RESERVE BANK OF INDIA

Macroeconomic and Monetary Developments in 2008-09

Issued with the Annual Policy Statement 2009-10

April 20, 2009

Macroeconomic and Monetary Developments in 2008-09

Reserve Bank of India
Mumbai

Contents

MACROECONOMIC AND MONETARY DEVELOPMENTS in 2008-09

Overview

The global economic conditions deteriorated sharply during the year 2008 with several advanced economies experiencing their sharpest declines in the post-World War II period. The associated adverse shocks spreading across emerging market economies (EMEs) particularly by the fourth quarter of the year, accentuated the synchronised global slowdown. The global inflation conditions witnessed sharp volatility during the year as headline inflation in major advanced economies firmed up considerably up to July 2008 but fell sharply thereafter. The global financial environment entered a crisis phase in mid-September 2008, following the growing distress among large international financial institutions and the declaration of bankruptcy of Lehman Brothers. As credit markets froze, central banks across the world, along with the respective governments, responded with both conventional and unconventional measures. The knock-on effect of these unprecedented adverse global developments became evident in the macroeconomic performance of the Indian economy, particularly in the second half of 2008-09.

The Indian economy, which was on a robust growth path up to 2007-08, averaging at 8.9 per cent during the period 2003-04 to 2007-08, witnessed moderation in 2008-09, with the deceleration turning out to be somewhat sharper in the third quarter. While the growth deceleration was primarily driven by the knock on effects of the global economic crisis, it also reflected to some extent the slowdown associated with cyclical factors. Industrial growth experienced a significant downturn and the loss of growth momentum was evident in all categories, viz., the basic, capital, intermediate and consumer goods. A hitherto key growth driver, services sector, witnessed some moderation, notwithstanding a counter-cyclical rise in the growth of community, social and personal services on the back of implementation of the Sixth Pay Commission recommendations. Although agriculture also recorded a deceleration in growth, the agricultural outlook remains satisfactory, with the sowing in the rabi season being higher than that in the previous year.

The slowdown in the Indian economy during 2008-09 has been associated with a deceleration in investment demand, which had been an important driver of growth in recent years. The adverse conditions for access to external capital, and the depressing effects of the global crisis on domestic business confidence contributed to the moderation in investment demand. The deceleration in private consumption expenditure was partly offset by a sharp increase in

Government consumption expenditure during the third quarter emanating from the discretionary fiscal stimulus measures and committed expenditures. The key deficit indicators of the Central Government, viz., the revenue deficit and the gross fiscal deficit as per the revised estimates for 2008-09 were, therefore, significantly higher than the budgeted level as well as those of the preceding year. *Implementing the fiscal stimulus packages required the Government to defer the attainment of the stipulated deficit targets under the Fiscal Responsibility and Budget Management (FRBM) Act, 2003. Corporate performance remained subdued during the year, with the impact on profitability being particularly adverse during the third quarter, when growth in sales, which had been strong in earlier quarters, also decelerated. External demand conditions weakened, particularly since October 2008, with the decline in exports resulting in a sharp widening of the merchandise trade deficit during April 2008-February 2009. Saving and investment rates, which had peaked in 2007-08, are likely to be affected adversely by the slowdown in economic growth during 2008-09.*

The balance of payments (BoP) developments during April-December 2008 reflected the impact of shocks emanating from the global economy through both trade and financial channels. There was a large expansion in trade deficit led by relatively higher growth in imports on account of high oil prices in the earlier part of the year, and slowdown in exports. During the third quarter of 2008-09 both imports and exports recorded sharp deceleration under the impact of contraction in the external demand, slowing domestic demand and falling commodity prices. Despite relative resilience of software services exports and remittances from overseas Indians, the large trade deficit led to an expansion in current account deficit to US$ 36.5 billion in April-December 2008 as compared with US$ 15.5 billion in April-December 2007. Large net outflows under portfolio investment and large repayments under short-term trade credit, along with a wider current account deficit led to a decline in reserves. It is indeed remarkable that the contagion spreading from a severe global crisis could be managed with a reserve loss (excluding valuation) of only US$ 20.4 billion over the period April-December 2008, out of which US$ 17.9 billion was incurred in the last quarter of 2008 alone. As on April 10, 2009 the foreign exchange reserves stood at US $ 253.0 billion, showing a decline of US$ 56.7 billion (including valuation) over the level at end-March 2008. India's external debt, debt sustainability indicators and the level of foreign exchange reserves continue to remain at comfortable levels and would ensure external stability.

Monetary growth witnessed moderation during 2008-09, reflecting deceleration in bank credit on the back of the slowdown in economic activity emanating from the deepening of the international financial turmoil. The consequent capital outflows contributed to the contraction of reserve money. The Reserve Bank, therefore, undertook a number of measures such as cuts in the cash reserve ratio (CRR), *unwinding/de-sequestering of balances held by the Government with the Reserve Bank under Market Stabilisation Scheme (MSS), open market operations (OMOs) and other measures to ensure ample rupee liquidity in the system. Consequently, the expansion of reserve money, adjusted for the CRR cuts, was substantial at 19.0 per cent in 2008-09, albeit, lower than that of 25.3 per cent in 2007-08. The expansion in non-food credit, after reaching a peak in October 2008, decelerated thereafter, reflecting the downturn in demand conditions in both the international economy and the domestic economy. The flow of resources to the commercial sector from non-banking and external sources declined sharply during the year. As a result of net capital outflows and consequent foreign exchange operations of the Reserve Bank, net foreign exchange assets of the Reserve Bank declined. On the other hand, net Reserve Bank credit to Centre increased reflecting its increased investments in government securities through open market operations (OMO) as also the decline in MSS.*

India also experienced the knock-on effects of adverse international developments in conjunction with domestic factors affecting liquidity conditions. Simultaneously capital flow reversals took place, which impacted the equity markets as well as the foreign exchange market. The Reserve Bank has taken a number of measures since mid-September 2008 to augment the domestic currency and foreign exchange liquidity through the banking system. Consequently, the liquidity conditions in India have been normal since mid-November 2008. The level of Government borrowings in 2008-09 was much higher than what was initially budgeted, which impacted market sentiment during the last quarter of 2008-09. The equity markets, which had remained subdued throughout 2008-09, began to pick-up in the last week of March, in line with the international developments.

During the first half of 2008-09, headline inflation increased in major economies but recorded sharp decline subsequently in consonance with movements in international energy and commodity prices. The recent declining trend in these prices was also contributed by moderation in demand pressures following the impact of the financial crisis. In India also, inflation as measured by year-on-year variation in the wholesale price index (WPI), declined from its intra-year peak of 12.9 per cent recorded on August 2, 2008 to 0.3 per cent as on March 28, 2009 led by the reductions in the administered prices of petroleum products and electricity as well as decline in the prices of freely priced petroleum products, oilseeds/edible oils/oil cakes, raw cotton, cotton textiles and iron and steel. It may be noted that the effective supply management measures and other policy actions have contributed to relatively lower volatility in key commodity prices in India as compared to the international trends. On the other hand, high food prices have kept consumer inflation at elevated levels in the range of 9.6-10.8 per cent during January/February 2009 as compared with 7.3-8.8 per cent in June 2008 and 5.2-6.4 per cent in February 2008.

In sum, the Indian economy has experienced some loss of growth momentum with major drivers of growth witnessing moderation. In particular, the broad-based industrial slowdown, dampened services sector growth, deceleration in private consumption and investment demand along with declining export demand are some of the major concerns facing the Indian economy in the wake of the global recession at the present juncture. The fiscal stimulus packages of the Government and the monetary easing of the Reserve Bank will, however, arrest the moderation in growth and revive consumption and investment demand, though with some lag, in the months ahead. Furthermore, prospects of the agricultural sector also remain bright, and this will continue to support the rural demand. Notwithstanding widened current account deficit in 2008-09, the balance of payments position remains sustainable in the context of the present level of foreign exchange reserves and external debt. Finally, in the wake of expected improvement in agricultural production as well as low international commodity prices, inflationary pressures are also anticipated to remain at a low level through the greater part of the 2009-10.

An important challenge in the macroeconomic and monetary policy making during 2008-09 has been to manage the volatility emerging in respect of several key economic indicators of the Indian economy. During the course of the year, while overall growth moderated from its high growth momentum, headline WPI inflation declined sharply from a double digit level to near zero per cent by the end of the year. India's financial sector activity confronted a sudden shift from a phase of high to that of sharply receding capital inflows. This was manifested in reversal of the appreciating trend in the exchange rate during the year. The consequent policy response to contain excessive volatility in the foreign exchange market by increasing the supply of foreign exchange posed a challenge in managing liquidity in the money markets. The knock-on impact from the global financial markets since September 2008 further tested the Reserve Bank's monetary management operations through both quantity as well as price instruments as the stance shifted from a contractionary to an accommodative mode. However, concious monetary policy measures pursued by the Reserve Bank restored orderly conditions in the money and foreign exchange markets by November 2008. Furthermore, in the wake of receding non-banking and external sources of funding of the commercial sector, bank credit availability provided some substitution. However, the moderating economic activity eventually resulted in decelerating growth of bank credit by the end of the year. Notwithstanding several challenges, particularly from the global economy, the Indian economy remained resilient, its financial institutions and private corporate sector remained sound and solvent. Furthermore, the macroeconomic management helped in maintaining lower volatility in both the financial and the real sectors in India relative to several other advanced and emerging market economies.

I. OUTPUT

The global financial crisis interrupted the growth momentum of India, despite the strong dominance of domestic sources of growth. There was clear moderation in growth by the third quarter of 2008-09. In relation to the agricultural sector, industry and services sectors have been affected more by the adverse external shocks, with some contribution to their growth deceleration arising from cyclical slowdown in certain sectors after a prolonged phase of high growth. In the context of the severity of the impact of the crisis on the real economy of countries around the world, the growth outcome reflects the resilience of the Indian economy.

I.1 The Indian economy, which witnessed robust growth up to the second quarter of 2008-09, recorded sharp deceleration thereafter in the wake of persistent global economic slowdown, particularly in the advanced economies. According to the estimates released by the Central Statistical Organisation (CSO) in February 2009, real GDP growth during the third quarter of 2008-09 was lower at 5.3 per cent as compared with 8.9 per cent in the corresponding period of 2007-08, reflecting deceleration of growth in all its constituent sectors (Table 1). While the slowdown in industrial growth was largely an outcome of some cyclical downturn and adverse global factors, the services sector also recorded moderation from its double-digit growth, notwithstanding a counter-cyclical rise in the growth of community social and personal services following the implementation of the Sixth Pay Commission recommendations. The cumulative position reveals that the real GDP growth was 6.9 per cent during 2008-09 (April-December) as compared with 9.0 per cent during the corresponding period of 2007-08. Although India's growth trajectory has been impacted both by the financial crisis and the global economic downturn, the structural drivers of the Indian economy continue to remain intact, sustaining the overall growth at a level much higher than most of the economies in rest of the world. It is expected that domestic demand in the Indian economy would be well supported by strong rural consumption demand as well as the coordinated monetary-fiscal stimulus measures undertaken recently.

Agricultural Situation

I.2 The performance of the South West monsoon during 2008 (June 1 to September 30) was satisfactory. Cumulative rainfall was two per cent below normal with 32 of 36 meteorological sub-divisions registering excess/normal rains. The performance of North-East monsoon (October 1 to December 31, 2008) was, however, subdued with cumulative rainfall being 31.0 per cent below the normal level. Moreover, the spatial distribution of rainfall was highly uneven (Chart 1). As on March 26, 2009, the total live water storage was 26.0 per cent (33.0 per cent last year) of the Full Reservoir Level (FRL). The long range monsoon forecast released by the India

Table 1: Growth Rates of Real GDP@

(Per cent)

Sector	2007-08*	2008-09#	2007-08			2008-09			2007-08	2008-09
			Q1	Q2	Q3	Q1	Q2	Q3	April-December	
1	2	3	4	5	6	7	8	9	10	11
1. Agriculture and Allied Activities	**4.9 (17.8)**	**2.6 (17.1)**	**4.4**	**4.4**	**6.9**	**3.0**	**2.7**	**-2.2**	**5.5**	**0.6**
2. Industry	**7.4 (19.2)**	**4.2 (18.7)**	**8.5**	**7.5**	**7.6**	**5.2**	**4.7**	**0.8**	**7.9**	**3.5**
2.1 Mining and Quarrying	3.3	4.7	0.2	3.9	4.3	4.8	3.9	5.3	2.8	4.7
2.2 Manufacturing	8.2	4.1	10.0	8.2	8.6	5.6	5.0	-0.2	8.9	3.4
2.3 Electricity, Gas & Water Supply	5.3	4.3	6.9	5.9	3.8	2.6	3.6	3.3	5.5	3.2
3. Services	**10.8 (63.0)**	**9.2 (64.2)**	**10.7**	**10.7**	**10.1**	**10.2**	**9.6**	**9.5**	**10.5**	**9.7**
3.1 Trade, Hotels, Restaurants, Transport, Storage and Communication	12.4	10.3	13.2	11.0	11.6	11.2	10.7	6.8	11.9	9.4
3.2 Financing, Insurance, Real Estate and Business Services	11.7	8.6	12.4	12.2	11.9	9.3	9.2	9.5	12.2	9.3
3.3 Community, Social and Personal Services	6.8	9.3	4.5	7.1	5.5	8.5	7.7	17.3	5.7	11.2
3.4 Construction	10.1	6.5	9.7	13.7	9.0	11.4	9.7	6.7	10.8	9.2
4. Real GDP at Factor Cost	**9.0 (100)**	**7.1 (100)**	9.1	9.1	8.9	7.9	7.6	5.3	9.0	6.9
Memo:									(Amount in Rupees crore)	
a) Real GDP at Factor Cost at 1999-2000 prices	31,29,717	33,51,653								
b) GDP at current market prices	47,23,400	54,26,277								

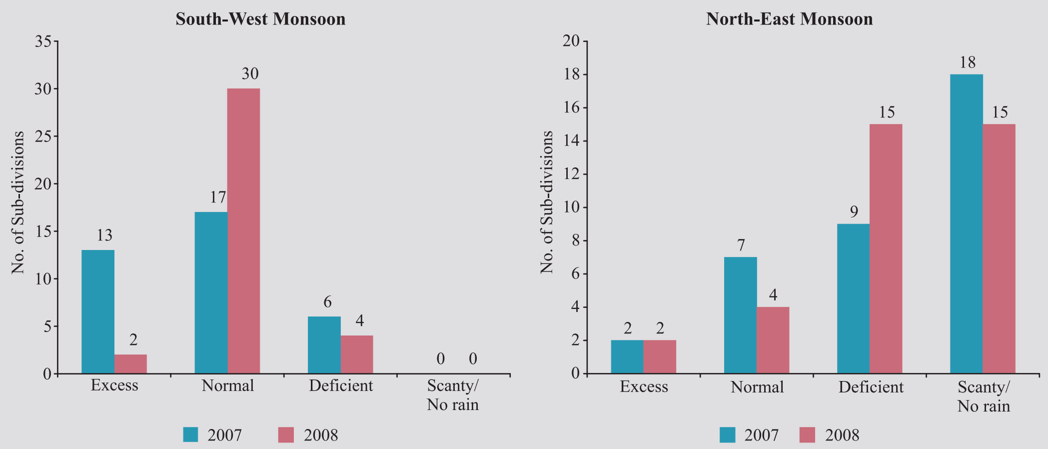
@ : At 1999-2000 Prices. * : Quick Estimates. # : Advance Estimates.
Note : Figures in parentheses indicate shares in real GDP.
Source : Central Statistical Organisation.

Meteorological Department on April 17, 2009 reveals that rainfall during the South-West monsoon season 2009, for the country as a whole is likely to be near normal, *viz.*, 96 per cent of the Long Period Average with a model error of ± 5 per cent.

I.3 The progress of acreage sown mirrors the prospects for agricultural production. The area covered under sowing of various crops declined marginally during the *kharif* season 2008-09 on account of moderate shortfall in rainfall. Nonetheless, the prospects for *rabi* production improved with area sown under *rabi* crops being higher than a year ago (Table 2).

I.4 The Ministry of Agriculture has set the target for foodgrains production for 2008-09 at 233.0 million tonnes. According to the Second Advance Estimates, the total foodgrains production during 2008-09 is placed at 227.9 million tonnes as compared with 230.8 million tonnes in 2007-08 (Table 3). The reduction in foodgrains production during 2008-09 is on account of decline in *kharif* foodgrains production attributable to the crop losses due to floods in States like Bihar, Eastern UP, Orissa and Assam during the *kharif* season 2008-09. There has been a decline in the production of

Chart 1: Rainfall during 2008-09



coarse cereals, pulses, oilseeds, cotton and sugarcane. The marginally lower estimates of wheat production for 2008-09 mainly reflected the unusually warm weather in January and early February 2009. However, growth in allied sectors like horticulture, livestock and fisheries is expected to remain favourable.

Table 2: Progress of Area Sown under Crops - 2008-09

(Million hectares)

Crop	Normal Area	Area Coverage (as on October 17, 2008)			Crop	Normal Area	Area Coverage (as on March 27, 2009)		
		2007	2008	Absolute Variation			2008	2009	Absolute Variation
1	2	3	4	5	6	7	8	9	10
		Kharif Crops					***Rabi Crops***		
Rice	39.1	37.3	38.5	1.1	Rice	3.7	4.4	4.6	0.3
Coarse cereals	22.7	21.1	20.0	-1.2	Wheat	26.5	28.1	27.8	-0.3
of which:					Coarse cereals	6.4	6.2	6.9	0.7
Bajra	9.2	8.3	7.7	-0.6	*of which:*				
Jowar	4.2	3.5	3.0	-0.5	Jowar	4.9	4.5	4.9	0.4
Maize	6.4	7.4	7.1	-0.3	Maize	0.8	1.1	1.2	0.2
Total Pulses	10.9	12.3	10.4	-1.9	Total Pulses	11.6	13.6	14.5	0.9
Total Oilseeds	15.9	17.5	18.3	0.8	Total Oilseeds	9.2	9.7	10.0	0.3
of which:					*of which*:				
Groundnut	5.4	5.4	5.3	-0.1	Groundnut	0.8	1.2	1.1	-0.2
Soyabean	7.3	8.7	9.6	0.9	Rapeseed/				
Sugarcane	4.1	5.3	4.4	-0.9	Mustard	6.3	6.0	6.6	0.7
Cotton	8.4	9.2	9.1	-0.1	Sunflower	1.3	1.1	1.2	0.1
All Crops	**101.9**	**103.9**	**101.5**	**-2.4**	**All Crops**	**57.4**	**62.0**	**63.8**	**1.9**

Source : Ministry of Agriculture, Government of India.

Table 3: Agricultural Production

(Million tonnes)

Crop	2007-08	2008-09	
		Target	Achievement@
1	2	3	4
Rice	96.7	97.0	98.9
Kharif	82.7	83.0	85.5
Rabi	14.0	14.0	13.4
Wheat	78.6	78.5	77.8
Coarse Cereals	40.8	42.0	37.0
Kharif	31.9	32.6	27.7
Rabi	8.9	9.4	9.3
Pulses	14.8	15.5	14.3
Kharif	6.4	5.9	4.8
Rabi	8.4	9.6	9.4
Total Foodgrains	**230.8**	**233.0**	**227.9**
Kharif	121.0	121.5	118.0
Rabi	109.8	111.5	109.9
Total Oilseeds	29.8	31.8	26.0
Kharif	20.7	20.0	16.3
Rabi	9.0	11.8	9.6
Sugarcane	348.2	340.0	290.4
Cotton #	25.9	26.0	22.2
Jute and Mesta ##	11.2	11.0	11.0

@ : Second Advance Estimates.

\# : Million bales of 170 kgs. each.

\#\# : Million bales of 180 kgs. each.

Source : Ministry of Agriculture, Government of India.

Food Management

I.5 The foodgrains procurement (rice and wheat) during 2008-09 was higher led by more than two-fold increase in wheat procurement (Table 4). The offtake of foodgrains (rice and wheat) during 2008-09 so far (up to January 31, 2009) was also higher than the level during corresponding period last year. The stocks of foodgrains with the Food Corporation of India (FCI) and other Government agencies nearly doubled to about 37.4 million tonnes as on February 1, 2009. The stocks of both rice and wheat are now higher than their norms.

Industrial Performance

I.6 The loss of growth momentum in the industrial sector was evident during 2008-09 (April-February) with the year-on-year expansion being 2.8 per cent as against 8.8 per cent in the corresponding period of the previous year (Table 5). The intra-year movement of growth in industrial production reveals that the Index of Industrial Production (IIP), which witnessed an average growth of around 5.6 per cent during the first four months of 2008-09 (April to July), slipped to a low of 1.7 per cent during August, before recovering to 6.0 per cent in September. The IIP growth, however, decelerated in October-November 2008 and January 2009 and recorded a negative growth during December 2008 and February 2009 (Chart 2). Before this, IIP had registered negative growth in April 1994.

I.7 The manufacturing sector witnessed a slowdown as 15 industry groups accounting for 74.4 per cent of the total weight in the IIP recorded decelerated/ negative growth during April-February 2008-09 (Table 6). Jute, most of the textiles, rubber, plastic, petroleum and coal products, food products, leather and fur products, wood and wood products, furnitures, fixtures, metal products and parts recorded a decline in production, while chemical and chemical products, machinery and equipment, basic metal and alloy industries, paper and paper products, transport equipment and parts, non-metallic mineral products, wool, silk and man-made fibre textiles and other

Table 4: Management of Food Stocks

(Million tonnes)

Year/Month	Opening Stock of Foodgrains			Procurement of Foodgrains			Foodgrains Offtake					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
2007-08	13.2	4.7	17.9	26.4	11.1	37.5	33.5	3.9	0.0	0.0	37.4	19.8	
2008-09@	13.8	5.8	19.8	32.8	22.7	55.4	28.9	2.6	0.5	0.0	32.0		
							(27.6)	(3.0)	(0.0)	(0.0)	(30.5)		
2007													
April	13.2	4.7	17.9	0.9	7.9	8.7	2.6	0.2	0.0	0.0	2.8	25.1	16.2
July	11.0	12.9	23.9	0.8	0.0	0.8	2.9	0.4	0.0	0.0	3.2	21.2	26.9
October	5.5	10.1	15.6	7.4	0.0	7.4	2.7	0.3	0.0	0.0	2.9	19.7	16.2
December	10.1	8.4	18.5	3.5	0.0	3.5	2.7	0.3	0.0	0.0	3.0	19.2	
2008													
January	11.5	7.7	19.2	4.5	0.0	4.5	2.9	0.3	0.0	0.0	3.2	21.4	20.0
April	13.8	5.8	19.8	1.1	12.6	13.7	2.7	0.0	0.0	0.0	2.8	30.7	16.2
July	11.3	24.9	36.3	0.1	0.2	0.3	2.8	0.3	0.0	0.0	3.1	34.3	26.9
September	8.5	23.3	31.8	1.4	0.0	1.4	2.8	0.4	0.0	0.0	3.2	30.0	
October	7.9	22.0	30.0	8.1	0.0	8.1	2.6	0.1	0.0	0.0	2.8	35.3	16.2
November	14.1	21.0	35.3	3.1	0.0	3.1	2.6	0.1	0.0	0.0	2.8	35.5	
December	15.6	19.6	35.5	4.2	0.0	4.2	3.0	0.5	0.2	0.0	3.6	36.2	
2009													
January	17.6	18.2	36.2	4.8	0.0	4.8	2.9	0.2	0.3	0.0	3.4	37.4	20.0
February	20.2	16.8	37.4	3.7	0.1	3.8	..	..	..	..	..	..	
March	..	..	..	2.4	0.0	2.4	..	..	..	..	..	..	

PDS : Public Distribution System. OWS : Other Welfare Schemes. OMS : Open Market Sales.

.. : Not Available.

@ : Offtake up to January 31, 2009.

Note : 1. 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.

2. Figures in parentheses indicate offtake of foodgrains during the corresponding period of 2007-08.

3. Total minimum stocks are to be maintained, as on April 1, July 1, October 1, and January 1, by public agencies under the 'new buffer stocking policy' with effect from March 29, 2005.

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

manufacturing industries recorded decelerated growth. On the contrary, only two industry groups, *viz.*, beverages, tobacco and related products and textile products recorded accelerated growth during the period.

I.8 Electricity sector witnessed its lowest growth since the introduction of current IIP series (1993-94=100), on account of deceleration in power generation in all spheres, *viz.*, thermal, nuclear and hydro-power plants. The mining sector growth also decelerated.

I.9 In terms of use-based classification, the growth in basic, capital and consumer goods sectors recorded a

Table 5: Index of Industrial Production - Sectoral and Use-Based Classification

(Per cent)

Industry Group	Weight in the IIP	Growth Rate			Weighted Contribution #		
		April-March	April-February		April-March	April-February	
		2007-08	2007-08	2008-09 P	2007-08	2007-08	2008-09 P
1	2	3	4	5	6	7	8
Sectoral							
Mining	10.5	5.1	5.2	2.4	4.2	4.0	5.9
Manufacturing	79.4	9.0	9.3	2.8	89.5	89.6	86.7
Electricity	10.2	6.3	6.6	2.4	6.3	6.4	7.3
Use-Based							
Basic Goods	35.6	7.0	7.3	2.7	24.7	25.2	28.6
Capital Goods	9.3	18.0	17.7	8.8	25.0	23.1	39.9
Intermediate Goods	26.5	8.9	9.3	-2.7	27.4	27.7	-25.9
Consumer Goods (a+b)	28.7	6.1	6.6	4.9	22.9	24.1	55.6
a) Consumer Durables	5.4	-1.0	-1.0	4.1	-1.0	-0.9	11.2
b) Consumer Non-durables	23.3	8.5	9.3	5.1	24.0	25.0	44.4
General	**100.0**	**8.5**	**8.8**	**2.8**	**100.0**	100.0	100.0

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

deceleration, while intermediate goods production registered a decline during 2008-09 (April-February). The contraction in the intermediate goods sector is due to a decline in the production of a number of textile items, PVC pipes and tubes,

Chart 2: Industrial Production

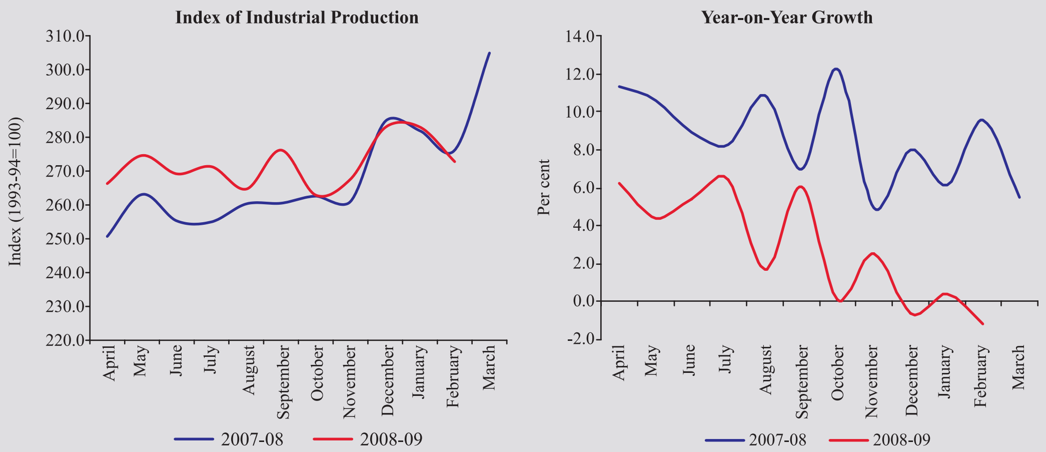


Table 6: Growth of Manufacturing Groups

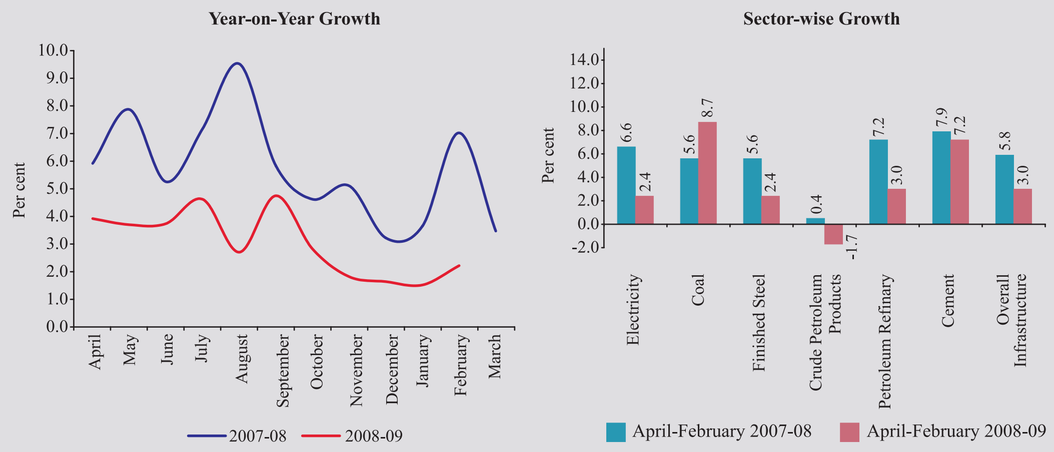
(Per cent)

Industry Group	Weight in the IIP	Growth Rate April-March 2007-08	Growth Rate April-February 2007-08	Growth Rate April-February 2008-09 P	Weighted Contribution # April-March 2007-08	Weighted Contribution # April-February 2007-08	Weighted Contribution # April-February 2008-09 P
1	2	3	4	5	6	7	8
1. Food products	9.08	7.0	7.9	-6.2	6.3	6.6	-17.0
2. Beverages, tobacco and related products	2.38	12.0	11.9	14.7	6.8	6.6	27.5
3. Cotton textiles	5.52	4.3	4.7	-2.6	2.0	2.1	-3.7
4. Wool, silk and man-made fibre textiles	2.26	4.8	3.9	1.1	1.5	1.2	1.1
5. Jute and other vegetable fibre textiles (except cotton)	0.59	33.0	30.8	-10.9	0.9	0.9	-1.2
6. Textile products (including wearing apparel)	2.54	3.7	4.2	4.5	1.4	1.6	5.4
7. Wood and wood products, furniture & fixtures	2.70	40.5	46.5	-8.9	5.3	5.6	-4.8
8. Paper and paper products and printing, publishing and allied industries	2.65	2.7	2.7	1.8	0.9	0.9	1.9
9. Leather and leather & fur products	1.14	11.7	11.6	-6.1	1.1	1.0	-1.8
10. Chemicals and chemical products (except products of petroleum & coal)	14.00	10.6	11.4	2.4	22.4	23.4	16.8
11. Rubber, plastic, petroleum and coal products	5.73	8.9	9.3	-2.3	6.1	6.2	-5.2
12. Non-metallic mineral products	4.40	5.7	6.3	0.8	4.1	4.4	1.9
13. Basic metal and alloy industries	7.45	12.1	12.8	4.9	13.4	13.6	17.8
14. Metal products and parts (except machinery and equipment)	2.81	-5.6	-2.8	-2.8	-1.5	-0.7	-2.2
15. Machinery and equipment other than transport equipment	9.57	10.5	9.8	9.7	19.0	16.9	56.0
16. Transport equipment and parts	3.98	2.9	3.1	1.4	2.3	2.3	3.4
17. Other manufacturing industries	2.56	19.8	18.6	2.9	8.0	7.3	4.1
Manufacturing – Total	**79.36**	**9.0**	**9.3**	**2.8**	**100.0**	**100.0**	**100.0**

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

railway/concrete sleeper, spun pipes, yarns, hessian, sacking, particle board and filament yarn. The basic goods sector decelerated sharply mainly on account of subdued growth in electricity sector, a fall in production of basic chemicals and rubber, petroleum and coal products and some steel and aluminium products. The capital goods sector moderated on account of decline in production of transport equipment and other machinery and equipments. Within the transport equipment, there was decline in production of broad gauge covered wagons, passenger carriage, commercial vehicles, H.T. insulators among non-metallic mineral products and agricultural implements. The consumer goods sector witnessed a

Chart 3: Growth in Infrastructure Industries



moderate deceleration, of which the growth of non durables segment decelerated, while that of consumer durables accelerated. The subdued growth in consumer non-durables was on account of the decline in production of cotton textiles, textile products, leather goods, basic chemicals, metal products such as razor blades, machinery and equipment other than transport equipment and other manufacturing industries.

Infrastructure

I.10 The core sector recorded lower growth of 3.0 per cent during April-February 2008-09, down from 5.8 per cent during the corresponding period of the previous year (Chart 3). The sharp deceleration in the growth of electricity, finished steel and petroleum refinery products sector and decline in crude oil production impacted the growth of infrastructure. Both cement and steel sectors recorded decelerated growth reflecting slowdown in construction.

Services Sector

I.11 The services sector recorded some moderation in growth during 2008-09. The moderation was visible particularly from the second quarter of the year, reflecting subdued performance of all the segments, except community, social and personal services. Cumulatively, the sector recorded a lower growth of 9.7 per cent during April-December 2008-09, as compared with 10.5 per cent during the corresponding period of 2007-08. However, the share of the services sector in real GDP has gone up during 2008-09 (see Table 1).

I.12 In terms of relative contribution to real GDP growth, while the slowdown was particularly evident in construction, trade, hotel, transport and communication, the contribution of community social and personal services increased, reflecting the Sixth Pay Commission payout (Table 7).

I.13 The indicators of services sector activity for 2008-09 suggest sharp negative growth in respect of foreign tourist arrivals,

Table 7: Growth in Services Sector

(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
2005-06	1.1	3.0	1.5	1.0	6.7
2006-07	0.8	3.5	1.9	0.8	6.9
2007-08 QE	0.7	3.4	1.7	0.9	6.7
2008-09 AE	0.5	2.9	1.3	1.2	5.8
2007-08 : Q1	0.7	3.5	1.8	0.6	6.6
: Q2	1.0	3.1	1.8	1.0	6.9
: Q3	0.6	3.1	1.6	0.7	6.0
: Q4	0.9	3.4	1.5	1.3	7.1
2008-09 : Q1	0.8	3.0	1.4	1.1	6.4
: Q2	0.7	3.0	1.4	1.1	6.3
: Q3	0.5	1.8	1.3	2.1	5.7

QE : Quick Estimates. AE : Advance Estimates.
Source: Central Statistical Organisation.

passengers handled at domestic terminals, commercial vehicles production, railway revenue earning freight traffic and import cargo handled by civil aviation. Furthermore, growth in new cell-phone connections, export cargo handled by civil aviation, production of cement and steel decelerated (Table 8).

Table 8: Indicators of Services Sector Activity

(Growth rates in per cent)

Sub-sector	2006-07	2007-08	April-January	
			2007-08	2008-09
1	2	3	4	5
Tourist arrivals	13.0	12.2	12.7	-0.1
Commercial vehicles production#	33.0	4.8	4.5 @	-23.4 @
Railway revenue earning freight traffic	9.2	9.0	9.0 @	-0.9 @
New cell phone connections	85.4	38.3	42.7	31.1
Cargo handled at major ports	9.5	11.9	11.9	3.0
Civil aviation				
Export cargo handled	3.6	7.5	6.7 *	5.5 *
Import cargo handled	19.4	19.7	21.5 *	-0.8 *
Passengers handled at international terminals	12.1	11.9	12.7 *	6.2 *
Passengers handled at domestic terminals	34.0	20.6	24.1 *	-11.6 *
Cement **	9.1	8.1	7.9 @	7.2 @
Steel **	13.1	5.1	5.6 @	2.4 @

* : April-December. # : Leading Indicator for transportation.
@: April-February. ** : Leading indicators for construction. SCBs : Scheduled Commercial Banks.
Source : Ministry of Tourism; Ministry of Commerce and Industry; Ministry of Statistics and Programme Implementation; Reserve Bank of India; and Centre for Monitoring Indian Economy.

II. AGGREGATE DEMAND

The role of aggregate demand in a phase of weakening growth impulses came to the forefront of public policy in 2008-09. The sharp contraction in external demand – as evident in falling global output, employment and global trade – clearly affected India's export performance. India's net exports (goods and services) showed a widening of deficit in 2008-09 (April-December) as compared with the previous year. Domestic demand, in the form of both private consumption and investment expenditure moderated, particularly in the third quarter of 2008-09. To offset the impact of the contraction in demand in other sectors of the economy, expanding the government demand became essential. Despite the pressures on the revenue side arising from the growth slowdown, the fiscal stimulus measures in the form of tax cuts and additional expenditure amounted to about 2.9 percent of GDP. Consequently, the targets set for deficits at the beginning of the year could not be attained, thereby necessitating deferment of the mandated deficit targets under the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 by two years. Corporate performance, after being robust for a number of consecutive years, showed signs of moderation in the third quarter of 2008-09.

II.1 The economic slowdown during 2008-09 has been associated with a considerable deceleration in investment demand, which had been a major driver of growth in recent years. There was also a marked deceleration in private consumption expenditure. Government final consumption, however, rose on account of the discretionary fiscal stimulus measures undertaken during the third quarter. As a result, key deficit indicators of the Central Government, *viz.*, the revenue deficit and the gross fiscal deficit (GFD) in the revised estimates for 2008-09 were significantly higher than the budgeted level as well as those of the preceding year. Corporate performance remained subdued, with the impact on profitability being particularly adverse during the third quarter. As regards external demand, merchandise trade deficit widened sharply during 2008-09 (April- February) as exports have contracted since October 2008. Imports also contracted since November 2008. However, during 2008-09 (April-February) the deceleration in export growth was much sharper than that of import growth. After peaking in 2007-08, saving and investment rates are likely to be lower in 2008-09 reflecting the slowdown in economic growth.

Domestic Demand

II.2 The moderation in overall growth during 2008-09 was driven by deceleration in both private consumption expenditure and investment, particularly during the third quarter of the year. The growth of real gross fixed investment decelerated to 5.3 per cent during the third quarter after registering double digit growth in earlier quarters. On the other hand, the growth in Government final consumption expenditure (GFCE) picked up sharply during the third quarter of 2008-09 reflecting the Sixth Pay Commission payout, expenditure on agricultural debt waiver, oil and fertiliser subsidies, and counter-cyclical fiscal measures (Table 9).

Table 9: Disposition of GDP at Market Prices (Base: 1999-2000) - Growth Rates

(Per cent)

Item	2007-08*	2008-09#	2007-08 Q1	2007-08 Q2	2007-08 Q3	2008-09 Q1	2008-09 Q2	2008-09 Q3	2007-08 April-December	2008-09 April-December
1	2	3	4	5	6	7	8	9	10	11
1. Total Final Consumption Expenditure	8.3	8.2	6.6	7.8	8.0	7.6	7.0	7.8	7.5	7.5
(i) Private Final Consumption Expenditure	8.5	6.8	8.4	7.5	8.9	7.7	6.9	5.4	8.3	6.6
(ii) Government Final Consumption Expenditure	7.4	16.8	-2.4	10.0	2.0	7.1	7.9	24.6	2.7	13.3
2. Gross Fixed Capital Formation	12.9	8.9	12.9	16.2	13.7	10.1	15.1	5.3	14.3	10.1
3. Change in Stocks	51.7	36.9	54.1	51.7	52.2	-32.0	-32.0	31.2	52.7	-10.2
4. Valuables	2.7	-10.4	-8.0	1.4	16.5	29.2	22.9	-8.9	3.5	12.5
5. Exports	2.1	20.8	-4.0	-4.8	6.1	23.2	10.6	11.4	-0.9	15.5
6. *Less* Imports	6.9	27.9	-0.7	-3.6	6.7	30.3	26.0	20.6	0.9	25.3
GDP at 1999-2000 prices	9.1	7.1	9.1	8.9	9.1	8.1	7.7	4.5	9.0	6.6

* : Quick Estimates. # : Advance Estimates.
Source: Central Statistical Organisation.

II.3 The Indian economy continues to be driven by domestic consumption and domestic investment. A noteworthy feature in recent years has been the contribution of gross fixed investment, which has made the growth process more sustainable. During 2008-09 (April-December), the share of private final consumption expenditure (PFCE) in real GDP declined while that of the Government final consumption expenditure (GFCE) increased. The share of gross fixed investment in real GDP, which peaked during the second quarter of 2008-09, declined during the third quarter of the year (Table 10).

Table 10: Disposition of GDP at Market Prices (Base: 1999-2000) - Shares

(Per cent)

Item	2007-08*	2008-09#	2007-08 Q1	2007-08 Q2	2007-08 Q3	2008-09 Q1	2008-09 Q2	2008-09 Q3	2007-08 April-December	2008-09 April-December
1	2	3	4	5	6	7	8	9	10	11
1. Total Final Consumption Expenditure	66.9	67.6	70.4	67.2	67.4	70.1	66.8	69.5	68.3	68.8
(i) Private Final Consumption Expenditure	57.2	57.0	60.1	58.5	59.0	59.8	58.0	59.5	59.2	59.1
(ii) Government Final Consumption Expenditure	9.8	10.6	10.4	8.7	8.4	10.3	8.7	10.0	9.1	9.7
2. Gross Fixed Capital Formation	31.6	32.1	31.7	33.0	30.8	32.3	35.3	31.0	31.8	32.8
3. Change in Stocks	3.1	4.0	3.3	3.2	3.0	2.1	2.1	3.7	3.1	2.7
4. Valuables	1.1	1.0	1.1	1.2	1.3	1.3	1.4	1.1	1.2	1.3
5. Exports	20.2	22.8	22.8	17.2	18.9	26.0	17.6	20.1	19.6	21.2
6. *Less* Imports	24.6	29.4	23.6	24.2	24.0	28.4	28.3	27.7	23.9	28.1
7. Discrepancies	1.5	1.8	-5.7	2.3	2.7	-3.3	5.1	2.1	-0.1	1.4
Memo:										(Rupees crore)
Real GDP at market prices	**34,02,716**	**36,44,011**	**7,69,806**	**7,88,864**	**8,99,235**	**8,32,350**	**8,49,407**	**9,39,458**	**24,57,905**	**26,21,215**

* : Quick Estimates. # : Advance Estimates.
Source : Central Statistical Organisation.

Combined Budgeted Government Finances: 2008-09

II.4 During 2008-09, the combined finances of the Central and State Governments were adversely impacted by the economic slowdown. This affected the revenue growth and necessitated additional expenditure on fiscal stimulus measures. In respect of the Central Government, the financial position as reflected in the revised estimates for 2008-09 shows sharp increases in major deficit indicators (Table 11). In respect of State Finances, the budgeted revenue surplus is expected to be wiped out due to lower revenue growth. The financing pattern of combined gross fiscal deficit indicates the continued dominance of market borrowing (Chart 4).

Central Government Finances: 2008-09

II.5 The Central Government finances came under pressure during the fiscal year 2008-09. During the first half of 2008-09, fiscal measures such as tax reductions and increased subsidies undertaken to reduce the impact of inflationary pressures caused by increase in global commodity prices (including petroleum products) expanded the revenue deficit and GFD. Fiscal stress continued during the second half of 2008-09 as spillover effect of the global financial crisis on the Indian economy necessitated the introduction of fiscal stimulus measures in the form of tax cuts and additional expenditure with a view to arrest the moderation in growth (Annex 1). The impact of these measures during 2008-09 is estimated to be around 2.9 per cent of GDP.

II.6 On account of the disproportionate growth in expenditure coupled with deceleration in revenue receipts, the revenue deficit and GFD in the revised estimates for the year 2008-09 were placed significantly higher than budget estimates,

Table 11: Key Fiscal Indicators

(Per cent to GDP)

Year	Primary Deficit	Revenue Deficit	Gross Fiscal Deficit	Outstanding Liabilities*
1	2	3	4	5
		Centre		
2007-08	-0.9	1.1	2.7	60.1
2008-09 BE	-1.1	1.0	2.5	56.4
2008-09 RE	2.5	4.4	6.0	57.8
2009-10 BE	1.8	4.0	5.5	56.6
		States		
2007-08 RE	0.1	-0.5	2.3	28.3
2008-09 BE	0.1	-0.5	2.1	27.4
		Combined		
2007-08 RE	-0.3	0.9	5.2	76.7
2008-09 BE	-0.8	0.5	4.5	71.7

RE : Revised Estimates. BE : Budget Estimates.

* : Includes external liabilities at historical exchange rates.

Note : 1. Negative sign indicates surplus.

2. Issuances of oil/fertiliser bonds in 2008-09 amounted to 1.8 per cent of GDP.

Chart 4: Financing Pattern of the Combined GFD

both in absolute terms as well as ratio of GDP (see Table 11). Revenue deficit at 4.4 per cent of GDP in 2008-09 (RE) was 3.4 percentage points higher than that of the budget estimates. Consequently, GFD relative to GDP rose to 6.0 per cent in 2008-09 (RE) from the budget estimates of 2.5 per cent.

II.7 During 2008-09, the economic slowdown and reduction in tax rates impacted the gross tax revenue, affecting both the net tax revenue of the Centre and the tax revenue transferred to the States. The gross tax revenue in the revised estimates for 2008-09 at Rs.6,27,949 crore was lower by 8.7 per cent than the budget estimates; collections under all major taxes were significantly lower than their budgeted levels (Chart 5). Non-tax revenue was marginally higher than the budget estimates due to a 10.0 per cent increase in 'other non-

Chart 5: Revenue Collections - Major Taxes

tax revenue' such as economic services, other general services and grants-in-aid and contribution. Major components of non-tax revenue, *viz*., dividends and profits, and interest receipts, however, declined. Reflecting this, the revenue receipts of the Centre are estimated to be lower than the budget estimates (Table 12).

II.8 The aggregate expenditure in the revised estimates for 2008-09 was significantly higher than the budget estimates mainly on account of fiscal stimulus measures aimed at supporting aggregate demand in the economy (Table 13 and Annex 1). Revenue expenditure, which accounted for 96.8 per cent of the increase in aggregate expenditure, was primarily on account of subsidies and defence under the non-plan component and rural development under the plan component. Expenditure on subsidies at Rs.1,29,243 crore (2.4 per cent of GDP) in the revised estimates for 2008-09 was 80.9 per cent higher than the budgeted amount, mainly due to food and fertiliser subsidies exceeding the budget estimates by Rs.10,960 crore (33.6 per cent) and Rs.44,863 crore (144.8 per cent), respectively (Chart 6). Rise in defence revenue expenditure was on account of implementation of the Sixth Pay Commission award for defence personnel. With regard to capital expenditure, while the defence capital outlay declined by Rs.7,007 crore, non-defence capital outlay increased by Rs.5,790 crore.

Table 12: Receipts of the Centre

(Amount in Rupees crore)

Item	2007-08 (Accounts)	2008-09 (BE)	2008-09 (RE)	Variation (4 over 3)	
				Amount	Per cent
1	2	3	4	5	6
1. Total Receipts (2+3)	**7,12,732 *** **(15.1)**	**7,50,884** **(13.8)**	**9,00,953** **(16.6)**	**1,50,069**	**20.0**
2. Revenue Receipts (i+ii)	5,41,925 (11.5)	6,02,935 (11.1)	5,62,173 (10.4)	-40,762	-6.8
i) Tax Revenue (Net)	4,39,547 (9.3)	5,07,150 (9.3)	4,65,970 (8.6)	-41,180	-8.1
ii) Non-Tax Revenue	1,02,378 (2.2)	95,785 (1.8)	96,203 (1.8)	418	0.4
3. Capital Receipts	1,70,807 (3.6)	1,47,949 (2.7)	3,38,780 (6.2)	1,90,831	129.0
of which:					
Market Borrowings	1,30,600	99,000	2,66,539	1,67,539	169.2
Recoveries of Loans	5,100	4,497	9,698	5,201	115.7
Disinvestment proceeds	38,795 *	10,165	2,567	-7,598	-74.7

RE : Revised Estimates. BE : Budget Estimates.

* : Includes an amount of Rs.34,309 crore on account of transfer of Reserve Bank's stake in State Bank of India (SBI) to the Central Government.

Note : Figures in parentheses are percentages to GDP.

Table 13: Aggregate Expenditure of the Centre

(Amount in Rupees crore)

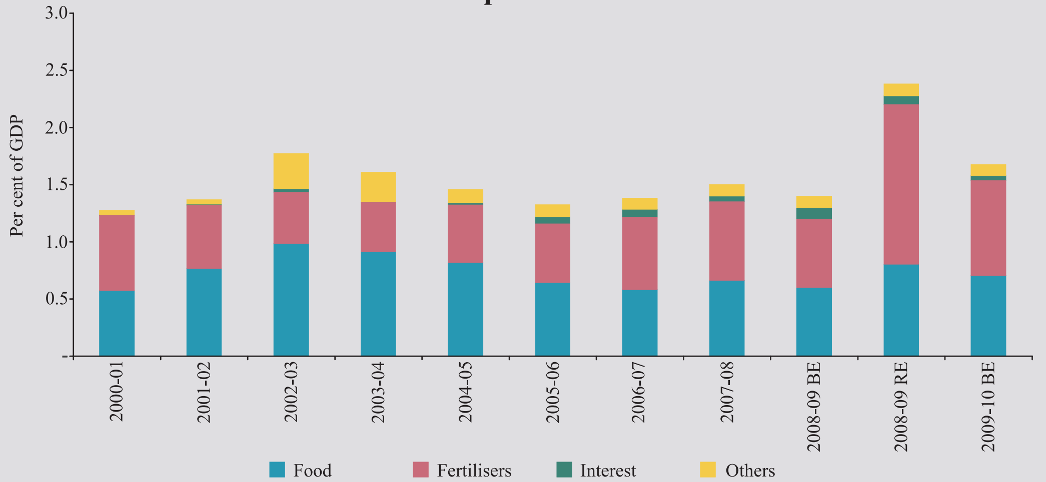
Item	2007-08 (Accounts)	2008-09 (BE)	2008-09 (RE)	Variation (4 over 3)	
				Amount	Per cent
1	2	3	4	5	6
1. Total Expenditure (2+3=4+5)	7,12,732 * (15.1)	7,50,884 (13.8)	9,00,953 (16.6)	1,50,069	20.0
2. Non-Plan Expenditure	5,07,650 * (10.7)	5,07,498 (9.4)	6,17,996 (11.4)	1,10,498	21.8
of which:					
Interest Payments	1,71,030 (3.6)	1,90,807 (3.5)	1,92,694 (3.6)	1,887	1.0
Defence Expenditure	91,681 (1.9)	1,05,600 (1.9)	1,14,600 (2.1)	9,000	8.5
Subsidies	70,926 (1.5)	71,431 (1.3)	1,29,243 (2.4)	57,812	80.9
3. Plan Expenditure	2,05,082 (4.3)	2,43,386 (4.5)	2,82,957 (5.2)	39,571	16.3
4. Revenue Expenditure	5,94,494 (12.6)	6,58,119 (12.1)	8,03,446 (14.8)	1,45,327	22.1
5. Capital Expenditure	1,18,238 * (2.5)	92,765 (1.7)	97,507 (1.8)	4,742	5.1

RE : Revised Estimates. BE : Budget Estimates.
* : Includes acquisition cost of Reserve Bank's stake in SBI at Rs.35,531 crore.

Financing of the Central Government

II.9 Gross and net market borrowings (dated securities and 364-day Treasury Bills excluding allocations under the Market Stabilisation Scheme) of the Centre for 2008-09 were budgeted at Rs.1,78,575 crore

Chart 6: Composition of Subsidies



and Rs.99,000 crore, respectively. In view of the increase in GFD by 2.4 times in the revised estimates over the budgeted level, the net market borrowings (dated securities and 364-day Treasury Bills) were hiked by 2.7 times of the budgeted level to Rs.2,66,539 crore, financing 81.6 per cent of GFD. Apart from market borrowings, short term borrowings (14-day, 91-day and 182-day Treasury Bills) would finance 16.2 per cent of GFD in the revised estimates as compared with 10.5 per cent of GFD in the budget estimates. In the public account, deposits and advances and State provident funds would finance 3.9 per cent and 1.5 per cent, respectively, of GFD in the revised estimates. Reserve funds would negatively contribute 5.1 per cent mainly on account of outflow with respect to railway funds exceeding that of inflow.

Extra-Budgetary Items

II.10 The Central Government has been supporting Food Corporation of India (FCI), fertiliser companies and oil marketing companies through issuance of special bonds in addition to providing explicit subsidies on food, fertiliser and petroleum through the budget. These bonds are considered to be fiscal deficit neutral since they do not involve immediate cash flow and are, therefore, not treated as part of budgetary expenditure/ receipts. However, these bonds have fiscal implications as they carry an obligation to repay at a later date and, hence, add to the fiscal liabilities of the Government. Furthermore, as interest payments on such bonds are treated as part of the revenue expenditure, they affect the revenue deficit and, thereby, the fiscal deficit.

II.11 During 2008-09, special bonds amounting to Rs.75,942 crore and Rs.20,000 crore were issued to oil marketing companies and fertiliser companies, respectively, together accounting for 1.8 per cent of the GDP. Repayment of special securities amounted to Rs.13,371 crore (including Rs.13,349 crore for oil bonds) during 2008-09. Taking into account this repayment, the outstanding special securities as at end-March 2009 amounted to Rs.1,99,011 crore (3.7 per cent of GDP).

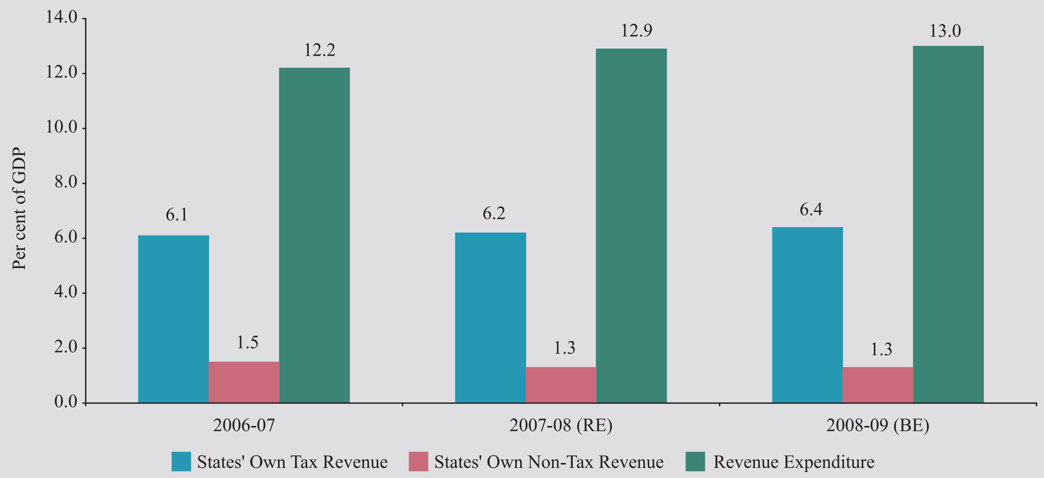
State Government Finances: 2008-09

II.12 The consolidated fiscal position of the State Governments during 2008-09 was budgeted to register a revenue surplus of 0.54 per cent of GDP. Reflecting the budgeted increase in revenue surplus as well as non-debt capital receipts, the GFD-GDP ratio at the consolidated level was budgeted to decline by 0.2 percentage points to 2.1 per cent (see Table 11). The States, while presenting their budgets for 2008-09, announced a number of policy initiatives aimed at augmenting revenues and directing expenditure towards priority areas. Allocations for agriculture and water conservation were proposed to be raised in 2008-09 by most of the States. All the States proposed higher expenditure on health and education sectors. State Governments also placed emphasis on development of infrastructure with higher allocations for development of roads and urban transport. A few States proposed higher allocations for urban development and housing sectors. They were also undertaking construction of houses for low and middle income group families, slum dwellers and below poverty line families under various schemes, including Indira Awas Yojana and Jawaharlal Nehru National Urban Renewal Mission (JNNURM). A number of State Governments extended their support for providing health as well as life insurance benefits to the poor. Several States also proposed computerisation of treasuries and tax departments.

II.13 During 2008-09, the consolidated revenue surplus of the State Government was budgeted to increase primarily through higher growth of the revenue receipts. The increase in revenue receipts in 2008-09 (BE) was indicated to be mainly contributed by States' own tax revenue and higher devolution and transfers from the Centre. As a ratio to GDP, the States' own non-tax revenue was to be maintained at previous year's level of 1.3 per cent (Chart 7). During 2008-09, the growth in revenue expenditure was budgeted to decelerate to 14.1 per cent from 19.9 per cent in the previous year.

II.14 The decomposition of consolidated GFD of all State Governments reveals that capital outlay was budgeted to exceed GFD for the third consecutive year in 2008-09 (BE), which was to be mainly financed by surpluses in the revenue account. The financing pattern of GFD of the State Governments underwent a compositional shift, with the market borrowings emerging as the major source of financing of GFD. In the past few years, special securities issued to the National Small Savings Fund (NSSF) used to be the major source of financing of GFD. Owing to the sharp decline in the collections under small savings, the special securities issued to NSSF financed less than one tenth of GFD in 2007-08 (RE) as compared with nearly three fourths in 2006-07. In 2008-09, the special securities issued to NSSF were budgeted to finance nearly one fifth of GFD, whereas market borrowings were budgeted to finance more than half of the GFD (Table 14). However, the progress during 2008-09 showed that due

Chart 7: States' Own Revenue Receipts and Revenue Expenditure



to a continued shortfall in collection under NSSF, State Governments were allowed to raise additional market borrowings as was done in 2007-08. Details of actual market borrowings of the Central and State Governments for the year 2008-09 are covered in Chapter V.

Central Government Finances: Budget Estimates for 2009-10

II.15 The Union Interim Budget for 2009-10 was presented against the backdrop of global economic slowdown adversely impacting the Indian economy and the consequent need to provide fiscal stimulus to contain the economic slowdown. The buoyancy in revenue collection significantly declined not only due to the economic slowdown but also due to tax rate reduction measures undertaken by the Government to provide stimulus. At the same time, expenditure was stepped up substantially to boost the aggregate demand in the economy.

II.16 Although the adverse impact of economic slowdown on the revenue receipts observed during 2008-09 is expected to persist during 2009-10, there is likely to be some improvement. Accordingly, revenue receipts during 2009-10 are budgeted to

Table 14: Decomposition and Financing Pattern of GFD of States

(Per ent)

Item	2006-07 (Accounts)	2007-08 (RE)	2008-09 (BE)
1	2	3	4
Decomposition (1+2+3-4)	**100.0**	**100.0**	**100.0**
1. Revenue Deficit	-32.1	-20.9	-25.2
2. Capital Outlay	126.5	118.9	128.9
3. Net Lending	8.0	9.8	9.7
4. Non-debt Capital Receipts	2.5	7.8	13.3
Financing (1 to 11)			
1. Market Borrowings	16.9	58.9	56.7
2. Loans from Centre	-11.5	3.2	6.2
3. Special Securities issued to NSSF/Small Savings	72.3	8.8	19.6
4. Loans from LIC, NABARD, NCDC, SBI & Other Banks	5.1	6.8	6.5
5. Small Savings, P.F., *etc*.	13.4	11.3	11.5
6. Reserve Funds	9.8	-8.9	1.1
7. Deposits & Advances	16.5	4.7	4.3
8. Suspense & Miscellaneous	6.0	-4.5	-1.6
9. Remittances	-0.4	-0.3	0.1
10. Others	-7.1	-2.2	-2.2
11. Overall Surplus (-) / Deficit (+)	-21.1	22.3	-2.1

RE : Revised Estimates. BE : Budget Estimates. NSSF : National Small Savings Fund.

Note : 1. 'Others' include Compensation and Other Bonds, Loans from other institutions, Appropriation to Contingency Fund, Inter-state Settlement and Contingency Fund.

2. Figures for 2006-07 (Accounts) in respect of Jammu and Kashmir and Jharkhand relate to revised estimates.

3. All financing items are on a net basis.

Source : Budget Documents of the State Governments.

increase by 8.4 per cent from 3.7 per cent in 2008-09 (RE). Growth of gross tax revenue at 6.9 per cent would be higher than that of 5.9 per cent in 2008-09. The gross tax revenue relative to GDP would, however, decline further during the year (Table 15). After the announcement of the Interim Budget, the Central Government announced further reductions in indirect tax rates as part of the fiscal stimulus package (see Annex 1), which could impact on the revenue collections.

Table 15: Gross Tax Revenues of the Centre

(Per cent to GDP)

Year	Direct	Indirect	Total
1	2	3	4
2004-05	4.2	5.5	9.7
2005-06	4.4	5.8	10.2
2006-07	5.3	6.1	11.5
2007-08	6.3	6.3	12.6
2008-09RE	6.4	5.2	11.6
2009-10BE	6.3	4.8	11.1

II.17 Aggregate expenditure is budgeted to decelerate in 2009-10 after the substantial increase during the preceding year (Table 16). The lower growth in aggregate expenditure would mainly emanate from revenue expenditure, which is budgeted to

Table 16: Union Interim Budget 2009-10 at a Glance

(Amount in Rupees crore)

Item	2008-09 (RE)	2009-10 (BE)	Growth rate (per cent) 2008-09	Growth rate (per cent) 2009-10
1	2	3	4	5
1. Revenue Receipts (i+ii)	5,62,173 (10.4)	6,09,551 (10.1)	3.7	8.4
i) Tax Revenue (Net)	4,65,970 (8.6)	4,97,596 (8.3)	6.0	6.8
ii) Non-Tax Revenue	96,203 (1.8)	1,11,955 (1.9)	-6.0	16.4
2. Non-Plan Expenditure	6,17,996 (11.4)	6,68,082 (11.1)	30.9*	8.1
of which:				
i) Interest Payments	1,92,694 (3.6)	2,25,511 (3.7)	12.7	17.0
ii) Defence Expenditure	1,14,600 (2.1)	1,41,703 (2.4)	25.0	23.7
iii) Subsidies	1,29,243 (2.4)	1,00,932 (1.7)	82.2	-21.9
3. Plan Expenditure	2,82,957 (5.2)	2,85,149 (4.7)	38.0	0.8
4. Revenue Expenditure	8,03,446 (14.8)	8,48,085 (14.1)	35.1	5.6
5. Capital Expenditure	97,507 (1.8)	1,05,146 (1.7)	17.9*	7.8
6. Total Expenditure	9,00,953 (16.6)	9,53,231 (15.8)	33.0*	5.8
7. Revenue Deficit	**2,41,273 (4.4)**	**2,38,534 (4.0)**	**359.0**	**-1.1**
8. Gross Fiscal Deficit	**3,26,515 (6.0)**	**3,32,835 (5.5)**	**157.3**	**1.9**
9. Gross Primary Deficit	**1,33,821 (2.5)**	**1,07,324 (1.8)**	**-403.3**	**-19.8**

* : Adjusting for acquisition cost of RBI's stake in SBI at Rs.35,531crore in 2007-08.
Note : Figures in parentheses are percentages to GDP.

decelerate to 5.6 per cent from 35.1 per cent growth in 2008-09. Containment of subsidies, in particular fertiliser subsidy, would be an important contributing factor to the slower growth in revenue expenditure during 2009-10. Growth in grants to States and Union Territories is budgeted to be lower at 10.4 per cent than 14.7 per cent a year ago. Capital expenditure, comprising capital outlay and loans and advances, is also budgeted to decelerate in 2009-10 over 2008-09 (adjusting for acquisition cost of Reserve Bank's stake in SBI in 2007-08). Capital outlay is budgeted to increase by 15.3 per cent as compared with an increase of 16.7 per cent (adjusting for acquisition cost of Reserve Bank's stake in SBI in 2007-08). While the defence capital outlay is estimated to increase by Rs.13,824 crore, the non-defence capital outlay would decline by Rs.1,100 crore.

II.18 The Union Interim Budget for 2009-10 has indicated the relaxation of the FRBM targets for 2008-09 and 2009-10 in order to mobilised resources to boost aggregate demand. However, as a medium term objective, it has recognised the need to revert to fiscal consolidation process at the earliest. The key deficit indicators, *viz.*, revenue deficit, GFD and primary deficit as per cent of GDP, are budgeted at 4.0 per cent, 5.5 per cent and 1.8 per cent in 2009-10, respectively, lower than 4.4 per cent, 6.0 per cent and 2.5 per cent, respectively, in the preceding year (see Table 11).

II.19 During 2009-10, net market borrowings (net of MSS) are budgeted to increase from Rs.2,66,539 crore in 2008-09 to Rs.3,08,647 crore. Inclusive of repayment of Rs.93,087 crore, gross market borrowings (net of MSS) are placed at Rs.4,01,734 crore in 2009-10. In terms of financing GFD, the share of net market borrowings (excluding allocations under MSS), investments by the NSSF in the special Central Government securities and external assistance are budgeted to increase in 2009-10 over 2008-09 (RE). Outflow from reserve funds is budgeted to be lower in 2009-10 than in 2008-09 (RE). During 2009-10, the budget expects no drawdown of cash balances to finance GFD as against 9.2 per cent of GFD in 2008-09 (RE) (Table 17).

Table 17: Financing Pattern of Gross Fiscal Deficit

(Amount in Rupees crore)

Item	2008-09 (RE)	2009-10 (BE)
1	2	3
Gross Fiscal Deficit	3,26,515	3,32,835
Financed by:		
Market Borrowings	2,66,539	3,08,647
	(81.6)	(92.7)
Securities issued against Small Savings	1,324	13,255
	(0.4)	(4.0)
External Assistance	9,603	16,047
	(2.9)	(4.8)
State Provident Fund	4,800	5,000
	(1.5)	(1.5)
NSSF	11,206	1,022
	(3.4)	(0.3)
Reserve Funds	-16,808	-3,358
	(-5.1)	(-1.0)
Deposit and Advances	12,788	9,026
	(3.9)	(2.7)
Postal Insurance and Life Annuity Funds	2,594	2,672
	(0.8)	(0.8)
Drawdown of Cash Balances	29,984	0
	(9.2)	(0.0)
Others	4,486	-19,477
	(1.4)	(-5.9)

Note: Figures in parentheses are percentages to GFD.

Corporate Performance

II.20 An analysis of the performance of select non-financial non-government companies during the first half of the year 2008-09 showed that sales recorded a strong growth in relation to the first half of 2007-08. This was mainly on account of high selling prices and continued consumer demand. However, expenditure growth remained higher than sales growth primarily on account of rising input costs, including power and fuel, rise in interest outgo and large provisioning towards marked-to-market (MTM) losses on foreign exchange related transactions. Burden of piled-up inventories and decline in other income also affected profit performance which remained subdued during the first half of 2008-09.

II.21 During the third quarter of 2008-09, however, sales growth slowed down considerably as demand weakened. As against accumulation of stocks in trade during the first half of 2008-09, sales were partly made through depletion of inventories in the third quarter. Although the expenditure growth also decelerated during this period, the deceleration in sales growth was sharper than that in expenditure growth. Consequently, profitability of these companies measured in terms of the ratios of gross profits to sales and profits after tax to sales deteriorated, indicating pressure on margins. The high growth in interest payments was one of the key factors in the decline in net profits in the third quarter of 2008-09 over the corresponding period of the previous year. More importantly, other income continued to decline over the third quarter as compared to substantial increases witnessed during the preceding year (Table 18).

II.22 The non-financial government (oil and non-oil) companies posted a growth of 11.1 per cent in revenue and a fall of 27.0 per cent in net profits during the third quarter of 2008-09 over the corresponding period of the previous year. While net profits of non-oil companies declined by 10.3 per cent, that of oil companies declined sharply by 45.4 per cent during the third quarter of 2008-09. The sharp reduction in crude and petroleum prices during the third quarter led to inventory valuation losses and lower realisation of exports which adversely affected the profits of oil companies. The profits of these companies were also affected by higher outgo on interest payments and increase in staff costs due to larger provisioning for anticipated wage revision. The three oil marketing companies, however, posted combined net profits of Rs.3,336 crore during the quarter. The issuance of oil bonds by Government to partially compensate the under-realisation suffered by them (as a result of non-revision of retail prices of petrol, diesel, LPG and kerosene in line with the international prices) had averted net losses in these companies.

External Demand

II.23 Net external demand, as reflected by net exports (goods and services) as a percentage of GDP, deteriorated to (-) 7.8 per cent during the first three quarters of 2008-09 as compared with (-) 4.7 per cent in the corresponding period of the previous year. Exports and imports (goods and services) grew by 17.1 per cent and 27.3

Table 18: Corporate Sector - Financial Performance

(Growth rates/Ratios in per cent)

Item	2007-08	2007-08	2008-09	2007-08				2008-09		
		April-December		Q1	Q2	Q3	Q4	Q1	Q2	Q3
1	2	3	4	5	6	7	8	9	10	11
Sales	18.3	17.9	23.9	19.2	16.0	18.0	20.6	29.3	31.8	9.5
Other income	46.2	68.0	-2.4	106.7	45.2	70.2	28.5	-8.4	-0.6	-4.8
Expenditure	18.4	17.7	28.3	18.0	15.3	18.9	23.3	33.5	37.5	12.6
Depreciation provision	14.8	17.4	14.9	18.1	15.8	17.9	15.4	15.3	16.5	16.8
Gross profits	22.8	23.7	-1.7	31.9	22.5	20.4	16.8	11.9	8.7	-26.7
Interest payments	28.8	25.1	65.4	4.4	18.4	45.7	35.8	58.1	85.3	62.9
Profits after tax	26.2	28.6	-16.7	33.9	22.7	29.4	14.1	6.9	-2.6	-53.4
Select Ratios										
Gross profits to Sales	16.3	16.0	13.1	16.7	16.3	16.2	15.0	14.5	13.5	11.0
Profits after tax to Sales	11.8	11.6	8.1	11.6	11.5	12.2	10.3	9.7	8.6	5.3
Interest to Sales	2.2	2.2	3.0	2.0	2.1	2.5	2.2	2.4	2.9	3.8
Interest to Gross profits	13.8	13.5	22.6	11.8	12.8	15.3	14.6	16.8	21.5	34.6
Interest Coverage (Times)	7.3	7.4	4.4	8.5	7.8	6.5	6.8	6.0	4.6	2.9
Memo:										(Amount in Rupees crore)
No. of Companies	2,359	2,476	2,059	2,342	2,228	2,329	2,357	2,500	2,386	2,486
Sales	11,41,711	9,08,339	10,35,713	2,80,814	2,97,110	3,06,238	3,50,917	3,65,303	3,93,626	3,74,686
Other income*	30,958	23,916	22,077	9,151	8,057	9,221	10,082	7,666	7,943	8,471
Expenditure	9,56,930	7,63,735	8,97,759	2,37,698	2,49,194	2,57,472	3,02,105	3,17,605	3,43,921	3,22,077
Depreciation provision	40,664	32,075	34,191	10,173	10,576	10,961	11,805	11,590	12,075	14,563
Gross profits	1,86,665	1,45,492	1,35,541	46,780	48,296	49,717	52,583	52,930	52,968	41,299
Interest payments	25,677	19,659	30,674	5,504	6,194	7,609	7,703	8,891	11,403	14,277
Profits after tax	1,34,291	1,05,686	83,664	32,699	34,266	37,470	36,109	35,295	33,844	19,962

*: Other income excludes extraordinary income/expenditure if reported explicitly.

Notes: 1. Data are based on abridged financial results of the select non-government non-financial listed 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. The quarterly data may not add up to annual data due to differences in the number and composition of companies covered in each period.

per cent, respectively, in April-December 2008 as compared with 23.3 per cent and 25.1 per cent, respectively, in April-December 2007. Merchandise trade deficit recorded a sharp increase during 2008-09 (April-February) on account of higher crude oil prices in the early part of the year coupled with loss of momentum in exports since September 2008. Export growth decelerated in September and thereafter turned negative in October 2008 and the negative trend continued till February 2009. Accordingly, merchandise trade deficit during 2008-09 (April-February) widened to US $ 113.8 billion from US $ 82.2 billion a year ago. A detailed discussion on the external demand conditions is set out in Chapter III.

Saving and Investment

II.24 The rate of Gross Domestic Saving (GDS) had steadily risen since 2002-03 to a peak of 37.7 per cent of GDP in 2007-08, mainly due to improved saving performance of the private corporate and public sectors. Improved profitability of joint stock companies contributed to the increase in private corporate savings. In respect of the public sector, a significant decline in the dissavings of government administration as enabled by the fiscal consolidation coupled with improved profitability of departmental enterprises and non-departmental undertakings contributed to higher savings. Household saving rate exhibited marginal improvement in 2007-08 over the previous year, owing to a rise in the physical saving rate (Table 19). The rate of Gross Domestic Capital Formation (GDCF) also peaked at 39.1 per cent of GDP in 2007-08. The saving-investment balance widened during 2007-08 reflecting continuous surge in investment activity ahead of the saving rate. It may, however, be noted that the steady trend of rise in saving and investment may not be sustained during 2008-09 on account of slowing down of economic activity.

Table 19: Rates of Gross Domestic Saving and Investment

(Per cent of GDP at current market prices)

Item	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07 PE	2007-08 QE
1	2	3	4	5	6	7	8
1. Household Saving	22.1	22.9	24.1	22.8	24.1	24.1	24.3
of which :							
a) Financial assets	10.9	10.3	11.4	10.1	11.7	11.7	11.7
b) Physical assets	11.3	12.6	12.7	12.7	12.4	12.4	12.6
2. Private Corporate Saving	3.4	4.0	4.6	6.7	7.7	8.3	8.8
3. Public Sector Saving	-2.0	-0.6	1.1	2.2	2.4	3.3	4.5
4. Gross Domestic Saving	23.5	26.3	29.8	31.7	34.2	35.7	37.7
5. Net capital inflow	-0.6	-1.2	-2.2	0.4	1.2	1.1	1.4
6. Gross Domestic Capital Formation #	22.8	25.2	27.6	32.1	35.5	36.9	39.1
7. Gross Capital Formation	24.2	25.2	26.8	31.6	34.8	36.4	38.7
of which :							
a) Public sector	6.9	6.1	6.3	6.9	7.6	8.0	9.1
b) Private corporate sector	5.4	5.9	6.8	10.8	13.7	14.8	15.9
c) Household sector	11.3	12.6	12.7	12.7	12.4	12.4	12.6
d) Valuables	0.6	0.6	0.9	1.3	1.2	1.2	1.1
8. Total Consumption Expenditure (a+b)	76.9	75.2	73.1	69.4	68.1	66.4	65.3
a) Private Final Consumption Expenditure	64.5	63.3	61.8	58.7	57.6	56.2	55.2
b) Government Final Consumption Expenditure	12.4	11.9	11.3	10.7	10.5	10.2	10.1
Memo							
Saving-Investment Balance (4-6)	0.6	1.2	2.2	-0.4	-1.2	-1.1	-1.4
Public Sector Balance	-8.9	-6.7	-5.3	-4.7	-5.2	-4.6	-4.6
Private Sector Balance	8.8	8.4	9.2	6.1	5.7	5.2	4.7
a) Private Corporate Sector	-2.1	-1.9	-2.2	-4.0	-6.0	-6.5	-7.0
b) Household Sector	10.9	10.3	11.4	10.1	11.7	11.7	11.7

PE : Provisional Estimates. QE : Quick Estimates. # : Adjusted for errors and omissions.

Note : Figures may not add up to the totals due to rounding off.

Source : Central Statistical Organisation.

Annex 1: Major Fiscal Stimulus Measures

October 20, 2008

- The supplementary demand for grants provided for a gross expenditure amounting to Rs.2,37,286 crore with net cash outgo of Rs.1,05,613 crore mainly to finance schemes/plans announced in the Union Budget for 2008-09 but for which no provisions were made.

December 7, 2008

- The three major *ad valorem* rates of Central Excise duty, *viz*., 14 per cent, 12 per cent and 8 per cent applicable to non-petroleum products were reduced by 4 percentage points each.
- For promoting exports, pre-shipment and post-shipment export credit for labour intensive exports, *i.e*., textiles (including handlooms, carpets and handicrafts), leather, gems & jewellery, marine products and SME sector is being made more attractive by providing an interest subvention of 2 per cent up to March 31, 2009 subject to minimum rate of interest of 7 per cent per annum. An additional fund of Rs.1,100 crore to ensure full refund of Terminal Excise duty/CST was announced. Furthermore, an additional allocation for export incentive schemes of Rs.350 crore was announced.
- In order to provide a counter-cyclical stimulus *via* plan expenditure, an additional Plan expenditure of up to Rs 20,000 crore in the current fiscal year was allocated.
- In the textile sector, an additional allocation of Rs.1,400 crore will be made to clear the entire backlog of Technology Up-gradation Fund (TUF) Scheme.
- In order to support the infrastructure schemes under Public Private Partnership mode, India Infrastructure Finance Company Limited (IIFCL) was authorised to raise Rs.10,000 crore through tax-free bonds by March 31, 2009.

December 19, 2008

- The second supplementary demand for grants provided for a gross expenditure amounting to Rs.55,605 crore with a net cash outgo of Rs.42,480 crore.

January 29, 2009

- The Debt Consolidation and Relief Facility (DCRF) guidelines for the year 2008-09 were relaxed by modifying the fiscal deficit target as 3.5 per cent so as to enable the States to borrow up to 3.5 per cent of their respective Gross State Domestic Product (GSDP) during 2009-10 as one-time relaxation for undertaking capital expenditure. In addition, the DCRF requirement of elimination of revenue deficit was also relaxed for 2008-09. On February 26, 2009, this relaxation was extended for the year 2009-10 also. The States will not lose benefits of DCRF, provided they achieve the fiscal deficit target of 3.5 per cent of GDP in 2009-10. The States will have to suitably amend their respective FRBM Act.

February 24, 2009 (Post-Interim Budget)

- General reduction in excise duty rates by 4 percentage points, which was made with effect from December 7, 2008, was extended beyond March 31, 2009. In addition, central excise duty was reduced from 10 per cent to 8 per cent. Service tax on taxable services was also reduced from 12 per cent to 10 per cent.

III. THE EXTERNAL ECONOMY

In the face of deteriorating external environment, the adverse effects of the contagion transmitting through different components of India's balance of payments (BoP) could largely be contained through policy actions. Reflecting higher trade and current account deficits in the face of lower net capital inflows, the foreign exchange reserves of India (excluding valuation effects) fell by US$ 20.4 billion during April-December 2008, even though the foreign exchange reserves level (including valuation effects) fell more sharply by US$ 53.8 billion during the same period, reflecting the impact of large volatility in major international currencies. The effect of the external shocks transmitting to India through the BoP could thus be contained with loss of reserves mainly in the third quarter of 2008-09, when the global crisis deepened and spread significantly with more visible real effects. Even though significant moderation in international oil prices in the second half of 2008-09 relieved the pressures on BoP through deceleration in import growth, slowdown in exports on account of contracting global demand, large reversal in portfolio flows, and reduced inflows of debt capital on account of the adverse global credit market conditions exerted sustained pressures on the BoP. Notwithstanding these adverse developments, sustained interest in India as a long-term investment destination and a comfortable reserve position suggest that the external sector could continue to support stability and growth.

III.1 The slowdown in global demand and credit market shocks adversely impacted India's balance of payments (BoP) in 2008-09 (April-December). The BoP position was marked by a widened trade deficit, a record level of current account deficit (CAD) and lower net capital inflows. During the third quarter of 2008-09, export growth turned negative for the first time since 2001-02, while import growth touched a single digit. At the same time, large net outflows under portfolio investment and large repayments under short-term trade credit led to a lower capital account surplus during April-December 2008. Except FDI and NRI deposits, all other components of capital flows declined in net terms. Reflecting these developments, India's foreign exchange reserves on BoP basis declined by US $ 20.4 billion during April-December 2008 (US $ 53.8 billion including valuation losses). As on April 10, 2009, the foreign exchange reserves stood at US $ 253.0 billion.

International Developments

III.2 The world economy experienced a synchronized downturn extending to the emerging markets with steeper fall in output and trade than earlier anticipated. Global economic activity continued to contract with the advanced economies experiencing their sharpest declines in the post-World War II period, notwithstanding policy efforts. The financial sector deleveraging in conjuction with weak credit markets, falling production and rapidly shrinking global trade, have led to a situation of a more prolonged recession. The impact is visible not only in the financial markets but also in the real economy across the globe. Significant fall in various asset prices, the end of a housing construction boom in a number of countries and fall in consumer and business sentiments are weighing on economic activity. While all major advanced economies including the US, Euro Area, Japan and the UK witnessed recessionary conditions in the fourth quarter of 2008, the growth in EMEs also showed significant moderation (Table 20).

III.3 Uncertainty surrounding the global economic outlook remains high mainly stemming from a scenario of ongoing financial market turmoil affecting the real economy more adversely than previously anticipated. Since the official recognition of recession in the US, the UK, the Euro Area and Japan, the downside risks to the global economy have increased. According to the forecast released by the International Monetary Fund (IMF) on March 19, 2009, world output is projected to contract by 0.5-1.0 per cent in 2009 as compared with a growth of 3.2 per cent in 2008, before recovering gradually in 2010 (Table 21).

Table 20: Real GDP Growth Rates – Global Scenario

(Per cent)

Region/Country	2007	2008 P	2009 P	2008			
				Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8
Advanced Economies							
Euro area	2.6	0.9*	-3.2*	2.2	1.5	0.6	-1.3
Japan	2.4	-0.7*	-5.8*	1.5	0.7	-0.2	-4.6
Korea	5.0	4.1	3.5	5.5	4.3	3.1	-3.4
UK	3.0	0.7	-2.8	2.6	1.7	0.2	-2.0
US	2.0	1.1*	-2.6*	2.5	2.1	0.7	-0.8
OECD Countries	2.6	1.2	-0.4	2.6	1.8	0.8	-1.6
Emerging Economies							
Argentina	8.7	6.5	3.6	8.5	7.8	6.9	4.9
Brazil	5.7	5.8	1.8	6.1	6.2	6.8	1.3
China	13.0	9.0	6.7	10.6	10.1	9.0	6.8
India	9.0#	7.1#	5.3@	8.8	7.9	7.6	5.3
Indonesia	6.3	6.1	5.5	6.3	6.4	6.1	5.2
Malaysia	6.3	5.8	4.8	7.4	6.7	4.7	0.1
Thailand	4.8	4.7	4.5	6.0	5.3	3.9	-4.3

P : IMF Projections.
* : Based on the revised data released in the IMF's WEO Update of March 19, 2009.
# : Data relate to fiscal years based on the C.S.O. estimates.
@ : IMF Public Information Notice No.09/35 dated March 17, 2009; fiscal year projections.
Source : International Monetary Fund; The Economist; and the OECD.

Table 21: Select Economic Indicators – World

Item	2006	2007	2008P	2009P
1	2	3	4	5
I. World Output (per cent change) #	5.1 (3.9)	5.2 (3.8)	3.2+	-1.0 to -0.5+
i) Advanced Economies	3.0	2.7	0.8+	-3.5 to -3.0+
ii) Other Emerging Market and Developing Countries	7.9	8.3	6.1+	1.5 to 2.5+
of which: Developing Asia	9.8	10.6	7.8	5.5
II. Consumer Price Inflation (per cent)				
i) Advanced Economies	2.4	2.1	3.5	0.3
ii) Other Emerging Market and Developing Countries	5.4	6.4	9.2	5.8
of which: Developing Asia	4.2	5.4	7.8	6.2
III. Net Capital Flows* (US $ billion)				
i) Net Private Capital Flows (a+b+c)**	223.0	632.8	528.6	286.6
a) Net Private Direct Investment	246.0	379.0	443.6	414.6
b) Net Private Portfolio Investment	-107.3	54.5	-6.6	-89.1
c) Net Other Private Capital Flows	84.4	199.5	91.8	-38.7
ii) Net Official Flows	-158.0	-140.7	-158.6	-135.4
IV. World Trade @				
i) Trade Volume	9.4	7.2	4.1	-2.8
ii) Export Volume@@	8.5	6.0	2.0	-9.0
iii) Trade Price Deflator	5.0	8.1	15.3	0.2
V. Current Account Balance (per cent to GDP)				
i) US	-6.0	-5.3	-4.6	-3.3
ii) China	9.4	11.3	9.5	9.2
iii) Middle East	21.1	18.4	22.9	17.1

P : IMF Projections.

+ : Based on the revised data released in the IMF's WEO Update of March 19, 2009.

: Growth rates are based on exchange rates at purchasing power parities. Figures in parentheses are growth rates at market exchange rates as given in World Economic Outlook October 2008 and WEO Update of January 28, 2009 and March 19, 2009.

* : 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.

@@ : Average of annual percentage change for world exports of goods and services according to the WTO.

Source : World Economic Outlook (October 2008), WEO Update (January 28, 2009 and March 19, 2009), International Monetary Fund.

III.4 According to the IMF, the US economy is projected to contract by 2.6 per cent in 2009 (as against an increase of 1.1 per cent in 2008) as households respond to depreciating real and financial assets and tightening financial conditions. Similarly, real GDP in the Euro Area is also projected to decline by 3.2 per cent in 2009 (as against an increase of 0.9 per cent in 2008) due to sharp decline in external demand, the impact of housing market corrections in some member states, intensification of financing constraints and falling confidence. The Japanese GDP has already shown contraction by 4.6 per cent in the fourth quarter of 2008 reflecting sluggish domestic demand and sharp decline in exports and business investment. Real GDP in Japan is projected to record a decline of 5.8 per cent in 2009 as the support to growth from net exports is expected to decline further. Financial conditions continue to present significant downside risks. Considerable uncertainty still remains about the extent and duration of the economic downturn in affected economies stemming from the crisis.

III.5 The growth rates in the emerging and developing economies, which were earlier considered to be resilient to the global financial disruptions, are also projected to slow appreciably to 1.5-2.5 per cent in 2009. Growth fell sharply across a broad spectrum of emerging economies, reflecting the confluence of weakening external demand, tightening financing constraints and falling commodity prices. The IMF projects that Developing Asia will grow by 5.5 per cent in 2009 (7.8 per cent in 2008). While China's growth is projected to moderate from 9.0 per cent in 2008 to 6.7 per cent in 2009, growth for India is placed at 5.3 per cent for 2009-10 (6.3 per cent in 2008-09) by the IMF. Nevertheless, the economic outlook for the EMEs still remains relatively positive when compared to advanced economies, but uncertainties about their resilience to the global shocks have considerably increased. The impact of the financial crisis is already in evidence in the currency and equity markets and in the capital outflows from the EMEs. However, the macroeconomic impact on the EMEs, including India, has so far been contained somewhat by the strength of domestic demand.

III.6 According to the IMF projections, world trade volume is expected to decline by 2.8 per cent in 2009, however, export volume of emerging and developing economies is projected to decline marginally by 0.8 per cent (see Table 21). The World Trade Organisation (WTO) has also projected that the collapse in global demand will drive exports volume down by 9 per cent in 2009, the biggest contraction since the World War II.

III.7 According to the IMF's International Financial Statistics, world merchandise exports, in dollar terms, grew by 22.6 per cent during January-September 2008, but subsequently declined during October-December 2008 by 10.1 per cent. The contraction in exports could be attributed to declining demand, falling production and a sharp shrinkage in credit to finance trade (WTO, 2009). The overall world exports during 2008 remained marginally higher than a year ago, mainly because of the higher export growth recorded in the first half of 2008 (Table 22). Exports from advanced economies showed a sharp deceleration, reflecting the impact of well entrenched recession. Exports from emerging and developing economies during 2008 grew sharply up to September 2008. However, a sharp shrinkage occurred since October, which subsequently got worsened with a rapid fall in export growth emanating from deteriorating external demand, sharp fall in commodity prices and severe constraints in accessing trade credit in the international markets.

Table 22: Growth in Exports - Global Scenario

(Per cent)

Region/Country	2007	2008
1	2	3
World	13.9	14.3
Advanced Economies	13.5	11.3
Emerging and Developing Economies	14.7	21.1
China	25.6	17.3
France	12.3	9.8
Germany	18.0	10.8
India	21.5	20.6
Indonesia	14.7	24.4
Japan	7.8	12.3
Korea	14.1	13.6
Malaysia	9.6	19.1
Singapore	10.1	13.0
Thailand	17.0	12.9
US	12.0	11.9

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

III.8 In response to the global economic slowdown, various national level as well as coordinated global monetary and fiscal policy measures have been put in place. The G-20 member countries on April 2, 2009 resolved to restore confidence, growth and jobs; repair the financial system to restore lending; strengthen financial regulation to rebuild trust; fund and reform the international financial institutions; promote global trade and investment and reject protectionism; and build an inclusive and sustainable recovery. This would be pursued through undertaking a concerted fiscal expansion (US $5 trillion), providing additional resources through international financial institutions and trade finance, trebling of resources to the IMF, supporting a new SDR allocation and additional lending by the Multilateral Development Banks, and using additional resources from IMF gold sales for concessional finance for the poorest countries. At the same time, attention has also been drawn to the need for credible exit strategies to ensure long-term fiscal sustainability and price stability (Box 1).

Merchandise Trade

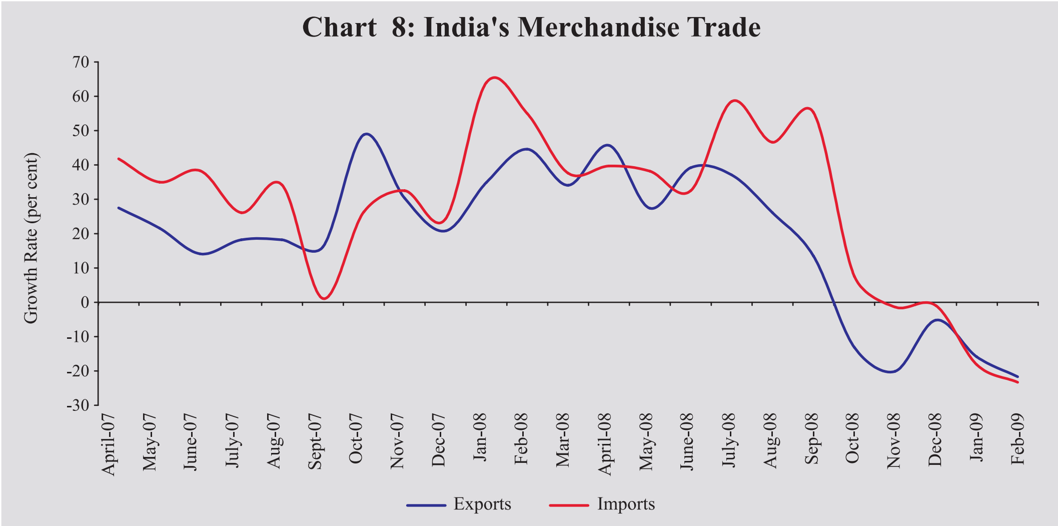
III.9 The impact of global slowdown was felt more severely on India's external demand, evident in the negative growth of merchandise exports that set in the third quarter of 2008-09. Imports growth also witnessed sharp slowdown in tandem as domestic activity slowed down rapidly. India's merchandise exports, which remained buoyant till August 2008 decelerated in September 2008 and thereafter recorded continuous negative growth till February 2009, under the impact of the global economic slowdown (Chart 8). With the result, exports during 2008-09 (April-February) recorded a lower growth of 6.4 per cent than 28.4 per cent a year ago. Imports during 2008-09 (April-February) also recorded a lower growth due to deceleration in growth of both petroleum, oil and lubricants (POL) and non-POL imports. During 2008-09 (April-February), POL imports showed a growth of 24.4 per cent lower than 35.3 per cent a year ago. Non-POL imports also exhibited moderation in growth during this period to 15.0 per cent from 42.6 per cent a year ago. Thus, merchandise trade deficit during 2008-09 (April-February) widened to US$ 113.8 billion from US $ 82.2 billion a year ago (Table 23).

Box 1: The G-20 Communique

According to the Press Communique of the meeting of the G-20 member countries held on April 2, 2009 in London, the members have planned to undertake a concerted fiscal expansion amounting to US $5 trillion to resolve the global crises. They further agreed for over US $1 trillion of additional resources for the world economy through international financial institutions and trade finance. It was agreed to treble resources available to the IMF (US $750 billion), to support a new SDR allocation (US $250 billion), to support additional lending by the Multilateral Development Banks (at least US $100 billion), to ensure support for trade finance (US $250 billion), and to use the additional resources from agreed IMF gold sales for concessional finance for the poorest countries. The G-20 countries have additionally pledged to put in place credible exit strategies to ensure long-term fiscal sustainability and price stability. The following major initiatives were agreed:

- Even-handed and independent IMF surveillance of member economies and financial sectors, of the impact of policies on others, and of risks facing the global economy.
- Establish the much greater consistency and systematic co-operation between countries, and the framework of internationally agreed high standards.
- A new Financial Stability Board (FSB) will be established with a strengthened mandate, as a successor to the Financial Stability Forum (FSF), including all G-20 countries, FSF members, Spain, and the European Commission. The FSB should collaborate with the IMF to provide early warning of macroeconomic and financial risks and the actions needed.
- Regulation and oversight should be extended to all the systemically important financial institutions, instruments and markets including, for the first time, systemically important hedge funds.
- FSB and the IMF to monitor progress, working with the Financial Action Taskforce and other relevant bodies, and to provide a report to the next meeting of the G-20 Finance Ministers in Scotland in November.
- IMF should implement the package of quota and voice reforms agreed in April 2008 and complete the next review of quotas by January 2011. For World Bank also, similar reform should be completed on an accelerated timescale, to be agreed by the 2010 Spring Meetings.
- The G-20 members have committed to refrain from raising new barriers to investment or to trade in goods and services, imposing new export restrictions, or implementing World Trade Organisation (WTO) inconsistent measures to stimulate exports.
- The G-20 members should not retreat into financial protectionism, particularly measures that constrain worldwide capital flows, especially to developing countries.

III.10 The commodity-wise exports data available for the period April-November 2008 revealed that manufactured goods continued to maintain the largest share at 64.7 per cent, followed by petroleum products (18.3 per cent) and primary



products (14.9 per cent). During April-November 2008, engineering goods and chemicals and related products showed higher growth in exports, while agriculture and allied products, ores and minerals, leather and manufactures, textiles and textile products, gems and jewellery and petroleum products showed deceleration. The handicrafts exports declined during the same period (Table 24).

Table 23: India's Merchandise Trade

(US $ billion)

Item	2007-08 R	2007-08 R	2008-09 P
		April-February	
1	2	3	4
Exports	162.9	145.6	154.9
Oil	28.4	24.3	21.6*
Non-oil	134.5	121.3	96.7*
Imports	251.4	227.9	268.7
Oil	79.6	70.6	87.8
Non-oil	171.8	157.3	181.0
Trade Balance	-88.5	-82.2	-113.8
Non-Oil Trade Balance	-37.3	-36.0	-36.4*
Variation (Per cent)			
Exports	28.9	28.4	6.4
Oil	51.8	42.6	25.3*
Non-oil	24.9	25.9	16.0*
Imports	35.4	40.2	17.9
Oil	39.4	35.3	24.4
Non-oil	33.6	42.6	15.0

R : Revised. P : Provisional.
* : April-November
Source : DGCI&S.

III.11 Destination-wise, during April-November 2008, developing countries continued to remain the major markets for India's exports with a share of 39.9 per cent, followed by OECD countries and the OPEC (Chart 9). The US with a share of 11.9 per cent continued to be the single largest export destination of India, though its share declined over the previous year. The US was followed by the UAE, Singapore, China and Hong Kong. Region-wise details available for April-November 2008 indicated that the growth rate of India's exports to major regions except the OPEC declined (Table 25).

III.12 The commodity-wise imports data for the period April-November 2008

Table 24: Exports of Principal Commodities

Commodity Group	US $ billion			Variation (Per cent)		
	2007-08	2007-08 R	2008-09 P	2007-08	2007-08	2008-09
		April-November			April-November	
1	2	3	4	5	6	7
1. Primary Products	**27.5**	**15.2**	**17.6**	**39.8**	**31.8**	**16.1**
of which:						
a) Agriculture and Allied Products	18.4	10.2	12.6	45.1	35.5	23.4
b) Ores and Minerals	9.1	5.0	5.1	30.2	24.8	1.2
2. Manufactured Goods	**102.9**	**65.4**	**76.5**	**21.2**	**20.5**	**16.9**
of which:						
a) Chemicals and Related Products	21.2	13.1	15.6	22.2	18.1	18.5
b) Engineering Goods	37.4	23.1	30.6	26.3	23.8	32.6
c) Textiles and Textile Products	19.4	12.5	12.9	11.8	11.4	3.6
d) Gems and Jewellery	19.7	13.3	13.7	23.2	28.0	3.0
3. Petroleum Products	**28.4**	**17.2**	**21.6**	**51.8**	**34.4**	**25.3**
4. Total Exports	**162.9**	**100.6**	**118.3**	**28.9**	**24.5**	**17.6**
Memo:						
Non-oil Exports	134.5	83.3	96.7	24.9	22.7	16.0

R : Revised. P : Provisional.
Source : DGCI&S.

indicated that POL imports showed sharp rise of 58.8 per cent as compared with 20.8 per cent a year ago on account of high international crude oil prices that prevailed during April-September 2008. Non-POL imports witnessed moderation in growth mainly due to decline in imports of gold and silver and electronic goods. The period (April-November 2008) also witnessed deceleration in

Chart 9: Direction of India's Exports

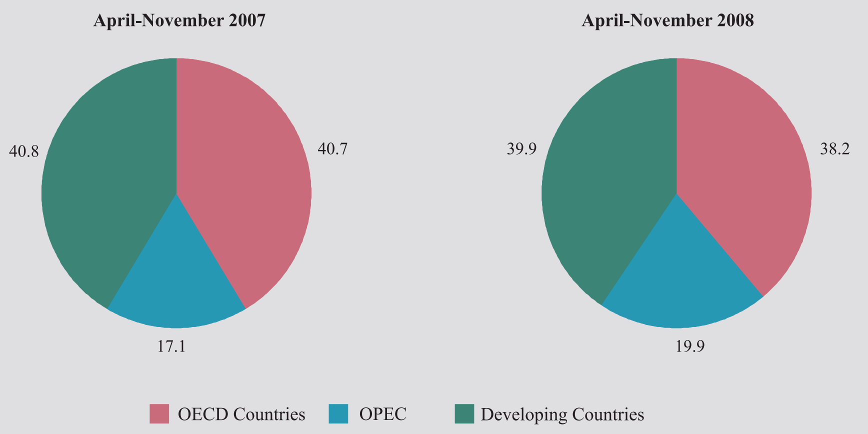


Table 25: Direction of India's Exports

Group/Country	US $ billion			Variation (Per cent)		
	2007-08	2007-08 R	2008-09 P	2007-08	2007-08	2008-09
		April-November			April-November	
1	2	3	4	5	6	7
1. OECD Countries	**62.6**	**40.9**	**45.2**	**20.4**	**20.7**	**10.5**
of which:						
EU	32.9	21.8	25.4	27.6	29.5	16.7
North America	22.0	14.5	14.9	10.0	10.2	3.1
US	20.7	13.7	14.0	9.8	10.2	2.6
2. OPEC	**26.7**	**17.2**	**23.6**	**28.8**	**25.0**	**37.2**
of which:						
UAE	15.6	10.1	13.3	29.9	25.9	31.7
3. Developing Countries	**69.6**	**41.0**	**47.2**	**37.1**	**28.4**	**15.2**
of which:						
Asia	51.5	30.0	34.3	36.9	26.2	14.3
People's Republic of China	10.8	5.9	5.2	30.6	24.4	-11.9
Singapore	7.4	4.5	6.0	21.4	7.1	33.9
4. Total Exports	**162.9**	**100.6**	**118.3**	**28.9**	**24.5**	**17.6**

R : Revised. P : Provisional.
Source : DGCI&S.

imports of iron and steel and edible oil, while fertilisers recorded higher growth (Table 26).

III.13 Source-wise, during April-November 2008, the OPEC had the highest share in India's imports, followed by

Table 26: Imports of Principal Commodities

Group/Country	US $ billion			Variation (Per cent)		
	2007-08	2007-08 R	2008-09 P	2007-08	2007-08	2008-09
		April-November			April-November	
1	2	3	4	5	6	7
Petroleum, Petroleum Products and Related Material	79.6	47.6	75.6	39.4	20.8	58.8
Edible Oil	2.6	1.9	2.1	21.4	22.4	10.1
Iron and Steel	8.7	5.9	6.8	35.3	45.8	15.0
Capital Goods	70.8	36.6	40.6	50.5	34.4	11.0
Pearls, Precious and Semi-Precious Stones	8.0	6.1	10.6	6.5	22.5	73.4
Chemicals	9.9	6.6	9.5	26.5	25.5	44.1
Gold and Silver	17.9	13.6	13.0	22.0	41.1	-4.8
Total Imports	**251.4**	**153.5**	**208.6**	**35.4**	**28.5**	**35.9**
Memo:						
Non-oil Imports	171.8	105.9	133.0	33.6	32.2	25.6
Non-oil Imports excluding Gold and Silver	153.9	92.3	120.1	35.1	31.0	30.1
Mainly Industrial Inputs*	141.7	84.1	104.6	35.4	30.3	24.4

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

developing countries and the OECD countries. China was the single largest source of imports, with a share of 10.0 per cent in total imports, followed by Saudi Arabia, the UAE, the US, Iran and Switzerland.

Balance of Payments

Current Account

III.14 The impact of the rapid shrinkage in global demand and trade was particularly felt on India's current account in Q3 of 2008-09 with widening trade deficit, some moderation in services exports and remittances and the consequent expansion in current account deficit. India's current account deficit increased to US$ 36.5 billion in April-December 2008 from US$ 15.5 billion in April-December 2007 mainly led by larger trade deficit on account of higher growth in imports coupled with a slowdown in export growth (Table 27 and Chart 10). On BoP basis, while merchandise exports increased by 17.5 per cent during April-December 2008 (21.9 per cent in April-December 2007), import payments recorded a growth of 30.6 per cent during the same period (28.3 per cent in April-December 2007). The lower growth of exports mainly reflected negative growth of 10.4 per cent during the third quarter, due to global economic slowdown. After remaining buoyant for almost six years, the growth in imports decelerated to single digit during the third quarter mainly led by lower crude oil prices. Overall, the trade deficit was higher at US$ 105.3 billion during April-December 2008 as compared with US$ 69.3 billion in April-December 2007.

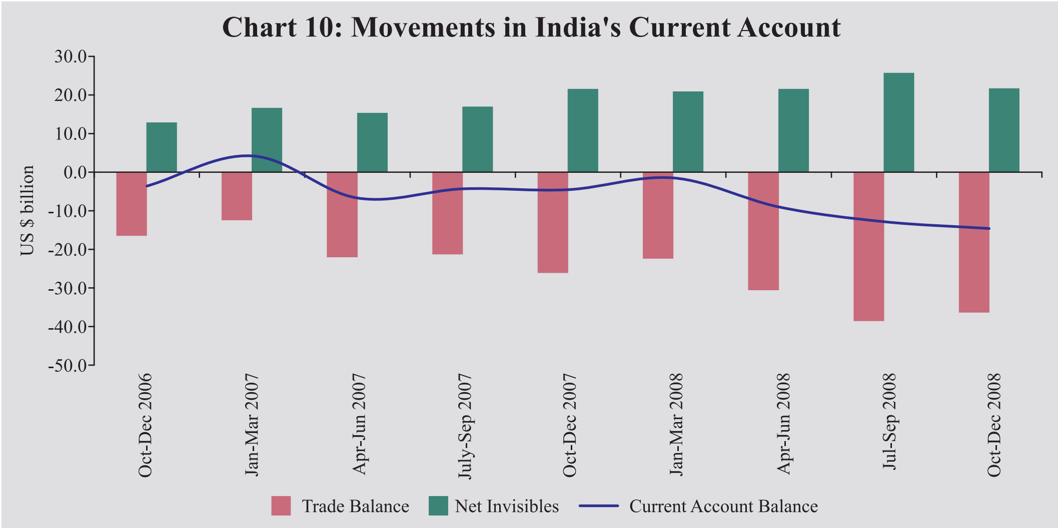
III.15 The widening of trade deficit during April-December 2008 could be attributed to higher import payments reflecting high international commodity prices, particularly crude oil prices during the first half of 2008-09 (Chart 11).

Table 27: India's Balance of Payments

(US$ billion)

Item	2007-08 PR	2007-08 PR				2008-09 P			
	Apr-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Apr-Dec	Apr-Jun	Jul-Sep	Oct-Dec	Apr-Dec
1	2	3	4	5	6	7	8	9	10
Exports	166.2	34.4	38.3	41.0	113.6	49.1	47.7	36.7	133.5
Imports	257.8	56.3	59.5	67.0	182.9	79.6	86.2	73.0	238.9
Trade Balance	-91.6	-22.0	-21.2	-26.1	-69.3	-30.5	-38.5	-36.3	-105.3
Net Invisibles	74.6	15.3	16.9	21.5	53.8	21.5	25.7	21.7	68.9
Current Account Balance	-17.0	-6.7	-4.3	-4.5	-15.5	-9.0	-12.8	-14.6	-36.5
Net Capital Account	108.0	17.8	33.2	31.0	82.0	11.1	7.9	-3.7	15.3
Overall Balance*	92.2	11.2	29.2	26.7	67.2	2.2	-4.7	-17.9	-20.4
Memo:									
Export growth (%)	28.9	15.8	17.0	33.0	21.9	43.0	24.6	-10.4	17.5
Import growth (%)	35.2	20.9	22.2	41.9	28.3	41.3	44.9	8.9	30.6
Invisibles receipts growth (%)	29.7	19.8	36.8	33.2	30.1	28.4	32.9	-0.6	18.8
Invisibles payments growth (%)	18.7	17.3	17.0	6.9	13.2	15.5	14.3	-2.1	8.7

*: Overall balance includes errors and omissions. PR: Partially Revised. P: Preliminary.



Invisibles

III.16 Gross invisibles receipts witnessed a lower growth of 18.8 per cent during April-December 2008 (30.1 per cent in the corresponding period of the previous year) mainly due to slow pace of growth in travel, business services and investment income receipts (Table 28). Similarly, invisibles payments also showed a lower growth of 8.7 per cent in April-December 2008 (13.2 per cent in April-December 2007) largely on account of slowdown in payments relating to travel, software services and a number of business and professional services. Net invisibles (invisibles receipts *minus* payments) increased by 28.1 per cent during April-December 2008, primarily led by receipts under private transfers and software services. At this level, the

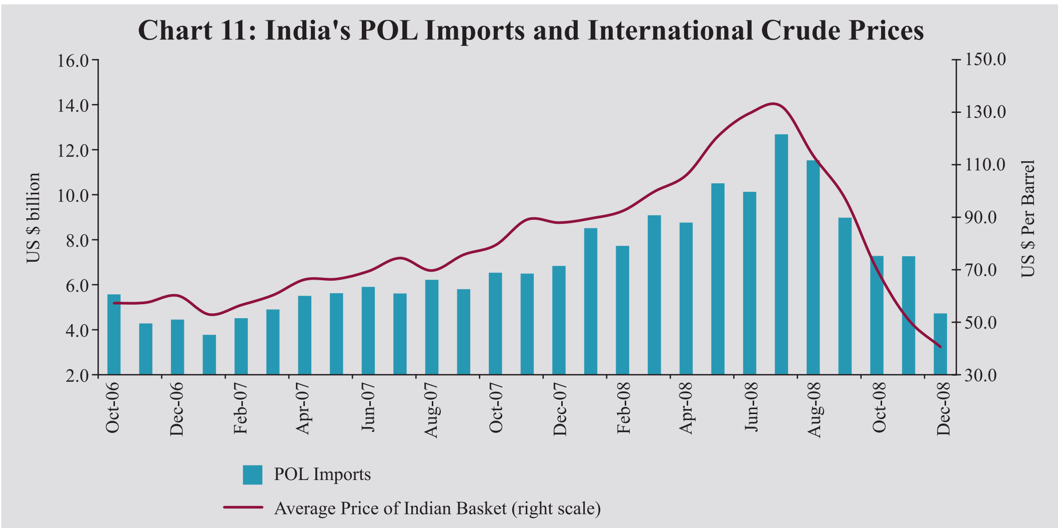


Table 28: Invisibles Gross Receipts and Payments

(US $ million)

Item	Invisibles Receipts				Invisibles Payments			
	April-March		April-December		April-March		April-December	
	2006-07	2007-08 PR	2007-08 PR	2008-09 P	2006-07	2007-08 PR	2007-08 PR	2008-09 P
1	2	3	4	5	6	7	8	9
1. Travel	9,123	11,349	7,731	8,214	6,684	9,254	6,472	6,857
2. Transportation	7,974	10,014	6,843	7,961	8,068	11,514	8,128	10,282
3. Insurance	1,195	1,639	1,152	1,058	642	1,044	730	803
4. Govt. not included elsewhere	253	330	252	308	403	376	313	438
5. Transfers	31,470	44,259	29,764	37,413	1,391	2,315	1,333	2,337
6. Income	9,308	14,268	9,587	10,909	16,639	19,185	14,244	14,250
Investment Income	8,926	13,808	9,288	10,273	15,688	18,089	13,481	13,258
Compensation of employees	382	460	299	636	951	1,096	763	992
7. Miscellaneous	55,235	66,745	48,117	56,991	28,514	30,324	18,454	19,019
Of which:								
Software	31,300	40,300	27,494	34,620	2,267	3,058	2,332	2,361
Non-Software	23,935	26,445	20,623	22,371	26,247	27,266	16,122	16,658
Total (1 to 7)	114,558	148,604	103,446	122,854	62,341	74,012	49,674	53,986

P : Preliminary. PR : Partially Revised.

invisibles surplus financed about 65.4 per cent of trade deficit during April-December 2008 as against 77.6 per cent during April-December 2007.

Capital Account

III.17 The adverse impact of the global financial market turmoil and liquidity problems on India's BoP was felt in terms of reversal of FIIs inflows and decline in long-term and short-term debt flows. A positive development was, however, turnaround in NRI flows and resilience of FDI inflows in the face of reversal of capital flows, reflecting the attractiveness of India as a long term investment destination. The capital account balance moderated during April-December 2008 mainly due to higher gross capital outflows coupled with lower gross capital inflows (Chart 12). While the gross capital inflows declined to US $ 246.4 billion during April-December 2008 from US $ 291.8 billion in April-December 2007, the gross capital outflows increased to US $ 231.1 billion from US $ 209.8 billion during the same period. The higher gross capital outflows were mainly an outcome of the developments during the third quarter of 2008-09, which was characterised by large portfolio outflows and higher repayments under short-term trade credits to India resulting in a negative quarterly capital account balance, a position last observed in the first quarter of 1998-1999.

III.18 Notwithstanding the deepening of the global financial and economic crisis, net inward FDI into India remained buoyant at US$ 27.4 billion during April-December

Chart 12: Movements in Capital Inflows and Outflows

2008 (US$ 20.0 billion in April-December 2007), reflecting the relative attraction of India as an investment destination and the continuing liberalization measures to attract FDI (Table 29). Gross inward FDI was US$ 31.7 billion during 2008-09 so far (April-February) as compared with US$ 27.6 billion in the corresponding period of the previous year (Table 30). During the same period, FDI was channeled mainly into

Table 29: Net Capital Flows

(US$ million)

Item	April-March		April-December	
	2006-07	2007-08 PR	2007-08 PR	2008-09 P
1	2	3	4	5
1. Foreign Direct Investment (FDI)	7,693	15,401	6,905	15,373
Inward FDI	22,739	34,236	20,039	27,357
Outward FDI	15,046	18,835	13,134	11,984
2. Portfolio Investment	7,060	29,556	33,292	-11,341
Of which:				
FIIs	3,226	20,327	24,471	-12,408
ADRs/GDRs	3,776	8,769	8,390	1,142
3. External Assistance	1,775	2,114	1,274	1,861
4. External Commercial Borrowings	16,103	22,633	17,410	7,114
5. NRI Deposits	4,321	179	-931	2,115
6. Banking Capital excluding NRI Deposits	-2,408	11,578	6,862	-2,244
7. Short-term Trade Credit	6,612	17,183	10,719	547
8. Rupee Debt Service	-162	-121	-45	-33
9. Other Capital	4,209	9,470	6,478	1,900
Total (1 to 9)	**45,203**	**1,07,993**	**81,964**	**15,292**

P : Preliminary. PR : Partially Revised.

Table 30:Capital Flows in 2008-09

(US $ billion)

Component	Period	2007-08	2008-09
1	2	3	4
FDI to India	April-February	27.6	31.7
FIIs (net)	April-March	20.3	(-)15.0
ADRs/GDRs	April-March	8.8	1.2
ECB Approvals	April-February	26.5	17.2
NRI Deposits (net)	April-February	(-) 0.3	2.8

FDI : Foreign Direct Investment.
FII : Foreign Institutional Investors.
ECB : External Commercial Borrowings.
NRI : Non Resident Indians.
ADR : American Depository Receipts.
GDR : Global Depository Receipts.

manufacturing (21.1 per cent) followed by financial services (17.4 per cent) and construction sector (10.1 per cent). Net outward FDI from India also continued to remain high at US$ 12.0 billion in April-December 2008 (US$ 13.1 billion invested in April-December 2007) with net outward flows of US$ 5.9 billion in Q3 of 2008-09. Thus, despite the deterioration in global credit markets, Indian companies, particularly in the mineral sector, continued their overseas expansion raising resources from the domestic markets.

III.19 Portfolio investment, primarily comprising foreign institutional investors' (FIIs) investments and American Depository Receipts (ADRs)/Global Depository Receipts (GDRs), witnessed net outflows in April-December 2008 as against net inflows in the corresponding period of the previous year. Outflows under portfolio investment were led by large sales of equities by FIIs in the Indian stock market and slowdown in net inflows under ADRs/GDRs due to drying-up of liquidity in the overseas market. During 2008-09, FIIs recorded a net outflow of US $ 15.0 billion as against net inflows of US$ 20.3 billion a year ago. In the current financial year, upto April 10, 2009, there was net inflows under FIIs to the tune of US $ 0.9 billion as against net outflows of US $ 1.5 billion during the same period last year.

III.20 Banking capital mainly consists of foreign assets and liabilities of commercial banks. NRI deposits, which constitute major part of the foreign liabilities, recorded a net inflow of US$ 2.1 billion in April-December 2008, a turnaround from net outflow of US$ 0.9 billion in April-December 2007, responding to the hikes in the ceiling interest rates on non-resident deposit schemes. Including other components, total banking capital, in net terms, turned marginally negative to US$ 0.1 billion during April-December 2008 as against net inflows of US$ 5.9 billion during April-December 2007. According to the latest available information, net inflows under NRI deposits increased to US$ 2.8 billion during April-February of 2008-09.

III.21 Reflecting the tight liquidity conditions in the overseas credit markets and increased cost of borrowings, gross inflows under external commercial borrowings (ECBs) to India moderated sharply during April-December 2008. However, ECB repayments by Indian companies increased marginally during April-December 2008. As a result, the net inflows under ECBs slowed down to US$ 7.1 billion in April-December 2008 (US$ 17.4 billion in April-December 2007).

During 2008-09 so far (April-February), approvals under ECBs remained low at US$ 17.2 billion as compared with US$ 26.5 billion a year ago.

III.22 Despite tightness in overseas credit markets, gross disbursements of short-term trade credit at US$ 31.4 billion during April-December 2008 were comparable with US$ 32.2 billion in April-December 2007. However, repayments of short-term trade credit increased to US$ 30.8 billion during April-December 2008 from US$ 21.5 billion during April-December 2007 mainly due to some problems in rollover observed during the third quarter of 2008-09. Net short-term trade credit stood at US$ 0.5 billion (inclusive of suppliers' credit up to 180 days) during April-December 2008 as compared with US$ 10.7 billion during the same period of the previous year.

Foreign Exchange Reserves

III.23 A sharp expansion in CAD in Q3 of 2008-09 alongwith net capital outflows resulted in the outgo of foreign exchange reserves to the extent of US $ 17.9 billion (excluding valuation). This magnitude of decline in reserves in a single quarter, although led to some stress on the exchange rate, was managed without creating disruptions in the financial markets. This level of decline in reserves was the highest during any one quarter in earlier years; a decline of US$ 4.7 billion in reserves was last observed in the third quarter of 2005-06. As a result of this, foreign exchange reserves on BoP basis (*i.e.*, excluding valuation) declined by US$ 20.4 billion in April-December 2008 as against accretion to reserves of US$ 67.2 billion in April-December 2007 (Chart 13). Taking into account the valuation effect, foreign exchange reserves recorded a decline of US$ 53.8 billion during April-December 2008 as against an accretion of US$ 76.1 billion in April-December 2007. Valuation losses, reflecting the depreciation of major currencies against the US dollar accounted for US$ 33.4 billion or 62.1

Chart 13: Quarterly Changes in India's Foreign Exchange Reserves

per cent of the total decline in foreign exchange reserves during April-December 2008.

III.24 India's foreign exchange reserves were US$ 252.0 billion as at end-March 2009, showing a decrease of US$ 57.7 billion over end-March 2008 (including valuation losses) (Table 31). The foreign exchange reserves, however, increased to US $ 253.0 billion as on April 10, 2009.

III.25 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 level consistent with the rate of growth, the size of the external sector in the economy and the size of risk-adjusted capital flows.

External Debt

III.26 India's external debt did not show a significant increase in Q3 of 2008-09 due to a decline in short-term debt. The ratio of short-term debt to total debt and the debt-service ratio remained at a reasonably low level. Recording an increase of around US$ 6.2 billion (2.8 per cent) over end-September 2008, India's total external debt

Table 31: Foreign Exchange Reserves

(US $ million)

Month	Gold	SDR	Foreign Currency Assets	Reserve Position in the IMF	Total (2+3+4+5)	*Memo*: Outstanding Net Forward Sales (-) / Purchases (+) of US dollar by the Reserve Bank at the end of the month
1	2	3	4	5	6	7
March 2007	6,784	2	191,924	469	199,179	–
March 2008	10,039	18	299,230	436	309,723	(+) 14,735
April 2008	9,427	18	304,225	485	314,155	(+) 17,095
May 2008	9,202	11	304,875	526	314,614	(+) 15,470
June 2008	9,208	11	302,340	528	312,087	(+) 13,700
July 2008	9,735	11	295,918	512	306,176	(+) 11,910
August 2008	8,692	4	286,117	496	295,309	(+) 9,925
September 2008	8,565	4	277,300	467	286,336	(+) 2,300
October 2008	8,382	9	244,045	447	252,883	(+) 90
November 2008	7,861	3	238,968	854	247,686	(-) 487
December 2008	8,485	3	246,603	877	255,968	(-) 1,752
January 2009	8,884	3	238,894	830	248,611	(-) 1,723
February 2009	9,746	1	238,715	816	249,278	(-) 1,953
March 2009	9,577	1	241,426	981	251,985	–
April 2009*	9,577	1	242,423	976	252,977	–

* : As on April 10, 2009. – : Not Available.

stood at US $ 230.8 billion at end-December 2008 (Table 32). The increase in external debt stock was essentially due to increase in long-term debt outstanding by US$ 9.4 billion, especially commercial borrowings and bilateral debt, during the third quarter of 2008-09. Short-term debt, however, declined by US$ 3.2 billion on account of all the components, except FII investment in government Treasury Bills and corporate debt instruments, which increased by US$ 543 million. NRI deposits declined by US$ 0.33 billion over end-September 2008 and stood at US$ 40.3 billion at end-December 2008 mainly reflecting valuation changes. The US dollar continued to be the leading currency in which India's external debt was denominated, accounting for about 53.1 per cent of total debt at end-December 2008.

III.27 Debt sustainability indicators remained at a comfortable level at end-December 2008. The debt service ratio was placed at 5.3 per cent during the third quarter of 2008-09. The ratio of short-term to total debt decreased to 20.6 per cent while the ratio of short-term debt to reserves increased to 18.5 per cent at end-December 2008 from 22.6 per cent and 17.7 per cent, respectively, at end-September 2008. India's foreign exchange reserves exceeded the external debt by US$ 25.1 billion, providing a cover of 110.9 per cent to the external debt stock at the end of December 2008.

III.28 Based on residual maturity (an important indicator for assessing the debt

Table 32: India's External Debt

(US $ million)

Item	End-March 2007	End-March 2008	End-June 2008	End-September 2008	End-December 2008
1	2	3	4	5	6
1. Multilateral	35,337	39,490	39,644	38,911	39,892
2. Bilateral	16,065	19,702	18,729	18,837	21,427
3. Trade Credit (above 1 year)	7,165	10,389	11,075	12,324	13,944
4. External Commercial Borrowings	41,443	62,504	61,231	61,568	66,158
5. NRI Deposit	41,240	43,672	42,612	40,622	40,296
6. Rupee Debt	1,951	2,016	1,866	1,707	1,652
7. Long-term (1 to 6)	143,201	177,773	175,157	173,969	183,369
8. Short-term	28,130	46,999	48,619	50,676	47,477
Total (7+8)	**171,331**	**224,772**	**223,776**	**224,645**	**230,846**
Memo:					(Per cent)
Total debt /GDP	18.1	19.0	..	..	..
Short-term/Total debt	16.4	20.9	21.7	22.6	20.6
Short-term debt/Reserves	14.1	15.2	15.6	17.7	18.5
Concessional debt/Total debt	23.1	19.7	19.1	18.5	18.7
Reserves/Total debt	116.2	137.8	139.5	127.5	110.9
Debt Service Ratio *	4.7	4.8	3.7	4.2	5.3

*: Relates to the corresponding fiscal year/quarter. .. : Not available.

service liability in the short-run), the total short-term residual maturity obligations stood at US$ 90.0 billion, which accounted for 39.0 per cent of the total external debt outstanding at end-December 2008. The total short-term debt in terms of residual maturity (US$ 90.0 billion) at end-December 2008 consists of short-term debt based on original maturity at US$ 47.5 billion and long term external debt due for payments within one year of US$ 42.5 billion. Out of these US$ 42.5 billion, the NRI deposits constitute the major portion (US$ 31.8 billion) and are expected to get rolled over.

International Investment Position

III.29 India's net international liabilities increased by US $ 10.2 billion between end-June 2008 and end-September 2008, as the decline in international assets (US $ 19.7 billion) exceeded that in international liabilities (US $ 9.5 billion) (Table 33). The decline in international assets was mainly

Table 33: International Investment Position of India

(US $ billion)

Item	March 2007 PR	March 2008 PR	June 2008 PR	September 2008 P
1	2	3	4	5
A. Assets	**247.6**	**384.1**	**377.9**	**358.2**
	(26.1)	**(32.5)**		
1. Direct Investment	30.9	49.8	52.7	55.9
2. Portfolio Investment	0.9	0.7	0.7	0.7
2.1 Equity Securities	0.5	0.6	0.6	0.6
2.2 Debt securities	0.4	0.1	0.1	0.0
3. Other Investment	16.6	23.9	12.4	15.3
3.1 Trade Credits	0.7	-0.1	-1.6	1.8
3.2 Loans	3.2	10.5	2.1	1.7
3.3 Currency and Deposits	8.5	8.2	6.4	5.5
3.4 Other Assets	4.2	5.2	5.6	6.4
4. Reserve Assets	199.2	309.7	312.1	286.3
	(21.0)	(26.2)		
B. Liabilities	**308.9**	**438.3**	**429.9**	**420.5**
	(32.6)	**(37.1)**		
1. Direct Investment	77.0	118.3	121.9	121.3
	(8.1)	(10.0)		
2. Portfolio Investment	79.4	120.1	108.2	101.8
	(8.4)	(10.2)		
2.1 Equity Securities	63.3	98.6	87.7	80.0
2.2 Debt securities	16.2	21.5	20.5	21.8
3. Other Investment	152.4	199.9	199.8	197.4
	(16.1)	(16.9)		
3.1 Trade Credits	27.7	45.2	47.5	48.2
3.2 Loans	80.9	106.9	106.4	105.6
3.3 Currency and Deposits	41.7	44.8	43.6	41.5
3.4 Other Liabilities	2.1	3.0	2.3	2.0
C. Net Position (A-B)	**-61.3**	**-54.2**	**-52.1**	**-62.2**
	(-6.5)	**(-4.6)**		

PR : Partially Revised. P : Provisional.

Note : Figures in parentheses are percentage to GDP.

on account of decrease in reserve assets amounting to US $ 25.8 billion. However, the direct investment and other investment position increased between end-June 2008 and end-September 2008. On the other hand, the decline in international liabilities is mainly attributed to outflow by FIIs from portfolio equity investment during July-September 2008 and also due to the effect of valuation changes.

IV. MONETARY CONDITIONS

The global crisis, which created intense uncertainties for funding liquidity in the face of tight market liquidity for financial instruments trading in almost all financial markets, brought to the fore the strong interactions between funding liquidity and market liquidity. As the global liquidity crisis started to affect the domestic money and foreign exchange markets in the last quarter of 2008, the Reserve Bank ensured adequate provision of both domestic and foreign exchange liquidity to the market through banks, with the aim of restoring normal functioning of the market, and thereby facilitating adequate flow of credit to the productive sectors of the economy. As the Reserve Bank's net foreign exchange assets contracted on account of provision of dollar liquidity to the market, net domestic assets were expanded through policy actions to offset the impact so that overall rupee liquidity remains comfortable. The monetary policy stance of the Reserve Bank shifted from concerns related to inflation in the first half of 2008-09 to maintaining financial stability and arresting the moderation of growth in the second half. While money supply evolved consistent with indicative projections, credit to the private sector reflected the conditions evolving in the real sector of the economy.

IV.1 Growth in monetary and liquidity aggregates during 2008-09 witnessed some moderation reflecting net capital outflows and deceleration in expansion of bank credit to the commercial sector. Broad money growth during the last quarter of 2008-09 moderated and remained marginally below the Reserve Bank's projected trajectory of 19.0 per cent for the year 2008-09. Expansion in bank credit to the commercial sector remained strong up to October 2008 on the backdrop of drying up of other sources of funds to industry but has since decelerated and remained below the Reserve Bank's Third Quarter Review projection of 24.0 per cent for the year 2008-09. The contractionary impact of decline in net foreign exchange assets on reserve money and domestic liquidity was offset by open market operations (OMO), unwinding under market stabilisation scheme (MSS) and other measures to augment rupee liquidity. Net Reserve Bank credit to Central Government increased substantially reflecting large purchases under OMO and unwinding under MSS. In response to the international financial turmoil and its possible impact on the domestic economy in the backdrop of the downturn in headline inflation, the Reserve Bank had taken a number of conventional and unconventional measures towards monetary easing since mid-September 2008. The aim of these measures was to ensure provision of ample liquidity to the banking system to make credit available for productive purposes for reviving the growth momentum.

Monetary Survey

IV.2 Broad money (M_3) growth, on a year-on-year (y-o-y) basis, was placed at 18.4 per cent at end-March 2009, which was lower than 21.2 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 – was lower at 18.2 per cent at end-March 2009 than 21.3 per cent a year ago. Similarly growth in liquidity aggregate, L_1, was lower at 17.6 per cent than 20.6 per cent a year ago (Table 34 and Chart 14).

Table 34: Monetary Indicators

(Amount in Rupees crore)

Item	Outstanding as on March 31, 2009	Variation (year-on-year)			
		Mar. 31, 2008		Mar. 31, 2009	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
I. Reserve Money (M_0)	9,87,902	2,19,412	31.0	59,600	6.4
(Reserve Money adjusted for CRR changes)		(1,72,412)	(25.3)	(1,61,850)	(19.0)
II. Narrow Money (M_1)	12,45,557	1,86,443	19.3	93,125	8.1
III. Broad Money (M_3)	47,58,504	7,01,580	21.2	7,40,932	18.4
a) Currency with the Public	6,66,095	85,475	17.7	97,815	17.2
b) Aggregate Deposits	40,86,865	6,14,546	21.7	6,46,627	18.8
i) Demand Deposits	5,73,918	99,410	20.9	-1,179	-0.2
ii) Time Deposits	35,12,947	5,15,137	21.9	6,47,806	22.6
of which:					
Non-Resident Foreign Currency Deposits	67,303	-10,525	-15.6	10,368	18.2
IV. NM_3	47,65,882	7,08,086	21.3	7,33,298	18.2
of which: Call Term Funding from FIs	1,11,739	20,668	24.1	5,235	4.9
V. a) L_1	48,79,353	7,07,388	20.6	7,31,918	17.6
of which: Postal Deposits	1,13,471	-698	-0.6	-1,380	-1.2
b) L_2	48,82,285	7,07,388	20.5	7,31,918	17.6
c) L_3	49,06,932	7,08,221	20.4	7,31,713	17.5
VI. Major Sources of Broad Money					
a) Net Bank Credit to the Government (i+ii)	12,83,165	71,612	8.6	3,77,318	41.7
i) Net Reserve Bank Credit to Government	69,913	-1,15,632	–	1,83,122	–
of which: to the Centre	69,311	-1,16,772	–	1,83,947	–
ii) Other Banks' Credit to Government	12,13,252	1,87,244	22.5	1,94,196	19.1
b) Bank Credit to the Commercial Sector	30,12,673	4,47,059	21.0	4,35,536	16.9
c) Net Foreign Exchange Assets of the Banking Sector	13,22,847	3,81,952	41.8	27,716	2.1
d) Government Currency Liability to Public	9,984	1,063	13.0	760	8.2
e) Net Non-Monetary Liabilities of the Banking Sector	8,70,165	2,00,107	35.1	1,00,399	13.0
Memo:					
Aggregate Deposits of SCBs	38,30,322	5,85,006	22.4	6,33,382	19.8
Non-food Credit of SCBs	27,23,801	4,32,846	23.0	4,06,287	17.5

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

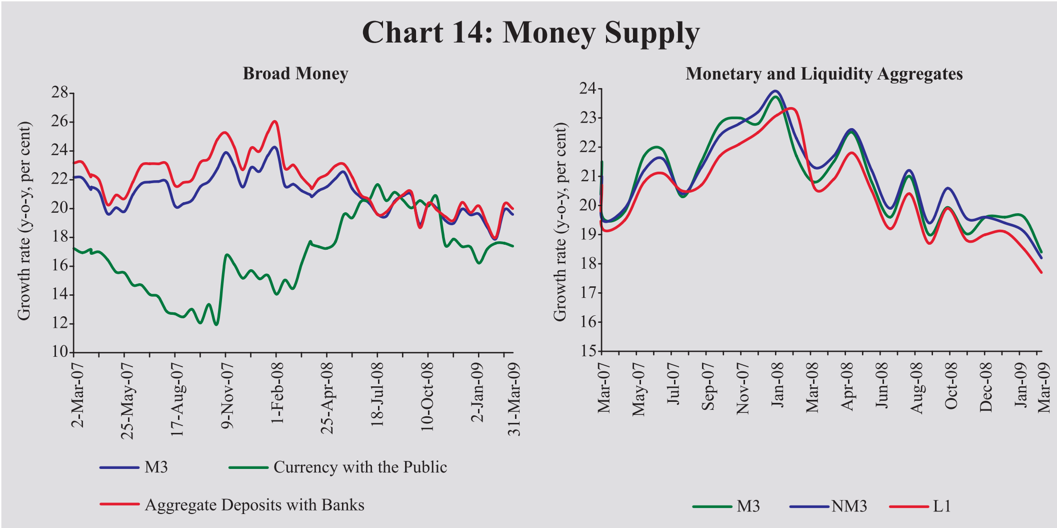
NM_3 is the residency-based broad money aggregate and L_1, L_2 and L_3 are liquidity aggregates compiled on the recommendations of the Working Group on Money Supply, 1998.

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 data for last available month are repeated as estimates.
2. Government Balances as on March 31, 2009 are before closure of accounts.



IV.3 Growth in key monetary aggregates during 2008-09 reflected changing liquidity conditions arising from domestic and global financial conditions and the necessary responses of monetary policy. The deterioration in the global financial conditions since September 2008 and capital outflows tightened domestic liquidity conditions. This necessitated the Reserve Bank to augment rupee and dollar liquidity and strengthen the credit delivery mechanisms for arresting the growth moderation through a series of policy measures. On the inflation front, WPI inflation moderated since August 2008 on account of the marked decline in international energy and commodity prices as well as slowdown in aggregate global demand due to persistence of financial market turmoil. In view of the prevailing macroeconomic scenario, the cash reserve ratio (CRR) has been reduced by a cumulative 4.0 percentage points from 9.0 per cent to 5.0 per cent since October 2008. This reduction in CRR released primary liquidity of the order of Rs.1,60,000 crore into the system. The repo rate was also reduced by a cumulative 4.0 percentage points to 5.0 per cent. The reverse repo rate was also reduced by 2.5 percentage points to 3.5 per cent (see Chapter VI, Table 66). The monetary and liquidity aggregates though remained strong, witnessed some moderation in the last quarter reflecting slowing down of economic growth.

IV.4 The moderation in broad money (M_3) growth mainly reflected a deceleration in aggregate deposits expansion during 2008-09 emanating from the downturn in economic activity. Currency in circulation remained high during the first half of 2008-09 reflecting the effects of disbursement under Farmers' Debt Waiver Scheme and the Sixth Pay Commission payouts. Currency with the public grew by 17.2 per cent (y-o-y) at end-March 2009 as compared with 17.7 per cent a year ago (Table 35). Growth in time deposits

Table 35: Monetary Aggregates – Variations

(Rupees crore)

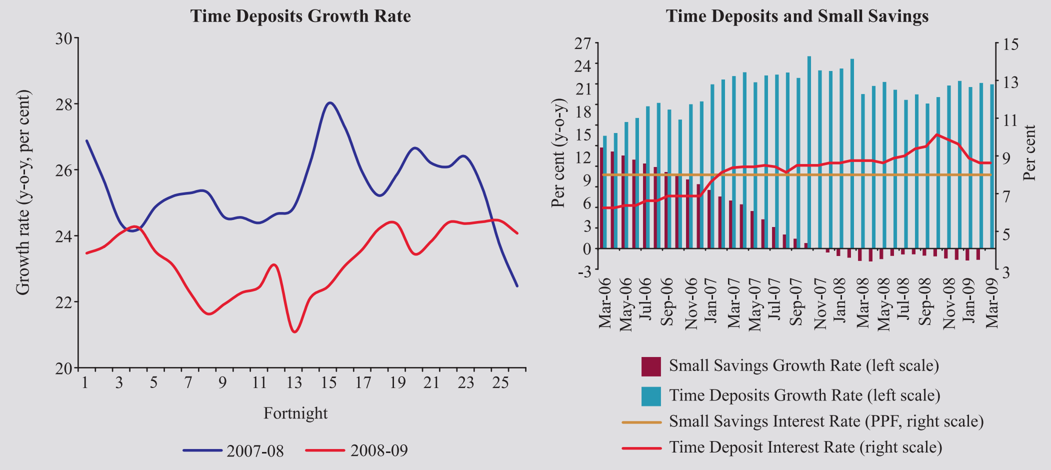
Item	2007-08	2008-09	2008-09			
			Q1	Q2	Q3	Q4
1	2	3	4	5	6	7
M_3 (1+2+3 = 4+5+6+7-8)	7,01,580 (21.2)	7,40,932 (18.4)	88,874	1,71,180	1,59,060	3,21,818
1. Currency with the Public	85,475 (17.7)	97,815 (17.2)	35,749	-17,971	40,431	39,606
2. Aggregate Deposits with Banks	6,14,546 (21.7)	6,46,627 (18.8)	57,235	1,88,636	1,11,585	2,89,171
2.1 Demand Deposits with Banks	99,410 (20.9)	-1,179 (-0.2)	-79,118	52,023	-61,730	87,646
2.2 Time Deposits with Banks	5,15,137 (21.9)	6,47,806 (22.6)	1,36,353	1,36,614	1,73,315	2,01,525
3. 'Other' Deposits with Banks	1,558 (20.8)	-3,510 (-38.8)	-4,110	514	7,045	-6,959
4. Net Bank Credit to Government	71,612 (8.6)	3,77,318 (41.7)	36,224	30,879	1,29,330	1,80,885
4.1 RBI's Net Credit to Government	-1,15,632	1,83,122	-13	51,360	30,230	1,01,545
4.1.1 RBI's Net Credit to the Centre	-1,16,772	1,83,947	1,430	51,379	29,932	1,01,206
4.2 Other Banks' Credit to Government	1,87,244	1,94,196	36,237	-20,482	99,101	79,339
5. Bank Credit to the Commercial Sector	4,47,059 (21.0)	4,35,536 (16.9)	31,107	1,59,864	88,766	1,55,799
6. NFEA of Banking Sector	3,81,952	27,716	66,858	7,271	-1,32,461	86,048
6.1 NFEA of the RBI	3,69,977	43,986	1,03,932	10,336	-1,56,330	86,048
7 Government's Currency Liabilities to the Public	1063	760	225	206	186	143
8 Net Non-Monetary Liabilities of the Banking Sector	2,00,107	1,00,399	45,541	27,040	-73,239	1,01,056
Memo:						
1. Non-resident Foreign Currency Deposits with SCBs	-10,525	10,368	2,048	3,898	-2,536	6,957
2. SCB' Call-term Borrowing from Financial Institutions	20,668	5,235	-1,116	7,015	-685	21
3. Overseas Borrowing by SCBs	12,546	-2,795	9,494	4,600	-5,185	-11,704

SCBs : Scheduled Commercial Banks. NFEA : Net Foreign Exchange Assets.
Note : 1. Data are provisional.
2. Figures in parentheses are percentage variations.

decelerated during the first two quarters of 2008-09 but witnessed robust expansion thereafter reflecting some switching of demand deposits and other savings instruments to time deposits. Time deposits recorded a higher growth of 22.6 per cent (y-o-y) at end-March 2009 as compared with 21.9 per cent a year ago. The net outflows from small savings schemes that started from December 2007 continued up to February 2009, the latest period for which the data are available (Chart 15).

IV.5 On the sources side of broad money (M_3), growth of bank credit to commercial sector decelerated and

Chart 15: Time Deposits and Small Savings

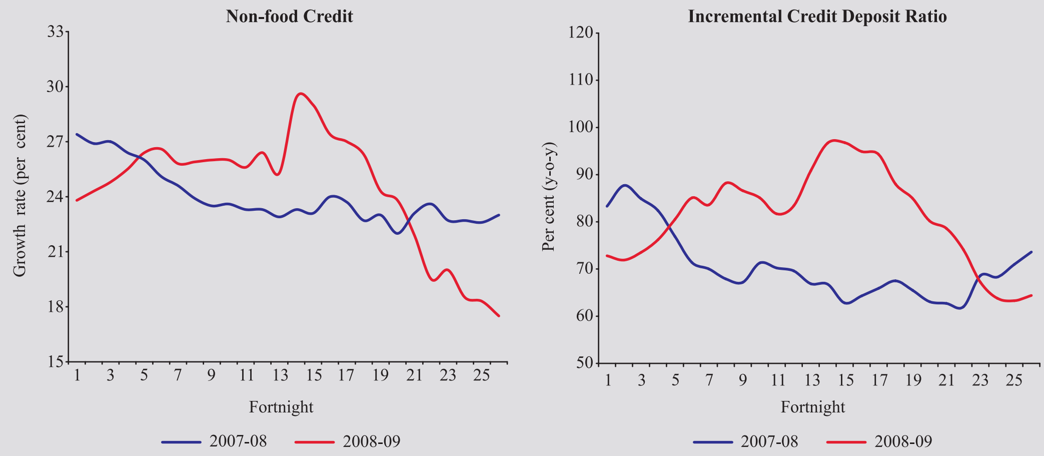


expansion in net foreign exchange assets of the banking sector moderated to a large extent. On the other hand, net Reserve Bank credit to the Centre increased reflecting the decline in outstanding balances under MSS, increase in open market operations (including purchase of oil bonds under special market operations) and decline in the Centre's surplus with the Reserve Bank. However, growth in scheduled commercial banks' (SCBs) credit to Government witnessed some moderation during this period. Bank credit to the commercial sector increased by 16.9 per cent (y-o-y) at end-March 2009 as compared with 21.0 per cent a year ago. Non-food credit growth (y-o-y) of SCBs picked up during the first two quarters of 2008-09, on the backdrop of sizeable rise in credit to petroleum sector due to the funding requirements of oil companies and substitution of funds raised by corporates from non-banking and external sources. It peaked during October-November 2008 but witnessed sustained deceleration thereafter. Non-food credit-growth (y-o-y) was 17.5 per cent at end-March 2009 as compared with 23.0 per cent a year ago (Table 36). The lower expansion in credit relative to the expansion in deposits resulted in a decline in the incremental credit-deposit ratio (y-o-y) of SCBs to 64.4 per cent at end-March 2009 from 73.6 per cent a year ago (Chart 16).

IV.6 Scheduled commercial bank's investment in SLR securities as a per cent of their net demand and time liabilities (NDTL) increased at end-March 2009 to 28.1 per cent from 27.8 per cent a year ago. However, adjusted for LAF collateral securities on an outstanding basis, SCB's holding of SLR securities amounted to Rs.11,10,156 crore or 26.7 per cent of NDTL at end-March, 2009 - implying an excess of Rs.1,13,817 crore or 2.7 per cent of NDTL over the prescribed SLR of 24.0 per cent of NDTL (Chart 17).

IV.7 Bank credit flow from scheduled commercial banks moderated to 17.3 per

Chart 16: Scheduled Commercial Banks' Credit Growth



cent (y-o-y) at end-March 2009 as compared with 22.3 per cent a year ago. The deceleration in credit expansion was observed across the banking system, but

Table 36: Scheduled Commercial Bank Survey

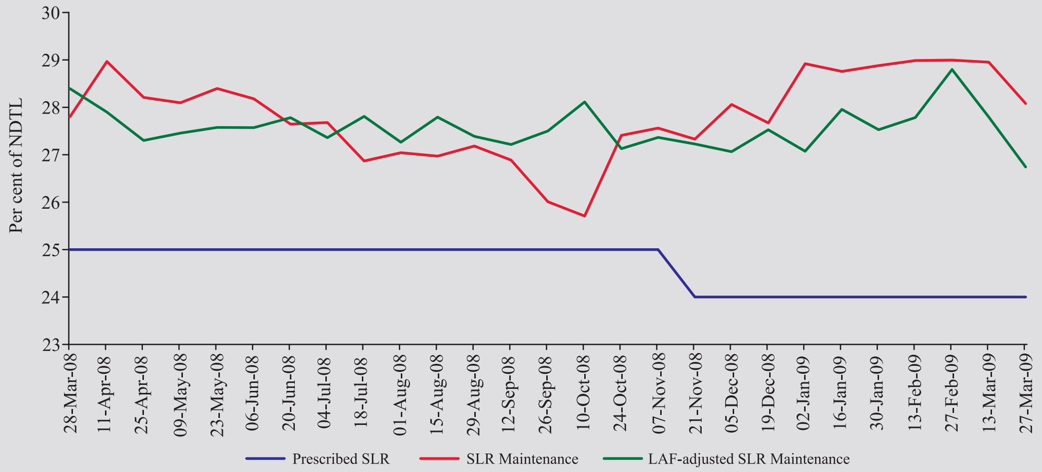
(Amount in Rupees crore)

Item	Outstanding as on Mar. 27, 2009	Variation (year-on-year)			
		As on Mar. 28, 2008		As on Mar. 27, 2009	
		Amount	Per cent	Amount	Per cent
1	2	3	4	5	6
Sources of Funds					
1. Aggregate Deposits	38,30,322	5,85,006	22.4	6,33,382	19.8
2. Call/Term Funding from Financial Institutions	1,11,739	20,668	24.1	5,235	4.9
3. Overseas Foreign Currency Borrowings	41,655	12,546	39.3	-2,795	-6.3
4. Capital	47,016	9,695	28.5	3,246	7.4
5. Reserves	2,81,673	60,126	35.6	52,821	23.1
Uses of Funds					
1. Bank Credit	27,70,012	4,30,724	22.3	4,08,099	17.3
of which: Non-food Credit	27,23,801	4,32,846	23.0	4,06,287	17.5
2. Investments in Government and Other Approved Securities	11,65,746	1,80,199	22.8	1,94,031	20.0
a) Investments in Government Securities	11,48,168	1,82,603	23.5	1,89,507	19.8
b) Investments in Other Approved Securities*	17,578	-2,405	-15.6	4,524	34.7
3. Investments in non-SLR Securities	2,11,953	30,155	21.5	41,344	24.2
4. Foreign Currency Assets	56,251	-27,564	-46.9	25,062	80.4
5. Balances with the RBI	2,38,195	76,900	42.7	-18,927	-7.4

***** : Refer 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.

Chart 17: SLR Investments by Scheduled Commercial Banks



it was sharper for the private and foreign banks (Table 37).

IV.8 Disaggregated data on sectoral deployment of gross bank credit available up to February 27, 2009 showed that 52.5 per cent of incremental non-food credit (y-o-y) was absorbed by industry as compared with 45.2 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, petroleum, coal products & nuclear fuels, iron & steel, engineering, construction and chemical & chemical products industries. Small enterprises (both small industrial and services enterprises) absorbed 15.4 per cent of the total incremental non-food credit as compared with 19.2 per cent in the same period of the previous year. The infrastructure sector alone accounted for 31.3 per cent of the incremental credit to industry as compared with 33.2 per cent in the corresponding period of the previous year. The agricultural sector absorbed 13.0

Table 37: Credit Flow from Scheduled Commercial Banks

(Amount in Rupees crore)

Item	Outstanding as on March 27, 2009	Variation (year-on-year)			
		As on March 28, 2008		As on March 27, 2009	
		Amount	Per cent	Amount	Per cent
1	2	3	4	5	6
1. Public Sector Banks	20,11,591	3,07,310	22.5	3,41,442	20.4
2. Foreign Banks	1,69,350	36,116	28.5	6,483	4.0
3. Private Banks	5,23,038	78,301	19.9	51,559	10.9
4. All Scheduled Commercial Banks*	27,70,012	4,30,724	22.3	4,08,099	17.3

*: Includes Regional Rural Banks

Note: Data are provisional.

per cent of the incremental non-food bank credit as compared with 9.2 per cent in the corresponding period of the previous year. Personal loans that accounted for 10.7 per cent of the incremental non-food credit witnessed some moderation; within personal loans, housing loans decelerated to a large extent. Growth in loans to commercial real estate and non-banking financial companies remained high (Table 38).

Table 38: Non-food Bank Credit - Sectoral Deployment

(Amount in Rupees crore)

Sector/Industry	Outstanding as on Feb. 27, 2009	Year-on-Year Variations			
		Feb. 15, 2008		Feb. 27, 2009	
		Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6
Non-food Gross Bank Credit (1 to 4)	**24,92,685**	**3,71,053**	**22.0**	**4,06,304**	**19.5**
1. Agriculture and Allied Activities	**2,97,753**	**34,013**	**16.4**	**52,742**	**21.5**
2. Industry (Small, Medium and Large)	**10,39,821**	**1,67,819**	**25.9**	**2,13,261**	**25.8**
3. Personal Loans	**5,55,392**	**58,669**	**13.2**	**43,559**	**8.5**
Housing	2,72,376	26,930	12.0	19,012	7.5
Advances against Fixed Deposits	45,779	5,773	15.6	2,872	6.7
Credit Cards	28,926	8,947	51.3	2,332	8.8
Education	27,832	5,938	40.9	7,030	33.8
Consumer Durables	8,211	525	5.9	-1,393	-14.5
4. Services	**5,99,719**	**1,10,553**	**28.4**	**96,742**	**19.2**
Transport Operators	38,638	9,669	43.3	5,783	17.6
Professional & Other Services	39,841	5,188	24.1	13,071	48.8
Trade	1,38,187	17,731	17.5	17,896	14.9
Real Estate Loans	90,765	11,361	26.7	34,533	61.4
Non-Banking Financial Companies	90,521	20,979	48.6	26,651	41.7
Memo:					
Priority Sector	**8,28,892**	**99,277**	**16.9**	**1,33,304**	**19.2**
Micro & Small Enterprises (Manufacturing & Services)	2,39,399	71,182	67.4	62,580	35.4
Industry (Small, Medium and Large)	**10,39,821**	**1,67,819**	**25.9**	**2,13,261**	**25.8**
Food Processing	53,855	11,720	32.0	5,190	10.7
Textiles	1,03,732	16,862	23.0	11,537	12.5
Paper & Paper Products	16,491	2,470	23.0	3,132	23.4
Petroleum, Coal Products & Nuclear Fuels	72,762	7,412	23.3	31,933	78.2
Chemicals and Chemical Products	73,269	7,437	13.9	11,899	19.4
Rubber, Plastic & their Products	13,269	1,355	16.1	3,368	34.0
Iron and Steel	1,00,383	11,661	19.2	27,117	37.0
Other Metal & Metal Products	30,111	3,634	18.5	6,302	26.5
Engineering	66,868	10,623	26.2	15,884	31.2
Vehicles, Vehicle Parts and Transport Equipments	35,505	7,337	38.4	7,157	25.2
Gems & Jewellery	27,242	2,073	9.3	2,454	9.9
Construction	38,207	5,856	33.3	14,141	58.8
Infrastructure	2,56,860	55,716	42.1	66,770	35.1

Note: 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, American Express Bank with Standard Chartered Bank and State Bank of Saurashtra with State Bank of India.
3. Credit growth for February 2008 has been calculated with outstanding as on February 15, 2008 to obtain variations over comparable 26 fortnights data.

IV.9 Apart from banks, the commercial sector mobilised resources from a variety of other sources such as issuances in capital markets, commercial paper, non-banking financial companies (NBFCs), financial institutions, external commercial borrowings, issuances of American Depository Receipts (ADRs)/Global Depository Receipts (GDRs) and foreign direct investment. During 2008-09, so far, flow of resources to the commercial sector declined reflecting subdued conditions in the domestic capital markets as well as deceleration of funds flow from external sources. Among the domestic sources, barring private placement and credit by housing companies, flow of resources from other sources have declined. Among the foreign sources, barring foreign direct investment, flow of resources from all other sources has declined (Table 39).

Table 39: Flow of Financial Resources to Commercial Sector

(Rupees crore)

Item	2007-08	2008-09
1	2	3
A. Adjusted non-food Bank Credit (NFC)	**4,44,807**	**4,14,902**
i) Non-Food Credit	4,32,846	4,06,287
ii) Non-SLR Investment by SCBs	11,961	8,615
B. Flow from Non-banks (B1+B2)	**3,35,698**	**2,64,138**
B1. Domestic Sources	**1,72,338**	**1,50,604**
1. Public issues by non-financial entities	51,478	14,205
2. Gross private placements by non-financial entities #	47,419	51,254
3. Net issuance of CPs subscribed by non-banks	10,660	5,365
4. Net Credit by housing finance companies **	8,693	16,438
5. Total gross accommodation by 4 RBI regulated AIFIs - NABARD, NHB, SIDBI & EXIM Bank #	4,650	9,862
6. Systemically important non-deposit taking NBFCs net of bank credit #	25,163	-12,335
7. LIC's gross investment in Corporate Debt, Infrastructure and Social Sector	24,275	65,815
B2. Foreign Sources	**1,63,360**	**1,13,534**
1. External Commercial Borrowings / FCCB #	70,382	32,765
2. ADR/GDR Issues excluding banks and financial institutions	13,023	4,788
3. Short-term Credit from abroad @	53,080	4,584
4. Foreign Direct Investment *	26,875	71,397
C. Total Flow of Financial Resources (A+B)	**7,80,505**	**6,79,040**

: Up to December 2008   * : Up to January 2009.
@ : Up to February 2009   ** : Up to September 2008.

Note: Data not comparable with those published in the *Macroeconomic Monetary Developments: Third Quarter Review 2008-09*, which were exclusive of item no. B1.7.

Reserve Money Survey

IV.10 The 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 changes in the CRR and large expansion in demand and time liabilities. In view of the inflationary pressures in the beginning of 2008-09, the Reserve Bank initially raised CRR by 150 basis points during April-August 2008-09 to 9.0 per cent. Subsequently, in view of the international financial turmoil and its possible impact on the domestic monetary and liquidity conditions on the backdrop of easing inflationary pressure, the Reserve Bank reduced CRR by a total 400 basis points since October 11, 2008. In the context of sharp changes in the CRR during 2008-09, for analytical purposes reserve money growth adjusted for the first round impact of CRR changes has become more relevant. Adjusted for the first round effect of the changes in CRR, reserve money growth (y-o-y) as on March 31, 2009 was lower at 19.0 per cent as compared with 25.3 per cent a year ago (Chart 18). On the sources side, reserve money was driven by net domestic assets during 2008-09 in contrast to net foreign exchange assets (adjusted for revaluation) being the major driver for preceding three years. The contractionary impact of decline in net foreign exchange assets on reserve money and domestic liquidity was offset by expansion of net domestic assets through open market operations (OMO), unwinding MSS and other measures to augment rupee liquidity (See Chapter V, Annex 2). Net Reserve Bank's credit to the Centre during 2008-09 increased by Rs.1,83,947 crore as against a decrease of Rs.1,16,772 crore during the corresponding period of the previous year (Table 40). The Reserve Bank's foreign currency assets (adjusted for

Chart 18: Reserve Money Growth

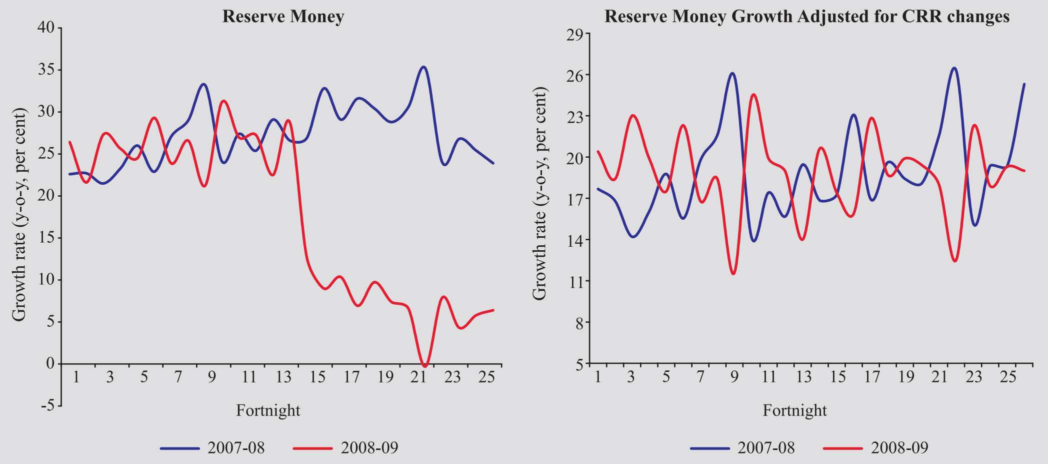


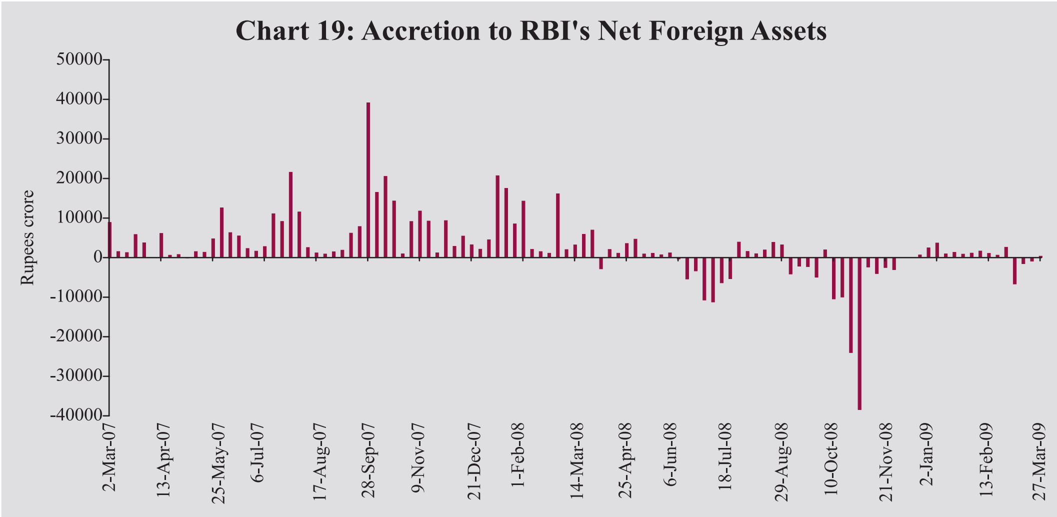
Table 40: Reserve Money - Variations

(Amount in Rupees crore)

Item	Outstanding as on Mar. 31,09	2007-08	2008-09	2008-09			
				Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8
Reserve Money	9,87,902	2,19,412	59,600	3,416	25,218	-70,452	1,01,417
		(31.0)	(6.4)				
Adjusted Reserve Money		*1,72,412*	*1,61,850*	*-24,584*	*-4,532*	*69,548*	*1,21,417*
		(25.3)	*(19.0)*				
Components (1+2+3)							
1. Currency in Circulation	6,91,083	86,702	1,00,282	36,859	-14,516	38,277	39,663
		(17.2)	(17.0)				
2. Bankers' Deposits with RBI	2,91,275	1,31,152	-37,172	-29,333	39,219	-1,15,773	68,714
		(66.5)	(-11.3)				
3. 'Other' Deposits with the RBI	5,544	1,558	-3,510	-4,110	514	7,045	-6,959
		(20.8)	(-38.8)				
Sources (1+2+3+4-5)							
1. RBI's net Credit to Government	69,913	-1,15,632	1,83,122	-13	51,360	30,230	1,01,545
of which: to Centre (i+ii+iii+iv-v)	69,311	-1,16,772	1,83,947	1,430	51,379	29,932	1,01,206
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	1,57,389	17,421	42,796	-39,239	56,975	-44,206	69,266
iv. RBI's Holdings of Rupee Coins	99	121	-34	-1	-26	27	-33
v. Central Government Deposits	88,177	1,34,314	-1,41,184	-40,670	5,570	-74,111	-31,974
2. RBI's Credit to Banks and Commercial Sector	24,177	-2,794	17,799	-3,358	4,963	5,032	11,163
3. NFEA of RBI	12,80,116	3,69,977	43,986	1,03,932	10,336	-1,56,330	86,048
		(42.7)	(3.6)				
of which :							
FCA, adjusted for revaluation	-	3,70,550	-1,00,308	15,535	-31,641	-92,102	7,900
4. Governments' Currency Liabilities to the Public	9,984	1,063	760	225	206	186	143
5. Net Non-Monetary Liabilities of RBI	3,96,289	33,202	1,86,068	97,369	41,648	-50,431	97,481
Memo:							
Net Domestic assets	-2,92,214	-1,50,565	15,614	-1,00,516	14,882	85,879	15,370
LAF- Repos (+) / Reverse Repos(-)	-1,485	21,165	-51,835	-45,350	51,480	-62,170	4,205
Net Open Market Sales # *	–	-5,923	-94,548	-8,696	-10,535	-7,669	-67,649
Centre's Surplus	16,319	26,594	-60,367	-42,427	6,199	-32,830	8,691
Mobilisation under the MSS	88,077	1,05,419	-80,315	6,040	-628	-53,754	-31,973
Net Purchases(+)/Sales(-) from Authorised Dealers	–	3,12,054	-1,60,765^	3,956	-52,761	-1,11,877	-83^
NFEA/Reserve Money @	129.6	133.2	129.6	143.8	141.1	134.7	129.6
NFEA/Currency @	185.2	209.2	185.2	213.5	220.2	183.3	185.2

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 2009.

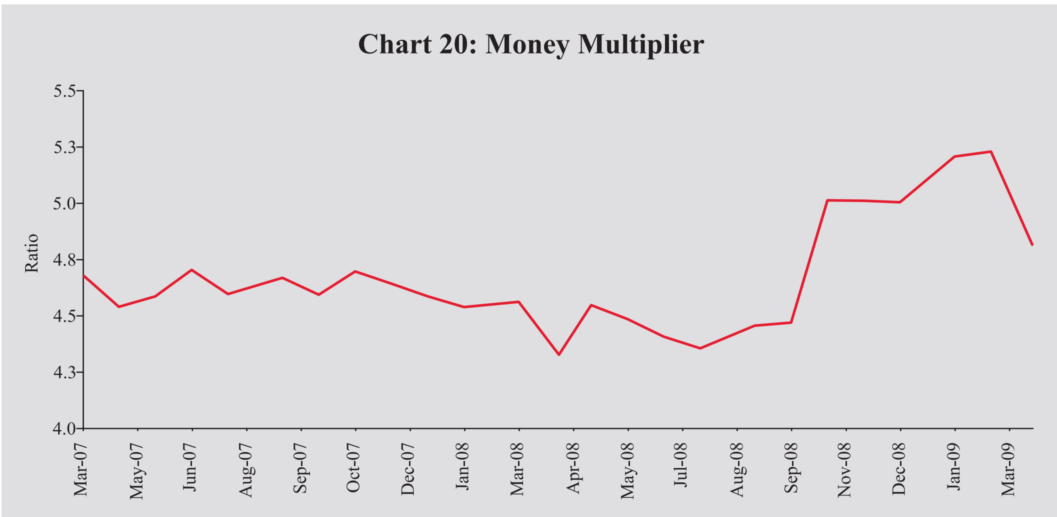
Note: 1. Data are based on March 31 for Q4 and last reporting Friday for all other quarters.
2. Figures in parentheses are percentage variations.
3. Government Balances as on March 31, 2009 are before closure of accounts.



revaluation) decreased by Rs.1,00,308 crore as against an increase of Rs.3,70,550 crore during the corresponding period of the previous year (Chart 19). Adjusted for the first round effect of the changes in CRR, reserve money growth (y-o-y) as on April 10, 2009 was at 17.3 per cent as compared with 20.4 per cent a year ago

IV.11 The changes in CRR have impacted the money multiplier, *i.e.*, the ratio between broad money and reserve money. The money multiplier, which had declined from 4.7 at end-March 2007 to 4.3 at end-March 2008 in the wake of CRR hikes, increased to 4.8 at end-March 2009, reflecting subsequent lowering of CRR (Chart 20).

IV.12 Movements in the net Reserve Bank's credit to the Central Government during 2008-09 largely reflected the



liquidity management operations by the Reserve Bank and changes in Central Government deposits with the Reserve Bank. In particular, the net Reserve Bank's credit to the Central Government increased on account of the Reserve Bank's purchases under OMO, decline in Centre's cash balances with the Reserve Bank and unwinding of balances under MSS (details in Chapter V, see Table 47).

V. FINANCIAL MARKETS

The process of deleveraging and dysfunctional financial markets in the advanced economies accentuating a global financial crisis has highlighted the importance of orderly functioning of markets for achieving macroeconomic objectives. In the third quarter of 2008-09, when liquidity dried down in the global money markets and the credit markets almost froze, there were knock-on effects on the domestic money and foreign exchange markets, which prompted the Reserve Bank to initiate measures to ensure adequate provision of both rupee and foreign exchange liquidity in the market. While orderly conditions were restored in the money market by November 2008, the pressure on the exchange rate continued, alongside pressure on the country's balance of payments and draw down of foreign exchange reserves. The equity markets followed the general global sentiments and market trends and after a phase of sharp downward movement, the market has shown some recovery since March 2009. In the government securities market, reflecting the economy's need for large fiscal stimulus, the gross market borrowings of the Government in 2008-09 were substantially higher than that for 2007-08. The entire market borrowing programme was managed smoothly by the Reserve Bank. In the credit market, following significant reduction in policy rates by the Reserve Bank, the lending rates of banks have begun to exhibit some moderation. In the context of the high volatility that was witnessed in global financial markets in 2008-09, one notable aspect of the Indian financial markets was that all segments functioned normally, with occasional volatility for short periods.

V.1 The subprime crisis, that emerged in the US housing mortgage market in the second half of 2007, snowballed into a global financial crisis and a global economic crisis. The global financial landscape changed significantly during the course of 2008-09 wherein several large international financial institutions either failed or were restructured, with the support of very large goverment interventions in many countries, to prevent imminent collapse. The significant deterioration in global financial conditions since mid-September 2008, led to severe disruptions in the short-term funding markets, widening of risk spreads, sharp fall in equity prices and inactivity in the markets for asset-backed securities. Consequently, the strain on the balance sheets of financial institutions increased, threatening the viability of some of the most well known financial entities in the world. The freezing up of credit markets necessitated extraordinary actions on the part of central banks and governments in countries across the world to mitigate the systemic risks posed by the ongoing financial crisis.

V.2 To restore confidence and facilitate orderly functioning of markets, central banks have been responding through both conventional and unconventional measures and there have been instances of coordinated policy actions by the central banks. The conventional measure of monetary easing has been achieved through policy rate cuts which has taken the policy rate to nearly zero as in the case of the US and to an all-time low of 0.5 per cent as in the case of UK and 1.25 per cent in the Euro area. The other measures include lending by central banks to non-banks, large-scale provision of term-funding in local currency and dollar markets and expansion of the range of acceptable collateral for receiving funding from the central bank. Further, steps have been taken to deal with distressed assets and provide liquidity, including through bank recapitalisation.

V.3 The important initiatives taken by the US Federal Reserve, besides reduction of the federal funds rate, include conducting direct purchases of agency debt and agency mortgage-backed securities, broadening of liquidity programmes to financial intermediaries and other central banks and initiating programmes in support of systemically important market segments. The US government entities also undertook extraordinary initiatives to support the financial sector by injecting capital into the banking system and providing guarantees on select liabilities of depository institutions. Many foreign central banks and governments took similar steps. Despite the host of measures taken in most countries, normalcy continues to elude the international financial markets. This has contributed to the continued uncertainty and deterioration of the world economic outlook. The financial markets need to be stabilised in order to achieve a turnaround in global growth conditions.

V.4 Restoring investor confidence is key to achieving financial stability. In this context, there is a paramount need to deal with distressed assets and recapitalise vital institutions. This entails substantial contribution from governments for support of the financial sector. Simultaneously, governments have been addressing the recession through growth stimulus packages, while the tax receipts are likely to reduce in the face of the economic downturn. The longer it takes to effectively implement the support packages for the financial sector, the negative feedback transmitting from the financial sector to the real sector may lead to more protracted recession. The US government and the Federal Reserve have initiated programmes for systemically important segments/institutions of the financial market. The authorities are conducting severe stress tests on all the major banks, and if they are found short of capital required under more severe but plausible scenarios, they could fill the gap by recourse to private financing or through temporary capital buffers made available by the government. The US Treasury, in conjunction with the Federal Deposit Insurance Corporation and the Federal Reserve, has announced the details of a Public-Private Investment Programme which would use US$ 75-100 billion of Troubled Assets Relief Programme (TARP) capital and capital from private investors and seek to generate US$ 500 billion in purchasing power to buy legacy assets, with the potential to expand to US$ 1 trillion over time.

V.5 Due to the inter-linkages in the global financial markets, the ramifications of developments in the advanced economies are felt in the emerging economies. Hence, there needs to be greater coordination and cooperation amongst the policy-making bodies so as to restore trust in the markets. In this regard, the Basel Committee on Banking Supervision and the Financial Stability Forum, to be known as Financial Stability Board in its expanded version, have extended their membership to a number of emerging market economies including India.

V.6 The knock-on effects of the international developments spilled into the Indian financial markets in mid-September 2008. The Reserve Bank, like most central banks, has since taken a number of conventional and unconventional measures to augment the domestic and foreign exchange liquidity and address the supply constraints impacting the growth momentum in the domestic economy. An important distinction between the actions taken by the Reserve Bank and other central banks is that the interaction is still largely through the banking channel and even the measures aimed at addressing the liquidity and redemption needs of mutual funds, non-banking financial companies (NBFCs) and housing finance companies are directed through the banks[1]. Another notable distinction is that there has not been any dilution of the collateral taken by the Reserve Bank. The array of instruments available allow for flexibility in Reserve Bank's operations. Liquidity modulation through flexible use of a combination of instruments, to a significant extent, cushioned the impact of the international financial turbulence on domestic financial markets by absorbing excessive market pressures and ensuring orderly conditions. Thus, liquidity pressures were evident in India for a temporary period in September and October 2008. The Indian financial markets are robust and working normally with no dislocations in the foreign exchange, money and government securities markets.

International Financial Markets

V.7 Since mid-October 2008, the developments in the international financial markets have been largely conditioned by the policy responses to the crisis. The pricing behaviour has begun to mirror the strains of the ongoing economic recession and prices have been decidedly volatile given the environment of heightened uncertainty. Pressure on credit market persists in the wake of recession in many economies and subdued corporate performance, which has given rise to the expectation of possible increase in defaults. During the fourth quarter of 2008-09, the equity valuations generally remained low on account of concerns stemming from the weak financial and economic outlook.

Money Markets

V.8 The policies initiated by central banks and the guarantees offered by governments assuaged to an extent the

[1] The Government of India had announced an arrangement for providing liquidity support to meet the temporary liquidity mismatches for eligible Systemically Important Non-Deposit taking Non-Banking Financial Companies (NBFC-ND-SI) through the Industrial Development Bank of India Stressed Asset Stabilisation Fund Trust, which has been notified as a Special Purpose Vehicle for undertaking this operation.

funding pressures that were evident in the international financial markets during September and October 2008. The spreads between Libor and overnight index swaps (OIS) have been gradually narrowing. In the UK, however, bank funding markets came under renewed pressure. The Sterling Libor-OIS spreads slightly widened and the interbank term-lending remained subdued during late January and February 2009.

V.9 The benchmark credit default swap (CDS) indices have shown significant spread volatility since end-November 2008 up to the fourth quarter of 2008-09. Investment grade spreads, however, mostly performed better than the lower-rated borrowers. For instance, between end-November 2008 and end-February 2009, the US five-year CDX high-yield index spread had risen by 148 basis points, while the investment grade spreads registered a decline of 28 basis points. The same pattern was exhibited by the European CDS indices. As problems persist in the banking sector internationally and recessionary conditions have become widespread, it is expected that default rates will increase. Risk tolerance in the market is low and lower-rated spreads are expected to see increased volatility. In March 2009, the Federal Reserve approved the application of the ICE Trust to become a member of the Federal Reserve system. The ICE trust would provide central counterparty services for CDS contracts conducted by its participants. Under the arrangement, the ICE Trust would work towards reducing the risk associated with the trading and settlement of CDS transactions by assuming counterparty credit risk and enforcing participation standards and margin requirements.

V.10 As spreads continued to be affected by financial market concerns, in January 2009, the authorities in the UK announced a further broad-based package for rescue of the financial institutions in the country. Additional support measures were announced by other European countries as well. However, as concerns mounted over the fiscal implications of the support packages and the depressed risk appetite, spreads on sovereign CDS rose during the first three months of 2009.

V.11 Recent measures taken by the governments and central banks do seem to be having a favourable impact on certain segments of the money and credit markets, which had faced severe disruptions during the acute phase of the crisis in the third quarter of 2008-09. For instance, the US government's announcement in November 2008 and the subsequent initiation of a programme for purchase of up to US$ 100 billion of direct obligations of housing-related government-sponsored enterprises and up to US$ 500 billion of mortgage-backed securities (MBS) backed by Fannie Mae, Freddie Mac, and Ginnie Mae has helped in reducing spreads on agency debt and the conditions for high-quality borrowers in the primary residential mortgage market recovered to an extent. In March 2009, the Federal Open Market Committee also announced plans to purchase an additional US$ 750 billion of agency MBS and invest an additional US$ 100 billion in agency debt. The Committee also announced that it would buy up to US$ 300 billion of longer-term Treasury securities over the next six months to help improve conditions in private credit markets.

V.12 The Federal Reserve launched the Term-Asset Backed Securities Loan Facility (TALF) on March 3, 2009 in an attempt to unfreeze markets for securities backed by loans. Spreads in the areas where the programme is focussed – pooled credit card, auto, student and small business loans – narrowed during the first two months of 2009 in anticipation of TALF and narrowed considerably in March with the launch of the programme. The first tranche of funding under TALF was settled on March 25, 2009.

V.13 The banking sector in the US and Europe continued to show further signs of problems, despite the massive injection of capital by the government and from private sources since late 2007. Notable instances of governments picking up or hiking their stakes in financial entities during the fourth quarter of 2008-09 include the German government taking a 25 per cent stake in the merged entity of Commerzbank and Dresdner Bank, the US authorities' investment of US $ 20 billion in Bank of America through a preferred equity stake and the UK government restructuring its investment in the Royal Bank of Scotland. The UK authorities continued to announce a series of measures during the fourth quarter of 2008-09 for enabling sufficient credit flow to households and businesses. These measures include capping the losses on banks' holdings of risky assets, state guarantees to facilitate bank funding and purchase of commercial paper, corporate bonds and other securities to enhance credit availability in the economy. In March 2009, the Bank of England embarked upon a policy of credit/quantitative easing entailing the purchase of £ 75 billion worth of conventional gilts and notified private sector assets in the secondary market, in a bid to support the flow of corporate credit. The UK programme has resulted in significantly lower yields for the gilts, which the Bank has agreed to buy. Corporate bond yields have also fallen. By the first week of April 2009, £ 26 billion of asset purchases had been made and it is expected that the programme will be completed in another two months. In April 2009, the Bank of Japan announced that it would offer credit-worthy commercial banks subordinated loans worth up to ¥1 trillion to smoothen financial intermediation in the country. The programme is likely to commence in May 2009.

Short-term Interest Rates

V.14 The easing of short-term interest rates in advanced economies persisted in the fourth quarter of 2008-09, as policy rates continued to be cut with inflation concerns disappearing and the recession in most advanced economies turning out to be deeper and more protracted than was earlier estimated (Table 41). The US federal funds rate remains in the range of 0.0-0.25 per cent set in mid-December 2008. The Bank of England effected a 50 basis point cut in policy rates in each of

Table 41: Short-term Interest Rates

(Per cent)

Region/Country	End of					
	March 2007	March 2008	June 2008	Sept 2008	Dec 2008	March 2009
1	2	3	4	5	6	7
Advanced Economies						
Euro Area	3.91	4.72	4.96	5.07	2.97	1.50
Japan	0.57	0.75	0.75	0.75	0.62	0.54
UK	5.55	6.01	5.93	6.25	2.73	1.70
US	5.23	2.26	2.29	2.04	0.44	0.50
Emerging Market Economies						
Argentina	9.63	10.44	16.50	13.81	19.56	14.44
Brazil	12.68	11.18	12.17	13.66	13.66	11.16
China	2.86	4.50	4.48	4.31	1.86	1.22
Hong Kong	4.17	1.83	2.33	3.66	1.00	0.90
India	**7.98**	**7.23**	**8.73**	**8.56**	**5.04**	**4.95**
Malaysia	3.64	3.62	3.69	3.70	3.40	2.09
Philippines	5.31	6.44	6.00	4.00	5.25	4.50
Singapore	3.00	1.38	1.25	1.75	0.91	0.56
South Korea	4.94	5.32	5.36	5.78	3.98	2.41
Thailand	4.45	3.25	3.65	3.85	3.85	1.80

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

the three months of the fourth quarter of 2008-09. As of March 5, 2009, the official bank rate was at an all-time low of 0.5 per cent. The ECB has reduced its policy rates by 300 basis points since October 2008, the rate for main refinancing operations thus stands reduced to 1.25 per cent. The softening of interest rates was broad-based and across the spectrum, as emerging economies also saw frequent cuts in policy rates and liquidity injections by the authorities. Countries that effected cuts in policy rates during the fourth quarter of 2008-09 include Turkey (cumulative reduction of 725 basis points since October 2008), South Africa (cumulative reduction of 250 basis points since October 2008) and South Korea (cumulative reduction of 300 basis points since October 2008). The policy rate cuts by the Czech Republic, Peru, Sri Lanka, Chile, Egypt, Canada, Poland, Malaysia, New Zealand, Iceland and Brazil, during the fourth quarter of 2008-09, ranged from 50 basis points to 600 basis points.

Government Bond Yields

V.15 There has been much volatility in the government bond yields because even as most advanced economies are facing a recession, concerns have mounted over the increased borrowing requirements of the governments. This contributed to the increase in the 10-year government bond yields in some advanced countries during the fourth quarter of 2008-09. The 10-year government bond yield in the US increased by 72 basis points between December 29, 2008 and April 8, 2009. During the same period, yields on 10-year government papers increased by 34 basis points in the Euro area, 20 basis points in Japan and 15 basis points in the UK (Chart 21).

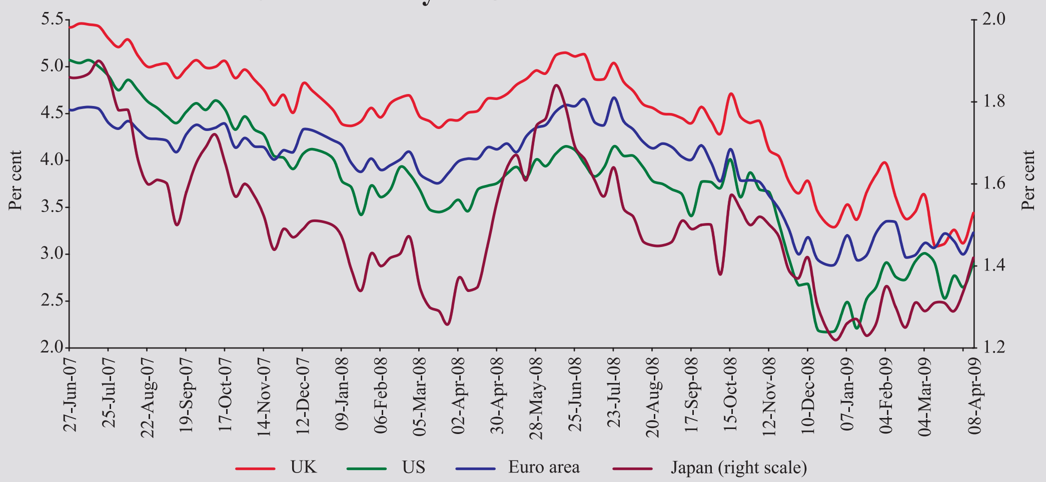
Foreign Exchange Markets

V.16 The international financial markets witnessed extreme dislocations in the period immediately following the collapse of the Lehman Brothers in mid-September 2008. The volatility in the markets, which peaked by end-2008, moderated somewhat in 2009. Due to the unwinding of carry trade positions and low risk appetite, the yen appreciated against most other currencies, including the US dollar during 2008-09. However, beginning mid-February 2009 up to mid-April 2009, the yen has generally depreciated against the US dollar.

V.17 Although, the foreign exchange swap spreads have begun to soften, the foreign exchange markets remained strained for most countries during the first quarter of 2009. The Bank of Mexico had to directly intervene in the foreign-exchange markets for the first time in more than a decade in February 2009 because of the severity of the impact of the crisis on its currency trading. Four eastern European central banks (of Romania, Hungary, Poland and the Czech Republic) announced that they would make coordinated effort to bolster their currencies as the sharp depreciations experienced by their respective currencies were not in line with the economic fundamentals.

V.18 The US dollar, generally, appreciated against most of the currencies

Chart 21: 10-year Government Bond Yields



as the US investors were liquidating their positions in overseas equity and bond markets and repatriating the money back to the US. Notwithstanding the deepening of the financial crisis and weakness in economic activity in the US, the flight to safety considerations helped strengthen the US dollar. During 2008-09, the US dollar appreciated against most major currencies including the euro and the pound sterling. The US dollar, however, depreciated against the Japanese yen, as a result of unwinding of carry trades. Amongst Asian currencies also, the US dollar appreciated against Korean won, Thai baht, Malaysian ringgit, Indonesian rupiah and Indian rupee but depreciated against Chinese yuan. As on April 14, 2009, however, the US dollar depreciated against most major currencies, except the euro and the Japanese yen, over end-March 2009 levels (Table 42).

Table 42: Appreciation (+)/ Depreciation (-) of the US dollar *vis-à-vis* other Currencies

(Per cent)

Currency	End-March 2008 @	End-March 2009 @	April 14, 2009*
1	2	3	4
Euro	-15.77	18.82	0.24
Pound Sterling	-1.53	38.67	-3.78
Japanese Yen	-14.92	-2.00	1.78
Chinese Yuan	-9.34	-2.61	-0.09
Russian Ruble	-9.68	44.25	-1.52
Turkish Lira	-5.75	27.69	-6.03
Indian Rupee	-8.30	27.47	-2.15
Indonesian Rupiah	1.09	25.58	-5.13
Malaysian Ringgit	-7.77	14.42	-1.41
South Korean Won	5.47	38.86	-3.26
Thai Baht	-10.16	12.85	-0.24
Argentine Peso	2.08	17.32	-0.84
Brazilian Real	-16.99	31.20	-3.02
Mexican Peso	-3.48	32.90	-7.53
South African Rand	11.34	17.22	-4.95

@ : Year-on-year variation.
* : Variation over end-March 2009.

Equity Markets

V.19 The year 2008-09 continued to be a dismal year for the stock markets. As a reflection of the economic and financial market outlook, the year was characterised by depressed equity valuations. Equity price indices in most advanced economies were relatively flat during July and August 2008, but caught on the downward spiral subsequently, which continued into the first two months of 2009 (Table 43).

V.20 Consequently, price/earnings ratios in most markets across the world followed a downward trend. They remained at or close to all-time low levels for most regions during the fourth quarter of 2008-09. Though the decline in equity valuations was broad-based across all sectors, financial institutions, particularly in Japan, were the worst sufferers. The volatility in the markets in the fourth quarter was compounded by the lack of detailed information about government rescue packages. The equity markets saw a slight recovery in most countries/regions since mid-March 2009, helped further by the US government announcing the details of the public-private investment programme aimed at repairing balance sheets of financial institutions.

Emerging Markets

V.21 The ongoing crisis has invalidated the 'decoupling hypothesis', as emerging economies too have been hit by the crisis.

Table 43: International Stock Markets

Country/Index	Percentage Variation (year-on-year)		
	End-March 2007	End-March 2008	End-March 2009
1	2	3	4
Developed Markets			
US (Dow Jones)	11.2	-0.7	-38.0
US (NASDAQ)	3.5	-5.9	-32.9
FTSE UK 100	5.8	-9.6	-31.2
Euro area (FTSE 100)	7.5	-15.7	-40.1
Japan (Nikkei 225)	1.3	-27.6	-35.3
Hong Kong (Hang Seng)	25.3	15.4	-40.6
Emerging Markets			
Russia	34.9	6.1	-66.4
Brazil	20.7	33.1	-32.9
Colombia	-3.7	-16.0	-10.6
South Africa	34.3	11.5	-32.7
South Korea	6.8	17.3	-29.2
Hungary	1.6	-7.3	-49.0
Singapore	28.2	-4.9	-43.5
Malaysia	34.6	0.1	-30.1
Argentina	16.8	0.0	-46.5
Turkey	1.8	-10.6	-34.0
Indonesia	38.4	33.7	-41.4
India	**15.9**	**19.7**	**-37.9**
Thailand	-8.1	21.3	-47.2
China	145.2	9.1	-31.7
Memo:			
World (MSCI)	13.4	-5.1	-44.0
EMEs (MSCI)	17.9	18.9	-48.4

Source : Bloomberg.

Even though institutions in most of the emerging economies did not have direct exposure to the toxic assets, these economies are suffering the consequences of the economic recession that has gripped the advanced economies. The emerging market economies witnessed capital flow reversals, sharp widening of spreads on sovereign and corporate debt and abrupt currency depreciations during 2008-09. Banks have curtailed their lending to emerging economies as reflected in the near halving of the total volume of international syndicated loan facilities given to borrowers in emerging markets in the last quarter of 2008 as against the corresponding period of the previous year.

V.22 The central and east European economies seem to have suffered the brunt of the global financial markets upheaval, given their large current account deficits. Banks in most of these countries are in need of government support in the form of recapitalisation. Several emerging eastern European countries, including Hungary, Romania and Ukraine, have sought IMF support to stabilise their financial markets. The emerging economies of Europe which saw plummeting valuations in equity markets include the Czech Republic, Hungary, Poland and Russia. During the fourth quarter of 2008-09, the foreign exchange markets of most emerging market economies continued to be under pressure. The Russian rouble continued the downward spiral against both the US dollar and the euro, with the plunge being particularly persistent during the fourth quarter of 2008-09. Some other currencies that suffered sharp losses during the period include the Czech koruna, the Hungarian forint, the Polish zloty, the Brazilian real, the Korean won, the Mexican peso and the Indonesian rupiah. Ten ASEAN members and China, Japan and Korea have together pledged US$ 120 billion to counter the risk of a currency collapse in the region by enhancing the total size of the multilateralised Chiang Mai Initiative.

Sovereign credit spreads in select emerging market economies showed improvement over the levels that were seen in October 2008. However, for most low-rated Latin American and Eastern European issuers, the spreads continued to be at record highs.

V.23 Though emerging market economies, including India, do not have direct or significant exposure to stressed financial instruments or troubled financial institutions, they are not immune to the adverse effects of the financial crisis. During the fourth quarter of 2008-09, a number of countries announced further measures for monetary easing, provision of liquidity and restructuring/ recapitalisation of the financial system (Table 44).

Table 44: Recent Global Response to Financial Market Turmoil

Country	Key Measures
1	2
United States	**Monetary Policy Easing** • The target range for federal funds rate was set between 0.00 and 0.25 per cent on December 16, 2008 and has remained unchanged since then. **Liquidity Provision** • Term funds continued to be auctioned through new channels such as the Term Auction Facility (TAF). • The set of eligible collateral for loans extended by the Term Asset-Backed Securities Loan Facility (TALF) was expanded to include four additional categories of asset-backed securities. • Five liquidity facilities – the Primary Dealer Credit Facility (PDCF), the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF), the Commercial Paper Funding Facility (CPFF), the Money Market Investor Funding Facility (MMIFF) and the Term Securities Lending Facility (TSLF) – were extended up to October 30, 2009. • The Temporary Money Market Funds Guarantee Program extended up to September 18, 2009. • The set of institutions eligible to participate in the MMIFF was expanded. Several economic parameters of the MMIFF were adjusted so that it remained a viable source of back-up liquidity for money market investors even at very low levels of money market interest rates. • The Federal Reserve to purchase US$ 1.25 trillion of agency mortgage-backed securities and US$ 200 billion of agency debt in 2009. • The Federal Reserve to purchase US$ 300 billion of longer-term Treasury securities by September 2009. • A Public-Private Investment Programme to generate purchasing power of up to US$ 1 trillion to buy legacy assets. **Recapitalisation of the Financial System** • Restructuring of Government's financial support to the American International Group (AIG) was announced in March 2009. • The US government entered into an agreement with Bank of America to provide a package of guarantees, liquidity access and capital. • The US Treasury to participate in Citigroup's exchange offering by converting a portion of its preferred security to common equity alongside the other preferred holders. • Community Development Financial Institutions (CDFI) Fund announced to award nearly US$ 100 million in grants and US$ 3 billion in additional tax credit authority to support community-based financial institutions such as loan funds, credit unions, banks, venture capital firms and other financing entities. • Total Capital Purchase Program (CPP) investment of US$ 195.3 billion in 359 institutions since October 2008. • Capital Assistance Programme announced for the major US banking institutions.

(Contd...)

Table 44: Recent Global Response to Financial Market Turmoil *(Concld.)*

Country	Key Measures
1	2
	Other Measures • A policy announced to help avoid preventable foreclosures on certain residential mortgage assets held, owned or controlled by a Federal Reserve Bank. • Application of the ICE trust to provide central counterparty services for certain CDS contracts was approved.
United Kingdom	**Monetary Policy Easing** • Official bank rate was cut thrice by 50 basis points (bps) each during January-March, 2009 to 0.5 per cent. **Liquidity Provision** • Asset Purchase Facility to buy gilts, commercial paper and corporate bonds from the secondary market using central bank reserves amounting to £ 75 billion. • Extension of the drawdown window of the Credit Guarantee Scheme (CGS) up to December 31, 2009. • Extension of the term of the Bank of England's permanent discount window facility to 364 days for an additional fee of 25 bps. **Financial Restructuring** • The UK Treasury's preference share investment in RBS was converted to ordinary shares. **Recapitalisation of the Financial System** • Asset Protection Scheme, which aims to remove uncertainty about the value of banks' past investments, clean up banks' balance sheets and enable them to rebuild and restructure their operations and increase lending in the economy. The scheme is available for a fee on eligible assets of select participating institutions. Agreement signed with Lloyds Banking Group and Royal Bank of Scotland. **Other Measures** • The Banking Act 2009, which strengthens the UK's statutory framework for financial stability and depositor protection, was enacted.
Other Countries	**Monetary Policy Easing** • ECB cut its interest rates on the main refinancing operations by 50 bps each in January and March 2009 and by 25 bps in April 2009 to 1.25 per cent, on the marginal lending facility by 50 bps in March 2009 and by 25 bps in April 2009 to 2.25 per cent and on deposit facility by 100 bps in January, 50 bps in March 2009 and 25 bps in April 2009 to 0.25 per cent. • Central Bank of the Republic of Turkey cut its overnight borrowing rate by 450 bps during January-March 2009. • South Korea reduced its monetary policy base rate by 50 bps each in January and February 2009 to 2.0 per cent as on February 12, 2009. **Liquidity Provision** • Japan issued fresh guidelines on eligible collateral for credit extended by banks. • Bank of Japan announced terms and conditions for the outright purchase of corporate financing instruments such as CP and corporate bonds. • The frequency and duration of special funds supplying operations were increased. Most other provisions taken for achieving financial stability, that were set to expire in April 2009, were extended up to at least September 2009. **Recapitalisation of the Financial System** • Germany extended a bailout package to Commerzbank to backstop losses at newly acquired Dresdner Bank and took a 25 per cent holding in the combined entity. • Ireland took control of the Anglo Irish Bank. • The Dutch authorities granted ING Group a backup facility guaranteeing part of the bank's securitised mortgage portfolio worth US$ 35 billion. **Other Measures** • To address continued pressures in global US dollar funding markets, the temporary reciprocal currency arrangements (swap lines) between the Federal Reserve and other central banks were extended till October 30, 2009.

Source : Websites of respective central banks, finance ministries.

Domestic Financial Markets

V.24 Beginning mid-September 2008, the Indian financial markets came under pressure owing to the knock-on effects of the global crisis through the monetary, financial, real and confidence channels. The contagion was initially felt in the equity markets due to the reversal of foreign institutional portfolio flows. With sharp tightening of global liquidity, Indian banks and corporates saw their overseas financing drying up. As a means of substitute financing, corporates withdrew their investments from domestic money market mutual funds, thereby putting redemption pressure on them and on NBFCs where the mutual funds had invested a significant portion of their funds. This substitution of overseas financing by domestic financing brought both money market and credit market under pressure. Moreover, the foreign exchange market was impacted by the reversal of capital flows as part of the global deleveraging process. Simultaneously, corporates were converting the funds raised locally into foreign currency to meet their external obligations. Both these factors put downward pressure on the rupee. Furthermore, the Reserve Bank's intervention in the foreign exchange market to manage the volatility in the rupee temporarily tightened the money market.

V.25 In response, the Reserve Bank initiated several measures since September 16, 2008 to augment domestic and foreign exchange liquidity for proper functioning of the domestic markets and maintaining financial stability (Annex 2). Reflecting the impact of the measures, call rates in the money market have settled back into the informal LAF corridor since November 2008, having breached the upper bound in the preceding two months (Table 45). In the foreign exchange market, the Indian rupee generally depreciated against major currencies. In the credit market, the lending rates of scheduled commercial banks (SCBs) have begun to exhibit some moderation since November 2008. The government securities market was bearish for most of the fourth quarter of 2008-09 and yields hardened. Indian equity markets, picking up global cues, staged some recovery in March 2009.

Liquidity Conditions

V.26 The Reserve Bank's monetary policy response to the global crisis impinging on India was to keep the domestic money and credit markets functioning normally and ensure that the liquidity stress did not trigger solvency issues. The need to maintain a comfortable rupee liquidity position, to augment foreign exchange liquidity and to ensure credit delivery to all productive sectors of the economy marked a reversal of Reserve Bank's policy stance from monetary tightening in the first half of 2008-09 to monetary easing in the second half. The measures to meet the above objectives came in several policy packages starting mid-September 2008.

Table 45: 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 MSS Out-standing# (Rs. crore)	Average Daily Reverse Repo (LAF) Out-standing (Rs. crore)	Average Daily BSE Turnover (Rs. crore)	Average Daily NSE Turnover (Rs. crore)	Average BSE Sensex**	Average S&P CNX Nifty**
1	2	3	4	5	6	7	8	9	10	11	12	13	14
2006-07	**21,725**	**7.22**	**4,863**	**7.78**	**18,540**	**45.28**	**26,824 ##**	**37,698**	**21,973**	**3,866**	**7,812**	**12,277**	**3,572**
2007-08	**21,393**	**6.07**	**8,104**	**7.91**	**34,044**	**40.24**	**78,203 ##**	**1,28,684**	**4,677**	**6,275**	**14,148**	**16,569**	**4,897**
2008-09 P	**22,436**	**7.06**	**7,175**	**7.56**	**–**	**45.92**	**–**	**1,48,889**	**2,885**	**4,498**	**11,212**	**12,366**	**3,731**
Apr 2008	19,516	6.11	6,657	8.10	37,580	40.02	4,325	1,70,726	26,359	5,773	13,561	16,291	4,902
May 2008	19,481	6.62	6,780	8.04	32,287	42.13	148	1,75,565	11,841	6,084	13,896	16,946	5,029
Jun 2008	21,707	7.75	6,835	8.43	38,330	42.82	-5,229	1,74,433	-8,622	5,410	12,592	14,997	4,464
Jul 2008	24,736	8.76	5,474	9.18	37,173	42.84	-6,320	1,72,169	-27,961	5,388	12,862	13,716	4,125
Aug 2008	23,408	9.1	7,498	9.06	38,388	42.94	1,210	1,71,944	-22,560	4,996	11,713	14,722	4,417
Sep 2008	23,379	10.52	10,418	8.45	44,700	45.56	-3,784	1,75,666	-42,591	5,147	12,489	13,943	4,207
Oct 2008	28,995	9.9	4,321	7.85	36,999	48.66	-18,666	1,69,123	-45,612	3,911	10,810	10,550	3,210
Nov 2008	21,812	7.57	5,866	7.41	31,322	49.00	-3,101	1,47,648	-8,017	3,539	9,618	9,454	2,835
Dec.2008	21,641	5.92	11,451	5.88	34,874	48.63	-318	1,24,848	22,294	3,851	95,928	9,514	2,896
Jan 2009	18,496	4.18	9,568	5.84	27,171P	48.83	-29	1,13,535	45,474	3,526	9,559	9,350	2,854
Feb 2009	22,241	4.16	5,916	5.98	24,840P	49.26	230	1,02,934	50,649	2,856	7,887	9,188	2,819
March 2009P	23,818	4.17	5,322	6.56	–	51.23	–	88,077	33,360	3,488	10,140	8,995	2,802

* : Average of daily weighted call money borrowing rates.
@ : Average of daily closing rates.
** : Average of daily closing indices.
LAF : Liquidity Adjustment Facility.
MSS : Market Stabilisation Scheme.
P : Provisional
+ : Average of daily outright turnover in Central Government dated securities.
# : Average of weekly outstanding MSS.
: Cumulative for the financial year.
BSE : Bombay Stock Exchange Limited
NSE : National Stock Exchange of India Limited .
– : Not available.
Note : In column 10, (-) indicates injection of liquidity, while (+) indicates absorption of liquidity.

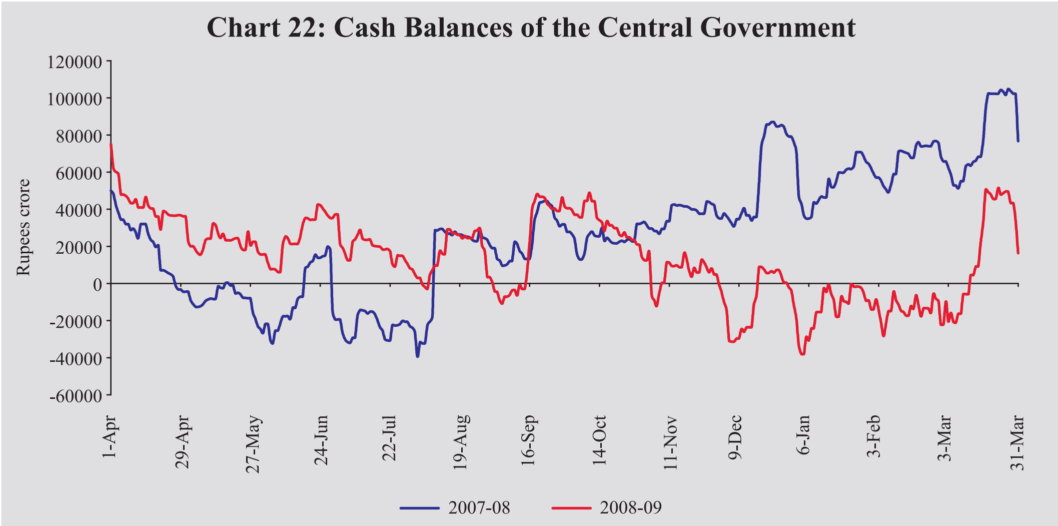
Cash Management of the Central Government

V.27 The surplus cash balance of Rs.76,686 crore as at end-March 2008 was used up by the Central Government to meet its expenditure needs and it resorted to ways and means advances (WMA) during August 4-6, 2008 and again during September 2-14, 2008. During the third quarter of 2008-09, the Government announced fiscal stimulus packages even as revenue receipts decelerated. The Central Government was in WMA for 23 days and resorted to overdraft (OD) for 10 days during the third quarter. The Central Government was in WMA for 70 days and in OD for 55 days during the fourth quarter of 2008-09 (Table 46 and Chart 22).

Table 46: Cash Management of the Central Government

	2007-08	2008-09
1	2	3
Total Number of Days		
WMA	91	109
OD	37	65
Cash Deficit	91	109
Average Daily Utilisation*		
WMA	3,615	2,077
OD	647	1,823

* : in Rupees crore.



Liquidity Management

V.28 During the financial year 2008-09, liquidity management operations had to change course beginning mid-September 2008 as the knock-on effects of the severe disruptions in international financial markets began to be felt in the domestic financial markets. The use of liquidity management tools such as the cash reserve ratio (CRR) and the Open Market Operation (OMO), including the Market Stabilisation Scheme (MSS) and the Liquidity Adjustment Facility (LAF), was thus modulated in accordance with the evolving conditions in financial markets. Variations in the cash balances of the Central Government and the capital flows and the concomitant foreign exchange operations of the Reserve Bank continued to be the key drivers of liquidity conditions during the year (Table 47).

V.29 There was a reduction in the generation of domestic liquidity during the period from April to mid-September 2008, as the drying up of capital inflows had brought a turnaround in the foreign exchange operations of the Reserve Bank from net spot purchases up to May 2008 to net spot sales thereafter, barring August 2008 (refer Table 47). Consequently, the MSS auctions of dated securities were kept in abeyance after end-April 2008 and MSS issuances, even through Treasury Bills, were stopped after September 2, 2008 (Chart 23). Reflecting the impact of these developments, the LAF turned from absorption mode to injection mode after the first week of June 2008.

V.30 Beginning mid-September 2008, the severe disruptions in international financial markets brought pressures on the domestic money and foreign exchange markets in conjunction with transient local factors such as advance tax payments. In order to alleviate these stresses and with the abatement of inflationary pressures, the Reserve Bank augmented rupee liquidity through a series of measures

Table 47: Reserve Bank's Liquidity Management Operations

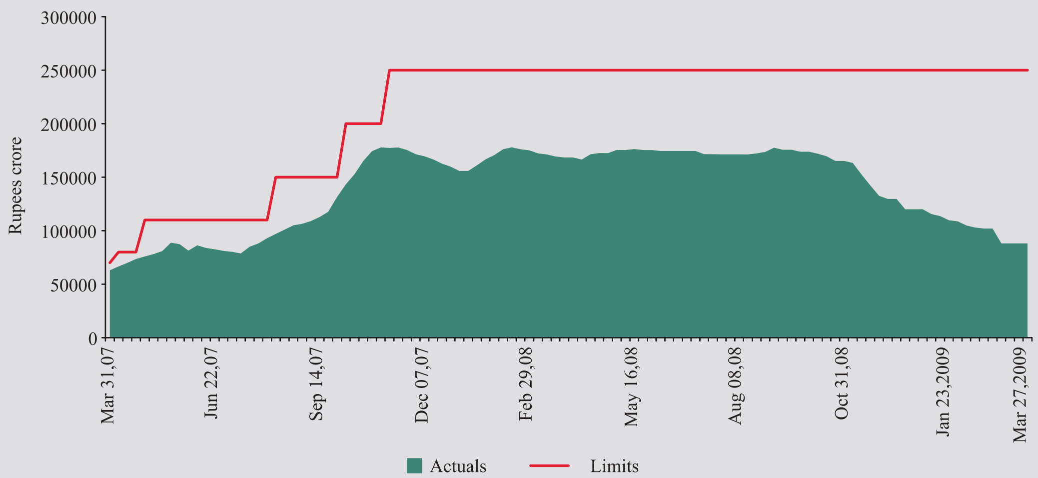
(Rupees crore)

Item	2007-08 (April-March	2008-09 (April-February)	2008-09 Q1	Q2	Q3	Jan	Feb
1	2	3	4	5	6	7	8
A. Drivers of Liquidity (1+2+3+4+5)	**2,03,121**	**-1,24,579**	**6,061**	**-18,917**	**-1,01,304**	**-12**	**-10,408**
1. RBI's net purchases from Authorised Dealers	3,12,054	-1,60,765	-8,555	-40,249	-1,12,168	-129	336
2. Currency with the Public	-85,475	-82,369	-30,071	12,294	-40,096	-7,724	-16,771
3. Surplus cash balances of the Centre with the Reserve Bank	-26,594	76,586	40,073	-3,845	36,554	3,804	0
4. WMA and OD	0	9,603	0	0	0	9,166	437
5. Others (residual)	3,136	32,366	4,615	12,884	14,406	-5,129	5,590
B. Management of Liquidity (6+7+8+9)	**-1,17,743**	**1,06,952**	**-37,659**	**7,217**	**1,33,325**	**-3,516**	**7,586**
6. Liquidity impact of LAF Repos	21,165	-1,10,170	-18,260	24,390	-71,110	-39,975	-5,215
7. Liquidity impact of OMO (Net) *	13,510	48,472	14,642	11,949	10,681	5,173	6,028
8. Liquidity impact of MSS	-1,05,418	66,400	-6,041	628	53,754	11,286	6,773
9. First round liquidity impact due to CRR change	-47,000	1,02,250	-28,000	-29,750	1,40,000	20,000	0
C. Bank Reserves (A+B) #	**85,378**	**-17,627**	**-31,598**	**-11,700**	**32,021**	**-3,528**	**-2,822**

(+) : 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.
* : Includes oil bonds but excludes purchases of Government securities on behalf of State Governments.
Note : Data pertain to March 31 and last Friday for all other months.

including reduction in CRR by a cumulative 400 basis points to 5.0 per cent and a slew of special facilities (refer Annex 2). Furthermore, the repo rate and the reverse repo rate under LAF were progressively reduced from 9.0 per cent

Chart 23: Market Stabilisation Scheme



to 5.0 per cent and 6.0 per cent to 3.5 per cent, respectively. These apart, MSS buyback auctions were started from November 6, 2008, largely dovetailed with the Government's normal market borrowing programme to provide another avenue for injecting liquidity (Table 48 and Chart 24). Reflecting the impact of these measures, the average daily net outstanding liquidity injection under LAF, which had increased to around Rs.43,000-46,000 crore during September and October 2008, declined sharply thereafter and turned into net absorption from early December 2008.

Table 48: 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
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	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	-43,260	1,71,327	15,043	1,43,110
August	-7,600	1,73,658	17,393	1,83,451
September	-56,480	1,73,804	40,358	1,57,682
October	-73,590	1,65,187	14,383	1,05,980
November	-9,880	1,32,531	7,981	1,30,632
December	14,630	1,20,050	3,804	1,38,484
2009				
January	54,605	1,08,764	-9,166	1,54,203
February	59,820	1,01,991	-9,603	1,52,208
March*	1,485	88,077	16,219	1,05,781
April 10	1,29,810	71,145	-13,779	1,87,176

@ : 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.

2. The Second LAF that was discontinued from August 6, 2007 was re-introduced from August 1, 2008 on reporting Fridays and from September 17, 2008 on a daily basis.

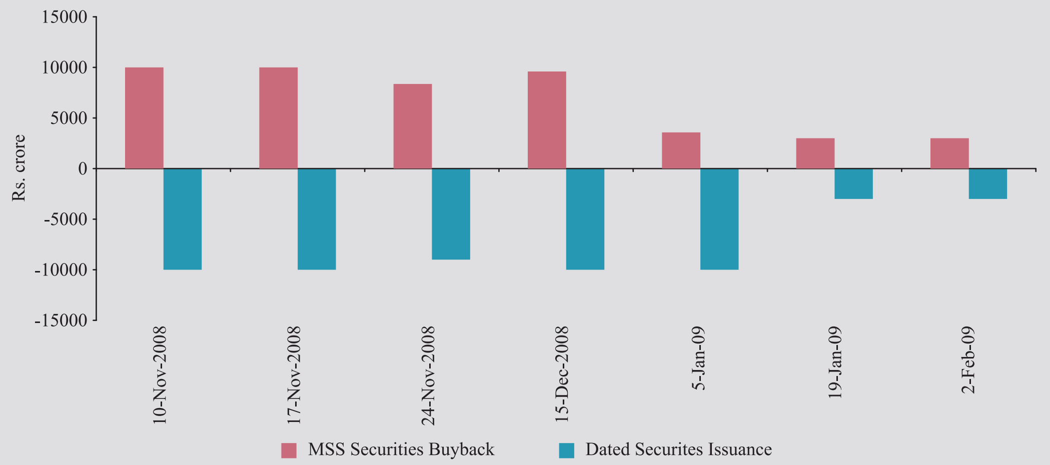
3. Negative sign in column 4 indicates injection of liquidity through WMA/OD.

V.31 For more effective liquidity management and to ensure that the market borrowing programme of the Government was conducted in a non-disruptive manner, the scope of the OMO was widened with effect from February 19, 2009 by including purchases of government securities through an auction-based mechanism in addition to purchases through the Negotiated Dealing System – Order Matching (NDS-OM) segment. The cut-off yields in the OMO purchase auctions were based on the attractiveness of offers for securities relative to their secondary market yields. Auction-based purchases aggregated Rs.5,000 crore whereas purchases through NDS-OM aggregated Rs.800 crore during February 2009.

V.32 With the change in the external accounts in the recent period resulting in attendant draining of primary liquidity reflecting the impact of the Reserve Bank's operations in the foreign exchange market, the Memorandum of Understanding (MoU) on the MSS was amended on February 26, 2009 to permit the transfer of the sterilised liquidity from the MSS cash account to the normal cash account of the Government (details covered in the Central Government securities section later in the Chapter).

V.33 In March 2009, the OMO

Chart 24: MSS Buyback and Issuance of Central Government Securities



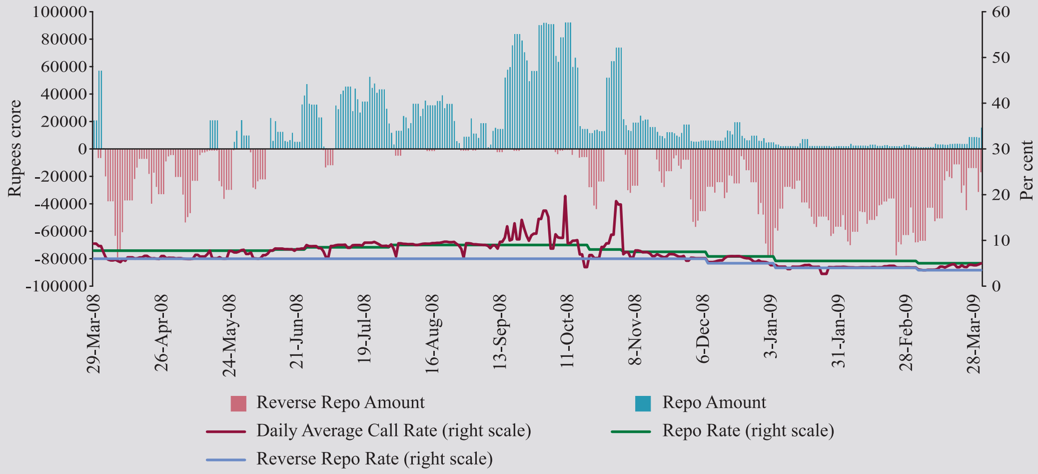
purchases through auctions and NDS-OM were placed at Rs.41,640 crore and Rs.4,475 crore, respectively, whereas MSS redemptions amounted to Rs.2,000 crore (over and above the de-sequestering of Rs.12,000 crore of MSS balances); these helped to further ease liquidity conditions. The average daily net outstanding liquidity absorption through LAF, however, declined to around Rs.33,000 crore in March 2009 from over Rs.50,000 crore in the previous month, reflecting, *inter-alia*, advance tax outflows. It is, however, noteworthy that the net injection of liquidity through LAF did not occur even on a single day of March 2009, including the last day of the month, in sharp contrast to the experience in the previous few years.

Money Market

V.34 During the first half of 2008-09 (up to mid-September 2008), reflecting the orderly conditions in the money market, the call rates remained largely within the informal corridor of the reverse repo and repo rates. The failure of Lehman Brothers and a few other global financial institutions in September 2008 saw the abrupt freezing of money market activities in the major financial centres. In order to contain the excess volatility in the foreign exchange market, the Reserve Bank made available substantial dollar liquidity. This had a tightening impact on rupee liquidity. The impact was magnified on account of domestic factors such as advance tax outflows from the banking system. The call rate moved above the repo rate in mid-September 2008 (Chart 25). As the series of measures initiated by the Reserve Bank to augment liquidity began to take effect, the weighted average call money rate declined and mostly remained within the LAF corridor from November 3, 2008 onwards.

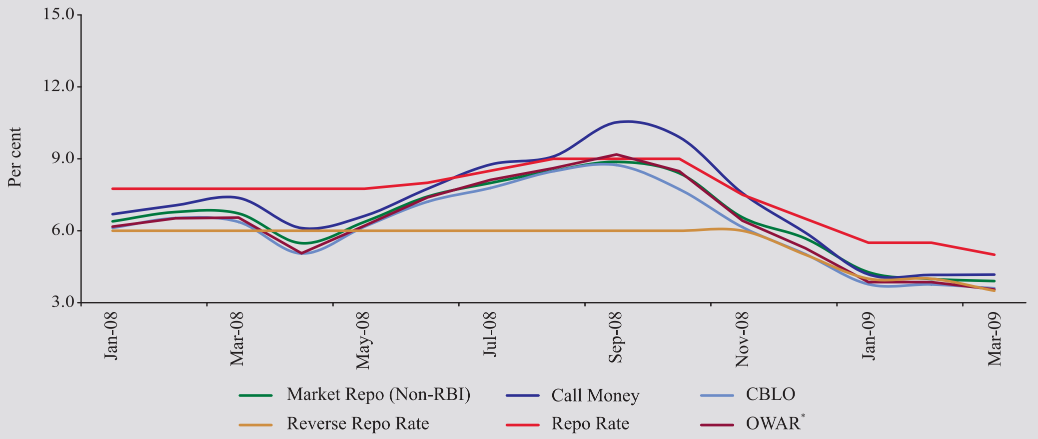
V.35 Interest rates in the collateralised segments of the money market – the market repo (outside the LAF) and the Collateralised Borrowing and Lending

Chart 25: Liquidity Adjustment Facility and the Call Rate



Obligation (CBLO) – moved in tandem with, but remained below, the call rate during 2008-09 in general, including in the last quarter of the year (Chart 26). Average daily volumes in the CBLO and market repo segments, declined sharply during April-October 2008, mainly on account of tightening of liquidity conditions and increasing recourse to LAF repos. The CBLO and market repo volumes picked up substantially in the last quarter of 2008-09, largely reflecting the easing of liquidity conditions and the enhanced lending capacity of mutual funds. The total average daily volume of the three segments of the money market was placed at Rs.82,000 crore in March 2009 as compared with Rs.41,000 crore in October 2008 and Rs.64,000 crore in April 2008. The shares of the CBLO, market repo and call

Chart 26: Money Market Interest Rates



* Overnight Weighted Average Rate (OWAR) is the daily volume-weighted interest rate of the overnight segments of call, CBLO and market repo.

segments in total money market were placed at 59 per cent, 26 per cent and 15 per cent in March 2009, nearly the same as in April 2008.

Certificates of Deposit

V.36 The outstanding amount of certificates of deposit (CDs) issued by SCBs increased from end-March 2008 up to September 2008. This was followed by a decline up to December 2008, reflecting the indirect impact of the global financial turmoil. Subsequently, with the easing of liquidity conditions, the outstanding amount of CDs rose from January 2009. The outstanding amount constituted 5.23 per cent of aggregate deposits of CD-issuing banks with significant inter-bank variation as on March 13, 2009. The weighted average discount rate (WADR) of CDs generally increased up to November 2008 but declined thereafter in consonance with the movements in other money market rates (Table 49).

Commercial Paper

V.37 The outstanding amount of commercial paper (CP) issued by

Table 49: 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)	Money Market Rate* (Per cent)	Term Money Market	Outstanding	WADR (Per cent)	Outstanding	WADR (Per cent)
1	2	3	4	5	6	7	8	9	10	11
2006-07	**10,863**	**8,419**	**16,195**	**35,477**	**6.57**	**506**	**21,329** +	**8.08** +	**64,821** +	**8.24** +
2007-08	**10,697**	**13,684**	**27,813**	**52,194**	**5.48**	**352**	**33,813** +	**9.20** +	**1,17,186** +	**8.94** +
2008-09 P	**11,218**	**14,330**	**30,776**	**56,323**	**6.43**	**397**	**47,312** +	**10.57** +	**1,61,257** +	**9.39** +
Apr 2008	9,758	14,966	38,828	63,552	5.31	374	37,584	8.85	1,50,865	8.49
May 2008	9,740	14,729	36,326	60,795	6.29	420	42,032	9.02	1,56,780	8.95
Jun 2008	10,854	11,262	35,774	57,890	7.35	253	46,847	10.03	1,63,143	9.16
Jul 2008	12,368	8,591	23,669	44,628	8.09	226	51,569	10.95	1,64,892	10.23
Aug 2008	11,704	10,454	22,110	44,268	8.65	501	55,036	11.48	1,71,966	10.98
Sep 2008	11,690	10,654	20,547	42,891	9.26	335	52,038	12.28	1,75,522	11.56
Oct 2008	14,497	9,591	16,818	40,906	8.66	345	48,442	14.17	1,58,562	10.00
Nov 2008	10,906	15,191	24,379	50,476	6.58	319	44,487	12.42	1,51,493	10.36
Dec 2008	10,820	16,943	32,261	60,024	5.37	415	40,391	10.70	1,51,214	8.85
Jan 2009	9,248	18,053	31,794	59,095	3.99	454	51,668	9.48	1,64,979	7.33
Feb 2009	11,121	19,929	38,484	69,534	3.89	669	52,560	8.93	1,75,057	6.73
March 2009 P	11,909	21,593	48,319	81,821	3.76	451	49,953	9.78 #	1,67,320	6.73 #

– : Not available. * : Weighted average rate of the call, CBLO and market repo segments.
+ : Fortnightly average for the year. Data for 2008-09 are up to mid-March 2009.
# : Provisional data as on mid-March 2009. P : Provisional.
WADR : Weighted Average Discount Rate.

corporates, which had increased gradually during April-August 2008-09, declined thereafter till December 2008, mainly reflecting tight liquidity conditions and general risk-aversion. Subsequently, the outstanding amount of CPs picked up, as liquidity conditions eased. Leasing and finance companies continued to be the major issuers of CPs, accounting for 63.1 per cent of total outstanding as of March 15, 2009 (Table 50). The WADR of CPs increased steadily up to October 2008, and generally declined subsequently up to mid-March 2009, with the easing of liquidity conditions (refer Table 49). The differential in the WADR of CP *vis-a-vis* CD, however, continues to remain elevated since October 2008.

Treasury Bills

V.38 The notified amounts for 91-day, 182-day and 364-day Treasury Bills (excluding MSS) were raised during the course of the year to finance the temporary cash mismatch, *inter alia*, arising from the expenditure on the Agricultural Debt Waiver Scheme. Thus, an additional amount of Rs.1,87,500 crore (Rs.97,000 crore, net) was raised over and above the notified amount during the year. During 2008-09, primary market yields on 91-day Treasury Bills increased steadily from 6.94 per cent on April 2, 2008 (first auction of the year 2008-09) and peaked at 9.36 per cent on July 30, 2008, reflecting tight liquidity conditions in response to measures taken to combat inflation such as hike in CRR and repo rate. It started declining thereafter, responding to various measures taken to ease liquidity and stimulate the economy amidst global recessionary trends. Yields on 91-day Treasury Bills declined sharply in December 2008 and were lowest at 4.58 per cent on January 14, 2009 and March 12, 2009 (Table 51 and Chart 27). Similar trend was observed in yields on 182-day

Table 50: Commercial Paper - Major Issuers

(Rupees crore)

Category of Issuer	End of					
	March 2007	March 2008	June 2008	September 2008	December 2008	March 15, 2009
1	2	3	4	5	6	
Leasing and Finance	12,594 (70.5)	24,925 (76.5)	34,957 (76.6)	39,053 (75.0)	27,965 (73.5)	31,528 (63.1)
Manufacturing	2,754 (15.4)	5,687 (17.4)	8,150 (17.4)	9,925 (19.1)	6,833 (18.0)	13,925 (27.9)
Financial Institutions	2,515 (14.1)	1,980 (6.1)	3,740 (8.0)	3,060 (5.9)	3,257 (8.5)	4,500 (9.0)
Total	**17,863 (100.0)**	**32,592 (100.0)**	**46,847 (100.0)**	**52,038 (100)**	**38,055 (100)**	**49,953 (100)**

Note : Figures in parentheses are percentage shares in the total outstanding.

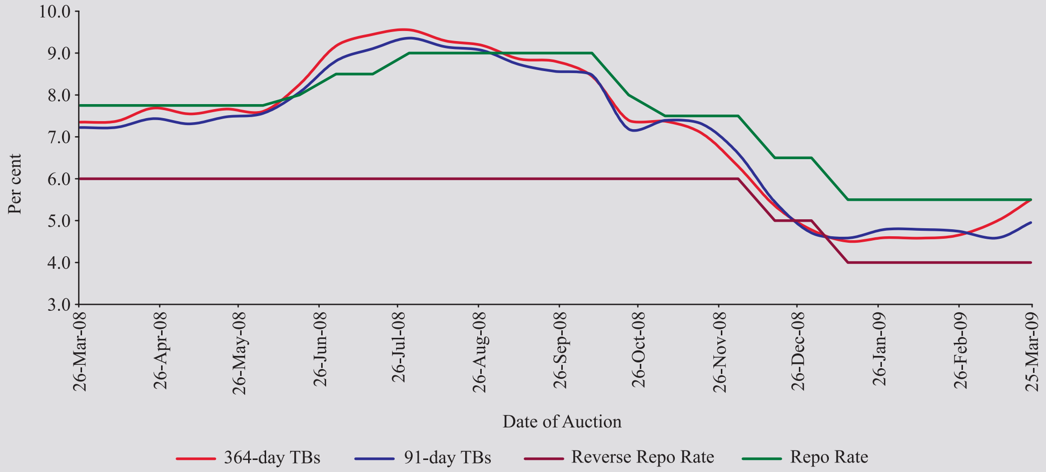
Table 51: Treasury Bills in the Primary Market

Year/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
2007-08	**2,24,500@**	**7.10**	**7.40**	**7.42**	**2.84**	**2.79**	**3.21**
2008-09	**2,99,000@**	**7.10**	**7.22**	**7.15**	**3.43**	**2.91**	**3.47**
Apr 2008	22,000	7.28	7.41	7.53	1.70	1.36	2.36
May 2008	21,000	7.41	7.55	7.61	2.65	2.78	3.05
Jun 2008	11,500	8.01	8.42	7.93	2.00	2.76	2.80
Jul 2008	16,000	9.07	9.33	9.39	2.35	2.72	2.70
Aug 2008	23,500	9.15	9.31	9.24	2.99	2.86	4.35
Sept 2008	25,000	8.69	8.92	8.83	3.06	3.04	3.57
Oct 2008	35,000	8.13	8.36	7.92	1.95	2.42	4.00
Nov 2008	28,000	7.30	7.13	7.23	7.95	2.97	4.33
Dec 2008	16,500	5.69	5.35	5.07	5.36	4.67	5.14
Jan 2009	38,500	4.69	4.60	4.64	4.56	3.22	4.80
Feb 2009	32,000	4.78	4.71	4.62	2.81	1.86	2.62
March 2009	25,000	4.77	4.86	5.25	2.10	2.67	1.44

@ : Total for the financial year.
Note : Notified amounts are inclusive of issuances under the MSS.

and 364-day Treasury Bills. The yield spread between 364-day and 91-day Treasury Bills was 48 basis points during March 2009 (8.9 basis points in March 2008).

Chart 27 : Yields on Treasury Bills



Foreign Exchange Market

V.39 During 2008-09, the rupee depreciated on account of widened trade deficit, capital outflows and strengthening of the US dollar *vis-à-vis* other major currencies. The rupee/US dollar exchange rate was Rs. 39.99 per dollar at end-March 2008. It fell to Rs. 52.09 per dollar on March 5, 2009, before recovering to Rs. 50.95 per dollar at end-March 2009. As on March 31, 2009, the Indian rupee had depreciated by 21.5 per cent against the US dollar over its level on March 31, 2008. Over the same period, the rupee experienced a depreciation of 6.5 per cent against the euro, 22.8 per cent against the Japanese yen and 23.6 per cent against the Chinese yuan. However, the rupee showed an appreciation of 9.1 per cent against the pound sterling. The rupee/US dollar exchange rate was 49.90 on April 15, 2009. As on April 15, 2009, the rupee had generally appreciated against the US dollar, the euro and the Japanese yen but depreciated against the pound sterling over the end-March 2009 level (Chart 28).

V.40 It is also useful to look at the indices of NEER and REER, which are often used as indicators of external competitiveness over a period of time. REER captures movements in cross-currency exchange rates as well as inflation differential between India and its major trading partners over time. The average 6-currency trade-based REER (base: 1993-94=100) was 114.09 in 2007-08, indicating an overvaluation of 14.1 per cent in real terms. There was a reduction in the extent of overvaluation during the first half of 2008-09 and the REER has moved closer to its base level (1993-94=100), especially since December 2008 (Chart 29). The 6-currency trade-based REER which stood at 112.16 in April 2008, indicating an overvaluation of 12.2 per cent, gradually declined to 100.07 in February 2009 mainly on account of significant depreciation of the rupee against the US dollar and against other major currencies like the euro, the Japanese yen and the Chinese yuan during 2008-09. The sharp decline in inflation rate in India

Chart 28: Movement of Rupee *vis-à-vis* Major Currencies

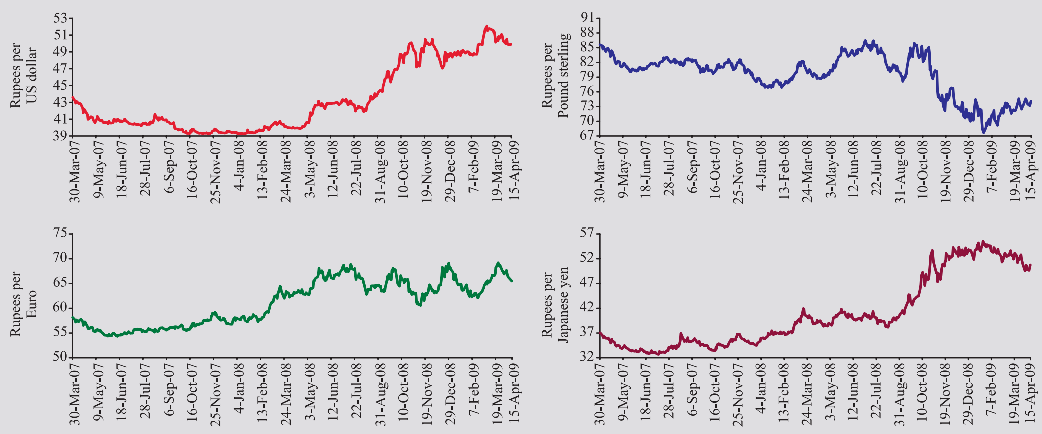
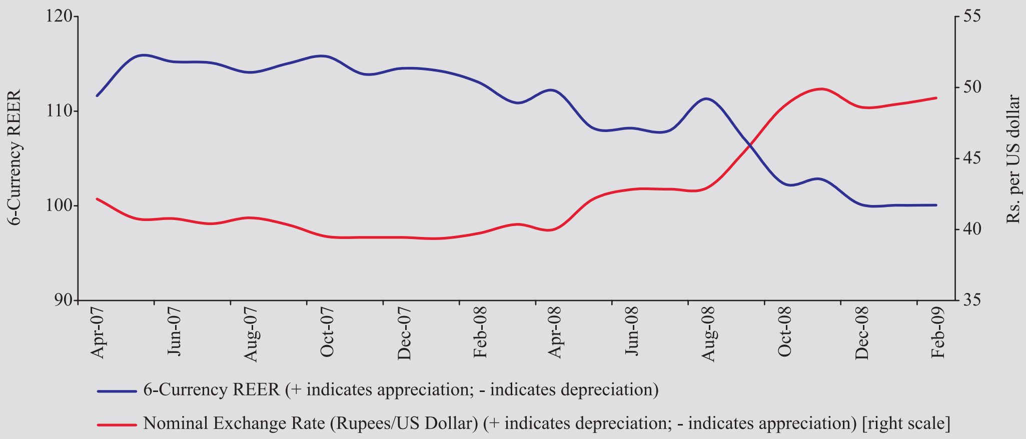


Chart 29: Nominal Exchange Rate (Rs./US Dollar) and 6-Currency REER



in the recent months has also contributed towards the correction in the extent of the overvaluation of the rupee. Over the same period, the 6-currency NEER declined gradually from 70.63 in April 2008 to 62.75 in February 2009 (Table 52).

V.41 The 36-currency trade-weighted NEER and REER depreciated by 5.3 per cent and 10.7 per cent, respectively, between March 2008 and February 2009 (as against an appreciation of 6.9 per cent and 3.0 per cent, respectively, during the

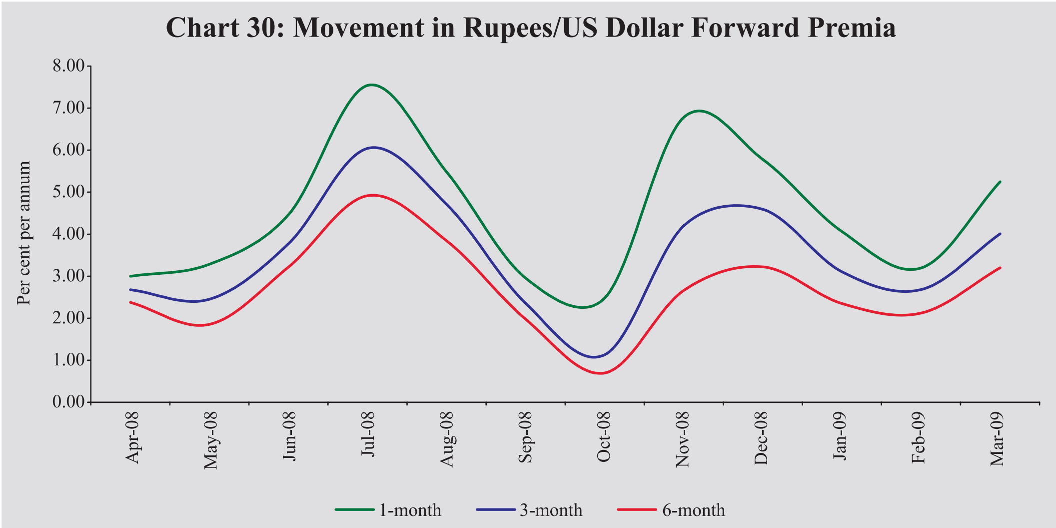
Table 52: Nominal and Real Effective Exchange Rate of the Indian Rupee (Trade-based Weights)

Year/Month	Base : 1993-94 (April-March) = 100				Year/Month	Base : 1993-94 (April-March) = 100			
	6-Currency Weights		36-Currency Weights			6-Currency Weights		36-Currency Weights	
	NEER	REER	NEER	REER		NEER	REER	NEER	REER
1	2	3	4	5	1	2	3	4	5
2007-08 (P)	**74.17**	**114.09**	**93.91**	**104.81**	Sep. 2008(P)	64.37	106.96	85.42	95.97
Apr 2008 (P)	70.63	112.16	93.26	101.86	Oct 2008(P)	62.08	102.36	83.23	92.29
May 2008 (P)	67.48	108.23	89.04	97.72	Nov 2008(P)	63.06	102.80	84.69	92.54
Jun 2008 (P)	66.38	108.20	87.65	97.76	Dec 2008(P)	62.12	100.18	83.91	90.40
July 2008(P)	65.83	107.94	87.04	97.40	Jan 2009(P)	62.28	100.06	83.63	90.01
Aug 2008(P)	67.22	111.30	88.60	99.65	Feb 2009(P)	62.75	100.07	85.20	91.07

Movement of Average Exchange Rate – Per cent change

	2007-08	2007-08 (April-Feb)	2008-09 (April-Feb)
36-currency trade-based REER	6.4	6.9	-9.4
36-currency trade-based NEER	9.3	9.9	-8.2
6-Currency trade-based REER	8.1	8.5	-7.8
6-Currency trade-based NEER	6.7	7.3	-12.9
Memo:			
Rupees/ US dollar Exchange Rate	12.5		-12.4*

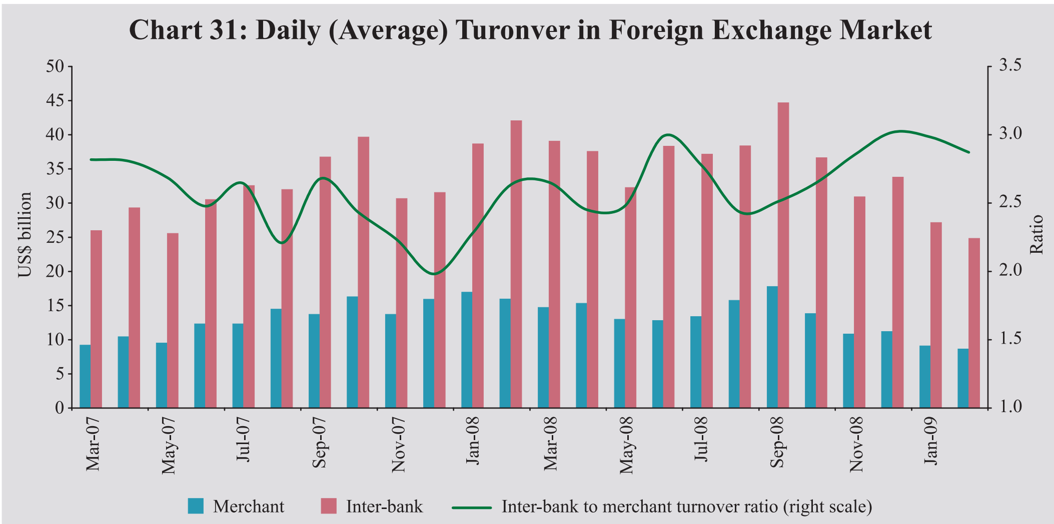
NEER : Nominal Effective Exchange Rate. REER : Real Effective Exchange Rate. P : Provisional.
* : Average for April-March.
Note : Rise in indices indicates appreciation of the rupee and *vice versa*.



corresponding period of the previous year).

V.42 During 2008-09, forward premia showed significant variation reflecting the underlying supply and demand conditions. As on March 31, 2009, the one month, three month and six month premia were at 4.71 per cent, 3.34 per cent and 2.78 per cent, respectively. As on April 9, 2009, the one month, three month and six month premia were 3.85 per cent, 3.29 per cent and 2.76 per cent, respectively (Chart 30).

V.43 The daily average turnover in the foreign exchange market was lower at US$ 47.8 billion during April-February 2008-09 as compared with US$ 47.4 billion during the corresponding period of the previous year. The ratio of inter-bank to merchant turnover increased to 2.7 from 2.4 during this period (Chart 31).



Credit Market

V.44 Bank deposit and lending rates, which had firmed up during 2008-09 up to October 2008, started easing from November 2008, reflecting measures taken by the Reserve Bank. Interest rates offered by public sector banks (PSBs) on deposits of maturity of one year to three years were in the range of 8.00-9.25 per cent in March 2009 as compared with the range of 8.50-10.75 per cent in December 2008, while those on deposits of maturity of over three years were in the range of 7.50-9.00 per cent as compared with the range of 8.50-9.75 per cent during the same period (Table 53). Similarly, the range of interest rates offered by private sector

Table 53: Deposit and Lending Rates

(Per cent)

Item	March 2007	March 2008	September 2008	December 2008	March 2009
1	2	3	4	5	6
1. Domestic Deposit Rate					
Public Sector Banks					
Up to 1 year	2.75-8.75	2.75-8.50	2.75-10.25	2.75-10.25	2.75-8.25
More than 1 year and up to 3 years	7.25-9.50	8.25-9.25	8.75-10.25	8.50-10.75	8.00-9.25
More than 3 years	7.50-9.50	8.00-9.00	8.50-9.75	8.50-9.75	7.50-9.00
Private Sector Banks					
Up to 1 year	3.00-9.00	2.50-9.25	3.00-9.75	3.00-10.00	3.00-8.75
More than 1 year and up to 3 years	6.75-9.75	7.25-9.25	8.30-10.50	9.00-11.00	7.50-10.25
More than 3 years	7.75-9.60	7.25-9.75	8.25-10.25	8.50-11.00	7.50-9.75
Foreign Banks					
Up to 1 year	3.00-9.50	2.25-9.25	3.50-9.75	3.50-9.75	2.50-8.50
More than 1 year and up to 3 years	3.50-9.50	3.50-9.75	3.50-10.50	3.50-11.25	2.50-9.50
More than 3 years	4.05-9.50	3.60-9.50	3.60-11.00	3.60.11.00	2.50-10.00
2. Benchmark Prime Lending Rate					
Public Sector Banks	12.25-12.75	12.25-13.50	13.75-14.75	12.50-14.00	11.50-14.00
Private Sector Banks	12.00-16.50	13.00-16.50	13.75-17.75	13.00-17.25	12.75-16.75
Foreign Banks	10.00-15.50	10.00-15.50	10.00-16.00	10.00-17.00	10.00-17.00
3. Actual Lending Rate*					
Public Sector Banks	4.00-17.00	4.00-17.75	6.00-18.75	5.25-18.00	–
Private Sector Banks	3.15-25.50	4.00-24.00	5.06-23.00	5.06-30.00	–
Foreign Banks	5.00-26.50	5.00-28.00	5.00-25.50	5.00-26.00	–
4. Weighted Average Lending Rate**					
Public Sector Banks	11.81	12.15 #	–	–	–
Private Sector Banks	11.91	12.67 #	–	–	–
Foreign Banks	13.03	12.94 #	–	–	–

– : Not available. # : Provisional.

* : 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.

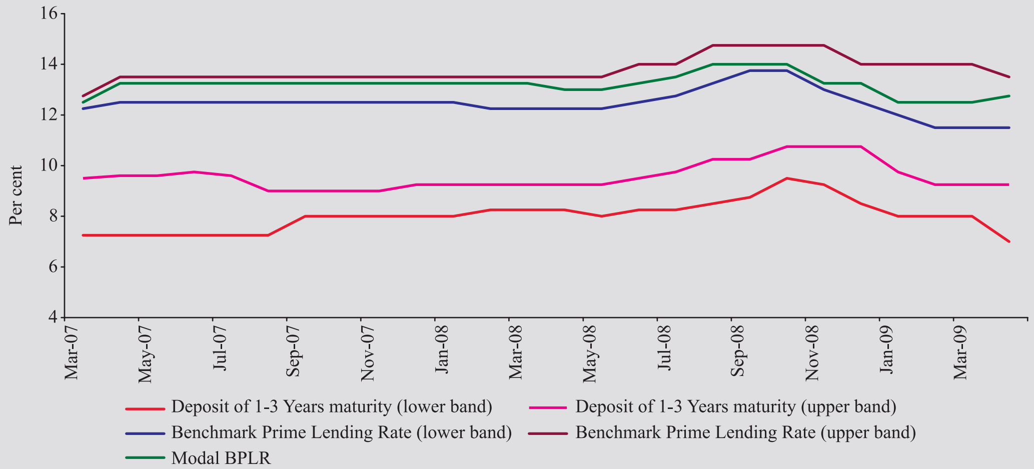
** : Data based on the accounts with credit limit of over Rs.2 lakh and is exclusive of inland and foreign bills purchased and discounted. Oustanding amounts are used as weights for calculating average lending rates.

banks and foreign banks on deposits of varying maturity declined in March 2009 as compared with the range in December 2008. Notably, the administered interest rates on most small savings instruments have remained unchanged since March 2003.

V.45 The benchmark prime lending rates (BPLRs) of PSBs and private sector banks declined from the range of 12.50-14.00 per cent and 13.00-17.25, respectively, in December 2008 to the range of 11.50-14.00 per cent and 12.75-16.75 per cent, respectively, in March 2009 (Chart 32). The range of BPLRs of foreign banks remained unchanged at 10.00-17.00 per cent during the same period. The weighted average BPLR of PSBs and private sector banks decreased from 14.00 per cent and 16.48 per cent, respectively, in October 2008 to 12.48 per cent and 16.03 per cent, respectively, in March 2009. The weighted average BPLR of foreign banks decreased marginally from 15.32 to15.07 per cent during the same period.

V.46 The share of sub-BPLR lending (excluding export credit and small loans) for PSBs decreased to 68.0 per cent in December 2008 from 70.6 per cent in March 2008. The sub-BPLR lending of private sector banks, at 87.9 per cent, decreased from the March 2008 level of 88.7 per cent. The sub-BPLR lending of foreign banks, however, declined significantly from the high of 77.6 per cent in March 2008 to 61.3 per cent in December 2008. Together, the share of sub-BPLR lending for all SCBs (excluding export credit and small loans) declined from 75.9 per cent in March 2008 to 71.5 per cent in December 2008. At the disaggregated level, the major share of sub-BPLR lending of PSBs was for longer tenure term loans (above 5 years), whereas for the private sector banks and foreign banks, the major share of sub-BPLR loans was for consumer credit.

Chart 32: Deposit and Lending Rates - Public Sector Banks



Government Securities Market

Central Government Securities

V.47 The financial year 2008-09 was characterised by a significantly higher level of Central Government market borrowing than budgeted earlier (as detailed in Chapter II), particularly during the second half of the year, in order to finance the expanding fiscal deficit in the wake of fiscal stimulus measures and various other committed expenditure of the Government. During the first six months of 2008-09, all issuances of dated securities were in accordance with the issuance calendar for the first half of the year, except on two occasions (Table 54). On the other hand, for the second half of the year, apart from the scheduled issuance calendar for dated securities released on September 26, 2008 in consultation with the Government of India, three additional indicative calendars were issued on December 5, 2008, January 6, 2009 and February 10, 2009. The Government of India raised Rs.1,16,000 crore to meet the additional expenditure approved by the Parliament by way of two supplementary demands for grants and various stimulus packages.

V.48 Furthermore, the MoU on the MSS signed between the Government of India and the Reserve Bank, in March 2004, was amended on February 26, 2009 to enable the Government and the Reserve Bank to de-sequester MSS cash balance for financing the Government's approved expenditure. Accordingly, it was decided to transfer an amount of Rs.45,000 crore, in installments, from the MSS cash account to the normal cash account of Government of India by March 31, 2009. An equivalent amount of government securities was to accordingly form part of the normal borrowing of the Government. In this regard, an amount of Rs.12,000 crore was transferred from the MSS cash account to the normal cash account of the Government of India on March 4, 2009. Inclusive of this amount, gross and net market borrowings (dated securities and 364-day Treasury Bills) of the Central Government during 2008-09 amounted to Rs.3,18,550 crore and Rs.2,42,316 crore, respectively, accounting for 93 per cent and 91 per cent of the revised market borrowings for the year, respectively. In view of the comfortable cash position, the Government of India, in consultation with the Reserve Bank, decided not to effect the transfer of the balance amount of Rs.33,000 crore in 2008-09. Based on the fund requirements of the Government, the balance amount would be de-sequestered against the approved market borrowing for 2009-10 or the MSS securities would be bought back in 2009-10. The MSS outstanding as on March 31, 2009 was Rs.88,773 crore.

V.49 Despite the significantly enhanced level, the market borrowing programme was managed smoothly by undertaking the following measures: (i) synchronising OMO (purchase of government securities) with issuances of dated securities under the market borrowing calendar, (ii) creating fiscal space by way of buyback of securities issued under the MSS, (ii) amending the MoU on MSS in February 2009, allowing

Table 54: Central Government Dated Securities Issued during 2008-09

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

	Borrowings as per Auction Calendar			Actual Borrowings			
Sr. No.	Period of auction	Amount	Residual Maturity	Date of Auction	Amount	Residual Maturity	Yield
1	2	3	4	5	6	7	8
1.	April 04 - 11, 2008	6,000	5-9 year	April 11, 2008	6,000	7.38	8.14
		4,000	20- year and above		4,000	24.37	8.67
2.	April 18 - 25, 2008	6,000	10-14 year	April 21, 2008	6,000	10.00	8.24
		4,000	20- year and above		4,000	28.13	8.77
3.	May 2-9, 2008	6,000	5-9 year	May 9,2008	6,000	7.92	7.96
		4,000	20-year and above		4,000	24.29	8.35
4.	May 16-23, 2008	6,000	10-14 year	May 23, 2008	6,000	9.91	8.07
		4,000	20-year and above		4,000	23.72	8.52
5.	May 30- June 6, 2008	6,000	10-14 year	June 6, 2008	6,000	9.87	8.26
		4,000	20 year and above		4,000	24.22	8.72
6.	June 13 - 20, 2008	6,000	15-19 year security	June 20,2008	6,000	18.64	9.25
7.	July 4-11, 2008	6,000	10-14 year	July 4, 2008	6,000	9.79	9.13
		4,000	20 year and above		4,000	23.60	10.02
8.	July 18-25,2008	6,000	15-19 year	July 24,2008	6,000	9.74	9.08
9.	August 1-8, 2008	6,000	10-14 year	August 8, 2008	6,000	9.70	9.14
		4,000	20 year and above		4,000	24.05	9.88
10.	August 14-22, 2008	6,000	15-19 year	August 22, 2008	6,000	18.47	9.86
11.	September 5-12, 2008	5,000	10-14 year	September 12, 2008	5,000	9.60	8.30
		3,000	20-year and above		3,000	23.95	8.70
				September 26,2008	6,000	12.65	9.04
					4,000	23.38	9.26
12.	October 3-10, 2008	6,000	5-9 year	Auction Cancelled	–	–	–
		4,000	20-year and above	Auction Cancelled	–	–	–
13.	October 17-24, 2008	6,000	10-14 year	Auction Cancelled	–	–	–
		4,000	20-year and above	Auction Cancelled	–	–	–
14.	October 31-November 7, 2008	6,000	5-9 year	October 31 , 2008	6,000	6.00	7.56
		4,000	20-year and above		4,000	23.82	8.08
				November 7,2008	6,000	9.45	7.73
					4,000	23.26	8.44
15.	November 14-21, 2008	6,000	5-9 year	November 14,2008	6,000	5.96	7.38
					4,000	23.78	8.21
				November 21,2008	6,000	5.94	7.16
					3,000	12.50	7.42

(Contd...)

Table 54: Central Government Dated Securities Issued during 2008-09 *(Concld.)*

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

	Borrowings as per Auction Calendar			Actual Borrowings			
Sr. No.	Period of auction	Amount	Residual Maturity	Date of Auction	Amount	Residual Maturity	Yield
1	2	3	4	5	6	7	8
16.	December 5-12, 2008	3,000	10-14 year	Preponed to			
				November 21, 2008	–	–	–
		6,000	5-9 year	December 12, 2008	6,000	4.72	6.24
		4,000	20-year and above		4,000	25.65	6.98
17.	January 2-9, 2009	6,000	5-9 year	January 2, 2009	6,000	8.65	5.73
		4,000	20-year and above		4,000	26.68	6.53
18.	January 5-9, 2009	7,000	5-9 year	January 9, 2009	7,000	7.25	6.70
		4,000	15-19 year		4,000	14.24	7.35
		4,000	20-year and above		4,000	25.58	7.60
19.	January 12-16, 2009	6,000	5-9 year	January 16, 2009	4,000	5.79	5.5
		4,000	20-year and above		3,000	30.00	6.83
					3,000	9.26	5.45
20.	January 23-30, 2009	6,000	10-14 year	January 30, 2009	3,000	5.75	6.02
		4,000	20-year and above		4,000	10.00	6.05
21.	February 6-9, 2009	5,000	5-9 year		3,000	29.96	7.35
		2,000	15-19 year	February 6, 2009	5,000	8.55	6.83
22.	February 13-20, 2009	6,000	10-14 year		2,000	14.17	7.15
		2,000	20-year and above	February 13, 2009	6,000	9.96	5.94
23.	February 20-27, 2009	6,000-7,000			2,000	29.23	7.37
		2,000-3,000		February 24, 2009	7,000	8.51	6.98
		2,000-3,000			3,000	13.22	7.50
24.	February 28-March 6, 2009	6,000-7,000			2,000	25.46	7.75
		2,000-3,000		March 6, 2009	8,000	9.90	6.50
		2,000-3,000			2,000	15.93	7.75
25.	March 6-March 13, 2009	6,000-7,000			2,000	29.86	7.90
		2,000-3,000		March 20, 2009	4,000	4.92	6.60
		2,000-3,000			6,000	9.86	6.59
26.	March 13-March 20, 2009	6,000-7,000		March 26,2009	5,000	4.43	6.77
		2,000-3,000			7,000	9.84	6.97
		2,000-3,000					

Note : 1. Issuances on December 12, 2008 and January 2, 2009 were as per calendar issued on December 5, 2008.
2. Issuances from January 12, 2009 to February 13, 2009 were as per calendar issued on January 6, 2009.
3. Issuances from February 24, 2009 to March 26, 2009 were as per calendar issued on February 10, 2009.

transfer from the MSS cash account to the normal cash account of the Government of India for financing of fiscal defict, and (iv) purchase of government securities on NDS-OM platform. All auctions during 2008-09 were for reissuance of existing securities, barring four new issues. The bid-cover ratio during 2008-09 was comparable with that of 2007-08. The devolvement on primary dealers (PDs) was higher in 2008-09 as compared with the previous year. The weighted average maturity and weighted average yield, both declined during 2008-09 (Table 55).

State Government Securities

V.50 The net allocation for the market borrowings of the State Governments during 2008-09 was placed at Rs.51,719 crore. Taking into account repayment of Rs.14,371 crore and additional allocation of Rs.62,990 crore (of which Rs.19,768 crore was on account of shortfall in NSSF collection and Rs.28,896 crore was on account of second fiscal stimulus package), the gross allocation of market borrowings was placed at Rs.1,29,081 crore for 2008-09 as compared with Rs.80,570 crore during the previous year. Twenty six State Governments and the Union Territory of Puducherry raised a total amount of Rs.1,18,138 crore through auctions (Table 56) with cut-off yields in the range 5.80-9.90 per cent as compared with Rs.67,779 crore by 25 State Governments (cut-off yields in the range 7.84-8.90 per cent) during the previous year. The weighted average interest rate on market loans was lower at 7.85 per cent during 2008-09 as compared with 8.25 per cent last year. The spreads of State Government securities over the yields of Central Government securities of corresponding maturity ranged between 21-236 basis points as compared with 19-90 basis points during 2007-08.

Table 55: Issuances of Central Government Dated Securities

	2007-08	2008-09
1	2	3
Number of Issuances		
Re Issue	34	52
New Issues	1	4
Bid-cover Ratio (Range)	1.58-4.76	1.22-4.51
Weighted Average		
Maturity (years)	14.9	13.8
Yield (per cent)	8.12	7.69
Devolvement on PDs (Rupees crore)	957	10,773

Secondary Market

V.51 Yields in the government securities market hardened from April 2008 till the first fortnight of July 2008 on account of the heightened inflationary expectations in the face of sharp increase in global commodity prices and concomitant monetary policy responses – hikes in the CRR and the LAF repo rate. Thereafter, the government securities' yields generally eased till around mid-September 2008 as inflationary pressures abated. The yields, however, temporarily hardened around end-September 2008 as liquidity conditions tightened in the wake of adverse developments in the international financial markets and advance tax outflows. In line with the liquidity augmenting measures taken by the

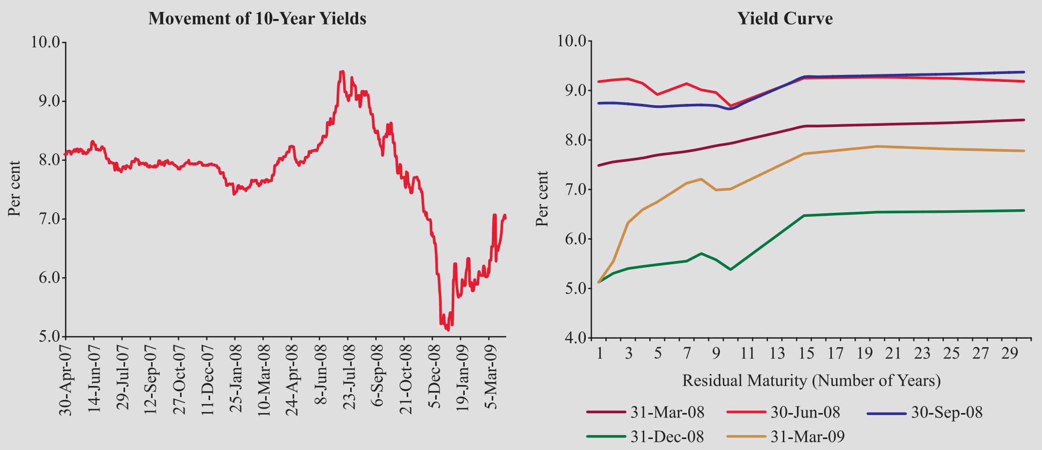
Table 56: Market Borrowings of the State Governments/U.T.s - 2008-09

Item		Date	Cut-off Yield (Per cent)	Tenor (Years)	Amount Raised (Rupees crore)
1		2	3	4	5
Auction					
i.	First	April 4, 2008	8.50-8.60	10	2,648
ii.	Second	May 27, 2008	8.39-8.68	10	3,264
iii.	Third	June 27, 2008	9.38-9.59	10	2,300
iv.	Fourth	July 10, 2008	9.81	10	500
v.	Fifth	August 31,2008	9.86-9.90	10	2,100
vi.	Sixth	August 26,2008	9.30-9.44	10	2,060
vii.	Seventh	September 9, 2008	8.80	10	1,800
viii.	Eighth	September 25, 2008	8.81-8.88	10	1,212
ix.	Ninth	October 7,2008	8.50-8.89	10	2,012
x.	Tenth	October 22, 2008	7.97-8.11	10	4,300
xi	Eleventh	November 11, 2008	8.21-8.54	10	3,595
xii.	Twelfth	November 20, 2008	7.77-7.86	10	4,850
xiii.	Thirteenth	December 11, 2008	6.95-7.10	10	5,910
xiv.	Fourteenth	December 23, 2008	6.38-6.45	10	4,795
xv.	Fifteenth	January 6, 2009	5.80-6.10	10	5,702
xvi.	Sixteeth	January 13, 2009	6.65-6.73	10	5,795
xvii.	Seventeenth	January 22,2009	7.00-7.13	10	7001
xviii.	Eighteenth	February 5,2009	7.24-7.29	10	5149
xix.	Nineteenth	February 17,2009	7.40-7.50	10	8362
xx.	Twentieth	February 27,2009	7.55-7.93	10	13424
xxi.	Twenty one	March 9, 2009	8.16-8.89	10	14095
xxii.	Twenty two	March 17, 2009	8.40-8.59	10	12215
xxiii.	Twenty three	March 24, 2009	8.08-8.48	10	5048
	Grand Total				**1,18,138**

Reserve Bank and the sharp decline in WPI inflation, the yields eased substantially till end-December 2008. The 10-year yield stood at 5.31 per cent as at end-December 2008, as compared with 8.63 per cent as at end-September 2008 and 7.93 per cent as at end-March 2008 (Chart 33).

V.52 Notwithstanding further reduction in the CRR and LAF rates in January 2009, market sentiment worsened in January and February 2009, following the large and abrupt increase in the Government's market borrowing programme for 2008-09, at a time when the system had excess SLR investment amounting to around Rs.1,79,000 crore. The large market borrowing requirement of the Government for 2009-10 also weighed on the market. Subsequent to the announcement of the Interim Budget on February 16, 2009, even as the Reserve Bank initiated a series of auction-based purchases of government dated securities in addition to its purchases through the NDS-OM, the 10-year yield increased to 6.02 per cent as at end-February 2009. The yields continued to

Chart 33: Yields on Central Government Securities



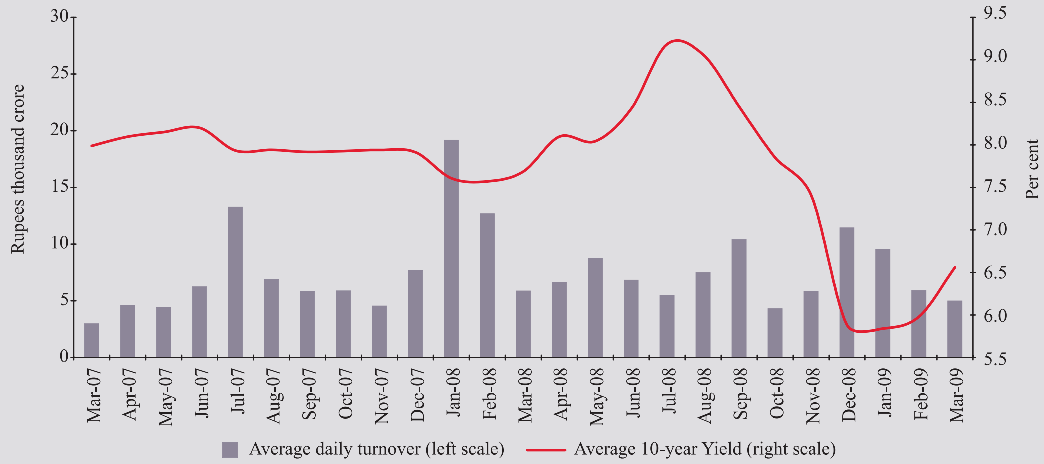
harden in early March 2009 despite a further cut in the LAF interest rates effective March 5, 2009. The benchmark 10-year paper (6.05 per cent government security 2019), however, dropped sharply by 40 basis points (from the closing level of March 12, 2009) to 7.07 per cent following the rejection of all bids received for sale of Government dated securities on March 13, 2009. The subsequent announcement of enhanced amounts of auction-based purchases of the government dated securities by the Reserve Bank on March 16 and 19, 2009, helped to improve market sentiments. The ten-year yield stood at 7.01 per cent as at end-March 2009.

V.53 The government securities yield curve moved upwards and peaked by end-July 2008 during 2008-09 (Chart 33). Thereafter, it moved downwards till end-December 2008 but again firmed up over the last quarter of 2008-09. The yield curve is kinked at the 5-year and 10-year yields where trading is concentrated and is flat beyond 15 years. As a sequel, the spread between 10-year and 15-year yields was 71 basis points as against the spread of 6 basis points between the 15-year and 30-year yields, as at end-March 2009.

V.54 The daily turnover in the Central Government securities market averaged Rs.6,935 crore during January-March 2009, which was around 4 per cent lower than that in the preceding quarter (Chart 34).

V.55 During 2008-09, the yield on 5-year AAA-rated corporate bonds, witnessed a hardening trend up to October 2008 and began to soften thereafter. The yield has been inching up again since February 2009. The credit spread between the yields on 5-year AAA-rated bonds and 5-year government securities have been wider in the second half of 2008-09 as compared with the first half (Chart 35). However, it narrowed during the fourth quarter of 2008-09, the spread being 179 basis points on March 31, 2009 as compared to 312 basis points on December 31, 2008.

Chart 34: Average Daily Turnover and Yields in Government Securities Market



Equity Market

Primary Market

V.56 The primary market segment of the domestic capital market witnessed a marginal increase during the fourth quarter of 2008-09. Cumulatively, resources raised through public issues declined sharply to Rs.14,671 crore during 2008-09 from Rs.83,707 crore during 2007-08. The number of issues also declined considerably from 119 to 45 (Table 57). Out of the 45 issues during 2008-09, 21 were initial public offerings (IPOs) issued by private sector companies, constituting 13.9 per cent of total resource mobilisation. Furthermore, all the issues during 2008-09 were equity issues by private non-financial companies except two by private financial companies. The average size of public issues declined

Chart 35: Credit Spreads

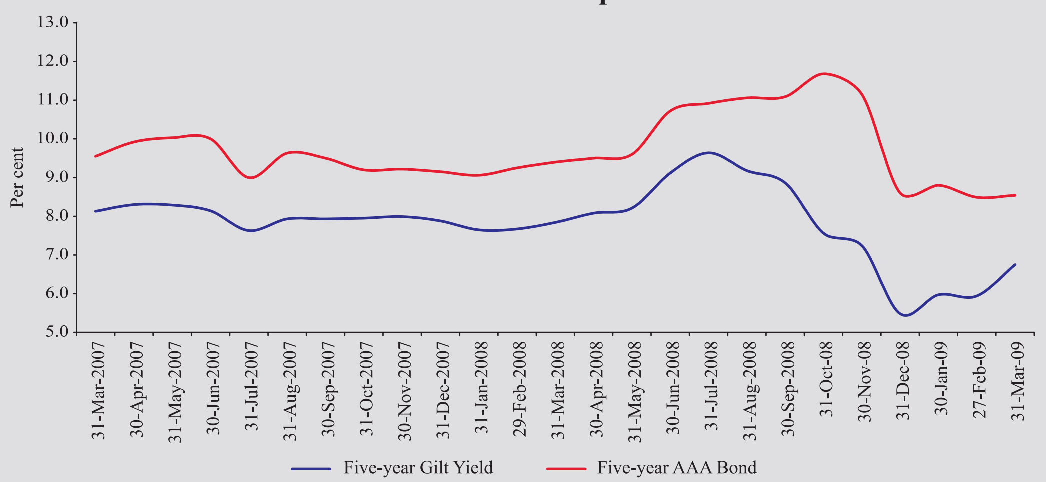


Table 57: Mobilisation of Resources from the Primary Market

(Amount in Rupees crore)

Item	No. of Issues	Amount	No. of Issues	Amount
1	2	3	4	5
	2007-08		2008-09 P	
A. Prospectus and Rights Issues*				
1. Private Sector (a+b)	**115**	**63,638**	**45**	**14.671**
a) Financial	11	14,676	2	466
b) Non-financial	104	48,962	43	14,205
2. Public Sector (a+b+c)	**4**	**20,069**	**–**	**–**
a) Public Sector Undertakings	–	–	–	–
b) Government Companies	2	2,516	–	–
c) Banks/Financial Institutions	2	17,553	–	–
3. Total (1+2)	**119**	**83,707**	**45**	**14,671**
of which:				
(i) Equity	116	82,398	45	14,671
(ii) Debt	3	1,309	–	–
	April-December 2007		April-December 2008	
B. Private Placement				
1. Private Sector (a+b)	**1,245**	**94,139**	**522**	**46,687**
a) Financial	693	63,916	235	26,265
b) Non-financial	552	30,223	287	20,422
2. Public Sector (a+b)	**117**	**55,817**	**130**	**65,605**
a) Financial	80	38,621	62	34,773
b) Non-financial	37	17,196	68	30,832
3. Total (1+2)	**1,362**	**1,49,956**	**652**	**1,12,292**
of which:				
(i) Equity	–	–	1	114
(ii) Debt	1,362	1,49,956	651	1,12,178
C. Euro Issues	**26**	**26,556**	**13**	**4,788**

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

from Rs.703.4 crore during 2007-08 to Rs.326.0 crore during 2008-09.

V.57 Mobilisation of resources through private placement declined by 25.1 per cent during April-December 2008 (the period for which the latest data are available) as against an increase of 35.2 per cent during April-December 2007 (refer Table 57). Public sector entities accounted for 58.4 per cent of total mobilisation as compared with 37.2 per cent during the corresponding period of the previous year. Resource mobilisation through financial intermediaries (both from public and private sector) registered a decline of 40.5 per cent over the corresponding period of last year and accounted for 54.4 per cent of the total mobilisation during April-December 2008.

However, resources raised by non-financial intermediaries registered an increase of 8.1 per cent (45.7 per cent of total resource mobilisation) during April-December 2008 over the corresponding period of the previous year.

V.58 During 2008-09, resources raised through Euro issues – American Depository Receipts (ADRs) and Global Depository Receipts (GDRs) – by Indian corporates declined significantly by 82.0 per cent to Rs.4,788 crore as compared with the corresponding period of the previous year. All the Euro issues during the financial year were GDR issues.

V.59 During 2008-09, net resource mobilisation by mutual funds turned negative; there was a net outflow of Rs.28,297 crore during the year as compared to a net inflow of Rs.1,53,801 crore during 2007-08 (Table 58). Scheme-wise, during 2008-09, income/debt oriented schemes witnessed a net outflow of Rs.32,161 crore, while growth/equity oriented schemes registered a net inflow of Rs.4,024 crore. There were substantial outflows during the months of June 2008 (Rs.39,233 crore), September 2008 (Rs.45,651 crore) and October 2008 (Rs.45,796 crore) due to the uncertain conditions in the stock markets and redemption pressures from banks and corporates on account of tight liquidity conditions prevailing at that time. The Reserve Bank then announced immediate measures to provide liquidity support to mutual funds through banks. With the easing of overall liquidity conditions, investment in mutual funds again became attractive. During November 2008 to February 2009, net resource mobilisation by mutual funds turned positive. However, during March 2009 there was a net outflow of Rs.98,697 crore.

Secondary Market

V.60 The domestic stock markets, after remaining weak and volatile during January-February 2009, witnessed gains

Table 58: Resource Mobilisation by Mutual Funds

(Rupees crore)

Category	2007-08		2008-09	
	Net Mobilisation	Net Assets	Net Mobilisation	Net Assets
1	2	3	4	5
Private Sector	1,33,304	4,15,621	-34,018	3,35,527
Public Sector *	20,497	89,531	5,721	81,772
Total	**1,53,801**	**5,05,152**	**-28,297**	**4,17,299**

* : Including UTI Mutual fund.

Note : 1. Data exclude funds mobilised under Fund of Funds Schemes.
2. Net Mobilisation is net of redemptions.
3. Net Assets is for end-period.

Source : Securities and Exchange Board of India.

during March 2009. The losses during the first two months of 2009 were mainly due to the downward trend in international equity markets on account of more than expected contraction of economic growth in the US, the UK, Japan and China pointing towards deepening of recession. Other factors that led to weak equity markets were heavy net sales by FIIs in the Indian equity market, slowdown in industrial and export growth, depreciation of the rupee against the US dollar, fall in ADR prices, lower than expected corporate earnings in the third quarter of 2008-09, revelations about financial irregularities in a particular information technology company and other sector and stock specific news. In line with the behaviour of equity markets across the world, the Indian stock markets have been showing improvement since March 2009. The reasons for the improvement are announcement of the details of US$ 1 trillion public private investment program by the US Treasury, some major US banks posting profits for the first two months of 2009, extention of the deadline for buyback of foreign currency convertible bonds (FCCBs) by the Reserve Bank to December 31, 2009, domestic consumer durable and capital goods output increasing by 2.5 per cent and 15.4 per cent, respectively, in January 2009, lower domestic inflation rate, strengthening of the rupee against the US dollar and net purchases by FIIs and mutual funds in domestic equity market. The BSE Sensex and the S&P CNX Nifty closed at 9709 and 3021 at end-March 2009 registering losses of 37.9 per cent and 36.2 per cent, respectively, over end-March 2008 (Chart 36). The BSE sensex closed at 11,023 on April 17, 2009.

V.61 According to the data released by the Securities and Exchange Board of India (SEBI), FIIs made net sales of Rs.48,249 crore (US $ 12.0 billion) in the Indian equity

Chart 36: Indian Stock Markets

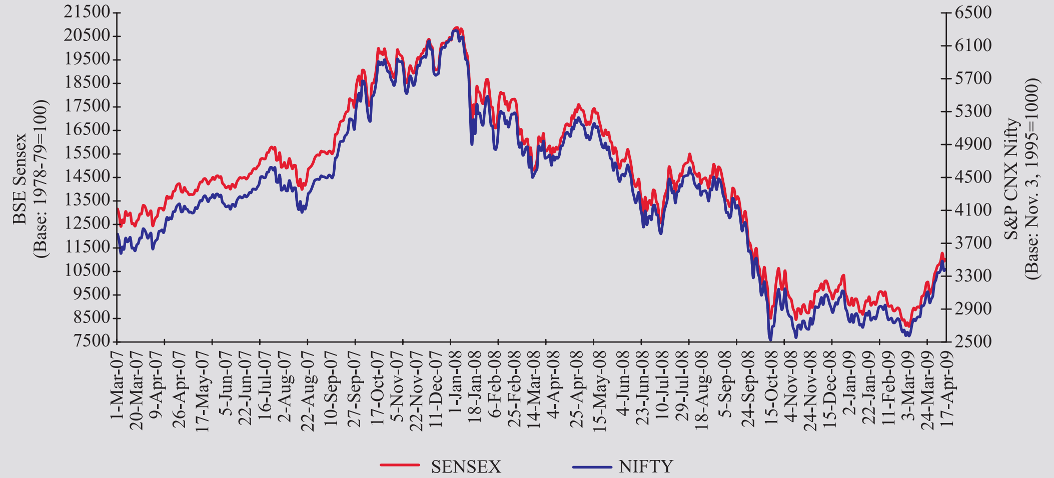
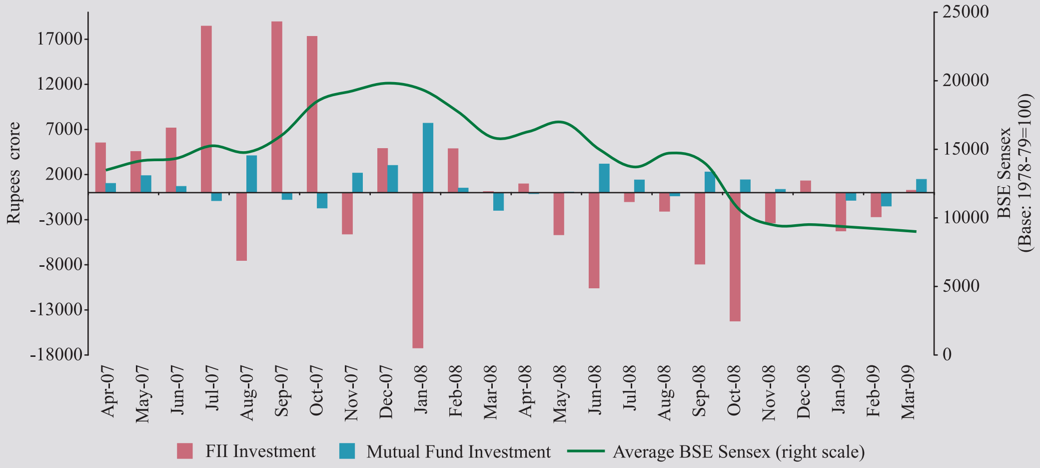


Chart 37: Net FIIs Investments and BSE Sensex



market during 2008-09 as against net purchases of Rs.52,574 crore (US $ 12.7 billion) during 2007-08 (Chart 37). Mutual funds, on the other hand, made net purchases of Rs.6,985 crore during 2008-09 as compared with net purchases of Rs.15,775 crore in the previous year.

V.62 The sectoral indices witnessed selling pressure across the board during 2008-09 *viz*., metal, consumer durables, capital goods, banking, IT, oil and gas, auto, public sector undertakings, healthcare and fast moving consumer goods sector (Table 59).

Table 59: BSE Sectoral Stock Indices

(Base: 1978-79=100)

Sector	Variation (per cent)		
	End-March 2007	End-March 2008	End-March 2009
1	2	3	4
Fast Moving Consumer Goods	-21.4	31.7	-11.1
Public Sector Undertakings	-3.2	25.4	-29.6
Information Technology	21.6	-27.6	-35.6
Auto	-8.5	-7.1	-32.3
Oil and Gas	30.5	56.0	-29.6
Metal	-4.3	65.2	-58.7
Health Care	-5.4	5.4	-26.5
Bankex	24.2	18.0	-41.8
Capital Goods	11.1	54.4	-53.8
Consumer Durables	11.1	8.8	-58.1
BSE 500	**9.7**	**24.3**	**-42.8**
BSE Sensex	**15.9**	**19.7**	**-37.9**

Source : Bombay Stock Exchange Limited.

V.63 In line with the downward trend in stock prices, the price-earnings (P/E) ratios of the 30 scrips included in the BSE Sensex declined from 20.1 at end-March 2008 to 13.7 at end-March 2009. The market capitalisation of the BSE also declined by 44.3 per cent between end-March 2008 and end-February 2009. The cash segment turnover of BSE and NSE also declined by 30.2 per cent during April-February 2008-09 over the corresponding period of 2007-08. The turnover in the derivative segment of BSE and NSE also declined by 25.1 per cent during April-February 2008-09 over the corresponding period of the previous year. The volatility in the stock market, measured as coefficient of variation, however, increased during 2008-09 (Table 60).

Table 60: Stock Market Indicators

Indicator	BSE		NSE	
	2007-08	2008-09	2007-08	2008-09
1	2	3	4	5
1. BSE Sensex / S&P CNX Nifty				
(i) End-period	15,644	9,709	4,735	3,021
(ii) Average	16,569	12,366	4,897	3,731
2. Coefficient of Variation	13.7	24.2	14.4	23.2
3. Price-Earning Ratio (end-period)*	20.1	13.7	20.6	14.3
4. Price-Book Value Ratio (end-period)*	5.2	2.7	5.1	2.5
5. Yield* (per cent per annum) (end-period)	1.0	1.8	1.1	1.9
6. Listed Companies	4,887	4924 #	1,381	1425 #
7. Cash Segment Turnover (Rupees crore)	15,78,856	10,30,284 #	35,51,038	25,49,224 #
8. Derivative Segment Turnover (Rupees crore)	2,42,308	12,264 #	1,30,90,478	99,70,552 #
9. Market Capitalisation (Rupees crore) @	51,38,015	28,62,873 #	48,58,122	26,75,622 #
10. Market Capitalisation to GDP Ratio (per cent)	108.8	52.8	102.9	49.3

* : Based on the 30 scrips included in the BSE Sensex and the 50 scrips included in the S&P CNX Nifty.
@ : As at end-period.
\# : As at end-February 2009.
Source : Bombay Stock Exchange Ltd. (BSE) and National Stock Exchange of India Ltd. (NSE).

Annex 2: Policy Response of the Reserve Bank since mid-September 2008	
Item	Key Measures
1	2
Monetary Measures	• Cut in the repo rate under the LAF by a cumulative 400 basis points from 9.0 to 5.0 per cent since October 20, 2008. • Cut in the reverse repo rate by a cumulative 250 basis points from 6.0 to 3.5 per cent since December 8, 2008.
Rupee Liquidity/ Credit Delivery	• Cut in the CRR by a cumulative 400 basis points of NDTL from 9.0 per cent to 5.0 per cent since October 11, 2008. • Introduction of a special refinance facility under Section 17(3B) of the Reserve Bank of India Act, 1934 under which all SCBs (excluding RRBs) are provided refinance from the Reserve Bank equivalent to up to 1.0 per cent of each bank's NDTL as on October 24, 2008 at the LAF repo rate up to a maximum period of 90 days. Banks are encouraged to use this facility for the purpose of extending finance to micro and small enterprises. The facility will continue up to September 30, 2009. • Institution of a term repo facility for an amount of Rs.60,000 crore under the LAF to enable banks to ease liquidity stress faced by mutual funds, NBFCs and housing finance companies (HFCs) with associated SLR exemption of 1.5 per cent of NDTL. This facility is available up to September 30, 2009 (banks can avail of this facility either on an incremental or on a rollover basis within their entitlement of up to 1.5 per cent of NDTL). • Reduction in statutory liquidity ratio (SLR) by one percentage point from 25 to 24 per cent of NDTL with effect from the fortnight beginning November 8, 2008. • Introduction of a mechanism to buyback dated securities issued under the MSS so as to provide another avenue for injecting liquidity of a more durable nature into the system. • Extension of the period of entitlement of the first slab of pre-shipment and post-shipment rupee export credit, by 90 days each, with effect from November 15, 2008 and December 1, 2008, respectively. • Increase in the eligible limit of the ECR facility for scheduled banks (excluding RRBs) from 15 per cent to 50 per cent of the outstanding export credit eligible for refinance at the prevailing repo rate under the LAF. • Amounts allocated, in advance, from SCBs for contribution to the SIDBI and the NHB to the extent of Rs.2,000 crore and Rs.1,000 crore, respectively, against banks' estimated shortfall in priority sector lending in March 2009. • Reduction in the provisioning requirements for all types of standard assets (for residential housing loan beyond Rs.20 lakh, standard advances in the commercial real estate sector, personal loans including outstanding credit card receivables, loans and advances qualifying as capital market exposure and

(Contd...)

Annex 2: Policy Response of the Reserve Bank since mid-September 2008 *(Contd.)*

Item	Key Measures
1	2
	non-deposit taking systemically important NBFCs) to a uniform level of 0.40 per cent except in case of direct advances to agricultural and SME sector which shall continue to attract provisioning of 0.25 per cent, as hitherto. • Downward revision of risk weights on banks' exposures to certain sectors, which had been increased counter-cyclically earlier. All unrated claims on corporates and claims secured by commercial real estate attract a uniform risk weight of 100 per cent as against the risk weight of 150 per cent prescribed earlier. Claims on rated as well as unrated non-deposit taking systemically important non-banking financial companies (NBFC-ND-SI) are uniformly risk weighted at 100 per cent. As regards the claims on asset financing companies (AFCs), there is no change in the risk weights, which continue to be governed by the credit rating of the AFCs, except the claims that attract a risk weight of 150 per cent under the new capital adequacy framework, reduced to a level of 100 per cent. • In order to provide liquidity support to housing, export and MSE sectors, the Reserve Bank provided a refinance facility of Rs.4,000 crore to the NHB, Rs. 5,000 crore to the EXIM Bank and Rs. 7,000 core to the SIDBI up to March 2010. • For more effective liquidity management, the Reserve Bank widened the scope of OMO by including purchases of government securities through an auction-based mechanism in addition to operations through NDS-OM.
Foreign Exchange Liquidity	• To continue selling foreign exchange (US dollars) through agent banks to augment supply in the domestic foreign exchange market or intervene directly to meet any demand-supply gaps. • To institute special market operations to meet the foreign exchange requirements of public sector oil marketing companies against oil bonds. • The ceiling rate on export credit in foreign currency increased to LIBOR plus 350 basis points subject to banks not levying any other charges. • Authorised Dealer (AD) category - I banks allowed to borrow funds from their head office, overseas branches and correspondents and overdrafts in nostro accounts up to a limit of 50 per cent of their unimpaired Tier 1 capital as at the close of the previous quarter or US$ 10 million, whichever was higher, as against the earlier limit of 25 per cent. • As a temporary measure, HFCs registered with the NHB were allowed to raise short-term foreign currency borrowings under the approval route, subject to compliance with prudential norms laid down by the NHB.

(Contd...)

Annex 2: Policy Response of the Reserve Bank since mid-September 2008 *(Concld.)*

Item	Key Measures
1	2
	• A forex swap facility with tenure up to three months to Indian public and private sector banks having overseas operations in order to provide them flexibility in managing their short term funding requirements at their overseas offices. The facility is available up to March 31, 2010. • Cumulative increase in the interest rate ceilings on FCNR (B) and NR(E)RA term deposits by 175 basis points each since September 16, 2008. • Proposals from Indian companies to prematurely buyback their FCCBs to be considered under the approval or automatic route, depending on the extent of discount of the FCCBs and the source of funds, subject to compliance with certain stipulated conditions. (The buyback should be financed by the company's foreign currency resources held in India or abroad and/or out of fresh external commercial borrowing (ECB) raised in conformity with the current norms for ECBs). Extension of FCCBs also to be permitted at the current all-in-cost for the relative maturity.
ECB Norms	• The all-in-cost ceiling for ECBs of average maturity period of three to five years and of maturity period over five years was enhanced to 300 basis points above LIBOR and 500 basis points above LIBOR, respectively. The all-in-cost ceiling for trade credit less than three years was enhanced to 6-month LIBOR plus 200 basis points. • ECBs up to US$ 500 million per borrower per financial year were permitted for rupee/foreign currency expenditure for permissible end-uses under the automatic route. • The definition of infrastructure sector for availing ECB was expanded to include mining, exploration and refinery sectors. Payment for obtaining license/permit for 3G spectrum by telecom companies was classified as eligible end-use for the purpose of ECB. • The requirement of minimum average maturity period of 7 years for ECB of more than US$ 100 million for rupee capital expenditure by the borrowers in infrastructure sector was dispensed with. • Borrowers were granted the flexibility to keep their ECB proceeds offshore or keep it with the overseas branches/subsidiaries of Indian banks abroad or to remit these funds to India for credit to their rupee accounts with AD category-I banks in India, pending utilisation for permissible end-uses. • NBFCs exclusively involved in financing of the infrastructure sector were permitted to avail of ECBs under the approval route from multilateral/regional financial institutions and Government-owned development financial institutions for on-lending to the borrowers in the infrastructure sector, subject to compliance with certain conditions.

VI. PRICE SITUATION

After reaching an intra-year peak of 12.9 per cent on August 02, 2008, inflation, as measured by year-on-year variations in WPI, fell sharply to 0.3 per cent on March 28, 2009. This large order of volatility in the inflation outcome in just one year is unprecedented. The sharp volatility in international commodity prices contributed significantly to the spiralling inflation in the first half, and then to the subsequent decline from a higher base at fast pace in the second half. When external and supply side factors condition the inflation trend along with demand pressures, demand management policy measures have to be employed in a calibrated manner. The surge that was witnessed in oil, food and commodity prices in the first half of 2008 had created testing conditions for the conduct of monetary policy. The sharp fall in inflation in the second half, however, has facilitated aggressive monetary easing, which aim at arresting the economic slowdown. Unlike the WPI based inflation, CPI based inflation in India, however, remains high, with recent evidence of very modest moderation, and the transmission process of lower inflation at the wholesale level to inflation at the retail level has emerged as an important issue in the conduct of Reserve Bank's monetary policy.

VI.1 During the first half of 2008-09, headline inflation increased in major economies, reflecting the combined impact of higher food and fuel prices as well as strong demand conditions, especially in emerging markets. Subsequently, inflation decelerated sharply as international energy and commodity prices declined substantially and demand pressures eased following the impact of global financial crisis. The monetary policy stance pursued by most central banks in advanced economies during 2008-09 was largely expansionary, aimed at mitigating the adverse implications of the financial crisis. The central banks in emerging market economies were engaged in pre-emptive monetary tightening till September 2008 to contain inflation and inflationary expectations. Subsequently, they reversed their policy stance and reduced their policy rates as the spillover of the US subprime crisis turned out to be much wider and deeper, severely affecting growth prospects.

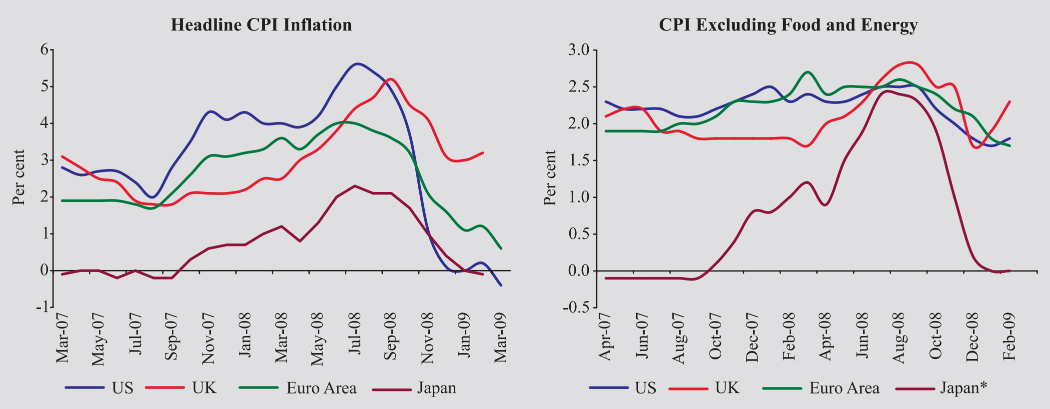
VI.2 In India, inflation as measured by year-on-year variations in the wholesale price index (WPI), increased sharply from 7.7 per cent at end-March 2008 to an intra-year peak of 12.9 per cent on August 2, 2008, reflecting the impact of some pass-through of higher international crude oil prices to domestic prices as well as continued increase in the prices of metals, chemicals, machinery and machinery tools, oilseeds/edible oils/oil cakes and raw cotton. Subsequently, WPI inflation declined sharply to 0.3 per cent as on March 28, 2009, led by the reductions in the administered prices of petroleum products and electricity as well as decline in the prices of freely priced petroleum products, oilseeds/edible oils/oil cakes, raw cotton, cotton textiles and iron & steel. The decline in prices of most of these commodities was in line with the decline in international commodity prices since July 2008. Consumer price inflation as reflected in various consumer price indices continued to remain high in the range of 9.6-10.8 per cent during January/February 2009 as compared with 7.3-8.8 per cent in June 2008 and 5.2-6.4 per cent in February 2008.

Global Inflation

VI.3 Headline inflation in major advanced economies firmed up till the second quarter of 2008-09 on account of higher energy and food prices and declined subsequently. Consumer price index (CPI) inflation in OECD countries increased from 3.6 per cent in March 2008 to 4.9 per cent in July 2008 but declined sharply to 1.3 per cent by February 2009. The recent decline in inflation in OECD countries was led by a decline in inflation of energy and food articles. Amongst major economies, headline inflation in the US declined to (-) 0.4 per cent in March 2009 from 5.6 per cent in July 2008. In the UK, inflation declined to 3.2 per cent in February 2009 from 5.2 per cent in September 2008. In the Euro area, inflation came down to 0.6 per cent in March 2009 from 4.0 per cent in July 2008 (Chart 38). Core inflation also moderated, though modestly in major economies. In OECD countries, inflation, excluding food and energy, came down to 1.9 per cent in February 2009 from 2.4 per cent in September 2008 (2.1 per cent at March 2008). Producer price index (PPI) inflation also moderated in both advanced and emerging market economies (EMEs). PPI inflation in the OECD countries, which firmed up from 6.3 per cent in March 2008 to 9.8 per cent in July 2008 declined sharply to (-)1.0 per cent in February 2009.

VI.4 According to the latest assessment of the US Federal Open Market Committee

Chart 38: Consumer Price Inflation



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

(FOMC) on March 18, 2009, in the light of increasing economic slackness in domestic and world economy, it was expected that inflation would remain subdued. Moreover, the Committee saw some risk that inflation rates could persist for a time below the levels that best foster economic growth and price stability in the longer term. However, the economy continued to contract. Furthermore, job losses, declining equity and housing wealth, and tight credit conditions weighed on consumer sentiment and spending. Against this backdrop, as the weak economic conditions warranted for exceptionally low levels of the federal funds rate (US policy rate), the FOMC kept the policy rate unchanged at a target range of 0.0-0.25 per cent since December 16, 2008. During 2008-09, the policy rate was reduced by a total of 200 basis points.

VI.5 According to the latest assessment of Monetary Policy Committee of the Bank of England, inflation is likely to fall below the 2 per cent target by the second half of 2009, reflecting diminishing contributions from retail energy and food prices and the impact of the temporary reduction in Value Added Tax. The committee viewed that there remains a substantial risk of undershooting the 2 per cent CPI inflation target in the medium term and that a further easing in monetary policy was warranted. Accordingly, the policy rate was reduced by 50 basis points to 0.5 per cent on March 5, 2009, taking the cumulative reduction to 475 basis points during 2008-09 (Table 61).

VI.6 According to the Governing Council of the ECB, inflation rates have decreased significantly and are expected to remain well below 2 per cent over 2009 and 2010 reflecting ongoing sluggish demand in Euro area and other countries. Accordingly, the ECB reduced the policy rate by 25 basis points to 1.25 per cent, effective April 8, 2009. Earlier, the ECB had cut the policy rate thrice by a total of 275 basis points since October 2008 to 1.50 per cent after raising it by 25 basis points in July 2008 (Chart 39).

VI.7 The Bank of Japan (BoJ), in its latest assessment on April 7, 2009, assessed that economic conditions have deteriorated significantly in Japan and are likely to continue deteriorating for the time being. Meanwhile, CPI inflation (excluding fresh food) has recently moderated reflecting the decline in the prices of petroleum products and the stabilisation of food prices. Furthermore, with increasing slackness evident in supply and demand conditions, CPI inflation rates are likely to become negative. Accordingly, the BoJ reduced its policy rate by 20 basis points each on October 31, 2008 and December 19, 2008 to 0.1 per cent.

VI.8 The policy rates were also reduced by the Reserve Bank of Australia by a total of 400 basis points to 3.00 per cent; Bank of Canada by a total of 250 basis points 0.50 per cent; Sveriges Riksbank (Sweden) by 375 basis points to 1.0 per cent and Swiss National Bank by 275 basis points to 0.0-0.75 per cent since October 2008.

Table 61: Global Inflation Indicators

(Per cent)

Country/ Region	Key Policy Rate	Policy Rate (As on April 16, 2009)	Changes in Policy Rates (basis points)		CPI Inflation (y-o-y)		PPI Inflation (y-o-y)		Real GDP Growth (y-o-y)	
			2007-08 (Apr-Mar)	Since end-March 2008	Mar. 2008	Mar. 2009	Feb. 2008	Feb. 2009	2007 (Q4)	2008 (Q4)
1	2	3	4	5	6	7	8	9	10	11
Developed Economies										
Australia	Cash Rate	3.00 (Apr.8, 2009)	100	(-) 425	3.0^	3.7^	2.8^	6.4^	3.9	0.3
Canada	Overnight Rate	0.50 (Mar. 3, 2009)	(-)75	(-) 300	1.8 *	1.4 *	-0.4	1.6	2.9	-0.7
Euro area	Interest Rate on Main Refinancing Operations	1.25 (Apr. 8, 2009)	25	(-) 275	3.6	0.6	5.3	-1.8	2.2	-1.3
Japan	Uncollateralised Overnight Call Rate	0.10 (Dec.19, 2008)	0	(-) 40	1.0*	-0.1*	3.6	-1.1	2.0	-4.3
UK	Official Bank Rate	0.50 (Mar. 5, 2009)	0	(-) 475	2.5*	3.2*	5.7	3.1	2.9	-2.0
US	Federal Funds Rate	0.00 to 0.25 (Dec.16, 2008)	(-)300	(-) 200	4.0	-0.4	6.4	-1.3	2.3	-0.8
Developing Economies										
Brazil	Selic Rate	11.25 (Mar. 12, 2009)	(-)150	0	4.7	5.6	10.6	7.4	6.2	1.3
India	Reverse Repo Rate	3.50 (Mar. 4, 2009)	0	(-) 250	5.5*	9.6*	7.7#	0.3#	8.9	5.3
	Repo Rate	5.00 (Mar. 4, 2009)	0 (150)	(-) 275 (-250)						
China	Benchmark 1-year Lending Rate	5.31 (Dec. 23, 2008)	108 (550)	(-) 216 (- 300)	8.7*	-1.6*	6.6	-4.5	11.2	6.8
Indonesia	Bank Indonesia Rate	7.50 (Apr.3, 2009)	(-) 100	(-) 50	6.3	7.9	23.8	7.9	6.3	5.2
Israel	Key Rate	0.50 (Apr.1, 2009)	(-) 25	(-) 325	3.7	3.6	10.7	-4.5	6.8	1.2
Korea	Base Rate**	2.00 (Feb 12, 2009)	50	(-) 300	3.9	3.9	6.6	5.2	5.5	-3.4
Philippines	Reverse Repo Rate	4.50 (Apr. 16, 2009)	(-) 250	(-) 50	6.4	6.4	-0.8	2.7	7.3	4.5
Russia	Refinancing Rate	13.00 (Dec.1, 2008)	(-) 25	275	13.3	14.0	25.7	-8.2	7.7	1.1
South Africa	Repo Rate	9.50 (Mar. 25, 2009)	200	(-) 150	9.8*	8.6*	11.3	7.3	4.6	1.0
Thailand	1-day Repurchase Rate	1.25 (Apr. 8, 2009)	(-) 125	(-) 200	5.3	-0.2	11.1#	-4.0#	5.7	-4.3

^ : Q4. *: February. # : March.

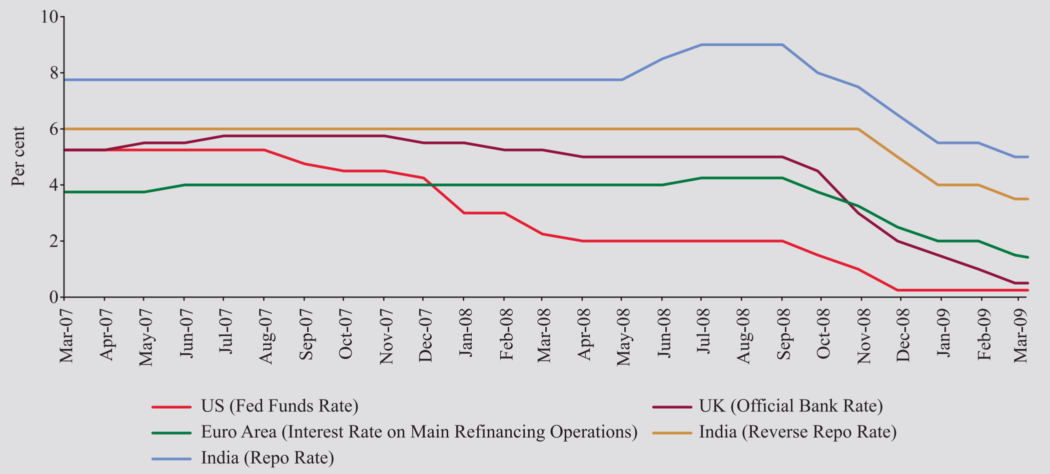
** : Since March 2008, the policy rate has been changed from overnight call rate to 'the Bank of Korea Rate or (Base Rate)' and fixed at the same level as the current call rate target of 5.0 per cent on March 7, 2008.

Note : 1. For India, data on inflation pertain to CPI for Industrial Workers.
2. Figures in parentheses in column (3) indicate the dates when the policy rates were last revised.
3. Figures in parentheses in columns (5) and (6) indicate the variation in the cash reserve ratios during the period**.**
4. Data for India and Indonesia pertains to WPI in columns (8) and (9).

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

VI.9 Among the major emerging economies, consumer price inflation in China declined sharply from 8.3 per cent in March 2008 to a negative 1.6 per cent in February 2009 (Chart 40). The Peoples Bank of China (PBC) reduced the benchmark 1-year lending rate by a total of 216 basis points to 5.31 per cent and

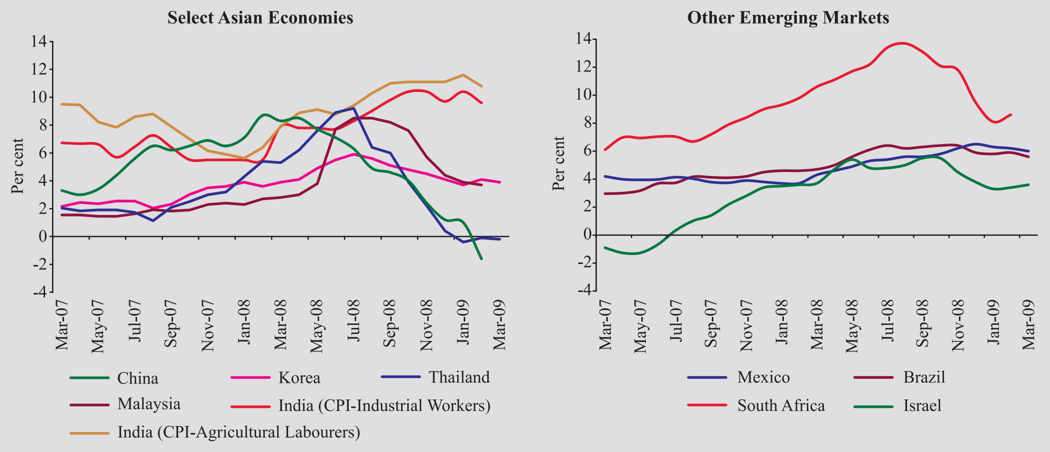
Chart 39: Central Bank Policy Rates



cash reserve ratio (CRR) by a total of 300 basis points (400 basis points for small and medium-sized depository financial institutions) since September 2008 to facilitate continued, stable and fast development of the national economy.

VI.10 The Bank of Korea reduced its policy rate by a total of 325 basis points since October 2008 to 2.0 per cent. In Thailand, the monetary policy committee (MPC) viewed that risks to economic growth increased while inflation was expected to decline further. It has reduced the policy rate by a total of 250 basis points since December 2008 to 1.25 per cent. The Bank Indonesia reduced its policy rate by a total of 200 basis points since December 2008 to 7.50 per cent to reinforce the domestic economy, macroeconomic stability and financial system.

Chart 40: Consumer Price Inflation – Emerging Market Economies



VI.11 Amongst the key macroeconomic indicators in select EMEs, consumer price inflation was in the range of (-)1.6 per cent to 14.0 per cent in February/March 2009. Real policy rates ranged between (-)4.6 and 6.9 per cent in March 2009 (Table 62). The real effective exchange rate (REER) for the select EMEs, barring the currency of China, underwent real depreciation, on a year-on-year basis, in March 2009.

Global Commodity Prices

VI.12 During 2008-09, international commodity prices recorded very high level of volatility. International commodity prices witnessed sharp increases up to July 2008 on account of substantial increases in oil, food and metal prices but declined significantly thereafter. The decline in global commodity prices have been led by sharp fall in price of crude oil, metals as well as agricultural commodities. The

Table 62: Key Macroeconomic Indicators: Emerging Markets

(Per cent)

Country	Consumer Price Inflation		Real Effective Exchange Rate (REER)		Central Govt. Fiscal Balance (per cent of GDP)		Real Policy Rate		Real GDP Growth	
	Mar. 2008	Mar. 2009	Mar. 2008	Mar. 2009	2007	2008	Mar. 2008	Mar. 2009	2007	2008
1	2	3	4	5	6	7	8	9	10	11
Brazil	4.7	5.6	12.9	-14.0	-2.3	-1.5	6.6	5.7	5.7	5.8
China	8.7 *	-1.6 *	4.7	14.5	1.0	0.8	-0.8	6.9	13.0	9.0
India	**5.5 ***	**9.6 ***	5.0	-11.5	**-2.7**	**-6.0 @**	**-0.2**	**-4.6**	**9.0**	**7.1**
	(7.7)	**(0.3)**			**(60.1)**	**(57.8)**	**(0.0)**	**(4.7)**		
Indonesia	6.3	7.9	-6.2	-9.7	-1.6	-1.1	1.7	-0.2	6.3	6.1
Israel	3.7	3.6	9.0	-2.2	-0.8	-1.9	0.0	-2.9	5.4	4.3
Korea	3.9	3.9	-13.7	-24.9	-1.5	-1.1	1.1	-1.9	5.0	4.1
Philippines	6.4	6.4	10.0	-1.6	-0.2	-1.0	-1.4	-1.7	7.2	4.4
Russia	13.3	14.0	5.5	-9.8	6.2	6.1	-3.1	-1.0	8.1	6.2
South Africa	9.8 *	8.6 *	-12.1	-1.1	2.0 **	2.8 **	0.4	1.9	5.1	3.1
Thailand	5.3	-0.2	2.4	-4.8	-1.7	-1.8	-2.1	1.7	4.8	4.7

* : February. @ : Revised estimates. ** : Africa.

Note:
1. For India, data pertain to fiscal years 2007-08 and 2008-09.
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. Data on fiscal balance for Israel pertain to general government balance.
6. Figures in parentheses in columns (6) and (7) refer to central government debt/GDP ratio.
7. Figures in parentheses in columns (8) and (9) for India are based on wholesale price inflation.
8. 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 and pertain to February.

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

Table 63: International Commodity Prices

Commodity	Unit	2004 Market Price	Index (2004=100) 2005	2006	2007	Mar. 2008	Jun. 2008	Sep. 2008	Dec. 2008	Mar. 2009	Variation (Per cent) Mar. 09/ Mar. 08	Mar. 09/ Jul. 08
1	2	3	4	5	6	7	8	9	10	11	12	13
Energy												
Coal	$/mt	53.0	90	93	124	223	302	283	149	115	-48.4	-66.1
Crude oil (Average)	$/bbl	37.7	142	170	188	270	349	264	110	124	-54.2	-64.9
Non-Energy Commodities												
Palm oil	$/mt	471.3	90	101	165	265	257	164	107	127	-52.2	-47.1
Soybean oil	$/mt	616.0	88	97	143	240	250	199	120	118	-50.9	-52.0
Soybeans	$/mt	306.5	90	88	125	188	203	166	117	123	-34.3	-40.4
Rice	$/mt	237.7	120	128	137	250	318	288	224	247	-1.0	-19.6
Wheat	$/mt	156.9	97	122	163	280	222	188	140	147	-47.5	-29.6
Maize	$/mt	111.8	88	109	146	210	257	209	142	147	-29.8	-38.0
Sugar	c/kg	15.8	138	206	141	184	169	189	164	187	1.5	-5.8
Cotton A Index	c/kg	136.6	89	93	102	129	124	119	90	83	-35.8	-33.4
Aluminium	$/mt	1716.0	111	150	154	175	172	147	87	78	-55.5	-56.5
Copper	$/mt	2866.0	128	235	248	294	288	244	107	131	-55.6	-55.4
Gold	$/toz	409.2	109	148	170	237	217	203	199	226	-4.6	-1.6
Silver	c/toz	669.0	110	173	200	287	255	182	154	196	-31.8	-27.4
Steel cold-rolled coilsheet	$/mt	607.1	121	114	107	132	181	181	181	148	12.5	-18.2
Steel hot-rolled coilsheet	$/mt	502.5	126	119	109	149	199	199	199	159	6.7	-20.0
Tin	c/kg	851.3	87	103	171	233	261	216	132	125	-46.1	-53.9
Zinc	c/kg	104.8	132	313	309	240	181	166	105	116	-51.5	-34.3

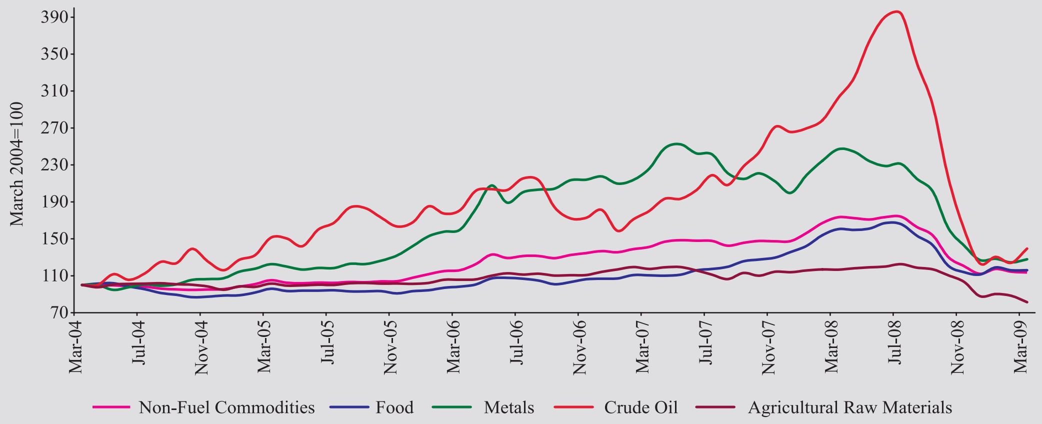
$: US dollar. c: US cent. bbl: barrel. mt: metric tonne. kg: Kilogram. toz: troy oz.

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.

global commodity prices have, however, remained broadly stable since December 2008 (Table 63 and Chart 41).

VI.13 International crude oil prices, represented by the West Texas Intermediate (WTI), increased sharply and

Chart 41: International Commodity Prices



Source: International Monetary Fund.

reached a historical peak of US $ 145.3 per barrel on July 3, 2008, reflecting tight supply-demand balance, geopolitical tensions, weakening of the US dollar against major currencies and increased interest from investors and financial market participants. Subsequently, the WTI crude oil prices declined precipitously to US $ 39.2 per barrel in February 2009, reflecting falling demand in the Organisation for Economic Co-operation and Development (OECD) countries as well as some developing countries, notably in Asia, following the economic slowdown (Table 64). Subsequently, WTI crude oil prices firmed up to US$ 50.0 per barrel on April 16, 2009.

VI.14 The latest meeting of OPEC on March 15, 2009 projected a decline in world demand for oil by 1 million barrel per day during 2009, indicating that the prices would remain stable at the current level. According to the US Energy Information Administration (EIA), sustainability of recent increase in world oil prices will largely depend upon the timing and pace of the recovery of the global economy. If global economic recovery begins earlier and is stronger, there is an upside risk of even higher oil prices from the current level. Assuming no major crude oil supply disruptions, average WTI prices are expected to be US$ 52.6 per barrel in 2009, which is 47 per cent lower than the average price for the year 2008 (US$ 99.6 per barrel). In view of the relatively tight demand supply-balance over the long run, the long term outlook for oil, however, remains highly uncertain (Table 65).

VI.15 Iron and steel prices increased sharply up to August 2008, reflecting increasing demand from emerging economies, especially China. Between

Table 64: 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
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
2007-08	77.3	82.4	82.3	80.7	79.2
March 2008	96.8	103.3	105.5	101.8	99.4
June 2008	127.6	133.1	133.9	131.5	129.8
July 2008	131.2	133.9	133.4	132.8	132.3
August 2008	113.2	113.9	116.6	114.6	113.5
September 2008	96.0	99.1	103.9	99.7	97.1
December 2008	41.0	41.6	41.4	41.3	41.2
January 2009	45.0	44.9	41.7	43.9	44.9
February 2009	43.1	43.2	39.2	41.8	43.2
March 2009	45.6	46.8	47.5	46.6	46.1

Source : International Monetary Fund and the World Bank.

Table 65: World Supply-Demand Balance of Oil

(Million barrels per day)

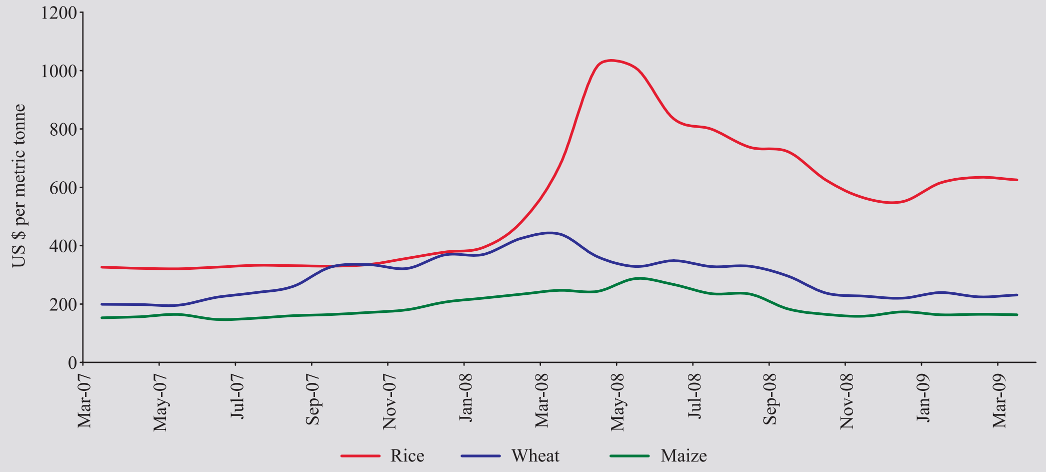
Item	2007	2008	2009 (P)	2009			
				Q1	Q2(P)	Q3(P)	Q4(P)
1	2	3	4	5	6	7	8
Demand							
1. OECD	49.1	47.3	45.7	46.4	44.7	45.2	46.7
2. Non-OECD	36.8	38.1	38.4	37.3	38.4	38.6	39.1
of which: China	7.6	7.9	8.0	7.5	8.0	8.2	8.4
3. Total (1+2)	85.9	85.4	84.1	83.7	83.1	83.8	85.8
Supply							
4. OPEC	34.4	35.7	33.7	33.0	33.4	33.8	34.4
5. Non-OPEC	50.0	49.8	49.8	49.6	49.9	49.8	49.8
6. Total (4+5)	84.4	85.5	83.4	82.6	83.3	83.6	84.1
Stock Changes	-1.5	0.1	-0.7	-1.0	0.2	-0.2	-1.7

P: Projections.
Source: US Energy Information Administration.

March and August 2008, the World Bank steel price product index increased by 37 per cent. International steel prices, however, declined by about 25 per cent since August 2008 as global economic downturn has led to lower prospects for construction activity and investment in capital equipment. Non-ferrous metal prices eased in 2008-09, reflecting weak demand in OECD countries and some improvement in supply. The IMF metals price index (which includes copper, aluminum, iron ore, tin, nickel, zinc, lead, and uranium price indices) declined by 48.2 per cent year-on-year, in March 2009.

VI.16 Food prices continued to increase sharply in the first quarter of 2008-09 led by rice, maize and oilseeds/edible oils prices, reflecting surging demand (both consumption demand and demand for non-food uses such as bio-fuels production) and low stocks of major crops. Food prices, however, eased significantly since the second quarter of the year on the back of improved supply prospects, particularly for oilseeds and grains in major producing countries. The World Bank's food price index declined by about 32 per cent year-on-year by March 2009, led by edible oils, rice, maize and wheat (Chart 42). According to the March 2009 projections of US Department of Agriculture, global wheat and rice production are projected to increase by about 12 per cent and 2 per cent, respectively, during 2008-09 crop season to 682 million metric tonnes and 441 million metric tonnes. Similarly, global supplies of oilseeds are also expected to increase by about 3 per cent during 2008-09 crop season. However, according to the Food and Agriculture Organisation (FAO), early indications for the year 2009 point to a reduction in cereal output.

Chart 42: International prices of Rice, Wheat and Maize



VI.17 International sugar prices have remained volatile during 2008-09 and the price level in February 2009 was almost the same as at end-March 2008. Since December 2008, international sugar prices rose by 14 per cent on expectations that India will become a net importer due to downward revision in its crop size and expectations of lower crops in the EU, US, China and Australia. Global cotton prices, have also been volatile during August 2008. World cotton prices (represented by the 'Cotton A Index') have declined by 34 per cent since August 2008. However, according to the International Cotton Advisory Committee (ICAC), world cotton production is expected to decline for the third consecutive season during 2009-10 and prices are projected to increase by 5 per cent.

Inflation Conditions in India

VI.18 The Annual Policy Statement for 2008-09 (April 2008) of the Reserve Bank was announced on the background of elevated inflation levels, and the Policy Statement reaffirmed its resolve to bring down inflation to around 5.5 per cent in 2008-09 with a preference for bringing it as close to 5.0 per cent as soon as possible, recognising the evolving complexities in globally transmitted inflation. As the potential inflationary pressures from international food and energy prices had amplified, the policy focused on conditioning perceptions for inflation in the range of 4.0-4.5 per cent so that an inflation rate of around 3.0 per cent became a medium-term objective consistent with India's broader integration into the global economy and with the goal of maintaining self-accelerating growth over the medium-term.

VI.19 Inflation hardened during the first quarter of 2008-09 on account of strong demand and significant international commodity price pressures. Therefore, it was recognised that an adjustment of overall aggregate demand on an economy-wide basis was warranted to ensure that generalised instability did not develop and erode the hard-earned gains in terms of both outcomes of and positive sentiments on India's growth momentum. The priority for monetary policy was identified to be eschewing any further intensification of inflationary pressures and to firmly anchor inflation expectations. Accordingly, the Reserve Bank increased the cash reserve ratio (CRR) by a total of 100 basis points between May and July 2008 to 8.75 per cent. Furthermore, the repo rate under the Liquidity Adjustment Facility (LAF) was increased by a total of 75 basis points to 8.50 per cent in June 2008. The First Quarter Review of the Annual Statement on Monetary Policy for 2008-09 expected that inflation would moderate from then prevailing high levels in the months to come. In view of the prevailing macroeconomic, liquidity and overall monetary conditions, the First Quarter Review announced an increase in the fixed repo rate under the LAF by 50 basis points from 8.5 per cent to 9.0 per cent with effect from July 30, 2008 and an increase in the CRR by 25 basis points to 9.0 per cent with effect from August 30, 2008 (Table 66).

VI.20 WPI inflation started to decline since August 2008, mainly on account of decline in prices of freely priced petroleum products, edible oils and textiles. The Mid-Term Review of Annual Policy for the Year 2008-09 observed that in the absence of further shocks, generalised inflation could not be sustained, especially with money supply contained at the average rate of 2003-08, a period when inflation was low and stable. The Review also noted that the effect of softening international commodity prices on inflation in India could be muted just as the elevation of international commodity prices was not fully passed on to domestic prices. The challenge for the setting of monetary policy was identified to be balancing the costs of lowering inflation in terms of output volatility (particularly in the context of the moderation in industrial and services sector activity) against the risk of then prevailing levels of inflation persisting and getting embedded in inflation expectations. The review highlighted the importance of remaining focused on bringing inflation down to levels that are compatible with a strong but stable momentum of growth in the economy and financial stability while recognising that there existed high level of uncertainty with this judgment.

VI.21 Since September 2008, the Reserve Bank adjusted its policy stance from demand management to arresting the moderation in growth, as India's growth trajectory has been impacted both by the financial crisis and the global economic downturn. Accordingly, between September 2008 and January 2009, the Reserve Bank reduced the repo rate under the LAF from 9.0 per cent to 5.5 per cent, the reverse repo rate under the LAF from 6.0 per cent to 4.0 per cent and the CRR from 9.0 per cent to 5.0 per cent. The aim of these measures was to augment domestic liquidity and to ensure that credit continues to flow to productive sectors of

Table 66: Movements in Key Policy Rates in India

(Per cent)

Effective since	Reverse Repo Rate	Repo Rate	Cash Reserve Ratio	WPI Inflation	CPI (IW) Inflation
1	2	3	4	5	6
June 9, 2006	5.75 (+0.25)	6.75 (+0.25)	5.00	4.9	7.7
July 25, 2006	6.00 (+0.25)	7.00 (+0.25)	5.00	4.7	6.7
October 31, 2006	6.00	7.25 (+0.25)	5.00	5.4	7.3
December 23, 2006	6.00	7.25	5.25 (+0.25)	5.8	6.9
January 6, 2007	6.00	7.25	5.50 (+0.25)	6.4	6.7
January 31, 2007	6.00	7.50 (+0.25)	5.50	6.7	6.7
February 17, 2007	6.00	7.50	5.75 (+0.25)	6.0	7.6
March 3, 2007	6.00	7.50	6.00 (+0.25)	6.5	6.7
March 31, 2007	6.00	7.75 (+0.25)	6.00	5.9	6.7
April 14, 2007	6.00	7.75	6.25 (+0.25)	6.3	6.7
April 28, 2007	6.00	7.75	6.50 (+0.25)	6.0	6.7
August 4, 2007	6.00	7.75	7.00 (+0.50)	4.4	7.3
November 10, 2007	6.00	7.75	7.50 (+0.50)	3.2	5.5
April 26, 2008	6.00	7.75	7.75 (+0.25)	8.3	7.8
May 10,2008	6.00	7.75	8.00 (+0.25)	8.6	7.8
May 24,2008	6.00	7.75	8.25 (+0.25)	8.9	7.8
June 12, 2008	6.00	8.00 (+0.25)	8.25	11.7	7.7
June 25, 2008	6.00	8.50 (+0.50)	8.25	11.9	7.7
July 5, 2008	6.00	8.50	8.50 (+0.25)	12.2	8.3
July 19, 2008	6.00	8.50	8.75 (+0.25)	12.5	8.3
July 30, 2008	6.00	9.00 (+0.50)	8.75	12.5	8.3
August 30, 2008	6.00	9.00	9.00 (+0.25)	12.4	9.0
October 11, 2008	6.00	9.00	6.50 (–2.50)	11.3	10.4
October 20, 2008	6.00	8.00 (–1.00)	6.50	10.8	10.4
October 25, 2008	6.00	8.00	6.00 (–0.50)	10.7	10.4
November 3, 2008	6.00	7.50 (–0.50)	6.00	8.7	10.4
November 8, 2008	6.00	7.50	5.50 (–0.50)	8.7	10.4
December 8, 2008	5.00 (–1.00)	6.50 (–1.00)	5.50	6.6	9.7
January 5, 2009	4.00 (–1.00)	5.50 (–1.00)	5.50	5.3	10.4
January 17, 2009	4.00	5.50	5.00 (–0.50)	4.9	10.4
March 4, 2009	3.50 (-0.50)	5.00 (-0.50)	5.00	2.4	–

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.

2. Figures in parentheses indicate change in policy rates.

the economy. The Third Quarter Review of the Annual Statement on Monetary Policy for 2008-09 assessed that the inflation rate was expected to moderate further in the last quarter of 2008-09. Keeping in view the global trend in commodity prices and the domestic demand-supply balance, WPI inflation was projected to decelerate to below 3.0 per cent by end-March 2009 from then prevailing level of 5.6 per cent. The review also noted that the consumer price inflation was yet to moderate and the decline in inflation expectations had not been commensurate with the sharp fall in WPI inflation. It recognised that the headline WPI inflation could fall below 3 per cent in the short-run partly because of statistical reason of high base since early 2008 mainly caused by exceptionally high global oil and commodity prices. It affirmed that with the policy endeavour of ensuring price stability with well-anchored inflation expectations, the Reserve Bank would take into account the behaviour of all the price indices and their components.

VI.22 As the global financial and economic conditions further deteriorated since the Third Quarter Review and the impact on India's growth trajectory has turned out to be deeper and wider than anticipated earlier, the Reserve Bank further announced monetary stimulus measures in terms of reduction in the repo rate under the LAF from 5.5 per cent to 5.0 per cent, the reverse repo rate under the LAF from 4.0 per cent to 3.5 per cent on March 4, 2009.

Wholesale Price Inflation

VI.23 During 2008-09, inflation in India, based on the wholesale price index (WPI) firmed up to an intra-year peak of 12.9 per cent on August 2, 2008 from 7.7 per cent at end-March 2008. The increase in inflation during March-August 2008 was mainly on account of some pass-through of high international crude oil prices to domestic prices as well as elevated levels of prices of iron and steel, basic heavy inorganic chemicals, machinery and machine tools, oilseeds/oil cakes, raw cotton and textiles. The increase in inflation during this period reflected strong demand pressures as well as international commodity price pressures.

VI.24 WPI inflation exhibited strong downward trend since August 2008 and reached 0.3 per cent as on March 28, 2009. Between August 2, 2008 and March 28, 2009, WPI declined by 5.8 per cent driven by the reduction in the administered prices of petroleum products and electricity as well as decline in prices of freely priced minerals oil items, iron and steel, oilseeds, edible oils, oil cakes and raw cotton (Table 67). Significant part of the end year reduction in WPI inflation could also be attributed to the base effect reflecting the rapid increase in inflation recorded during the last quarter of 2007-08.

VI.25 The inflation momentum, as indicated by the movement of the annualised month-over-month (M-o-M) seasonally adjusted WPI inflation, was declining since June 2008 and entered negative territory in September 2008 itself. Thereafter, it maintained a strong and secular disinflationary momentum till November 2008 and was reversed in January 2009. According to the latest data available, annualised WPI (seasonally

Table 67: Key Commodity Prices – Global *vis-à-vis* Domestic (year-on-year)

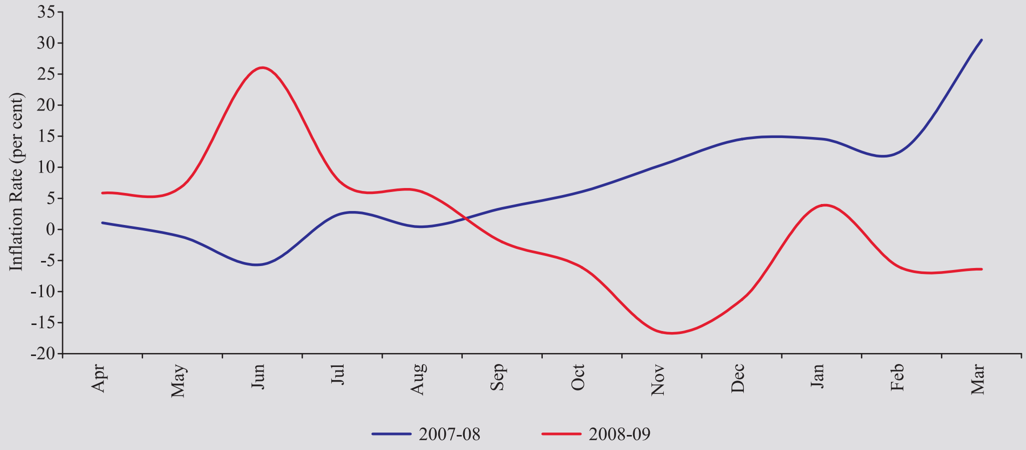
(Per cent)

Item	Annual Inflation		Recent trends	
	Global	India	Global	India
	Mar. 2009 over Mar. 2008	Inflation*	Mar. 2009 over July 2008	Mar.28, 2009 over Aug. 2, 2008
1	2	3	4	5
1. Rice	-1.0	12.8	-19.6	11.4
2. Wheat	-47.5	5.2	-29.6	2.8
3. Milk	..	6.1	..	3.9
4. Raw Cotton	-35.8	2.5	-33.4	-17.6
5. Oilseeds	-34.3	-2.3	-40.4	-8.7
6. Iron Ore	0.0	-16.8	0.0	-17.1
7. Coal mining	-48.4	-1.0	-66.1	-1.0
8. Minerals Oil	-54.2	-8.7	-64.9	-23.3
9. Edible Oils	-(51-52)	-10.2	-(47-52)	-11.5
10. Oil Cakes	-22.6	19.4	-32.5	-0.3
11. Basic Heavy Inorganic Chemicals	..	-13.7	..	-20.9
12. Basic Metals, Alloys and Products	-48.2 #	-12.2	-44.6 #	-14.7
- Iron and Steel	2.7	-18.4	-23.5	-20.6

***** : Based on WPI as on March 28, 2009.
\# : Represented by IMF metals price index, which covers copper, aluminium, iron ore, tin, nickel, zinc, lead and uranium.
Note: 1. Global price increases are based on the World Bank and IMF primary commodity prices data.
2. International edible oils prices are represented by palm oil and soybean oil.

adjusted) inflation for the month ended March 2009 remains in the negative territory (Chart 43). It may be noted that though M-o-M seasonally adjusted inflation is a useful indicator of inflationary conditions, it tends to be volatile.

Chart 43: Annualised M-o-M seasonally adjusted inflation of WPI-All Commodities

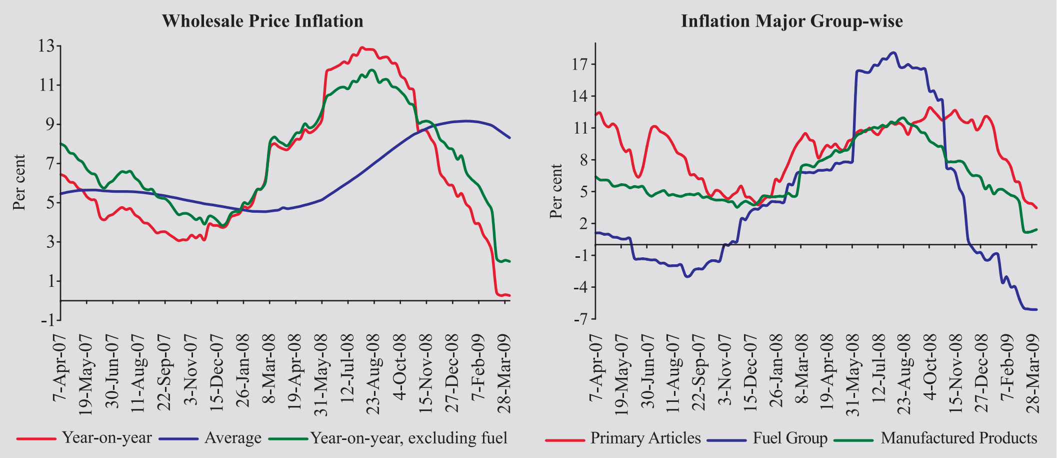


VI.26 At a disaggregated level, the y-o-y inflation, excluding fuel, was at 2.0 per cent as on March 28, 2009 as compared with 8.0 per cent a year ago. It can be observed that during the period June-October 2008, when WPI inflation was at substantially high levels, overall inflation was higher than the WPI excluding fuel inflation. Since October 2008 the overall inflation has been lower than the inflation excluding fuel with some convergence being observed in recent months (Chart 44). The annual average WPI inflation rate (average of 52 weeks) increased to 8.3 per cent as on March 28, 2009 from 5.7 per cent at end-June 2008 and 4.7 per cent at end-March 2008.

VI.27 Amongst major groups, primary articles inflation, y-o-y, increased from 9.7 per cent at end-March 2008 to a peak of 12.7 per cent on November 15, 2008. This mainly reflected increase in the prices of food articles as well as non-food articles. The volatility in prices of food articles was of substantially lower magnitude in contrast with sharp increase in international prices of food during the first half of 2008. The y-o-y increase in primary food articles' prices was 6.4 per cent in July 2008 as against 41.2 per cent increase in IMF food price index during the same period. This could be attributed to the various supply-side measures undertaken by the Government as well as improved domestic supply prospects. Some of the non-food articles such as oilseeds and raw cotton also witnessed increase in prices during this period largely on account of elevated global prices. Raw cotton prices increased by 24 per cent between March and September 2008 reflecting estimated lower domestic production (down by 14.3 per cent as per the Second Advance Estimates for 2008-09) as well as higher exports on the back of firm international prices.

VI.28 Primary articles inflation, however, eased substantially since January 2009 and

Chart 44: Annual WPI Inflation



reached 3.5 per cent as on March 28, 2009 as prices declined in the case of food articles, especially vegetables and fruits and non-food articles like raw cotton, oilseeds and minerals. While the decline in prices of food articles partly reflected the improved *rabi* crops during 2008-09 as well as seasonal pattern, the decline in non-food primary articles prices was largely driven by decline in international prices of cotton, oilseeds and minerals. Despite some recent easing, rice and pulses prices continue to be at elevated levels.

VI.29 As international crude oil prices shot up during the first half of 2008-09, fuel group inflation, increased to an intra-year peak of 18.0 per cent on August 2, 2008 from 6.8 per cent at end-March 2008. This was driven by increase in the prices of mineral oils reflecting the effect of the hikes in the prices of petrol (Rs.5 per litre), diesel (Rs.3 per litre) and LPG (Rs.50 per cylinder) on June 4, 2008 as well as increase in the prices of freely priced petroleum products.

VI.30 International crude oil prices started to decline since July 2008, and domestic prices of freely priced petroleum products followed the trends in international prices and declined substantially. Among the various freely priced petroleum products, prices declined by about 66 per cent in case of aviation turbine fuel (beginning the first week of September 2008), about 55 per cent in case of naphtha (beginning the first week of August 2008), about 53 per cent in case of furnace oil (beginning mid-August 2008), about 41 per cent in the case of light diesel oil (beginning the first week of December 2008) and about 32 per cent in the case of bitumen (beginning mid-November 2008) as on March 28, 2009. The monthly average Indian basket price for crude oil came down from US $ 132.3 per barrel in July 2008 to US $ 41.2 per barrel in December 2008. Against this backdrop, the Government cut the price of petrol by Rs.5 per litre and diesel by Rs. 2 per litre effective December 6, 2008. As the international crude oil prices continued to remain around US $ 40 per barrel the Government again cut the price of petrol by Rs. 5 per litre, diesel by Rs. 2 per litre and LPG for domestic use by Rs.25 per cylinder effective January 29, 2009. Consequently, the fuel group inflation turned negative (-6.1 per cent) as on March 28, 2009.

VI.31 Manufactured products inflation, year-on-year, increased to a peak of 11.9 per cent in mid-August 2008 from 7.3 per cent at end-March 2008 (Table 68). This was mainly driven by sharp increase in prices of iron and steel, sugar, edible oils/oil cakes, textiles, chemicals, and machinery and machine tools. Since September 2008, manufactured products inflation declined substantially and reached 1.4 per cent as on March 28, 2009.

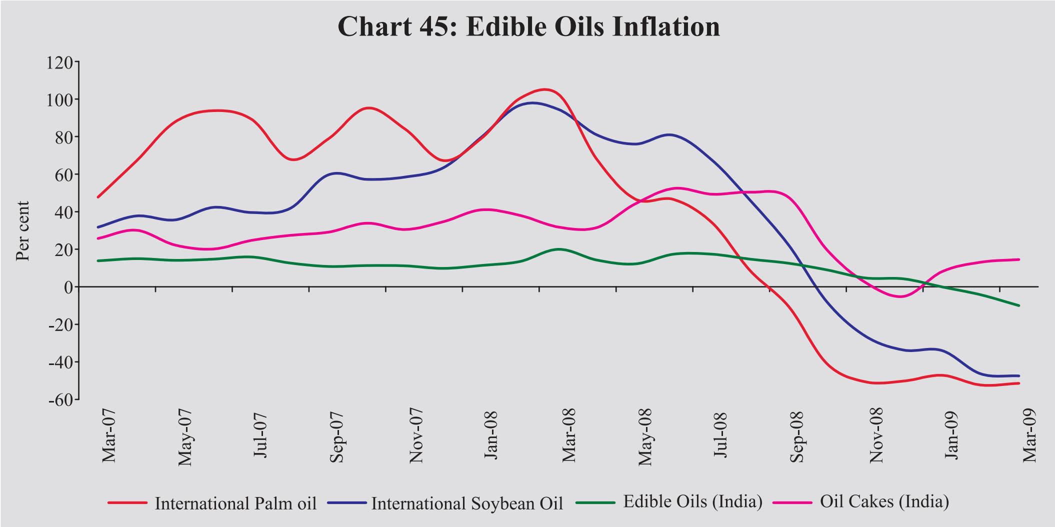
VI.32 The sharp increase in domestic edible oils and oil cake prices up to August 2008 reflected surge in demand, lower domestic *rabi* oilseeds production during 2007-08 as well as sharp increase in international prices. Thereafter, oilseeds and edible oils prices declined reflecting the effect of fiscal measures as well as easing

Table 68: Wholesale Price Inflation in India (year-on-year)

(Per cent)

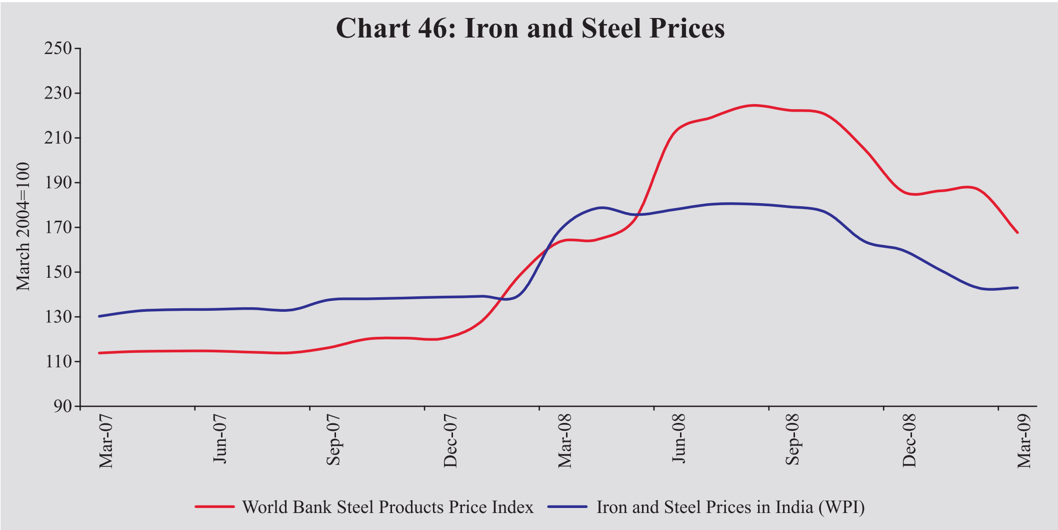
Commodity	Weight	2007-08 (March 29)		2008-09 P (March 28)	
		Inflation	WC	Inflation	WC
1	2	3	4	5	6
All Commodities	**100.0**	**7.7**	**100.0**	**0.3**	**100.0**
1. Primary Articles	**22.0**	**9.7**	**28.2**	**3.5**	**301.0**
Food Articles	15.4	6.5	13.2	6.3	369.7
i. Rice	2.4	9.1	2.5	12.8	104.9
ii. Wheat	1.4	5.1	1.0	5.2	28.1
iii. Pulses	0.6	-1.9	-0.2	8.3	20.7
iv. Vegetables	1.5	14.2	2.3	-4.0	-20.2
v. Fruits	1.5	4.1	1.0	8.1	53.7
vi. Milk	4.4	8.7	4.7	6.1	97.5
vii. Eggs, Fish and Meat	2.2	2.4	0.8	3.1	27.2
Non-Food Articles	6.1	11.4	8.8	-0.1	-2.0
i. Raw Cotton	1.4	14.0	2.0	2.5	11.1
ii. Oilseeds	2.7	20.3	6.7	-2.3	-24.4
iii. Sugarcane	1.3	-0.4	-0.1	0.0	0.0
Minerals	0.5	49.9	6.2	-12.8	-65.4
2. Fuel, Power, Light and Lubricants	**14.2**	**6.8**	**18.9**	**-6.1**	**-495.5**
i. Minerals Oil	7.0	9.3	15.1	-8.7	-422.9
ii. Electricity	5.5	1.5	1.4	-2.6	-66.7
iii. Coal Mining	1.8	9.8	2.5	-1.0	-7.6
3. Manufactured Products	**63.8**	**7.3**	**52.8**	**1.4**	**297.3**
i. Food Products	11.5	9.4	12.4	7.5	294.2
of which: Sugar	3.6	1.1	0.4	17.6	159.8
Edible Oils	2.8	20.0	5.5	-10.2	-91.8
ii. Cotton Textiles	4.2	-6.8	-2.8	16.7	174.9
iii. Man-made Fibres	4.4	2.8	0.7	-2.0	-14.0
iv. Chemicals and Products	11.9	6.0	8.7	1.5	61.6
of which : Fertilisers	3.7	5.1	2.0	5.2	60.3
v. Basic Metals, Alloys and Metal Products	8.3	20.3	25.2	-12.2	-496.3
of which: Iron and Steel	3.6	34.2	20.1	-18.4	-394.0
vi. Non-metallic Mineral Products	2.5	6.4	2.0	1.9	17.2
of which: Cement	1.7	5.1	1.1	2.2	13.8
vi. Machinery and Machine Tools	8.4	3.5	2.9	2.7	64.1
of which: Electrical Machinery	5.0	4.8	2.0	1.2	15.0
viii. Transport Equipment and Parts	4.3	3.9	1.7	3.4	41.5
Memo:					
Food Items (Composite)	**26.9**	**7.7**	**25.6**	**6.8**	**663.9**
WPI Excluding Food	**73.1**	**7.8**	**74.4**	**-2.0**	**-563.9**
WPI Excluding Fuel	**85.8**	**8.0**	**81.1**	**2.0**	**595.5**

WC: Weighted Contribution. P: Provisional.



international prices on the back of projected increase in global production (Chart 45). However, according to the Second Advance Estimates for 2008-09, domestic oilseeds crop is expected to be down by 12.8 per cent. Moreover, the Government has imposed 20 per cent customs duty on import of crude soybean oil to safeguard the interest of domestic producers on November 18, 2008. Reflecting the recent decline in raw cotton prices, cotton textile prices in India also declined since August 2008.

VI.33 Domestic iron and steel prices inflation had reached 36 per cent, y-o-y, by end-August 2008 reflecting sharp increases in global prices. Since then, iron and steel prices have shown a decline and y-o-y change has turned negative (-18.4 per cent as on March 28, 2009) (Chart 46).



This decline in domestic iron and steel prices could be attributed to declining global prices, expected deceleration in demand, both domestic and external, as well as various fiscal measures in the form of reductions in customs duties and imposition of export duties on various steel items announced by the Government since April 2008.

VI.34 Overall, during 2008-09 the movement of WPI inflation was largely driven by fuel group and 'manufactured products' group. Since September 2008, the contribution of fuel group to WPI inflation has been declining sharply and entered negative territory by December 2008, leading to faster decline in overall inflation (Chart 47).

VI.35 As per the latest information available, WPI inflation further declined to 0.2 per cent as on April 4, 2009 from 0.3 per cent at end-March 2009.

Consumer Price Inflation

VI.36 Inflation, based on y-o-y variation in consumer price indices (CPIs), increased since June 2008 mainly due to increase in the prices of food, fuel and services (represented by the 'miscellaneous' group). Various measures of consumer price inflation, though started declining, still remained high in the range of 9.6-10.8 per cent during January/ February 2009 as compared with 7.3-8.8 per cent in June 2008 and 5.2-6.4 per cent in February 2008 (Table 69). The higher level of consumer price inflation as compared to WPI inflation in recent months could be attributed to higher prices of food articles which have higher weight in CPIs.

Asset Prices

VI.37 Domestic equity prices underwent sharp corrections during 2008-09 in

Chart 47: Contribution of Major Groups to WPI Inflation

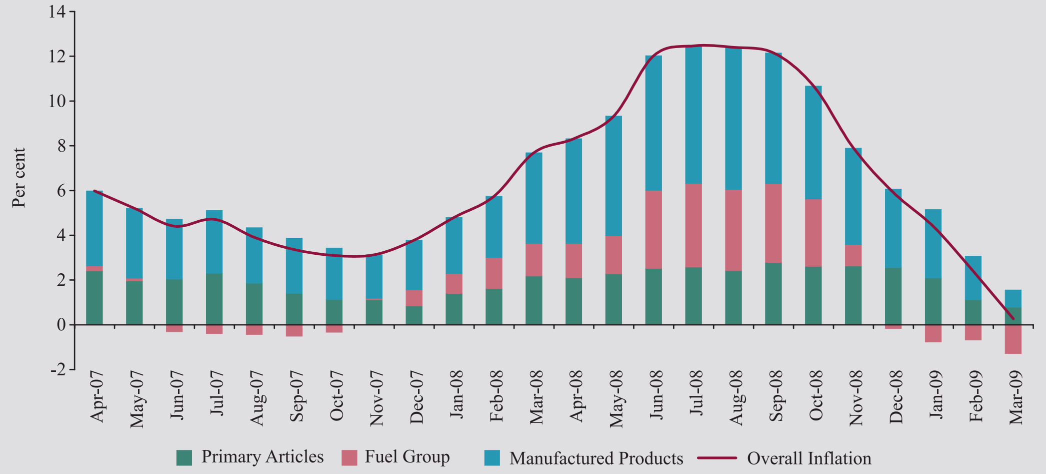


Table 69: Consumer Price Inflation - Major Groups

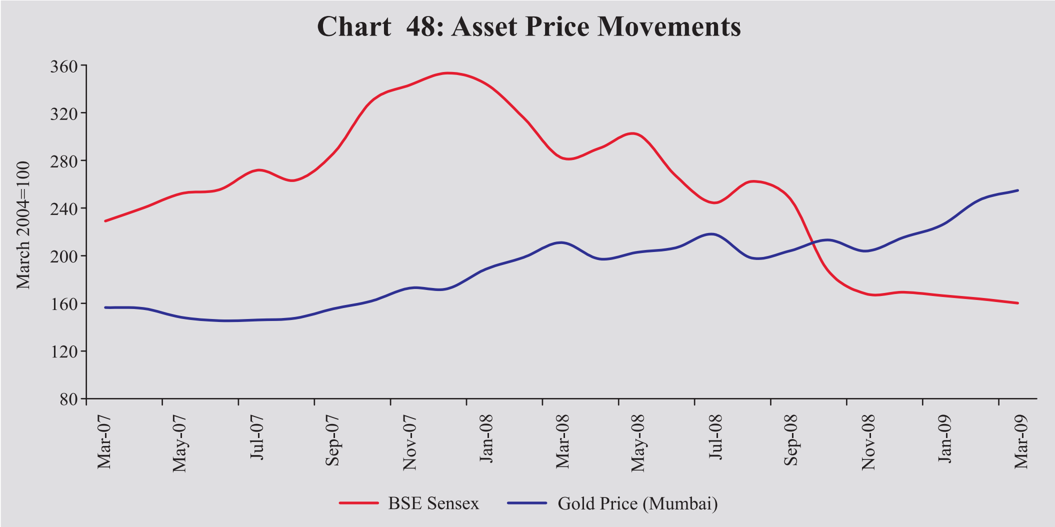
(Year-on-year variation in per cent)

CPI Measure	Weight	Mar-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08	Sep-08	Dec-08	Jan-09	Feb-09
1	2	3	4	5	6	7	8	9	10	11	12	13
CPI-IW (Base: 2001=100)												
General	**100.0**	**4.9**	**6.7**	**5.7**	**6.4**	**5.5**	**7.9**	**7.7**	**9.8**	**9.7**	**10.4**	**9.6**
Food Group	46.2	4.9	12.2	8.1	8.7	6.2	9.3	10.5	13.1	13.1	13.9	–
Pan, Supari *etc.*	2.3	3.1	4.4	9.6	10.3	10.3	10.9	7.1	7.8	8.5	6.8	–
Fuel and Light	6.4	-2.9	3.2	1.6	2.3	2.3	4.6	8.4	9.1	9.7	9.6	–
Housing	15.3	6.6	4.1	4.1	4.0	4.0	4.7	4.7	3.8	3.8	6.0	–
Clothing, Bedding *etc.*	6.6	3.0	3.7	4.4	5.3	3.5	2.6	2.5	2.5	4.2	3.4	–
Miscellaneous	23.3	4.6	3.3	4.0	4.0	4.7	6.3	6.2	7.6	8.3	8.2	–
CPI-UNME (Base: 1984-85=100)												
General	**100.0**	**5.0**	**7.6**	**6.1**	**5.7**	**5.1**	**6.0**	**7.3**	**9.5**	**9.8**	**10.4**	–
Food Group	47.1	5.3	10.9	7.7	7.7	6.2	7.8	9.6	13.2	13.4	14.0	–
Fuel and Light	5.5	1.9	6.4	7.2	7.0	5.4	4.6	5.3	6.2	7.7	8.0	–
Housing	16.4	5.5	5.6	5.6	4.9	4.7	4.0	3.8	3.5	3.5	5.8	–
Clothing, Bedding *etc.*	7.0	2.9	3.6	4.3	4.0	4.1	4.3	3.4	3.1	2.7	2.4	–
Miscellaneous	24.0	5.1	4.4	3.7	3.2	3.8	4.8	6.6	8.4	9.3	9.7	–
CPI-AL (Base: 1986-87=100)												
General	**100.0**	**5.3**	**9.5**	**7.8**	**7.9**	**5.9**	**7.9**	**8.8**	**11.0**	**11.1**	**11.6**	**10.8**
Food Group	69.2	5.5	11.8	8.8	8.8	6.2	8.5	9.6	12.0	11.9	12.7	11.6
Pan, Supari *etc.*	3.8	6.6	5.7	9.1	11.1	11.3	10.4	11.2	12.8	13.7	14.8	14.8
Fuel and Light	8.4	4.3	6.9	7.4	7.2	6.3	8.0	8.9	10.2	11.3	11.7	11.3
Clothing, Bedding *etc.*	7.0	2.2	3.5	2.7	1.9	1.3	1.8	3.1	6.0	7.0	7.0	7.2
Miscellaneous	11.7	5.5	6.8	6.7	5.5	5.2	6.1	6.5	7.1	7.0	6.8	6.5
CPI-RL (Base: 1986-87=100)												
General	**100.0**	**5.3**	**9.2**	**7.5**	**7.6**	**5.6**	**7.6**	**8.7**	**11.0**	**11.1**	**11.4**	**10.8**
Food Group	66.8	5.8	11.5	8.5	8.8	6.2	8.2	9.6	12.0	11.9	13.0	11.6
Pan, Supari *etc.*	3.7	6.3	5.7	9.3	11.6	11.5	10.6	10.9	12.5	13.4	14.8	14.5
Fuel and Light	7.9	4.0	6.9	7.4	7.2	6.3	8.0	8.9	10.5	11.3	11.2	11.0
Clothing, Bedding *etc.*	9.8	2.7	3.1	2.6	2.1	2.6	2.8	4.1	6.5	7.3	7.7	7.7
Miscellaneous	11.9	5.2	6.3	6.2	5.3	5.0	6.2	6.8	7.4	7.5	7.0	6.8
Memo:												
WPI Inflation (End of period)		4.1	5.9	4.4	3.4	3.8	7.7	12.0	12.1	5.9	4.0	2.4
GDP Deflator based Inflation*		4.9	5.5	5.4	3.9	2.7	4.9	8.0	10.6	8.3	–	–

*: Data for March pertain to full year.

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

consonance with trends in major international financial markets, which plunged in the wake of deepening turmoil in international financial markets following the US subprime crisis, and concerns about slowdown in the domestic



economy (see Chapter V). Domestic gold prices, which had eased somewhat during the second quarter of 2008-09 mirroring movements in international prices, hardened subsequently to around Rs.15,255 per 10 grams in March 2009 as international prices recorded further increase (Chart 48). Domestic gold prices, however, eased to Rs.14,205 per 10 grams by April 09, 2009.

VII. MACROECONOMIC OUTLOOK

An assessment of the economic conditions at the current juncture indicates that the global economic conditions deteriorated sharply during 2008 and the forecasts of the various international agencies point to deepening of recessionary conditions during 2009. Reflecting global developments and their impact on the Indian economy, as well as domestic cyclical factors, the various surveys of economic activity point towards prevalence of less than optimistic sentiment for the outlook of the Indian economy in the coming months.

VII.1 Macroeconomic outlook of the Indian economy, based on various business expectations surveys, continues to exhibit the persistence of less than normal sentiments. The professional forecasters' survey conducted by the Reserve Bank in December 2008 suggested further moderation in economic activity in 2008-09. As reported by the respondents, the downside risks to growth seem to have amplified due to projected global economic recession, deterioration in global financial markets and slowdown in domestic demand. The knock-on impact of global downturn is visible as the main drivers of the growth process in the Indian economy have moderated during the third quarter of 2008-09.

Business Expectations Surveys

VII.2 Business Confidence Index (BCI) of the National Council of Applied Economic Research (NCAER) quarterly business expectations survey (67th round) declined sharply from 119.9 in October 2008 to 91.4 in January 2009. Thus, the BCI lost 28.5 points (23.8 per cent) in January 2009 over its October 2008 level. According to the quarterly business expectations survey of the Confederation of Indian Industry (CII), the business confidence index (CII-BCI) for October 2008-March 2009 has also declined both over the preceding six months as well as over the corresponding period of the previous year (Table 70). The decline reflected uncertainties about global economic outlook and concerns about high cost of funds. The Dun and Bradstreet Business Optimism Index for the second quarter of 2009 declined marginally to 93.8, the lowest since its introduction in the fourth quarter of 2002. This followed a sharp decline by 31 per cent during the first quarter of 2009. The index also reported a decline of 39.0 per cent over the corresponding quarter of last year. Except for inventory levels, all the other indices (volume of sales, net profits, new orders, selling prices and employee levels) registered a decline in the second quarter of 2009 over the previous quarter.

VII.3 According to the Reserve Bank's Industrial Outlook Survey of manufacturing companies in the private sector, the business expectations indices based on the

Table 70: Business Expectations Surveys

Organisation	Business Expectations		Growth over a year ago (per cent)	Growth over previous round (per cent)
	Period	Index		
1	2	3	4	5
NCAER	November 2008- January 2009	Business Confidence Index	-40.6	-23.8
CII	October 2008-March 2009	Business Confidence Index	-15.1	-7.7
Dun & Bradstreet	April-June 2009	Business Optimism Index	-39.0	-2.0

assessment for January-March 2009 and expectations for April-June 2009 declined sharply by 20.7 per cent and 13.9 per cent, respectively, over the previous quarters. Similar trend was observed in these indices when compared with the corresponding quarters of the previous year (Chart 49).

VII.4 The optimism for the quarters January-March 2009 and April-June 2009 on major business sentiment indicators such as overall business situation, overall financial situation, production, order books, capacity utilisation, employment, exports, imports and profit margin significantly declined as compared to a year ago. The raw material cost eased substantially during January-March 2009 and significantly higher net proportion of respondents viewed that there would be a 'decline' in selling prices from the respective levels in the previous quarter (Table 71). The industry-wise breakup showed that while the net sentiments on 'overall business situation' for the sample companies were negative for the quarter January-March 2009. The industry groups, *viz.*, food products, pharmaceuticals and cement show positive sentiment with more companies

Chart 49: Reserve Bank's Industrial Outlook Survey- Business Expectation Index

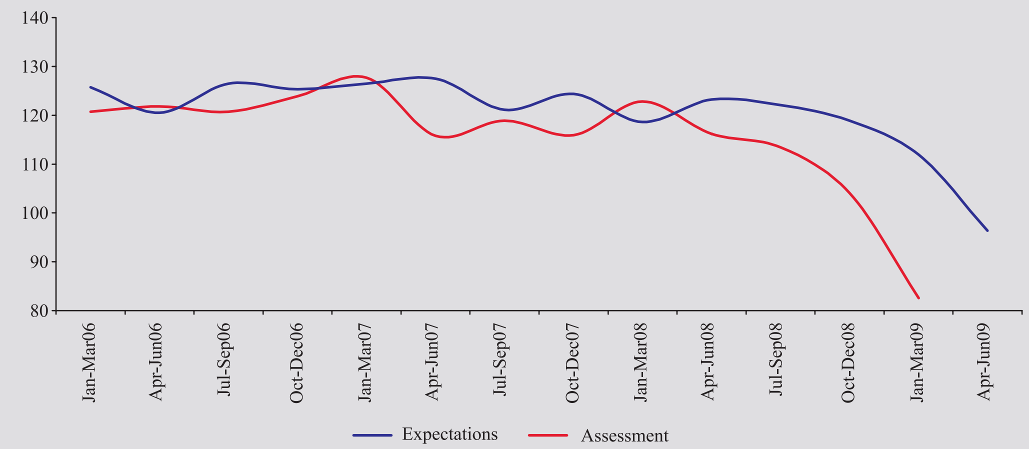


Table 71: Reserve Bank's Survey – Net Response on 'A Quarter Ahead' Expectations About the Industrial Performance

Parameter		Response	Apr-Jun 2008	Jul-Sep 2008	Oct-Dec 2008	Jan-Mar 2009	Apr-Jun 2009
1		2	3	4	5	6	7
1	Overall business situation	Better	46.0 (42.7)	41.8 (42.6)	33.7 (44.1)	21.1 (43.9)	11.2 (47.6)
2	Financial situation	Better	36.6 (51.6)	32.7 (53.0)	27.7 (52.5)	16.4 (53.2)	8.4 (52.7)
3	Working capital finance requirement	Increase	36.6 (56.5)	33.6 (57.3)	33.8 (57.7)	32.9 (57.1)	23.2 (61.0)
4	Availability of finance	Improve	32.3 (58.3)	30.2 (57.9)	23.3 (59.0)	13.7 (56.3)	9.3 (61.7)
5	Production	Increase	45.2 (41.0)	43.5 (36.6)	39.8 (42.1)	26.0 (42.3)	9.9 (44.9)
6	Order books	Increase	41.5 (44.3)	38.5 (43.5)	35.7 (46.1)	20.6 (46.1)	6.4 (44.4)
7	Pending orders, if applicable	Below normal	-4.3 (81.3)	2.2 (80.9)	4.6 (82.0)	11.5 (77.8)	23.2 (59.4)
8	Cost of raw material	Decrease	-48.2 (46.0)	-54.7 (39.1)	-61.1 (32.3)	-35.7 (39.7)	-16.2 (33.7)
9	Inventory of raw material	Below average	-7.0 (83.2)	-3.8 (81.8)	-7.6 (77.6)	-3.3 (81.3)	1.1 (80.2)
10	Inventory of finished goods	Below average	-5.8 (84.5)	-1.5 (84.5)	-4.3 (82.6)	-4.4 (80.9)	-4.4 (78.4)
11	Capacity utilisation (Main product)	Increase	25.6 (59.9)	22.2 (58.8)	26.4 (56.0)	12.3 (59.1)	-0.7 (55.0)
12	Level of capacity utilisation (Compared to the average in the preceding four quarters)	Above normal	9.4 (77.0)	3.6 (74.9)	-0.5 (78.7)	-7.4 (73.7)	-20.8 (66.4)
13	Assessment of the production capacity (With regard to expected demand in the next six months)	More than adequate	8.0 (81.2)	4.6 (81.3)	5.7 (81.7)	11.8 (81.0)	8.9 (70.7)
14	Employment in the company	Increase	20.8 (68.2)	15.8 (71.5)	16.6 (70.4)	7.7 (75.7)	-5.1 (74.0)
15	Exports, if applicable	Increase	27.7 (53.3)	27.7 (54.9)	27.3 (54.3)	16.0 (54.8)	-3.8 (57.3)
16	Imports, if any	Increase	25.3 (65.6)	21.3 (66.5)	21.4 (67.9)	9.1 (69.7)	-1.4 (68.8)
17	Selling prices are expected to	Increase	19.1 (66.0)	21.0 (61.5)	26.2 (57.6)	4.1 (61.7)	-9.1 (61.9)
18	If increase expected in selling prices	Increase at lower rate	9.0 (64.0)	3.0 (61.3)	0.6 (54.7)	0.9 (54.0)	25.9 (53.5)
19	Profit margin	Increase	7.2 (61.0)	3.8 (59.8)	-3.6 (54.7)	-12.9 (53.3)	-18.6 (50.6)

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.

expecting growth than those expecting contraction. For April-June 2009, the overall net sentiment for all industries except textiles is positive. The size-wise breakup shows that the contraction in the quarter January-March 2009 in ‘overall business situation’ is across the board. Moderate growth is expected across the various companies for the quarter April-June 2009. The expectations are less optimistic for smaller companies as compared to their bigger counterparts.

VII.5 The ABN-AMRO Purchasing Managers’ Index (PMI) for March 2009 was at 49.5, just below the neutral 50.0 mark, pointing to a weakening in the health of the Indian manufacturing industry, although the index indicated fractional improvement for the third straight month. Despite some gain in output index since January 2009, manufacturers continued to report decline in new orders from domestic and foreign clients due to global financial and economic conditions. The New Orders Index, a leading indicator of the activity for the next month at 49.5, is marginally lower than the neutral mark but improved significantly from a low of 45.9 in February 2009. Export orders further declined to 43.6 during the same month. Such a decline signals the possibility of further weakening of activity in the manufacturing sector. Low production and stock depletion strategies have led to declines in both pre and post-production stocks. These trends have mainly reflected in the deteriorating outlook for the manufacturing sector.

Survey of Professional Forecasters[1]

VII.6 The results of professional forecasters' survey conducted by the Reserve Bank in March 2009 suggested moderation in economic activity for 2008-09 on the whole (Table 72). Between the sixth round of survey conducted in December 2008 and seventh round survey in March 2009, median forecast of real GDP growth for 2008-09 was revised downwards to 6.6 per cent from 6.8 per cent. The sectoral growth rate forecast for the agriculture sector was revised downwards from 3 per cent to 1.6 per cent and for industry, from 4.9 per cent to 4.1 per cent. However, the sectoral growth rate forecast for services was revised upwards from 9.0 per cent in the last survey to 9.3 per cent in the current survey. According to this survey the median forecast of real

[1] Introduced by the Reserve Bank from the quarter ended September 2007. The forecasts made in the section are that of professional forecasters and not that of the Reserve Bank.

Table 72: Median Forecasts of Select Macroeconomic Indicators by Professional Forecasters: 2008-09 and 2009-10

		Actual 2007-08	Annual forecasts				Quarterly forecasts (2009-10)							
			2008-09		2009-10		Q1		Q2		Q3		Q4	
			E	L	E	L	E	L	E	L	E	L	E	L
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1	Real GDP growth rate at factor cost (in per cent)	9.0	6.8	6.6	6.0	5.7	6.1	5.3	6.3	5.6	6.8	6.2	–	6.5
	a. Agriculture & Allied Activities	4.9	3.0	1.6	3.0	3.0	3.0	3.0	3.0	2.5	3.0	3.0	–	3.0
	b. Industry	7.4	4.9	4.1	5.0	4.1	4.0	2.1	4.5	3.0	5.6	5.3	–	5.9
	c. Services	10.8	9.0	9.3	7.5	7.5	7.6	7.3	8.1	7.4	8.3	7.5	–	8.2
2	Gross Domestic Saving (per cent of GDP at current market price)	37.7	33.0	35.3	33.3	34.6	–	–	–	–	–	–	–	–
3	Gross Domestic Capital Formation (per cent of GDP at current market price)	39.1	34.9	37.5	34.0	35.4	34.0	36.2	34.3	34.5	35.3	34.1	–	33.8
4	Corporate profit after tax (growth rate in per cent)*	26.2	15.0	13.5	12.0	9.0	10.0	-2.5	12.5	2.0	12.5	16.5	–	12.5
5	Inflation WPI	4.7	8.3 #	8.3 #	–	–	2.4	-1.4	0.1	-2.5	3.0	1.6	–	4.8
6	Exchange Rate (US$/INR end period)	39.9	50.9 #	50.9 #	–	–	47.6	50.0	46.5	49.0	45.5	48.0	–	47.0
7	T-Bill 91 days Yield (per cent-end period)	7.1	5.0 #	5.0 #	5.5	5.0	–	–	–	–	–	–	–	–
8	10-year Govt. Securities Yield (per cent-end period)	7.9	7.0 #	7.0 #	6.0	6.5	–	–	–	–	–	–	–	–
9	Export (growth rate in per cent)	28.9	12.0	7.8	10.2	-4.0	–	–	–	–	–	–	–	–
10	Import (Growth rate in per cent)	35.4	17.7	17.2	-4.0	-8.4	–	–	–	–	–	–	–	–
11	Trade Balance (US $ billion)	–	–	–	–	–	-33.3	-25.0	-35.5	-27.0	-31.8	-27.1	–	-28.0

E : Earlier Projection. L : Latest Projection.

– : Not Available. # : Actuals. * : BSE listed companies.

Note : The latest round refers to seventh round for the quarter ended March 2009, while earlier round refers to sixth round for the quarter ended December 2008.

Source : Survey of Professional Forecasters, Fourth Quarter 2008-09.

GDP growth for 2009-10 has also been revised downwards to 5.7 per cent from 6.0 per cent.

VII.7 Forecasts by select agencies for real GDP growth in 2009-10 are set out in Table 73.

Table 73: Projections of Real GDP for India by Various Agencies – 2009-10

(Per cent)

Agency	Latest Projection				Month of Projection
	Overall Growth	Agriculture	Industry	Services	
1	**2**	3	4	5	6
ADB*	**5.0**	–	–	–	Mar-09
ASSOCHAM	**6.5**	–	–	–	Dec-08
JP Morgan	**6.2**	–	–	–	Nov-08
CRISIL	**6.1**	3.0	4.5	7.7	Feb-09
EAC to PM	**7.0-7.5**	–	–	–	Jan-09
Merrill Lynch	**5.3**	2.7	3.3	6.7	Mar-09
Citigroup	**5.5**	–	–	–	Mar-09
CMIE	**6.6**	–	–	–	Apr-09
NCAER	**6.9**	2.7	6.6	8.4	Jan-09
OECD	**4.3**	–	–	–	Mar-09
UNCTAD*	**7.0**	–	–	–	Jan-09
IMF	**5.25**	–	–	–	Mar-09
World Bank	**4.0**	–	–	–	Mar-09
ICRIER	**4.8-5.5**	–	–	–	Mar-09
Range	**4.0-7.5**	**2.7-3.0**	**3.3-6.6**	**6.7-8.4**	

* : Calendar year.