



**RESERVE BANK OF INDIA**

[www.rbi.org.in](http://www.rbi.org.in)

[www.rbi.org.in/hindi](http://www.rbi.org.in/hindi)

e-mail: [helpprd@rbi.org.in](mailto:helpprd@rbi.org.in)

**PRESS RELATIONS DIVISION**, Central Office, Post Box 406, Mumbai 400001  
Phone: 2266 0502 Fax: 2266 0358, 2270 3279

October 29, 2007

## **Macroeconomic and Monetary Developments: Mid-Term Review 2007-08**

The Reserve Bank of India today released the document “Macroeconomic and Monetary Developments: Mid-Term Review 2007-08” to serve as a backdrop to the Mid-Term Review of the Annual Policy Statement for 2007-08 being announced on October 30, 2007.

The highlights of macroeconomic and monetary developments during 2007-08 so far are:

### **The Real Economy**

- The Indian economy continued to maintain strong growth momentum during the first quarter of 2007-08, underpinned by sustained performances of the manufacturing and services sectors. According to the estimates released by the Central Statistical Organisation (CSO) in August 2007, real GDP growth was 9.3 per cent during the first quarter of 2007-08 as compared with 9.6 per cent during the same period in 2006-07.
- The cumulative rainfall during the South-West monsoon season 2007 (June to September) was 5 per cent above normal as compared with one per cent below normal during the corresponding period of the previous year. The area coverage of *kharif* crops has increased during 2007-08 (as on October 12, 2007) with reported sown area of 104.7 per cent of the normal, which was about 3.1 per cent higher than the previous year.
- During April-August 2007, the index of industrial production rose by 9.8 per cent as compared with a growth of 11.0 per cent recorded during the corresponding period of the previous year. The manufacturing sector registered a growth of 10.3 per cent during April-August 2007 on top of 12.2 per cent during April-August 2006.
- During April-August 2007, the infrastructure sector recorded a growth of 6.6 per cent as compared with 8.3 per cent a year ago, with five of the six core infrastructure industries registering a deceleration. The electricity sector was the only sector which recorded a higher growth than a year ago.
- The services sector continued to record double-digit growth (10.6 per cent) in April-June 2007. Leading indicators of service sector activity for April-August 2007 show that cargo handled at major ports and import cargo handled by civil aviation witnessed strong growth. Growth rates in commercial vehicle production, new cell phone connections, passengers handled by civil aviation and steel moderated during 2007-08 (April-August), *albeit* over a high base.

## **Fiscal situation**

- Available information on Central Government finances for 2007-08 (April-August) indicates that gross fiscal deficit (as proportion of the budget estimates) was placed higher than a year ago. Revenue deficit (adjusted for profit on sale of Reserve Bank's stake in SBI) was 122.9 per cent of the full year budget estimates. Tax revenue remained buoyant, rising by 22.0 per cent over that during April-August 2006. Non-tax revenue (net of profit on sale of Reserve Bank's stake in SBI) registered a growth of 21.2 per cent during the same period. Aggregate expenditure (adjusted for acquisition cost of Reserve Bank's stake in SBI) increased mainly on account of sharp increase in revenue expenditure and plan capital expenditure.
- Gross and net market borrowings (including 364-day Treasury Bills) of the Central Government during 2007-08 (up to October 22, 2007) were Rs.1,26,036 crore and Rs.75,363 crore, respectively, accounting for 66.7 per cent and 68.7 per cent of the estimated borrowings for the year.
- During 2007-08 (up to October 22, 2007), the States raised market loans amounting to Rs.20,362 crore (50.1 per cent of gross allocation) through auctions.

## **Price Situation**

- Headline inflation generally edged up in major economies during the quarter ended September 2007 as compared with the previous quarter. Many central banks further tightened monetary policy during the second quarter of 2007-08 against the backdrop of persistent inflationary pressures represented by core inflation, especially in view of continued strength of demand, ample liquidity and possible pass-through from past and present increases in oil and other commodity prices.
- Global commodity prices remained firm during the second quarter of 2007-08 led by food and crude oil prices, although there was some moderation in prices of metals during the quarter. International crude (WTI) prices crossed US \$ 80 a barrel by mid-September 2007 and reached a historical peak on October 18, 2007 at US \$ 89.5 a barrel, partly due to heightened geopolitical tensions in West Asia and the weakening of the US dollar. Food prices increased further led by wheat and oilseeds/edible oils, reflecting a shortfall in global production, decline in stocks and rising demand for non-food uses.
- In India, inflation based on the wholesale price index (WPI) eased from 4.4 per cent at end-June 2007 to 3.1 per cent by October 13, 2007, partly due to base effects and negative contribution from fuel prices.
- Consumer price inflation, however, remained firm during the second quarter of 2007-08 and continued to be above the WPI inflation, mainly reflecting the impact of higher food prices. Various measures of consumer price inflation were placed in the range of 5.7-7.9 per cent during August/September 2007 as compared with 5.7-7.8 per cent in June 2007 (and 6.7-9.5 per cent in March 2007).

- Fuel group inflation turned negative beginning the week ended June 9, 2007 and remained so (-1.6 per cent) on October 13, 2007, easing from 5.0 per cent a year ago, reflecting the cuts in domestic prices of petrol, diesel and other fuel products in November 2006 and February 2007. Primary articles' inflation eased to 5.2 per cent on October 13, 2007 from 9.3 per cent at end-June 2007 and 8.1 per cent a year ago. Manufactured products inflation eased to 4.1 per cent on October 13, 2007 from 4.9 per cent at end-June 2007 and 4.6 per cent a year ago.
- Pre-emptive monetary measures since mid-2004 accompanied by fiscal and supply-side measures have helped in containing inflation.

### **Monetary and Liquidity Conditions**

- Growth in broad money ( $M_3$ ), year-on-year (y-o-y), was 21.8 per cent (Rs. 6,41,464 crore) on October 12, 2007 as compared with 18.9 per cent (Rs. 4,66,603 crore) a year ago.
- Aggregate deposits of banks, y-o-y, increased by 23.4 per cent (Rs.5,83,198 crore) on October 12, 2007 as compared with 19.2 per cent (Rs. 4,01,717 crore) a year ago.
- Growth in bank credit moderated after the strong pace in the preceding three years. Non-food credit by scheduled commercial banks (SCBs) moderated to 23.5 per cent (Rs.3,77,759 crore), y-o-y, as on October 12, 2007 from 30.0 per cent (Rs.3,70,226 crore) a year ago.
- Reserve money expanded by 24.4 per cent (14.9 per cent adjusted for the first round impact of the increase in the cash reserve ratio), y-o-y, as on October 19, 2007 as compared with 20.2 per cent a year ago.
- Liquidity conditions continued to be influenced by movements in capital flows and cash balances of the Governments. The Reserve Bank modulated market liquidity with the help of issuances of securities under the Market Stabilisation Scheme (MSS), operations under Liquidity Adjustment Facility (LAF) and increase in the cash reserve ratio (CRR).

### **Financial Markets**

- During the second quarter of 2007-08, international financial markets turned volatile as uncertainties about the size and distribution of losses from the US sub-prime mortgage market made investors to adjust their positions. Emerging market economies have generally been less affected by developments in the advanced economies.
- Indian financial markets remained orderly for the most part of the second quarter of 2007-08.

- The call money rate, which had remained below the reverse repo rate during June-July 2007 on the back of the easing of liquidity conditions and ceiling on absorption through reverse repo operations under the liquidity adjustment facility (LAF) till August 3, 2007, reverted to the corridor set by the reverse repo and repo rates in August-September 2007. Interest rates in the collateralised segment of the overnight money market also hardened but remained below the call rate during the quarter.
- In the foreign exchange market, the Indian rupee generally appreciated *vis-a-vis* all major currencies (US dollar, Euro, Pound sterling and Japanese yen) during the quarter.
- Yields in the Government securities market softened.
- Banks' deposit and lending rates softened during the second quarter particularly at the upper end of the range of various maturities.

### **The External Economy**

- India's balance of payments position has remained comfortable during 2007-08 so far. The merchandise trade deficit, on balance of payments basis, increased from US\$ 16.9 billion in April-June 2006 to US\$ 21.6 billion in April-June 2007. Net surplus on the invisibles account exhibited buoyancy during the first quarter of 2007-08, led by exports of software, business services and private remittances, and continued to finance a large part (78.2 per cent) of the merchandise trade deficit.
- Despite large merchandise trade deficit, higher net invisible surplus contained the current account deficit (US\$ 4.7 billion) during the first quarter of 2007-08 at broadly the same level (US\$ 4.6 billion) as in the first quarter of 2006-07. The current account deficit was financed by capital flows which have remained large during 2007-08 so far.
- During 2007-08 (up to October 19, 2007), net inflows by FIIs amounted to US \$21.2 billion as compared with outflows of US \$ 933 million in the corresponding period of 2006-07. FDI inflows were US \$ 6.6 billion during April-July 2007 (US \$ 3.7 billion a year ago). On the other hand, non-resident Indian deposits registered net outflows amounting to US \$ 148 million during April-July 2007 as against net inflows of US \$ 1.6 billion during April-July 2006.
- During 2007-08 so far (April-August), growth of merchandise exports moderated, while imports posted a high growth rate. Non-oil imports registered high growth due to robust growth in capital goods. Oil imports registered a sharp deceleration from the strong growth recorded during the corresponding period of the previous year.
- India's foreign exchange reserves were US \$ 261.1 billion as on October 19, 2007, showing an increase of US \$ 62.0 billion over end-March 2007 level.

**Alpana Killawala**  
Chief General Manager