Macroeconomic and Monetary Developments in 2006-07

Reserve Bank of India
Mumbai

Contents

I. THE REAL ECONOMY

The Indian economy witnessed robust growth during 2006-07 for the fourth year in succession. According to the advance estimates released by the Central Statistical Organisation (CSO), real Gross Domestic Product (GDP) growth is expected to accelerate from 9.0 per cent in 2005-06 to 9.2 per cent in 2006-07. Real GDP growth is, thus, expected to average 8.6 per cent during the four year period from 2003-04 to 2006-07. The acceleration in growth during 2006-07 was driven by the continued momentum in the services and manufacturing sectors, both of which are expected to record double-digit growth. 'Agriculture and allied activities' growth, however, slowed down from 6.0 per cent in 2005-06 to 2.7 per cent in 2006-07 (Table 1 and Chart 1).

Table 1: Growth Rates of Real GDP

(Per cent)

Sector	2000-01 to 2006-07 (Average)	2004-05	2005-06*	2006-07#	2005-06	2006-07	2005-06			2006-07		
					April-December		Q1	Q2	Q3	Q1	Q2	Q3
1	2	3	4	5	6	7	8	9	10	11	12	13
1. Agriculture and Allied Activities	**2.5 (21.4)**	**0.0 (20.2)**	**6.0 (19.7)**	**2.7 (18.5)**	**6.0**	**2.2**	**4.0**	**4.0**	**8.7**	**3.4**	**1.7**	**1.5**
2. Industry	**7.6 (19.6)**	**8.4 (19.6)**	**8.0 (19.4)**	**10.2 (19.6)**	**7.8**	**10.1**	**9.8**	**6.6**	**7.2**	**9.7**	**10.5**	**10.0**
2.1 Mining and Quarrying	4.5	7.5	3.6	4.5	3.0	4.1	6.0	0.1	2.7	3.4	3.1	5.7
2.2 Manufacturing	7.5	8.7	9.1	11.3	9.0	11.3	10.7	8.1	8.2	11.3	11.9	10.7
2.3 Electricity, Gas and Water Supply	4.5	7.5	5.3	7.7	5.0	7.5	7.4	2.6	5.0	5.4	7.7	9.3
3. Services	**8.6 (59.0)**	**10.0 (60.2)**	**10.3 (60.9)**	**11.0 (61.9)**	**9.8**	**10.8**	**9.5**	**9.5**	**10.3**	**10.4**	**10.7**	**11.1**
3.1 Trade, Hotels, Restaurants, Transport, Storage and Communication	10.3	10.9	10.4	13.0	9.9	13.3	10.2	9.5	10.0	13.1	13.8	13.0
3.2 Financing, Insurance, Real Estate and Business Services	8.0	8.7	10.9	11.1	9.8	10.1	8.9	10.6	9.8	9.0	9.5	11.6
3.3 Community, Social and Personal Services	6.0	7.9	7.7	7.8	7.9	7.2	7.5	7.9	8.3	7.4	6.9	7.5
3.4 Construction	9.7	14.1	14.2	9.4	13.6	9.7	12.7	11.3	16.6	9.5	9.8	9.9
4. Real GDP at Factor Cost	**6.9**	**7.5**	**9.0**	**9.2**	**8.6**	**8.9**	**8.4**	**8.0**	**9.3**	**8.9**	**9.2**	**8.6**

Memo: (Amount in Rupees crore)

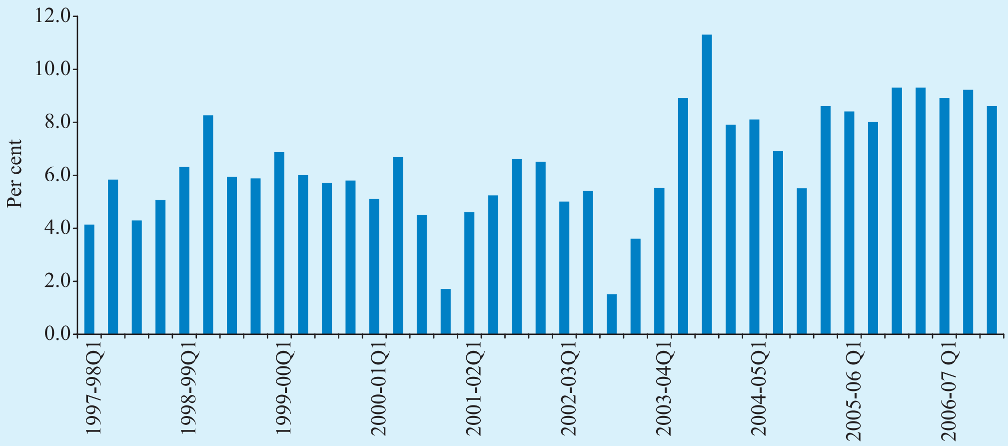
	2004-05	2005-06*	2006-07#
a) Real GDP at factor cost (1999-2000 prices)	23,89,660	26,04,532	28,44,022
b) GDP at current market prices	31,26,596	35,67,177	41,00,636

* : Quick Estimates. # : Advance Estimates.

Note : Figures in parentheses denote share in real GDP.

Source : Central Statistical Organisation.

Chart 1: Real GDP: Growth Rate



Agricultural Situation

The rainfall during the 2006 South-West monsoon season (June 1 to September 30) was close to normal, although the distribution was uneven. Excess rainfall during the first three weeks of August 2006 largely offset the deficiency in the rainfall from the second week of June to July 2006 and again in mid-September 2006. This resulted in a comfortable reservoir position at the end of the South-West monsoon season, with the total live water storage at 91 per cent of the Full Reservoir Level (FRL) (higher than that of 81 per cent in 2005 and the average of 71 per cent in the last 10 years), which augured well for the ensuing *rabi* crops. 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 during the North-East monsoon was deficient/scanty/no rain in 27 sub-divisions (19 sub-divisions during last year) (Table 2). As on March 29, 2007, the total live water storage was 39 per cent (37 per cent last year) of the FRL.

The uneven and delayed rainfall during the South-West monsoon season led to a reduction of 1.9 per cent in the area coverage under *kharif* crops in 2006 season, mainly in respect of rice, coarse cereals and oilseeds. On the other hand, favourable soil moisture conditions along with remunerative open market and support prices led to an increase of 2.1 per cent in the area sown under *rabi* crops (up to March 30, 2007); increase in the area covered under wheat, pulses and coarse cereals more than offset some decline in the area under oilseeds and rice (Table 3).

According to the Third Advance Estimates, production of foodgrains during 2006-07 is likely to be 211.8 million tonnes, an increase of 1.5 per cent over the previous year. Shortfall in the case of rice and coarse cereals would be offset by

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.

higher production of wheat and pulses. Among the non-foodgrains, sugarcane and cotton are expected to scale new peaks during 2006-07; the production of oilseeds is, however, expected to be lower on account of decline in acreage (Table 4).

Food Management

The procurement of foodgrains (rice and wheat) during 2006-07, at 35.9 million tonnes (mt), was 12.7 per cent lower than that in the preceding year mainly

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

(Million hectares)

Crop	Normal Area	Area Coverage 2005	Area Coverage 2006	Area Coverage Variation
1	2	3	4	5
***Kharif* Crops**				
Rice	38.2	37.4	37.2	-0.2
Coarse Cereals	22.9	22.8	21.1	-1.6
Of which:				
Bajra	9.4	9.4	8.1	-1.3
Jowar	4.4	3.9	3.7	-0.2
Maize	6.2	6.9	7.3	0.4
Total Pulses	10.9	11.4	11.5	0.1
Total *Kharif* Oilseeds	15.4	17.7	16.9	-0.8
Of which:				
Groundnut	5.5	5.6	4.8	-0.9
Soyabean	6.6	7.8	8.1	0.3
Sesamum	1.5	1.9	1.8	-0.1
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**

Crop	Normal Area	Area Coverage 2005	Area Coverage 2006	Area Coverage Variation
1	2	3	4	5
***Rabi* Crops (up to March 30, 2007)**				
Rice	4.9	4.3	4.1	-0.2
Wheat	26.1	26.7	28.5	1.8
Coarse Cereals	6.4	6.3	6.7	0.4
Of which:				
Jowar	5.0	4.9	4.8	-0.1
Maize	0.7	0.7	1.0	0.3
Total Pulses	11.0	13.8	14.2	0.5
Total Rabi Oilseeds	8.2	11.5	10.3	-1.2
Of which:				
Groundnut	0.8	1.2	1.1	-0.1
Rapeseed & Mustard	5.4	7.4	6.6	-0.7
Sunflower	1.1	1.5	1.3	-0.2
All Crops	**56.5**	**62.6**	**63.9**	**1.3**

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	91.8	92.8	91.1
Kharif	63.1	78.6	72.2	78.3	80.8	78.5
Rabi	8.7	9.9	10.9	13.5	12.0	12.5
Wheat	65.8	72.2	68.6	69.4	75.5	73.7
Coarse Cereals	26.1	37.6	33.5	34.1	36.5	32.9
Kharif	20.0	32.2	26.4	26.7	28.7	25.0
Rabi	6.1	5.4	7.1	7.3	7.8	7.9
Pulses	11.1	14.9	13.1	13.4	15.2	14.1
Kharif	4.2	6.2	4.7	4.9	5.8	4.8
Rabi	7.0	8.7	8.4	8.5	9.4	9.3
Total Foodgrains	**174.8**	**213.2**	**198.4**	**208.6**	**220.0**	**211.8**
Kharif	87.2	117.0	103.3	109.9	115.3	108.4
Rabi	87.6	96.2	95.1	98.7	104.8	103.4
Total Oilseeds	**14.8**	**25.2**	**24.4**	**28.0**	**29.4**	**23.3**
Kharif	9.0	16.7	14.1	16.8	18.1	13.9
Rabi	5.9	8.5	10.2	11.2	11.3	9.4
Sugarcane	287.4	233.9	237.1	281.2	270.0	322.9
Cotton #	8.6	13.7	16.4	18.5	18.5	21.0
Jute and Mesta ##	11.3	11.2	10.3	10.8	11.3	11.3

T : Target. A : Achievement.
$: Third Advance Estimates as on April 4, 2007.
: Million bales of 170 kgs each.
: Million bales of 180 kgs each.
Source : Ministry of Agriculture, Government of India.

on account of decline in the procurement of wheat from 14.8 mt to 9.2 mt (Table 5). The offtake of rice and wheat during 2006-07 (April 1, 2006 to January 31, 2007) at 30.4 mt was also lower by 12.7 per cent over the corresponding period of the previous year, mainly due to a fall in the offtake of wheat under the Targeted Public Distribution System (TPDS) and 'Other Welfare Schemes' (OWS). As a result of lower procurement, the total stock of foodgrains with the Food Corporation of India (FCI) and other Government agencies declined to 18.1 mt as on February 1, 2007 from 19.5 mt a year ago and was lower than the buffer stock norms (20.0 mt as on January 1, 2007). While the stocks of wheat were lower than the norm (8.2 mt), those of rice were higher than the buffer stock norm (11.8 mt).

Industrial Performance

Industrial production continued its growth momentum during April-February 2006-07, with growth accelerating to 11.1 per cent from 8.1 per cent a year ago (Chart 2 and Table 6). Growth during April-February 2006-07 was the highest since 1995-96. The manufacturing sector grew by 12.1 per cent during April-February 2006-07. It remained the key driver of industrial growth,

Table 5: Management of Food Stocks

(Million tonnes)

Month	Opening Stock of Foodgrains			Procurement of Foodgrains			Foodgrains Off-take					Closing Stock	Norms
	Rice	Wheat	Total	Rice	Wheat	Total	PDS	OWS	OMS - Domestic	Exports	Total		
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@				26.4	14.8	41.1	25.9	8.3	0.6	0.0	34.8	19.5	
2006-07@				26.7	9.2	35.9	26.2	4.1	0.0	0.0	30.4	18.1	
2006													
January	12.6	6.2	19.3	4.0	0.0	4.0	2.7	0.8	0.1	0.0	3.6	19.5	20.0
February	14.0	4.9	19.5	2.9	0.0	2.9	2.7	0.6	0.3	0.0	3.6	18.3	
March	14.1	3.5	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	2.9	0.4	0.0	0.0	3.3	22.3	
June	12.0	9.3	22.3	1.5	0.0	1.5	2.6	0.6	0.0	0.0	3.2	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	2.6	0.5	0.0	0.0	3.1	12.6	
October	6.0	6.4	12.6	8.0	0.0	8.0	2.5	0.3	0.0	0.0	2.9	18.7	16.2
November	12.5	6.0	18.7	2.0	0.0	2.0	2.5	0.4	0.0	0.0	2.9	17.8	
December	12.1	5.6	17.8	2.6	0.0	2.6	2.6	0.3	0.0	0.0	3.0	17.5	
2007													
January	12.0	5.4	17.5	4.3	0.0	4.3	2.7	0.4	0.0	0.0	3.1	18.1	20.0
February	12.6	5.4	18.1	2.4	0.0	2.4	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	
March*	N.A.	N.A.	N.A.	1.2	0.0	1.2	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	

PDS : Public Distribution System. OWS : Other Welfare Schemes. OMS : Open Market Sales. N.A.: Not Available.
@ : Offtake up to end-January. * : Procurement up to March 30, 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.

contributing almost 91 per cent of the growth in industry (Table 6). Electricity and mining sectors also picked up during the year.

Chart 2: Industrial Production

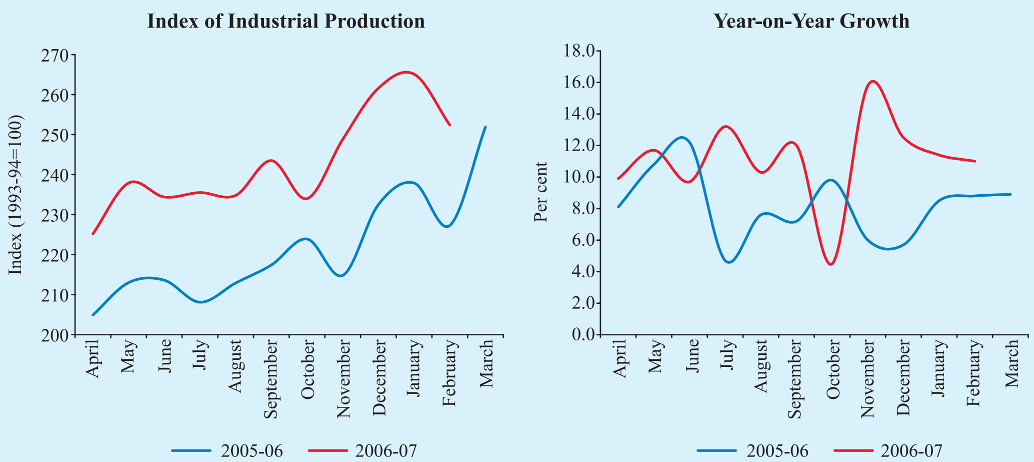


Table 6: Index of Industrial Production: Sectoral and Use-Based Classification of Industries

(Per cent)

Industry Group	Weight in the IIP	Growth Rate			Weighted Contribution #		
		April-March	April-February		April-March	April-February	
		2005-06	2005-06	2006-07 P	2005-06	2005-06	2006-07 P
1	2	3	4	5	6	7	8
Sectoral							
Mining	10.5	1.0	0.9	4.9	1.0	0.9	3.2
Manufacturing	79.4	9.1	9.1	12.1	93.3	93.0	91.1
Electricity	10.2	5.2	5.3	7.2	5.7	6.0	5.7
Use-Based							
Basic Goods	35.6	6.7	6.5	10.1	25.4	24.9	27.7
Capital Goods	9.3	15.7	16.3	17.8	20.0	20.2	17.3
Intermediate Goods	26.5	2.5	2.4	11.6	8.4	8.3	27.3
Consumer Goods (a+b)	28.7	12.0	12.0	9.5	46.3	46.7	28.0
a) Consumer Durables	5.4	15.3	14.7	9.8	14.9	14.5	7.5
b) Consumer Non-durables	23.3	10.9	11.1	9.4	31.4	32.2	20.5
General	**100.0**	**8.2**	**8.1**	**11.1**	**100.0**	**100.0**	**100.0**

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

The robust performance of the manufacturing sector was largely led by 'machinery and equipments', 'basic metal and alloy industries' and 'chemical and chemical products' (Table 7). 'Metal products and parts', 'leather and leather and fur products' and 'wood and wood products' made a turnaround.

Table 7: Growth of Manufacturing Groups

(Per cent)

Industry Group	Weight in the IIP	Growth Rate		Weighted Contribution #	
		April-February		April-February	
		2005-06	2006-07P	2005-06	2006-07P
1	2	3	4	5	6
1. Machinery and equipment other than transport equipment	9.6	12.1	14.0	20.7	18.4
2. Chemicals and chemical products except products of petroleum and coal	14.0	8.6	8.9	18.7	14.5
3. Basic metal and alloy industries	7.5	14.9	22.8	14.2	17.1
4. Transport equipment and parts	4.0	12.6	15.1	9.2	8.6
5. Non-metallic mineral products	4.4	10.1	13.2	7.0	7.0
6. Beverages, tobacco and related products	2.4	15.8	11.4	8.5	4.9
7. Rubber, plastic, petroleum and coal products	5.7	4.3	12.2	3.1	6.3
8. Cotton textiles	5.5	9.4	14.7	4.3	5.0
9. Textile products (including wearing apparel)	2.5	18.3	10.6	6.6	3.1
10. Other manufacturing industries	2.6	23.3	10.1	8.4	3.1
11. Paper and paper products and printing, publishing and allied activities	2.7	0.8	8.7	0.3	2.4
12. Metal products and parts (except machinery and equipment)	2.8	-1.3	7.7	-0.4	1.6
13. Wool, silk and man-made fibre textiles	2.3	0.4	8.7	0.2	2.2
14. Food products	9.1	0.6	6.2	0.6	4.3
15. Wood and wood products, furniture and fixtures	2.7	-5.6	21.8	-0.7	1.9
16. Jute and other vegetable fibre textiles (except cotton)	0.6	1.1	-15.1	0.0	-0.4
17. Leather and leather and fur products	1.1	-5.2	0.9	-0.6	0.1
Manufacturing – Total	**79.4**	**9.1**	**12.1**	**100.0**	**100.0**

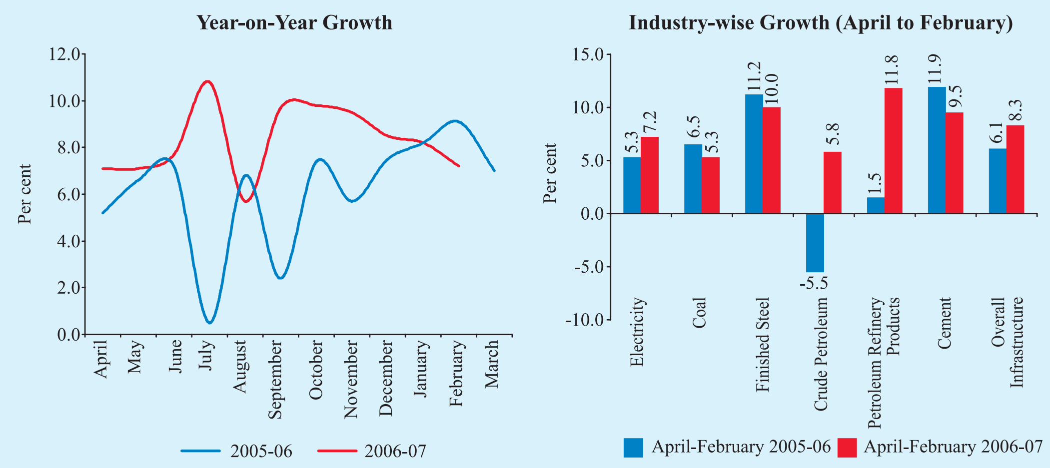
P : Provisional. # : Figures may not add up to 100 due to rounding off.
Source : Central Statistical Organisation.

In terms of the use-based classification, the capital goods sector maintained its growth momentum (17.8 per cent during April-February 2006-07 as compared with 16.3 per cent a year ago) on the back of strong investment demand (Table 6). Basic goods and intermediate goods sectors recorded growth of 10.1 per cent and 11.6 per cent, respectively - the highest growth rates since 1995-96 - spurred by higher production of cement, high speed diesel, iron and steel products, polyester fibre, viscose staple fibre, PVC pipes and tubes, and glazed tiles/ceramic tiles. Growth in consumer goods sector, both durables and non-durables, decelerated. Decline in production of some food products and a few drugs contributed to the lower growth in consumer non-durables.

Infrastructure

Growth in the infrastructure sector increased to 8.3 per cent during April-February 2006-07 from 6.1 per cent during the same period of 2005-06 on account of better performance of crude petroleum, electricity and petroleum refinery products (Chart 3). The higher thermal plant load factor and double-digit growth in hydro-power generation led to higher growth in electricity sector. Double-digit growth in the petroleum refinery products was partly due to the base effect and partly due to higher refinery capacity utilisation. The turnaround in crude petroleum production was on account of the restoration of production at Mumbai High offshore. Cement and steel production remained buoyant even on a high base.

Chart 3: Growth in Infrastructure Industries



Services Sector

The services sector, with a growth rate of 10.8 per cent during April-December 2006 as compared with 9.8 per cent a year ago, continued to be the key driver of economic activity (Table 1). 'Trade, hotels, transport and communication'

Table 8: 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	1.6	0.5	0.7	3.2
2001-02		0.2	2.0	0.9	0.6	3.8
2002-03		0.5	2.1	1.1	0.6	4.2
2003-04		0.7	2.9	0.8	0.8	5.2
2004-05		0.9	2.7	1.2	1.1	5.9
2005-06		0.9	2.7	1.5	1.1	6.2
2006-07		0.6	3.4	1.5	1.1	6.7
2005-06	Q1	0.8	2.5	1.2	1.0	5.5
	Q2	0.8	2.3	1.5	1.2	5.8
	Q3	0.9	2.4	1.2	1.1	5.7
	Q4	0.7	3.3	1.3	1.2	6.5
2006-07	Q1	0.6	3.3	1.3	1.0	6.2
	Q2	0.7	3.6	1.4	1.1	6.7
	Q3	0.6	3.3	1.5	1.0	6.4

and ‘financing, insurance, real estate and business services’ registered double-digit growth rates, offsetting the deceleration in ‘construction’. The sub-sector ‘trade, hotel, transport and communication’ contributed more than a third to overall real GDP growth during April-December 2006. It benefited from buoyancy in tourist arrivals, commercial vehicles production, telecom use, revenue earning freight of the railways, and passengers handled at domestic and international airports. The sub-sector ‘financing, insurance, real estate and business services’ benefited from acceleration of growth in bank deposits, sustained growth in non-food credit and continued buoyancy in business process outsourcing and information technology-enabled services exports (Tables 8 and 9).

Table 9: Indicators of Services Sector Activity

(Growth rates in per cent)

Sub-sector	2004-05	2005-06	April-January 2005-06	April-January 2006-07
1	2	3	4	5
Tourist arrivals	22.8	12.1	12.1$	14.4 $
Commercial vehicles production	28.6	10.6	10.0	34.8
Railway revenue earning freight traffic	8.1	10.7	10.4	9.4
New cell phone connections	10.4	89.4	68.0	96.4
Cargo handled at major ports	11.3	10.3	11.7	8.9
Civil aviation				
a) Export cargo handled	12.4	7.3	7.3	2.7
b) Import cargo handled	24.2	15.8	13.5	19.4
c) Passengers handled at international terminals	14.0	12.8	12.8	12.1
d) Passengers handled at domestic terminals	23.6	27.1	22.9	36.4
Roads: Upgradation of Highways	16.1	-23.4	–	–
Cement	8.2	10.7	11.9 #	9.5 #
Steel	7.6	6.0	11.2 #	10.0 #
Aggregate deposits	11.9	18.1	18.1 $	23.0 $
Non-food credit	31.6	31.8	31.8 $	28.0 $
Central Government expenditure	9.5*	8.7	7.7 *#	14.3 #

$: April-March. * : net of repayments to NSSF. # : April-February

Saving and Investment

Gross Domestic Savings (GDS), as per cent of GDP at current market prices, increased from 31.1 per cent in 2004-05 to 32.4 per cent in 2005-06 due to improvement in private corporate and household savings. The corporate savings rate has nearly doubled between 2002-03 and 2005-06 on the back of strong growth in profitability. While the overall savings rate increased by 1.3 percentage points of GDP in 2005-06, the overall investment rate increased by 2.3 percentage points of GDP to 33.8 per cent, reflecting the increase in current account deficit relative to GDP (Table 10).

Table 10: Gross Domestic Saving and Investment

(Per cent of GDP at current market prices)

	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05 (PE)	2005-06 (QE)
1	2	3	4	5	6	7	8
1. Household Saving	21.1	21.0	21.8	22.7	23.8	21.6	22.3
of which :							
a) Financial Assets	10.6	10.2	10.8	10.3	11.3	10.2	11.7
b) Physical Assets	10.5	10.8	10.9	12.4	12.4	11.4	10.7
2. Private Corporate Saving	4.5	4.3	3.7	4.2	4.7	7.1	8.1
3. Public Sector Saving	-0.8	-1.9	-2.0	-0.6	1.2	2.4	2.0
4. Gross Domestic Saving	24.8	23.4	23.5	26.4	29.7	31.1	32.4
5. Net Capital Inflow	1.1	0.6	-0.6	-1.2	-1.6	0.4	1.3
6. Gross Domestic Capital Formation	25.9	24.0	22.9	25.2	28.0	31.5	33.8
7. Gross Capital Formation	26.1	24.1	23.8	25.0	26.6	29.7	32.2
of which :							
a) Public Sector	7.4	6.9	6.9	6.1	6.3	7.1	7.4
b) Private Corporate Sector	7.4	5.7	5.4	5.9	6.9	9.9	12.9
c) Household Sector	10.5	10.8	10.9	12.4	12.4	11.4	10.7
d) Valuables +	0.8	0.7	0.6	0.6	0.9	1.3	1.2
8. Total Consumption Expenditure (a+b)	77.4	76.7	76.7	74.7	73.2	70.9	69.4
a) Private Final Consumption Expenditure	64.4	64.0	64.2	62.9	62.0	59.9	58.1
b) Government Final Consumption Expenditure	12.9	12.6	12.4	11.9	11.2	11.0	11.3
Memo:							
Saving-Investment Balance (4-6)	-1.1	-0.6	0.6	1.2	1.6	-0.4	-1.3
Public Sector Balance#	-8.2	-8.8	-8.9	-6.6	-5.2	-4.7	-5.4
Private Sector Balance#	7.7	8.8	9.2	8.6	9.2	7.4	6.9
a) Private Corporate Sector	-2.9	-1.4	-1.7	-1.7	-2.2	-2.8	-4.8
b) Household Sector	10.6	10.2	10.8	10.3	11.3	10.2	11.7

PE : Provisional Estimates. QE : Quick Estimates.
: Investment figures are not adjusted for errors and omissions.
\+ : Valuables cover the expenditures made on acquisition of valuables, excluding works of art and antiques.
Note : Figures may not add up to the totals due to rounding off.
Source : Central Statistical Organisation.

Business Expectations Surveys

Business confidence surveys conducted by various agencies present a mixed short-term outlook of the economy. According to the latest Business Confidence Survey conducted by the Federation of Indian Chambers and Commerce and Industry (FICCI) during the third quarter of 2006-07, the overall business confidence index increased by 4.0 per cent over the previous quarter (Table 11). Outlook on investment and exports for the next six months was, however, less encouraging, attributable to rising prices of capital goods, increasing cost of credit and rising input prices. The service sector emerged as the most optimistic sector among the three industry sectors surveyed, with 80 per cent of the respondents expecting their sector to perform 'moderately to substantially better' in the next six months.

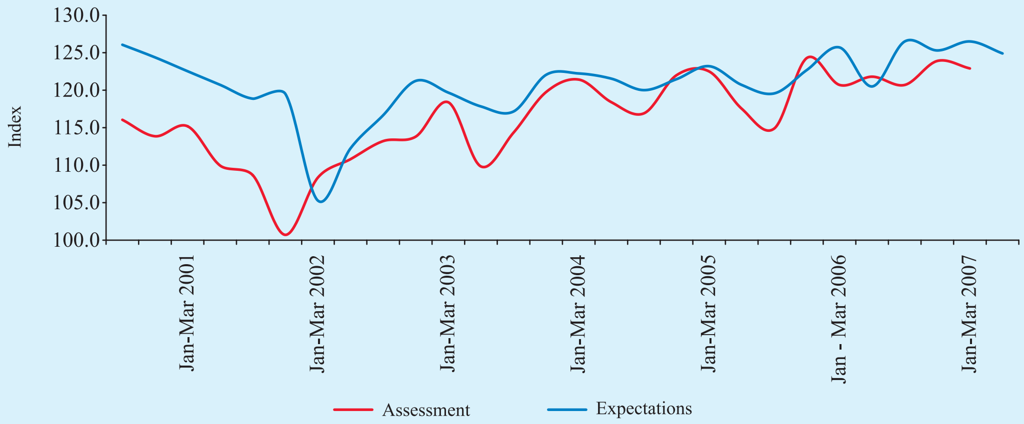
Table 11: Business Expectations Surveys

(per cent)

Agency	Business Expectations		Growth over a year ago	Growth over previous round
	Period	Index		
1	2	3	4	5
Dun & Bradstreet	January-March 2007	Business Optimism Index	16.0	9.8
NCAER	January-June 2007	Business Confidence Index	3.9	3.2
FICCI	January-June 2007	Business Confidence Index	-2.1	4.0
RBI	April-June 2007	Business Expectation Index	4.4	-1.6

According to the Reserve Bank's latest Industrial Outlook Survey conducted during December 2006-January 2007, the business expectations index based on assessment for January-March 2007 declined by 1.0 per cent (Chart 4). The

Chart 4: Reserve Bank's Industrial Outlook Survey: Business Expectation Index



business expectations index based on expectations for April-June 2007 also declined by 1.6 per cent over the previous quarter. The indices were, however, higher by 2.2 per cent and 4.4 per cent, respectively, than a year ago.

The decline in the expectations index for April-June 2007 over the previous quarter was on account of fall in expectations for major parameters of the survey such as overall business situation, production, working capital finance, order books, capacity utilisation and profit margin. Expectations of increase in employment, exports, imports and selling prices were, however, higher than the previous quarter (Table 12).

Forecasts by various agencies for real GDP growth in 2007-08 are set out in Table 13.

Table 12: Net Response on 'A Quarter Ahead' Expectations

(Per cent)

Parameter	Response	Apr-June 2006 (1086)	July-Sept. 2006 (1073)	Oct-Dec. 2006 (1138)	Jan-March 2007 (1115)	Apr-June 2007 (1108)
1	2	3	4	5	6	7
1. Overall business situation	Better	46.3	53.1	51.8	53.7	51.7
2. Financial situation	Better	40.4	43.4	41.9	44.5	43.8
3. Working capital finance requirement	Increase	30.6	32.7	35.4	36.2	35.3
4. Availability of finance	Improve	33.8	35.0	33.4	36.2	35.2
5. Production	Increase	42.5	49.4	49.7	50.7	47.8
6. Order books	Increase	39.1	45.2	46.3	47.3	45.7
7. Pending orders, if applicable	Below normal	-0.1	-0.8	-2.1	-2.7	-2.2
8. Cost of raw material	Decrease	-37.3	-45.8	-49.2	-41.7	-42.1
9. Inventory of raw material	Below average	-5.0	-6.3	-6.1	-7.1	-7.3
10. Inventory of finished goods	Below average	-4.5	-2.6	-4.9	-5.2	-4.4
11. Capacity utilisation (Main product)	Increase	24.8	32.1	33.2	33.3	29.4
12. Level of capacity utilisation (Compared to the average in the preceding four quarters)	Above normal	9.4	11.8	10.9	12.8	11.5
13. Assessment of the production capacity (With regard to expected demand in the next six months)	More than adequate	4.1	3.6	5.1	4.8	4.0
14. Employment in the company	Increase	14.5	16.4	17.9	18.1	18.3
15. Exports, if applicable	Increase	31.0	38.3	34.2	32.6	33.4
16. Imports, if any	Increase	22.7	23.8	23.4	20.8	21.6
17. Selling prices are expected to	Increase	12.4	16.6	16.8	14.2	15.5
18. If increase expected in selling prices	Increase at lower rate	12.0	10.5	14.5	10.5	12.1
19. Profit margin	Increase	9.3	11.1	9.2	11.6	9.9

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*.

Table 13: Projections of Real GDP for India for 2007-08 by various Agencies

(Per cent)

Agency	Overall Growth	Agriculture	Industry	Services	Month of Projection
1	2	3	4	5	6
ABN AMRO	7.6	–	–	–	March 2007
Asian Development Bank	8.0	–	–	–	March 2007
CII	8.5	3.0	9.3	9.9	April 2007
Citigroup	9.3	3.0	10.3	10.9	April 2007
CRISIL	7.9-8.4	–	–	–	March 2007
Indicus Analytics	8.4	3.0	7.9	9.7	April 2007
International Monetary Fund	8.4*	–	–	–	April 2007
ICRA	8.5	–	9.8	–	February 2007
JP Morgan	8.0	–	–	–	March 2007
National Council for Applied Economic Research	8.3	2.6	8.7	9.9	April 2007

– : Not Available. * : Calendar Year.

II. FISCAL SITUATION

Combined Government Finances: 2006-07

Combined Government finances were budgeted to improve in 2006-07, with key fiscal ratios placed 0.8-1.0 percentage points of GDP lower than in 2005-06, reflecting the improvement in the finances of both the Central and State Governments (Table 14). This was envisaged to be achieved through a reduction in expenditure (as percentage of GDP), particularly in the revenue account. The combined debt-GDP ratio was budgeted to decline from 78.5 per cent at end-March 2006 to 75.7 per cent at end-March 2007 (Chart 5).

The combined fiscal deficit during 2006-07 was budgeted to be financed primarily from domestic resources. Market borrowings were budgeted to finance 52.4 per cent of the gross fiscal deficit (GFD) during 2006-07 (45.5 per cent a year ago) while other liabilities (small savings, provident funds, reserve funds and deposits and advances) were budgeted to finance 44.9 per cent (43.7 per cent in 2005-06). External assistance was budgeted to finance 3.2 per cent of the combined fiscal deficit during 2006-07 as compared with 2.9 per cent in 2005-06 (Chart 6).

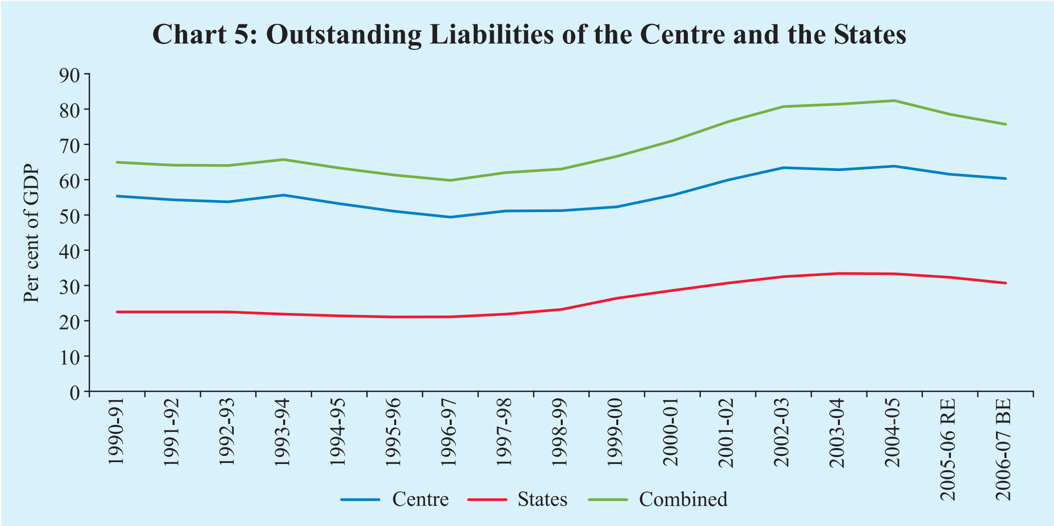
Table 14: Key Fiscal Indicators

(Per cent to GDP)

Year	Revenue Deficit	Gross Fiscal Deficit	Primary Deficit
1	2	3	4
		Centre	
2003-04	3.6	4.5	-0.03
2004-05	2.5	4.0	-0.04
2005-06	2.6	4.1	0.4
2006-07 BE	2.1	3.8	0.2
2006-07 RE	2.0	3.7	0.1
2007-08 BE	1.5	3.3	-0.2
		States	
2002-03	2.2	4.2	1.3
2003-04	2.2	4.5	1.5
2004-05	1.2	3.5	0.7
2005-06 RE	0.5	3.2	0.7
2006-07 BE	0.1	2.7	0.2
		Combined	
2002-03	6.6	9.6	3.1
2003-04	5.8	8.5	2.1
2004-05	3.7	7.5	1.4
2005-06 RE	3.1	7.4	1.6
2006-07 BE	2.2	6.4	0.8

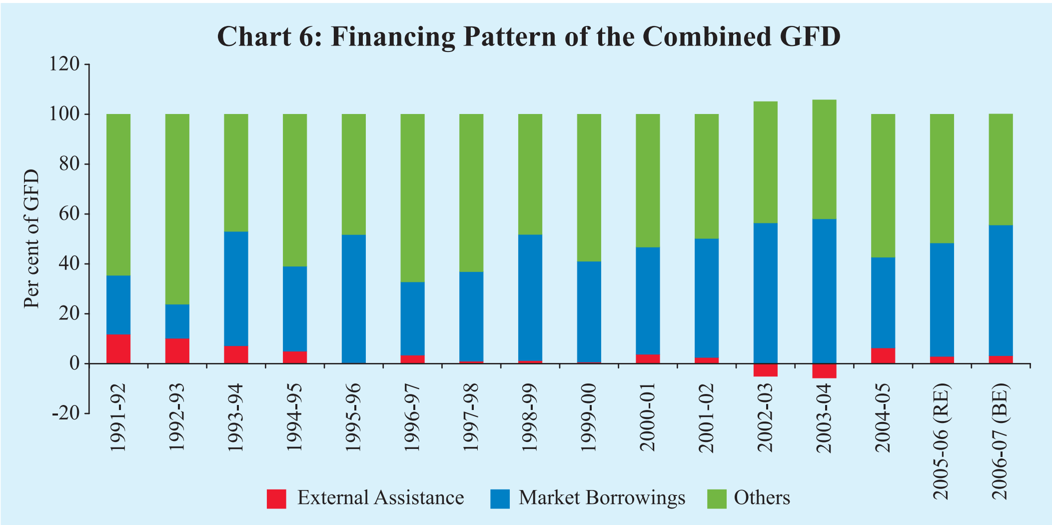
RE: Revised Estimates. BE: Budget Estimates.

Note: The fiscal ratios for finances of the Centre are from the Union Budget 2007-08. The fiscal ratios in respect of States and Combined finances for 2005-06 RE and 2006-07 BE are based on CSO's Quick Estimates and Advance Estimates, respectively.



Centre's Fiscal Situation: 2006-07

According to the revised estimates for 2006-07, the key deficit indicators of the Union Government, *viz.*, revenue deficit, gross fiscal deficit and primary deficit, relative to GDP, were placed lower than the budgeted levels. This mainly reflected buoyancy in revenue receipts, which more than offset the increased expenditures, particularly, in respect of interest payments, fertiliser and interest subsidies, and non-defence capital outlay. The Government could, therefore, effect reduction of 0.1 percentage point of GDP in each of the three key fiscal indicators *vis-à-vis* the budgeted levels. The reductions in GFD and revenue deficit (RD), relative to GDP,



of 0.4 percentage points and 0.6 percentage points, respectively, during 2006-07 (RE) over 2005-06 were also more than the minimum thresholds of 0.3 percentage points and 0.5 percentage points of GDP, respectively, stipulated under the Fiscal Responsibility and Budget Management (FRBM) Rules, 2004. The fiscal consolidation process was, thus, resumed during 2006-07 after a pause in 2005-06.

Revenue receipts in the revised estimates showed an increase of 4.9 per cent over the budgeted levels and were placed at 10.3 per cent of GDP. This was mainly on account of higher net tax revenue (5.7 per cent higher than budgeted) (Table 15), in turn, due to higher than budgeted collections in respect of personal income tax, corporation tax, customs duties and new taxes. However, collections under excise duties in the revised estimates were lower than the budget estimates (Chart 7). The collections under non-tax revenues were also better than the budget estimates on account of higher dividends and profits (10.7 per cent) and interest receipts (4.5 per cent). Among the capital receipts, recoveries of loans and advances were lower than budgeted, reflecting the impact of the debt waiver to the State Governments under the Twelfth Finance Commission (TFC) award.

The aggregate expenditure in the revised estimates for 2006-07 was 3.1 per cent higher than the budget estimates on account of higher revenue expenditure, particularly in interest payments, subsidies and grants to States (Table 16).

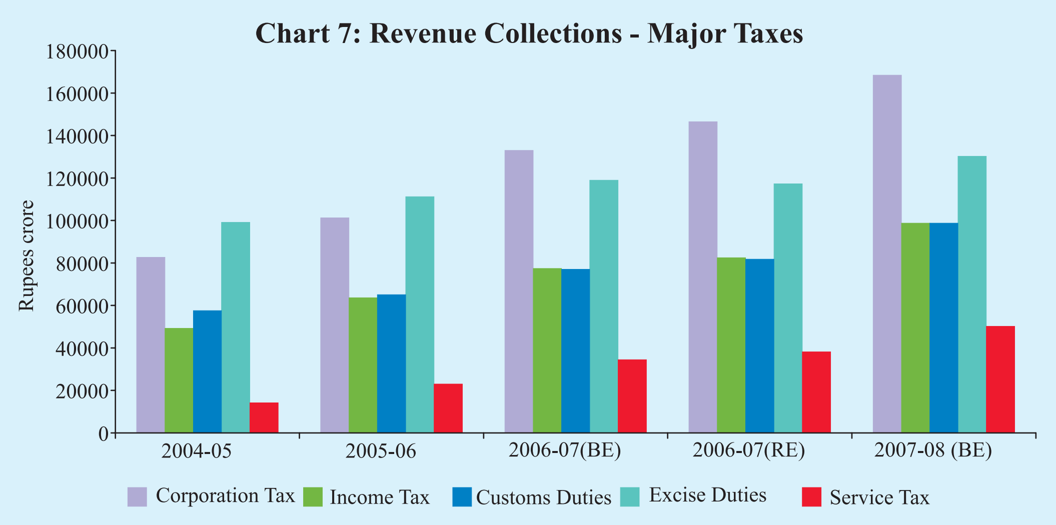
The total expenditure on subsidies at Rs.53,463 crore (1.3 per cent of GDP) in the revised estimates for 2006-07 was 15.7 per cent higher than the budgeted amount mainly on account of fertiliser and interest subsidies exceeding

Table 15: Receipts of the Centre

(Amount in Rupees crore)

Item	2005-06 (Accounts)	2006-07 (BE)	2006-07 (RE)	Variation (4 over 3)	
				Amount	Per cent
1	2	3	4	5	6
1. Total Receipts (2+3)	**5,06,123** **(14.2)**	**5,63,991** **(14.3)**	**5,81,637** **(14.2)**	**17,646**	**3.1**
2. Revenue Receipts (i+ii)	3,47,462 (9.7)	4,03,465 (10.2)	4,23,331 (10.3)	19,866	4.9
i) Tax Revenue (Net)	2,70,264 (7.6)	3,27,205 (8.3)	3,45,971 (8.4)	18,766	5.7
ii) Non-Tax Revenue	77,198 (2.2)	76,260 (1.9)	77,360 (1.9)	1,100	1.4
3. Capital Receipts	1,58,661 (4.4)	1,60,526 (4.1)	1,58,306 (3.9)	-2,220	-1.4
of which:					
Market Borrowings	1,06,241	1,13,778	1,10,500	-3,278	-2.9
Recoveries of Loans	10,645	8,000	5,450	-2,550	-31.9
Disinvestment Proceeds	1,581	3,840	528*	-3,312	-86.3

RE: Revised Estimates. BE: Budget Estimates.
* Represents bonus shares issued by Oil and Natural Gas Corporation (ONGC) Ltd.
Note : Figures in parentheses are percentages to GDP.



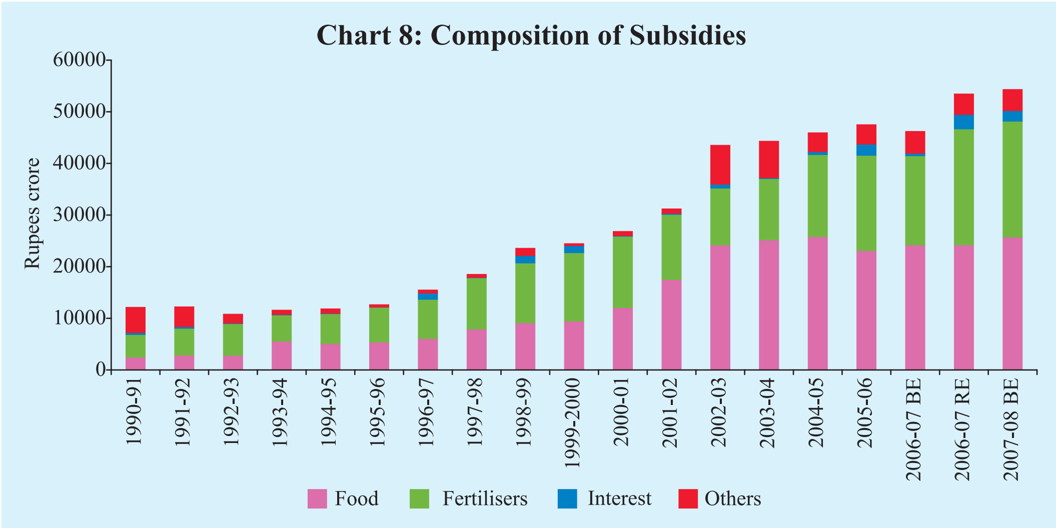
the budget estimates by Rs.5,199 crore (30.1 per cent) and Rs.2,320 crore (478.4 per cent), respectively (Chart 8). While fertilisers subsidies increased from Rs.17,253 crore in the budget estimates to Rs.22,452 crore in the revised estimates, interest subsidies increased from Rs.485 crore to Rs.2,805 crore. Fertiliser subsidies were higher than the budget estimates on account of increase in input costs and cost of imported fertiliser. Interest relief to debt stressed farmers

Table 16: Aggregate Expenditure of the Centre

(Amount in Rupees crore)

Item	2005-06 (Accounts)	2006-07(BE)	2006-07(RE)	Variation (4 over 3)	
				Amount	Per cent
1	2	3	4	5	6
1. Total Expenditure (2+3 = 4+5)	5,06,123 (14.2)	5,63,991 (14.3)	5,81,637 (14.2)	17,646	3.1
2. Non-Plan Expenditure	3,65,485 (10.2)	3,91,263 (9.9)	4,08,907 (10.0)	17,644	4.5
of which:					
Interest Payments	1,32,630 (3.7)	1,39,823 (3.5)	1,46,192 (3.6)	6,369	4.6
Defence Expenditure	80,549 (2.3)	89,000 (2.3)	86,000 (2.1)	-3,000	-3.4
Subsidies	47,520 (1.3)	46,213 (1.2)	53,463 (1.3)	7,250	15.7
3. Plan Expenditure	1,40,638 (3.9)	1,72,728 (4.4)	1,72,730 (4.2)	2	0.0
4. Revenue Expenditure	4,39,761 (12.3)	4,88,192 (12.4)	5,06,767 (12.4)	18,575	3.8
5. Capital Expenditure	66,362 (1.9)	75,799 (1.9)	74,870 (1.8)	-929	-1.2

RE : Revised Estimates. BE : Budget Estimates.
Note : Figures in parentheses are percentages to GDP.



and provision of interest subvention on short-term credit to farmers led to higher than budgeted interest subsidies.

Financing of the Union Budget

Gross and net market borrowings (dated securities and 364-day Treasury Bills excluding allocations under the Market Stabilisation Scheme) of the Centre for 2006-07 were budgeted at Rs.1,79,716 crore and Rs.1,13,778 crore, respectively. In the revised estimates, net market borrowings were placed lower at Rs.1,10,500 crore, thus, financing 72.5 per cent of GFD. Apart from market borrowings, drawdown of cash balances financed 7.2 per cent of GFD in the revised estimates as compared to nil percentage in the budget estimates. In the public account, deposits and advances, state provident funds and reserve funds financed 7.6 per cent, 3.3 per cent and 2.8 per cent, respectively, of GFD.

According to the Reserve Bank records, actual gross market borrowings by the Central Government through dated securities and 364-day Treasury Bills amounted to Rs.1,79,373 crore (net Rs.1,11,270 crore) during 2006-07. Gross market borrowings through dated securities by the Central Government amounted to Rs.1,46,000 crore (net Rs.1,06,916 crore) during 2006-07 as compared with Rs.1,31,000 crore (net Rs.98,370 crore) during the previous year (Table 17). Gross market borrowings through dated securities during 2006-07 were 94 per cent of the budget estimates, the same as that in the previous year. Of the 33 auctions held during 2006-07, 30 auctions were in respect of reissuance of existing securities. Three new securities of 10-year, 15-year and 30-year were issued to provide a benchmark in the secondary market. The total devolvement on the primary dealers (PDs) was Rs.5,604 crore.

Table 17: Central Government Securities Issued during 2006-07

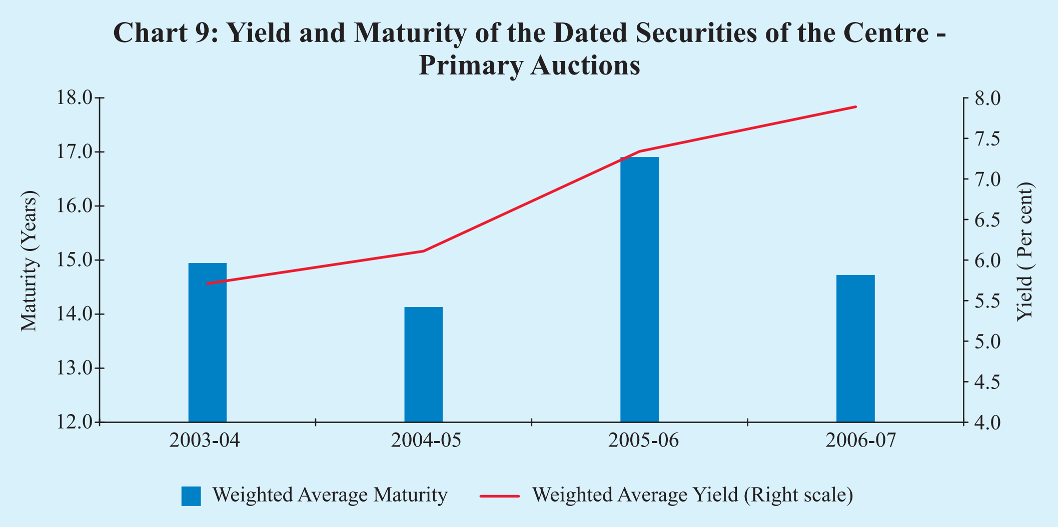
(Amount in Rupees crore/Maturity in years)

Sr. No.	Borrowings as per Issuance Auction Calendar: Date of Auction	Amount	Residual Maturity	Actual Borrowings: 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	7.39
		4,000	20 and above	June 6, 2006	4,000	30.00	8.33
6.	June 15-24, 2006	5,000	15-19	June 22, 2006	5,000	7.81	7.92
				June 22, 2006#	4,000	14.92	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	Not issued	–	–	–
		4,000	20 and above	January 12, 2007	4,000	29.39	8.24
17.	January 18-25, 2007	5,000	15-20	January 25, 2007	5,000	14.32	8.20
18.	February 2-9, 2007	6,000	5-9	February 9, 2007	6,000	7.18	7.88
		3,000	20 and above	February 9, 2007	3,000	29.32	8.19
19.	March 2-9, 2007	5,000	10-14	March 9, 2007	4,000	9.84	8.06
		3,000	20 and above	March 9, 2007	3,000	29.24	8.40

: Not scheduled.

The weighted average yield of the dated securities issued during 2006-07 increased to 7.89 per cent from 7.34 per cent during the previous year. The weighted average maturity of the dated securities issued during the year, on the other hand, fell to 14.72 years from 16.90 years during 2005-06 (Chart 9).

With the Reserve Bank withdrawing from participation in the primary issuance of the Central Government securities with effect from April 1, 2006 in accordance with the FRBM Act, 2003, the Ways and Means Advances (WMA) arrangements were revised from 2006-07 in consultation with the Government. Under the previous arrangements, the limits of WMA were fixed on a half-yearly basis. For 2005-06, the limits were Rs.10,000 crore for the first half of the fiscal



year (April-September) and Rs.6,000 crore for the second half of the fiscal year (October-March). In order to facilitate the transition necessitated by the new FRBM provisions, under the revised arrangements, the limits for 2006-07 were fixed on a quarterly basis instead of half-yearly basis. Accordingly, the WMA limits for 2006-07 were placed at Rs.20,000 crore and Rs.10,000 crore for the first and second quarters, respectively, and Rs.6,000 crore each for the third and fourth quarters of the year. The Reserve Bank retained the flexibility to revise the limits in consultation with the Government of India taking into consideration the transitional issues and prevailing circumstances. Furthermore, interest rates on WMA and overdraft have been linked to the repo rate as against the Bank Rate hitherto, following emergence of the repo rate as the short-term reference rate. Accordingly, the interest rate on WMA is at the repo rate and that on overdraft is at repo rate *plus* two percentage points.

The Central Government took recourse to WMA on 39 days during 2006-07 as compared with only two days during 2005-06. The average WMA utilisation during 2006-07 was Rs.402 crore as compared with Rs.3 crore in the previous year. The peak WMA availed amounted to Rs.11,754 crore on June 6, 2006. The Central Government did not resort to overdraft during the year.

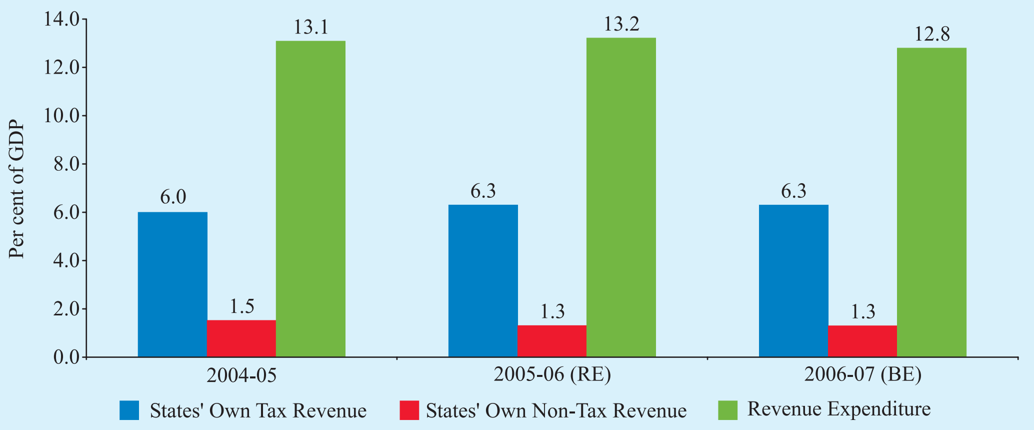
The surplus cash balances of the Centre which amounted to Rs.48,928 crore at end-March 2006 dwindled rapidly during April-May 2006. The Centre has, however, been maintaining surplus cash balance from August 8, 2006, mainly reflecting parking of surplus cash by the State Governments in the 14-day Intermediate Treasury Bills during the greater part of the year. The surplus balance rose to an intra-year high of Rs.77,473 crore on March 21, 2007, reflecting buoyancy in advance tax collections. As on March 31, 2007, the surplus balance amounted to Rs.50,092 crore. The daily surplus balance of the Central Government averaged Rs.28,022 crore during 2006-07 as compared with Rs.25,296 crore a year ago.

State Finances: 2006-07

Revenue deficit (RD) and gross fiscal deficit (GFD) of State Governments were budgeted at 0.1 per cent and 2.7 per cent, respectively, of GDP during 2006-07 - a reduction of 0.4 percentage points and 0.5 percentage points, respectively, over the previous year (Table 14). State budgets for 2006-07 reflect the efforts of the State Governments to pursue the process of fiscal correction and consolidation through the progressive enactment of Fiscal Responsibility Legislations (FRLs). The State Governments were aided in their effort by larger devolution and transfer through shareable Central taxes and grants under the TFC award. Furthermore, all States, barring Uttar Pradesh, have implemented value added tax (VAT) in *lieu* of sales tax, which is expected to provide buoyancy to the States' own tax revenue. Recognising that sustained fiscal correction lies in revenue augmentation, the State Governments in their budgets for 2006-07 laid stress on improvement in tax administration and streamlining and strengthening of tax and non-tax collections. For improving accountability of budget proposals, some States proposed to introduce 'Outcome Budget'. Several States announced introduction of new pension scheme based on defined contribution to restrict their rising pension obligations. The States also proposed to improve spending on education and health sector and implement the centrally sponsored scheme of rural employment guarantee scheme.

The fiscal correction in the revenue account during 2006-07 was proposed to be achieved primarily through containment of growth in revenue expenditure to 11.3 per cent in 2006-07 from 15.4 per cent in the previous year. As a proportion to GDP, revenue expenditure was envisaged to decline to 12.8 per cent during 2006-07 (BE) from 13.2 per cent in the previous year (Chart 10). Revenue receipts were budgeted to be maintained at the level of 12.7 per cent of GDP in 2006-07 (BE). States' own tax as well as own non-tax revenues, as percentage to GDP, at 6.3 per cent and 1.3 per cent, respectively, during 2006-07 (BE) would remain the same as

Chart 10: States' Own Revenue Receipts and Revenue Expenditure



a year ago. Higher grants coupled with the incentives provided by the TFC towards restructuring of State finances aided the States in their endeavour for fiscal correction and consolidation.

The decomposition of GFD of the State Governments reveals an improvement in the quality of fiscal consolidation, with the share of revenue deficit budgeted to decline substantially to 4.1 per cent in 2006-07 from 15.1 per cent in the previous year. Correspondingly, the share of capital outlay would move up from 74.9 per cent in 2005-06 (RE) to 88.0 per cent in 2006-07 (BE). As regards financing of GFD, securities issued to the National Small Savings Fund (NSSF) would continue to be the major source of financing, although its share would decline from 65.4 per cent to 53.1 per cent. Market borrowings with their share at 20.8 per cent (16.4 per cent during the previous year) would finance a larger share of GFD during 2006-07 (Table 18).

Table 18: Decomposition and Financing Pattern of GFD of States

(Per cent)

Item	1990-95 (Average)	1995-2000 (Average)	2000-04 (Average)	2004-05	2005-06 (RE)	2006-07 (BE)
1	2	3	4	5	6	7
Decomposition (1 to 4)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
1. Revenue Deficit	24.7	44.8	56.3	33.3	15.1	4.1
2. Capital Outlay	55.3	43.3	36.7	56.3	74.9	88.0
3. Net Lending	20.0	12.2	7.0	10.3	10.0	8.8
4. Disinvestment	–	-0.2	–	–	–	-0.9
Financing (1 to 11)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
1. Market Borrowings	16.0	16.1	24.6	31.6	16.4	20.8
2. Loans from Centre	49.0	40.6	7.8	-10.8	1.9	4.4
3. Special Securities issued to NSSF/Small Savings	–	28.9*	35.4	62.2	65.4	53.1
4. Loans from LIC, NABARD, NCDC, SBI and other banks	1.8	2.8	4.9	–**	4.9	6.9
5. State Provident Fund	14.3	13.4	8.3	7.2	7.9	8.0
6. Reserve Funds	6.8	5.5	4.5	6.5	2.9	4.0
7. Deposits and Advances	9.8	9.8	3.4	7.4	-0.6	-1.1
8. Suspense and Miscellaneous	4.3	2.7	-0.4	-2.4	3.3	3.3
9. Remittances	-1.4	-3.6	0.6	1.1	0.8	1.8
10. Overall Surplus(+)/Deficit(-)	4.4	-2.6	1.1	9.6	4.9	3.6
11. Others	-5.0	9.5	9.8	-12.4 $	-7.9	-4.7

BE: Budget Estimates. RE: Revised Estimates. – : Negligible/Not applicable.

* : Pertains to 1999-2000 as the scheme was introduced from that year only. The sum of items will not be equal to 100 for 1995-2000 (Average).

** : Tamil Nadu has shown a negative figure of Rs.1,376 crore under Loans from National Co-operative Development Corporation (NCDC) on account of adjustment of Tamil Nadu Industrial Development Corporation (TIDCO) bonds.

$: On account of Land Compensation and other bonds (Rs.1,962 crore) issued by Government of Tamil Nadu.

Notes : 1. 'Others' is a residual item and includes, *inter alia*, Contingency Funds, Appropriation to Contingency Funds, Miscellaneous Capital Receipts, Inter-State Settlement, Land Compensation and Other Bonds and Loans from Financial Institutions other than those mentioned in the Table.

2. Due to the change in the accounting procedure from 1999-2000, Loans from the Centre exclude States' share in small saving collections which are shown under Securities issued to the NSSF under internal debt. Accordingly, repayments of small saving collections included in under repayments of Loans to the Centre are now shown under discharge of Internal Debt to have consistent accounting for receipts and expenditure.

3. Figures for 2004-05 (Accounts) in respect of Jammu & Kashmir and Jharkhand relate to Revised Estimates.

4. All financing items are on net basis.

Source : Budget Documents of State Governments.

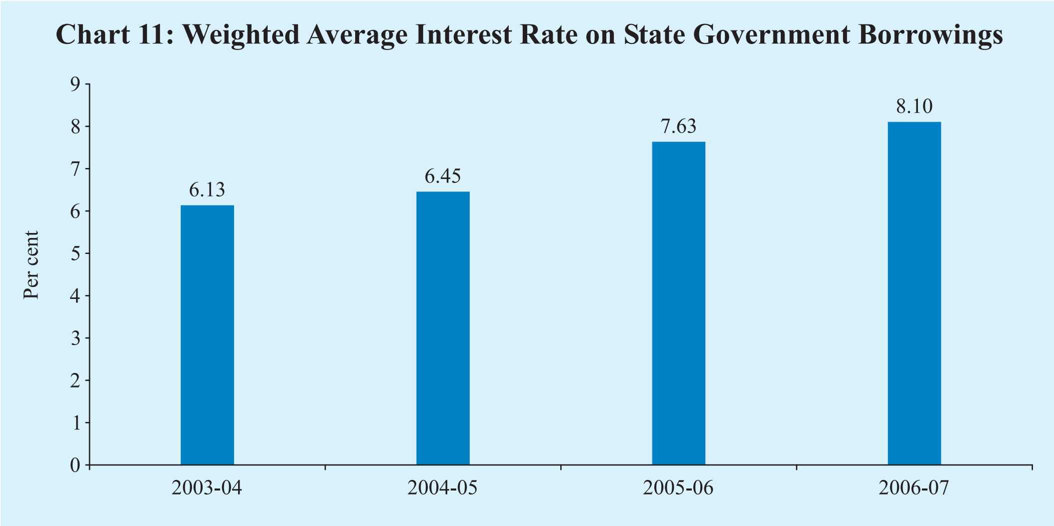
Market Borrowings

The provisional net allocation of market borrowings for all State Governments during 2006-07 was placed at Rs.17,243 crore. The gross allocation of market borrowings amounted to Rs.26,597 crore, including the additional allocation of Rs.2,803 crore and repayments of Rs.6,551 crore. During 2006-07, the States raised market loans amounting to Rs.20,825 crore (or 78.3 per cent of gross allocation) through auctions, with cut-off rates in the range 7.65-8.66 per cent (Table 19). The

Table 19: Market Borrowings of State Governments during 2006-07

Item	Date	Cut-off Rate (Per cent)	Tenor (Years)	Amount Raised (Rupees crore)
1	2	3	4	5
A. Tap Issues	–	–	–	–
B. Auctions (i to xii)				**20,825**
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
vi. Sixth	November 16, 2006	7.74	10	2,184
		7.80	10	91
		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	7.99	10	300
		7.99	10	100
		7.99	10	315
		7.96	10	500
ix. Ninth	February 2, 2007	7.95	10	200
x. Tenth	February 22, 2007	8.17	10	375
		8.10	10	47
		8.20	10	213
		8.19	10	300
		8.20	10	350
		8.19	10	500
		8.45	10	1,615
xi. Eleventh	March 13, 2007	8.38	10	212
		8.45	10	250
		8.40	10	470
		8.39	10	67
		8.39	10	70
		8.39	10	90
		8.32	10	300
		8.25	10	200
		8.32	10	414
		8.38	10	211
xii. Twelfth	March 23, 2007	8.35	10	738
Grand Total (A+B)				**20,825**

Source : Reserve Bank of India.



weighted average interest rate of market loans increased to 8.10 per cent during 2006-07 from 7.63 per cent during the previous year (Chart 11).

The liquidity position of the States remained comfortable during 2006-07. This was reflected in the weekly average investment by the States in the 14-day Treasury Bills which increased further during 2006-07 to Rs.43,075 crore from Rs.35,278 crore in the previous year (Chart 12). The surplus cash balances of the State Governments are automatically invested in 14-day Treasury Bills. The weekly average utilisation of WMA and overdraft by the States at Rs.234 crore in 2006-07 was lower than that of Rs.482 crore in 2005-06 (Chart 13).

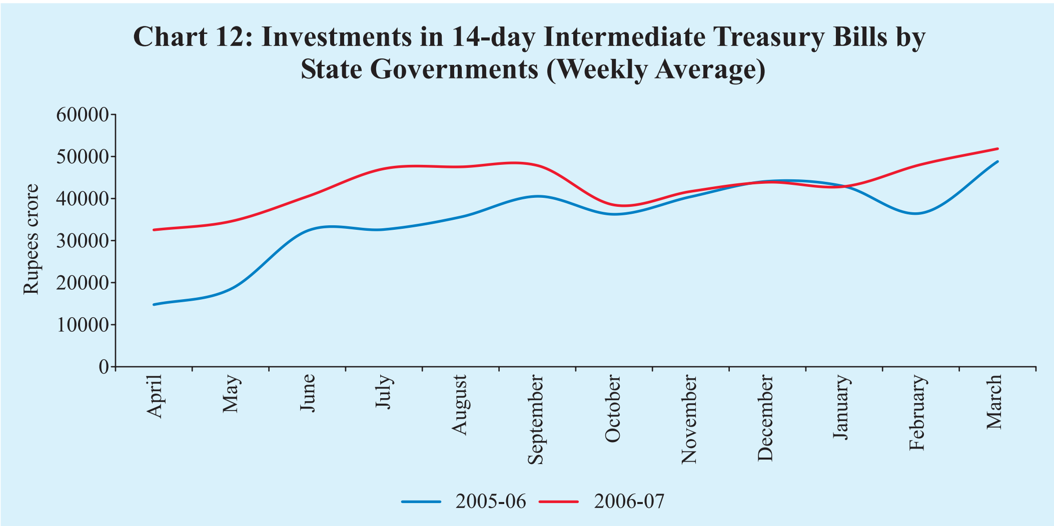
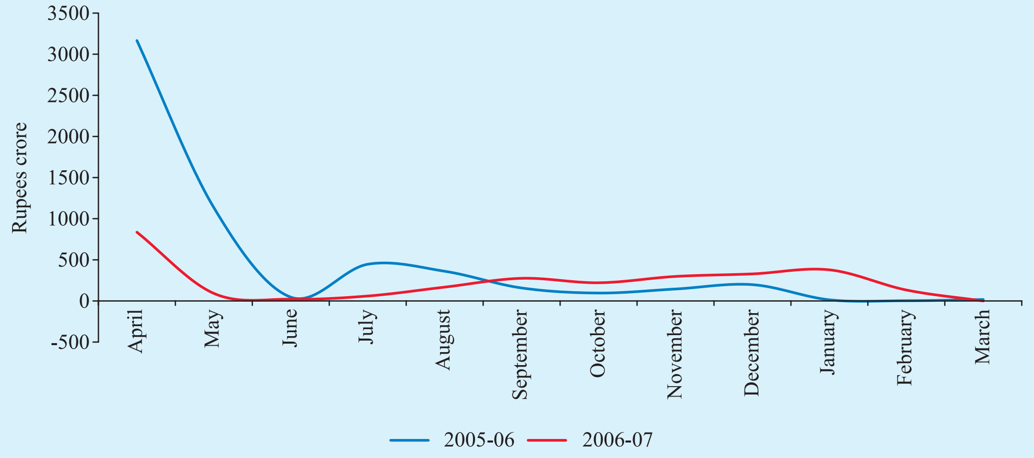


Chart 13: Utilisation of WMA and Overdraft by States (Weekly Average)



Two States resorted to overdraft during 2006-07 as compared with eight States during the previous year.

Fiscal Outlook: 2007-08

The Union Budget for 2007-08 proposes to continue the fiscal consolidation process, with the key deficit indicators, *viz.*, gross fiscal deficit (GFD), revenue deficit (RD) and primary deficit (PD), budgeted to be lower by 0.3-0.5 percentage points of GDP in 2007-08 than the previous year (Table 20). The Budget envisages a revenue-led fiscal consolidation along with reprioritisation of expenditure to augment allocations for improvement in the social and physical infrastructure, particularly in the rural areas so as to achieve a 'faster and more inclusive' growth process. The revenue deficit relative to GDP is budgeted to be reduced in 2007-08 by 0.5 percentage points, which is the minimum stipulated threshold limit under the FRBM Rule, 2004; therefore, a substantial correction in the revenue deficit of 1.5 percentage points would be required in 2008-09, the terminal year for meeting the FRBM target.

The gross tax-GDP ratio, which has been rising since 2002-03, is budgeted to improve from 11.4 per cent in 2006-07 (RE) to 11.8 per cent in 2007-08 (BE). This reflects expectations of high growth as well as the impact of measures taken to widen the tax base, rationalise exemptions and improve tax compliance (Table 21).

The budget estimates of total expenditure in the Union Budget 2007-08 include a sum of Rs.40,000 crore allocated for acquiring the Reserve Bank's equity holding in the State Bank of India (SBI). As this transaction is matched by the non-debt capital receipt of an equal amount, there would be no impact on the

Table 20: Union Budget 2007-08 at a Glance

(Amount in Rupees crore)

Item	2006-07 (RE)	2007-08 (BE)	Growth rate (per cent)	
			2006-07	2007-08
1	2	3	4	5
1, Revenue Receipts (i+ii)	4,23,331 (10.3)	4,86,422 (10.5)	21.8	14.9
i) Tax Revenue (Net)	3,45,971 (8.4)	4,03,872 (8.7)	28.0	16.7
ii) Non-Tax Revenue	77,360 (1.9)	82,550 (1.8)	0.2	6.7
2. Non-Plan Expenditure *of which*:	4,08,907 (10.0)	4,35,421* (9.4)	11.9	6.5
i) Interest Payments	1,46,192 (3.6)	1,58,995 (3.4)	10.2	8.8
ii) Defence Expenditure	86,000 (2.1)	96,000 (2.1)	6.8	11.6
iii) Subsidies	53,463 (1.3)	54,330 (1.2)	12.5	1.6
3. Plan Expenditure	1,72,730 (4.2)	2,05,100 (4.4)	22.8	18.7
4. Revenue Expenditure	5,06,767 (12.4)	5,57,900 (12.0)	15.2	10.1
5. Capital Expenditure	74,870 (1.8)	82,621* (1.8)	12.8	10.4
6. Total Expenditure	5,81,637 (14.2)	6,40,521* (13.8)	14.9	10.1
7. Revenue Deficit	83,436 (2.0)	71,478 (1.5)	-9.6	-14.3
8. Gross Fiscal Deficit	1,52,328 (3.7)	1,50,948 (3.3)	4.0	-0.9
9. Gross Primary Deficit	6,136 (0.1)	-8,047 (-0.2)	-55.6	-231.1

* : Adjusted for an amount of Rs.40,000 crore on account of transactions relating to transfer of RBI's stake in SBI to the Government.

Note : Figures in parentheses are percentages to GDP.

deficit indicators. Aggregate expenditure, after adjusting for this transaction, is budgeted to increase by 10.1 per cent in 2007-08. Growth in the revenue expenditure in 2007-08 is budgeted to decelerate to 10.1 per cent from 15.2 per cent in 2006-07 on account of containment of subsidies and deceleration in the growth of interest payments. The capital outlay (adjusted for transactions for purchasing stake in the SBI) is budgeted to increase by 15.3 per cent as compared with an increase of 18.4 per cent in 2006-07.

During 2007-08, net market borrowings (net of MSS) are budgeted to increase marginally from Rs.1,10,500 crore in 2006-07 (RE) to Rs.1,10,827 crore. Inclusive of repayments of Rs.76,942 crore, gross market borrowings, net of MSS, are placed at Rs.1,87,769 crore in 2007-08. Net market borrowings would finance

Table 21: Gross Tax Revenues of the Centre

(Per cent to GDP)

Year	Direct	Indirect	Total
1	2	3	4
1990-91	1.9	8.2	10.1
1991-92	2.3	8.0	10.3
1992-93	2.4	7.5	10.0
1993-94	2.4	6.5	8.8
1994-95	2.7	6.5	9.1
1995-96	2.8	6.5	9.4
1996-97	2.8	6.6	9.4
1997-98	3.2	6.0	9.1
1998-99	2.7	5.6	8.3
1999-00	3.0	5.8	8.8
2000-01	3.2	5.7	9.0
2001-02	3.0	5.2	8.2
2002-03	3.4	5.4	8.8
2003-04	3.8	5.4	9.2
2004-05	4.2	5.5	9.8
2005-06	4.6	5.6	10.3
2006-07 RE	5.6	5.8	11.4
2007-08 BE	5.8	6.1	11.8

73.4 per cent of GFD in 2007-08 as compared with 72.5 per cent in the revised estimates for 2006-07. Investments by the National Small Savings Fund (NSSF) in the special Central Government securities are budgeted to finance 7.0 per cent of GFD as against 2.0 per cent in the previous year. This reflects the reinvestment of redemption proceeds as well as investment from small savings collections in Central Government special securities following the policy decision to reduce the minimum obligation of the State Governments to borrow from the NSSF to 80 per cent of net collections from 100 per cent. External assistance is budgeted to finance 6.0 per cent of GFD as compared with 5.2 per cent of GFD in 2006-07.

III. MONETARY AND LIQUIDITY CONDITIONS

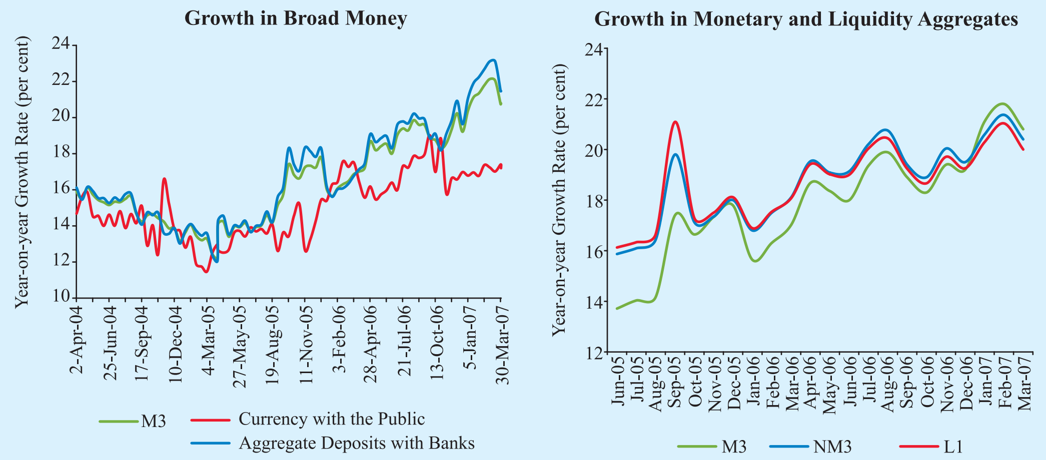
Broad money growth accelerated during 2006-07, and remained above the indicative trajectory projected by the Reserve Bank at the beginning of the fiscal year. Bank credit continued to grow at a strong pace for the third successive year, *albeit* with some moderation. Deposits exhibited sharp growth and enabled financing of sustained high demand for credit. Banks' investments in SLR securities increased during the year, but the pace of expansion did not keep pace with the expansion in their net demand and time liabilities (NDTL). As a result, banks' SLR investments, as a proportion of their NDTL, declined further during 2006-07. The Reserve Bank continued to modulate market liquidity with the help of repo and reverse repos under the liquidity adjustment facility (LAF), issuance of securities, including dated securities, under the Market Stabilisation Scheme (MSS) and the cash reserve ratio (CRR). The task of liquidity management was complicated during 2006-07 due to large variations in market liquidity on account of variations in cash balances of the Governments and capital flows.

Monetary Survey

Broad money (M_3) growth, year-on-year (y-o-y), accelerated to 20.8 per cent as at end-March 2007 from 17.0 per cent a year ago. Expansion in the residency-based new monetary aggregate (NM_3) – which does not directly reckon non-resident foreign currency deposits such as FCNR(B) – also accelerated from 18.1 per cent as at end-March 2006 to 20.4 per cent as at end-March 2007. Growth in liquidity aggregate, L_1, at 20.0 per cent was also higher than that of 18.1 per cent a year ago. Growth in NM_3 as at end-March 2007 was marginally lower than that in M_3. Growth in L_1 was marginally lower than that in NM_3 on account of lower growth in postal deposits *vis-à-vis* bank deposits (Chart 14 and Table 22).

Taking into account, *inter alia,* high growth in monetary aggregates, sustained growth in credit offtake, trends in liquidity absorbed under LAF/MSS, challenges emanating from the effects of capital flows on liquidity, acceleration in inflation, growth in real GDP, expectations of the private corporate sector of higher increase in prices of both inputs and outputs, reports of growing strains on domestic capacity utilisation, global developments in monetary management and the paramount need to contain inflationary expectations, the Reserve Bank has announced an increase of 150 basis points in the cash reserve ratio (CRR) in phases from December 2006 (see also Chapter IV). The first round of increase in the CRR, announced on December 8, 2006, of 50 basis points – 25 basis points each – was effective in the fortnights

Chart 14: Money Supply



beginning December 23, 2006 and January 6, 2007. The second round of the increase, announced on February 13, 2007, also of 50 basis points – 25 basis points

Table 22: Monetary Indicators

(Amount in Rupees crore)

Item	Outstanding as on March 31, 2007	Variation 2005-06 Amount	Variation 2005-06 Per cent	Variation 2006-07 Amount	Variation 2006-07 Per cent
1	2	3	4	5	6
I. Reserve Money	7,08,950	83,922	17.2	1,35,892	23.7
II. Narrow Money (M_1)	9,59,875	1,43,825	21.1	1,33,497	16.2
III. Broad Money (M_3)	32,96,919	3,96,881	17.0	5,67,372	20.8
a) Currency with the Public	4,84,171	58,248	16.4	71,052	17.2
b) Aggregate Deposits	28,05,261	3,38,081	17.1	4,95,704	21.5
i) Demand Deposits	4,68,216	85,025	26.5	61,829	15.2
ii) Time Deposits	23,37,045	2,53,056	15.3	4,33,875	22.8
of which: Non-Resident Foreign Currency Deposits	66,242	-16,876	-22.2	6,967	11.8
IV. NM_3	33,06,958	4,21,126	18.1	5,59,370	20.4
of which: Call Term Funding from FIs	86,151	11,224	15.6	3,007	3.6
V. a) L_1	34,21,762	4,36,397	18.1	5,70,256	20.0
of which: Postal Deposits	1,14,804	15,271	17.2	10,886	10.5
b) L_2	34,24,694	4,37,206	18.1	5,70,256	20.0
c) L_3	34,50,758	4,41,207	18.1	5,72,479	19.9
VI. Major Sources of Broad Money					
a) Net Bank Credit to the Government (i+ii)	8,32,867	17,888	2.4	66,272	8.6
i) Net Reserve Bank Credit to Government	4,362	35,799		-3,775	
ii) Other Banks' Credit to Government	8,28,505	-17,910	-2.3	70,046	9.2
b) Bank Credit to Commercial Sector	21,23,290	3,61,746	27.2	4,30,287	25.4
c) Net Foreign Exchange Assets of Banking Sector	9,30,319	78,291	12.1	2,04,125	28.1
Memo:					
SCBs Aggregate Deposits	25,94,259	3,23,913	18.1	4,85,210	23.0
SCBs Non-food Credit	18,76,672	3,54,193	31.8	4,10,285	28.0

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 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. Data reflect redemption of India Millennium Deposits (IMDs) on December 29, 2005.
3. Government balances as on March 31, 2007 are before closure of accounts.
4. Variation during 2006-07 is worked out from March 31, 2006, whereas variation during 2005-06 is worked out from April 1, 2005.

each – was effective in the fortnights beginning February 17, 2007 and March 3, 2007. On March 30, 2007, the Reserve Bank announced a further increase of 50 basis points in the CRR – 25 basis points each – effective in the fortnights beginning April 14, 2007 and April 28, 2007. As a result of the above increases in the CRR, an amount of about Rs.43,000 crore of resources of banks is likely to be absorbed.

Amongst the major components of M_3, growth in currency with the public was 17.2 per cent, year-on-year (y-o-y), as at end-March 2007 as compared with 16.4 per cent a year ago (Table 22). Currency with the public followed the usual seasonal pattern, contracting during the second quarter and expanding during the remaining quarters (Table 23). On a y-o-y basis, growth in demand deposits (15.2 per cent) as at end-March 2007 was of a lower order than a year ago (26.5 per cent). As a result, growth in narrow money, M_1, decelerated to 16.2 per cent as at end-March 2007 from 21.1 per cent a year ago.

Table 23: Monetary Aggregates – Variations

(Rupees crore)

Item	2005-06	2006-07	2006-07			
			Q1	Q2	Q3	Q4
1	2	3	4	5	6	7
M_3 (=1+2+3=4+5+6+7-8)	**3,96,881 (17.0)**	**5,67,372 (20.8)**	**55,414**	**1,65,809**	**62,607**	**2,83,542**
Components						
1. Currency with the Public	58,248 (16.4)	71,052 (17.2)	23,797	-3,091	27,849	22,497
2. Aggregates Deposits with Banks	3,38,081 (17.1)	4,95,704 (21.5)	33,227	1,68,447	35,253	2,58,777
2.1 Demand Deposits with Banks	85,025 (26.5)	61,829 (15.2)	-42,399	41,595	-7,462	70,094
2.2 Time Deposits with Banks	2,53,056 (15.3)	4,33,875 (22.8)	75,626	1,26,851	42,715	1,88,682
3. 'Other' Deposits with Banks	552	617	-1,610	453	-495	2,269
Sources						
4. Net Bank Credit to Government	17,888 (2.4)	66,272 (8.6)	23,431	15,705	-13,091	40,227
4.1 RBI's net credit to Government	35,799	-3,775	53	2,826	-12,754	6,100
4.1.1 RBI's net credit to Centre	33,374	-1,042	3,071	2,584	-12,568	5,871
4.2 Other Banks' Credit to Government	-17,910	70,046	23,378	12,879	-337	34,127
5. Bank Credit to Commercial Sector	3,61,746 (27.2)	4,30,287 (25.4)	14,930	1,39,859	76,271	1,99,227
6. Net Foreign Exchange Assets of Banking Sector	78,291	2,04,125	58,087	20,197	43,160	82,682
6.1 Net Foreign Exchange Assets of RBI	61,545	1,93,170	71,845	11,392	27,250	82,682
7. Government's Currency Liabilities to the Public	1,306	-525	-920	155	166	75
8. Net Non-Monetary Liabilities of Banking Sector	62,351	1,32,786	40,114	10,107	43,898	38,668
Memo:						
Non-resident Foreign Currency Deposits with SCBs	-16,876	6,967	3,917	1,671	1,233	145
SCBs' Call-term Borrowing from FIs	11,224	3,007	3,118	-1,576	-4,468	5,933
Overseas Borrowing by SCBs	1,295	2,543	3,301	-3,685	-2,774	5,702

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.
3. Data reflect redemption of India Millennium Deposits (IMDs) on December 29, 2005.
4. Government balances as on March 31, 2007 are before closure of accounts.

Growth in time deposits of banks accelerated to 22.8 per cent, y-o-y, as at end-March 2007 from 15.3 per cent a year ago (Chart 15) which could be attributed, *inter alia*, to higher economic activity, increase in interest rates on deposits and extension of tax benefits under Section 80C for deposits with maturity of five years and above. 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 7.25-9.50 per cent in March 2007. Rates offered by private sector banks on deposits of similar maturity increased from a range of 5.50-7.75 per cent to 6.75-9.75 per cent over the same period. Concomitantly, postal deposits, with unchanged interest rates, witnessed a deceleration in growth to 10.5 per cent in February 2007 from 17.2 per cent a year ago.

Demand for bank credit continued to remain strong during 2006-07, *albeit* with a marginal deceleration. On a year-on-year basis, scheduled commercial banks' (SCBs') non-food credit registered a growth of 28.0 per cent as at end-March 2007 on top of 31.8 per cent a year ago. The incremental credit-deposit ratio of SCBs, after remaining above/around 100 per cent for the most part between October 2004 and September 2006, has exhibited some moderation in subsequent months reflecting the combined impact of acceleration in deposit growth and modest deceleration in credit growth. As at end-March 2007, the incremental credit-deposit ratio was around 86 per cent (y-o-y) as compared with 110 per cent a year ago (Chart 16). Scheduled commercial banks' food credit rose by 14.3 per cent during 2006-07 as compared with an increase of 1.7 per cent in the previous year.

Disaggregated data available up to December 2006 show that credit growth has been largely broad-based. About 35 per cent of incremental non-food credit was absorbed by industry and another 12 per cent by agriculture. Personal loans absorbed 29 per cent of the incremental non-food credit, mainly as loans to the housing sector

Chart 15: Time Deposits Growth

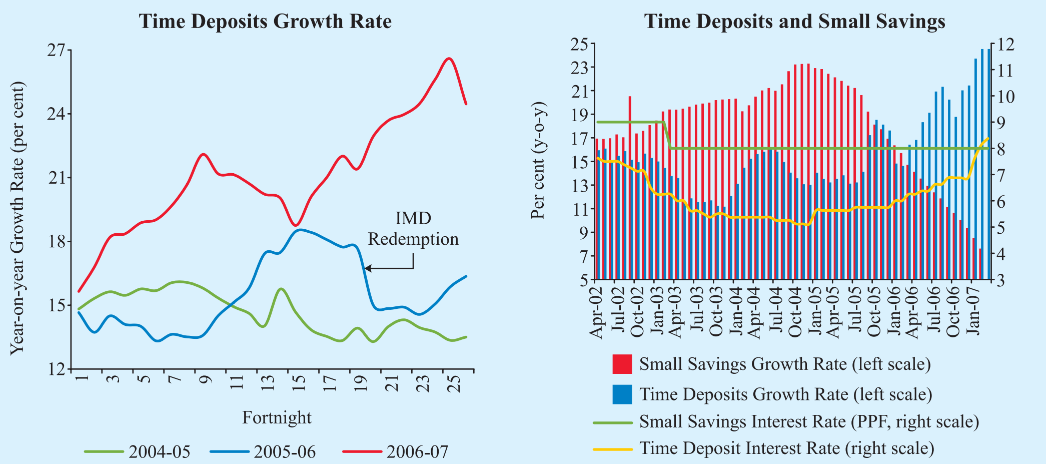
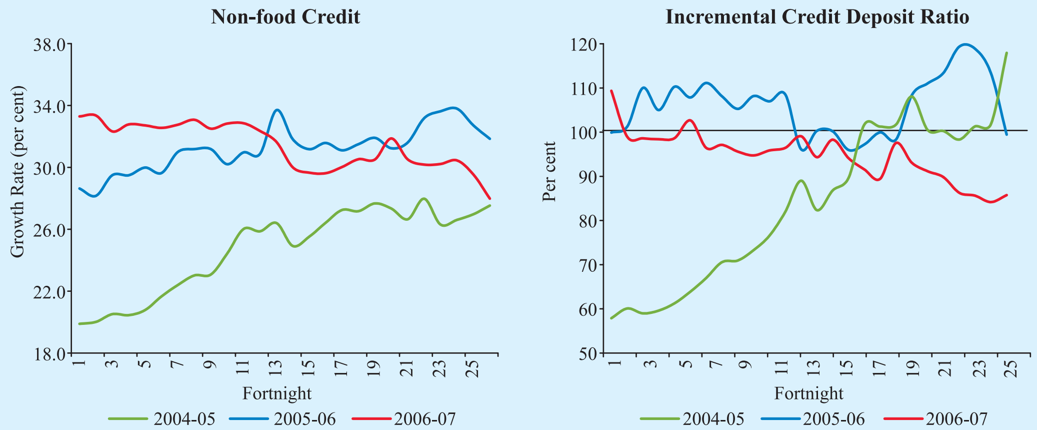


Chart 16: Scheduled Commercial Banks' Credit Growth*



*: Year-on-year basis, excluding conversion of a non-banking entity into a banking entity as on October 11, 2004.

and 'other retail loans'. Loans to commercial real estate, which increased by 66.7 per cent, y-o-y, absorbed 4.1 per cent of incremental non-food credit (Table 24). Against the backdrop of continuing high credit growth to the real estate sector, outstanding credit card receivables, loans and advances qualifying as capital market exposure and personal loans, the Reserve Bank in its Third Quarter Review (January 2007) raised provisioning requirements in respect of the standard assets in the aforesaid four categories of loans and advances (excluding residential housing loans) to two per cent from one per cent. The provisioning requirement for banks' exposures in the standard assets category to the non-deposit taking systemically important non-banking financial companies (NBFCs) was raised to two per cent from 0.4 per cent; the risk weight for banks' exposure to such NBFCs was also raised to 125 per cent from 100 per cent.

In addition to bank credit for financing their requirements, the corporate sector continued to rely on a variety of non-bank sources of funds such as capital markets, external commercial borrowings and internal funds. Resources raised through domestic equity issuances during 2006-07 (Rs.28,595 crore) were more than double of those raised in 2005-06. Mobilisation through issuances of commercial papers during 2006-07 registered a turnaround, notwithstanding some sluggishness in the second half of the year. Resources raised through markets abroad – equity issuances (ADRs/GDRs) and external commercial borrowings – also increased substantially during 2006-07. While amounts raised through ADRs/GDRs increased to Rs.16,184 crore during 2006-07 from Rs.7,263 crore a year ago, net disbursements under external commercial borrowings (ECBs) increased to Rs.48,328 crore during April-December 2006 from Rs.27,228 crore during April-December 2005. Finally, internal sources of funds continued to provide large financing support to the domestic corporate sector during the first three

Table 24: Deployment of Non-food Bank Credit

(Amount in Rupees crore)

Sector/Industry	Outstanding as on December 22, 2006	Year-on-year Variation			
		December 23, 2005		December 22, 2006	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
Non-food Gross Bank Credit (1 to 4)	**16,23,653**	**2,83,487**	**33.3**	**3,84,785**	**31.1**
1. Agriculture and Allied Activities	**1,97,763**	**41,771**	**39.6**	**46,991**	**31.2**
2. Industry (Small, Medium and Large)	**6,25,309**	**86,215**	**25.0**	**1,35,929**	**27.8**
Small Scale Industries	1,00,599	12,717	18.7	18,822	23.0
3. Personal Loans	**4,27,909**	**n.a.**	**n.a.**	**1,10,613**	**34.9**
Housing	2,17,829	n.a.	n.a.	50,622	30.3
Advances against Fixed Deposits	35,764	6.016	23.1	3,634	11.3
Credit Cards	11,913	n.a.	n.a.	3,595	43.2
Education	13,399	n.a.	n.a.	4,418	49.2
Consumer Durables	8,558	-1,084	-13.5	1,615	23.3
4. Others	**3,72,672**	**n.a.**	**n.a.**	**91,252**	**32.4**
Transport Operators	22,610	n.a.	n.a.	10,598	88.2
Professional and Others	19,379	n.a.	n.a.	6, 051	45.4
Trade	99,194	n.a.	n.a.	23,139	33.9
Real Estate Loans	39,642	14,201	155.4	15,859	66.7
Non-Banking Financial Companies	38,150	10,111	59.4	7,456	24.3
Memo:					
Priority Sector	**5,64,396**	**1,28,773**	**41.7**	**1,12,782**	**25.0**
Industry (Small, Medium and Large)	**6,25,309**	**86,215**	**25.0**	**1,35,929**	**27.8**
Food Processing	34,492	4,094	20.1	7,033	25.6
Textiles	69,305	10,891	30.7	18, 274	35.8
Paper and Paper Products	10,140	1,723	30.9	1,775	21.2
Petroleum, Coal Products and Nuclear Fuels	31,021	2,962	20.6	12,441	67.0
Chemical and Chemical Products	51,153	5,836	19.5	7,607	17.5
Rubber, Plastic and their Products	7, 979	2,660	92.4	1,950	32.3
Iron and Steel	58,896	10,391	38.2	14,877	33.8
Other Metal and Metal Products	19,727	2,821	29.6	5,737	41.0
Engineering	38,439	3,976	15.6	6,306	19.6
Vehicles, Vehicle Parts and Transport Equipments	20,272	5,319	91.5	3,771	22.9
Gems and Jewellery	21,795	4,572	42.3	3,613	19.9
Construction	16,524	2,992	38.7	4,784	40.7
Infrastructure	1,24,271	27,802	42.2	22,197	21.7

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.

quarters of 2006-07. Profits after tax of select non-financial non-government companies during April-December 2006 were almost 43 per cent higher than the corresponding period of 2005 (Table 25).

Commercial banks' investments in gilts increased by 10.0 per cent, y-o-y, as at end-March 2007 as against a decline of 2.7 per cent a year ago (Table 26). Growth in commercial banks' investments in gilts was, however, substantially below the growth of 23.5 per cent in their net demand and time liabilities (NDTL). As a result, commercial banks' holdings of Government securities declined to 28.0 per cent of their NDTL as at end-March 2007 from 31.3 per cent as at end-March 2006 (Chart 17). Excess SLR investments of SCBs fell to Rs.85,728 crore

Table 25: Select Sources of Funds to Industry

(Rupees crore)

Item	2005-06	2006-07	2006-07 Q1	Q2	Q3	Q4
1	2	3	4	5	6	7
A. Bank Credit to Industry #	1,27,192 (66,244)*	74,981*	-2,724	49,290	28,415	–
B. Flow from Non-banks to Corporates						
1. Capital Issues (i+ii)	13,781	29,180	10,627	1,882	10,840	5,831
i) Non-Government Public Ltd. Companies (a+b)	13,408	29,180	10,627	1,882	10,840	5,831
a) Bonds/Debentures	245	585	0	0	491	94
b) Shares	13,163	28,595	10,627	1,882	10,349	5,737
ii) PSUs and Government Companies	373	0	0	0	0	0
2. ADR/GDR Issues	7,263	16,184	4,965	2,130	924	8,165
3. External Commercial Borrowings (ECBs)	45,078 (27,228)*	48,328*	20,503	13,651	14,174	–
4. Issue of CPs	-1,517	6,384@	6,931	4,795	-908	-4,434@
C. Depreciation Provision +	28,883 (22,044)*	24,557*	8,449	8.892	9,172	–
D. Profit after Tax +	67,506 (52,891)*	75,460*	24,845	27,710	28,698	–

: 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 sample of non-financial non-Government companies. Quarterly variations may not add up to annual variation due to difference in coverage of companies.
* : Data pertain to April-December. @ : Up to March 15, 2007.

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.

as at end-March 2007 from Rs.1,45,297 crore as at end-March 2006. Thus, apart from higher deposit growth, excess SLR investments continued to provide banks the

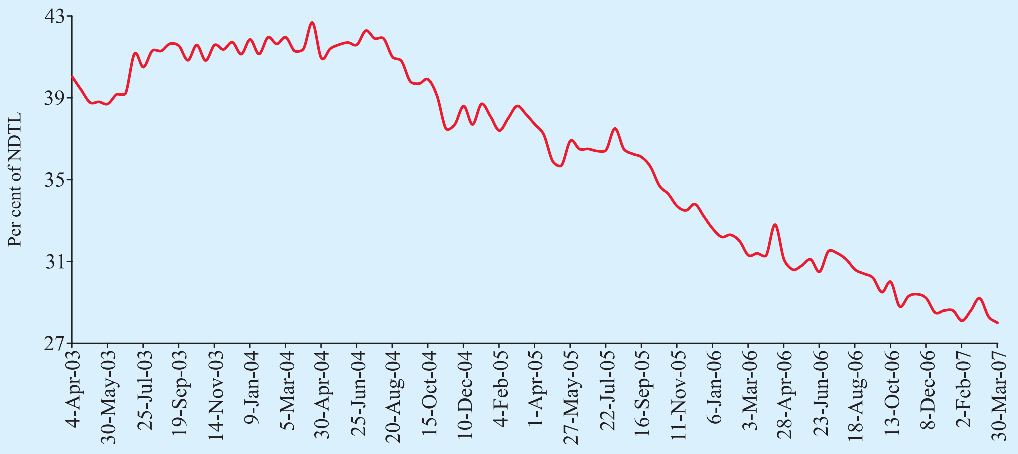
Table 26: Scheduled Commercial Bank Survey

(Amount in Rupees crore)

Item	Outstanding as on March 30, 2007	Variation (year-on-year) As on March 31, 2006 Amount	Per cent	As on March 30, 2007 Amount	Per cent
1	2	3	4	5	6
Sources of Funds					
1. Aggregate Deposits	25,94,259	3,23,913	18.1	4,85,210	23.0
2. Call/Term Funding from FIs	86,151	11,224	15.6	3,007	3.6
3. Overseas Foreign Currency Borrowings	32,377	1,295	4.5	2,543	8.5
4. Capital	33,868	5,705	21.2	1,254	3.8
5. Reserves	1,66,290	34,616	31.3	21,177	14.6
Uses of Funds					
1. Bank Credit	19,23,192	3,54,868	30.8	4,16,115	27.6
of which: Non-food Credit	18,76,672	3,54,193	31.8	4,10,285	28.0
2. Investments in Government Papers	7,71,060	-19,514	-2.7	70,318	10.0
3. Investments in Other Approved Securities	21,100	-3,295	-16.5	4,388	26.3
4. Investments in Non-SLR Securities	1,43,750	-11,838	-8.0	8,410	6.2
5. Foreign Currency Assets	39,287	14,059	47.8	-4,207	-9.7
6. Balances with the RBI	1,80,222	34,077	36.6	53,161	41.8

Note: Data are provisional.

Chart 17: SLR Investments by Scheduled Commercial Banks

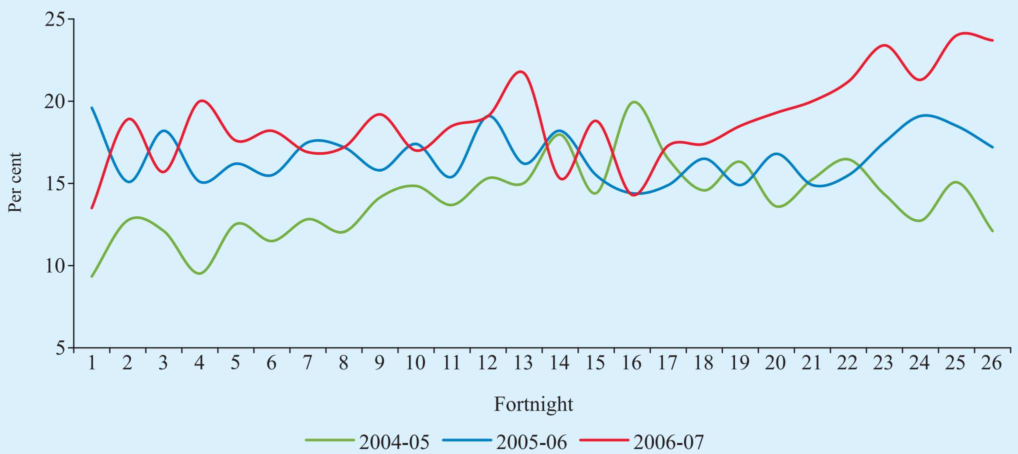


flexibility to sustain strong demand for bank credit. Banks' balances with the Reserve Bank expanded, reflecting the impact of the increase in their NDTL as well as the increase in the CRR.

Reserve Money Survey

Reserve money expanded by 23.7 per cent, y-o-y, as on March 31, 2007 as compared with 17.2 per cent a year ago (Chart 18). Adjusted for the first round effects of the hikes in the CRR, reserve money growth (y-o-y) was 18.9 per cent as on March 31, 2007.

Chart 18: Reserve Money Growth



Growth in reserve money during 2006-07 was driven largely by the expansion in the Reserve Bank's net foreign assets (NFA). The Reserve Bank's foreign currency assets (net of revaluation) increased by Rs.1,64,601 crore during 2006-07 as compared with an increase of Rs.68,834 crore during the previous year (Table 27 and Chart 19). More than one-half of the increase in the Reserve Bank's foreign currency assets (net of revaluation) during 2006-07 took place in the fourth quarter.

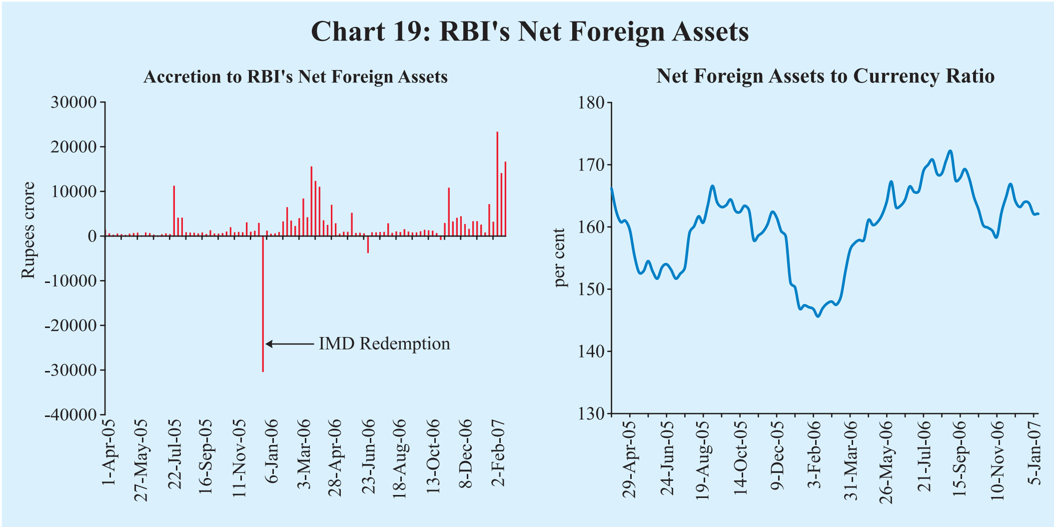
Table 27: Reserve Money

(Rupees crore)

	Outstanding as on March 31, 2007	Variation during					
		2005-06	2006-07	2006-07			
				Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8
Reserve Money (= 1+2+3 = 4+5+6+7-8)	7,08,950	83,922 (17.2)	1,35,892 (23.7)	13,470	18,666	14,210	89,546
Components							
1. Currency in Circulation	5,04,167	62,015 (16.8)	73,491 (17.1)	22,283	-2,011	26,871	26,348
2. Bankers' Deposits with RBI	1,97,295	21,515 (18.9)	61,784 (45.6)	-7,204	20,224	-12,165	60,929
3. 'Other' Deposits with the RBI	7,487	393 (6.1)	617 (9.0)	-1,610	453	-495	2,269
Sources							
4. RBI's net credit to Government	4,362	26,111	-3,775	53	2,826	-12,754	6,100
of which: to Centre (i+ii+iii+iv-v)	4,118	28,417	-1,042	3,071	2,584	-12,568	5,871
i. Loans and Advances	0	0	0	0	0	0	0
ii. Treasury Bills held by the RBI	0	0	0	0	0	0	0
iii. RBI's Holdings of Dated Securities	97,172	13,869	26,763	-27,610	24,944	22,733	6,696
iv. RBI's Holdings of Rupee coins	12	7	-143	9	-107	97	-142
v. Central Government Deposits	93,066	-14,541	27,662	-30,672	22,253	35,398	683
5. RBI's credit to banks and commercial sector	9,173	535	1990	-3,135	3,107	2,065	-47
6. NFEA of RBI	8,66,153	60,193 (9.8)	1,93,170 (28.7)	71,845	11,392	27,250	82,682
of which : FCA, adjusted for revaluation	–	68,834	1,64,601	28,107	10,948	31,634	93,913
7. Governments' Currency Liabilities to the Public	8,229	1,306	-525	-920	155	166	75
8. Net Non-Monetary liabilities of RBI	1,78,967	4,222	54,968	54,373	-1,186	2,517	-736
Memo:							
Net Domestic Assets	-1,57,203	23729	-57277	-58,376	7,274	-13,040	6,864
Reserve Bank's Primary Subscription to Dated Securities	0	10,000	0	0	0	0	0
LAF, Repos (+) / Reverse Repos (-)	29,185	12,080	36,435	-23,060	28,395	22,195	8,905
Net Open Market Sales # *	–	3,913	5,125	1,536	1,176	389	2,024
Mobilisation under MSS *	62,974	-35,149	33,912	4,062	8,940	-3,315	24,225
Net Purchases(+)/Sales(-) from Authorised Dealers	–	32,884	1,07,347@	21,545	0	19,776	66,026@
NFEA/Reserve Money £	122.2	117.4	122.2	127.0	125.0	126.5	122.2
NFEA/Currency £	171.8	156.3	171.8	164.4	167.7	164.0	171.8

NFEA: Net Foreign Exchange Assets. FCA : Foreign Currency Assets. @: up to end-February 2007.
*: At face value. # : Excludes Treasury Bills £ : per cent, end of period.

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.
3. Government balances as on March 31, 2007 are before closure of accounts.



Mirroring the liquidity management operations, the Reserve Bank's net credit to the Centre declined by Rs.1,042 crore in 2006-07 as against an increase of Rs.28,417 crore in the previous year. The decline in net RBI credit to the Centre during 2006-07 could be attributed mainly to an increase in balances under MSS (Rs.33,912 crore) and open market sales (Rs.5,125 crore), partly offset by increase in repo balances under LAF (Rs.36,435 crore).

Liquidity Management

During 2006-07, the Reserve Bank continued with its policy of active management of liquidity through open market operations (OMO) including MSS, LAF and CRR, and using all the policy instruments at its disposal flexibly. The liquidity management operations during the year were aimed at ensuring maintenance of appropriate liquidity in the system so that all legitimate requirements of credit, particularly for productive purposes, are met, consistent with the objective of price and financial stability. However, the task of liquidity management was complicated during 2006-07, with greater variation in market liquidity, largely reflecting variations in cash balances of the Governments and capital flows.

During the first quarter of 2006-07, unwinding of the Centre's surplus balances with the Reserve Bank and the Reserve Bank's purchase of foreign exchange from authorised dealers resulted in ample liquidity into the banking system. This was mirrored in an increase in the LAF reverse repo balances. Liquidity conditions continued to remain easy during the most part of the second quarter of 2006-07. Balances under the MSS also rose between May 2006 and September 2006, following the re-introduction of auctions under the MSS in May

2006. However, in view of some build-up of Government cash balances with the Reserve Bank during August-September 2006, there was a decline in balances under LAF reverse repos during the second quarter (Table 28).

Around mid-September 2006, liquidity conditions turned tight on account of advance tax outflows and festival season currency demand. The Reserve Bank, accordingly, injected liquidity through repos on eight occasions between mid-September 2006 and end-October 2006. However, there was net injection of liquidity only on two occasions (October 20 and October 23, 2006). Liquidity pressures eased by end-October 2006 following some decline in Government cash balances (Table 29). Liquidity conditions eased further during November 2006, partly reflecting purchases of foreign exchange by the Reserve Bank. Balances under LAF reverse repos started rising from the third week of November 2006, reaching Rs 34,255 crore as on December 6, 2006 (Chart 20).

Liquidity conditions, however, again turned tight from the second week of December 2006 largely due to advance tax outflows and announcement of increase in the CRR by 50 basis points. The Centre's surplus with the Reserve Bank increased from Rs.31,305 crore at end-November 2006 to Rs.73,534 crore as on December 22, 2006. In view of the prevailing liquidity conditions, the Reserve Bank injected liquidity into the system through repo operations from December 13,

Table 28: Reserve Bank's Liquidity Management Operations

(Rupees crore)

Item	2005-06	2006-07	2006-07						
			Q1	Q2	Q3	Q4	Jan.	Feb.	Mar.
1	2	3	4	5	6	7	8	9	10
A. Drivers of Liquidity (1+2+3+4)	**-31,696**	**60,981**	**36,247**	**-16,683**	**-25,903**	**67,320**	**22,708**	**26,744**	**17,868**
1. RBI's Foreign Currency Assets (adjusted for revaluation)	68,834	1,64,601	28,517	10,538	34,821	90,725	13,304	56,780	20,641
2. Currency with the Public	-57,256	-71,052	-19,648	-1,058	-27,296	-23,050	-10,306	-10,283	-2,461
3. Surplus Cash balances of the Centre with the Reserve Bank	-22,726	-1,164	40,207	-26,199	-30,761	15,590	23,088	-10,621	3,123
4. Others (residual)	-20,547	-31,405	-12,828	36	-2,667	-15,945	-3,379	-9,131	-3,435
B. Management of Liquidity (5+6+7+8)	**57,969**	**-24,257**	**-39,003**	**32,026**	**31,625**	**-48,905**	**-29,051**	**-28,817**	**8,963**
5. Liquidity impact of LAF Repos	12,080	36,435	-35,315	40,650	33,600	-2,500	-20,240	-18,385	36,125
6. Liquidity impact of OMO (Net) *	10,740	720	545	145	25	5	0	0	5
7. Liquidity impact of MSS	35,149	-33,912	-4,232	-8,769	4,750	-25,660	-2,061	-3,432	-20,167
8. First round liquidity impact due to CRR change	0	-27,500	0	0	-6,750	-20,750	-6,750	-7,000	-7,000
C. Bank Reserves (A+B) #	**26,273**	**36,724**	**-2,756**	**15,343**	**5,722**	**18,415**	**-6,343**	**-2,073**	**26,831**

(+) : 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.

Table 29: Liquidity Management

(Rupees crore)

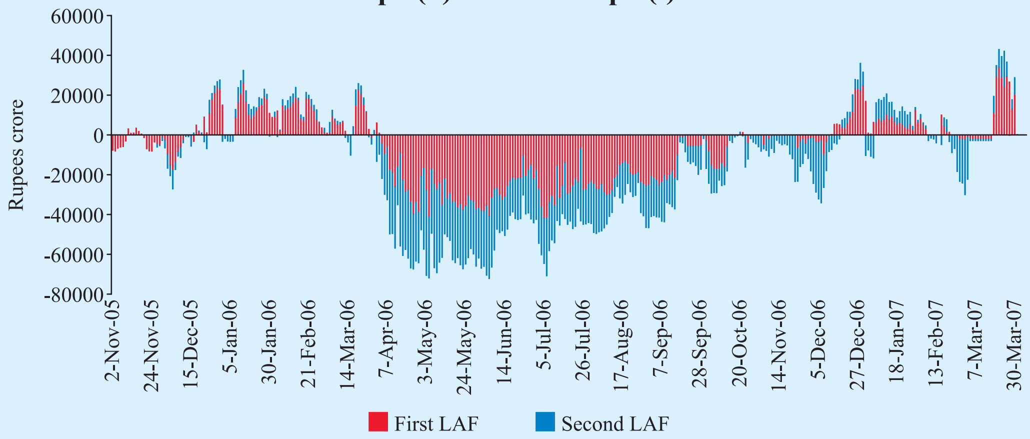
Outstanding as on last Friday of	LAF	MSS	Centre's Surplus with the RBI @	Total (2 to 4)
1	2	3	4	5
2005				
March*	19,330	64,211	26,102	1,09,643
April	27,650	67,087	6,449	1,01,186
May	33,120	69,016	7,974	1,10,110
June	9,670	71,681	21,745	1,03,096
July	18,895	68,765	16,093	1,03,753
August	25,435	76,936	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
2007				
January	-11,445	39,375	42,494	70,424
February	6,940	42,807	53,115	1,02,862
March*	-29,185	62,974	49,992	83,781

@ : 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.

2006. Average daily net injection of liquidity by the Reserve Bank amounted to Rs.15,013 crore during December 13-29, 2006 in contrast to the average daily

Chart 20: Repo (+)/ Reverse Repo (-) under LAF



Note: Additional LAF on March 31, 2006 and March 31, 2007 are shown under second LAF.

absorption of Rs.12,262 crore and Rs.9,937 crore during October and November 2006, respectively. Concomitantly, balances under the MSS declined during September-December 2006 in view of under-subscription in some of the auctions.

Although the Centre's surplus declined during January 2007, liquidity conditions remained tight, partly reflecting the impact of the CRR hike. The Reserve Bank continued to inject liquidity through LAF operations during January 2007 (except for January 3-5, when there were net absorption of liquidity). Daily net injection of liquidity averaged Rs.10,738 crore during January 2007.

Liquidity conditions eased from the second week of February 2007, partly reflecting the purchases of foreign exchange from authorised dealers. LAF window witnessed net absorption of liquidity during February 8 - March 4, 2007 (except during February 15-20, 2007). Taking into account, *inter alia*, the liquidity conditions, the Reserve Bank, on February 13, 2007, announced another increase of 50 basis points in the CRR – 25 basis points each – effective in the fortnights beginning February 17, 2007 and March 3, 2007. Furthermore, on a review of the liquidity conditions, the Reserve Bank on March 2, 2007 announced modifications in liquidity management operations. An enhanced MSS programme was put in place to restore LAF as a facility for equilibrating very short-term mismatches and modulating the liquidity it absorbs through the daily reverse repo auctions. It was decided to use a mix of Treasury Bills and dated securities for MSS issuances in a more flexible manner keeping in view the capital flows in the recent period, the assessment of volatility and durability of capital flows, and the paramount importance attached to liquidity management in containing inflation. Concomitantly, beginning March 5, 2007, daily reverse repo absorptions were restricted to a maximum of Rs.3,000 crore comprising Rs.2,000 crore in the First LAF and Rs.1,000 crore in the Second LAF. Reflecting the modified arrangements, the balances under the LAF remained at around Rs.3,000 crore during March 5-15, 2007 while those under the MSS increased from Rs.42,807 crore at end-February 2007 to Rs.62,974 crore by March 31, 2007.

Liquidity conditions tightened from March 16, 2007 in view of advance tax outflows, the concomitant increase in the Centre's surplus from Rs.36,476 crore as on March 9, 2007 to Rs.77,006 crore as on March 23, 2007 and the effect of the CRR hike. Accordingly, the Reserve Bank injected liquidity through repo operations, averaging Rs.31,254 crore during March 16-30, 2007. On March 21, 2007, the Reserve Bank clarified that the recourse to LAF by market participants should not be persistent in order to fund balance sheets for credit needs of customers, but banks could utilise the funds borrowed under this facility for inter-bank lending. Such inter-bank lending is part of normal money market functioning and enables daily liquidity management by market participants with temporary mismatches. At the request of the market participants, the Reserve Bank conducted an additional LAF auction between 3.30 PM and 4.00 PM on March 31, 2007.

Liquidity conditions eased in early April 2007, partly on account of the reduction in the Centre's surplus. Balances under LAF repos, net of reverse repos, fell from Rs.29,185 crore as on March 31, 2007 to Rs.1,455 crore as on April 8, 2007. During April 9-15, 2007, there was net absorption of liquidity. Absorptions under the reverse repo remained limited to a maximum of Rs.3,000 crore in accordance with the modified arrangements. There was again net injection of liquidity during April 16-18, 2007, averaging Rs.16,988 crore daily.

IV. PRICE SITUATION

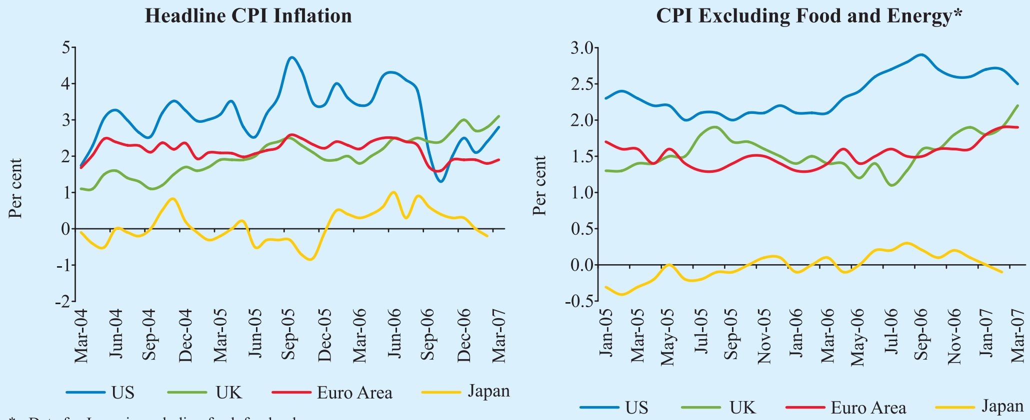
Headline and core inflation remained at elevated levels in many economies during the first half of 2006-07 reflecting high commodity prices and strong demand conditions. Although headline inflation eased somewhat from August 2006 levels in tandem with the softening of international crude oil prices and favourable base effects, it remains above the inflation targets/comfort zones 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. Amongst advanced economies, the European Central Bank (ECB), the Bank of England, the Reserve Bank of Australia and the Bank of Japan raised their policy rates during 2006-07. The US Fed, however, has left its rate unchanged since end-June 2006 in view of some slowing down of economic activity. Amongst emerging economies, central banks such as the South African Reserve Bank, the People's Bank of China, the Bank of Korea and the Central Bank of the Republic of Turkey raised their policy rates during 2006-07. Central banks in emerging market economies such as Korea, China and Russia also raised cash reserve requirements to address concerns regarding excess liquidity arising, particularly from large external flows. Some other central banks such as the Bank of Thailand and the Bank of Israel changed direction over the course of the year - raising rates initially and then cutting them to support growth.

In India, prices of primary food articles and manufactured products exerted upward pressures on headline inflation in 2006-07. Wholesale price inflation was generally within the Reserve Bank's indicative projections of 5.0-5.5 per cent up to mid-November 2006 and rose above the upper end of the band thereafter. The year-on-year (y-o-y) inflation was 5.7 per cent as on March 31, 2007 as compared with 4.0 per cent a year ago. Measures of consumer price inflation remained above the WPI inflation throughout the year, mainly reflecting the impact of higher food prices. The Reserve Bank continued with the policy of gradual withdrawal of monetary accommodation, using various instruments at its disposal flexibly to stabilise inflationary expectations, while continuing to pursue the medium term goal of a ceiling on inflation at 5.0 per cent. The Government also took fiscal and supply-side measures to contain inflation.

Global Inflation

Headline inflation in major advanced economies remained firm till August 2006 in tandem with crude oil prices reaching record highs. It 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 December 2006-March 2007 (Chart 21). Consumer price inflation in the OECD countries rose from 2.5 per cent

Chart 21: Consumer Price Inflation

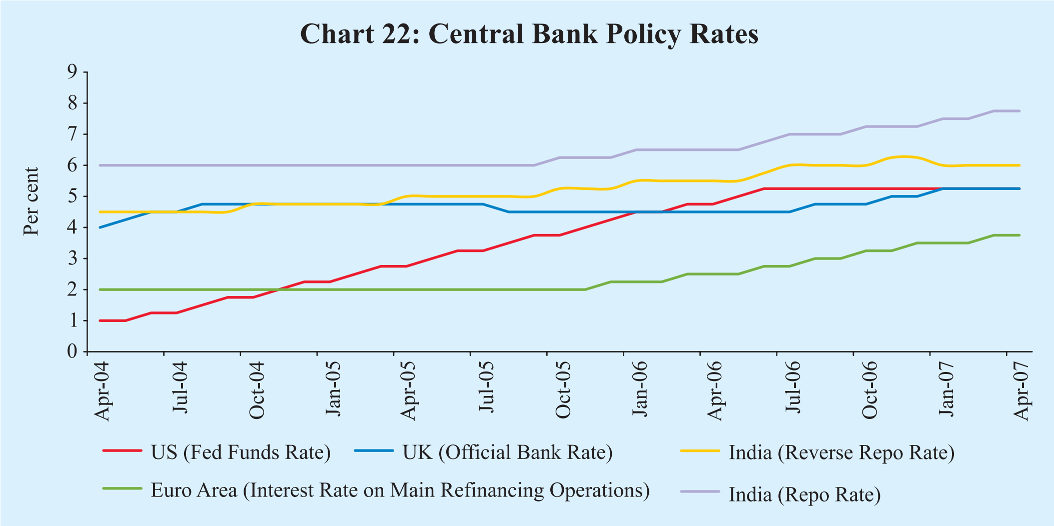


* : Data for Japan is excluding fresh food only.
Source: International Financial Statistics and official websites of respective countries.

in March 2006 to a peak of 3.1 per cent in June 2006 before moderating to 2.1 per cent in February 2007. Amongst major economies, headline inflation in the US rose from 3.4 per cent in March 2006 to 4.3 per cent in June 2006. Although it has since moderated to 2.8 per cent in March 2007, it remains at elevated levels. In the UK, CPI inflation increased to 3.1 per cent in March 2007 from 1.8 per cent a year ago. In the euro area, inflation remained above the target of 'below but close to 2.0 per cent' till August 2006, and moderated thereafter to 1.9 per cent in March 2007. Notwithstanding some moderation in headline inflation, core inflation still remains firm in major economies. CPI inflation (excluding food and energy) was 2.5 per cent in the US in March 2007 (2.1 per cent a year ago) and 2.1 per cent in the OECD countries in February 2007 (1.6 per cent a year ago). 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.

After having raised its target federal funds rate by 425 basis points since the tightening began in June 2004, the US Fed has paused at each of the meetings held since end-June 2006 (Chart 22). Economic growth moderated in the second half of 2006, partly reflecting a cooling of the housing market. Core inflation remains at elevated level. The Federal Open Market Committee in its latest meeting held on March 21, 2007 noted that the risk that inflation will fail to moderate as expected remains the predominant policy concern. It indicated that future policy adjustments 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 since August 2006, risks to the price outlook are seen on the upside due to the possibility of



further oil price rises, 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 on five occasions during 2006-07 (June 2006, August 2006, October 2006, December 2006 and March 2007). The policy rate has been increased by 175 basis points since the tightening began in December 2005 (Table 30). Given the favourable economic environment, the ECB is of the view that monetary policy continues to be on the accommodative side, with the key interest rates moderate, money and credit growth vigorous, and liquidity in the euro area ample by all plausible measures.

In view of strong economic activity, limited spare capacity, rapid growth of broad money and credit, 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 Bank of Japan (BoJ), after maintaining zero interest rates for an extended period, raised the uncollateralised overnight call rate (the operating target of monetary policy since March 2006) by 25 basis points each on two occasions - July 2006 and February 2007 - during the year to 0.50 per cent. The BoJ believes that monetary environment still remains very accommodative. With regard to the future course of monetary policy, the Bank of Japan has stated that it will adjust the level of interest rates gradually in the light of developments in economic activity and prices, while maintaining the accommodative financial conditions ensuing from very low interest rates for some time. Amongst other major advanced economies, central banks in Australia, Norway and New Zealand raised their policy rates during 2006-07.

Table 30: Global Inflation Indicators

(Per cent)

Country/ Region	Key Policy Rate	Policy Rates (As on April 18, 2007)	Changes in Policy Rates (basis points)		CPI Inflation (y-o-y)		Growth (y-o-y)	
			Since end-March 2005	Since end-March 2006	2006 (Mar.)	2007 (Mar.)	2005 (Q4)	2006 (Q4)
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 $	2.7	2.8
Canada	Overnight Rate	4.25 (May 24, 2006)	175	50	2.2	2.0 *	2.9	2.3
Euro area	Interest Rate on Main Refinancing Operations	3.75 (Mar. 8, 2007)	175	125	2.2	1.9	1.7	3.3
Japan	Uncollateralised Overnight Call Rate	0.50 (Feb. 21, 2007)	**	50	-0.1	-0.2 *	4.0	2.3
UK	Official Bank Rate	5.25 (Jan. 11, 2007)	50	75	1.8	3.1	1.8	3.0
US	Federal Funds Rate	5.25 (June 29, 2006)	250	50	3.4	2.8	3.2	3.1
Developing Economies								
Brazil	Selic Rate	12.50 (Apr. 18, 2007)	(-)675	(-)400	5.3	3.0	1.4	3.8
India	Reverse Repo Rate	6.00 (July 25, 2006)	125	50	4.9	7.6 *	9.3	8.6
	Repo Rate	7.75 (Mar. 30, 2007)	175 (150)	150 (150)				
China	Benchmark 1-year Lending Rate	6.39 (Mar. 18, 2007)	81 (300)	81 (300)	0.8	3.3	10.4	11.1 £
Indonesia	BI Rate	9.00 (Mar. 6, 2007)	50 @	(-)375	15.8	6.5	4.9	6.1
Israel	Key Rate	4.00 (Feb. 26, 2007)	50	(-)75	3.1	0.8 *	4.8	3.7
Korea	Overnight Call Rate	4.50 (Aug. 10, 2006)	125 (80)	50 (80)	2.0	2.2	5.3	4.0
Philippines	Reverse Repo Rate	7.50 (Oct. 20, 2005)	75	0	7.6	2.2	6.1	6.5
Russia	Refinancing Rate	10.50 (Jan. 29, 2007)	-250 (150)	-150 (150)	10.6	7.1	7.0	7.7
South Africa	Repo Rate	9.00 (Dec. 8, 2006)	150	200	3.9	5.7 *	4.5	6.1
Thailand	14-day Repurchase Rate	5.00 (June 7, 2006)	275	50	5.7	2.0	4.7	4.2
	1-day Repurchase Rate	4.00 (Apr. 11, 2007)	–	(-)94 ^				

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

* : February 2007. $: Q4 of 2006. £ : Q1 of 2007.

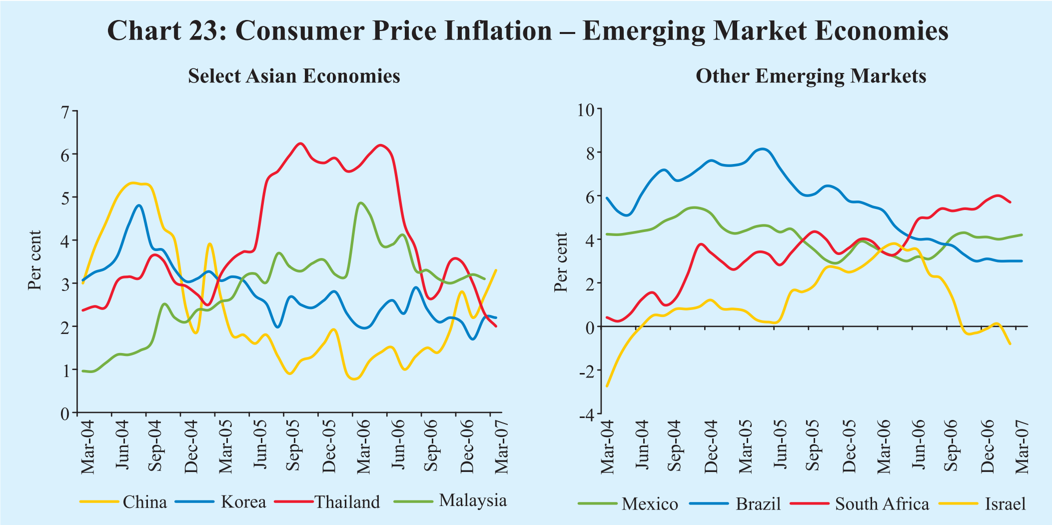
** : The Bank of Japan decided on March 9, 2006 to change the operating target of money market operations from the outstanding balance of current accounts at the Bank to the uncollateralised overnight call rate.

^ : 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.
3. Figures in parentheses in columns (4) and (5) give the variation in cash reserve ratios during the period.

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

Inflation remains relatively modest in several economies in Asia, reflecting both pre-emptive monetary tightening as well as appreciation of the exchange rates. Consumer price inflation in China increased to 3.3 per cent in March 2007 from 0.8 per cent a year ago, partly on the back of higher food prices (Chart 23). Real GDP growth accelerated to 10.7 per cent in 2006 from 10.4 per cent in the previous year. Growth in fixed investment decelerated in 2006, but still remains



large. The economic activity has remained buoyant in 2007 so far. Real GDP growth accelerated to 11.1 per cent during the first quarter of 2007 from 10.4 per cent a year ago. Owing to persistent BOP surplus, excess liquidity has built up in the banking sector, and loan expansion remains fairly large. In view of strong growth in money supply and credit, the People's Bank of China (PBC) increased the benchmark 1-year lending rate by 27 basis points each in April 2006, August 2006 and March 2007. Apart from continued issuances of its own bills to mop up liquidity, the PBC has also raised the cash reserve ratio by 300 basis points since July 2006 in six steps (50 basis points each effective July 5, 2006, August 15, 2006, November 15, 2006, January 15, 2007, February 25, 2007 and April 16, 2007) to 10.50 per cent. The monetary measures were supported by 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 a 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.

In Korea, real GDP growth moderated to 4.0 per cent in the quarter ended December 2006 from 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, in view of sharp growth in monetary and credit aggregates, and financial institutions' liquidity, led by inflows of foreign funds, the Bank of Korea increased the cash reserve ratio on demand deposits and money market deposit accounts from 5.0 per cent to 7.0 per cent, effective December 23, 2006. The reserve requirement on time deposits, various 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 rose from 3.0 per cent to 3.8 per cent. In response to these measures, the Bank of Korea expects that the pace of liquidity expansion will slow and the short-term bias of financial institutions' deposit structures will lessen.

In Thailand, real GDP growth was 4.2 per cent in the quarter ended December 2006 as compared with 4.7 per cent a year ago. In the first quarter of 2007, domestic demand slowed down led by private consumption and investment. Inflationary pressures are expected to moderate. Therefore, the Bank of Thailand has since January 17, 2007 lowered the 1-day repurchase rate (which replaced the 14-day repurchase rate as the policy rate) by 94 basis points to 4.00 per cent on April 11, 2007. The Bank of 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.

In Indonesia, economic activity gradually regained momentum during 2006, driven primarily by rapidly expanding exports and also by domestic consumption. Inflation, which had reached 18.4 per cent in November 2005, eased sharply to 6.5 per cent in March 2007 reflecting monetary policy actions as well as the easing of oil prices and the base effect. Bank Indonesia has, therefore, cut its policy rate by 375 basis points since May 2006 to 9.00 per cent in March 2007 to support growth. The policy rate was earlier raised by 425 basis points during July-December 2005 to contain inflation.

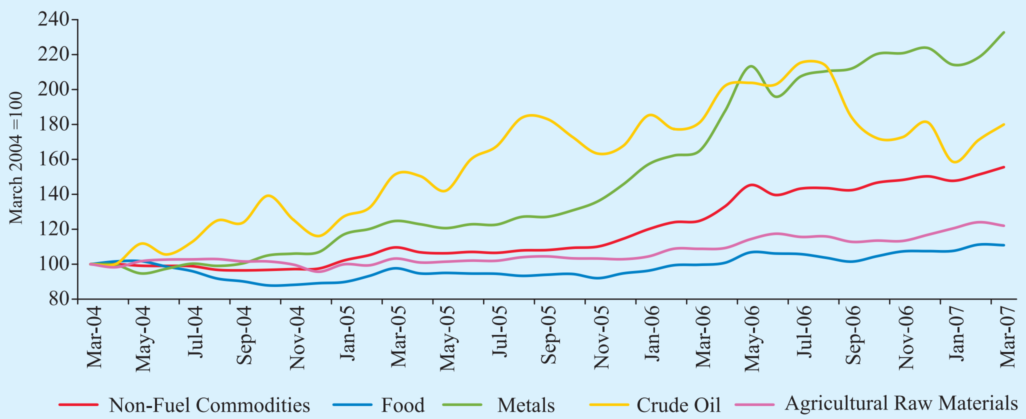
Amongst other emerging economies, the South African Reserve Bank raised the policy rate by 200 basis points - 50 basis points each in June, August, October and December 2006 - to 9.0 per cent to contain inflationary pressures emanating from volatility in oil prices and from food and services prices. 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 by 725 basis points since September 2005 to 12.50 per cent on April 18, 2007. The Bank of Israel has cut its policy rate by 150 basis points since October 2006 (25 basis points each in October and November 2006, 50 basis points in December 2006, 25 basis points each in January 2007 and February 2007) to 4.00 per cent to support growth, after having raised rates by 200 basis points between September 2005 and August 2006. In Russia, consumer price inflation remains high, although it eased somewhat to 7.1 per cent in March 2007 from 10.6 per cent a year ago. Money supply (M2) growth accelerated to 50.4 per cent, year-on-year, as on March 1, 2007 from 37.3 per cent a year ago. The Bank of Russia raised the required reserve ratio on credit institutions' liabilities to non-resident banks in rubles and foreign currency from 2.0 per cent to 3.5 per cent on October 31, 2006. It has, however, reduced the refinancing rate by 150 basis points - 50 basis points each on three occasions - from 12.0 per cent in December 2005 to 10.5 per cent in January 2007.

Global Commodity Prices

Non-fuel commodity prices firmed up during 2006-07 led by metals and food prices. Crude oil prices rose sharply in the first four months of 2006-07 to reach a record high but witnessed a sharp correction thereafter; on a year-on-year basis, prices were broadly unchanged in March 2007. Metals prices recorded large gains, especially during April 2006 up to mid-May 2006, on the back of robust demand in emerging economies, especially China. Food prices, led by wheat and edible oil, rose reflecting a shortfall in global production (Chart 24).

International crude oil prices (WTI) exhibited large intra-year volatility during 2006-07. Prices initially firmed up to reach a record high of US $ 78.4 a barrel on July 14, 2006 on concerns over Iran's nuclear programme and unrest in Nigeria, amidst limited spare capacity. Subsequently, prices eased to below US $ 60 a barrel during October-November 2006 on the back of signs of slowdown of the US economy, increased US stocks and easing of tension over Iran's nuclear programme (Tables 31 and 32). Prices edged up to around US $ 62-63 a barrel in December 2006 on

Chart 24: International Commodity Prices



Source: International Monetary Fund.

Table 31: 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
2006-07	60.9	64.4	64.7	63.3	62.4
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	69.5	68.0	66.8
May 2006	64.9	70.2	70.9	68.6	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	62.0	61.1
October 2006	56.5	58.4	58.9	58.0	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
January 2007	52.0	54.3	54.2	53.5	53.0
February 2007	55.7	57.8	59.3	57.6	56.6
March 2007	59.1	62.1	60.6	60.6	60.4

Source : International Monetary Fund and the World Bank.

the back of 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 balance supply and demand to support prices. Nonetheless, prices eased further to US $ 51 a barrel in January 2007 mainly on account of mild winter in the US and rise in the US stocks. Prices, however, rebounded in the last week of January 2007 and reached US $ 60 a barrel in February 2007 on the back of renewed winter demand and the second production cut of 0.5 mb/d by OPEC, effective February 1, 2007. Prices rose further to around US $ 67 in late March 2007 on tensions over Iran's detention of British naval personnel. Prices eased to US $ 64 a barrel by April 5, 2007 on the release of the British naval personnel.

Metals prices remained firm during 2006-07 on the back of robust demand and supply constraints amidst speculative investor interest. After witnessing a steady rise since late 2004 and, in particular, sharp rise during April 2006 and early May 2006, global metal prices witnessed sharp correction in mid-May 2006 on fears that further tightening by the US might slow down demand for metals. Prices have since then been largely range-bound, with intermittent episodes of corrections reflecting incoming information on global growth prospects. Some metals such as lead, nickel and tin registered large gains during 2006-07. Prices of aluminium, copper, tin and zinc during March 2007 were higher by about 14

Table 32: World Supply-Demand Balance of Oil

(Million barrels per day)

Item	2003	2004	2005	2006	2007 (P)	2008 (P)	2007 P Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8	9	10	11
Demand										
1. OECD	48.7	49.5	49.6	49.1	49.6	49.9	50.4	48.2	49.3	50.5
2. Non-OECD	31.2	33.0	34.4	35.4	36.5	37.8	35.9	36.0	36.5	37.5
of which: China	5.6	6.5	6.9	7.3	7.7	8.2	7.4	7.7	7.7	8.0
3. Total (1+2)	79.9	82.5	84.0	84.6	86.1	87.7	86.3	84.2	85.8	88.0
Supply										
4. Non-OPEC	48.9	50.1	50.3	49.3	50.0	50.8	49.6	49.7	50.1	50.5
5. OPEC	30.7	32.9	34.2	35.2	35.4	36.9	34.6	34.9	36.0	36.2
6. Total (4+5)	79.6	83.1	84.5	84.5	85.4	87.6	84.2	84.6	86.1	86.7
Stock Changes	0.3	-0.6	-0.5	0.1	0.7	0.0	2.1	-0.3	-0.4	1.2

P: Projections.
Source : US Energy Information Administration.

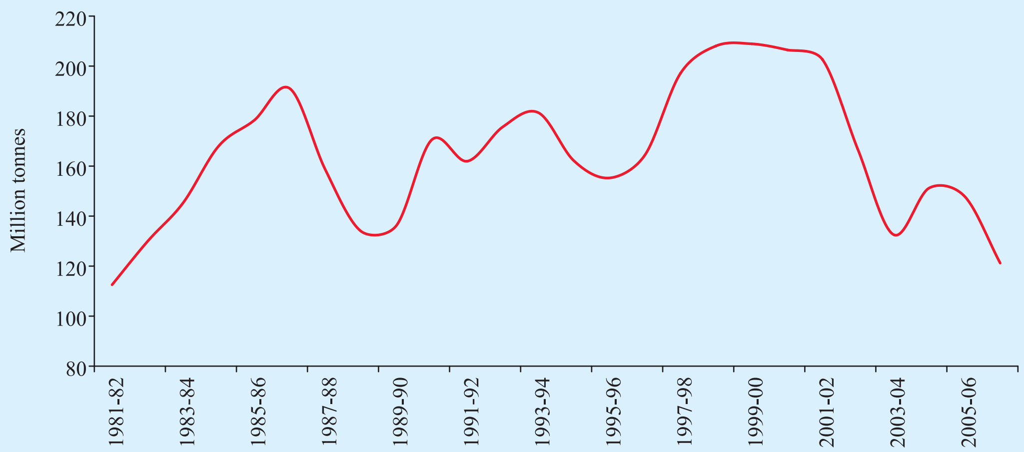
per cent, 26 per cent, 75 per cent and 35 per cent, respectively, over their levels a year ago while nickel prices nearly trebled. International steel prices declined during the year (Table 33).

Table 33: International Commodity Prices

Commodity	Unit	2004	Index 2004	2005	2006	2006-07 Apr.-Jun.	Jul.-Sept.	Oct.-Dec.	Jan.-Mar.	2007 March	Variation (per cent) (Mar. 2007 over Mar. 2006)
1	2	3	4	5	6	7	8	9	10	11	12
Energy											
Coal	$/mt	53.0	100.0	89.8	92.6	99.2	94.9	87.9	100.2	104.2	11.0
Crude oil (Average)	$/bbl	37.7	100.0	141.6	170.6	181.2	182.5	156.5	151.7	160.7	-0.5
Non-Energy Commodities											
Palm oil	$/mt	471.3	100.0	89.6	101.5	93.1	104.5	115.8	129.2	132.0	41.4
Soybean oil	$/mt	616.0	100.0	88.5	97.2	93.6	100.7	107.5	115.2	116.6	33.2
Soybeans	$/mt	306.5	100.0	89.6	87.6	86.0	86.1	94.6	103.7	105.1	25.8
Rice	$/mt	237.7	100.0	120.4	128.3	129.4	131.4	126.5	133.3	135.7	6.3
Wheat	$/mt	156.9	100.0	97.1	122.4	120.8	125.0	133.0	126.4	126.9	14.2
Sugar	c/kg	15.8	100.0	138.0	206.3	231.0	193.7	162.7	148.7	145.6	-39.7
Cotton A Index	c/kg	136.6	100.0	89.1	92.8	89.2	93.7	93.6	94.4	94.4	-0.3
Aluminium	$/mt	1716.0	100.0	110.6	149.8	154.6	144.6	158.7	163.2	161.0	13.7
Copper	$/mt	2866.0	100.0	128.4	234.5	251.6	267.6	246.6	207.0	225.1	26.4
Gold	$/toz	409.2	100.0	108.7	147.7	153.3	151.9	150.2	158.9	160.0	17.6
Silver	c/toz	669.0	100.0	109.7	172.9	183.3	174.7	188.8	199.1	196.7	26.8
Steel cold-rolled coil/sheet	$/mt	607.1	100.0	120.8	114.3	109.8	115.3	108.4	107.1	107.1	-13.3
Steel hot-rolled coil/sheet	$/mt	502.5	100.0	126.0	119.4	117.8	119.4	111.1	109.5	109.5	-15.4
Tin	c/kg	851.3	100.0	86.7	103.1	100.2	101.6	121.4	149.5	163.2	75.0
Zinc	c/kg	104.8	100.0	131.8	312.5	314.1	320.9	401.1	329.8	312.1	35.3

$: US dollar. c : US cent. bbl : barrel. mt : metric tonne. kg : Kilogram. toz: troy oz.
Source : Based on World Bank's actual commodity price data. The year 2004 has been taken as the base to better exhibit price trends over the relevant period.

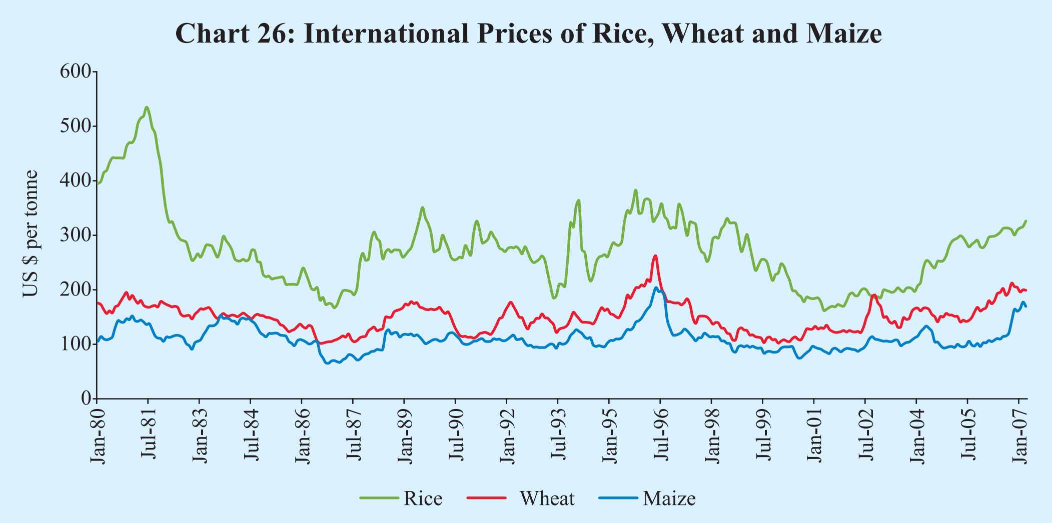
Chart 25: Global Wheat Stocks



Food prices firmed up led by wheat and edible oils on reports of shortfalls in production and increased demand for non-food uses. According to the latest assessment by the Food and Agriculture Organisation (FAO)/US Department of Agriculture (USDA), global wheat production is expected to decline by 4.4 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 about 18 per cent to 121 million tonnes by the end of 2006-07 season. At this level, the stocks of wheat will be the lowest since 1981-82 (112.5 million tonnes) (Chart 25). In view of these developments, wheat prices have firmed up since the second half of 2005. After some easing between November 2006 and January 2007, wheat prices again firmed up in February 2007. Prices in March 2007 were higher by about 14 per cent on a year-on-year basis (Chart 26). Rice production is also expected to decline during 2006-07, *albeit* marginally (by 0.4 per cent) resulting in a drawdown of stocks by 0.6 per cent. After showing signs of softness during October-November 2006, rice prices again firmed up from December 2006. Prices in March 2007 were higher by about 6 per cent on a year-on-year basis.

Prices of oilseeds and edible oils edged up sharply in the second half of 2006-07, *inter alia*, due to lower production coupled with strong demand for non-food uses such as fuels and as feedstock for bio-diesel production. On a year-on-year basis, soybean, soybean oil and palm oil prices in March 2007 were higher by 26 per cent, 33 per cent and 41 per cent, respectively.

International sugar prices, which had increased sharply in early 2006, eased significantly from August 2006 on forecasts of higher global production during 2006-07. Sugar prices have declined by almost 42 per cent by March



2007 from the recent peak touched in February 2006. According to the International Sugar Organisation, global sugar production is estimated to increase by 7.5 million tonnes to 160 million tonnes during 2006-07 (October-September) season, exceeding global consumption by 7.2 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 the EU output. Global cotton prices were largely range-bound during 2006-07.

Futures markets suggest that international crude oil and food prices could firm up further in the coming months. Metals prices are expected to remain at around current levels in the near term but could ease over the next year (Table 34).

Table 34: International Commodity Prices – Futures Market

Commodity	Unit	April/May 2007	July 2007	July 2008
1	2	3	4	5
Crude oil	$/bbl	63.1	65.7	69.8
Soybean oil	cents/pound	31.1	31.7	33.8*
Soybeans	cents/bushels	715	732	791
Rice	cents/cwt	1,011	1,051	1,158#
Wheat	cents/bushels	474	489	493
Aluminium	$/mt	2,836	2,880	2,703
Copper	$/mt	8,053	7,970	7,200
Tin	c/kg	14,400	14,200	13,325
Zinc	c/kg	3,685	3,698	3,378

: March 2008. * : May 2008.
Source : Chicago Board of Trade, London Metals Exchange and NYMEX.

Inflation Conditions in India

Monetary policy during 2006-07 was conducted to manage the transition to a higher growth path while ensuring that pressures on actual inflation and inflation expectations are contained. Taking into account the impact of real, monetary and global factors 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 by 25 basis points each to 5.75 per cent and 6.75 per cent, respectively, effective June 9, 2006. 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 warranted 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. The Bank Rate and cash reserve ratio were left unchanged.

In the Mid-Term Review of Annual Policy Statement for 2006-07 (October 2006), it was observed that the combination of high growth and consumer inflation coupled with escalating asset prices and tightening infrastructural bottlenecks underscored 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 although there was no conclusive evidence of potential overheating in the Indian economy at that time, the criticality of monitoring all available indications that could point to excess aggregate demand was perhaps more relevant. 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 (Table 35).

In the Third Quarter Review (January 2007), the Reserve Bank observed that early warning signals emanating from rising inflation in an environment of high money and credit growth (Chart 27) indicated that monetary policy was accommodative, warranting a policy response. Accordingly, the repo rate was increased by 25 basis points to 7.50 per cent while keeping the reverse repo rate unchanged at 6.0 per cent. It was also decided to reduce the interest rate ceilings on NR(E)RA and FCNR(B) deposits by 50 basis points and 25 basis points, respectively.

Table 35: 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 (+0.25)	7.9
October 2, 2004	4.50	6.00	5.00 (+0.25)	7.1
October 27, 2004	4.75 (+0.25)	6.00	5.00	7.4
April 29, 2005	5.00 (+0.25)	6.00	5.00	6.0
October 26, 2005	5.25 (+0.25)	6.25 (+0.25)	5.00	4.5
January 24, 2006	5.50 (+0.25)	6.50 (+0.25)	5.00	4.2
June 9, 2006	5.75 (+0.25)	6.75 (+0.25)	5.00	4.9
July 25, 2006	6.00 (+0.25)	7.00 (+0.25)	5.00	4.7
October 31, 2006	6.00	7.25 (+0.25)	5.00	5.3
December 23, 2006	6.00	7.25	5.25 (+0.25)	5.5
January 6, 2007	6.00	7.25	5.50 (+0.25)	6.1
January 31, 2007	6.00	7.50 (+0.25)	5.50	6.1
February 17, 2007	6.00	7.50	5.75 (+0.25)	6.7
March 3, 2007	6.00	7.50	6.00 (+0.25)	6.5
March 30, 2007	6.00	7.75 (+0.25)	6.00	6.5
April 14, 2007	6.00	7.75	6.25 (+0.25)*	

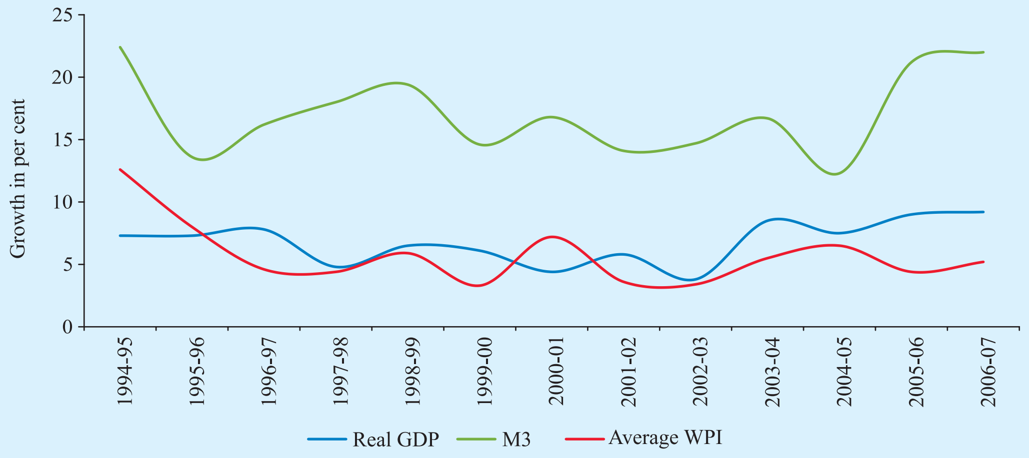
* : As announced on March 30, 2007, CRR will be hiked by further 25 basis points effective the fortnight beginning April 28, 2007.

Note : 1. With effect from October 29, 2004, the 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 usage of terms even for the period prior to October 29, 2004.

2. Figures in parentheses indicate change in policy rates.

In order to reinforce the measures already taken for maintaining price stability and anchoring inflation expectations to sustain the growth momentum,

Chart 27: Inflation Movements



the Reserve Bank, on March 30, 2007 announced a further hike of 25 basis points in the repo rate to 7.75 per cent, while leaving the reverse repo rate unchanged. It also decided to increase the CRR by another 50 basis points in two stages of 25 basis points each effective April 14, 2007 and April 28, 2007 - a cumulative increase of 150 basis points from December 2006 (see Chapter III). The Reserve Bank emphasised that the conduct of monetary policy would continue to demonstrate that inflation beyond its tolerance threshold was unacceptable and that the resolve to ensure price stability was always backed by timely and appropriate policy responses.

An assessment of key macroeconomic indicators in select EMEs indicates that over the past year, consumer price inflation has eased in a number of economies such as Brazil, Indonesia, Israel, the Philippines, Russia and Thailand. It, however, rose in China, India and South Africa. Major EMEs, except India and South Africa, have recorded surplus in current accounts. Although the Centre's fiscal deficit in India declined during 2006-07, it remained higher than most EMEs. The real policy rate in India in March 2007 was marginally lower than a year ago and remained below that in major EMEs (Table 36).

Table 36: Key Macroeconomic Indicators: Emerging Markets

(Per cent)

Country	Consumer Price Inflation		Current Account Balance (per cent to GDP)		Central Govt. Fiscal Balance (per cent of GDP)		Real Policy Rate		Real GDP Growth	
	March 2006	March 2007	2005	2006	2005	2006	March 2006	March 2007	2005	2006
1	2	3	4	5	6	7	8	9	10	11
Brazil	5.3	3.0	1.6	1.3	-3.4	-3.2	11.2	9.8	2.9	3.7
China	0.8	3.3	7.2	9.1	-1.3	-0.7	4.8	3.1	10.4	10.7
India	**4.9 *** **(4.1)**	**7.6 *** **(5.7)**	**-1.2 @** **(-6.5)**	**–**	**-4.1 @**	**-3.7 #**	**1.6** **(2.4)**	**0.2** **(2.0)**	**9.0 @**	**9.2 #**
Indonesia	15.8	6.5	0.1	2.7	-0.5	-1.0	-3.0	2.5	5.7	5.5
Israel	3.1 *	-0.8 *	2.9	5.2	-2.9	-2.7	1.2	4.8	5.2	5.1
Korea	2.0	2.2	1.9	0.7	1.9	1.8	2.0	2.3	4.2	5.0
Philippines	7.6	2.2	2.0	2.9	-2.7	-1.0	-0.1	5.3	5.0	5.4
Russia	10.6	7.1	10.9	9.8	7.5	7.5	1.4	3.4	6.4	6.7
South Africa	3.9 *	5.7 *	-3.8	-6.4	–	–	3.6	3.3	5.1	5.0
Thailand	5.7	2.0	-4.5	1.6	0.2	0.1	-1.2	2.5	4.5	5.0

* : February. @ : Data pertain to fiscal year 2005-06. # : Data pertain to fiscal year 2006-07.

Note : 1. As in Table 30, consumer price inflation data are on a year-on-year basis. Data for India are for CPI-Industrial Workers.
2. Real policy rate is the policy rate less year-on-year consumer price inflation.
3. Figures in parentheses in columns (2) and (3) refer to wholesale price inflation.
4. Figures in parentheses in column (4) refer to trade balance/GDP ratio.
5. Figures in parentheses in columns (8) and (9) for India are based on wholesale price inflation.
6. Data on fiscal balance for Korea and Israel pertain to general government balance.

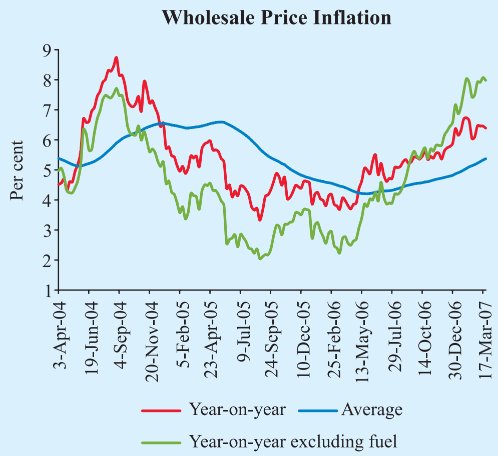
Source : IMF, ADB, official websites of respective central banks and the Economist.

Wholesale Price Inflation

Inflation movements in 2006-07 were driven by primary food articles and manufactured products prices reflecting the impact of both supply side and demand side pressures. The impact of mineral oils, the major driver of inflation since June 2004, petered out by early September 2006 on the back of decline in domestic fuel prices and the base effect. Headline inflation, based on movement in the wholesale price index (WPI), increased to 5.7 per cent, y-o-y, as on March 31, 2007 from 4.0 per cent a year ago. WPI inflation moved in a range of 3.7-6.7 per cent during 2006-07 (Chart 28 and Table 37). Headline inflation remained within the Reserve Bank's indicative projection of 5.0-5.5 per cent up to November 11, 2006 (except one week) and crossed 6.0 per cent between January 6, 2007 and March 24, 2007. The average WPI inflation rate (average of the 52 weeks) during 2006-07 at 5.4 per cent was higher than that of 4.4 per cent a year ago. The y-o-y inflation, excluding the fuel group, at 7.1 per cent was above the headline inflation rate of 5.7 per cent as on March 31, 2007.

Among the major groups, prices of primary articles led by wheat, pulses, milk, oilseeds and raw cotton posed upward pressures on inflation during 2006-07 (Chart 29). Wheat prices remained firm on the back of low stocks and firm international prices. Domestic wheat stocks were 5.4 million tonnes as on February 1, 2007 as against the buffer stock norm of 8.2 million tonnes. Although there was some moderation in early March 2007, wheat prices, on a year-on-year basis, increased by 7.6 per cent as on March 31, 2007 (global wheat prices, as noted earlier, increased by about 14 per cent, y-o-y, in March 2007). Prices of pulses also edged higher (12.0 per cent on top of 33.3 per cent increase a year ago),

Chart 28: Annual WPI Inflation



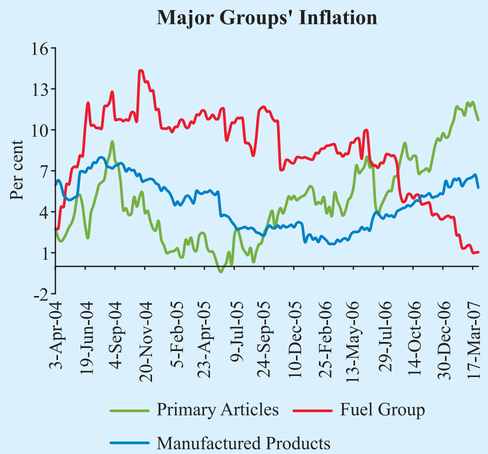


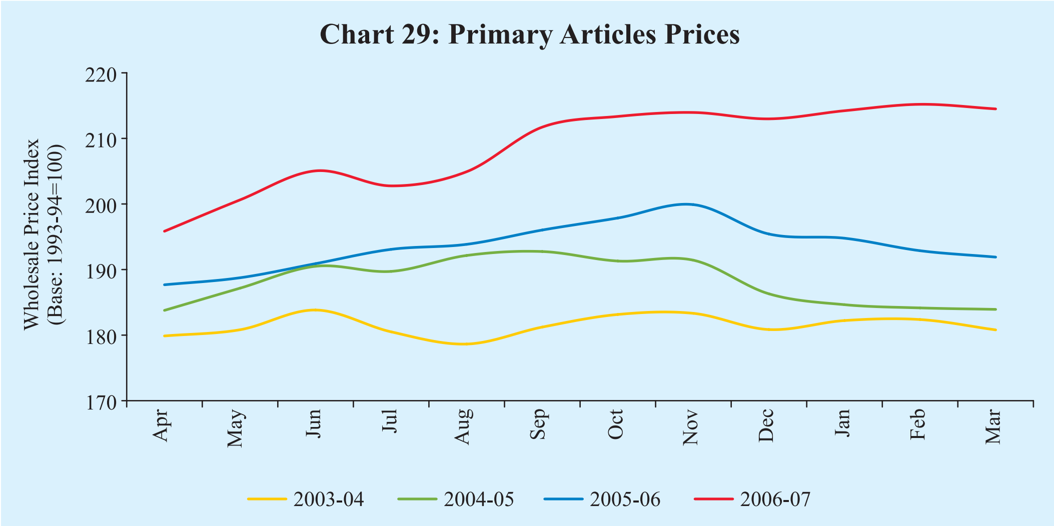
Table 37: Wholesale Price Inflation in India (year-on-year)

(Per cent)

Commodity	Weight	April 1, 2006		March 31, 2007 P	
		Inflation	WC	Inflation	WC
1	2	3	4	5	6
All Commodities	**100.0**	**4.0**	**100.0**	**5.7**	**100.0**
1. Primary Articles	**22.0**	**4.8**	**25.8**	**10.7**	**40.4**
Food Articles	15.4	5.9	22.5	8.3	22.3
i. Rice	2.4	2.1	1.1	5.7	2.1
ii. Wheat	1.4	12.7	4.3	7.6	1.9
iii. Pulses	0.6	33.3	4.5	12.0	1.4
iv. Vegetables	1.5	7.6	2.4	1.4	0.3
v. Fruits	1.5	-3.9	-1.9	5.5	1.7
vi. Milk	4.4	1.9	2.0	8.4	6.0
vii. Eggs, Meat and Fish	2.2	13.2	7.3	11.1	4.6
Non-Food Articles	6.1	-2.4	-3.5	16.6	15.5
i. Raw Cotton	1.4	-1.7	-0.4	21.4	3.6
ii. Oilseeds	2.7	-9.2	-5.5	30.6	11.0
iii. Sugarcane	1.3	0.7	0.3	1.1	0.3
Minerals	0.5	43.6	6.9	17.0	2.6
2. Fuel, Power, Light and Lubricants	**14.2**	**8.3**	**45.5**	**1.0**	**4.1**
i. Mineral Oils	7.0	12.0	37.2	0.5	1.2
ii. Electricity	5.5	4.5	8.3	2.3	2.9
iii. Coal Mining	1.8	0.0	0.0	0.0	0.0
3. Manufactured Products	**63.8**	**1.9**	**27.7**	**5.8**	**55.9**
i. Food Products	11.5	1.0	2.6	6.4	11.3
of which: Sugar	3.6	6.2	4.7	-12.7	-6.9
Edible Oils	2.8	-3.3	-1.8	14.7	5.1
ii. Cotton Textiles	4.2	2.3	2.1	-1.0	-0.6
iii. Man Made Fibres	4.4	-3.9	-2.1	3.7	1.3
iv. Chemicals and Chemical Products	11.9	3.3	9.7	2.9	5.8
of which : Fertilisers	3.7	0.2	0.1	1.8	1.0
v. Basic Metals, Alloys and Metal Products	8.3	-0.6	-1.5	11.0	17.6
of which: Iron and Steel	3.6	-4.2	-5.1	7.5	5.8
vi. Non-Metallic Mineral Products	2.5	9.6	5.4	9.0	3.7
of which: Cement	1.7	14.9	5.6	11.6	3.3
vii. Machinery and Machine Tools	8.4	3.2	5.2	8.0	8.8
of which: Electrical Machinery	5.0	4.1	3.1	12.8	6.9
viii. Transport Equipment and Parts	4.3	0.9	0.8	2.1	1.2
Memo:					
Food Items (Composite)	**26.9**	**3.9**	**25.1**	**7.5**	**33.6**
WPI Excluding Food	**73.1**	**4.0**	**74.9**	**5.1**	**66.4**
WPI Excluding Fuel	**85.8**	**2.8**	**54.5**	**7.1**	**95.9**

P: Provisional. WC: Weighted Contribution.

reflecting stagnant domestic production as well as higher demand. Milk prices increased by 8.4 per cent. Prices of oilseeds witnessed a sharp turnaround - an increase of 30.6 per cent, y-o-y, as against a decline of 9.2 per cent a year ago - which could be attributed to lower domestic production as well as firm global prices. Raw cotton prices increased sharply in March 2007 and prices were 21.4 per cent higher, y-o-y, as on March 31, 2007. Overall, prices of primary articles,



on a y-o-y basis, increased by 10.7 per cent (4.8 per cent a year ago). Primary articles inflation during 2006-07 was the highest in the past decade (Table 38).

In order to contain the price rise in primary commodities, the Government undertook a number of fiscal and supply 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 subsequently 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 its exports; (v) allowing imports of maize at zero duty in February 2007; (vi) reduction in customs duty

Table 38: Major Group's WPI Inflation (year-on-year)

(Per cent)

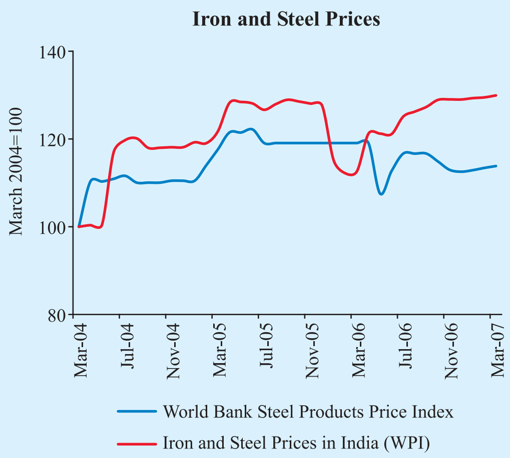
Year	All Commodities	Primary Articles	Fuel Group	Manufactured Products
1	2	3	4	5
1995-96	4.4	3.1	5.1	4.7
1996-97	5.4	9.2	13.3	2.4
1997-98	4.5	4.6	13.7	2.3
1998-99	5.3	7.6	3.2	4.9
1999-00	6.5	4.0	26.7	2.4
2000-01	4.9	-0.4	15.0	3.8
2001-02	1.6	3.9	3.9	0.0
2002-03	6.5	6.1	10.8	5.1
2003-04	4.6	1.6	2.5	6.7
2004-05	5.1	1.3	10.5	4.6
2005-06	4.1	5.4	8.9	1.7
2006-07	5.7	10.7	1.0	5.8

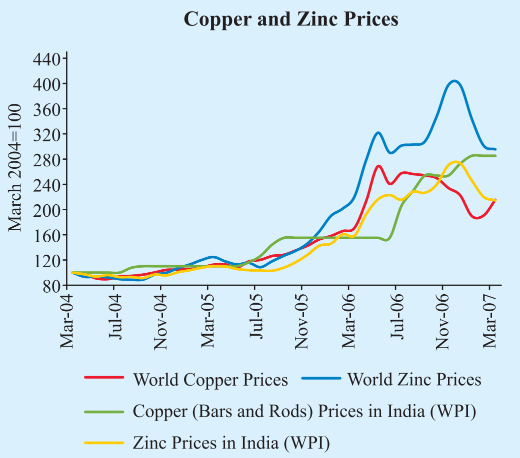
on palm oils by 10 percentage points each in August 2006 and April 2007, and on crude palm oil, sunflower oil and refined sunflower oil by 10 percentage points each in January 2007.

Fuel group inflation moderated to 1.0 per cent on March 31, 2007 from a peak of 9.9 per cent on June 17, 2006 and 8.3 per cent a year ago, reflecting the base effect as well as cuts in prices of petrol, diesel and other fuel products. 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 and, by a similar order again effective February 15, 2007. Earlier, in June 2006, the Government had (i) raised domestic petrol and diesel prices by Rs.4 and Rs.2 per litre, respectively, following the uptrend in international prices; (ii) reduced customs duty on petrol and diesel to 7.5 per cent from 10.0 per cent; and (iii) announced 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 issued oil bonds worth Rs. 24,121 crore during 2006-07 in five tranches.

Manufactured products inflation increased to 5.8 per cent as on March 31, 2007 from 1.9 per cent a year ago. Manufactured products inflation during 2006-07 was led by edible oils/oil cakes, metals, cement and electrical machinery. Metals group inflation was 11.0 per cent, y-o-y, as on March 31, 2007 and contributed 18 per cent to headline inflation. Within the metals group, non-ferrous metal prices rose by 29.3 per cent, y-o-y, on top of an increase of 17.5 per cent a year ago, broadly in line with international trends (Chart 30). Iron and steel prices increased by 7.5 per cent, y-o-y, in contrast to a decline of 4.2 per cent a year ago.

Chart 30: Metals Prices



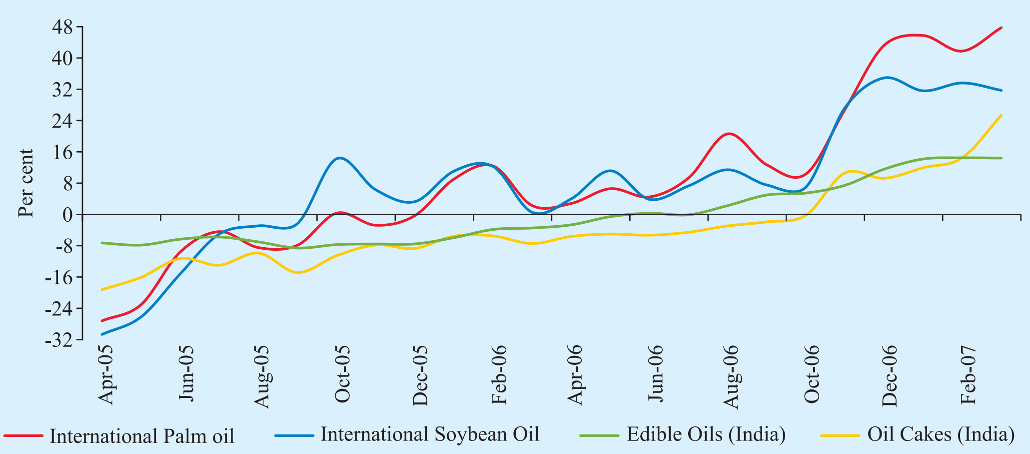


Domestic prices of cement increased by 11.6 per cent, y-o-y, as on March 31, 2007 on top of an increase of 14.9 per cent a year ago, in consonance with strong domestic demand emanating from construction activity. Real GDP originating from construction recorded double digit growth - averaging over 12 per cent per annum - between 2003-04 and 2005-06 on the back of strong housing and other infrastructure activities. Construction activity remained robust during 2006-07, notwithstanding some deceleration (9.7 per cent during April-December 2006). Capacity utilisation in the cement industry remains high (94 per cent during 2006-07 as compared with 90 per cent a year ago). Other manufactured items contributing to higher y-o-y inflation included electrical machinery (an increase of 12.8 per cent, y-o-y, as compared with an increase of 4.1 per cent a year ago) reflecting the higher input prices as well as strong investment demand.

Rise in prices of edible oils (increase of 14.7 per cent in contrast to a decline of 3.3 per cent a year ago), oil cakes (increase of 31.0 per cent as against a decline of 8.2 per cent), and grain mill products (increase of 21.4 per cent on top of an increase of 13.5 per cent a year ago) also contributed to manufactured products inflation (Chart 31). Edible oils and oil cakes along with oilseeds accounted for more than one-fifth of headline inflation. Domestic sugar prices declined by 12.7 per cent (as against an increase of 6.2 per cent a year ago) in line with global trend reflecting higher production.

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. The Government further reduced the peak customs duty from 12.5 per cent to 10.0 per cent in the Union Budget 2007-08

Chart 31: Edible Oils Inflation



and, in the case of some items, below the peak rate of 10.0 per cent. On April 3, 2007, the Government decided to exempt import of portland cement from countervailing duty and special additional customs duty; it was earlier exempted from basic customs duty in January 2007.

In brief, primary articles' contribution to the overall y-o-y inflation as on March 31, 2007 increased to 40.4 per cent (from 25.8 per cent a year ago) mainly due to higher prices of wheat, pulses, milk, oilseeds and raw cotton (Chart 32). Manufactured products group's contribution also rose to 55.9 per cent (27.7 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 the fuel group to the y-o-y headline inflation, on the other hand, declined sharply to 4.1 per cent from 45.5 per cent a year ago.

Consumer Price Inflation

Various measures of consumer price inflation remained higher than the WPI inflation during 2006-07, mainly reflecting the higher order of increase in food prices as well as the higher weight of food items in the CPI (Table 39). Food items have a weight of 69 per cent in the CPI for agricultural labourers, 67 per cent in the CPI for rural labourers, 47 per cent in the CPI for urban non-manual employees and 46 per cent in the CPI for industrial workers as compared with 27 per cent (composite) in WPI. Disaggregated data show that food group inflation in various CPI measures rose from 4.9-5.8 per cent in March 2006 to 11.2-11.8 per cent by February 2007. As a result of the higher order of increase in food prices coupled with their large weight in the indices, various measures of CPI inflation increased from 4.9-5.3 per cent in March 2006 to 7.6-9.8 per cent in February 2007.

Chart 32: Major Groups' Weighted Contribution to WPI Inflation (year-on-year)

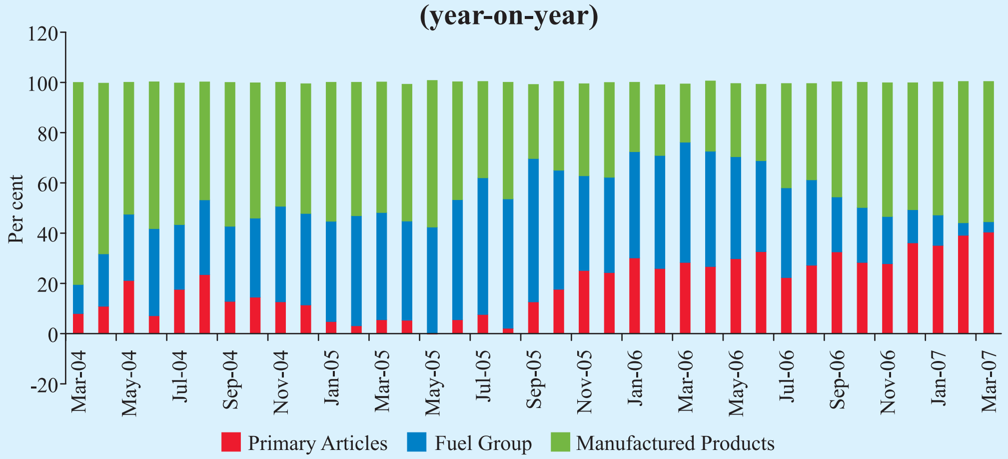


Table 39: Consumer Price Inflation : Major Groups

(Year-on-year variation in per cent)

CPI Measure	Weight	March 2003	March 2004	March 2005	March 2006	June 2006	September 2006	December 2006	February 2007
1	2	3	4	5	6	7	8	9	10
CPI-IW (Base: 2001=100)									
General	**100.0**	**4.1**	**3.5**	**4.2**	**4.9**	**7.7**	**6.8**	**6.9**	**7.6**
Food, Beverages *etc.*	46.2	3.7	3.1	1.6	4.9	10.0	8.9	9.6	–
Pan, Supari *etc.*	2.3	1.9	4.2	2.1	3.1	3.7	4.2	4.3	–
Fuel and Light	6.4	6.3	6.5	4.9	-2.9	8.7	6.5	5.9	–
Housing	15.3	5.4	3.9	20.4	6.6	6.6	7.1	7.1	–
Clothing, Bedding *etc.*	6.6	1.5	2.1	2.3	3.0	2.8	2.5	4.0	–
Miscellaneous	23.3	5.3	3.2	3.9	4.6	4.7	5.4	4.1	–
CPI-UNME (Base: 1984-85=100)									
General	**100.0**	**3.8**	**3.4**	**4.0**	**5.0**	**6.5**	**6.6**	**6.9**	**7.8**
Food, Beverages *etc.*	47.1	2.6	3.0	2.2	5.3	8.9	8.4	9.2	11.2
Fuel and Light	5.5	3.1	3.2	9.6	1.9	3.0	4.2	5.9	5.6
Housing	16.4	6.3	5.2	7.5	5.5	5.5	5.5	5.5	5.8
Clothing, Bedding *etc.*	7.0	2.6	2.6	2.0	2.9	2.7	3.4	3.8	3.6
Miscellaneous	24.0	6.0	2.8	4.4	5.1	6.1	6.5	4.6	4.6
CPI-AL (Base: 1986-87=100)									
General	**100.0**	**4.9**	**2.5**	**2.4**	**5.3**	**7.2**	**7.3**	**8.9**	**9.8**
Food, Beverages *etc.*	69.2	6.0	1.6	2.2	5.5	8.3	8.0	9.9	11.8
Pan, Supari *etc.*	3.8	3.5	4.7	-1.3	6.6	5.8	6.5	7.2	6.2
Fuel and Light	8.4	4.8	3.0	3.0	4.3	6.4	7.8	7.3	6.6
Clothing, Bedding *etc.*	7.0	3.0	4.1	2.5	2.2	2.5	3.3	3.3	3.2
Miscellaneous	11.7	3.1	2.7	5.5	5.5	5.2	7.0	7.4	6.8
CPI-RL (Base: 1986-87=100)									
General	**100.0**	**4.8**	**2.5**	**2.4**	**5.3**	**7.2**	**7.0**	**8.3**	**9.5**
Food, Beverages *etc.*	66.8	5.6	1.9	1.9	5.8	8.3	8.0	9.6	11.5
Pan, Supari *etc.*	3.7	3.5	4.7	-1.0	6.3	5.8	6.3	7.4	6.0
Fuel and Light	7.9	4.8	3.0	2.9	4.0	6.1	7.2	7.3	6.3
Clothing, Bedding *etc.*	9.8	3.3	3.4	2.8	2.7	2.9	3.5	2.9	2.9
Miscellaneous	11.9	3.1	3.0	5.5	5.2	4.9	6.4	7.2	6.3
Memo:									
WPI Inflation (End of period)		6.5	4.6	5.1	4.1	4.8	5.4	5.9	6.1
GDP Deflator		3.9	3.7	4.2	4.4	4.3	4.4	5.0	–

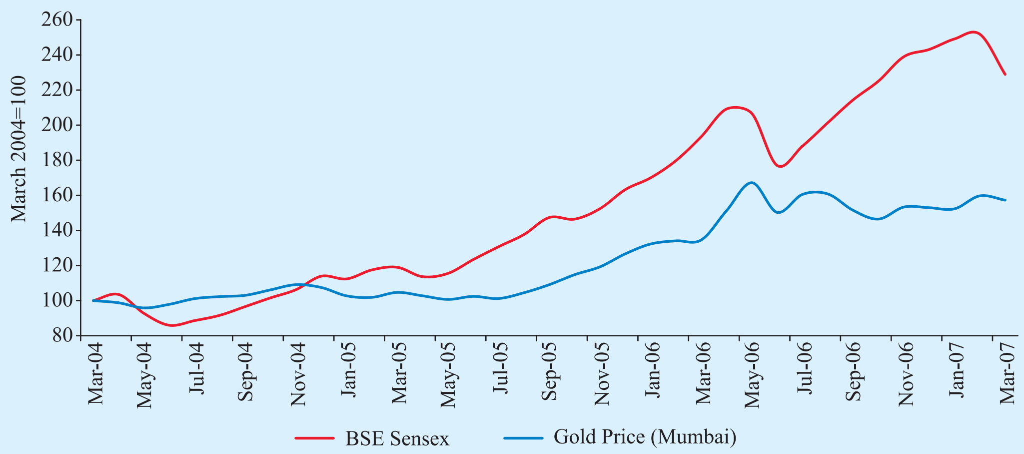
IW : Industrial Workers　UNME : Urban Non-Manual Employees
AL : Agricultural Labourers　RL : Rural Labourers

Higher fuel group prices also contributed to CPI inflation. Prices of services proxied by "miscellaneous group" exhibited a mixed trend, recording acceleration in February 2007 (as compared to March 2006) in the case of CPI-AL and CPI-RL and deceleration in the case of CPI-UNME. Housing inflation (reflecting rents on housing) rose to 7.1 per cent in January 2007 from 6.6 per cent in March 2006 in CPI-IW and to 5.8 per cent in February 2007 from 5.5 per cent in March 2006 in CPI-UNME.

Asset Prices

Domestic equity and bullion markets recorded gains during 2006-07, with intermittent corrections during the course of the year. Domestic equity prices fell during May and early June 2006 in line with international equity markets on concerns that monetary tightening might slow prospects for global growth. Equity prices recovered thereafter and the BSE Sensex touched a peak of 14652 on February 8, 2007 before witnessing some correction thereafter (see Chapter V). Overall, the BSE Sensex gained 15.9 per cent during 2006-07 (Chart 33). Domestic gold prices increased by about 10 per cent during 2006-07, broadly mirroring movements in international prices. International gold prices initially rose to US $ 715 per ounce on May 12, 2006 but fell to US $ 559 as on June 14, 2006 in consonance with the trends in various commodities in the international market. Gold prices recovered to US $ 664 per ounce as on July 14, 2006 but again eased to below US $ 600 per ounce in the second week of September 2006 as headline inflation in major economies eased in tandem with softening of international crude oil prices. Gold prices rebounded in the fourth quarter of 2006 and gained further during January-February 2007 to US $ 687 per ounce in late February 2007. Prices softened to around US $ 660 per ounce by end-March 2007.

Chart 33: Asset Price Movements



V. FINANCIAL MARKETS

International Financial Markets

During 2006-07 (April-March), short-term interest rates increased further in major advanced economies as well as emerging market economies (EMEs) (Table 40) as many central banks continued monetary tightening to contain inflation and stabilise inflationary expectations as detailed in the previous chapter. During the year, the US Federal Reserve increased the fed funds rate target twice by 25 basis points each in May 2006 and June 2006. It has since then paused. The European Central Bank increased its policy rate five times by 25 basis points each in June 2006, August 2006, October 2006, December 2006 and March 2007. The UK also raised its policy rate thrice by 25 basis points each in August 2006, November 2006 and January 2007. Other advanced economies such as Australia, Canada, Japan, New Zealand, Norway, Sweden and Switzerland also increased their policy rates during the year. The increase in short-term rates in the US during 2006-07 was lower than other major advanced economies reflecting the pause by the US Fed since end-June 2006. Central banks in many EMEs such as China, South Africa, South Korea, Taiwan and Turkey also increased their policy rates. Other EMEs such as Israel and Thailand initially raised their policy rates during the year but subsequently cut their policy rates to support growth; Brazil

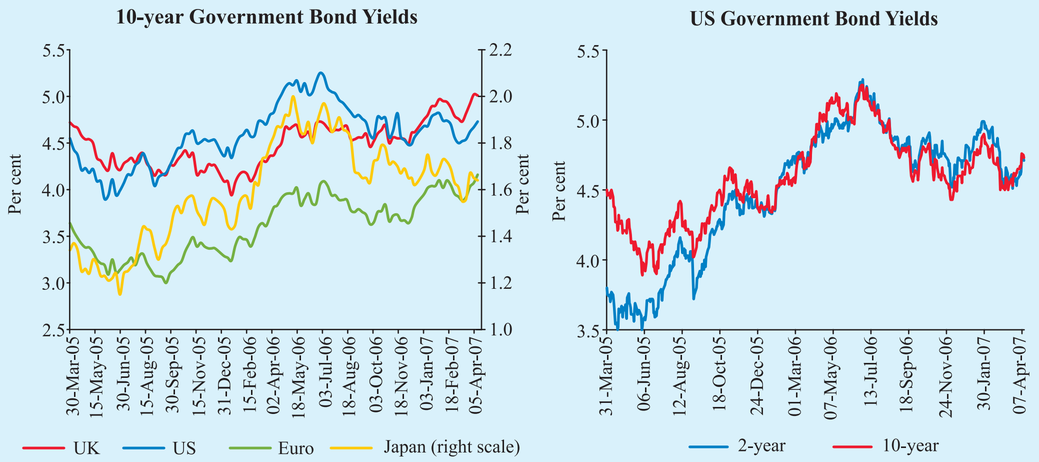
Table 40: Short-term Interest Rates

(Per cent)

Region/Country	At end of					
	March 2005	March 2006	June 2006	September 2006	December 2006	March 2007
1	2	3	4	5	6	7
Advanced Economies						
Euro Area	2.15	2.80	3.06	3.38	3.70	3.91
Japan	0.02	0.04	0.24	0.34	0.44	0.57
Sweden	1.97	1.99	2.23	2.55	2.94	3.21
UK	4.95	4.58	4.70	5.02	5.27	5.55
US	2.90	4.77	5.48	5.21	5.25	5.23
Emerging Market Economies						
Argentina	4.56	9.63	10.00	10.38	10.63	9.63
Brazil	19.25	16.54	15.18	14.17	13.19	12.68
China	2.25	2.40	3.00	2.95	2.88	2.86
Hong Kong	2.79	4.47	4.67	4.20	3.97	4.17
India	**5.37**	**6.11**	**6.36**	**6.60**	**7.18**	**7.98**
Malaysia	2.82	3.51	3.93	3.85	3.73	3.64
Philippines	7.25	7.38	8.00	7.63	6.56	5.31
Singapore	2.06	3.44	3.50	3.44	3.44	3.00
South Korea	3.54	4.26	4.57	4.63	4.73	4.94
Thailand	2.64	5.10	5.40	5.40	5.20	4.45

Note : Data for India refer to 91-day Treasury Bills rate and for other countries 3-month money market rates.
Source : The Economist.

Chart 34: Long-term Yields: Advanced Economies



continued to reduce policy rates throughout the year. Short-term interest rates, therefore, declined in such EMEs.

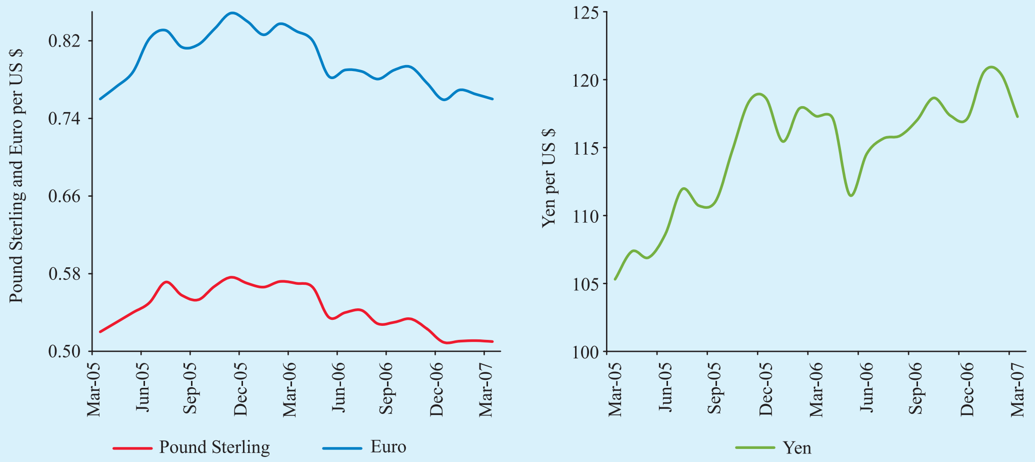
Long-term Government bond yields exhibited mixed trends in major advanced economies during 2006-07. During the year, 10-year yield declined by 18 basis points in the US and 12 basis points in Japan but increased by 56 basis points in the UK and 32 basis points in the euro area. The decline in the yield in the US could be attributed to easing of crude oil prices, weakening of economic growth and pause in monetary tightening by the Federal Reserve (Chart 34). The hardening of yields in the euro area and the UK could be attributed to higher short-term rates in the wake of further tightening and improved growth prospects. Since early June 2006, 10-year US bond yields have generally remained below those on 2-year bonds. Spreads on risky corporate debt in major advanced economies fell during the year, reaching record lows in the first quarter of 2007 on the back of strong risk appetite and sound corporate balance sheets. Spreads on emerging market debt also eased to record lows in the first quarter of 2007.

Global equity markets recorded further gains during 2006-07, interspersed with intermittent corrections (Chart 35). Equity markets initially registered losses between mid-May and early June 2006 in a number of economies reflecting concerns about growing inflationary pressures and concomitant increase in risk aversion. Global equity markets recovered part of the losses during the second and third quarters of 2006-07 reflecting strong corporate results, decline in crude oil prices, better than expected growth in the euro area, strong merger and acquisition activity and pause by the US Federal Reserve. Stock markets in a number of economies declined on December 19, 2006 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, with the market in Thailand, in particular, declining by 14.8 per cent on December 19, 2006 (over its level on the previous day). The markets, however, recovered some of these losses the next day as the BoT exempted investments in stock markets from the URR. During the last week of February 2007, equity markets in many advanced as well as EMEs fell. The Chinese stock markets declined by 9.0 per cent on February 27, 2007 but recovered some of these losses in the subsequent days. The equity markets in the US and several other developed and EMEs declined again in March 2007 on concerns over sub-prime mortgage lending and slowdown in the US economy. Notwithstanding these corrections during the course of the year, the MSCI World and MSCI emerging markets indices at end-March 2007 were higher by 13.4 per cent and 18.3 per cent, respectively, over their levels at end-March 2006. These gains were led by stock markets in China (143.6 per cent), followed by Russia (38.4 per cent), Indonesia (36.1 per cent), Malaysia (32.4 per cent), South Africa (32.0 per cent), Singapore (27.0 per cent) and the Hong Kong (24.2 per cent).

In the foreign exchange market, the US dollar depreciated against the major currencies during 2006-07, reflecting narrowing of interest rate differentials, moderation of activity in the US and robust growth in the euro area and Japan (Chart 36). Between end-March 2006 and end-March 2007, the US dollar depreciated by 11.4 per cent against the Pound sterling and 9.1 per cent against the euro but appreciated by 0.2 per cent against the yen. Amongst Asian currencies, the US dollar depreciated by 6.2 per cent against the Malaysian ringgit, 9.9 per cent against the Thai baht, 3.5 per cent against the Chinese yuan and 3.6 per cent against the Korean won over the same period. Between end-March 2006 and end-March 2007, the euro appreciated by 10.0 per cent

Chart 36: Exchange Rate of Major Currencies per US dollar



against the US dollar and 10.3 per cent against the yen, but depreciated by 2.5 per cent against the Pound sterling. Over the same period, the euro appreciated by 3.2 per cent against the Malaysian ringgit, 6.1 per cent against the Chinese yuan and 6.0 per cent against the Korean won; however, it depreciated by 0.9 per cent against Thai baht. The Japanese yen recorded depreciation against almost all the major currencies, *i.e.*, by 0.2 per cent against the US dollar, 9.3 per cent against the euro, 11.6 per cent against the Pound sterling, 10.1 per cent against the Thai baht, 6.4 per cent against the Malaysian ringgit, 3.9 per cent against the Korean won and 3.7 per cent against the Chinese yuan over the same period.

Domestic Financial Markets

Indian financial markets remained generally orderly for most part of 2006-07. There were, however, some spells of volatility at different points of time during the year reflecting developments in liquidity conditions on account of large and sudden changes in capital flows and cash balances of the Governments. Interest rates in various segments increased during the year. The call money rate edged up during the year in tandem with movements in policy rates. The call rate remained mostly within the corridor set by the Reserve Bank's repo and reverse repo rates during April-November 2006. In the subsequent months, there were a few brief episodes (last week of December 2006 and second half of March 2007) of higher volatility when the call rate exceeded the repo rate significantly. Interest rates in the collateralised segment of the overnight money market also hardened, but remained below the call rate during the year. In the foreign exchange market, the Indian rupee exhibited two-way movements with a strengthening bias since mid-July 2006.

Table 41: 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**	**6,256**	**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	5,480	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	**21,725**	**7.22**	**4,863**	**7.78**	**18,540**	**45.25**	**24,517##**	**2.14**	**37,698**	**21,973**	**3,877**	**7,883**	**12319**	**3585**
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	3,261	6,828	9935	2915
July	18,254	5.86	2,243	8.26	14,325	46.46	0	0.83	36,936	48,027	2,605	5,652	10557	3092
August	21,294	6.06	5,786	8.09	15,934	46.54	0	1.22	40,305	36,326	2,869	5,945	11305	3306
September	23,665	6.33	8,306	7.76	18,107	46.12	0	1.31	40,018	25,862	3,411	6,873	12036	3492
October	26,429	6.75	4,313	7.65	16,924	44.47	0	1.67	41,537	12,983	3,481	6,919	12637	3649
November	25,649	6.69	10,654	7.52	20,475	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	19,932	44.64	1,818	3.20	38,148	-1,713	4,276	8,505	13647	3918
January	22,360	8.18	4,822	7.71	21,065 P	44.33	2,830	4.22	39,553	-10,738	4,380	8,757	13984	4037
February	23,254	7.16	4,386	7.90	20,050 P	44.16	11,862	3.71	40,827	648	4,680	9,483	14143	4079
March	23,217	14.07	2,991	8.00	24,231 P	44.03	–	4.51	52,944	-11,858	3,716	7,998	12850	3731

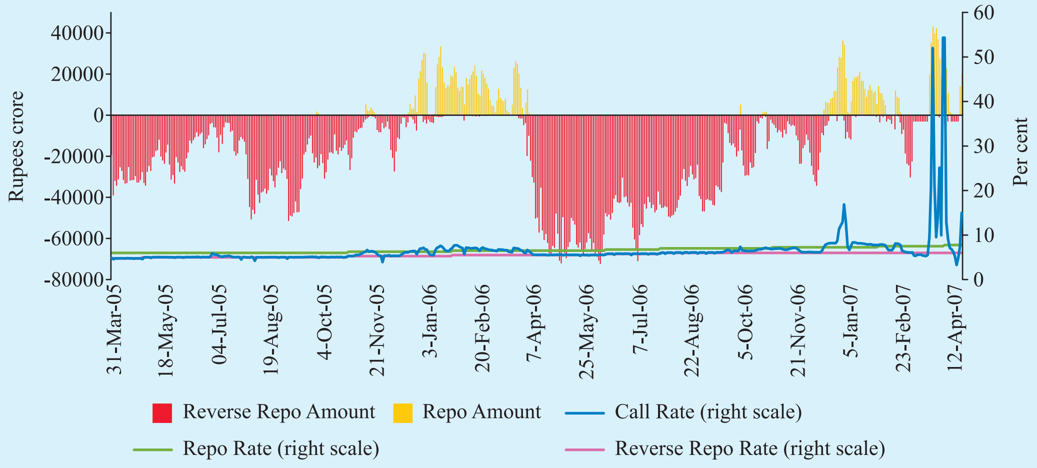
* : Average of daily weighted call money borrowing rates.
@ : Average of daily closing rates.
** : Average of daily closing indices.
LAF : Liquidity Adjustment Facility.
MSS : Market Stabilisation Scheme.
NSE : National Stock Exchange of India Ltd.
+ : Average of daily outright turnover in Central Government dated securities.
# : Average of weekly outstanding MSS.
: Cumulative for the financial year.
BSE : Bombay Stock Exchange Limited.
– : Not available.
P : Provisional.
Note : In column 11, (-) indicates injection of liquidity, while (+) indicates absorption of liquidity.

Yields in the Government securities market hardened during the year and the yield curve flattened. Banks' deposit and lending rates edged up, especially in the second half of the year. The stock markets reached record highs during the year interspersed with periodic corrections (Table 41). The primary market segment of the capital market continued to exhibit buoyancy.

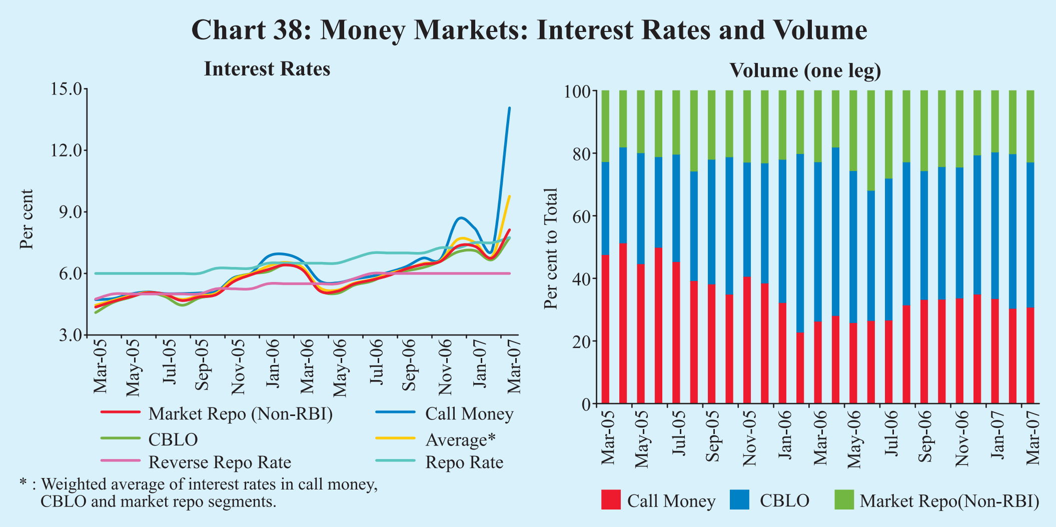
Money Market

Money market rates edged up during the year, broadly moving in line with the policy rates, with intra-year movements depending upon the evolving liquidity conditions. The call money rate was generally anchored close to the

Chart 37: Liquidity Adjustment Facility and the Call Rate



reverse repo rate up to mid-September 2006 (Chart 37). Liquidity conditions became relatively tighter in the second half of September 2006, *inter alia,* on account of liquidity pressures emanating from advance tax outflows and festive season currency demand coupled with high credit demand. The call rate crossed the repo rate and touched 7.38 per cent on September 29, 2006. The call rate eased below the repo rate by early October 2006 partly on account of reduction in Centre's surplus cash balances with the Reserve Bank and remained mostly within repo-reverse repo corridor between end-October to second week of December 2006. The call rates eased to near reverse repo levels by the last week of November 2006, before the announcement on December 8, 2006 of a hike of 25 basis points each in the cash reserve ratio (CRR) effective the fortnights beginning December 23, 2006 and January 6, 2007. The call rate again edged up 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 the CRR hike. The call rate eased from the elevated levels in the first week of January 2007 on the back of improvement in liquidity conditions. Notwithstanding an increase in the repo rate by 25 basis points on January 31, 2007 (reverse repo rate remained unchanged), the call rate eased further to around 6.5 per cent by the second week of February 2007 due to forex induced liquidity. Following the announcement (on February 13, 2007) of the hike of 25 basis points each in the CRR effective the fortnights beginning February 17, 2007 and March 3, 2007, the call rate again firmed up to about 8.0 per cent by mid-February 2007 but quickly eased to around 6.1 per cent by end-February 2007. It further declined to below the lower bound of the corridor between March 5-15, 2007 as liquidity conditions eased. Modified arrangements of liquidity



management were put in place effective March 5, 2007 under which a flexible arrangement of MSS auctions of dated securities was introduced along with a ceiling of Rs.3,000 crore under the LAF reverse repo (see Chapter III). The call money rate hardened in the second half of March 2007 as liquidity conditions tightened due to advance tax outflows, year-end considerations, sustained credit demand and asymmetric distribution of Government securities holdings across the banks. The call rate averaged 21.99 per cent during March 16-30, 2007 and reached an intra-year high of 54.3 per cent as on March 30, 2007. The call rate eased to 3.3 per cent on April 12, 2007 with the easing of liquidity conditions. It was 12.0 per cent on April 18, 2007.

The interest rates in the collateralised segments of the money market – the market repo (outside the LAF) and the Collateralised Borrowing and Lending Obligation (CBLO) – increased in line with the call rate, and continued to remain below the call rate during 2006-07. The rates in these segments exhibited relative stability *vis-à-vis* the call rate. For the financial year 2006-07, as a whole, the interest rates averaged 6.24 per cent and 6.34 per cent in the CBLO and market repo segments, respectively, as compared with 7.22 per cent in the call money market. The collateralised market is now the predominant segment in the money market, accounting for about 70 per cent of the total volume during 2006-07 (Chart 38 and Table 42). Mutual funds and insurance companies are the major lenders in the CBLO market with nationalised banks, primary dealers and non-financial companies being the major borrowers. In the market repo segment, mutual funds and foreign banks are the major provider of funds, while the foreign banks, private sector banks and primary dealers are the major borrowers.

Table 42: 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	Out-standing	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	**10,863**	**8,419**	**16,195**	**506**	**21,478**	**4,537**	**64,954**
April	8,455	5,479	16,329	447	16,550	6,065	44,059
May	9,037	9,027	17,147	473	17,067	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	23,299	6,460	65,621
September	11,833	9,185	14,771	568	24,444	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	68,911
December	12,084	7,170	15,512	481	23,536	3,080	68,619
January	11,180	6,591	15,758	515	24,398	3,490	70,149
February	11,627	7,794	19,063	467	21,167	2,763	72,795
March	11,608	8,687	17,662	739	19,102 *	2,106	92,468#

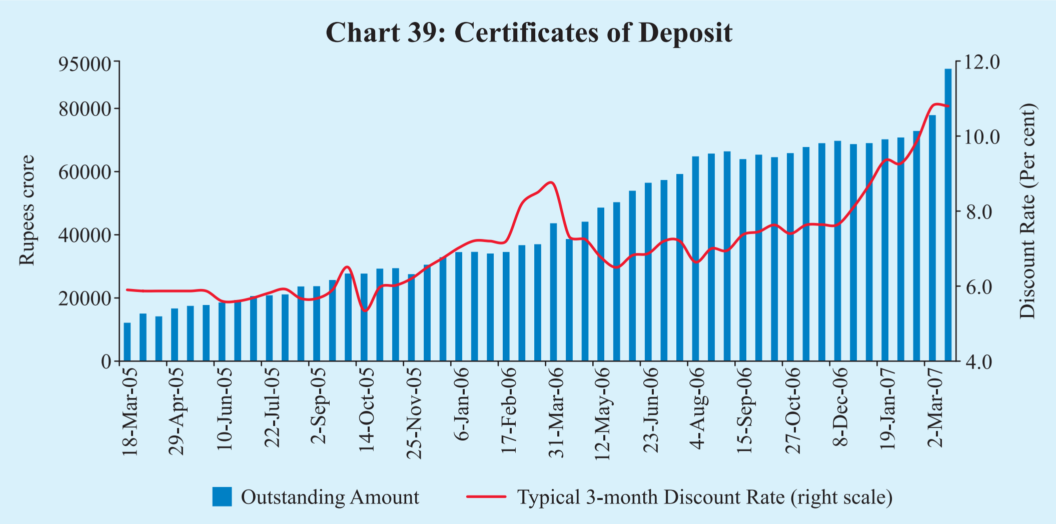
* : As on March 15, 2007. # : As on March 16, 2007.

Certificates of Deposit

The outstanding amount of certificates of deposit (CDs) more than doubled from Rs.43,568 crore at end-March 2006 (4.8 per cent of aggregate deposits of issuing banks) to Rs.92,468 crore (4.9 per cent) by March 16, 2007 as banks continued to supplement their efforts at deposit mobilisation to support sustained credit demand (Table 42 and Chart 39). The weighted average discount rate (WADR) of CDs increased by 215 basis points during the year to 10.77 per cent as on March 16, 2007. Mutual funds are amongst the major investors in the CDs. Since CDs can be traded and easily liquidated, mutual funds find them quite attractive.

Commercial Paper

Issuances of commercial papers (CPs) increased sharply in the first half of 2006-07, but fell during the second half of the year. Outstanding CPs rose from



Rs.12,718 crore at end-March 2006 to Rs.24,444 crore as on September 30, 2006 before declining to Rs.19,102 crore as on March 15, 2007 (Chart 40). The weighted average discount rate (WADR) on CPs increased from 8.59 per cent during the fortnight ended March 31, 2006 to 10.24 per cent during the fortnight ended March 15, 2007 in tandem with the increase in the money market rates. The discount rate on CPs moved from a range of 6.69-9.25 per cent during the fortnight ended March 31, 2006 to 7.50-13.35 per cent during the fortnight ended March 15, 2007.

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 43).

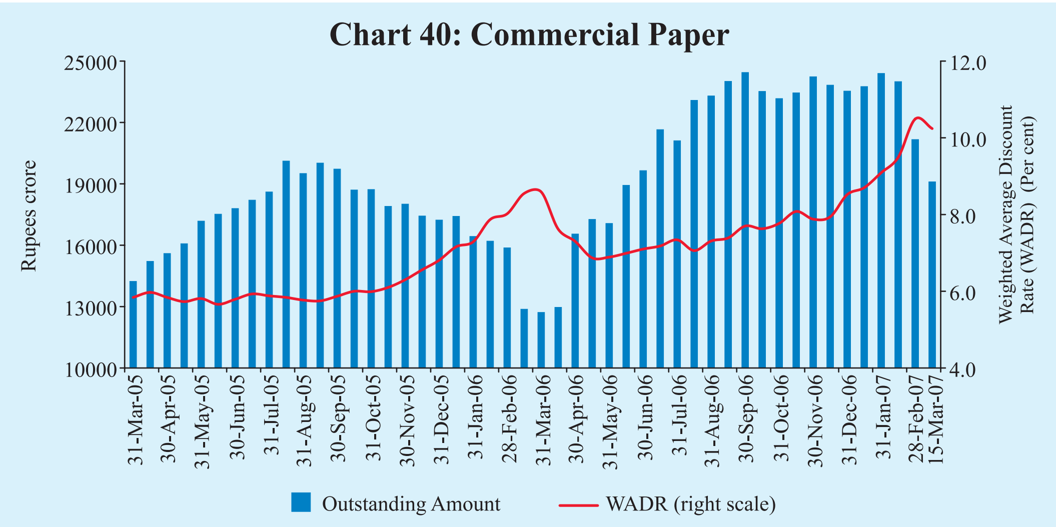


Table 43: Commercial Paper – Major Issuers

(Rupees crore)

Category of Issuer	End of					
	March 2005	March 2006	June 2006	September 2006	December 2006	March # 2007
1	2	3	4	5	6	7
Leasing and Finance	8,479	9,400	13,460	15,817	15,060	12,803
	(59.6)	(73.9)	(68.5)	(64.7)	(64.0)	(67.0)
Manufacturing	2,881	1,982	4,155	4,847	4,811	3,204
	(20.2)	(15.6)	(21.1)	(19.8)	(20.4)	(16.8)
Financial Institutions	2,875	1,336	2,035	3,780	3,665	3,095
	(20.2)	(10.5)	(10.4)	(15.5)	(15.6)	(16.2)
Total	**14,235**	**12,718**	**19,650**	**24,444**	**23,536**	**19,102**
	(100.0)	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**

#: As on March 15, 2007.
Note : Figures in parentheses are percentage shares in the total.

Treasury Bills

The primary market yields on Treasury Bills (TBs) increased in the range of 117-132 basis points during 2006-07. In the first quarter of 2006-07, yields on Treasury Bills firmed up over concerns of higher inflation, hike of fed funds rate target, larger issuances on account of reintroduction of the Market Stabilisation Scheme (MSS) and the hike in the repo and reverse repo rates by 25 basis points each effective June 9, 2006. After remaining broadly unchanged during July-November 2006, yields on Treasury Bills increased from December 2006 following hikes in the CRR and the repo rate (Chart 41). The yield spread between

Chart 41: Yields on Treasury Bills

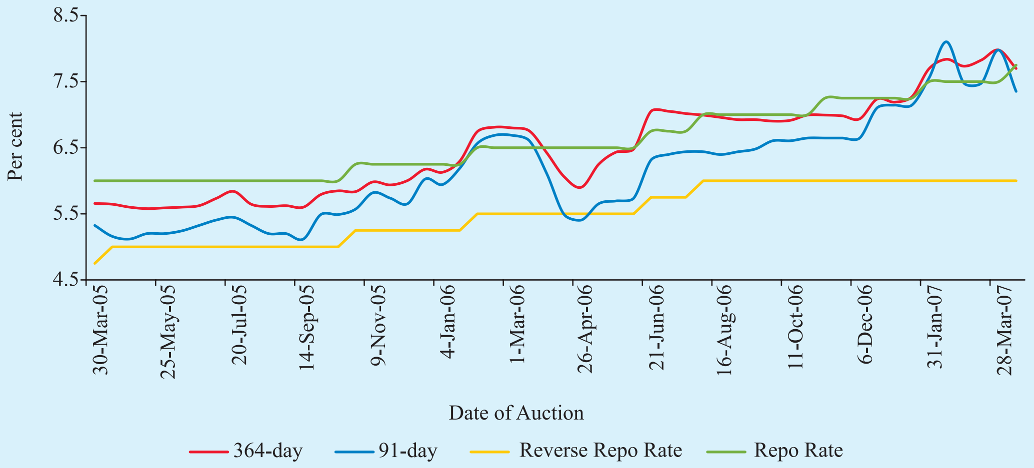


Table 44: Treasury Bills in the Primary Market

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**	**2.58**	**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	**1,86,500@**	**6.64**	**6.91**	**7.01**	**1.97**	**2.00**	**2.66**
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	19,000	7.28	7.45	7.39	1.02	1.35	1.74
February	15,000	7.72	7.67	7.79	2.48	2.56	3.16
March	15,000	7.68	7.98	7.90	2.08	2.15	3.87

@ : Total for the financial year.

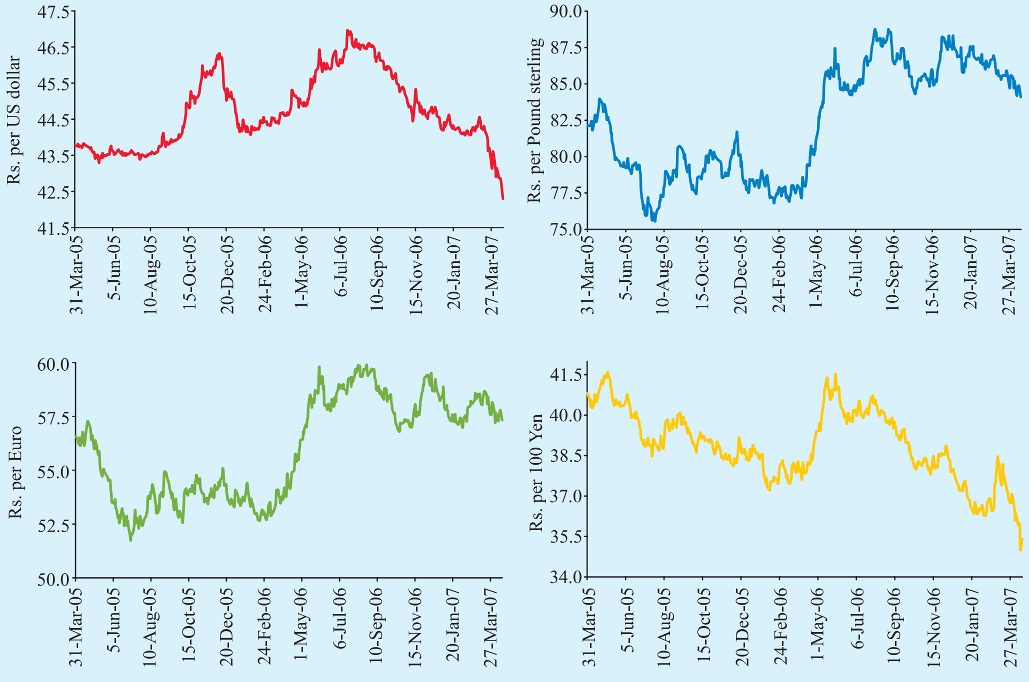
Note : 1. 182-day TBs were reintroduced with effect from April 2005.
2. Notified amounts are inclusive of issuances under the Market Stabilisation Scheme (MSS).

364-day and 91-day TBs was 22 basis points in March 2007, marginally higher than that in March 2006 (15 basis points) (Table 44). The notified amount of Rs.1,500 crore each for auctions of the 91-day TBs under the MSS was not fully subscribed at some of the auctions during the year, reflecting tight liquidity conditions. There was, however, no devolvement on the PDs.

Foreign Exchange Market

In the foreign exchange market, the Indian rupee exhibited two-way movements during 2006-07 moving in a range of Rs.43.14–46.97 per US dollar (Chart 42). The rupee initially depreciated against the US dollar during the year, reaching Rs.46.97 on July 19, 2006, reflecting higher crude oil prices, FII outflows and geo-political risks in the Middle East region. The rupee, however, strengthened thereafter on the back of moderation in crude oil prices, revival of FII inflows and weakness of the US dollar in the international markets. The rupee appreciated further in the second half of March 2007 to reach Rs.43.14 per US dollar on March 28, 2007, due to increased supply of dollars in the market. The exchange rate at Rs.43.60 per US dollar as on March 30, 2007 recorded an appreciation of

Chart 42: Movement of Rupee *vis-a-vis* Major Currencies



2.3 per cent over its level as on March 31, 2006 (Rs.44.61 per US dollar). Reflecting cross-currency movements, the rupee depreciated by 9.1 per cent against the Pound sterling and 6.8 per cent against the euro but appreciated by 2.7 per cent against the Japanese yen over the same period. The exchange rate was Rs.41.91 per US dollar as on April 18, 2007.

The nominal effective exchange rate (NEER) of the Indian rupee (six-currency trade-based weights) appreciated by 3.1 per cent between April 2006 and April 18, 2007. Over the same period, the real effective exchange rate (REER) of the Indian rupee (six-currency trade-based weights) appreciated by 7.8 per cent (Table 45).

Forward premia increased during 2006-07 reflecting growing interest rate differential in view of increase in domestic interest rates (Chart 43). While one-month forward premia increased from 3.79 per cent in March 2006 to 6.99 per cent in March 2007, the six-month premia increased from 2.43 per cent to 3.80 per cent over the same period.

The turnover in the inter-bank segment of the foreign exchange market increased from US $ 405 billion in March 2006 to US $ 533 billion in March 2007 and that in the merchant segment from US $ 141 billion to US $ 192 billion

Table 45: Indices of Nominal and Real Effective Exchange Rate of the Indian Rupee (6-Currency Trade Based Weights)

Year/Month	Base : 1993-94 (April-March) = 100	
	NEER	REER
1	2	3
1993-94	100.00	100.00
2000-01	77.30	102.64
2001-02	75.89	102.49
2002-03	71.09	97.43
2003-04	69.75	98.85
2004-05	69.26	101.35
2005-06	71.41	106.67
2006-07 (P)	68.13	104.91
March 2006	71.61	108.11
April 2006	70.22	104.12
May 2006	67.95	101.91
June 2006	67.39	101.79
July 2006	66.79	101.26
August 2006 (P)	66.28	101.20
September 2006 (P)	67.04	103.86
October 2006 (P)	68.31	106.49
November 2006 (P)	68.53	107.12
December 2006 (P)	68.01	105.99
January 2007 (P)	68.97	108.20
February 2007(P)	69.10	108.57
March 2007(P)	68.91	108.35
April 18, 2007 (P)	72.40	112.21

NEER: Nominal Effective Exchange Rate. REER: Real Effective Exchange Rate. P: Provisional.

Note: Rise in indices indicates appreciation of the rupee and *vice versa*.

(Chart 44). The ratio of inter-bank to merchant turnover at 2.8 during 2006-07 was almost the same as in 2005-06.

Chart 43: Movement in Forward Premia

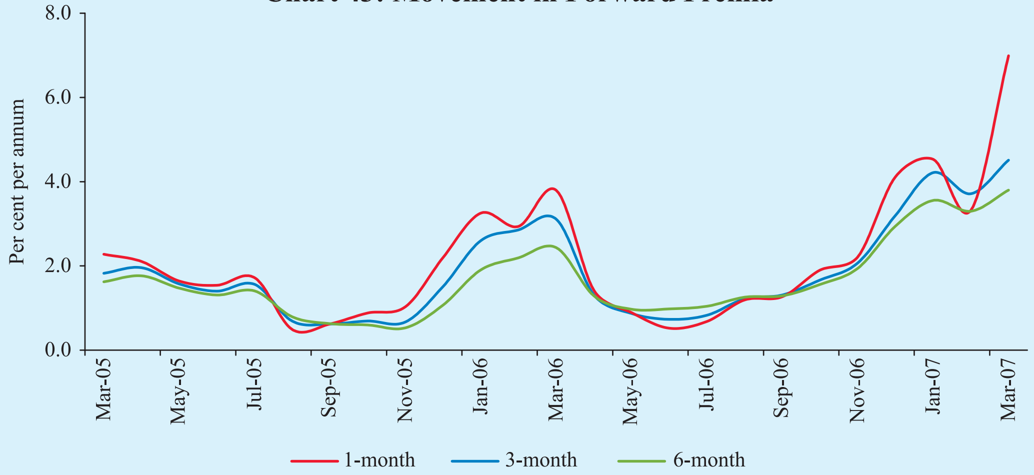
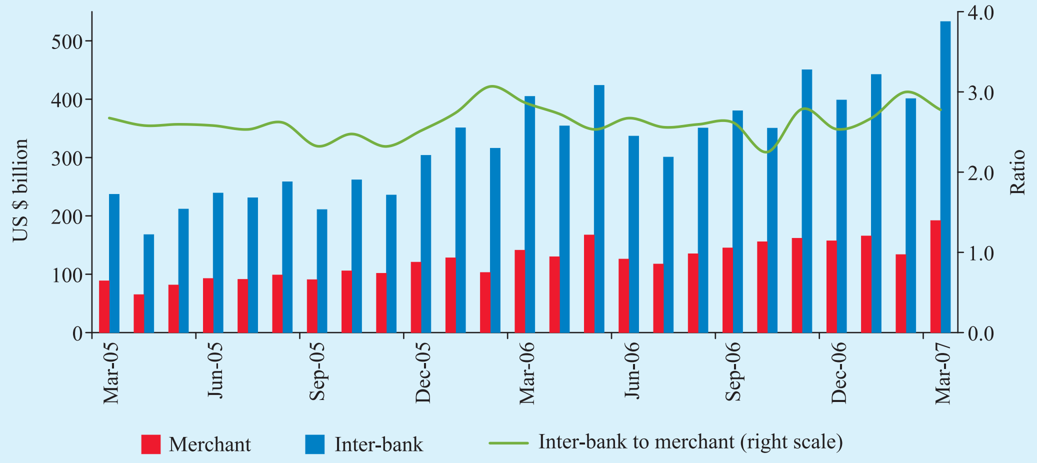


Chart 44: Turnover in Foreign Exchange Market



Credit Market

Both the deposit and lending rates of scheduled commercial banks (SCBs) increased during 2006-07. Interest rates offered by public sector banks (PSBs) on deposits of maturity of one year to three years were placed in the range of 7.25-9.50 per cent in March 2007 as compared with 5.75-6.75 per cent in March 2006, while those on deposits of maturity of above three years were placed in the range of 7.50-9.50 per cent in March 2007 as compared with 6.00-7.25 per cent in March 2006 (Table 46 and Chart 45). Similarly, interest rates offered by private sector banks on deposits of maturity of one year to three years were placed higher in the range of 6.75-9.75 per cent in March 2007 as compared with 5.50-7.75 per cent in March 2006, while those on deposits of maturity above three years were placed in the range of 7.75-9.60 per cent in March 2007 as compared with 6.00-7.75 per cent in March 2006. The rates offered by foreign banks on deposits of maturity of one year to three years were placed in the range of 3.50-9.50 per cent in March 2007 as compared with 4.00-6.50 per cent in March 2006.

As regards lending rates, the Benchmark Prime Lending Rates (BPLRs) of PSBs were placed in the range of 12.25-12.75 per cent in March 2007 as compared with that of 10.25-11.25 per cent in March 2006 (Table 46). The weighted average BPLR of public sector banks increased from 10.7 per cent in March 2006 to 11.6 per cent in December 2006 and further to 12.5 per cent in March 2007. Over the same period, the weighted average BPLR of private sector banks increased from 12.4 per cent in March 2006 to 13.2 per cent in December 2006 and further to 14.1 per cent in March 2007. The weighted average BPLR of

Table 46: Deposit and Lending Rates

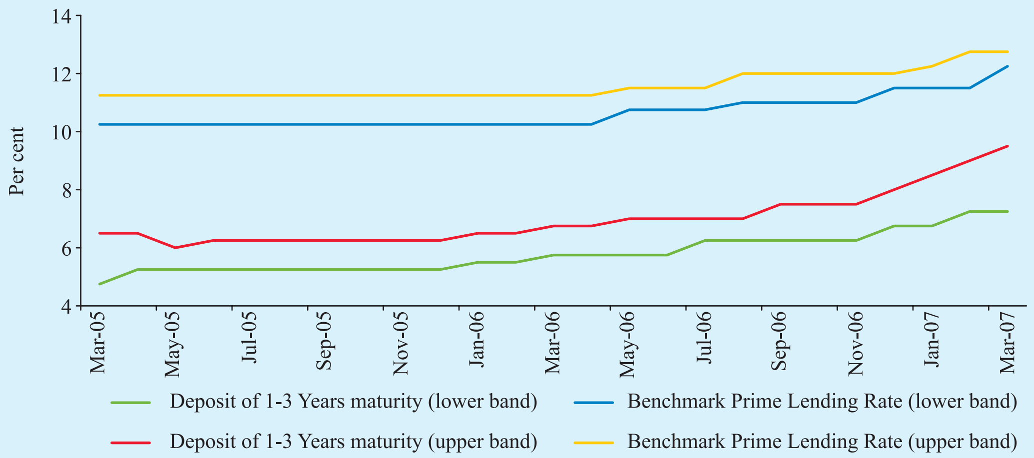
(Per cent)

Interest Rate	March 2005	March 2006	June 2006	September 2006	December 2006	March 2007
1	2	3	4	5	6	7
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	2.75-8.75
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	6.75-8.00	7.25-9.50
More than 3 years	5.25-7.00	6.00-7.25	6.00-7.25	6.50-8.00	7.00-8.00	7.50-9.50
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	3.00-9.00
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	6.40-8.50	6.75-9.75
More than 3 years	5.75-7.00	6.00-7.75	6.50-8.25	6.75-8.50	7.00-8.50	7.75-9.60
Foreign Banks						
Up to 1 year	3.00-6.25	3.00-6.15	3.25-6.50	3.00-7.50	3.00-7.25	3.00-9.50
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	3.50-9.50
More than 3 years	3.50-7.00	5.50-6.50	5.50-6.75	4.00-8.25	4.05-8.25	4.05-9.50
2. Benchmark Prime Lending Rate						
Public Sector Banks	10.25-11.25	10.25-11.25	10.75-11.50	11.00-12.00	11.50-12.00	12.25-12.75
Private Sector Banks	11.00-13.50	11.00-14.00	11.00-14.50	11.50-15.00	11.50-15.00	12.00-16.50
Foreign Banks	10.00-14.50	10.00-14.50	10.00-14.50	10.00-14.50	10.00-14.50	10.00-15.50
3. Actual Lending Rate*						
Public Sector Banks	2.75-16.00	4.00-16.50	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	3.15-24.00	–
Foreign Banks	3.55-23.50	4.75-26.00	4.75-25.00	4.50-23.00	4.50-26.50	–

* : 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.
– : Not available.

foreign banks at 12.7 per cent in March 2007 was the same as in December 2006 and in March 2006.

Chart 45: Deposit and Lending Rates - Public Sector Banks



Government Securities Market

The yields in the Government securities market hardened during 2006-07. Yields moved up from mid-April 2006 reflecting sustained credit demand, monetary policy tightening in the US and other economies, volatile crude oil prices, apprehensions over domestic fuel price hike, and hike in the reverse repo rate by 25 basis points effective June 9, 2006. Reflecting these factors, yields on 10-year paper reached an intra-year 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 target unchanged since end-June 2006, easing of crude oil prices, increased demand for gilts from banks to meet their SLR requirements and the announcement of the borrowing calendar of the Central Government for the second half of 2006-07 which 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 again some hardening of the yields from the second half of December 2006 in tandem with tightness in domestic liquidity conditions on the back of advance tax outflows, higher inflation and hikes in the CRR. The 10-year yield was 7.97 per cent as on March 31, 2007, 45 basis points higher than the level as on March 31, 2006 (7.52 per cent) (Chart 46). The yield was 8.07 per cent as on April 18, 2007. The yield curve flattened during 2006-07, with the spread between 1-10 year yields narrowing down to 42 basis points at end-March 2007 from 98 basis pints at end-March 2006. The spread between 10-year and 30-year yields, however, widened to 37 basis points at end-March 2007 from 30 basis points at end-March 2006.

The turnover in the Government securities market continued to be influenced by trends in yields. The turnover remained subdued during April-July 2006 as

Chart 46: Yields on Central Government Securities

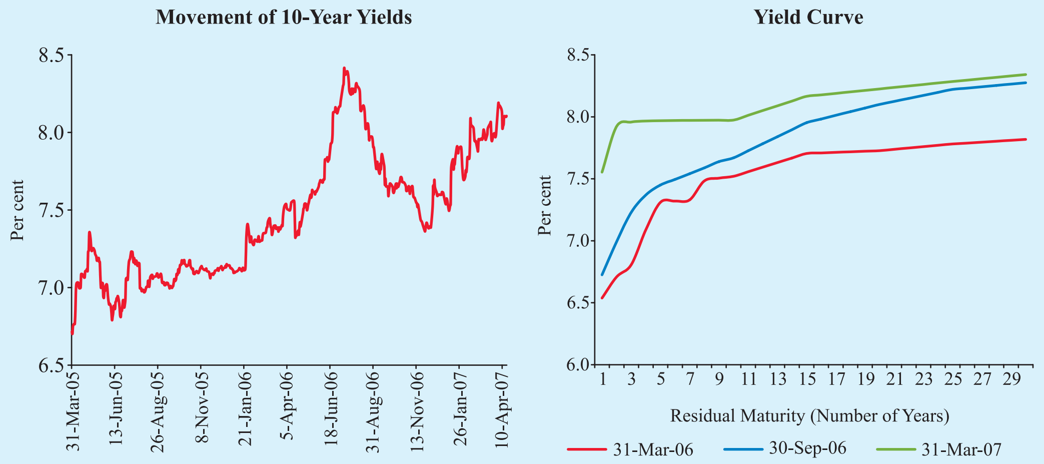
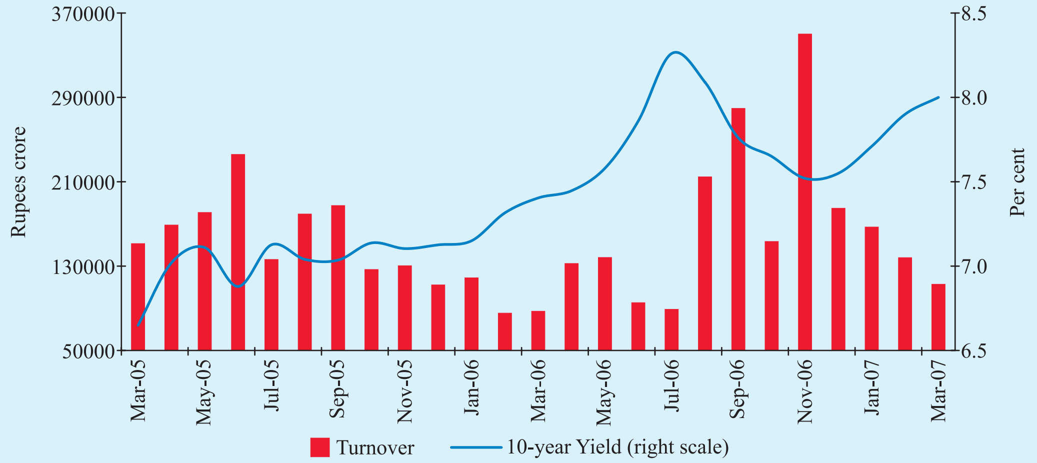


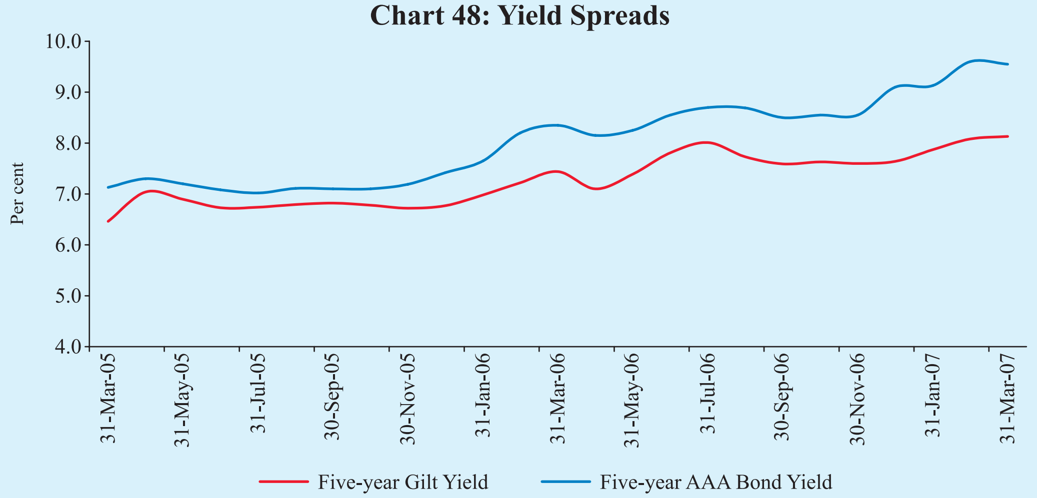
Chart 47: Government Securities Turnover and Yields



banks preferred to hold securities, rather than trade, in an environment of hardening of yields. The turnover, however, increased during August-November 2006 (the highest since June 2005) as yields trended downwards. The decline in turnover in October 2006 partly reflected lower number of trading days. The turnover again turned subdued from December 2006 as yields started hardening (Chart 47).

The yields on 5-year AAA-rated corporate bonds increased during 2006-07 in tandem with higher Government securities yield. The yield spread between 5-year AAA-rated bonds and 5-year Government securities, however, widened to 142 basis points at end-March 2007 from that of 91 basis points at end-March 2006 (Chart 48).

Chart 48: Yield Spreads



Equity Market

Primary Market

Resources raised through the public issues increased by 20.2 per cent to Rs.32,382 crore during 2006-07 (Table 47). The average size of issues increased to Rs.272 crore from Rs.195 crore during the corresponding period of the previous year. All issues, except one, during 2006-07 were by non-Government public limited companies (private sector) and mostly by non-financial companies. Out of 119 issues during the year, 75 issues were initial public offerings (IPOs) constituting 85.0 per cent of total resource mobilisation.

Mobilisation of resources through private placement increased by 50.8 per cent to Rs.1,03,169 crore during April-December 2006 over the corresponding period of the previous year (Table 47). This was mainly on account of a near doubling of resources mobilised by private sector entities to Rs.59,796 crore. Resources raised by public sector entities increased by only 11.4 per cent. Private sector entities, thus, raised more resources than public sector entities in contrast to the trend in 2005-06. Financial intermediaries (both from public sector and private sector) continued to account for the bulk of resource mobilisation from the private placement market (69.4 per cent of the total during April-December 2006 as compared with 64.1 per cent during April-December 2005).

Table 47: 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		2006-07 P	
A. Prospectus and Rights Issues*				
1. Private Sector (a+b)	**131**	**21,154**	**118**	**31,600**
a) Financial	11	7,746	9	2,420
b) Non-financial	120	13,408	109	29,180
2. Public Sector (a+b+c)	**7**	**5,786**	**1**	**782**
a) Public Sector Undertakings	–	–	–	–
b) Government Companies	1	373	–	–
c) Banks/Financial Institutions	6	5,413	1	782
3. Total (1+2)	**138**	**26,940**	**119**	**32,382**
Of which: (i) Equity	136	26,695	116	31,535
(ii) Debt	2	245	3	847
B. Private Placement@				
1. Private Sector	**673**	**29,501**	**1,111**	**59,796**
a) Financial	281	18,191	450	35,887
b) Non-financial	392	11,310	661	23,909
2. Public Sector	**108**	**38,926**	**84**	**43,373**
a) Financial	84	25,677	71	35,734
b) Non-financial	24	13,249	13	7,639
3. Total (1+2)	**781**	**68,427**	**1,195**	**1,03,169**
Of which: (i) Equity	1	150	1	57
(ii) Debt	780	68,277	1,194	1,03,112
C. Euro Issues	**48**	**11,352**	**40**	**17,005**

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

Table 48: Resource Mobilisation by Mutual Funds

(Rupees crore)

Mutual Fund	2005-06		2006-07	
	Net Mobilisation @	Net Assets	Net Mobilisation @	Net Assets
1	2	3	4	5
Private Sector	42,977	1,81,515	79,038	2,62,079
Public Sector	6,379	20,829	7,621	28,725
UTI	3,424	29,519	7,326	35,488
Total	**52,780**	**2,31,862**	**93,985**	**3,26,292**

@: Net of redemptions.
Source: Securities and Exchange Board of India.

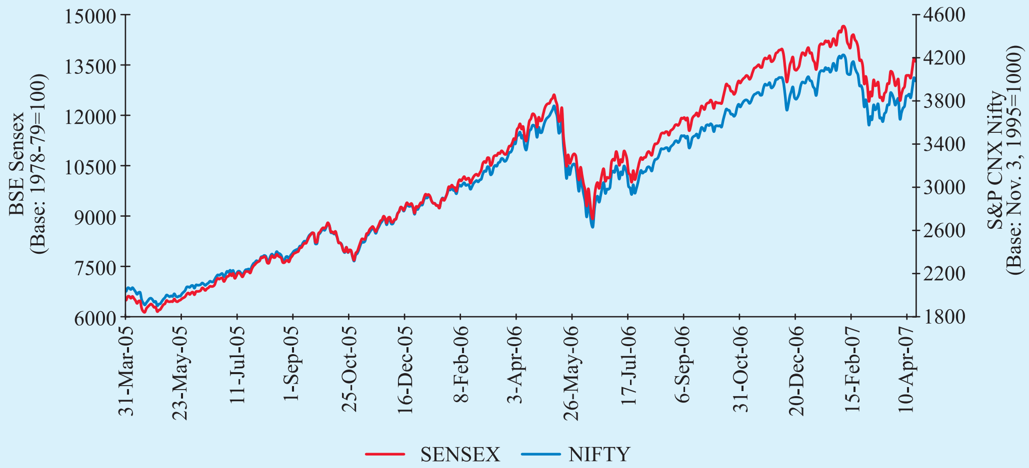
The resources raised through Euro issues - American Depository Receipts (ADRs) and Global Depository Receipts (GDRs) - by Indian corporates increased by 49.8 per cent to Rs.17,005 crore during 2006-07.

During 2006-07, net mobilisation of resources by mutual funds increased substantially by 78.1 per cent to Rs.93,985 crore over the corresponding period of previous year (Table 48). Bulk of the net mobilisation of funds (68.2 per cent of total) was under income/debt-oriented schemes, while growth/equity-oriented schemes accounted for 30.0 per cent of the net mobilisation of funds.

Secondary Market

The domestic stock markets recorded further gains during 2006-07 (Chart 49). FIIs investments in the domestic stock markets during 2006-07 were lower than a year ago. Mutual funds investments in the domestic stock markets

Chart 49: Indian Stock Markets



were also lower than a year ago. Growth in corporate profitability remained buoyant. Stock market gains were interspersed by some sharp corrections during the course of the year. In consonance with the trends in global equity markets, domestic stock markets witnessed correction during May-June 2006, December 2006 and February/ March 2007. The BSE Sensex reached an intra-year low of 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. The stock markets recouped these losses in the subsequent months and the BSE Sensex reached an all-time high of 14652 on February 8, 2007. The markets, however, witnessed some correction thereafter. The BSE Sensex closed at 13072 on March 30, 2007. The BSE Sensex, thus, increased by 15.9 per cent during 2006-07 (year-on-year) as compared with a gain of 73.7 per cent during 2005-06. The BSE Sensex was 13672 as on April 18, 2007.

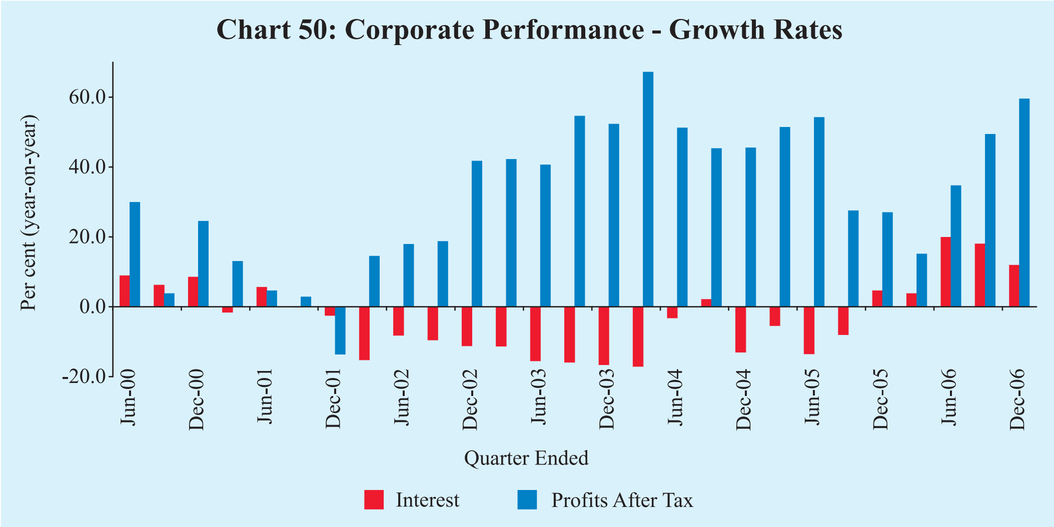
Profits after tax of corporates improved sharply in each of the first three quarters of 2006-07. Profits after tax of select non-Government non-financial companies increased by 48.7 per cent during April-December 2006 on top of 36.8 per cent growth recorded in the corresponding period of 2005. Ratio of profits after tax to sales improved to 11.0 per cent during the quarter ended December 2006 from 8.6 per cent a year ago (Table 49 and Chart 50).

Table 49: Corporate Financial Performance

(Growth rates in per cent)

Item	2004-05	2005-06	2005	2006	2005-06				2006-07		
			April-December		Q1	Q2	Q3	Q4	Q1	Q2	Q3
1	2	3	4	5	6	7	8	9	10	11	12
Sales	24.1	16.9	16.1	28.9	18.5	16.4	13.2	19.5	25.6	29.2	30.3
Expenditure	21.9	16.4	15.6	26.3	18.0	16.3	12.7	18.9	24.6	26.6	26.9
Depreciation Provision	11.2	10.2	7.0	16.7	4.4	7.4	10.2	13.2	14.9	16.4	16.8
Gross Profits	32.5	20.3	24.8	45.4	32.0	19.1	21.2	16.6	33.9	45.9	51.8
Interest	-5.8	1.9	-5.5	17.7	-13.5	-8.0	4.6	3.8	19.9	18.0	11.9
Profits After Tax	51.2	24.2	36.8	48.7	54.2	27.5	27.0	15.1	34.7	49.4	59.5
Select Ratios (Per cent)											
Gross Profits to Sales	11.9	13.0	13.8	16.1	13.1	13.0	12.8	12.7	15.6	15.9	15.8
Profits After Tax to Sales	7.2	8.7	9.1	11.1	8.6	8.5	8.6	8.7	10.6	11.0	11.0
Interest Coverage Ratio	4.6	6.4	6.1	7.8	6.0	6.2	6.2	7.3	7.2	7.8	8.0
Interest to Sales	2.6	2.0	2.3	2.1	2.2	2.1	2.1	1.7	2.2	2.0	2.0
Interest to Gross Profits	21.8	15.7	16.4	12.9	16.6	16.2	16.2	13.7	13.9	12.8	12.5
Memo:											(Amount in Rupees crore)
No. of Companies	2,214	2,210	2,251	1,933	2,355	2,361	2,366	2,415	2,228	2,263	2,258
Sales	5,49,449	7,74,578	5,79,881	6,80,662	1,94,608	2,12,693	2,19,098	2,49,971	2,34,610	2,51,125	2,60,064
Expenditure	5,14,574	6,66,690	4,95,284	5,64,331	1,66,972	1,83,717	1,88,934	2,18,511	1,95,556	2,09,437	2,16,053
Depreciation Provision	22,697	28,883	22,044	24,557	7,137	7,617	7,748	8,340	8,449	8,892	9,172
Gross Profits	65,301	1,00,666	79,937	1,09,432	25,577	27,620	28,135	31,652	36,567	40,041	41,169
Interest	14,268	15,789	13,095	14,137	4,241	4,467	4,555	4,348	5,083	5,121	5,162
Profits After Tax	39,599	67,506	52,891	75,460	16,726	18,169	18,790	21,634	24,845	27,710	28,698

Note :
1. Growth rates are percentage changes in the level for the period under reference over the corresponding period of the previous year.
2. Data in column (2) are based on audited balance sheets, while those in column (3) onwards are based on the abridged results of the sample non-Government non-financial companies.
3. Data for the full year and for the nine months period may not add to the quarterly totals due to difference in the number of companies covered.



According to the Securities and Exchange Board of India (SEBI), FIIs made net purchases of Rs.25,236 crore (US $ 6.0 billion) during 2006-07 on top of net purchases of Rs.48,542 crore (US $ 11.0 billion) during the previous year. Mutual funds also made net investments of Rs.9,024 crore during 2006-07 as compared with net purchases of Rs.14,302 crore during the previous year (Chart 51).

Major stock indices and sectors showed mixed trends during 2006-07 (Chart 52). On a point-to-point basis, the BSE 500 and the BSE Mid-cap increased by 9.7 per cent and 0.7 per cent, respectively, while the BSE Small-cap declined

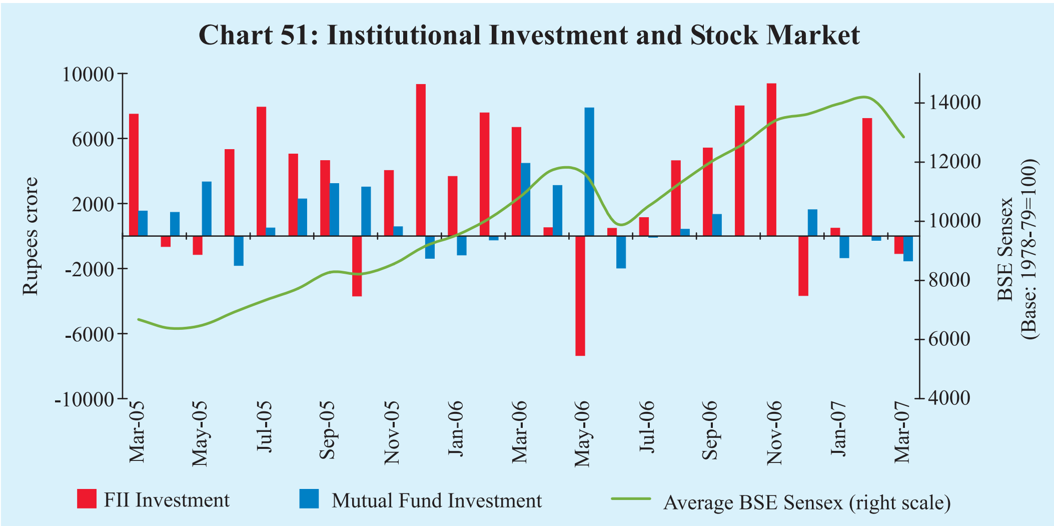
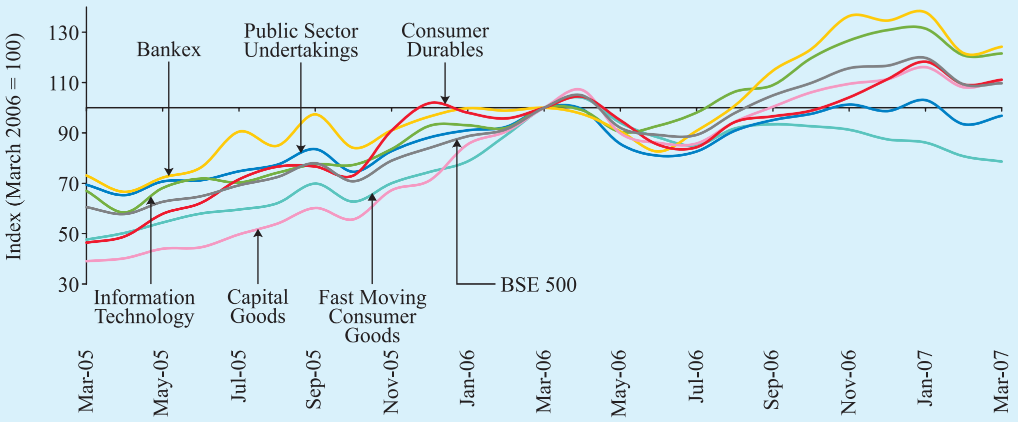


Chart 52: Trends in BSE Sectoral Stock Indices



by 1.9 per cent. Amongst major sectors, oil and gas stocks recorded gains of 30.5 per cent, followed by bank stocks (24.2 per cent), IT (21.6 per cent), consumer durables (11.1 per cent) and capital goods (11.1 per cent). However, losses were noticed in the fast moving consumer goods sector (21.4 per cent), auto sector stocks (8.7 per cent), healthcare (5.4 per cent), metals (4.3 per cent) and PSUs (3.2 per cent).

The price-earnings (P/E) ratio for the 30 scrips included in the BSE Sensex declined from 20.9 at end-March 2006 to 20.3 at end-March 2007 (Table 50). The market capitalisation of the BSE increased by 17.3 per cent between end-March 2006 and end-March 2007.

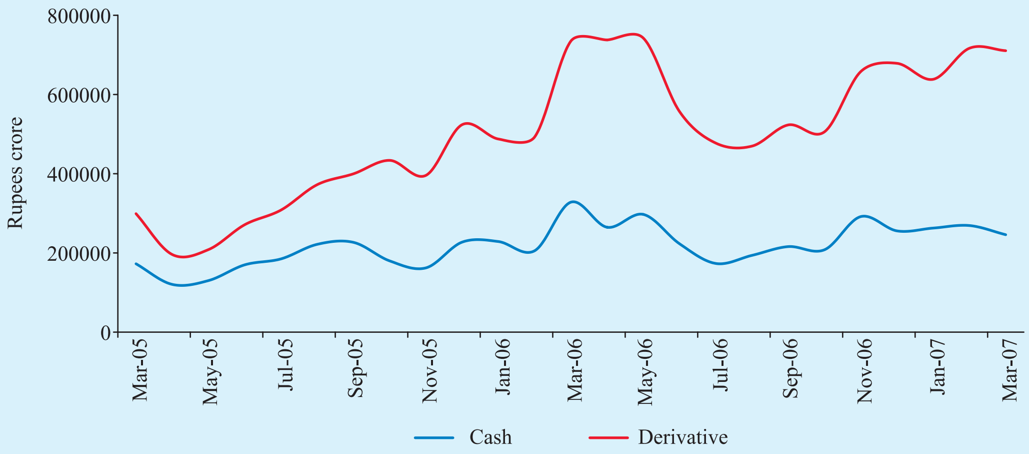
Table 50: Stock Market Indicators

Indicator	BSE			NSE		
	2004-05	2005-06	2006-07	2004-05	2005-06	2006-07
1	2	3	4	5	6	7
BSE Sensex / S&P CNX Nifty*						
End-period	6493	11280	13072	2036	3403	3822
Average	5741	8280	12277	1805	2513	3572
Volatility# (Per cent)	11.2	16.7	9.0	11.3	15.6	10.5
P/E Ratio (end-period)*	15.6	20.9	20.3	14.6	20.3	18.4
Turnover (Rupees crore)	5,18,716	8,16,074	9,56,185	11,40,071	15,69,556	19,44,645
Market Capitalisation (Rupees crore) (end-period)	16,98,429	30,22,190	35,45,041	15,85,585	28,13,201	33,67,350

* : For 30 scrips included in the BSE Sensex and 50 scrips included in the S&P CNX Nifty.
\# : Volatility is measured by coefficient of variation.
Source : Bombay Stock Exchange Limited (BSE) and National Stock Exchange of India Limited (NSE).

Total turnover (BSE and NSE) in the cash segment during 2006-07 at Rs.29,00,830 crore was 21.7 per cent higher than that in the corresponding period of 2005-06 (Chart 53). Total turnover (BSE and NSE) in the derivative segment increased by 53.7 per cent during 2006-07 to Rs.74,15,448 crore.

Chart 53: Turnover in Cash and Derivative Segment - BSE and NSE



VI. THE EXTERNAL ECONOMY

Merchandise exports, based on Directorate General of Commercial Intelligence and Statistics (DGCI&S) data, recorded a growth of 19.3 per cent during 2006-07 (April-February), lower than that of 26.3 per cent in the corresponding period of 2005-06. Growth in non-oil imports was led by imports of capital goods, indicative of strong investment demand, partly offsetting the decline in imports of pearls, precious and semi-precious stones. Growth in oil imports remained large, although there was some deceleration in consonance with the moderation in international crude oil prices. Net invisibles surplus expanded further during the first three quarters of 2006-07, benefiting from continued growth in exports of services and remittances, and financed a large part of the deficit on the merchandise trade account. The current account deficit was marginally lower than a year ago. Capital flows were substantially higher, led by foreign direct investment (FDI) flows and supported by foreign institutional investors (FIIs) flows and debt flows (external commercial borrowings and non-resident deposits). Outward FDI flows associated with acquisitions by Indian corporates abroad also increased. Capital flows (net) more than financed the current account deficit, resulting in the net accretion of US $ 47.6 billion in foreign exchange reserves during 2006-07.

International Developments

Global economic growth at 5.4 per cent during 2006 (4.9 per cent in 2005) turned out to be stronger than expected, led by a broad-based upswing in advanced economies and rapid growth in the emerging market economies. After a strong first quarter, economic activity in the US slowed down on the back of a significant weakening of the housing market. Nonetheless, for the year 2006, as a whole, economic growth in the US was marginally higher than in 2005. The economic activity in the euro area accelerated to 2.6 per cent – the highest since 2001– led by strong domestic as well as external demand. The Japanese economy expanded at a higher rate than in 2005. Growth momentum remained strong in China, India and other emerging economies as well (Table 51). Developing Asia recorded a growth of 9.4 per cent during 2006, the highest since 1995.

According to the International Monetary Fund (IMF) projections, the global economy is likely to maintain its run of strong growth during 2007, though with some loss of momentum (4.9 per cent from 5.4 per cent in 2006) (Table 52). There are also some downside risks to global growth prospects. These include revival of inflationary pressures in view of narrowing output gaps, the possibility of renewed oil price rise, sharper slowdown in the US economy in case the housing

Table 51: Growth Rates – Global Scenario

(Per cent)

Country	2004	2005	2006	2007 P	2008 P	2005	2006			
						Q4	Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8	9	10	11
Advanced Economies										
Euro area	2.0	1.4	2.6	2.3	2.3	1.8	2.2	2.7	2.6	3.3
Japan	2.7	1.9	2.2	2.3	1.9	2.8	2.9	2.1	1.5	2.3
Korea	4.7	4.2	5.0	4.4	4.4	5.3	6.3	5.1	4.8	4.0
UK	3.3	1.9	2.7	2.9	2.7	1.8	2.4	2.7	2.9	3.0
US	3.9	3.2	3.3	2.2	2.8	3.1	3.7	3.5	3.0	3.1
OECD Countries	3.2	2.5	3.0	2.5	2.7	3.0	3.3	3.3	2.9	3.3
Emerging Economies										
Argentina	9.0	9.2	8.5	7.5	5.5	9.1	8.6	7.9	8.7	8.6
Brazil	5.7	2.9	3.7	4.4	4.2	1.4	3.4	1.2	3.2	3.8
China	10.1	10.4	10.7	10.0	9.5	9.9	10.3	10.9	10.7	10.7
India	7.5	9.0	9.2	8.4	7.8	9.3	10.0	8.9	9.2	8.6
Indonesia	5.0	5.7	5.5	6.0	6.3	5.0	5.0	5.0	5.9	6.1
Malaysia	7.2	5.2	5.9	5.5	5.8	5.2	5.3	6.2	5.8	5.7
Thailand	6.3	4.5	5.0	4.5	4.8	4.3	6.1	5.0	4.7	4.2

P : IMF Projections.
Note : Data for India in columns 2 to 4 refer to fiscal years 2004-05, 2005-06 and 2006-07, respectively.
Source : International Monetary Fund; The Economist; and the OECD.

sector continues to deteriorate, financial market volatility and possible disorderly adjustment of global imbalances.

Table 52: Select Economic Indicators – World

Item	2001	2002	2003	2004	2005	2006	2007P	2008P
1	2	3	4	5	6	7	8	9
I. World Output (Per cent change) #	2.5	3.1	4.0	5.3	4.9	5.4	4.9	4.9
	(1.5)	(1.8)	(2.6)	(4.0)	(3.3)	(3.9)	(3.4)	(3.5)
i) Advanced economies	1.2	1.6	1.9	3.3	2.5	3.1	2.5	2.7
ii) Other emerging market and developing countries	4.3	5.0	6.7	7.7	7.5	7.9	7.5	7.1
of which: Developing Asia	6.0	7.0	8.4	8.7	9.2	9.4	8.8	8.4
II. Consumer Price Inflation (Per cent)								
i) Advanced economies	2.1	1.5	1.8	2.0	2.3	2.3	1.8	2.1
ii) Other emerging market and developing countries	6.7	5.8	5.8	5.6	5.4	5.3	5.4	4.9
of which: Developing Asia	2.7	2.0	2.5	4.1	3.6	4.0	3.9	3.4
III. Net Capital Flows* (US $ billion)								
i) Net private capital flows (a+b+c)	70.2	88.3	173.3	238.6	257.2	255.8	252.7	259.3
a) Net private direct investment	182.8	152.2	165.3	190.0	266.3	266.9	283.7	288.9
b) Net private portfolio investment	-80.5	-90.9	-12.1	25.0	29.4	-76.3	-62.0	-52.2
c) Net other private capital flows	-32.1	26.9	20.1	23.5	-38.5	65.2	30.9	22.6
ii) Net official flows	6.6	2.3	-44.5	-57.8	-122.6	-143.8	-96.4	-116.6
IV. World Trade @								
i) Volume	0.2	3.4	5.4	10.6	7.4	9.2	7.0	7.4
ii) Price deflator (in US dollars)	-3.5	1.2	10.4	9.8	5.5	5.4	2.8	0.8
V. Current Account Balance (Per cent to GDP)								
i) US	-3.8	-4.5	-4.8	-5.7	-6.4	-6.5	-6.1	-6.0
ii) China	1.3	2.4	2.8	3.6	7.2	9.1	10.0	10.5
iii) Middle East	6.2	4.7	8.4	12.1	18.8	18.1	12.1	10.7

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, April 2007.

Table 53: Growth in Exports - Global Scenario

(Per cent)

Region/Country	2005	2006
1	2	3
World	**14.0**	**15.7**
Industrial Countries	**8.5**	**12.6**
US	10.8	14.5
France	4.3	10.8
Germany	7.3	15.1
Japan	5.2	9.2
Developing Countries	**21.8**	**19.7**
Non-Oil Developing Countries	**19.2**	**19.7**
China	28.4	27.2
India	29.6	21.1
Indonesia	18.2	16.5
Korea	12.0	14.5
Malaysia	12.0	14.0
Singapore	15.6	18.4
Thailand	14.5	18.7

Source: International Financial Statistics, International Money Fund; DGCI&S for India.

Global merchandise trade grew at a robust pace in 2006 benefiting from favourable economic conditions, high commodity prices and recovery in global investment. Exports of developing countries, notwithstanding some deceleration, continued to post a higher growth in comparison with industrial countries (Table 53).

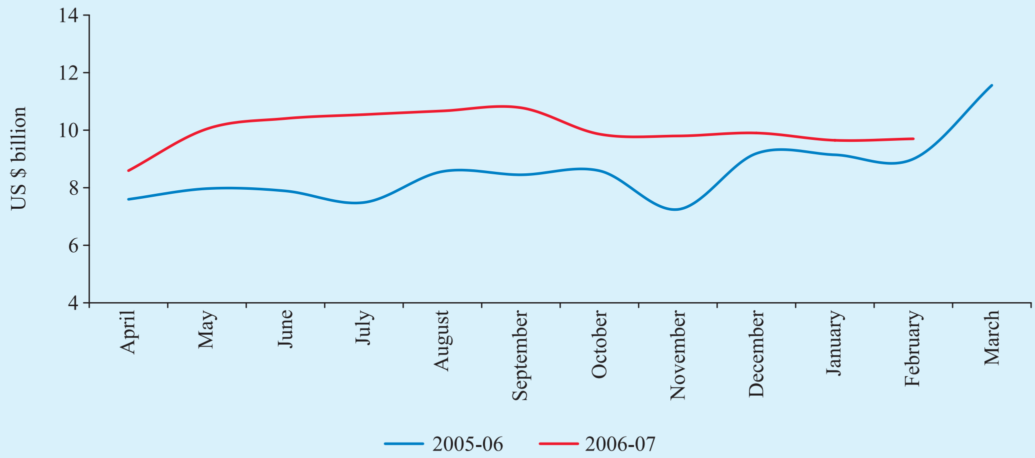
Merchandise Trade

According to the provisional data released by the Directorate General of Commercial Intelligence and Statistics (DGCI&S), India's merchandise exports during April-February 2006-07 registered a growth of 19.3 per cent as compared with 26.3 per cent a year ago. The export growth was strong in the first half (April-September 2006) of the fiscal at 27.2 per cent, but decelerated to 14.3 per cent during October 2006-February 2007 (Chart 54).

Commodity-wise data available for April-November 2006 reveal that engineering goods and petroleum products were the major growth drivers, together contributing almost 64 per cent of the export growth during this period. Gems and jewellery, textiles, and ores and minerals, on the other hand, showed decline or deceleration in exports (Table 54). Agriculture and allied products posted strong growth, driven mainly by the increase in the exports of sugar and molasses and raw cotton. Traditional export items like tea, coffee, tobacco and spices also maintained high growth, while exports of rice, wheat, cashew and marine products declined or decelerated.

The US continued to be the major destination of India's exports with a share of 15.4 per cent in 2006-07 (April-November) followed by the UAE (9.9 per cent), China (5.9 per cent), Singapore (5.2 per cent) and the UK (4.5 per cent)

Chart 54: India's Merchandise Exports



(Table 55). Among the major countries, growth in exports to the UAE accelerated to 57.4 per cent from 22.3 per cent a year ago. On the other hand, growth in exports to China, Singapore and Hong Kong decelerated.

India's merchandise imports registered a growth of 27.8 per cent during April-February 2006-07 on top of 32.7 per cent growth a year ago. After showing a slowdown in the latter half of 2005-06, non-oil imports have picked up since

Table 54: Exports of Principal Commodities

Commodity Group	US $ billion			Variation (per cent)		
	2005-06	2005-06	2006-07	2005-06	2005-06	2006-07
		April-November			April-November	
1	2	3	4	5	6	7
1. Primary Products	**16.4**	**9.6**	**11.4**	**20.8**	**29.7**	**18.9**
of which:						
a) Agriculture and Allied Products	10.2	6.0	7.4	20.5	20.4	23.5
b) Ores and Minerals	6.2	3.6	4.0	21.4	49.1	11.2
2. Manufactured Goods	**72.2**	**45.5**	**53.5**	**18.9**	**25.2**	**17.7**
of which:						
a) Chemicals and Related Products	14.8	9.0	10.9	18.6	23.3	21.0
b) Engineering Goods	21.5	13.4	18.5	23.7	33.2	38.5
c) Textiles and Textile Products	16.3	10.1	11.0	20.6	21.8	8.6
d) Gems and Jewellery	15.5	10.3	10.2	12.8	22.5	-0.8
3. Petroleum Products	**11.5**	**7.2**	**12.8**	**64.9**	**63.0**	**79.1**
4. Total Exports	**103.1**	**63.9**	**80.9**	**23.4**	**29.4**	**26.6**
Memo:						
Non-oil Exports	91.6	56.7	68.1	19.6	26.1	20.0

Source : DGCI&S.

Table 55: Direction of India's Exports

Group/Country	US $ billion			Variation (per cent)		
	2005-06	2005-06	2006-07	2005-06	2005-06	2006-07
		April-November			April-November	
1	2	3	4	5	6	7
1. OECD Countries	**45.8**	**28.7**	**33.4**	**25.6**	**29.3**	**16.2**
of which:						
a) EU	22.4	14.0	16.3	27.6	34.5	17.1
b) North America	18.4	11.6	13.2	25.6	25.6	13.0
US	17.4	11.0	12.4	26.1	25.9	12.8
2. OPEC	**15.2**	**9.1**	**13.6**	**15.4**	**19.9**	**50.1**
of which:						
UAE	8.6	5.1	8.0	16.9	22.3	57.4
3. Developing Countries	**39.7**	**24.6**	**32.0**	**25.8**	**35.8**	**30.1**
of which:						
Asia	31.0	19.2	23.8	24.1	35.6	23.7
People's Republic of China	6.8	3.9	4.8	20.4	56.5	22.7
Singapore	**5.4**	3.6	4.2	19.3	63.0	15.3
4. Total Exports	**103.1**	**63.9**	**80.9**	**23.4**	**29.4**	**26.6**

Source : DGCI&S.

September 2006 (Chart 55). During April-February 2006-07, non-oil imports grew by 25.7 per cent and accounted for almost 64 per cent of the rise in total imports.

Major import items like capital goods maintained high growth during April-November 2006, while imports of mainly export related items, particularly, pearls, precious and semi-precious stones declined (Table 56). Imports of capital goods increased by 38.2 per cent during April-November 2006, over and above

Chart 55: India's Non-Oil Imports

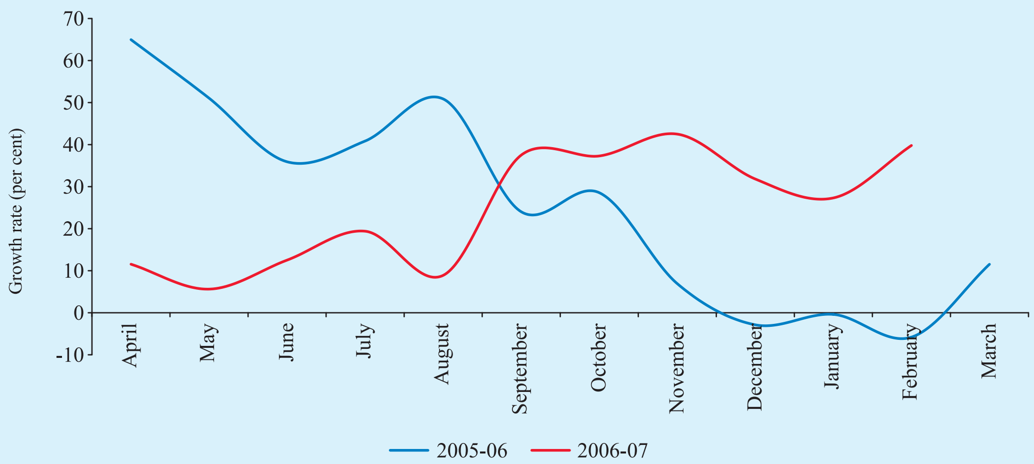


Table 56: Imports of Principal Commodities

Commodity Group	US $ billion			Variation (per cent)		
	2005-06	2005-06	2006-07	2005-06	2005-06	2006-07
		April-November			April-November	
1	2	3	4	5	6	7
Petroleum, Petroleum Products and Related Material	44.0	27.8	39.4	47.3	43.3	41.9
Edible Oils	2.0	1.5	1.5	-17.9	-9.2	3.2
Iron and Steel	4.6	3.2	4.1	71.3	106.4	28.4
Capital Goods	37.7	19.6	27.1	49.9	45.7	38.2
Pearls, Precious and Semi-Precious Stones	9.1	6.7	5.0	-3.1	30.8	-25.6
Chemicals	7.0	4.7	5.2	22.5	37.5	11.8
Gold and Silver	11.3	8.0	9.6	1.5	27.4	21.3
Total Imports	**149.2**	**93.5**	**119.4**	**33.8**	**41.2**	**27.8**
Memo:						
Non-oil Imports	105.2	65.7	80.0	28.8	40.4	21.8
Non-oil Imports excluding Gold and Silver	93.9	57.8	70.4	33.1	42.4	21.8
Mainly Industrial Imports*	87.5	53.3	64.5	34.7	43.8	21.1

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

the growth of 45.7 per cent recorded a year ago, reflecting the continued buoyancy in domestic investment activity. Imports of gold and silver registered a sharp jump during September-November 2006, offsetting the decline during April-August 2006. As a result, the cumulative growth was 21.3 per cent during April-November 2006.

Oil imports during April-February 2006-07 rose by 32.6 per cent on top of 49.7 per cent a year ago, reflecting partly the increase in volumes. In volume terms, oil imports increased by 22.5 per cent during April-November 2006 as compared with a growth of 0.8 per cent a year ago. Growth in the Indian basket of crude oil prices, on the other hand, decelerated to 12.7 per cent during 2006-07 from 42.3 per cent during 2005-06.

Source-wise, during April-November 2006, China was the major source of imports with a share of 9.3 per cent in India's total imports, followed by Saudi Arabia (7.9 per cent), the US (5.8 per cent), Switzerland (4.9 per cent) and the UAE (4.7 per cent).

Trade deficit at US $ 55.8 billion during 2006-07 (April-February), according to the DGCI&S data, was higher by 48.5 per cent than the previous year (US $ 37.6 billion) (Table 57). The deficit on the oil account increased by US $ 6.0 billion during April-November 2006 over the corresponding period of 2005, while the non-oil trade deficit increased by US $ 3.0 billion.

Table 57: India's Merchandise Trade

(US $ billion)

Item	2004-05	2005-06	2005-06 April-February	2006-07 April-February
1	2	3	4	5
Exports	83.5	103.1	91.5	109.2
Imports	111.5	149.2	129.1	165.0
Oil	29.8	44.0	39.8	52.7
Non-oil	81.7	105.2	89.3	112.3
Trade Balance	-28.0	-46.1	-37.6	-55.8
Non-Oil Trade Balance	-5.1	-13.6	-9.0 *	-11.9 *
				Variation (per cent)
Exports	30.8	23.4	26.3	19.3
Imports	42.7	33.8	32.7	27.8
Oil	45.1	47.3	49.7	32.6
Non-oil	41.8	28.8	26.4	25.7

*: April-November.

Source : DGCI&S.

Current Account

Buoyant net surplus under invisibles (services, transfers and income taken together) continued to finance bulk of the trade deficit during 2006-07 (April-December). Amongst major services, net surplus under software services increased by 29.1 per cent to US $ 20.1 billion during April-December 2006 (Table 58). Private transfers (net) at US $ 18.8 billion during April-December 2006 were 11.6 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 increased to US $ 40.5 billion during April-December 2006 from US $ 28.1 billion a year ago.

Table 58: Invisibles Account (Net)

(US $ million)

Item	2005-06 PR	2005-06 PR	2006-07 P	2005-06 PR	2006-07		
	April-March	April-December		Oct.-Dec.	April-June PR	July-Sept. PR	Oct.-Dec.P
1	2	3	4	5	6	7	8
Services	23,881	16,416	25,064	4,690	8,612	7,459	8,993
Travel	1,389	788	981	516	220	-31	792
Transportation	-1550	-1,087	-450	-405	-314	-31	-105
Insurance	22	100	365	-126	111	162	92
Government, not included elsewhere	-197	-107	-97	-18	-24	-62	-11
Software	22,262	15,597	20,143	5,755	6,601	6,678	6,864
Other Services	1,955	1,125	4,122	-1,032	2,018	743	1,361
Transfers	24,284	16,937	18,943	6,436	5,689	5,222	8,032
Investment Income	-4,921	-4,741	-3,100	-2,706	-1,043	-1,144	-913
Compensation of Employees	-589	-465	-426	-222	-131	-162	-133
Total	**42,655**	**28,147**	**40,481**	**8,198**	**13,127**	**11,375**	**15,979**

PR : Partially Revised. P : Preliminary.

The net invisible surplus financed 77.4 per cent of the merchandise trade deficit during April-December 2006. Current account deficit at US $ 11.8 billion in April-December 2006 was marginally lower than that in the corresponding period of the previous year on account of higher net invisibles receipts (Table 59 and Chart 56).

Capital Flows

Capital flows during 2006-07 were substantially higher than a year ago, led by foreign direct investment (FDI) flows, on the back of strong growth prospects and buoyant investment demand. FDI inflows at US $ 16.4 billion during April-January 2006-07 were substantially higher than the inflows in the corresponding period of the previous year (Table 60). FDI was channelled mainly into financial services, manufacturing, banking services, information technology services and construction. Mauritius, the US and United Kingdom remain the dominant sources of FDI to India. Outward direct investment from India also exhibited a significant rise to US $ 8.7 billion during April-December 2006 from US $ 1.9 billion a year ago due to some large overseas acquisitions by Indian corporates. Both FDI inflows

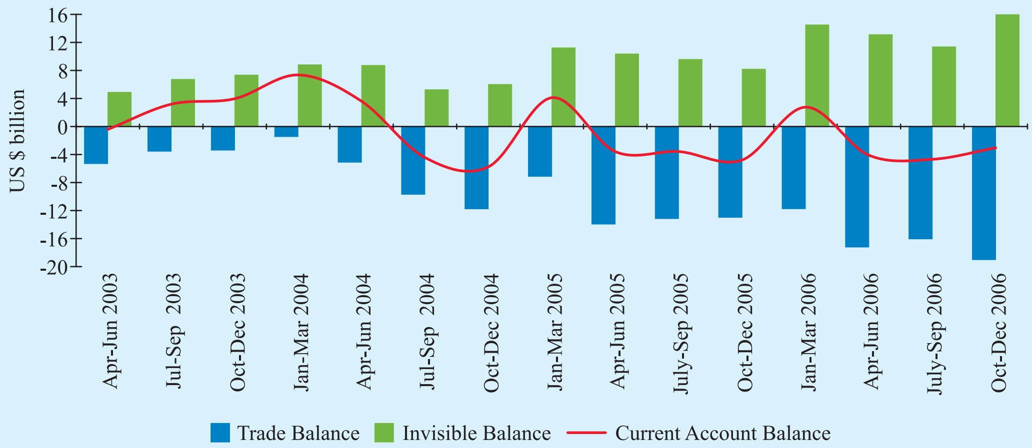
Table 59: India's Balance of Payments

(US $ million)

Item	2005-06 PR	2005-06 PR	2006-07 P	2005-06 PR	2006-07		
	April-March	April-December		Oct.-Dec.	April-June PR	July-Sept. PR	Oct.-Dec. P
1	2	3	4	5	6	7	8
Exports	1,05,152	74,573	91,334	25,318	29,674	32,798	28,862
Imports	1,56,993	1,14,662	1,43,636	38,298	46,898	48,855	47,883
Trade Balance	-51,841 (-6.4)	-40,089	-52,302	-12,980	-17,224	-16,057	-19,021
Invisible Receipts	92,294	63,594	82,633	23,990	25,056	25,576	32,001
Invisible Payments	49,639	35,447	42,152	15,792	11,929	14,201	16,022
Invisibles, net	42,655 (5.3)	28,147	40,481	8,198	13,127	11,375	15,979
Current Account	-9,186 (-1.1)	-11,942	-11,821	-4,782	-4,097	-4,682	-3,042
Capital Account (net)*	24,238 [29,738]@	13,773 [19,273]@	27,972	110 [5,610]@	10,475	6,950	10,547
of which:							
Foreign Direct Investment	4,730	3,347	5,822	1,218	1,273	2,268	2,281
Portfolio Investment	12,494	8,161	5,170	2,748	-527	2,141	3,556
External Commercial Borrowings $	2,723 [8,223]@	-1,211 [4,289]@	9,104	-4,136 [1,364]@	3,947	1,324	3,833
Short-term Trade Credit	1,708	1,731	1,329	759	417	1,554	-642
External Assistance	1,682	1,090	934	681	41	337	556
NRI Deposits	2,789	1,114	3,201	881	1,231	798	1,172
Change in Reserves #	-15,052	-1,831	-16,151	4,672	-6,378	-2,268	-7,505

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

Chart 56: Current Account Balance



and outflows include one transaction amounting to US $ 3.1 billion involving swap of shares. Net of this transaction, FDI inflows and outflows were US $ 13.3 billion and US $ 5.6 billion, respectively, also indicating a significant increase over the previous year.

Portfolio equity inflows by foreign institutional investors (FIIs) were lower than a year ago due to outflows witnessed during a few months on the back of global developments such as meltdown in global commodities and equity markets (May-July 2006), fall in Asian equity markets subsequent to the tightening of capital controls by Thailand (December 2006) and fall in Asian equity markets on account of concerns of slowdown in the US economy (late February 2007). Capital inflows through the issuances of American depository receipts (ADRs)/Global depository receipts (GDRs) during April-January 2006-07 remained higher than in the previous year.

Table 60: Capital Flows

(US $ million)

Components	Period	2005-06	2006-07
1	2	3	4
Foreign Direct Investment (FDI) into India	April-January	5,821	16,444 #
FDI Abroad	April-December	(-)1,939	(-)8,684 #
FIIs (net)	April-March	9,926	3,224
ADRs/GDRs	April-January	2,141	3,506
External Assistance (net)	April-December	1,153	949
External Commercial Borrowings (net) (Medium and long-term)	April-December	4,420 @	9,275
Short-term Trade Credits (net)	April-December	1,731	1,329
NRI Deposits (net)	April-January	1,681	3,686

: Include swap of shares of US $ 3.1 billion. @: Excluding IMD redemption.

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.

Amongst debt flows, demand for external commercial borrowings (ECBs) remained strong in consonance with buoyant domestic investment activity. Net disbursements under ECBs during April-December 2006 were more than double of those a year ago. Net inflows under various NRI deposits during April-January 2006-07 were also more than twice that a year ago, partly attributable to higher interest rates on various deposit schemes up to January 2007. The ceiling interest rate on NRE deposits was raised by 25 basis points each in November 2005 and April 2006 before being scaled down by 50 basis points to "LIBOR/SWAP rates of US dollar *plus* 50 basis points" in January 2007. The ceiling interest rate on FCNR(B) deposits was raised by 25 basis points to "LIBOR/SWAP rates for the respective currency/ maturity" in March 2006 but was reduced by 25 basis points to "LIBOR/ SWAP rates *minus* 25 basis points" in January 2007.

Foreign Exchange Reserves

India's foreign exchange reserves were US $ 199.2 billion as on March 31, 2007, showing an increase of US $ 47.6 billion over end-March 2006 levels (Table 61). The increase in reserves was mainly due to increase in foreign currency assets from US $ 145.1 billion at end-March 2006 to US $ 191.9 billion as at end-March 2007. As on April 13, 2007, India's foreign exchange reserves were US $ 203.1 billion.

Table 61: 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	170,187	546	177,251
January 2007	6,529	10	173,081	541	180,161
February 2007	6,883	2	187,211	467	194,563
March 2007	6,784	2	191,924	469	199,179
April 2007*	6,784	2	195,844	462	203,092

- : Negligible.
* : As on April 13, 2007.

India holds the fifth largest stock of reserves among the emerging market economies. The overall approach to the 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 $ 142.7 billion at end-December 2006, an increase of US $ 16.2 billion over end-March 2006. The increase during the period was mainly on account of higher external commercial borrowings and NRI deposits. As noted earlier, higher commercial borrowings could be attributed to sustained investment and import demand, while the rise in NRI deposits was partly on account of higher interest rates on these deposits for the period. Almost 46 per cent of the external debt stock was denominated in US dollars followed by the Indian Rupee (19 per cent), SDR (14 per cent) and Japanese Yen (12 per cent). Sustainability indicators such as the ratio of short-term to total debt and short-term debt to reserves remained almost unchanged between end-March 2006 and end-December 2006 and continued to be at quite low and comfortable levels (Table 62). Foreign exchange reserves remain in excess of the stock of external debt.

Table 62: India's External Debt

(US $ million)

Indicator	End-March 1995	End-March 2005	End-March 2006	End-June 2006	End-Sept 2006	End-Dec 2006
1	2	3	4	5	6	7
1. Multilateral	28,542	31,702	32,559	33,101	33,594	34,569
2. Bilateral	20,270	16,930	15,727	15,833	15,734	15,770
3. International Monetary Fund	4,300	0	0	0	0	0
4. Trade Credit	6,629	4,980	5,398	5,498	5,658	5957
5. External Commercial Borrowings	12,991	27,024	26,869	31,114	32,421	35,980
6. NRI Deposit	12,383	32,743	35,134	35,651	36,515	38,382
7. Rupee Debt	9,624	2,301	2,031	1,915	1,921	1,983
8. Long-term (1 to 7)	94,739	1,15,680	1,17,718	1,23,112	1,25,843	132,641
9. Short-term	4,269	7,524	8,696	9,105	10,625	10,015
Total (8+9)	**99,008**	**1,23,204**	**1,26,414**	**1,32,217**	**1,36,468**	**142,656**
Memo:						(Per cent)
Total debt /GDP	30.8	17.3	15.8	..	..	..
Short-term/Total debt	4.3	6.1	6.9	6.9	7.8	7.0
Short-term debt/Reserves	16.9	5.3	5.7	5.6	6.4	5.7
Concessional debt/Total debt	45.3	33.0	31.2	30.1	29.3	28.3
Reserves/ Total debt	25.4	114.9	120.0	123.2	121.1	124.3
Debt Service Ratio*	25.9	6.1	9.9	..	..	..

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

International Investment Position

India's international assets increased by US $ 16.4 billion during the half year ended September 2006 over end-March 2006 levels, mainly on account of an increase in reserve assets. India's direct investment abroad also maintained its rising trend, reflecting growing investment interest by Indian companies in the overseas markets. International liabilities of the country expanded by US $ 14.5 billion between end-March 2006 and end-September 2006, reflecting inflows on account of direct and portfolio investment, recourse to commercial borrowings and non-resident deposits. As the increase in international assets exceeded that in international liabilities during the period, India's net international liabilities declined by US $ 1.9 billion between end-March 2006 and end-September 2006 (Table 63).

Table 63: International Investment Position of India

(US $ billion)

Period	March 2005 PR	March 2006 PR	June 2006 PR	September 2006 P
1	2	3	4	5
A. Assets	**168.2**	**183.5**	**191.8**	**199.9**
	(23.5)	**(22.9)**	**..**	**..**
1. Direct Investment	10.0	13.0	13.6	14.4
2. Portfolio Investment	0.8	1.3	1.1	1.2
2.1 Equity Securities	0.4	0.7	0.5	0.5
2.2 Debt Securities	0.4	0.6	0.6	0.7
3. Other Investment	15.9	17.6	14.2	18.9
3.1 Trade Credits	2.2	0.4	0.3	2.8
3.2 Loans	1.9	2.6	1.6	2.3
3.3 Currency and Deposits	8.4	11.2	8.9	10.3
3.4 Other Assets	3.4	3.5	3.5	3.6
4. Reserve Assets	141.5	151.6	162.9	165.3
	(19.8)	(19.0)	..	..
B. Liabilities	**210.0**	**231.3**	**238.3**	**245.8**
	(29.4)	**(28.9)**	**..**	**..**
1. Direct Investment	44.0	50.7	51.5	54.9
	(6.2)	(6.3)	..	..
2. Portfolio Investment	55.7	64.6	64.8	67.4
	(7.8)	(8.1)	..	..
2.1 Equity Securities	43.2	54.7	52.5	54.8
2.2 Debt Securities	12.5	9.9	12.4	12.6
3. Other Investment	110.3	116.0	122.0	123.5
	(15.4)	(14.5)	..	..
3.1 Trade Credits	9.6	10.5	10.9	12.4
3.2 Loans	65.7	68.2	70.7	72.2
3.3 Currency and Deposits	33.6	36.2	39.2	37.6
3.4 Other Liabilities	1.4	1.1	1.2	1.4
C. Net Position (A-B)	**-41.8**	**-47.8**	**-46.4**	**-45.9**
	(-5.9)	**(-6.0)**	**..**	**..**

PR : Partially Revised. P : Provisional.

Note : Figures in parentheses are percentages to GDP.