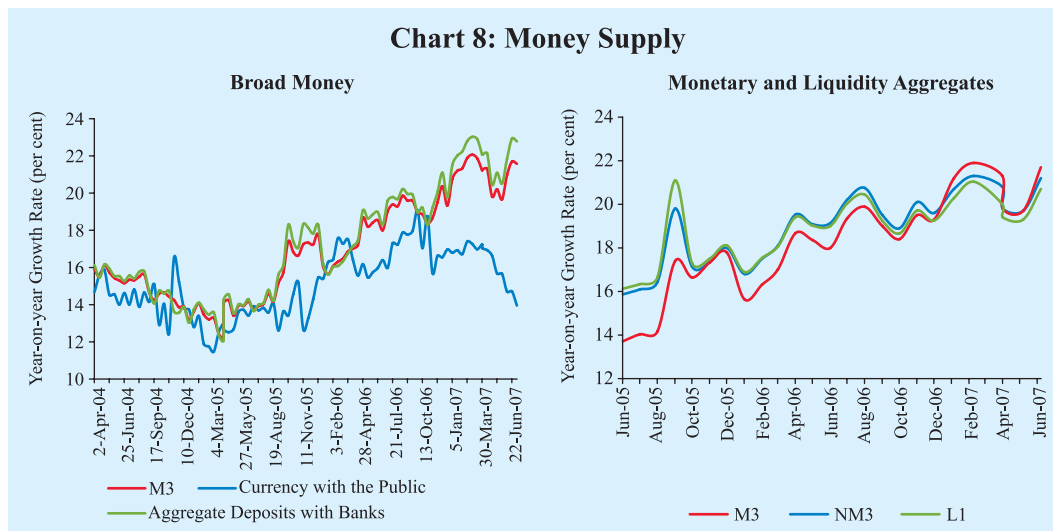


### III. MONETARY AND LIQUIDITY CONDITIONS

Growth in bank credit moderated during the first quarter of 2007-08 from the strong pace of the preceding three years. Accretion to banks' deposits remained buoyant, led by time deposits. Year-on-year growth of broad money ( $M_3$ ) on July 6, 2007 was marginally higher than that at end-March 2007, and also remained above the indicative trajectory of 17.0-17.5 per cent for 2007-08 set out in the Annual Policy Statement (April 2007). Banks' investments in SLR securities, as a proportion of their net demand and time liabilities (NDTL), rose during the quarter. Liquidity conditions continued to be dominated by movements in cash balances of the Governments and capital flows. The Reserve Bank modulated market liquidity with the help of issuances of securities under the Market Stabilisation Scheme (MSS), operations under the liquidity adjustment facility (LAF) and increase in the cash reserve ratio (CRR).

#### Monetary Survey

Growth in broad money ( $M_3$ ), year-on-year (y-o-y), was 21.6 per cent on July 6, 2007 as compared with 21.3 per cent at end-March 2007 and 19.0 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) deposits – also accelerated to 21.3 per cent on July 6, 2007 from 20.0 per cent a year ago. Growth in liquidity aggregate,  $L_1$ , at 20.7 per cent at end-June 2007 was higher than that of 20.4 per cent at end-March 2007 and 19.0 per cent a year ago (Chart 8 and Table 20).

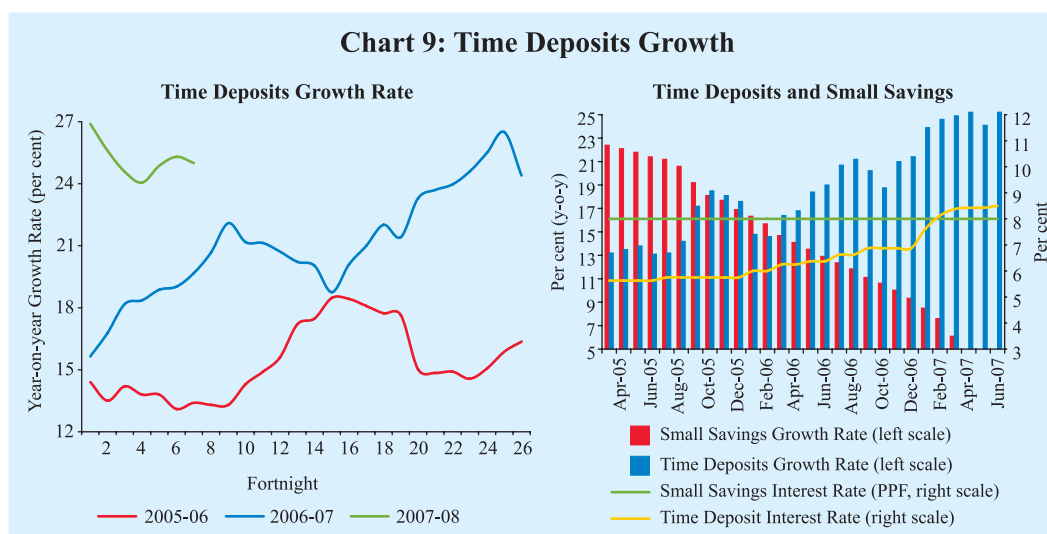


Monetary and Liquidity Conditions

**Table 20: Monetary Indicators**

(Amount in Rupees crore)							
Item	Outstanding as on July 6, 2007	Variation (year-on-year)					
		July 7, 2006		March 31, 2007		July 6, 2007	
		Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6	7	8
I. Reserve Money*	7,52,675	85,647	17.2	1,35,961	23.7	1,69,551	29.1
II. Narrow Money (M <sub>1</sub> )	9,55,793	1,39,774	20.6	1,38,820	16.8	1,38,933	17.0
III. Broad Money (M <sub>3</sub> )	34,34,643	4,51,636	19.0	5,80,733	21.3	6,09,610	21.6
a) Currency with the Public	4,97,817	60,216	16.0	70,352	17.0	60,960	14.0
b) Aggregate Deposits	29,25,038	3,90,409	19.6	5,09,754	22.1	5,42,766	22.8
i) Demand Deposits	4,46,188	78,547	26.6	67,841	16.7	72,089	19.3
ii) Time Deposits	24,78,850	3,11,862	18.4	4,41,913	23.2	4,70,677	23.4
of which: Non-Resident Foreign Currency Deposits	62,506	-13,174	-17.1	7,833	13.2	-1,185	-1.9
IV. NM <sub>3</sub>	34,41,815	4,73,728	20.0	5,70,274	20.8	6,03,306	21.3
of which: Call Term Funding from FIs	82,240	13,398	18.9	2,692	3.2	-2140	-2.5
V. a) L <sub>1</sub>	35,11,133	4,64,458	19.0	5,82,836	20.4	6,02,011	20.7
of which: Postal Deposits	1,15,204	14,301	15.4	11,286	10.9	-	-
b) L <sub>2</sub>	35,14,065	4,64,164	19.0	5,82,836	20.4	6,02,011	20.7
c) L <sub>3</sub>	35,40,129	4,67,208	18.9	5,85,059	20.3	6,04,234	20.6
VI. Major Sources of Broad Money							
a) Net Bank Credit to the Government (i+ii)	9,13,087	37,748	4.9	71,582	9.3	1,04,372	12.9
i) Net Reserve Bank Credit to Government	28,167	3,068	-	-2,384	-29.3	30,358	-
of which: to the Centre	27,847	3,265	-	-3,024	-58.6	30,191	-
ii) Other Banks' Credit to Government	8,84,920	34,680	4.5	73,967	9.8	74,014	9.1
b) Bank Credit to Commercial Sector	21,15,497	3,71,050	27.3	4,30,358	25.4	3,87,136	22.4
c) Net Foreign Exchange Assets	9,14,552	1,60,694	25.6	1,86,985	25.7	1,25,715	15.9
d) Government's Currency Liability to Public	8,457	2	0.0	-467	-5.3	624	8.0
e) Net Non-Monetary Liabilities of the Banking Sector	5,16,951	1,17,857	30.2	1,07,725	23.2	8,237	1.6
<b>Memo:</b>							
Aggregate Deposits of SCBs	27,13,843	3,77,392	20.9	4,99,260	23.7	5,31,881	24.4
Non-food Credit of SCBs	18,70,299	3,70,899	32.8	4,16,006	28.4	3,67,258	24.4
* : Data pertain to July 20, 2007.							
SCBs : Scheduled Commercial Banks. FIs : Financial Institutions. NBFCs : Non-Banking Financial Companies.							
NM <sub>3</sub> is the residency-based broad money aggregate and L <sub>1</sub> , L <sub>2</sub> and L <sub>3</sub> are liquidity aggregates compiled on the recommendations of the Working Group on Money Supply (Chairman: Dr. Y.V. Reddy, 1998).							
L <sub>1</sub> = NM <sub>3</sub> + Select deposits with the post office saving banks.							
L <sub>2</sub> = L <sub>1</sub> + Term deposits with term lending institutions and refinancing institutions (FIs) + Term borrowing by FIs + Certificates of deposits issued by FIs.							
L <sub>3</sub> = L <sub>2</sub> + Public deposits of non-banking financial companies.							
<b>Note :</b> 1. Data are provisional.							
2. Postal deposits data pertain to end-March 2007.							
3. Data reflect redemption of India Millennium Deposits (IMDs) on December 29, 2005.							

Consistent with the projections of money supply, the Annual Policy Statement for 2007-08 placed growth in aggregate deposits in 2007-08 at around Rs.4,90,000 crore. Based on an overall assessment of the sources of funding, the Statement noted that a graduated deceleration of non-food credit including investments in bonds/debentures/shares of public sector undertakings and private corporate sector and commercial paper (CP) to 24.0-25.0 per cent in 2007-08 from the average of 29.8 per cent over 2004-07 would be consistent with the monetary projections.



Growth of currency with the public on July 6, 2007 decelerated from end-March 2007 and also from the position a year ago. Growth in demand deposits, though higher than that at end-March 2007, was lower than a year ago. Consequently, growth in narrow money ( $M_1$ ), y-o-y, slowed down from 20.6 per cent on July 7, 2006 to 17.0 per cent on July 6, 2007, *albeit* marginally higher than 16.8 per cent at end-March 2007. On the other hand, growth in time deposits accelerated from 18.4 per cent on July 7, 2006 and 23.2 per cent at end-March 2007 to 23.4 per cent on July 6, 2007 (see Table 20). Concomitantly, the accretion to postal deposits decelerated to 10.9 per cent in March 2007 from 17.2 per cent a year ago. The higher order of increase in time deposits can be attributed, *inter alia*, to higher economic activity, increase in interest rates on bank deposits, unchanged interest rates on postal deposits and extension of tax benefits under Section 80C for bank deposits (Chart 9).

On a financial year basis, growth in  $M_3$  during 2007-08 (up to July 6, 2007) was 3.8 per cent as compared with 3.5 per cent during the comparable period of the previous year (Table 21).

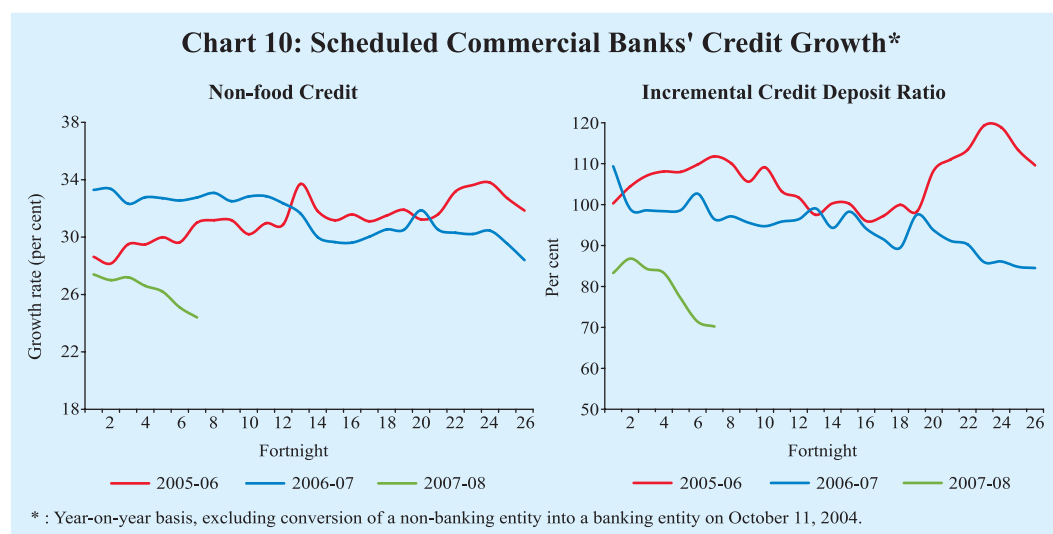
Bank credit to the commercial sector exhibited some moderation during the first quarter of 2007-08 from the strong pace of the previous three years. Scheduled commercial banks' (SCBs') non-food credit expanded by 24.4 per cent, y-o-y, on July 6, 2007 as compared with 28.4 per cent at end-March 2007 and 32.8 per cent a year ago. Non-food credit of SCBs including their non-SLR investments (shares, bonds/debentures and CPs) increased by 23.1 per cent (Rs.3,66,450 crore), y-o-y, on July 6, 2007 as compared with 29.5 per cent (Rs.3,60,938 crore) on July 7, 2006. Banks' investments in instruments issued by mutual funds increased by Rs.30,381 crore, y-o-y, on July 6, 2007 as compared with Rs. 15,331 crore on July 7, 2006. The deceleration in credit growth coupled with the acceleration in deposits

Monetary and Liquidity Conditions

**Table 21: Monetary Aggregates - Variations**

Item	(Rupees crore)						
	2006-07	2007-08	2006-07				2007-08
	(up to July 7)	(up to July 6)	Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6	7	8
<b>M<sub>3</sub> (1+2+3 = 4+5+6+7-8)</b>	<b>95,488</b>	<b>1,24,365</b>	<b>55,411</b>	<b>1,68,401</b>	<b>62,951</b>	<b>2,93,970</b>	<b>78,638</b>
	(3.5)	(3.8)					
<b>Components</b>							
1. Currency with the Public	23,738	14,346	23,797	-2,878	27,587	21,847	17,752
	(5.7)	(3.0)					
2. Aggregate Deposits with Banks	72,715	1,05,727	33,227	1,70,827	35,866	2,69,833	60,567
	(3.1)	(3.8)					
2.1 Demand Deposits with Banks	-32,289	-28,040	-42,399	43,794	-8,252	74,697	-42,300
	(-7.9)	(-5.9)					
2.2 Time Deposits with Banks	1,05,004	1,33,767	75,626	1,27,033	44,118	1,95,136	1,02,866
	(5.5)	(5.7)					
3. 'Other' Deposits with Banks	-964	4,292	-1,613	452	-502	2,291	319
<b>Sources</b>							
4. Net Bank Credit to Government	42,120	74,910	23,431	14,175	-13,204	47,180	18,976
	(5.5)	(8.9)					
4.1 RBI's Net Credit to Government	-10,328	22,415	53	2,826	-12,754	7,490	-25,483
4.1.1 RBI's Net credit to Centre	-7,504	25,711	3,071	2,584	-12,568	3,889	-21,825
4.2 Other Banks' Credit to Government	52,448	52,495	23,378	11,349	-451	39,690	44,459
5. Bank Credit to Commercial Sector	35,357	-7,865	14,930	1,44,204	78,099	1,93,125	-25,063
	(2.1)	(-0.4)					
6. NFEA of Banking Sector	62,643	1,373	58,087	20,197	43,160	65,542	-2,745
6.1 NFEA of RBI	76,402	1,373	71,845	11,392	27,250	82,682	-2,745
7. Government's Currency Liabilities to the Public	-920	171	-920	155	166	132	171
8. Net Non-Monetary liabilities of the Banking Sector	43,712	-55,776	40,117	10,330	45,269	12,009	-87,299
<b>Memo:</b>							
1. Non-resident Foreign Currency Deposits with SCBs	4,416	-4,602	3,917	1,671	1,233	1,011	-4,527
2. SCBs' Call-term Borrowing from Financial Institutions	1,236	-3,596	3,118	-1,576	-4,468	5,618	-2,916
3. Overseas Borrowing by SCBs	1,265	-6,850	3,301	-3,685	-2,774	5,229	-6,666
SCBs : Scheduled Commercial Banks. NFEA : Net Foreign Exchange Assets.							
<b>Note :</b> Figures in parentheses are percentage variations.							

growth led to a reduction in the incremental credit-deposit ratio (y-o-y) of SCBs to 70.2 per cent on July 6, 2007 from 96.4 per cent a year ago and 110.0 per cent at March 31, 2006 (Chart 10).



Disaggregated sectoral data available up to May 2007 show that about 39 per cent of incremental non-food credit (y-o-y) was absorbed by industry, led by infrastructure (power, port, telecommunication, etc.), textiles, iron and steel, engineering, petroleum, chemicals, construction and food processing industries. The infrastructure sector alone accounted for around 25 per cent of the incremental credit to the industry. The agricultural sector absorbed around 15 per cent of the incremental non-food credit expansion. Personal loans accounted for around 24 per cent of the incremental non-food credit; within personal loans, the share of incremental housing loans was around 11 per cent. Growth in loans to commercial real estate remained high (Table 22).

**Table 22: Deployment of Non-food Bank Credit**

(Amount in Rupees crore)					
Sector/Industry	Outstanding as on May 25, 2007	Year-on-Year Variation			
		May 26, 2006		May 25, 2007	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
<b>Non-food Gross Bank Credit (1 to 4)</b>	<b>17,52,349</b>	<b>3,10,316</b>	<b>32.2</b>	<b>3,65,814</b>	<b>26.4</b>
<b>1. Agriculture and Allied Activities</b>	<b>2,22,042</b>	<b>42,122</b>	<b>35.0</b>	<b>54,038</b>	<b>32.2</b>
<b>2. Industry (Small, Medium and Large)</b>	<b>6,76,440</b>	<b>98,947</b>	<b>26.4</b>	<b>1,41,280</b>	<b>26.4</b>
Small Scale Industries	1,15,884	14,863	20.3	26,387	29.5
<b>3. Personal Loans</b>	<b>4,55,439</b>	-	-	<b>87,944</b>	<b>23.9</b>
Housing	2,30,751	-	-	41,066	21.6
Advances against Fixed Deposits	39,092	6,076	22.9	6,237	19.0
Credit Cards	14,221	-	-	4,411	45.0
Education	15,438	-	-	4,903	46.5
Consumer Durables	8,831	-1,103	-13.3	1,661	23.2
<b>4. Services</b>	<b>3,98,428</b>	-	-	<b>82,551</b>	<b>26.1</b>
Transport Operators	25,321	-	-	7,922	45.5
Professional and other Services	24,834	-	-	8,999	56.8
Trade	1,05,536	-	-	23,319	28.4
Real Estate Loans	46,295	-	-	19,010	69.7
Non-Banking Financial Companies	44,425	11,564	64.0	12,401	38.7
<i>Memo:</i>					
<b>Priority Sector</b>	<b>6,25,298</b>	<b>1,22,394</b>	<b>33.7</b>	<b>1,20,463</b>	<b>23.9</b>
<b>Industry (Small, Medium and Large)</b>	<b>6,76,440</b>	<b>98,947</b>	<b>26.4</b>	<b>1,41,280</b>	<b>26.4</b>
Food Processing	37,367	4,545	19.9	6,758	22.1
Textiles	77,657	14,704	37.8	19,223	32.9
Paper & Paper Products	11,391	2,093	35.1	2,243	24.5
Petroleum, Coal Products & Nuclear Fuels	29,039	2,135	14.5	9,884	51.6
Chemical and Chemical Products	52,415	6,800	22.2	6,511	14.2
Rubber, Plastic and their Products	8,855	2,291	56.3	1,938	28.0
Iron and Steel	63,374	13,031	42.5	13,554	27.2
Other Metal & Metal Products	20,454	2,769	26.7	5,447	36.3
Engineering	42,592	5,683	22.3	8,553	25.1
Vehicles, Vehicle Parts and Transport Equipments	23,691	5,045	58.3	5,267	28.6
Gems and Jewellery	23,423	5,623	45.9	2,572	12.3
Construction	20,123	4,192	50.6	6,632	49.2
Infrastructure	1,43,520	25,557	35.0	35,292	32.6
- : Not available.					
<b>Note :</b> 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 onwards are not comparable with the earlier periods.					

Monetary and Liquidity Conditions

Apart from bank credit, the corporates continued to fund their requirements through non-bank sources of funds such as capital markets, external commercial borrowings (ECBs) and internal funds. Resources raised through domestic equity issuances remained strong at Rs.13,261 crore during 2007-08 (April-June) (Table 23). Resources raised from international markets through American depository receipts (ADRs) and global depository receipts (GDRs) were Rs.1,251 crore during 2007-08 (April-June) as compared with Rs.4,965 crore a year ago. Net mobilisation under ECBs almost doubled to Rs.88,472 crore during 2006-07 (April-March). Internal generation of funds continued to provide strong support to the funding requirements as profits after tax of sample non-financial non-government companies during 2006-07 were around 45 per cent higher than that in the previous year.

Investments by scheduled commercial banks in Government and other approved securities increased by 10.5 per cent, y-o-y, on July 6, 2007 as compared with 4.1 per cent a year ago (Table 24). Commercial banks' holdings of Government securities at 28.7 per cent of their net demand and time liabilities (NDTL) on

**Table 23: Select Sources of Funds to Industry**

Item	(Rupees crore)						
	2005-06	2006-07	2006-07			2007-08	
			Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6	7	8
<b>A. Bank Credit to Industry #</b>	<b>1,26,804</b>	<b>1,41,543</b>	<b>-2,336</b>	<b>49,290</b>	<b>28,415</b>	<b>66,174</b>	<b>-20,894 *</b>
<b>B. Flow from Non-banks to Corporates</b>							
1. Capital Issues (i+ii)	13,781	29,180	10,627	1,882	10,840	5,831	13,788
i) Non-Government Public Ltd. Companies (a+b)	13,408	29,180	10,627	1,882	10,840	5,831	13,261
a) Bonds/Debentures	245	585	0	0	491	94	0
b) Shares	13,163	28,595	10,627	1,882	10,349	5,737	13,261
ii) PSUs and Government Companies	373	0	0	0	0	0	527
2. ADR/GDR Issues	7,263	16,184	4,965	2,130	924	8,165	1,251
3. External Commercial Borrowings (ECBs)	45,078	88,472	20,498	14,232	16,077	37,665	N.A.
4. Issue of CPs	-1,517	4,970	6,931	4,795	-908	-5,848	7,661
<b>C. Depreciation Provision +</b>	<b>28,883</b>	<b>37,095</b>	<b>8,449</b>	<b>8,892</b>	<b>9,172</b>	<b>10,338</b>	<b>N.A.</b>
<b>D. Profit after Tax +</b>	<b>67,506</b>	<b>1,11,107</b>	<b>24,845</b>	<b>27,710</b>	<b>28,698</b>	<b>31,251</b>	<b>N.A.</b>

N.A. : Not available.

\* : April-May 2007.

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

+ : Data are based on audited/ unaudited abridged results of select non-financial non-Government companies. Data for the full year may not add to the quarterly totals due to difference in the number of companies covered in each period (see Chapter I).

**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.

3. Data on ADR/GDR issues exclude issuances by banks and financial institutions.

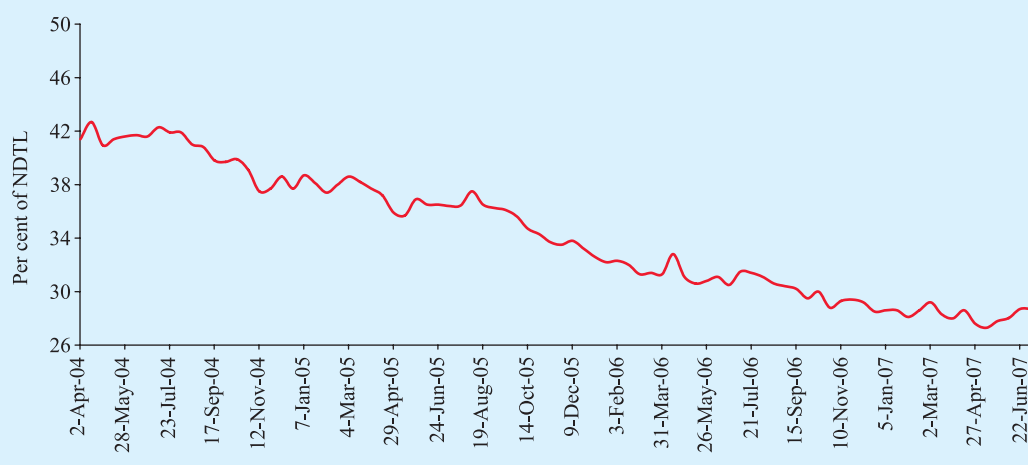
4. Data on external commercial borrowings include short-term credit. Data for 2005-06 are exclusive of the IMD redemption.

**Table 24: Scheduled Commercial Bank Survey**

Item	Outstanding as on July 6, 2007	Variation (year-on-year)			
		As on July 7, 2006		As on July 6, 2007	
		Amount	Per cent	Amount	Per cent
1	2	3	4	5	6
<b>Sources of Funds</b>					
1. Aggregate Deposits	27,13,843	377,392	20.9	5,31,881	24.4
2. Call/Term Funding from Financial Institutions	82,240	13,398	18.9	-2,140	-2.5
3. Overseas Foreign Currency Borrowings	25,055	3,190	11.4	-6,045	-19.4
4. Capital	36,748	987	3.5	7,792	26.9
5. Reserves	2,10,763	31,950	24.5	48,518	29.9
<b>Uses of Funds</b>					
1. Bank Credit	19,14,527	363,936	30.9	3,73,632	24.2
<i>of which: Non-food Credit</i>	18,70,299	3,70,899	32.8	3,67,258	24.4
2. Investments in Government and Other Approved Securities	8,49,946	30,101	4.1	80,715	10.5
a) Government Securities	8,29,251	33,351	4.6	76,409	10.1
b) Other Approved Securities	20,695	-3,250	-16.5	4,306	26.3
3. Investments in Non-SLR Securities	1,78,371	9,842	7.0	27,716	18.4
4. Foreign Currency Assets	62,065	4,202	14.8	29,420	90.1
5. Balances with the RBI	1,99,592	19,542	20.3	83,877	72.5

**Note :** Data are provisional.

July 6, 2007 were somewhat higher than 28.0 per cent at end-March 2007 but lower than that of 31.5 per cent a year ago (Chart 11). Excess SLR investments of SCBs increased to Rs.1,10,207 crore on July 6, 2007 from Rs.84,223 crore at end-March 2007 but were lower than Rs.1,59,029 crore a year ago. Banks' balances

**Chart 11: SLR Investments by Scheduled Commercial Banks**




## Monetary and Liquidity Conditions

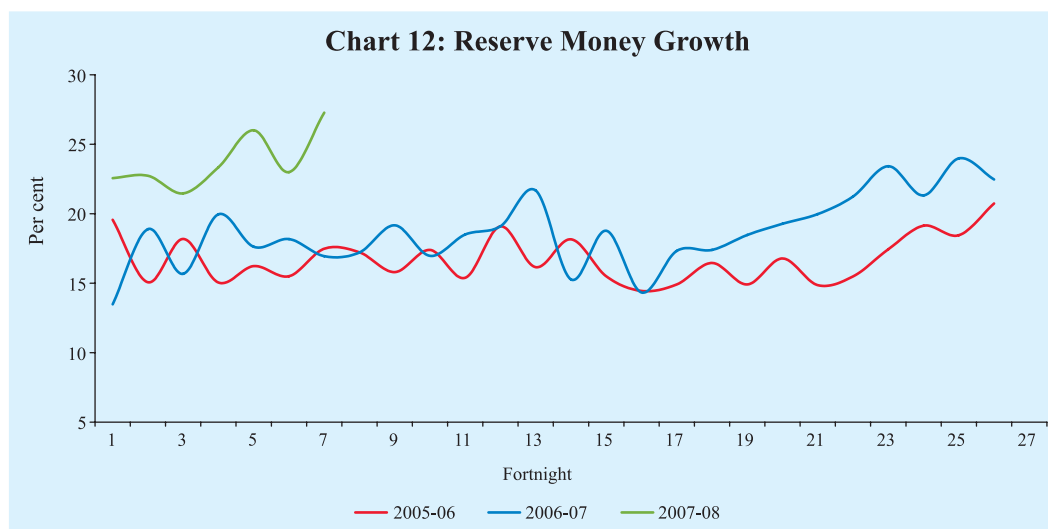
with the Reserve Bank expanded, reflecting the impact of the increase in their NDTL as well as the increase in the CRR. Investments by SCBs in non-SLR securities (such as shares/bonds/commercial papers) were also higher than a year ago. Banks' holdings of foreign currency assets abroad were higher than that in the previous year; their overseas borrowings contracted. Funds raised through capital issues as well as internal accruals were higher than in the previous year.

### Reserve Money Survey

Reserve money expanded by 29.1 per cent, y-o-y, as on July 20, 2007 (21.7 per cent adjusted for the first round effects of the hikes in the CRR<sup>1</sup>) as compared with 17.2 per cent a year ago (Chart 12).

During the financial year 2007-08 (up to July 20, 2007), reserve money expanded by 6.2 per cent (4.0 per cent adjusted for the first round effects of the hikes in the CRR) as compared with 1.8 per cent in the corresponding period of 2006-07. Growth in bankers' deposits with the Reserve Bank increased by 14.0 per cent during 2007-08 (up to July 20, 2007) as against a decline of 6.2 per cent during the corresponding period of 2006-07. Currency in circulation expanded by 2.1 per cent as compared with 4.6 per cent during the corresponding period of the previous year (Table 25).

On the sources side, reserve money continued to be driven by net foreign currency assets (adjusted for revaluation), which rose by Rs.72,947 crore in 2007-



<sup>1</sup> The cash reserve ratio was increased by 150 basis points in stages between December 2006 and May 2007 (see Table 33, Chapter 4) and this is estimated to have absorbed Rs.43,000 crore of banks' resources.



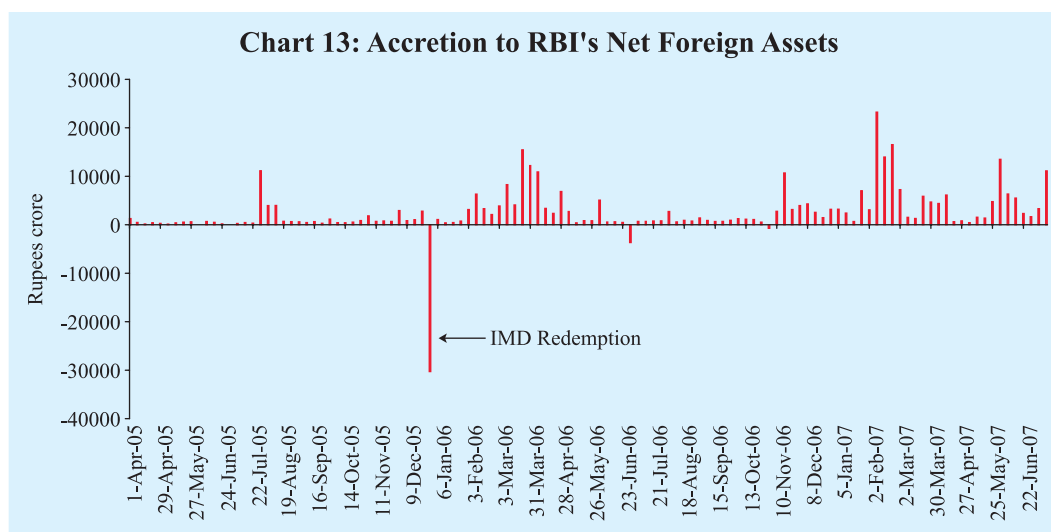
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<b>Table 25: Reserve Money</b>									
(Amount in Rupees crore)									
Item	Outstanding as on July 20, 2007	Variation							
		2006-07 (April March)	2006-07 (Up to July 21)	2007-08 (Up to July 20)	2006-07				2007-08
1	2	3	4	5	Q1	Q2	Q3	Q4	Q1
<b>Reserve Money</b>	<b>7,52,675</b>	<b>1,35,961</b>	<b>10,069</b>	<b>43,659</b>	<b>13,466</b>	<b>18,665</b>	<b>14,204</b>	<b>89,626</b>	<b>12,390</b>
<b>Components (1+2+3)</b>									
1. Currency in Circulation	5,14,605	73,549 (17.1)	19,630 (4.6)	10,380 (2.1)	22,283	-2,011	26,871	26,405	16,870
2. Bankers' Deposits with RBI	2,24,980	61,784 (45.6)	-8,453 (-6.2)	27,685 (14.0)	-7,204	20,224	-12,165	60,929	-4,800
3. 'Other' Deposits with the RBI	13,090	628 (9.1)	-1,108 (-16.1)	5,594 (74.6)	-1,613	452	-502	2,291	319
<b>Sources (1+2+3+4-5)</b>									
1. RBI's Net Credit to Government	21,884	-2,384	-9,374	16,132	53	2,826	-12,754	7,490	-25,483
<i>of which:</i> to Centre (i+ii+iii+iv-v)	21,011	-3,024	-6,356	18,875	3,071	2,584	-12,568	3,889	-21,825
i. Loans and Advances	30,058	0	0	30,058	0	0	0	0	0
ii. Treasury Bills held by the RBI	0	0	0	0	0	0	0	0	0
iii. RBI's Holdings of Dated Securities	75,990	26,763	-33,913	-21,182	-27,610	24,944	22,733	6,696	-34,284
iv. RBI's Holdings of Rupee coins	91	-143	-20	79	9	-107	97	-142	128
v. Central Government Deposits	85,127	29,644	-27,577	-9,921	-30,672	22,253	35,398	2,665	-12,330
2. RBI's Credit to Banks and Commercial Sector	1,394	1990	-3,094	-7,778	-3,135	3,107	2,065	-47	-6,450
3. NFEA of RBI	8,93,888	1,93,170 (28.7)	87,888 (13.1)	27,735 (3.2)	71,845	11,392	27,250	82,682	-2,745
<i>of which</i> :FCA, adjusted for revaluation		1,64,601	30,663	72,947	28,107	10,948	31,634	93,913	47,728
4. Government's Currency Liabilities to the Public	8,457	-467	-868	171	-920	155	166	132	171
5. Net Non-Monetary liabilities of RBI	1,72,948	56,347	64,483	-7,400	54,376	-1,184	2,524	632	-46,897
<i>Memo:</i>									
LAF Repos (+) / Reverse Repos (-)	-3,000	36,435	-38,820	-32,185	-23,060	28,395	22,195	8,905	-32,182
Net Open Market Sales # *		5,125	2,503	1,910	1,536	1,176	389	2,024	1,246
Centre's Surplus **	0	1,164	-42,699	-49,992	-27,321	13,313	38,713	-23,542	-34,597
Mobilisation under MSS *	85,027	33,912	8,664	22,053	4,062	8,940	-3,315	24,225	19,643
Net Purchases(+)/Sales(-) from Authorised Dealers		1,18,994	21,545	14,614 +	21,545	0	19,776	77,673	14,614 +
NFEA/Reserve Money @	118.8	122.2	130.5	118.8	127.0	125.0	126.5	122.2	119.7
NFEA/Currency @	173.7	171.8	169.0	173.7	164.4	167.7	164.0	171.8	165.7
NFEA : Net Foreign Exchange Assets. FCA : Foreign Currency Assets. LAF : Liquidity Adjustment Facility.									
* : At face value. + : Up to May 25, 2007. # : Excludes Treasury Bills. @ : per cent, end of period.									
** : Excludes minimum cash balances with the Reserve Bank in case of surplus.									
<b>Note</b> : 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.									

08 (up to July 20, 2007) as compared with Rs.30,663 crore during the corresponding period of the previous year (Chart 13). Movements in the Reserve Bank's net credit to the Centre largely reflected liquidity management operations by the Reserve Bank and trends in Government deposits. During 2007-08 (up to July 20, 2007), the Reserve Bank's holdings of Central Government's dated securities declined by Rs.21,182 crore, partly on account of absorption of liquidity



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under the liquidity adjustment facility (LAF). On the other hand, there was an increase of Rs.30,058 crore in ways and means advances/overdraft from the Reserve Bank. Central Government deposits declined reflecting a reduction in the Government's cash surplus (Rs.49,992 crore), partly offset by an increase in balances under the MSS (Rs.22,053 crore). Reflecting these developments, net Reserve Bank credit to the Centre increased by Rs.18,875 crore during 2007-08 (up to July 20, 2007) as against a decline of Rs.6,356 crore during the corresponding period of the previous year.

### Liquidity Management

During 2007-08, the Reserve Bank continued with its policy of active management of liquidity, using all the policy instruments at its disposal flexibly. Variations in cash balances of the Government and capital flows remained the key drivers of liquidity conditions.

Liquidity pressures eased gradually from April 4, 2007 onwards, partly on account of reduction in the Centre's cash balance from Rs.50,092 crore at end-March 2007 to Rs.32,023 crore by mid-April 2007. Consequently, the amount injected through LAF repos fell from Rs.29,185 crore at end-March 2007 to Rs.1,455 crore by April 5, 2007 and subsequently, liquidity was absorbed under the LAF reverse repos during April 9-15, 2007. The amount absorbed was capped at Rs.3,000 crore as per the modified arrangements effective March 5, 2007. Accordingly, amounts absorbed under LAF reverse repos since March 5, 2007 onwards are not comparable with previous data (Table 26 and Chart 14).

Although the Centre's cash balance declined further from mid-April 2007 onwards, liquidity conditions tightened; this could be partly attributed to the

**Table 26: Reserve Bank's Liquidity Management Operations**

Item	(Rupees crore)							
	2006-07	2006-07				2007-08		
	(April-March)	Q1	Q2	Q3	Q4	April	May	June
1	2	3	4	5	6	7	8	9
<b>A. Drivers of Liquidity (1 to 5)</b>	61,739	36,247	-16,896	-25,641	68,028	34,179	12,797	N.A.
1. RBI's net Purchases from Authorised Dealers	1,18,994	21,545	0	22,461	74,988	8,835	5,779	N.A.
2. Currency with the Public	-70,352	-19,648	-1,270	-27,033	-22,400	-19,953	-1,007	8,498
3. Surplus Cash Balances of the Centre with the Reserve Bank*	-1,164	40,207	-26,199	-30,761	15,590	49,992	0	0
4. WMA/Overdraft to the Centre	0	0	0	0	0	980	6,773	7,406
5. Others (residual)	14,260	-5,856	10,574	9,693	-150	-5,676	1,252	N.A.
<b>B. Management of Liquidity (6 to 9)</b>	-24,257	-39,003	32,026	31,625	-48,905	-39,879	-24,451	10,387
6. Liquidity Impact of LAF Repos	36,435	-35,315	40,650	33,600	-2,500	-19,189	-5,306	4,205
7. Liquidity Impact of OMO (Net)@	720	545	145	25	5	10	0	0
8. Liquidity Impact of MSS	-33,912	-4,233	-8,769	4,750	-25,660	-12,950	-11,395	6,182
9. First Round Liquidity Impact due to CRR change	-27,500	0	0	-6,750	-20,750	-7,750	-7,750	0
<b>C. Bank Reserves (A+B) #</b>	37,482	-2,756	15,130	5,984	19,123	-5,700	-11,654	15,047

N.A. : Not available.

(+) : Indicates injection of liquidity into the banking system.

(-) : Indicates absorption of liquidity from the banking system.

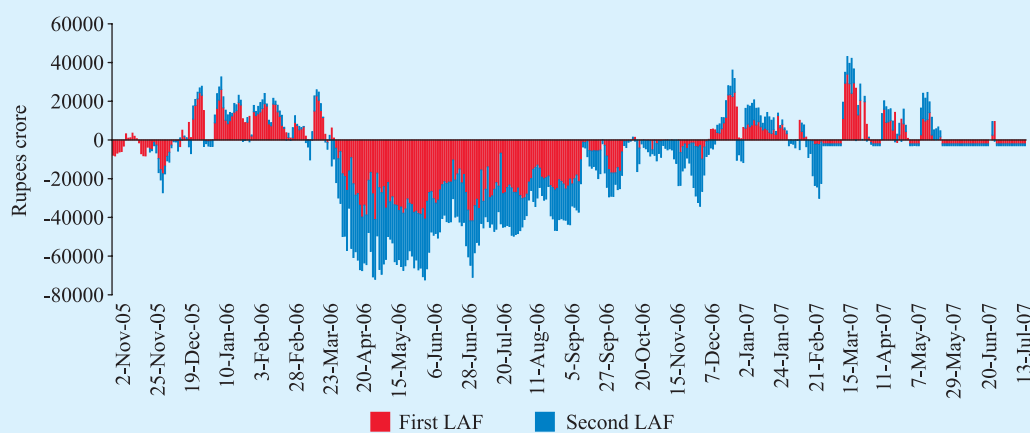
\* : Excludes minimum cash balances with the Reserve Bank in case of surplus.

# : Includes vault cash with banks and adjusted for first round liquidity impact due to CRR change.

@ : Adjusted for Consolidated Sinking Funds (CSF) and including private placement.

**Note :** For end-March, data pertain to March 31; for all other months data pertain to last Friday.

hikes of 25 basis points each in the CRR coming into effect from the fortnights beginning April 14, 2007 and April 28, 2007. The LAF window witnessed injection of liquidity during most part of April 16-May 27, 2007 with the daily net injection of liquidity averaging Rs.9,629 crore. Liquidity pressures eased from May 28,

**Chart 14: Repo (+)/Reverse Repo (-) under LAF**


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

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2007 onwards, reflecting increase in Government expenditure and net purchase of foreign exchange from authorised dealers by the Reserve Bank. The Centre's WMA/overdraft rose from Rs.7,753 crore on May 25, 2007 to Rs.26,707 crore by June 1, 2007 before falling to Rs.8,248 crore by June 15, 2007. The cash balance of the Government again turned into deficit on June 29, 2007 reflecting the transfer of the Reserve Bank's stake in the State Bank of India (SBI) to the Government. The LAF window turned into an absorption mode on May 28, 2007 and remained so up to July 24, 2007 (except during June 28-July 2, 2007 when liquidity was injected through repo operations to the tune of Rs.9,009 crore daily on an average). The amount of liquidity absorbed through the reverse repo operations remained limited to a maximum of Rs.3,000 crore in terms of the modified arrangements. Outstanding balances under the MSS rose from Rs.62,974 crore at end-March 2007 to Rs.85,027 crore by July 20, 2007 reflecting the enhanced MSS programme that was put in place in March/April 2007 to restore LAF as a facility for equilibrating very short-term mismatches (Table 27). Towards this objective, a mix of Treasury Bills and dated securities for MSS issuances is used in a more

**Table 27: 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
<b>2006</b>				
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	-1,203	83,859
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
<b>2007</b>				
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
April	-9,996	75,924	-980	64,948
May	-4,690	87,319	-7,753	74,876
June	-8,895	81,137	-15,159	57,083
July (as on 20 July)	3,000	85,027	-30,058	57,969

@ : Excludes minimum cash balances with the Reserve Bank in case of surplus.  
 \* : Data pertain to March 31.

**Note :** 1. Negative sign in column 2 indicates injection of liquidity through LAF repo.  
 2. Negative sign in column 4 indicates WMA/overdraft.  
 3. Beginning March 5, 2007, daily reverse repo absorptions under LAF have been 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.

flexible manner keeping in view the capital flows, the assessment of volatility and durability of capital flows.

In the recent period, there have been sharp variations in domestic liquidity conditions and overnight interest rates on the back of large movements in Government cash balances and capital flows. Reduction in Government cash balances and increase in capital inflows lead to an increase in market liquidity and downward pressures on overnight interest rates and *vice versa*. As noted earlier, modified liquidity management arrangements were put in place effective March 5, 2007. An enhanced MSS programme along with a cap of Rs.3,000 crore on absorption of liquidity under LAF reverse repos was put in place to restore LAF as a facility for equilibrating very short-term mismatches. However, in view of relatively large build-up of Government cash balances, the call rate reached a high of 54 per cent by end-March 2007. More recently, reduction in Government cash balances and large capital inflows have led to a sharp reduction in the call rate to below one per cent.