

## Currency Depreciation: Forces Behind the Falling Rupee

The Indian Rupee (INR) has been on a downward trajectory in recent times, sparking concerns among policymakers, businesses, and consumers alike. Here's a closer look at the factors contributing to the rupee's decline, its impact, and what the future might hold.



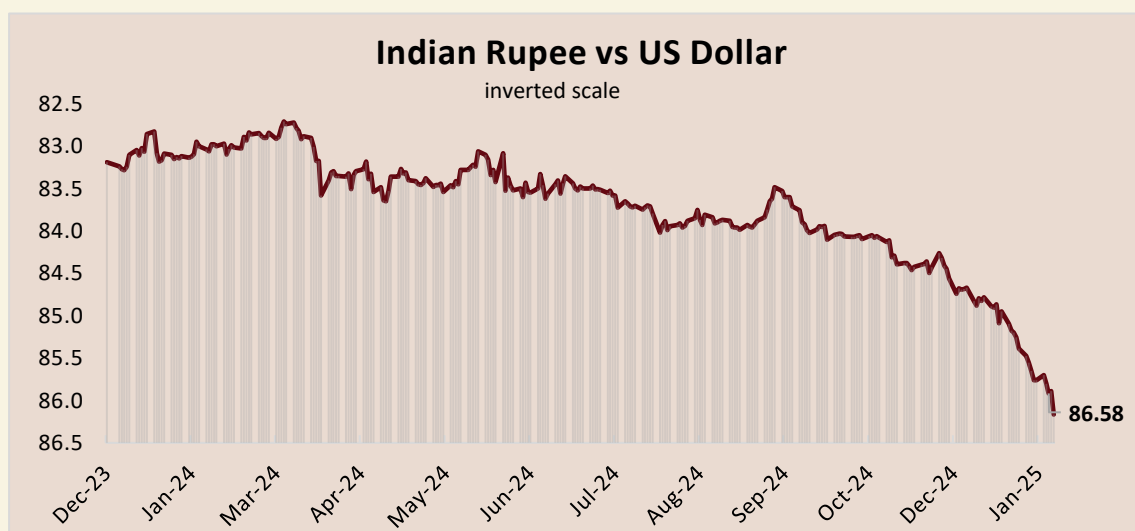
### 1. Why has the Rupee been depreciating?

The rupee has come under pressure in the last few months due to various domestic as well as international factors.

- Expectations of shallow rate cuts by the US Fed led to a spike in the US bond yields. High US yields made the US attractive to investors relative to emerging markets like India.
- Uncertainty regarding the new US government policies.
- Stronger-than-expected US jobs report, which strengthened the dollar and pressured emerging market currencies (including INR).
- Substantial FII outflows in past three months from Indian equity markets. (FIIs have withdrawn over \$4 billion till date from Indian stocks this month (Jan'25), following a \$11 billion outflow last quarter).

### 2. How has been Rupee's performance?

- **The Indian rupee plunges to all-time low, breaches 86 against US dollar** on Jan 13, 2025. In the last three months, the domestic currency has depreciated to Rs. 86.58 against the US dollar on Jan 13, 2025 from Rs. 83.94 on October 10, 2024. Rupee depreciated 3% in 2024 and it has plunged 3.1% in the past three months.
- The Dollar index, which reflects the strength of the dollar versus other major currencies, is at its peak at 109.



Data as on 13th Jan 2025. Source: Investing.com

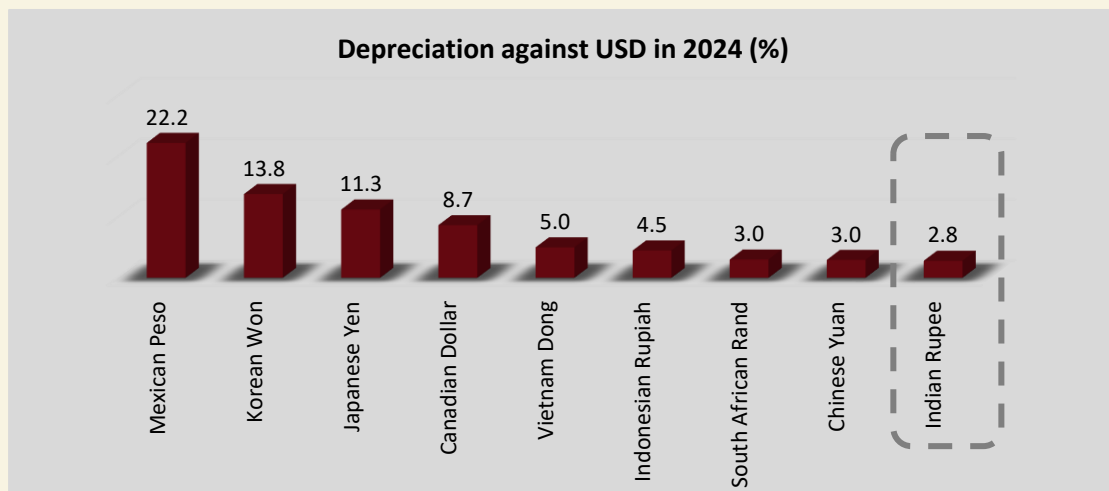
**3. How does a weak rupee affect the economy?**

- **Weak rupee increases the import bill.** India’s import dependency on crude oil was 88.1% between April-Nov 2024, compared to 87.6% in the corresponding period of the previous year.
- **Worsens government deficit:** India’s trade deficit touched an all-time high of \$32.8 bn in Nov 2024, compared to \$20.7 bn in Nov 2023.
- **Inflation goes up** as the cost of imported goods rises.
- **Dampens economic growth** by creating upward pressure on interest rates.

**4. How is RBI managing the rupee?**

- The RBI has been actively intervening in forex markets to stabilize the rupee.
- The central bank has been using the most common strategy for intervention, which is selling dollars in the spot market and **taking positions in the non-deliverable forward (NDF) market.**
- To mitigate the liquidity impact due to USD selling, the **RBI has also reduced CRR by 50bps in its Dec monetary policy review.**

**5. Rupee did better than peers due to RBI intervention**



Source: News articles

- **Rupee depreciation has been modest** compared to other countries.
- Though the RBI intervention has reduced rupee volatility, it has led to its overvaluation in REER (Real Effective Exchange Rate) terms. REER reflects the export competitiveness of a country.

**Outlook**

- **It is expected that rupee will continue to see headwinds** from slowing domestic growth and elevated external risks in the current financial year.
- Lower export growth due to the growth slowdown of **India’s major trading partners will put pressure on the rupee in the near term.**
- On the global front, **concerns over US monetary policy and uncertainty surrounding US President-elect Donald Trump’s planned policies** have led to increased bearish bets on the rupee.
- Moreover, a **possible interest rate hike by BoJ (Bank of Japan) will prove negative** for emerging market currencies, including India.

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