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Dun & Bradstreet's Macro Economic Forecasts

	Forecast	Latest Period
Inflation W.P.I	10.0%-10.3% Jun-10	10.16% May-10
Inflation C.P.I (I.W)	14.0%-15.0% May-10	13.33% Apr-10
INR/US\$	46.50-46.90 Jun-10	45.80 May-10
I.I.P Growth	14.5%-15.5% May-10	17.60% Apr-10
15-91 day's T-Bills	4.5%-4.8% Jun-10	4.13% May-10
10 year G-Sec yield	7.5%-7.7% Jun-10	7.39% May-10
Bank Credit*	17.5%-18% Jun-10	18.1% May-10

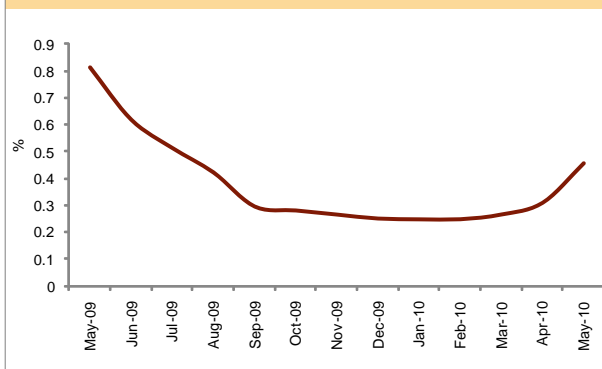
All figures are monthly averages

*Refers to End period

Dun & Bradstreet's GDP Forecasts (% y-o-y growth)

	Forecast (Q1 FY11)	Latest Period (Q4 FY10)
GDP	8.4	8.6
Agriculture	1.0	0.7
Industry	11.9	13.3
Services	8.7	8.4

3-month LIBOR started to rise



Source: British Bankers' Association

The strong growth clocked by IIP and GDP figures are significant developments and bodes well for the overall economic activity going forward. While the broad-based recovery in the manufacturing sector coupled with the substantial rise in investment since last few months are the promising aspects of these macroeconomic indicators, a strong recovery in the private consumption expenditure is warranted to ensure sustainability of the current growth momentum.

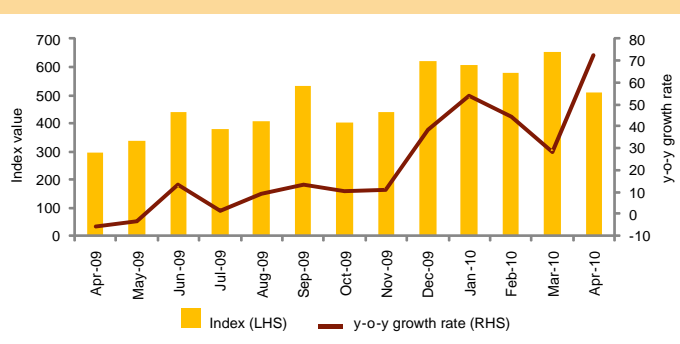
Even as various macroeconomic indicators confirm that the Indian economy is set on the recovery path, the elevated level of inflation and European debt crisis, could pose significant downside risks to growth. Although, better monsoon prospects might help in bringing down food articles inflation, high input costs, which if persists, could fan further inflationary pressures in the economy. However, D&B expects inflation rate to moderate after Sep-10, once base effect starts waning, and reach 5% by Dec-10 and 2.5% by Mar-11. While current inflationary pressures along with the significant growth in IIP builds a case for the RBI to hike policy rates, unfolding European debt crisis and its possible contagion impact might lead the RBI to adopt cautious approach in terms of further monetary tightening before the next monetary policy review. However, in the first quarter policy review during July 2010, D&B expects that the RBI would increase repo and reverse repo rates by around 25 basis points, while maintaining CRR constant.

The recent European debt crisis though has had no direct implications for the Indian economy, if prolonged and widespread could pose significant downside risks to exports growth going forward. Besides, increased risk aversion amongst foreign investors as well as weakening of Euro against US Dollar has led to higher volatility in the rupee value. After appreciating to 44.33 per US\$ (as on 26-Apr-10), the rupee depreciated to eight-month low of 47.57 per US\$ (as on 26-May-10). This, in turn, has made exchange rate risk management difficult for both exporters as well as importers.

In the coming months, growth in exports largely hinges on the further developments regarding the European debt crisis as well as the pace of recovery in the US economy. On the domestic front, there might be some moderation in next quarter's growth figures as it will be coming on a high statistical base. Nonetheless, the timely and widespread distribution of monsoon will provide support to the private consumption demand, thereby aiding overall economic growth.

Real Economy

Bouyant activity in the capital goods sector



Note: Data pertains to IIP for capital goods sector
Source: CSO

- India's GDP grew by 8.57% (y-o-y) during Q4 FY10 as compared to 6.53% during the previous quarter. While agriculture sector witnessed an increase 0.69% during Q4 FY10, the industry & services sectors grew by 13.27% & 8.43% respectively during the same quarter.
- Private final consumption expenditure during Q4 FY10 remained muted at 2.65% (y-o-y) as compared to 5.09% during Q4 FY09.
- The IIP grew by 17.60% (y-o-y) in Apr-10 as against 1.13% in Apr-09; base year effect in play.
- The capital goods sector marked a surprise growth of 72.83% during Apr-10. The consumer durables sector continued to register a strong growth of 36.96% during Apr-10 as against an increase of 17.60% during Apr-09.

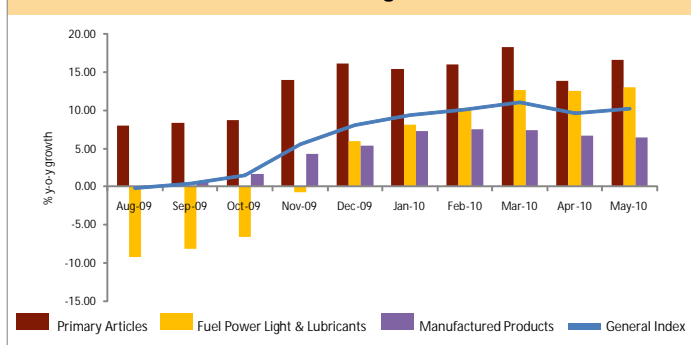
	Forecast	Actuals	
		Latest Period	Previous Period
I.I.P Growth	14.5%-15.5% May-10	17.60% Apr-10	13.93% Mar-10

The GDP clocked a strong growth rate of 8.6% during Q4 FY10 backed by a robust performance in the industrial segment indicating that the economy has firmly set its foothold on the growth path. The good output in the Rabi crop has helped the agriculture sector to post a positive growth rate during the fourth quarter. If the monsoon turns out to be normal it will further push the growth rates in the agriculture sector. While the services sector still remains below the double digit growth rates the continued strong growth recorded in the industrial production led by the capital goods augurs well for the overall economic activity going ahead. The 72.8% (y-o-y) growth in the capital goods sector during Apr-10 has come as a surprise. While low statistical base might have contributed to this jump, the impact of pent-up investment demand cannot be ruled out. Given the seasonal nature of IIP data, capital goods index value should have fallen more than 200 points from Mar-10 index value as compared to actual 144 points.

The composition wise GDP shows that the private demand conditions remain muted and given that, government does not have enough room for further stimulus measures going forward (due to surging fiscal deficit), a strong pick in the private demand is warranted to continue the growth path especially in the event of the European debt crisis.

Price Scenario

Headline Inflation touches double digit level



Source: Ministry of Commerce

- The WPI inflation surged to a double digit level of 10.16% during May-10 on account of substantial increase in primary articles and fuel group inflation.
- Inflation in primary articles surged to 16.60% during May-10 as compared to 13.88% in the previous month as inflation in the non-food articles and minerals grew by 18.60% and 8.30% during May-10 as compared to 10.53% and -6.84% during Apr-10, respectively.
- Surge in non-food articles inflation has been primarily driven by significant rise in prices of sugarcane (53.24% y-o-y)
- Primary food articles inflation witnessed some moderation though at elevated levels of 16.49%.
- Inflation in the manufactured products continued to moderate and stood at 6.41% during May-10 as compared to 6.70% during Apr-10.

	Forecast	Actuals	
		Latest Period	Previous Period
Inflation W.P.I	10.0%-10.3% Jun-10	10.16% May-10	9.59% Apr-10
Inflation C.P.I (I.W)	14.0%-15.0% May-10	13.33% Apr-10	14.86% Mar-10

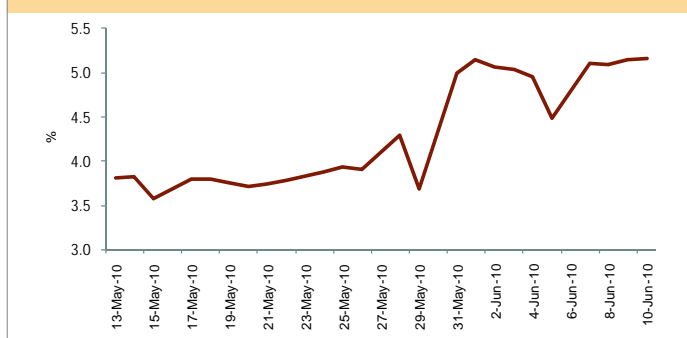
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An expected better rabi production coupled with anticipated normal monsoon, which has increased the prospect of better agriculture production are likely to ease off pressures on the food prices going forward. The food article inflation, which remained at elevated levels in the previous fiscal, is likely to start abating in the near future. Moreover, during May-10 commodity prices across the world have seen some corrections compared to the previous month and if it continues would augur well for the Indian inflation scenario. Average petroleum spot prices which had hovered around US\$ 84.2/bbl during Apr-10 have moderated to US\$ 75.8/bbl during May-10. D&B expects inflation rate to moderate after Sep-10, once the base effect starts waning, and will reach 5% by Dec-10 and 2.5% by Mar-11.

However, some upside risks do persist and would call for timely policy interventions going forward. Demand side pressures to inflation are likely to surface, as domestic demand gathers strength in the medium term. D&B expects monetary policy action to be tightened further to tackle any demand side pressures. In the first quarter policy review, D&B expects that the RBI would increase repo and reverse repo rates by around 25 basis points. Moreover, the decision on deregulation of fuel prices in response to under-recoveries for oil PSUs is likely to be taken in the near future and will add to the inflationary pressures.

Money & Finance

Call rates hover near the RBI's Repo Rate of 5.25%



Source: Clearing Corporation of India

- Scheduled commercial banks may avail of additional liquidity support under the LAF to the extent of up to 0.5% of their net demand and time liabilities (NDTL). For any shortfall in maintenance of SLR arising out of avilment of this facility, banks may seek waiver of penal interest purely as an ad hoc, temporary measure. This facility will be available till 2-Jul-10.
- Growth in bank credit increased by 18.1% (y-o-y) as on 28-May-10 as compared to 17.6% (y-o-y) as on 30-Apr-10.
- Call rates remained within the range of 5.00% and 5.16% during 31-May-10 and 10-Jun-10.

	Forecast	Actuals	
		Latest Period	Previous Period
15-91 day's T-Bills	4.5%-4.8% Jun-10	4.13% May-10	3.79% Apr-10
10 year G-Sec yield	7.5%-7.7% Jun-10	7.39% May-10	7.05% Apr-10
Bank Credit*	17.5%-18% Jun-10	18.1% May-10	17.6% Apr-10

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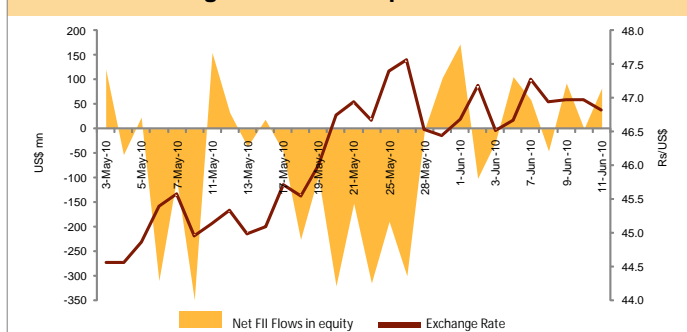
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Conditions of liquidity tightening have emerged in the banking system with the call rates firming up near the RBI's repo rate of 5.25%. Spectrum auction, high government borrowing coupled with advance tax payments and the high credit borrowing by the corporates to meet the pent up investment demand are likely to have led to this scenario. Moreover, FII outflows triggered by the risk aversion amongst foreign investors due to the ongoing financial crisis in some European countries have also affected liquidity conditions in the market. Although these liquidity pressures could be considered to be temporary in nature these are likely to impact the bond market and also lead to an increase call money rates as the banks face liquidity pressures.

In order to ensure that the credit demand does not get affected the RBI has reduced the SLR (the portion of a bank's deposits required to be invested in government bonds) by 0.5%. Given the tight liquidity conditions in the domestic markets D&B expects the RBI to maintain a status quo on the CRR front in the policy review. However, D&B expects that RBI would increase repo and reverse repo rates by around 25 basis points given the current inflationary conditions and robustness in the industrial activity.

External Sector

FII outflows weighs down the rupee value



Note: (+) implies FII inflows and (-) implies FII outflows

Source: SEBI, RBI

- India's exports for the month of Apr-10 stood at US\$ 16.89 bn, registering a growth of 36.22% (y-o-y), while imports grew by 43.33% (y-o-y) to US\$ 27.31 bn during the same month.
- Oil imports increased by as much as 70.5% to US\$ 8.08 bn, while non-oil imports grew by 34.3% during Apr-10 to US\$ 19.23 bn during the same month.
- Trade deficit amounted to US\$ 10.42 bn during Apr-10 as against US\$ 6.65 bn during Apr-09.
- The rupee depreciated to eight-month low of 47.57 per US\$ as on 26-May-10. Between the period 11-May-10 to 11-Jun-10, the rupee depreciated by almost 1 rupee and 68 paise.

	Forecast	Actuals	
		Latest Period	Previous Period
INR/US\$	46.50-46.90 Jun-10	45.80 May-10	44.50 Apr-10

All figures are monthly averages

The recent Greek debt crisis, if prolonged and spread to other European countries, can pose significant downside risks to exports growth and hence is likely to remain an area of concern in the near future. Europe is the major exports destination for India and worsening of the crisis in Europe could dampen demand for India's exports which is beginning to see some signs of revival.

Another emerging concern pertains to higher volatility in the rupee value since last few weeks, which has made exchange rate risk management difficult. After appreciating for some time during Apr-10, the rupee witnessed sharp depreciation towards the end of May-10. The rise in risk aversion amongst foreign investors due to the ongoing European debt crisis has led to significant foreign capital outflows, resulting in the depreciation of the rupee vis-à-vis US Dollar. Given the increased risk aversion amongst foreign investors coupled with high pace of growth in imports as against in exports, the rupee is expected to remain weak against US Dollar in the near future. However, as the uncertainty surrounding the Euro zone debt crisis subsides, India is expected to witness resumption in foreign fund inflows, leading to the appreciation of the rupee in the medium to long term.

Please send your feedback to Yashika Singh, Head-Operations, Economic Analysis Group

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