

INDIA

Rohini Malkani
+91-22- 6631-9876
rohini.malkani@citigroup.com
Mumbai

Anushka Shah
Mumbai

India Econ Flash

Update on Govt Finances – Expenditure pressures rise

- **Apr-August fiscal deficit – 68.5% of budget estimates:** The distortion in the fiscal picture seen earlier this year (*following the expenditure incurred on acquiring RBI's 59.7% stake in SBI*) was reversed in August, when the RBI transferred an equivalent amount in the form of dividend. As a result, the fiscal deficit during Apr-Aug was Rs1,033bn or 68.5% of budget estimates while the revenue deficit was Rs535bn or 75% of estimates as compared to it crossing 100% of estimates last month.
- **Tax collections – growth slows in line with budget targets:** From the 30%+ growth seen in 1Q FY08, growth in gross tax collections slowed to 18% in August – in line with the 17% budget target. The slowdown is primarily due to lower excise collections. (*see page 2 for a detailed table*). However, growth in cumulative tax collections remains over 22%, which bodes well for government finances.
- **Government to meet its target but watch out for NREGP:** The FY08 deficit is targeted at Rs1,509bn or 3.3% of GDP – in line with the FRBM¹ targets. While we maintain our view that the budget assumptions are conservative, a point to note is the rise in off-balance-sheet items² (oil bonds/possibility of further fertiliser subsidies), and the recent announcement of the extension of the National Rural Employment Guarantee Program³ (NREGP) – a possible indicator of the government getting ready for early elections

Note Released: 3-Oct-07

April- Aug 2007: Fiscal Data (Rs Bn, %)

	Aug-07	% YoY	Apr-Aug07	%YoY	FY08BE	Ytd of B
a. Revenue receipts	688	135.5	1,641	54.0	4,864	33.7
Net tax revenues	194	9.2	994	22.0	4,039	24.6
Non-tax (incl RBI's dividend)	493	332.5	647	157.8	826	78.4
b. Non-debt cap receipts	6	-32.8	39	23.0	432	9.1
c. Total receipts (a+b)	694	130.6	1,680	53.1	5,296	31.7
d. Revenue expenditure	399	31.3	2,176	17.0	5,579	39.0
e. Capital expenditure	34	-14.0	538	271.2	1,226	43.8
f. Total expenditure (d+e)	433	26.0	2,714	35.4	6,805	39.9
Plan Expenditure	125	57.3	723	34.1	2,051	35.3
Non- Plan Expenditure	308	16.6	1,990	35.9	4,754	41.9
g. Fiscal deficit (f-c)	(261)	-710.0	1,033	14.0	1,509	68.5
h. Revenue deficit (d-a)	(289)	-2531.4	535	-32.6	715	74.9

Source: Controller General of Accounts, Budget Documents

¹ Under the **FRBM Act**, beginning FY05, the central government has to reduce its fiscal and revenue deficit by 0.3% and 0.5% of GDP a year so as to eliminate the revenue deficit by 2009

² Off balance sheet items : (1) **Oil bonds** - In order to compensate oil companies for marketing losses, the government is likely to issue oil bonds to the tune of Rs190bn in FY08 as compared to Rs241bn in FY07 and Rs115bn in FY06 (2) **Fertilizers** – FY07 arrears of Rs88bn were paid out of the current year's subsidy bill which could result in the FY08 limit being breached

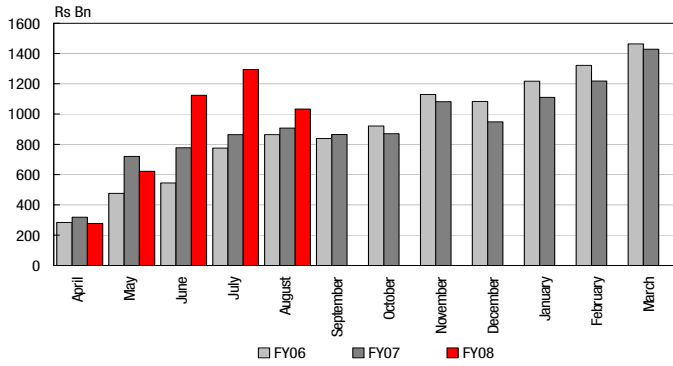
³ The implementation of the **National Rural Employment Guarantee Program (NREGP)** will also impose an additional fiscal strain. Implemented in 2006, the scheme enables one member of every rural household to 100 days a year of work at a minimum wage of Rs60 per day. The government initially rolled out this scheme in 200 districts and this number was later raised to 330 districts in the budget this year, with an initial allocation of Rs120bn. Now, the government intends to extend the program to all districts in the country (i.e 600), which would nearly double the outlays required.

Public Finances in Pictures

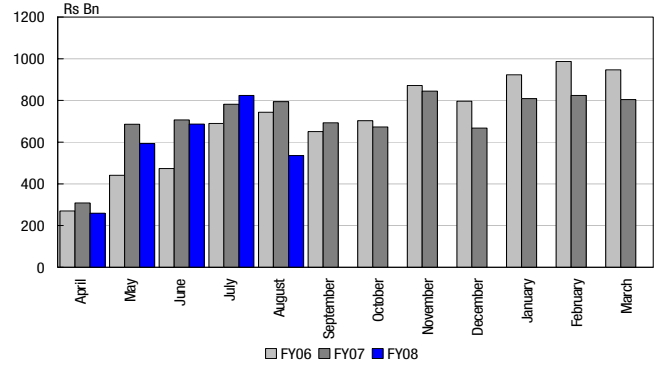
The fiscal deficit came in at 68.5% of budget estimates during Apr-Aug, with accounting entries due to RBI's stake sale in SBI being reversed

This accounting entry has resulted in the Revenue Deficit, coming in at 75% of budget estimates during Apr-Aug v/s over 100% last month

Cumulative Trends in the Fiscal Deficit (Rs Bn)



Cumulative Trends in the Revenue Deficit (Rs bn)



Tax collections remained robust. Although growth in tax revenues was up 22% during Apr-Aug, slower than trends seen earlier, growth was still above the government's targeted rate of 17%

The government's borrowing calendar for 2HFY08 is in line with expectation but the supply in Oct and Nov, together with the MSS supply will keep bonds range-bound

Cumulative Trends in the Revenue Deficit (Rs Bn)

	Aug-07	%YoY	Apr-Aug08	%YoY	FY08BE	% of B	Budgeted Growth Rate
Corporate	37	24.6	334	46.2	1,684	19.8	15.0
Income	48	44.0	237	34.4	988	24.0	19.8
Customs	86	15.4	403	18.7	988	40.8	20.7
Excise	93	1.2	352	4.9	1,302	27.0	11.0
Others	45	40.7	196	34.0	520	37.6	30.6
Gross Taxes	308	18.1	1,522	24.1	5,482	27.8	17.2
Devolt to States	112	37.8	519	28.0	1,443	36.0	18.4
Net Taxes	194	9.2	994	22.0	4,039	24.6	16.7

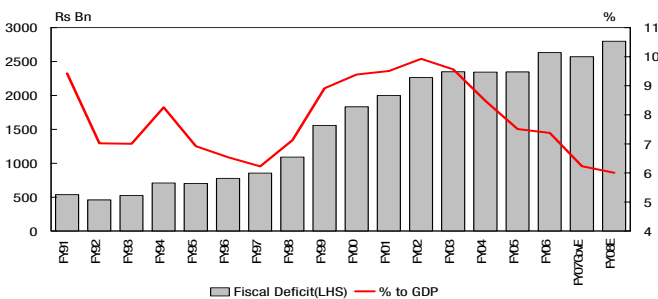
Issuance Calendar of Dated Securities(Rs Bn)

Period of Auction	Amt	Term of the Security
October 5-12	100	i) 10-14 year security for Rs60bn
		ii) 20-year and above security for Rs40bn
October 19-26	80	i) 5-9 year security for Rs.40bn
		ii) 15-19 year security for Rs.40bn
November 2-8	80	i) 10-14 year security for Rs.50bn
		ii) 20-year and above security for Rs30bn
November 16-23	70	i) 10-14 year security for Rs30bn
		ii) 15-19 year security for Rs40bn
December 7-14	70	i) 10-14 year security for Rs50bn
		ii) 20-year and above security for Rs.20bn
January 4-11	100	i) 10-14 year security for Rs60bn
		ii) 20-year and above security for Rs40bn
February 1-8	90	i) 10-14 year security for Rs.50bn
		ii) 20-year and above security for Rs40bn
Total	590	

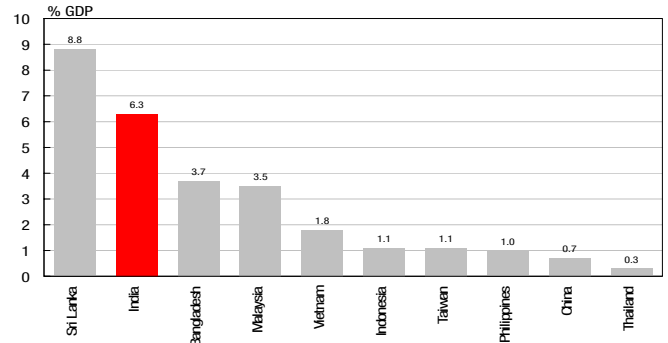
Looking ahead, the Ministry has stressed that it will continue to adhere to the path of fiscal consolidation and meet its targets

This is important given that despite reform initiatives, India's fiscal deficit still amongst the highest in the region.

Trends in the Combined Fiscal Deficit (Rs Bn, % GDP)



Fiscal Deficit- A Comparative View



Disclosure Appendix

ANALYST CERTIFICATION

This research report contains commentary and analysis by Rohini Malkani and Anushka Shah. Each of these individual analysts/strategists/economists hereby certifies that, with respect to the issuers about which they have provided commentary or analysis all of the views expressed in this research report accurately reflect the analyst's/strategists/economists personal views about the subject issuer(s) and its (their) securities. Each of these individuals also certifies that no part of their compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

Other Disclosures

ADDITIONAL INFORMATION REGARDING THIS REPORT IS AVAILABLE ON REQUEST.

Citigroup research analysts receive compensation based on a variety of factors. Like all Citigroup employees, analysts receive compensation that is impacted by Citigroup's overall profitability, which includes revenues from, among other things, investment banking activities. Analyst compensation is determined by Citigroup research management and other senior management (not including investment banking personnel).

ISSUER-SPECIFIC DISCLOSURES

Citigroup, its officers, directors and/or employees, may from time to time have long or short positions in, act as principal in connection with, and buy or sell securities or derivatives (including options and warrants) discussed in this report. For purposes of your review of this report, you should assume that this is the case with respect to the securities covered herein.

Citigroup does and/or seeks to do business with many issuers, including through the provision of investment banking or other services. For purposes of your review of this report, you should assume that Citigroup has acted as a manager or co-manager of an offering of securities discussed in this report within the prior 12 months or has provided other services to the issuer within the prior 12 months for which it has received or expects to receive compensation.

Citigroup is an active market maker or liquidity provider for many fixed-income securities and from time to time takes principal positions in such securities or related derivatives. For purposes of your review of this report, you should assume that this is the case with respect to the securities covered herein.

OTHER GENERAL DISCLOSURES

This research report was prepared by Citigroup Global Markets Inc. ("CGMI") and/or one or more of its affiliates (collectively, "Citigroup"), as further detailed in the report, and is provided for information and discussion purposes only. It does not constitute an offer or solicitation to purchase or sell any securities or other financial products.

This report does not take into account the investment objectives, financial situation or particular needs of any particular person. Investing in securities and other financial products entails certain risks, including the possible loss of the entire principal amount invested. Certain investments in particular, including those involving structured products, futures, options and other derivatives, are complex, may entail substantial risk and are not suitable for all investors. The price and value of, and income produced by, securities and other financial products may fluctuate and may be adversely impacted by exchange rates, interest rates or other factors. Prior to effecting any transaction in options or options-related products, investors should read and understand the current Options Clearing Corporation Disclosure Document, a copy of which may be obtained on request from your Citigroup representative. Certain securities may not be registered with, or subject to the reporting requirements of, the US Securities and Exchange Commission or any comparable regulatory authority. Information available on such securities may be limited. Investors should obtain advice from their own tax, financial, legal and other advisors and only make investment decisions on the basis of the investor's own objectives, experience and resources.

The information contained in this report is based on generally available information and, although obtained from sources believed to be reliable, its accuracy and completeness is not guaranteed. The analysis contained in this report is based on a number of assumptions. Changes in such assumptions could produce materially different results. This communication is not intended to forecast or predict future events. Past performance is not a guarantee or indication of future results.

Citigroup research analysts may communicate with sales and trading personnel and other Citigroup personnel for the purposes of gathering and analyzing market information and may discuss with such personnel information regarding, among other things, market trends, economic trends, the market for bonds of a specific issuer and other market information (such as current prices, spreads and liquidity), so long as such communications do not impair the analyst's independent ability to express accurately his or her personal views about any and all of the subject securities or issuers. Other Citigroup personnel who do not function as research analysts, including sales and trading personnel, may provide oral or written market commentary or trade ideas to Citigroup's customers or proprietary trading desks that differ from the views expressed in this report. Citigroup's proprietary trading and asset management businesses may make investment decisions that are different from the recommendations contained in this report.

Citigroup has no duty to update this report and the opinions, estimates and other views expressed in this report may change without notice. No liability whatsoever is accepted for any loss (whether direct, indirect or consequential) that may arise from any use of the information contained in or derived from this report.

Securities recommended, offered or sold by Citigroup (unless expressly stated otherwise): (i) are not insured by the Federal Deposit Insurance Corporation or any other body; and (ii) are not deposits or other obligations of Citibank, N.A. or any other insured depository institution.

Citigroup does not provide tax advice and nothing contained herein is intended to be, or should be construed as, tax advice. Any discussion of US tax matters contained in this report was written to support the promotion or marketing of the transactions or other matters addressed herein and is not intended to be used, and must not be used by any recipient, for the purpose of avoiding US federal tax penalties. Recipients of this report should seek tax advice based on the recipient's own particular circumstances from an independent tax adviser.

This report is intended for distribution solely to customers of Citigroup in those jurisdictions where such distribution is permitted. No part of this report may be copied or redistributed by any recipient for any purpose without Citigroup's prior written consent.

Local law requirements may prohibit certain investors from effecting a transaction in the security or securities covered in this report. US persons wishing further information or to effect a transaction should contact a registered representative of CGMI in the United States. Non-US persons wishing further information or to effect a transaction should contact a Citigroup entity located in their own jurisdiction unless applicable governing law permits otherwise.

AUSTRALIA: This report is made available in Australia to wholesale clients through Citigroup Global Markets Australia Pty Ltd. (ABN 64 003 114 832 and AFSL No. 240992) and to retail clients through Citigroup Wealth Advisors Pty Ltd. (ABN 19 009 145 555 and AFSL No. 240813), participants of the ASX Group, and regulated by

the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. **CANADA:** If this report is being made available in certain provinces of Canada by Citigroup Global Markets (Canada) Inc. ("CGM Canada"), CGM Canada has approved the Product. Citigroup Place, 123 Front Street West, Suite 1100, Toronto, Ontario M5J 2M3. **CHINA:** This report is made available in China through Citibank, N.A. Beijing Branch, 16F Tower 1 Bright China Chang-an Bldg., 7 Jianguomen Nei Avenue, Beijing, 100005 P.R. China. Citibank, N.A. Beijing Branch is regulated by the China Banking Regulatory Commission. **CZECH REPUBLIC:** This report is being distributed within the territory of the Czech Republic by Citibank a.s. Citibank a.s. is a bank and securities broker/dealer regulated by the Czech National Bank, Na Příkopě 28, Prague 1, Czech Republic. Unless expressly stated otherwise, Citibank a.s. is only distributing this report and, upon its distribution, it has not changed or amended the actual content of this report in any way (as such was prepared by respective entities and/or individuals as further detailed in the report). **HONG KONG:** If this report is made available in Hong Kong by, or on behalf of, Citigroup Global Markets Asia Ltd., it is attributable to Citigroup Global Markets Asia Ltd., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. Citigroup Global Markets Asia Ltd. is regulated by the Hong Kong Securities and Futures Commission. If this report is made available in Hong Kong by Citibank, N.A., it is attributable to Citibank, N.A., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. Citibank, N.A. is regulated by the Hong Kong Monetary Authority. **INDIA:** The Product is made available in India by Citigroup Global Markets India Private Limited, which is regulated by Securities and Exchange Board of India. Bakhtawar, Nariman Point, Mumbai 400-021. **INDONESIA:** This report is made available in Indonesia through Citibank, N.A. Indonesia Branch, Citibank Tower Lt 7, Jend. Sudirman Kav 54-55, Jakarta. Citibank, N.A. Indonesia Branch is regulated by the Bank of Indonesia. **JAPAN:** This report is being distributed in Japan by Nikko Citigroup Limited. If this report was prepared by a Citigroup affiliate of Nikko Citigroup Limited, it is being distributed by Nikko Citigroup Limited under license. If this report was prepared by Nikko Citigroup Limited, it may be based in part on a report produced by one of its affiliates used under license. If this report was prepared by Nikko Citigroup Limited and is being distributed in other jurisdictions by other Citigroup affiliates, or by Nikko Cordial Securities Inc., it is being distributed by them under license. Nikko Citigroup Limited is regulated by Financial Services Agency, Securities and Exchange Surveillance Commission, Japan Securities Dealers Association, Tokyo Stock Exchange and Osaka Securities Exchange. Shin-Marunouchi Building, 1-5-1 Marunouchi, Chiyoda-ku, Tokyo 100-6520 Japan. **KOREA:** The Product is made available in Korea by Citibank Korea Inc., which is regulated by the Financial Supervisory Commission and the Financial Supervisory Service. Address is Dadong 39, Jung Gu, Seoul, Korea, 100-180. **MEXICO:** This report is made available in Mexico by Acciones y Valores Banamex, S.A. De C. V., Casa de Bolsa, and Banco Nacional de México S.A. Acciones y Valores Banamex is regulated by Comisión Nacional Bancaria y de Valores. Its address is Reforma 398, Col. Juárez, 06600 Mexico, D.F. Banco Nacional de México S.A. is regulated by the Comisión Nacional Bancaria y de Valores. Its address is Actuario Roberto Medellín 800, Col. Santa Fé, (01210) Mexico City, Mexico. **NEW ZEALAND:** This report is made available in New Zealand through Citigroup Global Markets New Zealand Limited (Company No. 604457), a Participant of the New Zealand Exchange Limited and regulated by the New Zealand Securities Commission. Level 11, 23 Customs Street East, Auckland, New Zealand. **PHILIPPINES:** This report is made available in the Philippines through Citibank, N.A. Philippine Branch, 8741 Paseo de Roxas, Makati City, Philippines. Citibank, N.A. Philippine Branch is regulated by the Bangko Sentral ng Pilipinas. **POLAND:** The Product is made available in Poland by Dom Maklerski Banku Handlowego SA, an indirect subsidiary of Citigroup Inc., which is regulated by Komisja Papierów Wartościowych i Giełd. Bank Handlowy w Warszawie S.A. ul. Senatorska 16, 00-923 Warszawa. **RUSSIA:** The Product is made available in the Russian Federation through ZAO Citibank, which is licensed to carry out banking activities in the Russian Federation in accordance with the general banking license issued by the Central Bank of the Russian Federation and brokerage activities in accordance with the license issued by the Federal Service for Financial Markets. Neither the Product nor any information contained in the Product shall be considered as advertising the securities mentioned in this report within the territory of the Russian Federation or outside the Russian Federation. The Product does not constitute an appraisal within the meaning of the Federal Law of the Russian Federation of 29 July 1998 No. 135-FZ (as amended) On Appraisal Activities in the Russian Federation. 8-10 Gashka Street, 125047 Moscow. **SINGAPORE:** The Product is made available in Singapore through Citigroup Global Markets Singapore Pte. Ltd. and Citicorp Investment Bank Singapore Ltd. Citigroup Global Markets Singapore Pte. Ltd. is a Capital Markets Services License holder and regulated by the Monetary Authority of Singapore. 1 Temasek Avenue, #39-02 Millenia Tower, Singapore 039192. Citicorp Investment Bank Singapore Ltd. is a Merchant Banking License holder and regulated by the Monetary Authority of Singapore. 3 Temasek Avenue, #17-00 Centennial Tower, Singapore 039190. **SOUTH AFRICA:** Citigroup Global Markets (Pty) Ltd. is incorporated in the Republic of South Africa (company registration number 2000/025866/07) and its registered office is at 145 West Street, Sandton, 2196, Saxonwold. Citigroup Global Markets (Pty) Ltd. is regulated by the JSE Securities Exchange South Africa, the South African Reserve Bank and the Financial Services Board. The investments and services contained herein are not available to private customers in South Africa. **TAIWAN:** The Product is made available in Taiwan through Citibank, N.A., Taipei Branch, which is regulated by the Financial Supervisory Commission. No portion of the report may be reproduced or quoted in Taiwan by the press or any other person. F.8 No. 169, Section 4, Jen Ai Road, Taipei, Taiwan. **UNITED KINGDOM:** This report is being distributed in the United Kingdom by Citibank, N.A., London Branch, or Citigroup Global Markets Limited, Citigroup Centre, Canada Square, Canary Wharf, London E14 5LB, UK. This material is directed exclusively at market professional and institutional investor customers in the United Kingdom and is not for distribution to private customers in the United Kingdom as defined by the Financial Services Authority. Any investment or service to which this material may relate will not be made available to such private customers. This material may relate to investments or services of a person outside the United Kingdom or to other matters which are not regulated by the Financial Services Authority and further details as to where this may be the case are available on request in respect of this material. **UNITED STATES:** This report is being distributed in the United States by CGMI. If this report was prepared in whole or in part by a non-U.S. affiliate of CGMI, CGMI accepts responsibility for its contents (subject to the notices above). If this report covers non-U.S. securities, U.S. investors should be aware that non-U.S. companies may not be subject to uniform audit and reporting standards, practices and requirements comparable to those in the United States. Securities of some non-U.S. companies may be less liquid and their prices may be more volatile than securities of comparable U.S. companies. Exchange rate movements may have an adverse effect on the value of an investment in non-U.S. securities and its corresponding dividend payment for U.S. investors. CGMI is a member of the Securities Investor Protection Corporation. **EUROPEAN UNION:** Unless specified to the contrary, within EU Member States, the Product is made available by Citigroup Global Markets Limited, which is regulated by the Financial Services Authority. Many European regulators require that the firm must establish, implement and make available a policy for managing conflicts of interest arising as a result of publishing or distribution of investment research. The policy applicable to research analysts within Citigroup's Fixed Income Strategy and Analysis and Economic & Market Analysis divisions, as well as the investment research they produce, can be obtained by contacting Citigroup Global Markets Inc., 388 Greenwich Street 11th floor, NY NY 10013, Attention: Fixed Income Publishing.

© Citigroup Global Markets Inc., 2007. All rights reserved. Smith Barney is a division and service mark of Citigroup Global Markets Inc. and its affiliates and is used and registered throughout the world. Citi and Citi and Arc Design are trademarks and service marks of Citigroup Inc. or its affiliates and are used and registered throughout the world. CitiFx® is a service mark of Citicorp Inc.. Nikko is a service mark of Nikko Cordial Corporation. Any unauthorized use, duplication or disclosure is prohibited by law and may result in prosecution.