Indian Rupee: Worst to best within a year

Indian rupee registered its biggest quarterly gain since the September quarter of 2012 as heavy foreign buying of equities and debt boosted the local unit and the rupee breached the 60-per-dollar mark for the first time in eight months. The rupee has gained more than 12% from its all-time low of 68.93 hit in August 2013 and has become one of the best-performing currencies among emerging markets from being the worst in 2013. The rupee rose 3.15 percent in the March quarter, its best quarter since the 4.96 percent rise in the September quarter of 2012. The currency appreciation which began after RBI governor Raghuram Rajan put in place several rescue measures, is gathering further momentum with opinion polls putting Modi, the BJP's prime ministerial candidate, leading the race to head the government after the April-May polls. Here are some macro changes on the domestic front which have attributed to rupee strength as well:

- Foreign funds have purchased a net $3.7 billion in equities from the start of 2014 until March 27 while in debt the net inflows stand at $5.8 billion.
- India's foreign exchange (forex) reserves have risen by $1.83 billion to $297.28 billion for the week ended 14th March-14. This is the third consecutive week of increase in the country's forex reserves as overseas investors poured in money in local bonds and stock markets.
- India's trade deficit narrowed in February on sharp fall in imports as the trade deficit stood at $8.13 billion, more than 40 percent lower from a year ago.
- India's wholesale price-based inflation eased to a nine-month low in February and has been already subsided to around 5%.
- India's annual consumer price inflation eased more than expected to a 25-month low of 8.1 per cent in February, helped by moderating food prices.
- As per the CSO estimates, the economy would expand 4.9 percent in the current fiscal ending March, up from 4.5 percent recorded in 2012-13.

And the story goes on..

- The uptick in IIP numbers for the month of January 2014 at 0.1% from -0.2% in December 2013 is encouraging after witnessing negative trend since October 2013 and has finally shown some signs of recovery.
- India’s current account deficit (CAD) has narrowed sharply to USD 4.2 billion (0.9 percent of GDP) in Q3 of 2013-14 from USD 31.9 billion (6.5 percent of GDP) in Q3 of 2012-13 primarily on account of a decline in the trade deficit as merchandise exports picked up and imports moderated, particularly gold imports. We expect full year CAD to fall below 2 percent.
- India's manufacturing sector expanded in February at the strongest pace in 12 months, driven largely by growth in new business orders and an improved macroeconomic situation.
- Government has revised the fiscal deficit target to 4.6 percent of GDP from an earlier estimate of 4.8 percent and from a figure of 4.9 per cent of GDP in the previous financial year.

Policy makers have battled with a difficult combination of high inflation, falling growth, political uncertainty and corruption issues. Stagnation in India's investment cycle was one of the core reasons for India’s underperformance in recent years but political certainty will be the key to kick starting it again.

If the elections go well and we have a strong party at the center then it will improve sentiment which will ultimately lead to pick up of the investment cycle. Investors are not worried about rupee fallout from the ongoing Fed tapering given that Fed Chair Janet Yellen has already suggested that a rate hike could come as early as spring 2015.

We expect the rupee to withstand this Fed tapering and the rise in interest rates in the US. India is in a position where we can say that, we are amongst the best the emerging markets, and this will continue to be so in future. Economy has stabilized which is evident from the strengthening of the stock markets as well as the rupee and we will also see improvement in growth numbers.

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Journey of Indian Rupee

3rd April, 2014

Rupee Outlook

The Indian rupee is poised to gain further on the back of strong foreign flows. Reserve Bank of India may have already started soaking up US dollars. There is speculation among traders that the central bank has likely bought nearly $2-$3 billion over last week in its attempt to slow the rupee's rally. Drop in the WPI along with the recent corrections in the CPI, CAD and the trade figures point towards a trend of stabilization in the domestic economy. The rupee is expected to extend its gains in the next three months as international investors pump in dollars to buy stocks and bonds in anticipation of a stable government after the elections, delivering an economic revival. The rupee, which has posted a dramatic turnaround from being the worst performer among emerging market currencies to the best in a matter of months, is poised to climb to as high as 58 against the dollar. However, if we get the right government, equity flows will be buoyant and the rupee may climb further and may touch even 57 in months to come.

Although there is optimism in the market, downside risks still exist and therefore, the RBI will be very cautious. If they see large flows ahead of elections, they would be ready to mop it up. One should keep a close watch on INR weakness which can happen if there is a pull-out of FII money and on the back of any election-related negative news. India is not completely out of the woods as far as global issues are concerned – if the US Federal Reserve were to increase the pace of tapering then pressure may once again mount on the rupee and the Reserve Bank cannot afford to overlook such issues. If there is an unstable government, there could be an approximately $5-billion withdrawal from the stock market and we may go back to 65-to-a-dollar level.

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