

O V E R V I E W

International Developments

During February 2007, the US dollar, on average, depreciated against the euro and Pound sterling but appreciated vis-à-vis the Japanese yen. US economic data released at the beginning of February 2007 were mixed. While manufacturing sector activity figures were weak, the jobs report proved to be quite healthy and the services sector activity index posted a stronger-than-expected reading. The US dollar benefited from comments made by US Treasury Secretary Henry Paulson who said that a strong dollar was in the country's interest. The US currency, thereafter, shed some of its gains in the wake of the release of a wider-than-expected trade deficit of US\$61.2 billion in December 2006. The release of data showing a slower-than-expected pace of home construction in January 2007 fuelled expectations that the US Federal Reserve might start cutting interest rates later this year. The unexpected decline in the preliminary Reuters/University of Michigan consumer sentiment index for February 2007 added additional pressure on the US dollar. The US dollar was also hurt by comments made by US Federal Reserve Chairman Ben Bernanke, who told the Senate Banking Committee that inflation was starting to diminish, boosting chances of an interest rate cut later this year. Bernanke's remarks surprised those who expected him to, at least, echo comments from other Fed officials who have dwelt on upside risks to the inflation outlook. The US dollar thereafter regained its footing amid the release of higher-than-expected January 2007 consumer price index, both headline and core, despite a dip in energy prices. Minutes of the Fed's January 2007 Federal Open Market Committee (FOMC) meeting noted that Fed officials did not yet see a downward trend in core inflation as definitively establishing that they remained ready to push interest rate up if needed. These developments, which made market players review their expectations of a cut in US interest rates later this year, provided support to the US dollar.

The euro strengthened against the US dollar during February 2007, trading at an average of US\$1.3076 from an average of US\$1.2991 in January 2007. From US\$1.3020 on 2 February 2007, the euro came under pressure against the US dollar after the release of a report by Market News International stating that "well-informed sources" had said that the European Central Bank (ECB) could refrain from raising interest rates for a while after the rise expected in March 2007. On 6 February 2007, the euro hit its intra-month low of US\$1.2923 against the dollar. As widely expected, the ECB kept its key refinancing rate on hold at 3.50 per cent at its governing council meeting on 8 February 2007. The single currency moved higher against the US dollar after ECB President Jean Claude Trichet, in his post-meeting conference, warned that euro zone inflation, currently hovering around 1.7-1.9 per cent, might be only temporarily lower and upward price pressures would intensify later this year. Investors interpreted those remarks as signalling an imminent benchmark interest rate increase in March 2007. The euro remained supported against the US dollar, backed by figures from Eurostat showing that the euro zone economy grew by a better-than-expected 0.9 per cent in the fourth quarter of 2006 and by 2.7 per cent on an annual basis,

its best rate in six years and almost double the 1.4 per cent seen in 2005. Comments from one ECB Governing Council member on persistent upside risks to inflation also buoyed the single currency, which continued to benefit from expectations of higher euro zone interest rates. The euro closed February 2007 at its intra-month high of US\$1.3220 against the US dollar.

The Pound sterling moved marginally higher against the US dollar during February 2007, trading at an average of US\$1.9590 from US\$1.9588 in January 2007. From US\$1.9675 on 2 February 2007, the Pound sterling strengthened against the US dollar to hit its intra-month high of US\$1.9724 on 8 February 2007 amid the release of a robust British retail sales survey, which boosted expectations for higher interest rates this year, and also speculation of more inflows related to corporate takeovers. On the same day, the Bank of England (BoE) kept its key repo rate steady at 5.25 per cent. However, over the following few days, the Pound sterling shed all its gains on profit taking by investors, negative merger and acquisition news as well as on the release of a bigger than expected trade deficit. The British currency was also undermined by inflation data – producer input prices and consumer prices – that cooled expectations for a near-term interest rate hike, and hit its intra-month low of US\$1.9465 on 14 February 2007. The Pound sterling, however, managed to resume its general upward trend against the US dollar following the release of the BoE quarterly report, which showed inflation falling to 2 per cent in two years assuming one more interest hike in the second quarter of this year, to 5.5 per cent, as already priced in by markets. In addition, BoE Governor Mervyn King said that the outlook for inflation was highly uncertain due to energy prices, a comment which some interpreted as suggesting that UK interest rates could rise even further in the future if price pressures warranted it. Data released until the end of the month were mixed. While retail sales fell in January 2007, house price data were strong and mortgage lending rose. The Pound sterling closed February 2007 trading around US\$1.9635.

The Japanese yen depreciated against the US dollar during February 2007, trading at an average of ¥120.56 per US dollar from an average of ¥120.38 per US dollar in January 2007. From ¥120.71 per US dollar on 2 February 2007, the Japanese yen strengthened against the US dollar ahead of the Group of Seven meeting, especially in view of comments by European officials on the weakness of the Japanese currency. The yen hit its intra-month low of ¥121.97 per US dollar on 12 February 2007, undermined by the post-G7 meeting communiqué, which did not make any explicit reference to the Japanese currency, but rather called on investors to consider Japan's strengthening economy and be wary of one-way bets in foreign exchange. The subsequent release of surprisingly strong Japanese GDP data, bolstering expectations for a near-term Bank of Japan (BOJ) rate hike, managed to provide support to the yen although investors doubted whether a potential interest rate increase would do much to help the Japanese currency. In fact, the Japanese yen fell against the US dollar after the BOJ, on 21 February 2007, raised its key interest rates by 25 basis points to 0.5 per cent. Traders stated that market players started to dump the yen as the BOJ's statement following the rate announcement offered few surprises and they felt that the central bank would take time before raising rates again. Profit taking by investors and unwinding of carry trades, where low-yielding currencies are used to fund purchases of higher return assets, thereafter pushed the Japanese yen to its intra-month high of ¥118.49 per US dollar on 28 February 2007.

Oil prices moved higher during February 2007 as disappointing weekly US oil inventory reports kept the market nervous. The output cut of 500,000 barrels per day (bpd) that OPEC had decided at its 14 December 2006 meeting became effective on 1 February 2007. That resulted into a current output quota of 26.3 million bpd. The International Energy Agency, which advises 26 industrialised nations, boosted its forecast of 2007 oil demand growth to 1.55 million bpd from 1.39 million bpd in its latest monthly report due to robust economic expansion in China, the world's second-largest oil consumer. The report helped oil prices remain high. Moreover, tension between Iran and the United States over Tehran's nuclear program also supported oil prices. Oil prices are expected to trade around US\$59 a barrel in the weeks ahead as the market seems to be under certain strain.

NYMEX WTI (West Texas Intermediate benchmark crude oil) averaged US\$59.4 a barrel for February 2007, up from US\$54.3 a barrel in January 2007 but down from US\$61.9 a barrel in February 2006. IPE Brent futures averaged US\$58.8 a barrel during the period under review, up from US\$54.7 in January 2007 but down from US\$61.1 a barrel in February 2006.

COMEX gold futures, on average, moved higher during February 2007, trading in an intra-month closing range of US\$651.5/Oz-US\$689.8/Oz compared to a range of US\$606.9/Oz-US\$657.9/Oz in January 2007. Gold prices continued to be influenced more by speculative moves than fundamental demand and supply factors, supported by rising oil prices. COMEX averaged US\$670.0/Oz during February 2007, compared to an average of US\$631.9/Oz in January 2007.

Domestic Developments

Tourist arrivals rose by 6.3 per cent, from 86,218 in January 2006 to 91,628 in January 2007, while gross tourism receipts went up by 18.5 per cent, from Rs3,411 million in January 2006 to Rs4,043 million in January 2007. On a cumulative basis, over the period July 2006 to January 2007, tourist arrivals reached 519,767, representing an increase of 4.4 per cent over the 497,970 arrivals recorded over the corresponding period of the previous fiscal year. Tourism receipts for the period July 2006 to January 2007 grew by 24.2 per cent to reach Rs20,534 million compared to Rs16,531 million recorded over the corresponding period of the previous fiscal year.

The Consumer Price Index (CPI) increased from 133.9 in January 2007 to 134.9 in February 2007. "Alcoholic beverages and tobacco", "Communication" and "Restaurants and hotels" recorded no change in their sub-indices while the largest rise was noted in the sub-Division "Food and non alcoholic beverages", which increased by 1.5 per cent, followed by "Education" (+1.1 per cent), "Miscellaneous goods and services" (+1.0 per cent), "Health" (+0.7 per cent), "Transport" (+0.6 per cent), "Housing, water, electricity, gas and other fuels" (+0.5 per cent), "Furnishings, household equipment and routine household maintenance" (+0.3 per cent) and "Clothing and footwear" (+0.2 per cent). The sub-Division "Recreation and culture" registered a decline of 0.3 per cent. The main contributors to the rise in the index between

January 2007 and February 2007 were fresh vegetables and other food products, each registering an increase of 0.2 index point and milk and milk preparations, chicken, materials for the maintenance and repairs of dwellings, airfare, goods for personal care and hygiene and other goods and services, each registering an increase of 0.1 index point. The rate of inflation for the twelve-month period ended February 2007 stood at 9.4 per cent, up from 9.1 per cent for the twelve-month period ended January 2007.

While headline inflation for February 2007 stood at 9.4 per cent, CORE1, CORE2 and TRIM10 inflation rates stood at 7.7 per cent, 7.2 per cent and 6.9 per cent, respectively. Consequently, for February 2007, core inflation was between 1.7 and 2.5 percentage points lower than the headline inflation.

The Bank of Mauritius has been compiling and disseminating data based in terms of both the Depository Corporations Survey (DCS) framework, which is based on the recommendations of the Monetary and Financial Statistics Manual (MFSM), and the Monetary Survey (MS) framework, which was the standard framework recommended by the IMF prior to the publication of the MFSM. Effective January 2007, the Bank has discontinued the compilation of the Monetary Survey and is using the Depository Corporations Survey as the only framework for compiling, analysing and disseminating monetary statistics.

The Depository Corporations Survey consolidates data of the Bank of Mauritius and other depository corporations, which includes banks as well as non-bank deposit taking institutions. Time series of monetary data based on the DCS framework have been revised to exclude transactions of Global Business Licence (GBL) holders, as these do not have any bearing on domestic economic developments.

Consequently, the tables giving time series data on the Sectoral Balance Sheet of banks and non-bank deposit taking institutions have been introduced and the time series data for Other Depository Corporations Survey and Depository Corporations Survey have been revised.

Net foreign assets of depository corporations expanded by 13,660 million or 21.3 per cent, from Rs64,202 million at the end of June 2006 to Rs77,862 million at the end of January 2007. This increase was brought about by the expansion of net foreign assets of both other depository corporations and the Bank of Mauritius. Net foreign assets of other depository corporations grew by Rs13,459 million or 61.5 per cent to Rs35,347 million while those of the Bank of Mauritius rose by Rs200 million or 0.5 per cent to Rs42,515 million. Claims on non residents went up by Rs38,089 million or 15.5 per cent, from Rs245,127 million at the end of June 2006 to Rs283,216 million at the end of January 2007. Liabilities to non residents increased by Rs24,430 million or 13.5 per cent, from Rs180,925 million at the end of June 2006 to Rs205,355 million at the end of January 2007.

Domestic claims of depository corporations, excluding claims on GBL holders, expanded by Rs6,814 million or 3.4 per cent, from Rs198,606 million at the end of June 2006 to Rs205,420 million at the end of January 2007. Net claims on budgetary central Government contracted by Rs4,704 million or 9.7 per cent, from Rs48,544 million at the end of June 2006 to Rs43,840 million at the end of January 2007. Claims on other sectors, exclusive of claims on GBL holders, (claims on private sector) grew by Rs11,519 million or 7.7 per cent to Rs161,580 million over the first seven months of 2006-07.

Net claims on budgetary central Government from the Bank of Mauritius increased by Rs2,387 million or 236.0 per cent, from Rs1,011 million at the end of June 2006 to Rs3,398 million at the end of January 2007. Net claims on budgetary central Government from other depository corporations contracted by Rs7,091 million or 14.9 per cent, from Rs47,533 million to Rs40,442 million.

Claims on other sectors (claims on the private sector) from the Bank of Mauritius fell by Rs43 million or 17.6 per cent, from Rs244 million at the end of June 2006 to Rs201 million at the January 2007 while claims on other sectors, exclusive of claims on GBL holders (claims on the private sector) from other depository corporations grew by Rs11,562 million or 7.7 per cent, from Rs149,817 million to Rs161,379 million.

Broad Money Liabilities (BML) expanded by Rs8,288 million or 4.2 per cent, from Rs198,415 million at the end of June 2006 to Rs206,703 million at the end of January 2007. Of the components of BML, currency with public went up by Rs1,327 million or 12.7 per cent to Rs11,759 million while transferable deposits grew by Rs3,740 million or 10.4 per cent to Rs39,675 million. Savings deposits increased by Rs2,398 million or 3.9 per cent to Rs63,328 million while time deposits expanded by Rs1,902 million or 2.1 per cent to Rs90,573 million. Securities other than shares included in broad money fell by Rs1,079 million or 44.1 per cent to Rs1,367 million.

The monetary base, excluding Bank of Mauritius Bills, went up by Rs279 million, or 1.3 per cent, from Rs22,015 million at the end of June 2006 to Rs22,294 million at the end of January 2007. Currency in circulation rose by Rs2,026 million, or 16.5 per cent, from Rs12,248 million to Rs14,274 million while liabilities to other depository corporations fell by Rs1,631 million or 18.0 per cent, from Rs9,048 million to Rs7,417 million.

Broad money multiplier went up from 9.0 at the end of June 2006 to 9.3 at the end of January 2007, reflecting a greater expansion of BML as compared to the monetary base.

The Bank issued Government of Mauritius Treasury Bills/Bank of Mauritius Bills for a total nominal amount of Rs3,777 million through the Primary Market in February 2007. The weighted average yields on the 91-day, 182-day and 364-day Bills, for the month of February 2007 decreased by 5 basis points - from 12.75 per cent to 12.70 per cent, by 7 basis points - from 12.93 per cent to 12.86 per cent and by 3 basis points - from 13.37 per cent to 13.34 per cent, respectively.

During the month, the Bank carried out 4 repos at the Repo rate plus 50 basis points, that is, at 9.00 per cent, and 3 reverse repos at the repo rate less 50 basis points, that is, at 8.00 per cent. Overnight interbank transactions for the month of February amounted to Rs7,783 million with a high of Rs680 million and a trough of Rs80 million. The overnight interbank rates ranged between 8.00 and 9.00 per cent.

During February 2007, total transactions in Government of Mauritius Treasury/Bank of Mauritius Bills effected through primary dealers amounted to Rs844.4million, while trading of Treasury Bills on the Stock Exchange of Mauritius amounted to Rs29.8 million.

At the monthly auction of Treasury Notes held in February 2007, a total nominal amount of Rs1,000 million of Treasury Notes with maturities of 2, 3, and 4 years, and with interest payable semi-annually at the rates of 11.50, 11.90 and 12.15 per cent per annum, respectively, were put on tender. Bids received for the three maturities totalled Rs2,539 million, of which Rs1,000 million were accepted. The weighted average yields on bids accepted for the 2, 3, and 4-year maturities were 13.40, 13.74 and 13.83 per cent per annum, respectively.

The fourth issue of Five-Year Government of Mauritius Bonds for 2006-07 was undertaken on 23 February 2007, through an auction held on 21 February 2007. Bonds for a total nominal amount of Rs500 million were put on tender at a coupon rate equal to or higher than the lowest accepted yield at the auction. Bids for an amount of Rs1,877.8 million were received, of which an amount of Rs500 million was accepted. The weighted average yield on bids accepted was 12.85 per cent per annum, and the coupon rate was set at 12.85 per cent per annum.

In February 2007, the Bank intervened and sold US\$10.8 million and purchased US\$64.0 million on the domestic interbank foreign exchange market.

Between January 2007 and February 2007, the rupee, on average, appreciated vis-à-vis all major currencies. The weighted average dealt selling rates of the rupee, which are calculated on the basis of transactions of US\$30,000 and above, or the equivalent in other foreign currencies effected by banks showed that the rupee, on average, appreciated against the US dollar, Euro and Pound Sterling between January 2007 and February 2007.

At the end of January 2007, the net international reserves of the country amounted to Rs77,546 million. Following the release of external trade data for the fourth quarter of 2006, the end-January 2007 level of net international reserves of the country, based on the value of the import bill for calendar year 2006, exclusive of the purchase of aircraft and ship, represented 37.1 weeks of imports, up from 35.5 weeks of imports at the end of December 2006. The gross foreign exchange reserves of the Bank of Mauritius rose from Rs42,647 million at the end of January 2007 to Rs44,716 million at the end of February 2007, reflecting essentially Bank of Mauritius intervention on the interbank foreign exchange market.