Macroeconomic and Monetary Developments

Mid-Term Review 2007-08

Reserve Bank of India

Mumbai

Contents

I. THE REAL ECONOMY

The Indian economy continued to maintain strong growth momentum during the first quarter of 2007-08, underpinned by sustained performances of the manufacturing and services sectors which continued to register double-digit growth. According to the estimates released by the Central Statistical Organisation (CSO) in August 2007, real GDP growth remained high at 9.3 per cent during the first quarter of 2007-08 on top of 9.6 per cent during the same period in 2006-07 (Table 1 and Chart 1). A positive feature was a recovery in the agricultural sector which recorded an increase of one percentage point over the corresponding quarter of the previous year.

Table 1: Growth Rates of Real GDP

(Per cent)

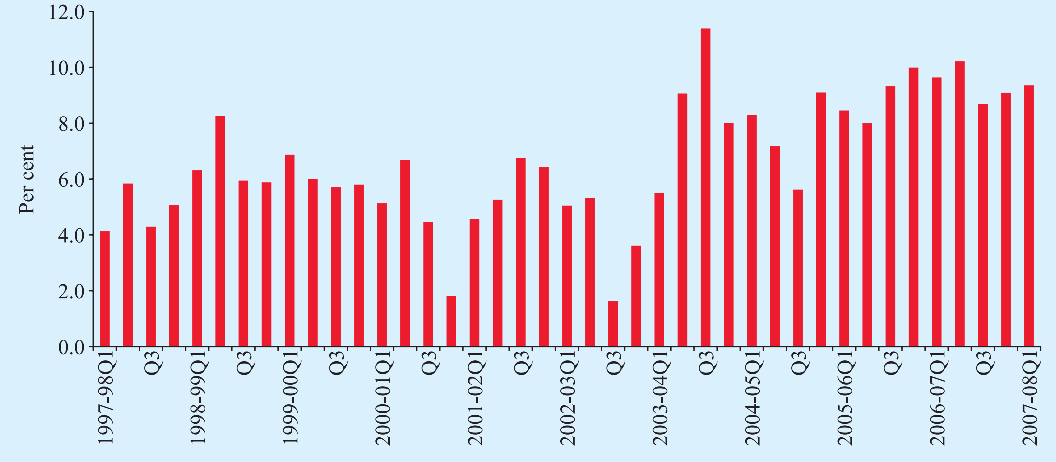
Sector	2000-01 to 2006-07 (Average)	2004-05	2005-06*	2006-07#	2006-07				2007-08
					Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6	7	8	9	10
1. Agriculture and Allied Activities	**2.5** **(21.4)**	**0.0** **(20.2)**	**6.0** **(19.7)**	**2.7** **(18.5)**	**2.8**	**2.9**	**1.6**	**3.8**	**3.8**
2. Industry	**7.0** **(19.6)**	**8.4** **(19.6)**	**8.0** **(19.4)**	**11.0** **(19.7)**	**10.6**	**11.3**	**10.8**	**11.2**	**10.6**
2.1 Mining and Quarrying	4.6	7.5	3.6	5.1	3.7	3.9	5.5	7.1	3.2
2.2 Manufacturing	7.7	8.7	9.1	12.3	12.3	12.7	11.8	12.4	11.9
2.3 Electricity, Gas and Water Supply	4.8	7.5	5.3	7.4	5.8	8.1	9.1	6.9	8.3
3. Services	**8.6** **(59.0)**	**10.0** **(60.2)**	**10.3** **(60.9)**	**11.0** **(61.8)**	**11.6**	**11.7**	**10.9**	**10.0**	**10.6**
3.1 Trade, Hotels, Restaurants, Transport, Storage and Communication	10.3	10.9	10.4	13.0	12.4	14.2	13.1	12.4	12.0
3.2 Financing, Insurance, Real Estate and Business Services	7.9	8.7	10.9	10.6	10.8	11.1	11.2	9.3	11.0
3.3 Community, Social and Personal services	6.0	7.9	7.7	7.8	11.3	8.3	6.7	5.7	7.6
3.4 Construction	9.9	14.1	14.2	10.7	10.5	11.1	10	11.2	10.7
4. Real GDP at Factor Cost	**6.9** **(100)**	**7.5** **(100)**	**9.0** **(100)**	**9.4** **(100)**	**9.6**	**10.2**	**8.7**	**9.1**	**9.3**
Memo:									(Amount in Rupees crore)
a) Real GDP at factor cost (1999-2000)		23,89,660	26,04,532	28,48,157					
b) GDP at current market prices		31,26,596	35,67,177	41,25,725					

* : Quick Estimates. # : Revised Estimates.

Note : Figures in parentheses denote shares in real GDP.

Source : Central Statistical Organisation.

Chart 1: Real GDP - Growth Rate



Agricultural Situation

The cumulative rainfall during the South-West monsoon season 2007 (June to September) was 5 per cent above normal as compared to one per cent below normal during the corresponding period of the previous year. The South-West monsoon set in over Kerala on May 28, 2007, four days in advance of the normal date of onset over the State. After a brief spell of hiatus during early June due to the formation of a super cyclone “Gonu” over the East-Central Arabian Sea, the South-West monsoon covered the North-Eastern States by June 10, 2007, peninsular and central India by June 25, 2007 and subsequently the entire country by July 4, 2007, nearly 11 days ahead of the normal schedule. Of the 36 meteorological sub-divisions, cumulative rainfall was deficient in 6 sub-divisions (10 sub-divisions during last year) (Table 2). As on October 18, 2007, the total live water storage of 81 important reservoirs[1] was 81 per cent of the Full Reservoir Level (FRL), lower than that of 83 per cent last year but higher than the average of 68 per cent for the past 10 years.

The area coverage of *kharif* crops has increased during 2007-08 (as on October 12, 2007) with reported sown area of 103.8 per cent of the normal, which was about 3.1 per cent higher than the previous year. While foodgrain crops such as pulses and rice have shown improvement in area sown, coarse grains witnessed a decline (Table 3). Among non-foodgrains, while area covered under oilseeds, sugarcane, cotton and jute increased, that under mesta declined.

The Ministry of Agriculture has set targets for foodgrains, pulses and oilseeds production for 2007-08 at 221.5 million tonnes, 15.5 million tonnes

[1] These 81 important reservoirs have FRL of 151.77 billion cubic metres and account for around 72 per cent of the total reservoir capacity of the country.

Table 2: Rainfall – South-West Monsoon (June-September)

Year	Cumulative Rainfall: Above(+)/Below (-) Normal (per cent)	Spatial Distribution (Number of Sub-Divisions)			
		Excess Rainfall	Normal Rainfall	Deficient Rainfall	Scanty/ No Rain
1	2	3	4	5	6
2000	-8	5	23	8	0
2001	-8	1	30	5	0
2002	-19	1	14	19	2
2003	2	7	26	3	0
2004	-13	0	23	13	0
2005	-1	9	23	4	0
2006	-1	6	20	10	0
2007	5	13	17	6	0

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 to -99 per cent. No Rain : -100 per cent.
Source : India Meteorological Department.

and 30 million tonnes, respectively. Reflecting the good rainfall and increase in area sown, total *kharif* foodgrains production during 2007-08, at 112.2 million tonnes (according to the First Advance Estimates), is likely to be 1.6 per cent higher than the previous year. Production of oilseeds, pulses, cotton and sugarcane is also expected to show improvement over the previous year. *Kharif* foodgrains production is, however, expected to fall short of the target of 114.2 million tonnes on account of coarse cereals. While *kharif* production of oilseeds is expected to

Table 3: Progress of Area under *Kharif* Crops - 2007-08

(Million hectares)

Crop	Normal Area	Area Coverage (as on October 12, 2007)		
		2006	2007	Variation
1	2	3	4	5
Rice	38.2	36.9	37.2	0.3
Coarse Cereals	22.9	22.1	22.0	-0.1
of which:				
Bajra	9.4	9.3	8.7	-0.6
Jowar	4.4	3.8	3.6	-0.2
Maize	6.2	6.8	7.5	0.6
Total Pulses	10.9	11.4	12.5	1.2
Total Oilseeds	15.4	16.5	17.6	1.1
of which:				
Groundnut	5.5	4.8	5.4	0.7
Soyabean	6.6	8.1	8.8	0.6
Sugarcane	4.2	4.8	5.1	0.3
Cotton	8.3	8.9	9.3	0.4
All Crops	**100.8**	**101.5**	**104.7**	**3.2**

Source : Ministry of Agriculture, Government of India.

Table 4: Agricultural Production

(Million tonnes)

Crop	2003-04	2004-05	2005-06	2006-07*	2007-08	
					T	A @
1	2	3	4	5	6	7
Rice	88.5	83.1	91.8	92.8	93.0	
Kharif	78.6	72.2	78.3	80.1	80.0	80.2
Rabi	9.9	10.9	13.5	12.7	13.0	
Wheat	72.2	68.6	69.4	74.9	75.5	
Coarse Cereals	37.6	33.5	34.1	34.3	37.5	
Kharif	32.2	26.4	26.7	25.7	28.7	26.6
Rabi	5.4	7.1	7.3	8.6	8.8	
Pulses	14.9	13.1	13.4	14.2	15.5	
Kharif	6.2	4.7	4.9	4.7	5.5	5.5
Rabi	8.7	8.4	8.5	9.5	10.0	
Total Foodgrains	213.2	198.4	208.6	216.1	221.5	
Kharif	117.0	103.3	109.9	110.5	114.2	112.2
Rabi	96.2	95.1	98.7	105.6	107.3	
Total Oilseeds	25.2	24.4	28.0	23.9	30.0	
Kharif	16.7	14.1	16.8	13.9	18.5	16.1
Rabi	8.5	10.2	11.2	9.9	11.5	
Sugarcane	233.9	237.1	281.2	345.3	310.0	345.6
Cotton #	13.7	16.4	18.5	22.7	22.0	22.9
Jute and Mesta ##	11.2	10.3	10.8	11.3	11.0	11.3

T : Target.
A : Achievement.
* : Fourth Advance Estimates as on July 19, 2007.
@ : First Advance Estimate as on September 19, 2007.
# : Million bales of 170 kgs each.
: Million bales of 180 kgs each.
Source : Ministry of Agriculture, Government of India.

be lower than the target for 2007-08, output of cotton and sugarcane is expected to exceed the targets (Table 4).

Food Management

Total procurement of rice and wheat during 2007-08 (up to October 16, 2007) aggregated 19.5 million tonnes, which was lower by 1.9 per cent than the corresponding period of 2006-07. While rice procurement declined by 21.4 per cent, wheat procurement increased by 20.6 per cent over the previous year. Total off-take of rice and wheat during 2007-08 (up to June 30, 2007) at 8.9 million tonnes was lower by 4.1 per cent than that of the corresponding period of the previous year. As on July 1, 2007, total stocks of foodgrains with the Food Corporation of India (FCI) and other Government agencies were at 23.9 million tonnes, which were higher by 16.6 per cent than those in the previous year (20.5 million tonnes) (Table 5). While the stocks of rice at 11.0 million tonnes were higher than the buffer stock norm of 9.8 million tonnes, those of wheat at 12.9 million tonnes were lower than the buffer stock norm of 17.1 million tonnes.

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	24.0	16.8	40.8	29.7	10.6	0.2	1.0	41.5	18.0	
2005-06	13.3	4.1	18.0	26.9	14.8	41.7	31.4	9.8	1.1	0.0	42.2	16.6	
2006-07	13.7	2.0	16.6	26.7	9.2	35.9	31.6	5.1	0.0	0.0	36.8	17.8	
2006-07@	13.7	2.0	16.6	10.7	9.2	19.9	7.9	1.4	0.0	0.0	9.3		
2007-08@	13.2	4.6	17.8	8.4	11.1	19.5	8.1	0.8	0.0	0.0	8.9		
2006													
April	13.7	2.0	16.6	1.7	8.7	10.3	2.5	0.3	0.0	0.0	2.8	22.8	16.2
May	12.8	9.0	22.8	1.6	0.6	2.2	2.5	0.4	0.0	0.0	3.0	22.3	
June	12.0	9.3	22.3	1.5	0.0	1.5	2.5	0.6	0.0	0.0	3.1	20.5	
July	11.1	8.2	20.5	0.8	0.0	0.8	2.7	0.4	0.0	0.0	3.1	17.1	26.9
August	9.5	7.3	17.1	0.5	0.0	0.5	2.7	0.4	0.0	0.0	3.1	15.5	
September	7.8	6.7	15.5	0.2	0.0	0.2	2.3	0.5	0.0	0.0	2.8	12.6	
October	6.0	6.4	12.6	8.0	0.0	8.0	2.4	0.3	0.0	0.0	2.7	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	2.7	0.5	0.0	0.0	3.1	19.1	
March	14.0	5.1	19.1	1.2	0.0	1.2	2.7	0.5	0.0	0.0	3.2	17.8	
April	13.2	4.6	17.8	0.9	7.9	8.7	2.5	0.2	0.0	0.0	2.8	25.1	16.2
May	13.5	11.6	25.1	1.5	2.6	4.0	2.8	0.2	0.0	0.0	3.0	25.9	
June	12.6	13.3	25.9	1.3	0.7	2.0	3.7	0.4	0.0	0.0	3.1	23.9	
July	11.0	12.9	23.9	0.8	0.0	0.8	–	–	–	–	–	–	26.9
August	–	–	–	0.1	0.0	0.1	–	–	–	–	–	–	
September	–	–	–	0.1	0.0	0.1	–	–	–	–	–	–	
October*	–	–	–	3.8	0.0	3.8	–	–	–	–	–	–	16.2

PDS : Public Distribution System. OWS : Other Welfare Schemes. OMS : Open Market Sales. – : Not Available.
@ : Procurement up to October 16 and offtake up to June 30. * : Procurement up to October 16, 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.

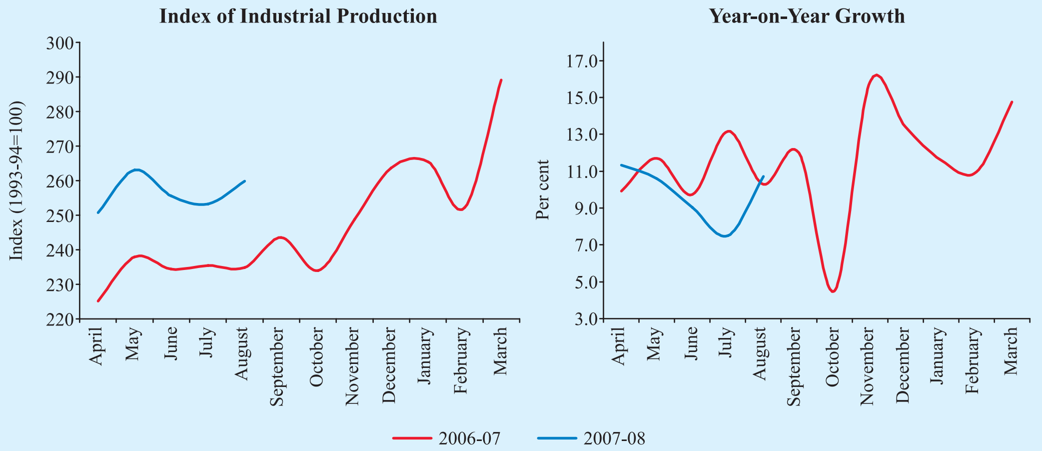
Source : Ministry of Consumer Affairs, Food and Public Distribution, Government of India.

Industrial Performance

During April-August 2007, the index of industrial production rose by 9.8 per cent as compared with a growth of 11.0 per cent recorded during the corresponding period of the previous year (Chart 2). The manufacturing sector registered a growth of 10.3 per cent during April-August 2007 on top of 12.2 per cent during April-August 2006. Growth rates in the mining and electricity sectors were higher at 5.4 per cent and 8.3 per cent, respectively, than a year ago (Table 6). Electricity sector registered the highest growth since 1998-99.

The moderation in the growth of manufacturing sector during April-August 2007 was on account of deceleration/negative growth in 12 out of 17 manufacturing industry groups, which account for 60.1 per cent weight in the manufacturing

Chart 2: Industrial Production



index (Table 7). 'Chemicals and chemical products except products of petroleum and coal', 'machinery and equipment', 'basic metal and alloy industries', 'non-metallic mineral products', 'cotton textiles' and 'transport equipment and parts' are among the major groups which registered a deceleration in growth, largely due to base effect. 'Metal products and parts' recorded a decline due to slowdown in the production of tin metal containers, welded link chains and razor blades.

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

(Per cent)

Industry Group	Weight in the IIP	Growth Rate			Weighted Contribution #		
		April-March	April-August		April-March	April-August	
		2006-07	2006-07	2007-08 P	2006-07	2006-07	2007-08 P
1	2	3	4	5	6	7	8
Sectoral							
Mining	10.5	5.3	3.0	5.4	3.4	2.0	3.8
Manufacturing	79.4	12.5	12.2	10.3	91.1	93.3	88.8
Electricity	10.2	7.3	5.7	8.3	5.5	4.8	7.4
Use-Based							
Basic Goods	35.6	10.3	8.3	10.0	27.2	23.4	30.7
Capital Goods	9.3	18.2	19.5	21.3	17.6	18.1	23.8
Intermediate Goods	26.5	12.0	10.4	9.3	27.0	25.7	25.7
Consumer Goods (a+b)	28.7	10.1	11.4	6.2	28.5	33.0	20.2
a) Consumer Durables	5.4	9.2	16.1	-2.3	6.7	11.9	-2.0
b) Consumer Non-durables	23.3	10.4	9.8	9.3	21.8	21.1	22.2
General	**100.0**	**11.5**	**11.0**	**9.8**	**100.0**	**100.0**	**100.0**

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

Table 7: Growth of Manufacturing Groups

(Per cent)

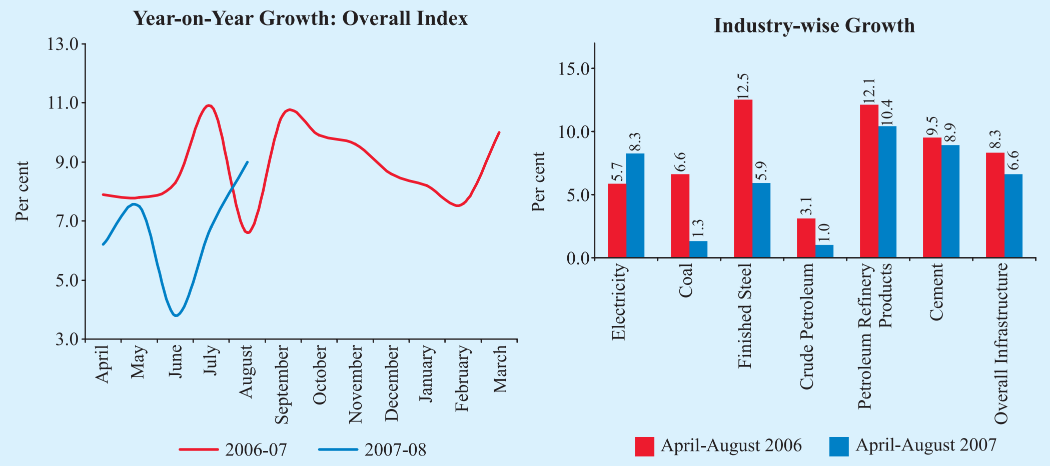
Industry Group	Weight in the IIP	Growth Rate April-March 2006-07	Growth Rate April-August 2006-07	Growth Rate April-August 2007-08 P	Weighted Contribution # April-March 2006-07	Weighted Contribution # April-August 2006-07	Weighted Contribution # April-August 2007-08 P
1	2	3	4	5	6	7	8
1. Machinery and equipment other than transport equipment	9.6	14.2	16.7	13.4	18.3	20.2	20.7
2. Basic metal and alloy Industries	7.5	22.9	21.5	19.4	16.6	14.9	17.8
3. Chemicals and chemical products except products of petroleum and coal	14.0	9.4	10.8	7.9	14.6	17.8	15.6
4. Non-metallic mineral products	4.4	12.9	13.0	8.3	6.6	6.7	5.2
5. Beverages, tobacco and related products	2.4	11.3	12.6	8.3	4.7	5.3	4.3
6. Other manufacturing industries	2.6	7.7	24.7	9.3	2.4	6.5	3.3
7. Cotton textiles	5.5	14.8	13.1	6.4	4.8	4.4	2.6
8. Transport equipment and parts	4.0	15.0	20.4	2.3	8.2	10.5	1.5
9. Textile products (including wearing apparel)	2.5	11.5	19.4	3.8	3.2	5.3	1.4
10. Wool, silk and man-made fibre textiles	2.3	8.1	7.3	4.0	2.0	1.8	1.2
11. Paper and paper products and printing, publishing and allied activities	2.7	8.4	10.7	0.8	2.2	2.9	0.2
12. Metal products and parts (except machinery and equipment)	2.8	11.4	5.5	-1.7	2.3	1.1	-0.4
13. Food products	9.1	8.7	-1.9	16.4	5.8	-1.1	9.7
14. Rubber, plastic, petroleum and coal products	5.7	12.7	8.8	12.6	6.3	4.5	7.8
15. Wood and wood products, furniture and fixtures	2.7	29.1	-2.1	80.1	2.4	-0.2	7.6
16. Leather and leather and fur products	1.1	0.4	-7.9	7.8	0.0	-0.7	0.7
17. Jute and other vegetable fibre textiles (except cotton)	0.6	-15.8	2.5	22.3	-0.4	0.1	0.6
Manufacturing – Total	**79.4**	**12.5**	**12.2**	**10.3**	**100.0**	**100.0**	**100.0**

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

'Food products', 'wood and wood products' and 'leather and leather and fur products', however, made a turnaround to register positive growth rates.

In terms of use-based classification, the basic and capital goods sectors witnessed strong growth during April-August 2007 (see Table 6). The basic goods sector benefited from the accelerated growth of the electricity sector and increased production of high speed diesel, caustic soda and some steel products. The growth in the capital goods sector was supported by strong investment demand. The growth in intermediate goods sector, however, moderated due to decline in the production of certain industries such as chemicals, metal and petroleum products. Consumer goods sector slowed down significantly due to the decline in the consumer durables segment, particularly in production of telephone instruments, television receivers, motor cycles and wrist watches.

Chart 3: Growth in Infrastructure Industries



Infrastructure

During April-August 2007, the infrastructure sector recorded a growth of 6.6 per cent as compared with 8.3 per cent a year ago, with five of the six core infrastructure industries registering a deceleration (Chart 3). The electricity sector was the only sector which recorded a higher growth than a year ago on account of increased plant load factor (PLF) in thermal power plants at 77.1 per cent during April-August 2007 (74.5 per cent during April-August 2006) and double-digit growth in power generation of hydropower plants. Moderation of growth in petroleum refinery products, cement and steel sectors could be attributed to base effect and capacity constraints. Decline in crude oil production reflected the decline in production in some of the ONGC oilfields such as Bassein, Neelam and Gujarat fields.

Services Sector

The services sector continued to record double-digit growth (10.6 per cent in April-June 2007 on top of 11.6 per cent in April-June 2006), driving the growth momentum of the economy. Services sector activity continued to be led by the sub-sector 'trade, hotel, transport and communication' (Table 8). This sub-sector recorded a growth of 12.0 per cent in the first quarter of 2007-08, contributing nearly 33.6 per cent to the overall real GDP growth of 9.3 per cent during the quarter. 'Financing, insurance, real estate and business services' recorded a growth of 11.0 per cent during April-June 2007 (10.8 per cent a year ago). The construction sector also recorded a higher growth at 10.7 per cent during the first quarter of 2007-08 than a year ago.

Table 8: Growth in Services Sectors

(Contribution to real GDP growth; percentage points)

Year/Quarter	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	0.7	3.4	1.5	1.1	6.7
2006-07: Q1	0.7	3.2	1.5	1.6	7.0
2006-07: Q2	0.8	3.7	1.6	1.3	7.4
2006-07: Q3	0.7	3.3	1.4	0.9	6.3
2006-07: Q4	0.8	3.4	1.3	0.8	6.2
2007-08: Q1	0.7	3.1	1.6	1.1	6.5

Leading indicators of services sector activity for April-August 2007 show that cargo handled at major ports and import cargo handled by civil aviation witnessed strong growth. Growth rates in commercial vehicles production, new cell phone connections, passengers handled by civil aviation and steel have moderated during 2007-08 (April-August), *albeit* over a high base (Table 9).

Table 9: Indicators of Services Sector Activity

(Growth rates in per cent)

Item	2005-06	2006-07	April-August	
			2006	2007
1	2	3	4	5
Tourist arrivals	13.8	13.0	14.3 @	10.8 @
Commercial vehicles production*	10.6	33.0	33.5	3.1
Railway revenue earning freight traffic	10.7	9.2	9.9	7.0
New cell phone connections	89.4	85.4	120.9	52.9
Cargo handled at major ports	10.4	9.5	6.0	14.2
Civil aviation				
a) Export cargo handled	7.3	3.6	5.9	5.4
b) Import cargo handled	15.8	19.4	21.2	23.5
c) Passengers handled at international terminals	12.8	12.1	12.9	12.4
d) Passengers handled at domestic terminals	27.1	34.0	40.1	27.8
Cement**	12.4	9.1	9.5	8.9
Steel**	10.8	11.7	12.5	5.9
Aggregate deposits	18.1	23.7	8.5 #	9.6 #
Non-food credit	31.8	28.4	9.4 #	5.3 #

@ : April-September   # : Up to October 12.
* : Leading indicator for transportation.   ** : Leading indicators for construction.
Sources : Ministry of Tourism, Ministry of Commerce and Industry, Ministry of Statistics and Programme Implementation, Reserve Bank of India and Centre for Monitoring Indian Economy.

Aggregate Demand

Estimates of expenditure of GDP for the first quarter of 2007-08 *vis-a-vis* the corresponding quarter of the previous year indicate that the growth remained domestic demand driven. The share of real private final consumption expenditure in total output declined from 60.8 per cent in 2006-07 to 58.8 per cent in the first quarter of 2007-08, while that of real gross fixed capital formation (GFCF) rose from 27.9 per cent to 29.6 per cent during the same period. Real GFCF rose by 15.9 per cent during the first quarter of 2007-08 as compared with 15.8 per cent during the corresponding quarter of the previous year. Total final consumption expenditure, both private and government, decelerated during this period indicating dominance of investment demand (Table 10). Around 37 per cent of the incremental growth in real GDP during April-June 2007 was on account of private final consumption demand (49.6 per cent during April-June 2006), while around 48 per cent (50.7 per cent a year ago) was on account of the rise in real GFCF.

Corporate Performance

The corporate sector continued to show impressive performance during the first quarter of 2007-08, notwithstanding some deceleration in the growth of sales and profits over the corresponding quarter of 2006-07 (Table 11). Net profits of select non-Government non-financial companies rose by 33.9 per cent, benefiting from the rise in other income and the lower rise in interest payments. Buoyant asset markets and hedging gains at the back of appreciating Indian rupee appears to have helped corporates to record marked increase in other income. Interest payments as proportion to gross profits declined to 11.7 per cent in the first quarter of 2007-08 from 13.9 per cent in April-June 2006-07. Profitability in terms of gross and net profit margins-gross profits to sales and profits after tax to sales-has shown

Table 10: Disposition of National Income (at 1999-2000 prices)

(Growth rates in per cent)

Item	2005-06 QE	2006-07 RE	2006-07 RE Q1	Q2	Q3	Q4	2007-08 Q1
1	2	3	4	5	6	7	8
1. Total Final Consumption Expenditure	7.2	6.6	11.8	3.7	5.1	6.1	6.5
a. Private Final Consumption Expenditure (PFCE)	6.7	6.2	6.5	6.3	6.0	6.0	5.6
b. Government Final Consumption Expenditure	9.8	9.0	47.6	-9.7	0.4	6.6	10.5
2. Gross Fixed Capital Formation (GFCF)	15.3	14.6	15.8	13.3	15.5	14.1	15.9
3. Change in Stocks	69.0	10.2	10.2	10.6	9.7	10.3	8.4
4. Valuables	0.4	38.0	38.4	47.1	29.8	37.8	10.5
5. Exports	5.9	8.6	10.3	18.9	-1.9	8.7	5.5
6. Imports	10.3	11.4	11.7	18.7	4.8	11.3	16.1
Memo:							
Real GDP at market prices	9.2	9.4	8.1	10.7	9.0	9.6	9.2

QE : Quick Estimates. RE : Revised Estimates.
Source : Central Statistical Organisation.

Table 11: Corporate Financial Performance

(Growth rates in per cent)

Item	2004-05	2005-06	2006-07	2006-07 Q1	2006-07 Q2	2006-07 Q3	2006-07 Q4	2007-08 Q1
1	2	3	4	5	6	7	8	9
Sales	24.1	16.9	26.2	25.6	29.2	30.3	22.5	19.2
Other Income	-0.9	10.3	7.4	22.4	19.3	11.3	9.8	76.4
Expenditure	23.6	16.4	23.5	24.6	26.6	26.9	19.5	19.3
Depreciation provision	11.2	10.2	15.4	14.9	16.4	16.8	18.1	18.1
Gross profits	32.5	20.3	41.5	33.9	45.9	51.8	39.2	28.6
Interest Payments	-5.8	1.9	17.4	19.9	18.0	11.9	32.3	4.4
Profits after tax	51.2	24.2	45.2	34.7	49.4	59.5	39.6	33.9
				Select Ratios				(Per cent)
Gross Profits to Sales	11.9	13.0	15.6	15.6	15.9	15.8	15.3	16.7
Other income to Profits after tax	30.1	32.0	26.4	24.0	26.1	22.1	31.9	33.3
Profits After Tax to Sales	7.2	8.7	10.7	10.6	11.0	11.0	10.6	11.6
Interest to Sales	2.6	2.0	2.1	2.2	2.0	2.0	2.0	2.0
Interest to Gross Profits	21.8	15.7	13.3	13.9	12.8	12.5	13.0	11.7
Interest Coverage (Times)	4.6	6.4	7.5	7.2	7.8	8.0	7.7	8.5
Memo:								(Amount in Rupees crore)
No of Companies	2,214	2,210	2,388	2,228	2,263	2,258	2,356	2,342
Sales	5,49,449	7,74,578	10,41,894	2,34,610	2,51,125	2,60,064	2,94,223	2,80,814
Other income	11,927	21,600	29,385	5,962	7,245	6,331	9,963	10,879
Expenditure	4,77,609	6,66,690	8,72,168	1,95,556	2,09,437	2,16,053	2,48,740	2,34,596
Depreciation Provision	22,697	28,883	37,095	8,449	8,892	9,172	10,338	10,173
Gross profits	65,301	1,00,666	1,62,017	36,567	40,041	41,169	45,108	46,925
Interest Payments	14,268	15,789	21,500	5,083	5,121	5,162	5,862	5,504
Profits after tax	39,599	67,506	1,11,107	24,845	27,710	28,698	31,251	32,699

Note : 1. Data for 2004-05 are based on audited balance sheet, while those for 2005-06 and 2006-07 are based on their abridged financial results of the select non-Government non-financial public limited companies.
2. Growth rates are percentage changes in the level for the period under reference over the corresponding period of the previous year for common set of companies.
3. Data for the full year may not add up to the quarterly totals due to difference in the composition and number of companies covered in each period.

improvement in April-June 2007-08 over the corresponding period of the preceding year mainly on account of substantial rise in other income.

Business Expectations Surveys

Business confidence surveys conducted by various agencies present a mixed short-term outlook of the economy (Table 12). According to the latest business confidence survey conducted by Federation of Indian Chambers of Commerce and Industry (FICCI) in August 2007, the overall business confidence index during April-June 2007 marginally declined by 0.9 per cent over the previous quarter, reflecting concerns over rupee appreciation and rising interest rates. The FICCI's expectations index for July-December 2007, however, showed improvement of 2.8 per cent over the previous survey. A majority of 70 per cent of the respondents (as compared with 64 per cent respondents in the previous survey) found the current overall economic conditions to be 'moderately to substantially better' than in the preceding six months. Among the three industry sectors surveyed, respondents from the services and heavy industry sectors were less optimistic about the current performance as well as

Table 12: Business Expectations Surveys

(Per cent)

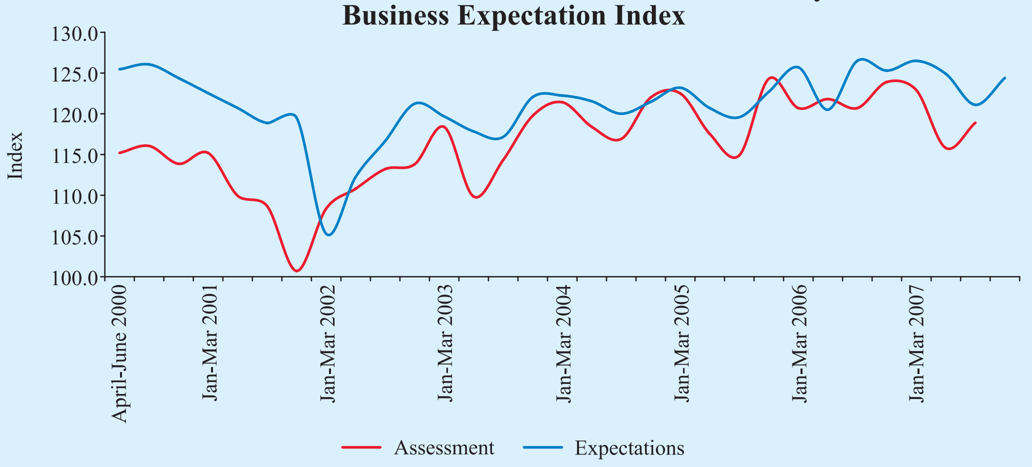
Agency	Business Expectations		Growth over a year ago	Growth over previous round
	Period	Index		
1	2	3	4	5
FICCI	July-December 2007	Expectations Index	-0.3	2.8
Dun & Bradstreet	October-December 2007	Business Optimism Index	9.1	15.5
NCAER	July-December 2007	Business Confidence Index	-2.7	-8.8
Reserve Bank of India	October-December 2007	Business Expectation Index	-0.7	2.7

performance in the ensuing six months than those from the light industry sector. The business optimism index of the survey by Dun and Bradstreet for October-December 2007 (conducted in September 2007) recorded a rise of 15.5 per cent over the preceding quarter *albeit* over a low base; five of the six optimism indices, *viz.*, volume of sales, selling prices, new orders, inventory levels and employees increased during the period. Among the sectors surveyed, expectations for October-December 2007 were the most optimistic in the capital goods and consumer durables sectors, while they were least optimistic in the case of services sector, due in part to the appreciation of the rupee.

According to the Reserve Bank's Industrial Outlook Survey conducted during July-September 2007, the business expectations indices based on assessment for July-September 2007 and on expectations for October-December 2007 increased by 2.7 per cent each over the previous quarter. In comparison with the previous year, the indices based on assessment and expectations were, however, lower by 1.5 per cent and 0.7 per cent, respectively (Chart 4).

The increase in the expectations index for October-December 2007 over the previous quarter was on account of improvement in expectations for most of

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



the parameters of the survey such as overall business situation, production, availability of finance, order books, capacity utilisation and profit margin. Expectations of increase in exports, imports, employment and selling prices were, however, lower than those in the previous quarter. The maximum proportion of respondents continued to be placed in the category of 'no change in expectations over the preceding quarter' for most of the parameters including pending orders and inventories of raw materials and finished goods (Table 13).

Table 13: Net Response on 'A Quarter Ahead' Expectations About the Industrial Performance

(Per cent)

Parameter	Response	Oct-Dec. 2006	Jan-March 2007	Apr-June 2007	July-Sept. 2007	Oct-Dec. 2007
1	2	3	4	5	6	7
1. Overall business situation	Better	51.8 (41.2)	53.7 (40.7)	51.7 (43.3)	49.5 (41.2)	50.5 (42.1)
2. Financial situation	Better	41.9 (50.6)	44.5 (49.9)	43.8 (49.8)	41.3 (49.8)	40.1 (51.3)
3. Working capital finance requirement	Increase	35.4 (58.3)	36.2 (59.2)	35.3 (59.2)	34.5 (59.2)	32.2 (62.6)
4. Availability of finance	Improve	33.4 (57.8)	36.2 (56.6)	35.2 (57.2)	32.1 (58.6)	33.8 (58.8)
5. Production	Increase	49.7 (39.6)	50.7 (40.1)	47.8 (41.6)	46.6 (41.1)	49.0 (40.9)
6. Order books	Increase	46.3 (42.6)	47.3 (43.1)	45.7 (45.4)	43.6 (46.1)	44.1 (46.0)
7. Pending orders, if applicable	Below normal	-2.1 (81.7)	-2.7 (82.9)	-2.2 (82.8)	2.2 (82.6)	-3.5 (82.4)
8. Cost of raw material	Decrease	-49.2 (46.4)	-41.7 (51.0)	-42.1 (52.0)	46.0 (49.7)	-42.4 (51.0)
9. Inventory of raw material	Below average	-6.1 (83.5)	-7.1 (83.8)	-7.3 (85.0)	5.4 (85.0)	-6.3 (85.0)
10. Inventory of finished goods	Below average	-4.9 (83.5)	-5.2 (84.5)	-4.4 (85.2)	2.7 (87.1)	-3.5 (86.4)
11. Capacity utilisation (Main product)	Increase	33.2 (56.6)	33.3 (57.7)	29.4 (60.4)	27.0 (61.4)	28.4 (61.5)
12. Level of capacity utilisation (Compared to the average in the preceding four quarters)	Above normal	10.9 (76.6)	12.8 (76.4)	11.5 (77.1)	9.4 (76.5)	10.7 (77.2)
13. Assessment of the production capacity (With regard to expected demand in the next six months)	More than adequate	5.1 (79.7)	4.8 (81.8)	4.0 (82.2)	3.0 (82.2)	4.2 (83.0)
14. Employment in the company	Increase	17.9 (73.3)	18.1 (73.7)	18.3 (73.3)	17.4 (73.5)	16.7 (74.1)
15. Exports, if applicable	Increase	34.2 (57.2)	32.6 (57.3)	33.4 (56.8)	32.6 (55.6)	31.4 (55.9)
16. Imports, if any	Increase	23.4 (68.1)	20.8 (68.0)	21.6 (68.4)	23.7 (68.2)	20.8 (68.6)
17. Selling prices are expected to	Increase	16.8 (68.0)	14.2 (69.2)	15.5 (68.9)	19.0 (67.1)	13.0 (68.5)
18. If increase expected in selling prices	Increase at lower rate	14.5 (67.0)	10.5 (68.1)	12.1 (66.7)	-10.4 (65.0)	-3.7 (66.8)
19. Profit margin	Increase	9.2 (60.6)	11.6 (61.7)	9.9 (62.5)	7.5 (62.6)	9.6 (59.6)
Memo: Number of companies included in the results		1,138	1,115	1,108	1,056	1,047

Note : 1. '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*.

2. Figures in parentheses are the percentages of respondents with 'no change over the preceding quarter' as responses.

Forecasts by various agencies for real GDP growth in 2007-08 are set out in Table 14.

Table 14: Projections of Real GDP for India by various Agencies – 2007-08

(Per cent)

Agency	Overall Growth	Agriculture	Industry	Services	Month of Projection
1	2	3	4	5	6
ASSOCHAM	8.5-8.7	–	–	–	August 2007
Confederation of Indian Industry (CII)	8.5	3.0	9.3	9.9	April 2007
	9.2	3.0	9.4	11.2	July 2007
Citigroup	9.3	3.0	10.3	10.9	April 2007
	9.3	3.0	10.0	11.0	September 2007
Merrill Lynch	8.5	–	–	–	March 2007
	8.8	4.0	9.5	10.0	September 2007
JP Morgan	8.0	–	–	–	March 2007
	8.6	2.6	9.8	10.0	September 2007
ICRA	8.5	–	–	–	April 2007
	9.0	–	–	–	September 2007
Standard and Poor	8.6	3.4	9.2	10.0	October 2007
Indicus Analytics	8.4	3.0	7.9	9.7	March 2007
	8.4	2.7	8.5	10.1	October 2007
Centre for Monitoring the Indian Economy (CMIE)	8.5	–	–	–	June 2007
	9.1	3.9	9.5	10.7	September 2007
National Council for Applied Economic Research (NCAER)	8.3	2.6	8.7	9.9	April 2007
	8.5	3.4	9.0	10.1	August 2007
Asian Development Bank	8.0	–	–	–	March 2007
	8.5	–	–	–	September 2007
International Monetary Fund	9.0 *	–	–	–	July 2007
	8.9 *	–	–	–	October 2007
Organisation for Economic Cooperation and Development (OECD)	8.5	–	–	–	May/October 2007
United Nations Conference on Trade and Development (UNCTAD)	8.5	–	–	–	September 2007
Reserve Bank of India	Around 8.5	–	–	–	April/July 2007

– : Not Available.
* : Calendar Year.

II. FISCAL SITUATION

Combined Government Finances: 2007-08

An overview of the combined finances of the Central and State Governments budgeted for 2007-08 indicates the continuance of the fiscal consolidation process. The key deficit indicators are budgeted to decline over the revised estimates for 2006-07, both in absolute terms and as percentage of GDP. The improvement in combined finances during 2007-08 would primarily reflect the strengthening of the State Governments' finances, the revenue account of which is envisaged to record a surplus. Even though the non-tax revenue would remain sluggish, buoyant tax revenue is expected to raise the revenue receipts (by 0.4 percent of GDP) in 2007-08, while revenue expenditure would be curtailed (by 0.5 per cent of GDP). Consequently, the combined revenue deficit in 2007-08 is budgeted to decline by 0.9 per cent of GDP. The envisaged improvement in the revenue account is expected to bring down the combined gross fiscal deficit (GFD) by 0.8 per cent of GDP in 2007-08 (Table 15).

Table 15: Key Fiscal Indicators

(Per cent to GDP)

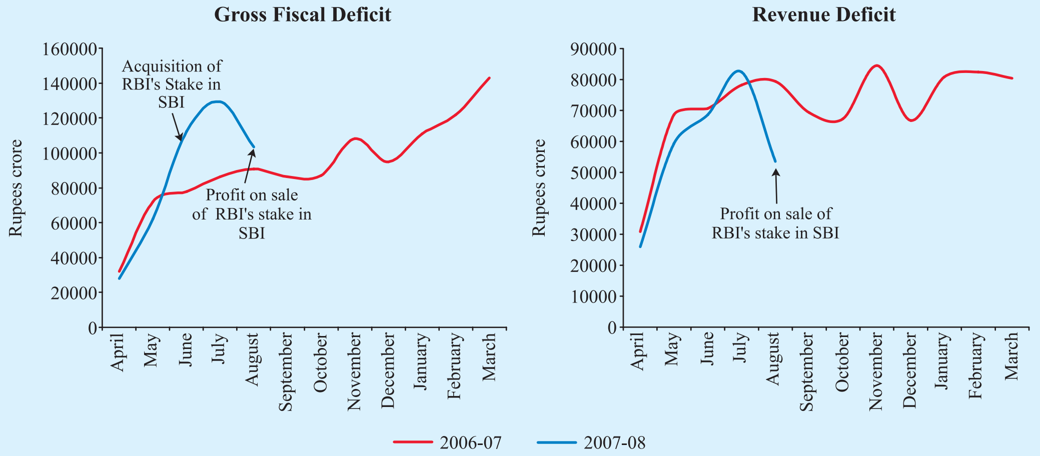
Year	Primary Deficit	Revenue Deficit	Gross Fiscal Deficit	Outstanding Liabilities *
1	2	3	4	5
		Centre		
2002-03	1.1	4.4	5.9	63.6
2003-04	-0.03	3.6	4.5	62.9
2004-05	-0.04	2.5	4.0	63.9
2005-06	0.4	2.6	4.1	63.4
2006-07 RE	0.2	2.0	3.7	61.5
	(0.2)	(1.9)	(3.5)	
2007-08 BE	-0.2	1.5	3.3	59.2
		States		
2002-03	1.3	2.2	4.2	32.5
2003-04	1.5	2.2	4.5	33.4
2004-05	0.7	1.2	3.5	33.3
2005-06	0.1	0.08	2.5	32.6
2006-07 RE	0.4	0.03	2.8	30.5
2007-08 BE	0.1	-0.4	2.4	29.6
		Combined		
2002-03	3.1	6.6	9.6	81.0
2003-04	2.1	5.8	8.5	81.6
2004-05	1.4	3.7	7.5	82.5
2005-06	0.9	2.7	6.7	80.5
2006-07 RE	0.8	2.1	6.4	77.0
2007-08 BE	0.1	1.2	5.6	74.2

RE : Revised Estimates. BE : Budget Estimates.
* : Includes external liabilities at historical exchange rates.
Note : 1. Figures in parentheses relate to provisional accounts.
2. Negative sign indicates surplus.
3. Data in respect of States are provisional from 2005-06 onwards and relate to 29 States (including National Capital Territory of Delhi).

Centre's Fiscal Situation: 2007-08

Available information on Central Government finances for 2007-08 (April-August) indicates that GFD (as proportion of the budget estimates) was placed higher than a year ago. The revenue deficit was, however, placed lower than April-August 2006 mainly on account of profit transfer from the Reserve Bank on sale of its stake in the State Bank of India (SBI). Adjusting for this transaction, revenue deficit (as proportion to budget estimates) was higher than a year ago. Tax revenue remained buoyant, rising by 22.0 per cent over April-August 2006. Non-tax revenue (net of profit on sale of Reserve Bank's stake in SBI) registered a growth of 21.2 per cent during the same period. During the first five months of 2007-08, revenue receipts (net of profit on sale of Reserve Bank's stake in SBI), however, accounted for only 26.7 per cent of the budget estimates, while the corresponding proportion for revenue expenditure was higher at 39.0 per cent. Consequently, during April-August 2007, revenue deficit (adjusted for profit on sale of Reserve Bank's stake in SBI) was 122.9 per cent of the full year budget estimates. Aggregate expenditure (adjusted for acquisition cost of Reserve Bank's stake in SBI) increased mainly on account of a sharp increase in revenue expenditure and plan capital expenditure. Plan capital expenditure increased mainly under economic services and loans and advances. Under non-plan expenditure, interest payments and subsidies were significantly higher than a year ago. GFD during the same period was 68.5 per cent of the budget estimates as against 61.0 per cent in April-August 2007(Chart 5). As against a primary

Chart 5: Key Deficit Indicators of the Centre



[1] In contrast to budget announcement of including the surplus transfer on account of transfer of Reserve Bank's stake in SBI to the Central Government under 'other capital receipts', the Controller General of Accounts (CGA) in its release of September 28, 2007 on summary information for the Central Government's Accounts for April-August 2007 has recorded this transaction under non-tax revenue receipts.

surplus of Rs.8,047 crore budgeted for 2007-08, the Centre recorded a gross primary deficit during the first five months of the year (Table 16).

Cash Management and Central Government Market Borrowings

During 2007-08 (up to October 22, 2007), the actual issuances of dated securities amounted to Rs.1,07,000 crore as against Rs.1,02,000 crore scheduled in the calendar for the same period. With the exception of one auction held on June 12, 2007 for Rs.5,000 crore, all auctions were in accordance with the indicative issuance calendar. All auctions were reissuances of existing securities, barring one new issue (10-year security) for Rs.6,000 crore on July 6, 2007.

Table 16 : Central Government Finances during April-August 2007

(Rupees crore)

Item	2007-08 (Budget Estimates)	April-August		Per cent of Budget Estimates April-August	
		2006	2007	2006	2007
1	2	3	4	5	6
1. Revenue Receipts (i + ii)	4,86,422	1,06,551	1,64,083 (1,29,775)	26.4	33.7 (26.7)
i) Tax Revenue	4,03,872	81,444	99,356	24.9	24.6
ii) Non-tax Revenue	82,550	25,107	64,727 (30,419)	32.9	78.4 (36.8)
2. Non-Debt Capital Receipts	43,151 (3,151)	3,207	3,946	27.1	9.1 (125.2)
3. Non-Plan Expenditure	4,75,421 (4,35,421)	1,46,516	1,99,042 (1,63,511)	37.4	41.9 (37.6)
of which:					
i) Interest Payments	1,58,995	51,089	63,039	36.5	39.6
ii) Defence	96,000	22,420	23,379	25.2	24.4
iii) Subsidies	51,247	23,784	30,034	53.1	58.6
iv) Grants to States	38,403	15,029	14,643	42.5	38.1
4. Plan Expenditure	2,05,100	53,920	72,325	31.2	35.3
5. Revenue Expenditure	5,57,900	1,85,949	2,17,598	38.1	39.0
6. Capital Expenditure	1,22,621 (82,621)	14,487	53,769 (18,238)	19.1	43.8 (22.1)
7. Total Expenditure	6,80,521 (6,40,521)	2,00,436	2,71,367 (2,35,836)	35.5	39.9 (36.8)
8. Revenue Deficit	71,478	79,398	53,515 (87,823)	93.7	74.9 (122.9)
9. Gross Fiscal Deficit	1,50,948	90,678	1,03,338 (1,02,115)	61.0	68.5 (67.6)
10. Gross Primary Deficit	-8,047	39,589	40,299 (39,076)	–	–

Note : Figures in parentheses are adjusted for transactions relating to transfer of the Reserve Bank's stake in SBI to the Government. Accordingly, an amount of Rs.40,000 crore was adjusted in non-debt capital receipts as well as in non-plan expenditure, capital expenditure and total expenditure in the budget estimates for 2007-08. During April-August 2007, an amount of Rs.34,308 crore, which represents transfer of profits on sale of Reserve Bank's stake in SBI in August 2007, was adjusted in non-tax revenue as well as in revenue receipts; an amount of Rs.35,531 crore which represents the actual acquisition cost of Reserve Bank's stake in SBI (including the book value of shares at Rs.1,223 crore) in June 2007 was adjusted in non-plan expenditure, capital expenditure and total expenditure.

Source : Controller General of Accounts, Ministry of Finance.

There was no devolvement on the primary dealers. Gross and net market borrowings (including 364-day Treasury Bills) during 2007-08 (up to October, 22, 2007) amounted to Rs.1,26,036 crore and Rs.75,363 crore, respectively, accounting for 66.7 per cent and 68.7 per cent of the estimated borrowings for the year. The weighted average maturity of dated securities issued during 2007-08 (up to October 22, 2007) at 14.41 years was higher than that of 14.08 years during the corresponding period of the previous year. The weighted average yield of dated securities issued during the same period increased to 8.20 per cent from 7.91 per cent (Table 17).

Table 17: Central Government Securities Issued during 2007-08

(Amount in Rupees crore/Maturity in years/Yield in per cent)

Sr. No.	Borrowings as per Issuance Auction Calendar: Period of Auction	Amount	Residual Maturity	Actual Borrowings: Date of Auction	Amount	Residual Maturity	Yield
1	2	3	4	5	6	7	8
1.	April 5-12, 2007	6,000	5-9	April 12, 2007	6,000	8.39	8.16
		4,000	20 and above	April 12, 2007	4,000	29.15	8.58
2.	April 20-27, 2007	6,000	10-14	April 27, 2007	6,000	9.71	8.16
3.	May 4-11, 2007	6,000	10-14	May 11, 2007	6,000	9.92	8.31
		4,000	20 and above	May 11, 2007	4,000	29.06	8.64
4.	May 18-25, 2007	5,000	5-9	May 25, 2007	5,000	8.26	8.24
		3,000	15-19	May 25, 2007	3,000	14.96	8.40
5.	June 1-8, 2007	6,000	10-14	June 5, 2007	6,000	9.86	8.18
		3,000	20 and above	June 5, 2007	3,000	29.00	8.52
				June 12, 2007*	5,000	9.84	8.44
6.	June 15-22, 2007	6,000	10-14	June 15, 2007	6,000	9.83	8.35
7.	July 6-13, 2007	6,000	10-14	July 6, 2007	6,000	10.00	7.99
		4,000	20 and above	July 7, 2007	4,000	28.93	8.45
8.	July 20-27, 2007	6,000	5-9	July 20, 2007	6,000	6.10	7.59
		3,000	20 and above	July 20, 2007	3,000	25.10	8.34
9.	August 3-10, 2007	6,000	10-14	August 3, 2007	6,000	9.93	7.93
		4,000	20 and above	August 3, 2007	4,000	25.06	8.45
10.	August 17-24, 2007	5,000	5-9	August 24, 2007	5,000	6.02	7.87
		2,000	10-14	August 24, 2007	2,000	9.89	7.91
11.	September 7-14, 2007	4,000	10-14	September 7, 2007	4,000	14.43	8.16
		3,000	20 and above	September 7, 2007	3,000	28.74	8.41
12.	October 5-12, 2007	6,000	10-14	October 12, 2007	6,000	9.73	7.91
		4,000	20 and above	October 12, 2007	4,000	25.20	8.45

Memo:

Year	Weighted Average Maturity	Weighted Average Yield
2003-04	14.94	5.71
2004-05	14.13	6.11
2005-06	16.90	7.34
2006-07	14.72	7.89
2006-07 (up to October 22, 2006)	14.08	7.91
2007-08 (up to October 22, 2007)	14.41	8.20

* : Not scheduled.

The Central Government's surplus cash balance of Rs.50,092 crore as at end-March 2007 was eroded rapidly and had turned into a deficit by April 27, 2007, reflecting sharp reduction in investments in Treasury Bills by the States, higher than anticipated spending and lower collections under the National Small Saving Fund (NSSF). The cash balance of the Government remained in deficit till June 17, 2007 except for a brief period of two days on May 17 and 18, 2007. On May 30, 2007, the cash deficit crossed the Ways and Means Advance (WMA) limit of Rs.20,000 crore for the first half and remained in an overdraft position till June 8, 2007. Additional issuance of 91-day and 182-day Treasury Bills amounting to Rs.27,500 crore (on six occasions), during June 6-27, 2007, auction of dated securities amounting to Rs.5,000 crore on June 12, 2007 outside the calendar, advance tax inflows for the April-June quarter and resumption of investment by States in Treasury Bills resulted in a build up of surplus position in Government balances from June 18, 2007, ahead of acquisition of the Reserve Bank's stake in SBI by the Government. With this acquisition, which involved a cash outgo of Rs.35,531 crore on June 29, 2007, the cash balance of the Government again turned into deficit of Rs.15,159 crore. The Centre's cash balances remained in deficit till August 8, 2007. Following the transfer of surplus from the Reserve Bank on August 9, 2007, the Centre's cash balance returned to a surplus mode and remained so thereafter. Reflecting advance tax flows, the cash balances exhibited the usual volatility in September 2007. As on October 19, 2007, the surplus cash balance was placed at Rs.22,021 crore. During 2007-08 (up to October 19, 2007), the Centre took recourse to WMA for 91 days as compared with 39 days during the same period in 2006-07. The Central Government resorted to overdraft on three occasions during 2007-08 (up to October 19, 2007); during the corresponding period of the previous year, the Centre did not resort to any overdraft. The average utilisation of WMA/OD during 2007-08 (up to end-September, 2007) was Rs.8,510 crore as compared with Rs.801 crore in the corresponding period of the previous year.

State Finances

State Governments in their budgets for 2007-08 have committed to improve their fiscal position in line with their Fiscal Responsibility Legislations. Notwithstanding some variations across the States, the consolidated revenue balance is budgeted to show a noticeable improvement in 2007-08, with a surplus of 0.4 per cent of GDP as compared to a deficit of 0.03 per cent of GDP in 2006-07 (RE). As a result, the GFD is estimated to decline to 2.4 per cent of GDP in 2007-08 (BE) from 2.8 per cent of GDP during 2006-07(RE). The consolidated primary deficit is budgeted at 0.1 per cent of GDP in 2007-08.

Cash Management and State Governments' Market Borrowings

The provisional net allocation under market borrowing programme for State Governments is placed at Rs.23,503 crore during 2007-08, excluding two

State Governments for which the Annual Plans are yet to be finalised. Taking into account the repayments of Rs.11,555 crore and additional allocation of Rs.5,625 crore, the gross allocation amounts to Rs.40,682 crore. During 2007-08 (up to October 22, 2007), the States have raised market loans amounting to Rs.20,362 crore (50.1 per cent of gross allocation) through auctions as compared with Rs.8,596 crore (41.3 per cent) during the corresponding period of the previous year. The cut-off yield ranged between 8.00-8.90 per cent. The weighted average interest rate on market loans firmed up to 8.33 per cent during 2007-08 (up to October 22, 2007) from 8.08 per cent in the corresponding period of the previous year (Table 18).

The average daily utilisation of WMA and overdraft by the States during 2007-08 (up to end-September 2007) at Rs.984 crore was higher than that of Rs.236 crore during the corresponding period of 2006-07 (Chart 6). Three States resorted to overdraft during 2007-08 (up to end-September 2007) as compared with one State during the corresponding period of the previous year. The WMA position as on October 19, 2007 was at Rs.19 crore.

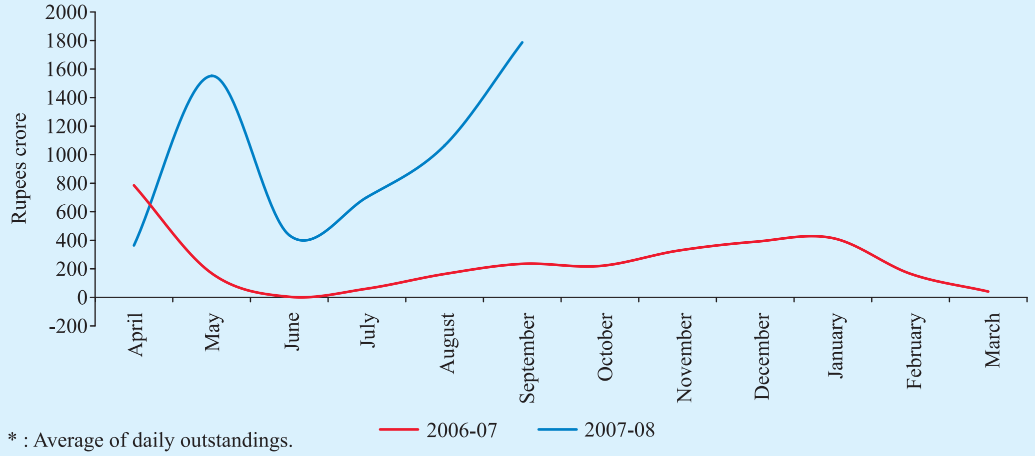
The cash surplus position of the States, as reflected in their investments in Treasury Bills (14-day and auction Treasury Bills), remained sizeable, although it declined from Rs.73,403 crore at end-March 2007 to

Table 18: Market Borrowings of State Governments during 2007-08

Item	Date	Cut-off Rate (Per cent)	Tenor (Years)	Amount Raised (Rupees crore)
1	2	3	4	5
Auctions				
i. First	April 19, 2007	8.30	10	1,837
ii. Second	May 10, 2007	8.34	10	350
iii. Third	May 17, 2007	8.40	10	1,400
iv. Fourth	June 19, 2007	8.45-8.57	10	3,566
v. Fifth	July 26, 2007	8.00-8.25	10	1,389
vi. Sixth	August 16, 2007	8.30-8.90	10	3,485
vii. Seventh	September 20, 2007	8.14-8.50	10	3,074
viii. Eighth	October 4, 2007	8.20	10	590
xi. Ninth	October 8, 2007	8.31-8.40	10	4,672
Grand Total				**20,363**
Memo:				
Year				Weighted Average Yield (per cent)
2003-04				6.13
2004-05				6.45
2005-06				7.63
2006-07				8.10
2006-07 (up to October 22, 2006)				8.08
2007-08 (up to October 22, 2007)				8.33

Source : Reserve Bank of India.

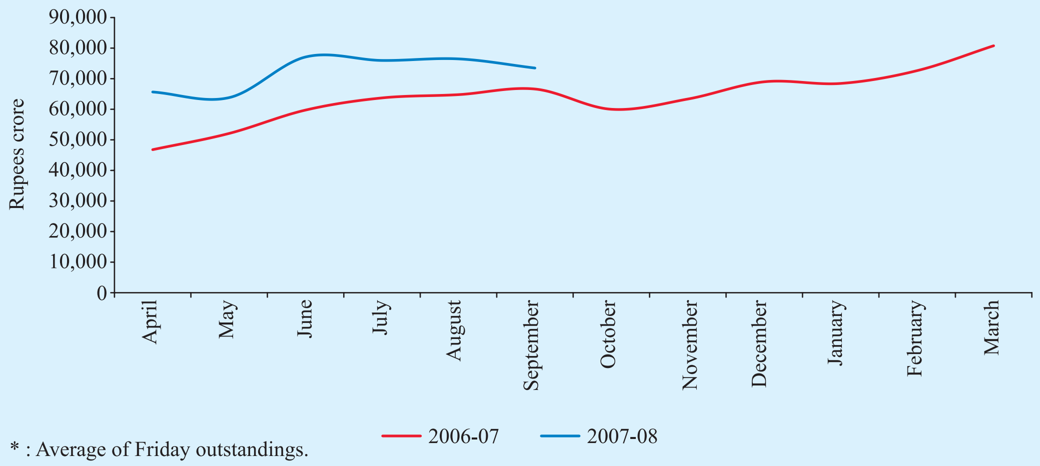
Chart 6: Utilisation of WMA and Overdraft by States*



* : Average of daily outstandings.

Rs.64,578 crore on October 19, 2007. The average investment by the States in Treasury Bills during April-September 2007 amounted to Rs.73,483 crore as against Rs.58,921 crore in the corresponding period of the previous year (Chart 7).

Chart 7: Investments in Treasury Bills by State Governments*



* : Average of Friday outstandings.

III. MONETARY AND LIQUIDITY CONDITIONS

Growth in monetary and liquidity aggregates remained strong during 2007-08 so far. Accretion to bank deposits remained buoyant, led by time deposits. Year-on-year (y-o-y) growth of broad money (M_3) on October 12, 2007 was higher than that at end-March 2007, hovering above the indicative trajectory of 17.0-17.5 per cent for 2007-08 set out in the Annual Policy Statement (April 2007). Growth in bank credit moderated during 2007-08 so far from the strong pace of the preceding three years. Banks' investments in SLR securities, as a proportion of their net demand and time liabilities (NDTL), were somewhat higher than the end-March level. Liquidity conditions during the second quarter of 2007-08 were influenced largely by movements in cash balances of the Governments and capital inflows. The Reserve Bank continued with the policy of according high priority to active management of liquidity and thereby modulated liquidity through issuances of securities under the market stabilisation scheme (MSS), operations under the liquidity adjustment facility (LAF) and changing the cash reserve ratio (CRR) as and when warranted.

Monetary Survey

For the purpose of monetary policy formulation, the Annual Policy Statement of April 2007 projected the rate of broad money (M_3) growth at around 17.0-17.5 per cent for 2007-08 in consonance with the outlook on economic growth and inflation. Consistent with the projections of money supply, the growth in aggregate deposits in 2007-08 was placed at around Rs.4,90,000 crore, while that of non-food credit including investments in bonds/debentures/shares of public sector undertakings and private corporate sector and commercial paper (CP) was projected at 24.0-25.0 per cent. Growth in M_3, year-on-year (y-o-y), was 21.8 per cent on October 12, 2007 as compared with 21.3 per cent at end-March 2007 and 18.9 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 21.5 per cent on October 12, 2007 from 19.5 per cent a year ago. Growth in liquidity aggregate, L_1, at 20.3 per cent at end-September 2007, was also higher than 19.3 per cent a year ago (Table 19 and Chart 8).

Growth of currency with the public decelerated during 2007-08. Growth in demand deposits was lower than that at a year ago and also lower than that at end-March 2007. Consequently, growth in narrow money (M_1), y-o-y, slowed down to 14.6 per cent on October 12, 2007 from 19.1 per cent a year ago and 16.8 per cent

Table 19: Monetary Indicators

(Amount in Rupees crore)

Item	Outstanding as on October 12, 2007	Variation (year-on-year)					
		October 13, 2006		March 31, 2007		October 12, 2007	
		Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6	7	8
I. Reserve Money*	7,66,077	1,03,533	20.2	1,35,961	23.7	1,50,089	24.4
II. Narrow Money (M_1)	9,65,335	1,35,118	19.1	1,38,820	16.8	1,22,995	14.6
III. Broad Money (M_3)	35,82,288	4,66,603	18.9	5,80,733	21.3	6,41,464	21.8
a) Currency with the Public	5,01,934	64,539	17.0	70,352	17.0	58,738	13.3
b) Aggregate Deposits	30,75,386	4,01,717	19.2	5,09,754	22.1	5,83,198	23.4
i) Demand Deposits	4,58,433	70,232	21.7	67,841	16.7	64,729	16.4
ii) Time Deposits	26,16,953	3,31,485	18.8	4,41,913	23.2	5,18,469	24.7
of which: Non-Resident Foreign Currency Deposits	60,702	-13,518	-17.3	7,833	13.2	-3,817	-5.9
IV. NM_3	35,89,296	4,82,094	19.5	5,71,550	20.8	6,36,279	21.5
of which: Call Term Funding from Financial Institutions	86,143	5,914	7.5	2,692	3.2	1,417	1.7
V. a) L_1	36,99,875	4,98,517	19.3	5,83,181	20.5	6,23,759	20.3
of which: Postal Deposits	1,16,886	13,775	14.2	11,631	11.2	5,863	5.3
b) L_2	37,02,807	4,98,528	19.3	5,83,181	20.4	6,23,759	20.3
c) L_3	37,28,871	5,02,412	19.3	5,85,404	20.3	6,24,245	20.1
VI. Major Sources of Broad Money							
a) Net Bank Credit to the Government (i+ii)	8,46,054	39,879	5.2	71,582	9.3	35,336	4.4
i) Net Reserve Bank Credit to Government	-1,36,711	14,109	–	-2,384	-29.3	-1,39,487	–
of which: to the Centre	-1,36,812	13,928	–	-3,024	-58.6	-1,39,378	–
ii) Other Banks' Credit to Government	9,82,765	25,769	3.3	73,967	9.8	1,74,823	21.6
b) Bank Credit to Commercial Sector	22,25,003	3,77,232	26.0	4,30,358	25.4	3,94,626	21.6
c) Net Foreign Exchange Assets	10,39,928	1,21,983	18.1	1,86,985	25.7	2,43,963	30.6
d) Government Currency Liability to Public	8,694	-753	-8.6	-467	-5.3	705	8.8
e) Net Non-Monetary Liabilities of the Banking Sector	5,37,392	71,737	16.6	1,07,725	23.2	33,165	6.6
Memo:							
Aggregate Deposits of SCBs	28,58,033	3,88,528	20.4	4,99,260	23.7	5,69,061	24.9
Non-food Credit of SCBs	19,82,156	3,70,226	30.0	4,16,006	28.4	3,77,759	23.5

* : Data pertain to October 19, 2007.

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

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

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

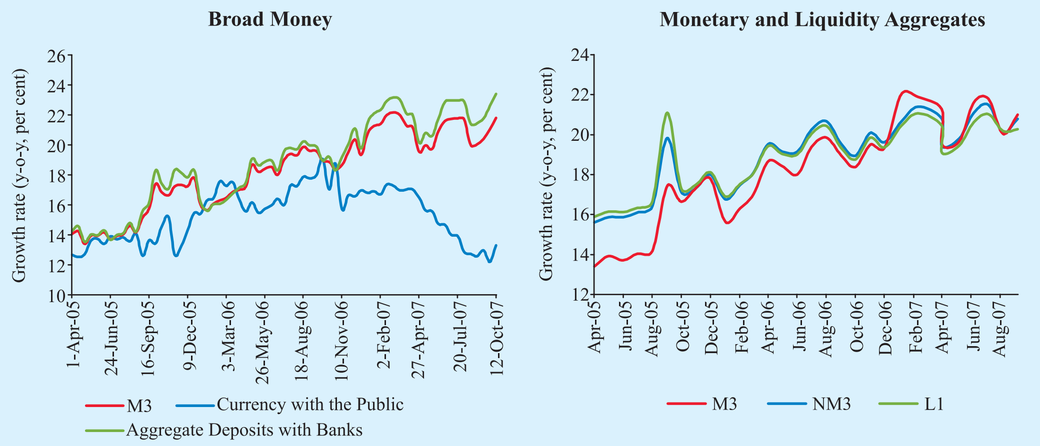
L_2 = L_1 +Term deposits with term lending institutions and refinancing institutions (FIs) + Term borrowing by FIs + Certificates of deposit issued by FIs.

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. Data for postal deposits pertain to August 2007, while liquidity aggregates pertain to September 2007.

at end-March 2007. On the other hand, growth in time deposits accelerated from 18.8 per cent on October 13, 2006 to 23.2 per cent at end-March 2007 and further to 24.7 per cent on October 12, 2007. Concomitantly, the accretion to postal deposits decelerated significantly during the year (Chart 9). 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.

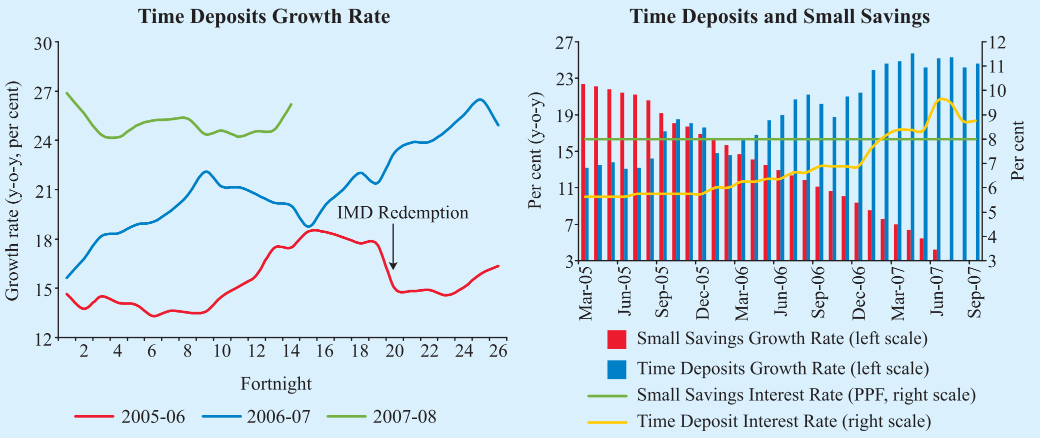
Chart 8: Money Supply



On a financial year basis, growth in M_3 during 2007-08 (up to October 12, 2007) was 8.2 per cent as compared with 7.7 per cent during the comparable period of the previous year (Table 20).

Bank credit to the commercial sector exhibited some moderation during 2007-08 so far from the strong pace of the previous three years. Scheduled commercial banks' (SCBs') non-food credit expanded by 23.5 per cent, y-o-y, as on October 12, 2007 as compared with 28.4 per cent at end-March 2007 and 30.0 per cent a year ago[1]. The deceleration in credit growth coupled with the

Chart 9: Time Deposits Growth



[1] The growth in adjusted non-food credit, that also includes investments in bonds/debentures/shares and commercial paper (CP), was 22.1 per cent, y-o-y, on October 12, 2007 as compared with 28.0 per cent a year ago.

Table 20: Monetary Aggregates – Variations

(Rupees crore)

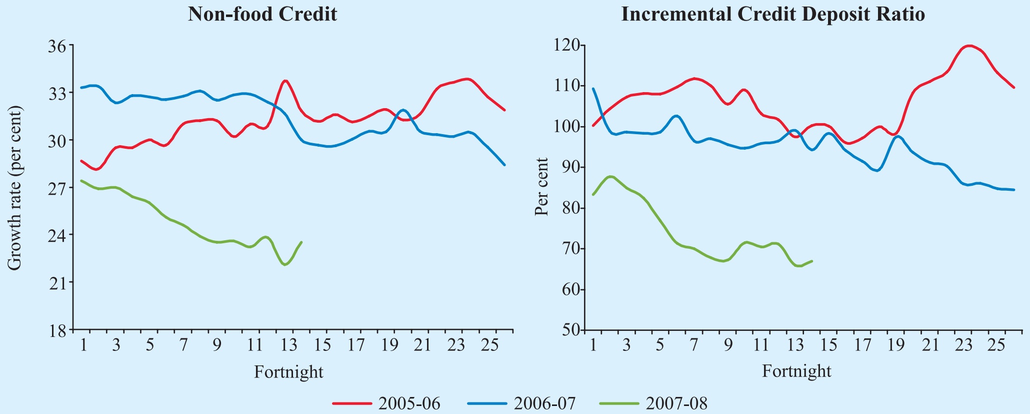
Item	2006-07 (up to Oct. 13)	2007-08 (up to Oct. 12)	2006-07 Q1	2006-07 Q2	2006-07 Q3	2006-07 Q4	2007-08 Q1	2007-08 Q2
1	2	3	4	5	6	7	8	9
M_3 (1+2+3 = 4+5+6+7-8)	2,11,279 (7.7)	2,72,010 (8.2)	55,411	1,68,401	62,951	2,93,970	76,194	1,87,954
Components								
1. Currency with the Public	30,077 (7.3)	18,464 (3.8)	23,797	-2,878	27,587	21,847	17,526	-13,937
2. Aggregates Deposits with Banks	1,82,630 (7.9)	2,56,075 (9.1)	33,227	1,70,827	35,866	2,69,833	59,104	2,03,387
2.1 Demand Deposits with Banks	-12,684 (-3.1)	-15,796 (-3.3)	-42,399	43,794	-8,252	74,697	-42,542	52,573
2.2 Time Deposits with Banks	1,95,315 (10.3)	2,71,870 (11.6)	75,626	1,27,033	44,118	1,95,136	1,01,646	1,50,814
3. 'Other' Deposits with Banks	-1,429	-2,528	-1,613	452	-502	2,291	-435	-1,496
Sources								
4. Net Bank Credit to Government	44,124 (5.8)	7,877 (0.9)	23,431	14,175	-13,204	47,180	24,833	9,669
4.1 RBI's Net Credit to Government	-5,361	-1,42,463	53	2,826	-12,754	7,490	-25,483	-54,695
4.1.1 RBI's Net credit to Centre	-2,593	-1,38,948	3,071	2,584	-12,568	3,889	-21,825	-55,588
4.2 Other Banks' Credit to Government	49,484	1,50,340	23,378	11,349	-451	39,690	50,315	64,364
5. Bank Credit to Commercial Sector	1,37,374 (8.1)	1,01,642 (4.8)	14,930	1,44,204	78,099	1,93,125	-31,873	1,40,392
6. NFEA of Banking Sector	69,771	1,26,749	58,087	20,197	43,160	65,542	-17,945	1,19,430
6.1 NFEA of RBI	74,726	1,41,949	71,845	11,392	27,250	82,682	-2,745	1,19,430
7. Government's Currency Liabilities to the Public	-766	407	-920	155	166	132	244	164
8. Net Non-Monetary liabilities of the Banking Sector	39,225	-35,335	40,117	10,330	45,269	12,009	-1,00,937	81,700
Memo:								
1. Non-resident Foreign Currency Deposits with SCBs	5,243	-6,407	3,917	1,671	1,233	1,011	-3,849	-2,110
2. SCB' Call-term Borrowing from Financial Institutions	1,582	307	3,118	-1,576	-4,468	5,618	-2,984	5,609
3. Overseas Borrowing by SCBs	431	-112	3,301	-3,685	-2,774	5,229	-6,928	7,443

SCBs : Scheduled Commercial Banks. NFEA : Net Foreign Exchange Assets.
Note : Figures in parentheses are percentage variations.

acceleration in deposits growth led to a reduction in the incremental credit-deposit ratio (y-o-y) of SCBs to 67.0 per cent as on October 12, 2007 from 94.3 per cent a year ago and 110.0 per cent at end-March 2006 (Chart 10).

Disaggregated sectoral data available up to August 17, 2007 show that about 41 per cent of incremental non-food credit (y-o-y) was absorbed by industry, compared to 33 per cent in the corresponding period of the previous year. The expansion of incremental non-food credit to industry during this period was led by infrastructure (power, port, telecommunication), textiles, iron and steel, engineering, petroleum, food processing, chemicals, vehicles and construction

Chart 10: 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.

industries. The infrastructure sector alone accounted for around 27 per cent of the incremental credit to the industry as compared with 21 per cent in the corresponding period of the previous year. The agricultural sector absorbed around 13 per cent of the incremental non-food gross bank credit expansion. Personal loans accounted for nearly 22 per cent of the incremental non-food credit; within personal loans, the share of incremental housing loans stood at 44 per cent. Growth in loans to commercial real estate remained high (Table 21).

Apart from bank credit, the corporate sector continued to fund their requirements through non-bank sources such as from capital markets, external commercial borrowings (ECBs) and internal funds. Resources raised through domestic equity issuances during second quarter of 2007-08 were higher than that during the corresponding period of the previous year. Resources raised from international markets through American depository receipts (ADRs) and global depository receipts (GDRs) during the second quarter of 2007-08 were also significantly higher than that during the corresponding period of the previous year. Net mobilisation under ECBs almost doubled during 2006-07 (April-March) and the data for the first quarter of 2007-08 show that the momentum is maintained. Internal generation of funds continued to provide a strong support to the funding requirements as profits after tax of select non-financial non-government companies during the first quarter of 2007-08 were more than 30 per cent higher than the corresponding period of the previous year (Table 22).

Commercial banks have mobilised large amounts of deposits during 2007-08 so far. Issuances of fresh capital and internal generation of funds by banks were also higher than a year ago. Strong expansion in the sources of funds along with the moderation in credit growth enabled banks to deploy their funds in

Table 21: Deployment of Non-food Gross Bank Credit

(Amount in Rupees crore)

Sector/Industry	Outstanding as on August 17, 2007	Year-on-Year Variation			
		August 18, 2006		August 17, 2007	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
Non-food Gross Bank Credit (1 to 4)	**18,09,338**	**3,48,501**	**34.8**	**3,41,920**	**23.3**
1. Agriculture and Allied Activities	**2,20,534**	**44,630**	**35.0**	**43,326**	**24.4**
2. Industry (Small, Medium and Large)	**7,10,984**	**1,13,606**	**29.0**	**1,40,531**	**24.6**
Small Scale Industries	1,19,379	15,926	21.6	28,510	31.4
3. Personal Loans	**4,64,057**	**–**	**–**	**76,649**	**19.8**
Housing	2,35,168	–	–	33,489	16.6
Advances against Fixed Deposits	40,272	7,238	28.1	7,071	21.3
Credit Cards	15,220	–	–	4,786	45.9
Education	16,926	–	–	5,145	43.7
Consumer Durables	8,515	630	8.3	334	4.1
4. Services	**4,13,763**	**–**	**–**	**81,416**	**24.5**
Transport Operators	27,655	–	–	8,117	41.5
Professional & Other Services	25,619	–	–	9,131	55.4
Trade	1,04,932	–	–	19,563	22.9
Real Estate Loans	46,665	13,262	80.1	16,145	52.9
Non-Banking Financial Companies	45,326	9,656	49.6	13,673	43.2
Memo:					
Priority Sector	**6,31,221**	**1,23,756**	**32.4**	**1,06,015**	**20.2**
Industry (Small, Medium and Large)	**7,10,984**	**1,13,606**	**29.0**	**1,40,531**	**24.6**
Food Processing	39,524	5,887	26.8	8,391	27.0
Textiles	79,362	16,117	39.1	17,378	28.0
Paper & Paper Products	11,499	1,666	24.6	1,813	18.7
Petroleum, Coal Products & Nuclear Fuels	33,252	5,563	34.2	8,752	35.7
Chemical and Chemical Products	55,360	8,750	28.5	7,672	16.1
Rubber, Plastic & their Products	9,247	2,668	64.4	1,913	26.1
Iron and Steel	65,643	15,040	45.4	11,335	20.9
Other Metal & Metal Products	20,423	4,801	44.0	2,756	15.6
Engineering	45,179	5,615	20.3	8,759	24.0
Vehicles, Vehicle Parts and Transport Equipments	24,923	5,163	52.8	5,532	28.5
Gems & Jewellery	23,417	5,516	41.0	1,657	7.6
Construction	19,877	4,302	45.7	5,237	35.8
Infrastructure	1,54,300	24,222	29.4	37,509	32.1

– : 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.

Government and other approved securities, which increased by 22.9 per cent, y-o-y, on October 12, 2007 as compared with 3.2 per cent a year ago (Table 23). Commercial bank's holdings of such securities as on October 12, 2007, at 30.0 per cent of their NDTL were the same as that of a year ago and somewhat higher than 28.0 per cent at end-March 2007 (Chart 11). Excess SLR investments of SCBs, which increased to Rs.1,56,851 crore on October 12, 2007 from Rs.1,27,842 crore a year ago and Rs.84,223 crore at end-March 2007. Banks' balances with the Reserve Bank expanded, reflecting the impact of the increase in

Table 22: Select Sources of Funds to Industry

(Rupees crore)

Item	2005-06	2006-07	2006-07				2007-08	
			Q1	Q2	Q3	Q4	Q1	Q2
1	2	3	4	5	6	7	8	9
A. Bank Credit to Industry #	**1,26,804**	**1,41,543**	**-2,336**	**49,290**	**28,415**	**66,174**	**-15,603**	**29,253 ***
B. Flow from Non-banks to Corporates								
1. Capital Issues (i+ii)	13,781	29,180	10,627	1,882	10,840	5,831	13,788	6,228
i) Non-Government Public Ltd. Companies (a+b)	13,408	29,180	10,627	1,882	10,840	5,831	13,261	4,238
a) Bonds/Debentures	245	585	0	0	491	94	0	0
b) Shares	13,163	28,595	10,627	1,882	10,349	5,737	13,261	4,238
ii) PSUs and Government Companies	373	0	0	0	0	0	527	1,990
2. ADR/GDR Issues	7,263	16,184	4,965	2,130	924	8,165	1,251	9,899
3. External Commercial Borrowings (ECBs)	45,078	88,472	20,498	14,232	16,077	37,665	33,115	–
4. Issue of CPs	-1,517	4,970	6,931	4,795	-908	-5,848	8,568	6,971 ^
C. Depreciation Provision +	**28,883**	**37,095**	**8,449**	**8,892**	**9,172**	**10,338**	**10,173**	–
D. Profit after Tax +	**67,506**	**1,11,107**	**24,845**	**27,710**	**28,698**	**31,251**	**32,699**	–

– : Not Available. ^ : Up to September 15, 2007. * : Up to August 17, 2007.

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

+ : Data are based on abridged results of select non-financial non-Government companies. Data for the full year may not add up to the quarterly totals due to difference in the composition and number of companies covered in each period (see Chapter 1).

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

their NDTL as well as the increase in the CRR. Banks' holdings of foreign currency assets declined, while their overseas borrowings expanded.

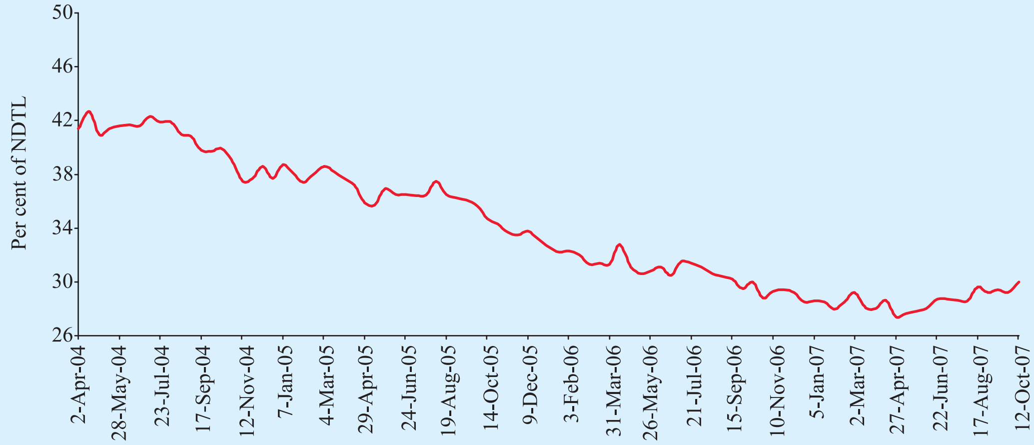
Table 23: Scheduled Commercial Bank Survey

(Amount in Rupees crore)

Item	Outstanding as on Oct. 12, 2007	Variation (year-on-year) As on Oct. 13, 2006		As on Oct. 12, 2007	
		Amount	Per cent	Amount	Per cent
1	2	3	4	5	6
Sources of Funds					
1. Aggregate Deposits	28,58,033	3,88,528	20.4	5,69,061	24.9
2. Call/Term Funding from Financial Institutions	86,143	5,914	7.5	1,417	1.7
3. Overseas Foreign Currency Borrowings	31,793	-2,097	-6.5	1,528	5.0
4. Capital	36,392	2,049	6.9	4,845	15.4
5. Reserves	2,14,549	33,184	25.2	49,511	30.0
Uses of Funds					
1. Bank Credit	20,19,175	3,66,463	28.8	3,81,334	23.3
of which: Non-food Credit	19,82,156	3,70,226	30.0	3,77,759	23.5
2. Investments in Government and Other Approved Securities	9,42,920	23,508	3.2	1,75,748	22.9
a) Investments in Government Securities	9,23,532	25,608	3.5	1,73,765	23.2
b) Investments in Other Approved Securities	19,388	-2,100	-10.8	1,983	11.4
3. Investments in Non-SLR Securities	1,78,920	10,850	7.8	28,935	19.3
4. Foreign Currency Assets	29,669	13,803	51.7	-10,852	-26.8
5. Balances with the RBI	2,18,684	11,151	9.8	93,605	74.8

Note: Data are provisional.

Chart 11: SLR Investments by Scheduled Commercial Banks

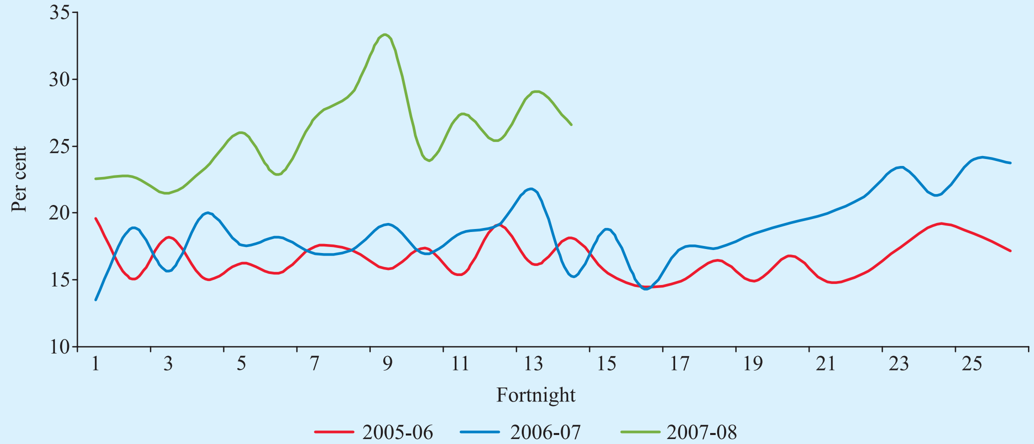


Reserve Money Survey

Reserve money expanded by 24.4 per cent, y-o-y, as on October 19, 2007 (14.9 per cent adjusted for the first round effects of the hikes in the CRR[2]) as compared with 20.2 per cent a year ago (Chart 12).

During the financial year 2007-08 (up to October 19, 2007), reserve money expanded by 8.0 per cent (3.7 per cent adjusted for the first round effect of the hikes in the CRR) as compared with 7.5 per cent in the corresponding period of 2006-07. Growth in bankers' deposits with the Reserve Bank increased by 18.7

Chart 12: Reserve Money Growth



[2] The CRR was increased by 200 basis points in stages between December 2006 and August 2007. Such increase in CRR in the first round, is estimated to have impounded banks' resources of Rs.58,500 crore.

Table 24: Reserve Money

(Amount in Rupees crore)

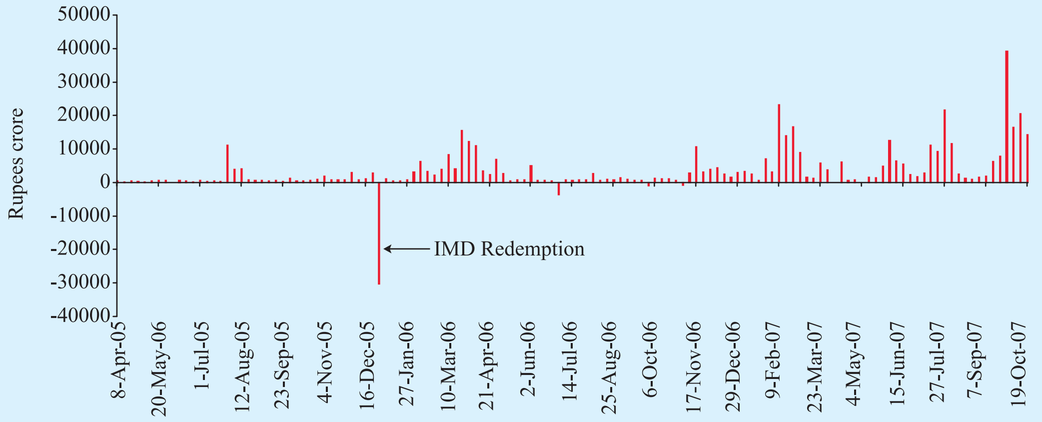
Item	2006-07 (April March)	2006-07 (Up to Oct. 20)	2007-08 (Up to Oct. 19)	Variation					
				2006-07				2007-08	
				Q1	Q2	Q3	Q4	Q1	Q2
1	2	3	4	5	6	7	8	9	10
Reserve Money	1,35,961 (23.7)	42,932 (7.5)	57,060 (8.0)	13,466	18,665	14,204	89,626	11,708	60,480
Components (1+2+3)									
1. Currency in Circulation	73,549 (17.1)	37,319 (8.7)	22,589 (4.5)	22,283	-2,011	26,871	26,405	16,943	-13,487
2. Bankers' Deposits with RBI	61,784 (45.6)	7,047 (5.2)	36,984 (18.7)	-7,204	20,224	-12,165	60,929	-4,800	75,464
3. 'Other' Deposits with the RBI	628 (9.1)	-1,434 (-20.9)	-2,513 (-33.5)	-1,613	452	-502	2,291	-435	-1,496
Sources (1+2+3+4-5)									
1. RBI's net credit to Government	-2,384	11,988	-1,46,754	53	2,826	-12,754	7,490	-25,483	-54,695
of which: to Centre (i+ii+iii+iv-v)	-3,024	15,029	-1,43,116	3,071	2,584	-12,568	3,889	-21,825	-55,588
i. Loans and Advances	0	0	0	0	0	0	0	0	0
ii. Treasury Bills held by the RBI	0	0	0	0	0	0	0	0	0
iii. RBI's Holdings of Dated Securities	26,763	491	-51,024	-27,610	24,944	22,733	6,696	-34,284	4,019
iv. RBI's Holdings of Rupee coins	-143	-132	96	9	-107	97	-142	128	20
v. Central Government Deposits	29,644	-14,670	92,189	-30,672	22,253	35,398	2,665	-12,330	59,627
2. RBI's credit to banks and commercial sector	1,990	-377	-7,770	-3,135	3,107	2,065	-47	-6,450	-1,256
3. NFEA of RBI	1,93,170 (28.7)	77,310 (11.5)	1,71,080 (19.8)	71,845	11,392	27,250	82,682	-2,745	1,19,430
of which : FCA, adjusted for revaluation	1,64,601	42,544	2,17,201	28,107	10,948	31,634	93,913	47,728	1,18,074
4. Governments' Currency Liabilities to the Public	-467	-766	407	-920	155	166	132	244	164
5. Net Non-Monetary liabilities of RBI	56,347	45,224	-40,098	54,376	-1,184	2,524	632	-46,142	3,162
Memo:									
LAF, Repos (+) / Reverse Repos (-)	36,435	8,730	-61,135	-23,060	28,395	22,195	8,905	-32,182	9,067
Net Open Market Sales # *	5,125	2,945	3,338	1,536	1,176	389	2,024	1,246	1,560
Centre's Surplus **	1,164	-19,117	-28,071	-27,320	13,313	38,713	-23,542	-34,597	15,376
Mobilisation under MSS	33,912	11,860	1,02,241	4,062	8,940	-3,315	24,225	19,643	48,856
Net Purchases(+)/Sales(-) from Authorised Dealers	1,18,994	21,545	93,268 +	21,545	0	19,776	77,673	38,873	54,395 +
NFEA/Reserve Money @	122.2	121.8	135.4	127.0	125.0	126.5	122.2	119.8	125.8
NFEA/Currency @	171.8	160.3	196.9	164.4	167.7	164.0	171.8	165.7	193.6

NFEA : Net Foreign Exchange Assets. FCA : Foreign Currency Assets. LAF : Liquidity Adjustment Facility.
* : At face value. + : Up to August 31, 2007. # : Excludes Treasury Bills. @ : per cent, end of period.
** : Excludes minimum cash balances with the Reserve Bank in case of surplus.
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.

per cent during 2007-08 (up to October 19, 2007) as compared with an increase of 5.2 per cent during the corresponding period of 2006-07. Currency in circulation expanded by 4.5 per cent as compared with 8.7 per cent during the corresponding period of the previous year (Table 24).

On the sources side, reserve money continued to be driven by the Reserve Bank's foreign currency assets (adjusted for revaluation), which rose by Rs.2,17,201 crore in 2007-08 (up to October 19, 2007) as compared with Rs.42,544 crore during the corresponding period of the previous year (Chart 13).

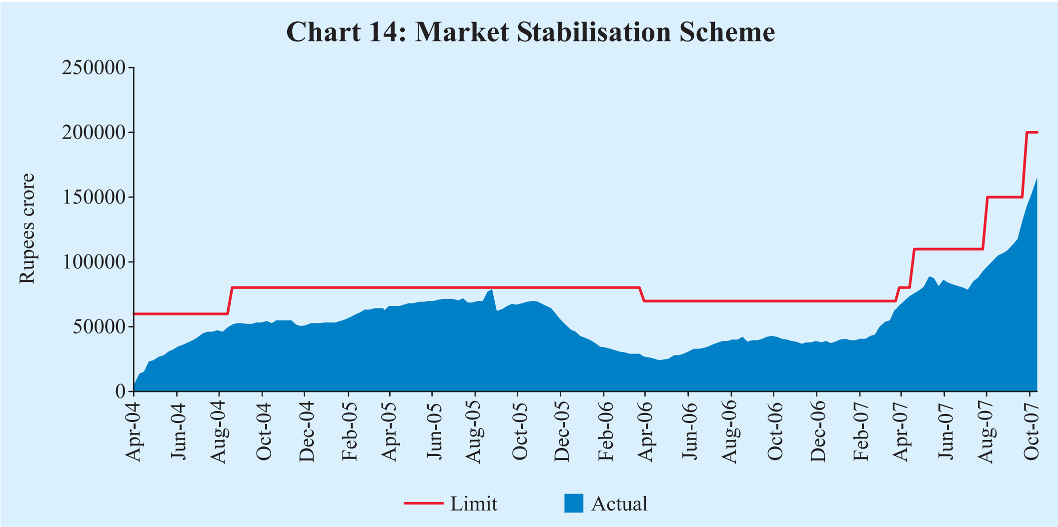
Chart 13: Accretion to RBI's Net Foreign Assets



Movements in the Reserve Bank's net credit to the Central Government largely reflected liquidity management operations by the Reserve Bank and movements in Government deposits. During 2007-08 (up to October 19, 2007), the Reserve Bank's holdings of Central Government's dated securities declined largely on account of increased absorption of liquidity under the LAF reverse repo. On the other hand, the sterilisation operations of the Reserve Bank under the MSS led to an increase in Central Government deposits with the Reserve Bank. Reflecting these developments, the Reserve Bank's net credit to the Centre declined by Rs.1,43,116 crore during 2007-08 (up to October 19) as against an increase of Rs.15,029 crore during the corresponding period of the previous year.

Liquidity Management

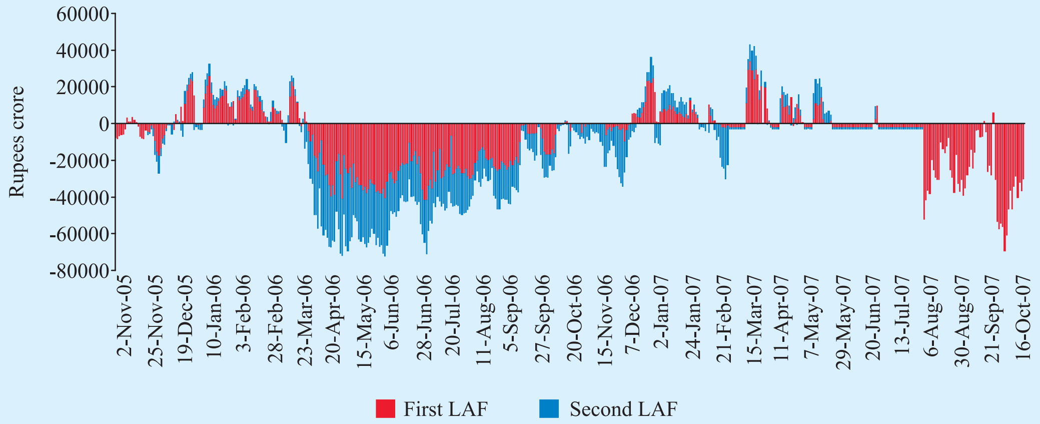
The Reserve Bank continued with its policy of active management of liquidity flexibly using various policy instruments at its disposal such as CRR, LAF and MSS. In the second quarter of 2007-08, variation in Government balances and capital inflows remained the key drivers of liquidity conditions. The Reserve Bank withdrew the ceiling of Rs.3,000 crore on daily reverse repo under LAF effective from August 6, 2007, while retaining the discretion to re-impose a ceiling as appropriate. The second LAF, which was introduced from November 2005 and had been conducted between 3:00 pm and 3:45 pm on a daily basis, was also withdrawn with effect from August 6, 2007. The Government, in consultation with the Reserve Bank, revised the ceiling for the outstanding under the MSS for the year 2007-08 to Rs.1,50,000 crore on August 8, 2007 from Rs.1,10,000 crore with Rs.1,35,000 crore set as the threshold of future revision of the ceiling. In view of the continuing large capital flows, the ceiling for the outstanding under



the MSS for the year 2007-08 was further increased to Rs.2,00,000 crore on October 4, 2007, with the threshold limit for revision set at Rs.1,85,000 crore (Chart 14). This was in consonance with the modified arrangement of the Reserve Bank's liquidity management to enhance the MSS programme and to use it more flexibly keeping in view the capital flows in the recent periods, the assessment of volatility and durability of the flows, and to restore LAF as a facility for equilibrating very short-term mismatches.

During the first quarter of 2007-08, liquidity pressures eased gradually from April 4, 2007 onwards partly on account of reduction in the Centre's cash balances 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 declined and liquidity was absorbed under the LAF reverse repos during April 9-15, 2007. The absorption under reverse repos, however, remained limited within the ceiling of Rs.3,000 crore as per the modified arrangements put in place on March 5, 2007. From mid-April 2007 onwards, liquidity conditions tightened, partly due to the hikes of 25 basis points each in the CRR effective from the fortnights beginning April 14, 2007 and April 28, 2007, leading to daily net injection of liquidity averaging Rs.9,629 crore during April 16-May 27, 2007. Liquidity pressures again started easing from May 28, 2007 onwards, reflecting increase in Government expenditure and the Reserve Bank's operations in the foreign exchange market. The LAF window shifted to an absorption mode from May 28, 2007 and remained so throughout the quarter except during June 28-July 2, 2007, when liquidity was injected through net repo operations to the tune of Rs.9,009 crore daily on an average (Chart 15). Outstanding balances under the MSS rose from Rs.62,974 crore at end-March 2007 to Rs.81,137 core by June 29, 2007 (Table 25).

Chart 15: Repo (+)/Reverse Repo (-) under LAF



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

During the second quarter of 2007-08, the Reserve Bank continued to absorb liquidity using the reverse repo window under the LAF. The sustained capital inflows and the decline in Government balances were reflected in the large

Table 25: Reserve Bank's Liquidity Management Operations

(Rupees crore)

Item	Variations								
	2006-07 (April-March)	2006-07				2007-08			
		Q1	Q2	Q3	Q4	Q1	July	August	September
1	2	3	4	5	6	7	8	9	10
A. Drivers of Liquidity (1+2+3+4+5)	61,739	36,247	-16,896	-25,641	68,028	51,935	51,012	22,854	–
1. RBI's net Purchases from Authorised Dealers	1,18,994	21,545	0	22,461	74,988	39,791	41,562	11,915	–
2. Currency with the Public	-70,352	-19,648	-1,270	-27,033	-22,400	-12,235	4,954	3,836	-144
3. Surplus Cash balances of the Centre with the Reserve Bank@	-1,164	40,207	-26,199	-30,761	15,590	49,992	0	-20,807	-9,964
4. WMA and OD	0	0	0	0	0	15,159	5,040	-20,199	0
5. Others (residual)	14,260	-5,856	10,574	9,693	-150	-40,772	-544	48,109	–
B. Management of Liquidity (6+7+8+9)	-24,257	-39,003	32,026	31,625	-48,905	-53,943	-18,735	-47,787	-2,099
6. Liquidity impact of LAF Repos	36,435	-35,315	40,650	33,600	-2,500	-20,290	-11,887	-13,863	22,925
7. Liquidity impact of OMO (Net) *	720	545	145	25	5	10	25	0	15
8. Liquidity impact of MSS	-33,912	-4,233	-8,769	4,750	-25,660	-18,163	-6,873	-18,424	-25,039
9. First round liquidity impact due to CRR change	-27,500	0	0	-6,750	-20,750	-15,500	0	-15,500	0
C. Bank Reserves (A+B) #	37,482	-2,756	15,130	5,984	19,123	-2,008	32,277	-24,933	34,195

– : Not Available.

(+) : 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 including private placement.

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

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

absorption of liquidity of Rs.52,070 crore on August 6, 2007 through reverse repo after the withdrawal of the ceiling for reverse repo[3]. The large reverse repo absorption declined gradually with the increase in Government cash balances from the second week of August and the impact of increase in CRR by 50 basis points to 7.0 per cent effective the fortnight beginning August 4, 2007. The amount of liquidity impounded due to the first round impact of the hike of the CRR was Rs.15,500 crore. Liquidity was further absorbed following the auction of dated securities and through MSS operations in August 2007. The outstanding amount of MSS reached Rs.1,06,434 crore on August 31, 2007 from Rs.92,954 crore on August 3, 2007 (Table 26).

Table 26: 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
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	-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
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
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	2,992	88,010	-20,199	70,803
August	16,855	1,06,434	20,807	1,44,096
September	-6,070	1,31,473	30,771	1,56,174
October (as on Oct. 19)	31,950	1,65,215	21,921	2,19,086

@ : 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 injection of liquidity through WMA/overdraft.
3. Between March 5 and August 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.

[3] The ceiling of Rs.3,000 crore for reverse repo, which was prevalent effective March 5, 2007, was removed effective August 6, 2007.

The average daily absorption of liquidity under the LAF declined gradually from Rs.42,059 crore during August 6-9, 2007 to Rs.25,553 during August 10-August 17, 2007 and further to Rs.12,126 during August 21-27, 2007. The absorption of liquidity under the LAF increased again during August 28-September 13, 2007 mainly resulting from a decline in Government cash balances. Liquidity was further absorbed during August 27-September 10, 2007 through auction of dated securities (Rs.14,000 crore), which was reflected in the moderation of the amount absorbed under LAF in the second week of September.

Advance tax outflows from the banking system to the Government in mid-September resulted in a decline in absorptions under LAF reverse repos. The Central Government's cash balances with the Reserve Bank also increased to Rs.38,453 crore by September 19, 2007 from Rs.13,258 crore on September 14, 2007 and averaged Rs.38,202 crore during September 23-28, 2007. The Reserve Bank injected liquidity through repo operations on September 21, 2007 (Rs.1,200 crore), for the first time in this quarter, and subsequently once more on September 28, 2007 (Rs.6,070 crore). Towards end-September, however, liquidity conditions generally remained easy following large inflow of foreign capital and the Reserve Bank broadly continued with net absorption of liquidity except on those two occasions. During October 2007, reflecting some decline in Government surplus and large capital inflows, liquidity in the system eased further, leading to average daily absorption of Rs.43,077 crore under reverse repo during October 1-23, 2007.

IV. PRICE SITUATION

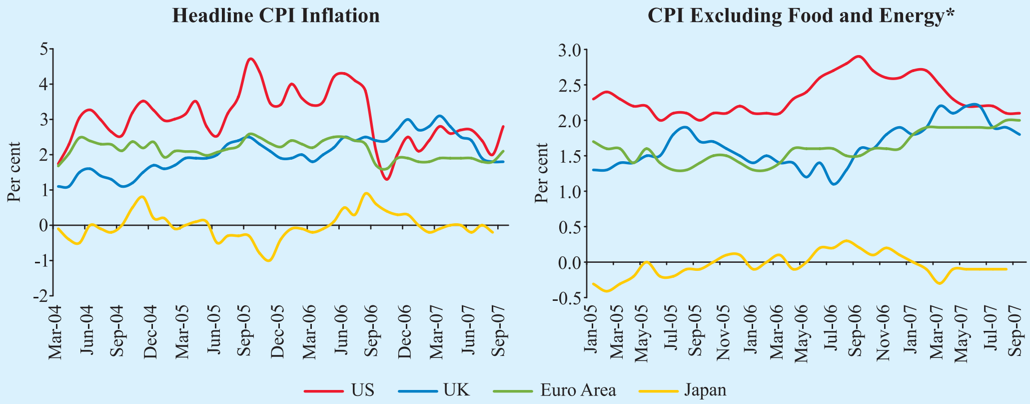
Headline inflation generally edged up in major economies during the quarter ended September 2007 as compared with the previous quarter. Core inflation also remained firm reflecting the combined impact of high commodity prices and strong demand conditions. During July 1, 2007 to October 24, 2007, several central banks (such as the Bank of England, Bank of Canada, Reserve Bank of Australia, Reserve Bank of New Zealand, Norges Bank (Norway), Sveriges Riksbank (Sweden), South African Reserve Bank, the Bank of Israel, the Bank of Korea and People's Bank of China) have further raised policy rates to contain inflation and inflationary expectations. The central bank of China also raised cash reserve requirements to address concerns regarding excess liquidity. On the other hand, central banks of Thailand, Indonesia, Turkey and Brazil have eased monetary policy during July 1, 2007 to October 24, 2007, in view of easing of inflationary pressures. After keeping its policy rate unchanged for more than a year, the US Fed also, in September 2007, reduced its target for the federal funds rate to help forestall some of the possible adverse effects of disruptions in financial markets on the broader economy. The discount rate in the US was also reduced to improve market liquidity.

In India, inflation based on the wholesale price index (WPI) eased below 4 per cent from mid-August 2007 to 3.1 per cent by October 6, 2007, partly due to base effects and negative contribution from fuel prices. Pre-emptive monetary measures since mid-2004 accompanied by fiscal and supply-side measures have helped in containing inflation. Consumer price inflation, however, remained firm during the second quarter of 2007-08 and continued to be above the WPI inflation, mainly reflecting the impact of higher food prices. Various measures of consumer price inflation were placed in the range of 5.7-7.9 per cent during August/ September 2007 as compared with 5.7-7.8 per cent in June 2007 (and 6.7-9.5 per cent in March 2007).

Global Inflation

Headline inflation in major advanced economies generally edged up towards the end of the second quarter of 2007-08, mainly reflecting hardening of food and fuel prices in the US, and clothing and education in the euro area. On the other hand, headline inflation in the UK eased due to downward contributions from housing and household services. Amongst major economies, headline inflation in September 2007 was 2.8 per cent in the US, 1.8 per cent in the UK and 2.1 per cent in the euro area as compared with 2.7 per cent, 2.4 per cent and 1.9 per cent, respectively, in June 2007 (Chart 16). Inflation fell to 1.8 per cent in August 2007 in the OECD countries from 2.2 per cent in June 2007 and 2.4 per cent in

Chart 16: Consumer Price Inflation



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

March 2007. Core inflation remained firm in major economies, reflecting strong demand conditions. In the US, CPI inflation (excluding food and energy) was 2.1 per cent in September 2007 (2.2 per cent in June 2007). In the OECD countries, CPI inflation (excluding food and energy) was 2.0 per cent in August 2007, same as in June 2007.

Many central banks further tightened monetary policy during the second quarter of 2007-08 against the backdrop of persistent inflationary pressures represented by core inflation, especially in view of continued strength of demand, ample liquidity and possible pass-through from past and present increases in oil and other commodity prices. In the UK, in view of steady growth in output, continued rapid growth in credit and broad money, limited spare capacity in businesses and elevated most indicators of pricing pressure, the risks to the outlook for inflation in the medium term were seen to lie on the upside. The Bank of England, therefore, raised its policy rate by 25 basis points on July 5, 2007 to 5.75 per cent – a cumulative increase of 125 basis points since the tightening began in August 2006 (Table 27). Notwithstanding some easing in inflation, however, the policy rate was left unchanged recognising the greater uncertainty in the outlook on inflation and growth following the turmoil in international financial markets begining August 2007.

In the euro area, risks to the price outlook were seen on the upside from increases in indirect taxes beyond those anticipated thus far and further increases in the prices of oil and agricultural products as well as stronger than expected wage developments and increase in the pricing power. The European Central Bank (ECB) viewed its monetary policy to be still on the accommodative mode with, *inter alia*, money and credit growth vigorous in the euro area amidst an

Table 27: Global Inflation Indicators

(Per cent)

Country/ Region	Key Policy Rate	Policy Rate (As on October 24, 2007)	Changes in Policy Rates (basis points)			CPI Inflation (y-o-y)		Real GDP Growth (y-o-y)	
			2005-06 (April-March)	2006-07 (April-March)	Since end-March 2007	Sep. 2006	Sep. 2007	2006 (Q2)	2007 (Q2)
1	2	3	4	5	6	7	8	9	10
Developed Economies									
Australia	Cash Rate	6.50 (Aug. 8, 2007)	0	75	25	4.0	2.1#	1.9	4.3
Canada	Overnight Rate	4.50 (July 10, 2007)	125	50	25	2.1	1.7*	2.9	2.5
Euro area	Interest Rate on Main Refinancing Operations	4.00 (June 6, 2007)	50	125	25	1.7	2.1	2.7	2.5
Japan	Uncollateralised Overnight Call Rate	0.50 (Feb. 21, 2007)	0 **	50	0	0.9	-0.2*	2.1	1.6
UK	Official Bank Rate	5.75 (July 5, 2007)	(-)25	75	50	2.4	1.8	2.7	3.1
US	Federal Funds Rate	4.75 (Sep. 18, 2007)	200	50	(-)50	2.1	2.8	3.2	1.9
Developing Economies									
Brazil	Selic Rate	11.25 (Sep. 5, 2007)	(-)275	(-)375	(-) 150	3.7	4.1	1.1	5.4
India	Reverse Repo Rate	6.00 (July 25, 2006)	75	50	0	6.3	7.3*	9.6	9.3
	Repo Rate	7.75 (Mar. 30, 2007)	50 (0)	125 (100)	0 (100)				
China	Benchmark 1-year Lending Rate	7.29 (Sep. 18, 2007)		81 (250)	90 (300) +	1.5	6.2	10.9	11.5
Indonesia	BI Rate	8.25 (July 5, 2007)	425 @	(-)375	(-)75	14.5	7.0	5.0	6.3
Israel	Key Rate	4.00 (Aug 27, 2007)	125	(-)75	0	1.3	1.4	5.2	4.4
Korea	Overnight Call Rate	5.00 (Aug. 9, 2007)	75	50 (80)	50	2.5	2.3	5.1	5.0
Philippines	Reverse Repo Rate	5.75 (Oct. 4, 2007) &	50	0	(-)175	5.7	2.7	5.5	7.5
Russia	Refinancing Rate	10.00 (June 19, 2007)	(-)100	(-)150 (150)	(-)50 (0)	9.5	9.5	7.4	7.8
South Africa	Repo Rate	10.50 (Oct. 11, 2007)	(-)50	200	150	5.4	6.7*	3.6	5.0
Thailand	14-day Repurchase Rate	5.00 (June 7, 2006)	225	50					
	1-day Repurchase Rate	3.25 (July 18, 2007)		(-)44 ^	(-)125	2.7	2.1	5.0	4.4

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

** : 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.

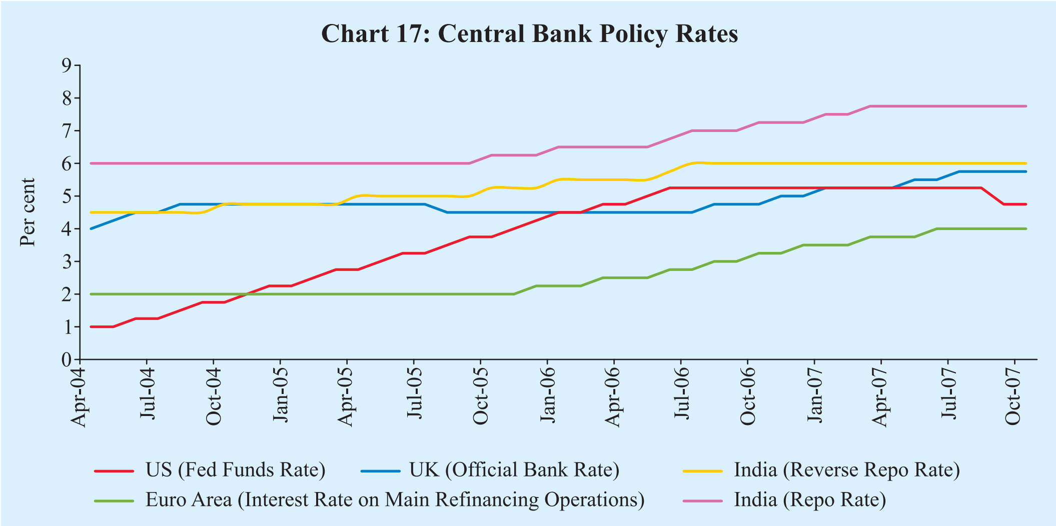
: Q2 of 2007. *: August 2007.

& : The tiering system on placements with the BSP was removed and interest rates were adjusted to 6.0 per cent for the reverse repo rate and 8.0 per cent for the repo rate effective July 13, 2007.

+ : Including 50 basis points hike to be effective from October 25, 2007.

Note : 1. For India, data on inflation pertain to CPI for Industrial Workers.
2. Figures in parentheses in column (3) indicate the date when the policy rates were last revised.
3. Figures in parentheses in columns (5) and (6) indicate the variation in cash reserve ratios during the period.

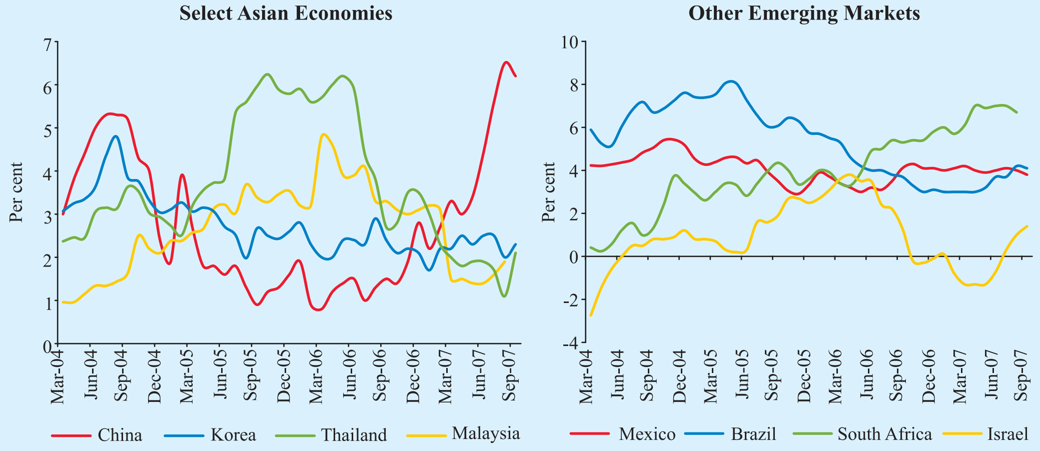
Source : International Monetary Fund, websites of respective central banks and the Economist.



increase in uncertainty emanating from financial market volatility and reappraisal of risks of recent weeks. The ECB, therefore, observed caution in the context of medium-term-oriented monetary policy strategy aimed at delivering price stability and left the key policy rates unchanged during the quarter. The policy rate was last raised by 25 basis points on June 6, 2007 – a cumulative increase of 200 basis points since the tightening began in December 2005 (Chart 17). Amongst other major advanced economies, policy rates were raised (25 basis points each) by the Bank of Canada, the Reserve Bank of Australia, the Reserve Bank of New Zealand and the Sveriges Riksbank, and Norges Bank by 50 basis points during the second quarter of 2007-08.

In the US, growth was moderate during the first half of 2007. According to the Federal Open Market Committee (FOMC), the developments in financial markets since August 2007 have increased the uncertainty surrounding the economic outlook. Viewing that the tightening of credit conditions had the potential to intensify the housing correction and to restrain economic growth more generally, the FOMC cut its target for the federal funds rate by 50 basis points to 4.75 per cent on September 18, 2007 (it had kept the rate unchanged since June 2006) to forestall some of the adverse effects on the economy that might otherwise arise from the disruptions in financial markets. The discount rate was also cut by 50 basis points each on August 17, 2007 and September 18, 2007 to 5.25 per cent to improve market liquidity. Notwithstanding some moderation in core inflation during the quarter, the FOMC noted that some inflation risks remained and monitoring of inflation developments carefully would have to be continued. Against the backdrop of moderate expansion of the Japanese economy and consumer price inflation remaining low, the Bank of Japan (BoJ) kept its policy rate unchanged at each of its meetings held since

Chart 18: Consumer Price Inflation – Emerging Market Economies



February 2007 when it had raised the uncollateralised overnight call rate (the operating target of monetary policy since March 2006) by 25 basis points to 0.50 per cent.

Amongst major emerging economies, consumer price inflation in China increased to 6.2 per cent in September 2007 (from 4.4 per cent in June 2007 and 1.5 per cent a year earlier) partly on the back of higher food prices (Chart 18). Economic activity has remained buoyant in 2007 so far with real GDP growth accelerating to 11.5 per cent during the second quarter of 2007 from 10.9 per cent a year ago. 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 72 basis points since end-June 2007 - 27 basis points effective July 21, 2007, 18 basis points effective August 22, 2007 and 27 basis points effective September 18, 2007 - to 7.29 per cent, *i.e.*, a total hike of 171 basis points since April 2006. Apart from continued issuances of its own bills to mop up liquidity, the PBC raised the cash reserve ratio (CRR) by another 150 basis points since end-June 2007 - 50 basis points each effective August 15, 2007 and September 25, 2007 and another 50 basis points to be effective October 25, 2007 - to 13.0 per cent. The CRR has, thus, been increased by 550 basis points since July 2006.

In Korea, inflation eased to 2.3 per cent in September 2007 from 2.5 per cent each in June 2007 (and September 2006) despite rise in international oil prices. Although the upward trend of real estate prices slowed down significantly, financial institutions' lending increased sharply. Against the backdrop of the domestic economy likely to maintain its upward trend, ample liquidity in the financial markets and financial market prices showing increased volatility following the recent international financial market unrest, the Bank of Korea raised its policy rate by 50 basis points during the second quarter of 2007-08 - 25 basis points each on July 12, 2007 and August 9, 2007 – to 5.0 per cent (a cumulative increase of 175 basis points since October 2005).

In other major Asian emerging economies such as Thailand and Indonesia, inflation remained relatively benign. Inflation was moderate in Thailand, at 2.1 per cent in September 2007 as compared with 1.9 per cent in June 2007 (and 2.7 per cent a year ago). Real GDP growth also remained moderate, reflecting slowdown in exports and sluggishness in private spending. According to the Monetary Policy Committee (MPC), although the risks to domestic growth and inflation remained unchanged, risks to the global economy and financial markets increased as a result of rising concerns in the US subprime market. Therefore, after lowering the 1-day repurchase rate by 25 basis points to 3.25 per cent on July 18, 2007, the Bank of Thailand left it unchanged thereafter. Thus, the policy rate has been lowered by 169 basis points since January 17, 2007, partly reversing the earlier increase of 275 basis points between June 2005 and June 2006. In Indonesia, economic activity regained momentum and the trend was likely to continue in the next quarter due primarily to stronger performance in exports, private consumption and investment. Although headline inflation edged higher to 7.0 per cent by September 2007 from 5.8 per cent in June 2007 (it remained substantially lower than the peak of 18.4 per cent in November 2005), core inflation remained largely unchanged. The Bank Indonesia noted that it would closely monitor the impact on the domestic economy from the present difficulties in the sub-prime mortgage market and the likelihood of a US economic slowdown. It also observed that despite pressures bearing down on Indonesia's financial markets and the exchange rate, financial system stability remained firm. Therefore, after cutting its policy rate by another 25 basis points to 8.25 per cent on July 5, 2007, the Bank Indonesia kept it unchanged since then. The policy rate had been cut by a total of 450 basis points since May 2006 to support growth. The policy rate had earlier been raised by 425 basis points during July-December 2005 to contain inflation.

Amongst other emerging economies, the South African Reserve Bank raised its policy rate by 100 basis points - 50 basis points each on August 16, 2007 and October 11, 2007 - to 10.50 per cent. The policy rate has been raised by 300 basis points since June 2006 to contain inflationary pressures emanating from oil and food prices and high rates of household consumption expenditure. The MPC noted that the recent financial market developments in some of the developed economies have had a spill-over effect on emerging markets including South Africa, although financial market turbulence appears to have subsided somewhat as per its latest assessment. On the other hand, the central bank of Turkey, after keeping the policy rates unchanged since August 2006 due to slowdown in domestic demand and moderation in inflation expectations, cut its policy rate by 25 basis points on September 13, 2007 and 50 basis points on October 16, 2007. The MPC noted that aggregate demand conditions continued to support the disinflation process and notwithstanding the risks related to energy, food and administered prices, inflation is expected to decelerate owing to the lagged effects of strong monetary tightening. The central bank of 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 volatility in international financial markets.

The central bank of Brazil also reduced its policy rate further by 75 basis points during the second quarter of 2007-08 – 50 basis points on July 18, 2007 and 25 basis points on September 5, 2007 – to 11.25 per cent in view of weak economic activity/benign inflation. The policy rate has, thus, been reduced by 850 basis points since September 2005. On the other hand, the Bank of Israel initially lowered its policy rate by 25 basis points each during May and June 2007 but increased its policy rate by 25 basis points each on July 23, 2007 and August 27, 2007 to 4.0 per cent in view of acceleration in inflation.

In Russia, consumer price inflation remained high, increasing from 7.4 per cent in March 2007 to 8.5 per cent in June 2007 and further to 9.5 per cent in September 2007. Growth in money supply (M2) accelerated to 50 per cent, year-on-year, as on September 1, 2007 from 45 per cent a year ago. The Bank of Russia which had raised the required reserve ratio on credit institutions' liabilities to non-resident banks in roubles and foreign currency by another 100 basis points to 4.5 per cent effective July 1, 2007, reduced it by 100 basis points to 3.5 per cent effective October 11, 2007. The refinancing rate has remained unchanged since June 2007, when it was reduced by 50 basis points to 10.0 per cent.

An assessment of key macroeconomic indicators in select EMEs shows that consumer price inflation was in the range of 1.4-9.5 per cent in select EMEs in August/September 2007 and inflation in India was the second highest amongst the select EMEs. Real policy rates in most countries ranged between 0.5 and 3.3 per cent in September 2007 (Table 28). Major EMEs, except India and South Africa, recorded surplus in current accounts in 2006. The real effective exchange rate (REER) for EMEs shows a mixed pattern in the recent period; in September 2007, while currencies of Korea, Indonesia and Israel exhibited depreciation, on a year-on-year basis, those of countries like India, China, Brazil, the Philippines, Thailand, South Africa and Russia underwent real appreciation. Although the Centre's fiscal deficit in India declined during 2006-07 and was budgeted to decline further during 2007-08, it was likely to remain higher than that in most EMEs.

Table 28: Key Macroeconomic Indicators: Emerging Markets

(Per cent)

Country	Consumer Price Inflation		Current Account Balance (per cent to GDP)		Real Effective Exchange Rate (REER)		Central Govt. Fiscal Balance (per cent of GDP)		Real Policy Rate		Real GDP Growth	
	Sept. 2006	Sept. 2007	2005	2006	Sept. 2006	Sept. 2007	2005	2006	Sept. 2006	Sept. 2007#	2005	2006
1	2	3	4	5	6	7	8	9	10	11	12	13
Brazil	3.7	4.1	1.6	1.2	6.0	10.8	-3.4	-3.2	10.6	7.2	2.9	3.7
China	1.5	6.2	7.2	9.4	0.5	6.1	-1.3 (17.9)	-0.7 (17.3)	4.4	1.1	10.4	11.1
India	**6.3** **(5.4)**	**7.3*** **(3.3)**	**-1.1** **(-6.4)**	**-1.1** **(-7.1)**	**-3.2**	**9.9**	**-4.1** **(63.4)**	**-3.5** **(61.5)**	**0.7** **(1.6)**	**0.5** **(4.5)**	**9.0**	**9.4**
Indonesia	14.5	7.0	0.1	2.7	24.4	-2.4	-0.5 (46.5)	-1.0 (40.9)	-3.3	1.3	5.7	5.5
Israel	1.3	1.4	3.3	5.6	1.7	-0.6	-2.9	-2.7	4.2	2.6	5.3	5.2
Korea	2.5	2.3	1.9	0.7	8.0	-2.5	1.9 (29.5)	1.8 (32.2)	2.0	2.7	4.2	5.0
Philippines	5.7	2.7	2.0	4.3	14.8	5.8	-2.7	-1.0	1.8	3.3	4.9	5.4
Russia	9.5	9.5	11.1	9.7	11.4	4.1	7.5	7.5	2.0	0.5	6.4	6.7
South Africa	5.4	6.7*	-4.0	-6.5	-13.5	2.9	–	–	2.6	3.3	5.1	5.0
Thailand	2.7	2.1	-4.5	1.6	9.5	3.6	0.2 (26.1)	0.1 (27.3)	2.3	1.2	4.5	5.0

#: Based on nominal policy rate as on September 30, 2007. *: August 2007.

Note :
1. For India, data pertain to fiscal years 2005-06 and 2006-07.
2. Consumer price inflation data are on a year-on-year basis. Data for India are for CPI-Industrial Workers.
3. Real policy rate is the policy rate less year-on-year consumer price inflation. For India, repo rate is used.
4. Figures in parentheses in columns (2) and (3) refer to wholesale price inflation.
5. Figures in parentheses in columns (4) and (5) refer to trade balance/GDP ratio.
6. Data on fiscal balance for Korea and Israel pertain to general government balance.
7. Figures in parentheses in columns (8) and (9) refer to central government debt/GDP ratio. For China, data refer to public sector debt.
8. Figures in parentheses in columns (10) and (11) for India are based on wholesale price inflation.
9. Data on REER refer to year-on-year variation in broad indices (CPI-based) compiled by the Bank for International Settlements. A positive figure indicates appreciation while a negative figure indicates depreciation. For India, data are based on movements in 6-currency indices.

Source : International Monetary Fund, Asian Development Bank, Bank for International Settlements, World Bank, official websites of respective central banks and the Economist.

While some countries have prioritised inflation objectives in the hierarchy of their policy goals, some other countries continue to pursue multiple objectives (Table 29). In the light of responses of central banks to the recent turbulence in financial markets, it is becoming evident that central banks do have a role beyond inflation targeting. Although the outlook on inflation remained uncertain, central banks of some economies, including inflation targeters such as Bank of England, reacted to the volatility in financial markets by injecting liquidity in order to limit the adverse impact of the financial turmoil on the real economic activity. Central banks like the US Federal Reserve with price stability as the predominant objective of monetary policy, responded to the financial market developments by injecting additional liquidity as well as cutting key policy rates to support growth and ensure financial stability. This suggests that both growth and financial stability matter for all the central banks.

Table 29: Inflation Target as Defined in Law/Policy – Select Countries

Country	Target/Objective	Measure	Additional Considerations (if any)
Inflation Targeting Countries			
United Kingdom	Price stability is defined by the Government's inflation target of 2%. The Government's inflation target is announced each year by the Chancellor of the Exchequer in the annual Budget Statement. The target is expressed in terms of an annual rate of inflation based on CPI.	CPI	If the target is missed by more than 1 percentage point on either side, the Governor must write an open letter to the Chancellor explaining the reasons why inflation has deviated from the target and what the Bank proposes to do to bring inflation to the target.
Australia	As agreed by the Governor and the Treasurer in the Third Statement on the Conduct of Monetary Policy, 2006, the appropriate target for monetary policy is to achieve an inflation rate of 2-3% on average, over the cycle.	CPI	The target is defined as a medium-term average rather than as a hard-edged target band within which inflation is to be held at all times.
New Zealand	The Reserve Bank of New Zealand (RBNZ) Act requires that price stability be defined in a specific and public contract, negotiated between the Government and the Reserve Bank, which is called the Policy Targets Agreement (PTA). As per the current PTA (there have been seven PTAs since the passage of the RBNZ Act, 1989) price stability is defined in terms of an inflation target of 1-3% on average over the medium term, defined in terms of the all groups CPI, as published by Statistics New Zealand.	CPI	The Act requires that the PTA sets out specific price stability targets and the agreement, or any changes to it, must be made public. The PTA also says that when external events push inflation above or below its medium term trend, "the Bank will respond consistent with meeting its medium term target". Furthermore, as it implements monetary policy to achieve price stability, the Bank "shall seek to avoid unnecessary instability in output, interest rates and the exchange rate."
Canada	Canada's monetary policy is built on a framework consisting of two key elements, namely, flexible exchange rate and inflation control target. At present, the inflation control target range established by the Bank of Canada and the federal government is 1-3% annual inflation as measured by the rate of change in the total CPI.	CPI	To keep inflation within this range, monetary policy aims at the 2% target mid-point over the six to eight quarters that are required for monetary policy to have most of its effect. By consistently aiming at 2 per cent for the 12-month rate of inflation, monetary policy can enhance the predictability of average inflation over longer time horizons.
Korea	As per the Bank of Korea Act (Formulation of operation plan of monetary policy), the Bank determines the annual inflation target for each year in consultation with the government. Currently, the target has been set for the period 2007-2009 as a range of $3\pm0.5\%$ in terms of the 3-year average of annual consumer price inflation.	CPI	In setting the inflation target itself at this range, the Bank aims to reflect the appropriate rate of inflation consistent with Korean economic fundamentals and to allow itself flexibility in conducting monetary policy to deal with short-term economic fluctuations.
Thailand	The Bank of Thailand decided to launch inflation targeting under the existing legal framework, whereby the Monetary Policy Board (MPB) was first appointed on April 5, 2000 and vested with the power to decide monetary policy by the Governor. Currently, the inflation target is set in terms of quarterly average core inflation in the range of 0 to 3.5%. The Bank adopted inflation targeting in May 2000.	Core CPI#	The amendment to the Bank of Thailand Act, which is currently going through the parliamentary process, will give the MPB its official legal status and its operational independence in the conduct of monetary policy. If core inflation strays from the target range, the MPC will have to explain why the target was breached and what measures have to be taken, as well as the time required, to bring inflation back within the range.

: Excluding raw food and energy prices from headline inflation.

Table 29: Inflation Target as Defined in Law/Policy – Select Countries *(Concld.)*

Country	Target/Objective	Measure	Additional Considerations (if any)
The Philippines	The primary objective of the BSP's monetary policy is "to promote price stability conducive to a balanced and sustainable growth of the economy" (Republic Act 7653). The adoption of inflation targeting framework of monetary policy in January 2002 is aimed at achieving this objective. The government's inflation target is defined in terms of the average year-on-year change in the CPI over the calendar year. The target for both 2006 and 2007 has been set at 4-5%.	CPI	To ensure accountability in cases where the BSP fails to achieve the inflation target, the BSP Governor issues an Open Letter to the President outlining the reasons why actual inflation did not fall within the target, along with the steps that will be taken to bring inflation towards the target.
Indonesia	Inflation targeting is consistent with the mandate of 1999 Act concerning Bank Indonesia as amended in 2004. The inflation target represents the overriding monetary policy objective set by the Government after coordinating actions with Bank Indonesia. The Government has set the inflation target for 2007 at 5±1%.	CPI	The determination of the inflation target considers the trade-off with economic growth in the effort to improve the living standards of the population. The setting of the intermediate targets is consistent with the desire to achieve a medium to long term inflation rate of 3% so that Indonesia can remain competitive with other Asian countries.
Chile	The focus of the Central Bank of Chile's monetary policy is price stability over time, taking into account the effects this policy has on economic activity and employment in the short and medium terms. Since 2001, the inflation target has been defined as a symmetrical range of 2 to 4%, centered on 3%, which must be met permanently over a medium-term horizon of two years.	CPI	Monetary policy can also play a role in stabilizing output over the short term, as long as it is consistent with meeting the inflation target in the medium term.
Other Major Countries			
Euro area	As laid down in the Treaty establishing the European Community, to maintain price stability is the primary objective. The treaty does not give a precise definition of what is meant by price stability. The Governing council of the European Central Bank (ECB) has defined price stability as a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area of below 2%.	HICP	The ECB has also clarified that, in pursuit of price stability, it aims to maintain inflation rates below, but close to, 2% over the medium term. "Without prejudice to the primary objective of price stability", the Eurosystem will also "support the general economic policies in the Community, which include a "high level of employment" and "sustainable and non-inflationary growth."
Japan	The Bank of Japan Law states that the Bank's monetary policy should be "aimed at, through the pursuit of price stability, contributing to the sound development of the national economy."		Monetary policy is implemented with the aim of maintaining price stability. Price denotes the overall level of prices of various goods and services.
US	The Federal Reserve Act says, "The Board of Governors of the Federal Reserve System and the Federal Open Market Committee shall maintain long run growth of the monetary and credit aggregates commensurate with the economy's long run potential to increase production, so as to promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates."		

Source : Websites of respective central banks.

Global Commodity Prices

Commodity prices remained firm during the second quarter of 2007-08 led by food and crude oil prices, although there was some moderation in prices of metals (Table 30 and Chart 19).

International crude oil prices, represented by the West Texas Intermediate (WTI), rose further during the second quarter of 2007-08, reflecting limited spare capacity, fall in US crude inventories, fears about hurricanes in the US disrupting refining capacity and expectations about growing tightness in supply-demand balance during the high-demand winter seasons (Table 31). WTI prices crossed US $ 80 a barrel by mid-September 2007 and reached a historical peak on October 18, 2007 at US $ 89.5 a barrel, partly due to heightened geopolitical tensions in West Asia and the weakening of the US dollar. The decision by the Organisation of the Petroleum Exporting Countries (OPEC) to raise output by 0.5 million barrels per day (mb/d) effective November 1, 2007 also could not alleviate the pressures on oil prices due to the tight demand-supply conditions. The OPEC had earlier cut production during November 2006 (1.2 mb/d) and February 2007 (0.5 mb/d) to support prices. In the first quarter of 2007-08, the Indian basket price had temporarily exceeded the WTI prices, since UK Brent and Dubai crude prices

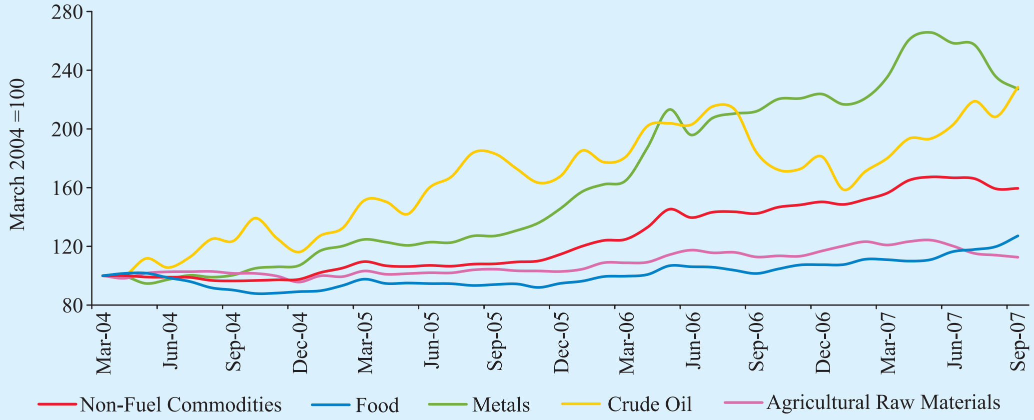
Table 30: International Commodity Prices

Commodity	Unit	2004	Index							Variation (per cent)	
			2004	2005	2006	2007				Sept. 2007 over Mar. 2007	Sept. 2007 over Sept. 2006
						Jan.-Sept.	Mar.	Jun.	Sept.		
1	2	3	4	5	6	7	8	9	10	11	12
Energy											
Coal	$/mt	53.0	100	90	93	113	105	116	129	23.3	45.0
Crude oil (Average)	$/bbl	37.7	100	142	170	174	161	181	203	26.7	23.6
Non-Energy Commodities											
Palm oil	$/mt	471.3	100	90	102	155	132	171	176	33.2	66.7
Soybean oil	$/mt	616.0	100	88	97	131	117	135	158	35.2	61.3
Soybeans	$/mt	306.5	100	90	88	114	105	118	140	33.6	66.8
Rice	$/mt	237.7	100	120	128	135	134	136	137	2.0	5.1
Wheat	$/mt	156.9	100	97	122	144	127	142	208	64.0	66.6
Sugar	c/kg	15.8	100	138	206	140	146	130	136	-6.5	-19.2
Cotton A Index	c/kg	136.6	100	89	93	99	94	98	109	15.2	14.3
Aluminium	$/mt	1716.0	100	111	150	158	161	156	139	-13.4	-3.3
Copper	$/mt	2866.0	100	128	235	248	225	261	267	18.6	0.6
Gold	$/toz	409.2	100	109	148	163	160	160	174	8.8	19.1
Silver	c/toz	669.0	100	110	173	196	197	197	193	-1.7	11.5
Steel cold-rolled coil/sheet	$/mt	607.1	100	121	114	107	107	107	107	0.0	-7.1
Steel hot-rolled coil/sheet	$/mt	502.5	100	126	119	109	109	109	109	0.0	-8.3
Tin	c/kg	851.3	100	87	103	164	163	166	176	8.1	66.2
Zinc	c/kg	104.8	100	132	313	329	312	344	275	-11.9	-15.3

$: 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 19: International Commodity Prices



Source: International Monetary Fund.

recorded higher increases *vis-à-vis* WTI crude prices. During July-September 2007, the Indian basket price, however, ruled below the WTI, reflecting the usual pattern. This was because the UK Brent prices fell below (by US $ 0.4 a barrel) the WTI, while the premium of the WTI over the Dubai variety increased significantly to US $ 5.5 a barrel. In contrast, during April-June 2007, Brent prices were US $ 3.8 a barrel above WTI prices while the premium of the WTI over the Dubai variety was only US $ 0.3 a barrel. Typically, WTI prices have been higher than other varieties.

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
March 2007	59.1	62.1	60.6	60.6	60.4
April 2007	63.8	67.4	63.9	65.1	65.3
May 2007	64.5	67.5	63.5	65.2	65.8
June 2007	65.8	71.3	67.5	68.2	68.1
July 2007	69.5	77.2	74.1	73.6	72.7
August 2007	67.2	70.8	72.4	70.1	68.7
September 2007	73.3	77.1	79.9	76.8	74.9

Source : International Monetary Fund and the World Bank.

For instance, during the six-year period, 2001-02 to 2006-07, WTI prices, on average, were US $ 1.7 a barrel above Brent and US $ 4.8 a barrel above Dubai crude.

In view of the tight demand-supply balance, prices were expected to remain firm. According to the US Energy Information Administration (EIA), global demand was expected to remain 1.1 million barrels a day above the global supply during 2007 (Table 32). Notwithstanding the announced increase in OPEC supply, oil market fundamentals are likely to remain under pressure reflecting rising consumption, moderate growth in non-OPEC supply and falling inventories. Accordingly, the EIA expects WTI prices to average US $ 68.8 a barrel in the calendar year 2007, higher than that of US $ 66.0 during 2006. For 2008, the EIA expects prices to average US $ 73.5 a barrel.

Metal prices eased during the second quarter of 2007-08, reflecting lower import demand and some improvement in supply. Between June 2007 and September 2007, prices of nickel, zinc and aluminum fell by 29 per cent, 20 per cent and 11 per cent, respectively, reflecting lower Chinese demand. On the other hand, copper prices remained largely range bound, while lead prices increased by 33 per cent over the same period. As a result, the IMF's metals price index declined by about 12 per cent between June-September 2007. On a year-on-year basis, in September 2007, while prices of lead (140 per cent) and tin (66 per cent) showed sharp increases, prices of other metals such as nickel, zinc and aluminium exhibited some decline. Steel prices have also declined, y-o-y, in September 2007, reflecting higher production in China and Brazil.

Food prices increased further during the second quarter of 2007-08 led by wheat and oilseeds/edible oils, reflecting a shortfall in global production, decline in stocks and rising demand for non-food uses (Chart 20). According to the assessment by the US Department of Agriculture (USDA) in October 2007, world

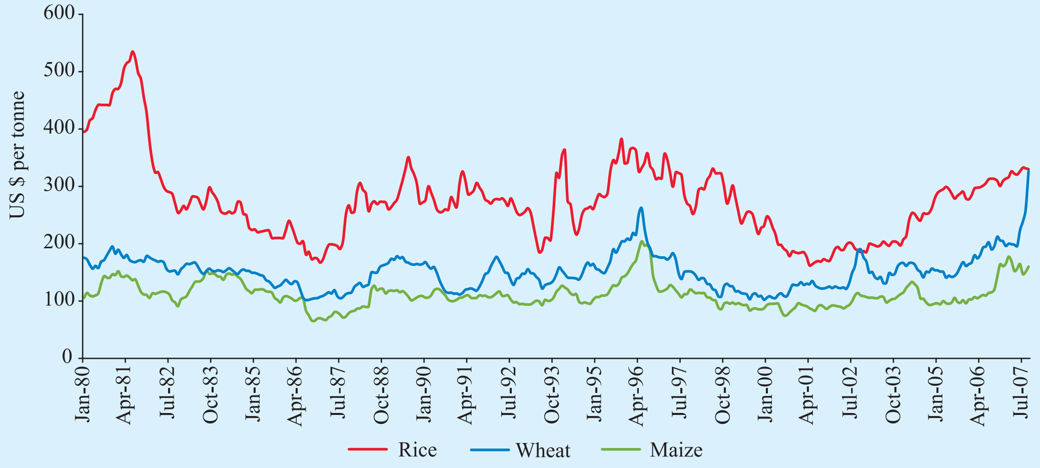
Table 32: World Supply-Demand Balance of Oil

(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	49.2	49.3	49.4	49.5	48.1	49.1	50.3
2. Non-OECD	31.2	33.0	34.4	35.4	36.5	37.8	36.0	36.4	36.5	37.1
of which: China	5.6	6.5	6.9	7.3	7.7	8.2	7.4	7.6	7.7	8.0
3. Total (1+2)	79.9	82.5	84.0	84.7	85.8	87.2	85.6	84.5	85.6	87.4
Supply										
4. Non-OPEC	48.9	50.1	50.3	49.3	49.9	50.7	49.7	49.9	49.6	50.2
5. OPEC	30.7	32.9	34.2	35.3	34.9	36.3	34.5	34.6	34.9	35.4
6. Total (4+5)	79.6	83.1	84.5	84.6	84.7	87.1	84.3	84.5	84.5	85.6
Stock Changes	0.3	-0.6	-0.5	0.1	1.1	0.1	1.3	0.0	1.1	1.8

P : Projections.
Source : US Energy Information Administration, October 9, 2007.

Chart 20: Prices of Rice, Wheat and Maize



vegetable oils stocks fell by 16 per cent during 2006-07 and were expected to fall by an additional 9 per cent in 2007-08. Edible oil prices increased moderately during the second quarter; on a y-o-y basis, however, prices in September 2007 were higher in the range of 61-67 per cent. Prices had hardened by about 15-30 per cent between March 2007 and June 2007. Amongst other food items, prices of wheat rose by 46 per cent between June-September 2007 on top of 12 per cent increase during March-June 2007, taking the y-o-y rise in September 2007 to 67 per cent. According to the USDA, although global wheat production is expected to increase by about 1 per cent in 2007-08 (June-May), global wheat stocks are likely to decline further in 2007-08 to 107.0 million tonnes - their lowest levels since 1981-82. Rice prices also remained firm, reflecting low stocks. According to the USDA, rice stocks are expected to decline by about 8 per cent during 2007-08. The overall food price index compiled by the IMF increased by about 25 per cent in September 2007 (y-o-y) on top of an increase of 8 per cent a year ago. The IMF's food price index in September 2007 has been the highest since early 1981.

International sugar prices increased by about 5 per cent during June-September 2007 in contrast to a decline of 11 per cent witnessed during March-June 2007 as the fall in domestic prices in exporter countries such as Brazil and India was offset by firm prices in importing countries of China and Russia. Prices in September 2007, however, were still 46 per cent lower than the recent peak touched in February 2006. According to the International Sugar Organisation, global sugar production is estimated to increase further by 4.1 million tonnes to 169.6 million tonnes during 2007-08 season, exceeding global consumption by 10.8 million tonnes. Global cotton prices increased by about 11 per cent during June-September 2007, reflecting shortfalls in production. According to the latest assessment by the International Cotton Advisory Committee (ICAC), the cotlook

A index is expected to increase by about 20 per cent during 2007-08 due to an estimated decline in world cotton stocks by about 14 per cent to 10.8 million tonnes in 2007-08.

Inflation Conditions in India

The Annual Policy Statement for 2007-08 (April 2007) of the Reserve Bank had observed that the stance of monetary policy in 2007-08 would be conditioned by the patterns in which the global and, more particularly, the domestic environment unfolded. It had also reaffirmed the resolve to respond swiftly with all possible measures to developments impinging on inflation expectations and the growth momentum. Noting that the overarching policy challenge was to manage the transition to a higher growth path while containing inflationary pressures, the policy preference for the period ahead was indicated as strongly in favour of price stability and well-anchored inflation expectations with the endeavour being to contain inflation close to 5.0 per cent in 2007-08 and to the range of 4.0–4.5 per cent over the medium-term. This objective would be conducive for maintaining self-accelerating growth over the medium-term.

The First Quarter Review of Annual Statement on Monetary Policy for 2007-08 (July 2007) noted that there were indications that the combination of lagged and cumulative effects of monetary policy actions and fiscal and administrative measures for supply management have had a salutary effect on inflation expectations, and headline inflation had turned benign in sharp contrast to the last quarter of 2006-07. Going forward, the Review added that monetary management would need to be watchful of movements in commodity prices, particularly oil prices, the elevated levels of asset prices and the re-emergence of pricing power among producers as potential threats to inflation expectations. Assuming that aggregate supply management would continue to receive public policy attention and that a more active management of the capital account would be demonstrated, the outlook for inflation in 2007-08 was left unchanged in the Review.

Furthermore, the Reserve Bank reiterated its resolve to continue with its policy of active demand management of liquidity through the use of all the policy instruments at its disposal flexibly, as and when the situation warranted. On a review of the liquidity situation, it was announced to increase the cash reserve ratio (CRR) by another 50 basis points with effect from the fortnight beginning August 4, 2007 (Table 33). The CRR was earlier raised by 50 basis points in two stages of 25 basis points each effective April 14, 2007 and April 28, 2007.

Wholesale Price Inflation

Headline inflation, based on movement in the wholesale price index (WPI), eased further to 3.1 per cent (y-o-y) as on October 6, 2007 from 4.4 per cent at end-June 2007 and 5.4 per cent a year ago (it was 5.9 per cent at end-March

Table 33: Movement in Key Policy Rates and Inflation in India

(Per cent)

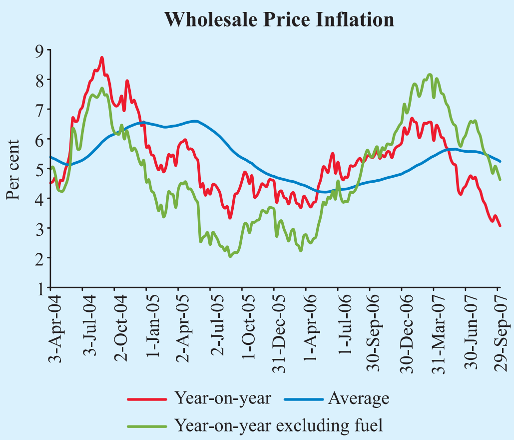
Effective since	Reverse Repo Rate	Repo Rate	Cash Reserve Ratio	WPI Inflation
1	2	3	4	5
March 31, 2004	4.50	6.00	4.50	4.6
September 18, 2004	4.50	6.00	4.75 (+0.25)	7.9
October 2, 2004	4.50	6.00	5.00 (+0.25)	7.1
October 27, 2004	4.75 (+0.25)	6.00	5.00	7.4
April 29, 2005	5.00 (+0.25)	6.00	5.00	6.0
October 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)	5.8
January 6, 2007	6.00	7.25	5.50 (+0.25)	6.4
January 31, 2007	6.00	7.50 (+0.25)	5.50	6.7
February 17, 2007	6.00	7.50	5.75 (+0.25)	6.0
March 3, 2007	6.00	7.50	6.00 (+0.25)	6.5
March 31, 2007	6.00	7.75 (+0.25)	6.00	5.9
April 14, 2007	6.00	7.75	6.25 (+0.25)	6.3
April 28, 2007	6.00	7.75	6.50 (+0.25)	6.0
August 4, 2007	6.00	7.75	7.00 (+0.50)	4.4

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.

2007). The y-o-y inflation excluding fuel, at 4.6 per cent, was above the headline inflation rate (Chart 21 and Table 34). Headline inflation has moved in a range of

Chart 21: Annual WPI Inflation



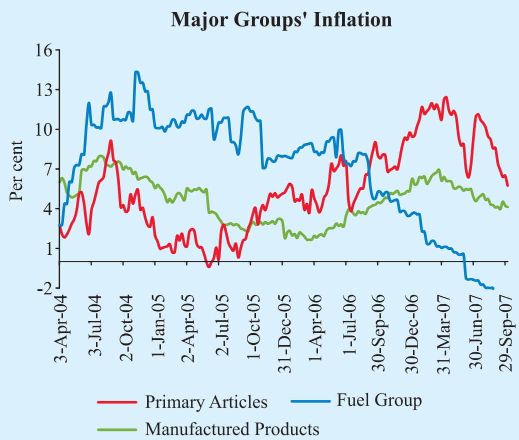


Table 34: Wholesale Price Inflation in India (year-on-year)

(Per cent)

Commodity		2006-07 (March 31)		2006-07 (October 7)		2007-08 P (October 6)	
	Weight	Inflation	WC	Inflation	WC	Inflation	WC
1	2	3	4	5	6	7	8
All Commodities	**100.0**	**5.9**	**100.0**	**5.4**	**100.0**	**3.1**	**100.0**
1. Primary Articles	**22.0**	**10.7**	**39.0**	**7.8**	**32.0**	**5.7**	**42.0**
Food Articles	15.4	8.0	20.8	8.7	25.1	3.7	19.3
i. Rice	2.4	5.7	2.1	1.2	0.5	6.7	4.6
ii. Wheat	1.4	7.3	1.8	18.3	4.5	1.7	0.8
iii. Pulses	0.6	12.5	1.4	44.0	4.7	-10.7	-2.8
iv. Vegetables	1.5	1.2	0.3	0.0	0.0	14.7	7.3
v. Fruits	1.5	5.7	1.8	9.6	3.3	-8.7	-5.4
vi. Milk	4.4	8.4	5.8	8.7	6.6	6.1	8.3
vii. Eggs, Fish and Meat	2.2	9.4	3.8	0.5	0.2	5.7	4.3
Non-Food Articles	6.1	17.2	15.6	3.4	3.6	12.7	22.7
i. Raw Cotton	1.4	21.9	3.5	9.3	1.7	12.8	4.2
ii. Oilseeds	2.7	31.6	11.0	-1.0	-0.5	26.9	19.2
iii. Sugarcane	1.3	1.1	0.3	0.7	0.2	1.1	0.5
Minerals	0.5	17.5	2.6	19.9	3.2	0.7	0.2
2. Fuel, Power, Light and Lubricants	**14.2**	**1.0**	**4.0**	**5.3**	**22.1**	**-2.3**	**-16.7**
i. Mineral Oils	7.0	0.5	1.1	5.7	14.0	-2.9	-12.5
ii. Electricity	5.5	2.3	2.8	6.0	8.2	-1.8	-4.2
iii. Coal Mining	1.8	0.0	0.0	0.0	0.0	0.0	0.0
3. Manufactured Products	**63.8**	**6.1**	**57.3**	**4.4**	**45.7**	**4.1**	**73.7**
i. Food Products	11.5	6.1	10.5	2.5	4.8	3.7	12.1
of which: Sugar	3.6	-12.7	-6.6	2.5	1.4	-15.4	-14.5
Edible Oils	2.8	14.1	4.7	5.4	2.1	11.1	7.4
ii. Cotton Textiles	4.2	-1.0	-0.6	6.4	3.8	-0.5	-0.5
iii. Man Made Fibres	4.4	3.9	1.3	5.2	2.0	-1.7	-1.2
iv. Chemicals and Chemical Products	11.9	3.6	7.1	2.5	5.3	5.2	18.8
of which: Fertilisers	3.7	1.8	1.0	2.1	1.3	0.7	0.7
v. Basic Metals, Alloys and Metal Products	8.3	11.3	17.4	6.3	11.1	4.1	12.6
of which: Iron and Steel	3.6	8.1	6.0	0.2	0.2	6.8	10.0
vi. Non-Metallic Mineral Products	2.5	9.0	3.6	12.6	5.1	8.9	6.7
of which: Cement	1.7	11.6	3.2	18.2	4.9	10.0	5.3
vii. Machinery and Machine Tools	8.4	8.1	8.6	4.6	5.4	7.1	14.4
of which: Electrical Machinery	5.0	12.9	6.7	8.0	4.5	12.8	12.9
viii. Transport Equipment and Parts	4.3	2.0	1.2	2.2	1.4	1.3	1.5
Memo:							
Food Items (Composite)	**26.9**	**7.3**	**31.2**	**6.2**	**29.9**	**3.7**	**31.3**
WPI Excluding Food	**73.1**	**5.5**	**68.8**	**5.1**	**70.1**	**2.9**	**68.7**
WPI Excluding Fuel	**85.8**	**7.4**	**96.0**	**5.4**	**77.9**	**4.6**	**116.7**

WC: Weighted Contribution. P : Provisional.

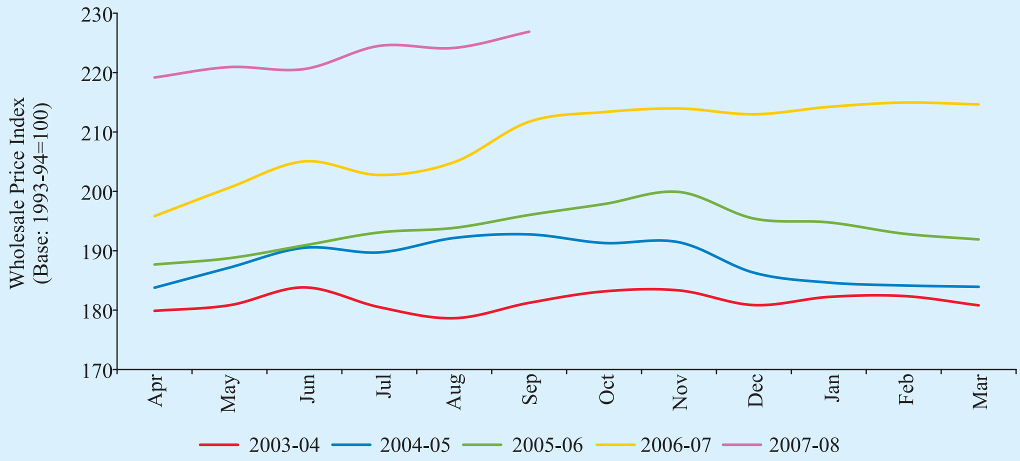
3.1-6.4 per cent during 2007-08 so far. The annual average WPI inflation rate (average of 52 weeks) for the week ended October 6, 2007 eased to 5.2 per cent from 5.6 per cent at end-June 2007, but was higher compared with 4.6 per cent a year ago.

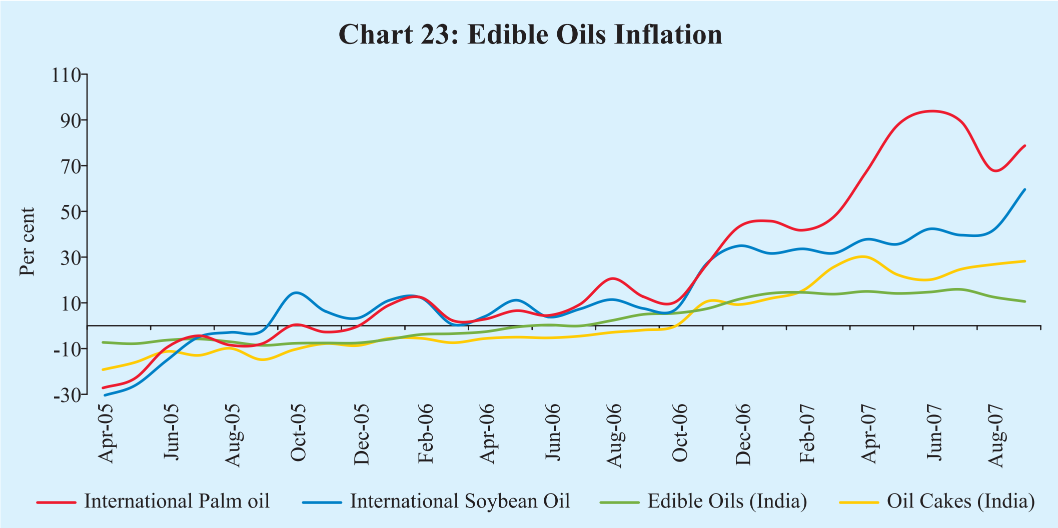
Primary articles' inflation, y-o-y, eased to 5.7 per cent on October 6, 2007 from 9.3 per cent at end-June 2007 and 7.8 per cent a year ago (it was 10.7 per cent at end-March 2007). Primary articles' inflation, y-o-y, was led by rice, vegetables, milk, oilseeds and raw cotton. Wheat prices increased marginally by 0.9 per cent between end-March 2007 and October 6, 2007, and were higher by 1.7 per cent on y-o-y basis (18.3 per cent a year ago). Prices of oilseeds increased by 26.9 per cent, y-o-y, as against a decline of 1.0 per cent a year ago, which could be attributed to lower domestic production as well as firm global prices. Raw cotton prices were 12.8 per cent higher, y-o-y, as on October 6, 2007 as compared with 9.3 per cent in the previous year (Chart 22).

Fuel group inflation, y-o-y, turned negative beginning the week ended June 9, 2007 and remained so (-2.3 per cent) on October 6, 2007, easing from 5.3 per cent a year ago, reflecting the cuts in domestic prices of petrol, diesel and other fuel products in November 2006 and February 2007. This has helped in moderating headline inflation. However, while domestic prices have remained unchanged since February 2007, international crude prices (WTI) have increased by almost 35 per cent over the same period up to September 2007. The Indian basket price of crude oil, which averaged US $ 57 a barrel in February 2007, increased to US $ 75 a barrel in September 2007. Thus, headline inflation has remained suppressed due to a halt in pass-through of higher international prices to domestic prices since February 2007.

Manufactured products inflation, y-o-y, eased to 4.1 per cent on October 6, 2007 from 4.9 per cent at end-June 2007 and 6.1 per cent at end-March 2007; it was 4.4 per cent a year ago. Manufactured products inflation was led by edible oils (increase of 11.1 per cent), oil cakes (34.6 per cent), chemicals (5.2 per

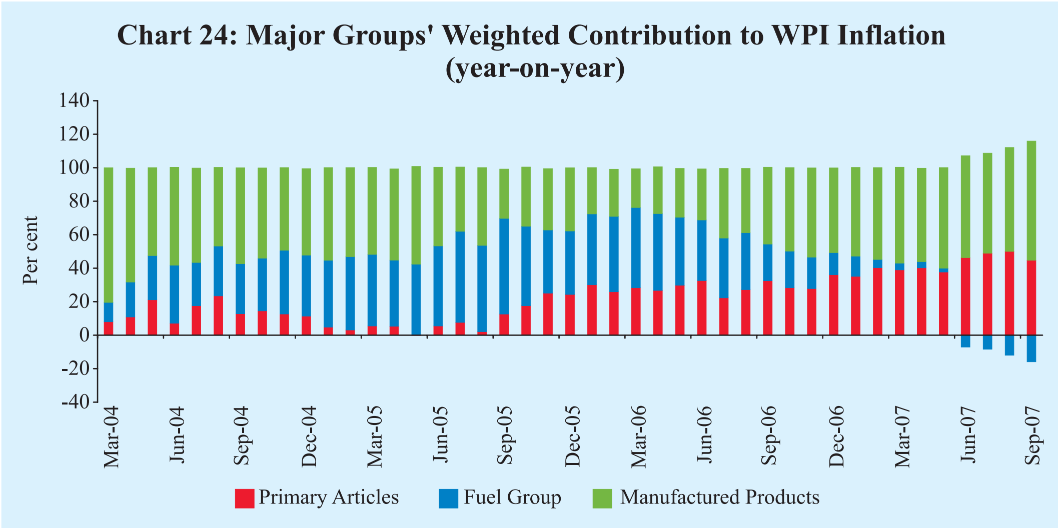
Chart 22: Primary Articles Prices





cent), cement (10.0 per cent), metals (4.1 per cent) and electrical machinery (12.8 per cent) (see Table 34). These commodities together contributed 71 per cent of the overall WPI inflation on October 6, 2007. Metals prices have remained broadly unchanged from end-June 2007 levels, although international prices, as mentioned earlier, have declined by about 12 per cent since end-June 2007. Higher prices of cement could be attributed largely to the strong demand from the construction sector and high capacity utilisation rates in the cement industry [94 per cent during 2007-08 (April-September) as compared with 90 per cent a year ago]. The hardening of electrical machinery prices reflected higher input prices as well as investment demand. The firming up of domestic edible oils and oil cakes prices reflected stagnant domestic production, increased demand and rise in international prices (Chart 23). Edible oils and oil cakes along with oilseeds accounted for 41 per cent of headline inflation on October 6, 2007. Sugar prices, however, declined by 15.4 per cent, y-o-y, and contributed negatively to manufacturing inflation.

In order to contain inflationary pressures, the Government initiated certain fiscal measures during 2007-08. 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. On July 23, 2007, the Government reduced the import duty on palm oils by five percentage points – from 50 per cent to 45 per cent in the case of crude palm oil and from 57.5 per cent to 52.5 per cent in the case of refined palm oil. As per the principle of equitable burden sharing among the different stakeholders, the Government, on October 11, 2007, decided to bear the burden to the extent of 42.7 per cent of the total under-recoveries in the retail sale of petroleum products



by oil marketing companies through issuance of oil bonds; the Government issued oil bonds worth Rs.24,121 crore during 2006-07.

Overall, manufactured products were the major driver of domestic inflation as on October 6, 2007 (with weighted contribution of 73.7 per cent) followed by primary articles (42.0 per cent) (Chart 24). The fuel group's contribution to the y-o-y headline inflation, on the other hand, was negative at 16.7 per cent.

Consumer Price Inflation

Consumer price inflation remained firm during the second quarter of 2007-08, and also remained higher than WPI inflation. This could be attributed to the higher order of increases in food prices as well as the higher weight of food items in the CPI. Various measures of consumer price inflation were placed in the range of 5.7-7.9 per cent during August/September 2007 as compared with 5.7-7.8 per cent in June 2007 (and 6.7-9.5 per cent in March 2007). Disaggregated data show that food group inflation in various CPI measures hardened to 7.7-10.3 per cent in August/September 2007 from 7.7-8.8 per cent in June 2007; it was 10.9-12.2 per cent in March 2007 (Table 35).

Asset Prices

Domestic equity prices recorded further gains during the quarter ended September 2007, with intermittent corrections (see Chapter V). Bullion prices also firmed up during the second quarter in line with international trends. Domestic equity prices, represented by the BSE sensex, increased by 12 per cent to 16,046 in September 2007 from the level of 14,334 in June 2007, reflecting

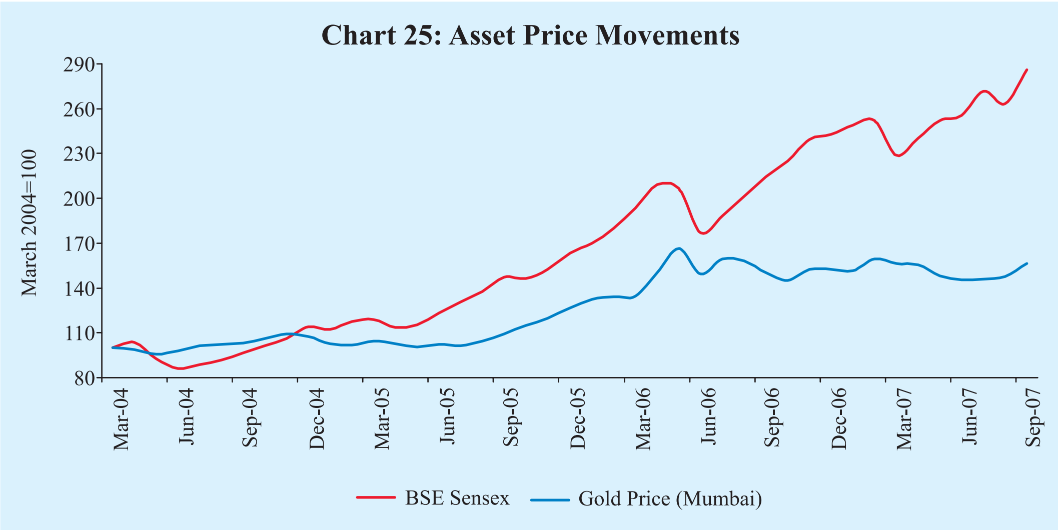
Table 35: Consumer Price Inflation – Major Groups

(Year-on-year variation in per cent)

CPI Measure	Weight	March 2003	March 2004	March 2005	March 2006	March 2007	June 2007	August 2007
1	2	3	4	5	6	7	8	9
CPI-IW (Base: 2001=100)#								
General	**100.0**	**4.1**	**3.5**	**4.2**	**4.9**	**6.7**	**5.7**	**7.3**
Food Group	46.2	3.7	3.1	1.6	4.9	12.2	8.1	9.6
Pan, Supari *etc.*	2.3	1.9	4.2	2.1	3.1	4.4	9.6	10.3
Fuel and Light	6.4	6.3	6.5	4.9	-2.9	3.2	1.6	0.8
Housing	15.3	5.4	3.9	20.4	6.6	4.1	4.1	4.0
Clothing, Bedding *etc.*	6.6	1.5	2.1	2.3	3.0	3.7	4.4	4.4
Miscellaneous	23.3	5.3	3.2	3.9	4.6	3.3	4.0	3.2
CPI-UNME (Base: 1984-85=100)								
General	**100.0**	**3.8**	**3.4**	**4.0**	**5.0**	**7.6**	**6.1**	**5.7 ***
Food Group	47.1	2.6	3.0	2.2	5.3	10.9	7.7	7.7 *
Fuel and Light	5.5	3.1	3.2	9.6	1.9	6.4	7.2	7.0 *
Housing	16.4	6.3	5.2	7.5	5.5	5.6	5.6	4.9 *
Clothing, Bedding *etc.*	7.0	2.6	2.6	2.0	2.9	3.6	4.3	4.0 *
Miscellaneous	24.0	6.0	2.8	4.4	5.1	4.4	3.7	3.2 *
CPI-AL (Base: 1986-87=100)								
General	**100.0**	**4.9**	**2.5**	**2.4**	**5.3**	**9.5**	**7.8**	**7.9 ***
Food Group	69.2	6.0	1.6	2.2	5.5	11.8	8.8	10.3
Pan, Supari *etc.*	3.8	3.5	4.7	-1.3	6.6	5.7	9.1	10.9
Fuel and Light	8.4	4.8	3.0	3.0	4.3	6.9	7.4	7.2
Clothing, Bedding *etc.*	7.0	3.0	4.1	2.5	2.2	3.5	2.7	1.9
Miscellaneous	11.7	3.1	2.7	5.5	5.5	6.8	6.7	5.6
CPI-RL (Base: 1986-87=100)								
General	**100.0**	**4.8**	**2.5**	**2.4**	**5.3**	**9.2**	**7.5**	**7.6 ***
Food Group	66.8	5.6	1.9	1.9	5.8	11.5	8.5	10.0
Pan, Supari *etc.*	3.7	3.5	4.7	-1.0	6.3	5.7	9.3	11.1
Fuel and Light	7.9	4.8	3.0	2.9	4.0	6.9	7.4	7.0
Clothing, Bedding *etc.*	9.8	3.3	3.4	2.8	2.7	3.1	2.6	2.3
Miscellaneous	11.9	3.1	3.0	5.5	5.2	6.3	6.2	5.3
Memo:								
WPI Inflation (End of period)		6.5	4.6	5.1	4.1	5.9	4.4	3.8
GDP Deflator based inflation @		3.9	3.7	4.2	4.4	5.3	5.2	–

* : September 2007. @ : Data for March pertain to full year.
\# : Data prior to January 2006 are based on the old series (Base: 1982=100).
IW : Industrial Workers. UNME : Urban Non-Manual Employees.
AL : Agricultural Labourers. RL : Rural Labourers.

strong domestic growth, better corporate performance, liquidity support from FIIs and improved market sentiment following further easing of domestic inflation since June 2007 (Chart 25). Domestic gold prices have increased by about 7 per cent since June 2007 to around Rs.9,360 per 10 grams in September 2007 (these were Rs.9,369 per 10 grams in March 2007) in line with movement in international prices, which increased by about 9 per cent over the same period. International



gold prices firmed up to above US $ 700 per ounce during September 2007 and edged up further to reach a peak of US $ 764 per ounce on October 18, 2007, reflecting weakening of US dollar, hardening of oil prices and uncertainties surrounding the global financial markets.

V. FINANCIAL MARKETS

International Financial Markets

During the second quarter of 2007-08 (July-September), international financial markets turned volatile as uncertainties about the size and distribution of losses from the US sub-prime mortgage market made investors to adjust their positions. The fallout from strains in the US sub-prime mortgage market led to spikes in yields on structured credit vehicles and in other high risk credit markets, particularly in the US and the Euro area. Rising concerns about counterparty risks led to a drying up of liquidity in various segments of the financial market which forced major central banks to step in to inject liquidity to manage volatility. The losses, though concentrated in the US, dispersed globally to European and Asian investors holding asset-backed securities and collateralised debt obligations. Within Asia, exposure was reported to be concentrated in Japan, China, Taiwan Province of China, South Korea and Australia. Uncertainty over the location and scale of exposures induced a widespread 'safe-haven' demand for short maturity Government paper for collateral and investment purposes. As a result, long-term bond yields softened. Global equity markets recorded further gains, *albeit* with intermittent corrections. In the currency markets, the US dollar depreciated against major currencies.

Central banks in the US and other affected economies have undertaken measures by injecting liquidity to stabilise inter-bank markets. Open market operations of increased size and maturity were undertaken by the Bank of England, the European Central Bank (ECB) and the US Federal Reserve System. Central bank actions have, to some extent, stabilised short-term inter-bank markets but appetite for asset-backed commercial paper (ABCP) may take some time to return.

According to IMF's assessment in October 2007[1], notwithstanding the recent volatility and the 'extremely turbulent correction', an underlying resilience in the advanced economies lay in the form of the strong balance sheets and capital positions of core financial institutions, the high profitability and generally low leverage of the corporate sector, healthy situation in labour markets and household net wealth. Emerging market economies (EMEs) have generally been less affected by turbulence in the advanced economies. The resilience of these economies reflected absence of innovative credit instruments and institutional structures prevalent in the advanced economies as well as strengthening of public balance sheets and policy frameworks, thereby reducing their external vulnerabilities. Nevertheless, financial market conditions continue to pose a major source of downside risk to the global outlook. Furthermore, although emerging markets have been less affected so far, some of them have become dependent on large external financing and may get adversely affected if a fuller re-pricing of risk and tightening of lending standards, and a general increase in risk aversion were to take place in the wake of continued turbulent conditions.

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[1] World Economic Outlook, International Monetary Fund, October 2007.

Several central banks such as the Bank of England, Bank of Canada, Reserve Bank of Australia, Reserve Bank of New Zealand, Sveriges Riksbank (Sweden), Norges Bank (Norway), People's Bank of China, Bank of Korea and South African Reserve Bank raised their policy rates further during the quarter ended September 2007 to contain inflation and stabilise inflationary expectations. Money market rates hardened further during the quarter ended September 2007 in a number of economies on account of elevated volatility in financial markets (Table 36). On the other hand, short-term interest rates in the US declined reflecting the cut in the fed funds target rate by 50 basis points to 4.75 per cent on September 18, 2007. The fed funds rate cut in the US was the first after a series of 17 consecutive rate hikes by the Federal Reserve Board from June 2004 to June 2006 followed by a pause up to August 2007. Short-term rates eased in a few EMEs such as Brazil and Thailand, as central banks in these countries continued to cut policy rates to support growth. Bangko Sentral ng Pilipinas (Philippines) lowered its key policy rates, *i.e.*, overnight borrowing rate and overnight lending rate by 25 basis points each to 5.75 per cent and 7.75 per cent, respectively, on October 4, 2007.

In contrast to money market interest rates, long-term Government bond yields softened in major advanced economies during the second quarter of 2007-08, reversing the increasing trend of the first quarter (Chart 26). Decline in bond yields reflected lower investor appetite for riskier assets in the wake of deteriorating housing market and turmoil in the credit market. Between end-June 2007 and end-September 2007, 10-year yield declined by 46 basis points in the US, 35 basis points in the UK,

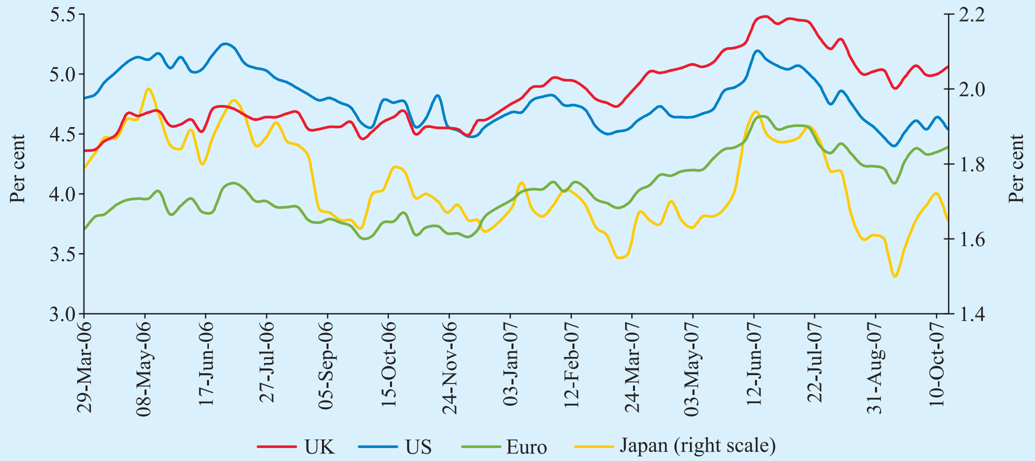
Table 36: Short-term Interest Rates

(Per cent)

Region/Country	At end of				
	March 2006	March 2007	June 2007	September 2007	October 2007*
1	2	3	4	5	6
Advanced Economies					
Euro Area	2.80	3.91	4.16	4.73	4.66
Japan	0.04	0.57	0.63	0.73	0.73
Sweden	1.99	3.21	3.42	3.54	3.74
UK	4.58	5.55	5.92	6.28	6.25
US	4.77	5.23	5.27	4.72	4.72
Emerging Market Economies					
Argentina	9.63	9.63	9.25	12.31	12.94
Brazil	16.54	12.68	11.93	11.18	11.18
China	2.40	2.86	3.08	3.86	3.87
Hong Kong	4.47	4.17	4.43	4.97	5.45
India	**6.11**	**7.98**	**7.39**	**7.19**	**7.10**
Malaysia	3.51	3.64	3.62	3.62	3.62
Philippines	7.38	5.31	6.19	6.94	6.63
Singapore	3.44	3.00	2.55	2.56	2.50
South Korea	4.26	4.94	5.03	5.34	5.34
Thailand	5.10	4.45	3.75	3.55	3.55

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

Chart 26: 10-year Government Bond Yields



21 basis points in Japan and 16 basis points in the Euro area. Between end-March 2007 and October 17, 2007, 10-year yield declined by 8 basis points in the US and 2 basis points in Japan, while these increased by 36 basis points in the Euro area and 14 basis points in the UK. Higher long-term bond yields in the UK and Euro area reflected higher short-term rates and better growth prospects.

Global equity markets recorded further gains during the second quarter of 2007-08, amidst intermittent corrections. Robust corporate earnings, buoyant merger and acquisition activity and increased risk appetite buoyed equity markets in major emerging market economies (Chart 27). However, factors such as slump in the US home sales and rising concerns about the US mortgage and corporate lending

Chart 27: Variation in International Stock Market Indices

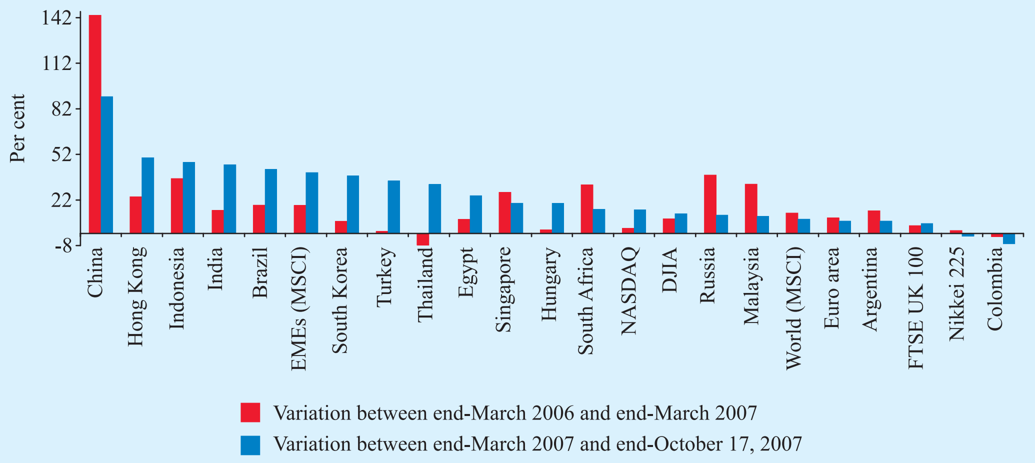


Table 37: Appreciation (+)/Depreciation (-) of the US dollar *vis-à-vis* other Currencies

(Per cent)

Currency	End-March 2006 @	End-March 07 @	October 19, 2007 *
1	2	3	4
Euro	7.1	-9.1	-6.8
Pound Sterling	8.5	-11.4	-4.4
Japanese Yen	9.4	0.2	-2.2
Chinese Yuan	-3.1	-3.4	-2.9
Russian Rubble	-0.6	-6.1	-4.5
Turkish Lira	-2.0	3.2	-13.6
Indian Rupee	2.2	-2.5	-8.7
Indonesian Rupiah	-4.3	0.5	-1.1
Malaysian Ringgit	-3.0	-6.2	-2.7
South Korean Won	-4.7	-3.7	-2.4
Thai Baht	-0.7	-9.9	-2.4
Argentine Peso	5.4	0.7	2.0
Brazilian Peso	-18.1	-6.4	-12.0
Mexican Peso	-2.6	1.3	-2.1
South African Rand	-0.5	17.2	-6.8

@ : Year-on-year variation. * : Variation over end-March 2007.

markets, increase in international crude oil prices, surge in China's inflation rate and contraction in Japan's economy affected the market sentiment intermittently. Between end-March 2007 and October 17, 2007, the MSCI World and MSCI emerging market indices increased by 9.4 per cent and 40.1 per cent, respectively. These gains in the stock markets were led by China (90.0 per cent), Hong Kong (49.8 per cent), Indonesia (46.7 per cent), India (45.3 per cent), Brazil (42.1 per cent), South Korea (37.8 per cent), Turkey (34.5 per cent) and Thailand (32.2 per cent).

In the foreign exchange market, the US dollar has depreciated against major currencies during 2007-08 so far (up to October 19, 2007), reflecting worries in the mortgage market, falling housing sales in the US and weakening consumer confidence. While the pound sterling strengthened against the US dollar and reached a 25-year high level during July 2007, Japanese yen appreciated against US dollar as a result of unwinding of Yen carry trade. Between end-March 2007 and October 19, 2007, the US dollar depreciated by 6.8 per cent against the euro, 4.4 per cent against the Pound sterling and 2.2 per cent against the yen. Amongst the Asian currencies, the US dollar depreciated by 2.9 per cent against Chinese Yuan, 2.7 per cent against the Malaysian Ringgit, 2.4 per cent against Thai Baht and 2.4 per cent against South Korean won (Table 37).

Domestic Financial Markets

Indian financial markets remained orderly for the most part of the second quarter of 2007-08. The call money rate, which had remained below the reverse repo rate during June-July 2007 on the back of the easing of liquidity conditions and prevalence of a ceiling on absorption through reverse repo operations under

Table 38: Domestic Financial Markets at a Glance

Year/ 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 3-month Forward Premia (Per cent)	Average MSS Out-standing# (Rs. crore)	Average Daily LAF Out-standing (Rs. crore)	Average Daily BSE Turnover (Rs. crore)	Average Daily NSE Turnover (Rs. crore)	Average BSE Sensex**	Average S&P CNX Nifty**
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
2004-05	**14,170**	**4.65**	**4,826**	**6.22**	**8,892**	**44.93**	**20,847 ##**	**1.66**	**46,445**	**35,592**	**2,050**	**4,506**	**5741**	**1805**
2005-06	**17,979**	**5.60**	**3,643**	**7.12**	**12,738**	**44.27**	**8,143 ##**	**1.60**	**58,792**	**10,986**	**3,248**	**6,253**	**8280**	**2513**
2006-07	**21,725**	**7.22**	**4,863**	**7.78**	**18,717**	**45.25**	**26,824 ##**	**2.14**	**37,698**	**21,973**	**3,865**	**7,812**	**12277**	**3572**
Mar 2006	18,290	6.58	2,203	7.40	17,600	44.48	8,149	3.11	29,652	-6,319	5,397	9,518	10857	3236
Apr 2006	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 2006	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
Jun 2006	17,425	5.73	2,258	7.86	15,310	46.06	0	0.73	31,845	48,610	3,130	6,567	9935	2915
Jul 2006	18,254	5.86	2,243	8.26	14,325	46.46	0	0.83	36,936	48,027	2,604	5,652	10557	3092
Aug 2006	21,294	6.06	5,786	8.09	15,934	46.54	0	1.22	40,305	36,326	2,867	5,945	11305	3306
Sep 2006	23,665	6.33	8,306	7.76	18,107	46.12	0	1.31	40,018	25,862	3,410	6,873	12036	3492
Oct 2006	26,429	6.75	4,313	7.65	16,924	45.47	0	1.67	41,537	12,983	3,481	6,919	12637	3649
Nov 2006	25,649	6.69	10,654	7.52	20,475	44.85	3,198	2.07	38,099	9,937	4,629	8,630	13434	3869
Dec 2006	24,168	8.63	5,362	7.55	19,932	44.64	1,818	3.20	38,148	-1,713	4,276	8,505	13628	3910
Jan 2007	22,360	8.18	4,822	7.71	21,171	44.33	2,830	4.22	39,553	-10,738	4,379	8,757	13984	4037
Feb 2007	23,254	7.16	4,386	7.90	20,298	44.16	11,862	3.71	40,827	648	4,675	9,483	14143	4084
Mar 2007	23,217	14.07	2,991	8.00	25,992	44.03	2,307	4.51	52,944	-11,858	3,715	7,998	12858	3731
Apr 2007	29,689	8.33	4,636	8.10	28,131 P	42.15	2,055	6.91	71,468	-8,937	3,935	8,428	13478	3947
May 2007	20,476	6.96	4,442	8.15	24,843 P	40.78	4,426	4.58	83,779	-6,397	4,706	9,885	14156	4184
Jun 2007	16,826	2.42	6,250	8.20	30,132 P	40.77	3,192	2.59	83,049	1,689	4,537	9,221	14334	4222
Jul 2007	16,581	0.73	13,273	7.94	32,254 P	40.41	11,428	1.12	82,996	2,230	5,684	12,147	15253	4474
Aug 2007	23,603	6.31	6,882	7.95	33,400 P	40.82	1,815	1.59	1,00,454	21,729	4,820	10,511	14779	4301
Sep 2007	21,991	6.41	5,859	7.92	36,557 P	40.34	–	1.45	1,17,674	16,558	6,157	13,302	16046	4660

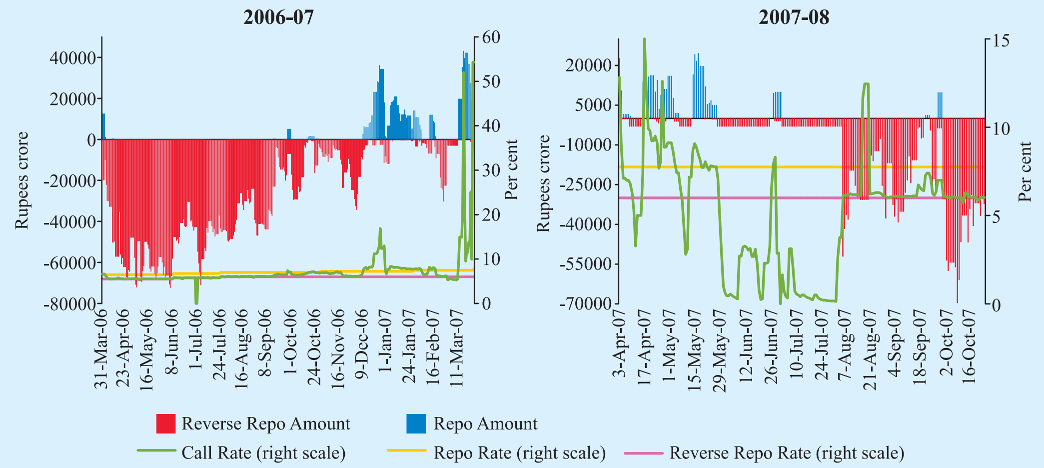
* : Average of daily weighted call money borrowing rates.
\+ : Average of daily outright turnover in Central Government dated securities.
@ : Average of daily closing rates.
\# : Average of weekly outstanding MSS.
** : Average of daily closing indices.
\## : Cumulative for the financial year.
LAF : Liquidity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

the liquidity adjustment facility (LAF), reverted to the corridor set by the reverse repo and repo rates in August-September 2007 after removal of the reverse repo ceiling. Interest rates in the collateralised segment of the overnight money market also increased in tandem and remained below the call rate during the quarter. In the foreign exchange market, the Indian rupee generally appreciated *vis-à-vis* the US dollar during the quarter. Yields in the Government securities market softened. Banks' deposit and lending rates softened during the second quarter particularly at the upper end of the range of various maturities. The stock markets remained buoyant and the benchmark indices reached record highs (Table 38). The primary market segment of the capital market witnessed increased activity in the second quarter of 2007-08.

Money Market

Money market rates eased during the first quarter of 2007-08 from their elevated levels witnessed in the second half of March 2007 (Chart 28). This trend continued in July 2007 with call money rates remaining below one per cent level for most of days and averaging 0.73 per cent for the month. In view of the prevailing

Chart 28: Liquidity Adjustment Facility and the Call Rate

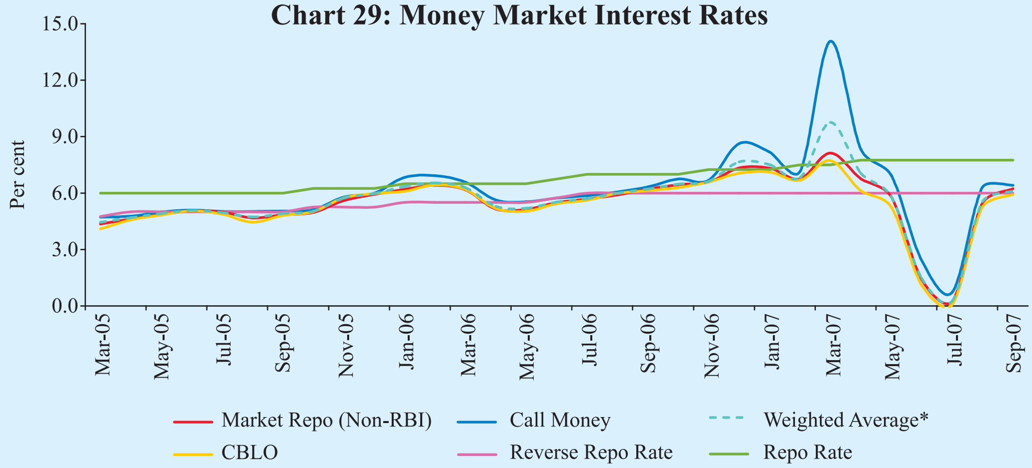


macroeconomic and overall monetary and liquidity conditions, the First Quarter Review of the Annual Statement on Monetary Policy for 2007-08 announced the withdrawal of the ceiling of Rs.3,000 crore on daily reverse repo under the LAF and the discontinuation of the Second LAF with effect from August 6, 2007. After the withdrawal of daily reverse repo ceiling, the weighted average rate in the call money market increased to 6.31 per cent during August 2007. Barring a few days in August 2007, call money rates have remained within the informal corridor set by reverse repo and repo rates. The call money rate was at 6.02 per cent on October 24, 2007.

Interest rates in the collateralised segment of the money market – market repo (outside the LAF) and collateralised borrowing and lending obligation (CBLO) – increased in line with call rates, but remained lower than the call money rate during July-September 2007 (Chart 29). During July-September 2007, interest rates averaged 4.48 per cent, 3.74 per cent and 3.98 per cent, respectively, in the call, CBLO and market repo segments (6.08 per cent, 5.91 per cent and 5.93 per cent, respectively, a year ago). The weighted average rate in all the three money market segments combined together was 3.97 per cent during July-September 2007 (5.97 per cent a year ago).

The average daily total volumes in the call, CBLO and market repo (outside the LAF) segments during July-September 2007 were 48.4 per cent higher than those in the same period of 2006. The collateralised market remained the predominant segment of the money market, accounting for about 80 per cent of the total volume during the second quarter of 2007-08 (Table 39). In both the CBLO and market repo segments, mutual funds have been the major lenders, while banks and primary dealers (PDs) have been the major borrowers.

Chart 29: Money Market Interest Rates



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

Certificates of Deposit

The outstanding amount of certificates of deposit (CDs) increased from Rs.93,272 crore at end-March 2007 (4.8 per cent of aggregate deposits of issuing banks) to Rs. 1,13,892 crore (5.9 per cent of deposits) by September 14, 2007 (Table 39). Most of the CDs issued were of 12-month duration. As on September 14, 2007, the weighted average discount rate (WADR) declined to 8.64 per cent from 9.37 per cent at end-June 2007 (10.75 per cent as at end-March 2007) in tandem with the decline in other money market rates.

Commercial Paper

Issuances of commercial paper (CP) increased in the second quarter of 2007-08. Outstanding CP rose from Rs. 17,838 crore at end-March 2007 to Rs.33,227 crore by September 15, 2007 (Table 39). The weighted average discount rate (WADR) on CP declined to 8.84 per cent as on September 15, 2007 from 8.93 per cent at end-June 2007 (11.33 per cent at end-March 2007) following easy liquidity conditions in short-term money market. The most preferred maturity of CP was for periods ranging from '61 to 90 days' and '181 days and above'. Leasing and financing companies continued to be the major issuers of CP partly reflecting the policy decision to phase out the access of these companies to public deposits (Table 40).

Treasury Bills

The primary market yields on Treasury Bills (TBs) softened in July 2007, reflecting the trends in money market segments as well as fall in domestic inflation rate (Chart 30). TBs' yields dipped on July 18, 2007, reflecting easy liquidity conditions and very low short term rates. The surplus liquidity in the

Table 39: Activity in Money Market Segments

(Rupees crore)

Year/ Month	Average Daily Volume (One Leg)					Commercial Paper		Certificates of Deposit	
	Call Money Market	Repo Market (Outside the LAF)	Collateralised Borrowing and Lending Obligation (CBLO)	Total (2+3+4)	Term Money Market	Outstanding	WADR (per cent)	Outstanding	WADR (per cent)
1	2	3	4	5	6	7	8	9	10
2004-05	**7,085**	**4,284**	**3,349**	**14,718**	**263**	**11,723**	**5.34**	**6,052**	**–**
2005-06	**8,990**	**5,296**	**10,020**	**24,306**	**417**	**17,285**	**6.46**	**27,298**	**–**
2006-07	**10,863**	**8,419**	**16,195**	**35,477**	**506**	**21,372**	**8.08**	**65,021**	**8.23**
Mar 2006	9,145	7,991	17,888	35,024	669	12,718	8.59	43,568	8.62
Apr 2006	8,455	5,479	16,329	30,263	447	16,550	7.30	44,059	7.03
May 2006	9,037	9,027	17,147	35,211	473	17,067	6.89	50,228	7.17
Jun 2006	8,713	10,563	13,809	33,085	628	19,650	7.10	56,390	7.19
Jul 2006	9,127	9,671	15,670	34,468	432	21,110	7.34	59,167	7.65
Aug 2006	10,647	7,764	15,589	34,000	510	23,299	7.31	65,621	7.77
Sep 2006	11,833	9,185	14,771	35,789	568	24,444	7.70	65,274	7.80
Oct 2006	13,214	9,721	16,964	39,899	466	23,171	7.77	65,764	7.73
Nov 2006	12,825	9,374	16,069	38,268	348	24,238	7.88	68,911	7.99
Dec 2006	12,084	7,170	15,512	34,766	481	23,536	8.52	68,619	8.28
Jan 2007	11,180	6,591	15,758	33,529	515	24,398	9.09	70,149	9.22
Feb 2007	11,627	7,794	19,063	38,484	467	21,167	10.49	72,795	9.87
Mar 2007	11,608	8,687	17,662	37,957	739	17,838	11.33	93,272	10.75
Apr 2007	14,845	7,173	18,086	40,104	440	18,759	10.52	95,980	10.75
May 2007	10,238	8,965	20,810	40,013	277	22,024	9.87	99,715	9.87
Jun 2007	8,413	10,295	20,742	39,450	308	26,256	8.93	98,337	9.37
Jul 2007	8,290	12,322	20,768	41,380	288	30,631	7.05	1,05,317	7.86
Aug 2007	11,802	16,688	26,890	55,380	319	31,527	8.30	1,09,224	8.67
Sep 2007	10,995	17,876	29,044	57,915	265	33,227*	8.84*	1,13,892+	8.64+

* : As on September 15, 2007. + : As on September 14, 2007. – : Not available.
WADR : Weighted Average Discount Rate.

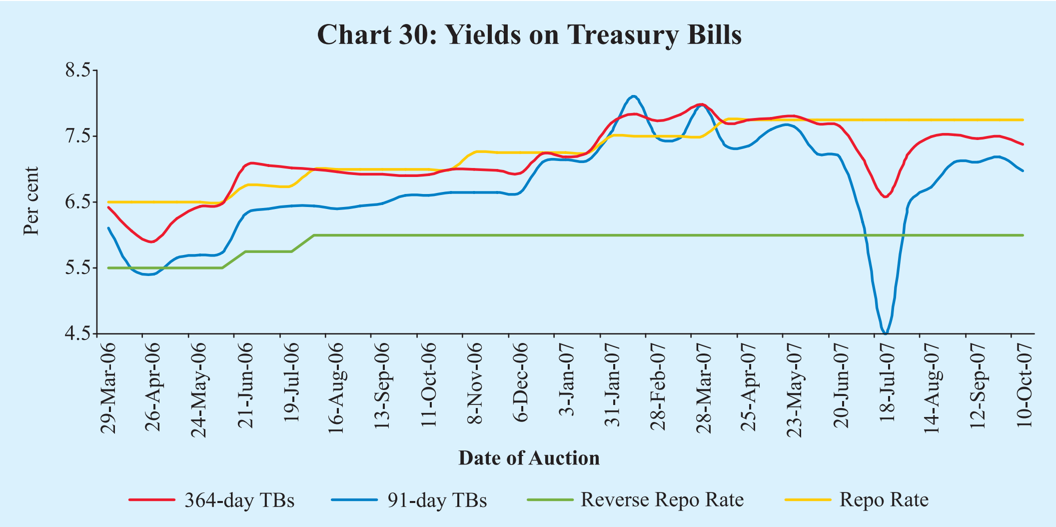
wake of ceiling of Rs. 3,000 crore in LAF reverse repo resulted in extremely low short-term rates and aggressive bidding in auctions of TBs and hence the lower auction cut-off. TBs' yields hardened during August-September 2007 in tandem with higher money market interest rates and removal of the ceiling on absorption

Table 40: Commercial Paper – Major Issuers

(Rupees crore)

Category of Issuer	End of			
	March 2006	March 2007	June 2007	September 2007*
1	2	3	4	5
Leasing and Finance	9,400 (73.9)	12,569 (70.5)	18,260 (69.5)	24,191 (72.8)
Manufacturing	1,982 (15.6)	2,754 (15.4)	3,956 (15.1)	6,006 (18.1)
Financial Institutions	1,336 (10.5)	2,515 (14.1)	4,040 (15.4)	3,030 (9.1)
Total	**12,718** **(100.0)**	**17,838** **(100.0)**	**26,256** **(100.00)**	**33,227** **(100.00)**

* : As on September 15, 2007.
Note : Figures in parentheses are percentage shares in the total outstanding.



through reverse repo. The yield spread between 364-day and 91-day TBs widened to 40 basis points in September 2007 from 26 basis points in June 2007 (17 basis points in March 2007) (Table 41).

Table 41: Treasury Bills in the Primary Market

Month	Notified Amount (Rupees crore)	Average Implicit Yield at Minimum Cut-off Price (Per cent)			Average Bid-Cover Ratio		
		91-day	182-day	364-day	91-day	182-day	364-day
1	2	3	4	5	6	7	8
2004-05	**1,38,500 @**	**4.91**	**–**	**5.16**	**2.43**	**–**	**2.52**
2005-06	**1,55,500 @**	**5.68**	**5.82**	**5.96**	**2.64**	**2.65**	**2.45**
2006-07	**1,86,500 @**	**6.64**	**6.91**	**7.01**	**1.97**	**2.00**	**2.66**
Mar 2006	6,500	6.51	6.66	6.66	4.17	3.43	3.36
Apr 2006	5,000	5.52	5.87	5.98	5.57	4.96	2.02
May 2006	18,500	5.70	6.07	6.34	1.88	1.84	1.69
Jun 2006	15,000	6.15	6.64	6.77	1.63	1.35	2.11
Jul 2006	16,500	6.42	6.75	7.03	1.82	1.55	3.12
Aug 2006	19,000	6.41	6.70	6.96	2.03	2.71	3.48
Sep 2006	15,000	6.51	6.76	6.91	1.35	1.80	2.92
Oct 2006	15,000	6.63	6.84	6.95	1.31	1.20	2.02
Nov 2006	18,500	6.65	6.92	6.99	1.33	1.22	2.49
Dec 2006	15,000	7.01	7.27	7.09	1.19	1.29	3.34
Jan 2007	19,000	7.28	7.45	7.39	1.02	1.35	1.74
Feb 2007	15,000	7.72	7.67	7.79	2.48	2.56	3.16
Mar 2007	15,000	7.73	7.98	7.90	2.08	2.15	3.87
Apr 2007	15,000	7.53	7.87	7.72	2.87	3.36	3.16
May 2007	18,500	7.59	7.70	7.79	2.33	2.57	2.33
Jun 2007	35,000	7.41	7.76	7.67	3.23	4.11	3.97
Jul 2007	12,500	5.07	5.94	6.87	4.48	2.70	4.56
Aug 2007	20,500	6.74	7.37	7.42	2.11	1.41	2.46
Sep 2007	25,000	7.08	7.33	7.48	2.07	2.91	2.83

@ : 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).

Foreign Exchange Market

During the second quarter of 2007-08, the Indian rupee generally appreciated *vis-à-vis* the US dollar (Chart 31). Between end-March 2007 and October 24, 2007, the rupee moved in the range of Rs.39.31-43.15 per US dollar. The rupee, which had appreciated till end of May 2007, depreciated thereafter up to the last week of June 2007. The rupee, however, appreciated again from the first week of July 2007 and reached a level of Rs. 39.31 per US dollar on October 15, 2007 from its level of Rs. 43.60 per US dollar at end-March 2007. The rupee's appreciation reflected, *inter alia*, large capital inflows and weakening of US dollar overseas against all the major currencies. The exchange rate of the rupee was Rs. 39.58 per US dollar as on October 24, 2007. At this level, the Indian rupee appreciated by 10.1 per cent *vis-à-vis* the US dollar over its level on March 31, 2007. Over the same period, the rupee appreciated by 5.6 per cent against the Pound sterling, 3.1 per cent against the Euro and 7.2 per cent against the Japanese yen.

The six-currency nominal effective exchange rate (NEER) and real effective exchange rate (REER) of the Indian rupee, on an average basis, appreciated by 6.3 per cent and 7.1 per cent, respectively, between March 2007 and September 2007. The six-currency NEER and REER appreciated further by 1.1 per cent and 1.3 per cent, respectively, between end-September 2007 and October 15, 2007. The 36-currency NEER and REER of the Indian rupee, on an average basis,

Chart 31: Movement of Rupee *vis-a-vis* Major Currencies

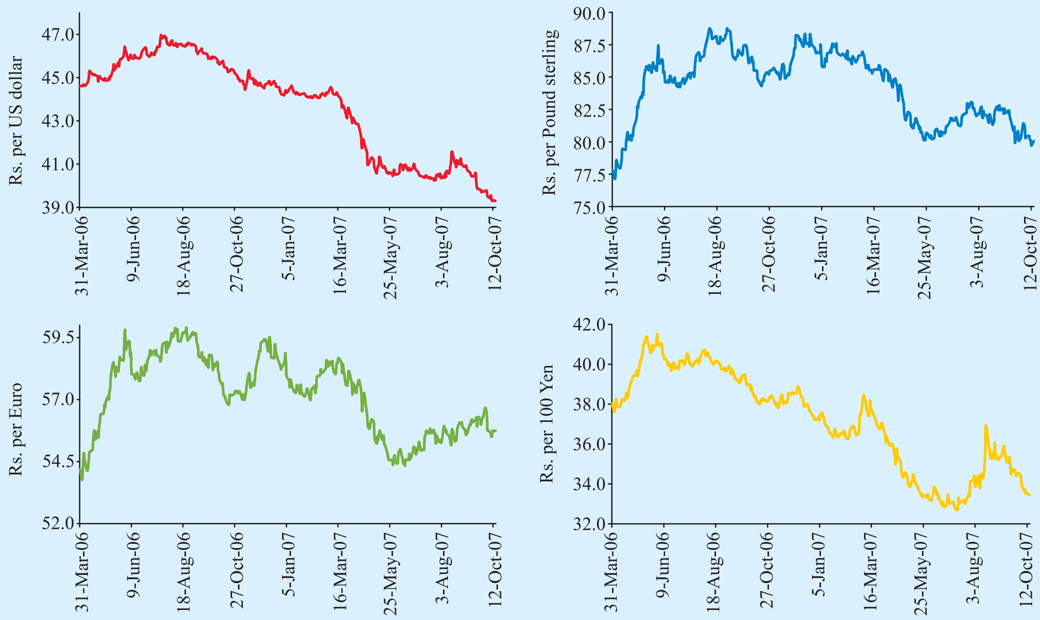


Table 42: Nominal and Real Effective Exchange Rate of the Indian Rupee (Trade-Based Weights)

Base : 1993-94 (April-March) = 100

Year/Month	6-Currency Weights		36-Currency Weights	
	NEER	REER	NEER	REER
1	2	3	4	5
1993-94	100.00	100.00	100.00	100.00
2000-01	77.43	102.82	92.12	100.09
2001-02	76.04	102.71	91.58	100.86
2002-03	71.27	97.68	89.12	98.18
2003-04	69.97	99.17	87.14	99.56
2004-05	69.58	101.78	87.31	100.09
2005-06	72.28	107.30	89.85	102.35
2006-07 (P)	68.93	105.47	85.88	98.50
Mar 2006	72.45	107.41	89.52	101.25
Apr 2006	71.04	105.75	87.73	98.22
May 2006	68.79	103.48	85.43	96.44
Jun 2006	68.21	103.06	85.11	96.57
Jul 2006	67.59	102.25	84.22	95.72
Aug 2006	67.08	102.14	83.61	95.61
Sep 2006	67.84	104.75	84.65	97.98
Oct 2006	69.11	107.25	86.18	99.94
Nov 2006	69.34	107.82	86.50	100.31
Dec 2006	68.82	106.39	85.89	99.16
Jan 2007 (P)	69.77	107.70	87.05	100.74
Feb 2007 (P)	69.88	107.71	87.13	100.63
Mar 2007 (P)	69.70	107.41	87.11	100.74
Apr 2007 (P)	72.18	111.59	91.50	103.79
May 2007 (P)	74.64	115.67	94.38	107.21
Jun 2007 (P)	74.83	115.28	93.24	107.37
Jul 2007 (P)	74.62	114.95	93.06	107.70
Aug 2007 (P)	73.91	114.10	–	–
Sep 2007 (P)	74.11	115.08	–	–
October 15, 2007	75.53	117.54	–	–

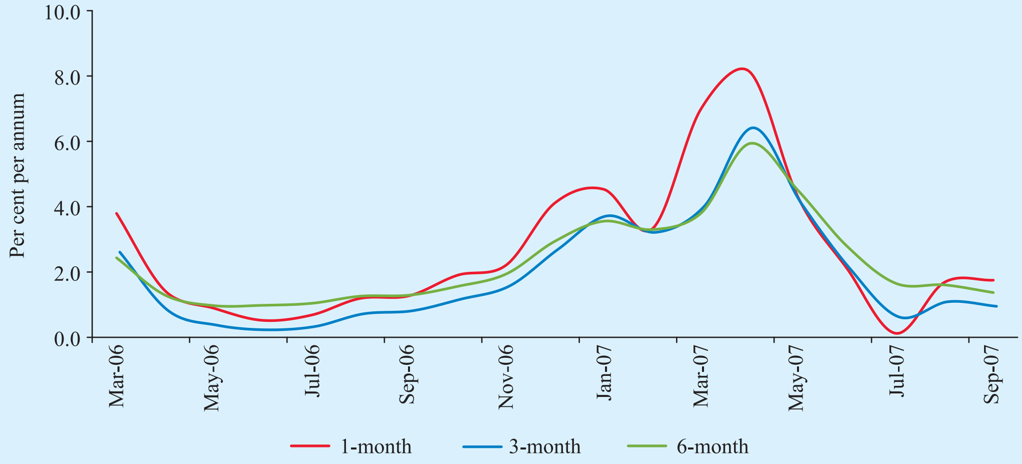
NEER : Nominal Effective Exchange Rate. REER : Real Effective Exchange Rate.
P : Provisional. – : Not available.
Note : Rise in indices indicates appreciation of the rupee and *vice versa*.

appreciated by 6.8 per cent and 6.9 per cent, respectively, between March 2007 and July 2007 (Table 42).

Forward premia increased during the second quarter of 2007-08, after dipping in July 2007, in tandem with the domestic overnight interest rates (Chart 32). The forward premia, however, remained lower than their end-March 2007 and end-June 2007 levels. The one-month forward premia declined from 6.99 per cent in March 2007 to 1.75 per cent in September 2007, while the six-month forward premia declined from 3.80 per cent to 1.37 per cent over the same period.

The average daily turnover in the foreign exchange market increased to US $ 43.8 billion during April-September 2007 from US $ 23.0 billion in the

Chart 32: Movement in Forward Premia



corresponding period of 2006. While the average inter-bank turnover increased to US $ 30.9 billion from US $ 16.6 billion, the average merchant turnover increased to US $ 13.0 billion from US $ 6.4 billion (Chart 33). The ratio of inter-bank to merchant turnover was 2.5 during April-September 2007 as compared with 2.6 a year ago.

Credit Market

Deposit rates of scheduled commercial banks (SCBs) softened somewhat, particularly at the upper end of the range for various maturities during the second quarter of 2007-08. Interest rates of public sector banks (PSBs) on

Chart 33: Turnover in Foreign Exchange Market

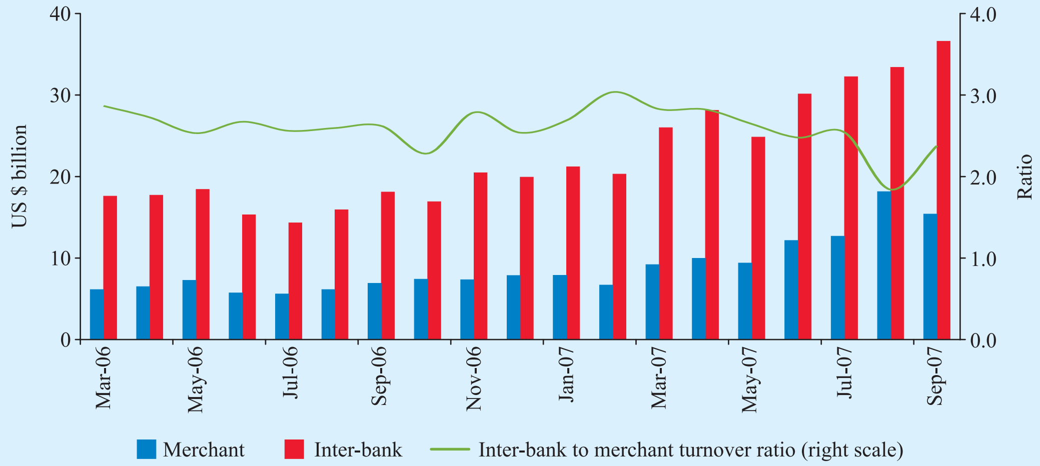


Table 43: Deposit and Lending Rates

(Per cent)

Interest Rate	March 2006	March 2007	June 2007	September 2007	October 2007 @
1	2	3	4	5	6
1. Domestic Deposit Rate					
Public Sector Banks					
Up to 1 year	2.25-6.50	2.75-8.75	2.75-8.75	2.75-8.50	2.75-8.50
More than 1 year and up to 3 years	5.75-6.75	7.25-9.50	7.25-9.75	8.00-9.00	8.00-9.00
More than 3 years	6.00-7.25	7.50-9.50	7.75-9.75	8.00-9.50	8.00-9.50
Private Sector Banks					
Up to 1 year	3.50-7.25	3.00-9.00	3.00-9.50	2.50-9.25	2.50-9.25
More than 1 year and up to 3 years	5.50-7.75	6.75-9.75	6.75-10.25	6.25-10.00	6.25-9.60
More than 3 years	6.00-7.75	7.75-9.60	7.50-10.00	7.25-10.00	7.25-10.00
Foreign Banks					
Up to 1 year	3.00-6.15	3.00-9.50	0.25-9.00	2.00-9.00	2.00-9.00
More than 1 year and up to 3 years	4.00-6.50	3.50-9.50	3.50-9.50	2.00-9.50	2.00-9.50
More than 3 years	5.50-6.50	4.05-9.50	4.05-9.50	2.00-9.50	2.00-9.50
2. Benchmark Prime Lending Rate					
Public Sector Banks	10.25-11.25	12.25-12.75	12.50-13.50	12.50-13.50	12.50-13.50
Private Sector Banks	11.00-14.00	12.00-16.50	13.00-17.25	13.00-16.50	13.00-16.50
Foreign Banks	10.00-14.50	10.00-15.50	10.00-15.50	10.00-15.50	10.00-15.50
3. Actual Lending Rate*					
Public Sector Banks	4.00-16.50	4.00-17.00	4.00-17.75	–	–
Private Sector Banks	3.15-20.50	3.15-25.50	4.00-26.00	–	–
Foreign Banks	4.75-26.00	5.00-26.50	2.98-28.00	–	–

– : Not available. @ : As on October 19, 2007.

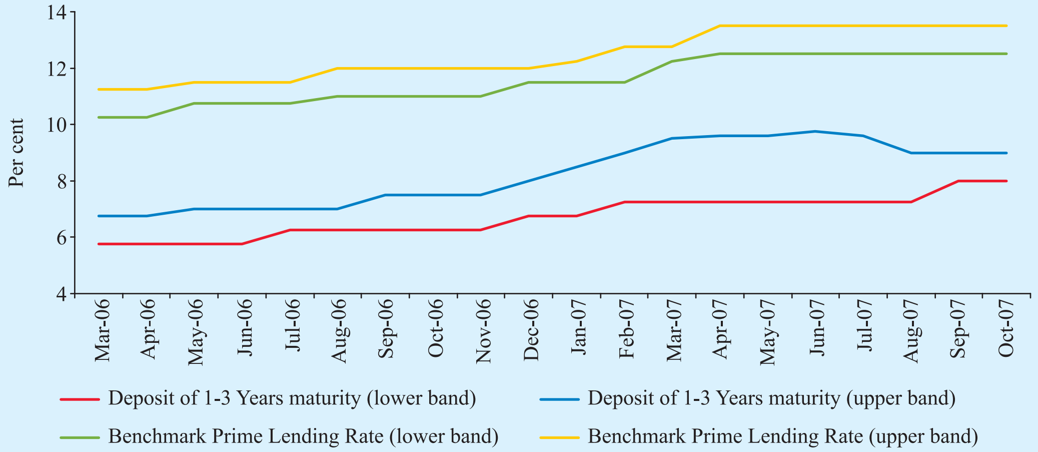
* : Interest rate on non-export demand and term loans above Rs.2 lakh excluding lending rates at the extreme five per cent on both sides.

deposits of maturity of one year to three years were placed in the range of 8.00-9.00 per cent by mid-October 2007 as compared with 7.25-9.75 per cent in June 2007 (7.25-9.50 per cent in March 2007), while those on deposits of maturity of above three years were placed in the range of 8.00-9.50 per cent by mid-October 2007 as compared with 7.75-9.75 per cent in June 2007 (7.50-9.50 per cent in March 2007).

Benchmark Prime Lending Rates (BPLRs) of private sector banks softened to the range of 13.00-16.50 per cent by mid-October 2007 from 13.00-17.25 per cent in June 2007. The range of BPLRs of PSBs and foreign banks, however, remained unchanged during this period (Table 43 and Chart 34).

The weighted average BPLR of public sector banks increased from 12.43 per cent in March 2007 to 13.07 per cent in June 2007 and remained unchanged in October 2007. The weighted average BPLR of private sector banks increased from 14.34 per cent in March 2007 to 15.12 per cent in June 2007, but marginally softened to 15.08 per cent in October 2007. The weighted average BPLR of foreign banks increased from 12.63 per cent in March 2007 to 13.83 per cent in June 2007 and further to 14.07 per cent in October 2007.

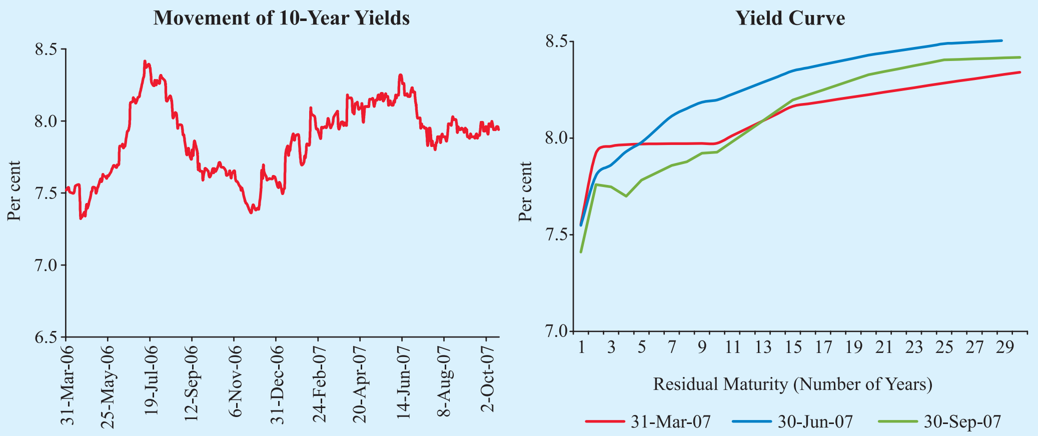
Chart 34: Deposit and Lending Rates - Public Sector Banks

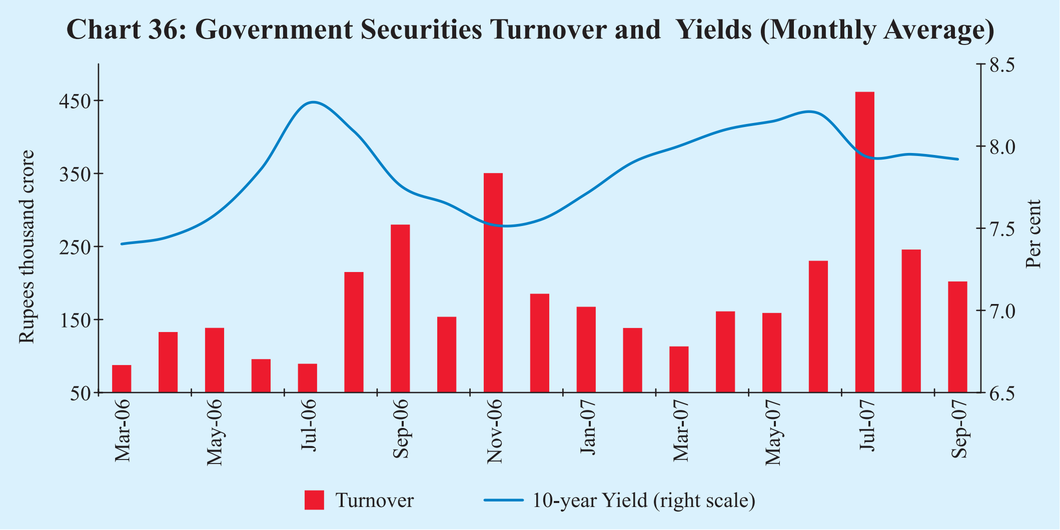


Government Securities Market

Yields in the Government securities market softened during the second quarter of 2007-08, partly reflecting global trends in yields, lower inflation and comfortable liquidity conditions (Chart 35). The 10-year yield moved in a range of 7.80-8.32 per cent during 2007-08 (up to October 24, 2007). As on October 24, 2007, the yield was 7.89 per cent, 8 basis points lower than that at end-March 2007. The spread between 1-10 year yields was 52 basis points at end-September 2007 as compared with 65 basis points at end-June 2007 (42 basis points at end-March 2007). The spread between 10-year and 30-year yields was 49 basis points at end-September 2007 as compared with 31 basis points at end-June 2007 (37 basis points at end-March 2007).

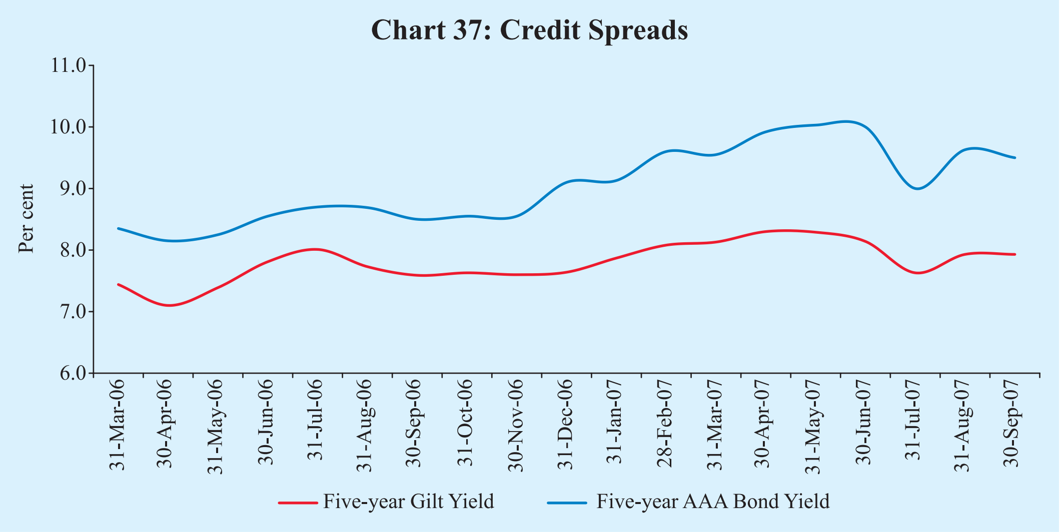
Chart 35: Yields on Central Government Securities





The turnover in the Government securities market almost doubled in July 2007 from its level in June 2007 on account of low funding cost at the shorter-end, but reverted in August-September 2007 as overnight rates rose to the corridor set by the reverse repo and repo rates (Chart 36).

The yield on 5-year AAA-rated corporate bonds softened during the second quarter of 2007-08 in tandem with lower Government securities yield. The credit spread between the yields on 5-year AAA-rated bonds and 5-year Government securities narrowed to 157 basis points at end-September 2007 from 186 basis points at end-June 2007 (142 basis points at end-March 2007) (Chart 37).



Equity Market

Primary Market

Resources raised through public issues at Rs.31,854 crore increased by 149.4 per cent during April-September 2007 over the corresponding period of 2006. The number of issues also increased from 50 to 60 (Table 44). Most of the resources raised were, however, during June-2007 (Rs.22,688 crore out of Rs.31,854 crore), due to two large issues. The average size of public issues increased from Rs.255 crore during April-September 2006 to Rs.531 crore during April-September 2007. All the public issues during April-September 2007 were in the form of equity except one

Table 44: Mobilisation of Resources from the Primary Market

(Amount in Rupees crore)

Item	2006-07 (April-September)		2007-08 (April-September) P	
	No. of Issues	Amount	No. of Issues	Amount
1	2	3	4	5
A. Prospectus and Rights Issues*				
1. Private Sector (a+b)	**50**	**12,770**	**57**	**28,521**
a) Financial	3	261	5	11,021
b) Non-financial	47	12,509	52	17,500
2. Public Sector (a+b+c)	**–**	**–**	**3**	**3,333**
a) Public Sector Undertakings	–	–	–	–
b) Government Companies	–	–	2	2,517
c) Banks/Financial Institutions	–	–	1	816
3. Total (1+2)	**50**	**12,770**	**60**	**31,854**
of which:				
(i) Equity	50	12,770	59	31,354
(ii) Debt	–	–	1	500
	2006-07 (April-June)		2007-08 (April-June)	
B. Private Placement				
1. Private Sector	**312**	**15,315**	**428**	**30,872**
a) Financial	113	7,963	195	13,728
b) Non-financial	199	7,352	233	17,144
2. Public Sector	**22**	**15,813**	**20**	**19,002**
a) Financial	20	14,118	14	11,971
b) Non-financial	2	1,695	6	7,031
3. Total (1+2)	**334**	**31,128**	**448**	**49,874**
of which:				
(i) Equity	–	–	–	–
(ii) Debt	334	31,128	448	49,874
Memo:				
C. Euro Issues (Apr-Sep)	**29**	**7,916**	**10**	**11,284**

P : Provisional.
* : Excluding offers for sale. – : Nil/Negligible.

issue. Out of 60 issues during April-September 2007, 46 issues were initial public offerings (IPOs), constituting 62.3 per cent of total resource mobilisation.

Mobilisation of resources through private placement increased by 60.2 per cent to Rs.49,874 crore during April-June 2007 as compared with an increase of 48.4 per cent during April-June 2006 (see Table 44). Public sector entities accounted for 38.1 per cent of total mobilisation during April-June 2007, lower than the corresponding period of the previous year (50.8 per cent). Resource mobilisation through financial intermediaries (both from public sector and private sector) registered a growth of 16.4 per cent over the corresponding period of last year, accounting for 51.5 per cent of total mobilisation during April-June 2007. Resources raised by non-financial intermediaries registered a higher growth of 167.2 per cent (48.5 per cent of total resource mobilisation) during April-June 2007 over the corresponding period of last year.

During April-September 2007, resources raised through Euro issues – American Depository Receipts (ADRs) and Global Depository Receipts (GDRs) – by Indian corporates increased sharply by 42.5 per cent to Rs.11,284 crore (see Table 44).

During April-September 2007, net mobilisation of funds by mutual funds increased by 75.9 per cent to Rs.1,05,614 crore (Table 45). Inflows in private sector mutual funds increased by 107.0 per cent over the corresponding period of last year. Net inflows were witnessed in both income/debt-oriented schemes and growth/equity-oriented schemes.

Secondary Market

The domestic stock markets recorded further gains during the second quarter of 2007-08 amidst intermittent corrections (Chart 38). Liquidity support from foreign institutional investors (FIIs) on the back of strong GDP growth, robust

Table 45: Resource Mobilisation by Mutual Funds

(Rupees crore)

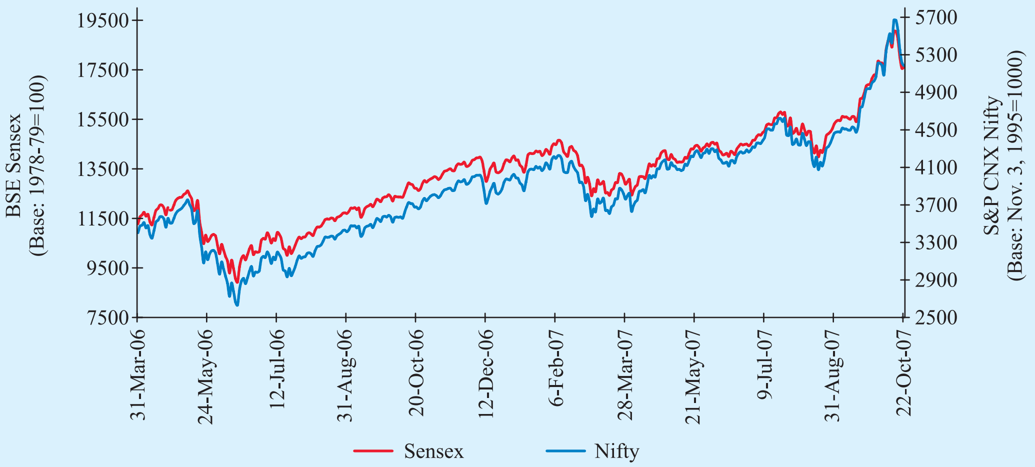
Mutual Fund	April-March		April-September			
	2006-07		2006-07		2007-08	
	Net Mobilisation @	Net Assets #	Net Mobilisation @	Net Assets #	Net Mobilisation @	Net Assets #
1	2	3	4	5	6	7
Private Sector	79,038	2,62,079	46,311	2,28,254	95,845	3,93,431
Public Sector *	14,947	64,213	13,737	62,953	9,769	83,558
Total	**93,985**	**3,26,292**	**60,048**	**2,91,207**	**1,05,614**	**4,76,989**

@ : Net of redemptions. #: End-period. * : Including UTI Mutual fund.

Note : Data exclude funds mobilised under Fund of Funds Schemes.

Source : Securities and Exchange Board of India.

Chart 38: Indian Stock Markets

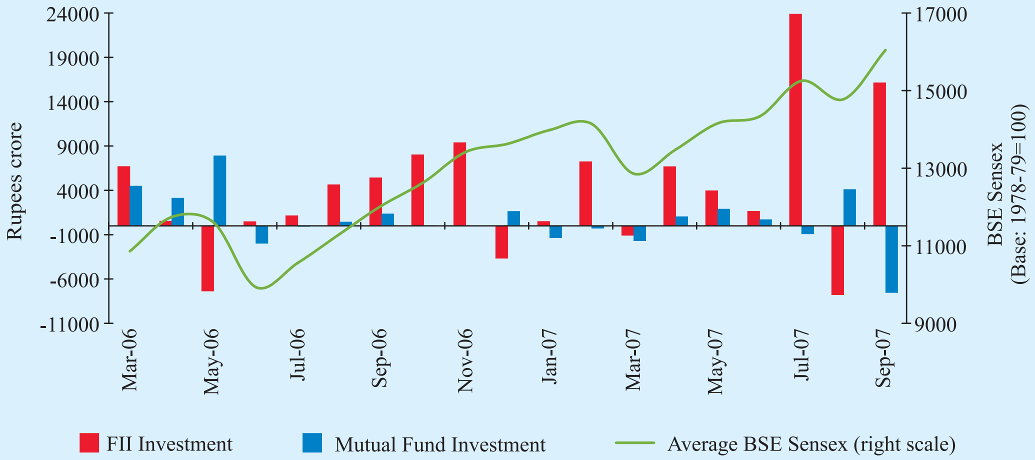


corporate profitability, decline in domestic inflation rate and upward trend in major international equity markets provided support to the domestic stock markets. However, slump in the US home sales and rising concerns over the US sub-prime mortgage and corporate lending markets, increase in global crude oil prices to record high levels, political uncertainty in the wake of the Indo-US nuclear deal and deceleration in India's industrial production during the month of July 2007 depressed the markets intermittently.

Between end-March 2007 and end-September 2007, the BSE Sensex moved in a range of 12455-17291. The BSE Sensex closed at a record high of 19059 on October 15, 2007, an increase of 45.8 per cent over end-March 2007. The S&P CNX Nifty also reached a record high of 5670 on October 15, 2007. However, key indices slipped from their record levels after the Securities and Exchange Board of India (SEBI) proposed to restrict investments through offshore derivative instruments/participatory notes on October 16, 2007 leading to large sales by FIIs. Subsequently, on allaying concerns of overseas investors by the SEBI and assuring them speeding up the process of registration as FIIs, the BSE Sensex recorded biggest ever single day gain of 879 points on October 23, 2007. The BSE Sensex closed at 18513 on October 24, 2007.

According to the data released by the SEBI, FIIs have invested Rs.62,139 crore (US $ 15.1 billion) in the Indian stock markets during 2007-08 so far (up to October 19, 2007) as compared with net purchases of Rs.10,231 crore (US $ 2.2 billion) during the corresponding period of the previous year (Chart 39). Mutual funds have made net investments of Rs. 2,595 crore during 2007-08 so far (up to October 19, 2007) as compared with net investments of Rs.10,344 crore during the corresponding period of the last year.

Chart 39: Institutional Investment and Stock Market



The major gainers in the domestic stock markets during the current financial year so far (up to October 19, 2007) were metal followed by capital goods, oil and gas, public sector undertaking, banking, consumer durables, fast moving consumer goods, auto and healthcare sector stocks (Table 46).

Reflecting the upward trend in stock prices, the price-earnings (P/E) ratios of the 30 scrips included in the BSE Sensex rose from 20.3 at end-March 2007 to 23.3 by end-September 2007 (Table 47). The market capitalisation of the BSE increased by 46.7 per cent between end-March 2007 and end-September 2007. The volatility in the stock markets declined during April-September 2007. The combined turnover of BSE and NSE in the cash and derivatives segments during

Table 46: BSE Sectoral Stock Indices

(Base: 1978-79=100)

Sector	Variation (per cent)		
	End-March 2006 @	End-March 2007 @	October 19, 2007 #
1	2	3	4
Fast Moving Consumer Goods	109.9	-21.4	16.2
Public Sector Undertakings	44.0	-3.2	38.7
Information Technology	49.2	21.6	-4.4
Auto	101.2	-8.5	8.8
Oil and Gas	61.1	30.5	59.6
Metal	40.3	-4.3	70.6
Health Care	51.2	-5.4	1.8
Bankex	36.8	24.2	35.1
Capital Goods	156.0	11.1	70.0
Consumer Durables	115.4	11.1	33.8
BSE 500	65.2	9.7	37.4
BSE Sensex	73.7	15.9	34.3

@ : Year-on-year variation. # : Variation over end-March 2007.
Source : Bombay Stock Exchange Limited.

April-September 2007 was higher by 43.2 per cent and 51.5 per cent, respectively, over the corresponding period of 2006.

Table 47: Stock Market Indicators

Indicator	BSE				NSE			
	2005-06	2006-07	April-September		2005-06	2006-07	April-September	
			2006	2007			2006	2007
1	2	3	4	5	6	7	8	9
1. BSE Sensex / S&P CNX Nifty								
(i) End-period	11280	13072	12454	17291	3403	3822	3588	5021
(ii) Average	8280	12277	11167	14679	2513	3572	3280	4300
2. Coefficient of Variation	16.7	11.1	7.7	6.2	15.6	10.4	7.8	5.9
3. Price-Earning Ratio (end-period)*	20.9	20.3	21.3	23.3	20.3	18.4	20.9	22.6
4. Price-Book Value Ratio*	5.1	5.1	4.6	5.5	5.2	4.9	4.8	5.4
5. Yield* (per cent per annum)	1.2	1.3	1.4	1.0	1.3	1.3	1.3	1.1
6. Listed Companies	4,781	4,821	4,785	4,871	1,069	1,228	1,116	1,319
7. Cash Segment Turnover (Rupees crore)	8,16,074	9,56,185	4,44,731	6,27,022	15,69,556	19,45,285	9,23,664	13,34,318
8. Derivative Segment Turnover (Rupees crore)	9	59,007	379	1,12,316	48,24,174	73,56,242	35,06,882	52,90,968
9. Market Capitalisation (Rupees crore) @	30,22,191	35,45,041	31,85,680	52,02,955	28,13,201	33,67,350	29,94,132	48,86,561

* : Based on 30 scrips included in the BSE Sensex and 50 scrips included in the S&P CNX Nifty. @: End period.

Source : Bombay Stock Exchange Ltd. (BSE) and National Stock Exchange of India Ltd. (NSE).

VI. THE EXTERNAL ECONOMY

India's balance of payments position has remained comfortable during 2007-08 so far. Merchandise exports after registering robust growth in 2006-07, witnessed some moderation during April-August 2007. Cumulative imports during April-August 2007 posted a high growth rate; oil imports, however, witnessed a sharp deceleration from the strong growth recorded during the corresponding period of the previous year. Net invisibles surplus remained buoyant during the first quarter of 2007-08, led by higher growth in private transfers. The surplus on the invisibles account contained the current account deficit at broadly the same level as in the first quarter of 2006-07. Net capital inflows were substantially higher than those in the corresponding period of 2006-07, reflecting large flows under portfolio investment and external commercial borrowings. Foreign exchange reserves increased further by US $ 62.0 billion during 2007-08 (up to October 19, 2007).

International Developments

The global economy sustained strong growth of above 5 per cent during the first half of 2007. Growth in the US economy, however, moderated during this period, as the housing correction continued to apply considerable drag. While private consumption growth slowed markedly in the US in the face of rising gasoline prices, net external demand provided a significant boost to growth – exports benefited from strong partner country growth combined with the weakening dollar, while imports weakened in line with slower household spending. Growth in the Euro area, Japan and OECD countries slowed in the second quarter after two quarters of high growth (Table 48). The slowdown in the Japanese economy during the second quarter was largely driven by decline in public and residential investment and weaker consumption growth. The Chinese economy, on the other hand, gained further momentum growing by 11.5 per cent during the first half of 2007. India and Russia also continued to grow at a rapid pace. These three countries alone have accounted for one half of global growth over the past year. China for the first time has become the largest contributor to the world growth both in terms of market as well PPP based exchange rates. According to the International Monetary Fund (IMF), India is projected to record 8.9 per cent growth in 2007. Developing Asia is projected to grow by 9.8 per cent in 2007 and 8.8 per cent in 2008.

The current global expansion has been the strongest period of growth since the early 1970s and it is also remarkable in other dimensions. First, with the rapid growth of world trade, openness (exports *plus* imports as proportion to GDP) has risen by over 10 percentage points since 2001, while financial openness (capital inflows *plus* outflows as proportion to GDP) has also risen rapidly. Second,

Table 48: Growth Rates – Global Scenario

(Per cent)

Region/Country	2004	2005	2006	2007 P	2008 P	2006				2007	
						Q1	Q2	Q3	Q4	Q1	Q2
1	2	3	4	5	6	7	8	9	10	11	12
Advanced Economies											
Euro area	2.0	1.5	2.8	2.5	2.1	2.2	2.7	2.8	3.3	3.0	2.5
Japan	2.7	1.9	2.2	2.0	1.7	3.0	2.1	1.4	2.2	2.6	1.6
Korea	4.7	4.2	5.0	4.8	4.6	6.3	5.1	4.8	4.0	4.0	5.0
UK	3.3	1.8	2.8	3.1	2.3	2.4	2.7	2.9	3.0	3.0	3.1
US	3.6	3.1	2.9	1.9	1.9	3.3	3.2	2.4	2.6	1.5	1.9
OECD Countries	3.1	2.5	2.9	2.7	2.7	3.2	3.3	2.8	3.1	2.6	2.5
Emerging Economies											
Argentina	9.0	9.2	8.5	7.5	5.5	8.6	7.9	8.7	8.6	8.0	8.7
Brazil	5.7	2.9	3.7	4.4	4.0	3.9	1.1	4.4	4.4	4.3	5.4
China	10.1	10.4	11.1	11.5	10.0	10.3	10.9	10.7	10.7	11.1	11.5
India	7.5	9.0	9.4	8.9	8.4	10.0	9.6	10.2	8.7	9.1	9.3
Indonesia	5.0	5.7	5.5	6.2	6.1	5.0	5.0	5.9	6.1	6.0	6.3
Malaysia	7.2	5.2	5.9	5.8	5.6	6.0	6.1	6.0	5.7	5.3	5.7
Thailand	6.3	4.5	5.0	4.0	4.5	6.1	5.0	4.7	4.3	4.3	4.4

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.

emerging market and developing countries now account for a high share of growth – over two-thirds compared to around half in the 1990s. Third, the growth process has been widespread across countries and regions rather than being driven by only a few dynamic countries. These countries/regions are doing well by their own past standards as reflected in the decline in the dispersion of growth rates relative to trend. Fourth, the volatility of growth has declined substantially.

According to the projections released by the IMF in October 2007, growth in the world economy is likely to moderate to 5.2 per cent in 2007 and 4.8 per cent in 2008 from 5.4 per cent in 2006 (Table 49). The downside risks to the global outlook have increased considerably on account of tightening of credit conditions resulting from reduced risk appetite and less optimistic prospects for a turnaround in the US housing market. The cutback in residential construction is reported to have directly reduced the annual rate of US economic growth by about 0.75 per cent on an average over the past year and half. In case the current conditions persist in mortgage markets, the demand for homes could weaken further, with possible implications for the broader economy. However, at the present juncture, the broad assessment by the IMF is that sound fundamentals and the strong momentum of the emerging market economies will continue to support the solid growth. The extent of the impact on growth will depend on how quickly more normal market liquidity is restored and the extent of the retrenchment in credit market.

According to the IMF, growth in world trade is expected to moderate to 6.6 per cent in volume terms in 2007 from 9.2 per cent in the preceding year (Table 49). Exports of other emerging market and developing countries are projected to grow by 9.2 per cent in 2007 (11.0 per cent a year ago), while those of advanced countries are expected to grow by 5.4 per cent (8.2 per cent a year ago).

Table 49: 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	4.8	5.4	5.2	4.8
	(1.5)	(1.9)	(2.6)	(3.9)	(3.3)	(3.8)	(3.5)	(3.3)
i) Advanced economies	1.2	1.6	1.9	3.2	2.5	2.9	2.5	2.2
ii) Other emerging market and developing countries	4.3	5.1	6.7	7.7	7.5	8.1	8.1	7.4
of which: Developing Asia	6.0	7.0	8.3	8.8	9.2	9.8	9.8	8.8
II. Consumer Price Inflation (Per cent)								
i) Advanced economies	2.1	1.5	1.8	2.0	2.3	2.3	2.1	2.0
ii) Other emerging market and developing countries	6.5	5.7	5.7	5.4	5.2	5.1	5.9	5.3
of which: Developing Asia	2.7	2.0	2.5	4.1	3.6	4.0	5.3	4.4
III. Net Capital Flows* (US $ billion)								
i) Net private capital flows (a+b+c)**	80.6	90.1	168.3	239.4	271.1	220.9	495.4	291.3
a) Net private direct investment	185.9	154.7	164.4	191.5	262.7	258.3	302.2	293.9
b) Net private portfolio investment	-79.8	-91.3	-11.7	21.1	23.3	-111.9	20.6	-93.1
c) Net other private capital flows	-25.8	26.0	14.5	25.1	-17.0	73.6	171.0	88.8
ii) Net official flows	0.1	-2.7	-48.7	-67.2	-146.4	-165.8	-132.1	-141.2
IV. World Trade @								
i) Volume	0.2	3.5	5.5	10.8	7.5	9.2	6.6	6.7
ii) Price deflator (in US dollars)	-3.5	1.2	10.4	9.5	5.7	4.8	7.0	2.4
V. Current Account Balance (Per cent to GDP)								
i) US	-3.8	-4.4	-4.8	-5.5	-6.1	-6.2	-5.7	-5.5
ii) China	1.3	2.4	2.8	3.6	7.2	9.4	11.7	12.2
iii) Middle East	6.3	4.8	8.3	11.7	19.4	19.7	16.7	16.0

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.
** : On account of data limitations, flows listed under 'Net private capital flows' may include some official flows.
@ : Average of annual percentage change for world exports and imports of goods and services.
Source : World Economic Outlook, October 2007, International Monetary Fund.

World exports (in US dollar terms) in the first six months of 2007 (January-June) recorded a growth of 13.3 per cent (13.5 per cent in the corresponding period a year ago) supported by export growth in industrial countries (Table 50).

Table 50: Growth in Exports - Global Scenario

(Per cent)

Region/Country	2005	2006	2006 (January – July)	2007 (January – July)
1	2	3	4	5
World	**14.1**	**15.7**	**13.5 ***	**13.3 ***
Industrial Countries	**8.5**	**12.6**	**9.9 ***	**12.4 ***
USA	10.8	14.5	13.9	11.2
France	4.6	10.3	8.2 *	10.1 *
Germany	7.3	15.1	7.9 *	19.9 *
Japan	5.2	9.2	7.8 #	7.2 #
Developing Countries	**22.0**	**19.7**	**18.7**	**15.1**
Non-Oil Developing Countries	**19.4**	**20.0**	**19.6**	**16.6**
China	28.4	27.2	24.8	28.6
India	29.9	21.3	21.3 #	17.3 #
Indonesia	22.9	19.0	17.6	15.4
Korea	12.0	14.4	13.4	14.9
Malaysia	12.0	14.0	14.8	7.5
Singapore	15.6	18.4	22.4	9.3
Thailand	14.5	18.7	18.8	16.1

* : January-June. # : January-August.
Source: International Financial Statistics, International Money Fund; DGCI&S for India.

However, exports from developing countries showed a moderation in growth at 15.1 per cent during January-July 2007 from 18.7 per cent registered during the corresponding period a year ago. Amongst developing countries, exports from China maintained the high growth momentum at 28.6 per cent during January-July 2007.

Merchandise Trade

India's merchandise exports after registering strong growth in 2006-07, witnessed some moderation in the first five months of 2007-08 (Chart 40). According to the Directorate General of Commercial Intelligence and Statistics (DGCI&S), merchandise exports during 2007-08 (April-August) registered a growth of 18.2 per cent as compared with 27.1 per cent in the corresponding period of the previous year. Imports, on the other hand, posted high growth during April-August 2007-08 (31.0 per cent as compared with 20.6 per cent a year ago). Non-oil imports, which registered a growth of 44.3 per cent (10.9 per cent a year ago), accounted for 93 per cent of the overall import growth during 2007-08 (April-August). Oil imports showed a sharp deceleration in growth at 6.0 per cent as against 44.5 per cent during 2006-07 (April-August).

Commodity-wise data available for April-May 2007 show that the growth in exports emanated mainly from petroleum products, engineering goods and gems and jewellery, which together accounted for 69 per cent of the export growth (66 per cent in April-May 2006). Primary products showed a deceleration in April-May 2007, mainly due to a deceleration in exports of agriculture and allied products. Agricultural products exhibited moderation in growth on account of the decline in exports of raw cotton and sugar. Among the exports of manufactured goods, textiles and textile products exports showed a decline in April-May 2007; gems and jewellery

Chart 40: India's Merchandise Trade

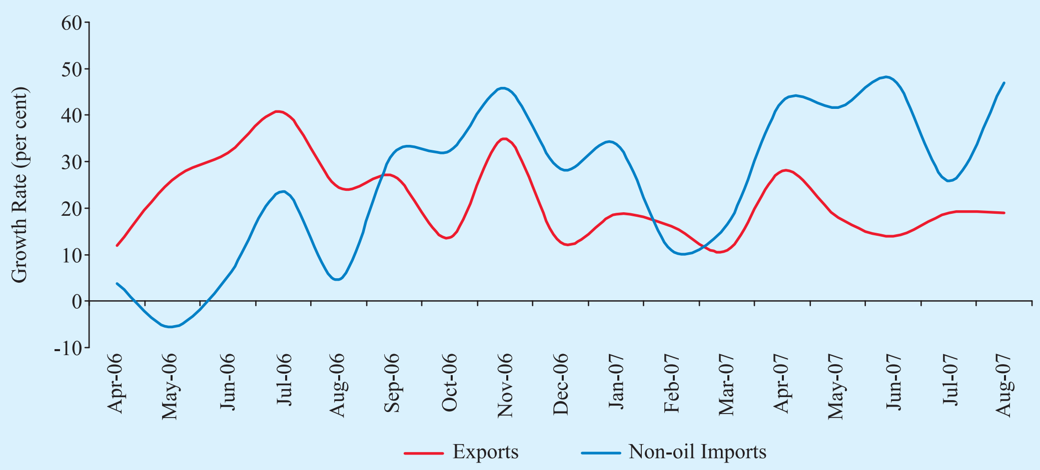


Table 51: Exports of Principal Commodities

Commodity Group	US $ billion			Variation (per cent)		
	2006-07	2006-07	2007-08	2006-07	2006-07	2007-08
		April-May			April-May	
1	2	3	4	5	6	7
1. Primary Products	**19.7**	**2.9**	**3.1**	**20.2**	**9.9**	**7.1**
of which:						
a) Agriculture and Allied Products	12.7	1.9	1.9	24.2	18.2	2.4
b) Ores and Minerals	7.0	1.0	1.2	13.6	-2.4	15.6
2. Manufactured Goods	**84.9**	**12.6**	**14.1**	**17.0**	**12.2**	**12.7**
of which:						
a) Chemicals and Related Products	17.3	2.5	2.7	17.4	12.1	7.9
b) Engineering Goods	29.6	4.1	5.3	36.1	20.2	27.9
c) Textiles and Textile Products	17.4	2.8	2.6	5.9	11.6	-7.7
d) Gems and Jewellery	16.0	2.5	2.9	2.9	3.9	18.1
3. Petroleum Products	**18.7**	**2.4**	**4.0**	**60.5**	**85.6**	**65.0**
4. Total Exports	**126.4**	**18.6**	**23.2**	**22.6**	**18.1**	**24.6**
Memo:						
Non-oil Exports	107.7	16.2	19.2	17.7	12.0	18.6

Source : DGCI&S.

exports witnessed a revival in April-May 2007 with a growth rate of 18.1 per cent as compared with a growth rate of only 3.9 per cent in April-May 2006 (Table 51).

Destination-wise, the US continued to be the major market for India's exports during 2007-08, though its share declined from 15.4 per cent in April-May 2006 to 13.1 per cent in April-May 2007. The US was followed by the UAE (10.3 per cent), China (5.6 per cent), Singapore (5.1 per cent) and the UK (4.2 per cent). Among the major regions, exports to OPEC decelerated, while that to the European Union (EU) and Asia showed higher growth in April-May 2007 (Table 52).

Table 52: Direction of India's Exports

Group/Country	US $ billion			Variation (per cent)		
	2006-07	2006-07	2007-08	2006-07	2006-07	2007-08
		April-May			April-May	
1	2	3	4	5	6	7
1. OECD Countries	**52.1**	**7.7**	**8.8**	**13.6**	**12.8**	**15.5**
of which:						
a) European Union	25.8	3.8	4.6	15.3	10.4	19.9
b) North America	20.0	3.0	3.2	9.0	17.3	5.7
US	18.9	2.9	3.0	8.8	17.9	5.8
2. OPEC	**20.7**	**3.0**	**3.9**	**35.6**	**42.4**	**30.7**
of which:						
UAE	12.0	1.7	2.4	39.8	49.9	37.0
3. Developing Countries	**50.7**	**7.6**	**9.8**	**27.6**	**16.0**	**29.5**
of which:						
Asia	37.6	5.9	7.0	21.3	17.1	18.0
People's Republic of China	8.3	1.2	1.3	22.7	4.4	10.1
Singapore	6.0	1.2	1.2	11.0	16.5	-4.5
4. Total Exports	**126.4**	**18.6**	**23.2**	**22.6**	**18.1**	**24.6**

Source : DGCI&S.

Table 53: Imports of Principal Commodities

Commodity Group	US $ billion			Variation (per cent)		
	2006-07	2006-07	2007-08	2006-07	2006-07	2007-08
		April-May			April-May	
1	2	3	4	5	6	7
Petroleum, Petroleum Products and Related Material	57.1	8.8	11.1	30.0	39.1	25.6
Edible Oil	2.1	0.4	0.3	4.2	24.2	-5.2
Iron and Steel	6.4	0.9	1.5	40.5	18.3	65.1
Capital Goods	47.1	6.3	8.2	25.0	39.6	31.1
Pearls, Precious and Semi-Precious Stones	7.5	1.2	1.5	-18.0	-29.4	23.0
Chemicals	7.8	1.1	1.5	12.1	-0.5	31.2
Gold and Silver	14.6	2.5	4.6	29.4	-25.8	82.7
Total Imports	**185.7**	**26.9**	**37.0**	**24.5**	**17.0**	**37.5**
Memo:						
Non-oil Imports	128.6	18.0	25.9	22.2	8.6	43.4
Non-oil Imports excluding Gold and Silver	114.0	15.5	21.3	21.4	17.5	37.0
Mainly Industrial Imports*	104.7	14.5	20.0	19.6	17.9	38.1

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

Source : DGCI&S.

Commodity-wise data on imports available for April-May 2007 show that growth in non-oil imports was more diversified as compared with April-May 2006. Capital goods continued to be the major contributor to the growth in non-oil imports, but its relative share in growth declined in April-May 2007. On the other hand, the contribution of gold and silver, iron and steel, pearls, precious and semi-precious stones increased. Capital goods accounted for 31.8 per cent of total non-oil imports in April-May 2007 followed by gold and silver (17.8 per cent), metalliferrous ores and metal scrap (6.9 per cent), pearls, precious and semi-precious stones (5.8 per cent) and iron and steel (5.6 per cent) (Table 53).

Source-wise, China was the major source of imports (oil *plus* non-oil imports) in April-May 2007, accounting for 10.4 per cent of total imports, followed by Switzerland (7.0 per cent), the UAE (6.0 per cent), Saudi Arabia (5.1 per cent), the US (4.8 per cent), Australia (4.8 per cent), Iran (4.6 per cent), Germany (3.9 per cent) and Singapore (3.2 per cent).

Trade deficit during 2007-08 (April-August) widened to US $ 32.5 billion, an increase of US $ 12.6 billion from US $ 19.9 billion a year ago (Table 54). The trade deficit on the oil account increased by US $ 0.7 billion in April-May 2007 to US $ 7.1 billion, while the non-oil trade deficit increased by US $ 4.8 billion to US $ 6.6 billion.

Table 54: India's Merchandise Trade

(US $ billion)

Item	2005-06	2006-07	2006-07	2007-08
			April-August	
1	2	3	4	5
Exports	103.1	126.4	50.3	59.4
Imports	149.2	185.7	70.2	92.0
Oil	44.0	57.1	24.4	25.9
Non-oil	105.2	128.6	45.8	66.1
Trade Balance	-46.1	-59.4	-19.9	-32.5
Non-Oil Trade Balance	-13.8	-20.9	-3.9	–
				Variation (per cent)
Exports	23.4	22.6	27.1	18.2
Imports	33.8	24.5	20.6	31.0
Oil	47.3	30.0	44.5	6.0
Non-oil	28.8	22.2	10.9	44.3

– : Not Available.
Source: DGCI&S.

Current Account

Net surplus under invisibles (services, transfers and income taken together) exhibited buoyancy during the first quarter of 2007-08, showing an increase of 36.4 per cent. Exports of services and higher transfer receipts comprising mainly remittances remained the key drivers of the net surplus (Table 55). Amongst services, both software and business services continued to record robust growth. Private transfers during April-June 2007 increased by over 45 per cent over the corresponding quarter of 2006-07.

The net invisible surplus offset a large part of the trade deficit – 78.2 per cent during April-June 2007 as compared with 73 per cent during the corresponding period of the previous year. Despite large merchandise trade deficit, higher net invisible surplus, mainly emanating from private transfers, contained the current

Table 55: Invisibles Account (Net)

(US $ million)

Item	2006-07 P	2006-07				2007-08
	April-March	April-June PR	July-Sept. PR	Oct.-Dec. PR	Jan-March P	April-June P
1	2	3	4	5	6	7
Services	32,727	7,965	7,268	7,467	10,027	9,150
Travel	2,188	220	-31	792	1,207	207
Transportation	-788	-314	-31	-255	-188	-484
Insurance	559	111	162	92	194	233
Government, not included elsewhere	-144	-24	-62	-11	-47	-16
Software	28,798	6,601	6,678	6,864	8,655	7,884
Other Services	2,114	1,371	552	-15	206	1,326
Transfers	27,415	5,692	5,226	7,844	8,653	8,327
Investment Income	-4,282	-1,147	-1,300	-1,088	-747	-486
Compensation of Employees	-564	-131	-162	-133	-138	-108
Total	**55,296**	**12,379**	**11,032**	**14,090**	**17,795**	**16,883**

P : Preliminary. PR : Partially Revised.

Table 56: India's Balance of Payments

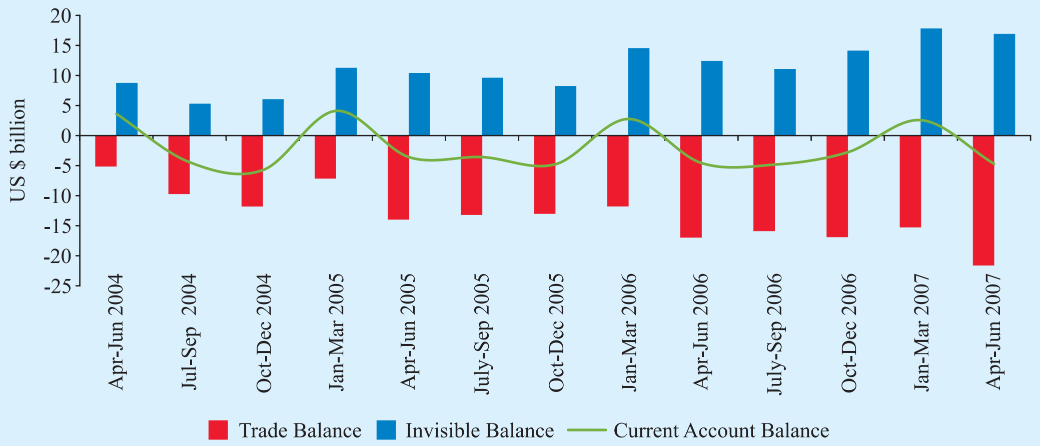
(US $ million)

Item	2006-07 P	2006-07				2007-08
	April-March	April-June PR	July-Sept. PR	Oct.-Dec. PR	Jan-March P	April-June P
1	2	3	4	5	6	7
Exports	127,090	29,674	32,700	30,664	34,052	34,960
Imports	191,995	46,620	48,562	47,529	49,284	56,540
Trade Balance	-64,905 (-7.1)	-16,946	-15,862	-16,865	-15,232	-21,580
Invisible Receipts	119,163	24,643	25,597	31,658	37,265	31,432
Invisible Payments	63,867	12,264	14,565	17,568	19,470	14,549
Invisibles, net	55,296 (6.0)	12,379	11,032	14,090	17,795	16,883
Current Account	-9,609 (-1.1)	-4,567	-4,830	-2,775	2,563	-4,697
Capital Account (net)*	46,215	10,946	7,100	10,280	17,889	15,897
of which:						
Foreign Direct Investment	8,437	1,416	2,426	2,558	2,037	461
Portfolio Investment	7,062	-505	2,152	3,569	1,846	7,458
External Commercial Borrowings +	16,084	3,959	1,458	3,994	6,673	7,048
Short-term Trade Credit	3,275	417	1,554	-316	1,620	1,048
External Assistance	1,770	49	337	633	751	258
NRI Deposits	3,895	1,231	797	1,236	631	-447@
Change in Reserves #	-36,606	-6,379	-2,270	-7,505	-20,452	-11,200
Memo:						
Current Account net of Private Transfers	**-36,804 (-4.0)**	**- 10,280**	**-10,047**	**-10,429**	**-6,048**	**-13,037**

P : Preliminary. PR : Partially Revised.
* : Includes errors and omissions. # : On balance of payments basis (excluding valuation); (-) indicates increase.
+ : Medium and long-term borrowings. @ : Includes Non-resident Rupee Deposits for April-June 2007.
Note : Figures in parentheses are percentages to GDP.

account deficit at US $ 4.7 billion in the first quarter of 2007-08, broadly at the same level as in the first quarter of 2006-07 (Table 56 and Chart 41). Net of remittances, the current account deficit was US $ 13.0 billion during April-June 2007.

Chart 41: Movement in Current Account Balance



Capital Flows

Capital flows to India have remained buoyant during the financial year 2007-08 so far. Among the major components of capital flows, foreign investment recorded an inflow of US $ 20.7 billion during April-July 2007. Inflows under foreign direct investment (FDI) into India at US $ 6.6 billion during April-July 2007 (US $ 3.7 billion in April-July 2006) witnessed significant increase, reflecting the continuing pace of expansion of domestic activities, positive investment climate, and long-term view of India as the investment destination. FDI was channelled mainly into services sector (34.2 per cent), followed by construction industry (20.6 per cent). While Mauritius continued as the dominant sources of FDI to India, FDI from Singapore exceeded that from the US.

Foreign institutional investors (FIIs) inflows (net) have aggregated US $ 21.2 billion during the current financial year so far (up to October 19, 2007), reflecting, *inter alia*, strong corporate performance and strong domestic equity markets (Table 57). The number of FIIs registered with the SEBI increased from 997 by end-March 2007 to 1,113 by October 15, 2007. Capital inflows through American depository receipts (ADRs)/global depository receipts (GDRs) abroad amounted to US $ 2.3 billion during April-July 2007.

During the first quarter of 2007-08 (April-June 2007), net inflows under external commercial borrowings (ECBs) continued to be buoyant at US $ 7.0 billion. Ongoing technological upgradation and modernisation combined with expansion of domestic industrial activities have led to increased investment demand by Indian companies, and some hardening of domestic interest rates, which is reflected in higher recourse to ECBs.

Table 57: Capital Flows

(US $ million)

Item	Period	2006-07	2007-08
1	2	3	4
Foreign Direct Investment (FDI) into India	April-July	3,675	6,609
FDI Abroad	April-June	-1,124	-5,422
FIIs (net)	April-October *	933	21,209
ADRs/GDRs	April-July	1,547	2,336
External Assistance (net)	April-June	49	258
External Commercial Borrowings (net) (Medium and long-term)	April-June	3,959	7,048
Short-term Trade Credits (net)	April-June	417	1,048
NRI Deposits (net)	April-July	1,585	-148

*: Up to October 19.

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.

Non-Resident Indian (NRI) deposits during April-July 2007 recorded a net outflow of US $ 148 million, which can be partly attributed to the impact of two downward revisions in ceiling interest rates during January 2007 and April 2007. While there were net inflows under Foreign Currency Non-Resident (Banks) [FCNR(B)] deposits, the higher magnitude of outflows under Non-Resident External Rupee Account [NR(E)RA] deposits resulted in overall net outflows.

With net capital flows being substantially higher than the current account deficit, the overall balance of payments recorded a surplus of US $ 11.2 billion in the first quarter of 2007-08 (US $ 6.4 billion in the first quarter of 2006-07).

Foreign Exchange Reserves

India's foreign exchange reserves were US $ 261.1 billion as on October 19, 2007, higher by US $ 62.0 billion over end-March 2007. The increase in reserves was mainly due to an increase in foreign currency assets from US $ 191.9 billion during end-March 2007 to US $ 253.3 billion as on October 19, 2007 (Table 58).

India holds the fifth largest stock of reserves among the emerging market economies and sixth largest in the world. 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.

Table 58: Foreign Exchange Reserves

(US $ million)

Month	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
March 2007	6,784	2	191,924	469	199,179
April 2007	7,036	11	196,899	463	204,409
May 2007	6,911	1	200,697	459	208,068
June 2007	6,787	1	206,114	460	213,362
July 2007	6,887	12	219,753	455	227,107
August 2007	6,881	2	221,509	455	228,847
September 2007	7,367	2	239,955	438	247,762
October 2007*	7,367	13	253,324	439	261,143

* : As on October 19, 2007.

External Debt

India's total external debt was placed at US $ 165.4 billion at end-June 2007, recording an increase of US $ 8.7 billion (5.6 per cent) over end-March 2007. The increase in external debt during the period was mainly on account of higher external commercial borrowings, followed by higher NRI deposits and short-term trade credit. Over 50 per cent of the external debt stock was denominated in US dollars followed by the Indian rupee (18.0 per cent), SDR (12.3 per cent) and Japanese yen (12.0 per cent). Debt sustainability indicators such as the ratio of short-term to total debt and short-term debt to reserves increased marginally between end-March 2007 and end-June 2007. Foreign exchange reserves remained in excess of the stock of external debt (Table 59).

International Investment Position

India's net international liabilities declined by US $ 2.7 billion between end-March 2006 and end-March 2007, as the increase in international assets (US $ 60.8 billion) exceeded the increase in international liabilities (US $ 58.1 billion) (Table 60). The increase in international assets was mainly on account of reserve assets, which registered an increase of US $ 47.6 billion between end-March 2006 and end-March 2007, followed by direct investment abroad which

Table 59: India's External Debt

(US $ million)

Item	End-March 1995	End-March 2005	End-March 2006	End-March 2007	End-June 2007
1	2	3	4	5	6
1. Multilateral	28,542	31,698	32,559	35,641	35,958
2. Bilateral	20,270	17,011	15,734	16,104	15,687
3. International Monetary Fund	4,300	0	0	0	0
4. Trade Credit (above 1 year)	6,629	5,021	5,419	6,964	7,782
5. External Commercial Borrowings	12,991	27,857	26,902	42,780	48,314
6. NRI Deposit	12,383	32,743	36,282	41,240	42,603
7. Rupee Debt	9,624	2,301	2,031	1,949	2,031
8. Long-term (1 to 7)	94,739	116,631	118,927	144,678	152,375
9. Short-term	4,269	7,529	8,696	11,971	13,019
Total (8+9)	**99,008**	**124,160**	**127,623**	**156,649**	**165,394**
Memo:					(per cent)
Total debt /GDP	30.8	17.4	16.0	16.6	–
Short-term/Total debt	4.3	6.1	6.8	7.6	7.9
Short-term debt/Reserves	16.9	5.3	5.7	6.0	6.1
Concessional debt/Total debt	45.3	33.1	30.9	25.5	23.8
Reserves/ Total debt	25.4	114.0	118.8	127.1	129.0
Debt Service Ratio*	25.9	6.1	9.9	4.8	4.6

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

increased by US $ 11 billion during the same period. International liabilities reflected increases in direct and portfolio investment and loans at end-March 2007 from their levels at end-March 2006. A major part of the liabilities like direct and portfolio investments reflects cumulative inflows, which are at historical prices.

Table 60: International Investment Position of India

(US $ billion)

Item	March 2004 R	March 2005 PR	March 2006 PR	March 2007 P
1	2	3	4	5
A. Assets	**136.0**	**166.8**	**182.8**	**243.6**
	(21.3)	**(23.3)**	**(22.9)**	**(25.7)**
1. Direct Investment	7.8	10.0	13.0	24.0
2. Portfolio Investment	0.4	0.5	1.0	0.8
2.1 Equity Securities	0.2	0.3	0.5	0.4
2.2 Debt securities	0.2	0.2	0.5	0.4
3. Other Investment	14.9	14.8	17.2	19.7
3.1 Trade Credits	0.5	1.1	-0.3	2.5
3.2 Loans	1.8	1.9	2.6	2.6
3.3 Currency and Deposits	9.5	8.4	11.6	10.3
3.4 Other Assets	3.1	3.4	3.3	4.2
4. Reserve Assets	113.0	141.5	151.6	199.2
	(17.7)	(19.8)	(19.0)	(21.0)
B. Liabilities	**183.2**	**209.8**	**230.8**	**288.9**
	(29.0)	**(29.4)**	**(28.9)**	**(30.5)**
1. Direct Investment	38.2	44.5	51.1	72.3
	(6.0)	(6.2)	(6.4)	(7.6)
2. Portfolio Investment	43.7	55.7	64.6	80.3
	(6.9)	(7.8)	(8.1)	(8.5)
2.1 Equity Securities	33.9	43.2	54.7	63.3
2.2 Debt securities	9.8	12.5	9.9	17.0
3. Other Investment	101.3	109.7	115.0	136.4
	(16.1)	(15.4)	(14.4)	(14.4)
3.1 Trade Credits	6.3	9.6	10.5	13.7
3.2 Loans	61.9	65.3	67.8	81.1
3.3 Currency and Deposits	32.2	33.6	36.2	40.7
3.4 Other Liabilities	1.0	1.2	0.6	0.9
C. Net Position (A-B)	**-47.2**	**-43.0**	**-48.0**	**-45.3**
	(-7.6)	**(-6.0)**	**(-6.0)**	**(-4.8)**

R : Revised. PR : Partially Revised. P : Provisional.
Note : Figures in parentheses represent percentage to GDP.