

O V E R V I E W

International Developments

During March 2007, the US dollar, on average, depreciated against the Japanese yen and euro but appreciated vis-à-vis the Pound sterling. While the US dollar was buoyed by strong factory activity data at the start of the month, those gains were later reversed following the release of weaker-than-expected figures on durable goods orders. The US dollar remained under pressure after the Federal Reserve Beige Book, which provides an anecdotal report on the economy, showed that 4 out of 12 districts reported slowing activity in the latter part of February 2007. The US currency, thereafter, recouped its losses, as global stock markets recovered from a sell-off and made investors comfortable about rebuilding carry trades. The US dollar also benefited from the release of fairly encouraging economic data on job creation and trade that eased speculation of a possible rate cut by the Federal Reserve. The US dollar, however, could not hold onto its gains amid concerns over growing problems in the US mortgage and housing sectors that could potentially impact on the broader economy. In fact, former Federal Reserve Chairman Alan Greenspan later warned of contagion risks in the subprime mortgage market where defaults and foreclosures had been rising. The downward movement of the US dollar was exacerbated by the sell-off in US stock markets and as investors trimmed exposure to carry trades. Comments by People's Bank of China Governor, who was quoted as saying that China would stop stockpiling foreign exchange reserves, also weighed on the US currency. The US dollar was also undermined after the Federal Reserve held its federal funds rate steady at 5.25 per cent and dropped its reference to possible further rate hikes in its accompanying statement. The Fed also indicated that future policy adjustments would depend on the evolution of the outlook for both inflation and economic growth. The US dollar managed to draw only short-lived gains from a surprise jump in existing US home sales for February 2007 as data indicating a fall in new home sales came shortly after. Softer-than-expected consumer confidence data and lingering concerns about a slowing US housing market, which rekindled expectations for the Federal Reserve to trim interest rates in the next few months, also pressured the US dollar towards the end of March 2007.

The euro strengthened against the US dollar during March 2007, trading at an average of US\$1.3247 from an average of US\$1.3076 in February 2007. Against the backdrop of a strong US dollar, the euro, which started the month trading at around US\$1.3223, reached its intra-month low of US\$1.3101 on 6 March 2007. The single currency moved within tight ranges even after the European Central Bank (ECB), as expected, lifted its key refinance rate by 25 basis points to a five-year high of 3.75 per cent on 8 March 2007. In fact after his post-meeting press conference, ECB President Jean-Claude Trichet left investors uncertain about how much further rates might rise, describing interest rates as moderate rather than "low" as credit conditions were less stimulative. The euro, however, thereafter embarked on a generally upward trend against the weakening US dollar, partly supported by the release of the ECB's March 2007 monthly report, indicating potential further rises in euro zone interest rates. On 22 March 2007, the euro hit its intra-month high of US\$1.3384 against the US dollar. The single currency remained well supported until the end of the month with members of the ECB's Governing Council stressing that

rates were still supporting economic growth while medium term inflation risks were persisting. Such comments supported the view that the ECB would push on with higher interest rates in the months ahead. The euro closed March 2007 trading around US\$1.3345 against the US dollar.

The Pound sterling moved lower against the US dollar during March 2007, trading at an average of US\$1.9478 from US\$1.9590 in February 2007. Opening the month trading around US\$1.9619, the Pound sterling came under pressure to hit its intra-month low of US\$1.9261 on 6 March 2007 as investors unwound their long positions into the British currency amid uncertainty in global financial markets. The Pound sterling thereafter managed to gain ground against the US dollar, benefiting from the release of stronger-than-expected retail sales figures that rekindled speculation over a possible further rise in interest rates later this year. On 8 March 2007, as expected, the Bank of England (BoE) kept its key repo rate unchanged at 5.25 per cent for the second month running. Nonetheless, the British currency continued to trade in tight ranges until 19 March 2007, when it crossed the US\$1.94 mark, indirectly supported by its strength against the yen. Thereafter, the Pound sterling got a boost from the release of above-consensus inflation and housing data, which reinforced expectations of a further interest rate rise from the Bank of England. On 27 March 2007, the Pound sterling hit its intra-month high of US\$1.9690, but later shrugged off some of its gains after BOE governor, Mervyn King, in his testimony to the UK Parliamentary Committee, said that there were more signs that the housing market was beginning to slow. The Pound sterling closed March 2007 trading around US\$1.9637.

The Japanese yen appreciated against the US dollar during March 2007, trading at an average of ¥117.23 per US dollar from an average of ¥120.56 per US dollar in February 2007. From ¥118.17 per US dollar at the start of March, the Japanese yen strengthened against the US dollar as investors continued to unwind carry trades and as stock markets around the world stumbled. On 15 March 2007, the Japanese currency hit its intra-month high of ¥115.72 per US dollar, benefiting from comments by St. Louis Federal Reserve President William Poole who said that he saw nothing disruptive in carry trades, or bets on high-yielding currencies financed by borrowing in low-yielding currencies, such as Japanese yen or Switzerland franc. Thereafter, the Japanese currency weakened against the US dollar as recovery in US and Japanese stock markets alleviated fears that more investors might cut back on risky positions in their portfolios. The Japanese yen hit its intra-month low of ¥118.23 per US dollar on 23 March 2007 before closing the month trading around ¥117.83 per US dollar.

Oil prices, on average, moved higher during March 2007 with disappointing weekly US oil inventory reports keeping the market edgy and driving prices upward. At its meeting on 15 March 2007 in Vienna, Austria, OPEC decided to leave its output quota of 26.3 million barrels per day (bpd) unchanged. For several consecutive weeks, the US Energy Information Administration had been reporting a significant fall in US gasoline stocks. Analysts were of the view that these reports were an indication that oil demand would remain elevated for some time in particular ahead of the US driving season. This would in turn keep oil futures well supported. News that Iran captured 15 British navy personnel exacerbated tensions between Iran and the West and led oil prices to levels above US\$65 a barrel. The decision by Iran thereafter to release the British navy personnel eased oil prices to some extent. However, oil prices are expected to trade around US\$63 a barrel in the weeks ahead as the US driving season approaches.

NYMEX WTI (West Texas Intermediate benchmark crude oil) averaged US\$60.7 a barrel in March 2007, up from US\$59.4 a barrel in February 2007 but down from US\$62.9 a barrel in March 2006. IPE Brent futures averaged US\$62.5 a barrel during the month under review, up from US\$58.8 in February 2007 but down from US\$63.0 a barrel in March 2006. On the domestic front, effective 2 April 2007, the Certification Committee of the Automatic Pricing Mechanism decided to keep the retail price of Mogas unchanged at Rs32.50 per litre but to increase that of Diesel by 6.98 per cent, from Rs26.50 to Rs28.35 per litre.

COMEX gold futures, on average, moved lower during March 2007, trading in an intra-month closing range of US\$639.2/Oz-US\$669.0/Oz compared to a range of US\$651.5/Oz-US\$689.8/Oz in February 2007. Prices were driven down by heavy fund selling after sharp falls in global stock prices turned investors more risk-averse. Market players also liquidated their bullion positions to cover losses made in financial markets. Gold prices continued to be influenced more by speculative moves than fundamental demand and supply factors. COMEX averaged US\$655.6/Oz during March 2007, compared to an average of US\$670.0/Oz in February 2007.

Domestic Developments

In the March 2007 issue of its National Accounts Estimates, the Central Statistics Office revised the real growth rate of the economy for 2006 to 5.0 per cent, from the 4.7 per cent estimated in December 2006, essentially on account of better performances of the EPZ and the non-EPZ manufacturing (excluding sugar) sectors. Exclusive of sugar, the growth of the economy was estimated at 5.3 per cent.

The main contributors to growth in 2006 were the 'Transport, storage and communications', 'Financial intermediation', 'Real estate, renting and business services' and 'Wholesale and retail trade' industry groups, which grew by 7.2 per cent, 7.0 per cent, 6.2 per cent and 5.4 per cent, respectively. The tourism industry grew by 3.5 per cent with tourist arrivals reaching 788,276 in 2006. The EPZ sector grew by an estimated 4.6 per cent after four years of contraction. After a contraction of 5.2 per cent in 2005, the construction industry rebounded in 2006, growing by 5.1 per cent due to the construction of new hotels and implementation of projects under the Integrated Resort Scheme (IRS). The sugar industry contracted by 2.9 per cent with a sugar production of 504,857 tonnes, down from 519,816 tonnes in 2005.

Investment in the economy recovered, in real terms, by 18.2 per cent in 2006 following a contraction of 2.4 per cent in 2005. The investment rate, as measured by the ratio of GDFCF to GDP at market prices, increased from 21.3 per cent in 2005 to 24.0 per cent in 2006. Private sector investment grew by 13.6 per cent in 2006, mainly on account of the high investments in hotels and IRS projects, after a decline of 1.0 per cent in 2005. Public sector investment expanded by 29.1 per cent in 2006, mainly as a result of investment in aircrafts, following a contraction of 5.4 per cent in 2005.. The savings rate fell to 16.2 per cent in 2006 from 17.3 per cent in 2005.

The economy is forecast to grow by around 5.0 per cent in 2007, the same as in 2006. Exclusive of sugar, the forecast growth would be around 5.2 per cent. The earlier forecast of a 5.5 per cent growth of the economy has been revised down due mainly to a downward revision of sugar production from

550,000 tonnes to 500,000 tonnes following the passage of cyclone Gamede in February 2007. The tourism sector is forecast to grow by 7.3 per cent, with tourist arrivals estimated at 850,000. The financial intermediation and construction sectors are expected to post a growth of 7.0 per cent and 7.5 per cent, respectively, while the EPZ sector is forecast to expand by 2.5 per cent.

Tourist arrivals went up by 11.5 per cent, from 64,894 in February 2006 to 72,338 in February 2007, while gross tourism receipts grew by 25.6 per cent, from Rs2,716 million in February 2006 to Rs3,411 million in February 2007. On a cumulative basis, over the period July 2006 to February 2007, tourist arrivals reached 592,105, representing an increase of 5.2 per cent over the 562,864 arrivals recorded over the corresponding period of the previous fiscal year. Tourism receipts for the period July 2006 to February 2007 rose by 24.4 per cent to reach Rs23,945 million compared to Rs19,247 million recorded over the corresponding period of the previous fiscal year.

The Consumer Price Index (CPI) increased from 134.9 in February 2007 to 136.1 in March 2007. The largest rise was noted in the sub-Division "Food and non alcoholic beverages", which went up by 2.2 per cent, followed by "Furnishings, household equipment and routine household maintenance" (+0.9 per cent), "Restaurants and hotels (+0.8 per cent), "Alcoholic beverages and tobacco" (+0.7 per cent), "Miscellaneous goods and services" (+0.5 per cent), "Health" (+0.3 per cent), "Housing, water, electricity, gas and other fuels" (+0.2 per cent) and "Clothing and footwear" (+0.2 per cent). The sub-Divisions "Recreation and culture" and "Transport", registered declines of 0.3 per cent and 0.2 per cent, respectively. "Communication" and "Education" recorded no change in their sub-indices. The main contributors to the rise in the index between February 2007 and March 2007 were fresh vegetables which rose by 0.3 index point and fresh fruits, powdered milk, meat, chicken, fish, ginger, wine, washing materials and softeners, food and drinks in bars and restaurants and other goods and services, each registering an increase of 0.1 index point. This was partially offset by a decrease of 0.1 index point in airfare. The rate of inflation for the twelve-month period ended March 2007 stood at 9.7 per cent, up from 9.4 per cent for the twelve-month period ended February 2007.

While headline inflation for March 2007 stood at 9.7 per cent, CORE1, CORE2 and TRIM10 inflation rates stood at 7.7 per cent, 7.6 per cent and 7.0 per cent, respectively. Consequently, for March 2007, core inflation was between 2.0 and 2.7 percentage points lower than the headline inflation.

Net foreign assets of depository corporations went up by Rs17,251 million or 26.9 per cent, from Rs64,202 million at the end of June 2006 to Rs81,453 million at the end of February 2007. This expansion reflects the increase in net foreign assets of both other depository corporations and the Bank of Mauritius. Net foreign assets of other depository corporations grew by Rs15,038 million or 68.7 per cent to Rs36,925 million while those of the Bank of Mauritius increased by Rs2,213 million or 5.2 per cent to Rs44,527 million. Claims on non-residents rose by Rs51,190 million or 20.9 per cent, from Rs245,127 million at the end of June 2006 to Rs296,317 million at the end of February 2007. Liabilities to non-residents increased by Rs33,939 million or 18.8 per cent, from Rs180,925 million at the end of June 2006 to Rs214,864 million at the end of February 2007.

Domestic claims of depository corporations, excluding claims on GBL holders, grew by Rs4,340 million or 2.2 per cent, from Rs198,606 million at the end of June 2006 to Rs202,946 million at the end of February 2007. Net claims on budgetary central Government contracted by Rs6,490 million or 13.4 per cent, from Rs48,544 million at the end of June 2006 to Rs42,054 million at the end of February 2007. Claims on other sectors, exclusive of claims on GBL holders but inclusive of extra budgetary units, rose by Rs10,831 million or 7.2 per cent to Rs160,893 million over the first eight months of 2006-07.

Net claims on budgetary central Government from the Bank of Mauritius went up by Rs1,275 million or 126.0 per cent, from Rs1,011 million at the end of June 2006 to Rs2,286 million at the end of February 2007. Net claims on budgetary central Government from other depository corporations contracted by Rs7,765 million or 16.3 per cent, from Rs47,533 million to Rs39,768 million.

Claims on other sectors from the Bank of Mauritius edged up by Rs13 million or 5.1 per cent, from Rs244 million at the end of June 2006 to Rs257 million at the February 2007 while claims on other sectors, exclusive of claims on GBL holders but inclusive of claims on extra budgetary units, from other depository corporations grew by Rs10,819 million or 7.2 per cent, from Rs149,817 million to Rs160,636 million.

Broad Money Liabilities (BML) grew by Rs12,670 million or 6.4 per cent, from Rs198,415 million at the end of June 2006 to Rs211,085 million at the end of February 2007. Of the components of BML, currency with public increased by Rs1,220 million or 11.7 per cent to Rs11,652 million while transferable deposits went up by Rs4,665 million or 13.0 per cent to Rs40,600 million. Savings deposits rose by Rs3,062 million or 5.0 per cent to Rs63,993 million while time deposits expanded by Rs4,957 million or 5.6 per cent to Rs93,628 million. Securities other than shares included in broad money fell by Rs1,234 million or 50.5 per cent to Rs1,212 million.

The monetary base went up by Rs494 million, or 2.2 per cent, from Rs22,015 million at the end of June 2006 to Rs22,509 million at the end of February 2007. Currency in circulation grew by Rs1,819 million, or 14.9 per cent, from Rs12,248 million to Rs14,067 million while liabilities to other depository corporations fell by Rs1,215 million or 13.4 per cent, from Rs9,048 million to Rs7,833 million.

Broad money multiplier went up from 9.0 per cent at the end of June 2006 to 9.4 per cent at the end of February 2007, reflecting a greater expansion of BML as compared to the monetary base.

The Bank issued Government of Mauritius Treasury/Bank of Mauritius Bills for a total nominal amount of Rs12,500 million through the Primary Market in March 2007. The weighted average yields of the 91-day, 182-day and 364-day Bills, for the month of March 2007 decreased from 12.56 per cent to 11.54 per cent, from 12.83 per cent to 11.59 per cent and from 13.07 per cent to 11.25 per cent, respectively.

During the month of March 2007, the Bank carried out 9 reverse repos at the Repo rate less 50 basis points, that is, at 8.00 per cent. No repo transaction was carried out. Overnight interbank transactions for the month of March 2007 amounted to Rs6,495 million with a high of Rs944 million and a trough of Rs1 million. The weighted average overnight interbank rate for March 2007 stood at 8.17 per cent compared to 8.70 per cent for the previous month.

During March 2007, total transactions in Government of Mauritius Treasury/Bank of Mauritius Bills effected through primary dealers amounted to Rs1,708 million, while trading of Treasury Bills on the Stock Exchange of Mauritius amounted to Rs55.5 million.

At the monthly auction of Treasury Notes held in March 2007, a total nominal amount of Rs1,500 million with maturities of 2, 3, and 4 years, and with interest payable semi-annually at the rates of 11.25, 11.65 and 11.90 per cent per annum, respectively, was put on tender. Bids received for the three maturities totalled Rs4,210.9 million, of which Rs1,500 million was accepted. The weighted average yields on bids accepted for the 2, 3, and 4-year maturities were 11.67, 11.97 and 11.98 per cent per annum, respectively.

In March 2007, the Bank purchased US\$75.3 million on the domestic interbank foreign exchange market.

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

At the end of February 2007, the net international reserves of the country amounted to Rs78,601 million. The end-February 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 37.6 weeks of imports, up from 37.1 weeks of imports at the end of January 2007. The gross foreign exchange reserves of the Bank of Mauritius rose from Rs44,716 million at the end of February 2007 to Rs47,337 million at the end of March 2007, reflecting essentially Bank of Mauritius intervention on the interbank foreign exchange market.

Provisional estimates for calendar year 2006 suggest that the current account of the balance of payments recorded a higher deficit of Rs19,608 million compared with Rs9,569 million in 2005, reflecting mainly a deterioration in the merchandise account largely on account of the purchase of three aircrafts. The deficit in the merchandise account of the balance of payments surged to Rs34,494 million, from Rs23,515 million a year earlier. The deficit on the merchandise account was, however, partly offset by surpluses on the services, income and current transfers accounts. The capital and financial account, inclusive of reserve assets, recorded lower net inflows of Rs6,051 million in 2006 compared to Rs9,043 million in 2005. The overall balance of payments for 2006, measured as the change in reserve assets excluding valuation changes, registered a lower deficit of Rs4,573 million compared to a deficit of Rs4,888 million in 2005.