O V E R V I E W

International Developments

During June 2008, the US dollar, on average appreciated against the euro and the Japanese yen but depreciated against the Pound sterling. At the beginning of the month, the US dollar drew support from Federal Reserve Chairman Ben Bernanke’s rare warning in his address in Spain that the weak US currency posed a risk to inflation. His comments were seen by some market participants as the Fed's version of a "strong dollar policy" and added to views the central bank could raise interest rates later this year. However, the positive note proved to be temporary after an unexpected surge in the May 2008 US jobless rate to 5.5 per cent, the highest since October 2004, which revived fears of a deeper and more prolonged economic downturn, thereby diminishing prospects of any interest rate hikes by year-end. Pressure on the US currency was also added by the jump in oil prices to record highs of over $138 per barrel. Renewed comments from the Federal Reserve Chairman that the latest surge in energy prices was adding to the dangers from inflation and that the risk of a substantial downturn in the US economy has receded, convinced market players that rate hikes could come this year, thereby resulting in broad US dollar gains. In addition, Dallas Federal Reserve President Richard Fisher said that a weak dollar was adding to inflation, while US Treasury Secretary Henry Paulson reiterated his stance that he would not rule out intervention to boost the dollar. The renewed surge in oil prices briefly weighed on the US dollar, which managed to pick up thereafter on the release of a surprisingly strong gain in US retail sales in May 2008 and as consumers used government rebate checks to support spending at a time of high gas prices and falling housing prices. An unexpectedly steep contraction in New York state manufacturing and a $2.8 billion quarterly loss from investment bank Lehman Brothers Inc, however, undermined the US dollar as investors believed weakness in the credit and lending system would make the Fed less likely to withdraw liquidity from the banking system by tightening monetary policy. The US dollar depreciated further as a plunge in US consumer confidence and declining home prices raised doubts about the Federal Reserve's ability to hike interest rates to stem inflation. At its two day meeting held on 24-25 June, the Fed held its benchmark rate steady at 2.0 per cent and expressed worries about upside risks to inflation, although it also expected price pressures to moderate this year. Towards the close of the month, the dollar extended its losses after oil prices surged to new record high of $140, data showed US consumer sentiment hit a 28-year low and Wall Street stocks extended their slide.

The euro depreciated against the US dollar trading at an average of US$1.5552 during June 2008 compared to an average of US$1.5557 in May 2008. The euro started the month on a rather weak note after a report showed that German retail sales in April 2008 fell for the second month in a row. However, the euro surged after European Central Bank (ECB) President, Jean-Claude Trichet, signaled a July rate increase for the euro-zone to quell inflation pressures. Trichet's hawkish remarks were made following the ECB's expected decision on 5th June to leave its main lending rate unchanged at 4 per cent. The positive note proved to be temporary and the euro declined on comments from officials that suggested the ECB was not about to embark on an extended period of monetary tightening. Adding pressure on the euro, was news of a potential $46.3 billion outflow from euros to dollars as Belgium's InBev - the world's largest brewer by volume - launched a bid for Anheuser-Busch, the US maker of Budweiser and Michelob. The euro also lost ground after Irish voters rejected a treaty promoting closer European Union unity. However, market players doubted whether this would have a sustained impact on the euro since the treaty mainly concerned the strengthening of political ties and seemed to have fewer economic implications. Nonetheless, the euro managed to regain footing, supported by data that showed euro zone inflation reached a record 3.6 per cent in May and cemented expectations that the ECB would hike interest rates next month. The single currency shrugged off its gains as high energy costs soured German business sentiment and the euro zone's manufacturing and service sectors contracted, reducing the case for higher euro zone interest rates. However, towards the close of the month, expectations for a July ECB rate rise remained intact after data from Germany pointed to an increase in inflation in the euro zone's biggest economy. The ECB has repeatedly said that it might lift interest rates in July to fight inflation, thus helping to push the euro near an intra-month high of $1.5790.

The Pound sterling appreciated against the US dollar during June 2008, trading at an average of US$1.9650 from an average of US$1.9647 in May 2008. The Pound started the month on a rather weak tone, after the Chief Executive of British mortgage lender Bradford & Bingley quit, rekindling concerns about short-term prospects for the UK mortgage market. The British currency maintained its downward trend, pressurized by a surprising contraction in the UK services sector and a further fall in consumer confidence which underlined continuing weakness in the economy. The Bank of England (BOE), as expected, at its MPC meeting held on 5 June 2008, left its key repo rate on hold at 5 per cent. The Pound lost further ground after the Halifax UK House Price Index fell more than expected in May. However, the Pound managed to regain momentum after UK factory gate inflation hit a record in May, highlighting the BOE's dilemma as it struggled with inflation and slowing economic growth. The British currency drew further support from prospects that the UK inflation figures would bolster the case for higher interest rates. However, the Pound could not hold on to its gains after the BOE stated it was uncertain about the path to take to get British inflation back on track following higher than expected inflation data. Minutes from the last policy meeting showed that some members considered hiking rates, while one of them argued for a cut. But with the members eventually voting to keep borrowing costs at 5 per cent, as deteriorating inflation outlook ruled out the case for an immediate rate cut, added to the Pound’s woes. However, the release of strong May 2008 British retail sales data prompted some speculation that the economic outlook might not be as gloomy as previously thought, rekindling expectations that the BOE might raise interest rates and the British currency closed the month at its intra-month high of US$1.9932.

The Japanese yen depreciated against the US dollar, trading at an average of ¥106.91 per US dollar during June 2008 compared to an average of ¥104.20 per US dollar during May 2008. The yen slid broadly prompting some market players to sell the low-yielding yen for higher-yielding currencies in the carry trade. It fell further after a Japanese government survey of large manufacturers showed that sentiment deteriorated in the second quarter.

Oil prices moved higher during June 2008, mainly supported by supply disruptions in Nigeria and Iran's dispute with the West. US dollar weakness and slumping stock markets also partly supported oil prices upwards. NYMEX and IPE Brent settled record highs of US$140.2 a barrel and US$140.3 a barrel on 27 June 2008, respectively. The Energy Information Administration (EIA) indicated that crude oil stockpiles were down 1.2 million barrels to 301 million barrels, less of a decline than was expected. EIA indicated that global oil demand will rise by 800,000 barrels per day (bpd) this year, 230,000 bpd less than its previous forecast.

NYMEX WTI (West Texas Intermediate crude oil) averaged US$134.0 a barrel in June 2008, up from US$125.5 a barrel in May 2008 and US$67.6 a barrel in June 2007. IPE Brent figures averaged US$133.8 a barrel during the month under review, up from US$124.6 a barrel in May 2008 and US$70.5 a barrel in June 2007.

COMEX gold futures, on average, moved up during June 2008, trading in an intra-month closing range of US$865.0/Oz–US$931.3/Oz compared to US$850.9/Oz–US$928.6/Oz in May 2008. Gold prices reached a peak of US$931.3/Oz on 27 June 2008, supported by a weak US dollar and high oil prices. The bullion averaged US$892.1/Oz during June 2008, compared to an average of US$891.3/Oz in May 2008.

Domestic Developments

In the June 2008 issue of its National Accounts Estimates, the Central Statistics Office has maintained the real growth rate of the economy for 2007 at 5.4 per cent. Exclusive of sugar, the growth of the economy is estimated at 6.1 per cent. The main contributors to growth in 2007 were the "Construction", "Hotels and restaurants", "Transport, storage and communications", "Real estate, renting and business activities" and "Financial Intermediation" industry groups, which grew by 15.2 per cent, 14.0 per cent, 7.8 per cent, 7.6 per cent and 7.5 per cent, respectively. The manufacturing sector grew by 2.2 per cent, which is the combined effect of growths of 4.0 per cent and 8.5 per cent in food (excluding sugar) and textile respectively and contractions of 13.6 per cent and 3.1 per cent in sugar and other manufacturing, respectively. It is worth noting that activities of Export Oriented Enterprises, comprising of enterprises involved in manufacturing activities for export in addition to enterprises manufacturing goods for export and holding a registration certificate issued by the Board of Investment, grew at a higher rate of 8.0 per cent compared to a growth of 4.6 per cent in 2006.

Gross Domestic Fixed Capital Formation (GDFCF) grew, in real terms, by 8.6 per cent in 2007. Exclusive of aircrafts, GDFCF grew by 17.0 per cent compared to 5.5 per cent in 2006. The investment rate, as measured by the ratio of GDFCF to GDP at market prices, went up from 24.3 per cent in 2006 to 25.1 per cent in 2007. Excluding purchase of aircrafts, it increased from 21.5 per cent in 2006 to 24.1 per cent in 2007. Private sector GDFCF grew, in real terms, by 24.0 per cent while public sector GDFCF declined by 24.7 per cent in 2007 after a high growth 28.3 per cent in 2006. The savings rate, as measured by the ratio of Gross National Saving to GDP at market prices, rose to 21.3 per cent in 2007 from 17.1 per cent in 2006.

For 2008, the growth forecast has been revised downwards to 5.7 per cent from the earlier forecast of 6.0 per cent, mainly due to an expected lower sugar production of 455,000 tonnes compared to the previous estimate of 520,000 tonnes. Exclusive of sugar, the growth rate would be around 5.8 per cent compared with the previous estimate of 5.6 per cent.

Tourist arrivals rose by 3.7 per cent, from 65,301 in May 2007 to 67,705 in May 2008, while gross tourism receipts went up by 18.9 per cent, from Rs2,970 million in May 2007 to Rs3,530 million in May 2008. On a cumulative basis, over the period July 2007 to May 2008, tourist arrivals reached 876,894 representing an increase of 8.6 per cent over 807,668 arrivals recorded over the corresponding period of the previous fiscal year. Tourism receipts for the period July 2007 to May 2008 grew by 19.1 per cent to reach Rs40,156 million compared to Rs33,720 million recorded over the corresponding period of the previous fiscal year.

The Consumer Price Index (CPI) increased from 113.0 in May 2008 to 113.4 in June 2008. The largest rise of 1.1 per cent was noted in the Division “Food and non alcoholic beverages” followed by “Miscellaneous goods and services” (+1.0 per cent), “Furnishings, household equipment and routine household maintenance” (+0.6 per cent), “Transport” (+0.2 per cent), “Restaurants and hotels” (+0.2 per cent) and “Housing, water, electricity, gas and other fuels” (+0.1 per cent). The divisions “Communication”, “Recreation and culture”, “Alcoholic beverages and tobacco” and “Health” registered declines of 0.3 per cent, 0.2 per cent, 0.1 per cent and 0.1 per cent, respectively, while “Clothing and footwear” and “Education” recorded no change in their indices. The main contributors to the rise in the index between May 2008 and June 2008 were trader's rice which registered an increase of 0.3 index point, and vegetables, other food products and other goods and services, each registering an increase of 0.1 index point. A drop of 0.1 index point for fruits and telephone services was noted. The rate of inflation for fiscal year 2007-08 stood at 8.8 per cent, unchanged from the previous month

With headline inflation at 8.8 per cent for June 2008, CORE1, CORE2 and TRIM10 inflation rates stood at 6.6 per cent, 5.5 per cent and 6.5 per cent, respectively. Consequently, for June 2008, core inflation was between 2.2 and 3.3 percentage points lower than the headline inflation.

Net foreign assets of depository corporations rose by Rs4,078 million, or 4.9 per cent, from Rs83,162 million at the end of June 2007 to Rs87,240 million at the end of May 2008, on account of the increase in the net foreign assets of Bank of Mauritius offsetting the decrease in those of the other depository corporations. Net foreign assets of other depository corporations fell by Rs1,474 million, or 4.8 per cent, to Rs29,465 million while those of the Bank of Mauritius rose by Rs5,552 million, or 10.6 per cent, to Rs57,775 million.

Domestic claims of depository corporations, excluding claims on GBL holders, went up by Rs39,695 million, or 18.9 per cent, from Rs210,443 million at the end of June 2007 to Rs250,138 million at the end of May 2008. Net claims on budgetary central Government rose by Rs8,686 million, or 20.6 per cent, from Rs42,235 million at the end of June 2007 to Rs50,921 million at the end of May 2008. Claims on other sectors, that is, credit to the private sector grew by Rs31,009 million, or 18.4 per cent, to Rs199,216 million in May 2008.

Net claims on budgetary central Government from the Bank of Mauritius fell by Rs1,601 million, or 112.9 per cent, from negative Rs1,417 million at the end of June 2007 to negative Rs3,018 million at the end of May 2008. Net claims on budgetary central Government from other depository corporations rose by Rs10,286 million, or 23.6 per cent, from Rs43,653 million to Rs53,939 million.

Claims on Other Sectors from the Bank of Mauritius fell by Rs102 million or 42.9 per cent, from Rs238 million at the end of June 2007 to Rs136 million at the end of May 2008 while claims on Other Sectors from other depository corporations expanded by Rs31,111 million, or 18.5 per cent, from Rs167,969 million to Rs199,080 million.

Broad Money Liabilities (BML) grew by Rs33,801 million, or 15.7 per cent, from Rs215,408 million at the end of June 2007 to Rs249,209 million at the end of May 2008. Of the components of BML, currency with public rose by Rs1,199 million, or 10.3 per cent, to Rs12,797 million while transferable deposits rose by Rs8,852 million, or 21.0 per cent, to Rs51,001 million. Savings deposits rose by Rs6,345 million, or 9.7 per cent, to Rs71,689 million while time deposits went up by Rs17,721 million, or 18.8 per cent, to Rs112,199 million. Securities other than shares included in broad money fell by Rs317 million, or 17.2 per cent, to Rs1,523 million.

The monetary base rose by Rs784 million, or 3.3 per cent, from Rs23,841 million at the end of June 2007 to Rs24,625 million at the end of May 2008. Currency in circulation grew by Rs1,554 million, or 11.5 per cent, from Rs13,512 million to Rs15,066 million while liabilities to other depository corporations decreased by Rs219 million, or 2.3 per cent, from Rs9,480 million to Rs9,261 million.

Broad Money Liabilities multiplier rose from 9.0 at the end of June 2007 to 10.1 at the end of May 2008, reflecting a greater expansion of Broad Money Liabilities as compared to monetary base.

With a view to manage the excess liquidity in the Rupee market, the Bank issued during the month, 56-day BOM Bills for a total nominal amount of Rs600 million at a fixed rate of 7.15 per cent per annum.

The Bank issued Government of Mauritius Treasury Bills for a total nominal amount of Rs9,100 million through the weekly Primary Auctions in June 2008. Between end-May and end-June 2008, the weighted average yields of the 91-day, 182-day and 364-day Bills increased from 7.22 per cent to 7.39 per cent, from 7.11 per cent to 7.74 per cent and from 7.46 per cent to 7.58 per cent, respectively. During June 2008, the market preference remained skewed towards the 91-day Bills.

Transactions on the interbank money market in June 2008 amounted to Rs9,849 million with a high of Rs1,014 million and a trough of Rs79 million. The weighted average overnight interbank rate for June 2008 was 6.43 per cent compared to 6.56 per cent for the previous month.

During June 2008, total transactions in Government of Mauritius Treasury Bills/Bank of Mauritius Bills effected through primary dealers amounted to Rs187.5 million. There were no transactions of Bills on the Stock Exchange of Mauritius. A total amount of Rs14.55 million Treasury Bills/Treasury Notes was sold over the counter at the Bank to 30 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 June 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 7.80, 8.20 and 8.50 per cent per annum, respectively, were put on tender. Bids received for the three maturities totalled Rs180.1 million only. The weighted average yields on bids accepted for the 2, 3, and 4-year maturities were 7.75, 7.92 and 8.72 per cent per annum, respectively.

In June 2008, the Bank intervened on the domestic foreign exchange market and sold US$15.0 million.

Between May 2008 and June 2008, the rupee, on average appreciated vis-à-vis the Japanese yen but depreciated against the Pound sterling, euro and US dollar. 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 May and June 2008 the rupee, on average, appreciated against the US dollar and the euro but depreciated against the Pound sterling.

At the end of May 2008, the net international reserves of the country amounted to Rs 87,563 million. The end-May 2008 level of net international reserves of the country, based on the value of the import bill for calendar year 2007, exclusive of the purchase of aircraft, represented 38.5 weeks of imports, up from 35.6 weeks of imports at the end of April 2008. The gross foreign exchange reserves of the Bank of Mauritius decreased from Rs57,872 million at the end of May 2008 to Rs57,059 million at the end of June 2008.