

OVERVIEW

International Developments

During September 2007, the US dollar, on average, depreciated against all major currencies amid bearish market sentiment over the health of the US economy in the wake of weak data releases and fears of recession. Weak data releases started with the US Labour Department reporting, in the first week of the month, that employers, for the first time in four years, had cut down 4,000 jobs in August 2007, surprising financial markets that were anticipating 110,000 new jobs and raising expectations for the Fed to cut rates by 50 basis points to stave off a deeper economic slowdown and help relieve a squeeze in money markets. Data showing a narrowing of the trade deficit in July 2007 to US\$59.2 billion from an upwardly revised estimate of US\$59.4 billion in June 2007, had relatively no impact on the US dollar. At its FOMC meeting on 18 September 2007, the Federal Reserve reduced its benchmark interest rates by 50 basis points to 4.75 per cent. Further data releases thereafter justified the interest rate move. Producer price inflation (PPI) eased to an annual rate of 2.2 per cent in August 2007 from 4.0 per cent in July 2007 while year-on-year consumer price inflation fell to 2.0 per cent in August 2007 from 2.4 per cent in July 2007. The US National Association of Home Builders reported a dip in its September 2007 housing market index to 20, matching the record low registered in January 1991 when the economy was mired in recession, while the US Commerce Department showed that sales of new single-family homes dropped by 8.3 per cent in August 2007 to an annual rate of 795,000, the slowest in seven years. These data releases kept the US dollar under selling pressure and reinforced expectations that the Fed might lower interest rates again at its FOMC meeting on 30-31 October 2007, a move that would further hurt the dollar's yield appeal.

The euro moved higher against the US dollar, trading at an average of US\$1.3886 during September 2007 compared to an average of US\$1.3619 during August 2007, capitalizing mostly on the broad-based weakness of the US dollar. The European Central Bank (ECB), amid concerns relating to the credit crisis, left its key-refinancing rate on hold at 4.00 per cent at its Governing Council meeting on 6 September. In his post-meeting press conference, ECB President Jean-Claude Trichet avoided using language that might signal a rate rise in October 2007 but rather stated that given the high level of uncertainty, additional information was needed before further conclusions for monetary policy could be drawn. Amid general US dollar weakness, the euro gained ground against the US currency, supported by views that the ECB could still boost rates once financial markets stabilize. On 12 September 2007 the euro reached a new high of US\$1.3880 in Tokyo trade and a day later surged to US\$1.3930 in New York trade on remarks from European policymakers suggesting that future euro-zone rate hikes remained on the table. As it continued to benefit from its anti-dollar status, the euro broke the key psychological level of US\$1.40 for the first time, reaching US\$1.4064 in Tokyo trade on 20 September 2007. The single currency thereafter attained a new high of US\$1.4120 in New York trade on 21 September 2007 but surrendered some of its gains following the release of weaker than expected services data relating to Purchases Managers Index (PMI). On 26 September 2007, the euro, in Tokyo trade, reached an all-time high of US\$1.4163 before closing the month at US\$1.4159.

The Pound sterling moved higher against the US dollar, trading at an average of US\$2.0168 during September 2007 compared to an average of US\$2.0101 during August 2007. The Pound started the month on a firm note against the US dollar, benefiting from the release of robust manufacturing and sales

data. At the end of the two-day Monetary Policy Committee (MPC) meeting on 5-6 September, the Bank of England (BoE) left its key repo rate unchanged at 5.75 per cent amid worries over the ongoing credit crunch. In a rare move, the BoE even issued a communiqué indicating that it was too early to tell to what extent consumers and companies would suffer from the storm sweeping global financial markets. The Pound sterling, however, edged down against the US dollar as BoE's decision to issue a statement indicated that policymakers were increasingly worried by the implications of the ongoing credit crunch. Remarks by BoE Governor Mervyn King in front of the parliament's Treasury Committee, suggesting that UK interest rates might not be raised further, coupled with news that thousands of depositors pulling their money from UK mortgage lender Northern Rock added pressure on the Pound. Minutes of the latest MPC meeting revealing that the MPC members voted unanimously to leave interest rate on hold, thereby confirming market expectations that interest rates might have peaked at the current 5.75 per cent, further weighed on the Pound. However, the release thereafter of data showing stronger-than-expected retail sales and firm mortgage lending figures for August 2007 provided support to the Pound sterling which closed the month at US\$2.0226.

The Japanese yen moved higher against the US dollar on the back of the broad-based weakness of the US currency, trading at an average of ¥115.03 per USD during September 2007 compared to an average of ¥116.69 per USD during August 2007. The Bank of Japan (BOJ) left its target interest rate unchanged at 0.50 per cent at the end of its two-day policy board meeting on 18-19 September 2007 as expected in the wake of turbulence in global financial markets. The BOJ's nine-member board voted 8-1 to keep rates steady.

Oil prices moved higher during September 2007 mainly on supply concerns. Weather disturbances in the Gulf of Mexico and in Texas, threatening oil production units, kept the market edgy and fuelled supply worries. Simultaneously, the US Energy Information Administration reported sharp falls in US crude stock levels week after week. Unrest in Nigeria and mounting tensions between Syria and Israel in the second week of September also weighed on the market. At its 11 September meeting, OPEC decided to increase its output quota by 500,000 barrels effective 1 November 2007. The market viewed the quota increase as being insufficient and oil futures moved to record levels above US\$80 a barrel thereafter. The fact that oil futures crossed the key psychological level of US\$80 a barrel supported fund buying in the oil market, which in turn, drove prices to record high levels. NYMEX and IPE Brent reached all-time highs of US\$83.3 a barrel on 20 September and US\$80.0 a barrel on 27 September, respectively. US dollar weakness also partly supported oil prices upwards. In the last week of September, concerns over the health of the US economy eased oil prices to some extent. In the weeks ahead, oil prices would most likely trade above US\$79 a barrel ahead of the high oil-demand Northern Hemisphere winter season.

NYMEX WTI (West Texas Intermediate benchmark crude oil) averaged US\$79.6 a barrel in September 2007, up from US\$72.4 a barrel in August 2007 and US\$63.9 a barrel in September 2006. IPE Brent futures averaged US\$77.0 a barrel during the period under review, up from US\$71.2 a barrel in August 2007 and US\$63.6 a barrel in September 2006.

COMEX gold futures, on average, moved sharply higher during September 2007, trading in an intra-month closing range of US\$690.7/Oz-US\$750.0/Oz compared to a range of US\$658.0/Oz-US\$686.3/Oz in August 2007. Gold prices moved higher during the period under review on US dollar weakness and high oil prices. Moreover, the 50 basis points interest rate cut by the US Federal Reserve supported gold prices. The bullion even crossed the key psychological level of US\$700/Oz. COMEX averaged US\$723.4/Oz during September 2007, compared to an average of US\$675.5/Oz in August 2007.

Domestic Developments

In the September 2007 issue of its National Accounts Estimates, the Central Statistics Office has maintained the real growth rate of the economy for 2006 at 5.0 per cent. Exclusive of sugar, the growth of the economy is estimated at 5.3 per cent in 2006. The main contributors to growth in 2006 were the 'Transport, storage and communications', 'Financial intermediation', 'Wholesale and retail trade' and 'Real estate, renting and business services' industry groups, which grew by 7.4 per cent, 7.0 per cent, 5.2 per cent and 6.3 per cent, respectively. The tourism industry grew by 3.5 per cent with tourist arrivals reaching 788,276 in 2006. The textile sector grew by an estimated 2.9 per cent after four years of contraction. Following a contraction of 4.4 per cent in 2005, the construction industry rebounded in 2006, registering a growth of 5.2 per cent, mainly attributable to the construction and renovation of hotels and the implementation of projects under the Integrated Resort Scheme (IRS). The sugar sector contracted by 2.9 per cent in 2006.

Investment in the economy recovered, in real terms, by 19.2 per cent in 2006 following a contraction of 1.9 per cent in 2005. The investment rate, as measured by the ratio of GDFCF to GDP at market prices, increased from 21.4 per cent in 2005 to 24.3 per cent in 2006. Private sector investment grew by 15.3 per cent in 2006 after a decline of 0.3 per cent in 2005. Public sector investment expanded by 28.5 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 17.0 per cent in 2006 from 17.4 per cent in 2005.

The economy is now projected to grow by 5.8 per cent in 2007, up from the June 2007 estimate of 5.3 per cent, mainly owing to higher projected growths of "Manufacturing", "Construction" and "Hotels and restaurants". Exclusive of sugar, the growth rate would be around 6.4 per cent compared with the previous estimate of 5.8 per cent. The manufacturing sector is forecast to grow by 3.7 per cent in 2007, mainly on account of growths of 7.2 per cent and 3.9 per cent in textile and food processing industries, respectively. The "Hotels and restaurants" sector is expected to grow by 13.1 per cent, based on a projection of 900,000 tourist arrivals. The financial sector would grow by an estimated 7.2 per cent. The construction sector is expected to post a stronger performance in 2007, mainly due to the construction and renovation of hotels, IRS projects and expansion of textile and wearing apparel industries, with a growth of 12.0 per cent. The "Wholesale and Retail Trade" sector would expand by an estimated 4.3 per cent. The sugar sector, affected by tropical cyclone Gamede which hit the country in February 2007, is expected to contract by 7.9 per cent, based on a sugar production of 465,000 tonnes.

Tourist arrivals went up by 8.8 per cent, from 64,307 in August 2006 to 69,941 in August 2007, while gross tourism receipts grew by 28.0 per cent, from 2,483 million in August 2006 to Rs3,177 million in August 2007. On a cumulative basis, over the period January to August 2007, tourist arrivals reached 579,279, representing an increase of 18.2 per cent over 489,984 arrivals recorded over the corresponding period of the previous year. Tourism receipts for the period January to August 2007 rose by 30.4 per cent to reach Rs25,909 million compared to Rs19,863 million recorded over the corresponding period of the previous year.

The Central Statistics Office conducted a new Household Budget Survey from July 2006 to June 2007 to update the basket of goods and services used for the computation of the Consumer Price Index (CPI). The results of the survey will be available on 26 October 2007. The official CPI as from July 2007 will be based on the survey and will be released by mid-November 2007.

An estimate of the CPI for September 2007 has been made on the basis of the consumption pattern of the 2001-02 Household Budget Survey and prices collected in September 2007. The CPI is estimated to

have increased from 141.3 in August 2007 to 142.8 in September 2007. The rate of inflation for the twelve-month period ended September 2007 is estimated at 10.0 per cent, down from the estimate of 10.3 per cent in August 2007.

With an estimate of 10.0 per cent for headline inflation for September 2007, CORE1, CORE2 and TRIM10 inflation rates are estimated at 6.5 per cent, 6.8 per cent and 7.2 per cent, respectively. Consequently, for September 2007, core inflation was between 2.8 and 3.5 percentage points lower than the headline inflation.

Net foreign assets of depository corporations expanded by Rs3,625 million or 4.4 per cent, from Rs83,162 million at the end of June 2007 to Rs86,787 million at the end of August 2007, on account of the increase in net foreign assets of other depository corporations offsetting the fall in those of the Bank of Mauritius. Net foreign assets of other depository corporations grew by Rs3,931 million or 12.7 per cent to Rs34,870 million while those of the Bank of Mauritius fell by Rs305 million or 0.6 per cent to Rs51,918 million. Claims on non-residents rose by Rs22,266 million or 7.0 per cent, from Rs319,995 million at the end of June 2007 to Rs342,261 million at the end of August 2007. Liabilities to non-residents increased by Rs18,641 million or 7.9 per cent, from Rs236,833 million at the end of June 2007 to Rs255,474 million at the end of August 2007.

Domestic claims of depository corporations, excluding claims on GBL holders, went up by Rs1,671 million or 0.8 per cent, from Rs210,443 million at the end of June 2007 to Rs212,114 million at the end of August 2007. Net claims on budgetary central Government dropped by Rs545 million or 1.3 per cent, from Rs42,235 million at the end of June 2007 to Rs41,690 million at the end of August 2007. Claims on other sectors, that is, credit to the private sector grew by Rs2,218 million or 1.3 per cent to Rs170,425 million in August 2007.

Net claims on budgetary central Government from the Bank of Mauritius contracted by Rs179 million or 12.6 per cent, from negative Rs1,417 million at the end of June 2007 to negative Rs1,596 million at the end of August 2007. Net claims on budgetary central Government from other depository corporations fell by Rs367 million or 0.8 per cent, from Rs43,653 million to Rs43,286 million.

Claims on Other Sectors from the Bank of Mauritius declined by Rs60 million or 25.0 per cent, from Rs238 million at the end of June 2007 to Rs178 million at the end of August 2007 while claims on Other Sectors from other depository corporations expanded by Rs2,277 million or 1.4 per cent, from Rs167,969 million to Rs170,246 million.

Broad Money Liabilities (BML) grew by Rs4,835 million or 2.2 per cent, from Rs215,408 million at the end of June 2007 to Rs220,243 million at the end of August 2007. Of the components of BML, currency with public rose by Rs377 million or 3.2 per cent to Rs11,974 million while transferable deposits fell by Rs2,136 million or 5.1 per cent to Rs40,012 million. Savings deposits declined by Rs809 million or 1.2 per cent to Rs64,535 million while time deposits went up by Rs7,400 million or 7.8 per cent to Rs101,878 million. Securities other than shares included in broad money rose by Rs3 million or 0.2 per cent to Rs1,843 million.

The monetary base, excluding Bank of Mauritius Bills, fell by Rs614 million, or 2.6 per cent, from Rs23,841 million at the end of June 2007 to Rs23,227 million at the end of August 2007. Currency in circulation grew by Rs473 million, or 3.5 per cent, from Rs13,512 million to Rs13,985 million while liabilities to other depository corporations decreased by Rs977 million or 10.3 per cent, from Rs9,480 million to Rs8,503 million.

Broad Money Liabilities multiplier rose from 9.0 at the end of June 2007 to 9.5 at the end of August 2007, reflecting the increase in Broad Money Liabilities and the fall in the monetary base.

The Bank issued Government of Mauritius Treasury Bills/Bank of Mauritius Bills for a total nominal amount of Rs2,632 million through the Primary Market in September 2007. Between end-August and end-September 2007, the weighted average yields of the 91-day and 182-day Bills decreased from 9.10 per cent to 8.90 per cent and from 9.76 to 9.60 per cent respectively, while the weighted average yield of the 364-day Bill increased from 9.86 per cent to 9.91 per cent.

No repurchase transactions were carried out by the Bank during the month. Interbank transactions in September amounted to Rs19,377 million with a high of Rs1,355 million and a trough of Rs180 million. The weighted average overnight interbank rate for September 2007 was 8.87 per cent compared to 8.76 per cent for the previous month.

During September 2007, total transactions in Government of Mauritius Treasury/Bank of Mauritius Bills effected through primary dealers amounted to Rs973.2 million, while no trading of Treasury Bills occurred on the Stock Exchange of Mauritius. A total amount of Rs25.5 million Treasury Bills/Treasury Notes was sold over the counter to 63 individual members of the public for individual amounts ranging from the minimum of Rs100,000 to a maximum amount of Rs1.8 million.

At the monthly auction of Treasury Notes held in September 2007, a total nominal amount of Rs800 million of Treasury Notes with maturities of 2, 3, and 4 years, and with interest payable semi-annually at the rates of 10.05, 10.20, and 10.35 per cent per annum, respectively, was put on tender. Bids received for the three maturities totalled Rs1,129.9 million, of which Rs800 million was accepted. The weighted average yields on bids accepted for the 2, 3, and 4-year maturities were 10.14, 10.32 and 10.45 per cent per annum, respectively.

The first issue of Government of Mauritius Bonds for 2007-08 was undertaken on 14 September, through an auction held on 12 September 2007. Bonds with maturities of 7, 13 and 20 years for a total nominal amount of Rs1.0 billion were put on tender at coupon rates of 10.60, 10.75 and 10.90 per cent per annum respectively. Bids for the three maturities totalled Rs1,498.3 million, of which an amount of Rs1.0 billion was accepted. The weighted average yields on bids accepted were 11.46, 11.76 and 12.22 per cent per annum respectively.

Between August and September 2007, the rupee, on average, appreciated vis-à-vis the US dollar but depreciated against the euro, Pound sterling and 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, depreciated against the Euro and the Pound Sterling between August and September 2007.

At the end of August 2007, the net international reserves of the country amounted to Rs84,504 million. The end-August 2007 level of net international reserves of the country, based on the value of the import bill for fiscal year 2006-07, exclusive of the purchase of aircrafts, represented 39.5 weeks of imports, down from 39.9 weeks of imports at the end of July 2007. The gross foreign exchange reserves of the Bank of Mauritius fell from Rs52,754 million at the end of August 2007 to Rs52,271 million at the end of September 2007.