MONTHLY MONITOR

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	Highlights
High industrial growth continues and becoming broad based	**The growth of Index of Industrial Production for the month of April 2010 was 17.6 percent which is substantially higher than March's 13.5 percent expansion. The uptrend in industrial activity continues. The revival in demand supported by the low base for the year 2009 is able to deliver this continuous high growth. The 17.6 per cent growth was the seventh straight double-digit monthly expansion, driven largely by robust manufacturing output. The recovery has also become more broad-based with 14 out of 17 industry groups recording positive growth during the year 2009-10.**
Inflation in double digits And oil prices to be the major worry for the coming months	**Inflation rate stood at 10.16 percent for the month of May 2010 as compared to 9.59 percent in April 2010. The data for March 2010 was revised upwards to 11.04 percent from provisional figure of 9.9 percent. The rapid rise of IIP, the slow growth of agriculture and the low base effect explains this double digit inflation. To reduce the inflationary expectations, the Reserve Bank of India continues with it rate hikes.**
Exchange rate depreciates	**The exchange rate was 46.56 for June 2010. It was 46.49 on June 30 as against 44.44 on April 30, 2010 which was 19 months high. Rupee appreciated 12.9 percent during the year 2009-10 as against a depreciation of 25.5 percent in the previous year.**
FII flows at a healthy US$2424 million	**The foreign institutional investments (FII) in Indian market were around US $2423.99 millions in June 2010. As Indian economy has been growing at a faster rate among the major world economies, there is a robust inflow of foreign capital into the country. The expected appreciation of rupee is increasing the prospects of returns further. It dipped to US$ -1504.87 million only in May 2010 as a response to the Greek crisis.**
Exports jump 35% in May	**India's exports continue to show high growth as the global economic recovery boosted demand for Indian goods. Imports are also growing due to a steep increase both in oil and non-oil imports. The exports expanded at 35.1 percent and imports grew at 38.5percent in dollar terms in May 2010.**

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IEG FORECAST

Variables	Latest Information available	Forecast for next three months
Inflation rate (WPI)	10.16% in May 2010	11.12%,10.97%,9.54%.
Inflation rate (CPI)	13.91 % in May 2010	13.82%, 13.54 %,13.17%
Growth rate of IIP	17.6% in April 2010	14.96 %, 14.58%,13.78%
Growth rate of M3	14.5% on June18, 2010.	14.75 %, 14.93 %, 15.07 %
Prime lending rate	11-12 % in June 2010.	Around 11.6 % for the next three months
Re/$ exchange rate	. 46.56 in June 2010	46.33, 46.24,46.01
Forex reserves	(US$ 276.98 billion on 25th June2010))	$278.54, $282.53,$289.36
FII inflows (Net)	US$ 2423.99million in June 2010	Inflows to be moderate
Growth rate of exports	35.1% for May 2010	33.12% 34.69%,.32.34%
Growth rate of imports	38.5% for May 2010	39.22%,44.68%,42.63%

Inflation

Oil price and food inflation to be the major worry

Inflation rate stood at 10.16 percent for the month of May 2010 as compared to 9.59 percent in April 2010. The data for March 2010 was revised upwards to 11.04 percent from provisional figure of 9.9 percent. The rapid rise of IIP, the slow growth of agriculture and the low base effect explains this double digit inflation.

The primary articles index was up 3.5 per cent in May 2010 over the previous month while the index for fuel, power, light and lubricants as well as the index for manufacturing products rose by 1.2 percent.

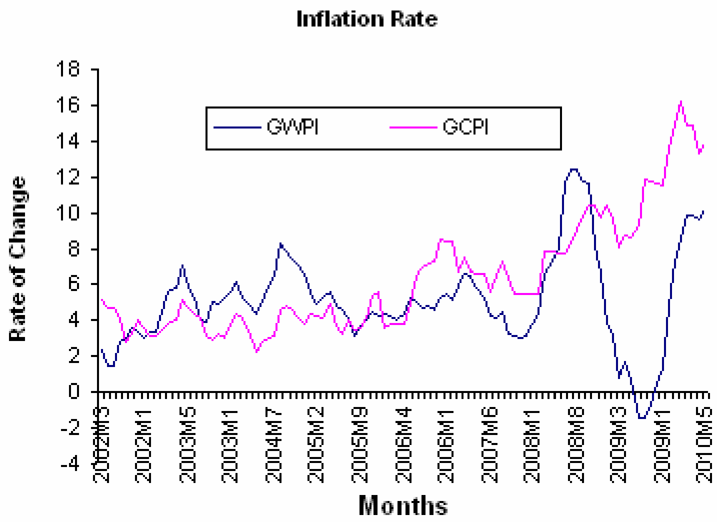
The rainfall is forecasted to improve substantially as against last year. This may dampen the inflationary expectation to an extent. The recent revision of crude prices as well as the demand side pressure will contribute to the price rise, assuming the current euro zone crisis is a temporary phenomenon. 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 go up for the next month and then start to cool down.

CPI decreased marginally

The annual growth in all India Consumer Price Index Number for Industrial Workers for the month of May 2010 was 13.91 percent as against 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, the double digit growth of CPI will continue, though it may come down a bit, for the next three months.

Forecast:

The WPI inflation forecasts are 11.12%, 10.97% and 9.54% *for June, July and August 2010, respectively. The CPI inflation forecasts are* 13.82%, 13.54 % and 13.17% *for June, July and August 2010, respectively.*



Industrial Production

The annual growth of Index of Industrial Production for the month of April has come out at 17.6 percent versus 13.5 percent in March 2010, and is largely explained by demand expansion and low base effects.

High industrial growth continues and becoming broad based

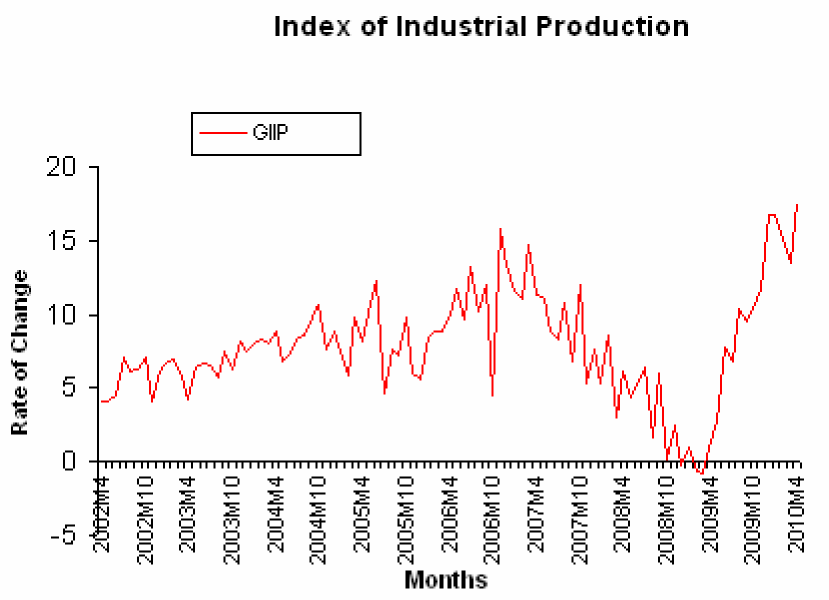
The 17.6 per cent growth in IIP was the seventh straight double-digit monthly expansion, driven largely by robust manufacturing output. The index recorded a growth of 17.6 per cent in December 2009, 16.7 per cent in January 2010 and 15.1 percent in February 2010. The uptrend in industrial activity continues. The recovery has also become more broad-based with 14 out of 17 industry groups recording accelerated growth during the year 2009-10. During April 2010, 15 groups showed positive growth out of 17 groups. The revival in demand supported by the low base for the year 2009 is able to deliver this continuous high growth. The IIP growth is likely to moderate further due to the base effect and the expected tightening of monetary policy by the RBI, even though the expected good monsoon may put a break on inflationary expectations. 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 Mining, Manufacturing and Electricity sectors for the month of April 2010 grew at 11.4 percent, 19.4 percent and 6.0 percent, respectively, as compared to the same month in the previous year. These sectors grew at 11.0 percent, 14.3 percent and 7.7 percent in the previous month.

Capital goods grew at a astounding rate of 72.8 percent. The sharp pick-up in the growth of the capital goods sector, which is in double digits since September 2009, points to the revival of investment activity which is a good sign for the sustainability of future growth momentum.

Forecast:

Based on the available information we forecast the IIP growth rate for the next three months are 14.96 %, 14.58%, 13.78% *for May, June and*



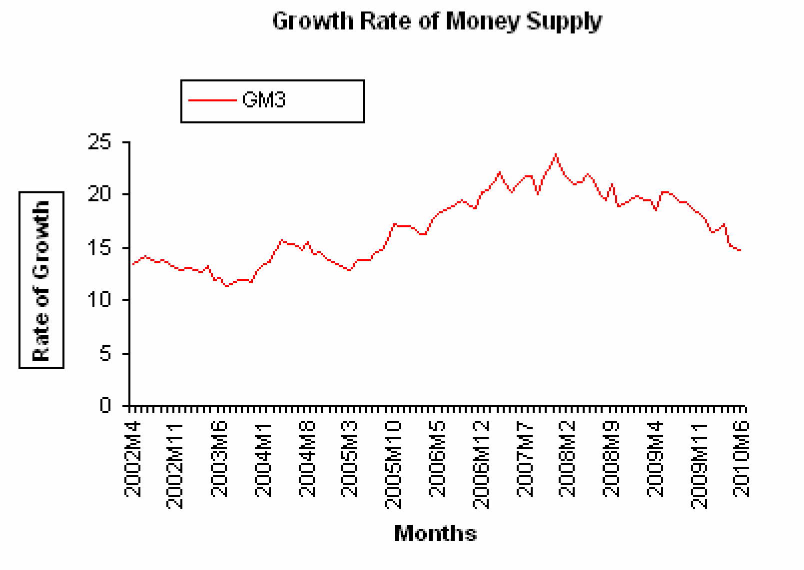
Money and Credit

Money supply growth is slowing down

Money supply grew at a slower rate of 14.5 percent June18, 2010 as against 15.03 percent on May 21, 2010. The funds flow is slowing down due to the monetary tightening of RBI. The huge fees, the central government is going to receive from the 3 G auctions may slow down the borrowing program of the government this fiscal. The expansion in money supply is likely to be mainly contributed by credit to the commercial sector and increase in net foreign assets. The money supply is forecasted to grow at about 15 percent for the next three months.

Forecast:

*The forecasts for the growth rate of money supply (M3) are*14.75 %**,** 14.93 % and 15.07 % *for July, August and September 2010*



Interest rates

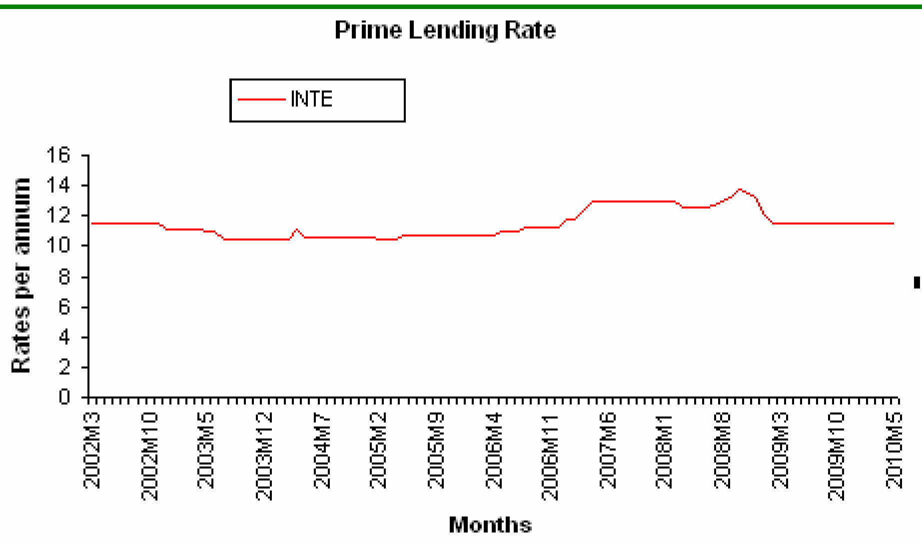
PLR remains static though policy rates revised upwards

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 given the inflationary pressure in the economy. Recently, RBI increased both repo and reverse repo rates by 25 basic points. The rise in prices has already started spilling over from supply to demand side. However, it is unlikely that the prime lending rates to see much change as is expected. Currently the prime lending rates are in the range of 11 to 12 per cent. However, in the medium term, high increases in prices and GDP will increase the demand for money while monetary tightening by RBI will reduce the supply putting a pressure on the market interest rates. The RBI needs to maintain a fine balance so as to put pressure on inflation without disturbing much the growth path.

The inflation rates (WPI) has touched double digits after turning positive in the first half of September 2009. The inflationary expectations are continues to be high as growth in food prices are not declining much and the growth momentum in the economy picking up. In fact, the Central bank will be closely watching how the Euro zone crisis is being resolved by the European countries along with the domestic growth rates and the monsoon forecasts before deciding whether to increase the policy rates further. Thus the complexities of macro economic management are increasing after the Greek debt crisis. On balance, we would like to believe that the policy rates may be revised upwards in small doses.

Forecast:

The Prime Lending Rates(PLR) are forecasted to stay around 11.6 % for the next three months



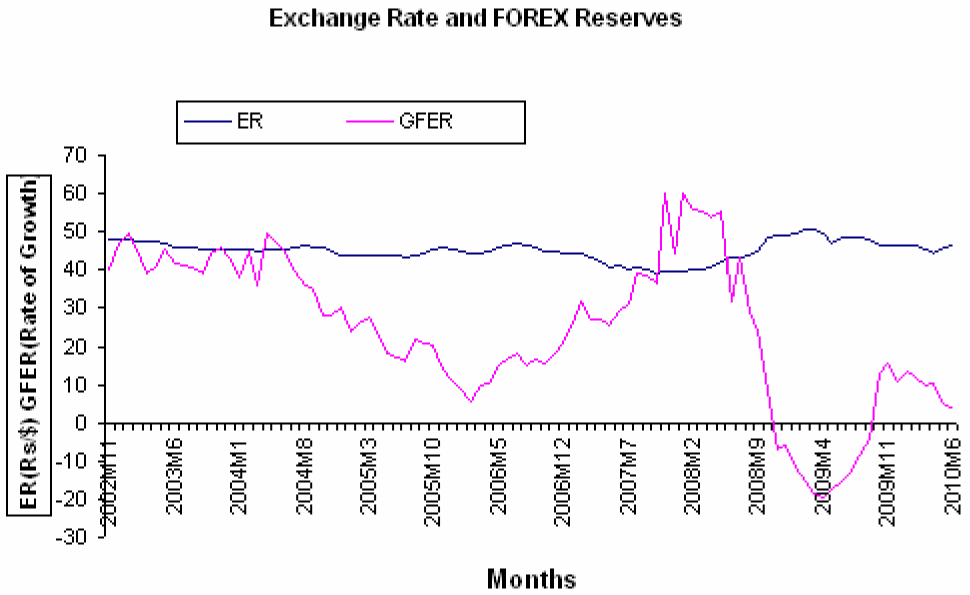
Exchange rate depreciates

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 exchange rate was 44.44 on April 30, 2010 hitting a 19 month high. 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 risk reduction in the Indian market. However, the expected widening of trade deficit may put pressure on ruppe. The rupee has deppreciated to 46.56 in June 2010 with respect to the previous couple of months, though it appreciate 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 Eurozone crisis. It is forecasted to appreciate in the next three months though it is unlikely to reach the April 30 figures so soon as Eurozone concerns remain. The RBI is likely to intervene to reduce the volatility in Rupee but it may let rupee appreciate in the long run.

Forecast:

In coming months, exchange rate are expected to be around Rs/$46.33, Rs/$46.24 and Rs/$46.01 for July ,August and September 2010.



Foreign Exchange Reserves

Forex reserves increase

Foreign exchange reserves stood at US$ 276.98 BILLION ON 25TH June 2010. It was US$ 273.72 billion in May 28, US$ 279.63 billion as in April, 279.06 billion in March and 278.36 billion in February 2010. This is a 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 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. As the world economy is looking up, the interest of foreign investors is likely to increase in the Indian market. The rise in stock market indices also attracting FII inflows. However, the Euro zone crisis, which may continue for sometime, could hamper inflow of foreign funds. Besides, if the world economy grows at the predicted rate, the high oil import prices could also restrain the accumulation of reserves.

Forecast:

Forex reserves expected to be $278.54 *billions*, $282.53 *billions* and $289.36 *billions for July, August and September2010, respectively.*

Foreign Institutional Investment

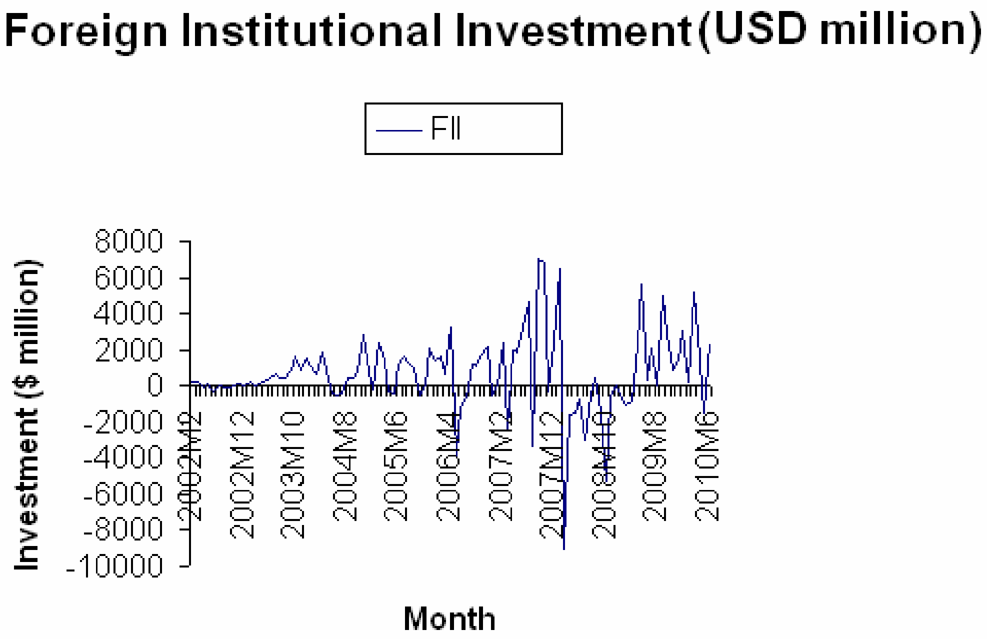
The foreign institutional investments (FII) in Indian market were around US$2433.99 million in June 2010 showing foreign investors' confidence about India's long term growth prospects. The expected appreciation of rupee is increasing the prospects of returns further. The FII flows was as low as US$ -1504.87 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.

FII flows at a healthy US$2424 million

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 around 17,000 mark recently showing renewed confidence of Indian as well as foreign investors resulting in reversing of FIIs movements. However, the current global cues are not conducive. If the Euro Zone crisis is arrested successfully, then the share markets will improve and the trend in inflows will continue.

The flows are likely to be moderate for the next three months mainly due to the Democles' sword of Eurozone concerns..

Forecast:
Inflows are expected to be moderate next three months



Exports and Imports

The revival in the external demand following the recovery in industrialized

Exports jump 35% and imports by 38.5% in May

nations and large base effect has resulted in this sustained positive growth in exports. India's May exports rose at an annual 35 per cent to $16.1 billion while it grew at an annual 36.2 percent in April 2010. The demand has picked up for India's iron ore, oil and leather goods. However, the jump in exports growth can also be attributed to the statstical base effect. This is the seventh consecutive rise after 13 straight months of decline. India’s exports increased in March 2010 at the fastest pace in six years at 54.1 percent in dollar terms. This is in spite of the Indian rupee strengthening for May, 2010. It is expected that the exports would grow at more than 30 per cent in the next three months. However, Euro Zone and China concerns remain.

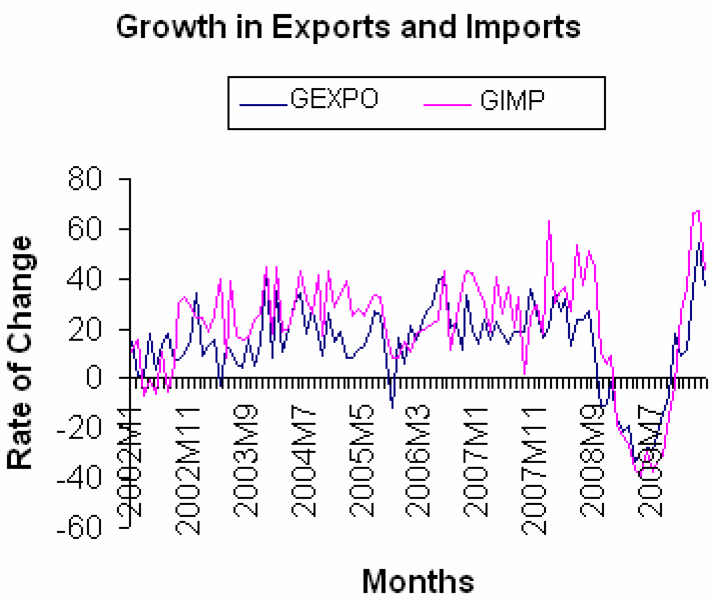
Imports rose 38.5 per cent to $27.4 billion in May 2010. Oil imports during May 2010 grew at 66.7 percent over the corresponding period last year Non-oil imports grew at 32.3 percent in May 2010. India’s oil imports surged 70.5 percent in April 2010 while non-oil imports grew 34.3 percent in April 2009. The trend of oil prices increase is likely to continue in the medium term assuming the euro zone problem gets resolved in the short run. The substantive rise in non-oil imports during last few months shows the demand side is picking up due to the recovery process in the economy.

Deficit to grow

The trade deficit widened to $11.3 billion in May 2010 from $10.42 billion in April 2010. The larger positive trend in imports has resulted in widening of trade deficit. The exports are forecasted to increase at around the same rate while imports growth is likely to be higher in the next three months. As a result, the deficit is predicted to increase further.

Forecast:

Exports growths are forecasted as **33.12%, 34.69% and 32.34%** *for June, July and August 2010 respectively. Imports are expected to increase by* **39.22%, 44.68% and 42.63%** *for June, July and August 2010 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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