

## A Happy New Year for Re as RBI's Focus to Shift to Growth

### Central bank likely to bring down short-term policy rates

The rupee is expected to regain some of its lost ground in 2012. Reserve Bank of India's shift in focus from fighting inflation to promoting growth will support the exchange rate this year. RBI is also expected to bring down the short-term rates to ensure that the economy's faltering growth gets a leg up, making it attractive for foreign institutional investors (FIIs) to invest in India.

Currency expert and founder of Mumbai-based treasury risk management consultant Mecklai Financial, Jamal Mecklai, said, "It is a happy New Year for the rupee. The blood bath on the currency is over. It is not going to get worse than this. Inflation is going to be lower and the focus of both the government and the RBI will be on growth."

The rupee closed at 53.08/09 to the dollar on the last trading day of calendar year 2011, marginally down from Thursday's close of 53.07/08. During 2011, the rupee fell 15.8 per cent, compared with a fall of 19.1 per cent during the global financial crisis in 2008. The rupee hit a all time low of 54.3 on December 15, forcing the RBI to impose restrictions on banks' trading limits to help rein in speculation in forward markets.

Ashutosh Khajuria, associate vice-president treasury at Federal Bank, said, "RBI's pro-growth monetary policy stance in the coming quarters and the lower inflation levels may attract more capital inflows in the country. But the Indian economy is saddled with a \$220 billion trade deficit this financial year. The higher fiscal deficit at over 5.6 per cent of GDP is also a big dampener. But the government will sort that problem out in the budget." The euro zone treaty that may be signed in February will ensure fiscal discipline of the euro zone countries and may result in the resolution of their problem. Under this treaty, all governments are expected to get fiscal targets and a breach of the targets will attract sanctions against these countries.

Harihar Krishnaswamy, head of treasury at South African bank First Rand, said, "The euro zone treaty, if implemented in the current framework, will resolve the debt crisis in the region. Much of the uncertainties of the global economy will vanish if the euro debt issue is settled, resulting in FIIs investing back into emerging economies like India."

"However, the Banglad-eshi taka or the Sri Lankan and the Pakistani currencies have not been depreciating, which is a good sign and that means India's problem is more internal like the slow movement on the reforms front or the issues relating to corruption than a regional malaise," said Khajuria.

Much of the slide in the value of the rupee in 2011 came after senior RBI officials, like deputy governor Subir Gokarn, talked down the rupee by saying that the firepower available with the central bank is limited and they would not interfere with the exchange rate except to stem its volatility. What Gokarn meant was that the forex reserves of \$300.86 billion is too meagre an ammunition available with the RBI to protect the exchange rate.

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“Even if that was the case the central bank should never say that it will be indifferent to the levels of the exchange rate. This resulted in the offshore rupee market (non-deliverable forward market) speculation on the rupee gaining momentum. When that reaches a particular level, the domestic rate also reaches that level in a few trading days. Now, the RBI officials have realised that caution on their statements is as important as the action in the market,” said a senior economist who did not want to be identified.

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*<http://www.mydigitalfc.com/policy/happy-new-year-re-rbi%E2%80%99s-focus-shift-growth-183>*