India Macroscope

Reforms – Rearguard Not Roaring

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

- **Policy support – Could see more of it both at global and India level —** Global growth prospects have deteriorated, reflecting not just the European crisis but also a broad-based slowdown in emerging markets, including China. We see greater policy support both at the global and India level. This should be positive.

- **Why India needs it? —** India is hugely and intrinsically linked to global financial markets. Trade matters less. With limited fiscal or monetary maneuverability, the economy is more vulnerable to global developments. This, along with a weak currency, rating action and the RBI's stress on supply-side imbalances, significantly shifts the onus onto the government to deliver change.

- **Will the change of guard at the finance ministry make this happen? —** We see greater action, but not as much as the market may be inferring. Structurally, not much has changed: the dual leadership model in the government remains intact and consequently non-populist reforms may not be implemented. Nonetheless, small fuel price hikes, coupled with measures that are largely execution in nature, could make the environment conducive for investment.

- **Monsoons a risk to GDP, inflation and deficits —** If monsoons remain weak: (1) *GDP* could be impacted by 40-80bps, to 5.6-6% from 6.4% currently; (2) *Inflation* – Our 7.5% average WPI estimate could be breached – key to note is the interplay of domestic (structural drivers, MSPs) and global factors (commodities and currencies) impacting inflation; (3) *Fiscal* – The slippage could be higher than earlier expected due to relief measures as well as higher consumption of diesel, which could increase fuel subsidy.

- **Rates and the rupee** — Given the RBI's focus on inflation and addressing supply-side imbalances, our 50-75bp rate cut call for the year is contingent on government policy action. On the rupee, a narrowing CAD (due to oil and gold) will likely keep the unit range-bound at 54-55.5 over a 12-month horizon.

Figure 1. India — Macro Snapshot (%)

Year -end 31 March	FY07	FY08	FY09	FY10	FY11	FY12	FY13E	FY14E
Real GDP growth (%)	9.6	9.3	6.7	8.4	8.4	6.5	6.4	6.9
Agriculture growth (%)	4.2	5.8	0.1	1.0	7.0	2.8	3.0	3.0
Industry growth (%)	12.2	9.7	4.4	8.4	7.2	3.4	4.1	4.5
Services growth (%)	10.1	10.3	10.0	10.5	9.3	8.9	8.3	8.9
Fiscal Deficit (Centre+States)	-5.4	-4.1	-8.4	-9.7	-8.3	-8.4	-8.0	-8.0
Current Account Deficit	-1.0	-1.3	-2.3	-2.8	-2.7	-4.2	-3.5	-2.6
WPI (Average)	6.5	4.8	8.0	3.6	9.6	8.8	7.5	7.0
INR/USD (Average)	45.2	40.2	46.0	47.4	45.6	48.1	55.0	54.0

Source: CSO, Budget Documents, RBI, Citi Research

Contents

Statistical Snapshot

Figure 2. India – Macroeconomic Summary, FY00-14E (%)

Year to 31 March	FY01	FY02	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13E	FY14E
National Income Indicators*														
Nominal GDP (Rs bn)	21,840	23,676	25,500	28,617	32,422	36,934	42,947	49,871	56,301	64,574	76,741	88,558	101,399	116,609
Nominal GDP (US$ bn)	478	493	528	623.5	720.5	833.7	950.2	1240.6	1223.9	1362.3	1683.7	1,841	1,844	2,159
Per Capita GDP (US$)	469	474	500	582	662	754	847	1,090	1,061	1,163	1,416	1,526	1,505	1,711
Real GDP growth (%)	4.4	5.8	3.8	8.5	7.6	9.5	9.6	9.3	6.7	8.4	8.4	6.5	6.4	6.9
Agriculture growth (%)	-0.2	6.3	-7.2	10.0	1.6	5.1	4.2	5.8	0.1	1.0	7.0	2.8	3.0	3.0
Industry growth (%)	6.4	2.7	7.1	7.4	9.4	9.7	12.2	9.7	4.4	8.4	7.2	3.4	4.1	4.5
Services growth (%)	5.7	7.2	7.5	8.5	9.4	10.9	10.1	10.3	10.0	10.5	9.3	8.9	8.3	8.9
By Demand * (%YoY)														
Consumption	3.0	5.3	2.3	5.4	2.3	8.6	7.9	9.3	7.6	8.1	8.1	5.4	5.8	6.7
Pvt Consm	3.4	6.0	2.9	5.9	2.1	8.5	8.7	9.2	7.1	7.0	8.1	5.5	6.0	6.7
Public Consm	0.9	2.3	-0.4	2.6	3.4	8.9	3.8	9.6	10.4	14.3	7.8	5.1	5.0	7.0
Gross Fixed Capital Formn	0.0	7.4	6.8	13.6	20.7	16.2	13.8	16.2	3.5	6.8	7.5	5.6	5.5	8.0
Cons; Invst, Savings ** (%GDP)														
Consumption	78.5	78.9	77.2	75.0	70.3	69.3	68.3	67.4	68.8	69.4	68.4	67.7	67.0	66.0
Gross Capital Formation	23.8	22.3	24.6	26.9	32.8	34.7	35.7	38.1	34.3	36.1	35.8	35.5	36.0	36.0
Gross Domestic Savings	23.2	22.9	25.7	29.1	32.4	33.4	34.6	36.8	32.0	33.8	32.3	32.0	32.5	33.0
Real Indicators (%YoY)														
Cement despatches (domestic)	-1.9	9.8	8.7	5.8	8.1	10.1	10.2	9.8	8.5	11.2	5.2	7.0	8.0	9.0
Commercial vehicle sales	-11.9	-4.5	28.0	36.2	22.4	10.1	33.3	4.2	-21.4	39.2	27.0	19.5	5.0	10.0
Car sales	-5.3	3.2	7.8	27.2	17.8	7.7	20.7	12.1	0.3	25.7	29.3	3.9	5.0	20.0
Two-wheelers	0.7	15.3	17.0	11.3	15.7	13.6	11.5	-7.8	2.7	25.9	25.8	13.9	6.0	10.0
Diesel consumption	-3.4	-3.7	0.3	1.2	6.9	1.4	6.7	11.1	8.5	8.9	6.5	8.0	8.0	8.0
Mobile Tele density	0.3	0.6	1.3	3.1	4.8	8.2	14.1	22.0	33.0	48.9	66.8	75.1	79.0	81.9
Monetary Indicators (% YoY)														
Money supply	16.8	14.1	14.7	16.8	12.0	21.4	21.3	21.1	19.3	16.7	16.0	16.0	16.0	17.0
Inflation – WPI (Avg)	7.1	3.6	3.4	5.5	6.5	4.4	6.5	4.8	8.0	3.6	9.6	8.8	7.5	7
CPI (Avg)	3.7	4.3	4.1	3.8	3.9	4.2	6.8	6.2	9.1	13.0	7.0	6.5	5.0	6.0
Bank credit growth	17.3	15.3	23.7	15.3	30.9	37.0	28.1	22.3	17.5	16.7	21.5	17.0	17.0	17.0
Deposit growth	18.4	14.6	16.1	17.5	13.0	24.0	23.8	22.4	18.0	17.0	16.0	16.0	16.0	16.0
Fiscal Indicators (% GDP)														
Centre's fiscal deficit)	-5.4	-6.0	-5.7	-4.3	-3.9	-4.0	-3.3	-2.5	-6.0	-6.5	-4.9	-5.9	-5.5	-5.5
State fiscal deficit	-4.0	-4.1	-3.9	-4.2	-3.3	-2.4	-1.8	-1.5	-2.4	-2.9	-2.7	-2.5	-2.5	-2.5
Combined deficit (Centre+State)	-9.1	-9.5	-9.1	-8.1	-7.2	-6.5	-5.4	-4.1	-8.4	-9.6	-8.3	-8.4	-8.0	-8.0
Off Balance Sheet Items	-	-	-	-	-	-0.5	-0.9	-0.6	-1.7	-0.2	0.0	0.0	0.0	0.0
Combined liabilities (dom+ext)	77.1	82.0	85.5	85.4	85.2	83.0	79.3	76.1	76.1	75.0	71.3	70.5	69.2	69.2
External Sector (% YoY)														
Exports (US$bn)	45.5	44.7	53.8	66.3	85.2	105.2	128.9	166.2	189.0	182.4	250.5	309.8	346.9	395.5
% YoY	21.1	-1.6	20.3	23.3	28.5	23.4	22.6	28.9	13.7	-3.5	37.3	23.7	12.0	14.0
Imports (US$bn)	57.9	56.3	64.5	80.0	118.9	157.1	190.7	257.6	308.5	300.6	381.1	499.5	537.0	590.7
%YoY	4.6	-2.8	14.5	24.1	48.6	32.1	21.4	35.1	19.8	-2.6	26.7	31.1	7.5	10.0
Trade deficit (US$bn)	-12.5	-11.6	-10.7	-13.7	-33.7	-51.9	-61.8	-91.5	-119.5	-118.2	-130.6	-189.8	-190.1	-195.2
Invisibles (US$bn)	9.8	15.0	17.0	27.8	31.2	42.0	52.2	75.7	91.6	80.0	84.6	111.6	125.4	138.7
Current Account Deficit (US$bn)	-2.7	3.4	6.3	14.1	-2.5	-9.9	-9.6	-15.7	-27.9	-38.2	-45.9	-78.2	-64.7	-56.4
% to GDP	-0.6	0.7	1.2	2.3	-0.3	-1.2	-1.0	-1.3	-2.3	-2.8	-2.7	-4.2	-3.5	-2.6
Capital Account (US$bn)	8.8	8.6	10.8	16.7	28.0	25.5	45.2	106.6	6.8	51.6	62.0	67.8	60.6	59.6
% GDP	1.9	1.7	2.1	2.7	3.9	3.1	4.8	8.6	0.6	3.8	3.7	3.7	3.3	2.7
Forex Assets (excl gold) (US$bn)	39.6	51.0	71.9	106.1	135.1	145.1	191.9	299.1	241.6	252.8	273.7	260.9	256.8	260.0
Months of imports	8.2	10.9	13.4	15.9	13.6	11.1	12.1	13.9	9.4	10.1	8.6	6.3	5.7	5.3
External Debt (US$bn)	101.3	98.8	104.9	112.7	134.0	139.1	172.4	224.4	224.5	261.0	250.5	309.8	346.9	395.5
Short Term Debt	3.6	2.7	4.7	4.4	17.7	19.5	28.1	45.7	43.3	52.3	37.3	23.7	12.0	14.0
Exchange Rate														
US$/INR - annual avg	45.7	48.0	48.3	45.9	45.0	44.3	45.2	40.2	46.0	47.4	45.6	48.1	55.0	54.0
% depreciation	5.3	5.0	0.6	-5.0	-2.0	-1.6	2.0	-11.1	14.4	3.0	-3.8	5.5	14.3	-1.8
US$/INR - year end	46.5	48.9	47.5	43.6	43.8	44.6	43.6	40.1	50.7	44.9	44.6	50.3	55.0	53.1
% depreciation	6.7	5.2	-2.9	-8.2	0.3	2.0	-2.3	-8.0	26.4	-11.4	-0.7	12.8	9.3	-3.5

** At current prices. Source: CSO, RBI, Ministry of Finance and Citi Research

Theme – Reforms: Rearguard Not Roaring

Global growth blues – EA recession and EM slowdown

Figure 3. GDP Fcsts (%YoY)

	2011	2012F	2013F
Global	3.6	3.0	3.2
US	1.7	2.1	2.0
Japan	-0.7	2.7	1.4
Euro Area	1.5	-0.7	-0.8
Australia	2.0	3.7	3.4
UK	0.6	-0.4	0.6
Emerging Mkts	6.0	4.9	5.5
Brazil	2.7	2.3	4.5
Russia	4.3	3.5	4.0
India (2011=FY12)	6.5	6.4	6.9
Indonesia	6.5	6.1	6.3
China	9.2	7.8	7.9
South Africa	3.1	2.7	3.6
Turkey	8.5	2.5	4.3

Source: Citi Research; GEOS June 12

Over the last month, global growth prospects have worsened resulting in our team cutting global growth forecasts for both 2012 and 2013 - the second consecutive monthly downgrade (see June 2012), with estimates below consensus forecasts.

EA Recession: Our team remains gloomy on euro area prospects and expects a recession in both 2012 and 2013 amidst high financial market strains, the likelihood that both Italy and Spain will need bailouts for their sovereign debt and a 50-75% probability of a Grexit. Economic weakness is likely to hit revenues and cause government debt/GDP ratios to overshoot official forecasts in most periphery countries and create continued widespread doubts about medium-term fiscal prospects. All this worsens the vicious circle between weak economies, capital-weak banks and fiscally-weak governments.

US – Growth continuing at a disappointing pace: While the cyclical upturn remains on a sluggish 2% track, recent data points such as the ISM manufacturing index plunging to sub-50 levels, weak core retail sales and deteriorating consumer confidence are disappointing. Moreover, concern remains over financial spillovers from the Eurozone crisis and the ongoing uncertainties surrounding the "fiscal cliff".

EM slowdown – More broad-based than expected: Over the past month, there have been substantial downgrades to our EM 2012-13 growth forecasts including Brazil, China, India, Indonesia, Hungary, Korea and South Africa. The causes of these downgrades vary, but the common pattern is a mix of (1) past tightening, (2) softer economic data, (3) adverse spillovers from the EMU crisis, and (4) the gradual pace of policy stimulus. However, the biggest worry in the EM world is China. Despite policy efforts to "stabilize growth", China's domestic-demand-led slowdown was more than expected in 2Q. While there is hope based on cyclical policy easing, the recovery is likely to be shallow prompting our team to cut their 2012 and 2013 GDP estimates to 7.8% and 7.9% from 8.1% and 8.5% respectively.

Policies – Monetary easing; positive EU summit

Monetary Easing Ahead

ECB: likely to resume LTRO

Fed: QE likely if recovery falters

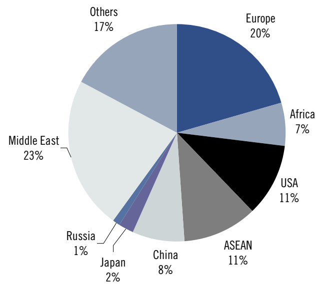
UK: QE likely in July meeting

China: Two rate cuts and two RRR cuts

Against this background, our team continues to expect further widespread monetary policy loosening in coming months. The ECB is likely to cut rates by 0.25% at the July meeting, and will probably resume its multi-year LTRO programme soon after. For the US, the Fed's decision to extend Operation Twist may not be the last easing step, and extra QE will be likely if recovery appears threatened or the outlook deteriorates significantly further. The UK is likely to restart QE at the July meeting. For China, additional policy measures this year could include two more rate cuts to boost demand and two more RRR cuts to bring money growth to 14%.

EA/EU Summit – Positive, yes, but conditions preventing a breakup unfulfilled: The outcome of the June 28-29 Summit exceeded very low market expectations with the EA/EU leaders not just signing off on the already-agreed '€120bn Growth Compact', but making more progress towards banking union and also hinting at some measures that could provide short-term relief for the Spanish and Italian sovereign debt markets (See Did Summit Avoid Nadir?). However, our team believes that many key necessary conditions for preventing a break-up of the EA remain unfulfilled. These include (1) boosting the inadequate size of the fiscal rescue facilities and providing a credible funding backstop (2) EA/EU wide bank resolution regime/recapitalization fund (3) EA-wide deposit guarantee scheme that would also insure against redenomination risk and (4) ways to enhance the legitimacy and accountability of the supranational institutions (ECB/ESM) that stand to gain the additional authority and new powers.

Figure 4. Direction of Trade (%)



Source: Citi Research

Impact on India – More via financial channels than trade

As is well known, the interplay of the four deficits (current account, fiscal, liquidity and governance) has taken its toll on the India story with growth slowing to a nine-year low. As mentioned earlier (See India Macroscope - Deficits – Not Twins, But Quadruplets), an aggressive thrust on policy and execution reform is key to reversing the slowdown. While the slowdown is predominantly due to domestic factors, the worry is that with limited fiscal or monetary maneuverability, the economy is relatively more vulnerable to global developments.

Direct trade channels are weak

India is largely a domestic-oriented economy with merchandise exports comprising 17% of GDP. The share of EU has moderated from close to 30%+ of total exports in the early 1990s to 17.6% currently. While the 25% depreciation in the currency does limit direct damage in terms of trade linkages, nonetheless, recessionary conditions will impact exports. We have tempered our FY13 export growth forecasts to 12%YoY from 17% expected earlier v/s the 24% growth seen in FY12.

…But financial markets are integrated

Figure 5. India – External Debt Snapshot (US$bn)

	FY08	FY09	FY10	FY12
Multilateral	39.5	39.5	42.9	50.5
Bilateral	19.7	20.6	22.6	26.8
IMF	1.1	1.0	6.0	6.2
Trade Credit	10.3	14.5	16.9	19.9
Commercial Borrowing	62.3	62.5	70.8	104.4
NRI Deposits(>1year)	43.7	41.6	47.9	58.6
Rupee Debt	2.0	1.5	1.7	1.4
Total Long term debt	**178.7**	**181.2**	**208.7**	**267.6**
FII Invst in T-Bills	0.7	2.1	3.4	9.4
Others(trade related)	41.9	39.9	47.5	65.1
Other	3.2	1.3	1.5	3.7
Total Short term debt	**45.7**	**43.3**	**52.3**	**78.2**
GROSSTOTAL	**224.4**	**224.5**	**261.0**	**345.8**

Source: MoF; RBI

Although India's trade linkages are limited, its external financing needs remain high (current account deficit + debt repayments). Thus if the current risk-on situation reverses, this could impact India via higher funding costs and lower capital flows.

Reserve adequacy – India relatively vulnerable to flows: In a study done by our regional economist – Johanna Chua, the external liquidity situation of India looks vulnerable to a protracted period of lower global capital inflows due to the sizeable increase of the CAD, forex reserve erosion and domestic policy risks that exacerbated confidence (See Re-Assessing Foreign Currency Reserve Adequacy Metrics).

Adequacy ratios include:

(a) total reserves as a ratio of short-term debt by remaining maturity and the current a/c deficit;

(b) potential drain from foreign holdings in stocks and bonds.

Given this backdrop, we believe while India is relatively better placed in terms of its low exports/GDP, domestically financed fiscal deficit, captive demand for government bonds, and limited exposure to foreign liabilities, India does tend to come on the radar in an environment of risk aversion due to its high fiscal and current account deficits and reliance on external capital.

Figure 6. Asia – Selected FX Reserve Coverage Ratios

In US$bn	CH	ID	IN	KR	MY	PH	TH	TW
A. Latest FX Reserves	**3,305.0**	**111.5**	**285.9**	**310.9**	**136.0**	**76.0**	**179.0**	**389.3**
B.Net Forward Book	0	-0.1	-3.5	29.0	9.2	7.5	32.4	0.0
C. Total Res (TR) = A+B	**3305.0**	**111.4**	**282.4**	**339.9**	**145.2**	**83.5**	**211.4**	**389.3**
D. ST Debt by <1yr Maturity*	475.7	31.1	78.1	136.3	63.9	9.0	48.6	107.8
E. Amortizations	38.8	29.3	15.6	46.0	9.3	8.5	8.7	6.2
F.ST Debt by Rem Mat (D+E)	**514.5**	**60.4**	**93.7**	**182.3**	**73.2**	**17.5**	**57.3**	**114.0**
G. CAD (Avg of 2012/13F)	**-155.8**	**16.4**	**76.6**	**-10.4**	**-30.5**	**-7.3**	**3.5**	**-42.4**
H. Total Ext Financing (F+G)	**358.7**	**76.8**	**170.2**	**172.0**	**42.7**	**10.3**	**60.8**	**71.6**
TR /ST Debt By Rem. Mty	6.4	1.8	3.0	1.9	2.0	4.8	3.7	3.4
TR /Total Ext Fin Req (C/H)	**9.2**	**1.4**	**1.7**	**2.0**	**3.4**	**8.1**	**3.5**	**5.4**
Foreign Bond Holdings >1yr	0.0	22.3	43.0	69.0	36.7	1.5	8.0	0.0
FH of equities	30.0	162.7	174.1	288.0	91.3	95.3	77.1	140
TR/ (TEF + 20% of FH of bonds & stocks)	**9.1**	**1.0**	**1.3**	**1.4**	**2.1**	**2.8**	**2.7**	**3.9**

Source: Citi Research, CB data (using SDDS template where available), CEIC, IIF, BIS, Moody's, Korea FSC

Onus on policy - Will a change of guard help?

Presidential Elections – Significance

Importance: India follows a parliamentary form of govt…

…However, the presidential election due on July 19 has assumed significance largely because most political analysts are predicting another coalition govt in the 2014 General Election…

…. This makes the role of the President crucial as in a hung parliament the President has discretion to appoint the Prime Minister but that discretion is limited to the choice of one who in the opinion of the President is capable of winning the confidence of the House.

Policy paralysis – A quick recap: Weak fundamentals on the macro front have been exacerbated by a lack of policy decisiveness and the diminishing popularity of the incumbent UPA, as seen in recent state elections. Moreover, allegations of corruption have been negative for sentiment and investment projects. Concerns are rising that the dual leadership model of the Congress that worked well in the past may not prove very successful this time around (See *India Macroscope: Tough Times = 12 Tough Tasks to Sustain Growth at ~7% in 2012)*. Policy uncertainty and governance deficit are issues that need to be resolved first – and are imperative for other macro parameters to be corrected, in our view.

What's new? Although the party position in Parliament remains status quo, the key development over the last month has been the change of guard in the Finance Ministry. With the former FM Pranab Mukherjee now standing for Presidential election, PM Manmohan Singh has taken over charge of the Finance Ministry. Expectations are running high for Dr Singh to bring the economy back to a high-growth path and restore confidence. The reasons are: (1) Dr Singh's first term as Finance Minister in 1991-96 resulted in liberalization and far-reaching changes; and (2) The potential conflicts of interest as a coalition manager and FM required taking tough decisions.

Have things really changed? Some political commentators don't believe so. Questions have been raised about who wields real power, which is why some think the emphasis on welfare and subsidies will continue – steering clear from reforms that alienate a few losers in the short term even though they could produce winners in the long term. Moreover, as seen in the past, there has never been a lack of conviction by the leadership, but merely a lack of political will.

Figure 7. Current Structure of the Government at the Centre

Party	State	Seat	Party	State	Seats
Congress	All India	207	BJP		116
Trinamool Congress	W Bengal	19	Janata Dal (U)		20
DMK	Tamil Nadu	18	Shiv Sena	MH	11
NCP	MH	9	SAD	Punjab	4
J&K National Conf	J&K	3	TRS	AP	2
Indian Muslim League		2	Left Demo. Front	Kerala	24
Jharkhnd Vikas Morcha	Jharkhand	2	Biju Janata Dal	Orissa	14
Rashtriya Lok Dal	UP	5	AIADMK	TN	9
Others/independents		12	TDP	AP	6
UPA		**277**	Janata Dal	Karntaka	3
Supporting Parties			Others		8
Samajwadi Party (SP)	UP	22	**Total**		**217**
Bahujan Samaj Party	UP	21			
Rashtriya Janata Dal	Bihar	4			
Total		**47**			
UPA incl. Outside Support		**324**	**TOTAL**		**541**

Source: Election Commission of India

Figure 8. Composition of the Rajya Sabha – Party-Wise Position

Party	Strength	Party	Strength
Congress	71	Bharatiya Janata Party	51
DMK	7	Janta Dal (United) (JD(U))	8
Nationalist Congress Party	7	Shiv Sena (SS)	4
Trinamool Congress (TMC)	6	Shiromani Akali Dal (SAD)	3
J&K National Conference	2	Indian National Lok Dal	1
Rashtriya Lok Dal (RLD)	1	Asom Gana Parishad	2
UPA	**94**	**Total NDA**	**69**
Supporting Parties		**Left Parties**	**34**
Bahujan Samaj Party (BSP)	18		
Samajwadi Party (SP)	5	Nominated	5
Rashtriya Janata Dal (RJD)	4	Other Parties/Independents	6
Bodoland People's Front (BPF)	1		
Lok Janasakti Party (LJP)	1		
Sikkim Democratic Front (SDF)	1		
Nagaland People's Front (NPF)	1		
Mizo National Front	1		
UPA incl Outside Support	**126**	**TOTAL RAJYA SABHA**	**240**

Source: www.rajyasabha.nic.in

Pending reforms – What can one realistically expect?

Inheriting a slowing economy with elevated inflation and low levels of confidence, Dr Singh clearly has his hands full. Given the setback to one of the allies that has stymied several reforms such as raising FDI limits in insurance, aviation, retail; pension reforms; land acquisition; fuel price changes; railway tariff hikes etc, there is some hope that the next few months could see a bit of thawing on the policy front. However, as is well known, unless there is full political support, it will be difficult to push through painful reforms. But there are a host of measures that are largely execution in nature, which if implemented could make the environment conducive for investment and help reduce the number of projects being stalled. These include:

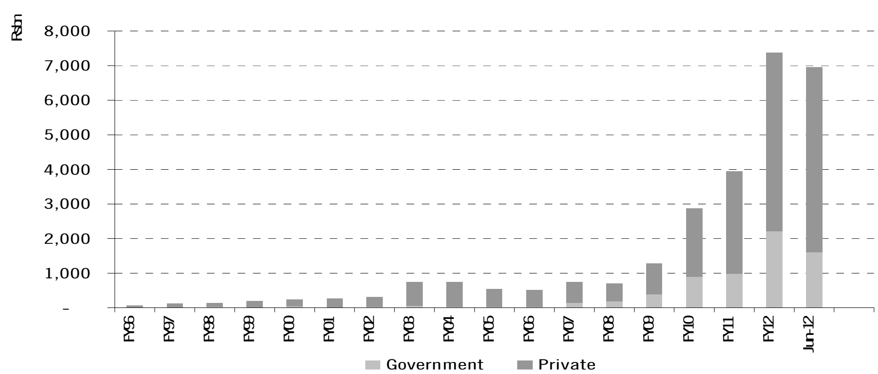
1. Addressing coal availability concerns and SEB losses in power
2. Clarity on land acquisition and sorting out mining issues
3. Fast tracking clearances on infrastructure investments in the oil space, Delhi Mumbai Industrial Corridor
4. Clearing doubts on the inconsistencies in the taxation policy both on retrospective taxation and GAAR
5. Clarity on spectrum pricing in the telecom space
6. Enhancing capital flows through a commercial dollar bond issuance
7. Implementing Fiscal Reforms – GST; Use of Aadhar for minimizing subsidies
8. Raising FDI Limits in various sectors

INVST PICK-UP: CRITICAL FACTOR

It is now widely recognized that the deceleration has been due to a slowing in investments

The RBI has emphasized that '*the main reason for the apparent decline in the trend rate of growth relative to the pre-crisis period is the emergence of significant supply bottlenecks on a variety of fronts – infrastructure, energy, minerals and labor*'

Figure 9. Trends in projects under implementation which have been stalled



Source: CMIE

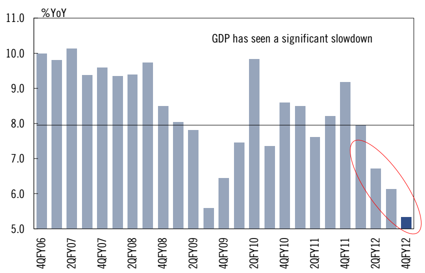
Diesel price hikes are crucial given that it accounts for ~62% of under-recoveries.

What about fuel price hikes? Oil companies are losing ~Rs400/LPG cylinder; Rs31/ltr on kerosene and Rs10/ltr on diesel. While de-regulation is clearly ruled out, partial price hikes especially on diesel would go a long way in not only signaling a move that the government is taking steps in alleviating demand-supply imbalances but also reducing the subsidy bill. (Under-recoveries for FY13 are estimated at Rs1.52trn – and incorporate modest price hikes in regulated fuels i.e Rs4/ltr in diesel, Rs70/cylinder for LPG and ~Rs2/ltr in kerosene. If there are no price hikes, the under-recoveries would touch Rs1.78trn.) Key to note is that diesel losses account for 62% of losses.

Real Indicators

FY12 growth at a nine-year low; Trends to remain bleak

Figure 10. Trends in Qtrly GDP Growth (%)

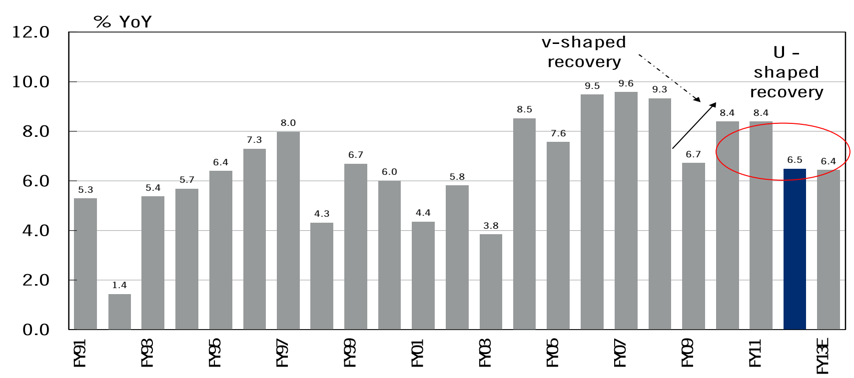


Source: CSO; Citi Research

FY12 GDP – A nine-year low: India's 4QFY12 GDP came in at 5.3% YoY – the lowest quarterly reading in the current GDP series – even during the 2008-09 global crisis, quarterly GDP growth had troughed to 5.6%. The slowdown in 4QFY12, coupled with revisions to previous data, resulted in the govt's advance GDP estimate for FY12 being revised down to 6.5% from 6.9%.

FY13 outlook – Agriculture, a wild card: Looking ahead, we expect growth in FY13 to edge marginally lower to 6.4%YoY. Our assumptions factor in: (1) Agri growth at the trend rate of 3%, monsoons remains a wildcard. Poor agriculture growth could result in headline GDP coming in the 5.6-6% range; (2) Industry growth remaining lackluster at 4.1% - policy reforms would be key to an uptick as execution-related challenges are resulting in an increase in stalled projects; and (3) Services decelerating due to slowing trends in trade and banking services.

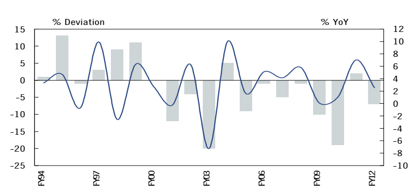
Figure 11. Trends in Annual GDP (%)



Source: CSO; Citi Research

Headwinds to FY13 numbers — Monsoons, global woes

Fig 12. Trends in Rainfall and Agri Growth (% LPA, %YoY)



Source: IMD; CSO

Monsoons – Monsoons have had a poor start, with cumulative rainfall in June being ~30% below normal. While the Met dept is predicting normal monsoons for July – the crucial month of sowing, reports also indicate that the growing likelihood of an El-Nino event. This leads to a warming of Sea Surface Temperatures leading to lower rainfall.

Despite the changing composition of GDP (share of agri at 15% v/s 30%) and mitigating factors such as NREGA, growing share of winter crop, use of gold as collateral, the economy is not yet water-proof. (1) Agriculture employs ~50% of the workforce and only ~36% of India's land area is irrigated. (2) Rainfall correlation with agri is (0.63) and private consumption (0.4). A poor monsoon could result in GDP coming in at 5.6%-6%. (see Monsoon Watch – Clear Skies, Cloudy Outlook)

Figure 13. Sensitivity of GDP to Agriculture Growth (%)

							FY13E		
	Wts*	FY08	FY09	FY10	FY11	FY12	Normal Monsoon	Weak Monsoon	Bad Monsoon
Agriculture	14.4	5.8	0.1	1.0	7.0	2.8	3.0	0.0	-3.0
Industry	27.9	9.7	4.4	8.4	7.2	3.4	4.1	4.1	4.1
Services	57.7	10.3	10.0	10.5	9.3	8.9	8.3	8.3	8.3
GDP	**100.0**	**9.3**	**6.7**	**8.4**	**8.4**	**6.5**	**6.4**	**6.0**	**5.6**

Source: CSO, Citi Research

- **Global woes** – Global growth forecasts have been shaved off for two consecutive months and our team maintains the view that Greece would leave EMU in early 2013. This would be followed by policy responses aimed at limiting adverse spillovers. Nonetheless, global developments could impact India through 3 key channels: (1) Real economy via exports; (2) Banking Sector via higher funding costs; and (3) Portfolio Flows - fall in global risk appetite could result in lower flows to a capital dependent economy like India's.

Figure 14. Trends in Annual GDP (%YOY)

	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13E
Agriculture	5.1	4.2	5.8	0.1	1.0	7.0	2.8	3.0
Industry	9.7	12.2	9.7	4.4	8.4	7.2	3.4	4.1
Services	10.9	10.1	10.3	10.0	10.5	9.3	8.9	8.3
Consumption	**8.6**	**7.9**	**9.3**	**7.6**	**8.1**	**8.1**	**5.4**	**5.8**
% to GDP	69.9	69.0	68.7	71.1	71.0	70.1	69.1	68.4
Private Consumption	8.5	8.7	9.2	7.1	7.0	8.1	5.5	6.0
Public Consumption	8.9	3.8	9.6	10.4	14.3	7.8	5.1	5.0
Gross Capital Formation	**16.2**	**13.4**	**18.1**	**-5.2**	**15.6**	**11.1**	**5.5**	**5.4**
% to GDP	34.9	36.2	39.0	35.6	38.0	38.5	38.0	37.4
Fixed Capital Formation	**16.2**	**13.8**	**16.2**	**3.5**	**6.8**	**7.5**	**5.6**	**5.5**
% to GDP	30.5	31.8	33.7	33.5	33.1	32.5	32.1	31.6
Net Exports (% to GDP)	-3.2	-3.8	-4.7	-7.2	-7.0	-6.0	-7.4	-6.3
GDP	**9.5**	**9.6**	**9.3**	**6.7**	**8.4**	**8.4**	**6.5**	**6.4**

Source: CSO: Citi Research

Rating Agencies/RBI put growth ball in govt's court

During the last few months, S&P and Fitch have revised their sovereign outlooks on India from stable to negative. While previous concerns on India have largely focused on its twin deficits – current account and fiscal - both Fitch and S&P in their much talked about "Will India *become the first 'fallen angel' among the BRIC nations"* report highlight slowing growth and its impact on fiscal consolidation coupled with political roadblocks as key factors behind the outlook change. While Moody's has maintained its stable outlook has said that "it is predicated that there will be some policy effort to curtail the primary deficit ….although a turnaround in fiscal trends is unlikely without a turnaround in growth"

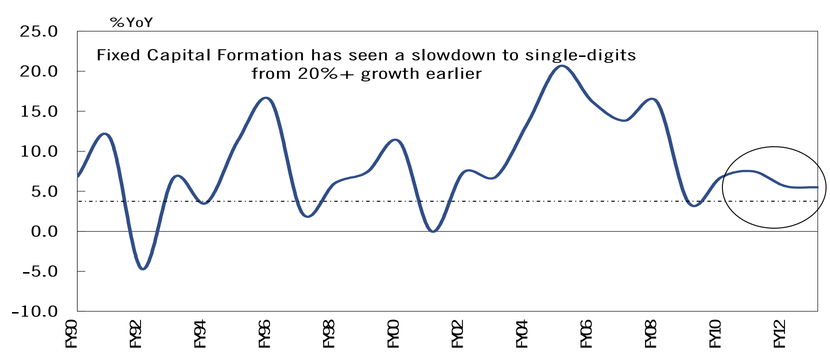
Figure 15. India — Sovereign Ratings

	S&P	Moody's	Fitch
LT Foreign Currency	BBB-	Baa3	BBB-
LT Local Currency	BBB-	Baa3	BBB-
Outlook (FC)	Negative	Stable	Negative

Source: Rating Agencies

Bottom line: These rating actions, coupled with the RBI's latest policy stressing on the need to address supply-side imbalances, once again put the onus on the govt to create a positive investment environment.

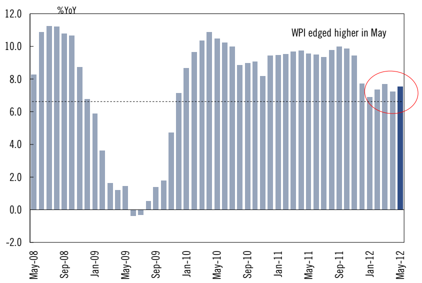
Figure 16. Trends in Investment (%)



Source: CSO; Citi Research

Monetary Indicators

Figure 17. Trends in the WPI (%)



Source: Office of the Economic Advisor,

Inflation interplay of global and domestic factors

Headline Inflation rises but core stabilizes: Headline inflation in May, measured both the WPI and CPI, remained elevated at 7.6% and 10.4% respectively, with the uptrend largely on account of primary articles. However, more importantly, the RBI's proxy to core inflation i.e 'manufactured non-food product' inflation came in at 4.9% - in line with recent trends.

We maintain our view that due to the base effect inflation is likely to come in the 7%-7.5% range in the near term, but could edge higher in the latter half of the year depending on interplay of global and domestic factors. On the global front, key variables to watch (1) The interplay between currencies and commodity prices – while on the domestic front are (2) moves to lower 'suppressed inflation' (3) Monsoons, which could add to volatility in food prices which in any case is trending higher due to structural factors at play as well as the recent rise in Minimum Support Prices (MSP's) of agri crops.

What to watch?

1. Fuel price pass through: Petrol prices were recently raised by 11%. However, given the low weight of petrol in the WPI index (1.1%), it only has a 15bps direct impact on the WPI. Key would be the extent to which prices of regulated fuels are adjusted. Assuming a partial adjustment in the other fuels (diesel – Rs5/ltr, LPG – Rs70/cylinder and Kerosene – Rs2/ltr), the impact on inflation would be ~80bps. As seen in Fig 18 'suppressed' inflation – one of the key focus areas of the RBI – currently stands at 3.4%.

Figure 18. Implications of Oil Prices for the WPI (%)

	Weight in WPI	Current Losses	Required Price Hikes*	Impact on Inflation	Partial Adjustment	Impact on Inflation
Liquefied petroleum gas	0.90%	396	99.0%	0.89%	18%	0.16%
Kerosene fuel	0.70%	31	206.1%	1.44%	14%	0.09%
High speed diesel	4.70%	10	22.5%	1.06%	9%	0.42%
Petrol	1.10%					
Overall impact	**7.40%**			**3.4%**		**0.67**

* For full-adjustment. Source: LPG Prices Rs/Cylinder, all else Rs/ltr Office of the Economic Advisor, Citi Research

2. MSP Increases: Recent hikes in Minimum Support Prices (MSPs) of key crops ranging from 16% in paddy (rice) to 53% in jowar (coarse cereals) will translate to a rise in the inflation indices. The impact on the CPI will likely be more than the WPI, given the higher weight of food/primary products in the CPI (Food wts: CPI 49.7%; WPI 20.1%), Moreover, in the event of a weak monsoon, restricted supply could further push prices higher. (Rains so far are currently 29% below normal).

Figure 19. Combined CPI (%YoY)

	Wts	Mar-12	Apr-12	May-12
1. Food, Tobacco	49.7	8.3	10.2	10.5
2. Fuel and Light	9.5	11.8	11.2	10.7
3. Clothing	4.7	12.4	11.8	11.4
4. Housing	9.8	14.4	14.8	15.7
5. Miscellaneous	26.3	8.6	8.2	8.0
Headline CPI	**100**	**9.4**	**10.3**	**10.4**
%MoM		0.8	1.4	0.9
Rural	57.0	8.7	9.7	9.6
Urban	43.0	10.3	11.1	11.5

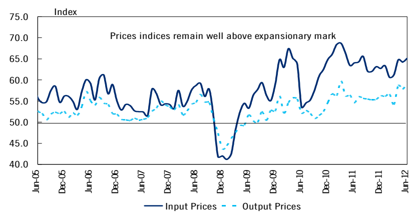
Source: CSO, CEIC Data

RBI – Supply-side constraints; inflation remains key

In its latest monetary policy, contrary to market expectations, the RBI left all rates unchanged (repo at 8%; reverse repo at 7% and CRR at 4.75%). Despite the prior policy being hawkish, expectations of a rate cut had built up due to a collapse in growth, stabilizing core inflation and deterioration in the global macro environment. However, despite the sharp slowdown in growth, the RBI remained clearly concerned about inflation, stating *"persistence of overall inflation both at the wholesale and retail level points to serious supply bottlenecks and sticky inflation expectations."*

The supply-side constraints highlighted by the RBI include (1) Widening current account deficit despite a slowdown in growth (2) Absence of fuel price pass-through has resulted in unchanged consumption patterns and a burgeoning subsidy bill. Additional pressure points to the inflation outlook include: (a) possibility of another round of QE, and (b) the monsoon, which would determine food prices. (See

Figure 20. Trends in Input and Output Prices



Source: Markit

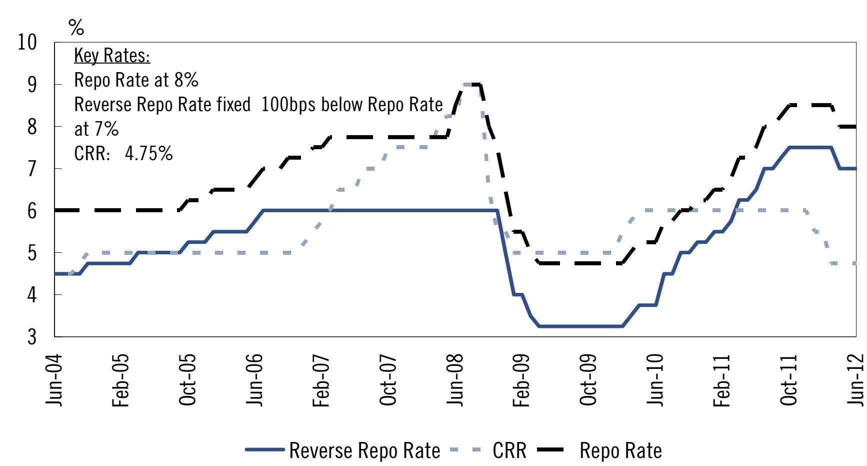
PMI Data – A further hurdle to monetary easing: While the growth outlook is weak and monsoons playing truant, price trends are sticky. The latest PMI data indicate input and output prices rising significantly in June, with <u>input prices</u> at a nine-month high, up 0.8pts to 65.1. Much of this appears to have been passed on to consumers with <u>output prices</u> also up 1.7pts to 59.5. As seen in fig 20, output prices are at highest levels seen since April 2005. (See June PMI: Headline Rises but Forward Looking Indicators and Price Indices Worsen). Given RBI's priority to tackle inflation even if it means sacrificing growth, monetary easing may be delayed further.

Key reasons for us holding on to our 50-75bps rate cut call include: (1) Core inflation is trending to its medium term target of 4% (2) Commodity prices – particularly oil have come off further which could offset the INR depreciation (3) Growth is now well below the RBI's non-inflationary rate of growth of 7% - Note, given that there are visible signs of a weakening consumer story, higher rates could bite more than expected and result in downside to growth estimates (RBI's growth estimate stands at 7.3%; Citi at 6.4%). (4) Global growth slowdown not just in EA but also in the EM world.

But rate cuts contingent on government policy action: Given that the current slowdown in growth is largely due to a collapse in investment – which we and many investors believe is due in large part to 'policy paralysis' – the RBI has stated that the role of interest rates is small and thus it feels that a reduction in rates could exacerbate inflationary pressures. See (RBI Surprises, Keeping ALL Rates on Hold; Ball Now in Govt's Court to Revive Growth.) With inflation likely to remain sticky, we think this now puts onus on the gov't to implement stalled legislation, which may be likely post the July 19 presidential elections.

Given RBI's priority to tackle inflation even if it means sacrificing growth, monetary easing may be delayed further.

Figure 21. India – Trends in Key Domestic Rates (%)



Source: RBI

Fiscal Indicators

FY13 fiscal pressure points increase

Figure 22. Budget Snapshot (Rs Bn)

Rs bn	FY12RE	FY13BE	Growth
a. Revenue receipts	**7,670**	**9,357**	**22.0**
Tax revenues	6,423	7711	20.1
Non-tax	1,247	1646	32.0
b. Non-debt receipts	**298**	**417**	**40.0**
Recoveries of loans	143	116.5	-18.3
Divestments	155	300	93.6
c. Total receipts (a+b)	**7,967**	**9,773**	**22.7**
h Plan expenditure	4,266	5210.25	22.1
i. Non-plan expenditure	8,921	9699	8.7
j. Total Expend (h+i)	**13,187**	**14,909**	**13.1**
j. Fiscal Balance (c-j)	**-5220**	**-5136**	**-1.6**
% to GDP	-5.9	-5.1	-13.7
Revenue Balance (a-d)	**-3950**	**-3504**	**-11.3**
% to GDP	-4.4	-3.4	-22.2
Primary Balance (j-1)	**-2464**	**-1938**	**-21.3**
% to GDP	-2.8	-1.9	-31.0
GDP assumption	**89,122**	**101,599**	**14.0**

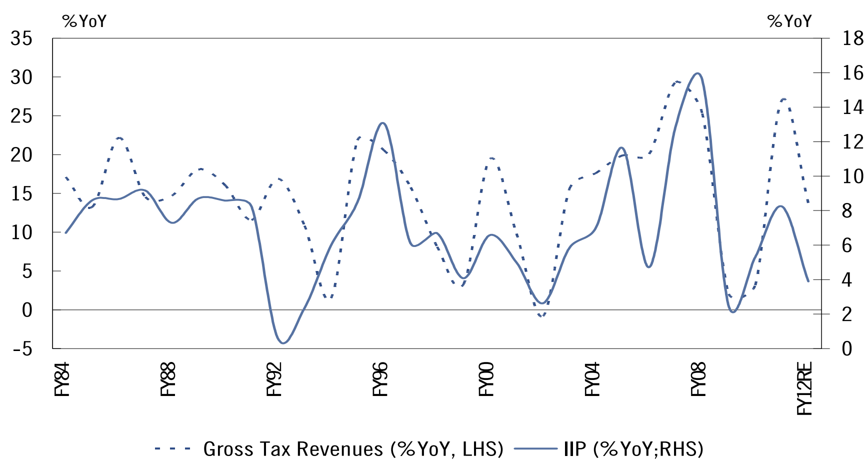
Source: Budget Documents

Revenues - Lower growth could impact collections

A quick re-cap, the Rs5,136bn or 5.1% of GDP FY13 budget arithmetic is based on nominal growth of 14% (real GDP of 7.6% and inflation of 6.5%), revenues +22.7% and expenditure +13.1%. Looking at the revenues, the budget has estimated a 19.5% increase in gross tax collections. (*excise 29.1 %, customs 22 %, services 30.5%, corporate 13.9 %, and income 13.9%).*

While the increase in excise and services tax rates from 10% to 12%, coupled with the widening of the service tax net, will provide a buffer, lower growth could take a toll on tax collections.

Figure 23. Trends in Tax Collections and IIP Growth (%, YoY)



Source: CSO; Budget Documents

Expenditure – Subsidies…Is one serious about the 2% cap?

A quick recap: the FY13 Budget proposed a 2% cap on the subsidy bill where in it said that the government would fully provide for food subsidies while the others (fuel and fertilizer) would be funded to the extent that they can be borne by the economy without any adverse implications. Price hikes in the regulated fuels are critical as the FY13 budget provision on fuel subsidies have been utilized for payment of FY12 dues. The budget factors in oil subsidies at Rs436bn; but this incorporates the Rs385bn deferred oil subsides from FY12.

The budget factors in oil subsidies at Rs436bn; but this incorporates the Rs385bn deferred oil subsides from FY12.

Figure 24. Trends in Subsidies (Rs Bn)

	FY06	FY07	FY08	FY09	FY10	FY11	FY12RE	FY13BE
Food	**231**	**240**	**313**	**438**	**584**	**638**	**728**	**750**
% GDP	0.6	0.6	0.6	0.8	0.9	0.8	0.8	0.7
Fertilizer	**185**	**262**	**325**	**766**	**613**	**623**	**672**	**610**
% GDP	0.5	0.6	0.7	1.4	0.9	0.8	0.8	0.6
Fuel	**27**	**27**	**28**	**29**	**150**	**384**	**685**	**436**
%GDP	0.1	0.1	0.1	0.1	0.2	0.5	0.8	0.4
Total	**475**	**571**	**709**	**1,297**	**1,414**	**1,734**	**2,163**	**1,900**
%YoY	3.4	20.2	24.2	82.9	9.0	22.7	24.7	-12.2
% GDP	1.3	1.3	1.4	2.3	2.2	2.3	2.4	1.9

Source: Budget Documents

Despite lower oil, fuel price increases are key to subsidy targets

Despite lower oil prices, the weak rupee is likely to result in under-recoveries rising to Rs1,519bn in FY13 v/s Rs1,385bn in FY12

FY13 under-recoveries pegged at Rs1.52trn: With crude falling from its highs of ~US$125 in March to current sub-US$100 levels, Saurabh Handa our oil analyst expects the FY13 under-recoveries are likely to come in at ~Rs1.52tn, lower than the earlier estimated ~Rs1.62tn. This however, is still higher than the Rs1.38tn in FY12, primarily due to a sharp depreciation in the rupee. Key to note is that the Rs1.52trn under-recoveries incorporate modest price hikes in regulated fuels i.e Rs4/ltr in diesel, Rs70/cylinder for LPG and ~Rs2/ltr in kerosene.

Better outlook in FY14: Citi expects crude to average US$110 over FY13E, largely because fundamentals could support demand in 2QFY13. However, the new supply dynamics in North America could lead to crude falling further to average US$96 in FY14 leading to a decline in subsidies to ~Rs0.81tr levels.

UNDER- RECOVERIES

US$1/bbl change in oil prices = Rs 30bn

Every Rs depreciation = Rs90bn

Figure 25. Oil Subsidy Sharing Mechanism (Rs Bn)

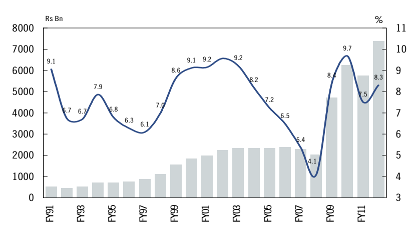
	FY09	FY10	FY11	FY12	FY13E	FY14E
Gross under-recoveries	**1,033**	**461**	**782**	**1,385**	**1,519**	**811**
- Diesel	575	144	365	812	914	407
- LPG	176	143	220	300	302	162
- Kero	282	174	197	273	303	242
Less: upstream sharing	329	144	303	550	608	324
% of Total		*31%*	*39%*	*40%*	*40%*	*40%*
Less: oil bonds/cash	**713**	**260**	**410**	**835**	**836**	**405**
% of Total		*56%*	*52%*	*60%*	*55%*	*50%*
Net under-recoveries	(9)	56	69	(0)	76	81
Brent Crude (US$/bbl)	**85**	**71.5**	**86.6**	**115**	**110**	**96**
USD/INR		47.5	45.6	48.0	54.0	53.0

Source: Citi Research

Implications – Ratings; continued recourse to OMO's

The sharp deterioration in the fiscal situation, with the combined deficit rising from 4.1% in FY08 to 8-9% levels currently, is worrying. While captive demand for government bonds and the domestically-financed fiscal deficit are positive, what is concerning is the growing recognition that the rise in the deficit is structural rather than cyclical. With S&P and Fitch already revising the outlook from stable to negative, we believe a lack of measures on fiscal consolidation could impact the overall rating which is currently at the lowest rung of investment grade (Baa3/BBB-).

Figure 26. Trends in Combined Deficit (%)



Source: Budget Documents; Citi Research

We maintain our view that the FY13 fiscal deficit of Rs5,136bn or 5.1% of GDP could overshoot targets by a minimum of ~40bps to 5.5% of GDP. Taking into account liquidity conditions, similar to FY12, we expect the RBI to continue with Open Market Purchases. A quick recap, fiscal year to date, the RBI has till date purchased bonds worth Rs555bn through OMO's. (In FY12, the RBI conducted expansionary Open Market operations to the tune of Rs1.3trn and also injected Rs0.8trn through CRR cuts)

Figure 27. India — Sovereign Ratings Snapshot

	S&P	Moody's	Fitch
LT Foreign Currency	BBB-	Baa3	BBB-
LT Local Currency	BBB-	Baa3	BBB-
Outlook (FC)	Negative	Stable	Negative

Source: Rating Agencies

External Sector

CAD likely to see positive trend reversal in FY13

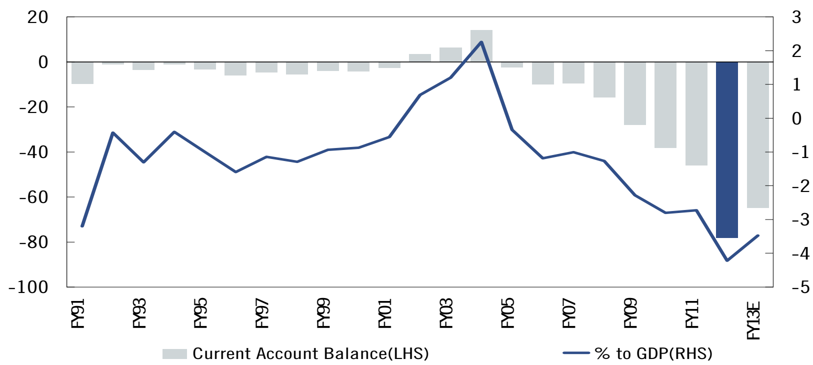
Of the four deficits contributing to the de-rating of the India story (see Deficits – Not Twins, But Quadruplets), the sharp deterioration in India's Current Account Deficit (CAD) from US$45.9bn (2.7% of GDP) in FY11 to US$78.2bn (4.2%) in FY12 has been key to the ~25% weakness in the INR. The deterioration in the CAD was primarily a result of higher oil and gold imports. These commodities, even on a net basis (i.e. taking into account both petro product and jewelry exports), are India's top two import items, which resulted in the trade deficit widening to US$189.8bn or 10.2% of GDP v/s US$130.6bn or 7.8% in FY11.

Higher imports – particularly oil and gold – have resulted in India's trade deficits widening from ~2.5% of GDP in the 1990s to ~10% of GDP currently…

…..While earnings from invisibles have remained buoyant at ~6% of GDP….

…. the sharp increase in the trade deficit resulted in the current a/c deficit widening to ~4% of GDP in FY12 from an average of 2% in the recent past

Figure 28. Trends in the Current Account Deficit (US$bn, % GDP)



Source: RBI, Citi Research

Going forward for FY13, we maintain our view of the CAD likely to narrow to US$64.7bn or 3.5% of GDP. This is due to lower oil prices and falling gold demand which more than offsets a deceleration in exports due to the global slowdown. The key assumptions underlying the improvement in the CAD are:

- **Export growth decelerating to 12% from 23.7% in FY12**: Despite the recent INR weakness, the changing composition of India's exports coupled with the synchronized global slowdown (EU, China, Brazil, and other EMs) and worries about the US fiscal cliff are likely to take a toll on India's exports. Export growth would have been lower were it not for the ~25% depreciation in the currency.

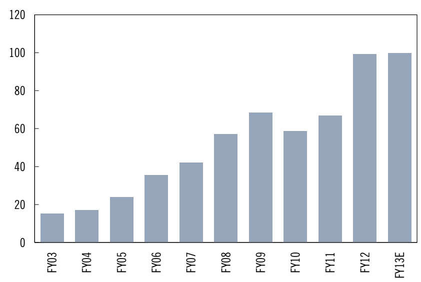
- **Moderating gold demand:** As the largest consumer of gold, this is India's third-largest import item, imports comprising ~10% of India's total import bill. In volume terms, gold imports have increased from 600-700 tonnes in 07-08 to 800-900 currently. The government's recent focus on curbing gold demand coupled with the weaker rupee, have resulted in lower imports. We expect gold imports to come off 20% to 650tonnes which could result in savings to the tune of US$7bn.

Figure 29. Net Gold Imports

		FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12*
Gold Imports	Tonnes	711	650	761	704	609	749	933	792
Gold Prices	$/Oz	414	477	629	765	868	1,025	1,295	1,650
Actual Imports	US$bn	10.5	10.8	14.5	16.7	20.7	28.6	33.9	46.6
Precious Stone Imports	US$bn	9.4	9.1	7.5	8.0	16.6	16.2	31.3	27.2
Total Gold Imports	**US$bn**	**20.0**	**20.0**	**21.9**	**24.7**	**37.3**	**44.8**	**65.1**	**73.8**
Gems/Jewelry Exports	US$bn	13.8	15.5	16.0	19.7	28.0	29.0	40.8	37.4
Net Gold Imports	**US$bn**	**6.2**	**4.4**	**6.0**	**5.0**	**9.4**	**15.8**	**24.3**	**36.4**

Source: *Apr-JanWGC, CMIE, Citi Research, CEIC

Figure 30. Trends in Net Oil Imports(US$bn)



Source: CMIE: Citi Research

- **Lower oil prices are likely to make the vicious cycle turn virtuous:** A quick recap, India imports 80% of its crude oil requirements, with oil comprising over 30% of its import bill. Rising oil prices in FY12 resulted in oil imports touching US$156bn v/s US$104bn in FY11. Taking into account petro-product exports, every US$1/bbl change in oil prices impacts the CAD by US$900mn. Thus despite consumption increasing, moderating oil prices will stabilize the net oil import bill.

Figure 31. Trends in Net Oil Imports

Year	FY07	FY08	FY09	FY10	FY11	FY12	FY13E	FY14E
A. Crude oil prod (mn T)*	34.0	34.1	33.5	33.7	35.6	37.8	40.5	44.8
B. Crude oil imports (mn T)	111.5	121.7	128.2	159.3	166.1	176.3	187.9	205.7
Crude requirements (A+B)**	145.5	155.8	161.7	192.9	201.8	214.1	228.3	250.5
Natural Gas Production (bcm)	31.7	32.3	32.8	47.6	53.1	48.7	44.0	42.2
In Volume Terms (Mn T)								
Consmp of Petro products	120.8	129.0	133.6	138.2	141.8	146.3	157.8	162.6
Petroleum Product Exports	32.7	40.8	36.9	51.0	63.9	67.8	69.6	85.7
In Value Terms (US$bn)								
A. Oil/ Product Imports	59.7	84.7	95.5	89.2	106.8	159.4	157.4	153.8
B. Petroleum product exports	17.8	27.6	27.2	30.5	40.0	60.1	57.7	64.1
Net oil import bill (A-B)	**41.9**	**57.2**	**68.3**	**58.7**	**66.8**	**99.3**	**99.7**	**89.7**
Avg Oil Price (Indian basket)	63.4	80.2	89.0	70.0	80.0	115.0	107.0	96.0

IncludescapacityadditionsbyONGC,CairnandReliance'sKGD6.Source: Citi Research

FY13 BoP to stay in deficit as capital flows remain weak

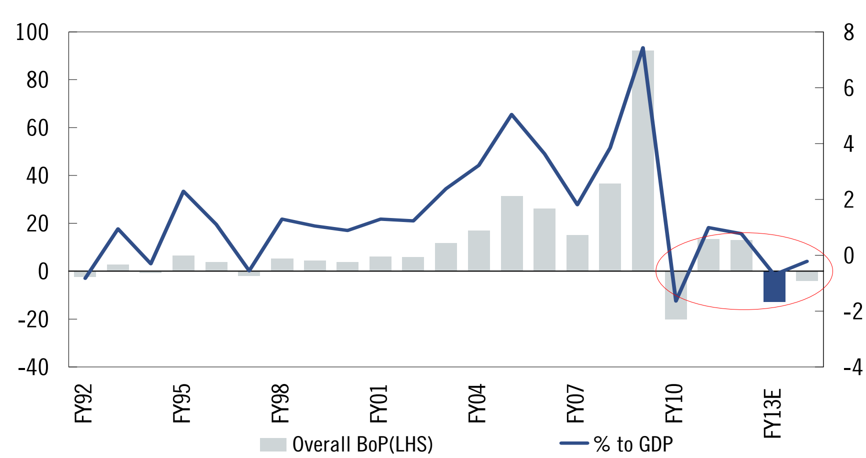
Figure 32. BoP Snapshot (US$bn)

	FY12	FY13E	FY14E
Current Account (a+b)	**-78.2**	**-64.7**	**-56.4**
a. Trade Balance	-189.7	-190.1	-195.2
b. Invisibles	111.6	125.4	138.7
Capital Account	**67.8**	**60.6**	**59.6**
Of which: FII	17.2	18.0	20.0
FDI	22.1	13.0	14.0
Overall Balance	**-12.8**	**-4.1**	**3.2**

Source: RBI; Citi Research

While trends on the current account are improving, the picture on the capital account is not as bright. Key worries are: (a) Lower FDI – largely a result of a non-conducive domestic policy environment; (b) Commercial borrowings moderating due to global macro blues. Consequently, we expect capital flows to come in at US$60.6bn. Taking into account the CAD of US$64.7bn, we expect to see a second consecutive year in a drawdown of reserves. However, the moderating CAD in FY13 will likely limit the drawdown to US$4.1bn v/s US$12.8bn in FY12. That said, one buffer could be if the RBI issues a dollar bond - similar to the IMD/RIB issued in 1998/ 2000 respectively.

Figure 33. Trends in Overall Balance of Payments (US$bn; % to GDP)



Source: RBI; Citi Research

Financial Markets

Global FX – USD strength to continue

Our global strategists remain positive on the USD with its strength being central to their currency forecasts. In addition to periodic bouts of risk aversion, this reflects the likely resilience of US growth relative to elsewhere and the outperformance of both US productivity and equity markets compared with the rest of the world. Our team expects across the board weakness in the EUR as further ECB rate cuts and LTROs, as well as rising risk premia, undermine the single currency. Consequently, they expect the EUR/USD consolidating in a 1.20-1.30 band for the next few months before trending through the lower level of this band over 6-12 months with a 1.10-1.20 trading range then possible.

EM FX – Weaker backdrop due to growth slowdown

The growth slowdown underway in EM economies provides a weaker backdrop for many EM currencies compared to recent years. The downshift in growth in China is the big influence, generating weakness in the likes of AUD and EM Asia. Capital flight is an added vulnerability in many, with foreign bond and equity ownership sharply higher than it was before various quantitative easing programs began. However, our strategists highlight the need to balance this against stretched US dollar longs that have skewed the balance of risks towards prospective EM FX strength in the very near term.

Figure 34. Quarterly FX Forecasts

	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Euro	1.25	1.24	1.21	1.18	1.15	1.19	1.23	1.26
Japanese Yen	80.00	80.00	81.00	81.00	82.00	83.00	83.00	84.00
British Pound	1.56	1.55	1.52	1.49	1.46	1.51	1.55	1.60
Swiss Franc	0.96	0.97	0.99	1.02	1.04	1.01	0.98	0.95
Australian Dollar	1.00	1.00	0.99	0.97	0.96	0.94	0.93	0.91
EM Asia								
Chinese Renminbi	6.36	6.33	6.34	6.34	6.35	6.30	6.25	6.20
HK Dollar	7.76	7.75	7.75	7.76	7.76	7.76	7.75	7.75
Indonesian Rupiah	9508	9405	9489	9571	9650	9650	9650	9650
Indian Rupee	**56.50**	**54.00**	**54.50**	**55.00**	**55.50**	**54.60**	**53.80**	**53.10**
Korean Won	1160	1140	1149	1157	1164	1142	1121	1100
Malaysian Ringgit	3.19	3.10	3.11	3.13	3.14	3.09	3.04	2.99
Philippine Peso	42.60	42.10	42.20	42.40	42.50	42.00	41.60	41.2
Singapore Dollar	1.28	1.25	1.26	1.27	1.27	1.26	1.24	1.23
Thai Baht	31.80	30.70	31.10	31.50	31.90	31.40	30.90	30.40
Taiwan Dollar	30.00	30.30	29.80	29.30	28.80	28.70	28.60	28.60
Other EMs								
Turkish Lira	1.82	1.78	1.82	1.85	1.88	1.87	1.86	1.86
South African Rand	8.44	8.41	8.56	8.71	8.85	8.85	8.85	8.85
Brazilian Real	2.06	2.01	1.99	1.97	1.95	1.92	1.90	1.87
Mexican Peso	13.80	13.40	13.50	13.60	13.70	13.30	12.90	12.60

Source: *Citi Foreign Exchange Forecasts* dated June 25, 2012

INR outlook – Two powerful and conflicting forces in play

Trends: A combination of domestic and global factors has resulted in the INR being among the worst performing currencies over the last year. The weakness to ~Rs57/USD levels despite the sharp correction in crude oil prices has caught many by surprise. The recent rally to Rs55/USD currently is largely due to global factors and in line with trends seen in the Won, Lira, Ruble and Indonesian Rupiah.

Figure 35. Trends in USD/INR

Source: RBI

– **Domestic Factors:** Key drivers behind the INR weakness include the issue of the deficits (See Deficits – Not Twins, But Quadruplets) resulting in India's top down macro story de-rating over the last year, with growth expectations now in the 5.5%-6.5% range v/s 7.5% - 8% levels just a year ago. As we have highlighted in the past, a rising CAD and lackluster foreign flows have resulted in forex reserves remaining largely stagnant over the last three years. This is reflected in forex import cover coming off significantly from 14 months of import cover in FY08 to 5.7 months in FY12. Added to this are the sovereign rating outlook changes from stable to negative. While the RBI/MoF have been taking various measures to enhance dollar inflows, these have perceived as being "re-active" thus resulting in the unit remaining weak.

– **External Factors:** In addition to domestic factors, the INR has also been impacted by a deteriorating global risk sentiment and concerns on global.

Outlook: Our global macro team expects the INR to retrace to the 54-55.5 range over the 12-month forecast horizon. The projections have two powerful and conflicting forces. On the one hand, the INR is clearly oversold, and policy makers are expected to intervene strongly as the INR weakens further. To some extent, there is also room for INR to play "catch up" with equity gains and falls in oil prices – the latter should also help India's current account position. Added to this is the likelihood that the RBI/MoF will continue to take measures to enhance dollar inflows. Going forward, we could also see the possibility of a commercial dollar bond issue dollar swap-lines, and gold imports coming under further scrutiny – all of which could have a more meaningful impact on dollar inflows than the 'baby' steps being currently taken. (See pg 18 for details on all policy measures to attract flows).

But on the other hand, the macro setting in India is particularly poor – with a combination of high interest rates, sizeable twin deficits and prospective ratings downgrades providing an unhelpful backdrop for INR strength.

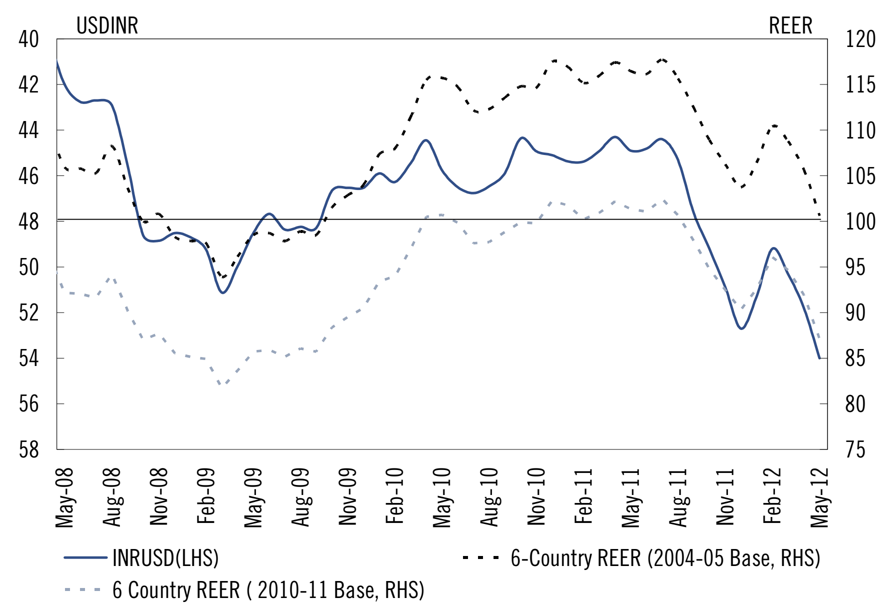
CATCH-UP WITH FUNDAMENTALS?

In a sense, the current round of INR depreciation can be viewed as a catch-up with fundamentals.

The six-country trade-based REER, available till May 25 is at 100.1 (Base 2004-05) and 87.1 (Base 2010-11)

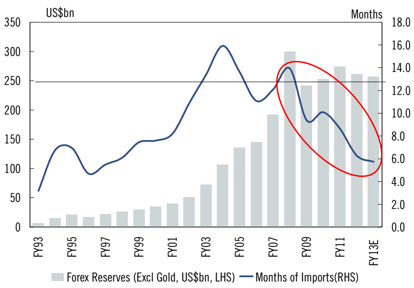
The six-country REER is the weighted average of bilateral exchange rates, adjusted for relative inflation rates. Comprises (1) US dollar, (2) Euro-zone (Euro), (3) UK (Pound Sterling), (4) Japan (Yen), (5) China (Yuan), and (6) Hong Kong (Dollar).

Figure 36. Trends in REER



Source: RBI

Figure 37. Forex Reserves & Import Cover



Source: RBI; Citi Research

Measures to Enhance Capital Flows

Rising current account deficits coupled with dwindling capital flows resulted in India's import coverage declining from 14 months to 6 months currently. Following the weakness in the currency, since November 2011, policy officials – both the RBI and the Ministry of Finance – have been taking several steps to stem the depreciation in the INR and deterioration seen in import coverage ratio.

Figure 38. Key Steps Taken to Enhance Capital Inflows

Instrument	Steps	Comment
Steps to Curb Speculation	- Forward contracts are not allowed to be re-booked; - Reduction on the US$100m limit on net FX supply through rupee swaps	Interbank volumes are down 40% from US$5bn/day to US$3bn.
Encouraging NRI Deposits	- Interest rates raised on Non-Resident (External) Rupee (NRE) Term Deposits and Foreign Currency Non-Resident (Banks) (FCNR (B)) deposits. - Later in Dec, interest rates on NRE Deposits and Non-Resident Accounts were deregulated.	Higher rates have would encourage NRI deposits given soft global interest rates
Relaxing ECB Norms	- Loans with a maturity between 3-5 years can now be raised at a spread of Libor+350bps from Libor +300bps previously. - Funds raised must be brought back into India immediately. - ECBs permitted to part finance rupee debt of existing power projects - Co's with FX earnings permitted to use ECB funding for prepayment/fresh rupee capex up to US$10bn - Withholding tax on interest payments for ECBs reduced from 20% to 5% for key infra sectors.	Measures would facilitate funding and provide cushion on the capital account as more companies, particularly in the infra sector, borrow overseas to take advantage of lower rates
FII Flows	- Permitting Qualified Foreign Investors (QFIs) to directly invest in the equity and corporate bond market - Relaxing foreign limits on debt – FII limits on GOI bonds raised initially from US$10bn to US$15bn and now US$20bn; Limits on Corporate bonds raised from US$15bn to US$20bn and now - Investor base for GOI securities broadened to included Sovereign Wealth Funds, multi-lateral agencies, foreign central banks, insurance/pension funds - Permitting two-way fungibility in Indian Depository Receipts subject to a ceiling - Implementing Advance Pricing Agreement - GAAR deferred to FY14	Measures aim to encourage greater foreign participation in Indian capital market. The Advance Pricing Agreement would bring down tax litigation and provide tax certainty to foreign investors
Relaxing accounting rules for forex loans of companies	- Extending the deadline for charging losses on forex loans from March 2012 to March-end 2020.	Fears on corporate profitability being hit due to the move in the exchange rate muted. Moreover, it reduces future pressure on hedging
Steps to Curb Black Money	- 82 Double Taxation Avoidance Agreements (DTAA) and 17 Tax Information Exchange Agreements (TIEA) finalized - A dedicated cell set up for the speedy exchange of tax information with treaty countries is fully functional in CBDT - Directorate of IT Criminal Investigation established	These steps would help tackle the circulation and transfer of black money. The govt has also proposed to table a White paper on Black Money in parliament this session
Gold Imports	- Basic customs duty on standard gold bars; gold coins of high purity and platinum were raised from 2% to 4%; non-standard gold from 5% to 10% in the budget - Excise duty on refined gold increased from 1.5% to 3% - NBFCs required to maintain LTV ratio of <60% for loans against gold collateral. Gold financing companies required to maintain Tier I capital of 12%	Given that gold imports comprise ~ 10% of total imports,; the govt has been taking steps to curb imports

Source: RBI, Ministry of Finance, Citi Research

Measures last month included increasing the FII limit on govt and corporate debt. While this will incrementally help, the market was disappointed as (1) expectations on RBI action were high and (2) the existing limits have still not been fully utilized. We maintain our view that the RBI/MoF will continue to take measures to enhance dollar inflows. Going forward, we could also see the possibility of a commercial dollar bond issue dollar swap-lines, and gold imports coming under further scrutiny.

Monthly Monitor

Figure 39. India — Key Monthly Indicators (percent change from a year ago unless otherwise stated)

	Apr11	May11	Jun11	Jul11	Aug11	Sept11	Oct11	Nov11	Dec11	Jan12	Feb12	Mar12	Apr12	May12
Consumption Trends														
Two-Wheelers	22.0	14.5	14.8	12.6	16.1	22.7	1.8	25.0	8.5	13.6	12.0	8.0	10.8	11.2
Passenger Car Sales	13.1	7.0	1.5	-15.8	-10.1	-1.9	-24.3	6.0	7.2	6.3	11.8	18.4	3.4	2.8
Commercial Vehicle Sales	8.5	15.9	18.8	24.8	23.5	18.8	21.6	37.2	16.7	15.0	20.0	16.4	5.6	10.1
LCV	14.9	22.4	31.2	37.9	36.1	36.6	19.8	52.4	23.0	16.9	34.0	35.6	18.2	26.5
MHCV	0.9	8.6	6.2	10.4	9.8	1.8	23.9	18.8	9.1	12.7	5.3	-1.3	-11.6	-10.6
Investment Trends														
Infrastructure Index	5.6	6.7	6.4	8.9	4.8	3.3	1.2	7.7	5.5	1.6	7.7	2.3	3.1	3.8
Cement Dispatches	0.5	0.6	2.2	11.2	6.7	1.8	-1.0	19.0	13.4	9.6	10.7	6.6	8.8	11.6
Diesel Consumption	1.4	10.7	2.9	5.3	6.4	9.8	7.7	16.4	6.0	7.5	11.7	10.8	8.0	9.0
Steel Production	4.8	5.4	14.4	7.2	17.3	6.7	5.4	2.2	4.5	1.5	0.0	12.5	10.4	10.6
Manufacturing PMI*	58.0	57.5	55.3	53.6	52.6	50.4	52.0	51.0	54.2	57.5	56.6	54.7	54.9	54.8
Output	63.9	63.2	58.4	57.2	56.0	51.1	52.7	50.5	55.8	62.9	60.5	56.3	56.1	56.5
New Orders	63.1	62.4	60.1	54.5	53.1	51.3	53.7	52.8	57.9	62.2	62.8	58.1	61.1	59.6
Industrial Production Index														
General	5.3	6.2	9.5	3.7	3.4	2.5	-5.0	6.0	2.7	1.1	4.1	-3.5	0.1	
Manufacturing	5.7	6.3	11.1	3.1	3.9	3.1	-6.0	6.6	2.8	1.4	3.9	-4.4	0.1	
Mining	1.6	1.8	-1.4	0.7	-5.5	-7.5	-5.9	-3.5	-3.3	-2.4	2.8	-1.3	-3.1	
Electricity	6.5	10.3	8.0	13.1	9.5	9.0	5.6	14.6	9.1	3.2	8.0	2.7	4.6	
Use Based Basic Goods	7.1	7.5	7.8	10.0	5.8	5.3	1.2	6.5	5.5	1.8	7.7	1.1	2.3	
Capital goods	6.6	6.2	38.7	-13.7	4.0	-6.5	-26.5	-4.7	-16.0	-1.7	10.2	-21.3	-16.3	
Intermediate goods	3.9	0.1	1.6	-0.1	-1.0	-1.4	-8.4	1.3	-1.5	-2.8	-0.2	-2.1	-1.4	
Consumer goods	3.2	7.2	3.1	6.4	2.1	5.7	0.1	12.8	10.1	2.9	-0.3	0.7	5.2	
Consumer Durables	1.6	5.1	1.6	9.0	5.5	8.9	-0.4	10.4	5.1	-7.1	-6.1	0.2	5.0	
Consumer Non-Durables	4.6	9.0	4.3	4.1	-0.7	2.7	0.5	15.0	13.8	11.0	4.5	1.0	5.4	
Services														
Major Port traffic	6.1	3.7	5.4	3.7	3.5	-4.4	-7.4	-0.7	-6.5	-5.7	-6.2	-8.5	-6.5	
Railway freight	7.4	7.4	6.2	7.4	2.0	-1.8	-1.3	5.9	8.7	5.4	9.0	5.6	3.5	
Tourist arrivals ('000)	417	369	396	498	402	401	563	637	715	681	677	623	452	
Cellular subscriber Adds (Mn)	15.9	13.0	11.4	7.0	7.5	8.0	7.9	3.7	9.2	9.9	6.8	8.1	6.7	
Banking Trends														
Money supply(M3)	17.3	16.9	17.2	16.7	17.0	16.3	15.3	15.6	16.2	15.2	13.8	13.0	13.3	13.3
Loan(Credit) growth	21.5	22.1	20.4	19.2	20.4	18.9	18.9	18.0	16.9	16.7	15.6	16.6	18.0	18.3
Deposit growth	17.0	16.9	18.0	15.9	18.1	16.6	15.4	16.9	17.4	16.4	14.6	13.6	13.6	14.1
Non-food credit	22.3	22.4	20.4	18.8	19.9	19.7	19.1	17.7	16.7	16.4	15.4	16.8	17.1	16.9
Inflation														
CPI –Industrial Workers	9.4	8.7	8.6	8.4	9.0	10.1	9.4	9.3	6.5	5.3	7.6	8.6	10.2	10.2
WPI	9.7	9.6	9.5	9.4	9.8	10.0	9.9	9.5	7.7	6.9	7.4	6.9	7.2	7.5
Manufactured Products	6.8	7.4	7.9	7.7	7.9	8.0	8.0	8.2	7.6	6.7	5.8	4.9	5.1	5.0
Primary Products	15.1	12.9	11.3	11.5	12.5	12.2	11.0	8.9	3.6	2.8	7.1	9.6	9.7	10.9
Fuel Index	13.0	12.3	12.8	12.0	12.9	14.0	14.8	15.5	15.0	14.6	13.6	10.4	11.0	11.5
Interest rates (Average, %)														
Call money rate	6.6	7.2	7.5	7.6	7.9	8.0	8.1	8.3	8.5	8.8	9.0	8.8	8.6	8.6
91-day T-Bills	7.5	8.1	8.2	8.4	8.4	8.4	8.7	8.8	8.5	8.6	9.1	9.0	8.4	8.5
Corp Bond Spreads (5y GOI-AAA)	1.0	0.9	1.1	0.9	0.9	0.9	0.8	0.7	0.8	1.0	0.9	0.9	0.8	0.9
10-year government bond	8.0	8.3	8.3	8.3	8.3	8.3	8.7	8.9	8.5	8.3	8.2	8.4	8.6	8.5
Trade - customs data* **														
Exports(%YoY)	25.0	54.5	25.7	59.5	46.2	30.2	25.3	4.6	6.7	10.1	4.3	-5.7	3.2	-4.1
Imports(%YoY)	16.0	52.0	36.3	38.1	45.6	18.7	26.8	34.9	19.8	20.3	20.6	24.3	3.8	-7.3
Oil	37.6	53.4	69.6	54.9	73.7	5.4	35.0	57.8	11.2	26.8	39.5	32.4	7.0	13.4
Non-oil	6.8	51.4	23.7	31.5	35.4	24.1	24.0	26.4	23.4	17.6	13.5	19.9	2.1	-15.8
Trade Deficit (US$bn)	-14.7	-19.5	-14.1	-15.3	-14.9	-11.3	-18.7	-16.4	-12.7	-14.8	-15.2	-13.9	-13.5	-16.2
Brent Prices ($/bbl)	123.0	114.5	113.7	116.6	110.0	109.8	108.8	110.3	107.7	111.6	119.1	124.4	120.5	110.2
Foreign investment (US$ mn)														
FII	1,618	-1,480	1,014	1,807	-2,394	7	347	-787	31	2,037	5,128	1,685	-206	-58
FDI	3,121	4,664	5,656	1,099	2,830	1,765	1,161	2,538	1,353	2,004	2,211	1,628	2,775	
Exchange rate and reserves														
US$ exchange rate average	44.4	44.9	44.8	44.2	45.3	47.7	49.2	50.9	52.6	51.3	49.2	50.4	51.9	54.5
US$ exchange rate month end	44.2	45.1	44.7	44.4	46.1	49.0	48.7	52.2	53.1	49.5	49.0	50.9	52.7	56.1
Forex reserves incl.gold (US$bn)	313.5	310.2	309.0	319.1	319.2	311.5	320.4	304.4	296.7	293.9	295.0	294.4	295.4	285.8

* Values over 50 indicate expansion. ** Only GSM subscribers available. *** Provisional. Source: CSO, RBI, Ministry of Finance, Markit

Balance of Payments

Figure 40. India – Trends and Forecasts in the Balance of Payments (US$B, %)

	FY08	FY09	FY10	FY11	FY12	FY13E	FY14E	Comments
CURRENTACCOUNT								
Exports(RBI)	**166.2**	**189.0**	**182.4**	**250.5**	**309.8**	**346.9**	**395.5**	
Y/Y%	28.9	13.7	-3.5	37.3	23.7	12.0	14.0	While a weak currency helps exports, the impact is muted
% of GDP	13.4	15.6	13.2	14.9	16.7	18.6	18.0	Due to changing composition and global slowdown
Exports–Customs*	**162.9**	**182.8**	**178.8**	**251.1**	**303.7**	**340.1**	**391.2**	
Y/Y%	28.9	12.2	-2.2	40.5	20.9	12.0	15.0	
Imports(RBI)	**257.6**	**308.5**	**300.6**	**381.1**	**499.5**	**537.0**	**590.7**	
Y/Y%	35.1	19.8	-2.6	26.7	31.1	7.5	10.0	
%to GDP	20.8	25.4	21.8	22.6	27.0	28.9	26.8	
Imports-Customs*	**251.4**	**298.8**	**288.3**	**369.7**	**488.6**	**521.9**	**581.1**	
Y/Y%	35.4	18.8	-3.5	28.2	32.2	6.8	11.3	
Of which Oil	79.6	93.7	87.1	103.9	155.6	157.2	161.7	Crude at US$111/bbl in FY12; US$108/bbl in FY13
Y/Y%	39.9	17.6	-7.0	19.3	49.8	1.0	2.9	∆US$1/bbl in oil prices=US$900m impact on deficit
Non-Oil	171.8	205.2	201.2	265.8	333.0	364.6	419.3	
Y/Y%	33.4	19.4	-1.9	32.1	25.3	9.5	15.0	
a. Trade balance (RBI)	**-91.5**	**-119.5**	**-118.2**	**-130.6**	**-189.8**	**-190.1**	**-195.2**	Lower oil prices and lower gold demand will help deficit
% of GDP	-7.4	-9.8	-8.7	-7.8	-10.2	-10.2	-8.9	
Trade Balance(Customs)	-88.5	-116.0	-109.6	-118.6	-184.9	-181.7	-189.9	
Difference bet. RBI and Customs Data	**-2.9**	**-3.5**	**-8.6**	**-12.0**	**-4.9**	**-8.3**	**-5.3**	Difference normally represents defense imports.
b. Invisibles	**75.7**	**91.6**	**80.0**	**84.6**	**111.6**	**125.4**	**138.7**	
Non-factor services	38.9	53.9	35.8	48.8	64.1	67.0	77.4	
Of which: Software Services	36.9	43.5	48.2	53.3	61.0	71.0	82.4	
Non-Software Services	1.9	10.4	-12.5	-4.4	3.1	-4.0	-5.0	
Investment income	-5.1	-7.1	-8.0	-17.3	-16.0	-10.0	-11.0	
Remittances**	41.7	44.6	52.1	53.1	63.5	68.0	72.0	
Official transfers	0.2	0.2	0.3	0.0	0.0	0.4	0.4	
1.Currenta/cbalance (a+b)	**-15.7**	**-27.9**	**-38.2**	**-45.9**	**-78.2**	**-64.7**	**-56.4**	
% of GDP	-1.3	-2.3	-2.8	-2.7	-4.2	-3.5	-2.6	Current a/c to narrow to 3.5 % of GDP in FY13
CAPITALACCOUNT								
c. Loans	**40.7**	**8.3**	**12.4**	**28.4**	**19.3**	**18.0**	**18.0**	Global developments could impact bank loans
External assistance	2.1	2.4	2.9	4.9	2.3	2.0	2.0	
Commercial borrowings***	22.6	7.9	2.0	12.5	10.3	10.0	10.0	
Short-term credit	15.9	-2.0	7.6	11.0	6.7	6.0	6.0	
d. FDI(Net=a-b)	**15.9**	**19.8**	**18.0**	**9.4**	**22.1**	**13.0**	**14.0**	Policy clarity could help FDI
(a)FDI-To India	34.7	37.7	33.1	25.9	33.0	25.0	29.0	
(b)FDI-Abroad	-18.8	-17.9	-15.1	-16.5	-10.9	-12.0	-15.0	
e. Portfolio Invst(FII+ADRs/GDRs)	**27.4**	**-14.0**	**32.4**	**30.3**	**17.2**	**18.0**	**20.0**	Increase in FII limits in debt will help
f. Banking Capital	**11.8**	**-3.2**	**2.1**	**5.0**	**16.2**	**11.0**	**7.0**	
Of which NRI deposits	0.2	4.3	2.9	3.2	11.9	10.0	6.0	
g. Rupee debt service	**-0.1**	**-0.1**	**-0.1**	**-0.1**	**-0.1**	**-0.4**	**-0.4**	
h. Other capital****	**11.0**	**-4.0**	**-13.2**	**-11.0**	**-6.9**	**1.0**	**1.0**	
2.Capitala/c(c+d+e+f+g+h)	**106.6**	**6.8**	**51.6**	**62.0**	**67.8**	**60.6**	**59.6**	
Errors & Omissions	1.3	1.1	0.0	-3.0	-2.4	0.0	0.0	
Overall balance(1+2)	**92.2**	**-20.1**	**13.4**	**13.1**	**-12.8**	**-4.1**	**3.2**	
Forex								
Forex assets	299.1	241.6	252.8	273.7	260.9	256.8	260.0	
FCA to months of imports	13.9	9.4	10.1	8.6	6.3	5.7	5.3	
Exchange rate								
Rs/US$-annual avg	40.2	46.0	47.4	45.6	48.1	54.5	53.0	
%depreciation	-11.1	14.4	3.0	-3.8	5.5	13.3	-2.8	
Rs/US$-yearend	40.1	50.7	44.9	44.6	50.3	54.8	51.5	
%depreciation/(-)appreciation	-8.0	26.4	-11.4	-0.7	12.8	8.9	-6.0	

Data on exports and imports differ from those given by DGCI&S on account of differences in coverage, valuation and timing (e.g. RBI data on imports includes defence)**.** Remittances - 50% are for family maintenance; balance is local withdrawal from NRI rupee deposits. ***Commercial Borrowings include US$4.1bn of the Resurgent Bond Issue repaid in September 2003 and repayment of India Millennium Bonds in FY06. * Other capital refers to leads and lags in exports, advances received pending issue of shares, funds held abroad. Source: RBI, Citi Research

Direction and Composition of Trade

Figure 41. India — Composition of Imports (US$bn, %)

	FY07	FY08	FY09	FY10	FY11	FY12*
Petroleum crude& products	57.1	79.7	91.5	86.8	106.1	108.6
% to total	30.8	31.9	30.6	30.2	30.1	30.5
% YoY	29.8	39.6	14.8	-5.1	22.0	44.6
Capital goods	30.8	49.8	48.5	44.5	49.9	46.2
% to total	16.6	20.0	16.2	15.5	14.2	13.0
% YoY	26.8	61.9	-2.8	-8.2	12.2	20.9
Gold & Silver	14.6	17.9	22.8	29.6	35.6	45.5
% to total	7.9	7.1	7.6	10.3	10.1	12.8
% YoY	29.1	22.1	27.8	29.8	20.2	54.1
Pearls precious stones	7.5	7.3	16.6	16.2	31.3	22.9
% to total	4.0	2.9	5.5	5.6	8.9	6.4
% YoY	-18.1	-2.0	126.5	-2.6	93.3	0.6
Chemicals, related products	13.8	18.7	29.2	23.5	27.4	27.9
% to total	7.5	7.5	9.8	8.2	7.8	7.8
% YoY	21.6	34.8	56.7	-19.7	16.8	25.4
Electronic Goods	15.9	20.2	23.4	21.0	21.5	25.2
% to total	8.6	8.1	7.8	7.3	6.1	7.1
%YoY	20.3	26.7	15.8	-10.3	2.5	24.2
Food & related items	4.9	5.3	5.8	10.0	10.0	10.0
% to total	2.7	2.1	1.9	3.5	2.8	2.8
% YoY	50.5	8.8	8.3	72.9	-0.3	30.1
Other non-POL items	33.8	42.7	52.2	46.8	56.1	3.0
% to total	18.3	17.1	17.4	16.3	15.9	0.8
% YoY	37.3	26.2	22.4	-10.4	19.9	21.7
Other commodities	6.6	8.2	9.3	9.3	18.3	11.3
% to total	3.6	3.3	3.1	3.2	4.1	3.2
% YoY	-16.5	24.1	13.4	-0.4	56.9	19.0
TOTAL IMPORTS	**185.1**	**249.8**	**299.3**	**287.6**	**359.2**	**356.0**
% YoY	24.1	35.0	19.8	-3.9	22.5	32.4

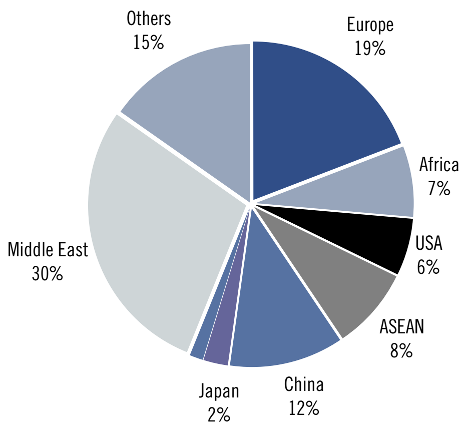
* Apr- Dec. Source: CMIE ,RBI, Citi Research

Figure 42. Composition of Exports (US$bn, %)

	FY07	FY08	FY09	FY10	FY11	FY12*
Engineering goods	29.5	37.2	47.0	38.1	68.8	52.0
% to total	23.3	22.8	25.7	21.4	27.3	23.7
%YoY	36.3	26.4	26.3	-18.9	80.5	13.9
Petroleum, crude prods	18.7	28.4	26.9	28.0	42.0	43.0
% to total	14.8	17.4	14.7	15.7	16.7	19.6
%YoY	60.4	52.0	-5.3	4.3	49.9	51.8
Gems & Jewellery	16.0	19.7	28.0	29.0	36.6	33.7
% to total	12.6	12.1	15.3	16.3	14.5	15.4
%YoY	2.8	23.3	42.2	3.6	26.2	46.9
Agri, allied products	12.7	18.4	17.6	17.7	24.7	25.7
% to total	10.0	11.3	9.6	10.0	9.8	11.7
%YoY	24.1	45.5	-4.8	1.1	39.2	53.0
Chemicals & related	12.1	15.6	17.3	17.4	21.5	19.5
% to total	9.6	9.5	9.5	9.7	8.5	8.9
%YoY	18.1	28.3	11.3	0.4	23.7	27.9
Textiles (incl RMG)	17.4	19.4	20.0	19.9	23.4	20.5
% to total	13.7	11.9	10.9	11.1	9.3	9.4
%YoY	5.9	11.9	3.2	-0.9	17.6	22.7
Ores & minerals	7.0	9.1	7.8	8.7	10.7	6.0
% to total	5.5	5.6	4.3	4.9	4.2	2.7
%YoY	13.6	30.4	-14.4	11.0	23.0	-18.4
Other manuf goods	9.9	11.1	11.0	10.9	13.8	13.9
% to total	7.9	6.8	6.0	6.1	5.5	6.4
%YoY	13.9	11.7	-1.4	-0.7	27.0	42.6
Other commodities	3.1	4.0	7.5	8.6	10.5	5.1
% to total	2.4	2.5	4.1	4.8	4.2	2.3
%YoY	22.5	30.5	86.9	15.2	21.1	-36.5
TOTAL EXPORTS	**126.3**	**163.0**	**183.1**	**178.3**	**252.0**	**219.4**
% YoY	22.5	29.1	12.3	-2.6	41.3	28.5

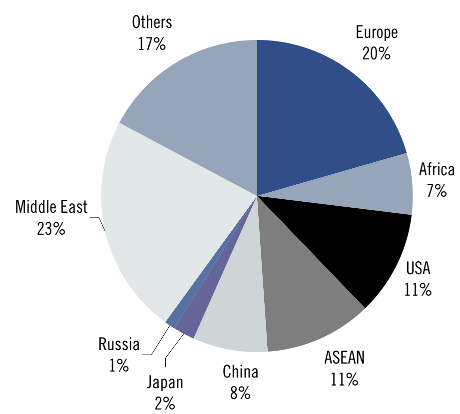
* April-Dec. Source: CMIE, RBI, Citi Research

Figure 43. Direction of Imports FY11



Source: DGCI&S, CMIE, Citi Research

Figure 44. Direction of Exports FY11



Source: DGCI&S, CMIE, CIRA

Government Finances

Figure 45. India – Snapshot of Central Government Finances (Rs Bn, %)

	FY07	FY08	FY09	FY10	FY11	FY12RE	FY13BE	BUDGET FY13– KEY HIGHLIGHTS
a. Gross Tax Revenue	**4,735**	**5,931**	**6,053**	**6,245**	**7,931**	**9,017**	**10,776**	
% to GDP	11.0	11.9	10.8	9.7	10.3	10.1	10.6	**Revenues**
% YoY	29.3	25.3	2.0	3.2	27.0	13.7	19.5	Key Assumptions: Income Tax +13.9%,
Corporation tax	1,443	1,929	2,134	2,447	2,987	3,277	3,732	Customs +22%, Excise +29.1%,
Income tax	751	1,026	1,060	1,224	1,391	1,667	1,899	Corporate +13.9%, Service +30.5%
Excise duty	1,176	1,234	1,086	1,030	1,377	1,501	1,937	
Import duty	863	1,041	999	833	1,358	1,530	1,867	Increase in service taxes from 10% to
Service tax	376	513	609	584	710	950	1,240	12%, negative list introduced
b. (-) Devolvement to States & UTs	**1,223**	**1,536**	**1,620**	**1,680**	**2,232**	**2,594**	**3,065**	Excise duties also raised from 10% to
c. Net tax revenues (a-b)	3,512	4,395	4,433	4,565	5,699	6,423	7,711	12%
d. Non tax revenues	832	1,023	969	1,163	2,186	1,247	1,646	
e. Net revenue receipts (c+d)	**4,344**	**5,419**	**5,403**	**5,728**	**7,885**	**7,670**	**9,357**	
f. Non-debt capital receipts	**64**	**439**	**67**	**332**	**353**	**298**	**417**	Divestment targets appear more realistic
Recovery of loans	59	51	61	86	124	143	117	
Divestments/Other	5	388	6	246	228	155	300	
g. TOTAL REVENUES (e+f)	**4,408**	**5,858**	**5,470**	**6,060**	**8,237**	**7,967**	**9,773**	
%YoY	22.7	32.9	-6.6	10.8	35.9	-3.3	22.7	
h. Revenue expenditure	**5,146**	**5,945**	**7,938**	**9,118**	**10,407**	**11,619**	**12,861**	**Expenditures**
Interest (1)	1,503	1,710	1,922	2,131	2,340	2,756	3,198	
Defense	517	543	733	907	921	1,048	1,138	
Subsidies	571	709	1,297	1,414	1,734	2,163	1,900	Fuel subsidies appear understated
Pensions	221	243	329	561	574	562	632	
Grants to States	357	358	382	459	498	553	642	
Admin and social services	553	647	927	1,107	1,198	1,075	1,146	
Plan expenditure	1,424	1,736	2,348	2,539	3,142	3,462	4,205	
i. Capital expenditure	**688**	**1,182**	**902**	**1,127**	**1,566**	**1,568**	**2,048**	
Defense	338	375	410	511	621	661	796	
Loans	75	493	87	121	298	102	247	
Plan expenditure	274	315	405	495	648	804	1,005	
j. Plan expenditure	**1,699**	**2,051**	**2,752**	**3,034**	**3,790**	**4,266**	**5,210**	Plan exp budgeted to rise 22.1%YoY
k Non Plan expenditure	**4,135**	**5,077**	**6,087**	**7,211**	**8,183**	**8,921**	**9,699**	Non-plan exp slated to rise 8.7%
l. TOTAL EXPENDITURE (h+i): (j+k)	**5,834**	**7,127**	**8,840**	**10,245**	**11,973**	**13,187**	**14,909**	
% YoY	15.4	22.2	24.0	15.9	16.9	10.1	13.1	
Deficit trends								
m. Fiscal Balance (g-l)	**-1,426**	**-1,270**	**-3,370**	**-4,185**	**-3,736**	**-5,220**	**-5,136**	**Fisc Deficit for FY13 budgeted at 5.1%**
% to GDP	-3.3	-2.5	-6.0	-6.5	-4.9	-5.9	-5.1	**from 5.9% in FY12RE**
n. Revenue Balance (e-h)	**-802**	**-526**	**-2,535**	**-3,390**	**-2,523**	**-3,950**	**-3,504**	We expect a slippage of ~40bps to 5.5%
% to GDP	-1.9	-1.1	-4.5	-5.2	-3.3	-4.4	-3.4	
o. Primary Deficit (m-1)	**77**	**441**	**-1,448**	**-2,054**	**-1,396**	**-2,464**	**-1,938**	
% to GDP	0.2	0.9	-2.6	-3.2	-1.8	-2.8	-1.9	
Financing the deficit								
Market borrowings (Net)	1,104	1,318	2,336	3,984	3,254	4,364	4,790	Market Borrowings are up 9.8%YoY
PPF & special deposits	52	39	80	161	125	100	120	
Small savings	0	-113	-13	133	112	-103	12	
Net external assistance	85	93	110	110	236	103	101	
Others	140	204	418	-189	-56	1,000	112	
Cash Surplus	45	-271	438	-14	64	-245	0	
Total financing								
Memo items (% to GDP)								
Centre	-3.3	-2.5	-6.0	-6.5	-4.9	-5.9	-5.1	
State	-1.8	-1.5	-2.4	-3.3	-2.5	-2.5	-2.5	
Combined	**-5.4**	**-4.1**	**-8.4**	**-9.6**	**-8.3**	**-8.0**	**-7.7**	
Off Balance Sheet Items	-0.9	-0.6	-1.7	-0.2	1.0			
Total Deficit	**-6.3**	**-4.7**	**-10.1**	**-9.8**	**-7.3**	**-8.0**	**-7.7**	
Combined liabilities	79.3	76.1	76.1	75.0	71.3	70.0	69.0	

*Includes proceeds of transfer of RBI's stake in SBI. RE: Revised Estimates; **BE: Budgeted Estimates, based on the government's nominal GDP forecast of Rs101599bn or 14%YoY.** Source: Budget Documents, CIRA

Global Forecasts

Figure 46. Selected Countries — Economic Forecast Overview (Percent) 2011-2015F

	GDP Growth					CPI					Short Term Interest Rates				
	2011	**2012**	**2013**	**2014**	**2015**	**2011**	**2012**	**2013**	**2014**	**2015**	**2011**	**2012**	**2013**	**2014**	**2015**
Global	3.0	2.6	2.7	3.6	3.7	3.7	2.8	2.7	2.8	2.8	2.53	2.35	2.34	2.60	2.89
Based on PPP weights	*3.6*	*3.0*	*3.2*	*3.9*	*4.0*	*4.2*	*3.2*	*3.1*	*3.1*	*3.1*					
Industrial Countries	1.3	1.2	1.0	2.1	2.3	2.3	1.7	1.3	1.5	1.5	0.76	0.58	0.53	0.67	0.99
United States	1.7	2.1	2.0	3.5	3.5	2.5	1.7	1.5	2.1	2.2	0.25	0.25	0.25	0.40	1.15
Japan	-0.7	2.7	1.4	1.5	1.5	-0.3	0.2	-0.1	0.3	0.4	0.10	0.10	0.10	0.10	0.13
Euro Area	1.5	-0.7	-0.8	0.8	1.1	2.7	2.3	1.6	1.1	1.0	1.19	0.75	0.5	0.5	0.5
Australia	2.0	3.7	3.4	3.8	3.8	3.4	1.8	3.2	2.9	2.7	4.75	3.56	3.44	4.5	5.0
United Kingdom	0.6	-0.4	0.6	1.1	1.7	4.5	2.6	1.8	1.8	1.6	0.5	0.5	0.5	0.5	0.5
Emerging Markets	**6.0**	**4.9**	**5.5**	**5.7**	**5.7**	**6.1**	**4.7**	**4.8**	**4.7**	**4.6**	**5.7**	**5.3**	**5.2**	**5.5**	**5.6**
China	9.2	7.8	7.9	7.6	7.3	5.4	2.9	3.1	3.8	4.0	3.2	3.2	3.0	3.6	4.0
Taiwan	4.0	2.8	4.2	4.5	4.5	1.4	1.9	2.1	1.8	1.8	0.8	0.9	0.9	1.1	1.3
India	**6.5**	**6.4**	**6.9**	**7.1**	**7.3**	**8.8**	**7.4**	**6.5**	**6.0**	**6.0**	**8.2**	**7.8**	**7.5**	**7.5**	**7.5**
Indonesia	6.5	6.1	6.3	6.7	6.5	5.4	4.4	4.7	5.3	5.8	5.4	3.8	4.2	4.5	4.6
Korea	3.6	2.8	3.6	3.8	4.0	4.0	2.8	3.0	3.1	3.0	3.2	3.1	2.9	3.5	4.3
Czech Republic	1.7	-1.0	1.0	2.6	3.3	1.9	3.2	2.4	1.8	2.3	0.8	0.6	0.3	1.0	1.6
Hungary	1.7	-0.9	0.8	2.0	2.0	3.9	5.2	3.5	3.5	3.1	6.0	6.8	6.0	6.0	5.9
Poland	4.3	2.7	2.4	3.1	3.4	4.3	3.9	2.6	2.5	2.5	4.2	4.7	4.3	4.4	4.8
Russia	4.3	3.5	4.0	4.1	4.0	8.4	5.1	6.9	5.8	5.5	8.1	8.0	7.1	6.0	6.0
Turkey	8.5	2.5	4.3	4.6	4.6	6.5	9.4	7.0	6.0	5.9	6.0	5.8	6.3	8.0	7.6
Nigeria	7.8	7.4	6.8	7.2	6.9	10.8	12.4	9.8	10.3	9.5	8.9	15.0	12.5	10.5	10.0
South Africa	3.1	2.7	3.6	4.4	4.4	5.0	6.1	5.4	5.2	5.4	5.5	5.5	6.1	6.5	6.5
Argentina	8.9	3.0	3.0	2.0	2.0	9.8	9.6	11.4	14.4	15.0	18.4	13.5	17.7	16.0	14.0
Brazil	2.7	2.3	4.5	4.5	4.5	6.6	5.1	5.3	4.5	4.0	11.7	8.5	7.9	9.4	9.0
Mexico	3.9	3.9	3.8	3.5	3.6	3.4	4.0	3.9	3.9	3.8	4.5	4.5	4.5	4.6	5.5
Venezuela	4.2	5.0	3.5	4.0	3.0	27.1	23.6	27.5	31.6	29.6	13.3	14.4	14.4	13.0	12.9

Source: Citi Investment Research and Analysis Estimates, *Global Economic Outlook and Strategy, 27th June 2012*

Figure 47. Selected Countries — Economic Forecast Overview (Percent) 2011-2015F

	Current Balance (Pct of GDP)					Fiscal Balance (Pct of GDP)					Government Debt (Pct of GDP)				
	2011	**2012**	**2013**	**2014**	**2015**	**2011**	**2012**	**2013**	**2014**	**2015**	**2011**	**2012**	**2013**	**2014**	**2015**
Global	0.5	0.3	0.3	0.1	0.2	-4.9	-4.3	-3.4	-2.9	-2.6	80	82	82	82	81
Based on PPP weights	*0.7*	*0.5*	*0.3*	*0.1*	*0.1*	*-4.3*	*-3.9*	*-3.2*	*-2.8*	*-2.6*					
Industrial Countries	-0.5	-0.6	-0.4	-0.3	-0.2	-6.8	-5.7	-4.5	-3.8	-3.2	105	111	113	115	115
United States	-3.1	-3.2	-3.0	-3.1	-3.2	-9.4	-7.8	-5.9	-4.6	-4.0	98	104	106	108	108
Japan	2.0	1.5	1.7	2.0	2.0	-10.7	-10.5	-8.1	-7.9	-7.5	228	235	242	246	251
Euro Area	0.0	0.0	0.1	0.2	0.4	-4.1	-3.3	-2.7	-2.5	-1.8	87	95	97	97	96
Australia	-2.3	-4.1	-5.3	-4.9	-3.5	-3.4	-3.0	0.1	0.1	0.3	6	10	9	9	8
United Kingdom	-1.9	-1.7	-0.7	0.2	1.0	-8.3	-6.7	-7.9	-7.4	-6.8	83	89	96	102	106
Emerging Markets	**2.2**	**1.9**	**1.4**	**0.8**	**0.7**	**-1.5**	**-1.8**	**-1.7**	**-1.6**	**-1.7**	**34**	**34**	**33**	**32**	**31**
China	2.8	2.0	1.5	1.0	1.0	-1.3	-2.4	-1.5	-1.0	-1.0	15	16	16	15	15
Taiwan	8.8	8.7	8.4	8.0	8.0	-1.9	-1.6	-1.6	-1.3	-1.0	39	39	40	42	43
India	**-4.0**	**-3.5**	**-2.6**	**-2.2**	**-1.7**	**-8.4**	**-8.0**	**-7.7**	**-7.0**	**-6.5**	**69**	**69**	**68**	**66**	**64**
Indonesia	0.2	-1.9	-1.2	-0.9	-1.0	-1.2	-1.8	-0.7	-1.0	-0.5	26	25	24	23	23
Korea	2.4	1.8	1.9	1.2	0.2	1.5	1.2	1.5	1.6	1.5	33	3	32	31	29
Czech Republic	-3.0	-2.2	-2.2	-3.7	-2.3	-3.1	-3.2	-2.9	-2.3	-1.5	4	45	46	45	44
Hungary	1.7	1.2	1.9	1.5	1.0	4.3	-2.8	-2.5	-3.0	-3.0	8	7	78	77	77
Poland	-4.3	-3.8	-4.5	-5.2	-5.3	-5.1	-3.1	-2.5	-1.8	-1.5	54	52	50	48	47
Russia	5.3	5.8	2.4	-1.0	-1.0	2.0	0.3	0.1	-0.1	-1.1	8	9	9	8	8
Turkey	-10.0	-7.5	-6.9	-6.4	-5.9	-1.3	-2.2	-2.5	-2.5	-2.7	41	41.0	39.4	39	38
Nigeria	6.1	5.7	6.4	5.0	4.0	-3.1	-2.2	-2.1	-2.6	-3.0	NA	NA	NA	NA	NA
South Africa	-3.4	-4.7	-5.6	-6.6	-6.3	-5.0	-4.8	-4.2	-3.6	-3.5	38	41	42	43	43
Argentina	0.0	0.1	-0.3	-0.5	-0.6	-1.6	-3.0	-2.0	-1.3	-0.6	41	43	47	52	53
Brazil	-2.1	-2.1	-2.5	-2.7	-3.0	-2.6	-1.9	-2.7	-2.5	-2.3	63	63	63	64	64
Mexico	-0.8	-1.4	-2.0	-2.5	-2.4	-2.5	-2.2	-2.0	-1.9	-1.9	40	40	38	38	38
Venezuela	9.1	4.9	3.7	5.6	5.8	-5.0	-5.0	-4.0	-5.2	-5.0	43	35	35	35	36

Note: US debt and deficit figures are for the Federal government only. All other countries are general government debt and deficits.
Source: Citi Research, *Global Economic Outlook and Strategy, 27 June 2012*

Figure 48. Selected Countries — Economic Forecast Overview and Exchange Rate Forecasts (Percent) 2011-2015F

	10-Year Yields					Exchange Rates Versus U.S. Dollar*				
	2011	2012	2013	2014	2015	2011	2012	2013	2014	2015
Industrial Countries										
United States	2.80	1.80	2.25	3.00	3.40	NA	NA	NA	NA	NA
Japan	1.12	0.98	1.22	1.50	1.75	79	81	82	84	84
Euro Area	2.71	1.52	1.53	2.30	2.50	1.39	1.26	1.19	1.30	1.33
Australia	4.63	3.35	3.85	4.90	5.25	1.01	1.01	0.95	0.90	0.90
United Kingdom	3.00	1.87	2.00	2.50	3.00	1.59	1.56	1.50	1.64	1.68
Emerging Markets										
China	3.52	2.70	2.56	3.25	3.62	6.46	6.33	6.31	6.16	6.12
Taiwan	1.38	1.35	1.50	1.60	1.70	29.40	29.88	28.86	28.50	28.39
India	**8.40**	**8.25**	**8.25**	**8.25**	**8.25**	**46.63**	**53.99**	**54.74**	**52.34**	**51.43**
Indonesia	7.20	6.84	7.00	7.25	7.00	8763	9387	9630	9640	9593
Korea	3.90	3.45	3.50	4.13	4.88	1108	1146	1146	1079	1047
Czech Republic	3.68	3.39	3.39	3.46	3.82	17.7	20.4	21.8	19.0	17.9
Hungary	7.63	8.35	8.00	7.91	7.69	201	226	243	223	215
Poland	5.99	5.63	5.38	5.55	5.57	2.96	3.37	3.70	3.04	2.94
Russia	NA	NA	NA	NA	NA	29.4	32.5	34.9	33.0	31.9
Turkey	NA	NA	NA	NA	NA	1.68	1.80	1.87	1.86	1.88
Nigeria	NA	NA	NA	NA	NA	156	161	165	163	165
South Africa	8.24	8.21	8.90	9.15	9.20	7.26	8.27	8.81	8.92	9.27
Argentina	NA	NA	NA	NA	NA	4.13	4.55	5.45	6.75	8.34
Brazil	11.45	10.07	9.48	9.24	8.75	1.67	1.97	1.93	1.85	1.83
Mexico	6.83	6.26	6.74	7.10	7.38	12.4	13.4	13.4	12.3	12.5
Venezuela	13.65	12.44	12.64	13.90	13.80	4.29	4.30	6.50	6.50	9.75

Source: Citi Research, *Global Economic Outlook and Strategy, 27 June 2012*

Figure 49. Foreign Exchange Forecasts (End of Period), as of 27 June 2012

	vs. USD						vs. EUR					
	Current	Sep 12	Dec 12	Mar 13	Jun 13	Sep 13	Current	Sep 12	Dec 12	Mar 13	Jun 13	Sep 13
United States	NA	NA	NA	NA	NA	NA	1.25	1.24	1.21	1.18	1.15	1.19
Japan	80	80	81	81	82	83	100	99	98	96	95	98
Euro Area	1.25	1.24	1.21	1.18	1.15	1.19	NA	NA	NA	NA	NA	NA
Canada	1.03	1.03	1.02	1.01	1.00	0.99	1.28	1.27	1.23	1.19	1.15	1.18
Australia	1.00	1.00	0.99	0.97	0.96	0.94	1.25	1.24	1.23	1.21	1.20	1.26
New Zealand	0.79	0.79	0.77	0.75	0.73	0.70	1.59	1.56	1.56	1.57	1.58	1.69
Norway	5.99	6.06	6.19	6.34	6.47	6.24	7.49	7.50	7.48	7.47	7.45	7.42
Sweden	7.05	7.26	7.35	7.43	7.51	7.24	8.81	8.99	8.88	8.76	8.65	8.61
Switzerland	0.96	0.97	0.99	1.02	1.04	1.01	1.20	1.20	1.20	1.20	1.20	1.20
United Kingdom	1.56	1.55	1.52	1.49	1.46	1.51	0.80	0.80	0.80	0.79	0.79	0.79
China	6.36	6.33	6.34	6.34	6.35	6.30	8.0	7.8	7.7	7.5	7.3	7.5
India	**56.7**	**54.0**	**54.5**	**55.0**	**55.5**	**54.6**	**70.8**	**66.9**	**65.9**	**64.8**	**63.9**	**65.0**
Korea	1162	1140	1149	1157	1164	1142	1452	1412	1388	1363	1341	1359
Poland	3.41	3.40	3.59	3.77	3.94	3.68	4.26	4.22	4.33	4.44	4.54	4.38
Russia	33.2	33.4	34.2	34.9	35.6	34.9	41.5	41.4	41.3	41.1	41.0	41.5
South Africa	8.45	8.41	8.56	8.71	8.85	8.85	10.56	10.41	10.34	10.26	10.20	10.53
Turkey	1.82	1.78	1.82	1.85	1.88	1.87	2.28	2.21	2.19	2.18	2.17	2.23
Brazil	2.07	2.01	1.99	1.97	1.95	1.92	2.58	2.49	2.40	2.32	2.24	2.29
Mexico	13.9	13.4	13.5	13.6	13.7	13.3	17.3	16.6	16.3	16.0	15.8	15.8

Source: Citi Research, *Global Economic Outlook and Strategy, 27 June 2012*

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

Analysts' compensation is determined based upon activities and services intended to benefit the investor clients of Citigroup Global Markets Inc. and its affiliates ("the Firm"). Like all Firm employees, analysts receive compensation that is impacted by overall firm profitability which includes investment banking revenues.

For important disclosures (including copies of historical disclosures) regarding the companies that are the subject of this Citi Research product ("the Product"), please contact Citi Research, 388 Greenwich Street, 28th Floor, New York, NY, 10013, Attention: Legal/Compliance [E6WYB6412478]. In addition, the same important disclosures, with the exception of the Valuation and Risk assessments and historical disclosures, are contained on the Firm's disclosure website at https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures. Valuation and Risk assessments can be found in the text of the most recent research note/report regarding the subject company. Historical disclosures (for up to the past three years) will be provided upon request.

NON-US RESEARCH ANALYST DISCLOSURES

Non-US research analysts who have prepared this report (i.e., all research analysts listed below other than those identified as employed by Citigroup Global Markets Inc.) are not registered/qualified as research analysts with FINRA. Such research analysts may not be associated persons of the member organization and therefore may not be subject to the NYSE Rule 472 and NASD Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account. The legal entities employing the authors of this report are listed below:

Citigroup Global Markets India Private Limited	Rohini Malkani; Saurabh Handa
Citigroup Global Markets Asia	Johanna Chua

OTHER DISCLOSURES

For securities recommended in the Product in which the Firm is not a market maker, the Firm is a liquidity provider in the issuers' financial instruments and may act as principal in connection with such transactions. The Firm is a regular issuer of traded financial instruments linked to securities that may have been recommended in the Product. The Firm regularly trades in the securities of the issuer(s) discussed in the Product. The Firm may engage in securities transactions in a manner inconsistent with the Product and, with respect to securities covered by the Product, will buy or sell from customers on a principal basis.

Securities recommended, offered, or sold by the Firm: (i) are not insured by the Federal Deposit Insurance Corporation; (ii) are not deposits or other obligations of any insured depository institution (including Citibank); and (iii) are subject to investment risks, including the possible loss of the principal amount invested. Although information has been obtained from and is based upon sources that the Firm believes to be reliable, we do not guarantee its accuracy and it may be incomplete and condensed. Note, however, that the Firm has taken all reasonable steps to determine the accuracy and completeness of the disclosures made in the Important Disclosures section of the Product. The Firm's research department has received assistance from the subject company(ies) referred to in this Product including, but not limited to, discussions with management of the subject company(ies). Firm policy prohibits research analysts from sending draft research to subject companies. However, it should be presumed that the author of the Product has had discussions with the subject company to ensure factual accuracy prior to publication. All opinions, projections and estimates constitute the judgment of the author as of the date of the Product and these, plus any other information contained in the Product, are subject to change without notice. Prices and availability of financial instruments also are subject to change without notice. Notwithstanding other departments within the Firm advising the companies discussed in this Product, information obtained in such role is not used in the preparation of the Product. Although Citi Research does not set a predetermined frequency for publication, if the Product is a fundamental research report, it is the intention of Citi Research to provide research coverage of the/those issuer(s) mentioned therein, including in response to news affecting this issuer, subject to applicable quiet periods and capacity constraints. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in the Product must take into account existing public information on such security or any registered prospectus.

Investing in non-U.S. securities, including ADRs, may entail certain risks. The securities of non-U.S. issuers may not be registered with, nor be subject to the reporting requirements of the U.S. Securities and Exchange Commission. There may be limited information available on foreign securities. Foreign companies are generally not subject to uniform audit and reporting standards, practices and requirements comparable to those in the U.S. Securities of some foreign companies may be less liquid and their prices more volatile than securities of comparable U.S. companies. In addition, exchange rate movements may have an adverse effect on the value of an investment in a foreign stock and its corresponding dividend payment for U.S. investors. Net dividends to ADR investors are estimated, using withholding tax rates conventions, deemed accurate, but investors are urged to consult their tax advisor for exact dividend computations. Investors who have received the Product from the Firm may be prohibited in certain states or other jurisdictions from purchasing securities mentioned in the Product from the Firm. Please ask your Financial Consultant for additional details. Citigroup Global Markets Inc. takes responsibility for the Product in the United States. Any orders by US investors resulting from the information contained in the Product may be placed only through Citigroup Global Markets Inc.

Important Disclosures for Morgan Stanley Smith Barney LLC Customers: Morgan Stanley & Co. LLC (Morgan Stanley) research reports may be available about the companies that are the subject of this Citi Research research report. Ask your Financial Advisor or use smithbarney.com to view any

available Morgan Stanley research reports in addition to Citi Research research reports.
Important disclosure regarding the relationship between the companies that are the subject of this Citi Research research report and Morgan Stanley Smith Barney LLC and its affiliates are available at the Morgan Stanley Smith Barney disclosure website at www.morganstanleysmithbarney.com/researchdisclosures.
For Morgan Stanley and Citigroup Global Markets, Inc. specific disclosures, you may refer to www.morganstanley.com/researchdisclosures and https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures.
This Citi Research research report has been reviewed and approved on behalf of Morgan Stanley Smith Barney LLC. This review and approval was conducted by the same person who reviewed this research report on behalf of Citi Research. This could create a conflict of interest.

The Citigroup legal entity that takes responsibility for the production of the Product is the legal entity which the first named author is employed by. The Product is made available in **Australia** through Citi Global Markets Australia Pty Ltd. (ABN 64 003 114 832 and AFSL No. 240992), participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is made available in Australia to Private Banking wholesale clients through Citigroup Pty Limited (ABN 88 004 325 080 and AFSL 238098). Citigroup Pty Limited provides all financial product advice to Australian Private Banking wholesale clients through bankers and relationship managers. If there is any doubt about the suitability of investments held in Citigroup Private Bank accounts, investors should contact the Citigroup Private Bank in Australia. Citigroup companies may compensate affiliates and their representatives for providing products and services to clients. The Product is made available in **Brazil** by Citigroup Global Markets Brasil - CCTVM SA, which is regulated by CVM - Comissão de Valores Mobiliários, BACEN - Brazilian Central Bank, APIMEC - Associação dos Analistas e Profissionais de Investimento do Mercado de Capitais and ANBID - Associação Nacional dos Bancos de Investimento. Av. Paulista, 1111 - 11º andar - CEP. 01311920 - São Paulo - SP. If the Product 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. This product is available in **Chile** through Banchile Corredores de Bolsa S.A., an indirect subsidiary of Citigroup Inc., which is regulated by the Superintendencia de Valores y Seguros. Agustinas 975, piso 2, Santiago, Chile. The Product is made available in **France** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 1-5 Rue Paul Cézanne, 8ème, Paris, France. The Product is distributed in **Germany** by Citigroup Global Markets Deutschland AG ("CGMD"), which is regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin). CGMD, Reuterweg 16, 60323 Frankfurt am Main. Research which relates to "securities" (as defined in the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong)) is issued in **Hong Kong** by, or on behalf of, Citigroup Global Markets Asia Limited which takes full responsibility for its content. Citigroup Global Markets Asia Ltd. is regulated by Hong Kong Securities and Futures Commission. If the Research is made available through Citibank, N.A., Hong Kong Branch, for its clients in Citi Private Bank, it is made available by Citibank N.A., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. Citibank N.A. is regulated by the Hong Kong Monetary Authority. Please contact your Private Banker in Citibank N.A., Hong Kong, Branch if you have any queries on or any matters arising from or in connection with this document. 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. The Product is made available in **Indonesia** through PT Citigroup Securities Indonesia. 5/F, Citibank Tower, Bapindo Plaza, Jl. Jend. Sudirman Kav. 54-55, Jakarta 12190. Neither this Product nor any copy hereof may be distributed in Indonesia or to any Indonesian citizens wherever they are domiciled or to Indonesian residents except in compliance with applicable capital market laws and regulations. This Product is not an offer of securities in Indonesia. The securities referred to in this Product have not been registered with the Capital Market and Financial Institutions Supervisory Agency (BAPEPAM-LK) pursuant to relevant capital market laws and regulations, and may not be offered or sold within the territory of the Republic of Indonesia or to Indonesian citizens through a public offering or in circumstances which constitute an offer within the meaning of the Indonesian capital market laws and regulations. The Product is made available in **Israel** through Citibank NA, regulated by the Bank of Israel and the Israeli Securities Authority. Citibank, N.A, Platinum Building, 21 Ha'arba'ah St, Tel Aviv, Israel. The Product is made available in **Italy** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. Via dei Mercanti, 12, Milan, 20121, Italy. The Product is made available in **Japan** by Citigroup Global Markets Japan Inc. ("CGMJ"), which 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. If the Product was distributed by SMBC Nikko Securities Inc. it is being so distributed under license. In the event that an error is found in an CGMJ research report, a revised version will be posted on the Firm's Citi Velocity website. If you have questions regarding Citi Velocity, please call (81 3) 6270-3019 for help. The Product is made available in **Korea** by Citigroup Global Markets Korea Securities Ltd., which is regulated by the Financial Services Commission, the Financial Supervisory Service and the Korea Financial Investment Association (KOFIA). Citibank Building, 39 Da-dong, Jung-gu, Seoul 110-180, Korea. KOFIA makes available registration information of research analysts on its website. Please visit the following website if you wish to find KOFIA registration information on research analysts of Citigroup Global Markets Korea Securities Ltd. http://dis.kofia.or.kr/fs/dis2/fundMgr/DISFundMgrAnalystPop.jsp?companyCd2=A03030&pageDiv=02. The Product is made available in **Malaysia** by Citigroup Global Markets Malaysia Sdn Bhd (Company No. 460819-D) ("CGMM") to its clients and CGMM takes responsibility for its contents. CGMM is regulated by the Securities Commission of Malaysia. Please contact CGMM at Level 43 Menara Citibank, 165 Jalan Ampang, 50450 Kuala Lumpur, Malaysia in respect of any matters arising from, or in connection with, the Product. The Product is made available in **Mexico** by Acciones y Valores Banamex, S.A. De C. V., Casa de Bolsa, Integrante del Grupo Financiero Banamex ("Accival") which is a wholly owned subsidiary of Citigroup Inc. and is regulated by Comision Nacional Bancaria y de Valores. Reforma 398, Col. Juarez, 06600 Mexico, D.F. In **New Zealand** the Product is made available to 'wholesale clients' only as defined by s5C(1) of the Financial Advisers Act 2008 ('FAA') through Citigroup Global Markets Australia Pty Ltd (ABN 64 003 114 832 and AFSL No. 240992), an overseas financial adviser as defined by the FAA, participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is made available in **Pakistan** by Citibank N.A. Pakistan branch, which is regulated by the State Bank of Pakistan and Securities Exchange Commission, Pakistan. AWT Plaza, 1.1. Chundrigar Road, P.O. Box 4889, Karachi-74200. The Product is made available in the **Philippines** through Citicorp Financial Services and Insurance Brokerage Philippines, Inc., which is regulated by the Philippines Securities and Exchange Commission. 20th Floor Citibank Square Bldg. The Product is made available in the Philippines through Citibank NA Philippines branch, Citibank Tower, 8741 Paseo De Roxas, Makati City, Manila. Citibank NA Philippines NA is regulated by The Bangko Sentral ng Pilipinas. The Product is made available in **Poland** by Dom Maklerski Banku Handlowego SA an indirect subsidiary of Citigroup Inc., which is regulated by Komisja Nadzoru Finansowego. Dom Maklerski Banku Handlowego S.A. ul.Senatorska 16, 00-923 Warszawa. 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 Gasheka Street, 125047 Moscow. The Product is made available in **Singapore** through Citigroup Global Markets Singapore Pte. Ltd. ("CGMSPL"), a capital markets services license holder, and regulated by Monetary Authority of Singapore. Please contact CGMSPL at 8 Marina View, 21st Floor Asia Square Tower 1, Singapore 018960, in respect of any matters arising from, or in connection with, the analysis of this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). The Product is made available by The Citigroup Private Bank in Singapore through Citibank, N.A., Singapore Branch, a licensed bank in Singapore that is regulated by Monetary Authority of Singapore. Please contact your Private Banker in Citibank N.A., Singapore Branch if you have any queries on or any matters arising from or in connection with this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). This report is distributed in Singapore by Citibank Singapore Ltd ("CSL") to selected Citigold/Citigold Private Clients. CSL provides no independent research or analysis of the substance or in preparation of this report. Please contact your Citigold//Citigold Private Client Relationship Manager in CSL if you have any queries on or any matters arising from or in connection with this report. This report is intended for recipients who are accredited investors as defined under the Securities and Futures Act (Cap. 289). 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 JSE Securities Exchange South Africa, South African Reserve Bank and the Financial Services Board. The investments and services contained herein are not available to private customers in South Africa. The Product is made available in **Spain** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 29 Jose Ortega Y Gasset, 4th Floor, Madrid, 28006, Spain. The Product is made available in the **Republic of China** through Citigroup Global Markets Taiwan Securities Company Ltd. ("CGMTS"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan and/or through Citibank Securities (Taiwan) Company Limited ("CSTL"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan, subject to the respective license scope of each entity and the applicable laws and regulations in the Republic of China. CGMTS and CSTL are both regulated by the Securities and Futures Bureau of the Financial Supervisory Commission of Taiwan, the Republic of China. No portion of the Product may be reproduced or quoted in the Republic of China by the press or any third parties [without the written authorization of CGMTS and CSTL]. If the Product covers securities which are not allowed to be offered or traded in the Republic of China, neither the Product nor any information contained in the Product shall be considered as advertising the securities or making recommendation of the securities in the Republic of China. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security or financial products. Any decision to purchase securities or financial products mentioned in the Product must take into account existing public information on such security or the financial products or any registered prospectus. The Product is made available in **Thailand** through Citicorp Securities (Thailand) Ltd., which is regulated by the Securities and Exchange Commission of Thailand. 18/F, 22/F and 29/F, 82 North Sathorn Road, Silom, Bangrak, Bangkok 10500, Thailand. The Product is made available in **Turkey** through Citibank AS which is regulated by Capital Markets Board. Tekfen Tower, Eski Buyukdere Caddesi # 209 Kat 2B, 23294 Levent, Istanbul, Turkey. In the **U.A.E**, these materials (the "Materials") are communicated by Citigroup Global Markets Limited, DIFC branch ("CGML"), an entity registered in the Dubai International Financial Center ("DIFC") and licensed and regulated by the Dubai Financial Services Authority ("DFSA") to Professional Clients and Market Counterparties only and should not be relied upon or distributed to Retail Clients. A distribution of the different Citi Research ratings distribution, in percentage terms for Investments in each sector covered is made available on request. Financial products and/or services to which the Materials relate will only be made available to Professional Clients and Market Counterparties. The Product is made available in **United Kingdom** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. This material may relate to investments or services of a person outside of the UK or to other matters which are not regulated by the FSA and further details as to where this may be the case are available upon request in respect of this material. Citigroup Centre, Canada Square, Canary Wharf, London, E14 5LB. The Product is made available in **United States** by Citigroup Global Markets Inc, which is a member of FINRA and registered with the US Securities and Exchange Commission. 388 Greenwich Street, New York, NY 10013. Unless specified to the contrary, within EU Member States, the Product is made available by Citigroup Global Markets Limited, which is regulated by Financial Services Authority.

Pursuant to Comissão de Valores Mobiliários Rule 483, Citi is required to disclose whether a Citi related company or business has a commercial relationship with the subject company. Considering that Citi operates multiple businesses in more than 100 countries around the world, it is likely that Citi has a commercial relationship with the subject company.

Many European regulators require that a firm must establish, implement and make available a policy for managing conflicts of interest arising as a result of publication or distribution of investment research. The policy applicable to Citi Research's Products can be found at https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures.

Compensation of equity research analysts is determined by equity research management and Citigroup's senior management and is not linked to specific transactions or recommendations.

The Product may have been distributed simultaneously, in multiple formats, to the Firm's worldwide institutional and retail customers. The Product is not to be construed as providing investment services in any jurisdiction where the provision of such services would not be permitted.

Subject to the nature and contents of the Product, the investments described therein are subject to fluctuations in price and/or value and investors may get back less than originally invested. Certain high-volatility investments can be subject to sudden and large falls in value that could equal or exceed the amount invested. Certain investments contained in the Product may have tax implications for private customers whereby levels and basis of taxation may be subject to change. If in doubt, investors should seek advice from a tax adviser. The Product does not purport to identify the nature of the specific market or other risks associated with a particular transaction. Advice in the Product is general and should not be construed as personal advice given it has been prepared without taking account of the objectives, financial situation or needs of any particular investor. Accordingly, investors should, before acting on the advice, consider the appropriateness of the advice, having regard to their objectives, financial situation and needs. Prior to acquiring any financial product, it is the client's responsibility to obtain the relevant offer document for the product and consider it before making a decision as to whether to purchase the product.

With the exception of our product that is made available only to Qualified Institutional Buyers (QIBs), Citi Research concurrently disseminates its research via proprietary and non-proprietary electronic distribution platforms. Periodically, individual Citi Research analysts may also opt to circulate research posted on such platforms to one or more clients by email. Such email distribution is discretionary and is done only after the research has been disseminated via the aforementioned distribution channels. Citi Research simultaneously distributes product that is limited to QIBs only through email distribution.

The level and types of services provided by Citi Research analysts to clients may vary depending on various factors such as the client's individual preferences as to the frequency and manner of receiving communications from analysts, the client's risk profile and investment focus and perspective (e.g. market-wide, sector specific, long term, short-term etc.), the size and scope of the overall client relationship with Citi and legal and regulatory constraints.

Citi Research product may source data from dataCentral. dataCentral is a Citi Research proprietary database, which includes Citi estimates, data from company reports and feeds from Reuters and Datastream.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST