

July 18, 2011

Economic Weekly



Indian Economy

* **WPI Inflation on the rise:** WPI inflation for June 2011 stood at 9.44% YoY compared with 9.06% YoY in May due to rise in the index by 0.9% MoM. WPI inflation for April 2011 was revised to 9.74% YoY from 8.66% YoY. Given the steep revisions of provisional inflation numbers, its is highly probable that the June figures would actually be well above double digits.

* **Money Supply & SCB Credit Growth:** Money Supply (M3) growth improved marginally to 17.10% YoY from 17.08% YoY a fortnight ago as demand and time deposits growth improved during the fortnight ending July 2, 2011. SCB credit growth for the week ending July 2, 2011, declined to 19.90% YoY compared with 21.02% YoY a week ago, as both food and non food credit growth declined. Higher interest rates and moderation in industrial growth has led to decline in SCB credit growth in the last two months .

* **Forex reserves declined marginally to \$314.6 billion:** Forex reserves decreased to \$314.6 billion in the week ending July 9, 2011, due to a fall in foreign currency assets. During the week forex reserves declined by \$1.1 billion to \$314.6 billion.

* **Currency Trends:** Highlights of currency and NIFTY movements last week.

Global Economy

* **US could loose AAA status:** US could face a rating downgrade if it fails to raise its debt ceiling of \$14.29 trillion by August 2, 2011. Debt ceiling debate between Democrats and Republicans has reached a deadlock as Republicans have refused to vote for an increase in the debt ceiling until there is an agreement on the spending cuts to be implemented by the Barack Obama administration. The US debt crisis threatens the financial markets and also the future of the world's largest economy. If US fails to raise the debt ceiling, it might default on a whole host of payments — such as salaries — leading to a debt crisis.

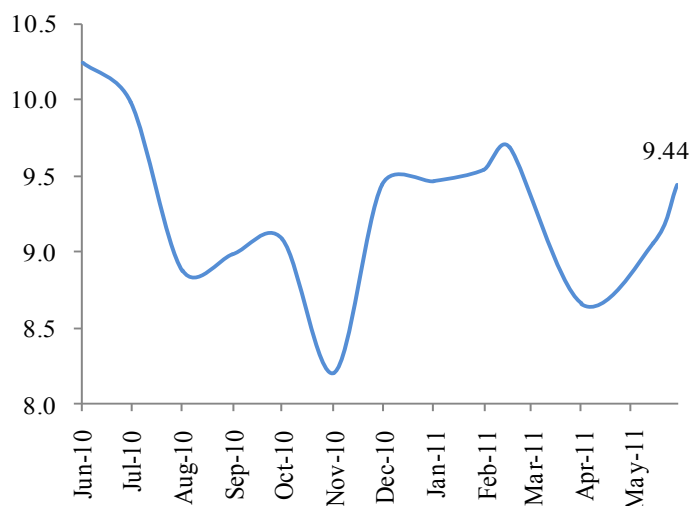
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WPI Inflation for June Surges to 9.44% YoY

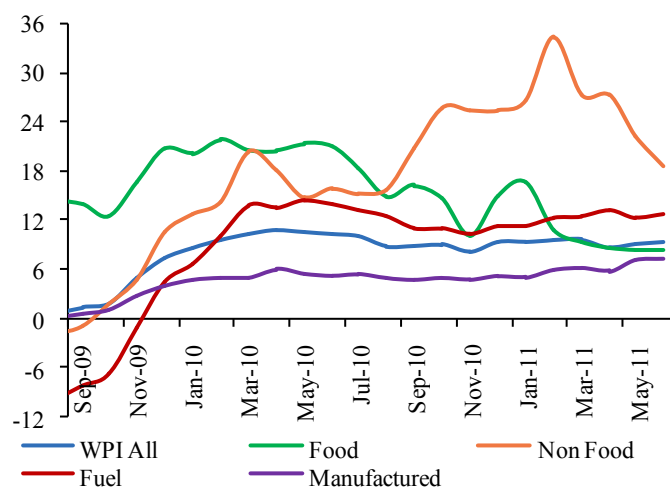
WPI inflation for June 2011 stood at 9.44% YoY compared with 9.06% YoY in May due to rise in the index by 0.9% MoM. Manufactured products prices rose further to 7.43% YoY which reflects the pass through of higher food and fuel prices to core inflation. Primary articles inflation increased to 12.2% YoY compared with 11.3% YoY in May.

- ◆ **Across-the-board jump in prices:** WPI inflation in June rose due to an across-the-board rise in prices, except of non-food articles. Primary articles index grew by 2.8% MoM, fuel index by 0.7% MoM and manufactured products index by 0.10% MoM.
- ◆ **Revised Inflation Situation Even Worse :** WPI inflation for April 2011 was revised to 9.74% YoY from 8.66% YoY. Given the steep revisions of provisional inflation numbers, its is highly probable that the June figures would actually well be in the double digits.
- ◆ **Rate hike likely in coming RBI policy Meet on July 26, 2011:** As inflation threatens the economy with an unrelenting price spiral, and given RBI's anti inflationary stance, we expect a 25 bps hike in benchmark rates in the monetary policy meet on July 26, 2011. The revised inflation scenario makes inflation situation more threatening as it clearly points to double digits levels.
- ◆ **More fuel to fire:** With indirect pass through of higher fuel prices, there are clear more upsides to inflation. As fuel prices impact all walks of life, the indirect impact of recent hike in diesel prices will soon start making itself more evident.

WPI Inflation, % YoY



Monthly Trends, % YoY

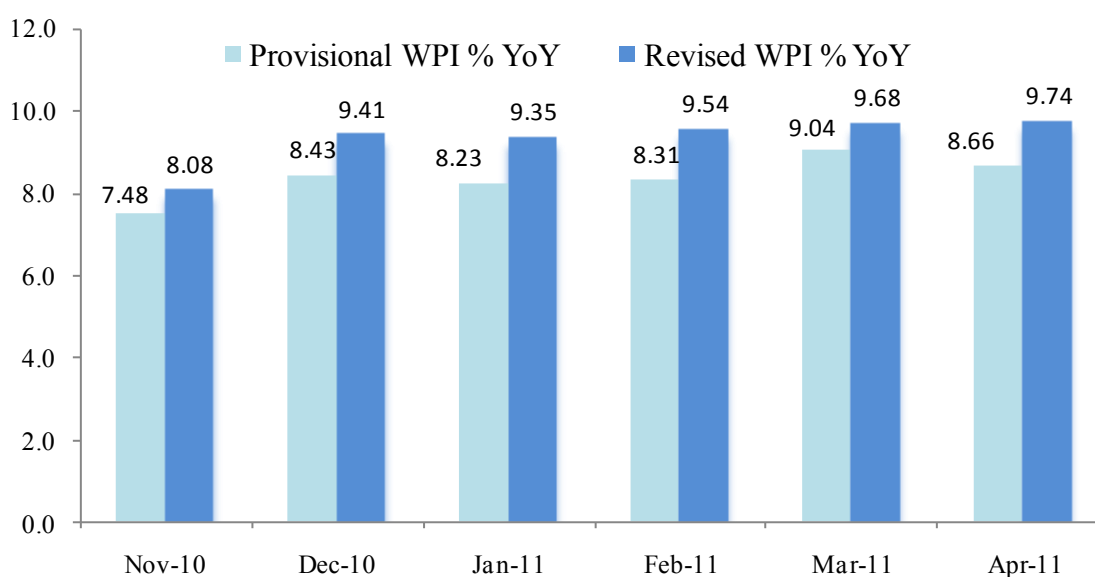


		% YoY	% YoY	% MoM	% MoM
	Index	Jun-11	May-11	Jun-11	May-11
WPI	153.0	9.44	9.06	0.86	0.73
Primary articles	197.5	12.20	11.30	2.80	0.30
Food Articles	190.1	8.44	8.38	1.93	1.63
Non Food Articles	181.3	18.60	22.30	-1.97	-4.40
Fuel	161.6	12.80	12.30	0.70	0.30
Manufactured products	137.3	7.43	7.27	0.10	1.00

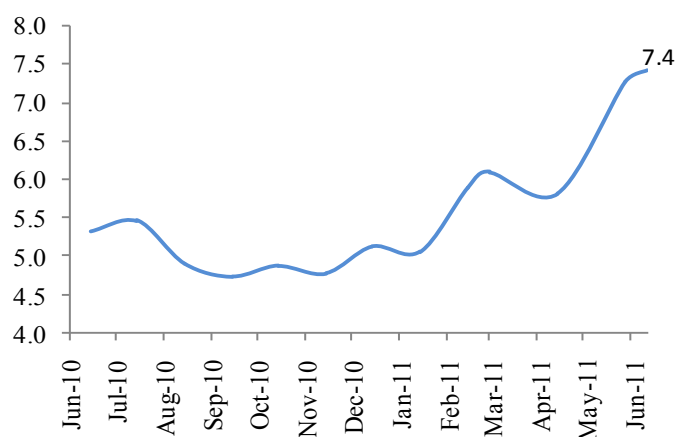
Double Digit Inflation Just A Revision Away:

WPI inflation for April 2011 was revised to 9.74% YoY from 8.66% YoY before. Given the steep revisions of provisional inflation numbers, its is highly probable that the June figures would actually be well above double digits. As can be seen from the trend, revisions have been on the upside in the range of 60– 123 bps in data relating to the past months.

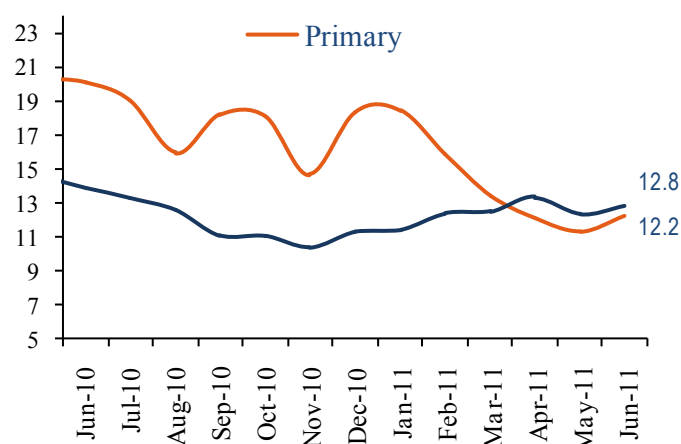
Steep Revisions In The WPI Data:



Manufactured Products Inflation % YoY



Primary Articles & Fuel Inflation Rising Again, % YoY

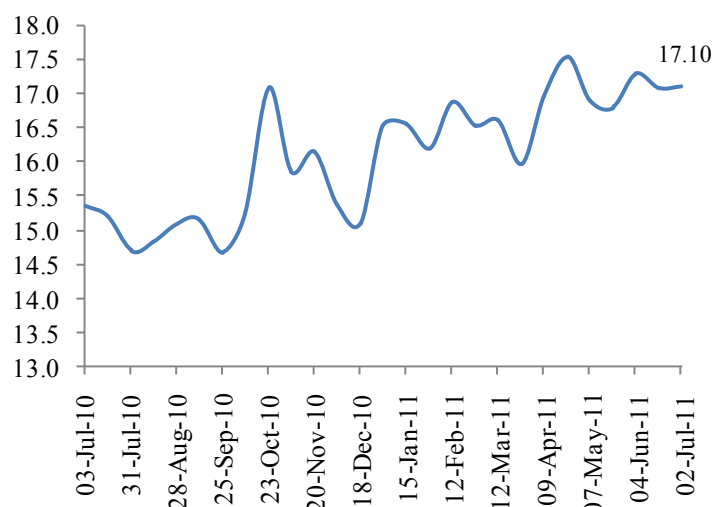


Policy Implications: With Inflation clearly on the rise, including subsequent higher revisions of data, the case for a rate hike in the coming monetary policy review on July 26, 2011, becomes stronger. We expect RBI to hike benchmark interest rates by 25 bps in the coming policy meet.

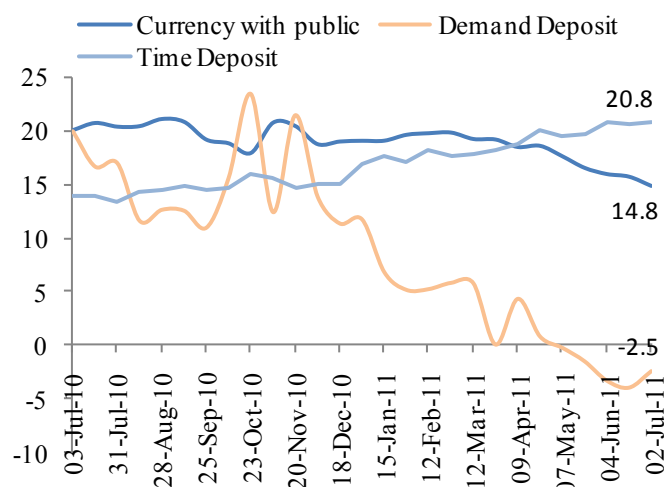
Money Supply Increased And Credit Growth Declined:

- ◆ Money Supply (M3) improved marginally to 17.10% YoY as demand and time deposits all posted marginal increase during the fortnight ending July 2, 2011.
- ◆ During the fortnight ending July 2, 2011, currency with public eased to 14.80% YoY from 15.68% YoY, while demand deposit posted an improvement with a negative growth of 2.05% YoY compared with 4.05% YoY in the immediately preceding fortnight. Time deposits growth improved to 20.80% YoY compared with 20.68% YoY.
- ◆ SCB credit growth for the week ending July 2, 2011, declined to 19.90% YoY compared with 21.02% YoY a week ago as both food and non-food credit growth decreased. SCB credit growth has declined in the past two months with higher interest rates and moderation in industrial growth.
- ◆ Non-food credit growth declined to 19.67% YoY from 20.59% YoY a week ago while food credit eased to 46.20% YoY from 47.17% YoY before.

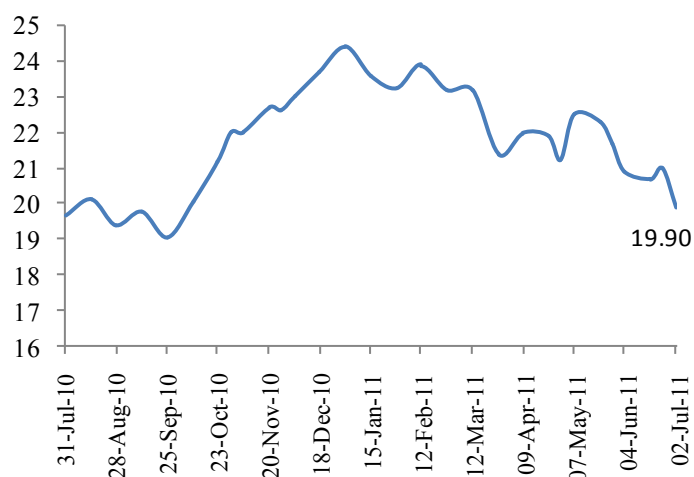
Money Supply (M3), % YoY



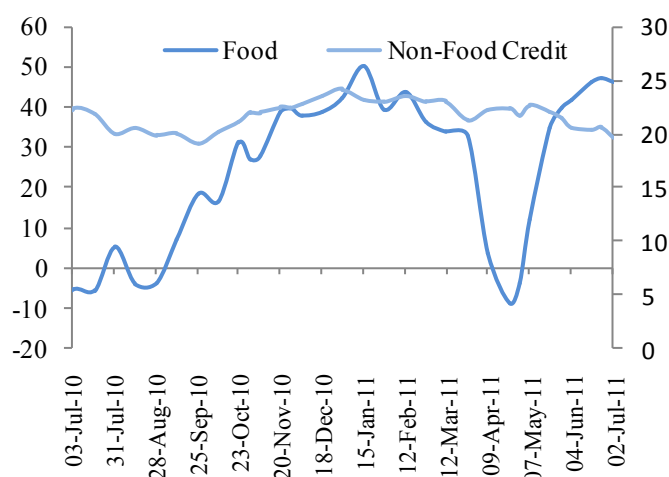
Time and Demand Deposits, % YoY



SCBs Credit, % YoY



Food & Non Food Credit, % YoY



Forex Reserves Decline To \$314.6 billion

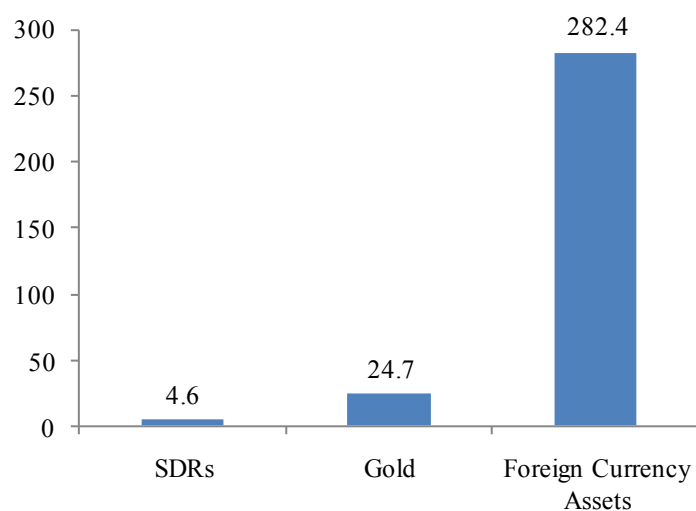
Forex reserves decreased to \$314.6 billion in the week ending July 9, 2011, due to a fall in foreign currency assets. Forex reserves in India are valued in US dollars. During the week forex reserves declined by \$1.1 billion to \$314.6 billion.

Total forex reserves comprise foreign currency assets, SDRs and the central bank's position in gold, all of which are measured in US dollars.

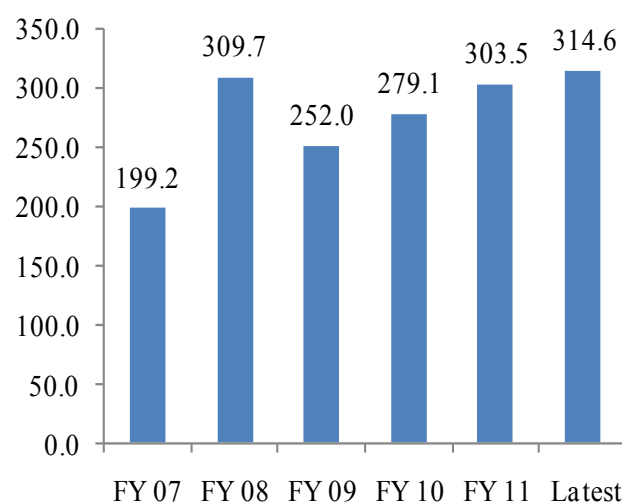
- ◆ During the week ending July 9, 2011, foreign currency assets declined by \$1.1 billion to \$282.4 billion due to revaluation changes which led to decline in the overall position in forex reserves.
- ◆ Positions in gold and reserve position with IMF and SDRs remained unchanged during the week.

US\$ bn	Forex reserves	SDRs	Reserve Position in IMF	Gold	Foreign currency assets
18-Jun-11	310.6	4.6	3.0	24.4	278.6
25-Jun-11	309.0	4.6	3.0	24.4	277.1
02-Jul-11	315.7	4.6	3	24.7	283.5
09-Jul-11	314.6	4.6	3	24.7	282.4

Forex Reserves Components (in \$ billion)



Forex Reserves Annual Trends (in \$ billion)

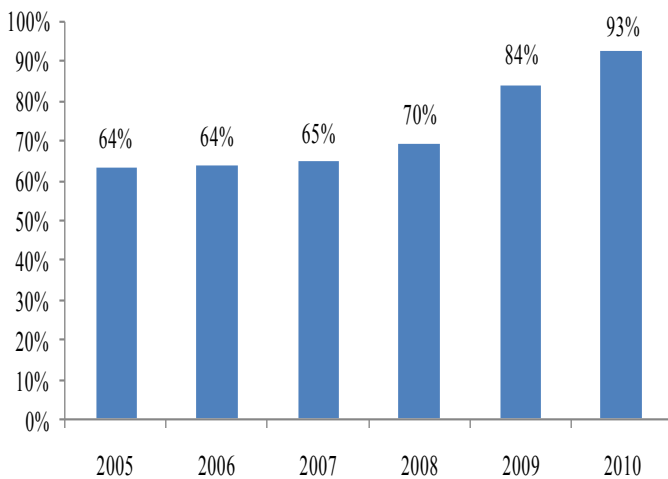


US Debt Ceiling Deadline:

US Debt Crisis Looms: US is one the few countries where the Congress decides the debt ceiling. US is likely to touch \$14.29 trillion debt ceiling which was raised in February 12, 2010. Once US reaches its debt ceiling, it will not be able to raise further debt to make necessary payments (such as, salaries) and the economy could see its creditworthiness downgraded. There could be deferment of social security payments, interest payments to US government bonds holders, Medicare bills, and tax payers refunds, among other things, if US fails to increase the debt ceiling.

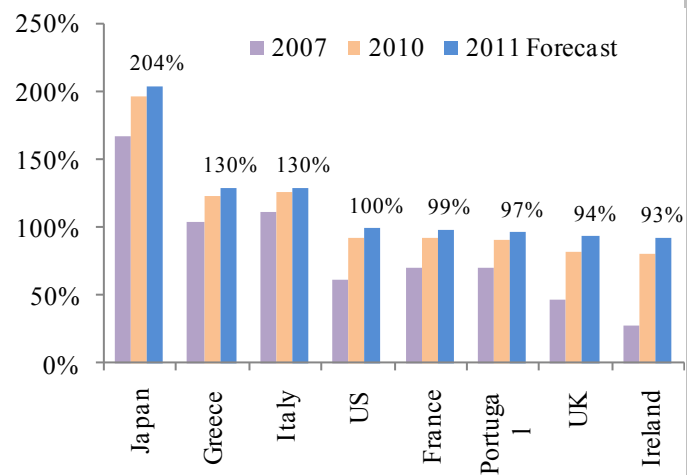
- ◆ **US could loose AAA status:** Ceiling debate has become even much riskier as Moody’s, a rating agency, has hinted that it would downgrade the AAA rating of the world’s largest economy. In US, the Democrats and Republicans are still to reach a consensus on increasing the debt ceiling before the deadline of August 2, 2011. As the central banks of almost every nation invest in US treasuries, a possible downgrade can lead them to diversify their forex assets further.
- ◆ **Republicans hold the Key:** Republicans are not agreeing to an increase in the debt ceiling. They will relent only on one condition: a steep and phased cut in spending and a pledge to bring down the budget deficit. The debt ceiling deadlock is likely to force Democrats to opt for a compromise on the spending programme to avert the crisis.
- ◆ **US growing Debt:** Though US faces a default crisis at the moment, but given the levels of debt as a percentage of GDP, it also needs to address its long-term debt situation. US debt has risen substantially post the financial crisis. US debt as a percentage of GDP rose to 93% in 2010. US ranks among the most indebted nations, some of which are facing economic crisis.

US Debt Trends as a % of GDP



Source: US Treasury

Debt as a % of GDP



Source: IMF

Currency and Nifty Movement

	USD/INR	EUR/INR	NIFTY
Open:	44.43	63.072	5648.05
High:	44.76	63.579	5653.95
Low:	44.345	61.835	5496.95
Close:	44.51	62.857	5581.1

USD/INR:

Last week, \$/INR continued to be in range of 44.43-44.76. For this week, we expect \$/INR to trade in a range of 44.40–44.80. Good support is built at 44.35 levels.

INR Weekly Support and Resistance are as follows for the coming week:

Resistance 1:	44.7300	Support 1:	44.3200
Resistance 2:	44.9500	Support 2:	44.1500

EUR/INR:

Last week, EUR/INR traded in a volatile range of 61.8350-63.5800. For this week, we expect the pair to trade in a range of 61.90-62.90.

EUR/INR Weekly Support and Resistance are as follows for the coming week:

Resistance 1:	63.6700	Support 1:	61.9350
Resistance 2:	64.5010	Support 2:	61.0130

NIFTY:

Last week, Nifty traded in a range of 5496.95 - 5653.95. For this week, we expect the pair to trade in a range of 5450 – 5600 with a negative bias.

Nifty Weekly Support and Resistance are as follows for the coming week:

Resistance 1:	5657.72	Support 1:	5500.72
Resistance 2:	5734.33	Support 2:	5420.33

Factors that impacted the markets last week:

- ◆ US Debt Crisis: Dollar Negative – Euro Positive
- ◆ Europe Crisis: Dollar Positive – Euro Negative
- ◆ European Bank's Stress Test : Dollar Positive – Euro Negative



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