



Decide with Confidence

View from the top

Dun & Bradstreet's Macro Economic Forecasts

	Forecast	Latest Period
Inflation W.P.I	8.0%-8.2% Oct-10	8.62% Sep-10
Inflation C.P.I (I.W)	9.7%-9.9% Sep-10	9.88% Aug-10
INR/US\$	44.30-44.50 Oct-10	46.06 Sep-10
I.I.P Growth	6.0%-7.0% Sep-10	5.57% Aug-10
15-91 day's T-Bills	6.0%-6.2% Oct-10	5.83% Sep-10
10 year G-Sec yield	7.9%-8.1% Oct-10	8.10% Sep-10
Bank Credit*	19.0%-19.2% Oct-10	19.0% Sep-10

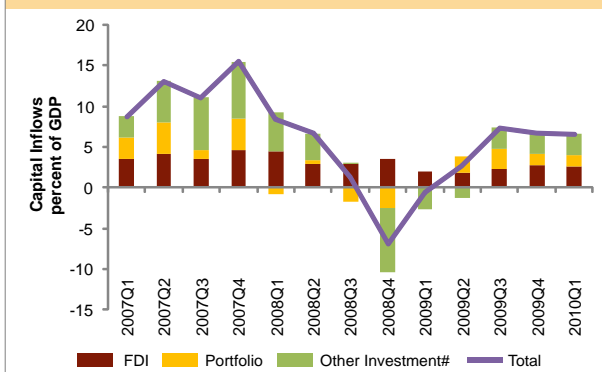
All figures are monthly averages

*Refers to End period

Dun & Bradstreet's GDP Forecasts

	Forecast (Q2 FY11)	Latest Period (Q1 FY11)
GDP	8.5	8.8
Agriculture	4.2	2.8
Industry	10.2	10.3
Services	8.6	9.7

Capital Inflows in Emerging Asia*



* Emerging Asia: China, Hong Kong SAR, India, Indonesia, Korea, Malaysia, Philippines, Singapore, Taiwan Province of China, and Thailand.

Other investment includes financial derivatives.

Source: IMF

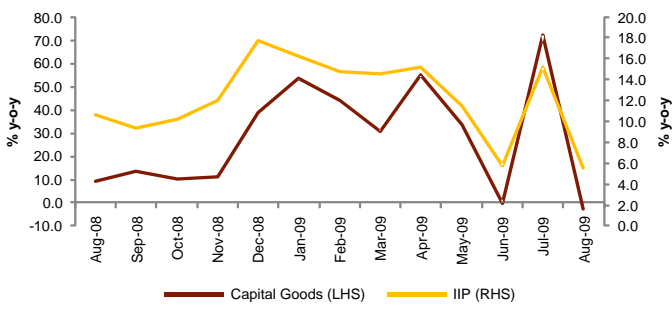
After recording a double digit growth of 11.9% during Apr-Jul 10, a single digit growth of 5.6% in IIP was definitely disappointing and below our expectations. While all the major categories in IIP witnessed some moderation, a decline in capital goods production was more significant as it pulled down the overall IIP by almost 4%. Growth in capital goods sector has been volatile since past three months. On the other hand, intermediate and basic goods sectors have witnessed sustained growth which augurs well for the overall industrial activity going forward. Growth in consumer durables has also been strong for past few months and is in part indicative of improving domestic demand. While the significant volatility in IIP growth, especially capital goods production, has raised concerns regarding the robustness of the current recovery, improved performance of some lead indicators such as non-oil imports, commercial vehicle production, and resource mobilisation in primary capital market strengthens the case for sustainability of the current growth momentum. Moreover, the impressive performance of D&B's composite Business Optimism Index (BOI) for Oct-Dec 2010 reflects optimism regarding the future business conditions.

The headline inflation, though moderated to single digit, continues to remain far above the RBI's tolerance level. The RBI has already hiked key policy rates in an attempt to anchor inflationary expectations in the economy. The lagged impact of these monetary tightening measures by the RBI along with waning low base effect and better prospects of agricultural output given the substantial improvement in area sown under Kharif crop during this season are expected to ease off inflationary pressures during the second half of the current fiscal. With the headline inflation expected to taper in the coming months and normalisation of policy interest being almost complete, the RBI might maintain a status quo in terms of repo and reverse repo rates in the forthcoming monetary policy review. However, the RBI might increase the CRR by around 25 bps in the near future to limit any excess liquidity pressures from surfacing, at the backdrop of current surge in foreign fund inflows.

The widened interest rate differentials between India and major global economies along with strong domestic growth prospects have led to strong foreign capital inflows to India in past few months. However, though the net FII inflows to India are expected to remain strong in FY11 as compared to the crisis period, it is not expected to touch the pre-crisis level given the slow pace of recovery in major global economies.

Real Economy

Fluctuating capital goods production renders IIP volatile



Source: CSO

- As per the first advance estimate of production of foodgrains for 2010-11, the total kharif production is 114.63 million tonnes better than 103.84 million tonnes in 2009-10, which was a drought year; however, it is lower than 2008-09, which was a normal year.
- The IIP growth moderated to a single digit level of 5.6% (y-o-y) during Aug-10, after recording a robust growth of 15.2% during Jul-10.
- Growth in index of six core-infrastructure industries, having a combined weight of 26.7% in IIP, moderated to 3.7% (y-o-y) during Aug-10 from 4.0% during Jul-10.
- Growth in mining, manufacturing and electricity stood at 7.0%, 5.9% and 1.0% respectively during Aug-10.

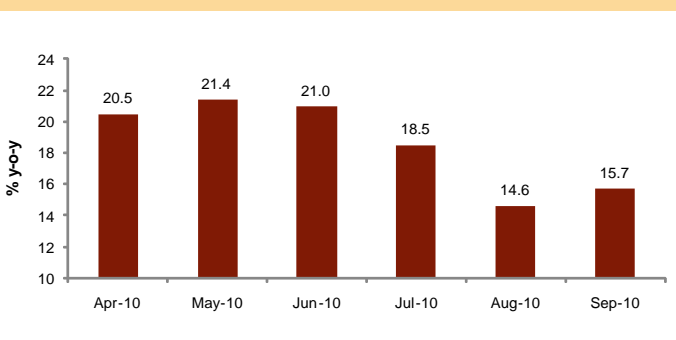
	Forecast	Actuals	
		Latest Period	Previous Period
I.I.P Growth	6.0%-7.0% Sep-10	5.57% Aug-10	15.20% Jul-10

The IIP numbers for Aug-10 are definitely below our expectations; however, the trend in IIP for the next few months needs to be observed before raising any signs of caution. The dynamics in the production of some components of the capital goods sector has been playing a significant role in the recent volatility seen in the overall IIP numbers. Moreover, performance of the intermediate and basic goods sectors has remained resilient and augurs well for the overall industrial activity going forward. IIP for consumer durables has also shown robust growth for past few months and is in part indicative of improving demand conditions. The advent of the festive season is likely to have supported the consumer durables production. Further, better prospect of agriculture sector is also likely to stimulate demand in the domestic economy. Moderating inflation and expected revival in rural demand might aid the consumer non-durables sector in the medium to long term period.

Expected improvement in domestic demand conditions coupled with sustained infrastructure investment is likely to support overall industrial activity going forward. Nonetheless, muted exports demand might limit the growth in the manufacturing industries. Going forward, although growth in IIP is expected to remain in single digit, it is expected to average at 8.5% during H2 FY11 above the 5.6% growth recorded in Aug-10.

Price Scenario

Prices of primary food articles continue to remain elevated



Source: Ministry of Commerce & Industry

- The Wholesale Price Index (WPI) for all commodities rose by 8.6% (y-o-y) during Sep-10 as against 8.5% in the previous month.
- Inflation in primary articles continued to remain elevated at 17.45% during Sep-10 due to high prices of primary food articles particularly fruits & vegetables.
- Inflation in fuel group moderated to 11.1% during Sep-10 as against 12.6% during Aug-10 due to substantial moderation in mineral oils inflation.
- Inflation in manufactured products also eased marginally to 4.6% during Sep-10 as compared to 4.8% during Aug-10.

	Forecast	Actuals	
		Latest Period	Previous Period
Inflation W.P.I	8.0%-8.2% Oct-10	8.62% Sep-10	8.51% Aug-10
Inflation C.P.I (I.W)	9.7%-9.9% Sep-10	9.88% Aug-10	11.25% Jul-10

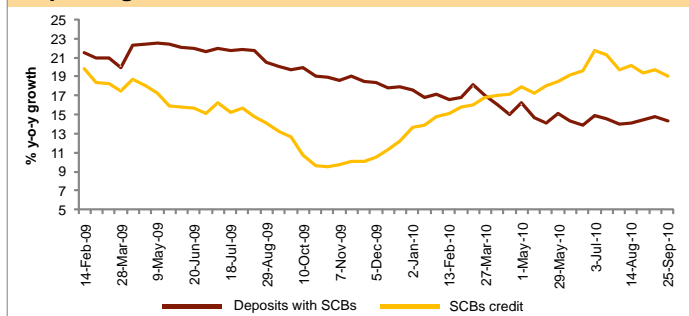
All figures are monthly averages

The WPI inflation that was in double digits during Mar-Jul 10 has witnessed some moderation in past few months. The headline inflation is expected to moderate further owing to the waning low base effect and the lagged impact of monetary tightening measures taken by the RBI in the first half of the current fiscal. Prices of primary food articles which were at an alarmingly high level in the first half of FY11 are also expected to witness some moderation given the better prospects of agricultural output consequent to the substantial improvement in area sown under Kharif crop during this season. This will help in further easing the inflationary pressures in the economy. The headline inflation is expected to be around 6.5% by end Dec-10 and further moderate to 3.5% by end March-11.

In view of expected moderation in the WPI inflation in the coming months and some consolidation seen in IIP growth, the RBI is not expected to raise policy interest rates in the forthcoming policy review. Nonetheless, the RBI might increase the CRR by around 25 bps in the near future to limit any excess liquidity pressures from surfacing, at the backdrop of current surge in foreign fund inflows.

Money & Finance

Raising interest rates expected to support muted deposit growth



Source: RBI

- The Government of India (GOI) increased the current limit of Foreign Institutional Investors (FII) investment in Government securities by US\$ 5 bn, raising the cap to US\$ 10 bn and the incremental limit of US\$ 5 bn be invested in securities with residual maturity of over 5 years.
- The GOI increased the current limit of FII investment in corporate bonds by US\$ 5 bn raising the cap to US\$ 20 bn and the incremental limit of US\$ 5 bn be invested in corporate bonds with residual maturity of over 5 years issued by companies in infrastructure sector.
- The GOI reduced its borrowing requirement for the H2 FY11 by Rs. 100 bn, aided by the windfall revenues through auction of telecom spectrum and robust tax revenues

	Forecast	Actuals	
		Latest Period	Previous Period
15-91 day's T-Bills	6.0%-6.2% Oct-10	5.83% Sep-10	5.63% Aug-10
10 year G-Sec yield	7.9%-8.1% Oct-10	8.10% Sep-10	8.11% Aug-10
Bank Credit*	19.0%-19.2% Oct-10	19.0% Sep-10	19.4% Aug-10

All figures are monthly averages

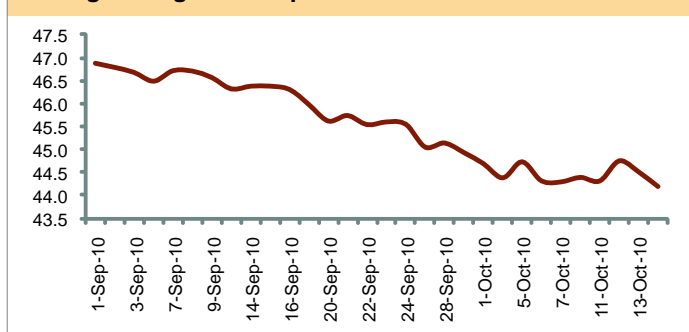
*Refers to End period

Continuing the normalisation of policy interest rates, the RBI increased the repo and reverse repo rates by 25 bps and 50 bps respectively during the mid-quarter review of monetary policy. Consequent to this policy action, many banks have raised their deposit and lending rates. While raising interest rates are likely to aid deposit growth in the near term, it might have a moderating impact on credit demand. High lending rates, however, are unlikely to have a major impact on investment demand given the easy availability of funds from other non-bank sources.

Liquidity conditions are expected to remain tight in the next few weeks given the forthcoming IPO issue of a major public sector company. However, subsequently the liquidity conditions might improve in case the RBI intervenes in the forex market to cap the rapidly raising rupee value. In an attempt to limit any excess liquidity pressures from surfacing, at the backdrop of current surge in foreign fund inflows, the RBI might increase the CRR by around 25 bps points in the near future. However, with inflation expected to taper in the coming months and growth momentum showing signs of moderation, we expect that RBI would maintain a status quo on the repo and reverse repo front in the forthcoming mid-term policy review.

External Sector

Strengthening of the rupee vis-à-vis US Dollar



Source: RBI

- India's exports grew by 22.5% (y-o-y) to US\$ 16.6 bn during Aug-10, while imports increased by 32.2% to US\$ 29.7 bn during the same month, leading to a trade deficit of US\$ 13.0 bn.
- The higher trade deficit along with the lower invisibles surplus led to widening of the current account deficit for Q1 FY11 to US\$ 13.7 bn, as compared with US\$ 4.5 bn in Q1 FY10.
- With net foreign capital flows being higher than the current account deficit, the overall balance of payment was in surplus at US\$ 3.7 bn during Q1 FY11.
- The robust FII inflows in equities led to sharp appreciation of the rupee to 44.03 per US\$ as on 15-Oct-10 as against 46.37 per US\$ as on 15-Sep-10.

	Forecast	Actuals	
		Latest Period	Previous Period
INR/US\$	44.30-44.50 Oct-10	46.06 Sep-10	46.57 Aug-10

All figures are monthly averages

With the robust FII inflows in domestic equities, the rupee recorded significant appreciation during Sep-10. Given the strong fundamentals of the Indian economy coupled with widened interest rate differential between India and other developed economies, FII inflows are expected to remain robust in the coming months, leading to further appreciation of the rupee. The stronger rupee vis-à-vis US\$ is likely to be a key concern in the near future as it would affect competitiveness of India's exports which are yet to pick-up completely. The exports realisation will also be adversely affected due to the strong rupee. While sharp appreciation in the rupee is expected to have dampening impact on exports growth, growth in imports might remain strong given the recovery in domestic consumption and investment demand, leading to further widening of trade deficit.

Despite the sharp rupee appreciation, the intervention in the forex market by the RBI through banks has so far been limited as this would lead to excess liquidity pressures in the economy. However, in the event that the rupee continues to rise unabated on the back of robust FII inflows, the RBI might need to intervene in the forex market to cap gains in the rupee.

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

Dun & Bradstreet Information Services India Pvt. Ltd., ICC Chambers, Saki Vihar Road, Powai, Mumbai 400 072
Tel: 91-22-28574190 / 92 / 94 Fax: 91-22-28572060 Email: D&BEconomyObserver@mail.dnb.co.in www.dnb.com