BANK OF MAURITIUS

Released on 8 March 2019

Minutes of the 50th Monetary Policy Committee Meeting held on 22 February 2019

The 50th meeting of the Monetary Policy Committee (MPC) was held on Friday 22 February 2019 at 10:00 hours at the Bank of Mauritius and was chaired by Mr. Yandraduth Googoolye, Governor.

Members present: Dr Renganaden Padayachy (First Deputy Governor); Mr. Mahendra Vikramdass Punchoo (Second Deputy Governor); Dr Streevarsen Narrainen; Mr. Lim Chan Kwong Lam Thuon Mine; Ms. Marie Rosy Priscilla Pattoo; Mr. Mohammad Mushtaq Namdarkhan; and Professor Sanjeev Kumar Sobhee (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 49th MPC meeting held on 9 November 2018. The MPC also assessed staff's macroeconomic projections and evaluated risks to the domestic economic outlook.

Global economic and financial developments

1. **After two years of solid economic growth globally, a synchronised slowdown is emerging, thereby throwing substantial uncertainty about the strength of the international economy.** The US economy appears to have lost impetus, growth has been falling in the Eurozone, China is struggling to sustain economic momentum and lingering Brexit-related uncertainty continues to take a toll on the British economy. The IMF has, in its January 2019 World Economic Outlook (WEO) Update, maintained the 2018 global growth rate at 3.7 per cent, same as projected in October 2018. In contrast, most multilateral organisations including the IMF, World Bank, UN and OECD have lowered their global growth projections for 2019 and 2020.

2. **Purchasing Managers' Indices (PMIs), which are broad indicators of world economic activity, have been losing momentum lately.** J.P. Morgan's Global All-Industry Output Index dropped to a two-and-a-half-year low of 52.1 in January 2019, as growth of new orders eased and international trade contracted. Global manufacturing sector activity growth slowed closer to stagnation at 50.7 in January 2019 compared to 51.4 in December 2018, reflecting mainly stalling new orders. Growth in the global services sector also eased to a 28 months' low of 52.6 in January 2019.

3. **Global inflationary pressures were broadly contained in 2018, thanks to lower commodity prices, especially energy prices, and faltering global economic momentum.** As per the January 2019 IMF WEO Update, inflation in advanced economies is projected to be lower at 1.7 per cent in 2019, from 2.0 per cent in 2018. This contrasts with an uptick projected for emerging market economies, from 4.9 per cent in 2018 to 5.1 per cent in 2019.

4. **Crude oil prices broadly remained on a downtrend since the last MPC meeting, amidst prospects of weak demand and excess supply concerns.** After peaking at about US$86 a barrel in October 2018, Brent crude oil went through a marked correction, falling by about 40 per cent towards the end of 2018. In 2019, the oil price is expected to continue decreasing as the US ramps up production against a backdrop of reduced OPEC production and lower demand. The ICE Brent is expected to average US$61/barrel in 2019, lower than the average of US$71/barrel in 2018.

5. **Reflecting weaker world trade volume growth and ample supply, international commodity prices have also remained somewhat contained.** The FAO Food Price Index, which systematically declined from 176 points in May 2018 to 162 points in November 2018, rose to 165 points in January 2019, and was still 4 points below January 2018 readings. The International Grains Council's Grains and Oilseed Index dropped to 194.5 in January 2019, reflecting lower prices of soyabeans and barley, which superseded higher prices of maize and rice. The January 2019 World Bank Global Economic Prospects Report has painted a rather stable price outlook for agricultural prices over the medium term.

6. **The US Fed again hiked its policy interest rate at its December 2018 FOMC meeting, while other major advanced economies' central banks adopted a more cautious approach and kept their policy rate unchanged.** While it was stated in December 2018 that any further increase in interest rates would be undertaken gradually, the tone has changed in January 2019, with the Fed adopting a wait-and-see approach. The European Central Bank ended its asset purchase programme in December 2018 and acknowledged that risks to the Eurozone economy have shifted to the downside. The Bank of England maintained the Bank Rate unchanged amid favourable economic developments but agreement over a Brexit deal might influence a future hike in interest rate.

Domestic economic developments

7. **The domestic growth momentum eased to 3.3 per cent in 2018Q3, down from 3.6 per cent in 2018Q2, mainly attributed to the decline in sugar output, which negatively impacted on activity in both manufacturing and agricultural sectors.** Domestic demand continued to sustain growth, supported by consumption expenditure and sharp growth in investment, at the expense of ongoing net external demand. On the supply side, economic expansion was led by services sectors and buoyant construction activity. In its latest forecast, Statistics Mauritius estimated real GDP growth to be 3.8 per cent for 2018 and 4.0 per cent for 2019.

8. **Domestic inflation, as measured by the change in the CPI, declined further in January 2019.** Headline inflation dropped to 2.8 per cent in January 2019, from 4.0 per cent in January 2018 and the peak of 5.0 per cent recorded in March/April 2018. Year-on-year inflation declined from 6.2 per cent in January 2018 to 0.5 per cent in January 2019, the lowest recorded since May 2016. The Bank's core

inflation measures remained under check and were indicative of subtle inflationary pressures. The majority of other derived inflation indicators also pointed to inherent stability and contained pressures.

9. **The unemployment rate improved in 2018Q3 amidst a fall in the labour force, accompanied with a decline in employment.** Employment dropped by 5,600 and was complemented by a contraction in the labour force of 6,400 compared to 2017Q3, which brought down the number of unemployed by 800. The unemployment rate, thus, declined from 7.0 per cent in 2017Q3 to 6.9 per cent in 2018Q3.

10. **The wage rate index rose by 4.1 per cent in 2018Q3 compared to 2017Q3, largely driven by an increase in private sector wages, which contributed to higher household disposable income.** Sectors such as transport, professional services, administrative services and other services recorded an increase in wages of around 5 per cent while wholesale and retail trade, information and communication and financial services sectors recorded higher wages of 6 to 7 per cent. The divergence between labour productivity growth and wage compensation remains a drag for the economy's competitiveness.

11. **Preliminary estimates of balance of payments have pointed to a worsening of the current account deficit to 8.3 per cent of GDP in 2018Q3, due primarily to a higher deficit on the goods account, although mitigated by surpluses on both the services and primary income accounts.** The widening deficit on the goods account is projected to increase the current account deficit from 5.9 per cent in 2018 to 6.1 per cent in 2019 (excluding the purchase of aircraft), which however would be fully funded from higher net inflows on the capital and financial account. Imports on account of infrastructure-linked investments would partly drive the deficit, while the performance of exports of goods would remain cause for concern.

12. **The Bank actively conducted open market operations through the issue of its own securities in order to maintain money market rates around the policy rate.** Since the last MPC meeting of 9 November 2018 up to end-January 2019, the rupee liquidity in excess of cash ratio requirements increased to an average of Rs12 billion, as compared to an average of Rs11 billion for period 21 August to 9 November 2018. It is estimated that banks kept a higher amount of liquidity as precautionary balances in December 2018 to meet demand from the public during the festive period. The Bank also proceeded with sterilised foreign exchange interventions.

13. **The rupee exchange rate has been fairly stable, benefitting from capital inflows and backed by macroeconomic stability.** Between 9 November 2018 and 13 February 2019, on a weighted average dealt selling rate basis, the rupee appreciated by 0.7 per cent, 1.1 per cent and 2.5 per cent against the euro, the US dollar and the Pound sterling, respectively. On a nominal effective exchange rate basis, as measured by MERI1, the rupee appreciated marginally by 0.2 per cent and 0.6 per cent in November and December 2018, respectively, but depreciated by 0.1 per cent in January 2019 on a month-on-month basis. On a real effective exchange rate basis, the rupee appreciated mildly by 0.8 per cent in December 2018.

14. **Broad money supply has kept pace since the last MPC meeting, indicating adequate supply of liquidity in the economy.** The annual growth rate of Broad Money Liabilities (BML) rose to 6.3 per cent in December 2018, from 4.4 per cent in September 2018. Growth of bank loans to Other

Nonfinancial Corporations, households and other sectors (excluding GBCs) dropped from 5.6 per cent in October 2018 to 4.2 per cent in December 2018, mostly reflecting a ‘carve-out’ operation, whereby selected portfolios of non-performing loans have been transferred away from loan books.

15. **The banking sector stability continues to be maintained, as banks remain broadly sound and well-capitalised.** The aggregate capital adequacy ratio improved to 17.9 per cent as at end-December 2018, up from 17.4 per cent as at end-September 2018. The level of impaired credit dropped to Rs35 billion as at end-December 2018 compared to Rs42 billion as at end-September 2018, thereby improving asset quality of the overall bank credit portfolio. The ratio of non-performing loans to total loans decreased from 5.9 per cent to 4.9 per cent. Concurrently, specific provisions set aside by banks against non-performing loans have improved as the coverage ratio stood at 60.8 per cent as at end-December 2018, up from 57.8 per cent as at end-September 2018.

Staff economic outlook

16. **In the absence of major supply shocks, headline inflation is forecast at around 2.1 per cent in 2019, down from the previous estimate of 3.0 per cent.** The downward revision emanates principally from favourable base effects as well as relatively contained cost pressures. The current benign inflationary environment would persist in the near term. Demand-driven inflationary pressures in the economy are also projected to remain contained, with the economy still operating with some degree of spare capacity. On the external front, inflation in our major trading partners remains low and imported inflation is expected to be low in the near-term. Global commodity prices are also expected to remain mild over the medium term, while lower global oil prices would contribute to a downward bias in inflationary pressures on the domestic front.

17. **GDP growth is forecast to remain resilient at about 3.9 per cent in 2019.** The slight downgrade from 4.0 per cent would result from the current global economic uncertainty and the fact that some of our major trading partners have revised down their growth outlook, which could dent demand from these economies. At home, the sectoral issues that could weigh on growth performance include difficulties faced by some textile companies, and lower sugar production and tourism growth.

Monetary Policy Decision

18. **Members agreed that the external situation warranted careful monitoring given that global growth and trade momentum were losing traction.** They commented on a number of risks associated with the outlook for economic activity over the short- to medium-term and noted that risks to the downside have been growing. The possibility of a higher-than-expected slowdown in global economic growth, particularly in China and Europe, and policy uncertainties associated with Brexit, an escalation in international trade policy tensions, and other geo-political pressures would weigh on the economic performance of the country through the trade channel given that Mauritius is an export-oriented economy.

19. **With regards to the inflation outlook in Mauritius, Members viewed that inflationary pressures were broadly contained.** They remarked that factors, such as the decline in global oil prices, slower global growth and softer inflation abroad have contributed to dampen domestic inflationary

pressures and may continue to do so in the near term. Headline inflation was projected to remain low amidst contained demand pressures and inflationary expectations.

20. **Since the November 2018 MPC meeting, domestic macroeconomic developments had mostly remained on track, except for some sectoral fragilities**. In their discussions on the domestic economic situation and outlook, the Committee noted that the Mauritian economy was somewhat resilient, expanding at a reasonable pace, albeit below its potential. The outlook for business investment and public sector infrastructure spending was positive. Growth in household consumption was expected to remain supported, amidst an improved household disposable income. The unemployment rate remained on a downtrend. Members discussed lengthily on the performance of various sectors of the economy, including the sugar, manufacturing and tourism sectors. They reiterated their concerns over the performance of domestic exports, which is adversely impacting on the current account balance.

21. **At the current juncture, Members preferred to remain prudent over the stance of monetary policy given the high degree of global economic uncertainty**. They noted that short-term interest rates continued to be around the Key Repo Rate following the implementation of appropriate monetary policy operations.

Voting Pattern

22. **Based on their current assessments, the Committee unanimously voted to maintain the Key Repo Rate at 3.50 per cent per annum.** The MPC weighed the risks to the growth and inflation outlook and concluded that the current monetary policy stance was broadly appropriate. The MPC remarked that it would be preferable to maintain stability in the monetary policy stance, which is continuing to support the domestic economy whilst maintaining price stability.

23. **The Committee will continue to exercise vigilance should there be a resurgence of inflationary pressures in the economy.** It also stands ready to meet in between its regular meetings, if the need arises.

24. **The next MPC meeting is scheduled on 17 May 2019.**

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 22 February 2019, the last available data on national accounts, employment and external trade were for 2018Q3. The last data available on Consumer Price Index (CPI) and inflation were for January 2019.

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

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

CORE1 inflation excludes food, beverages and tobacco and mortgage interest on housing loan from the CPI basket.

CORE2 inflation excludes food, beverages and tobacco, mortgage interest, energy prices and administered prices from the CPI basket.

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

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

GMTBs refer to Government of Mauritius Treasury Bills.