

NEWS

1. The US\$, which largely strengthened against most of its international trading partners during the week, touched 3-month highs against both the Euro and the Pound. It strengthened the most (by 1.5%) against the Japanese Yen, followed by 1.2% against both the Swiss Franc and the Danish Krona. It also gained against the Euro (1.2%), the Pound (0.7%), Canadian \$ (0.4%) and the Singapore \$ (0.3%).
2. Jobless claims in the US fell by 14,000 to 298,000 for the week and the number of people on jobless benefits dropped by 49,000 to 2.5 million. This is the lowest number of benefit seekers recorded since June 2007. Consumer prices advanced in July at their slowest pace since February, an indication of softened inflation pressures that might just give the Fed more flexibility in deciding its interest rate stance.
3. In the Euro zone, the preliminary estimate for purchasing managers' index (PMI) for the manufacturing sector fell to a 13-month low of 50.8 in August, from 51.8 in July. The composite indicator of the manufacturing and services industries dropped to 52.8 from 53.8 in July. The disappointing numbers have come on the back of stagnating growth in the three largest economies of the region. Meanwhile, the European Union (EU) has agreed to disburse €125 Mn (approx. \$170 Mn) in the form of emergency compensation to vegetable growers hit by Russia's ban on imported food items from the EU.
4. Private consumption in Japan has dropped by a sharp 5% from the previous quarter. Despite the Bank of Japan buying government bonds worth billions of Dollars, Abenomics (a combination of fiscal profligacy, loose monetary policy and a weak exchange rate) has not yet succeeded in igniting real wages, which have fallen by 3.2% over the year. Meanwhile, the latest trade numbers suggest that the cheaper yen has had a greater

impact in fuelling the nation's oil import bill rather than providing a big fillip to exports.

5. HSBC's China manufacturing PMI fell to 50.3 in August, from an 18-month high of 51.7 seen in May. Even though growth in exports has somewhat managed to cushion the impact of a domestic slowdown, long-term borrowings for capex and construction have continued to decelerate (they stand at 15% on the year as compared to 17.5% at the end of 2013) despite monetary easing.
6. On the domestic interbank market, the rupee-dollar exchange rate traded in the range of Rs 60.38 – Rs 60.88 per \$, ending the week with a gain of 29 paise for the rupee to close at Rs 60.48 per \$. The forward premium levels across maturities of 1-month, 3-month, 6-month and 12-month are 8.74%, 8.43%, 8.49% and 7.74% respectively as against 8.18%, 8.31%, 8.42% and 7.82% in the previous week.

VIEWS

1. On the international front, the most influential people in global finance, including central bankers and other policy makers, met on Friday at Jackson Hole primarily to discuss the state of the world economy and the possibility of an exit strategy from what has culminated into a massive phase of liquidity. Chairperson Janet Yellen's speech was expectedly two-handed as she spoke about recovery in the labor market as well as underutilization of work force, in the same breath.
2. With the Fed's quantitative easing (QE3) program set to end in a month or two, market focus is increasingly shifting to the timing and extent of an interest rate hike next year. The Fed Chairperson will be on a tightrope walk, since there is a need to shrink the size of the Fed's balance sheet (which is expected to grow by over 5 times between 2008 and 2014 to \$ 4.4 trillion). Clearly, it cannot contemplate simultaneously an increase in interest rates and tightening liquidity through reducing its assets, and will therefore keep a keen watch on inflation over the next few years. As long

as inflation remains low, it would give priority to asset sale rather than moving interest rates higher. However, there does not appear to be at present a concrete road map in the face of what Alan Greenspan has called “*an unprecedented era in international economics*”.

3. The prevalence of near-zero interest rates in the world’s biggest economies has led to unusual placidity in the FX markets in the past few months. Floating exchange rates have shown uncharacteristic stability as volatility (measured by the JP Morgan global currency volatility index) has dropped near its lowest level in close to two decades.
4. In the international forex markets, the British pound has been on a weakening streak for the seventh consecutive week, its longest losing momentum since September 2008. We expect that the major non-USD currencies will remain in their projected bands as given below:
\$ 1.62 – 1.72 per GBP,
\$ 1.32 – 1.42 per EUR, and
JPY 95 – 105 per \$.
5. The sudden drop in global oil prices has been almost inexplicable. On the demand-side, while this may be a subtle indication of growth slowing down in the biggest oil importing countries (significantly China), it augurs well for India’s oil import bill. It could also lend the government, some space to get rid of the diesel subsidy even while not increasing prices. No doubt, this is a happy event for India both on the balance of payments and the inflation rate. Each dollar’s fall in the Brent oil price means a monthly reduction of \$ 825 mn in our net oil imports, while a \$ 1 drop also means a reduction of about 75 paise per litre in the price (or subsidy) of petroleum products.
6. No change in our rupee script. On the back of a likely large Balance of Payments surplus, we expect the rupee-dollar exchange rate to drift towards Rs 60 per \$. We therefore continue to advise exporters to hedge the bulk of their net receivables. Importers should hedge exposures using out-of-the-money option contracts.

DOMESTIC MARKETS

FOREIGN EXCHANGE MARKETS

SPOT EXCHANGE RATES

	INR/Currency
USD	60.48
PDS	100.23
EUR	80.09
YEN (100)	58.18
SFr	66.19
DKK	10.74
CAD	55.27
AUD	56.35
SGD	48.42
CNY	9.83

FORWARD EXCHANGE RATES

Month-end	INR/USD	Premium % p.a.
Aug-14	60.52	4.53
Sep-14	60.98	8.66
Oct-14	61.42	8.34
Nov-14	61.81	8.36
Dec-14	62.27	8.37
Jan-15	62.70	8.43
Feb-15	63.09	8.42
Mar-15	63.53	8.47
Apr-15	64.00	8.53
May-15	64.38	8.46
Jun-15	64.78	8.43
Jul-15	65.16	8.28

CURRENCY SWAPS

	2-Year	5-Year
*/USD	8.08	8.11

INR/USD CURRENCY OPTIONS*

1-mth Option on USD 1, price in paise		
Strike	Call	Put
60.00	106	14
60.50	71	29
61.00	44	51
61.50	26	83
62.00	15	122
62.50	9	165

3-mth Option on USD 1, price in paise		
Strike	Call	Put
62.00	81	101
62.50	63	131
63.00	48	165
63.50	36	203
64.00	27	243
64.50	20	285

INTEREST RATE MARKETS

	2-Year	5-Year	10-Year
GOI BOND	8.54	8.56	8.51

INTEREST RATE SWAPS

	2-Year	5-Year
OIS	8.11	8.03
MIOCS	8.08	8.11

INTERNATIONAL MARKETS

FOREIGN EXCHANGE MARKETS

SPOT EXCHANGE RATES

	Against USD
PDS	1.6572
EUR	1.3242
YEN	103.95
SFr	0.9138
DKK	5.6300
CAD	1.0943
AUD	0.9317
SGD	1.2491
PKR	101.10
CNY	6.1528

PDS 3mth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
1.64	2.77	1.19
1.66	1.88	1.88
1.68	1.06	3.06

EUR 3mth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
1.30	2.99	0.55
1.32	1.46	1.47
1.34	0.69	2.69

YEN 3mth CURRENCY OPTIONS*

(Prices in US cents)		
Strike	Call	Put
105.92	2.32	0.55
103.92	1.24	1.24
101.92	0.52	2.46

INTEREST RATE MARKETS

OFFSHORE CURRENCY

	1 MONTH	3 MONTH	6 MONTH	12 MONTH
USD	0.16	0.23	0.33	0.56
EUR	0.07	0.15	0.25	0.41
PDS	0.50	0.56	0.70	1.05
YEN	0.09	0.13	0.18	0.33
SwFr	0.00	0.02	0.08	0.20

INTEREST RATE SWAPS

	2-Year	5-Year	10-Year
USD	0.71	1.80	2.56
EUR	0.32	0.58	1.21
PDS	1.27	2.03	2.57
YEN	0.21	0.30	0.67
SwFr	0.09	0.30	0.91

OTHER MARKETS

COMMODITIES		EQUITY INDICES	
NYMEX crude (\$/barrel)	93.4	DJIA	17,001
GOLD (\$/ounce)	1,281	FTSE	6,775
COPPER (\$/ton)	7,088	DAX	9,339
ALUMINIUM (\$/ton)	2,055	NIKKEI	15,539

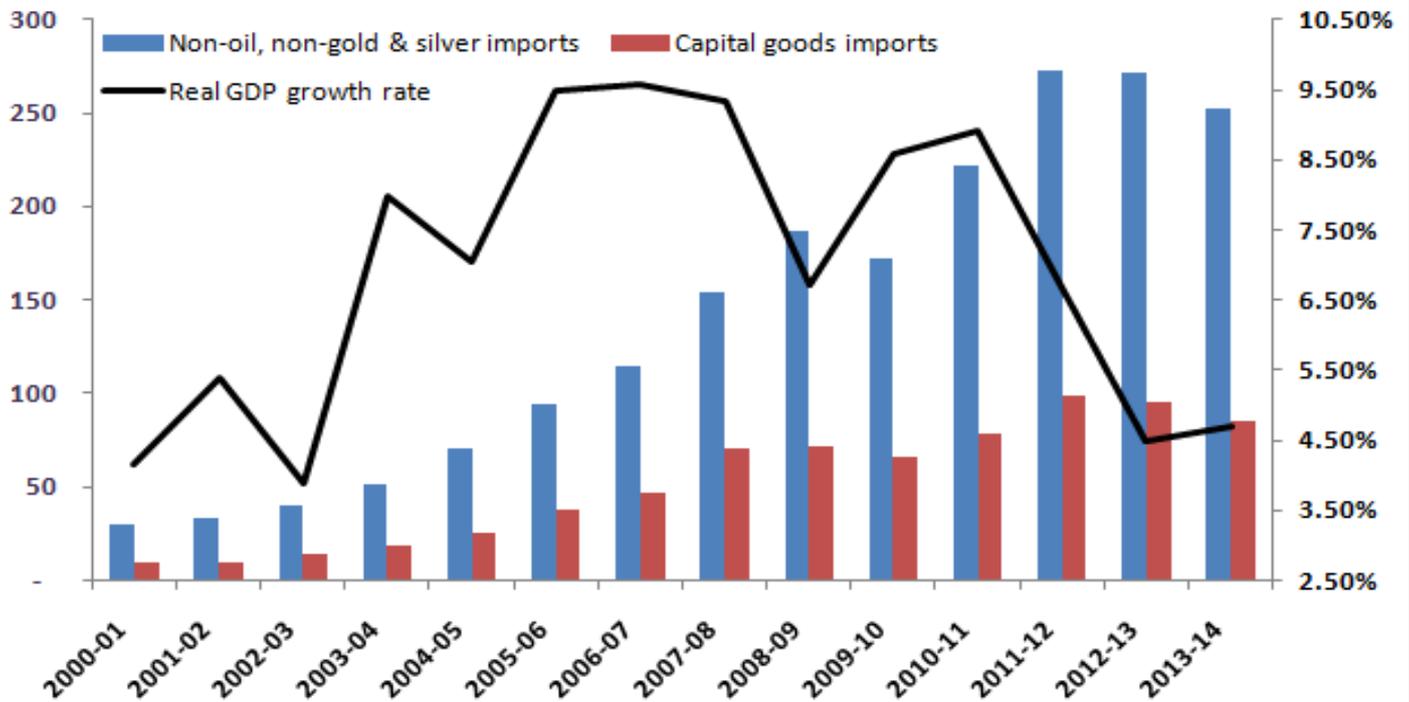
Information herein is believed to be reliable, but AVRCO does not warrant its completeness or accuracy

* indicative only

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India-key imports (USD Bn) and GDP growth



Non-oil, non-gold & silver imports as % Total imports
Capital goods imports as % Total imports

