Currency Risk Management Report

(for the week ended May 22, 2015)

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RISK MANAGEMENT CONSULTANTS
Forex, Interest Rates & Derivatives

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NEWS

1. On the international foreign exchange markets, the US dollar strengthened across the board against its major international trading partners this week. It strengthened the most (3.8%) against the Euro and the Danish krona, by 3% against the Swiss franc, 2.5% against the Australian $, by 2.2% against the Canadian $, 2% against the Yen, 1.5% against the Pound and by 1.2% against the Singapore $.
2. The average number of Americans filing for unemployment benefits dropped to a 15-year low, as the four-week moving average for jobless claims decreased to 266,250. The number of people continuing to receive jobless benefits fell marginally to 2.2 million, the lowest level since 2000. However, the US economy remains on a modest growth path in the second quarter of 2015, with home sales dropping in April and manufacturing activity contracting in May, as growth struggles to rebound after the slumping at the start of the year.
3. Euro zone's flash manufacturing PMI for the month of May jumped to a 13-month high of 52.3 but services PMI dropped to a 4-month low of 53.3, sending mixed signals to the financial markets about recovery in the region. Germany seems to be more affected than its peers by the growth weakness in the US and China. The latter's manufacturing index grew less than expected in May.
4. Britain's consumer price inflation fell below zero for the first time in half a century as prices fell 0.1% in April, compared to a year ago period. Food prices fell 3% and fuels and lubricants fell 12.3% as BoE Governor Mark Carney said that "*any period of falling prices will be temporary*" and that he "*expected a pick-up in inflation by the end of this year*". Separately the Office of National Statistics announced that producer prices were down almost 2% over the year, while input prices collapsed 11.7% primarily driven by the oil price drop. Separately, house prices accelerated to 9.6% in March from 7.4% in February.
5. Japan's economy grew during the first three months of 2015 by an annualized 2.4% (better than the market expectations of 1.5%), led by the fact that Japanese businesses are starting to increase their spending and manufacturing in their own country. Corporate spending increased by 0.4% at the same time, being buoyed by a weaker Yen, which is making manufacturing abroad more expensive. However, much of the fillip to growth has come in the form of increased inventories that have added close to 0.5% points to the non-annualized expansion in the first quarter.
6. On the domestic interbank market, the rupee-dollar exchange rate traded in the range of Rs 63.46-63.89 per $ and the rupee ended the week with a loss of 2 paise to close at Rs 63.53 per $. The forward premia levels across maturities of 1-month, 3-month, 6-month and 12-month stood at 7.82%, 7.56%, 7.44% and 6.73% p.a. as against 7.78%, 7.56%, 7.48% and 6.88% respectively in the previous week. RBI's foreign exchange reserves as on the week ended May 15, 2015 stood at $353 billion (swelling by a $1.75 billion during over the previous week).

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VIEWS

1. The recent episode of rupee weakness, which saw the domestic currency drop all the way to around Rs 64.28 per $ before recovering, has once again given a fillip to the argument that the rupee is over-valued in real terms and that its strength is to blame for the fall in India's exports. A closer look at the disaggregated data however, reveals that such a prognosis is simplistic at best. The category of 'manufactured goods' in our export basket, is one of the most sensitive items to exchange rate fluctuations, and the fact that it has grown 14% over 2014-15 (by an absolute amount of $9 billion) indicates that a strong rupee cannot be solely blamed for the falling gross exports. Moreover, textile exports, which are also exchange rate sensitive owing to being highly labor intensive, have grown 12% over FY 2013-14. The drop in exports is primarily driven by oil exports, reflecting the sharp drop in international prices. As far as imports are concerned, the malaise seems to lie in the fact that substantial jumps were seen in both gold imports (20%) and electronic goods' imports (15%). A contributory factor has also been imports of iron ore, traditionally an export item, due to the closure of mines in Goa.

2. Service export numbers for the last quarter of FY 2014-15 suggest that we are likely looking at a current account surplus of $5-7 billion for the last three months and a current account deficit (CAD) to the tune of $20-22 billion for the year as a whole. This would be less than 1% of GDP. Such a low CAD once again brings to the fore a fundamental issue in respect of our Balance of Payments – should we not be increasing imports of capital goods in order to secure a better growth rate for the future? After all, the CAD also reflects the excess of domestic investments over domestic savings. If we continue to attract large capital inflows, should we not be increasing investments instead of mindlessly adding to forex reserves?

3. We expect the rupee to stabilize around the Rs 63-63.50 per $ level in the coming week, and thereafter may even drift towards Rs 62.50. This could be undermined by unfavorable international events, which could take it beyond the Rs 64 per $ mark. While the markets seem to have factored in a 25 basis point repo rate reduction on the June 2 monetary policy meeting, forward premia levels could see some amount of softening. The current levels are attractive for exporters to lock their medium (and even long term) receivables through forwards, while importers should continue to leave their medium and long term exposures un-hedged while keeping a pre-determined stop loss level.

4. The threat looming on the financial markets is that of Greece exiting the euro zone. The endless games between the Greek politicians and the troika negotiating the debt restructuring only seem to be postponing the inevitable. Policymakers on both sides of the divide are now working on the possibility of Greece staying within the euro zone, even after staging a technical default on its debts, most of which comes due by the end of next month. However, as the German Finance Minister has warned, "*Countries can stumble into a crisis.*" The currency is likely to remain volatile for the coming weeks, if not months. We are keeping our ranges for the non-dollar currencies unchanged, as follows:

   $1.48 – 1.60 per GBP
   $1.08 – 1.18 per EUR and
   JPY112 – 122 per $

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May 22, 2015

CRMR

DOMESTIC MARKETS

FOREIGN EXCHANGE MARKETS

SPOT EXCHANGE RATES

	INR/Currency
USD	63.53
PDS	98.41
EUR	69.97
YEN (100)	52.27
SFr	67.33
DKK	9.38
CAD	51.74
AUD	49.70
SGD	47.53
CNY	10.25

FORWARD EXCHANGE RATES

Month-end	INR/USD	Premium % p.a.
May-15	63.58	5.75
Jun-15	64.00	7.72
Jul-15	64.40	7.35
Aug-15	64.80	7.52
Sep-15	65.19	7.37
Oct-15	65.57	7.35
Nov-15	65.95	7.38
Dec-15	66.33	7.27
Jan-16	66.69	7.25
Feb-16	67.06	7.25
Mar-16	67.43	7.18
Apr-16	67.81	7.20

CURRENCY SWAPS

	2-Year	5-Year
`/USD	6.96	7.04

INR/USD CURRENCY OPTIONS*

	1-mth Option on USD 1, price in paise	
Strike	Call	Put
63.00	-	17
63.50	-	33
64.00	-	57
64.50	33	-
65.00	20	-
65.50	14	-

	3-mth Option on USD 1, price in paise	
Strike	Call	Put
64.00	-	63
64.50	-	85
65.00		112
65.50	67	-
66.00	53	-
66.50	41	-

INTEREST RATE MARKETS

	2-Year	5-Year	10-Year
GOI BOND	7.84	7.86	7.86

INTEREST RATE SWAPS

	2-Year	5-Year
OIS	7.21	7.10
MIOCS	6.96	7.04

INTERNATIONAL MARKETS

FOREIGN EXCHANGE MARKETS

SPOT EXCHANGE RATES

	Against USD
PDS	1.5490
EUR	1.1013
YEN	121.54
SFr	0.9435
DKK	6.7711
CAD	1.2279
AUD	0.7823
SGD	1.3366
PKR	101.92
CNY	6.1974

PDS 3mnth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
1.53	3.79	2.00
1.55	2.82	2.82
1.57	1.95	3.95

EUR 3mnth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
1.08	3.76	1.56
1.10	2.53	2.53
1.12	1.68	3.68

YEN 3mnth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
123.49	2.14	0.87
121.49	1.43	1.43
119.49	0.83	2.28

INTEREST RATE MARKETS

	OFFSHORE CURRENCY			
	1 MONTH	3 MONTH	6 MONTH	12 MONTH
USD	0.18	0.28	0.41	0.72
EUR	-0.07	0.00	0.04	0.15
PDS	0.52	0.55	0.71	0.99
YEN	0.07	0.10	0.15	0.23
SwFr	-0.79	-0.75	-0.78	-0.62

	INTEREST RATE SWAPS		
	2-Year	5-Year	10-Year
USD	0.96	1.88	2.32
EUR	0.07	0.42	0.90
PDS	0.96	1.58	2.00
YEN	0.12	0.33	0.72
SwFr	-0.71	-0.15	0.32

OTHER MARKETS

COMMODITIES		EQUITY INDICES	
NYMEX crude ($/barrel)	59.0	DJIA	18,232
GOLD ($/ounce)	1,206	FTSE	7,031
COPPER ($/ton)	6,197	DAX	11,815
ALUMINIUM ($/ton)	1,725	NIKKEI	20,264

Information herein is believed to be reliable, but AVRCO does not warrant its completeness or accuracy

** indicative only*

 # for payables

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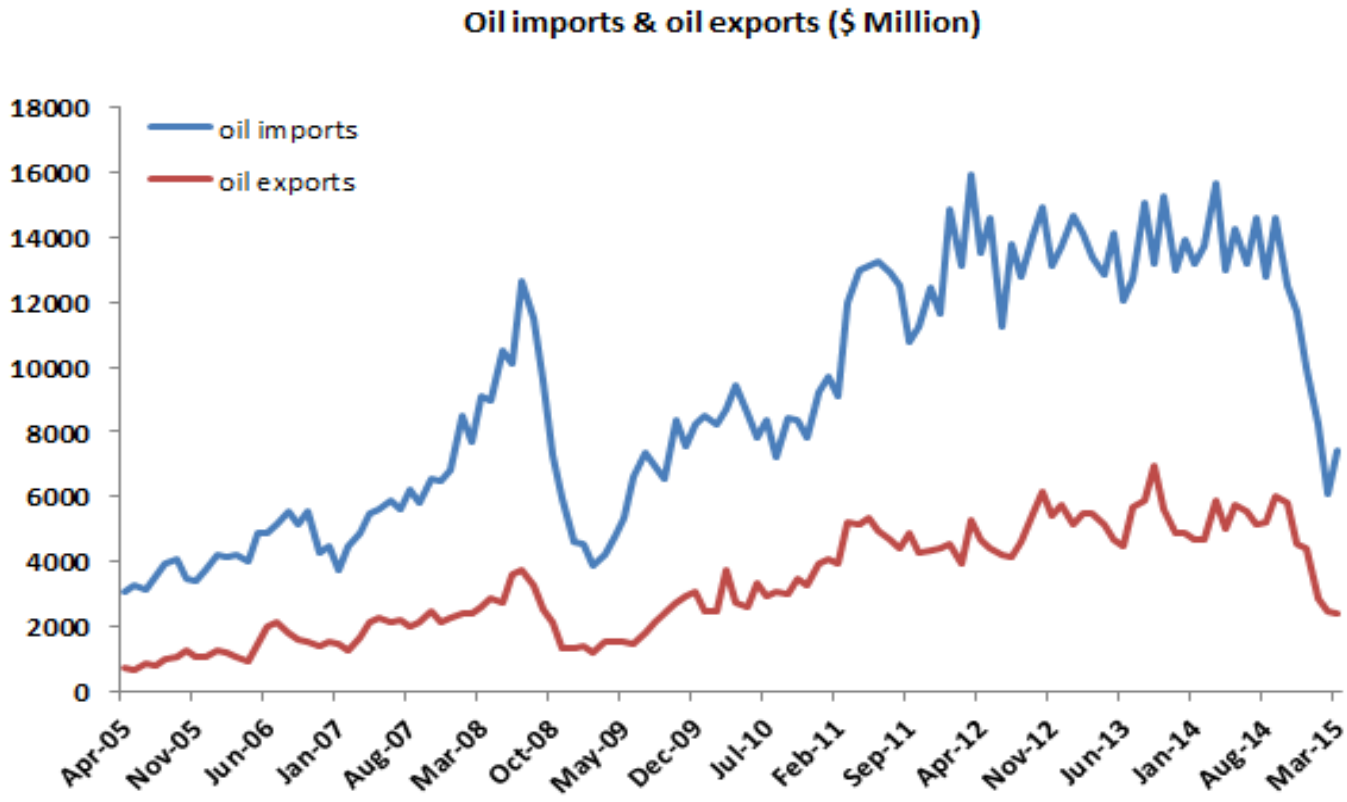

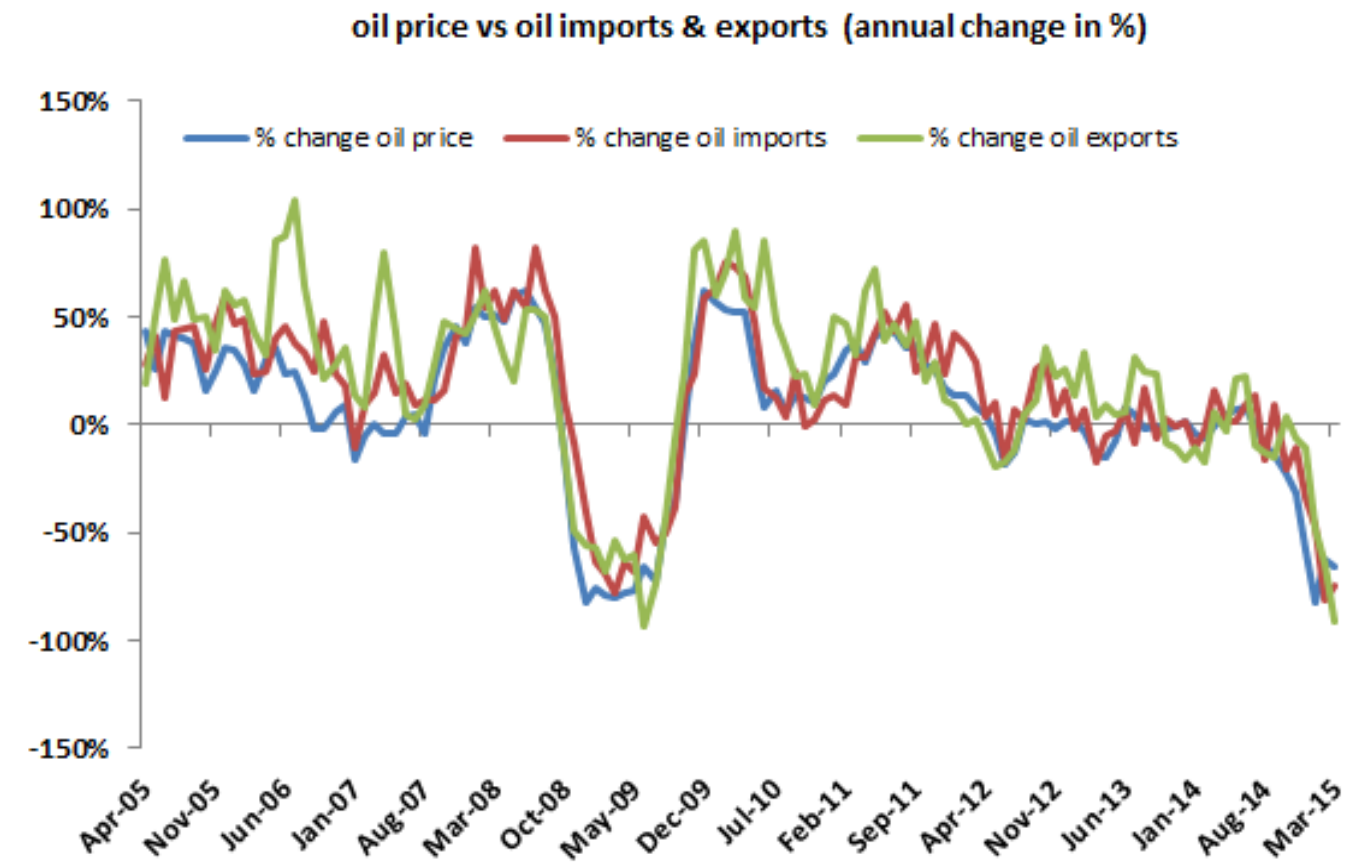

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