RBI predominantly net buyer of US dollar over the past decade

ANJALI KUMARI
Mumbai, 20 December

Over the past decade, the Reserve Bank of India (RBI) has been predominantly a net buyer of US dollars in the spot market, except in the financial years 2018-19, and 2022-23 when it became a net seller. In the current financial year, the central bank has continued to be a net buyer and significantly contributed to the substantial growth of India's foreign exchange reserves, which have more than doubled compared to 2013, allowing India to shed the previously associated "fragile five" label.

NEWS ANALYSIS

The rupee has depreciated by 21 per cent since September 2013. In the current financial year, the central bank net bought $17.4 billion as of October.

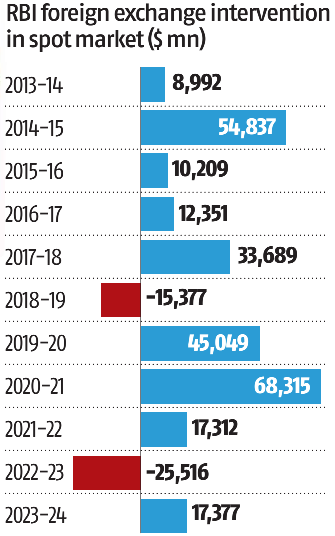
India's foreign exchange reserves were the fourth highest among major foreign exchange reserves-holding countries, having increased so far by $28.4 billion during 2023-24.

The RBI has strongly refuted the International Monetary Fund's (IMF's) report reclassifying India's exchange rate regime from a floating to a stabilised arrangement.

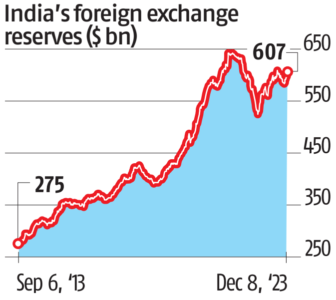
The central bank has asserted on several occasions that its interventions in the foreign exchange market are solely aimed at curbing volatility rather than manipulating the exchange rate.

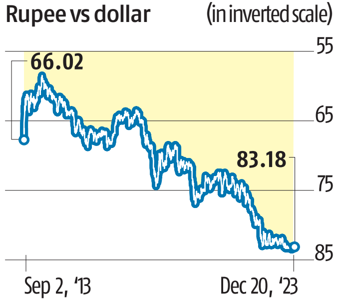
Notably, this stance comes after a challenging 2022, during which the Indian rupee experienced a 10 per cent depreciation against the US dollar. However, in 2023, the Indian currency has demonstrated remarkable stability. "The governor was very clear in this matter, and the stance hasn't changed. The Reserve Bank's stated position is that they do not target any particular level. They just act to reduce volatility on either side. All of this is just active management by the Reserve Bank. I do not see what prompted IMF to change its stance" said Vikas Goel, Managing Director and CEO at PNB Gilts Ltd. "The IMF is saying that the intervention is more than that, it's just a matter of degree. At different points in time, the Reserve Bank's definition of what is volatile changes. When there is a great degree of uncertainty globally, then they would prefer less volatility. On the other hand, if there is stability globally, then they might tolerate much higher volatility. Reserve Bank's routine foreign exchange rate management policy, it is flexible and it is not a static policy," he added.

BY THE NUMBERS



Note: +/–: Sold/purchased; 2023–24 data for April–October
Source: RBI





Source: Bloomberg
Compiled by BS Research Bureau

The IMF reclassified India's exchange rate regime, shifting it from "floating" to a "stabilized arrangement" for the period between December 2022 and October 2023.

This change is linked to perceived interventions by the RBI in the foreign exchange market, as the rupee exhibited a notably limited range against the US dollar. According to the IMF report, these interventions might have exceeded the required levels for addressing disorderly market conditions. Between December 2022 and October 2023, the rupee depreciated by 0.6 per cent.

"There are two perspectives to consider in this matter. From a domestic policy standpoint, maintaining a relatively stable currency range makes sense, especially when combating inflation. India, with substantial reserves, utilised them effectively to manage potential depreciation pressures. This approach prevented the need for higher interest rates or an elevated repo rate, as currency depreciation often correlates with inflationary impacts. Given the domestic conditions and the actions taken by the RBI, there seems to be a justified rationale without any basis for criticism," said Indranil pan, chief economist at YES Bank. "On the other hand, from the IMF's viewpoint, the expectation might lean towards a more freely fluctuating currency in various markets. A freely moving currency is often considered beneficial for trade relationships," he added.

The Rupee has displayed remarkable stability against the US dollar in the current calendar year, marking the least volatility witnessed in over two decades. The local currency experienced a marginal depreciation of 0.5 per cent against the greenback. In the current financial year, the rupee has depreciated by 1.2 per cent. Market participants attribute the stability to the RBI's timely intervention in the foreign exchange market both in terms of selling and buying dollars. Moreover, the domestic market witnessed robust foreign inflows which kept the rupee afloat during global uncertainties. The RBI remained active in the market to curb the volatility in the exchange rate. Market participants said that the intervention protected the local currency from weakening further to 84 per US dollar this year.