

FIRST LIGHT

16 December 2022

RESEARCH

BOB ECONOMICS RESEARCH | CURRENCY OUTLOOK

What's next for INR

SUMMARY

INDIA ECONOMICS: CURRENCY OUTLOOK

Driven by a sharper than expected moderation in US CPI, dollar eased, leading to gains in most major currencies. However, some of these gains have since been reversed as the Fed signaled a higher terminal rate. Importantly, it also stated that rates are going to stay higher for longer, against market expectations of a rate cut next year. DXY has since strengthened, which has put pressure on other currencies. INR depreciated in the last fortnight, showing significant divergence from its other Asian peers. INR depreciated by 1.2%, erasing much of the gains it made last month. Volatility in INR also increased. We see limited upside risk for the INR while there are significant risks on the downside, mostly on the BoP front. We expect a range of 82-83/\$ in the near-term.

[Click here](#) for the full report.

Daily macro indicators

Indicator	13-Dec	14-Dec	Chg (%)
US 10Y yield (%)	3.50	3.48	(2bps)
India 10Y yield (%)	7.27	7.22	(4bps)
USD/INR	82.81	82.45	0.4
Brent Crude (US\$/bbl)	80.7	82.7	2.5
Dow	34,109	33,966	(0.4)
Hang Seng	19,596	19,673	0.4
Sensex	62,533	62,678	0.2
India FII (US\$ mn)	12-Dec	13-Dec	Chg (\$ mn)
FII-D	(28.8)	(471.1)	(442.4)
FII-E	437.5	80.8	(356.6)

Source: Bank of Baroda Economics Research

BOBCAPS Research

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CURRENCY OUTLOOK

15 December 2022

What's next for INR

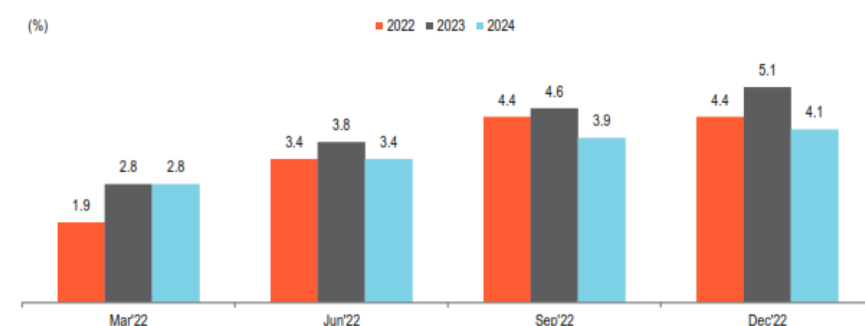
Driven by a sharper than expected moderation in US CPI, dollar eased, leading to gains in most major currencies. However, some of these gains have since been reversed as the Fed signaled a higher terminal rate. Importantly, it also stated that rates are going to stay higher for longer, against market expectations of a rate cut next year. DXY has since strengthened, which has put pressure on other currencies. INR depreciated in the last fortnight, showing significant divergence from its other Asian peers. INR depreciated by 1.2%, erasing much of the gains it made last month. Volatility in INR also increased. We see limited upside risk for the INR while there are significant risks on the downside, mostly on the BoP front. We expect a range of 82-83/\$ in the near-term.

Aditi Gupta
Economist

Fed policy and DXY

The dollar eased to a 6-month low as a softer than expected CPI print in the US, which raised the possibility that the Fed will ease the pace of rate hikes going forward. US CPI eased to 7.1% in Nov'22 from 7.7% in Oct'22. Investors eagerly awaited the Fed policy to look for signs of a likely Fed pivot. These hopes were quickly quashed as the Fed, while tempering the pace of rate hike to an expected 50bps, gave no signs that the fight against inflation was nearing an end. In fact, as per the latest projections released, the terminal Fed Fund rate is expected to be higher at 5.1% in 2023 (4.8% earlier), implying another 75bps of rate hike in subsequent meetings. This also essentially quelled market expectations of rate cuts in the latter part of CY23, meaning that rates will remain higher for longer than expected. Hence, while DXY weakened in the last fortnight, it has regained some strength today.

Figure 1: Projections of Federal Fund rate higher



Source: Statement of Economic Projections, Federal Reserve, Bank of Baroda Research

Currency movement in the last fortnight

Most global currencies gained amidst a broad based improvement in risk sentiment. This was led by expectations that global inflation has peaked and reopening in China. EUR and GBP gained 3.1% and 2.7% against the dollar. DXY index fell by 2.1%. Apart from the weakness in dollar, positive macro data (improvement in investor sentiment index in Germany and rebound in UK's monthly GDP) also aided gains in the respective currencies.



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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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