MONTHLY MONITOR

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Highlights

Industrial growth cools down

The annual growth of Index of Industrial Production for the month of September has come out at 4.4 percent versus 5.6 percent in August 2010, and is largely explained by the 4.2 percent decline in capital goods sector. **The capital goods increased at a whopping 63 percent in July 2010. The industrial activity is cooling down after many months of high growth. The recovery has also become more broad-based with 14 out of 17 industry groups recording positive growth in August and September of 2010 as well as during the whole of 2009-10.**

WPI inflation decreases marginally

The year on year WPI inflation was 8.58 percent for the month of October, 2010 as compared to 8.62 percent for September and 8.51 percent for August 2010 **mainly due to increase in prices of food articles. The rapid growth of IIP, the slow growth of agriculture and the low base effect explains this high inflation for the last many months.**

Consumer Price inflation declined marginally

The annual growth in all India Consumer Price Index Number for Industrial Workers came down marginally to 9.70 percent in October, 2010 from 9.82 percent for September, 2010.

Rupee depreciated marginally

The continuous flow of FIIs into Indian stock market and the strong growth of Indian economy in recent months have assisted in strengthening the Indian rupee. However, the exchange rate depreciated marginally to 44.94 per dollar in November 2010. It is forecasted to depreciate to about 45.5 for the next three months on the uncertainties in global markets.

FII flows are US$ 4784.75million

The foreign institutional investments (FIIs) in Indian market were around US$ 4784 million in November 2010. The FIIs were US$ 5468 million in October, US$ 4262.60 million in September, US$ 3082.75 million in August, US$ 5285.33 million in July and US$2433.99 million in June 2010. **These impressive figures clearly show the foreign investors' confidence about India's long term growth prospects. The expected medium term appreciation of rupee and the prospects of returns increasing further are forming a virtuoso cycle. The recent decision of the Federal**

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Exports maintains its growth momentum while imports slows down	**reserve to buy $600 billion in government bonds will also stimulate the flows to India.** **India's exports after growing at a very high pace in past few months are slowing down, though it grew at a healthy 21.3 percent in October 2010, mainly due to the newer market of Latin America and Africa. The wearing out of the base effects is also contributing to this slow down. The imports expanded at a low rate of 6.8 percent in dollar terms in October 2010 largely due to the base effect.** The trade deficit in October 2010 US$ 9.7 billion from US$ 11.1 billion in a year ago. The relatively lower deficit is due to slower growth of imports.

IEG FORECAST

Variables	Latest Information available	Forecast for next three months
Inflation rate (WPI)	8.58% in October 2010	8.26%, 7.96%, 7.73%
Inflation rate (CPI)	9.70% in October 2010	9.56%, 9.32%, 9.10%
Growth rate of IIP	4.4% in September 2010	6.99%, 7.89%, 9.01%
Growth rate of M3	16.2% on November 19, 2010.	16.22%,16.29%,16.39%
Re/$ exchange rate	. 44.94 in November,2010	45.10, 45.32, 45.59
Forex reserves	US$ 293.98 billion on November 26, 2010	$297.84, $300.58, $295.79
FII inflows (Net)	US$4784.75 million in November, 2010	Inflows for the next three months to be positive
Growth rate of exports	21.3% for October 2010	19.73%,18.43%,17.37%
Growth rate of imports	6.8% for October 2010	14.66%,12.70%, 14.11%

WPI inflation decreased marginally

CPI declined marginally

Inflation

The year on year WPI inflation was 8.58 percent for the month of October, 2010 as compared to 8.62 percent for September and 8.51 percent for August 2010, based on the new series. The new WPI index tracks 676 commodities in contrast to the old index which was based on 435 commodities. The rapid growth of GDP, the slow growth of agriculture and the low base effect explains this high inflation for the last many months.

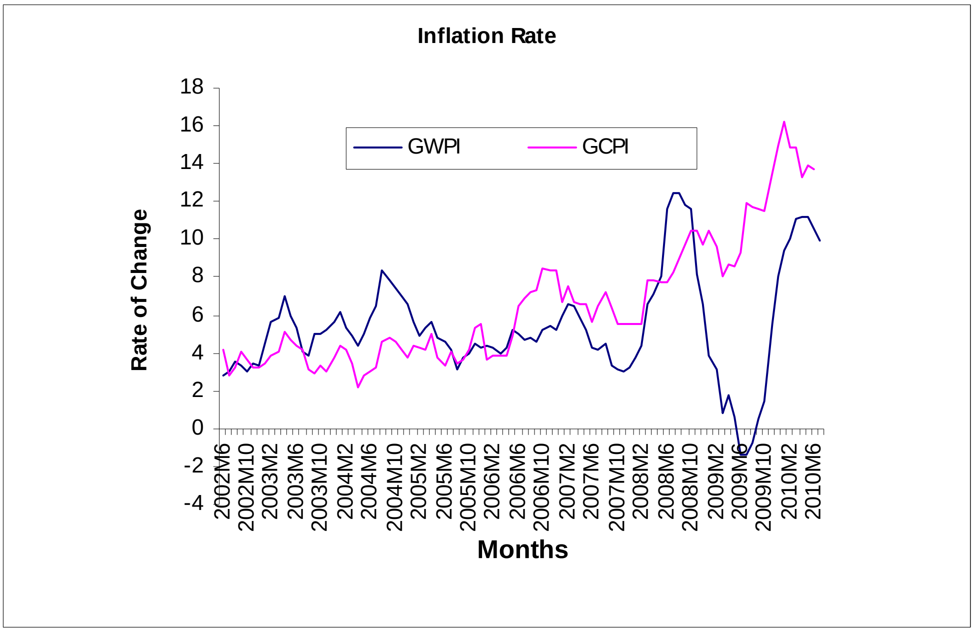
The primary articles index with a weight of 20.12 percent was up by 0.8 percent in October 2010 over the previous month while the index for fuel, power, light and lubricants with a weight 14.91 percent was up by 0.3 percent, and the index for the major sector, the manufacturing products with a weight of 64.97 percent increased also by 0.3 percent.

The marginal increase in inflation indicates a cooling down of inflationary expectations. Except for the East and the North-East, the rainfall has already been adequate and there is already a perceptible shift towards high value crops which may bring down the inflationary expectations in Food sector further. However, the withering of the base effect, the continuing monetary tightening of RBI though at a slower pace and the medium term rising trend of rupee will put a downward pressure on inflation. On balance, the inflation is likely to cool down in the next three months.

The annual growth in all India Consumer Price Index Number for Industrial Workers came down marginally to 9.70 percent in October, 2010 from 9.82 percent for September, 2010. It was 9.88 percent in August 2010, 11.25 percent in July, 13.73 percent in June, 13.91 percent in May and 13.33 percent in April 2010. In March, 2010 it remained at 14.86 percent which was same as the growth in February, 2010. The gap between inflation rates as measured by the wholesale price index and as measured by consumer price index is explained by the higher weightage given to primary products and food items in CPI, whereas WPI covers a wider range of the outputs of various commodities. It is forecasted that the growth rates in CPI, following the trend, will come down further the next three months.

Forecast:

The WPI inflation forecasts are8.26 %,7.96 %, and7.73 % for November, December 2010 and January 2011 respectively. The CPI inflation forecasts are 9.56%,9.32% and 9.10% for November, December 2010and January 2011 respectively.



Industrial Production

Industrial growth cools down further

The annual growth of Index of Industrial Production for the month of September has come out at 4.4 percent versus 5.6 percent in August 2010, and is largely explained by the 4.2 percent decline in capital goods sector. The IIP grew at 13.8 percent in July, 7.1 percent in June, at 11.6 percent in May, 17.6 percent in April and at 13.5 percent in March 2010. The 7.1 per cent growth in IIP in June came after the eighth straight double-digit monthly expansion, driven largely by robust manufacturing output. The index recorded high growths of 17.6 per cent in December 2009, 16.7 per cent in January 2010 and 15.1 percent in February 2010.

The uptrend in the industrial activity is getting consolidated. The cumulative growth for the period April-September 2010-11 is 10.2 percent over the same period in 2009. The recovery has also become more broad-based with 14 out of 17 industry groups recording positive growth during the year 2009-10. During September 2010 also, out of 17 groups, 14 groups showed positive growth. The revival in demand supported by the low base for the year 2009 is able to deliver this continuous positive growth. However, the pace of growth is seen to be tapering off as the low-base effect wears off and the impact of rate hikes and withdrawal of stimulus picks up. The global recovery is also expected to be week. The IIP growth is likely to hover around 7 to 9 percent in next three months due to the base effect and the tightening of monetary policy by the RBI, even though the good monsoon may put a break on inflationary expectations.

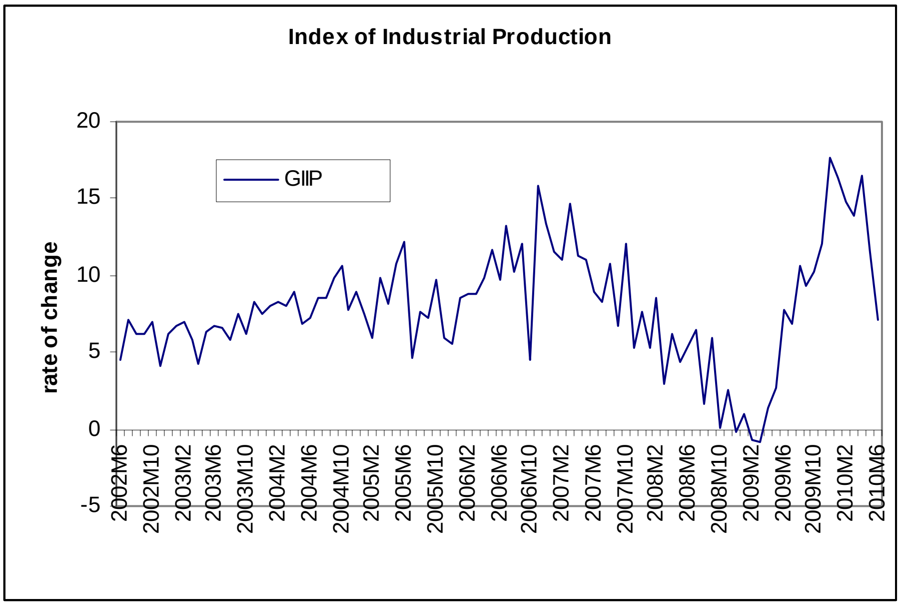
The slow IIP growth at 4.4 percent

The Mining, Manufacturing and Electricity sectors for the month of June 2010 grew at 5.2 percent, 4.5 percent and 1.7 percent, respectively, as compared to the same month in the previous year. Industry groups like 'Leather and Leather & Fur Products', 'Transport Equipment and Parts' and 'Rubber, Plastic, Petroleum and Coal Products' have grown at 26.8, 21.6 and 13.7 percents and have helped the IIP to maintain its positive trend. The mining sector may slow down in the in short run as environmental and tribal rights issues may take time to resolve. Similarly, land acquisition issues also affect the industry sector as whole. Even though the domestic demand remains strong, the uncertainty associated with the global demand may act as a constraint for the growth in Manufacturing sector.

The annual growth rates in Basic goods and in Intermediate goods are 3.5 percent and 10.3 percent, where as Capital goods declined by 4.2 percent in August 2010. The negative Capital goods growth is not good sign for sustaining the over all growth rate in the economy. The Consumer goods grew at 5.2 percent in August 2010 while the Consumer durables grew at 10.9 percent and Consumer non-durables declined at 2.5 percent.

Forecast:

Based on the available information we forecast the IIP growth rate for the next three months to be 6.99%,7.89% and 9.01% for October November and December2010



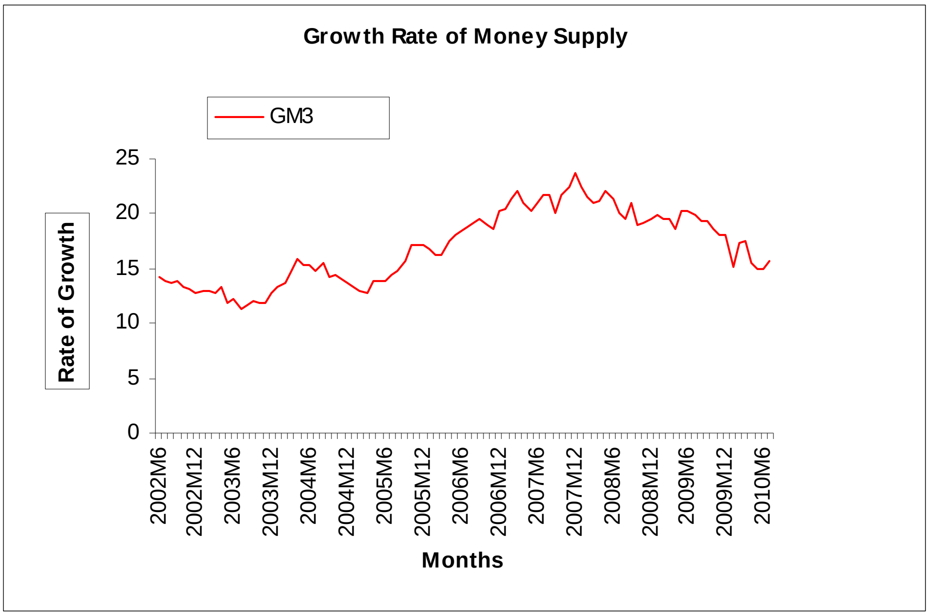
Money and Credit

Money supply at 16.2 percent

As on November 19, 2010, Money supply grew at 16.2 percent as against 19.2 percent in the previous year. In 2010, it grew at 15.8 percent in October 8, 15.6 percent in September 10 as against 14.5 percent June18, in the same year. Though the monetary tightening of RBI has reduced the liquidity in the system, the picking up of credit off take has helped the money supply to increase. The expansion in money supply is mainly contributed by the net credit to the Government at 20.4 percent. The growth rate is marginally higher for credit to commercial sector and change in net foreign exchange assets at about 21.5 percent each. Though the huge fees, the central government has received from the 3 G and broadband auctions have slowed down the borrowing program of the government this fiscal, the expected increase in social sector schemes may put pressure on the deficits. The bankers are predicting that the credit off take is likely to pick up in the second half of this financial year. The FIIs have started pouring in money to India reaffirming their faith into its growth prospects. The government has increased the FII limits recently. The money supply is forecasted to grow at about 16 percent for the next three months.

Forecast:

The forecast for the growth rate of money supply (M3) is16.22 %,16.29 % and 16.39 % for December2010, January and February 2011



Interest rates

As the positive signs of the revival of the economy is sustaining itself, the RBI is slowly withdrawing from its low policy rates regime and the trend is going to continue, even though at a slower pace, given the inflationary pressure in the economy. The RBI has already raised its repo rate by 150 basic points since March 2010 to 6.25 percent. The reverse repo rate is now 5.25 percent. The rise in prices, though has started cooling down, has already spilled over from supply to demand side. The inflation rates (WPI) has started coming down from the double digits, however, the inflationary expectations continues to be high even though the growth in food prices are likely to decline. The growth momentum in the economy backed by domestic demand is putting pressure on prices. The prime lending rates are also seeing upward revision both due to the monetary tightening and the uncertainty in the global scenario. In the medium term, increases in prices and GDP will increase the demand for money while monetary tightening by RBI will reduce the supply putting further pressure on the market interest rates. The corporates may increase their borrowings from outside the country as interest rates are low there, which may have a softening effect on the interest rates. Though, thus the complexities of macro economic management are likely to increase as the global recovery is expected to slow down, the RBI needs to maintain a fine balance so as to put pressure on inflation without disturbing the growth path. On balance, we would like to believe that the market interest rates may increase further.

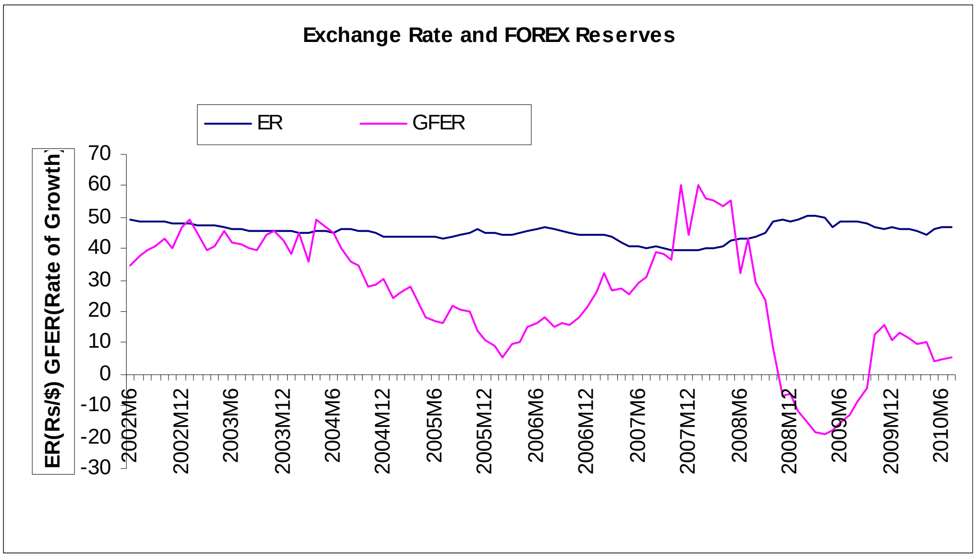
Exchange rate

The continuous flow of FIIs into Indian stock market and the strong growth of Indian economy in recent months have assisted in strengthening the Indian rupee. The rupee hit a five month high on the 4th October 2010 at 44.24 rupees per dollar. Rupee appreciated 12.9 percent during the year 2009-10 as against a depreciation of 25.5 percent in the previous year. This appreciation was mainly due to economic recovery. Foreign institutional investors have been returning to Indian stock exchanges due to the foreign investors' confidence about India's long term growth prospects. However, the expected widening of trade deficit may put pressure on rupee. The rupee was 46.55 per dollar in August, 46.85 in July and 46.56 in June 2010. The rupee has depreciated to these levels with respect to the previous couple of months, though it appreciated in comparison with the June 2009 figure of 47.67, mainly due to the drying of flows to the Indian stock market due to the Euro zone crisis. The exchange rate was 44.94 in November and 44.45 in October 2010. It is forecasted to be about 45.5 for the next three months due to the uncertainties prevailing in the Euro Zone.

Rupee depreciated marginally

Forecast:

In coming months, exchange rate is expected to be around Rs/$45.10 , Rs/$45.32 and Rs/$45.59 for December 2010 , January and February 2011



Foreign Exchange Reserves

Foreign exchange reserves stood at US$ 297.99 billion on November 19, 2010. It went up progressively from US$ 273.72 billion in May 28, 2010 to US$ 295.44 billion on October 22, 2010. This is a substantial progress from a few months back when reserves reached below 250 billion mark, though it is away from the peak of 314.61 billion of May 2008. The rise in reserves is mainly due to inflow of foreign investment into Indian market. The rise in stock market indices attracting huge FII inflows. The high interest rate differentials between India and the rest of the world as well as the rising rupee, which is also likely to continue for sometime, must have helped in this increase. More money is expected from abroad as government has recently increased the FII limit in debt market from US$20 billion to US$30 billion and the previous cap of $5 billion has already been breached on government securities. However, if the world economy grows at the predicted rate, the high oil import prices could restrain the accumulation of reserves. The likely outflow of Indian FDI to other countries could also restrain the accumulation. On balance, we forecast higher reserves for the next three months.

Foreign Exchange Reserves at healthy US$ 293.98 billion

Forecast:

Forex reserves expected to be $297.84 billions, $300.58billions and $ 295.79billions in December 2010, January and February 2011

Foreign Institutional Investment

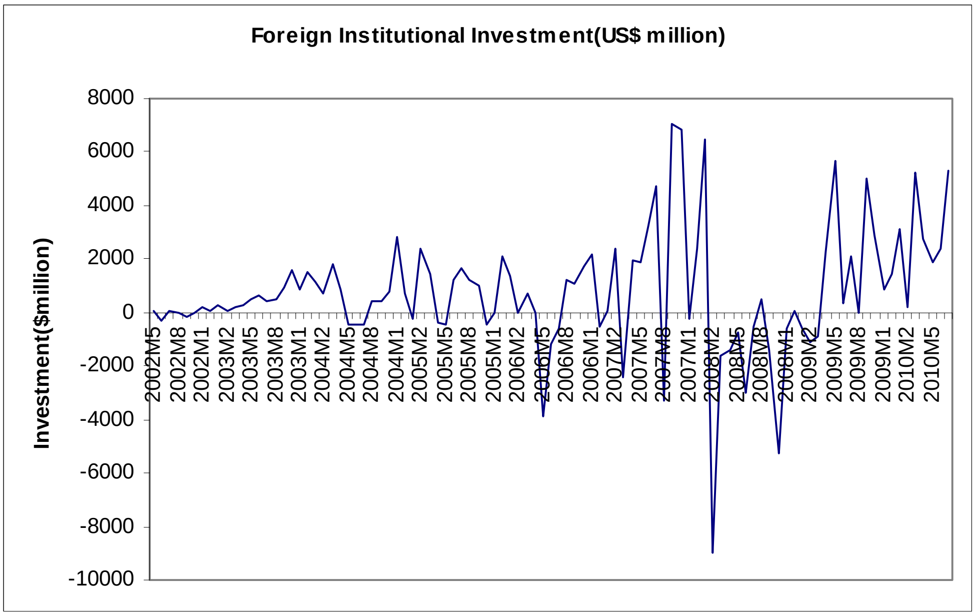
The foreign institutional investments (FIIs) in Indian market were around US$ 4784 million in November 2010. The FIIs were US$ 5468 million in October, US$ 4262.60 million in September, US$ 3082.75 million in August, US$ 5285.33 million in July and US$2433.99 million in June 2010. These figures clearly show the foreign investors' confidence about India's long term growth story. The expected medium term appreciation of rupee and the prospects of returns increasing further are forming a virtuoso cycle. The recent decision of the Federal reserve to buy $600 billion in government bonds will also stimulate the flows to India.

FII flows are at high US$ 4784 million

The FII flows was as low as US$ -1504.87 million in May mainly due to Euro zone crisis, US $2783.32 millions in April 2010, US $5206 million in March and only US $230 million in February 2010. For 2009-10, the cumulative FIIs were 29047 million as against -15017 million for 2008-09. The revival in major global economies along with the improvement in Indian share markets have helped in reversing the negative trend of foreign institutional investments of the crisis period of the economy. After registering a huge fall during the crisis, the 30 share index of Bombay Stock exchange Sensex started recovering and is hovering above the high 20,000 mark recently showing renewed confidence of Indian as well as foreign investors. Though the current global cues are highly uncertain, the domestic growth forecasts may push the Sensex higher. It is forecasted that the flows are likely to be high for the next three months.

Forecast:

Inflows for the next three months to be positive



Exports and Imports

The revival in the external demand following the recovery in industrialized nations and large base effect has resulted in this sustained positive growth in exports. The exports to the newer markets of Latin America and Africa have helped sustaining the growth. The export growth was at 21.3 percent in October at US $ 17.96 billion where as it was 23.2 percent in September at US $ 18.02 billion. It grew at 22.5 percent in August and only at 13.2 percent in July 2010 where as it grew at an annual 30.4 percent in June, at 35 percent in May and at 36.2 percent in April 2010. India's exports increased in March 2010 at the fastest pace in six years at 54.1 percent. It is expected that the exports would grow at around 18 per cent in next month. This relatively lower forecast, despite the recent stimulus majors by government to increase exports, is mainly due to the not so encouraging scenario in USA and Europe.

Exports rises at 21 percent

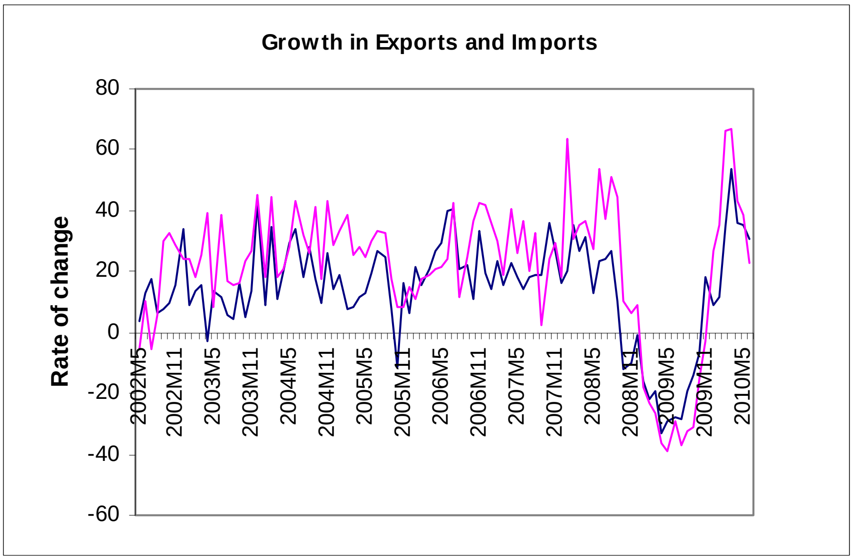
Imports rose at 6.8 percent in October, 2010 at $ 27.69 billion as against at 26.1 percent in September, 2010 at $ 27.14 billion. It grew at 32.6 percent in August, at 34.3 percent in July, at 23 percent in June and at 38.5 per cent in May 2010. This very low growth in October is mainly due to base effects. In October 2010, oil imports grew at 0.3 percent over the corresponding period last year, while non-oil imports grew at 9.9 percent. Non-oil imports during the April-October 2010 are 26.7 per cent higher than the level of such imports in the same period last year. The substantive rise in non-oil imports during last seven months shows the demand side is stabilizing at a higher level due to the rapid recovery process in the domestic economy.

Imports grows only at 6.8 percent

The trade deficit in October 2010 US$ 9.7 billion from US$ 11.1 billion in a year ago. The relatively lower deficit is due to slower growth of imports. The deficit was US$ 9.12 billion in September, US$13.06 billion in August, US$12.9 billion in July, US$10.6 billion in June, US$11.3 billion in May and US$10.4 billion in April 2010. The exports are forecasted to increase at a faster pace than the imports.

Forecast:

Exports growths are forecasted as19.73%,18.43% and17.37% for November December 2010 and January 2011 respectively. Imports are expected to increase by 14.66%,12.70% and 14.11% for November, December2010 and January 2011 respectively.



Note:

The forecasts that are presented in this document are based on the time series model namely Vector Autoregression model (VAR). Each variable has an independent model. This is based on monthly data from April 1993 onwards upto latest information available. The lag length for each VAR model is chosen with the help of Akaike Information Criterion (AIC). We estimate and forecast the VAR models by using Micro FIT software. More details is available at "A Short-term Time Series Forecasting Model for Indian Economy" available on our institute website at **http://www.iegindia.org/dis_bhanu_72.pdf**

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