MONETARY POLICY CONSULTATIVE COMMITTEE (MPCC)

ECONOMIC REVIEW AND INFLATION REPORT

JANUARY 2020

ECONOMIC POLICY, RESEARCH AND STATISTICS DEPARTMENT

CENTRAL BANK OF ESWATINI

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Major Highlights

Real GDP	*Provisional annual estimates for economic activity show that GDP grew by 2.4 per cent in 2018, up from a revised estimate of 2.0 per cent in 2017.*
Quarterly GDP	*Quarterly (Q-o-Q seasonally adjusted) GDP figures show that economic activity declined by 0.4 per cent(y-o-y) in the third quarter of 2019, down from a revised 4.5 per cent increase in the previous quarter.*
Inflation	*Headline inflation rate rose slightly to 1.8 per cent in November 2019 from 1.6 per cent recorded in October 2019.*
Inflation Forecasts	*The country's overall inflation forecast for 2020 has been revised downwards to 3.46 per cent, down from the previous forecast of 4.58 per cent.*
Foreign reserves	*Gross official reserves declined by 14.2 per cent in December 2019, from 3.2 per cent decline in the previous month, and could cover an estimated 2.6 months of imports of goods and services.*
Exchange rate	*Since the previous MPCC, the Lilangeni strengthened against the US dollar and the Euro while remaining weak against the Pound Sterling. The US dollar averaged E14.42 in December 2019 from E14.91 in October 2019.*
Credit Extension	*Credit to the private sector fell slightly from 1.8 per cent contraction in October 2019, to a 1.9 per cent contraction in November 2019. On a year-on-year basis, private sector credit contracted by 1.9 per cent.*
Public Debt	*The country's stock of debt increased from E18.3 billion recorded in October 2019 to E 19.9 billion in December 2019, reflecting an 8.7 per cent increase in debt.*
Balance of Payments	*Eswatini recorded a trade surplus of E623.4 million in December 2019, from the E255.3 million observed in November 2019.*

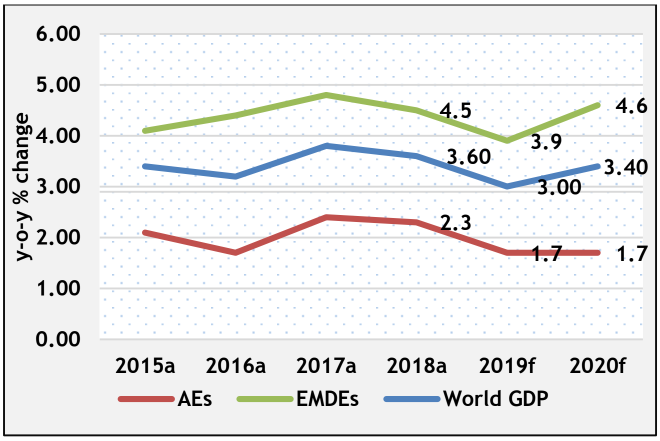
PART A: ECONOMIC REVIEW

1.0 GLOBAL ECONOMIC CONDITIONS

1.1 Global GDP Growth

According to the latest IMF World Economic Outlook (WEO) released on 16 October 2019, the global economy is in a synchronized slowdown with growth being downgraded to 3 per cent in 2019. This represents a 0.3 percentage point downgrade from the April 2019 WEO, with global growth at its lowest level since 2008-2009 (being the global financial crisis period - GFC).

Figure 1: GDP Growth: World Output (revised) - 2015 - 2020



Source:https://www.imf.org/en/Publications/WEO/Issues/2019/10/01/world-economic-outlook-october-2019

Global growth in 2020 is projected to improve modestly to 3.4 per cent, a downward revision of 0.2 per cent from the April WEO projections. However, unlike the synchronized slowdown, the 2020 recovery is not broad based and is precarious. Growth for advanced economies is projected to slow to 1.7 per cent in 2019 and 2020, while emerging market and developing economies (EMDEs) are projected to experience a growth pick up from 3.9 per cent in 2019 to 4.6 per cent in 2020. Majorly influencing the continued downturn in global growth is a deterioration in global manufacturing activity, which has weakened to levels substantially not seen since the GFC (IMF WEO, 16 October 2019).

1.2 Global Inflation and Commodities Overview

According to the IMF World Economic Outlook published in October 2019, Consistent with the softening of energy prices and the moderation in growth, consumer price inflation is expected to average 1.5 per cent this year in advanced economies, down from 2.0 per cent in 2018. With the US economy operating above potential, core consumer price inflation is projected at about 2.6 per cent in 2020–21, above its medium-term value of 2.2 per cent (the level consistent with the medium-term target of 2.0 per cent for personal consumption expenditure inflation).

According to the OPEC Monthly Oil Market Report published in December 2019, the monthly oil price rebounded in November by 5.1% m-o-m, its largest percentage gain since April 2019, to settle at $62.94 a barrel. The rise reflects increases in the physical crude benchmarks and firm crude differentials, which were supported by robust seasonal crude demand, particularly from Asia, and higher refinery runs during November in almost all regions to meet winter oil products demand.

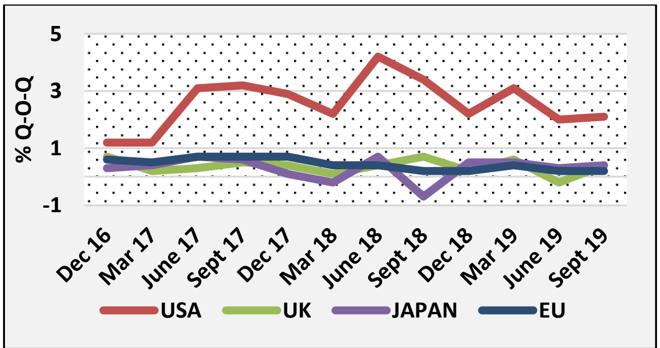
Meanwhile, according to Bloomberg, Brent crude hit $70 a barrel on Monday, 6 January 2020 the highest level since attacks on Saudi oil installations in September that crimped global supply by about 5 per cent. Unlike three months ago, the hostilities between the U.S. and Iran are yet to yield any actual impact on supply, and buyers in Asia are keeping a watching brief.

1.3 Advanced Economies GDP Growth

According to the US Bureau of Economic Analysis, the US economy grew by an annualized 2.1 per cent in the third quarter of 2019, unchanged from the second estimate and following a 2 per cent expansion in the previous three-month period. The increase in real GDP in the third quarter reflected positive contributions from Personal Consumption Expenditure, federal government spending, residential investment, exports, and state and local government spending that were partly offset by negative contributions from non-residential fixed investment and private inventory investment (US Bureau of Economic Analysis, 8 January 2020).

According to latest data from Eurostat, the Eurozone quarterly economic growth was confirmed at 0.2 per cent in the third quarter of 2019, the same as in the previous three-month period, the final estimate showed. Household consumption, government spending and fixed investment supported the expansion, while net trade and inventory changes contributed negatively to GDP (Eurostat, 5 December 2019).

Figure 2: Advanced Economies GDP Growth Trends



Source:https://www.imf.org/en/Publications/WEO/Issues/2019/10/01/world-economic-outlook-october-2019

According to the UK Office for National Statistics, UK's gross domestic product grew by 0.4 per cent in the third quarter of 2019 (revised higher from the earlier preliminary estimate of 0.3 per cent), recovering from a 0.2 per cent contraction in the previous three-month period and matching market expectations of a 0.4 per cent expansion, a revised estimate showed. Net trade made a larger positive contribution than previously estimated. (UK Office for National Statistics, 18 December 2019).

According to latest data published by the Japanese Cabinet Office, Japan's quarterly GDP growth was revised higher to 0.4 per cent in the third quarter of 2019 from a preliminary estimate of 0.1 per cent and above market expectations of 0.2 per cent. (Japan Cabinet Office, 9 December 2019).

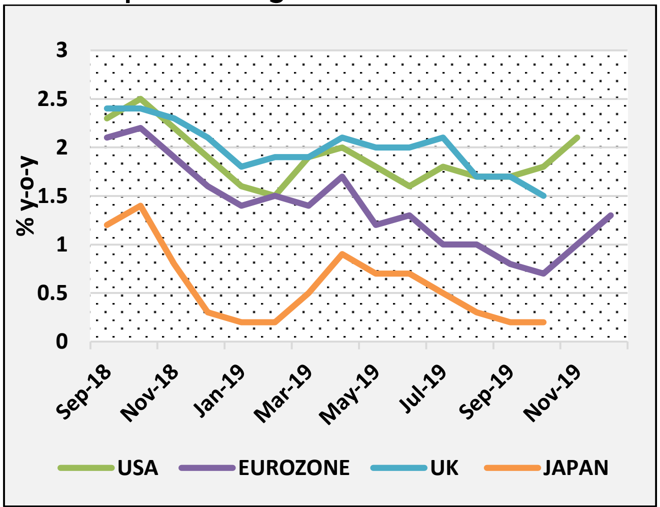
1.4 Advanced Economies CPI

According to the US Bureau of Labour Statistics, US annual inflation rate went up to 2.1 per cent in November 2019 from 1.8 per cent in October, beating market expectations of 2 per cent. It was the highest rate since November 2018, as food inflation was little-changed while energy prices dropped at a much slower pace. The core inflation rate, which excludes volatile items such as food and energy, was unchanged at 2.3 per cent, in line with market expectations. On a monthly basis, consumer prices increased by 0.3 per cent in November, after a 0.4 per cent gain in October. (US Bureau of Labour Statistics, 11 December 2019).

According to the latest Eurostat report, the annual inflation rate in the Eurozone accelerated to 1.3 per cent year-on-year in December 2019 from 1.0 per cent in the previous month and in line with market consensus, a preliminary estimate showed. That is the highest rate since June, mainly boosted by a rebound in energy prices and a faster increase in unprocessed food cost. (Eurostat, 07 January 2020).

According to the UK Office for National Statistics, the annual inflation rate in the UK held steady at 1.5 per cent year-on-year in November 2019, the same as in October 2019, the lowest level since November 2016, but slightly above market expectations of 1.4 percent.

Figure 3: Advanced Economies Consumer prices - annual price change



Source: www.bls.gov, ec.europa.eu/eurostat, www.stat.go.jp www.ons.gov.uk.

The latest result was mainly due to a slowdown in housing & utilities prices as a regulator's tariff cap pushed down electricity and gas cost (UK Office for National Statistics, 13 November 2019).

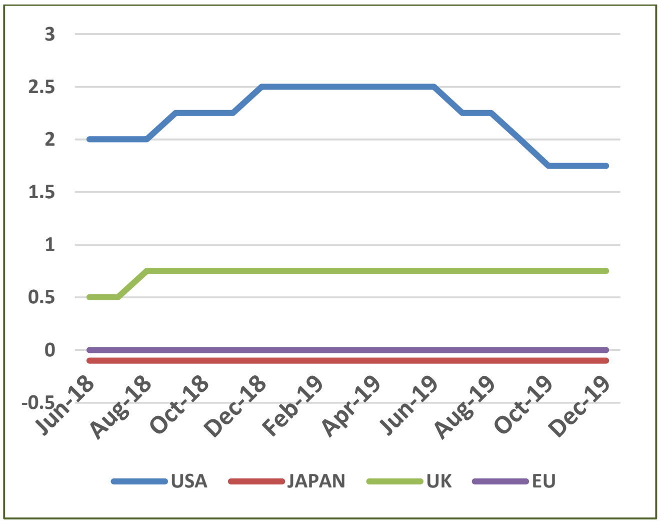
According to Japan's Statistics Office, consumer price inflation in Japan rose to 0.5 per cent year-on-year in November 2019 from 0.2 per cent in the previous month and above market consensus of 0.2 per cent. This was the highest rate in four months, as food and housing prices increased faster while transport deflation eased. On a monthly basis, consumer prices rose by 0.2 per cent (Statistics Japan, 20 December 2019).

1.5 Monetary Policy in Advanced Economies

The US Federal Reserve left the target range for its federal funds rate unchanged at 1.5-1.75 per cent on 11th December 2019, following a 25 basis points cut in the October 2019 meeting. The decision came in line with market expectations. Policymakers consider the current stance of monetary policy appropriate to support sustained growth, strong labour market conditions, and inflation near the 2 per cent target (US Federal Reserve, 11 December 2019).

Furthermore, Federal Reserve officials agreed that the current interest rate stance is likely to remain unchanged for a period of time, despite raising concerns that low interest rates could exacerbate imbalances in the financial sector, as reflected in minutes of the December policy meeting. US Federal Reserve, 03 January 2020).

Figure 4: Interest Rates in Advanced Economies



Source:www.federalreserve.gov,ecb.europa.eu/home, bankofengland.co.uk, boj.or.jp

The ECB left its key interest rates and stimulus package unchanged during Christine Lagarde's first policy meeting in charge on the 12 December 2019, with the main refinancing rate remaining at 0 per cent and the deposit rate at -0.5 per cent. Policymakers said they expect interest rates to remain at their present or lower levels until the inflation outlook converges to their aim. The bank also cut its growth forecast for 2020, due to weak trade growth, while inflation is seen below the 2 per cent target through at least 2022.

According to the minutes of the Bank of England's Monetary Policy Committee (BOE MPC), voted by a majority of 7-2 to hold Bank Rate at 0.75 percent during its December 2019 policy meeting, as policymakers took a wait-and-see approach following Prime Minister Boris Johnson's election victory and its possible implications on Brexit. Policymakers further noted that monetary policy could respond in either direction to changes in the economic outlook in order to ensure a sustainable return of inflation to the 2 per cent target (Bank of England, 19 December 2019).

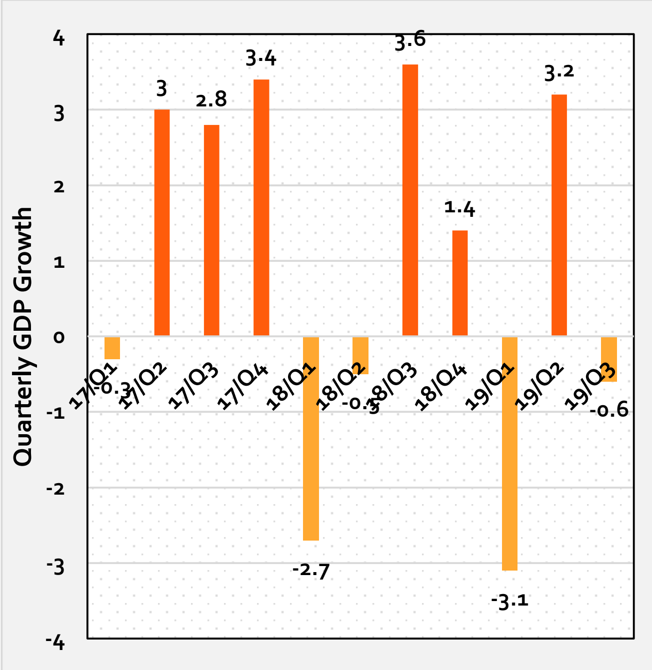
The Bank of Japan left its key short-term interest rate unchanged at -0.1 per cent during its December 2019 meeting, and kept the target for the 10-year Japanese government bond yield at around 0 per cent. Policymakers also maintained its upbeat assessment of the economy, despite a consumption tax hike in October 2019, while offered weaker views on exports, production and business sentiment mainly due to the impact of natural disasters and sluggish demand from overseas economies (Bank of Japan, 20 December 2019).

2.0 ECONOMIC DEVELOPMENTS IN SOUTH AFRICA

2.1 GDP Growth

According to Statistics South Africa, the South African economy contracted by an annualized 0.6 per cent quarter-on-quarter in the three months to September 2019, following an upwardly revised 3.2 per cent growth in the previous period and much worse than market expectations of a 0.1 per cent expansion.

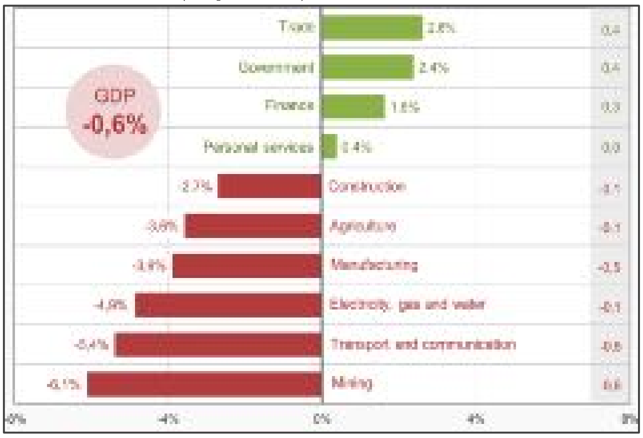
Figure 5: South Africa GDP Growth: January 2017 - September 2019



Source: www.statssa.gov.za

Mining, manufacturing and transport, storage and communication industries contributed the most to the GDP contraction. Year-on-year, the economy expanded by a meagre 0.1 per cent, below 0.9 percent in Q2-2019 and forecasts of 0.4 per cent. Year-to-date, the GDP advanced 0.3 per cent but the South African Treasury expects it to grow by 0.5 per cent in 2019 (Statistics South, 3 December 2019).

Figure 6: Contributing Sectors to Q2-2019 SA GDP Growth (% points)



Source: [*www.statssa.gov.za*](http://www.statssa.gov.za)

Notably, the mining sector shrank by 6.1 per cent, following a 17.4 per cent jump in Q2-2019, mainly due to lower output for platinum group metals (PGMs), coal and iron ore. Manufacturing slumped by 3.9 per cent (+2.1 per cent in Q2-2019), mainly due to a drop in production of basic iron and steel, non-ferrous metal products, metal products and machinery. The transport, storage and communication industry also found itself on the back foot, falling by 5.4 per cent. This is the biggest quarter-on-quarter fall for the industry since 1993. A slowdown in activity related to freight and passenger transport dampened growth in the third quarter.

Agriculture saw its third consecutive quarter of contraction. Lower production was recorded for field crops such as maize, wheat, sunflower seeds, and tobacco and soya beans. The construction industry failed to pull itself out of recession, registering its 5th consecutive quarter of negative growth. Decreases were reported for activities related to residential and non-residential buildings, as well as construction works (Statistics South, 3 December 2019).

2.2 Consumer Prices

The annual inflation rate in South Africa fell to 3.6 per cent in November 2019 from 3.7 per cent in the previous month, matching market expectations. It was the lowest inflation rate since December 2010, mainly due to a slowdown in cost of food & non-alcoholic beverages and a fall in transport prices.

Annual core inflation rate, which excludes cost of food, non-alcoholic beverages, fuel and energy, was at 3.9 per cent in November, slowing from a 4 per cent gain in the prior month, in line with forecasts and reaching its lowest since December 2011.

On a monthly basis, consumer prices rose by 0.1 per cent, after being unchanged in October 2019. Prices for food & non-alcoholic beverages rebounded (0.3 per cent compared to -0.1 per cent) while transport prices were flat, following a 0.3 per cent increase in the previous month (Statistics South Africa, 11 December 2019).

According to Statistics South Africa, the unemployment rate in South Africa increased to 29.1 per cent in the Q3-2019 following a 29 per cent increase in the second quarter of 2019, it is the highest level since comparable data began in Q1-2008, matching market expectations. The number of unemployed rose by 78 000 to 6.73 million while employment increased by 62 000 to 16.38 million (Statistics South Africa, 29 October 2019).

2.3 Monetary Policy

The South African Reserve Bank (SARB) held its benchmark repo rate unchanged at 6.50 per cent during its November meeting, as widely expected.

The decision was not unanimous. Policymakers noted that monthly inflation has been lower than the mid-point of the target range and that inflation expectations have continued to moderate gradually. Looking ahead, the SARB disclosed that projections point to one repo cut of 25 basis points in Q3-2020, but this direction is dependent on new developments and changing data and risks (SARB, 21 November 2019).

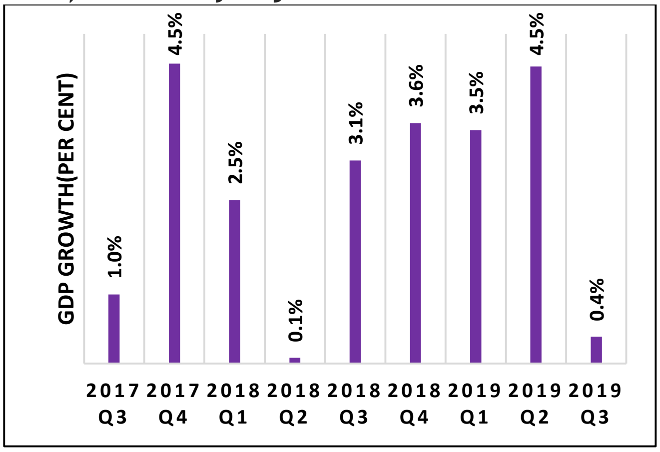
3.0 DOMESTIC ECONOMIC DEVELOPMENTS

3.1 GDP Growth

Economic activity, as measured by the Quarterly Gross Domestic Product (QGDP) declined by 0.4 per cent on a year-on-year basis (seasonally adjusted) in the third quarter of 2019, down from a revised 4.5 per cent increase in the previous quarter. On a quarter-on-quarter basis, economic activity remained on the negative trajectory, declining by 1.0 per cent (seasonally adjusted) in the third quarter of 2019, from a decline of 0.3 per cent in the second quarter of 2019. The slowdown can largely be attributed to slower economic activity in the tertiary sector.

The tertiary sector declined by 4.0 per cent year-on-year, in the third quarter of 2019 compared to a growth of 2.5 per cent in the previous quarter. Notable negative performance was observed in 'wholesale and retail', 'information and communication', 'tourism related activities' and 'professional and administrative activities'. The poor performance observed in the services subsectors reflect weak demand in light of depressed real disposable incomes as well as general poor performance of the economy. Public administration remained on a negative territory for the fourth consecutive quarter in line with a hiring freeze adopted by the Government of Eswatini over the past two years in light of deepening fiscal challenges.

Figure 7: Quarterly GDP Growth Rates (Year-on-Year) Seasonally Adjusted



Source: CSO

Positive growth within the tertiary sector was mainly observed in the 'transport and storage' and 'financial services' subsectors. Transportation and storage grew by 12.8 per cent, year-on-year, in the third quarter from 11.1 per cent in the previous quarter. Financial services recorded a slower growth of 15.7 per cent, year-on-year, in the quarter under review from 31.0 per cent in the previous quarter.

The secondary sector, on the other hand, grew at a slower rate of 9.7 per cent, year-on-year, in the third quarter of 2019, from 12.9 per cent in the previous quarter. The manufacturing sector rose by 10.4 per cent in the third quarter down from 15.4 per cent in the previous quarter. The slower growth in manufacturing activity was largely due to a 12 per cent year-on-year decrease in the manufacturing of textiles and wearing apparels. Construction activity remained on a negative territory but contracted by a slower margin of 1.0

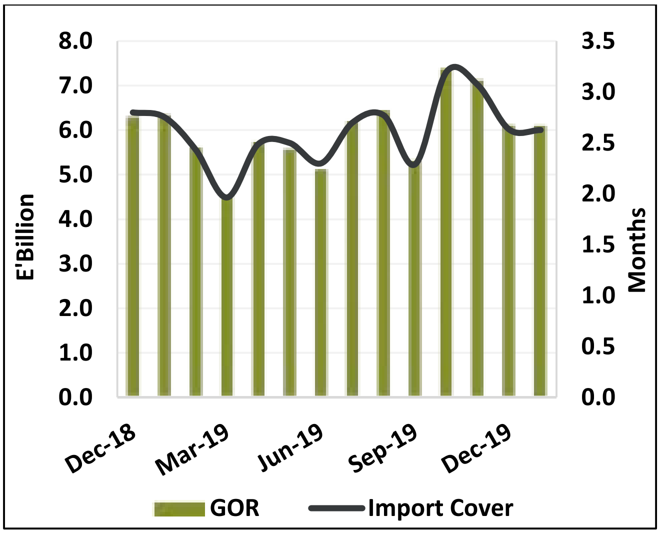
per cent in the quarter under review, an improvement from a contraction of 11.9 per cent in the previous quarter.

The primary sector remained flat recording a negative growth of 1.3 per cent, year-on-year, in the third quarter of 2019, same as it was in the previous quarter.

3.3 Monetary Sector Developments

3.3.1 Gross official Reserves

Figure 8: Gross Official Reserves & Import Cover



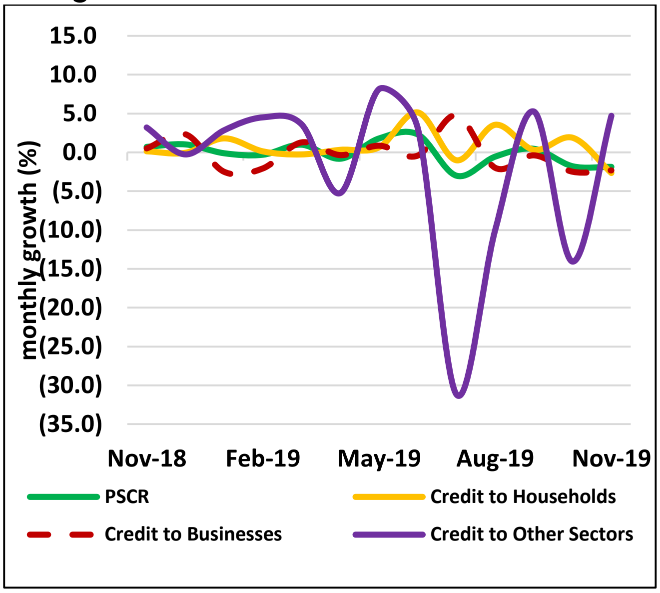
Source: Central Bank of Eswatini

Gross official reserves fell for two consecutive months, reflecting the impact of rand outflows and government fiscal situation in 2019/20. The reserves declined by 14.2 per cent to E6.1 billion at the end of December 2019, following a 3.2 per cent fall the previous month. Consequently, the import cover fell from 3.1 months in November 2019 to 2.6 months at the end of December 2019. On a year-on-year basis, gross official reserves declined by 3.1 per cent. As at 3 January 2020, gross official reserves stood at E6.1 billion, equivalent to 2.6 months of imports of goods and services.

3.3.2 Credit Extension

Credit to the private sector continued on a downward trajectory falling by 1.9 per cent to E14.4 billion at the end of November 2019, the lowest it has been in fourteen months. This development was on account of weakened demand for credit by the household and business sectors, which collectively account for more than 90 per cent of private sector credit in the economy. Year-on-year, credit to the private sector contracted by 1.9 per cent.

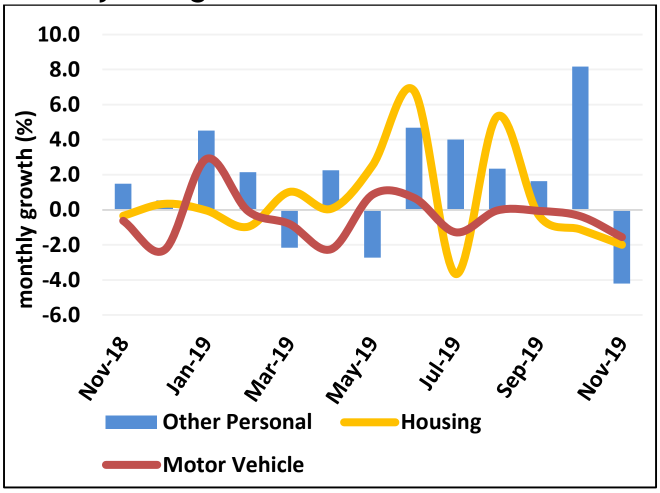
Figure 9: Private Sector Credit: Monthly Changes



Source: Central Bank of Eswatini

Credit to households & non-profit institutions serving households (NPISH) declined by 2.7 per cent to E6.7 billion over the review month. The household sector reined in credit across all product lines. Other personal (unsecured) loans declined by 4.2 per cent while housing and motor vehicle loans fell by 2.0 per cent and 1.6 per cent over the review month. However, compared to the previous year, credit to households depicted an increase of 9.9 per cent.

Figure 10: Household Credit by Product: Monthly Changes



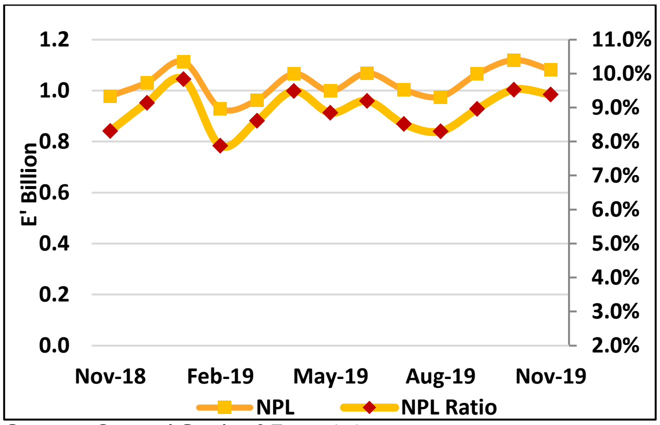
Source: Central Bank of Eswatini

Credit to the business sector fell for the fourth consecutive month, falling by 2.3 per cent to settle at E6.7 billion at the end of November 2019. The decline was driven by weak demand for credit in the distribution & tourism, construction, real estate and community, social & personal services industries. The declines were partially offset by increases in credit to manufacturing, transport & communication and agriculture & forestry while credit to mining & quarrying remained unchanged.

Credit to other sectors, on the other hand, grew by 4.7 per cent to E1.4 billion in November 2019, a turnaround from the 14.1 per cent decline observed the preceding month. The rebound was as a result of improved demand for credit by public nonfinancial corporations and local government. Credit to public nonfinancial corporations increased by 27.2 per cent while credit to local government went up by 3.0 per cent over the review period. However, credit to other financial corporations recorded a decline of 5.4 per cent.

Non-performing loans (NPLs) declined from E1.2 billion the previous month to E1.1 billion at the end of November 2019. At this level, the NPL ratio stood at 9.4 per cent, a slight improvement from the 9.5 per cent realized the previous month. However, year-on-year, NPLs grew by 17.0 per cent and the NPL ration by 0.8 percentage points.

Figure 11: Non-Performing Loans as a Per centage of Total Loans Ratio



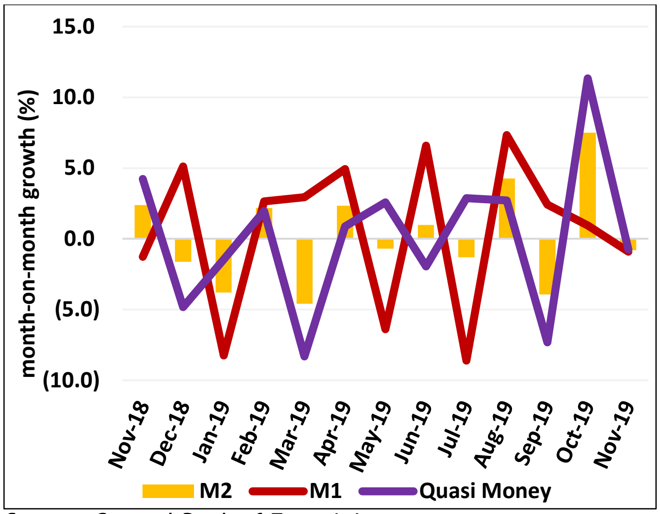
Source: Central Bank of Eswatini

3.3.3 Money Supply

Broad money supply (M2) stood at E18.3 billion at the end of November 2019, depicting a month-on-month decline of 0.8 per cent. The fall was observed in both its components; narrow money supply (M1) and quasi money supply. Compared over the year, broad money supply decreased by a marginal 0.2 per cent.

Narrow money supply (M1) amounted to E6.4 billion at the end of November 2019, 0.9 per cent lower than the previous month. The fall in M1 was on account of transferable (demand) deposits which fell by 2.0 per cent to E5.5 billion. Emalangeni in circulation, on the other hand, grew by 7.4 per cent E808.4 million as economic agents preferred holding cash over the review month.

Figure 12: Money Supply: Monthly Changes



Source: Central Bank of Eswatini

Quasi money supply declined by 0.8 per cent month-on-month to settle at E12.0 billion in November 2019. The fall was due to time deposits which fell by 1.0 per cent to E10.0 billion. Savings deposits, on the other hand, recorded an increase of 0.4 per cent to E1.9 billion at the end of November 2019.

3.4 Soundness of the Banking Sector

The banking sector remains stable, liquid and adequately capitalized. There was muted growth in banking sector aggregate assets during the year to September 2019, growing by 0.1 per cent to reach E20.3 billion. On the liability side, deposits experienced a 4.6 per cent decrease to settle at E14.9 billion while total shareholders' funds grew by 5.5 per cent from E2.9 billion in September 2018 to E3.1 billion at the end of September 2019.

3.4.1 Capital Adequacy

On aggregate, commercial banks in Eswatini were well-capitalized in terms of meeting the minimum capital requirements and capital adequacy ratios as they remained above the minimum regulatory ratios in the year to September 2019. The average industry-wide regulatory tier 1 capital adequacy ratio and total capital adequacy ratio stood at 15.1 per cent and 17.8 per cent respectively. This is lower than 15.6 per cent for tier 1 capital adequacy ratio and 18.4 per cent for total capital adequacy ratio as at September 2018. However, the leverage ratio increased marginally by 0.8 percentage points from 11.1 per cent in September 2018 to 11.8 per cent at the end of September 2019, showing the banks' loss absorption capabilities. In addition, non-performing loans (net of specific provisions) to capital improved from 26.0 per cent in September 2018 to 23.8 per cent in September 2019 showing capital at risk caused by asset quality deterioration.

3.4.2 Earnings and Profitability

Banking sector profitability improved in the year to September 2019. The average return on banks' total assets (ROA) and on total equity (ROE) increased from 2.2 per cent and 15.1 per cent respectively at the end of September 2018 to 2.7 per cent and 17.4 per cent respectively in the year to September 2019. The cost-to-income ratio also improved from 75.3 per cent in September 2018 to 72.0 per cent in September 2019. On average, banks' operating expenses accounted for 48.2 per cent of total income. Therefore, banking sector earnings are considered sustainable to supplement capital. The sector's after-tax profits increased by 21.7 per cent to reach E537.5 million in September 2019 from E441.6 million in September 2018.

3.4.3 Banks' Asset Quality

Bank lending increased over the year to September 2019 despite the shrink in deposit base. Overall credit extended by banks stood at E12.3 billion in September 2019, increasing by 3.1 per cent from September 2019. Loans remain the key business of banks as shown by the loans to assets ratio of 60.7 per cent.

The asset quality, measured as a proportion of non-performing loans to total gross loans, deteriorated from 8.1 per cent in September 2018 to 9.0 per cent in September 2019, signifying increased credit risks in 2019. In the same spirit, specific provisions to total NPLs increased from 21.5 per cent in September 2018 to 33.2 per cent in September 2019 to cover expected losses.

3.4.4 Liquidity Risk

Average bank liquidity marginally increased from 33.2 per cent in September 2018 to 33.7 per cent in September 2019 against a regulatory minimum of 25.0 per cent. Government securities represented 42.8 per cent of liquid assets holding of banks. As a share of total assets, liquid assets declined from 25.6 per cent to 24.8 per cent during the period under review. The ratio of loans and advances to deposits increased to 82.6 per cent in September 2019 from 76.4 per cent in September 2018 as a result of the fall in deposit base.

3.5 Public Debt

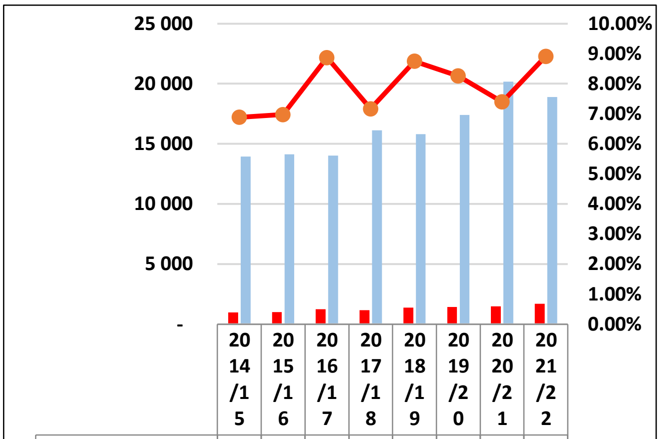
3.5.1 Total Public Debt

The country's stock of debt surged to E19.9 billion, an equivalent of 29.9 per cent of GDP at end of December 2019. This reflects an increase of 8.7 per cent from the E18.3 billion recorded in October, mainly driven by an increase in domestic debt, which is attributed to disbursement of the full CBE Advance to Government and improved uptake of T-bills and bonds during the period. The Suppliers Bond was reopened and it performed very well with an allotment rate of 150 per cent. Quarter on quarter, external debt increased from E7.0 billion to E7.8 billion due to disbursements for project funding, as well as depreciation of the local currency.

3.5.2 Debt Sustainability Review

The country's debt ratios have remained significantly low compared to the Government debt sustainability measure of 35 per cent of GDP. Debt to GDP currently is estimated at 30 per cent, below the 35 per cent threshold. The recent surge in total public debt has been from the domestic side as Government increased its operations in the domestic capital markets. In the advent of the cash flow challenges beginning 2015/16 financial year, Government increased the issuance securities in order to finance her operations.

Figure 13: Debt Service to Revenue



	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Debt service	961	986	1 2	1 1	1 3	1 4	1 4	1 6
Revenue	13	14	14	16	15	17	20	18
% Revenue	6.89	6.98	8.87	7.17	8.75	8.26	7.39	8.91

Source: Central bank of Eswatini

Debt service to revenue, a key indicator for liquidity constraints, is also very low compared to the Bretton Woods Institutions sustainability level of 40 per cent of domestic revenue. For the 2019/20 financial year, debt service to revenue is forecasted to reach 9 per cent, way below the 40 per cent level. Over the years, from 2014/15 financial year, debt service to revenue as averaged about 8 per cent.

Although the country's debt ratios are markedly low, caution must be exercised in acquiring new debt. Off budget, borrowing is especially discouraged because this will shoot debt levels above the 35 per cent of GDP threshold. This will also exert pressure on the volatile revenue flows, which could otherwise be efficiently utilised for budgeted developmental projects.

The country's public debt is more vulnerable to macro-fiscal shocks, notably; growth, primary balance, and real interest rate shocks. Precisely, the Debt Sustainability Analysis (DSA) conducted by Government in August 2019, suggest that the risk from fiscal shocks in the absence of concrete fiscal restraint would take the public debt to GDP ratio beyond the 60 per cent of GDP regional indicative threshold of SADC by 2024. A prudent and credible medium-term fiscal stance is therefore, essential to ensure that downside risks to the debt outlook are contained. This can be achieved by constantly monitoring and controlling the major drivers of public debt accumulation, especially off-budget expenditures.

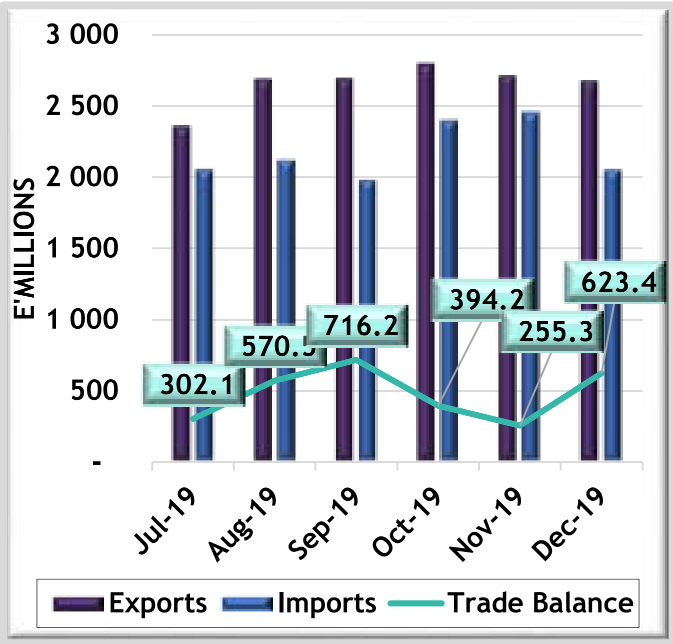
3.6 The External Sector

3.6.1 Trade Developments

In the month of December 2019, Eswatini recorded a trade surplus amounting to E623.4 million, which marked a 144.1 per cent increase from the E255.3 million trade surplus recorded in the previous month.

Month-on-month export earnings depicted a marginal decline of 1.4 per cent from E2.719 billion to E2.682 billion. On a year-on-year basis, monthly export earnings increased significantly by 12.6 per cent. Year-on-year annual export earnings increased significantly by 16.6 per cent, from E24.650 billion generated in 2018 to E28.751 billion generated in 2019.

Figure 14: Merchandise Trade; July 2019 - December 2019



Source: Eswatini Revenue Authority

In the period under review, the import bill underwent a month-on-month dip of 16.5 per cent from E2.464 billion to E2.058 billion. On a year-on-year basis, the import bill increased by 3.6 per cent from E1.986 billion recorded in December 2018 to E2.058 billion recorded in December

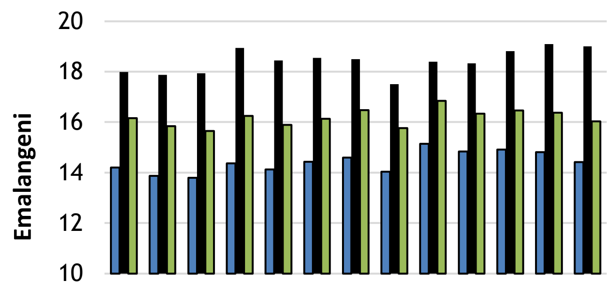
2019. The annual import bill for the year 2019 amounted to E25.152 billion, which represents a marginal year-on-year increase of 1.0 per cent from the E24.901 billion recorded in the previous year. The preliminary annual figures indicate that the country posted a trade surplus amounting to E3.598 billion in 2019, a complete shift from the trade gap of E250.6 million that was recorded in 2018.

An analysis of export earnings for the month under review indicates that month-on-month Sugar and sugar confectionery products exported declined by 50.4 per cent from E804.0 million to E398.5 million. Miscellaneous edible products exported increased significantly by 58.7 per cent, from E1.135 billion to E1.801 billion in December 2019, while wood and wood articles declined significantly by 33.2 per cent from E140.7 million to E94.0 million in December 2019. Textile and textile apparel products exported declined significantly by 46.6 per cent in December 2019 relative to the previous month, from E362.8 million to E193.8 million.

3.6.2 Exchange Rates Developments

Since the MPCC meeting in November 2019, the Lilangeni as influenced by regional and international factors, strengthened against the US dollar and the Euro while remaining weaker against the Pound Sterling. Against the US Dollar, the domestic unit strengthened by 3.3 per cent to average E14.42 in December 2019 from E14.91 in October 2019. The Rand, hence the Lilangeni benefitted more from positive global sentiments largely driven by the easing of US-China trade tensions. Bouts of weakening in the local unit driven more by domestic factors such as weak economic data release in South Africa, Fitch's decision to leave South Africa's credit rating at junk status and mounting nationwide electricity blackouts by Eskom were evident but not strong enough to offset the appreciation recorded in the period under review. The local unit ended the month of December 2019 trading at E14.02 to the US Dollar, E18.52 to the Pound Sterling and E15.75 to the Euro.

Figure 15: Lilangeni Exchange Rates against Selected Major Currencies



	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19
USD	14.	13.	13.	14.	14.	14.	14.	14	15.	15	15	15	14
GBP	17.	17.	17.	18.	18	18.	18.	18	18.	18	19	19	19.
Euro	16.	15.	15.	16.	15.	16.	16.	16	16.	16	16	16	16

Source: Central Bank of Eswatini

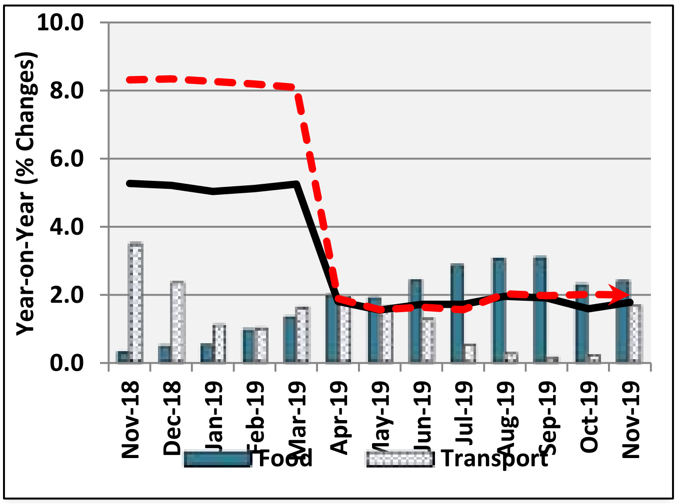
While the US and China trade truce seems likely, it is only a temporary solution with much uncertainty to the stability of emerging market currencies, including the Rand. The Rand/Lilangeni is set to remain volatile as South Africa pursues restorative policies to remedy the vicious cycle of low growth, high unemployment and poor performance of state owned enterprise which puts pressure on government expenditure. In the UK, the prospect of a no-deal Brexit occurrence spearheaded by the new government, pose major risks to the Rand/Lilangeni outlook.

PART B: INFLATION DEVELOPMENTS

4.1 Headline Inflation

The country's headline consumer price inflation rose slightly to 1.8 per cent in November 2019 from 1.6 per cent in the previous month. The moderate upswing in consumer prices was largely due to an increase in domestic fuel prices. A fuel levy of 80 cents/ litre was introduced in November 2019 resulting in a 1.7 per cent year-on-year increase in transport inflation in the month under review compared to 0.2 per cent in the previous month. In addition, food inflation rose slightly to 2.4 per cent in November 2019 from 2.3 per cent in the previous month mainly driven by moderate increases in price of cereal products and 'oils and fats'.

Figure 16: Consumer Inflation November 2018 to November 2019



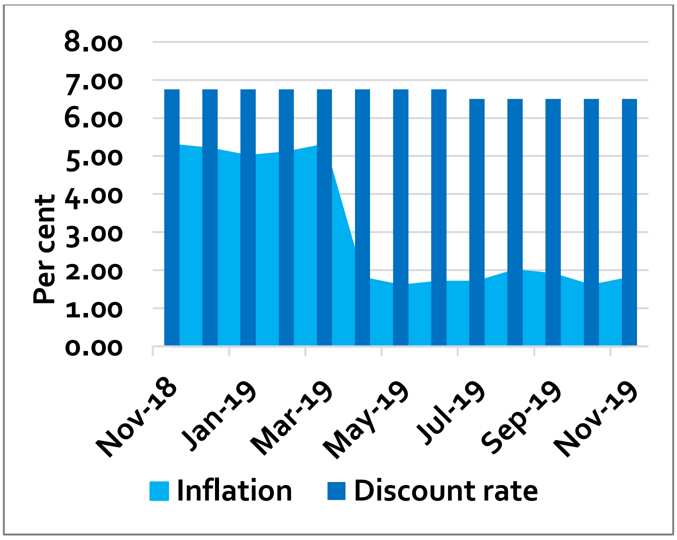
Source: Central Statistical Office

On month-on-month rates, consumer inflation rose by 0.3 per cent in November 2019 compared to a decline 0f 0.1 in October 2019. Month-on-month increases were mainly observed in the price indices for 'transport', 'food and non-alcoholic beverages' and 'alcoholic beverages and tobacco'.

Core inflation, which is CPI excluding volatile items such as food, fuel and energy, slightly rose to 2.1 per cent in November 2019 from 2.0 per cent in October 2019. On month-on-month rates, core inflation increased to 0.2 per cent in November 2019.

4.2 Inflation and Interest Rate Trends in Eswatini

Figure 17: Inflation and Discount Rates



Source: Central Statistics Office and Central Bank of Eswatini

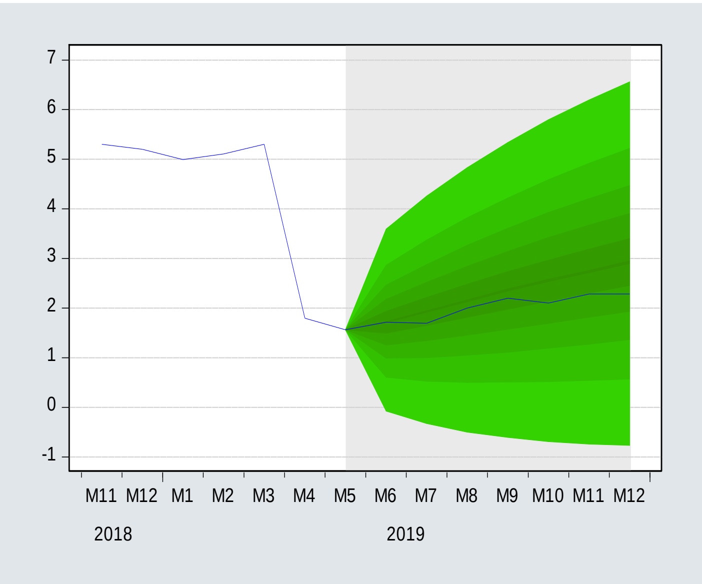
The Bank adopted an easing monetary policy stance in 2019 cutting the discount rate once by 25 basis points in July 2019 from 6.75 per cent to 6.5 per cent. In November 2019 the Bank kept the discount rate at 6.5 per cent, maintaining 0 per cent differential between Eswatini and South Africa. The SARB also maintained the repo rate at 6.5 per cent in November.

4.3 Inflation Outlook

Since April 2019, the country's overall inflation improved significantly falling below 2 per cent for the most part of the remainder of the year 2019, largely due to a freeze on utility tariffs of electricity and water. As a result, the annual forecast for 2019 is placed at 2.61 per cent with the fourth quarter of 2019 revised down to 1.72 per cent (from 1.99 per cent). With the ongoing negotiations by the power utility company to increase the tariffs, inflation is expected to pick up in the short-to-medium term. The proposed hike in public transport fares due to be implemented in January 2020 is also expected to add more inflationary pressure to the year's trajectory over and above the already implemented fuel levy of 85 cents per litre and the increase in the price of bread prices.

However, the Bank remains cautious of the magnitude of the pressure towards the inflation trajectory particularly concerning the proposed increment in electricity tariff which has been revised down from 15 per cent to 6 per cent and transport fares. Hence, the country's overall inflation forecast for 2020 has been revised downwards to 3.46 per cent, down from the previous (November 2019) forecast of 4.58 per cent. The forecast for the first quarter of 2020 has been revised down to 2.28 per cent (from 3.36 per cent) before increasing to 3.57 per cent in the second quarter.

Figure 18: Inflation Fan Chart; May 2019 to December 2019



Source: CBE Inflation Forecasting Model

Medium term forecasts show that inflation will average 4.12 per cent in 2021 (lower than the 5.18 per cent forecasted previously) and slow to 3.89 per cent in 2022. The near and medium term trajectory remain subject a change in the increases in administered prices. Furthermore, increases in the Brent oil prices and a weakening in the Rand against major currencies (driven by weak fundamentals in South Africa), pose as upside risk to the outlook.

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