RBI’s THIRD QUARTER REVIEW OF MONETARY POLICY 2010-11:

RBI’s considerations for policy announcements:

- Need to persist with measures to contain inflation and anchor inflationary expectations since inflationary pressures have re-merged significantly.
- A heightened upside risk to domestic inflation due to a sharp rise in global commodity price.
- India’s growth having moved close to its pre crisis growth trajectory as reflected in the 8.9% GDP growth in FH 2010-11 even in the face of an uncertain global environment.
- The global economic situation particularly in the US has improved. The Euro zone still faces uncertainty but there is an overall improvement in global growth prospects.

RBI’s expectations from the policy actions announced in this review:

- Contain the spill-over from rise in food and fuel prices to generalized inflation.
- Rein in rising inflationary expectations, which may have aggravated by the structural and transitory nature of food price increases.
- Be moderate enough to not disrupt growth.
- Continue to provide comfort to banks in their liquidity management operations.

Projections:

- The baseline projection of real GDP growth is retained at 8.5% with an upward bias.
- The baseline projection of WPI inflation for March 2011 is revised upwards to 7.00 % from 5.5%.
- The overall CAD for 2010-11 is expected to be about 3.5% of GDP.

Monetary Measures announced:

- Bank Rate remains unchanged at 6.00%.
- Repo rate increased by 25 bps to 6.50% with immediate effect.
- Reverse Repo rate increased by 25 bps to 5.50% with immediate effect.
- Cash Reserve Ratio of scheduled banks remains unchanged at 6.00% of their NDTL.

Liquidity Management Measures: Extension of following liquidity measures

- The additional liquidity support to scheduled commercial banks under the LAF to the extent of up to one per cent of their net demand and time liabilities (NDTL), currently set to expire on January 28, 2011, is now extended up to April 8, 2011. For any shortfall in maintenance of the SLR arising out of availability of this facility, banks may seek waiver of penal interest purely as an ad hoc measure.
- The second LAF (SLAF) will be conducted on a daily basis up to April 8, 2011.
ICICI Prudential Mutual Fund House Views

The RBI's rate hike through the policy announcements have been in line with our expectations. What is interesting is RBI's revision in its baseline inflation projection of WPI inflation for March 2011 from 5.5% to 7%. We believe that the projection numbers are now more realistic.

The other interesting thing in the policy is that RBI is going to start using moral suasion with banks to control credit. This is the first time that RBI has mentioned in its policy note that it will use moral suasion by checking which banks are lending, if borrowing is skewed in any particular direction and questioning banks on where they are lending.

We were expecting that RBI might raise reserve requirements for asset purchases as done in past instances when the inflation was high. This time however, RBI has not resorted to such measures and rather used a wide ranging comment on use of moral suasion to curb lending by banks. RBI has made it clear that it is not very happy with the loan growth outstripping deposit growth this year. This is partly because the Banks have been slow in raising deposit rates and now that deposit rates have become rational, deposit growth rate is still low.

RBI has also indicated that government has to also play its part in controlling inflation. We do believe that this comment from RBI is not in isolation and possibly is a result of discussions with the Finance Ministry. The Hon'ble Finance Minister in the past has mentioned a 4.8% deficit and this comment will build up to that expectation.

Inflation is getting stickier due to supply side issues. If supply is slow in catching up there will need some moderation in demand. RBI has first time raised concerns on high current account deficit (CAD) and is worried about a sustained CAD remaining.

RBI has raised issues in light of global market outlook improving which include issues like capital flows, while emerging market can face both inflationary pressures and capital flows. The other issue highlighted is moderation in domestic growth in the next financial year. While inflation remains the predominant current issue, somewhere on the back of its mind it continues to see growth as a major issue.

The March Policy announcements will be critical since it is a post budget policy announcement and also the last policy before the state elections in next financial year.

We believe that the yield curve upto one year is at a high level. There could still be some potential upside due to demand supply mismatch in the last quarter. The liquidity is slightly better than what was seen in December as is likely to improve at the end of current quarter as the government spending catches up. We believe that the growth in currency circulation could be low in next two to three months than it has been so far.

Unless there is dramatic rise in commodity prices one can see inflation stabilizing. RBI is going to balance both inflation and growth. Government's fiscal deficit, borrowing program and inflation are going to be critical for the fixed income markets.

- We recommend investors with ability to lock away money to invest atleast 30-50% of their fixed income allocation in One year and One Year Plus FMPs.
- The balanced 30 to 50% should ideally be locked away in mid market funds like ICICI Prudential Short Term Plan, ICICI Prudential Long Term Plan and ICICI Prudential Regular Savings Fund.

From Equity point of view, we believe that the policy announcements were in line with the market expectations. The direction of 10 year benchmark yields and 1 year CD rates can potentially impact equity markets as well. The positives of corporate earnings and growth outlook may
balance out the high inflation and rising commodity prices. With global growth prospects, especially for US having improved in recent weeks, there could be capital flowing back to the developed world in the short run. Our extremely bullish view on Long term India growth story remains intact. We believe that markets are expected to continue to remain volatile. Hence, we believe that investors need to provide for greater volatility in their equity strategy. We consequently recommend ICICI Prudential Dynamic Plan for lumpsum investments and SIP in ICICI Prudential Focused Bluechip Equity Fund, ICICI Prudential Discovery Fund and ICICI Prudential Infrastructure Fund for effectively managing volatility and better risk adjusted returns.

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ICICI Prudential Short Term Plan [IPSTP]* (An open-ended Income Fund. It is an additional Plan under the existing ICICI Prudential Income Plan with characteristics similar to ICICI Prudential Income Plan. The objective of the Plan is to generate income through investments in a range of debt and money market instruments of various maturities with a view to maximising income while maintaining the optimum balance of yield, safety and liquidity. Exit Load: If the amount sought to be redeemed or switched out, is invested for a period of – (a) upto six months from the date of allotment - 0.50% of the applicable NAV (b) more than six months from the date of allotment – Nil; ICICI Prudential Long Term Plan [IPLTP]* (An open-ended Income Fund. Objective is to generate income through investments in a range of debt and money market instruments of various maturities with a view to maximising income while maintaining the optimum balance of yield, safety and liquidity. Exit Load: If the amount sought to be redeemed or switched out, is invested for a period of - (a) upto 1 year from the date of allotment- 0.75 % of applicable NAV; (b) more than 1 year from the date of allotment- Nil;

ICICI Prudential Regular Savings Fund (IPRSF)* is an open-ended income fund that intends to provide reasonable returns, by maintaining an optimum balance of safety, liquidity and yield, through investments in a basket of debt and money market instruments with a view to delivering consistent performance. However, there can be no assurance that the investment objective of the Scheme will be realized. Exit Load: (i) If the amount sought to be redeemed or switched out, is invested upto 1 year from the date of allotment - 2% of the applicable NAV; (ii) If the amount,
sought to be redeemed or switched out, is invested for a period of more than 1 year from the date of allotment – Nil.

ICICI Prudential Dynamic Plan (IPDP)@ an open-ended Equity Fund. The objective is to seek to generate capital appreciation by actively investing in equity and equity related securities and for defensive consideration in debt / money market instruments. Exit Load: ##.

ICICI Prudential Focused Bluechip Equity Fund (IPFBEF)@ (An open-ended equity scheme) that seeks to generate long-term capital appreciation and income distribution to unit holders from a portfolio that is invested in equity and equity related securities of about 20 companies belonging to the large cap domain and the balance in debt securities and money market instruments. The Fund Manager will always select stocks for investment from among Top 200 stocks in terms of market capitalization on the National Stock Exchange of India Ltd. If the total assets under management under this scheme goes above Rs. 1000 crores the Fund Manager reserves the right to increase the number of companies to more than 20. Investment in the scheme may have concentration risk as the scheme invests in about 20 stocks. Exit Load: ##.

ICICI Prudential Infrastructure Fund (IPIF)@ is an Open-ended equity Scheme that seeks to generate capital appreciation and income distribution to unit holders by investing predominantly in equity/equity related securities of the companies belonging to the infrastructure industries and balance in debt securities and money market instruments. Exit Load: ##.

ICICI Prudential Discovery Fund@ (IPDP) (An open-ended Equity Fund). Objective is to generate returns through a combination of dividend income and capital appreciation by investing primarily in a well-diversified portfolio of value stocks). Exit Load: ##

##Exit Load: (i) If the amount, sought to be redeemed or switched out is invested for a period of upto one year from the date of allotment - 1% of applicable Net Asset Value; (ii) If the amount, sought to be redeemed or switched out is invested for a period of more than one year from the date of allotment - Nil. Entry Load Not Applicable under all the above mentioned schemes.

@ Investments in the scheme may be affected by trading volumes, settlement periods, volatility, price fluctuations, liquidity risks, derivative risk, market risk, risk relating to fluctuations in foreign exchange for investments in foreign securities, lending & borrowing risks, credit & interest rate risks relating to debt investment.

*Investments in the Scheme may be affected by risks relating to trading volumes, settlement periods, interest rate, liquidity or marketability, credit, reinvestment, regulatory, investment in unlisted securities, default risk including the possible loss of principal, derivatives, investment in securitised instruments and risk of Co-mingling etc.

IPSTP, IPLTP, IPRSF, IPDP, IPFBEF, IPIF and IPDP are only the name of the schemes and do not in any manner indicate either the quality of the Scheme or their future prospects and returns. Please read the Statement of Additional Information and Scheme Information Document carefully before investing.