

Equity Market	Return %
BSE Sensex	-5.04%
S&P Nifty	-5.73%
BSE MID CAP	-5.30%
BSE SMALL CAP	-7.30%
BSE100	-5.61%
BSE200	-5.53%
BSE Bankex	-12.53%
BSE IT	8.96%
Dow Jones	-1.42%
FTSE	-0.56%
HangSeng	-4.75%
KLSE	-0.29%
Kospi	1.45%
Nikkei	3.53%
MSCI Emerging Markets Index	1.55%
BSE Reality	-17.60%
Market Levels	as on 30th May 08
INR USD	42.16
Inflation	8.10%
Gold	886.5
Crude (Brent)	127.08
10 Year G Sec	8.108%
5 Year AAA	9.625%
5 Year G Sec	8.063%

Source: Bloomberg, MFI

The benchmark indices, Sensex and Nifty, remained range-bound with a negative bias during May 2008. The indices ended the month with negative returns of around 5% and 6% respectively.

Equity Market

Continuously rising crude prices, sustained high prices of other commodities and inflation near 8% levels were some of the main factors which impacted the markets in May 2008. Increased concerns about an economic slowdown in India (IIP growth) and less-than-optimistic US economic scenario also kept the markets subdued. On the other hand, mostly in-line quarterly results and upbeat global markets during the month provided some support to Indian stocks.

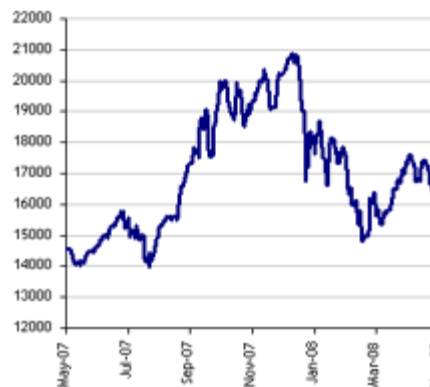
One of the major concerns for the global economy is high crude prices, which have touched a high of \$135/barrel. Crude prices have risen by 17% in the past month and by 39% in the current calendar year. Prices have more than doubled v/s May 2007. Several reasons like increasing demand, depreciating US dollar (v/s most currencies) and speculative activity are among reasons for the steep rise in crude prices.

OPEC has refused to increase supplies of crude as it sees speculation as the main reason for the rise in crude prices. As India imports more than 70% of its crude requirements, the impact of rising crude prices on the Indian economy is relatively higher. Moreover, the depreciation in the rupee v/s the US dollar is also pushing up the import bill. The crude import bill, which touched \$77 bn in FY08, is expected to cross the \$100 bn mark in the current fiscal, according to industry estimates.

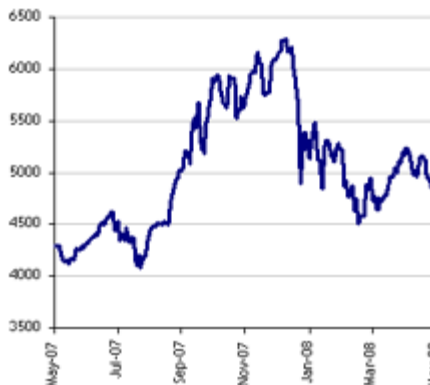
According to a study on the first 1429 companies' declared results (excluding banks and FIs), revenues grew about 22.7% YoY and PAT rose about 20%. However, operating margins were lower mainly because of the rise in raw material prices.

According to the quick estimates of the Central Statistical Organization (CSO), the Index of Industrial Production (IIP) rose 3.0% in March 2008, as compared to 14.8% in the same month last year. The headline number was subdued on the back of slower growth of 2.9% in the manufacturing sector as against 16.0% in the corresponding period of

Sensex Movement (May 07 - May 08)



Nifty Movement (May 07 - May 08)



BSE Mid Cap Movement (May 07 - May 08)



BSE Small Cap Movement (May 07 - May 08)



Fixed Income Markets

The Headline WPI inflation number for the week ended 17th May 2008 came at a three and a half year high at 8.1%.

WPI inflation for the week ended 22nd March was revised upwards from 7.00% to 7.85%. The point to note is that the extent of the revision was much lower compared to that of 15th March which saw a massive revision from 6.68% to 8.02% in that week. This indicates that the revisions in the coming weeks are probably likely to be more tempered and therefore would not lead to a significant jump in the advanced estimates number released in the previous weeks.

The situation with respect to Headline WPI inflation continues to look grim and is expected to inch up higher in the coming weeks, more definitely so as the domestic fuel price hike now looks inevitable. Official statements from the Government and the Planning Commission of India indicate that the current high inflation levels could sustain for the next 3-4 months before easing. Headline WPI inflation could rise further and peak at around 9.5% somewhere near end-November 2008 before coming down to end the calendar year at around 6.0%.

Going forward, there could be more fiscal measures to moderate the inflationary pressures. However, the official voices are asking all to be patient on the inflationary scenario, which could indicate some amount of helplessness on the part of the fiscal to absorb higher hits on account of fiscal adjustments. Already, we estimate that the hit to the fiscal out of the various rounds of adjustments to soothe inflation could be in the region of Rs. 6,500 crore to Rs. 7,500 crore.

The fourth quarter GDP number for FY08 came stronger than expected at 8.8% - thus pulling up the full year GDP growth to 9% - higher than CSO's advanced estimate of 8.7%. We admit that a higher than expected growth number will give the RBI some added comfort and flexibility to maintain a tight monetary policy in order to fight inflation. However, we continue to maintain that while the RBI will remain watchful of the inflation trends, it is unlikely to raise policy interest rates anytime soon as there are some genuine concerns on the growth front which are unlikely to manifest itself more clearly in FY09. We believe that any further monetary tightening – if warranted – will come either in the form of further CRR hikes or MSS issuances which are relatively easier to reverse in case of a larger than expected growth slowdown as compared to a policy rate hike.

Overall, most of the factors currently are seen to be negative for the bond market. RBI is expected to keep a tight leash on rupee liquidity as inflation fears gather momentum. High international crude oil prices will do little to bring down these fears in the immediate horizon. In the immediate future, it could be difficult to expect the 10-year benchmark to come down below the 7.95% levels and the broad trading range should be at around 7.95-8.10%.

10 Yr GOI Yield (May 07 - May 08)



Gold Prices (May 07 - May 08)



Inflation (May 07 - May 08)



Oil (May 07 - May 08)





Forex Markets

After registering a significant 10% appreciation v/s the US dollar in FY08, the rupee has depreciated by about 6.7% over the past three months to Rs. 42.67/US dollar. In May 2008 itself, it depreciated by about 5%. The main reasons for this are the significant increase in crude prices and reduction in capital inflows into India.

Although the recent easing on the ECB curbs will probably lend some appreciation support to the Rupee, we do not expect the Rupee to appreciate sharply anytime soon as the concerns related to the global financial markets are unlikely to abate anytime soon. On the contrary, the Rupee might face a depreciation pressure once again in the near term if the global crude oil prices start to climb higher from the recent levels of US\$127/bbl.

We expect the USD/INR to hover in the range of around 41.50-43.00 in the short-to-medium term.