



## BANK OF MAURITIUS

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### Minutes of the 41<sup>st</sup> Monetary Policy Committee Meeting held on 10 November 2016

The 41<sup>st</sup> meeting of the Monetary Policy Committee (MPC) was held on Thursday 10 November 2016 at 10:30 hours at the Bank of Mauritius and was chaired by Mr Rameswurlall Basant Roi GCSK, Governor.

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

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

The Bank's staff reported on economic and financial developments which took place since the 40<sup>th</sup> MPC meeting held on 20 July 2016.

#### *Global economic and financial developments*

1. **The MPC noted that global economic conditions remained subdued.** Growth in developed and emerging market and developing economies (EMDEs) continued but at a pace that has fallen short of expectations. Global growth would remain modest over the near-term. The IMF's October 2016 World Economic Outlook (WEO) report forecasts world output at 3.1 per cent in 2016, down from 3.2 per cent in 2015, but higher at 3.4 per cent in 2017, due to better performance of the US and EMDEs.
2. **Inflationary pressures in major advanced economies remain muted, but were diverse in EMDEs.** Inflation in advanced economies is forecast to increase from 0.3 per cent in 2015 to 0.8 per cent in 2016 and further to 1.7 per cent in 2017, mirroring a rise in energy prices and lowering of the output gap. Inflation in EMDEs is expected to edge down from 4.7 per cent in 2015 to 4.5 per cent in 2016 and further to 4.4 per cent in 2017, partly due to the diminishing impact of previous weakening of their currencies.
3. **Commodity prices firmed up somewhat but equities' performances have been rather mixed since July 2016,** reflecting uncertainties regarding the US Fed's normalisation of its interest rate despite supportive economic data and amidst geopolitical issues. The MSCI World shed 1.0 per cent while the MSCI Emerging Markets gained 3.9 per cent between 20 July and 31 October 2016.
4. **Currency markets were broadly influenced by issues related to the impact of Brexit and monetary policy stances of major advanced economies.** The US dollar fluctuated broadly in line

with news regarding the imminence of the next US interest rate hike but the Pound sterling was hit by political worries in Britain and further accommodative monetary policy by the Bank of England. The euro weakened, weighed down by headwinds post UK's vote to leave the European Union, the broad-based strength of the US dollar, weaker economic data and comments from the European Central Bank on the downside risks to Eurozone's growth. Currencies of major commodity-exporter countries, namely Brazil, Russia, and South Africa, generally appreciated, reflecting a pick-up in commodity prices, amongst others.

### **Domestic economic developments**

5. **Statistics Mauritius projects real GDP to grow by 3.7 per cent in 2016, up from 3.0 per cent in 2015.** Final consumption expenditure growth is expected to rise to 2.9 per cent in 2016, driven by a sharp increase in general Government expenditure growth from 1.8 per cent in 2015 to 3.0 per cent in 2016. Household consumption expenditure is projected to remain unchanged at 2.9 per cent. Investment is expected to post a solid growth of 5.9 per cent in 2016, as a result of a rebound by 6.1 per cent in private sector investment and a marked rise of 5.3 per cent in public investment. Exports and imports of goods and services are expected to increase by 3.7 and 2.2 per cent, respectively. Key services sectors, such as financial services, information and communication, accommodation and food service activities and professional services, are projected to register growth of close to or above 6 per cent. The economy would continue to operate below its potential at the current growth trajectory.
6. **Domestic inflation so far remains muted, in line with subdued global commodity prices and persistent slack in the domestic economy.** Headline inflation dropped to 0.8 per cent in October 2016. The majority of the other inflation measures showed broad stability and subdued price pressures. Inflation expectations, assessed from the August 2016 Bank's survey, remained skewed to the downside and contained. The ebbing of domestic input cost pressures was noticeable from the drop in producer price inflation (Manufacturing).
7. **Labour market conditions improved somewhat during 2016Q2, with a reduction in the unemployment rate associated to some extent by a contraction of the labour force.** The unemployment rate is estimated to have declined from 7.8 per cent in 2015Q2 to 7.4 per cent in 2016Q2. It is projected to fall to 7.5 per cent in 2016, from 7.9 per cent in 2015.
8. **Preliminary estimates of Mauritius' balance of payments point to a current account deficit of about 4.4 per cent of GDP for 2016Q2 compared to 5.2 per cent of GDP for 2015Q2.** A higher surplus in the services account, in absolute terms, would to some extent offset the increase in the trade deficit mainly caused by lower exports. The country recorded a higher balance of payments surplus of Rs8.3 billion in 2016Q2 compared to Rs2.6 billion in 2015Q2. For 2016, the current account deficit is estimated at 4.4 per cent of GDP for 2016, down from 4.8 per cent in 2015. The balance of payments surplus is estimated at Rs20.1 billion for 2016.
9. **Broadly reflecting the movements of major currencies on international markets and the domestic demand and supply conditions, the rupee appreciated against the euro and the Pound sterling but depreciated against the US dollar,** point-to-point, between 20 July and 31

October 2016. On a trade-weighted basis, the real effective exchange rate of the rupee depreciated marginally by 0.1 per cent y-o-y in September 2016, but posted an appreciation of 0.5 per cent in September 2016 compared to July 2016.

10. **The level of excess liquidity was effectively contained as a result of active open market operations conducted by the Bank.** From the last MPC meeting held on 20 July to 21 October 2016, the overall average excess liquidity in the banking system has remained almost unchanged at about Rs7.9 billion. As at close of business on 24 October 2016, the total outstanding amount of instruments issued for liquidity management stood at Rs58.2 billion, inclusive of deposits placed by banks on account of sterilized foreign exchange intervention. The movements of yields on Government securities broadly reflected the 40 basis points cut in the Key Repo Rate at the July 2016 MPC meeting. The weighted yields for the 91-Day, 182-Day and 364-Day Government of Mauritius Treasury Bills declined to 2.48 per cent, 2.65 per cent and 2.80 per cent as at 28 October 2016. A similar decline was noted for medium- and long-term securities.
12. **The pace of expansion of broad money supply remained solid as at end-September 2016 while private sector credit growth stayed subdued.** The growth in broad money continued to be supported by its most liquid components. The annual growth rate of broad money declined from 9.2 per cent in May 2016 to 8.9 per cent in September 2016, and was supported by the increase in the net foreign assets. The annual growth rate of banks' credit to the private sector (excluding credit to GBC entities) fell from 2.7 per cent in May 2016 to 2.1 per cent in September 2016, explained by a decline in the annual growth rates of both household and corporate credit.
13. **The domestic banking sector remained adequately capitalised as at end-June 2016.** The capital adequacy ratio for the banking industry dropped from 18.1 per cent as at end-March 2016 to 17.5 per cent as at end-June 2016. The ratio of NPL to total loans remained unchanged at 7.1 per cent as at end-June 2016.

#### *Staff economic outlook*

14. **Bank staff have estimated that, based on the current domestic and global economic conditions, headline inflation is expected to remain low in the near term but is likely to rise gradually over the forecast horizon.** Headline inflation is projected at around 1 per cent in 2016 and to rise gradually to a range of 2 to 3 per cent in 2017. Inflationary pressures would be generated mainly from a gradual hike in commodity prices and a narrowing of the output gap over the projection period.
15. **Bank staff forecast that economic growth will continue to be below potential.** Overall, growth performance for 2016 would still be better than for 2015. Bank staff is now projecting a real GDP growth rate of 3.5 per cent for 2016, given the prevailing economic uncertainties clouding visibility and also due to worries over the performance of the manufacturing sector and in particular, the textile sector. Staff, however, project economic growth for 2017 ranging between 3.8 per cent and 4.0 per cent on the strength of major infrastructure projects to be implemented in the course of 2017 in line with the Budget Speech 2016-17.

## Monetary Policy Decision

16. **The Chairman noted that overall monetary conditions have remained stable since the July 2016 MPC meeting.** Performance in the tourism sector remains commendable while the current account deficit has narrowed. Inflation has persisted at low levels. In terms of demand by expenditure, he noted that investment is not firming up while consumption is stagnating. Domestic savings have also remained at the same level. This has implications for growth, going forward. The Chairman underlined that prevailing economic and financial conditions continue to support stability in the financial system, but evolving circumstances in an uncertain and volatile global environment require close monitoring with a view to timely addressing any emerging risk to financial stability.
17. **Members debated on the role of the interest rate with respect to declining investment and sub-par growth.** Some members viewed that monetary policy seemed to have reached its limits and any further cut in the interest rate would most likely fuel unproductive investment. Members argued for the need of a clear strategy amid prevailing uncertainty and weak external demand.
18. **The MPC reiterated the key importance of financial stability in the context of the current level of non-performing loans and low domestic savings in the economy.** The Chairperson pointed that a strong regulatory and supervisory framework is critical for the development of the financial sector and the economy as a whole. Members took note of the fiscal measures being considered to assist UK exporters which have been hurt by the significant depreciation of the Pound sterling vis-à-vis the US dollar on global currency markets. Members also viewed that domestic growth would pick up next year as major infrastructural projects reach implementation stage.
19. **On the external front, global economic uncertainty very much persists and clouds visibility.** The impact of Brexit and geo-political risks continued to weigh heavily on the global economic and financial environment. Diverging monetary policy trends as the US Federal Reserve System's (US Fed) commits to the normalisation of its monetary policy while other central banks would retain their accommodative stance would also contribute to a blurred outlook.
20. **Members took note of measures taken by the Bank to sterilise excess liquidity in the banking system.** Average excess liquidity levels have declined and yields on money market instruments have somewhat stabilised. Ms M Heerah-Pampusa, Assistant Director, Financial Markets and Reserve Management Division, made a presentation to the MPC on the proposed new operational framework of monetary policy. The new framework would be implemented in early 2017, after excess liquidity would have been further reduced. The dilemma in domestic policy-making with a trade-off between excess liquidity and an appreciation of the rupee was highlighted. Members noted that a prolonged misalignment of the domestic currency with regard to economic fundamentals was not in line with the objective of an orderly and balanced economic development.
21. **The MPC weighed the risks to the growth and inflation outlook and considered that monetary conditions were appropriate at this juncture.** Economic uncertainties as well as limits of monetary policy were considered.

## Voting Pattern

22. **At the conclusion of the discussions, the Committee unanimously voted to keep the Key Repo Rate unchanged at 4.00 per cent per annum.**
23. **The MPC would continue to monitor economic and financial developments.** The MPC would also stand ready to meet in between its regular meetings, if the need would arise.
24. **The next MPC meeting is scheduled on Wednesday 22 February 2017.**

### Editor's Note

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

When the MPC met on 10 November 2016, the last available data on national accounts, employment and external trade were for 16Q2. The last data available on CPI and inflation were for October 2016.

### Abbreviations and Definitions

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

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

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