OVERVIEW

International Developments

During August 2008, the US dollar, on average, appreciated against all major currencies. Sentiment towards the US dollar, at the start of the month, was bearish. The subsequent release of some upbeat US economic data, which demonstrated more resilience than initially thought and even generated optimism about the prospects of the broader economy, raised expectations of higher US interest rates by year end. On 5 August, the US Federal Reserve at its FOMC meeting kept interest rates on hold even as other central banks were prepared to cut them and maintained its focus on quelling persistent US inflation pressures in the economy. Benefiting from this decision, the US dollar drew further support from the slide in oil prices, which raised hopes that US economic growth would pick up and inflation would subside. Moreover, expectations that economic growth in Europe and Asia might slow more sharply than in the United States combined with the release of additional data in the US showing an unexpected rise in manufacturing activity in the New York state area and an increase in industrial output and consumer confidence further supported the US currency. However, the US dollar experienced its setback from a recovery in gold and oil prices as well as concerns about the US financial system. Persistent worries that a bailout of the two US mortgage finance giants Fannie Mae and Freddie Mac could pose further risks to an already battered financial system also made investors careful about buying the US dollar. However, losses in the dollar were limited by predominating views that slowing global growth would prompt central banks outside the United States, such as the European Central Bank and the Bank of England to lower interest rates. Towards the close of the month, the US dollar managed to inch up as the release of upbeat second quarter GDP figures lifted some of the gloom over the US economy. US GDP grew at a faster 3.3 per cent annual rate in the second quarter compared with an initial estimate of 1.9 per cent, bolstered by consumer spending and exports.

The euro depreciated against the US dollar trading at an average of US$1.5001 in August 2008 compared to an average of US$1.5770 in July 2008. As expected, on 7 August 2008, the ECB, at its governing council meeting, left rates unchanged at 4.25 per cent. In his post-meeting news conference, ECB President, Jean-Claude Trichet cooled expectations for an interest rate hike by sounding a note of concern on the slowing euro zone economy. As the currency market focused on Trichet's comments on the economy, interpreting them as a sign that the central bank might less likely hike rates, the euro lost ground against the US dollar. Mounting signs that economic weakness had spread beyond the United States spurred more euro selling. The release of data showing euro zone growth contracting in the second quarter of 2008 for the first time ever further undermined the euro as it helped scotch any expectations of euro zone interest rate increases. However, short covering combined with hawkish comments by ECB Executive Board member Axel Weber, stating that talks about lower interest rates in the euro zone was premature, managed to provide some respite to the single currency. At the close of the month, the euro retreated against the US dollar on the release of upbeat US GDP, but it remained off its lows, hit after the ECB doused expectations for a rate cut.

The Pound sterling depreciated against the US dollar during August 2008, trading at an average of US$1.8942, from an average of US$1.9885 in July 2008. The Pound sterling started the month on a rather weak tone, undermined by the release of bleak UK data. The index of British manufacturing activity contracted for the third month running and at the sharpest rate in a decade to 44.3 in July 2008, the lowest since December 1998, stoking recession fears. A survey from the Chartered Institute of Purchasing and Supply also showed that British construction activity fell at a record pace in July as the credit crunch took an increasing toll on the property market. Against the background of broad weakness in the UK economy, the Bank of England, at its MPC meeting held on 7 July 2008, opted to hold interest rates unchanged at 5 per cent. The Pound maintained its downward trend against the US dollar amid growing conviction that the UK economy was stagnating after the British property market showed more signs of strain, with house prices falling in July to their lowest in two years, according to data released from Halifax, Britain's biggest mortgage lender. The Bank of England's quarterly inflation report also added pressure on the Pound as it endorsed a dovish view on interest rates given that inflation was expected to fall back dramatically below target level in two year's time while the economy would slow down sharply further. The release of the Bank of England's August meeting minutes showing a nervous Monetary Policy Committee split three ways on the direction of interest rates further undermined the British currency. The Pound ultimately closed August trading at its intra-month low of US$1.8340, a two-year trough against the US dollar, after another run of weak UK house price and retail sales data, which intensified fears of a recession. According to the Nationwide building society, British house prices fell by 1.9 per cent in August, to post their biggest annual drop since the series was introduced in 1991 while a survey from the Confederation of British Industry pointed that retail sales fell at their sharpest pace since records began in 1983.

International oil prices, on average, moved lower during August 2008 supported by a stronger US dollar and concerns about slowing world demand. NYMEX and IPE Brent settled highs of US$124.2 a barrel and US$125.1 a barrel on 01 August 2008, respectively before sliding. The Organization of Petroleum Exporting Countries, which cut its 2008 demand forecast on August 15, added that ample supplies were paving the way to building inventories.

NYMEX WTI (West Texas Intermediate crude oil) averaged US$116.7 a barrel in August 2008, down from US$133.5 a barrel in July 2008 and up from US$72.4 a barrel in August 2007. IPE Brent figures averaged US$115.2 a barrel during the month under review, down from US$134.3 a barrel in July 2008 and up from US$71.2 a barrel in August 2007.

COMEX gold futures, on average, moved down during August 2008, trading in an intra-month closing range of US$792.1/Oz-US$913.5/Oz compared to US$871.2/Oz-US$978.7/Oz in July 2008. Gold prices reached a peak of US$913.5/Oz on 01 August 2008, supported by a strong US dollar and fall in oil prices. The bullion averaged US$842.5/Oz during August 2008, compared to an average of US$934.8/Oz in July 2008.

Domestic Developments

Tourist arrivals rose by 5.1 per cent, from 77,225 in July 2007 to 81,169 in July 2008, while gross tourism receipts went up by 2.7 per cent, from Rs2,980 million in July 2007 to Rs3,059 million in July 2008. On a cumulative basis, over the period January 2008 to July 2008, tourist arrivals reached 536,927 representing an increase of 5.4 per cent over 509,338 arrivals recorded over the corresponding period of the previous year. Tourism receipts for the period January to July 2008 grew by 11.0 per cent to reach Rs25,229 million compared to Rs22,732 million recorded over the corresponding period of the previous year.

The Consumer Price Index (CPI) increased from 115.6 in July 2008 to 116.3 in August 2008. The largest rise of 2.3 per cent was noted in the Division “Restaurants and hotels” followed by “Food and non alcoholic beverages” (+1.0 per cent), “Furnishings, household equipment and routine household maintenance” (+0.8 per cent), “Education” (+0.7 per cent), “Health” (+0.6 per cent), “Housing, water, electricity, gas and other fuels” (+0.3 per cent), “Transport” (+0.3 per cent) and “Clothing and footwear” (+0.1 per cent). The divisions “Alcoholic beverages and tobacco”, “Communication” and “Miscellaneous goods and services” registered declines of 0.3 per cent, 0.2 per cent and 0.3 per cent, respectively while “Recreation and culture” recorded no change in its index. The main contributors to the rise in the index between July 2008 and August 2008 were other goods and services, which registered an increase of 0.2 index point and sugar, soft drinks, vegetables, other food products and expenditure in bars and restaurants, each registering an increase of 0.1 index point. The rate of inflation for the twelve-month period ended August 2008 stood at 9.5 per cent, up from 9.1 per cent for the twelve month period ended July 2008.

While headline inflation stood at 9.5 per cent for August 2008, CORE1, CORE2 and TRIM10 inflation rates stood at 7.8 per cent, 5.9 per cent and 5.9 per cent, respectively. Consequently, core inflation was between 1.7 and 3.6 percentage points lower than the headline inflation.

Net foreign assets of depository corporations fell by Rs2,492 million, or 3.0 per cent, from Rs83,628 million at the end of June 2008 to Rs81,136 million at the end of July 2008, on account of the decrease in both the net foreign assets of Bank of Mauritius and those of the other depository corporations. Net foreign assets of other depository corporations fell by Rs1,210 million, or 4.5 per cent, to Rs25,391 million while those of the Bank of Mauritius fell by Rs1,281 million, or 2.2 per cent, to Rs55,746 million.

Domestic claims of depository corporations, excluding claims on GBL holders, went up by Rs1,269 million, or 0.5 per cent, from Rs258,704 million at the end of June 2008 to Rs259,973 million at the end of July 2008. Net claims on budgetary central Government rose by Rs394 million, or 0.7 per cent, from Rs53,171 million at the end of June 2008 to Rs53,565 million at the end of July 2008. Claims on other sectors, that is, credit to the private sector grew by Rs876 million, or 0.4 per cent, to Rs206,408 million in July 2008.

Net claims on budgetary central Government from the Bank of Mauritius fell by Rs1,085 million, or 24.9 per cent, from negative Rs4,362 million at the end of June 2008 to negative Rs5,447 million at the end of July 2008. Net claims on budgetary central Government from other depository corporations rose by Rs1,479 million, or 2.6 per cent, from Rs57,533 million to Rs59,012 million.

Claims on Other Sectors from the Bank of Mauritius was almost unchanged at Rs135 million at the end of July 2008 while claims on Other Sectors from other depository corporations expanded by Rs876 million, or 0.4 per cent, from Rs205,398 million to Rs206,274 million.

Broad Money Liabilities (BML) rose by Rs4,176 million, or 1.7 per cent, from Rs252,175 million at the end of June 2008 to Rs256,351 million at the end of July 2008. Of the components of BML, currency with public rose by Rs84 million, or 0.7 per cent, to Rs12,999 million while transferable deposits rose by Rs705 million, or 1.3 per cent, to Rs54,102 million. Savings deposits rose by Rs103 million, or 0.1 per cent, to Rs74,001 million while time deposits went up by Rs3,295 million, or 3.0 per cent, to Rs113,722 million. Securities other than shares included in broad money fell by Rs12 million, or 0.8 per cent, to Rs1,528 million.

The monetary base fell by Rs1,044 million, or 3.8 per cent, from Rs27,328 million at the end of June 2008 to Rs26,283 million at the end of July 2008. Currency in circulation grew by Rs531 million, or 3.5 per cent, from Rs15,008 million to Rs15,539 million while liabilities to other depository corporations decreased by Rs1,512 million, or 12.7 per cent, from Rs11,933 million to Rs10,421 million.

Broad Money Liabilities multiplier rose from 9.2 at the end of June 2008 to 9.8 at the end of July 2008, reflecting a greater expansion of Broad Money Liabilities as compared to monetary base.

Effective for the monitoring period starting 15 August 2008, the minimum Cash Reserve Ratio (CRR) was raised from 4.0 per cent to 6.0 per cent while the minimum CRR that banks have to maintain on any particular day was increased from 2.0 per cent to 4.0 per cent. The Bank of Mauritius took this decision in the wake of the current high rate of monetary expansion and excess liquidity on the money market. Most banks adjusted their Prime Lending Rate by 25 basis points but left their savings deposit rate unchanged.

Following the increase in the Cash Reserve Ratio of banks, some tightness emerged in the money market whereby the Bank had to proceed with the early redemption of Bank of Mauritius Bills for an amount of Rs1.7 billion and the purchase of Government of Mauritius Treasury Bills for an amount of Rs2.3 billion by the Secondary Market Cell. The Bills were of maturities ranging between 6 and 78 days.

The Bank issued Government of Mauritius Treasury Bills for a total nominal amount of Rs2,500 million through the weekly Primary Auctions in August 2008. Between end-July and end-August 2008, the weighted average yields of the 91-day, 182-day and 364-day Bills increased from 7.38 per cent to 7.77 per cent, from 7.53 per cent to 8.32 per cent and from 8.20 per cent to 8.70 per cent respectively. During August 2008, the market preference remained skewed towards the 91-day Bills.

Transactions on the interbank money market in August 2008 amounted to Rs10,122 million with a daily average of Rs327 million, a high of Rs975 million and a trough of Rs15 million. The weighted average overnight interbank rate for August 2008 increased to 6.71 per cent from 6.48 per cent for the previous month.

During August 2008, total transactions in Government of Mauritius Treasury Bills/Bank of Mauritius Bills effected through primary dealers amounted to Rs410.2 million. There were no transactions of Bills on the Stock Exchange of Mauritius. A total amount of Rs18.85 million Treasury Bills/Treasury Notes was sold over the counter at the Bank to 39 individual members of the public for individual amounts ranging from the minimum of Rs50,000 to the maximum amount of Rs2 million.

At the monthly auction of Treasury Notes held in August 2008, a total nominal amount of Rs1,200 million of Treasury Notes with maturities of 2, 3 and 4 years, and with interest payable semi-annually at the rates of 8.25, 8.50 and 8.90 per cent per annum, respectively, were put on tender. Bids received for the three maturities totalled Rs457.8 million only. The weighted average yields on bids accepted for the 2, 3 and 4-year maturities were 8.68, 8.99 and 10.13 per cent per annum, respectively.

In August 2008, the Bank intervened on the domestic foreign exchange market and sold US$25.0 million.

Between July 2008 and August 2008, the rupee, on average appreciated vis-à-vis the euro and Pound sterling, while it depreciated against the US dollar 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 reported by banks, showed that between July and August 2008 the rupee, on average, depreciated against the US dollar but appreciated against the euro and Pound sterling.

At the end of July 2008, the net international reserves of the country amounted to Rs81,447 million. Following the release of external trade data for second quarter 2008, the end-July 2008 level of net international reserves of the country, based on the value of the import bill for fiscal year 2007-08, exclusive of the purchase of aircraft, represented 33.1 weeks of imports, down from 34.1 weeks of imports at the end of June 2008. The gross foreign exchange reserves of the Bank of Mauritius increased from Rs55,778 million at the end of July 2008 to Rs56,656 million at the end of August 2008.

Provisional estimates for the period January 2008 to June 2008 indicated that foreign direct investment (FDI) in Mauritius stood at Rs3,690 million. Investment was mainly directed to the tourism sector (Rs1,850 million), mainly under the Integrated Resorts Scheme (IRS). The main source of FDI inflows to Mauritius was the United Kingdom (Rs803 million) and United Arab Emirates (Rs500 million). Outward FDI is estimated at Rs921 million for the first six months of 2008 with significant investment destined to the tourism sector in Maldives and the Manufacturing sector in Madagascar.

Provisional estimates for 2007-08 showed that the current account of the balance of payments surged to a higher deficit of Rs21,964 million compared with Rs17,404 million in 2006-07. The deficit in the merchandise account of the balance of payments deteriorated to Rs55,272 million, from Rs38,007 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 higher net inflows of Rs12,571 million in 2007-08 compared to Rs6,212 million in 2006-07. The overall balance of payments for 2007-08, measured as the change in reserve assets excluding valuation changes, registered a surplus of Rs9,110 million.

It may be noted that data on certain components of 'Other Investment' (namely, banks' assets, banks' liabilities and other short term assets and other short term liabilities) for fiscal year 2007-08 in the Capital and Financial Account have been derived using data culled from the Depository Corporations Survey (DCS) and are not strictly comparable to data for fiscal year 2006-07, which was based on Monetary Survey.