Currency depreciation: RBI's response: Signposts for other central banks?

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The domestic currencies of various economies, especially of emerging market economies, have been subject to steep declines in the last 6 months. Amongst the worst hit has been the Indian Rupee, which has depreciated nearly 15% during the April-November'13 period, touching a lifetime low of Rs.68.8/US dollar. This fall in the currencies of emerging market economies has been the result of the shift in foreign investor preference towards US markets and dollar denominated assets with the US Federal Reserve indicating that improving US economic environment could see it scale down, earlier than anticipated, its quantitative easing programme i.e. its $ 85 bn monthly bond buying programme that has been largely responsible for infusing liquidity into the global markets and propelling asset prices. The purpose here is to examine what all the RBI has done to restore confidence in the rupee which can serve as a template for other central banks too.

Although, fundamental factors such as India's high current account deficit (CAD) (4.8% of GDP in the last fiscal year) and the surge in FII outflows from the domestic capital markets ($ 12 bn between June-August following indications of the tapering of US economic stimulus programme), have been the chief contributors to the rupees steep decline, weak investor sentiments towards India on account of its sluggish economic growth and widening budget deficits, added to the weakness in the Indian Rupee.

The decline in the Rupee emerged as the foremost macro-economic concern for the country. Already suffering from high budget deficits and given the high inelastic or essential imports of the country, a depreciating currency is something India could ill afford. Curbing/reversing the steep and persistent fall in the rupee necessitated various policy measures from the Indian central bank i.e. Reserve Bank of India (RBI) as well at the government. To this end in the last few months a series of measures have been announced ranging from adjusting interest rates to rein in fund outflows from the country, to measures attracting foreign inflows into the country (FDI,FII and NRI deposits), increasing the import duty of non-essential items viz. gold, sale of dollars from RBI reserves to policies that build investor sentiments. While some of these measures have been temporary in nature, having already been reversed, some of them have long term implications.

We have listed here the various measures introduced by the RBI in the last 6 months to control the rupee depreciation and try to gauge the overall effectiveness of these so far.

1. Reduction in the limit of Overseas Direct Investment (ODI) under automatic route for all fresh ODI transactions (wef 14 Aug'13) from 400% of net worth to 100% of net worth of an Indian entity. This limit applies to remittances made by Indian Companies under the ODI scheme for setting up unincorporated entities outside India in the energy and natural resources sectors. This limit does not apply for ODI by the Navratna PSU's, ONGC Videsh Ltd and Oil India in overseas unincorporated entities and incorporated entities, in the oil sector. This also does not apply for all financial commitments made on or before 14 Aug'13, in compliance with the earlier limit of 400% of net worth and for financial commitments funded by way of external commercial borrowings (ECBs).

2. Reduction in limit for remittances made by Resident Individuals, under the Liberalized Remittance Scheme (LRS), from USD 200,000 to USD 75,000 per financial year. While resident Individuals have been permitted to set up Joint Venture (JV)/Wholly Owned Subsidiary (WOS) outside India under the ODI route within the revised LRS limit, LRS cannot be used for acquisition of immovable property outside India directly or indirectly. Earlier restriction on use of LRS for prohibited transactions such as margin trading and lottery continues.

3. Raising of interest rate ceiling on long-term maturity Foreign Currency Non-Resident [FCNR (B)] deposits by from LIBOR/Swap plus 300 bps to LIBOR/Swap plus 400 bps for deposits with maturity of 3-5 years.

4. Deregulation of interest rates on Non-Resident (External) Rupee (NRE) Deposits. Earlier, interest rates offered by banks on NRE deposits could not be higher than those offered on comparable domestic rupee deposits. However, in order to pass on the benefit of exemption provided on incremental NRE deposits with maturity of 3 years and above from CRR/ SLR requirements and to increasing fund inflows, the RBI decided to give banks the freedom to offer interest rates on such deposits without any ceiling.

5. Restrictions on gold imports that includes ban on import of gold coins and medallions, 20% of every lot of gold imported to the country to be exclusively made available for purpose of exports and only the balance for domestic use. Definition of domestic use of gold modified as gold available to entities engaged in jewellery business/bullion dealers and to banks authorized to administer the Gold Deposit Scheme against full upfront payment. The RBI has also put curbs on credit directed to purchase of gold. The demand for gold and thereby the higher gold imports have been attributed to the country's high CAD.

6. Adjusting the Marginal Standing Facility (MSF) Rate. The MSF, introduced in May'11, enables banks to borrow in excess of the regular repo auctions under LAF, but at a higher cost. At inception the MSF rate was designed to be 100 bps above repo rate. This rate was increased to 200 bps above repo rate on 20 Sept'13 in an attempt at constraining liquidity in the system. The MSF rate has however been bought back to the 100 bps above repo rate level. This had helped to lower the speculative positions being taken by some banks in the forex market by borrowing thought the repo window.

7. Restriction on bank borrowing through the LAF (Liquidity Adjustment Facility) window (from 1% of Net Demand and Time Liabilities to 0.5%) in an attempt to curb liquidity and thereby speculative activity.

8. Introduction of liquidity tightening measures through CMB (cash management bills) auctions every week to take out funds from the banking system.

9. RBI decided to directly sell dollars to three public sector oil marketing companies to meet their import requirements through a special window to reduce the pressure on the rupee. Oil companies are the largest buyers of dollars, as such their demand for dollars has been a major factor driving the exchange rate. The RBI since early November'13 has reduced the quantum of dollar sales to the oil companies and they have been sourcing a part of their requirement from the market.

10. Dollar sales by the RBI. The RBI has been time and again intervening in the forex markets by way of dollar sales from its reserves. The central bank has for the period Apr-Sept'13 sold US dollars amounting to $24.7 bn (for the whole of FY13 the RBI dollar sales were $16.2 bn) to curtail the depreciation in the Indian Rupee. The effectiveness and sustainability of this tool to retain the value of the domestic currency has been debated given the limited foreign currency reserves with the RBI. As of mid-November'13, the RBI has in its reserves foreign currency assets totaling $256 bn.

11. Increase in overseas borrowing limit for banks from 50% to 100% of their unimpaired Tier-1 Capital and allowed banks to convert the same into rupee and hedging the same with the RBI at concessional rates.

12. The RBI has opened a special swap window for banks till 30 November'13 to swap foreign currency non-resident (FCNR) dollar deposits with a minimum duration of 3 years at a fixed rate of 3.5% per annum.

13. The RBI has provided exporters and importers more leeway/flexibility in cancelling and rebooking forward exchange contracts. Exporters are permitted to rebook cancelled forward exchange contracts to the extent of 50 % of the value of cancelled contracts. Earlier this limit was capped at 25 %. Importers too can rebook to the extent of 25%. Importers were previously not allowed to rebook cancelled forward exchange contracts.

The government too enacted measure that complemented the RBI measures to rein in the currency fall. Some of the main government measures to shore up the rupee included raising the duty on non-essential import items viz. gold, increasing the limit of its currency swap agreements with Japan from $15 bn to $50 bn and liberalization of FDI limits in 12 sectors.

The measures enacted by the RBI and the government, often argued to have yielded only a limited result, has nevertheless had an overall positive impact on the Rupee. The rupee has recovered from its low of over Rs.68/$ and is currently seen to be relatively stable around Rs.62-63/$. The inflows of funds into the country too have increased and the RBI forex position too has improved. India's trade balances too have been recording encouraging improvements in recent month. Nevertheless, the downside risks to the currency persist. With the tapering of the US quantitative easing regarded to be a given, although timelines for the same are yet to be finalized, the rupee could come under renewed pressure in the coming future. The rupee would also be susceptible to external shocks that could disrupt its trade dynamics i.e. impact on the country's oil imports and its overall exports. Continued monitoring and proactive policy action from the RBI and the government is essential to maintain the value of the Rupee.

DG Khan Cement Company Ltd senior management visit LSE

- LSE Press Release

DG Khan Cement Company Ltd senior management visited The Lahore Stock Exchange to participate in the Corporate Briefing Program. CBP is an interactive program initiated by the Lahore Stock Exchange under the Corporate Communications Department to encourage companies to come forward and share their financials and non financial projects before the members, TREC Holders, investors and the media to abridge the communicational gap between the listed companies and the market participants through this platform.

Chief Financial Officer and Director, Mr. Inyat Ullah Niazi, Company Secretary, Mr. Khalid. M. Chohan and Senior Manager Finance, Mr. Syed Anees Hassan addressed the participants explaining and highlighting the financial performance of the company. Mr. Anees while sharing DGKCC's financial performance stated that energy shortage is one of the biggest challenges faced by the industrial sector of Pakistan. He also mentioned that the company has successfully installed and operated Waste Heat Recovery plant and Alternate Fuels project