



## BANK OF MAURITIUS

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### Minutes of the 44<sup>th</sup> Monetary Policy Committee Meeting held on 6 September 2017

The 44<sup>th</sup> meeting of the Monetary Policy Committee (MPC) was held on Wednesday 6 September 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 43<sup>rd</sup> MPC meeting held on 5 May 2017.

#### *Global economic and financial developments*

- 1. The pace of global economic activity maintained its sustainable gait since the May 2017 MPC meeting.** The IMF, in its July 2017 World Economic Outlook (WEO) update, broadly kept its world growth forecasts for 2017 and 2018 unchanged from its projections made in April 2017. US growth projections were scaled down marginally against the backdrop of a less expansionary fiscal policy. In the UK, growth projection was downgraded on weaker-than-expected economic activity in the first quarter of 2017. However, positive surprises came from the euro area and Japan, where economic growth projections were revised upward. The MPC noted that the global growth outlook was subject to downside risks stemming mainly from policy uncertainty in advanced economies, financial sector vulnerabilities in some countries, and rise in protectionism.
- 2. The MPC observed that, amidst easing oil prices, global inflationary pressures had somehow subsided.** In advanced economies, inflation remained at levels below central bank targets. Inflation in the US, UK and euro area declined in July 2017. Oil prices dropped as rising crude oil output from US shale fields disrupted OPEC's efforts to rebalance supply and demand. The monthly average oil price of NYMEX WTI, which gradually fell from US\$51.2 per barrel in April 2017 to US\$45.2 per barrel in June 2017, ticked up to US\$46.7 in July 2017. The FAO Food Price Index maintained its pace mostly due to supply constraints and currency movements. The index increased from 168.9 in April 2017 to 179.1 in July 2017, or by 6.0 per cent, sustained by the higher prices of dairy, cereals and meat. The International Grains Council's (IGC) Grains and Oilseed Index rose from an average of 181.8 in April 2017 to 199.6 in July 2017, up by 9.8 per cent, reflecting broad-based increases in its sub-components.

3. **The annual growth rate of global trade growth is forecast to accelerate from 2.3 per cent in 2016 to 4.0 per cent in 2017, supported by the pick-up in trade flows of both advanced economies and EMDEs.** The pick-up in economic activity in advanced economies would back the increase in the volume of goods and services traded, from 2.3 per cent in 2016 to 3.9 per cent in 2017. Trade growth for EMDEs is also expected to accelerate from 2.2 per cent to 4.1 per cent, bolstered by an anticipated rebound in demand for imports from large EMDEs.
4. **Global equity markets kept its momentum and emerging market equities outperformed those of developed markets following, amongst others, encouraging economic data from China and higher corporate earnings growth.** The MSCI World and MSCI Emerging Markets Index ended higher by 3.4 per cent and 9.0 per cent, respectively, between the two MPC meetings. European equities were supported by improving growth prospects. In the US, gains were checked by the US administration's inability to pass the healthcare bill and geopolitical tensions.
5. **The US dollar depreciated due to political and fiscal worries in the US, geopolitical tensions and dimmer prospects for another hike in US interest rates this year.** The euro gained ground as the European Central Bank grew increasingly hawkish, pointing to a possible tightening of monetary conditions. Between 5 May and 17 August 2017, the euro gained 6.8 per cent against the US dollar. The Pound sterling depreciated by 0.7 per cent against the US dollar amid heightened political uncertainty after the general elections in the UK.

#### *Domestic economic developments*

6. **After a strong performance in 2016Q4, the domestic economy moderated in 2017Q1, dragged down by the decline in exports and moderation in final consumption expenditure.** Investment spending increased noticeably, bolstered by a surge in building and construction work. At the sectoral level, the manufacturing sector stagnated on the back of contractions in textile and food sub-sectors, while growth in the construction sector remained buoyant. The services sector remained the major driver of growth, notwithstanding the slowdown in the accommodation and food service activities sector. Real GDP grew by 3.4 per cent y-o-y, compared to 3.8 per cent in 2016Q1 and 4.2 per cent in 2016Q4. Gross Fixed Capital Formation contributed positively to growth, increasing by 4.2 per cent in 2017Q1 compared to 3.8 per cent in 2016Q4 and 3.5 per cent in 2016Q1.
7. **The MPC noted that the increase in the domestic inflation rate since the last MPC meeting has been due to transient factors, which included the impact of higher prices of alcoholic beverages, tobacco and Mogas and diesel oil.** Headline inflation rose from 1.3 per cent in March 2017 to 2.7 per cent in July 2017. Y-o-y inflation, which accelerated to a five-year peak of 6.4 per cent in June 2017, subsided to 5.3 per cent in July 2017. Based on the stability in core inflation measures, the MPC did not find reasons to believe that inflationary pressures could intensify in the foreseeable future. Inflation expectations (headline) assessed in the May 2017 BoM survey, while swinging to the upside, remained consistent with developments in headline inflation.

8. **Labour market conditions did not change materially in 2017Q1, with the change in employment amounting to 7,900, while the labour force increased by 8,700 compared to 2016Q1.** The seasonally-adjusted unemployment rate declined from 7.3 per cent in 2016Q4 to 7.1 per cent in 2017Q1. The unemployment rate is expected to be about 7.3 per cent for 2017.
9. **The wage rate index rose by a further 4.3 points or 3.2 per cent, from 2016Q1 to 2017Q1, attributed to increased wages in key sectors of the economy,** such as manufacturing (0.8 point), financial activities (0.7 point), wholesale and retail trade, transportation and storage and construction (0.4 point each).
10. **Preliminary estimates of Mauritius' balance of payments point to almost a doubling in the current account deficit, from 4.4 per cent of GDP in 2016Q1 to 7.4 per cent in 2017Q1.** The higher current account deficit would reflect a wider deficit on the goods account, emanating from falling exports and growing imports, albeit partly offset by a higher surplus on the services and income accounts. The country is expected to register a higher current account deficit of about 5.0 per cent of GDP in 2017 compared to 4.3 per cent in 2016.
11. **The rupee 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 5 May and 22 August 2017, the rupee appreciated against the US dollar and the Pound sterling by 4.4 per cent and 4.0 per cent, respectively, but depreciated by 3.2 per cent against the euro. On a real effective basis, the rupee appreciated by about 5 per cent during the first half of 2017.
12. **The Bank maintained its open market operations to absorb the excess liquidity in the system, reflecting somewhat net maturing securities.** Excess cash reserves in the banking system averaged Rs13.2 billion between the last MPC meeting to 18 August 2017 compared to an average of Rs10.4 billion for the period 20 February to 5 May 2017. As at 25 August 2017, total outstanding amount of instruments issued for liquidity management stood at Rs74.3 billion.
13. **The annual growth of Broad Money Liabilities (BML) moderated, while private sector credit gathered some momentum in 2017H1.** BML grew at a lower pace of 2.9 per cent in 2017H1, compared to a rise of 3.9 per cent in 2016H1. Bank credit to the private sector (excluding credit to the GBC sector) bounced back into positive territory, with growth of 1.6 per cent in 2017H1 as against a contraction of 0.8 per cent in 2016H1.
14. **The banking sector remains sound and well-capitalised, with the aggregate capital adequacy ratio standing at 17.7 per cent at the end of March 2017, up from 17.4 per cent as at end-December 2016.** The ratio of non-performing loans to total loans fell to 6.9 per cent in 2017Q1, from 7.1 per cent in 2016Q1 but was marginally higher compared to 6.8 per cent in 2016Q4.

## Staff Economic Outlook

15. **Bank staff forecast, barring any major shock, that headline inflation would rise from its current level.** The recent transitory shock to the CPI is expected to dissipate over the coming months. The headline inflation forecast for 2017 has been projected at about 4.0 per cent and at about 3.8 per cent for 2018.
16. **Bank staff have lowered their projections for real GDP growth at market prices to between 3.6 – 3.8 per cent for 2017 but forecast higher growth of about 4.2 per cent for 2018.** The current monetary conditions and business optimism as revealed in private sector confidence surveys are expected to support domestic economic activity over the forecast horizon. The implementation of massive public investment projects assisted by private sector projects would further drive the domestic growth momentum in 2018.

## Monetary Policy Decision

17. **The Chairperson observed that the global economic conditions remained more or less unchanged, despite political uncertainties in some regions.** Global growth projections have been maintained and the outlook remains positive for the near term. The outcome of Brexit is still unsettled. He mentioned that domestic growth performance has been adversely affected by the performance of the exports sector. He noted that bank credit performance has been rather muted despite the small pick-up. The current account deficit is projected to deteriorate in 2017 due to a higher deficit in the goods account. Domestic inflationary pressures have been driven by temporary factors so far, and there do not appear to be any significant build-up in underlying inflationary pressures. The rupee has appreciated somewhat on a real effective basis, but remained broadly stable. Capital inflows have to some extent influenced the movement of the rupee. The Bank has been conducting sterilised foreign exchange intervention to smooth out volatility of the rupee.
18. **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 while investment spending has firmed up, final consumption expenditure moderated and export of goods and services kept declining. The MPC took note of the Bank's efforts to deal with the excess liquidity situation.
19. **The MPC perceived that the global economic environment would remain fraught with uncertainty over the near term, as divergent monetary policy paths across major central banks would be expected to prevail.** Uncertainty surrounding the monetary policy stance of the US Fed continues to influence inflation expectations, while accommodative monetary policy stance via conventional and unconventional tools would continue for the euro area and Japan. Mauritius, being a small open economy, is exposed to quite a significant extent to external developments.
20. **Weighing the risks to the domestic growth and inflation outlook, the MPC decided to give a fillip to the growth momentum.** Accordingly, the MPC decided to cut the Key Repo Rate by 50 basis points to 3.50 per cent per annum. Members agreed on the need to stimulate more investment into the productive sectors of the Mauritian economy.

## Voting Pattern

21. **At the conclusion of the discussions, the Committee unanimously voted to reduce the Key Repo Rate by 50 basis points to 3.50 per cent per annum.**
22. **The MPC continues to monitor economic and financial developments and stands ready to meet in between its regular meetings, if the need arises.**
23. **The next MPC meeting is scheduled on 29 November 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 6 September 2017, the last available data on national accounts, employment and external trade were for 17Q1. The last data available on CPI and inflation were for July 2017.

### 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 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.