Indian Express edit

No cause for them. Sensex worries are overdone and India is in a much better position to deal with it.

Given how global markets rose after the US Fed's decision to reduce its monthly bond purchases from $85 billion to $75 bn, the Sensex reaction seems overdone. While markets in China and Hong Kong also fell on fears that foreign investors would flock back to the US, where stock market yields are strong, keep in mind that things are quite different from the last time that talk of the taper gained ground. For one, with the US GDP growing at 3.6 per cent in the second quarter of 2013, a number last seen six quarters ago, a taper isn't expected to reduce US growth much, and this week's budget agreement suggests US politics may finally be coming together.

At that time, India's current account deficit was also out of control and, with the talk of the taper, around $7.1 bn of FII funds exited the country in June, another $3.1 bn in July and $2.3 bn in August — between June and August, the rupee fell from 54.39 to 62.68 to the dollar — and then the net inflows were just slightly positive for the next few months. The combined effect of an out-of-whack CAD and exiting FIIs sent the rupee into a tailspin. What made things worse was the fear that, as investors took up speculative positions against the rupee, it looked as if the RBI wouldn't have enough dollars to defend it. The perfect storm, as it were.

Things look very different today. Apart from the massive controls put on gold imports, the collapse in economic growth has meant the CAD has shrunk dramatically, from 4.9 per cent in the first quarter of this financial year to a mere 1.2 per cent in the second quarter — this means the full year's CAD is more likely to be in the 2.7 per cent of GDP range as compared to last year's 4.8 per cent, and is fully financeable from the current level of reserves. Added to this is the fact that the RBI's imaginative swaps, both for banks raising capital as well as those raising NRI deposits, brought in an additional $34 bn — in addition, $2.1 bn FII money came in the first 17 days of December. And since the RBI also extended a swap agreement to oil companies — they were sold dollars directly by the RBI in return for a promise to repay them later — this had the effect, in a full year, of reducing demand for dollars by $160 bn. To ensure there was no rush for dollars when oil dollars needed to be returned, the RBI said the difference between purchase and sale prices of dollars could be redeemed in rupees. In other words, the RBI has more of a war-chest and the ability to reduce dollar demand, and the global economy is stronger. No cause for taper tantrums.