BANK OF MAURITIUS

Website: http://bom.intnet.mu

PRESS COMMUNIQUE

Financial Stability Report – Seventh Issue

The Bank is releasing today the seventh issue of its Financial Stability Report. The Report focuses on global and domestic financial stability issues in the first semester of 2011.

The global economy continued to recover albeit at a slower-than-expected pace during the first half of 2011. Uncertainties over the growth outlook have increased as a result of the geopolitical disturbances in the Middle East and North Africa, disasters in Japan and growing concerns over the fiscal situation in advanced economies. Despite the negative developments, financial markets have not been excessively volatile although some parts of the financial markets have to a large extent reflected the increasing doubts about fiscal sustainability in the euro area and the US.

In Mauritius, according to the Central Statistics Office, the economy grew by 4.3 per cent in 2010 and is expected to expand at 4.5 per cent in 2011, driven by real estate, renting and business activities, manufacturing and financial intermediation. The economy remains vulnerable to a number of risks arising from external developments and, in particular, the inability of advanced economies to improve the pace of economic recovery. The extent to which the advanced economies surmount their economic and fiscal problems will be key to the domestic growth outlook.

The overall balance of payments for the first quarter of 2011 posted a surplus of Rs1,797 million as against a deficit of Rs315 million in the corresponding period of 2010. The current account deficit, which is estimated at around 4.5 per cent of GDP in the first quarter of 2011, is not considered as posing a risk to financial stability. However, the evolution of net FDI inflows in subsequent quarters warrants closer monitoring.

The level of gross official international reserves as at end-June 2011 represented more than 7 months of import cover and provided a comfortable cushion to absorb external shocks.

Public sector debt, which fell to 55.9 per cent of GDP as at end-June 2011, is projected to reach 60.3 per cent as at end-December 2011 and 61.1 per cent as at end-December 2012 before coming down to 59.0 per cent at end-December 2013. The debt-service ratio of the country is forecast to hover in the range of 2.8- 3.0 per cent between 2011 and 2013.

Households remained among the largest borrower groups in the banking sector, with household funding mainly channelled to asset-building rather than consumption. As at end-March 2011, household debt reached 18.3 per cent of GDP, up from 16.8 per cent as at end-March 2010. While this may not necessarily point to increased vulnerability, the household sector may warrant closer monitoring, particularly with regard to debt repayment capacity.

On the domestic financial market, the Bank tightened monetary policy in the first half of 2011 through two Key Repo Rate hikes totalling 75 basis points. Due to large excess liquidity in the banking system, interbank market rates trended downwards during the first few months of 2011 before moving back up following an increase in the cash reserve ratio and the Bank's issuance of its own securities on the domestic money market. These interventions helped to contain banks' excess reserves, which were even negative towards end-May 2011.

The rupee exchange rate continued to reflect movements of major currencies on the international markets as well as domestic supply and demand conditions. The Bank intervened on the domestic foreign exchange market on several occasions to purchase and to sell foreign currencies.

The domestic banking sector witnessed the entry of a full-fledged Islamic bank in March 2011, which brought the total number of banks in operation to 20. The banking sector remained profitable and financial stability indicators were found to be at reasonable levels. The capital adequacy ratio hovered well above the minimum of 10 per cent and the non-performing loans ratio for the sector was relatively low. Due to their strong capital position, many banks in Mauritius appeared well-positioned to meet the more demanding Basel III capital standards. The Herfindahl-Hirschmann Index (HHI), a measure of concentration of the banking sector, continued to be in the 'moderate concentration' band as at end-June 2011.

The insurance sector registered a deceleration in asset growth in 2010 compared to the previous year, with a deceleration recorded in both the long-term insurance business segment and the general insurance business segment. Concentration in the long-term insurance segment remained high with the three largest firms accounting for 84.7 per cent of total assets while the general insurance business segment was found to be moderately concentrated.

Non-Bank Deposit Taking Institutions were profitable in 2010 despite registering a deceleration in activity compared to 2009. Indicators of profitability, namely return on assets and return on equity, improved compared to the previous year.

The payment system infrastructure in Mauritius appears robust enough to cater for the operations of the banking sector. As the regulatory authority, the Bank ensures that the system keeps up with latest technological advances so that there is no major disruption to banking operations.

The Financial Stability Report is available on the Bank's website at *http://bom.intnet.mu*.

Bank of Mauritius
30 August 2011