

## **Deep Impact: How A Vulnerable Rupee Is Affecting Performance of Indian Firms?**

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**Abstract:** *The Indian Rupee has witnessed a torrid run this year. The currency plummeted to its all time low near 70 dollar mark in August before improving. The currency is still down nearly 50% over last five years and is around 15% lower compared to last year. Clearly, the Rupee has been one of the worst performing currencies in the world. This has turned out to be a major problem for local companies, particularly the ones with a heavy exposure to the overseas trade. Corporates need foreign exchange for multiple reasons- making payments for raw materials, raising funds, overseas mergers and acquisitions, managing foreign subsidiaries etc. We develop an understanding of the forex earnings and expenses of top local corporate- as represented by the NIFTY 50 companies. In order to get an idea of the quantum of these companies forex exposure, we take out a stock of their forex earnings and expenses over last five years and find out that there is an overwhelming rise in such exposure. Fluctuations in currency have been a key factor boosting earnings for some firms; particularly the export heavy firms while certain corporate have been hurt heavily at the same time though. An analysis of the movement in the USD/INR pair indicates that the volatility in the pair has been on the rise as well and could affect the local firms much more in coming months. We identify that firms with heavy foreign debt are facing a double whammy due to soaring interest cost and a bloated repayment amount. The structurally weak undertone of the local economy and worries about a probable shift in ultra easy money policies of the US are expected to keep the Rupee under overwhelming pressure in next few months. We strongly feel that the currency play would become a dominant factor for the local firms and would have a deep impact on business performance and valuation. We analyze the performance of the major companies with significant forex exposure and heavy overseas debt. We conclude that yet another bout of weakness in the local currency; similar to the one witness in mid 2013 could have a catastrophic medium term impact on local business environment and monetary policy decision-making.*

### **I. INTRODUCTION:**

The massive deterioration witnessed in the Indian Rupee is probably the most intriguing aspect of business environment for Indian companies over last one year. The sharp depreciation of the rupee in mid-2013 highlights domestic economy's difficult transition following an extended period of low growth, high inflation and a widening in the current account deficit. The currency plummeted to its all time low near 70 dollar mark in August before improving. The rupee is still down nearly 50% over last five years and is around 15% lower compared to last year. The recent slide in rupee has been linked to global factors, particularly because of the strengthening of the dollar and signals from the US that it may start cutting down on stimulus spending. However, a decade low growth rate for the local economy and weak investment cycle has also been important reasons for the poor performance of the local currency.

The US Fed has eventually decided to cut back on its asset purchases- dubbed as Quantitative Easing in the middle of December. A forceful deterioration in the exchange rate of the Indian Rupee means that a number of sectors are being badly affected. Import heavy companies with a relatively less export exposure are the obvious victims of the turmoil in Rupee. IT giants, Petroleum companies and automotive manufacturers have topped the list. A continued spell of weakness in rupee could widen India's current account deficit, which has already been a big concern for the country over last couple of years. However, what is more worrying than the rapid depreciation of the currency is the volatility in the USD/INR pair over the last few months. This makes the business environment uncertain and adds an additional layer of risk for corporate with a heavy exposure to foreign exchange expenses and incomes.

Indian corporates have already stepped up borrowings from the international market over last few years. The surge in the forex exposure of the companies and increase in the external borrowing adds the concerns about the currency fluctuation. The companies need funds for treasury operations, overseas funding for foreign branches, takeovers and mergers, expansions of businesses, In addition to this corporates require the foreign exchange to repay the import bills. India's External commercial borrowings have more than doubled during 2011-12 and continued to see a steady rise in 2012-2013 as well. The local companies have borrowed due to wide difference in cost of credit. The tight monetary policy in India raised the key interest rates and therefore the cost of borrowing from domestic money market. The widening gap between internal and external sources pushed the corporates to borrow from international market. The increase in foreign debt of Indian corporates has underlined the currency risk. Although the borrowers obtained finance at lower interest rate, the debt repayments in rupee terms have increased sharply with devaluation of rupee. This could neutralize the benefit of low interest rate. In fact, now the Indian corporates face the dual risk of interest rate volatility and exchange rate volatility but the companies seem to have favored the currency risk against the risk of interest volatility (Ila patnaik, 2012). This provides the background for an interesting case study of Indian corporate; how they have been affected by volatility in exchange rate

### **Currency Exposure: Practical Insights from Developed Economies**

Currency exposure is a critical aspect of business environment, with constantly changing exchange rates adding in an additional layer of uncertainty to the company's profitability. How do currency fluctuations affect financial performance of a company and what do the companies do to insulate themselves against adverse currency moves? When a firm has shareholders to report to, and the figures can run into millions, how does it grapple with such an intricate matter that can have a serious impact on profits and losses?

If a US-based firm makes EUR 10 million, they can end up with much more or less than they thought depending on the movement of the EUR/USD exchange rate. For example, in January 2013 it would have been worth \$13.2 million, but in May 2013 it would have been worth 12.8 million and \$13.7 in December 2013. Needless to say that these issues also exist when finalizing contracts with international clients. Although something may seem like a good deal when it is first written down, it can turn bad a few months later when the contract is fulfilled.

A study by SunGard Data Systems in the middle of 2012 polled 275 US businesses of various sizes. It found that 59% of those surveyed had seen a loss or gain of more than 5% as a result of currency fluctuations in the previous year. The study points out that the majority of corporations are in the business of doing business, producing and manufacturing, not hedging currencies. A lot of companies were caught unawares by volatility. Looking at where the exposure lies instead of waiting for quarterly results to discover the impact of fluctuations was a better approach. SunGard notes that this is a stance more and more firms are taking.

Therefore, organizations have to evaluate the risks of doing business on an international level. But it doesn't always work in their favor. For instance, McDonald's saw sales in Europe increase in 2011, but the yearly profits were actually down as a result of a weakening euro. Indeed, some experts think investors should be cautious this year too given that the US dollar has strengthened so much recently and is expected to continue doing so. As McDonald's generate nearly three quarters of its profits overseas, this could be a major issue if they have not hedged.

Another major instance of this happened with a multinational was at eBay, with CFO Bob Swan admitting that currency fluctuations will hit the bottom line by around three points in 2012. Foreign currency effects are estimated to negatively impact net revenue growth by approximately 200-300 basis points in the first quarter, the company had stated.

### **India's Experience with Currency Fluctuation:**

India's experience with the movement of its currency has been interesting. No country can remain isolated from the tidal wave of globalization and a major emerging economy like India has been no exception. The impact of economic fluctuation in a country affects the other country through various channels and exchange rate fluctuation is one of the most prominent of such channels. The world economy has witnessed a massive increase in international trade with the emerging economies accounting for a growing share of the cross border exchange of goods and services. Volatility in the exchange rate, therefore, has been one of the major elements in shaping up economic policies as well as corporate performance. An exchange rate is a function of the supply and demand dynamics of a currency. Quite simply, the exchange rate is a function of trade balance, the interest rate differential and differential inflation expectations between the two countries.

Indian rupee has witnessed torrid exchange rate volatility not only because of depreciating INR value but also a preference for the US Dollar amid times of rising global uncertainty. At times, the dollar has acted as a safe haven asset in global markets in the aftermath of the great global crisis that struck the world economy around five years back. Slowdown in the domestic economy along with increase in current account deficit has also affected the local currency. Fluctuations in the exchange rate affect the balance sheet of the country and the local industry. Overall trade balance of the country is nothing but the sum of the activities of individual firms clubbed with the government actions. Therefore the fluctuations in the rupee in coming months likely to affect Indian corporate sector more intensely.

Fluctuations in currency have been a key factor boosting earnings for some firms; particularly the export heavy firms while certain corporate have been hurt heavily at the same time though. An analysis of the movement in the USD/INR pair indicates that the volatility in the pair has been on the rise as well and could affect the local firms much more in coming months.



Source: CCIL

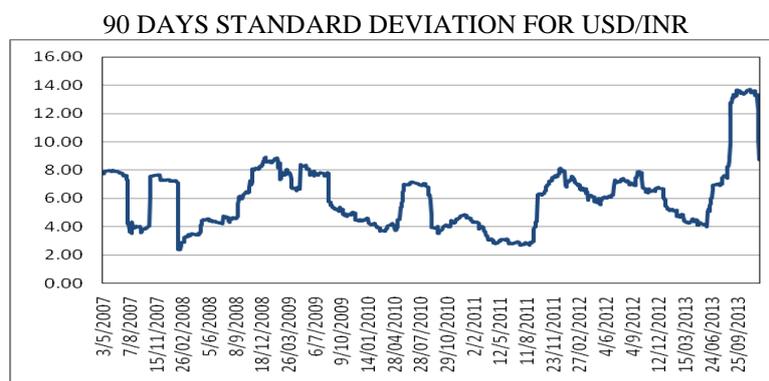
The currency's fall comes at a bad time for India. The country has just begun to recover from the slowest growth in a decade, and a weakening rupee may hurt any recent improvements in the country's economic situation. Inflation, as measured by the consumer price inflation (CPI) for the month of November 2013 was alarmingly high at 11.24%, maintaining its upward trajectory even as the tempo in overall economic growth remains subdued. India's finance ministry expects GDP to grow 5-5.5% in the fiscal year 2013-14. The economy grew 5% in the last fiscal year, the slowest pace in a decade, as companies put investments on hold and consumers cut back on spending in the face of high borrowing costs.

The Rupee has been one of the worst performing currencies in the world. Local stock markets were in disarray following the twin effects of weak economic growth and the currency's poor performance before staging a spectacular comeback in the last quarter of the calendar year. Local equity benchmarks hit fresh all time highs as 2013 drew to a close. The Rupee has also recovered from its ultra low levels and lingers around 62 per dollar levels as the year draws to a close. However, the scenario appears grim as the dichotomy between Rupee and local stock market seems to have gone for a toss. It is worth remembering that when the local equity markets had attained the current levels first time five years back, the INR was quoting at around 40 per US dollar levels.

The currency depreciation could also have an impact on the fiscal deficit, which has been narrowing over the past few months. While India's central bank has stepped with a slew of well timed measures to stem the slide, these are only short-term measures and what the country needs are long-term solutions like kick starting the investment cycle in India and increasing foreign cash inflows. Unfortunately, with General Elections being held in less than six months time and prevalence of none too optimistic global economic background means that it would be highly unlikely to see a fundamental push being given to the economy in near term.

### **Volatility Puzzle of The Indian Rupee:**

While the INR has been sliding consistently over last few years, the meltdown witnessed in mid 2013 was cataclysmic. The course of action after the global financial crisis surfaced around five year back has seen the local currency loose from around 40 per US dollar to around 62 right now. On a longer term, the decline is less dramatic, though by no means ordinary. Over the last 20 years, rupee depreciated from Rs 25 to Rs 60 to a dollar. During this period, the rupee appreciated against the dollar between January 2004 to about July 2007, touching its peak of under Rs 40 to the dollar, before 2008, where after it fell rapidly to below Rs 50. All through this period, India's trade balance was adverse, along with higher inflation. However, none of the previous episodes of Rupee decline are equivalent to the meltdown seen in 2013. The currency fell at a rapid rate and the volatility in the USD/INR pair shot up through the roof as well. The standard deviation for the pair surged dramatically as the currency dropped. Standard deviation over a period of 90 days or one quarter- surged to as high as 13 in September 2013. This measure never managed to break above around 8 in last six years- even in times of extreme stress for the local currency and stock markets. Even in the troubled times in 2009- when local stocks plummeted to a near decade low, the volatility in the USD/INR pair did not reach the dizzying highs witnessed in the current year.



Rupee has to find stability given the persistent increase in India's international trade. According to the RBI, demand for internationalization of the rupee, especially greater use of rupee for trade invoicing, would increase as in the case of China. In the region, India holds an important position in terms of economic growth and volume of trade. India has a growing role in Asia as an engine of economic growth. It is increasingly getting integrated with East Asian Countries. The value of the Indian rupee is market determined and not pegged to any currency. India's foreign exchange reserves are amongst the largest in the region. All these factors make the Indian rupee a natural candidate for being considered for greater internationalization.

Presently, a cash market for the Indian rupee exists outside the country, e.g., in the Middle East and in South East Asia. The Rupee NDF market which was not very large or liquid till a few years back has increased significantly in size in the recent period. The size of Rupee NDF market which was reported to be around US\$ 100 million per day in 2003-04 has increased to around US\$ 800 million in 2008-09. The volumes have only surged thereafter with the Finance Minister P.Chidambaram expressing concerns over the large volume of rupee market being played out in overseas market leading to high volatility. According to media reports in mid December 2013, the Finance Minister noted that volume of trading of rupee in the NDF market is said to be a multiple of the volumes in the official domestic exchanges.

#### **Understanding Impact of Currency Depreciation on Local Firms:**

There are a number of ways through which corporates tend to get affected because of the volatility in currency rates. Corporates need foreign exchange for multiple reasons- making payments for raw materials, raising funds, overseas mergers and acquisitions, managing foreign subsidiaries etc. Here is an account of the major corporate in India with reference to currency swings. The analysis focuses on the latest earnings season ending September 2013. Though the volatility would affect the businesses even more in quarter ending December, given the lagged effect, we are highlighting the latest data available to make the study up to date.

#### **Tata Consultancy Services Ltd.**

India's largest software exporter TCS reported 34% jump in consolidated net profit at Rs 4.70 billion (bn) for the July-September 2013 quarter on the back of large deal wins and currency depreciation. Total revenue grew 34.3% to Rs.20 bn in the second quarter of the current fiscal from Rs.15 bn in the corresponding quarter last fiscal. The company's margins improved by over 300 basis points due to currency depreciation.

#### **Reliance Industries Ltd.**

Reliance posted a net profit of Rs.54.90 bn for the July-to-September quarter, just 1.5% compared to corresponding period last year. Meanwhile the company's sales rose 15% to an all time high of Rs.1.04 trillion. The growth in sales totally reversed the 4.6% decline seen in the June quarter, thanks to the currency depreciation. However, a sharp increase in raw material costs on account of higher crude oil prices hurt operating performance. RIL's operating profit margin declined to 7.56% - lowest in five quarters.

#### **Ranbaxy Ltd.**

The pharmaceutical major reported consolidated sales of Rs.27.5 bn and EBITDA of Rs.2.0 bn for the quarter ended September 2013. It noted that The depreciation of the INR against the US dollar, though favorable to Ranbaxy's export business had an adverse impact on the Company mainly on account of application of the accounting standards that require Marking to Market the entire derivatives and foreign currency denominated loans outstanding. There was a charge of Rs.3.6 bn during Q3 2013 and Rs.7.6 bn during YTD September 2013 on account of these forex items.

#### **Bharti Airtel Ltd.**

Bharti's consolidated net profit fell to Rs.5.12 bn for its fiscal second quarter ended September 30 from Rs.7.21 bn a year earlier- a near 30% drop. The company reported an EBITDA margin of 32%, higher than 30.6% in the year-ago quarter. However, the continued depreciation of the Indian rupee has resulted in forex restatement and derivative losses of Rs 3.42 bn versus Rs.0.25 bn loss for the corresponding period last year.

#### **Hero Moto Corp Ltd.**

Hero MotoCorp Ltd, which posted its first profit gain in five quarters, aims to sell motorcycles in eight more overseas markets by March to ramp up its export earnings in response to an increasingly combative home market. India's largest maker of two-wheeled vehicles reported a net profit of Rs.4.8 bn for the fiscal second quarter ended September 30 2013, up nearly 9% year on year. Revenues increased 10.4% to Rs.57.2 bn in second quarter from Rs.52 bn crore in a year ago period. However, the rupee depreciation has pulled up the cost of essential commodities such as steel, nickel, copper and rubber. Going forward, these higher input prices, combined with increasing labour cost, are likely to put a lot of pressure on margins in the industry, the company noted.

### **Hindustan Uniliver Ltd.**

Revenue growth at Hindustan Unilever slowed for the sixth straight quarter between July and September. Sales volumes in the September quarter grew 5%, in line with market estimates of about 4-5% growth but slower than the 7% growth logged a year before. HUL said its net profit in the September quarter rose an annual 13.2% to 9.14 billion rupees. Net sales rose 9.6% year-on-year, to 67.47 billion rupees. However, on a specific note, Material Cost / Net Sales ratio declined by 169 bps Y-o-Y & 65 bps Q-o-Q to 51.4%. Gross margins improved by 169 basis points Y-o-Y & 65 basis points Q-o-Q despite sharp rupee depreciation in Q2FY14, largely due to hedging of raw material.

### **External Commercial Borrowings: Has The Limit Been Breached?**

The soaring debt servicing payment following the depreciation in rupee would remain the cause of concern. Indian corporate had borrowed heavily through external commercial borrowing. The reserve bank of India adopted the tight monetary policy from March 2010 to October 2011. The key interest rate rose 13 times to 8.50%, as a result the commercial bank also raised the deposit and lending rates (**Deokar, Jangili 2013**). The cost of borrowing from domestic market increased substantially. At the same time, the local corporates were able to source funding from overseas at London Interbank offered rate (Libor) +300/400 basis points. This facilitated firms to borrow from external sources at relatively very low interest rates. The decelerated growth in corporate borrowing from the domestic commercial banks since 2009 reveals the same. According to RBI report there has been surge in ECB outstanding since 2008-09. The Interest rate difference between domestic and international market led to increase in ECB debt up to \$1,20,893 million in 2012-13 from \$62,461 million in 2008-2009. However, apart from the sheer quantum of the ECBs, the servicing of this debt is acting as a major drag on the country's forex exchange resources. The interest payments on these ECBs hit \$6310 million in FY 2012-13- up sharply by 16.60% compared to the previous fiscal.

**India's External Debt Service Payments - (\$ million)**

<b>Year</b>	<b>2009-10</b>	<b>2010-11</b>	<b>2011-12</b>	<b>2012-13</b>
ECBs	14,472	13,959	25,198	23,224
Repayment	11,498	10,451	19,782	16,914
Interest	3,244	3,508	5,416	6,310

Source: RBI, Bulletin, December 2013.

The companies borrow at the cost of exchange rate risk and seemed to have been caught off guard by the weak rupee. The fragile rupee has led to surge in interest payment. Note that the above figures pertain to the previous fiscal and interest payments on ECBs could surge even more sharply this fiscal given the plight of the local currency. In addition to this, if international interest rates rise in the wake of the altering stance of the US Fed, the Indian corporates would be more vulnerable than before on the external debt front.

According to the Global agency Moody's, a weak rupee and higher borrowing costs will impact credit quality of several Indian companies especially, IOC, Tata Steel and Tata power. "Increased borrowing costs and the weak rupee will pressure the credit quality of rated Indian non-financial companies," Moody's noted in a report titled 'Higher borrowing costs, weak rupee will pressure Indian corporate credit metrics'.

Depreciation of the Indian Rupee will lead to revaluation of debt issued in US dollars, which in turn could put pressure on some covenants. The agency highlighted that the 14 non-financial companies that it rates in India have a combined debt of Rs. 2.2 lakh crore which is maturing in the fiscal year ending March 2014. Out of this, over 50% is denominated in foreign currency.

Referring to IOC, Tata Steel and Tata Power Company, Moody's said these companies are highly leveraged over the next 12 months and face a steeper increase in interest costs. "We believe they will be able to refinance their maturing debt, but possibly at higher credit spreads than on existing debt," it said. On ONGC, RIL, TCS and Gail, it said they operate with large cash balances, which provide a buffer to fund any shortfall in working capital requirements and support near-term refinancing needs, if required.

The report also said that rated companies with debt denominated in foreign currencies will report an increase in total debt value as a result of the historically low rupee exchange rate. If the companies total reported debt increases owing to foreign exchange moves, their financial covenant cushion will likely decline, particularly with respect to interest coverage and debt service coverage ratios, as we expect their interest costs to increase as well.

### **Hedging Mechanism in India Inc: Need to do More!**

Corporate hedging is a mechanism to protect a firm's exposure to foreign exchange risk. The process is managed by corporate treasury officials and they work towards maximizing forex income and minimizing costs. In the process, they try to minimize losses from the volatility in the currency markets, by covering the exposure. The extent of the foreign currency risk for a firm depends on the value of the foreign exchange rates, among other things.

The Reserve Bank of India moved towards a more market-determined exchange rate since the early 90s. The rupee has become more volatile against the dollar and other major currencies over the years; particularly after the derivatives trading was allowed in the INR in 2008. This, coupled with a highly turbulent global currency market forced local companies to hedge their foreign currency exposure. Another reason why companies attempt to hedge is because they see foreign currency fluctuations as risks that are directly linked to the central business in which they operate. Hedging objectives vary widely from firm to firm, even though it appears to be a fairly common issue faced by corporate. Another reason for hedging the exposure of the firm to its financial price risk is to maintain the competitiveness of the firm. Sometimes there is an opportunity loss in hedging, which is why some corporate, as a matter of risk management strategy, do not.

There risks arising out of transaction with clients and other business associated which are called transactional risks. A foreign currency loan would yield a different value on conversion, depending on the way currency markets are moving. Similarly, an importer faces a currency risk as there could be a significant movement in currency value from the date on which it contracted the purchase and prevailing exchange rate on the delivery date. The same logic holds for exporters. Corporates also hedge interest risks as in the global markets; interest rates are also not steady.

In recent times, the local industry has been involved in two-way hedging, wherein both the importers as well as the exporters are hedging. This is due to the unpredictability in the direction of the currency movement. Corporates have to take a critical call on when to hedge and when not to, along with the extent to which it should be hedged and what hedging instrument should be used to avert an opportunity loss. While the practical considerations for hedging mechanism differ from business to business; the following structure could be used to explain the currency risk management practices in general.



**Source: Hedging Strategy for Indian IT, Finstream**

According to some media reports, following the recent bout of volatility in the rupee, many small- and mid-size companies in India are rushing to hedge their foreign currency risk. These companies are in businesses in which exports and imports form a significant part of revenues and payments, such as textiles, shipping, and oil and gas. Hedging has become a necessity for these companies that are deeply impacted by the uncertainty in the forex market. In the last couple of months, there has been an increase in small- and mid-size companies seeking to hedge their forex exposures because they have been hit hard when the rupee neared its all time low of 70 per US dollar.

In a report published in July 2013, CRISIL Research indicated that it expects India Inc to be severely impacted by the rupee's depreciation against the dollar given the large foreign currency debt on the books and only partial hedging. Moreover, the rupee's depreciation will lift input costs across many sectors amidst weak demand environment as reflected in low double digit topline growth expected in 2013-14. Even exporters are unlikely to benefit significantly as clients may seek to renegotiate contracts. We expect the rupee to strengthen from its current levels, but the 2013-14 average will still be 5-8% weaker than the 2012-13 average.

Mark-to-market losses and higher debt servicing costs are likely to be key pressure points in the near term. According to Mukesh Agarwal, President, CRISIL Research, "For companies in the CNX Nifty (excluding banking and financial services), around 40% of debt is denominated in foreign currency. In total, corporate India had forex debt outstanding of over \$200 billion as of March 2013 of which close to 45% is short-term debt. Moreover, only half their forex exposure is hedged. Persistent weakness in the rupee and heightened volatility has reduced the benefits of borrowing overseas."

From the growth and profitability perspective, sectors that will be negatively impacted by the rupee's depreciation include automobiles, auto components, airlines, consumer durables, oil marketing companies (OMCs), and fertilisers. The increase in fuel costs will hurt demand for automobiles, especially small cars, as fuel alone accounts for nearly 25-30% of the ownership cost of a small car in the year of purchase. Airlines with a high proportion of revenues accruing from domestic operations will also be hurt as 70% of their operating costs are incurred in dollars, and their ability to pass on any cost increase is limited.

### **What the Financials Reveal About Currency Exposure Of Local Companies?**

Analyzing the financial data for the existing set of NIFTY 50 companies, we can infer about their forex exposure and how the structure of the same has increased over the years. The most basic measures of interest in company financials as far as forex exposure is concerned are Revenue earnings in forex and Revenue expenses in forex. We can notice that there is a perceptible rise in these two metrics of local corporate performance. The analysis encompasses the NIFTY companies, excluding the banks and NBFCs and a couple of other corporates which did not present relevant data for the time frame under consideration. After removing such entries, we are left with a list of 37 companies.

The cement majors seem to be grappling with falling forex revenues while all the auto makers seem to be enjoying a healthy rise in the forex earnings. Manindra and Mahindra is the only exception to the rule though it has witnessed the most prominent increase in net sales over last five years- a surge of 258% that outsmarts all other auto majors and indicates that the company has penetrated the local markets quite successfully over the years compared to its peers.

The IT majors have obviously seen an impressive increase in their forex revenues which are totally in sync with their sales figures. HCL is the only company which has seen the sales rising much more than forex earnings. However, a rise of 159% and 173% in forex revenue expenses compared to sales growth of 135% and 88% for Infosys and WIPRO respectively makes up an interesting reading.

Pharmaceutical companies seem to be deriving a massive chunk from overseas sales. The top five Pharma companies- Lupin, Ranbaxy, Sun Pharma, Dr Reddys Laboratories and CIPLA are witnessing an increase in forex revenues which is mostly greater than increase in their sales. Sun Pharma, with a 23% drop in net sales over last five years and a staggering 140% rise in foreign earnings seem to be heavily focused on export markets and should gain a lot from weakening rupee.

Reliance Industries Limited (RIL), India's largest private sector enterprise, has witnessed a generous rise in its forex exposure with forex earnings and expenses rising by 200% and 186% respectively over last five years. The company's sales have surged by a healthy 170% during the same time. The scenario is quite similar for other top corporates like GAIL, Asian Paints and ONGC.

FOREX EXPOSURE OF INDIA INC

Companies	% Change From 2008 To 2013		
	Revenue Expenses	Revenue Earnings	Net Sales
ACC*	204	-80	65
AMBUJA CEMENTS	8	-88	74
HUL	48	-57	89
ITC	90	76	115
INFOSYS	159	149	135
JP ASSOCIATES	631	417	235
LARSON AND TOURBO	241	132	143
LUPIN	72	196	182
MAHINDRA AND MAHINDRA	322	166	258
MARUTI SUZUKI	287	514	144
NTPC	68	54	77
ONGC	243	97	39
POWER GRID	22	3428	176
RANBAXY	98	49	49
RIL	186	200	169
SUN PHARMA	88	140	-23
TCS	142	174	165
TATA MOTORS	44	72	57
TATA POWER	17	1812	62
TATA STEEL	203	4	94
ULTRATECH CEMENT	-7	-31	266
WIPRO	173	118	88
SESA STERLITE	200	-57	-35
JINDAL STEEL	230	148	179
HINDALCO	54	18	38
HERO MOTORS	49	156	130
HCL	8	150	171
GRASIM	38	232	-49
GAIL	333	13	196
DR REDDYS	76	172	151
DLF	38	-60	61
CIPLA	74	99	105
BHARTI AIRTEL	30	81	76
BPCL	136	148	118
BHEL	95	-38	148
BAJAJ AUTO	123	216	131
ASIAN PAINTS	265	126	162

\* The latest data is as on March 31 2012 and % change is adjusted accordingly

Source: Company Data, Capitaline

Broadly speaking, companies like ITC, Infosys, Tata Motors, Mahindra & Mahindra, Dr Reddy's Laboratories, Tata Consultancy Services, Sun Pharmaceuticals, Wipro, Cipla and BHEL - benefit from a falling rupee as the total foreign exchange earnings of these firms are far greater than their forex expenses. Reliance Industries - the country's largest exporter - also gains from a weak rupee. While its forex outgo is more than its forex earnings, a significant part of its rupee earnings are pegged to the dollar. Metal companies including Tata Steel are likely to benefit at the operating level as most of their selling prices are denominated in US dollars while their costs are denominated in Indian rupees. However, the weakness in the domestic economy could negate these benefits to some extent.

According to an update from Fitch Ratings, the Steel Authority of India imports approximately 80% of its coking coal requirements, but its product prices are import parity-indexed and hence appropriately hedged, but with a lead time of one quarter. The more significant risk is likely to be higher reported debt levels stemming from FX translation adjustments, particularly for those companies with substantial foreign currency (FC)-denominated debt which is typically held at offshore subsidiaries. Higher reported debt levels will have a negative impact on a number of key credit metrics including financial leverage.

In the case of Tata Motors, UK-based Jaguar Land Rover plc accounts for over 75% of its revenue and 90% of its EBITDA. As the proportion of Tata Motors consolidated debt in FC currency is lower at 76%, the final impact from Indian rupee depreciation is likely to be positive.

However, Fitch has also noted that the more significant risk is likely to be higher reported debt levels stemming from FX translation adjustments, particularly for those companies with substantial foreign currency (FC)-denominated debt which is typically held at offshore subsidiaries. Higher reported debt levels will have a negative impact on a number of key credit metrics including financial leverage.

## **Conclusion**

The massive drop in local currency has left the businesses vulnerable on two counts. The first impact is linked directly to the core aspects of business activity – import and exports. The second impact is linked more to the financing activities of a firm i.e. foreign debt. The structurally weak undertone of the local economy and worries about a further shift in ultra easy money policies of the US are expected to keep the Rupee under overwhelming pressure in next few months. We strongly feel that the currency play would become a dominant factor for the local firms and would have a deep impact on business performance and valuation. If the US Fed does scale back its asset purchases even further in the next year, it could lead to a concerted sell off in emerging market currencies. The havoc caused by the Rupee in mid 2013 has affected not just the corporate earnings and financial structure but led to the domestic central bank pursuing a counter cyclical stance. The weakness in currency is surely expected to keep the domestic inflation levels elevated in coming months, tying up the hands of the RBI even in the face of a decade low growth rate. Thus, we conclude that yet another bout of weakness in the local currency; similar to the one witnessed in mid 2013 could have a catastrophic medium term impact on local business environment and monetary policy decision-making.

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