O V E R V I E W

International Developments

During January 2007, the US dollar, on average, appreciated against all major currencies. The US dollar garnered support from the significant drop in oil prices and the release of a series of upbeat data, which dampened market expectations that the Federal Reserve might cut interest rates in the coming months. The US Labour Department reported that 167,000 jobs were created in December 2006, leaving the unemployment rate unchanged at 4.5 per cent and also revised up hiring data for the two preceding months. Data also showed that the trade deficit unexpectedly shrank to US$58.2 billion in November 2006 from US$58.9 billion in October 2006, the smallest since July 2005. December 2006 retail sales data also came in better than expected. Net inflows of capital into US assets were to the tune of US$74.9 billion in November 2006, more than enough to cover the month's trade deficit. Profit-taking by investors temporarily halted the US dollar's ascent, which however managed to shrug off its losses amid the release of upbeat consumer sentiment and new home sales data that reinforced market view that an interest rate cut might not be necessary this year. On 31 January 2007, as widely expected, the Federal Reserve kept its federal funds rate steady at 5.25 per cent. The Fed's accompanying statement, which mentioned that inflationary pressures were likely to moderate, thereby suggesting that the US central bank might not raise interest rates in the coming months, triggered some US dollar sell-off. Market players had expected a more hawkish view on US inflation given the release of relatively solid economic data, including fourth-quarter 2006 GDP, which grew at an annualised pace of 3.5 per cent, above forecasts of 3.0 per cent.

The euro weakened against the US dollar during January 2007, trading at an average of US$1.2991 from an average of US$1.3209 in December 2006. Starting January 2007 at its intra-month high of US$1.3286, the euro embarked on a generally downward movement against the US dollar. As widely expected, at its governing council meeting on 11 January 2007, the European Central Bank (ECB) left its key refinancing rate unchanged at 3.50 per cent. On 12 January 2007, the single currency hit its intra-month low of US$1.2902 against the US dollar, undermined by comments from ECB President Jean-Claude Trichet, who, in his post-meeting conference, downplayed the prospects of a February 2007 rate hike that some market players had factored in. He nonetheless indicated that it was reasonable to expect that the ECB would probably raise interest rates near the end of the first quarter of 2007. The euro, however, recouped its losses following hawkish statements from ECB policymakers that euro zone interest rates would need to go up in the face of solid economic growth. In addition, the release of stronger-than-expected November 2006 industrial orders data also helped to bolster the euro. The euro closed January 2007 trading around US$1.2959.

The Pound sterling moved lower against the US dollar during January 2007, trading at an average of US$1.9588 from an average of US$1.9639 in December 2006. From US$1.9742 at the start of January 2007, the Pound sterling weakened against the US dollar, amid position adjustment and in the wake of the release of mortgage lender Halifax's report showing a drop in house prices in December 2006, to hit its intra-month low of US$1.9291 on 8 January 2007. The British currency thereafter embarked on a generally upward trend against the US dollar, benefiting from the release of strong retail sales data that led investors to price in further interest rate hikes by the Bank of England later this year. On 11 January 2007, the Bank of England surprised the market with a 25 basis points increase in its key repo rate to 5.25 per cent. Amid market expectations that the BOE would keep interest rate on hold in January 2007 and hike it in February 2007, the rate decision provided a boost to the Pound. Expectations of further tightening and remarks by Bank of England Governor Mervyn King stating that risks to British inflation and growth have shifted to the upside provided further support to the Pound. On 23 January 2007, on the New York market, the Pound sterling hit a 14-year high of US$1.9917 against the US dollar, challenging the psychologically key US$2.0 level. However, the Pound's move towards US$2.0 level was capped by the release of the Bank of England Monetary Policy Committee meeting minutes which showed that only five of its nine members voted for the surprise interest rate hike, sowing doubts about chances of more rate hikes. The Pound sterling closed January 2007 trading around US$1.9629.

The Japanese yen depreciated against the US dollar during January 2007, trading at an average of ¥120.38 per US dollar from an average of ¥117.19 per US dollar in December 2006. From an intra-month high of ¥118.30 per US dollar reached on 5 January 2007, the Japanese yen came under broad-based pressure, undermined by its low-yielding status even if investors saw the odds tilted in favour of Bank of Japan raising interest rates at its next policy meeting to 0.5 per cent, its highest level since 1995. On 18 January 2007, the Bank of Japan (BOJ) left its interest rate on hold at 0.25 per cent in a 6-3 vote, marking an abrupt shift in expectations. After the meeting, Governor Toshihiko Fukui said that the central bank found it prudent to await more data, given that indicators have been mixed. The release of soft December 2006 consumer price figures and a slide in Japanese retail sales cast further doubt on whether the Bank of Japan would raise interest rates in February 2007, thereby causing the yen to hit its intra-month low of ¥121.81 per US dollar on 29 January 2007. The Japanese yen closed January 2007 trading around of ¥121.53 per US dollar.

Oil prices moved lower during January 2007 amid mild US weather conditions in the first two weeks of January 2007, followed by some fund selling. Moreover, weekly US oil inventory reports were satisfactory. As mild weather conditions persisted for some time, heating oil demand was limited and weekly reports showed increases in stock levels. Several OPEC members were concerned about the fall in oil prices, which came as low as US$50.5 a barrel on 18 January 2007. But comments from Saudi Arabia Oil Minister saying that there was no need for OPEC to panic about the fall in prices and no need for an emergency meeting quelled doubts about any adverse OPEC action. Oil prices are expected to trade around US$55 a barrel in the weeks ahead as the US government stated that it would buy 11 million barrels over the next few months to fill its Strategic Petroleum Reserve.

NYMEX WTI (West Texas Intermediate benchmark crude oil) averaged US$54.3 a barrel in January 2007, down from US$62.1 a barrel in December 2006 and US$65.5 a barrel in January 2006. IPE Brent futures averaged US$54.7 a barrel during the period under review, down from US$62.3 in December 2006 and US$63.8 a barrel in January 2006.

COMEX gold futures, on average, moved lower during January 2007, trading in an intra-month closing range of US$606.9/Oz-US$657.9/Oz compared to a range of US$617.9/Oz-US$650.9/Oz in December 2006. Gold prices continued to be influenced more by speculative moves than fundamental demand and supply factors, with falling oil prices and a stronger US dollar pulling prices down. COMEX averaged US$631.9/Oz during January 2007, compared to an average of US$632.3/Oz in December 2006.

Domestic Developments

Tourist arrivals grew by 6.4 per cent, from 90,519 in December 2005 to 96,309 in December 2006, while gross tourism receipts increased by 24.8 per cent, from Rs3,154 million in December 2005 to Rs3,935 million in December 2006. Tourist arrivals for the year 2006 reached 788,276, representing a rise of 3.6 per cent over the 761,063 arrivals recorded in 2005. Tourism receipts for the year 2006 increased by 24.3 per cent to reach Rs31,942 million compared to Rs25,704 million recorded in 2005.

The Consumer Price Index (CPI) increased from 133.7 in December 2006 to 133.9 in January 2007. The largest rise was noted in the sub-Division “Education”, which rose by 7.8 per cent, followed by “Food and non-alcoholic beverages” (+2.0 per cent), “Recreation and culture” (+1.8 per cent), “Clothing and footwear” (+1.2 per cent), “Miscellaneous goods and services” (+1.2 per cent) and “Alcoholic beverages and tobacco” (+1.1 per cent). The largest decline of 7.1 per cent was recorded in the “Transport” sub-Division. The main contributors to the rise in the index between December 2006 and January 2007 were other goods and services, which rose by 0.3 index point, and trader’s rice, frozen mutton, chicken, fish, powdered milk, fresh eggs, refined oil, fresh vegetables, whisky, ready made clothing, school textbooks, school fees, tuition fees and food and drinks in bars and restaurants, each registering an increase of 0.1 index point. This was partially offset by decreases of 1.1 index point in gasoline and 0.1 index point in motor vehicles, kerosene, diesel oil and airfare. The rate of inflation for the twelve-month period ended January 2007 stood at 9.1 per cent, up from 8.9 per cent for calendar year 2006.

While headline inflation for January 2007 stood at 9.1 per cent, CORE1, CORE2 and TRIM10 inflation rates stood at 7.6 per cent, 7.2 per cent and 6.7 per cent, respectively. Consequently, for January 2007, core inflation was between 1.5 and 2.4 percentage points lower than the headline inflation.

Money supply M2 grew by Rs9,177 million or 5.2 per cent, from Rs177,527 million at the end of June 2006 to Rs186,704 million at the end of December 2006 on account of the increase in both quasi money and narrow money supply. Narrow money supply M1 went up by Rs3,095 million or 12.4 per cent to Rs28,164 million while quasi-money went up by Rs6,082 million or 4.0 per cent to Rs158,540 million.

Net foreign assets of the banking system expanded by Rs12,214 million or 19.9 per cent, from Rs61,435 million at the end of June 2006 to Rs73,649 million at the end of December 2006. Net foreign assets of Bank of Mauritius increased by Rs1,673 million or 3.9 per cent to Rs44,127 million on account of valuation changes, which were partly offset by Bank of Mauritius intervention in the foreign exchange market, while net foreign assets of banks grew by Rs10,541 million or 55.5 per cent to Rs29,522 million over the same period.

Domestic credit grew by Rs8,582 million or 5.2 per cent, from Rs164,961 million at the end of June 2006 to Rs173,543 million at the end of December 2006. Net credit to Government from the banking system contracted by Rs3,279 million or 7.2 per cent, from Rs45,490 million at the end of June 2006 to Rs42,211 million at the end of December 2006. Net credit to Government from Bank of Mauritius rose by Rs4,488 million or 273.5 per cent to Rs6,129 million while net credit to Government from banks fell by Rs7,767 million or 17.7 per cent to Rs36,082 million. Credit to the private sector expanded by Rs11,862 million or 9.9 per cent, from Rs119,471 million at the end of June 2006 to Rs131,333 million at the end of December 2006. Between end June 2006 and end December 2006, additional credit was extended to “Financial and Business Services” (Rs2,660 million), “Tourism” (Rs2,618 million), “Traders” (Rs2,610 million), “Construction” (Rs1,412 million), “Personal” (Rs991 million), “Infrastructure” (Rs614 million), “Public Nonfinancial Corporations” (Rs387 million), “Manufacturing” (Rs241 million) and “Transport” (Rs175 million). Over the same period, a decline of Rs108 million was recorded at the “Agriculture and Fishing” sector.

Reserve money grew by Rs1,275 million or 5.2 per cent, from Rs24,543 million at the end of June 2006 to Rs25,818 million at the end of December 2006

The Bank issued Government of Mauritius Treasury Bills/Bank of Mauritius Bills for a total nominal amount of Rs5,658 million through the Primary Market in January 2007. The weighted average yields on the 91-day, 182-day and 364-day bills, for the month of January 2007, increased by 107 basis points - from 11.68 per cent to 12.75 per cent, by 101 basis points - from 11.92 per cent to 12.93 per cent and by 100 basis points - from 12.37 per cent to 13.37 per cent respectively.

During the month, the Bank carried out eleven reverse repurchase transactions at 8.00 per cent i.e. the repo rate less 50 basis points. Overnight interbank transactions for the month of January 2007 amounted to Rs12,415 million, with a high of Rs888 million and a trough of Rs90 million. The overnight interbank rates ranged between 8.00 and 9.00 per cent.

During January 2007, total transactions in Government of Mauritius Treasury/Bank of Mauritius Bills effected through primary dealers amounted to Rs1,325.1 million, while trading of Treasury Bills on the Stock Exchange of Mauritius amounted to Rs0.5 million.

At the monthly auction of Treasury Notes held in January 2007, a total nominal amount of Rs1,500 million of Treasury Notes with maturities of 2, 3, and 4 years, and with interest payable semi-annually at the rates of 10.00, 10.40 and 10.65 per cent per annum, respectively, were put on tender. Bids received for the three maturities totalled Rs1,630 million, of which Rs1,500 million were accepted. The weighted average yields on bids accepted for the 2, 3, and 4-year maturities were 13.41, 13.64 and 13.85 per cent per annum, respectively.

In January 2007, the Bank intervened and sold US$38 million on the domestic interbank foreign exchange market.

Between December 2006 and January 2007, the rupee, on average, appreciated vis-à-vis the euro and Japanese yen but depreciated against the US dollar and the Pound sterling. 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 December 2006 and January 2007.

At the end of December 2006, the net international reserves of the country amounted to Rs74,192 million. The end-December 2006 level of net international reserves of the country, based on the value of the import bill for fiscal year 2005-06, exclusive of the purchase of aircraft, represented 38.2 weeks of imports, up from 38.0 weeks of imports at the end of November 2006. The gross foreign exchange reserves of the Bank of Mauritius fell from Rs44,127 million at the end of December 2006 to Rs42,647 million at the end of January 2007, reflecting essentially Bank of Mauritius intervention on the interbank foreign exchange market.

Provisional estimates for the third quarter of 2006 indicate that the current account of the balance of payments surged to a higher deficit of Rs6,419 million compared to a deficit of Rs3,253 million in the third quarter of 2005, reflecting essentially a deterioration in the merchandise and income accounts as well as a lower surplus on the services account. The deficit in the merchandise account of the balance of payments increased to Rs6,851 million in the third quarter of 2006, from Rs5,249 million a year earlier. The deficit on the income account widened significantly to Rs1,551 million in the third quarter of 2006 from Rs290 million in the corresponding period of 2005. The capital and financial account, inclusive of reserve assets, recorded net inflows of Rs1,591 million in the third quarter of 2006 compared to Rs2,515 million in the third quarter of 2005. The overall balance of payments for the third quarter of 2006, measured as the change in reserve assets excluding valuation changes, registered a deficit of Rs1,901 million.

Provisional estimates for calendar year 2006 indicate that gross foreign direct investment (FDI) in Mauritius stood at Rs6,410 million compared to Rs2,807 million in 2005. Investment was mainly directed to the banking sector (Rs2,730 million) and the tourism sector (Rs2,610 million), mostly under the Integrated Resorts Scheme (IRS). Among the main sources of FDI inflows to Mauritius were the United Kingdom (Rs3,107 million), followed by Switzerland (Rs584 million) and France (Rs425 million). Gross outward FDI flows were estimated at Rs1,134 million in 2006 compared to Rs1,942 million in the preceding year. Significant investments were directed to the tourism sector (Rs391 million), mainly in the Maldives and the Seychelles and the agricultural sector in Mozambique (Rs270 million). Direct investment to Madagascar amounted to Rs291 million and was mostly destined to the manufacturing sector.