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TPC Trade Promotion Council of India
Notified in the Foreign Trade Policy by Department of Commerce, Government of India

Forex Market Insights

Newsletter

Volume 09 → May 07th to May 13th 2022

Welcome

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Dear Stakeholders,

An eventful week for the financial markets, which kept market participants at the edge of their seats. A scheduled rate hike from Fed and BoE to an unscheduled one from RBI ensured enough volatility in the system. Fed's tightening policy would continue on track after the non-farm payrolls number expands in April.

Emerging market currencies closed in red for the week, but hopes of dollar inflows for LIC IPO took the Rupee a tad below 76. Eventually the Rupee tanked to test its low of Mar 7 of 76.97,, but heavy intervention kept it from making a new low. It took RBI just 2 months to exhaust its 1 year of dollar purchases. High oil price and consistent dollar outflows have pressurized Indian equities, which moved down along with global indices as long term treasury yields rise to multi year highs. Volatile times are ahead, but are we heading to an inflation-led recession?

Regards

Mr Vijay Gauba
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Trade Promotion Council of India

Key Takeaway Summaries

₹ INR

The policy repo rate has surged by 40 basis points to 4.40% with immediate effect.

€ EUR

US dollar strength was extensive but risk-aversion boosted the low-yield currency.

£ GBP

Bank of England has projected a recession for the UK economy in the 4th quarter of 2022.

¥ JPY

Looking at BOJ policy and yields above 3% much recovery in yen is not expected.

₹ INR

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
4.4%	1.84%	6.95%	7.8%	$-20.07B

Events to WATCH

May 12, 17:30
CPI (YoY) (Apr)

May 12 17:30
Manufacturing Output (MoM) (Mar)

May 13, 17:00
FX Reserves, US$

May 03, 17:50
Trade Balance

The US$/INR pair ended the week at 76.9150. In an unscheduled briefing on Wednesday, RBI Governor Shaktikanta Das announced that the Monetary Policy Committee voted to hike rates. The policy repo rate has surged by 40 basis points to 4.40% with immediate effect. The SDF rate is now at 4.15% and the MSF rate and bank rate stand at 4.65%. The Reserve Bank Of India also increased the CRR by 50 bps to 4.5% effective from May 21. Liquidity withdrawal due to this increase would be to the order of Rs 87,000 crore. The public issue of LIC continued to receive a positive response from investors as the offer garnered another Rs 5,000 crore worth of bids.

Investors have poured in Rs 20,269 crore into the IPO in 3 days. The US Fed delivered a hefty 50 bps surge in its short-term interest rates. US also plan to start reducing its US$ 9 trillion balance sheet starting next month. The central bankers took action to fight the inflationary pressure post the Ukraine-Russia conflict. The upcoming week's events for rupee are Federal Fiscal Deficit (Mar), CPI (YoY) (Apr), Manufacturing Output (MoM), Trade Balance and Industrial Production (YoY) (Mar). The major stats due next week for US are Core CPI (MoM) (Apr), Crude Oil Inventories & Initial Jobless Claims.

$ USD

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
1.0%	-1.4%	8.5%	3.6%	$-109.80B

Events to WATCH

May 11, 18:00
Core CPI (MoM) (Apr)

May 11, 20:00
Crude Oil Inventories

May 11, 20:00
Cushing Crude Oil Inventories

May 12, 18:00
PPI (MoM) (Apr)

May 12, 18:00
Initial Jobless Claims

May 12, 18:00
Core PPI (MoM) (Apr)

After trading in the range of 76.00 – 76.75 for 3 weeks, US$/INR broke above the band and touched the all-time low of 76.97. This is the third attempt towards the 76.90 – 76.97 region (red horizontal lines). Bank of England's comment that they could slip into a recession next year spooked financial markets – global equities collapsed and there was a significant flight to safety (dollar gained and bond yields rose). On the daily candlestick chart, a new price up gap has been formed today – 76.295 to 76.57, highlighted by green horizontal lines. Do recall that there are 2 long standing price gaps yet to be filled: 74.73 (23 Feb'22) to 75.0225 (24 Feb'22) – blue horizontal lines, and 73.9750 (13 Jan'22) to 74.04 (14 Jan'22) – purple horizontal lines. Quite surprising since price gaps in US$/INR unusually gets filled up. An upward moving trend line (pink colour), connecting dollar lows of 73.77 (12 Jan'22), 74.53 (23 Feb'22) and 75.31 (5 Apr'22) comes around 75.80-75.90. This region could be an important short-term support. Momentum indicators are erratic and predominantly neutral. Dollar exporters to increase their hedge ratios at spot above 76.80. After recent interest rate hikes by the Fed and RBI, forward premiums have stabilized around 4%. Strong recommendation to use vanilla options to hedge & some forwards to reduce overall cost of hedge. Dollar importers need to be extremely vigilant – start hedging for short term on any rupee gains towards 76.00 – 76.20. Use more of forwards and some vanilla options.

€ EUR

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
0.0%	0.2%	7.5%	6.8%	€-7.62B

Events to WATCH

May 10, 14:30
German ZEW Economic Sentiment (May)

May 10, 14:30
German ZEW Current Conditions (May)

May 11, 11:30
German CPI (MoM) (Apr)

May 11, 15:00
German 10-Year Bund Auction

May 13, 14:30
Industrial Production (MoM) (Mar)

The week was completely volatile and ended with EUR/US$ hovering around 1.056, closer to the year-to-date low of 1.047. The pair recovered part of its last weekly losses but retained the selling sentiment inclusively. EUR/US$ floated around 1.054 as sellers took a pause. US dollar strength was extensive but risk-aversion boosted the low-yield currency. The US Nonfarm Payrolls report of April was published yesterday adding 428K jobs to the economy, more than the 391K predicted by analysts. Manufacturing, transportation, Leisure, hospitality, and warehousing steered the Job growth. US stocks contemplated the pessimistic market sentiment and increased losses for the second consecutive day. After a prolonged downtrend, euro has found a base support around the 1.05 mark.

In a scenario when inflation (and consequently interest rate decisions/expectations) along with geo-political factors are dominating global financial markets, making a technical assessment becomes quite challenging (and sometimes futile too). On the daily candlestick chart, euro has traded around the psychologically important 1.05 level for seven consecutive trading sessions. Despite intra-day attempts below that mark, it never closed any day below it. A Doji-like candlestick pattern was formed yesterday, with a high-low range of around 117 pips but open-close just 6 pips apart. Following an extended decline, a Doji-like candle indicates indecision and confusion. Momentum indicators (MACD and RSI) are near their oversold territories. MACD has crossed above its Signal line, indicating a ‘buy’ signal. Comparing current euro’s low with the low of 7 Mar’22, there are visible positive divergences in MACD Forest and RSI – prices have declined to a new low while the indicators have not. Technically, EUR/US$ looks to be a good buy; such EUR/US$ levels have not been seen since Jan’17. If one wants to trade, can go long on euro with a strict stop loss and a defined take profit. For hedging purposes, one can look to buy euro for import liabilities for the next 1-2 months.

£ GBP

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
1.0%	1.3%	7.0%	3.8%	£-9.26B

Events to WATCH

May 12, 11:30
GDP (QoQ) (Q1)

May 12, 11:30
GDP (YoY) (Q1)

May 12, 11:30
Manufacturing Production (MoM) (Mar)

May 12, 11:30
Trade Balance (Mar)

GBP/US$ fell 1.8% this week, Pair remained on a back foot from the start of week, though GBP tried to rebound and went 1.26+ post US interest rate hike by 50 bps as expected but couldn't sustain there as Bank of England projected a recession for the UK economy in the 4th quarter of 2022, post increasing the interest rate by 25bps. Looking at current economic conditions of UK, global growth fears and US treasury yields trading above 3% levels one cannot expect much recovery in the pair, despite such attractive levels for buying which were seen 22 months ago. It's quite an important week ahead for the pair on the event side as lot of important data is scheduled – Industrial production, Manufacturing production, Trade balance of march month along with Q1 yearly and quarterly GDP.

The GBPUS$ pair ended the week on downward side. Pair made a high of 1.2638 and went as low as 1.2273. Looking at trend it's getting difficult for the GBP to rebound but pair can take a move towards 1.2750 as 20 days SMA is there breaking of 1.2750 hurdle can push the pair towards psychological level of 1.29 and 1.30. RSI is also indicating bullish reversal as it trading at 27 levels which is considered to be an oversold zone while MACD is at neutral zone. Last week cable took a move towards 1.2250 levels but we saw sudden recovery there. These levels could be good support for the upcoming days breaking of these levels can push towards 1.2170 (static level from May 2020) could act as interim supports ahead of 1.2100.

¥ JPY

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
-0.10%	1.1%	1.2%	2.6%	¥-412B

Events to WATCH

May 09, 6:00
Services PMI
(Apr)

US$JPY ended the week 0.5% higher at 120.56. the air went to a high of 130.80 and went as low as 128.61. Japanese currency tried to recover this week after Fed Chairman Powell's denied of a 75 basis point hike in June which led to a fall in US treasury yields and aided yen to gain but on Thursday US equities plunged more than 4% and yields rocked almost 15 points and close above 3% which again pushed pair above 130 levels. Looking at BOJ policy and yields above 3% we don't expect much recovery in yen. It's a quiet week ahead for the pair as only services PMI is set to release in the start of week itself.

The US$/JPY remains within the range that originated in the 1st week of May. The division at 129.00 has turned from resistance into support. The Moving Average Convergence Divergence price line crossed the signal line last Wednesday but until a divergence opens, especially one that occurs in time with an approach to the lower side of the track. Furthermore, the Relative Strength Index dipped out of the overbought zone on Wednesday without giving a convincing argument for a turn in the pair's fortunes. The first resistance is at 130.81 level, if the pair breaks it which is very likely then the second resistance is at 131.25. The first support can be seen at 130 followed by the second at 129.05.

BLOG

Is managing foreign exchange risk essential for hedging?

Foreign exchange risk is a financial risk which exists when a home currency is converted into another during the transaction. Unfavorable currency movements lead to a lower value of assets which are quoted in domestic currency in the international markets.

All corporates dealing with international markets are exposed to foreign exchange risks. Foreign exchange markets fluctuate due to many factors beyond the control of a company and thus these risks have to be incorporated while quoting prices to the clients and suppliers overseas.

Factors such as the recent US China global trade war or geopolitical uncertainties due to UK **Brexit** or Pakistan's terror attack on India etc. lead to high fluctuations in the currencies and may trigger stop loss levels for high volume currency pairs. Thus dealing in currency is highly risky and calls for an expert who tracks the foreign exchange markets on a regular basis to assist corporates to manage them. Revenues earned abroad will be affected with the currency risks. Already uncertainties due to global trade war have created havoc in the currency markets. Though some risk aversion assets like Gold, Japanese Yen, Swiss Franc have seen appreciation in such times, risk assessment remains critical.

Why manage currency risk?.

Managing **currency risk** helps protect the cash flows along with profit margins, which in turn help to assimilate financial budgeting and forecasting. Once cash flows are determined, it becomes easier to plan for the future and work around costing accordingly. With clarity around finances, the corporate is in a better position to understand the borrowing capacity especially when expanding from growth perspective.

Every change in currencies affects the balance sheet which is turn affects the health of the corporate. Thus business benefits are many for effectively managing the foreign currency risks.

How does one go about managing forex risk?

The first step towards managing forex risk is to create a foreign exchange policy within the corporate. Once the cash flows are in place, the process of understanding which **currency fluctuation** will affect which portion of the balance sheet is important as many factors are in place at one go. Periodic reviewing of the operating cycle helps in pinpointing the risks areas. While negotiating with the clients (be it buyer or seller), the risk exposure before execution of the transaction should be understood. Thus the level of hedging can be determined accordingly. **Transaction risks** occur due to time gap between the commitment of the contract and actual cash flows.

More often than not, these risks are easier to manage as they can he hedged using financial derivative instruments. Thus understanding the quantum to hedge is important. Formulating a corporate policy is easy but to review it periodically is the key with the ever changing **foreign exchange markets**.

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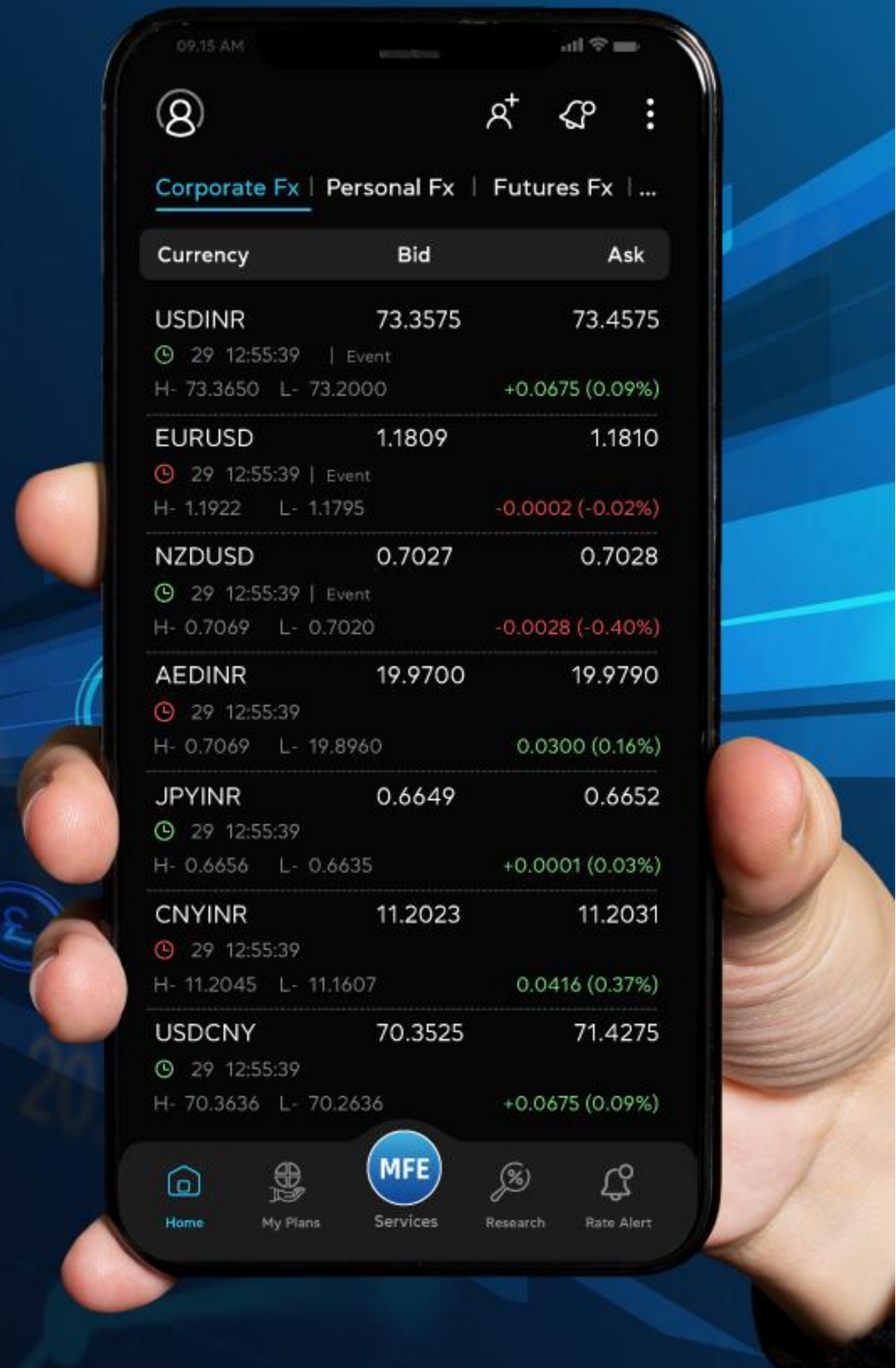

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