BANK OF MAURITIUS

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Minutes of the 45th Monetary Policy Committee Meeting held on 29 November 2017

The 45th meeting of the Monetary Policy Committee (MPC) was held on Wednesday 29 November 2017 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. Mohammad Mushtaq Namdarkhan, Dr Streevarsen Narrainen, Dr Renganaden Padayachy 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 44th MPC meeting held on 6 September 2017.

Global economic and financial developments

1. **Global economic growth has broadly kept momentum since the September 2017 MPC meeting, while global financial conditions have remained relatively easy.** In its October 2017 World Economic Outlook (WEO), the IMF projected global growth to be higher by 0.1 percentage point for both 2017 and 2018, at 3.6 per cent and 3.7 per cent, respectively, compared to projections made in April 2017. The more optimistic outlook resulted from growth upgrades for the Euro area, Japan, China, Emerging Europe and Russia. In addition, Global Purchasing Managers' Indices, which are leading global output indicators, have recovered since the slump in early 2016 and touched new highs in October 2017.

2. **The MPC noted that global inflation had gained some traction in the third quarter of 2017 on account of the pick-up in energy prices but remained under check.** The October 2017 WEO had projected inflation in advanced economies to rise from 0.8 per cent in 2016 to 1.7 per cent in 2017, reflecting both the increase in demand and pick-up in energy prices in the third quarter of 2017. Inflation in Emerging Market and Developing Economies is forecast to decline slightly from 4.3 per cent in 2016 to 4.2 per cent in 2017. Oil prices had gathered momentum, reflecting prospects of tighter supply conditions due to Saudi Arabia's commitment to help to rebalance the global crude market, the drop in US crude oil inventories and disruptions caused by geopolitical tensions. The monthly average oil price of NYMEX WTI thus firmed from US$49.9 per barrel in September 2017 to US$51.6 per barrel in October 2017 and has been averaging US$56.3 between 1 and 23 November 2017.

3. **The FAO food price index declined in October 2017, while grains prices were broadly stable.** Benefiting from favourable supply conditions and intense competition among exporters, the FAO food price index retreated to 176.4 in October 2017, and had remained quite contained over the past two years. Grains prices had also remained relatively stable since the last MPC meeting, with the International Grains Council's Grains and Oilseed Index declining from a monthly average of 193.9 in September 2017 to 192.9 in October 2017.

4. **Global equity markets had kept pace, while the US dollar strengthened since the last MPC meeting.** MSCI World and MSCI Emerging Markets Index rose by 4.8 per cent and 6.4 per cent, respectively, reflecting positive economic data and robust corporate earnings. Emerging markets performances were characterised by strong global growth momentum and encouraging economic activity in China. The US dollar's strength reflected favourable economic data, easing tensions with North Korea, prospects of tax reforms and further monetary policy tightening by the US Federal Reserve. Between 6 September and 23 November 2017, the US dollar index appreciated by about 1 per cent, while the Dow Jones US dollar index was up by 0.8 per cent.

5. **The MPC noted that the major central banks, with the exception of the Bank of England (BoE), had left their policy rates unchanged at their last interest-rate setting meetings but were moving prudently towards reducing their monetary stimulus packages**. The US Federal Reserve signalled that it could hike the Federal funds rate further by end-2017 and had begun, since October 2017, to reduce its holdings of around US$4.2 trillion in US Treasury bonds and mortgage-backed securities acquired in the aftermath of the global financial crisis. The European Central Bank indicated that it would halve its monthly asset purchase programme to EUR30 billion between January and September 2018, or until it sees inflation consistent with its target. The BoE, at its November meeting, increased interest rates for the first time in a decade by 25 basis points to 0.5 per cent in a bid to curtail high inflation.

Domestic economic developments

6. **The domestic economy's performance was better in 2017Q2 relative to both 2017Q1 and 2016Q2.** Real GDP growth was higher at 4.1 per cent in 2017Q2, following a 3.4 per cent gain in 2017Q1 and 2.6 per cent growth in 2016Q2. Quarter-on-quarter and seasonally-adjusted, real GDP increased by 0.9 per cent in 2017Q2 following expansion of 0.3 per cent in 2017Q1. Overall investment spending increased significantly, supported by a robust increase in 'building and construction work' as well as a rebound in capital expenditure on 'machinery and equipment'. Statistics Mauritius expects real GDP at market prices to grow by 3.9 per cent in 2017, supported by a significant rebound in the construction sector. On the supply side, the main economic sectors continued to expand and would further support growth.

7. **The MPC noted that headline inflation kept its uptrend and reached 3.4 per cent in October 2017, while year-on-year (y-o-y) inflation decelerated from 5.3 per cent in July 2017 to 3.5 per cent in October 2017**. The decline in y-o-y inflation reflected the downward adjustment of vegetables prices back to their market levels and the decline in mortgage interest rates on the back of the reduction of the Key Repo Rate in early September. Given developments in y-o-y

inflation and core inflation measures, the MPC viewed that inflationary pressures would not intensify in the foreseeable future. Inflation expectations (headline) assessed in the August 2017 BoM survey were broadly in line with developments in headline inflation.

8. **The unemployment rate moderated in the second quarter of 2017, as the rise in employment more than offset the increase in the labour force.** The rate of unemployment decreased from 7.4 per cent in 2016Q2 to 7.2 per cent in 2017Q2 while on a seasonally-adjusted basis, the unemployment rate also dropped from 7.1 per cent to 6.9 per cent. Based on projections made by Statistics Mauritius, the unemployment rate is expected to drop marginally to 7.2 per cent in 2017, from 7.3 per cent in 2016.

9. **The wage rate index rose by 3 per cent between 2016Q4 and 2017Q2, reflecting higher wages in sectors like 'public administration and defence; compulsory social security', 'education', 'administrative and support service activities' and 'information and communication' and 'manufacturing'.** Notwithstanding improvements in labour productivity, unit labour costs are projected to increase further by around 1 per cent in 2017.

10. **Preliminary estimates of Mauritius' balance of payments would show a higher current account deficit in 2017 compared to 2016, mostly due to the deepening of the goods account deficit.** The current account deficit has been estimated at Rs23.3 billion or 5.1 per cent of GDP in 2017, compared to Rs19.7 billion or 4.5 per cent of GDP in 2016. The goods account deficit is forecast to widen from Rs72.8 billion in 2016 to Rs84.7 billion in 2017, mainly as a result of higher imports and lower exports of goods. The surplus on the services account is estimated to rise from Rs27.2 billion in 2016 to Rs29.2 billion in 2017 thanks to higher gross tourism receipts. A higher surplus on the income account and a lower deficit on the current transfers account due to receipts of external grants are also being estimated. Overall, financial flows are expected to be more than adequate to finance the current account deficit.

11. **The rupee has continued to reflect the outcome of movements of major currencies on international markets, as well as domestic demand and supply conditions.** On a point-to-point weighted average dealt rate basis, between 6 September and 23 November 2017, the rupee depreciated against the US dollar, the Pound sterling and the euro by 2.7 per cent, 5.0 per cent and 1.5 per cent, respectively. On a real effective basis, the rupee depreciated by about 2 per cent in October 2017.

12. **The Bank continued with its open market operations to contain the expansion of excess liquidity in the system.** Between 6 September and 22 November 2017, the overall average excess liquidity in the banking system hardly changed, compared to the period 5 May to 5 September 2017 and averaged Rs12.7 billion. Bank of Mauritius Bills for tenors 91-Day, 182-Day and 364-Day are being issued simultaneously through separate auctions as from May 2017. As at close of business on 27 November 2017, the total outstanding amount of instruments issued for liquidity management stood at Rs68.9 billion, comprising Rs56.5 billion of Bank of Mauritius securities, Rs9.6 billion of deposits placed by banks and Rs2.8 billion of Treasury Bills.

13. **Broad money supply and private sector credit expansion gathered momentum in 2017Q3 compared to the same quarter in 2016.** Broad Money Liabilities grew by 8.8 per cent y-o-y in October 2017 compared to 7.3 per cent in July 2017. Bank credit to the private sector exclusive of credit to the GBC sector expanded by 5.7 per cent in October 2017, compared to 2.0 per cent in July 2017, supported by growth in corporate credit.

14. **The banking sector continued to remain sound and well-capitalised during the quarter ended September 2017.** The aggregate capital adequacy ratio fell from 17.9 per cent as at end-June 2017 to 17.1 per cent as at end-September 2017. Over the quarter ended September 2017, the ratio of non-performing loans to total loans increased marginally by 0.2 per cent to 8.0 per cent, somewhat due to higher impaired credit in Mauritius.

Staff Economic Outlook

15. **Bank staff forecasts for headline inflation and real GDP growth are conditional on specific assumptions regarding developments both abroad and at home.**

16. **Bank staff project that, barring any major shock, headline inflation would be more or less unchanged in 2018 compared to 2017.** Recent transitory shocks to the CPI are expected to dissipate over the coming months. The headline inflation forecast for 2017 has been revised down to about 3.6 per cent, reflecting the combined effect of lower prices of fresh vegetables and the reduction in mortgage interest payments. Bank staff project that headline inflation would be around 3.5 per cent for 2018, conditional on the absence of major supply shocks.

17. **Bank staff have maintained their forecasts for real GDP growth at market prices at about 3.8 per cent for 2017 but have projected growth to be higher at about 4.2 per cent for 2018.** The domestic real GDP growth momentum is expected to be sustained over the forecast horizon amid positive economic indicators. Accommodative monetary conditions, favourable business conditions, and substantial public and private investment projects, amongst others, are expected to provide the fillip to real GDP growth.

Monetary Policy Decision

18. **The Chairperson observed that global economic conditions had, so far, remained more or less unchanged, and the global economic outlook for 2018 would appear to be brighter**. The world economy was picking up, in spite of persistence of some downside risks associated with some economic and political uncertainties. On the domestic front, real GDP growth was forecast at around 3.8 per cent, thanks to the pick-up in investment and strong performance of the tourism sector. Tourism receipts are projected at around Rs60 billion in 2017. The balance of payments outlook would reflect a firming up of domestic demand conditions, in the context of the implementation of public and private projects and the introduction of a minimum wage policy.

19. **The Chairperson noted with concern that export of goods had declined by over Rs10 billion over the last three years.** This decline had been more or less offset by an increase in export of services such that overall, export of goods and services had remained stagnant. The current account deficit was estimated to rise to about 5 per cent of GDP in 2017 and would continue to be adequately financed by capital flows. Private sector credit growth, adjusted for the issue of bonds by large corporates, at around 7 per cent, was in line with nominal GDP growth and there was no risk to inflation from credit expansion at this stage.

20. **The MPC noted that global economic performance was upheld since the start of the second half of 2017 amid improved growth performances of some major economies, as well as, major commodity-exporting countries**. Members reviewed the economic performances and outlook of Mauritius' major trading partners and noted an improvement in economic fundamentals. They viewed that global inflation was expected to remain moderate. They noted that the global economy remained under the spell of challenges - both political and economic. Members would remain attentive vis-à-vis major central banks' call for reduction of their monetary stimulus packages in line with global economic recovery.

21. **Members reviewed domestic economic conditions and remained concerned with the export performance.** They also discussed lengthily on the growth performance and inflation developments. Overall, they observed that investment spending was firming and would support growth momentum. They viewed that conditions were well in place to ensure a higher growth performance in 2018 but maintained that the Committee would remain alert to any adverse developments.

22. **The MPC members discussed lengthily on the implications of the introduction of the minimum wage policy and negative income tax in Mauritius.** Members recognised that these initiatives are a major stride towards reforming the labour market.

Voting Pattern

23. **At the conclusion of the discussions, the Committee unanimously decided to maintain the Key Repo Rate at 3.50 per cent per annum with a view to continuing to support economic growth.**

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

25. **The next MPC meeting is scheduled on 28 February 2018.**

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 29 November 2017, the last available data on national accounts, employment and external trade were for 2017Q2. The last data available on Consumer Price Index (CPI) and inflation were for October 2017.

Abbreviations and Definitions

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. Both headline and y-o-y CORE1 inflation measures are available.
CORE2 inflation excludes food, beverages and tobacco, mortgage interest, energy prices and administered prices from the CPI basket. Both headline and y-o-y CORE2 inflation measures are available.
Y-o-y refers to year-on-year changes.
Q-o-q refers to quarter-on-quarter changes.
GMTBs refer to Government of Mauritius Treasury Bills.