kotak Securities

FOREIGN EXCHANGE INSIGHT

FX, RATES & MACRO DESK

MARCH 25'2019

INSTRUMENT	LAST PRICE	1 DAY	1 MONTH	1 YEAR
USD/INR	69.06	0.11%	-2.8%	6%
EUR/INR	78.03	0.07%	-3.4%	-3%
GBP/INR	91.11	0.43%	-1.9%	-1%
JPY/INR	62.86	0.22%	-1.7%	2%
EUR/USD	1.1300	-0.02%	-0.5%	-9%
GBP/USD	1.3194	-0.11%	0.7%	-7%
USD/JPY	109.85	-0.06%	-1.1%	4%
USD/CNH	6.7198	-0.05%	0.5%	7%
10 YR YIELD- IN	7.31	(0.03)	(0.11)	(0.25)
10 YR YIELD- USA	2.44	(0.00)	(0.23)	(0.38)
GOLD ($/Oz)	1,316	0.1%	-1%	-3%
SILVER ($/Oz)	15.47	0.3%	-3%	-7%
BRENT CRUDE ($/Brl)	66.56	-0.7%	3%	-6%
COPPER 3M ($/Ton)	6312	-1.7%	-3%	-6%
NIFTY	11353	-0.90%	4.35%	14%
HANGSENG	28587	-1.81%	-1.29%	-6%
S&P 500	2801	-1.90%	0.16%	8%
INR 1M FWD	0.32	0.02	0.08	0.01
INR 2M FWD	0.52	(0.00)	(0.01)	(0.04)
INR 3M FWD	0.75	0.01	(0.01)	(0.02)
INR 6M FWD	1.35	(0.01)	(0.10)	(0.03)
INR 12M FWD	2.50	0.01	(0.26)	(0.06)

	1 DAY	MTD	QTD	CTD
FII INVESMENT- EQ ($ Mn)	196	3,816	6,112	6,112
FII INVESMENT- DEBT ($ Mn)	259	2,037	384	384
TOTAL- ($ Mn)	455	5,853	6,496	6,496

CURRENCY	ECONOMIC DATA
USD	FOMC Member Evans Speaks
EUR	German Ifo Business Climate

FX VIEW

We kick-off the final trading week of FY19. It has been a year of wild swings, opposite of the calm waters of FY18. Rupee depreciated from 63.30 to 74.50 against USD and then went on to recoup half of those losses, to test 68.30.

RBI has been a busy body in FY19. First half they sold Dollars aggressively, using cash and derivative positions to contain the slide of Rupee. However, during the second they got the opportunity to recoup part of that dollars which they sold. Bulk of that buying occurred during the current quarter. Between end of Dec'2018 and March 15th, RBI's FX reserves have increased by over 10 billion dollars. Considering the fact that Dollar has been largely flat against most of the major currencies during this period, the impact of FX variation would have been minimal. Therefore, RBI may have purchased around USD 10 billion. During the same time, FPIs have bought a little over USD 6 billion in debt and equity markets. Add another USD 7/8 billion of probable FDI flows in Jan-March quarter. The rest of the components of the financial account are too volatile to predict. Hence, it can be said that RBI has mopped up around three-fourths of the FDI+FPI inflows into India. This is the reason why Rupee has been a median performer, when compared against a broad basket of currencies around the world. Even when one compares against USD, the pair, USDINR is more or less flat, around the level of 69.00 on spot.

Thanks to FX swap, the cost to hedge Dollars in the forward months have tumbled. This has led to spike in capital flows into corporate bonds, both through VRR route as well as non-VRR route. We expect the spread to narrow considerably in the coming days, as demand for arbitrage causes the forward premia to move higher. Remember, a lower forward premium has two sides to it. Though on one hand it can induce the FX arbitrage we mentioned, but on the other hand, it can reduce appetite for carry trade from specs who use the forwards to earn rolling yield. It also exposes Rupee to any kind of a global contagion or domestic shock.

Though reversal of flows in favour of INR can continue to support INR but two other factors would prevent appreciation beyond 68.50 difficult to sustain. On one hand, economic data continues to point towards a protracted slowing down of the world economy. In US, yield curve has inverted dangerously. Analysts are gradually downgrading their expectation of corporate earnings around the globe, and India is no exception. Valuations are looking increasingly stretched. Any negative surprise in US-China trade talks and or, deeper than expected slowdown across Europe and EMs causing stress in US can knock global equities off their lofty peaks.

Indian debt is another story. When globally, yields are crashing and yield curves are flattening. Indian yield curve remains defiantly steep. RBI is expected to lower rates by another 25 bps in the April meeting and sound dovish. A steeper yield curve may pricing in the premium of having to absorb massive amount of supply of bonds central government during the first half FY20. At the same time, with credit-deposit ratios at a decadal high, there is little reason for banks to load up on GOIsecs. FPIs till now have shown little appetite for GOIsecs. If that changes in the coming weeks, especially post RBI, they not only the Indian 10 year yields can fall sharply, but also further inflows can support INR. Having said that, we need to keep an eye on oil prices. As of now, oil is finding resistance closer to 68.00/70.00 region on Brent, thanks to the growth jitters around the world. However, any breakout above that region can make Indian debt unattractive.

Technically, USDINR remains in downtrend as long as below 69.60 on spot. Having said that, if global risk-off intensifies, JPYINR would be a tactical long with stop below 61.00. Refer to the chart on next page.

*** CHART ON NEXT PAGE***

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Source: Bloomberg

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