OVERVIEW

International Developments

During December 2008, the US dollar, on average, appreciated against the Pound sterling but depreciated vis-à-vis the Japanese yen and euro. The US dollar started the month on a good note as volatile equity markets and fears of a deepening global recession led investors to seek the US currency as a haven. Extreme risk aversion and repatriation flows also supported the US currency. However, traders were reluctant to take big bets ahead of the release of key US employment report by the end of the first week of December 2008. The US dollar rose as US shares rallied, but then lost ground as investors seized on data showing that US payrolls fell by 533,000 in November 2008, the biggest monthly drop in 34 years, heightening worries about a deepening economic slowdown. The US dollar maintained its downward movement as President-elect Barack Obama's plan for massive infrastructure spending lifted global stock markets, spurring investors to reduce holdings of safe-haven dollars and take on more risk. With safe-haven demand fading and as investors began booking year-end profits following months of steady dollar buying, the US dollar remained under pressure. However, by mid-December the US dollar trimmed its losses, boosted by optimism about the US auto sector after the government said it would step in to help the troubled industry. In a historic move, on 16 December 2008 the Federal Reserve cut its target for the federal funds rate from 1.0 per cent to a range of zero to 0.25 per cent, a record low, and said that it was willing to keep rates low for an extended period. This dramatic cut diminished the US currency's yield appeal, which stayed under strain. Thin trading and position adjustments by the end of 2008 maintained the US dollar's gloom outlook at year close.

The euro appreciated against the US dollar trading at an average of US$1.3491 in December 2008 compared to an average of US$1.2720 in November 2008. The euro started the month on a weak note, trading at its intra-month low of US$1.2621 on 2 December 2008, as selling pressure on the single currency mounted amid growing expectations that slowing euro-zone inflation might lead policy makers to cut rates more aggressively. At its governing council meeting held on 4 December 2008, the European Central Bank (ECB) lowered its benchmark lending rates by 75 basis points, from 3.25 per cent to 2.50 per cent. However, trading conditions thinning ahead of year end, pushed investors towards the euro, which carried interest rates higher not only than US rates but also those in Britain, Japan and Switzerland. Implied rate spreads also moved in the euro's favour after ECB Executive Board member Juergen Stark said the bank did not have a lot of room to manoeuvre on rates after lowering them to

2.50 per cent. The single currency rose further against the US dollar after the Federal Reserve's dramatic interest rate cut, trading at its intra-month high of US$1.4431 on 18 December 2008. However, the euro fell sharply to session lows against the US dollar, surrendering earlier gains, as traders booked profits after the currency's rapid advance. Adding to pressure on the euro was an announcement from the ECB that it would widen its interest-rate corridor and cut the return it gave to banks for holding cash at the central bank. At the close of the month, the euro was trading at US$1.4079. According to analysts, currency trading has been mainly driven by technical factors rather than fundamentals at year end, with many players winding up for the New Year's holiday and thin market conditions adding to volatility.

The Pound Sterling depreciated against the US dollar during December 2008, trading at an average of US$1.4928, from an average of US$1.5335 in November 2008. The Pound started the month on a soft tone, as weak UK manufacturing and mortgage data raised the stakes for a bold Bank of England interest rate cut. The Pound lost ground further after the Bank of England slashed its policy rate as expected by 1 percentage point to 2 per cent, at its MPC meeting held on 3-4 December 2008, in order to shore up the faltering UK economy. In a statement accompanying its interest rate decision, the BoE warned that the economic downturn had gathered pace, raising hopes for the central bank to deliver more cuts to prop up confidence in the UK economy. The Pound continued its downward trend, as figures showed a steeper-than-expected decline in manufacturing and industrial production for October 2008, while another hefty monthly trade gap showed that UK exporters were not benefiting from sterling's sharp depreciation. Nonetheless, the Pound managed to recoup some of its losses, as some traders crept back into the UK currency following a deep sell-off. However the gain was short lived as sterling fell broadly as weak UK December retail sales data and dovish Bank of England meeting minutes fed expectations of more aggressive monetary easing after the US Federal Reserve cut rates to near zero. Heavy selling of the Pound accelerated after Bank of England deputy governor Charles Bean said rates could fall "all the way to near zero" from 2 per cent now and that further capital injections into UK banks might be required. The Pound moved further down against the US dollar as data showed that the UK economy contracted by 0.6 per cent, more than the 0.5 per cent expected in the third quarter of 2008, the biggest quarterly decline since 1990, reinforcing views of a deepening recession and prospects for further aggressive monetary easing. Moreover, the Royal Institution of Chartered Surveyors expecting UK house prices to fall by 10 per cent next year and a Chartered Institute of Personnel and Development report showing that 600,000 UK jobs could also be lost in 2009 due to the recession added to further gloom about the UK economy. At the close of the month, overall sentiment towards the Pound sterling still remained negative, with illiquid trading conditions as the year drew to a close exaggerating movements.

The Japanese yen appreciated against the US dollar, trading at an average of ¥91.27 per US dollar during December 2008 compared to an average of ¥96.91 per US dollar in November 2008. The yen rose sharply, as falling stock prices and persistent worries about a deepening global downturn prompted investors to keep unwinding riskier position.

International oil prices, on average, continued to fall during December 2008, amid ongoing fears of declining global demand in the wake of deepening economic recession. NYMEX and IPE Brent both started the December 2008 trading at intra-month highs of US$49.3 a barrel and US$48.0 a barrel, respectively before sliding throughout the month. At its meeting on 17 December 2008 in Oran, Algeria, OPEC made the expected decision to cut output by around 4.2 million barrels per day due to global economic downturn. The next OPEC meeting will be held in Vienna, Austria, on 15 March 2009. The U.S Energy Information Administration projects that there will virtually be no growth in the US oil consumption in 2009, reflecting the combined effect of recently enacted Corporate Average Fuel Economy (CAFE) standards, requirements for increased use of renewable fuels, and an assumed rebound in oil prices as the world economy recovers.

NYMEX WTI (West Texas Intermediate crude oil) averaged US$42.1 a barrel in December 2008, down from US$57.4 a barrel in November 2008 and US$91.9 a barrel in December 2007. IPE Brent figures averaged US$43.0 a barrel during the month under review, down from US$54.9 a barrel in November 2008 and US$91.6 a barrel in December 2007.

COMEX gold futures, on average, moved up during the month of December 2008, trading in an intra-month closing range of US$752.2/Oz-US$884.3/Oz compared to US$705.0/Oz-US$819.5/Oz in November 2008. Gold prices reached a peak of US$884.3 on 31 December 2008, supported by a fall in oil prices. The bullion averaged US$824.1/Oz during December 2008, compared to an average of US$755.9/Oz in November 2008.

Domestic Developments

In the December 2008 issue of its National Accounts Estimates, the Central Statistics Office revised the growth rate of the Mauritian economy to 5.2 per cent for 2008, lower than the forecast of 5.6 per cent made in September 2008, mainly on account of lower growths in “Textile manufacturing” and “Hotels and restaurants” that were partly offset by a higher growth in “Financial intermediation”. The main contributors to economic growth in 2008 were “Financial intermediation”, “Transport, storage and communications”, “Real estate, renting and business activities”, “Construction” and “Wholesale and retail trade, and repairs” with respective growth rates of 10.1 per cent, 7.2 per cent, 7.6 per cent, 11.0 per cent and 4.6 per cent.

Gross Domestic Fixed Capital Formation (GDFCF) grew by 3.0 per cent in 2008 lower than the 8.6 per cent growth in 2007. Private sector GDFCF expanded by 9.2 per cent, lower than the high growth of 24.0 per cent registered in 2007, while public sector GDFCF contracted by a further 19.2 per cent in 2008 from a contraction of 24.7 per cent in 2007. The investment rate, defined as the ratio of GDFCF to GDP at market prices, decreased to 24.6 per cent in 2008 from 25.1 per cent in 2007.

On the basis of information gathered on key sectors of the economy and taking into consideration measures announced in the stimulus package by Government to cushion the adverse effects of the international financial and economic crisis on the domestic economy, economic growth for 2009 is forecast at around 4.0 per cent. In the agricultural sector, sugar production is estimated at 500,000 tonnes (from 460,000 tonnes in 2008) coupled with increased exports of refined sugar. The manufacturing sector is forecast to grow by 2.1 per cent compared to 1.8 per cent in 2008 while the construction sector is expected to grow at a lower rate of 2.5 per cent as against 11.0 per cent in 2008. Tourist arrivals are forecast at 935,000, unchanged from 2008 while “Transport, storage and communications”, “Financial intermediation” and “Business activities” are projected to record lower growth rates of 6.0 per cent, 6.5 per cent and 8.0 per cent, respectively.

Tourists arrivals declined by 2.4 per cent, from 77,236 in November 2007 to 75,380 in November 2008, while gross tourism receipts went down by 26.9 per cent, from Rs4,041 million in November 2007 to Rs2,955 million in November 2008. On a cumulative basis, over the period January 2008 to November 2008, tourist arrivals reached 833,068 representing an increase of 3.7 per cent over 803,301 arrivals recorded over the corresponding period of the previous year. Tourism receipts for the period January 2008 to November 2008 grew by 1.6 per cent to reach Rs36,752 million.

The Consumer Price Index (CPI) decreased from 116.5 in November 2008 to 115.5 in December 2008. The main contributors to the fall in the index between November 2008 and December 2008 were gasoline and interest on housing loans, each registering a decrease of 0.3 index point and trader's rice, milk, other food products, alcoholic beverages, diesel and motor vehicles, each registering a decrease of 0.1 index point. Increases of 0.1 index point for air tickets and other goods and services were noted. The largest decline of 2.7 per cent was noted in the Division “Transport” followed by “Housing, water, electricity, gas and other fuels” (-1.8 per cent), Food and non alcoholic beverages” (-0.7 per cent), “Alcoholic beverages and tobacco” (-0.5 per cent), “Recreation and culture” (-0.3 per cent), “Furnishings, household equipment and routine household maintenance” (-0.2 per cent), “Communication” (-0.2 per cent), “Health” (-0.1 per cent) and “Miscellaneous goods and services” (-0.1 per cent). The division “Clothing and footwear” registered an increase of 1.5 per cent while “Education” and “Restaurants andhotels” recorded no change in their indices. The rate of inflation for the twelve-month period ended December 2008 stood at 9.7 per cent, down from 9.9 per cent for the twelve-month period ended November 2008.

While headline inflation for December 2008 was 9.7 per cent, CORE1, CORE2 and TRIM10 inflation rates stood at 8.7 per cent, 6.1 per cent and 3.5 per cent, respectively.

Net foreign assets of depository corporations rose by Rs512 million, or 0.6 per cent, from Rs83,628 million at the end of June 2008 to Rs84,140 million at the end of November 2008, largely on account of the increase in the net foreign assets of the other depository corporations, offsetting the decrease in the net foreign assets of the Bank of Mauritius. Net foreign assets of other depository corporations rose by Rs4,239 million, or 15.9 per cent, to Rs30,841 million while those of the Bank of Mauritius fell by Rs3,727 million, or 6.5 per cent, to Rs53,300 million.

Domestic claims of depository corporations, excluding claims on GBL holders, rose by Rs7,529 million, or 2.9 per cent, from Rs258,704 million at the end of June 2008 to Rs266,233 million at the end of November 2008. Net claims on budgetary central Government fell by Rs6,246 million, or 11.8 per cent, from Rs53,171 million at the end of June 2008 to Rs46,925 million at the end of November 2008. Claims on other sectors, that is, credit to the private sector grew by Rs13,774 million, or 6.7 per cent, to Rs219,307 million in November 2008.

Net claims on budgetary central Government from the Bank of Mauritius fell by Rs1,738 million, or 39.8 per cent, from negative Rs4,362 million at the end of June 2008 to negative Rs6,100 million at the end of November 2008. Net claims on budgetary central Government from other depository corporations fell by Rs4,507 million, or 7.8 per cent, from Rs57,533 million to Rs53,026 million.

Claims on Other Sectors from other depository corporations expanded by Rs13,775 million, or 6.7 per cent, from Rs205,398 million to Rs219,173 million. Claims on Other Sectors from the Bank of Mauritius decreased marginally by Rs0.3 million, or 0.2 per cent to Rs134 million at the end of November 2008.

Broad Money Liabilities (BML) grew by Rs13,430 million, or 5.3 per cent, from Rs252,175 million at the end of June 2008 to Rs265,605 million at the end of November 2008. Of the components of BML, currency with public rose by Rs1,122 million, or 8.7 per cent, to Rs14,036 million while transferable deposits rose by Rs2,076 million, or 3.9 per cent, to Rs55,473 million. Savings deposits rose by Rs1,039 million, or 1.4 per cent, to Rs74,937 million while time deposits went up by Rs9,215 million, or

8.3 per cent, to Rs119,642 million. Securities other than shares included in broad money fell by Rs22 million, or 1.4 per cent, to Rs1,518 million.

The monetary base rose by Rs1,143 million, or 4.2 per cent, from Rs27,328 million at the end of June 2008 to Rs28,471 million at the end of November 2008. Currency in circulation increased by Rs1,462 million, or 9.7 per cent, from Rs15,008 million to Rs16,470 million while liabilities to other depository corporations decreased by Rs100 million, or 0.8 per cent, from Rs11,933 million to Rs11,833 million.

Broad Money Liabilities multiplier rose from 9.2 at the end of June 2008 to 9.3 at the end of November 2008, reflecting a greater expansion of Broad Money Liabilities as compared to Monetary Base.

With effect from the two-week monitoring period beginning 19 December 2008, the minimum Cash Reserve Ratio (CRR) was reduced from 5.0 per cent to 4.5 per cent and the minimum cash reserve ratio that banks have to maintain on any particular day was lowered from 4.0 per cent to 3.0 per cent. The Bank of Mauritius took this decision as part of the measures to counter the possible adverse impact of the ongoing global economic crisis on Mauritius, and to support the initiatives being taken by Government to stimulate the economy.

In December 2008, the Bank issued Government of Mauritius Treasury Bills for a total nominal amount of Rs3,258 million through the weekly Primary Auctions. Between end-November and end-December 2008, the weighted average yields of the 91-day Bills, 182-day Bills and 364-day Bills decreased from 9.27 per cent to 8.65 per cent, 9.10 per cent to 8.70 per cent and 9.43 per cent to 8.91 per cent respectively. During December 2008, the market preference remained skewed towards the 364-day Bills.

During the month, the Bank carried out three repurchase transactions for a total amount of Rs3,050 million on an auction basis for period of 7 to 21 days and the accepted rates were 9.00 per cent and 8.00 per cent following the reduction of 100 basis points in the key repo rate on 8 December 2008. Transactions on the interbank money market in December 2008 amounted to Rs12,041 million with a daily average of Rs388 million, a high of Rs1,549 million and a trough of Rs19 million. The weighted average overnight interbank rate for December 2008 decreased to 7.23 per cent, from 8.87 per cent for the previous month.

Bills traded by primary dealers amounted to Rs342.3 million. There were no transactions of Bills on the Stock Exchange of Mauritius. A total amount of Rs29.1 million Treasury Bills/Treasury Notes was sold over the counter at the Bank to 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 December 2008, a total nominal amount of Rs1,500 million of Treasury Notes with maturities of 2, 3 and 4 years, with interest payable semi-annually at the rates of 8.25, 8.50 and 8.75 per cent per annum, respectively, were put on tender. Bids received for the three maturities totalled Rs2,970.6 million. The weighted average yields on bids accepted for the 2, 3 and 4-year maturities were 9.45, 9.48 and 10.20 per cent per annum, respectively. The market preference shifted towards the 3-year Note.

The third issue of Five-Year Government of Mauritius Bonds for fiscal year 2008-2009 was undertaken on 19 December 2008, through an auction held on 17 December 2008. Bonds for a total nominal amount of Rs1,000 million were put on tender. Bids for a total nominal amount of Rs1,243.5 million were received, of which an amount of Rs1,000 million was accepted. The weighted average yield on bids accepted was 10.40 per cent per annum and the coupon rate was set at 10.33 per cent per annum.

The Bank introduced effective 20 December 2008 a Special Foreign Currency Line of Credit aggregating US$125 million to be made available to banks to enable them to continue their banking operations in the event of non-availability or inadequacy of foreign exchange credit facilities from their usual sources. This facility will be provided to banks in US$ against their holdings of Government of Mauritius and Bank of Mauritius securities, for a period of three months on a roll-over basis.

Between November 2008 and December 2008, the rupee, on average appreciated vis-à-vis the Pound sterling, but depreciated against the euro, Japanese yen and US dollar. The weighted average dealt selling rates of the rupee against the US dollar, Euro and Pound sterling, 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 November and December 2008 the rupee, on average, appreciated against the US dollar and the Pound sterling but depreciated against the Euro.

At the end of November 2008, the net international reserves of the country stood at Rs84,763 million, which based on the value of the import bill for the fiscal year 2007-08 and exclusive of the purchase of aircraft, represented 34.4 weeks of the imports, down from 35.3 weeks of imports at the end of October 2008. The gross foreign exchange reserves of the Bank of Mauritius increased from Rs53,333 million at the end of November 2008 to Rs56,060 million at the end of December 2008