MONTHLY MONITOR

Prepared by
Basanta K Pradhan & Sangeeta Chakravarty

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Highlights	
High industrial growth becoming broad based	The growth of Index of Industrial Production for the month of March 2010 is 13.5 percent which is lower than expected. The pace of growth is seen to be tapering off as the low-base effect wears off and the impact of rate hikes, withdrawal of stimulus picks up.
Oil prices to be the major worry for inflation in the coming months	The growth of IIP was also slower than February's 15.1 percent expansion. However, the 13.5 per cent growth was the sixth straight double-digit monthly expansion, driven largely by robust manufacturing output. 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. The revival in demand supported by the low base for the year 2009 is able to deliver this continuous high growth.
Food prices remaining high	Inflation rate stood at 9.59 percent for the month of April 2010 as compared to 9.90 percent for the previous month and 1.31% during the corresponding month of the previous year. The data for February 2010 was revised upwards to 10.06 percent from provisional figure of 9.89 percent.
Money supply growth is slowing down	Money supply grew at a slower rate of 15.17 percent in April 2010. Its growth for the month of March was 16.8 percent which is slightly more than 16.4 percent for February 2010.
	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.
Exchange rate appreciated substantially	The foreign institutional investments (FII) in Indian market were around US $2783.32 millions in April 2010. As Indian economy started recovering earlier than many major economies and its financial market is quite liquid there is an increasing inflow of foreign capital into the country.
Forex reserves increases	India's merchandise exports expanded in March at the fastest pace in six years at 54.1 percent in dollar terms as the global

Development Planning Centre, Institute of Economic Growth, Delhi University Enclave, Delhi-110007, India. Phone: (00)-91-11-27667365, Fax: (00)-91-11-27667410
E-mail: basanta@iegindia.org / sangeeta@iegindia.org URL: www.iegindia.org

to US$279.71 billions **Exports and imports surges ahead**	**economic recovery boosted demand for Indian goods. India's imports grew at a whooping 67.1 percent in dollar terms in March, 2010 due to a steep increase in oil import bill. Non-oil imports also increased substantially. The quick estimates of growth of exports and imports as reported in press for April 2010 are 36.2 percent and 43.3 percent, respectively. The surge in the external demand for cars, gems and Jewelry, and textiles mainly contributed to the exports growth.**

IEG FORECAST

Variables	Latest Information available	Forecast for next three months
Inflation rate (WPI)	9.59% in April 2010	9.09%,8.87%,7.93%.
Inflation rate (CPI)	14.86% in March 2010	14.53%, 14.21%,13.91%
Growth rate of IIP	13.5% in March 2010	13.40 %, 12.86%,13.21%
Growth rate of M3	15.17% on April 23, 2010.	15.28 %, 15.39 %, 15.49 %
Prime lending rate	11-12 % in April 2010.	Around 11.6 % for the next three months
Re/$ exchange rate	. 44.44 on April 30, 2010	45.52, 45.60,45.65
Forex reserves	US$ 279.71 billion in April , 2010	$280.55, $278.81,$276.61
FII inflows (Net)	US$ 2783.32million in April 2010	Inflows to be moderate
Growth rate of exports	36.2% for April 2010	38.96% 34.61%,.33.34%
Growth rate of imports	43.3% for April 2010	49.98%,45.68%,48.63%

Inflation

Oil price and food inflation to be the major worry

Inflation rate stood at 9.59 percent for the month of April 2010 as compared to 9.90 percent for the previous month and 1.31% during the corresponding month of the previous year. The data for February 2010 was revised upwards to 10.06 percent from provisional figure of 9.89 percent.

The indices for primary articles rose by 2.3 for fuel, power, light and lubricants rose by 0.6 percent from the previous month. The index for manufactured products accounting for 63.75 percent of weights rose by 0.8 percent from the previous month. The index for 'Food Articles' group rose by 2.8 percent. However, the index for 'Food Products' group declined by 3.1 percent.

High CPI a cause for concern

The primary articles index was up 16.76 per cent for the year ending May 1, 2010, compared with the previous week's 13.93 per cent and 6.39 percent during the corresponding week for 2009 while the index for fuel, power, light and lubricants rose 12.33 per cent as compared to 12.69 percent for the previous week and -6.17 percent during the corresponding week for the previous year.

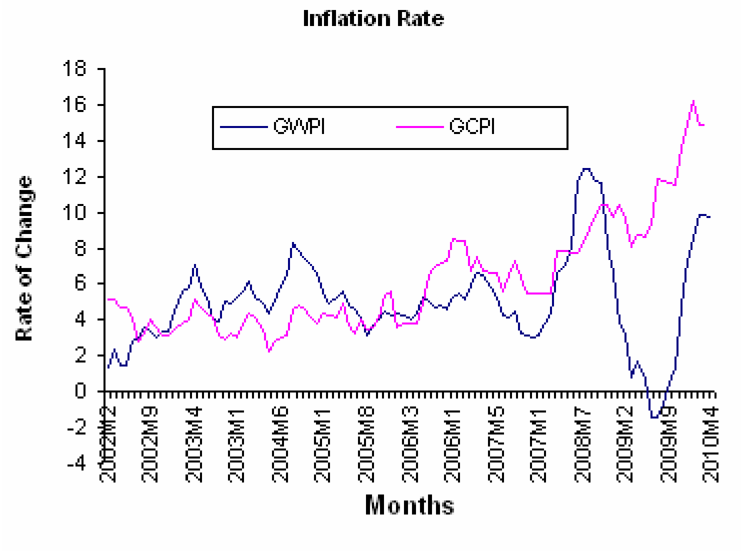
The India Meteorological Department has forecasted that the rainfall is likely to be 98 percent of the long-term average. This may dampen the inflationary expectation to an extent. The crude prices as well as the demand side pressure may contribute to the price rise, assuming the current euro zone crisis 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 cool down in the next three months.

The annual growth in all India Consumer Price Index Number for Industrial Workers for the month of March, 2010 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.

It is likely that inflation rates have peaked in March 2010.

Forecast:

The WPI inflation forecasts are 9.09%, 8.87%, 7.93% for May, June and July, 2010, respectively. The CPI inflation forecasts are 14.53%, 14.21% and 13.91% for April, May and June, 2010, respectively.



Industrial Production

The Quick Estimates of growth of Index of Industrial Production for the month of March 2010 is 13.5 percent which is lower than expected. 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.

IIP declined compared to February 2010

The growth was also slower than February's 15.1 percent expansion. However, the 13.5 per cent growth was the sixth straight double-digit monthly expansion, driven largely by robust manufacturing output. The uptrend in industrial activity continues. The index recorded a growth of 17.6 per cent in December 2009 and 16.7 per cent in January 2010. The recovery has also become more broad-based with 14 out of 17 industry groups recording accelerated growth during the year 2009-10. 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 Mining, Manufacturing and Electricity sectors for the month of March 2010 grew at 11.0 percent, 14.3 percent and 7.7 percent as compared to the same month in the previous year.

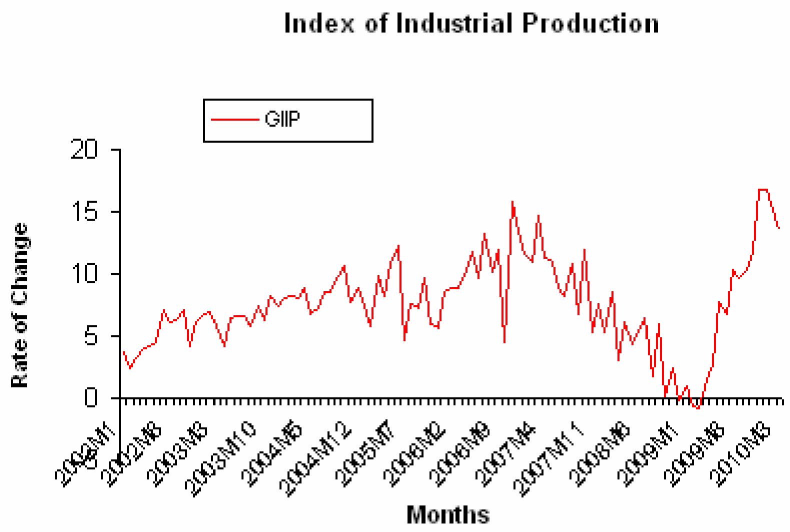
The industry group 'Metal Products and Parts, except Machinery and Equipment' have shown the highest growth of 42.8 percent, followed by 40.1 percent in 'Other Manufacturing Industries' and 26.2 percent in 'Food Products'.

Manufacturing industries were the main contributor to the high IIP growth

The Sectoral growth rates in March 2010 are 10.1 percent in Basic goods, 27.4 percent in Capital goods and 12.7 percent in Intermediate goods. The Consumer durables and Consumer non-durables have recorded growth of 32.0 percent and 3.3 percent respectively. The sharp pick-up in the growth of the capital goods sector, 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 to be 13.40%, 12.86% and 13.21% for April May and June 2010



Money and Credit

Money supply grew at a slower rate of 15.17 percent in April 2010. Its growth for the month of March was 16.8 percent which is slightly more than 16.4 percent for February 2010. There has been substantial credit flow to the government sector followed by moderate flow to the commercial sector. The huge fees the central government is expecting 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.

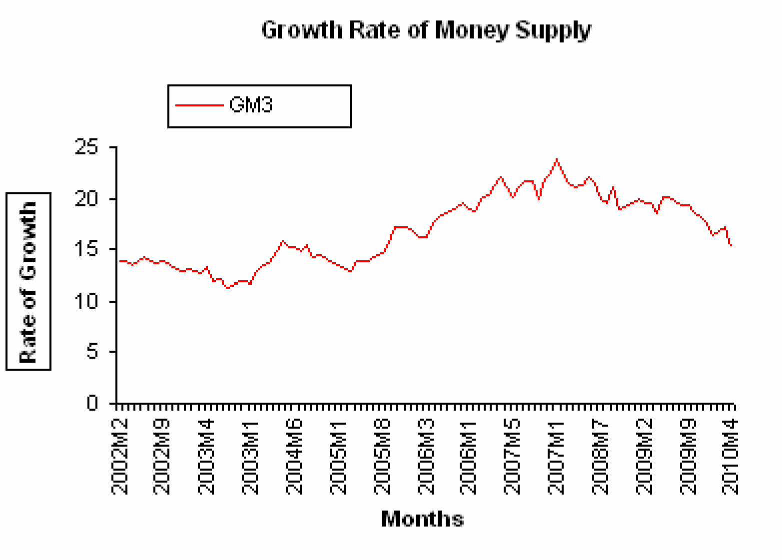
Money supply at 15.17 percent

The time deposits and other deposits with RBI increased substantially, while currency with the public and demand deposits with banks increased moderately. The RBI projects that the aggregate deposits of scheduled commercial banks are to grow by 18 percent and M3 to grow by 17 percent in 2010-11.

As the economy reviving, growth in money supply and real growth are moving in the same direction underlying the fact that the improved demand for credit from real economic activities. 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 choking the growth process. The RBI needs to maintain a fine balance so as to put pressure on inflation without disturbing the growth path.

Forecast:

The forecast for the growth rate of money supply (M3) is15.28 %, 15.39% and 15.49 % for May ,June and July 2010



Interest rates

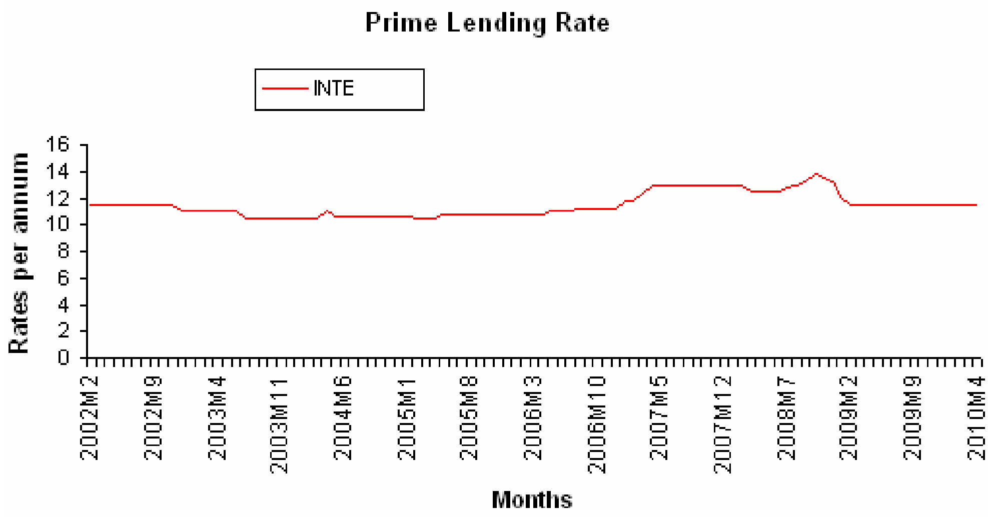
As the positive signs of the revival of the economy is sustaining itself, the RBI is slowly withdrawing from its low policy rates regime and the trend is going to continue given the inflationary pressure in the economy. The rise in prices has already started spilling over from supply to demand side. However, it is unlikely that the prime lending rates to see much change as was expected. Currently the prime lending rates as per RBI data 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 choking the growth process. The RBI needs to maintain a fine balance so as to put pressure on inflation without disturbing much the growth path.

PLR remains static though policy rates revised upwards

The inflation rates (WPI) has touched almost 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 is being defended by the European countries along with the domestic growth figures and the monsoon before deciding whether to spruce up policy rates. 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

The continuous flow FIIs into Indian stock market, strong growth of Indian economy and sudden weakness of the US dollar against other major currencies in the month of April helped the Indian rupee to strengthen. 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. The increase in capital inflows is putting pressure on exchange rates.

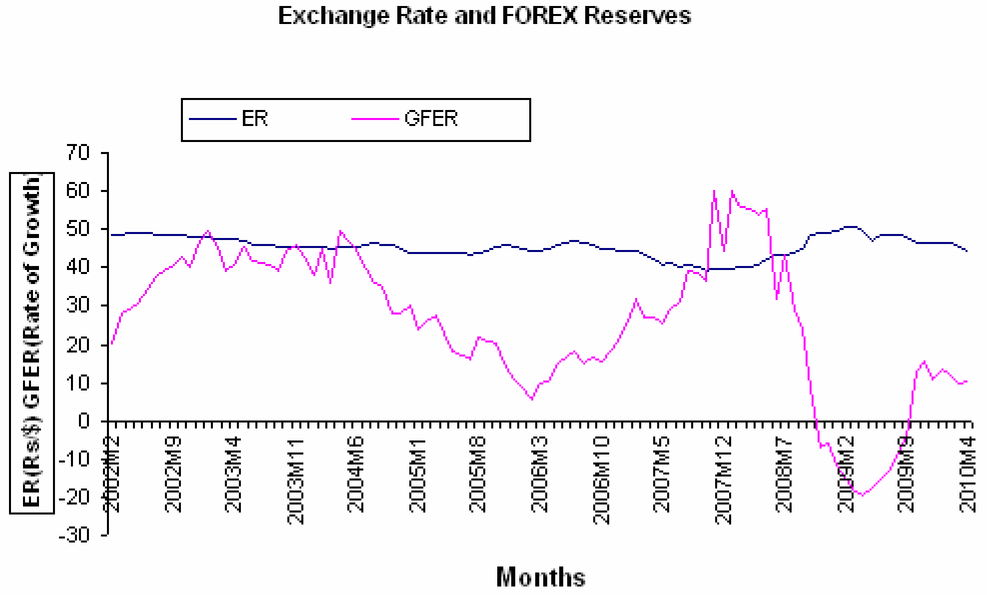
Too much appreciation of the rupee may be harmful to the economy specially in a scenairo when other major emerging economy is having a fixed rate. The RBI may intervene to reduce the volatility in Rupee but it may let rupee appreciate in the long run.

The current Euro Zone crisis and the further monetary tightening in China may reduce flows to India through the stock market. We predict a deppreciation of rupee in the next three months.

Forecast:

Substantial appreciation of rupee

In coming months, exchange rate are expected to be around Rs/$45.52, Rs/$45.60 and Rs/$45.65 for May, June and July 2010.



Foreign Exchange Reserves

Foreign exchange reserves stood at US$ 279.63 billion as on April 30, 2010. It was 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, which is 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. Though in the medium to long run there may be an increase in net capital flows to the country, in the short run it may not happen. Managing high foreign flows also has its attendant risks.

Accumulation in foreign exchange reserves

Forecast:

Forex reserves expected to be $280.55billions, $278.81 billions and $276.61 billions for May ,June and July 2010

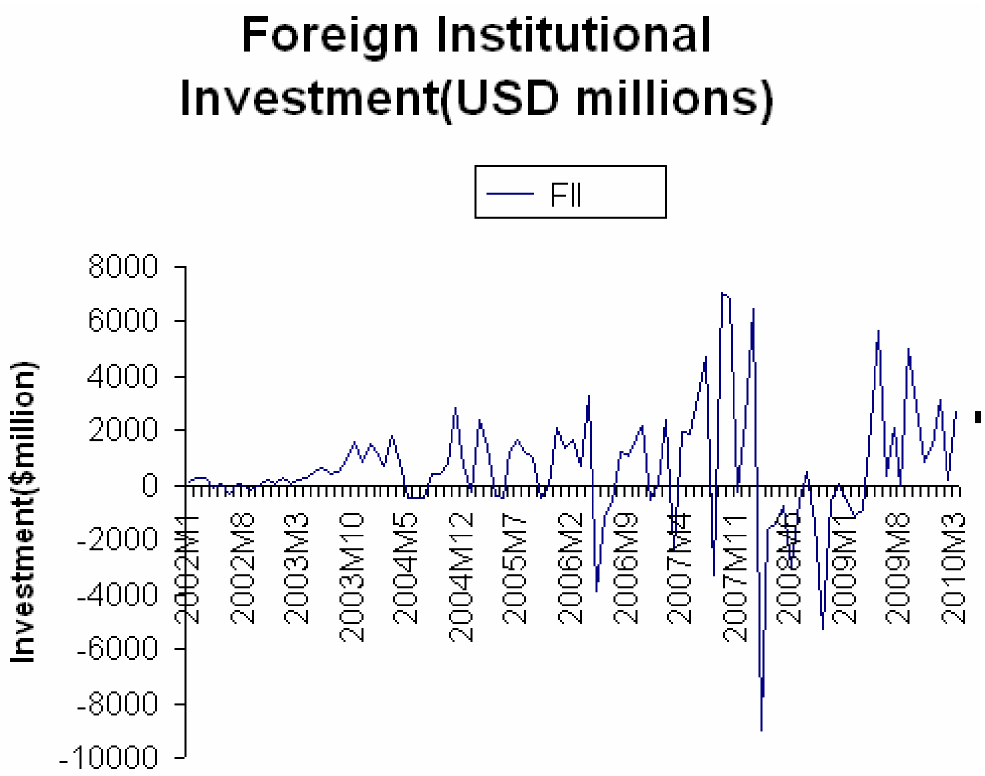
Foreign Institutional Investment

The foreign institutional investments (FII) in Indian market were around US $2783.32 millions in April 2010. It was 5206 million in March and only 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

FII inflow aids local currency's rise	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. The strong recovery signs of the global economy and the encouraging high GDP growth forecasts have added stimulus to the recent FIIs inflows into the country. 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 finance ministry is considering increasing the foreign institutional investment (FII) limit in the local debt market which will be a positive development for foreign flows. However, the market is worried as there are concerns on the debt problems in Europe and fears of further tightening in China.

Forecast:

Inflows are expected to be moderate next three months



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. India's merchandise exports expanded in March at the fastest pace in six years at 54.1 percent in dollar terms as the global economic recovery boosted demand for Indian goods. This is in spite of the Indian rupee strengthening for the fourth month in April in a row. It increased by 36.9 per cent in rupee terms. The growth in exports was 34.8 percent per annum in dollar terms in February 2010. The big jump in exports growth can also be attributed to the statstical base effect. Indian exports are gaining as consumer demand improves in the U.S. and Europe. However, apart from the recent Euro Zone crisis, the fixed Yuan remains a worry as China is a big trading partner as well as a competetor. As the global economic outlook is improving, it is expected that the exports would grow further but at a slower rate in the next three months.

High growth of Exports and Imports

The government is reviewing to extend incentives to a few selected sectors like engineering goods, electronics, handicrafts, carpets and cotton yarn which saw drop in shipments. This appears to be necessary, especially, in view of the recent Euro Zone crisis. The crisis ridden economies of Spain, Portugal and Greece account for about four percent of India's exports.

India's imports grew at a whooping 67.1 percent in dollar terms in March, 2010 due to a steep increase in oil import bill. However, due to the appreciation of rupee it increased by 48.4 per cent in rupee terms. Oil imports during March, 2010 was 85.2 percent higher than oil imports n the corresponding period last year as the oil prices increased in the world market. The trend is likely to continue in the medium term assuming the euro zone problem gets resolved in the short run. Non-oil imports during March, 2010 were 61.0 per cent higher than non-oil imports in March, 2009. This shows the demand side is picking up due to the recovery process in the economy.

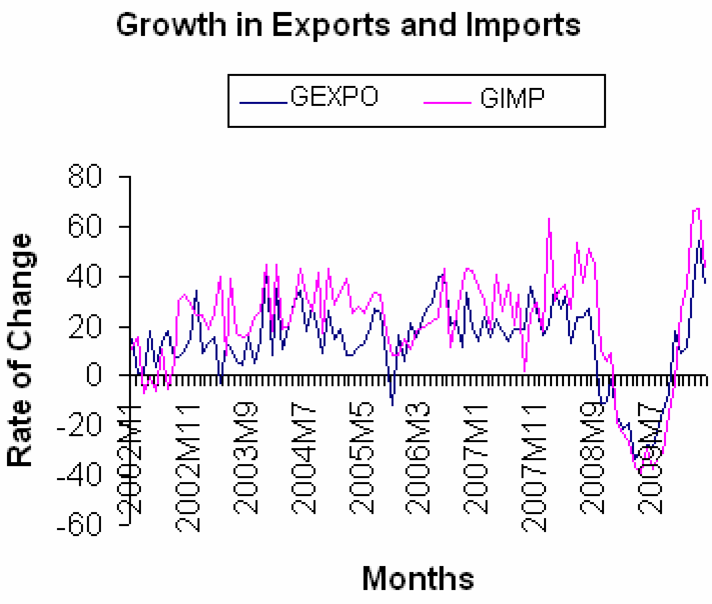
Textiles and jewelry are the main contributor of Export

The quick estimates of growth of exports and imports as reported in press for April 2010 are 36.2 percent and 43.3 percent, respectively. The surge in the external demand for cars, gems and Jewelry, and textiles mainly contributed to the exports growth.

Though the trade deficit has widened in the month, for April 2009- March, 2010 over the corresponding period last year, it has declined slightly as export declines were less steep in relative terms in earlier months The larger positive trend in imports has resulted in widening of trade deficit and, even though, both exports and imports are forecasted to increase at slower rates in the next three months, the deficit is predicted to increase further.

Forecast:

Exports growths are forecasted as 38.96%, 34.61 % and 33.34% for, May, June and July 2010 respectively. Imports are expected to increase by 49.98%, 45.68% and 48.63% for May , June and July 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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