

FOREIGN EXCHANGE RATE POLICY

6.84 The foreign exchange rate policy in recent years has been guided by the broad principles of careful monitoring and management of exchange rates with flexibility, without a fixed or a pre-announced target or a band, while allowing the underlying demand and supply conditions to determine the exchange rate movements over a period in an orderly manner. Subject to this predominant objective, the Reserve Bank of India's intervention in the foreign exchange market has been driven by the objectives of reducing excess volatility, maintaining adequate level of reserves, and developing an orderly foreign exchange market.

6.85 In the year 2006-07, the average annual exchange rate of rupee was 45.25 per US dollar, Rs 85.64 per pound sterling, Rs 58.05 per euro and Rs

38.73 per 100 yen. During the fiscal 2007-08, due to high capital inflows, the rupee appreciated against major international currencies. The appreciation was 12.4 per cent against the US dollar (Rs 40.26 per dollar), 6.0 per cent against pound sterling (Rs 80.83 per pound sterling), 1.8 per cent against euro (Rs 57.06 per euro) and 9.6 per cent against Japanese yen (Rs 35.35 per 100 yen).

6.86 In the fiscal 2008-09, however, the rupee depreciated against major international currencies, except pound sterling, due to deceleration in capital flows and widening trade deficit. The annual average exchange rate was Rs 45.99 per US dollar, Rs 64.98 per euro and Rs 46.22 per 100 yen, indicating depreciation by 12.5 per cent, 12.2 per cent and 23.5 per cent respectively in 2008-09. The rupee appreciated by 3.2 per cent against pound sterling (Rs 78.29 per pound sterling).

Table 6.19 : Exchange rates and RBI's sale/purchase of foreign currency in exchange market, 2008-09

Month	Monthly average exchange rates (Rupee per foreign currency)*,				RBI Net sale (-) / purchase (+) US\$ million
	US\$	Pound	Euro	Yen**	
April 2008	40.02 (0.8)	79.20 (2.0)	63.03 (-0.6)	38.93 (3.0)	(+) 4325
May 2008	42.13 (-5.0)	82.74 (- 4.3)	65.55 (- 3.9)	40.41 (- 3.7)	(+) 148
June 2008	42.82 (-1.6)	84.11 (-1.6)	66.57 (-1.5)	40.07 (0.9)	(-) 5229
July 2008	42.84 (-0.04)	85.17 (- 1.3)	67.56 (- 1.5)	40.15 (- 0.2)	(-) 6320
August 2008	42.91 (-0.2)	81.34 (4.7)	64.45 (4.8)	39.34 (2.1)	(+) 1210
September 2008	45.56 (-5.8)	82.06 (-0.9)	65.55 (-1.7)	42.74 (-8.0)	(-) 3784
October 2008	48.66 (-6.3)	82.65 (-0.7)	64.84 (1.1)	48.57 (-12.0)	(-) 18666
November 2008	49.01 (-0.7)	75.18 (9.9)	61.67 (5.1)	51.15 (-5.0)	(-) 3101
December 2008	48.63 (0.8)	72.56 (3.6)	65.67 (-6.1)	53.30 (-4.0)	(-)318
January 2009	48.79 (-0.3)	70.77 (2.5)	65.10 (0.9)	54.04 (-1.4)	(-) 29
February 2009	49.26 (-1.0)	70.83 (-0.1)	62.89 (3.5)	53.47 (1.1)	(+) 230
March 2009	51.23 (-3.8)	72.90 (-2.9)	66.92 (-6.0)	53.51 (1.8)	(-) 3388
Average 2008-09	45.99 (-12.5)	78.29 (3.2)	64.98 (-12.2)	46.22 (-23.5)	

Source : RBI

* FEDAI indicative rate;

** Per 100 Yen Figures in parentheses indicate appreciation (+) and depreciation (-) over the previous month/year.

6.87 The month-to-month movement of exchange rate in the year 2008-09 indicated that the rupee depreciated against the US dollar in May-June 2008 but remained almost stable during July-August 2008. It depreciated sharply against the US dollar during September-October 2008 (Rs 45.6 in September 2008 and Rs 48.7 in October 2008) and moved in a narrow range of Rs 48.6 to Rs 49.3 during November 2008-February 2009. The rupee however recorded a depreciation of 3.8 per cent to Rs. 51.2 in March 2009.

6.88 The daily movement of exchange rate during 2008-09 revealed that the rupee/US dollar exchange rate, which was Rs 40.4 per dollar at end March 2008, crossed Rs 50.1 per US dollar mark on October 27, 2008 and depreciated further to Rs 52.1 per dollar on March 5, 2009, before recovering to Rs 50.2 per dollar on March 20, 2009. The rupee depreciation during 2008-09 reflected mainly the supply-demand imbalance in the foreign exchange market, which widened significantly during September-October 2008, as a fallout of the global crisis. This led RBI to

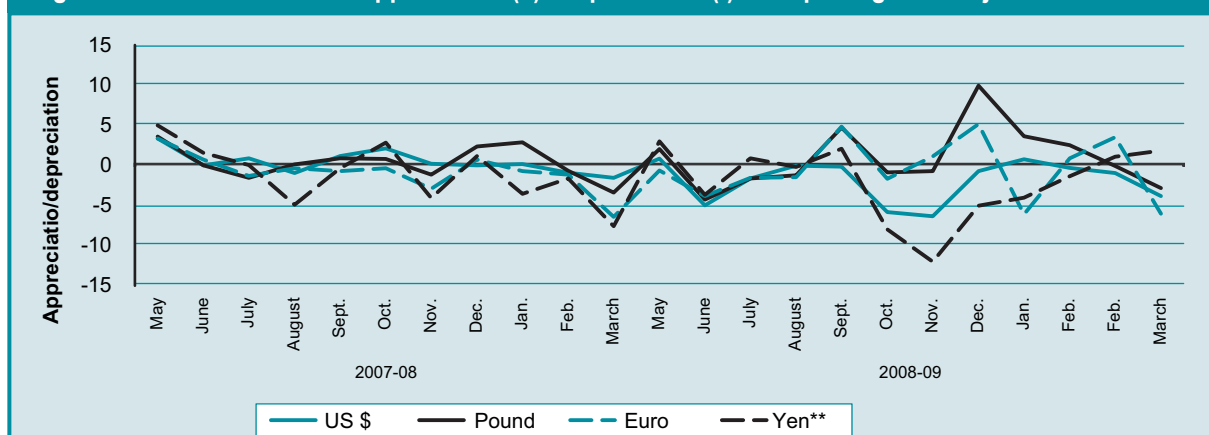
augment supply of dollars to stabilize the rupee in the foreign exchange market (Table 6.19).

6.89 Movement in exchange rate of rupee vis-à-vis major international currencies during 2007-08 to 2008-09, month-wise is presented in Figure 6.5.

6.90 The exchange rate of rupee vis-à-vis select international currencies since 1980-81, year-wise, and during 2008-09, month-wise, is indicated at Appendix 6.5.

6.91 The indices of nominal effective exchange rate (NEER) and real effective exchange rate (REER) is used as indicators of external competitiveness of the country over a period of time. NEER is the weighted average of bilateral nominal exchange rates of the home currency in terms of foreign currencies. REER is defined as a weighted average of nominal exchange rates adjusted for relative price differential between the domestic and foreign countries. REER captures movements in cross-currency exchange rates as well as inflation differential between India and its major trading partners. RBI has been

Figure 6.5 : Month on month appreciation (+) / depreciation (-) of Rupee against major currencies



constructing six currency (US dollar, euro for eurozone, pound sterling, Japanese yen, Chinese renminbi and Hong Kong dollar) and 36 currency indices of NEER and REER.

6.92 While the rupee has depreciated against the US dollar by 12.5 per cent, the rupee depreciation against the six-currency trade-weighted NEER was modest during 2008-09. The average six-currency trade-weighted REER (base:1993-94=100) at 114.09 in 2007-08 indicated an overvaluation of rupee by 14.1 per cent in real terms. REER declined from 112.16 in April 2008 to 95.65 in March 2009 mainly on account of significant depreciation of the rupee against US dollar, euro and Japanese yen. The sharp

decline in inflation rate in recent months has also contributed towards the correction in overvaluation of the rupee (Table 6.20 and Appendix 6.6)

6.93 In the international market, the US dollar appreciated against most of the other major international currencies as the U.S. investors were liquidating their investment in overseas equity and bonds and repatriating the money back to the United States as direct fallout of the global economic slowdown. Notwithstanding the deepening of financial crisis and weakening in economic activity after the collapse of the Lehman Brothers in mid-September 2008, the flight to safety considerations facilitated strengthening of

Table 6.20 : Movement of rupee and indices of NEER and REER during 2008-09

Month/Year	Rs per US dollar	Appreciation (+)/depreciation (-) in Rs per dollar over previous month	NEER *	REER *	Appreciation (+)/depreciation (-) in NEER over previous month	Appreciation (+)/depreciation (-) in REER over previous month
2007-08 (April March)	40.26		74.17	114.09		
2008-09						
April 2008	40.02		70.63	112.16		
May 2008	42.13	-5.0	67.48	108.23	-4.5	-3.5
June 2008	42.82	-1.6	66.38	108.20	-1.6	-0.03
July 2008	42.84	-0.04	65.83	107.94	-0.8	-0.2
August 2008	42.91	-0.2	67.22	111.30	+2.1	+3.1
September 2008 (P)	45.56	-5.8	64.46	107.11	-4.1	-3.8
October 2008 (P)	48.66	-6.4	62.08	102.36	-3.7	-4.4
November 2008 (P)	49.01	-0.7	63.06	102.80	+1.6	+0.4
December 2008 (P)	48.63	0.8	62.12	100.18	-1.5	-2.6
January 2009 (P)	48.79	-0.3	62.28	99.64	+0.3	-0.5
February 2009 (P)	49.26	-1.0	62.80	99.87	+0.8	+0.2
March 2009 (P)	51.23	-3.8	60.18	95.65	-4.2	-4.2

Source : RBI

* 6-Currency Trade Based Weights- Base: 1993-94 (April-March) =100

Table 6.21 : Exchange rate of US dollar against international currencies

Month/Year	GBP/US\$	Euro/US\$	US\$/JPY
March 2008	1.9885	1.5812	100.10
April 2008	1.9668	1.5540	104.08
May 2008	1.9735	1.5508	105.66
June 2008	1.9917	1.5764	106.40
July 2008	1.9805	1.5611	107.99
Aug 2008	1.8128	1.4716	108.31
Sept 2008	1.8161	1.4395	105.87
Oct 2008	1.6076	1.2726	98.46
Nov 2008	1.5380	1.2705	95.57
Dec 2008	1.4626	1.3978	90.60
Jan 2009	1.4435	1.3409	90.87
Feb 2009	1.4322	1.2668	97.63
March 2009	1.4327	1.3249	98.84
US\$ Appreciation (+) / Depreciation (-) (End March 2008– End March 2009)	38.8	19.3	- 1.3

Source : RBI

the US dollar. During 2008-09, the US dollar appreciated against the euro and the pound sterling; however, it depreciated against the Japanese yen. The exchange rate of US dollar vis-à-vis other major international currencies, viz., pound sterling, euro, and Japanese yen is presented in Table 6.21.