WHY RUPEE VALUE DEPRECIATING IN COMPARISON TO THE US DOLLAR?

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ABSTRACT

In this article, the effects of the recent rupee depreciation versus the dollar on the Indian economy have been examined. The data is collected through secondary sources. The study addresses the main causes of the depreciation of the Indian rupee and how it is effecting the Indian economy. The major reasons for rupee value depreciation are the increased cost of crude oil, a large-scale outflow of FI, and the increased US fed rate. The weakening of the currency made domestic products and services more inexpensive than before. Exports grow as imports decline. Developing countries frequently work to enhance their export industry in order to raise their GDP level.

Keywords: *Depreciation, GDP , Foreign Income, Fed rates, Export Industry.*

Introduction

A country's currency depreciates when there is a fall in the value of the floating exchange rate of the currency. This means depreciation of the rupee refers to a decline in the value of the rupee relative to the dollar. It means that the rupee is now weaker than what it used to be earlier. Import costs will increase when the value of the domestic currency falls, but export costs will decrease. Since their purchasing power is diminished when they purchase goods and travel overseas, a fall in the value of the rupee might result in residents' living standards declining. If an international debt is held in a foreign currency, devaluation may increase the cost of interest payments on that debt as well as restrain foreign investors (Singh,2013).

The following are the primary causes of rupee appreciation or depreciation:

I. Inflation Rate: When India's inflation rate is lower than that of other nations, demand for Indian goods and services from overseas consumers will increase. It may result in increased demand for Indian currency, which would cause an appreciation in terms of Indian money.

II. Interest Rate: Interest rate differences between two nations lead to demand. Interest rates are typically between 4 and 6 percent in developing nations like India, which encourages capital inflow from investors because they can earn a better return than they might in their home nations like the US (where interest rates are between 1.5 and 1.75 percent), which results in rupee appreciation.

III. Export-Import: If a nation (India) exports more than it imports from other nations, this would indicate stronger demand for that currency (the rupee), which results in that currency's appreciation against other currencies.

IV. Forex market: Speculative trading on the Forex market constantly causes exchange rates to fluctuate. This trading is influenced by several basic variables, including the economy's capacity for development, interest rate differences, and the level of inflation in other nations. In India, the government buys the rupee in exchange for foreign currency to raise the economy's money supply, which causes the rupee to depreciate, while it buys foreign currency in return for the rupee to decrease the economy's money supply, which causes the rupee to appreciate.

Recently, the rupee value depreciated from 63.33 against the dollar in December 2014 to 81.93 in October 2022 (economic times report, October 2020). This is the highest decline that the economy has seen in the past.

Why Rupee Value Falling?

The currency exchange rate in India has reached its lowest point of Rs 81 per dollar this year, a devaluation of more than 7%. Supply and demand influence the value of the Indian rupee in respect to the US dollar. The value of the Indian rupee falls when demand for US dollars rises, and vice versa. If a country imports more than it exports, demand for the dollar will outstrip supply, which will result in a decline in the value of the local currency, such as the rupee in India, relative to the dollar.

Below is a list of some of the main causes behind the currency's swings between low points:

US Fed Rate Increase

The United States is anticipated to raise interest rates further as consumer price inflation surges to a 40-year high. The nation raised its interest rate by 100 basis points in June, which sent the US currency surging to a 20-year high. Typically, central banks raise interest rates to reduce consumer

demand and control inflation.

The US Federal Reserve is expected to adopt an aggressive monetary policy with frequent rate rises as a result of the country's inflation rate of 9.1%, which is significantly higher than the forecasted rate of 8.8%. To rebuild the pandemic-ravaged economy, the US has been pursuing an expansionary strategy since 2020.

This increase will have an impact on emerging nations like India since capital is moving to stronger economies with higher yields. Investors frequently take out loans from established nations and use the money to make higher-yielding investments in emerging market economies. However, a rise in interest rates in the US would make investing in India less appealing to these investors.

Large-scale FI outflow

The conflict between Russia and Ukraine has had a wide range of effects on the Indian economy, and foreign portfolio investors (FPIs) have so far withdrawn more than Rs 2 lakh crore from Indian markets. The RBI has found it challenging to stop the depreciation of the rupee as a result of the decline in foreign exchange reserves.

The Cost of Crude and Inflation

The world's oil supply and crude oil prices have been significantly impacted by the conflict in Ukraine. This proved to be a very difficult situation for a nation like India, which is largely dependent on oil imports, and it caused increased inflation.

In April 2022, India's annual inflation rate reached 7.8%, the highest level since May 2014. The Reserve Bank of India (RBI), burdened by inflationary pressures, was unable to maintain low-interest rates to attract international investment. Despite India's impressive development narrative, outflows persisted. Consumer spending and the nation's current account imbalance were halted by rising consumer inflation. The CAD was 1.2% of GDP in 2021–2022 due to an expansion in the trade imbalance.

The depreciating rupee increased India's import costs and increased manufacturing costs, which further increased inflation. The Indian economy might gain from a weaker rupee by increasing exports. However, it is unlikely to help the nation given the weak global demand environment at the moment.

How does the Economy and People affected by the Weak Rupee?

India pays in US dollars since it imports the majority of its commodities, including electronics, metals, and other items like crude oil. Now, to buy the same quantity of items will cost more if the rupee is weak. When this happens, the price of production and raw materials rises, passing the cost on to

consumers.
On the other hand, a weaker national currency boosts exports as shipments become more competitive and foreign consumers have higher purchasing power. Exporters, however, are opposed to the currency decline given the current conditions of weak global demand and persistent volatility.

Given that over 80% of India's crude oil is imported, making it the country's largest import, inflation would be the issue that the weakening rupee would most likely influence. Oil has been priced at or over $100 a barrel ever since Russia invaded Ukraine in February of this year. As a result of rising oil prices and a falling rupee, inflationary pressures in the economy will only become worse.

Conclusion

Depreciation lowers a nation's currency's value in comparison to other currencies. Depreciation discourages imports by making imported items more expensive as a result of a decline in the value of the rupee. The rising cost of products causes inflation.

Rupees, a currency that foreign investors frequently utilise, are used to redeem assets in India. Before using them, they will need to exchange their rupee holdings (into dollars). Rupees will be traded for dollars. As a result, the dollar gains popularity while the rupee loses popularity. Foreign investors are leaving Indian equities as a result of the rupee's fall.

Simply said, India would have to spend more rupees on imports if dollar demand increases, which will fuel the country's inflation rate. The central bank (RBI) will use rate increases to control this inflation, which will make borrowing more expensive and eventually have an impact on the public.

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