OVERVIEW

International Developments

During September 2003, the US dollar, on average, depreciated against the major currencies, hurt by renewed doubts that the pace of US economic recovery might not be sustainable amid a persistently weak labour market and rising “twin deficits”. The US dollar, which was relatively well supported in early September, lost ground steadily against all major currencies. A rise in US jobless claims while economists anticipated a small decline, weaker-than-expected US August employment report and mounting war costs, which could widen the budget deficit projected just two months ago at 5 per cent of GDP, raised doubts about the strength of the economic recovery. On 16 September 2003, the Federal Open Market Committee (FOMC) kept as widely expected the fed funds rate unchanged at 1.00 per cent, highlighting that interest rates could remain low for a considerable period. It added that on balance the risk of inflation becoming undesirably low remained the predominant concern for the foreseeable future and described the labour market as “weakening”. The US dollar, which had until then been supported by recurrent yen-selling intervention by the Japanese authorities, gave way after the G-7 Finance Ministers’ meeting on 20-21 September 2003 called for more flexibility on exchange rates, prompting speculation that Japan would find it difficult to conduct aggressive currency intervention. The US dollar remained fragile as the market interpreted US support for the G-7 statement as a departure from the US strong dollar policy.

The euro, which had fallen below US$1.09 in the last week of August 2003, was stuck in narrow ranges against the US dollar in the first week of September 2003 despite the release of quite favourable data for the euro zone. The closely watched Reuters Eurozone PMI ticked upward to 49.1 in August 2003, close to the 50 level while the business activity index survey came in unexpectedly strong in August. However, data on manufacturing activity showed that the manufacturing sector was still contracting and producer prices were more subdued than expected. The ECB interest rate-setting meeting held on 4 September 2003 left, as expected, its key refinancing rate unchanged at 2.00 per cent. Meanwhile, more data releases showed that the euro zone second quarter GDP contracted, as expected, by 0.1 per cent, euro zone inflation increased to 2.1 per cent in August 2003 from 1.9 per cent in July 2003, while industrial production expanded by 0.6 per cent between June and July 2003. Concerns about the US economic recovery benefited the euro, which remained close to USD1.13 up to 19

September 2003. However, following the G-7 Finance Ministers meeting, the euro appreciated strongly against the US dollar and reached levels above US$1.16 on 30 September 2003.

With the manufacturing sector in the UK recovering faster than expected and the renewed surge in house prices as well as the favourable outlook for the services sector, which grew at its fastest pace since January 2001, the Pound sterling gained ground steadily against the US dollar and remained well bid throughout September 2003. Reflecting the good health of the British economy, jobs data showed that unemployment fell again in July 2003 giving an unchanged jobless rate of 5.1 per cent. The overall weakness of the US dollar on the international market also benefited the British currency. At its Monetary Policy Committee (MPC) two-day meeting on 3-4 September 2003, the Bank of England left its key repo rate unchanged at 3.50 per cent. But the minutes of the MPC September meeting later released showed that some policymakers contemplated a rate rise although all nine members voted to keep interest rates steady. Signs that the UK economy was gaining momentum as well as the US dollar rapid decline in the week following 22 September 2003 propped up the Pound, which closed September 2003 at US$1.6685.

Data releases in September 2003 in Japan indicated that the Japanese economy might have turned around. Japanese companies boosted spending on plant and equipment in April-June 2003, while exports went up by 5.4 per cent, signalling that Japan was recovering firmly due to strong overseas demand. Moreover, GDP growth was revised upwards in April-June 2003. Signs that the Japanese economy was recovering were evident as Japanese stocks soared higher inducing strong repatriation of funds from Japanese investors as well as foreign investment in Japanese assets. Repatriation of funds by domestic investors for the half-year book closing at the end of September 2003 also boosted the yen, but its gains against the US dollar were limited by market wariness over yen-selling intervention. In the wake of the G-7 Finance Ministers' statement calling for more exchange rate flexibility, the yen shot up against the US dollar and reached a three-year high at around JPY111.00 per US dollar on 30 September 2003.

Domestic Developments

Tourist arrivals increased by 6.5 per cent, from 53,395 in August 2002 to 56,844 in August 2003, while gross tourism receipts fell by 7.7 per cent, from Rs1,488 million in August 2002 to Rs1,374 million in August 2003. Cumulatively for the period January 2003 to August 2003, tourist arrivals increased by 4.1 per cent, to 450,553 from 432,811 for the same period in 2002. However, over the same period, gross tourism receipts declined by 3.1 per cent, from Rs12,109 million in 2002 to Rs11,731 million in 2003.

The Consumer Price Index (CPI) rose from 107.4 in August 2003 to 107.9 in September 2003. The rate of inflation for the 12-month period ended September 2003 stood at 4.6 per cent.

Monetary developments in August 2003 largely reflected the take-over of the Post Office Savings Bank (POSB) by the Mauritius Post and Cooperative Bank on 1 August 2003.

Money supply M2 expanded by Rs2,469 million or 2.0 per cent, from Rs123,405 million at the end of June 2003 to Rs125,874 million at the end of August 2003. Narrow money supply M1, one of the components of M2, fell by Rs388 million or 2.2 per cent to Rs17,051 million, while quasi-money rose by Rs2,857 million or 2.7 per cent to Rs108,822 million.

Net foreign assets of the banking system declined by Rs598 million, from Rs47,568 million at the end of June 2003 to Rs46,969 million at the end of August 2003. Net foreign assets of the Bank of Mauritius rose by Rs186 million or 0.5 per cent to Rs39,770 million while net foreign assets of Category 1 banks fell by Rs785 million or 9.8 per cent to Rs7,200 million.

Domestic credit rose by Rs2,331 million or 2.2 per cent, from Rs106,927 million at the end of June 2003 to Rs109,258 million at the end of August 2003. Net credit to Government by the banking system expanded by Rs1,546 million or 7.2 per cent to Rs23,023 million, reflecting the increase of Rs1,801 million or 5.6 per cent in net credit to Government from Category 1 banks that was partly offset by the decrease of Rs254 million or 2.3 per cent in net credit to Government from the Bank of Mauritius.

Credit to the private sector from Category 1 banks rose by Rs766 million or 0.9 per cent, from Rs85,080 million at the end of June 2003 to Rs85,846 million at the end of August 2003. Credit was mainly channelled to “Traders” (Rs474 million), “Financial & Business Services” (Rs410 million) and “Construction” (Rs246 million). There was a drop in credit to “Statutory & Parastatal Bodies” (Rs220 million) and “Manufacturing” (Rs180 million).

Reserve money increased by Rs652 million or 4.4 per cent, from Rs14,776 million at the end of June 2003 to Rs15,428 million at the end of August 2003, mainly as a result of BoM Bills issued by the Bank of Mauritius.

The Bank did not carry out any repurchase/reverse repurchase transaction during September 2003.

Total transactions in eligible Government securities effected through the primary dealers during September 2003 amounted to Rs1,119 million.

Direct sales of foreign currencies by the Mauritius Sugar Syndicate to the banking sector during September 2003 amounted to an equivalent of US$33.77 million. As the comfortable liquidity situation in the domestic foreign exchange market continued to prevail, the Bank intervened and purchased a total of US$9.10 million in September 2003. Between August 2003 and September 2003, the rupee, on average, appreciated vis-à-vis the US dollar but depreciated against the euro, Pound sterling and the Japanese yen.

With a view to lengthening the maturity structure of Government debt, the Bank of Mauritius announced on 11 September 2003 that it would proceed, in its capacity as agent of Government, with four quarterly issues of Rs500 million each of Five-Year Government Bonds with coupon rates varying between 8.00-8.50 per cent during fiscal year 2003-04. In addition, there would be two issues of Mauritius Development Loan Stocks with maturities ranging from seven to fifteen years, the first issue to be held on Friday 21 November 2003 for an amount of up to Rs2.0 billion and the second issue on Friday 19 March 2004 for the remaining balance of approximately Rs1.0 billion, thus bringing the total nominal amount of Government securities to be issued to Rs5.0 billion.

At the auction of Five-Year Government Bonds held on 30 September 2003 for a total tender amount of Rs500 million, the coupon rate was fixed at 8.00 per cent. Bids were received for a total nominal amount of Rs576 million, of which Rs500 million were accepted. Yields received ranged from 9.20 to 9.80 per cent and the weighted yield on bids accepted was 9.49 per cent compared to 9.73 per cent obtained at the auction held on 30 June 2003.

At the end of August 2003, the net international reserves of the country amounted to Rs47,805 million. Data on net international reserves for the months of June and July 2003 have been revised upwards on account of an increase in Mauritius's Reserve Position in the Fund. Following the release of external trade data for the second quarter of 2003, the end-August 2003 level of net international reserves of the country, based on the value of the import bill for fiscal year 2002-03, exclusive of purchase of aircrafts, represented 38.1 weeks of imports, up from 32.7 weeks of imports as at the end of August 2002. At the end of

September 2003, the foreign exchange reserves of the Bank of Mauritius amounted to Rs41,098 million, up from Rs39,770 million at the end of August 2003.