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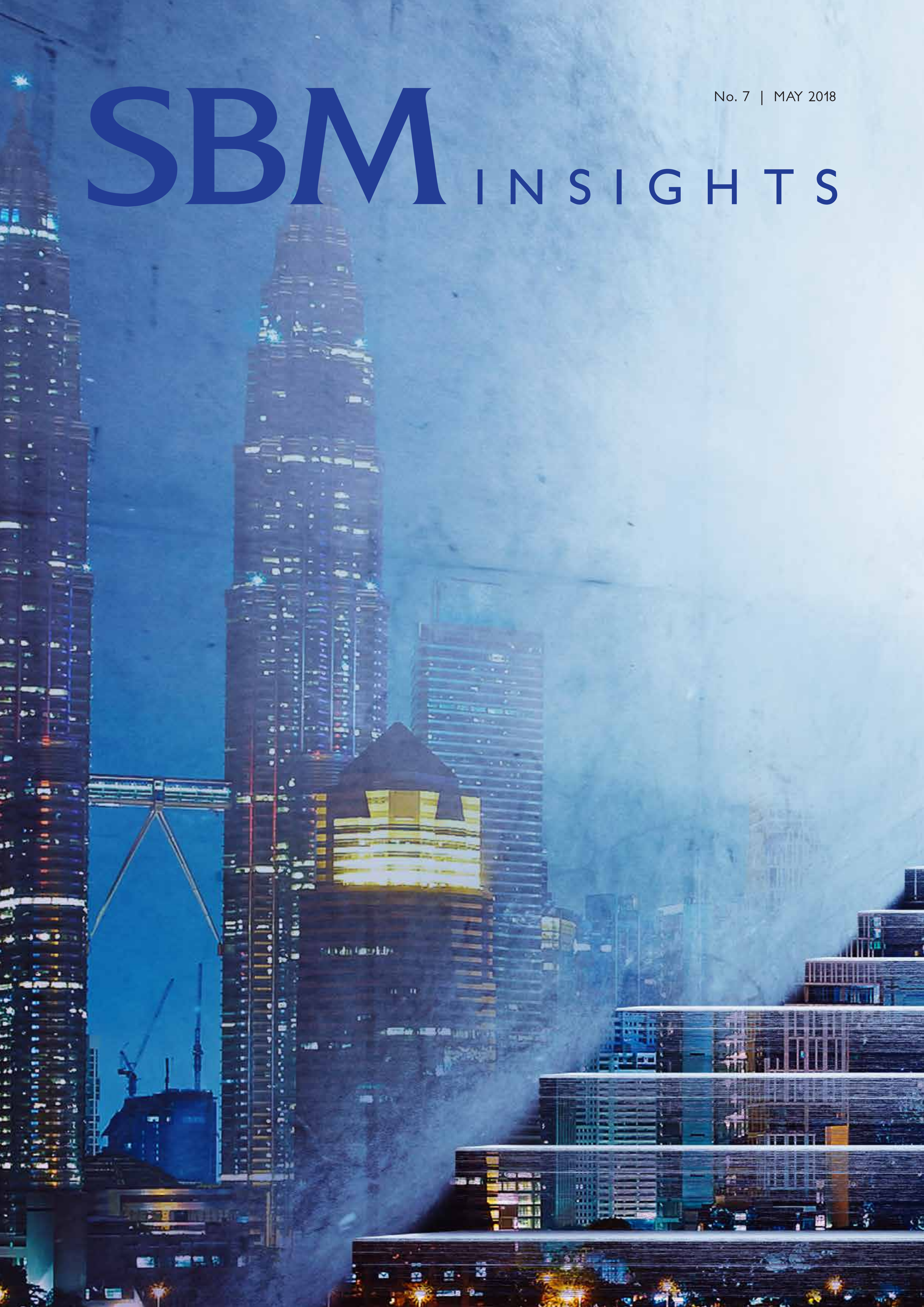
SBM INSIGHTS



FOREWORD BY SBM GROUP CHAIRMAN

Dear Reader,

Two years have elapsed since our first publication of SBM Insights. During that period the global economy has been surfing in and out a difficult environment characterized by volatility, uncertainty, complexity and ambiguity (VUCA). The situation is no different at the moment. Recent events on the global scene seem to remain erratic, constantly adding fuel to the VUCA situation, notably in respect of the political and policy stance. Unexpected changes, at both global and national levels, seem to be the new norm nowadays. The ongoing trade dispute between the world's two largest economies, US and China, is a major cause of concern. Imposing tariffs on a large basket of US and Chinese goods would have a domino effect globally. This would result into retaliation from other developed and developing economies, thus threatening trade flows and ultimately stifling global economic growth. Nonetheless, the economic fundamentals that led the global economy to post the strongest expansion rate since six years in 2017 remain firmly in place. A solid trade cycle, relatively accommodative financial conditions and resilient private consumption in the wake of historically low unemployment rates in most large economies including the US and the Eurozone are strong underpinnings of global economic growth. The sub-Saharan African economy edged up in the final quarter of 2017, as the region's gradual recovery continued - Ghana being one of the star performers. Regional GDP increased 3.2% annually in Q4, above prior month's preliminary estimate of a 3.0% expansion and Q3's 3.0% increase, on the back of higher commodity prices, solid global growth and healthier harvests. Commodity-wise, the price of oil has witnessed an upward trend following geopolitical tensions and OPEC's production cuts. Food prices have also been on a rising trend as a result of adverse climatic conditions, for instance, drought in the US limiting supply of wheat in the wake of increasing global demand. All these factors could potentially disrupt the global economy and have spill-over effects on the domestic economic landscape.

On the domestic front, there have been several developments, some positive and some not-so-positive. On a positive note, the Economic Development Board has now been set up and started operations in January 2018, following the fusion of the Board of Investment, Enterprise Mauritius, the Financial Services Promotion Agency and the Mauritius Africa Fund. The objective of this new entity is to provide strong institutional support for strategic economic planning and ensure coherence and effectiveness in economic policy formulation and implementation that would ultimately drive Mauritius to the high income economy status. As such, we remain optimistic about the execution of public projects in the medium and long terms. The first phase of the much awaited Metro Express project kick started in February 2018. Several smart cities are currently under construction and some are expected to be completed by 2019, providing tailwinds to the construction sector. Both the introduction of the minimum wage and the negative income tax are expected to boost standard of living of the lower income groups, hence stimulating economic growth through increased consumption. Conversely, one of the main concerns remains the rising inflation rate. Cyclones like Berguitta and Fakir caused damage to crops, hence causing a significant rise in the prices of vegetables. Following the recent atypical climatic conditions that have also impacted on tourist arrivals in the first four months of the year, our Economic Research team has revised down its growth rate forecast for 2018 to 3.9%. The team expects the construction sector to be, once again, the key engine of growth.

2017 was another year full of achievements for the Group, several initiatives materialized in line with our strategy. We strengthened our footprint in the African region, after the acquisition of Fidelity Commercial Bank, by taking over selected assets and liabilities of another Kenyan Bank, Chase Bank, which would significantly increase our balance sheet. In the same vein, the Group has been granted the Wholly

FOREWORD BY SBM GROUP CHAIRMAN

Owned Subsidiary Licence (WOS) by the Reserve Bank of India, becoming the first foreign bank to be issued a WOS Licence in India. We expect to better serve our Indian customers and position ourselves as a financial bridge in the Asia-Africa corridor. Expansion continues in Madagascar with the opening of a fifth branch. The Group is also considering different options for entering the Seychelles market. In the arena of digitalization, SBM is the first bank to partner with the global leader of digital financial services and lifestyle platform, Alipay, the sister company of Alibaba and operated by Ant Financial Services. Last but not least, I take great pride to mention that Afrexim Bank, a pan-African financial institution that exists since 1993, designated SBM for the listing of its shareholding to the public on the Stock Exchange of Mauritius. This transaction marked a series of firsts, namely:

I. the first time that a supranational bank opened its capital to the general public through the emission of Depositary Receipts;
II. the first time that a supranational bank listed its Depositary Receipts on an African Stock Market;
III. the first time that a Mauritian Stockbroker issued Depositary Receipts; and
IV. the first time that the Stock Exchange of Mauritius listed Depositary Receipts.

SBM successfully raised USD 165 million of Depository Receipts for the supranational bank - the highest pre-listing capital ever raised on the Stock Exchange of Mauritius, reaching another important milestone in its history.

SBM continues its path towards diversification into a broad-based bank with the launch of new products, services and businesses, like Factoring, Microfinance, Investment Banking, MOOV for the SMEs and Green Finance amongst others. A special purpose vehicle (SPV) in the name of SBM Mauritius Infrastructure Development Company Ltd has been set up to act as a channel between Export-Import Bank of India (EXIM Bank) and Mauritian public sector entities for the execution of infrastructure projects in the country.

In line with the Group's broader objective to serve the society in which it operates, our economic publication aspires to help SBM Group's stakeholders gain a better understanding of the global, regional and domestic economic landscape as well as to contribute to economic debate in the country. Hence, we expect to continue our positive contribution to the nation and bring to the fore any topic or material we deem pertinent for the economy.

In this edition, the Strategy & Research team has reviewed the global economy and updated its forecasts for the Mauritian economy. The country report focuses on Ghana - an economy with tremendous business and investment opportunities. The document ends with a special report on Bridging the Infrastructure Gap in Africa - Towards New Partnership Models. I trust that you will relish reading this edition of SBM Insights and find it to be a valuable tool to use. I take this opportunity to wish you all the best for 2018.

LI KWONG WING Kee Chong, G.O.S.K.
Chairman,
SBM Holdings Ltd

CHIEF EDITOR'S NOTE

World economic expansion has strengthened in 2017, and prospects for the period ahead are strong. Among the advanced economies, the US and the Eurozone are projected to record robust performances, accompanied by labor market improvements. The US is thus set to continue, or even accelerate, its cycle of interest rate increases, while the EU is also expected to gradually remove policy accommodation. On the other hand, the UK economy has slowed down, as investment and consumption are dampened in the wake of uncertainty as well as higher inflation following Brexit. Emerging markets should, for their part, benefit from resurging global demand and an upturn in the commodity cycle. Indeed, projections for commodity prices, particularly oil, have undergone a notable revision since our last forecasts. The prognosis regarding exchange rates is mixed, with market players balancing strong prospects and rising interest rates in the US against risks of rising protectionism and geopolitical tensions, among others.

The Mauritian economy has remained resilient in 2017 and, buoyed by a projected rise in investment both in the public and private sectors, activity in the construction sector is expected to accelerate this year, with the momentum remaining strong in 2019. Services sectors should also post appreciable growth rates, although risks are prevalent, particularly over the medium term in the business and financial services segment. The solid economic performance should help support an improvement in the labor market situation. However, inflation has temporarily soared on the back of weather-related shocks and increases in fuel prices, but core inflation should remain within manageable levels. The current account deficit deteriorated last year in line with poor export performance and higher commodity prices, but the deficit is expected to narrow this year under the assumption of a weaker dollar on an annual average basis. With financial flows remaining strong, the balance of payments is expected to remain in a surplus situation, thus supporting the currency.

Our regional focus for this edition is on Ghana. The West African nation bounced back from a drought-induced slowdown to grow by 8.5% in 2017, the strongest expansion rate in five years. However, the country has been struggling with inflation. Despite significant cocoa, gold and oil exports, Ghana has experienced sustained current account deficits, being dependent on imports of refined oil. The government has embarked on a long term development plan to support the transformation of the economy, earmarking several infrastructure and other projects. It is deemed that there are many potential cooperation avenues between Mauritius and Ghana as these two countries share common objectives and can mutually benefit from cross-border investments and sharing of expertise.

The Special Report also puts emphasis on the African continent, with a discussion on the topical issue of infrastructure financing. Various sources confirm that there is a huge infrastructure gap in Africa, and bridging that gap, even partially, would have significant positive effects on growth, industrialization, job creation and quality of life of Africans. However, traditional ways to finance infrastructure may not be adequate to meet the funding requirements. We argue that, to boost investments into infrastructure in Africa, a cooperative arrangement should be pursued, whereby a coalition of stakeholders (government, end users, suppliers, investors and banks) is formed within a structured financial and legal framework, with the interests of each stakeholder group protected in line with reasonable risk-reward profiles. Besides, innovative financial instruments need to be developed to cater for the different investment horizons and expected returns of potential investors.

We wish you good reading and welcome your valuable comments and suggestions at research@sbmgroup.mu

SREEKEESSOON Shailen
Head of Strategy and Research
16 May 2018

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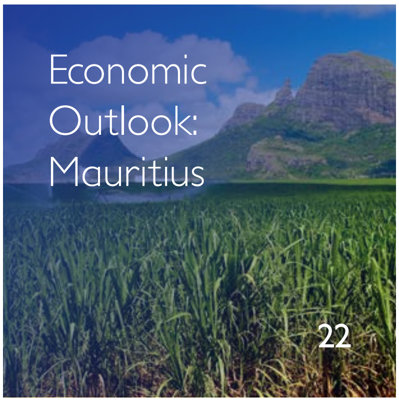
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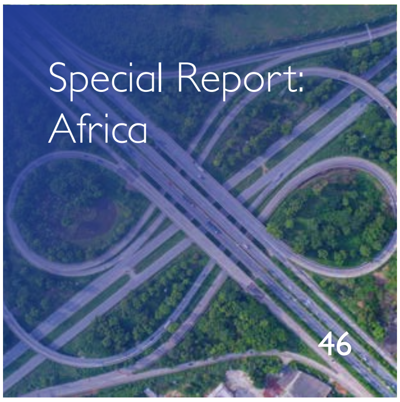
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ABBREVIATIONS

AfDB	African Development Bank
Bn	Billion
BoE	Bank of England
BoG	Bank of Ghana
CPI	Consumer Price Index
DTAA	Double Taxation Avoidance Agreement
ECB	European Central Bank
ECOWAS	Economic Community of West African States
EPZ	Export Processing Zone
ERP	Economic Recovery Program
EU	European Union
EUR	Euro
FDI	Foreign Direct Investment
GBP	Great Britain Pound
GDP	Gross Domestic Product
G-to-G	Government to Government
GHS	Ghanaian Cedi
GIPC	Ghana Investment Promotion Centre
G7	Group of Seven
ICT	Information and Communications Technology
IMF	International Monetary Fund
MCCI	Mauritius Chamber of Commerce and Industry
Mn	Million
MPC	Monetary Policy Committee
MSCI	Morgan Stanley Capital International
NPLs	Non-Performing Loans
ONS	Office of National Statistics
OPEC	Organization of the Petroleum Exporting Countries
PMI	Purchasing Managers' Index
PPP	Purchasing Power Parity
PPP	Public-Private Partnership
RBI	Reserve Bank of India
SARB	South African Reserve Bank
SEZ	Special Economic Zone
SOEs	State Owned Enterprises
UNCTAD	United Nations Conference on Trade and Development
USD	US Dollar
WEF	World Economic Forum

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GLOBAL MACROECONOMIC ENVIRONMENT

HIGHLIGHTS

- The US economy maintained its momentum in the fourth quarter of 2017 with the real GDP growth rate reaching 2.9% (quarter on quarter, annualized). The Federal Reserve's Open Market Committee voted unanimously to raise the target range for the federal funds rate to between 1.50% - 1.75%, up 25 basis points, from the previous 1.25% - 1.50% range - a move widely anticipated by market participants. Once the labor market hits full employment and inflation reaches the Federal Reserve's 2% objective over the medium term, the federal funds rate would likely return to normal levels.

- The UK economy grew by 0.4% in the fourth quarter of 2017; slightly higher than the second quarter (Q2: 0.2%) and marginally lower than the third quarter (Q3: 0.5%). However, the labor market continued to show resilience in the three months to January 2018, in spite of weak GDP figures. The Bank of England maintained its policy interest rate (Bank Rate) unchanged at 0.5%, during its monetary policy meeting in March.

- Eurozone GDP increased by a robust 0.6% (quarter on quarter) in the fourth quarter on the back of external trade. According to Eurostat, labor market conditions were broadly stable in December with an unemployment rate of 8.7% - the lowest reading since January 2009. The ECB kept interest rates unchanged in line with market expectations and signaled that its asset purchase program would continue until September 2018 or beyond, if required.

- China ended 2017 on a positive note by registering a growth rate of 6.9% - the first annual acceleration since 2010, above the government's GDP target of around 6.5% and 2016 growth rate of 6.7%. The main drivers of growth were robust exports growth, a rebound in the industrial sector and a resilient property market.

- In India, the economy expanded by 7.2% year-on-year in the third quarter of fiscal year 2017/2018 (October-December quarter) - higher than the 6.5% increase recorded in the second quarter and above-expectations - representing the highest quarterly year-on-year growth rate in over a year. This was achieved in the wake of a gradual dispersion in the initial confusion that followed the implementation of the Goods and Services Tax and demonetization.

- South Africa's economy maintained its momentum in the fourth quarter, with an expansion of 2.3% quarter on quarter, exceeding market expectations of a softer expansion of 1.8%. Consequently in March 2018, Moody's Investors Service maintained South Africa's Baa3 rating and upgraded its outlook from negative to stable, stating that the previous weakening of national institutions was gradually reversing, which supported an economic recovery.

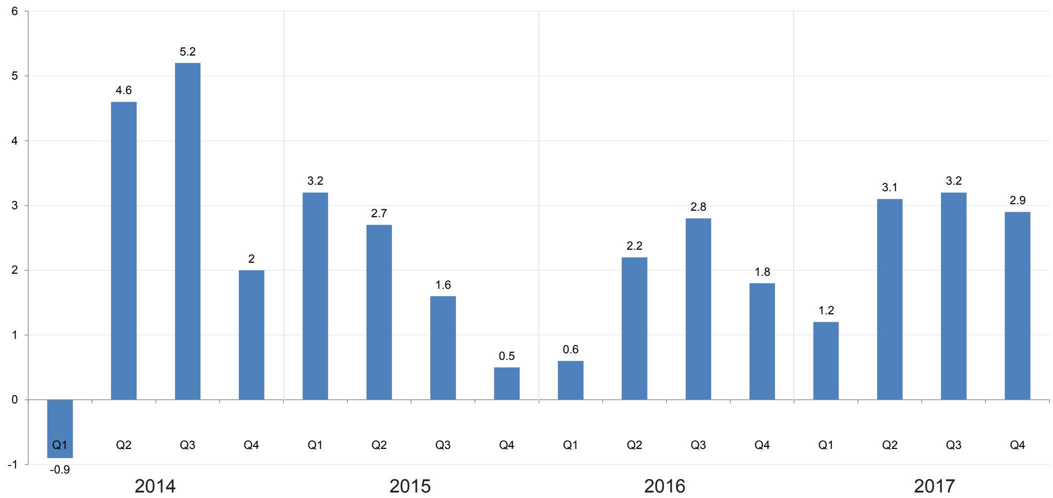
- Oil prices ended the year 2017 at USD 66.87/barrel - the highest end of year price since 2013 - on the back of robust global demand and curtailments in crude oil production by OPEC members during the year.

- The US dollar depreciated against most major developed and developing country currencies from late October to the end of the year 2017, despite positive economic data and the increased likelihood of a rate hike.

1.1 US

The US economy maintained its momentum in the third quarter of 2017 with the real GDP growth rate reaching 3.2% (quarter on quarter, annualized) compared to 3.1% in the second quarter. However, GDP growth decelerated in the last quarter, but remained strong at 2.9% according to the third estimate (second estimate: 2.5%). The robust performance was attributed to positive contributions from personal consumption expenditures, residential and non-residential fixed investment and rising exports. Personal consumption expenditure registered growth rates of 2.2% and 4.0% (previous estimate: 3.8%) in the third and last quarters respectively, on account of an upward trend in consumer confidence (Refer to Figure 1-B). Since consumer spending accounts for nearly 70% of the US economic activity, both personal consumption expenditure and consumer confidence index provide a sound indication of the US economy's health based on current economic conditions and consumers' expectations for the next six months. Tax cuts and the strong job market were the main drivers of consumer optimism.

Figure 1-A: Real GDP - Percent Change from Preceding Quarter (seasonally adjusted at annualized rates)



Source: U.S. Bureau of Economic Analysis

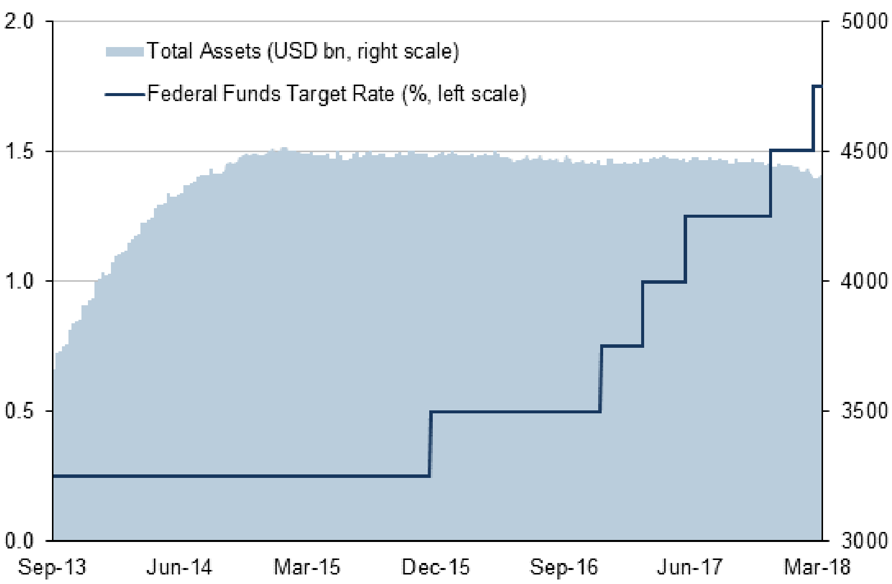
Residential fixed investment growth stood at -4.7% and 12.8% (second estimate: 13.0%) in the third and fourth quarters, respectively. The sudden pick-up in the fourth quarter was due to a surge in US single-family homebuilding and permits in November - exceeding a 10-year high - as disruptions from hurricanes Harvey and Irma dispersed. Likewise, non-residential fixed investment rose by 4.7% and 6.8% (previously estimated at 6.6%) respectively in the last two quarters, due to an increase in spending on equipment. Net exports also went up, driven by a weak dollar. On the other hand, a decline in private inventories confined the pace of growth in real GDP. All in all, the US economy grew at 2.3% in 2017 compared to 1.5% in 2016, a sign of faster growth than the prior year but short of Trump administration's goal of a GDP growth rate of 3.0%. See Table 1-A for growth forecasts.

Figure 1-B: US Consumer Confidence Index

Source: The Conference Board

At its March 2018 monetary policy meeting, the Federal Reserve's Open Market Committee voted unanimously to raise the target range for the federal funds rate to between 1.50% - 1.75%, up 25 basis points, from the previous 1.25% - 1.50% range - a move widely anticipated by market participants. As stated in our November edition, the Federal Reserve began its balance sheet normalization program in October 2017, reducing its securities holdings by decreasing reinvestment of principal payments; at a pace of USD 50 billion per month. Consequently, this process is expected to shrink the Federal Reserve's USD 4.5 trillion balance sheet to below USD 3.0 trillion by 2020. Concurrently, once the labor market hits full employment and inflation reaches the Federal Reserve's 2% objective over the medium term, the federal funds rate would likely return to normal levels. Higher growth and inflation forecasts and lower unemployment rate estimates have prompted the Federal Reserve to move up their interest rate expectations for 2019 (from two hikes to three hikes) and 2020 (two hikes instead of one hike) and kept their 2018 estimate unchanged at three interest rate hikes. In its latest monetary policy meeting in May, the Federal Reserve kept the federal funds rate at the current range of 1.50% - 1.75%, citing improving labor market conditions and inflation outlook.

Figure 1-C: Monetary Policy Chart



Source: Federal Reserve

1.2 UK

The Office of National Statistics (ONS) confirmed that the UK economy grew by 0.4% in the fourth quarter of 2017 (unchanged from the second estimate of GDP); slightly higher than the second quarter (Q2: 0.2%) and marginally lower than the third quarter (Q3: 0.5%). The biggest component of GDP, consumer spending, experienced limited growth of 0.3% quarter on quarter due to a weak sterling squeezing household budgets. The main contributor to the 0.3% growth was housing spending. Moreover, business investment growth was flat between the third and fourth quarters. Sector-wise, business services and finance within the services sector drove the last quarter's growth, on the back of an expansion rate of 0.6% (quarter on quarter). On an annual basis, GDP increased by 1.8% in 2017; an upward revision of 0.1 percentage point from the second estimate, but the slowest rate of annual growth since 2012's rate of 1.5%. Among the G7, UK was the only economy experiencing a deceleration in GDP growth in 2017 due to the impact of Brexit-related uncertainties on business investment, a weaker sterling making imports more expensive and reduced living standards.

The UK labor market continued to show resilience in the three months to January 2018, in spite of weak GDP figures. Accordingly, the unemployment rate fell to 4.3% in November-January, from 4.4% in the previous three-month period and down from 4.8% in 2016 - the lowest since 1975. Inflation remained above the BoE's 2% target since February 2017, reaching 3.0% in December (November: 3.1%) as a result of the fall in the value of the sterling making imports more expensive. In February 2018, inflation fell to 2.7% from 3.0% in January. Following the drop in the inflation rate in February, the Bank of England decided to keep its policy interest rate (Bank Rate) unchanged at 0.5%, during its monetary policy meeting in March. The Bank of England pointed out in its recent communique that it will tighten its monetary policy stance in the medium/long term but not in the near future on account of subdued growth. Refer to Table 1-B for interest rate projections.

1.3 Eurozone

The Eurozone real GDP growth rate in the fourth quarter stood at 0.6% (quarter on quarter), down from the 0.7% recorded in the third quarter, driven mainly by external trade. Exports increased by 1.9% quarter on quarter while imports rose by 1.1%, indicating that the negative impact of the appreciating euro on the trade balance was limited. Besides, investment picked up from a contraction of 0.2% in the third quarter to an expansion of 0.9% in the fourth quarter, supported by renewed business confidence. However, consumer spending growth slowed from 0.3% in the third quarter to 0.2% in the last quarter. Germany and France were the main contributors to the overall good performance while Italy experienced a more subdued economic expansion, making for an overall economic growth of 2.3% in the Eurozone, on an annual basis. According to Eurostat, labor market conditions were broadly stable in December with an unemployment rate of 8.7% - the lowest reading since January 2009.

At its monetary policy meeting in April, the ECB kept interest rates unchanged in line with market expectations. The main refinancing rate was kept at 0.00% and the marginal lending rate and deposit facility rate at 0.25% and -0.40%, respectively. The ECB signaled that its asset purchase program would continue until September 2018 or beyond, if required, but made no mention of enlarging the program which currently stands at EUR 30 billion per month. The statement made by the ECB president was practically similar to that of its March monetary policy meeting; he asserted that economic growth in the Eurozone remained anemic while remaining optimistic that underlying fundamentals are solid and broad-based. Inflation in the Eurozone stayed below the Central Bank's target of "close to" but below 2%. The harmonized inflation rate stood at 1.4% in December (year on year) while core inflation was 1.1% year on year, thus supporting the ECB's accommodative monetary policy stance.

Table 1-A: Growth Projections – Selected Major Global Economies

	POLL OF FORECASTERS, MAY AVERAGES				
	2017	2018		2019	
Percent change in real GDP		Average	Range	Average	Range
US	2.3	2.8	2.6–3.1	2.5	2.0–3.0
UK	1.7	1.4	1.2–1.7	1.5	1.0–1.9
Eurozone	2.4	2.3	2.1–2.6	2.0	1.7–2.4
China	6.8	6.6	6.4–6.8	6.4	6.1–6.9
India*	6.4	7.2	6.6–7.7	7.5	7.2–7.9
South Africa	0.9	1.9	1.7–2.2	2.1	1.7–2.9

Source: The Economist (May poll of forecasters)
* For the fiscal year ending March of the following year.

Table 1-B: Central Bank Interest Rates

		APRIL SURVEY - MEDIAN FORECASTS	
Percent	Current	Q2 2018	Q2 2019
Federal Funds Rate	1.50–1.75	1.75–2.00	2.50–2.75
BoE Bank Rate	0.50	0.75	1.00
ECB Main Refinancing Rate	0.00	0.00	0.00

Source: Bloomberg

1.4 Selected Emerging Markets

1.4.1 China

The East Asian giant ended 2017 on a positive note by registering a growth rate of 6.9% - the first annual acceleration since 2010 - above the government's GDP target of around 6.5% and 2016 growth rate of 6.7%. The fourth quarter of 2017 recorded a GDP growth of 6.8% (Q3: 6.8%), slightly above analysts' forecast of 6.7%. The main drivers of growth were robust exports growth, a rebound in the industrial sector and a resilient property market. China's imports and exports performed well in 2017 on the back of global recovery and domestic demand, with exports growing by 10.8%. Industrial production rose by 6.6% in 2017 compared to 6.0% in 2016 and real estate investment grew by 7%, compared with 6.9% in 2016. Despite strong GDP figures, there are several downside risks including: recent US trade restrictions on Chinese exports; reports of irregularities in economic data and the exceedingly high debt figure. According to the IMF, the debt is equivalent to 234% of the economy's total output.

1.4.2 India

In the third quarter of fiscal year 2017/2018 (October-December quarter), the Indian economy expanded by 7.2% year-on-year, higher than the 6.5% increase recorded in the second quarter. This above-expectations performance - representing the highest quarterly year-on-year growth rate in over a year was achieved in the wake of a gradual dispersion in the initial confusion that followed the implementation of the Goods and Services Tax and demonetization. Though industrial output slowed down in December from November's outstanding performance, it remained resilient and above market expectations. Private consumption growth moderated from 6.6% year-on-year in the second quarter to 5.6% in the third quarter - the weakest since fiscal year 2014/2015. On the other hand, fixed investment growth soared to 12.0% in annual terms in the third quarter, higher than the 6.9% increase recorded in the previous three-month period (the best reading in six quarters) attributable to increased public capital spending.

During its first bi-monthly monetary policy meeting on 04-05 April, the RBI revised its inflation rate projections upward for the first half of fiscal year 2018/2019 to 4.7% - 5.1% and 4.4% in the second half, against the background of rising commodity prices in the wake of stronger global growth. The RBI also projected the GDP growth rate to pick up from 6.6% in 2017/2018 to 7.4% in 2018/2019 on the back of improved investment activity derived from robust global demand. Nonetheless, the repo rate (key lending rate) was kept unchanged at 6.00%. The reverse repo rate also remained at 5.75% along with the Marginal Standing Facility Rate and Bank Rate at 6.25%.

1.4.3 South Africa

The South African economy expanded at 3.1% quarter on quarter (seasonally adjusted, annualized) in the fourth quarter compared to 2.3% in the third quarter, exceeding market expectations of a softer expansion of 1.8%. Several economic indicators propelled the last quarter's growth rate; private consumption rose by 3.6% quarter on quarter compared to the previous quarter's 2.4% increase on the back of a steady inflation rate and increased spending on household furnishing and equipment and health services. Fixed investment grew by 7.4% (Q3: 2.7%) - a 1-year high - on account of increased investment in machinery and other equipment. Exports expanded by 12.3% compared to a contraction of 0.6% registered in the third quarter of 2017. High global demand for precious metals (for instance platinum) led to rising exports but a higher imports growth dampened the external sector's performance.

Activity in the private sector contracted in the five months to December 2017. The drop in business activity was largely due to muted demand and deteriorated business conditions. The Standard Bank Purchasing Managers' Index (PMI) was reflective of the situation and stood at 48.4 in the last month of 2017, below November's 48.8. Yet again, the poor reading was attributed to a decline in output, total new orders and new businesses from abroad. In March 2018, Moody's Investors Service maintained South Africa's Baa3 rating and upgraded its outlook from negative to stable, stating that the previous weakening of national institutions was gradually reversing which supported an economic recovery.

At its monetary policy meeting in March, the Monetary Policy Committee of the South African Reserve Bank (SARB) cut the repo rate from 6.75% to 6.50% - the last repo rate cut was in July 2017. The decision was based on the fact that political conditions were improving and inflation rate remained moderate. Inflation climbed from 4.6% in November to 4.7% in December, but stayed within the Central Bank's target range of 3.0% - 6.0%. The repo rate cut is expected to be a relief for the South African consumers, partly mitigating the impact of the 1% VAT increase that will become effective as from 01 April 2018. Reflecting recent economic developments, and considering improved business and consumer confidence, the Central Bank has revised upward its growth forecast for 2018 to 1.7% (previous forecast: 1.4%).

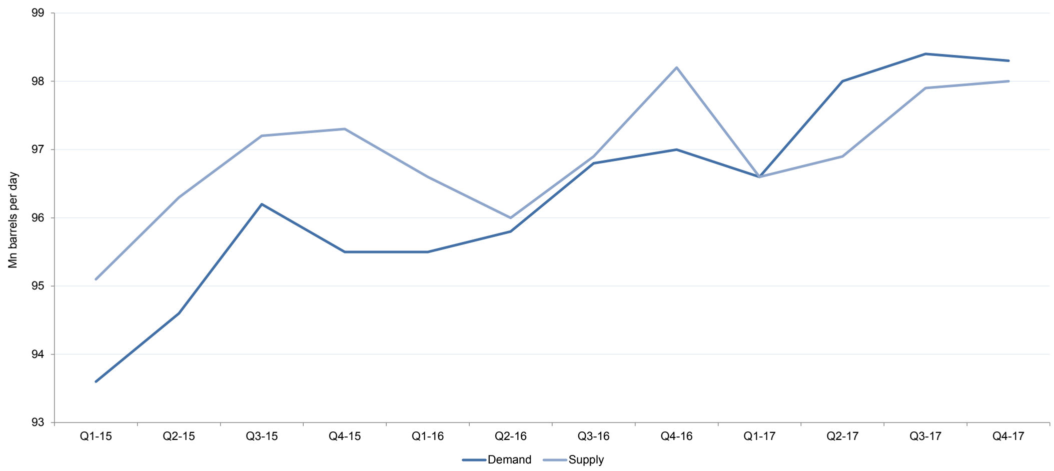
1.5 Commodities

Despite relatively high US crude oil production, oil prices ended 2017 at USD 66.87/barrel, the highest end of year price since 2013 as robust global demand and curtailments in crude oil production by OPEC members supported oil price increases during the year. The International Energy Agency expected world oil demand to exceed supply in 2017, by 1.9 million barrels per day. In the last three quarters, demand exceeded supply by an average of 0.6 million barrels per day (see Figure 1-E). However for 2018, the International Energy Agency expects world oil supply to outpace demand on account of rising global oil production, led by the US. Refer to Table 1-C for Brent price forecasts.

Figure 1-D: Brent Price Evolution

Source: Bloomberg

Figure 1-E: World Oil Supply and Demand



Source: International Energy Agency

Table 1-C: Brent Price Forecasts

USD/barrel	ACTUAL Q4 2017	ACTUAL Q1 2018	Q2 2018	Q3 2018	Q4 2018
Bloomberg median (as of 30/04/2018)	61	67	65	65	65
US Energy Information Administration	61	67	73	72	71

Sources: Bloomberg, US Energy Information Administration

The World Bank's metals and minerals price index continued its upward trend throughout 2017. Yet again, China, the world's largest consumer of metals, drove the prices of metal up. The global aluminum price has continued its bull run due to environment and supply-side restrictions in China coupled with higher input costs and strong industrial activity. However, the likely impact of the United States' Section 232 tariff on aluminum imports and its potential effect on global trade flows continue to blur the metal's outlook in the foreseeable future.

The World Bank's grains price index edged up by 10% in February 2018 against the same month in 2017. Between October and December, the index gained 9% on account of rising wheat prices. Ongoing drought conditions across the US continued to weigh down on production output whilst global demand keeps rising.

Figure 1-F: World Bank Commodity Price Indices

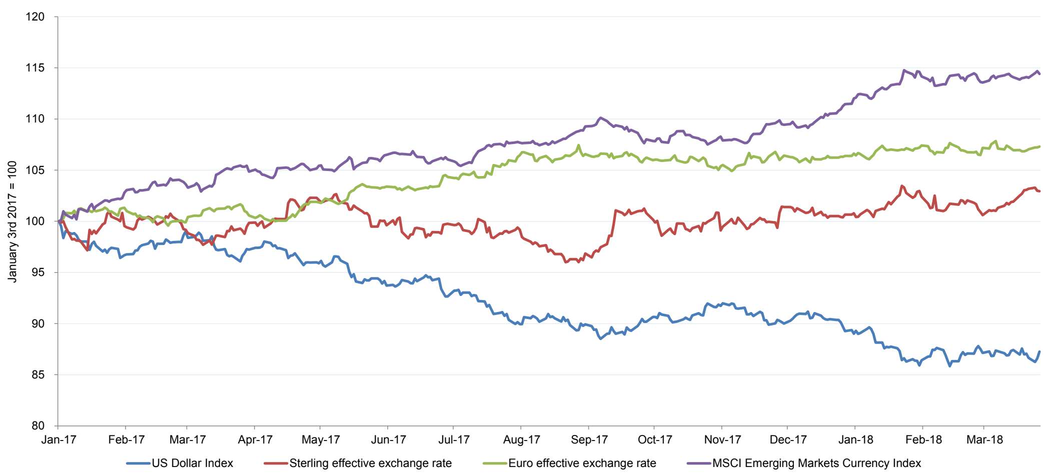
Source: World Bank

1.6 Currencies

The US Dollar Index, which measures the value of the dollar relative to six advanced-economy currencies, ended the year lower by 2.3% from late October, in spite of positive economic data and the increased likelihood of a rate hike by the Federal Reserve Open Market Committee. It is noted that the US Dollar Index remained bound within a relatively tight range, despite positive news in late 2017. A range of factors, such as strengthening commodity prices and the likely impact of Trump administration's policies on the economy, continued to put pressure on the US Dollar Index in the first months of 2018. Conversely, many emerging-market currencies gained against the dollar during that period - as reflected by the upward trend of the MSCI Emerging Markets Currency Index, which tracks the value of 25 emerging-market currencies against the US dollar (refer to Figure 1-G).

The euro effective exchange rate - a trade-weighted measure of the euro's value - gained 1.1% between late October and the end of December, on the strength of an easing political landscape and the optimistic outlook of the ECB committee members contemplating an early exit from quantitative easing during their December meeting. The sterling advanced by 0.7% on a trade-weighted basis in the two months to December, within the context of a weaker dollar. The easing pressure on the sterling is purportedly also due to "visible progress" being made in the Brexit negotiations. Refer to Table 1-D for exchange rate forecasts.

Figure 1-G: Evolution of Indices of Major Global Currencies



Sources: Bloomberg, Bank of England, European Central Bank, MSCI

Table 1-D: Exchange Rate Forecasts

	PREVIOUS	ACTUAL	FORECASTS			
	31/10/2017	Q1 2018	Q2 2018		Q3 2018	
			Median	Range	Median	Range
EUR/USD	1.16	1.23	1.22	1.15-1.29	1.24	1.13-1.40
GBP/USD	1.33	1.40	1.40	1.32-1.48	1.41	1.26-1.48

Source: Bloomberg

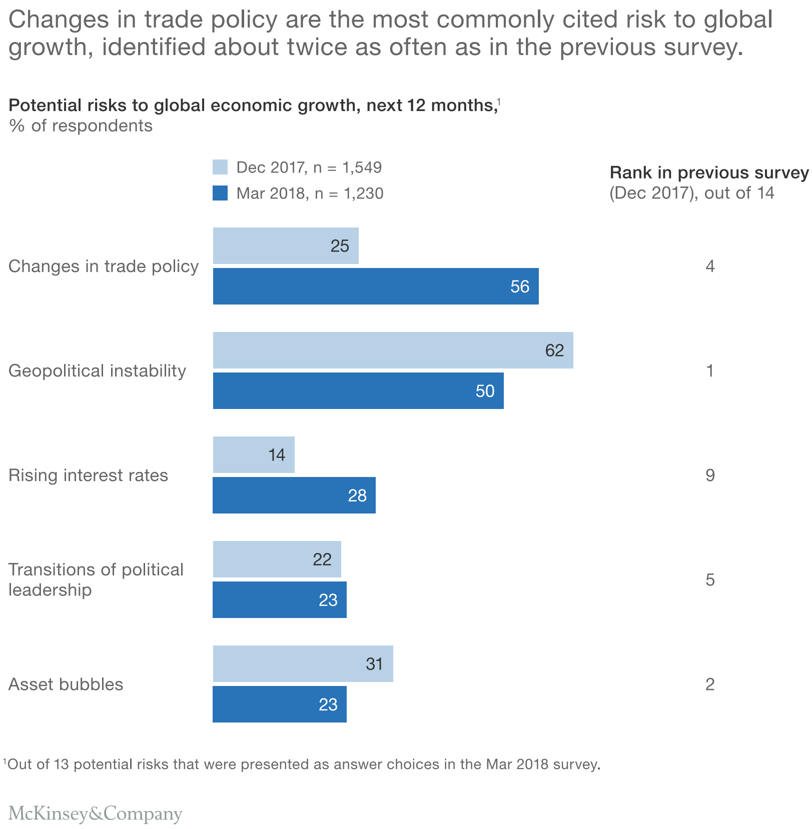
1.7 Risks to the Outlook

Over the medium and long terms, risks to the outlook remain mostly skewed to the downside on account of heightened uncertainty, instability and fragility across economies. Below are some major risks that may disrupt global growth:

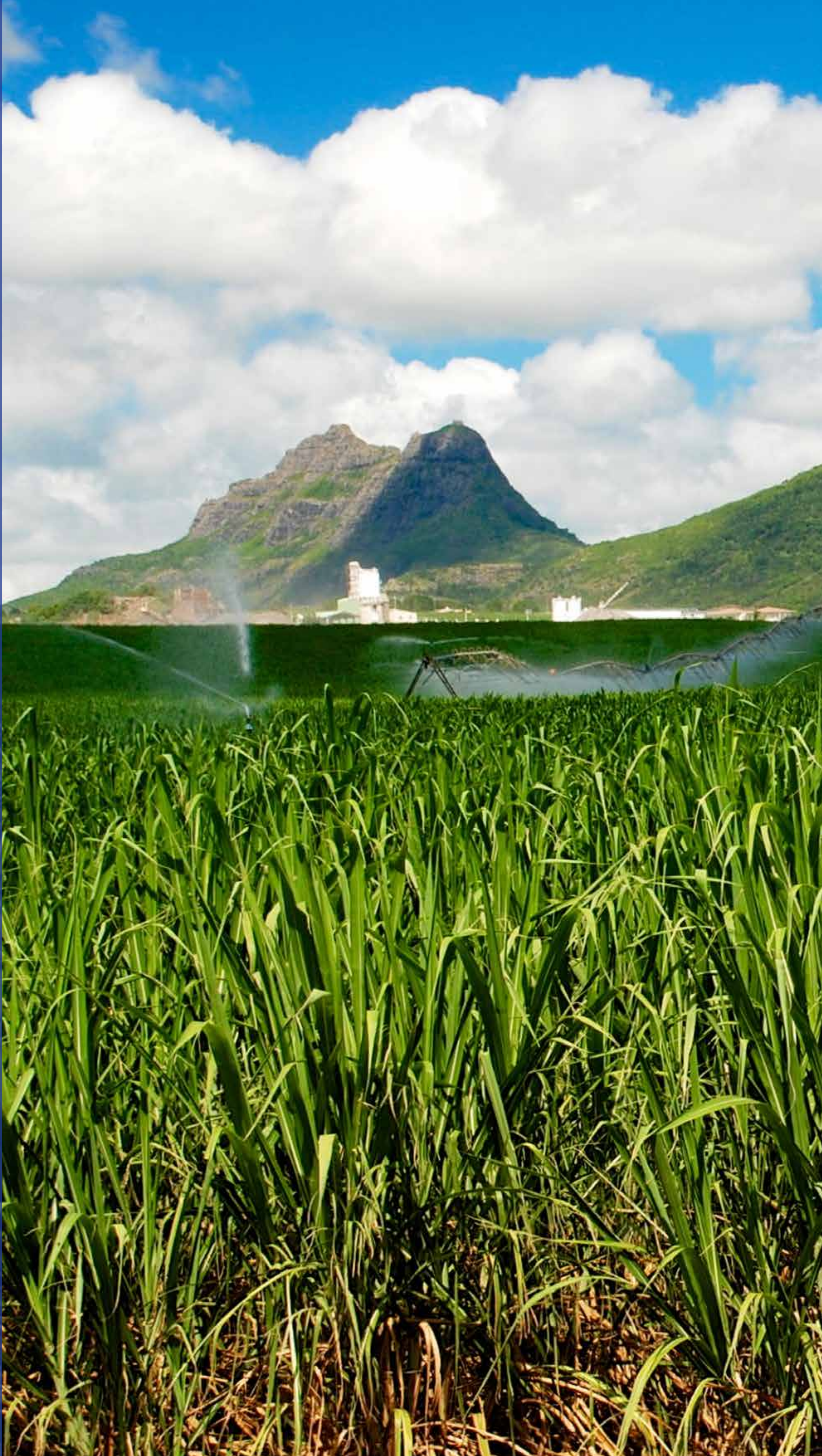
- Geopolitical tensions, particularly in East Asia and the Middle East;
- Political uncertainties leading to reform implementation risks or the likelihood of reoriented policy agendas, including in the context of recent and upcoming elections (Italy, Russia, Brazil, Colombia and Mexico);
- Protectionist measures leading to trade wars across developed and developing economies, disrupting global supply chains;
- Aggressive tightening of interest rates by the Federal Reserve leading the US economy into recession;
- A sharp economic slowdown in China due to a disorderly unravelling of the credit boom;
- Recent extreme adverse climatic conditions - hurricanes in the Atlantic, drought in sub-Saharan Africa and Australia - point to the risk of recurrent, potent climatic events that would lead to significant humanitarian costs and economic losses. Consequently, such climatic events might increase migration flows and destabilize already fragile recipient countries.

McKinsey carried out a survey on economic conditions in March, whereby global respondents were requested to identify rising risks to global economic growth. The results of the survey showed that the number of respondents, citing changes to trade policy as the most risky, more than doubled since the previous survey carried out in December 2017. The results of the survey have been illustrated in Figure 1-H.

Figure 1-H: Potential Risks to Global Economic Growth



ECONOMIC OUTLOOK - MAURITIUS



HIGHLIGHTS

- After growing by a resilient 3.5% in 2017, the Mauritian economy is expected to experience an upswing in the periods ahead, with a projected growth rate of 3.9% in both 2018 and 2019.
- The construction sector is expected to be a key driver of activity, potentially touching double-digit growth in 2018, driven by the implementation of major public sector infrastructure projects as well as an upturn in private sector investment, mainly related to hotels and property development.
- Services sectors are expected to maintain an appreciable performance, albeit subject to risks, particularly in 2019 in the business and financial services segment.
- On the other hand, sugar and export-oriented industry are expected to face continued challenges.
- Despite the difficulties foreseen in the agriculture and manufacturing sectors, the unemployment rate should maintain a downward trend, supported by the positive outlook in construction and tourism to reach 7.0% in 2018 and 6.9% in 2019.
- Despite a projected weaker dollar on an annual average basis, the inflation rate is expected to shoot up to 4.1% in 2018 on the back of higher vegetable and fuel prices. However, core inflation would be relatively stable.
- The current account deficit is expected to narrow to around 4½% in both 2018 and 2019, compared to a high of 6.6% in 2017, mainly due to a weaker dollar projected on average. The balance of payments is projected to remain in surplus on the assumption that capital outflows are contained.
- The exchange rate of the rupee is thus expected to be stable in effective terms. Based on projected movements of international currencies, this would translate into an appreciation of the rupee vis-à-vis the dollar and a depreciation against the euro and the sterling.
- Under the baseline scenario, it is anticipated that monetary policy will remain accommodative throughout the forecast period. Should growth consolidate as projected, the Monetary Policy Committee of the Bank of Mauritius may be tempted to review the rates slightly upward.
- The budget deficit for financial year 2017/18 is on track to achieve the Budget estimates of 3.2% of GDP. The public sector debt level is expected to decline, albeit remaining high.
- With the global and domestic economies still in a transition phase, the risks to the outlook are tilted to the downside. Material deviations in the global economic/geopolitical environment, commodity prices, currency rates, net capital flows, project implementation timelines, and climatic conditions, among others, could warrant changes to the forecasts.
- Decisive action to steer the economy towards a new paradigm that is outward focused, innovation driven and geared towards value addition and sustainability could help achieve a higher growth and employment path.

2.1 Economic Growth

2.1.1 2017 review

The March 2018 National Account estimates by Statistics Mauritius situate the real growth rate for the Mauritian economy in 2017 at 3.5%, that is, 20 basis points below the December 2017 prognosis, and 30 basis points lower than the SBM Insights projection made in November 2017, as some key sectors of the economy – notably textile manufacturing, accommodation and food services activities, and public administration and defence – achieved a lower growth rate than earlier anticipated. Notwithstanding the downgrade, the overall expansion rate is broadly in line with the prior year's performance, indicating continued resilience of the economy. As anticipated, the main drivers of growth were business and financial services and the construction sector, the latter posting a solid expansion rate of 7.5% after a cumulative contraction of 24% in the previous six years. On the other hand, textile manufacturing and sugar continued to be a drag factor on the economy.

Table 2-A: Real GDP Growth Rate Forecasts: Comparatives

	ESTIMATES	2017		2018	
	As at	Projected	Latest Estimate*	As at	Forecasts
SBM (at basic prices)	Nov-17	3.8%	3.5%	May-18	3.9%
Statistics Mauritius (at basic prices)	Dec-17	3.7%		Mar-18	3.9%
Bank of Mauritius (at market prices)	Dec-17	3.8%		Mar-18	4.0%
MCCI	Nov-17	4.0%		Nov-17	4.4%
IMF (at basic prices)	Oct-17	3.9%		Apr-18	3.9%
World Bank (at market prices)**	Jun-17	3.4%		Jan-18	3.8%

Sources: Statistics Mauritius, Bank of Mauritius, MCCI, IMF, World Bank

Note:
* Estimate revised on 30 March 2018
** In its latest economic prospects in January 2018, World Bank revised up its growth forecast for 2017 to 3.9%

2.1.2 What has changed since our last forecasts?

Since our previous forecasts in November last, the main challenge to our assumptions has been the adverse climatic conditions experienced in the first few months of 2018. While beneficial to water resources, heavy rainfall in the first four months of the year, partly linked to the passage of three cyclones near the islands, engendered flooding, work disruptions, damage to agricultural output, flight rescheduling, and project delays, among others. Besides, the ensuing sustained rise in vegetable prices caused a spike in inflation, which would have a negative impact on consumption and growth.

Global oil and other fuel prices have also trended higher than what was earlier anticipated by the markets, prompting an upward revision of price forecasts. For instance, in November 2017, the US Energy Information Administration projected the average prices of Brent oil, gasoline and diesel fuel in 2018 at USD 55.61 per barrel, USD 1.67 per gallon and USD 1.78 per gallon respectively. In April 2018, these projections were reviewed upwards by 13.9%, 12.6% and 10.1% respectively. This is expected to have an adverse impact on inflation and the current account deficit, among others.

On a brighter note, investor confidence has continued to strengthen. The latest MCCI Business Confidence Indicator for Q1 2018, indicated a 4.1% rise in the confidence index, which reached 128.1 points, that is, the highest level since the indicator was launched in 2010. It also marked the 6th consecutive quarter where an increase was noted in the index. Reflecting the improvement in investor confidence, an increase has been observed in the pipeline for private sector investment projects.

2.1.3 Updated forecasts for 2018 and preliminary forecasts for 2019

Within the context of a lower projected growth in agriculture and consumption-linked sectors, such as commerce and domestic-oriented manufacturing, our projection for economic growth in 2018 has been brought down by 20 basis points to 3.9%. This still represents a strong upswing from the 3.5% recorded in 2017, underpinned by the buoyancy expected in the construction sector and sustained resilience of services. However, operating conditions in the agriculture and manufacturing sectors are expected to remain difficult. Looking ahead, the growth momentum should continue into 2019, although risk factors are prevalent, particularly in business and financial services.

Table 2-B (i): Contribution to GDP - Selected Sectors (%)

	2014	2015	2016	2017(e)
Agriculture, forestry and fishing	3.7	3.6	3.6	3.5
Mining and quarrying	0.3	0.2	0.2	0.2
Manufacturing	15.3	14.7	14.0	13.4
Construction	4.8	4.4	4.2	4.3
Trade	11.9	12.0	11.9	12.1
Transportation and storage	6.1	6.2	6.3	6.3
Accommodation and food service activities	6.2	6.5	6.9	7.1
Information and communication	4.3	4.4	4.2	4.2
Financial and insurance activities	11.9	12.0	12.1	11.9
Real estate activities	6.1	6.0	5.9	5.9

Source: Statistics Mauritius (e) Estimates

Table 2-B (ii): Contribution to GDP - Selected Industry Groups (%)

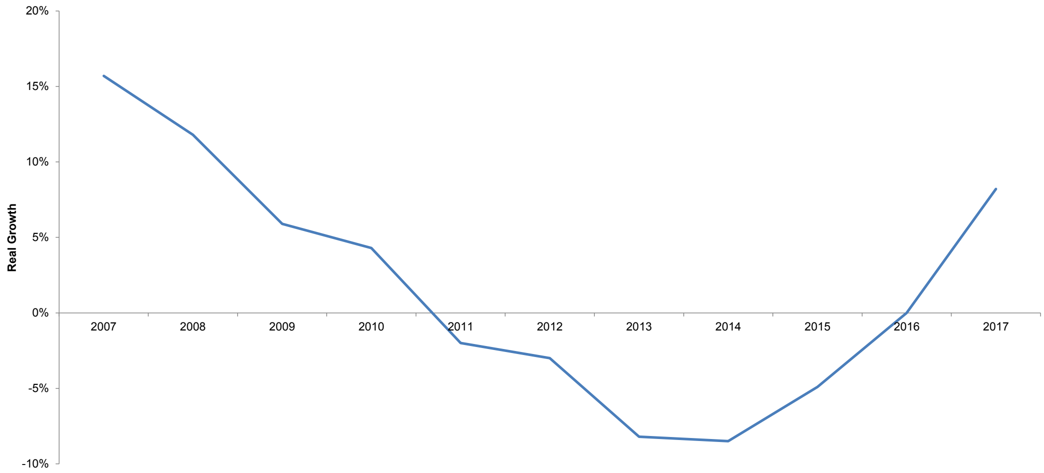
	2014	2015	2016	2017(e)
Export oriented enterprises	5.9	5.8	5.2	4.9
Seafood	1.0	1.0	1.0	1.0
Freeport	0.6	0.7	0.6	0.6
Tourism	7.0	7.4	7.8	8.0
ICT	5.6	5.8	5.7	5.6
Global Business	6.0	5.8	5.6	5.7

Source: Statistics Mauritius (e) Estimates

As highlighted in our November 2017 edition, the construction sector should be a key engine of growth in 2018. Works on the Metro Express project have already started and are deemed to be progressing satisfactorily. Similarly, the contracts for the overhaul of the road infrastructure around the Phoenix Pont Fer and Jumbo roundabouts – a major traffic bottleneck – and for the building of the A1-M1 Bridge have already been allocated. The construction of a sports complex project in Cote d'Or, ahead of the Indian Ocean Island Games, is also under way. These major projects should provide support to activity in 2018 as well as in 2019, assuming that supply constraints, such as the availability of labor and materials, are addressed in a timely manner.

On the private sector side, following an upturn in tourist arrivals over the past few years, and consolidating margins of hotel operators, there has been renewed interest in the construction and renovation of hotels. Moreover, upmarket property development projects are progressing well, although many of them are dependent on foreign demand. Another landmark project this year is the setting up of a modern studio for filmmaking.

Figure 2-A: Construction Sector Performance



Source: SBM Staff Forecasts

Against this background, another stellar performance of the construction sector is projected in 2018, with growth potentially touching double-digits. The momentum should continue in 2019, although the expansion rate should be lower in view of base effects.

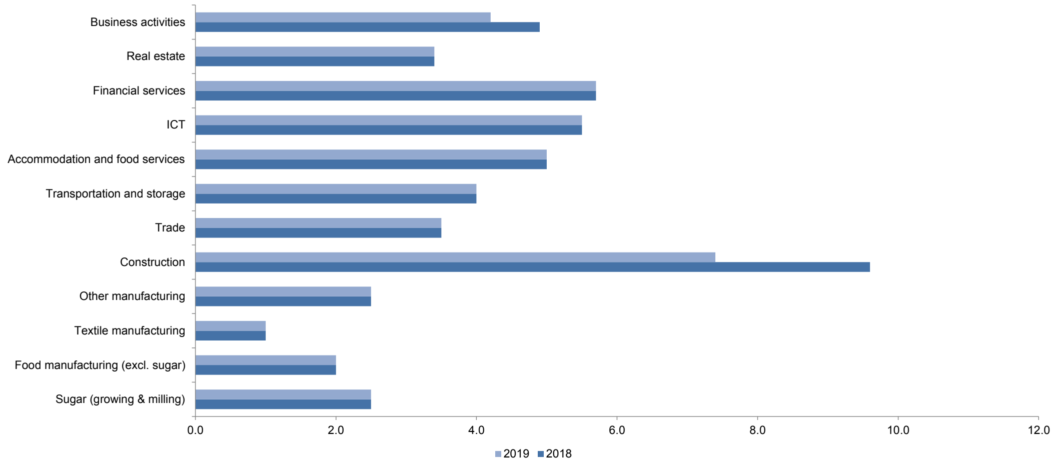
The hospitality sector is also expected to sustain a commendable performance in 2018 and 2019 supported, on the demand side, by favorable conditions for outbound tourism in key source markets and, on the supply side, by a projected expansion in the hotel park and in air seat capacity. Potential increases in airfares, following an increase in fuel prices on international markets, could, however, be a constraining factor.

Investment in real estate and hotel development should have positive spillover effects on a number of other sectors including trade, transportation and financial services. The trade sector is expected to also benefit from higher consumption growth, partly linked to the implementation of the minimum wage accompanied by a relatively favorable salary compensation for low income earners. Thus, trade is expected to post a higher growth rate in 2018 and 2019, compared to 2017, although the forecast for this year has been slightly brought down on account of higher than previously anticipated inflation.

Business and financial services, for their part, should benefit from an uptick in credit demand and reducing pressures on margins as the Bank of Mauritius mops up excess liquidity. Already, yields on Treasury bills have started edging higher. The sector should also be supported by diversification and regional expansion efforts by banks. However, the performance of the cross-border segment would be somewhat dependent on the availability of dollar funding. Whereas there are at present no major signs of stress - actually, dollar deposits and international reserves have been trending upwards - the foreign currency dynamics post April 2019 is yet to be fully ascertained. The major risk factor is the possibility of capital flight following the end of the grandfathering phase relating to capital gains tax treatment under the revised DTAA between Mauritius and India, and, to a lower extent, a toughening of regulatory requirements. Our forecasts have factored in a mild slowdown in 2019 as it is deemed that the restructuring process which is already under way in the industry, through product deepening and market diversification, should help temper the adverse impact of the changes in the operating environment, and should at least maintain the level of activity in the professional services segment.

On a different note, it is projected that the sugar and manufacturing sectors will continue to struggle in spite of incentives put in place to support them. Whilst the import of raw sugar for refining has helped sugar millers compensate for the drop in sugarcane output, the industry as a whole has been under pressure as a result of historically low sugar prices globally further to the liberalization of the EU sugar market. Export-oriented manufacturing is also expected to struggle as cost and availability of labor remain important constraints while currency dynamics continue to be broadly unfavorable for exporters.

Figure 2-B: Selected Industry Growth Forecasts



Source: SBM Staff Forecasts

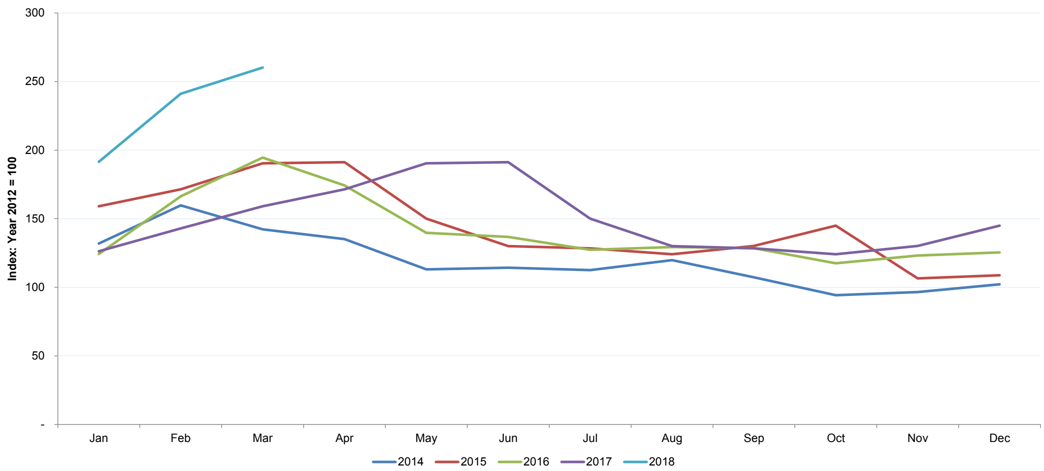
2.2 Unemployment

With some job-heavy sectors, such as construction and tourism, performing well, and following Government measures to reduce information asymmetry in the labor market, the unemployment level of Mauritians increased by 6,500 from 538,600 in 2016 to 545,100 in 2017, and the unemployment count decreased by 600 to 41,800. As a result, the joblessness rate improved from 7.3% in 2016 to 7.1% in 2017. In 2018 and 2019, difficulties in the sugar and textile manufacturing sectors would weigh negatively on net employment creation, but this should be more than compensated for by labor demand in the construction, tourism and other services sectors. The implementation of a minimum wage structure could also exert pressures on the labor market in the short term although, as argued in previous editions of SBM Insights, it is expected that - under reasonable conditions - the long term benefits would outweigh the short term costs, by triggering a shift towards higher value added activities, promoting equity and supporting increases in real wages. Overall, the unemployment rate is expected to improve slightly in 2018 and 2019.

2.3 Inflation

The inflation rate stood at 3.7% in 2017, that is, marginally higher than our projection made in November last, compared to 1.0% in 2016. Alcoholic beverages and tobacco, fruit and vegetables, and fuel prices were the main drivers of inflation. In the first few months of 2018, the headline inflation rate shot up significantly to reach 5.0% as at March 2018 (year-on-year inflation at 6.7%) as vegetable prices skyrocketed following unfavorable weather conditions in the early months of the year. Indeed, during the first quarter of 2018, vegetable prices were, on average, 55% higher than in 2017, and 48% higher than the average of the last four years.

Figure 2-C: Consumer Price Index of Vegetables



Source: Statistics Mauritius

An increase in fuel prices in December last also added to inflationary pressures in the first quarter. Whereas prices of vegetables are expected to move back closer to their seasonal trends in the second half of the year, there could be additional hikes in the price of fuel in view of the upwardly revised projections of energy prices on international markets. Overall, the inflation rate is forecast to rise to 4.1% in 2018, before gradually falling back to around 2.5% in 2019, assuming a normal weather pattern next year. Excluding vegetable prices, the inflation rate is projected at 3.3% in 2018 and 3.2% in 2019, compared to 3.4% in 2017. Notwithstanding the increase in the headline inflation rate, core inflation has been relatively stable at 2.2% in March 2018, similar to the rate in December 2017, and is expected to remain around this level in future periods as most of the price increase would emanate from volatile portions of the basket, namely food, beverages, tobacco and energy prices, that are excluded in the computation of core inflation.

2.4 External sector

Despite a fall in the value of the dollar, on an annual average basis, and a relatively good performance of the tourism sector, the current account deficit worsened from 4.3% of GDP in 2016 to 6.6% of GDP in 2017, slightly above our November 2017 projection. The widening of the current account deficit came as domestic exports of goods declined by 4.2%, dragged down by the poor performance of the textile sector, while imports went up by 9.3%, driven by fuel and food. Nonetheless, the surplus on the balance of payments improved from 6.0% of GDP to 6.2% of GDP, reflecting significant net financial inflows, particularly in the last quarter of the year. Against this background, the trade-weighted exchange rate of the rupee appreciated on an annual average basis.

Looking ahead, the current account should remain under pressure in 2018 and 2019 as exports of goods, mainly sugar and textiles, continue to struggle. The impact on the external balances would be compounded by higher expected imports related to the implementation of major infrastructure and other construction projects, albeit moderated by a weaker dollar on an annual average basis. On the other hand, the current transfers account should improve as a result of grants by foreign governments linked to the implementation of some earmarked capital projects. On this basis, the current account deficit is expected to narrow to around 4½% of GDP in 2018 and 2019. Based on recent trends, net financial inflows are expected to remain strong. However, these could progressively weaken, but remain overall positive, as interest rates in the US increase and India-related flows slow down towards mid-2019.

Within this context, the effective exchange rate of the rupee is forecast to remain relatively strong. Reflecting projected movements of international currencies in global markets, the rupee is expected to appreciate on an annual average basis against the US dollar, and depreciate vis-à-vis the euro and the pound sterling.

Table 2-C: Mauritius - Selected Economic and Financial Indicators

	UNIT	2014	2015	2016	2017(e)	2018(f)	2019(f)
REAL SECTOR							
GDP at market prices	MUR Bn	392	410	435	460	484	513
GDP at market prices per capita	USD	10,155	9,241	9,598	10,465	11,473	12,259
GDP at basic prices - real growth	%	3.6	3.0	3.6	3.5	3.9	3.9
Gross domestic saving (GDS)	% GDP	10.6	10.5	11.0	10.7	9.9	9.7
Gross fixed capital formation (GFCF)	% GDP	18.9	17.4	17.2	17.3	17.7	17.8
Private sector	% GDP	14.0	12.7	12.4	12.4	12.6	12.6
Public sector	% GDP	4.8	4.7	4.8	4.9	5.1	5.2
Headline inflation	%	3.2	1.3	1.0	3.7	4.1	2.5
Unemployment	%	7.8	7.9	7.3	7.1	7.0	6.9
FINANCIAL SECTOR							
Credit to the private sector (excl. GBL) †	% GDP	70.1	69.8	65.7	67.0	66.9	66.3
Deposits (Segment A)	% GDP	88.2	92.5	95.2	99.0	100.7	101.7
Key Repo Rate	%	4.65	4.40	4.00	3.50	3.50	4.00
Average MUR lending rate*	%	8.01	7.60	7.06	6.59	6.19	6.50
Average MUR deposit rate*	%	3.25	2.90	2.42	1.99	1.71	2.00
Average Treasury Bills rate*	%	2.37	2.14	2.68	2.21	3.54	3.75
GOVT SECTOR							
Budget balance	% GDP	-3.2	-3.2	-3.5	-3.5	-3.2	-3.0
Public sector gross debt	% GDP	60.7	63.6	64.4	63.4	62.7	62.1
EXTERNAL SECTOR							
Balance of visible trade	% GDP	-19.7	-18.2	-18.6	-21.6	-20.4	-20.1
Foreign direct investment (FDI)	% GDP	4.7	2.4	3.1	3.8	3.0	3.0
Current account balance	% GDP	-5.6	-5.0	-4.3	-6.6	-4.4	-4.6
Balance of payments	% GDP	5.9	4.9	6.0	6.2	6.0	4.5
USDMUR annual average change	%	-0.1	14.8	2.1	-3.1	-4.1	-0.9

Sources: Statistics Mauritius, Bank of Mauritius, Ministry of Finance, SBM staff estimates

†End of period * mean of monthly weighted averages (e) Estimates (f) SBM staff forecasts

‡ due to the change in fiscal year from calendar year to a July-June cycle in 2015, 2014 figures relate to calendar year, the 2015 figure relates to the Jan-Jun 2015 period, and the 2016, 2017, 2018 and 2019 figures relate to the Jul15-Jun16, Jul16-Jun17, Jul17-Jun18 and Jul18-Jun19 fiscal years respectively.

Note:
Public sector gross debt excludes the line of credit of USD 500 million from EXIM Bank of India, expected to be raised through SBM (Mauritius) Infrastructure Company Ltd, to finance infrastructure projects on account of the Government.

2.5 Monetary and fiscal policy

On 06 September 2017, the Monetary Policy Committee (MPC) of the Bank of Mauritius brought down the Key Repo Rate by 50 basis points to 3.50% in an attempt to stimulate growth. The MPC took the view that the increasing trend in inflation would taper off and that there was a need to give a boost to productive sectors of the economy. Although inflation has increased further since, the rate was subsequently put on hold as economic expansion is yet to substantively take off, while core inflation remains stable and under control. With no material changes to the growth and inflation dynamics projected in the periods ahead, monetary policy is expected to remain accommodative throughout 2018 and 2019, although the MPC could be tempted to gradually start removing some of the accommodation in view of movements in global interest rates, and if growth rates pick up.

On the fiscal front, based on current trends, the budget deficit is expected to be close to the set target of 3.2% of GDP in financial year 2017/18 as compared to 3.5% in the preceding financial year. The Central Government debt level declined from 59.4% of GDP as at December 2016 to 56.8% of GDP as at December 2017. This drove a decrease in the overall public sector debt level from 64.5% of GDP to 63.2% of GDP over the same period, even though the debt level of public enterprises went up from 6.6% of GDP to 8.0% of GDP. It is projected that Government debt will continue to fall over 2018 and 2019, as many of the major projects currently underway are being supported through external grants. Public external debt stood at 12.5% of GDP as at end December 2017, compared to 12.6% of GDP a year earlier. As per the IMF, public external debt as a percentage of GDP is expected to decline in 2018 and 2019.

2.6 Key risk factors

As both the global and domestic economies are in a transition phase, several risk factors prevail. Downside risks include the following:

1. A reduction in and/or reversal of net financial inflows in the balance of payments

This could be linked to a pullout of capital flows from emerging markets as US interest rates rise. However, the probability of a massive outflow is deemed as remote. More significantly, a material reduction in global business activity after March 2019, particularly as a result of the reviewed Mauritius-India DTAA, could weaken the balance of payments position and dampen growth in business and financial services. Whereas a mild impact has been factored in, a massive net outflow of capital could require a downgrade in growth forecasts. At the same time, it could entail an important depreciation of the currency - which would fuel inflation. The impact should nonetheless be manageable, given the significant international reserves position, while export-oriented sectors could also benefit from a more competitive rupee.

2. A sharp slowdown in world growth

Whilst our projections are based on the assumption of a fairly favorable global environment, an important downgrade - due, for instance, to an escalation of protectionism or geopolitical conflicts - would act as headwinds to export-oriented sectors, such as tourism, and may potentially dent investor confidence. This is likely to impair growth in investment and net exports, thus tempering overall expansion.

3. Volatility in international commodity prices, particularly fuel, and in exchange rates

Fuel prices have increased significantly over the past few months, but a moderation is projected in the second half of 2018 and in the first semester of 2019. However, should the upward trend be maintained, there would be a negative impact on the forecasts for inflation, external balances and, potentially, growth and employment. Similarly, the prognosis for exchange rates has been based on the median of forecasters in the Bloomberg poll, which anticipates a depreciation of the US dollar vis-à-vis the euro and the sterling. These currency dynamics are broadly favorable to Mauritius. Should the reverse happen, which is a possibility particularly if the firming of interest rates in the US is accelerated, growth in net exports could be lower than projected while inflation could be higher.

4. Delayed implementation of projects

Based on recent execution experience, there is reasonable confidence in the expected project timelines, both on the public sector and private sector fronts. However, a series of factors could dent these assumptions including weather conditions, protracted legal cases, and geotechnical conditions, among others. Delays in implementation would directly impact investment, growth and employment.

5. Climatic disruptions

Recently, weather patterns have been relatively atypical and have uncharacteristically affected various parameters in the economy. The projections are based on relatively normal climatic conditions. Hence, in case of major disruptions in the period ahead, the forecasts may have to be revised.

On the upside, a faster transition to a new economic model would positively weigh on macroeconomic conditions. As discussed in previous editions of SBM Insights, this new paradigm would, among others, include:

I. positioning Mauritius as a hub for investments into Africa;
II. transforming the Global Business sector through higher value added services;
III. digitalizing citizen services and reviewing the service delivery model;
IV. facilitating the transition to innovation-driven industries;
V. harnessing the power of renewables, and
VI. attracting, developing and retaining talent.

In this regard, one of the challenges of the forthcoming National Budget would be to develop a coherent strategy, with mutually reinforcing initiatives along the above lines, to facilitate the transformation of the Mauritian economy.

COUNTRY INSIGHTS: GHANA

GHANA: A PROMISING ECONOMIC LANDSCAPE

HIGHLIGHTS

- Ghana (formerly known as Gold Coast) was a British colony until it gained its independence in 1957, becoming the first sub-Saharan country to break free from colonial rule.
- Strong internal and external pressures on the government led to the declaration of a liberal constitution in 1992.
- Since then, Ghana has maintained a steady democratic system of governance. In relation to its African peers, Ghana enjoys a stable, democratic and accountable political system.
- The country possesses a rich and diverse resources base that includes gold, diamond, manganese ore and oil, nonetheless it has had a tumultuous economic past, suffering from prolonged period of serious economic deterioration due to hyperinflation, slack fiscal management and excessive government intervention.
- To rescue the nation from further economic damage, the IMF and the World Bank proposed an economic recovery program (ERP) in 1983, which required the liberalization of the external sector and the implementation of market-oriented policies.
- As a result there was a drastic fall in the inflation rate from over 100% in 1983 to 10% in the 1990s and the country recorded an average GDP growth of 5% per annum over the same period.
- Today, Ghana is more stable and more open to trade and investments compared to neighboring economies, and its economy has changed into one of Africa's rising stars.
- According to the latest provisional GDP estimates, published by Ghana Statistical Service, the Ghanaian economy grew by 8.5% in 2017 compared to 3.7% in 2016 - the fastest growth rate in five years. However, the economy has been struggling with double digit inflation rates for almost a decade. But in 2017, the inflation rate fell from 17.5% in 2016 to 11.8%, closer to BoG's target range.
- Despite significant cocoa, gold and oil exports, the country has experienced sustained current account deficits, as Ghana is dependent on imported refined fuels.
- On 26 March, the monetary policy committee of the BoG decided to reduce the policy rate by 200 basis points to 18.0% from 20.0% - the lowest policy rate in four years.
- In spite of its recent strong macroeconomic performance, Ghana is positioned at the 111th place out of 138 countries, according to the World Economic Forum's (WEF) Global Competitiveness Report 2017-2018.
- The Long-Term National Development Plan (LTNDP) 2018-2057 is a framework, adopted by the Ghanaian government, for the transformation of the economy into a sustained high-growth economy by 2057.
- Both Ghana and Mauritius are committed to achieve the African dream of unity and prosperity among the African people. The gradual realization of projects would generate tremendous benefits to both parties, in terms of growth and wealth creation - eventually establishing an exemplary bilateral relationship in the African continent.

3.1 Background

Situated in West Africa, Ghana (formerly known as Gold Coast) was a British colony until it gained its independence in 1957, becoming the first sub-Saharan country to break free from colonial rule. Between 1964 and 1992, Ghana underwent five military takeovers. Hence, elected political parties have been unable to survive for more than three years without being overthrown in a coup d'état, owing to the characteristics of the political parties themselves. Eventually, strong internal and external pressures on the government led to the declaration of a liberal constitution in 1992. A new constitution was adopted and the multi-party system was restored. Similar to the United States of America, Ghana operates a presidential system whereby the President has executive powers. Elections are held every four years. Since it returned to constitutional rule in 1992, Ghana has maintained a steady democratic system of governance. In relation to its African peers, Ghana enjoys a stable, democratic and accountable political system. The foundation of the system is based on strong principles of good governance, respect of human rights and adherence to the rule of law.

3.2 Economic Landscape

Ghana possesses a rich and diverse resources base that includes gold, diamond, manganese ore and oil. Similar to many of its African peers, the agricultural sector remains the main source of employment. The sector employs nearly 42% of its working population and contributes approximately 19% to GDP; cocoa is the key cash-crop, providing about one third of export receipts. Nonetheless, Ghana has had a tumultuous economic past. The Ghanaian economy suffered from a prolonged period of serious economic deterioration due to hyperinflation, slack fiscal management and excessive government intervention. In order to rescue the nation from further economic damage, the IMF and the World Bank proposed an economic recovery program (ERP) in 1983.

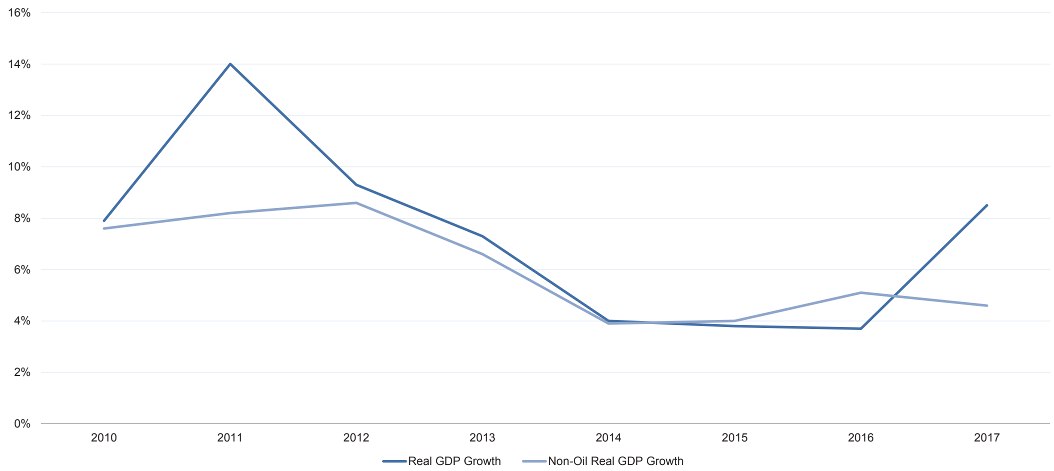
The ERP required the liberalization of the external sector and the implementation of market-oriented policies. Through the execution of this program, Ghana has been able to restore macroeconomic stability. A key evidence is the drastic fall in the inflation rate from over 100% in 1983 to 10% in the 1990s and the country recorded an average GDP growth of 5% per annum over the same period. Since then, establishing and maintaining macroeconomic stability have been a major policy goal for the government, and a number of structural reforms have been put in place. Today, Ghana is more stable and more open to trade and investments compared to neighboring economies, and its economy has changed into one of Africa's rising stars.

Nonetheless, the economy suffers from numerous challenges, including logistical and infrastructural deficiencies while the market potential is stifled by problems associated with energy supply. To address these shortcomings, a PPP legal framework has been put in place and the government has developed a national infrastructure plan. Besides, as a member of ECOWAS, Ghana has signed an interim Economic Partnership Agreement with the EU that will open the country up to trade. It also continues to explore the establishment of a Continental Free Trade Area for the West African region. Furthermore, Ghana has applied the Common External Tariff (CET), as agreed by members of ECOWAS. All these measures taken by the government are expected to boost medium and long term economic growth.

3.3 Recent Economic Performance

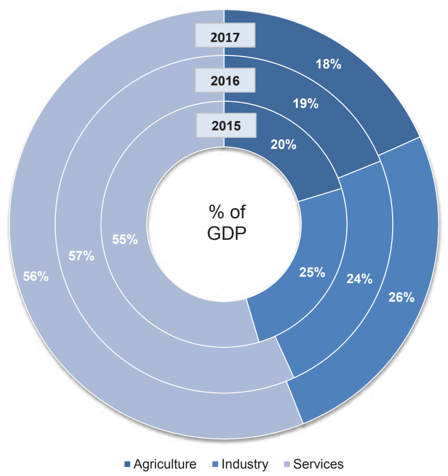
According to the latest provisional GDP estimates, published by Ghana Statistical Service, the Ghanaian economy grew by 8.5% in 2017 compared to 3.7% in 2016 – the fastest growth rate in five years. The industrial sector recorded the highest growth rate of 16.7%, on the back of surging oil and gas output. The start of production at the Sankofa oil field in May 2017 contributed largely to the rise in oil and gas production, thus boosting the country's finances. The agricultural sector registered a growth rate of 8.4% while the services sector – which is the largest contributor to GDP, with a share of 56.2% in 2017 – grew by 4.3%.

Figure 3-A: Ghana's GDP Growth Performance, 2010-2017



Source: Ghana Statistical Service

Figure 3-B: Composition of GDP, 2015-2017



Sources: Ghana Statistical Service, Ministry of Finance

The Ghanaian economy has been struggling with double digit inflation rates for almost a decade. The Bank of Ghana's (BoG) target range for inflation is 6% - 10%, but the actual rate has frequently exceeded the upper bound. The inflation rate fell from 17.5% in 2016 to 11.8% in 2017, that is, closer to BoG's target range. Factors that contributed to the decline were: lower utility prices, exchange rate stability and the transmission effect of earlier increases in the monetary policy rate. The IMF expects Ghana to witness a further decline in the inflation rate during 2018, with a forecast average level of 9% due to the fading effects of the 2015-2016 drought, a more stable exchange rate, and benefits obtained from the IMF Extended Credit Facility (ECF) agreement.

Table 3-A: Selected Macroeconomic Indicators

SELECTED MACROECONOMIC INDICATORS	UNIT	2013	2014	2015	2016	2017	2018(f)	2019(f)
GDP, constant prices	% Change	7.3	4.0	3.8	3.7	8.4	6.3	7.6
GDP, current prices	USD Bn	47.8	38.8	36.9	42.8	47.0	51.6	56.7
Population	Mn	25.6	26.2	26.9	27.6	28.3	29.0	29.7
GDP per capita, current prices	USD	1,870	1,479	1,372	1,552	1,663	1,780	1,907
GDP per capita in PPP terms	USD	4,061	4,191	4,290	4,394	4,730	5,013	5,374
Total investment	% GDP	13.3	18.8	16.7	14.5	13.6	14.2	15.3
Gross national savings	% GDP	1.3	9.3	9.0	7.8	9.1	10.1	11.3
Inflation, average consumer prices	%	11.7	15.5	17.2	17.5	12.4	8.7	8.0
Volume of imports of goods and services	% Change	1.7	-15.0	0.9	-2.9	8.7	4.9	5.8
Volume of exports of goods and services	% Change	9.6	3.4	-8.4	5.8	31.0	-0.7	7.0
General government revenue	% GDP	16.7	18.4	19.6	17.2	17.5	17.9	18.0
General government total expenditure	% GDP	28.7	29.4	25.0	26.1	22.5	23.0	21.7
General government gross debt	% GDP	57.2	70.2	72.2	73.4	71.8	69.1	65.9
Current account balance	% GDP	-11.9	-9.5	-7.7	-6.7	-4.5	-4.1	-4.0

Source: IMF World Economic Outlook Database, April 2018 (f) Forecasts

Despite significant cocoa, gold and oil exports, the country has experienced sustained current account deficits, as Ghana is dependent on imported refined fuels. Additionally, the imports of capital goods for the development and maintenance of oil refineries have contributed to the current account deficit. Encouragingly, Ghana's current account deficit has been on a narrowing trend since 2016 on account of the launch of the TEN (Tweneboa, Enyenra, Ntomme) oilfield as well as growing gold exports. The IMF forecasts the current account deficit to narrow further to 4.5% of GDP in 2017. As a result of the improving external sector, the domestic currency remained stable throughout 2017. Overall, the Ghanaian Cedi (GHS) depreciated by 4.9% against the USD year-on-year, the strongest performance of GHS against USD since 2011. However, given the high dependency on commodity exports, the current account is vulnerable to price shocks. Adverse international price movements would likely translate into a worsening deficit, which would put pressures on the exchange rate and on inflation.

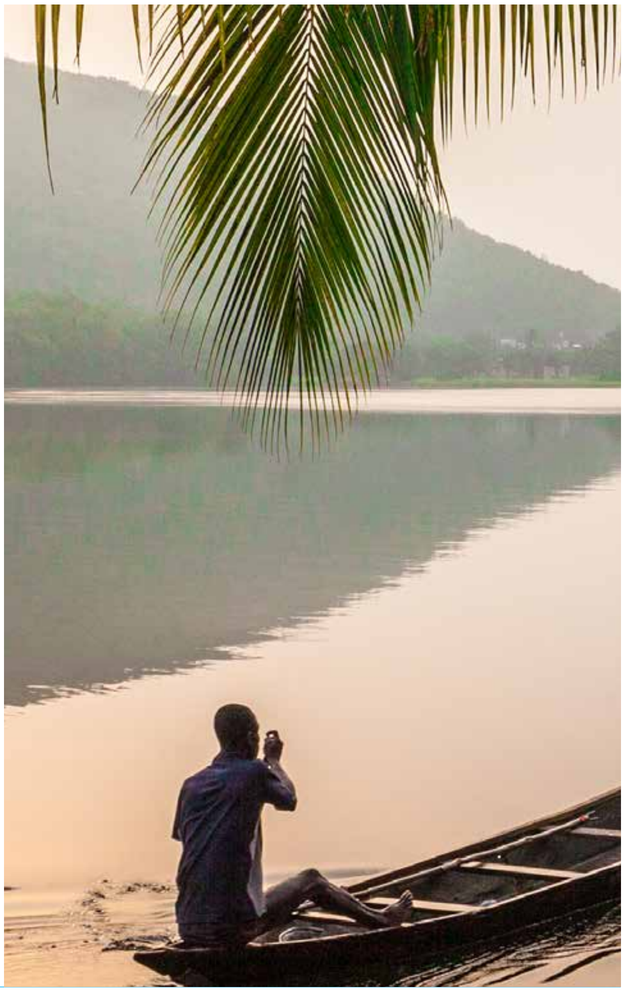


Table 3-B: Top Trading Partners for Exports and Imports of Goods, 2016

EXPORTS

COUNTRY	VALUE (USD Mn)*	SHARE
Switzerland	1,775	18%
India	1,480	15%
UAE	1,356	13%
EU 28	1,343	13%
China	895	9%
Vietnam	522	5%
Burkina Faso	406	4%
South Africa	333	3%
Mali	285	3%
Togo	276	3%
Others	1,416	14%
TOTAL	**10,087**	**100%**

IMPORTS

COUNTRY	VALUE (USD Mn)*	SHARE
EU 28	3,378	31%
China	1,867	17%
USA	838	8%
India	502	5%
South Africa	317	3%
UAE	274	3%
Turkey	273	3%
South Korea	264	2%
Brazil	260	2%
Canada	225	2%
Others	2,626	24%
TOTAL	**10,824**	**100%**

Source: Eurostat
* The original figures are in EUR. They have been translated to USD at 1.0517 using Bloomberg end-Dec 2016 exchange rate.

Ghana has suffered from large fiscal deficits over the last decade, leading to significant increases in public debt and eroding the fiscal buffers created by earlier debt relief. Fiscal slippages have been particularly pronounced in election years, setting in motion an increase in external and domestic imbalances from which Ghana has only partially recovered. The IMF forecasts that Ghana's fiscal deficit will be equivalent to 4.5% of GDP in 2017, a substantial improvement compared to the level experienced in 2013 where the deficit was equal to 12% of GDP. Ghana has an ongoing USD 918 million credit program with the IMF that aims to restore fiscal balance: this comes after there was an unreported gap in the former administration's budget. However, financing conditions have recently eased, and Ghana's external credit spreads have continued to decline from their peak in early 2016. The government had a record bond issuance of over GHS 9 billion (equivalent to USD 2.2 billion) in April 2017, mostly acquired by non-resident investors.

On 26 March, the monetary policy committee of the BoG decided to reduce the policy rate by 200 basis points from 20.0% to 18.0% - the lowest policy rate in four years. This decision was highly expected by market experts. The downward revision in the interest rate was as a result of relatively subdued inflationary pressures and the expected convergence of the inflation rate toward the BoG target range of 6% - 10% in the medium term. It is expected that the growth momentum experienced in 2017 will continue in 2018, evidenced by the BoG Composite Index of Economic Activity which grew by 3.1% year-on-year in January 2018. The central bank's confidence surveys conducted in February also indicated positive opinions on growth prospects, realization of business expectations and general improvements in the economy.

Following its monetary policy committee meeting, BoG released its latest statistics regarding public debt. As at December 2017, public debt stood at GHS 142 billion, representing 69.8% of GDP. Compared to December 2016, this is a considerable improvement in the debt situation (Dec-16: 73.3%), but it remains at a worrying level, as already cautioned by the IMF. Fiscal consolidation by the government is expected to improve the debt metrics further going forward.

3.4 The Ghanaian Financial Sector

Overall, the banking sector is profitable, liquid and solvent although asset quality is a major cause for concern. Return on assets improved from 17.8% at the end of December 2016 to 18.8% at the end of December 2017 while efficiency indicators on cost to income remained largely unchanged compared to the previous year. The banking industry's capital adequacy ratio (CAR), which fell to 14.8% in June 2017 after the Asset Quality Review exercise, increased to 18.0% at the end of December 2017, significantly above the 10.0% prudential requirements after the implementation of capital restoration plans in the sector.

Other financial soundness indicators recorded some improvements, but the quality of banks' loan portfolios remains a source of concern as the non-performing loans (NPLs) ratio rose from 21.6% at the end of October 2017 to 22.7% in December 2017, with over half of these loans in the loan loss category. Adjusting for the loss category that has been fully provisioned for, the ratio drops to a still high 10.8%. Debts owed to banks by state owned enterprises (SOEs) especially in the energy sector have been a primary cause of defaults. The energy sector levy was introduced as part of the solution to retire these nagging facilities in the books of banks. The restructuring and ongoing payment of the legacy debts owed by SOEs to banks, are expected to lead to an improvement in the NPL ratios in the long term.

Credit to the private sector by banks grew steadily from 6.8% in August 2017 to 12.8% in December, on a year-on-year basis. The gradual increase in private sector credit extension was supported by some easing of credit stance on loans to small, medium and large enterprises. However, despite the 20% GDP contribution from the agriculture industry, banks are generally reluctant to extend credit to the agriculture, forestry and fishing sectors of the economy due to their largely informal nature. Subsistence farming, inaccessible farms and inadequate skills to improve efficiencies may have contributed to the insignificant exposures to this sector. Almost a third of the industry's loans and advances is concentrated within commerce and finance. Gradually, manufacturing is becoming less attractive, and loans and advances to the manufacturing sector have declined. The sector is experiencing reduced margins arising from high cost of capital, limited access to inputs, high cost of utilities and unreliable power supply. The elevated risk profile of manufacturing concerns does not encourage banks to extend credit facilities to customers in this sector.

Table 3-C: Financial Soundness Indicators

INDICATORS	DEC-13	DEC-14	DEC-15	DEC-16
	%	%	%	%
Capital Adequacy				
Regulatory capital to risk-weighted assets	18.5	17.9	17.8	17.8
Regulatory Tier 1 capital to risk-weighted assets	14.7	15.3	14.6	14.4
Asset Quality				
Non-performing loans to total gross loans	12.0	11.3	14.7	17.3
Profitability				
Return on assets	6.2	6.4	4.6	3.8
Return on equity	31.1	32.2	22.1	18.0

Source: IMF

3.5 Credit Profile

In October 2017, Standard and Poor's affirmed Ghana's long-term foreign sovereign credit rating at "B-" but revised its outlook to positive on the possibility of an upgrade to "B" over the next 12 months. The rating agency stated that the "B-" status has been maintained due to the substantial debt in the energy sector that could exert pressure on the country's finances. Late payments from state-owned organizations in the sector have led to the accumulation of non-performing loans in the banking sector. Nonetheless, Standard and Poor's is optimistic that the situation is improving as the government has implemented measures to strengthen public finances - hence, the positive outlook. The rating agency perceives that the new leadership will spearhead an ambitious economic reform program, accompanied by sound fiscal consolidation. A rating upgrade would hinge on market improvements in the fiscal and external balances, and on an effective monetary policy transmission mechanism. However, Standard and Poor's reckoned that the outlook on Ghana's rating could be returned to stable if economic growth is materially lower than expected. A sluggish economic growth would be viewed as a potential impediment to the establishment of a firm fiscal consolidation path.

Table 3-D: Sovereign Risk Ratings

CREDIT RATING AGENCY	RATINGS	OUTLOOK	DATE
Moody's Investors Service	B3	Stable	Feb-18
Fitch	B	Stable	Sep-17
Standard & Poor's	B-	Positive	Oct-17

Sources: Moody's Investors Service, Fitch Ratings & S&P Global Market Intelligence

In September 2017, Fitch affirmed Ghana's long-term foreign Issuer Default Ratings at "B" and maintained a stable outlook. The "B" rating is based on the assumption of increased oil production in 2017-2018 and a rise in international oil prices. According to Fitch, the main factors that could result into a negative rating action are: (i) failure to narrow the fiscal deficit, (ii) inability to reduce the government debt-to-GDP ratio, and (iii) a decline in international reserves. A positive rating action would be taken if Ghana reduces its current deficit, fiscal deficit and government debt as well as promotes macroeconomic stability.

Moody's affirmed Ghana's issuer rating at "B3" and retained the stable outlook in February 2018. The rating agency mentioned that the rating affirmation was the result of the following improving conditions:

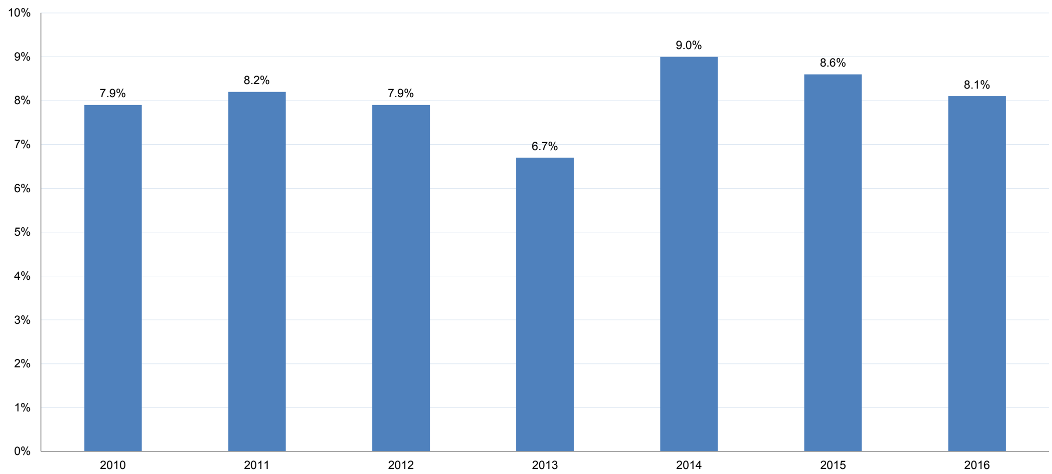
I. lower, albeit still elevated, borrowing needs;
II. progress with the restructuring of substantial debts of state-owned power utilities, and
III. benefits to growth and the external accounts from the hydrocarbon production boost following the coming on-stream of the Sankofa oil field.

Nevertheless, it also stated that the country is still plagued by persisting credit challenges including a high debt burden; weak debt affordability; and weak fiscal institutions reflected in revenue target underperformance. The stable rating outlook mirrors the rating agency's view that risks to the B3 rating are balanced. Factors that would contribute to an upward revision to the credit rating are: continued fiscal consolidation consistent with revenue projections and arrears clearance commitments, in particular if they lead to a material and sustained reduction in the government debt-to-GDP ratio. Conversely, a downgrade to the credit rating would be triggered by factors such as funding constraints to meet the government's financing requirements and a continued underperformance with respect to revenue targets.

3.6 Foreign Direct Investment

According to UNCTAD, FDI inflows to Ghana increased by 9% from USD 3.2 billion in 2015 to USD 3.5 billion in 2016. The total number of projects registered in the first three quarters of 2017 was 139 with a total estimated investment value of approximately USD 3.4 billion, according to the Ghana Investment Promotion Centre (GIPC). The FDI component was USD 3.25 billion against USD 1.8 billion recorded in the same period in 2016, representing an 80% increase. The manufacturing sector recorded the highest number of investments with 37 projects, followed by the services sector with 34 projects. The agriculture sector recorded only one project whilst there was no investment recorded in the tourism sector. From January to September 2017, China was the leading source of investments in terms of number of projects, registering 25 projects. In terms of FDI value, Netherlands topped the list, followed by India.

Figure 3-C: FDI Inflows (% of GDP)



Source: UNCTAD

Table 3-E: Investment Projects

TOP SOURCES OF INVESTMENTS (NO. OF PROJECTS) Q1 – Q3 (2017)	
China	25
India	19
UK	13
South Africa	8
Turkey	8
USA	6
France	5
Mauritius	5
Netherlands	4
Denmark	3
Germany	3

INVESTOR COUNTRIES BY FDI VALUE (USD MN)	
Netherlands	2,438
India	412
France	139
UK	54
China	49
Denmark	22
DRC	20
Mauritius	17
USA	15
Canada	12

Source: GIPC

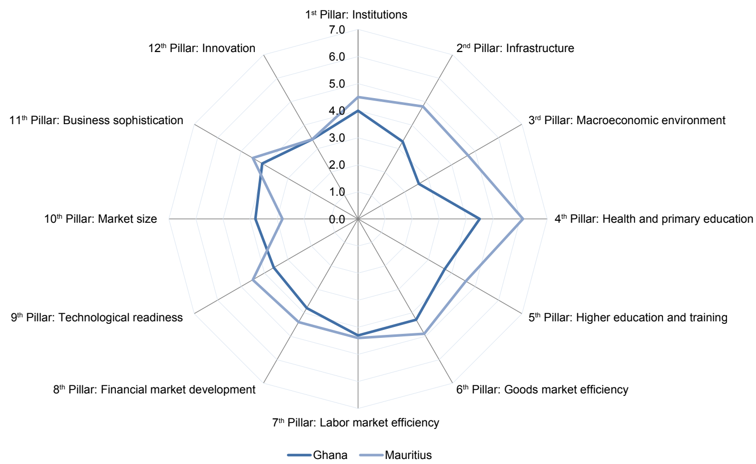
In spite of its recent strong macroeconomic performance, Ghana is positioned at the 111th place out of 138 countries, according to the World Economic Forum's (WEF) Global Competitiveness Report 2017-2018. In the African region, the nation is positioned at the 13th place. It gained 3 places from its 2016-2017 ranking. Ghana's best performance was in the 12th pillar - Innovation - where it ranked 57th on the global stage followed by at the 59th, 60th and 62nd position in institution, business sophistication and labor market efficiency, respectively. The country's worst performances were in health and primary education (120th) and macroeconomic environment (131st).

Table 3-F: International Rankings

PUBLICATIONS	RANKING	
	2016-2017	2017-2018
Ease of Doing Business	108th out of 190	120th out of 190
WEF Global Competitiveness Index	114th out of 138	111th out of 138
Index of Economic Freedom	118th out of 186	122nd out of 186
Corruption Perceptions Index	70th out of 176	81st out of 176
Human Development Index	139th out of 188	NA
Global Gender Gap Report	59th out of 144	72nd out of 144
Mo Ibrahim Index	7th out of 54	8th out of 54

Sources: World Bank, World Economic Forum, The Heritage Foundation, Mo Ibrahim Foundation, Transparency International

Figure 3-D: Ghana's Competitiveness



Source: World Economic Forum

3.7 The Long-Term National Development Plan

The Long-Term National Development Plan (LTNDP) 2018-2057 is a framework for the transformation of the Ghanaian economy into a sustained high-growth economy by 2057. It also provides a transparent basis for measuring the performance of the government. The government sees it as an innovative approach to blending continuity and change in an evolving democratic environment. The process is guided by ten medium term (4-year) plans which will be translated into annual plans linked to a relevant fiscal budget.

The LTNDP has five strategic goals, namely to:

- build an industrialized, inclusive and resilient economy;
- create an equitable, healthy and disciplined society;
- build safe, well-planned and sustainable communities;
- build effective, efficient, and dynamic institutions for development; and
- strengthen the country's role in international affairs.

The reforms needed for this includes changes to competition policy, industrial policy, consumer protection laws and land use laws.

Despite improvements to conditions for growth, macroeconomic stability will continue to be challenged by a volatile currency and relatively high inflation heading into 2018. Real GDP growth is likely to rise to 6.3% in 2018 as inflation falls and small and medium-sized enterprises gain access to funds as the main policy rate is lowered. The government has agreed to an extension of the IMF credit facility – this will help with fiscal consolidation measures in 2018.

Ghana has the potential to record modest real GDP growth of 4.0% - 7.0% in the medium to long term but, as its stands, this is largely dependent on exports of commodities such as oil, gold and cocoa. Going forward, the government is seeking to diversify the economy in order to reduce reliance on commodities for growth and employment. The ensuing shift in the economic structure from the primary to the secondary and tertiary sectors would drive growth in net exports and an improvement in productivity, while integrating a greater number of workers in the formal sector. As a result, tax revenue should increase which, alongside other fiscal consolidation measures, would help reduce the pressure on the budget deficit and the public debt level.

Meanwhile, the government has shown commitment to dealing with power supply shortages and ensuring investment in key infrastructure. Oil production should rise in 2017-18, in line with output from the TEN project and Sankofa-Gye Nyame oil fields, and this will contribute to an increase in economic growth. Positively, a recent maritime border dispute with Cote d'Ivoire was settled in favor of Ghana and ensures that the TEN project will continue to generate revenue for the country. Increasingly business-friendly policies, a stable political environment, a relatively very young population and the country's large natural resources provide a strong foundation for future economic growth. Ghana does not suffer from the inter-ethnic and tribal conflicts that have derailed many African countries' development, but gaps in the provision of education and youth unemployment remain important challenges to the long-term outlook.

3.8 Business/Investment Opportunities

As indicated in the Ghanaian 2018 Budget Statement, there are plans to invest heavily in agriculture with a focus on mechanization and also to ensure rapid industrialization of the economy. The Ministry of Finance has set out a list of policy initiatives to be implemented in 2018 in its latest budget and some have been tabled below:

Area	Project Opportunity
Construction	• The completion of the construction of a dry bulk jetty at Takoradi port and a new container terminal at the Tema port • The construction of 10,000 housing units of various types in all the regional capitals of Ghana • The construction of reinforced concrete drains in selected flood prone areas across Ghana • The completion of the construction of greenfield airports and the rehabilitation of existing airports • The construction of a new terminal building, extension of the existing runway and other ancillary facilities at the Kumasi Airport • The completion of the construction of a new terminal, currently about 57% complete, to accommodate up to five million passengers yearly • The construction of 35 major roads and 99 bridges
Employment and Labour	• Formulation of a National Labor Migration Policy with a view to facilitating labor migration and protecting the Ghanaians who embark on work-related foreign travels
Infrastructure	• The construction of 340 km Kojokrom-Kumasi Western railway line • The construction of 85 km Tema-Akosombo railway line, to facilitate the transfer of cargo to and from the Tema Port • The development of the Eastern railway line and the Boankra Inland Port - the government is looking for strategic investors
Fisheries and Aquaculture	• To increase domestic fish production and offset fish imports, eventually making Ghana a net exporter of fish by 2030, the government will implement an Aquaculture Development Program
Education	• The implementation of a Free Senior High School policy and the setting up of a Voluntary Education Fund • The government will grant relief from corporate income tax paid by privately-owned and managed universities • The alignment of public Technical and Vocational Education and Training (TVET) institutions under the Ministry of Education and the construction of 20 modern TVET schools and 10 regional Science, Technology, Engineering and Math (STEM) centers
ICT	• The construction of an Information and Communications Technology (ICT) Park to promote Research and Development and entrepreneurship among the youth • The completion of the commercialization of 50% of the 780 km eastern corridor fibre optic project - to raise revenue • The extension of mobile network services to all areas where access is currently unavailable

3.9 Bilateral Relations – Ghana and Mauritius

In 2015, Ghana and Mauritius signed three memoranda of understanding on bilateral cooperation with a view to strengthening the already extensive bilateral, trade and political ties between the countries. The signed agreements are as follows:

Mutual Visa Exemption - waiving visa requirements for Mauritian nationals holding ordinary, diplomatic and service passports who wish to travel to Ghana for a period not exceeding 90 days, and vice versa. The objective is to enhance interconnectivity and the movement of people between the two countries.

Standardization and Conformity Assessment - elimination of non-tariff barriers and enhancing trade relations in areas of standardization and conformity assessment to promote and facilitate trade between Ghana and Mauritius.

Tertiary Education - providing for mutual recognition of qualifications, inter-university linkages, staff and student exchanges, academic scholarship programmes, collaborative research and funding.

It is well known that Mauritius has been a pioneer in the development of the free zone, through the successful establishment of an EPZ in the 1970s and the creation of a freeport in 1992. This development strategy was adopted to boost the country's economic growth. As such, several African peers have sought the assistance of the Mauritian government to develop such free zone models in their respective countries, including Ghana. In 2015, a G-to-G agreement was signed with Ghana for the development of a SEZ for the setting up of a Technology and Business Park in Accra. The project is expected to be conceptualized in two phases. The first phase will cover an area of 6.1 hectares with an investment of USD 260 million while the second phase will comprise an area of 37 hectares. The Park will accommodate a cyber tower, a three-star hotel, a polyvalent centre of conferences and an apartment block.

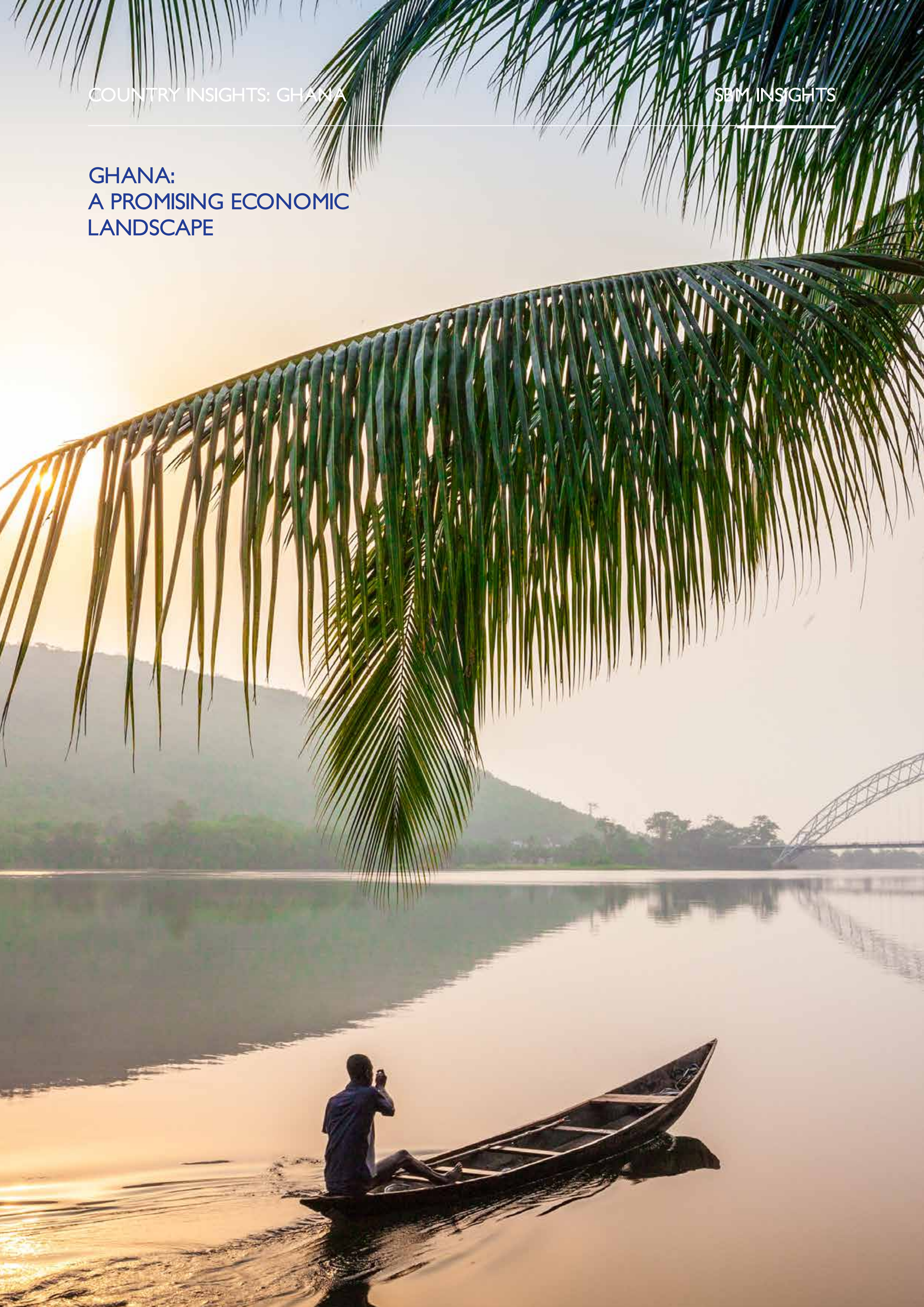
Ghana and Mauritius embarked on a new journey of cooperation with the signing of a Double Taxation Avoidance Agreement in 2017. The objective of the agreement is to create a conducive business environment for investors willing to engage in large cross-border activities, through the elimination of double taxation which has been a barrier to economic activities between the two countries. The agreement is yet to be ratified. Concurrently, a Permanent Joint Commission on Bilateral Cooperation was set up to consolidate trade interests. Ghana and Mauritius have agreed to collaborate in various fields namely (i) arts and culture; (ii) gold and jewelry with the setting up of the Mauritius International Derivatives and Commodities Index; and (iii) collaboration between the Utility Regulatory Authorities – for the benefit of both parties at both regional and international levels.

Several other projects are in the pipeline, such as:

I. the setting up of a Joint Trade and Investment Committee;
II. the conclusion of a memorandum of understanding between the Mauritius Chamber of Commerce and Industry and that of Ghana for the setting up of a business council and development of the ICT, handicraft and health sectors, with the possible recruitment of Mauritian health practitioners in Ghana; and
III. the assistance of Ghana for the setting up of a slavery museum in Mauritius.

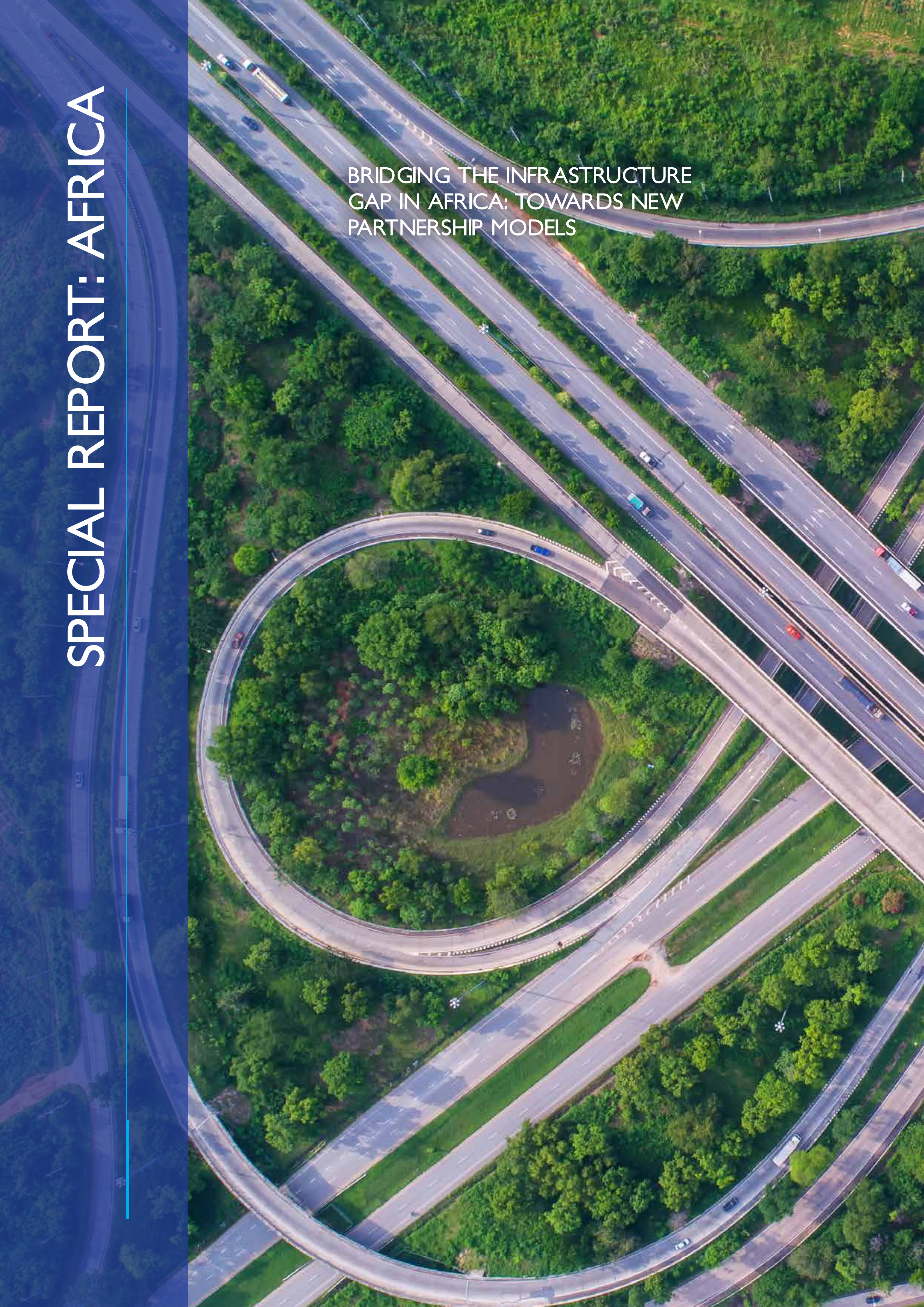
It is believed that there are many other potential arenas of collaborations in sectors such as sugar and textile. Since both Ghana and Mauritius are committed to achieving the African dream of unity and prosperity among the African people, the gradual realization of such projects would generate tremendous benefits to both parties, in terms of growth and wealth creation – eventually establishing an exemplary bilateral relationship in the African continent.

GHANA: A PROMISING ECONOMIC LANDSCAPE



SPECIAL REPORT: AFRICA

BRIDGING THE INFRASTRUCTURE GAP IN AFRICA: TOWARDS NEW PARTNERSHIP MODELS



HIGHLIGHTS

- Infrastructure is a recurrent topic in policy debates and its provision is a catalyst for economic growth and development.
- According to the World Bank and the African Development Bank, Mauritius is among the leading countries in Africa when it comes to infrastructure provision.
- However, sub-Saharan Africa lags behind in terms of infrastructure. Recent estimates from the 2018 African Economic Outlook of the African Development Bank point toward a spending requirement of between USD 140 billion to USD 170 billion; corresponding to an estimated annual gap of between USD 68 billion to USD 108 billion. (AfDB, 2018)
- The traditional way of financing public infrastructure projects, that is, through government expenditure, places a strain on the public budget and adds to the debt burden of a country.
- There is a pressing need to involve private investors in the financing of public infrastructure projects. Financing from large pools of capital such as pension funds or private equity funds is an avenue that needs to be explored.
- Nevertheless, investing in Africa can prove to be challenging mainly due to low savings rates, poor institutions and underdeveloped financial markets.
- Despite the many challenges, infrastructure investments in Africa can be attractive as they may potentially offer higher returns than similar investments elsewhere, while partly ring-fencing risks, if properly structured.
- Investing in infrastructure projects in Africa will require complex financial and resilient legal structures to form a coalition of stakeholders (banks, suppliers, governments, end users and investors) and to ensure that the interests of each stakeholder are reasonably protected.
- In order to promote investment in African infrastructure, there is also the need to develop financial instruments that reconcile the idiosyncrasies of the African infrastructure landscape with the risk/return profile of potential investors.

4.1 Overview of the African Infrastructural Landscape

Since its independence, the Mauritian economy has been able to adequately respond to infrastructure demands, making the small island nation one of the leading African countries in terms of the quantity and quality of infrastructure provided (Boston Consulting Group, 2017, Calderon and Serven, 2010). In its 3 year strategic plan 2017-2020, the Mauritian government put forward 62 key capital projects with a total value estimated at MUR 62 billion spread over the period 2017 to 2020. While the Mauritian economy prepares itself to meet a growing infrastructure demand, most of its sub-Saharan African peers have lagged behind.

Indeed, countries in sub-Saharan Africa (SSA) are still plagued by the low quantity and the poor quality of infrastructure. Electricity production falls short of demand and its distribution is inadequate. 5 out of 10 people do not have access to electricity (AfDB, 2018) and about 79% of firms suffer from power outages which, on average, last for 5.7 hours, reducing total sales value for firms by 8.3% (Enterprise surveys, 2016). Limited access to clean drinking water and precarious sanitation have also afflicted the continent leading to poor health conditions and outbreaks of disease in certain regions. The access to piped running water in SSA stands at only 68% compared to a world average of above 90% (2015 estimate) (World Bank, 2018). This has a high cost for the African economies; it is estimated that inadequate water and sanitation cost Africa 5% of its GDP each year (AfDB, 2014).

Roads are the most predominant mode of transport in Africa but the lack of spending on road development and maintenance leave the roads in poor condition. Despite the fact that roads carry at least 80% of goods and 90% of passengers, only 53% of such roads are paved. Consequently, less than half of Africa's population has access to reliable roads, resilient to climatic conditions (AfDB, 2014). Moreover, deficient roads cause about 225,000 fatalities every year in Africa.

While Africa has lagged behind in the provision of power, water, sanitation and transport facilities, the continent has seen impressive development in the communications sector. The rapid growth of the telecommunications industry is being fueled by the increased affordability of mobile phones, an emerging middle class, competitive offers from service providers and rapid urbanization. From 2007 to 2017, mobile telephone subscription penetration rate increased from 23.5 per 100 inhabitants to 77.8, representing an annualized growth of 12.7%. Over the same period, the number of households having an internet connection increased at a yearly rate of about 13% (International Telecommunications Union, 2018). The high growth figures in the telecommunications industry, especially the mobile-cellular sector have attracted strong interests from private investors. This has considerably narrowed the spending gap that exists in the sector; in fact, over the period of 2005 to 2013, about two thirds of total "private participation in public infrastructure" (PPI) finance was allocated to the telecommunications industry (Brookings Institutions, 2015).

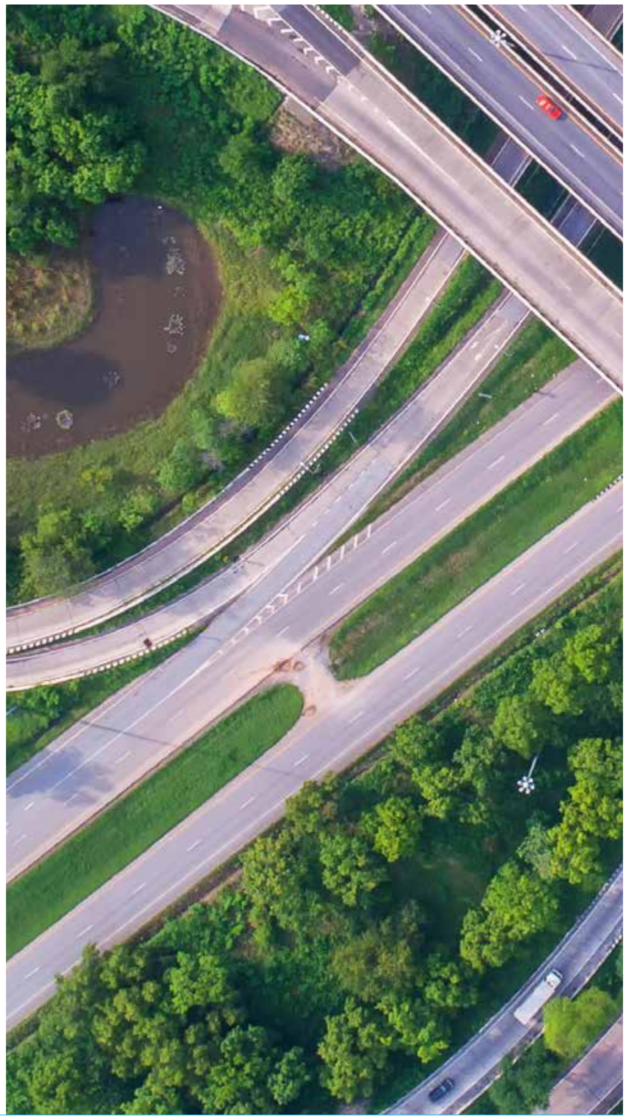


Figure 4-A: Estimate of the African Infrastructure Funding Gap in Energy, Transport and WSS* Industries

ENERGY	TRANSPORT	WSS*	
Power demand will increase 93% up till 2035	Roads carry at least 80% of goods and 90% of people	Access to water in Africa's poorest countries has recently increased to 68%	
Electrification rate stands at only 46% across the continent.	Around 225,000 road accidents are recorded yearly	Most of the bodies of fresh water in Africa are controlled by several governments	
Nearly 700 million people live without clean cooking facilities	53% of roads are unpaved	Water treatment and purification facilities are inadequate	
Electricity coverage is at 65% in urban areas and 28% in rural ones	Inefficient connectivity among ports, railways and roads	Adverse climate and geography coupled with limited storage facility	
USD Bn	USD Bn	USD Bn	
35-50	35-47	56-66	Requirements
20	24.5	10.5	Current Spending
15-30	10.5-22.5	45.5-55.5	Gap

*WSS: Water Supply and Sanitation

Infrastructure provision can also be gauged by analyzing the spending gaps in different sectors, namely energy, transport and water supply and sanitation (WSS) (See Figure 4-A). The spending gap is calculated as the spending requirement to achieve a target level of infrastructure minus the current spending level. In the energy sector, it is estimated that yearly spending ranging from USD 35 billion to USD 50 billion will be needed to achieve an electrification rate of 100% in urban areas and 95% in rural areas (AfDB, 2018). With current spending of USD 20 billion in 2016, the energy sector faces an annual spending gap estimated between USD 15 billion to USD 30 billion. Similarly, yearly spending between USD 56 billion and USD 66 billion will be needed to achieve 100% access to water and sanitation in both urban and rural Africa (AfDB, 2018). However, spending in 2016 totaled USD 10.5 billion, leading to a spending gap of USD 45.5 billion to USD 55.5 billion. In the transport industry, reaching the objective of preserving and maintaining 80% of current capacity and further developing an additional 20% capacity in the form of new roads, railways, airports and harbors would require an annual spending of USD 35 billion to USD 47 billion (AfDB, 2018). The transport sector faces an annual spending gap estimated between USD 10.5 billion to USD 22.5 billion with spending in 2016 amounting to USD 24.5 billion only. As mentioned above, the telecommunications sector has seen a considerable increase in funding in recent years and with a total spending of USD 1.6 billion in 2016, the spending gap to reach 50% mobile coverage ratio and a 10% fibre penetration rate in households, stands between USD 2.4 billion to USD 5.4 billion.

Therefore, taking into consideration the energy, transport, WSS and telecommunications industries and factoring in potential efficiency gains, the infrastructure spending gap in Africa is estimated between USD 68 billion and USD 108 billion (AfDB, 2018).

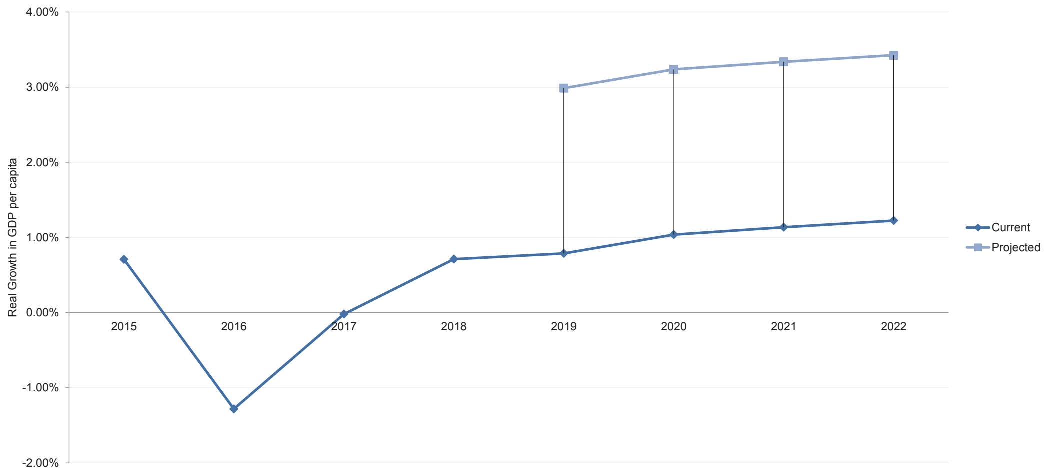
4.2 Investing in Infrastructure: Potential Benefits and Challenges

4.2.1 Potential Benefits

Good quality infrastructure is vital for the proper functioning of an economy. It increases economic growth through an increase in total factor productivity (TFP), which is a measure of how efficiently an economy's resources are used in production. Additionally, good infrastructure is synonymous to higher capital spending which, through the multiplier effect, increases the GDP of an economy.

Calderon (2009) attempted to assess the impact of infrastructure on GDP per capita. By measuring the infrastructure stock and the quality of infrastructure in several countries, Calderon established that Mauritius was among the African leaders in terms of infrastructure. With further extrapolation, it was found that raising SSA infrastructure to the Mauritian level would increase the region's annual real growth in GDP per capita by a significant 2.3 percentage points.

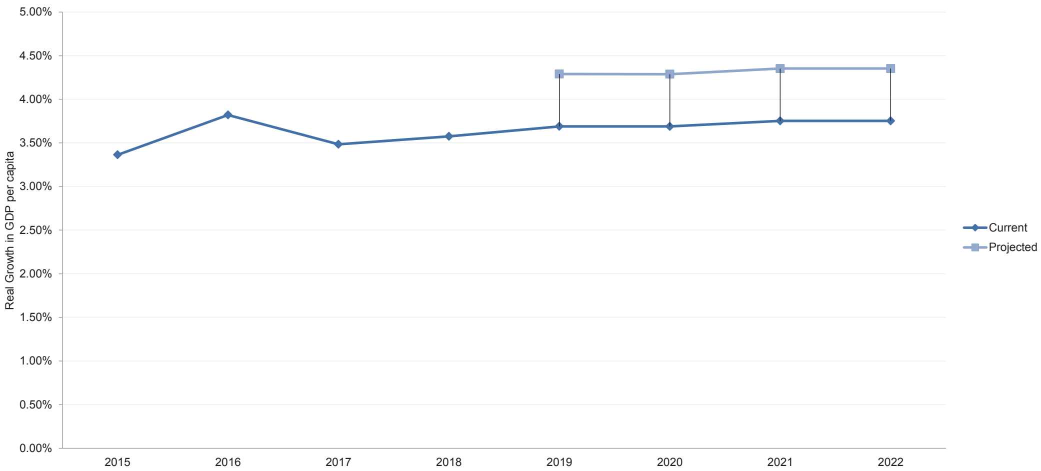
Figure 4-B: SSA Projected Growth with Infrastructure at Mauritian Level



Source: World Bank, Calderon (2009)

Furthermore, Calderon (2009) claimed that even if Mauritius was among the African leaders in terms of infrastructure, there was still room for improvement. Enhancing the infrastructure stock and quality to the level demonstrated by a representative Western European country would increase Mauritius' GDP growth per capita by 0.6 percentage point per annum.

Figure 4-C: Mauritius Projected Growth with Representative European Country Infrastructure Level



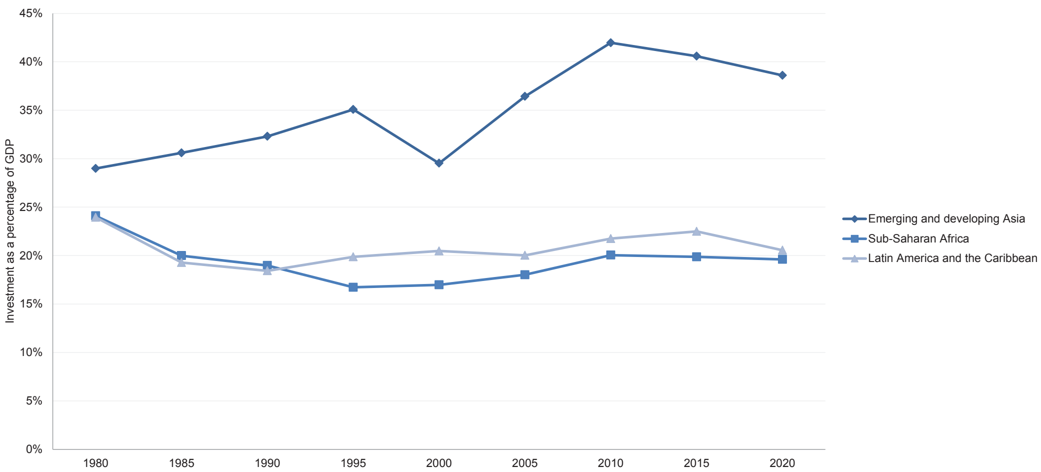
Source: World Bank, Calderon (2009)

4.2.2 Challenges

(i) Low Savings and Investment

Despite the potential benefits of improving infrastructure provision, Africa faces relatively low spending levels as summarized by the large infrastructure spending gap mentioned above. Such a gap is reflected in the low level of investments in the SSA region.

Figure 4-D: Investment Levels in Selected Regions



Source: World Economic Outlook, IMF

Over the last 3 decades, the level of investment in sub-Saharan African economies has declined from 24% of GDP in 1980 to less than 19% of GDP in 2017. While such a trend is comparable to South America, it is far behind the investment path of Emerging and Developing Asia. The difference between the investment levels in Africa and Asia is partly due to the difference in savings rates.

Savings are essential for the good running of an economy because they provide the resources for investment. They may take the form of bank deposits, investment in financial instruments, or increased cash holdings. Through financial intermediation (loans & investments), bank deposits generate excess cash holdings which are saved by households, leading to further savings and investments. Similarly, savings may be channeled to investment managers who will invest to generate higher excess cash holdings, leading to higher savings and investment. However, savings outside the investment cycle (i.e. savings in cash) represent an outflow and do not generate additional cash holdings that can be reinvested.

The low savings rate implies that there is limited scope for raising capital domestically. The alternative of raising funds internationally is inevitably more expensive as the rate of return expected by investors has to price in a higher liquidity risk (because of underdeveloped financial markets), potential foreign exchange risks (if capital is raised in local currency) and higher default risks associated with poor institutions and geopolitical instability. Therefore, the limited availability of domestically raised capital and the higher costs associated with internationally sourced capital often result in sub-optimal investment levels in many African countries.

Figure 4-E: The Savings Cycle

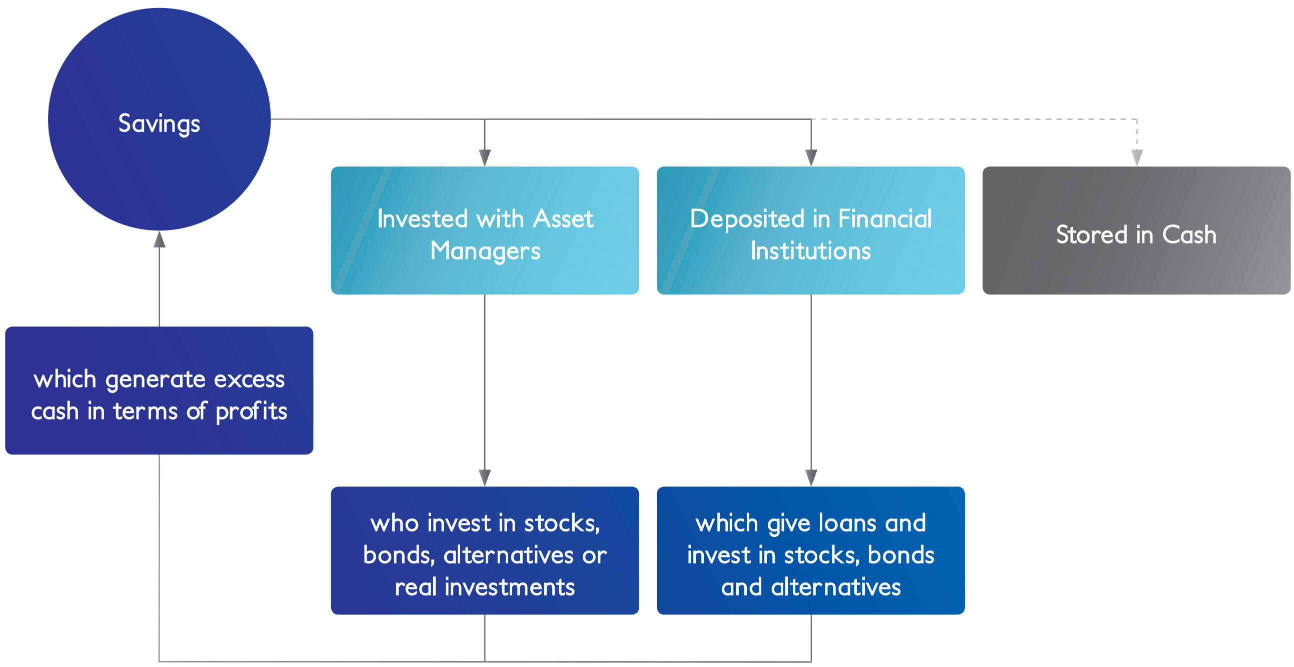
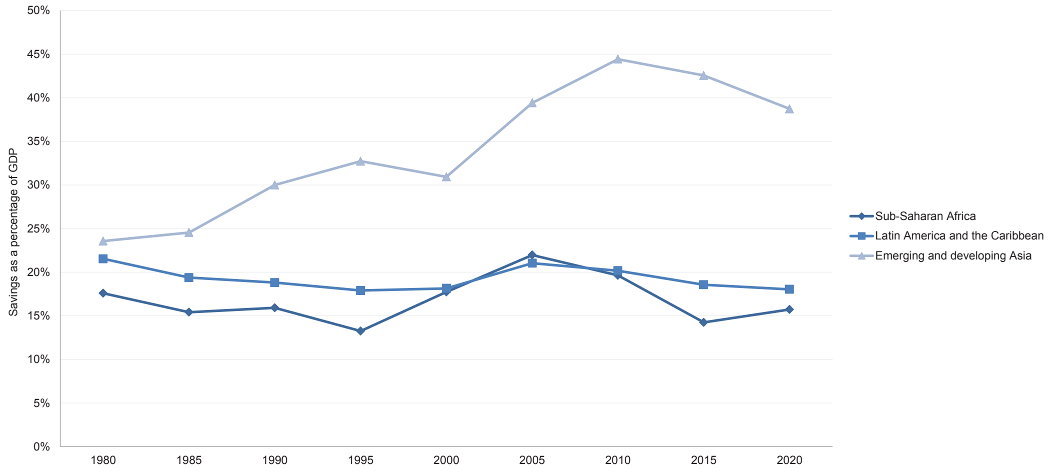
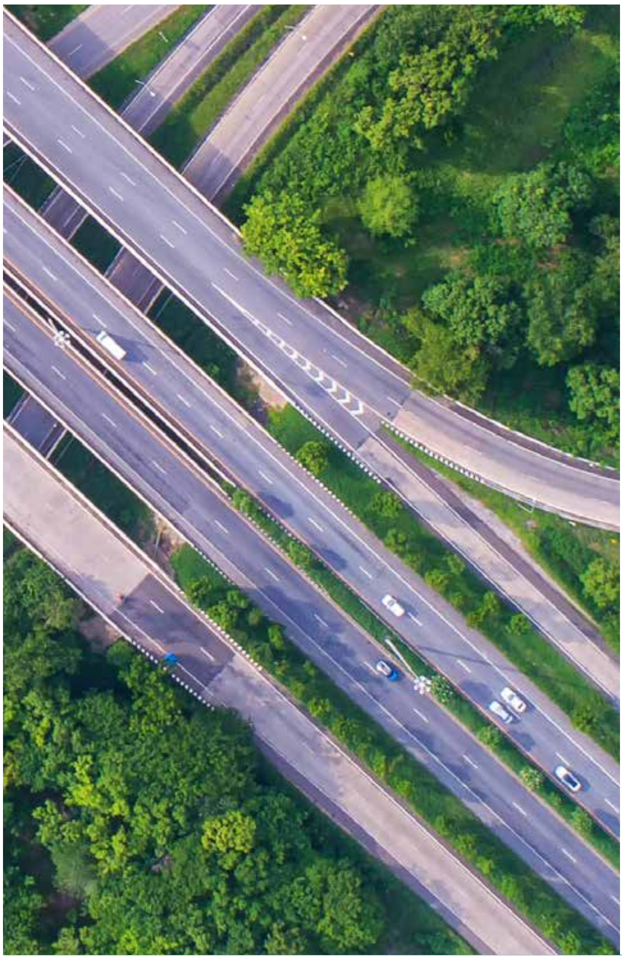


Figure 4-F: Selected Savings Rates



Source: World Economic Outlook, IMF

Even though the low savings rate may account for the lack of investment in infrastructure in Africa, the inability to transform savings into investment is also a major shortcoming of African financial markets. With the exception of South Africa and Nigeria, African financial markets are very narrow and are often underdeveloped, offering mostly plain vanilla opportunities to investors. Furthermore, funds from large pools of capital such as pension funds are rarely used outside of South Africa (Boston Consulting Group, 2018). In fact, some economies including Mauritius have excess of private savings but, due to under-developed financial markets, the amount of funding channeled to profitable projects, including infrastructure, is sub-optimal.

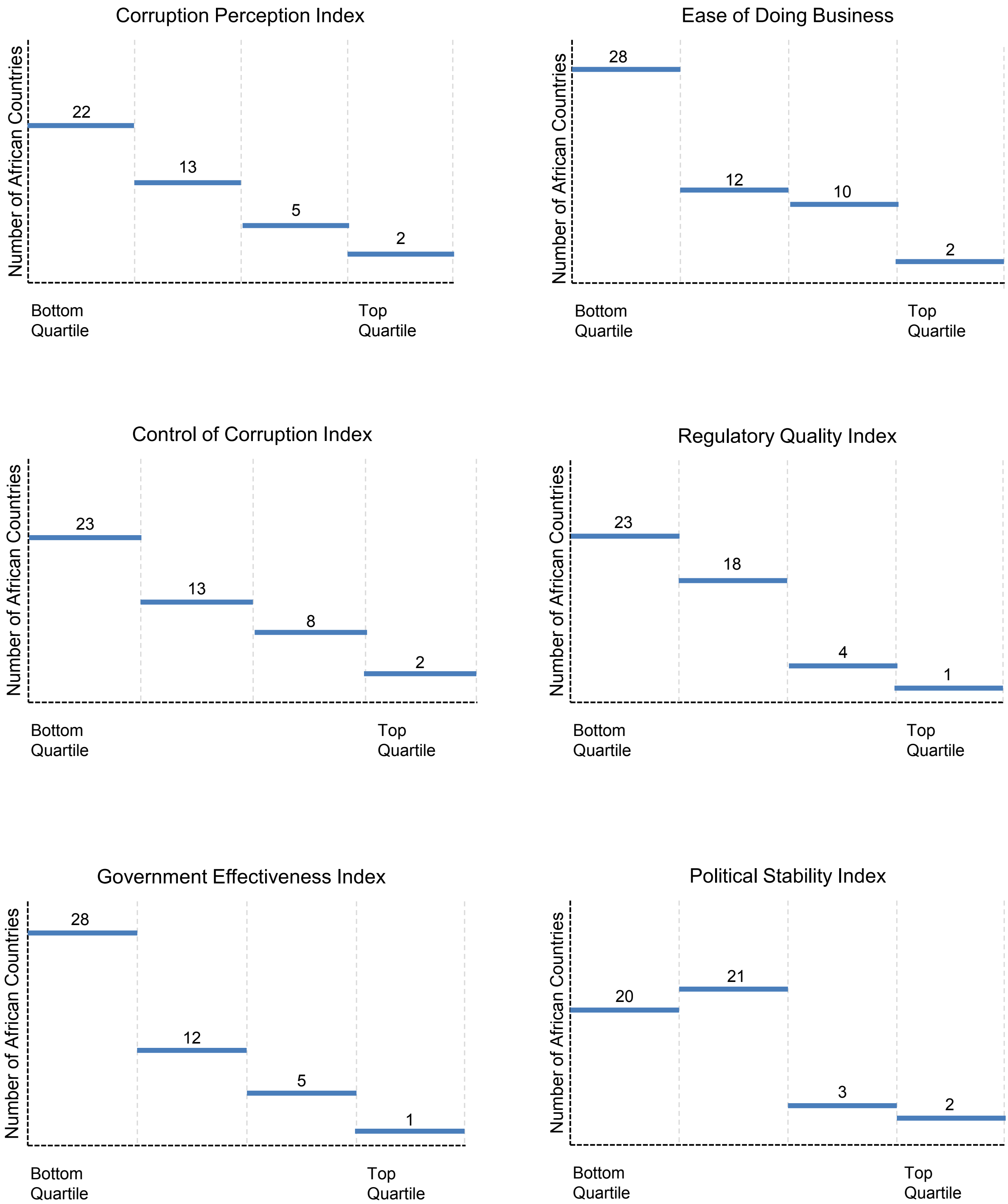


(ii) Africa's Poor Institutional Quality

While adverse geography, unfavorable climatic conditions, lack of openness and over-dependence on the primary sector have been blamed for Africa's low economic growth, there is consensus that the lack of robust institutions is one of the continent's main obstacles. Institutions can be defined as rules that are upheld by society over a long enough time to make a difference to individual actors (North, 1990). They englobe the protection of property rights, the enforcement of contracts, the rule of law and social capital amongst other determinants of long-run economic performance (Aron, 2000).

Poor institutional quality largely contributes to the lack of investment in African economies as it erodes investor confidence. Institutional quality can be measured by various indicators among which the World Bank Governance Indicators, the Ease of Doing Business Index and Transparency's International's Corruption Perception Index.

Figure 4-G: Selected Governance Indicators



Source: World Bank; Transparency International

Africa's generally poor institutional quality is reflected in the presence of many countries at the bottom of the different indicators of good governance (See Figure 4-G). Weak institutions which render the outcome of a project more uncertain add to the risk premium of an investment. Consequently, some investors may expect a higher return (increasing the cost of raising finance) from such investments while others may not invest at all.

(iii) Economic Challenge

Rent-seeking behavior, the lack of good public administration, a weak regulatory environment and the inability to control corruption often result in inefficient use of resources, especially financial resources. Consequently, in many cases, the authorities attempt to relieve the strain placed on the country's finances by either increasing the money supply or by borrowing, both locally and internationally. While these measures may relieve the pressure on the economy's finances in the short run, they can also hinder long-term economic stability. Increasing the money supply without any growth in real output inevitably leads to inflation. In fact, SSA's inflation rate stands at 11% compared to an average of 4.2% for emerging markets and developing economies (IMF, 2018). Similarly, increased borrowing negatively impacts the exchange rate of some African currencies. As at 2017, 16 countries were facing adverse exchange rate conditions according to IMF's Exchange Rate Market Pressure (EMP) (AfDB, 2017).

Debt overhang is also a common feature of several African economies and this induced the World Bank and the IMF to create the HIPC (Heavily Indebted Poor Countries) initiative in 1996. The HIPC initiative is a debt relief program aimed at reducing poverty and bringing debt to sustainable levels in developing countries. As at 2017, 36 countries of which 30 African ones had received the full amount of debt relief they were eligible to under the HIPC and related initiatives (World Bank, 2017). However, public debt is still a concern for many African countries. From 2014 to 2016, the median public debt to GDP ratio increased by 11 percentage points from 37% to 48% (AfDB, 2017). Moreover, out of the 28 countries that are in debt distress or face a high risk of debt distress, half are in Africa (IMF, 2018).

(iv) Project - Related Risks

In addition to traditional risks (interest rate, FX, liquidity), investment in infrastructure poses additional risks and challenges. Greenfield infrastructure projects involve a construction risk, that is, the risk that the final deliverable (such as a road, bridge, power station, etc.) is not constructed on time or is not constructed at all. The construction risk is exacerbated by the fact that some African regions face a weak regulatory environment, an unstable political landscape and generally low public sector capabilities. As a result, investment in infrastructure in certain regions of the continent can prove to be a very risky endeavor. A high construction risk also implies a high debt refinancing risk as any potential delays may cause the entity responsible for project to default on their debt obligations.

African infrastructure projects are also hindered by the lack of local skillful labor. This has been the result of a long-term tendency of awarding contracts to non-African companies, limiting the scope for knowledge and technology transfer (Boston Consulting Group, 2017). Consequently, the implementation of infrastructure projects requires the employment of internationally sourced labor and expertise to fill in the gaps and this imposes extra costs to the project. Another alternative would be to train the local workforce. However, training is also synonymous to extra costs and involves a time lag before the locally trained staff/worker contributes to the project.

Long gestation periods are generally common for infrastructure projects, especially large-scale ones. Gestation periods are even longer in African infrastructure projects. In fact, a project gestation period of seven to ten years is typical in Africa, compared to three to five years elsewhere (Boston Consulting Group, 2017). A period of seven to ten years normally covers at least two electoral cycles, increasing the risks related to political and policy uncertainty. Thus, the increased risks related to the high gestation periods call for a higher risk premium for the investment, therefore increasing the cost of capital. Moreover, another disincentive to invest in infrastructure projects is the significant upfront costs related to research, feasibility studies, environmental impact assessment and similar activities. This is a peculiarity of the African infrastructural landscape; feasibility and R&D costs are generally not borne by the private investor in other parts of the world. It is estimated that such costs can amount to 5% to 15% of total cost (Boston Consulting Group, 2017).

4.3 Bridging the Infrastructure Investment Gap: Some Potential Avenues

4.3.1 The Cascade Approach: A Ranking of Financing Solutions

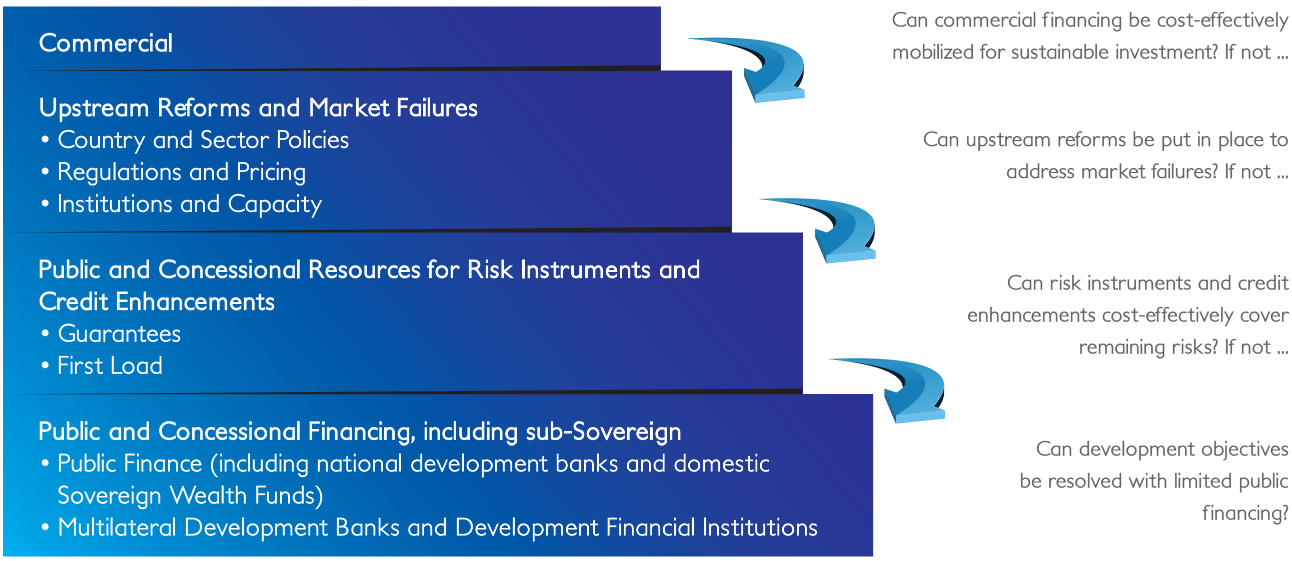
While government expenditure remains the most common way of financing infrastructure projects, other means of finance are on the rise. Recently, the increased presence of China in the African infrastructure landscape has led to the initiation and completion of several projects, especially in the transport sector. Through its private equity and venture capital fund, the China Africa Development Fund (CADF), Beijing has invested over USD 3.5 billion in 87 projects across 30 countries (Forum on China-Africa Cooperation, 2016). The fund had a capacity of USD 5 billion and, in 2015, China's President Xi Jinping, proposed an additional USD 5 billion to add to the capacity of the fund (Forum on China-Africa Cooperation, 2016)

Although Chinese investments in African infrastructure possess some of the elements of private finance, they cannot be construed as a purely private investment. The fact that the CADF is ultimately financed by the Chinese government, which may pursue non-financial objectives such as building political ties with African countries, renders the purely financial motive debatable. As a result, despite the significant inflow of capital from China, the lack of private finance in African infrastructure is still relevant.

The World Bank has been championing private investment in African infrastructure since the mid-1990s, claiming that 50% of infrastructure projects can be funded by private investors (World Bank, 1994). It recommends a 'cascade approach' to investment in infrastructure. This approach deploys finance based on a hierarchy of considerations where the best option for infrastructure financing is a purely commercial one. The objective behind the promotion of private finance in infrastructure is two-fold:

I. Make a more efficient use of public and concessional resources and
II. Minimize public debt levels and transfer the investment risks and rewards to the private sector.

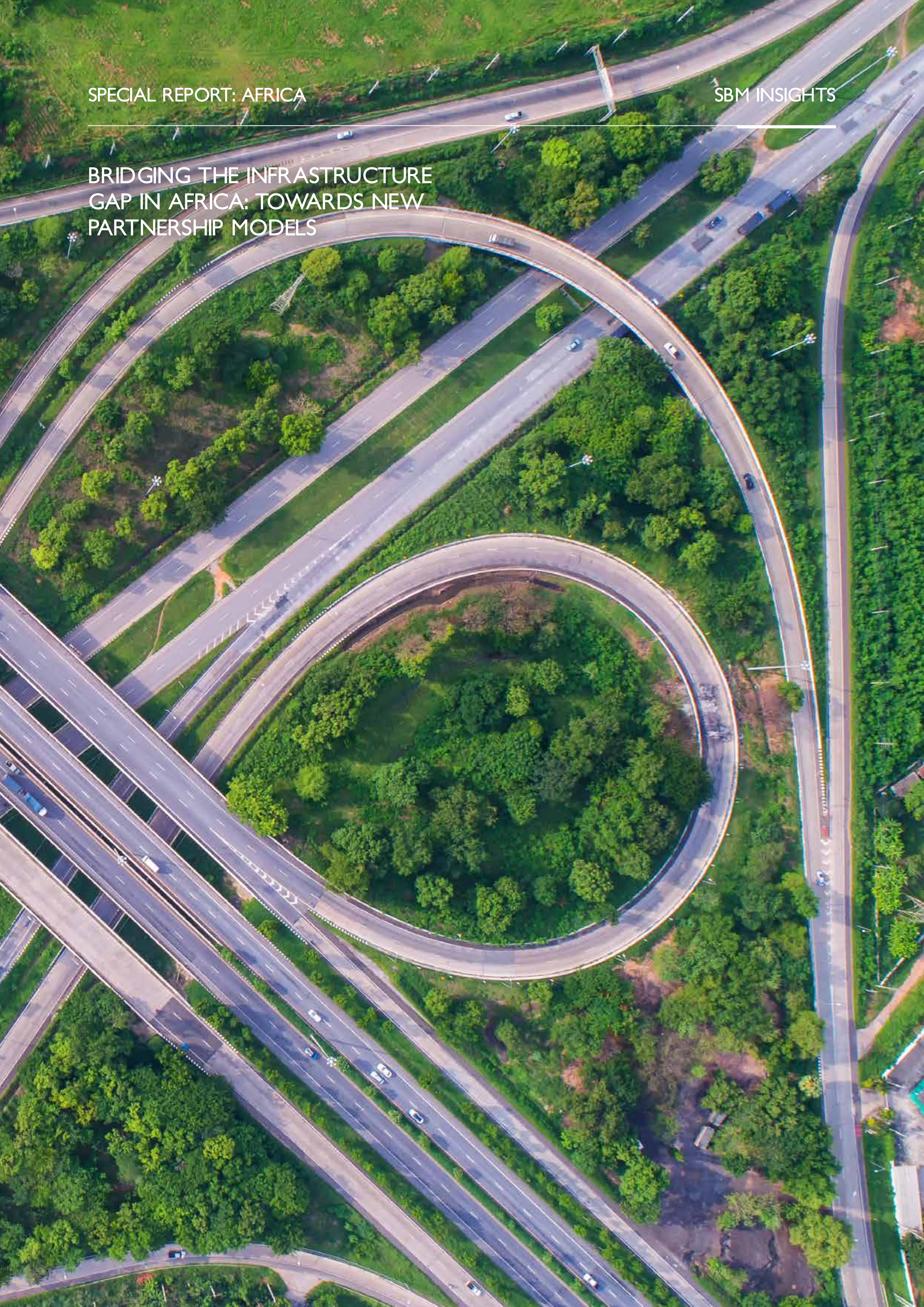
Figure 4-H: The Cascade Approach



Source: World Bank, AfDB

The cascade approach has four levels of diagnosis. The first point is to identify whether the infrastructure project can be financed by commercial means only. If commercial financing is not viable due to risks of market failures, the best alternative would be to attempt to implement reforms to strengthen policies, regulations and institutions. If risks and costs remain high after the implementation of reforms, financing costs can be lowered by deploying public resources into risk-sharing instruments such as guarantees. If credit enhancements are not effective in making commercial finance viable, the last resort would be to mobilize public and concessional resources.

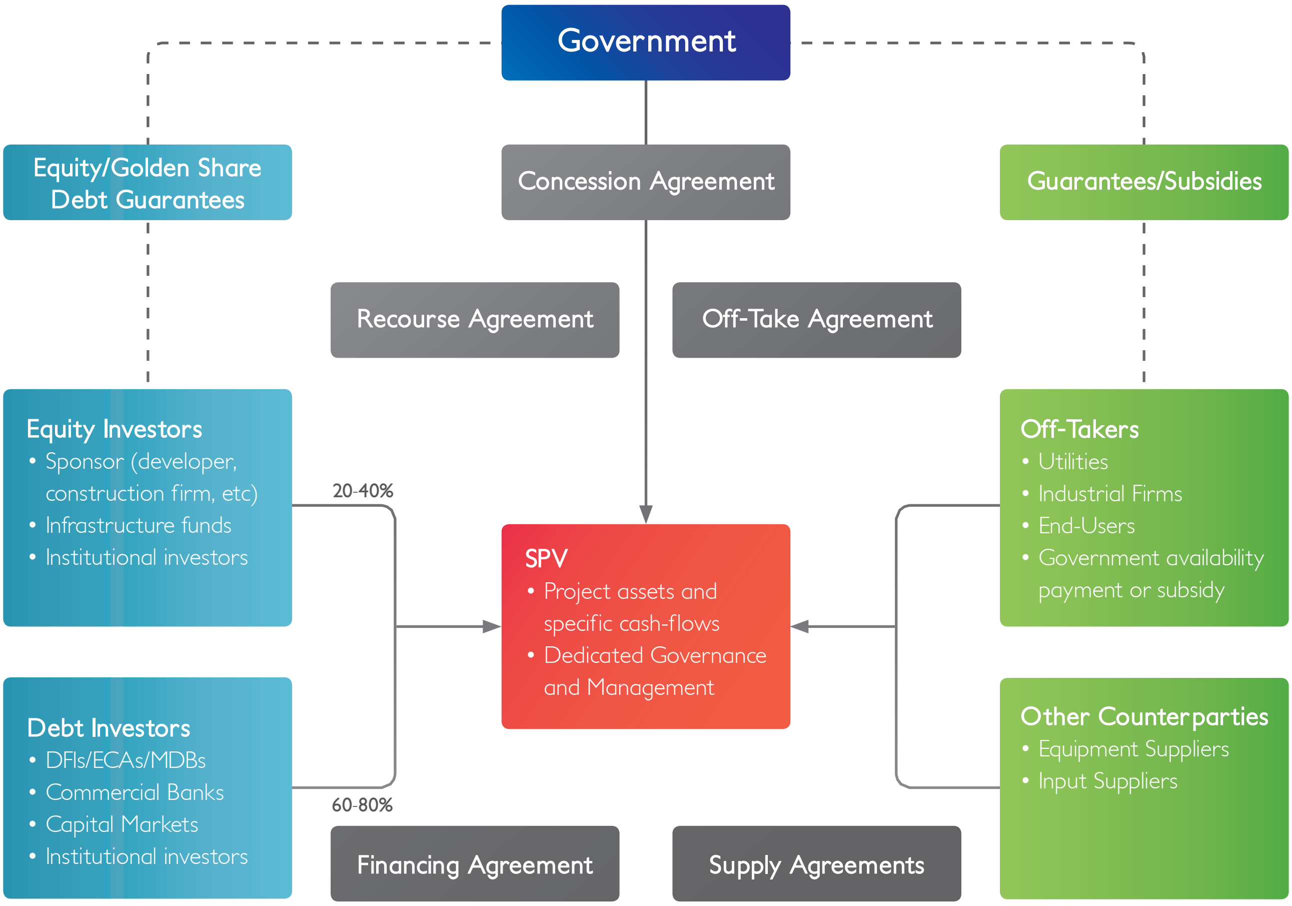
BRIDGING THE INFRASTRUCTURE GAP IN AFRICA: TOWARDS NEW PARTNERSHIP MODELS



4.3.2 Project Finance

In the cascade approach to infrastructure financing, all the solutions to infrastructure financing require some form of coalition among the different stakeholders, i.e. the government, the investors, the financial institutions and the suppliers. However, the coalition will only be successful if the interests of all the stakeholders are reasonably protected. A project finance structure with the investment of multiple stakeholders would be ideal to finance large and risky projects. Project finance can be viewed as a series of agreements and risk mitigation mechanisms that allow sponsors who do not have an extensive capital base to finance large infrastructure projects.

Figure 4-I: A Project Finance Structure



Source: AfDB

The project finance structure comprises several parties:

- The **government** acts as the main facilitator of the project. It grants the sponsor of the project the right to operate a specific business through the concession agreement. It may also mitigate the risks of low take up by an off-take agreement. Moreover, the government can also reduce the project risks in different ways. One of them is by a recourse agreement where the lender has the right to put a charge on the borrower's assets should s/he default on his/her obligations. Another way of mitigating financial risks is by offering debt guarantees to the lenders. The government may also grant subsidies to the off-taker (i.e. the end-user of the project) to support its credit worthiness.

- The **special purpose vehicle (SPV)** is the entity responsible for the project assets and specific cash flows. The SPV is generally a stand-alone subsidiary of a larger company and its sole purpose is to ensure the proper execution of the infrastructure project. Its main source of cash for debt service is the cash flow generated from the project.

- The **off-taker** is typically the end-user or the purchaser of the output of the project. It is the main source of cash flow for the SPV. An example of an off-taker in Mauritius would be the Central Electricity Board (CEB) buying power from independent power producers (IPPs).

- The **supplier** will supply the inputs necessary to complete the project. They normally deal with the SPV.

- The **sponsors** are generally the equity investors of the project and they take part in the risks involved. Such sponsors can be the owner of the SPV, infrastructure funds and institutional investors. The sponsors will normally oversee the operations of the SPV. An example of a sponsor in Mauritius would be a sugar estate overseeing the operations of their energy-producing line of business.

- **Lenders/debt investors** are key participants in the project finance structure. Debt finance typically accounts for 60% to 80% of a project. Lenders can be Development Financial Institutions (DFIs), Export Credit Agencies (ECAs), Multilateral Development Banks (MDBs) or commercial banks. Debt finance can also be raised from capital markets through bonds issuance.

While the project finance structure described in Figure 4-I provides a good framework to finance infrastructure, it is not a blanket solution. The financial and legal framework of the project finance structure should be modified to accommodate the idiosyncrasies of different projects. In parallel, there is a need to develop financial instruments that suit not only the financing requirements of the project but also the risk/return profile of potential investors.

Case Study: The Mauritian Energy Sector

The Mauritian Energy sector is a good example of how good policies and cooperation among the different stakeholders of the economy can contribute to infrastructural development.

In 1997, following the recommendations of the World Bank, Mauritius was able to address the challenges associated with a growing demand for electricity by increasingly involving the private sector in energy production through the 'Independent Power Producers' (IPP) scheme. Under this new framework, with IPPs producing more electricity, the Central Electricity Board was able to reduce its contribution to total electricity produced, therefore shifting parts of its costs and risks to the private sector.

The success of IPPs in Mauritius was based on several key enablers:

- **Policy:** The Mauritian authorities put forward the Multi Annual Adaptation Strategy (MAAS) which encouraged sugar producers to diversify their operations following a drastic fall in the price of sugar. This motivated sugar estates to scale up their power plants by adding electricity production from coal to their existing bagasse-based production.
- **Guarantees:** The CEB offered the IPPs an off-take agreement where all the power produced would be bought at a guaranteed price. Therefore, risks of low take-up and price fluctuations are mitigated.
- **Commercial Funding:** The strong Mauritian financial sector allowed the sugar producers to raise funds to finance their diversification into electricity production.

Since the scaling up of the power stations, IPPs contribution to electricity production increased from 17% in 1991 to 60% in 2015 (Statistics Mauritius, 2017).

The IPP scheme is not a flawless model and, since its introduction, it has often been criticized for various reasons. Nonetheless, it has been beneficial to the Mauritian economy in many ways. Since its inception, part of the costs and risks associated with electricity production were transferred to the private sector and this had the benefit of relieving the pressure on the finances of the CEB. Moreover, the IPP scheme has been the precursor to other programs such as the Small Independent Power Producers (SIPP) Scheme whereby households are encouraged to produce their own electricity from renewable sources. Additionally, with the cane industry facing declining sugar prices in the 1990s, electricity production through the IPP framework was an opportunity for diversification, which helped revive a sunset industry at that time.

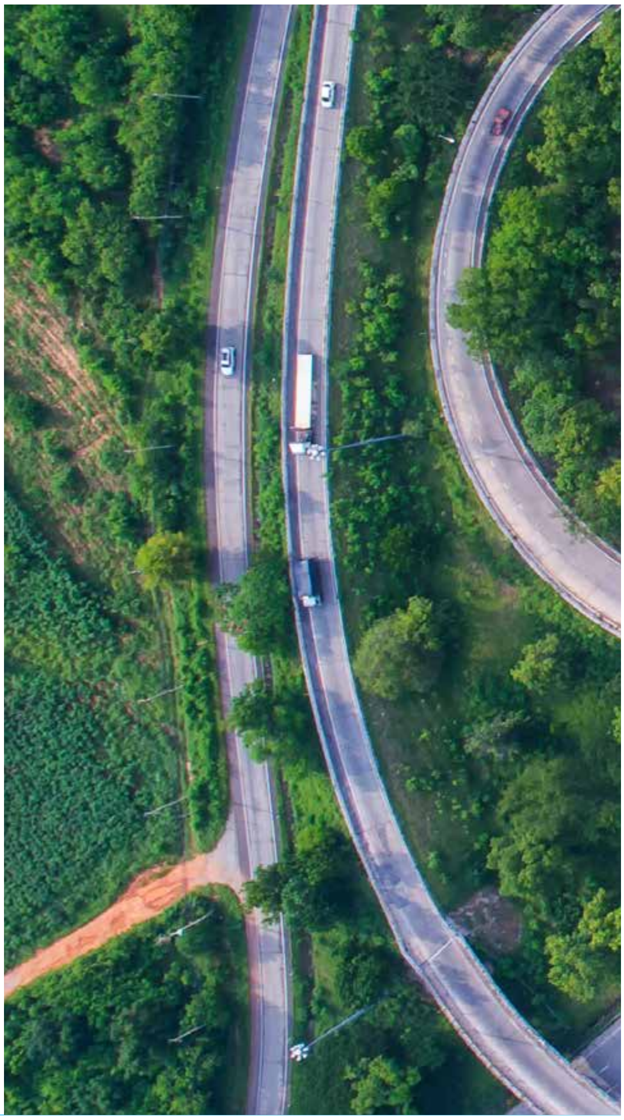
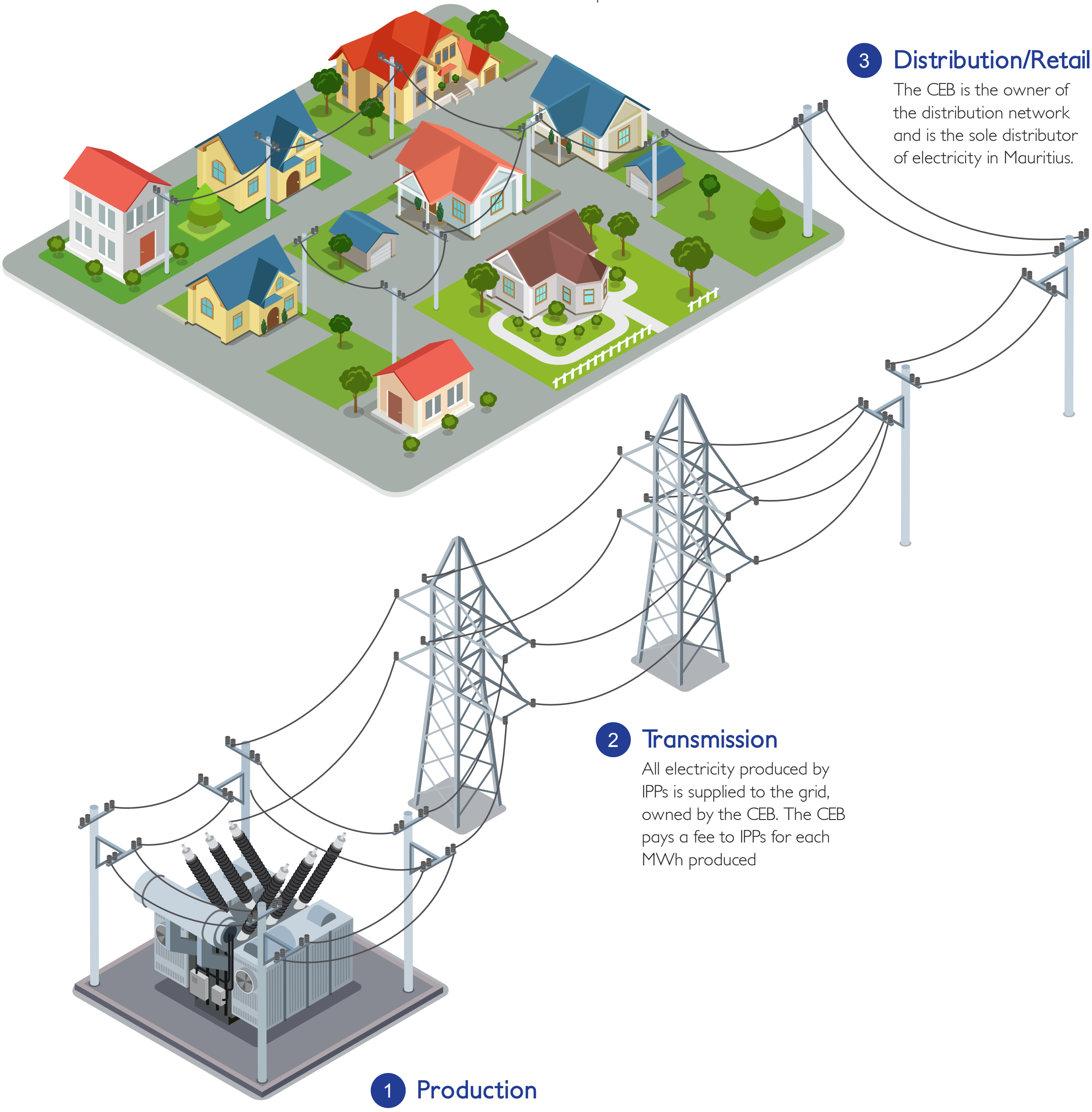


Diagram: The IPP Framework



4 End User

The CEB charges end users namely, households and businesses for electricity consumption

3 Distribution/Retail

The CEB is the owner of the distribution network and is the sole distributor of electricity in Mauritius.

2 Transmission

All electricity produced by IPPs is supplied to the grid, owned by the CEB. The CEB pays a fee to IPPs for each MWh produced

1 Production

The **CEB** produces 40% of total electricity as at 2016.

IPPs mainly sugar estates produce 60% of total electricity as at 2016.

4.3.3 Infrastructure as an Investment Class

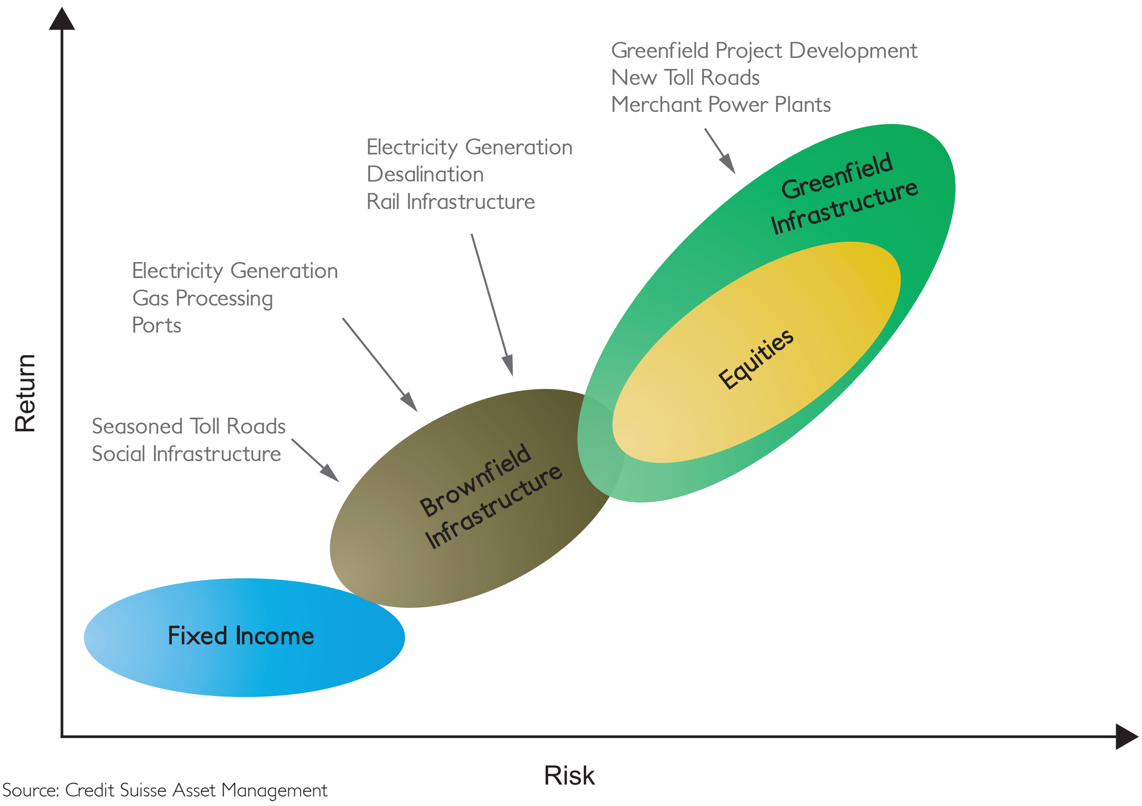
Investing in African infrastructure is a risky business. According to statistics from the World Bank (PPI World Bank, 2018), from 1990 to 2017, PPI (Private Participation in Public Infrastructure) has been a hit-or-miss. While 575 projects reached financial closure, 575 other were cancelled or are currently in distress. Given the 50% rate of failure, investors need to adapt their strategy to ensure that a particular investment will be profitable.

A variety of instruments, each combining different risk and return profiles can be used to invest in infrastructure. In developed financial markets, innovative instruments have been developed to finance infrastructure projects. For example, Yieldcos, a type of equity instrument, have been used to finance several energy projects in the US. However, in Africa (with the exception of South Africa and Nigeria), financial markets are relatively under-developed limiting the banks' ability to design complex financial structures.

Given the 'hit-or-miss' opportunities in terms of infrastructure investments and if investors are to remain traditional distant finance providers, fixed income will be more convenient for financing small-scale brownfield infrastructure projects. Development Financial Institutions (DFIs) such as the African Development Bank have been putting forward the use of infrastructure project bonds as a means of attracting private finance in African infrastructure. Project bonds differ from traditional bonds in different ways: 1) they are issued to raise capital for specific stand-alone projects; 2) they are repaid from cash generated by the project; and 3) they assume, and their performance is subject to, certain project specific risks (AfDB, 2013). Project bonds are inherently more risky than traditional bonds as the risks are concentrated on a single project as opposed to a diverse set of activities for traditional bonds. The credit risk associated with project bonds can be enhanced by guarantees from the government. Risks of default are therefore lower, leading to a yield quite close to that of the issuing country's sovereign bond.

For large-scale infrastructure projects, there is a need to tap into large pools of private savings such as pension funds or private equity funds. With narrow financial markets and the perceived riskiness of infrastructure projects, the African landscape calls for investments in unlisted infrastructure. In fact, infrastructure, especially the unlisted type, can be considered as a separate asset class with different types of projects offering different risk and return profiles.

Figure 4-J: Infrastructure as an Asset Class



Source: Credit Suisse Asset Management

Direct investments in unlisted infrastructure tend to be less accessible than listed infrastructure as the former usually requires higher capital outlays. This is why large infrastructure projects in Africa would be more suitable to large-scale institutional investors such as pension funds. Indeed, pension funds are large pools of capital that are capable of investing in large infrastructure projects without taking the risk of a too high concentration in one particular asset class. Additionally, since infrastructure investments require a long term view and pension funds invest with the objective of providing consistent returns over the long run, infrastructure investments provide somewhat a maturity match. An ideal privately financed infrastructure investment should function like a perpetuity contract, offering constant cash flow over an infinite period. It is projected that pension fund investments in African infrastructure will reach USD 1.1 trillion by 2020 (AfDB, 2018).

However, a hands-off finance provider approach will not suffice to generate a satisfactory return on investment. Proper due diligence, a long-term view of projects, an entrepreneurial outlook and finding strong support from the authorities are all essential ingredients to successful investment in African infrastructure projects.

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