NEWS

1. The US$ had a mixed response this week trading against its major international partners. It strengthened by 0.7% against the Swiss franc followed by 0.5% each against the Euro and the Danish kroner. It also rose by 0.3% against the British pound and by 0.2% against the Singapore $. However it weakened by 2.1% against the Canadian $ and by 0.4% against the Japanese Yen, ending the week stable against the Australian $.

2. Initial claims for unemployment benefits fell sharply by 8% to a seasonally adjusted seven-year low 297,000 in the week ended May 10. A longer-run view of claims that evens out weekly volatility (the four-week moving average) dropped slightly by 0.6%. Besides, the number of continuing unemployment benefits (those drawn by workers for more than a week) fell by a modest 0.3% to 2.67 mn in the preceding week. The unemployment rate for April dropped to 6.3%. Meanwhile, inflation is showing an early sign of picking up after years of dormancy. The consumer-price index rose a seasonally adjusted 0.3% in April from the prior month, driven by increasing costs for staples such as gasoline, food and shelter. It was the strongest monthly gain since last June. April consumer prices were up 2% from a year earlier, a marked pickup from October when annual inflation slipped to a four-year low of 1%. Excluding volatile food and energy, prices climbed 1.8% in April from a year earlier. That was the fastest annual increase since last August. The Fed's inflation target is based on a separate inflation gauge, the Commerce Department's personal consumption expenditures price index, which rose 1.1% in March from a year earlier. However, a broad gauge of U.S. industrial output fell at its fastest rate in nearly two years in April. Industrial production declined 0.6% in April from the prior month.

3. Economic activity in the 18-country euro-zone rose by just 0.8%, in annualized terms, during the first three months of 2014 compared with the previous quarter.

4. The Japanese economy expanded 1.5% in the first three months of 2014, the fastest since the third quarter of 2011, as consumer spending surged before April's sales tax increase. Private consumption which accounts for about 60% of the GDP, expanded 2.1% and contributed 1.8% to growth. Capital spending grew 4.9%, contributing 0.7% to the expansion, marking its biggest gain since the last quarter of 2011. External demand shaved off 0.3% from the growth as gains in exports (+6%) were not enough to offset a rise in imports (+6.3%).

5. On the domestic interbank market, the rupee-dollar exchange rate traded in a range of ₹58.63 – ₹60.05 per $, ending the week with a gain of 125 paise for the rupee at ₹58.79 per $. The forward premium levels across the maturities were in the range of 7.2% - 8.2% p.a.

VIEWS

1. On the domestic front, the decisive victory for Mr. Modi predictably led to some rupee appreciation. It would not be surprising to see greater dollar inflows from over-enthusiastic foreign institutional investors (FIIs). It will be interesting to see whether the Reserve Bank of India (RBI) succumbs to the pressure (economic as well as political) to allow rupee appreciation. The classic argument is that a strong rupee helps to keep inflation under control. Since a high interest rate regime is already making industry pay the price of RBI's view that inflation is the greater enemy than unemployment, one will have to wait and see if this is accentuated by the temptation to show the world how strong the country has become under a new leadership through a strong rupee.

2. The RBI Governor has already asserted at an international forum that monetary policy is within his purview, clearly hinting that the tight policy

will be in place until the inflation rate, as measured by the consumer price index (CPI) comes down to an acceptable level. Another important policy measure for the RBI is the exchange rate. If the same CPI-based parameter is to be used, the rupee's neutral value (as measured by the 36-country REER) would be Rs 63 per $. At the current level of Rs 58.79 per $, the rupee is overvalued by 6.7%.

3. On the international forex markets, Portugal, following on the heels of Ireland, exits the international bail-out package on 17th May. Post this exit, the country will lose the safety of the ECB's precautionary credit lines. Ironically, the week witnessed selloffs in bonds issued by Greece and Portugal as the euro came under bear pressure. The euro has declined by 1.3% over the fortnight, the most since the 2-week period ended Nov. 8 2013. It also dropped 0.8% to 139 yen and reached 138.78, a level not seen since mid-Feb. The euro's woes have been caused by increased market concern that the euro-zone economy is struggling to accelerate. Excluding Germany, which grew at an annualized 3.3% pace in the first quarter of 2014, economies in the rest of the bloc actually contracted a bit. Italian GDP fell by an annualized 0.5% last quarter, joining the Netherlands, Finland, Portugal, Greece, Estonia and Cyprus among those with falling output. Spain is the only major euro-zone economy besides Germany that is clearly growing. GDP rose by a 1.5% annualized rate last quarter, the third consecutive quarter of growth. But Spanish GDP remains far below its pre-crisis peak, and unemployment is still over 25%. Euro-zone GDP has risen only 1% since the first quarter of 2013, the lowest point of the bloc's six-year slump, and remains 2.5% below its peak in early 2008 with unemployment currently 11.8% of the workforce.

4. Meanwhile, considering that the dollar has now recovered ground from its lows, we are retaining our ranges for the non-$ currencies, as follows:

$ 1.62 – 1.72 per GBP,

$ 1.32 – 1.42 per EUR, and

JPY 95 – 105 per $.

DOMESTIC MARKETS

FOREIGN EXCHANGE MARKETS

SPOT EXCHANGE RATES

	₹/Currency
USD	58.79
PDS	98.83
EUR	80.51
YEN (100)	57.92
SFr	65.86
DKK	10.78
CAD	54.13
AUD	55.03
SGD	46.98
CNY	9.43

FORWARD EXCHANGE RATES

Month-end	₹/USD	Premium % p.a.
May-14	58.93	7.24
Jun-14	59.33	8.18
Jul-14	59.73	8.22
Aug-14	60.07	7.72
Sep-14	60.47	7.84
Oct-14	60.82	7.59
Nov-14	61.15	7.51
Dec-14	61.53	7.49
Jan-15	61.87	7.44
Feb-15	62.20	7.43
Mar-15	62.56	7.38
Apr-15	62.98	7.50

CURRENCY SWAPS

	2-Year	5-Year
₹/USD	7.87	7.97

INR/USD CURRENCY OPTIONS*

	1-mth Option on USD 1, price in paise	
Strike	Call	Put
58.00	140	22
58.50	104	35
59.00	74	55
59.50	50	80
60.00	32	113
60.50	20	150

	3-mth Option on USD 1, price in paise	
Strike	Call	Put
59.00	171	72
59.50	141	91
60.00	114	113
60.50	92	141
61.00	74	171
61.50	59	205

INTEREST RATE MARKETS

	2-Year	5-Year	10-Year
GOI BOND	8.47	8.77	8.86

INTEREST RATE SWAPS

	2-Year	5-Year
OIS	8.26	8.29
MIFOR	7.87	7.97

Information herein is believed to be reliable, but AVRCO does not warrant its completeness or accuracy

INTERNATIONAL MARKETS

FOREIGN EXCHANGE MARKETS

SPOT EXCHANGE RATES

	Against USD
PDS	1.6811
EUR	1.3694
YEN	101.50
SFr	0.8927
DKK	5.4512
CAD	1.0861
AUD	0.9360
SGD	1.2514
PKR	98.54
CNY	6.2334

PDS 3mnth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
1.66	3.31	1.32
1.68	2.19	2.19
1.70	1.34	3.35

EUR 3mnth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
1.35	3.00	1.08
1.37	1.90	1.90
1.39	1.05	3.13

YEN 3mnth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
103.48	2.43	0.89
101.48	1.55	1.55
99.48	0.64	2.85

INTEREST RATE MARKETS

	OFFSHORE CURRENCY			
	1 MONTH	3 MONTH	6 MONTH	12 MONTH
USD	0.15	0.23	0.33	0.54
EUR	0.23	0.29	0.37	0.53
PDS	0.49	0.53	0.63	0.92
YEN	0.10	0.14	0.18	0.33
SwFr	-0.01	0.01	0.06	0.19

	INTEREST RATE SWAPS		
	2-Year	5-Year	10-Year
USD	0.52	1.65	2.60
EUR	0.41	0.80	1.59
PDS	1.11	2.01	2.69
YEN	0.22	0.35	0.78
SwFr	0.09	0.35	1.08

OTHER MARKETS

COMMODITIES		EQUITY INDICES	
NYMEX crude ($/barrel)	102.0	DJIA	16,491
GOLD ($/ounce)	1,293	FTSE	6,855
COPPER ($/ton)	6,948	DAX	9,629
ALUMINIUM ($/ton)	1,731	NIKKEI	14,097

** indicative only* *# for payables*

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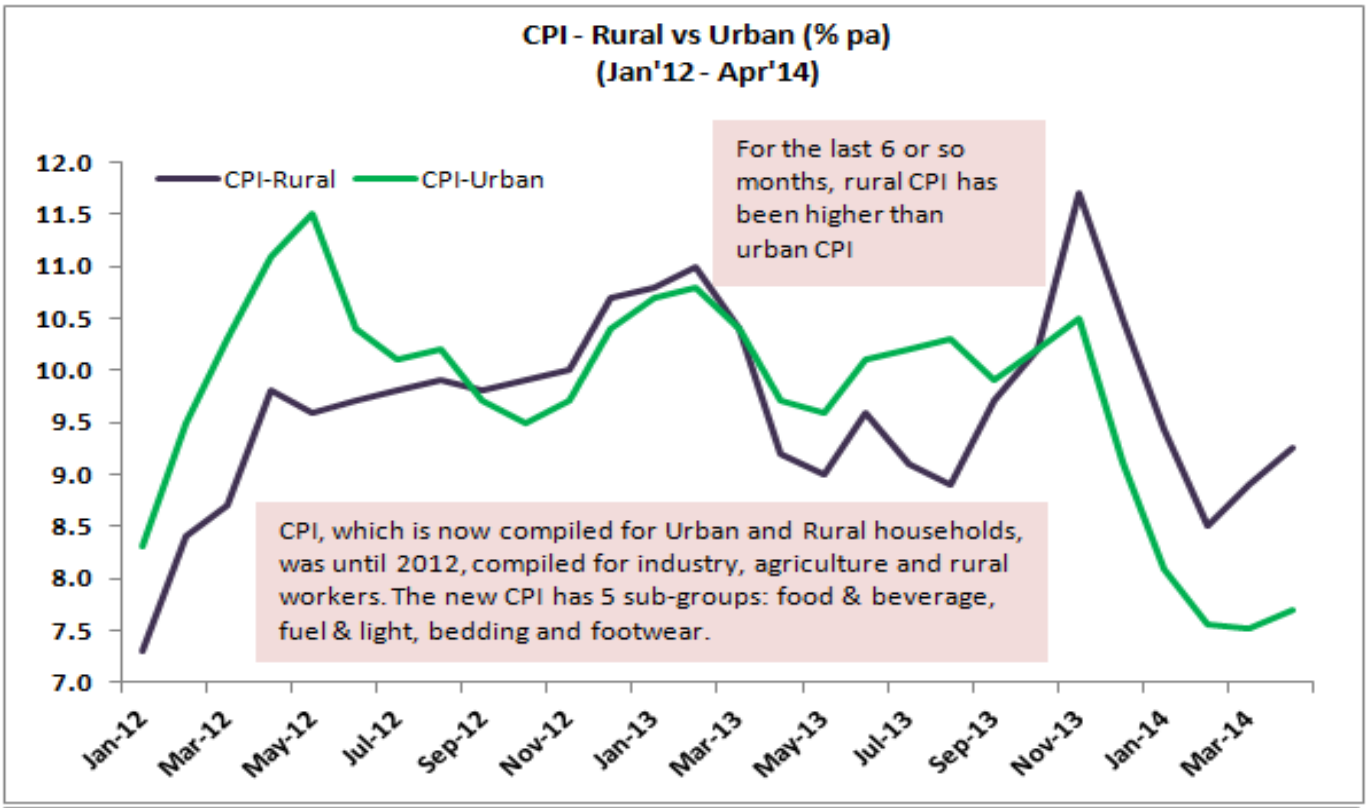
CPI - Rural vs Urban (% pa)
(Jan'12 - Apr'14)
CPI-Rural
CPI-Urban
For the last 6 or so months, rural CPI has been higher than urban CPI
CPI, which is now compiled for Urban and Rural households, was until 2012, compiled for industry, agriculture and rural workers. The new CPI has 5 sub-groups: food & beverage, fuel & light, bedding and footwear.
12.0
11.5
11.0
10.5
10.0
9.5
9.0
8.5
8.0
7.5
7.0
Jan-12
Mar-12
May-12
Jul-12
Sep-12
Nov-12
Jan-13
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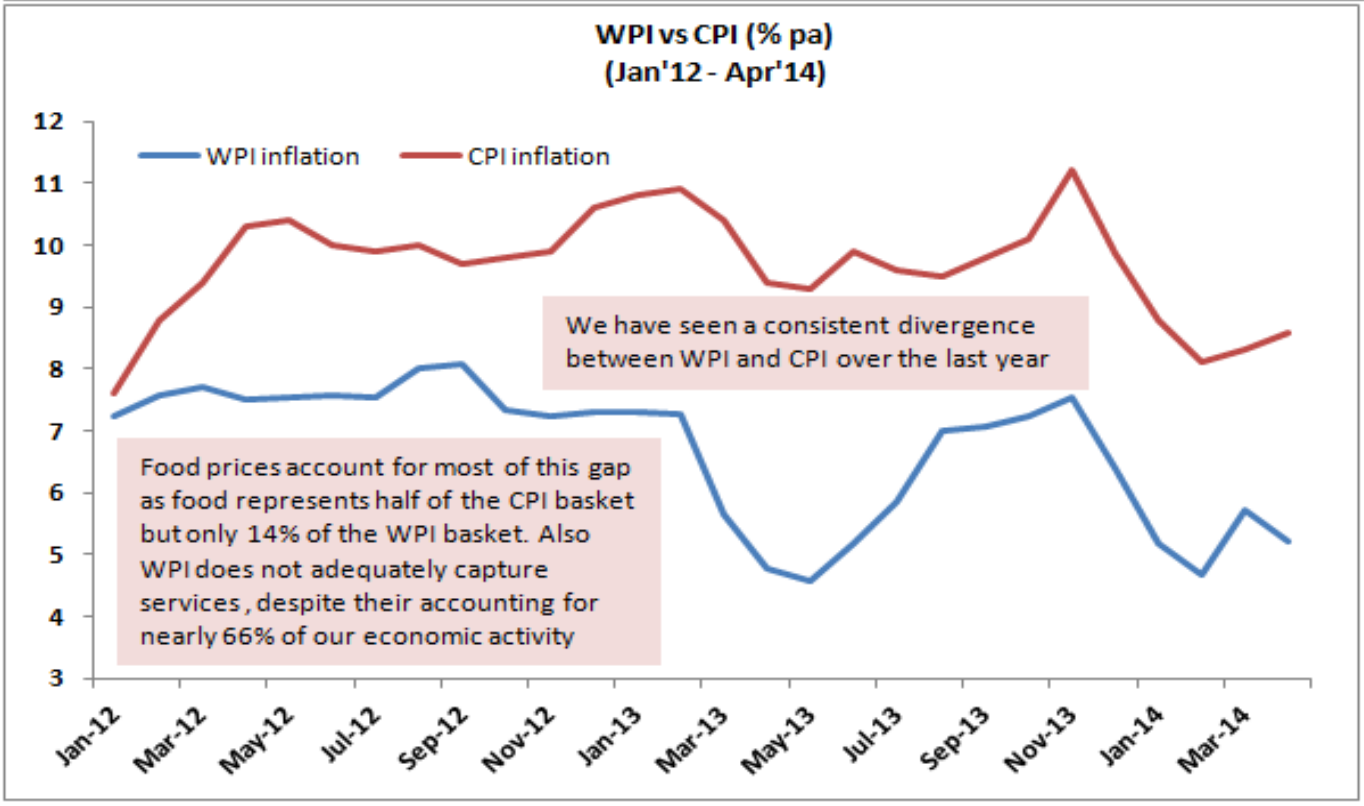
WPI vs CPI (% pa)
(Jan'12 - Apr'14)
WPI inflation
CPI inflation
We have seen a consistent divergence between WPI and CPI over the last year
Food prices account for most of this gap as food represents half of the CPI basket but only 14% of the WPI basket. Also WPI does not adequately capture services, despite their accounting for nearly 66% of our economic activity
12
11
10
9
8
7
6
5
4
3
Jan-12
Mar-12
May-12
Jul-12
Sep-12
Nov-12
Jan-13
Mar-13
May-13
Jul-13
Sep-13
Nov-13
Jan-14
Mar-14