OVERVIEW

International Developments

During August 2004, the US dollar, on average, appreciated against all major currencies. The US dollar remained somewhat vulnerable during the first three weeks of August, marked by the release of conflicting US data, which raised doubts about the sustainability of the US economic recovery. The greatest concerns seemed to be centered on the apparent lack of job growth, the ability of consumers to keep spending in the wake of rising interest rates and higher energy prices. US non-farm payrolls added only 32,000 jobs in July 2004, far weaker than the 228,000 new jobs expected, and US personal consumption also fell much sharply-than-expected by 0.7 per cent in June 2004, its biggest drop since September 2001. The US Federal Reserve, however, appeared to be far less concerned about the "soft patch" that the economy hit in recent weeks, considering that it was only transitory due to the substantial rise in energy prices. At its regular FOMC meeting on 10 August 2004, the US Federal Reserve raised the federal funds rate by another 25 basis points to 1.50 per cent. However, by the last week of August 2004, the US dollar gained ground across the board, supported by a retreat in oil prices and upbeat comments from Federal Reserve officials stating that while the US recovery was facing some challenges, the economic expansion remained intact, thereby keeping alive market expectations for a continued "measured" monetary tightening by the US Federal Reserve.

The euro, which opened August 2004 trading around US$1.2058, drew support from position adjustments and the underlying weakness of the US dollar to move to its intra-month high of US$1.2377 by the end of the third week of August. The single currency, however, bearing the brunt of the broad-based revival of the US dollar, shrugged off most its gains and by the close of the month, the euro had reached its intra-month low of US$1.1994. On 5 August 2004, the ECB at its governing council meeting held its key interest rates steady at 2.0 per cent. According to analysts, the ECB remained reluctant to tighten credit until it became sure that a return of domestic demand, needed to sustain a fully-fledged recovery, would not be tripped up by high energy prices or a slowdown in the euro zone's main trading partners.

The Pound sterling, amid easing expectations of aggressive UK monetary tightening, remained under pressure vis-à-vis the US dollar. As widely expected, the Bank of England raised its key interest rate at its monthly Monetary Policy Committee meeting on 5 August 2004 for the fifth time since November 2003 to 4.75 per cent, its highest in almost three years. The central bank said that the move was needed to keep inflationary pressures in check as the economy was still expanding briskly. But the release of UK consumer prices, which fell by 0.3 per cent on the month in July 2004, taking the annual rate down to 1.4 per cent, well below the Bank of England's 2.0 per cent target, has cast a shadow on future tightening. Minutes of the Bank of England's MPC meeting released later during the month further raised expectations that British interest rate might be close to their peak.

The Japanese yen, which was trading at around ¥111.14 against the US dollar in early August, gained ground to reach its intra-month high of ¥108.99 on 20 August 2004. The yen thereafter declined against the generally strong US dollar and by the close of the month was trading at around ¥109.61 vis-à-vis the US dollar.

A number of factors, already affecting the world oil market, piled up during the first three weeks of August 2004 to set oil prices at several record highs. Since prices hit the US$40 plus level and threatened to slow economic growth, OPEC has increased its production to the highest level in 25 years in an effort to keep prices under control. This has left little spare capacity to OPEC members, except Saudi Arabia. The strain on the world supply has left it more vulnerable to supply disruptions and increased the likelihood of price spikes. This has attracted further buying interest from hedge funds betting that prices could go even higher. Political tensions in the Middle East and violence in Iraq undermined traders' confidence in security of supply from the region, which pumps a third of the world's oil. The financial crisis at Russian oil giant Yukos, which produces around 20 per cent of Russia's crude has intensified supply concerns. Furthermore, an apprehension was instilled in the oil market that the referendum on Venezuelan President Hugo Chavez' rule could again destabilise Venezuelan exports. That weighed on the market until the win result of President Hugo Chavez declared on 16 August 2004. Supply security concerns have spurred many countries to increase strategic inventories, withdrawing supply from an already tight market. The United States continues to fill its strategic petroleum reserves despite high prices. Other countries including India, South Korea, Taiwan and China are building reserves or plan to start soon. NYMEX crossed several record highs in August. At the close of August 2004, though oil prices eased significantly as big speculators cashed in profits on news that Iraq had resumed its oil export loadings, oil prices remained at a relatively high level.

For the month of August 2004, NYMEX WTI (West Texas Intermediate benchmark crude oil) averaged US$44.9 a barrel, compared to US$31.6 a barrel in August 2003 and peaked at a high of US$49.40 a barrel on 20 August 2004 in overnight trade. IPE Brent futures averaged US$41.8 a barrel for the same period, compared to US$29.4 a barrel in August 2003.

COMEX gold futures strengthened further during August 2004, with an intra-month closing range between US$394.4/Oz and US$415.5/Oz compared to a range between US$387.0/Oz and US$408.4/Oz in July 2004. COMEX gold’s direction reflected to a large extent the performance of the US dollar on the foreign exchange market and the reaction of traders to the release of a set of economic data in the United States. Amid high oil prices, the inflation hedge status of gold bullion also weighed on the mind of investors. COMEX averaged US$404.2/Oz in August 2004, compared to an average of US$ 398.7/Oz in July 2004.

Domestic Developments

Tourist arrivals rose by 6.5 per cent, from 58,403 in July 2003 to 62,173 in July 2004, while gross tourism receipts increased by 18.2 per cent, from Rs1,415 million in July 2003 to Rs1,672 million in July 2004. For the period January 2004 to July 2004, tourist arrivals reached 394,850, representing an increase of 0.3 per cent compared to arrivals of 393,709 in the corresponding period of the preceding year. Tourism receipts for the period January 2004 to July 2004 grew by 31.2 per cent to reach Rs13,607 million compared to Rs10,371million recorded in the corresponding period in 2003.

The Consumer Price Index (CPI) increased from 112.5 in July 2004 to 112.7 in August 2004. The rate of inflation for the twelve-month period ended August 2004 stood at 4.0 per cent, compared to 3.9 per cent in July 2004.

Money supply M2 fell by Rs193 million or 0.1 per cent, from Rs141,132 million at the end of June 2004 to Rs140,939 million at the end of July 2004, reflecting seasonal factors. Narrow money supply M1, one of the components of M2, dropped by Rs100 million or 0.5 per cent to Rs21,222 million while quasi money, the other component of M2, declined by Rs93 million or 0.1 per cent to Rs119,717 million.

Net foreign assets of the banking system declined by Rs557 million or 1.1 per cent, from Rs49,120 million at the end of June 2004 to Rs48,563 million at the end of July 2004. Net foreign assets of Bank of Mauritius rose by Rs169 million or 0.4 per cent, from Rs43,262 million at the end of June 2004 to Rs43,431 million at the end of July 2004. Net foreign assets of Category 1 banks fell by Rs726 million or 12.4 per cent, from Rs5,858 million at the end of June 2004 to Rs5,132 million at the end of July 2004.

Domestic credit went up by Rs1,384 million or 1.1 per cent, from Rs128,799 million at the end of June 2004 to Rs130,183 million at the end of July 2004. Net credit to Government rose by Rs1,058 million or 3.0 per cent, from Rs35,346 million at the end of June 2004 to Rs36,404 million at the end of July 2004, driven by increases of Rs146 million and Rs913 million in net credit to Government from Bank of Mauritius and Category 1 banks, respectively. Credit to the private sector from Category 1 banks went up by Rs326 million, from Rs93,120 million at the end of June 2004 to Rs93,446 million at the end of July 2004. Over that period, additional credit was directed to the following sectors: “Personal” (Rs221 million), “Construction” (Rs206 million), “Statutory and Parastatal Bodies” (Rs142 million), “Traders” (Rs97 million) and “Infrastructure” (Rs42 million). Declines to the tune of Rs167 million, Rs97 million and Rs84 million were recorded at the following respective sectors “Manufacturing”, “Financial and Business Services” and “Agriculture and Fishing”.

Reserve money declined by Rs643 million or 2.6 per cent, from Rs24,905 million at the end of June 2004 to Rs24,262 million at the end of July 2004.

Taking into account liquidity conditions in the market in August 2004, the Bank carried out five reverse repurchase transactions. All the transactions were conducted for a period of 7 days at a fixed yield of 1.15 per cent.

During August 2004, total transactions in Treasury/Bank of Mauritius Bills effected through primary dealers amounted to Rs693 million while trading of Treasury Bills on the Stock Exchange amounted to Rs10 million.

Spot sales of foreign currencies by the Mauritius Sugar Syndicate to the banking sector during August 2004 amounted to an equivalent of US$2.3 million. The Bank intervened and sold US$20.3 million to banks during the month.

Between July and August 2004, the rupee, on average, appreciated against the Pound sterling, euro and Japanese yen but depreciated against the US dollar.

At the end of July 2004, the net international reserves of the country amounted to Rs49,466 million. Based on the value of the import bill for calendar year 2003, exclusive of purchase of aircrafts, the end-July 2004 level of net international reserves of the country represented 39.4 weeks of imports, down from 39.8 weeks of imports at the end of June 2004. At the end of August 2004, the foreign exchange reserves of the Bank of Mauritius amounted to Rs43,627 million, up from Rs43,521 million at the end of July 2004.