GILT NEWS

for the fortnight ended 16 July, 2010

Economy & Financial Markets Review

Domestic Developments

IIP shows signs of moderation, grows at 11.5% in May'10

Higher fuel prices push up June WPI inflation number to 10.55%

Inflation figure for April revised upwards to 11.23% as against 9.59% as per initial estimate

International Developments

US treasuries pare losses at the end of fortnight amid renewed concerns about the US economy

After touching a high of 3.12% during the fortnight, US 10-yr yield ends at 2.92%

Crude oil price recover to end at USD 76.01 a barrel

G-sec Market

Bond markets remain dull and range bound amid cautious market undertone

Government borrows Rs. 25,000 crore during the fortnight

Yield on 7.80% GOI 2020 ends higher at 7.64% as against 7.56% in the previous fortnight

Money Market

Call rates nudge higher on interest rate hike by RBI

RBI injects funds to the tune of Rs. 53,124 crore on a daily average basis during the fortnight

Forex Market

Rupee trades range bound amid mix global cues

Rupee ends almost flat at 46.78/USD vis-à-vis previous fortnight's level of 46.79/USD

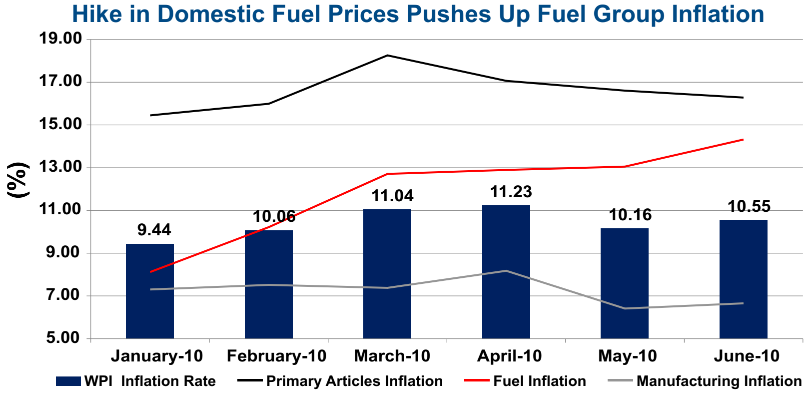
Fortnightly average of 3M & 6M fwd annualized premia at 4.47% & 3.84% as against previous fortnight's level of 3.98% & 3.56% respectively

Equity Market

Expectation of good domestic growth induces buying in equities

Sensex and Nifty decline by 2.83% & 2.99% respectively

Hike in Domestic Fuel Prices Pushes Up Fuel Group Inflation



MACROECONOMIC INDICATORS

(Rs. Billion)

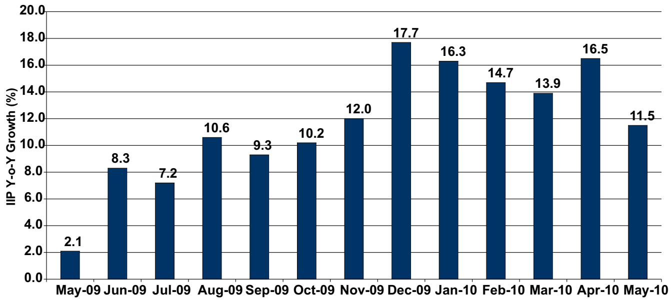
	As on 2nd July'10	Variation over the fortnight	Variation over LRF of March	YOY % growth
Aggregate Deposits	46,327	1,152	1,399	14.93
Bank Credit	34,024	920	1,576	21.71
Non - food Credit	33,479	905	1,516	22.28
Banks Investment in G-Sec	14,250	184	466	7.40
Broad Money M3	57,821	1,051	1,824	15.35
Reserve Money 09/07	11,782	(102)	226	25.02
Market Stabilisation Scheme Outstanding 09/07	3	0		
Forex Reserves (USD bn) 09/07	279	2.4	0	5.87
Credit - Deposit Ratio	73.44			
LAF Repo Rate (%)	5.50			
LAF Reverse Repo Rate (%)	4.00			
Cash Reserve Ratio (%)	6.00			

DOMESTIC DEVELOPMENTS

Industrial Production Growth Slows to 11.50%

Displaying signs of moderation after witnessing robust growth in the past seven months, the Indian industrial output dipped to grow at 11.5% in May'10 from 16.52% in April'10. Though the decline in IIP growth rate is quite remarkable, the same does not pose as a concern as the industry is expected to witness some consolidation at lower levels. Further, as the low base effect gradually phases out some more moderation in the IIP number may be witnessed in the coming months. All the three constituents of the IIP basket recorded lower growth rates during the month. Manufacturing output, which accounts for nearly 80% of the IIP basket grew at a rate of 12.3% as against 17.9% in the previous month. On the other hand, mining and electricity output grew at annual pace of 8.7% and 6.4% respectively. Within manufacturing, growth rate of capital goods segment almost halved to 34.3% from 69.9% in April'10. Consumer durables growth, too, slowed down from 32.8% in April'10 to 23.7% in May'10.

IIP Growth Moderates to 11.5%



Costlier Fuel Pushes Up WPI Inflation for June to 10.55%

The WPI inflation rate nudged higher as a result of pass through of fuel price hike announced at the end of June'10. The sharp upward revision in fuel prices was reflected in the June's fuel group inflation index as the same grew at annual rate of 14.32% as against 13.05% in the month of May'10. Manufacturing inflation too inched up to 6.66% in June'10 as against 6.41% in May'10. On the other hand, primary articles inflation witnessed marginal moderation to 16.28% as against 16.60% in the month of May. In food articles, the price increase was a marginal 0.20% during the month as cereals turned cheaper. The full impact of the fuel price hike is expected to reflect in the July inflation numbers as the effect of the same percolates to the other categories. Though the inflation figure at 10.55% came a tad lower than expectations, the sharp upward revision of April inflation figure raises concern about revision of the June figure as well. The inflation for April has been revised to 11.23% from initial estimate of 9.59%.

Wholesale Price Index

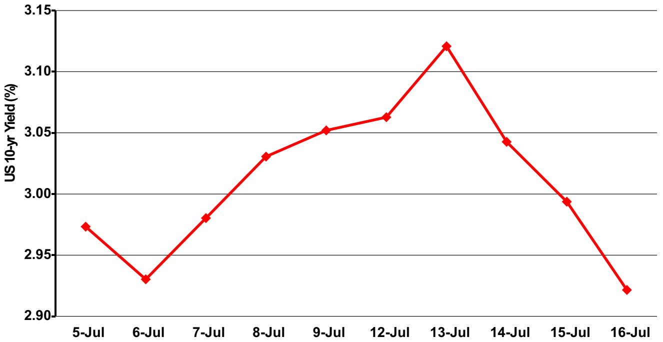
Name of commodity	Weights	Index as on		Y-O-Y % increase	
		31-May-10	30-Jun-10	31-May-10	30-Jun-10
All commodities (WPI)	100.00	258.1	259.8	10.16%	10.55%
Primary Articles	22.02	299.9	302.1	16.60%	16.28%
Fuel, Power, Light & Lubricants	14.23	368.2	374.4	13.05%	14.32%
Manufactured Products	63.75	219.1	219.5	6.41%	6.66%

INTERNATIONAL DEVELOPMENTS

US Treasuries

After easing below 3.0% mark last fortnight, treasuries started this fortnight on a shaky note as lower-than-expected job cuts turned sentiments cautious. Spread between 2-yr and 10-yr paper increased for the first time in five days on reduced deflation concern. With yields hovering near the lowest level in a year, investors refrained from building huge positions. At the same time, slew of disappointing data releases and deepening of concerns of a double dip recession prevented investors

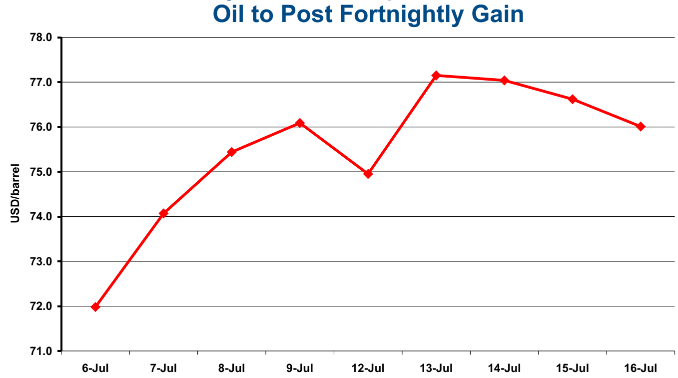
US Treasuries Reverse Losses Amid Weak Economic Data Releases



Global Economic Calendar

Date	Event	Period	Prior
20-Jul	US Housing Starts	June	593K
22-Jul	US Leading Indicators	June	0.40%
	US Existing Home Sales	June	5.66M
26-Jul	US New Home Sales	June	300K
27-Jul	US Consumer Confidence	July	52.9
30-Jul	US Core PCE QoQ	2Q	0.70%
	US GDP QoQ	2Q	2.70%

Recovery in Global Equities Direct Crude Oil to Post Fortnightly Gain



from moving away from treasuries. Towards the end of the first week, yields treaded upwards as bigger-than-forecast drop in initial claims for unemployment benefits last week damped bonds' haven appeal. Further, supply of bonds weighed heavy on treasury yields as despite good demand, yields continue to rise as investors preferred not to invest at current yield levels. Huge auction supply in 3-yr, 10-yr and 30-yr segment resulted in steepening of yield curve. Rally in the stock market too deterred investments in treasuries pushing 10-yr yield to rise to 3.12%. Towards the end of the fortnight, 10-yr yields slipped below 3.0% again as decline in retail sales followed by release of Fed minutes stating risks to the recovery has increased triggered buying. Expectation of Fed maintaining rates at record low levels for a very long time supported treasuries. On the last trading day, release of data showing declining inflation and tumbling consumer confidence enhanced the allure of treasuries. 10-yr paper ended the fortnight at 2.92% as against previous fortnight's close of 2.97%.

COMMODITIES

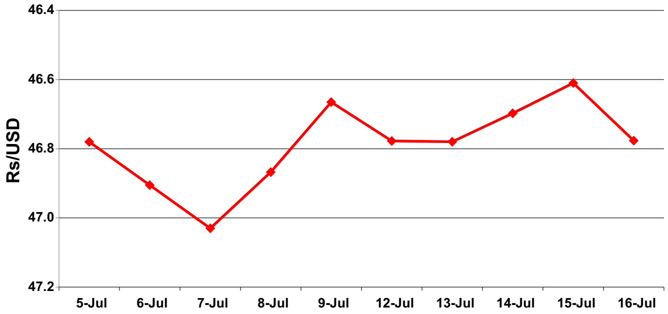
International Crude Oil

Recovering from sharp decline in the previous fortnight, crude oil prices rebounded tracking recovery in global equities. A slew of favourable economic data releases in the first week helped oil prices recover smartly from previous fortnight's lows. Growth in US retail sales at the fastest pace in almost four years triggered the upward movement pushing up oil prices by 2 dollars past USD 74 a barrel. Decline in US stockpiles and jobless claims also turned sentiments bullish. Further, rise in industrial production in Germany and upward revision of global economic growth by IMF also boosted demand for oil. With the start of the second week, oil witnessed marginal downward correction as dollar strengthened against euro on renewed concerns regarding the health of the European economy. However, oil pared losses and rose again tracking surge in equities and decline in dollar. More than expected decline in US stockpiles and increase in operating rates by oil refiners too turned market sentiments positive. However at the end of the fortnight, oil prices treaded downwards on concerns that the US economic recovery will be slow. Crude oil closed the fortnight at USD 76.01 a barrel as against USD 72.14 in the previous fortnight.

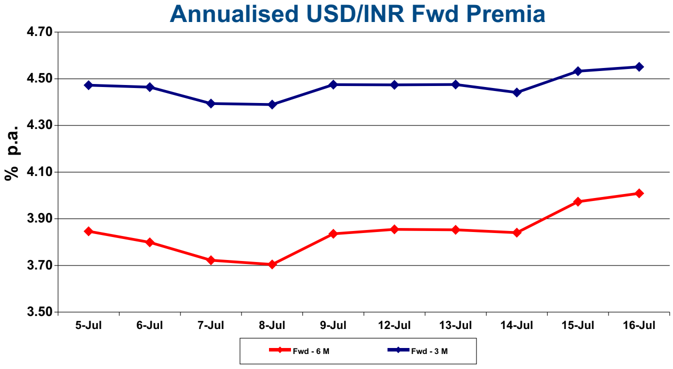
Metals

Base metals prices traded choppy during the fortnight. In the first week, traders continued to tread cautiously as the strength of US dollar continuously weighed on commodities. Moreover the concerns over pace of economic recovery weighed on prices while bargain buying supported metals somewhat. In the second week too metal trading remained lackluster and volumes

Rupee Trades Range Bound During the Fortnight



Annualised USD/INR Fwd Premia



Major Stock Indices

	2-Jul-10	16-Jul-10	% change
Indian Indices			
Sensex	17,461	17,956	2.83%
Nifty	5,237	5,394	2.99%
FMCG	3,219	3,225	0.19%
IT	5,238	5,459	4.22%
Banking	10,664	11,396	6.87%
Auto	8,184	8,337	1.86%
Capital Goods	14,494	15,010	3.56%
Healthcare	5,708	5,729	0.37%
PSU	9,445	9,389	-0.59%
World Indices			
Dow Jones	9,686	10,098	4.25%
Nikkei	9,204	9,408	2.22%
FTSE	4,838	5,159	6.63%

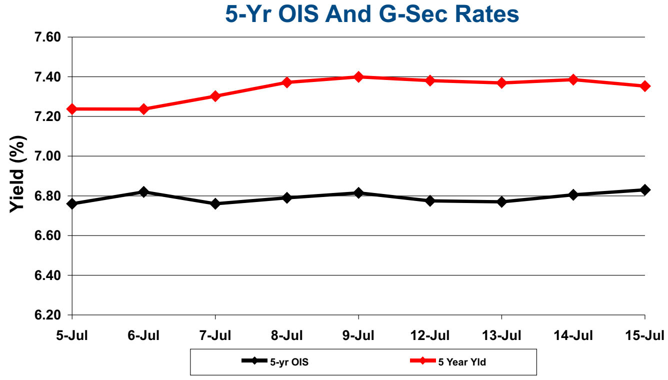
remained low. While Copper and nickel prices traded sideways, lead and zinc prices declined. Though, aluminum looks strong in base metal complex. US Empire State manufacturing index declined to 5.1 in July as against 19.6 in June, which also weighed on market sentiments.

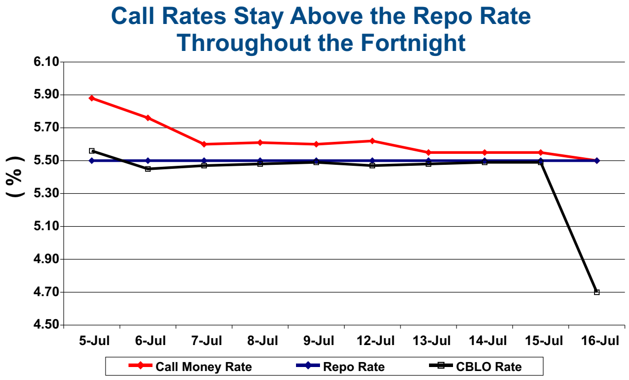
FOREX MARKET

Rupee started the fortnight on a positive note after central bank increased benchmark borrowing costs for the third time in this year. Higher interest rates are expected to boost foreign inflows in country. However, rupee failed to sustain the momentum owing to weak global economic conditions. Rupee weakened beyond 47.0/USD as foreign investors withdrew funds from equities in wake of rising fears of further decline in global economic growth. However, 9.4% growth projection for Indian economy by IMF boosted market sentiments. After rallying for 3-days, rupee weakened on announcement of lower-than-expected industrial production growth in month of May followed by dismal quarterly performance report by IT major. Rupee stabilized towards the end of the fortnight as rise in global markets and strengthening of Euro spurred optimism that the economic impact of Europe's debt crisis will be contained and investors will return to emerging markets. Rupee closed the fortnight at 46.78/USD as against previous fortnight's closing of 46.79/USD.

EQUITY MARKET

Equity markets rose considerably during the fortnight on subsiding of concerns regarding global economic condition. Market started the fortnight with a flat trading session but posted steep rise on the subsequent day riding on positive global cues and short-covering by participants. IT sector leaded the rally on expectations of strong quarterly results. However, profit booking curbed further rise in the market. The rising momentum continued in the second week as well with growth projection for Indian economy at 9.5% by IMF boosting market sentiments considerably. Sensex rose steadily to touch 18,000-points mark in intra-day trade. However, emergence of huge profit booking pressure prevented Sensex to sustain the level for long. High IIP growth of over 11.0% too supported buying. Announcement of 2.4% decline in quarterly profits by IT major deteriorated the outlook for the segment triggering a sell-off. However, market received constant support from rising global markets and firm Asian cues. On the last trading day, market witnessed volatile but rangebound trading session. TCS leaded the gainers pack on better-than-expected quarterly results announcement. Sensex ended the fortnight at 17,956 points as against 17,461 registering growth of 2.83% during the fortnight. Nifty





registered 2.99% rise and closed at 5,394 points.

In global markets, all major indices recovered sharply with European index FTSE registering 6.63% growth during the fortnight on account of subsiding of concerns over the health of the economy. Dow Jones too registered growth of 4.25% during the fortnight.

INTEREST RATE DERIVATIVES

Swap rates firmed up in the beginning of the fortnight after RBI increased the repo and reverse repo rates by 25 bps each at the end of previous fortnight. 5-yr swap rates witnessed rangebound movement during first half. After steep firming, swap rates eased somewhat moving in line with G-sec yields. However, concerns over another rate hike in the upcoming policy meet prevented much easing. In the second half, swap rates rose consistently amid tight liquidity conditions. 5-yr swap rates moved in range of 6.76% - 6.86% and closed the fortnight at 6.86% rising by 20 bps over previous closing of 6.66%. 5-year MIFOR rate firmed up marginally by 2 bps to close the fortnight at 5.30% after trading in range of 5.20% - 5.45%.

MONEY MARKET

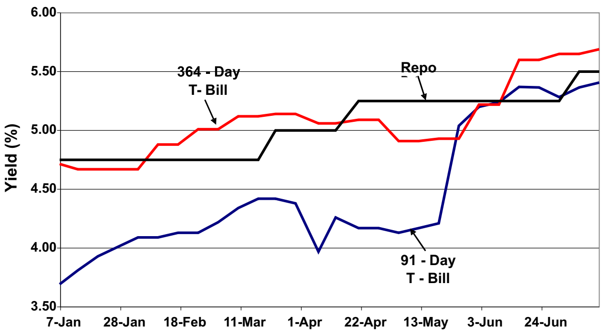
Money rates remained at elevated levels in the fortnight under review and adjusted with the new LAF corridor. Call rates continued to trade above the upper bound of the corridor as liquidity conditions remained little changed compared to the previous fortnight. CBLO rates too hovered close to the repo rate and daily average volume in the same remained low at Rs. 33,636 crore. During the fortnight, RBI injected liquidity to the tune of Rs. 53,124 crore on a daily average basis. Call rates ended the fortnight at 5.50% as compared to 5.19% in the previous fortnight. While CBLO rates ended the fortnight at 4.70% vis-à-vis previous fortnight's closing of 4.20%.

Details of all the Treasury bill auctions held in the fortnight ended 17th July 2010 have been tabulated as under:

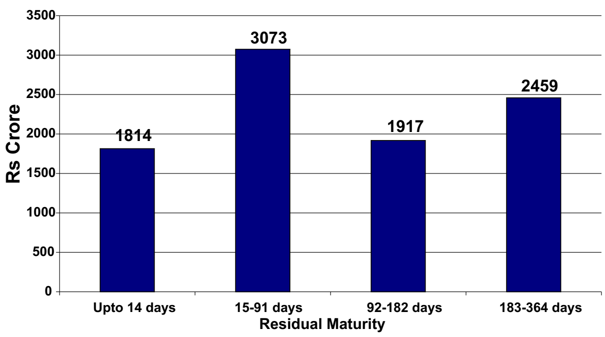
(Rs. Crore)

Particulars	91 Day		182 Day	364 Day
Date Of Auction	07 Jul	14 Jul	07 Jul	14 Jul
Cut-off Price (Rs)	98.68	98.67	97.20	94.63
Implicit Yield (%)	5.37	5.41	5.78	5.69
Weighted Avg. Yield (%)	5.32	5.37	5.63	5.66
Competitive Bids Received	8361.25	5500.43	2746.50	5460.00
Competitive Bids Accepted	2000.00	2000.00	1500.00	1000.00
Non-Competitive Bids Accepted	500.00	500.00	300.00	Nil
Total Bills Issued	2500.00	2500.00	1800.00	1000.00
Of which MSS	Nil	Nil	Nil	Nil

Yield Movement - 91 Day and 364 Day T- Bills



SGL Volumes - Treasury Bills



TREASURY BILLS

Primary Market

Short-term rates remained under pressure as liquidity condition continues to be unfavourable. GOI raised Rs. 6,500 crore by issuing T-bills during the fortnight. Cut off yield on 91-day T bill rose from 5.37% in the first week to 5.41% in the second week. Demand for 182-day T-bill remained weak as indicated by bid to cover ratio at 1.83. Yield on the same rose sharply to 5.78% as against 5.37% in the previous fortnight. On the other hand, 364-day T-bill was issued at a yield of 5.69% as against 5.65% in the previous fortnight.

Secondary Market

Trading volumes during the fortnight declined to Rs. 9,264 crore vis-à-vis previous fortnight's level of Rs. 12,640 crore. Average daily trading volume stood at Rs. 926 crore. Segment wise trades in treasury bills are given in the exhibit. Highest volume of Rs. 3,073 crore was witnessed in the 15 - 91 days residual maturity bucket. During the fortnight Public Sector Banks and Private Sector Banks were net buyers while Foreign Banks Mutual Funds and Primary Dealers were net sellers.

GOVERNMENT SECURITIES

Primary Market

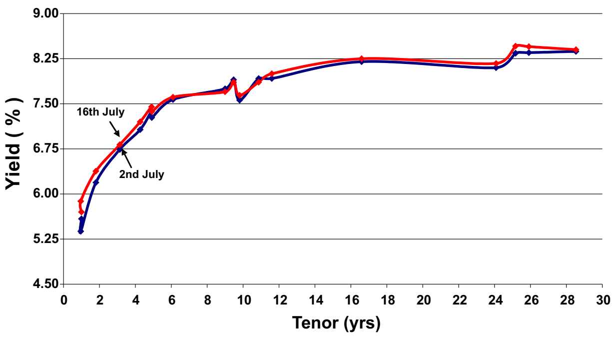
During the first week, GOI raised Rs. 12,000 crore through issue of 5-yr paper, 7.17% GOI 2015 (Rs. 4,000 crore), 10-yr paper 7.80% GOI 2020 (Rs. 5,000 crore) and 22-yr paper 8.32% GOI 2032 (Rs. 3,000 crore). The papers were underwritten at 0.75 paise, 0.89 paise and 0.90 paise respectively. The short term paper, 7.17% GOI 2015 witnessed highest demand with bid to cover ratio at 3.19. Owing to high liquidity in the paper, market participants bid aggressively resulting in the cut-off yield for the same being lower than market expectations. The 10-yr paper witnessed subdued demand and the bid-to-cover ratio remained low at 1.72. The 10-yr paper was subscribed at a yield of 7.67% (Rs. 100.90). The long term paper witnessed good demand and was sold at a yield of 8.33% (Rs. 99.92).

In the second week, GOI raised Rs. 13000 crore through issue of 7-yr paper 7.46% GOI 2017 for Rs. 5000 crore, 12-yr paper 8.20% GOI 2022 for Rs. 5,000 crore and 17-yr paper 8.26% GOI 2027 Rs. 3,000 crore. 7-yr paper and 17-yr papers were underwritten at a fee of 0.93 paise and 0.95 paise. 12-yr paper witnessed highest underwriting fee at 1.04 paise. Bid-to-cover ratio of all papers remained above 2. 7-yr paper was subscribed at cut-off price of Rs. 99.13 (YTM: 7.62%). 12-yr and 17-yr papers were subscribed at Rs.101.50 (YTM: 8.0%) and Rs. 100.20 (YTM: 8.24%) respectively.

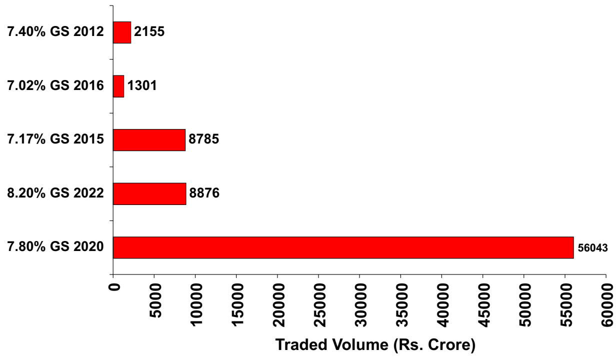
Secondary Market Developments

Bond markets remained lackluster during the fortnight as important economic data release kept traders largely at bay. Lack of firm global cues also kept sentiments cautious. Yields opened on a firm note in reaction to the unscheduled interest

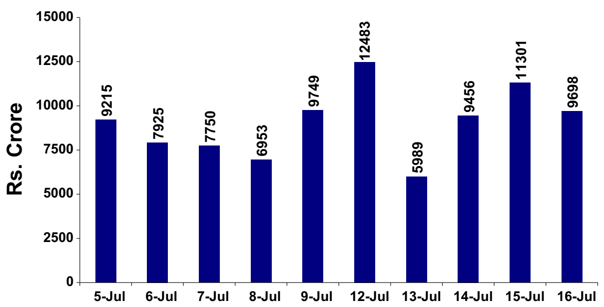
Short Term Yields Rise During the Fortnight



Most Traded Securities



Dated Securities Trading Volumes



rate hike on 2nd July'10. 10-yr yield rose past the psychological mark of 7.60% as RBI increased the repo and reverse repo rates by 25 bps a month ahead of the first quarter monetary policy review to combat stubborn inflation. Though expectation of buoyant monsoons helped in easing of yields, the decline was snapped as a slew of primary market supply in the first week prompted players to remain sidelined. Yields rose further with 10-yr yield rising to 7.65% as traders remained watchful ahead of industrial output and inflation data releases in the second week of the fortnight. With the start of the second week, yields dropped in reaction to the lower than expected IIP growth rate for the month of May. In May industrial output grew at an annual pace of 11.5% as against expectation of over 16%. Thereafter yields traded in a narrow range with an upward bias as continued rise in inflation and expectation of further rise in the same owing to the recent hike in fuel prices weighed on sentiments. Inflation showing no signs of abatement rose in the month of June'10 to 10.55% as fuel group inflation quickened. During the fortnight 10-yr yield rose by 8 bps to close at 7.64% as against 7.56% in the previous fortnight. Spread between 30-yr and 1-yr papers declined to 270 bps from 270 bps in the previous fortnight.

Trading Volumes

Total trading volumes declined during the fortnight to Rs. 90,519 crore as against Rs. 1,34,046 crore in the previous fortnight. The first week's average daily trading volume stood at Rs 8,318 crore vis-à-vis second week's level of Rs. 9,785 crore. The highest single day trading volume was Rs. 12,483 crore. Top two traded securities 7.80% GOI 2020 and 8.20% GOI 2020 cornered 84.14% of the top five traded securities volume. During the fortnight Public Sector Banks and Private Sector Banks were net buyers while Primary Dealers, Foreign Banks and Mutual Funds were net buyers while Public Sector Banks were net sellers.

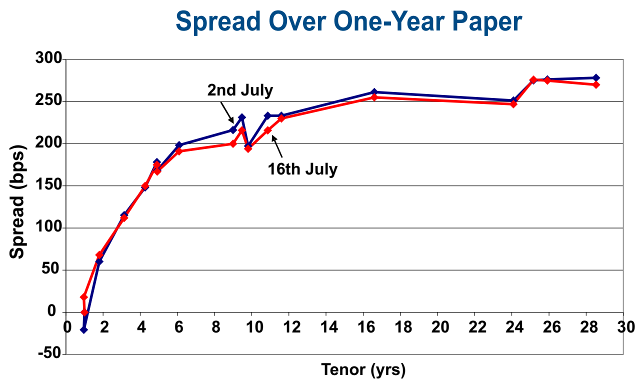
OUTLOOK

Debt market has been trading with a cautious undertone since the unscheduled rate hike by RBI on 2nd July'10. Despite lower than anticipated IIP growth rate for the month of April at 11.55%, market players refrained from building heavy position ahead of first quarter policy review. Sharp upward revision in WPI inflation rate for April to 11.23% as against initial estimate of 9.59% is weighing heavy on market sentiments as the same has raised concerns of RBI resorting to further tightening in the upcoming policy review.

In the coming fortnight, yields are expected to open lower taking cues from sharp decline in US treasury yields. Absence of G-sec auction in the first week of the fortnight may also induce demand in secondary market. However, apprehensions regarding action in first quarter policy review may cap sharp decline in yields. Though the market has discounted another 25 bps hike in the key interest rates, inflation figures released during the fortnight have raised expectations of a steeper hike in the policy rates be RBI.

SPREAD MONITOR

	TTM (yrs)	YTM		Change in YTM (bps)
		2-Jul	16-Jul	
364 Day T Bill	1.00	5.59	5.70	11
9.39% GOI 2011	0.96	5.38	5.88	50
7.40% GOI 2012	1.80	6.19	6.38	19
7.32% GOI 2014	4.27	7.07	7.20	13
6.49% GOI 2015	4.90	7.37	7.45	8
7.02% GOI 2016	6.09	7.57	7.61	4
6.90% GOI 2019	9.00	7.75	7.70	-5
6.35% GOI 2020	9.47	7.90	7.86	-4
7.80% GOI 2020	9.81	7.56	7.64	8
7.94% GOI 2021	10.86	7.92	7.86	-6
8.20% GOI 2022	11.59	7.92	8.00	8
8.24% GOI 2027	16.60	8.20	8.25	5
7.50% GOI 2034	24.08	8.10	8.17	7
7.40% GOI 2035	25.17	8.34	8.46	12
6.83% GOI 2039	28.53	8.37	8.40	3



CASH FLOWS FOR THE FORTHCOMING FORTNIGHT
GOVERNMENT SECURITIES

(Rs. crore)

INFLOWS				OUTFLOWS		
Date	Security	Coupon Receipts	Redemptions	Date	Security	Scheduled auction amount
19-Jul	6.83% GOI 2039	444	0	June 26 - 30	5-9 year	6000-7000
28-Jul	11.30% GOI 2010	1708	30235		10-14 year	5000-6000
29-Jul	12.32% GOI 2011	583	0		15-19 year	2000-3000
					20-yr and above	2000-3000
Total Inflows		**2,735**	**30,235**	**Total Outflows**		**15,000**

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