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Dun & Bradstreet's Macro Economic Forecasts

	Forecast	Latest Period
Inflation W.P.I	9.5%-9.7% Aug-10	9.97%Jul-10
Inflation C.P.I (I.W)	13.3%-13.5% Jul-10	13.73% Jun-10
INR/US\$	46.30-46.50 Aug-10	46.84 Jul-10
I.I.P Growth	8.0%-9.0% Jul-10	7.13% Jun-10
15-91 day's T-Bills	5.4%-5.6% Aug-10	5.43% Jul-10
10 year G-Sec yield	7.7%-7.9% Aug-10	7.70% Jul-10
Bank Credit*	19.8%-20.0% Aug-10	19.7% Jul-10

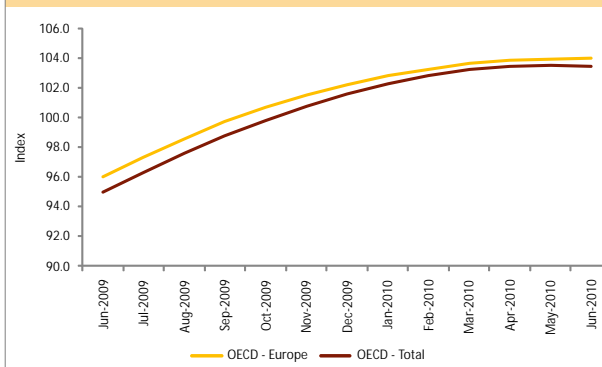
All figures are monthly averages

*Refers to End period

Dun & Bradstreet's GDP Forecasts

	Forecast (Q1 FY11)	Latest Period (Q4 FY10)
GDP	8.7	8.6
Agriculture	2.7	0.7
Industry	10.7	13.3
Services	9.3	8.4

Composite Leading Indicators (CLIs)



Source: OECD

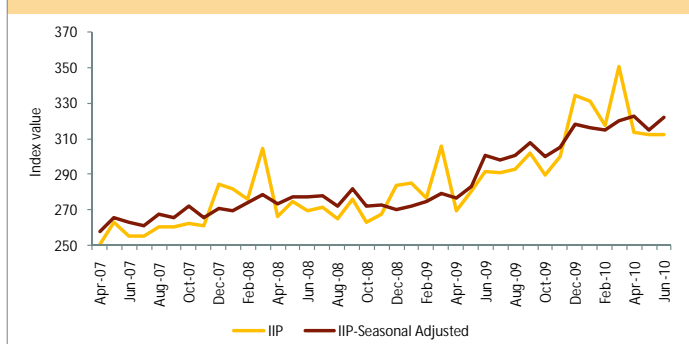
Given the persistent inflationary pressures along with strong performance of various macroeconomic indicators, the recent policy rate hike by the RBI was widely anticipated. Nonetheless, the 50 bps hike in the reverse repo rate was above expectations. The hike in policy rates has induced many banks to increase their lending rates given that the demand for bank credit is marching upwards following the strong economic activity. This, in turn, is expected to help in containing the demand side pressures that are likely to surface once domestic demand strengthens. The rise in lending rates, however, is unlikely to hamper investment activity given the improvement in the private investment coupled with Government's thrust on investment in infrastructure sector. The deposit rates are also expected to increase further as the banks compete to attract deposits, thereby inducing people to increase their savings with banks. Nonetheless, given the current liquidity shortage which is expected to be temporary, the hike in the reverse repo rate will have limited impact in the near term. However, it will help in absorbing excess liquidity from the banking system once the liquidity conditions go back to surplus.

The lagged impact of monetary tightening measures by the RBI along with waning base effect, better prospects of agricultural output in anticipation of normal monsoon and relatively low level of international commodity prices are expected to ease off inflationary pressures after Sep-10. D&B expects the WPI inflation to moderate to 6.5% by end-December 2010. However, given the deregulation of oil prices, the pace of moderation in the headline inflation is expected to be slightly slow. Moreover, the output gap which is expected to remain positive during the first half of the current fiscal with the actual output marginally exceeding the potential output, will lead to inflationary pressures in the economy. Hence, despite some moderation in the WPI inflation by Dec-10, the RBI is expected to continue with its tight monetary policy. D&B expects further hike in repo and reverse repo rates by 25 bps each and CRR by 50 bps during the current fiscal in order to contain inflationary expectations going forward.

Further, the widening interest rate differentials between India and major advanced economies along with strong domestic growth prospects are expected to attract foreign capital inflows, thereby adding to liquidity pressures further. Hence, the future monetary policy measures would be calibrated to contain any excess liquidity pressures in order to anchor inflationary expectations.

Real Economy

High Base effect moderating the IIP growth



Source: CSO, D&B India

- The IIP growth moderated to a single digit level of 7.1% (y-o-y) during Jun-10, after recording double digit growth for eight consecutive months.
- Growth in index of six core-infrastructure industries, having a combined weight of 26.7% in IIP, moderated to 3.4% (y-o-y) during Jun-10 as against 6.3% during Jun-09.
- Growth in mining, manufacturing and electricity moderated to 9.5%, 7.3% and 3.5% respectively during Jun-10 as compared to 14.2%, 8.0% and 8.0% during Jun-09.
- The capital goods sector grew by 9.7% (y-o-y) during Jun-10, lower compared to the high growth of 34.2% registered during May-10.

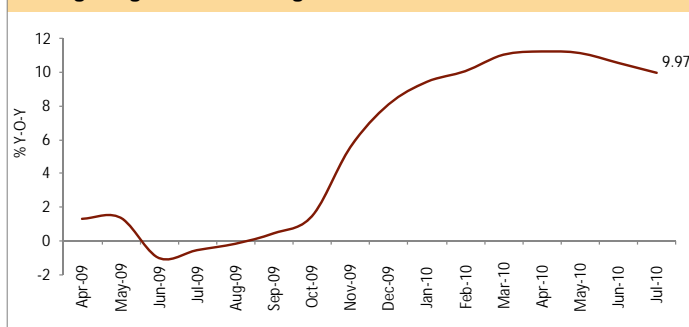
	Forecast	Actuals	
		Latest Period	Previous Period
I.I.P Growth	8.0%-9.0% Jul-10	7.13% Jun-10	11.34% May-10

Industrial activity continued to consolidate with IIP growth moderating for second consecutive month. Release of pent-up demand of the crisis period, re-stocking of inventories, which had been drawn-down by the companies during the crisis, had stimulated the IIP growth in the last few months. The impact of these factors on the industrial production has probably phased away leading to consolidation of the industrial activity. The single digit growth of 7.1% is also a result of high base of the previous year when the IIP had grown by 8.3% (compared to 2% in May-09). The IIP number increased significantly during Jun-09, marking the upturn in production cycle as the Indian economy was emerging from the global slowdown, defying the usual seasonal pattern of lower industrial activity in June compared to May.

The current moderation in the IIP numbers even underscores the impact of usual seasonal slowdown on industrial production. Lower production of coal & cement industries (which generally witnesses moderation during the monsoon season) has weighed down the overall growth in six infrastructure industries. IIP growth is likely to remain around the current level in the next few months as the industrial production continues to consolidate further and the impact of high base effect begins to play out. Going forward, relatively slower pace of growth in IIP is inevitable, but it would be more sustainable.

Price Scenario

The WPI inflation moderates to single digit level due to waning low base effect



Source: Ministry of Commerce

- The WPI inflation for the month of Jul-10 moderated to single digit level at 9.97% (y-o-y) as against 10.55% during Jun-10.
- Inflation in primary articles, though registered some moderation, continued to remain elevated at 14.94% during Jul-10 due to higher prices of primary food articles and significant rise in prices of non-food articles & minerals.
- Inflation in fuel group stood at 14.29% during Jul-10 as against 14.32% during Jun-10.
- Inflation in manufactured products moderated to 6.15% during Jul-10 as against 6.66% during Jun-10.

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Inflation C.P.I (I.W)	13.3%-13.5% Jul-10	13.73% Jun-10	13.91% May-10

All figures are monthly averages

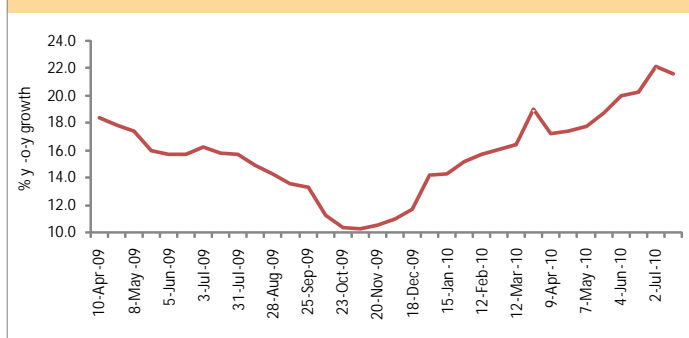
With waning low base effect and significant moderation in the prices of primary food articles, the WPI inflation figures for Jul-10 moderated to single digit level. Inflation in manufactured products also eased marginally due to some moderation in prices of manufactured food products and non-metallic mineral products.

The WPI inflation is expected to moderate further after Sep-10 given the high base effect which is expected to set in after Sep-10, the lagged impact of monetary tightening by the RBI and prospects of better agriculture production in anticipation of normal monsoon during this season. However, the pace of moderation in headline inflation is expected to be slow given the recent hike in fuel prices. D&B expects the WPI inflation to moderate to 6.5% by end-December 2010.

Although inflationary pressures are expected to ease off to certain extent after Sep-10, given that demand side pressure are likely to surface once domestic demand strengthens, the RBI is expected to continue with its monetary tightening during the current fiscal. D&B expects further hike in repo and reverse repo rate by 25 bps each and CRR by 50 bps during current fiscal in order to contain inflationary expectations without impacting growth momentum.

Money & Finance

Growth in Non-food Bank Credit Gathering Pace



Source: RBI

- The Repo rate under the Liquidity Adjustment Facility (LAF) increased by 25 basis points from 5.5% to 5.75% with effect from 27-Jul-10.
- The Reverse Repo rate under the Liquidity Adjustment Facility (LAF) increased by 50 basis points from 4.0% to 4.5% with effect from 27-Jul-10
- RBI revised its GDP growth forecast for FY11 upwards to 8.5% from 8.0% and WPI projection by end-March 2011 upwards to 6.0% from 5.5%.
- Non-food credit extended by Schedule Commercial Banks (SCBs) increased by 19.94% (y-o-y) outstanding as on 31-Jul-10 as compared with an increase of 15.82% in the year-ago period.

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		Latest Period	Previous Period
15-91 day's T-Bills	5.4%-5.6% Aug-10	5.43% Jul-10	5.23% Jun-10
10 year G-Sec yield	7.7%-7.9% Aug-10	7.70% Jul-10	7.39% Jun-10
Bank Credit*	19.8%-20.0% Aug-10	19.7% Jul-10	21.7% Jun-10

All figures are monthly averages

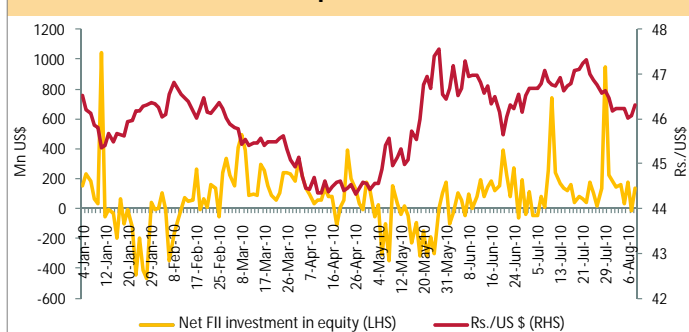
*Refers to End period

Continuing its move towards normalisation of the policy rates, the RBI increased the repo and reverse repo rates by 25 bps and 50 bps respectively. A more than proportionate hike in the reverse repo rates is expected to ensure that the rate at the lower end of the LAF corridor remains at a higher level when liquidity conditions go back to surplus, thereby aiding efficient liquidity management. With the hike in policy interest rates, many banks increased their lending rates. Even the deposit rates have been on a rise as the banks compete to attract deposits, which have witnessed some moderation in the recent past. High interest rate scenario, going forward, might have some moderating impact on bank credit demand, which began to gain momentum in the last few months.

The normalisation of policy interest rates is expected to continue given that the demand side pressures to inflation would surface as domestic demand gathers strength. Mounting inflationary pressures could pose significant downside risk to growth and hence, anchoring inflationary expectations would remain at the forefront of the monetary policy agenda. D&B expects further hike in repo and reverse repo rates by 25 bps each and CRR by 50 bps during current fiscal in order to contain inflationary expectations going forward.

External Sector

Volatile inflows render Rupee volatile



Source: SEBI & RBI

- India's exports for the month of Jun-10 stood at US\$ 17.74 bn, registering a growth of 30.42% (y-o-y), while imports grew by 22.97% (y-o-y) to US\$ 28.29 bn during the same month.
- Oil imports recorded an increase of 26.5% (y-o-y) and stood at US\$ 8.35 bn during Jun-10. Non-oil imports grew by 21.5% (y-o-y) to US\$19.95 during Jun-10.
- Trade deficit amounted to US\$ 10.55 bn during Jun-10 taking the trade deficit for the Q1 FY10 to US\$ 32.27 bn.
- Rupee continued to be volatile during the month of Jul-10 and stood at 46.58 per US\$ on 13-Aug-2010.

	Forecast	Actuals	
		Latest Period	Previous Period
INR/US\$	46.30-46.50 Aug-10	46.84 Jul-10	46.56 Jun-10

All figures are monthly averages

The moderation in imports growth to 22.97% during Jun-10 as compared to 38.53% in May-10 could in part be attributed to base effect of the previous year. With the domestic economic activity gaining traction the imports are expected to remain strong in the next few months. On the other hand, exports growth is expected to see some moderation in the medium term, though it would remain resilient. Concerns over growth of Euro area and US economies, which are our major export destinations, is expected to weigh on the demand for Indian exports.

In the forex market, the rupee is expected to remain volatile given the confluence of factors exerting positive as well as negative influences on the rupee value. Increasing interest rate differential coupled with strong growth prospects of the domestic economy, which could attract foreign investment, are expected to exert upward pressure on the rupee value. However, at the same time the increased concerns about the growth prospects of the Euro area and US might result in increased risk aversion, in turn weighing down the rupee value. In the long term, D&B expects positive factors to weigh over the negative factors in turn aiding the rupee to appreciate.

Please send your feedback to Dr Arun Singh, Senior Economist.

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