Occasional paper **No: 70**

MCB Focus

Economic update

October 2017

MCB GROUP

Disclaimer

TABLE OF CONTENTS

Page intentionally left blank

RECENT DEVELOPMENTS

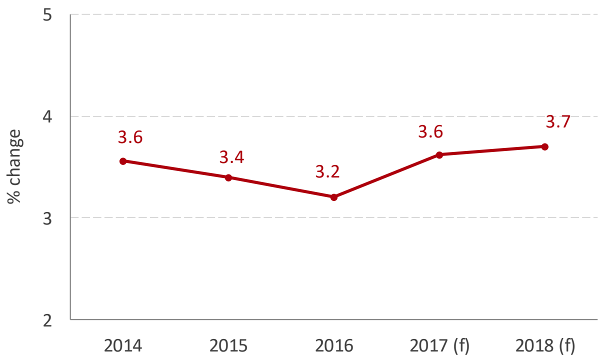
The international backdrop

After several years characterised by what have been termed as false economic dawns, the long-awaited upswing in global activity is perceptibly underway. Indeed, a general acceleration in real GDP growth is being witnessed across both advanced as well as emerging market and developing economies. As per the latest IMF World Economic Outlook, global growth is forecast to edge up to 3.6% this year and attain 3.7% in 2018, representing an upgrade of 10 basis points for each year compared to the prior prognosis formulated in July. The Fund underscored that *"The picture is very different from early last year, when the world economy faced faltering growth and financial market turbulence. Broad-based upward revisions in the euro area, Japan, emerging Asia, emerging Europe, and Russia more than offset downward revisions for the United States and the United Kingdom."* Basically, the global upturn would be driven by appreciable outcomes with regard to investment, trade and industrial production, accompanied by a strengthening of business and consumer confidence. On the other hand, the IMF stressed that the global recovery process is not complete, mainly since growth remains weak in several countries and inflation is below target in most advanced economies. Additionally, several commodity-exporting nations are still struggling to adjust to lower commodity prices relative to those prevailing earlier in the decade. Importantly also, while short-term risks are regarded as being broadly balanced, medium-term risks to the global growth outlook are tilted to the downside. Potential hazards include the following: (i) a more rapid and sizeable tightening of global financial conditions; (ii) financial turmoil in emerging market economies; (iii) persistently low inflation in advanced economies; and (iv) non-economic factors such as geopolitical tensions, political discord, weak governance, extreme weather events as well as terrorism and security concerns. On another note, oil prices have generally rebounded in recent months, to some extent due to signs of a slowdown in US shale production growth. Albeit starting from a low base, they are, on average, expected to recover by an important margin this year when compared to 2016. However, partly given high inventory levels, the evolution of oil prices is likely to be relatively subdued in 2018, with the IMF referring to a flat movement therein on average and the World Bank citing a marginal rise. On the currency markets, partly due to uncertainties regarding the fiscal agenda and even if pressures somewhat abated in recent weeks as the Fed indicated that a further hike is projected before year end, the US dollar has, across several months now, weakened by a notable margin against a broad range of currencies, thus more than offsetting gains registered after the Presidential Election.

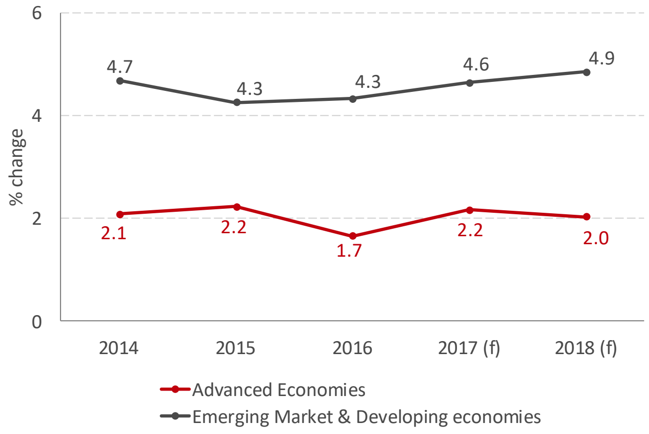
Regarding our key exports markets, growth in the euro area would increase by 30 basis points to attain 2.1% in 2017 on the back mostly of an acceleration in exports, attributable to the recovery in global trade and higher growth in domestic demand linked to accommodative policy conditions. Growth would, nonetheless, moderate to 1.9% in 2018, owing to country-specific factors and the persistence of long-standing headwinds, including weak productivity levels as well as public and private debt overhang. As for the United Kingdom, it has seen weaker-than-expected growth outturns in the first half of the year in the wake of modest private

Box I: Evolution of IMF's real GDP growth projections globally

World output

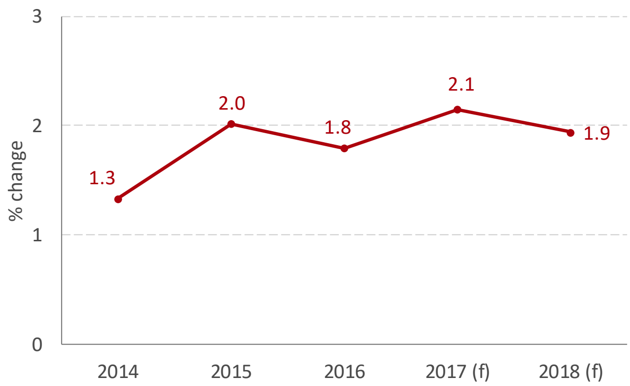


Advanced and Emerging Market & Developing economies

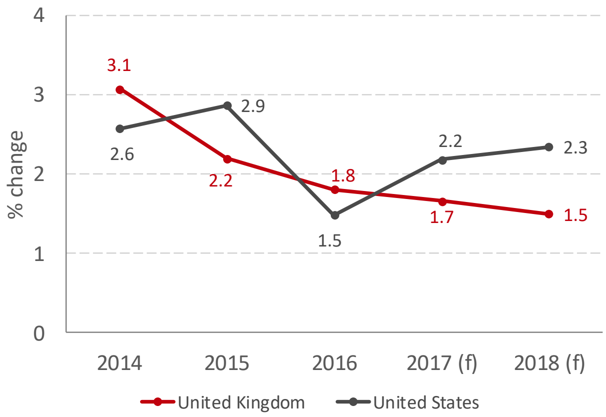


Performance across regions and countries

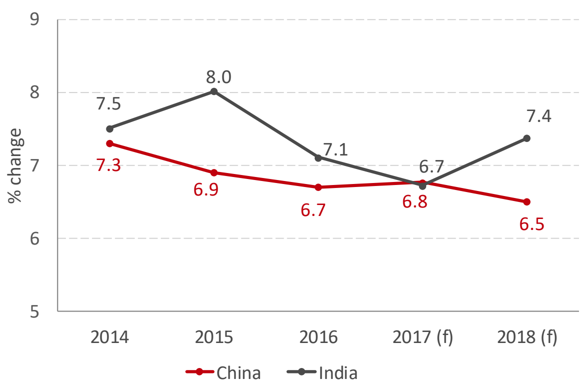
Euro Area



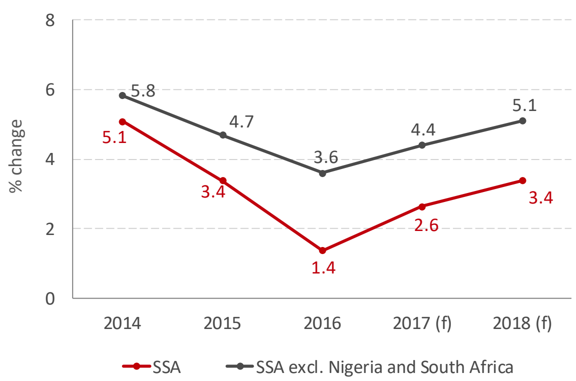
United Kingdom and United States



China and India



Sub-Saharan Africa



(f) forecasts
Sources: IMF World Economic Outlook, October 2017 and MCB Staff estimates

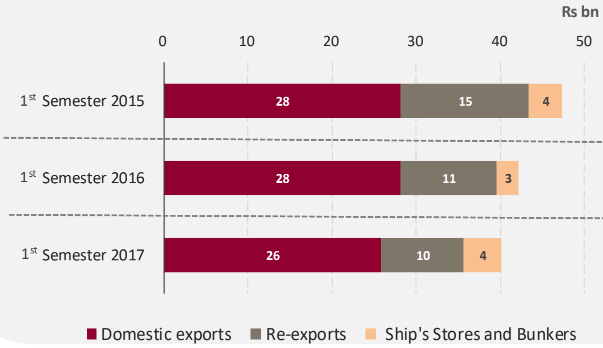
consumption as the pound sterling's depreciation weighed on household real income. In this conjuncture, growth is anticipated to abate in both 2017 and 2018, with economic and business activities to be also impeded by uncertainties linked to the outcome of ongoing Brexit negotiations. As for the medium term, growth will largely hinge on the specificities of the new economic relationship that will be forged with the EU and the extent of any increase in barriers to trade, migration and cross-border financial activity. In the US, notwithstanding significant policy uncertainties, growth is likely to increase to 2.2% in 2017 and 2.3% in 2018, underpinned by supportive financial conditions as well as strong business and consumer confidence. With regard to emerging market and developing economies, GDP growth is foreseen to be reinforced in the near term. To some extent, this would be attributable to a robust performance by China, spurred by policy easing and supply-side reforms. As for the other powerhouse, namely India, growth is, while remaining quite appreciable, projected to notch down this year, owing to the persisting disruptions associated with the currency exchange initiative introduced in November 2016 as well as transition costs related to the launch of the national Goods and Services Tax in July 2017. Yet, as per the IMF, key structural reforms being executed would push up growth next year and elevate it above the 8% mark over the medium term. As for sub-Saharan Africa, whereas sizeable disparities exist across countries, growth is projected to firm up in the near term, partly due to an expected recovery in commodity prices. Nevertheless, activity levels would be constrained by idiosyncratic factors weighing on performances of key economies, i.e. South Africa and Nigeria. On excluding these countries, a more favourable picture is exhibited, with growth likely to stand at 4.4% and 5.1% for 2017 and 2018 respectively.

The domestic scene

While awaiting for planned infrastructure-upgrading projects and policy measures to be comprehensively put into execution and achieve their intended consequences, the real, fiscal and external sectors of the Mauritian economy have been exposed to key challenges in recent periods. In spite of some sectors continuing to fare well – notably tourism which posted an annual growth of around 6% in arrivals over the January to September 2017 period – nationwide output continued to move at a rather restrained pace lately on the back of sluggish investment levels and difficulties faced on the external front, with the country's exports of goods being hit by subdued demand in several key markets and the relative strength of the rupee. Against this backdrop, the Monetary Policy Committee (MPC) of the Bank of Mauritius cut the Key Repo Rate by 50 basis points in September last in an attempt to stimulate investment into the productive sectors and provide a boost to the growth momentum. Of note, the magnitude of this decline has caught the attention of market players given inflation trends. In fact, it can be recalled that, in the last MPC meeting, the Bank of Mauritius indicated that headline inflation would rise from its current level to reach around 4.0% as at the end of the year. Already, although remaining within manageable levels, headline inflation has drifted into a sustained upward trajectory in recent periods. Coming off from 0.8% in the corresponding month of last year, it attained 3.2% as at September 2017. Likewise for CORE 1 inflation (which does not cater for the 'food, beverages and tobacco' and 'mortgage interest on housing loan' components), it went up by a noticeable margin in recent periods to reach 1.5% as at September last compared to 0.6% one year earlier.

Box II: Zoom on Mauritius' recent export performance

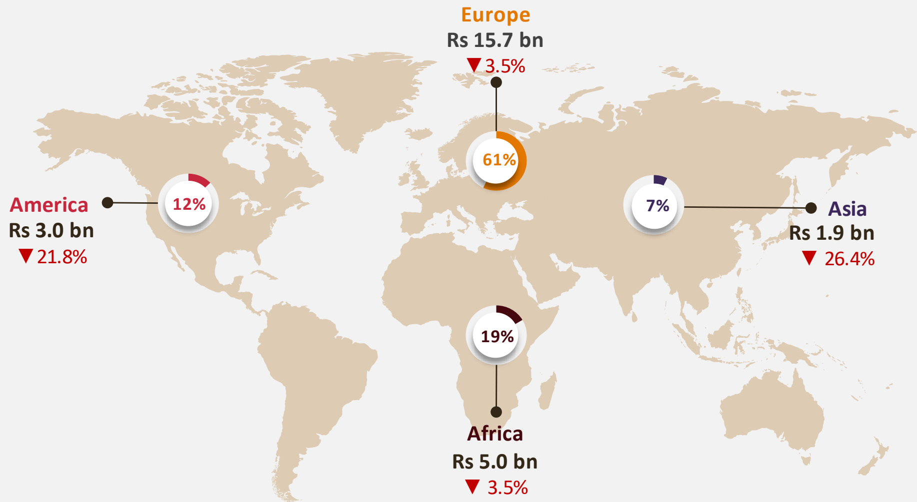
Exports of goods



Year-on-year change (%)
(1st semester of the year vs. corresponding period of the previous year)

Domestic exports	Re-exports	Ship's Stores and Bunkers	Total exports
-3.6	+69.8	-43.2	**+5.1**
0.0	-25.2	-31.9	**-10.8**
-8.2	-14.1	+68.2	**-5.0**

Domestic exports by region (1st semester 2017)



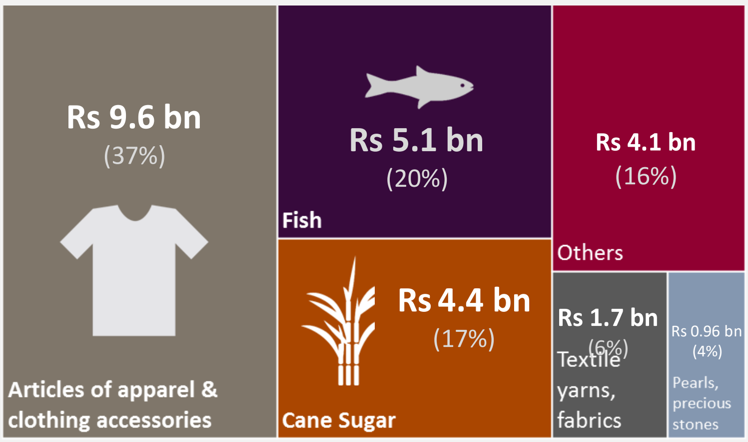
Notes:
(i) Figures in the circles represent the mix of the region in total domestic exports
(ii) Figures in red denote the year-on-year change

Year-on-year change (%)
(1st semester of 2017 vs. 1st semester of 2016)

Top destinations

- ▼ 15 % UK
- ▼ 17% France
- ▲ 5% Italy
- ▼ 22% USA
- ▼ 12% South Africa

Domestic exports by product (1st semester 2017)



Figures in brackets represent the mix of the product in total domestic exports

Top products

- ▼ 16% Articles of apparel & clothing accessories
- ▲ 4% Fish and fish preparations
- ▲ 12% Cane sugar
- ▲ 4% Textile yarns, fabrics, made-up articles
- ▼ 34% Pearls & precious metals

Sources: Statistics Mauritius and MCB Staff estimates

ECONOMIC OUTLOOK

Figure 1 **Main economic indicators**

	Unit	2014	2015	2016[(1)]	2017[(2)]	2018[(2)]
GDPmp	*Rs bn*	392	410	434	460	491
Per capita GDP	*USD*	10,151	9,228	9,588	10,474	11,182
GDP growth (at market prices)	*%*	3.7	3.5	3.8	3.7	4.0
GDP growth (at basic prices)	*%*	3.6	3.0	3.6	3.6	4.0
GDS	*% GDP*	10.6	10.4	11.0	10.7	11.2
GFCF	*% GDP*	18.9	17.4	17.3	17.2	18.8
Private sector investment	*% GDP*	14.0	12.6	12.8	13.0	13.4
Public sector investment	*% GDP*	4.8	4.7	4.4	4.3	5.4
Headline inflation	*Dec, %*	3.2	1.3	1.0	3.6	3.2
Budget balance	*CY, % GDP*	-3.2	-	-	-	-
Budget balance	*FY, % GDP*	-	-3.9*	-3.5	-3.5	-3.2
Public sector debt	*Dec, % GDP*	60.7	63.6	64.5	64.7	63.6
Balance of visible trade	*Rs bn*	-77.3	-74.7	-81.6	-94.6	-101.8
Current account balance	*% GDP*	-5.6	-5.0	-4.3	-5.9	-6.2
Overall balance of payments	*Rs bn*	+23.0	+20.0	+26.2	+15.4	+17.0
Overall balance of payments	*% GDP*	5.9	4.9	6.0	3.4	3.5
Unemployment rate	*average, %*	7.8	7.9	7.3	7.2	7.0

(1) Revised estimates (2) MCB revised forecasts

** The budget deficit for 2015 in the table relates to the January to June period as per official disclosures and based on computations from GDP for H1 2015*

Sources: Statistics Mauritius, Ministry of Finance & Economic Development, Bank of Mauritius & MCB staff estimates

Economic growth

Revised forecast for 2017

Reminiscent of the prevailing conjuncture and as highlighted in recent editions of the MCB Focus, the country's economic expansion is anticipated to remain relatively subdued this year. Our latest projections, which are broadly in line with those of the Bank of Mauritius, while slightly undershooting those of Statistics Mauritius and the IMF, show that real GDP growth would attain 3.7% when measured at market prices and 3.6% when computed at basic prices. These forecasts are respectively 10 basis points and 20 basis points lower than the prognosis formulated in June last. In addition to factoring in an upwardly revised real GDP growth estimate for 2016, the revisions have been mainly prompted by the incurrence of greater-than-expected delays with respect to the initiation and execution of envisioned large-scale infrastructure-upgrading projects, notably those assigned in the Public Sector Investment Programme, with a key case in point being the Road Decongestion Programme. Against this backdrop, we have, on the sectorial front, further downgraded our outlook for construction. Thus, contrary to prior expectations and in spite of recording a relative upturn after several years of lacklustre growth, the sector's impact on nationwide activities would be quite contained. Likewise, despite measures executed to boost activity levels, several strategically-important sectors – notably seafood as well as the export- and domestic-oriented manufacturing industries – would post dimmed performances, mainly owing to challenging market access and local structural bottlenecks. Additionally, our growth predictions have been scaled down for sugar on the back of lower production and ICT following the observed drop in telecommunication activities during the first semester as per Statistics Mauritius. On a favourable note, the ICT sector would still cast a noteworthy impact on economic growth on account of its competitiveness and market diversification breakthrough, likewise for financial and business services, although global business operators are likely to face up to challenges in adapting to the evolving operating environment, in particular in relation to their endeavours to diversify into new markets and broaden the product base.

As hinted above, the contribution of national investment to real GDP growth would remain subdued this year on the back of its contained evolution. At a granular level, it is comforting to note that the first sod has been turned in respect of specific large-scale ventures. In particular, pre-construction works have started on the site of the Metro Express project in September last and the water pipe replacement project has kick-started. Besides, the project at the port involving *inter alia* the extension of the quay of the Mauritius Container Terminal and the expansion of the container stacking yard has been concluded. However, in keeping up with execution delays, several ongoing and envisaged ventures would, in all probability, remain at a preliminary phase of implementation by the end of the year, with the bulk of expenditures for various undertakings to unfold only as from the first quarter of 2018. Against this backdrop, public sector investment would end up remaining flat in 2017. Consequently, while being at odds with pronouncements made in terms of capacity-building, such capital outlays would account for only 4.3% of GDP in 2017, which is well below the level advocated to enhance the country's growth pattern. As for private investment, it is, in line with recent trends, predicted to register an appreciable growth performance. This outcome would be principally attributable to a notable expansion in respect of non-residential outlays, especially those pertaining to hotel renovation. Yet, the progression of private investment still calls for scrutiny insofar as it continues to be marred across most economic sectors and is, by this means, anchored on relatively narrow foundations. On the whole, the share of national investment to GDP is forecast to stand at a relatively low rate of 17.2% in 2017.

Box III: Evolution of growth-related indicators

Impact of indicators on real GDP growth

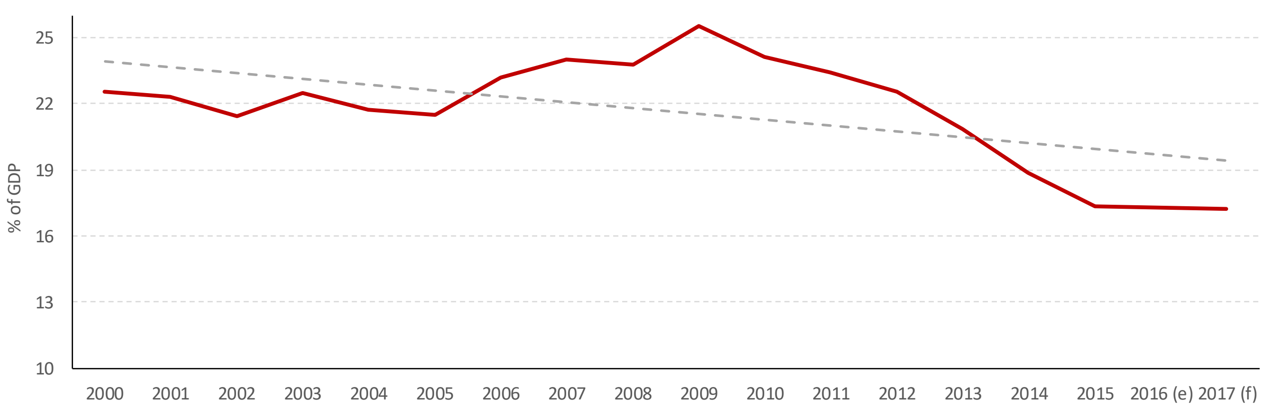
The country's economic expansion has been restrained in recent times, with real GDP growth at market prices averaging around 3.6% over 2012-16, compared to some 4.6% during the previous 5-year period. This performance was largely driven by the bridled national investment climate and the sluggish evolution of net exports of goods and services. As highlighted in the report, these indicators would remain in unfavourable territories in 2017 as well.

Contribution to real GDP growth (% point)	2013	2014	2015	2016(e)	2017(f)
Investment	**-0.7**	**-1.2**	**-1.0**	**0.6**	**0.6**
Public	-0.3	0.1	0.0	-0.1	0.0
Private	-0.5	-1.3	-1.1	0.8	0.6
Consumption	**2.2**	**2.6**	**2.6**	**2.6**	**2.7**
Net exports of goods & services	**-2.8**	**0.1**	**-4.2**	**-2.3**	**-1.6**
Net exports of goods	-1.0	-0.5	-4.2	-4.1	-1.3
Net exports of services	-1.8	0.6	0.0	1.8	-0.3
Inventories (incl. statistical discrepancies)	***4.8***	***2.3***	***6.2***	***2.8***	***2.0***
GDP at market prices	**3.4**	**3.7**	**3.6**	**3.8**	**3.7**

National investment

Over time, the national investment rate pursued a marked downward trajectory, plunging below the psychological threshold of 20% of GDP since 2014. Subdued/erratic trends were noted in respect of both public and private investment.

Nationwide investment rate



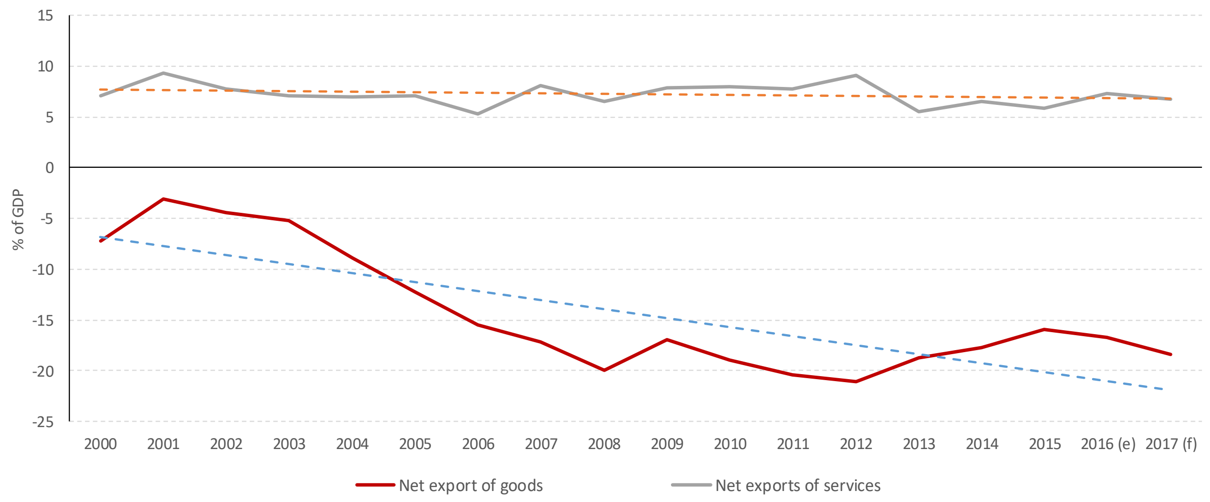
(e) Revised estimates (f) MCB forecasts
Sources: Statistics Mauritius, National Accounts & MCB staff estimates

Box III: Evolution of growth-related indicators (Cont'd)

External trade

Partly attributable to the tepid economic conditions characterising our key trading partners, net exports of goods and services have, in recent years evolved at a tepid pace, with the trend regarding our exports of goods warranting attention.

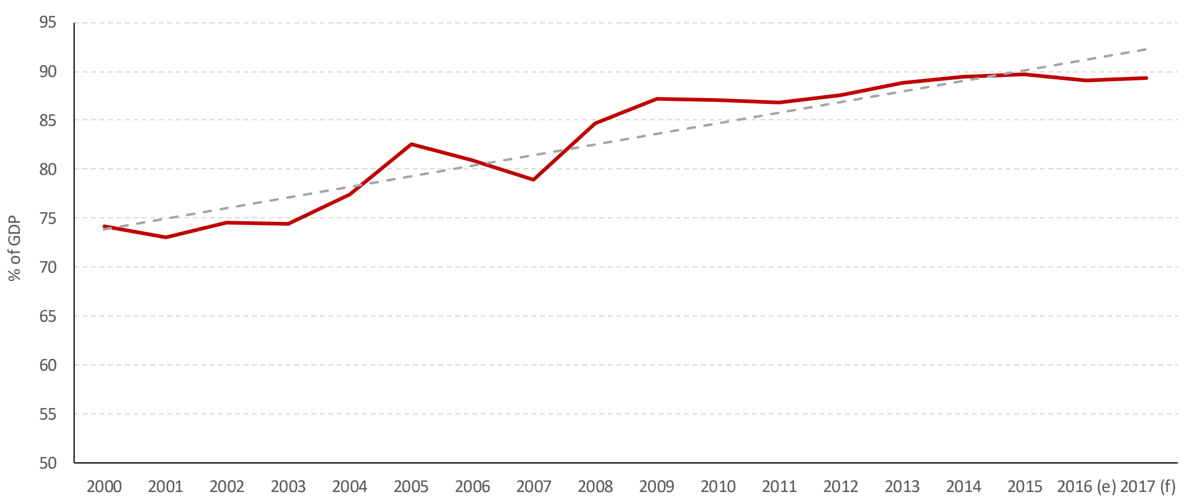
Net exports of goods and services



Final consumption expenditure

Whilst the ratio of final consumption expenditure to national output has stayed generally elevated, its overall net impact on value added in the economy is, nonetheless, limited by the relatively sizeable import content associated.

Total consumption



(e) Revised estimates (f) MCB forecasts
Sources: Statistics Mauritius, National Accounts & MCB staff estimates

As a major source of apprehension and in line with the afore-mentioned recent trends, the tepid evolution of net exports of goods and services would, amidst the demanding global context and compounded by the prevalence of domestic imbalances, have a non-negligible impact on the forecasted real GDP growth. Their share of GDP is foreseen to deteriorate, with concerns mainly fuelled with respect to exports of goods. The latter's share of national output is on course to decline for the third consecutive year to attain close to 18%, which is far inferior to a rate of around 27% witnessed a decade ago. Overall, these outcomes are worrisome as they testify to the limitative nature of our productivity and competiveness foundations, which tend to prevent the country from optimally tapping into international markets for goods and services. Nevertheless, it is widely recognised that external trade is a focal engine for attaining high, balanced and long-term economic expansion. Thus, embracing such a trajectory is deemed to be particularly essential for Mauritius given the small size of the domestic market and the fact that the net impact of consumption on value added is limited by its relatively high import content.

Updated outlook for 2018

In light of unfolding developments, our real GDP growth forecast for 2018 has, in our baseline scenario, been maintained at 4.0%, when measured at both basic and market prices. In addition to factoring in the projected recovery in global economic conditions – especially within some of our main export markets, with the exception of the UK – the growth performance, which would improve as compared to 2017, is foreseen be anchored on a relatively prompt operationalisation of initiatives earmarked by public and private stakeholders. Essentially, alongside being aided by the likely appreciable performances by selected key economic sectors, we expect the country's expansion in 2018 to be predominantly driven by a notable expansion in national investment, largely spurred by an anticipated significant growth in public investment. Essentially, in spite of making allowance for their technical complexities, the sheer size of projects announced by the authorities suggests that the subsequent impact on real GDP growth should be important if the ventures are instigated on a timely basis and/or are, at least, subject to a relative acceleration in their pace of implementation when compared to works undertaken this year. Illustratively, in line with announcements made by the authorities, several major capital projects are, to varying magnitudes, set to be implemented during the course of next year. Markedly, on-site works for the Metro Express project are likely to gain momentum, while several ventures earmarked within the Road Decongestion Programme would unfold. In reference to that, the authorities have proclaimed that major investments will take place to enhance the national transport network, notably those relating to the Jumbo-Phoenix round about, the second fly-over to connect directly the Motorway M1 to the Terre Rouge Verdun motorway, and the A1M1 Bridge at Sorèze. In the same vein, the Graded Separated Junction project on M1 – which is scheduled to be completed by December 2018 as per the authorities – is underway, with the aim being to alleviate traffic congestion at the entrance of Port Louis Centre. Other earmarked/ongoing projects at the national level include the upgrade of water distribution systems, the further extension and modernisation of port infrastructures, the reinforcement of the power generation and distribution set-ups, the improvement of health facilities, and the deployment of social housing and community development initiatives. As for private investment, it is forecast to record an appreciable growth, prompted by the realisation of ventures, especially those related to Smart Cities, tourism and energy, alongside being, in the latter case, aided by recourse to Public Private Partnerships for specific projects. All in all, the national investment ratio would improve by a relatively important margin to attain 18.8% of GDP in 2018. Nevertheless, this figure is still several percentage points below the level advocated to gratifyingly foster high and sustainable activity and employment creation on the national scale. Also, due circumspection is warranted when appraising the overall significance of investment in boosting real GDP growth as (i) several ventures would come across with a particularly sizeable import content; and (ii) the financial and commercial viability of some undertakings would need to be conclusively ascertained.

Appraisal of the growth performance

The macroeconomic performance of Mauritius calls for in-depth scrutiny insofar as the country continues to be exposed to non-negligible challenges in its bid to cope with growth-hindering factors and realise its ambitions.

Resilience and firmness of growth

It is essential that we remain vigilant in our assessment of the country's growth performance insofar as the operating context remains unsteady. In fact, our projections will, in due course and as deemed appropriate, be subject to appraisal in light of changes affecting the local and international landscapes. In this spirit, backed by assumptions formulated, the following figure depicts an overview of alternative scenarii for investment and growth for the Mauritian economy in 2018, in the event that identified downside and upside risks materialise. As it stands, the distribution of risks to the growth outlook is, on balance, slightly tilted on the downside. Notably, growth could turn out to be lower than currently anticipated if acute delays are incurred in the accomplishment of key investment projects and identified projects are realised in a less ambitious way than planned. Besides, partly reflecting the country's sub-optimal idiosyncratic capabilities, the growth momentum could lose traction if risks to the global outlook materialise and the pace of the international economic recovery process is derailed. That being said, it is, also, important to highlight that the growth outlook is subject to non-negligible upside risks. Especially, bearing in mind the line-up of several sizeable infrastructure projects, their impact on nationwide value added could be more meaningful that our baseline scenario suggests if the authorities improve project implementation rates beyond historical trends, backed by upgraded capabilities. In another respect, our growth performance could be boosted if appropriate actions are taken to enable the country to more effectively capitalise on the firming up of the global economic recovery. On this aspect, after asserting that the global growth acceleration process can be regarded as more broad-based that at any time since the start of this decade, the IMF has, indeed, stressed that "*Although it is not yet complete, the more favorable conjuncture offers an opportunity to tackle key policy challenges to stave off medium-term downside risks, rebuild buffers, and raise potential output. The window for action the current cyclical upswing offers will not be open forever*."

Figure 2 Risks to our growth outlook

Scenario	Description and expected impact	Probability of occurrence	Indicative impact on baseline projected national investment ratio	Indicative impact on baseline real GDP growth forecast
Upside	The Mauritian economy manages to comprehensively and timely tap into the growth-avenues linked to the recovering global economic activity levels, thus leading to better-than-expected performances as regards our exports of goods and services and further boosting investment in the country	Low	Up to + 40 bp	Up to + 20 bp
	A higher-than-envisioned growth is achieved in respect of public sector investment, with an enhancement of the authorities' productive capabilities paving the way for a relatively more prominent execution rate for infrastructure undertakings when compared to that depicted during the past few years	Moderate		
	Private sector investment records a notable expansion rate in the aftermath of measures adopted by the authorities to improve the business facilitation framework and an increase in the leveraging of Public-Private Partnerships for ongoing infrastructure projects	Low to moderate		
Baseline	The external environment improves at a noteworthy pace, in line with IMF's baseline growth scenario for the world economy	High	-	-
	The execution of announced reform and policy measures measures provides appreciable support to nationwide activity levels	Moderate		
	Public sector investment is underpinned by the initiation and comprehensive unfolding of large-scale ventures, albeit at a relatively contained pace when making allowance for sub-optimal project implementation capabilities	High		
	An appreciable growth in private sector investment is observed, notably supported by the improved business environment and the unleashing of Government projects	High		
Downside	The global economic recovery is subject to stumbling blocks and loses steam when compared to the baseline expectation, as risks to the outlook materialise	Low to Moderate	Up to - 70 bp	Up to - 30 bp
	A lower-than-envisaged implementation rate of public undertakings is attained, reflecting protracted delays in the materialisation of contemplated ventures – particularly spanning road transport – to some extent attributable to the inherent technical complexities of such undertakings	Moderate		
	Private sector investment evolves at a tempered pace, reflecting the restrained implementation of infrastructure-upgrading projects and a deterioration of the business climate amidst a slower-than-foreseen implementation of the reform agenda and sub-optimal economic measures	Low to Moderate		

Sources: MCB staff estimates

Level and quality of growth

While embodying, *per se*, improving activity levels, our predicted real GDP growth for 2018 continues to evoke a relatively sub-par performance. Basically, as opposed to being comprehensively underpinned by a broadening of idiosyncratic growth-stimulating foundations, the outcome would be partly instigated by the low base effect spawned by the cumulative statistical impact of numerous years of restrained national economic expansion. Besides, growth is still deemed to fall short of the level required for entrenching extensive grounds for employment creation and achieving the country's social inclusiveness aspirations. In this respect, latest indications are that, though a relative improvement in the trend is being witnessed, the unemployment rate would remain rather elevated in the near term. It is expected to stand at 7.2% in 2017 and improve moderately to around 7.0% in 2018 on the back of the challenging economic landscape and ingrained labour market inadequacies. Beyond this headline picture, apprehensions subsist as regard the effectiveness of the country's employment creation ability, especially after considering recent statistics. Official figures for this year's second quarter have revealed that, out of the total unemployed people: (i) 44% were aged below 25 years; (ii) 36% had been looking for work for more than one year; (iii) 69% had working experience. Besides, as a dent to the scope required for underpinning long-term economic progress, the country's activity rate continued to oscillate at around 60%, with an even lower rate of 46% being posted for women, which compares quite unfavourably when juxtaposed against several peer economies (see Box IV). From a holistic perspective, the persistence of gender imbalances in the labour market calls for close inspection, the more so considering that the female unemployment rate has been hovering above the 10% mark for quite some time. It is important to highlight that the subdued participation of women in the employment force tends to expose the country to a paucity of labour resources and a lack of intellectual capital that would, otherwise, have boosted nationwide output by an important margin. As per IMF's Christine Lagarde, *"If women participated in the labor force in the same numbers as men, GDP could increase by as much as 5 percent in the US, 27 percent in India, and 34 percent in Egypt".*

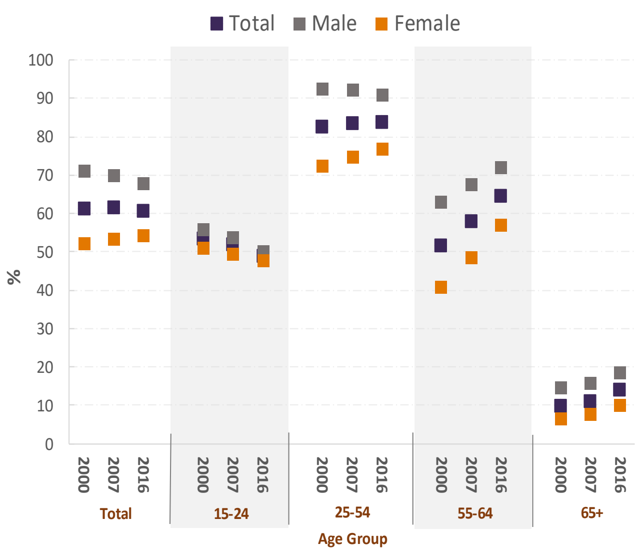
Strength and sustainability of growth

Furthermore, notwithstanding trends characterising real GDP growth, it is, concurrently, essential that we do not be lulled into a misguided sense of security as regards the intrinsic aptitude of the Mauritian economy to nurture robust conditions in support of a high, sound and balanced growth pattern over the medium to long term. In effect, though headway has been made at several echelons, pockets of concern prevail regarding the intrinsic ability of the local economy to (i) display adequate resilience when confronted by external shocks; (ii) cope with foreign market access constraints and competitiveness imperatives that continuously surface on the regional and international markets; and (iii) fittingly and opportunely capitalise on international growth-inducing avenues. These limitations are deemed to be instigated by the persistence of supply-side bottlenecks and

Box IV: Labour force participation rates across countries

As per the IMF's World Economic Outlook: *"In advanced economies, fewer people in the adult population (those 15 and older) have been working or actively looking for work since the turn of the century. This mild downturn in the labor force participation rate began around 2000, appears to have picked up since 2007, and is generally projected to continue and eventually gather pace as populations age*.'' In fact, the ageing of the population exerts downward pressures on the overall labour participation rate. In turn, lower labour force participation tends, in general, to hold back the growth in potential output.

Labour force participation rates by age group and gender in advanced economies



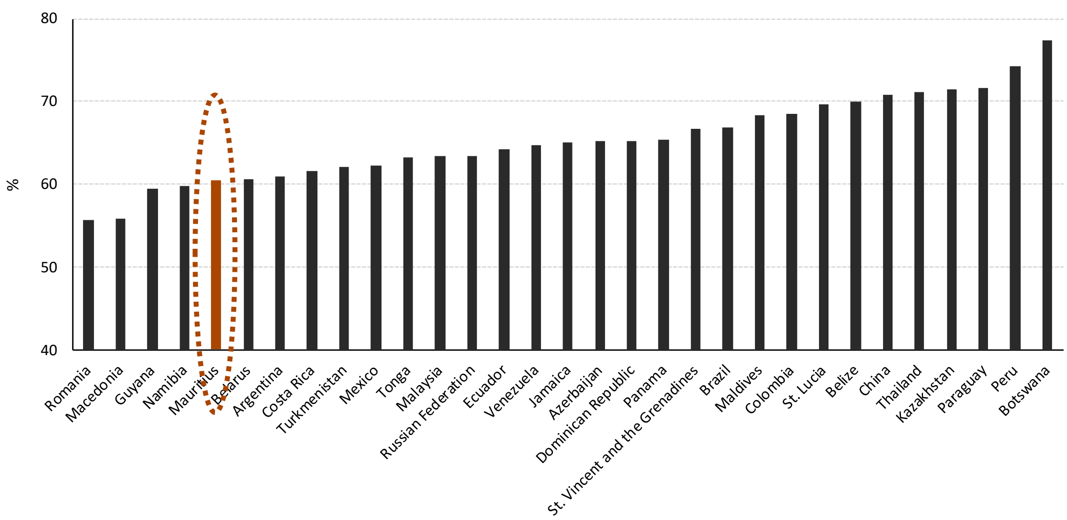
Shifting population share

With regard to advanced economies, the population shares of young (age 15–24) and prime-age workers (age 25–54) have been declining, while those of the 54–64 and 65+ age groups have been on an upward trend. Given that the latter two age groups have lower participation rates than the prime-age group, these shifts tend to lower the overall participation rate.

Rising female participation rate

There have been remarkable gains in the participation rates of women in some countries. According to the IMF, if such gains continue and broaden, the demographic transition may not immediately translate into a slowdown in the growth of the labour force.

Labour force participation rates: Mauritius vs. selected upper-middle income countries



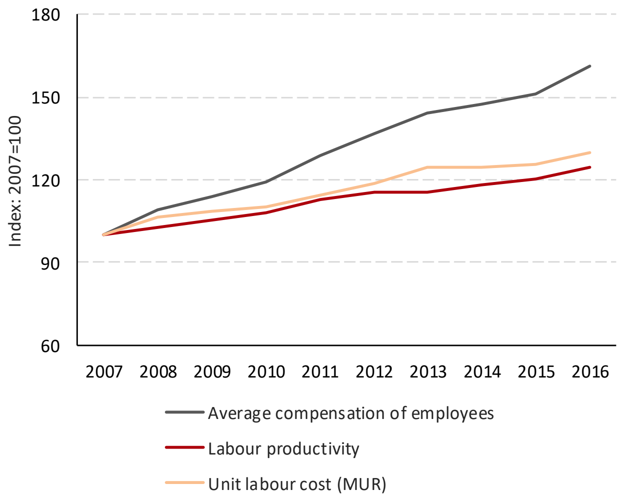
Sources: IMF World Economic Outlook, October 2017, World Bank and MCB Staff estimates

Box V: Productivity-related indicators

Total economy

Productivity	Average annual growth rates 1997-2006	Average annual growth rates 2007-2016	2014	2015	2016
Labour	4.1	2.7	2.3	1.7	3.4
Capital	-0.5	-0.2	0.7	0.8	1.1
Multifactor	1.9	0.9	1.1	1.1	2.0

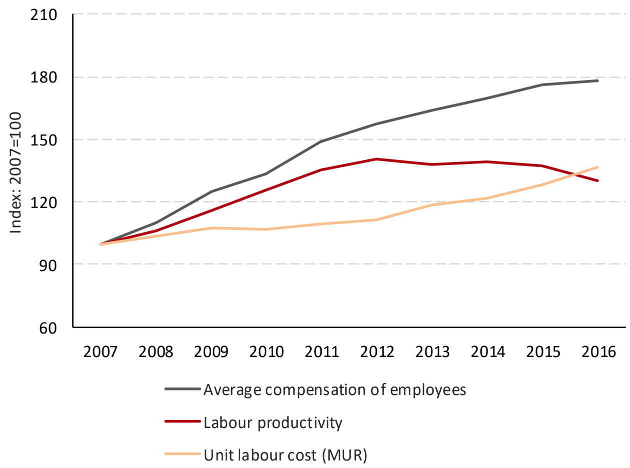
Unit labour cost	Average annual growth rates 1997-2006	Average annual growth rates 2007-2016	2014	2015	2016
MUR	3.4	3.4	-0.1	1.0	3.2
USD	-1.1	2.3	0.2	-12.0	0.9



Export oriented enterprises

Productivity	Average annual growth rates 1997-2006	Average annual growth rates 2007-2016	2014	2015	2016
Labour	3.5	3.6	1.0	-1.3	-5.1
Capital	-2.6	3.8	-3.8	0.3	-4.1
Multifactor	0.1	3.4	-1.1	-0.7	-5.0

Unit labour cost	Average annual growth rates 1997-2006	Average annual growth rates 2007-2016	2014	2015	2016
MUR	4.5	3.8	2.6	5.3	6.7
USD	0.0	2.6	2.9	-8.2	4.4



Source: Statistics Mauritius

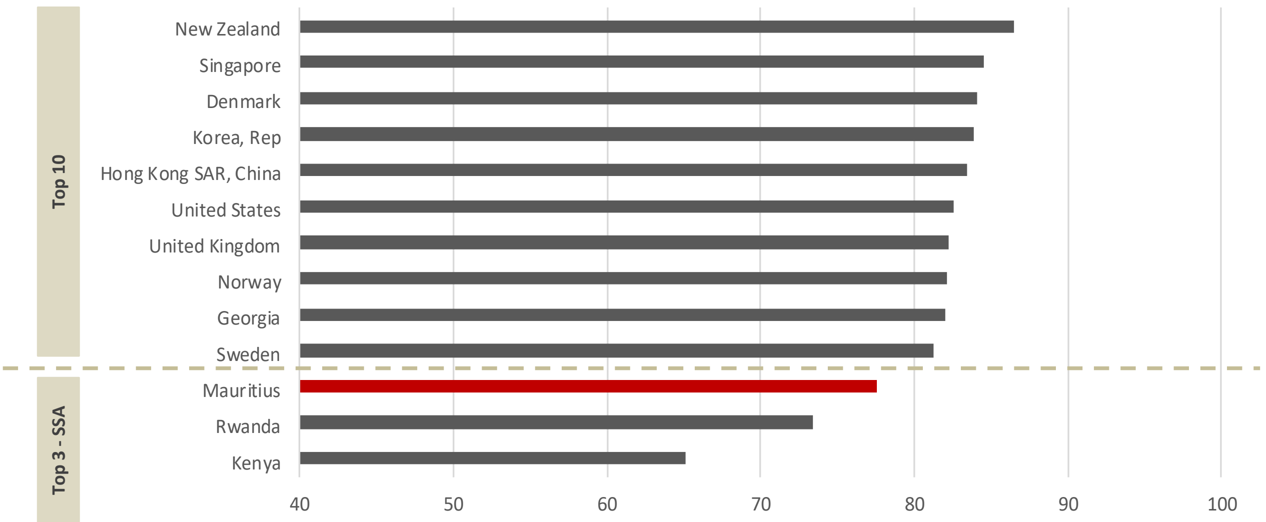
domestic imbalances. In this perspective, key growth-inhibiting factors especially relate to (i) the effectiveness of the institutional and governance set-up; (ii) the efficiency of product and labour markets; (iii) the appeal and adaptability of the business and investment facilitation framework when factoring in the demands and necessities spawned by the international economic and market landscapes; (iv) the dissemination of innovative technologies across productive sectors; and (v) the country's human and capital productivity levels.

Illustratively, latest statistics by Statistics Mauritius showed that the economy's multi-factor productivity stayed in a dimmed zone over time and recorded a growth rate of close to nil during the 10-year period ending 2016 when measured on an average annual basis. With regard to 2016, it is even more striking to observe that the export oriented industry displayed a particularly tepid performance, as testified by contractions of some 5% and 4% in respect of labour and capital productivity respectively. Beyond this element, other limitations exhibited by the Mauritian economy can be underlined via insights gathered from the country's positioning across global performance indicators. For instance, judging by rankings displayed in the Global Competitiveness Report 2017-18 of the World Economic Forum, further efforts are required to improve our performance with regard *inter alia* to the quality of the port infrastructure, the effectiveness of higher education and training, the primary and secondary enrolment rates, the flexibility of wage determination, the level of female participation in the labour force, and the country's technological and innovation readiness. Some of these inadequacies have likewise been underscored by the Global Human Capital Report 2017, which has also shed light on the country's perceived weaknesses in relation to its employment gender gap, unemployment rate, skill diversity in graduates and employee know-how. From a sectorial angle, Mauritius has posted relatively sub-par global rankings as per the Travel and Tourism Competitiveness Index 2017, notably in terms of our price competitiveness and air transport infrastructure, the comprehensiveness of annual tourism and travel data, the quality of our natural and cultural resources as well as the country brand strategy. Besides, the latest edition of the Global Financial Centres Index – which is produced by the China Development Institute and Z/Yen Partners in London – has positioned Mauritius at the 69th spot globally. This ranking tends to suggest that the country needs to make further progress towards improving its international profile, notwithstanding the fact that our financial services sector has, during the past two decades, made noteworthy inroads in diversifying its foreign market footprint and upholding its reputation as an International Financial Centre of repute and substance. Furthermore, whilst it is laudable to take note of the leap achieved by Mauritius in its global ranking in the World Bank's Doing Business Report 2018 to stand at the 25th position amongst 190 countries (see Box VI) – supported by the passing of the Business Facilitation Act 2017 – additional efforts are deemed necessary to further and continuously improve the quality of our business environment as well as uphold our competitive edge in a rapidly evolving international landscape. In fact, as per insights from the afore-mentioned report, key areas currently warranting the country's attention relate *inter alia* to (i) trading across borders, notably the cost to export and import both in terms of documentary and border compliance; (ii) getting electricity, in terms of the cost in percentage of income per capita; and (iii) getting credit, principally in relation to the strength of legal rights index.

Box VI: Ease of Doing Business – Performance of Mauritius

The Doing Business project, launched in 2002, assesses domestic small and medium-size companies and measures the regulations applying to them through their life cycle. The study has become one of the flagship knowledge products in the field of private sector development, and has supported the design of several regulatory reforms in developing countries. By gathering and analysing comprehensive quantitative data to compare business regulation environments across economies and over time, Doing Business encourages economies to compete towards more efficient regulation; offers measurable benchmarks for reform; and serves as a resource for academics, journalists, private sector researchers and others interested in the business climate of each economy. In the Doing Business 2018 report, the methodology for the paying taxes indicator was refined in accordance to best practices, towards better capturing value added tax and corporate income tax audits. As per this year's report, Mauritius has gained 24 spots relative to last year to stand at the 25th position amongst the 190 countries ranked. Worth noting, the country is the only sub-Saharan African nation to feature in the top 25 ranking. Conspicuously, our distance to frontier scores across the 'Starting a business', 'Dealing with construction permits', 'Paying taxes', 'Getting electricity' and 'Registering property' sub-indexes have improved by an appreciable margin. In fact, with regard to the latter, the report highlights that *"Mauritius made the biggest improvement in the ease of registering property in 2016/17. It did this by eliminating the 10% transfer tax and registration duty, implementing a complaint mechanism and publishing service standards."* On the other hand, our scores in respect notably of 'Getting credit', 'Protecting minority investors' and 'Resolving insolvency' remained unchanged from last year.

Distance to Frontier scores for 2018: Mauritius vs. selected countries

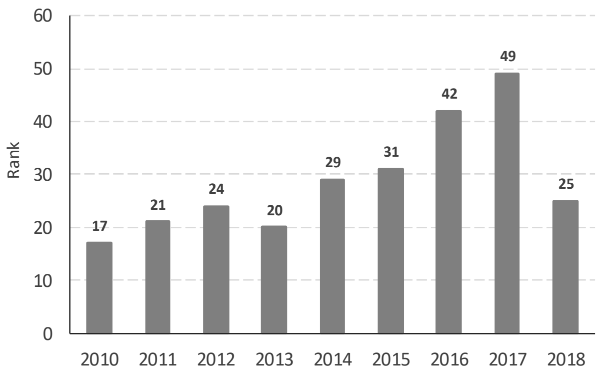


Note: The Distance to Frontier (DTF) score measures the distance of each economy to the "frontier," which represents the best performance observed on each of the indicators across all economies in the Doing Business sample since 2005. An economy's distance to frontier is reflected on a scale from 0 to 100, where 0 represents the lowest performance and 100 represents the frontier.

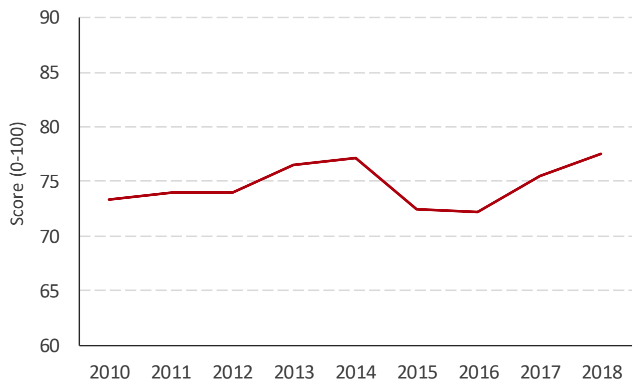
Source: World Bank Doing Business 2018 Report

Box VI: Ease of Doing Business – Performance of Mauritius (Cont'd)

Evolution of our ranking



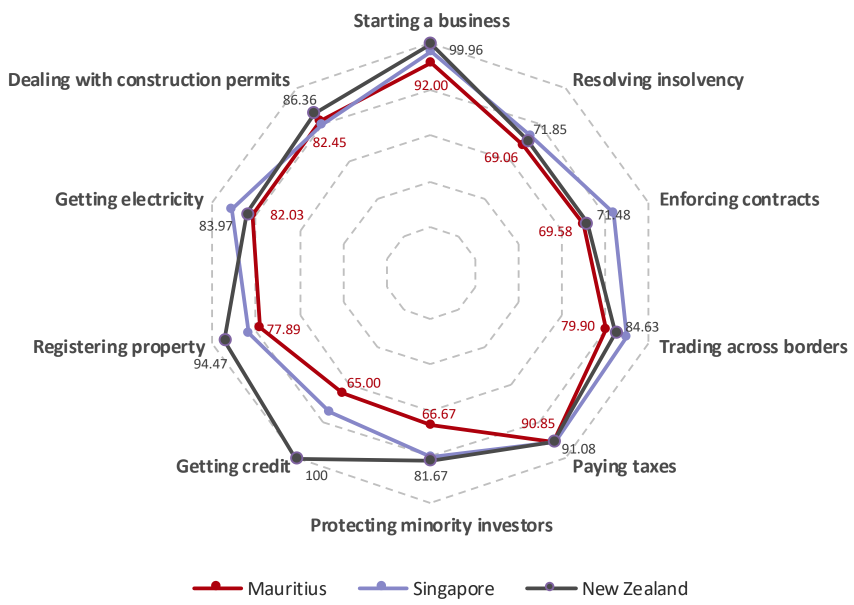
Evolution of our DTF score



Note: Rankings for 2010 to 2017 have been restated to capture the effects of factors such as data corrections and change in methodologies

Radar chart: Mauritius vs. Top 2 performers

Distance to Frontier scores



Scale: Lowest score 0 center, Highest score 100 outer edge

Source: World Bank, Doing Business 2018 Report

Other indicators

In line with prior sustained increases in the consumer price index on the back of hikes in the prices of vegetables, alcoholic beverages and tobacco, as well as gasolene and diesel, headline inflation is forecast to pursue its uptrend in the months ahead and attain 3.6% as at December 2017. While this ascending trajectory is predicted to be maintained during the first few months of 2018, inflation is, barring exceptional shocks, likely to eventually slide down to around 3.2% as at December 2018, as the impact of earlier price movements gradually dissipates. Besides, this anticipated drift factors in IMF estimates suggesting that international commodity prices would evolve at a restrained pace next year, alongside making allowance for the expected relative stability of the effective exchange rate of the rupee during the period. Consequently, inflation should, next year, continue to support the case for the maintenance of a broadly accommodative monetary policy stance by the authorities.

On another note, the level and quality of fiscal balances have continued to warrant close scrutiny lately, in view of the country's socio-economic ambitions and the ongoing and envisaged implementation of major projects by the authorities. As a source of concern, public sector debt accounted for 64.9% of GDP as at June 2017 as per latest figures, which is broadly similar to the preceding year's figure. For the fiscal year ending 30 June 2017, the budget deficit is estimated to have been broadly in line with Government projections positioning it at 3.5% of GDP. For FY 2017/18, the authorities expect the budget deficit to decline to 3.2% of GDP. Notwithstanding a significant rise in capital outlays linked to the deployment of infrastructure projects and higher recurrent expenditures, the improved budget outturn would be mainly underpinned by an anticipated notable rise in taxes on goods and services, the receipt of external grants and the rationalisation of special funds.

On the external front, the exacerbation of imbalances warranted close attention lately in the wake of the subdued global environment and market access strains, while currency dynamics also mattered. In fact, whereas remedial measures have been put into place by the authorities, operators across specific areas were confronted by upward pressures on the rupee during prolonged periods, pursuant notably to prevalence of high liquidity conditions in domestic currency markets. Basically, the effective exchange rate of the rupee appreciated by 4.1% on point-to-point basis over the year ending September 2017. For the first semester of 2017, while re-exports fell by 14%, domestic exports declined by 8.2% on a year-on-year basis, mainly due to a major drop at the level of 'articles of apparel and clothing accessories'. After factoring in a rise of 10% in imports amidst higher commodity prices on average, the balance of trade deficit deteriorated by some Rs 10 billion, with adverse trends persisting in July and August. Subsequently, the current account deficit deteriorated by around 74% during the first semester of the year, while its share of national output is estimated at around 5.8%. Reflecting the deterioration in the current account deficit and a drop in capital and financial flows in spite of positive net errors and omissions, the balance of payments surplus contracted to attain Rs 6.5 billion in the first semester of 2017, which is less than half the outcome posted during the corresponding period of 2016.

As for our outlook, the balance of trade deficit is predicted to worsen by a significant margin in 2017 to attain around Rs 95 billion. For 2018, the trade deficit is on course to break through the centurial threshold and attain around Rs 102 billion, representing 20.7% of GDP, amidst (i) a contained rise in exports given strains on our competitiveness levels and the still soft economic conditions in specific markets such as UK and South Africa; and (ii) a notable hike in imports linked to the undertaking of major infrastructure projects. Consequently, the current account deficit is set to escalate to 5.9% of GDP in 2017, before further worsening to attain 6.2% of national output in 2018, notwithstanding the surplus on the services account. In spite of being impacted by the foreseen rental payments associated with the delivery of two planes through operating leases, the latter performance would be notably driven by higher gross tourism receipts in line with a further expansion in arrivals. Overall, while the forecasted surplus has, to a noticeable margin, been revised downward, the balance of payments would stay in a comfortably positive zone in 2017, with a broadly similar outcome to be realised in 2018 amidst sustained appreciable levels of capital and financial flows, inclusive *inter alia* of the project-based disbursement of the tranches relating to the grant and the lines of credit received from the Government of India.

CONCLUDING REMARKS

While global and domestic activity levels are likely to pick up over the near term, it is essential that the country's private and public stakeholders maintain and strengthen their efforts – notably in terms of their strategic intentions and resource mobilisation – with a view to achieving strong, sustainable, balanced, and inclusive growth. Basically, an immediate priority is to make sure that contemplated infrastructure projects are deployed in an opportune and comprehensive fashion, alongside upholding their commercial viability. More fundamentally, the country is called upon to improve its long-term-term potential output, which would be a decisive move that will sustain and outspread the improvements in living standards registered in recent decades. Yet, alongside striving to considerably improve execution rates for infrastructure projects, the country will only succeed in increasing its potential growth rate from its current level of 4.0 - 4.2% range to above the 5% mark if it manages to tackle deep-seated structural impediments to activity levels. This will be accomplished by means of the further broadening and deepening of structural reforms, which focus on those which are well-sequenced and adapted to the country's inherent circumstances. In this respect, the country would stand to benefit from measures geared towards achieving improved total factor productivity, enhanced external competitiveness levels as well as the further expansion and diversification of our economic base and international market space. In addition to deploying ambitious infrastructure-upgrading projects towards creating an environment which is conducive to the sustained development of the private sector, key focus areas include product and labour market reforms, continuous investments in human capital, the strengthening of the institutional and governance framework for improving the climate for business and investment, and the reinforcement of initiatives in favour of further regional and international trade integration. Moreover, as an important way forward, an improvement in labour supply will act as a major ingredient to boost our potential growth rate, aided by the carefully-planed recourse to high-skilled foreign human capital and rising labour participation rates, notably with respect to women.

With the desired trajectory having been expressed, it is equally important for the Mauritian economy to lay due emphasis on key success factors that will steer its actions in the righty direction. Markedly, the recourse to economic rationality principles is called for in order to foster broad-based and sustainable activity growth. In this respect, while an Exchange Rate Support Scheme has been introduced by the Government as a temporary support to exporters facing the impact of the sharp depreciation of the US dollar, it appears essential that this initiative be, over time, supplanted by the adoption of broad-based structural reforms that will provide perceptive assistance in reinvigorating our external competitiveness levels from a holistic perspective. This will also enable Mauritius to revert to a single exchange rate mechanism in line with internationally-advocated norms pertaining to the adoption of simple and market-based currency practices. Beyond that and from a general perspective, the onboarding of several other growth enablers is also deemed as crucial in order to help the authorities achieve their targets and ensure the perennity of socio-economic benefits, with notable examples being delineated hereafter. Firstly, an important step is to ensure that project implementation aptitudes are strengthened at both private and public sector levels to ensure that earmarked policy measures and business undertakings are brought to fruition as per pre-defined schemas. Secondly, relevant economic sectors are called upon to be sufficiently flexible and resourceful in their strategic intents and operational capabilities towards finding their way and thriving in the increasingly problematic and competitive global trade and investment environment. Thirdly, key and often sensitive economic matters under consideration call for quick resolutions from a social optimality perspective. A case in point relates to the introduction of a national minimum wage, which needs to make allowance for competitiveness imperatives, while it is important that we guard ourselves against labour market distortions that can impact national productivity levels by means of a misallocation of resources. Fourthly, it would be desirable to safeguard the key tenets of the country's competitive advantages, which have so far stood us in good stead, especially the low, simple and predictable tax system, notwithstanding the fact that some distortionary policy measures have, of late, been introduced, thus rendering the tax regime less efficient from a Pareto perspective. Finally, macroeconomic stability would be buttressed by the espousal of fiscal policy which is growth-friendly, prioritises quality investments and contains credible initiatives that guide debt management and consolidation efforts. Importantly, the country stands to benefit from public sector debt levels that evolve in accordance with statutory requirements and help to preserve the investment-grade status of the sovereign credit profile towards assisting economic sectors to judiciously tap into international financial markets.

As it braces itself for 2018, Mauritius Inc. is confronted by the key test of embedding productive and competitive postures that will enable it to navigate through the demanding and complex operating landscape, alongside progressively and convincingly accelerating its transformation as a knowledge-based, innovative and entrepreneurial economy. Nonetheless, steadfastly putting the country on a higher growth plateau is quite a daunting task given the shaky global context and deep-rooted local structural rigidities. Yet, as formulated by Henry Ford, *"Coming together is a beginning, staying together is progress, and working together is success."* Indeed, headwinds and challenges faced by the country can be overcome by ensuring that partnerships between the public and private sectors are strengthened, anchored on a pragmatic and collaborative approach.

J. Gilbert Gnany
Chief Strategy Officer

October 31, 2017

Sources

Bank of Mauritius, *Minutes of Monetary Policy Committee Meeting, Annual Reports & Various* Publications

China Development Institute in Shenzhen and Z/Yen Partners in London, *Global Financial Centres Index (GFCI 22), September 2017*

Government Information Service

IMF Blog, Various articles

IMF, World Economic Outlook Online database

IMF, *World Economic Outlook, October 2017*

IMF, *Regional Economic Outlook, October 2017*

MCB Focus, *Previous issues*

Ministry of Finance & Economic Development, *National Budget Speech 2017/18, Public Sector Investment Programme 2017/18 - 2019/20, Three Year Strategic Plan 2017/18-2019/20, Various Other Publications and Pronouncements*

OECD, *Interim Economic Outlook, September 2017*

Selected Internet and Newspaper Articles

Statistics Mauritius, *National Accounts Estimates, External Trade, Labour Force, Employment and Unemployment, International Travel and Tourism, & Various Publications*

World Bank, *Commodities Price Data (The Pink Sheet), October 2017*

World Bank, *Commodities Market Outlook, October 2017*

World Bank, *Doing Business Report 2018*

World Bank, Global Economic Prospects, *June 2017*

World Economic Forum, *Global Competitiveness Report 2017-18, Global Human Capital Report 2017 & Travel & Tourism Competitiveness Report 2017*

MCB Strategy, Research & Development, Staff Estimates

Page intentionally left blank

MCB GROUP