

## **OVERVIEW**

### **International Developments**

During July 2003, the US dollar, on average, appreciated vis-à-vis the euro, Pound sterling and Japanese yen. The US currency rose in the second and third weeks of July 2003 against major currencies as expectations for a US economic recovery gathered steam and sent Wall Street stocks higher. However, a lack of concrete evidence of any rebound made markets uneasy and blunted the dollar's upward momentum. In his testimony to the US congress on 15 July 2003, Fed Chairman Alan Greenspan reassured markets that the central bank would maintain an accommodative monetary policy to ensure a strong economic recovery. In June 2003, the US unemployment rate climbed to a nine-year high of 6.4 per cent, from 6.1 per cent in May 2003. However, in the week ended 19 July 2003, the number of new US jobless claims, for the first time since February 2003, dropped to 386,000, below the critical 400,000 mark. The preliminary estimates of US GDP growth rate for the second quarter of 2003 stood at 2.6 per cent on a year-on-year basis.

Following its retreat to levels around US\$1.14 in the last week of June 2003, the euro in July 2003 lost the strength it had in May 2003 partly because investors expected growth in the US to be better than in the euro zone. At its meeting on 10 July 2003, the Governing Council of the ECB decided to leave its key refinancing rate unchanged at 2.00 per cent. Latest data on the euro zone in July 2003 continued to suggest that economic growth remained subdued in the second quarter of 2003 after standing at 0.1 per cent on a quarter-on-quarter basis in the first quarter of 2003. Euro zone inflation data showed that the monthly inflation rate was 0.1 per cent in June 2003 while the yearly inflation rate increased to 2.0 per cent in June 2003 from 1.9 per cent in May 2003. On 14 July 2003, French President Jacques Chirac made the strongest statement by any EU Head of State calling for a more flexible interpretation of EU's Growth and Stability Pact (GSP) on fiscal discipline. The GSP requires EU member countries to have debt levels of not more than 60 per cent of GDP and a budget deficit of not more than 3.0 per cent of GDP. With French GDP growth projected at below 1.0 per cent this year and barely 2.0 per cent in 2004, France's budget deficit and debt levels are expected to hit 3.5 per cent of GDP and 61 per cent of GDP, respectively. Germany's fiscal and economic situation also remained dismal.

After months of staying on the sidelines, the Bank of England surprised financial markets by cutting its key repo rate by a quarter percentage point to a new 48-year low of 3.50 per cent at its first MPC meeting with Mervyn King as Governor on 9–10 July 2003. The minutes showed that members voted 8-1 in favour of the 25-basis points rate cut and said that the Pound's rise since May 2003 could lower growth and inflation in the coming months. Not surprisingly, the Pound plunged immediately following the decision, mirroring its reaction to the Bank's last rate cut in February 2003. UK second-quarter growth stood at 0.3 per cent on a quarter-on-quarter basis and 1.8 per cent on a yearly basis. UK inflation data released in July 2003 showed that monthly RPIX was 0.1 per cent in June 2003 and annual RPIX declined from 2.9 per cent in May 2003 to 2.8 per cent in June 2003.

The Japanese yen depreciated against the US dollar mainly on account of an improvement in some US economic indicators. The Bank of Japan held its two-day Policy Board meeting on 14-15 July 2003 and, as expected, left its monetary policy unchanged. For the first time in a year, the Japanese government, in its July 2003 monthly report, upgraded its assessment of the economy. However, latest trade figures released on 24 July 2003 showed that Japan's export growth came to a standstill in June 2003 as demand faltered in the United States and Asia, its top two markets. Japan's exports to the United States fell by 12 per cent in value terms and by 10.6 per cent in volume terms. Nevertheless, most analysts see a pick-up in both Japanese exports and the Japanese economy as a whole later this year, helped by an expected improvement in the United States.

### **Domestic Developments**

Tourist arrivals increased by 7.2 per cent from 39,048 in June 2002 to 41,841 in June 2003, while gross tourism receipts increased by 16.9 per cent, from Rs1,186 million in June 2002 to Rs1,387 million in June 2003. During fiscal year 2002-03, gross tourism receipts fell by 5.5 per cent to Rs17,996 million from Rs19,045 million in 2001-02. However, total tourist arrivals increased by 4.0 per cent from 667,247 in 2001-02 to 694,247 in 2002-03.

The Consumer Price Index (CPI) rose from 106.9 in June 2003 to 107.5 in July 2003. The rate of inflation for the 12-month period ended July 2003 stood at 5.0 per cent.

Money supply M2 rose by Rs12,938 million or 11.7 per cent, from Rs110,467 million at the end of June 2002 to Rs123,405 million at the end of June 2003. Narrow money supply M1, one of the components of M2, went up by Rs2,304 million or 15.2 per cent to Rs17,439 million and quasi-money rose by Rs10,634 million or 11.2 per cent to Rs105,966 million.

Net foreign assets of the banking system expanded by Rs7,642 million or 19.1 per cent, from Rs39,974 million at the end of June 2002 to Rs47,616 million at the end of June 2003. Net foreign assets of the Bank of Mauritius rose by Rs9,720 million or 32.5 per cent to Rs39,632 million while net foreign assets of Category 1 banks fell by Rs2,078 million or 20.7 per cent to Rs7,984 million.

Domestic credit rose by Rs7,531 million or 7.6 per cent, from Rs99,396 million at the end of June 2002 to Rs106,927 million at the end of June 2003. Net credit to Government by the banking system increased by Rs2,496 million or 13.2 per cent to Rs21,476 million, reflecting the increase of Rs10,283 million or 46.4 per cent in net credit to Government from Category 1 banks that was partly offset by the drop of Rs7,787 million in net credit to Government from the Bank of Mauritius.

Credit to the private sector from Category 1 banks rose by Rs5,104 million or 6.4 per cent, from Rs79,976 million at the end of June 2002 to Rs85,080 million at the end of June 2003. Credit was mainly channelled to "Tourism" (Rs2,105 million), "Personal & Professional" (Rs1,006 million), "Traders" (Rs949 million), "New Economy" (Rs925 million), "Agriculture & Fishing" (Rs772 million) and "Construction" (Rs316 million). There was a drop in credit to "Statutory & Parastatal Bodies" (Rs989 million), "Manufacturing" (Rs530 million) and "Infrastructure" (Rs108 million).

Reserve money increased by Rs1,851 million or 14.3 per cent, from Rs12,925 million at the end of June 2002 to Rs14,776 million at the end of June 2003.

Taking into account liquidity conditions in the market in July 2003, the Bank carried out two reverse repurchase transactions for 1 and 2 days, respectively, and one repurchase transaction for 1 day. The highest yield accepted for the reverse repurchase transactions was 1.25 per cent per annum while the lowest yield accepted for the repurchase transaction was 5.00 per cent per annum.

Total transactions in eligible Government securities effected through primary dealers during July 2003 amounted to Rs1,136 million.

Direct Sales of foreign currencies by the Mauritius Sugar Syndicate to the banking sector during July 2003 amounted to an equivalent of US\$3.60 million. As the comfortable liquidity situation in the domestic foreign exchange market continued to prevail, the Bank intervened and purchased a total of US\$17.35 million in July 2003. Between June 2003 and July 2003, the rupee, on average, depreciated against the euro, the Pound Sterling, the US dollar and the Japanese yen.

At the end of June 2003, the net international reserves of the country amounted to Rs48,200 million. Based on the value of the import bill for calendar year 2002, the end-June 2003 level of net international reserves of the country represented 42.0 weeks of imports, up from 39.4 weeks at the end of May 2003. At the end of July 2003, the foreign exchange reserves of the Bank of Mauritius amounted to Rs40,166 million, up from Rs39,632 million at the end of June 2003.