Quarterly Economic Report

March 2019

BANK OF MAURITIUS

QUARTERLY ECONOMIC REPORT

March 2019

Section 4(1) of the Bank of Mauritius Act 2004 states that the primary object of the Bank of Mauritius is to maintain price stability and to promote orderly and balanced economic development. The formulation and determination of monetary policy is entrusted to the Monetary Policy Committee (MPC) as set out in Sections 54 and 55 of the Bank of Mauritius Act 2004. The MPC determines the appropriate monetary policy stance through changes in the Key Repo Rate. The MPC usually meets four times during a year, but stands ready to meet in between its regular meetings. In their decision-making process, MPC members assess the balance of risks between economic growth and inflation by considering a wide range of domestic and international economic and financial data and information. Given the time lags before monetary policy takes effect, the MPC is pre-emptive and forward-looking, and relies on a number of indicators, namely forecasts of relevant economic variables and assumptions.

This edition of the Quarterly Economic Report is the first issue of an on-line publication that will be released by the Bank of Mauritius on a quarterly basis. This Report supersedes the former Monetary Policy and Financial Stability Report. It aims to enhance the public's understanding of the policies applied to achieve the mandate of the Bank of Mauritius. The analysis in this Report is based on macroeconomic data available at the date of its preparation. Unless otherwise stated, this edition relies on information and financial data available as at 22 February 2019.

This Report is available on the Bank of Mauritius' website at https://www.bom.mu under the URL item *Publications and Statistics*. The Bank of Mauritius welcomes feedback from readers. Please forward comments and suggestions to *communications@bom.mu*

Quarterly Economic Report March 2019

ISSN 1694-3740

TABLE OF CONTENTS

1. SUMMARY

At its meeting held on 22 February 2019, the MPC unanimously voted to keep the Key Repo Rate unchanged at 3.50 per cent per annum. The MPC weighed the risks to the growth and inflation outlook and concluded that the monetary policy stance was broadly appropriate. The MPC remarked that it would be preferable to maintain stability in the monetary policy stance, which was continuing to support the domestic economy whilst maintaining price stability.

A synchronised global economic slowdown appeared to have kicked in. Most multilateral organisations including the IMF, World Bank, UN and OECD, have lowered their global growth projections for 2019 and 2020. Mauritius' major trading partner countries' output growth would be lower than initially projected. Global inflationary pressures have been projected to be relatively contained in the near-term, aided by the drop in energy prices in the last quarter of 2018.

In Mauritius, headline inflation, measured by the change in the 12-month average CPI, 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 and various derived inflation indicators also remained subdued and stable, indicative of subtle inflationary pressures. Demand-driven inflationary pressures in the economy also remained contained, as the economy was estimated to be operating with some degree of spare capacity. The impact of external pressures was mitigated with the decline in global oil prices, slower global growth and muted inflation abroad. The Bank assessed risks to the inflation outlook to be inclined to the downside and projected headline inflation at about 2.1 per cent for 2019 and 2.5 per cent for 2020 in the absence of major supply shocks.

The domestic economy was expected to remain on a steady growth path in 2019, led by domestic demand. Real GDP growth was forecast at 3.9 per cent for 2019 and around 4 per cent in 2020, backed by the performance of key sectors like construction, tourism, information and communication, and financial services sectors. On the expenditure side, economic activity would benefit from several public infrastructure projects; resilient household consumption expenditure; and various initiatives such as the support for small-scale entrepreneurs, youth skills development and female labour force participation. While global uncertainties and risks persist, the domestic economic environment would appear resistant as the current domestic policy mix remains stimulating.

The unemployment rate dropped from 7.0 per cent in 2017Q3 to 6.9 per cent in 2018Q3. On an annual basis, the unemployment rate has declined to a 17-year low of 6.9 per cent in 2018, from 7.1 per cent in 2017. The gradual decline in the unemployment rate has been associated with improved labour market outcomes on the supply side of the economy, with active labour market policies targeting specific segments of the unemployed.

Broad money supply has kept pace, indicating adequate supply of liquidity in the economy. The annual growth rate of Broad Money Liabilities rose to 6.3 per cent in December 2018, from 4.4 per cent in September 2018. The annual growth of bank loans to Other Nonfinancial Corporations, households and other sectors (excluding GBCs) decelerated 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.

The current account deficit was expected to increase in 2019, reflecting a widening deficit on the goods account arising from the higher imports associated with major infrastructure projects. This would, however, be fully funded from higher net inflows on the capital and financial account. As a percentage to GDP, the current account deficit was estimated to increase from around 5.7 per cent in 2018 to around 6.1 per cent (excluding the purchase of aircraft) in 2019. The improved performance of both the services and primary income accounts would partly contain the goods account deficit.

Excess liquidity in the banking system has been contained at tolerable levels thanks to the Bank's active open market operations through the issue of its own securities and sterilisation of proceeds following interventions on the domestic foreign exchange market. In addition, the 91-Day Treasury Bill rate has remained well within the interest rate corridor of the Bank's operational framework for monetary policy.

Table 1.1: Mauritius - Selected Economic Indicators

	2013	2014	2015	2016	2017	2018*	2019**
Real GDP at market prices (Y-o-y, per cent)@	3.4	3.7	3.6	3.8	3.8	3.8	3.9
Nominal GDP (Y-o-y, per cent)	6.2	5.3	4.5	6.1	5.2	6.1	6.0
Per capita GDP (Rs)	295,591	310,862	324,570	344,029	361,664	383,376	n.a.
Consumer price index (end of period)	92.9	93.1	94.3	96.5	100.6	102.4	n.a.
Consumer price index (average)	91.4	94.3	95.5	96.5	100.0	103.2	105.4
Average annual inflation (per cent)	3.5	3.2	1.3	1.0	3.7	3.2	2.1
Exchange rate (end of period, Rs/US$)	30.60	32.10	36.53	36.82	34.35	34.81	34.72 [1]
Exchange rate (average, Rs/US$)	31.14	31.06	35.61	36.33	35.33	34.60	34.77 [2]
Nominal depreciation (-) (average, per cent)	-1.5	0.3	-12.8	-2.0	2.8	2.1	-3.3 [3]
REER (end of period)	117.71	117.80	126.70	124.40	120.30	118.90	n.a.
REER (depreciation (-), end of period, per cent)	3.81	-0.08	-7.02	1.85	3.41	1.18	n.a.
91-Day Treasury/ BoM Bill yield (end of period, per cent)	3.26	2.21	3.39	2.76	2.41	3.40	3.28 [4]
91-Day Treasury/ BoM Bill yield (average, per cent)	2.59	2.21	1.83	2.54	2.13	3.38	3.27 [5]
Unemployment rate (per cent)	8.0	7.8	7.9	7.3	7.1	6.9	6.7
Per cent of GDP	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**2016/17**	**2017/18**	**2018/19****
Budgetary revenue	21.2	21.0	20.5	20.9	21.1	22.5	22.9
of which: Tax revenue	*18.2*	*18.8*	*18.4*	*18.5*	*18.8*	*19.4*	*19.5*
Budgetary expenditure	23.2	24.5	24.2	24.4	24.6	25.5	26.1
of which: Wages and salaries	*5.6*	*6.2*	*6.1*	*6.2*	*6.4*	*6.2*	6.1
Interest payments	*2.7*	*2.6*	*2.5*	*2.4*	*2.5*	*2.4*	2.6
Budget balance	-2.0	-3.5	-3.7	-3.5	-3.5	-3.1	-3.2
of which: Central Government primary balance	*0.7*	*-0.9*	*-1.2*	*-1.1*	*-1.0*	*-0.6*	*-0.6*
Per cent of GDP	**Dec-16**	**Dec-17**	**Mar-18**	**Jun-18**	**Sep-18**	**Dec-18**	**June-19****
Total Budgetary Central Government debt	59.1	56.9	56.6	57.0	57.6	56.8	57.0
of which: Domestic	47.2	47.1	47.0	47.5	48.8	48.3	*48.6*
External	11.9	9.9	9.6	9.5	8.8	8.5	8.4
Total public sector debt	64.2	63.4	62.9	63.3	64.0	64.5	63.1
of which: Domestic	49.4	50.9	50.8	51.1	52.5	53.3	51.8
External	14.7	12.5	12.2	12.2	11.5	11.2	11.3
Per cent of GDP	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019****
Trade balance	-18.7	-17.7	-16.0	-16.6	-19.8	-21.1	-22.7
Current account balance	-6.2	-5.4	-3.6	-4.0	-5.6	-5.7	-7.2
of which: Exports of goods, f.o.b	*23.6*	*24.2*	*22.8*	*19.4*	*17.8*	*16.6*	*16.1*
Exports of services	*22.9*	*22.7*	*23.4*	*23.1*	*23.0*	*22.3*	*21.7*
Imports of goods, f.o.b	*-42.3*	*-41.9*	*-38.7*	*-36.0*	*-37.6*	*-37.7*	*-38.8*
Imports of services	*-18.2*	*-16.6*	*-17.5*	*-16.8*	*-16.6*	*-15.3*	*-14.8*
Overall balance of payments (Rs billion)	+16.6	+23.0	+20.0	+26.2	+28.3	+16.6	+9.8
Gross Official International Reserves (Rs million)	105.0	124.3	152.9	178.9	200.4	217.6	226.5
Y-o-y, per cent	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019****
Net foreign assets	-1.3	15.5	15.6	3.8	3.2	0.7	4.8
Net domestic assets	14.6	-0.3	6.7	3.5	16.5	-6.8	7.9
*of which: Claims on other sectors^*	*13.5*	*-2.8*	*8.1*	*1.0*	*15.0*	*-8.8*	*7.0*
Net Claims on Central Government	*29.9*	*28.8*	*-6.2*	*29.1*	*28.5*	*8.1*	*13.8*
Broad money	5.8	8.7	10.2	9.1	9.3	6.3	8.0
Private sector credit	5.9	1.3	4.2	-0.2	8.0	n.a.	n.a.
Income velocity of money	1.0	1.0	0.9	0.9	0.9	0.9	0.9
Money multiplier	5.9	5.9	6.0	5.8	5.1	5.5	5.5

*Note: *: Estimate. **: Forecast. Y-o-y: Year-on-year.*

@Bank of Mauritius staff estimate for 2019. n.a. not available.

[1] Data for 22 February 2019. [2] Average up to 22 February 2019.

[3] Average for 1 January to 22 February 2019 compared to February 2018.

[4] Data for auction held on 22 February 2019. [5] Average up to 22 February 2019.

^Effective May 2018, Financial Derivatives are recorded at market or fair values and are not strictly comparable with prior months' data.

Unless otherwise stated, this Table is based on data available as at 22 February 2019.

2. Recent Global Economic and Financial Developments

The global economy, which started the year 2018 on a solid footing, lost some momentum during the second half of the year on account of a host of factors. Accordingly, growth projections for 2019 have been scaled down successively by a number of major forecasting institutions, notably the International Monetary Fund (IMF), Organisation for Economic Cooperation and Development (OECD), World Bank and the United Nations (UN). Downside risks to global growth have intensified, casting shadows over the near-to-medium term outlook. On the other hand, global inflation was expected to remain broadly contained in 2019.

2.1 Economic Activity

The IMF lowered its global growth rate projection for both 2018 and 2019 by 0.2 percentage point to 3.7 per cent in October 2018 and reduced the growth rate for 2019 further to 3.5 per cent in January 2019 (Table 2.1). In the first two World Economic Outlook (WEO) reports of 2018, the IMF pointed to a brightening outlook of the world economy, reflecting a strengthening of economic activity and suggesting that the economic recovery would be more balanced and evenly distributed across various economic areas. Risks to the growth outlook in the near term were also assessed to be broadly balanced. However, the adverse impact of the imposition of trade tariffs in the US and China on trade and economic activity and the slowdown in growth in some key economies, including Germany, Japan, Italy and Turkey, largely due to idiosyncratic influences during the second quarter of 2018 prompted the growth downgrade.

Table 2.1: Real GDP Growth Rates in Selected Economies

	IMF				OECD				World Bank				United Nations			
	January 2019 World Economic Outlook Update Projections		Difference from October 2018 World Economic Outlook Projections		November 2018 Economic Outlook Projections		Difference from September 2018 Interim Economic Outlook Projections		January 2019 Global Economic Prospects Projections		Difference from June 2018 Global Economic Prospects Projections		World Economic Situation and Prospects 2019 Projections		Difference from World Economic Situation and Prospects 2018 Projections	
	Per cent		*Percentage point*		*Per cent*		*Percentage point*		*Per cent*		*Percentage point*		*Per cent*		*Percentage point*	
	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019
World Output	**3.7**	**3.5**	**0.0**	**-0.2**	**3.7**	**3.5**	**0.0**	**-0.2**	**3.0**	**2.9**	**-0.1**	**-0.1**	**3.1**	**3.0**	**-0.1**	**-0.2**
Advanced Economies	**2.3**	**2.0**	**-0.1**	**-0.1**	**n.a**	**n.a**	**n.a**	**n.a**	**2.2**	**2.0**	**0.0**	**0.0**	**2.2**	**2.1**	**0.0**	**0.0**
United States	2.9	2.5	0.0	0.0	2.9	2.7	0.0	0.0	2.9	2.5	0.2	0.0	2.8	2.5	0.3	0.2
Euro Area	1.8	1.6	-0.2	-0.3	1.9	1.8	-0.1	-0.1	1.9	1.6	-0.2	-0.1	2.0	1.9	-0.1	0.0
Japan	0.9	1.1	-0.2	0.2	0.9	1.0	-0.3	-0.2	0.8	0.9	-0.2	0.1	1.0	1.4	-0.6	-0.1
Emerging Market and Developing Economies	**4.6**	**4.5**	**-0.1**	**-0.2**	**n.a**	**n.a**	**n.a**	**n.a**	**4.2**	**4.2**	**-0.3**	**-0.5**	**4.4**	**4.3**	**-0.4**	**-0.5**
China	6.6	6.2	0.0	0.0	6.6	6.3	-0.1	-0.1	6.5	6.2	0.0	-0.1	6.6	6.3	0.1	0.0
India	7.3	7.5	0.0	0.1	7.5	7.3	-0.1	-0.1	7.3	7.5	0.0	0.0	7.4	7.6	-0.1	0.0

n.a not available.
Sources: IMF, OECD, World Bank and United Nations.

The OECD, World Bank and UN also revised down their respective global growth forecasts during the course of 2018. In March 2018, the OECD projected the world economy to grow at 3.9 per cent in both 2018 and 2019 and also corroborated the IMF's standpoint that the world economy was expected to strengthen and that the recovery was becoming more broad-based. In September 2018, the OECD revised down global growth rates by 0.2 percentage point to 3.7 per cent for both 2018 and 2019, arguing that the outlook was plagued with heightening risks, notably mounting trade conflicts, tightening financial conditions in emerging market economies and political risks. In November 2018, the global growth forecast for 2019 was trimmed by another 0.2 percentage point to 3.5 per cent, albeit that for 2018 was maintained at 3.7 per cent. The OECD attributed the gloomier economic outlook for 2019 to worsening prospects, particularly in emerging market economies, namely Turkey, Argentina and Brazil. The World Bank, in the January 2019 issue of its Global Economic Prospects, viewed global economic activity to be slowing, dragged down by a loss of momentum in both investment and international trade, elevated trade conflicts and financial market turmoil in a number of emerging market economies. The UN, through its bi-annual report on the World Economic Situation and Prospects (WESP) published in January 2019, lowered global growth forecasts by 0.1 percentage point and 0.2 percentage point for 2018 and 2019 to 3.1 per cent and 3.0 per cent, respectively. The UN indicated that world growth might have peaked as the pace of expansion of global industrial production and merchandise trade volumes had been decelerating since early 2018.

Against the backdrop of softening growth momentum, risks over the near-to-medium term have tilted to the downside due to mounting uncertainty arising from tighter financial conditions, trade conflicts and geopolitical tensions. The implementation of protectionist trade measures and uncertainty surrounding major trade negotiations such as the NAFTA and the post-Brexit relationships, have impacted on consumer confidence and might threaten trade and investment. In addition, higher interest rates in the US and a stronger US dollar could curtail capital inflows to emerging economies and further weaken their currencies, which were already vulnerable due to high debt commitments and constrained policy space.

Simultaneously, global financial markets became increasingly turbulent amid the negative impact of protectionist trade measures, and US risk assets outperforming assets in other jurisdictions. The divergence between the US and other major financial markets was most evident in equity prices and was mainly explained by solid corporate earnings and buybacks that were boosted by the recent tax reform and higher returns of the US technology sector. In the medium-term, risks could stem from a potential continued build-up of financial vulnerabilities, subdued global growth outlook, and intensification of the global trade disputes, among others.

In the US, real GDP growth reached a three-year high in 2018Q3, but latest economic data had shown a moderation in economic activity. US growth accelerated to 3.0 per cent in 2018Q3, bolstered by higher consumer spending amidst ongoing fiscal stimulus. Sound labour market developments, with the unemployment rate falling to a 49-year low of 3.7 per cent in 2018Q3, remained supportive of consumption spending. However, the Purchasing Managers Indices (PMIs) have begun to show signs of weakening, indicating that the economy's expansion might have peaked. The Manufacturing PMI slid to a one-year low of 53.8 in December 2018, while both the Services and Composite PMI dropped to 54.4, as new orders' growth slowed. Ongoing trade tensions between US and China have engendered much uncertainty, thereby undermining business sentiment and investment growth. Concerns over the global slowdown and monetary policy stance have also been weighing on investors' confidence. Growth in the US economy was expected to ease to 2.5 per cent in 2019, from 2.9 per cent in 2018, as support to domestic activity from the fiscal stimulus was being withdrawn. The Fed has halted its interest rate tightening cycle.

Eurozone's growth continued to be hampered by a combination of transitory shocks. Real GDP growth slipped to 1.6 per cent in 2018Q3, from 2.2 per cent in 2018Q2 and 2.8 per cent in 2017Q3, broadly reflecting the impact of introduction of new rules on car emission in Germany, higher borrowing costs on sovereign yields in Italy, as well as street protests and industrial action in France. Private consumption expenditure had, nevertheless, remained resilient and was supported by broad-based employment growth across European economies as the unemployment rate dropped to a nine-year low of 8.1 per cent in 2018Q3. The PMI for the manufacturing sector dropped to 51.4 in December 2018, its lowest reading since February 2016. The Services PMI also plunged to a four-year low of 51.2. The euro area's economic growth rate was expected to decline from 1.8 per cent in 2018 to 1.6 per cent in 2019.

UK's economy continued to expand at a tempered pace, with Brexit-related uncertainties plaguing business activity. Real GDP growth inched higher to 1.5 per cent in 2018Q3, from 1.4 per cent in 2018Q2, with the buoyancy in consumption spending contributing to support the economic growth momentum. Household consumption benefitted from improved consumer sentiment amid strong labour market indicators, as reflected in the drop of the unemployment rate to 3.8 per cent in 2018Q3. However, investment spending stagnated, with decision-making constrained by uncertainty over the Brexit outcome. Although the Manufacturing PMI recovered from its October 2018 trough of 51.1 to 54.2 in December 2018, it remained weak on account of subdued external demand. The Services and Composite PMI settled near recent lows of 51.2 and 51.4, respectively, in December 2018, as intensifying Brexit-uncertainty pushed economic agents to delay spending plans. Real GDP growth was expected to recover modestly to 1.5 per cent in 2019, from 1.4 per cent in 2018, benefitting from the fiscal stimulus announced in the 2019 Budget, but subject to the country striking a Brexit deal.

The pace of expansion in activity has slowed in emerging market and developing economies (EMDEs). Growth expansion in EMDEs was estimated to have eased from 4.7 per cent in 2017 to 4.6 per cent in 2018 and would drop to 4.5 per cent in 2019. China's growth momentum softened as domestic activity was constrained by policies to regulate the financial sector while the effects of ongoing trade frictions with the US were becoming increasingly apparent. Alongside, government efforts to curb risks emanating from elevated financial debt and tighter global financing conditions contributed to low investment growth. The Manufacturing PMI fell sharply to 49.7 in December 2018, as US-China trade dispute weighed heavily on external demand, which pushed manufacturers to reduce stock levels. The Services PMI recovered from the 13-month low of 50.8 reached in October 2018 to 53.9 in December 2018, contributing to supporting the Composite PMI to 52.2. Considering the impact of recent trade developments on economic activity, GDP growth in China was expected to moderate further to 6.2 per cent in 2019. The growth estimates for other emerging economies, including Turkey and Argentina, had also been revised down on account of prevailing financial distress, higher political risks and heightened uncertainties.

In contrast, India was expected to secure its position as the driver of growth across EMDEs, and post a robust growth rate of 7.5 per cent in 2019. India grew at an appreciable rate of 7.2 per cent in 2018Q3, though lower compared to 7.8 per cent in 2018Q2. The dynamism in capital investment, in particular by the public sector, helped in sustaining the growth momentum. Business activity indicators remained quite upbeat, reflecting sustained optimism in economic conditions in India, albeit a modest decline in both the Manufacturing and Services PMI to 53.2 in December 2018, with the Composite PMI settling at 53.6. Massive public sector spending on capital goods and implementation of structural reforms were expected to further boost the economy.

The real GDP growth of major trading partner countries for Mauritius also moderated during the course of 2018. The Trading Partner Countries' Growth (TPG) rate for Mauritius, derived on the basis of the country's export destination, declined from 2.5 per cent in 2018Q1 to 2.3 per cent in 2018Q2 and further to 2.1 per cent in 2018Q3. The moderation in the TPG resulted from the marked slowdown across Eurozone countries and key emerging economies, including China. TPG rate should drop from 2.5 per cent in 2017 to 2.3 per cent in 2018 (Chart 2.1).

Bearing the brunt of easing global growth momentum amidst global economic uncertainty, world trade volumes slowed markedly, while the Baltic Dry Index (BDI) plunged sharply. In November 2018, the annual growth of world trade volume dropped to 0.7 per cent, from 5.2 per cent in October 2018, reflecting moderating growth in both world imports and exports. Export and import activities in advanced economies declined because of sluggish domestic economic growth. In contrast, export and import activities in developing economies increased as a result of frontloading and policy to reduce import duties in China and economic gains in India. The BDI mirrored the evolution of world trade volume, falling systematically since September 2018 but recouped in December 2018. The BDI more than halved to 624 in February 2019[1], from 1,335 in December 2018, thereby pointing to further moderation in global trade volumes.

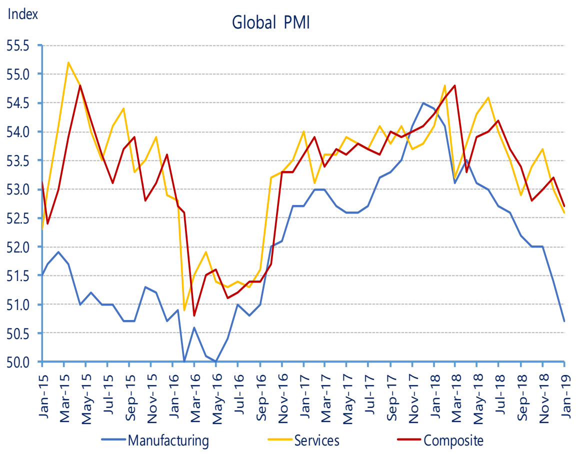
2.2 Global Commodity Prices

Crude oil prices have been rather volatile in the second half of 2018 and were influenced by a number of factors ranging from geopolitical tensions to trade frictions, but picked up in the beginning of 2019, supported by OPEC's decision to curb supply. While oil prices soared to a four-year high above US$85/barrel in October 2018 amid the imposition of sanctions on Iran by the US, they subsided to lower levels thereafter, with downward pressures stemming from prospects of weak demand, given signs of the softening of global economic growth and concerns over excess supply. The ICE Brent and the NYMEX West Texas Intermediate (WTI) closed 2018 at US$53.8/barrel and US$45.4/barrel, respectively, almost 20 per cent and 25 per cent lower compared to the reading at the start of the year. However, the ICE Brent and NYMEX WTI jumped to US$64.1/barrel and US$54.6/barrel, respectively, in February 2019[1] on OPEC's supply tightening (Chart 2.2).

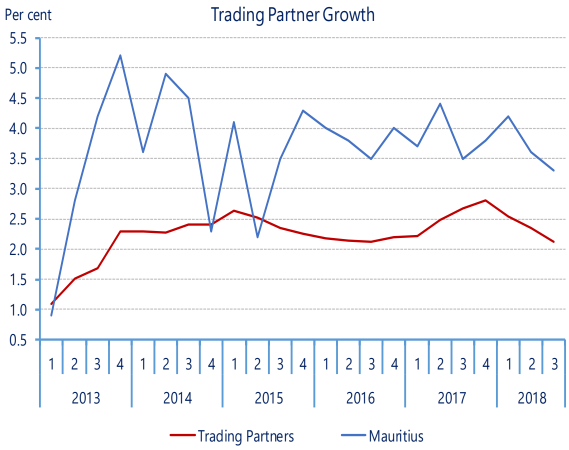
[1] *Average 1-22 February 2019.*

Global food prices, including prices in the grains market, have been broadly on a downtrend since June 2018 notwithstanding the uptick in January 2019. The FAO Food Price Index dropped from 173 in June 2018 to 162 in November 2018, but recovered to 165 in January 2019. On a y-o-y basis, the Index was still lower by about 2 per cent in January 2019. Sugar prices declined by 9.0 per cent in January 2019, reflecting favourable harvest and ample inventories. The Oils Price Index continued its slide, falling by 19.6 per cent, led by high stock levels in major producer economies. The Meat Price Index was lower by 2.7 per cent. Dairy and Cereals prices shirked the trend, increasing by 1.2 per cent and 7.3 per cent, respectively. The International Grains Council (IGC) Grains and Oilseed Index averaged 195 points in February 2019[2], down by 2.5 per cent y-o-y and 3.5 per cent lower compared to June 2018. The January 2019 World Bank Global Economic Prospects projected agricultural prices to remain broadly stable over the medium term.

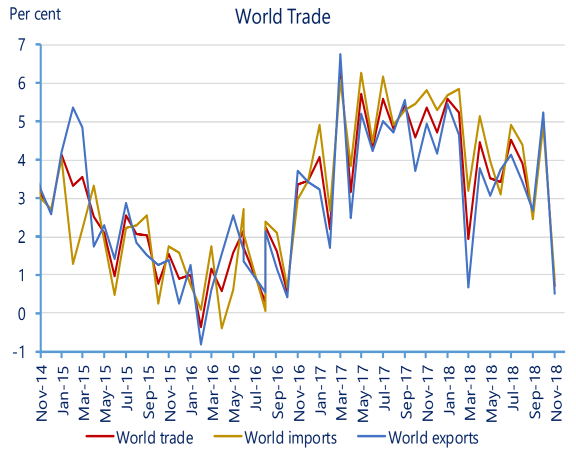
Chart 2.1: Real GDP Growth and World Trade



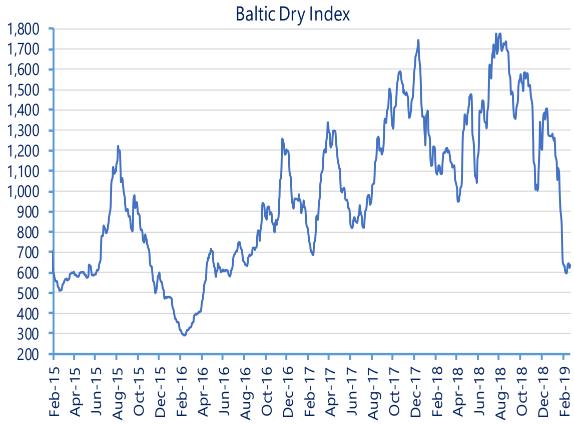
Source: Markit.



Source: Bank staff calculations.



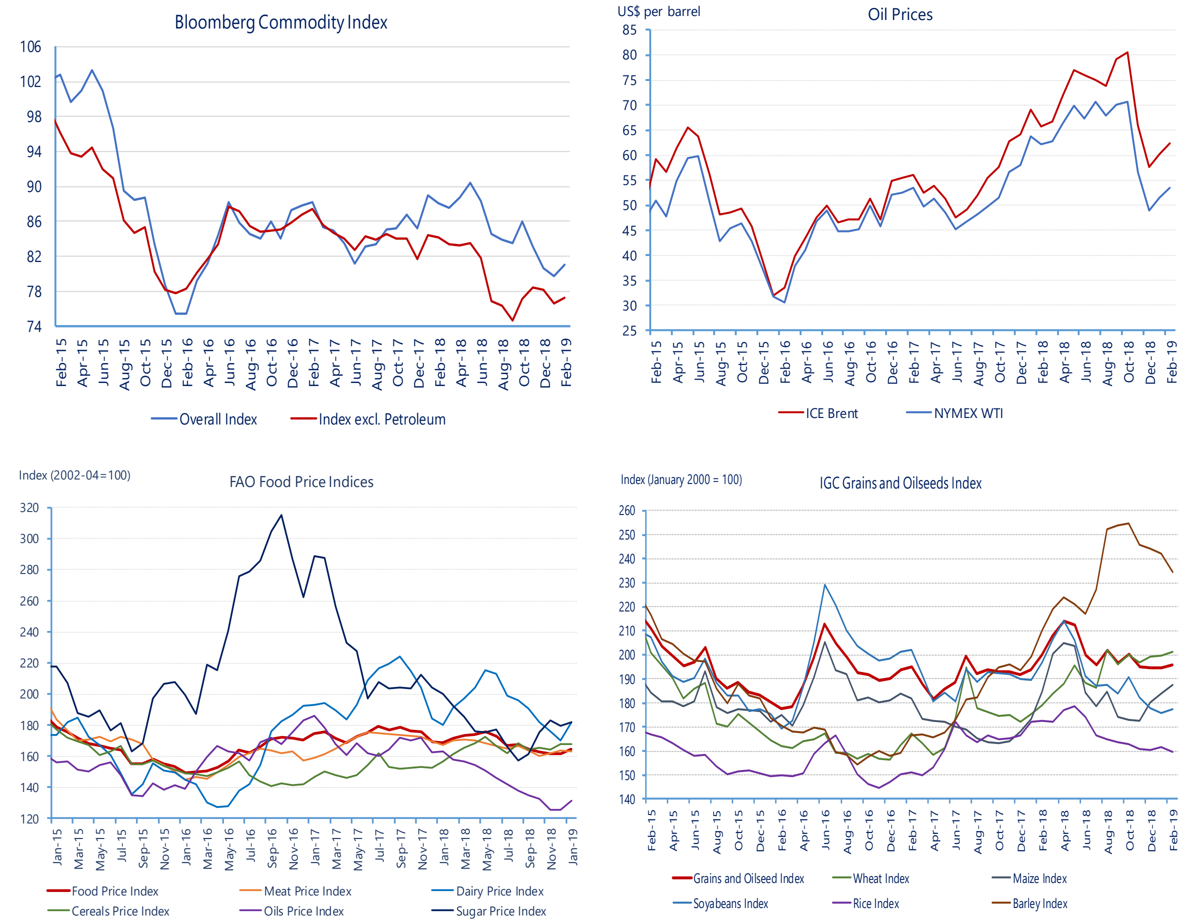
Source: CPB Netherlands Bureau of Economic Research.



Source: Reuters.

[2] *Average 1-22 February 2019.*

Chart 2.2: Global Commodity Prices



Sources: Bloomberg, Reuters, FAO and IGC.

2.3 Global Equity Markets

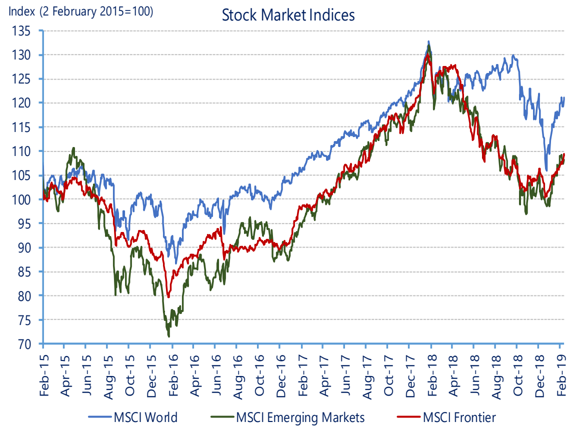
Global stock markets have been quite jittery since August 2018 and underwent some corrections. Between June 2018 and February[3] 2019, the MSCI World Index, the MSCI Emerging Market Index and the MSCI Frontier Market Index declined by 3.1 per cent, 5.8 per cent and 4.3 per cent, respectively (Chart 2.3). The sell-off was, to a certain extent, explained by the US interest rate normalisation cycle and expectations that the US Federal Reserve would continue to hike interest rates. Stock markets also performed poorly due to intensified concerns over the ongoing trade dispute between US and China that kept a lid on investors' risk appetite. Other factors that took a toll on the performance of stock markets were uncertainties surrounding the Brexit negotiations, the Italian crisis resulting from budget disagreement, and worries over the slowdown in global growth momentum.

Heightened uncertainty prevailed between June 2018 and January 2019, caused by Brexit negotiations; political uncertainty in Italy; the sustainability of robust earnings; as well as the trade conflict between US and China and geopolitical concerns. The Global Economic Policy Uncertainty Index rose by 46 per cent, from 196 in June 2018 to 287 in January 2019 and compared to January 2018, the index surged by 154 per cent. The indices for the US, Europe and UK increased by 111 per cent, 6 per cent and 9 per cent, respectively. On the other hand, volatility, as gauged by

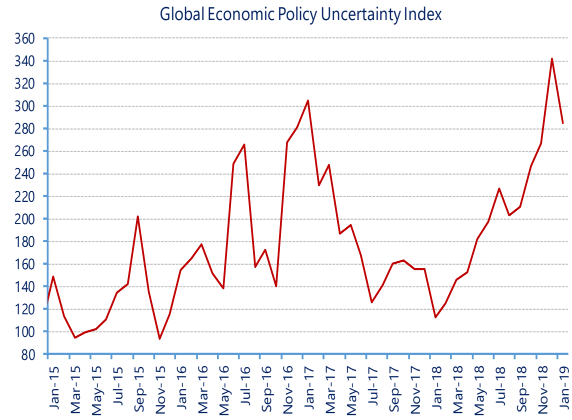
[3] *Average 1-22 February 2019.*

VIX and VIX-Emerging Markets, which peaked at 25 and 32, respectively, on 24 October 2018, attributable to turbulences in Turkey, Indonesia and Argentina, retreated subsequently to 14 and 17, respectively, on 22 February 2019.

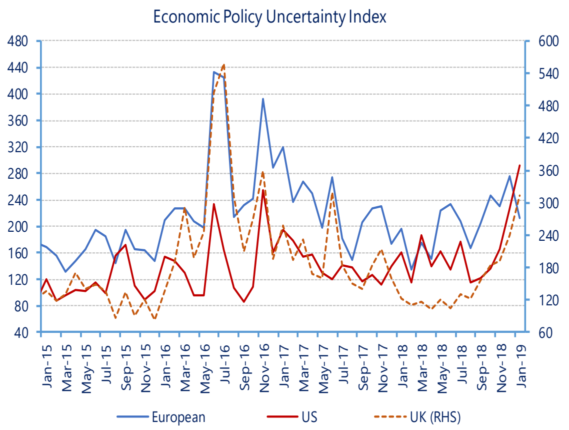
Chart 2.3: Stock Market and Volatility



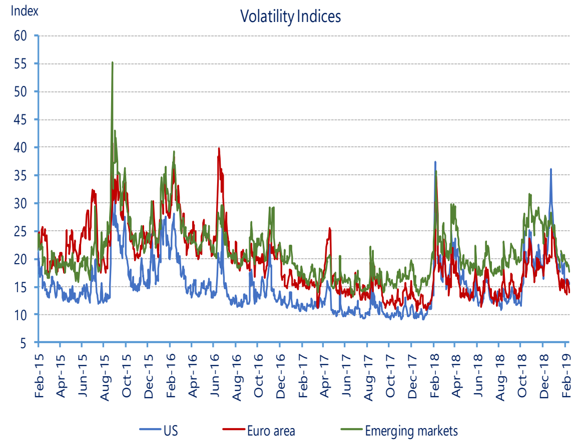
Source: Reuters.



Source: http://www.policyuncertainty.com



Source: http://www.policyuncertainty.com



Source: Reuters.

2.4 Global Inflation Developments

Global inflationary pressures remained broadly contained in 2018Q4, partly aided by the drop in energy prices in 2018Q4. Inflation in the US dropped from 2.5 per cent in October 2018 to a sixteen-month low of 1.9 per cent in December, reflecting the drastic decline in gasoline, fuel oil and electricity costs. Inflation in the Eurozone dropped from a five-year high of 2.2 per cent in October 2018 to 1.6 per cent in December 2018. In the UK, inflation moderated from a high of 2.7 per cent in August 2018 to 2.1 per cent in December 2018, the lowest since January 2017, with lower cost of petrol and airfares accounting to a major extent for the decrease in inflation. Inflation in China eased to 1.9 per cent in December 2018, after peaking at 2.5 per cent in October 2018, thanks to subdued price developments in food items. Inflation in India retreated from 3.4 per cent in October 2018 to 2.2 per cent in December 2018, largely attributed to the substantial decline in crude oil prices, amidst sluggish domestic demand conditions. Inflationary pressures in South Africa subsided, with the inflation rate dropping to 4.5 per cent in December 2018, the lowest since May 2018. The decline in transport costs, associated with lower prices for fuel and a stronger currency, largely accounted for the decrease in the inflation rate. According to the January 2019 IMF WEO

Update, inflation in advanced economies would firm from 1.7 per cent in 2017 to 2.0 per cent in 2018, and inflation in emerging economies would rise from 4.3 per cent to 4.9 per cent (Table 2.2).

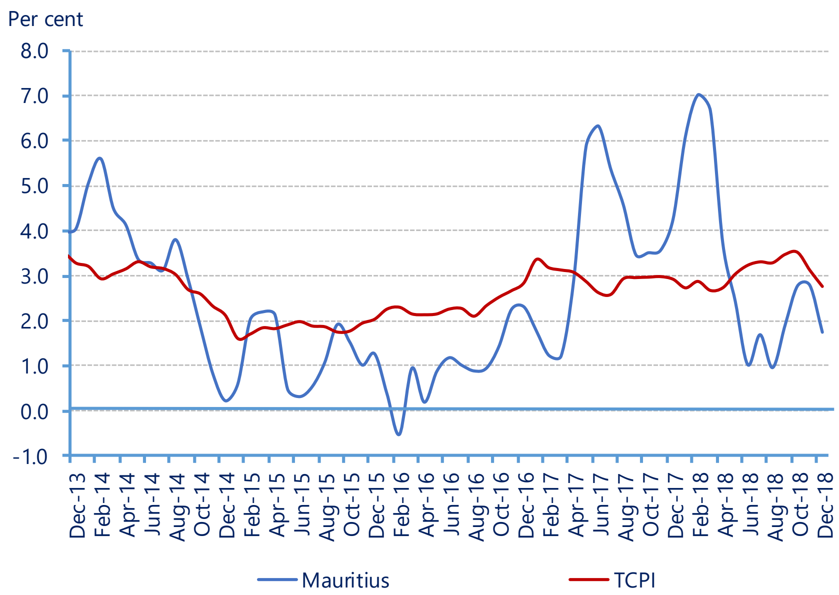
Table 2.2: Consumer Price Inflation in Selected Economies

	Actual			April 2018 WEO Projections		October 2018 WEO Projections		Difference from April 2018 WEO Projections	
	Per cent			Per cent		Per cent		Percentage point	
	2015	2016	2017	2018	2019	2018	2019	2018	2019
Advanced Economies	**0.3**	**0.8**	**1.7**	**2.0**	**1.9**	**2.0**	**1.9**	**0.0**	**0.0**
of which									
United States	0.1	1.3	2.1	2.5	2.4	2.4	2.1	-0.1	-0.3
Euro Area	0.0	0.2	1.5	1.5	1.6	1.7	1.7	0.2	0.1
Germany	*0.1*	*0.4*	*1.7*	*1.6*	*1.7*	*1.8*	*1.8*	*0.2*	*0.1*
France	*0.1*	*0.3*	*1.2*	*1.5*	*1.6*	*1.9*	*1.8*	*0.4*	*0.2*
Italy	*0.1*	*-0.1*	*1.3*	*1.1*	*1.3*	*1.3*	*1.4*	*0.2*	*0.1*
Spain	*-0.5*	*-0.2*	*2.0*	*1.7*	*1.6*	*1.8*	*1.8*	*0.1*	*0.2*
United Kingdom	0.0	0.7	2.7	2.7	2.2	2.5	2.2	-0.2	0.0
Japan	0.8	-0.1	0.5	1.1	1.1	1.2	1.3	0.1	0.2
Emerging Market and Developing Economies	**4.7**	**4.3**	**4.0**	**4.6**	**4.3**	**5.0**	**5.2**	**0.4**	**0.9**
Sub Saharan Africa	6.9	11.2	11.0	9.5	8.9	8.6	8.5	-0.9	-0.4
South Africa	4.6	6.3	5.3	5.3	5.3	4.8	5.3	-0.5	0.0
Emerging and Developing Asia	2.7	2.8	2.4	3.3	3.3	3.0	3.2	-0.3	-0.1
of which									
China	1.4	2.0	1.6	2.5	2.6	2.2	2.4	-0.3	-0.2
India	4.9	4.5	3.6	5.0	5.0	4.7	4.9	-0.3	-0.1

Source: October 2018 IMF WEO.

Inflationary pressures in the main trading partner countries of Mauritius abated by end-2018 and were projected to remain subdued. The Trading Partner Countries' Consumer Price Inflation (TCPI), based on the source import countries, dropped from 3.5 per cent in October 2018 to 2.8 per cent in December 2018, reflecting the fall in energy prices (Chart 2.4). Overall, the TCPI has remained almost flat at around 3 per cent since December 2016.

Chart 2.4: Trading Partner Inflation

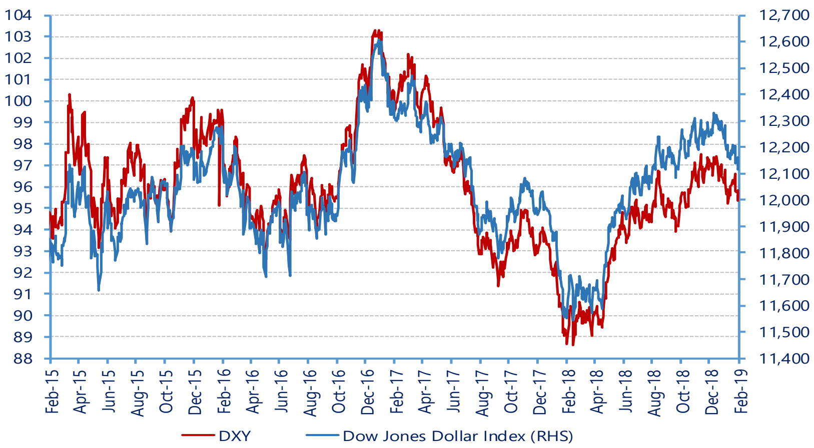


Source: Bank staff calculations.

2.5 Exchange Rates

Global currency markets were largely influenced by the ongoing trade dispute between the US and China, the hawkish stance of the US Fed and political risks in Europe. The US dollar appreciated against major currencies, underpinned by upbeat economic data and prospects for a tighter monetary policy stance by the US Fed, although heightened trade conflict between the US and China limited to some extent the gains. Safe-haven flows amid growing uncertainties and geopolitical tensions lent further support to the US currency. Between June 2018 and February 2019[4], the Dollar Index and the Dow Jones Dollar Index appreciated by 2.3 per cent and 1.7 per cent, respectively (Chart 2.5). Compared to December 2018, both indices were down by 0.3 per cent and 0.5 per cent, respectively. The European Central Bank's (ECB) survey of professional forecasters downward revision of the Eurozone growth and inflation rates for both 2018 and 2019 weighed on the euro. Further, the European Commission's decision to reject the Italian government's budget plan for 2019; political uncertainties in Germany; a fall in the Sentix Eurozone investor confidence index to a two-year low, weak retail sales data and a lower current account surplus also hit the euro. The euro depreciated by 2.9 per cent between June 2018 and February 2019[2], while compared to December 2018, it depreciated by 0.3 per cent. The Pound sterling came under pressure during most of the period under consideration, driven by disagreements between the UK and the EU during the Salzburg Summit in Austria; domestic political tensions and Brexit-related uncertainties. The Pound sterling was also adversely impacted by diminished prospects for higher interest rates by the Bank of England (BoE) in the near future as inflation moved closer to the BoE's inflation target of 2.0 per cent. However, a resilient UK construction sector and Brexit speculation buoyed the British currency. The Pound sterling depreciated by 2.5 per cent vis-à-vis the US dollar between June 2018 and February 2019[2], but appreciated by 2.3 per cent compared to December 2018. Emerging market currencies underperformed, reflecting the broad-based strength of the US dollar. Several emerging market economies saw their currencies weaken as the US continued with its interest rate normalisation cycle, which in turn, impacted negatively on emerging economies' financial markets, triggering sharp depreciations in their currencies. These included the Turkish lira and the Argentine peso, among others.

Chart 2.5: Dollar Index



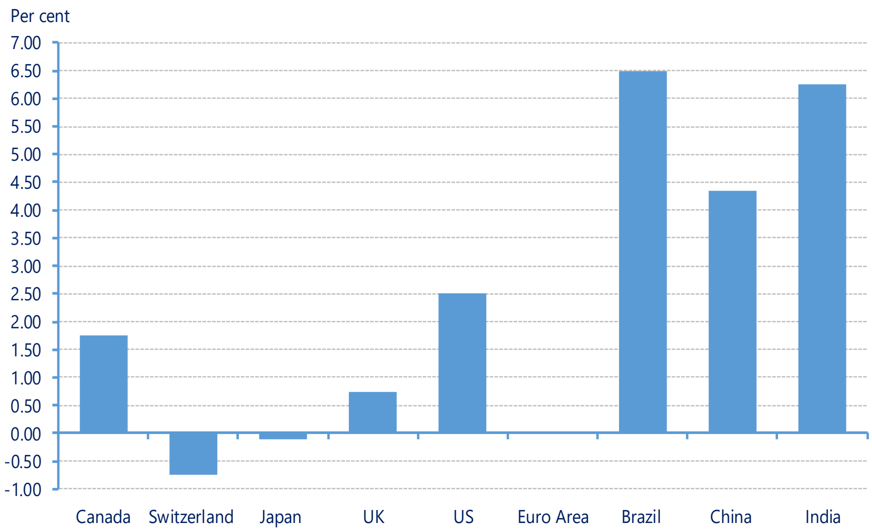
Source: Reuters.

[4] *Average 1-22 February 2019.*

2.6 Monetary Policy Stances

While the US Fed had embarked on a monetary policy tightening agenda, other major central banks remained more cautious. After hiking its benchmark federal funds rate by 25 basis points from 1.75-2.00 per cent to 2.00-2.25 per cent at its September 2018 Federal Open Market Committee (FOMC) meeting, the US Fed left the policy rate unchanged at its November 2018 meeting. Amid improved economic activity, lower unemployment and strong consumer spending, the US Fed raised the target rate to 2.25-2.50 per cent at its December 2018 FOMC meeting (Chart 2.6). However, the US Fed indicated a pause in its interest rate cycle lately. As announced, the ECB ended its asset purchase programme of €15 billion in December 2018, despite growing concerns over risks to the Eurozone economic outlook. The ECB was expected to keep its policy rate unchanged as long as required, until the inflation rate would converge to the target of below, but close to 2 per cent. The BoE left its Bank Rate unchanged at 0.75 per cent, while the asset purchase target was maintained at £435 billion. The BoE judged its monetary policy stance appropriate to achieve the 2 per cent inflation target while fostering growth and employment. Agreement over the Brexit outcome would weigh on the future course of the BoE's monetary policy stance.

Chart 2.6: Policy Rate as at 22 February 2019



Source: Central banks' websites.

Meanwhile, a number of emerging economies also raised their policy rates in a bid to address stubborn increases in inflation linked to higher fuel costs and to ward off a currency crisis. Indonesia's central bank increased its main interest rate twice to 5.75 per cent in September 2018 and to 6.00 per cent in December 2018 to support its currency. Likewise, Russia's central bank also had two rate hikes of 25 basis points each, raising its key policy rate to 7.75 per cent in December 2018, while taking into account that the inflation rate was increasing faster-than-expected. The central banks of Turkey and Philippines tightened monetary policy by 625 basis points and 25 basis points, respectively, to tame persistent increases in inflation and to avert a currency crisis.

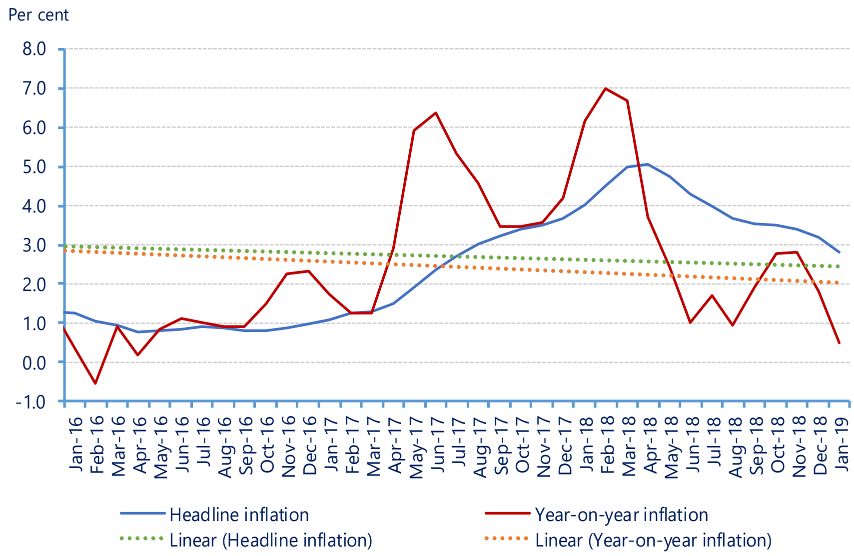
3. Recent Domestic Economic Developments

Headline inflation in Mauritius trended down and remained low, characterised by subdued domestic price pressures in most of the CPI components. The underlying inflationary measures, as reflected in the Bank's CORE1 and CORE2 measures of inflation, were also contained at low levels. Real economic activity in Mauritius continued to expand, driven by the services sectors to a significant extent. The unemployment rate declined to a 17-year low of 6.9 per cent in 2018, from 7.1 per cent in 2017. A wider deficit on the goods account increased the current account deficit in 2018, which was fully funded by higher net inflows on the capital and financial account. Gross official international reserves climbed to USD6.5 billion at the end of January 2019, thereby ensuring a cover of about 10.7 months of imports of goods and services. Public sector external debt declined from 12.5 per cent of GDP as at end-December 2017 to 11.2 per cent of GDP as at end-December 2018.

3.1 Inflation

Benefitting from favourable base effects and the impact of the reduction in domestic petroleum prices in January 2019, the CPI rose at a slower pace, thereby resulting in a lower inflation outturn. Headline inflation dropped to 2.8 per cent in January 2019, from 3.2 per cent in December 2018. The y-o-y inflation rate stood at 0.5 per cent in January 2019, the lowest rate attained since May 2016 (Chart 3.1). The CPI rose by 1.4 index points, from 102.4 in December 2018 to 103.8 in January 2019, reflecting the increase in prices of vegetables (+0.6 index point), followed by other goods and services (+0.7 index point) and other food products (+0.4 index point), which more than offset the decrease of 0.2 index point in gasoline prices and 0.1 index point in air tickets. The momentum of price changes, as indicated by the 3-month moving average (seasonally adjusted) inflation, was contained, while the uptick in price pressures as suggested by sequential inflation was moderate (Charts 3.2 and 3.3).

Chart 3.1: Headline and Year-on-year Inflation



Source: Statistics Mauritius.

Chart 3.2: 3-Month Moving Average (Seasonally Adjusted) Inflation

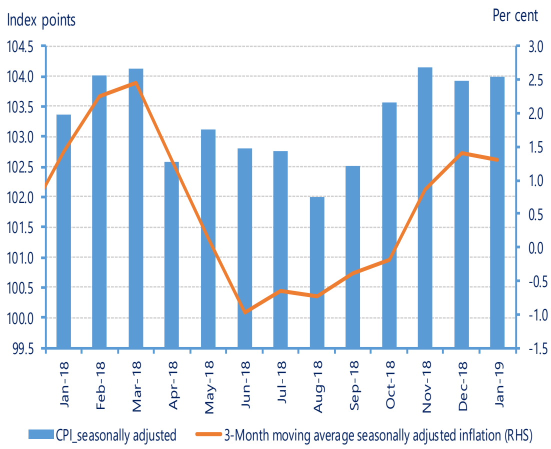
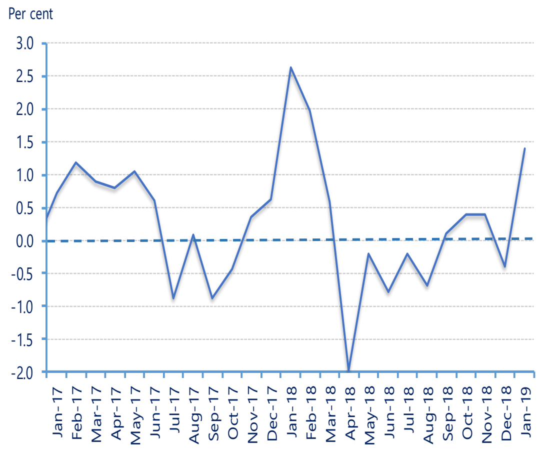


Chart 3.3: Sequential Inflation



Source: Bank of Mauritius calculations.

Drilling down into the main divisions of the CPI basket, 'Food and non-alcoholic beverages' and 'Transport' accounted for over half of headline inflation in January 2019 (Table 3.1). The 'Food and non-alcoholic beverages' division contributed 1.2 percentage points to headline inflation on account of gyrations in the prices of vegetables, while 'Transport' division contributed 0.7 percentage point on the back of the lingering effects of the net increase in the prices of petroleum products under the Petroleum Pricing Committee (PPC). 'Transport' and 'Clothing and footwear' contributed positively to the slight increase in the y-o-y inflation.

Table 3.1: Weighted Contribution to Y-o-y and Headline Inflation: January 2019

DIVISION	Weights	Consumer Price Index		CPI-Average		Contribution to Inflation	
		Jan-18	Jan-19	12-Mth Average to Jan-18	12-Mth Average To Jan-19	Y-o-y Inflation *(Percentage point)*	Headline Inflation *(Percentage point)*
Food and non-alcoholic beverages	248	106.8	105.6	101.0	105.7	-0.3	1.2
Alcoholic beverages and tobacco	110	104.6	105.0	100.8	104.2	0.0	0.4
Clothing and footwear	46	100.9	104.5	100.2	101.9	0.2	0.1
Housing, water, electricity, gas and other fuels	112	99.0	98.2	99.9	98.1	-0.1	-0.2
Furnishings, household equipment and routine household maintenance	59	102.1	103.0	100.3	102.2	0.1	0.1
Health	38	102.9	105.2	100.3	103.3	0.1	0.1
Transport	147	102.6	105.4	100.5	105.1	0.4	0.7
Communication	44	99.9	99.5	100.0	99.5	0.0	0.0
Recreation and culture	42	101.0	101.1	100.1	100.9	0.0	0.0
Education	50	102.8	105.5	100.3	103.9	0.1	0.2
Restaurants and hotels	54	100.9	105.5	100.2	102.5	0.1	0.1
Miscellaneous goods and services	50	100.2	102.7	100.0	101.8	0.0	0.1
Consumer Inflation	**1,000**	**103.3**	**103.8**	**100.5**	**103.3**	**0.5**	**2.8**

Figures may not add up to totals due to rounding.
Sources: Statistics Mauritius and Bank of Mauritius calculations.

Core inflation measures remained low and broadly contained below 3 per cent. Y-o-y CORE1 inflation fell from 2.1 per cent in December 2018 to 1.8 per cent in January 2019, while y-o-y CORE2 inflation rose from 2.1 per cent to 2.7 per cent. On a 12-month average period, CORE1 inflation remained unchanged at 2.3 per cent between December 2018 and January 2019 and CORE2 inflation inched up from 1.8 per cent to 1.9 per cent.

The majority of other inflation measures also depicted inherent stability and subdued price pressures (Tables 3.2 and 3.3). Y-o-y food price inflation waned from 4.0 per cent in September 2018 to -1.3 per cent in January 2019, mainly reflecting a downward pull of favourable base effects. On a 12-month average period, food price inflation fell from 5.7 per cent in September 2018 to 4.8 per cent in January 2019. Y-o-y goods inflation receded from 2.3 per cent in September 2018 to zero per cent in January 2019, while services inflation rose from 1.2 per cent to 2.1 per cent. On a 12-month average period, goods inflation declined from 4.7 per cent to 3.4 per cent, while services inflation inched up from 1.3 per cent to 1.5 per cent.

Excluding mortgage interest from the CPI basket, both y-o-y CPIX_M inflation and 12-month average period CPIX_M inflation fell to 0.7 per cent and 3.1 per cent in January 2019, respectively. Y-o-y imported inflation declined from 1.2 per cent to 0.8 per cent between September 2018 and January 2019 and on a 12-month average period, imported inflation also receded from 3.6 per cent to 2.3 per cent.

Table 3.2: Y-o-y Inflation Indicators

Per cent

	CPI inflation	Food price inflation	CPI excl. mortgage payments inflation	Imported inflation	Goods inflation	Services inflation	CORE1 inflation	CORE2 inflation	CPI Inflation excl. vegetables
Dec-17	4.2	5.6	4.6	5.3	5.6	1.6	2.9	2.2	3.6
Jan-18	6.2	12.7	6.4	5.2	8.3	1.6	2.9	1.8	3.6
Feb-18	7.0	16.7	7.3	4.4	9.5	1.8	2.7	1.8	3.2
Mar-18	6.7	16.2	7.0	3.4	9.0	1.8	2.1	1.6	2.7
Apr-18	3.7	6.9	4.2	3.4	5.2	1.3	2.2	1.5	2.5
May-18	2.4	2.0	2.9	3.9	3.5	0.7	2.2	1.3	2.7
Jun-18	1.0	-1.8	1.4	3.4	1.4	0.5	2.6	1.6	2.2
Jul-18	1.7	0.8	2.0	2.5	2.0	1.3	2.5	1.9	2.1
Aug-18	0.9	0.8	1.3	1.0	1.1	0.8	1.8	1.4	1.1
Sep-18	1.9	4.0	2.2	1.2	2.3	1.2	2.1	1.8	1.3
Oct-18	2.8	6.4	2.9	1.2	3.1	2.3	2.3	2.1	1.7
Nov-18	2.8	5.4	3.0	1.5	3.0	2.5	2.6	2.5	2.0
Dec-18	1.8	2.4	1.9	1.0	1.6	2.2	2.1	2.1	1.7
Jan-19	0.5	-1.3	0.7	0.8	0.0	2.1	1.8	2.7	1.7

Note: excl. - excluding.

Table 3.3: 12-Month Average Inflation Indicators

Per cent

	Headline inflation	Food price inflation	CPI excl. mortgage payments inflation	Imported inflation	Goods inflation	Services inflation	CORE1 inflation	CORE2 inflation	CPI Inflation excl. vegetables
Dec-17	3.7	3.6	3.9	4.2	4.4	2.2	2.2	2.2	3.4
Jan-18	4.0	4.6	4.2	4.5	4.9	2.2	2.4	2.2	3.5
Feb-18	4.5	6.2	4.7	4.6	5.7	2.2	2.5	2.2	3.6
Mar-18	5.0	8.0	5.2	4.6	6.3	2.2	2.5	2.2	3.6
Apr-18	5.0	8.4	5.3	4.6	6.5	2.1	2.6	2.1	3.5
May-18	4.7	7.6	5.0	4.6	6.2	1.9	2.5	2.0	3.4
Jun-18	4.3	6.4	4.6	4.4	5.6	1.7	2.6	1.9	3.2
Jul-18	4.0	5.9	4.3	4.2	5.2	1.6	2.6	1.9	3.1
Aug-18	3.7	5.5	4.0	3.9	4.8	1.5	2.5	1.8	2.8
Sep-18	3.5	5.7	3.9	3.6	4.7	1.3	2.5	1.8	2.6
Oct-18	3.5	6.0	3.8	3.3	4.6	1.4	2.4	1.8	2.5
Nov-18	3.4	6.2	3.7	3.0	4.5	1.4	2.4	1.8	2.4
Dec-18	3.2	6.0	3.5	2.6	4.1	1.5	2.3	1.8	2.2
Jan-19	2.8	4.8	3.1	2.3	3.4	1.5	2.3	1.9	2.1

Note: excl. - excluding.

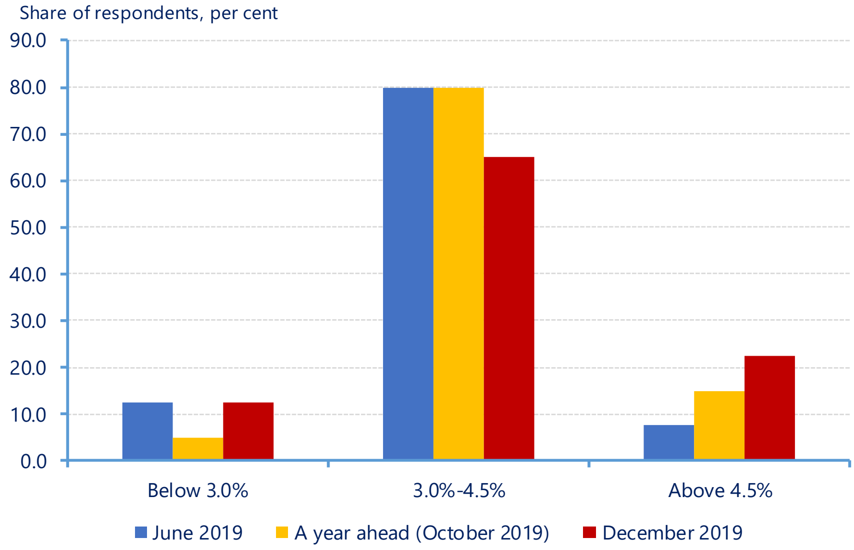
Inflation expectations (headline) assessed in the November 2018 Bank's Survey remained skewed to the downside and were consistent with the reigning low inflation (Table 3.4). Inflation expectations for the mean inflation rates outturn expected by respondents in the survey month of November 2018 were 3.7 per cent for June 2019; 3.9 per cent a year ahead (i.e. October 2019) and 4.0 per cent for December 2019. For the horizon period ended December 2019, 65 per cent of respondents were anticipating an inflation rate ranging between 3.0 per cent and 4.5 per cent (Chart 3.4).

Table 3.4: Inflation Expectations

Per cent

Expectations		1-year ahead	Jun-19	Dec-19
Survey Period	**Aug-18**	4.4	4.3	n.a
	Nov-18	3.9	3.7	4.0

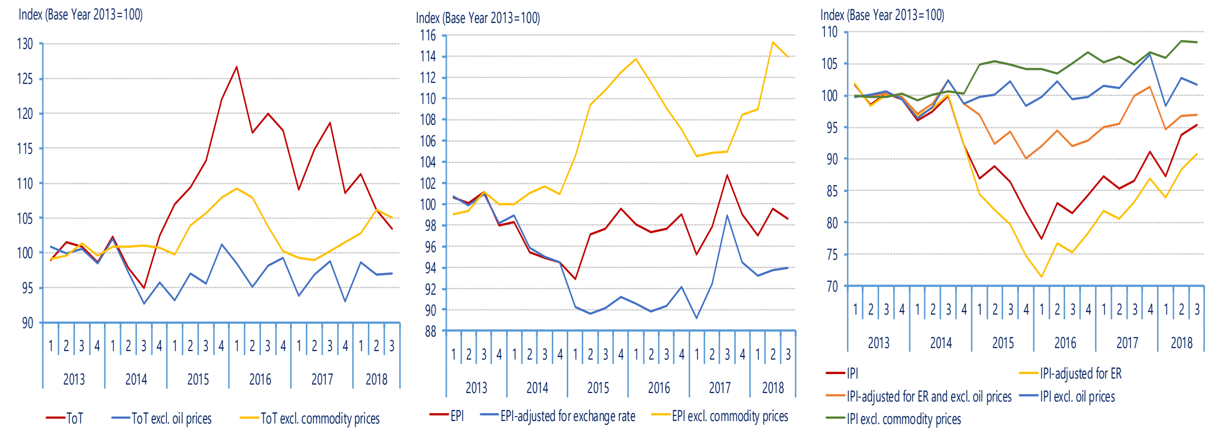
Chart 3.4: Sample Respondents' Expectations of Headline Inflation – November 2018 Survey



Producer Price Inflation-Manufacturing (PPI-M) and Producer Price Inflation-Agriculture (PPI-A) increased somewhat in 2018Q3. Y-o-y PPI-A inflation rate rose from -12.9 per cent in June 2018 to 6.7 per cent in September 2018, reflecting increases in the prices of both its main components, namely 'Crop products' and 'Animals and animal products'. Over the 12-month period, PPI-A inflation rate inched up from -2.0 per cent in June 2018 to 0.1 per cent in September 2018 but remained negligible. Y-o-y PPI-M inflation rate rose from 2.9 per cent in June 2018 to 3.5 per cent in September 2018, reflecting higher prices in the manufacture of food products and beverages. Over the 12-month period, PPI-M inflation rate went up from 2.5 per cent to 2.7 per cent.

Higher import prices of '*Mineral fuels, lubricants and related materials*' deteriorated the terms of trade (ToT) in 2018Q3. The ToT was down by 2.7 per cent over the quarter and worsened by 12.9 per cent y-o-y. Excluding import prices of '*Mineral fuels, lubricants and related materials*', the ToT was steady quarter-on-quarter (q-o-q) but weakened by 1.9 per cent y-o-y (Chart 3.5). Reflecting an almost broad-based decline in the prices of its components, the export price index fell by 1.0 per cent q-o-q and 4.0 per cent y-o-y, largely mirroring the significant decline in the export price of sugar (35.8 per cent, y-o-y). Import prices went up by 1.7 per cent q-o-q as a result of increases in the prices of certain high-weight items, notably '*Mineral fuels, lubricants and related materials*' (+6.7 per cent) and '*Manufactured goods classified chiefly by material*' (+2.0 per cent) but partly offsetting the decline in the prices of other items. Y-o-y, import prices rose by 10.3 per cent and were driven essentially by the 47.2 per cent increase in the prices of '*Petroleum, petroleum products and related materials*'. In volume terms, exports fell by 1.7 per cent in 2018Q3 compared to 2017Q3, while imports picked up by 5.6 per cent over the corresponding period.

Chart 3.5: Terms of Trade, Export Price Index (EPI) and Import Price Index (IPI)



Note: ER - exchange rate.
Sources: Statistics Mauritius and Bank of Mauritius calculations.

3.2 GDP by Sector

Real economic activity in Mauritius increased at a marginally slower pace in 2018Q3 compared to the corresponding period of 2017. Real GDP advanced by 3.2 per cent y-o-y in 2018Q3, down from 3.4 per cent in 2018Q2 and 3.3 per cent in 2017Q3. However, on a q-o-q seasonally adjusted basis, real GDP increased by 1.0 per cent in 2018Q3, from 0.3 per cent in 2018Q2. Growth remained supported by key services sectors in the economy, besides the robust contribution from the construction sector (Table 3.5).

The services sectors contributed the most to the GDP growth momentum in 2018Q3. In particular, '*financial and insurance activities*', '*information and communication*' and '*accommodation and food service activities*' grew by 5.0 per cent, 5.3 per cent and 4.0 per cent, respectively, and more or less around trend levels. The '*wholesale and retail trade*' sector also remained strong, supported by household spending, and grew solidly by 3.7 per cent in 2018Q3 compared to 2.6 per cent in 2017Q3. Growth in the '*construction'* sector remained buoyant at 8.5 per cent in 2018Q3. However, the economic growth performance masked the decline of 0.7 per cent in the '*manufacturing*' sector and the contraction of 19.3 per cent in the '*sugar milling'* sub-sector, combined with weaker performance of the '*textile'* sub-sector for the fifth consecutive quarter.

In its December 2018 National Accounts Estimates, Statistics Mauritius (SM) revised down real GDP growth rate for 2018 from 3.9 per cent to 3.8 per cent, mainly on account of lower-than-expected growth performance in sectors such as '*agriculture, forestry and fishing*', '*manufacturing*' and '*financial and insurance activities*' (Table 3.6). In September 2018, SM estimated that the agricultural sector would contract by 0.8 per cent in 2018. However, the poor performance of the sugar sub-sector during the year resulted in a higher contraction of 2.1 per cent for the overall agricultural sector. The '*manufacturing*' sector also registered a lower growth of 0.8 per cent in 2018, reflecting a contraction of 19.3 per cent in '*sugar milling*' and 6.2 per cent in '*textile*' sub-sectors. The financial services sector grew by 5.4 per cent in 2018, marginally down from the earlier estimate of 5.5 per cent. SM projected real GDP growth for 2019 at 4.0 per cent.

Table 3.5: GDP - Sectoral Real Growth Rates (Year-on-year)

Per cent

	2017			2018		
	Q1	Q2	Q3	Q1	Q2	Q3
Primary Sector						
Agriculture forestry & fishing	3.4	-0.6	-0.4	-5.9	-4.3	-0.4
Mining & quarrying	2.7	1.9	0.8	-0.9	2.9	3.0
Secondary Sector						
Manufacturing	0.3	2.2	1.6	1.3	0.4	-0.7
Electricity, gas, steam & AC	4.9	3.8	2.4	5.2	4.4	2.1
Water supply	1.9	-0.7	2.1	5.1	4.4	2.0
Construction	5.7	8.9	8.7	9.6	9.8	8.5
Tertiary Sector						
Wholesale & retail trade	3.3	2.9	2.6	3.9	3.4	3.7
Transportation & storage	4.1	3.6	3.3	3.9	3.5	3.3
Accommodation & food service activities	3.4	9.2	4.3	4.9	1.5	4.0
Information and communication	5.6	5.6	5.3	5.8	5.6	5.3
Financial & insurance	5.3	5.9	5.3	5.7	5.5	5.0
Real estate	3.4	2.9	3.6	3.7	3.5	2.7
Professional, scientific & technical activities	5.7	5.3	5.1	4.8	5.2	5.2
Administrative & support service activities	5.9	5.9	5.7	5.6	5.7	6.0
Public administration	1.7	1.8	-1.4	-1.9	3.8	2.1
Education	2.5	1.2	1.6	2.2	2.3	2.1
Health	4.1	6.4	5.0	4.1	3.7	3.3
Art, entertainment & recreation	5.5	4.7	4.0	4.8	5.0	4.9
Other service activities	3.5	2.9	3.4	4.0	3.1	3.6
GDP at basic prices	**3.6**	**4.0**	**3.3**	**3.7**	**3.4**	**3.2**
Taxes on products (net of subsidies)	4.1	6.7	4.4	7.3	5.3	4.0
GDP at market prices	**3.7**	**4.4**	**3.5**	**4.2**	**3.6**	**3.3**

Source: Statistics Mauritius.

Table 3.6: GDP - Sectoral Real Growth Rates (Annual)

	September 2018 Issue	December 2018 Issue	Changes
	(1)	(2)	(2) - (1)
	Per cent	Per cent	Percentage Point
Primary Sector			
Agriculture forestry & fishing	-0.8	-2.1	-1.3
Mining & quarrying	1.5	1.8	0.3
Secondary Sector			
Manufacturing	0.9	0.8	-0.1
Electricity, gas, steam & AC	3.4	3.4	0.0
Water supply	3.7	3.7	0.0
Construction	9.5	9.5	0.0
Tertiary Sector			
Wholesale & retail trade	3.8	3.8	0.0
Transportation & storage	3.5	3.5	0.0
Accommodation & food service activities	3.6	3.7	0.1
Information & communication	5.6	5.6	0.0
Financial & insurance	5.5	5.4	-0.1
Real estate	3.6	3.3	-0.3
Professional, scientific & technical activities	5.1	5.1	0.0
Administrative & support service activities	5.8	5.7	-0.1
Public administration	1.7	1.4	-0.3
Education	2.6	2.4	-0.2
Health	4.5	3.8	-0.7
Arts, entertainment & recreation	5.1	5.1	0.0
Other service activities	3.5	3.5	0.0
GDP at basic prices	**3.7**	**3.6**	**-0.1**
Taxes on products (net of subsidies)	5.1	5.1	0.0
GDP at market prices	**3.9**	**3.8**	**-0.1**

Sources: Statistics Mauritius and BoM staff estimates.

The index of industrial production provides an indication of activity of industry in the economy. The overall index remained almost constant in 2018Q3 at 104.2 compared to 104.3 in 2017Q3, notwithstanding diverging performance by some key players in the industrial sector. The Export Oriented Enterprises (EOE) sector and sugar milling output fell by 10.6 per cent and 19.3 per cent, respectively. This was mainly offset by the increase of 5.4 per cent in the production by the non-EOE sector.

3.3 GDP by Expenditure

On the expenditure side, the domestic growth momentum in 2018Q3 was underpinned by robust consumption expenditure and sustained recovery in Gross Fixed Capital Formation (GFCF); whereas the performance of net external demand continued to be a drag (Table 3.7). Growth in final consumption spending largely benefited from the dynamism in household consumption spending which complemented the slowdown in government consumption. Final consumption expenditure expanded by 3.2 per cent in 2018Q3, compared to 3.9 per cent in the previous quarter. Growth in household consumption spending remained solid, up from 3.3 per cent in 2018Q2 to 3.4 per cent in 2018Q3. Broadly stable employment conditions and the implementation of measures supportive of households' purchasing power contributed to the resilience in households' consumption spending. In contrast, growth in general government consumption spending decelerated to 2.2 per cent in 2018Q3, from a solid growth of 6.9 per cent in 2018Q2.

Investment spending pursued its recovery, bolstered by the remarkable upturn in spending in 'machinery and equipment'. Growth in GFCF strengthened from 5.9 per cent in 2018Q2 to an impressive 12.9 per cent in 2018Q3, after contracting by 0.2 per cent in 2018Q1. Capital spending on '*building and construction work*' was sustained, growing by 10.3 per cent in 2018Q3 compared to 10.1 per cent in 2018Q2. Within the category, growth was driven by the strong expansion of 65.6 per cent in spending on '*other construction work*', but was partly dented by investment in '*residential building*' and '*non-residential building*', which contracted by 4.3 per cent and 9.5 per cent, respectively. Concurrently, investment in '*machinery and equipment*' rebounded from two consecutive periods of contraction to post an impressive growth of 17.8 per cent in 2018Q3. This was mainly attributed to increased investment in '*passenger car*' and '*other machinery and equipment*', which grew by 7.9 per cent and 28.9 per cent, respectively. Investment spending drew support from the buoyancy in investment, encompassing renovation and construction of hotels and new projects in the real estate sector, while public sector investment gained traction due to the large-scale infrastructural projects.

Net external demand remained the drag on domestic growth. Exports of goods and services contracted for the fifth consecutive quarter in 2018Q3, albeit its pace of contraction was lower at 1.2 per cent in 2018Q3 compared to 2.3 per cent in 2018Q2. Interestingly, exports of goods improved by 4.4 per cent, while exports of services contracted by 5.7 per cent. Amid a perceptible improvement in domestic demand, imports of goods and services increased by 7.6 per cent in 2018Q3, recovering from a contraction of 4.4 per cent in 2018Q2. The rise in imports was mainly attributed to a robust expansion in imports of goods to 15.2 per cent, which dampened the contraction of 12.2 per cent in imports of services.

Table 3.7: GDP - Domestic and External Demand (Annual growth rates)

Per cent

	2016				2017[1]				2018		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1[1]	Q2[1]	Q3[2]
I. Domestic Demand											
Final consumption	**2.6**	**3.2**	**2.7**	**3.2**	**3.4**	**3.0**	**2.7**	**2.8**	**3.5**	**3.9**	**3.2**
Households	2.6	2.8	2.9	3.4	3.4	3.2	3.1	3.2	3.4	3.3	3.4
General Government	2.4	5.1	1.5	2.3	3.3	2.1	0.5	0.4	3.7	6.9	2.2
GFCF	**3.5**	**-2.3**	**9.8**	**3.8**	**0.1**	**8.1**	**6.4**	**3.8**	**-0.2**	**5.9**	**12.9**
Building & construction work	-3.8	-6.3	9.3	6.4	5.7	7.9	7.8	5.8	8.7	10.1	10.3
Machinery & equipment	16.1	4.7	10.7	-1.0	-8.1	8.2	4.2	0.5	-14.1	-0.4	17.8
II. Net External Demand											
Exports of Goods & Services	**-2.4**	**-8.7**	**-4.4**	**1.2**	**-0.5**	**1.9**	**-3.3**	**-2.1**	**-5.5**	**-2.3**	**-1.2**
Exports (goods)	-11.4	-14.4	-11.0	-4.6	-2.6	-5.2	-7.7	-5.1	-12.2	-4.0	4.4
Exports (services)	5.8	-2.8	2.2	6.0	1.0	8.3	0.5	0.1	-0.4	-0.9	-5.7
Imports of Goods & Services	**10.5**	**0.7**	**3.7**	**-2.7**	**-6.3**	**6.4**	**-0.7**	**10.7**	**-10.0**	**-4.4**	**7.6**
Imports (goods)	13.2	1.5	3.9	-1.5	-8.0	4.5	-1.9	13.2	-13.4	-3.9	15.2
Imports (services)	3.6	-1.7	3.0	-6.1	-1.5	12.2	2.6	3.1	-1.1	-5.7	-12.2
III. GDP at market prices	**4.0**	**3.8**	**3.5**	**4.1**	**3.7**	**4.4**	**3.5**	**3.8**	**4.1**	**3.7**	**3.7**

[1] *Revised estimates.* [2] *First estimates.*

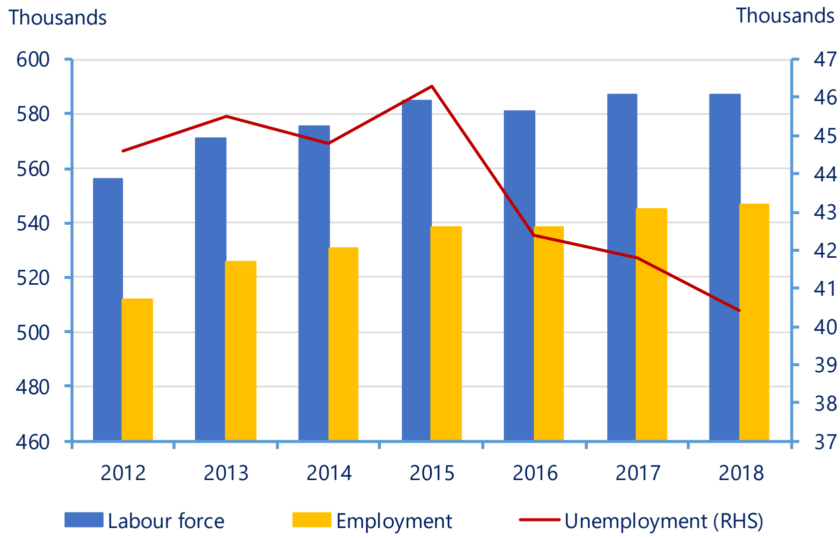
Source: Statistics Mauritius.

3.4 Labour Market and Unit Labour Costs

Labour market conditions improved somewhat in 2018, with the rate of unemployment falling further. The unemployment rate maintained its downtrend from 7.0 per cent in 2017Q3 to 6.9 per cent in 2018Q3. Employment dropped by 5,600 and was accompanied by a contraction in the labour force of 6,400 compared to 2017Q3, which brought down the number of unemployed by 800. On an annual basis, the unemployment rate declined to a 17-year low of 6.9 per cent in 2018, from 7.1 per cent in 2017 (Chart 3.6). The gradual decline in the unemployment rate was associated with improved labour market outcomes on the supply side of the economy, with active labour market policies targeting specific segments of the unemployed. In parallel, increased activity due to large public infrastructural upgrading as well as public sector recruitment have contributed to lowering the unemployment rate in 2018.

Wage developments continued to bolster the purchasing power of employees and to sustain growth in disposable income and support household consumption. The wage rate index (WRI) rose by 4.1 per cent in 2018Q3 compared to 2017Q3, thanks to higher private sector wages. Per sector, the rise in the WRI was due to an increase in wages in sectors such as wholesale and retail trade, transport, information and communication, financial services, professional services and administrative services, which recorded an increase in wages of about 5 per cent or more. Wages in the manufacturing sector increased by 10.1 per cent compared to 2017Q3. Given the pick-up in inflation and the slowdown in nominal wage growth since 2017, real wages have risen by around 1 per cent between 2017 and 2018.

Chart 3.6: Labour Market Indicators

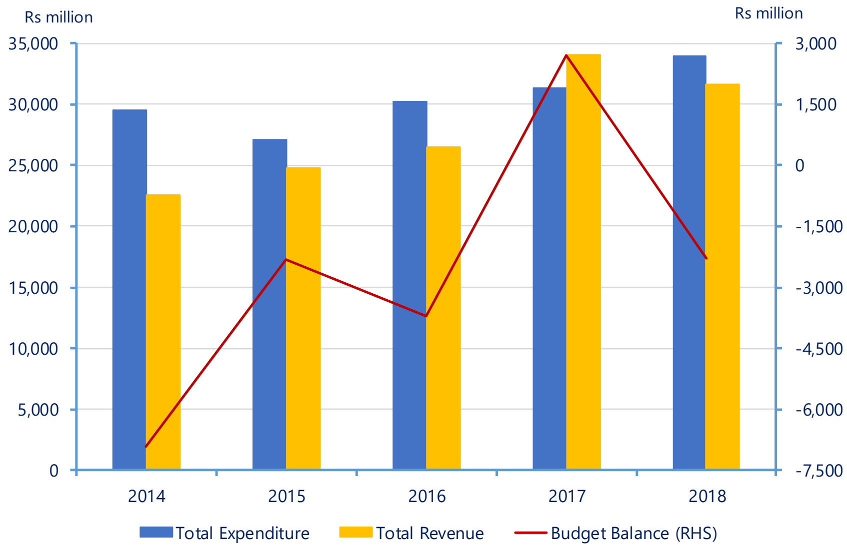


Source: Statistics Mauritius.

3.5 Fiscal Developments

Higher implementation of capital projects and lower external grants received deteriorated the budget balance from a surplus of 2.2 per cent of GDP in 2017Q4 to a deficit of 1.7 per cent of GDP in 2018Q4. External grants during 2018Q4 amounted to Rs0.8 billion compared to Rs5.0 billion in 2017Q4. Consequently, total revenue dropped from Rs34 billion in 2017Q4 to almost Rs32 billion in 2018Q4. However, tax revenue rose by 7.9 per cent, from Rs27 billion in 2017Q4 to Rs29 billion in 2018Q4. Total expenditure increased from Rs31 billion to Rs34 billion over the same period. Capital projects amounted to Rs2.0 billion in 2018Q4 compared to Rs1.6 billion in 2017Q4. The budget deficit was financed solely from domestic sources in 2018Q4 (Chart 3.7 and Table 3.8).

Chart 3.7: Revenue, Expenditure and Budget Balance, 2014Q4 to 2018Q4



Source: Statistics Mauritius.

Table 3.8: Statement of Government Operations

Rs million

	2015Q4 (Actual)	2016Q4 (Actual)	2017Q4 (Actual)	2018Q4 (Provisional)
1. Revenue	**24,797**	**26,519**	**34,093**	**31,673**
Taxes on income, profits & capital gains	5,357	6,436	7,379	8,342
Taxes on goods & services	13,105	14,101	16,417	17,381
2. Expense	**27,104**	**30,221**	**31,391**	**33,967**
Compensation of employees	7,027	7,919	8,118	8,526
Social benefits	*7,256*	*7,958*	*8,386*	*9,166*
of which: Acquisition of non-financial assets	*1,343*	*1,665*	*1,652*	*1,919*
3. Budget Balance	**-2,307**	**-3,701**	**2,702**	**-2,294**
Budget balance as a share of GDP	*-2.1*	*-3.1*	*2.2*	*-1.7*
Primary Balance	***162***	***-1,073***	***5,565***	***874***
Financing				
Domestic	2,427	3,102	-4,804	4,997
Foreign	174	90	178	(369)

Source: Statistics Mauritius.

3.6 Public Sector Debt

The rise in public sector debt as a ratio to GDP reflected the increase in domestic debt. Public sector debt rose from 63.4 per cent of GDP as at end-December 2017 to 64.5 per cent as at end-December 2018. Central Government domestic debt as a share to GDP rose from 47 per cent as at end-December 2017 to 48 per cent as at end-December 2018, mostly reflecting additional issuance of long-term domestic debt, which bodes well in the light of a lengthening of the debt's maturity profile. Notwithstanding the increase in the overall public sector debt, public sector external debt declined from 12.5 per cent of GDP as at end-December 2017 to 11.2 per cent of GDP as at end-December 2018. Central government external debt fell to 8.5 per cent of GDP, a ratio last recorded in September 2010, and following from the peak of 14.1 per cent of GDP in March 2015 (Table 3.9).

3.7 Monetary Aggregates

Broad money liabilities (BML) remained somewhat expansionary, backed by its major components, including growth in rupee time deposits. Y-o-y, BML rose by 6.3 per cent in December 2018, higher than the 4.4 per cent recorded in September 2018. Of the components of BML, currency outside depository corporations, that is, currency with public, declined by 1.8 per cent y-o-y in December 2018, which could reflect the reduced usage of the highest denomination of banknotes by the public (Table 3.10). There was a sharp rise of 11.8 per cent in time deposits in December 2018. The growth in BML in December 2018 reflected a marked increase in foreign currency deposits of 11.4 per cent y-o-y as against a contraction of 1.1 per cent in September 2018, in addition to the rise of 2.4 per cent in rupee deposits. The velocity of circulation of broad money was unchanged at around 0.9 in December 2018.

The growth in Net Foreign Assets (NFAs) of depository corporations slowed to 0.7 per cent y-o-y in December 2018, from 1.4 per cent in September 2018. This was largely attributed to a major decline of growth in the NFAs of the Bank of Mauritius, from 18.3 per cent in September 2018 to 8.5 per cent in December 2018. The NFAs of other depository corporations (ODCs) declined, albeit less pronounced, from -6.8 per cent y-o-y in September 2018 to -3.6 per cent in December 2018.

Y-o-y, the growth in depository corporations' claims on other sectors (excluding financial derivatives) stood at 5.4 per cent in December 2018, higher compared to an increase of 5.1 per cent in September 2018. Between end-September 2018 and end-December 2018, claims on other sectors (excluding financial derivatives) rose by Rs5.4 billion, or by 1.2 per cent to Rs459.4 billion. Net claims on central government rose noticeably by 8.1 per cent y-o-y in December 2018, accelerating from 4.9 per cent in September 2018.

The monetary base contracted by 1.3 per cent y-o-y in December 2018, after growing by 16.1 per cent in September 2018. This reflected a fall in currency with public by 1.8 per cent and lower deposits of ODCs of 3.0 per cent y-o-y held with the Bank of Mauritius. The broad money multiplier remained broadly stable at 5.5 in December 2018.

Table 3.9: Public Sector Debt

Rs million

	Dec-16	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18
1. Budgetary Central Government Domestic Debt	**205,197**	**215,336**	**217,587**	**223,719**	**232,486**	**234,258**
- Short Term	*23,907*	*25,273*	*25,060*	*25,856*	*27,938*	*26,283*
- Medium Term	*52,769*	*49,899*	*54,899*	*54,393*	*55,362*	*56,791*
- Long Term	*119,432*	*137,746*	*138,318*	*144,640*	*150,525*	*153,194*
Government securities issued for mopping up excess liquidity	*10,172*	*3,727*	*1,021*	*894*	*894*	*894*
Consolidation adjustment (iro Govt Securities held by non-financial public corporations)	*-1,083*	*-1,309*	*-1,711*	*-2,064*	*-2,233*	*-2,904*
As percentage to GDP	***47.2***	***47.1***	***47.0***	***47.5***	***48.8***	***48.3***
Budgetary Central Government Domestic Debt excluding Government securities issued for mopping up excess liquidity	195,025	211,609	216,566	222,825	231,592	233,364
As percentage to GDP	***44.9***	***46.3***	***46.7***	***47.3***	***48.6***	***48.1***
2. Budgetary Central Government External Debt	**51,637**	**45,128**	**44,544**	**44,538**	**42,078**	**41,414**
- Short Term	*32*	*28*	*29*	*14*	*12*	*17*
- Medium & Long Term	*46,933*	*40,495*	*39,838*	*39,823*	*37,422*	*36,786*
- Long term debt liability - IMF SDR Allocations	*4,672*	*4,605*	*4,677*	*4,701*	*4,644*	*4,611*
As percentage to GDP	***11.9***	***9.9***	***9.6***	***9.5***	***8.8***	***8.5***
3. Budgetary Central Government Total Debt	**256,834**	**261,773**	**263,842**	**270,321**	**276,797**	**276,797**
As percentage to GDP	***59.1***	***57.2***	***56.9***	***57.4***	***58.1***	***57.0***
4. Public Enterprises Total Debt	**21,980**	**29,574**	**29,458**	**29,751**	**30,387**	**37,193**
Public Enterprises Debt as percentage to GDP	***5.1***	***6.5***	***6.4***	***6.3***	***6.4***	***7.7***
Public Sector Domestic Debt	214,816	232,754	235,375	240,758	250,022	258,629
Public Sector Domestic Debt as percentage to GDP	*49.4%*	*50.9%*	*50.8%*	*51.1%*	*52.5%*	*53.3%*
Public Sector External Debt	64,124	57,386	56,317	57,342	55,020	54,327
Public Sector External Debt as percentage to GDP	*14.7%*	*12.5%*	*12.2%*	*12.2%*	*11.5%*	*11.2%*
5. Public Sector Debt	**278,940**	**290,140**	**291,691**	**298,100**	**305,042**	**312,956**
As percentage to GDP	**64.2**	**63.4**	**62.9**	**63.3**	**64.0**	**64.5**
Public Sector Debt excluding government securities issued for mopping up excess liquidity	268,768	286,413	290,670	297,206	304,148	312,062
As percentage to GDP	**61.8**	**62.6**	**62.7**	**63.1**	**63.8**	**64.3**

Source: Ministry of Finance and Economic Development.

Table 3.10: Components and Sources of Broad Money Liabilities[1]

Rs million

Components of Broad Money Liabilities [2]	Dec-14	Dec-15	Dec-16	Dec-17	Dec-18
I. Currency with Public	**25,391**	**27,638**	**29,731**	**32,218**	**31,636**
II. Deposit Liabilities	**368,807**	**405,833**	**442,364**	**482,668**	**501,478**
II.I. Rupee Deposits	315,928	340,382	370,422	402,595	412,277
II.2. Foreign Currency Deposits	52,879	65,451	71,943	80,072	89,201
III. Debt Securities	**3,358**	**4,528**	**5,693**	**7,197**	**21,900**
BROAD MONEY LIABILITIES (I+II+III)	**397,557**	**437,999**	**477,789**	**522,083**	**555,014**
Sources of Broad Money Liabilities	Dec-14	Dec-15	Dec-16	Dec-17	Dec-18
I. Net Foreign Assets	**457,823**	**529,026**	**549,151**	**566,913**	**570,677**
Bank of Mauritius	122,735	151,519	177,669	200,039	217,004
Other Depository Corporations	335,088	377,506	371,482	366,873	353,672
1. Net Claims on Central Government	***44,771***	***41,980***	***54,205***	***69,678***	***75,333***
Bank of Mauritius	(20,743)	(28,635)	(38,387)	(24,932)	(19,273)
Other Depository Corporations	65,515	70,615	92,592	94,611	94,606
2. Claims on Other Sectors [3]	***402,035***	***434,672***	***439,052***	***504,900***	***460,262***
Bank of Mauritius	152	3,669	3,786	3,843	3,927
Other Depository Corporations	401,882	431,004	435,266	501,057	456,335
2.1 Claims on other sectors, excluding financial derivatives	*377,116*	*408,360*	*408,210*	*435,641*	*454,883*
II. Domestic Claims (1+2)	**446,806**	**476,653**	**493,258**	**574,578**	**535,595**
III. Net Non-Monetary Liabilities	**507,073**	**567,680**	**564,619**	**619,408**	**551,258**
BROAD MONEY LIABILITES (I+II-III)	**397,557**	**437,999**	**477,789**	**522,083**	**555,014**

Figures may not add up to totals due to rounding.

[1] *Based on the methodology of the IMF's Depository Corporations Survey framework.*

[2] *Effective October 2018, the Bank discontinued the dissemination of narrow money liabilities and quasi-money liabilities. Instead, the components of Broad Money Liabilities will comprise Currency with public, Deposit liabilities and Debt securities (formerly known as Securities other than Shares).*

[3] *Effective May 2018, Financial Derivatives are recorded at market or fair values and are not strictly comparable with prior months' data.*

3.8 Credit Developments

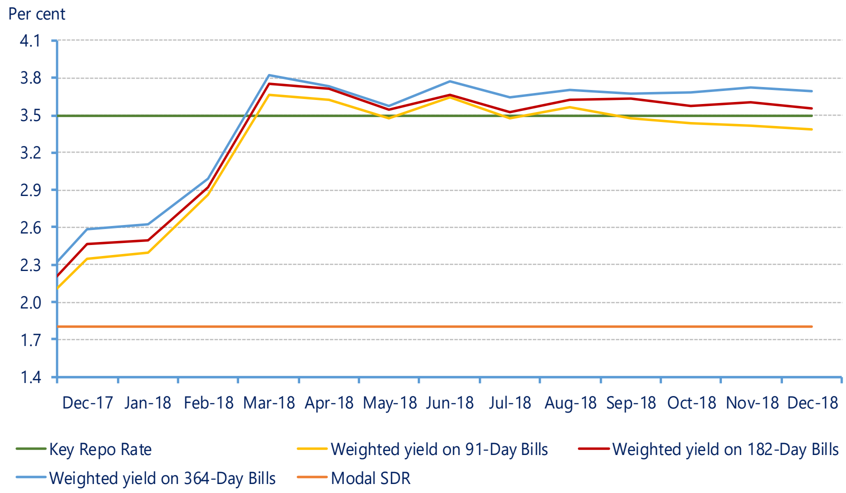
With effect from October 2018, the Bank introduced a new format for the collection and compilation of statistics on bank credit to the private sector. The new table provides details on loans (including overdrafts and finance leases) disbursed by banks to Other Nonfinancial Corporations (ONFCs), households and other sectors. Loans to ONFCs are classified as per the United Nations International Standard Industrial Classification of All Economic Activities ('ISIC') while credit granted to households are classified as per the purpose of the loans. Accordingly, data prior to October 2018 would not be strictly comparable to historical data due to this reclassification of credit granted by banks.

Bank loans to ONFCs, households and other sectors (excluding GBCs) fell from Rs301 billion in October 2018 to Rs298 billion in December 2018. This reflected a decline of loans in several sectors of the economy, of which the most noteworthy were the agricultural sector (Rs3.0 billion) and construction, real estate, and wholesale and retail trade sectors (around Rs1 billion each). Loans to households for housing purposes also declined by Rs1.1 billion over the same period. This was associated with a 'carve-out' operation, whereby selected portfolios of non-performing loans were transferred away from loan books.

3.9 Interest Rates

Given that the Key Repo Rate (KRR) has remained unchanged since September 2017, banks' Savings deposit (SDR) and Prime lending rates have also remained unchanged in the range of 1.35-2.10 per cent and 5.65-8.50 per cent, respectively, as at end-December 2018. The modal savings rate and the modal prime lending rate were also unchanged at 1.80 per cent and 6.25 per cent, respectively. The weighted average interest rate on rupee deposits was at 1.72 per cent in December 2018, almost unchanged compared to September 2018. Similarly, the weighted average rupee lending rate was 6.21 per cent. As a result, the spread between the rupee weighted lending and weighted deposit rates, a key determinant of profitability in the banking sector, narrowed marginally from 4.51 per cent to 4.49 per cent over the period September to December 2018 (Chart 3.8).

Chart 3.8: KRR, SDR and Weighted Average Yields on 91-Day, 182-Day and 364-Day Bills



3.10 Exchange Rate Developments

The rupee exchange rate has been fairly stable, reflecting broad movements of major currencies in international markets, in addition to domestic demand and supply conditions (Chart 3.9). Foreign capital inflows reflected somewhat domestic economic fundamentals and macroeconomic stability. Low and stable inflation in 2018 as well as the build-up of foreign exchange reserves contributed to enhancing macroeconomic stability. Between 9 November 2018 and 22 February 2019, on a weighted average dealt selling rate basis, the rupee appreciated by 0.4 per cent and 0.1 per cent against the euro and the Pound sterling, respectively, and was rather flat against the US dollar. 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 marginally by 0.1 per cent in November and 0.8 per cent in December. Since the November 2018 MPC meeting, the Bank intervened on four occasions on the domestic foreign exchange market; purchasing US$15.0 million each in November and December 2018, US$10.0 million in January 2019 and US$30.0 million in February 2019 (Chart 3.10).

Chart 3.9: Evolution of the Rupee against the US Dollar

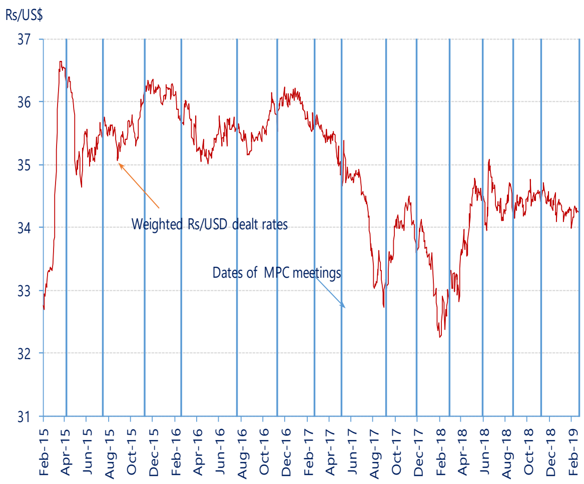
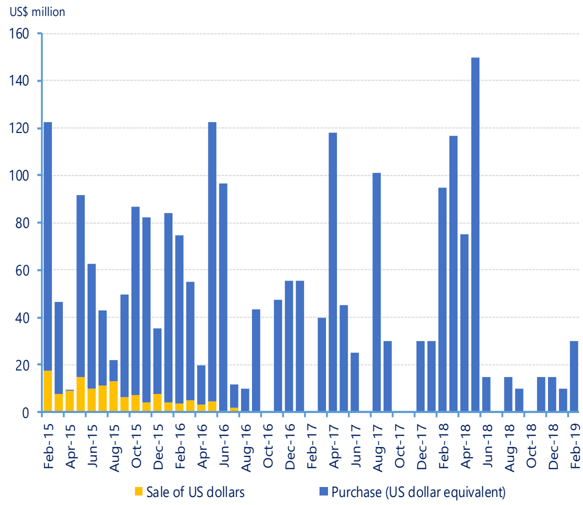


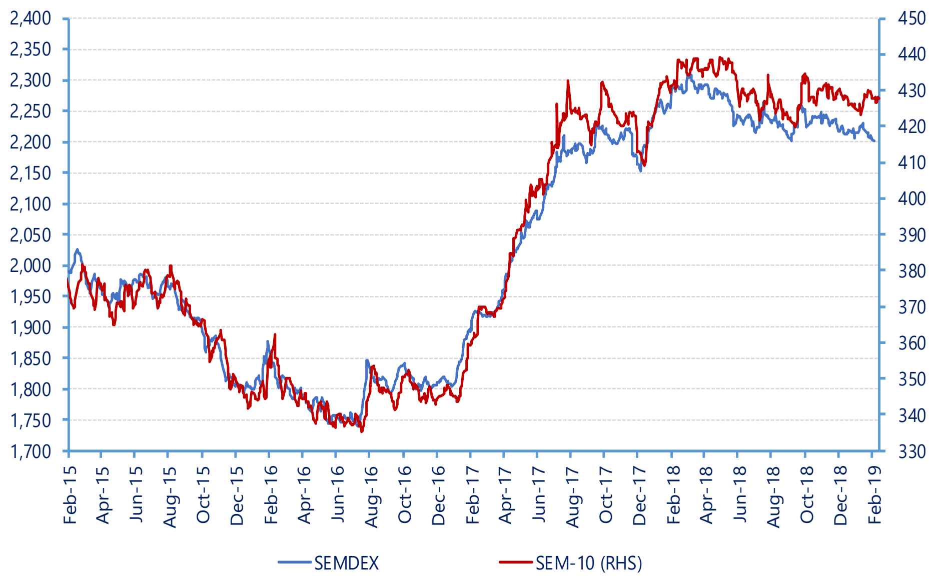
Chart 3.10: Intervention on the Domestic Foreign Exchange Market



3.11 Stock Market Developments

The domestic stock market was subject to some bouts of volatility during 2018H2 as investors seemed to have remained cautious. On a point-to-point basis, the SEMDEX fell by 1.8 per cent between 9 November 2018 and 22 February 2019 and the SEM-10, which comprises the ten most capitalised stocks on the Official Market, declined by 0.6 per cent (Chart 3.11). The decrease in the SEMDEX was driven mainly by lower prices of stocks of operators in the distributive trade and sugar-linked sectors. Notwithstanding net sales by non-residents, their holdings increased from Rs50.5 billion in January 2018 to Rs57.6 billion in January 2019, or by 14.1 per cent, presumably reflecting valuation changes.

Chart 3.11: Evolution of SEMDEX and SEM-10

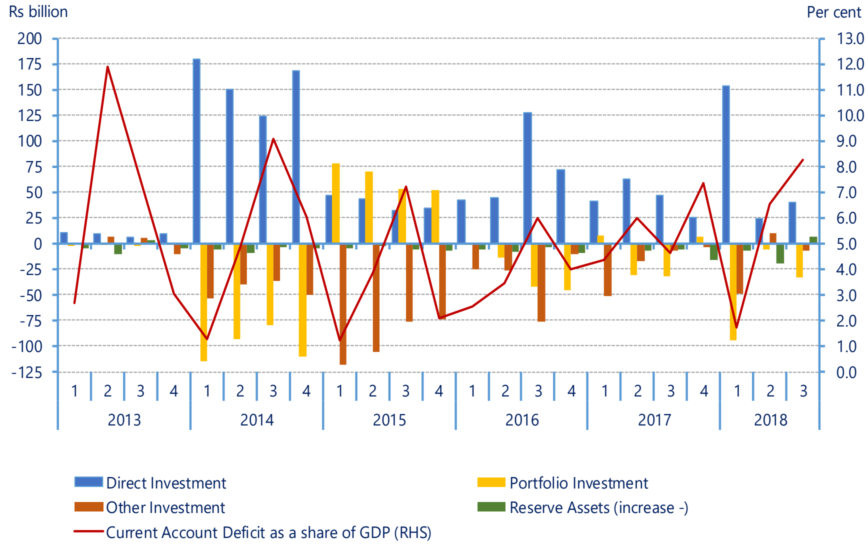


3.12 Balance of Payments and Gross Official International Reserves

Preliminary estimates of balance of payments have pointed to a worsening of the current account deficit in 2018Q3. The deterioration of the current account deficit was primarily caused by a higher deficit on the goods account, which was mitigated by surpluses on both the services and primary income accounts. The current account deficit was estimated to have widened from Rs5.2 billion in 2017Q3 to Rs9.8 billion in 2018Q3, or from 4.6 per cent of GDP to 8.3 per cent of GDP (Chart 3.12). The deficit on the goods account widened from Rs20 billion in 2017Q3 to Rs27 billion in 2018Q3. Notwithstanding the impact of lower exports of goods, imports picked up in the wake of a surge in the prices of petroleum products, coupled with higher value of imported goods intended for infrastructural investments. Net inflows on the capital and financial account (inclusive of reserve assets) were estimated to have risen from Rs1.9 billion in 2017Q3 to Rs7.2 billion in 2018Q3. An overall balance of payments deficit of Rs6.9 billion was recorded in 2018Q3, to a large extent due to the decline in banks' foreign currency balances held with the Bank of Mauritius as against a surplus of Rs5.9 billion in 2017Q3.

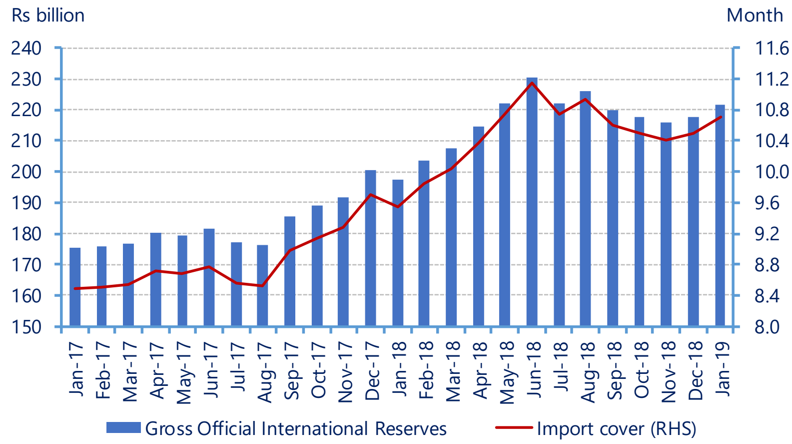
The widening deficit on the goods account was projected to increase the current account deficit in both 2018 and 2019, which would remain fully funded from higher net inflows on the capital and financial account. As a percentage to GDP, the current account deficit is estimated to increase from 5.9 per cent in 2018 to 6.1 per cent (excluding the purchase of aircraft) in 2019. The improved performance on both the services and current transfers accounts would partly contain the goods account deficit. The capital and financial account, inclusive of reserve assets, was estimated to record higher net inflows of Rs37 billion in 2019 compared to Rs31 billion in 2018.

Chart 3.12: Financing of the Current Account Deficit



The gross official international reserves (GOIR) of the country remained on an uptrend, consolidating the buffer against external shocks. The GOIR increased by Rs4 billion, from Rs218 billion as at end-October 2018 to Rs222 billion as at end-January 2019. Compared to a year ago, GOIR rose by nearly Rs25 billion. In US dollar terms, the GOIR increased from USD6,312.5 million as at end-October 2018 to USD6,501.9 million as at end-January 2019. Based on the value of imports of goods (f.o.b.) and services for the calendar year 2017, GOIR of the country represented 10.7 months of imports as at end-January 2019 compared to 10.5 months as at end-October 2018 and 9.5 months as at end-January 2018 (Chart 3.13).

Chart 3.13: Gross Official International Reserves



Diminishing gross external debt and rising gross official international reserves have been beneficial to mitigate external vulnerabilities. The major reserve adequacy metrics have improved as at end-December 2018 (Table 3.11). Gross external debt of the country declined from Rs77.7 billion as at end-December 2017, representing 17.0 per cent of GDP, to Rs73.8 billion as at end-December 2018, equivalent to 15.2 per cent of GDP. The ratio of gross external debt to exports of goods and services increased to 43.4 per cent, while the level of gross official international reserves as at end-December 2018 were nearly three times the level of gross external debt.

Table 3.11: External Debt Indicators

		Dec-15	Dec-16	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18
		Rs million						
Gross External Debt [1]	*as at end*	89,112	85,274	77,678	75,256	76,622	74,370	73,823
External Debt Service [1]	*year ended*	7,699	9,588	12,586	8,806	8,616	8,685	8,147
Exports of Goods	*year ended*	93,290	84,456	81,317	79,730	79,620	62,248	64,099
Exports of Goods and Services	*year ended*	190,271	184,915	186,406	187,059	187,240	168,992	170,067
Imports of Goods and Services	*year ended*	230,282	229,581	248,037	245,632	248,702	197,349	197,628
Gross Official International Reserves [2]	*as at end*	152,902	178,858	200,368	207,516	230,496	219,899	217,585
GDP at market prices	*year ended*	409,892	434,765	457,464	463,382	470,951	476,598	485,191
Broad Money Liabilities	*as at end*	437,999	477,789	522,083	529,215	537,638	537,076	555,014
I. Solvency *(Per cent)*		**Dec-15**	**Dec-16**	**Dec-17**	**Mar-18**	**Jun-18**	**Sep-18**	**Dec-18**
Gross External Debt/GDP [3]		21.7	19.6	17.0	16.2	16.3	15.6	15.2
Gross External Debt/Exports of Goods		95.5	101.0	95.5	94.4	96.2	119.5	115.2
Gross External Debt/Exports of Goods and Services		46.8	46.1	41.7	40.2	40.9	44.0	43.4
External Debt Service/Exports of Goods		8.3	11.4	15.5	11.0	10.8	14.0	12.7
External Debt Service/Exports of Goods and Services		4.0	5.2	6.8	4.7	4.6	5.1	4.8
II. Reserve Adequacy *(Per cent)*		**Dec-15**	**Dec-16**	**Dec-17**	**Mar-18**	**Jun-18**	**Sep-18**	**Dec-18**
Reserves/Imports of Goods and Services		66.4	77.9	80.8	84.5	92.7	111.4	110.1
Reserves/Broad Money Liabilities		34.9	37.4	38.4	39.2	42.9	40.9	39.2
Reserves/Gross External Debt		171.6	209.7	257.9	275.7	300.8	295.7	294.7

[1] Gross external debt outstanding as at end of period excludes global business companies' and other deposit taking institutions' debts.

[2] Gross Official International Reserves as at end of period comprise gross foreign assets of the Bank of Mauritius, reserve position in the IMF and the foreign assets of Government.

[3] GDP figures for 2013 onwards are based on SNA 2008.

Note: Exports and Imports data for year ending March 2018 are preliminary projections.

Sources: MoFED, Statistics Mauritius and Bank of Mauritius.

4. Monetary Policy Decisions and Implementation

The Monetary Policy Committee of the Bank of Mauritius unanimously voted to keep the KRR unchanged at 3.50 per cent both at its November 2018 and February 2019 MPC meetings. Excess liquidity in the banking system has been contained at tolerable levels thanks to the Bank's active open market operations through the issue of its own securities and sterilisation of proceeds following interventions on the domestic foreign exchange market. In addition, the 91-Day Treasury Bill rate has remained well within the interest rate corridor of the Bank's operational framework for monetary policy.

4.1 Monetary Policy Decisions

In November 2018, the MPC assessed the global economic environment to be challenging and that the outlook was fraught with uncertainties. These uncertainties ranged from trade frictions to the outcome with regard to the modalities of the exit of UK from the European Union and geopolitical tensions. The MPC noted that the IMF had downgraded global growth projections for 2018 and 2019 in its World Economic Outlook released in October 2018. Oil prices on international markets had generally been volatile and quite elevated, at the time of the meeting.

On the domestic front, the MPC viewed economic activity to be commendable in an environment of subdued inflationary pressures. Cost-push pressures arising from adverse weather conditions that contributed to volatile inflation during 2018H1 had dissipated. The MPC viewed the outlook of the domestic economy to remain quite upbeat, taking into account that the economy continued to operate with some spare capacity. The MPC noted that short-term interest rates remained close to the KRR following the implementation of appropriate measures by the Bank which remained committed to undertake open market operations, as required, to achieve the desired monetary policy stance. The MPC unanimously decided to maintain the KRR at 3.50 per cent per annum as the prevailing stance of monetary policy would continue to support economic growth, while maintaining price stability.

At its February 2019 MPC meeting, the MPC noted that data released pointed to a slowdown in global economic activity in 2018H2 while global growth forecasts for 2019 were revised further down by major multilateral organisations. Risks to the global growth outlook included, among others, the US-China trade disputes, uncertainties relating to Brexit and geopolitical tensions. Global inflation was broadly contained and inflationary pressures were expected to remain benign amid relatively low commodity prices and weakening global growth. Oil prices reversed course amid prospects of weak demand and oversupply.

The domestic economy continued to be resilient in the face of an increasingly challenging external environment. Broadly, inflationary pressures remained contained and the muted inflationary environment mainly reflected the absence of supply shocks. While the deficit in the current account increased due to a deterioration of the goods account, it was financed by financial flows without any undue pressure on the rupee. Rupee balances held by banks in excess of the cash reserve ratio requirements were kept in check amid the Bank's active involvement in the domestic money market. Open market operations as carried out by the Bank helped short-term money market interest rates to remain within the corridor of the KRR. Considering the monetary policy stance as conducive to economic growth and price stability, the MPC decided unanimously to maintain the KRR at 3.50 per cent per annum.

4.2. Monetary Policy Implementation

On average, the level of rupee excess reserves increased somewhat, but masked the amount that banks voluntarily keep as precautionary reserves. Since the November 2018 MPC meeting up to 22 February 2019, the rupee liquidity in excess of cash ratio requirements averaged of Rs12.0 billion, as compared to an average of Rs11.0 billion for period 21 August to 9 November 2018. This increase in excess liquidity was mainly driven by net government expenditure, that was partly financed by sale of foreign exchange from their account maintained with the Bank and the scaling down of issuances by Government during December 2018, with the amount of Treasury Notes scheduled for issuance in December 2018 at Rs1.0 billion, and not issuing Treasury Bills.

The Bank issued more of its instruments than were maturing and proceeded with sterilised foreign exchange intervention with a view to containing the build-up of excess liquidity. During the period under review, the Bank issued a total amount of Rs23.9 billion of Bank of Mauritius securities as against maturing BoM instruments of Rs20.3 billion, of which around Rs11 billion was issued in December 2018. The Bank also intervened on the domestic foreign exchange market on four occasions since 09 November 2018 to purchase a total amount of USD70 million. The Bank sterilised the rupee proceeds for a total amount of Rs861 million as one-year deposits.

The short term yields continued to hover near the KRR. The 91-Day yield remained close to the KRR during the period under review, hovering within a range of 3.20 per cent to 3.45 per cent. The average weighted yields for the 91-Day, 182-Day and 364-Day Bills, which stood at 3.46 per cent, 3.65 per cent and 3.76 per cent, respectively, at 9 November 2018, decreased by 18 basis points, 17 basis points and 13 basis points to reach 3.28 per cent, 3.48 per cent and 3.63 per cent, respectively, on 22 February 2019. The overnight interbank interest rate, which stood at 3.26 per cent in November 2018, dropped to an average of 3.18 per cent in December 2018 before picking up slightly to an average of 3.20 per cent in January 2019. Thereafter, the overnight interbank interest rate fell again to 3.00 per cent as at 22 February 2019 (Chart 4.1). The scaling up of open market operations by the Bank led to an increase in the amount of outstanding BoM securities from Rs92 billion as at 9 November 2018 to Rs97 billion as at 22 February 2019 (Table 4.1).

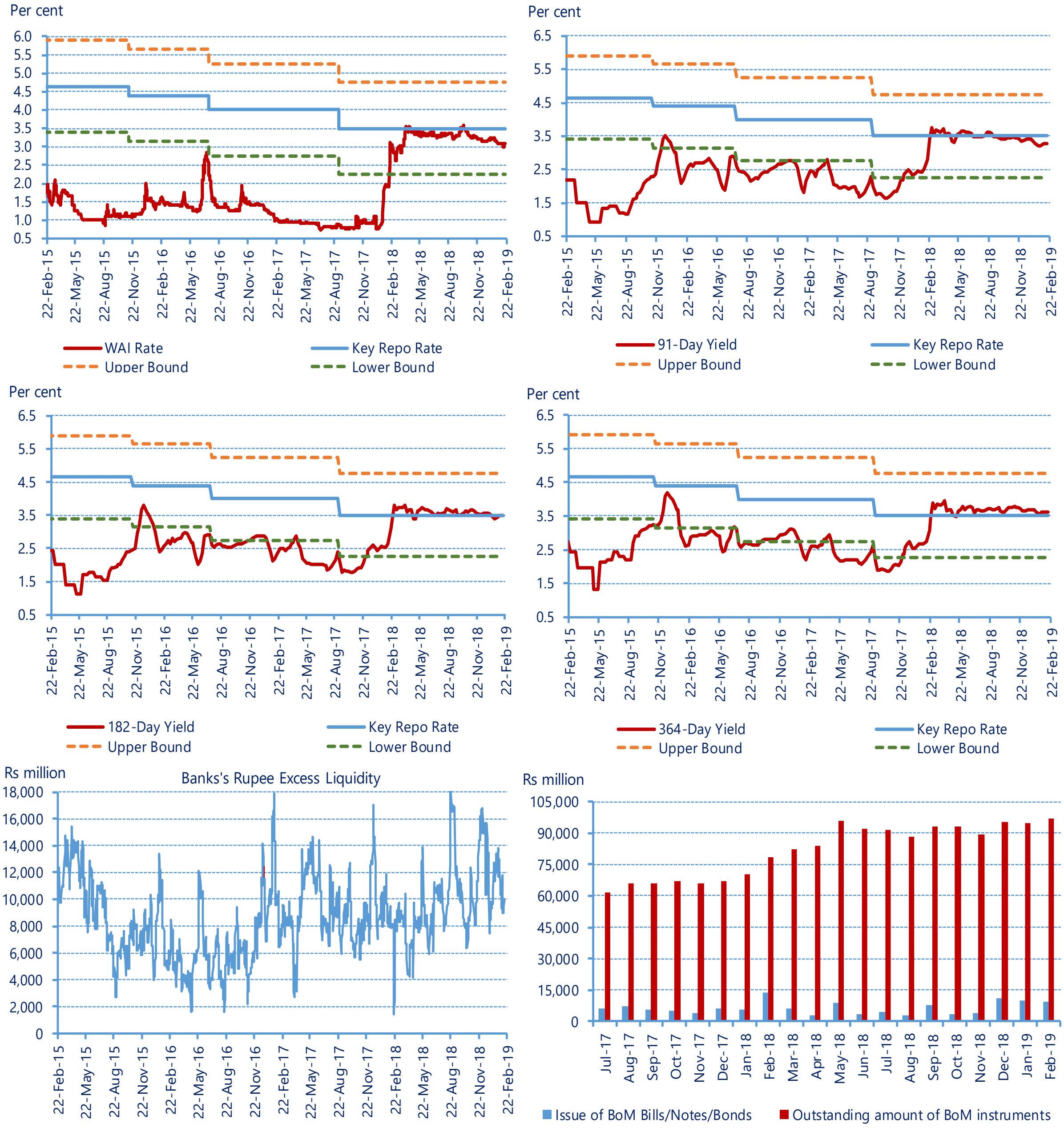
Table 4.1: Outstanding BoM Securities

Rs million

	Amount outstanding as at 20 August 2018	Amount outstanding as at 09 November 2018	Amount outstanding as at 31 January 2019	Amount outstanding as at 15 February 2019	Amount outstanding as at 22 February 2019
Bank of Mauritius Bills	34,442.9	31,643.8	31,214.7	34,047.2	34,813.6
Special Deposits	18,280.6	18,280.6	17,115.1	15,977.6	15,779.0
Bank of Mauritius Notes	27,050.0	33,050.0	37,050.0	37,050.0	37,050.0
3-Year Bank of Mauritius Golden Jubilee Bonds	8,974.4	8,974.4	8,974.4	8,974.4	8,974.4
15-Year Bank of Mauritius Bonds	500.0	500.0	500.0	500.0	500.0
Total	**89,247.9**	**92,448.8**	**94,854.2**	**96,549.2**	**97,117.0**

Figures may not add up to total due to rounding.

Chart 4.1: Excess Liquidity and Money Market Rates



5. DOMESTIC ECONOMIC OUTLOOK

The Bank's forecast of key macroeconomic indicators is based on data available as at end-January 2019 and takes into consideration global economic projections made by various international multilateral agencies, like the IMF, World Bank, OECD and UN as well as recent domestic economic trends and projections. Based on these assumptions, the Bank revised down its forecast for headline inflation to 2.1 per cent for 2019, down from the previous estimate of 3.0 per cent and at around 2.5 per cent for 2020 in the absence of major supply shocks. Economic activity will continue to expand in terms of domestic demand and real GDP growth is forecast to remain resilient at about 3.9 per cent in 2019 and at 4 per cent in 2020.

5.1 Background and Assumptions

Since the beginning of 2019, the outlook for the global economy's growth has deteriorated and trading partner countries' output growth has been projected to be lower than initially anticipated. High frequency indicators, including short-term confidence indicators, have also been pointing towards a loss of momentum in global growth. The Global Manufacturing PMI, a forward-looking index designed to hint at the direction of activity in the manufacturing sector, touched a 29-month low in January 2019. The pace of growth in the new orders sub-index has slowed, suggesting less buoyant future economic activity. Global economic uncertainty remained elevated.

Most international organisations have made substantial downward revisions to their forecasts lately. The major factors pulling down world growth were:

- Slowdown in world trade against the backdrop of increasing trade barriers which, engendered uncertainty, given the interdependence of global production chains;
- Steady rise in interest rates resulting from increased inflation expectations in the US had induced higher volatility in financial markets and brought about rising financing problems for many emerging economies with large current account deficits;
- Slowdown in the euro area arising from a decline in the growth contribution of net exports;
- Slowdown in the growth rate of China; and
- Lingering Brexit negotiations.

Given the softer readings of recent economic indicators which could reveal a slowdown of global economic growth, other central banks have been following the US Fed's more dovish lead:

- Both the ECB and the Bank of Japan have expressed increasing concerns about the downside risks for their economic outlook, thereby hinting that their policy stance would remain accommodative for even longer than previously expected.
- The Reserve Bank of Australia (RBA) lowered its growth and inflation forecasts and the RBA has moved away from a tightening bias to a more symmetric stance.

- The Bank of England lowered its growth forecasts, inferring that the next rate hike might be deferred.
- Emerging market central banks have also turned more dovish, with the Reserve Bank of India surprisingly cutting its policy rate, the Bank of Mexico adopting a neutral stance given lower inflation and weaker growth, and the central banks of Brazil and Russia both lowering their readings on inflation.

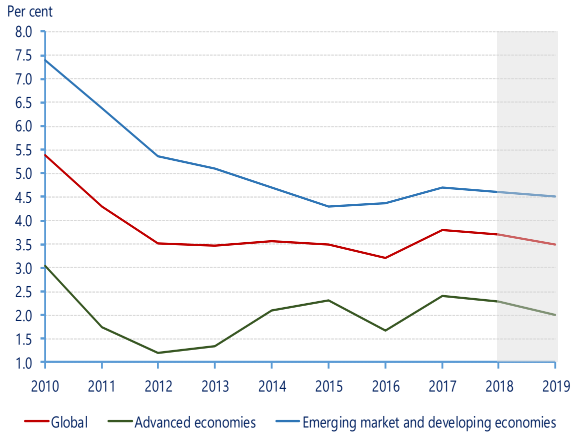
Global growth was estimated to have become more asynchronous and disparate across major economies. Advanced economies' growth rate, which eased from 2.4 per cent in 2017 to 2.3 per cent in 2018, was expected to weaken to 2.0 per cent in 2019 - a downward revision of 0.1 percentage point compared to the October 2018 IMF WEO projections (Chart 5.1). Growth in the US economy was expected to soften to 2.5 per cent in 2019, from 2.9 per cent in 2018, as support to domestic economic activity from the fiscal stimulus was being withdrawn amid monetary policy tightening. A worsening outlook was being predicated for the euro area, with the growth rate dropping to 1.6 per cent in 2019, from 1.8 per cent in 2018. Lower economic activity would emanate from growth downgrades in Germany, Italy and France, reflecting some country-specific headwinds. Real GDP growth in the UK was expected to recover modestly to 1.5 per cent in 2019, from 1.4 per cent in 2018, benefitting from the fiscal stimulus under the 2019 Budget, though conditional on the country striking a Brexit deal.

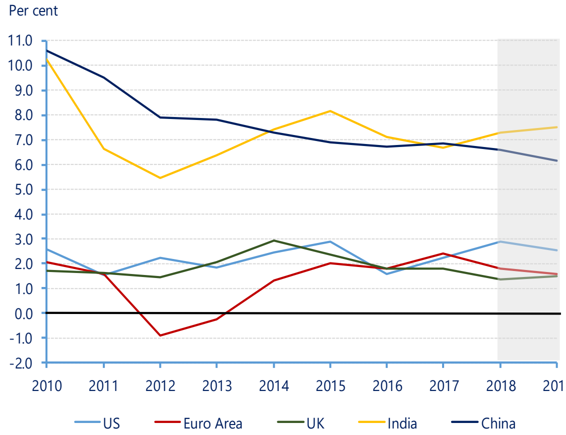
In EMDEs, growth was also anticipated to decelerate in 2019 before picking up in 2020. The block was forecast to grow by 4.5 per cent in 2019, 0.2 percentage point lower compared to the IMF October 2018 WEO forecast, but would recover to 4.9 per cent in 2020. Chinese growth momentum would also soften as domestic activity was being constrained by government policies to regulate the financial sector amid tighter global financing conditions, while the effects of ongoing trade frictions with the US was becoming increasingly entrenched. Considering the impact of recent trade developments on its economic activity, China's GDP growth was projected to moderate further to 6.2 per cent in 2019, from 6.6 per cent in 2018.

Growth estimates for other emerging economies, including Turkey, Argentina, South Africa and Brazil, had also been revised down on account of prevailing financial distress, higher political risks and heightened uncertainties. India, on the other hand, was expected to secure its position as the driver of growth across EMDEs, attaining a robust growth rate of 7.5 per cent in 2019, marginally up from 7.3 per cent in 2018. Massive public sector spending on capital goods and implementation of structural reforms were anticipated to provide an impetus to growth in the Indian economy.

Lingering trade tensions as well as tighter monetary policy in the US and volatile financial markets were expected to continue to weigh on the outlook of world trade. The IMF, in its January 2019 WEO Update, forecast world trade volume to grow by 4.0 per cent in 2019, same as in 2018. Growth in international trade volume was expected to increase from 3.2 per cent in 2018 to 3.5 per cent in 2019 for advanced economies while, it was projected to decline from 5.4 per cent in 2018 to 4.8 per cent in 2019 for EMDEs.

Chart 5.1: Global Growth





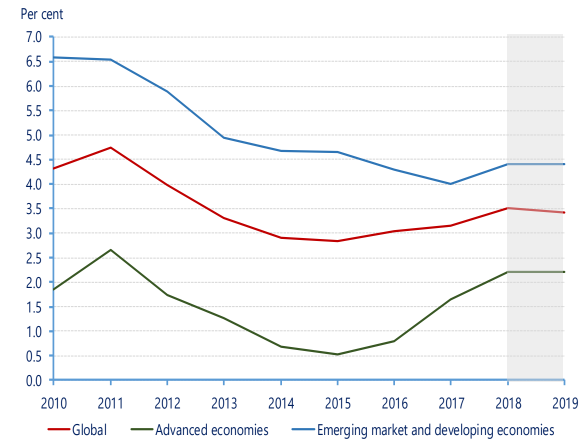
Source: IMF's January 2019 WEO Update.

The US Fed marked a major turnaround in its interest rate tightening cycle while other major advanced economies' central banks remained prudent, keeping their policy rate unchanged. In view of strong labour market conditions and inflation expectations, the US Fed raised the target for the federal funds rate to 2.25-2.50 per cent at its December 2018 FOMC meeting. While the US Fed Chairman stated, in December 2018, that any further increase in interest rates would be undertaken gradually, the tone changed at the FOMC meeting held in January 2019. Notwithstanding robust US growth, global headwinds, softer survey data and tighter financial conditions have put the FOMC under risk management mode. A flat yield curve, together with a policy rate at the lower end of the neutral interest rate, estimated by the US Fed to be in the region 2.5-3.5 per cent, constrained its ability to further tighten monetary policy.

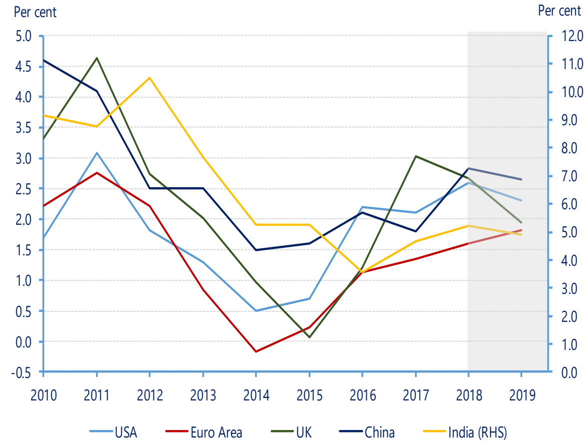
As announced, the ECB proceeded with its decision to end its asset purchase programme at a monthly pace of €15 billion in December 2018 and acknowledged that risks to the Eurozone economy have shifted to the downside. The policy interest rate was expected to be kept on hold, at least until the end of 2019. The BoE maintained the Bank Rate unchanged at 0.75 per cent amid favourable economic developments. However, agreement over a Brexit deal might influence a future hike in the interest rate.

Global inflationary pressures were projected to remain relatively contained, while core inflation would be muted. While inflation in advanced economies has remained generally muted, it has ticked up in the US, reflecting a positive output gap. Declining oil prices have led to lower inflationary impulses in emerging market economies although the pass-through of weakening currencies have, to some extent, outweighed the easing pressure on prices. As per the January 2019 IMF WEO Update, inflation in advanced economies was projected to be lower at 1.7 per cent in 2019, from 2.0 per cent in 2018. This contrasted with the projected increase in inflation in emerging and market economies, from 4.9 per cent in 2018 to 5.1 per cent in 2019 (Chart 5.2).

Chart 5.2: Global Inflation



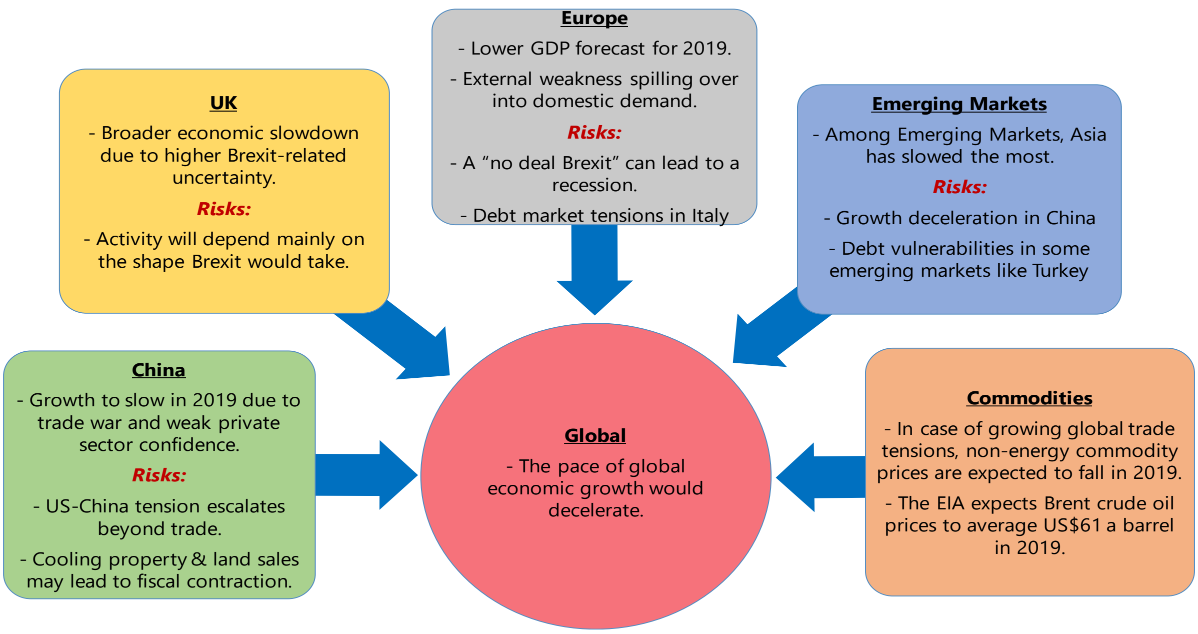
Source: IMF's January 2019 WEO Update.



Source: IMF's October 2018 WEO.

The balance of risks to the global growth forecast was tilted to the downside in a context of elevated economic and political uncertainty. The implementation of protectionist trade measures, growth slowdown in China and uncertainty surrounding Brexit negotiations had dented business sentiment and could jeopardise the trade and investment growth momentum, which would potentially disrupt global supply chains. The trade war between the US and China also added a legion of uncertainty to the global business climate despite the 90-day truce. Higher interest rates in the US and a stronger US dollar would curtail capital inflows to emerging economies and weaken further their currencies, which were already vulnerable due to high debt levels and limited policy space. In the medium term, risks would stem from a potential continued build-up of financial vulnerabilities, subdued global growth outlook, and intensification of the global trade dispute, among others (Chart 5.3).

Chart 5.3: Key Global Risks



Oil Price Developments

On average, oil was expected to trade lower in 2019, as the US would ramp up production against a backdrop of reduced OPEC production and a fall in demand resulting from slowdown in global economic growth. The production gains in the US would stem from increasing pipe capacity along with the national policy to become energy self-sufficient or independent. Commencing in January 2019, OPEC would be curtailing production in order to stabilise oil prices. On the demand side, lower oil prices would also emanate from less oil consumption in line with expectations of curtailed economic growth in the US, Europe, Japan and China. The oil market was still concerned about the oversupply in the future as well as softer-than-expected oil demand due to the deterioration in global economic outlook (Table 5.1).

Demand for OPEC crude in 2019 was forecast at 30.8 mb/d[5], around 0.9 mb/d lower than the 2018 level. Compared to the same quarter in 2018, demand for the first and second quarters was forecast to fall by 1.1 mb/d and 0.6 mb/d, respectively, while demand for the third and fourth quarters was expected to fall by 0.6 mb/d and 1.4 mb/d, respectively. The ICE Brent would average US$61 a barrel in 2019, lower than the average of US$71 in 2018 (Table 5.2). The expected growth slowdown in emerging and developing economies as well as higher production in the US would keep oil prices in check. However, uncertainty would prevail in the aftermath of the planned production cuts by the OPEC, which were expected to end by June 2019. Furthermore, upside pressures could resurface once the US removes the waivers that it had granted to eight countries regarding the Iranian sanctions.

Table 5.1: Supply and Demand for Oil, mb/d

	2018	2019Q1	2019Q2	2019Q3	2019Q4	2019
World oil demand	**98.8**	**99.1**	**99.3**	**100.7**	**101.3**	**100.1**
Non-OPEC supply	*62.1*	*63.3*	*63.1*	*64.3*	*65.8*	*64.2*
OPEC NGLs and non-conventionals	*5.0*	*5.1*	*5.1*	*5.1*	*5.1*	*5.1*
Total non-OPEC supply and OPEC NGLs	**67.0**	**68.4**	**68.2**	**69.4**	**71.0**	**69.3**

Note: 2018 - Estimate 2019 - Forecast Figures may not add up to total due to rounding.
Non-OPEC supply includes Qatar. Source: OPEC.

Table 5.2: Energy Prices

Crude oil (*US dollar per barrel*)	2018				2019				2020				2018	2019	2020
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
West Texas Intermediate Spot Average	62.9	68.1	69.7	59.6	53.1	53.7	55.0	57.3	58.0	58.0	58.0	58.0	65.1	54.8	58.0
Brent Spot Average	66.8	74.5	75.0	68.3	61.1	61.4	60.3	61.3	62.0	62.0	62.0	62.0	71.2	61.0	62.0

Source: US EIA.

[5] *Million barrels per day.*

Assumptions for Domestic Inflation and Real GDP Growth Rates Forecasts

The domestic inflation projection would remain dependent on a set of domestic and global macroeconomic developments including the changes in international food and oil prices. Oil prices have continued to decline throughout November and December 2018 as investors remained concerned about oil market oversupply amid rising trade tensions between China and the US and signs of slower economic growth, which could curb global oil demand in 2019. In late December 2018, the ICE Brent price tumbled to around US$50 per barrel, its lowest point since August 2017 amid low market liquidity. While prices recovered somewhat in January 2019, they might not be back to US$75-US$80 levels in the near future.

At its meeting of 12 January 2019, the PPC in Mauritius reduced petrol prices given falling international crude prices. For generating the forecasts, the baseline projection rested on the PPC keeping the price of petroleum products unchanged. The latter was posited against the current global oil price outlook and EIA's outlook that global oil supply would be roughly in line with demand in 2019. No marked increase in the prices of administered goods and services had also been made, while the rupee exchange rate was posited to be broadly stable. In addition, it was assumed that inflation expectations would continue to remain well-anchored; business and consumer confidence would remain unchanged; household consumption would be sustained at current levels; and no significant supply shock would affect the economy and the production of fresh food products. In particular, any transitory price increases with regard to fresh food products that could arise would be reversed once production returns to normal levels.

Assumptions regarding the external environment have been summarised in Table 5.3.

Table 5.3: Selected Indicators' Projections

Countries	Real GDP growth and inflation forecasts, per cent (Reuters poll)									
	Quarter-on-quarter real GDP growth rate *(Per cent)*					Year-on-year inflation rate *(Per cent)*				
	2018Q4	2019Q1	2019Q2	2019Q3	2019Q4	2019Q1	2019Q2	2019Q3	2019Q4	2020Q1
United States (Y-o-y)	2.6	2.1	2.3	2.1	1.9	1.8	1.9	2.0	2.1	2.3
United Kingdom	0.2	0.3	0.3	0.4	0.4	2.1	2.1	1.9	1.9	2.0
Eurozone	0.3	0.4	0.4	0.4	0.4	1.7	1.5	1.3	1.3	1.5
of which: France	0.2	0.4	0.4	0.5	0.4	1.4	1.3	1.2	1.5	1.7
China (Y-o-y)	6.4	6.3	6.3	6.2	6.2	2.1	2.3	2.2	2.2	2.2
India (Y-o-y)	7.0	6.9	7.0	7.5	7.5	3.1	3.8	4.1	4.5	4.3
South Africa	1.8	1.2	1.5	2.0	2.0	4.8	4.9	5.1	5.2	5.5
Australia	0.7	0.8	0.7	0.7	0.7	1.8	1.9	2.1	2.3	2.3

	Oil price forecasts, US$ per barrel (US Energy Information Administration)				
	2019Q1	2019Q2	2019Q3	2019Q4	2020Q1
NYMEX West Texas Intermediate	50.0	52.0	56.0	58.6	60.0
ICE Brent	58.0	60.0	61.3	62.6	64.0

Sources: Reuters, OECD and US EIA.

5.2 Inflation Forecast in the Baseline Scenario

The current muted inflationary environment in Mauritius was projected to persist in the near-term. The beginning of 2019 was not marked by adverse weather conditions as had been the case in 2018, whereby cyclonic conditions and heavy rainfalls prevailed for an extended period. This led to lower-than-expected outturns in the prices of vegetables. In addition, the contribution of the energy component to CPI growth remained mostly negative during 2018, owing initially to the negative base effects arising from the course of oil prices with that of the same period in the previous year.

Demand-driven inflationary pressures in the economy also remained contained, with the economy still operating with some degree of spare capacity. The rather weak pass-through of exchange rate to domestic prices and some economic slack associated with negative output gap contributed mildly to generating inflationary pressures. Inflationary pressures from the domestic economy would be contained by some anti-inflationary influence of import prices associated with subdued growth in foreign prices and the relative stability of the rupee exchange rate. The combined influence of weak demand-pull and cost-push factors on CPI inflation has resulted in a tame domestic inflationary environment.

Inflation in our major trading partners had remained low and imported inflation was assumed to be low in the near-term given global inflationary developments. Inflation in the US, UK and Eurozone was expected to remain contained in 2019. Global commodity prices were anticipated to remain mild over the medium-term, while relatively lower global oil prices would contribute to a downward bias in inflationary pressures.

In the absence of major supply shocks, headline inflation has been forecast at around 2.1 per cent in 2019, down from the Bank's previous estimate of 3.0 per cent. The downward revision emanated principally from favourable base effects as well as relatively contained cost pressures. Headline inflation was projected at around 2.5 per cent in 2020, conditional on the absence of material exogenous shocks.

5.3 Real GDP Growth Projection in the Baseline Scenario

In 2019, the domestic economy was expected to remain on a steady growth path, supported principally by domestic demand. Sustained private consumption growth and the anticipated acceleration of government consumption and gross fixed capital formation, including a sizeable increase in public investment would continue to back growth. Major projects included the first phase of the metro express, smart cities, Victoria and Immigration bus terminals and other infrastructure works, including the road decongestion programme. Underlying economic factors were also deemed to provide continued support to domestic economic growth, including a lower unemployment rate and appropriate monetary conditions. Household consumption would remain supportive, while the economy would also be stimulated by a positive fiscal impulse. However, net external demand would remain a drag on the domestic growth performance. The trade deficit would remain sizeable, partly due to the underperformance of the exports of goods and imports of goods associated to infrastructure projects. Household disposable income was projected to remain supported through growth in wages and salaries, while social benefits income was deemed to make a commendable contribution.

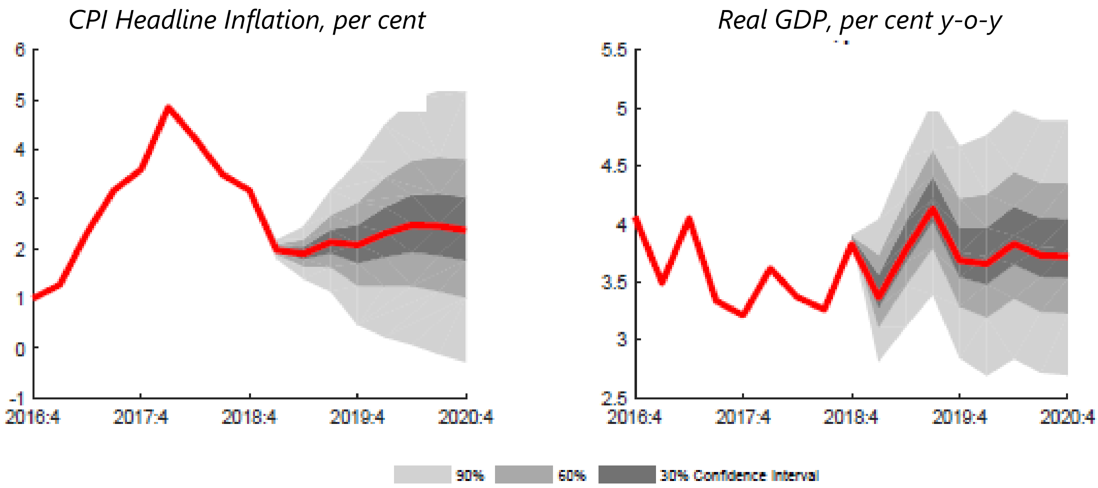
At the sectoral level, the services sector would remain the major engine of growth in 2019. The 'financial and insurance activities' sector was expected to expand by 5.4 per cent, supported by the authorities' initiatives to instil confidence in the sector while promoting its resilience, with the "Financial Sector Blueprint". The *'wholesale and retail trade'* sector was expected to remain sustained, given robust household consumption and improving employment conditions. The *'accommodation and food service activities'* sector was projected to grow by 3.5 per cent in 2019 based on expected tourist arrivals of around 1,450,000. The *'manufacturing'* sector was expected to grow by around 1.7 per cent in 2019. The *'construction'* sector would continue to experience a strong performance, with a growth of 8.5 per cent, supported by new and existing projects. The agricultural sector was expected to grow by 2.3 per cent based on a sugar production of around 320,000 tonnes.

GDP growth was forecast to remain resilient at about 3.9 per cent in 2019 and at 4 per cent in 2020. The slight downgrade in the GDP growth forecast had resulted from the current global uncertainty and the fact that some of our major trading partners revised down their growth outlook, which could dent demand from these economies. At home, the sectoral issues that could weigh on growth performance would include difficulties faced by a couple of textile companies and lower sugar production.

5.4 Balance of Risks

Headwinds to attaining the expected domestic growth rate and inflation rate over the projection horizon still exist and the fan chart depicts the probability of various outcomes for CPI inflation and real GDP growth (Chart 5.4). Over the forecast period, the distribution reflects uncertainty over the evolution of CPI inflation and real GDP growth in the future.

Chart 5.4: Fan Charts - Headline Inflation and Real GDP Growth

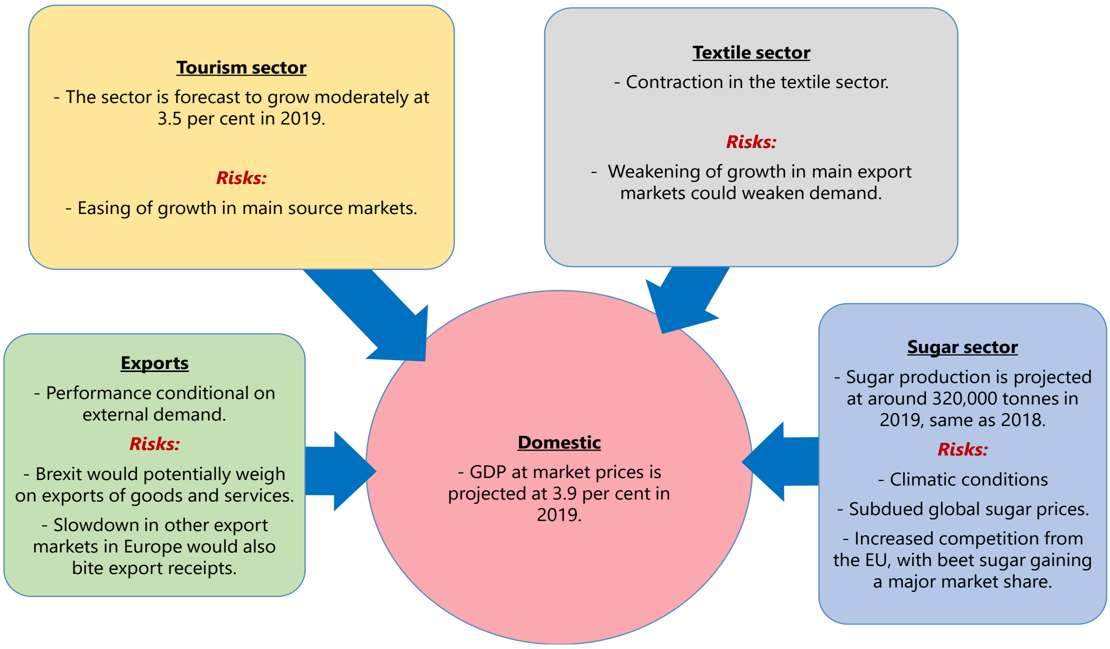


The fan chart is constructed so that the projections are expected to lie within each pair of the lighter coloured areas, i.e., the confidence intervals. In any particular quarter of the forecast period, CPI inflation and real GDP growth are therefore expected to lie somewhere within the fan on 90 out of 100 occasions, i.e., at 90 per cent confidence interval. The uncertainty associated with the forecasts of CPI inflation and real GDP growth is reflected with the widening dispersion from the central estimate as the projection horizon increases.

The risks to the baseline scenario of the projections for GDP growth were somewhat tilted to the downside. On the external front, an escalation in the adoption of protectionist measures, which could affect the buoyancy of trade and of activity at the global level and heightened uncertainty surrounding Brexit along with potential deterioration of the economic situation in some of our major trading partners, especially the Eurozone, could represent a risk for the demand for domestic goods and services. On the domestic front, potential delays in the implementation of infrastructure projects would raise the risk of lower growth of public investment, thus impacting on the domestic growth momentum (Chart 5.5).

As regards inflation, the risks were rather tilted to the downside reflecting favourable base effects notwithstanding the increases in wages faster than productivity gains. The pass-through from foreign prices to domestic prices was projected to remain low and contained, while the economy would continue to operate with a negative output gap.

Chart 5.5: Risks to the Domestic Economy



Unforeseen circumstances may cause the actual forecast to deviate from the forecast generated under the baseline scenario. Should some threats materialise, the trajectories for inflation or real GDP growth would differ from the projections under the baseline scenario. Major occurrences that could generate a different growth path than the one under the baseline scenario were:

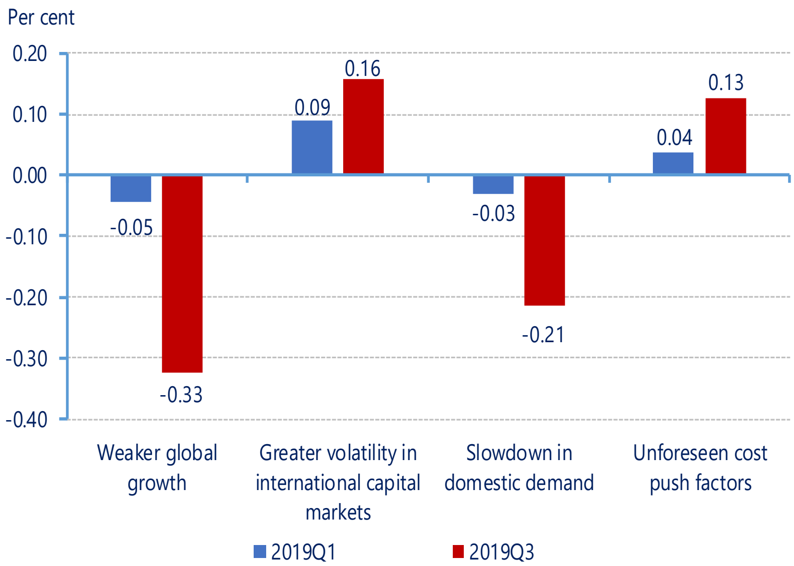
a) Global growth would decelerate as a result of Brexit-related uncertainties, US-China trade friction and weak growth in the Eurozone;
b) Commodity price increases, thus putting upward pressure on the import bill;
c) Business confidence to remain upbeat, boding well for private sector investment and stepping up of public sector investment; and
d) Monetary conditions to remain accommodative, helping to bolster credit growth and supporting the economic momentum.

Factors that could possibly change the projected path of inflation from the baseline scenario include:

a) A slowdown in the global growth momentum;
b) Easing of domestic demand stemming from execution lags of both public and private sector investment projects;
c) Temporary cost-push shocks, including adverse weather conditions; and
d) A change in the monetary policy stance by the US Fed, triggering heightened volatility in international financial markets.

Based on a number of different projections, the balance of risks to the inflation outlook for the year 2019 would seem to be inclined to the downside. Chart 5.6 illustrates how individual risk factors would influence the projection for inflation in 2019. The balance of risk is computed as the difference between the inflation rate forecast under the baseline scenario and the one that would actually be obtained in case explicit shocks, as outlined above, materialise but modified by the probability that these shocks become a reality.

Chart 5.6: Balance of Risks



LIST OF CHARTS

LIST OF TABLES

LIST OF ACRONYMS

BDI	Baltic Dry Index
BML	Broad Money Liabilities
BoE	Bank of England
CPI	Consumer Price Index
ECB	European Central Bank
EMDEs	Emerging Market and Developing Economies
EOE	Export Oriented Enterprises
FAO	Food and Agriculture Organisation
FDI	Foreign Direct Investment
FOMC	Federal Open Market Committee
GBC	Global Business Companies
GFCF	Gross Fixed Capital Formation
GDP	Gross Domestic Product
GOIR	Gross Official International Reserves
GOS	Gross Operating Surplus
IGC	International Grains Council
IMF	International Monetary Fund
ISIC	International Standard Industrial Classification of All Economic Activities
KRR	Key Repo Rate
MERI	Mauritius Exchange Rate Index
MPC	Monetary Policy Committee
MSCI	Morgan Stanley Capital International
NAFTA	North American Free Trade Agreement
NFA	Net Foreign Assets
NYMEX	New York Mercantile Exchange
ODCs	Other Depository Corporations
OECD	Organisation for Economic Co-operation and Development
ONFCs	Other Nonfinancial Corporations
PMIs	Purchasing Managers' Indices
PPC	Petroleum Pricing Committee
PPI-A	Producer Price Inflation-Agriculture
PPI-M	Producer Price Index-Manufacturing
Q-o-q	Quarter-on-quarter
RBA	Reserve Bank of Australia
SEM	Stock Exchange of Mauritius
SM	Statistics Mauritius
SMEs	Small and Medium Enterprises
ToT	Terms of Trade
TCPI	Trading Partner Countries' Consumer Price Inflation
TPG	Trading Partner Countries' Growth
TPPI	Trading Partner Countries' Producer Price Inflation
UN	United Nations
US Fed	US Federal Reserve System
WEO	World Economic Outlook
WESP	World Economic Situation and Prospects
WRI	Wage Rate Index
Y-o-y	Year-on-year

BANK OF MAURITIUS

Address Sir William Newton Street
Port Louis
Mauritius
Website https://www.bom.mu

ISSN 1694-3740