MONTHLY MONITOR

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Highlights

Sharp fluctuations in Industrial activity continues

The annual growth of Index of Industrial Production for the month of March increased by 2.5 percent as against an increase of 0.6% in February 2013, an increase of 2.4% in January 2013, a decline of 0.6 percent in December 2012, while in October 2012 it rose to an unexpected level of 8.2 per cent. This increase in March 2013 is largely explained by the increase in the growth of manufacturing sector. When the industrial activity was showing the signs of pick up, the high policy rates are squeezing the demand and pulling the growth down.

Substantive drop in headline inflation

The year on year WPI inflation decreased to 4.89 percent in April from 5.96 percent in March and 6.84 percent in February 2013. The inflation in the same month of the previous year was 7.50 per cent. This substantive decline in inflation is largely explained by lower inflation for fuel, power, light and lubricants.

CPI inflation falls

The Consumer Price Index (CPI) for Industrial Workers fell to 10.24 percent in April from 11.44 percent in March 2013. The upward pressure on CPI is primarily attributable to increase in the prices of the food group which increased by 2.08 percent. The CPI was 10.22 percent during the same month of the previous year. The much sensitive food Inflation decreased to 12.39 percent in April from 13.21 percent in March 2013. It was a relatively lower at 10.66 per cent in during the same month of the previous year.

Rupee is marginally down

The monthly average rupee-dollar rate depreciated marginally to 54.87 in May, 2013 as against 54.40 until April 18, 2013, 54.37 in March 2013, 53.75 in February 2013 due to the increase in current account deficit. The Rupee is depreciating though the short-term portfolio inflows in the stock market have picked up substantially as there is a large current account deficit. The widening of trade deficit caused by the negative export growth rates in recent months was putting pressure on the rupee.

Reserves decreases

Foreign exchange reserves on May 24, 3013 stood at US$ 292.08 billion, to which foreign currency assets contributed US$ 261.57 billion, as against US$ 295.25 billion on April 12 2013. The accumulation of reserves is not going to go up substantially unless the uncertainties in the implementation of domestic policy reforms are reduced. The excess money at at abysmally low interest rates in OECD countries is helping in this accumulation process.

Exports growth decelerates

Exports grew by 1.68% in April 2013 in dollar terms over the corresponding month of the previous year as against the growth of 6.97 percent in March and 4.23 percent in February 2013. The incentives announced in recent foreign trade policy (FTP) helped in arresting the further fall in exports. High base effect, slow growth in USA and the Euro zone crisis were pulling down the exports growth even if depreciation of rupee was very substantial. High fluctuations in IIP at home are not good signs for exports.

Higher non-oil imports

Imports during April 2013 have shown an annual growth of 10.96 percent as against a growth of (-) 2.87 percent in March and 2.65 per cent in February 2013. Cumulative value of imports for the year 2012-13 stood at US$ 491.487 billion registering a growth of 0.44 per cent over the same period last year. Though there was a substantive fall in the growth in non-oil imports during last fiscal it has increased substantially in April 2013. However one needs to wait a few months to see whether the demand side is able to pick up to a higher level.

The high domestic inflation and the euro zone crisis have pulled down the export growth to negative zone in recent times The low export growth and elevated oil prices resulted in huge trade deficits. It is a big positive that oil prices have come down and, in policy front, there is a lot of action since September 2012 though uncertainties in implementation remains.

Trade deficit remains elevated

The trade deficit for April 2013 remains elevated at US $ 17.79 billion, as against US $ 14.04 billion for the same period last year. The trade deficit for the year 2012-13 was at US $ 190.91 billion which was 4.12 per cent higher than the deficit during the corresponding period of the previous year.

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IEG FORECAST

Variables	Latest Information available	Forecast for next three months
Inflation rate (WPI)	4.89% in April 2013	5.18%,4.91%,4.67%
Inflation rate (CPI)	10.24% in April 2013	9.56%,9.38%,9.02%
Growth rate of IIP	2.5% in March 2013	2.98%, 4.56%, 6.02%
Growth rate of M3	12.2% on May 17, 2013.	12.52 %,12.68%,12.89%
Re/$ exchange rate	54.87 in May 2013.	55.91, 55.63, 54.18
Forex reserves	US$ 292.08 billion on May 24, 2013	$293.28, $294.02, $294.89
FII inflows (Net)	US$5175.53 million in May, 2013	Positive and moderate
Growth rate of exports	1.68% in April 2013	2.13% on average for next three months
Growth rate of imports	10.96% in April 2013	7.87% on average for next three months

Inflation

WPI inflation is down substantially

The year on year WPI inflation decreased to 4.89 in April from 5.96 in March 2013. It was at 6.84 percent in February, 6.62 percent in January 2013, and 7.18 percent in December, 7.24 per cent in November, 7.45 per cent in October and 7.81 per cent in September 2012. The inflation in the same month of the previous year was 7.50 per cent. This substantive decrease in inflation is largely explained by lower inflation for fuel, power, light and lubricants.

In April 2013, the year on year primary articles inflation, with a weight of 20.12 per cent in the index, was 5.75 per cent of which the food articles inflation was 6.08 per cent. The inflation for fuel, power, light and lubricants, with a weight of 14.91 per cent in the index, was 8.84 percent and the inflation for the principal sector, the manufacturing products with a weight of 64.97 per cent in the index, was 3.41 per cent.

Since August 2010 when the new series was introduced, the inflation rate was always higher than 8 per cent. However, this trend saw a decline from December 2011 as the WPI has come down to a relatively more comfortable orbit of less than 8 per cent. Since last two months it has come down to below 6 percent. However, there is a likelihood that it may start increasing after a few months. Infrastructure deficit will put pressure on prices through supplies. The high fiscal deficit and the low value of rupee are putting an upward pressure on inflation. The reforms announced a few months ago by the government are helping to contain the fiscal deficits. The good rabi crops will help in bringing down food inflation. Further, the policy rates are still high and putting a downward pressure on demand.

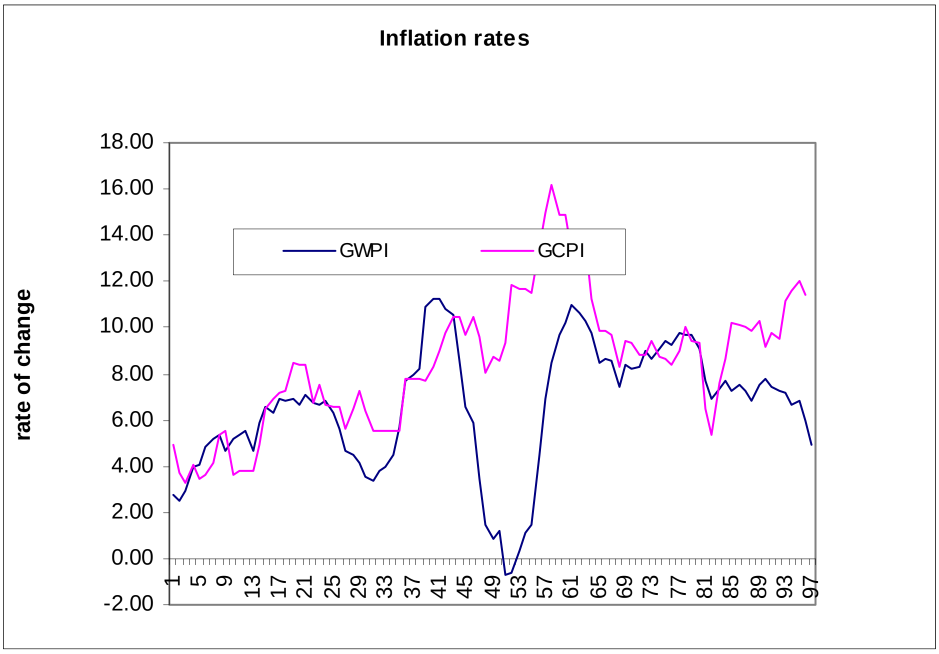
On balance, the inflation is likely to be around five percent in next three months.

A marginal fall in CPI inflation

The Consumer Price Index (CPI) for Industrial Workers fell to 10.24 percent in April from 11.44 percent in March 2013, 12.06 percent in February 2013 and 11.62 percent in January 2013. The upward pressure on CPI is primarily attributable to increase in the prices of the food group which increased by 2.08 percent. The CPI was 10.22 percent during the same month of the previous year. The much sensitive food Inflation decreased to 12.39 percent in April from 13.21 percent in March 2013, 14.98 percent in February and 14.08 percent in January 2013. It was a relatively lower at 10.66 per cent in during the same month of the previous year.

Forecast:

The WPI inflation forecasts are 5.18%, 4.91% and 4.67% for May, June and July 2013, respectively. The CPI inflation forecasts are 9.56%, 9.38% and 9.02% for May, June and July 2013, respectively.



Industrial Production

Sharp fluctuations in Industrial activity continues

The annual growth of Index of Industrial Production for the month of March increased to 2.5 percent from 0.6 percent in February 2013, 2.4 percent in January 2013, while in December 2012 it declined by 0.6 percent and in November 2012 it declined by 0.1 percent. This increase in March 2013 is largely explained by the increase in the growth of manufacturing sector.

The Mining, Manufacturing and Electricity sectors having weights of 141.57, 755.27 and 103.16, grew by (-) 2.9 percent, 3.2 percent and 3.5 percent, respectively, for the month of March 2013 as compared to the same month in the previous year. The cumulative growth in the above-mentioned three sectors have been (-) 2.5 percent 1.2 percent and 4.0 percent respectively, during April-March 2012-13 over the same period last year. This led to an increase of 1.0 percent in the overall cumulative growth in the General Index.

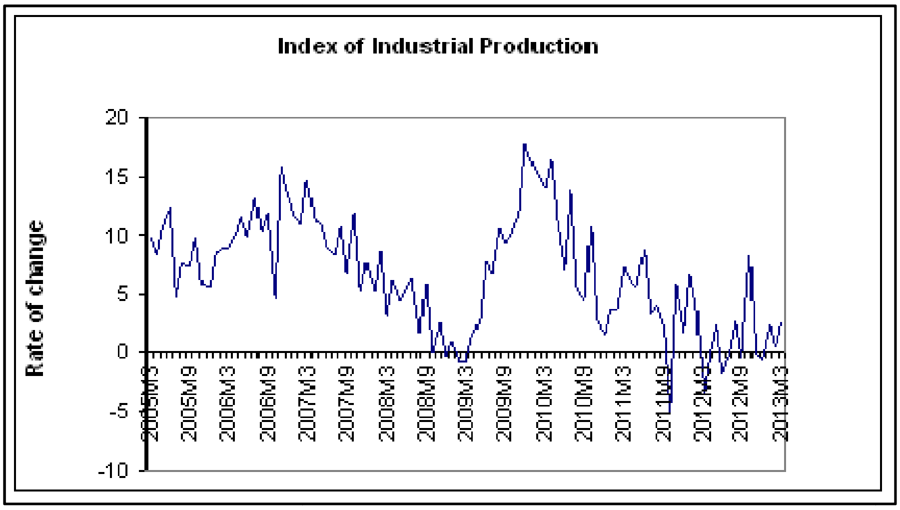
Out of the twenty-two industry groups, only ten groups have shown positive growth during March 2013. Industry groups like ‘Wearing apparel; dressing and dyeing of fur’, ‘Electrical machinery & apparatus n.e.c.’ and ‘Medical, precision & optical instruments, watches and clocks’ have recorded growth rates of 152.3, 64.6 and 37.7 percents, respectively, thus contributing to the increase in the general index.

In March 2013, the annual growth rates in Basic goods and in Intermediate goods stood at 2.6 percent and (-) 0.2 percent, respectively whereas the crucial Capital goods sector grew at a reasonably high rate of 6.9 per cent. The capital goods sector contracted by 6.3 per cent during April-March 2012-13. This is not a very good sign for sustaining the overall growth rate in the economy especially when there is not much flexibility in the output gap in the economy. The Consumer goods sector rose by 1.6 percent, the Consumer durables recorded a fall of 4.5 percent, whereas the Consumer nondurables registered an increase of 6.5 percent in March 2013.

Besides the high interest rates, the land acquisition and environmental clearance issues are also affecting the industry sector as a whole. The industrial activity is not able to break the low level trajectory. Rather, recently, the IIP growth has become extremely volatile. The revival in demand supported by the low base for the year 2009 was able to deliver continuous higher growth rates later on. However, the pace of growth got tapered off afterwards as the base effect wore off and the impact of high policy rates became effective. The global situation is adding fuel to the fire. The inflation pushed rate hikes are squeezing the demand and pulling the growth down. However, the recent policy announcements have been the sources of great relief. Inflation has also come down below 5 percent and RBI is reducing the policy rates though at a slower pace. The government needs to keep the tempo of policy reforms in reducing the fiscal deficit and trade deficit, and addressing the long run supply concerns in agriculture. It is also time for the RBI to reduce the policy rates further from the existing high level.

Forecast:

Based on the available information we forecast the IIP growth rate for the next three months to be 2.98%, 4.56% and 6.02% for April, May and June 2013, respectively.



Money and Credit

Money supply growth remains unchanged

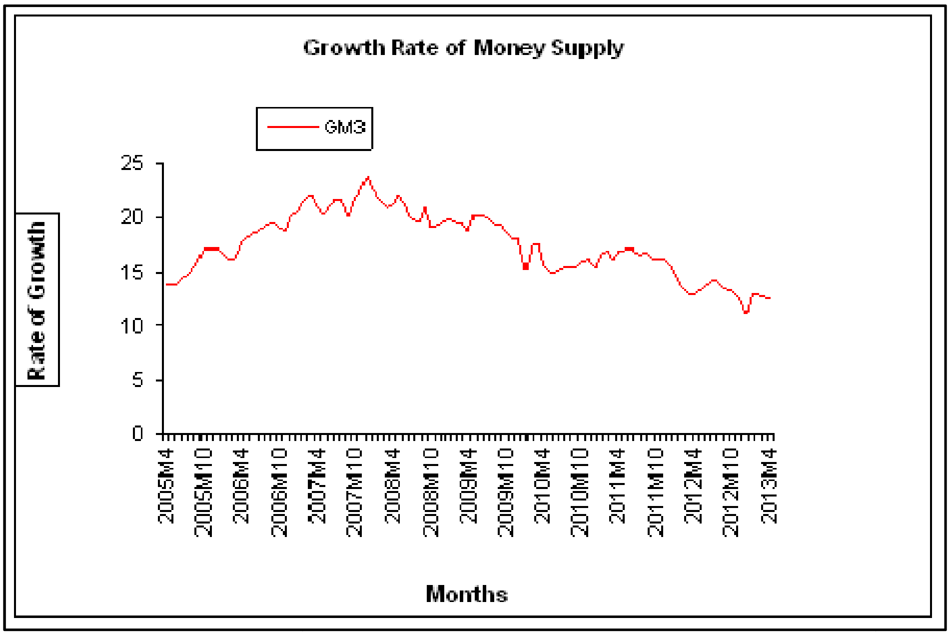
The year-on-year growth rate of broad money (M3) supply clocked 12.2 percent on May 17, 2013 as against 12.6 percent on March 8, 2013, 12.7 percent on February 8, 2013, 11.2 per cent on December 28, 2012 and 12.5 percent on November 30, 2012. This is lower than its growth of 13.8 percent for the last year. This is also about one per cent lower than its projected growth of 13 per cent set for the whole year. The expansion in money supply was contributed by the net credit to the government at 13.7 percent and credit to the commercial sector at 13.8 percent among other sources.

Non-food credit has grown only at 1.9 percent annually on May 17, 2013. Food credit growth has been negative.

Money supply has slowed down even if the FIIs are pouring in large sums of money to the equity markets in India, as expectations of implementation of policy reforms are high. The money supply is forecast to grow over 12.5 per cent for the next three months.

Forecast:

The growth rates of money supply (M3) are forecast to be 12.52%, 12.68% and 12.89% for June, July and August 2013, respectively.



Interest rates

Interest rates are declining gradually

The growth in the economy is not picking up. The headline inflation is sharply down since last two months though it remained elevated for a long time. The RBI gave a positive surprise by reducing the repo rate by 50 basis points to 8 per cent in April 2012. The subsequent cuts in repo rate and in CRR down to 7.25 percent and 4.00 percent, respectively, are also helpful. As India is showing the sign of moving towards a stagflation like situation, RBI should go for a reduction in policy rates by another 50 basis points in the next policy review. On the positive side, the government is announcing measures since September 2012 that are expected to help in checking the fiscal deficit though uncertainties about implementation at ground level remains.

Earlier, the prime lending rates saw upward revision due to both the continuous upward revision of policy rates, upward revision of deposit rates and the uncertainty in the global scenario. However, there are recent reductions by banks in interest rates though these reductions are much less than the reduction in repo rates. In the medium term, increases in GDP growth will increase the growth in demand for money while monetary easing by RBI will increase the supply softening pressure on the market interest rates. The corporates may increase their borrowings from outside the country as the interest rates are very low, which may have a softening effect on the domestic interest rates. On balance, we believe that the market interest rates may come down, though gradually, in the next three months.

Exchange rate

Rupee depreciates marginally

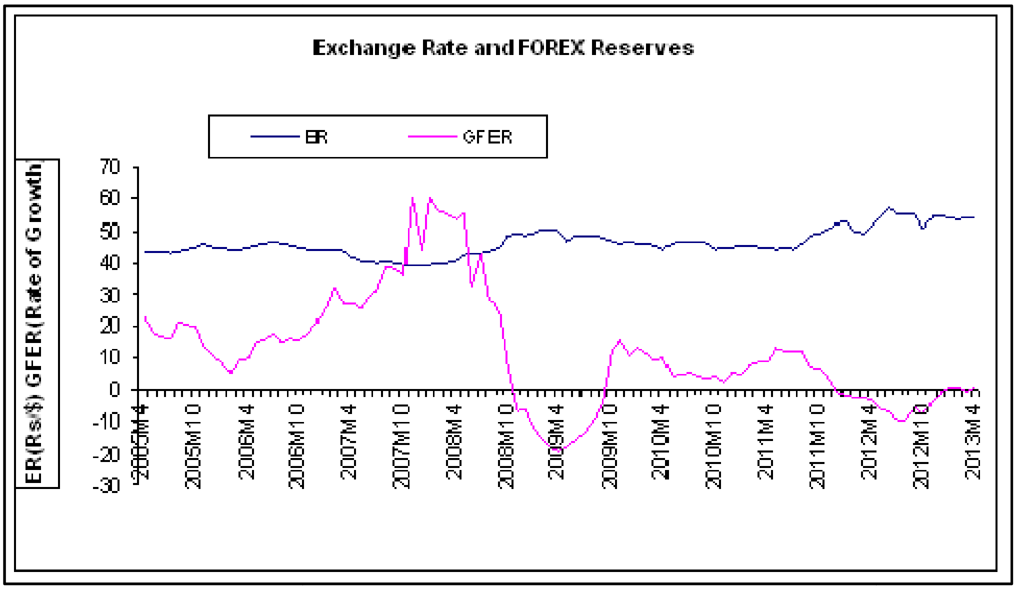
The monthly average rupee-dollar rate depreciated marginally to 54.87 in May, 2013 as against 54.40 until April 18, 2013, 54.37 in March 2013, 53.75 in February 2013 due to the increase in current account deficit. The Rupee is depreciating though the short-term portfolio inflows in the stock market have picked up substantially as there is a large current account deficit which was more than 6 percent in December quarter. Currently rupee has sharply declined to about 57 rupees per dollar.

Earlier, the exchange rate slipped to 54.41 for the month of May from 51.73 for the month of April and 50.21 for the month of March 2012, as the current account deficit widened to 4 per cent of GDP. The monthly average of exchange rate went down further to 56.00 till August 17, 55.48 in July and 55.99 in June 2012 contributed by internal policy lethargy and a not so comforting external situation. The widening of trade deficit caused by the rise in crude prices as well as the negative export growth rates in recent months were putting pressure on the rupee.

However, the low value of rupee is proving to be a short run phenomenon. In medium to long run, the rupee is expected to be stronger. By the middle of the next fiscal, when growth starts picking up, rupee will start gaining. The monthly average of the rupee-dollar rates were 44.7 until August 24, 44.62 until May 20 and 45.18 until March 17, 2011. The continuous flow of FIIs into the stock market and the underlying strong growth potential of the economy had assisted in strengthening the Indian rupee during this period. The rupee hit a five-month high on the 4^{th} October 2010 at 44.24 per dollar and it touched a record low of about Rs 57 against the US dollar in mid-June 2012. Rupee appreciated 12.9 per cent during the year 2009-10 as against a depreciation of 25.5 per cent in the previous year. This appreciation was mainly due to macroeconomic recovery during that period.

Forecast:

In coming months, the exchange rate is expected to be around 55.91, 55.63, and 54.18 for June, July and August 2013, respectively.



Foreign Exchange Reserves

Reserves decreases

Foreign exchange reserves on May 24, 3013 stood at US$ 292.08 billion, to which foreign currency assets contributed US$ 261.57, as against US$ 295.25 billion on April 12 2013, US$ 293.37 on March 22, 2013, US$ 291.92 billion on February 22, 2013 and US$ 296.25 billion on January 11, 2013. The total reserves stood at US$ 294.88 billion on October 12, US$ 294.48 billion on September 14, US$ 289.17 billion on August 10, US$ 288.62 billion on June 22, and US$ 288.26 billion on May 25, 2012.

Foreign exchange reserves went up impressively from US$ 273.72 billion in May 28, 2010 to US$ 297.99 billion on November 19, US$ 295.03 billion on December 24, 2010 and US$ 318.36 billion on October 7, 2011. This is a substantial progress from the below 250 billion mark during 2009. In the process, it crossed the peak of 314.61 billion of May 2008.

The recent rise in reserves is mainly due to the rise in inflow of foreign investment into Indian market. The rise in the stock market indices attracting huge FII inflows. The high interest rate differentials between India and the rest of the world, which is also likely to continue for some time, must have helped in this increase. The current domestic policy uncertainty is not helpful to the accumulation of reserves. On balance, we forecast an increase in the forex reserves for the next three months.
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Forecast:
Forex reserves are expected to be US$293.28, $294.02 and $294.89 billion in June, July and August, 2013, respectively.

Foreign Institutional Investment

Substantive increase in FII inflows

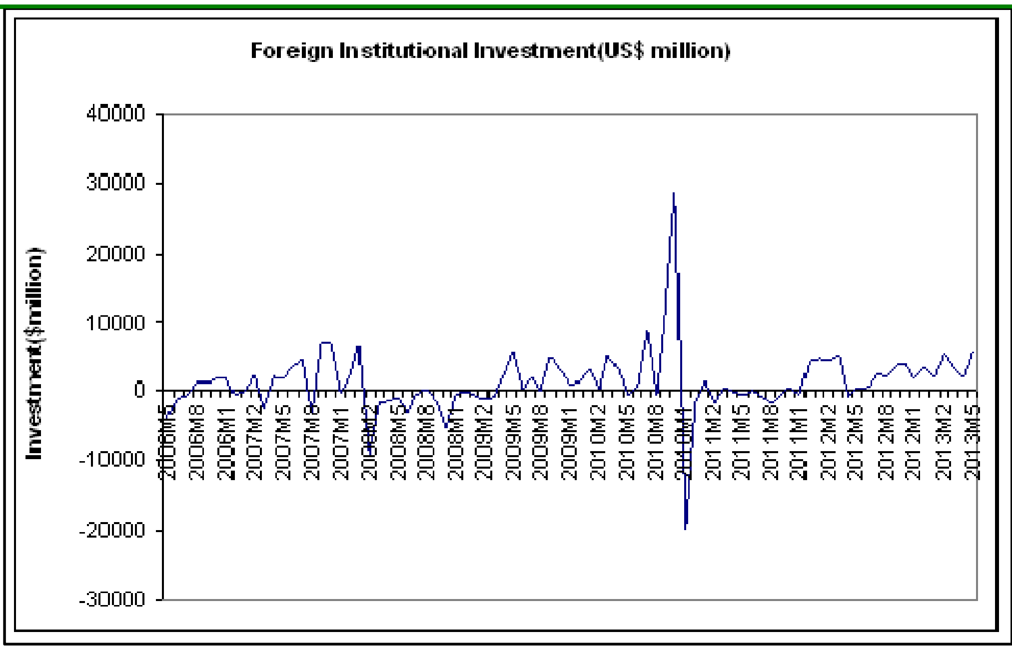
The average monthly foreign institutional investments (FIIs) in the Indian economy was at US$ 5175.53 million for the month of May 2013 of which equity was US$ 4042.64 million, as against US$ -76.15 million for the month ending 18 April, 2013 of which equity was US$ 573.96 million, and US$2741.49 million in March, 2013 of which equity was US$ 1675.48million. The monthly average of FIIs stood at US$ 4416.89 million till January 16, 2013 of which equity was US$ 4284.74 million, US$ 5572.55 million till December 27, 2012 of which equity was US$ 5082.47 million, even if uncertainties about the reform process in the domestic economy still remained. The reform packages by the Indian government if implemented at the ground level then inflows may rise pushing up the stock market indices further.

The monthly foreign institutional investments (FIIs) in the Indian market was modest at US$ 209.14 million for June 2012 though the FIIs in equity market were negative at US$ -86.16 million. The monthly average of FIIs was US$ 211.46 million until October 28, US$ -1790.59 million until August 24, US$ -651.93 million until May 20 and US$ -721.13 million for February 2011. This was mainly due to the Euro zone uncertainty. However, the FIIs were a high US$ 4784 million in November, US$ 5468 million in October, US$ 4262.60 million in September, and US$ 5285.33 million in July 2010. These later figures clearly show the foreign investors' confidence about India's long-term growth story.

The expected long-term appreciation of the rupee and the prospects of returns are making the Indian economy attractive for the FII inflows in the long term. For 2009-10, the cumulative FIIs were US$ 29047 million as against US$ -15017 million for 2008-09. The revival in major global economies along with the improvement in the Indian share markets had 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 crossed the 20,000 mark, and now hovering around 19,500.

Forecast:

Inflows are expected to be positive and moderate



Exports and Imports

Exports decelerates

Exports grew by 1.68 percent in April 2013 in dollar terms over the corresponding month of the previous year as against the growth of 6.97 percent in March, 4.23 percent in February, 0.82 percent in January 2013, contraction of1.92 percent in December, 4.17 per cent in November, 1.63 per cent in October, 10.78 per cent in September, 9.7 per cent in August, 14.8 per cent in July and 5.45 per cent in June 2012. The incentives announced in recent foreign trade policy (FTP) helped in arresting the further fall in exports. The government is planning to provide further support to exports soon. High base effect, slow growth in USA and the Euro zone crisis were pulling down the exports growth even if depreciation of rupee was very substantial. High fluctuations in IIP and higher inflation at home were not good signs for exports. However, inflation has already come down below 5 percent. The exports growth fluctuated in a very wide range from an astonishing 82 per cent expansion in July 2011 to a 14.8 per cent contraction in July 2012.The cumulative value of exports for the period April -March 2012 -13 was US $ 300.57 billion registering a negative growth of 1.76 per cent in dollar terms over the same period last year.

Imports during April, 2013 have shown an annual growth of 10.96 percent in dollar terms as against a growth of -2.87 per cent in March, 2.65 percent in February, 6.12 per cent in January 2013, 6.26 per cent in December, 6.35 per cent in November, 7.37 per cent in October, 5.09 per cent in September, - 5.08 per cent in August and - 6.47 per cent in July 2012. Cumulative value of imports for the period April-March 2012-13 stood at US$ 491.487 billion registering a growth of 0.44 per cent over the same period last year.

High growth in non Oil imports

Oil imports during April, 2013 were pegged at US $ 14.09 billion up by 3.92 percent over the corresponding period last year. Oil imports during the year 2012-13 were at US$ 169.253billion up by 9.22 percent over the corresponding period last year. Non-oil imports during March 2013 were estimated at US $ 27.87 billion, which was 14.90 per cent higher over the corresponding period last year. Non-oil imports during the year 2012-13 pegged at US$ 322.23 billion lower by 3.62 per cent over the corresponding period last year.

The abysmally low growth in non-oil imports during the last year shows the demand side was not able to sustain at higher level due to Euro zone crisis externally and high policy rates internally. The high domestic inflation and the euro zone crisis have pulled down the export growth to negative zone in recent times. The low export growth and elevated oil prices resulted in huge trade deficits. It is a big positive that oil prices have come down, non-oil import growth has picked up and, in the policy front, there is a lot of action since September 2012 though uncertainties in implementation remains.

Trade deficit at high level

The trade deficit for April 2013 was estimated at US $ 17.79 billion, as against US $ 14.04 billion for the same period last year. The trade deficit for April-March, 2012-13 was at US $ 190.91 billion which was 4.12 per cent higher than the deficit during the corresponding period of the previous year.

Forecast:

Exports growth rate is forecast to be at monthly average of 2.13% and import growth rate at monthly average of 7.87% for May, June and July 2013.