



BANK OF MAURITIUS

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Minutes of the 36th Monetary Policy Committee Meeting of 6 April 2015

The 36th meeting of the Monetary Policy Committee (MPC) was held on 6 April 2015 at 10:15 hours at the Bank of Mauritius and was chaired by Mr Rameswurlall Basant Roi, Governor.

Members present: Mr Yandraduth Googoolye - First Deputy Governor; Mr Mahendra Vikramdass Punchoo - Second Deputy Governor; Mr Pierre Dinan, Mr Mohammad Mushtaq Namdarkhan, Dr Streevarsen Narrainen and Mr Guy Wong So - External Members.

Member absent (with apologies): Mr Nishan Degnarain – External Member.

Summary of Reports on Economic and Financial Developments

International economic environment

- The MPC was briefed on the revised global growth projections set out in the January 2015 Update of the IMF's World Economic Outlook**, in which global growth was scaled down by a quarter of a percentage point to 3.5 per cent and 3.7 per cent for 2015 and 2016, respectively. Growth divergences persisted among major economies, and except for the US, the economic performance of all major economies fell short of expectations. Global stock markets had moved higher on the back of the strength of the US economy, aided by the accommodative policy in major economies and low interest rate environment in developed economies.
- Global inflation remains muted due to low commodity prices as well as subdued world output growth.** Low inflation and, in some cases deflation, have led to another global round of monetary policy easing lately. Since December 2014, as many as 20 central banks around the world – including all the major central banks – have eased monetary conditions by slashing policy rates towards zero or below zero. However, the US Federal Reserve is expected to commence hiking policy rates sometime in 2015.
- Currency markets have thus far reflected the contrast between the major central banks' policy outlook, with the US considering its first hike this year while policy outlook is expected to remain ultra-loose in Europe and Japan.** Since the last MPC meeting and up till end-March 2015, the trade-weighted dollar index (DXY) appreciated by about 13 per cent, reflecting the strength of the US economy amongst others. The euro tumbled vis-à-vis other major currencies against a backdrop of sluggish economic conditions, the Greek political and financial situation, and the ECB's quantitative easing programme.

Domestic economic developments

4. **In its latest issue of national accounts in March 2015, Statistics Mauritius (SM) maintained its growth estimates of the domestic economy for 2014 at 3.5 per cent and forecast the growth rate for 2015 at around 4.1 per cent.** Growth in 2014 stemmed principally from an improved performance in '*accommodation and food service activities*' (which reflected higher tourist arrivals) and '*public administration and defence*'. In terms of domestic demand, growth was sustained by household consumption and improved net external demand while investment activity lagged behind.
5. **Latest quarterly data showed that the economy grew by 3.7 per cent y-o-y in 2014Q4, a full percentage point higher than in 2013Q4,** recording growth in all sectors (except for '*construction*') and driven to a significant extent by activities in the tertiary sector. On a seasonally-adjusted q-o-q basis, the economy expanded by 0.6 per cent, same as in 2014Q3.
6. **Reflecting higher job creation in 2014, the rate of unemployment dropped to 7.8 per cent, from 8.0 per cent in 2012 and 2013.** However, the labour market continued to operate below capacity with higher unemployment rate among the youth and female workforce.
7. **Broad money liabilities accelerated further in February 2015 and private sector credit growth maintained its recovery.** Broad money accelerated to 9.6 per cent in February 2015, from 8.3 per cent in September 2014. The growth rate of bank credit to the private sector (excluding credit to global business entities), which declined to negative 0.6 per cent in September 2014, recovered in October 2014 and posted a y-o-y increase of 1.2 per cent in February 2015.
8. **The current account deficit worsened further in 2014.** The current account deficit increased to 10.2 per cent of GDP in 2014, from 9.9 per cent of GDP in 2013, as the marked deterioration in the income account fully offset the improvement in the goods, services as well as the current transfers' accounts. The balance of payments recorded a surplus of Rs23 billion in 2014 and the gross official international reserves of the country rose to Rs124 billion at the end of 2014, from Rs105 billion at the end of 2013.
9. **Significant excess liquidity in the banking system continued to depress money market interest rates.** On average, excess reserves reached Rs15 billion for the two-week period ended 19 March 2015. The build-up in excess reserves was due to the net redemption of Government (and BOM) securities.
10. **The rupee depreciated on account of the strength of the US dollar on the international market.** Separately, the decision of the State Trading Corporation to purchase 50 per cent or more of its foreign exchange requirements from domestic banks contributed to restore the free interplay of market forces in determining the exchange rate. The rupee weakened against the US dollar after the October 2014 MPC meeting as the greenback strengthened on international markets. Between 27 October 2014 and 31 March 2015, on a point-to-point

dealt basis, the rupee depreciated by 14.1 per cent and 6.8 per cent against the US dollar and Pound sterling, respectively but appreciated by 1.2 per cent against the euro.

11. **Inflationary pressures remained subdued as a result of low international commodity prices, low global inflation and tame inflation expectations in the domestic economy.** Headline inflation dropped from 3.8 per cent in October 2014 to 2.5 per cent in February 2015. Y-o-y inflation, which declined from 1.9 per cent in October 2014 to a low of 0.2 per cent in December 2014, rose steadily to 2.2 per cent in February 2015 on account of higher prices of fresh vegetables following adverse climatic conditions in the first two months of 2015.

Staff economic outlook

12. **Headline inflation is forecast at about 3.0 per cent in 2015, conditional on the set of assumptions.** The projected inflation dynamics would reflect trends of food and non-food inflation, modest growth of domestic absorption, moderate global growth and subdued global inflation (that would lower imported inflation), and an improvement in Mauritius' terms of trade on account of the stability of international commodity prices at their current levels.
13. **Domestic growth is estimated at about 4.3 per cent for 2015, on relatively strong fundamentals and conducive monetary conditions.** The strengthening of domestic economic activity would also be supported by the recent budgetary measures and their expected positive impact on investment and business confidence. Going forward, the negative output gap is expected to close gradually.

Monetary Policy Decision

14. **The Governor briefed MPC members about the Bank's current monetary policy operational framework and the disconnect between the key repo rate and interest rates in the domestic money market.** He stated that the excess liquidity in the banking system was driving the yields on Government papers down and thus, the interest rate structure was distorted.
15. **Consequently, he announced that the Bank would come up with a new monetary policy framework and undertake to mop up the excess liquidity in the banking system in a phased manner.** It is expected that money market interest rates would move in line with the key repo rate. He added that since January 2015, the Bank has been conducting sterilised intervention on the foreign exchange market.
16. **Furthermore, the Governor mentioned that the Bank was contemplating to review the allocation process for the auctioning of Government securities.**
17. **Members commended the move to improve the effectiveness of the monetary policy framework.**

18. **In their discussion on the current domestic economic conditions and outlook, the MPC observed that the domestic economy was gathering momentum and would perform better than 2014.** The recent budgetary measures were expected to give a fillip to domestic economic growth. In addition, the MPC took note of the market adjustment of the rupee following the significant appreciation of the US dollar on the international markets lately.
19. **Members were of the opinion that that CPI inflation would remain modest in 2015, barring any exceptional developments.** There would be limited build-up of inflationary pressures until the end of 2015. It is not expected that the depreciation of the rupee would have a notable impact on inflation given the current international economic environment.
20. **Members also discussed about the relationship between interest rates and savings.** A majority of members was of the view that the relationship was at best ambiguous given the interplay of an income effect and a substitution effect. Moreover, there was little empirical evidence that interest rates determine national savings. Given the uncertain global economic environment and the recent budgetary measures announced to kick-start investment amid subdued inflation, members deemed it more appropriate to maintain the current monetary policy stance at this juncture.

Voting pattern

21. **All members unanimously voted to keep the KRR unchanged at 4.65 per cent per annum.**
22. **The MPC continues to monitor economic and financial developments** and stands ready to meet in between its regular meetings, if the need arises.
23. **The next meeting is scheduled on Thursday 16 July 2015.**

Editor's Note

According to the Bank of Mauritius Act 2004, the primary object of the Bank shall be to maintain price stability and to promote orderly and balanced economic development. The Act gives the Monetary Policy Committee (MPC) responsibility to formulate and determine the monetary policy to be conducted by the Bank. The MPC normally meets on a quarterly basis but can meet more frequently.

When the MPC met on 6 April 2015, the last available data on national accounts, employment and external trade were for 2014Q4. The last data available on CPI and inflation were for February 2015.

Abbreviations and Definitions

Headline inflation is measured by the change in the average Consumer Price Index (CPI) over a twelve-month period compared with the corresponding previous twelve-month period.

Y-o-y inflation is measured by the change in the CPI for a given month compared with the corresponding month of the preceding year.

CORE1 inflation excludes food, beverages and tobacco and mortgage interest on housing loan from the CPI basket. Both headline and y-o-y CORE1 inflation measures are available.

CORE2 inflation excludes food, beverages and tobacco, mortgage interest, energy prices and administered prices from the CPI basket. Both headline and y-o-y CORE2 inflation measures are available.

Dealt exchange rate is the weighted average rupee selling rate derived from transactions of US\$30,000, and above, or equivalent.

KRR refers to the Key Repo Rate.

MER11 is the Mauritius Exchange Rate Index, a nominal effective exchange rate introduced in July 2008, based on the currency distribution of merchandise trade.

Y-o-y refers to year-on-year changes.

Q-o-q refers to quarter-on-quarter changes.