OVERVIEW

International Developments

During August 2003, the US dollar, on average, appreciated vis-à-vis the main currencies following the release of a series of favourable economic data indicating that the US economy was poised for an economic pick-up. The preliminary GDP report, released early August, showing US economic growth at a stronger-than-expected 2.4 per cent, which was later revised upward to 3.1 per cent, followed through by consistently positive data releases on manufacturing activity, factory orders, industrial output, retail sales, and productivity as well as upbeat consumer and business sentiment kept the US currency well supported throughout the month. Even the current account deficit, which has been a lingering concern, showed signs of improving with the US trade deficit shrinking to $39.55 billion in June 2003 from a revised $41.48 billion in May 2003, after exports posted their highest level since June 2001 and imports remaining flat. Meanwhile, deflationary risks to the US economy seemed to have receded with core consumer price data rising by 0.2 per cent in July 2003 after remaining unchanged in June 2003. This bright picture was, however, dulled by the employment report pointing to a jobless recovery. On 12 August 2003, the Federal Open Market Committee unanimously decided to keep the Federal funds rate steady at 1.00 per cent indicating that it intended to keep interest rates low for an extended period. In its accompanying policy statement, the FOMC reiterated that the upside and downside risks to economic growth remained balanced and also noted that the labour market continued to display mixed signals while prices remained subdued.

In contrast to the US economy, euro zone data released in August 2003 were quite disappointing. The economic sentiment index for the euro zone, which had been stable from April to June 2003, slipped in July, while quarter-on-quarter growth data pointed to a stagnating euro zone economy in the second quarter of 2003, with an economic contraction noted in the three biggest economies of the euro zone namely, Germany at –0.1 per cent, a contraction mainly attributed to a decline in exports, France at –0.3 per cent, and Italy at –0.1 per cent. Trade data released towards mid-August underscored the fall in exports in the euro zone with the trade balance of the euro area posting a surplus of 5.4 billion euros in June, about half the size of the surplus it recorded a year earlier. Reflecting the lacklustre performance of the euro zone, the euro, which was relatively well supported against the US dollar since the beginning of the month, lost ground steadily from 14 August onwards to reach US$1.0842 on 27 August, its lowest level since 16 April 2003. Towards the end of August, however, with the market hopeful of a rebound in the euro zone after German ifo business climate index had risen for the fourth straight month in August, the euro recovered slightly to finish the month at US$1.0875.

In the United Kingdom, data releases in August 2003 broadly indicated that the economy was recovering from the global downturn with the manufacturing sector returning to growth in July for the first time in nine months, while the construction industry expanded at its fastest pace since November 2002. On 7 August 2003, the Bank of England Monetary Policy Committee concluded its two-day meeting by leaving its key repo rate unchanged at 3.50 per cent, as widely expected, in the face of record consumer debt and signs that the economy was picking up. The minutes of the Bank of England's MPC meeting released later in the month showed that MPC members decided unanimously to leave rates steady in August 2003 and acknowledged that retail spending and the housing market had been surprisingly strong. Stronger-than-expected services and industrial production data out later in the month together with upbeat UK jobs market data as well as better-than-expected British public finances reinforced the views that the UK economy had turned around. However, July 2003 producer prices in the UK came in stronger-than-expected and there was a surprise upturn in UK inflation with the RPIX rising to 2.9 per cent in July 2003 from 2.8 per cent in June 2003, while the harmonized index of consumer prices (HICP), which is set to supplant the RPIX as the Bank of England's primary inflation measure later this year, in November 2003, climbed to 1.3 per cent from 1.1 per cent. Throughout that period, the Pound remained well bid around USD1.59-US$1.61 but mixed signals with falling retail sales and business investment and a second quarter GDP data, which showed the UK economy growing by a meagre 0.3 per cent quarter-on-quarter, brought the Pound down in the final weeks of August 2003 to close the month at US$1.5772.

Prospects of continued, though gradual, recovery were supportive of the yen throughout August 2003. Sizeable repatriation by Japanese investors and foreign capital inflows lifted Tokyo stocks and the Japanese currency. The latter, which at the start of August, was trading at slightly above 120 yen against the US dollar appreciated steadily throughout the month to trade at 117.02 yen against the US currency on 29 August 2003. Data released during August 2003 showed that the Japanese economy grew at a higher-than-expected rate of 0.6 per cent from the previous quarter and by an annualised 2.3 per cent, while first quarter GDP was revised upwardly to 0.3 per cent from the previously reported 0.1 per cent. In addition, manufacturing activity expanded at its fastest pace in a year in July, while core machinery orders rose by 2.4 per cent in June against expectations of a fall. However, with the GDP deflator at -2.1 per cent, deflation remained a big problem in Japan. On 8 August 2003, the Bank of Japan concluded its two-day Policy Board Meeting and, as expected, left interest rates unchanged. The yen's gains were limited by the market's wariness over intervention by the Japanese authorities after the Ministry of Finance later revealed that it spent 4.6116 trillion yen on intervention, during April-June 2003. Signs that the Japanese economy was recovering were more apparent towards the end of the month, with the release of the June 2003 all-industries activity index, which rose by a higher-than-expected 0.9 per cent, and the July 2003 trade data showing both exports and imports rising stronger than consensus forecasts.

Domestic Developments

Tourist arrivals increased by 3.0 per cent from 56,709 in July 2002 to 58,403 in July 2003, while gross tourism receipts went up by 5.2 per cent, from Rs1,332 million in July 2002 to Rs1,401 million in July 2003. Cumulatively for the period January to July 2003, gross tourism receipts fell by 2.5 per cent to Rs10,357 million from Rs10,620 million for the corresponding period in 2002.

The Consumer Price Index (CPI) declined from 107.5 in July 2003 to 107.4 in August 2003. The rate of inflation for the 12-month period ended August 2003 stood at 4.8 per cent.

Money supply M2 dropped by Rs61 million, from Rs123,405 million at the end of June 2003 to Rs123,344 million at the end of July 2003. Narrow money supply M1, one of the components of M2, fell by Rs436 million or 2.5 per cent to Rs17,003 million, but that fall was partly offset by the rise of Rs375 million or 0.4 per cent in quasi-money, which stood at Rs106,341 million.

Net foreign assets of the banking system were virtually unchanged at Rs47,566 million at the end of July 2003. Net foreign assets of the Bank of Mauritius rose by Rs534 million or 1.3 per cent to Rs40,117 million while net foreign assets of Category 1 banks fell by Rs536 million or 6.7 per cent to Rs7,449 million.

Domestic credit rose by Rs313 million or 0.3 per cent, from Rs106,927 million at the end of June 2003 to Rs107,240 million at the end of July 2003. Net credit to Government by the banking system went down by Rs279 million or 1.3 per cent to Rs21,197 million, reflecting the decrease of Rs793 million or 7.2 per cent in net credit to Government from Bank of

Mauritius that was partly offset by the increase of Rs513 million in net credit to Government from Category 1 banks .

Credit to the private sector from Category 1 banks rose by Rs596 million or 0.7 per cent, from Rs85,080 million at the end of June 2003 to Rs85,676 million at the end of July 2003. Credit was mainly channelled to "Traders" (Rs255 million), "Personal & Professional" (Rs249 million), "Agriculture & Fishing" (Rs218 million) and "Construction" (Rs192 million). There was a drop in credit to "Financial & Business Services" (Rs186 million), "Manufacturing" (Rs122 million) and "Statutory & Parastatal Bodies" (Rs87 million).

Reserve money declined by Rs400 million or 2.7 per cent, from Rs14,776 million at the end of June 2003 to Rs14,376 million at the end of July 2003.

As from Friday 22 August 2003 the Bank of Mauritius has been issuing Government of Mauritius Treasury Bills (GMTB) as well as Bank of Mauritius Bills (BOM Bills) in the primary auctions. GMTB are issued to meet the borrowing requirements of the Government while BOM Bills are issued for monetary policy purposes. Both GMTB and BOM Bills are eligible for trading under conditions prevailing for GMTB.

The Bank did not carry out any repurchase/reverse repurchase transaction during August 2003.

Total transactions in eligible Government securities effected through the primary dealers during August 2003 amounted to Rs921.4 million.

Direct sales of foreign currencies by the Mauritius Sugar Syndicate to the banking sector during August 2003 amounted to an equivalent of US$14.45 million. The comfortable liquidity situation in the domestic foreign exchange market continued to prevail. The Bank intervened and purchased a total of US$9.40 million in August 2003. Between July 2003 and August 2003, the rupee, on average, appreciated vis-à-vis the euro, the Pound Sterling, the US dollar and the Japanese yen.

At the end of July 2003, the net international reserves of the country amounted to Rs48,152 million. Based on the value of the import bill for calendar year 2002, the end-July 2003 level of net international reserves of the country represented 41.9 weeks of imports, same as at the end of June 2003. It should be noted that following the revision of the Bank of Mauritius net foreign assets figure for June 2003, the net international reserves figure was revised from

Rs48,200 million to Rs48,151 million. At the end of August 2003, the foreign exchange reserves of the Bank of Mauritius amounted to Rs39,770 million, down from Rs40,117 million at the end of July 2003.