Weakening Rupee

Why in new?

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Rupee crashed to a lifetime low of 69 against US Dollar.

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How is the rupee trend?

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- Rupee was pushed to a life-time intraday low of 69.10 a dollar.
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- The rupee is the worst-performing currency in Asia this year.
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- It has lost almost 8% in value since January 2018.
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- The rupee's previous historic low was in November 2016 (it plunged to 68.86).
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- It is, however, not the only currency to be in the weakening trend.
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- Emerging market currencies as a group have witnessed a sharp correction in their value against the dollar this year.
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What are the causes?

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- The rise in international **crude oil prices** is one of the reasons.
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- Importers have had to shell out more dollars to fund their purchases.
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- The rise in global trade tensions amidst the ongoing **trade war** is another factor.
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- But its impact on the rupee remains unclear as of now.
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- But by far the most important reason is the tightening of **U.S. monetary policy**.
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- Investors attracted by higher yields in the US have been pulling their capital out of India.
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- Also, **China** has been **depreciating** its currency (yuan).
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- This is to offset the effect of duties imposed by the US.
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- The Indian unit also seems to be moving in tandem with the yuan so that exporters don’t lose out.
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What will the implications be?

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- **CAD** -India’s CAD jumped to 1.9% of GDP in the fourth quarter of 2017-18 from just 0.6% a year earlier.
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- It is now expected to widen to 2.5% in FY 2019.
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- This could impact the rupee as the demand for dollars could turn out to be overwhelming.
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- But although current account deficit has widened, it remains modest relative to GDP.
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- Also, it is largely financed by equity inflows, including foreign direct investment.
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- **External risks** - Moody’s Investors Service has ruled out any risk with this development.
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- India’s large and relatively stable domestic financing base restricts its external vulnerability.
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- It will contribute to the economy’s resilience by protecting from abrupt changes in external financing conditions.
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- **Debt Affordability** - Currency depreciation transmitting into materially weaker debt affordability is limited.
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- This is because of India’s low dependence on foreign-currency borrowing to fund its debt burden.
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- India’s significant build-up of foreign exchange reserves in recent years to all-time highs provides a support buffer.
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- This will contribute to mitigating the external vulnerability risk.
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How does the future look?

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- The tightening of monetary policy by the U.S. Federal Reserve has traditionally caused impact on the global credit cycle.
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- It is hard to determine if the worst is over yet for emerging market currencies.
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- But the American central bank expects to raise interest rates further this year.
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- It suggests that there could possibly be more ramifications in the economy.
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- The government, as well as the RBI, recently raised domestic interest rates.
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- This was in response to the rising external economic risks.
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- There is a need for reassessing the policy of altering domestic rates in response to the US Fed rates.
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Source: BusinessLine, The Hindu

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