Macroeconomic and Monetary Developments

Third Quarter Review 2006-07

Reserve Bank of India
Mumbai

Contents

I.	**The Real Economy**	**1**
	Agricultural Situation	2
	Industrial Performance	4
	Services Sector	8
II.	**Fiscal Situation**	**12**
	Combined Government Finances	12
	Centre's Fiscal Situation	12
	State Finances	17
III.	**Monetary and Liquidity Conditions**	**20**
	Monetary Survey	20
	Reserve Money Survey	27
	Liquidity Management	29
IV.	**Price Situation**	**33**
	Global Inflation	33
	Global Commodity Prices	39
	Inflation Conditions in India	43
V.	**Financial Markets**	**56**
	International Financial Markets	56
	Domestic Financial Markets	59
	Money Market	60
	Foreign Exchange Market	65
	Credit Market	67
	Government Securities Market	69
	Equity Market	71
VI.	**The External Economy**	**77**
	International Developments	77
	Merchandise Trade	79
	Current Account	83
	Capital Flows	85
	Foreign Exchange Reserves	86
	External Debt	87

I. THE REAL ECONOMY

The robust performance of the Indian economy continued during the second quarter (July–September) of 2006-07. According to the Central Statistical Organisation (CSO), real gross domestic product (GDP) growth accelerated to 9.2 per cent in the second quarter from 8.9 per cent in the preceding quarter and 8.4 per cent a year ago. Strong growth in industrial activity and the services sub-sector ‘trade, hotels, restaurants, transport, storage and communication’ contributed to higher overall growth in the second quarter of 2006-07 (Table 1 and Chart 1). With both the first and second quarters of 2006-07 recording higher growth over the corresponding quarters of 2005-06, real GDP growth accelerated to 9.1 per cent in the first half of 2006-07 from 8.5 per cent a year ago.

Table 1: Growth Rates of Real GDP

(Per cent)

Sector	2000-01 to 2005-06 (Average)	2004-05*	2005-06#	2005-06				2006-07		2005-06	2006-07
				Q1	Q2	Q3	Q4	Q1	Q2	(April-September)	
1	2	3	4	5	6	7	8	9	10	11	12
1. Agriculture and Allied Activities	**2.3 (22.2)**	**0.7 (20.8)**	**3.9 (19.9)**	**3.4**	**4.0**	**2.9**	**5.5**	**3.4**	**1.7**	**3.7**	**2.6**
1.1 Agriculture	2.0	0.7	N.A.								
2. Industry	**6.2 (19.6)**	**7.4 (19.5)**	**7.6 (19.3)**	**9.5**	**6.3**	**7.0**	**7.9**	**9.7**	**10.5**	**7.9**	**10.1**
2.1 Mining and Quarrying	4.2	5.8	0.9	3.1	-2.6	0.0	3.0	3.4	3.1	0.3	3.2
2.2 Manufacturing	6.9	8.1	9.0	10.7	8.1	8.3	8.9	11.3	11.9	9.4	11.6
2.3 Electricity, Gas and Water Supply	3.8	4.3	5.3	7.4	2.6	5.0	6.1	5.4	7.7	5.0	6.5
3. Services	**8.1 (58.2)**	**10.2 (59.7)**	**10.3 (60.7)**	**10.1**	**10.3**	**9.7**	**11.0**	**10.5**	**10.7**	**10.2**	**10.6**
3.1 Trade, Hotels, Restaurants, Transport, Storage and Communication	9.9	10.6	11.5	11.7	11.0	10.2	12.9	13.2	13.9	11.4	13.5
3.2 Financing, Insurance, Real Estate and Business Services	7.1	9.2	9.7	8.8	10.5	8.9	10.5	8.9	9.5	9.6	9.2
3.3 Community, Social and Personal Services	5.8	9.2	7.8	7.3	8.0	8.4	7.6	7.4	6.9	7.7	7.2
3.4 Construction	8.9	12.5	12.1	12.4	12.3	11.5	12.0	9.5	9.8	12.4	9.7
4. Real GDP at Factor Cost	**6.4 (100)**	**7.5 (100)**	**8.4 (100)**	**8.5**	**8.4**	**7.5**	**9.3**	**8.9**	**9.2**	**8.5**	**9.1**

*: Quick Estimates. #: Revised Estimates. N.A.: Not available.

Note : 1. Figures in parentheses denote percentage shares in real GDP.
2. Q1: First Quarter (April-June); Q2: Second Quarter (July-September); Q3: Third Quarter (October-December); and Q4: Fourth Quarter (January-March).

Source : Central Statistical Organisation.

Agricultural Situation

The rainfall during the 2006 South-West monsoon season (June 1 to September 30) turned out to be close to normal, although the distribution of rainfall was uneven. The initial phase of deficiency of rainfall witnessed from the beginning of second week of June and up to July 2006 and again in mid-September was offset by excess rainfall during the first three weeks of August, especially over Central India. Furthermore, it led to improvement in reservoir position at the end of the South-West monsoon season with total live water storage at 91 per cent of the Full Reservoir Level (FRL), which was higher than the last year's position (81 per cent) and the last ten year's average (71 per cent). Cumulative rainfall during the North-East monsoon (October 1, 2006 to December 31, 2006) was, however, 21 per cent below normal as compared with 10 per cent above normal during the corresponding period of the previous year. Of the 36 meteorological sub-divisions, cumulative rainfall was deficient/ scanty/ no rain in 27 sub-divisions (19 sub-divisions during last year) (Table 2). As on January 4, 2007, the total live water storage was 66 per cent (same as last year) of the FRL.

In view of uneven rainfall during the South-West monsoon season, the area coverage under *kharif* crops in 2006 season was around 1.9 per cent lower than a year ago, mainly on account of shortfall in the case of rice, coarse cereals and oilseeds. In contrast, area sown under *rabi* crops so far (up to January 5, 2007) has been about 3.4 per cent higher than a year ago. The higher sowing under *rabi* crops was mainly on account of increase in area covered under wheat, pulses and coarse cereals, which more than offset some decline in area under oilseeds (Table 3).

Table 2: Spatial Distribution of Rainfall

Year	Cumulative Rainfall: Above(+)/ Below (-) Normal (per cent)	Excess Rainfall	Normal Rainfall	Deficient Rainfall	Scanty/ No Rain	Year	Cumulative Rainfall: Above(+)/ Below (-) Normal (per cent)	Excess Rainfall	Normal Rainfall	Deficient Rainfall	Scanty/ No Rain
		Number of Sub-Divisions						Number of Sub-Divisions			
1	2	3	4	5	6	1	2	3	4	5	6
	South-West Monsoon (June-September)						**North-East Monsoon (October-December)**				
1998	6	12	21	3	0	1998	47	28	6	1	1
1999	-4	3	26	7	0	1999	19	20	7	6	3
2000	-8	5	23	8	0	2000	-47	0	4	13	19
2001	-8	1	30	5	0	2001	13	14	10	9	3
2002	-19	1	14	19	2	2002	-33	3	7	12	14
2003	2	7	26	3	0	2003	9	9	9	6	12
2004	-13	0	23	13	0	2004	-11	8	10	17	1
2005	-1	9	23	4	0	2005	10	11	6	5	14
2006	-1	6	20	10	0	2006	-21	3	6	14	13

Excess : +20 per cent or more. Normal : +19 per cent to -19 per cent. Deficient : -20 per cent to -59 per cent.
Scanty : -60 per cent or less. No Rain : -100 per cent.
Source : India Meteorological Department.

According to the First Advance Estimates, the total *kharif* foodgrains production during 2006-07 at 105.2 million tonnes will be 4.1 per cent lower than the previous year, mainly on account of the likely shortfall in the production of rice (2.9 per cent) and coarse cereals (9.2 per cent). In the case of non-foodgrains, production of *kharif* oilseeds and cotton is likely to decline over the previous year, while that of sugarcane is expected to increase marginally (Table 4).

Table 3: Progress of Area under Crops - 2006-07

(Million hectares)

Crop	Normal Area	Area Coverage			Crop	Normal Area	Area Coverage		
		2005	2006	Variation			2005	2006	Variation
1	2	3	4	5	1	2	3	4	5
***Kharif* Crops**					***Rabi* Crops (up to January 5, 2007)**				
Rice	38.2	37.4	37.2	-0.2	Rice	4.9	0.9	1.0	0.1
Coarse Cereals	22.9	22.8	21.1	-1.6	Wheat	26.1	25.8	27.6	1.8
Of which:					Coarse Cereals	6.4	6.3	6.7	0.4
Bajra	9.4	9.4	8.1	-1.3	*Of which*:				
Jowar	4.4	3.9	3.7	-0.2	Jowar	5.0	4.8	4.8	0.0
Maize	6.2	6.9	7.3	0.4	Maize	0.7	0.7	1.0	0.3
Total Pulses	10.9	11.4	11.5	0.1	Total Pulses	11.0	12.7	13.3	0.6
Total *Kharif* Oilseeds	15.4	17.7	16.9	-0.8	Total Rabi Oilseeds	8.2	10.2	9.3	-0.9
Of which:					*Of which*:				
Groundnut	5.5	5.6	4.8	-0.9	Rapeseed and Mustard	5.4	7.3	6.6	-0.6
Soyabean	6.6	7.8	8.1	0.3	Groundnut	0.8	0.5	0.6	0.0
Sesamum	1.5	1.9	1.8	-0.1	Sunflower	1.1	1.2	1.1	-0.2
Sunflower	0.5	0.9	0.9	-0.1					
Sugarcane	4.2	4.3	4.4	0.2					
Cotton	8.3	8.5	8.9	0.4					
All Crops	**99.8**	**101.9**	**100.0**	**-1.9**	**All Crops**	**56.5**	**55.9**	**57.8**	**1.9**

Source : Ministry of Agriculture, Government of India.

Table 4: Agricultural Production

(Million tonnes)

Crop	2002-03	2003-04	2004-05	2005-06 $	2006-07	
					T	A $$
1	2	3	4	5	6	7
Rice	71.8	88.5	83.1	91.0	92.8	
Kharif	63.1	78.6	72.2	78.0	80.8	75.7
Rabi	8.7	9.9	10.9	13.0	12.0	
Wheat	65.8	72.2	68.6	69.5	75.5	
Coarse Cereals	26.1	37.6	33.5	34.7	36.5	
Kharif	20.0	32.2	26.4	27.0	28.7	24.5
Rabi	6.1	5.4	7.1	7.7	7.8	
Pulses	11.1	14.9	13.1	13.1	15.2	
Kharif	4.2	6.2	4.7	4.7	5.8	5.0
Rabi	7.0	8.7	8.4	8.5	9.4	
Total Foodgrains	**174.8**	**213.2**	**198.4**	**208.3**	**220.0**	
Kharif	87.2	117.0	103.3	109.7	115.3	105.2
Rabi	87.6	96.2	95.1	98.6	104.8	
Total Oilseeds	**14.8**	**25.2**	**24.4**	**27.7**	**29.4**	
Kharif	9.0	16.7	14.1	16.8	18.1	13.2
Rabi	5.9	8.5	10.2	10.9	11.3	
Sugarcane	287.4	233.9	237.1	278.4	270.0	283.4
Cotton #	8.6	13.7	16.4	19.6	18.5	18.1
Jute and Mesta ##	11.3	11.2	10.3	10.7	11.3	10.9

T : Target A : Achievement.
$: Fourth Advance Estimates as on July 15, 2006.
$$: First Advance Estimates as on September 15, 2006.
: Million bales of 170 kgs each.
##: Million bales of 180 kgs each.
Source : Ministry of Agriculture, Government of India.

Food Management

The procurement of foodgrains (rice and wheat) during 2006-07 (up to January 9, 2007) at 29.9 million tonnes (mt) was 13.4 per cent lower than that in the corresponding period of the preceding year on account of decline in procurement of wheat from 14.8 million tonnes to 9.2 million tonnes (Table 5). The offtake of rice and wheat during 2006-07 (April 1 to October 31, 2006) at 20.6 mt was also lower by 16.7 per cent over the corresponding period of the previous year, mainly due to a fall in the offtake under Other Welfare Schemes (OWS). In view of lower procurement, the total stock of foodgrains with the Food Corporation of India (FCI) and other Government agencies declined to 18.7 mt as on November 1, 2006 from 19.8 mt a year ago due to decline in the stocks of wheat to 6.0 mt from 9.1 mt. While the stocks of wheat were lower than the buffer stock norm (11.0 mt), those of rice exceeded the buffer norm (5.2 mt).

Industrial Performance

Industrial production has continued with its momentum during 2006-07, with growth accelerating to 10.6 per cent during April-November 2006 from 8.3

Table 5: Management of Food Stocks

(Million tonnes)

Month	Opening Stock of Foodgrains: Rice	Wheat	Total	Procurement of Foodgrains: Rice	Wheat	Total	Foodgrains Off-take: PDS	OWS	OMS - Domestic	Exports	Total	Closing Stock	Norms
1	2	3	4	5	6	7	8	9	10	11	12	13	14
2004-05	13.1	6.9	20.7	24.2	16.8	41.0	29.7	10.6	0.2	1.0	41.5	18.0	
2005-06	13.3	4.1	18.0	26.6	14.8	41.4	31.4	9.8	1.0	0.0	42.2	16.6	
2005-06@				19.7	14.8	34.5	18.2	6.3	0.2	0.0	24.7	19.8	
2006-07@				20.6	9.2	29.9	17.5	3.1	0.0	0.0	20.6	18.7	
2005													
September	6.4	11.6	18.4	0.4	0.0	0.4	2.7	0.7	0.1	0.0	3.5	15.5	
October	4.9	10.3	15.5	7.5	0.0	7.5	2.7	0.5	0.0	0.0	3.2	19.8	16.2
November	10.3	9.1	19.8	2.7	0.0	2.7	2.3	0.5	0.1	0.0	2.8	19.0	
December	11.1	7.6	19.0	2.9	0.0	2.9	2.7	0.7	0.2	0.0	3.6	19.3	
2006													
January	12.6	6.2	19.3	4.3	0.0	4.3	2.7	0.8	0.1	0.0	3.6	19.5	20.0
February	14.0	4.9	19.5	2.5	0.0	2.5	2.7	0.6	0.3	0.0	3.6	18.3	
March	14.1	3.4	18.3	1.9	0.0	1.9	2.8	0.9	0.2	0.0	3.9	16.6	
April	13.7	2.0	16.6	1.7	8.7	10.3	2.5	0.3	0.0	0.0	2.8	22.8	16.2
May	12.8	9.0	22.8	1.6	0.6	2.2	2.5	0.4	0.0	0.0	3.0	22.3	
June	12.0	9.3	22.3	1.5	0.0	1.5	2.5	0.6	0.0	0.0	3.1	20.5	
July	11.1	8.2	20.5	0.8	0.0	0.8	2.7	0.4	0.0	0.0	3.1	17.1	26.9
August	9.5	7.3	17.1	0.5	0.0	0.5	2.7	0.4	0.0	0.0	3.1	15.5	
September	7.8	6.7	15.5	0.2	0.0	0.2	2.3	0.5	0.0	0.0	2.8	12.6	
October	6.0	6.4	12.6	8.0	0.0	8.0	2.4	0.4	0.0	0.0	2.7	18.7	16.2
November	12.5	6.0	18.7	2.0	0.0	2.0	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	
December	N.A.	N.A.	N.A.	2.6	0.0	2.6	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	
2007													
January*	N.A.	N.A.	N.A.	1.9	0.0	1.9	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	20.0

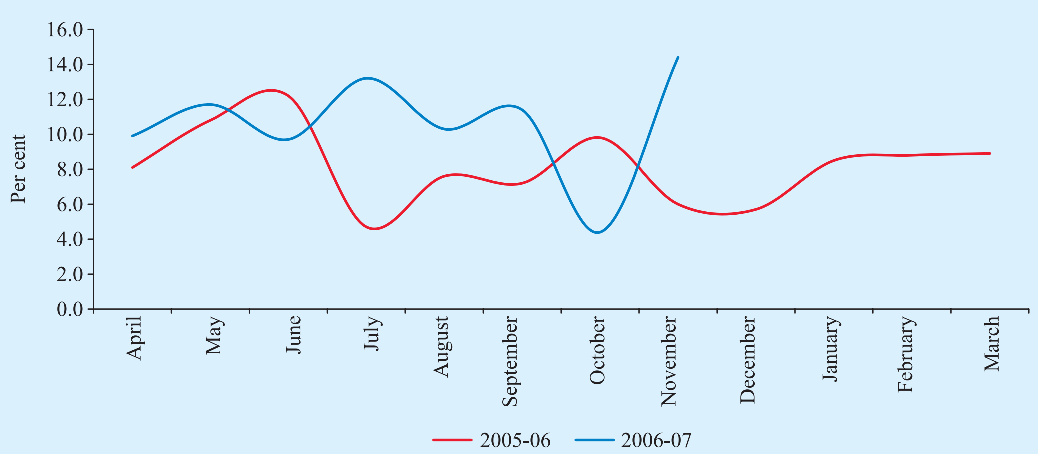
PDS :Public Distribution System. OWS :Other Welfare Schemes. OMS : Open Market Sales. N.A. : Not Available.
@ : Procurement up to January 9 and offtake up to end-October. * :Procurement up to January 9, 2007.

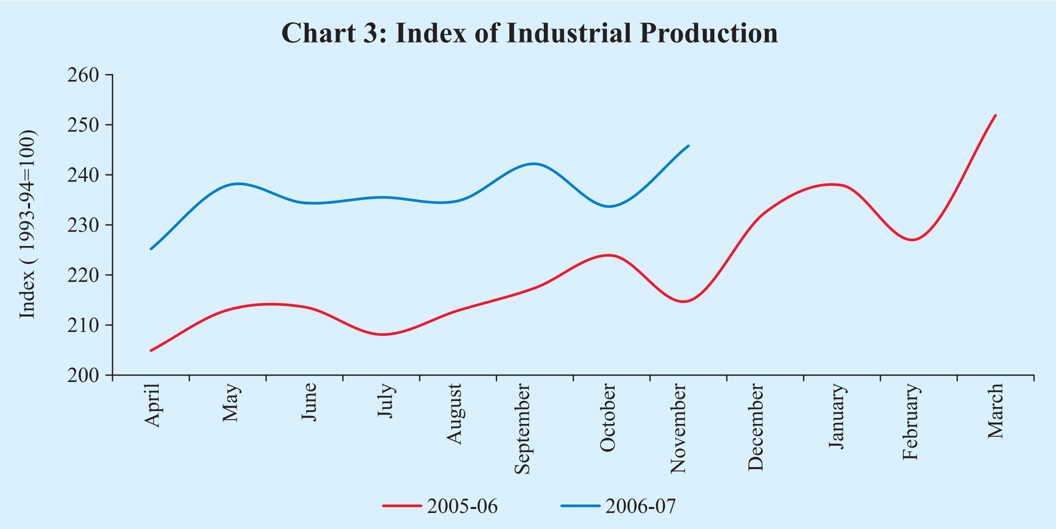
Note : Closing stock figures may differ from those arrived at by adding the opening stocks and procurement and deducting, offtake, as stocks include coarse grains also.

Source : Ministry of Consumer Affairs, Food and Public Distribution, Government of India.

per cent a year ago (Chart 2). Dip in industrial growth during October 2006 and the jump during November 2006 could be partly attributed to the base effect

Chart 2: Index of Industrial Production: Year-on-Year Growth





(Chart 3).The manufacturing sector with double-digit growth (11.5 per cent) continued to be the key driver of industrial activity, contributing almost 91.2 per cent of the growth in industry (Table 6). Electricity and mining sectors also picked up during April-November 2006.

The sustained buoyancy in manufacturing activity was led by the sub-sectors such as machinery and equipments, transport equipments and parts, basic metal and alloy industries and non-metallic mineral products (Table 7). These four sub-sectors contributed more than a half of industrial growth during April-November 2006.

Table 6: Index of Industrial Production: Sectoral and Use-Based Classification of Industries

(Per cent)

Industry Group	Weight in the IIP	Growth Rate			Weighted Contribution #		
		April-March	April-November		April-March	April-November	
		2005-06	2005	2006 P	2005-06	2005	2006 P
1	2	3	4	5	6	7	8
Sectoral							
Mining	10.5	1.0	0.5	3.8	1.0	0.5	2.7
Manufacturing	79.4	9.1	9.4	11.5	93.3	93.8	91.2
Electricity	10.2	5.2	5.0	7.3	5.7	5.6	6.2
Use-Based							
Basic Goods	35.6	6.7	6.1	9.3	25.4	23.1	27.2
Capital Goods	9.3	15.7	16.2	16.1	20.8	19.4	16.2
Intermediate Goods	26.5	2.5	2.5	10.9	8.2	8.5	27.5
Consumer Goods (a+b)	28.7	12.0	13.3	9.7	47.4	49.2	29.4
a) Consumer Durables	5.4	15.3	14.2	12.5	14.6	13.9	10.1
b) Consumer Non-durables	23.3	10.9	12.9	8.7	32.8	35.2	19.3
General	**100.0**	**8.2**	**8.3**	**10.6**	**100.0**	**100.0**	**100.0**

P : Provisional. # : Figures may not add up to 100 due to rounding off.
Source : Central Statistical Organisation.

Table 7: Growth of Manufacturing Groups

(Per cent)

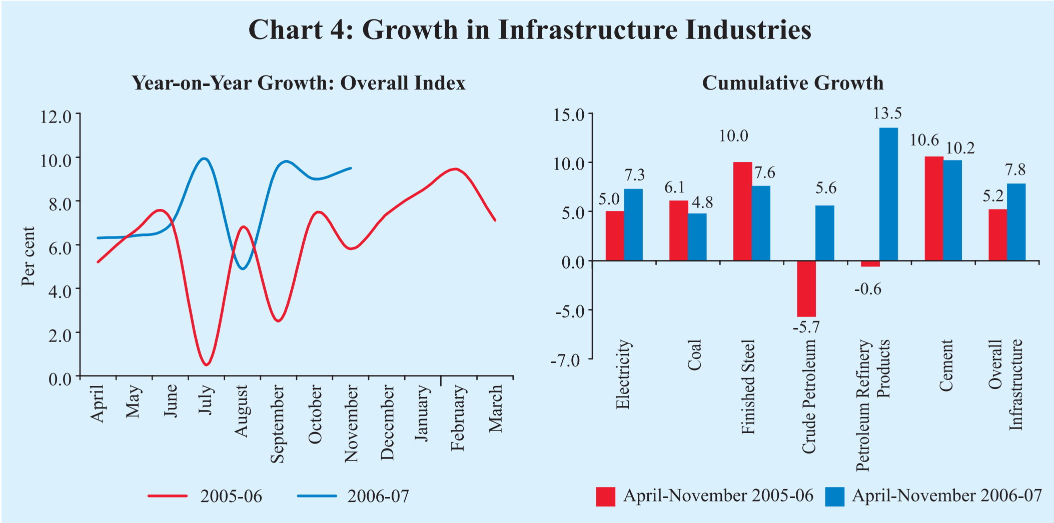
Industry Group	Weight in the IIP	Growth Rate April-November 2005	Growth Rate April-November 2006 P	Weighted Contribution # April-November 2005	Weighted Contribution # April-November 2006 P
1	2	3	4	5	6
1. Machinery and equipment other than transport equipment	9.6	10.8	14.1	18.0	19.3
2. Chemicals and chemical products except products of petroleum and coal	14.0	11.7	9.1	25.2	16.2
3. Basic metal and alloy industries	7.5	15.6	20.4	14.3	16.1
4. Transport equipment and parts	4.0	12.5	16.3	9.0	9.7
5. Non-metallic mineral products	4.4	8.3	13.7	5.7	7.6
6. Beverages, tobacco and related products	2.4	17.4	12.5	8.9	5.6
7. Rubber, plastic, petroleum and coal products	5.7	2.8	11.9	2.0	6.5
8. Cotton textiles	5.5	11.3	13.0	5.0	4.8
9. Textile products (including wearing apparel)	2.5	20.6	12.9	7.1	4.0
10. Other manufacturing industries	2.6	23.0	10.4	8.1	3.4
11. Paper and paper products and printing, publishing and allied activities	2.7	5.2	8.4	1.9	2.4
12. Metal products and parts (except machinery and equipment)	2.8	-2.2	6.8	-0.7	1.5
13. Wool, silk and man-made fibre textiles	2.3	-0.8	6.6	-0.3	1.8
14. Food products	9.1	-4.6	1.9	-3.9	1.1
15. Wood and wood products, furniture and fixtures	2.7	-3.5	2.4	-0.5	0.2
16. Jute and other vegetable fibre textiles (except cotton)	0.6	2.6	1.0	0.1	0.0
17. Leather and leather and fur products	1.1	0.0	-3.7	0.0	-0.3
Manufacturing – Total	**79.4**	**9.4**	**11.5**	**100**	**100**

P : Provisional. # : Figures may not add up to 100 due to rounding off.
Source : Central Statistical Organisation.

In terms of use-based classification, the capital goods sector continued to exhibit a high growth (see Table 6). Sustained growth in domestic production of capital goods along with large growth in their imports is indicative of ongoing strong investment activity in the economy. Basic and intermediate goods recorded an acceleration on account of higher production of cotton yarn, viscose staple fibre and minerals. Growth of consumer goods sector moderated on the back of deceleration in growth of consumer non-durables. This was, in turn, due to decline in production of milk powder, wheat flour and edible oils.

Infrastructure

Growth in infrastructure industries improved to 7.8 per cent during April-November 2006 from 5.2 per cent during the same period of 2005 on account of better performance of electricity, crude petroleum and petroleum refinery products (Chart 4). Higher plant load factor in thermal power plants and higher than targeted hydro power generation led to a higher growth in the electricity sector. Double-digit growth in the petroleum refinery products was partly attributable to the base effect. The turnaround in crude oil production largely reflected restoration of production of crude oil at Mumbai High offshore. Cement production continued to record a strong growth, even on a high base, on the back of strong construction demand.



Services Sector

During the first half of 2006-07, growth in the services sector accelerated to 10.6 per cent from 10.2 per cent during the first half of 2005-06 (see Table 1). The services sector, thus, continued to be the key driver of economic activity in the country, contributing nearly three-fourth to overall growth. The sub-sector 'trade, hotels, restaurants, transport, storage and communication', which constitutes almost one fourth of GDP, led the growth in the services, benefiting from growth in activities such as tourism, telecommunications, railways freight traffic and civil aviation (Table 8). The sub-sector 'financing, insurance, real

Table 8: Indicators of Services Sector Activity

(Growth rates in per cent)

Sub-sector	2004-05	2005-06	April-October	
			2005	2006
1	2	3	4	5
Tourist arrivals	24.0	12.7	13.0^	13.5^
Commercial vehicles production	28.6	10.6	15.3 *	31.6 *
Railway revenue earning freight traffic	8.1	10.7	9.5	9.9
New cell phone connections	10.4	89.4	38.4	121.9
Cargo handled at major ports	11.3	10.3	13.2	6.6
Civil aviation				
a) Export cargo handled	12.4	7.3	15.5	-3.1
b) Import cargo handled	24.2	15.8	12.3	19.3
c) Passengers handled at international terminals	14.0	12.8	12.8	11.9
d) Passengers handled at domestic terminals	23.6	27.1	22.5	38.8
Cement	8.2	10.7	10.6 *	10.2 *
Steel	7.6	6.0	10.0 *	7.6 *
Aggregate deposits	11.9	22.3	8.9 #	12.9 #
Non-food credit	31.6	38.4	17.5 #	16.9 #
Central Government expenditure ##	9.4	8.4 P	10.8 *	14.9 *

^ : Up to December. * : April-November. # : up to January 5, 2007. P : Provisional.
: Data for the years 2003-04 and 2004-05 are taken net of repayments to NSSF.

Table 9: Growth in Services Sectors

(Contribution to Overall Real GDP Growth, percentage points)

Year	Construction	Trade, Hotels, Transport and Communication	Financing, Insurance, Real Estate and Business Services	Community, Social and Personal Services	Total Services
1	2	3	4	5	6
2000-01	0.4	1.5	0.5	0.7	3.1
2001-02	0.2	2.0	0.9	0.6	3.8
2002-03	0.5	2.1	1.1	0.5	4.1
2003-04	0.7	2.9	0.6	0.8	4.9
2004-05	0.8	2.6	1.2	1.3	5.9
2005-06	0.8	2.9	1.3	1.1	6.1
2005-06 Q1	0.8	2.9	1.2	1.0	5.9
Q2	0.8	2.7	1.5	1.2	6.3
Q3	0.7	2.5	1.1	1.1	5.3
Q4	0.7	3.3	1.3	1.1	6.5
2006-07 Q1	0.6	3.3	1.2	1.0	6.2
Q2	0.7	3.6	1.4	1.1	6.7

estate and business services' witnessed a strong growth, though with some moderation, on the back of buoyancy in business services (such as software), growth in deposits and credit offtake. Construction activity also continued to record a strong growth, *albeit* somewhat lower than a year ago (Table 9).

Business Expectations Surveys

Business confidence surveys suggest that economic activity is likely to remain buoyant in the near term. After having declined in the previous round in the aftermath of volatility in stock market and elevated oil prices, business confidence indices compiled by various agencies recovered on the back of rebound in the stock market, decline in international crude oil prices from their record highs, close to normal monsoon, strong economic growth, high level of capacity utilisation and improved expectations of financial performance. Dun & Bradstreet's composite business optimism index for the period January-March 2007 increased by 9.8 per cent over the previous quarter; five out of six indices, *viz.*, volume of sales, net profits, selling prices, new orders and inventory levels are expected to increase over the previous quarter. About 94 per cent of the respondents anticipated an increase in profitability, while 95 per cent anticipated an increase in sales volume. The National Council of Applied Economic Research's (NCAER's) business confidence index (BCI) for October-December 2006 rose by 3.2 per cent over the previous round (Table 10).

According to the Reserve Bank's latest Industrial Outlook Survey, the business expectations indices based on assessment for October-December 2006

Table 10: Business Expectations Surveys

Agency	Business Expectations		Growth over a year ago (per cent)	Growth over previous round (per cent)
	Period	Index		
1	2	3	4	5
Dun & Bradstreet	January-March 2007	Business Optimism Index	16.0	9.8
NCAER	October-December 2006	Business Confidence Index	3.9	3.2
RBI	January-March 2007	Business Expectation Index	0.6	1.0

and on expectations for January-March 2007 increased by 2.7 per cent and 1.0 per cent, respectively, over the previous quarter. Business confidence has, thus, continued with the general uptrend that began in early 2002, *albeit* with some fluctuations (Chart 5).

The improvement in expectations index for January-March 2007 was backed by higher net responses for major parameters of the survey such as the overall business situation, production, order books, capacity utilisation, employment, and profit margins over the previous quarter. The financial situation is expected to show an improvement, as the higher working capital finance requirement is also expected to be met by improvement in the availability of finance. Expectations of increase in selling prices, exports and imports have, however, moderated *vis-à-vis* the previous quarter (Table 11).

To sum up, the industry and the services sectors have remained strong during 2006-07 so far. Business confidence surveys also suggest that economic activity

Chart 5: Reserve Bank's Industrial Outlook Survey: Business Expectation Index

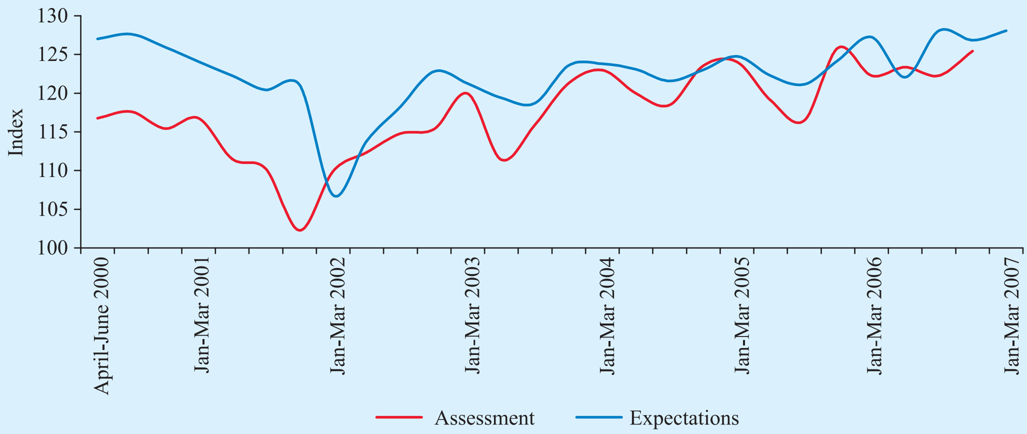


Table 11: Net Response on 'A Quarter Ahead' Expectations About the Industrial Performance

(Per cent)

Parameter	Response	Jan.-March 2006 (934)	April-June 2006 (1086)	July-Sept. 2006 (1073)	Oct.-Dec. 2006 (1138)	Jan.-March 2007 (1115)
1	2	3	4	5	6	7
1. Overall business situation	Better	49.8	46.3	53.1	51.8	53.7
2. Financial situation	Better	40.7	40.4	43.4	41.9	44.5
3. Working capital finance requirement	Increase	31.9	30.6	32.7	35.4	36.2
4. Availability of finance	Improve	34.1	33.8	35.0	33.4	36.2
5. Production	Increase	46.3	42.5	49.4	49.7	50.7
6. Order books	Increase	41.0	39.1	45.2	46.3	47.3
7. Cost of raw material	Decrease	-35.9	-37.3	-45.8	-49.2	-41.7
8. Inventory of raw material	Below average	-6.8	-5.0	-6.3	-6.1	-7.1
9. Inventory of finished goods	Below average	-4.7	-4.5	-2.6	-4.9	-5.2
10. Capacity utilisation	Increase	29.6	24.8	32.1	33.2	33.3
11. Level of capacity utilisation	Above normal	11.4	9.4	11.8	10.9	12.8
12. Assessment of the production capacity	More than adequate	4.9	4.1	3.6	5.1	4.8
13. Employment in the company	Increase	13.3	14.5	16.4	17.9	18.1
14. Exports, if applicable	Increase	31.8	31.0	38.3	34.2	32.6
15. Imports, if any	Increase	20.8	22.7	23.8	23.4	20.8
16. Selling prices are expected to	Increase	10.8	12.4	16.6	16.8	14.2
17. If increase expected in selling prices	Increase at lower rate	16.3	12.0	10.5	14.5	10.5
18. Profit margin	Increase	12.6	9.3	11.1	9.2	11.6

Note : 1. Figures in parentheses represent number of companies included in the results.
2. 'Net response' is measured as the percentage share differential between the companies reporting 'optimistic' (positive) and 'pessimistic' (negative) responses; responses indicating status quo (no change) are not reckoned. Higher 'net response' indicates higher level of confidence and *vice versa*.

is likely to remain buoyant in the near term. The ongoing momentum in economic growth is, thus, likely to remain robust in the rest of 2006-07 (Table 12).

Table 12: Projections of Real Gross Domestic Product for India by Various Agencies for 2006-07

(Per cent)

Agency		Overall Growth	Agriculture	Industry	Services	Month of Projection
1		2	3	4	5	6
Asian Development Bank	a)	7.8	..	..	..	Sep-06
Investment Information and Credit Rating Agency of India	a)	7.4-8.2	2.0	8.2-9.7	9.1-9.7	Jan-06
	b)	8.1	1.0	10.8	9.5	Jul-06
Centre for Monitoring Indian Economy	a)	8.5	2.6	9.7	10.3	Dec-06
National Council of Applied Economic Research.	a)	8.1	..	..	..	Nov-06
	b)	8.4	2.7	9.1	10.2	Jan-07
International Monetary Fund	a)	7.3 @	..	..	..	Apr-06
	b)	8.3 @	..	..	..	Sep-06
Reserve Bank of India	a)	7.5-8.0	..	..	..	Apr-06
	b)	Around 8.0	..	..	..	Oct-06
JP Morgan	a)	8.0	..	..	..	Oct-06
	b)	8.4	..	..	..	Dec-06
Citigroup	a)	8.3	..	..	..	Sep-06
	b)	8.3	..	..	..	Jan-07
ABN AMRO	a)	7.5	..	..	..	Sep-06
	b)	8.2	2.4	8.4	10.0	Dec-06
Indicus Analytics	a)	7.9	..	..	..	Sep-06
	b)	8.9	3.0	9.7	10.5	Dec-06

.. : Not Available. @ : Calendar year 2006.

II. FISCAL SITUATION

Combined Government Finances: 2006-07

With the resumption of fiscal consolidation process at the Centre in terms of the Fiscal Responsibility and Budget Management (FRBM) Rules, 2004 and enactment of fiscal responsibility legislations by most of the States, public finances are budgeted to show improvement during 2006-07. Key deficit indicators of the Centre and States taken together are budgeted to decline by 0.7-0.9 per cent of GDP in 2006-07 on the back of buoyancy in tax collections and reprioritisation of expenditure towards development expenditure (Table 13).

Centre's Fiscal Situation

The Central Government finances for the first eight months (April-November) of the fiscal year 2006-07 show that fiscal deficit, as per cent of budget estimates (BE), was placed lower than that in the corresponding period of the previous year (Chart 6 and Table 14). Till September 2006, fiscal deficit (as per

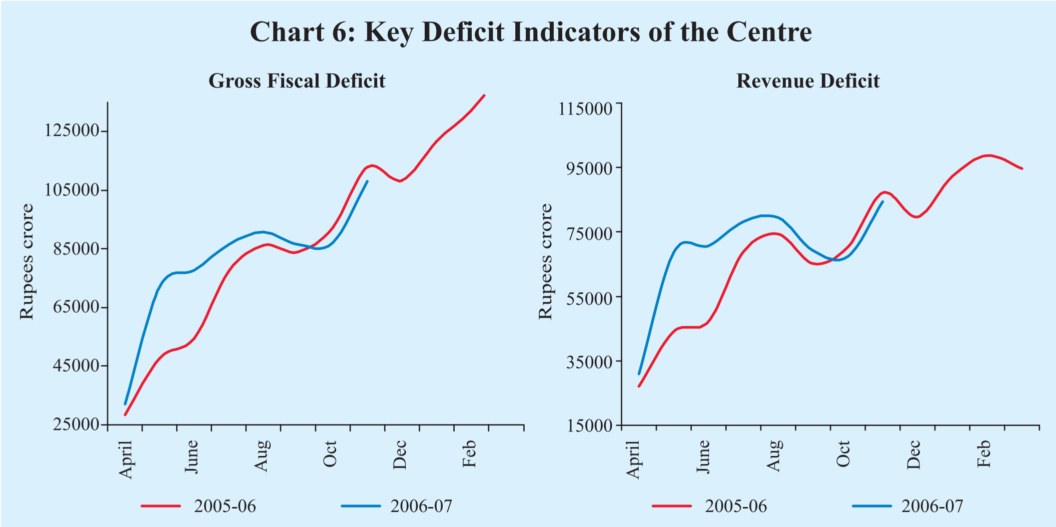
Table 13: Key Fiscal Indicators

(Per cent to GDP)

Year	Primary Deficit	Revenue Deficit	Gross Fiscal Deficit
1	2	3	4
		Centre	
2002-03	1.1	4.4	5.9
2003-04	-0.03	3.6	4.5
2004-05	0.06	2.5	4.01
2005-06 RE	0.5	2.6	4.1
	(0.4)	(2.7)	(4.1)
2006-07 BE	0.2	2.1	3.8
		States	
2002-03	1.3	2.2	4.2
2003-04	1.5	2.2	4.5
2004-05	0.7	1.2	3.5
2005-06 RE	0.7	0.5	3.2
2006-07 BE	0.3	0.1	2.8
		Combined	
2002-03	3.1	6.7	9.6
2003-04	2.1	5.8	8.5
2004-05	1.4	3.7	7.5
2005-06 RE	1.6	3.1	7.5
2006-07 BE	0.9	2.3	6.6

RE: Revised Estimates. BE: Budget Estimates.

Note : 1. Figures in parentheses are provisional accounts for 2005-06.
2. Data in respect of States are provisional from year 2004-05 onwards.



cent to BE) was placed higher than a year ago. Revenue deficit during April-November 2006, as per cent of BE, however, continued to be higher than the previous year on account of increase in non-Plan expenditure which offset buoyant tax revenues. Contraction in non-defence capital outlay and loans and advances, however, moderated the impact on fiscal deficit.

Table 14: Central Government Finances during April-November 2006

Items	2006-07 (Budget Estimates) (Rupees crore)	April-November			
		Rupees crore		Per cent of Budget Estimates	
		2005	2006	2005	2006
1	2	3	4	5	6
1. Revenue Receipts (i+ii)	4,03,465	1,73,703	2,21,190	49.5	54.8
i) Tax Revenue (Net)	3,27,205	1,30,095	1,76,956	47.6	54.1
ii) Non-Tax Revenue	76,260	43,608	44,234	56.1	58.0
2. Non-Debt Capital Receipts	11,840	6,370	7,148	53.1	60.4
3. Non-Plan Expenditure	3,91,263	2,10,638	2,45,393	56.8	62.7
of which:					
i) Interest Payments	1,39,823	75,526	87,943	56.4	62.9
ii) Defence	89,000	37,617	43,184	45.3	48.5
iii) Major Subsidies	44,792	31,149	36,505	67.2	81.5
4. Plan Expenditure	1,72,728	82,384	91,146	57.4	52.8
5. Revenue Expenditure	4,88,192	2,60,884	3,05,673	58.4	62.6
6. Capital Expenditure	75,799	32,138	30,866	47.4	40.7
7. Total Expenditure	5,63,991	2,93,022	3,36,539	57.0	59.7
8. Revenue Deficit	84,727	87,181	84,483	91.5	99.7
9. Fiscal Deficit	1,48,686	1,12,949	1,08,201	74.7	72.8
10. Primary Deficit	8,863	37,423	20,258	217.6	228.6

Source: Controller General of Accounts, Ministry of Finance.

During April-November 2006, tax revenues, as per cent of BE, were higher than a year ago on account of impressive growth in income tax, corporation tax, customs duties and services tax. Receipts from new taxes - fringe benefit tax, securities transaction tax and banking cash transaction tax - also remained buoyant in the first eight months of 2006-07. Union excise duties, however, continued to show subdued growth. Non tax-revenues, as per cent of BE, were higher than a year ago on account of higher dividends and profits. Aggregate expenditure, as per cent of BE, was higher on account of sustained increase in non-Plan expenditure, particularly interest payments, subsidies and grants to States. Plan expenditure, in terms of budget estimates, declined under both the revenue and capital accounts. Capital outlay in the first eight months showed a modest increase on account of a rise in defence capital outlay.

Mid-Year Review by Government of India

The Central Government finances during the first half of the year (April-September 2006) exhibited stress with the key deficit indicators, as per cent of BE, being higher than their levels in the corresponding period of the previous year. The deficit indicators, *viz.*, the revenue and fiscal deficit fell short of the half yearly FRBM targets. In the document Mid-Year Review for 2006-07, as required under the FRBM Act, 2003, the Central Government contended that the accelerated pace of expenditure partly reflected front-loading of expenditures, particularly in the first quarter, to smoothen intra-year asymmetry in spending and avoid bunching of expenditures and parking of funds in the last quarter. The stress in the finances was also attributed to the acceleration in non-Plan expenditures in the second quarter. The Government is confident of evening out the mismatch in expenditure and receipts during the second half of the year. Buoyant economic growth is also expected to contribute towards augmenting the Government's revenue, thereby enabling it to meet the deficit targets set in the Budget.

Financing of the Union Budget

Net market borrowings (excluding allocations under the Market Stabilisation Scheme) of the Centre for 2006-07 are budgeted at Rs.1,13,778 crore, which would finance 76.5 per cent of the gross fiscal deficit in 2006-07 as compared with 69.2 per cent in the preceding year. Including repayment obligations of Rs.68,097 crore (as per Reserve Bank records), gross market borrowings of the Central Government work out to Rs.1,81,875 crore. During 2006-07 (up to January 22, 2007), the issuances of dated securities at Rs.1,25,000 crore were higher than the amount raised (Rs.1,15,000 crore) in the corresponding period of the preceding year (Table 15). Although the Central Government frontloaded its market borrowings by an additional Rs.4,000 crore on June 22, 2006, gross

Table 15: Central Government Securities Issued during 2006-07

(Amount in Rupees crore/Maturity in years)

	Borrowings as per Issuance Auction Calendar			Actual Borrowings			
Sr. No.	Date of Auction	Amount	Residual Maturity	Date of Auction	Amount	Residual Maturity	Yield (Per cent)
1	2	3	4	5	6	7	8
1.	April 3-12, 2006	5,000	10 -14	April 10, 2006	5,000	10.00	7.59
		3,000	20 and above	April 10, 2006	3,000	28.30	7.97
2.	April 18-25, 2006	6,000	5-9	April 25, 2006	6,000	6.02	7.06
		4,000	20 and above	April 25, 2006	4,000	26.34	8.00
3.	May 2-9,2006	6,000	10-14	May 4, 2006	6,000	9.94	7.55
		4,000	20 and above	May 4, 2006	4,000	28.26	8.14
4.	May 16-24, 2006	5,000	15 -19	May 23, 2006	5,000	15.00	7.94
5.	June 1- 8, 2006	6,000	5-9	June 6, 2006	6,000	5.07	8.33
		4,000	20 and above	June 6, 2006	4,000	30.00	7.39
6.	June 15-24, 2006	5,000	15-19	June 22, 2006	5,000	8.52	7.92
				June 22, 2006*	4,000	14.95	8.46
7.	July 3-11, 2006	6,000	10-14	July 11, 2006	5,000	9.75	8.29
		4,000	20 and above	July 11, 2006	2,000	28.08	8.75
8.	July 17-25, 2006	5,000	15-19	July 27, 2006	4,000	3.79	7.69
9.	August 1-8, 2006	6,000	5-9	August 8, 2006	6,000	4.90	7.94
		3,000	20 and above	August 8, 2006	3,000	9.68	8.27
10.	August 14-22, 2006	5,000	10-14	August 18, 2006	5,000	10.40	8.12
		3,000	20 and above	August 18, 2006	3,000	29.79	8.72
11.	September 4-12, 2006	6,000	10-14	September 8, 2006	6,000	9.59	7.76
		3,000	20 and above	September 8, 2006	3,000	27.91	8.45
12.	October 6-13, 2006	6,000	10 -14	October 13, 2006	6,000	9.49	7.63
		3,000	20 and above	October 13, 2006	3,000	29.64	8.10
13.	November 3-10, 2006	6,000	5-9	November 3, 2006	6,000	5.49	7.50
		3,000	20 and above	November 3, 2006	3,000	27.76	8.02
14.	November 17-24, 2006	5,000	10-14	November 24, 2006	5,000	10.13	7.43
15.	December 1-8, 2006	6,000	5-9	December 8, 2006	5,000	7.35	7.31
		3,000	20 and above	December 8, 2006	4,000	29.49	7.63
16.	January 5-12, 2007	5,000	10-14	@	@	@	@
		4,000	20 and above	January 12, 2007	4,000	29.39	8.24

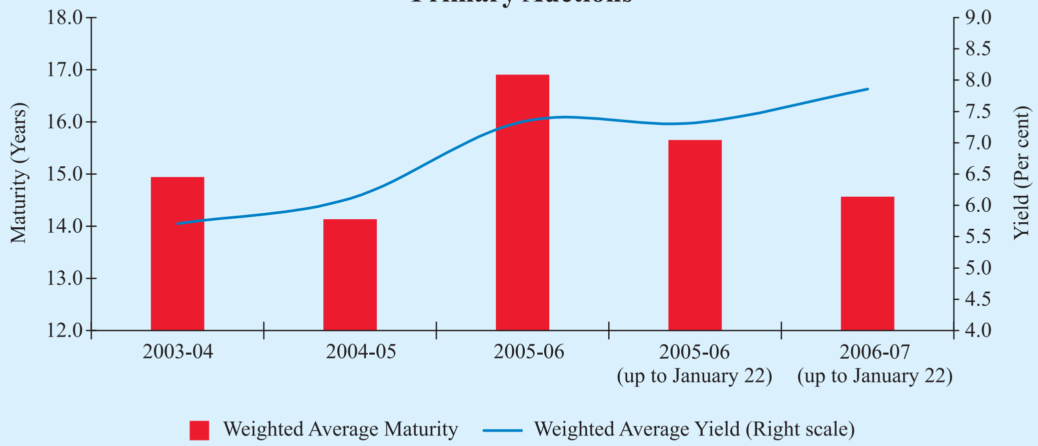
*: Not scheduled. @ : Auction cancelled.

market borrowings during 2006-07 (up to January 22, 2007) were Rs.5,000 crore lower than the indicative issuance calendar reflecting (i) the reduction in the notified amounts from Rs.6,000 crore and Rs.4,000 crore (as per issuance auction calendar) to Rs.5,000 crore and Rs.2,000 crore, respectively, in the auctions held on July 11, 2006 and from Rs.5,000 crore to Rs.4,000 crore on July 27, 2006 and (ii) cancellation of the auction of Rs 5,000 crore scheduled for January 5-12, 2007 on a review of the Government's borrowing requirements. Furthermore, in the auction held on December 8, 2006, the notified amount of short tenor security was reduced by Rs.1,000 crore, while that of the longer tenor security was increased by Rs.1,000 crore. During the year so far, 28 securities have been issued. While 25 securities were reissues, three new securities of 10-year, 15-year and 30-year maturity were issued to provide benchmarks in the respective segments. Gross and net market borrowings (including dated securities and 364-day Treasury Bills) raised by the Centre during 2006-07 up to January 22, 2007 amounted to 83.1 per cent and 80.4 per cent of the budget estimates as compared with 84.9 per cent and 82.7 per cent, respectively, a year ago.

The weighted average maturity of dated securities of the Central Government during 2006-07 (up to January 22, 2007) at 14.56 years was lower than that of 15.61 years in the corresponding period of the preceding year. The weighted average yield of the dated securities issued over the same period, on the other hand, increased to 7.86 per cent from 7.29 per cent (Chart 7). In this context, it may be noted that the secondary market yield on 10-year Central Government securities increased from 7.02 per cent during April-December 2005 to 7.76 per cent during April-December 2006.

The Central Government has taken recourse to ways and means advances (WMA) on 39 days during 2006-07 so far (up to January 22, 2007) as compared with only two days during the entire fiscal year 2005-06. The average WMA utilisation during 2006-07 (up to January 22, 2007) was Rs.533 crore as compared with Rs.4 crore in the corresponding period of the preceding year. The Central Government continued to maintain large cash surplus with the Reserve Bank. The average daily surplus balance of the Central Government with the Reserve Bank was Rs.23,077 crore during 2006-07 (up to January 22, 2007) as compared with Rs.21,817 crore during the corresponding period of the previous year.

Chart 7: Yield and Maturity of the Dated Securities of the Centre – Primary Auctions



State Finances

Financing of the States' Budgets

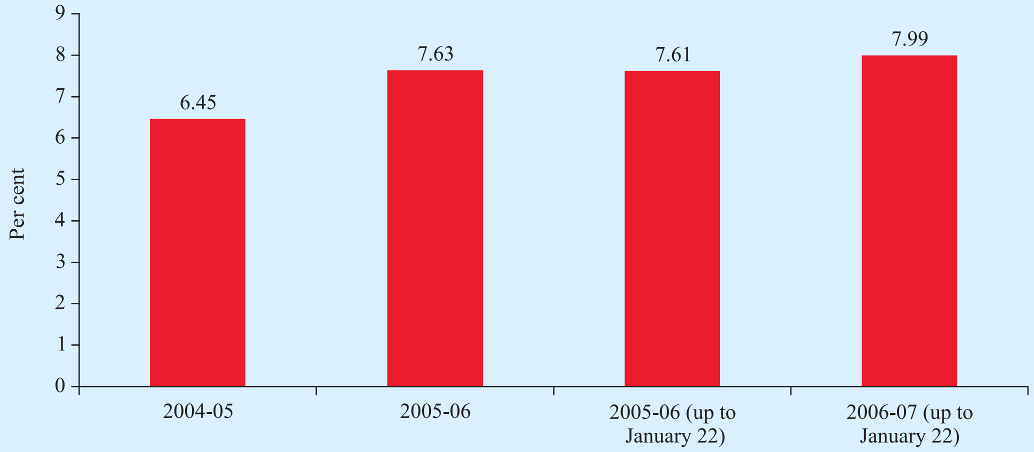
The provisional net allocation under market borrowing programme for State Governments is placed at Rs.17,242 crore during 2006-07. Taking into account additional allocations amounting to Rs.2,066 crore and repayments of Rs.6,551 crore, the gross allocation amounts to Rs.25,860 crore. During 2006-07 so far (up to January 22, 2007), the States have raised market loans amounting to Rs.14,204 crore (or 54.9 per cent of gross allocation) exclusively through auctions with cut-off rates in the range of 7.65-8.66 per cent (Table 16). Over the same period of 2006-07, the weighted average interest rate of market loans firmed up to 7.99 per cent from 7.61 per cent in the corresponding period of the previous year (Chart 8).

Table 16: Market Borrowings of State Governments during 2006-07 (up to January 22, 2007)

Item	Date	Cut-off Rate (Per cent)	Tenor (Years)	Amount Raised (Rupees crore)
1	2	3	4	5
A. Tap Issues	–	–	–	–
B. Auctions				**14,204**
i. First	April 27, 2006	7.65	10	300
ii. Second	May 11, 2006	7.89	10	500
		8.00	10	1,646
		7.95	10	881
		8.04	10	150
		7.96	10	130
		7.87	10	400
		7.91	10	500
		7.98	10	57
		8.05	10	15
		7.93	10	1,307
iii. Third	July 13, 2006	8.65	10	933
		8.66	10	300
		8.62	10	225
iv. Fourth	August 25, 2006	8.11	10	1,050
v. Fifth	October 17, 2006	7.99	10	153
		8.04	10	48
		7.74	10	2,184
		7.80	10	91
vi. Sixth	November 16, 2006	7.82	10	156
vii. Seventh	December 14, 2006	7.81	10	340
		7.89	10	166
		7.93	10	809
		7.94	10	455
		7.99	10	193
viii. Eighth	January 18, 2007	7.96	10	500
		7.99	10	715
Grand Total (A+B)				**14,204**

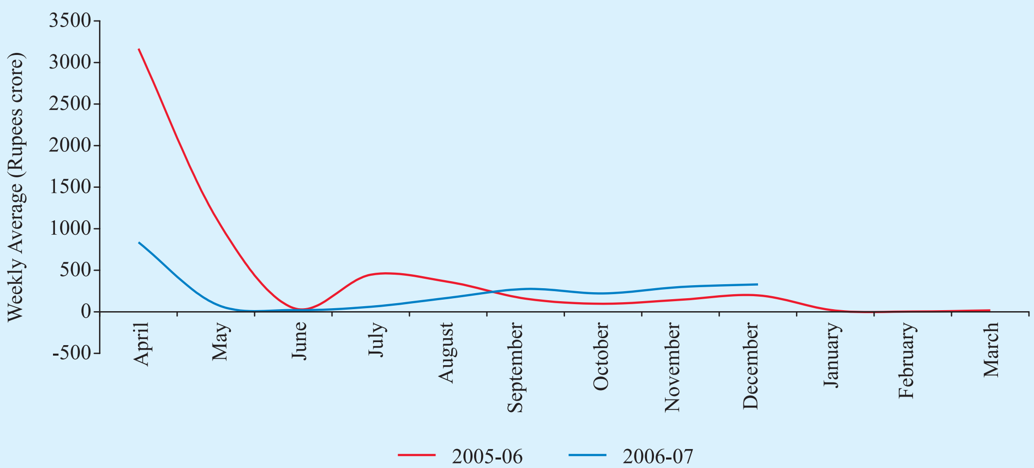
Source: Reserve Bank of India.

Chart 8: Weighted Average Interest Rate on State Government Market Borrowings



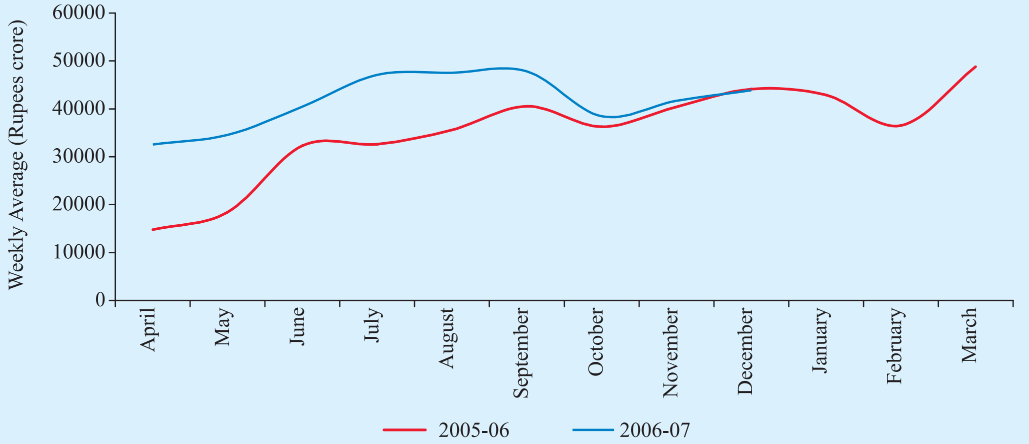
The liquidity position of the States has remained comfortable during 2006-07 so far. Notwithstanding the increase in WMA availment between September and November 2006, the weekly average utilisation of WMA and overdraft by the States at Rs.256 crore during April-December 2006 was lower than that of Rs.639 crore in the corresponding period of 2005 (Chart 9). Two States resorted to overdraft during 2006-07 (up to January 22, 2007) as compared with nine States during the corresponding period of the previous year. The cash surplus position of the State Governments has improved further during 2006-07 so far. This was reflected in an increase in their investments in 14-day Treasury Bills to Rs.41,567 crore

Chart 9: Utilisation of WMA and Overdraft by States



(weekly average) during April-December 2006 from Rs.32,789 crore in the corresponding period of the previous year (Chart 10). The surplus cash balances of State Governments are automatically invested in 14-day Treasury Bills.

Chart 10: Investments in 14-day Intermediate Treasury Bills by State Governments



III. MONETARY AND LIQUIDITY CONDITIONS

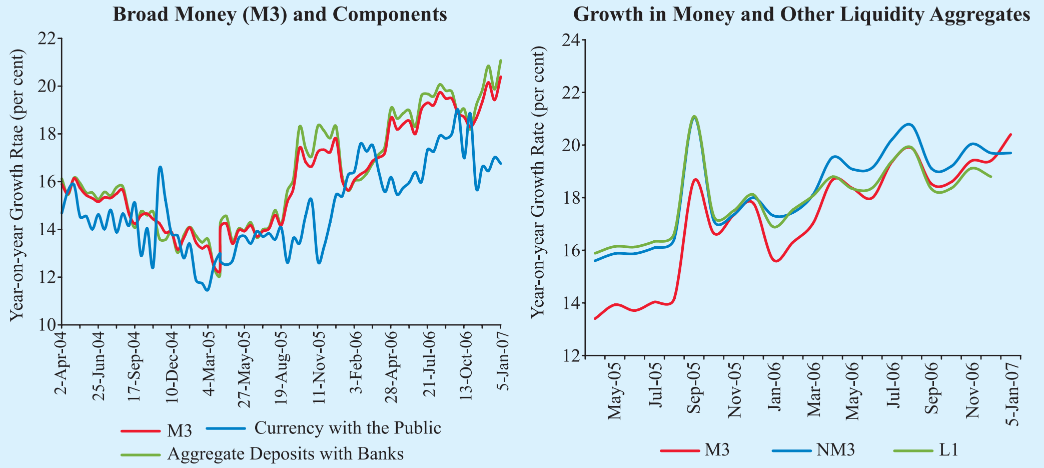
Bank credit has continued to grow at a strong pace. Sustained growth of bank credit was accommodated by acceleration in deposit growth. Concomitantly, broad money growth has remained above the indicative trajectory, reflecting strong demand conditions. Banks' SLR investments, as a proportion of their net demand and time liabilities (NDTL), have declined further from their end-March 2006 levels. The Reserve Bank continued to modulate market liquidity with the help of LAF repo and reverse repos and issuance of securities under the Market Stabilisation Scheme (MSS). Furthermore, the Reserve Bank raised cash reserve ratio (CRR) by 50 basis points in two phases with effect from the fortnight beginning December 23, 2006.

Monetary Survey

Broad money (M_3) growth, year-on-year (y-o-y), accelerated to 20.4 per cent as on January 5, 2007 from 17.0 per cent at end-March 2006 and 16.0 per cent a year ago. On a fiscal year basis too, M_3 growth during 2006-07 so far (January 5, 2007 over March 31, 2006), at 11.9 per cent, was higher than that of 8.8 per cent in the corresponding period of 2005-06 (January 6, 2006 over April 1, 2005). Taking into account, *inter alia*, these trends in monetary aggregates, sustained growth in credit offtake, and additional absorption of liquidity under the MSS, the Reserve Bank, on December 8, 2006, decided to increase the CRR by 50 basis points in two stages – 25 basis points each effective the fortnights beginning December 23, 2006 and January 6, 2007. Other developments in the domestic economy impacting upon the decision to increase the CRR included growth in real GDP, acceleration in inflation, expectations of the private corporate sector of higher increase in prices of both inputs and outputs, reports of growing strains on domestic capacity utilisation, and challenges emanating from capital flows and consequent impact on increasing liquidity (see Box 1, Chapter IV). The increase in the CRR is estimated to have absorbed banks' resources to the extent of Rs.13,500 crore.

Expansion in the residency-based new monetary aggregate (NM_3) – which, *inter alia*, does not directly reckon non-resident foreign currency deposits such as India Millennium Deposits (IMDs) and FCNR(B) – was lower than M_3, partly reflecting lower recourse to call/term funding from financial institutions. Growth in liquidity aggregate L_1 was lower than that in NM_3 on account of decline in postal deposits (Chart 11 and Table 17).

Chart 11: Money Supply



Amongst its major components, both currency and time deposits contributed to acceleration in growth in M_3 (Table 18). On a year-on-year basis,

Table 17: Monetary Indicators

(Amount in Rupees crore)

Item	Outstanding as on January 5, 2007	Variation (year-on-year) January 6, 2006 Amount	January 6, 2006 Per cent	January 5, 2007 Amount	January 5, 2007 Per cent
1	2	3	4	5	6
I. Reserve Money*	6,41,790	69,213	14.9	1,06,846	20.0
II. Broad Money (M_3)	30,54,159	3,50,747	16.0	5,17,318	20.4
a) Currency with the Public	4,64,820	53,106	15.4	66,719	16.8
b) Aggregate Deposits	25,83,864	2,97,561	16.2	4,49,751	21.1
i) Demand Deposits	4,06,292	76,065	28.7	65,584	19.2
ii) Time Deposits	21,77,571	2,21,496	14.1	3,84,167	21.4
of which: Non-Resident Foreign Currency Deposits	65,068	-19,944	-26.5	9,658	17.4
III. NM3	30,64,566	3,79,996	17.4	5,04,467	19.7
of which: Call Term Funding from FIs	84,629	16,070	24.6	3,265	4.0
IV. a) L_1	31,20,180	4,02,881	18.1	4,92,888	18.8
of which: Postal Deposits	95,752	17,552	21.0	-5,447	-5.4
b) L_2	31,23,112	4,03,916	18.1	4,92,888	18.7
c) L_3	31,44,806	4,05,712	18.1	4,92,888	18.6
V. Major Sources of Broad Money					
a) Net Bank Credit to the Government (i+ii)	8,02,930	22,088	2.9	21,932	2.8
i) Net Reserve Bank Credit to Government	-312	21,206	-	-19,253	-
of which: to the Centre	-919	22,611	-	-19,845	-
ii) Other Banks' Credit to Government	8,03,242	882	0.1	41,184	5.4
b) Bank Credit to Commercial Sector	19,51,885	3,16,802	26.1	4,20,026	27.4
c) Net Foreign Exchange Assets of Banking Sector	8,28,046	60,495	10.1	1,68,746	25.6
Memo:					
SCBs Aggregate Deposits	23,81,242	2,85,182	17.2	4,38,037	22.5
SCBs Non-food Credit	17,14,396	3,11,013	31.2	4,07,735	31.2

* : Data pertain to January 19, 2007.

SCBs : Scheduled Commercial Banks. FIs : Financial Institutions. NBFCs : Non-Banking Financial Companies.

NM_3 is the residency-based broad money aggregate and L_1, L_2 and L_3 are liquidity aggregates compiled on the recommendations of the Working Group on Money Supply (Chairman: Dr. Y.V. Reddy, 1998). Liquidity aggregates are defined as follows:

L_1 = NM_3 + Select deposits with the post office saving banks.

L_2 = L_1 +Term deposits with term lending institutions and refinancing institutions (FIs) + Term borrowing by FIs + Certificates of deposits issued by FIs.

L_3 = L_2 + Public deposits of non-banking financial companies.

Note : 1. Data are provisional.
2. Liquidity aggregates pertain to end-December 2006.
3. Data reflect redemption of India Millennium Deposits (IMDs) on December 29, 2005.

growth in currency with the public increased from 15.4 per cent as on January 6, 2006 to a peak of 19.4 per cent as on October 27, 2006 before moderating to 16.8 per cent as on January 5, 2007. Acceleration in growth in October 2006 could be partly attributed to the early onset of festival season currency demand during the current year (Table 18).

Growth in aggregate deposits accelerated to 21.1 per cent, y-o-y, as on January 5, 2007 from 16.2 per cent a year ago, on the back of higher accretion to time

Table 18: Monetary Aggregates – Variations

(Rupees crore)

	Variation during									
	2005-06 (April-March)	2005-06 (up to Jan 6)	2006-07 (up to Jan 5)	2005-06 Q1	2005-06 Q2	2005-06 Q3	2005-06 Q4	2006-07 Q1	2006-07 Q2	2006-07 Q3
1	2	3	4	5	6	7	8	9	10	11
M3 (=1+2+3=4+5+6+7-8)	3,96,868 (17.0)	2,04,175 (8.8)	3,24,624 (11.9)	27,448	1,22,456	45,104	2,01,860	55,427	1,65,903	67,757
Components										
1. Currency with the Public	58,272 (16.4)	43,230 (12.2)	51,677 (12.5)	20,492	-10,835	30,124	18,491	23,773	-3,099	27,988
2. Aggregates Deposits with Banks	3,38,037 (17.1)	1,62,637 (8.2)	2,74,350 (11.9)	8,819	1,32,531	15,729	1,80,958	33,271	1,68,549	40,131
2.1 Demand Deposits with Banks	83,861 (26.1)	19,346 (6.0)	1,069 (0.3)	-21,953	41,566	-2,357	66,604	-41,235	41,558	-7,167
2.2 Time Deposits with Banks	2,54,176 (15.4)	1,43,291 (8.7)	2,73,282 (14.4)	30,772	90,965	18,086	1,14,354	74,506	1,26,991	47,298
3. 'Other' Deposits with Banks	560	-1,692	-1,403	-1,862	760	-750	2,411	-1,617	453	-363
Sources										
4 Net Bank Credit to Government	20,386 (2.7)	32,292 (4.3)	33,838 (4.4)	17,398	-5,017	-5,722	13,726	20,933	15,705	-16,375
4.1 RBI's net credit to Government	35,799	46,603	-8,448	18,963	-25,251	19,879	22,208	53	2,826	-12,754
4.1.1 RBI's net credit to Centre	33,374	47,140	-6,079	19,556	-25,251	19,812	19,256	3,071	2,584	-12,568
4.2 Other Banks' Credit to Government	-15,413 (-2.0)	-14,311 (-1.8)	42,286 (5.6)	-1,565	20,234	-25,601	-8,481	20,881	12,879	-3,621
5 Bank Credit to Commercial Sector	3,59,703 (27.0)	2,00,600 (15.1)	2,60,924 (15.4)	10,235	1,18,712	61,731	1,69,025	16,973	1,39,990	79,885
6 Net Foreign Exchange Assets of Banking Sector	78,291	11,397	1,01,852	-12,026	24,062	27,701	38,554	58,087	20,197	27,250
6.1 Net Foreign Exchange Assets of RBI	61,545	6,980	1,06,806	-13,243	24,823	23,741	26,224	71,845	11,392	27,250
7 Governments' Currency Liabilities to the Public	1,306	1,193	-700	384	910	-100	112	-920	155	66
8 Net Non-Monetary liabilities of Banking Sector	62,817	41,308	71,289	-11,456	16,210	38,507	19,557	39,646	10,144	23,069
Memo:										
1 Non-resident Foreign Currency Deposits with SCBs	-16,876	-20,741	5,793	804	187	1,856	-19,723	3,917	1,671	490
2 SCB' Call-term Borrowing from Financial Institutions	11,224	9,443	1,485	-1,002	7,359	1,836	3,031	3,118	-1,576	-4,883
3 Overseas Borrowing by SCBs	1,295	2,198	-3,691	-925	3,618	-622	-775	3,301	-3.685	-2,787

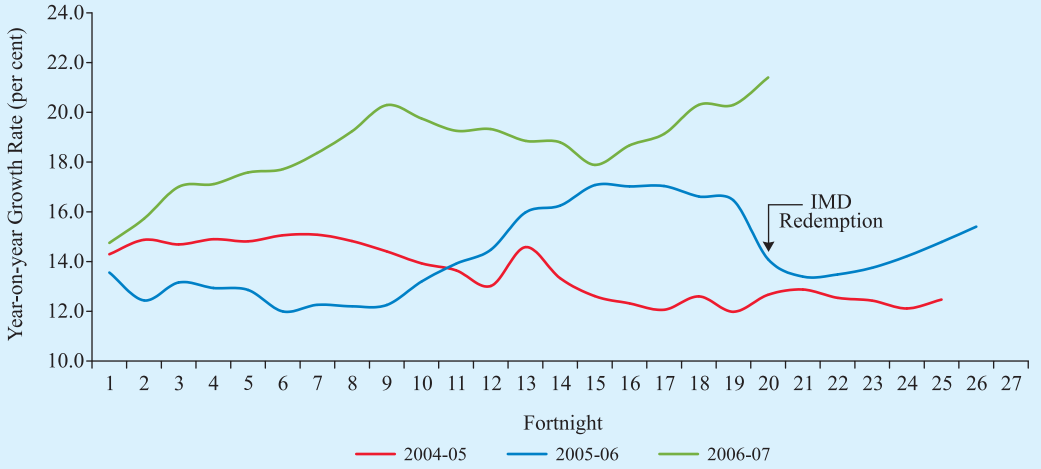
SCBs: Scheduled Commercial Banks.

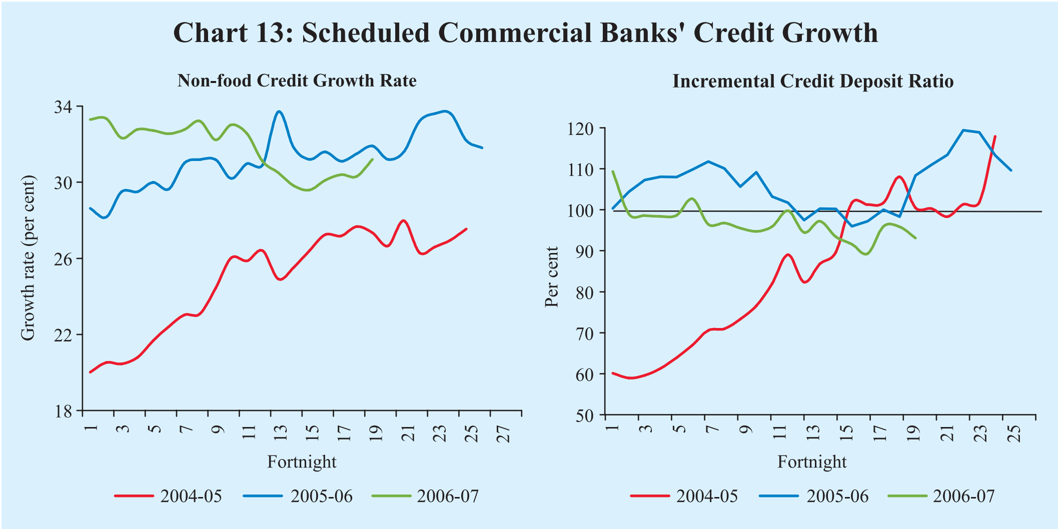
Note: 1. Variation during 2006-07 is worked out from March 31, 2006 whereas the variation during 2005-06 is worked out from April 1, 2005.
2. Figures in parentheses are percentage variations during the fiscal year.
3. Data reflect redemption of India Millennium Deposits (IMDs) on December 29, 2005.

deposits. On a y-o-y basis, growth in demand deposits (19.2 per cent) as on January 5, 2007 was of a lower order than a year ago (28.7 per cent). Accretion to time deposits was, however, significantly higher than that in the previous year (Chart 12). Growth in time deposits of scheduled commercial banks accelerated to 22.9 per cent (y-o-y) as on January 5, 2007 from 15.0 per cent a year ago. This, apart from acceleration in economic activity, could be attributed to higher interest rates on deposits as well as tax benefits. Interest rates on time deposits of 1-3 years maturity offered by public sector banks increased from a range of 5.75-6.75 per cent in March 2006 to 6.75-8.25 per cent in January 2007. Rates offered by private sector banks on deposits of similar maturity increased from a range of 5.50-7.75 per cent to 6.75-9.25 per cent over the same period. Growth in time deposits also appears to have benefited from the recently introduced tax benefits under Section 80C for deposits with maturity of five years and above. Concomitantly, with unchanged interest rates, postal deposits have witnessed a significant decline since end-March 2006.

Commercial sector's demand for bank credit has continued to remain strong during 2006-07 so far. On a year-on-year basis, non-food credit of scheduled commercial banks (SCBs) registered a growth of 31.2 per cent as on January 5, 2007 – the same rate as a year ago. On a fiscal year basis, growth in non-food credit decelerated marginally to 16.9 per cent as on January 5, 2007 from 17.5 per cent a year ago. In view of the acceleration in deposits, the incremental credit-deposit ratio of SCBs, after remaining above/around 100 per cent for the most part since October 2004, has exhibited some moderation in recent months. As on January 5, 2007, the incremental credit-deposit ratio was around 93 per cent (y-o-y) as compared with 108 per cent a year ago (Chart 13). Scheduled commercial banks' food credit has recorded a modest rise (5.9 per cent) during 2006-07 (up to January 5, 2007), reflecting lower order of procurement of foodgrains.

Chart 12: Time Deposits Growth Rate





Disaggregated data available up to October 2006 show that credit growth has been largely broad-based (Table 19). About 34 per cent of incremental non-food credit was absorbed by industry, 12 per cent by agriculture, 15 per cent by loans to the housing sector and another 11 per cent by 'other retail loans'. Loans to commercial real estate, which increased by 84 per cent, y-o-y, absorbed 5 per cent of incremental non-food credit.

Apart from bank credit, the corporate sector continued to rely on non-bank sources of funds for financing their requirements. Resources raised through domestic equity issuances during the first nine months of 2006-07 (Rs 23,843 crore) were more than double of that in the corresponding period of 2005-06. After remaining subdued during the second quarter, amounts raised from the primary market picked up during the third quarter of 2006-07. Mobilisation of resources through equity issuances abroad (ADRs/GDRs) during April-December 2006 (Rs.8,019 crore) were 55 per cent higher than that in the same period of 2005. Recourse to external commercial borrowings (ECBs) during the first half of 2006-07 was almost double of that in the corresponding period of 2005-06, with net disbursements under ECBs increasing from Rs.17,551 crore during April-September 2005 to Rs.34,031 crore during April-September 2006. Mobilisation through issuances of commercial papers during April-December 2006 was more than three times of that a year ago, notwithstanding some sluggishness in the third quarter. Finally, internal sources of funds continued to provide large financing support to the domestic corporate sector during the first half of 2006-07. Profits after tax of select non-financial non-government companies during April-September 2006 were almost 40 per cent higher than those in the first half of 2005-06. Profits after tax during the second quarter of 2006-07 were higher than those in each of the five preceding quarters (Table 20).

Table 19: Deployment of Non-food Bank Credit

(Amount in Rupees crore)

Sector/Industry	Outstanding as on October 27, 2006	Year-on-year Variations 2005-06 (October 28, 2005 over October 29, 2004)		2006-07 (October 27, 2006 over October 28, 2005)	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
Non-food Gross Bank Credit (1 to 4)	**15,37,978**	**2,66,092**	**32.4**	**3,51,904**	**29.7**
1. Agriculture and Allied Activities	**1,86,533**	**37,867**	**37.2**	**43,919**	**30.8**
2. Industry (Small, Medium and Large)	**5,95,310**	**81,666**	**24.0**	**1,18,481**	**24.8**
Small Scale Industries	94,518	10,641	15.8	15,976	20.3
3. Personal Loans	**3,98,055**	**n.a.**	**n.a.**	**1,01,631**	**34.3**
Housing	2,09,468	n.a.	n.a.	51,191	32.3
Advances against Fixed Deposits	33,744	4,957	19.3	3,005	9.8
Credit Cards	11,870	n.a.	n.a.	4,016	51.1
Education	12,692	n.a.	n.a.	4,435	53.7
Consumer Durables	9,291	195	2.7	804	9.5
4. Others	**3,58,080**	**n.a.**	**n.a.**	**87,873**	**32.5**
Transport Operators	20,671	n.a.	n.a.	9,673	88.0
Professional and Others	18,286	n.a.	n.a.	5,978	48.6
Trade	90,855	n.a.	n.a.	25,593	39.2
Real Estate Loans	37,838	n.a.	n.a.	17,260	83.9
Non-Banking Financial Companies	33,317	5,791	33.3	7,453	28.8
Memo:					
Priority Sector	**5,41,017**	**1,30,751**	**45.1**	**1,08,056**	**25.0**
Industry (Small, Medium and Large)	**5,95,310**	**81,666**	**24.0**	**1,18,481**	**24.8**
Food Processing	32,399	3,301	16.2	6,181	23.6
Textiles	65,203	9,647	28.3	16,631	34.2
Paper and Paper Products	10,179	787	12.8	2,139	26.6
Petroleum, Coal Products and Nuclear Fuels	29,423	3,566	22.6	8,708	42.0
Chemical and Chemical Products	51,476	3,584	12.0	10,916	26.9
Rubber, Plastic and their Products	7,757	2,302	81.0	2,260	41.1
Iron and Steel	56,693	9,529	36.2	14,554	34.5
Other Metal and Metal Products	18,638	3,001	32.7	4,817	34.9
Engineering	37,803	4,562	18.0	5,008	15.3
Vehicles, Vehicle Parts and Transport Equipments	19,154	5,335	95.9	3,302	20.8
Gems and Jewellery	22,474	3,802	33.1	4,014	21.7
Construction	16,079	2,366	30.8	5,321	49.5
Infrastructure	1,18,840	23,814	36.4	22,353	23.2

n.a. : Not available.

Note: 1. Data are provisional and relate to select scheduled commercial banks.
2. Owing to change in classification of sectors/industries and coverage of banks, data for 2006 are not comparable with earlier data.

In the fiscal year 2006-07 (up to January 5, 2007), commercial banks' investments in gilts witnessed a large expansion of Rs.43,222 crore in contrast to a decline of Rs.15,580 crore a year ago, reflecting the need to meet statutory requirements. On a y-o-y basis, commercial banks' investments in gilts increased by 5.6 per cent as against a decline of 0.1 per cent a year ago (Table 21). Over the same period, growth in commercial banks' NDTL accelerated to 20.7 per cent from 18.3 per cent a year ago. With incremental investment in gilts not keeping pace with the high growth in NDTL, commercial banks' holdings of Government securities

Table 20: Select Sources of Funds to Industry

(Rupees crore)

Item	2005-06 (April-March)	2005-06 April-December @	2006-07 April-December @	2005-06 Q1	2005-06 Q2	2005-06 Q3	2005-06 Q4	2006-07 Q1	2006-07 Q2	2006-07 Q3
1	2	3	4	5	6	7	8	9	10	11
A. Bank Credit to Industry #	1,22,165	39,209	46,566	11,148	28,061	24,484	58,472	-2,724	49,290	-
B. Flow from Non-banks to Corporates										
1. Capital Issues (i+ii)	13,871	9,571	24,334	1,264	2,758	5,549	4,210	10,627	1,882	11,825
i) Non-Government Public Ltd. Companies (a+b)	13,408	9,571	24,334	1,264	2,758	5,549	3,837	10,627	1,882	11,825
a) Bonds/Debentures	245	118	491	118	0	0	127	0	0	491
b) Shares	13,163	9,453	23,843	1,146	2,758	5,549	3,710	10,627	1,882	11,334
ii) PSUs and Government Companies	373	0	0	0	0	0	373	0	0	0
2. ADR/GDR Issues	7,263	5,171	8,019	789	739	3,643	2,092	4,965	2,130	924
3. External Commercial Borrowings (ECBs)	45,078	17,551	34,031	4,317	13,234	9,677	17,850	20,366	13,665	-
4. Issue of CPs	-1,517	2,999	10,618	3,562	1928	-2,491	-4,516	6,931	4,795	-1,108
C. Depreciation Provision +	28,883	13,625	15,710	7,137	7,617	7,748	8,340	8,449	8.892	-
D. Profit after Tax +	67,506	32,016	44,927	16,726	18,169	18,790	21,634	24,845	27,710	-

: Data pertain to select scheduled commercial banks. Figures for 2005-06 are not comparable with those of 2006-07 due to increase in number of banks selected in the sample.

+ : Data are based on audited/ unaudited abridged results of select non-Government non-financial listed public limited companies. Quarterly variations may not add up to annual or half-yearly variations due to difference in coverage of companies.

@ : Data for bank credit, ECBs, depreciation provision and profit after tax pertain to April-September.

Note: 1. Data are provisional.
2. Data on capital issues pertain to gross issuances excluding issues by banks and financial institutions. Figures are not adjusted for banks' investments in capital issues, which are not expected to be significant.
3. Data on ADR/GDR issues exclude issuances by banks and financial institutions.
4. Data on ECBs include short-term credit. Data for 2005-06 are exclusive of the IMD redemption.

declined to 28.6 per cent of their NDTL as on January 5, 2007 from 31.3 per cent at end-March 2006 and 32.6 per cent a year ago (Chart 14). Excess SLR investments

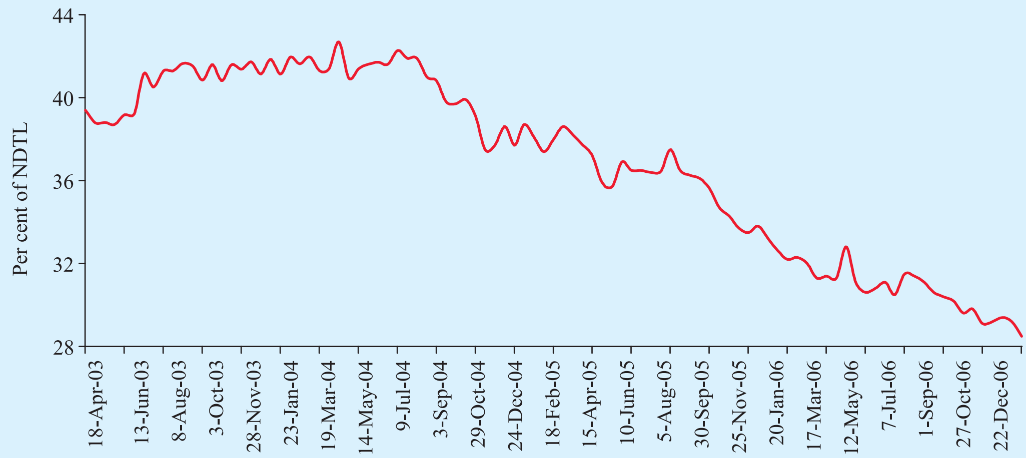
Table 21: Scheduled Commercial Banks' Survey

(Amount in Rupees crore)

Item	Outstanding as on January 5, 2007	Variation (year-on-year) As on Jan 6, 2006 Amount	As on Jan 6, 2006 Per cent	As on Jan 5, 2007 Amount	As on Jan 5, 2007 Per cent
1	2	3	4	5	6
Sources of Funds					
1. Aggregate Deposits	23,81,242	2,85,182	17.2	4,38,037	22.5
2. Call/Term Funding from Financial Institutions	84,629	16,070	24.6	3,265	4.0
3. Overseas Foreign Currency Borrowings	26,143	5,644	22.5	-4,595	-14.9
4. Capital and Reserves	1,96,070	39,528	30.3	26,034	15.3
Uses of Funds					
1. Bank Credit	17,57,479	3,09,053	29.7	4,07,718	30.2
of which: Non-food Credit	17,14,396	3,11,013	31.2	4,07,735	31.2
2. Investments in Government Papers	7,43,964	-729	-0.1	39,288	5.6
3. Investments in Other Approved Securities	21,821	-2,710	-13.1	3,793	21.0
4. Investments in Non-SLR Securities	1,39,237	-11,957	-8.6	11,761	9.2
5. Foreign Currency Assets	50,617	7,388	23.1	11,261	28.6
6. Balances with the RBI	1,30,341	19,399	23.7	29,223	28.9

Note: Data are provisional.

Chart 14: SLR Investments by Scheduled Commercial Banks

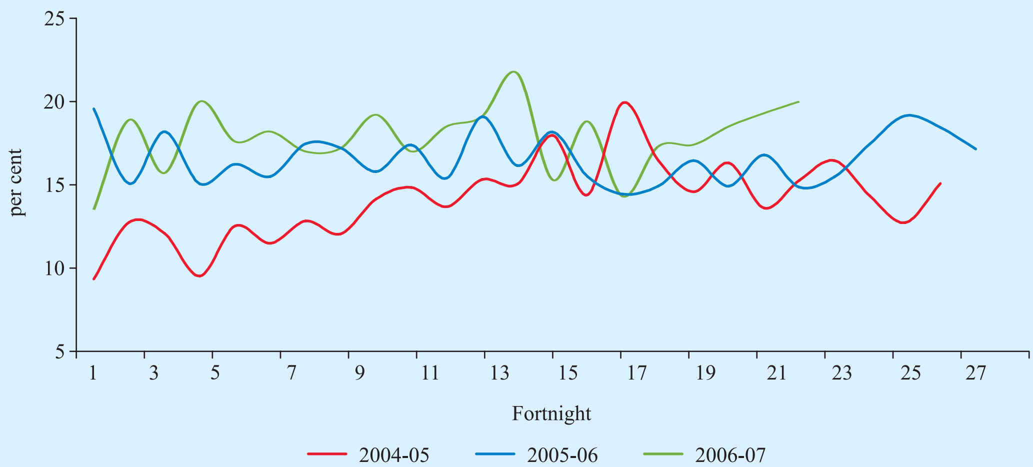


of SCBs fell to Rs.96,407 crore as on January 5, 2007 from Rs.1,68,029 crore a year ago. Funds raised through equity issuances in the primary market as well as higher internal reserves also enabled banks to fund strong credit demand.

Reserve Money Survey

Reserve money expanded by 20.0 per cent, y-o-y, as on January 19, 2007 as compared with 14.9 per cent a year ago (Chart 15). Adjusted for the first round effect of the hike in the CRR, reserve money growth was 17.4 per cent as on January 19, 2007. Reserve money movements over the course of the year reflected the Reserve Bank's market operations.

Chart 15: Reserve Money Growth



The Reserve Bank's foreign currency assets (net of revaluation) increased by Rs.80,166 crore during the fiscal year 2006-07 (up to January 19, 2007) as compared with an increase of Rs.11,185 crore during the corresponding period of the previous year (Table 22 and Chart 16).

Mirroring the liquidity management operations through LAF, the Reserve Bank's holdings of Government securities increased by Rs.10,615 crore during 2006-07 (up to January 19, 2007) as against an increase of Rs.27,435 crore in the corresponding period of 2005-06. During 2006-07 so far, Central Government

Table 22: Variation in Reserve Money

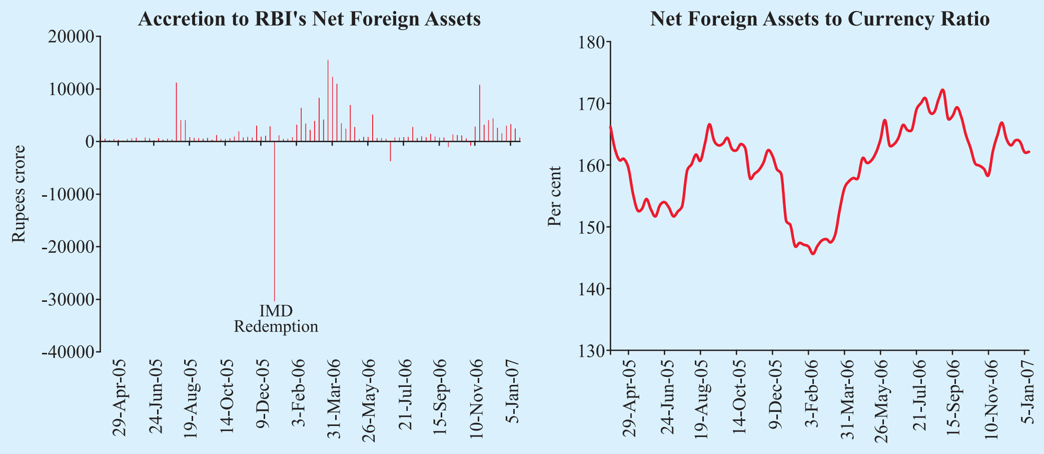
(Rupees crore)

Item	Outstanding as on Jan. 19, 2007	Variation during									
		2005-06		2006-07	2005-06				2006-07		
		(April-March)	(up to Jan.20)	(up to Jan.19)	Q1	Q2	Q3	Q4	Q1	Q2	Q3
1	2	3	4	5	6	7	8	9	10	11	12
Reserve Money	6,41,790	83,930 (17.2)	45,809 (9.4)	68,724 (12.0)	7,177	1,061	25,438	50,254	13,463	18,666	14,243
Components (1+2+3)											
1. Currency in Circulation	4,88,251	62,015 (16.8)	48,574 (13.2)	57,575 (13.4)	19,877	-9,479	29,154	22,462	22,283	-2,011	26,771
2. Bankers' Deposits with RBI	1,47,830	21,515	-870	12,319	-10,680	9,780	-2,967	25,382	-7,204	20,224	-12,165
3. Other Deposits with the RBI	5,709	401	-1,896	-1,170	-2,021	760	-750	2,411	-1,617	453	-363
Sources (1+2+3+4-5)											
1. RBI's net credit to Government	12,242	26,111	45,297	4,106	9,275	-25,251	19,879	22,208	53	2,826	-12,754
of which: to Centre (i+ii+iii+iv-v)	12,123	28,417	50,622	6,963	14,600	-25,251	19,812	19,256	3,071	2,584	-12,568
i. Loans and Advances	0	0	0	0	0	0	0	0	0	0	0
ii. Treasury Bills held by the RBI	0	0	0	0	0	0	0	0	0	0	0
iii. RBI's Holdings of Dated Securities	81,024	13,869	27,435	10,615	8,221	-17,243	19,378	3,513	-27,610	24,944	22,733
iv. RBI's Holdings of Rupee coins	117	7	73	-37	-40	-33	157	-77	9	-107	97
v. Central Government Deposits	69,018	-14541	-23,113	3,615	-6,419	7,974	-277	-15,820	-30,672	22,253	35,398
2. RBI's credit to banks and commercial sector	9,711	535	1,776	2,528	1,155	-1,869	101	1,148	-3,135	3,107	2,065
3. NFEA of RBI	7,87,321	60,193 (9.8)	2,043 (0.3)	1,14,337 (17.0)	-14,595	24,823	23,741	26,224	71,845	11,392	27,250
of which: FCA, adjusted for revaluation		68,834	11,185	80,166	5,034	23,665	11,998	28,137	28,107	10,948	31,634
4. Governments' Currency Liabilities to the Public	8,054	1,306	1,216	-700	384	910	-100	112	-920	155	66
5. Net Non-Monetary liabilities of RBI	1,75,537	4,215	4,524	51,547	-10,957	-2,449	18,183	-562	54,380	-1,186	2,384
Memo:											
Net Domestic Assets	-1,45,531	23,737	43,766	-45,613	21,771	-23,761	1,697	24,030	-58,382	7,274	-13,007
Reserve Bank's Primary Subscription to Dated Securities		10,000	0	0	0	0	0	10,000	0	0	0
LAF, Repos (+) / Reverse Repos (-)	11,810	12,080	33,100	19,060	9,660	-14,835	18,635	-1,380	-23,060	28,395	22,195
Net Open Market Sales #		3,913	3,405	3,656	1,543	941	261	1,168	1,536	1,176	389
Mobilisation under MSS	40,491	-35,149	-24,508	11,429	7,469	-4,353	-19,713	-18,552	4,062	8,940	-3,315
Net Purchases(+)/Sales(-) from Authorised Dealers		32,884	-14,932	35,901@	0	17,027	0	15,857	21,545	0	14,356@
NFEA/RM (per cent) (end-period)	122.7	117.4	114.9	122.7	120.5	125.3	123.7	117.4	127.0	125.0	126.5
NFEA/Currency (per cent) (end-period)	161.3	156.3	147.4	161.3	154.0	164.4	158.4	156.3	164.4	167.7	164.0

NFEA : Net Foreign Exchange Assets. FCA : Foreign Currency Assets. @ : up to end-November 2006.
* : At face value. # : Excludes Treasury Bills $: Adjusted for Centre's surplus investment.

Note: 1. Data are based on March 31 for Q4 and last reporting Friday for all other quarters.
2. Figures in parentheses are percentage variations during the fiscal year.

Chart 16: RBI's Net Foreign Assets



deposits with the Reserve Bank have increased by Rs.3,615 crore. The Reserve Bank's net credit to the Centre, thus, increased by Rs.6,963 crore during the fiscal year 2006-07 (up to January 19, 2007) as against an increase of Rs.50,622 crore during the corresponding period of 2005-06 (see Table 22).

Liquidity Management

The Reserve Bank continued to ensure that appropriate liquidity is maintained in the system so that all legitimate requirements of credit are met, particularly for productive purposes, consistent with the objective of price and financial stability. Towards this end, the Reserve Bank continued with its policy of active demand management of liquidity through OMO including MSS, LAF and CRR, and using all the policy instruments at its disposal flexibly. However, liquidity management emerged to be more complex during the past year, with greater variation in market liquidity, largely reflecting variations in cash balances of the Governments and capital flows.

During the first quarter, unwinding of the Centre's surplus balances with the Reserve Bank and the Reserve Bank's purchase of foreign exchange from authorised dealers led to ample liquidity into the banking system. This was mirrored in an increase in the LAF reverse repo balances. However, in view of some build-up of Centre's cash balances with the Reserve Bank during August 2006, the absorption under LAF reverse repos witnessed some decline during the second quarter.

Beginning mid-September 2006, liquidity conditions turned tight on account of advance tax outflows and festival season currency demand. The Reserve Bank injected liquidity through repos on eight occasions between mid-September 2006 and end-October 2006. However, net injection of liquidity was witnessed only on two occasions (October 20 and October 23, 2006). Liquidity pressures

Table 23: Reserve Bank's Liquidity Management Operations

(Rupees crore)

Item	2005-06 (April-March)	2006-07 (April-Jan 19)	Variations during 2006-07 Q1	Q2	Q3	Oct.	Nov.	Dec.
1	2	3	4	5	6	7	8	9
A. Drivers of Liquidity (1+2+3+4)	**-31,719**	**2,678**	**36,271**	**-16,675**	**-26,143**	**-8,006**	**8,552**	**-26,689**
1. RBI's Foreign Currency Assets (adjusted for revaluation)	68,834	80,166	28,517	10,538	34,821	4,031	17,066	13,724
2. Currency with the Public	-57,280	-58,870	-19,624	-1,049	-27,435	-18,228	-170	-9,038
3. Surplus Cash balances of the Centre with the Reserve Bank	-22,726	401	40,207	-26,199	-30,761	8,953	-5,437	-34,277
4. Others (residual)	-20,547	-19,019	-12,828	36	-2,767	-2,762	-2,908	2,902
B. Management of Liquidity (5+6+7+8)	**57,969**	**-5,154**	**-39,003**	**32,026**	**31,625**	**-8,382**	**-1,541**	**41,548**
5. Liquidity impact of LAF Repos	12,080	19,060	-35,315	40,650	33,600	-10,355	-3,725	47,680
6. Liquidity impact of OMOs (Net) *	10,740	715	545	145	25	0	10	15
7. Liquidity impact of MSS	35,149	-11,429	-4,232	-8,769	4,750	1,973	2,174	603
8. First round liquidity impact due to CRR change	0	-13,500	0	0	-6,750	0	0	-6,750
C. Bank Reserves (A+B) #	**26,250**	**-2,476**	**-2,732**	**15,351**	**5,482**	**-16,388**	**7,011**	**14,859**

(+) : Indicates injection of liquidity into the banking system.
(-) : Indicates absorption of liquidity from the banking system.
: Includes vault cash with banks and adjusted for first round liquidity impact due to CRR change.
* : Adjusted for Consolidated Sinking Funds (CSF) and Other Investments and including private placement.
Note : Data pertain to March 31 and last Friday for all other months.

eased by end-October 2006 following some decline in Centre's surplus cash balances (Table 24). Liquidity conditions eased during November 2006, partly

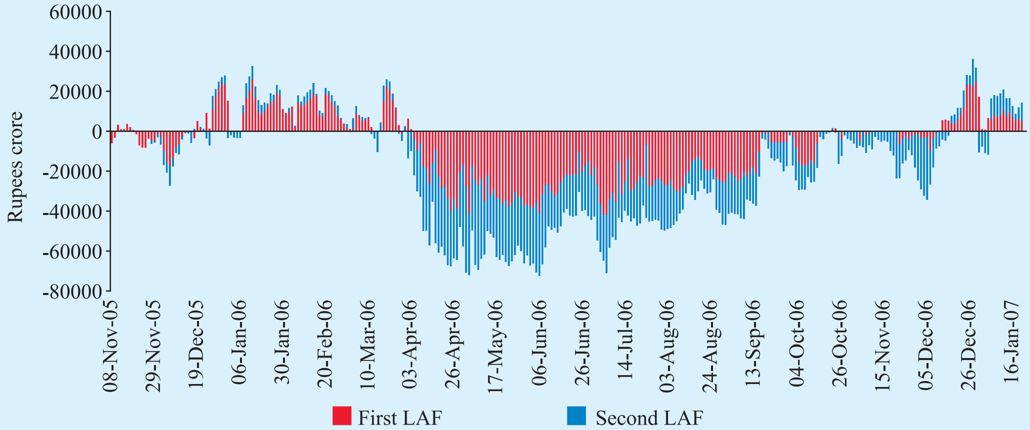
Table 24: Liquidity Management

(Rupees crore)

Outstanding as on last Friday of	LAF	MSS	Centre's Surplus with the RBI @	Total (2 to 4)
1	2	3	4	5
2005				
March*	19,330	64,211	26,102	1,09,643
April	27,650	67,087	6,449	1,01,186
May	33,120	69,016	7,974	1,10,110
June	9,670	71,681	21,745	1,03,096
July	18,895	68,765	16,093	1,03,753
August	25,435	76,936	23,562	1,25,933
September	24,505	67,328	34,073	1,25,906
October	20,840	69,752	21,498	1,12,090
November	3,685	64,332	33,302	1,01,319
December	-27,755	46,112	45,855	64,212
2006				
January	-20,555	37,280	39,080	55,805
February	-12,715	31,958	37,013	56,256
March*	7,250	29,062	48,828	85,140
April	47,805	24,276	5,611	77,692
May	57,245	27,817	0	85,062
June	42,565	33,295	8,621	84,481
July	44,155	38,995	8,770	91,920
August	23,985	42,364	26,791	93,140
September	1,915	42,064	34,821	78,800
October	12,270	40,091	25,868	78,229
November	15,995	37,917	31,305	85,217
December	-31,685	37,314	65,582	71,211
January (as on 19th)	-11,810	40,491	48,428	77,109

@ : Excludes minimum cash balances with the Reserve Bank. * : Data pertain to March 31.
Note : Negative sign in column 2 indicates injection of liquidity through LAF repo.

Chart 17: Repo (+)/ Reverse Repo (-) under LAF

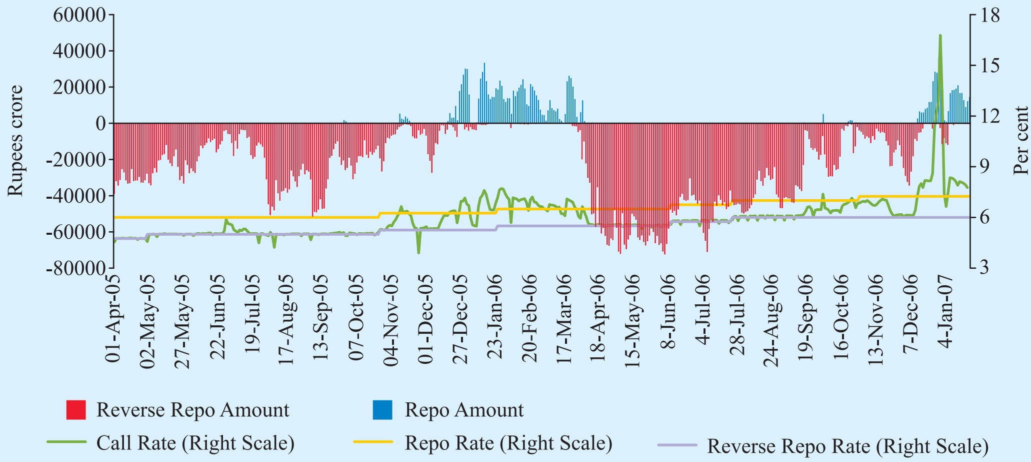


Note: Additional LAF on March 31, 2006 between 9:00 PM and 9:30 PM is shown under second LAF.

reflecting market purchases of foreign exchange by the Reserve Bank. This was mirrored in balances under LAF reverse repos, which increased to Rs 34,255 crore as on December 6, 2006 (Chart 17).

Liquidity conditions, however, turned tight from the second week of December 2006 largely due to payments for auctioned Central Government securities, advance tax outflows (with concomitant increase in the Centre's surplus cash balances with the Reserve Bank from Rs.42,716 crore as on December 15, 2006 to Rs.73,634 crore as on December 22, 2006), and the increase in the CRR by 50 basis points in two phases. In view of the prevailing liquidity conditions, the Reserve Bank injected liquidity into the system through repo operations from December 12, 2006 (Chart 18). Average

Chart 18: Liquidity Adjustment Facility and Call Rate



daily net injection of liquidity by the Reserve Bank increased from Rs.5,615 crore during December 13-21, 2006 to Rs.25,585 crore during December 22-29, 2006, in contrast to the average daily absorption of Rs.12,262 crore and Rs.9,937 crore during October 2006 and November 2006, respectively. Average daily net injection of liquidity by the Reserve Bank moderated to Rs.10,814 crore during January 2007 (up to January 20, 2007), as liquidity pressures eased partly on account of reduction in the Centre's balance with the Reserve Bank from Rs.65,682 crore as on December 29, 2006 to Rs 48,528 crore as on January 19, 2007. Net outstanding balance under LAF repos was Rs.10,190 crore as on January 24, 2007.

IV. PRICE SITUATION

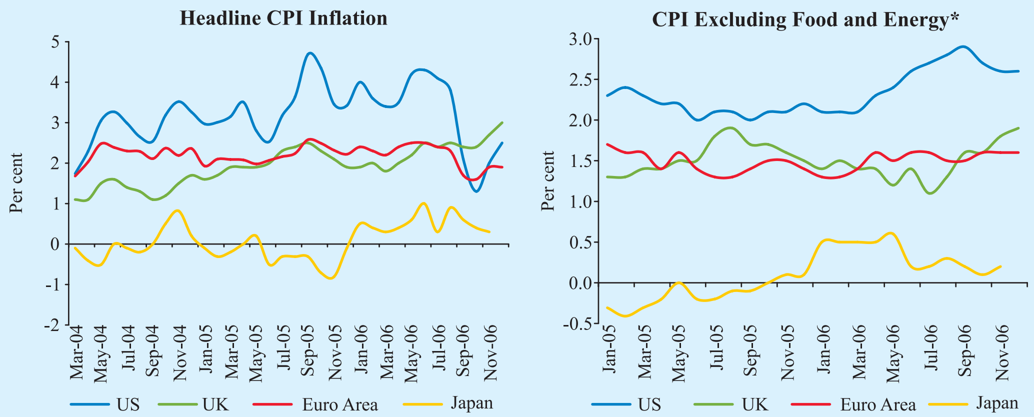
Headline inflation in major advanced economies eased during September-October 2006-07 in tandem with the softening of international crude oil prices. However, inflation again increased during November-December 2006 and core inflation still remains at elevated levels in many economies. Many central banks continued with pre-emptive monetary tightening to mitigate the second round effects, especially in the face of continuing strong demand. Several central banks such as the European Central Bank (ECB), the Bank of England, the Reserve Bank of Australia and the South African Reserve Bank have raised their policy rates since end-September 2006. The US Fed, however, has left its rates unchanged since end-June 2006 in view of slowing down of economic activity.

In India, prices of primary food articles and manufactured products posed upward pressures on headline inflation during the quarter. Wholesale price inflation was 6.0 per cent as on January 13, 2007 as compared with 4.1 per cent at end-March 2006. Pre-emptive monetary and fiscal measures along with the moderation in fuel prices could have helped to some extent in containing inflationary expectations, although underlying inflationary pressures remain. Measures of consumer price inflation remain at elevated levels, mainly reflecting the impact of food prices.

Global Inflation

Headline inflation in major advanced economies eased during September-October 2006 on the back of base effects as well as the sharp decline in international crude oil prices but again rose during November-December 2006 (Chart 19). Consumer price inflation in the OECD countries moderated from 3.2 per cent in June 2006 to 1.7 per cent in October 2006 before rising to 2.1 per cent in November 2006. Amongst major economies, headline inflation in the US eased from 4.3 per cent in June 2006 to 1.3 per cent in October 2006 before increasing to 2.5 per cent in December 2006. Similarly, in the euro area, inflation which remained above the target of 'below but close to 2.0 per cent' till August 2006, moderated to 1.6 per cent in October 2006 before increasing again to 1.9 per cent in December 2006. Notwithstanding some moderation in headline inflation, core inflation still remains firm in major economies. CPI inflation (excluding food and energy) was 2.6 per cent in the US in December 2006 (2.2 per cent a year ago) and 2.2 per cent in November 2006 (1.9 per cent a year ago) in the OECD countries. Many central banks have, therefore, continued to tighten monetary policies in order to contain inflation and inflationary expectations, especially in view of continued strength of demand and possible stronger pass-through of past increases in oil prices.

Chart 19: Headline CPI Inflation



*: Data for Japan is excluding fresh food only.
Source: International Financial Statistics and official websites of respective countries.

The US Fed has paused at each of its three meetings held since end-June 2006, after having raised its target federal funds rate by 425 basis points since the tightening began in June 2004 (Chart 20 and Table 25). Economic growth has moderated from its strong pace earlier this year, partly reflecting a cooling of the housing market. Although core inflation has remained elevated in recent months, and the high level of resource utilisation has the potential to sustain inflation pressures, the Fed sees inflation pressures likely to moderate over time, reflecting reduced impetus from energy prices, contained inflation expectations, and the cumulative effects of monetary policy actions and other factors restraining aggregate demand. The Federal Open Market Committee has indicated that the

Chart 20: Central Bank Policy Rates

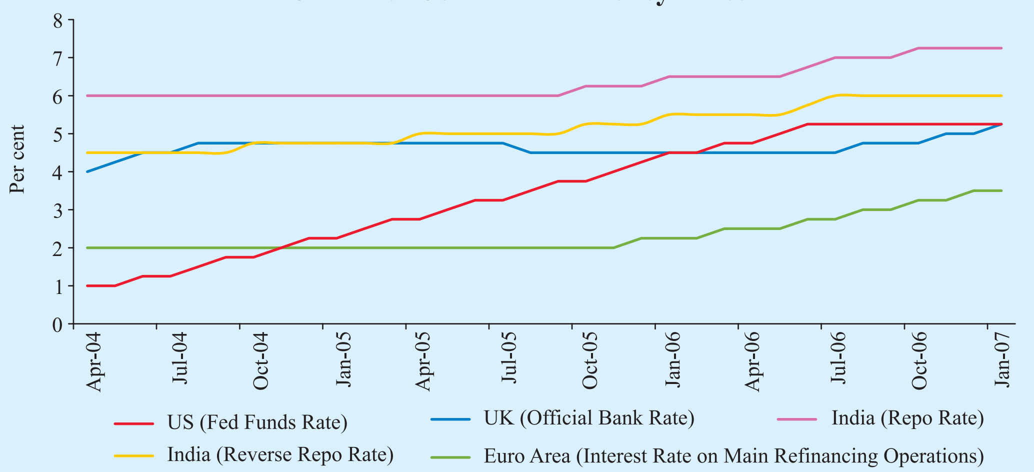


Table 25: Global Inflation Indicators

(Per cent)

Country/ Region	Key Policy Rate	Policy Rates (As on January 23, 2007)	Changes in Policy Rates (basis points)		CPI Inflation (y-o-y)		Growth (y-o-y)	
			Since end-March 2005	Since end-March 2006	2005 (Dec.)	2006 (Dec.)	2005 (Q3)	2006 (Q3)
1	2	3	4	5	6	7	8	9
Developed Economies								
Australia	Cash Rate	6.25 (Nov. 8, 2006)	75	75	2.8	3.3 #	2.6	2.2
Canada	Overnight Rate	4.25 (May 24, 2006)	175	50	2.0	1.4 *	2.8	2.5
Euro area	Interest Rate on Main Refinancing Operations	3.50 (Dec. 7, 2006)	150	100	2.2	1.9	1.6	2.7
Japan	Uncollateralised Overnight Call Rate	0.25 (July 14, 2006)	**	25	-1.0	0.3 *	2.6	1.6
UK	Official Bank Rate	5.25 (Jan. 11, 2007)	50	75	1.9	3.0	1.9	2.9
US	Federal Funds Rate	5.25 (June 29, 2006)	250	50	3.4	2.5	3.4	3.0
Developing Economies								
Brazil	Selic Rate	13.25 (Nov. 29, 2006)	(-)600	(-)325	5.7	3.1	1.0	3.2
India	Reverse Repo Rate	6.00 (July 25, 2006)	125	50	5.3	6.3 *	8.4	9.2
	Repo Rate	7.25 (Oct. 31, 2006)	125	75				
Indonesia	BI Rate	9.50 (Jan. 4, 2007)	100 @	(-)325	17.1	6.6	5.6	5.5
Israel	Key Rate	4.50 (Dec. 25, 2006)	100	(-)25	2.4	-0.1	5.7	4.6
Korea	Overnight Call Rate	4.50 (Aug. 10, 2006)	125	50	2.7	2.1	5.3	4.0 #
Philippines	Reverse Repo Rate	7.50 (Oct. 20, 2005)	75	0	6.7	4.3	4.1	4.8
South Africa	Repo Rate	9.00 (Dec. 8, 2006)	150	200	3.4	5.4 *	4.9	4.5
Thailand	14-day Repurchase Rate	5.00 (June 7, 2006)	275	50	5.8	3.5	5.5	4.7
	1-day Repurchase Rate	4.75 (Jan. 17, 2007)	–	(-)19	&			

@ : Change since July 2005 when Bank Indonesia adopted BI rate as the reference rate with the formal adoption of inflation targeting.

* : November. #: Q4 of 2006.

** : The Bank of Japan decided on March 9, 2006 to change the operating target of money market operations from the outstanding balance of current accounts at the Bank to the uncollateralised overnight call rate.

& : Change over January 16, 2007. Effective January 17, 2007, the 1-day repurchase rate replaced the 14-day repurchase rate as the policy rate.

Note : 1. For India, data on inflation pertain to CPI for Industrial Workers.
2. Figures in parentheses in column (3) give the date when the policy rates were last revised.

Source : International Monetary Fund, websites of respective central banks and the Economist.

extent and timing of any additional firming, that may be needed to address the inflation risks, will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information.

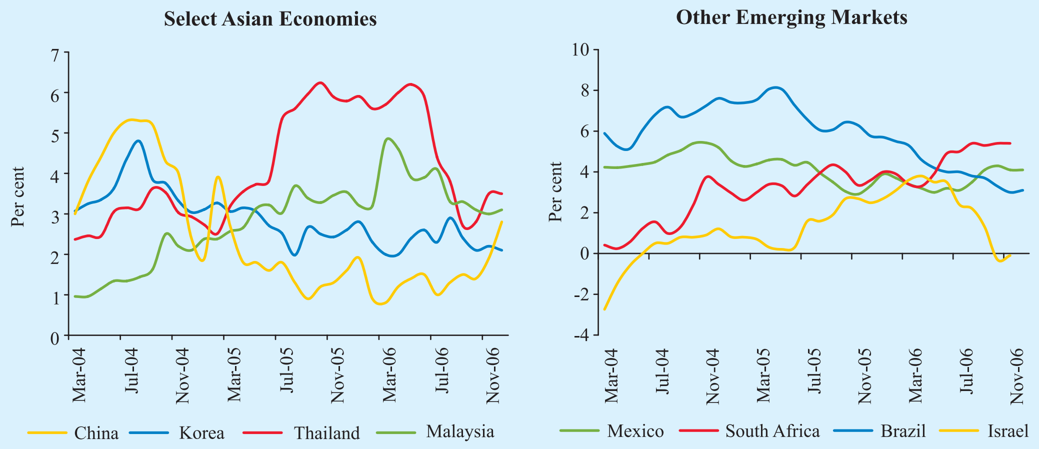
In the euro area, notwithstanding some easing in inflation from August 2006, risks to the price outlook are seen on the upside due to the possibility of stronger pass-through of past oil price rises, the possibility of renewed oil price increases, additional increases in administered prices and indirect taxes and stronger than currently expected wage developments. The European Central Bank (ECB), therefore, raised the key policy rate by 25 basis points each in October and December 2006 – a total increase of 150 basis points since the tightening began in December 2005 – to keep medium to long-term inflation expectations in the euro area anchored to levels consistent with price stability.

In the UK, CPI Inflation increased from 2.4 per cent in September 2006 to 3.0 per cent in December 2006. In view of strong economic activity, limited spare capacity, rapid growth of broad money and credit, continued rise in asset prices and expectations about inflation remaining above the target in the near term, the Bank of England raised its policy rate by 25 basis points each in August 2006, November 2006 and January 2007 to 5.25 per cent. The Reserve Bank of Australia raised its policy rate further by 25 basis points in November 2006 to 6.25 per cent – a total increase of 75 basis points since May 2006 – in response to strong economic activity and underlying inflation pressures. In Japan, the Bank of Japan (BoJ) has kept the uncollateralised overnight call rate (adopted as the operating target of monetary policy since March 2006) unchanged since July 14, 2006, when the rate was increased by 25 basis points.

Inflation remains relatively modest in several economies in Asia, reflecting both pre-emptive monetary tightening over the past 18 months as well as appreciation of the exchange rates. However, there is an emerging concern regarding excess liquidity arising particularly from large external capital flows.

Consumer price inflation in China increased to 2.8 per cent in December 2006 from 1.9 per cent a year ago (Chart 21). Real GDP growth remains strong, although it exhibited some deceleration in the second half of 2006 from the pace recorded in the first half of 2006. Nonetheless, growth during the calendar year

Chart 21: Consumer Price Inflation - Emerging Market Economies



2006 at 10.7 per cent exceeded that of 10.4 per cent in the previous year. Growth in fixed investment decelerated in 2006, but still remains large. In view of stronger growth in money supply and credit, the People's Bank of China increased the benchmark 1-year lending rate by 27 basis points each in April 2006 and August 2006. It has also raised the cash reserve ratio by 200 basis points since July 2006 in four steps - 50 basis points each effective July 5, 2006, August 15, 2006, November 15, 2006 and January 15, 2007 - to 9.5 per cent. Since the beginning of 2006, the Government has also introduced a series of industrial structure adjustments and trade policies - such as terminating/lowering the export tax rebate for non-ferrous metals and scraps - to curb the export of high energy-consuming and high-polluting sectors and resources. In response to the sharp rise in foreign investment in the real estate sector and the purchase of housing by overseas institutions and individuals, measures were taken by the authorities in July 2006 to regulate foreign investment in China's real estate market. The Monetary Policy Committee of the People's Bank of China has suggested that measures should be taken to strengthen macro-management, maintain continuity and stability of various macroeconomic policies, boost domestic demand, control investment growth at a reasonable level and improve investment structure. The Committee has indicated that efforts will be made to keep money and credit growth at an appropriate level and promote optimal credit structure. The managed floating exchange rate regime will be further improved in a self-initiated, controllable and gradual manner to give market supply and demand a fundamental role in the formation of RMB exchange rate and keep RMB exchange rate broadly stable at an adaptive and equilibrium level.

In Korea, exports continue to show steady growth, while private consumption is exhibiting a slowdown in the pace of its expansion. Real GDP growth moderated to 4.0 per cent in the quarter ended December 2006 from 4.8 per cent in the preceding quarter and 5.3 per cent a year ago. Consumer price inflation and core inflation both remain stable. The Bank of Korea has, therefore, kept its policy rate unchanged at 4.5 per cent since August 2006 (after having raised the rates by 125 basis points since the tightening began in October 2005). However, monetary and credit aggregates, and financial institutions liquidity have witnessed a sharp growth, led by inflows of foreign funds. The Bank of Korea, therefore, decided to increase the average reserve requirement ratio by widening the difference in reserve requirement ratios between short-term and long-term deposits. The reserve requirement ratio on demand deposits and money market deposit accounts was increased from 5.0 per cent to 7.0 per cent, effective December 23, 2006. The cash reserve ratio on time deposits, instalment savings deposits, mutual instalment deposits, housing instalment deposits, and certificates of deposits was kept unchanged at 2.0 per cent, while long-term time and savings deposits were exempted from the existing 1.0 per cent requirement. Following this adjustment, the average reserve requirement ratio has risen from 3.0 per cent to 3.8 per cent. As a result of the adjustment in the cash reserve ratio, the Bank of Korea expects that the pace of liquidity expansion will slow. It also expects that the short-term bias of financial institutions' deposit structures will lessen, as incentives for long-term deposits are strengthened in response to the widened gap between reserve requirement ratios on long-term and short-term deposits.

In Thailand, latest economic indicators point towards a slowdown in domestic demand. In particular, consumption and investment in the first two months of the fourth quarter of 2006 showed a continued moderation from the previous quarter. Real GDP growth was 4.7 per cent in the quarter ended September 2006 as compared with 5.3 per cent a year ago. Inflationary pressures are also expected to moderate, particularly from lower oil prices, significantly reducing the chances that core inflation will exceed the target band over the next two years. On balance, inflationary pressures have moderated, while the risks to growth have increased. Therefore, Thailand lowered the 1-day repurchase rate from 4.94 per cent to 4.75 per cent, effective January 17, 2007. From this day, the 1-day repurchase rate replaced the 14-day repurchase rate as the policy rate. Thailand had earlier raised the policy rate by 275 basis points between June 2005 and June 2006.

In order to discourage speculative short-term capital flows and to help maintain stability in the Thai baht with the objective of sustaining long-run growth in the Thai economy, the Bank of Thailand (BoT) on December 18, 2006 decided to impose unremunerated reserve requirement (URR) of 30 per cent on short-term capital flows. However, on December 19, 2006, the BoT exempted investments in stock markets from the URR. Foreign exchange transactions related to current account activities, including transactions related to exchange of goods, services, income, transfers and aid are also exempted from the URR. Foreign direct investment (defined as investments by non-residents in resident entities where the investor owns at least 10 per cent of the equity capital and has managerial power) is also exempt from the URR. Foreign currencies bought or exchanged against baht for the following transactions are subject to the URR: (i) investments in debt securities transacted from December 19, 2006 onwards; and, (ii) foreign currency borrowings transacted from December 19, 2006 onwards.

In Indonesia, economic activity, after showing some weakening in early 2006 as a result of falling public purchasing power in the wake of the October 2005 fuel price hike, has gradually regained momentum. Growth in 2006 was driven primarily by rapidly expanding exports and also by consumption. From the second half of 2005 to April 2006, the tightening of monetary policy pursued by Bank Indonesia succeeded in curbing rising inflation expectations. Inflation, which had reached 18.4 per cent in November 2005, eased sharply to 6.6 per cent in December 2006 with the easing of oil prices and the base effect. In Indonesia, the policy rate has, therefore, been cut by 325 basis points since May

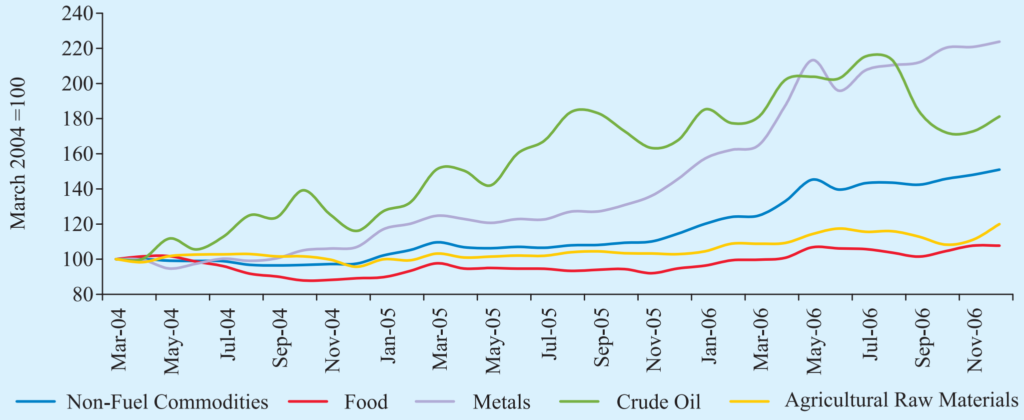
2006 to 9.50 per cent to support growth. The Bank Indonesia had earlier raised policy rates by 425 basis points during July-December 2005.

Amongst other emerging economies, South Africa raised the policy rates further by 50 basis points each in October and December 2006 to 9.0 per cent (a total increase of 200 basis points since June 2006) to contain inflationary pressures emanating from volatility in oil prices and from food and services prices. Turkey has kept rates unchanged since August 2006 on the back of slowdown in domestic demand and moderation in inflation expectations. Turkey had earlier increased its policy rate by 425 basis points during June-July 2006 on concerns over the possible pass-through effect of the exchange rate movements arising from the volatility in international financial markets. On the other hand, in view of weak economic activity, Brazil has reduced policy rates on twelve occasions (by 650 basis points) since September 2005 to 13.25 per cent on November 29, 2006. The Bank of Israel has cut its policy rate by 100 basis points since October 2006 - 25 basis points each in October and November 2006 and 50 basis points in December 2006 - to support growth, after having raised rates by 200 basis points between October 2005 and August 2006.

Global Commodity Prices

Non-fuel commodity prices rose during the third quarter of 2006-07 led by metals and food prices. Metals prices, barring copper, firmed up further on the back of robust demand in emerging economies, especially China (Chart 22). Amongst food items, prices of wheat and edible oils rose, reflecting a shortfall in global production. Crude oil prices, on the other hand, have eased in recent months.

Chart 22: International Commodity Prices



Source: International Monetary Fund.

Table 26: International Crude Oil Prices

(US dollars per barrel)

Year/Month	Dubai Crude	UK Brent	US WTI	Average Crude Price	Indian Basket Price
1	2	3	4	5	6
2001-02	21.8	23.2	24.1	23.0	22.4
2002-03	25.9	27.6	29.2	27.6	26.6
2003-04	26.9	29.0	31.4	29.1	27.8
2004-05	36.4	42.2	45.0	41.3	38.9
2005-06	53.4	58.0	59.9	57.1	55.4
March 2004	30.5	33.8	36.7	33.7	31.9
March 2005	45.6	53.1	54.2	50.9	48.8
March 2006	57.7	62.3	62.9	60.9	59.6
April 2006	64.1	70.4	69.4	68.0	66.8
May 2006	64.9	70.2	70.9	68.7	67.2
June 2006	65.1	68.9	70.9	68.3	66.7
July 2006	69.1	73.9	74.4	72.5	71.1
August 2006	68.8	73.6	73.0	71.8	70.9
September 2006	59.8	62.8	63.8	62.1	61.1
October 2006	56.5	58.4	58.9	57.9	57.3
November 2006	56.8	58.5	59.1	58.1	57.5
December 2006	58.7	62.3	62.0	61.0	60.2

Source : International Monetary Fund and World Bank.

International crude oil prices (WTI) eased sharply from the peak of US $ 78.4 a barrel in July 2006 to around US $ 60 a barrel in the second half of September 2006 and further to below US $ 60 a barrel in early October 2006 on the back of signs of slowdown of the US economy, increased US stocks and easing of tension over Iran's nuclear programme (Table 26). After remaining below US $ 60 a barrel in early November 2006, prices edged up to around US $ 62-63 a barrel in December 2006 on the back of the fall in US product inventories and production cuts by the Organisation of the Petroleum Exporting Countries (OPEC). The OPEC reduced crude oil production by 1.2 million barrels per day (mb/d) effective November 1, 2006 to support prices. In its meeting held on December 14, 2006, the OPEC decided to reduce output by a further 0.5 mb/d effective February 1, 2007 to balance supply and demand. Prices, however, eased further to reach US $ 51 a barrel in January 2007 on the back of mild winter in the US and rise in the US stocks. It is, however, uncertain as to whether the current level of oil prices will be sustained in view of limited spare global crude oil production capacity and tight supply-demand balance (Table 27). Prices increased sharply on January 23, 2007 to US $ 55 a barrel.

Metals prices, except copper, recorded further gains during the third quarter of 2006-07 on the back of robust demand and supply constraints amidst speculative investor interest. As a result, prices of aluminium, tin and zinc during December 2006 were higher by about 25 per cent, 66 per cent and 142 per cent, respectively, over their levels a year ago. Prices of copper fell by 12 per cent during the quarter

Table 27: World Supply-Demand Balance of Oil

(Million barrels per day)

Item	2003	2004	2005	2006 (P)	2007 (P)	2006			
						Q1	Q2	Q3 P	Q4 P
1	2	3	4	5	6	7	8	9	10
Demand									
1. OECD	48.7	49.5	49.6	49.2	49.6	50.1	47.9	48.8	49.9
2. Non-OECD	31.2	33.0	34.4	35.7	36.8	35.1	35.2	35.4	36.9
of which: China	5.6	6.5	6.9	7.4	7.9	7.2	7.3	7.4	7.6
3. Total (1+2)	79.9	82.5	84.0	84.8	86.3	85.2	83.1	84.2	86.8
Supply									
4. Non-OPEC	48.9	50.1	50.3	50.8	51.9	50.4	50.4	51.1	51.4
5. OPEC	30.7	32.9	34.2	33.9	33.9	34.0	33.7	34.2	33.6
6. Total (4+5)	79.6	83.1	84.5	84.7	85.8	84.4	84.1	85.3	85.0
Stock Changes	**0.3**	**-0.6**	**-0.5**	**0.1**	**0.5**	**0.8**	**-1.0**	**-1.1**	**1.8**

P : Projections.
Source: US Energy Information Administration.

ended December 2006 on reports of rising stocks; nonetheless, prices were still 46 per cent higher than a year ago. International steel prices, which edged higher during June-July 2006, softened in October-December 2006 (Table 28).

Table 28: International Commodity Prices

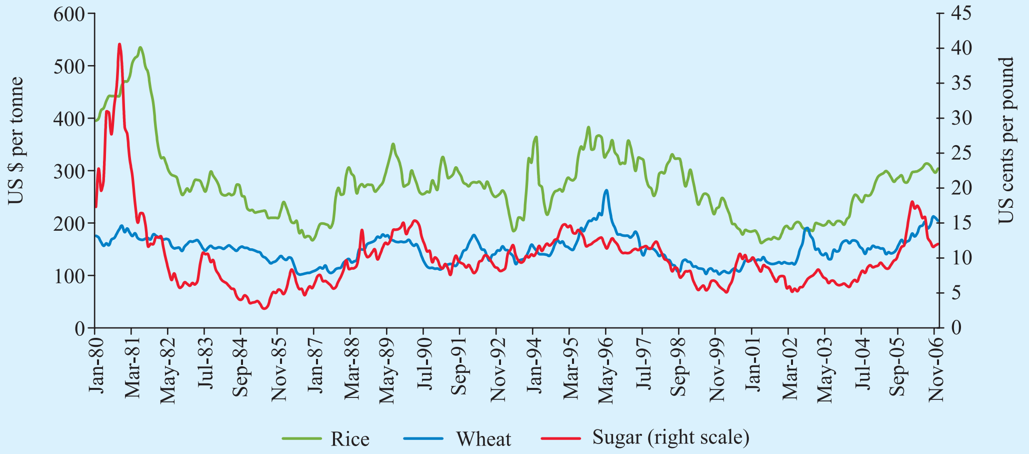
Commodity	Unit	2004	2005	2005	2006		2006					
				Oct-Dec.	July-Sep.	Oct-Dec.	May	Jun.	Sept.	Oct.	Nov.	Dec.
1	2	3	4	5	6	7	8	9	10	11	12	13
Energy												
Coal	$/mt	53.0	47.6	39.6	50.3	46.6	52.6	52.4	47.1	44.1	46.0	49.8
Crude oil (Average)	$/bbl	37.7	53.4	56.6	68.8	59.0	68.7	68.3	62.1	57.9	58.1	61.0
Non-Energy Commodities												
Palm oil	$/mt	471.3	422.1	438.3	492.7	542.8	440.0	437.0	497.0	507.0	547.0	574.3
Soybean oil	$/mt	616.0	544.9	558.7	620.3	662.2	588.0	601.0	602.0	615.0	675.0	696.7
Soybeans	$/mt	306.5	274.7	258.9	263.9	289.4	266.0	267.0	257.0	273.0	300.0	295.3
Rice	$/mt	237.7	286.3	281.6	312.4	300.3	308.0	312.5	309.2	301.0	296.3	303.7
Wheat	$/mt	156.9	152.4	164.5	196.1	208.7	193.2	195.2	196.0	212.1	209.7	204.3
Sugar	c/kg	15.8	21.8	26.3	30.6	26.0	37.1	34.0	26.6	25.7	26.0	26.5
Cotton A Index	c/kg	136.6	121.7	126.1	128.0	127.6	120.2	121.5	131.0	125.8	126.5	130.5
Aluminium	$/mt	1716.0	1898.0	2076.0	2482.0	2724.0	2861.0	2477.0	2473.0	2655.0	2703.0	2814.0
Copper	$/mt	2866.0	3679.0	4302.0	7670.0	7068.0	8046.0	7198.0	7602.0	7500.0	7029.0	6675.0
Gold	$/toz	409.2	444.8	485.6	621.5	614.5	675.4	596.1	598.2	585.8	627.8	629.8
Silver	c/toz	669.0	734.0	808.0	1169.0	1263.0	1337.8	1077.4	1160.0	1162.0	1298.0	1330.0
Steel products index	1990=100	121.5	137.9	138.6	135.8	132.1	125.2	131.2	135.8	133.7	131.5	131.0
Steel cold-rolled coil/sheet	$/mt	607.1	733.3	750.0	700.0	658.3	600.0	650.0	700.0	675.0	650.0	650.0
Steel hot-rolled coil/sheet	$/mt	502.5	633.3	650.0	600.0	558.3	550.0	575.0	600.0	575.0	550.0	550.0
Tin	c/kg	851.3	738.0	643.2	865.3	1033.5	883.7	789.6	903.9	976.8	1007.9	1115.9
Zinc	c/kg	104.8	138.1	164.0	336.3	420.4	356.6	322.6	340.3	382.3	438.2	440.5

$: US dollar c : US cent bbl : barrel mt : metric tonne kg : Kilogram toz : troy oz.
Source: World Bank.

Food prices firmed up led by wheat and oilseeds/edible oils. According to the latest assessment by the Food and Agriculture Organisation (FAO), global wheat production is expected to decline by 5.2 per cent in 2006-07 on the back of hot and dry weather/drought affecting crops in Australia, Argentina and Brazil. As a result, wheat stocks are expected to fall by 15.8 per cent by the end of 2006-07 season. Rice production is also expected to decline, though only marginally by 0.2 per cent resulting in a drawdown of stocks by 0.6 per cent. In view of these developments, wheat prices have firmed up since the second half of 2005. Notwithstanding some easing in November-December 2006, wheat prices in December 2006 were still higher by about 24 per cent on a year-on-year basis (Chart 23). Rice prices exhibited some softness from August 2006 but again firmed up in December 2006. Prices in December 2006 were higher by about 8 per cent on a year-on-year basis. The recent rise in international prices of wheat and rice comes after a period of some softness in the late 1990s. International prices of rice had eased from 1997 onwards to stabilise at around US $ 200 per tonne during 2000-2003. Since then, prices have edged higher to cross US $ 300, but still remain lower than the levels touched in the mid-1990s. Similarly, prices of wheat, after remaining largely range-bound between 1998 and 2004, have edged higher from mid-2005.

Prices of oilseeds and edible oils have edged up sharply in recent months, *inter alia*, due to lower production coupled with strong consumption demand, including demand for non-food uses such as fuels and as feedstock for biodiesel production. On a year-on-year basis, soybean, soybean oil and palm oil prices in December 2006 were higher by 12 per cent, 30 per cent and 34 per cent, respectively. On the other hand, international sugar prices have eased sharply since August 2006 on forecasts of higher global production during 2006-07. According to the International Sugar Organisation, global sugar production is

Chart 23: International Prices of Rice, Wheat and Sugar



estimated to increase by 5.8 million tonnes to 158 million tonnes during 2006-07 (October-September) season, exceeding global consumption by 5.8 million tonnes. A record crop in Brazil, the world's largest producer, significant growth in output in the Far East along with likely higher production in India is expected to more than offset the contraction in EU output. Sugar prices have declined by almost 33 per cent from the recent peak touched in February 2006. Global cotton prices remained broadly unchanged during the quarter ended December 2006.

Inflation Conditions in India

Taking into account the real, monetary and global factors having a bearing on domestic prices, the Reserve Bank in its Annual Policy Statement for 2006-07 (April 2006) noted that containing inflationary expectations would continue to pose a challenge to monetary management and the policy endeavour would be to contain the year-on-year inflation rate for 2006-07 in the range of 5.0-5.5 per cent. Against the backdrop of widespread and simultaneous monetary policy tightening by several countries in early June 2006 following marked and heightened volatility in the international financial markets, and in the light of the prevailing domestic monetary and credit environment, the LAF reverse repo and repo rates were increased effective June 9, 2006 by 25 basis points each to 5.75 per cent and 6.75 per cent, respectively. In its First Quarter Review of the Annual Statement on Monetary Policy (July 2006), the Reserve Bank observed that containing inflation in the range of 5.0-5.5 per cent warrants appropriate priority in policy responses. Accordingly, the Reserve Bank raised the reverse repo rate and the repo rate by 25 basis points each to 6.00 per cent and 7.00 per cent, respectively, on July 25, 2006 while continuing to keep the Bank Rate and cash reserve ratio unchanged.

In the Mid-Term Review of the Annual Policy Statement for 2006-07 (October 2006), the Reserve Bank observed that recent developments, in particular, the combination of high growth and consumer inflation coupled with escalating asset prices and tightening infrastructural bottlenecks underscore the need to reckon with dangers of overheating and the implications for the timing and direction of monetary policy setting. The Mid-term Review further noted that while there is no conclusive evidence of potential overheating in the Indian economy at the current juncture, the criticality of monitoring all available indications that point to excess aggregate demand is perhaps more relevant now than ever before. In the Mid-term Review, the repo rate was increased by 25 basis points to 7.25 per cent while keeping the reverse repo rate unchanged at 6.00 per cent. On a review of the macroeconomic and monetary conditions, the Reserve Bank on December 8, 2006 announced a hike of 50 basis points in the cash reserve ratio (CRR) in two tranches to 5.5 per cent (Table 29 and Box 1).

Table 29: Movement in Key Policy Rates and Inflation

(Per cent)

Effective since	Reverse Repo Rate	Repo Rate	Cash Reserve Ratio	WPI Inflation @
1	2	3	4	5
March 31, 2004	4.50	6.00	4.50	4.6
September 18, 2004	4.50	6.00	4.75	7.9
October 2, 2004	4.50	6.00	5.00	7.1
October 27, 2004	4.75	6.00	5.00	7.4
April 29, 2005	5.00	6.00	5.00	6.0
October 26, 2005	5.25	6.25	5.00	4.5
January 24, 2006	5.50	6.50	5.00	4.2
June 9, 2006	5.75	6.75	5.00	4.9
July 25, 2006	6.00	7.00	5.00	4.7
October 31, 2006	6.00	7.25	5.00	5.3
December 23, 2006	6.00	7.25	5.25	5.5
January 6, 2007	6.00	7.25	5.50	6.1

@: As on the date of change in policy rates.

Note : With effect from October 29, 2004, nomenclature of repo and reverse repo was changed in keeping with international usage. Now, reverse repo indicates absorption of liquidity and repo signifies injection of liquidity. Prior to October 29, 2004, repo indicated absorption of liquidity while reverse repo meant injection of liquidity. The nomenclature in this Report is based on the new use of terms even for the period prior to October 29, 2004.

The conduct of monetary policy in India has been guided by the objectives of maintaining price stability and ensuring adequate flow of credit to the productive sectors of the economy for sustaining overall economic growth. The relative emphasis between price stability and growth, however, has changed depending on the underlying macroeconomic conditions. Monetary policy in India, thus, strives for a judicious balance between price stability and growth. The policy reverse repo rate was cut by 150 basis points between March 2002 and August 2003 to support growth after inflation had been brought down to an average of around five per cent from the long-term average of 8-9 per cent during the 1970s and 1980s. With the recovery of economic activity, and on signs of emerging inflationary pressures, the process of withdrawal of monetary accommodation was initiated in a phased and pre-emptive manner beginning September 2004 with the increase in the cash reserve ratio by 50 basis points in two stages and the hike in reverse repo rate in October 2004. The reverse repo rate has been increased by 150 basis points since then, while the repo rate has been increased by 125 basis points. The LAF corridor - the gap between the repo rate and the reverse repo rate - has been varied in response to the evolving macroeconomic situation. The gap, which was 200 basis points in March 2003, was reduced to 100 basis points in April 2005 before increasing to 125 basis points in October 2006. The cash reserve ratio has been raised by 100 basis points since September 2004. Thus, monetary policy accommodation has been withdrawn since September 2004 in a phased manner to contain inflation and stabilise inflation expectations. Monetary policy affects its final goals with long and variable lags but on a cumulative basis, thus warranting a forward looking approach. Further, effective monetary policy has as much to do with inflation expectations as the actual

Box 1: Cash Reserve Ratio (CRR)

The Reserve Bank in its Mid-Term Review of Annual Policy Statement for the year 2006-07 (October 31, 2006) noted, *inter alia*, that: "Furthermore, containing inflation expectations in the current environment and consolidating gains achieved so far in regard to stability would warrant appropriate, immediate measures and willingness to take recourse to all possible measures in response to evolving circumstances promptly. The objective is to continue to maintain conditions of stability that contribute to sustaining the momentum of growth on an enduring basis. Towards this objective, the monetary policy stance and measures will need to be in a process of careful rebalancing and timely adjustment".

Subsequent to the announcement of the Mid-term Review, there were a number of significant developments, particularly on the domestic front. These included:

1. Real GDP growth at 9.2 per cent during July-September 2006 and 9.1 per cent in the first half of 2006-07.
2. Continued high growth in non-food bank, acceleration in money supply (M3) growth and reserve money growth and absorption of additional liquidity under the market stabilisation scheme (MSS) (see Chapter III).
3. Increase in WPI inflation, with inflation based on the various consumer price indices being higher than WPI.
4. As per the RBI's Industrial Outlook survey, a majority of respondents from the private corporate sector expect higher increase in prices of both inputs and outputs. There were reports of growing strains on domestic capacity utilisation. There were also reports that expansion of capacity is underway but the realisation could be constrained over the next two years.

A seasonal decline in prices of food articles could moderate the inflation pressures but the WPI inflation excluding food articles remains at elevated levels. The reduction in prices of petrol and diesel in end-November 2006 will moderate inflation, but the overall impact on inflation expectations requires to be monitored and moderated.

The external sector continues to be strong and current account deficit is likely to be close to the trend, and will continue to be accommodated by net capital flows. However, it is necessary to recognize the challenges emanating from capital flows and consequent impact on increasing liquidity.

In view of the above, the Reserve Bank, on December 8, 2006, decided to increase the cash reserve ratio (CRR) of the scheduled commercial banks, regional rural banks (RRBs), scheduled state co-operative banks and scheduled primary (urban) co-operative banking system by 50 basis points of their net demand and time liabilities (NDTL) in two stages – 25 basis points each effective from fortnights beginning December 23, 2006 and January 6, 2007. As a result of the increases in CRR on liabilities to banking system, an amount of about Rs.13,500 crore of resources of banks would be absorbed.

outcome of inflation. It may be seen that monetary policy was tightened even when inflation was at relatively low level (Table 29). Pre-emptive monetary policy actions by the Reserve Bank since September 2004, supported by supply-side and fiscal measures, have helped in containing inflation and anchoring inflation expectations while evidently supporting the growth momentum. In response to evolving circumstances, the stance of monetary policy has changed from time to time (Box 2).

Box 2: Stance of Monetary Policy in India since April 2003

Statement on Monetary and Credit Policy for the year 2003-04 (April 2003) and Mid-term Review (November 2003)

- Provision of adequate liquidity to meet credit growth and support investment demand in the economy while continuing a vigil on movements in the price level.
- In line with the above, to continue with the present stance of preference for a soft and flexible interest rate environment within the framework of macroeconomic stability.

2004-05

Annual Policy Statement for the Year 2004-05 (May 2004)

- Provision of adequate liquidity to meet credit growth and support investment and export demand in the economy while keeping a very close watch on the movements in the price level.
- Consistent with the above, while continuing with the *status quo*, to pursue an interest rate environment that is conducive to maintaining the momentum of growth and, macroeconomic and price stability.

Mid-term Review of Annual Policy for the Year 2004-05 (October 2004)

- Provision of appropriate liquidity to meet credit growth and support investment and export demand in the economy while placing equal emphasis on price stability.
- Consistent with the above, to pursue an interest rate environment that is conducive to macroeconomic and price stability, and maintaining the momentum of growth.
- To consider measures in a calibrated manner, in response to evolving circumstances with a view to stabilising inflationary expectations.

2005-06

Annual Policy Statement for the Year 2005-06 (April 2005)

- Provision of appropriate liquidity to meet credit growth and support investment and export demand in the economy while placing equal emphasis on price stability.
- Consistent with the above, to pursue an interest rate environment that is conducive to macroeconomic and price stability, and maintaining the momentum of growth.
- To consider measures in a calibrated manner, in response to evolving circumstances with a view to stabilising inflationary expectations.

First Quarter Review of Annual Statement on Monetary Policy for the Year 2005-06 (July 2005)

- The overall stance of monetary policy for the remaining part of the year 2005-06 will continue to be as set out in the annual policy Statement of April 2005, but the Reserve Bank would respond, promptly and effectively, to the evolving situation depending on the unfolding of the risks.

Mid-term Review of Annual Policy Statement for the year 2005-06 (October 2005)

- Consistent with emphasis on price stability, provision of appropriate liquidity to meet genuine credit needs and support export and investment demand in the economy.

(Contd....)

(Concld.)

- Ensuring an interest rate environment that is conducive to macroeconomic and price stability, and maintaining the growth momentum.
- To consider measures in a calibrated and prompt manner, in response to evolving circumstances with a view to stabilising inflationary expectations.

Third Quarter Review of Annual Statement on Monetary Policy for the Year 2005-06 (January 2006)

- To maintain the emphasis on price stability with a view to anchoring inflationary expectations.
- To continue to support export and investment demand in the economy for maintaining the growth momentum by ensuring a conducive interest rate environment for macroeconomic, price and financial stability.
- To provide appropriate liquidity to meet genuine credit needs of the economy with due emphasis on quality.
- To consider responses as appropriate to evolving circumstances.

Annual Policy Statement for the Year 2006-07 (April 2006)

- To ensure a monetary and interest rate environment that enables continuation of the growth momentum consistent with price stability while being in readiness to act in a timely and prompt manner on any signs of evolving circumstances impinging on inflation expectations.
- To focus on credit quality and financial market conditions to support export and investment demand in the economy for maintaining macroeconomic, in particular, financial stability.
- To respond swiftly to evolving global developments.

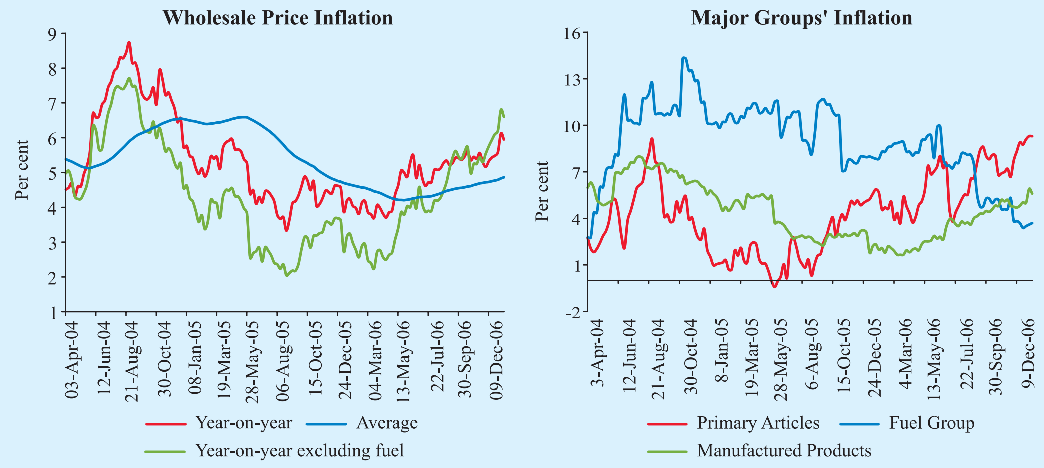
First Quarter Review of Annual Statement on Monetary Policy for the Year 2006-07 (July 2006)

- To ensure a monetary and interest rate environment that enables continuation of the growth momentum while emphasising price stability with a view to anchoring inflation expectations.
- To reinforce the focus on credit quality and financial market conditions to support export and investment demand in the economy for maintaining macroeconomic and, in particular, financial stability.
- To consider measures as appropriate to the evolving global and domestic circumstances impinging on inflation expectations and the growth momentum.

Mid-term Review of Annual Policy Statement for the Year 2006-07 (October 2006)

- To ensure a monetary and interest rate environment that supports export and investment demand in the economy so as to enable continuation of the growth momentum while reinforcing price stability with a view to anchoring inflation expectations.
- To maintain the emphasis on macroeconomic and, in particular, financial stability.
- To consider promptly all possible measures as appropriate to the evolving global and domestic situation.

Chart 24: Annual WPI Inflation



Inflation movements in 2006-07 have been driven by primary food articles and manufactured products prices. The impact of mineral oils, the major driver of inflation over the past two years, petered out by early September 2006 on the back of the base effect. Headline inflation, based on movement in the wholesale price index (WPI), increased to 6.0 per cent as on January 13, 2007 from 4.1 per cent at end-March 2006 and 4.2 per cent a year ago. WPI inflation has moved in a range of 3.7-6.1 per cent during 2006-07 so far (Chart 24 and Table 30). The average WPI inflation rate (average of the 52 weeks) for the week ended January 13, 2007 was 4.9 per cent, higher than that of 4.7 per cent a year ago. The y-o-y inflation, excluding the fuel group, at 6.6 per cent was above the headline inflation rate of 6.0 per cent as on January 13, 2007.

Among the major groups, prices of primary articles led by wheat, pulses, fruits, milk and oilseeds posed upward pressures on inflation (Chart 25). Wheat prices have remained firm on the back of low stocks and high international prices. Domestic wheat stocks were 6.0 million tonnes as on November 1, 2006 as against the buffer stock norm of 11 million tonnes. On a year-on-year basis, wheat prices have increased by 14.7 per cent as on January 13, 2007 (global wheat prices, as noted earlier, increased by about 24 per cent, y-o-y, in December 2006). Prices of pulses also edged higher (25.4 per cent) from last year's level, reflecting stagnant domestic production as well as higher demand (Chart 26). Fruits and milk prices have increased by 12.0 per cent and 7.6 per cent, respectively. Prices of oilseeds witnessed a sharp turnaround - an increase of 21.0 per cent, y-o-y, as against a decline of 11.9 per cent a year ago - which could be attributed to lower domestic production as well as firm global prices. On the other hand, prices of vegetables increased moderately by 0.8 per cent, y-o-y, as compared with 28.9 per cent a

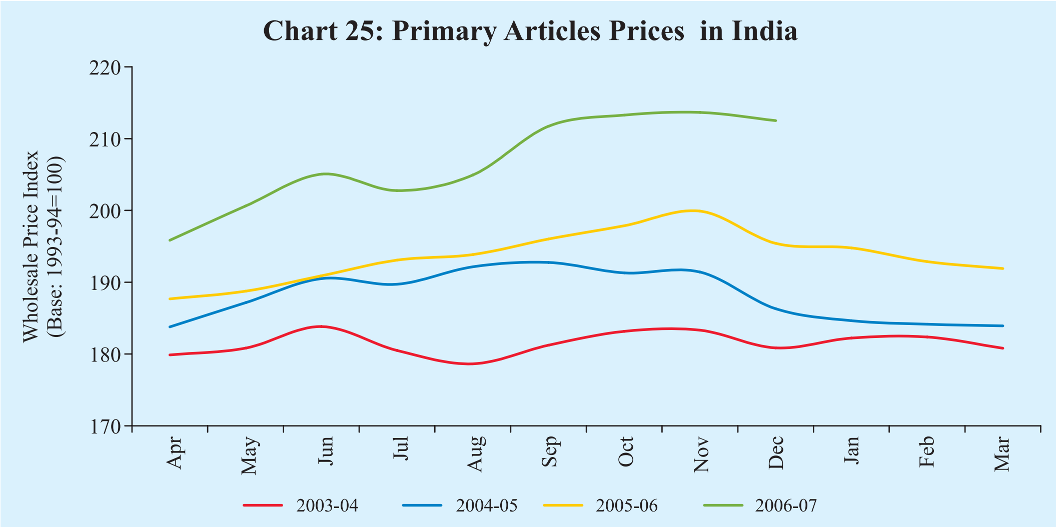
Table 30: Wholesale Price Inflation in India (year-on-year)

(Per cent)

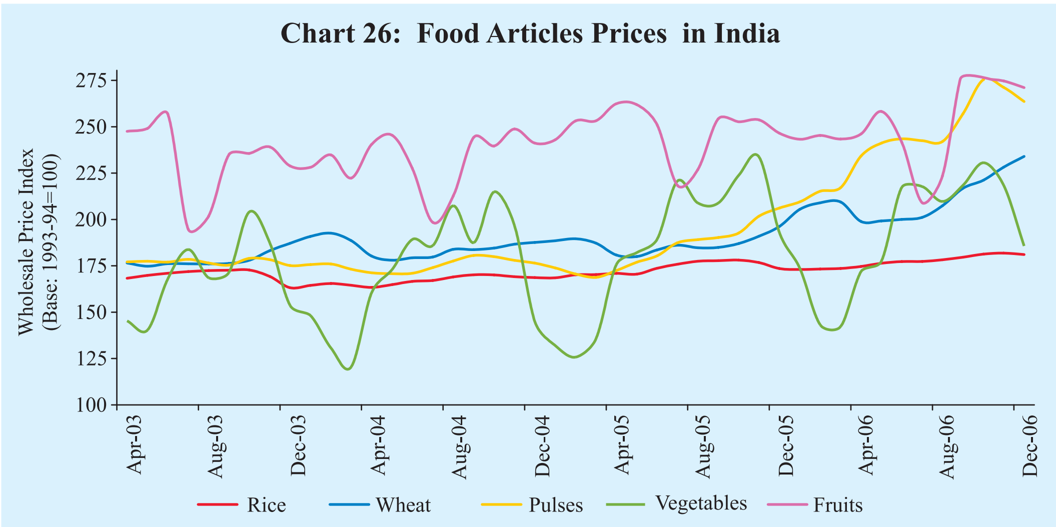
Commodity	Weight	2005-06 (March 25) Inflation	WC	2005-06 (Jan.14) Inflation	WC	2006-07 P (Jan. 13) Inflation	WC
1	2	3	4	5	6	7	8
All Commodities	**100.0**	**4.1**	**100.0**	**4.2**	**100.0**	**6.0**	**100.0**
1. Primary Articles	**22.0**	**5.4**	**28.3**	**5.6**	**28.7**	**9.3**	**34.1**
Food Articles	15.4	6.6	24.2	7.4	26.5	8.5	22.0
i. Rice	2.4	2.7	1.4	2.3	1.2	5.0	1.8
ii. Wheat	1.4	12.9	4.3	8.3	2.8	14.7	3.6
iii. Pulses	0.6	33.2	4.4	18.2	2.4	25.4	2.7
iv. Vegetables	1.5	8.1	2.1	28.9	7.3	0.8	0.2
v. Fruits	1.5	-1.0	-0.5	1.9	0.8	12.0	3.7
vi. Milk	4.4	1.9	1.9	-1.5	-1.5	7.6	5.2
vii. Eggs, Fish and Meat	2.2	14.3	7.9	22.4	11.8	-1.0	-0.4
Non-Food Articles	6.1	-1.9	-2.7	-2.4	-3.3	9.6	8.9
i. Raw Cotton	1.4	-1.4	-0.4	7.6	1.9	-1.4	-0.3
ii. Oilseeds	2.7	-7.8	-4.5	-11.9	-7.1	21.0	7.5
iii. Sugarcane	1.3	0.7	0.3	0.7	0.3	0.0	0.0
Minerals	0.5	43.6	6.8	34.8	5.7	20.6	3.0
2. Fuel, Power, Light and Lubricants	**14.2**	**8.9**	**47.9**	**7.9**	**41.1**	**3.7**	**14.0**
i. Mineral Oils	7.0	13.2	39.8	12.5	36.2	3.5	7.8
ii. Electricity	5.5	4.5	8.2	2.7	4.9	4.9	6.0
iii. Coal Mining	1.8	0.0	0.0	0.3	0.2	0.0	0.0
3. Manufactured Products	**63.8**	**1.7**	**23.2**	**2.2**	**29.9**	**5.6**	**52.3**
i. Food Products	11.5	0.9	2.2	0.8	2.0	2.7	4.8
of which: Sugar	3.6	6.6	4.9	0.4	0.3	-5.6	-2.9
Edible Oils	2.8	-2.4	-1.3	-5.9	-3.1	11.2	3.8
ii. Cotton Textiles	4.2	1.1	1.0	-1.8	-1.5	3.0	1.7
iii. Man Made Fibres	4.4	-4.6	-2.5	-4.0	-2.1	3.1	1.1
iv. Chemicals and Products	11.9	3.6	10.2	3.1	8.5	2.8	5.4
of which : Fertilisers	3.7	0.3	0.2	2.4	1.9	1.8	1.0
v. Basic Metals, Alloys and Metal Products	8.3	-2.9	-6.7	1.6	3.5	13.4	20.2
of which: Iron and Steel	3.6	-7.5	-8.7	-2.6	-2.9	11.4	8.2
vi. Non-Metallic Mineral Products	2.5	8.6	4.7	8.4	4.2	12.5	4.6
of which: Cement	1.7	13.0	4.8	12.9	4.2	17.9	4.5
vii. Machinery and Machine Tools	8.4	3.9	6.1	2.8	4.3	7.6	8.1
of which: Electrical Machinery	5.0	4.7	3.6				
viii. Transport Equipment and Parts	4.3	1.2	1.1	2.8	2.4	1.6	0.9
Memo:							
Food Items (Composite)	**26.9**	**4.2**	**26.5**	**4.6**	**28.6**	**6.2**	**26.8**
WPI Excluding Food	**73.1**	**4.0**	**73.5**	**4.0**	**71.4**	**5.9**	**73.2**
WPI Excluding Fuel	**85.8**	**2.7**	**52.1**	**3.2**	**58.9**	**6.6**	**86.0**

WC : Weighted Contribution.

year ago. Overall, prices of primary articles have increased by 10.3 per cent since end-March 2006 (6.4 per cent a year ago) and, on a y-o-y basis, by 9.3 per cent (5.6 per cent a year ago). Accordingly, on a y-o-y basis, the contribution of primary articles to headline inflation increased to about 34 per cent as on January 13, 2007 from 29 per cent a year ago.



In order to contain the price rise in primary commodities so as to stabilise inflation expectations, the Government undertook a number of fiscal measures such as (i) allowing the State Trading Corporation (STC) to tender overseas for 55 lakh tonnes of wheat to supplement domestic availability; (ii) permitting private traders to import wheat initially at 5 per cent duty from June 27, 2006 and then at zero duty from September 9, 2006; (iii) allowing import of pulses at zero duty from June 8, 2006 and a ban on their exports from June 27, 2006; (iv) exempting sugar from customs duty from June 22, 2006 and a ban on their exports; and (v) reduction in customs duty on palm oils by 10 percentage points to 70-80 per cent in August 2006. The Government also announced a hike of

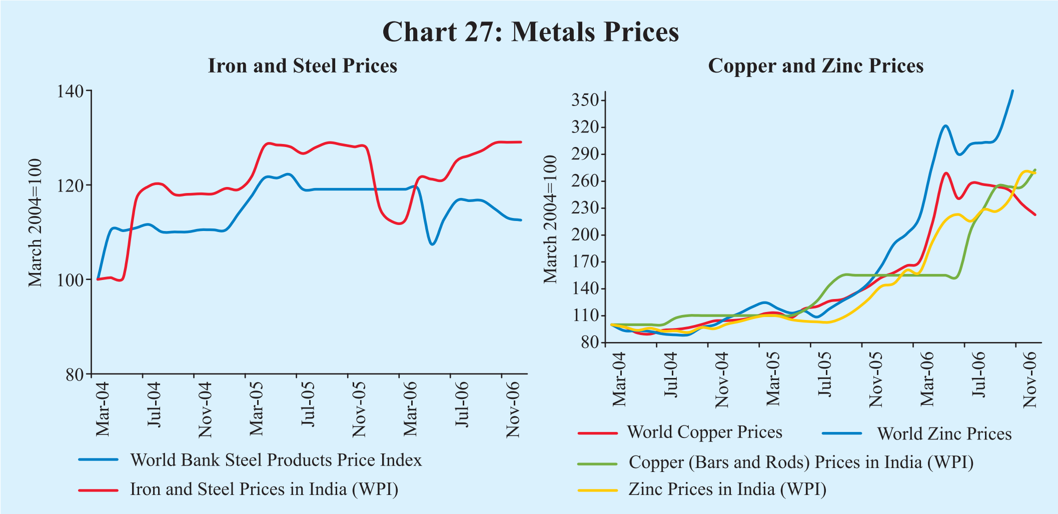


Rs.100 per quintal in the minimum support price (MSP) for wheat to increase domestic procurement to meet the requirements of the public distribution system in the ensuing season.

Fuel prices dominated the inflation outcome till end-August 2006, notwithstanding the incomplete pass-through of higher international crude oil prices. Apart from raising domestic petrol and diesel prices by Rs.4 and Rs.2 per litre, respectively, in June 2006, the Government also announced the following measures: (i) reduction in customs duty on petrol and diesel to 7.5 per cent from the existing 10.0 per cent; and (ii) issuance of oil bonds worth Rs.28,000 crore (over and above Rs.11,500 crore issued during 2005-06) to oil marketing companies to compensate for their under-recoveries in domestic operations. The Government has so far issued oil bonds worth Rs.14,150 crore in the current fiscal year in three tranches. Following the reduction in international crude oil prices, domestic prices of petrol and diesel were reduced by Rs.2 per litre (around 4 per cent) and Re. 1 per litre (around 3 per cent), respectively, on November 29, 2006. Reflecting the base effect as well as cuts in prices of petrol, diesel and other freely-priced products such as naphtha and furnace oil, fuel group inflation moderated to 3.7 per cent on January 13, 2007 from a peak of 9.9 per cent on June 17, 2006 and 7.9 per cent a year ago. While evaluating movements in fuel group inflation, it may be noted that the pass-through of higher international oil prices has been restricted to petrol and diesel. Domestic prices of liquefied petroleum gas (LPG) and kerosene have remained unchanged since November 2004 and April 2002, respectively, on grounds of societal concerns.

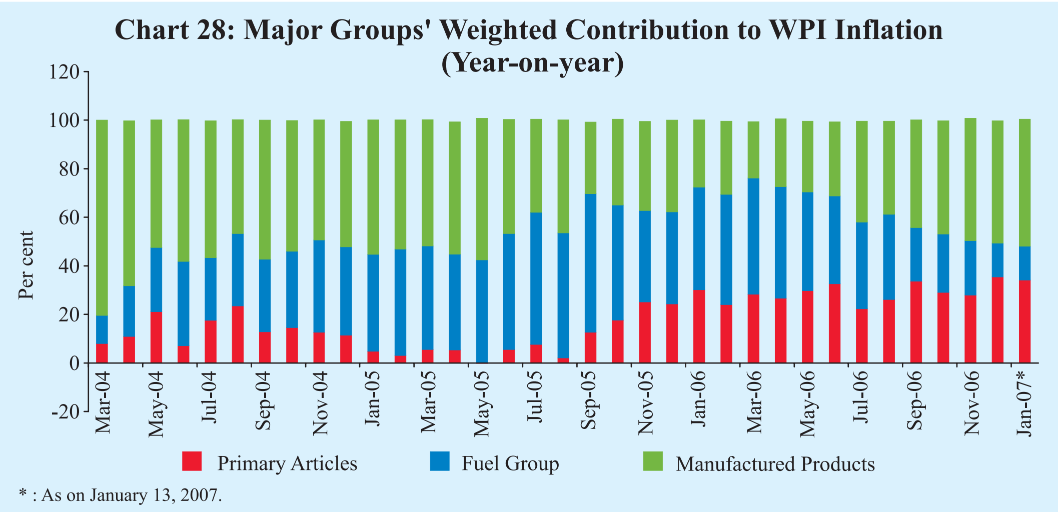
Manufactured products inflation increased to 5.6 per cent as on January 13, 2007 from 1.7 per cent at end-March 2006 and 2.2 per cent a year ago. Manufactured products inflation during 2006-07 has been led by edible oils, metals, cement and electrical machinery. Non-ferrous metal prices have broadly moved in line with international trends (Chart 27). Illustratively, domestic prices of copper and zinc have increased, y-o-y, by about 84 per cent and 76 per cent, respectively, as on January 13, 2007. Iron and steel prices have increased by 11.4 per cent, y-o-y, in contrast to a decline of 2.6 per cent a year ago.

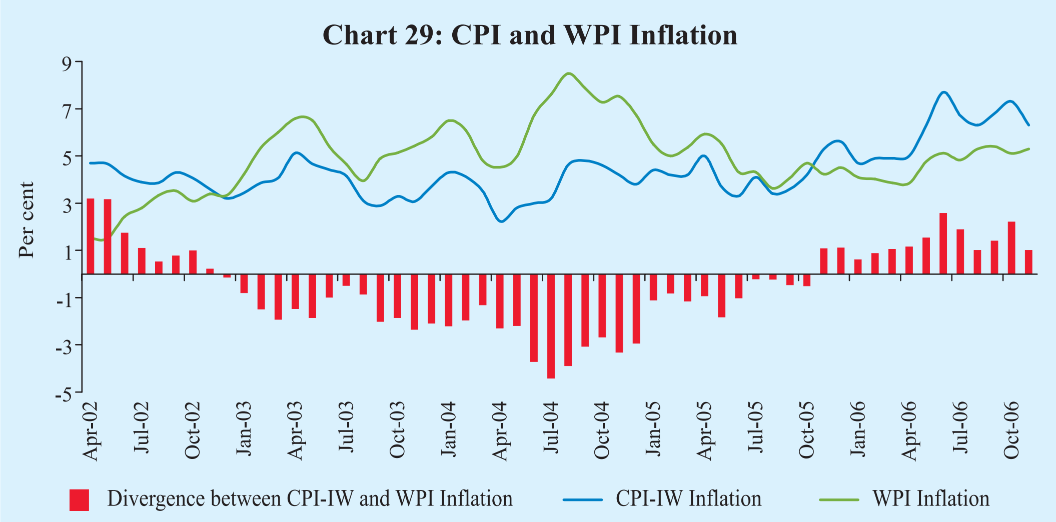
Domestic prices of cement increased by 17.9 per cent, y-o-y, as on January 13, 2007 on top of an increase of 12.9 per cent a year ago, reflecting strong domestic demand emanating from construction activity. Other manufactured items contributing to higher y-o-y inflation were electrical machinery (increase of 11.3 per cent as compared with an increase of 1.9 per cent a year ago), edible oils (increase of 11.2 per cent in contrast to a decline of 5.9 per cent a year ago) and grain mill products (increase of 17.7 per cent as compared with an increase of 13.0 per cent a year ago). Domestic sugar prices have eased in recent months in line with global trends.



Competitive pressures, productivity gains as well as strong corporate profitability have provided firms the flexibility to absorb a part of higher input prices into their profit margins. Furthermore, pre-emptive monetary actions by anchoring inflation expectations have contained the second order effects of past increases in oil prices. In order to reduce cost of manufacturing and infrastructure development, the Government took fiscal measures on January 22, 2007 in the form of reduction in customs duties on select items such as inorganic chemicals, non-ferrous metals, cement, capital goods and project imports.

In brief, primary articles' contribution to the overall y-o-y inflation on January 13, 2007 increased to 34 per cent (from 29 per cent a year ago) mainly due to higher prices of wheat, pulses, fruits, milk and oilseeds (Chart 28).





Manufactured products group's contribution was higher at 52 per cent (30 per cent a year ago) largely on account of increase in prices of edible oils/oil cakes, metals, cement and electrical machinery. The contribution of fuel prices to the y-o-y headline inflation, on the other hand, declined to 14 per cent from 41 per cent a year ago.

Consumer Price Inflation

Various measures of consumer price inflation were placed higher in the range of 6.3-8.9 per cent during November/December 2006. Consumer price inflation has remained higher than the WPI inflation since November 2005, reflecting the higher order of increase in food prices as well as the higher weight of food items in the CPI (Chart 29 and Table 31).

Table 31: Consumer Price Inflation (CPI) in India (year-on-year)

(Per cent)

Inflation Measure	March 2003	March 2004	March 2005	March 2006	June 2006	August 2006	Sept. 2006	Oct. 2006	Nov. 2006	Dec. 2006
1	2	3	4	5	6	7	8	9	10	11
CPI-IW	4.1	3.5	4.2	4.9	7.7	6.3	6.8	7.3	6.3	–
CPI- UNME	3.8	3.4	4.0	5.0	6.5	6.1	6.6	7.2	6.7	6.9
CPI-AL	4.9	2.5	2.4	5.3	7.2	6.5	7.3	8.4	8.3	8.9
CPI-RL	4.8	2.5	2.4	5.3	7.2	6.2	7.0	8.1	8.0	8.3
Memo:										
WPI Inflation	6.5	4.6	5.1	4.1	4.8	5.3	5.4	5.4	5.3	5.6

IW : Industrial Workers
AL : Agricultural Labourers
UNME : Urban Non-Manual Employees
RL : Rural Labourers

Table 32: CPI for Industrial Workers- Major Groups (Base: 2001=100)

(Per cent)

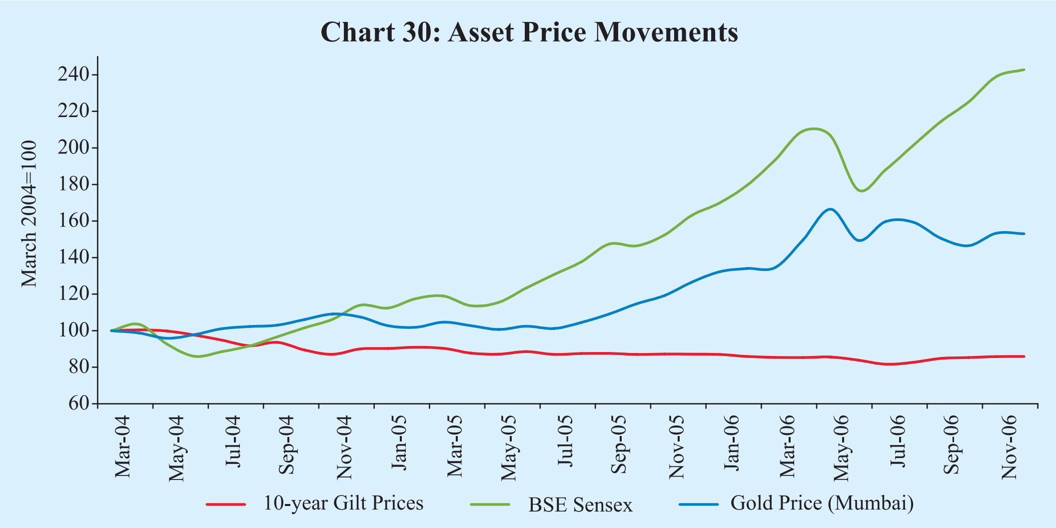
		Year-on-Year Variation				
		2005	2006			
	Weight	November	March	June	September	November
1	2	3	4	5	6	7
General Index	**100.0**	**5.3**	**4.9**	**7.7**	**6.8**	**6.3**
I. Food Group	**46.2**	**6.6**	**4.9**	**10.0**	**8.9**	**7.8**
i) Cereals and Products	13.5	3.3	8.3	13.1	13.1	14.5
ii) Pulses and Products	2.9	9.7	20.3	18.5	24.1	21.4
iii) Oils and Fats	3.2	-5.7	-2.9	3.2	4.9	8.8
iv) Meat, Fish and Eggs	4.0	5.5	3.5	10.4	8.9	11.4
v) Milk and Products	7.3	1.9	2.4	4.0	4.3	6.1
vi) Condiments and Spices	2.6	19.1	0.7	4.6	-1.1	-3.1
vii) Vegetables and Fruits	6.1	18.9	3.0	10.1	11.5	-1.8
viii) Other Foods	6.7	6.1	4.3	3.5	3.6	3.6
II. Pan, Supari, Tobacco and Intoxicants	**2.3**	**1.6**	**3.1**	**3.7**	**4.2**	**3.9**
III. Fuel and Light	**6.4**	**-5.5**	**-2.9**	**8.7**	**6.5**	**6.6**
IV. Housing	**15.3**	**11.7**	**6.6**	**6.6**	**7.1**	**7.1**
V. Clothing, Bedding and Footwear	**6.6**	**2.6**	**3.0**	**2.8**	**2.5**	**4.0**
VI. Miscellaneous Group (Services)	**23.3**	**4.0**	**4.6**	**4.7**	**5.4**	**4.6**
i) Medical Care	4.6	2.3	5.3	6.8	6.5	7.2
ii) Education, Recreation and Amusement	6.2	7.1	3.3	2.5	2.6	1.8
iii) Transport and Communication	4.9	6.4	7.3	7.9	8.5	7.7
iv) Personal Care and Effects	4.2	1.9	3.1	3.6	3.5	4.0
v) Other Miscellaneous Items	3.4	3.1	3.1	4.5	5.3	4.2

Note : The variations are worked out by linking the new series (Base: 2001=100) with the old series (Base: 1982=100) with the relevant conversion factors.

Disaggregated data for CPI-Industrial Workers (CPI-IW), available up to November 2006, indicate that food group inflation increased from 6.6 per cent in November 2005 (y-o-y) to 7.8 per cent in November 2006 (y-o-y). This, in turn, was due to sharp increases of 14.5 per cent and 21.4 per cent, respectively, in prices of cereals and pulses. Higher prices of meat, fish and eggs, and oils and fats also contributed to food group inflation. Prices of fuel and light increased by 6.6 per cent y-o-y in November 2006 as against a decline of 5.5 per cent a year ago. On the other hand, housing inflation, reflecting rents on housing, decelerated from 11.7 per cent in November 2005 to 7.1 per cent in November 2006 (Table 32).

Asset Prices

Asset prices remained buoyant during the quarter October-December 2006. Domestic equity markets recorded further gains during the third quarter of 2006-07 on the back of renewed buying interest by the FIIs, strong growth prospects and better corporate results. Stock markets reached record highs with the BSE Sensex touching 14218 on January 18, 2007. The BSE Sensex



was 14041 as on January 23, 2007, 24.5 per cent higher over end-March 2006 levels (Chart 30). Domestic gold prices have increased by about seven per cent since end-March 2006 mirroring movements in international prices. International gold prices, after rising to US $ 715 per ounce on May 12, 2006, witnessed a sharp correction and fell to US $ 559 as on June 14, 2006 in consonance with the trends in various commodities in the international market on concerns over rising global inflation. Prices initially recovered to US $ 664 per ounce as on July 19, 2006 but again fell to below US $ 600 in the second week of September 2006 as headline inflation in major economies eased in tandem with softening of international crude oil prices. Since then prices have been range-bound. Gilt prices have declined and yields have increased in 2006-07 so far. Gilt prices initially fell during the first quarter of 2006-07 in tandem with major economies on the back of concerns over domestic inflation in view of higher oil prices and the hike in the reverse repo rate. Gilt prices, however, rose during July-November 2006, *inter alia*, reflecting softening of international crude oil prices. Gilt prices fell and yields rose during December 2006 and January 2007 in view of some tightness in domestic liquidity conditions.

V. FINANCIAL MARKETS

International Financial Markets

During the third quarter (October-December 2006) of 2006-07, short-term interest rates increased further in major advanced economies as some central banks further tightened their policies to contain inflation and stabilise inflationary expectations (Table 33). Since end-September 2006, the European Central Bank has increased its policy rate by 25 basis points each on October 5, 2006 and December 7, 2006. The UK raised its policy rate by 25 basis points each on November 9, 2006 and January 11, 2007. Other advanced economies such as Australia, Sweden and Norway have also increased their policy rates since end-September 2006. The increase in short-term rates in the US since end-September 2006 has been lower than other major advanced economies as the fed funds rate has remained unchanged since end-June 2006. Short-term interest rates declined in a number of emerging market economies (EMEs) as the central banks in some of these economies cut their rates or kept them unchanged.

In line with the upward trend in short-term rates, long-term Government bond yields increased in major advanced economies. Between end-September

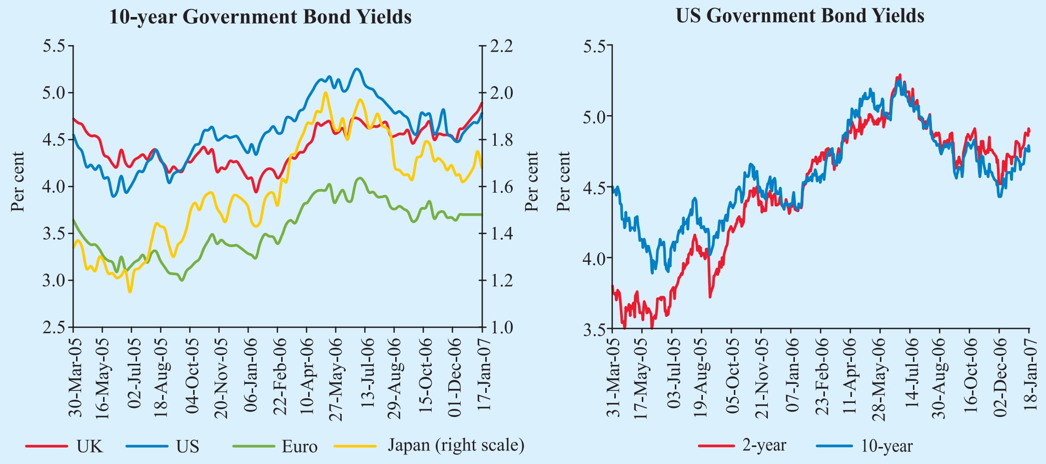
Table 33: Short-term Interest Rates

(Per cent)

Region/Country	At end of							
	March 2005	March 2006	June 2006	September 2006	October 2006	November 2006	December 2006	January 2007*
1	2	3	4	5	6	7	8	9
Advanced Economies								
Euro Area	2.15	2.80	3.06	3.38	3.54	3.63	3.70	3.75
Japan	0.02	0.04	0.24	0.34	0.34	0.40	0.44	0.48
Sweden	1.97	1.99	2.23	2.55	2.74	2.89	2.94	3.14
UK	4.95	4.58	4.70	5.02	5.11	5.20	5.27	5.52
US	2.90	4.77	5.48	5.21	5.23	5.24	5.25	5.24
Emerging Market Economies								
Argentina	4.56	9.63	10.00	10.38	10.13	10.56	10.63	10.19
Brazil	19.25	16.54	15.18	14.17	13.67	13.68	13.19	13.19
China	2.25	2.40	3.00	2.95	3.00	3.50	2.88	2.80
Hong Kong	2.79	4.47	4.67	4.20	4.14	4.10	3.97	3.99
India	**5.37**	**6.11**	**6.36**	**6.60**	**6.65**	**6.69**	**7.19**	**7.14**
Malaysia	2.82	3.51	3.93	3.85	3.80	3.73	3.73	3.73
Philippines	7.25	7.38	8.00	7.63	7.81	6.19	6.56	5.63
Singapore	2.06	3.44	3.50	3.44	3.44	3.40	3.44	3.41
South Korea	3.54	4.26	4.57	4.63	4.61	4.64	4.73	4.93
Thailand	2.64	5.10	5.40	5.40	5.25	5.25	5.20	5.25

* : As on January 17, 2007.
Note : Data for India refer to 91-day Treasury Bills rate and for other countries 3-month money market rates.
Source : The Economist.

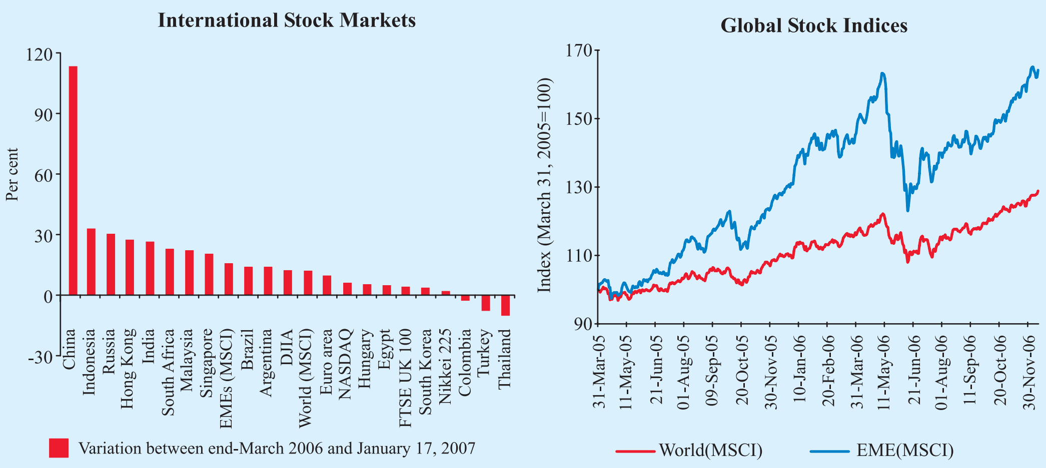
Chart 31: Long-term Yields: Advanced Economies



2006 and January 17, 2007, 10-year yields increased by 43 basis points in the UK, 19 basis points in the US, seven basis points in the euro area and five basis points in Japan (Chart 31). The hardening of yields in the euro area and the UK could be attributed to higher short-term rates in view of further tightening and improved growth prospects. US yields edged higher on the back of stronger than expected data. Since early June 2006, 10-year US bond yields have remained below those on 2-year bonds.

Global equity markets recorded further gains during the third quarter of 2006-07 (Chart 32). The MSCI World and MSCI emerging markets indices

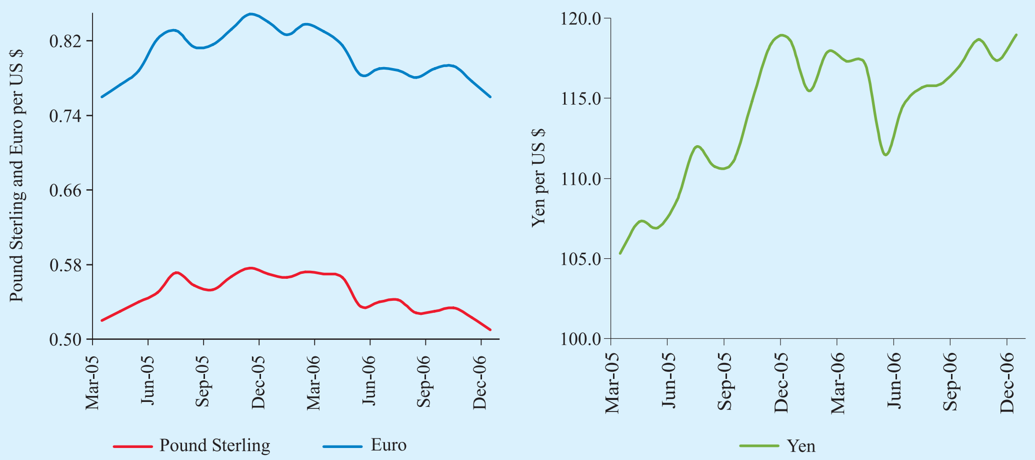
Chart 32: International Stock Markets



increased by 8.5 per cent and 15.2 per cent, respectively, between end-September 2006 and January 17, 2007. Since end-March 2006, these indices have gained 11.9 per cent and 15.7 per cent, respectively. Strong corporate results, better than expected growth in the euro area, strong merger and acquisition activity, pause by the US Federal Reserve and decline in crude oil prices provided support to the equity markets during the third quarter of 2006-07. Stock markets in Thailand declined by 14.8 per cent on December 19, 2006 (over its level on the previous day) following the decision of the Bank of Thailand (BoT) to impose unremunerated reserve requirement (URR) of 30 per cent on short-term capital flows to discourage speculative short-term capital flows. The markets, however, recovered some of these losses the next day as the BoT exempted investments in stock markets from the URR. In the current fiscal year (up to January 17, 2007) amongst major economies, stock markets in China recorded the largest gains (113.3 per cent), followed by Indonesia (32.9 per cent), Russia (30.1 per cent), Hong Kong (27.4 per cent) and India (26.4 per cent).

In the foreign exchange market, the US dollar depreciated against the Pound sterling and the euro during the third quarter of 2006-07, reflecting narrowing of interest rate differentials, moderation of activity in the US and robust growth in the euro area (Chart 33). Between end-September 2006 and January 19, 2007, the US dollar depreciated by 5.2 per cent against the Pound sterling and 2.3 per cent against the euro but appreciated by 3.0 per cent against the yen. Amongst Asian currencies, the US dollar depreciated by 5.0 per cent against Malaysian Ringgit, 3.9 per cent against Thai Baht, 1.6 per cent against Chinese Yuan and 0.9 per cent against Korean Won.

Chart 33: Exchange Rate of Major Currencies per US dollar



Domestic Financial Markets

Indian financial markets remained largely orderly during the third quarter of 2006-07. Short-term money rates remained generally within the reverse repo rate and repo rate corridor till mid-December 2006. However, during the last fortnight of December 2006, call rates shot up. In the foreign exchange market, the Indian rupee appreciated *vis-à-vis* the US dollar during the third quarter. Yields on the longer maturity bonds in the Government securities market softened during October and November 2006 but hardened subsequently. Banks' deposit and lending rates edged up further during the quarter in the wake of strong credit demand. The stock markets recorded further gains, reaching record highs (Table 34). Resources

Table 34: Domestic Financial Markets at a Glance

Month	Call Money		Government Securities		Foreign Exchange				Liquidity Management		Equity			
	Average Daily Turnover (Rs. crore)	Average Call Rates* (Per cent)	Average Turnover in Govt. Securities (Rs. crore)+	Average 10-Year Yield@ (Per cent)	Average Daily Inter-bank Turnover (US $ million)	Average Exchange Rate (Rs. per US $)	RBI's net Foreign Currency Sales(-)/ Purchases (+) (US $ million)	Average Forward Premia 3-month (Per cent)	Average MSS Out-standing# (Rs. crore)	Average Daily Reverse Repo (LAF) Out-standing (Rs. crore)	Average Daily BSE Turnover (Rs. crore)	Average Daily NSE Turnover (Rs. crore)	Average BSE Sensex**	Average S&P CNX Nifty**
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
2004-05@@	**14,170**	**4.65**	**4,826**	**6.22**	**8,892**	**44.93**	**20,847 £**	**1.66**	**46,445**	**35,592**	**2,050**	**4,506**	**5741**	**1805**
2005-06@@	**17,979**	**5.60**	**3,643**	**7.12**	**12,738**	**44.27**	**8,143 £**	**1.60**	**58,792**	**10,986**	**3,248**	**6,253**	**8295**	**2518**
April	17,213	4.77	3,001	7.02	9,880	43.74	0	1.96	65,638	30,675	1,890	4,136	6379	1987
May	15,269	4.99	3,805	7.11	10,083	43.49	0	1.57	68,539	22,754	1,971	3,946	6483	2002
June	20,134	5.10	6,807	6.88	10,871	43.58	-104	1.40	70,651	13,916	2,543	4,843	6926	2134
July	20,046	5.02	3,698	7.13	11,003	43.54	2,473	1.56	70,758	10,754	3,095	6,150	7337	2237
August	16,158	5.02	4,239	7.04	11,749	43.62	1,552	0.69	71,346	34,832	3,452	6,624	7726	2358
September	16,292	5.05	5,207	7.04	11,040	43.92	0	0.62	67,617	30,815	3,871	6,923	8272	2512
October	17,164	5.12	2,815	7.14	13,087	44.82	0	0.69	68,602	18,608	2,955	6,040	8220	2487
November	22,620	5.79	3,314	7.10	11,228	45.73	0	0.67	67,041	3,268	2,635	5,479	8552	2575
December	21,149	6.00	2,948	7.13	13,808	45.64	-6,541	1.51	52,040	1,452	3,516	6,814	9162	2773
January	17,911	6.83	3,094	7.15	16,713	44.40	0	2.60	40,219	-15,386	3,966	7,472	9540	2893
February	13,497	6.95	2,584	7.32	15,798	44.33	2,614	2.85	33,405	-13,532	3,688	7,125	10090	3019
March	18,290	6.58	2,203	7.40	17,600	44.48	8,149	3.11	29,652	-6,319	5,398	9,518	10857	3236
2006-07														
April	16,909	5.62	3,685	7.45	17,712	44.95	4,305	1.31	25,709	46,088	4,860	9,854	11742	3494
May	18,074	5.54	3,550	7.58	18,420	45.41	504	0.87	26,457	59,505	4,355	9,155	11599	3437
June	17,425	5.73	2,258	7.86	15,310	46.06	0	0.73	31,845	48,610	3,130	6,854	9935	2915
July	18,254	5.86	2,243	8.26	14,086 P	46.46	0	0.83	36,936	48,027	2,604	5,652	10557	3092
August	21,294	6.06	5,786	8.09	15,630 P	46.54	0	1.22	40,305	36,326	2,867	5,945	11305	3306
September	23,665	6.33	8,306	7.76	17,837 P	46.12	0	1.31	40,018	25,862	3,411	6,873	12036	3492
October	26,429	6.75	4,313	7.65	16,233 P	44.47	0	1.67	41,537	12,262	3,481	6,919	12637	3649
November	25,649	6.69	10,654	7.52	20,207 P	44.85	3,198	2.07	38,099	9,937	4,629	8,630	13416	3869
December	24,168	8.63	5,362	7.55	19,827 P	44.64	-	3.20	38,148	-1,713	4,276	8,505	13628	3910

* : Average of daily weighted call money borrowing rates.
\+ : Average of daily outright turnover in Central Government dated securities.
@ : Average of daily closing rates.
\# : Average of weekly outstanding MSS.
@@ : Data are monthly averages.
** : Average of daily closing indices.
£ : Cumulative for the financial year.
LAF : Liquidity Adjustment Facility.
BSE : The Stock Exchange, Mumbai.
NSE : National Stock Exchange of India Ltd.
MSS : Market Stabilisation Scheme.
P : Provisional.
\- : Not available.

Note : In column 11, (-) indicates injection of liquidity while (+) indicates absorption of liquidity.

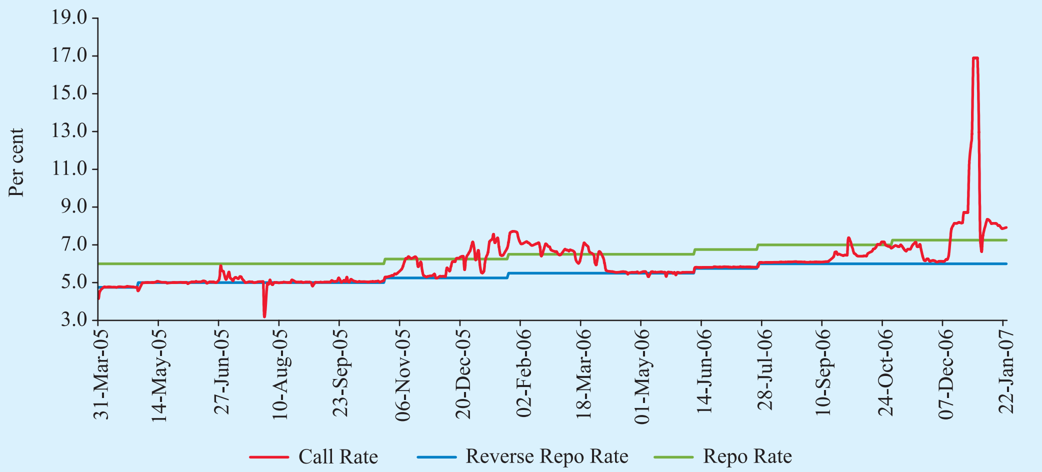
raised in the primary market segment of the equity market during the third quarter of 2006-07 were higher than the preceding quarter.

Money Market

Call money rate remained generally close to the reverse repo rate up to mid-September 2006 (Chart 34). Liquidity conditions, however, became relatively tighter in the second half of September 2006 on account of advance tax outflows and festival season currency demand amidst high credit demand. Call rates crossed the repo rate and touched 7.38 per cent as on September 29, 2006. Call rates eased below the repo rate by early October 2006 and remained mostly within repo-reverse repo corridor till early November 2006 as liquidity pressures eased, partly on account of reduction in Centre's surplus. Call rates eased further to reverse repo levels by the last week of November 2006, but edged higher from the second week of December 2006, crossing the repo rate to touch 16.88 per cent on December 29, 2006 under the impact of advance tax outflows and hike of 25 basis points each in the cash reserve ratio (CRR) effective the fortnights beginning December 23, 2006 and January 6, 2007. Call rates eased in the first week of January 2007 on the back of improvement in liquidity conditions. The call rate was 7.88 per cent as on January 23, 2007, 81 basis points higher than that at end-September 2006 and 124 basis points higher than that at end-March 2006.

A screen-based negotiated quote-driven system for all dealings in call/notice and term money markets (NDS-CALL), as announced in the Annual Policy Statement for the year 2005-06, was launched on September 18, 2006. The

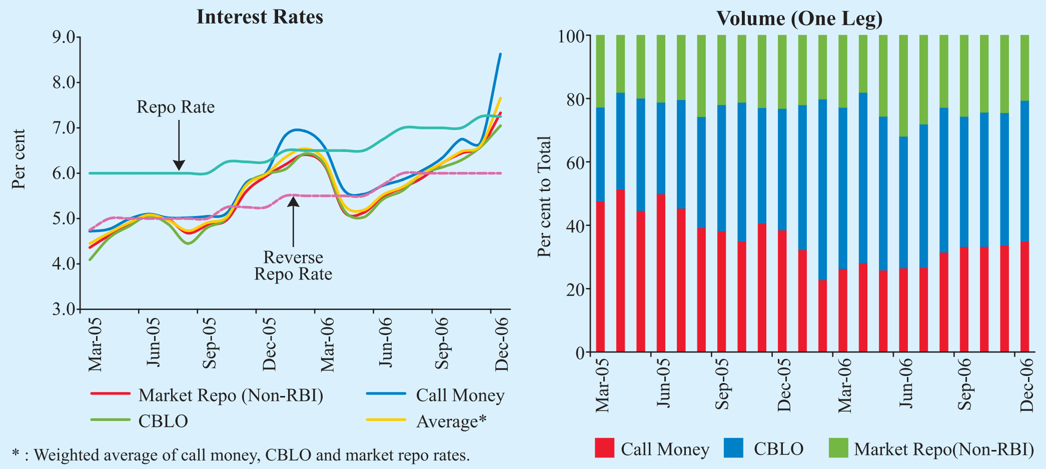
Chart 34: Call Rate



dealing on this platform is optional; 80 banks (including 15 co-operative banks) and 10 primary dealers have taken membership of NDS-CALL so far. Trading on NDS-CALL is expected to bring about increased transparency and better price discovery in the call money market.

Interest rates in the collateralised segments of the money market – the market repo (outside the LAF) and the Collateralised Borrowing and Lending Obligation (CBLO) – remained below the call rate during the third quarter. Till mid-December 2006, these rates remained within repo - reverse repo rate corridor. In tandem with tightness in money markets, interest rates in these segments also edged up and crossed the repo rate in the second half of December 2006, but remained below the call rates. During October-December 2006, the CBLO and market repo rates averaged 6.64 per cent and 6.79 per cent, respectively, as compared with 7.36 per cent in the call market. During the fiscal year 2006-07 (up to December 2006), interest rates averaged 5.92 per cent and 5.99 per cent in the CBLO and market repo segments, respectively, as compared with 6.36 per cent in the call money market. The weighted average interest rate of call, CBLO and market repo increased from 6.29 per cent in March 2006 and 6.22 per cent in September 2006 to 7.66 per cent in December 2006; the weighted average interest rate was 7.49 per cent as on January 23, 2007. The collateralised market is now the predominant segment in the money market, with a share of around 65 per cent in total volume during 2006-07 so far (Chart 35 and Table 35). Mutual funds and financial institutions are the major lenders in the CBLO market with nationalised banks being the major borrowers. In the market repo segment, mutual funds are the major provider of funds, while foreign banks, private sector banks and primary dealers are the major borrowers.

Chart 35: Money Markets: Interest Rates and Volume



* : Weighted average of call money, CBLO and market repo rates.

Table 35: Activity in Money Market Segments

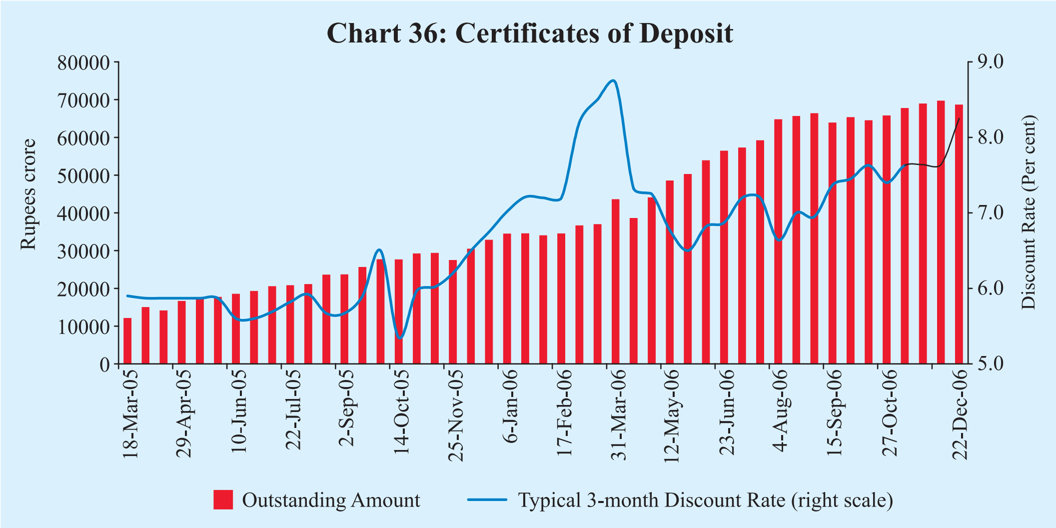
(Rupees crore)

Month	Average Daily Volume (One Leg)				Commercial Paper		Certificates of Deposit Outstanding
	Call Money Market	Repo Market (outside the LAF)	Collateralised Borrowing and Lending Obligation (CBLO)	Term Money Market	Outstanding	Amount Issued	
1	2	3	4	5	6	7	8
2004-05 *	**7,085**	**4,284**	**3,349**	**263**	**11,723**	**1,090**	**6,052**
2005-06 *	**8,990**	**5,296**	**10,020**	**417**	**17,285**	**3,140**	**27,298**
April	8,607	3,044	5,185	331	15,598	3,549	16,602
May	7,635	3,422	6,117	273	17,182	3,824	17,689
June	10,067	4,291	5,896	267	17,797	2,925	19,270
July	10,023	4,526	7,646	359	18,607	3,360	20,768
August	8,079	5,331	7,272	377	19,508	4,110	23,568
September	8,146	4,718	8,572	558	19,725	2,519	27,641
October	8,582	5,245	10,882	367	18,726	2,892	29,193
November	11,310	6,415	10,248	459	18,013	2,483	27,457
December	10,575	6,394	10,633	388	17,234	3,304	32,806
January	8,956	6,149	12,817	545	16,431	1,937	34,521
February	6,749	6,024	17,081	407	15,876	3,160	34,487
March	9,145	7,991	17,888	669	12,718	2,813	43,568
2006-07							
April	8,455	5,479	16,329	447	16,525	6,065	44,059
May	9,037	9,027	17,147	473	16,922	4,701	50,228
June	8,713	10,563	13,809	628	19,650	4,981	56,390
July	9,127	9,671	15,670	432	21,110	5,812	59,167
August	10,647	7,764	15,589	510	22,854	6,460	65,621
September	11,833	9,185	14,771	568	24,419	5,220	65,274
October	13,214	9,721	16,964	466	23,171	3,373	65,764
November	12,825	9,374	16,069	348	24,238	6,392	68,910
December	12,084	7,170	15,512	481	23,336	3,080	68,619

* : Data are monthly averages.

Certificates of Deposit

The outstanding amount of certificates of deposit (CDs) increased further during the third quarter of 2006-07 as banks continued to supplement their efforts at deposit mobilisation to support sustained credit demand (Table 35 and Chart 36). The amount of outstanding CDs increased from Rs.65,274 crore at end-September 2006 (4.5 per cent of aggregate deposits of issuing banks with significant intra-group variation) to Rs.68,619 crore (4.3 per cent) by December 22, 2006. The weighted average discount rate (WADR) of CDs of '6 months to less than 1 year' maturity at 8.28 per cent as on December 22, 2006 was 48 basis points higher than its level (7.80 per cent) at end-September 2006. Mutual funds have emerged as key investors in CDs. The fact that CDs can be traded makes them attractive for investors like mutual funds, who look for easily encashable investments.



Commercial Paper

After increasing in each of the previous two quarters, the outstanding amount of commercial papers (CPs) declined marginally during the third quarter from Rs.24,419 crore as on September 30, 2006 to Rs.23,336 crore as on December 31, 2006 (Chart 37). The weighted average discount rate (WADR) on CPs increased from 7.70 per cent on September 30, 2006 to 8.52 per cent as on December 31, 2006 in tandem with the increase in the money market rates. The discount rate on CPs moved from a range of 7.10-9.25 per cent during the fortnight ended September 30, 2006 to 7.74-10.00 per cent during the fortnight ending

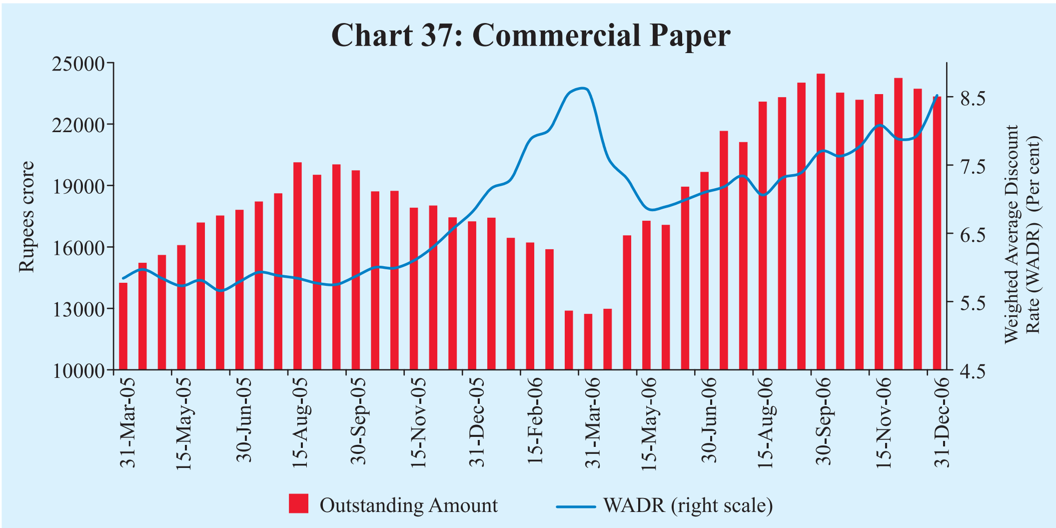


Table 36: Commercial Paper – Major Issuers

(Rupees crore)

Category of Issuer	End of				
	March 2005	March 2006	June 2006	September 2006	December 2006
1	2	3	4	5	6
Leasing and Finance	8,479 (59.6)	9,400 (73.9)	13,460 (68.5)	15,792 (64.6)	15,060 (64.5)
Manufacturing	2,881 (20.2)	1,982 (15.6)	4,155 (21.1)	4,847 (19.9)	4,611 (19.8)
Financial Institutions	2,875 (20.2)	1,336 (10.5)	2,035 (10.4)	3,780 (15.5)	3,665 (15.7)
Total	**14,235** **(100.0)**	**12,718** **(100.0)**	**19,650** **(100.0)**	**24,419** **(100.0)**	**23,336** **(100.0)**

Note : Figures in parentheses are percentage shares to the total.

December 31, 2006. The most preferred tenors of CPs were '61 to 90 days' and '181 days and above'.

Leasing and finance companies continued to remain the pre-dominant issuers of CPs in the absence of the access of these companies to public deposits (Table 36).

Treasury Bills

The primary market yields on Treasury Bills (TBs), after remaining broadly unchanged during October-November 2006, increased during December 2006 (Chart 38). The yield spread between 364-day and 91-day TBs narrowed to eight basis points in December 2006 from 40 basis points in September 2006 (Table 37).

Chart 38: Yields on Treasury Bills

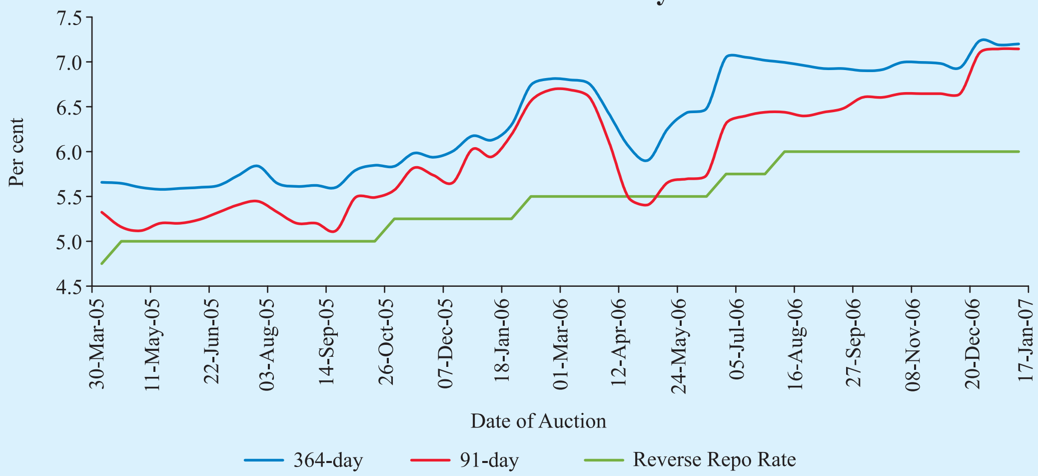


Table 37: Treasury Bills in the Primary Market

Month	Notified Amount (Rupees crore)	Average Implicit Yield at Minimum Cut-off Price (Per cent)			Average Bid-Cover Ratio		
		91-day	182-day	364-day	91-day	182-day	364-day
1	2	3	4	5	6	7	8
2004-05 *	**1,38,500 @**	**4.91**	**–**	**5.16**	**2.43**	**–**	**2.52**
2005-06 *	**1,55,500 @**	**5.68**	**5.82**	**5.96**	**2.64**	**2.65**	**2.45**
April	19,000	5.17	5.36	5.62	4.03	4.48	2.54
May	15,000	5.19	5.35	5.58	3.30	3.37	2.29
June	18,500	5.29	5.37	5.61	1.54	2.42	1.81
July	11,500	5.46	5.67	5.81	1.21	1.79	1.68
August	21,000	5.23	5.42	5.63	3.07	2.68	2.54
September	23,000	5.24	5.37	5.70	1.52	1.45	1.61
October	15,000	5.50	5.71	5.84	1.69	1.53	3.44
November	11,000	5.76	5.85	5.96	2.12	1.92	2.30
December	5,000	5.89	6.00	6.09	3.07	2.97	2.36
January	5,000	6.25	6.22	6.21	2.86	2.83	2.72
February	5,000	6.63	6.74	6.78	3.04	2.07	2.71
March	6,500	6.51	6.66	6.66	4.17	3.43	3.36
2006-07							
April	5,000	5.52	5.87	5.98	5.57	4.96	2.02
May	18,500	5.70	6.07	6.34	1.88	1.84	1.69
June	15,000	6.14	6.64	6.77	1.63	1.35	2.11
July	16,500	6.42	6.75	7.03	1.82	1.55	3.12
August	19,000	6.41	6.70	6.96	2.03	2.71	3.48
September	15,000	6.51	6.76	6.91	1.35	1.80	2.92
October	15,000	6.63	6.84	6.95	1.31	1.20	2.02
November	18,500	6.65	6.92	6.99	1.33	1.22	2.49
December	15,000	7.01	7.27	7.09	1.19	1.29	3.34
January ^	11,500	7.14	7.14	7.23	1.29	2.54	1.64

***** : Data are monthly averages. @ : Total for the financial year. ^ : Up to January 19, 2007.

Note : 1. 182-day TBs were reintroduced with effect from April 2005.

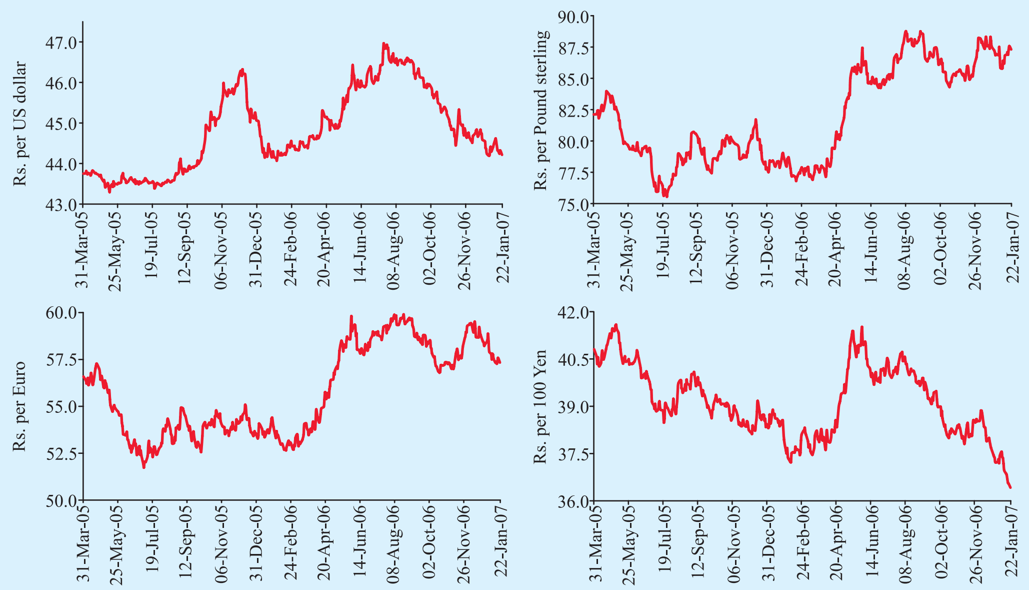
2. For 91-day TBs, notified amount of Rs.2,000 crore includes Rs.1,500 crore under the Market Stabilisation Scheme (MSS). For 182-day TBs, notified amount of Rs.1,500 crore includes Rs.1,000 crore under the MSS. For 364-day TBs, notified amount of Rs.2,000 crore includes Rs.1,000 crore under the MSS.

Notified amount of Rs.1,500 crore each for auctions of the 91-day TBs under the Market Stabilisation Scheme (MSS) were not fully subscribed at some of the auctions during the quarter October-December 2006, reflecting tight liquidity conditions. There was, however, no devolvement on the PDs.

Foreign Exchange Market

In the foreign exchange market, the Indian rupee appreciated *vis-à-vis* the US dollar during the quarter ended December 2006. The rupee, which had started to appreciate from the last week of July 2006 on the back of revival of FII inflows and easing of international crude oil prices, rose further amidst weakness of the US dollar in the international markets. The rupee has moved in a range of Rs.44.20–46.97 per US dollar during 2006-07 so far (up to January 23, 2007) (Chart 39). The exchange rate was Rs.44.22 per US dollar as on January 23, 2007; it has recorded an appreciation of 3.9 per cent over its level as at end-September 2006. On a fiscal year basis (up to January 23, 2007), the

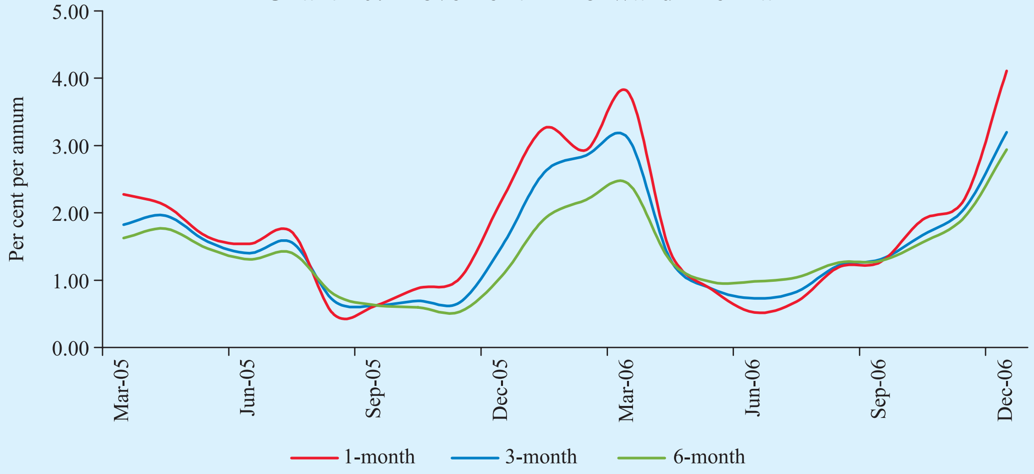
Chart 39: Movement of Rupee *vis-a-vis* Major Currencies

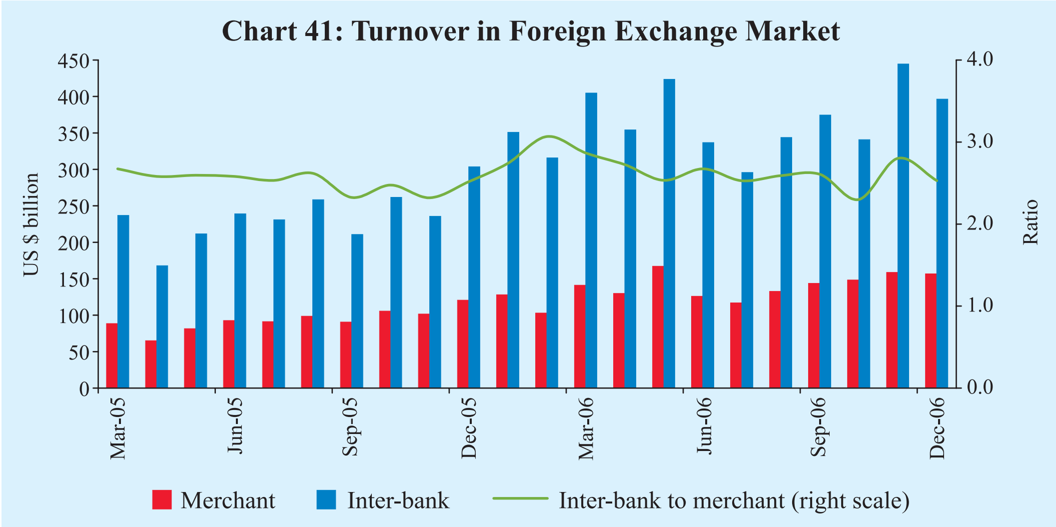


rupee has appreciated by 0.9 per cent *vis-à-vis* the US dollar and 4.6 per cent against the Japanese yen but depreciated by 11.1 per cent against the Pound sterling and 5.3 per cent against the euro.

Forward premia increased further during the third quarter of 2006-07, reflecting increase in domestic interest rates (Chart 40).

Chart 40: Movement in Forward Premia





The turnover in the inter-bank as well as merchant segments of the foreign exchange market increased to US $ 549 billion (monthly average) during the third quarter of 2006-07 from US $ 376 billion in the corresponding period of 2005-06. While inter-bank turnover increased from US $ 267 billion during the third quarter of 2005-06 to US $ 394 billion in the third quarter of 2006-07, the merchant turnover increased from US $ 109 billion to US $ 155 billion (Chart 41). The ratio of inter-bank to merchant turnover was marginally higher at 2.5 during the third quarter of 2006-07 as compared with 2.4 a year ago.

Credit Market

The interest rates offered by public sector banks (PSBs) on deposits of maturity of more than one year and up to three years were placed in the range of 6.75-8.25 per cent in January 2007 as compared with 6.25-7.50 per cent in September 2006 while those on deposits of maturity of above three years were placed in the range of 7.00-8.50 per cent in January 2007 as compared with 6.50-8.00 per cent in September 2006 (Table 38 and Chart 42). The interest rates offered by private sector banks on deposits of maturity up to one year were placed in the range of 3.00-8.25 per cent in January 2007 as compared with 3.00-7.25 per cent in September 2006 while those on deposits of maturity above three years were placed in the range of 7.00-9.25 per cent in January 2007 as compared with 6.75-8.50 per cent in September 2006. As regards foreign banks, the rates offered on deposits of maturity up to one year were placed in the range of 3.00-8.00 per cent in January 2007 as compared with 3.00-7.50 per cent in September 2006. On the lending side, most PSBs and some private sector banks have raised their Benchmark Prime Lending Rates (BPLRs) since

Table 38: Movements in Deposit and Lending Rates

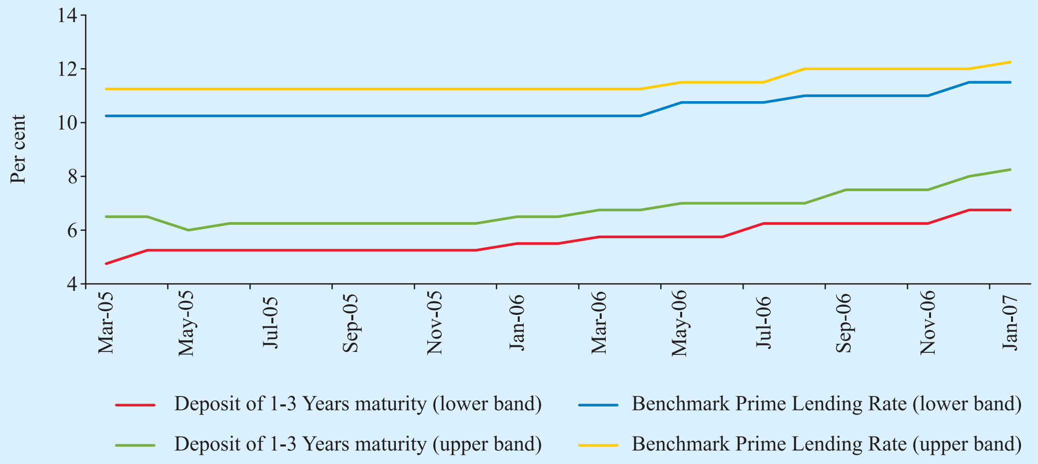
(Per cent)

Interest Rate	March 2005	March 2006	June 2006	September 2006	October 2006	November 2006	December 2006	January 2007
1	2	3	4	5	6	7	8	9
1. Domestic Deposit Rate								
Public Sector Banks								
Up to 1 year	2.75-6.00	2.25-6.50	2.75-6.50	2.75-7.00	2.75-7.00	2.75-7.00	2.75-7.00	2.75-7.50
More than 1 year and up to 3 years	4.75-6.50	5.75-6.75	5.75-7.00	6.25-7.50	6.25-7.50	6.25-7.50	6.75-8.00	6.75-8.25
More than 3 years	5.25-7.00	6.00-7.25	6.00-7.25	6.50-8.00	6.75-8.00	6.75-8.00	7.00-8.00	7.00-8.50
Private Sector Banks								
Up to 1 year	3.00-6.25	3.50-7.25	3.50-6.75	3.00-7.25	3.00-8.00	3.00-8.00	3.00-8.00	3.00-8.25
More than 1 year and up to 3 years	5.25-7.25	5.50-7.75	6.50-7.75	6.75-8.25	6.75-8.25	6.75-8.25	6.40-8.50	6.75-9.25
More than 3 years	5.75-7.00	6.00-7.75	6.50-8.25	6.75-8.50	6.75-8.50	7.00-8.50	7.00-8.50	7.00-9.25
Foreign Banks								
Up to 1 year	3.00-6.25	3.00-6.15	3.25-6.50	3.00-7.50	3.00-7.50	3.00-7.25	3.00-7.25	3.00-8.00
More than 1 year and up to 3 years	3.50-6.50	4.00-6.50	5.00-6.50	3.50-8.15	3.50-8.15	3.50-8.15	3.50-8.15	3.50-8.15
More than 3 years	3.50-7.00	5.50-6.50	5.50-6.75	4.00-8.25	4.00-8.25	4.05-8.25	4.05-8.25	4.05-8.00
2. Benchmark Prime Lending Rate								
Public Sector Banks	10.25-11.25	10.25-11.25	10.75-11.50	11.00-12.00	11.00-12.00	11.00-12.00	11.50-12.00	11.50-12.25
Private Sector Banks	11.00-13.50	11.00-14.00	11.00-14.50	11.50-15.00	11.50-15.00	11.50-15.00	11.50-15.00	11.75-15.50
Foreign Banks	10.00-14.50	10.00-14.50	10.00-14.50	10.00-14.50	10.00-14.50	10.00-14.50	10.00-14.50	10.00-14.50
3. Actual Lending Rate*								
Public Sector Banks	2.75-16.00	4.00-16.50	4.00-16.50	4.00-16.50	-	-	-	-
Private Sector Banks	3.15-22.00	3.15-20.50	3.15-26.00	3.15-24.00	-	-	-	-
Foreign Banks	3.55-23.50	4.75-26.00	4.75-25.00	4.50-23.00	-	-	-	-

* : Interest rate on non-export demand and term loans above Rs.2 lakh excluding lending rates at the extreme five per cent on both sides.

September 2006. The range of BPLRs of PSBs changed to 11.50-12.25 per cent in January 2007 from 11.00-12.00 per cent in September 2006. The weighted

Chart 42: Deposit and Lending Rates - Public Sector Banks



average BPLR of PSBs increased from 10.7 per cent in March 2006 to 11.3 per cent in September 2006 and further to 11.6 per cent in December 2006. The weighted average BPLR of private sector banks increased from 12.4 per cent in March 2006 to 12.9 per cent in September 2006 and further to 13.2 per cent in December 2006. The weighted average BPLR of foreign banks at 12.7 per cent in December 2006 was the same as that in March 2006 and September 2006.

Government Securities Market

Yields on 10-year paper hardened in the first quarter to reach a peak of 8.40 per cent on July 11, 2006, an increase of 88 basis points over end-March 2006. Subsequently, yields softened in consonance with easing of Government bond yields in the US, the Fed's decision to keep the fed funds rate unchanged, easing of crude oil prices and increased demand for gilts from banks to meet their SLR requirements. The announcement of the borrowing calendar of the Central Government for the second half of 2006-07 was in accordance with market expectations. The 10-year yield reached a low of 7.38 per cent as on November 28, 2006. There was, however, hardening of the yields from the second half of December 2006 in tandem with the tightness in liquidity conditions on the back of advance tax outflows and hike in the cash reserve ratio. The 10-year yield was 7.87 per cent as on January 23, 2007, 20 basis points higher than the level at end-September 2006 and 35 basis points higher than the level as on March 31, 2006 (7.52 per cent) (Chart 43). The yield curve flattened during the quarter, with the spread between 1-10 year yields narrowing from 94 basis points at end-September 2006 to 34 basis points at end-December 2006. The spread between 10-year and 30-year yields also narrowed from 61 basis points at end-September 2006 to 17 basis points at end-December 2006 (30 basis points at end-March 2006).

Chart 43: Yields on Central Government Securities

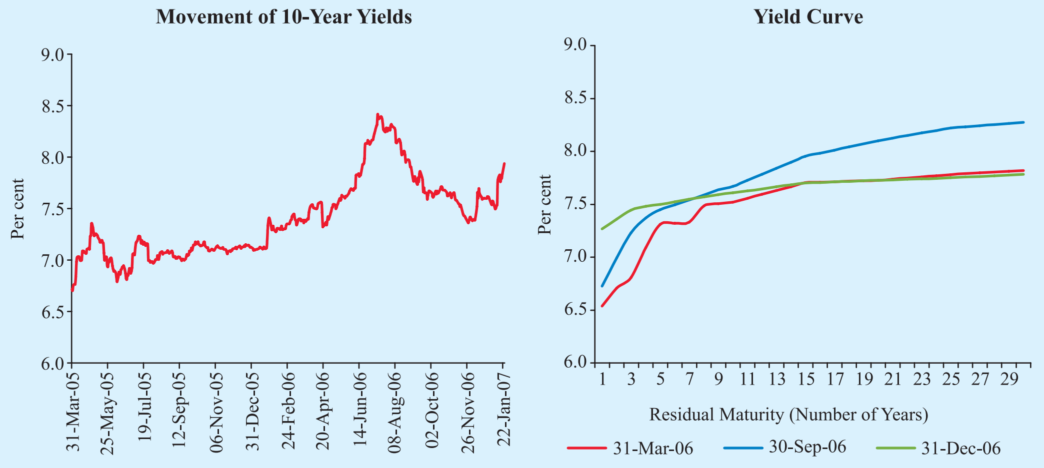
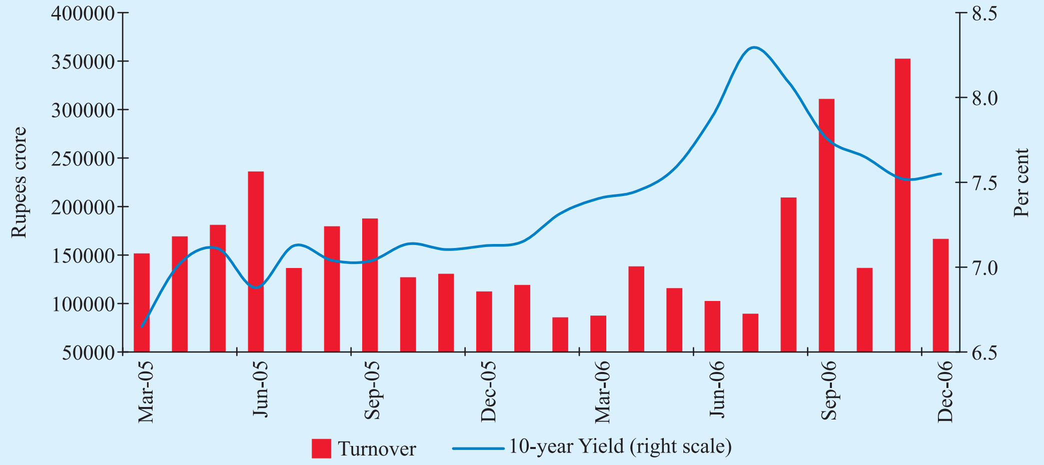


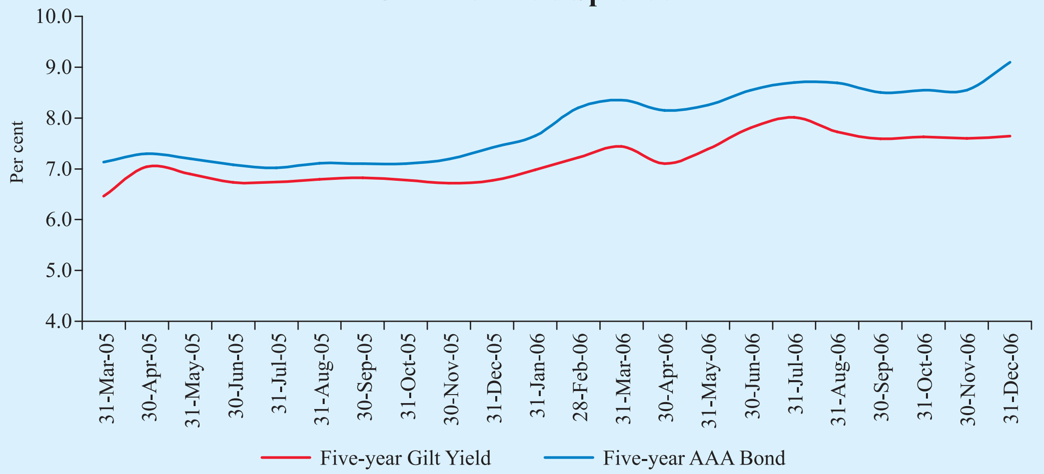
Chart 44: Government Securities Turnover and Yields



The turnover in Government securities has increased since August 2006 in tandem with easing of yields (Chart 44). The decline in turnover in October 2006 partly reflected lower number of trading days while that in December 2006 could be attributed to tight liquidity conditions.

The yields on 5-year AAA-rated corporate bonds increased during the third quarter of 2006-07. The yield spread between 5-year AAA-rated bonds and 5-year Government securities, thus, widened to 146 basis points at end-December 2006 from that of 91 basis points at end-September 2006 as well as at end-March 2006 (Chart 45).

Chart 45: Yield Spreads



Equity Market

Primary Market

Resources raised through the public issues segment picked-up during the quarter ended December 2006 *vis-à-vis* the previous quarter. Cumulative resources raised through public issues during April-December 2006 increased by 33.0 per cent to Rs. 25,365 crore, even as the number of issues came down from 88 to 78 (Table 39). The average size of public issues increased from Rs.217 crore during April-December 2005 to Rs.325 crore during April-December 2006. Except one issue, all public issues during April-December 2006 were in the form of equity. Out of 78 issues during April-December 2006, 41 issues were initial public offerings (IPOs), accounting for 78.7 per cent of resource mobilisation.

Table 39: Mobilisation of Resources from the Primary Market

(Amount in Rupees crore)

Item	No. of Issues	Amount	No. of Issues	Amount
1	2	3	4	5
	2005-06 (April-December)		2006-07 (April-December) P	
A. Prospectus and Rights Issues*				
1. Private Sector (a+b)	**85**	**16,553**	**78**	**25,365**
a) Financial	6	6,982	5	1,031
b) Non-financial	79	9,571	73	24,334
2. Public Sector (a+b+c)	**3**	**2,520**	**-**	**-**
a) Public Sector Undertakings	-	-	-	-
b) Government Companies	-	-	-	-
c) Banks/Financial Institutions	3	2,520	-	-
3. Total (1+2)	**88**	**19,073**	**78**	**25,365**
Of which:				
(i) Equity	87	18,955	77	24,874
(ii) Debt	1	118	1	491
	2005-06 (April-September)		2006-07 (April-September)	
B. Private Placement				
1. Private Sector	**471**	**22,893**	**697**	**38,241**
a) Financial	179	13,681	259	21,834
b) Non-financial	292	9,212	438	16,407
2. Public Sector	**83**	**22,800**	**54**	**32,797**
a) Financial	62	14,257	47	28,033
b) Non-financial	21	8,543	7	4,764
3. Total (1+2)	**554**	**45,693**	**751**	**71,038**
Memo:				
Euro Issues@	**34**	**8,825**	**35**	**8,841**

P : Provisional. * : Excluding offers for sale. – : Nil/Negligible. @: April-December.

Mobilisation of resources through private placement increased by 55.5 per cent to Rs.71,038 crore during April-September 2006 over the corresponding period of the previous year (Table 39). Resources mobilised by private sector entities increased by 67.0 per cent, while those by public sector entities increased by 43.8 per cent during April-September 2006. Financial intermediaries (both from public sector and private sector) accounted for the bulk (70.2 per cent) of the total resource mobilisation from private placement market during April-September 2006 (61.1 per cent during April-September 2005).

The resources raised through Euro issues - American Depository Receipts (ADRs) and Global Depository Receipts (GDRs) - by Indian corporates during April-December 2006 at Rs.8,841 crore were almost the same as in the corresponding period of previous year (Table 39).

During April-December 2006, net mobilisation of resources by mutual funds increased substantially by 190 per cent to Rs.79,708 crore over the corresponding period of 2005 (Table 40). Bulk of the net mobilisation of funds was under income/debt-oriented schemes (73.0 per cent of total), while growth/equity-oriented schemes accounted for 25.8 per cent of the net mobilisation of funds.

Secondary Market

The domestic stock markets remained buoyant and recorded further gains during the third quarter of 2006-07 (Chart 46). Continued buying by FIIs on the back of strong domestic fundamentals, robust corporate results, upward trend in the international equity markets and decline in global crude oil prices provided support to domestic stock markets. Domestic stock markets declined during May-June, 2006 in consonance with global trends amidst

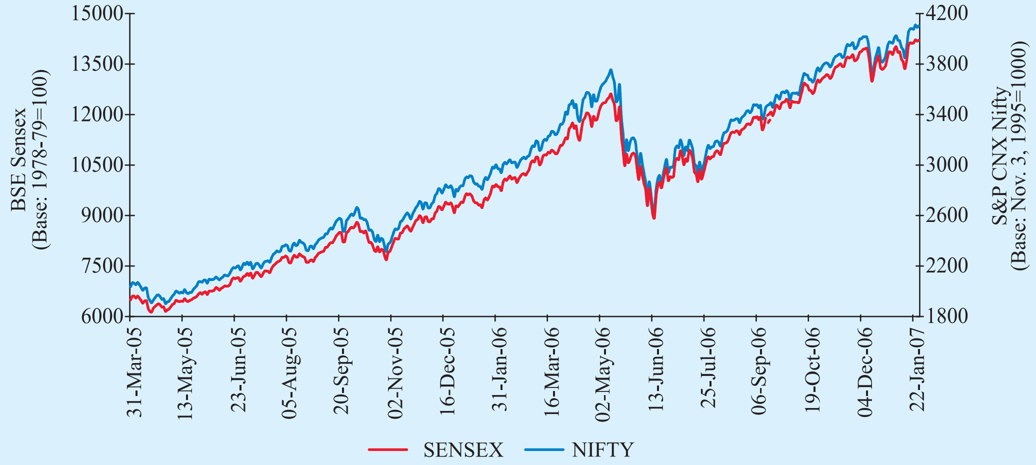
Table 40: Resource Mobilisation by Mutual Funds

(Rupees crore)

Mutual Fund	April-March 2005-06		April-December 2005-06		April-December 2006-07	
	Net Mobilisation @	Net Assets #	Net Mobilisation @	Net Assets *	Net Mobilisation @	Net Assets *
1	2	3	4	5	6	7
Private Sector	42,977	1,81,515	20,824	1,55,260	64,140	2,56,725
Public Sector	6,379	20,829	5,683	18,760	6,364	28,765
UTI	3,424	29,519	1,032	25,228	9,204	38,108
Total	**52,780**	**2,31,862**	**27,537**	**1,99,248**	**79,708**	**3,23,598**

@ : Net of redemptions. # : As at end of March. * : As at end of December.
Source : Securities and Exchange Board of India.

Chart 46: Indian Stock Markets



increased risk aversion over concerns of slowdown in global growth, increase in global inflation, higher international interest rates and meltdown in base metal prices. The BSE Sensex reached 8929 as on June 14, 2006, a decline of 29.2 per cent over the then all-time high of 12612 reached on May 10, 2006. Stock markets recovered these losses in the following months, reflecting fresh buying by FIIs, recovery in base metal prices and decline in international crude oil prices amidst continuing robust macroeconomic fundamentals. The BSE Sensex reached a new high of 13972 on December 7, 2006. The markets witnessed some correction in the next few days, *inter alia*, due to profit taking at higher levels, deceleration in industrial activity for October 2006, announcement of CRR hike and the decision of the Bank of Thailand (BoT) to impose unremunerated reserve requirement (URR) on short-term capital flows. The markets, however, recovered in the next few days. The BSE Sensex closed at all-time high of 14218 on January 18, 2007. The Sensex was 14041 on January 23, 2007, 24.5 per cent above its end-March 2006 level.

Profits after tax of corporates exhibited further improvement in the second quarter of 2006-07. Ratio of profits after tax to sales also improved to 11.0 per cent during the quarter ended September 2006 from 10.6 per cent in the preceding quarter and 8.5 per cent a year ago (Table 41 and Chart 47).

FIIs turned net sellers in Indian stock markets in December 2006 after making large purchases during August-November 2006. According to the Securities and Exchange Board of India (SEBI), FIIs made net purchases of Rs.18,176 crore (US $ 3.9 billion) during 2006-07 (up to January 22, 2007) as compared with net purchases of Rs.33,461 crore (US $ 7.5 billion) during the corresponding period of the previous year (Chart 48). Mutual funds have also

Table 41: Corporate Financial Performance

(Growth rates in per cent)

Item	2003-04	2004-05	2005-06	2005-06	2006-07	2005-06				2006-07	
				April-September		Q1	Q2	Q3	Q4	Q1	Q2
1	2	3	4	5	6	7	8	9	10	11	12
Sales	16.0	24.1	16.9	17.2	27.4	18.5	16.4	13.2	19.5	25.6	29.2
Expenditure	14.4	22.9	16.4	16.6	25.6	18.0	16.3	12.7	18.9	24.6	26.6
Gross Profits	25.0	32.5	20.3	26.7	39.8	32.0	19.1	21.2	16.6	33.9	45.9
Interest	-11.9	-5.8	1.9	-10.3	20.8	-13.5	-8.0	4.6	3.8	19.9	18.0
Profits After Tax	59.8	51.2	24.2	41.3	41.6	54.2	27.5	27.0	15.1	34.7	49.4
Select Ratios (Per cent)											
Gross Profits to Sales	11.1	11.9	13.0	13.3	15.6	13.1	13.0	12.8	12.7	15.6	15.9
Profits After Tax to Sales	5.9	7.2	8.7	8.7	10.6	8.6	8.5	8.6	8.7	10.6	11.0
Interest Coverage Ratio	3.3	4.6	6.4	6.0	7.1	6.0	6.2	6.2	7.3	7.2	7.8
Interest to Sales	3.4	2.6	2.0	2.2	2.2	2.2	2.1	2.1	1.7	2.2	2.0
Interest to Gross Profits	30.7	21.8	15.7	16.6	14.1	16.6	16.2	16.2	13.7	13.9	12.8
Memo:											(Amount in Rupees crore)
No. of Companies	2,214	2,214	2,210	2,128	2,053	2,355	2,361	2,366	2,415	2,228	2,263
Sales	4,42,743	5,49,449	7,74,578	3,67,769	4,24,565	1,94,608	2,12,693	2,19,098	2,49,971	2,34,610	2,51,125
Expenditure	4,22,110	5,14,574	6,66,690	3,15,139	3,53,505	1,66,972	1,83,717	1,88,934	2,18,511	1,95,556	2,09,437
Depreciation Provision	20,406	22,697	28,883	13,625	15,710	7,137	7,617	7,748	8,340	8,449	8,892
Gross Profits	49,278	65,301	100,666	48,781	66,265	25,577	27,620	28,135	31,652	36,567	40,041
Interest	15,143	14,268	15,789	8,083	9,358	4,241	4,467	4,555	4,348	5,083	5,121
Profits After Tax	26,182	39,599	67,506	32,016	44,927	16,726	18,169	18,790	21,634	24,845	27,710

Note : 1. Growth rates are percentage change in the level for the period under reference over the corresponding period of the previous year.

2. Data in column (2) and (3) are based on audited balance sheets while those in column (4) onwards are based on the un-audited/audited abridged results of the non Government non-financial companies.

made net investments of Rs.12,172 crore in the current financial year so far (up to January 19, 2007) as compared with net purchases of Rs.9,438 crore during the corresponding period of last year.

Chart 47: Corporate Performance - Growth Rates

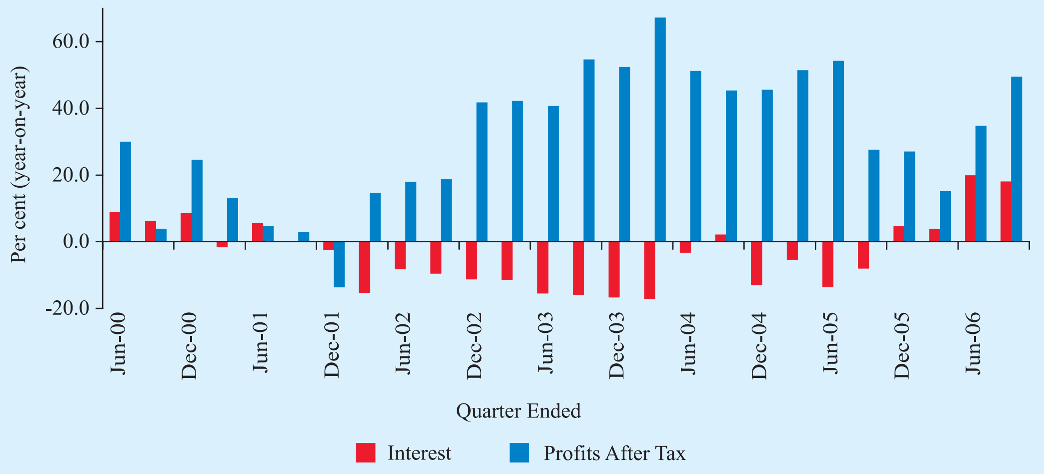
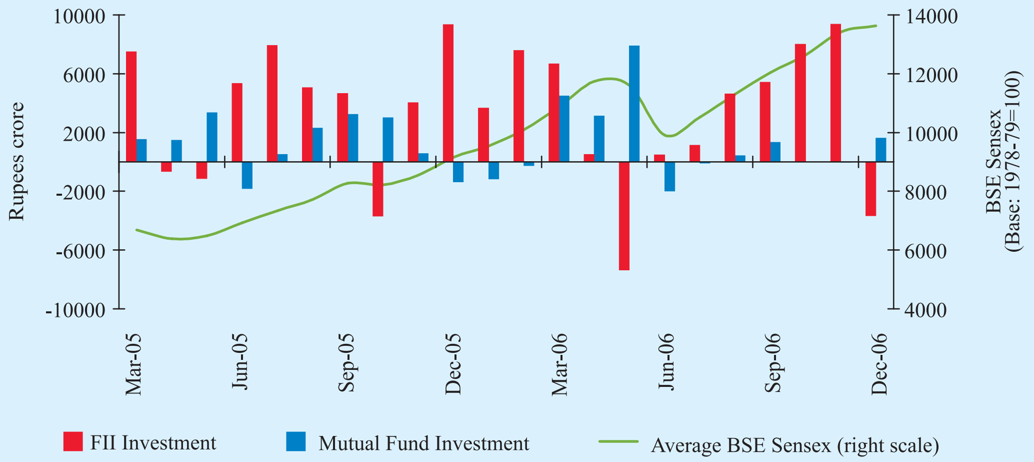


Chart 48: Institutional Investment and Stock Market



Major indices and sectors have shown mixed trends during 2006-07 so far (Chart 49). On a point-to-point basis (up to January 22, 2007), BSE 500, BSE Mid-cap and BSE Small-cap increased by 20.7 per cent, 13.8 per cent and 14.8 per cent, respectively. Amongst major sectors, bank stocks recorded gains of 42.0 per cent over end-March 2006, followed by oil and gas (34.7 per cent), IT stocks (32.8 per cent), consumer durables (20.2 per cent), capital goods (15.1 per cent), auto (6.2 per cent), public sector undertakings (1.9 per cent), metals (1.3 per cent) and healthcare (1.0 per cent). However, fast moving consumer goods registered losses of 10.7 per cent (Chart 49).

Chart 49: Trends in BSE Sectoral Stock Indices

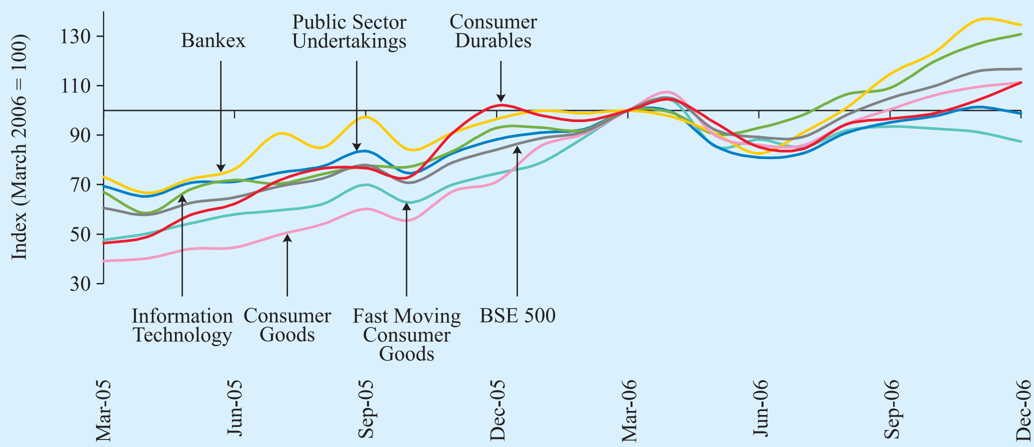


Table 42: Stock Market Indicators

Indicator	BSE				NSE			
	April-March		April-December		April-March		April-December	
	2004-05	2005-06	2005-06	2006-07	2004-05	2005-06	2005-06	2006-07
1	2	3	4	5	6	7	8	9
BSE Sensex / S&P CNX Nifty								
End-period	6493	11280	9398	13787	2036	3403	2837	3966
Average	5741	8279	7668	11845	1805	2513	2339	3454
Volatility	11.2	16.7	12.2	10.4	11.3	15.6	11.3	9.7
P/E Ratio (end-period)*	15.61	20.92	18.61	22.76	14.60	20.26	17.16	21.26
Turnover (Rupees crore)	5,18,716	8,16,074	5,47,922	7,01,710	11,40,071	15,69,556	10,75,345	14,22,014
Market Capitalisation (Rupees crore) (end-period)	16,98,429	30,22,191	24,89,386	36,24,357	15,85,585	28,13,201	23,22,392	34,26,236

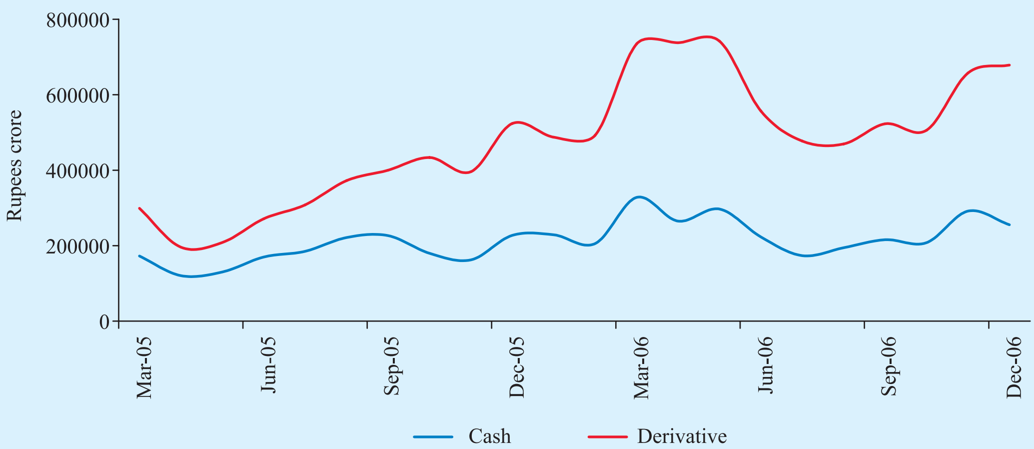
* : For 30 scrips included in the BSE Sensex and 50 scrips included in the S&P CNX Nifty.

Source : The Stock Exchange, Mumbai (BSE) and National Stock Exchange of India Ltd. (NSE).

The price-earnings (P/E) ratio for the 30 scrips included in the BSE Sensex increased from 20.9 at end-March 2006 to 22.8 at end-December 2006 (Table 42). The market capitalisation of the BSE increased by 19.9 per cent between end-March 2006 and end-December 2006. Volatility during April-December 2006 was lower than that in the same period a year ago.

Total turnover (BSE and NSE) in the cash segment during April-December 2006 at Rs.21,23,724 crore was 30.8 per cent higher than that in the corresponding period of 2005 (Chart 50). Total turnover (BSE and NSE) in the derivative segment increased by 72.0 per cent during April-December 2006 to Rs.53,49,595 crore.

Chart 50: Turnover in Cash and Derivative Segment - BSE and NSE



VI. THE EXTERNAL ECONOMY

India's external sector has continued to register robust performance during 2006-07 so far. Merchandise exports have exhibited strong growth, notwithstanding some deceleration. Non-oil imports recorded a deceleration mainly on account of decline in imports of gold and silver, and pearls, precious and semi-precious stones; imports of capital goods, however, remained buoyant. Growth in oil imports remained high, *albeit* lower than last year. Sustained growth in exports of services and remittances continued to provide buoyancy to the surplus in the invisibles account, which enabled financing a large part of the deficit on the merchandise trade account. Although, the current account deficit widened in the wake of higher oil imports, it was easily financed by normal capital flows. Foreign exchange reserves have increased by US $ 26.5 billion during 2006-07 (up to January 19, 2007).

International Developments

The global economy continued to expand at a robust pace in the third quarter of 2006, *albeit* with some moderation in the growth momentum (Table 43). Real GDP growth in the US slowed further in the third quarter, primarily on the back of drop in residential investment, acceleration in imports and deceleration in consumer spending for services. The Japanese economy also witnessed a deceleration in growth in the third quarter, attributable to a fall in domestic demand. Economic activity in the euro area, on the other hand,

Table 43: Growth Rates – Global Scenario

(Per cent)

Country	2004	2005	2006 P	2007 P	2005		2006		
					Q3	Q4	Q1	Q2	Q3
1	2	3	4	5	6	7	8	9	10
Advanced Economies									
Euro Area	2.1	1.3	2.4	2.0	1.6	1.8	2.2	2.7	2.7
Japan	2.3	2.6	2.7	2.1	2.6	2.8	3.6	2.5	1.6
Korea	4.7	4.0	5.0	4.3	4.5	5.3	6.1	5.3	4.8
UK	3.3	1.9	2.7	2.7	1.9	1.8	2.2	2.6	2.9
US	3.9	3.2	3.4	2.9	3.4	3.1	3.7	3.5	3.0
OECD Countries	3.3	2.8	3.1	2.9	2.8	3.0	3.3	3.4	3.0
Emerging Economies									
Argentina	9.0	9.2	8.0	6.0	9.2	9.1	8.6	7.9	8.7
Brazil	4.9	2.3	3.6	4.0	1.0	1.4	3.4	1.2	3.2
China	10.1	10.2	10.0	10.0	9.4	9.9	10.2	11.3	10.6
India	7.5*	8.4#	8.3	7.3	8.4	7.5	9.3	8.9	9.2
Indonesia	5.1	5.6	5.2	6.0	5.6	4.9	4.7	5.2	5.5
Malaysia	7.2	5.2	5.5	5.8	5.3	5.2	5.3	5.9	5.9
Thailand	6.2	4.5	4.5	5.0	5.5	4.3	6.1	5.0	4.7

* : FY 2004-05. # : FY 2005-06. P : IMF Projections.

Source : International Monetary Fund; The Economist; and the OECD.

continued to expand, led by strong domestic demand. Amongst emerging economies, economic activity in China continued to exhibit double-digit growth in the third quarter of 2006, though with some moderation from the pace recorded in the first half of 2006.

According to the International Monetary Fund (IMF), global economic activity will remain buoyant in 2007, led by emerging economies. In terms of exchange rates based on purchasing power parities, global economy will expand by 4.9 per cent in 2007, marginally lower than that of 5.1 per cent in 2006 (Table 44). Growth prospects, however, remain subject to downside risks from uncertainties regarding the persistent global macroeconomic imbalances, the underlying inflationary pressures on account of limited spare capacity, emerging wage pressures, possibility of renewed rise in crude oil prices and possibility of re-pricing of risks in global financial markets.

Global trade exhibited a modest deceleration during 2006, mainly on account of slowdown in developing countries (Table 45). World exports in US dollar terms grew by 14.1 per cent in the first nine months of 2006 as compared

Table 44: Select Economic Indicators - World

Item	2001	2002	2003	2004	2005	2006 P	2007 P
1	2	3	4	5	6	7	8
I. World Output (Per cent change) #	2.6 (1.5)	3.1 (1.8)	4.1 (2.7)	5.3 (3.9)	4.9 (3.4)	5.1 (3.8)	4.9 (3.5)
i) Advanced economies	1.2	1.5	1.9	3.2	2.6	3.1	2.7
ii) Other emerging market and developing countries	4.4	5.1	6.7	7.7	7.4	7.3	7.2
of which: Developing Asia	6.1	7.0	8.4	8.8	9.0	8.7	8.6
II. Consumer Price Inflation (Per cent)							
i) Advanced economies	2.1	1.5	1.8	2.0	2.3	2.6	2.3
ii) Other emerging market and developing countries	6.5	5.7	5.8	5.6	5.3	5.2	5.0
of which: Developing Asia	2.7	2.0	2.5	4.1	3.5	3.8	3.6
III. Net Capital Flows* (US $ billion)							
i) Net private capital flows (a+b+c)	64.6	77.3	165.6	205.9	238.5	211.4	182.2
a) Net private direct investment	179.4	150.6	159.1	176.9	255.9	263.3	246.1
b) Net private portfolio investment	-78.2	-91.7	-10.9	13.9	3.2	-31.1	-4.6
c) Net other private capital flows	-36.6	18.4	17.3	15.1	-20.6	-20.8	-59.2
ii) Net official flows	-3.3	-4.3	-53.1	-64.7	-151.8	-238.7	-174.1
IV. World Trade (Per cent change)@							
i) Volume	–	3.4	5.3	10.6	7.4	8.9	7.6
ii) Price Deflator (in US dollars)	-3.2	1.2	10.5	9.7	5.4	4.6	2.2
V. Current Account Balance (Per cent to GDP)							
i) US	-3.8	-4.5	-4.8	-5.7	-6.4	-6.6	-6.9
ii) China	1.3	2.4	2.8	3.6	7.2	7.2	7.2
iii) Middle East	6.2	4.6	8.3	11.9	18.5	23.2	22.5

P : IMF Projections.
: Growth rates are based on exchange rates at purchasing power parities. Figures in parentheses are growth rates at market exchange rates.
* : Net capital flows to emerging market and developing countries.
@ : Average of annual percentage change for world exports and imports of goods and services.
Source : World Economic Outlook, IMF, September 2006.

Table 45: Growth in Exports - Global Scenario

(Per cent)

Region/Country	2005	2005	2006
		January-October	
1	2	3	4
World	**13.9**	**15.5** *	**14.1** *
Industrial Countries	**8.4**	**10.3** *	**11.2** *
USA	10.8	10.1	14.8
France	3.5	6.8	8.2
Germany	7.3	9.3	12.8
Japan	5.2	5.8	8.0
Developing Countries	**21.8**	**23.0** *	**17.9** *
Non-Oil Developing Countries	**19.2**	**20.6** *	**19.4** *
China	28.4	31.3 *	26.5 *
India	29.8	30.2 #	21.7 #
Indonesia	18.2	20.4	20.5
Korea	12.0	11.6 $	14.0 $
Malaysia	12.0	11.1	13.2
Singapore	15.6	27.3 #	19.9 #
Thailand	14.5	15.5	18.2

* : January-September. # : January-November. $: January-August.

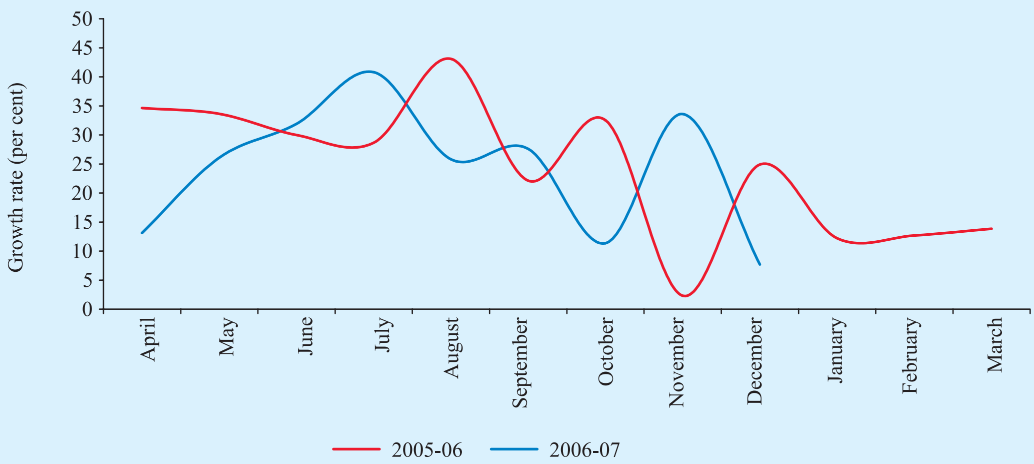
Source : International Financial Statistics, International Monetary Fund, January 2007; DGCI&S for India.

with 15.5 per cent in the corresponding period of 2005. Exports of industrial countries, on the other hand, accelerated, led by the US.

Merchandise Trade

According to the provisional data released by the Directorate General of Commercial Intelligence and Statistics (DGCI&S), India's exports recorded a growth of 22 per cent during April-December 2006 as compared with 30 per cent registered a year ago (Chart 51).

Chart 51: India's Merchandise Exports



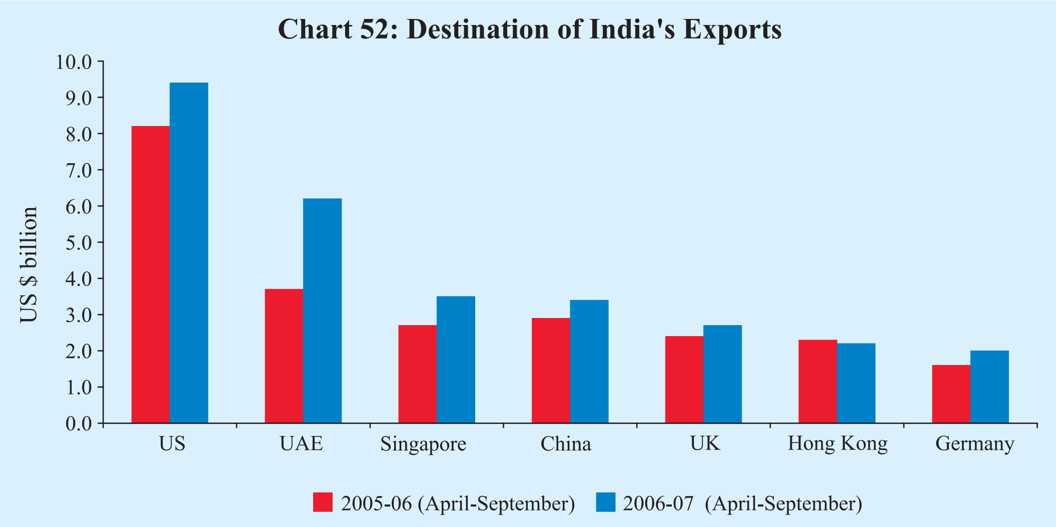
Commodity-wise data available for April-September 2006 reveal that exports of all major groups, with the exception of petroleum products and engineering goods, recorded deceleration (Table 46). Exports of petroleum products registered substantial growth reflecting the increase in both price and quantity. In volume terms, exports of petroleum products increased by 60 per cent during April-September 2006. The deceleration in primary products was mainly due to decline in exports of iron ore. However, exports of agriculture and allied products maintained the growth momentum on the back of large increase in exports of raw cotton and sugar. Among the traditional agricultural products, exports of tea, coffee, tobacco, spices and oil meals recorded a strong growth, while that of rice, wheat, cashew and marine products posted a decline/ low growth. Within manufactured products, exports of engineering goods, basic chemicals and pharmaceuticals maintained their growth momentum. On the other hand, exports of gems and jewellery and handicrafts recorded a decline while those of 'leather and manufactures' and textiles exhibited a deceleration.

Destination-wise, the US was the largest export market for India during April-September 2006 with a share of 15.3 per cent in India's total exports followed by the UAE (10.1 per cent) and Singapore (5.8 per cent) (Chart 52). Amongst major markets, India's exports to the Organisation of Petroleum Exporting Countries (OPEC) recorded a growth of 56 per cent with exports to the UAE growing by 65 per cent. Exports to the US, Singapore, Germany, UK and China recorded a deceleration, while exports to Hong Kong declined.

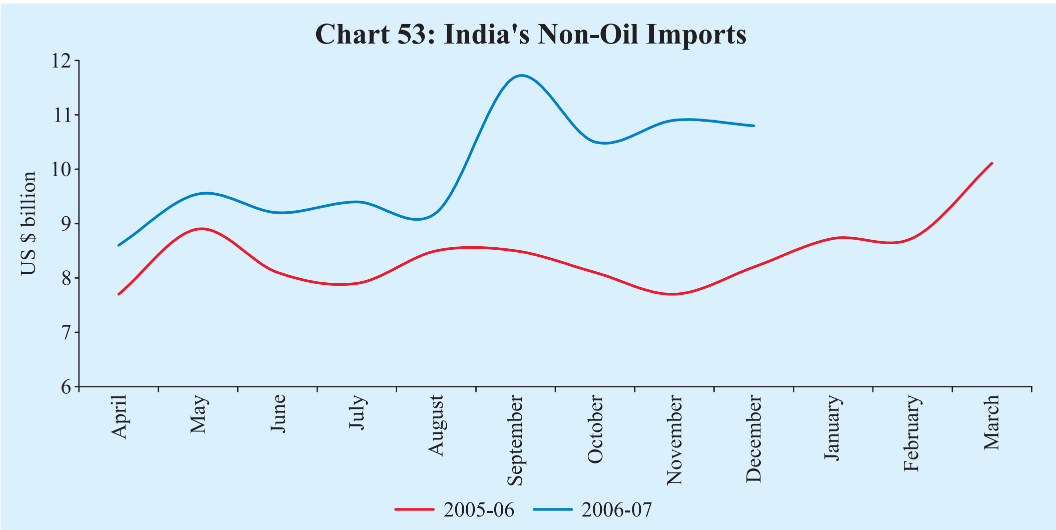
Table 46: Exports of Principal Commodities

Commodity Group	US $ billion			Variation (per cent)		
	2005-06	2005-06	2006-07	2005-06	2005-06	2006-07
		April-September			April-September	
1	2	3	4	5	6	7
1. Primary Products	**16.4**	**7.2**	**8.5**	**20.8**	**38.3**	**18.1**
of which:						
a) Agriculture and Allied Products	10.2	4.5	5.6	20.5	24.1	23.9
b) Ores and Minerals	6.2	2.7	2.9	21.4	71.1	8.2
2. Manufactured Goods	**72.2**	**34.6**	**41.0**	**18.9**	**28.8**	**18.6**
of which:						
a) Chemicals and Related Products	14.8	6.8	8.2	18.6	30.1	21.2
b) Engineering Goods	21.5	10.2	14.3	23.7	38.6	40.5
c) Textiles and Textile Products	16.3	7.7	8.5	20.6	21.1	10.4
d) Gems and Jewellery	15.5	7.8	7.8	12.8	26.4	-0.7
3. Petroleum Products	**11.5**	**4.9**	**9.8**	**64.9**	**67.2**	**100.4**
4. Total Exports	**103.1**	**48.0**	**61.2**	**23.4**	**33.4**	**27.5**
Memo:						
Non-oil Exports	91.6	43.1	51.4	19.6	30.5	19.2

Source : DGCI&S.



Growth in India's merchandise imports decelerated during April-December 2006 to 25 per cent from 38 per cent a year ago. Imports of petroleum, oil and lubricants (POL) increased by 39 per cent during April-December 2006, reflecting both higher prices and volumes. In volume terms, oil imports increased by 18 per cent during April-September 2006 as against a decline of 0.4 per cent a year ago. Non-oil imports, after remaining subdued in the beginning of current fiscal year, have picked up since September 2006 (Chart 53). Nonetheless, the overall growth in non-oil imports at 19 per cent during April-December 2006 was substantially lower than that of 34 per cent



recorded during the corresponding period of the previous year, mainly reflecting the decline in the imports of gold and silver, and pearls, precious and semi-precious stones (Table 47). Imports of capital goods remained buoyant, posting a growth of 39 per cent during April-September 2006 on top of 48 per cent in the corresponding period of 2005 in consonance with strong investment activity in the economy.

Country-wise, China was the largest source for India's imports during April-September 2006 with a share of 9.2 per cent in India's total imports, followed by Saudi Arabia (8.2 per cent), the US (5.8 per cent) and the UAE (5.1 per cent). Region-wise, developing countries (including OPEC) accounted for 66 per cent of India's imports; OPEC countries alone accounted for 33 per cent of India's total imports during April-September 2006.

The trade deficit widened to US $ 41.6 billion during April-December 2006 from US $ 31.7 billion a year ago (Table 48). The trade deficit on the oil account increased by US $ 3.7 billion during April-September 2006, while the non-oil trade deficit declined by US $ 0.3 billion.

Table 47: Imports of Principal Commodities

Commodity Group	US $ billion			Variation (per cent)		
	2005-06	2005-06	2006-07	2005-06	2005-06	2006-07
		April-September			April-September	
1	2	3	4	5	6	7
POL	44.0	21.0	29.5	47.3	43.7	41.0
Edible Oils	2.0	1.2	1.0	-17.9	-3.6	-11.8
Fertilisers	2.1	1.0	1.5	54.5	88.4	43.9
Iron and Steel	4.6	2.5	2.9	71.3	123.0	16.8
Capital Goods	37.7	14.2	19.7	49.9	47.8	38.8
Pearls, Precious and Semi-Precious Stones	9.1	5.4	3.6	-3.1	37.5	-32.8
Chemicals	7.0	3.5	3.9	22.5	48.9	9.1
Gold and Silver	11.3	7.0	6.7	1.5	58.5	-3.6
Total Imports	**149.2**	**70.8**	**87.3**	**33.8**	**47.0**	**23.4**
Memo:						
Non-oil Imports	105.2	49.8	57.8	28.8	48.5	16.1
Non-oil Imports excluding Gold and Silver	93.9	42.8	51.1	33.1	47.0	19.2
Mainly Industrial Imports*	87.5	39.5	47.3	34.7	48.2	19.7

* : Non-oil imports net of gold and silver, bulk consumption goods, manufactured fertilisers and professional instruments.

Source : DGCI&S.

Table 48: India's Merchandise Trade

(US $ billion)

Item	2004-05	2005-06	2005-06 April-December	2006-07 April-December
1	2	3	4	5
Exports	83.5	103.1	73.4	89.5
Imports	111.5	149.2	105.1	131.2
Oil	29.8	44.0	31.5	43.8
Non-oil	81.7	105.2	73.6	87.4
Trade Balance	-27.9	-46.1	-31.7	-41.6
Non-oil Trade Balance	-5.1	-13.6	-6.7*	-6.3*
				Variation (per cent)
Exports	30.8	23.4	29.9	22.0
Imports	42.7	33.8	37.8	24.8
Oil	45.1	47.3	46.9	39.2
Non-oil	41.8	28.8	34.3	18.7

* : April-September.
Source : DGCI&S.

Current Account

Earnings from exports of services and inflows under remittances remained buoyant during the second quarter (July-September) of 2006-07. Amongst major services, net surplus under software services amounted to US $ 6.1 billion during the quarter ended September 2006, an increase of 23 per cent from a year ago (Table 49). Private transfers at US $ 5.5 billion during

Table 49: Invisibles Account (Net)

(US $ million)

Item	2005-06 PR	2005-06 PR			2006-07		
	April-March	April-June	July-Sept.	April-Sept.	April-June PR	July-Sept. P	April-Sept. P
1	2	3	4	5	6	7	8
Services	23,881	5,647	6,079	11,726	7,744	6,554	14,298
Travel	1,389	87	185	272	257	-17	240
Transportation	-1550	-396	-286	-682	-164	219	55
Insurance	22	-14	240	226	111	162	273
Government, not included elsewhere	-197	-26	-63	-89	-24	-62	-86
Software	22,262	4,853	4,989	9,842	5,947	6,138	12,085
Other Services	1,955	1,143	1,014	2,157	1,617	114	1,731
Transfers	24,284	5,511	4,990	10,501	5,690	5,521	11,211
Investment Income	-4,921	-670	-1365	-2,035	-865	-921	-1,786
Compensation of Employees	-589	-121	-122	-243	-116	-149	-265
Total	**42,655**	**10,367**	**9,582**	**19,949**	**12,453**	**11,005**	**23,458**

PR : Partially Revised. P : Preliminary.

July-September 2006 were nine per cent higher than a year ago. Investment income deficit narrowed from a year ago, on account of higher earnings on India's external assets. On balance, the net surplus under invisibles (services, transfers and income taken together) increased from US $ 9.6 billion during July-September 2005 to US $ 11.0 billion during July-September 2006. The cumulative surplus increased to US $ 23.5 billion during the first half of 2006-07 from US $ 19.9 billion a year ago.

The net invisible surplus financed 61 per cent of the merchandise trade deficit during July-September 2006. However, in view of the large expansion in the merchandise trade deficit, the current account deficit widened to US $ 6.9 billion from US $ 3.6 billion a year ago. The current account deficit during the first half of 2006-07 (April-September 2006) at US $ 11.7 billion was also higher than that of US $ 7.2 billion a year ago (Table 50 and Chart 54).

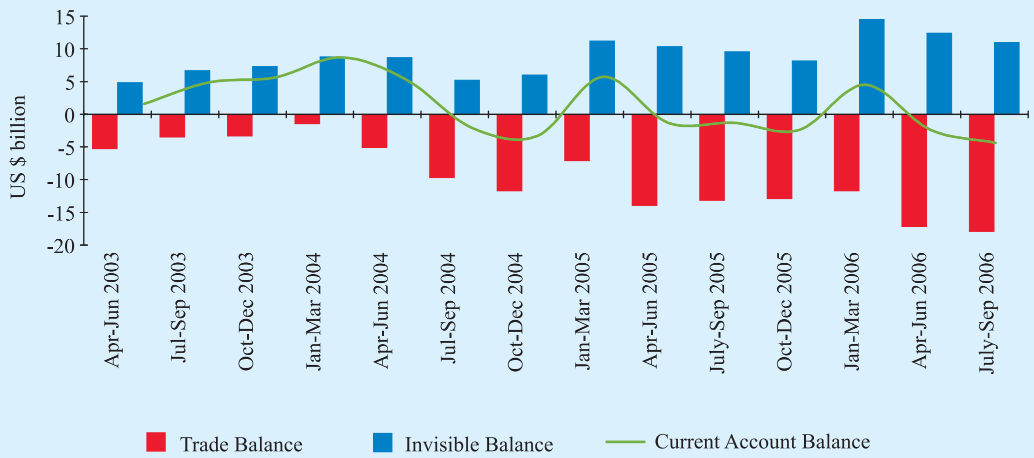
Table 50: India's Balance of Payments

(US $ million)

Item	2005-06 PR	2005-06 PR			2006-07		
	April-March	April-June	July-Sept.	April-Sept.	April-June PR	July-Sept. P	April-Sept. P
1	2	3	4	5	6	7	8
Exports	1,05,152	23,998	25,257	49,255	29,674	30,876	60,550
Imports	1,56,993	37,947	38,417	76,364	46,882	48,809	95,691
Trade Balance	-51,841 (-6.5)	-13,949	-13,160	-27,109	-17,208	-17,933	-35,141
Invisible Receipts	92,294	19,926	19,678	39,604	24,809	26,126	50,935
Invisible Payments	49,639	9,559	10,096	19,655	12,356	15,121	27,477
Invisibles, net	42,655 (5.3)	10,367	9,582	19,949	12,453	11,005	23,458
Current Account	-9,186 (-1.2)	-3,582	-3,578	-7,160	-4,755	-6,928	-11,683
Capital Account (net)*	24,238 [29,738]@	4,829	8,834	13,663	11,133	9,196	20,329
of which:							
Foreign Direct Investment	4,730	1,203	926	2,129	1,689	2,529	4,218
Portfolio Investment	12,494	972	4,441	5,413	-527	2,141	1,614
External Commercial Borrowings $	2,723 [8,223]@	1,116	1,809	2,925	3,838	1,255	5,093
Short-term Trade Credit	1,708	-151	1,123	972	417	1,521	1,938
External Assistance	1,682	212	197	409	48	310	358
NRI Deposits	2,789	-108	341	233	1,231	798	2,029
Change in Reserves #	-15,052	-1,247	-5,256	-6,503	-6,378	-2,268	-8,646

PR : Partially Revised. P : Preliminary.
* : Includes errors and omissions.
$: Medium and long-term borrowings.
: On a balance of payments basis (excluding valuation); (-) indicates increase.
@ : Excluding the IMD redemption.
Note : Figures in parentheses are per cent to GDP.

Chart 54: Current Account Balance



Capital Flows

Capital flows, both debt and non-debt, during 2006-07 so far have been higher than a year ago, reflecting growing investor interest in the Indian economy on the back of strong growth prospects and buoyant investment demand. Within non-debt flows, foreign direct investment (FDI) inflows at US $ 8.6 billion during April-November 2006 were almost twice the inflows in the corresponding period of the previous year (Table 51). FDI was channelled mainly into financial services, manufacturing, banking services, information technology services and construction. Mauritius, the US and Singapore remain the dominant sources of FDI to India. As regards portfolio equity flows, foreign institutional investors (FIIs) made large purchases in the Indian stock market during August-November

Table 51: Capital Flows

(US $ million)

Components	Period	2005-06	2006-07
1	2	3	4
Foreign Direct Investment into India	April-November	4,461	8,552
FIIs (net)	April-January *	5,790	2,491
ADRs/GDRs	April-November	1,715	1,850
External Assistance (net)	April-September	409	358
External Commercial Borrowings (net) (Medium and long-term)	April-September	2,925	5,093
Short-term Trade Credits (net)	April-September	972	1,938
NRI Deposits (net)	April-November	476	2,715

* : Up to January 12.

Note : Data on FIIs presented in this table represent inflows into the country. They may differ from data relating to net investment in stock exchanges by FIIs.

2006, more than offsetting the outflows witnessed during May-July 2006. During December 2006, however, FIIs registered outflows against the backdrop of volatility in Asian equity markets subsequent to the tightening of capital controls by Thailand. On the whole, net FII inflows during 2006-07 so far (up to January 12, 2007) amounted to US $ 2.5 billion. Resources mobilised through the issuances of American depository receipts (ADRs)/global depository receipts (GDRs) abroad were also higher during April-November 2006.

Amongst debt flows, demand for external commercial borrowings (ECBs) continued to remain strong in consonance with buoyant domestic investment activity. Net inflows under various NRI deposits during April-November 2006 were substantially higher than a year ago, partly attributable to higher interest rates on various deposit schemes. The ceiling interest rate on NRE deposits was raised by 25 basis points each in November 2005 and April 2006 to "LIBOR/SWAP rates of US dollar plus 100 basis points". The ceiling interest rate on FCNR(B) deposits was also raised by 25 basis points to "LIBOR/SWAP rates for the respective currency/ maturity" in March 2006 from "LIBOR/ SWAP rates *minus* 25 basis points".

Foreign Exchange Reserves

India's foreign exchange reserves have increased by US $ 26.5 billion during 2006-07 so far (up to January 19, 2007) to US $ 178.1 billion, mainly due to an increase in foreign currency assets (Table 52). India holds the fifth largest stock of reserves among the emerging market economies. The overall approach to the

Table 52: Foreign Exchange Reserves

(US $ million)

Period	Gold	SDR	Foreign Currency Assets	Reserve Position in the IMF	Total (2+3+4+5)
1	2	3	4	5	6
March 1995	4,370	7	20,809	331	25,517
March 2000	2,974	4	35,058	658	38,694
March 2005	4,500	5	135,571	1,438	141,514
March 2006	5,755	3	145,108	756	151,622
April 2006	6,301	6	153,598	772	160,677
May 2006	7,010	–	156,073	785	163,868
June 2006	6,180	–	155,968	764	162,912
July 2006	6,557	7	157,247	766	164,577
August 2006	6,538	1	158,938	767	166,244
September 2006	6,202	1	158,340	762	165,305
October 2006	6,068	7	160,669	648	167,392
November 2006	6,494	1	167,598	548	174,641
December 2006	6,517	1	170,817	546	177,251
January 2007 *	6,517	1	171,068	542	178,128

– : Negligible.
* : As on January 19, 2007.

management of India's foreign exchange reserves in recent years reflects the changing composition of the balance of payments and the 'liquidity risks' associated with different types of flows and other requirements. Taking these factors into account, India's foreign exchange reserves continued to be at a comfortable level and consistent with the rate of growth, the share of external sector in the economy and the size of risk-adjusted capital flows.

External Debt

India's total external debt was placed at US $ 136.5 billion at end-September 2006, an increase of US $ 4.3 billion over end-June 2006. The increase during the quarter was mainly on account of higher external commercial borrowings, NRI deposits and short-term trade credits. Higher commercial borrowings and short-term credits could be attributed to increased investment and import demand, while the rise in NRI deposits was, *inter alia*, on account of the upward revision in interest rates on these deposits. Sustainability indicators such as the ratio of short-term to total debt and short-term debt to reserves recorded a modest rise during the quarter but are still placed at quite low and comfortable levels (Table 53). Foreign exchange reserves remain in excess of the stock of external debt.

Table 53: India's External Debt

(US $ million)

Indicator	End-March 1995	End-March 2005	End-March 2006	End-June 2006	End-Sept 2006
1	2	3	4	5	6
1. Multilateral	28,542	31,702	32,559	33,101	33,594
2. Bilateral	20,270	16,930	15,727	15,834	15,734
3. International Monetary Fund	4,300	0	0	0	0
4. Trade Credit	6,629	4,980	5,395	5,498	5,663
5. External Commercial Borrowings	12,991	27,024	26,849	31,099	32,462
6. NRI Deposit	12,383	32,743	35,134	35,651	36,563
7. Rupee Debt	9,624	2,301	2,031	1,915	1,921
8. Long-term (1 to 7)	94,739	1,15,680	1,17,695	1,23,098	1,25,937
9. Short-term	4,269	7,524	8,696	9,105	10,579
Total (8+9)	**99,008**	**1,23,204**	**1,26,391**	**1,32,203**	**1,36,516**
Memo:					(Per cent)
Total debt/GDP	30.8	17.3	15.8	..	..
Short-term/Total debt	4.3	6.1	6.9	6.9	7.7
Short-term debt/Reserves	16.9	5.3	5.7	5.6	6.4
Concessional debt/Total debt	45.3	33.0	31.2	30.1	29.3
Reserves/Total debt	25.4	114.9	120.0	123.2	121.1
Debt Service Ratio*	25.9	6.1	10.2	..	..

* : Relates to the fiscal year.
.. : Not Available.