Rupee seen range-bound, widening CAD a risk

MANOJIT SAHA & BHASKAR DUTTA
Mumbai, 1 January

The Indian rupee is expected to trade between 80 and 84 against dollar in the first three months of 2023 with support from overseas inflows though worsening current account deficit (CAD) and reduced interest rate differential between the US and India pose challenges.

According to a *Business Standard* Poll of 10 participants, most said the rupee could gain strength in January due to foreign inflows, and the Reserve Bank of India (RBI) is not expected to allow the currency to depreciate ahead of the Union Budget scheduled on February 1.

The rupee depreciated 10.15 per cent in 2022, its worst performance since 2013 as the war in Europe and the interest rate increase by the US Federal Reserve prompted investors to flee emerging markets. The Indian unit closed 2022 at 82.74 a dollar.

"Things would slightly improve for the better — the rupee has depreciated quite a lot in the last couple of months," said Abhishek Goenka, founder and CEO, IFA Global.

"Possibly in the New Year, we could see some flows coming in. I'm not seeing the market breaking 83/$ very actively. Even if it goes up, it will not stay. The Budget is also nearing. Before the Budget, I don't think they (RBI and the government) would like the rupee to make too much noise," Goenka said.

"2022 the year of high inflation, higher interest rates, slow growth and flight of capital to USD leading to stronger USD, weaker emerging markets and thereby rupee," said Amit Pabari, managing director, CR Forex.

"However, entering into 2023, as the inflation across borders and domestically has shown sustained signs of cooling off, the central banks, especially Fed, is likely to pause after another two rate increases in 2023, given by the fears of excessive tightening and hard landing," Pabari said.

The support for the Indian unit could come from seasonal uptick in overseas flows in the January-March period. Support could come from the central bank also, which has been active against any sharp volatility in 2022.

BS POLL

	₹/$ by end January	₹/$ by end March
CR Forex	81.5	79-80
Finrex	82.5	81.5
Mecklai Financial	82	81.0
IDFC First Bank	81-83.5	81-83.5
Quant Eco Research	NA	83.5
HDFC Bank	82-83	82.83.50
Barclays	NA	84
Shinhan Bank	81.60-83.50	80.80 – 82.00
IFA Global	82	81.5
India Ratings	82.5	82.20-82.50

Compiled by *BS* Research Bureau

"We expect USD/INR to remain range-bound till March 2023, trading between 81 to 83.50/$. Seasonal factors and market expectation of a dovish Fed will limit the upper end of the range till 83.50. RBI is likely to use periods of dollar weakness to build FX reserves which will limit USDINR from falling below 81 levels," said Gaura Sen Gupta, economist with IDFC First Bank.

The central bank used its foreign exchange reserves to support the rupee. In 2022, the country's exchange reserves depleted by around $70 billion.

One of th biggest challenges for the Indian currency is worsening CAD. The CAD shot up to an all-time high of $36.4 billion, about 4.4 per cent of the country's gross domestic product (GDP), in the quarter ended September 2022, owing to a widening of the merchandise trade gap.

The narrowing rate differential between India and US could also pressure the rupee as few participants expect the rupee to depreciate by March, and to hit 83.50-84.00/$ levels.

"We are seeing the rupee at 84/$1 by March-end because you will still have ongoing tightening in the US monetary policy cycle so the rate differentials are moving against India at the margin," said Rahul Bajoria, managing director and chief India economist, Barclays.

"At the same time, the balance of payment situation is improving but it's not improving very rapidly. We also reckon that the RBI would be looking to buy back some dollars to build up their reserves again, so general underperformance can be expected," Bajoria said. 2023 will not be as volatile as 2022 and that the worst for the rupee could be over, though there could be some spells of weakness — this was the overall mood of the foreign exchange market participants.