MONTHLY MONITOR

Prepared by
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	Highlights
Industrial growth up	**The annual growth of Index of Industrial Production for the month of October has come out at 10.8 percent versus lows of 4.4 percent in September and 5.6 percent in August 2010, and is largely explained by the increase of 31 percent in non-durable consumer goods and 22.0 percent in capital goods sector. The capital goods increased at a whopping 63.0 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 15 out of 17 industry groups recording positive growth in October 2010 and 14 out of 17 industry groups during the whole of 2009-10.**
WPI inflation cooling down	**The year on year WPI inflation was 7.48 percent for the month of November as compared to 8.58 percent for October, 8.62 percent for September and 8.51 percent for August 2010. Though accelerated food price increase is putting an upward pressure on overall inflation, 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 is putting a downward pressure on inflation.**
Marginal decline in Consumer Price inflation	**The annual growth in all India Consumer Price Index Number for Industrial Workers came down marginally to 8.33 percent in November from 9.70 percent in October and 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 45.21 per dollar in December 2010 as FIIs flows declined substantially. It is forecasted to appreciate for the next three months.**
Quantum of FII flows decline sharply	**Foreign exchange reserves stood at low of US$ 295.03 billion on December 24, 2010. It went up progressively from US$ 273.72 billion in May 28, 2010 to US$ 297.99 billion on November19, 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. These impressive**

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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.

Exports maintains its growth momentum while imports growth is still low

India's exports after growing at a very high pace in past few months are now slowing down, though it grew at a healthy 26.5 percent in November 2010, mainly due to the newer markets of Latin America and Africa. The wearing out of the base effects is contributing to this slow down. The exports expanded at a lower rate of 11.2 percent in dollar terms in November 2010 largely due to the base effect. The trade deficit in November 2010 was down to US$ 8.9 billion from US$ 10.0 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)	7.48% in November 2010	7.56%, 7.21%, 6.89%
Inflation rate (CPI)	8.33% in November 2010	8.40%, 8.37%, 8.28%
Growth rate of IIP	10.8% in October 2010	9.8%, 9.19% , 8.72%
Growth rate of M3	15.0% on December 17, 2010	15.12 %,15.25%,15.36%
Re/$ exchange rate	. 45.21 in December 2010	45.15, 44.99, 44.78
Forex reserves	US$ 295.03 billion on December 24, 2010	$296.73, $299.78, $297.98
FII inflows (Net)	US$ 710 million in December, 2010	Inflows for the next three months to be in the lower side
Growth rate of exports	26.5% in November 2010	26.32%,28.13%,34.12%
Growth rate of imports	11.2% in November 2010	19.98%,22.03%, 23.16%

Inflation

WPI inflation cooling down

The year on year WPI inflation was 7.48 percent for the month of November, 2010 as compared to 8.58 percent for October, 8.62 percent for September and 8.51 percent for August, 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 November 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 price for 'Non-Food Articles' group rose by a high 3.9 percent over the last month. The prices of light diesel oil and aviation turbine fuel increased by 5 and 4 percents respectively. In the Manufacturing group, the prices of electric connectors / plugs/sockets/holders rose by 20 percent, rubber moulded goods by 16 percent, woolen yarn by 15 percent, tea leaf by11 percent, viscose staple fiber by 8 percent and plastic/pvc pipes by 8 percent.

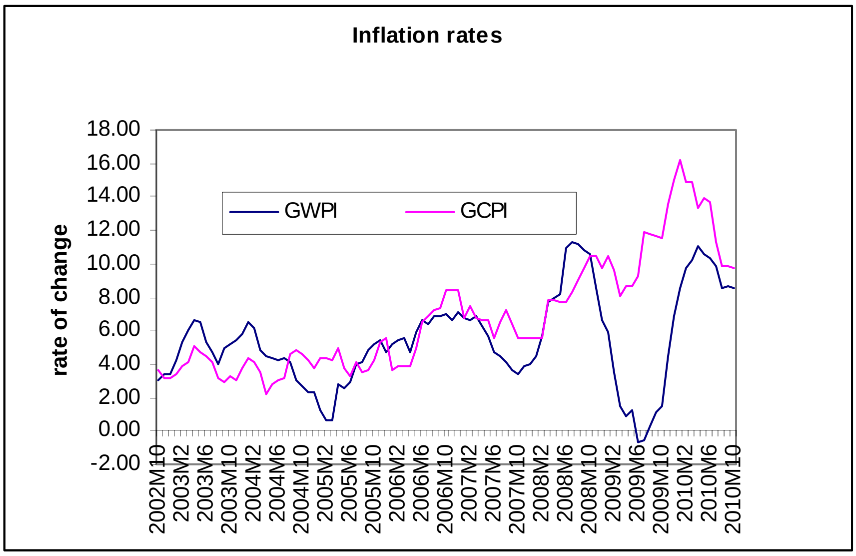
Though accelerated food price increase is putting an upward pressure on inflation, the withering of the base effect, the continuing monetary tightening of RBI though at a slower pace and the medium term rising trend of rupee is putting a downward pressure on inflation. On balance, the inflation is likely to be marginally down in the next three months.

CPI declines marginally

The annual growth in all India Consumer Price Index Number for Industrial Workers came down marginally to 8.33 percent in November from 9.70 percent in October and 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. 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 will remain around the same in the next three months as in November, mainly, due to the rise in food prices.

Forecast:

The WPI inflation forecasts are7.56 %,7.21 %, and6.89 % for December 2010, January and February 2011 respectively. The CPI inflation forecasts are 8.40%, 8.37% and 8.28% for December 2010, January and February 2011 respectively.



Industrial Production

Industrial growth is up

The annual growth of Index of Industrial Production for the month of has come out at 10.8 percent in October versus 4.4 percent in September 2010, and is largely explained by the increase of 31 percent in non-durable consumer goods and 22 percent in capital goods sector. The IIP grew at 5.6 percent in August, 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-October 2010-11 is 10.3 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 October 2010 also, out of 17 groups, 15 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 slow. The IIP growth is likely to hover around 7 percent in next three months due to the base effect and the tightening of monetary policy by the RBI.

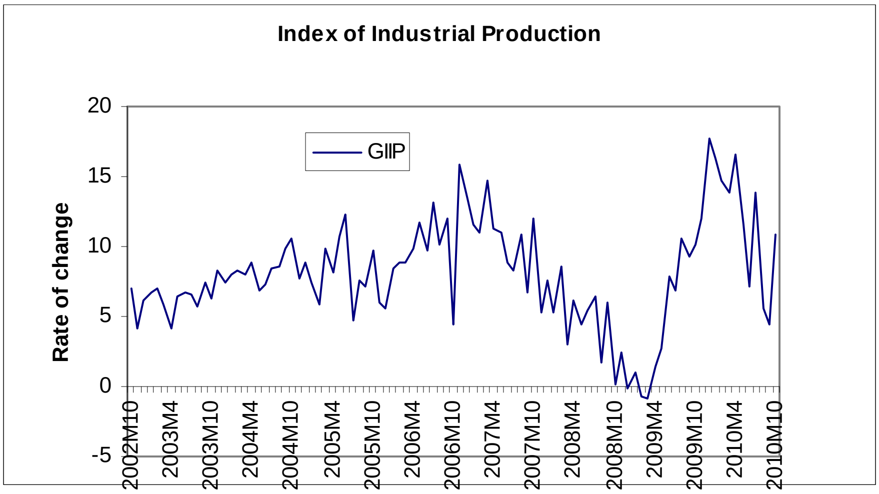
The Mining, Manufacturing and Electricity sectors for the month of October 2010 grew at 6.5 percent, 11.3 percent and 8.8 percent, respectively, as compared to the same month in the previous year. Industry groups like 'Transport Equipment and Parts', 'Leather and Leather & Fur Products' and 'Other Manufacturing Industries' have increased at high rates of 39.5, 26.0 and 24.6, respectively, 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 affecting 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.

Capital goods grow at 22 percent

In October 2010, the annual growth rates in Basic goods and in Intermediate goods are 7.7 percent and 9.5 percent, where as Capital goods increased by 22 percent. The high Capital goods growth is a good sign for sustaining the over all growth rate in the economy specially when capacity constraint has started raising its head in the economy. The Consumer goods grew at 9.6 percent while the Consumer durables grew at 31.0 percent and Consumer non-durables at 0.1 percent.

Forecast:

Based on the available information we forecast the IIP growth rate for the next three months to be 9.8%,9.19% and 8.72% for November , December2010 and January 2011



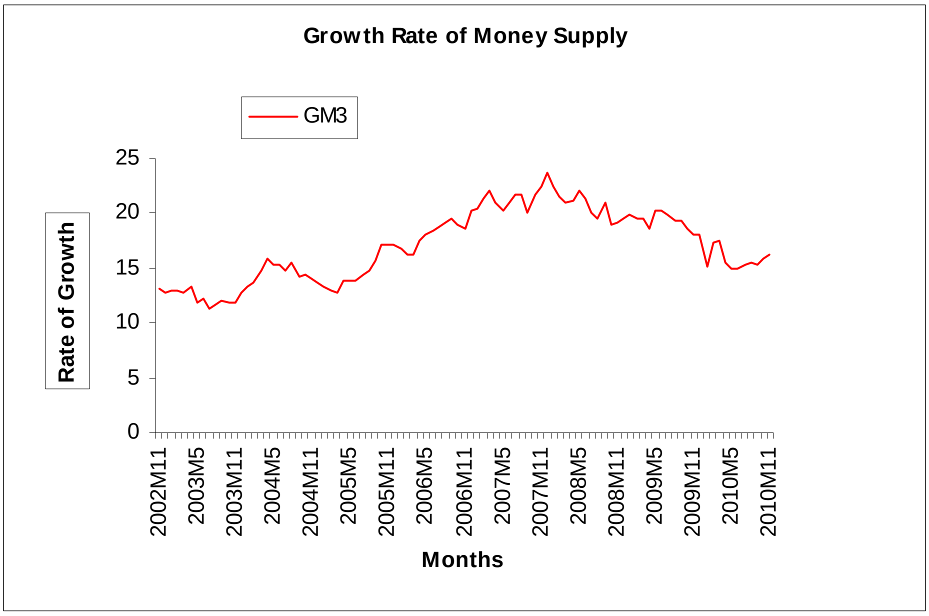
Money and Credit

Money supply up at 15 percent

As on December 17, 2010, Money supply grew at 15.0 percent as against 18.0 percent in the previous year. In 2010, it grew at 16.2 percent in November 19, 15.8 percent in October 8, and 15.6 percent in September 10. 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 contributed by the net credit to the Government increasing at 18.7 percent and credit to commercial sector at 22.4 percent. 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 has 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 15 percent for the next three months.

Forecast:

The forecast for the growth rate of money supply (M3) is15.12 %,15.25 % and 15.36 % for January, February and March 2011



Interest rates

Interest rates are in upward spiral

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 as the growth in food prices has risen. 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 continuous upward revision of policy rates, upward revision of deposit rates 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 policy rates as well as the market interest rates may increase further.

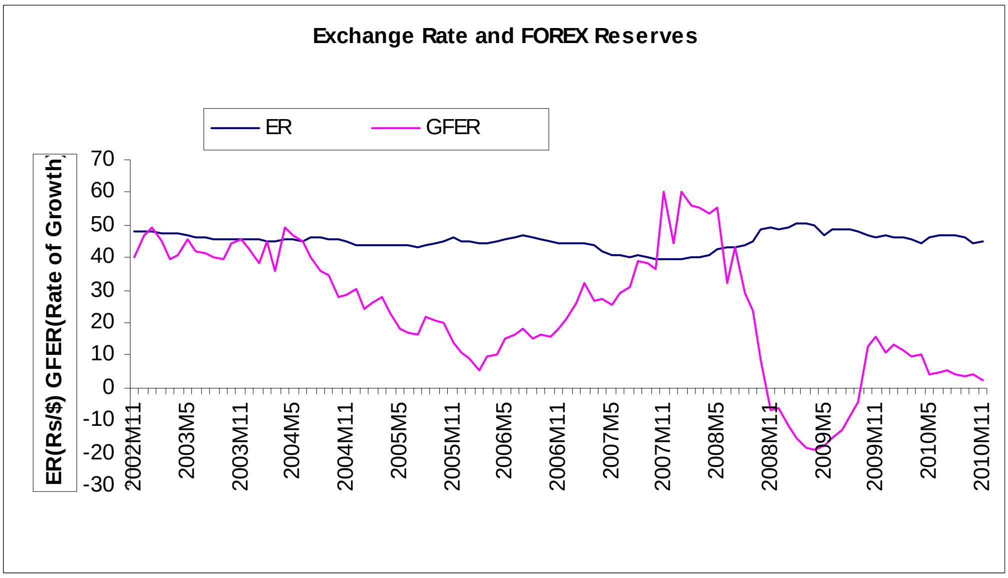
Rupee depreciate marginally

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 45.21 in December, 44.94 in November and 44.45 in October 2010. It is forecasted to appreciate in the next three months due to the likely increase in flows and growth in exports.

Forecast:

In coming months, exchange rate is expected to be around Rs/$45.15 , Rs/$44.99 and Rs/$44.78 for January, February and March 2011



Foreign Exchange Reserves

Foreign Exchange

Foreign exchange reserves stood at US$ 295.03 billion on December 24, 2010. It went up progressively from US$ 273.72 billion in May 28, 2010 to US$ 297.99 billion on November19, 2010. This is a substantial progress from a few months back when reserves reached below 250 billion mark, though it is away

Reserves at healthy US$ 295.03 billion

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, which is also likely to continue for sometime, must have helped in this increase. However, if the world economy grows at the predicted rate, the high oil import prices could restrain the accumulation of reserves. The increasing outflow of Indian FDI to other countries is also restraining the accumulation. On balance, we forecast marginally higher reserves for the next three months.

Forecast:

Forex reserves expected to be $296.73 billions, $299.78billions and $ 297.98billions in January , February and March 2011

Foreign Institutional Investment

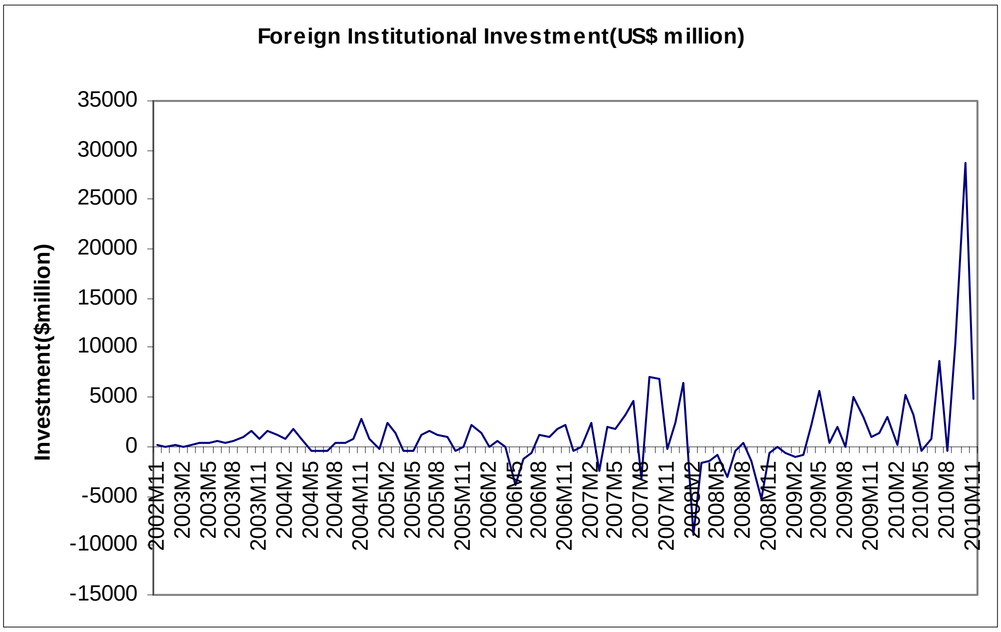
FII flows are at low US$ 710 million

The foreign institutional investments (FIIs) in Indian market were only US$ 710 million in December 2010. Where as the FIIs were US$ 4784 million in November, 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 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 on the lower side in comparison to last few months, for the next three months.

Forecast:

Inflows for the next three months to be in the lower side in comparison to the last few months.



Exports and Imports

Exports rises at healthy 26.5 percent

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. In terms of sectors, engineering, Gems and jewellery and petroleum products are contributing to the healthy export growth. The export growth was at 26.5 percent in November at US$ 18.9 billion where as it was 21.3 percent in October at US$ 18.0 billion. It grew at an annual 23.2 percent in September, 22.5 percent in August, 13.2 percent in July, 30.4 percent in June, 35 percent in May and 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 between 25 to 35 percent in next three month. This relatively higher forecast, is mainly due to the encouraging scenario in USA.

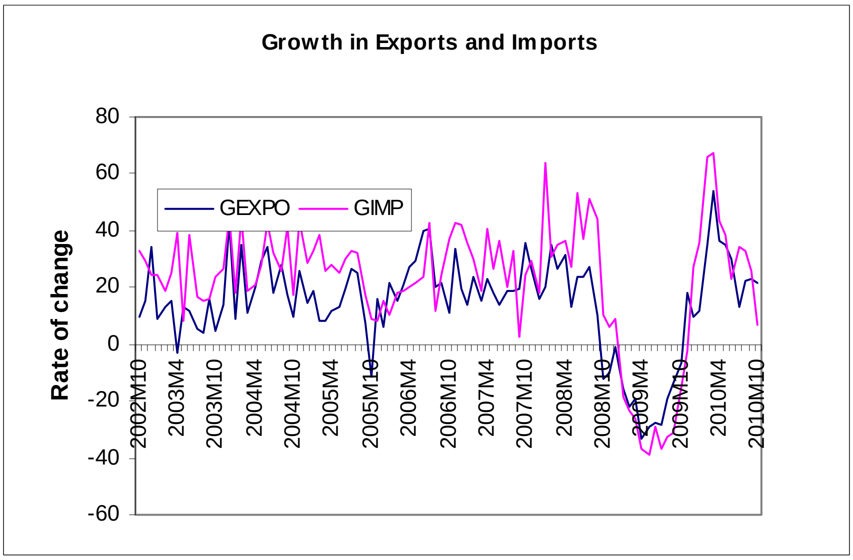
Imports grows only at 11.2 percent

Imports rose at 11.2 percent in November, 2010 at US$ 27.8 billion as against at a very low 6.8 percent in October, 2010 at US$ 27.7 billion. It grew at 26.1 percent in September, 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 low growth in November is mainly due to base effects. In November 2010, oil imports grew at 2.31 percent over the corresponding period last year, while non-oil imports grew at 15.05 percent. Non-oil imports during the April-November 2010 are 25.05 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.

The trade deficit in November 2010 was down to US$ 8.9 billion from 10.0 billion a year ago. The relatively lower deficit is due to slower growth of imports. The deficit was US$ 9.7 billion in October, 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 as26.32%,28.13% and34.12% for December 2010 ,January and February 2011 respectively. Imports are expected to increase by 19.98%,22.03% and 23.16% for December2010, January and February 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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