

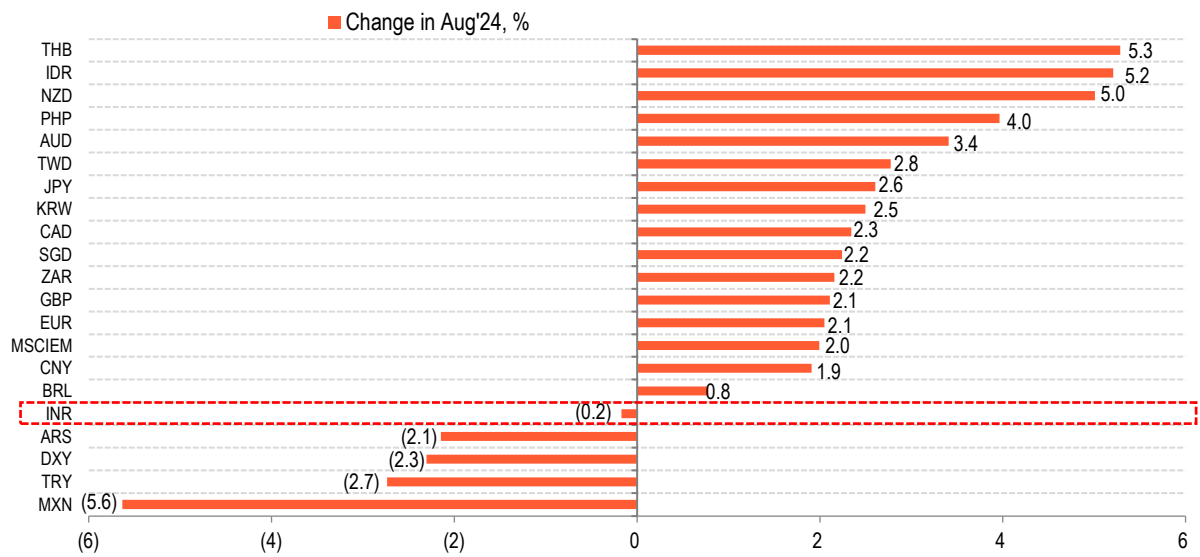
Currency update

INR depreciated by 0.2% in Aug'24 (-0.4% in Jul'24) to currently trade at 83.87/\$, close to its lifetime low of 83.97/\$. This was despite weakening US\$. The factors that impacted Rupee include: slowdown in FPI inflows (mainly equity segment), and increased dollar demand by importers. However, the decline was not as steep as it was in case of other currencies, mainly due to relatively steady FPI inflows in the debt segment and lower oil prices. As a result, INR traded in the range of 83.72-83.97/\$. In the next fortnight, we expect movement in INR to remain range bound. Domestic currency is expected to benefit from possibility of renewed FPI inflows in the equity segment (due to changes announced in the MSCI index) and moderation in oil prices. However, pressure may arise as DXY is beginning to regain ground as investors scale back their expectation of a large rate cut by Fed in Sep'24. Further, any escalation in geo-political tensions in the Middle East will also increase the demand for safe haven currencies, thus adversely impacting INR. We thus expect INR to trade in the range of 83.8-83.9/\$.

Movement in global currencies in Aug'24

In Aug'24, major global currencies appreciated against the dollar. The movement in global currencies was led by weakness in dollar. DXY index, measuring the dollar's value against a basket of currencies was 2.3% lower in Aug'24 (weakest since Nov'23), following the 1.7% decline in Jul'24. Much of the weakness was noted in the second fortnight of Aug'24 when it fell by 1.5%, compared with 1.1% decline noted in the first fortnight. However some revival in dollar demand has been visible towards the end of the month, as incoming macro data points towards a smaller rate cut by Fed in Sep'24. During the course of the month, Fed Chair in his statement at Jackson Hole Symposium confirmed that the time has come for Fed to lower rates. However the quantum of rate cuts this year remains a topic of debate. Most analyst are pricing in 100bps cut by the end of this year. This view has been supported by continued weakness in the manufacturing sector activity, 4th consecutive rise in unemployment rate in Jul'24, slowdown in home sales amidst low levels of new home supply and elevated prices. As risk sentiment improved, Asian currencies gained the most. Apart from them, JPY, EUR and GBP also made significant gains. GBP gained following the comments of Bank of England Governor Bailey at Jackson Hole Symposium. He cautioned that it would be too early to declare a victory over inflation currently, and rates would have to remain restrictive for a longer period of time to bring inflation down to central bank's target on a durable basis.

Figure 1: Movement in global currencies in Aug'24



Performance of rupee

In contrast to most global currencies which rose against the dollar, INR declined. It was down by (-) 0.2% in Aug'24 hovering at 83.87/\$, close to its lifetime low of 83.97/\$. This is also in contrast to the performance of MSCI EM index, which gained (2%) due to dip in DXY index. However, amongst the set of 4 currencies, which fell against the US\$, it fell the least. Mexican Peso performed the worst (-5.6%), followed by Turkish Lira (-2.7%) and Argentine Peso (-2.1%). One of the key factor which impacted domestic currency's performance was slowdown in FPI inflows in Aug'24 to US\$ 3bn from US\$ 5.8bn in Jul'24. This was mainly seen in case of equity inflows (US\$ 0.9bn versus US\$ 3.9bn) than debt inflows (US\$ 2.1bn versus US\$ 2.7bn). This could be due to smaller gains made in Sensex (0.8%) or Nifty (1.1%) in Aug'24, compared with equity markets in US (Dow Jones: 1.8%; S&P 500: 2.3%). Apart from this, dollar demand by importers also impacted rupee's performance. However, lower international oil prices are a positive for the currency and has helped cap the losses in INR.

Outlook

As the rupee touched its record low level in Aug'24 (83.97/\$), at a time when US\$ was still weak, we believe, that movement in INR is expected to remain range bound. The factors that will support the domestic currency include: weakness in international oil prices and changes announced to the MSCI index (addition of 7 Indian stocks and higher adjustment factor for HDFC bank). This is expected help boost FPI inflows in the equity segment. On the other hand, pressure may arise from renewed strength of US\$, as investors scale back their expectation of super-sized rate cut by Fed in Sep'24 meeting. Any escalation in geo-political tensions in the Middle East will also increase the demand for safe haven currencies, which in turn may support US\$ and add pressure on INR. However, in case RBI decides to use its all-time high forex reserves (~US\$ 681bn as of 23 Aug 2024), then that may give INR an upward bias. On balance, we expect INR to trade the range of 83.8-83.9/\$ in the next fortnight.

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