बैंक ऑफ़ बड़ौदा
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Currency update

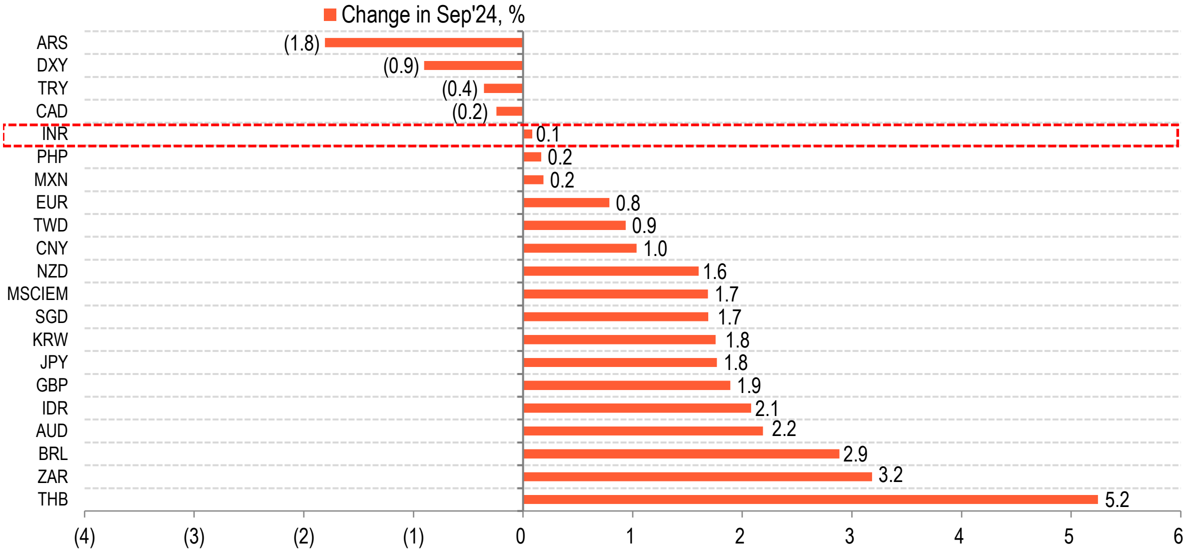
INR appreciated by 0.1% in Sep'24 against a depreciation of -0.2% seen in Aug'24. This was supported by a weaker dollar. Apart from this, increased quantum of FPI flows (record high equity inflows), range bound commodity prices and the narrative of easier liquidity conditions amidst global monetary policy easing, have lent comfort. However, in terms of gains observed in major EM peers, INR was largely capped. This may be attributable to quarter end phenomenon and higher dollar demand from importers and banks. In the near term, macro conditions remain favourable forINR. DXY is expected to trade with a downward bias as disinflation is underway in the region and consumption demand is softening. FPI flows will further gain strength as index inclusion becomes broad based with increased weightage which in turn will attract security specific flows. On external front, enough cushioning in terms of adequate forex reserves along with timely intervention of RBI will ensure volatility of rupee to be largely contained. We expect INR to trade in the range of 83.7-83.8/USD in Oct'24, with an appreciating bias.

Movement in global currencies in Sep'24

In Sep'24, major global currencies appreciated against the dollar. This comes in the wake of a weaker dollar. Dollar rhetoric was supported by a weaker private consumption demand in the US (Q2, 3rd estimate), slowly converging to its trend. This coupled with disinflation in core PCE and falling wages, signalled that more softening on labour market is imminent. This was addressed in the latest Fed policy where a sizable cut was delivered of 50bps. Thus, DXY fell by 0.9%. Asian currencies remained bullish triggered by risk on sentiment. However, Asian central banks have hinted that whether it would be ahead or behind the monetary policy curve is more contingent on domestic growth-inflation play off. JPY continued to gain from expectation of policy normalisation, major macros such as stickier CPI data and moderation in jobless rate and improved retail sales numbers, all reflect the same. However, coming days remain crucial with the election of new Liberal Democratic Party leader. Some policy discontinuity may be seen. EUR USD pair got comfort albeit ECB delivering a rate cut of 25bps, second in its current cycle. ECB Chief's reiteration that inflation is comfortably nearing its targeted level may tune market to remain less bullish on currency, going ahead. The latest Germany's inflation print also confirms the same. EUR USD pair also got support from stimulus in China which is a major trading partner. GBP USD pair got support from a weaker dollar; future correction may be witnessed as recovery in private consumption demand is underway. BoE officials have been vocal about a staggered response amidst fear of renewed concerns of inflation. CNY got support especially in the last week of Sep coinciding with the announcement of fiscal and monetary stimulus. From cut in 7-day reverse repurchase rate, liquidity injection, propping up credit demand to targeted sector specific measures; broad based impetus helped in uplifting market fundamentals, supporting its currency.

Going forward, DXY is expected to trade with a downward bias. However, some decline in the index will be capped. The current week holds crucial as major jobs data is scheduled to be released. Fed Chair has already hinted at a neutral stance without rushing into policy response. Any deviation from the terminal rate of 4-4.25% for Fed fund rate this year as reflected in CME data, pose headwinds to major currency pairs.

Figure 1: Movement in global currencies in Sep'24



Source: Bloomberg, Bank of Baroda Research | Note: Data as of 30 Sep 2024 | Figures in brackets indicate depreciation against the dollar

<u>Performance of rupee</u>

In contrast to most global currencies, gain in INR USD pair was limited. It underperformed MSCI EM, rising by 0.1% in Sep'24 hovering on an average at 83.82/$, shying off its lifetime low of 83.98/$. MSCI EM index, on the other hand rose by 1.7%, due to dip in DXY index. Amongst major EM peers, rupee's underperformance is only next to Argentine Peso (-1.8%) and Turkish Lira (-0.4%). Albeit robust macro fundamentals, favourable commodity prices and recent moderation in inflation, what has arrested rupee's gain? In fact, for the month of Sep, even FPI flows have been buoyant. Equity flows at US$ 6.9bn, have been the highest recorded in CY24 so far. Debt flows (general limit+VRR+FAR) amounted to US$ 3.9bn. A possible explanation could be a quarter end seasonal phenomenon and higher dollar demand from importers and banks.

<u>Outlook</u>

Going forward, the narrative for rupee remains favourable. Export cycle seems favourable in an easier monetary condition, globally. Favourable domestic inflation, astute liquidity management strategy of RBI, will further lend support. RBI intervention will provide additional resistance. Record high forex reserves already enumerate enough cushion on external sector front. India's robust high frequency growth indicators along with prudent fiscal policy has already attracted stable foreign capital in terms of FDI. FPIs have also seen a sharp turnaround and the pace is likely to continue as global index weightage is gradually increasing. Another interesting thing is that the volatility of rupee is gradually diminishing, which holds positive. We expect rupee to remain rangebound at 83.7-83.8/USD in Oct'24.

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