When the rupee gained currency

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The rupee displayed remarkable stability against the dollar this calendar year, marking the least volatility it witnessed in nearly three decades.

The currency experienced a marginal depreciation of 0.5 per cent against the greenback. The last time the Indian unit exhibited such stability was in 1994, when it appreciated by 0.4 per cent.

Market participants attribute the stability to the Reserve Bank of India's (RBI's) timely intervention in the foreign exchange market, both in 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 throughout the year to curb volatility in the exchange rate. Market players said the intervention protected the currency from weakening further to ₹84 this year. According to them, the rupee might regain its ground in 2024 against the greenback on the back of foreign inflows. It might appreciate to ₹82 during the year.

While most of the emerging-market currencies regained ground against the dollar in November, the rupee lagged its peers, primarily due to persistent demand for the dollar among importers. Last month, on November 10, it had hit a record of ₹83.48. The expected inflows resulting from India's inclusion in the JP Morgan bond index are seen starting from January.

While the central bank is poised to absorb a significant portion of these inflows, the overall impact is anticipated to be beneficial for the country's balance of payments, leading to a surplus, market participants said.

"Apart from the RBI's intervention, the other factor is that our current account deficit (CAD) has remained less than 2 per cent (of GDP) in FY24," said Gaura Sengupta, economist at IDFC First Bank. "We expect it to strengthen in the next year, and trade between ₹82 and ₹80," she added, "as we expect the flows to come in because of India's inclusion in the JP Morgan bond index. The interest rate differential is expected to widen. The RBI rate cut cycle is expected to follow the Fed (Federal Reserve) with a delay, and is expected to be shallower".

JP Morgan had announced the inclusion of India in its widely followed emerging market bond index on September 22. India will be included in its flagship index, GBI-EM Global Diversified index, a process that will start in June next year. The inclusion will be phased over a 10-month period, with a 1 per cent weighting included in each month, till March 31, 2025. Indian bonds will have a 10 per cent weighting, like China.

Inflows of $25-30 billion are expected due to the bond index inclusion, market participants said. The Fed hinted at three potential interest rate cuts in 2024 in the last meeting. Back home, the monetary policy review on the whole was interpreted by the market as dovish as compared to the previous two policies. The domestic rate-setting panel decided to keep the policy repo rate unchanged at 6.5 per cent for the fifth straight review meeting and the "withdrawal of accommodation" stance while stopping short of clearly communicating that the rate cycle had peaked. The market expects the current quarter may mark the bottom of the economic cycle. From the next quarter onwards, there is an optimistic forecast for an uptick in economic activities. Another reason for this optimistic outlook is the expected actions of central banks. The RBI is expected to initiate rate cuts, following a three-month lag, after the projected rate cut from the Fed in May. "The rupee remains underpinned by the retreat in US treasury yields and falling oil prices. The resumption of foreign portfolio investment (FPI) inflows can also help the sentiment," said Hitesh Jain, strategist, institutional equities research, YES Securities India.

"The RBI governor," he added, "has opined that the Indian rupee has witnessed low volatility and orderly movements when compared with other emerging market currencies."

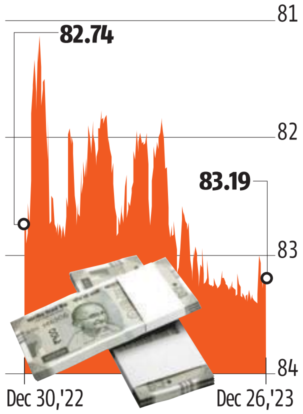
"India's CAD/GDP for FY24 is seen at 1.7 per cent, which is much better than the FY23 number. On economic growth, FY24 GDP growth is upwardly revised to 7 per cent, quite an enviable number when compared with the global backdrop." The Indian unit was stable in the first half of 2023 after a turbulent 2022 following the war in Europe and interest-rate hikes by the Fed. It appreciated by 0.16 per cent in the first six months of the current calendar year on the back of robust foreign inflows.

"The rupee has outperformed other emerging market currencies primarily because the RBI has kept it in a tight band," the treasury head at a private bank said. "And in the past few months we have seen a reversal of fortune in terms of FPI inflows." The weakening of the yuan was the primary reason for the weakening of the rupee in August, prompted by the reduction of the interest rate differential between the yuan and the dollar.

Geopolitical tensions in West Asia and rising crude oil prices led to foreign outflows, which further weighed on the currency starting October.

This financial year, the rupee has depreciated by 1.2 per cent so far.

RUPEE SPOT (in inverted scale)



ASIAN CURRENCIES AGAINST $

	Dec 26, 2023	% change (YTD)
Japanese Yen	142.3	-7.9
Malaysian Ringgit	4.6	-5.1
Chinese Renminbi	7.1	-3.4
South Korean Won	1,294.2	-2.6
Taiwanese Dollar	31.0	-0.8
Indian Rupee	83.2	-0.5
Hong Kong Dollar	7.8	-0.1
Thai Baht	34.6	0.1
Indonesian Rupiah	15,484.0	0.6
Singapore Dollar	1.3	1.2

Source: Bloomberg