BANK OF MAURITIUS

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Minutes of the 51st Monetary Policy Committee Meeting held on 17 May 2019

The 51st meeting of the Monetary Policy Committee (MPC) was held on Friday 17 May 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 50th MPC meeting held on 22 February 2019. The MPC also assessed staff's macroeconomic projections and evaluated risks to the domestic economic outlook.

Global economic and financial developments

1. **Staff commented on latest data releases pertaining to the performance of our major trading partners, including global growth revisions and noted that the global economic environment was still fraught with uncertainty.** For instance, the IMF revised down global growth projections for 2019 for the third time in its April 2019 World Economic Outlook (WEO) on the back of an anticipated weak economic performance in the first half of 2019, amidst persistent headwinds across countries, including the US, China, Germany, Italy, France and UK. The IMF has estimated that around 70 per cent of economies across the world would experience a growth slowdown in 2019. Nevertheless, the IMF predicted a gradual recovery in the second semester of 2019. The IMF is expecting the global economy to grow at 3.3 per cent in 2019, before recovering to 3.6 per cent in 2020, down by 0.4 percentage point and 0.1 percentage point, respectively, compared to forecasts made in October 2018.

2. **As regards to leading output indicators, the latest readings of Purchasing Managers' Indices (PMI) have been hinting towards a possible slowdown in global economic growth performance.** J.P.Morgan's Global Composite PMI was down to 52.1 in April 2019, from 52.8 in March 2019. The lower PMI was attributed to a decline in both sub-indices, although the fall in manufacturing was more pronounced compared to services. The manufacturing PMI dropped in US, UK and India while the services PMI was down in US, UK and China. Lower international trade weighed on global economic activity, with export orders continuing to fall, especially in Germany and China.

3. **Global inflation is expected to remain subdued in the near term.** It gradually increased from 3.2 per cent in 2017 to 3.6 per cent in 2018 on the back of higher energy prices, but is projected to remain unchanged at 3.6 per cent in 2019, mainly reflecting the subdued outlook for economic growth and commodity prices. Core inflation has remained mild amidst broadly contained inflation expectations in major advanced economies. According to the April 2019 IMF WEO, inflation in advanced economies is expected to drop from 2.0 per cent in 2018 to 1.6 per cent in 2019, amid weak supply side pressures. After an anticipated modest rise to 4.9 per cent this year, from 4.8 per cent in 2018, inflation in emerging economies is forecast to decelerate steadily to settle at around 4 per cent in the medium-term.

4. **Crude oil prices had reversed course since the last MPC meeting due to supply concerns and the decision by the US to end waivers on the import of Iranian oil.** Brent crude oil increased from US$57.7 per barrel in December 2018 to US$60.2 per barrel in January 2019 and further to US$71.6 per barrel in April 2019. Since the beginning of 2019 and until 10 May 2019, Brent crude oil has risen by about 29 per cent. NYMEX WTI mimicked Brent's trend, rising from US$49.0 per barrel in December 2018 to US$51.6 per barrel in January 2019 and further to US$63.9 per barrel in April 2019. The rebound in oil prices has been attributed to the OPEC's oil supply disruption, the US sanctions on Iran's and Venezuela's crude oil exports and also from the US decision to end sanction exemptions for Iranian oil exports.

5. **Amid unfavourable supply conditions and decline in world trade volume, the international agricultural food commodity prices remained broadly contained.** After dropping to 161.5 points in February 2019, from 163.9 points in January 2019, the FAO Food Price index rose to 170.1 points in April, reflecting significant increases in prices of dairy products and meat. The International Grains Council's Grains and Oilseed Index fell from 194 points in February 2019 to 183 points in April, paralleling a fall in the prices of barley, wheat, maize and soyabeans. According to the April 2019 World Bank Commodity Markets Outlook, food commodity prices are expected to decline by 2.6 per cent in 2019 but would recover in 2020 on the back of lower crop production and higher costs for energy and fertilisers.

6. **Congruent to the US Fed's decision to keep its interest rates unchanged at least till the end of this year, other major central banks have been treading on cautious stances.** In December 2018, the US Fed forecast two interest rate hikes for 2019 but has now changed its outlook for no increase in 2019, motivated by weak economic data amid slowdown in household expenditure and business investment. The European Central Bank left its main refinancing rate at zero per cent and announced that the rate would remain unchanged as long as necessary until the inflation rate converged to the Bank's objective of 2 per cent. Notwithstanding the decision of Bank of England to keep its policy rate unchanged, the future movement of interest rates in the UK would largely be influenced by the outcome and nature of Brexit.

Domestic economic developments

7. **Growth in the domestic economy picked up in 2018Q4, attributed to a surge in investment and strong exports performance on the demand side.** On the production side, the momentum in the services sector persisted. Higher activity in the construction sector, mostly due to the public sector's investment push, supported the growth performance. Real GDP expanded by 4.1 per cent in 2018Q4 compared to 3.3 per cent in 2018Q3. For 2019, Statistics Mauritius is forecasting GDP at market prices

to grow by 3.9 per cent, slightly down by 0.1 percentage point, from 4.0 per cent projected in December 2018. The downward revision reflected mainly lower growth in the manufacturing and financial & insurance activities sectors. The construction sector, together with the financial & insurance activities and wholesale & retail trade sectors, are expected to account for almost 40 per cent of growth in 2019.

8. **Domestic inflation, as measured by the change in the CPI, remained low both on 12-month average and year-on-year basis on the back of moderate global economic activity and inflation as well as the persistence of slack in the domestic economy.** Headline inflation stood at 1.2 per cent in April 2019, down from 2.8 per cent in January 2019 and 5.0 per cent in April 2018. After being in negative territory in February and March 2019, year-on-year inflation rose to 0.6 per cent in April 2019, mainly due to base effects arising from the much sharper drop in prices of vegetables a year earlier. Core inflation measures remained broadly contained below 3 per cent and the majority of the other inflation indicators also depicted stability and subdued price pressures.

9. **The unemployment rate continued its downtrend and reached a ten-year low of 6.4 per cent in 2018Q4, from 6.7 per cent in 2017Q4.** Employment rose by 5,200 in 2018Q4 compared to a year earlier while the labour force was up by 3,700, thereby reducing the number of unemployed by 1,500. Higher employment in wholesale and retail trade, construction and human health sectors were partly offset by job losses in other service activities, transport and manufacturing sectors.

10. **In 2018, wages across the economy rose by 4.4 per cent compared to 2017.** On a sectoral basis, the most noticeable increases were recorded in the manufacturing and electricity sectors, with growth of 10.9 per cent and 8.7 per cent, respectively. Other sectors with sharp wage increases of 6-8 per cent included transportation & storage, administrative services, wholesale & retail trade, arts, entertainment & recreation and other service activities. Higher wages in 2018 were driven by a marked increase in private sector wages. In the medium-term, wage developments in excess of productivity growth could constitute an upside risk to the economy's competitiveness.

11. **Preliminary estimates of Mauritius' balance of payments have pointed to a worsening of the current account deficit to 6.3 per cent of GDP in 2018Q4,** that stemmed mainly from the widening goods account deficit coupled with a lower surplus on the primary income account, but which were partly dampened by surpluses on both the services and the secondary income accounts. A wider deficit on the goods account associated with higher imports geared to major infrastructure projects would raise the current account deficit from 5.8 per cent of GDP in 2018 to 5.9 per cent of GDP in 2019. This would, however, be fully funded from higher net inflows on the capital and financial account.

12. **The Bank maintained its efforts to keep excess liquidity in the banking system at a reasonable level by issuing its own instruments in excess of those maturing.** Since the last MPC meeting held in February 2019 and up to end-April 2019, rupee liquidity maintained by banks above the minimum cash ratio requirement declined to an average of Rs11.5 billion. In a bid to keep excess liquidity under control, additional special deposits for an amount of Rs3.0 billion were issued for a period of up to two years. The Bank continued to intervene on the domestic foreign exchange market.

13. **The exchange rate of the rupee moved broadly in consonance with international trends and domestic market conditions but was accompanied by relatively less volatility amid macroeconomic stability and interventions by the Bank.** Between 22 February 2019 and 30 April 2019, on a weighted average dealt selling rate basis, the rupee depreciated by 2.2 per cent, 1.0 per cent and 1.8 per cent against the US dollar, euro and the Pound sterling, respectively. On a nominal effective exchange rate basis, as gauged by MERI1, the rupee depreciated by 0.6 per cent in April 2019 on a month-on-month (m-o-m) basis, from depreciation of 0.9 per cent in March 2019. On a real effective exchange rate basis, the rupee appreciated by 1.6 per cent and 0.4 per cent m-o-m, respectively, in February and March 2019.

14. **Broad money supply rose at a slightly higher pace since the last MPC meeting.** Broad Money Liabilities grew by 6.4 per cent in March 2019, an uptick from 6.3 per cent in December 2018. Bank loans to Other Nonfinancial Corporations ('ONFCs'), households and other sectors (excluding GBCs) increased further to Rs299.1 billion as at end-March 2019, from Rs297.9 billion as at end-December 2018. The expansion in bank loans was principally backed by an increase in household borrowings, which more than offset the decrease in loans to ONFCs and other sectors.

15. **Banks remain broadly sound and well-capitalised.** The aggregate capital adequacy ratio improved further to 18.5 per cent as at end-March 2019, from 18.1 per cent as at end-December 2018. A deterioration was noted in the asset quality of banks' credit portfolio, with the ratio of non-performing loans to total loans rising from 4.9 per cent as at end-December 2018 to 5.6 per cent as at end-March 2019. Concomitantly, specific provisions set aside by banks against non-performing loans have declined and the coverage ratio stood at 54.1 per cent as at end-March 2019, down from 60.8 per cent as at end-December 2018.

Staff economic outlook

16. **Headline inflation is forecast to remain at low levels in the coming months.** Cost push pressures appear to be well contained due to subdued global and trading partner inflation, muted global commodity prices and a stable rupee exchange rate. Demand-driven inflationary pressures in the domestic economy are also expected to remain in check, with the economy still operating with some degree of spare capacity. Under the central projection, the absence of major food price shocks in 2019Q1 has resulted in a downward revision of the previously announced inflation forecast of 2.1 per cent for calendar year 2019 to below 1.5 per cent and to about 2 per cent in 2020.

17. **The domestic economy is projected to maintain its growth momentum in 2019, expanding at a similar pace to 2018. Real GDP growth at market prices is forecast at about 3.9 per cent in 2019 and 4 per cent in 2020, notwithstanding higher uncertainty due to increasing downside risks.** GDP growth may turn out to be lower given the current global uncertainty and the fact that some of our major trading partners have revised down their growth outlook, which can potentially dent demand from these economies. On the domestic front, the sectoral issues that could weigh on growth performance include the challenges faced by the textile sector, lower sugar production and tourist arrivals. The growth forecast remains dependent on the timely implementation of major public investment projects.

Monetary Policy Decision

18. **Members agreed that the external situation warranted careful monitoring given the recent global growth downgrades and as trade tensions appeared to intensify.** The Committee noted that monetary policy in the major advanced and emerging market countries had remained accommodative in the current global economic environment. Members remained careful in their assessment of global economic and financial conditions, as the world economy was being subject to a host of idiosyncratic shocks. They considered that the global economy could have entered in a new economic cycle and that the risks and uncertainties that surrounded their outlook at the last MPC meeting continued. The major sources of uncertainty have persisted. They also commented on the various reasons of low global inflation and specifically referred to the various factors that had been impacting the changing inflation dynamics.

19. **With regards to the domestic inflation outlook, Members viewed that inflationary pressures remained broadly muted and the latest inflation outturn had come in lower than anticipated.** Headline inflation was projected to remain low in the short-term, barring any unforeseen exogenous shocks, amidst contained demand pressures and inflationary expectations. Core inflation measures have remained more or less flat. The MPC reiterated that it would continue to monitor inflation developments closely.

20. **Members noted that domestic macroeconomic developments had mostly remained on track, despite that some sectoral fragilities remained**. The MPC assessed the domestic economic performance and noted, on the basis of the Bank's projections, that growth in 2019 would be broad-based. The outlook for business investment and public sector infrastructure spending was positive. The key factors that would influence household consumption were supportive of consumer expenditure. Labour market conditions have remained commendable and the unemployment rate would be contained at more or less around its 2018 level. Members reviewed the latest performances of listed companies as well as of various sectors of the economy, including the sugar, manufacturing and tourism sectors.

21. **In their discussion of monetary policy, Members consented that it would be appropriate to maintain prudence over its stance**. 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, as it was continuing to support the domestic economy whilst maintaining price stability.

23. **The Committee stands ready to meet in between its regular meetings, if the need arises**.

24. **The next MPC meeting is scheduled on 9 August 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 17 May 2019, the last available data on national accounts, employment and external trade were for 2018Q4. The last data available on Consumer Price Index (CPI) and inflation were for April 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.