

## Currency Outlook

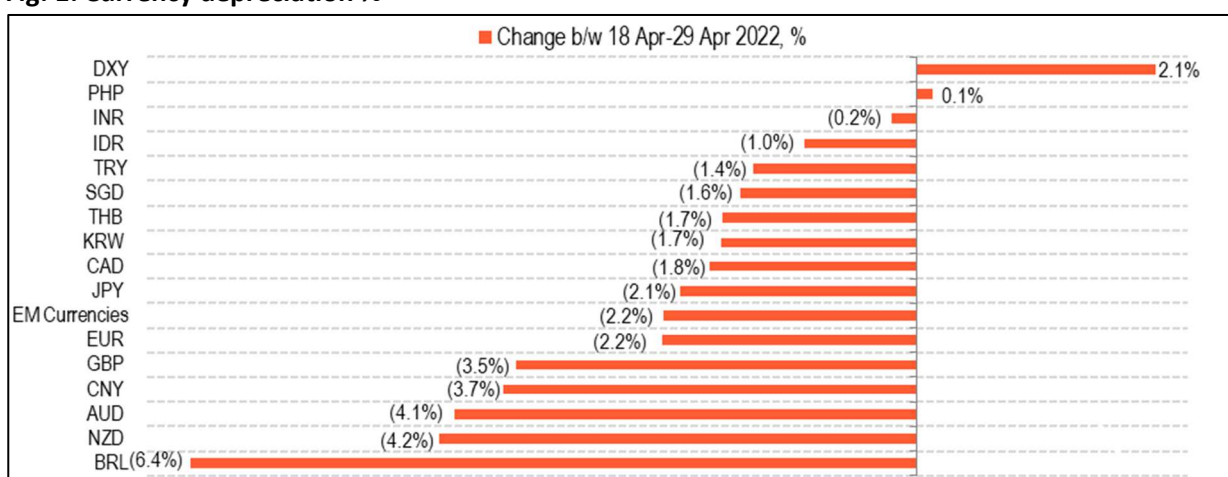
### INR to remain range-bound

Global currencies depreciated against the dollar in the last fortnight. Concerns over global growth and inflation, as well as expectations of aggressive rate hikes by Fed, underpin the recent strength in US\$. In fact, DXY index surged to a 20-year high in Apr'22. Other major currencies languished near multi-year lows, weighed down by increased policy divergence between Fed and other global central banks. GBP, EUR, CNY and JPY were the biggest losers. As a result, volatility in the forex market also increased. INR depreciated by 0.2% between 18-29 Apr 22 amidst higher oil prices and FII outflows. We continue to believe that the rupee will trade the range of Rs 76-77/\$ in the next fortnight.

### How have currencies fared?

Barring Philippines peso (PHP), other global currencies depreciated against the dollar in last fortnight of Apr'22 (18 Apr-29 Apr 2022). DXY strengthened by 2.1% in this period, to a two-decade high, despite an unexpected decline in US Q1CY22 GDP. Expectations of aggressive policy tightening by Fed have contributed to the broad-based dollar strength. Apart from this, concerns over global growth amidst a surge in Covid-19 cases in China have also contributed to the safe-haven's appeal. Chinese yuan (CNY) fell sharply by 3.7%, to its lowest level since Nov'20 as a flare up in Covid-19 infections in major cities threaten to derail growth recovery. However, the currency found some comfort from People's Bank of China's (PBOC) decision to cut foreign reserve requirement ratio. The government has also pledged support for the economy. JPY depreciated by 2.1% to a 20-year low, as Bank of Japan (BoJ) reaffirmed its ultra-dovish policy stance. This policy divergence between BoJ and Fed has widened the yield differential between dollar and yen, weighing on JPY.

**Fig: 1: Currency depreciation %**



Source: Bloomberg, Bank of Baroda | Data as of 29 Apr 2022

Amongst other advanced economies, EUR depreciated by 2.2% in the fortnight, to trade near a 5-year low amidst surging inflation and slowing growth. Russia's ban on gas supply to Poland and Bulgaria threatens the energy security of the region and further fuel inflationary pressures, thus

weighing on the EUR. GBP too depreciated by 3.5% as UK's macro data was weaker than expected. GfK's consumer confidence index declined sharply in Apr'21, and retail sales declined more than expected. New Zealand and Australian dollar too fell amidst a risk-off sentiment in global markets. Emerging market currencies fell by 2.2%. This was led by 6.4% decline in Brazilian real (BRL). Political tensions weighed on the currency.

INR depreciated by 0.2% in the last fortnight led by higher oil prices and FII outflows. While oil prices increased by 1.9%, FII outflows were US\$ 3.2bn. In Apr'22, INR depreciated by 0.8%.

### Currency volatility:

Apart from daily changes in currencies, volatility is also a major factor for the markets. Here, we compare volatility in two periods; 1-17 Apr 2022 and 18-29 Apr 2022. For almost all currencies, volatility has increased in the latter period. Some observations which can be drawn are:

- Except Hong Kong dollar (HKD), Turkish lira (TRY), Philippines peso (PHP) and Taiwanese dollar (TWD), volatility in all other currencies increased in the last fortnight.
- Brazilian real (BRL) has seen a sharp increase in volatility in the latter period.
- Volatility in currencies such as New Zealand, Korea, UK, Australia, Japan and South Africa has surged to double-digits.
- In fact, volatility in JPY increased 4 times in the latter period.
- Volatility in INR has also increased from 3.5% to 5.9%. However it still remained below the median level of 7.3%.

**Table 1: Annualized average daily volatility (%)**

Annualised daily volatility, %	1 Apr-17 Apr 22	18 Apr-29 Apr 22
HKD	0.3%	0.2%
TRY	4.0%	2.4%
PHP	6.4%	3.0%
TWD	3.8%	3.7%
SGD	2.7%	4.4%
IDR	1.0%	5.1%
MYR	2.1%	5.6%
INR	3.5%	5.9%
THB	3.7%	6.4%
CNY	2.6%	6.9%
DXY	3.8%	7.3%
EUR	5.4%	7.3%
CAD	5.0%	8.2%
MXN	9.0%	9.1%
NZD	5.5%	10.3%
KRW	6.0%	11.0%
GBP	5.3%	11.2%
AUD	7.5%	11.7%
JPY	4.0%	14.5%
ZAR	7.7%	16.8%
BRL	14.4%	25.7%

Source: Bloomberg, Bank of Baroda Research

**Outlook for INR:**

India's foreign exchange reserves have declined to US\$ 600.4bn as of 22 Apr 2022 from a record high of US\$ 642.5bn in Sep'21. Forex reserves have declined for 7-straight weeks now as RBI intervened in the forex market to support INR. FPI outflows once again intensified amidst expectations of faster rate hikes by Fed. With the Fed likely to raise policy rates by 50bps this week, FPI outflows may accelerate further. Further, commodity prices remain elevated, which will have a negative impact on India's trade balance. RBI is likely to intervene in the currency market to arrest any sharp movements in INR.

Fed commentary and movement in oil prices will determine the trajectory of INR in the near term. Overall, we expect INR to trade in the range of Rs 76-77/\$ in the next fortnight.

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