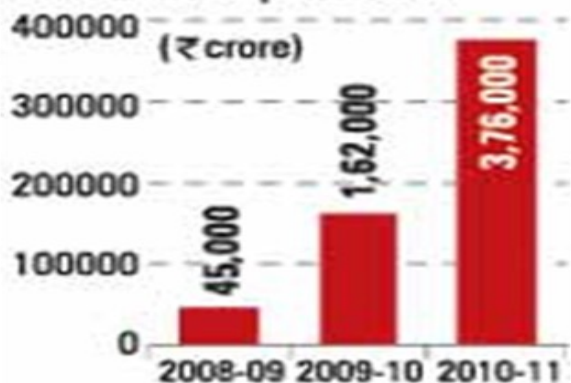


THE WEEKLY BUZZ

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Surge in inflation pushes consumer expenditure



Source: Central Statistical Organisation and CRISIL estimates

HIGH INFLATION COST INDIAN HOUSEHOLDS RS.376,000 CR. IN FY11

In the last 3 years, inflation has burnt quite a large hole in the pockets of Indian consumers. According to research done by CRISIL, galloping inflation pushed consumer expenditure up by an astounding amount of Rs 3,76,000 cr. in 2010-11—an increase of 736% over an additional expenditure of Rs 45,000 cr. in 2008-09. The study shows that growth of private consumption expenditure in nominal terms increased to nearly 17% per year during this period from 14% in the preceding 3 years mainly due to the rise in food inflation.

According to D. Joshi, chief economist at CRISIL, “The rise in inflation to 8% per year during FY09 - FY11 from 5% per year in the preceding 3 years eroded the purchasing power of money and inflated the consumption expenditure bill of Indian households by Rs 5,80,000 cr.”

Inflation was, however, not uniform, with food items seeing a sharper price increase, compared to non-food items. Food inflation stood at 11.6% during 2008-09 to 2010-11, compared to non-food inflation at 5.7%. In the non-food category, prices of many items declined. The fall in prices was more evident in the durables category, including television sets, washing machines and air conditioners. Consumers immediately feel the impact of rising inflation in food articles because these items are purchased on a daily basis. Durables are not purchased frequently and hence, a fall in their prices tends to be overlooked while forming inflation expectations.

The middle-income and high-income groups benefit more from falling prices of non-food manufactured items, particularly durable goods, as these groups have higher disposable income to spend on other goods and services, including consumer durables and for savings. The poor, with limited discretionary income to spend on consumer durables, do not benefit much from the lower prices. In contrast, rising prices of food items strain their discretionary spending.

SOON YOU CAN TRADE S&P 500 AND DJIA FUTURES ON THE NSE

The National Stock Exchange (NSE) has got regulatory approval to launch futures contracts on benchmark US indices S&P 500 and Dow Jones Industrial Average (DJIA), paving the way for Indian investors to bet on the world’s most influential stock market.

The rupee-denominated futures contracts, which are going to be launched on NSE soon, will be traded from 9 am to 5 pm from Monday to Friday. This will be the first time an Indian stock exchange will utilize the entire permitted market hours for an equity derivatives product. At present, trading in the cash and derivatives segments of both NSE and the Bombay Stock Exchange (BSE) happens between 9 am and 3:30 pm. NSE will launch four quarterly futures contracts on S&P 500 and DJIA having expiries in March, June, September and December. The expiry date for these contracts will be the third Friday of the respective contract month.

Even though Indian investors can invest up to \$200,000 a year to buy shares in overseas markets, there are a lot of restrictions in doing that. Apart from the maximum investment limit per year, Indian investors are only allowed to invest in the cash market in overseas stock exchanges at present, and not in derivatives. Therefore, these products will make a lot more sense for domestic investors who'd like to take a call on the US markets.

Of course, it has to be said that derivative contracts are not for the faint-hearted. As Warren Buffett famously said in 2002, "In my view, derivatives are financial weapons of mass destruction, carrying dangers that, while now latent, are potentially lethal."

COAL IMPORTS COULD ACCOUNT FOR 29% OF DEMAND IN 5 YEARS

In five years, India could be forced to import almost 30 per cent of the coal required to meet its electricity needs. This would mean that consumers across the country could find electricity prices shooting up. Or else, distribution utilities would be pushed closer to bankruptcy on account of the increased strain on their finances from costly coal imports.

Against a projected requirement of 742 million tonnes of thermal coal for fuelling coal-fired stations by the end of the Twelfth Plan, only 527 million tonnes of domestic coal is likely to be available even in the best case scenario. This translates into a shortfall of 215 million tonnes or 29% of India's total requirement projected by 2017.

There are two aspects to the widening gap between demand and supply. The first is the sharp increase in project commissioning in the last three years of the current Plan period, which is expected to continue into the Twelfth Plan as well, aided mainly by a private sector surge. The second is domestic coal mining is failing to keep pace with the demand.

FOREIGNERS CAN NOW DIRECTLY INVEST IN INDIAN MUTUAL FUNDS

In an attempt to manage volatile capital flows, the finance ministry has allowed foreign individuals to cumulatively invest up to \$10 billion in domestic mutual funds. The Securities and Exchange Board of India (SEBI) will notify the rules by August 1.

At present, besides resident Indians, only foreign institutional investors (FIIs), sub-accounts registered with SEBI and non-resident Indians can invest in mutual funds in India. The move will give mutual funds access to more foreign money and comes at a time when the government is finding it difficult to fund its current account deficit due to volatile capital flows and higher imports. Foreign retail participation in mutual funds may address the balance of payments problem by bringing in more stable funds and reducing the dependence on FII inflows, which are volatile.

This is the first major overhaul of the rules for foreign investment in the Indian markets since 1991, when foreign investors were allowed in through Sebi-registered FIIs.

The new class of investors, called qualified foreign investors (QFIs), will be able to invest through the depository participant (DP) route as well as the unit confirmation receipt (UCR) system, which will involve custodians. In the first option, a QFI will open a demat account with a depository in India and buy units. In the second option, an investor will place an order with an overseas depository, which will then transfer it to a custodian bank in India for buying the units. QFIs can be individuals and bodies, including pension funds. Fund houses will be responsible for deducting tax at source.

For mutual funds, besides widening the investor base, it would also give them access to international investors. Till now, major Indian mutual funds have had to set up base abroad when they wanted foreign investments, but there too, the investment was restricted to FIIs only.

Did You Know?

The Employees Provident Fund Organisation (EPFO) is starting the facility for online information on account balance from July 1, 2011. Members would have to go to the EPFO website (www.epfindia.com) and click on the relevant section for getting account balance. They will have to mention their account number and register their mobile number. Once this is done, members will receive an SMS giving details

Weekly Spotlight

	June 24	July 1	% change	
			Weekly	YTD
Sensex	18,240.68	18,762.80	↑ 2.86	↓ (8.51)
Nifty	5,471.25	5,627.20	↑ 2.85	↓ (8.27)
US	11,934.58	12,582.77	↑ 5.43	↑ 8.68
China	2,746.21	2,759.36	↑ 0.48	↓ (1.73)
Japan	9,678.71	9,868.07	↑ 1.96	↓ (3.53)
Hong Kong	22,171.95	22,398.10	↑ 1.02	↓ (2.77)
Germany	7,121.38	7,419.44	↑ 4.19	↑ 7.31
UK	5,697.70	5,989.76	↑ 5.13	↑ 1.52
Brazil	61,017.00	63,394.34	↑ 3.90	↓ (8.53)
NYMEX Crude (\$ per barrel)	91.20	94.94	↑ 4.10	↑ 3.87
Gold (\$ per oz)	1,514.75	1,483.00	↓ (2.10)	↑ 5.51
Weekly DII Inflow (Rs.cr)	1,206.19	(2,810.73)		
Weekly FII Inflow (\$ mn)	(250.70)	1,021.75		
Cumulative DII Inflow - YTD (Rs.cr)	16,506.60	13,695.87		
Cumulative FII Inflow - YTD (\$ mn)	(390.13)	631.62		
Food Inflation (%)	9.13	7.78		

The greatest mistake you can make in life is to be continually fearing that you will make one.
- Elbert Hubbard

Research Analyst: K. Sanjay Karanth | Email: research@sunshinefinancials.com | For archives: www.sunshinefinancials.com

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