Economics

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The Two-day fallout

The sudden devaluation of the renminbi on 11th August 2015 has had repercussions across countries in terms of impact on currencies where there has been considerable volatility. The response may be considered to be more than temporary as central banks all over would be monitoring the permanency of such depreciation in the renminbi before taking any action through intervention.

The Table below provides information on how some major currencies have moved between Monday the 10th and Wednesday the 12th – i.e. over two trading sessions. China had devalued the renminbi on Tuesday by 1.9% after which most currencies have also moved downwards. In the table, a positive change should be read as depreciation and negative change as appreciation.

Table 1: Movement of currencies (Relative to USD)

	8/10/2015	8/11/2015	8/12/2015	% Change
Euro	*0.9096*	*0.9058*	*0.8931*	*-1.8118*
Argentina	9.2138	9.2202	9.2335	0.2138
Australia	1.3506	1.3724	1.3557	0.3776
Brazil	3.4705	3.5108	3.4724	0.0547
Britain	*0.6433*	*0.6422*	*0.6394*	*-0.6016*
Canada	*1.3056*	*1.3148*	*1.2973*	*-0.6357*
China	6.2083	6.3242	6.3875	2.8865
Hong Kong	7.7530	7.7629	7.7560	0.0387
India	63.7810	64.3560	64.8000	1.5977
Indonesia	13,600	13,555	13,801	1.4779
Japan	*124.5800*	*124.8600*	*123.9100*	*-0.5378*
Malaysia	3.9290	3.9614	4.0389	2.7971
Mexico	16.1560	16.3350	16.2980	0.8789
Philippines	45.8110	46.1660	46.1510	0.7422
Russia	63.2560	64.3560	64.2860	1.6283
South Africa	12.6760	12.8020	12.7690	0.7337
Korea	1162.6000	1182.4000	1175.1000	1.0752
Taiwan	31.6510	32.1620	32.1430	1.5545
Thailand	35.1060	35.3920	35.2530	0.4187
Turkey	*2.7856*	*2.7809*	*2.7702*	*-0.5528*

Source: Pacific Exchange Rate Services

As can be seen from the table:

1. Most of the developed countries have witnessed appreciation in their currencies vis-à-vis the dollar. Turkey is one of the few emerging markets that have witnessed appreciation.

2. Coincidentally the developed countries that have witnessed appreciation like Euro region or UK or Japan were the ones which have been pursuing quantitative easing over the years which in turn has weakened their currencies through the natural course.
3. The currencies that have declined sharply are those of Malaysia by 2.7% which is even more than that of China followed by Russia (1.6%), India (1.6%), Taiwan and Indonesia.

Implications for India

1. Just at the time the rupee looked stable, there is turbulence once again from an external force.
2. Imports would tend to become cheaper from China which can affect domestic production of companies in areas like metals, electronics, auto parts, textiles etc.
3. To retain export competitiveness to the extent possible, the rupee must also decline. It may be pointed out here that since 2013 onwards when the RBI took corrective measures to steady the rupee, our currency has performed better than those of other emerging markets. There are definitely signs of competitive depreciations across countries – driven currently by market forces and not governments or central banks.
4. The markets are going to keep guessing the RBI's intervention and action and hence the rupee will be volatile. A lot depends on when the depreciation of the renminbi stops and at what level it stabilizes. Market believes 6.6-6.7 renminbi to a dollar could be the rate.
5. With CPI inflation also coming less than 4% there can be reason to expect the RBI to cut rates now as the external factor of Fed raising rates has receded with the Fed also expected to defer their plans. Earlier it was felt that the RBI would not lower rates as this could deter FII flows. But in the present situation, a depreciation of the rupee would be welcome.
6. Based on developments so far, the expectation is that in the absence of clear intervention from the RBI the exchange rate will be in the range of Rs 64.5-65.25 – however, the view will change depending on the way the renminbi goes.

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