

### III. MONETARY AND LIQUIDITY CONDITIONS

Monetary and liquidity aggregates continued to expand during the first quarter of 2008-09. Year-on-year (y-o-y) growth in broad money ( $M_3$ ) during 2008-09 so far (up to July 4, 2008) was above the indicative trajectory of 16.5-17.0 per cent set out in the Annual Policy Statement (APS) released in April 2008, notwithstanding some moderation mainly reflecting the decline in capital inflows during 2008-09 so far. Accretion to bank deposits, led by time deposits, remained strong, although the pace moderated. Expansion in bank credit to the commercial sector 2008-09 so far was above the Reserve Bank's policy projection of 20.0 per cent for 2008-09 as indicated in the APS (April 2008). Banks' investments in SLR securities as a proportion of their net demand and time liabilities (NDTL) remained almost at the same level as at end-March 2008. Large capital inflows that remained a key driver of monetary and liquidity conditions during 2007-08 have witnessed slowdown during 2008-09 so far. The Reserve Bank continued to actively manage liquidity by using all the policy instruments at its command, 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 placed at 20.5 per cent as on July 4, 2008 as compared with 21.8 per cent a year ago, reflecting the impact of some deceleration in time deposits. 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 lower at 20.8 per cent as on July 4, 2008 than 21.5 per cent a year ago. Growth in liquidity aggregate,  $L_1$ , at 20.3 per cent at end-June 2008 was marginally lower than that of 20.7 per cent a year ago (Table 22 and Chart 8).

In view of the continued underlying inflationary pressures, monetary policy recognised the need to smoothen and enable an adjustment of overall demand on an economy-wide basis so that inflation expectations were contained. Accordingly, the CRR was raised by 125 basis points in three phases during April-July 2008-09. The estimated amount of liquidity impounded in the first round on account of CRR hikes was Rs.48,000 crore<sup>1</sup>. Furthermore, the Reserve

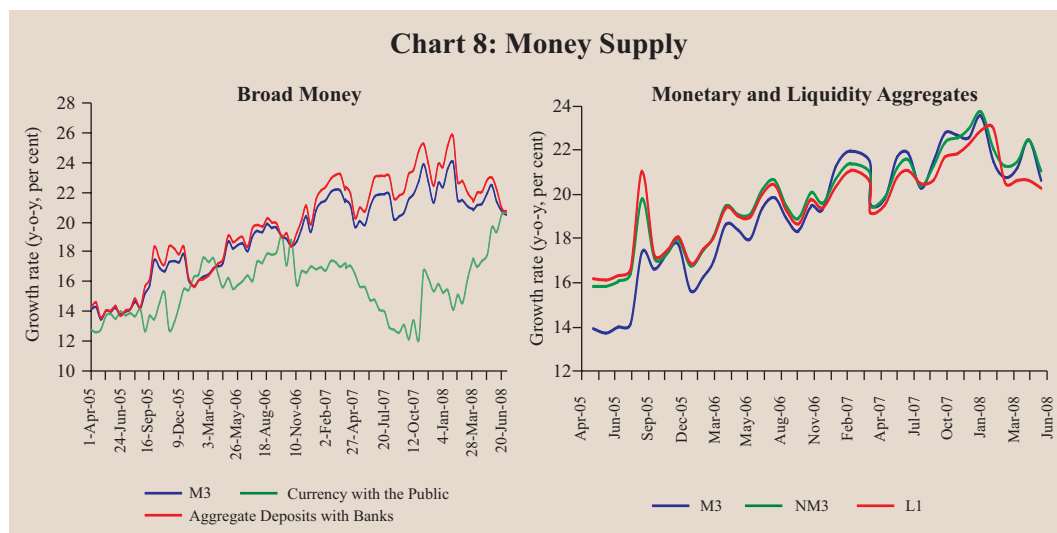
<sup>1</sup> Between December 2006 and July 2008, the Reserve Bank increased CRR by 375 basis points and the estimated amount of liquidity impounded in the first round due to hikes in the CRR was Rs. 1,22,500 crore.

**Table 22: Monetary Indicators**

(Amount in Rupees crore)							
Item	Outstanding as on July 4, 2008	Variation (year-on-year)					
		July 6, 2007		March 31, 2008		July 4, 2008	
		Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6	7	8
I. Reserve Money*	9,51,698	1,68,946	29.0	2,19,427	30.9	1,99,628	26.5
II. Narrow Money (M <sub>1</sub> )	11,24,308	1,38,122	16.9	1,84,864	19.1	1,69,327	17.7
III. Broad Money (M <sub>3</sub> )	41,46,197	6,17,118	21.8	6,90,629	20.8	7,04,046	20.5
a) Currency with the Public	6,00,675	61,336	14.0	84,571	17.5	1,02,483	20.6
b) Aggregate Deposits	35,40,593	5,50,653	23.1	6,04,485	21.4	6,07,668	20.7
i) Demand Deposits	5,18,704	71,658	19.2	98,721	20.8	72,948	16.4
ii) Time Deposits	30,21,889	4,78,996	23.9	5,05,765	21.5	5,34,720	21.5
of which: Non-Resident Foreign Currency Deposits	59,009	-548	-0.9	-10,525	-15.6	-4,135	-6.5
IV. NM <sub>3</sub>	41,66,159	6,10,463	21.5	7,08,101	21.3	7,17,186	20.8
of which : Call Term Funding from FIs	1,03,569	-1,853	-2.2	20,668	24.1	21,042	25.5
V. a) L <sub>1</sub>	42,26,766	6,03,635	20.7	7,07,012	20.6	7,14,009	20.3
of which: Postal Deposits	1,14,460	9,402	8.8	-1,089	-0.9	-2,113	-1.8
b) L <sub>2</sub>	42,29,698	6,03,635	20.7	7,07,012	20.4	7,14,009	20.3
c) L <sub>3</sub>	42,55,666	6,06,631	20.7	7,08,284	20.4	7,14,358	20.2
VI. Major Sources of Broad Money							
a) Net Bank Credit to the Government (i+ii)	9,51,475	1,08,683	13.4	72,842	8.7	34,077	3.7
i) Net Reserve Bank Credit to Government	-1,09,022	30,358	-	-1,15,632	-	-1,37,189	-
of which : to the Centre	-1,08,981	30,191	-	-1,16,772	-	-1,36,827	-
ii) Other Banks' Credit to Government	10,60,498	78,325	9.7	1,88,474	22.7	1,71,266	19.3
b) Bank Credit to the Commercial Sector	26,27,205	3,90,915	22.6	4,39,834	20.6	5,07,929	24.0
c) Net Foreign Exchange Assets	13,89,047	1,10,515	14.0	3,81,952	41.8	4,89,695	54.4
d) Government Currency Liability to Public	9,486	593	7.6	1,064	12.9	1,059	12.6
e) Net Non-Monetary Liabilities of the Banking Sector	8,31,016	-6,412	-1.3	2,05,063	36.0	3,28,714	65.4
<b>Memo:</b>							
Aggregate Deposits of SCBs	33,08,225	5,36,617	24.6	5,85,006	22.4	589,646	21.7
Non-food Credit of SCBs	23,57,859	3,69,109	24.6	4,32,846	23.0	485,709	25.9
*: Data pertain to July 18, 2008.							
SCBs: Scheduled Commercial Banks. FIs: Financial Institutions. NBFCs: Non-Banking Financial Companies.							
NM <sub>3</sub> is the residency-based broad money aggregate and L <sub>1</sub> , L <sub>2</sub> and L <sub>3</sub> are liquidity aggregates compiled on the recommendations of the Working Group on Money Supply (Chairman: Dr. Y.V. Reddy, 1998).							
L <sub>1</sub> = NM <sub>3</sub> + Select deposits with the post office saving banks.							
L <sub>2</sub> = L <sub>1</sub> + Term deposits with term lending institutions and refinancing institutions + Term borrowing by FIs + Certificates of deposit issued by FIs.							
L <sub>3</sub> = L <sub>2</sub> + Public deposits of NBFCs.							
<b>Note:</b> 1. Data are provisional. Wherever data are not available, for estimates the available data for latest month have been repeated.							
2. Liquidity aggregates pertain to end-June 2008.							

Bank increased the repo rate first by 25 basis points and then by another 50 basis points to 8.5 per cent effective from June 12 and June 25, 2008, respectively.

Currency with the public grew by 20.6 per cent (y-o-y) as on July 4, 2008 as compared with 14.0 per cent a year ago. Growth in demand deposits (y-o-y) as on July 4, 2008 at 16.4 per cent was lower than that of 19.2 per cent a year



ago. Accordingly, narrow money growth ( $M_1$ ), y-o-y, was 17.7 per cent as on July 4, 2008 as compared with 16.9 per cent a year ago. The growth of time deposits was placed at 21.5 per cent (y-o-y) as on July 4, 2008 as compared with 23.9 per cent a year ago. 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 postal deposits decelerated significantly up to November 2007. Beginning December 2007 there were net outflow from small saving schemes (Chart 9). In order to revive interest in postal deposits, the Government announced in December 2007 some incentives, including tax benefits for certain postal deposits. However, net outflows continued up to March 2008, the latest period for which the data are available.

On a financial year basis, growth in  $M_3$  during 2008-09 (up to July 4, 2008) was 3.5 per cent as compared with 3.8 per cent during the corresponding period of the previous year. Currency with the public expanded by 5.9 per cent (up to July 4, 2008) as compared with 3.2 per cent during the corresponding previous period (Table 23).

Expansion in the bank credit to the commercial sector increased by 24.0 per cent (y-o-y) as on July 4, 2008, as compared with 22.6 per cent a year ago. Non-food credit by scheduled commercial banks (SCBs) expanded by 25.9 per cent, y-o-y, as on July 4, 2008, higher than 24.6 per cent a year ago. The higher

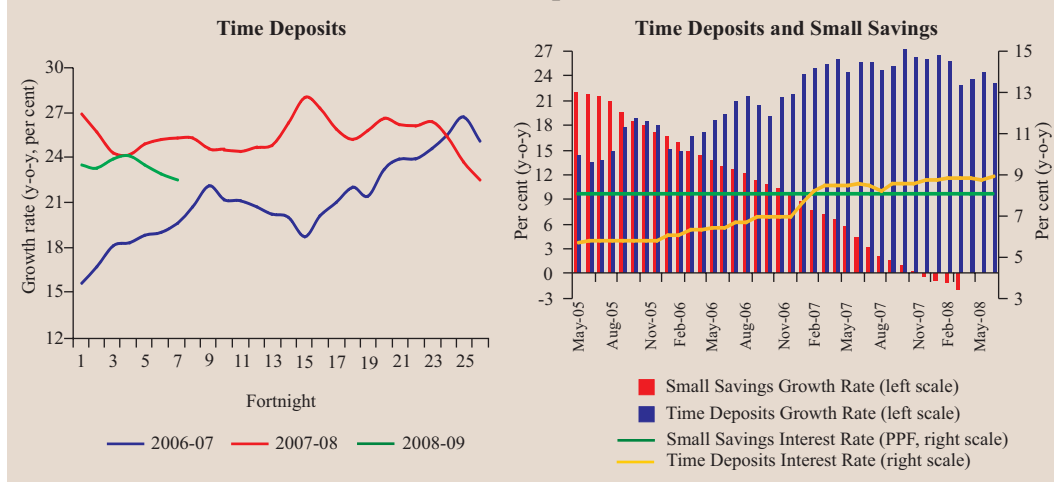
**Table 23: Monetary Aggregates - Variations**

(Rupees Crore)							
Item	2007-08 (up to July 6)	2008-09 (up to July 4)	2007-08			2008-09	
			Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6	7	8
<b>M<sub>3</sub> (1+2+3 = 4+5+6+7-8)</b>	<b>1,26,058 (3.8)</b>	<b>1,39,475 (3.5)</b>	<b>73,824</b>	<b>1,99,109</b>	<b>1,09,807</b>	<b>3,07,889</b>	<b>84,387</b>
<b>Components</b>							
1. Currency with the Public	15,287 (3.2)	33,199 (5.9)	18,237	-14,756	48,013	33,076	36,481
2. Aggregates Deposits with Banks	1,07,234 (3.8)	1,10,416 (3.2)	56,023	2,15,344	62,600	2,70,519	52,214
2.1 Demand Deposits with Banks	-29,931 (-6.3)	-55,704 (-9.7)	-44,030	58,180	-6,878	91,449	-78,171
2.2 Time Deposits with Banks	1,37,165 (5.8)	1,66,120 (5.8)	1,00,053	1,57,164	69,478	1,79,070	1,30,385
3. 'Other' Deposits with Banks	3,537	-4,141	-436	-1,479	-806	4,294	-4,308
<b>Sources</b>							
4. Net Bank Credit to Government	83,163 (10.0)	44,399 (4.9)	28,117	15,618	-35,538	64,646	32,597
4.1 RBI's Net Credit to Government	25,744	4,187	-22,154	-54,695	-65,787	27,004	-13
4.1.1 RBI's Net credit to the Centre	25,711	5,655	-21,825	-55,588	-65,078	25,719	1,430
4.2 Other Banks' Credit to Government	57,419	40,212	50,270	70,313	30,249	37,642	32,610
5. Bank Credit to the Commercial Sector	-10,802 (-0.5)	57,293 (2.2)	-30,547	1,45,442	82,172	2,42,767	42,252
6. NFEA of Banking Sector	-13,827	93,915	-17,945	1,18,249	94,204	1,87,444	1,03,932
6.1 NFEA of the RBI	1,373	93,915	-2,745	1,19,430	94,681	1,58,610	1,03,932
7. Government's Currency Liabilities to the Public	166	161	166	354	312	232	161
8. Net Non-Monetary liabilities of the Banking Sector	-67,358	56,293	-94,033	80,553	31,343	1,87,200	94,555
<b>Memo:</b>							
1. Non-resident Foreign Currency Deposits with SCBs	-4,317	2,074	-4,202	-1,181	-3,490	-1,653	1,789
2. SCB' Call-term Borrowing from Financial Institutions	-3,309	-2,936	-2,984	5,756	7,441	10,455	-1,664
3. Overseas Borrowing by SCBs	-6,672	3,477	-6,928	7,830	1,734	9,909	9,747
SCBs: Scheduled Commercial Banks. NFEA: Net Foreign Exchange Assets.							
<b>Note:</b> 1. Data are provisional.							
2. Figures in parentheses are percentage variations.							

expansion in credit growth relating to the expansion in deposit growth resulted in an increase in the incremental credit-deposit ratio (y-o-y) of SCBs to 83.5 per cent as on July 4, 2008 from 70.0 per cent a year ago (Chart 10).

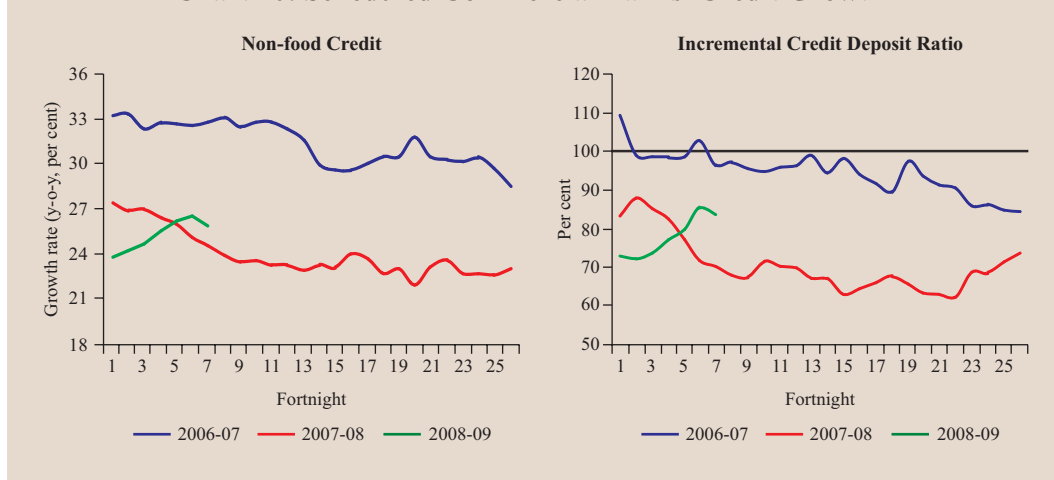
Disaggregated sectoral data available up to May 23, 2008 showed that about 43 per cent of incremental non-food credit (y-o-y) was absorbed by industry as compared with 39 per cent in the corresponding period of the previous year. The expansion of incremental non-food credit to industry during this period was led by infrastructure (power, port and telecommunication), petroleum, textiles,

Chart 9: Time Deposits Growth



iron and steel, food processing, chemicals, engineering, vehicles and construction industries. The infrastructure sector alone accounted for 33 per cent of the incremental credit to industry as compared with 25 per cent in the corresponding period of the previous year. The agricultural sector absorbed around 10 per cent of the incremental non-food bank credit expansion as compared with 15 per cent in the corresponding period of the previous year. Personal loans accounted for nearly 17 per cent of incremental non-food credit; within personal loans, the share of incremental housing loans was at 44 per cent. Growth in loans to commercial real estate remained high, notwithstanding moderation (Table 24).

Chart 10: Scheduled Commercial Banks' Credit Growth



**Table 24: Non-food Bank Credit - Sectoral Deployment**

(Amount in Rupees Crore)					
Sector/Industry	Outstanding as on May 23, 2008	Year-on-Year Variations			
		May 25, 2007		May 23, 2008	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
<b>Non-food Gross Bank Credit (1 to 4)</b>	<b>21,74,767</b>	<b>3,65,814</b>	<b>26.4</b>	<b>4,22,418</b>	<b>24.1</b>
<b>1. Agriculture and Allied Activities</b>	<b>2,64,787</b>	<b>54,038</b>	<b>32.2</b>	<b>42,745</b>	<b>19.3</b>
<b>2. Industry (Small, Medium and Large)</b>	<b>8,58,515</b>	<b>1,41,280</b>	<b>26.4</b>	<b>1,82,075</b>	<b>26.9</b>
Small Scale Industries	1,76,282	26,387	29.5	60,398	52.1
<b>3. Personal Loans</b>	<b>5,28,046</b>	<b>87,944</b>	<b>23.9</b>	<b>72,607</b>	<b>15.9</b>
Housing	2,62,486	41,066	21.6	31,735	13.8
Advances against Fixed Deposits	42,220	6,237	19.0	3,128	8.0
Credit Cards	26,596	4,411	45.0	12,375	87.0
Education	21,352	4,903	46.5	5,914	38.3
Consumer Durables	8,297	1,661	23.2	-534	-6.0
<b>4. Services</b>	<b>5,23,249</b>	<b>82,551</b>	<b>26.1</b>	<b>1,24,821</b>	<b>31.3</b>
Transport Operators	35,248	7,922	45.5	9,927	39.2
Professional & Other Services	31,942	8,999	56.8	7,108	28.6
Trade	1,22,438	23,319	28.4	16,902	16.0
Real Estate Loans	61,045	19,010	69.7	14,750	31.9
Non-Banking Financial Companies	71,974	12,401	38.7	27,549	62.0
<i>Memo:</i>					
<b>Priority Sector</b>	<b>7,39,964</b>	<b>1,20,463</b>	<b>23.9</b>	<b>1,14,666</b>	<b>18.3</b>
Industry (Small, Medium and Large)	8,58,515	1,41,280	26.4	1,82,075	26.9
Food Processing	50,493	6,758	22.1	13,126	35.1
Textiles	93,916	19,223	32.9	16,259	20.9
Paper & Paper Products	13,826	2,243	24.5	2,435	21.4
Petroleum, Coal Products & Nuclear Fuels	47,289	9,884	51.6	18,250	62.8
Chemicals and Chemical Products	65,397	6,511	14.2	12,982	24.8
Rubber, Plastic & their Products	11,116	1,938	28.0	2,261	25.5
Iron and Steel	78,834	13,554	27.2	15,460	24.4
Other Metal & Metal Products	25,112	5,447	36.3	4,658	22.8
Engineering	52,551	8,553	25.1	9,959	23.4
Vehicles, Vehicle Parts and Transport Equipments	30,015	5,267	28.6	6,324	26.7
Gems & Jewellery	24,826	2,572	12.3	1,403	6.0
Construction	26,082	6,632	49.2	5,959	29.6
Infrastructure	2,03,331	35,292	32.6	59,811	41.7
<b>Note:</b> 1. Data are provisional and relate to select scheduled commercial banks.					
2. Data also include the figures of Bharat Overseas Bank, which was merged with Indian Overseas Bank on March 31, 2007.					

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 the first quarter of 2008-09 (Rs.2,031 crore) were significantly lower than those in the corresponding period of the previous year mainly reflecting the decline in investor optimism in the secondary equity market. Net mobilisation through external commercial borrowings (ECBs) during 2007-08 increased by 54 per cent over the preceding year. Mobilisation through issuances of commercial paper (CPs) during April-June 2008-09 was 66 per cent higher than that during the corresponding period of the

previous year. Resources raised in the form of equity issuances through American depository receipts (ADRs) and global depository receipts (GDRs) during April-June 2008-09 (Rs.4,056 crore) were more than three times than those during the corresponding period of the previous year. Internal generation of funds continued to provide a strong support to the funding requirements of the corporate sector, despite the profit after tax of select non-financial non-government companies during 2007-08 witnessing some deceleration in comparison with the previous year (Table 25 and Table 12).

Scheduled commercial banks' investment in SLR securities expanded by 19.6 per cent (y-o-y) as on July 4, 2008, as compared with 10.4 per cent a year ago. The higher growth in investment in SLR securities mainly reflected the need to maintain SLR requirements in consonance with the increase in their net demand and time liabilities (Table 26). Commercial banks' holdings of such securities as on July 4, 2008 were 27.7 per cent of their NDTL as compared with

**Table 25: Select Sources of Funds to Industry**

Item	(Rupees Crore)						
	2006-07	2007-08	2007-08				2008-09
			Q1	Q2	Q3	Q4	
1	2	3	4	5	6	7	8
A. Bank Credit to Industry #	1,41,543	1,74,566	-15,603	59,776	40,993	89,400	-13,385 ^
B. Flow from Non-banks to Corporates							
1 Capital Issues (i+ii)	29,178	51,479	13,788	6,226	14,400	17,065	2,031
i) Non-Government Public Ltd. Companies (a+b)	29,178	48,962	13,261	4,236	14,400	17,065	2,031
a) Bonds/Debentures	585	809	0	0	0	809	0
b) Shares	28,593	48,153	13,261	4,236	14,400	16,256	2,031
ii) PSUs and Government Companies	0	2,517	527	1,990	0	0	0
2 ADR/GDR Issues	16,184	13,023	1,251	9,899	289	1,584	4,056
3 External Commercial Borrowings (ECBs)	1,04,046	1,60,221	35,993	36,755	43,093	44,380	-
4 Issue of CPs	5,145	14,903	8,568	7,358	6,629	-7,651	14,256
C. Depreciation Provision +	37,095	38,528 *	10,173	10,576	10,961	11,805	-
D. Profit after Tax +	1,11,107	1,27,968 *	32,699	34,266	37,470	36,109	-
- : Not Available.                      ^ : Up to May 23, 2008.                      * : Provisional. # : 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).							
<b>Note :</b> 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.							

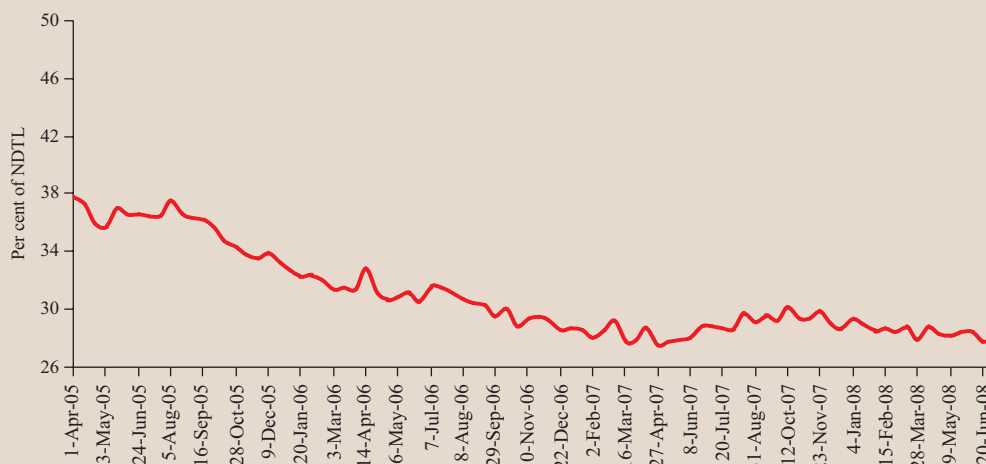
**Table 26: Scheduled Commercial Bank Survey**

Item	Outstanding as on July 4, 2008	(Amount in Rupees Crore)			
		Variation (Year-on-Year)			
		As on July 6, 2007		As on July 4, 2008	
		Amount	Per Cent	Amount	Per Cent
1	2	3	4	5	6
<b>Sources of Funds</b>					
1. Aggregate Deposits	33,08,225	5,36,617	24.6	5,89,646	21.7
2. Call/Term Funding from Financial Institutions	1,03,569	-1,853	-2.2	21,042	25.5
3. Overseas Foreign Currency Borrowings	47,928	-5,867	-18.9	22,696	89.9
4. Capital	44,424	6,927	23.9	8,541	23.8
5. Reserves	2,74,089	50,943	31.4	60,902	28.6
<b>Uses of Funds</b>					
1. Bank Credit	24,08,579	3,75,483	24.4	4,92,202	25.7
of which: Non-food Credit	23,57,859	3,69,109	24.6	4,85,709	25.9
2. Investments in Government and Other Approved Securities	1,0,15,382	79,938	10.4	1,66,213	19.6
a) Investments in Government Securities	9,96,627	81,310	10.8	1,62,475	19.5
b) Investments in Other Approved Securities*	18,755	-1,372	-8.4	3,738	24.9
3. Investments in non-SLR Securities	1,71,382	23,445	15.6	-2,718	-1.6
4. Foreign Currency Assets	34,364	30,356	93.0	-28,636	-45.5
5. Balances with the RBI	2,69,482	83,877	72.5	69,889	35.0

\* : 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.

27.8 per cent at end-March 2008 and 28.7 per cent a year ago (Chart 11). Excess SLR investments of SCBs increased to Rs.99,238 crore as on July 4, 2008 from Rs. 98,033 crore at end-March 2008; excess investments in SLR securities were

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

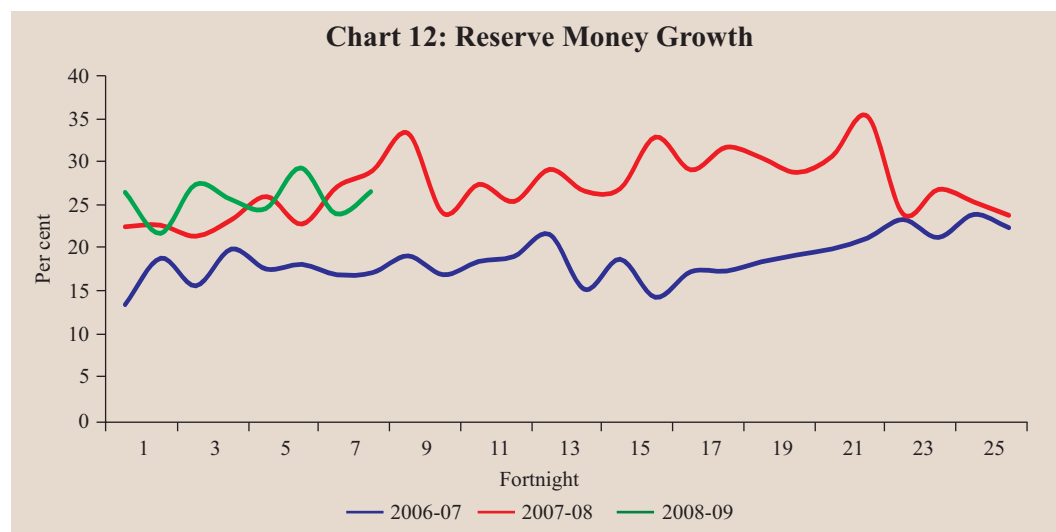


Rs.1,09,366 crore a year ago. Banks' overseas foreign currency borrowings accelerated. Banks also drew down their holdings of foreign currency assets.

### Reserve Money Survey

Reserve money growth at 26.5 per cent, y-o-y, as on July 18, 2008 was lower than that of 29.0 per cent a year ago (Chart 12). Adjusted for the first round effect of the hike in CRR, reserve money growth at 18.4 per cent was lower than 21.6 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.

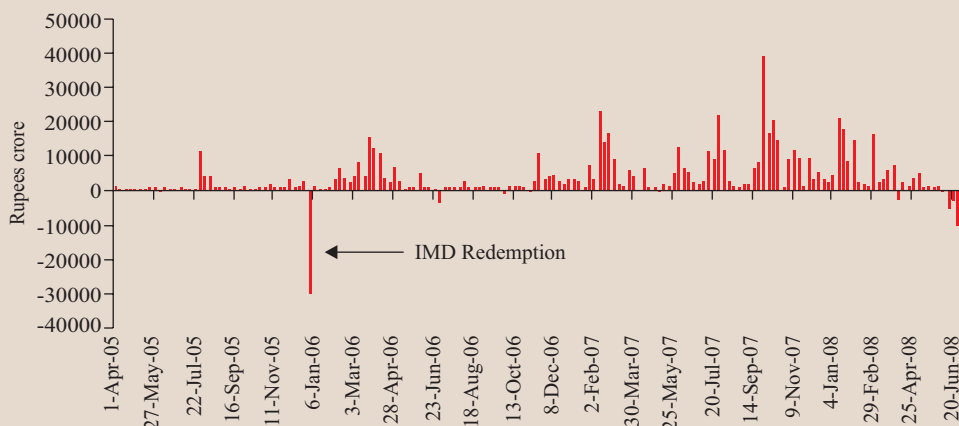
During the financial year 2008-09 (up to July 18, 2008), reserve money grew by 2.5 per cent as compared with an increase of 6.1 per cent in the corresponding period of the previous year. Bankers' deposits with the Reserve Bank decreased by 2.3 per cent (up to July 18, 2008) as against an increase of 14.0 per cent in the corresponding period of 2007-08. Currency in circulation expanded by 5.9 per cent as compared with 2.1 per cent during the corresponding period of the previous year (Table 27). On the sources side, net Reserve Bank's credit to Government increased by Rs. 54,113 crore (up to July 18, 2008) as compared with an increase of Rs. 19,461 crore in the corresponding period of 2007-08. The Reserve Bank's foreign currency assets (adjusted for revaluations) declined by Rs. 18,139 crore as against an increase of Rs. 72,947 crore during the corresponding period of the previous year (Chart 13).



**Table 27 : Reserve Money - Variations**

(Amount in Rupees crore)								
Item	2007-08 (April- March)	2007-08 (Up to July 20)	2008-09 ( Up to July 18)	2007-08				2008-09
				Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6	7	8	9
<b>Reserve Money</b>	<b>2,19,427</b>	<b>43,080</b>	<b>23,281</b>	<b>11,630</b>	<b>60,688</b>	<b>26,606</b>	<b>1,20,503</b>	<b>3,155</b>
<b>Components (1+2+3)</b>								
1. Currency in Circulation	86,702	10,539	34,915	16,866	-13,297	46,781	36,352	36,795
		(2.1)	(5.9)					
2. Bankers' Deposits with RBI	1,31,152	27,685	-7,481	-4,800	75,464	-19,369	79,857	-29,333
		(14.0)	(-2.3)					
3. 'Other' Deposits with the RBI	1,573	4,855	-4,153	-436	-1,479	-806	4,294	-4,308
		(64.8)	(-45.8)					
<b>Sources (1+2+3+4-5)</b>								
1. RBI's net credit to Government	-1,15,632	19,461	54,113	-22,154	-54,695	-65,787	27,004	-13
of which: to Centre (i+ii+iii+iv-v)	-1,16,772	18,875	55,581	-21,825	-55,588	-65,078	25,719	1,430
i. Loans and Advances	0	30,058	0	0	0	0	0	0
ii. Treasury Bills held by the RBI	0	0	0	0	0	0	0	0
iii. RBI's Holdings of Dated Securities	17,421	-21,182	-2,172	-34,284	4,019	20,874	26,812	-39,239
iv. RBI's Holdings of Rupee Coins	121	79	-68	128	20	3	-31	-1
v. Central Government Deposits	1,34,314	-9,921	-57,821	-12,330	59,627	85,956	1,062	-40,670
2. RBI's Credit to Banks and Commercial Sector	-2,794	-7,778	-873	-6,450	-1,256	848	4,064	-3,358
3. NFEA of RBI	3,69,977	27,735	75,552	-2,745	1,19,430	94,681	1,58,610	1,03,932
		(3.2)	(6.1)					
of which :								
FCA, adjusted for revaluation	3,70,550	72,947	-18,139	47,728	1,18,074	1,00,888	1,03,860	15,535
4. Governments' Currency Liabilities to the Public	1,064	330	161	166	354	312	232	161
5. Net Non-Monetary liabilities of RBI	33,187	-3,333	1,05,673	-42,812	3,145	3,448	69,406	97,567
<b>Memo:</b>								
LAF- Repos (+) / Reverse Repos (-)	21,165	-32,185	-16,025	-32,182	9,067	16,300	27,980	-45,350
Net Open Market Sales # *	-5,923	1,910	-18,183	1,246	1,560	-3,919	-4,810	-8,696
Centre's Surplus **	26,594	-49,992	-56,919	-34,597	15,376	54,765	-8,950	-42,427
Mobilisation under the MSS	1,05,419	22,053	3,047	19,643	48,855	31,192	5,728	6,040
Net Purchases(+)/Sales(-) from Authorised Dealers	3,12,054	60,824	17,356 ^	38,873	1,01,814	87,596	83,771	17,356 ^
NFEA/Reserve Money @	133.1	118.9	137.8	119.8	125.8	133.4	133.1	143.8
NFEA/Currency @	209.2	173.7	209.6	165.7	193.6	194.3	209.2	213.5
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 May 30, 2008.								
** : Excludes minimum cash balances in case of surplus.								
<b>Note:</b> 1. Data are based on March 31 for Q4 and last reporting Friday for all other quarters.								
2. Figures in parentheses are percentage variations during the fiscal year.								

Movements in the Reserve Bank's net credit to the Central Government during 2008-09 so far (up to July 18, 2008) largely reflected the liquidity management operations by the Reserve Bank and movements in Government deposits with the Reserve Bank. Surplus cash balances of the Central Government with the Reserve Bank declined. The Reserve Bank's holdings of Central Government dated securities decreased reflecting Reserve Bank's special market operation (SMO) and LAF operations. The sterilisation operations of the Reserve Bank under the MSS led to an increase in Central Government deposits

**Chart 13: Accretion to RBI's Net Foreign Assets**

with the Reserve Bank. Reflecting these developments, the Reserve Bank's net credit to the Centre increased by Rs.55,581 crore during 2008-09 so far (up to July 18, 2008) as compared with an increase of Rs. 18,875 crore during the corresponding period of the previous year.

### Liquidity Management

The Reserve Bank continued with its policy of active management of liquidity in 2008-09 through appropriate use of the CRR and OMO, including MSS and LAF, and other policy instruments at its command flexibly. The objective is to maintain appropriate liquidity in the system such that all legitimate requirements of credit are met, consistent with the objective of price and financial stability. During 2008-09 so far variations in cash balances of the Central Government, hikes in the CRR and the Reserve Bank's foreign exchange operations remained the key drivers of liquidity conditions.

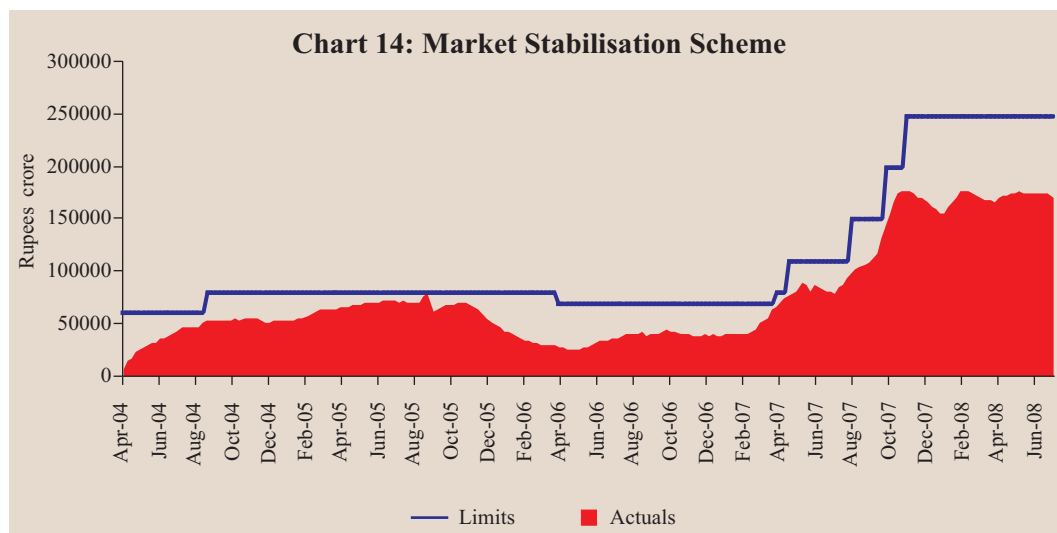
Liquidity conditions turned easy after the commencement of 2008-09 mainly due to substantial reduction in the cash balances of the Central Government (Table 28). On a review of the liquidity situation, the Reserve Bank announced on April 17, 2008, a two-stage hike of CRR by 25 basis points each to 8.0 per cent, effective from the fortnights beginning from April 26, 2008 and May 10, 2008, respectively. Auctions under the MSS (which were kept in abeyance since mid-February) were resumed on April 9, 2008 and the balances under the MSS increased to Rs.1,72,444 crore as on April 25, 2008. The daily average net liquidity absorption through the LAF was Rs.26,359 crore during

**Table 28: Reserve Bank's Liquidity Management Operations**

(Rupees Crore)							
Item	2007-08	2007-08				2008-09	
		Q1	Q2	Q3	Q4	April	May
1	2	3	4	5	6	7	8
<b>A. Drivers of Liquidity (1+2+3+4+5)</b>	<b>2,04,026</b>	<b>51,146</b>	<b>1,11,169</b>	<b>-1,984</b>	<b>43,695</b>	<b>27,083</b>	<b>17,989</b>
1. RBI's net purchases from Authorised Dealers	3,12,054	39,791	1,00,896	88,545	82,822	11,469	5,887
2. Currency with the Public	-84,571	-12,946	9,465	-47,422	-33,667	-22,196	-10,250
3. Surplus cash balances of the Centre with the Reserve Bank @	-26,594	49,992	-30,771	-49,820	4,005	40,037	19,447
4. WMA and OD	0	15,159	-15,159	0	0	0	0
5. Others (residual)	3,137	-40,850	46,739	6,712	-9,465	-2,227	2,905
<b>B. Management of Liquidity (6+7+8+9)</b>	<b>-1,17,743</b>	<b>-53,943</b>	<b>-68,621</b>	<b>-11,189</b>	<b>16,010</b>	<b>-86,427</b>	<b>21,080</b>
6. Liquidity impact of LAF Repos	21,165	-20,290	-2,825	27,795	16,485	-83,115	42,365
7. Liquidity impact of OMO (Net) *	13,510	10	40	5,260	8,200	740	133
8. Liquidity impact of MSS	-1,05,419	-18,163	-50,336	-28,244	-8,675	-4,052	-2,918
9. First round liquidity impact due to CRR change	-47,000	-15,500	-15,500	-16,000	0	0	-18,500
<b>C. Bank Reserves (A+B) #</b>	<b>86,283</b>	<b>-2,797</b>	<b>42,548</b>	<b>-13,173</b>	<b>59,705</b>	<b>-59,344</b>	<b>39,069</b>
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).							
@ : Excludes minimum cash balances in case of surplus.							
<b>Note:</b> Data pertain to March 31 and last Friday for all other months.							

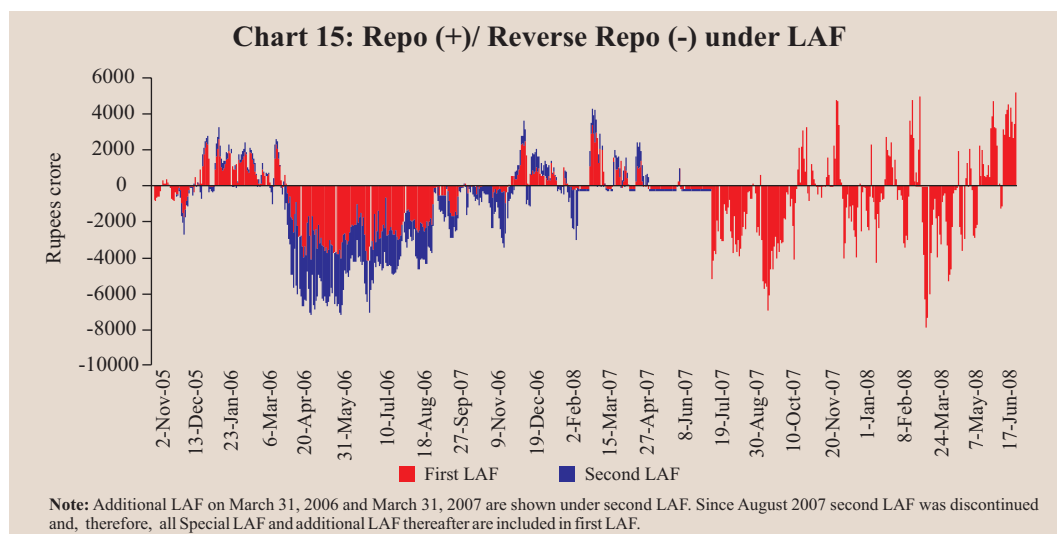
April 2008. On a review of the evolving liquidity situation, the Annual Monetary Policy Statement issued on April 29, 2008, announced an increase in CRR by 25 basis points to 8.25 per cent with effect from the fortnight beginning May 24, 2008. Reflecting the impact of the CRR hikes, average daily net absorption through LAF declined to Rs.11,841 crore during May 2008. No auction of dated securities under the MSS was conducted during May 2008 and the outstanding balance under the MSS was placed at Rs.1,75,362 crore on May 30, 2008 (Chart 14).

Liquidity conditions eased in the early part of June and the average daily net absorption under the LAF was placed at Rs.15,469 crore during June 1-9, 2008. On a review of the prevailing macroeconomic and overall monetary conditions and with a view to containing inflationary expectations, the Reserve Bank increased the repo rate under the LAF by 25 basis points to 8 per cent with effect from June 12, 2008. Subsequently, with the build-up in Central Government balances in the face of advance tax collections, liquidity conditions turned into a deficit mode and the average daily net injection under LAF during June 10-27, 2008 was Rs.17,288 crore (Chart 15). With a view to containing demand pressures, as reflected in the increase in inflation and inflationary expectations, engendered by unrelenting pressures from international commodity prices, particularly crude and metals, the Reserve Bank increased the repo rate under LAF by 50 basis points to 8.5 per cent with effect from June 25, 2008 and also increased the CRR by 50 basis points to 8.75 per cent in two stages (25 basis



points each) with effect from the fortnights beginning July 5 and July 19, 2008, respectively. No MSS auction was conducted during June 2008 and the outstanding balance as on June 27, 2008, was placed at Rs.1,74,433 crore (Table 29). The average daily net injection through the LAF during June was Rs. 8,622 crore.

Liquidity conditions eased during the first week of July mainly on account of a decline in the cash balances of the Central Government but tightened significantly thereafter mainly due to two stage hike in CRR announced in the previous month. The average liquidity injection during July 1-18, 2008 was at Rs. 23,421 crore.



**Table 29: 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
<b>2007</b>				
January	-11,445	39,375	42,494	70,424
February	6,940	42,807	53,115	1,02,862
March *	-29,185	62,974	49,992	83,781
April	-9,996	75,924	-980	64,948
May	-4,690	87,319	-7,753	74,876
June	-8,895	81,137	-15,159	57,083
July	2992	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
<b>2008</b>				
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	32,765	1,72,444	36,549	2,41,758
May	-9,600	1,75,362	17,102	1,82,864
June	-32,090	1,74,433	36,513	1,78,856
July (up to 18)	-34,325	1,71,440	19,667	1,56,782

@: 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. The Second LAF was discontinued from August 6, 2007.

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

Keeping in view the systemic implications of liquidity and other related issues currently faced by public sector oil marketing companies (OMCs) arising from the unprecedented escalation in international crude oil prices, the Reserve Bank announced Special Market Operation (SMO) on May 30, 2008, for the smooth functioning of financial markets and for overall financial stability. Under SMO, the Reserve Bank conducts open market operation (outright or repo at its discretion) in the secondary market through designated banks in oil bonds held by public sector OMCs in their own accounts, subject to an overall ceiling of Rs.1,500 crore (revised upwards from Rs.1,000 crore on June 11, 2008) on any single day, and provides equivalent foreign exchange through designated banks at market exchange rate to the oil companies. The settlement of the foreign exchange and the Government securities legs of the operations are synchronised so that there is no liquidity impact on account of these operations. These operations are ad hoc, temporary in nature and subject to review on a continuous basis. These operations commenced from June 5, 2008. The oil bonds purchased by the Reserve Bank under SMO up to July 11, 2008 aggregated Rs. 17,655 crore (face value).