

INDIA

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Table of Contents

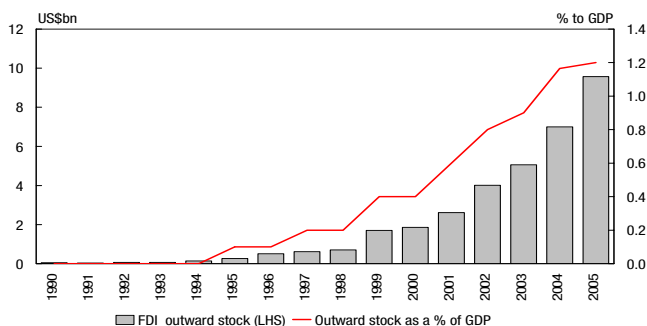
Market Summary +	1
Spotlight	
Market in Pictures	2-3
India Mkt Monitor +	
Financial Mkt Forecasts	4

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CitiViews – India Market Watch

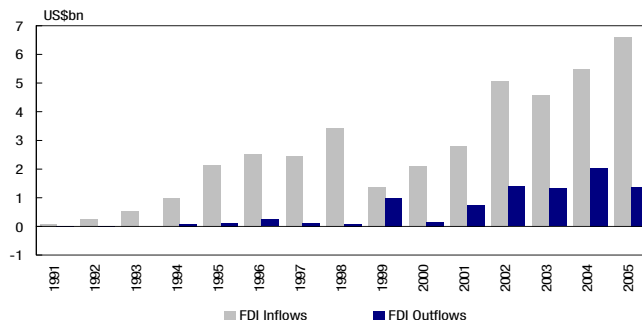
- **Spotlight on Outward FDI:** In a marked reversal of trade and investment flows, companies from emerging countries including India have been acquiring firms in developed markets. In the latest World Investment Report, UNCTAD has said that the key reasons for Indian firms acquiring companies abroad are (1) greater market access, (2) broad-basing product range, and (3) need to pursue customers for niche products. Besides this, we believe a key factor behind such acquisitions is greater technological and financial strength for companies - which provide them with ownership advantages abroad¹. (*see Sept05 Macroscope for details*).
- **India - An Emerging ‘Global Investor’:** Latest data indicates on a stock basis, outward FDI from India totaled over US\$9bn. A recent report by Grant Thorton also indicates that although inbound deals are larger in value terms, the **number** of outbound deals has seen a faster increase, rising from just 60 deals in 2004, to 266 in 2006. However, more recently, there has been a reversal in trend, with outbound deals outpacing inbound ones **even in value terms**. Some of the recent overseas takeovers by Indian firms include Tata Steel’s US\$12bn acquisition of Corus Group; Dr Reddy’s acquisition of Germany’s Betapharm for \$572 million; and wind-turbine maker Suzlon Energy’s \$520 million acquisition of Belgium’s Hansen Transmissions. Although overseas acquisitions may result in lower net FDI inflows into India, the impact on the BoP position is likely to be eventually neutralized by higher export earnings and improved corporate performance.
- **Bond Market:** The 10-year yield fell to 7.69% from 7.88% as RBI kept all rates unchanged except for the 25bps hike in the repo rate to 7.5%. Other positives were the S&P upgrade and continued improvement in govt finances. Going forward, we maintain our view that 2007 will likely be a year of multiple policy instruments – a possible cut in the SLR and hike in the CRR/Reverse Repo.
- **Forex Market:** Rupee gained to close at Rs44.12/US\$ from Rs44.24/US\$ in the previous week. Though, importer demand and dollar buying by state-run banks saw the rupee touch an intra-week low of 44.33/US\$, S&P’s sovereign upgrade saw the rupee test Rs44/US\$ levels before closing at Rs44.12/US\$.

Trends in Outward FDI Stock



Source: World Investment Report 2006

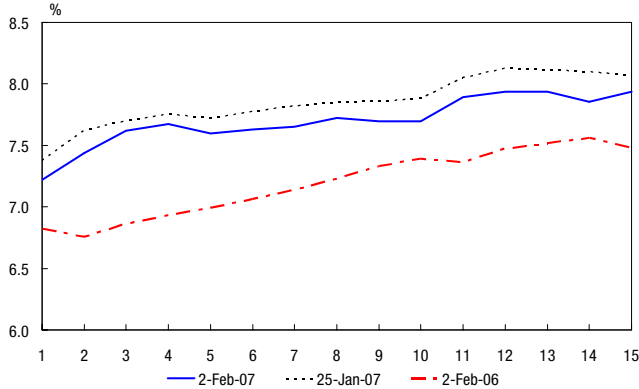
Trends in FDI Inflows and Outflows



¹ This is known as the “OLI Paradigm” which stresses that Ownership, Location, and Internalization are the key factors behind FDI. Pls see “*India Macroscope – FDI: Will Cross Border Deals from India Overtake Inward Flows?*”, 9 September 2005

India – Markets in Pictures

Trends in GOI Yield Curve



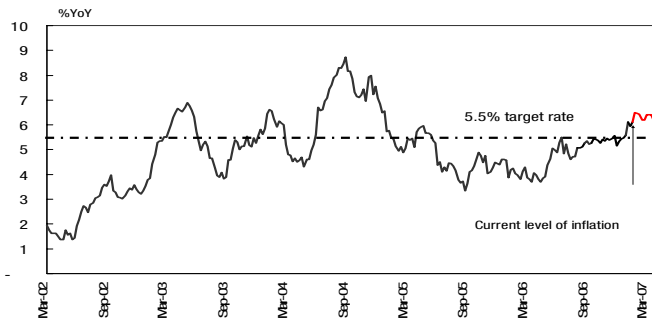
The yield curve dropped mid-week due to (1) the S&P upgrade and (2) the monetary policy review which kept all rates on hold except the repo rate. Spread between 2-year and 15-year yield widened to 50 bps from 44 bps while the curve beyond the short term flattened

Trends in Exchange Rate - Rs/US\$



Rupee appreciated to Rs44.12/US\$ from Rs44.24/US\$ in the previous week. The rating upgrade by S&P saw the rupee to test Rs44/US\$ levels but buying by state-run banks saw the rupee fall to a low of 44.33 intra-week

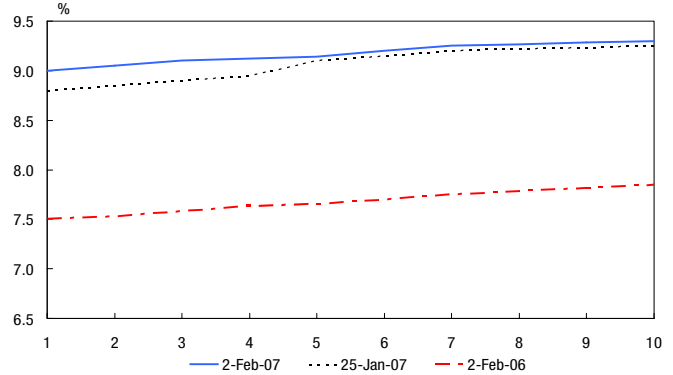
Trends in Inflation (% YoY)



Inflation crossed the 6% mark once again; rising to 6.1%yoY for the week-ended 20th Jan. While the index for Primary Articles was up 9.8% from its level the previous year, Manufactured Products reported a rise of 5.7%yoY and the Fuel Index was up 3.7%. The Ministry also revised inflation data for 25th Nov from 5.3% to 5.55%.

Source: Reuters, Bloomberg

Trends in AAA Yield Curve



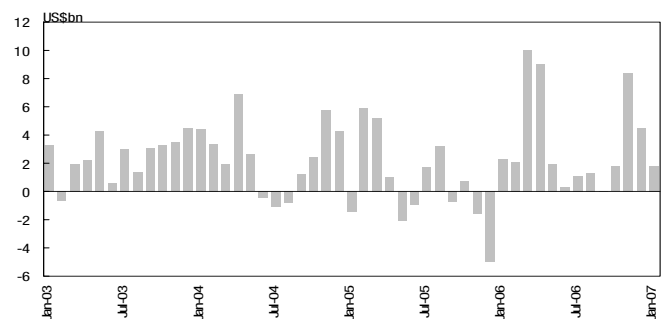
Bond yields inched up marginally with the 5-year benchmark up 4 bps to 9.14% while the credit spread widened 12 bps to 132 bps

Trends in Six-Month Premiums (%)



Premium slipped to 3.62% from 3.97% in choppy trade. Premia saw receiving interest on the back of the S&P upgrades which improved the outlook for dollar inflows

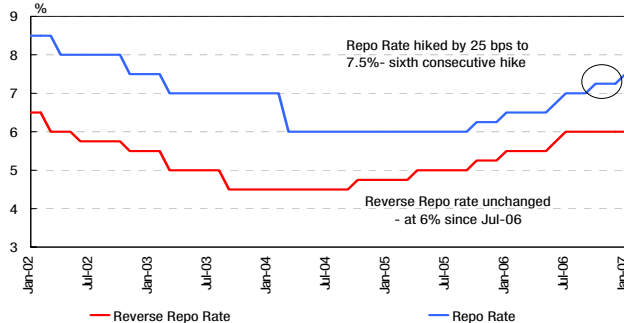
Monthly Increase in Forex Reserves (US\$bn)



Total forex reserves, including gold, rose by US\$924mn for the week ended 26th Jan. Fiscal YTD, foreign currency assets have also increased by US\$26.9bn and currently stand at US\$171bn as compared to US\$133bn the previous year. Forex reserves including gold stand at US\$179bn

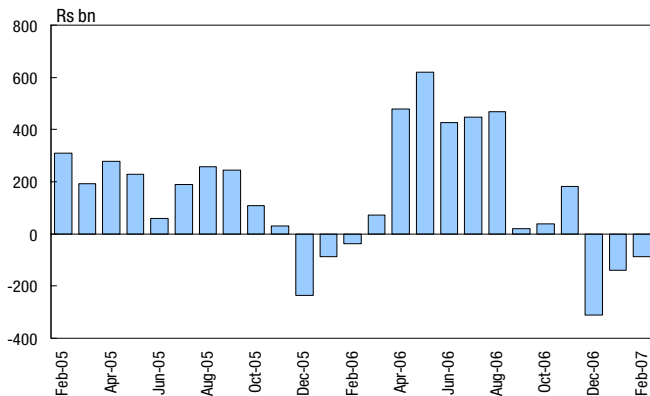
India – Markets in Pictures

RBI - Monetary Policy



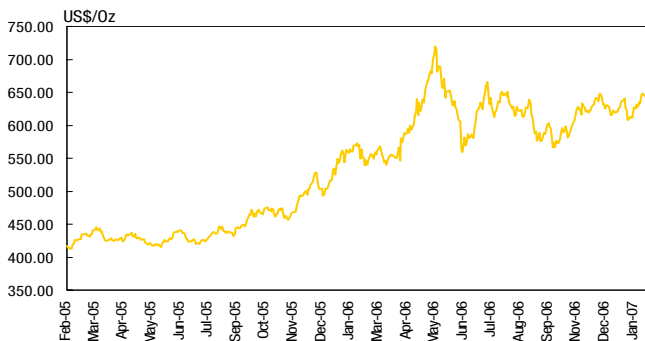
In its 3QFY07 monetary policy review, the RBI hiked the repo rate by 25bps to 7.5% but kept all other rates unchanged. In addition, it announced sector specific measures to address asset price increases. These measures are positive and in line with the RBI's objective of removing monetary accommodation, liquidity mgmt and keeping a check on credit quality.

Trends in Reverse Repos/Repos (Rs bn)



Repo bids fell to Rs100bn from Rs122bn in the previous week while the average reverse repo bids rose to Rs14bn from Rs2bn reflecting a net liquidity injection of Rs86bn

Trends in Commodities – Gold(US\$/Oz)



Gold ended at US\$648.25/oz from US\$645.35/oz with trading driven mainly by technicals which saw gold touch a 6-month high above US\$660 intra-week

Source: Reuters; Bloomberg; Citigroup

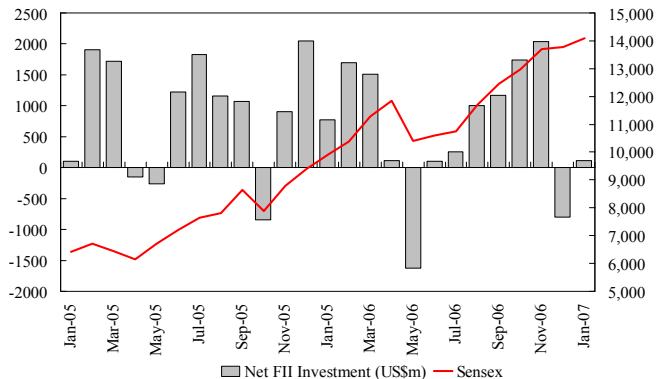
Standard & Poors (S&P) Raises India Ratings to Investment Grade

	S&P*	Moody's**	Fitch***
Long term Foreign Currency	BBB-	Baa3	BBB-
Short term Foreign Currency	A-3	-	B
Long term Local Currency	BBB-	Ba2	BBB-
Short term Local Currency	A-3	-	Not rated
Long Term Outlook			
Sovereign outlook (FC)	Stable	Stable	Stable
Sovereign outlook (local)	Stable	Stable	Stable

*Ratings and outlook effective Jan 2007. ** Ratings effective Jan 2004, Outlook effective May 2006. ***Ratings effective Aug 2006

S&P raised India's foreign and local currency ratings to Investment Grade. The investment grade rating comes after a gap of 15 years and bodes well for the India sustaining growth over 8%+ levels...as it will lower the cost of financing, lead to more inflows and is in line with our rupee appreciation view.

Trends in FII Flows, Two Years (US\$ m)



Equities saw FII outflows to the tune of US\$72mn for the trading week ended Feb 2nd. Fiscal YTD, total FII flows amounted to US\$4.1bn, as compared with US\$7.7bn during the same period last year.

Trends in Commodities – Oil (US\$/bbl)



Brent continued to edge higher touching US\$57.25/bbl from US\$55.50/bbl in the previous week. This was on the back of forecast for Cold US weather and political concerns from Nigeria and Iran which provided supply concerns

India- Market Monitor

	Units	Latest	Previous	1M ago	3M ago	12M ago
Interest Rates						
Overnight	%	7.9	8.10	6.20	7.00	6.80
1 year Treasury Bill	%	7.7	7.27	7.19	6.99	5.66
1 year OIS	%	7.59	7.57	5.84	6.90	6.48
1 year MIFOR	%	8.82	8.85	5.84	7.21	6.92
5 year Corp AAA spread over GOI	%	1.32	1.20	0.65	0.97	0.59
10 year GOI	%	7.69	7.88	7.18	7.60	7.39
Currency & Reserves						
USD/INR		44.12	44.24	45.09	44.89	44.26
EUR/USD		1.30	1.30	1.18	1.28	1.210
USD/JPY		120.98	120.45	117.92	116.92	117.52
12 Month INR Forward Premium	%	3.08	3.16	2.94	1.72	1.80
FX Assets – excl gold - As On (26 Jan 07)	US\$ bn.	172.0	171.1	170.2	160.2	133.3
Money & Banking						
Credit-Deposit Ratio	%	73.9	73.8	73.8	72.2	69.5
Money Supply - M3	% YoY	21.1	20.4	19.4	18.6	16.4
Inflation - WPI (20 Jan 07)	% YoY	6.11	5.95	5.48	5.61	4.19

Source: Citigroup; RBI.

Financial Market Forecasts

Currency Forecasts and Forwards

	Range in Jan	Spot	1 Month		3 Months		6 Months		12 Months	
		1-Feb	Forecast	Forward	Forecast	Forward	Forecast	Forward	Forecast	Forward
Versus USD										
Japan YEN	118.59-121.91	120.56	121.00	120.10	120.00	119.10	120.00	117.70	118.00	115.07
Euro EUR	1.2891-1.3278	1.3033	1.2800	1.3050	1.2600	1.3083	1.2600	1.3127	1.2400	1.3198
India INR	44.11-44.54	44.05	44.00	44.20	43.75	44.39	43.50	44.61	43.00	45.05
China RMB	7.7709-7.8162	7.7588	7.7300	7.7195	7.6300	7.6425	7.5000	7.5480	7.3000	7.3700

Source: Reuters, Citigroup estimates.

Interest Rate Forecasts

	Range in Jan	1- Feb	1Q07	2Q07	3Q07	4Q07	
US	Fed Fund Rate	5.25 - 5.25	5.25	5.25	5.25	5.00	5.00
	10-Year Treasuries	4.60 - 4.89	4.81	4.80	4.90	4.95	4.95
EU	Repo Rate	3.5 - 3.5	3.50	3.50	3.50	3.50	3.75
	10-Year Bunds	3.93 - 4.11	4.10	3.90	3.90	3.95	3.95
JP	Call Money	0.22 - 0.395	0.27	0.50	0.50	0.50	0.75
	10-Year JGBs	1.65 - 1.76	1.71	1.75	1.85	1.95	2.00
IN	Reverse Repo Rate	6 - 6	6.00	6.25	6.25	6.25	6.25
	91-Day T Bill	7.14 - 7.56	7.56	6.75	6.75	6.75	6.75
CN	PBOC base rate (3-Month)	6.12 - 6.12	6.12	6.12	6.39	6.39	6.39
	Bond repo rate (7-Day)	1.34 - 2.07	2.04	1.50	1.90	2.00	2.20
	Govt Bond Yield (5 Year)	2.58-2.64	2.64	2.75	2.80	2.95	3.00

Source: Datastream, CEIC Data Company Limited, Bloomberg, Moneyline Telerate, Citigroup estimates.

Disclosure Appendix

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