## BANK OF MAURITIUS

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### MONETARY POLICY STATEMENT

The Monetary Policy Committee (MPC) of the Bank of Mauritius decided to maintain the key Repo Rate at 5.75 per cent per annum at its regular meeting held on 22 June 2009. The interest rate chargeable on the Special Deposits Facility, set at 100 basis points below the key Repo Rate, remains at 4.75 per cent per annum while that on the Overnight Facility, set at 150 basis points above the key Repo Rate, is held at 7.25 per cent per annum. The interest rate payable on the Standing Facility, set at 400 basis points above the key Repo Rate, is 9.75 per cent per annum.

The MPC reviewed recent international and domestic economic as well as financial developments and assessed the outlook for the global and domestic economy before reaching its decision.

**International developments and outlook**

The data indicate a more rapid downturn of the global economy in the first quarter of 2009 than initially anticipated. However, since the MPC last met in March 2009, leading indicators suggest some stabilisation of global conditions. Latest data even point to a bottoming out from the global economic recession implying that the worst could be over, although more evidence was required to determine the timing and pace of the recovery. Economic conditions and confidence indicators in many economies - especially in the United States, Canada, France, United Kingdom, China and India - have started showing encouraging signs of improvement. These positive developments result from the unprecedented fiscal stimulus and monetary policy easing implemented in a number of countries accompanied by the support to major financial systems.

While expectations point to better global economic performance as from the second half of 2009, the global growth outlook remains vulnerable. Observers expect that a sustained and robust recovery will be delayed until confidence returns fully and credit conditions ease, leading to improvement in international trade as well as labour markets.

The International Monetary Fund's April 2009 World Economic Outlook forecasts world output to contract by 1.3 per cent in 2009 before recovering to a growth of 1.9 per cent in 2010. Growth in emerging economies is projected to begin to rise during the second half of this year, but advanced economies are foreseen to recover durably at a later stage. Emerging and developing countries would lead the global recovery with a positive real growth rate of 1.6 per cent in 2009 and 4.0 per cent in 2010. In contrast, real output growth in advanced economies is forecast to fall by 3.8 per cent in 2009 and to remain flat in 2010.

Central banks across the world have continued to ease monetary policy albeit at a generally less aggressive pace. In advanced economies, monetary policy was eased further with reductions in interest rates while some central banks are carrying on with quantitative easing. Several major central banks continue to use non-conventional measures, such as asset purchase, to sustain credit flows to consumers and the business sector. In emerging countries, the easing monetary policy stance is maintained. Global interest rates could stay at low levels for several quarters ahead.

The disinflationary momentum remains strong worldwide but there are growing signs of stabilisation of inflation at a low level. However, while the inflation outlook reveals a return to low and steady inflation over the next few quarters given the extent of economic slack, it is feared that the massive fiscal stimulus and monetary easing could lead to higher inflation when the global economy recovers. Rising oil and food prices are likely to worsen the inflation outlook. The Food and Agricultural Organisation Food Price Index started rising to reach 152 in May 2009, after hitting a trough of 139 in February 2009. Crude oil prices have continued to rise, reaching an average of US$70 a barrel up to 22 June 2009 compared to US$48 in March 2009.

Weak economic performance and prospects accompanied by rising unemployment in the euro area, the United Kingdom and the United States have been denting consumer demand. However, recent data provide some encouraging signs of recovery in retail sales in these markets as well as an improvement in international travel sentiment, which augur well for the export-oriented sectors in Mauritius.

**Domestic developments and outlook**

Economic conditions in Mauritius have been influenced by these global economic developments. The data show that quarterly growth declined steadily in the last three quarters of 2008 to reach 4.3 per cent in the final quarter. This trend is expected to have persisted during the first semester of 2009. The MPC noted that visibility in the global growth outlook has improved slightly since March 2009. As a result, a reversal of the declining trend in quarterly domestic growth rate is anticipated in the second half of 2009 given brighter prospects in major export markets. The Central Statistics Office projects economic growth at 2.5 per cent for 2009, which converges around the forecasts made by a number of observers. The economy is projected to grow at a higher rate in 2010 against the backdrop of an anticipated improvement in the global growth outlook.

The performance in key export sectors is expected to have been negative in the first two quarters of 2009, as weak external demand weighed on exports. However, the outward-looking sectors appear to have survived the worst and a gradual recovery is anticipated in the second half of 2009. After falling by 9.9 per cent in the first quarter of 2009, tourist arrivals should gradually pick up in the second half of 2009 as the international travel sentiment improves. It is hoped that recovery in retail sales in main export markets will favourably affect the textile sector. Overall, there may not be further downside risks to the domestic growth outlook relative to the March 2009 assessment.

The MPC noted that the outlook for employment remains weak. The unemployment rate rose in the first quarter of 2009 relative to the last quarter of 2008. Labour market developments are likely to reflect trends in the broader economy with some lag, suggesting a possible rise in unemployment in the coming quarters. Nonetheless, job losses are expected to be mitigated to some extent by the fiscal stimulus package, which ties down job preservation with the financial and operational help the Government gives to viable firms in difficulty.

Overall, growth in money and credit aggregates remains moderate and does not jeopardise the attainment of low inflation over the short to medium term. The growth rate of money supply in the year to April 2009 rose marginally to 15.1 per cent, from 15.0 per cent in March 2009. The growth rate of credit to the private sector continued to slow in the year to April 2009, reaching 18.7 per cent, from 20.0 per cent a month earlier. This deceleration is indicative of the slowdown in domestic economic activity. The banking sector remains robust and availability of credit is not a cause for concern.

Inflationary pressures have continued to subside. Inflation for the twelve-month period ended May 2009 declined to 7.4 per cent, from 9.7 per cent in December 2008. On a year-on-year basis, inflation dropped more substantially to 2.8 per cent in May 2009, from 6.7 per cent in December 2008. The MPC expects inflation, measured by both the average and year-on-year methodologies, to converge to around 4 per cent in the course of 2009. Looking forward, however, while domestically-generated inflationary pressures appear highly subdued, the inflation outlook is clouded by uncertainties regarding the evolution of oil prices on international markets and exchange rate movements. While the MPC continues to monitor both the twelve-month average and year-on-year inflation, it is attributing more weight to the year-on-year inflation rate in guiding monetary policy decisions.[1] The Bank of Mauritius is already publishing the year-on-year inflation rate on its website and in its publications.

The current account deficit of the balance of payments shrank to Rs1.7 billion during the first quarter of 2009, from Rs5.2 billion in the first quarter of 2008, due to an improvement in the merchandise trade deficit, as nominal total imports plunged more than total exports. The significant decline in nominal imports seems to confirm the slowdown in aggregate demand. The revised current account deficit as a proportion of GDP for 2009 is now estimated at 7.2 per cent, compared to 10.4 per cent in 2008. During the first quarter of 2009, gross foreign direct investment inflows have slowed and portfolio investment registered net outflows relative to a year ago, reflecting a deceleration in private capital flows.

Concern was also expressed about the saving rate estimated at 14.7 per cent in 2009, the second lowest rate since 1976.

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[1] *Year-on-year inflation is computed as the change in the Consumer Price Index (CPI) for a given month compared with the same month of the preceding year in percentage terms. The Central Statistics Office computes the inflation rate by comparing the average level of prices, as measured by the CPI, during a twelve-month period with the average level during the corresponding previous twelve-month period.*

The domestic foreign exchange market remains fairly well balanced, with the rupee exchange rate reflecting mostly international currency trends. There is, however, need for continued vigilance in preventing excessive exchange rate movements, containing balance of payments pressures and maintaining a prudent level of foreign exchange reserves.

The MPC noted that the fiscal stimulus package implemented by the Government and the substantial easing of monetary policy by a cumulative 250 basis points since October 2008 have supported business as well as consumer sentiment. The MPC weighed the risks to the growth and inflation outlook over the policy-relevant horizon. In the light of its assessment, it determined that the inflation outlook will continue to improve in the short to medium term with, however, potential upside risks in the longer term, while a reversal of the declining trend in the quarterly growth rate from the second half of 2009 onwards should take place provided global growth prospects remain favourable. It noted that the full effects of the coordinated expansionary economic policies were yet to be felt. The MPC judged that, on balance, the current stance of monetary policy remains appropriate.

The MPC will continue to monitor economic and financial developments and remains committed, as per its mandate, to formulate and determine monetary policy, taking into account the orderly and balanced economic development of Mauritius.

**Voting Pattern**

The MPC voted unanimously to maintain the key Repo Rate at 5.75 per cent per annum.

**Date for Regular Meeting**

The MPC will convene its next quarterly meeting on 29 September 2009. It stands ready to meet outside regular meetings as and when required to assess the evolution of the economic situation and, if needed, take appropriate policy measures.

*Bank of Mauritius*
*22 June 2009*