SBM INSIGHTS

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CHIEF EDITOR'S NOTE

Brexit has continued to be in the highlights over the last few months. Whilst data following the referendum have suggested limited impact to date – the sharp drop in the GBP being a notable exception – we remain cautious around its medium and long term ramifications. Indeed, it appears that the post Brexit journey would be a long and winding road. For 2017, the UK economy is projected to slow down markedly. On the other hand, the euro area growth outlook has been only slightly downgraded, but risks – particularly related to Brexit – are prevalent.

Following a subdued performance in the first half, the US economy started the second half strongly, raising the likelihood that the Federal Reserve will raise its policy rate later this year. China's economy is expected to grow at a slower, albeit still solid and potentially more resilient, pace while India should maintain a robust performance. With commodity prices expected, on an annual average basis, to rebound going forward, resource rich countries should also benefit.

In Mauritius, strong performances have been achieved by the sugar, tourism and financial, business and support activities sectors in the first half of 2016, but the impact on overall growth was mitigated by another contraction in textiles and construction. Measures announced in the National Budget have enhanced growth prospects going forward, and the impact should be felt mostly as from 2017. Overall, our growth forecast for 2016 remains unchanged from our July 2016 estimate of 3.4% while that for 2017 has been upgraded by 50 basis points to 3.9%, underpinned by a notable recovery in the construction sector.

Our special report focuses on the construction sector, which has undergone a downturn since 2011. A reduction in investment in non-residential buildings has been a key drag factor, particularly in respect of hotels and commercial space. Encouragingly, budget initiatives to boost public infrastructure, foster wider home ownership and ease constraints for property development, alongside a strong momentum in tourist arrivals, should help reverse the downward trend in construction activity.

Notwithstanding the improved outlook, important risk factors prevail and require close monitoring. Besides, overall growth rates remain below desired levels and the country should look to consolidate gains and build on the momentum by making further inroads into business facilitation, connectivity, openness and implementation of a fully digital economy, among others.

In our "country insight" section, we provide an extended review of South Africa. The rainbow nation has been at the heart of political and economic turmoil recently, but we believe that it has undeniable long term potential on the back of its strong institutions and deep financial markets. There are strong business linkages between Mauritius and South Africa, which are called upon to grow further as Mauritius positions itself as a financial hub for Africa.

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October 31, 2016

SBM INSIGHTS

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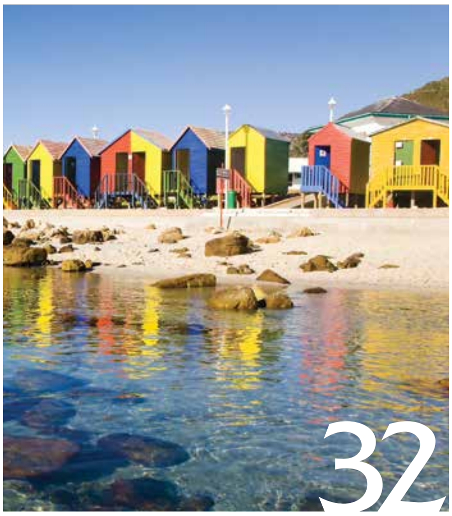

FEATURES

ABBREVIATIONS

BOE	Bank of England
BOI	Board of Investment
CECPA	Comprehensive Economic Cooperation and Partnership Agreement
COMESA	Common Market for Eastern and Southern Africa
DTAT	Double Taxation Avoidance Treaty
DXY	US Dollar Index
ECB	European Central Bank
EU	European Union
EUR	Euro
FOMC	Federal Open Market Committee
FSC	Financial Services Commission
GBP	British pound
GDP	Gross Domestic Product
GVA	Gross Value Added
HDI	Human Development Index
ICT	Information and Communication Technology
IMF	International Monetary Fund
JSE	Johannesburg Stock Exchange
MoU	Memorandum of Understanding
MPC	Monetary Policy Committee
MTSP	Medium Term Strategic Plan
MUR	Mauritian rupee
NDP	National Development Plan
OPEC	Organization of the Petroleum Exporting Countries
PMI	Purchasing Managers' Index
PPP	Purchasing Power Parity
PTA	Preferential Trade Agreement
SADC	Southern African Development Community
S&P	Standard & Poor's
UK	United Kingdom
USD	United States dollar
ZAR	South African rand

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GLOBAL MACROECONOMIC ENVIRONMENT

HIGHLIGHTS

- Economic growth in the US was slow in the first half of the year but picked up sharply in the third quarter. At its policy meeting in September 2016, the Federal Reserve again left the benchmark interest rate unchanged. But it hinted that a rate hike is imminent due to favourable economic data, including solid job gains.
- The UK economy grew at a decent rate in Q3 2016, suggesting that it remained fairly resilient following the EU referendum. Nevertheless, a slowdown remains likely going forward, particularly next year. In August, the Bank of England cut its benchmark rate for the first time in seven years in response to the weakened prospects.
- Growth in the eurozone is forecast to slow slightly next year due to the impact of Brexit. The European Central Bank has not loosened monetary policy following the Brexit vote, but policy remains very accommodative.
- The slowdown of China's growth rate is expected to continue this year. The government has ramped up investment this year in a bid to achieve its full-year growth target of 6.5–7%.
- India continues to be the fastest-growing major economy in the world. For the fiscal year ending in March 2017, GDP is forecast to increase by more than 7%, driven by strong growth in private consumption, and a good monsoon.
- Sub-Saharan Africa looks set to grow this year at its slowest pace in over 20 years, due to contraction or stagnation in its two largest economies—Nigeria and South Africa. This is against a backdrop of depressed oil prices which are causing foreign currency shortage in Nigeria, and weak investment in South Africa amid low investor confidence.

The US, UK, and eurozone are all expected to grow at a slower rate this year than last. But, among major developed economies, the US remains furthest ahead on the path to monetary policy normalization, having raised its policy rate once in the past year and being likely to raise it again by the end of the year. By contrast, the UK cut its benchmark rate in August 2016 in response to the Brexit vote while monetary policy in the eurozone is not expected to be tightened for some time. In emerging markets, the slowdown of China's growth rate is projected to continue this year, while India remains the fastest-growing major economy in the world.

US

The US economy performed sluggishly in the first half of the year. In the second quarter, real GDP grew by 1.4% (quarter on quarter, annualized; 1.3% year on year), an improvement on the disappointing 0.8% recorded in the first. This was driven by a surge in consumer spending, while private investment declined for the third consecutive quarter. But the economy started the second half of 2016 strongly. According to the advance estimate of GDP, quarterly growth in the third quarter accelerated sharply to 2.9% (annualized; 1.5% year on year), the highest level in two years. A surge in exports contributed significantly to the growth figure, but consumer spending remained the main driver. Meanwhile, private investment ended its losing streak. For 2016 as a whole, the IMF forecasts growth of 1.6%.

At its September meeting, the Federal Reserve again left the federal funds rate unchanged, opting for a wait-and-see approach. However, it noted that information received since its previous meeting in July had strengthened the case for a rate hike. In particular, the labour market continued to progress, with job gains averaging over 200,000 per month in the four months to September. Most Federal Open Market Committee (FOMC) participants forecast a rate hike by the end of the year; and three (out of ten) FOMC members voted for an immediate increase at the September meeting. Two FOMC meetings remain for this year, namely in November and December.

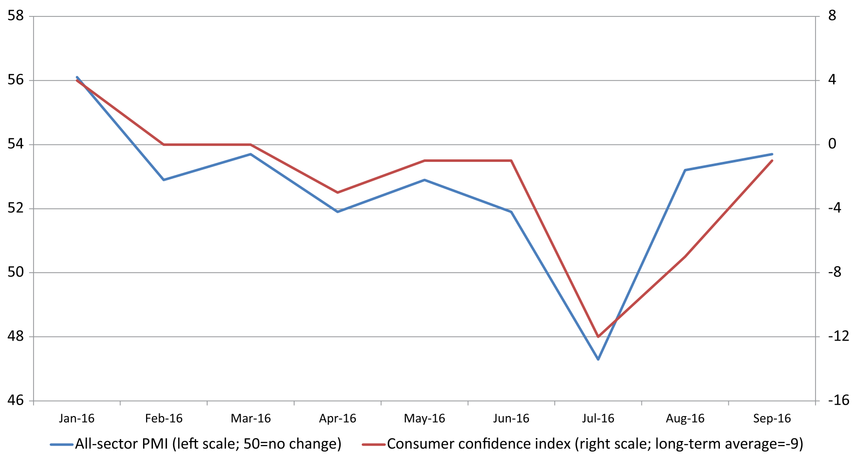
UK

In response to weakened economic prospects following Britain's vote to leave the EU, the Bank of England (BOE) introduced a bold stimulus package in August. This includes: a 25-basis-point cut in the Bank Rate to 0.25% (the first change in seven years), the purchase of GBP 10 billion of corporate bonds, and the purchase of an extra GBP 60 billion of government bonds. In September, the BOE left policy unchanged but signalled that a further rate cut was on the cards this year.

National accounts data suggest that any uncertainties in the run-up to the EU referendum (held on June 23) had little effect on the UK economy: on a quarterly basis, real GDP grew by a satisfactory 0.7% in the second quarter (2.1% on an annual basis), a small acceleration compared to the first-quarter increase of 0.4%. In the third quarter, which is the first full quarter following the referendum, the economy remained fairly resilient—according to the preliminary estimate of GDP, quarterly growth was a respectable 0.5% (2.3% year on year), beating the BOE's forecast of 0.2%. For the full year, the economy looks on track to grow by nearly 2%.

It is still early days, however, in the Brexit journey; the formal process of withdrawing from the EU (under Article 50 of the Lisbon Treaty) will only begin in the first quarter next year. Uncertainty is expected to persist as the eventual arrangement between the UK and the EU would take time to be resolved, and this will weigh on investment and employment. According to The Economist's poll of forecasters, projections of UK GDP growth for 2017 range from -0.5% to 1.3% (average 0.7%), compared with a range of 1.5–2.6% (average 2.0%) before the referendum.

UK survey indicators around the Brexit vote



Sources: IHS Markit; GfK; Trading Economics

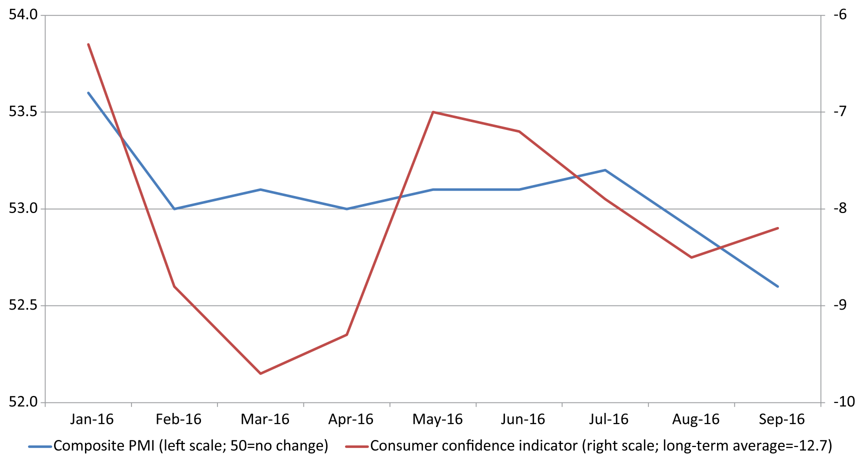
Survey-based indicators fell sharply in the immediate aftermath of the Brexit vote. In July, the Markit/CIPS all-sector PMI fell to its lowest level since 2009, while the GfK Consumer Confidence Index dropped to a 31-month low. But by September, both indices had rebounded to pre-referendum levels. This quick recovery is likely due to: the prompt reorganization of the government which calmed political uncertainty, the introduction of stimulus measures by the Bank of England, and the sharp depreciation of the pound which has aided exporters and boosted tourist spending.

EUROZONE

Eurozone real GDP growth slowed to 0.3%, quarter on quarter, in the second quarter (1.6% year on year), after registering 0.5% in the first. Britain's vote to leave the EU seems to have had little impact on eurozone economic activity so far. PMI data indicate that growth in the third quarter has continued at the same pace as in the second. For the full year, the European Central Bank (ECB) foresees growth of 1.7%, which is slightly above its pre-Brexit forecast. For 2017, however, various organizations have downgraded their forecasts, to reflect expectation of weaker import demand from the UK and of dampened investment growth due to uncertainty as to the eventual relationship with the UK. The ECB projects real GDP growth of 1.6% in 2017 (down from 1.7% pre Brexit), while the mean forecast in The Economist's poll of private forecasters is 1.3% (versus 1.6% pre Brexit).

Despite the impaired economic outlook, the ECB has left its policy instruments unchanged since the UK referendum (its last decision was in October). Nevertheless, monetary policy remains very accommodative, with a negative deposit rate, other key interest rates at or close to zero, and an EUR 80 billion-per-month asset purchase programme. In October, the ECB reiterated its belief that its policy rates will remain at present or lower levels for an extended period of time. As for the asset purchase programme, which runs until March 2017, the consensus is that it will be extended and, to cope with potential shortages of eligible securities, broadened.

Eurozone survey indicators around the Brexit vote



Sources: IHS Markit; European Commission

The Brexit vote had limited immediate impact on eurozone survey indicators. Eurozone PMI and consumer confidence actually diverged in July—the European Commission's consumer confidence indicator weakened slightly, reflecting more negative assessments of the future economic situation; while the Markit Eurozone Composite PMI rose to a six-month high, driven by faster output expansion in Germany.

EMERGING MARKETS

China's real GDP increased by 6.7%, year on year, in the third quarter of 2016, the same rate as in the first and second. This is the slowest pace since 2009, as the downward trend in China's growth rate continues. Growth in the first nine months of the year was supported by government spending—investment in fixed assets by state-owned enterprises increased by 21.1% year on year, while private investment rose by only 2.5% (the ratio of private to total investment was 61.4%, a decline of 3.4 percentage points compared to the same period last year). For the full year, the IMF forecasts growth of 6.6%, within the government's target range of 6.5–7%. In 2017, the IMF expects the expansion rate to slow to 6.2%.

In India, real GDP rose by 7.1%, year on year, in the first quarter of the fiscal year (ending March 2017), down from the 7.9% registered in the previous quarter. Growth in private consumption, the largest component of GDP, slowed while gross fixed capital formation declined for the second consecutive quarter. But consumption growth is expected to accelerate in the second half due to an increase in civil servants' pay and pensions, and higher rural spending following a good monsoon. Private investment should receive a boost from the recent cut in interest rates by the central bank. For the fiscal year, the IMF forecasts GDP to grow by 7.6%.

Sub-Saharan Africa is on course to grow in 2016 at its slowest pace in over 20 years, as its two largest economies, Nigeria and South Africa, experience sharp slowdowns. The IMF forecasts the region's real GDP to expand by only 1.4% this year. Nigeria is expected to contract by 1.7%—its first full-year recession in more than two decades—reflecting disruptions to oil and electricity production due to militant attacks on oil and gas infrastructure, foreign currency shortage due to depressed oil prices, and weak investor confidence. Meanwhile, South Africa is expected to grow by a mere 0.1%—its slowest expansion rate since 2009—against a backdrop of weak fixed investment (which contracted in the first half of the year) and low business and consumer confidence.

Table 1.1: Growth, inflation, and current account

	Real GDP % change		Consumer prices % change		Current account % of GDP	
	2015	2016*	2015	2016*	2015	2016*
US	2.6	1.6	0.1	1.2	-2.6	-2.5
UK	2.2	1.8	0.1	0.7	-5.4	-5.9
Eurozone	2.0	1.7	0.0	0.3	3.2	3.4
China	6.9	6.6	1.4	2.1	3.0	2.4
India†	7.6	7.6	4.9	5.5	-1.1	-1.4
Sub-Saharan Africa	3.4	1.4	7.0	11.3	-5.9	-4.5
Nigeria	2.7	-1.7	9.0	15.4	-3.1	-0.7
South Africa	1.3	0.1	4.6	6.4	-4.3	-3.3

Source: IMF
* Projections.
† Data and forecasts are for the fiscal year ending in March of the following year.

COMMODITIES

Since reaching a three-month low of USD 42/barrel in early August, the price of Brent has rallied to above USD 50/barrel in early October on the back of speculation and later confirmation that OPEC plans to curtail its output. The cartel announced in late September that it aims to reduce crude oil output to a range of 32.5–33 million barrels per day; in September, it produced 33.6 million barrels per day. This plan, if successfully implemented, will help to reduce excess supply more quickly. In the second quarter, excess supply stood at 0.3 million barrels per day, down from 1.7 million barrels per day in 2015. Futures markets suggest that oil prices will rise next year; Brent futures for December 2017 delivery traded near USD 55/barrel as of early October, compared to around USD 52/barrel for front-month futures.

After crossing over USD 1,300/troy oz. just after Britain's referendum, the price of gold traded between USD 1,300/troy oz. and USD 1,370/troy oz. until early October, when it fell below USD 1,300/troy oz. as better-than-expected manufacturing data in the US raised expectations of a rate hike this year.

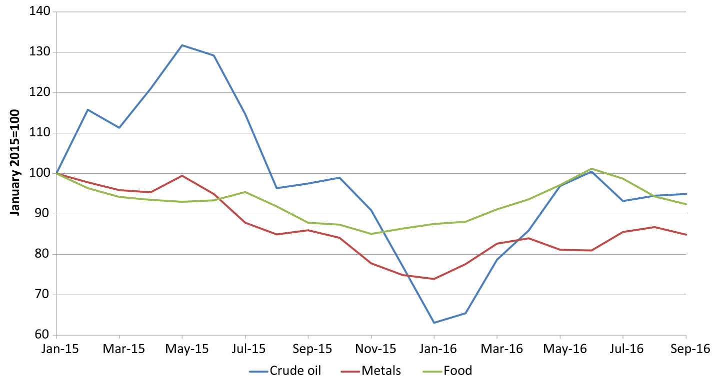
Industrial metals (as tracked by the IMF's metals price index) have appreciated by over 10% this year. Iron ore has performed particularly well. Its price is up by nearly 30% this year, supported by high steel production in China; average monthly steel output in China from March to August was 69.2 million tonnes, close to the record high of 70.7 million tonnes reached in March. But these gains are not seen as sustainable due to persistent oversupply. Iron ore futures for December 2017 delivery traded around USD 43/tonne in early October, while the average spot price in September was USD 57/tonne.

Food prices (as measured by the IMF's food price index) are up by more than 5% this year, with most food commodities appreciating. But wheat prices have fallen this year amid good crop prospects for the 2016/17 season. The benchmark US No. 1 Hard Red Winter averaged USD 123/tonne in September, down by 25% compared to the January average. Global wheat production is projected to reach a record 742 million tonnes in 2016/17, with stocks rising to 234 million tonnes, the highest level since 2001/02.

Figure 1.1: Gold spot price

Source: Bloomberg

Figure 1.2: IMF commodity price indices



Source: IMF

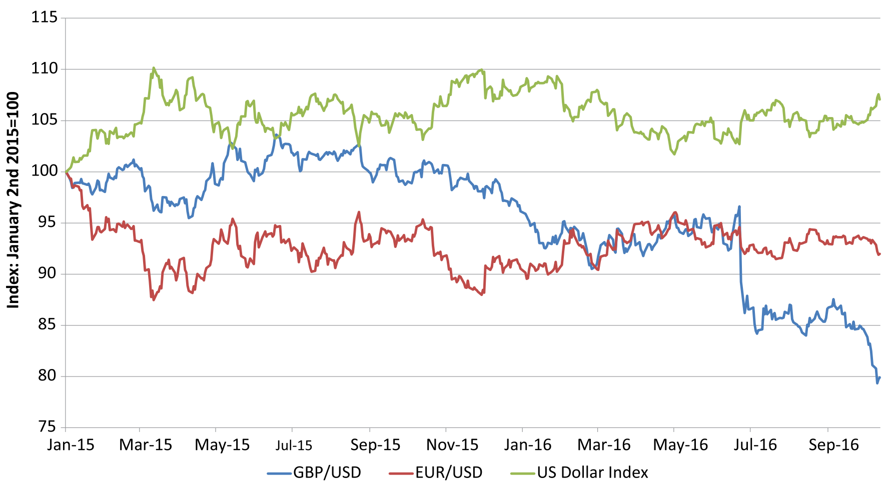
CURRENCIES

The pound sterling has lost more than 15% against the US dollar since June 23, the day of the Brexit referendum. In early October, sterling fell to a 31-year low against the dollar after the prime minister announced that Article 50 of the Lisbon Treaty will be invoked no later than in March 2017.

The euro has shown resilience despite the UK's vote to leave the EU, trading only about 2% lower against the dollar, and more than 15% higher against the pound, compared to June 23.

After rising by more than 20% in 2014–2015, the US Dollar Index (DXY) has this year struggled to find momentum as the Fed has delayed raising its policy rate. The index is down by about 2% since the start of the year. But the dollar has lately received support from expectations of a rate hike later this year; from its August low, the DXY is up by more than 2%.

Figure 1.3: Currencies



Source: Bloomberg

RISKS TO THE OUTLOOK

Risks to the outlook are mostly the same as those flagged in our previous issue, including a 'hard' Brexit—by which the UK sacrifices membership of the single market to regain full control of immigration—and a hard landing in China in the next couple of years. Political uncertainty, lingering geopolitical issues, the potential disorderly unwinding of high debt levels in advanced economies, and rising protectionism are also non-negligible risk factors.

ECONOMIC OUTLOOK: MAURITIUS

HIGHLIGHTS

- Notwithstanding notable growth momentum exhibited by key service sectors such as business and financial services, ICT and tourism, the Mauritian economy continued to grow at a moderate rate with textile and construction remaining major drags on economic activity.
- Indeed, real GDP growth rate at basic prices of the economy dropped sharply to 2.5% in the second quarter of 2016.
- Looking forward, multiple risks to the growth outlook exist, for instance, relating to the abolition of the EU sugar quota regime anticipated for September 2017, uncertainties following the Brexit vote and challenges emanating from the changes in international taxation – revision of India-Mauritius DTAT as well as the Common Reporting Standards.
- Nonetheless, an improved performance is anticipated in the second half of 2016 and in 2017 on the back of strong incentives presented in the budget.
- Our overall real GDP growth projection for 2016 has been maintained at 3.4% while the forecast for 2017 has been upgraded by 50 basis points to 3.9%.
- Whilst the economic situation has remained fragile, the unemployment rate improved in the first half of 2016. It is expected to pursue a downward trend to reach 7.4% in 2016 and 7.2% in 2017, spurred by employment-enhancing measures and improved performance anticipated in some key sectors.
- The relative firming up of the global commodity prices would put pressure on inflation and external balances going forward. On a positive note, anticipated strong tourism receipts as well increase in financial grants would provide some relief to the external balances.
- On an annual average basis, the exchange rate of MUR is projected to remain relatively stable, with a downward bias against the USD and an upward bias vis-à-vis the GBP. Nonetheless, on account of multiple risk factors, exchange rates would face significant volatility.
- Monetary and fiscal policies should continue be supportive in the face of the challenging economic climate, although the scope for further accommodation is restrained.

DESPITE A ROBUST PERFORMANCE IN SUGAR AND SERVICES, GROWTH SLOWED DOWN MARKEDLY IN THE Q2 2016, DRAGGED DOWN BY SHARP CONTRACTION RATES IN TEXTILES AND CONSTRUCTION.

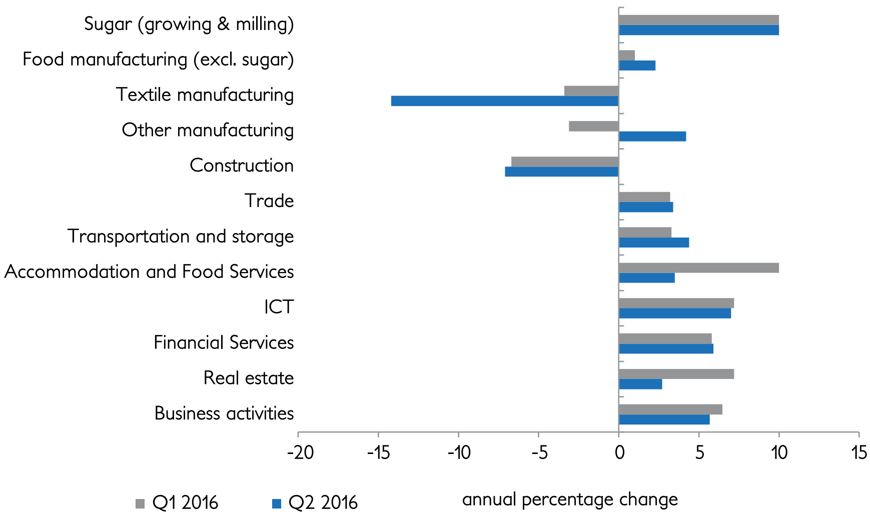
The sugar sector maintained a healthy performance in Q2 2016 on the back of improved climatic conditions compared to last year. Several services sectors, such as information and communication as well as business and financial services also continued to post robust growth rates within the 5-7% range. Notwithstanding these appreciable outturns, overall GDP expansion for the quarter, on a year-on-year basis, slowed down considerably to 2.5% from 4.0% in the first quarter of 2016, as per Statistics Mauritius.

The deceleration is largely due to sharp contractions recorded in the textiles and construction sectors. Indeed, textiles manufacturing output declined by 14.2% in the second quarter year-on-year as apparel and textiles exports slumped by 9.0% amidst ongoing competitiveness concerns. For its part, construction activity contracted by 7.1%, representing the 16th consecutive quarter of negative growth, on a year-on-year basis, within the context of persistently weak investment in buildings and construction, particularly in respect of large private sector projects.

As regards other major sectors, the performance of the trade sector remained subdued, with an expansion rate of 3.4%, reflecting tepid, albeit positive, consumption growth, while expansion in accommodation and food service activities moderated to 3.5% during the second quarter of this year, after three successive quarters of double-digit growth.

For the first semester of this year, economic growth is estimated at 3.2% year-on-year, compared to 3.4% in the previous semester and 2.6% in the first half of 2015.

Figure 2.1: Real growth rates in selected economic sectors – first and second quarters of 2016



*Business activities include: Professional, scientific and technical activities & Administrative and support service activities
Source: Statistics Mauritius

Table 2.1: Selected economic indicators – Mauritius

	Units	2013	2014	2015 (e)	2016 (f)	2017 (f)
REAL SECTOR						
GDP (at market prices)	MUR bn	372	392	410	**435**	**459**
GDP per capita	USD	9,499	9,988	9,073	**9,456**	**9,767**
Real GDP growth rate at basic prices	%	3.4	3.6	3.0	**3.4**	**3.9**
Gross domestic saving (GDS)	% GDP	11.1	10.6	10.4	**10.8**	**10.9**
Investment (GFCF)	% GDP	20.8	18.9	17.4	**17.0**	**17.5**
Private sector investment	% GDP	15.9	14.0	12.6	**12.3**	**12.5**
Public sector investment	% GDP	4.9	4.8	4.7	**4.7**	**5.0**
Headline Inflation	%	3.5	3.2	1.3	**1.2**	**2.0**
Unemployment	%	8.0	7.8	7.9	**7.4**	**7.2**
FINANCIAL SECTOR						
Credit to private sector (excl. GBL) †	% GDP	72.8	70.1	69.9	**68.2**	**68.5**
Deposits (segment A) †	% GDP	86.4	88.2	92.6	**94.0**	**93.5**
Key Repo Rate †	%	4.65	4.65	4.40	**4.00**	**4.00**
Average rupee lending rate *	%	8.25	8.01	7.60	**7.04**	**6.61**
Average rupee deposit rate *	%	3.32	3.25	2.90	**2.41**	**2.11**
Average Treasury bills rate *	%	2.86	2.37	2.14	**2.63**	**2.50**
GOVT SECTOR						
Budget balance ‡	% GDP	(3.5)	(3.2)	(3.9)	**(3.5)**	**(3.3)**
Public sector debt †	% GDP	59.1	60.7	63.7	**63.5**	**61.9**
Public sector debt (for debt ceiling) †	% GDP	53.0	53.4	55.7	**55.4**	**54.3**
EXTERNAL SECTOR						
Balance of visible trade	% GDP	(20.8)	(19.7)	(18.1)	**(18.2)**	**(19.2)**
Foreign Direct Investment (FDI)	% GDP	3.7	4.7	2.4	**3.0**	**3.3**
Current account balance	% GDP	(6.2)	(5.6)	(4.8)	**(5.1)**	**(5.9)**
Balance of Payments	% GDP	4.5	5.9	4.9	**4.5**	**3.8**

(e) Revised estimates
(f) SBM staff forecasts
† As at end December
* Arithmetic mean of monthly weighted averages
‡ Due to the change in fiscal year from calendar year to a July-June cycle in 2015, 2013 and 2014 figures relate to calendar year, the 2015 figure relates to the Jan-Jul 2015 period, and the 2016 and 2017 figures relates to Jul15-Jun16 and Jul 16-Jun 17 fiscal years respectively.
Source: Statistics Mauritius, Bank of Mauritius, Ministry of Finance and Economic Development, and SBM staff estimates and forecasts

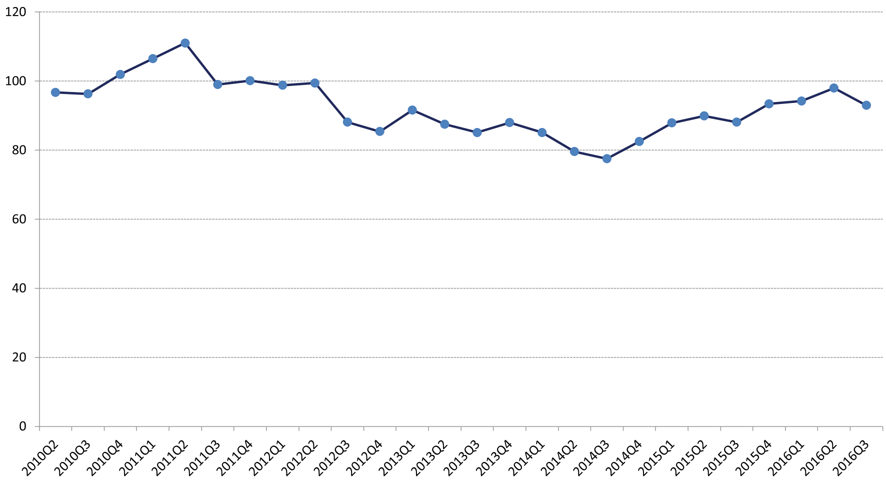
NOTWITHSTANDING MULTIPLE THREATS, GROWTH PERFORMANCE IS PROJECTED TO IMPROVE GOING FORWARD IN THE LIGHT OF RECENTLY ANNOUNCED INITIATIVES

Looking ahead, several challenges prevail. Whereas the performance in key export markets post the UK referendum vote has mostly surprised on the upside, concerns of a hard Brexit, with adverse repercussions on both the UK and the euro area, have not been entirely allayed. Thus, the risks to the Mauritian economy that were elaborated in the July 2016 issue of SBM Insights – reduced demand for exports of goods and services, deterioration in terms of trade, tempered investment due to heightened uncertainty and potential loss in relative trade preferences, among others – still loom. Besides, forthcoming changes in international taxation, including the Double Taxation Avoidance Agreement between Mauritius and India and, at a further horizon, the Common Reporting Standards, are likely to adversely impact the Mauritian Global Business sector, particularly with regard to equity investments from Mauritius into India, and related activities. Another area of concern relates to the planned abolition of the EU sugar quota regime in September 2017, which portends more restrictive market access.

Notwithstanding these threats, we anticipate an improvement in the growth performance going forward, underpinned – inter alia – by far-reaching initiatives announced in the National Budget 2016-2017. Primarily, measures to upgrade public infrastructure and to ease the business environment, for instance, by removing restrictions in respect of the foreign market and by providing incentives for property development and acquisition, are likely to contribute to reversing the downward trend in the construction sector, albeit with a lag. Whereas a contraction in the construction industry is still anticipated for 2016 on the back of the poor first half outcome, the sector is expected to post a robust expansion rate of some 6% in 2017, after several years of declining output (see our special report on construction at pages 24 to 31 for a more in-depth analysis).

By the same token, accommodation and food services activities should benefit from renewed buoyancy in tourist arrivals, on the strength of a heftier marketing and promotion budget and, importantly, enhanced air access policy, which has already translated in increased seat capacity. In Q3 2016, tourist arrivals increased by 9.2% year-on-year, with the number of visitors from the UK and other European markets going up by 11.5% and 18.7% respectively, alleviating immediate fears of a downturn post the Brexit vote, although longer term effects are yet to be ascertained. Moreover, seat capacity should increase further with an expansion of the fleet for the national carrier as well as new airlines coming into operation on the Mauritius route. Against this background, and on the basis of current trends, we expect that the accommodation and food services and transportation sectors to maintain robust growth rates in 2016 and 2017. Looking further forward, the positioning of Mauritius as a hub in the Africa-Mauritius-Singapore-Asia Air Corridor is also a laudable initiative which, if well implemented, should support the hospitality sector, as well as transportation

Figure 2.2: MCCI Business Confidence Indicator



Source: Mauritius Chamber of Commerce and Industry (MCCI)

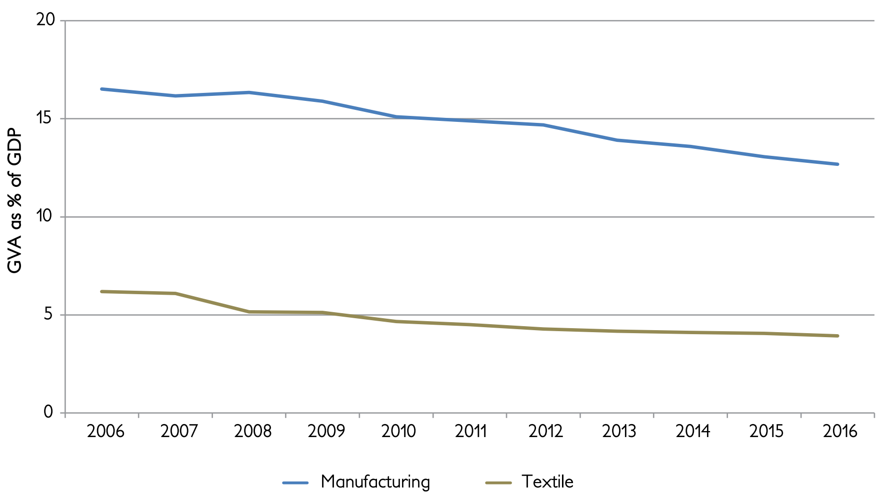
and logistics. In the same breath, Mauritius has the potential of becoming a cargo-hub between Asia and Africa due to its geographical location and dual COMESA / SADC membership.

Regarding the business and financial services sector, whereas the toughening of the operating environment represents a daunting prospect, incentives provided in the Budget should help mitigate the impact on growth through product and market diversification. For instance, the budgetary measure of developing Mauritius as a Renminbi hub for Africa would further strengthen the positioning of Mauritius as an international financial center over the long term, especially in capturing the trade, investment and financial flows between Africa and Asia. Ongoing overseas expansion initiatives of domestic players would also help strengthen the sector.

Similarly, the information and communication sector is expected to sustain an appreciable growth momentum, supported by plans to upgrade the ICT infrastructure – through initiatives such as the 'Third Undersea Cable' project and 'Fibre-To-The-Home programme' – and promote e-services, at both public and private sector levels. We believe that the increase in the country's connectivity and bandwidth would be a stepping stone for achieving further inroads towards a fully digital economy and smart living (Refer to the special report in the March 2016 edition of SBM Insights for a further discussion on the topic), which would act as a catalyst for growth in the ICT sector as well as in the economy in general through enhanced productivity.

On the flipside, manufacturing activity is expected to remain feeble over the forecast period and its share in total output is projected to maintain a downward trend. Already, in July and August 2016, exports of goods to the UK declined by 26% and 10% respectively compared to the same period in 2015. Worryingly, the outlook could be further worsened should a "hard Brexit" profile ahead. In addition to a weakening of demand from the UK and, potentially, the euro area, there may be adverse implications about Mauritius' relative trade preferences in respect of access to the UK market. For instance, in the seafood sector, where the UK market accounted for some 30% of total domestic exports in 2015, the current duty free regime could be replaced by the rates of 20.5%-24% currently applied under the Generalized Systems of Preferences (GSP) or Most Favored Nation (MFN) rules. This would significantly erode the competitiveness of Mauritius vis-à-vis countries such as Thailand, Philippines or Indonesia. Relative preferences in the textiles and garments sector could also worsen.

Figure 2.3: Manufacturing GVA as a share of GDP



Source: Statistics Mauritius

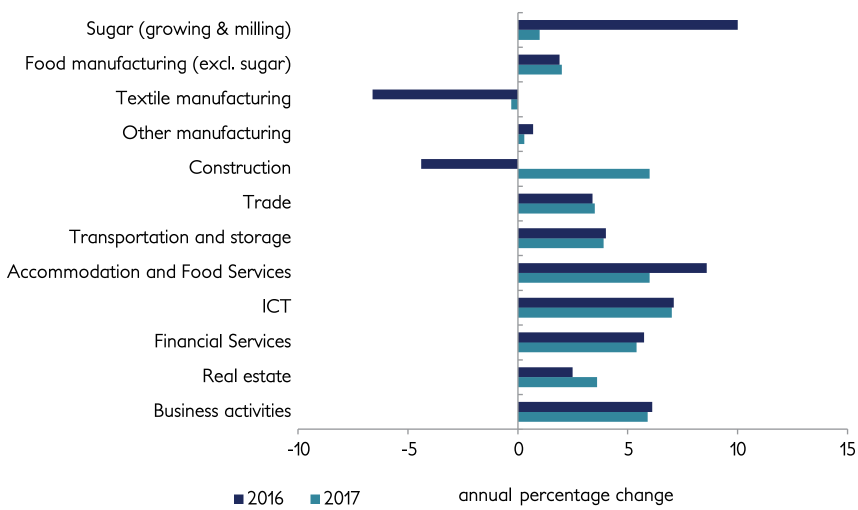
Given that the manufacturing sector contributes significantly to exports and employmentthere is an urgency to conduct an in-depth study on the sector to probe into the causes of underperformance, and identify ways to boost productivity. For example, it may be beneficial over the long term to ease restrictions on the import of skilled labor so as to curb the delocalization of operations to cheaper geographies. At the same time, appropriate measures to increase the contribution of the 'blue economy' and the 'green economy'would be identified. The study findings would complement the laudable initiatives taken in the Budget to diversify the manufacturing base, and should help rekindle growth in the sector in the medium term. In parallel, diplomatic efforts should be stepped up and refocused with the aim of safeguarding the country's interests and identifying areas for expansion. In this respect, Mauritius could take advantage of the renewed discussions on the Comprehensive Economic Cooperation and Partnership Agreement (CECPA) and Preferential Trade Agreement (PTA) with India to identify opportunities for tapping into this fast growing market.

On a brighter note, the sugar sector growth forecast has been revised upwards on the basis of an improved local sugar production and extraction rate in 2016 as well as an expected increase in the quantity of refined sugar produced out of imported raw sugar. Nonetheless, the expansion rate in 2017 should normalize in view of base effects, on the basis of similarly favorable climatic conditions as this year. Moreover, market access developments require close monitoring, especially in view of the intensified competitive environment, namely in the context of the abolition of the EU sugar quota regime anticipated for 2017.

The trade sector, for its part, should continue to post moderate, albeit resilient, expansion rates in line with growth in consumption.

On the whole, whereas Budget proposals have enhanced growth prospects going forward, the impact will mostly be felt as from 2017, taking into consideration the lead time in the execution of projects at both public and private sector levels. Hence, our growth projections for 2016 have remained unchanged at 3.4%, which is 30 basis points lower than the revised forecast of Statistics Mauritius. On the other hand, our prognosis for 2017 has been upgraded, with a growth rate of 3.9% now forecast, that is, 50 basis points higher than the July 2016 figure. The upward revision is mainly attributable to an enhanced investment outlook translating primarily into an upturn in the construction sector, as well as increased resilience to shocks now anticipated in several other sectors in the light of recent policy orientations, as discussed above.

Figure 2.4: Projected real growth rates of the key sectors of Mauritian economy



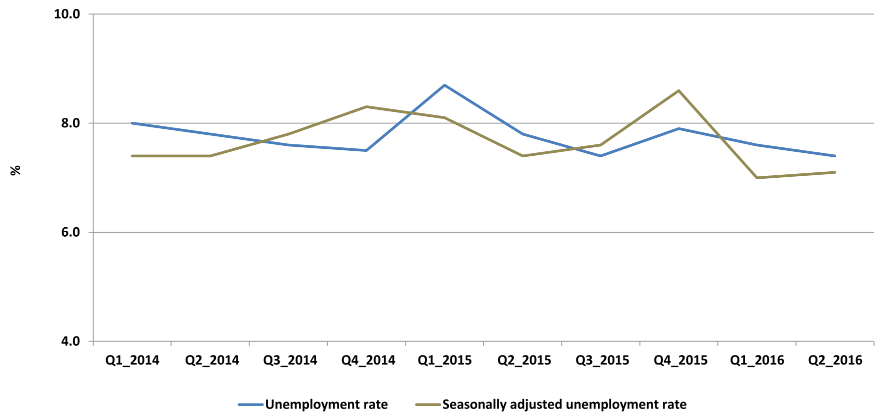
Source: SBM Staff Forecasts

Risks to the growth outlook abound, but are fairly balanced. A worse than expected performance in key markets and delays in the implementation of budget proposals, especially infrastructure and construction projects, could temper the recovery. On the other hand, a prompt execution of announced projects, in both the public and private sectors, may push growth on a higher path. Moreover, measures to consolidate and supplement initiatives taken to encourage foreign talent and wealth into the country would also help support growth.

DECLINING UNEMPLOYMENT RATE IN SPITE OF DIFFICULTIES IN JOB-HEAVY SECTORS

Labor market conditions showed marked signs of improvement in the second quarter of 2016, with an unemployment count of 43,100, lower by 2,900 as compared to Q2 2015. The jobless rate thus declined by 40 basis points year on year to 7.4% in Q2 2016. On a seasonally adjusted basis, the unemployment rate increased marginally from 7.0% in Q1 2016 to 7.1% in Q2 2016.

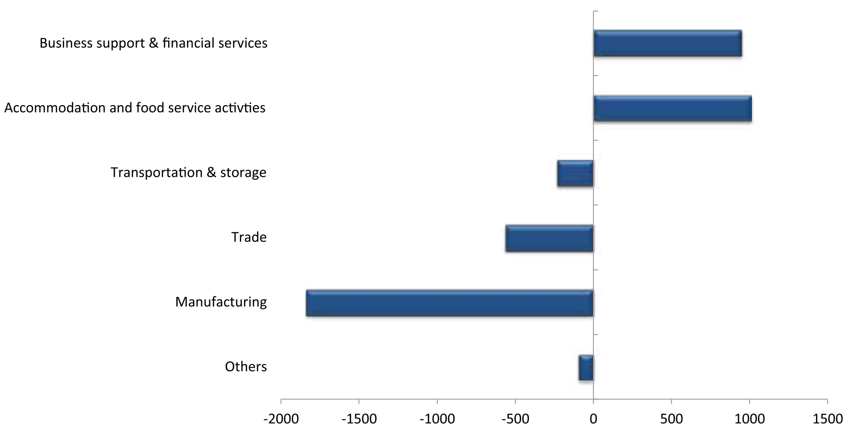
Figure 2.5: Unemployment trend



Source: Statistics Mauritius

The improvement in the unemployment rate has been largely driven by better performances in services sectors such as tourism and financial services, as highlighted in March 2016 data on employment in large establishments. On the other hand, the net contribution of the manufacturing sector to the job count has maintained a declining trend in line with difficulties therein.

Figure 2.6: Change in employment in large establishments across sectors (March 2015-March 2016)



Source: Statistics Mauritius

On the basis of current trends, and taking into consideration that employment tends to be seasonally higher in the second half, it is expected that the unemployment rate would improve to 7.4% in 2016, that is, 50 basis points lower than in 2015. Whereas the improvement in the labor market situation is commendable, concerns persist around specific areas such as high youth and female unemployment – of 24.9% and 10.9% respectively in Q2 2016 – relatively low labor force activity rate of some 60%, and industry-specific challenges, particularly in agriculture and manufacturing.

In this respect, it is encouraging to note that the National Budget 2016/2017 has laid significant emphasis on reducing unemployment. Besides direct employment creation initiatives, the Budget comprises a number of measures to support training and employability, notably through the National Skills Development Programme, which would already be operational in November 2016. The strengthening of the institutional framework – through the creation of a National Employment Agency and a Skills Development Authority as well as the reinforcement of the legal setup for technical and vocational education and training – is also an important step forward.

Against this background, and considering anticipated recovery of the construction industry as well as sustained solid growth in services, the unemployment rate is expected to improve further to 7.2% in 2017. Delays in the implementation of announced measures could, however, postpone the decline in unemployment.

RISING COMMODITY PRICES WOULD PUT PRESSURE ON INFLATION AND EXTERNAL BALANCES GOING FORWARD

Low commodity prices and a stable Mauritian rupee have reined in inflationary pressures, limiting the erosion of the purchasing power of households as well as sustaining the viability of certain delayed investment projects. Headline inflation, as measured by the change in the 12-month moving average of the Consumer Price Index, pursued a downward trend to stand

at 0.8% in September 2016, compared to 1.3% as at December 2015. However, with commodity prices now expected to pursue an upward trend on average, and considering price hikes in some products following the Budget, the inflation rate is expected to slightly pick up going forward, but should remain in the low single digits at 1.2% as at December 2016 and 2.0% as at December 2017.

Similarly, imports are now expected to be higher than previously anticipated on the basis of latest projections for international commodity prices. The forecast pickup in investment activity is also likely to weigh on the import bill, given a relatively high foreign content in some construction materials, machinery and equipment. The effect on external balances would be compounded by subdued manufacturing exports in view of pressures on demand from key markets, in particular the UK, and potentially the euro area, which accounts for a bigger share of the country's exports of goods and services. Thus, the evolution of demand from these key markets, and the movement of their respective currencies, need to be closely monitored. On a brighter note, projected strong tourism receipts and anticipated increase in grants would provide some relief to the external balances. Overall, the current account deficit is expected to widen slightly to 5.1% of GDP in 2016 and 5.9% of GDP in 2017 (2015: 4.8% of GDP).

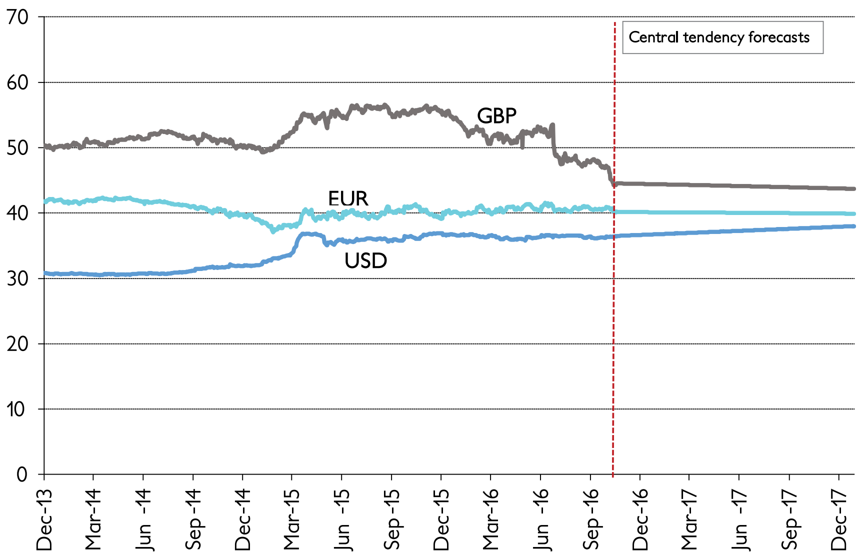
Net financial inflows should nonetheless be sustained at robust levels, supported by the global business sector as well as net inward foreign direct investment. Indeed, foreign direct investment into Mauritius (excluding flows related to the global business sector) contributed MUR 5.2 billion to the financial account on a net basis in the first half of 2016, 76.4% up from the corresponding period in 2015, supported by continued strong investment in real estate.

On this basis, the balance of payments is expected to maintain a surplus position in 2016 and 2017. Looking further forward, the sustainability of financial inflows would be subject to significant risks relating to the global business sector, due to potential changes in international taxation such as the Common Reporting Standards and revision of the Double Taxation Avoidance Treaty between Mauritius and India.

The movements in the rupee exchange rate reflect developments in the major currency markets. As at September 2016, the rupee appreciated by 14.4% vis-à-vis the Pound Sterling but depreciated by 0.4% and 0.1% against the US dollar and euro respectively, compared to a year ago. In nominal effective terms, the rupee as measured by the MERI2, obtained through the currency distribution of merchandise trade and tourism earnings, depreciated by 0.4% between August 2015 and August 2016.

Reflecting the external position, the MUR is projected to remain relatively stable on an annual average basis. The evolution against individual currencies will depend on currency markets, with the MUR expected to have a downward bias vis-à-vis the USD and an upward bias versus the GBP. Nonetheless, on account of multiple risk factors, exchange rates would face significant volatility.

Figure 2.7: Exchange Rate of MUR vis-à-vis major trading currencies



Source: SBM Staff Forecasts

POLICIES SHOULD REMAIN BROADLY ACCOMMODATIVE …

Against the background of weak economic activity, following the Brexit vote and the forthcoming US Presidential November Elections, among others, the Monetary Policy Committee of the Bank of Mauritius slashed the Key Repo rate by 40 basis points to 4% with the objective of boosting investment activity in the country and raising the growth potential of the economy. Pending solid economic recovery, the policy rate is expected to remain low, around the current level.

Fiscal policy would also remain supportive of economic activity, with a planned increase of 12.9% in compensation of employees, in line with additional recruitment in the public sector, and a massive 67.4% boost in acquisition of non-financial assets (mostly infrastructure expenditure). Notwithstanding the increased spending, the budget deficit is projected to decline from 3.5% of GDP in fiscal year 2015/16 to 3.3% of GDP in 2016/17, taking into consideration of an increase of more than MUR 6 billion in external grants, emanating mainly from the Government of India. Public sector debt stood at 65.0% of GDP as at June 2016, and is expected to decline to 62.8% of GDP in June 2017. For the purpose of the statutory debt ceiling, public sector net debt as a percentage of GDP stood at 55.6% as at June 2016 and is projected to remain at the same level in June 2017. On current trends, the objective to reduce this ratio to the statutory debt target of at most 50% of GDP by 2018 seems challenging, and would require considering alternative measures.

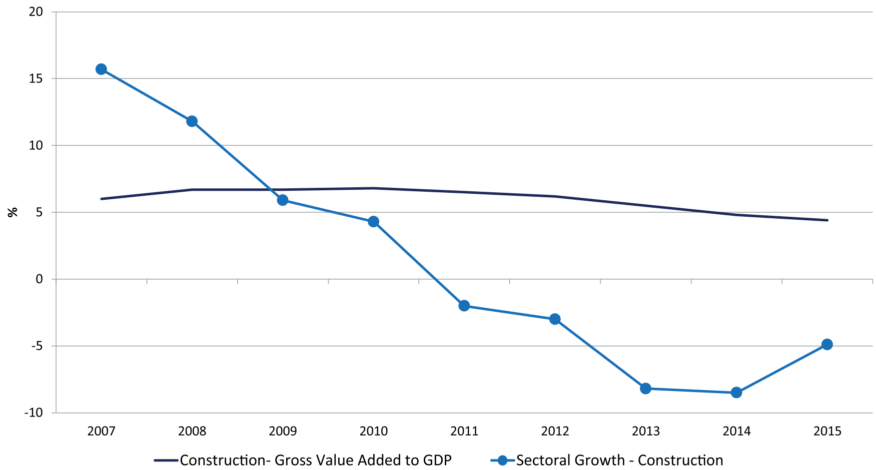
CONSTRUCTION SECTOR: AT A CROSSROADS

HIGHLIGHTS

- The construction sector has been facing difficult conditions since some years, in line with a decline in investment in building and construction works.
- Investment in non-residential buildings has declined sharply since 2010, and has been the main cause for the decline in investment and construction works and, thus, of the construction sector.
- The drop in investment is largely attributable to a significant contraction in accommodation and food service activities, as hotel construction stalled post the global financial crisis.
- There has also been a decline in the number of non-residential permits issued as well as the decrease in floor area.
- Investment in residential buildings is expected to gain momentum in 2017 on the back of measures to boost home ownership within various income classes.
- Mixed signals persist with regard to investment in non-residential buildings, although an overall increase is anticipated in view of renewed interest in hotel development in particular.
- Investment related to other construction works is also expected to go up as a result of increased public spending to enhance the infrastructure setup in various areas.
- Overall, there is a strong likelihood that investment in building and construction works, and by extension activity in the construction sector, will recover as from 2017, albeit subject to multiple risk factors.

The construction sector has been facing difficult conditions since some years. Although the sector experienced good growth momentum at 5.9% in 2009 and 4.3% in 2010, it has subsequently followed a downtrend, contracting in every single year since 2011. As a result, the contribution of the construction sector to the economy has dropped from 6.8% in 2010 to 4.4% of GDP in 2015, and is expected to decline further this year, considering a poor first half performance. The value added by the sector amounted to MUR 16 billion in 2015 at current basic prices.

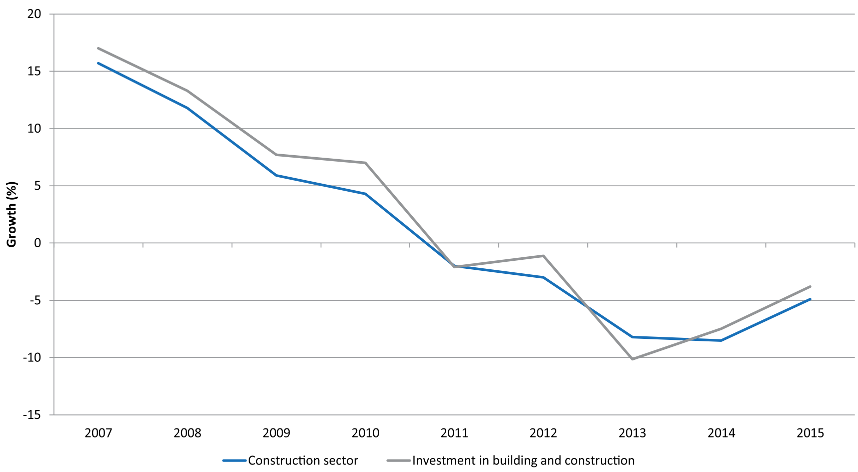
Figure 3.1: Construction sector in Mauritius



Source: Statistics Mauritius

As highlighted in Figure 3.2, the decline in construction activity is highly correlated to the pattern in investment in building and construction works.

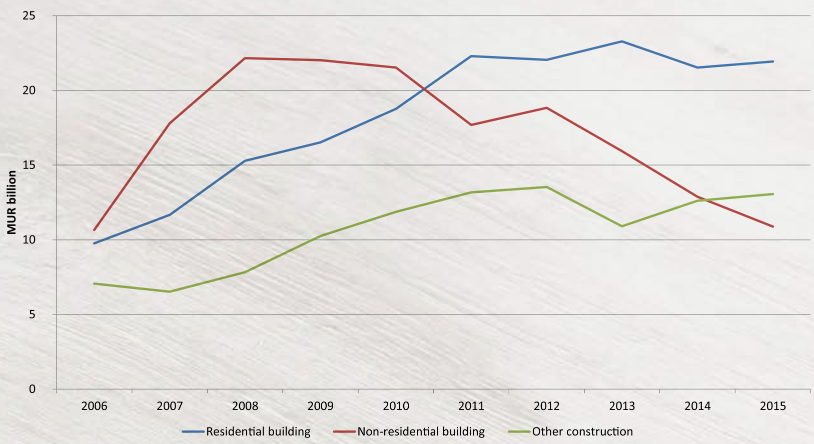
Figure 3.2: Correlation between construction sector and investment in Building and Construction works



Source: Statistics Mauritius

The investment in building and construction works can be broken down into 3 main components: residential, non-residential and other construction works. As shown below, each of these three has followed a specific trajectory over the years.

Figure 3.3: Investment by type



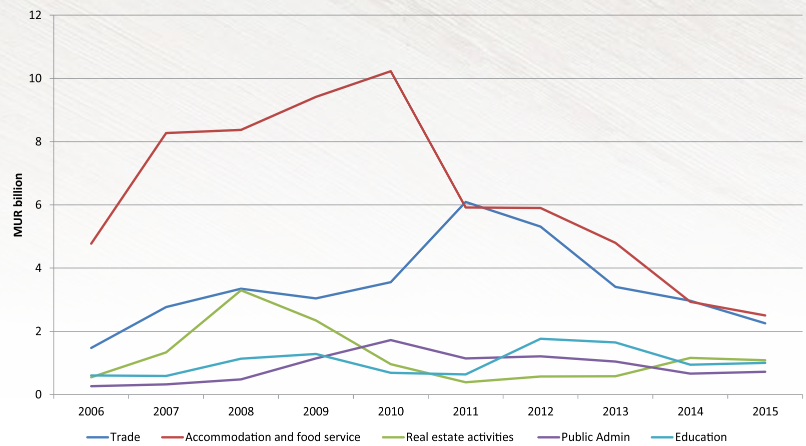
Source: Statistics Mauritius

Whereas investment in residential buildings (mainly the household segment) and in other construction works (principally linked to public infrastructure) has been resilient over the years, albeit progressing at a slower pace in recent years, investment in non-residential buildings has declined sharply since 2010, and has been the main cause for the decline in investment and construction works and, thus, of the construction sector.

A further breakdown by industrial activity, as shown in Figure 3.4, indicates that the drop in investment is largely attributable to a significant contraction in accommodation and food service activities, as hotel construction stalled post the global financial crisis. Similarly, the trade sector faced declining investment in commercial space linked to the perception of oversupply in the segment.

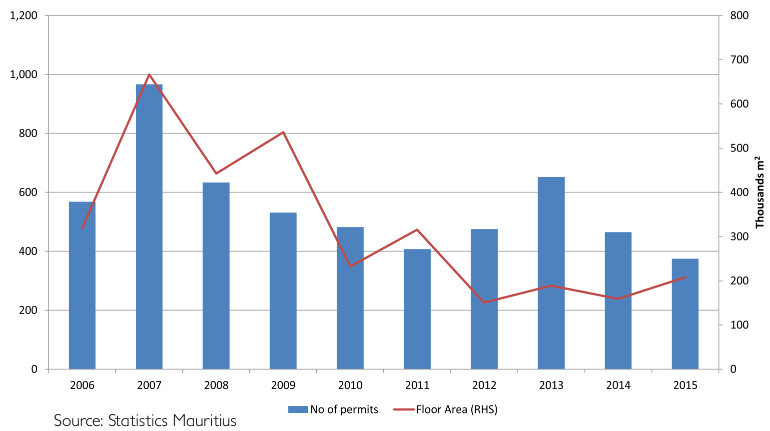
The underperformance in investment in non-residential buildings is also reflected in the decline in the number of non-residential permits issued as well as the decrease in floor area, as depicted in Figure 3.5.

Figure 3.4: Non-residential investment by sector



Source: Statistics Mauritius

Figure 3.5: Number of issued non-residential permits

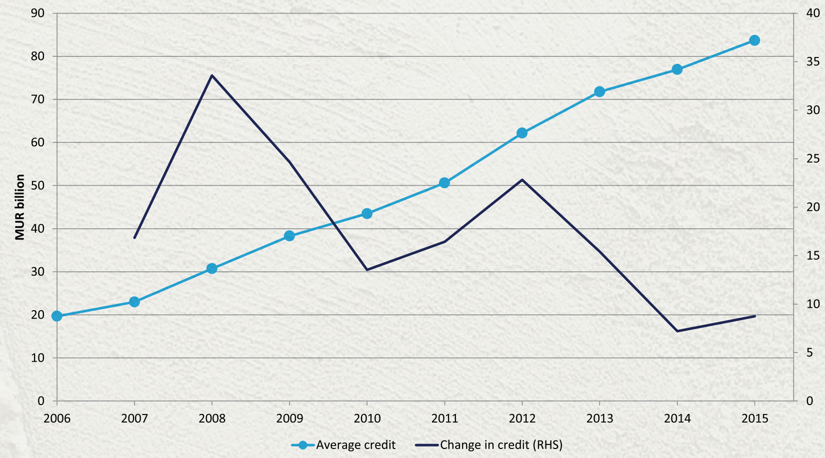


Source: Statistics Mauritius

STATISTICS ON CONSTRUCTION SECTOR

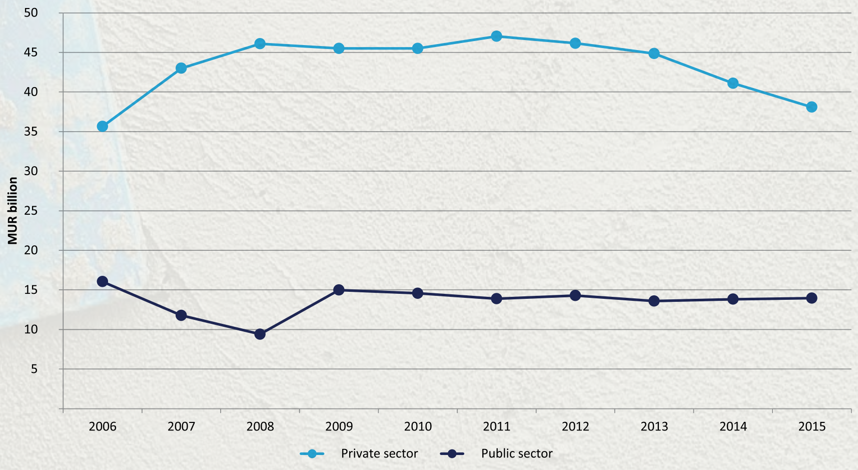
Alongside the dwindling contribution to the economy, credit given by banks to the construction sector has also pursued a decelerating, albeit positive growth trend.

Figure 3.6: Credit to construction sector



Source: Bank of Mauritius

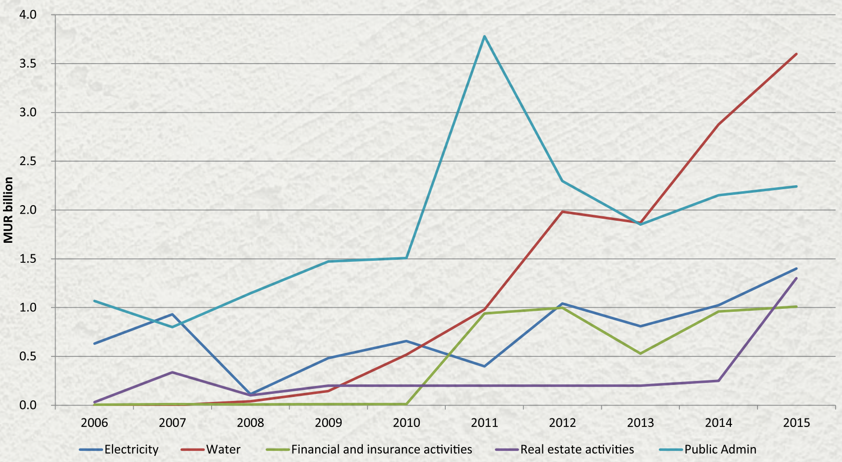
Figure 3.7: Investment by sector



Source: Statistics Mauritius

Figure 3.7 depicts the trend in public and private investment. Private sector investment has declined by 19% since a peak of MUR 47 billion in 2011. On the other hand, public sector investment has remained stable at MUR 14 billion per year. Meanwhile, total investment as a share of GDP has fallen by 32% since 2009.

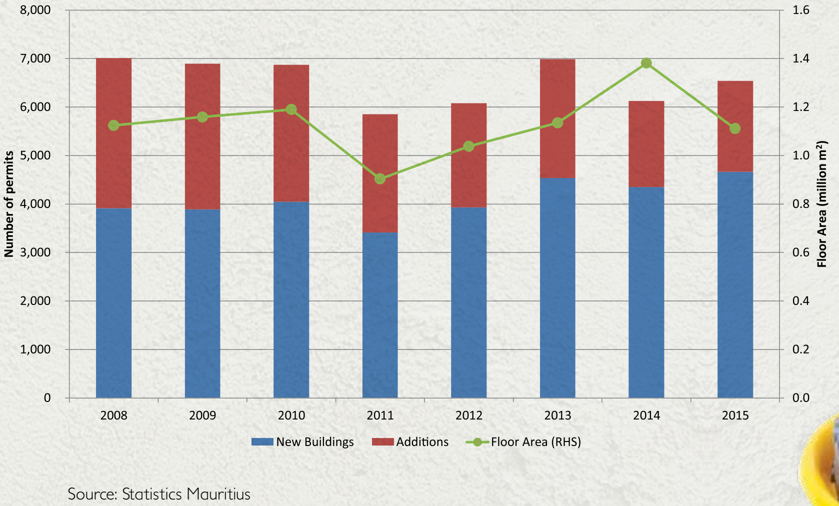
Figure 3.8: Investment in other construction works by sector



Source: Statistics Mauritius

The number of permits allocated for residential buildings has remained stable over the years. Nevertheless, the floor area has risen indicating that investment in residential buildings is focused more on quality rather than quantity.

Figure 3.9: Number of issued residential permits



Source: Statistics Mauritius

UPTURN EXPECTED IN 2017 ON THE BACK OF BUDGET INCENTIVES AND INFRASTRUCTURE DEVELOPMENT

Investment in residential buildings is expected to gain momentum in 2017 on the back of measures to boost home ownership within various income classes, as well as to enlarge the market through an easing of constraints in respect of ownership by foreigners. This is particularly pertinent given that growth in the number of households has considerably slowed and is expected to stall in the years ahead.

As regards investment in non-residential buildings, which pertains mainly to the business segment, mixed signals persist. On the one hand, following continued positive performance in the tourism sector, hotel projects, including renovations, are expected to pick up. Encouragingly, interest in real estate projects is also firming up further to the incentives provided in the budget. Private investment in universities and health centers could also increase, albeit at a lower magnitude, in line with efforts to promote the education and wellness hub (also see the annex on pg 31). On the other hand, investment in industrial and commercial space should remain lacklustre given subdued prospects in manufacturing and trade. On the whole, an upturn is expected in 2017 from prior year lows, although high levels of uncertainty, notably linked to global risks, could temper investor confidence.

Besides, investment related to other construction works is also expected to go up as a result of increased public spending to enhance the infrastructure setup in various areas, including water, energy, port development and land transportation, as shown in table 3.1 below. However, project implementation requires close monitoring in view of delays being typically experienced in public infrastructure projects.

Table 3.1: Planned expenditure in public infrastructure

Figures in MUR million	2015/16 Provisional Actual	2016/17 Estimates	2017/18 Planned	2018/19 Planned
Water Projects	1,388	3,505	3,402	2,676
Sewerage	370	805	1,618	1,215
Roads & Drains (incl. Metro Express)	442	4,821	4,295	4,035
Energy	3,194	8,990	10,220	7,627
Port Development	1,786	3,096	1,761	350
Air Transport	54	691	182	23

Source: Public Sector Investment Programme 2016-17 – 2020-21, Ministry of Finance and Economic Development

Overall, there is a strong likelihood that investment in building and construction works, and by extension activity in the construction sector, will recover as from 2017, albeit subject to multiple risk factors.

ANNEX

Residential buildings

Segment	
Lower cost housing segment	• VAT Refund on construction of a new dwelling or acquisition of a newly built apartment up to a cap of MUR 500,000. The builder need not be VAT registered. There are no eligibility criteria for floor area. Construction value has been reviewed on the rise from MUR 2.5 million to MUR 4 million.
	• No registration duty on secured housing loan up to a maximum value not exceeding MUR 2 million.
Middle to upper range housing segment	• Exemption from payment of registration duty on acquisition of a new house or a new apartment for an amount not exceeding MUR 6 million over the period 01 September 2016–30 June 2020
	• Promoters/Developers will be exempted from payment of land transfer tax on sale of residential units valued up to MUR 6 million till 2020
Foreigners	• Occupation Permit for non-citizens made easier
	• Eligibility for non-citizens who have been granted a permanent residence permit to purchase an apartment for personal residence
	• Review of the Property Development Scheme, removing restrictions on the maximum extent of land for development of a project, and the % of residential units that can be sold to non-citizens
	• Use of land conversion rights obtained under the SIE Act in Smart City projects allowed on an apportioned basis

Non residential buildings

	Drivers	Challenges
Industrial	• New manufacturing segments being promoted in the Budget	• Industrial activity expected to remain tepid • Number of active manufacturing enterprises on a downward trend
Commercial	• Increased tourist arrivals • New "foreign" segment promoted by openness policy • Duty-free island concept	• Perception of persisting excess supply in the commercial space
Hotels	• Tourist arrivals expected to remain buoyant • Increased margins by hotel operators • Moratorium on hotels lifted • Planned renovations	• Uncertainties generated by Brexit
Office	• New "foreign" segment promoted by openness policy • Incentives in the financial services sector	• Threats to the Global Business sector due to changes in global taxation
School and hospitals	• Education and wellness hub concept • Ageing population	• Slow growth in youth segment

SOUTH AFRICA: THE RAINBOW NATION

HIGHLIGHTS

- Located at the southern tip of Africa, the Republic of South Africa is one of the largest economy of the continent.
- It is currently considered as one of the most advanced African countries and is the top producer of platinum in the world and counts among the leaders for gold production and diamond extraction.
- South Africa drafted a National Development Plan 2030 in 2011 to eliminate poverty and reduce inequality in the country.
- Various initiatives have been earmarked to achieve these goals, including: increasing the share of renewable energy; expansion of regional trade and exploratory drilling for gas.
- Currently, the manufacturing, transport and government services sectors are other important pillars of the economy.
- The South African economy registered average annual economic growth of 1.9% over the period 2012 to 2015.
- A decline in global demand, driven by China, for South Africa's main exports (platinum, gold and other metals) and the subsequent fall in prices of commodities have negatively impacted the nation during 2015.
- The central bank has significantly tightened monetary policy recently with four rate hikes since mid-2015, namely in July 2015, November 2015, January 2016 and March 2016.
- GDP in South Africa is projected to remain flat in 2016 with a marginal growth of 0.1%. The difficulties that the economy faced in 2015 are expected to continue in 2016.
- Mauritius and South Africa already collaborate in many areas.
- Opportunities for Mauritian firms in South Africa are mainly in the financial services and manufacturing sectors.

BACKGROUND

Located at the southern tip of Africa, the Republic of South Africa is one of the largest economy of the continent. It is home to around 54 million people and the country is bordered by Botswana, Lesotho, Mozambique, Namibia, Swaziland and Zimbabwe. Its political capital is Pretoria. Owing to the diverse nature of its population, South Africa is often termed as the "Rainbow Nation". This multiversity is reflected in its culture with 11 official languages recognized by the authorities. The population is mostly made up of Sub Saharan Africans while people of Asian and European origins also constitute a sizeable proportion of the population.

After having undergone periods of severe instability, especially with Apartheid, South Africa has gone from strength to strength and is currently considered as one of the most advanced African countries. It is the top producer of platinum in the world and counts among the leaders for gold production and diamond extraction.

POLITICAL ENVIRONMENT

South Africa is considered a parliamentary republic with 9 administrative provinces. The country's legislative capital is Cape Town. The President is both the Chief of State and Head of Government and is indirectly elected by the National Assembly for a 5-year term. The current President of South Africa is Jacob Zuma and new elections will be held in 2019. The Rainbow Nation has had to go through many ups and downs to achieve the current political environment whereby every South African can vote indistinct of color or race. Indeed, the country was subject to Apartheid for a very long time. In 1936, an act was passed to prevent people of color to vote in ordinary elections. This segregation was further reinforced by the National Party which came to power in 1948. Under this situation, white minority rule was maintained while rights of the majority black population was restrained. There were many scenes of violence and wars during the Apartheid period. This continued until the 1990s when steps were taken to erase Apartheid. The latter was dismantled through a series of negotiations between 1990 and 1993 and subsequently, the first general elections with universal suffrage were held in 1994. Nelson Mandela was chosen as the President of the country and three Presidents have succeeded him. The country has been relatively peaceful except for the occasional bout of violence. There has recently been some unrest in South African universities owing to conflict over tuition fees, shortages of student accommodation, low-paid staff and the language of instruction. Underlying youth anger are the legacies of racial discrimination and colonialism, high levels of unemployment and pronounced and increasing income inequality. Workers from the mining sector have also protested at times due to loss of jobs and some mining sites shutting down. Nevertheless, the country is one of the most stable on the African continent.

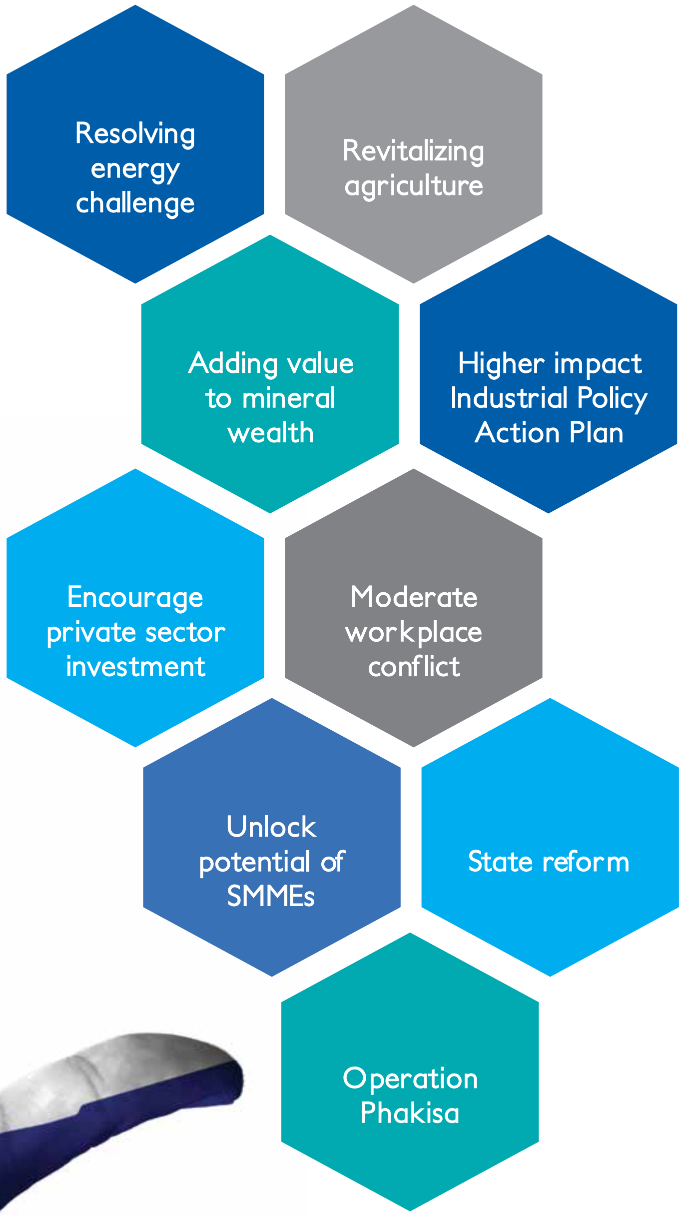
LONG TERM STRATEGY

Following slow economic growth post the global financial crisis in 2009, South Africa drafted a National Development Plan 2030 in 2011. The aim behind this plan is to eliminate poverty and reduce inequality in the country. The plan identifies six interlinked priorities to achieve this namely achieve prosperity and equity, promote active citizenry, faster economic growth and investment, focus on key skills, build a capable state, and encourage strong leadership.

Macroeconomic objectives enunciated in the plan include reducing the unemployment rate to 6% in 2030 and increasing Gross Domestic Product by 2.7 times by 2030. Various initiatives have been earmarked to achieve these goals, including: increasing the share of renewable energy; expansion of regional trade and exploratory drilling for gas. To this effect, the Medium Term Strategic Plan (MTSP) 2014-2019 was announced in 2014. However, it did not have the expected impact. This strategic plan has been brought to the fore again recently and it is expected to help implement aspects of the NDP for which the government is responsible till 2019. Under this plan, the President has signed performance agreements with every Ministry to hold them accountable.

In parallel, the President has announced a Nine Point Plan for the economy. The aim behind this plan is to create jobs and boost the economy, both through consolidation of the existing base and through the development of new sectors. The government is aiming to ensure a stable supply of electricity for the population and businesses through the improvement of maintenance practices and operations at Eskom – the national electricity firm. In the same vein, support for small farmers will be increased so as to boost agricultural activities. Plans have also been drawn up to safeguard jobs in the mining sector and revitalize the manufacturing sector. State reforms will also be undertaken alongside incentives for the private sector so as to increase efficiency and improve services. The last plan is the ambitious "Operation Phakisa".

Figure 4.1: South Africa's Nine Point Plan

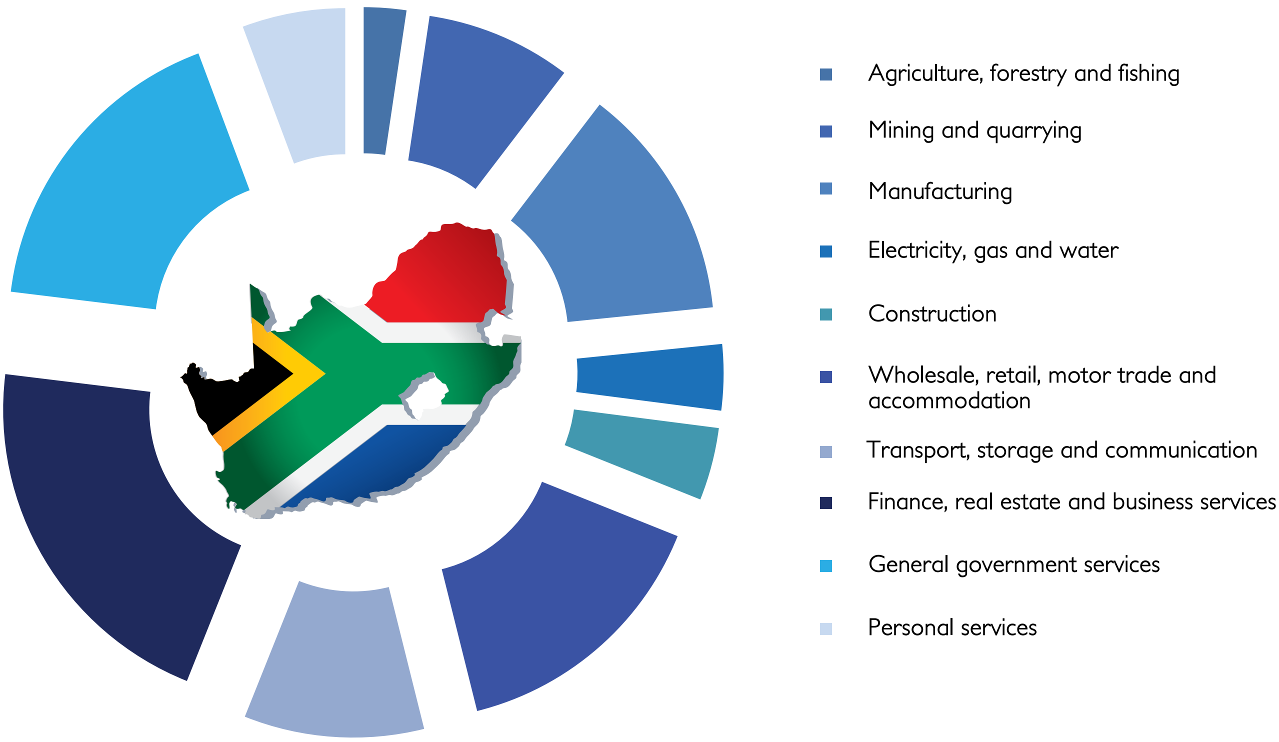


"Operation Phakisa" is a cross-sector programme where various stakeholders engage to implement initiatives and concrete actions to address constraints to delivery in a prioritized focused area for Public accountability and transparency. This has already been tested in the ocean economy, health, ICT in education and is currently being tested in the mining sector. A ZAR 9 billion investment in rig repair and maintenance facilities at Saldanha Bay is planned, and work has begun on a new gas terminal and oil and ship repair facilities at Durban.

ECONOMY

Sectoral contribution to GDP reflects the fact that South Africa is a resource rich country alongside being one of the most advanced countries in the continent. Indeed, for the financial year 2015, the primary sector (agriculture, forestry and fishing, mining and quarrying) contributed around 10% to GDP while financial services and wholesale and retail trade contributed more than a quarter. The manufacturing, transport and government services sectors are other important pillars of the economy. Together, these seven sectors represent over 85% of GDP.

Figure 4.2: Sectoral contribution to the economy, 2015



Source: StatsSA

Economic review

Table 4.1: Selected macroeconomic indicators

Selected Macroeconomic Indicators	Unit	2012	2013	2014	2015	2016(f)	2017(f)
GDP, constant prices	% change	2.2	2.3	1.6	1.3	0.1	0.8
GDP, current prices	USD billion	396	368	352	315	280	288
Population	million	52.4	53.2	54.1	55.0	55.9	56.8
GDP per capita, current prices	USD	7,570	6,914	6,503	5,727	5,018	5,074
GDP per capita in PPP terms	USD	12,593	12,889	13,119	13,209	13,179	13,348
Investment	% GDP	20.0	21.0	20.7	20.7	19.6	19.3
Gross national savings	% GDP	14.8	15.2	15.5	16.4	16.3	16.1
Inflation, average consumer prices	%	5.7	5.8	6.1	4.6	6.4	6.0
Volume of imports of goods and services	% change	4.2	5.0	-0.5	5.3	-0.4	1.4
Volume of exports of goods and services	% change	0.8	3.6	3.3	4.1	0.7	2.7
General government gross debt	% GDP	41.0	44.0	46.9	49.8	51.7	53.3
Current account balance	% GDP	-5.1	-5.9	-5.3	-4.3	-3.3	-3.2

Source: IMF World Economic Outlook Database, October 2016

The South African economy registered average annual economic growth of 1.9% over the period 2012 to 2015. This performance is lower than the regional average of 4.5% over the same period and reflects the difficulties that South Africa has been facing in recent years. The 1.3% economic growth registered in 2015 is the lowest in a decade. A decline in global demand, driven by China, for South Africa's main exports (platinum, gold and other metals) and the subsequent fall in prices of commodities have negatively impacted the Rainbow Nation. This was reflected in export earnings despite an 8.6% increase in volume, a decline in investment as a share of GDP and increased job losses. Many businesses have also closed down. This has worsened the country's unemployment problem. Indeed, South Africa has been grappling with very high unemployment since many years. Around a quarter of its labor force is currently unemployed.

GDP per capita at current prices has been declining over the years especially with a rise in the US dollar. Nevertheless, GDP per capita in PPP terms has increased by around 4.9% since 2012. Government debt has been rising owing to low economic growth. The level of inflation was brought within the central bank inflation band of 3-6% in 2015, from 6.1% recorded in 2014 to 4.6% in 2015. The South African Reserve Bank has adopted an inflation targeting system and the Monetary Policy Committee takes decision after taking into account the rate of inflation. The central bank has significantly tightened monetary policy recently with four rate hikes since mid-2015, namely in July 2015, November 2015, January 2016 and March 2016. Repurchase rates were raised to anchor inflation within the target range and deal with worsening external positions and falling exchange rates.

Figure 4.3: Risk assessment of the South African economy

S STRENGTHS	W WEAKNESSES	O OPPORTUNITIES	T THREATS
• One of the largest economy in Africa • Strategic position • High literacy rate • Strength of institutions	• High reliance on commodity exports • Low productivity • High prevalence of HIV/AIDS • High cost of labor	• Infrastructure development • Trade with India and China • BRICS Development Fund	• Drop in commodity prices • Climate change • Political tensions and rise in xenophobia

Outlook

GDP in South Africa is projected to remain flat in 2016 with a marginal growth of 0.1%. The difficulties that the economy faced in 2015 are expected to continue in 2016. Low commodity prices, weak export demand, power shortages and reduced agricultural productivity due to drought are expected to continue throughout 2016. Whereas the IMF is projecting a pickup in 2017, growth should remain weak at 0.8%. Against this backdrop, the Fund has highlighted the need to implement structural reforms to boost the economy, namely with regard to competition, labor market policies and industrial relations. Similarly, improvement in efficiency and government policies would improve the outlook.

RATINGS AND RANKINGS

Table 4.2: Latest sovereign credit ratings

Credit Rating Agency	Local Currency Denominated Debt	Foreign Currency Denominated Debt	Outlook
Moody's Investors Service	Baa2	Baa2	Negative
Standard & Poor's	BBB-	BBB+	Negative
Fitch Ratings	BBB-	BBB	Stable

South Africa's debt is currently rated as investment grade. At the latest rating exercise conducted by the three major credit agencies, Moody's Investors Service and Standard & Poor's opted to maintain their local currency debt ratings at Baa2 and BBB- respectively while Fitch Ratings lowered its rating by one notch to BBB-. Alongside local currency debt, foreign currency debt was rated Baa2, BBB+ and BBB. The ratings were supported by the likelihood of a growth recovery beyond 2016, stabilization of government debt ratios and the strength of South African institutions. Nevertheless, Moody's and S&P have issued a negative outlook on the ratings amidst impending challenges. These include low GDP growth trend, significant fiscal and external deficits, high debt levels, heightened political risks, the potential adverse fallout of drought and persisting structural constraints. Moreover, concerns remain about the implementation risks associated with the structural and legislative reforms that the government, business and labor recently agreed in order to restore confidence and encourage private sector investment.

Table 4.3: International rankings

	2013	2014	2015	2016
Ease of Doing Business Report	39th	41st	69th	73rd
Global Competitiveness Index	53rd	56th	49th	
Corruption Perceptions Index	72nd	67th	61st	
Human Development Index	121st	116th	116th	
Index of Economic Freedom	74th	75th	72nd	80th
Global Gender Gap Report	17th	18th	17th	

Source: World Bank, World Economic Foundation, Heritage Foundation, Transparency International

Although South Africa has remained broadly stable in the different rankings since some years, there has been a huge drop in Ease of Doing Business. It should be noted, however, that 2015's ranking is not the published ranking. Rather, it is a comparable one for the published 2015 ranking that captures the effects of factors such as data revisions and changes in methodology. Though consistently ranked among the leaders in Africa, the gap with the overall top ranked countries is still high. Additional actions are needed to bridge the gap. In the same vein, the country has to put in more efforts with regard to Human Development Indicators. Indeed, low life expectancy in the country (57.4 years) brings the country down in the rankings. Nonetheless, South Africa has made steady progress since 2010 when it was ranked 123rd. The rise in HDI ranking over this period is mainly attributed to a rise in life expectancy at birth, expected years of schooling and mean years of schooling. Of note, South Africa scores highly for global gender gap and is consistently ranked in the top 20. The index notes South Africa's efforts in reducing gender disparities based on economic participation, education, health and political empowerment.

PROSPECTS FOR MAURITIUS

Mauritius and South Africa already collaborate in many areas ranging from financial services to trade. The two countries have double taxation avoidance agreements and investment promotion and protection agreements in place. As a result, there is considerable investment flow between South Africa and Mauritius in the global business sector. In the same vein, the Board of Investment of Mauritius has opened an office in Johannesburg to attract additional investments from that country into Mauritius.

Many Mauritian firms already operate in South Africa and vice versa. These firms operate mostly in the tertiary sector including financial services and ICT. Many South African firms have also recently moved to Mauritius to take advantage of untapped potential, for instance in the manufacturing sector. A number of JSE-listed companies also have primary listings in Mauritius, including offshore-focused property funds, which are required to have primary listings elsewhere in order to be allowed a listing in Johannesburg. Another South African firm, Growfish

International Ltd, signed a Memorandum of Understanding (MoU) for collaboration and cooperation in the field of aquaculture with the Ministry of Ocean Economy, Marine Resources, Fisheries, Shipping and Outer Islands in April 2016. The company would invest around MUR 1.4 billion in sea cages, land hatcheries, quarantine facilities, larval husbandry facility, maturation nursery for juvenile fish production and a fish processing facility.

Opportunities for Mauritian firms in South Africa are mainly in the financial services sector. In addition, the measures announced in the Mauritian Budget 2016/17 have provided additional opportunities for local firms. Incentives announced for firms holding specific types of licenses allocated by the Financial Services Commission would open new avenues for business.

Nevertheless, these measures have to be included in the legislation first. In the same vein, the benefits announced for firms engaged in industrial fishing would further encourage firms to set up shop in the country. In so doing, it will also develop the ocean economy, which is one of the key areas of focus for Mauritius. The shared Anglophone heritage of the two countries is also an advantage for Mauritian firms to capitalize on. South Africa is also a major prospect due to its policies for revamping its public health care system. The Mauritian government has announced a Pharmaceutical Village in Budget 2016/17. This village would manufacture pharmaceuticals products for the African continent. Given South Africa's objective, there exists opportunities for Mauritius-based pharmaceutical companies to enter the market.

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