OVERVIEW

International Developments

During July 2005, the US dollar, on average, appreciated against all major currencies. The US dollar started July 2005 on a strong note as the market remained focused on the US currency's interest rate advantage over other major currencies. The release, thereafter, of weaker-than-expected June 2005 jobs report as well as profit taking by currency traders pressured the US dollar. The US currency, however, managed to regain ground after the release of data showing a narrower-than-expected trade deficit of US$55.35 billion in May 2005, followed by data pointing to a rise to US$60 billion in net inflow of foreign capital into US assets, more than the amount needed to finance the trade gap. US Federal Reserve Chairman, Alan Greenspan's bullish testimony before the US Congress on 20 July 2005, which helped to confirm the view that the US economy was on a solid footing, provided further support to the US currency. China's announcement on 21 July 2005 that it was abandoning its dollar peg in favour of a basket of its main trading partners' currencies to manage the yuan and its currency's revaluation from a fixed value of 8.28 to 8.11 per US dollar, kept the US currency's gains in check. But as the impact of China's yuan revaluation faded and officials of the People's Bank of China played down talk of a further revaluation of the yuan, the US dollar picked up again.

The euro, which traded on average around US$1.2166 in June 2005, moved lower against the US dollar in July 2005, trading on average around US$1.2047. The euro at the start of July fell as far as US$1.1889 in London trade, its lowest level since late May 2004, after ECB Governing Council member Christian Noyer said that any euro country could abandon the single currency. As widely expected, on 7 July 2005, the ECB kept its key refinancing rate unchanged at 2.0 per cent. The euro, however, managed to shrug off its losses after Luxembourg, on 10 July 2005, gave a solid approval of 56.52 per cent to the EU constitution. Dampening expectations for an interest rate cut in the euro zone thereafter benefited the single currency, which reached its intra-month high of US$1.2217. In the wake of the bullish market sentiment favouring the US dollar, the euro could not hold up to its gains. By the close of the month, the euro was trading around US$1.2122.

The Pound sterling depreciated against the US dollar in July 2005, trading on average around US$1.7528, down from US$1.8194 in June 2005. From an intra-month high of US$1.7861 at the start of July, the Pound sterling fell to US$1.7417, its lowest level since December 2003, after a series of bomb blasts on 7 July 2005 in London raised concerns about terrorist attacks in the UK. As the financial markets calmed down, the Pound sterling, amid position adjustments, managed to regain ground against the US dollar. But the release thereafter of weak data on UK jobless claims and home sales, fuelling expectations of a near term rate cut, weighed on the Pound. Market views that the Bank of England would cut its interest rate at its August monetary policy meeting were further reinforced after the release of the minutes of the July 2005 MPC meeting which revealed that 4 out of the 9 members voted for a 25 basis points rate cut. While the subsequent release of soaring UK retail sales data provided a brief respite to the Pound, heightened security concerns after the failed four bombs attack on London transport system on 21 July 2005 added pressure on the British currency. By the close of the month, the Pound traded around US$1.7542.

The Japanese yen, on average, depreciated vis-à-vis the US currency, trading on average around ¥111.92 per US dollar in July 2005 as against ¥108.59 per US dollar in the previous month. From its intra-month high of ¥111.00 per US dollar at the start of July, the Japanese yen fell vis-à-vis the US dollar, pressured by the record high level of oil prices. However, in the aftermath of China's decision on 21 July 2005 to revalue the yuan, the Japanese yen gained sharply against the US dollar. The yen's rise further accelerated after Malaysia changed the ringgit peg of 3.8 per US dollar to a managed float. By the close of the month, the yen had shed some of its gains amid position adjustment and on market belief that China would not make any other significant changes to its exchange rate for some time and that further appreciation of its currency would be limited.

Oil prices continued to rise during July 2005, trading consistently above US$57 a barrel. Weekly reports from US Energy Information Administration (EIA), showing, on average, unsatisfactory US crude oil stock levels, supported oil prices upward. Growing worries over US refiners' ability to meet the demand for heating oil and diesel during the forthcoming winter season in the United States also impacted on oil prices. Formation of two hurricanes during the period under review pushed prices upwards as they were expected to disturb oil production in the Gulf of Mexico. Fortunately, these storms did not have any major impact on oil production infrastructure. In the last week of July, fire broke out at two refineries, one in the United States and one in the North Sea, adding further nervousness in the international oil market and pushing oil prices to new record highs. Looking ahead, oil prices would most likely trade above US$55 a barrel in the forthcoming weeks.

For the month of July 2005, NYMEX WTI (West Texas Intermediate benchmark crude oil) averaged US$59.0 a barrel, compared to US$56.4 a barrel in June 2005 and US$40.8 a barrel in July 2004. IPE Brent futures averaged US$58.0 a barrel during the period under review, compared to US$55.4 a barrel in June 2005 and US$37.7 a barrel in July 2004. NYMEX and IPE Brent reached new all-time highs of US$61.3 a barrel and US$59.9 a barrel respectively, on 6 July 2005.

COMEX gold futures, on average, moved lower in July 2005, trading in an intra-month closing range of US$420.2/Oz-US$435.8/Oz compared to a range of US$417.7/Oz-US$443.2/Oz. During the period under review, fund and speculative selling drove gold prices down. US dollar strength also weighed on gold prices. COMEX averaged US$425.1/Oz during July 2005, compared to an average of US$433.4/Oz in June 2005.

Domestic Developments

The Bank of Mauritius increased the Lombard Rate, which is used as the signalling mechanism of its monetary policy stance, by 50 basis points from 10.00 per cent to 10.50 per cent per annum on 5 August 2005. This measure, which was taken in the light of recent domestic and international economic developments, aims at containing inflationary pressures in the economy, enhancing the attractiveness of domestic financial instruments and improving savings mobilisation. The decision was also premised on the need to tighten demand management policies to avoid undue pressures on the rupee, given the weakening external sector outlook.

Tourist arrivals rose by 10.7 per cent, from 38,826 in June 2004 to 42,994 in June 2005, while gross tourism receipts declined by 2.0 per cent, from Rs1,569 million in June 2004 to Rs1,537 million in June 2005. For the year 2004-05, tourist arrivals reached 735,495, representing an increase of 5.2 per cent compared to 699,389 arrivals in the year 2003-04. Tourism receipts for the year 2004-05 grew by 7.6 per cent to reach Rs24,097 million compared to Rs22,394 million recorded in the previous fiscal year.

The Consumer Price Index (CPI) increased from 117.3 in June 2005 to 118.0 in July 2005. The rate of inflation for the twelve-month period ended July 2005 stood at 5.6 per cent, unchanged from the rate for fiscal year 2004-05.

In the June 2005 issue of the National Accounts Estimates, released in July 2005, the Central Statistics Office has used the results obtained from the Census of Economic Activities (CEA) carried out in 2002 to update and rebase the main National Accounts aggregates for the years 2002 to 2005. The data are thus not strictly comparable with earlier series, which are based on the 1997 Census data. The real growth rate of the economy for 2004 has been revised to 4.1 per cent, marginally lower than the 4.2 per cent estimated in March 2005. Exclusive of sugar, the growth rate for 2004 works out to 4.0 per cent, the same rate as estimated earlier.

The growth rate of the economy for 2005 has been revised downwards to 3.8 per cent from the March 2005 forecast of 5.1 per cent. Exclusive of sugar, the real growth for 2005 is estimated at 4.1 per cent. The sugar sector is now expected to register a negative growth of 3.9 per cent compared to a positive growth of 6.5 per cent in 2004, based on a sugar production of around 550,000 tonnes compared to the previous estimate of 575,000 tonnes and down from 572,316 tonnes in 2004. This decline is explained by unfavourable climatic conditions prevailing during the first few months of the year. The EPZ sector is projected to register a larger contraction of 8.0 per cent as a result of closures and downsizing of units due to the elimination of textile trade quotas and the severe competition faced from low cost producing economies. The tourism sector is forecast to grow by 4.8 per cent with tourist arrivals estimated at 755,000 instead of the 775,000 assumed in March 2005. The construction sector is expected to expand by 1.0 per cent, lower than the prior estimate of 3.8 per cent, owing to delays in the construction of hotels and shopping malls.

Investment in the economy is forecast to grow, in real terms, by 2.5 per cent in 2005 compared to 1.5 per cent in 2004. The investment rate, as measured by the ratio of GDFCF to GDP at market prices, is projected to decrease slightly from 21.6 per cent in 2004 to 21.5 per cent in 2005. Private sector investment is expected to contract by 1.3 per cent in 2005 after a high growth of 15.8 per cent in 2004. Public sector investment is forecast to expand by 11.2 per cent in 2005 after a contraction of 20.9 per cent in 2004. The savings rate is expected to fall to 19.6 per cent in 2005 from 22.8 per cent in 2004.

Money supply M2 expanded by Rs11,996 million or 8.5 per cent, from Rs141,132 million at the end of June 2004 to Rs153,128 million at the end of June 2005. Narrow money supply M1, one of the components of M2, grew by Rs1,325 million or 6.2 per cent to Rs22,647 million while quasi-money, the other component of M2, went up by Rs10,670 million or 8.9 per cent to Rs130,481 million.

Net foreign assets of the banking system rose by Rs3,385 million or 6.9 per cent, from Rs49,120 million at the end of June 2004 to Rs52,505 million at the end of June 2005. Net foreign assets of Bank of Mauritius fell by Rs566 million or 1.3 per cent to Rs42,696 million while net foreign assets of former Category 1 banks grew by Rs3,951 million or 67.4 per cent to Rs9,809 million.

Domestic credit grew by Rs14,495 million or 11.3 per cent, from Rs128,799 million at the end of June 2004 to Rs143,294 million at the end of June 2005. Net credit to Government from the banking system went up by Rs5,543 million or 15.7 per cent to Rs40,889 million. Net credit to Government from Bank of Mauritius rose by Rs1,498 million or 215.6 per cent to Rs803 million while net credit to Government from former Category 1 banks increased by Rs4,045 million or 11.2 per cent to Rs40,086 million. Credit to the private sector from former Category 1 banks expanded by Rs8,949 million or 9.6 per cent, from Rs93,120 million at the end of June 2004 to Rs102,069 million at the end of June 2005. Over that period, additional credit was directed to "Construction" (Rs3,048 million), "Traders" (Rs1,988 million), "Personal (Rs1,238 million), "Manufacturing" (Rs1,075 million), "Tourism" (Rs924 million), "Statutory and Parastatal Bodies" (Rs679 million), "Infrastructure" (Rs397 million), "Professional" (Rs197 million) and "Transport" (Rs191 million). Over the same period, declines were registered at "New Economy" (Rs495 million), "Agriculture & Fishing" (Rs413 million) and "Financial and Business Services" (Rs216 million).

Reserve money fell by Rs1,964 million or 7.9 per cent, from Rs24,905 million at the end of June 2004 to Rs22,941 million at the end of June 2005.

Taking into account liquidity conditions in the market, the Bank did not carry out any repurchase transaction in July 2005.

During July 2005, total transactions in Government of Mauritius Treasury/Bank of Mauritius Bills effected through primary dealers amounted to Rs360.0 million while trading of Treasury Bills on the Stock Exchange of Mauritius amounted to Rs4.8 million.

Between June and July 2005, the rupee, on average, appreciated vis-à-vis the euro, Pound sterling and Japanese yen but depreciated against the US dollar.

Spot sales of foreign currencies by the Mauritius Sugar Syndicate to the banking sector during July 2005 amounted to an equivalent of US$2.1 million. The Bank intervened and sold US$26.0 million to banks during the month. The weighted average dealt selling rates of the rupee, which are calculated on transactions of US$30,000 and above, or the equivalent in other foreign currencies, effected by commercial banks, showed that the rupee, on average, depreciated against the US dollar but appreciated against the Euro and Pound sterling between June and July 2005.

At the end of June 2005, the net international reserves of the country amounted to Rs53,486 million. The end-June 2005 level of net international reserves of the country, based on the value of the import bill for calendar year 2004, exclusive of the purchase of aircraft, represented 36.4 weeks of imports, down from 37.1 weeks at the end of May 2005. Reflecting mainly intervention by the Bank on the foreign exchange market, the foreign exchange reserves of the Bank of Mauritius declined to Rs42,005 million at the end of July 2005, from Rs42,734 million at the end of June 2005.