



# **National Bank of Rwanda** **Banki Nkuru y'u Rwanda**

## **QUARTERLY INFLATION REPORT**

**Second Quarter, 2018**



**Second Quarter 2018**

## EXECUTIVE SUMMARY

The world economic performance remained strong in 2018Q2 and this good performance is expected to continue in 2018Q3. The world economy is projected to grow by 3.9 percent in both 2018 and 2019 against 3.7 percent recorded in 2017. Key factors that will contribute to growth include favorable global financial conditions, the improvement in global trade and international commodity prices. Business conditions indicate a strong economic outlook. However, the potential re-emergence of global trade barriers, rising volatility in asset markets and continued US interest rates normalization are likely to impact the near-term growth prospects.

In emerging and developing economies, the growth will remain close to 2017 levels. China's GDP growth is projected to decelerate to 6.6% in 2018 and furthermore to 6.3% in 2019 from 6.9% recorded in 2017. Growth is projected at 4.9% in emerging and developing economies and to 3.4% in Sub-Saharan Africa, from 4.7% and 2.8% respectively in 2017. In EAC economies, growth is expected to remain strong in 2018 and in 2019.

Globally, global demand is likely to continue supporting the Rwandan economic prospects. Foreign demand for local export products is anticipated to remain strong, which will continue supporting Rwandan export earnings. However, due to excess supply of coffee and tea, prices are likely to decline.

The Rwandan economy recorded good performance in the first half of 2018, growing by 10.6 percent in 2018Q1 and 6.7 percent in 2018Q2. The growth was mainly supported by favorable weather conditions, recovery in construction sector, improvement in transport services and increase of fixed investment as well as private consumption. This good economic performance is expected to continue in the second half of 2018 because of agricultural season B good performance, on-going construction projects and improving international commodity prices. However, aggregate demand will remain non-inflationary.

Despite the growth in formal imports value by 1.4 percent, Rwanda's trade deficit improved by 7.6 percent in 2018Q2, to a deficit of USD 309.0 million from a deficit of USD 334.6 million in 2017Q2. The improvement followed an increase in formal exports value by 15.8 percent. Formal exports covered 44.1 percent of formal imports in 2018Q2 from 38.6 percent in 2017Q2.

In 2018Q2, the foreign exchange pressure on Franc Rwandais (FRW) remained modest, due to the continued improvements in external sector. Relative to December 2017, the FRW depreciated by 1.7 percent against the USD at end June 2018. It depreciated by 0.9 percent and 0.8 percent in 2018Q2 and 2018Q1 respectively.

In 2018Q2, the NBR maintained an accommodative monetary policy stance aimed at continuing supporting the financing of the economy by the banking sector, since both inflationary and exchange rate pressures remained subdued. The NBR kept its policy rate at 5.5 percent in June 2018. Outstanding credit to the private sector increased by 7.3 percent in 2018Q2 compared to 8.0 percent in 2017Q2. The broad money increased by 9.6 percent in 2018Q2 compared to 12.7 percent in the same period of 2017.

Despite rising from 0.9 percent in 2018Q1 to 2.5 percent in 2018Q2, headline inflation broadly remains low and stable compared with the medium target of 5 percent. The developments in headline inflation were mainly reflected in food and energy prices as well as in transport costs. Core inflation remained benign, slightly increasing from 1.7 percent to 1.8 percent during the same period and this was consistent with the prevailing level of aggregate demand and subdued exchange rate pressures.

Looking ahead, agricultural production in season B and C 2018 pushed down vegetables prices and this is expected to continue towards the end of September 2018. Oil prices are likely to continue rising, putting pressures on local pump prices and leading to an increase in the import bill. The latter is likely to be partially offset by the anticipated increase in export earnings. In view of these risks, headline inflation is projected to lie between 1.5% and 2.5% for 2018Q3.

**LIST OF ACRONYMS AND ABBREVIATIONS**

NBR	: National Bank of Rwanda
CIEA	: Composite Index of Economic Activities
CPS	: Credit to the Private Sector
GDP	: Gross Domestic Product
EAC	: East African Community
ECB	: European Central Bank
IMF	: International Monetary Fund
KCC	: Kigali Convention Center
M3	: Broad money
NCG	: Net Credit to Government
NDA	: Net Domestic Assets
NFA	: Net Foreign Assets
NISR	: National Institute of Statistics of Rwanda
OPEC	: Organization of the Petroleum Exporting Countries
UK	: United Kingdom
US	: United States
USD	: United States Dollars
WEO	: World Economic Outlook
WTI	: Western Texas Intermediate

## TABLE OF CONTENTS

<b>EXECUTIVE SUMMARY .....</b>	<b>I</b>
<b>TABLE OF CONTENTS .....</b>	<b>IV</b>
<b>LIST OF TABLES .....</b>	<b>VI</b>
<b>LIST OF FIGURES.....</b>	<b>VII</b>
<b>I. GLOBAL ECONOMIC AND FINANCIAL DEVELOPMENTS .....</b>	<b>1</b>
1.1 ECONOMIC DEVELOPMENTS .....	1
1.1.1 DEVELOPMENTS IN UNITED STATES .....	1
1.1.2 DEVELOPMENTS IN EUROZONE.....	1
1.1.3 DEVELOPMENTS IN CHINA.....	2
1.1.4 DEVELOPMENTS IN SUB-SAHARAN AFRICA AND EAC.....	2
1.2 RECENT DEVELOPMENTS IN COMMODITY PRICES .....	3
1.3 FINANCIAL MARKETS AND FOREIGN EXCHANGE MARKET .....	5
1.4 OUTLOOK FOR THE GLOBAL ECONOMY .....	6
<b>II. DOMESTIC ECONOMY AND FINANCIAL DEVELOPMENTS .....</b>	<b>7</b>
2.1 DOMESTIC DEMAND AND OUTPUT .....	7
2.1.1 DOMESTIC DEMAND .....	7
2.1.2 ECONOMIC PERFORMANCE BY SECTOR .....	8
2.1.3 THE OUTPUT GAP .....	9
2.1.4 OUTLOOK OF THE DOMESTIC DEMAND AND OUTPUT.....	10
2.2 EXTERNAL SECTOR DEVELOPMENTS.....	10
2.2.1 FORMAL TRADE BALANCE .....	10
2.2.1.1 FORMAL EXPORTS OF GOODS .....	11
2.2.1.2 FORMAL IMPORTS OF GOODS.....	13
2.2.2 FORMAL TRADE WITH EAC COUNTRIES .....	15
2.2.3 INFORMAL CROSS-BORDER TRADE.....	16
2.2.4 THE EXCHANGE RATE: BILATERAL AND EFFECTIVE .....	17
2.3 MONETARY DEVELOPMENTS .....	18
2.3.1 MONETARY POLICY STANCE .....	18
2.3.2 MONEY SUPPLY AND DEMAND.....	19
2.3.2.1 MONEY SUPPLY .....	19

2.3.2.2 MONEY DEMAND .....	21
2.3.3 BANKING SYSTEM LIQUIDITY DEVELOPMENTS.....	22
2.3.4 INTEREST RATES DEVELOPMENTS.....	23
<b>III. INFLATION DEVELOPMENTS.....</b>	<b>25</b>
<b>IV. INFLATION OUTLOOK AND RISKS .....</b>	<b>29</b>
4.1 DEMAND-SIDE PRESSURES .....	29
4.2 SUPPLY SHOCKS.....	29
4.3 EXCHANGE RATE DEVELOPMENTS .....	29
4.4 GLOBAL AND REGIONAL INFLATIONARY PRESSURES.....	29
4.5 INFLATION FORECASTS.....	29

**LIST OF TABLES**

TABLE 1: ECONOMIC GROWTH DEVELOPMENTS (IN %)	2
TABLE 2: ECONOMIC GROWTH IN EAC COUNTRIES (IN %)	3
TABLE 3: HEADLINE INFLATION IN EAC COUNTRIES, IN %	3
TABLE 4: WORLD BANK COMMODITY PRICES (IN PERCENT CHANGE)	4
TABLE 5: INTEREST RATES DEVELOPMENTS (IN % PER ANNUM)	5
TABLE 6: EXCHANGE RATE (DOLLARS/ UNIT CURRENCY, INVERSELY FOR YEN)	5
TABLE 7: DOMESTIC DEMAND (% CHANGE)	7
TABLE 8: AGRICULTURE PRODUCTION (CHANGE IN PERCENTAGE)	9
TABLE 9: EXPORTS DEVELOPMENTS (ANNUAL % CHANGE)	12
TABLE 10: IMPORTS DEVELOPMENTS (ANNUAL % CHANGE)	14
TABLE 11: TRADE FLOW OF RWANDA WITHIN EAC BLOC, (VALUE FOB IN MILLION USD)	16
TABLE 12: RWANDA INFORMAL CROSS BORDER TRADE (USD MILLION)	17
TABLE 13: APPRECIATION/ DEPRECIATION RATE OF SELECTED CURRENCIES AGAINST THE FRW	18
TABLE 14: MONETARY AGGREGATES (FRW BILLION)	19
TABLE 15: NEW AUTHORIZED LOANS BY SECTOR (FRW BILLION, UNLESS OTHERWISE INDICATED)	20
TABLE 16: DISTRIBUTION OF NEW AUTHORIZED LOANS BY SECTOR OF ACTIVITIES (% SHARE OF TOTAL NEW LOANS)	21
TABLE 17: DEPOSITS BY CATEGORY OF DEPOSITORS (% SHARE)	22
TABLE 18: MOST LIQUID ASSETS OF COMMERCIAL BANKS (FRW BILLION)	23
TABLE 19: MARKET INTEREST RATES (% AVERAGE)	24
TABLE 20: INFLATION DEVELOPMENTS FOR KEY ITEMS (% , Y-O-Y)	25



## LIST OF FIGURES

Figure 1: Crude oil price developments (USD/barrel).....	4
Figure 2: Quarterly Real GDP growth (% change, y-o-y).....	8
Figure 3: The Output gap for Rwanda (% deviation from the trend).....	10
Figure 4: Trade balance in millions of USD .....	11
Figure 5: Exports developments (% share).....	11
Figure 6: Imports developments (% share).....	14
Figure 7: Drivers of real effective exchange rate .....	18
Figure 8: Currency to broad money ratio and CIC growth (% , y-o-y).....	21
Figure 9: Type of deposits (% share).....	22
Figure 10: Money market interest rates (%).....	23
Figure 11: Contribution to Food Inflation (% , Y-o-Y).....	25
Figure 12: Contribution to Housing Inflation (% , Y-o-Y) .....	26
Figure 13: Contribution to Transport Inflation (% , Y-o-Y) .....	26
Figure 14: Contribution to Imported Inflation (% , Y-o-Y) .....	27
Figure 15: Contribution to Domestic Inflation (% , Y-o-Y) .....	27



## **I. GLOBAL ECONOMIC AND FINANCIAL DEVELOPMENTS**

### **1.1 Economic Developments**

The world economic performance remained strong in 2018Q2 and this good performance is expected to continue in 2018Q3. According to the IMF's July 2018 estimates, the world economy is projected to grow by 3.9 percent in both 2018 and 2019 against 3.7 percent recorded in 2017, supported by favorable global financial conditions, the improvement in global trade and international commodity prices. The global Manufacturing Purchase Manager Index remains high, pointing to favorable business conditions that are supporting a strong economic outlook. However, the potential re-emergence of global trade barriers, rising volatility in asset markets and continued US interest rates normalization are likely to impact the near-term growth prospects. Positive growth expectations in 2018 are likely to push up core inflation, stimulating Central Banks to consider tightening policy. However, core inflation remained below central banks' targets in most developed countries, pointing to a continuation of accommodative monetary policy, except in the US.

#### **1.1.1 Developments in United States**

In USA, Real GDP grew by 4.2 percent in 2018Q2 from 2.0 percent in 2018Q1, buoyed by increased business investments, and rising consumer spending. The US growth outlook is anticipated to remain strong, standing at 3.0 percent in 2018Q3 due to expansionary fiscal policy. For 2018, US GDP growth rate is expected to pick up to 2.9 percent from 2.3 percent in 2017. The cut in the tax bill and the Job Act of 2017 are likely to further spur growth for the year 2018. US inflationary pressures continue to rise, with annual inflation increasing from 2.4 percent in March 2018 to 2.9 percent in June 2018. Core inflation increased to 2.3 percent in June 2018 higher than the Federal Reserve target of 2.0 percent. As inflationary pressures keep rising, markets are expecting more interest rate hikes over the course of the year 2018.

#### **1.1.2 Developments in Eurozone**

In Eurozone, real GDP increased by 2.1 percent in 2018Q2 compared to 2.5 percent realized in 2018Q1, and is expected to grow by 1.9 percent in 2018Q3. Economic growth is projected to decelerate from 2.4 percent in 2017 to 2.2 percent in 2018 and 1.9 percent in 2019. Forecasts for 2018 growth have been revised down for Germany, France, and Italy. Wider sovereign spreads and tighter financial conditions in the wake of recent political uncertainty are likely to weigh on domestic demand. Overall, however, the growth remains strong on the back of healthy global demand and improving productivity.

**Table 1: Economic growth developments (in %)**

	2017				2018				Annual average project.		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2017	2018	2019
United States (QoQ)	1.2	3.1	3.2	2.9	2.0	4.2	3.0	2.8	2.3	2.9	2.7
Euro area (YoY)	2.1	2.4	2.6	2.7	2.5	2.1	1.9	1.7	2.4	2.2	1.9
Japan (YoY)	-	-	2.0	2.0	1.0	1.3	0.8	1.0	1.7	1.0	0.9
United Kingdom (YoY)	-	-	1.7	1.4	1.2	1.3	1.3	1.3	1.7	1.4	1.5
China (YoY)	6.9	6.9	6.8	6.8	6.8	6.7	6.6	6.5	6.9	6.6	6.3
India (YoY)	6.1	5.6	6.3	7.0	7.7	8.2	7.4	7.2	6.7	7.3	7.5

**Source:** BLOOMBERG and IMF, World economic Outlook, April 2018

In 2018Q2, inflation in Eurozone stood at 2.0 percent, up from 1.3 percent in 2018Q1 and 1.3 percent in 2017Q2. Inflation remains below the ECB target and this may continue influencing the ECB monetary policy.

### 1.1.3 Developments in China

Chinese GDP grew by 6.7 percent in 2018Q2, backed by stronger external demand, improving domestic demand together with resilient real estate activity. Real GDP growth is projected to slow to 6.6 percent in 2018Q3, reflecting continuous drag from Chinese tightening monetary policy and the slowing fiscal stimulus as well as the issue of the US trade barriers. This may affect China's exports growth. Projections point to a deceleration in China's GDP growth to 6.6 percent in 2018 and further to 6.3 percent in 2019 from 6.9 percent recorded in 2017. In China, inflation increased to 1.9 percent in June 2018, from 1.8 percent recorded in May 2018, and 1.5 percent in June 2017. The increase was reflected in consumer goods prices.

### 1.1.4 Developments in Sub-Saharan Africa and EAC

In Sub-Saharan Africa, economic growth is projected to rise to 3.4 percent in 2018 and to 3.8 percent in 2019, from 2.8 percent in 2017. Growth is expected to pick up in commodity exporting countries, such as South Africa and Nigeria, as the recovery in commodity prices continues. South Africa is expected to grow by 1.5 percent in 2018 and 1.7 percent in 2019 up from 1.3 percent recorded in 2017. In Nigeria, GDP is projected to increase by 2.1 percent and 2.3 percent respectively in 2018 and 2019 against -1.6 percent registered in 2017.

Inflationary pressures were mainly due to the impact of droughts and weak currencies in Sub-Saharan Africa. Headline inflation was 11.0 percent in 2017 but is expected to fall to 9.5 percent in 2018 and 8.9 percent in 2019 as local currencies will be recovering, following the increase in commodity exports.

In the East African Community (EAC), GDP growth is projected at 5.8 percent in 2018 and 6.2 percent in 2019 from 5.2 percent in 2017. Apart from Burundi whose growth is projected to remain subdued, growth in the EAC countries is expected to remain strong in both 2018 and 2019.

Rwanda's economic growth stood at 10.6 percent in 2018Q1 from 10.5 percent in 2017Q4. In Uganda, GDP growth remained unchanged at 6.4 percent in 2018Q1 and 2017Q4. During the same period, Kenya's real GDP growth increased from 5.3 percent to 5.7 percent.

**Table 2: Economic growth in EAC countries (in %)**

	2016	2017				2018	Annual Average			
	Q4	Q1	Q2	Q3	Q4	Q1	2016	2017	2018	2019
Burundi	-	-	-	-	-	-	-	0.0	0.1	0.4
Kenya	6.1	4.8	4.7	4.7	5.3	5.3	5.7	4.8	5.5	6.0
Rwanda	2.4	1.7	4.0	8.0	10.5	10.5	10.6	6.1	7.2	7.8
Tanzania	5.6	5.7	7.8	6.8	8.1	8.1	-	7.1	6.4	6.6
Uganda	2.8	4.5	6.5	7.3	6.4	6.4	6.4	4.5	5.2	5.8

**Source:** National Bureau of Statistics Websites and IMF WEO, April 2018

In EAC, despite rising oil prices, inflation remained benign in the first half of 2018. Low inflation levels followed rising agriculture production owing to favorable weather conditions as well as easing exchange rate pressures.

**Table 3: Headline inflation in EAC countries, in %**

	2017				2018						Annual average	
	Mar.	Jun.	Sept.	Dec.	Jan.	Feb.	Mar.	Apr.	May	June.	2017	2018Proj
Burundi	21.1	15.1	15.2	10.3	6.1	-1.3	-2.6	-1.7	-1.0	-0.4	16.6	12.7
Kenya	10.3	9.2	7.1	4.5	4.8	4.5	4.2	3.7	4.0	4.3	8.0	4.8
Rwanda	7.7	4.8	3.8	0.7	1.3	0.7	0.9	1.7	3.0	2.9	4.8	2.8
Tanzania	6.4	5.4	5.3	4.0	4.0	4.1	3.9	3.8	3.6	3.4	5.3	4.8
Uganda	6.4	6.4	5.3	3.3	3.0	2.1	2.0	1.8	1.7	2.2	5.6	3.6

**Source:** Country Bureaus of Statistics, IMF, World Economic Outlook, April 2018

## 1.2 Recent developments in commodity prices

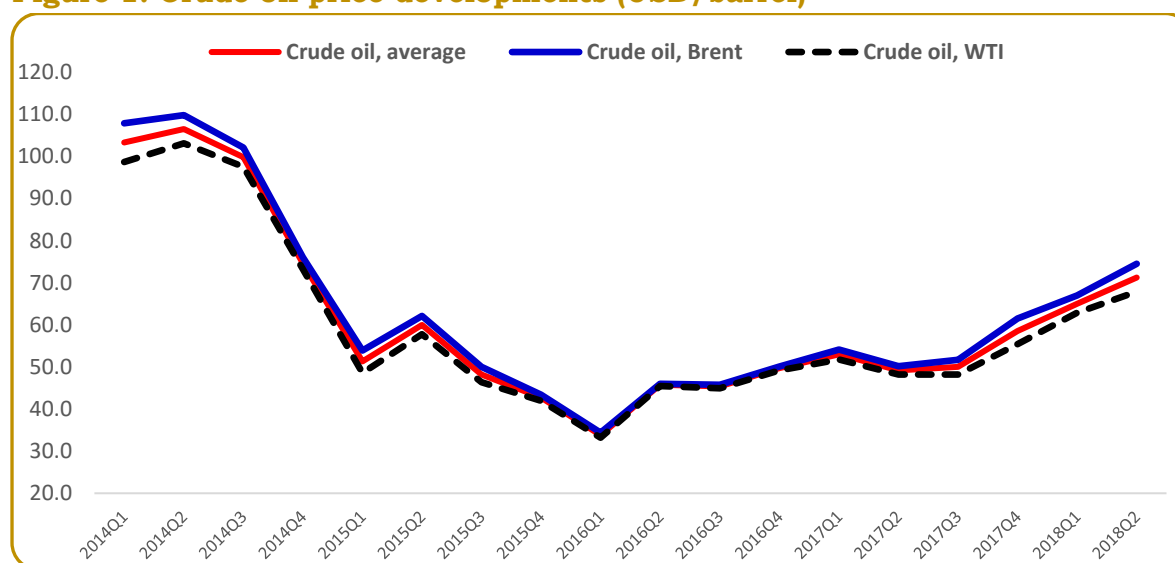
In 2018Q2, the global commodity price index continued to increase, reflecting improving global economic activity and supply constraints for a number of commodities. Global energy and non-energy prices picked up, spurred by a sustained global demand. Crude oil prices rose on the back of geopolitical concerns, tightening product inventories as well as a strong global demand, in addition to the continuous OPEC oil supply adjustments.

**Table 4: World Bank commodity prices (%)**

	2017		2018		Forecast, % changes	
	Q1	Q2	Q1	Q2	2018	2019
<b>Energy</b>	<b>57.8</b>	<b>14.8</b>	<b>21.3</b>	<b>40.1</b>	<b>19.9</b>	<b>-0.4</b>
Crude oil, average	61.8	10.3	22.0	44.5	23.1	0.0
<b>Non-energy</b>	<b>13.0</b>	<b>2.1</b>	<b>3.6</b>	<b>8.7</b>	<b>4.1</b>	<b>0.3</b>
<b>Agric. commodities</b>	<b>7.7</b>	<b>-3.1</b>	<b>-0.5</b>	<b>4.3</b>	<b>2.3</b>	<b>1.3</b>
Beverages	-0.4	-9.9	-7.3	1.3	-0.2	1.2
Arabica coffee	10.0	-5.5	-17.2	-10.0	-2.1	0.3
Robusta coffee	43.3	21.5	-17.3	-13.4	-10.3	1.0
Tea Mombasa	20.3	32.9	-3.1	-12.6	-1.6	0.3
Grains/Cereals	-6.0	-4.0	12.3	11.9	7.6	1.5
<b>Metals &amp; Minerals</b>	<b>32.0</b>	<b>19.6</b>	<b>13.8</b>	<b>19.4</b>	<b>8.6</b>	<b>-2.1</b>
Tin	29.6	17.9	5.9	5.1	0.0	3.2
Iron ore	77.7	13.2	-13.0	3.6	-10.9	-6.3
Gold	3.3	-0.2	9.0	3.9	3.3	-1.4
<b>Fertilizers</b>	<b>-9.1</b>	<b>-9.6</b>	<b>0.6</b>	<b>10.1</b>	<b>2.0</b>	<b>2.5</b>

**Source:** World Bank

Average prices rose for agriculture commodities because of unfavorable weather conditions that reduced harvests of many grains and oilseeds. During the same period, Arabica and Robusta coffee prices fell by 10.0 percent and 13.4 percent respectively. Prices for fertilizers went up by 10.1 percent in 2018Q2 compared to a decrease of 9.6 percent in the same period of 2017. Prices for the three major fertilizers (DAP, TSP and UREA) are now higher compared to those of last year.

**Figure 1: Crude oil price developments (USD/barrel)****Source:** World Bank

### 1.3 Financial markets and Foreign Exchange market

The Monetary policy remained accommodative in most advanced economies with the central bank rate remaining unchanged in the Eurozone and UK. The European Central Bank rate (ECB) was maintained at 0 percent and the asset purchase program kept at 30 billion Euro a month and likely to remain until September 2018. The Bank of England (BoE) kept unchanged the bank rate at 0.50 percent in 2018Q2, as inflation remained broadly stable at around 2.3 percent since 2018Q1. The Bank of Japan continued to apply a negative 0.1 percent interest rate and to buy government bonds to encourage the financing of economic activities.

The three-month deposit rates remained negative in the Eurozone, standing at -0.37 percent in 2018Q2 same as in 2018Q1, affecting banks' deposits in the Central bank and encouraging economic financing.

**Table 5: Interest rates developments (in % per annum)**

		2016			2017				2018	
		Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
USA	3-month deposit rate	1.018	0.885	1.535	1.430	1.300	1.350	1.705	2.295	2.365
	10-year interest rate	1.470	1.596	2.444	2.387	2.304	2.334	2.405	2.739	2.860
Euro area	3-month deposit rate	-0.270	-0.280	0.350	-0.320	-0.388	-0.373	-0.375	-0.373	-0.373
	10-year interest rate	-0.130	-0.119	0.208	0.328	0.466	0.464	0.427	0.497	0.302
Japan	3-month deposit rate	-0.120	-0.310	-0.440	-0.090	-0.095	-0.145	-0.120	0.750	0.710
	10-year interest rate	-0.217	-0.089	0.046	0.070	0.086	0.068	0.048	0.049	0.036
UK	3-month deposit rate	0.670	0.560	0.610	0.430	0.400	0.380	0.511	0.702	0.710
	10-year interest rate	0.867	0.746	1.239	1.139	1.257	1.365	1.190	1.350	1.278

**Source:** Bloomberg

On the foreign exchange market, the US dollar is recovering against major currencies, notably the Euro and the British pound while it continued to weaken compared to the Yen.

**Table 6: Exchange rate (dollars/unit currency, inversely for Yen)**

	2016	2017				2018	
	Q4	Q1	Q2	Q3	Q4	Q1	Q2
USD/GBP	0.8101	0.7968	0.7677	0.7465	0.7402	0.7134	0.7572
USD/EUR	0.9506	0.9385	0.8752	0.8464	0.8330	0.8114	0.8558
USD/JPY	116.96	111.39	112.39	112.51	112.69	106.28	110.76

**Source:** Bloomberg

In 2018Q2, the US dollar appreciated by 2.30 percent against the pound and 2.74 percent against the Euro compared to 2017Q4. The US dollar weakened by 1.71 percent against the Japanese Yen, compared to 2017Q4.

## 1.4 Outlook for the global economy

The global economy remains strong. The prospective growth is supported by favorable global financial conditions, the improvement in global trade and international commodity prices. Most advanced economies are performing above their potential, indicating a continued stronger aggregate demand in the near future.

Despite the current move in Federal Reserve monetary policy, which is, creating volatility in asset markets, US positive growth dynamics continue and production is expected to increase. Core and headline inflation are moving slightly higher than the target, pointing to further interest rate hikes. The Eurozone economy is expected to decelerate. However, growth remains strong on the back of healthy global demand, improving productivity and competitiveness. Rising demand together with improving private consumption are expected to push inflation close to the target.

In emerging and developing economies, the growth will remain close to 2017 levels as a gradual slowdown in Chinese growth prospects will be offset by the recovery in commodity exporting countries. Growth for all EAC economies is expected to remain strong in 2018 and 2019.

Globally, strong global demand is likely to continue supporting the Rwandan economic prospects. Foreign demand for local export products is expected to remain strong and continue supporting Rwandan export earnings, particularly, from metals and minerals. However, the excess supply of coffee and tea, may exert downward pressures to export earnings.

On the other hand, rising global demand and increasing international commodity prices are likely to fuel inflation globally particularly as spare capacity gets used up. The resulting interest rate tightening may drive up short-term and long-term interest rates and therefore strengthening currencies in major advanced economies. This will result into high imported inflation and financial market volatilities. Besides, there may be capital flights from emerging and developing economies searching for higher returns in advanced market economies. An appreciation of the USD and/or other major currencies against the Franc Rwandais, a continued increase in oil prices and rising foreign inflation are likely to exert pressures on domestic prices in 2018.

## II. DOMESTIC ECONOMY AND FINANCIAL DEVELOPMENTS

### 2.1 Domestic Demand and Output

The Rwandan economy recorded good performance in 2018Q2, growing by 6.7 percent. The growth was mainly supported by favorable weather conditions, recovery in construction sector, improvement in transport services and increase of fixed investment as well as private consumption.

#### 2.1.1 Domestic demand

Domestic demand recovered in 2018Q2, growing by 7.1 percent from a decline of 0.2 percent in 2017Q2, boosted by strengthening investment and improvement in private consumption.

**Table 7: Domestic demand (% change)**

	2017				2018	
	Q1	Q2	Q3	Q4	Q1	Q2
<b>Domestic demand</b>	<b>-0.5</b>	<b>-0.2</b>	<b>3.8</b>	<b>1.4</b>	<b>9.3</b>	<b>7.1</b>
<b>Total final consumption Expenditure</b>	<b>5.0</b>	<b>0.0</b>	<b>6.0</b>	<b>1.0</b>	<b>5.0</b>	<b>3.0</b>
Government	6.0	18.0	9.0	10.0	0.0	-1.0
Households and NGOs	5.0	-2.0	5.0	-1.0	6.0	4.0
<b>Gross capital formation</b>	<b>-12.0</b>	<b>-2.0</b>	<b>16.0</b>	<b>27.0</b>	<b>36.0</b>	<b>21.0</b>
Gross fixed capital formation	-12.0	-1.0	15.0	27.0	35.0	20.0
Construction	-7.0	-4.0	-1.0	-1.0	8.0	11.0
Other	-20.0	3.0	48.0	94.0	90.0	36.0
Change in inventories	-33.0	-11.0	30.0	33.0	79.0	33.0
<b>Imports of goods &amp; serv.</b>	<b>4.0</b>	<b>0.0</b>	<b>17.0</b>	<b>20.0</b>	<b>17.0</b>	<b>7.0</b>

**Source:** National Institute of Statistics of Rwanda

Gross capital formation continued to sustain its recovery with an expansion of 21.0 percent in 2018Q2 from a decline of 2.0 percent in 2017Q2. This increase came from other fixed investment; that expanded by 36.0 percent and investment for construction purpose; which recovered, growing by 11.0 percent in 2018Q2 from a decrease of 4.0 percent in 2017Q2. The high growth of other fixed investment is reflected in imported machines and devices equipment, which increased by 4.0 percent in value in 2018Q2 from a decline of 32.7 percent in 2017Q2. The recovery of construction investment was driven by on-going construction projects and is indicated by the good performance of construction sector. Private consumption increased by 4.0 percent in 2018Q2 from -2.0 percent in 2017Q2; partly supported by an increase in food production following good harvest in agricultural season A, 2018. This improvement in private consumption strengthened the increase in total final consumption by 3.0 percent in 2018Q2. Private consumption represented 83.9 percent in total final consumption of 2018Q2.

After stagnating in 2017Q2, the imports of goods and services increased by 7.0 percent in 2018Q2 led mainly by goods imports, which increased by 8.4 percent in 2018Q2 from a decline of 11.8 percent in 2017Q2. Goods imports' growth was widespread as consumer goods imports expanded by 14.1 percent in volume, capital



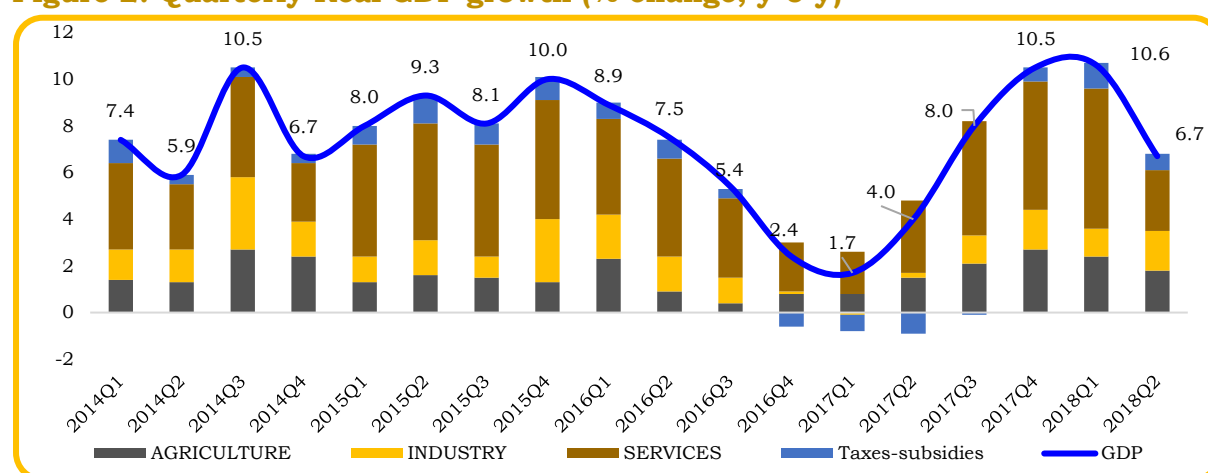
goods by 15.0 percent, intermediary goods by +33.2 percent and energy and lubricants by +30.6 percent.

## 2.1.2 Economic performance by sector

### 2.1.2.1 Real Sector

Growth in 2018Q2 was boosted by outstanding performance of industry sector, which grew 10.0 percent in 2018Q2 from 1.0 percent in 2017Q2. The agriculture sector followed with a growth of 6.0 percent and the services sector rose by 5.0 percent. However, the services continued to be the leading sector, with a share of 47.0 percent of GDP in 2018Q2 while agriculture and industry sectors represent 30.0 percent and 16.0 percent respectively.

**Figure 2: Quarterly Real GDP growth (% change, y-o-y)**



**Source:** NBR, Monetary Policy Department

The industry sector was boosted by the recovery of construction sub-sector as well as the good performance of manufacturing sub-sector, both representing 78.6 percent of industry sector. The construction sub-sector grew by 11.0 percent in 2018Q2 from a decline of 4.0 percent in 2017Q2 supported by on-going construction projects, principally Bugesera International Airport construction. The latter was further reflected in the increase of domestic demand of cement by 37.3 percent in 2018Q2 against an increase of 4.7 percent in 2017Q2. Manufacturing sub-sector increased by 12.0 percent in 2018Q2 against 6.0 percent recorded in the same period of 2017. This growth was mainly supported by “food industries”; “Beverages & tobacco”; “textiles, clothing and leather goods industries” and “metal products, machinery and equipment industries” that grew by 19.0 percent, 8.0 percent, 13.0 percent and 37.0 percent respectively in 2018Q2 from 10 percent, -10.0 percent, 39.0 percent and 2.0 percent in 2017Q2.

The agriculture sector recorded a good performance in 2018Q2, growing to 6.0 percent from 4.0 percent in 2017Q2, mainly driven by food crops production which represents 59.0 percent of the sector. Food crops increased by 5.9 percent in 2018Q2 owing to favorable weather conditions during the agricultural season A of 2018.

**Table 8: Agriculture production (change in %)**

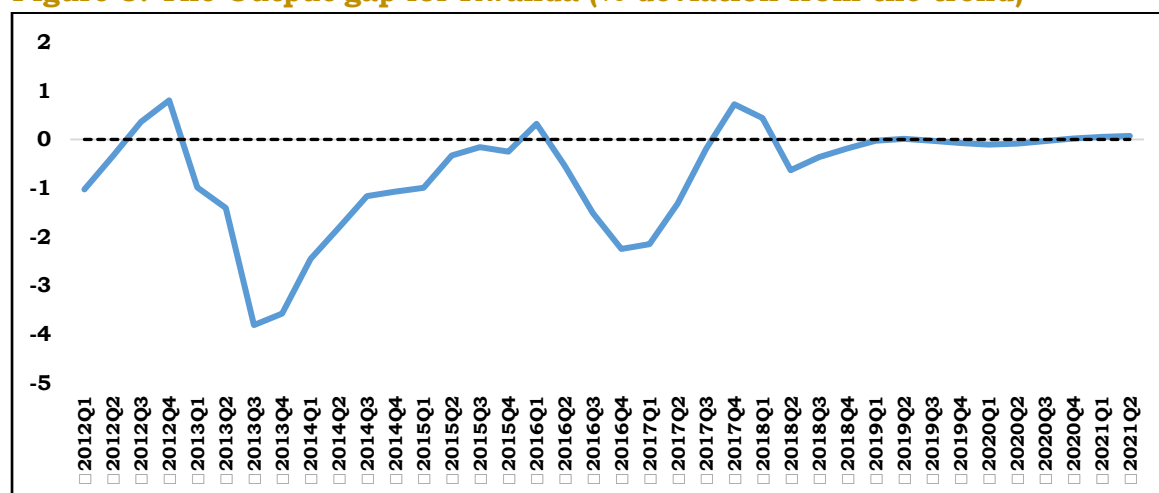
	2017 Q1	2017 Q2	2018 Q1	2018 Q2
<b>Agriculture</b>	<b>2.7</b>	<b>5.7</b>	<b>8.4</b>	<b>6.5</b>
Food crops	4.1	4.1	5.9	5.9
Cereals	5.0	5.0	3.5	3.5
Roots & Tubers	11.6	11.6	8.7	8.7
Vegetables	-8.3	-8.3	15.9	15.9
Bananas & fruit	7.6	7.6	-8.1	-8.1
Oil seeds and oleaginous fruit	43.1	43.1	7.8	7.8

**Source:** NBR, Statistics Department

The services sector increased by 5.0 percent in 2018Q2, supported by the recovery of wholesale and retail trade (+18.5 percent from -2.0 percent in 2017Q2) and good performance of transport services (+20.5 percent from 6.0 percent in 2017Q2). Wholesale and retail trade performance was supported by the recovery in private consumption as well as construction sector; which was in turn reflected in the demand of cement. The good performance in the transport services was enhanced by air transport that increased by 17.0 percent in 2018Q2 and land transport services. The latter category recovered after falling by 8.0 percent in 2017Q2 and increased by 12.0 percent in 2018Q2. The services sector's performance resulted also from the good performance of information and communication services (+18.0 percent), hotels and restaurant (+9.0 percent) and financial services (+7.0 percent). However, the decline of Administrative & support service activities (-12.0 percent) and Professional, scientific & technical activities (-6.0 percent) weighed on the good performance of other sub-sector, leading to the slowdown of the services sector in 2018Q2 compared to 6.0 percent growth of 2017Q2.

### 2.1.3 The Output gap

The estimated output gap of 2018Q2 stood at -0.6 percent, improving from -1.3 percent of 2017Q2, in line with the observed good performance of the Rwandan economy in the last four quarters. Nevertheless, the aggregate demand is still below potential. Furthermore, the projected trend of output gap rises throughout the second half of 2018, therefore signaling continuity of good economic performance in that period.

**Figure 3: The Output gap for Rwanda (% deviation from the trend)**

**Source:** NBR, Monetary Policy Department

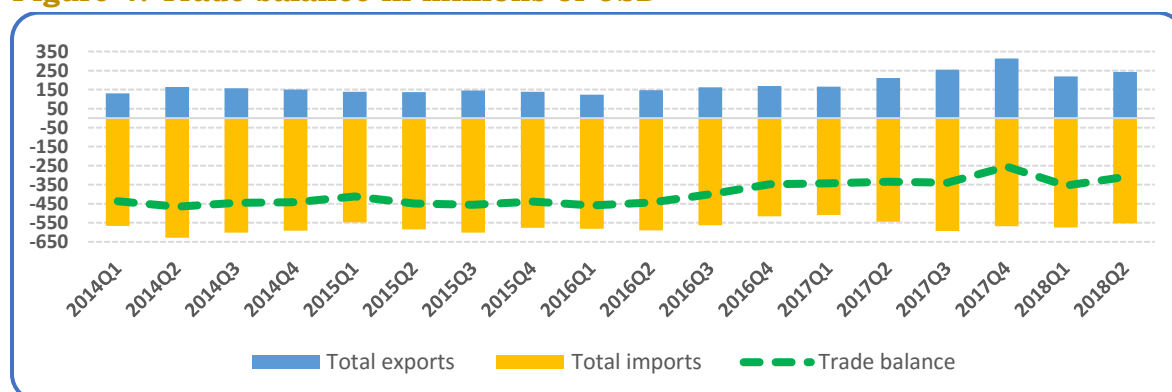
### 2.1.4 Outlook of the domestic demand and output

The Good economic performance realized in the first half of 2018, is expected to continue in the second half of 2018. The trend of output gap provides evidence for improving aggregate demand in the second half of 2018. This coincides with 2018 agricultural season B good performance, on-going construction projects and improving international mineral commodity prices. Despite flooding and land sliding in some regions, the agricultural season B, 2018 was good as reflected by the decline in food inflation and farmers' views in the price expectations survey. During the first two months of 2018Q3, local food inflation decreased by 1.6% on average against an increase of 6.9% on average during the same period in 2017. Commodity prices on international market are projected to increase in 2018, supported by improving global growth combined with some supply commodity constraints. Metal and minerals international prices are projected to increase by 9.0% in 2018 and this is expected to boost Rwanda's minerals exports.

## 2.2 External Sector Developments

### 2.2.1 Formal trade balance

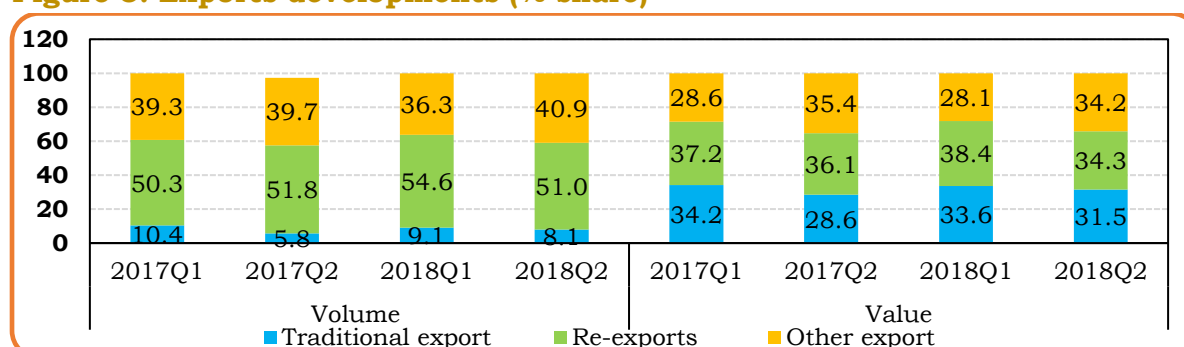
Despite the growth in formal imports value by 1.4 percent, Rwanda's trade deficit improved by 7.6 percent in 2018Q2, to a deficit of USD 309.0 million from a deficit of USD 334.6 million in 2017Q2. The improvement followed an increase in formal exports value by 15.8 percent. Formal exports covered 44.1 percent of formal imports in 2018Q2 from 38.6 percent in 2017Q2.

**Figure 4: Trade balance in millions of USD**

**Source:** NBR, Monetary Policy Department

### 2.2.1.1 Formal exports of goods

Rwanda's formal exports are composed of traditional exports, re-exports and non-traditional exports. In 2018Q2, formal exports were dominated by re-exports with a share of 34.3 percent of the total export earnings, followed by non-traditional exports with 34.2 percent, and traditional exports<sup>1</sup> representing 31.5 percent. The gradual diversification of the export base continued, as the share of traditional exports is gradually declining.

**Figure 5: Exports developments (% share)**

**Source:** NBR, Monetary Policy Department

Total formal export receipts continued to expand, recording an increase of 15.8 percent in 2018Q2 from 43.5 percent in 2017Q2 (USD 243.43 million in 2018Q2 from USD 210.14 million in 2017Q2), following growth recorded by minerals (+62.3 percent), coffee (+14.7 percent), tea (+1.7 percent), re-exports (+10.2 percent) and other exports (+12.0 percent). Formal exports volume also increased by 12.6 percent in 2018Q2, due to the growth in coffee (+7.7 percent), minerals (+24.1 percent), tea (+13.7 percent), re-exports (+11.0 percent) and non-traditional exports (+16.1 percent).

<sup>1</sup> composed of tea, coffee, pyrethrum, minerals as well as hides and skins

**Table 9: Exports developments (annual % change)**

	Volume				Value			
	2017Q1	2017Q2	2018Q1	2018Q2	2017Q1	2017Q2	2018Q1	2018Q2
<b>Total exports</b>	<b>43.3</b>	<b>27.1</b>	<b>25.4</b>	<b>12.6</b>	<b>35.3</b>	<b>43.5</b>	<b>34.3</b>	<b>15.8</b>
<b>Traditional exports</b>	8.2	-31.4	9.1	56.8	16.7	19.4	30.0	27.6
Coffee	-13.3	10.9	50.3	7.7	-12.1	14.0	54.3	14.7
Tea	13.2	-2.5	6.9	13.7	25.9	36.4	13.6	1.7
Minerals	22.2	7.2	12.3	24.1	26.4	12.3	40.7	62.3
Cassiterite	42.7	25.6	1.0	26.2	63.9	46.4	-2.1	30.5
Coltan	17.1	4.7	20.5	26.9	4.8	-5.0	83.8	96.0
Wolfram	-16.0	-25.8	43.5	14.2	-13.0	-12.9	109.7	66.2
Hides and Skins	19.5	-1.8	-50.5	-60.2	24.7	18.4	-25.4	-42.5
Pyrethrum	-91.3	-38.1	2427.7	796.5	-92.2	-39.7	923.6	15.2
<b>Re-exports</b>	50.7	34.6	36.5	11.0	38.3	20.7	41.6	10.2
<b>Non-Traditional exports</b>	46.7	24.9	15.5	16.1	61.7	122.9	30.1	12.0

**Source:** NBR, Statistics Department

Traditional exports, composed of coffee, tea, minerals, pyrethrum as well as hides and skins rose by 27.6 percent, amounting to USD 76.61 million in 2018Q2 from USD 60.03 million in 2017Q2 as reflected in all its components.

Compared to 2017Q2, coffee exports receipts increased by 14.7 percent in 2018Q2, to USD 9.76 million from USD 8.51 million, because of increased exported volume by 7.7 percent as well as rising unit price by 6.5 percent, from 2.76 USD/Kg in 2017Q2 to 2.94 USD/Kg in 2018Q2. The growth of coffee's prices was due to the increased exports volume of fully washed coffee (+35.5 percent). The increase in coffee volume exports is attributable to increased production by 12.7 percent, from 3,053.4 tons in 2017Q2 to 3,443.5 tons in 2018Q2 following favorable weather conditions.

Tea exports receipts slightly increased by 1.7 percent from USD 23.62 million in 2017Q2 to USD 24.01 million in 2018Q2 due to the increase in volume, outweighing the decrease in prices. Tea exports volume increased by 13.7 percent, from 7,336.4 tons in 2017Q2 to 8,339.3 tons in 2018Q2, on the account of increased tea production that rose by 10.7 percent from 7,712.4 tons in 2017Q2 to 8,536.8 tons in 2018Q2. The increased production came from good season for export crops, while its prices decreased by 10.6 percent from 3.22 USD/Kg in 2017Q2 to 2.88 USD/Kg in 2018Q2.

The mining sector continued to perform well in 2018Q2, owing to rising metal prices at the international market on the account of strong global demand. Exports value of traditional minerals (Coltan, Cassiterite and Wolfram) significantly increased by 62.3 percent from USD 25.04 million recorded in 2017Q2 to USD 40.64 million in 2018Q2. This good performance was due to the increase in export earnings from Coltan (+96.0 percent), cassiterite (+30.5 percent) as well as wolfram (+66.2 percent) following the rise in their unit prices that rose by 54.4 percent, 3.4 percent and 45.5 percent respectively.

Receipts from exported hides and skins decreased by 42.5 percent, from USD 1.60 million to USD 1.09 million, mainly due to the decrease in exported volume by 60.2 percent. However, the unit price increased by 44.5 percent from 1.27 USD/Kg in 2017Q2 to 1.83 USD/Kg in 2018Q2. Pyrethrum exports performed well in 2018Q2 in both value and volume. Exports receipts from pyrethrum amounted to USD 1.11 million in 2018Q2 from USD 0.96 million in 2017Q2.

Re-exports (mainly composed of petroleum products, machines and engines, vehicles and other re-exports) increased in both value and volume by 10.2 percent and 11.0 percent respectively. This was mainly driven by increase in other re-exports by 30.7 percent in value and 42.4 percent in volume, despite a decrease in re-exports of petroleum products by 13.7 percent and 18.8 percent in value and volume respectively. Changes in other re-exports component was due to the increased demand of foodstuffs like cooking oil, rice and other manufactured products exported to DRC.

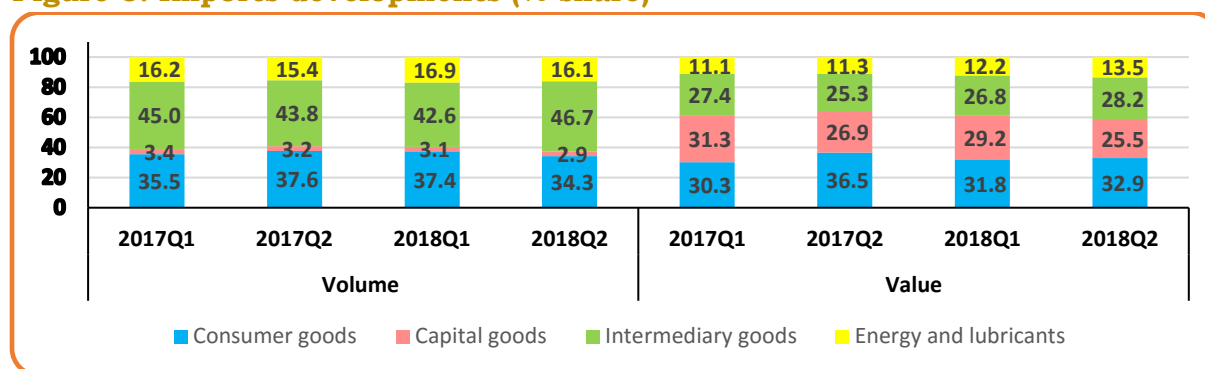
Non-traditional exports, dominated by other minerals, products of milling industry and other manufactured products significantly increased by 12.0 percent, amounting to USD 83.27 million in 2018Q2 from USD 74.32 million in 2017Q2. The increase mainly came from the growth in exports of the products of milling industry by 35.5 percent in 2018Q2, to USD 16.87 million from USD 12.63 million in 2017Q2, thanks to the increased production by the local milling industry prompted by high demand from DRC and Uganda. In addition, revenues from flowers, mainly exported to Netherlands, went up to USD 0.96 million in 2018Q2 from USD 0.50 million in the corresponding period of 2017 on the account of new investments that boosted production. The growth in the non-traditional category is also explained by the increase in exports of other manufactured products like textiles (+107.9 percent), iron and steel (+79.6 percent) and mattresses (+15.7 percent) among others, following the government initiative of increasing local production of goods for exports.

### **2.2.1.2 Formal imports of goods**

Rwanda's formal imports are composed of consumer goods, capital goods, intermediary goods as well as energy and lubricants. In 2018Q2, imports in volume were dominated by intermediary goods with a share of 46.7 percent of the total formal imports volume, followed by consumer goods (34.3 percent), energy & lubricants (16.1 percent) and capital goods (2.9 percent). In value terms, consumer goods dominated with a share of 32.9 percent, followed by intermediary goods (28.2 percent), capital goods (25.5 percent) and energy & lubricants (13.5 percent).

In 2018Q2, formal imports value increased by 1.4 percent from -7.4 percent recorded in 2017Q2, (to USD 552.46 million from USD 544.72 million in 2017Q2), due to the increase in intermediary goods by 13.1 percent and in energy & lubricants by 21.3 percent. Consumer goods decreased by 8.7 percent and capital goods by 4.1 percent. The volume of formal imports increased by 25.1 percent after a decrease of 1.3 percent in 2017Q2, following an increase in volume of all formal import components.

Figure 6: Imports developments (% share)



Source: NBR, Monetary Policy Department

Table 10: Imports developments (annual % change)

	Volume				Value			
	2017Q1	2017Q2	2018Q1	2018Q2	2017Q1	2017Q2	2018Q1	2018Q2
<b>Total imports</b>	-1.9	-1.3	11.6	25.1	-9.4	-7.4	13.0	1.4
<b>Consumer goods</b>	-10.8	1.4	17.7	14.1	-11.8	9.2	18.6	-8.7
Food products	-9.1	10.0	19.3	15.9	28.4	28.8	-4.6	2.8
Beverages and tobacco	48.7	-19.2	-12.5	64.4	10.9	-23.0	2.8	43.7
Article of Clothing	-63.3	-55.9	37.4	-16.3	-50.6	-7.7	69.7	-19.9
Health and care	-2.1	-19.9	7.9	12.6	-4.2	2.2	30.3	-16.6
Domestic articles	-4.9	-11.7	15.7	-5.9	-40.0	-37.2	18.2	-12.2
Non-utility transport	12.8	-25.3	22.6	50.9	9.9	-41.5	59.6	59.1
Papers and cartons	-22.8	38.6	15.1	-33.4	-24.3	31.8	21.1	-37.7
Other goods	-12.4	6.4	23.8	-9.3	-58.0	25.7	82.7	-33.2
<b>Capital goods</b>	-20.6	-23.0	1.4	15.0	-15.9	-30.3	5.6	-4.1
Transport Materials	-11.4	-18.7	-24.6	-12.3	20.4	-9.4	-32.3	-29.0
Machines, devices and tools	-34.5	-23.3	33.3	44.8	-28.1	-32.7	15.3	4.0
<b>Intermediary goods</b>	8.2	-1.7	5.7	33.2	-5.7	-3.3	10.5	13.1
Construction materials	-11.8	-10.6	16.7	30.2	-28.2	-21.3	7.1	15.4
Industrial products	31.9	12.8	-1.7	37.2	5.7	19.5	12.5	14.7
Fertilizers	0.7	-54.9	3.2	76.6	11.8	-61.9	-6.4	88.7
<b>Energy and lubricants</b>	-0.9	-0.8	16.5	30.6	12.1	15.4	24.4	21.3
Petroleum products	4.3	-1.2	14.0	14.7	14.0	15.1	24.8	23.4
<b>Trade balance (Exports less imports)</b>					-343.3	-334.6	-352.3	-306.7
<b>Cover rate of imports/ exports, %</b>					32.6	38.6	38.7	44.5

Source: NBR, Statistics Department

Imports of consumer goods mainly composed of foodstuffs decreased by 8.7 percent in value, to USD 181.52 million in 2018Q2 from USD 198.90 million in 2017Q2. Consumer goods increased by 14.1 percent in volume, to 197.83 thousand tons in



2018Q2 from 173.36 thousand tons in 2017Q2. The decrease in value of consumer goods is mainly driven by imports of articles of clothing by 46.7 percent, health and care (mainly pharmaceutical products) by 16.6 percent, as well as domestic articles (-12.2 percent). In contrast, imports of food products increased in value and volume by 2.8 percent and 15.9 percent respectively due to the rise in imports of cereals, flour and seeds (+7.5 percent) and vegetables, fruits and spices (+49.9 percent).

During the same period, imports of capital goods, dominated by machines, devices and tools as well as transport materials, decreased by 4.1 percent in value (to USD 140.74 million, from USD 146.73 million) and increased by 15.0 percent in volume. The increase in volume is largely due to soared imports bill on machinery, electrical and electronic equipments as their volume increased substantially by 44.8 percent, offsetting the decline in transports materials which dropped by 12.3 percent.

In 2018Q2, imports of intermediary goods, dominated by construction materials, industrial products and fertilizers, increased by 13.1 percent in value and 33.2 percent in volume, respectively. The increase is attributed to the increased demand of industrial products by 14.7 percent imported by various local industries for production purposes. In addition, imports of cement and similar products increased by 49.8 percent in value and 46.0 percent in volume, due to increased demand of imported cement (increase by 13.1 percent). CIMERWA's maintenance of machinery which occurred during April 2018 led to lower domestic production (-29.6 percent in 2018Q2 compared to +15.6 percent in 2017Q2),

Imports of energy and lubricants, of which 92.6 percent is petroleum products, increased by 21.3 percent in value and by 30.6 percent in volume. This increase is explained by the rise in imports of petroleum products by 23.4 percent in value and 14.7 percent in volume. Oil prices increased following the decision by OPEC countries, together with a number of non-OPEC producers led by Russia to cut oil production between January 2017 and March 2018. The deal was later extended to run through 2018 based on concerns about geopolitical tensions and supply disruptions in crude-producing nations.

### **2.2.2 Formal Trade with EAC Countries**

In 2018Q2, Rwanda's trade deficit with the EAC member countries expanded by 22.6 percent to stand at USD 80.8 million from USD 65.9 million in 2017Q2. The worsening of trade balance follows the high increase in imports bill by USD 15.5 million (representing +13.6 percent) that outweighed USD 0.6 million (+1.2 percent) increase in exports.

**Table 11: Trade flow of Rwanda within EAC bloc, (Value FOB in million USD)**

Exports (FOB USD)								Yoy % change
	2016Q4	2017Q1	2017Q2	2017Q3	2017Q4	2018Q1	2018Q2	
Burundi	10.1	4.8	5.6	5.5	5.3	3.9	3.4	-39.3
Kenya	24.84	25.6	32.5	21.1	31.5	29.5	32.5	0.0
South Sudan	0.2	0.2	0.1	0.1	0.2	0.2	0.2	100.0
Tanzania	0.57	0.4	0.3	0.8	0.5	0.4	0.5	66.7
Uganda	2.52	5.4	9.9	7.6	9.3	11.5	12.3	24.2
Total exports	38.2	36.4	48.4	35.1	46.8	45.4	49.0	1.2
Imports (CIF USD)								
Burundi	0.5	0.8	0.5	0.5	1.6	1.1	0.7	40.0
Kenya	33.7	33.7	40.1	40.8	33.4	36.9	37.4	-6.7
South Sudan	-	-	-	-	-	-	-	-
Tanzania	25.7	21.4	22.9	25.6	27.2	22.9	28.7	25.3
Uganda	55.4	51.3	50.8	58.4	57.2	57.5	63	24.0
Total imports	115.3	107.2	114.3	125.3	119.4	118.4	129.8	13.6
Trade balance	-77.1	-70.8	-65.9	-90.2	-72.6	-73	-80.8	22.6

**Source:** BNR, Statistics Department

The increase in Rwanda's exports to EAC region from USD 48.45 million to USD 49.0 million is largely driven by high increase in exports to Uganda, which expanded by USD 2.42 million (+24.4 percent) compared to the same period in 2017. This has been mainly on account of higher exports of milling industry products specifically corn soya blend exported by World Food Program that constitute around 58.6 percent of the total exports to Uganda. The ratio of exports to EAC region in the total formal exports reduced to 17.1 percent from 23.0 percent of the same period in 2017. It implies that the increase in exports to EAC were outweighed by that of those traded to the rest of the world.

Imports from EAC countries increased by 13.6 percent amounting to USD 129.8 million in 2018Q2 from USD 114.3 million in the same period of 2017. This growth is reflected in high increase in imports from Uganda, rising by USD 12.2 million to stand at USD 63.0 million. It was also reflected in imports from Tanzania growing by USD 5.8 million, totalizing USD 28.7 million. This is mainly because of higher imports of cement and food products especially cereals such as maize corn, rice and sorghum. The ratio of imports from EAC partner states in the total formal imports stood at 23.0 percent raising from 21.0 percent in the same period, an indication of EAC products surging on Rwanda's domestic market.<sup>3</sup>

### 2.2.3 Informal cross-border trade

In 2018Q2, Rwanda's informal cross border trade (ICBT) registered a trade surplus of USD 25.5 million (+38.2 percent) up from USD 18.4 million in 2017Q2. Informal exports with neighboring countries in 2018Q2 constitute a share of 11.1 percent of the total formal exports receipts and increased by 31.0 percent from USD 24.3 million in 2017Q2 to USD 31.8 million. The increase is explained by good performance in agricultural production following favorable weather conditions experienced during

season A 2018. We note that agricultural products are predominant in this trade. The main informal export partners include DR Congo, representing 79.2 percent of the total informal exports, followed by Uganda (+16.1 percent), Burundi (+3.9 percent) and Tanzania (+0.8 percent).

**Table 12: Rwanda Informal Cross Border trade (USD, million)**

	2016		2017				2018	
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Exports	30.73	24.99	22.46	24.28	25.17	26.50	31.38	31.80
% change (yoy)	28.3	-24.0	-27.1	-31.4	-18.1	6.1	39.7	31.0
Imports	8.22	7.52	4.45	5.87	6.46	5.82	4.91	6.36
% change(yoy)	43.3	65.8	-31.8	-28.9	-21.4	-22.7	10.4	8.3
Trade Balance	22.51	17.47	18.01	18.41	18.71	20.68	26.47	25.45
% change (yoy)	24.6	-36.4	-48.7	-32.1	-16.9	18.4	47.0	38.2

**Source:** BNR, Statistics Department

Informal cross border imports increased by 8.3 percent, from USD 5.9 million in 2017Q2, largely contributed by trade flows from Tanzania that grew by 6.3 percent, followed by Uganda (+6.1 percent) and Burundi (+2.3 percent) despite the decline by 6.4 percent from DRC. Uganda remains the leading ICBT trading partner with 60.5 percent of the total ICBT imports followed by Burundi (18.4 percent), DRC (13.0 percent) and Tanzania (8.1 percent). The growth of ICBT imports is mainly driven by high imports of clothing, cement, Irish potatoes seeds and modern drinks notably alcoholic and non-alcoholic drinks from Uganda and hashed rice from Tanzania.

#### 2.2.4 The exchange rate: bilateral and effective

In 2018Q2, the foreign exchange rate pressures on Franc Rwandais (FRW) remained modest, due to the continued improvements in external sector resulting from a significant increase in exports by 15.8 percent while imports grew by 1.4 percent.

Relative to December 2017, the FRW depreciated by 1.7 percent against the USD at end June 2018, slightly higher than 1.3 percent observed in the same period of 2017, but far below 4.8 percent recorded in 2016Q2. Compared to 2017Q2, FRW depreciated by 3.6 percent in 2018Q2 lower than 6.0 percent recorded in 2017Q2 while on quarterly basis, it depreciated by 0.9 percent and 0.8 percent in 2018Q2 and 2018Q1 respectively.

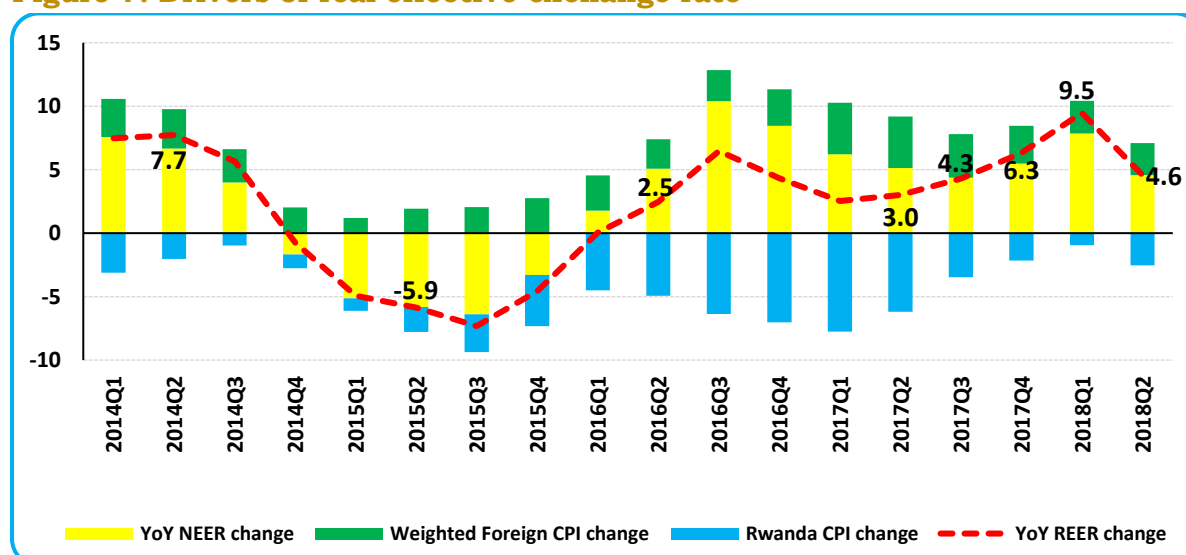
Compared to other major currencies, relative to December 2017, the FRW appreciated by 0.9 percent and 0.4 percent against the British pound and Euro respectively. Compared to regional currencies, the FRW depreciated by 4.0 percent and 1.5 percent against the Kenyan shillings and the Burundian Francs, respectively, but appreciated by 4.7 percent and 0.1 percent against the Ugandan and Tanzanian shillings.

**Table 13: Appreciation/Depreciation rate of selected currencies against the FRW**

	USD/FRW	GBP/FRW	EUR/FRW	KES/FRW	TZS/FRW	UGS/FRW	BIF/FRW
2016Q1	2.8	-0.2	6.3	3.9	1.4	2.8	1.5
2016Q2	4.8	-5.0	6.6	6.1	3.3	3.7	-3.7
2016Q3	8.4	-5.1	11.3	9.5	7.1	8.0	-0.5
2016Q4	9.7	-9.2	5.3	9.6	8.6	2.3	-0.2
2017Q1	0.8	2.5	2.5	0.3	-1.6	0.8	-0.3
<b>2017Q2</b>	<b>1.3</b>	<b>7.5</b>	<b>10.4</b>	<b>0.0</b>	<b>-1.4</b>	<b>2.0</b>	<b>-1.0</b>
2017Q3	2.2	11.8	14.7	1.5	-0.9	2.6	-1.4
2017Q4	3.1	13.2	16.9	2.3	0.4	2.7	-1.0
2018Q1	0.9	5.6	4.6	3.3	0.0	-0.6	0.8
<b>2018Q2</b>	<b>1.7</b>	<b>-0.9</b>	<b>-0.4</b>	<b>4.0</b>	<b>-0.1</b>	<b>-4.7</b>	<b>1.5</b>

**Source:** NBR, Monetary Policy Department

The FRW real effective exchange rate depreciated by 4.6 percent (y-o-y) in 2018Q2 against 3.0 percent recorded during the corresponding period in 2017. This was mostly attributed to the depreciation of the nominal value of the FRW against currencies of some of the major trading partners. In nominal effective terms, it also depreciated by 4.6 percent compared to a depreciation of 5.1 percent recorded in 2017Q2.

**Figure 7: Drivers of real effective exchange rate**

**Source:** NBR, Monetary Policy Department

## 2.3 Monetary Developments

### 2.3.1 Monetary Policy Stance

In 2018Q2, the NBR continued to implement an accommodative monetary policy stance to continue supporting the financing of the economy by the banking sector, since both inflationary and exchange pressures remained subdued. The NBR

decreased its policy rate from 6.25 percent in December 2016 to 6 percent in June 2017 and 5.5 percent in December 2017 while keeping it unchanged in June 2018. As a result, outstanding credit to the private sector increased by 7.3 percent in 2018Q2 compared to 8.0 percent in 2017Q2. The broad money increased by 9.6 percent in 2018Q2 compared to 12.7 percent in the same period of 2017.

## 2.3.2 Money Supply and Demand

### 2.3.2.1 Money Supply

The 9.6% expansion in broad money was driven by the increase in net domestic assets by 9.7 percent in 2018Q2 from 3.5% in 2017Q2, although the net foreign assets (NFA) grew by 9.4 percent less than 29.0% during the same period. The increase in net domestic assets mainly resulted from surge in credit to public sector (especially loans to RWANDAIR) which expanded by 94.8 percent in 2018Q2 from 10.1% in 2017Q2, while credit to the private sector increased by 7.3% slightly less than 8.0%, during the same period. The contraction in NFA growth was caused by a reduction in commercial banks' NFA by 31.1 percent in 2018Q2, as result of external loan repayment by some banks and transfers to some large local companies.

**Table14: Monetary aggregates (FRW, billion)**

	2016 Q2	2017 Q2	2018 Q2	% change	
				2017Q2/ 2016Q2	2018Q2/ 2017Q2
<b>Net foreign assets</b>	<b>567.5</b>	<b>731.9</b>	<b>800.8</b>	<b>29.0</b>	<b>9.4</b>
Foreign assets	890.1	1101.8	1226.3	23.8	11.3
Foreign liabilities	322.5	369.9	425.5	14.7	15.0
<b>Net domestic assets</b>	<b>1004.9</b>	<b>1040.3</b>	<b>1141.2</b>	<b>3.5</b>	<b>9.7</b>
Domestic credit	1451.7	1575.9	1767.3	8.6	12.1
Central government (net)	124.4	141.7	190.5	13.9	34.5
Credit	318.3	344.4	441.6	8.2	28.2
Deposits	193.9	202.7	251.0	4.6	23.8
Public enterprises	39.9	43.9	85.4	10.1	94.8
<i>O/W in foreign currency</i>	<i>17.6</i>	<i>22.7</i>	<i>36.3</i>	<i>29.0</i>	<i>60.0</i>
Private sector	1287.4	1390.3	1491.3	8.0	7.3
<i>O/W in foreign currency</i>	<i>178.9</i>	<i>193.3</i>	<i>199.5</i>	<i>8.0</i>	<i>3.2</i>
Other items net (Assets: +, Liab: -)	-446.8	-535.6	-626.1	-19.9	-16.9
<b>Broad money M3</b>	<b>1572.4</b>	<b>1772.2</b>	<b>1942.0</b>	<b>12.7</b>	<b>9.6</b>
Currency in circulation	150.8	159.7	181.6	5.9	13.7
Deposits	1421.6	1612.5	1760.4	13.4	9.2
of which: Demand deposits	640.0	680.2	699.8	6.3	2.9
Time and savings deposits	512.4	542.3	615.4	5.8	13.3
Foreign currency deposits	269.2	390.0	446.2	44.9	14.4

**Source:** BNR, Monetary Policy Department

New authorized loans by the banking sector increased by 0.9 percent in 2018Q2, standing at FRW 204.8 billion from a decline of 10.7 percent recorded in 2017Q2, following the good performance of economic activities. The growth in new authorized loans in 2018Q2 was largely reflected in Non-classified activities mainly composed by personal loans (+23.7 percent), manufacturing activities (+11.6 percent) and agriculture fisheries and livestock (+52.6 percent).

**Table 15: New authorized loans by sector (FRW billion, unless otherwise indicated)**

Branch of activity	2016 Q2	2017				2018		% change	
		Q1	Q2	Q3	Q4	Q1	Q2	2017Q2/ 2016Q2	2018Q2/ 2017Q2
Non-classified activities	18.8	23.4	21.1	22.1	24.0	25.2	26.2	12.5%	23.7%
Agriculture, fisheries& livestock	2.8	2.9	2.0	2.2	1.7	2.6	3.1	-28.7%	52.6%
Mining activities	1.0	0.4	0.3	0.0	0.2	0.0	0.2	-75.4%	-5.5%
Manufacturing activities	22.5	8.0	20.4	13.4	18.4	10.3	22.8	-9.2%	11.6%
Water & energy activities	0.2	8.0	0.9	4.9	6.5	0.2	0.0	269.5%	-98.8%
Public works and buildings	54.1	55.2	50.0	61.5	64.1	51.0	50.8	-7.5%	1.6%
Commerce restaurants and hotels	112.2	84.7	84.6	69.9	71.7	65.1	80.2	-24.6%	-5.2%
Transport & warehousing & communication	10.1	19.7	18.5	12.7	22.7	33.0	15.4	84.1%	-16.8%
OFI & Insurances and other non-financial services	0.5	5.4	1.1	2.2	0.8	0.4	0.6	107.5%	-43.4%
Services provided to the community	5.1	6.1	4.1	3.5	5.8	10.1	4.6	-19.2%	12.5%
<b>Total</b>	<b>227.2</b>	<b>213.7</b>	<b>202.9</b>	<b>192.5</b>	<b>215.7</b>	<b>197.9</b>	<b>204.8</b>	<b>-10.7%</b>	<b>0.9%</b>

**Source:** BNR, Financial Stability Directorate

Considering the distribution of new authorized loans by sector of activities, commerce, restaurants and hotels remained the most financed economic sector, representing 39.2 percent of the total new authorized loans, followed by public works and buildings (24.8 percent).

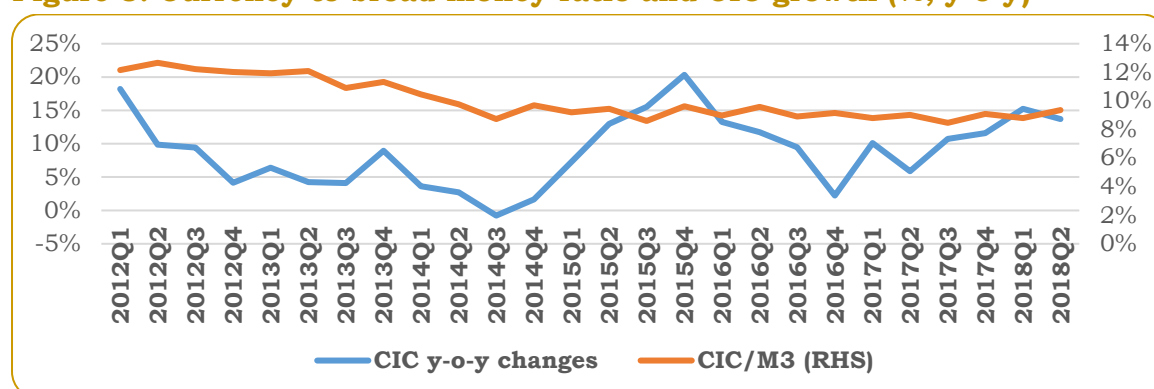
**Table 16: Distribution of new authorized loans by sector of activities (% share of total new loans)**

Branch of activity	2016 Q2	2017				2018	
		Q1	Q2	Q3	Q4	Q1	Q2
Non-classified activities	8.3	11.0	10.4	11.5	11.1	12.7	12.8
Agricultural, fisheries& livestock	1.2	1.4	1.0	1.2	0.8	1.3	1.5
Mining activities	0.5	0.2	0.1	0.0	0.1	0.0	0.1
Manufacturing activities	9.9	3.8	10.1	7.0	8.5	5.2	11.1
Water & energy activities	0.1	3.7	0.4	2.6	3.0	0.1	0.0
<b>Public works and buildings</b>	<b>23.8</b>	<b>25.8</b>	<b>24.6</b>	<b>31.9</b>	<b>29.7</b>	<b>25.8</b>	<b>24.8</b>
<b>Commerce restaurants and hotels</b>	<b>49.4</b>	<b>39.6</b>	<b>41.7</b>	<b>36.3</b>	<b>33.2</b>	<b>32.9</b>	<b>39.2</b>
Transport & warehousing & communication	4.4	9.2	9.1	6.6	10.5	16.7	7.5
OFI & Insurances and other non-financial services	0.2	2.5	0.5	1.2	0.3	0.2	0.3
Services provided to the community	2.2	2.8	2.0	1.8	2.7	5.1	2.2
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

**Source:** BNR, Financial Stability Directorate

### 2.3.2.2 Money demand

Currency in circulation (CIC) picked up by 13.7 percent, in 2018Q2, from 5.9 percent in 2017Q2. That upturn in CIC was explained by an improvement in economic activities. In addition, the monetization of economy continued to improve as the ratio of broad money to GDP increased to 23.4 percent in 2017 from 15.4 percent in 2013. The currency in circulation to broad money ratio remains low, standing at 9 percent in 2018Q2, below an average of 10 percent in the last 5 years. This downward trend in the ratio of CIC to broad money continues to be mainly caused by the improvement in financial inclusion and payment systems modernization.

**Figure 8: Currency to broad money ratio and CIC growth (% , y-o-y)**

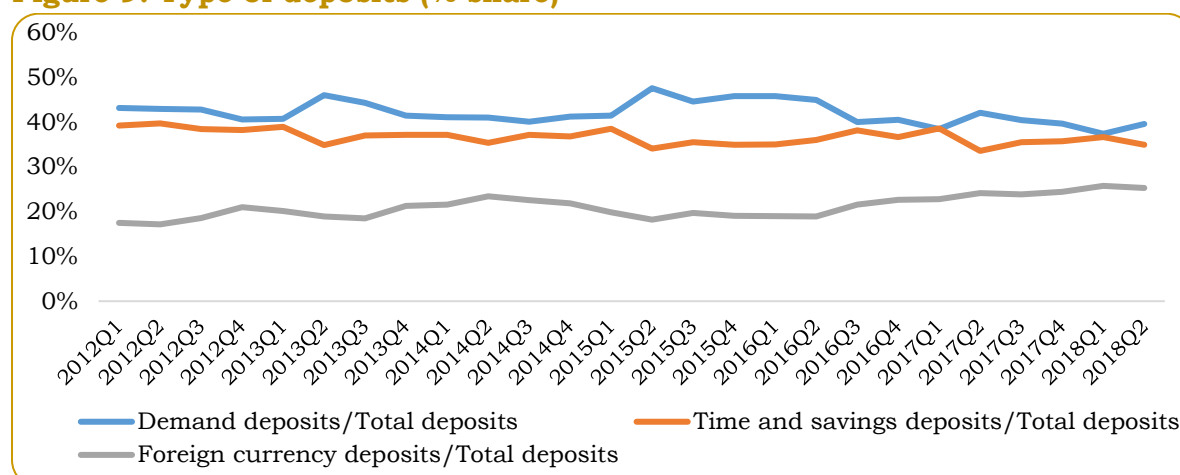
**Source:** BNR, Statistics Department

Total deposits rose by 9.2 percent y-o-y in 2018Q2, versus 13.4 percent in 2017Q2. Demand, time and foreign currency deposits increased by 2.9 percent, 13.3 percent and 14.4 percent in 2018Q2 respectively, against 6.3 percent, 5.8 percent and 44.9 percent in the same period of last year. The increase in time and savings deposits can be partially attributed to the removal of the 15 percent withholding tax on the category of deposits for the maturity of 1 year and above. The share of demand



deposits in total deposits remains high but with a downturn trend, amounting to 40 percent in 2018Q2, lower than 42 percent in the last five years. Time and saving deposits follows with 37 percent from 36 percent, and foreign currency deposits with 26 percent, compared to 21 percent in the last five years.

**Figure 9: Type of deposits (% share)**



**Source:** BNR, Statistics Department

With regard to the deposits by category of depositors, Households and non- profit Institutions Serving Households (NPISHs) continued to have the biggest share, with 44.9 percent end 2018Q2 followed by other non-financial corporations (26.7 percent), social security funds (16.9 percent), other financial institutions (8.5 percent) and public enterprises (3.0 percent).

**Table 17: Deposits by category of depositors (% share)**

	2015	2016				2017				2018	
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Other financial institutions	9.3	8.3	8.4	7.4	7	8	8.6	7.8	7.6	9.0	8.5
Social Security Funds	15.8	16.3	14.9	15.7	15	16.1	15.3	19.1	17.3	17.9	16.9
Public enterprises	4.2	5.0	4.2	3.6	3.8	3.9	3.7	3.0	2.9	3.2	3.0
Other non-financial corporations	25.9	25.9	26.0	25.0	26.4	25.5	27.8	25.0	26.6	25.8	26.7
Households and NPISH	44.9	44.5	46.6	48.2	47.8	46.5	44.7	45.0	45.6	44.1	44.9
Total	100	100	100	100	100	100	100	100	100	100	100

**Source:** BNR, Statistics Department

### 2.3.3 Banking system liquidity developments

The banking system liquidity conditions continued to ease during 2018Q2 compared to the same quarter of the previous year. Commercial banks' most liquid assets expanded by 22.8 percent standing at FRW 379.7 billion in 2018Q2 from FRW 309.1

billion recorded in 2017Q2. Comparatively to their levels in the previous quarter, they decelerated by 3.8 percent.

**Table18: Most liquid assets of commercial banks (FRW, billion)**

	2016			2017				2018		% change	
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q2-18/ Q2-17	Q2-18/ Q1-18
<b>T-bills</b>	214.0	176.3	173.7	187.3	207.9	245.0	243.6	253.5	249.5	20.0	-1.6
<b>Central bank bill</b>	-	4.0	4.0	5.0	-	9.0	6.0	37.0	18.5	-	-50.0
<b>Repo</b>	34.0	0.0	30.5	21.0	60.4	13.0	30.0	54.7	45.0	-25.5	-17.7
<b>Excess reserves</b>	31.7	20.5	24.5	14.8	9.9	15.2	20.6	17.2	36.8	271.7	114.0
<b>Cash in vault</b>	32.0	28.3	30.8	31.4	30.9	28.4	33.1	32.1	29.9	-3.2	-6.9
<b>Total</b>	<b>311.7</b>	<b>229.2</b>	<b>263.6</b>	<b>259.5</b>	<b>309.1</b>	<b>310.6</b>	<b>333.3</b>	<b>394.5</b>	<b>379.7</b>	<b>22.8</b>	<b>-3.8</b>

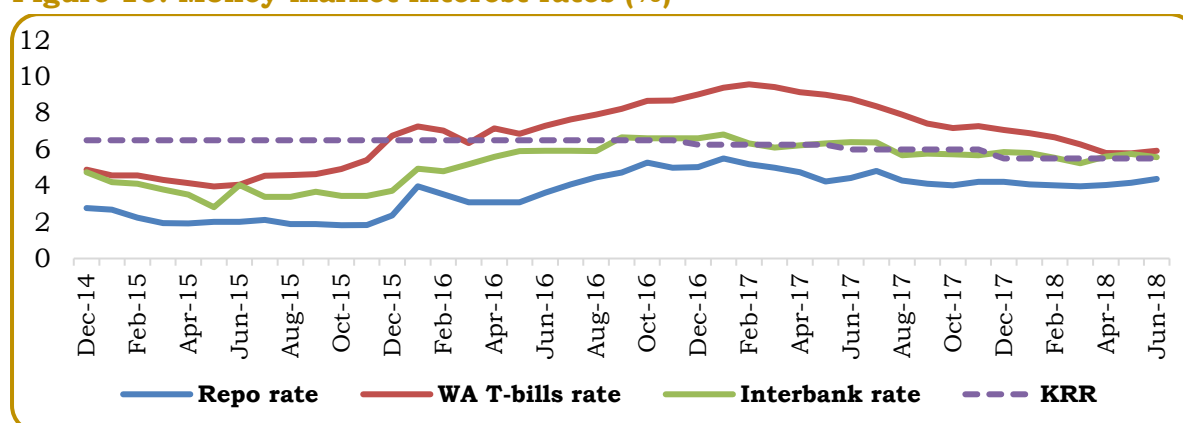
**Source:** BNR, Monetary Policy Department

The liquidity conditions during the quarter under review, were mainly improved by less sales to banks that lessened to USD 45.7 million in 2018Q2 from USD 68.6 million sold in 2017Q2. There was also a moderate growth in new loans as they grew by 0.9 percent in 2018Q2. In addition, there was liquidity injection through swaps of USD 4.8 million in 2018Q2.

### 2.3.4 Interest rates developments

In line with favorable liquidity conditions and cut in the key repo rate, money market interest rates have been trending downward. Repo, T-bills and interbank rate respectively decreased on average to 4.19 percent, 5.83 percent and 5.64 percent in 2018Q2 from 4.47 percent, 8.97 percent and 6.32 percent in 2017Q2.

**Figure 10: Money market interest rates (%)**



**Source:** BNR, Monetary Policy Department

With regard to commercial banks interest rates, lending rates declined by 10 basis points to stand on average at 17.01 percent in 2018Q2 from 17.11 percent in 2017Q2. Deposit rate increased by 7 basis points standing at 8.18 percent on average from 8.11 percent during the same period. This reduced the interest spread to 8.83 percent in 2018Q2 from 9.00 percent in 2017Q2, which showed some competition among commercial banks.

**Table 19: Market interest rates (percent, average)**

	2013	2014	2015	2016	2017	2017				2018	
						Q1	Q2	Q3	Q4	Q1	Q2
Lending	17.32	17.26	17.33	17.29	17.17	17.03	17.11	17.41	17.21	17.03	17.01
Deposit	9.93	8.24	8.24	7.91	7.63	7.48	8.11	7.73	7.19	7.44	8.18
Spread	7.39	9.02	9.09	9.38	9.54	9.55	9.00	9.68	10.02	9.59	8.83

**Source:** BNR, Monetary Policy Department

### III. INFLATION DEVELOPMENTS

Despite recent upturn from 0.9 percent in 2018Q1 to 2.5 percent in 2018Q2, headline inflation broadly remains low and stable compared with the medium target of 5 percent. The developments in headline inflation were mainly reflected in food and energy prices as well as in transport costs. Core inflation remained benign, slightly increasing from 1.7 percent to 1.8 percent during the same period and this was consistent with the prevailing level of aggregate demand and subdued exchange rate pressures.

**Table 20: Inflation developments for key items (% , Y-o-Y)**

	2017				2018	
	Q1	Q2	Q3	Q4	Q1	Q2
<b>Headline</b>	7.7	6.2	3.5	2.2	0.9	2.5
<b>Domestic</b>	7.4	6.0	3.4	1.4	-0.1	1.8
<b>Food:</b>	16.6	13.3	7.4	1.9	-1.8	0.6
- Vegetables	21.0	13.3	4.6	-0.5	-5.4	2.3
<b>Housing</b>	2.0	1.8	1.7	2.3	2.4	4.4
<b>Transport</b>	8.5	5.4	1.2	3.0	3.0	8.2
<b>Imported</b>	8.8	6.9	3.9	4.7	4.4	5.0
<b>Core</b>	5.5	4.6	3.1	2.5	1.7	1.8
<b>Energy</b>	4.3	5.2	3.5	6.3	7.3	12.7

**Source:** NBR, Research Department (2018)

Food prices increased by 0.6 percent in 2018Q2, from -1.8 percent in 2018Q1, resulting from the vegetables inflation that picked up to 2.3 percent in 2018Q2 from -5.4 percent in 2018Q1. The increase in vegetables prices come from the reduction in the quantity supplied on the market due to the heavy rains that destroyed some crops in April and May 2018.

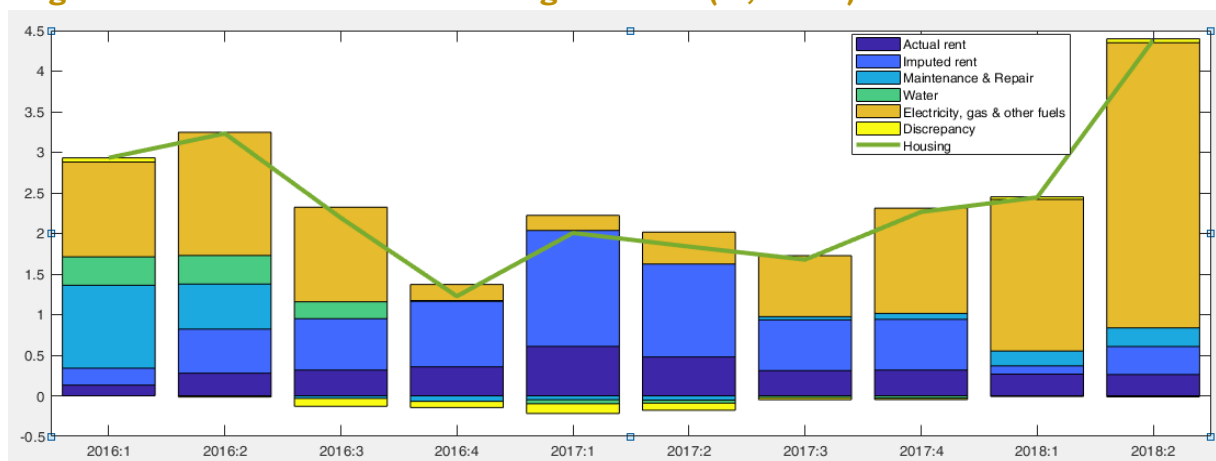
**Figure 11: Contribution to Food Inflation (% , Y-o-Y)**



**Source:** NBR, Research Department (2018)

Housing inflation increased from 2.4 percent in 2018Q1 to 4.4 percent in 2018Q2. The increase resulted from the changes in solid fuels prices (charcoals and firewood) which is one of the components of housing inflation. Solid fuels prices increased by 20.9 percent in 2018Q2, higher than 10.3 percent in 2018Q1, due to the heavy rains that reduced the production and transport of those solid fuels.

**Figure 12: Contribution to Housing Inflation (% , Y-o-Y)**



**Source:** NBR, Research Department (2018)

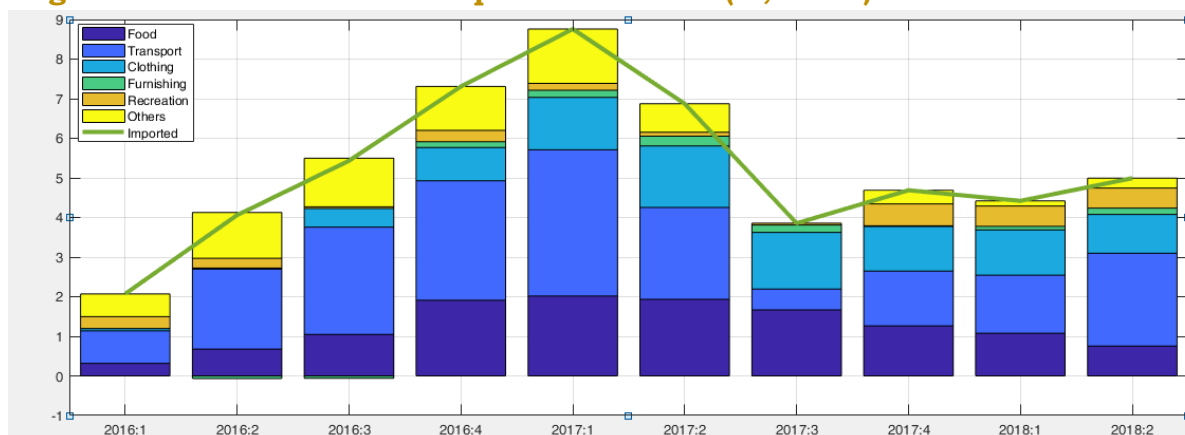
Transport inflation increased to 8.2 percent in 2018Q2 from 3.0 percent in 2018Q1, following notably higher transport services inflation (7.8 percent in 2018Q2 from 0.3 percent in 2018Q1) and the appreciation of the Yen against the USD that put some pressures on imported cars from Japan.

**Figure 13: Contribution to Transport Inflation (% , Y-o-Y)**



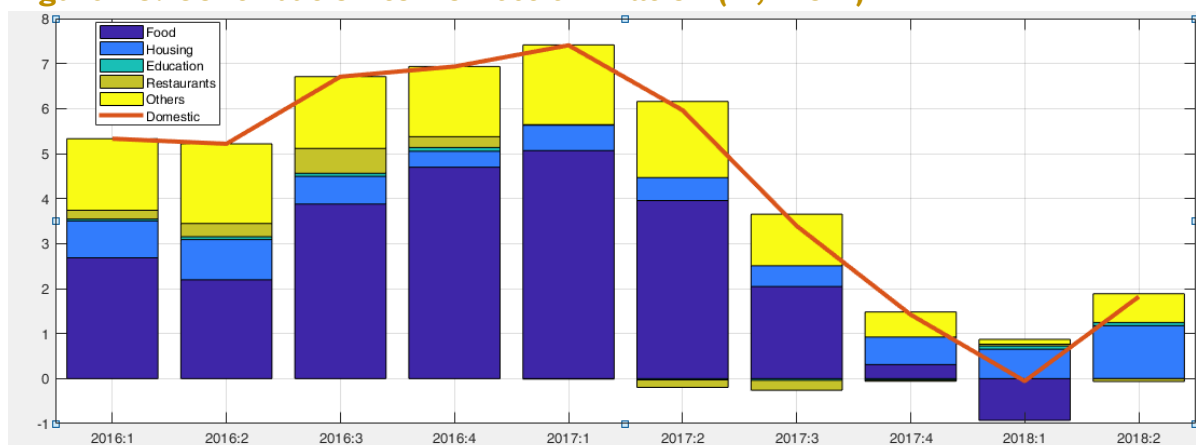
**Source:** NBR, Research Department (2018)

Imported inflation increased to 5 percent in 2018Q2 from 4.4 percent in 2018Q1, following an upturn in imported transport inflation, that increased to 9 percent in 2018Q2, from 6 percent in 2018Q1.

**Figure 14: Contribution to Imported Inflation (% , Y-o-Y)**

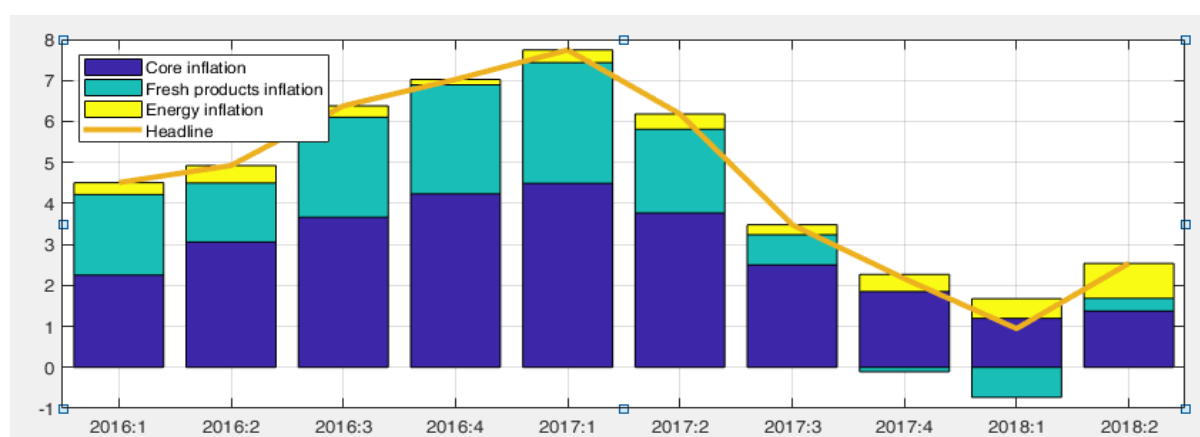
**Source:** NBR, Research Department (2018)

Domestic inflation picked up from -0.1 percent in 2018Q1 to 1.8 percent in 2018Q2 following the increase in housing inflation from 2.4 percent in 2018Q1 to 4.4 percent in 2018Q2.

**Figure 15: Contribution to Domestic Inflation (% , Y-o-Y)**

**Source:** NBR, Research Department (2018)

Consistent with the prevailing level of aggregate demand and subdued exchange rate pressures, core inflation marginally increased from 1.7 percent in 2018Q1 to 1.8 percent in 2018Q2. Energy inflation has increased from 7.3 percent in 2018Q1 to 12.7 percent in 2018Q2, due to the aforementioned heavy rains that reduced the production and transport of solid fuels (charcoal and firewood).

**Figure 16: Core, Energy and Fresh Products Inflation (% , Y-o-Y)**

**Source:** NBR, Research Department (2018)



## IV. INFLATION OUTLOOK AND RISKS

### 4.1 Demand-side pressures

Though aggregate demand has progressively been improving in line with the good performance of the economy since 2017Q2, it remains broadly non-inflationary. This trend is expected to continue in the medium-term. Other high frequency indicators, such as growth in monetary aggregates, confirm the observed trend in aggregate demand.

### 4.2 Supply shocks

Since March 2018, favorable climate conditions during the agricultural season B led to an increase in food production and hence a decline in prices. Climate conditions are likely to remain good during agricultural season C 2018. Therefore, food prices are expected to remain low until 2018Q3.

### 4.3 Exchange rate developments

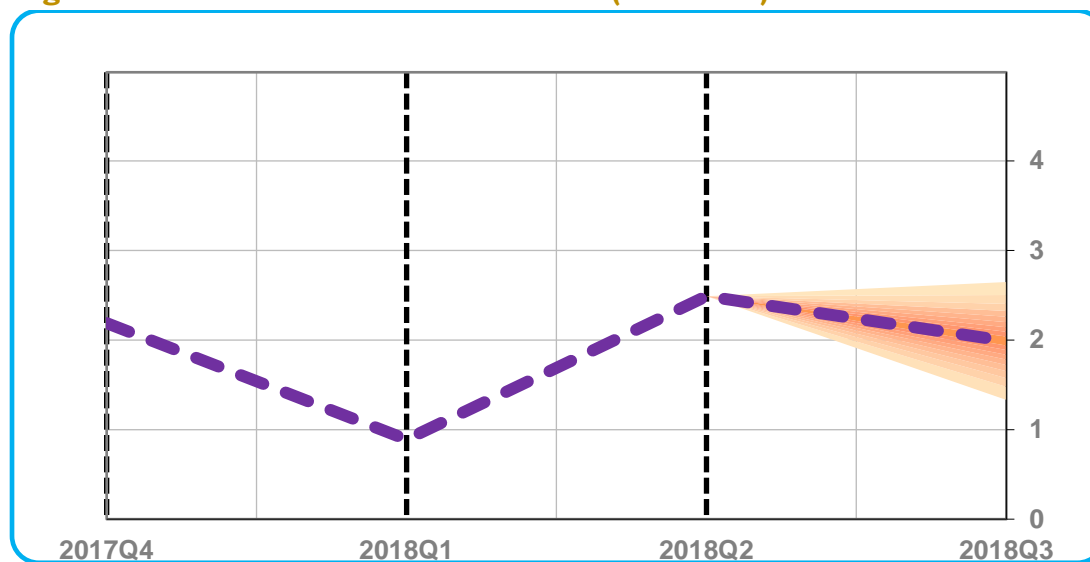
Exchange rate pressures on Franc Rwandais (FRW) remained modest, due to ongoing improvements in external sector, amid significant increase in exports. Exchange rate pressures are expected to remain moderate, thus posing no significant pressures on imported inflation going forward.

### 4.4 Global and regional inflationary pressures

The global economy remains strong and expected to further pick up over the next two years. Most advanced economies are performing above their potential, indicating a continued stronger aggregate demand in the near future. The resilience of the global economy is expected to continue, stimulating not only Rwanda's export receipts but also easing exchange rate pressures. However, oil prices are expected to continue rising, putting pressures on local pump prices and leading to an increase in the import bill. The latter is likely to be partially offset by the anticipated increase in export revenues especially resulting from an increase in prices of minerals. Furthermore, pressures on imported inflation will be mitigated by the reduction in the Common External Tariff (CET), mainly for sugar and rice.

### 4.5 Inflation forecasts

Agricultural production in season C is expected to push down vegetables prices and this is expected to continue towards the end of September 2018. Oil prices are expected to continue rising, putting pressures on local pump prices and leading to an increase in the import bill. The latter is likely to be partially offset by the anticipated increase in export revenues especially resulting from an increase in prices of metals and minerals. In view of the abovementioned downward and upward risks, headline inflation is projected to lie between 1.5% and 2.5% for 2018Q3.

**Figure 18: Headline inflation forecasts (fan chart)**

**Source:** BNR, Monetary Policy & Research Department