RBI's 2013 playbook to rebuild forex reserves unlikely to work: Analysts

Reuters
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The Reserve Bank of India's 2013 playbook to buffer the domestic currency against steep declines and rebuild foreign exchange reserves is unlikely to prove fruitful in the current crisis as economic fundamentals are vastly different, say analysts.

India's forex reserves have tumbled about \$110 billion from a peak of \$642 billion in September last year, and though that is largely due to the fall in the value of holdings in dollars and other currencies, another significant reason is the central bank's intervention in the currency market to protect the rupee.

The local unit fell about 11 per cent against the US dollar in 2013, a slide it has already matched so far this year, with most market participants expecting further declines by the end of 2022. To defend the rupee, the RBI has dipped into its forex reserves. It has sold a net \$43.15 billion worth of dollars since the start of 2022, including \$4.25 billion this August, the latest available data released on Monday showed.

"It would be important to rebuild FX reserves for sure. There will be urgency as fundamentals are also adverse," said Madan Sabnavis, chief economist at Bank of Baroda.

The RBI, in July, announced some measures to liberalise foreign exchange inflows, including giving foreign investors access to a larger portion of government debt and banks wider room to raise more deposits from non-residents. But these measures are unlikely to prove as effective right now as they had in 2013.

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UNPROFITABLE SPREADS

Back in 2013, the RBI had offered to swap the US dollars banks had raised via foreign currency non-resident (FCNR) deposits or foreign currency funding for rupees at concessional rates.

It swapped FCNR deposits, with a maturity of three years or more, at a fixed rate of 3.5 per cent per year, which was about 3 percentage points less than market rates at the time, while it swapped foreign currency funding at 1 percentage point below market rates.

These two swap windows had brought in around \$34 billion at a crucial time, with \$26 billion via the FCNR route alone. But these methods are unlikely to be as fruitful now.

"The FCNR deposits route might not be as effective this time around, including for reasons like a narrower US-IN rate spread and less aggressive rate hikes in this cycle versus back in 2013," said Radhika Rao, senior economist at DBS Bank.