

GILT NEWS

for the fortnight ended 04 June, 2010

Economy & Financial Markets Review

Domestic Developments

Indian economy notches higher than estimated growth of 7.4% in FY 2009-10

Food inflation rises to 16.55% as against 16.23% in previous week

Credit growth rate rises past 18.0%; Deposits register y-o-y growth of 14.16%

International Developments

Disappointing employment data pulls down US treasury yields

Benchmark 10-yr US treasury yield declines by 4 bps to end the fortnight at 3.20%

Crude oil closes the fortnight at USD 71.51 a barrel after touching USD 70.04 during the fortnight

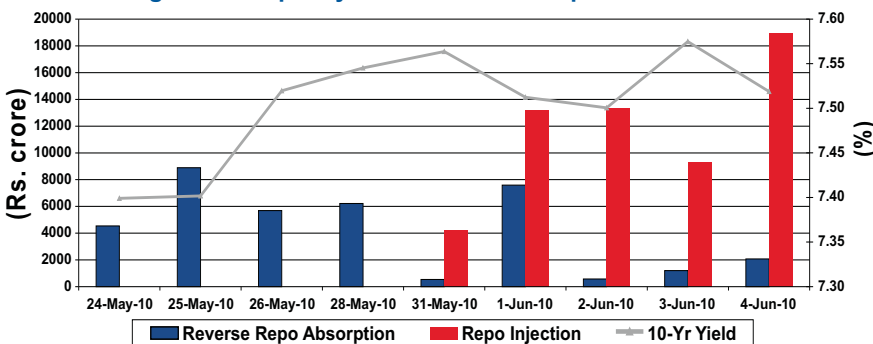
G-sec Market

Tight liquidity condition weighs on domestic bond market

Government borrows Rs. 25,000 crore during the fortnight

Yield on 7.80% GOI 2020 rises to 7.52% from 7.38% in the previous fortnight

Tightened Liquidity Conditions Push Up 10-Yr Yield



Money Market

Call and CBLO rates end the fortnight at 4.89% and 4.46% respectively

RBI injects funds to the tune of Rs. 11,800 crore on a daily average basis during the second week of fortnight

Forex Market

Rebound in domestic equity market helps ease pressure on rupee

Rupee ends the fortnight at 46.84/USD vis-à-vis previous fortnight's level of 45.93/USD

Fortnightly average of 3M & 6M fwd annualized premia at 3.13% & 2.56% as against previous fortnight's level of 2.59% & 2.41% respectively

Equity Market

Improved global conditions and robust domestic GDP figures lift up equity markets

Sensex and Nifty rise by 4.08% & 4.14% respectively

MACROECONOMIC INDICATORS

(Rs. Billion)

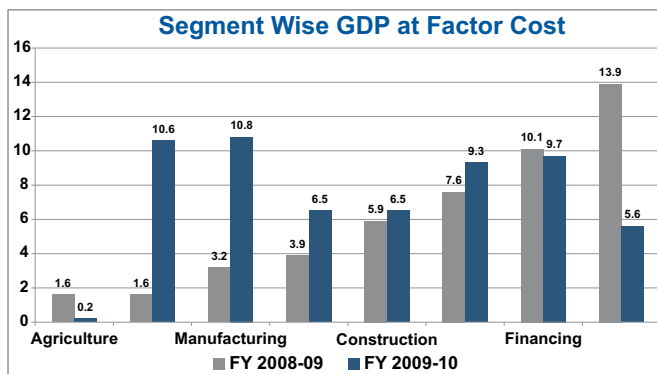
	As on 21st May'10	Variation over the fortnight	Variation over LRF of March	YOY % growth
Aggregate Deposits	45,262	(50)	334	14.16
Bank Credit	32,302	24	(146)	18.04
Non - food Credit	31,808	56	(155)	18.73
Banks Investment in G-Sec	14,383	165	599	15.38
Broad Money M3	56,722	88	927	14.55
Reserve Money 28/05	11,866	178	313	24.21
Market Stabilisation Scheme Outstanding 28/05	3	0		0.00
Forex Reserves (USD bn) 28/05	272	(1.3)	(7)	3.68
Credit - Deposit Ratio	71.37			
LAF Repo Rate (%)	5.25			
LAF Reverse Repo Rate (%)	3.75			
Cash Reserve Ratio (%)	6.00			



DOMESTIC DEVELOPMENTS

8.6% Growth in the Fourth Quarter Pushes Annual GDP Growth to 7.4%

The Indian economy notched up a brilliant 7.4% growth during FY 2009-10 backed by robust 8.6% growth recorded in the last quarter of the year. Higher than estimate GDP growth figures underscore strong revival in domestic demand. The growth was led by the manufacturing sector which grew at an annual rate of 16.3% during the fourth quarter. During the year manufacturing sector witnessed a growth of 10.8% as against 3.2% in the previous year. 0.7% rise in agricultural output in the last quarter came off as a pleasant surprise as the same pushed up the growth rate for the whole year to 0.2% as against a contraction of 0.2% indicated as per the advanced estimates. Expectation of normal monsoons for the current year augurs well for the agriculture sector which could give further boost to the economy. Growth in services sector was dragged down by slower growth in community and social services as government expenditure declined as against the previous year. The growth rate of the "community, social and personal services" sector declined considerably to 5.6% which is much lower than the advanced estimates at 8.2% and previous year's growth figure of 13.9%.



Banks investment in G-sec rises by Rs. 165 crore during the fortnight

Food Inflation Accelerates to 16.55%

After witnessing a brief spell of cool down, food inflation quickened to 16.55% in the week ended 22nd May'10 as against 16.23% in the previous week. The rise was mainly on back of rise in prices of milk, pulses and fruits. However, stubborn food prices are expected to soften on back of good rabi crop in coming months. On the other hand index of primary articles which includes food articles rose by 16.89% as against 15.90% in the previous week. The fuel group inflation also surged sharply to 14.14% as against 12.08% in the previous week. De regulation of fuel prices if implemented may exert further pressure on the overall inflation figure.

Bank Credit growth climbs above 18.0%

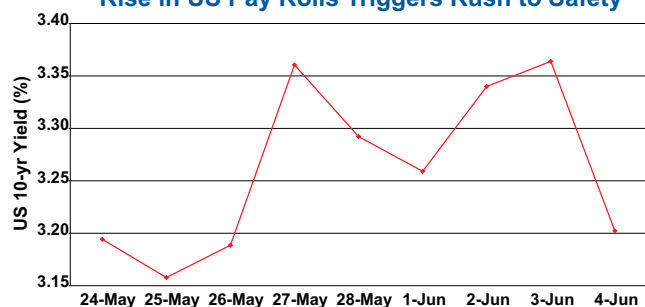
Credit growth picked up further momentum and y-o-y growth rate rose to 18.04% on back of huge disbursements to infrastructure sector. During the fortnight, banks disbursed funds aggregating Rs. 24 billion. Non food credit registered growth of 18.73%. Banks investment in G-sec rose by Rs. 165 crore during the fortnight. During the fortnight, deposits mobilized fell by Rs. 50 billion mainly due to decline in time deposits. On a year-on-year basis, deposits rose 14.16%.

INTERNATIONAL DEVELOPMENTS

US Treasuries

US treasuries started the fortnight on a positive note amid persisting European crisis concerns. Amid high risk aversion

US 10-yr Yield Ends Flat as Lower Than Estimated Rise in US Pay Rolls Triggers Rush to Safety



demand for treasuries remained high and government sold 2-yr paper at record low yield. However, yields began to rise owing to huge auctions amid signs of recovery in economy. In auctions, demand from indirect bidders which includes foreign central banks declined significantly. Fading away of worsening of European crisis concerns led to an over 18 bps rise in 10-yr yield in a single day. Yields eased towards end of first half as government data showed consumer spending in the U.S. unexpectedly stalled in April, fueling speculation of slow economic recovery. Decline in China's factory growth rate and prospects of more bank write downs in Europe pulled down yields on short-term securities. After registering the highest monthly decline since 2008, yields rose during remaining part of the fortnight as robust data releases reduced demand for safe haven securities. Rise in pending home resale and expectation of favorable US payroll and unemployment rate data pulled treasury prices lower. On the last day of the fortnight, weaker-than-expected data release triggered a rally in the treasuries resulting in yield on 10-yr paper easing to 3.20% as against previous fortnight's close of 3.24%.

Global Economic Calendar

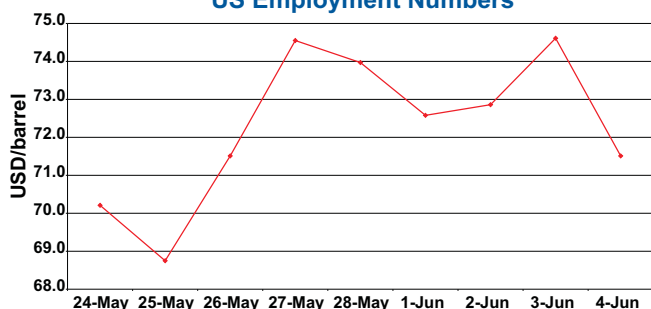
Date	Event
10-Jun	US Trade Balance, Apr (USD -40.4 bn)
	BoE & ECB Monetary Policy Meet
11-Jun	US Advance Retail Sales, May (0.4%)
14-Jun	BoJ Monetary Policy Meet
16-Jun	US Industrial Production, May (0.8%)
	US Housing Starts, Apr (672K)
	US Producer Price Index, May (5.5%)
17-Jun	US Consumer Price Index, May (2.2%)
	US Leading Indicators, May (-0.1%)

*[Figures in () are prior readings]

Economic International Crude Oil

After falling sharply in the previous fortnight, crude oil prices recovered and rose by 5.6% during the first week of the fortnight ended 4th June'10. Though a stronger dollar weighed on crude prices in the beginning of the fortnight, prices jumped above USD 70 a barrel following reports stating that demand for fuels in US rose to the highest level in over a year and durable goods orders surged. Rally in global equities on easing of concerns over Euro crisis also boosted sentiments. However prices dipped marginally after Fitch reduced AAA rating of Spain which accelerated demand for dollar. In the second week of the fortnight, oil failed to maintain the upward momentum as disappointing Chinese manufacturing data weighed on sentiments. Though decline in US gasoline stockpiles helped reverse losses, continued strengthening of dollar against the euro capped sharp rise in prices. Oil plunged sharply on the last trading day of the fortnight falling by as much as 4.16% on lower than estimated rise in non farm payrolls in the month of May'10. Payrolls rose by 4,31,000 in May as against an estimate of 5,36,000. After taking a hit from disappointing employment data, crude oil closed the fortnight at USD 71.51 a barrel as against USD 70.04 a barrel in the previous fortnight.

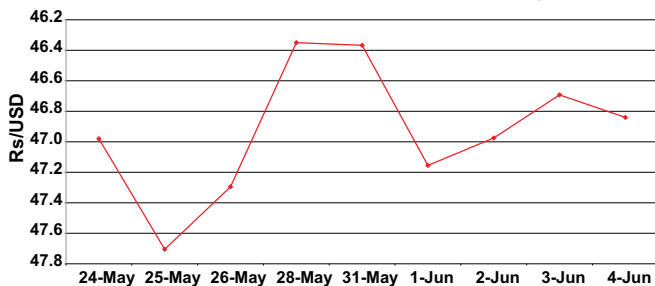
Crude Oil Pares Gains on Back of Disappointing US Employment Numbers



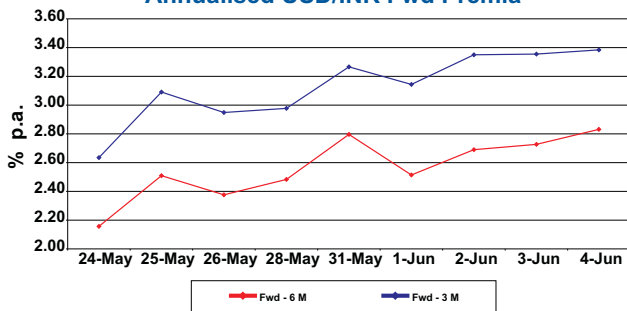
FOREX MARKET

Rupee declined to eight-month low level during the fortnight owing to continuous slide in equities. With rise in risk aversion

Rupee Climbs Up in Tandem With Equity Markets



Annualised USD/INR Fwd Premia



Major Stock Indices

	21-May-10	4-Jun-10	% change
Indian Indices			
Sensex	16,446	17,117	4.08%
Nifty	4,931	5,136	4.14%
Banking	2,876	3,069	6.72%
Healthcare	5,047	5,296	4.95%
FMCG	10,394	10,773	3.65%
IT	7,399	7,894	6.70%
PSU	13,386	13,809	3.16%
Auto	5,279	5,509	4.36%
Capital Goods	8,842	9,171	3.73%
World Indices			
Dow Jones	10,193	9,932	-2.56%
Nikkei	9,785	9,901	1.19%
FTSE	5,063	5,126	1.25%

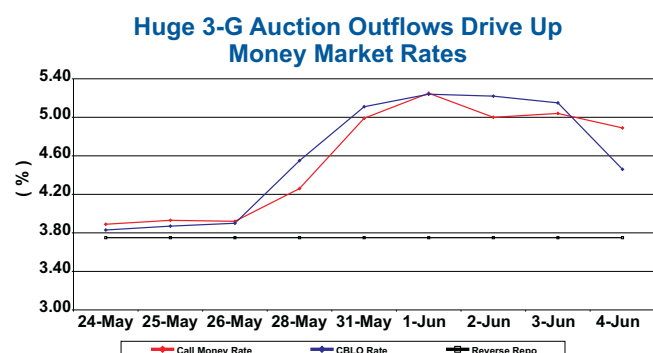
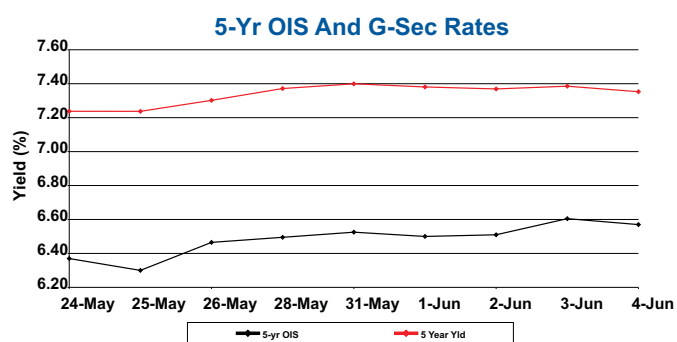
due to European crisis, foreign fund houses pulled out funds from volatile emerging markets resulting in high demand for dollars. Rupee, however, recovered smartly during the middle of the week after regional stocks rally spurred risk-taking and exporters took advantage of recent weakness to repatriate funds. Rupee registered decline of 4.3% during the month of May. Release of robust GDP figures provided some support to rupee but weak Chinese manufacturing data spurred concern that Europe's financial crisis will derail global economic recovery. Continued decline in stock market index too weighed on market sentiments as foreign investors are expected to further reduce holdings of Indian assets. However, recovery in global and domestic equity markets helped rupee stabilize a bit towards the end of the fortnight. Rupee closed the fortnight at 46.84/USD as against previous fortnight's closing of 46.92/USD.

EQUITY MARKET

Equity markets recovered during the fortnight and rose consistently under improving global and domestic economic conditions. Pact between the industrialist Ambani brothers triggered a rally followed by heavy profit booking which capped gains. Continued profit booking and pulling out of funds by foreign investors owing to weak global cues pulled Sensex below 16,000-points mark. Thereafter Sensex witnessed a major rebound to end the fortnight above 17,000-points. Recovery in European and Asian markets induced buying which was further accentuated by release of robust GDP numbers. GDP for Q4 rose to 8.6% as against 6.5% during Q3. Decline in Chinese manufacturing pace raised concerns over global economic conditions and Sensex declined owing to sell-off in major shares. However, firming global trends in subsequent days induced buying. IT and Banking sectors remained best performers and grew by 6.7% and 6.72% respectively. Sensex and Nifty grew by 4.08% and 4.14% respectively during the fortnight. Globally, Dow Jones plunged below 10,000-points after release of weak US jobs reports.

INTEREST RATE DERIVATIVES

Swap rates rose considerably during the fortnight amid tight liquidity conditions. Short-term rates especially 1-month rates shot up after payment of license fee of around Rs. 67,000 crore by telecom companies led to a considerable decline in liquidity. 1-month OIS rates traded above 2-month and 3-month swap rates. As the current tight liquidity condition is considered to be a short term phenomenon and rates are expected to ease in July, 1-month OIS rate firmed up the most by 50 bps during the fortnight while 3-month OIS rates firmed up by 34 bps. 5-yr



swaps used mostly for hedging of G-sec rose by 20 bps to 6.57% tracking 14 bps rise in G-sec benchmark yield. 5-year MIFOR rate too rose from 4.88% during the previous week to 5.15%.

MONEY MARKET

Call money rates firmed up considerably during the fortnight on back of squeeze in liquidity following heavy 3-G auction outflows to the tune of Rs. 67,000 crore. Advanced tax outflows that will happen near the middle of the month also prompted players to lend at higher rates. RBI infused liquidity in the second week of the fortnight aggregating Rs. 11,800 crore on a daily average basis. Reverse repo absorptions remained minimal averaging at RS. 4,144 crore during the fortnight. Both call and CBLO rates zoomed past 5.25% reflecting the tightness in liquidity condition. Call rates ended the fortnight at 4.89% versus previous fortnight's level at 3.69%. While CBLO rates ended the fortnight at 4.46% vis-à-vis previous fortnight's closing of 2.35%.

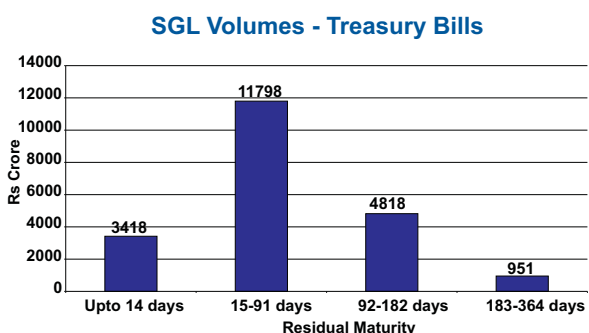
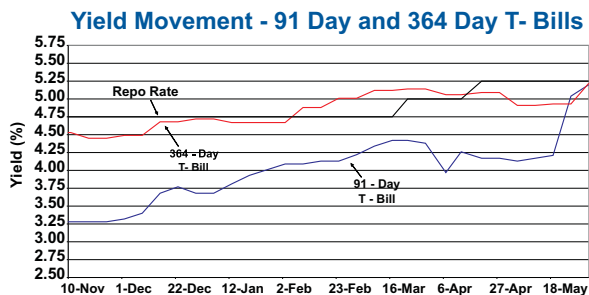
TREASURY BILLS Primary Market

During the fortnight, government raised Rs. 12,000 crore as against scheduled quantum of Rs. 17,000 crore through issuance of T-bills. Keeping in view the temporary tightness in liquidity conditions owing to huge 3-G auction advance tax outflows, RBI proactively reduced the T-bill auction quantum for the month of June from Rs. 37,000 crore to Rs. 15,000 crore. Demand in Rs.9,000 crore 91-day and 182-day T-bill auctions held in the first week remained subdued and players demanded higher yield in tandem with rise in money market rates. Cut off yield on 91-day T-bill stood at 5.04% higher than yield on 182-day T-bill which was set at 4.97%. In the second week, yields charted up further and 91 day T-bill was sold at 5.20%. On the

Details of all the Treasury bill auctions held in the fortnight ended 4th June 2010 have been tabulated as under:

(Rs. Crore)

Particulars	91 Day		182 Day	364 Day
	26 May	02 Jun	26 May	02 Jun
Cut-off Price (Rs)	98.76	98.72	97.58	95.05
Implicit Yield (%)	5.04	5.20	4.97	5.22
Weighted Avg. Yield (%)	4.87	5.12	4.91	5.19
Competitive Bids Received	11380.75	8243.50	5570.00	4725.00
Competitive Bids Accepted	7000.00	2000.00	2000.00	1000.00
Non-Competitive Bids Accepted	Nil	Nil	Nil	Nil
Total Bills Issued	7000.00	2000.00	2000.00	1000.00
Of which MSS	Nil	Nil	Nil	Nil



Tight liquidity condition led to rise in under writing fees

other hand 364-day T-bill was auctioned at a yield of 5.22% as against 4.93% in the previous fortnight.

Secondary Market

Trading volumes during the fortnight rose to Rs. 20,985 crore vis-à-vis previous fortnight's level of Rs. 18,674 crore. Average daily trading volume stood at Rs. 2,332 crore. Segment wise trades in treasury bills are given in the exhibit. Highest volume of Rs 11,798 crore was witnessed in the 15 - 91 days residual maturity bucket. During the fortnight Foreign Banks, Public Sector Banks and Private Sector Banks were net buyers while Mutual Funds and Primary Dealers were net sellers.

GOVERNMENT SECURITIES

Primary Market

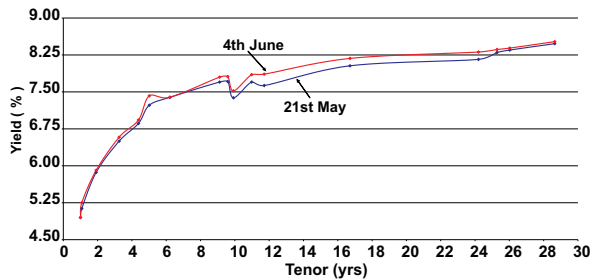
During the week GOI raised Rs. 12,000 through issue of 5-yr paper 7.38% GOI 2015 (Rs. 4,000 crore), 10-yr paper 7.80% GOI 2020 (Rs. 5,000 crore) and 22-yr paper 8.28% GOI 2032 (Rs. 3,000 crore). With yields being on a rising trend due to liquidity concerns, underwriting cut-offs rose from the previous levels and the papers were underwritten at 0.31 paise, 0.47 paise and 0.79 paise respectively. Bid-to-cover ratios too remained on a lower side except for 10-yr paper, which registered bid-to-cover ratio of 2.52. Cut-offs for 5-yr paper, 10-yr paper and 22-yr paper stood at Rs. 99.86 (YTM: 7.41%), Rs. 101.40 (YTM: 7.60%) and Rs. 100.70 (YTM: 8.25%).

In the second week, GOI raised Rs. 13,000 through issue of 6-yr paper 7.02% GOI 2016 (Rs. 5,000 crore), 12-yr paper 8.20% GOI 2022 (Rs. 5,000 crore) and 17-yr paper 8.26% GOI 2027 (Rs. 3,000 crore). Tight liquidity conditions and likelihood of this being the last auction of 6-yr security led to a rise in underwriting fee for the same to 1.58 paise. 12-yr and 17-yr paper were also subscribed at higher fee of 0.95 paise and 0.97 paise as against 0.29 paise and 0.69 paise in the previous auction of these securities. Bid-to-cover ratio of all papers remained above 2 with 12-yr paper witnessing highest ratio of 2.57. Cut-offs for 6-yr paper, 12-yr paper and 17-yr paper stood at Rs. 96.70 (YTM: 7.70%), Rs. 102.30 (YTM: 7.90%) and Rs. 100.80 (YTM: 8.18%).

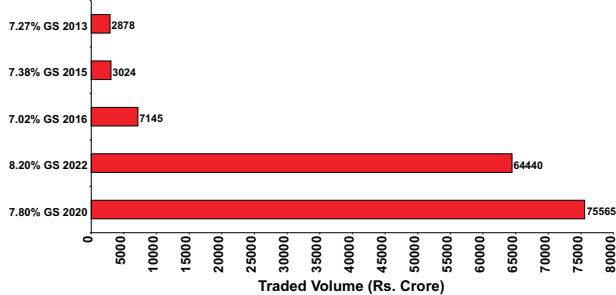
Secondary Market Developments

During the fortnight ended 4th June, bond yields rose sharply following cash concerns in the banking system due to the payment of 3-G license fees and corporate taxes. Rise in yields could also be attributed to profit booking by players after yields slipped to 6-month low levels as huge 3-G auction revenue triggered expectations of lower government borrowings for the year. Rise in US treasury yields following easing of concerns regarding the Euro crisis also led to rise in domestic bond yields. Short-term yields firmed up even more steeply reflecting the tightness in liquidity conditions. During the first week, 10-yr yield firmed

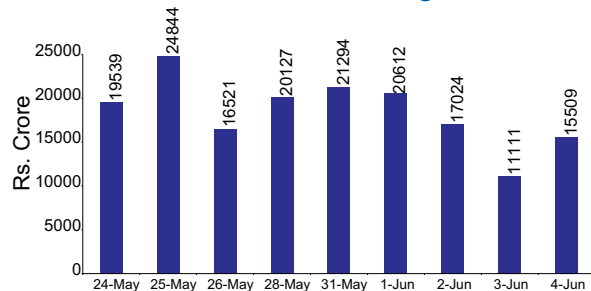
Yield Curve Shifts Upward During the Fortnight



Most Traded Securities



Dated Securities Trading Volumes



up by 17 bps to close at 7.55%. With the start of the second week, yields eased off boosted by measures taken by the central bank to prevent a severe cash crunch in the system. Apart from double LAF facility throughout June, RBI has also reduced the T-bill auction quantum for the month of June by 60%. Favourable global cues resulting from continued uncertainty over the European crisis and expectations that RBI may not hike rates before the policy review in July also pulled down yields marginally. However, yields rose again as tight domestic liquidity conditions deterred heavy buying by traders. Sentiments also remained cautious ahead crucial US employment data release and G-sec auction of Rs. 13,000 crore. However taking comfort from better than expected result in the G-sec auction, yields cooled off marginally. Yield on the 10-yr benchmark paper 7.80% GOI 2020 closed at 7.52% as against 7.38% during the previous fortnight. Spread between 30-yr and 1-yr papers rose marginally to 357 bps from 353 bps in the previous fortnight.

Trading Volumes

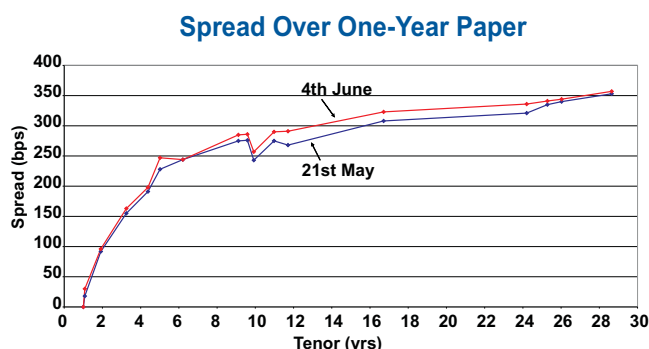
Total trading volumes declined during the fortnight to Rs. 1,66,579 crore as against Rs. 1,97,151 crore in the previous fortnight. The first week's average daily trading volume stood at Rs 20,258 crore vis-à-vis second week's level of Rs. 17,110 crore. The highest single day trading volume was Rs. 24,844 crore. Top two traded securities 7.80% GOI 2020 and 8.20% GOI 2020 cornered 91% of the top five traded securities volume. During the fortnight Public Sector Banks and Private Sector Banks were net buyers while Foreign Banks, Mutual Funds and Primary Dealers were net sellers.

OUTLOOK

Tight liquidity conditions and rise in US treasury yields drove up bond yields in the period under review. Sharp decline in systemic liquidity has been witnessed after a long gap and the central bank had remained quite watchful of the same. RBI took measures to prevent a severe crunch in liquidity and reduced the T-bill auction quantum considerably. Short term yields rose steeply resulting in flattening of the yield curve. Spread between 1-yr and 10-yr yield declined to 194 bps as against an average of 302 bps during April'10. 10-yr yield witnessed strong support near 7.60% levels. RSI of the 10-yr paper which had remained above 70 since its issuance plunged below 50 as traders turned cautious during the fortnight. Bond yields are expected to open lower in the new fortnight as sharp fall in US treasury yields following poor employment data may trigger similar movement in domestic yields. Towards the end of the first week market may witness some selling as traders may cut positions ahead of advance tax outflows which may put further pressure on already tight liquidity conditions. Domestically, players will keenly watch decision on de-regulation of oil prices, monthly inflation figure and IIP data to be released in the coming fortnight.

SPREAD MONITOR

	TTM (yrs)	YTM		Change in YTM (bps)
		21-May	4-Jun	
364 Day T Bill	1.00	4.95	4.95	0
9.39% GOI 2011	1.08	5.13	5.25	12
7.40% GOI 2012	1.92	5.87	5.91	4
7.32% GOI 2014	4.38	6.86	6.93	7
6.49% GOI 2015	5.01	7.23	7.42	19
7.02% GOI 2016	6.21	7.39	7.39	0
6.90% GOI 2019	9.11	7.70	7.80	10
6.35% GOI 2020	9.59	7.71	7.81	10
7.80% GOI 2020	9.92	7.38	7.52	14
7.94% GOI 2021	10.98	7.70	7.85	15
8.20% GOI 2022	11.71	7.63	7.86	23
8.24% GOI 2027	16.71	8.03	8.18	15
7.50% GOI 2034	24.20	8.16	8.31	15
7.40% GOI 2035	25.28	8.30	8.36	6
6.83% GOI 2039	28.65	8.48	8.52	4



CASH FLOWS FOR THE FORTHCOMING FORTNIGHT GOVERNMENT SECURITIES

(Rs. crore)

INFLOWS				OUTFLOWS		
Date	Security	Coupon Receipts	Redemptions	Date	Security	Scheduled auction amount
7-Jun	8.33% GOI 2036	2457		June 7 - 11	5-9 year	5000-6000
8-Jun	6.49% GOI 2015	1298			10-14 year	4000-5000
11-Jun	11.50% GOI 2010	411	7153		20-yr and above	2000-3000
12-Jun	6.05% GOI 2019	333		June 14 - 18	Less than 5-yr	6000-7000
12-Jun	6.17% GOI 2023	432			10-14 year	5000-6000
14-Jun	8.75% GOI 2010	22				
Total Inflows		4,953	7,153	Total Outflows		22,000

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