Key Takeaways - IIBF-FEDAI joint Webinar on "INR in 2022-2023" on 12th May 2022

CEO Biswaketan Das welcomed the Honorable Guest Speakers Mr. Madan Sabnavis, Chief Economist, BOB and Mr. Neeraj Gambhir, Head, Axis Bank. He also welcomed the Moderator of the webinar Mr. Ashwani Sindhwani, Head FEDAI and extended his heartfelt thanks to FEDAI with whose association, the webinar is being conducted.

CEO introduced the today's topic i.e. "INR in 2022-23" and the background behind choosing the same. He commented that the topic is contemporary to the present scenario as Rupee is reflection of the Indian economy as multiple factors like trade deficit, export-imports, inflation, interest rates are manifested in the same.

He requested the first guest speaker Mr. Madan Sabnavis to give his talk on the topic.

Key takeaways from Mr. Madan Sabnavis' speech

There are three/ four factors that drive the Indian currency in the FY:

1. Fundamentals

2. External factors that is happening in the global economy particularly, Dollar

3. RBI decisions w.r.t Rupee

4. Real effective exchange rate (REER)

Fundamentals- This refers more to the demand and supply of Dollar. We need to refer to the Balance of payments to understand the same which comprises current account and capital account. At the current account level, the more important factor is trade deficit which is difference of exports and imports. The exports are booming at present and it has grown by more than 20% by the end of April. However, when there is growth in the exports, the imports also tend to grow thereby pushing up the Dollar. The commodity prices have increased due to war and high difference of imports over exports has created high trade deficit globally thereby depreciating the Rupee. It is expected that the trade deficit will remain to high due to other factors like high inflation and RBI increasing the interest rates. Two elements that are expected to be positive are software receipts and remittances that may provide some cushioning effect. The global economy is expected to be slow due the war and also most of the global banks restricting the demand forces. We may the current account deficit reduce to 2.5-3% of GDP instead of surplus thereby creating pressure on the rupee.

The quantitative easing is being rolled back by Fed Reserve and FDI/ FPI are expected to be in the negative zone. The advantage of borrowings through ECBs may not really be there for the Indian corporates due to higher interest rates. Considering all the above factors in the fundamentals, Rupee is expected to further depreciate in the FY 2022-23.

External factors-The Dollar is growing as the US economy is strong and Fed Reserve is pulling back by increasing rates. The Dollar is expected to remain stronger throughout the year thereby, putting pressure on the Rupee including other currencies. If we compare our currency with 20 other Global Currencies, we are not doing that bad as we are the median level. If the Rupee is allowed to depreciate, it will boost the exports or, else we may lose the competitive edge in the global exports.

RBI Decisions-If the RBI supports the Rupee, it may regain its strength. The RBI position is that they are not looking at any particular value of the Rupee but they want less volatility. It is not clearly known how RBI is going to control the Rupee as their sudden decisions may tilt the Rupee position going forward.

Real Effective Exchange Rate (REER)- The real effective exchange rate (REER) is the weighted average of a country's currency in relation to an index or basket of other major currencies. The weights are determined by comparing the relative trade balance of a country's currency against that of each country in the index. The Rupee is quite fairly valued presently and REER is moving in the similar direction. In case the US inflation rate of around 8% remains more than Indian inflation rate of around 7%, the REER will remain in the right direction.

Considering all the above four factors, it will be pretty difficult to predict the correct Rupee position in the current Fiscal. If the current situation continues, it can be expected that the Rupee will remain around 78-79 which is driven by adaptive expectation.

After his talk, Mr. Neerraj Gambhir was requested to give his talk.

Key takeaways from Mr. Neeraj Gambhir's speech

He started with an apt quote stating "The chapter on the fall of Rupee you may omit. It is somewhat too sensational"—Oscar Wilde said in1895. While the fall of rupee may have seen sensational in 1895, he would like to argue that it is not the same in 2022.

1. While there has some volatility in the Rupee, it is somewhat well contained and Rupee has been pretty well performing currency. In the last month, Rupee has depreciated around 2% and around 3.5- 3.7% in the last six months. If we compare our figures with J P Morgan Asian currency market average, the rupee depreciation is less than the other Asian currencies. In comparison, other major currencies like Chinese Yuan has depreciated 5% in the last 1 month and Brazilian Real has depreciated 9%. The implied volatility in the Options market is around 7% whereas other currencies have higher implied volatility compared to Rupee. We have an advantage here as ours is a managed currency by the Central Bank which can manage the position in both ways.

2. On the fundamental front, it is pointing towards a depreciation. Higher crude imports, electronic imports will lead to higher current account deficit of around 3.5% of GDP. Historically, our current account deficit has been less than 2% but this year it is expected to be more than 3% which is reflecting the Rupee value. Due to tightening of the US economy, there has been substantially high portfolio outflows of around USD 2 billion. In spite of huge outflow, the effect has not been massive as RBI has used the huge forex reserves to give a cushioning effect.

3. FDI continues to be strong. However, less FDI expected this year compared to last year. Government measure like production linked incentives will support the FDI to remain robust. Overall the balance of payments will be net negative, rough estimate being 25 billion USD.

4. The decisions of the global central banks will depend upon what decisions are taken by Fed Reserve. The current US inflation rate is 6-8% and will continue to remain the same. Whenever the US economy tightens, there is always a reverse flow of Dollar from emerging economies.

5. It has been observed that there has been reluctance from the exporting community to participate in the market in a meaningful way. Since the Rupee is expected to depreciate further, they have held back their hedging and probably waiting for the opportune moment. On the contrary, importers have taken more hedging positions thereby weakening the Rupee.

Considering all the above factors, Mr. Gambhir ended his speech stating that Rupee is not expected to depreciate further. Quarter 3 &4 tends to be always better for the Rupee due to positive fund flows.

After both the speakers ended their speech, **Mr. Ashwani Sindhwani** was requested to start the moderation of the panel discussion on the Topic.

He welcomed both the guests and started the panel discussion.

Q1. Is the country heading towards a twin deficit?

M Sabnavis: There is no major fundamental weakness as such and the economy is expected to do well with higher growth trajectory. Even though there may be twin deficit, it will not have a major impact on the economy.

Q2. Considering the tightening of the US economy, what is the prospects of FDI

N Gambhir: US bonds market have reacted sharply to the readjustment of US interest rates. RBI has also raised the interest rates to contain the inflation which will send a positive signal to global investors.

Q3. What is the view regarding management of currency volatility is concerned?

N Gambhir: Market participants allowed to participate in the NDF market has supported to contain the interest volatility.

Q4. What is the level rupee will go?

N Gambhir: Depends on the forward curve and would not like to predict the approximate position

Q5. How will the value go back to 76 and what are the possibilities?

M Sabnavis: There is a possibility if the fundamentals can change, war coming to an end, commodity prices coming down and current account deficit softening.

After this, a few questions raised by the meeting participants were addressed satisfactorily.

The meeting came to an end with a vote of thanks to the panel by Dr. R Muralidaran, Director-Academics.