OVERVIEW

International Developments

During May 2008, the US dollar, on average, appreciated vis-à-vis all the major trading currencies. The US dollar started the month on a good note amid market sentiment that the US Federal Reserve might keep rates on hold for a while. Moreover, reports showing manufacturing activity shrinking by less than expected in April and a surprisingly big rise in consumer spending assuaged investor worries about the depths of the US economy's troubles. News that the US economy shed only 20,000 jobs in April also supported views that the Federal Reserve would refrain from cutting interest rates again, provided economic data and financial markets conditions did not deteriorate further. Furthermore, the release of stronger-than-expected US April retail sales data and a government report showing a slight rise in US import prices, which pointed to growing inflationary pressures, managed to provide support to the US currency. Nagging doubts on whether the US economy would be able to cope without further policy easing, however, resurfaced on the market with the release of additional weak data. Factory activity in the US mid-Atlantic region shrank for a sixth straight month in May, while manufacturing in New York State also declined, according to reports by regional Federal Reserve banks. The dollar further lost ground after the Reuters/University of Michigan index of consumer confidence dropped to 59.5 in May, the lowest level since June 1980, thereby highlighting the threat to economic growth. Adding to the US dollar's woes was the rise in oil prices reaching record highs of US$130 a barrel and a surge in gold prices. Furthermore, the Federal Reserve cut its 2008 growth estimate to a meagre 0.3-1.2 per cent range from its initial forecast of 1.3-2.0 per cent made three months ago and warned against risks of higher unemployment, reducing prospects of an interest rate hike later this year. News that the stock of unsold US houses reached a record high in April, thereby indicating that the housing market rout was far from over, also weighed on the US dollar. Towards the close of the month, the US dollar managed to recover, benefiting from the release of US April 2008 durable goods orders, which fell by less than expected, while orders, excluding transportation equipment, rose by 2.5 per cent, the biggest gain since July. The data further underscored market expectations for the Federal Reserve to keep interest rates on hold or even raise them by year-end. Demand for US dollar gained ground after the US government said that the US economy grew at an upwardly revised 0.9 per cent pace in the first quarter, slightly better than previously estimated and as hawkish comments from Federal Reserve officials boosted expectations for an interest rate increase this year.

The euro depreciated against the US dollar trading at an average of US$1.5557 during May 2008 compared to an average of US$1.5761 in April 2008, affected by a run of weak sentiment data from the euro zone and rising inflation risks. The single European currency started the month on a weak tone, undermined by the release of euro zone's consumer prices, which rose by 3.3 per cent in the 12 months to April 2008, which though being below the prior month's reading remained still well above the ECB's target of 2 per cent. The euro extended losses against the US dollar after weak euro zone retail sales data raised concerns about downside risks to the region's economy. However, the euro rebounded after the European Central Bank left interest rates unchanged on 8 May 2008 and its President focused more on inflation than some had expected. ECB President Jean-Claude Trichet mentioned that inflation remained his top concern, signalling that the bank would not cut interest rates anytime soon. He stressed that high energy and food costs meant that the euro zone still faced "a protracted period" of high inflation and the currency zone was proving vulnerable to fallout from the global credit crisis. Sentiment toward the euro soured after a rights issue from France's Credit Agricole when it reported write-downs related to the US subprime mortgage sector. This indicated that the euro zone was not immune to the problems in the United States and analysts were convinced that growing signs of a slowdown in economic activity in the euro area might force the ECB to cut interest rates at some point this year. The European currency, however managed to recover after strong first-quarter growth data in Germany and France highlighted the relative strength of the European economy. But the positive tone proved to be temporary as the single currency lost ground after French business confidence slumped to a 2-1/2 year low in May and the forward-looking German GfK index pointed to an unexpected deterioration in consumer sentiment in June. The euro extended its losses vis-à-vis the US dollar, hampered by figures showing the first rise in Germany's seasonally adjusted jobless total in over two years, adding to concerns that the region's economy was also slowing down. Other data in Europe showing the outflow of investment from the euro zone accelerating in March further weighed on the single currency. The data supported expectations for the ECB to retain its hawkish, inflation-fighting stance despite signs of an economic slowdown seen in recent sentiment surveys from euro zone member states.

The Pound sterling depreciated against the US dollar during May 2008, trading at an average of US$1.9647 from an average of US$1.9803 in April 2008. The Pound, which started the month on a rather firm note, weakened after data showed that the UK service sector stagnated in April, providing further evidence that the credit crunch was biting into economy growth and raised the chance of another interest rate cut. The British currency slid further amid more data releases that underscored weak consumer morale, output and job figures, thereby keeping investors focused on a sharply slowing UK economy and the prospect of further UK interest rate cuts. Yet, the Bank of England (BOE) Monetary Policy Committee, as expected, at the end of its two-day meeting on 8 May 2008, faced with rising inflation and a sharp economic slowdown, held its key Repo Rate at 5 per cent. But a spate of poor British data from housing to retail sales left analysts convinced that a cut was likely next month, potentially eroding the Pound's yield appeal. The Pound, however, managed to recoup some of its losses after robust UK wholesale inflation data prompted investors to pare back expectations on how far the Bank of England might cut interest rates this year. Yet a surge in British consumer prices underlining concerns that high inflation was further choking an already limp economy moved the Pound further down. British consumer prices surged 0.8 per cent in April from March, far exceeding expectations for a 0.5 per cent rise, and taking annual inflation to 3.0 per cent. The Pound remained under selling pressure as investors grew worried by the combination of high inflation and slowing growth in the UK economy. The BOE, in its quarterly inflation report, delivered a bearish prognosis on British economic prospects, stating that inflation was set to remain stubbornly high in the coming months, limiting the central bank's ability to act to bolster an ailing economy with interest rate cuts. The British currency, however managed to regain its footing, reaching its intra-month high of US$1.9819 on 26 May 2008 after a smaller-than-expected fall in UK retail sales, driven by purchases of computer games, kept any prospect of near-term monetary easing at bay. At the close of the month, the Pound had shrugged off some of its gains as investors' concerns about surging inflation and slowing growth in the UK resurfaced and the release of data showing a record fall in UK house prices added to the view that the economy might continue to weaken.

The Japanese yen depreciated against the US dollar, trading at an average of ¥104.20 per US dollar during May 2008 compared to an average of ¥100.52 per US dollar during April 2008. The yen lost ground, undermined by a fall in Tokyo stocks which prompted investors to unwind risky carry trades.

Oil prices moved higher during May 2008 against the backdrop of a weak US dollar, concerns that the global demand could further strain supplies and market expectations that prices would rise further. Oil production disruptions in Nigeria also pressured prices upwards. NYMEX and IPE Brent settled record highs of US$133.2 a barrel and US$132.7 a barrel, respectively, on 21 May 2008. According to the latest Oil Market Report from the International Energy Agency, world oil demand will rise by less than expected in 2008 because of record prices and slower growth in the United States and elsewhere. The IEA said that consumption will rise by 1.03 million barrels per day, 230,000 barrels per day less than the previous forecast. The next OPEC meeting will be convened in Vienna, Austria, on September 9, 2008.

NYMEX WTI (West Texas Intermediate crude oil) averaged US$125.5 a barrel in May 2008, up from US$112.5 a barrel in April 2008 and US$63.5 a barrel in May 2007. IPE Brent figures averaged US$124.6 a barrel during the month under review, up from US$110.4 a barrel in April 2008 and US$67.8 a barrel in May 2007.

COMEX gold futures, on average, moved down during May 2008, trading in an intra-month closing range of US$850.9/Oz-US$928.6/Oz compared to US$865.1/Oz-US$948.3/Oz in April 2008. Gold prices reached a peak of US$928.6/Oz on 21 May 2008, supported by a weak US dollar and high oil prices. The bullion averaged US$891.3/Oz during May 2008, compared to an average of US$913.1/Oz in April 2008.

Domestic Developments

Tourist arrivals rose by 3.6 per cent, from 70,297 in April 2007 to 72,837 in April 2008, while gross tourism receipts went up by 7.8 per cent, from Rs3,468 million in April 2007 to Rs3,740 million in April 2008. On a cumulative basis, over the period July 2007 to April 2008, tourist arrivals reached 809,189, representing an increase of 9.0 per cent over the 742,367 arrivals recorded over the corresponding period of the previous fiscal year. Tourism receipts for the period July 2007 to April 2008 grew by 19.1 per cent to reach Rs36,626 million compared to Rs30,750 million recorded over the corresponding period of the previous fiscal year.

The Consumer Price Index (CPI) increased from 111.9 in April 2008 to 113.0 in May 2008. The largest rise of 3.1 per cent was noted in the Division "Transport" followed by "Miscellaneous goods and services" (+1.8 per cent), "Alcoholic beverages and tobacco" (+1.5 per cent), "Food and non alcoholic beverages" (+1.3 per cent), "Restaurants and hotels" (+0.9 per cent) and "Clothing and footwear" (+0.3 per cent). The divisions "Housing, water, electricity, gas and other fuels", "Furnishings, household equipment and routine household maintenance" and "Communication" registered declines of 0.9 per cent, 0.3 per cent and 0.3 per cent, respectively, while "Health", "Recreation and culture" and "Education" recorded no change in their indices. The main contributors to the rise in the index between April 2008 and May 2008 were trader's rice (+0.5 index point), bus fare (+0.3 index point) and chicken, other food products, rum, air tickets, prepared food and motor vehicle's insurance, each registering an increase of 0.1 index point. A drop of 0.1 index point for powdered milk, fresh fruits and interest payment on housing loan was noted. The rate of inflation for the twelve-month period ended May 2008 stood at 8.8 per cent, down from 8.9 per cent for the twelve month period ended April 2008.

While headline inflation for May 2008 stood at 8.8 per cent, CORE1, CORE2 and TRIM10 inflation rates stood at 6.2 per cent, 5.6 per cent and 6.7 per cent, respectively. Consequently, for May 2008, core inflation was between 2.1 and 3.2 percentage points lower than the headline inflation.

Net foreign assets of depository corporations fell by Rs2,285 million, or 2.7 per cent, from Rs83,162 million at the end of June 2007 to Rs80,877 million at the end of April 2008, on account of the decrease in the net foreign assets of other depository corporations offsetting the increase in those of the Bank of Mauritius. Net foreign assets of other depository corporations fell by Rs4,595 million, or 14.9 per cent, to Rs26,344 million while those of the Bank of Mauritius rose by Rs2,311 million, or 4.4 per cent, to Rs54,533 million.

Domestic claims of depository corporations, excluding claims on GBL holders, went up by Rs29,647 million, or 14.1 per cent, from Rs210,443 million at the end of June 2007 to Rs240,090 million at the end of April 2008. Net claims on budgetary central Government rose by Rs6,662 million, or

15.8 per cent, from Rs42,235 million at the end of June 2007 to Rs48,897 million at the end of April 2008. Claims on other sectors, that is, credit to the private sector grew by Rs22,986 million, or 13.7 per cent, to Rs191,193 million in April 2008.

Net claims on budgetary central Government from the Bank of Mauritius rose by Rs390 million, or 27.6 per cent, from negative Rs1,417 million at the end of June 2007 to negative Rs1,027 million at the end of April 2008. Net claims on budgetary central Government from other depository corporations rose by Rs6,271 million, or 14.4 per cent, from Rs43,653 million to Rs49,924 million.

Claims on Other Sectors from the Bank of Mauritius fell by Rs29 million or 12.0 per cent, from Rs238 million at the end of June 2007 to Rs209 million at the end of April 2008 while claims on Other Sectors from other depository corporations expanded by Rs23,015 million, or 13.7 per cent, from Rs167,969 million to Rs190,984 million.

Broad Money Liabilities (BML) grew by Rs27,785 million, or 12.9 per cent, from Rs215,408 million at the end of June 2007 to Rs243,193 million at the end of April 2008. Of the components of BML, currency with public rose by Rs1,200 million, or 10.3 per cent, to Rs12,797 million while transferable deposits rose by Rs6,404 million, or 15.2 per cent, to Rs48,552 million. Savings deposits rose by Rs5,179 million, or 7.9 per cent, to Rs70,523 million while time deposits went up by Rs15,338 million, or 16.2 per cent, to Rs109,815 million. Securities other than shares included in broad money fell by Rs334 million, or 18.2 per cent, to Rs1,506 million.

The monetary base rose by Rs1,586 million, or 6.7 per cent, from Rs23,841 million at the end of June 2007 to Rs25,427 million at the end of April 2008. Currency in circulation grew by Rs1,644 million, or 12.2 per cent, from Rs13,512 million to Rs15,156 million while liabilities to other depository corporations increased by Rs483 million, or 5.1 per cent, from Rs9,480 million to Rs9,963 million.

Broad Money Liabilities multiplier rose from 9.0 at the end of June 2007 to 9.6 at the end of April 2008, reflecting a greater expansion of Broad Money Liabilities as compared to monetary base.

With a view to manage the excess liquidity in the domestic money market, the Bank issued during the month 28-day and 56-day BOM Bills for a total nominal amount of Rs1,400 million at fixed rates of 7.05 per cent per annum and 7.15 per cent per annum, respectively, of which Rs580 million was issued for the 28-day Bills.

The Bank issued Government of Mauritius Treasury Bills for a total nominal amount of Rs4,463 million through the Primary Market in May 2008. Between end-April and end-May 2008, the weighted average yields of the 91-day, 182-day and 364-day Bills decreased from 7.60 per cent to 7.22 per cent, from 7.67 per cent to 7.11 per cent and from 7.71 per cent to 7.46 per cent, respectively. During May 2008, market preference remained for the 91-day Bills.

Transactions on the interbank money market in May 2008 amounted to Rs11,303 million with a high of Rs750 million and a trough of Rs35 million. The weighted average overnight interbank rate for May 2008 was 6.56 per cent compared to 6.79 per cent for the previous month.

During May 2008, total transactions in Government of Mauritius Treasury Bills/Bank of Mauritius Bills effected through primary dealers amounted to Rs402.1 million. No Treasury Bills were traded on the Stock Exchange of Mauritius. A total amount of Rs26.85 million Treasury Bills/Treasury Notes was sold over the counter at the Bank to 32 individual members of the public for individual amounts ranging from a minimum of Rs50,000 to a maximum amount of Rs2 million.

At the monthly auction of Treasury Notes held in May 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 Rs2,420.9 million, out of which Rs1,200 million was accepted. The weighted average yields on bids accepted for the 2, 3 and 4-year maturities were 7.70, 7.97 and 8.69 per cent per annum, respectively.

In May 2008, the Bank intervened on the domestic foreign exchange market and sold US$30.0 million.

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 April and May 2008 the rupee, on average, depreciated against the US dollar, Euro and Pound sterling.

At the end of April 2008, the net international reserves of the country amounted to Rs 81,136 million. The end-April 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 35.6 weeks of imports, down from 35.9 weeks of imports at the end of March 2008. The gross foreign exchange reserves of the Bank of Mauritius increased from Rs 54,768 million at the end of April 2008 to Rs 57,872 million at the end of May 2008.

Between April 2008 and May 2008, the rupee, on average, depreciated vis-à-vis all the major trading partner currencies.

Provisional estimates for the period January 2008 to March 2008 indicate that foreign direct investment (FDI) in Mauritius stood at Rs1,660 million. Foreign direct investment inflows were mainly directed to the tourism sector (Rs976 million), mainly under the Integrated Resorts Scheme (IRS). The main sources of FDI inflows to Mauritius were France (Rs215 million) and United Arab Emirates (Rs210 million) Outward FDI is estimated at Rs522 million for the first three months of 2008 with significant investment destined to the tourism sector in Maldives and Seychelles and the manufacturing sector in Madagascar.

Provisional estimates for the first quarter 2008 indicate that the current account of the balance of payments recorded a deficit of Rs4,492 million as against a surplus of Rs890 million in the corresponding quarter of 2007. This was mainly due to a marked deterioration in the merchandise account of the balance of payments, which surged to Rs14,613 million in the first quarter 2008 from Rs7,542 million in the first quarter of 2007. The merchandise deficit was, however, partly offset by surpluses on the services, income and current transfers accounts. The capital and financial account, inclusive of reserve assets, recorded a net outflow of Rs11 million in the first quarter of 2008. The overall balance of payments for the first quarter of 2008, measured as the change in reserve assets excluding valuation changes, registered a surplus of Rs5,841 million.

First quarter 2008 data on certain components of 'Other Investment' (namely, banks' assets, banks' liabilities and other short term liabilities) in the Capital and Financial Account are not strictly comparable to the previous quarters because they have been derived using data culled from the Depository Corporations Survey (DCS). Preceding quarters' revised data will be eventually published in the Monthly Statistical Bulletin.