Government Lays Out a Safety Net for the Rupee

The doomsayers have been having a field day ever since the rupee went into freefall. But their voices have been drowned out ever since the government got its act together and managed to stem the rapid plunge in our national currency. Reports all over the mainstream media confirm that the Finance Ministry has been taking a proactive role in tandem with the Planning Commission. Finance Minister P Chidambaram, has rightly told the markets not to overreact in panic, since currency fluctuations have been happening all over the globe. Indeed the rupee has depreciated by approximately 7.5% this year, but so have several currencies across continents. That includes Indonesian rupiah (4.5%), Brazilian real (4.7%), Philippine peso (5.5%), Turkish lira (6.1%), Korean won (6.2%), Russian ruble (6.9%) and South African rand (17.2%), say reports. As such, when compared to its peers, the Rupee has not performed badly.

Though the situation remains difficult, the worst seems to be over with clear signs of the Rupee bouncing back, slowly but surely after the RBI and Sebi took steps to curb volatility, while banks and exporters sold the US currency. Market regulator SEBI has also been working in close collaboration with the central bank, the RBI. The RBI has been selling dollars and buying excess rupees from the system, helping the currency stay afloat. The apex bank has also come out with clear guidelines to curb speculation in the falling rupee—and these diktats have commendably managed to curb the fall. According to RBI governor D Subbarao the global factors have contributed to the currency's fall. "It's difficult to say how long that effect (from worldwide factors) will persist because these factors (are) beyond our control," he said. This factor has also led to the apex bank withholding the option to cut interest rates to boost a sagging economy.

Ergo, the Indian regulators have their collective task cut out for them. Among the many pitfalls facing the government's carefully charted strategy is the precarious situation of our foreign exchange reserves. The forex kitty has dwindled to a mere $260 billion dollars—and reports have it that around $172 billion worth of debt will come in for repayment over the next 12 months. And this is just one of the many difficult situations that lie ahead. Inflation has also been difficult to tame.

SEBI has also clamped down hard on open position limits on members to eliminate rupee speculation. "In consultation with the RBI and in view of the recent turbulent phase of extreme volatility in dollar-rupee exchange rate, it has been decided to curtail position limits and increase margin requirements for currency derivatives," the capital market regulator said in a statement recently. It is welcome that the government is in active fire-fighting mode and Chief Economic Adviser Raghuram Rajan has indicated that Government might be considering India's first sovereign bonds issuance.

On the global front, at G-20 summit earlier this year, the world leaders had also declared to move towards more market determined exchange rate system and enhance exchange rate flexibility to reflect underlying economic fundamentals and refrain from competitive devaluation of currencies. It was agreed that advanced economies, including those with reserve currencies, will be vigilant against excess volatility and disorderly movement in exchange rates. India has also agreed to refrain from "competitive devaluation" and bring in exchange rate flexibility to ensure that no country gets undue advantage.

Amid the gloom and boom, a few export-oriented sectors are looking forward to some better days. Financial institutions are also targeting NRIs, who have seen their net worth in rupees rapidly climb. A few financial analysts are also predicting that India's macroeconomic indicators remain fundamentally robust over the long run. According to a leading financial analytics company, the Indian economy "will be able to weather currency risks and continue to grow" over the next few months.

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