects. With a view to preventing excessive leveraging by corporates, defaults in instalments and problems loans have to be closely monitored at bankwise level for early detection of vulnerabilities and potential systemic risks in the financial system.

1. Executive Summary

Over the year ended December 2016, the banking sector remained adequately capitalised and supported by a gradual improvement of profitability ratios that was attributable mainly to the performance of domestic-owned banks. Growth in total banking assets remained moderate, with accumulation of domestic assets by local banks largely offsetting the contraction in foreign assets held by branches and subsidiaries of foreign-owned banks. However, financial soundness indicators point to lingering weaknesses associated with high non-performing loans ratios pertaining to both domestic and cross-border credit, a decline in the coverage ratios, and bank claims on the private sector being contingent to credit concentration risk. Non-bank deposit-taking institutions have also reported average rates of growth in total assets although the strengthening of the aggregate capital adequacy ratio points to increased resilience of the non-bank deposit-taking sector to withstand balance sheet shocks.

During 2016H2, the payment and clearing systems regulated and supervised by the Bank remained resilient, and payments were processed and settlement effected within the prescribed parameters and with high degree of technical reliability. The Mauritius Automated Clearing and Settlement System and the Port Louis Automated Clearing House operated smoothly without any significant downtime, confirming their robust capacity to process high volumes of transactions based on Real Time Gross Settlement principles.

Financial Stability Cobweb[1]



Source: Bank of Mauritius staff estimates.

Risks to financial stability emanating from the global economy increased slightly in 2016Q4 compared to 2015Q4. The increase was driven by higher food and energy prices while volatility was relatively low in financial markets. Growth performance was rather mixed in major trading partner countries. Financial stability risks emanating from the domestic front fell between 2015Q4 and 2016Q4. GDP growth and investment rate improved, while the current account recorded a lower deficit. Nevertheless, these improvements were weighed by higher y-o-y inflation, appreciation of the rupee and deterioration in the terms of trade.

Household debt risk declined over the year to 2016Q4. However, sub-indicators within the household sector were rather mixed. Household indebtedness was lower as a result of relatively higher growth of disposable income compared to bank credit to households. Slow credit expansion also resulted in credit-to-GDP gap dipping further into negative and pointed to lower risk. Debt service cost of households has fallen as a result of lower domestic interest rates. Non-performing loans ratio on personal and professional credit has increased over the year to 2016Q4 but was lower compared to 2016Q3.

Risks to financial stability emanating from the corporate sector have hardly changed, remaining at the same high score for three consecutive years. The non-performing loans ratio in key economic sectors point to deteriorating asset quality. Notwithstanding continued deleveraging, some corporates still have debt in multiples of their equity. Profitability, as measured by the return on equity, has fallen in 2016 on a consolidated basis as well as the coverage of finance costs. On a positive note, the cost of debt has fallen with the cut in the Key Repo Rate and corporate credit-to-GDP gap has fallen.

Akin to corporates, banking sector risk did not change much over the year but remained on a high score. Asset quality of banks has continued to deteriorate as evidenced by relatively high non-performing loans ratios - both in Mauritius and cross-border. Nevertheless, banks were adequately capitalised and liquid. Profitability was on the rise with higher return on equity. The value of large exposures to capital fell over the year.

[1] *See Bank of Mauritius Annual Report Year Ended 30 June 2016 for technical information regarding the construction of the financial stability cobweb.*

Table 1.1: Mauritius: Selected Economic Indicators, 2014-2016

	2014	2015	2016
Nominal GDP (billions of Rupee)	392.1	409.5	434.2
Real GDP growth (basic prices; growth rate in %)	3.6	3.0	3.5
Inflation rate (y-o-y end period; growth rate in %)	0.2	1.3	2.3
CORE1 (y-o-y end period; growth rate in %)	0.8	1.1	0.3
CORE2 (y-o-y end period; growth rate in %)	2.1	2.3	1.7
Key Repo Rate (end December)	4.65	4.40	4.00
Unemployment rate (in %)	7.8	7.9	7.3
Nominal exchange rate (Rs/US$) - End of Period	32.1	36.5	36.8
Nominal exchange rate (Rs/US$) - Period Average	32.0	36.6	36.8
Nominal Effective Exchange Rate (Indices) [1]			
MERI1 (currrency weighted)	94.4	103.3	101.5
MERI2 (currrency weighted)	93.8	102.2	100.3
NEER (trade weighted)	94.3	98.4	95.4
Real Effective Exchange Rate [1]	84.3	88.5	85.4
Saving-Investment Balance (in % GDP)			
Investment *	18.9	17.4	17.2
Private	14.0	12.6	12.8
Public	4.8	4.7	4.4
Change in Inventories	0.8	0.7	-0.5
Savings*	18.9	17.4	17.2
External (with global business)	5.6	5.0	4.3
Domestic	13.3	12.4	12.9
Private	14.2	14.0	15.8
Public [2]	-0.9	-1.6	-2.9
Public Finance (in % GDP)			
Revenue	20.3	20.6	20.8
Expenditure	23.5	23.3	24.8
Current	21.1	21.9	23.4
Capital	2.4	1.4	1.4
Budget Balance	-3.2	-2.8	-4.0
Primary Balance	-0.6	-0.4	-1.6
Public Debt	60.7	63.7	64.5
Domestic	44.7	47.2	49.7
External	16.0	16.5	14.8
Monetary & Financial			
Private sector bank credit (growth rate in %)	1.3	4.2	-0.2
Velocity of circulation	1.04	0.98	0.95
Balance of Payments			
Current account (in % GDP)	-5.6	-5.0	-4.3
Trade balance (in % GDP)	-17.7	-16.0	-16.8
Gross official reserves (in Rs million)	124,344	152,902	178,858
Gross official reserves (in US$ million)	3,919	4,260	4,967
Reserve import coverage [3]	6.2	7.7	9.3

[1] An increase in the index indicates depreciation of the rupee.
[2] Defined as the difference between Government's total revenue and current expenditure.
[3] In months of imports of goods and services.

** Reflects accounting identity of investment being equal to savings (external plus domestic).*

2. External Economic Developments

Global economic activity improved in the last months of 2016 and latest economic indicators point to a continued improvement in 2017. Concurrently, the growth forecasts by leading international institutions and private sector analysts have been revised upward. The pick-up in commodity prices has led to an uptick in global headline inflation, helping to reduce deflationary pressures in advanced economies. While monetary policy stance in a majority of advanced economies is expected to remain accommodative, downside risks to global growth could emanate from a number of factors, namely potential slowdown in global trade flows, tighter global financial conditions and heightened geopolitical strains.

2.1 Growth

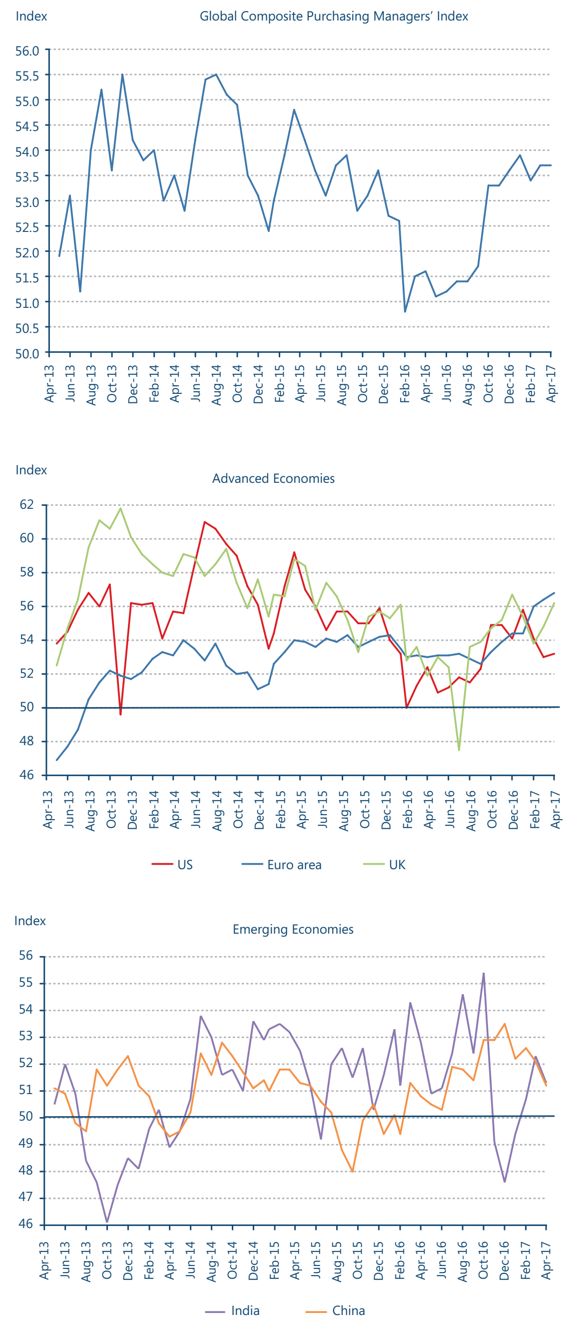
The world economy is currently pointing towards an upturn, albeit modest. The rebound in economic activity is being upheld in both advanced and emerging market and developing economies (EMDEs). Nonetheless, the pace of global GDP growth would stay lower compared to the period before the economic and financial crisis on account of decelerating productivity growth and lower rates of expansion in global trade.

Lately, the improving dynamics have been confirmed by higher frequency data, suggesting a pick-up in global growth in 2017. For instance, the Global Composite Purchasing Managers' Index increased from 51.6 in April 2016 to 53.7 in April 2017 (Chart 2.1). The increased growth momentum is also reflected in the latest global economic growth forecast of the International Monetary Fund (IMF). According to the April 2017 World Economic Outlook, global growth is expected to rise to 3.5 per cent this year and 3.6 per cent in 2018, from 3.1 per cent in 2016.

The IMF's optimistic outlook for 2017 is mostly based on expectations of higher growth in advanced economies. Real output growth in advanced economies is forecast to accelerate to 2.0 per cent in 2017, from 1.7 per cent in 2016 on the basis of relatively stronger activity in 2016H2, coupled with anticipated fiscal stimulus in the US. The IMF now reckons higher GDP growth for most advanced economies compared to its January 2017 projections, with major upward revisions applicable to the UK, Japan and Spain.

EMDEs are also forecast to record an increase in real activity in 2017 as macroeconomic conditions revert to normal in several large economies. Growth is expected to increase from 4.1 per cent in 2016 to 4.5 per cent in 2017. Growth prospects were slightly revised up for China to 6.6 per cent on the back of expected further policy stimulus measures. India is projected to expand by 7.2 per cent, while Brazil would grow by 0.2 per cent.

Chart 2.1 Composite Purchasing Managers' Index

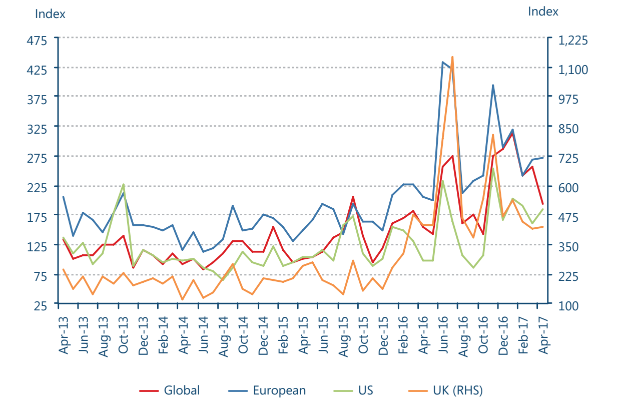


Source: Markit.

Nevertheless, the global economy remains subject to a number of uncertainties, which include the future stance of US economic policy, the upcoming exit of the UK from the European Union ("Brexit"), growing streams of nationalist and protectionist policies, difficult geopolitical situations and refugee migration. In addition, 'a faster-than-expected pace' of interest rate normalisation in the US could tighten financial conditions in various parts of the world and result in a strengthening of the US dollar, which altogether would strain some EMDEs, especially those having their currencies pegged to the US dollar.

Though falling since December 2016, global policy uncertainty has remained elevated as the various indices more than doubled over the year to April 2017 (Chart 2.2). Mostly, political events were behind the spikes noted. The results of the presidential election in the US and the ensuing policy stance of the new US administration which sent the index to record highs; issues surrounding Brexit; presidential elections in major European countries; and geopolitical strains in the Middle East weighed on market sentiment. Uncertainties still prevail given the lack of clarity over the ramifications of these events and as new challenges - including the old Greek debt issue - re-emerge.

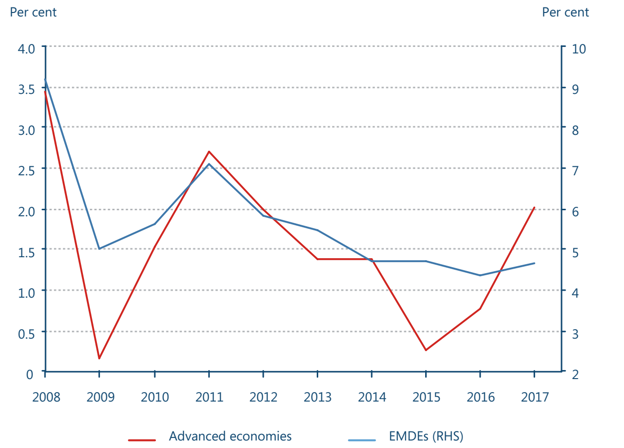
Chart 2.2 **Global Economic Policy Uncertainty Index***



** The Global Economic Policy Uncertainty Index is a measure of policy-related economic uncertainty and is based on media coverage and divergences in economic forecasts derived from different sources.*

Source: http://www.policyuncertainty.com

Chart 2.3 **Inflation in Advanced and Emerging Economies**



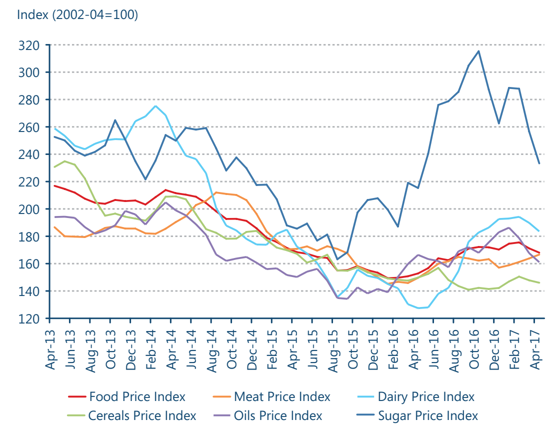
Source: OECD.

2.2 Macro-Financial Risks

Monetary policy remains highly accommodative in a number of countries, somewhat lending support to high asset prices and build-up in debt liabilities. The negative interest rate policy pursued by some central banks, including the European Central Bank (ECB) and Bank of Japan, may impact the financial sectors in these economies by eroding profitability of the banking sector and hindering lending activity. Persistently low interest rates may lead to asset price bubbles and high NPL, which pose a risk to global financial stability.

The US Federal funds rate hikes in December 2016 and March 2017 may also impact negatively on the financial markets of EMDEs as investors search for higher yields. The tightening of monetary policy in the US might prompt central banks in EMDEs to revisit their own monetary policy stance with a view to restraining massive capital outflows. Fluctuations in financial flows

Chart 2.4 **FAO Food Price Indices**



Source: FAO.

experienced after the US elections in November 2016 might increase the funding cost for banks in EMDEs, potentially having an adverse impact on domestic credit conditions in these economies.

The challenges facing the European banking system mirror more general concerns, including subdued economic growth and excessive sovereign debt. Given the size and magnitude of European banks and their interrelationship with the rest of the world, an intensification of problems in Europe could have implications on the cost and availability of funding, thereby posing a major risk to financial stability.

2.3 Inflation

Global inflationary pressures continue to remain low in major advanced economies, although headline inflation rates have recently been on an uptrend on the back of strengthening commodity prices. Core inflation rates - which exclude energy prices - have, however, remained more or less stable, mostly undershooting inflation targets in a number of advanced countries. In contrast, mixed inflation outcomes remain prevalent in EMDEs against the backdrop of diverging exchange rate movements and idiosyncratic factors. While headline inflation has increased in several EMDEs amid higher commodity prices, they have retreated in others, reflecting waning pass-through from substantial weakening of currencies in 2015 and early 2016. In China, inflation recovered as producer price inflation turned positive after more than four years of deflation, reflecting mainly a decline in spare capacity, firmer commodity prices, and improving real estate investment. Inflation in advanced economies is forecast to increase from 0.8 per cent in 2016 to 2.0 per cent in 2017, mirroring a rise in energy prices and closing of the output gap. Inflation in EMDEs is expected to rise from 4.4 per cent in 2016 to 4.7 per cent in 2017 (Chart 2.3).

2.4 Commodity Prices

Food prices reversed course in 2016 and 2017Q1. After bottoming at 149.3 in January 2016, the Food and Agriculture Organisation (FAO) Food Price Index climbed to 168.0 points in April 2017. Compared to April 2016, the index rose by about 12.5 per cent, more or less reflecting broad-based hikes in all of its components. Notably, the dairy index increased by 26.5 per cent; sugar by 17.0 per cent and oils by 15.8 per cent. The sugar price surge emanated from lower production in major sugar-producing and exporting countries, namely Brazil, Thailand and India, with crops being affected by unfavourable weather conditions (Chart 2.4).

Grain prices generally trended downward in 2016H2 but recovered, to some extent, in early 2017. The International Grains Council's (IGC) Grains and Oilseed Index retreated to 188.6 on 30 December 2016, representing a decline of 13.3 per cent relative to the peak of 217.5 recorded on 8 June 2016. The decline in the index was mainly due to a glut in production that depressed price quotations. However, the index recouped some of its losses, averaging 190 during the first four months of 2017 on the back of weather-related worries for wheat, maize and soyabeans in key exporter countries. Buoyant demand and currency movements provided some impetus to the index (Chart 2.5).

Oil prices were on a broad uptrend in 2016 and early 2017, after bottoming out in January 2016. The monthly average oil price of NYMEX WTI gradually increased from US$31.7 per barrel in January 2016 to US$51.2 per barrel in April 2017. The price of ICE Brent also rose from US$31.9 per barrel to US$53.9 per barrel over the same period. Higher prices were mainly due to tight oil supply reflecting lower production by US shale companies, wildfires in Canada leading to closures of oil sand sites, and military turmoil in Nigeria curtailing oil production to 22-year lows, amongst others. The pick-up in oil prices towards end-2016 was driven by the agreement among all member countries of the Organisation of Petroleum Exporting Countries and several other major producers to cut oil production, for the first time since 2008, to 32.5 million barrels a day (Chart 2.6).

The price of gold recovered to an average of US$1,276.6 an ounce in June 2016, from a low of US$1,050.8 an ounce in December 2015. Heightened uncertainty after the Brexit referendum led to a sell-off of riskier assets as investors favoured the safe-haven appeal of gold. However, gold prices declined to an average of US$1,150.5 an ounce in December 2016 after the US Federal Reserve System

(US Fed) tightened monetary policy, which prompted investors to take short positions as the opportunity cost of holding gold increased. Prices picked up to an average of US$1,269.5 an ounce in April 2017 on safe haven demand amid rising geopolitical risk in Europe and concerns over the policies of the new US administration.

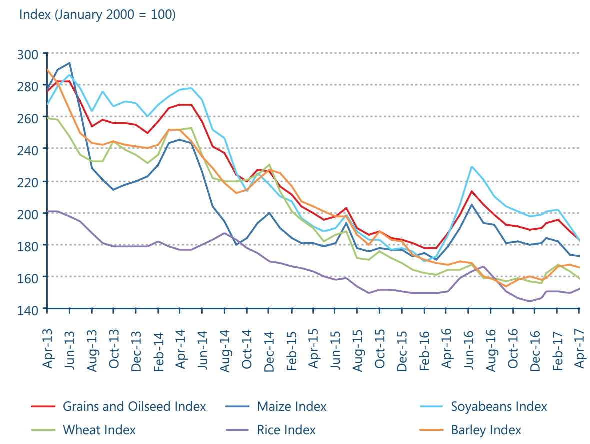
2.5 Exchange Rate Developments

Currency markets remained under the spell of uncertainties related to the impact of Brexit and monetary policy stances of major advanced economies. During 2016, the US dollar underperformed on the back of a number of factors, including uncertainty over further monetary policy tightening by the US Fed and dovish comments by the US Fed Chair focusing on downside risks to the US economy. However, the US dollar appreciated amid safe haven demand after the result of the Brexit referendum. Although the US dollar was pressured ahead of the US presidential election in November 2016, it strengthened thereafter against major currencies, reflecting a rise in US Treasury yields which posted their largest gains in more than five years. In addition, expectations that the newly elected US President's administration would adopt expansionary fiscal policies, which would trigger higher inflation and faster-than-expected interest rate hikes, also boosted the US currency.

The euro broadly weakened during the period under review, weighed down by headwinds following UK's vote to leave the EU, the broad-based strength of the US dollar, weaker economic data amid downside risks to Eurozone's growth, widening interest rate differentials, and political uncertainty in the Eurozone. However, the single currency rallied in April 2017 on the back of subdued political risks following the victory of Emmanuel Macron in the French presidential elections. Increasing expectations that the ECB might signal policy tapering also supported the euro.

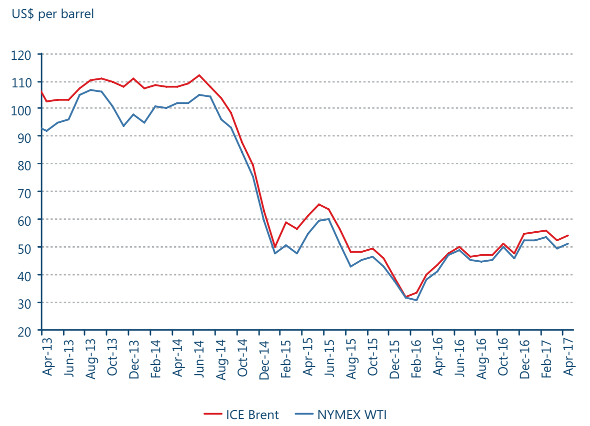
Initially, the Pound sterling was hit by political woes in Britain and further accommodative monetary policy by the Bank of England (BoE) in August 2016. Subsequently, the British currency recouped some of its previous losses on improvement in investor sentiment, following UK Prime Minister's call for snap general elections (Chart 2.7).

Chart 2.5 IGC Grains and Oilseed Indices



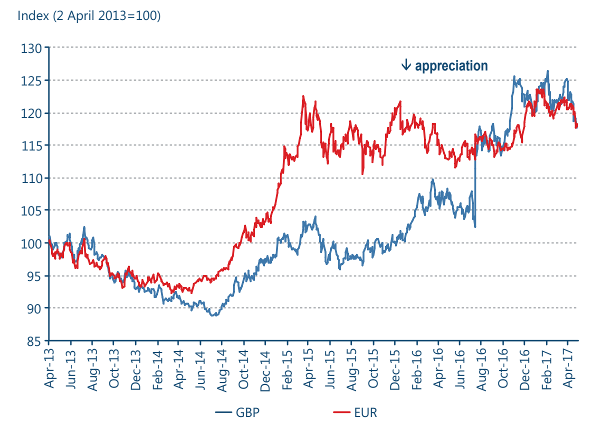
Source: International Grains Council.

Chart 2.6 Crude Oil Prices



Source: Thomson Reuters.

Chart 2.7 Evolution of the GBP and EUR against the US Dollar



Source: Thomson Reuters.

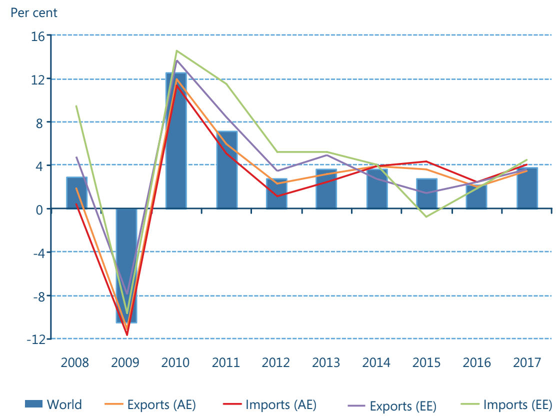
Exchange rate volatility, as measured by the standard deviation of the daily exchange rate on a monthly basis spanning from May 2016 to April 2017, showed that volatility peaked in November 2016 for the US dollar and the euro. Currencies of commodity-exporter countries - namely Brazil, Russia, and South Africa - generally appreciated, reflecting a pick-up in commodity prices and improved market sentiment vis-à-vis EMDEs amid ongoing accommodative monetary policy in the majority of advanced economies.

2.6 Trade

Global trade growth has touched its lowest level since the financial crisis, falling short of global GDP growth for the first time in 15 years. The growth rate of world trade volume of goods and services decelerated from 2.7 per cent in 2015 to 2.2 per cent in 2016 (Chart 2.8). Factors explaining the subdued global trade performance include the slowdown of both exports and imports of advanced economies and EMDEs, weak investment, and contracting imports in China and in major commodity exporters.

Global trade is projected to recover in 2017 to 3.8 per cent, supported by a pick-up in trade flows of both advanced economies and EMDEs. The volume of goods and services traded by advanced economies is forecast to rise from 2.1 per cent in 2016 to 3.5 per cent in 2017 as a result of an increase in economic activity. Corresponding figures for EMDEs are 2.5 per cent and 3.6 per cent, respectively, aided by an expected rebound in demand for imports from large EMDEs. However, factors likely to weigh on world trade, going forward, include sustained weakness in global investment, and a lower pace of trade liberalisation on the back of uncertain trade policy in the US and Europe. Protectionist measures might also exacerbate to the drag in global trade.

Chart 2.8 **World Trade**



Note: AE: Advanced economies EE: Emerging economies.

Source: IMF WEO, April 2017.

2.7 Monetary Policy

Increasing divergence is currently being observed in monetary policy stances of the central banks of advanced economies. After upgrading the assessment of the US economy, the US Fed, at its Federal Open Market Committee meetings of December 2016 and March 2017, raised its target rate for the Federal funds rate by 50 basis points cumulatively from a range of 0.25-0.50 per cent to 0.75-1.00 per cent

Table 2.1: Monetary Policy Stance

	Current rate *(Per cent p.a)*	Change since Dec 2015 (basis points)	Change since Dec 2016 (basis points)	Forecast (Per cent)
Developed Economies				
United States	1.00	+75	+50	1.00
Euro Area	0.00	-5	0	0.00
United Kingdom	0.25	-25	0	0.25
Japan	-0.10	-20	0	-0.10
Emerging Market and Developing Economies				
South Africa	7.00	+75	0	7.00
China	4.35	0	0	4.15
India	6.25	+50	0	6.00

Source: JPMorgan.

(Table 2.1). In contrast, the ECB, which started its corporate bond purchase programme on 8 June 2016 and a new programme of long-term loans to banks on 22 June 2016, extended its debt-buying programme on 8 December 2016. In August 2016, the BoE cut its benchmark interest rate to a record low of 0.25 per cent, initiated the purchase of UK corporate bonds of up to GBP10 billion, and expanded the UK Government bond purchase programme by an additional GBP60 billion, as part of a broad package of measures to further stimulate the UK economy and meet its inflation target.

Monetary policy stances across central banks other than major advanced economies remained also accomodative. The Reserve Bank of India cut the repo rate twice in 2016 to support growth and to attain an inflation target of 5 per cent by end of FY2016-17. The central banks of Australia and New Zealand reduced rates on, at least, two occasions in 2016 so as to fight deflationary pressures or persistently low inflation and to restrain the strengthening of their respective currencies. Brazil's central bank lowered its policy rate by a total of 300 basis points from October 2016 to April 2017 in an attempt to overcome its deepest recession on record.

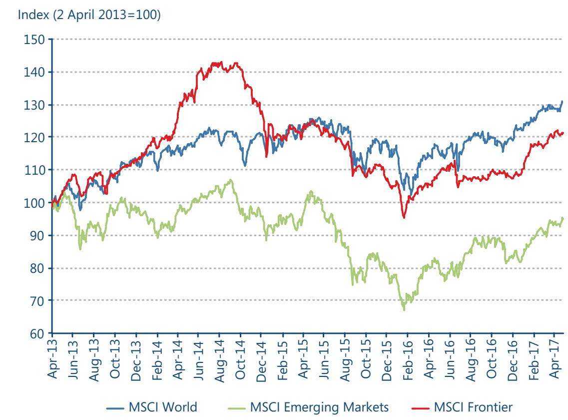
2.8 Equity Markets

Global equity indices, which were marked with episodes of volatility during 2016H2, have recovered somewhat in the first four months of 2017. Markets remained volatile due to lack of clarity of the modalities of Brexit. In addition, banking sector woes in the EU and the US presidential election kept investors on edge. After the US election results, markets rallied on expectations of pro-growth policies of the new US administration. The MSCI World Index increased by 11.4 per cent between April 2016 and April 2017, while the MSCI Emerging Markets Index was higher by 15.5 per cent. The MSCI Frontier Index gained 13.4 per cent over the same period (Chart 2.9).

2.9 Volatility

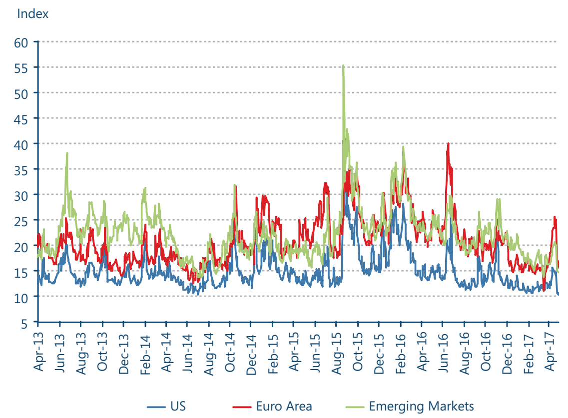
Prior to Brexit, global financial markets mostly stabilised, but post-Brexit, volatility emerged. The largely unpredicted results of the UK referendum sent shock waves through financial markets, raising volatility, as measured by VIX and VIX-Emerging Markets, by 49.3 per cent and 15.2 per cent, respectively, on 24 June 2016 compared to the previous day. Thereafter, volatility declined. Nevertheless, financial markets were subject to some volatility again at the beginning of November 2016 amid significant speculation over the result of the US presidential election. Volatility subsided, following supportive investor sentiment emanating from the election of Donald Trump in the US who indicated that he would spend massively on infrastructure and would streamline business regulations.

Chart 2.9 MSCI World, Emerging Markets and Frontier Indices



Source: Thomson Reuters.

Chart 2.10 Volatility Indices



Source: Thomson Reuters.

3. Domestic Economic Developments

The domestic economy recovered in the second half of 2016, but more strikingly, investment experienced a major turnaround as private investment grew for the first time in five years. The economic outlook is expected to brighten somewhat, supported by major infrastructural projects. Statistics Mauritius expects real GDP to grow by 3.8 per cent in 2017, supported by a significant rebound in the construction sector. Bank staff forecasts that the real GDP growth rate would be in the range of 3.8 to 4.0 per cent conditional on the timely implementation of major public sector infrastructural projects.

3.1 GDP by Expenditure

The domestic economy gathered momentum in 2016H2, supported by sustained final consumption expenditure and a substantial pick-up in investment. After growing by 2.3 per cent in 2016Q2, real GDP accelerated by 3.7 per cent in 2016Q3 and grew by a further 4.1 per cent in 2016Q4 (Chart 3.1). Household consumption expenditure, which makes up about 75 per cent of GDP, remained resilient in 2016H2 and rose by 3.1 per cent in real terms, unchanged from 2015H2. Government consumption expenditure growth increased from 0.8 per cent in 2015H2 to 1.1 per cent in 2016H2.

A revival in overall investment spending in 2016H2 – attributable to increased building and construction activities as well as robust capital spending on machinery and equipment, especially in 2016Q3 – gave extra impetus to real GDP growth. In real terms, Gross Fixed Capital Formation (GFCF) grew by 5.6 per cent in 2016H2 as against a contraction of 8.7 per cent in 2015H2 (Table 3.1). The investment rate, defined as the ratio of GFCF to GDP at market prices, increased to 17.0 per cent in 2016H2, from 16.8 per cent in 2015H2.

Net exports turned into a drag on real GDP growth due to the continuous underperformance of exports of goods and services, which contracted by 2.8 per cent in 2016H2, after declining by 5.8 per cent in 2015H2. Imports of goods and services also fell by 1.1 per cent in 2016H2, after growing at 1.5 per cent in 2015H2 mostly associated with a contraction of 7.7 per cent in imports of services.

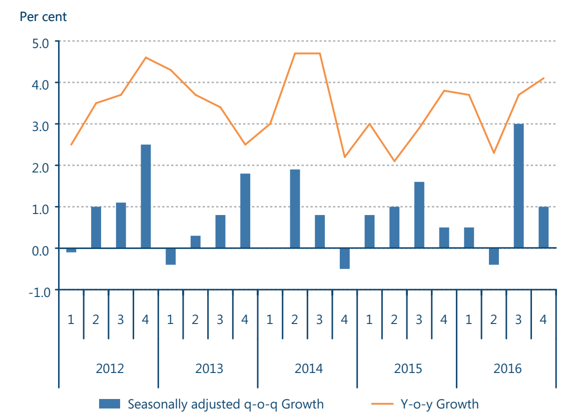
The drags from external demand would be expected to subside gradually in 2017, with a better growth outlook of major trading partners.

The '*National Export Strategy*[1]' should also give a boost to domestic exports through the identification of niche markets. However, the prospects for a sustained recovery in domestic exports remain subject to uncertainty. A lingering weakness of the European economies, together with a sluggish performance of the UK due to Brexit, could pose some downside risks to the export sector. Domestically, household consumption expenditure should continue to lend support to growth in real activity, and large-scale infrastructure works and building activities are expected to hold up quite well given the substantial increase in public investment. Inbound tourism and financial services are also expected to be supportive to domestic growth momentum.

3.2 GDP by Sector

On the supply side, all the sectors registered positive growth in 2016H2. The average real GDP growth rate for 2016H2 was 3.9 per cent, up from 3.4 per cent in 2015H2. Growth momentum was underpinned by buoyant activity in the key services sectors and a rebound in the construction sector (Table 3.2).

Chart 3.1 Real GDP Growth Rate



Source: Statistics Mauritius.

[1] *The 'National Export Strategy' is a government initiative to identify trade opportunities and address trade challenges of the export sector, considering the erosion of commercial preferences such as the abolition of the EU sugar quota in 2017.*

The '*Agriculture*' sector grew by 3.0 per cent in 2016H2, after expanding by 1.4 per cent in 2015H2, reflecting a higher sugar production of 386,277 tonnes in 2016 compared to 366,070 tonnes in 2015 and higher sugar prices. The '*Sugarcane*' sub-sector grew by 5.8 per cent in 2016H2 as against a contraction of 6.0 per cent in 2015H2. The share of sugar exports in total exports rose from 9.1 per cent in 2015H2 to 10.8 per cent in 2016H2.

The '*Manufacturing*' sector recovered slightly in 2016H2, echoing a better performance of the '*Sugar milling*' sub-sector. '*Manufacturing*' grew by 1.4 per cent in 2016H2 compared to a growth of 0.4 per cent in 2015H2. The '*Sugar milling*' sub-sector expanded by 7.0 per cent in 2016H2 as against a contraction of 8.9 per cent in 2015H2. However, '*Textile*' experienced again a poor performance as it contracted by 2.5 per cent after a decline of 1.1 per cent in 2015H2. For the year 2016, value added by the manufacturing sector represented nearly 14.0 per cent of total value added in the economy.

The '*Construction*' sector recorded a significant rebound in the second half of 2016. After shrinking by 2.3 per cent in 2015H2, the sector registered a commendable growth of 6.8 per cent in 2016H2. While the number of building permits for residential buildings fell from 3,334 in 2015H2 to 3,239 in 2016H2, those for non-residential buildings rose from 165 to 230 over the same period, which would be expected to support the sector.

The '*Accommodation and food service activities*' sector grew by 9.7 per cent in 2016H2, as the sector reaped the benefit of improved air access and market diversification efforts. Tourist arrivals were higher in 2016H2, reaching 688,763 compared to 617,471 in 2015H2. Total tourist nights also went up from 6,059,625 in 2015H2 to 6,626,375 in 2016H2. The upbeat performance of the tourism industry, as reflected by a higher number of tourist arrivals in 2017Q1, would surely consolidate the sector's contribution to the domestic growth performance.

In the '*Information and communication*' sector, growth remained robust, supported by continued demand for data communication services. The sector grew by 5.9 per cent in 2016H2, up from 5.6 per cent in 2015H2. Among other key services sectors, '*Financial and insurance activities*' grew by 5.6 per cent in 2016H2 while '*Professional, scientific and technical activities*' and '*Wholesale and retail trade*' registered growth of 5.8 per cent and 3.0 per cent, respectively.

The domestic economy is projected to grow faster at a close-to-trend rate in 2017. According to Statistics Mauritius, the '*Construction*' sector

Table 3.1: Domestic and External Demand (per cent, y-o-y)

	2014			2015			2016		
	Q3	Q4	Avg	Q3	Q4	Avg	Q3	Q4	Avg
I. Domestic Demand									
Final consumption	**3.1**	**3.4**	**3.3**	**3.4**	**2.2**	**2.8**	**2.6**	**3.0**	**2.8**
Households	3.1	2.9	3.0	3.2	3.0	3.1	2.9	3.3	3.1
General Government	3.1	6.5	4.8	3.9	-2.4	0.8	0.9	1.3	1.1
GDFCF	**-11.4**	**-4.2**	**-7.8**	**-2.9**	**-14.4**	**-8.7**	**9.4**	**1.7**	**5.6**
Building and construction work	-8.4	-7.1	-7.8	-3.7	-2.5	-3.1	8.8	6.6	7.7
Machinery and equipment	-16.5	0.3	-8.1	-1.5	-30.3	-15.9	10.7	-7.4	1.7
II. Net External Demand									
Exports of goods and services	**20.0**	**7.0**	**13.5**	**-5.8**	**-5.8**	**-5.8**	**-5.9**	**0.3**	**-2.8**
Exports (goods)	18.8	7.6	13.2	-8.4	-13.1	-10.8	-12.3	-5.7	-9.0
Export (services)	21.3	6.4	13.9	-3.0	0.8	-1.1	0.3	5.0	2.7
Imports of goods and services	**8.9**	**14.1**	**11.5**	**4.9**	**-1.9**	**1.5**	**2.0**	**-4.2**	**-1.1**
Imports (goods)	9.4	14.5	12.0	5.8	-0.6	2.6	3.6	-0.7	1.5
Imports (services)	7.5	13.1	10.3	2.5	-5.2	-1.4	-2.0	-13.3	-7.7
III. GDP at market prices	**4.7**	**4.0**	**4.4**	**2.6**	**3.2**	**2.9**	**3.6**	**4.3**	**4.0**

Source: Statistics Mauritius and BoM staff estimates.
Avg: Average.

is expected to experience a strong recovery in 2017 with major projects planned for take-off. The spillover effects in the 'Construction' sector to other activities such as architectural services, engineering and quantity surveying would also be supportive to domestic economic activity. The '*Manufacturing*', '*Professional, scientific and technical activities*', '*Administrative and support service activities*' and '*Information and communication*' sectors are all anticipated to perform better in 2017 compared to 2016 (Table 3.3). The '*Accommodation and food service activities*' sector is forecast to grow at a relatively lower rate mainly due to base effects arising from a high growth rate in the previous year. Nonetheless, the sector would benefit from higher tourist arrivals of around 1,350,000 and tourism earnings of about Rs58 billion. Overall, for 2017, Statistics Mauritius projects GDP growth to pick up to 3.8 per cent. Private sector analysts project the economy to grow by a slightly higher rate of 3.9 per cent. The IMF also sees growth strengthening to 3.9 per cent in 2017 (Table 3.4).

Bank staff estimate domestic output growth for 2017 ranging between 3.8 per cent and 4.0 per cent. Supportive monetary conditions, improving business confidence and considerable public investment programmes are expected to back domestic output in 2017. Nonetheless, headwinds to domestic growth prospects still prevail, as the materialisation of the real GDP growth forecasts depends much on the implementation of announced public investment projects. In addition, continued uncertainties in the global environment, including political uncertainties, could impact negatively on external demand.

Table 3.2: Sectoral Growth Rates (per cent, y-o-y)

	2015			2016		
	Q3	Q4	Avg	Q3	Q4	Avg
Primary Sector						
Agriculture forestry and fishing	2.6	0.2	1.4	3.5	2.5	3.0
Mining and quarrying	-5.6	-3.5	-4.6	0.9	1.4	1.2
Secondary Sector						
Manufacturing	-0.8	1.5	0.4	1.2	1.6	1.4
Electricity, gas, steam and AC	1.7	6.9	4.3	3.1	2.3	2.7
Water supply	1.9	2.6	2.3	3.9	1.1	2.5
Construction	-2.7	-1.8	-2.3	7.3	6.2	6.8
Tertiary Sector						
Wholesale and retail trade	3.1	2.9	3.0	2.9	3.0	3.0
Transportation and storage	2.9	4.1	3.5	4.1	3.7	3.9
Accommodation and food service activities	10.1	10.8	10.5	7.4	12.0	9.7
Information and communication	5.0	6.2	5.6	4.8	6.9	5.9
Financial and insurance activities	5.5	5.7	5.6	5.6	5.6	5.6
Real estate activities	1.7	9.8	5.8	3.2	2.6	2.9
Professional, scientific and technical activities	5.2	5.3	5.3	5.8	5.7	5.8
Administrative and support service activities	6.6	6.8	6.7	6.6	5.6	6.1
Public administration and defence	2.5	-2.9	-0.2	3.4	3.1	3.3
Education	2.2	1.4	1.8	1.0	0.2	0.6
Human health and social work activities	4.3	2.9	3.6	2.3	2.4	2.4
Art, entertainment and recreation	4.8	5.1	5.0	5.2	4.8	5.0
Other service activities	2.8	3.6	3.2	3.2	3.2	3.2
GDP at basic prices	**2.9**	**3.8**	**3.4**	**3.7**	**4.1**	**3.9**
Taxes on products (net of subsidies)	7.0	7.1	7.1	1.2	3.2	2.2
GDP at market prices	**2.6**	**3.2**	**2.9**	**3.6**	**4.3**	**4.0**

Source: Statistics Mauritius and BoM staff estimates.

Avg: Average.

Table 3.3: Sectoral Real Growth Rates (per cent over previous year)

	2015	2016	2017
Primary Sector			
Agriculture, forestry and fishing	-0.3	3.7	2.3
Mining and quarrying	-3.4	1.0	1.5
Secondary Sector			
Manufacturing	0.0	-0.1	1.1
- sugar	-8.9	7.0	1.5
- food processing (excluding sugar)	3.0	1.5	1.5
- textile	-2.8	-5.5	0.2
- other manufacturing	-0.2	3.2	1.5
Electricity, gas, steam and AC	3.8	4.2	4.0
Water supply	3.0	2.0	2.5
Construction	-4.9	0.0	7.0
Tertiary Sector			
Wholesale and retail trade	2.8	3.0	3.0
Transport and storage	3.4	3.9	3.8
Accomodation and food service activities	8.7	9.2	4.1
Information and communication	6.9	5.9	6.0
Financial and insurance activities	5.3	5.7	5.5
Real estate activities	4.3	3.9	3.4
Professional, scientific and technical activities	5.1	5.7	6.0
Administrative and support service activities	6.7	5.9	6.1
Public administration and defence	0.8	2.5	3.0
Education	2.5	0.5	2.4
Human Health and social work activities	3.4	2.1	3.9
Arts, entertainment and recreation	4.8	5.0	4.9
Other service activities	3.0	3.1	3.1
GDP at basic prices	**3.0**	**3.5**	**3.8**
Taxes on products (net of subsidies)	6.9	5.6	5.0
GDP at market prices	**3.5**	**3.7**	**3.9**

Source: Statistics Mauritius.

Table 3.4: Comparison of 2017 Real GDP Growth Rate Projections (in per cent)

	Real GDP Growth Rate Projections
Statistics Mauritius[1]	3.8
IMF[2]	3.9
MCB Focus[3]	3.9
SBM Insights[4]	3.9
Bank of Mauritius	3.8 - 4.0

[1] *National Accounts - March 2017.*
[2] *IMF World Economic Outlook - April 2017.*
[3] *MCB Focus - March 2017.*
[4] *SBM Insights - March 2017.*

3.3 Labour Market and Unit Labour Costs

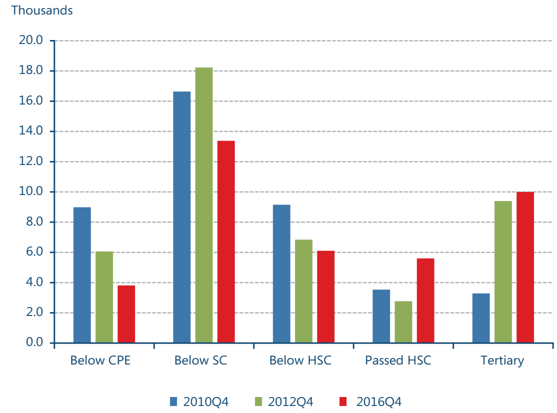
The labour market continues to exhibit rigidities in terms of skills mismatch and structural unemployment, resulting in high levels of both youth and female unemployment. Labour market characteristics in 2016Q4 showed that the unemployed youth (that is, those aged between 16 and 24 years) accounted for 47.0 per cent of the total unemployed. By gender, two out of three who are unemployed are women. Unemployment by educational attainment was biased towards two segments, namely those not having passed the School Certificate and those with tertiary education, representing 44.2 per cent and 25.7 per cent, respectively, of the total unemployed (Chart 3.2). In terms of duration of unemployment, 16 per cent of the unemployed had been looking for work for more than a year, underscoring the risk of long-term unemployment (Chart 3.3).

The supply of labour depends on the participation of those aged over 16 years in the labour force. The activity rate fell to 59.8 per cent in 2016Q4, from 61.0 per cent in 2015Q4 given a higher proportion of Mauritian population aged 16 years and over. There is some evidence of labour market slack, as this growing population seems to have increased the inactive population from 378,600 in 2015Q4 to 392,900 in 2016Q4. Going forward, to make optimal use of the economy's labour resources, it would be necessary to bring back the inactive population into the labour force through necessary inducements.

The unemployment rate has been estimated to drop to 7.3 per cent in 2016, from 7.9 per cent in 2015. This decline in the unemployment rate reflects more of a reduction in both the number of unemployed and labour force, which could possibly point towards labour market slack.

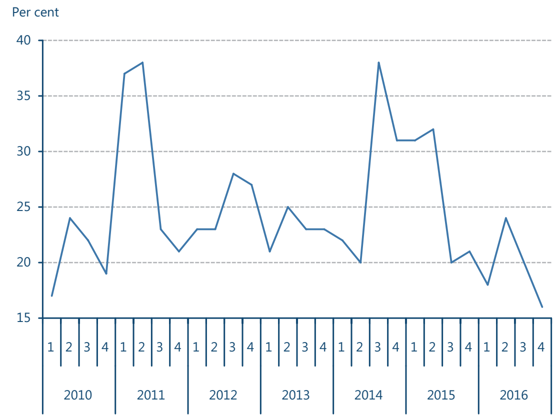
Quarterly data revealed that the unemployment rate dropped drastically from 7.9 per cent in 2015Q4 to 6.6 per cent in 2016Q4, with the seasonally-adjusted rate also falling from 8.6 per cent to 7.3 per cent. The unemployment pool shrunk by 7,700 in 2016Q4 compared to 2015Q4. The net change in employment was positive, increasing from 545,600 in 2015Q4 to 546,600 in 2016Q4, also reflecting the rise in male employment which more than offset a drop in female employment of age groups above 40 years.

Chart 3.2 Unemployment by Educational Attainment



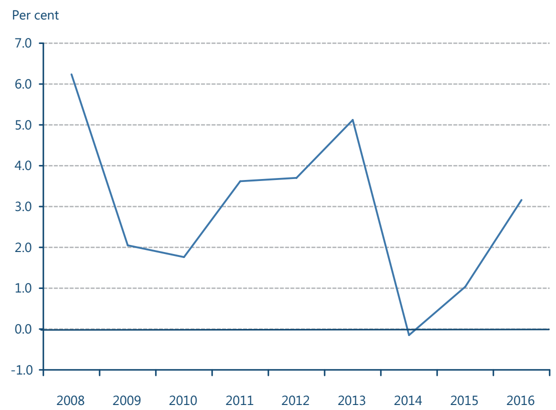
Source: Statistics Mauritius.

Chart 3.3 Unemployment by Duration (More than one year)



Source: Statistics Mauritius.

Chart 3.4 Growth in Unit Labour Costs



Source: Statistics Mauritius.

Compensation growth has continued to push unit labour costs up, having surpassed labour productivity growth again in 2016. Labour productivity is estimated to have increased by 3.4 per cent compared to 1.7 per cent in 2015, on account of a recovery in output growth and the slight increase in employment. Unit labour costs, which is calculated as compensation of employees divided by labour productivity, rose by 3.2 per cent in 2016 compared to an increase of 1.0 per cent in 2015 attributed to higher compensation in 2016 (Chart 3.4). On annual average basis, compensation has increased by 5.1 per cent over the period 2010 to 2016, outpacing labour productivity growth of about 2.4 per cent, thereby raising unit labour costs by about 2.6 per cent (Chart 3.5).

Wage increases tend to overlook whether there have been associated gains in productivity, driving up unit labour costs and impacting on competitiveness of our exports. Measures to boost output through innovation in capital and processes as well as on-going human capital development are required.

Chart 3.5 Growth in Labour Productivity and Compensation of Employees

Source: Statistics Mauritius.

3.4 Fiscal Sector Developments

Total revenue increased by 3.2 per cent, y-o-y, to Rs66.9 billion over the period July 2016 to March 2017 (Table 3.5). As a ratio of GDP, total revenue stood at 20.0 per cent, compared to 20.5 per cent for the period July 2015 through March 2016.

Total tax revenue, which accounted for nearly 90 per cent of total revenue, went up by 6.5 per cent from Rs 56.6 billion to Rs60.3 billion, driven mainly by strong increases of 12.8 per cent and 5.8 per cent in receipts from taxes on income and profits and taxes on goods and services, respectively. The low growth of 1.1 per cent in property tax collection can be associated to the budgetary measure to waive registration duty for first-time buyers of land and for the purchase of new houses and apartments. Social contributions went up by 3.0 per cent while revenue from grants declined by 47 per cent over the period under review.

Expenditure rose by 8.8 per cent from Rs69.6 billion to Rs75.8 billion over the period July to March 2017. As a ratio of GDP, expenditure went up from 22.1 per cent to 22.7 per cent. Increases in the wage bill, grants and social benefits accounted around 87 per cent of the increase in government expense. Net acquisition of non-financial assets remained unchanged at Rs3.5 billion and represented 1.0 per cent of GDP.

The budget deficit deteriorated significantly by 48.8 per cent, from Rs8.3 billion to Rs12.4 billion, as expenditure growth far outpaced revenue increases. The budget deficit stood 3.7 per cent of GDP over the period July through March 2017, compared to 2.6 per cent over the corresponding period in 2015/16. The deficit was financed exclusively from domestic sources. Foreign financing of the budget deficit was negative at about 1.6 per cent of GDP.

Public Debt

Public sector debt has trended upwards in recent years, reflecting primarily the persistence of domestically-funded fiscal deficits. Public sector debt increased by 8.1 per cent, from Rs267 billion as at end-March 2016 to Rs289 billion as at end-March 2017 (Table 3.6). As a share of GDP, it rose from 64.3 per cent to 65.6 per cent over the same period. Government securities issued for mopping up excess liquidity stood at nearly Rs16 billion as at end of March 2017, compared to Rs10 billion a year earlier. The discounted public sector debt as a ratio of GDP edged down from 56.1 per cent as at end-March 2016 to 55.6 per cent as at end-March 2017.

Domestic public sector debt rose by 15.0 per cent to Rs231 billion at the end of March 2017, while the share of long term domestic obligations in budgetary central government domestic debt has increased by 3.1 percentage points to 62.2 per cent. External public sector debt fell by 12.6 per cent to Rs58 billion, reflecting mainly an early repayment of external loan obligations amounting to $120 million in January 2017. Public sector external debt represented 13.2 per cent of GDP as at end-March 2017, compared to 16.0 per cent a year earlier.

The currency composition of budgetary central government external debt remained fairly balanced, suggesting relatively low foreign exchange risk. As at end-March 2017, 38 per cent of external debt was denominated in euro, while 34.8 per cent was in US dollar. With regard to the interest rate mix of public sector external debt, the share of variable interest rate stood at 57 per cent at the end of March 2017 (Table 3.7).

Table 3.5: Statement of Budgetary Central Government Operations

	2014-15	2015-16	2016-17 (Estimates)	July 2015 - March 2016	July 2016 - March 2017
					(Rs million)
1. Revenue	**82,063**	**88,236**	**102,400**	**64,783**	**66,865**
Taxes on income, profits, and capital gains	18,059	19,176	20,554	13,105	14,786
Taxes on goods & services	47,488	50,130	55,082	36,886	39,027
2. Expense	87,385	97,167	107,335	69,616	75,755
of which Interest	9,931	10,119	11,296	7,529	8,075
3. Net Acquisition of Non-Financial Assets	**9,498**	**5,987**	**10,020**	**3,491**	**3,498**
4. Budget Balance	**-14,820**	**-14,918**	**-14,954**	**-8,323**	**-12,388**
Primary Balance	***-4,889***	***-4,799***	***-3,658***	***-794***	***-4,313***
Overall borrowing requirement	**17,243**	**14,929**	**18,546**	**9,049**	**10,889**
Financing					
Domestic	17,661	16,228	23,555	10,345	16,122
Foreign	-418	-1,299	-5,009	-1,296	-5,234
			As a ratio to GDP (Per cent)		
1. Revenue	**20.5**	**20.9**	**22.7**	**20.5**	**20.0**
Taxes on income, profits, and capital gains	4.5	4.5	4.6	4.2	4.4
Taxes on goods & services	11.9	11.9	12.2	11.7	11.7
2. Expense	**21.8**	**23.0**	**23.8**	**22.1**	**22.7**
of which Interest	2.5	2.4	2.5	2.4	2.4
3. Net Acquisition of Non-Financial Assets	**2.4**	**1.4**	**2.2**	**1.1**	**1.0**
4. Budget Balance	**(3.7)**	**(3.5)**	**(3.3)**	**(2.6)**	**(3.7)**
Primary Balance	***(1.2)***	***(1.1)***	***(0.8)***	***(0.3)***	***(1.3)***
Overall borrowing requirement	**4.3**	**3.5**	**4.1**	**2.9**	**3.3**
Financing					
Domestic	4.4	3.8	5.2	3.3	4.8
Foreign	(0.1)	(0.3)	(1.1)	(0.4)	(1.6)

Sources: Statistics Mauritius and Ministry of Finance and Economic Development.

Table 3.6: Public Sector Debt

	Dec-15	Mar-16	Dec-16	Mar-17 *Provisional*
		(Rs million)		
1. Short-term Domestic Obligations [1]	22,386	23,781	23,907	24,932
2. Medium-term Domestic Obligations [1]	51,104	49,704	52,769	51,549
3. Long-term Domestic Obligations [1]	102,192	105,998	119,432	125,601
4. Government Securities Issued For Mopping up Excess Liquidity	5,967	10,408	10,172	15,947
5. Domestic Central Government Debt (1+2+3+4)	181,649	189,891	206,280	218,029
	(44.4)	*(45.7)*	*(47.5)*	*(49.5)*
6. External Government Debt	54,676	54,024	51,637	46,103
	(13.4)	*(13.0)*	*(11.9)*	*(10.5)*
7. Extra Budgetary Unit Domestic Debt	24	24	24	24
8. Extra Budgetary Unit External Debt	126	126	102	101
9. Local Government Debt	0	0	0	0
10. Public Enterprise Domestic Debt	11,532	10,732	9,595	12,598
11. Public Enterprise External Debt	12,674	12,261	12,385	11,870
12. Domestic Public Sector Debt	193,205	200,647	215,899	230,651
	(47.2)	*(48.3)*	*(49.7)*	*(52.4)*
13. External Public Sector Debt	67,476	66,411	64,124	58,074
	(16.5)	*(16.0)*	*(14.8)*	*(13.2)*
14. Total Public Sector Debt (12+13)	260,681	267,058	280,023	288,725
	(63.7)	*(64.3)*	*(64.5)*	*(65.6)*

[1] *By original maturity.*

Notes: *(i) Short-term: Up to 12 months; Medium-term: Over 1 year but less than 5 years; Long-term: 5 years and above.*
(ii) Figures in brackets are percentages to GDP.
(iii) Figures may not add up to totals due to rounding.

Source: Ministry of Finance and Economic Development.

Table 3.7: Public Sector External Debt by Interest Rate Mix (Per cent)

	Mar-13	Mar-14	Mar-15	Mar-16	Mar-17 *Provisional*
Fixed Rate	40.1	36.3	35.1	37.8	41.2
Floating Rate	57.3	61.4	62.6	60.0	57.2
Interest-Free	2.7	2.3	2.3	2.3	1.6

Notes: Figures may not add up to total due to rounding.

Source: Ministry of Finance and Economic Development.

3.5 Monetary Aggregates

The y-o-y growth in broad money liabilities (BML) remained sustained, despite the drop to 8.8 per cent in April 2017, from 9.0 per cent in April 2016. All the components of BML except time deposits contributed largely to money growth. The velocity of circulation of broad money remained stable at around 1.0 over the past year (Table 3.8).

The annual growth rate in net foreign assets (NFA) of depository corporations (DCs) recovered from negative 7.4 per cent in April 2016 to 5.0 per cent in April 2017, led by improvements in both of its components (Table 3.9). NFA of other depository corporations (ODCs) recovered from negative growth of 14.2 per cent in April 2016 to 1.0 per cent in April 2017, while the NFA of the Bank of Mauritius registered an annual growth of 14.4 per cent, reflecting the Bank's active foreign exchange intervention on the domestic market.

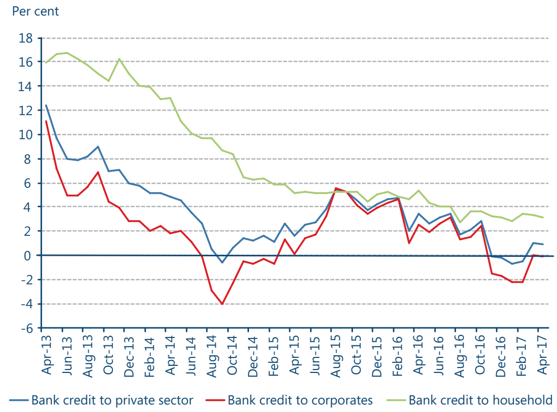
Y-o-y domestic claims of DCs went up from 5.9 per cent in April 2016 to 9.7 per cent in April 2017. Net claims on central government rose from Rs48.8 billion at end-April 2016 to Rs59.6 billion at end-April 2017. On the other hand, claims on other sectors, which comprised mostly of credit to private sector, increased by 8.3 per cent, from Rs431.1 billion to Rs467.0 billion over the same period.

The monetary base posted robust growth in April 2017, reflective somewhat of the build-up in rupee excess liquidity in the banking sector. The monetary base recorded an expansion of 24.4 per cent y-o-y in April 2017, as against a contraction of 10.3 per cent in April 2016. Year on year, liabilities to ODCs, one of the major components of monetary base, accelerated by 37.0 per cent in April 2017, from negative growth of 20.1 per cent in April 2016. The broad money multiplier dropped to 5.8 in April 2017, from 6.6 in April 2016.

3.6 Credit Developments

Bank credit to the private sector (excluding GBCs) reduced pace compared to the previous year. The annual growth rate of bank credit to the private sector (excluding GBCs) stood at 0.9 per cent in April 2017, down from 3.4 per cent in April 2016 (Chart 3.6). The drop in the annual growth rate emanated from a slowdown in corporate credit,

Chart 3.6 Y-o-y Growth in Bank Credit to Private Sector[1]



[1] *Excludes loans to GBC entities.*

Chart 3.7 Weighted Average Rupee Lending Rate by Sector

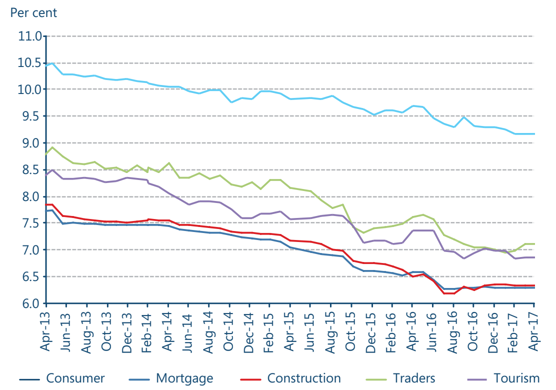
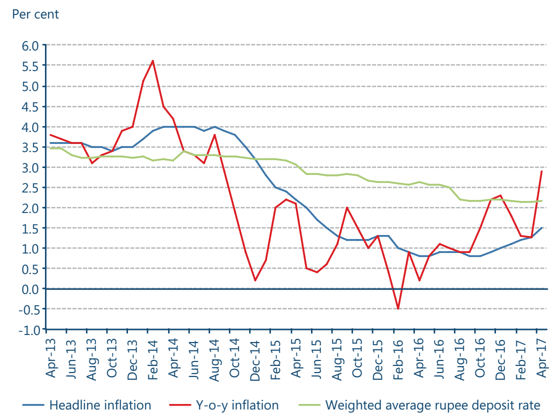


Chart 3.8 Inflation and Weighted Average Rupee Deposit Rate



which contracted by 0.1 per cent in April 2017. With the exception of a marginal improvement in March 2017, corporate credit growth has

Table 3.8: Depository Corporations Survey*, 2013-2017 [1]

	2013	2014	2015	2016 Mar	2016 Jun	2016 Sep	2016 Dec	Apr-17
	(Rs million)							
Net Foreign Assets	**396,299.9**	**457,823.2**	**529,025.5**	**507,495.6**	**529,764.9**	**541,173.8**	**549,150.7**	**551,541.8**
BOM (net)	103,497.9	122,735.5	151,519.5	157,406.7	166,725.9	169,580.8	177,668.6	179,152.6
ODCs (net)	292,802.0	335,087.7	377,506.1	350,088.9	363,039.0	371,593.0	371,482.1	372,389.2
Domestic Claims	**448,174.6**	**446,806.1**	**476,652.6**	**482,473.1**	**485,682.3**	**492,756.7**	**493,257.7**	**526,534.9**
Net Claims on Central Government	**34,759.0**	**44,771.5**	**41,980.5**	**47,471.8**	**48,559.1**	**52,695.1**	**54,205.3**	**59,555.1**
Claims on Central Government	65,605.5	78,031.4	83,459.8	89,542.7	94,349.5	98,954.6	100,984.1	110,707.1
Liabilities to Central Government	-30,846.5	-33,259.9	-41,479.3	-42,070.9	-45,790.4	-46,259.5	-46,778.8	-51,152.0
Claims on Other Sectors	**413,415.5**	**402,034.6**	**434,672.1**	**435,001.3**	**437,123.2**	**440,061.6**	**439,052.4**	**466,979.7**
of which loans to various sectors of the economy	**336,942.4**	**350,895.8**	**379,160.1**	**377,393.3**	**379,785.3**	**386,226.3**	**385,302.8**	**394,347.9**
Other items (net)	**-205,643.5**	**-193,481.8**	**-220,659.7**	**-227,440.4**	**-228,039.7**	**-221,805.8**	**-225,115.9**	**-244,202.9**
o/w Shares & equity	-137,324.9	-143,257.8	-170,609.6	-168,102.1	-168,868.7	-169,538.6	-171,014.6	-172,781.2
financial derivaties	-48,880.6	-24,875.9	-26,324.6	-31,338.6	-24,269.8	-28,631.5	-30,683.1	-49,009.8
Broad Money Liabilities	**365,608.7**	**397,556.5**	**437,998.6**	**442,449.9**	**454,966.2**	**461,720.5**	**477,788.9**	**486,422.5**
Currency Outside Depository Corporations	23,316.7	25,391.2	27,637.6	26,183.7	26,254.0	26,679.6	29,731.3	28,264.1
Transferable Deposits	80,391.4	92,719.2	107,987.4	110,751.6	116,495.9	117,359.1	122,416.8	127,498.1
Savings Deposits	137,028.6	151,721.3	171,829.5	177,427.0	182,445.8	187,659.0	196,181.0	200,961.2
Time Deposits	121,803.1	124,366.9	126,016.4	122,824.9	124,361.8	124,477.9	123,766.6	123,884.1
Securities other than Shares	3,069.0	3,358.0	4,527.8	5,262.6	5,408.7	5,544.9	5,693.2	5,815.0
GBC deposits	**273,222.3**	**313,590.9**	**347,019.8**	**320,078.4**	**332,441.3**	**350,404.2**	**339,503.5**	**347,451.3**
	(Average annual growth rates; in Per cent)							
Net Foreign Assets	**-1.3**	**15.5**	**15.6**	**-9.0**	**1.9**	**7.0**	**3.8**	**5.0**
BOM (net)	13.0	18.6	23.5	13.2	20.3	17.4	17.3	14.4
ODCs (net)	-5.5	14.4	12.7	-16.4	-4.8	2.8	-1.6	1.0
Domestic Claims	**14.6**	**-0.3**	**6.7**	**4.4**	**5.4**	**4.8**	**3.5**	**9.7**
Net Claims on Central Government	**29.9**	**28.8**	**-6.2**	**15.3**	**4.5**	**20.6**	**29.1**	**21.9**
Claims on Central Government	7.1	18.9	7.0	17.6	18.4	20.7	21.0	19.3
Liabilities to Central Government	-10.6	7.8	24.7	20.4	38.0	20.8	12.8	16.5
Claims on Other Sectors	**13.5**	**-2.8**	**8.1**	**3.4**	**5.5**	**3.2**	**1.0**	**8.3**
of which Loans to various sectors of the economy	**10.1**	**4.1**	**8.1**	**4.0**	**4.6**	**3.8**	**1.6**	**4.7**
Other items (net)	**16.4**	**-5.9**	**14.0**	**2.6**	**7.6**	**1.7**	**2.0**	**9.5**
o/w Shares & equity	2.1	4.3	19.1	2.3	1.8	1.6	0.2	3.1
financial derivaties	44.1	-49.1	5.8	3.9	-0.4	6.1	16.6	82.5
Broad Money Liabilities	**5.8**	**8.7**	**10.2**	**7.7**	**8.7**	**8.9**	**9.1**	**8.8**
GBC deposits	**1.2**	**14.8**	**10.7**	**-17.4**	**-5.1**	**4.8**	**-2.2**	**3.6**
Memo items:								
Nominal GDP (market prices)	**372,397.0**	**392,062.0**	**409,524.0**	**434,188.0**	**434,188.0**	**434,188.0**	**434,188.0**	**459,841.0**
BML + GBC deposits	**638,831.0**	**711,147.5**	**785,018.4**	**762,528.3**	**787,407.5**	**812,124.7**	**817,292.4**	**833,873.8**
Velocity of Broad money (BM)	1.1	1.0	1.0	1.0	1.0	1.0	0.9	1.0
Velocity of BM plus GBC	0.6	0.6	0.5	0.6	0.6	0.6	0.5	0.6
Velocity of Narrow Money Liabilities(NML)	5.3	5.0	4.7	4.9	4.8	4.7	4.6	4.7
Money multiplier	5.9	5.9	6.0	6.4	6.5	6.3	5.8	5.8

* *Includes the accounts of Banks and Non-bank deposit taking institutions.*
[1] *Data is up to April 2017.*

Table 3.9: Bank of Mauritius Balance Sheet, 2013-2017[1]

	2013	2014	2015	2016 Mar	2016 Jun	2016 Sep	2016 Dec	Apr-17
	(Rs million)							
Net Foreign Assets	**103,497.9**	**122,735.5**	**151,519.5**	**157,406.7**	**166,725.9**	**169,580.8**	**177,668.6**	**179,152.6**
Net Domestic Claims	**-24,504.0**	**-31,099.7**	**-48,724.2**	**-53,838.2**	**-60,482.2**	**-62,150.4**	**-61,241.9**	**-60,646.1**
Claims on ODCs	2,715.7	2,467.9	1,056.7	1,011.9	867.0	902.9	884.5	777.7
Net Claims on Central Government 1	-6,903.8	-16,238.5	-21,718.4	-25,081.8	-29,552.8	-30,781.3	-31,222.4	-31,710.0
Claims on Other Sectors	172.7	152.2	3,668.5	3,623.0	3,760.7	3,762.3	3,786.1	3,761.3
Other items (net)	-20,488.5	-17,481.4	-31,731.1	-33,391.4	-35,557.0	-36,034.2	-34,690.1	-33,475.2
Monetary Base	**62,350.0**	**67,933.6**	**73,569.0**	**69,446.0**	**70,419.8**	**73,083.8**	**82,062.5**	**83,832.7**
Currency in circulation	30,127.7	32,530.9	33,337.4	30,743.3	30,580.8	31,412.2	35,918.4	33,183.7
Liabilities to ODCs	32,222.4	35,402.7	40,231.7	38,702.7	39,839.0	41,671.6	46,144.1	50,649.1
BoM securities	**16,644.0**	**23,702.2**	**29,226.2**	**34,122.5**	**35,823.9**	**34,346.6**	**34,364.2**	**34,673.8**
Held by banks	10,796.4	17,219.3	19,286.0	23,507.9	25,600.9	23,208.8	23,108.4	22,662.1
Held by Social Security Funds	4,028.9	4,505.0	6,916.5	6,876.9	6,360.6	7,160.7	7,164.2	7,836.2
Other holders	1,818.7	1,977.8	3,023.8	3,737.6	3,862.4	3,977.1	4,091.6	4,175.4
	(Contribution to Monetary Base growth; in Per cent)							
Net Foreign Assets	**22.7**	**30.9**	**42.4**	**24.9**	**39.2**	**37.5**	**35.5**	**33.5**
Net Domestic Assets/Claims	**15.0**	**-10.6**	**-25.9**	**-10.2**	**-28.2**	**-23.4**	**-17.0**	**-8.3**
Claims on ODCs	1.7	-0.4	-2.1	-1.9	-1.6	-0.6	-0.2	-0.4
Net Claims on Central Government	5.4	-15.0	-8.1	-8.1	-19.1	-15.5	-12.9	-6.1
Claims on Other Sectors	0.0	0.0	5.2	4.8	0.1	0.1	0.2	0.2
Other items (net)	8.0	4.8	-21.0	-4.9	-7.6	-7.4	-4.0	-1.9
Monetary Base	**18.5**	**9.0**	**8.3**	**-5.6**	**-1.6**	**9.2**	**11.5**	**24.4**
Currency in circulation	6.0	3.9	1.2	3.4	3.0	3.9	3.5	4.1
Liabilities to ODCs	12.5	5.1	7.1	-9.0	-4.7	5.3	8.0	20.3
BoM securities	**-19.2**	**-11.3**	**-8.1**	**-20.4**	**-12.7**	**-5.0**	**-7.0**	**-0.8**
Held by banks	-13.1	-10.3	-3.0	-16.0	-9.3	-2.1	-5.2	1.0
Held by Social Security Funds	-4.3	-0.8	-3.5	-3.4	-0.7	-1.1	-0.3	-1.3
Other holders	-1.8	-0.3	-1.5	-1.0	-2.6	-1.8	-1.5	-0.5
	(Annual growth rate; in Per cent)							
Net Foreign Assets	**13.0**	**18.6**	**23.5**	**13.2**	**20.3**	**17.4**	**17.3**	**14.4**
Net Domestic Assets/Claims	**-24.4**	**26.9**	**56.7**	**16.1**	**50.2**	**33.7**	**25.7**	**10.2**
Claims on ODCs	50.5	-9.1	-57.2	-58.6	-57.2	-30.9	-16.3	-27.1
Net Claims on Central Government	-29.0	135.2	33.7	31.1	86.2	50.9	43.8	15.0
Claims on Other Sectors	-6.4	-11.8	2,310.0	2,749.3	1.5	2.4	3.2	3.8
Other items (net)	-17.0	-14.7	81.5	12.1	18.0	16.0	9.3	4.0
Monetary Base	**18.5**	**9.0**	**8.3**	**-5.6**	**-1.6**	**9.2**	**11.5**	**24.4**
Currency in circulation	11.7	8.0	2.5	8.9	7.7	9.0	7.7	9.0
Liabilities to ODCs	25.6	9.9	13.6	-14.6	-7.8	9.3	14.7	37.0
BoM securities	**155.2**	**42.4**	**23.3**	**78.5**	**33.9**	**10.7**	**17.6**	**1.6**
Held by banks	175.7	59.5	12.0	100.5	35.3	6.4	19.8	-3.0
Held by Social Security Funds	130.8	11.8	53.5	57.4	8.8	11.3	3.6	12.7
Other holders	111.4	8.8	52.9	23.4	93.6	43.6	35.3	9.3
Memo item:								
End-period exchange rate (Rs/US$)	30.1	31.7	35.9	35.4	35.5	35.4	36.0	35.0

** Excludes BoM securities holdings by social security funds.*

[1] *Data is up to April 2017.*

remained negative since November 2016, mainly due to on-going deleveraging by certain operators in the tourism sector. The issue of bonds/debentures via private placements at the expense of bank borrowing also contributed to the slow growth in credit. Notwithstanding the credit contraction in the corporate sector, credit extended to households continued to grow during the period under review, bolstered by an increase in mortgage loans. Consumer credit contributed negatively to household credit growth throughout the period under review (Table 3.10).

3.7 Interest Rates

Banks' retail lending and deposit rates have dropped since last July in line with the reduction in the Key Repo Rate (KRR). Following the cut in KRR by 40 basis points in July 2016, financing conditions eased, as reflected by a drop in lending rates. Lending rates applicable to key sectors of the economy - construction, traders and tourism - fluctuated in the range of 6.2 per cent to 7.3 per cent between August 2016 and April 2017, compared to a higher range of 6.6 per cent to 7.9 per cent between August 2015 and April 2016 (Chart 3.7). The reduction in the KRR was also mirrored in the weighted average rupee deposit rate, which dropped from 2.62 per cent as at end-April 2016 to 2.16 per cent as at end-April 2017. Real interest rates on Rupee deposits have generally remained positive except in December 2016 and April 2017, when they were outpaced by y-o-y inflation (Chart 3.8). Banks' Savings Deposit Rates and Prime Lending Rates varied between 1.75-2.75 per cent and 6.00-8.50 per cent, respectively, compared to 1.75-4.00 per cent and 6.25-8.50 per cent, respectively, in the previous year.

Table 3.10: Bank Credit to Private Sector, 2011-2017[1]

						2016				2017
	2011	2012	2013	2014	2015	Mar	Jun	Sep	Dec	Apr
	(Average annual growth rates; in Per cent)									
Total credit to private sector	**8.3**	**12.8**	**5.9**	**1.3**	**4.2**	**2.1**	**3.1**	**2.1**	**-0.2**	**0.9**
Corporates	5.9	11.5	2.8	-0.7	3.9	1.0	2.7	1.5	-1.7	-0.1
Construction	11.5	32.1	10.9	3.4	4.0	-2.9	-2.2	-6.4	-6.4	-1.2
Tourism	6.6	4.1	8.8	-2.4	1.4	1.6	-0.2	0.2	-10.9	-15.9
Traders	19.2	9.0	-7.6	9.0	1.0	-0.6	3.4	-4.0	-5.6	-0.2
Financial services	2.8	5.9	5.4	-7.0	6.8	-5.6	6.3	8.3	21.9	32.9
Manufacturing	1.7	3.6	2.2	-2.2	12.0	3.5	7.7	7.1	-3.9	-5.1
Agriculture & Fishing	11.5	12.0	5.0	0.7	12.1	20.1	10.7	13.7	-0.7	0.0
Other	-10.8	23.3	-7.4	-6.7	-4.5	-2.4	-0.6	0.1	4.2	1.2
Households	16.4	16.6	15.0	6.2	5.0	4.6	4.1	3.7	3.2	3.1
Personal credit	7.6	14.1	21.3	2.1	-2.1	-2.0	-1.9	-1.2	-1.4	-1.9
Mortgages	22.6	18.3	11.1	8.9	9.4	8.6	7.6	6.4	5.7	5.9
	(Contribution to growth of total credit to private sector; in Per cent)									
Total credit to private sector	**8.3**	**12.8**	**5.9**	**1.3**	**4.2**	**2.1**	**3.1**	**2.1**	**-0.2**	**0.9**
Corporates[2]	4.5	8.6	2.1	-0.5	2.7	0.7	1.9	1.1	-1.2	0.0
Construction	1.0	2.9	1.1	0.4	0.4	-0.3	-0.3	-0.7	-0.7	-0.1
Tourism	1.3	0.8	1.5	-0.4	0.2	0.3	0.0	0.0	-1.8	-2.6
Traders	2.2	1.1	-0.9	1.0	0.1	-0.1	0.4	-0.4	-0.6	0.0
Financial services	0.3	0.6	0.5	-0.7	0.6	-0.6	0.6	0.8	2.0	3.0
Manufacturing	0.1	0.3	0.2	-0.2	0.8	0.3	0.6	0.5	-0.3	-0.4
Agriculture & Fishing	0.8	0.9	0.4	0.0	0.8	1.3	0.7	0.9	-0.1	0.0
Other	-1.2	2.1	-0.7	-0.6	-0.4	-0.2	0.0	0.0	0.3	0.1
Households	3.8	4.1	3.9	1.7	1.5	1.3	1.2	1.1	0.9	0.9
Personal credit	0.7	1.4	2.1	0.2	-0.2	-0.2	-0.2	-0.1	-0.2	-0.2
Mortgages	3.1	2.8	1.8	1.5	1.7	1.6	1.4	1.2	1.1	1.1

[1] *Data is up to April 2017.*

[2] *Includes Public Corporations.*

3.8 Excess Liquidity and Yield Curves

The Bank has been striving to bring down banks' excess reserves to a tolerable level. Besides Government issuing its own securities, the Bank has had recourse to the issue of its own papers and to the conduct of sterilised foreign exchange intervention. Rupee excess reserves peaked at Rs17.8 billion on 26 January 2017 (Chart 3.9). Banks' excess reserves accumulated significantly at the end of 2016 and early 2017, reflecting in part the usual end-of-year build-up as a result of the payment of bonuses but also due to net maturing securities and unsterilised intervention by the Bank. Subsequently, the Bank stepped in aggressively to issue its own instruments to lower the level of excess reserves, which dropped to Rs2.7 billion on 02 April 2017. Thereafter, excess reserves started picking up again to reach Rs10.7 billion by the end of April 2017, mainly due to the Bank's unsterilized intervention of Rs4.1 billion on 26 April 2017. As at close of business on 28 April 2017, total outstanding amount of instruments issued for liquidity management purposes stood at Rs64.5 billion, of which an amount of Rs34.8 billion of Bank of Mauritius securities were issued; Special Deposits totalling Rs11.2 billion and Rs18.5 billion of Treasury Bills were also issued for liquidity management purposes (Chart 3.10).

The level of excess liquidity prevailing in the banking system impacted on the movements of short-term interest rates (Chart 3.11). The gap between the KRR and key short-term interest rates (i.e., the yields on Treasury Bills and the interbank money market rate) started to widen since December 2016. The overall weighted yields on Treasury Bills decreased from 2.87 per cent in December 2016 to 2.75 per cent in April 2017, while the weighted average interbank rates fell from 1.52 per cent to 1.09 per cent. The drop in short-term interest rates has coincided with a period of sizeable intervention by the Bank on the domestic foreign exchange markets that led to an increase in official reserves from US$4,967 million as at end-December 2016 to about US$5,145 million as at end-April 2017 (Chart 3.12).

Chart 3.9 Banks' Excess Liquidity and CRR

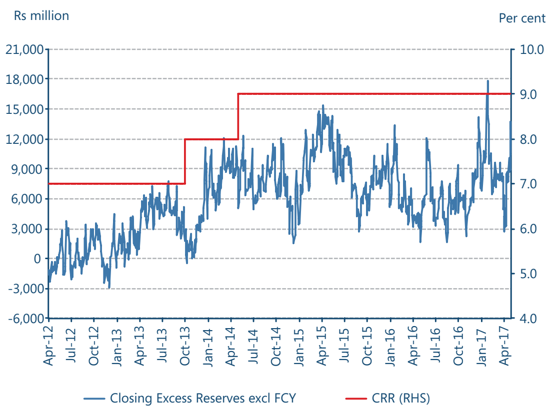


Chart 3.10 Outstanding BOM Securities

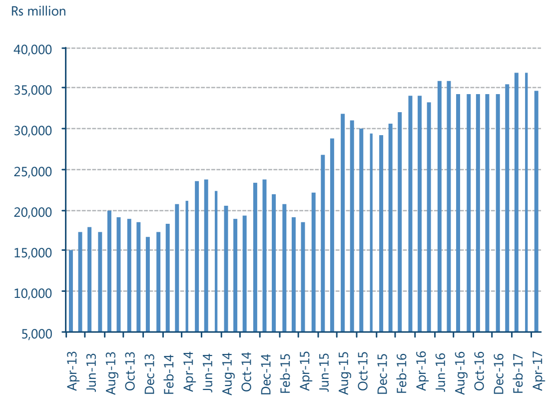
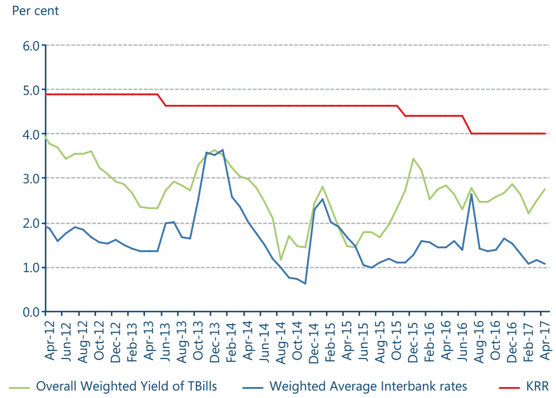


Chart 3.11 KRR, Money Market and Interbank Interest Rates



3.9 Exchange Rate Developments

The rupee remained influenced by movements of major currencies on the international markets and by domestic demand and supply conditions. Notwithstanding the Bank's efforts on the domestic foreign exchange market, the rupee on a nominal effective exchange rate basis appreciated somewhat, reflecting capital inflows in the economy. On a point-to-point weighted average dealt rate basis, between November 2016 and April 2017, the rupee appreciated against the euro and the US dollar but depreciated slightly against the Pound sterling. The currency-weighted nominal exchange rate (MERI1) was broadly stable in recent months (Chart 3.13). The Bank will maintain its vigilance on risks emanating from global economic and financial uncertainty and strive to ensure that the rupee reflects domestic economic fundamentals.

3.10 Domestic Stock Market

The surge in the domestic stock market index, which became more entrenched by end-2016 and early 2017, corroborated with the rally in global equity markets and growing optimism on the economic outlook, both domestic and international. The SEMDEX, which was at a three-and-a-half-year low of 1,744 in May 2016, gained support as investors grew increasingly optimistic amid measures announced in the 2016-17 Budget Speech presented in June 2016. Nonetheless, this optimism was short-lived and the domestic stock market was somewhat flustered with uncertainty. Subsequently, the SEMDEX recouped its losses and rose to about 1,981 in April 2017. The surge in the domestic stock market corroborated with the rally in global equities, notwithstanding prevalent global economic uncertainty. The SEM-10, comprising the 10 most capitalised stocks on the Official Market, closely tracked the movements of the SEMDEX.

Net sales by non-residents slowed somewhat to Rs1,870 million for the year ended April 2017, from Rs2,503 million for the year ended April 2016 (Chart 3.15). As a result, holdings by non-residents fell to about 10.3 per cent of total market capitalisation at the end of April 2017, from 12.6 per cent at the end of April 2016.

Chart 3.12 **BoM Forex Intervention and MERI1**

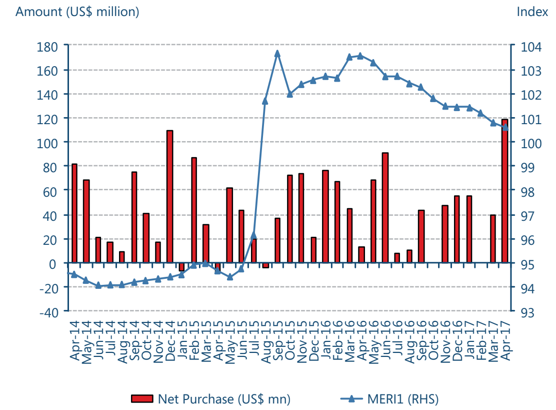
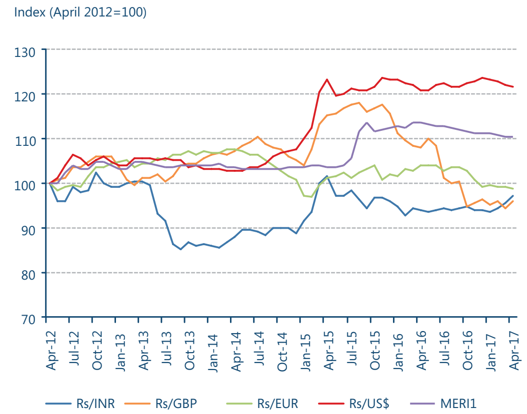
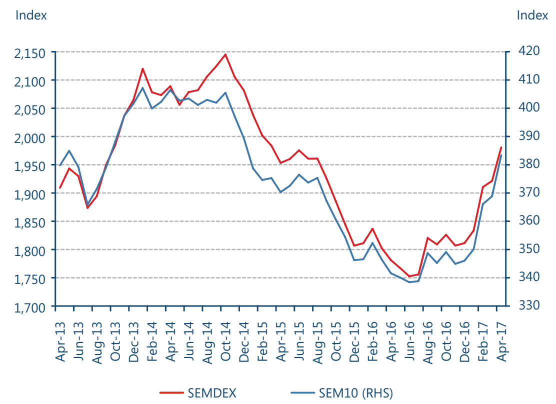


Chart 3.13 **Evolution of the Rupee and MERI1**



Note: The MERI1 is based on the currency distribution of merchandise trade and services, excluding transactions in Rupees.

Chart 3.14 **Evolution of SEMDEX and SEM-10**



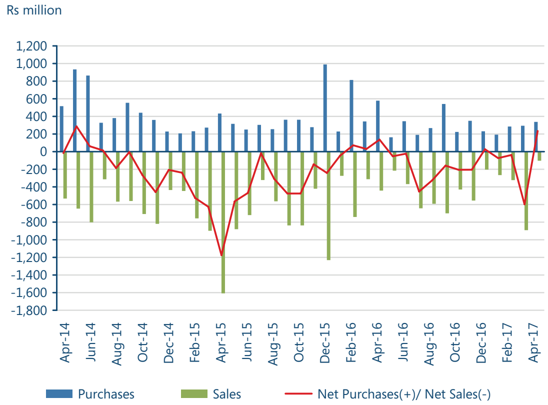
Note: SEM-10 replaced the SEM-7 index as from 2nd October 2014.

Source: The Stock Exchange of Mauritius Ltd.

3.11 Saving-Investment Balance

Investment as a share of GDP continued to decline in 2016 and remained at a historically low level. The drop in the investment-to-GDP ratio in the last three years has been mainly due to contraction in private investment, while growth in public investment remained sluggish. The decline in private investment reflected, among other factors, the weak external demand and a high level of corporate indebtedness that continues to restrict businesses' ability to undertake new investment. The Incremental Capital Output Ratio (ICOR), measured as the ratio of GDFCF to GDP divided by the GDP growth rate, has decreased substantially since 2012 (Chart 3.16). For the period 2009 to 2016, the estimated median ICOR of 5.6 per cent was marginally higher than the historical median of 5.5 per cent.

Chart 3.15 Investment by Non-Residents on the SEM



Source: The Stock Exchange of Mauritius Ltd.

Table 3.11: Saving-Investment Balance

	2014	2015	2016	2017*
	(Rs million)			
Investment	**73,989**	**71,155**	**74,747**	**82,400**
Private (GDFCF)	55,048	51,735	55,576	58,735
Public	18,941	19,420	19,171	23,665
Change in inventories	3,152	2,999	-2,048	-1,258
Savings	73,989	71,155	74,747	82,400
External	21,824	20,472	18,881	20,296
Domestic	52,165	50,683	55,866	62,104
Private	55,598	57,437	68,393	n.a.
Public	-3,433	-6,754	-12,527	n.a.
Investment *(in per cent of GDP)*	**18.9**	**17.4**	**17.2**	**17.9**
Private (GDFCF)	14.0	12.6	12.8	12.8
Public	4.8	4.7	4.4	5.1
Change in inventories	0.8	0.7	-0.5	-0.3
Savings *(in per cent of GDP)*	**18.9**	**17.4**	**17.2**	**17.9**
External (with global business)	5.6	5.0	4.3	4.4
Domestic	13.3	12.4	12.9	13.5
Private	14.2	14.0	15.8	n.a.
Public	-0.9	-1.6	-2.9	n.a.
Savings *(in per cent of GDP)*	**19.2**	**17.4**	**17.2**	**17.9**
External (with global business)	5.7	5.0	4.3	4.4
Domestic	13.5	12.4	12.9	13.5
Private	14.4	14.0	15.8	n.a.
Public	-0.9	-1.7	-2.9	n.a.
Memo item:				
CY GDP (millions of Rs)	392,062	409,524	434,188	459,841
CY GNDI	385,321	409,227	434,215	461,592

** Forecast.*

Sources: Statistics Mauritius and Bank of Mauritius estimates.

Mauritius' recourse to external savings is expected to have declined in 2016 (Table 3.11). The external current account deficit is projected to have narrowed from 5.0 per cent of GDP in 2015 to 4.3 per cent of GDP in 2016. The decline in the current account deficit reflected a lower trade deficit than in 2015, amid falling global commodity prices. The current account deficit continued to be largely financed by net Foreign Direct Investment (FDI) flows and portfolio investment from GBCs. During 2016, the Bank accumulated gross international reserves of nearly US$5 billion. Reserve import coverage by end of 2016 was equivalent to 9 months of imports of goods and services.

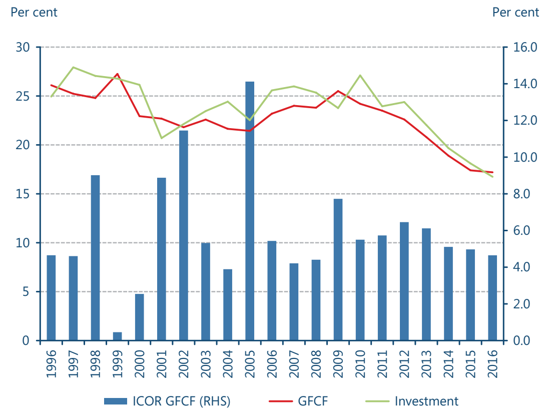
3.12 Balance of Payments

Terms of Trade Developments

The country's terms of trade improved from 112.8 in 2015 to 120.3 in 2016, thanks to lower global commodity prices (Table 3.12). The export price index (EPI) rose from 96.9 in 2015 to 98.0 in 2016 due to higher 'Sugar' export prices while the import price index decreased from 85.9 to 81.5 on account of lower 'Mineral fuel' and 'Manufacturing' import prices. However, dynamics from quarterly data point to a worsening of the terms of trade in 2016Q4 compared to 2015Q4. Lower 'Apparel & clothing' and 'Other export' export prices more than offset the higher 'Sugar' and 'Fish' export prices, thereby resulting in a slightly lower EPI in 2016Q4 compared to 2015Q4. A rebound in 'Mineral fuel' import prices and higher 'Machinery and transport equipment' import prices led to a noticeable rise in IPI in 2016Q4 compared to 2015Q4. Looking ahead, with stabilization in commodity prices, oil prices trading in the range of US$50-55 barrel and 'Machinery and transport equipment' remaining elevated on the import side, and apparel and other manufacturing export prices remaining pressured on the export side, the terms of trade could be expected to deteriorate in 2017, thus weighing on the current account balance of the country.

The current account deficit is projected to have improved in 2016 despite a worsening of the

Chart 3.16 Gross Fixed Capital Formation, Investment[1] and ICOR



[1] *Investment is GFCF plus net change in inventories.*

Sources: Statistics Mauritius and Bank of Mauritius staff estimates.

Table 3.12: International Terms of Trade (Index: 2013 =100)

	Weights	2014	2015	2016	2015Q4	2016Q4
Export price index	**1.0000**	**95.8**	**96.9**	**98.0**	**99.6**	**99.0**
Apparel & clothing	0.4236	101.1	111.0	111.7	114.3	108.6
Sugar	0.2033	88.4	79.7	84.7	81.9	87.7
Fish	0.2454	90.7	83.1	81.8	85.4	90.2
Other exports	0.1277	99.6	103.8	105.0	106.3	102.1
Import price index	**1.0000**	**96.4**	**85.9**	**81.5**	**81.6**	**84.2**
Food	0.2511	97.3	93.7	93.9	90.3	89.8
Mineral Fuels	0.3996	92.7	64.5	53.2	56.3	60.7
Manufacturing	0.1116	99.0	108.1	102.2	106.3	101.5
Machinery and Transport Equipment	0.0887	99.8	101.0	108.1	101.6	115.1
Other	0.1490	101.0	104.5	105.1	104.4	106.4
Terms of trade		**99.3**	**112.8**	**120.3**	**122.1**	**117.6**

Note: Figures may not add up to total due to rounding.

Source: Ministry of Finance and Economic Development.

goods account, thanks to a higher surplus on the services and income accounts. Preliminary estimates indicate a narrowing of the current account deficit from Rs20.5 billion in 2015 to Rs18.9 billion in 2016 (Table 3.13). As a percentage of GDP, the current account deficit fell from 5.0 per cent in 2015 to 4.3 per cent in 2016. The increase in the deficit on the goods account, from Rs65.4 billion in 2015 to Rs72.8 billion in 2016, emanated from the larger nominal decline in the value of exports relative to the value of imports. Exports declined by 10.1 per cent in 2016 to Rs83.9 billion, driven by all of its three components, notably 'ship's stores and bunkers' which fell by 20.3 per cent; re-exports which dropped by 18.1 per cent and domestic exports which declined by 5.2 per cent. Imports (f.o.b) fell by 1.3 per cent to Rs156.6 billion in 2016, mainly on account of lower import value of 'Mineral fuels, lubricants, and related products'. The surplus on the services account widened to Rs28.5 billion in 2016, supported by a buoyant tourism sector. The income account is expected to have recorded a higher surplus of Rs33.6 billion in 2016 while current transfers registered a higher deficit of Rs8.2 billion.

Capital and financial flows during 2016 were more than adequate to finance the current account deficit, resulting in an overall balance of payments surplus of Rs26.2 billion, higher than the increase of Rs20.0 billion recorded in 2015. Direct investment posted net inflows of Rs461.9 billion

Table 3.13: Balance of Payments, 2014-2017

	2014	2015 [1]	2016 [2]	2017 [3]
	(Rs million)			
Current account	**-21,824**	**-20,472**	**-18,881**	**-22,071**
Goods balance	-69,394	-65,398	-72,782	-81,517
Services balance	21,154	21,095	28,496	28,817
Income balance	32,867	31,748	33,648	35,582
o/w GBC1s	38,339	31,624	32,515	31,094
Current transfers	-6,451	-7,917	-8,243	-4,953
Capital and Financial account	**18,586**	**17,871**	**24,014**	**22,071**
Capital account	-146	-136	-36	-224
Financial account	18,732	18,007	24,050	22,295
Direct investment	16,845	11,708	461,949	366,275
Portfolio investment	-13,025	-24,642	-238,040	-195,650
Other investment	*37,931*	*50,900*	*-173,632*	*-134,668*
o/w Banks	*-42,348*	*-9,839*	*461*	*-6,284*
Reserve assets	*-23,019*	*-19,960*	*-26,227*	*-13,662*
Net errors and omissions	**3,238**	**2,601**	**-5,132**	**0**
	(Per cent of GDP)			
Current account	**-5.6**	**-5.0**	**-4.3**	**-4.8**
Goods balance	-17.7	-16.0	-16.8	-17.7
Services balance	5.4	5.2	6.6	6.3
Income balance	8.4	7.8	7.7	7.7
o/w GBC1s	*9.8*	*7.7*	*7.5*	*6.8*
Current transfers	-1.6	-1.9	-1.9	-1.1
Capital and Financial account	**4.7**	**4.4**	**5.5**	**4.8**
Capital account	0.0	0.0	0.0	0.0
Financial account	4.8	4.4	5.5	4.8
Direct investment	4.3	2.9	106.4	79.7
Portfolio investment	-3.3	-6.0	-54.8	-42.5
Other investment	*9.7*	*12.4*	*-40.0*	*-29.3*
o/w Banks	-10.8	-2.4	0.1	-1.4
Reserve assets	-5.9	-4.9	-6.0	-3.0
Net errors and omissions	**0.8**	**0.6**	**-1.2**	**0.0**

[1] Revised. *[2] Partially revised estimates.* *[3] Forecast.*

in 2016, which were amply sufficient to offset the respective net outflows of Rs238.0 billion and Rs173.6 billion recorded on the portfolio and other investment accounts (Chart 3.17).

The current account deficit has been projected at Rs22.1 billion, representing about 4.8 per cent of GDP in 2017, mainly on account of a deterioration of the balance of trade. Nonetheless, capital and financial flows in 2017 are expected to be more than adequate to finance the current account deficit. The capital and financial account, inclusive of reserve assets, is estimated to record net inflows of Rs22.1 billion in 2017. An overall balance of payments surplus of Rs13.7 billion is projected for 2017.

At the end of April 2017, the gross official international reserves of the country rose to

Chart 3.17 Financing of the Current Account

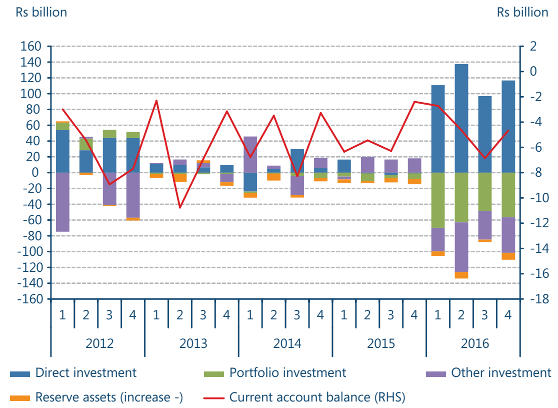


Table 3.14: Exports and Imports by SITC

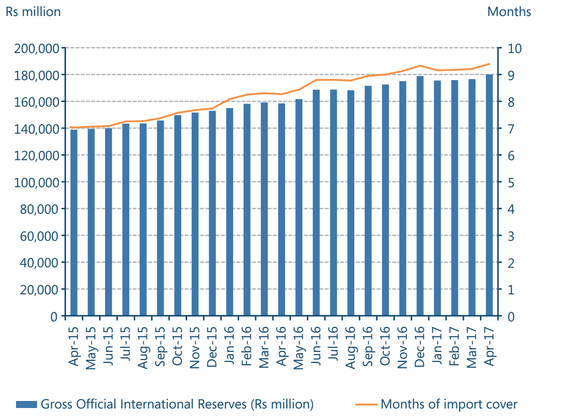
	2015			2016			Growth rate (Year-on-Year)		
	Q3	Q4	Semester 2	Q3	Q4	Semester 2	Q3	Q4	Semester 2
	(Rs million)						(Per cent)		
Total Exports (f.o.b.)	**23,706**	**22,349**	**46,055**	**20,792**	**20,906**	**41,698**	**- 12.3**	**- 6.5**	**- 9.5**
Domestic exports	15,276	15,583	30,859	13,855	13,954	27,809	- 9.3	- 10.5	- 9.9
Re-exports	6,780	4,866	11,646	5,362	5,247	10,609	- 20.9	7.8	- 8.9
Of which: Freeport re-exports	5,380	3,820	9,200	4,060	4,026	8,086	- 24.5	5.4	- 12.1
Ship's Stores and Bunkers	1,650	1,900	3,550	1,575	1,705	3,280	- 4.5	- 10.3	- 7.6
Exports by section									
Food and live animals	6,422	6,408	12,830	6,588	7,639	14,227	2.6	19.2	10.9
Machinery and transport equipment	3,270	972	4,242	1,730	765	2,495	- 47.1	- 21.3	- 41.2
Miscellaneous manufactured goods	8,815	8,961	17,776	7,748	7,334	15,082	- 12.1	- 18.2	- 15.2
of which: Articles of apparel & clothing accessories	7,062	6,897	13,959	6,191	5,853	12,044	- 12.3	- 15.1	- 13.7
Manufactured goods classified chiefly by material	2,197	2,199	4,396	1,602	1,650	3,252	- 27.1	- 25.0	- 26.0

	2015			2016			Growth rate (Year-on-Year)		
	Q3	Q4	Semester 2	Q3	Q4	Semester 2	Q3	Q4	Semester 2
	(Rs million)						(Per cent)		
Total Imports (c.i.f)	**41,973**	**44,352**	**86,325**	**41,889**	**45,934**	**87,823**	**- 0.2**	**3.6**	**1.7**
Freeport imports	5,305	3,549	8,854	3,160	3,602	6,762	- 40.4	1.5	- 23.6
Other imports	36,668	40,803	77,471	38,729	42,332	81,061	5.6	3.7	4.6
Imports by section									
Food and live animals	8,669	9,196	17,865	9,510	8,981	18,491	9.7	- 2.3	3.5
Mineral fuels, lubricants, & related products	5,812	6,246	12,058	5,266	7,503	12,769	- 9.4	20.1	5.9
Machinery & transport equipment	9,518	10,044	19,562	9,961	11,244	21,205	4.7	11.9	8.4
Miscellaneous manufactured articles	3,719	4,605	8,324	3,810	4,978	8,788	2.4	8.1	5.6
Manufactured goods classified chiefly by material	7,733	7,499	15,232	6,836	6,663	13,499	- 11.6	- 11.1	- 11.4

Source: Statistics Mauritius.

Rs180 billion or an equivalent of USD5,145 million despite Government having effected the early repayment of an external debt obligation in January 2017. Based on the value of imports of goods (f.o.b.) and non-factor services for the year 2016, these reserves represented an import cover of 9.4 months, higher by about 1.1 months compared to end-April 2016 (Chart 3.18). Such a level of foreign reserves provides the country with a comfortable buffer to withstand potential external shocks.

Chart 3.18 **Gross Official International Reserves and Import Cover**



3.13 Selected External Vulnerability Indicators

External vulnerability indicators improved somewhat during 2017Q1, mainly as a result of lower gross external debt and rising gross international reserves (Table 3.15). The gross external debt of the country declined to Rs87.2 billion as at end-March 2017, representing about 19.8 per cent of GDP, compared to Rs94.2 billion as at end-December 2016, and equivalent to 21.7 per cent of GDP. The ratio of gross external debt to GDP declined to its lowest rate since end-December 2011. The fall in gross external

Table 3.15: External Debt Indicators, December 2012 to March 2017

		Dec-12	Dec-13	Dec-14	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17
		(Rs million)								
Gross External Debt [1]	as at end	79,881	88,974	94,678	99,424	98,189	96,886	96,895	94,211	87,211
External Debt Service [1]	year ended	6,896	9,847	9,331	7,820	7,761	7,042	6,418	7,782	12,194
Exports of Goods	year ended	79,658	88,049	94,776	93,290	91,828	88,208	85,294	83,851	82,590
Exports of Goods and Services	year ended	181,871	173,232	192,497	192,925	192,957	187,928	185,372	185,760	184,192
Imports of Goods and Services	year ended	226,846	225,493	240,737	237,228	233,768	229,735	229,458	230,046	235,458
Gross Official International Reserves [2]	as at end	92,988	105,009	124,344	152,902	159,175	168,679	171,563	178,858	176,570
GDP at market prices	year ended	350,644	372,397	392,062	409,524	415,530	421,677	427,498	434,188	440,447
Broad Money Liabilities	as at end	345,617	365,609	397,557	437,999	442,450	454,966	461,720	477,789	485,071
I. Solvency (Per cent)		**Dec-12**	**Dec-13**	**Dec-14**	**Dec-15**	**Mar-16**	**Jun-16**	**Sep-16**	**Dec-16**	**Mar-17**
Gross External Debt/GDP		22.8	23.9	24.1	24.3	23.6	23.0	22.7	21.7	19.8
Gross External Debt/Exports of Goods		100.3	101.1	99.9	106.6	106.9	109.8	113.7	112.4	105.6
Gross External Debt/Exports of Goods and Services		43.9	51.4	49.2	51.5	50.9	51.6	52.3	50.7	47.3
External Debt Service/Exports of Goods		8.7	11.2	9.8	8.4	8.5	8.0	7.5	9.3	14.8
External Debt Service/Exports of Goods and Services		3.8	5.7	4.8	4.1	4.0	3.7	3.5	4.2	6.6
II. Reserve Adequacy (Per cent)		**Dec-12**	**Dec-13**	**Dec-14**	**Dec-15**	**Mar-16**	**Jun-16**	**Sep-16**	**Dec-16**	**Mar-17**
Reserves/Imports of Goods and Services		41.0	46.6	51.7	64.5	68.1	73.4	74.8	77.7	75.0
Reserves/Broad Money Liabilities		26.9	28.7	31.3	34.9	36.0	37.1	37.2	37.4	36.4
Reserves/Gross External Debt		116.4	118.0	131.3	153.8	162.1	174.1	176.9	189.8	202.5

[1] *Gross external debt outstanding as at end of period excludes global business companies' and other deposit taking institutions' debts.*

[2] *Gross Official International Reserves as at end of period comprise gross foreign assets of the Bank of Mauritius, reserve position in the IMF and the foreign assets of Government.*

Sources: Statistics Mauritius, Ministry of Finance and Economic Development and Bank of Mauritius.

debt has been driven by net repayments of both private and public external debts as well as the early repayment of an external loan obligation by Government in January 2017. Reflecting the latter, external debt servicing rose to Rs12.2 billion as at end-March 2017. Gross official international reserves were over two times the level of gross external debt as at end March 2017, amounting to 202.5 per cent compared to 189.8 per cent as at end-December 2016 and 162.1 per cent a year earlier.

4. Inflation: Developments and Outlook

Headline inflation started rising from the end of 2016 but remained at low levels so far. Various other inflation measures were also contained at low levels and remained almost stable. Latest forecasts show that headline inflation would most likely settle below 3 per cent in 2017, barring exceptional shocks and conditional on specific assumptions.

4.1 Recent Trends

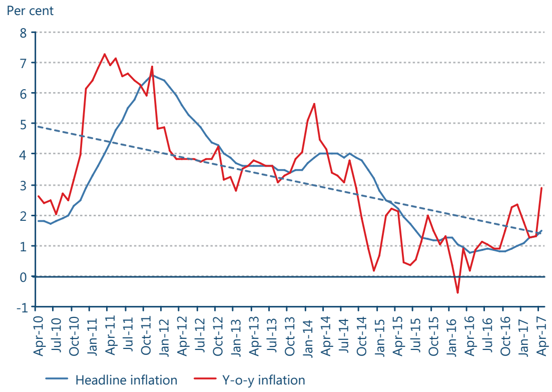
Notwithstanding its uptrend, domestic inflation remained contained at relatively low levels, reflecting somewhat subdued domestic demand conditions, stable rupee exchange rate, moderate global economic activity and the absence of major supply shocks. Headline inflation, as measured by the change in the average level of the consumer price index (CPI) during a twelve-month period, hovered within a narrow range of just under 1.0 per cent until November 2016 before trending upwards to reach 1.5 per cent in April 2017. The uptick in headline inflation reflected, amongst others, volatile vegetable prices since the beginning of the year as well as the rise in petroleum prices last February.

Year-on-year (y-o-y) inflation, however, showed contrasting paths as a result of the impact of vegetable prices, which were quite volatile during the first four months of 2017 base effects. Y-o-y inflation fluctuated within a narrow range of 0.2 per cent and 1.1 per cent in 2016Q3 before maintaining an upward momentum in the last quarter of 2016. Y-o-y inflation, thereafter, subsided to 1.8 per cent in January 2017 and further to 1.3 per cent in March 2017 on account of base effects (Chart 4.1) before picking up to 2.9 per cent in April 2017. The momentum of price changes, as indicated by the 3-month moving average seasonally adjusted nonetheless indicates that price pressures remained contained during the period under review (Chart 4.2).

Generally, the various other inflation measures also have moved on an uptrend since the beginning of 2017, but remained at moderate levels. Based on the year–on-year methodology, goods inflation rose from -0.1 per cent in April 2016 to 3.2 per cent in April 2017, reflecting amongst others, volatility in the price of vegetables and base effects. Services inflation rose from 0.9 per cent in April 2016 to 2.2 per cent in April 2017. CPIX_M inflation, which excludes mortgage payments in the CPI basket, mirrored more or less the path of y-o-y inflation. However, imported inflation is expected to have firmed up to 3.7 per cent in April 2017, from 0.6 per cent in April 2016, somewhat reflecting a pick-up of external price pressures notwithstanding a stable rupee exchange rate (Table 4.1 and Chart 4.3).

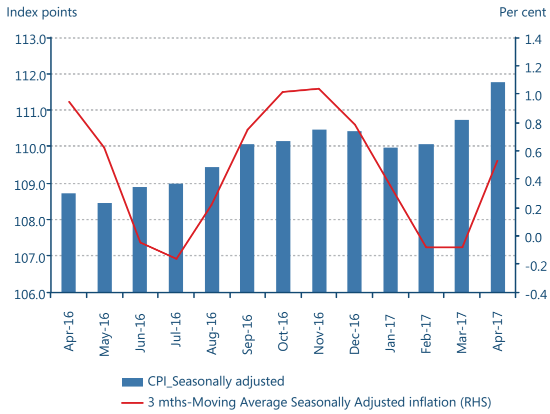
On a 12-month average basis, goods inflation increased from 1.0 per cent in April 2016 to 1.7 per cent in April 2017. Both services and CPIX_M inflation were higher while imported inflation went up from 0.5 per cent in September 2016 to 1.1 per cent in April 2017 (Table 4.2).

Chart 4.1 **Inflation Dynamics**



Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

Chart 4.2 **3-month Moving Average Seasonally Adjusted Inflation**



Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

The underlying trend inflation measures, namely CORE1 and CORE2, maintained their diverging path, swayed by existing price rigidity (Chart 4.4). Y-o-y CORE1 inflation firmed to 1.9 per cent in April 2017, from 0.7 per cent in April 2016 while Y-o-y CORE2 inflation eased from 2.6 per cent to 2.1 per cent. Based on the 12-month average methodology, the core measures were subdued.

Food inflation exhibited quite some volatility mostly on the back of seasonal pressures on the prices of vegetables . Y-o-y food inflation, which rose to a peak of 3.8 per cent in November 2016, plummeted to -3.5 per cent in March 2017 before rising to 1.9 per cent in April 2017. Based on the 12-month average methodology, food inflation fluctuated within a range of 0.4 per cent and 1.5 per cent during the period under review (Chart 4.5).

Reflecting the increase in excise duties on alcoholic beverages and tobacco in August 2016, CPI inflation remained dominated by developments in the 'Alcoholic beverages and

Table 4.1: Measures of Inflation (per cent, y-o-y)

Period	Food price inflation	CPIX_M*	Imported inflation	Goods inflation	Services inflation	CORE1	CORE2
Apr-16	-1.3	0.4	0.6	-0.1	0.9	0.7	2.6
May-16	2.7	1.0	-0.6	0.9	0.8	-0.1	1.7
Jun-16	4.1	1.3	-1.1	1.2	1.1	0.4	2.3
Jul-16	2.7	1.2	-0.6	0.9	1.4	0.7	2.6
Aug-16	0.4	1.1	0.4	1.0	0.8	-0.4	1.8
Sep-16	0.6	1.2	0.7	1.1	0.7	-0.3	1.9
Oct-16	2.2	1.7	1.3	2.0	0.4	-0.4	1.8
Nov-16	3.8	2.5	1.5	2.9	1.0	0.1	1.8
Dec-16	3.4	2.5	1.4	2.8	1.3	0.3	1.7
Jan-17	0.9	2.0	1.4	1.9	1.7	0.5	1.7
Feb-17	-2.4	1.4	2.4	1.1	1.7	1.1	1.6
Mar-17	-3.5	1.4	3.4	1.0	1.7	1.7	1.8
Apr-17	1.9	3.0	3.7	3.2	2.2	1.9	2.1

** Refers to CPI excluding mortgage payments in inflation.*
Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

Table 4.2: Measures of Inflation (per cent, 12-month average)

Period	Food price inflation	CPIX_M*	Imported inflation	Goods inflation	Services inflation	CORE1	CORE2
Apr-16	0.4	0.9	1.0	1.0	0.4	0.7	2.2
May-16	0.5	1.0	1.0	1.0	0.4	0.7	2.2
Jun-16	1.0	1.0	0.8	1.0	0.5	0.7	2.2
Jul-16	1.1	1.1	0.7	1.0	0.6	0.7	2.3
Aug-16	1.0	1.1	0.6	1.0	0.7	0.7	2.3
Sep-16	0.7	1.0	0.5	0.9	0.7	0.6	2.3
Oct-16	0.6	1.0	0.6	0.9	0.7	0.5	2.3
Nov-16	0.8	1.1	0.7	1.0	0.8	0.4	2.3
Dec-16	0.9	1.2	0.7	1.1	0.9	0.4	2.2
Jan-17	1.3	1.3	0.7	1.2	0.9	0.3	2.1
Feb-17	1.5	1.5	0.7	1.4	1.0	0.3	2.0
Mar-17	1.0	1.5	0.9	1.4	1.1	0.4	1.9
Apr-17	1.3	1.7	1.1	1.7	1.2	0.5	1.9

**Refers to CPI excluding mortgage payments in inflation.*
Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

tobacco' sub-group followed by 'Food and non-alcoholic beverages', which carries the largest weight in the CPI basket (Chart 4.6). The contributions of other divisions, in particular, 'Transport' and 'Housing, water, electricity, gas and other fuels' were also quite significant to y-o-y inflation due to the increase in domestic petroleum prices in February last.

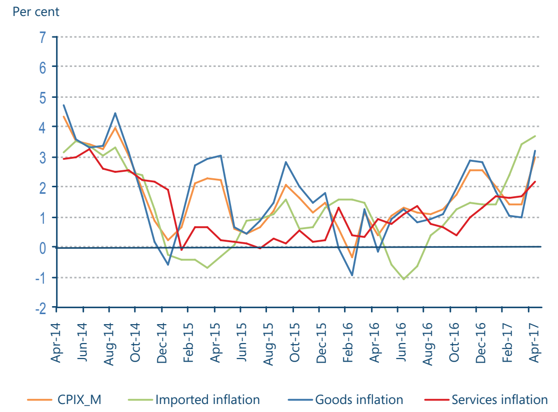
Inflation expectations have remained well contained over the different time horizons and were consistent with the prevailing low domestic headline inflation. During the survey month of February 2017, the mean headline inflation rates that were expected by respondents were 1.8 per cent and 2.4 per cent for June 2017 and a year ahead, respectively, compared with 2.5 per cent and 2.3 per cent, respectively, for the survey month of May 2016 (Chart 4.7).

4.2 Inflation and GDP Growth Projections – The Baseline Scenario

As a small open economy, Mauritius remains under the influence of external economic and financial developments. Bank staff inflation and growth projections are thus conditioned on assumptions about developments in foreign output including that of its main trading partners, commodity prices, trading partner inflation and global interest rates. The medium-term growth and inflation outlook has been generated using a quarterly forward-looking projection model calibrated for the Mauritian economy.

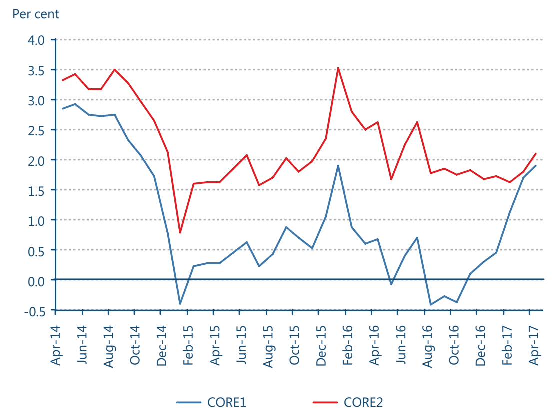
The IMF April 2017 WEO projections highlighted that world output growth would pick up in 2017 and 2018, signalling an improvement in external demand. Though higher in 2017 compared to 2016, world oil prices would be expected to remain subdued in the near term. Though the FAO Food Price Index recently picked up, this firming is not expected to sustain throughout the near term on account of supply considerations. Global inflation is, therefore, projected to increase on the back of improving economic conditions and rising commodity prices and hover mostly around target levels. European interest rates are projected to remain at their current low level throughout 2017, with the ECB maintaining its stimulus program to lend support to Eurozone growth during the year, and heading for normalisation in 2018. Conversely, the US economy is geared towards an expansionary

Chart 4.3 Goods, Services and Imported Inflation (y-o-y)



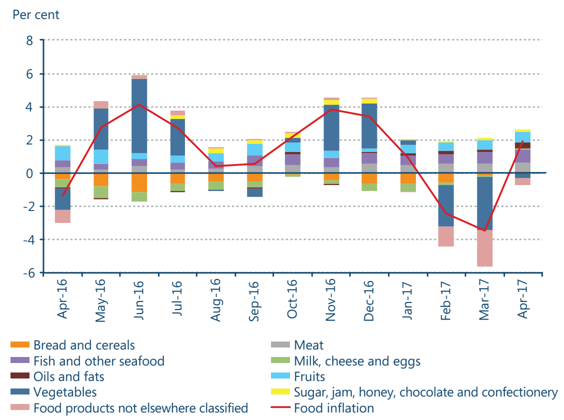
Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

Chart 4.4 Core Inflation (y-o-y)



Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

Chart 4.5 Weighted Contribution of Various Food Products to Y-o-y Food Inflation



Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

path and the anticipated US interest rate hikes during 2017, would likely trigger an appreciation of the US dollar. An unchanged fiscal stance has been assumed in line with Government's intention to move for fiscal consolidation. The implementation of public sector infrastructure projects would provide the necessary impetus to boost domestic output in the medium term. Forecasts are generated on the assumption that no further significant change in administered prices is planned over the projection period. The rupee exchange rate has been relatively stable recently, and it is assumed to tread on this stable path in the near term.

4.3 Inflation Projection

The prevailing inflation environment exhibits stability and reflects somewhat tame inflationary impulses arising from local food prices as well as subdued external pressures. Headline inflation is projected to depict somewhat broad stability in the near term and would rise gradually in the near term. Moreover, a decline in domestic spare capacity is expected to contribute mild pressures to domestic inflation. On the external front, the surge in international commodity prices, together with an anticipated gradual firming up in trading partners' inflation rates, uncertainty surrounding US policies and their repercussions on the domestic economy through the price channel can potentially contribute to higher domestic headline inflation in the medium term.

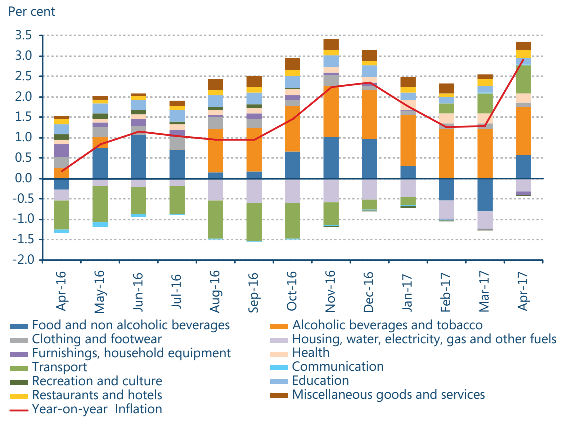
Headline inflation is anticipated to rise from its current level but would remain below 3 per cent in 2017, barring exceptional shocks (Chart 4.8).

4.4 Real GDP Growth Projection

The domestic economic landscape is suitable for sustainable real GDP growth, supported by accommodative monetary conditions and positive trends in business confidence. Large-scale public investment projects are also expected to boost domestic output in the medium term. The momentum in real GDP growth is projected to be sustained over the forecast horizon, with real GDP growth expected to be in the range of 3.8 per cent to 4.0 per cent in 2017 (Chart 4.9).

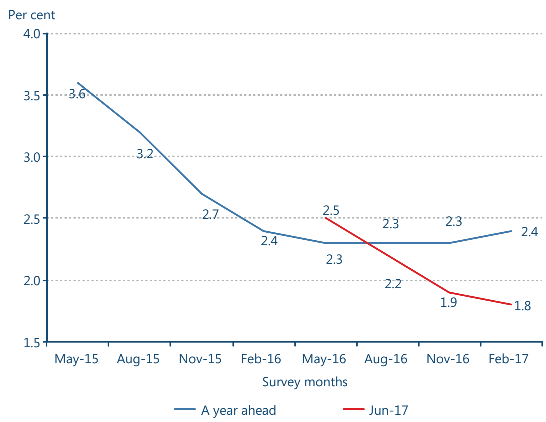
On a sectoral basis, numerous factors are expected to contribute to the upbeat growth

Chart 4.6 Evolution of the Main Divisions' Contribution to Y-o-y Inflation



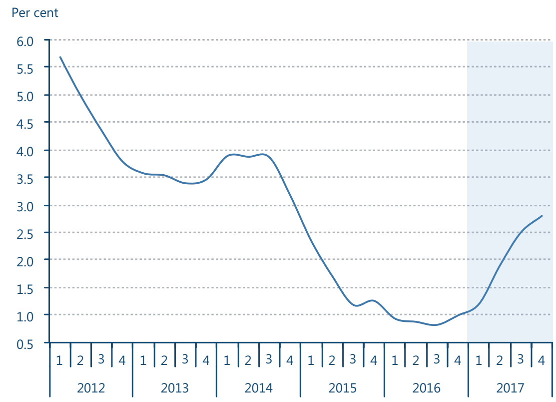
Sources: Statistics Mauritius and Bank of Mauritius staff calculations.

Chart 4.7 Inflation Expectations



Source: Bank of Mauritius staff calculations.

Chart 4.8 Headline Inflation



Source: Bank of Mauritius staff estimates.

outlook. The implementation of major public infrastructure projects, most notably the Metro Express project would help in the overhauling of the construction sector, resulting in an expected rebound of the sector by 7.0 per cent in 2017. Economic growth will also be boosted by higher public investment through the execution of announced infrastructure projects including the Decongestion Programme, the erection of smart cities, construction of a multisport complex to house the 2019 Indian Ocean games and social housing projects amongst others. In addition, the Property Development Scheme, representing potential investment of Rs18 billion will act as a positive impulse for the real estate sector.

Nonetheless, headwinds can result in a deviation of economic performance away from the projected trajectory. Brexit threatens to impede on the domestic outlook through the trade, financial and tourism channels. In particular, the depreciation of the Pound sterling could adversely impact the manufacturing sector triggering slower demand for textiles. Adverse changes to the US policy mix would result in global ramifications that could also influence local economic developments. Protectionist tone adopted by leaders of major advanced economies can negatively affect trade prospects. The gradual phasing out of the Mauritius-India DTAA blurs the outlook for the financial services sector somewhat. In addition, delays in the implementation of infrastructural projects and longer-than-expected corporate deleveraging could derail the growth trajectory.

4.5 Balance of Risks

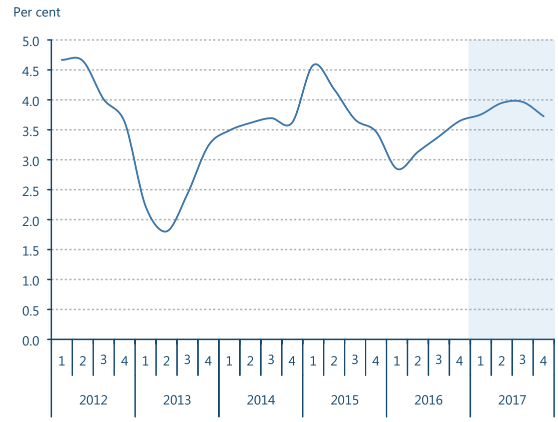
Forecasts are generated conditional on a specific set of assumptions, and are not immune to the occurrence of unanticipated events that may affect the direction and magnitude of projections. The materialisation of major economic risks can potentially cause real GDP growth and inflation to drift away from their respective projected trajectories. It is, therefore, imperative to identify some major risks and assess their probable effects on the forecasted trajectory in order to evaluate the balance of risks. The main risks that could divert the inflation rate away from the baseline scenario would include:

- ***Lower global growth.*** Prevalent economic uncertainties that could drag global growth down would include potential economic slowdown in UK and the Euro area following consequences of Brexit and resurfacing debt concerns in Greece, China's structural adjustment to a slower pace of growth resulting from its economic rebalancing and lower capital flows in emerging economies as US proceeds with interest rate normalisation and geopolitical tensions. The materialisation of such risks could translate into lower trading partner growth, thereby dampening external demand, which would then result in containing nascent inflationary pressures. External demand would also be adversely impacted, if major trading partners opt for protective trade policies.

- ***Domestic demand shock.*** An optimistic growth forecast rests upon the assumption of timely implementation of announced public and private investment projects, but implementation delays could derail the growth forecast. Sources of domestic uncertainties also stem from the upcoming phasing out of the Mauritius-India DTAA, which could curb investment flows. The domestic demand shock would potentially be a drag on real GDP, also exerting downward pressures on the inflation rate.

- ***Domestic supply shock.*** Cost-push factors such as the introduction of minimum wage legislation and specific supply-side shocks, on account of adverse climatic conditions, could

Chart 4.9 Average Real GDP Growth



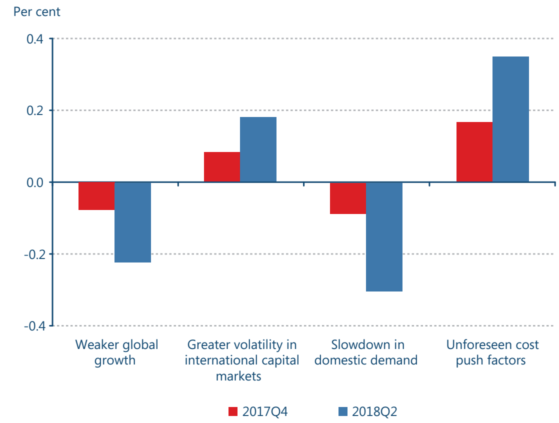
Source: Bank of Mauritius staff estimates.

weigh on prices of some goods and services. Increases in wages beyond inflation indexation and productivity gains remain a major upside risk to the inflation outlook.

- ***Increased volatility and uncertainty in international financial markets.*** Increased volatility in international financial markets could manifest through a potential sizeable fiscal impulse and monetary policy tightening in the US. Such an occurrence could set the basis for further strengthening of the US dollar and thus, put downward pressure on the domestic currency, which would translate into higher domestic prices through the exchange rate pass-through mechanism.

Staff assessment is that, for the year 2017, based on alternative projections, the balance of risks to the inflation outlook appears somewhat tilted on the upside. The probability that inflation will divert above the forecast in the baseline scenario is estimated to be higher than the probability that it will divert below this forecast. Chart 4.10 shows the impact of the individual risk factors on the inflation outcome for 2017, measured as the difference between the baseline scenarios's projected inflation rate and the inflation rate that would prevail under materialisation of the above-mentioned specific shocks, but adjusted for the probability of occurrence of these shocks. Each bar in the chart illustrates the magnitude and direction of the impact of these factors. The balance of risk is derived by taking the sum across the various effects, and shows the deviation of the inflation projection from the baseline scenario.

Chart 4.10 Balance of Risks to the Inflation Outlook



Source: Bank of Mauritius staff estimates.

BOX I: STATEMENT ON PRICE STABILITY

The Bank's current monetary policy stance remains accommodative and supportive of economic activity amidst the low inflation environment and anchored inflation expectations.

At its November 2016, February 2017 and May 2017 meetings, the Monetary Policy Committee (MPC), voted unanimously to maintain the Key Repo Rate unchanged at 4.00 per cent per annum. The MPC's decision was motivated by protracted global economic uncertainty, following a series of global events, as well as the low domestic inflation environment.

The domestic economy is expected to perform better in 2017 compared to 2016 and will remain supported broadly by all sectors in the economy. A revival in investment spending in 2016H2 would sustain the domestic growth momentum. Household consumption would remain supported, while the underperformance of the exports sector remained a matter of concern. In this respect, MPC members took note of the recently launched National Exports Strategy to boost domestic exports through the identification of niche markets. This initiative is warranted given that the trade deficit has been widening as a result of higher global commodity prices.

The domestic economy has been operating below its potential amid structural bottlenecks and weak external demand. With the launch of massive public investment programmes, the benefits of declining spare capacity are expected to be felt over the medium term. Rising business confidence would comfort investor optimism and is expected to support the domestic growth momentum. Headwinds to domestic growth prospects, however, still prevail. Downside risks, ranging from delays in launching public and private investment projects, weak productivity levels, changing US policy mix, the unanticipated shocks of Brexit, European elections and the impact of the Mauritius-India DTAA, can derail the projected growth trajectory. Bank staff have maintained their real GDP projection in the range of 3.8 to 4.0 per cent for 2017, conditional on the timely implementation of large infrastructural projects.

The MPC has also taken note of the evolution of excess liquidity in the banking sector and of the Bank's active role to bring down excess reserves to a tolerable level. The dilemma in domestic policy-making with a trade-off between excess liquidity and an appreciation of the rupee was highlighted. Members noted that any prolonged misalignment of the domestic currency with regard to economic fundamentals would not be in line with the objective of an orderly and balanced economic development. The Bank will continue its efforts to achieve the necessary monetary conditions prior to the implementation of the new monetary policy framework for an effective transmission of monetary policy to the real sector of the economy.

Inflationary impulses, so far, have remained stable and contained at desirable levels in the economy reflecting tame external and domestic pressures. Headline inflation has gradually increased from 0.8 per cent in September 2016 to 1.5 per cent in April 2017, reflecting among others the behaviour of volatile vegetable prices and the increase in domestic petroleum prices in February 2017. Year-on-year inflation, reflecting inherent dynamics, has been quite volatile and varied between 1.3 per cent and 2.9 per cent. The combination of inflationary impulses arising from local food prices, limited pressures from exchange rate developments and subdued domestic and external demand conditions have generally provided for an environment conducive to stable inflation.

Conditional on a set of assumptions, Bank staff estimate that the prevailing domestic and external economic environment is expected to contribute mildly to headline inflation in the near term, with a gradual rise anticipated over the projection horizon. Volatile domestic food prices, the gradual reduction of domestic spare capacity, an expected further strengthening of the US dollar arising from further normalisation of monetary policy in the US and a potential uptick in international oil prices due to geopolitical tensions and OPEC's output cut agreement would contribute to domestic price pressures. Latest forecasts by Bank staff show that headline inflation would settle at below 3.0 per cent in 2017, barrring exceptional supply shocks.

Overall, domestic monetary and financial conditions have remained supportive of economic activity in the year to April 2017. Liquidity conditions have remained adequate, while the relatively low and stable retail interest rates offered the necessary backing for private sector financing. Going forward, the Bank will maintain vigilance on the unfolding of economic developments both at home and abroad so as to ensure an enabling monetary and financial environment required to sustain the country's growth momentum, while safeguarding price stability.

5. Debt Indicators of Households and Corporates

*Household debt-to-disposable income ratio receded in 2016 after peaking in 2015, as the increase in household disposable income fully offset the decline in household credit. The drop in bank credit to households was driven, to a large extent by consumption credit, which continued to register negative annual growth rates. The cut in the Key Repo Rate in July 2016 lowered borrowing service costs through a drop in lending interest rates and brought about a decline in the debt service cost of households. Corporate deleveraging remains ongoing but return on equity, in general, was somewhat lower compared to previous years. With the slowdown in corporate credit growth, corporate debt-to-GDP ratio equally dropped. The credit-to-GDP gap dipped further into negative territory.**

Credit extended by banks to the private sector (excluding GBC) dropped to Rs285.5 billion as at end-December 2016, from Rs286.2 billion a year earlier, reflecting a y-o-y contraction of 0.2 per cent. The slowdown in private sector credit was the result of contraction in corporate credit while household credit has continued to grow, albeit at a slower pace (Chart 5.1). The contraction in private sector credit and continued nominal GDP growth coalesced into a decline in the credit-to-GDP ratio to 65.8 per cent as at end-2016, from 69.9 per cent as at end-2015. Private sector credit-to-GDP gap[2] deepened to -7.6 per cent in 2016Q4, from -2.1 per cent in 2015Q4. As a result of a higher growth in household credit coalesced with a contraction in corporate credit, banks' exposure to the household sector increased. Thus, the share of household credit in total private sector credit increased by 1 percentage point to 30.6 per cent as at end-December 2016, from 29.6 per cent a year earlier.

5.1 Households

On average, about 65 per cent of bank credit to households is for housing purposes, with the rest granted as consumption credit. The pace of growth in household credit, which moderated to 5.0 per cent in 2015, fell further to 3.2 per cent in 2016. This decline was driven to a large extent by the continual fall in consumption credit (Chart 5.2). Concurrently, the other component of household credit - credit for residential purposes – also posted lower y-o-y growth. As at end-December 2016, credit extended by banks to households for housing purposes grew by 5.7 per cent, lower than the 9.4 per cent increase recorded a year earlier. Notwithstanding higher building permits approved, the slowdown in the growth of housing credit was quite noticeable (Chart 5.3). Consumption credit contracted by 1.4 per cent as at end-December 2016, lower than the contraction of 2.1 per cent registered in the corresponding period of 2015.

As the banking system remained flushed with excess liquidity, the decline in the growth of household credit appears to be more demand driven. The decline in the number of reports drawn from the Mauritius Credit and Information Bureau (MCIB) in 2016 would tend to support

Chart 5.1 **Contribution to Growth of Private Sector Credit**

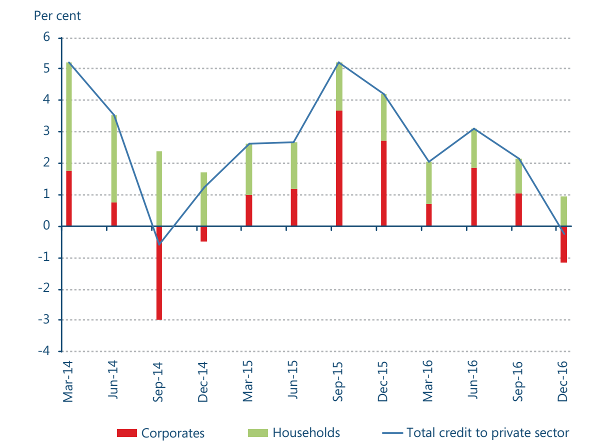
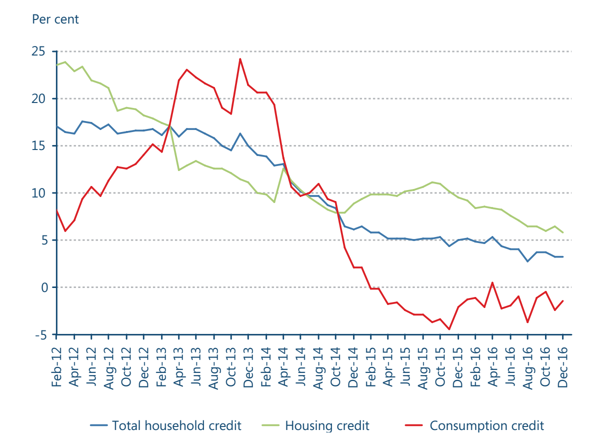


Chart 5.2 **Y-o-y Growth of Credit to Households**



[2] *The credit-to-GDP gap is estimated as the percentage deviation between the credit-to-GDP ratio and an estimate of its trend using the Hodrick-Prescott filter.*

** Analysis in this chapter is based on data as reported by banks, unless stated otherwise.*

this view (Chart 5.4). On a y-o-y basis, reports drawn from the MCIB contracted by 10.1 per cent during 2016H2, twice the contraction of 5.0 per cent in the corresponding period of 2015.

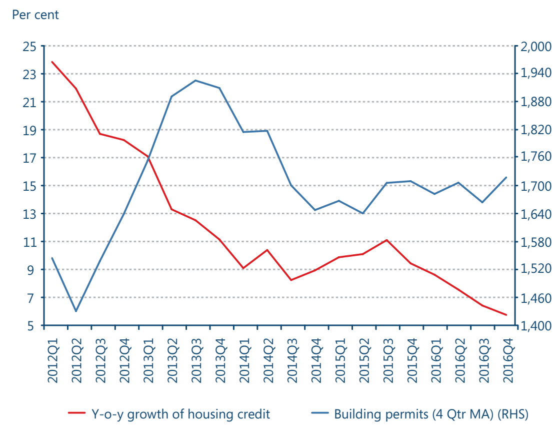
Foreign exchange risk arising from banks' foreign currency exposure to households appears mitigated as households borrow mostly in the domestic currency. As at end-December 2016, credit extended by banks to households in domestic currency accounted for about 96.5 per cent of total household credit, while foreign currency borrowings accounted for the remaining 3.5 per cent (Chart 5.5).

Household debt-to-disposable income ratio subsided in 2016 after reaching an all-time high in 2015. The decline was the result of higher expansion of household disposable income relative to household credit. While the increase in household disposable income was supported by improving economic conditions and the PRB wage award, the slower growth in household credit reflected the contraction in consumption credit. Household debt from banks as a ratio to disposable income fell to 52.7 per cent as at end-December 2016, from 54.5 per cent as at end-December 2015 (Chart 5.6). A broader definition of household indebtedness, which includes debt from non-bank deposit-taking institutions as well as insurance companies, more or less pointed to a similar downtrend in 2016 and stood at 79.3 per cent as end-December 2016 compared to 82.6 per cent as at end-December 2015 (Chart 5.7). Indebtedness of households compares favourably with countries in the region like Namibia and South Africa. During 2016, most of the comparator countries witnessed an increase in the household indebted ratios (Chart 5.8).

Compensation of employees, as reported in the country's National Accounts data, is part of household disposable income. Following the PRB salary award, compensation of employees increased by 6.6 per cent 2016, higher than the growth 4.0 per cent recorded 2015 (Chart 5.9).

The drop in the household debt service ratio in 2016 would somewhat reflect lower risks to financial stability arising from indebtedness of households. The decline in the debt service ratio resulted from lower interest rates on housing and consumption credit as well as higher disposable income of households. Following the cut in the KRR in July 2016, interest rates on both housing and consumption credit edged

Chart 5.3 Number of Building Permits and Y-o-y Growth in Housing Credit



Sources: Statistics Mauritius and Bank of Mauritius.

Chart 5.4 Number of Reports drawn from the Mauritius Credit and Information Bureau

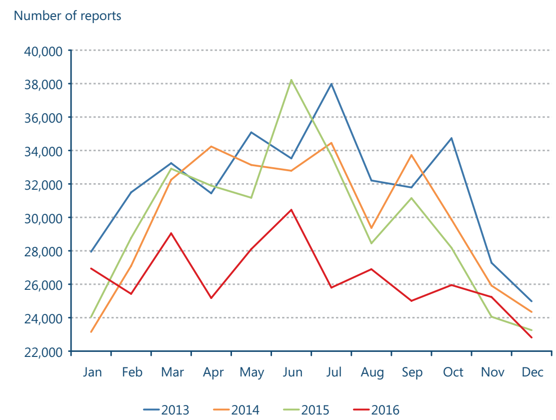
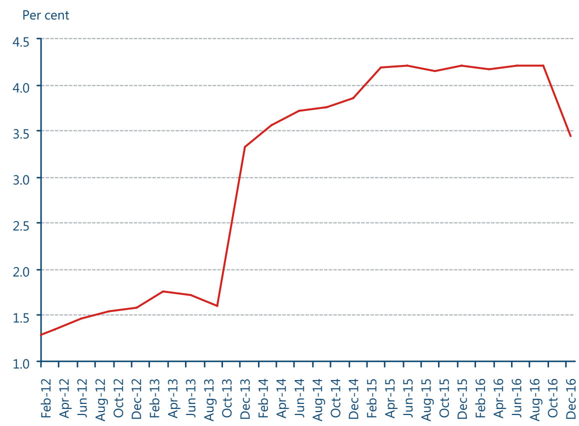


Chart 5.5 Share of Foreign Currency Credit in Total Household Credit



lower, thereby contributing to lower debt service cost. The debt service ratio - measured as debt service to disposable income – shed slightly over one percentage point, from 17.5 per cent as at end-December 2015 to 16.4 per cent as at end-December 2016 (Chart 5.10). At the regional level, the debt service cost of households is relatively higher than in comparator countries and might be due to interest rate differential (Chart 5.11). Nevertheless, as against Mauritius, Namibia and South Africa reported an increase in debt service ratios in 2016 compared to 2015.

Household credit-to-GDP gap has plunged further into negative territory in 2016. The Basel III capital reforms prescribe the use of the gap between the credit-to-GDP ratio and an estimate of its long-term trend to determine countercyclical capital buffers. The credit-to-GDP gap is useful as an early warning indicator for detecting banking crisis but authorities have to assess the build-up of systemic risk in the banking sector while imposing the countercyclical buffer[3]. While an increase in the credit-to-GDP gap may point to the potential build-up of vulnerabilities in the banking sector, a decline in the rate may be seen as indicating falling financial deepening. In 2016, growth of credit extended by banks to households has slowed, while nominal GDP growth hovered around 5 per cent. This resulted in a decline in the household credit-to-GDP ratio to 20.1 per cent as at end-December 2016 compared to 20.7 per cent as at end-December 2015. As a consequence, the household credit-to-GDP gap dipped further into negative territory and has been estimated at -1.6 per cent as at end-December 2016, down from -1.1 per cent a quarter earlier and -0.1 per cent as at end-December 2015 (Chart 5.12). The decline in the household credit-to-GDP gap was the consequence of both lower housing and consumption credit.

Non-performing loans (NPLs) resulting from credit advanced to personal and professional sectors increased to Rs2,937 million and Rs211 million, respectively, as at end-December 2016 and were 10.4 per cent and 7.7 per cent higher compared to their levels as at end-December 2015. Nevertheless, impairment on outstanding credit card advances to households fell by 4.6 per cent, y-o-y, to Rs193 million as at end-December 2016. Thus, the NPL ratio, that is the ratio of

[3] *The Basel III capital reforms prescribe a countercyclical buffer within a range of 0-2.5 per cent comprising of common equity.*

Chart 5.6 Household Debt to Disposable Income

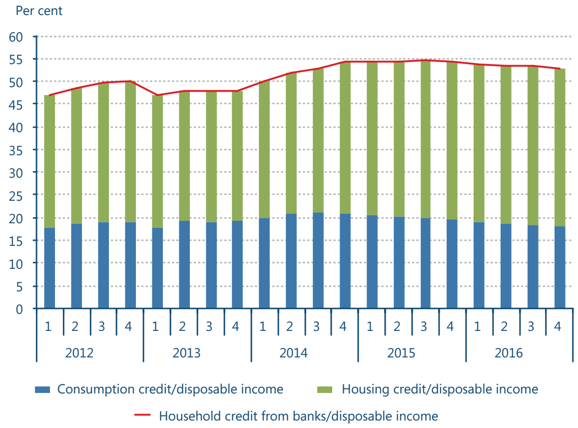
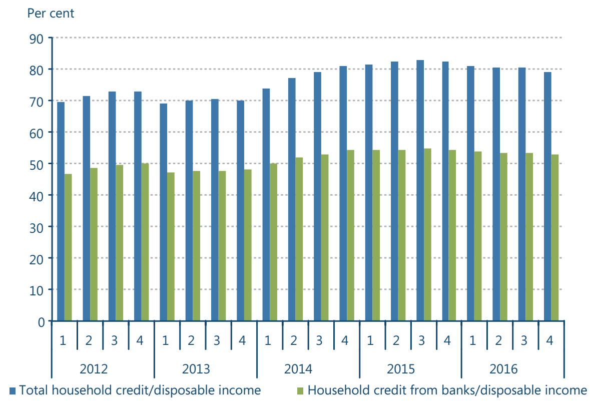
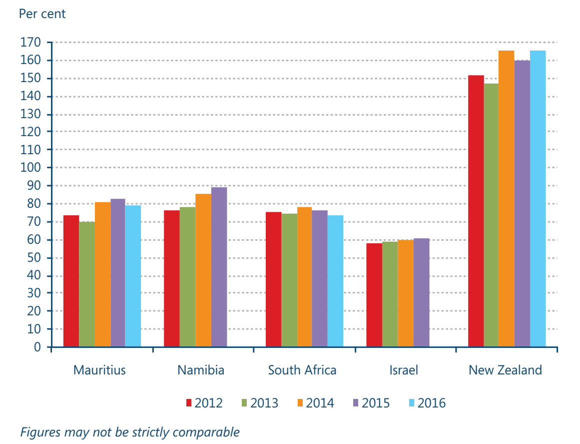


Chart 5.7 Estimates of Household Indebtedness Ratio (Banks and Non-Bank financial intermediaries)



Note: Total household credit includes credit from banks, non-bank deposit-taking institutions and insurance companies.

Chart 5.8 Household Debt in Selected Countries



Note: Data for Namibia and Israel for the year 2016 not yet available.

Sources: Various central banks' FSR and Bank of Mauritius staff estimates.

NPLs to total credit, was higher in the personal and professional sectors at 10.3 per cent and 16.3 per cent, respectively, as at end-December 2016 compared to 9.2 per cent and 15.7 per cent as at end-December 2015. The NPL ratio for credit card advances fell to 8.7 per cent as at end-December 2016, from 9.3 per cent a year earlier.

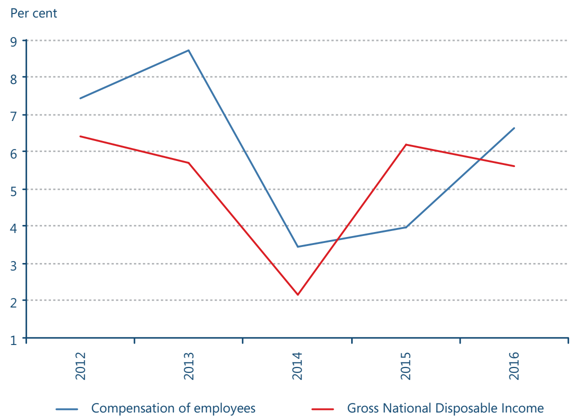
More recent dynamics using a q-o-q analysis, however, showed an improvement in asset quality with a decline in NPL ratio for the personal sector and on credit card advances. NPL ratio for personal credit stood at 10.3 per cent as at end-December 2016 was lower compared to 10.6 per cent as at end-September 2016. Similarly, NPL ratio for professional credit was lower compared to end-September 2016. With regard to credit cards, about 8.7 per cent of the advances were classified as non-performing as at end-December 2016 compared to 10.3 per cent as at end-September 2016 (Chart 5.13).

Generally, in a low interest rate environment, a credit take-off would be expected. However, in Mauritius, households have deleveraged since implementation of a set of macroprudential measures in 2014. The decline in household debt-to-disposable income ratio and lower debt service cost has dampened somewhat risks to financial stability emanating from indebtedness of households. Notwithstanding this improvement, a close monitoring of the asset quality to households and non-performing loans remains warranted for early detection of nascent vulnerabilities.

5.2 Corporates

Banks are heavily exposed to corporates in Mauritius, as indicated by a share of about 68 per cent to total private sector credit. The performance of the corporate sector, thus, has an important bearing on financial system stability and on the overall performance of the economy. Gross Operating Surplus (GOS), which may be used as a proxy for the value-added provided by incorporated enterprises' operating activities after deducting for labour input costs, increased by 6.0 per cent in 2016, up from growth of 4.6 per cent recorded in 2015 (Chart 5.14). The increase in GOS may reflect higher internal sources of funding for investment.

Chart 5.9 Y-o-y Growth of Compensation of Employees and GNDI



Source: Statistics Mauritius.

Chart 5.10 Household Debt Service Cost and Interest Rates

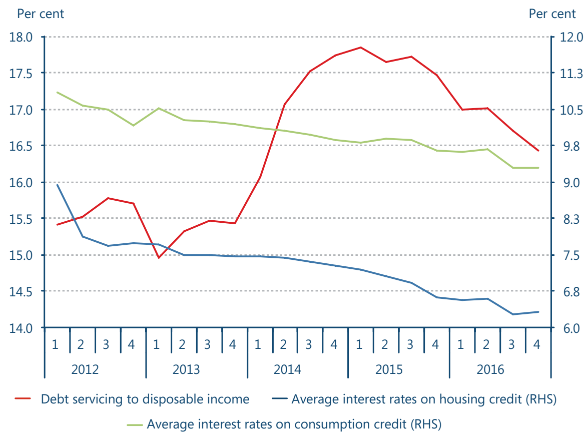
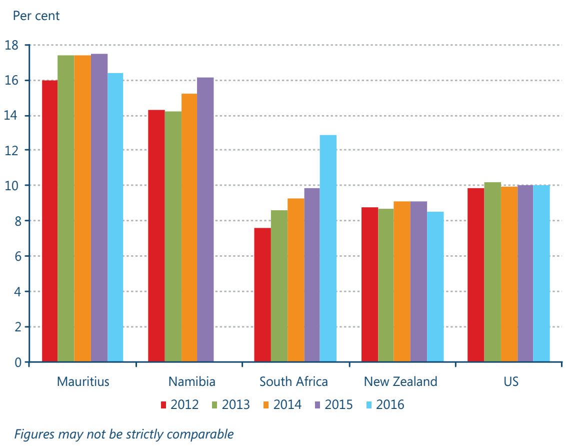


Chart 5.11 Household Debt Service Cost in Selected Countries



Note: Data for Namibia for the year 2016 not yet available.

Sources: Various central banks' FSR and Bank of Mauritius staff estimates.

The slowdown in private sector credit revealed the deleveraging of corporates in Mauritius. The debt-to-equity ratio has declined markedly for operators in construction and real estate sectors, from an average of 54.0 per cent over a 2-year period of 2013-2014 to 34.9 per cent in the two-year of 2015-2016. The decline in the leverage ratio would corroborate with a decline in activity in the construction sector over the past years (Table 5.1 and Chart 5.15). In the tourism sector, despite a decline in the leverage ratio, some operators still have debt in multiples of their equity. For the 2-year period ending 2016, the debt-to-equity ratio of operators in the tourism sector was estimated at 122.2 per cent, lower than 164.0 per cent in the 2-year period of 2013-2014. As regard the manufacturing sector, which is among the most important sector in economy, accounting for about 12.5 per cent of GDP, its debt-to-equity ratio is estimated at about 29.5 per cent over the 2-year period of 2015-2016. Operators in the sugar-linked sector were slightly more leveraged with a debt-to-equity ratio estimated at 40.5 per cent, higher from 38.9 per cent in the 2-year period of 2013-2014.

The profitability of operators in the construction and real estate, traders and sugar-linked sectors, as indicated by the return-on-equity ratio, declined in the 2-year period of 2015-2016 compared to the 2-year period of 2013-2014. However, in the tourism sector, return-on-equity increased to 4.2 per cent, from 2.5 per cent over the corresponding period. In the manufacturing sector, the return-on-equity ratio hovered around 7 per cent. Cost of debt, as measured by interest expense to total debt ratio, has fallen whereas the coverage of interest payments has increased, presumably reflecting lower bank borrowing interest rates.

Total corporate debt has fallen in 2016, both in absolute terms and as a ratio to GDP and pointed somewhat to lower risks arising from the indebtedness of corporates. From 55.6 per cent in 2015, corporate debt-to-GDP ratio dropped to 51.3 per cent in 2016. This decline resulted from a fall in both external and domestic debt, while nominal GDP continued to increase. The level of corporate debt in Mauritius compares relatively well on a selective cross-country basis (Chart 5.16). While, the corporate debt-to-GDP ratio has been increasing at the regional level, in Mauritius it has has generally been on a downtrend since 2012.

Domestic debt of corporates accounted for around 88 per cent of total corporate debt in 2016. As a ratio to GDP, it dropped from 48.8 per cent in 2015 to 45.0 per cent in 2016 (Table 5.2). External debt of corporates, that accounted for around 12 per cent of total corporate debt, have also declined in nominal terms and as a ratio to GDP, from 6.8 per cent of GDP in 2015 to 6.3 per cent in 2016. The lower external debt stock was

Chart 5.12 Household Credit-to-GDP Gap

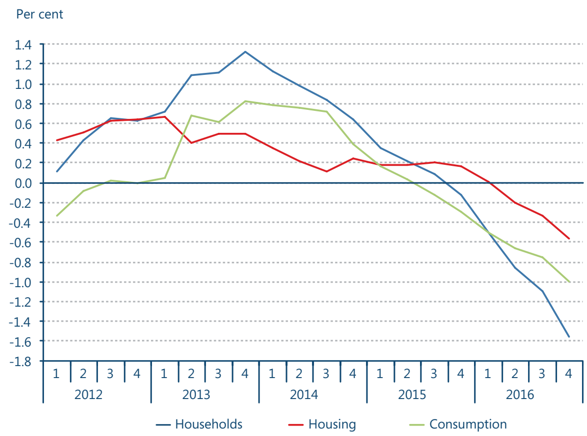
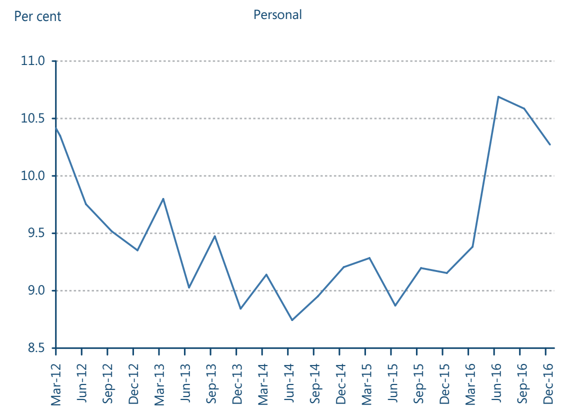
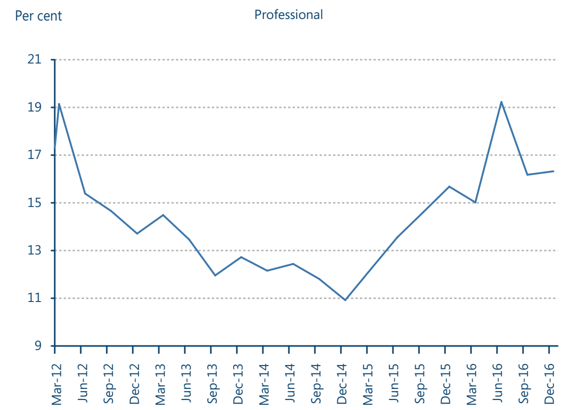


Chart 5.13 Non-performing Loans to Total Loans





reflected in the decline of external debt to gross official international reserves ratio, from 18.4 per cent as at end-December 2015 to 15.3 per cent as at end-December 2016. External debt as a ratio total export proceeds fell marginally from 13.9 per cent to 13.8 per cent.

Corporate domestic debt-to-GDP ratio has fallen in 2016 and resulted from the decline in credit to key sectors of the economy namely tourism, construction (excluding housing), manufacturing and traders. Reflecting deleveraging by some operators, all these sectors recorded negative y-o-y growth rates as at end-December 2016 as against growth in the corresponding period of 2015 (Table5.3). Credit extended for construction purposes (excluding housing) contracted by 6.4 per cent as end-December 2016 as against an increase of 4.0 per cent in the corresponding period of 2015. Credit extended by banks to operators in the tourism sector contracted by 10.9 per cent as at end-December 2016 as against growth of 1.4 per cent as at end-December 2015.

The decline in construction activity since 2011 has led to a lower demand for credit by this sector and hence, a falling share of the construction sector in GDP to 44.6 per cent at the end of December 2016 (Chart 5.17). In contrast, activity of traders has been rising, as evidenced by their increasing share in GDP but they accounted for a lower share in total private sector credit. As regard the tourism sector, despite higher activity in 2016, its share in total corporate credit has decreased, reflecting ongoing deleveraging.

Chart 5.13 Non-performing Loans to Total Loans (cont'd)

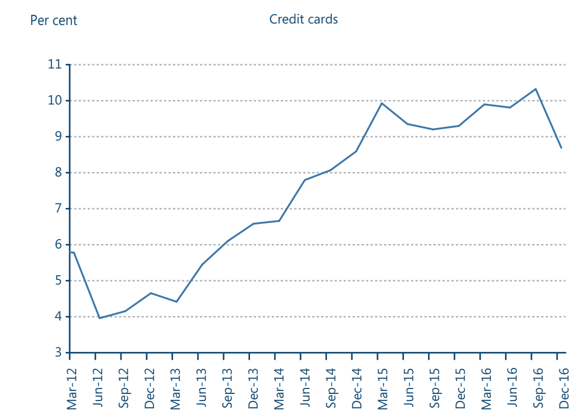
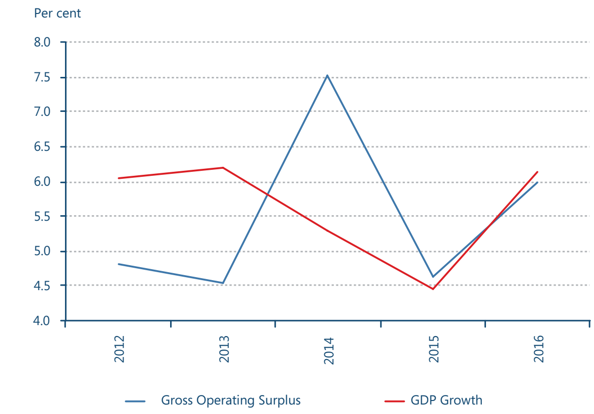
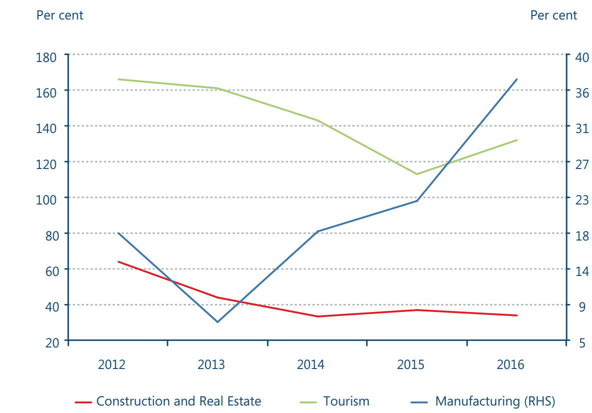


Chart 5.14 Growth of Gross Operating Surplus and GDP



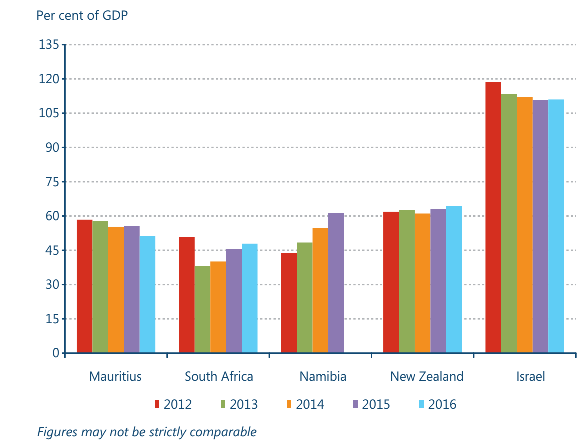
Source: Statistics Mauritius.

Chart 5.15 Leverage Ratio of Leading Economic Sectors



Source: Thomson Reuters and Bank of Mauritius staff calculations.

Chart 5.16 Corporate Debt-to-GDP ratio in Selected Countries



Note: Data for Namibia for the year 2016 not yet available.

Sources: Various central banks' FSR and Bank of Mauritius staff estimates.

Chart 5.17 Share of Selected Sectors in GDP and in Total Corporate Credit

Sources: Statistics Mauritius and Bank of Mauritius.

Table 5.1: Risk Analysis of Leading Entreprises in Mauritius Listed on the Stock Exchange of Mauritius

	2011-2012	2013-2014	2015-2016
Construction and Real Estate			
Return on equity	15.70%	12.47%	5.55%
Cost of debt	7.15%	9.46%	7.24%
Leverage (Debt-to-equity)	95.51%	54.04%	34.90%
Interest Coverage Ratio	2.61	2.15	2.27
Tourism			
Return on equity	2.93%	2.45%	4.20%
Cost of debt	4.56%	5.49%	5.66%
Leverage (Debt-to-equity)	153.07%	163.95%	122.22%
Interest Coverage Ratio	1.16	0.91	1.59
Manufacturing			
Return on equity	8.06%	7.46%	7.33%
Cost of debt	12.80%	5.67%	5.34%
Leverage (Debt-to-equity)	19.85%	12.66%	29.53%
Interest Coverage Ratio	22.48	10.97	21.47
Traders			
Return on equity	15.00%	13.28%	9.64%
Cost of debt	6.78%	6.17%	6.29%
Leverage (Debt-to-equity)	68.68%	82.27%	71.41%
Interest Coverage Ratio	16.22	6.22	11.65
Sugar-linked			
Return on equity	7.11%	7.33%	3.50%
Cost of debt	11.28%	6.73%	8.09%
Leverage (Debt-to-equity)	47.31%	38.85%	40.49%
Interest Coverage Ratio	2.84	4.68	2.84

Note: Cost of debt: interest expense-to-total debt.

Sources: Thomson Reuters and Bank of Mauritius staff calculations.

The credit-to-GDP gap for the corporate sector has remained anchored in negative territory since 2014. As at end-December 2016 the corporate credit-to-GDP gap was estimated at -5.0 per cent compared to -0.8 per cent in the corresponding period of 2015 (Chart 5.18), thereby indicating that the corporate sector is having less recourse to bank credit. On a sectoral basis, the credit-to-GDP gap of key sectors of the economy like construction, tourism and traders dipped further into negative. In the construction sector, credit-to-GDP gap was estimated at -2.2 per cent as at end-December 2016 compared to -0.1 as at end-December 2015. Similarly, for the tourism and traders sectors, credit-to-GDP gap fell to -3.2 per cent and -0.8 per cent, respectively, as at end-December 2016 compared to -1.0 per cent and zero per cent a year earlier. In the manufacturing sector, credit-to-GDP gap stayed positive but has fallen to 0.3 per cent as at end-December 2016 . The decline in the credit-to-GDP gap corroborates with the deleveraging of operators in the private sector but may pose risks to GDP growth going forward, as these operators can be thought of adopting a wait-and-see attitude with regards to investment projects.

Chart 5.18 **Credit-to-GDP Gap**

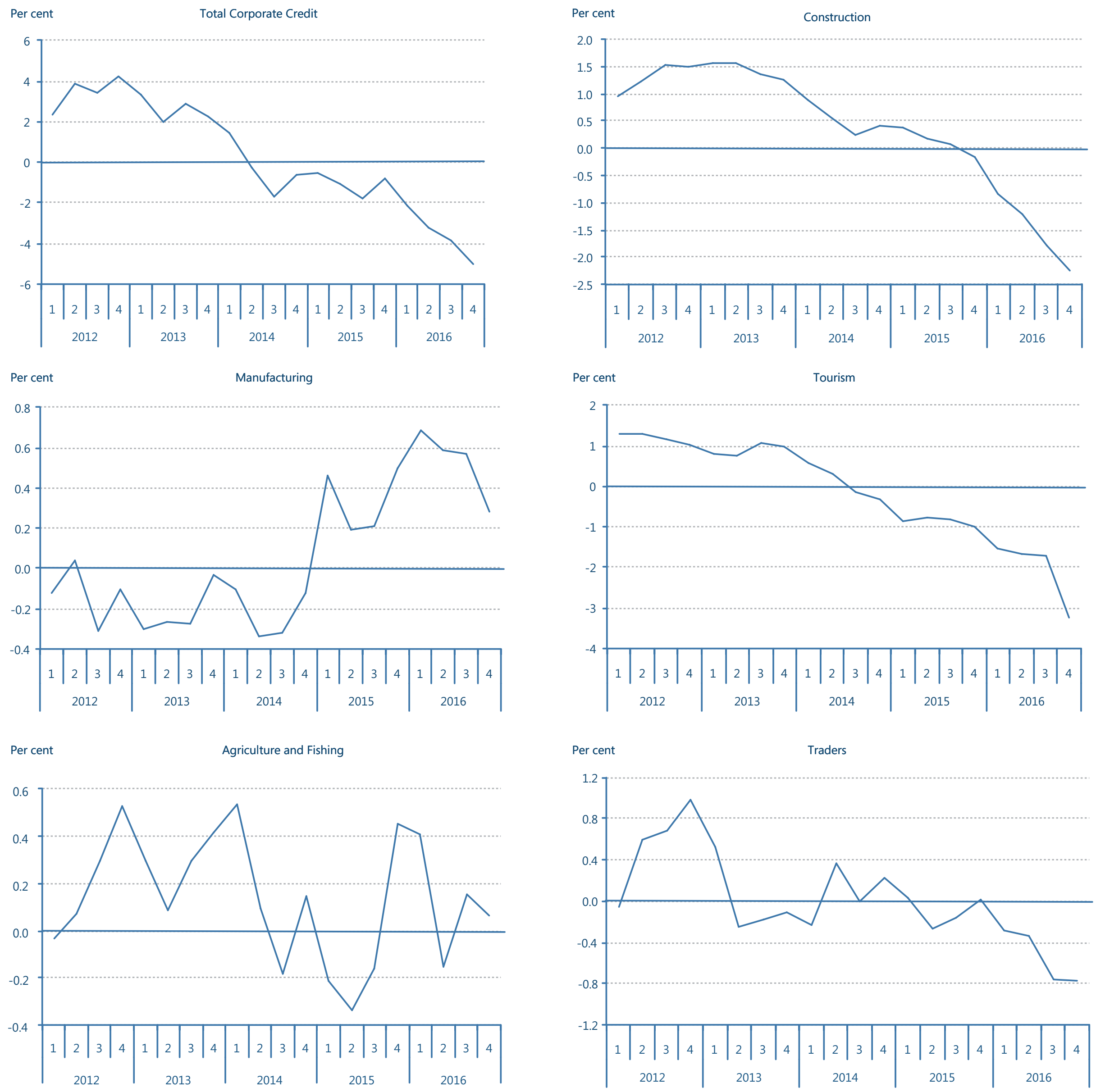


Table 5.2: Domestic and External Corporate Debt

	2012	2013	2014	2015	2016			
					Q1	Q2	Q3	Q4*
	Rs Million							
Total Corporate Debt	**204,863**	**215,579**	**216,977**	**227,552**	**225,233**	**223,901**	**224,773**	**222,756**
Corporate External Debt	21,680	26,468	27,316	27,875	28,168	27,977	28,238	27,380
Short Term[1]	3,534	3,861	4,269	4,733	5,278	5,290	5,303	5,315
Long Term[2]	18,146	22,607	23,047	23,142	22,890	22,687	22,935	22,064
Corporate Domestic Debt[#]	183,183	189,110	189,661	199,677	197,065	195,923	196,535	195,376
	Per cent of total corporate debt							
Total Corporate Debt	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**
Corporate External Debt	10.6	12.3	12.6	12.3	12.5	12.5	12.6	12.3
Short Term[1]	1.7	1.8	2.0	2.1	2.3	2.4	2.4	2.4
Long Term[2]	8.9	10.5	10.6	10.2	10.2	10.1	10.2	9.9
Corporate Domestic Debt[#]	89.4	87.7	87.4	87.7	87.5	87.5	87.4	87.7
	Per cent of GDP							
Total Corporate Debt	**58.4**	**57.9**	**55.3**	**55.6**	**54.3**	**53.2**	**52.7**	**51.3**
Corporate External Debt	6.2	7.1	7.0	6.8	6.8	6.6	6.6	6.3
Short Term[1]	1.0	1.0	1.1	1.2	1.3	1.3	1.2	1.2
Long Term[2]	5.2	6.1	5.9	5.7	5.5	5.4	5.4	5.1
Corporate Domestic Debt[#]	52.2	50.8	48.4	48.8	47.5	46.5	46.1	45.0

** Provisional.*

[#] Culled from banks' sectorwise distribution of credit.

[1] Refers mainly to trade credit as recorded in balance of payments statistics.

[2] Excluding loans of Global Business Companies.

Sources: Mauritius SDDS country page and Bank of Mauritius.

Table 5.3: Distribution of Credit to the Private Sector

	2006-2012	2013	2014	2015	2016Q1	2016Q2	2016Q3	2016Q4
	Per cent of GDP							
Total credit to private sector	**66.6**	**74.0**	**71.0**	**69.9**	**68.4**	**67.4**	**67.0**	**65.7**
Corporates	**47.9**	**51.6**	**49.0**	**48.8**	**47.5**	**46.5**	**46.1**	**45.0**
Agriculture & Fishing	4.5	5.2	4.9	5.2	5.2	4.6	5.0	4.9
Manufacturing	6.2	5.3	4.9	5.2	5.3	5.1	5.0	4.7
Tourism	11.4	13.3	12.3	11.8	11.4	11.3	11.3	9.9
Construction (ex housing)	5.4	8.1	7.9	7.8	7.4	7.3	7.0	6.9
Traders	8.6	7.9	8.1	7.8	7.4	7.4	6.9	6.9
Financial & Business Services	7.3	7.3	6.5	6.5	6.3	6.3	6.5	7.5
Households	**15.4**	**20.7**	**20.8**	**20.7**	**20.5**	**20.3**	**20.3**	**20.1**
Housing	8.9	12.4	12.8	13.3	13.3	13.2	13.3	13.2
Consumption Credit	6.5	8.3	8.0	7.4	7.2	7.1	7.1	6.9
	(Average annual growth rates; in per cent)							
Total credit to private sector	**12.1**	**5.9**	**1.3**	**4.2**	**2.1**	**3.1**	**2.1**	**-0.2**
Corporates	**12.5**	**3.2**	**0.3**	**5.3**	**2.0**	**3.4**	**1.9**	**-2.2**
Agriculture & Fishing	12.7	5.0	0.7	12.1	20.1	10.7	13.7	-0.7
Manufacturing	3.7	2.2	-2.2	12.0	3.5	7.7	7.1	-3.9
Tourism	16.3	8.8	-2.4	1.4	1.6	-0.2	0.2	-10.9
Construction (ex housing)	27.7	10.9	3.4	4.0	-2.9	-2.2	-6.4	-6.4
Traders	9.4	-7.6	9.0	1.0	-0.6	3.4	-4.0	-5.6
Financial & Business Services	13.1	5.4	-7.0	6.8	-5.6	6.3	8.3	21.9
Households	**15.1**	**15.0**	**6.2**	**5.0**	**4.6**	**3.7**	**3.7**	**3.2**
Housing	17.7	11.1	8.9	9.4	8.6	7.6	6.4	5.7
Consumption Credit	11.8	21.3	2.1	-2.1	-2.0	-1.9	-1.2	-1.4

6. Developments in the Financial Sector

The macro-financial landscape in Mauritius comprises banks, non-bank deposit taking institutions, cash dealers, insurance companies and pension funds. Given the relatively important share of banking assets in GDP, it is undeniable that banks play a macro-critical role. Despite this size, systemic risks appeared to be well contained mainly due to prudent and sound macro-financial policies being pursued in the jurisdiction.

6.1 Banking Sector

Overview

The distribution of total bank assets at end-December 2016 stood as follows: domestic-owned banks (52.1 per cent), subsidiaries of foreign-owned banks (44.3 per cent), and branches of foreign-owned banks (3.6 per cent). Growth of total assets in the banking sector accelerated to 4.1 per cent at end-December 2016, compared to a growth rate of 3.4 per cent as at end-December 2015, although it remains below its end-December 2014 growth rate of 10.8 per cent (Table 6.1). Domestic assets held by both domestic-owned and foreign-owned banks expanded by 8.6 per cent, while foreign assets grew by only 0.4 per cent, with different growth trends observed for domestic-owned and foreign-owned banks. Foreign assets held by domestic-owned banks expanded by 15.2 per

Chart 6.1 Banking Sector Assets

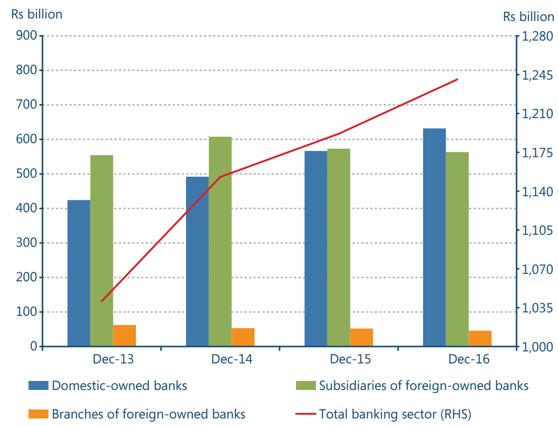


Table 6.1: Banks' Assets, 2014-2016

Growth rates of assets (Per cent) | *Assets (contribution to asset growth) (Per cent)*

I. Foreign Assets

	Dec-14	Dec-15	Dec-16		Dec-14	Dec-15	Dec-16
Domestic banks	42.9	32.1	15.2	Domestic banks	3.7	3.6	2.2
Subsidiary	11.7	-8.0	-3.8	Subsidiary	5.1	-3.5	-1.5
Branch	-25.3	-13.2	-30.4	Branch	-0.8	-0.3	-0.5
Total	**14.6**	**-0.2**	**0.4**	**Total**	**8.0**	**-0.1**	**0.2**

II. Domestic Assets

	Dec-14	Dec-15	Dec-16		Dec-14	Dec-15	Dec-16
Domestic banks	8.6	9.1	9.9	Domestic banks	2.8	2.9	3.3
Subsidiary	0.7	5.2	6.6	Subsidiary	0.1	0.5	0.6
Branch	-3.6	6.4	-0.4	Branch	-0.1	0.2	0.0
Total	**6.0**	**8.1**	**8.6**	**Total**	**2.7**	**3.5**	**3.9**

III. Total Assets

	Dec-14	Dec-15	Dec-16		Dec-14	Dec-15	Dec-16
Domestic banks	15.9	15.2	11.5	Domestic banks	6.5	6.5	5.5
Subsidiary	9.6	-5.7	-1.7	Subsidiary	5.1	-3.0	-0.8
Branch	-14.6	-2.2	-12.1	Branch	-0.9	-0.1	-0.5
Total	**10.8**	**3.4**	**4.1**	**Total**	**10.8**	**3.4**	**4.1**

Note: Totals may not add up due to rounding off.

cent, while those of subsidiaries and branches of foreign-owned banks contracted by 3.8 and 30.4 per cent respectively. Domestic assets held by domestic-owned banks and subsidiaries of foreign-owned banks expanded by 9.9 and 6.6 per cent respectively, while those of branches foreign-owned banks contracted by 0.4 per cent.

As at end-December 2016, the balance sheet of domestic-owned banks grew by 11.5 per cent, while that of subsidiaries and of branches of foreign-owned banks contracted by 1.7 and 12.1 per cent respectively. For domestic-owned banks, this balance sheet expansion was slower than the growth rate observed at end-December 2015 (15.2 per cent). For subsidiaries of foreign-owned banks, the contraction at end-December 2016 was less severe than the one observed at end-December 2015 (5.7 per cent). Branches of foreign-owned banks, on the other hand, experienced a more severe contraction at end-December 2016, compared to 2.2 per cent end-December 2015.

Table 6.2: Other Depository Corporations Balance Sheet, 2012-2016

	2012	2013	2014	2015	2016			
					Mar	Jun	Sep	Dec
	(Rs million)							
Net Foreign Assets	**309,761**	**292,802**	**335,088**	**377,506**	**350,089**	**363,039**	**371,593**	**371,482**
Claims on nonresidents	802,936	772,471	782,494	777,975	744,937	730,343	715,696	725,605
Liabilities to nonresidents	-493,175	-479,669	-447,407	-400,469	-394,848	-367,304	-344,103	-354,123
Claims on Central Bank (net)	**32,315**	**47,005**	**56,013**	**71,667**	**73,909**	**78,950**	**78,848**	**85,396**
o/w Reserve deposits and securities	25,340	32,105	35,352	47,601	46,965	49,445	51,757	56,871
o/w BoM securities held by ODCs[1]	3,916	10,796	17,351	26,748	31,830	35,388	33,639	33,624
Domestic Claims	**250,348**	**273,493**	**292,486**	**304,856**	**308,456**	**315,064**	**330,768**	**326,031**
Net Claims on Central Government	38,215	45,692	65,515	70,615	79,431	84,473	90,637	92,592
Claims on Other Sectors	364,089	413,243	401,882	431,004	431,378	433,363	436,299	435,266
Other items net	-151,956	-185,441	-174,911	-196,762	-202,352	-202,771	-196,168	-201,827
Broad Money Liabilities	**322,441**	**340,146**	**370,055**	**407,068**	**412,434**	**424,670**	**430,863**	**443,464**
Transferable Deposits	74,619	80,380	92,691	107,961	110,731	116,474	117,322	122,385
Savings Deposits	123,940	137,029	151,721	171,829	177,427	182,446	187,659	196,181
Time Deposits	122,768	121,487	124,262	125,773	122,752	124,204	124,314	123,296
Securities other than Shares	1,114	1,250	1,380	1,504	1,525	1,546	1,568	1,602
GBC deposits	**269,984**	**273,155**	**313,533**	**346,962**	**320,020**	**332,383**	**350,346**	**339,445**
	(Annual growth rates, per cent)							
Net Foreign Assets	**6.6**	**-5.5**	**14.4**	**12.7**	**-16.4**	**-4.8**	**2.8**	**-1.6**
Claims on Central Bank (net)	**0.3**	**45.5**	**19.2**	**27.9**	**18.1**	**12.3**	**12.9**	**19.2**
o/w Reserve deposits and Securities	7.1	26.7	10.1	34.6	-1.7	1.5	15.7	19.5
o/w BoM securities held by ODCs[1]	-29.3	175.7	60.7	54.2	118.9	43.7	17.7	25.7
Domestic Claims	**6.9**	**9.2**	**6.9**	**4.2**	**6.5**	**8.3**	**10.4**	**6.9**
Net Claims on Central Government	0.5	19.6	43.4	7.8	22.8	23.9	28.5	31.1
Claims on Other Sectors	17.1	13.5	-2.7	7.2	2.5	5.5	3.2	1.0
Other items net	32.4	22.0	-5.7	12.5	3.4	7.9	1.2	2.6
Broad Money Liabilities	**8.2**	**5.5**	**8.8**	**10.0**	**7.5**	**8.3**	**8.7**	**8.9**
Transferable Deposits	7.5	7.7	15.3	16.5	10.1	13.9	11.8	13.4
Savings Deposits	8.5	10.6	10.7	13.3	12.5	12.4	14.5	14.2
Time Deposits	8.2	-1.0	2.3	1.2	-1.1	-1.5	-1.5	-2.0
GBC deposits	**4.3**	**1.2**	**14.8**	**10.7**	**-17.4**	**-5.1**	**4.8**	**-2.2**

[1] *As reported in the BoM's balance sheet.*

As at end-December 2016, subsidiaries of foreign-owned banks contributed -0.8 per cent towards growth of total assets compared to 5.5 per cent for domestic-owned banks, and -0.5 per cent for branches of foreign-owned banks. As at end-December 2016, the total assets of domestic-owned banks, subsidiaries and branches of foreign-owned banks grew by 11.5 per cent, -1.7 per cent and -12.1 per cent respectively on a year-on-year basis. For domestic-owned banks, growth of domestic assets accounted for much of the expansion.

Market Concentration

Measures of concentration such as the Herfindahl-Hirschman Index (HHI) edged upwards, from 1,112 as at end-December 2015 to 1,177 as at end-December 2016 for assets and from 1184 to 1283 for deposits over the same period, thereby hinting at a relatively more concentrated market structure (Chart 6.2). This trend has been observed since 2012, although the index did occasionally point towards stability in the concentration ratios for some time. Compared to end-December 2011, the Lorenz curve which depicts relative inequality in the distribution of assets and of advances in the system indicates continued inequality in distribution of assets in the system (Chart 6.3), although the share of total assets held by the four largest banks dropped from 59 per cent as at end-December 2011 to 56 per cent as at end-December 2016, due in part to a change in the landscape of banking in Mauritius, with new licensees establishing their presence and a restructuring of two major banking group in 2015.

Financial Soundness indicators

Profitability

Profitability of the overall banking sector improved during the year ended December 2016. The decline in interest income in the banking sector was more than offset by the decline in interest expense, yielding positive net interest income during the period. Banks also benefited from other income such as profit from dealings in foreign currencies and net gains from sale of securities. Overall profitability results were also mirrored in improvements in Return on Assets (ROA) and Return on Equity (ROE) figures for all three categories of banks: domestic-owned banks, subsidiaries of foreign-owned banks, and branches of foreign-owned banks (Charts 6.4 and 6.5). Both ROA and ROE for the banking sector

Chart 6.2 **Herfindahl-Hirschman Index, 2011-2016**

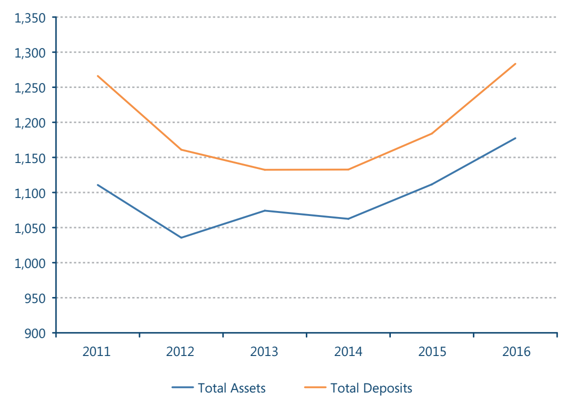
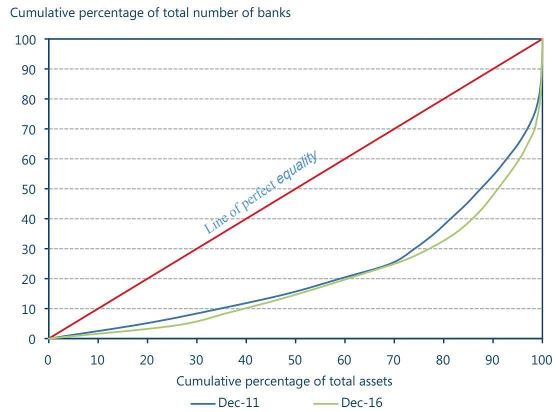


Chart 6.3 **Distribution of Banks' Assets and Advances**



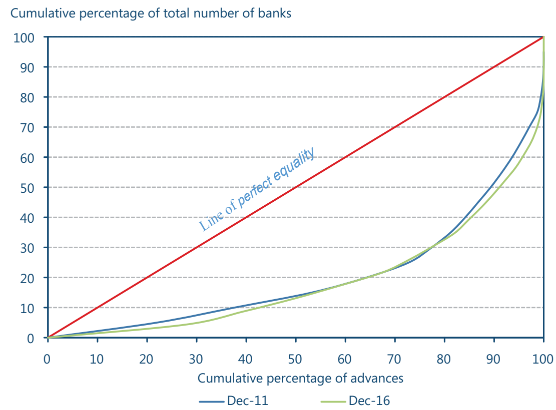


Table 6.3: Financial Stability Indicators[1] of Other Depository Corporations (Banks and NBDTIs[2])

Core Set of Financial Soundness Indicators	Dec-14	Jun-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16
							Per cent
Capital-based							
Regulatory capital to risk-weighted assets	17.1	17.6	18.4	18.7	18.2	18.2	18.2
Regulatory Tier 1 capital to risk-weighted assets	15.1	15.2	17.0	17.2	16.5	16.6	16.7
Non-performing loans net of provisions to capital	16.4	17.8	19.1	18.7	18.5	18.7	18.7
Asset Quality							
Non-performing loans to total gross loans[3]	4.9	5.8	7.2	7.8	8.0	8.0	7.8
Sectoral distribution of loans to total loans[3]							
Interbank loans	0.3	0.1	0.1	0.2	0.2	0.3	0.5
Other financial corporations	1.5	1.5	1.5	1.6	1.6	2.3	2.3
Non-financial corporations	33.6	34.8	36.8	37.1	37.0	36.4	35.6
Other domestic sectors	19.2	20.2	21.0	21.6	21.8	21.8	22.0
Non-residents	45.4	43.4	40.6	39.5	39.5	39.2	39.5
Earnings and Profitability							
Return on assets	1.4	1.1	1.2	1.4	1.4	1.5	1.5
Return on equity	15.2	11.4	12.1	13.1	13.6	14.0	14.0
Interest margin to gross income	49.0	62.0	68.5	62.7	67.2	63.0	71.4
Non-interest expenses to gross income	36.9	40.6	44.3	36.2	41.8	38.9	44.6
Liquidity							
Liquid assets to total assets	24.1	25.1	27.1	27.4	27.9	28.3	27.9
Liquid assets to short-term liabilities	30.2	31.7	34.5	34.4	34.1	34.3	33.9
Sensitivity to Market Risk							
Net open position in foreign exchange to capital	2.4	2.8	3.0	2.5	2.9	3.0	3.1
Encouraged Set of Financial Soundness Indicators	**Dec-14**	**Jun-15**	**Dec-15**	**Mar-16**	**Jun-16**	**Sep-16**	**Dec-16**
Capital to assets	9.3	10.3	10.5	10.5	10.5	10.6	10.6
Value of large exposures to capital	201.9	209.6	184.3	190.2	188.4	176.5	159.8
Customer deposits to total (non-interbank) loans	133.2	142.3	146.8	144.4	148.2	150.9	149.8
Residential real estate loans to total loans[3]	6.2	8.7	9.1	9.4	9.5	9.3	9.4
Commercial real estate loans to total loans[3]	5.0	5.6	5.8	5.8	5.5	5.1	4.6
Trading income to total income	35.4	15.0	10.0	16.2	7.9	17.9	9.6
Personnel expenses to non-interest expenses	40.8	48.5	50.5	50.6	52.0	47.7	47.3

Table 6.3: Financial Stability Indicators[1] of Other Depository Corporations (Banks and NBDTIs[2])(cont'd)

Macroeconomic Indicators	Dec-14	Jun-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16
							Per cent
Headline inflation[4]	3.2	1.7	1.3	0.9	0.9	0.8	1.0
Year-on-year inflation[4]	0.2	0.4	1.3	0.9	1.1	0.9	2.3
Key Repo Rate (end of period)	4.7	4.7	4.4	4.4	4.4	4.0	4.0
Total Public Sector Debt/GDP (end of period)	60.7	62.9	63.7	64.3	65.2	65.1	64.4
Total Public Sector External Debt/GDP (end of period)	16.0	16.8	16.5	16.0	15.6	15.4	14.8
Import coverage of Gross International Reserves (months of goods & services)	6.2	7.1	7.7	8.1	8.5	8.7	9.0
Deposits/Broad Money Liabilities[5]	92.8	93.4	92.7	92.9	93.0	93.0	92.6
Household Debt/GDP (end of period)[6]	20.5	20.6	20.7	20.5	20.3	20.3	20.1
Corporate Debt/GDP (end of period)[6]	48.4	47.3	48.8	47.4	46.5	46.0	45.0
	2014Q4	**2015Q2**	**2015Q4**	**2016Q1**	**2016Q2**	**2016Q3**	**2016Q4**
Real GDP growth[4]	2.2	2.1	3.8	3.7	2.3	3.7	4.1
Unemployment rate	7.5	7.8	7.9	7.6	7.4	7.6	6.6
Current account deficit/GDP	3.0	5.4	2.1	2.7	4.4	6.4	3.9

[1] FSIs are calculated on a domestic consolidation basis using the Financial Soundness Indicators Compilation Guide of the International Monetary Fund. Figures may be slightly different from other parts of this Report.

[2] NBDTIs refer to Non-Bank Deposit-Taking Institutions.

[3] Total gross loans include commercial loans, installment loans, hire-purchase credit, loans to finance trade credit and advances, finance leases, repurchase agreements not classified as a deposit, and overdrafts

[4] Percentage change over corresponding period of previous year.

[5] Rupee and foreign currency deposits from domestic banks.

[6] Debts contracted with banks only.

Note: Figures may not add up due to rounding.

Chart 6.4 **Return on Assets of the Banking Sector**

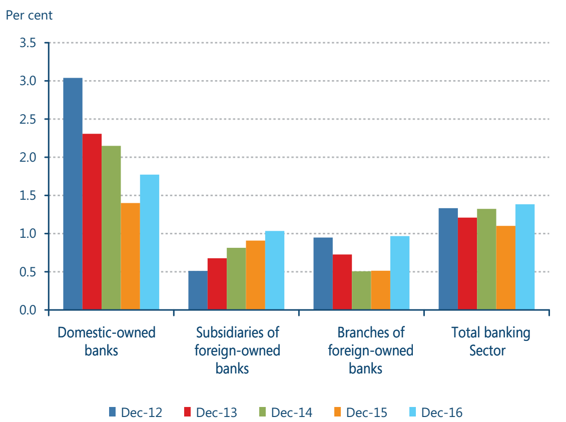
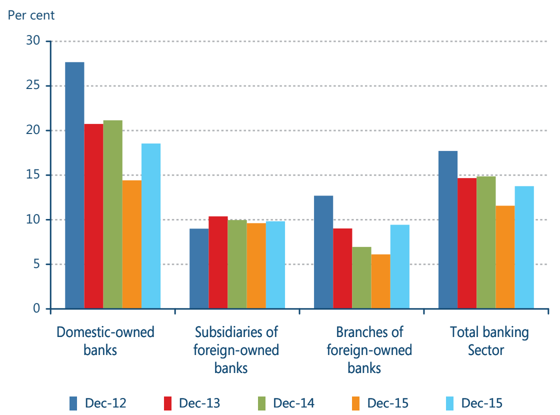


Chart 6.5 **Return on Equity of the Banking Sector**



improved from 1.1 per cent and 11.6 per cent as at end-December 2015 to 1.4 percent and 13.8 per cent as at end-December 2016, respectively.

Regulatory Capital

The Capital Adequacy Ratio of banks stood at a comfortable level of 17.5 per cent as at end-December 2016, which is well above the regulatory requirement of 10.0 per cent. In line with regulatory requirements, banks are phasing-in the Basel III capital framework. The capital base of the banking sector amounted to Rs124.7 billion as at end-December 2016, up by Rs4.6 billion from that of end-December 2015. Tier 1 capital ratio of banks hovered at around 15.9 per cent for the banking sector as at end-December 2016, down from 16.1 per cent as at end-December 2015. Tier 1 ratio continued to be highest for branches of foreign-owned banks at 22.7 per cent, followed by subsidiaries of foreign-owned banks at 19.1 per cent, and by domestic-owned banks at 13.4 per cent as at end-December 2016 (Chart 6.6).

Results from the Bank's newly developed top-down macro stress testing model show that the banking system is resilient to perturbations in economic activity, including shocks to GDP, interest rate and exchange rate (See Box II for more details).

The Bank continues to exercise caution with regards to Domestic-Systemically Important Banks (D-SIBs), in line with Guidelines issued in June 2014 for dealing with these banks. The systemic importance of these banks can be gauged from the potential contagious impact that one bank's failure could have on the entire financial system, through the network of connected contractual claims including interbank obligations, cross-border exposures, investments, as well as membership of conglomerate groups. D-SIBs are required to hold a capital surcharge ranging from 1.0 per cent to 2.5 per cent of their risk-weighted assets, depending on their systemic importance, with the surcharge being applicable over a four-year period.

Chart 6.6 Tier 1 Capital Ratio

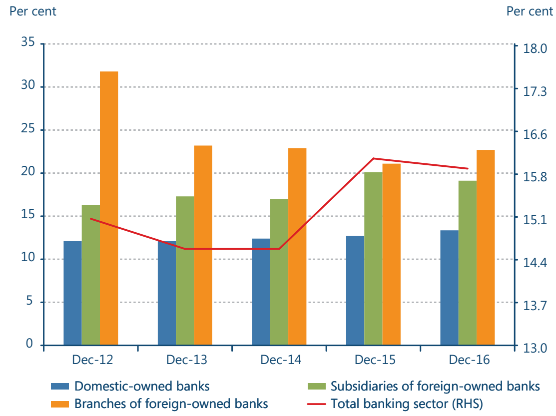


Chart 6.7 Non-Performing Loans of Banks

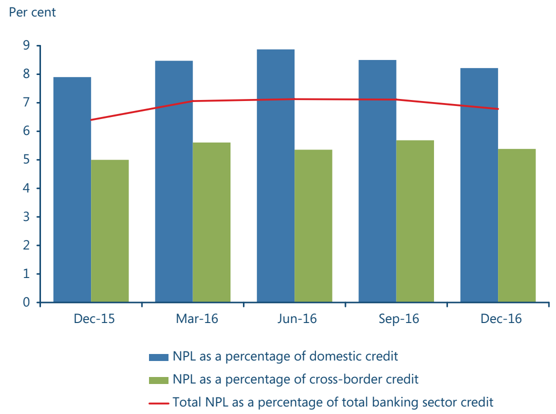
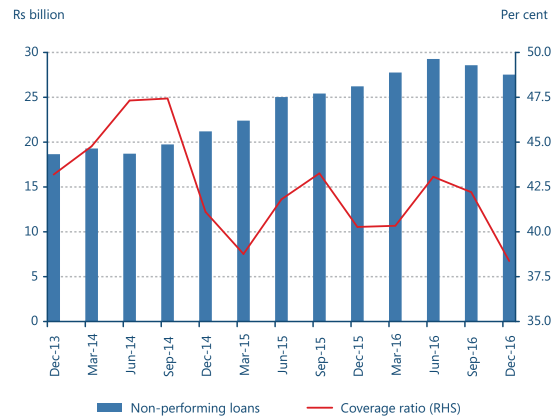


Chart 6.8 Non-Performing Loans in Mauritius and Coverage Ratio



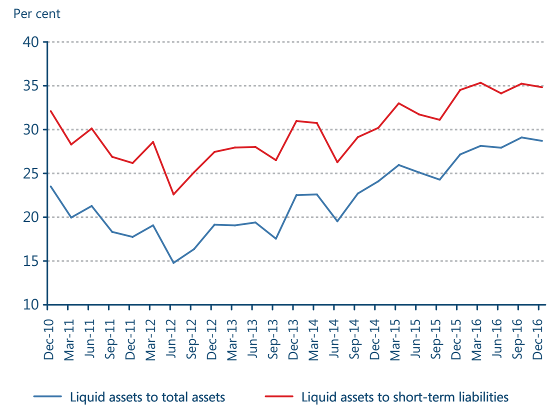
Asset Quality

The level of Non-Performing Loans (NPLs) in the banking sector continued its upward trend and amounted to approximately Rs46.0 billion as at end-December 2016, indicating a deterioration in asset quality and enhanced credit risks. Measured as a ratio of total credit facilities, impaired credit rose from 6.4 per cent as at end-December 2015 to 6.8 per cent as at end-December 2016. This deterioration in asset quality could mainly be explained on two grounds, namely rising impaired credit ratio for credit extended outside Mauritius from 5.0 per cent as at end-December 2015 to 5.4 per cent as at end-December 2016, and rising impaired credit ratio, from 7.9 per cent to 8.2 per cent, for credit extended within Mauritius. While the former remained more or less stable during year 2016, the latter showed an ascending tendency during 2016H1 but took a downward trend during 2016H2 (Chart 6.7).

On the domestic and more sectoral level, the NPL to gross loans in the traders sector declined from 13.0 per cent as at end-December 2015 to 11.8 per cent as at end-December 2016. Over the same period, the tourism sector showed some signs of deterioration, with the ratio of NPL to gross loans rising from 6.2 per cent to 7.9 per cent. Construction sector experienced some stress, despite a pick-up in performance in the second half of 2016, with the NPL ratio increasing from 8.9 to 9.2 per cent. Meanwhile, the Global Business Sector (GBC), which faced some uncertainties in 2016 over the revision to the DTAA treaty between Mauritius and India, witnessed a hike in NPL ratio from 3.6 per cent to 4.6 per cent. The importance of the GBC sector, in view of its complex inter-linkages to the banking sector, underscores the importance of accelerated efforts by the authorities to collect data on the sector so as to better track and monitor any potential sources of vulnerabilities that may unfold, going forward.

The macro stress testing model developed at the Bank highlights the importance of continued monitoring of asset quality in several of the heavy weight cyclical sectors. The sensitivity of asset quality in these sectors to the unfolding of macroeconomic events under adverse shock scenarios, underscores the importance of macroeconomic stability and of pro-active macroprudential policies as an

Chart 6.9 **Liquidity Ratios of Banks**



important pre-requisite for sustaining the quality of banks' portfolios.

Coverage ratio

The ratio of specific provisions to NPL, also known as the coverage ratio stayed broadly unchanged at 48.8 per cent as at end-December 2016, compared to its end-December 2015 level of 48.7 per cent. During the year 2016, it increased over the first three quarters of the year to an apex of 51.3 per cent at end-September 2016, before taking a downward trend in the last quarter to broadly settle at its beginning of year level.

The evolution in the level of specific provisioning during the year 2016 broadly mirrored the evolution of impaired credit during the year, albeit at a faster face. This tendency was pronounced for credit extended outside Mauritius, with the level of provisioning being made for impaired credit rising from 62.3 per cent at end-December 2015 to 64.6 per cent as at end-March 2016, and falling to 61.0 per cent as at end-June 2016, before picking up to 65.3 per cent at end-September 2016 and, finally, falling to 64.5 per cent at end-December 2016 (a level higher than its beginning-of-year level).

The coverage ratio for credit extended in Mauritius increased in the first half of 2016 from 40.3 per cent at end-December 2015 to 43.0 per cent at end-June 2016, before receding in the second half of the year to settle at 38.4 per cent at end-December 2016, a level lower than its beginning-of-year level (Chart 6.8). At a sectoral level, the coverage ratio for the construction and GBC sector declined from 36.6 per cent and 79.9 per cent at end-December 2015 to 33.3 per cent and to 52.1 per cent at end-December 2016 respectively. On the other hand, for the Tourism sector, coverage ratio for NPL improved from 13.9 per cent to 17.7 per cent over the same period.

Banks' Liquidity and Foreign Exchange Open Positions

Given the relative importance of deposits as source of their funding, banks in Mauritius hold a reasonable proportion of liquid assets to manage liquidity risks. The latter arises from essentially from the intermediation role of banks in transforming maturity of short-term liabilities, especially deposits, into long-term assets, especially loans.

Measured as a ratio of total assets, liquid assets of the banking system which essentially comprise balances with the Bank of Mauritius, holdings of securities, and short-term placements with banks abroad improved from 27.8 per cent as at end-December 2015 to settle at 28.7 per cent at end-December 2016 (Chart 6.9). This can be explained by the increase of 2.4 per cent in liquid assets from Rs367.6 billion to Rs376.6 billion and by the decrease of 0.5 per cent in total assets from Rs1.320.0 billion to Rs1, 313.4 billion during the year ended 31 December 2016. During that period, the liquidity asset ratio remained stable for domestically-owned banks at about 24 per cent, while for subsidiaries of foreign banks, it improved from 31.5 per cent to 34.4 per cent. On the other hand, the liquidity ratio somewhat deteriorated for branches of foreign banks from 25.7 per cent to 20.6 per cent.

Table 6.4: Credit Concentration Risk

	Percentage of aggregate large exposures to capital base	Percentage of aggregate large exposures to total credit facilities
Dec-14	218.5	31.7
Mar-15	205.6	31.5
Jun-15	218.3	34.2
Sep-15	207.4	32.6
Dec-15	198.6	32.8
Mar-16	206.7	38.9
Jun-16	204.8	38.2
Sep-16	194.1	35.7
Dec-16	175.6	29.6

Table 6.5: Exposure of Banks to Ten Largest Borrowers

	Ten largest borrowers (Rs million)	Ten largest borrowers to total large exposures (Per cent)	Ten largest borrowers to total capital base (Per cent)
Dec-14	81,177	33.2	72.6
Mar-15	83,977	32.8	67.4
Jun-15	88,703	34.2	74.6
Sep-15	87,049	35.2	73.0
Dec-15	89,146	37.0	73.6
Mar-16	102,001	39.1	85.0
Jun-16	94,043	39.0	77.0
Sep-16	94,558	42.0	79.0
Dec-16	86,035	39.0	69.0

Liquidity risks prospects may be explored further by looking at the evolution of maturity mismatches and currency mismatches in the banking system's assets and liability structure. Regarding the former, the ratio of liquid assets to short-term liabilities which comprise unsecured wholesale deposits, interbank borrowings, short-term retail deposits, fell from 35.5 per cent as at end-December 2015 to reach 34.8 per cent as at end-December 2016, mainly on account of the increase of 4.4 per cent in short-term liabilities from Rs1,036.8 billion to Rs1,082.7 billion. Both subsidiaries and branches of foreign banks experienced deterioration in the ratio of their liquid assets to short-term liabilities, notably, from 42.9 to 41.9 per cent (for subsidiaries) and from 28.6 to 24.1 per cent (for branches) during that period. However, domestic-owned banks experienced an improvement in their ratio, with an improved bulwark from 28.8 per cent to 29.5 per cent.

Banks engaged in cross-border activities manage their funding and liquidity risks across currencies by matching their liabilities, to the extent possible, with assets in the same currency and maturity buckets. Regulation in Mauritius does not allow individual banks to have a net foreign exposure position of more than 15 per cent of Tier 1 capital. The overall net foreign exchange exposure ratio has remained below this prudential limit in recent years, although it stood at 3.5 per cent as at end-December 2016, compared to 3.3 per cent as at end-December 2015. Subsidiaries of foreign banks experienced enhanced net foreign exchange exposure over this period, while domestic-owned banks and branches of foreign banks saw a retrenchment in their net foreign exchange position.

Overall, given that balance sheets of banks in Mauritius exhibited fairly low currency mismatches, the risk of loss from adverse movements in foreign exchange rates was assessed to be relatively benign. The banking sector in Mauritius remains well-funded and liquid. Under the Basel framework, two specific recommendations have been made pertaining to liquidity of banks in general, namely the Liquidity Coverage Ratio (LCR) which ensures availability of liquid assets to withstand a 30-day adverse shock scenario and a Net Stable Funding ratio (NSFR) which ensures that banks fund their activities using more stable sources of funding. In Mauritius, an updated Guideline on Liquidity Risk, onboarding principles based on LCR is currently in the stage of preparation for future implementation so as to ensure a more robust liquidity risk management framework of the banking system.

Concentration of Credit

Credit concentration is an important risk to monitor for financial stability purposes, given the weights of some sectors in banks' loan portfolios, as well as the presence of large groups and financial conglomerates. Regarding one important financial soundness metric for credit concentration, namely the ratio of aggregate exposures to total credit, two diverging patterns were noticeable during the course of 2016: the proportion of total credit accounted for by large exposures increased during the first half of 2016, before the trend reversed in the second half. From end-December 2015 to end-December 2016, this ratio declined by 3.2 percentage points to stand at 29.6 per cent. Over the same period, the ratio of large exposures to capital base contracted from 198.6 per cent to 175.6 per cent, with a noticeable uptick in the first quarter of the year (Table 6.4).

Although banks' exposures to the ten largest borrowers rose from Rs89.1 billion (73.6 per cent of total capital base) at end-December 2015 to reach Rs102.0 billion (85.0 per cent of capital base) at end-March 2016, this somewhat lessened over the remaining quarters of the year before settling at about Rs86 billion (69.0 per cent of capital base) at end-December 2016. Gauged from a different metric, namely as a percentage of total exposures, exposure to ten largest borrowers was on the rise during the first three quarters of the year (from 37.0 to 42.0 per cent), before retrenching to 39.0 per cent in the last quarter of 2016 (Table 6.5).

On an overall basis, while the credit concentration ratio continued to remain below the aggregate prudential limit of 800 per cent of the capital base, vigilance must be exercised since the attendant financial stability risks arising from a potential unwinding of credit concentration risks can be long-lasting.

6.2 Non-Bank Financial Intermediaries

Non-Bank Deposit-Taking Sector

Non-Bank Deposit-Taking Institutions' (NBDTIs) main activity relates to the mobilisation of deposits and the granting of leasing and loan facilities to individuals and corporates. There were eight NBDTIs in operation as at end-December 2016. Business operations of NBDTIs progressed over the year ended 31 December 2016 at a slower pace than in the previous year.

Year-on-year growth of total assets of NBDTIs slowed down by 0.8 percentage points to reach 6.8 per cent at end-December 2016, compared to end-December 2015 (Chart 6.10). Over the same period, there was a slowdown in growth of deposits from 6.3 per cent to 4.3 per cent. During the course of 2016, the structure of assets and of liabilities of NBDTIs also experienced changes. As at end-December 2016, around 71.1 per cent of total assets of NBDTIs constituted of loan and leasing facilities, a mild deterioration compared to end-December 2015 when this figure stood at 73.2 per cent. On the liabilities side, total deposits accounted for 57.5 per cent of the total liabilities of NBDTIs at end-December 2016, a deterioration of 1.4 percentage points compared to end-2015.

Liquidity

With liquidity ratios above the statutory minimum of 10 per cent, NBDTIs remained relatively liquid, despite a deterioration in several liquidity metrics for NBDTIs. The shrinking value of liquid assets of NBDTIs during year 2016 accounted for much of this deterioration. Measured as a ratio of total assets, liquid assets fell to 11.9 per cent at end-December 2016, down from 12.8 per cent at end-December 2015. The ratio of liquid assets to deposits also deteriorated over the same period, in part due to an expanding deposit base of 4.2 per cent during 2016. The proportion of deposits accounted for by liquid assets in NBDTIs fell from 21.7 per cent as at end-December 2015 to 20.7 per cent as at end-December 2016. Important patterns in the evolution of both metrics were noticed during the course of 2016. During the first half of 2016, both ratios deteriorated, before picking up in the second half of the year to settle at their end-December 2016 levels (Chart 6.11).

Chart 6.10 Y-o-Y Growth of Total Assets and Deposits of NBDTIs

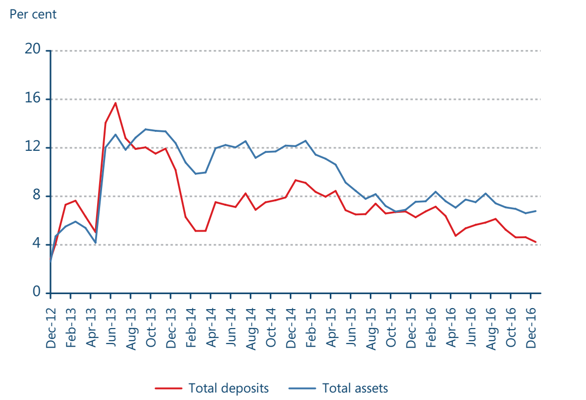


Chart 6.11 Liquidity Indicators of NBDTIs

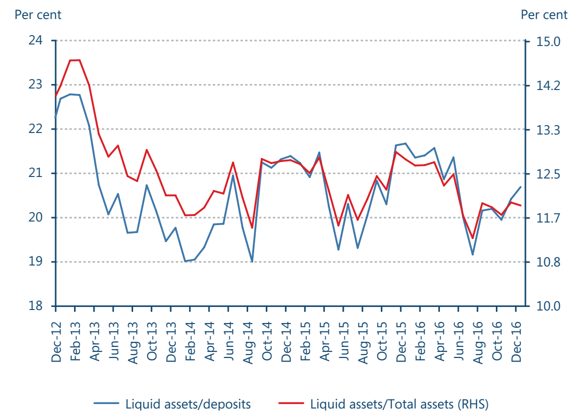
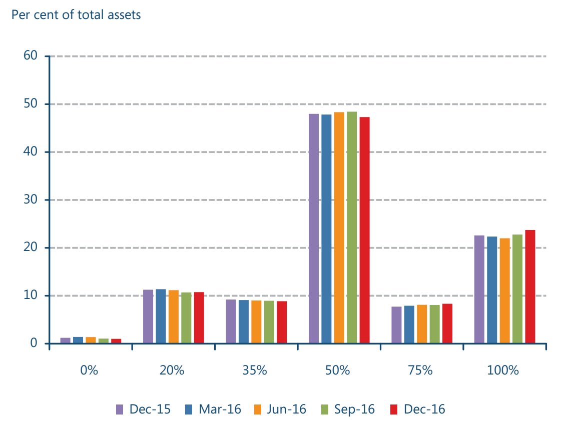


Chart 6.12 Risk Diversification Matrix of NBDTIs



Capital Adequacy

The NBDT sector remained adequately capitalized during the period under review. The aggregate Capital Adequacy ratio of NBDT sector stood at 30.5 per cent as at end-December 2016 compared with 29.0 per cent as at end-December 2015, indicating greater resilience and enhanced capacity of NBDTIs to withstand balance sheet shocks. Assets of NBDTIs remained concentrated in the 50.0 per cent and 100.0 per cent risk-weight buckets. Around 46.0 per cent and 24.0 per cent of total NBDTIs' assets were classified in the 50.0 per cent and 100.0 per cent buckets respectively as at end-December 2016. This is broadly comparable to 2015 figures (Chart 6.12).

Sectoral Credit and NPL

Total credit extended by NBDTIs grew at a much slower pace in 2016, compared to the year before. As at end-December 2016 (end-December 2015), credit expanded by 8.6 per cent (16.0 per cent) on a year-on-year basis. The personal sector accounted for the bulk of total credit allocated (62.0 per cent), followed by the construction sector (13.0 per cent), Traders (3.0 per cent), Manufacturing (3.0 per cent), and Tourism (1.0 per cent).

Asset quality of NBDTIs deteriorated during year 2016, with the ratio of NPL to total credit rising from 6.0 per cent at end-December 2015 to 6.3 per cent at end-December 2016, with impaired credit rising more than proportionately compared to the growth in total credit. Among all sectors to which NBDTIs lend, the construction sector continued to face the highest NPL ratio which stood at 22.0 per cent as at end-December 2016 (Chart 6.13). The personal sector which receives the bulk of credit experienced a deterioration in asset quality with NPL ratio moving from 2.0 per cent at end-December 2015 to 2.8 per cent at end-December 2016. Impairment in the personal sector is relatively lower at end-December 2016 than in other less heavyweight sectors such as traders, manufacturing, tourism, let alone, construction.

6.3 Insurance Sector

Long Term Insurance Business

During 2015, eight licensed long-term insurers were in operation, and one new license was issued to the National Insurance Company (NIC Life), with BAI Co (Mtius) Ltd (BAI) having transferred its conventional business portfolio to NIC Life. The BAI was put under special administration, and its going concern was split between NIC Life and the National Property Fund (NPF). The majority of the company's single premium policies - known as 'Super Cash Back Gold' (SCBG) and estimated at about Rs20 billion - were transferred to the NPF and consequently, this transfer has brought about a striking disruption to long-term market

Chart 6.13 **NPL as a Ratio of Sectoral Credit in Key Sectors**

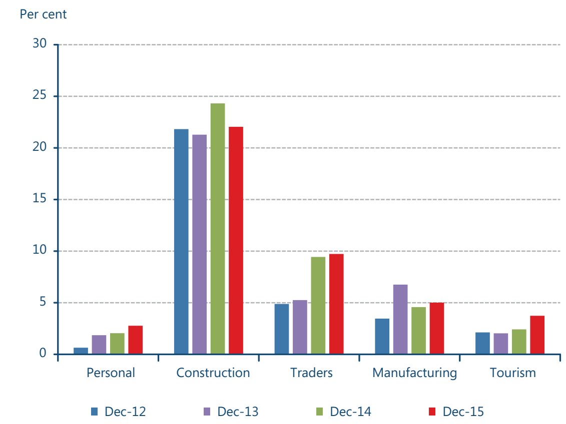
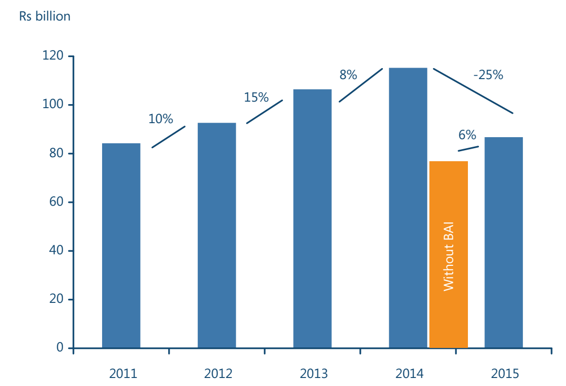


Chart 6.14 **Value of Assets of Long-Term Insurance Segment**



Source: Financial Services Commission.

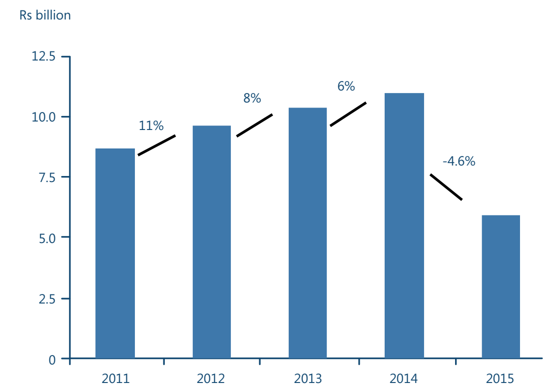
data for the insurance sector. As a result, the analysis provided in this section pertains to the performance of the insurance sector that excludes BAI and NIC Life for the year 2015, and consolidated data for the year 2015 is not strictly comparable to previous years.

Excluding data pertaining to the BAI and the NIC Life for the year 2015, the assets of long-term insurers rose by an average yearly rate of 2 per cent over the period 2011 to 2015. As at end-December 2015, total assets of long-term insurers stood at Rs87 billion, with the exclusion of BAI resulting in about 25 per cent decline in the value of total assets for the long-term insurance sector (Charts 6.14). Excluding the data for BAI, an increase of 6 per cent in 2015 was recorded in total assets, from Rs82 billion in 2014. The five-year average investment in government bonds and equities represented 14 per cent and 21 per cent, respectively, of the asset portfolio of insurers. Over the recent years, investment in 'other assets' was generally being favoured to traditional instruments such as properties, equities and bonds.

Capital and reserves held in the books of long-term insurers dropped by Rs5.2 billion as at end-December 2015 to Rs6.0 billion as at end-December 2014 (Chart 6.15). The ratio of capital and reserves to the Life Fund segment stood at 12 per cent for 2015 compared to 15 per cent for 2014. With the introduction of the Insurance (Risk Management) Rules 2016, it is projected that capital and reserves will maintain an upward trend in future years, thereby contributing to reduce the likelihood of possible failure of insurers.

Gross Premiums have traditionally enjoyed yearly increases of about 7 to 8 per cent. However, with the exclusion of BAI, gross premiums suffered a decline of 43 per cent, from Rs16 billion in 2014 to Rs9 billion in 2015. With the omission of BAI data for 2014, gross premiums rose by 14 per cent in 2015 from Rs8 billion in 2014 (Chart 6.16). Likewise, new policies decreased from 52,571 in 2014 to 38,257 in 2015. The effect of BAI resulted in a significant decline of 27 per

Chart 6.15 **Capital and Reserves of Long-Term Insurance Segment**



Source: Financial Services Commission.

Table 6.6: Average Solvency Margin

	Average Solvency Margin 2014	Average Solvency Margin 2015
Big Companies (G Premiums > Rs 1bn)	295 per cent	542 per cent
Medium Companies (G Premiums > Rs 500m, < Rs 1bn)	122 per cent	144 per cent
Small Companies (G Premiums < Rs 500m)	157 per cent	137 per cent

Source: Financial Services Commission.

Table 6.7: Average Surplus

	Average Surplus 2014 *Rs (million)*	Average Surplus 2015 *Rs (million)*
Big Companies, gross premium above Rs 1 billion	1,478	2,380
Medium Companies, gross premiums between Rs 500 million and Rs 1 billion	204	204
Small Companies, gross premiums below Rs 500 million	48	89

Source: Financial Services Commission.

cent from 2014, while policies in force followed the same declining rate of negative 25 per cent. Business in force stood at 281,884 in 2015, down from 431,057 in 2014. By excluding BAI data in 2014, policies in force in 2015 increased by 4 per cent from 271,599 in 2014 (Chart 6.17).

Solvency Position

In terms of the provisions of the Mauritius Insurance Act 2005, long-term insurers are subject to a risk-based minimum capital, also referred to as 'solvency margin'. Six long-term insurers were required to submit financial accounts. For the financial year 2015, the solvency position of these insurers is provided in Table 6.6.

The average solvency margin of big and medium companies has improved over the year whilst that of small companies is observed to have weakened as compared to the previous year.

Surplus of the Life Fund

Surpluses are determined by the insurer's statutory Actuary on a yearly basis. The valuation of liabilities and determination of surpluses are prescribed in the Insurance (Long-Term Solvency Business Solvency) Rules 2007. The surplus position for the financial years 2014 and 2015 are shown in Table 6.7. Big and small companies registered almost a two-fold increase in their average surplus over the year, while that of medium companies remained flat at Rs204 million.

Effect of Interest Rate

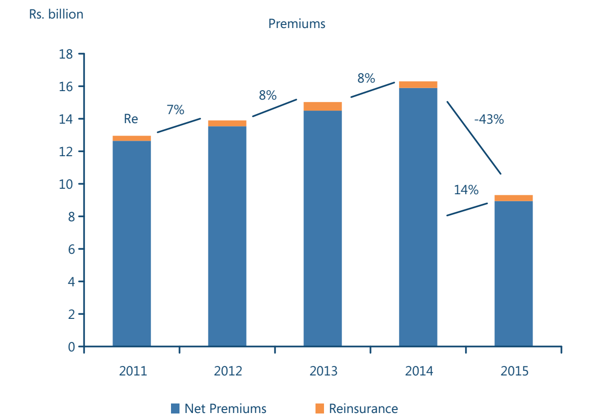
An analysis of surplus of the six insurers with regard to 'investment returns' and 'interest rate' is provided in Table 6.8.

Despite negative results from departure in assumptions (investment returns), the reinforcing of the actuarial reserves (change in basis) has resulted into positive overall surpluses (Table 6.7).

General Insurance Business

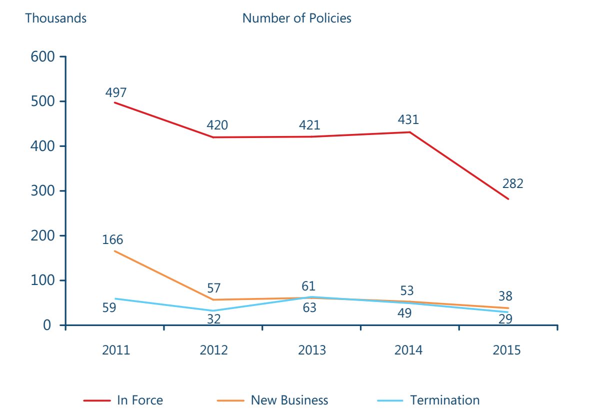
During 2015, a new license was issued to NIC General Insurance Co Ltd and as at 31 December 2015, fifteen domestic insurers were licensed to conduct general insurance business. Total value of assets rose by 11 per cent, from Rs15.1 billion as

Chart 6.16 Net Premiums and Reinsurance



Source: Financial Services Commission.

Chart 6.17 Number of Policies: In Force, New Business and Termination



Source: Financial Services Commission.

Table 6.8: Effect of Interest Rate

(Rs million)

	Investment Returns		Change in Basis (economic)		Change in Provision (interest)		Total	
	2014	2015	2014	2015	2014	2015	2014	2015
Big Companies (G Premiums > Rs 1bn)	192.3	-171.8	-535	-187.2			-342.7	-359.1
Medium Companies (G Premiums > Rs 500m, < Rs 1bn)	-7.4	-175.5	-26	-39.6			-100	-215.1
Small Companies (G Premiums < Rs 500mn)	3.3	6.3	-13	-7.1	9	-5.8	-0.7	-6.6

bn: billion *mn: million*

Source: Financial Services Commission.

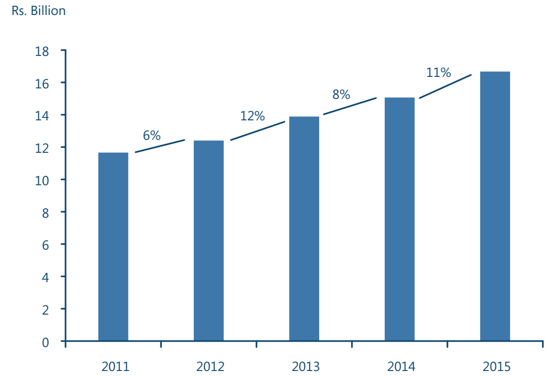
at end-December 2014 to Rs16.7 billion as at end-December 2015 (Chart 6.18). The 5-year average rate of increase in total assets stood at 9 per cent in 2015 (4% preceding 5 year moving average). rate of increase in total assets stood at 9 per cent in 2015 (4% preceding 5 year moving average).

During the period 2011 to 2015, the average proportion of assets in 'equities' and 'cash equivalents' was at 13 per cent and 20 per cent respectively (14 per cent and 22 per cent respectively preceding moving average). During 2015, a huge shift to 'government bonds' when compared to 'cash equivalents' was noted, and consequently, holdings in 'government bonds' rose by 134 per cent, while holdings in 'cash equivalents' fell by 3 per cent.

Over the past five years, the amount of 'other assets' stood at an average of 57 per cent. The major component of 'other assets' has been 'reinsurance receivable', which tantamount to the industry's heavy dependence on reinsurance for risk management. Capital and reserves have increased from 7.0 billion in 2014 to Rs 7.6 billion in 2015. The Capital and reserves tends to be increasing at a yearly rate of 13 per cent compared to the last 5 years. The majority of companies held a solvency ratio above 150 per cent although few entities were below that level but were subject to continuous monitoring.

In comparison to technical reserves, capital and reserves comprised the larger composition of liabilities held by General Insurers. While capital and reserves averaged 45 per cent of total liabilities for the last five years, technical reserves remained at a lower average of 44 per cent of total liabilities. With the coming into force of the new Insurance (Risk Management) Rules 2016, insurers would be called to maintain stronger reserves compared to capital.

Chart 6.18 Value of Assets of General Insurance Business



Source: Financial Services Commission.

In 2015, the FSC conducted a survey on general insurers' claims triangle for years 2010-13. Claims data was collected by accident years and each general insurers' outstanding claims reserves were recomputed using 4 different actuarial techniques. Except for some misreporting of data, no major issues were noticed in regard to insurers' outstanding claims reserve, including incurred but not reported (IBNR) reserves.

Gross premiums for motor business stood at Rs 2.9 billion in 2015, representing an increase of 3 per cent over the previous year. Gross Premiums for non-motor business rose marginally by 1 per cent during the year and stood at Rs4.6 billion in 2015. Motor premiums have been increasing at a 5 year average rate of 3 per cent yearly (6 per cent preceding 5 year moving average) whereas non-motor premiums have been increasing at 7 per cent yearly for the last 5 years (9 per cent preceding 5 year moving average).

Table 6.9: Solvency Position

	Ten largest borrowers *(Rs million)*	Ten largest borrowers to total large exposures *(Per cent)*
Big Companies (G Premiums > Rs 1bn)	236 per cent	222 per cent
Medium Companies (G Premiums > Rs 500m, < MUR 1bn)	324 per cent	347 per cent
Small Companies (G Premiums < Rs 500m)	263 per cent	341 per cent

Source: Financial Services Commission.

Motor gross claims for 2015 stood at Rs2.0 billion, up from Rs1.6 billion for 2014. Non-motor gross claims amounted to Rs2.1 billion for 2015 compared to Rs2.3 billion for 2014. Non-motor claims were heavily reliant on reinsurance as compared to motor claims. The average increase for motor claims over the past five years hovered around an annual rate of 10 per cent compared to 6 per cent for non-motor businesses.

Underwriting profits decreased to Rs270 million in 2015, down from Rs600 million in 2014. In contrast, operating profits dropped by 24 per cent from Rs1,041 million in 2014 to Rs788 million in 2015. The yearly average rate of change for the operating profits for the last 5 years stood at negative 9 per cent. The number of policies for motor business stood at 353,153 in 2015 compared to 333,604 in 2014. On the other hand, the number of policies for non-motor business was at 170,400 in 2015, down from 180,500 in 2014.

Most of the general insurance business was classified under motor insurance averaging 67 per cent for the last 5 years, whereas non-motor averaged 33 per cent, out of total policies in force. The number of motor claims stood at 47,624 for 2015 (47,118 for 2014). On the other hand, the number of non-motor claims figured out of 170,132 in 2015 (231,776 in 2014).

The majority of claims belonged to non-motor business averaging to 82 per cent for the last 5 years (81 per cent preceding 5 year moving average), whereas the motor business averaged 18 per cent, out of total claims (19 per cent preceding 5 year moving average).

Solvency Position

For the financial year ended December 2015, the solvency position of the fourteen general insurers are provided in Table 6.9. The average solvency position of small and medium companies improved over the year while that of big companies were somewhat weaker compared to the previous year.

6.4 Pension Funds

Private Pension Schemes

The Private Pension Scheme Act 2012, which came into force on 01 November 2012, and requires private pension schemes to submit actuarial valuation reports to the FSC on a triennial basis. As of date, 25 private pension schemes with defined benefit arrangements have had their actuarial valuations performed and these reports have been submitted to the FSC.

Funding Ratio and Surplus Positions

With the coming into force of the Private Pension Schemes (Technical Funding Requirement) Rules 2013, defined benefit schemes are required to maintain a funding ratio of at least 100 per cent. Compliance with legal provisions relating to technical funding would ensure that private pension schemes have adequate technical provisions to meet future liabilities (Table 6.10).

Twenty-three out of the twenty-five defined benefit private pension schemes reported on analysis of surplus which showed results regarding 'investment returns' and 'change in basis' which is the gap between the assumptions that affects the technical provisions rather

Table 6.10: Funding Ratio

No. of Pension Funds	Range
4	More than 100 per cent
4	Between 90 per cent and 100 per cent
12	Between 60 per cent and 100 per cent
5	Less than 60 per cent

Source: Financial Services Commission.

Table 6.11: Surplus Position of Pension Funds for Financial Years 2012-14

	Average Surplus *(Rs million)*
Aggregate for the 25 private pension schemes	-233.86
Highest value	38
Lowest value	-1416

Source: Financial Services Commission.

than the absolute amounts (Table 6.11). In the majority of cases, poor performance was noted in respect of investment assumptions. It was also noted that most of these schemes experienced surpluses in terms of contribution amounts. This brought down the overall deficit. Investment return performance was the major factor that resulted in the deficits of these schemes.

Regulatory Initiatives

New Insurance (Risk Management) Rules will come into force as from 01 July 2017, requiring each insurer to develop, inter alia, on a yearly basis, (a) a risk appetite statement; (b) a risk management strategy; (c) a 3-year rolling business plan; (d) an own-risk and solvency assessment (ORSA); (e) a liquidity policy. Insurance companies will henceforth be bound to undertake a committed approach towards risk management with a view to building up the resilience of the sector against shocks.

The Online Data Capture System was launched in February 2016 with the aim of facilitating submission of survey data and relevant statutory fillings online, including annual reports and audited financial statements in an efficient and effective manner. A circular letter was also issued in January 2017 to introduce the Financial Services (Exemption from Approval of Controllers and Beneficial Owners) Rules 2016, where provision is made to exempt from seeking the approval of the FSC in instances where there is an issue or transfer of shares which do not carry voting rights in the licensee.

Table 6.12: Analysis of Surplus

	Investment Returns (Rs million)	Change in Basis (economic) (Rs million)	Interest on Surplus/Deficit (Rs million)	Total (Rs million)
Total average value	-58.85	-53.41	-68.91	-181.17
Highest value	9	773.1	13.6	
Lowest value	-469.4	-797	-460.3	

Source: Financial Services Commission.

BOX II: STRESS TESTING THE BANKING SYSTEM

Stress testing involves assessing the resilience of a system by putting a severe amount of pressure on it. Applied to the banking system, it involves assessing how banks would cope with extreme but plausible adverse hypothetical scenarios which are more severe than expected. Examples of these scenarios include severe recessions, sharp contraction in house prices, rising interest rates and rising unemployment. Stress tests can be applied to assess solvency issues (e.g., whether banks' capital can withstand certain shocks) or to assess liquidity situation of banks (e.g., whether banks will be able to sell assets or to refund / refinance themselves under constrained situations to meet contractual payment obligations). The stress testing value-chain for solvency typically involves mapping the links from adverse scenarios to identified risk factors inherent in the banking system, and ultimately to banks' profitability and capital positions.

The choice of an appropriate modelling technique from the smorgasbord of econometric tools available is important to quantify the impact of the adverse scenarios on banks' profits and balance sheets. From the vantage point of the regulator, stress tests support risk measurement and risk management and can complement existing prudential policy aimed at enhancing soundness of individual banks (microprudential policy) and of the entire banking system (*macroprudential policy*). The former is usually implemented at the individual bank level (bottom-up approach) while the latter is usually implemented by the regulator (top-down approach[1]). One of the advantages of the top-down approach is that it takes into account feedback and amplification mechanisms following the interractions between banks or between banks and financial markets. As such, they help gauge the importance of systemic risks in a jurisdiction.

Stress Tests form the kernel of the IMF's Financial Sector Assessment Program (FSAP) and have gained prominence in some of the world's various jurisdictions, especially in the aftermath of the 2008 Global Financial Crisis (GFC). The rest of this box is organized as follows. Section A provides an overview of stress testing pursued in some of the main financial jurisdictions of the world. Section B provides the reader with some insights about the stress testing model developed at the Bank of Mauritius. Finally, Section C provides some eye-opening remarks about the importance of judiciously using stress tests for the very purposes for which they have been designed.

A. Stress-Testing in other Jurisdictions

IMF FSAP

IMF stress tests under the Financial Sector Assessment Program (FSAP) are designed to support financial stability assessments and are usually adaptable to each individual country's circumstances. Before the 2008 GFC, the onus of FSAP stress tests was on solvency risks of banks. After the 2008 GFC, the scope for risk assessment was broadened to incorporate market and liquidity risks. More recently, there have been efforts to onboard other financial institutions such as pension funds and insurance into the stress testing assignments. Efforts to explore the systemic interconnectedness among financial institutions are also currently under way.

[1] *Throughout this Box, reference will be made to the Top-Down (i.e., regulator's) approach, unless otherwise stated.*

US FED

In 2011, the US authorities launched the Comprehensive Capital Analysis and Review (CCAR). The CCAR incorporates results from stress tests required under the Dodd-Frank Act (DFAST), topped up with other requirements including a qualitative assessment of risk management practices in banks, capital plans and the results of banks' own stress test models. The DFAST's practice of building a severe and adverse scenario is essentially countercyclical in nature. Thus, if the economy is going through the upswing phase of the business cycle (i.e., the lower unemployment currently is), the larger the shock to unemployment that will be required as part of an extreme but plausible scenario. Unemployment, stock prices, GDP, interest rates and exchange rate are the usual macroeconomic variables that get shocked to assess the resilience of the US banking system.

EU

Responsibility to conduct EU-wide stress testing exercise migrated from the Committee of European Banking Supervisors (CEBS) to the European Banking Authority (EBA) in 2011. For year 2016, 51 banks representing about 70 percent of EU banking sector assets participated in the test across the EU. Macroeconomic scenarios are developed by the European Central Bank and European Systemic Risk Board (ESRB) and captures systemic risks that can materially pose a threat to the EU financial sector.

Bank of England

The Bank of England has developed a new stress testing framework and ran the first test in 2016. Seven UK banks, representing about 80 percent of total lending, took part in the tests. Scenarios are designed as per the judgements of policymakers on risks associated with the concurrent state of the financial cycle. Scenario variables include credit variables, financial market variables and other asset prices. The hurdle rate which is crucial in determining the 'pass / fail' criterion of banks is set at a level which is higher than the internationally agreed minima applying to all banks.

Bank of Japan

The Bank of Japan runs a semi-annual top-down macro stress test which appears in their Financial System Report. Stress testing is carried out using data for about 350 banks, which include large, medium and small banks. Macroeconomic scenarios reflect the state of the macro-financial situation of the country. The framework is designed to help the Bank of Japan to analyse feedbacks and spillovers in a stress, between the banking and macroeconomic sectors, as well as across banks.

B. Stress-Testing at the Bank of Mauritius[2]

Stress testing models adopted in various jurisdictions have an element of commonality in their approach, although they tend to differ in substance or in the exigencies required for modelling. The Macro-based Stress-Testing model being developed at BoM uses a standard top-down approach which is on par with the ones utilized in the some of major jurisdictions around the world. Coverage is extended to 14 banks[3] over a period running from 2009Q1

[2] A top-down liquidity risk LCR template is currently being formalized. The LCR template will enable BoM to gauge the impact of liquidity scenarios on liquidity situation of banks. This template will serve as a prelude to developing a more well-entrenched liquidity stress testing model.

[3] Banks have been excluded on the basis of size and nature of activity.

till 2015Q4 (projection period: 2016Q1-2018Q4). Nine sectors have been covered, namely, manufacturing, construction, tourism, ICT, trade, personal, agriculture, infrastructure, financial services, and transport[4]. A dynamic Generalized Methods of Moments (GMM) model, taking into account the endogeneity and non-stationarity of regressors, was estimated on a sectoral basis to identify statistically-significant macroeconomic variables, around which an appropriate adverse scenario can be built. The results are consolidated across all sectors for each bank and the links between bank profitability and capital position established. A run of the model using consistent stressed scenarios including interest rate hike, exchange rate depreciation and declining GDP growth rate has shown that the banking system as a whole in Mauritius is resilient in capitalization terms.

C. Some Caveats about Stress Testing

Stress tests are a useful complement to Central Banks' existing repertoire of toolkits, including early warning indicators. However, they do not intend to be a panacea to all financial stability problems. They need to be carefully designed taking into account the specificities and realities of banks in the jurisdiction. Model audits must be performed regularly to ensure appropriate calibration of model parameters. Inappropriate use and communication of stress test results may lead to unnecessary panics in the vanguard of the banking community. Thus, it is not uncommon for Central Banks to invest in appropriate communication strategies in order to disclose the results of their top-down stress tests. Furthermore, the scenarios developed by the regulator must be shared with the banks so that appropriate simulations can be carried out at the individual-bank level taking into account the specificities of their business model using identical scenarios. The results can then be cross-checked with those of the regulator for validation purposes. Meanwhile, research is ongoing about building ways to strengthen amplification and feedback mechanisms in stress test models, to incorporate behavioral responses of banks, as well as to extend the scope of stress tests beyond the banking sector. Extending stress tests beyond banks is important in an era of complex securitization, financial engineering, and one in which risks can easily migrate to those institutions not covered by stress tests.

[4] *GBC data was also analysed but no significant relations could be unearthed from the regression results. Furthermore, while discussing with Supervision staff, it emerged that no information about sources and destinations of GBC flows that are intermediated through the Mauritian banking system.*

7. Payment Systems Infrastructure

Robust financial market infrastructures (FMIs) contribute to ensuring the resilience of the financial system. The Bank owns and operates two FMIs, namely the Mauritius Automated Clearing and Settlement System (MACSS) which is a real time gross settlement system, and the Port Louis Automated Clearing House (PLACH) wherein cheques and low value electronic payments are settled on deferred net settlement basis. The MACSS has been designated as an FMI of systemic importance.

During 2016, the FMIs have operated satisfactorily, without encountering any technical or operational weaknesses that would have had an impact on financial stability in Mauritius. The critical systems processed payments within the prescribed parameters with high degree of technical reliability and in a timely manner.

With the current pace of technological advancement in the domain of payment systems, banking and financial business are stepping into a digital era. Due to the growing number of payment operators coming from banking as well as non-banking sectors, the Bank deemed it appropriate to lay down the foundations of an enabling environment for heterogeneous payment systems to co-exist without jeopardizing the stability of the domestic financial system.

As advocated by the Committee on Payment and Market Infrastructures of the Bank for International Settlements, the Bank envisages to adopt the Principles of Financial Market Infrastructures with a view to mitigating risks associated with FMIs. This endeavour will ensure that the FMIs operate in line with international best practices. Accordingly, a full-fledged national payment systems legislation is under preparation to provide a strong legal foundation for the operations of the FMIs. A payment system oversight framework will concurrently be adopted shortly to ensure the pro-active monitoring of FMIs.

The Bank will also launch the National Payment Switch (NPS) which will open the way for inter-operable digital banking systems and innovation in the mode of payments. Under the NPS, all payments made via cards, mobile phones and internet based systems will be routed to a centralised system for authorisation and settlement. The NPS will henceforth provide a single platform for the integration of all electronic payment transactions, thereby leading to efficiency and cost-effectiveness in the payment systems in Mauritius.

Availability of MACSS

During 2016H2, MACSS operated smoothly without experiencing any significant downtime. MACSS settled 400,885 transactions for a total value of Rs1.3 trillion, representing an increase of 8.0 per cent in volume terms and of 17.8 per cent in value terms compared to 2015H2 (Chart 7.1). All transactions were settled with real-time promptness and without rejection, thereby underscoring the reliability of the system. In December 2016, a peak volume of 260,639 transactions was settled without transaction delay, evidencing that the system is optimally sized for various market volumes.

Chart 7.1 Transactions on MACSS

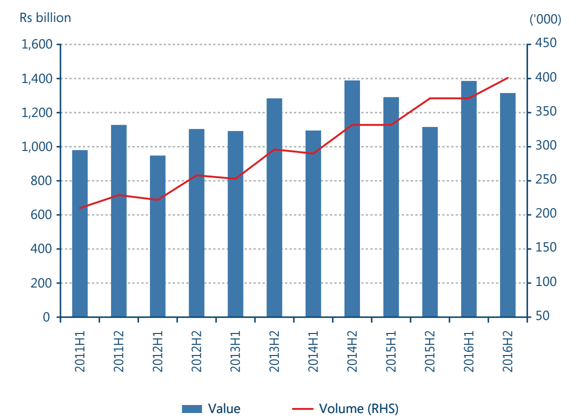
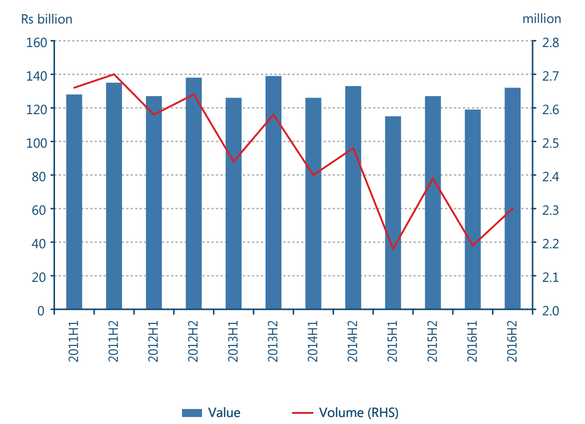


Chart 7.2 Cheques Cleared



Throughput on Bulk Clearing Systems

In 2016H2, 2,297,900 cheques were cleared compared to 2,386,587 for the corresponding period in 2015, representing a fall of 3.7 per cent. The value of cheques cleared, however, posted an increase of 3.5 per cent to reach Rs131 billion, mainly attributable to an increase in the volume of high value cheques (Chart 7.2).

Concurrently, during 2016H2, 1,916,015 Electronic Funds Transfers (EFTs) were cleared for a total amount of Rs53.0 million, representing respective increases of 10.9 per cent and 17.8 per cent, in volume and value (Chart 7.3). The value of EFTs cleared during 2016H2 constituted 28.7 per cent of total instruments cleared on the Bulk Clearing System (BCS) compared to 26.1 per cent during the corresponding period in 2015 (Chart 7.4).

The growing use of electronic payments in the payment mainstreams is deemed to influence the velocity of money circulation as the clearing cycles of EFTs are shorter than clearing of cheques.

Business Continuity Procedures

Given the systemic importance of payment systems in Mauritius, the Bank viewed that there was a need to implement a well-defined Business Continuity Plan where the systems would operate on fully redundant machines with real time replication to the Bank's Disaster Recovery site. Business continuity deals with unforeseen events such as hardware or software failures, communication outages or natural disasters. Those events, although statistically unlikely, can jeopardise the operations of the whole financial system. The Bank regularly conducts verification tests on its contingency arrangements through full-day operations from its Disaster Recovery site.

Oversight Framework

Safe and efficient systems are fundamental to money being an effective means of payment and to the smooth functioning of financial markets. Well-designed and managed systems help to maintain financial stability by preventing financial crises, and reduce the cost and uncertainty of settlement which could otherwise act as an impediment to economic activity. Payment and settlement systems must, therefore, remain functional even when markets around them are in crisis.

In accordance, the Bank holds a core responsibility of ensuring the safe and efficient functioning of the payment and settlement systems in Mauritius. Through the application of relevant standards and keeping a close monitoring of the payment systems, the Bank is able to achieve various objectives that include, *inter alia*, maintaining public confidence in the domestic currency, performing its role as lender of last resort, and utilising the payment systems as a transmission channel for implementing monetary policy. The oversight of payment systems has, thus, become a crucial element in the Bank's mandate of maintaining stability of the domestic financial system.

Chart 7.3 Electronic Clearing Transactions

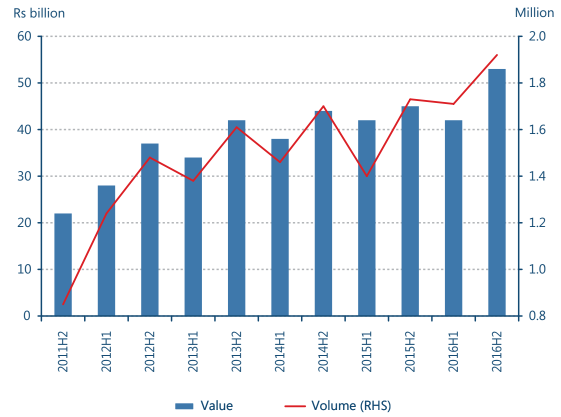
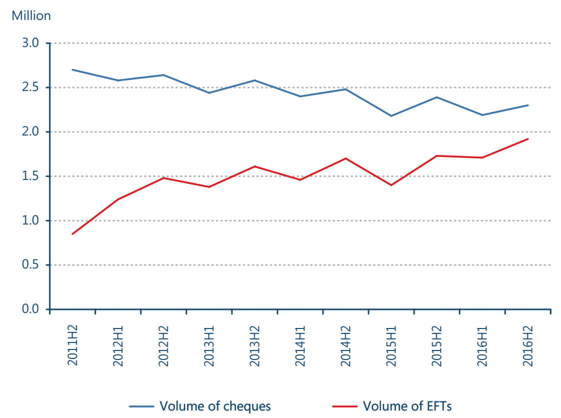


Chart 7.4 Volume of Cheques and EFTs on BCS



In terms of regulatory oversight, the Bank views the current approach to be essentially reactive, based on periodical self-assessment reports and incident-reporting by participants of the MACSS and BCS. From this perspective, the Bank proposes to shift to a more pro-active approach that will involve the implementation of a comprehensive payment system oversight. The new framework is principally intended to promote smooth and safe functioning of payment and settlement systems, protect the financial system from systemic risk, and safeguard public interest at large.

8. Risk Analysis of the Domestic Banking System

This section presents a summary assessment of the main risks to the domestic banking system. The heat-map below provides a synopsis of these risks and their likely evolution over the next 6 months.

Table 8.1: Risks to Financial Stability for the Upcoming Six Months

	Risk to domestic financial stability		Expected change*
	Jun-16	**Mar-17**	
Global Economy			
Global economic activity			Up ↑
Oil price			Up ↑
Food prices			Up ↑
Volatility (ViX)			Up ↑
Domestic Economy			
Economic growth			Up ↑
Inflation			Up ↑
Terms of trade			Down ↓
Domestic savings			Unchanged →
Investment/GDP			Up ↑
Exchange rate			Unchanged →
Household Debt Risks			
Household debt-to-disposable income			Up ↑
Household debt service-to-disposable income			Unchanged →
Corporate Debt Risks			
Corporate debt-to-GDP			Down ↓
Return on equity			Down ↓
Leverage			Down ↓
Banking			
Large exposures			Down ↓
Return on equity			Unchanged →
Asset quality (domestic market)			Up ↑
Cross-border exposures			Unchanged →

Risk analysis key

High		Medium		Low	
6	5	4	3	2	1

** Expected change between March 2017 and September 2017.*

Source: Bank of Mauritius staff estimates.

Risk Analysis of the Domestic Banking System

As an open small island economy, Mauritius' banking system is vulnerable to global economic developments through trade and financial linkages. While global growth has remained rather subdued in 2016, it is expected to gather momentum in 2017 with improved performance in our major trading partners. The brighter outlook, nevertheless, is not insulated from the potential tightening of credit conditions in the US in addition to trade protectionist measures. In the UK, as the outcome of the snap general elections and Brexit negotiations unfold, uncertainty surrounding policy could dissipate but markets may be subject to bouts of volatility amid legislative elections in major European countries and geopolitical tensions.

On the domestic front, GDP growth has improved, closing gradually the gap against potential output. While the economic environment remains challenging, activity is expected to benefit with a projected rebound in the construction sector and spillover effects to other sectors of the economy. Inflation has remained low and inflationary pressures are expected to remain contained, notwithstanding the rise in food and energy prices. The deficit in the current account was adequately financed from financial flows without undue pressure on rupee exchange rates. Nevertheless, the rise in global food and energy prices would have a bearing on merchandise trade deficit, going forward. The rupee remains upbeat amid capital inflows. The investment rate increased in 2016, driven by a rebound in private sector investment. Notwithstanding this improvement, the investment rate is still low but is projected to get a major boost with implementation of mega projects in 2017. This would impact positively on future growth momentum.

Indebtedness of households, as measured by the debt-to-disposable income ratio, has fallen in 2016 as credit facilities supplied to and availed by households grew relatively lower compared to their disposable income. The decline in the household debt-to-disposable income points to relatively lower risk to financial stability arising from indebtedness of households. While macroprudential policies are in place to prevent excessive leveraging of households, household debt-to-disposable income potentially remains vulnerable to macroeconomic shocks. Debt service costs of households have fallen with the cut in the Key Repo Rate that led to lower retail interest rates, thereby giving a boost to the purchasing power of households. The low interest rate environment should continue to support households in servicing their debt. Notwithstanding these improvements, continuous monitoring of indebtedness of households for assessment of emerging risks to financial stability is ongoing.

The deleveraging process is continuing for leading corporates in Mauritius though some still operate with relatively high leverage ratios. With the slowdown in credit growth, corporate debt-to GDP ratio has fallen. While corporates continue to operate in a challenging economic environment, profitability has fallen somewhat as shown by the decline in return-on-equity and lower coverage of interest payments. The cut in the Key Repo Rate in July 2016 has led to lower financing costs of corporates, thereby providing a breather for cash flows. Corporates remain vulnerable to unfolding of macroeconomic scenarios on the global as well as domestic front. The improving economic outlook would help to consolidate the financial position of domestic corporates.

Banks in Mauritius remains well capitalised with capital adequacy ratio above the regulatory minimum. The capital adequacy ratio stood at 17.5 per cent as at end-December 2016 compared to 17.8 per cent a year earlier and the quality of capital has increased with a higher share of Tier1 capital in total capital. Profitability improved with an increase in return-on-equity and banks were amply liquid. The ratio of aggregate large exposures of banks to their capital base has fallen to 175.6 per cent as at end-December 2016 compared to 198.6 per cent a year earlier. Nevertheless, banks in Mauritius remain exposed to concentration risk, including large and interconnected borrowers. The asset quality of deposit-taking institutions improved somewhat in the last quarter of 2016. The NPL ratio of the deposit-taking institutions dropped from 8.0 per cent as at end-June and end-September 2016 to 7.8 per cent as at end-December 2016, reflecting a decline in the level of non-performing loans.

Overall, risks to financial stability, assessed as at end-March 2017, have moderated slightly, reflecting the improvement in both household and corporate debt, while the domestic economic outlook appears to be improving on the back of the implementation of infrastructural projects and improved business climate following the enactment of the Business Facilitation (Miscellaneous Provisions) Act 2017.

BOX III: STATEMENT ON FINANCIAL STABILITY

The domestic financial system in Mauritius remained resilient during 2016. Financial intermediaries continued to operate in a sound environment, while remaining profitable despite a challenging economic conjecture characterized by subdued domestic demand and stalling international recovery.

Global economic activity improved in 2016, especially in the second half of the year, led by advanced economies and some large emerging market and developing economies. GDP growth improved in the US as firms grew more confident about future demand and remained solid in the UK, as the economy proved quite resilient in the aftermath of the Brexit. In many of the euro area countries, activity surprised on the upside, while in Japan growth was revised upwards. Despite these improvements, risks remain over the short-to-medium term especially regarding a faster than expected increase in US interest rates that could tighten financial conditions. In addition to threats of deepening geopolitical tensions, inward-looking policies could pose risks to global economic integration.

On the domestic front, GDP growth turned higher in 2016 on the back of improving activity in key sectors of the economy. Investment experienced a turnaround, with growth in private investment in 2016, for the first time in five years. While inflationary pressures remained benign, the deficit in the current account narrowed and the rupee remained broadly in line with fundamentals. Though the domestic economic outlook remains challenging, mega projects announced to start in 2017 would most probably support domestic growth this year. Statistics Mauritius expects real GDP growth to improve further to 3.8 per cent in 2017, supported by a rebound in the construction sector.

The banking sector remains supported by strong capital positions, despite a weakening of some financial soundness indicators. Over recent years, the capital adequacy ratio of the banking system has consistently hovered above the regulatory requirement of 10 per cent. Results from Macro-based Stress Testing model developed internally at the Bank show that, under a stressed scenario projection of subdued growth, mounting interest rates, and a weakening currency, the banking sector in Mauritius remains adequately capitalised. Going forward, the ongoing phased implementation of capital buffer consolidation in line with the Basel III framework should reinforce banks' capital as a buffer against shocks.

Nonetheless, as at December 2016, the asset quality of banks slightly deteriorated compared to a year before, with the NPL ratio rising from 6.4 per cent to 6.8 per cent, reflecting an impairment in both credit extended within and outside Mauritius. The coverage ratio which measures the ratio of specific provisions to non-performing loans deteriorated from 40.3 per cent as at end-December 2015 to 38.4 per cent as at end-December 2016. The proportion of bank credit extended to the ten largest borrowers as at end-December 2016 declined on a year-on-year basis. Although credit concentration indicators remain below prudential limits, their evolution – measured by aggregate large exposures as a ratio of total credit or as a ratio of capital base – needs to be monitored. As at end-December 2016, the banking system was assessed to be well-funded and liquid.

With the slowdown of credit extended by banks and continued rise in disposable income, indebtedness of households as measured by household debt to disposable income has fallen since the assessment made in the last Anual Report of the Bank. Debt service cost of household debt has also declined following the cut in the Key Repo Rate that led to lower interest rates. The lower indebtedness ratio and debt service cost point to lower risks to financial stability emanating from indebtedness of households. However, this should be interpreted with caution as households remain vulnerable to unfolding economic events. As regard corporates, the deleveraging process is ongoing but some still operate with a relatively high gearing ratio. The low interest rate environment contributed to a decline in the cost of debt of corporates while coverage of interest payment has increased. Corporate debt-to-GDP ratio has fallen in 2016 and the difference between the ratio and its underlying trend has dipped further into negative territory.

The payment system has operated efficiently during 2016 and transactions have been settled without delay or loss. A robust infrastructure system for payments is a critical requisite for maintaining the integrity of financial transactions and for safeguarding financial stability. It is expected that the upcoming National Payment Switch project which serves as a platform routing all electronic payments for authorization and settlement, will help enhance efficiency of the market infrastructure for transactions and contribute towards effectiveness of financial intermediation in Mauritius.

Overall, the financial system is assessed to be sound. The Bank continues its surveillance of the five Domestic Systemically Important Banks (D-SIBs) for better traction on financial stability. Following the revisions brought to the DTAA treaty between India and Mauritius in May 2016, the activities of GBC sector in banks are carefully being monitored by the Bank. Macroprudential measures have been introduced in 2014 with the aim of containing systemic build-up of vulnerabilities, including the pro-cyclical feedback between the financial sector and the real economy, over time. Projects in the pipeline such as establishment of: a crisis resolution regime; an asset management company, and a deposit insurance scheme, will also strengthen the repertoire of measures aimed at safeguarding financial stability. In parallel, the supervisory approach at the Bank is in the process of being overhauled with onset of effective consolidated supervision, conglomerate supervision, and risk-based supervision, with the benefit of technical assistance from international institutions. In September 2016, several amendments were brought to the Banking Act 2004 and to the Bank of Mauritius Act 2004 to empower the Bank to request information from any financial entity for financial stability purposes. Various guidelines issued by the Bank to the banking community are being beefed up and updated. Others, including one on liquidity risk factoring in Basel framework for Liquid Coverage Ratio (LCR), are in the state of preparation and will be implemented after consultations with banks. Finally, the Bank has also been steadfast in monitoring progress among banks in implementing IFRS9 expected credit loss framework within the agreed timeline.

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List of Charts

Acronyms

BAI	British American Insurance
BCS	Bulk Clearing System
BML	Broad Money Liabilities
BoE	Bank of England
CAR	Capital Adequacy Ratio
CCAR	Comprehensive Capital Analysis and Review
CPI	Consumer Price Index
CPMI	Committee on Payment and Market Infrastructures
CRR	Cash Reserve Ratio
DCs	Depository Corporations
DFAST	Dodd-Frank Act
DR	Disaster Recovery
D-SIBs	Domestic Systematically Important Banks
ECB	European Central Bank
EFTs	Electronic Fund Transfers
EMDEs	Emerging Market and Developing Economies
FAO	Food and Agriculture Organisation
FDI	Foreign Direct Investment
FMI	Financial Market Infrastructures
FOMC	Federal Open Market Committee
FSAP	Financial Sector Assessment Programme
FSC	Financial Services Commission
FSR	Financial Stability Report
GBC	Global Business Companies
GDP	Gross Domestic Product
GFC	Global Finance Crisis
GFCF	Gross Fixed Capital Formation
GMM	Generalized Methods of Moments
GOI	Grains and Oilseed Index
ICOR	Incremental Capital Output Ratio
IGC	International Grains Council
IMF	International Monetary Fund
IPI	Import Price Index
HHI	Herfindahl-Hirschman Index
KRR	Key Repo Rate

Acronyms

MACSS	Mauritius Automated Clearing and Settlement System
MERI	Mauritius Exchange Rate Index
MPC	Monetary Policy Committee
MSCI	Morgan Stanley Capital International
NBDTIs	Non-Bank Deposit-Taking Institutions
NFA	Net Foreign Assets
NML	Narrow Money Liabilities
NPLs	Non-Performing Loans
NPF	National Pension Fund
ODCs	Other Depository Corporations
OPEC	Organisation of the Petroleum Exporting Countries
PLACH	Port Louis Automated Clearing House
PMI	Purchasing Managers' Index
PPI-A	Producer Price Index - Agriculture
PPI-M	Producer Price Index - Manufacturing
ROA	Return On Assets
ROE	Return On Equity
SCBG	Super Cash Back Gold
US FED	US Federal Reserve System
WEO	World Economic Outlook

Glossary

Basis point is a unit equal to one hundredth of a percentage point.

CORE1 inflation excludes food, beverages and tobacco and mortgage interest on housing loan from the CPI basket. Both headline and year-on-year 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 year-on-year CORE2 inflation measures are available.

Credit-to-GDP gap is the percentage deviation between the credit to GDP ratio and an estimate of its trend.

Economic Policy Uncertainty Index is a measure of policy-related economic uncertainty. It is based on media coverage and divergences in economic forecasts derived from different sources.

GBC1s are resident corporations which conduct business outside Mauritius. The law has recently been amended to allow them to transact with residents provided that their activities in Mauritius are ancillary to their core business with non-residents.

H1 refers to first semester.

H2 refers to second semester.

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

Herfindahl-Hirschman Index is a measure of the average size of firms in relation to the industry and an indicator of the amount of competition among them. It is a commonly accepted measure of market concentration.

ICOR is measured as the ratio of GFCF to GDP divided by the growth rate of GDP.

Key Repo Rate is the key policy rate used by the Bank of Mauritius to signal changes in its monetary policy stance.

Leverage ratio is used to calculate the financial leverage of a company to get an idea of the company's methods of financing or to measure its ability to meet financial obligations. It is meant to evaluate the company's debt levels.

Lorenz Curve is typically used to depict distributive inequalities. Curves that stretch further away from the line of perfect equality show higher inequality.

MERI1 is the Mauritius Exchange Rate Index, a nominal effective exchange rate introduced in July 2008, based on the currency distribution of merchandise trade.

MERI2 is the Mauritius Exchange Rate Index, a nominal effective exchange rate introduced in July 2008, based on the currency distribution of merchandise trade and tourist earnings.

ROA is the annualised pre-tax return on assets and is measured by the ratio of pre-tax profit to average assets.

ROE is the annualised pre-tax return on equity and is measured by the ratio of pre-tax profit to average equity.

SEM-10 is an index launched by the Stock Exchange of Mauritius on 02 October 2014. It is designed to meet international standards and provide a larger and more attractive investible benchmark for both domestic and foreign market participants and comprises the ten largest eligible shares of the Official Market, measured in terms of average market capitalization, liquidity and investibility criteria.

SEMDEX is an index of prices of all listed shares on the Stock Exchange of Mauritius wherein each stock is weighted according to its share in the total market capitalisation.

Tier 1 capital is a term used to qualify eligible capital of a bank and is constituted of the components having the highest loss absorbing capacity.

VIX is a volatility index, showing markets' expectations of short term volatility. It is constructed based on the prices on the S&P 500 index options.

Y-o-y change compares the value of a variable at one period in time compared with the same period the previous year.

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