

WEEKLY NEWSLETTER

RUPEE HITS NEW ALL-TIME LOWS AS DOMESTIC ASSETS CONTINUE TO UNDERPERFORM



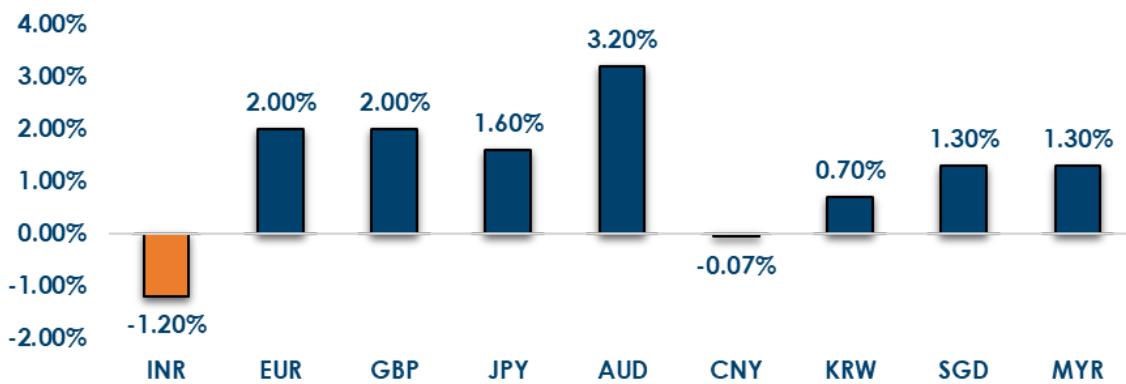
Global Developments:

- The week began with Trump announcing tariffs on European allies to coerce them into entering into an agreement on Greenland, but subsequently backtracked, saying he wouldn't impose tariffs from Feb 1 (as he had threatened earlier).
- Incursion into Venezuela, aggressive stance on Greenland, intervention in Iran, concerns around Fed independence, lack of respect for established organizations like NATO, and COP are all factors that have triggered erosion of confidence in the dollar as a haven. It has accelerated the De-Dollarization process. This is most evident in previous metals, which just continue to soar. Gold neared the USD 5000 psychological mark while Silver breached the USD 100 mark!
- Japanese 10-year yield is the highest since Jun'97 at 2.26%. The 40-year yield had hit 4.23% and ended the week at 3.94%. One-sided Yen weakness and JGB selloff could trigger a systemic crisis (a VaR shock). The Fed is concerned about the same and conducted a rate check, which is typically seen intent to intervene.
- Domestic assets continued to underperform. The market is fixated on the trade deal. A depreciating Rupee is further fuelling anxiety among FPIs. Rupee, equities, and bonds are all under pressure.
- The RBI late Friday announced liquidity infusion of over Rs 2lakh crs through 91-day VRR (Rs 25000crs), Buy-Sell swap of USD 10bn (Rs 92000crs), and OMO purchase (Rs 1 lakh crs)

Foreign Exchange

- The Dollar weakened across the board last week. NZD (+3.4%), NOK (+3.3%), and AUD (+3.2%) led gains, while EUR, GBP, and DKK rose ~2%. CAD and JPY lagged but still advanced 1.6%, highlighting broad USD softness.**
- The Euro gained solidly against the Dollar, supported by broad USD weakness, though upside remained capped by muted growth expectations in the Eurozone.
- Sterling matched the Euro's advance, benefiting from the softer Dollar, while lingering UK growth and inflation uncertainties kept gains measured.**
- Yen strengthened by 2.2% on Friday itself as the BoJ and the Fed both signaled they would intervene to prevent one-sided depreciation of the Yen.
- Asian currencies were largely steady to stronger against the Dollar this week, led by gains in SGD and MYR (+1.3% each), followed by KRW and THB (+0.7%), PHP (+0.5%), IDR (+0.4%), and CNH (+0.3%), while TWD and HKD were flat, and INR underperformed, declining 1.2%.
- Rupee traded in a 90.62-91.98 range and ended at almost the weakest point at 91.96 compared to the previous week's close of 90.88**
- FX Reserves rose USD 14.2bn to USD 701.4bn as on week ending 16th Jan, mainly due to revaluation of Foreign currency assets.**
- As per RBI's latest bulletin, the 40 currency trade-weighted REER dropped to the lowest since 2014, indicating that the Rupee has slipped deeper into undervalued territory on continuing underperformance.**

Weekly % change in Currencies



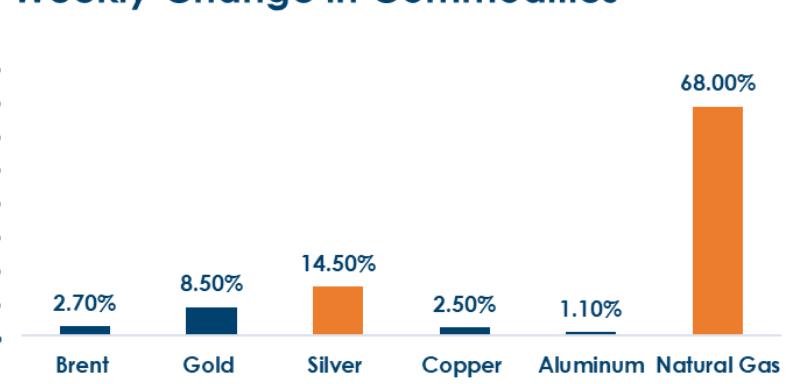
Fixed Income

Yields on the US 2y treasury ended 1bps lower at 3.59%. Yield on the US 10y had risen to 4.29% this week, but ended almost unchanged at 4.22%. 10y yields across the Eurozone were up 5-10bps, with the exception of France, which was flat, and Greece, which was up 17bps. Yield on the 10y JGB ended 1bp lower at 2.24% after having spiked to 2.34% during the week. Yield on the benchmark 10y traded a 6.63-6.695% range and ended at 6.66%. 1y OIS rose 6bps this week to 5.60%. 5y OIS rose 12bps to 6.14%. FPIs have bought net USD 700mn of domestic bonds in January so far.

Commodities

- Commodities had a strong week — Brent rose 2.7%, US Natural Gas surged 68%, Aluminum gained 1.1%, Copper added 2.4%, while precious metals outperformed with Gold up 8.5% and Silver soaring 14.5%.
- Precious metals continued to zoom on concerns over the Dollar. There is a definitely urge to move towards a physical store of value from fiat currencies given the current geopolitical uncertainties.
- US Natural Gas surged on a massive arctic cold wave which resulted in a sharp surge in demand for heating.

Weekly Change in Commodities



Option Structures for Exporter Importer

EXPORTER ENHANCED COLLAR

Spot ref 91.60
 Tenor 6m
 Fwd level 92.85
 Buy put 92.70
 Sell call 92.85 with eki at 93.75
 Net zero cost



IMPORT SEAGULL

Spot ref 91.60
 Tenor 3m
 Buy call Atmf (92.30)
 Sell put 91.00
 Sell call 93.50
 Net cost 5 ps



Our Views: What we like?

FX

We continue to remain bearish on the Dollar overall and expect the Rupee to continue to underperform. The market is fixated on the trade deal, and any RBI intervention may just be used as an opportunity to enter into fresh long Dollar positions. Domestic Q3 earnings have been disappointing, and FPI selloff in equities continues. We see the Rupee trade in a 91-93 range over the next 6 weeks.

Fixed Income

We expect the yield on the 10y to trade in a 6.60-6.70% range till the budget. There is a possibility that the government may choose to defer fiscal consolidation given the current domestic macro challenges. There would be panic in bond markets if this were to happen. A high nominal GDP growth expectation used for budgeting purposes may not go down well with markets, too, as it would be seen as being unrealistic (anything over 10%).

Commodities

Rally in precious metals is likely to continue, and any dip of 8-10% should be seen as a buying opportunity. There is a definite trend of preference to hold physical assets over fiat currencies, and we see this playing out over a protracted period of time.

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