

III. MONETARY AND LIQUIDITY CONDITIONS

Monetary and liquidity aggregates continued to expand at a strong pace during 2007-08, *albeit* with some moderation, reflecting large and persistent capital flows. Broad money growth at 20.7 per cent at end-March 2008 was above the indicative trajectory of 17.0-17.5 per cent for 2007-08 set out in the Annual Policy Statement in April 2007. Expansion in bank credit to the commercial sector moderated and remained within the Reserve Bank's policy projection of 24.0-25.0 per cent (April 2007). Accretion to bank deposits, led by time deposits, remained buoyant. Banks' investments in SLR securities increased in tandem with growth in deposits. As a result, their SLR investments as a proportion of their NDTL remained almost at the same level as at end-March 2007. The Reserve Bank continued to actively manage liquidity during 2007-08 by using all the policy instruments at its disposal including cash reserve ratio (CRR), issuances of securities under the market stabilisation scheme (MSS), operations under the liquidity adjustment facility (LAF) and conduct of open market operations (OMO).

Monetary Survey

Broad money (M_3) growth, on a year-on-year (y-o-y) basis, was at 20.7 per cent as at end-March 2008 lower than 21.5 per cent a year ago, reflecting some deceleration in time deposits. Broad money growth, nevertheless, was strong with expansion in aggregate deposits, y-o-y, remaining higher than the projected aggregates of Rs. 4,90,000 crore for 2007-08 set out in the Annual Policy Statement (April 2007). The primary source of monetary expansion continued to be the accretion to net foreign exchange assets, while bank credit to the commercial sector moderated. 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 – was marginally higher at 21.2 per cent at end-March 2008 than 21.0 per cent a year ago. Growth in liquidity aggregate, L_1 , at 20.4 per cent at end-March 2008 was marginally lower than that of 20.6 per cent a year ago (Table 25 and Chart 11).

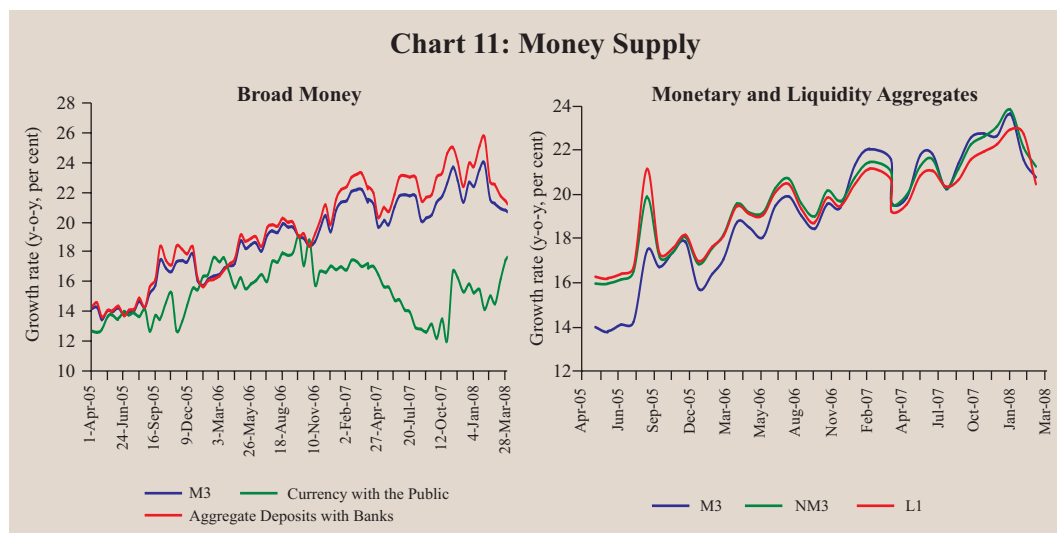
Taking into consideration the evolving monetary and liquidity conditions, while the focus of the Reserve Bank's operations was generally on managing excess capital flows through various instruments at its disposal, it remained vigilant to the evolving situation. The CRR was raised by 150 basis points in

Table 25: Monetary Indicators

(Amount in Rupees crore)						
Item	Outstanding as on March 31, 2008	Variation				
		March 31, 2007		March 31, 2008		
		Absolute	Per cent	Absolute	Per cent	
1	2	3	4	5	6	
I. Reserve Money	9,28,317	1,35,935	23.7	2,19,326	30.9	
II. Narrow Money (M ₁)	11,43,640	139,714	16.9	1,77,550	18.4	
III. Broad Money (M ₃)	40,02,189	5,86,548	21.5	6,86,096	20.7	
a) Currency with the Public	5,67,746	69,786	16.9	84,840	17.6	
b) Aggregate Deposits	34,25,379	5,16,134	22.3	5,99,687	21.2	
i) Demand Deposits	5,66,829	69,300	17.1	91,142	19.2	
ii) Time Deposits	28,58,550	4,46,834	23.5	5,08,546	21.6	
of which: Non-Resident Foreign Currency Deposits	56,564	8,185	13.8	-10,897	-16.2	
IV. NM ₃	40,27,891	5,77,013	21.0	7,03,293	21.2	
of which: Call Term Funding from FIs	1,05,857	2,692	3.2	20,021	23.3	
V. a) L ₁	41,42,470	5,88,644	20.6	7,02,323	20.4	
of which: Postal Deposits	1,14,579	11,631	11.2	-970	-0.8	
b) L ₂	41,45,402	5,88,644	20.6	7,02,323	20.4	
c) L ₃	41,71,370	5,90,718	20.5	7,03,594	20.3	
VI. Major Sources of Broad Money						
a) Net Bank Credit to the Government (i+ii)	9,04,927	70,969	9.3	67,363	8.0	
i) Net Reserve Bank Credit to Government	-1,10,223	-2,384	-	-1,15,975	-	
of which: to the Centre	-1,10,353	-3,024	-	-1,12,489	-	
ii) Other Banks' Credit to Government	10,15,150	73,353	9.7	1,83,338	22.0	
b) Bank Credit to Commercial Sector	25,62,652	4,37,074	25.8	4,32,574	20.3	
c) Net Foreign Exchange Assets	12,66,297	1,86,985	25.7	3,53,118	38.7	
d) Government Currency Liability to Public	9,228	-493	-5.6	968	11.7	
e) Net Non-Monetary Liabilities of the Banking Sector	7,40,915	1,07,987	23.2	1,67,926	29.3	
Memo :						
Aggregate Deposits of SCBs	31,92,141	5,02,885	23.8	5,80,208	22.2	
Non-food Credit of SCBs	23,04,094	4,18,282	28.5	4,19,425	22.3	
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 + Term borrowing by FIs + Certificates of deposit issued by FIs.						
L ₃ = L ₂ + Public deposits of NBFCs.						
Note : 1. Data are provisional. Wherever data are not available the estimates for the last available month have been repeated.						
2. Data for postal deposits pertain to February 2008.						
3. Government Balances as on March 31, 2008 are before closure of accounts.						

three phases (April, August and November 2007) during 2007-08. The estimated amount of liquidity impounded in the first round on account of increase in CRR during 2007-08 was Rs.47,000 crore¹. The ceiling on the outstanding amount under the MSS for the year 2007-08 was also successively raised on four occasions (April, August, October and November 2007) to Rs. 2,50,000 crore

¹ Between December 2006 and March 2008 the Reserve Bank increased CRR by 250 basis points and the estimated amount of liquidity impounded in the first round due to the hike in CRR was Rs. 74,500 crore.



from the initial limit of Rs.80,000 crore. In view of the prevailing liquidity conditions, the Reserve Bank during 2008-09 so far increased CRR by 50 basis points to 8.0 per cent in two stages, 25 basis points in each stage, effective from the fortnight beginning April 26, 2008 and May 10, 2008, respectively. As a result of the above hike in CRR, an amount of about Rs. 18,500 crore of resources of banks is likely to be absorbed.

Expansion in currency with the public was of a lower order throughout 2007-08, except in November 2007, when it increased sharply on account of festive season currency demand. Currency with the public increased by 17.6 per cent, y-o-y, as at end-March 2008, marginally higher than the growth of 16.9 per cent a year ago. Growth in demand deposits, y-o-y, as at end-March, 2008 was higher at 19.2 per cent than 17.1 per cent a year ago. Demand deposits, after remaining subdued for most part of the year, expanded during the brief period of January and beginning of February 2008, mainly reflecting developments in the equity market. Accordingly, growth in narrow money (M_1), y-o-y, was higher at 18.4 per cent at end-March 2008 higher than 16.9 per cent recorded a year ago. The buoyancy in time deposits continued in 2007-08, although some moderation was observed during the last quarter of 2007-08. Growth in time deposits was 21.6 per cent, y-o-y, as at end-March 2008 as compared with 23.5 per cent a year ago (Table 26). The strong growth in time deposits could be attributed, *inter alia*, to robust economic activity, higher interest rates on bank deposits relative to postal deposits and extension of tax benefits under Section 80C for bank deposits. During 2007-08 accretion to

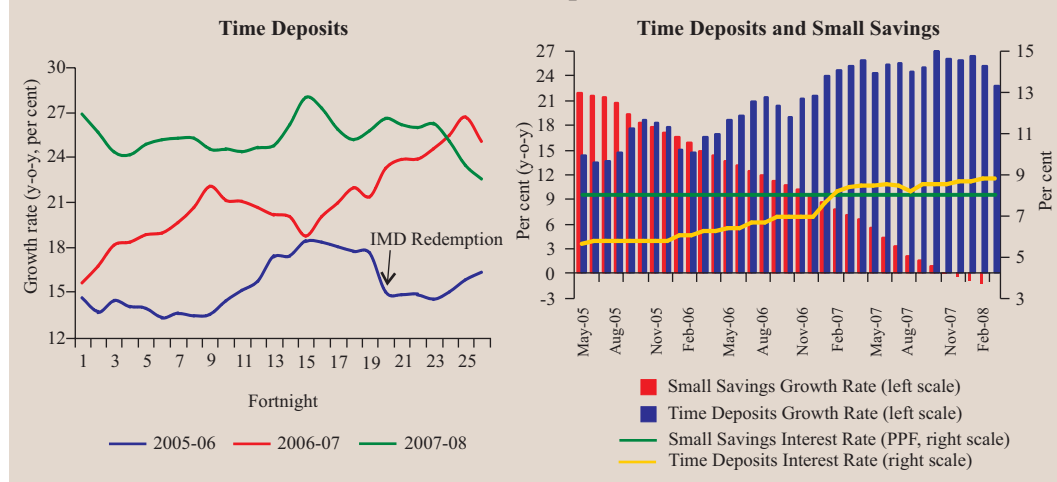
Table 26: Monetary Aggregates - Variations

Item	(Rupees Crore)					
	2006-07	2007-08	2007-08			
			Q1	Q2	Q3	Q4
1	2	3	4	5	6	7
M ₃ (1+2+3 = 4+5+6+7-8)	5,86,548 (21.5)	6,86,096 (20.7)	73,824	1,93,671	1,15,159	3,03,443
Components						
1 Currency with the Public	69,786 (16.9)	84,840 (17.6)	18,237	-14,478	47,731	33,350
2 Aggregates Deposits with Banks	5,16,134 (22.3)	5,99,687 (21.2)	56,023	2,09,628	68,233	2,65,804
2.1 Demand Deposits with Banks	69,300 (17.1)	91,142 (19.2)	-44,030	58,308	-6,809	83,673
2.2 Time Deposits with Banks	4,46,834 (23.5)	5,08,546 (21.6)	1,00,053	1,51,320	75,042	1,82,131
3 'Other' Deposits with Banks	628	1,568	-436	-1,479	-805	4,289
Sources						
4 Net Bank Credit to Government	70,969 (9.3)	67,363 (8.0)	24,787	17,137	-37,057	62,495
4.1 RBI's Net Credit to Government	-2,384	-1,15,975	-25,483	-54,695	-65,787	29,990
4.1.1 RBI's Net Credit to Centre	-3,024	-1,12,489	-21,825	-55,588	-65,078	30,002
4.2 Other Banks' Credit to Government	73,353	1,83,338	50,270	71,832	28,730	32,505
5 Bank Credit to Commercial Sector	4,37,074 (25.8)	4,32,574 (20.3)	-30,547	1,38,692	89,513	2,34,916
6 NFEA of Banking Sector	1,86,985	3,53,118	-17,945	1,18,249	94,204	1,58,610
6.1 NFEA of RBI	1,93,170	3,69,977	-2,745	1,19,430	94,681	1,58,610
7 Government's Currency Liabilities to the Public	-493	968	166	354	312	136
8 Net Non-Monetary Liabilities of the Banking Sector	1,07,987	1,67,926	-97,362	80,760	31,814	1,52,714
<i>Memo:</i>						
1 Non-resident Foreign Currency Deposits with SCBs	8,185	-10,897	-4,202	-1,181	-3,490	-2,025
2 SCB' Call Term Borrowing from Financial Institutions	2,692	20,021	-2,984	5,756	7,441	9,808
3 Overseas Borrowing by SCBs	2,071	13,644	-6,928	7,830	1,734	11,008
SCBs: Scheduled Commercial Banks.			NFEA: Net Foreign Exchange Assets.			
Note: 1. Figures in parentheses are percentage variations.						
2. Government Balances as on March 31, 2008 are before closure of accounts.						

postal deposits decelerated significantly up to November 2007 and started depleting thereafter (Chart 12). In order to revive interest in postal deposits, the Government of India had announced in December 2007 some incentives, including tax benefits for certain postal deposits.

Expansion in the bank credit to the commercial sector moderated during 2007-08 and remained within the Reserve Bank's policy projection in April 2007, after a strong pace of credit expansion for three consecutive years. Non-food credit by scheduled commercial banks (SCBs) expanded by 22.3 per cent,

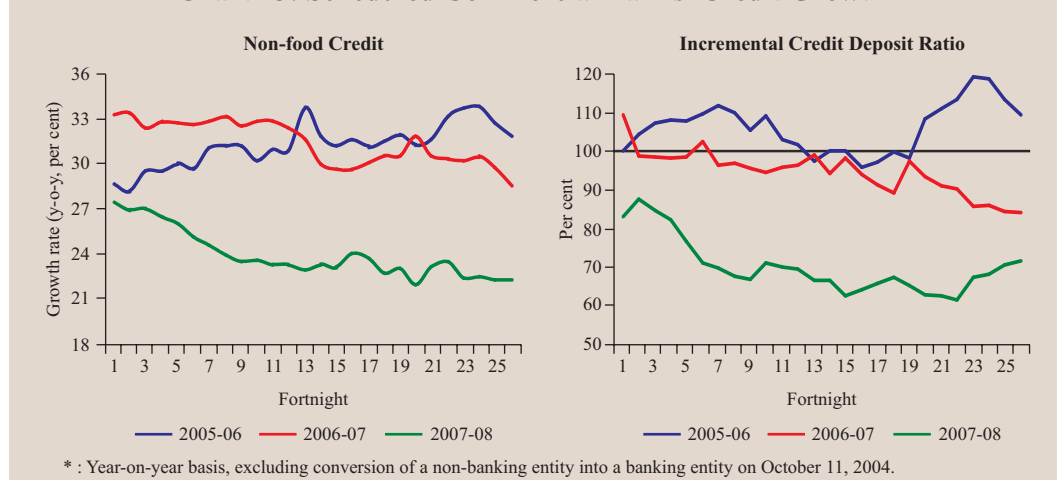
Chart 12: Time Deposits Growth



y-o-y, as at end-March 2008 as compared with 28.5 per cent a year ago. The deceleration in credit growth relative to the acceleration in deposit growth led to a decline in the incremental credit-deposit ratio, y-o-y, of SCBs to 71.9 per cent as at end-March 2008 from 84.3 per cent a year ago (Chart 13).

Disaggregated sectoral data available up to February 15, 2008 showed that about 45 per cent of incremental non-food credit, y-o-y, was absorbed by industry, compared with 36 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 and telecommunication), textile, food processing, iron and steel, engineering, chemicals, vehicles, construction and

Chart 13: Scheduled Commercial Banks' Credit Growth*



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

petroleum industries. The infrastructure sector alone accounted for around 33 per cent of the incremental credit to industry as compared with 21 per cent in the corresponding period of the previous year. The agricultural sector absorbed around 9 per cent of the incremental non-food bank credit expansion as compared with 12 per cent in the corresponding period of the previous year. Personal loans accounted for 16 per cent of incremental non-food credit; within personal loans, the share of incremental housing loans was at 46 per cent. Growth in loans to commercial real estate remained high, notwithstanding some moderation (Table 27).

Table 27: Non-food Bank Credit - Sectoral Deployment

(Amount in Rupees Crore)					
Sector/Industry	Outstanding as on February 15, 2008	Year-on-Year Variations			
		February 16, 2007		February 15, 2008	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
Non-food Gross Bank Credit (1 to 4)	20,60,131	3,90,095	30.1	3,71,053	22.0
1. Agriculture and Allied Activities	2,41,802	46,212	28.6	34,013	16.4
2. Industry (Small, Medium and Large)	8,14,976	1,41,459	28.0	1,67,819	25.9
Small Scale Industries	1,41,283	21,052	24.9	35,553	33.6
3. Personal Loans	5,03,728	1,04,225	30.6	58,669	13.2
Housing	2,51,688	46,019	25.8	26,930	12.0
Advances against Fixed Deposits	42,671	3,018	8.9	5,773	15.6
Credit Cards	19,344	4,003	45.3	6,502	50.6
Education	20,471	5,170	55.3	5,938	40.9
Consumer Durables	9,368	1,720	24.2	525	5.9
4. Services	4,99,625	98,198	33.9	1,10,553	28.4
Transport Operators	31,984	7,521	50.9	9,669	43.3
Professional & Other Services	26,689	7,154	50.1	5,188	24.1
Trade	1,18,892	23,719	30.9	17,731	17.5
Real Estate Loans	53,897	18,770	79.0	11,361	26.7
Non-Banking Financial Companies	64,106	12,021	39.2	20,979	48.6
<i>Memo :</i>					
Priority Sector	6,85,567	1,09,094	22.9	99,277	16.9
Industry (Small, Medium and Large)	8,14,976	1,41,459	28.0	1,67,819	25.9
Food Processing	48,290	7,904	27.6	11,720	32.0
Textiles	90,261	19,191	35.5	16,862	23.0
Paper & Paper Products	13,190	1,650	18.2	2,470	23.0
Petroleum, Coal Products & Nuclear Fuels	39,291	12,489	64.4	7,412	23.3
Chemicals and Chemical Products	60,892	8,610	19.2	7,437	13.9
Rubber, Plastic & their Products	9,788	1,988	31.0	1,355	16.1
Iron and Steel	72,290	14,609	31.8	11,661	19.2
Other Metal & Metal Products	23,302	5,459	38.5	3,634	18.5
Engineering	51,203	6,198	18.1	10,623	26.2
Vehicles, Vehicle Parts and Transport Equipments	26,437	2,028	11.9	7,337	38.4
Gems & Jewellery	24,353	2,619	13.3	2,073	9.3
Construction	23,418	6,132	52.6	5,856	33.3
Infrastructure	1,88,171	29,033	28.2	55,716	42.1
Note : Data are provisional and relate to select scheduled commercial banks.					

In addition to bank credit for financing their requirements, the corporate sector continued to rely on a variety of non-bank sources of funds such as capital markets, external commercial borrowings and internal generation of funds. Resources raised through domestic equity issuances during 2007-08 (Rs.48,153 crore) were 68 per cent higher than a year ago. Net mobilisation through external commercial borrowings (ECBs) during April-December of 2007-08 increased by 54 per cent over the corresponding period of the previous year. Mobilisation through issuances of commercial paper (CPs) during 2007-08 was nearly three times the issuances during the previous year. Internal generation of funds continued to provide a strong support to the funding requirements of the corporate sector, despite the profits after tax of select non-financial non-government companies during April-December of 2007-08 witnessing some deceleration as compared with the corresponding period of the previous year (see Table 12). Resources raised in the form of equity issuances through American depository receipts (ADRs) and global depository receipts (GDRs) during 2007-08 (Rs.13,023 crore) were lower by nearly 20 per cent than a year ago (Table 28).

Table 28: Select Sources of Funds to Industry

Item	2006-07	2007-08	(Rupees Crore)			
			2007-08			
			Q1	Q2	Q3	Q4
1	2	3	4	5	6	7
A. Bank Credit to Industry #	1,41,543 (46,566) *	85,166 *	-15,603	59,776	40,993	32,476 ^
B. Flow from Non-banks to Corporates						
1 Capital Issues (i+ii)	29,178	51,479	13,788	6,226	14,400	17,065
i) Non-Government Public Ltd. Companies (a+b)	29,178	48,962	13,261	4,236	14,400	17,065
a) Bonds/Debentures	585	809	0	0	0	809
b) Shares	28,593	48,153	13,261	4,236	14,400	16,256
ii) PSUs and Government Companies	0	2,517	527	1,990	0	0
2 ADR/GDR Issues	16,184	13,023	1,251	9,899	289	1,584
3 External Commercial Borrowings (ECBs)	1,04,046 (70,966) *	1,09,592 *	35,808	36,168	37,616	-
4 Issue of CPs	4,970	14,904	8,568	7,358	6,629	-7,651
C. Depreciation Provision +	37,095 (24,392) *	29,604 *	10,173	10,576	10,961	-
D. Profits after Tax +	1,11,107 (75,036) *	99,272 *	32,699	34,266	37,470	-

- : Not Available.

* : April-December. ^ : up to February 15, 2008.

: Data pertain to select scheduled commercial banks.

+ : Data are based on abridged results of select non-financial non-Government companies. The quarterly data may not add up to annual data due to differences in the number and composition 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 and are not adjusted for banks' investments in capital issues, which are not expected to be significant.

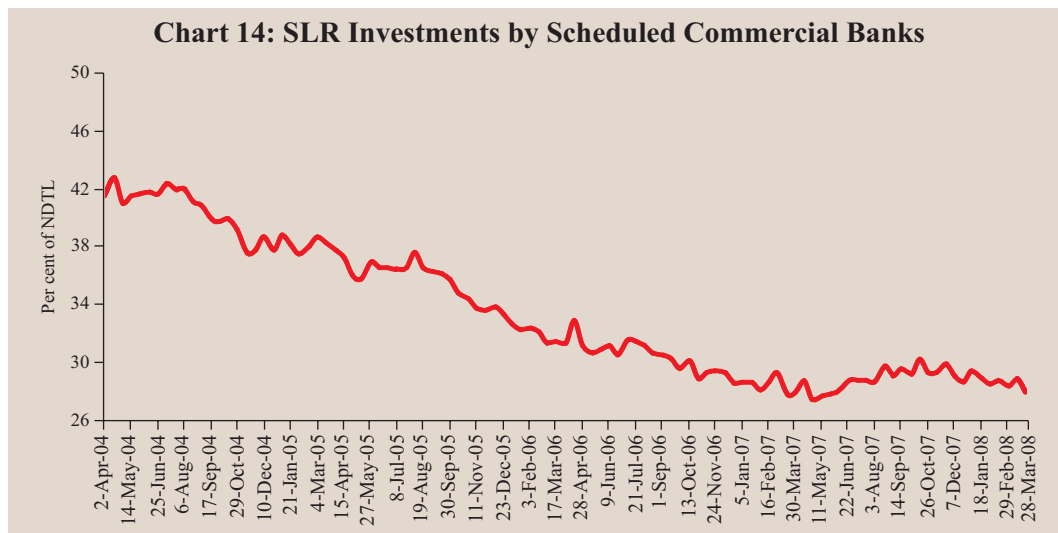
3. Data on ADR/GDR issues exclude issuances by banks and financial institutions.

4. Data on external commercial borrowings include short-term credit.

Scheduled commercial banks' investment in Government and other approved securities expanded during 2007-08, mainly reflecting the need to maintain SLR requirements in consonance with the increase in their net demand and time liabilities. Investment in SLR securities by SCBs increased by 22.9 per cent, y-o-y, as at end-March 2008 as compared with 10.3 per cent a year ago (Table 29). Commercial banks' holdings of such securities at end-March 2008 remained at 27.9 per cent of their NDTL almost the same as at end-March 2007 (Chart 14). Excess SLR investments of SCBs, thus, increased to Rs.1,02,422 crore as at end-March 2008 from Rs.81,484 crore at end-March 2007. Investment by SCBs in non-SLR securities increased substantially during the year. Banks' overseas foreign currency borrowings accelerated. They also drew down their holdings of foreign currency assets.

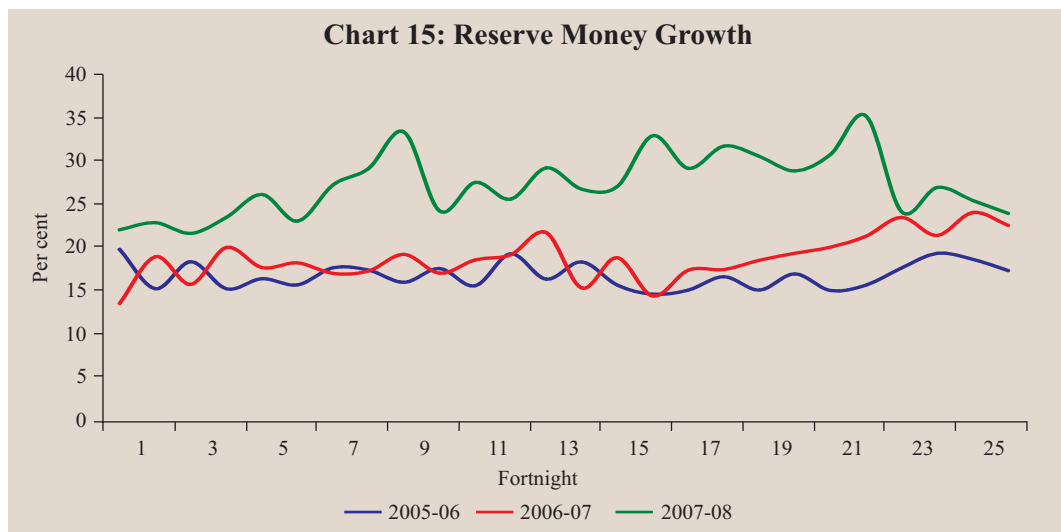
Table 29: Scheduled Commercial Bank's Survey

Item	(Amount in Rupees Crore)				
	Outstanding as on March 28, 2008	Variation (Year-on-Year)			
		As on Mar 30, 2007		As on Mar 28, 2008	
		Amount	Per Cent	Amount	Per Cent
1	2	3	4	5	6
Sources of Funds					
1. Aggregate Deposits	31,92,141	5,02,885	23.8	5,80,208	22.2
2. Call/Term Funding from Financial Institutions	1,05,857	2,692	3.2	20,021	23.3
3. Overseas Foreign Currency Borrowings	45,549	2,071	6.9	13,644	42.8
4. Capital	43,598	1,461	4.5	9,523	27.9
5. Reserves	2,26,068	23,613	16.3	57,343	34.0
Uses of Funds					
1. Bank Credit	23,48,493	4,24,112	28.1	4,17,304	21.6
<i>of which:</i> Non-food Credit	23,04,094	4,18,282	28.5	4,19,425	22.3
2. Investments in Government and Other Approved Securities*	9,72,738	74,062	10.3	1,81,222	22.9
a) Investments in Government Securities	9,53,525	75,316	10.7	1,77,467	22.9
b) Investments in Other Approved Securities	19,213	-1,255	-7.5	3,755	24.3
3. Investments in non-SLR Securities	1,68,526	5,114	3.8	28,071	20.0
4. Foreign Currency Assets	30,884	15,260	35.1	-27,869	-47.4
5. Balances with the RBI	2,57,122	53,161	41.8	76,900	42.7
* : Refers to investment in SLR securities as notified in the Reserve Bank notification DBOD No. Ref. BC. 61/12.02.001/2007-08 dated February 13, 2008.					
Note: Data are provisional.					



Reserve Money Survey

Expansion in reserve money as on March 28, 2008, y-o-y, was 23.8 per cent higher than 22.5 per cent a year ago (Chart 15). Reserve money growth was higher at 30.9 per cent, y-o-y, as on March 31, 2008 than 23.7 per cent a year ago mainly due to Reserve Bank's injection of liquidity through LAF, reflecting the year-end liquidity requirements of the banks. Adjusted for the first round effect of the hike in CRR, reserve money growth at 25.3 per cent was higher than 18.9 per cent a year ago. Intra-year movements in reserve money largely reflected the Reserve Bank's market operations and movements in bankers' deposits with



the Reserve Bank in the wake of hikes in the CRR and large expansion in demand and time liabilities. Bankers' deposits with the Reserve Bank expanded by 66.5 per cent during 2007-08 as compared with 45.6 per cent during 2006-07. Growth in currency in circulation at 17.2 per cent during 2007-08 was marginally higher than 17.1 per cent a year ago (Table 30).

On the sources side, reserve money continued to be driven by Reserve Bank's foreign currency assets (adjusted for revaluation), increasing by

Table 30 : Reserve Money - Variations

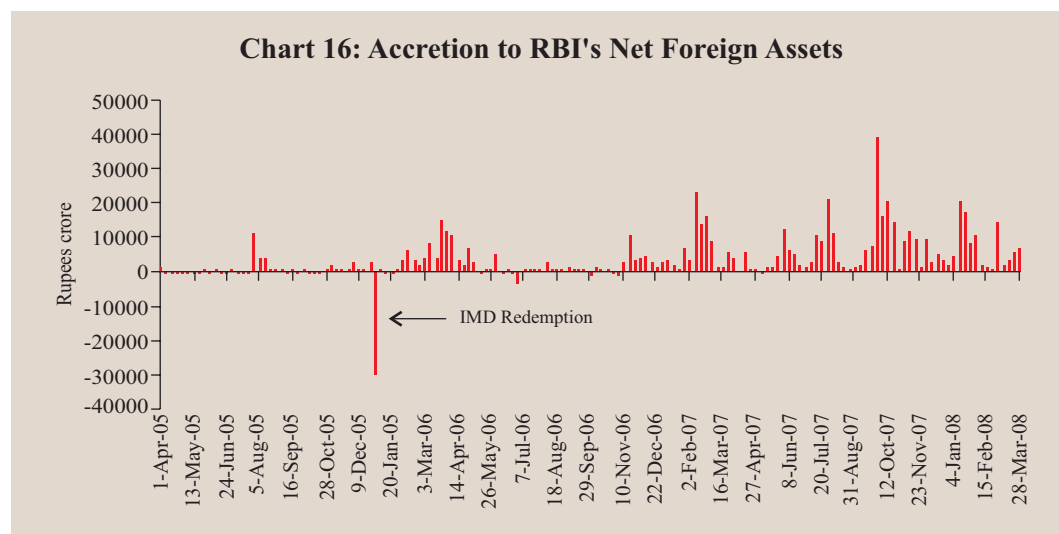
Item	Outstanding as on March 31, 2008	2006-07	2007-08	(Amount in Rupees Crore)			
				2007-08			
				Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8
Reserve Money	9,28,317	1,35,935	2,19,326	11,630	60,688	26,607	1,20,402
Components (1+2+3)		(23.7)	(30.9)				
1. Currency in Circulation	5,90,805	73,523	86,606	16,866	-13,297	46,781	36,256
		(17.1)	(17.2)				
2. Bankers' Deposits with RBI	3,28,447	61,784	1,31,152	-4,800	75,464	-19,369	79,857
		(45.6)	(66.5)				
3. 'Other' Deposits with the RBI	9,065	628	1,568	-436	-1,479	-805	4,289
		(9.1)	(20.9)				
Sources (1+2+3+4-5)							
1. RBI's net Credit to Government	-1,10,223	-2,384	-1,15,975	-25,483	-54,695	-65,787	29,990
<i>of which:</i> to Centre (i+ii+iii+iv-v)	-1,10,353	-3,024	-1,12,489	-21,825	-55,588	-65,078	30,002
i. Loans and Advances	0	0	0	0	0	0	0
ii. Treasury Bills held by the RBI	0	0	0	0	0	0	0
iii. RBI's Holdings of Dated Securities	1,14,593	26,763	17,421	-34,284	4,019	20,874	26,812
iv. RBI's Holdings of Rupee coins	132	-143	121	128	20	3	-31
v. Central Government Deposits	2,25,079	29,644	1,30,031	-12,330	59,627	85,956	-3,221
2. RBI's Credit to Banks and Commercial Sector	6,378	1,990	-2,794	-6,450	-1,256	848	4,064
3. NFEA of RBI	12,36,130	1,93,170	3,69,977	-2,745	1,19,430	94,681	1,58,610
		(28.7)	(42.7)				
<i>of which</i> : FCA, adjusted for revaluation		1,64,601	3,70,550	47,728	1,18,074	1,00,888	1,03,860
4. Governments' Currency Liabilities to the Public	9,228	-493	968	166	354	312	136
5. Net Non-Monetary Liabilities of RBI	2,13,197	56,347	32,849	-46,142	3,145	3,447	72,398
<i>Memo:</i>							
LAF- Repos (+) / Reverse Repos (-)	50,350	36,435	21,165	-32,182	9,067	16,300	27,980
Net Open Market Sales # *		5,125	-5,923	1,246	1,560	-3,919	-4,810
Centre's Surplus	76,686	1,164	26,594	-34,597	15,376	54,765	-8,950
Mobilisation under MSS	1,68,392	33,912	1,05,419	19,643	48,855	31,192	5,728
Net Purchases(+)/Sales(-) from Authorised Dealers		1,18,994	3,00,875 ^	38,873	1,01,814	87,596	72,592 ^
NFEA/Reserve Money @	133.2	122.2	133.2	119.8	125.8	133.4	133.2
NFEA/Currency @	209.2	171.8	209.2	165.7	193.6	194.3	209.2
NFEA : Net Foreign Exchange Assets.		FCA : Foreign Currency Assets.		LAF : Liquidity Adjustment Facility.			
* : At face value.		# : Excludes Treasury Bills		@ : Per cent, end of period.		^ : up to end-February 2008	
Note: 1. Data are based on March 31 for Q4 and last reporting Friday for all other quarters.							
2. Figures in parentheses are percentage variations during the fiscal year.							
3. Government Balances as on March 31, 2008 are before closure of accounts.							

Rs.3,70,550 crore during 2007-08 as compared with Rs.1,64,601 crore during the previous year (Chart 16).

Movements in the Reserve Bank's net credit to the Central Government during 2007-08 largely reflected the liquidity management operations by the Reserve Bank and movements in Government deposits with the Reserve Bank. The sterilisation operations of the Reserve Bank under the MSS led to an increase in Central Government deposits with the Reserve Bank. Surplus cash balances of the Central Government with the Reserve Bank also increased. Reserve Bank's holdings of Central Government dated securities increased on account of injection of liquidity under LAF. Reflecting the net impact of these developments, the Reserve Bank's net credit to the Centre declined by Rs.1,12,489 crore during 2007-08 as compared with the decline of Rs. 3,024 crore during 2006-07.

Liquidity Management

The Reserve Bank continued with its policy of active management of liquidity during 2007-08 through appropriate use of the CRR and open market operations (OMO), including MSS and LAF and other policy instruments at its disposal flexibly. The objective was to maintain appropriate liquidity in the system such that all legitimate requirements of credit were met, consistent with the objective of price and financial stability. The liquidity management operations during 2007-08 had to contend with greater variations in market liquidity, on account of variations in cash balances of the Central Government and capital flows.

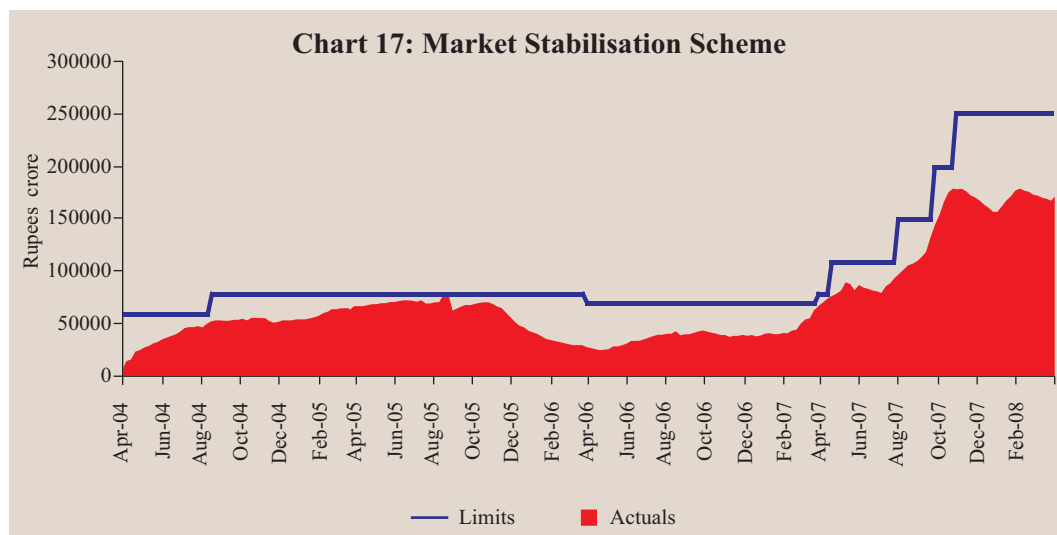


In the first quarter of 2007-08, liquidity conditions remained largely easy with transient periods of tightness (Table 31). Liquidity was modulated mainly through increase in CRR by 50 basis points in April 2007 and issuances of government securities under the MSS as and when required, as the liquidity absorption through reverse repos was capped at Rs.3,000 crore under the modified arrangement of LAF. The annual ceiling of MSS outstandings for 2007-08 was raised to Rs.1,10,000 crore on April 27, 2007 from Rs.80,000 crore (Chart 17). The Reserve Bank injected liquidity through LAF during the brief period of liquidity tightness from June 28-July 2, 2007.

In the second quarter, with the withdrawal of the ceiling on daily reverse repos under the LAF with effect from August 6, 2007, the sustained capital flows and the decline in Central Government balances were reflected in the Reserve Bank's absorption of large liquidity through reverse repos under LAF in addition to sizeable absorptions under the MSS. In view of the large and continuous capital flows, the ceiling of the MSS was again raised to Rs.1,50,000 crore in August 2007. The cumulative impact of the hike in the CRR by 50 basis points to 7.0 per cent in August 2007 and also market operations under the MSS moderated the daily absorption through reverse repos towards the close of the quarter. On account of quarterly advance tax outflow in mid-September, some

Table 31: Reserve Bank's Liquidity Management Operations

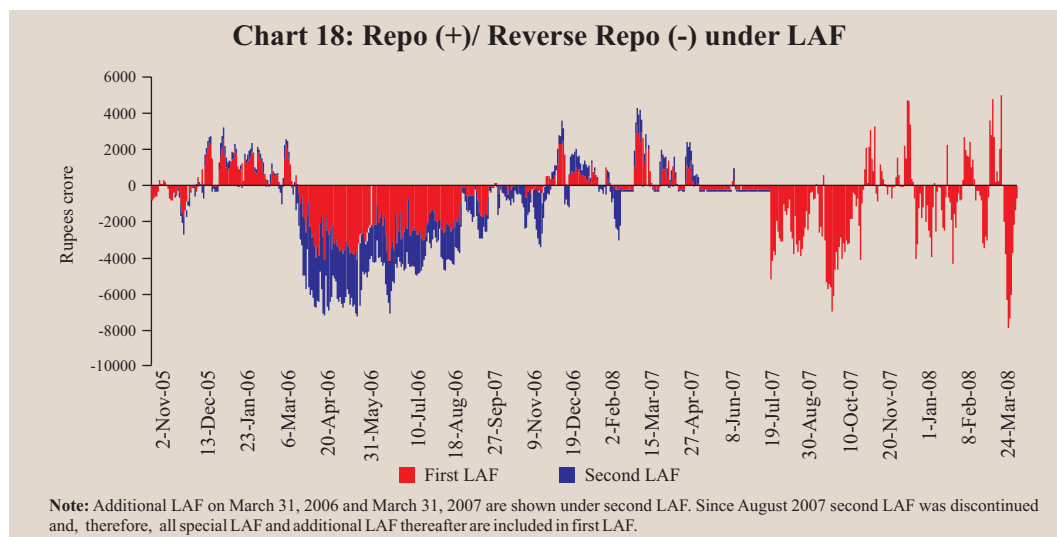
(Amount in Rupees Crore)									
Item			Variation						
	2006-07 (April - March)	2007-08 (April - February)	2007-08						
			Q1	Q2	Q3	Jan	Feb	March	
1	2	3	4	5	6	7	8	9	
A. Drivers of Liquidity (1+2+3+4+5)	62,278	2,11,440	51,146	1,10,891	-1,702	38,154	12,950		-
1. RBI's net Purchases from Authorised Dealers	1,18,994	3,00,875	39,791	1,00,896	88,545	47,554	24,089		-
2. Currency with the Public	-69,786	-71,353	-12,946	9,187	-47,139	-7,220	-13,233	-13,488	
3. Surplus Cash Balances of the Centre with the Reserve Bank	-1,164	-18,546	49,992	-30,771	-49,820	9,934	2,119	-8,048	
4. WMA and OD	0	0	15,159	-15,159	0	0	0	0	0
5. Others (residual)	14,234	463	-40,850	46,739	6,712	-12,114	-24	-	
B. Management of Liquidity (6+7+8+9)	-24,257	-1,85,361	-53,943	-68,621	-11,189	-39,112	-12,790	67,912	
6. Liquidity impact of LAF Repos	36,435	-37,270	-20,290	-2,825	27,795	-34,850	-7,100	58,435	
7. Liquidity impact of OMO (Net) *	720	10,730	10	40	5,260	2,760	2,660	2,780	
8. Liquidity impact of MSS	-33,912	-1,12,115	-18,163	-50,336	-28,244	-7,022	-8,350	6,697	
9. First round liquidity impact due to CRR change	-27,500	-47,000	-15,500	-15,500	-16,000	0	0	0	
C. Bank Reserves (A+B) #	38,021	25,785	-2,797	42,270	-12,891	-958	160	60,133	
- : Not Available	WMA : Ways and means advances		OD: Overdraft						
(+) : 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.									



tightness was observed during the end of the quarter and accordingly the Reserve Bank injected liquidity on two occasions through LAF.

Liquidity conditions eased at the beginning of the third quarter on account of a decline in surplus balances of the Central Government and Reserve Bank's foreign exchange operations. Notwithstanding brief periods of tightness on account of festive season currency demand, liquidity conditions remained easy up to November 2007, reflecting continued inflows of foreign capital. This necessitated upward revisions in the ceiling for outstandings under the MSS to Rs. 2,00,000 crore on October 4, 2007 and further to Rs. 2,50,000 crore on November 7, 2007. The CRR was also raised by 50 basis points to 7.5 per cent in November 2007. However, as the surplus cash balances of the Central Government increased, liquidity conditions tightened by the end of the month. The tightness in liquidity condition persisted in December 2007 largely on account of quarterly advance tax outflows. This necessitated injection of liquidity by the Reserve Bank through LAF (Chart 18).

Liquidity conditions in the last quarter of 2007-08 were driven mainly by variation in the Central Government's surplus cash balances and capital flows. Some easing of the liquidity condition was observed in the beginning of the quarter on account of reduction in the surplus cash balances of the Central Government and foreign exchange operations by the Reserve Bank in the wake of large capital flows over the period. Keeping in view the evolving liquidity conditions, auction of dated securities under the MSS was resumed in January 2008, after a gap of two-and-half months (Table 32). However, in the second-half of January 2008, surplus liquidity declined with the increase in Centre's cash balances with the Reserve Bank. The daily average net outstanding liquidity



absorption through LAF was Rs.15,692 crore during January 2008. During February 2008, the LAF window shifted from absorption to injection mode on account of further increase in surplus cash balances of the Central Government with the Reserve Bank. The average daily net outstanding liquidity injection was Rs. 1,294 crore in February 2008. In view of the prevailing liquidity conditions, no auction under the MSS was conducted from the middle of the month. The liquidity conditions eased in the beginning of March 2008 due to reduction in the surplus cash balances of the Centre and purchase of securities under the OMO² by the Reserve Bank. The absorption under the LAF was Rs. 30,335 crore as on March 13, 2008.

Liquidity conditions tightened from March 17, 2008 in view of advance tax outflows and concomitantly the Centre's surplus increased from Rs. 66,241 crore on March 14, 2008 to Rs. 1,03,645 crore on March 28, 2008. The Reserve Bank, in anticipation of the usual schedule of advance tax outflows and demand for funds at the end-of-the financial year, made additional arrangements for smoothening the liquidity and conducted (i) three-day repo/reverse repo auctions under additional LAF on March 14, 2008; (ii) seven-day repo auction under additional LAF on March 17, 2008; and (iii) two-day repo/reverse repo auctions under additional LAF on March 31, 2008. Reserve Bank injected Rs. 50,350 crore on March 31, 2008 through its LAF operation. The average daily net outstanding liquidity injection was Rs. 8,271 crore during March 2008.

² During 2007-08, the total amount of Government of India securities purchased under OMO was Rs. 13,510 crore. The OMO operations are liquidity neutral up to the amount of redemption of Government securities in the portfolio of the Reserve Bank.

Table 32: Liquidity Management

(Rupees crore)				
Outstanding as on Last Friday	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	18,135	1,74,277	23,735	2,16,147
November	-1,320	1,71,468	36,668	2,06,816
December	-33,865	1,59,717	80,591	2,06,443
2008				
January	985	1,66,739	70,657	2,38,381
February	8,085	1,75,089	68,538	2,51,712
March *	-50,350	1,68,392	76,586	1,94,628
April (up to April 18)	7,045	1,72,533	40,283	2,19,861

@ : 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. 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. Negative sign in column 4 indicates injection of liquidity through WMA/overdraft.

The liquidity conditions eased from the beginning of April 2008, mainly due to substantial reduction in cash balances of the Central Government. The auctions under the MSS have been resumed and the balances under MSS stand at Rs. 1,72,533 crore as on April 18, 2008. The absorption under LAF stands at Rs. 17,130 crore as on April 23, 2008.