

Performance of INR in FY26

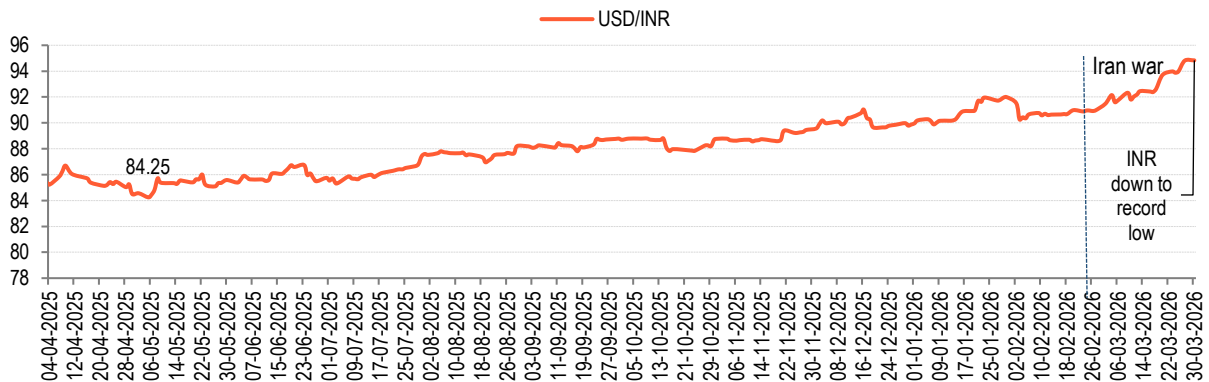
A confluence of factors were responsible for weakness in the currency in FY26, largely attributed to the geopolitical events, including tariff negotiations and the US-Iran war. Persistent FPI outflows, tightening liquidity added undue pressure on the currency. The oil prices accelerated sharply and given our dependence on oil imports, the imports bill is expected to edge up significantly. The supply related disruptions pushed investors to move towards safe heaven assets and boosted the dollar demand. In the coming year, rupee is expected to witness bouts of uncertainty given escalated concerns on geopolitical front, risk of elevated inflation especially due to oil prices and widening of current account deficit. These are expected to weigh in on currency. Despite this, India macro fundamentals remains much stronger than its global counterparts. Overall, we expect INR to trade in the range of 93-95/\$ in the near term supported by strong forex reserves, with focus on crude price movement and global central bank actions.

What drove the INR this year?

The performance of INR this year has been interesting mix of upswing and downswing. The currency has depreciated by 9.8% this year against a 2.5% fall noted in FY25. For the same period, dollar index has weakened by 3.2% against a fall of 0.3% in the previous year. This is compared to steepest decline noted back in FY12, when the currency depreciated by 12.4% and that was on account of the taper tantrum and was more domestic led than the current one. Notably, not only INR but other Asian currencies have also weakened during the same period, with yen and yuan down by 5.5% and 5% respectively from last year.

It is important to understand the major fall in the INR this year is largely on account of external factors rather than the domestic ones. There are various factors responsible for driving down the rupee, including the uncertainty on account of the possible US-India trade deal wherein the US had initially imposed tariffs as high as 50%. This happened back in Aug'25 and later in Feb'26 a revised trade deal was agreed upon bringing the tariff down to 18%. Not only the forex market but the tariff concerns even weighed on the equity and bond market. The ongoing geopolitical conflict worsened the situation across the globe, bringing forth heightened volatility across financial markets and resulting in sustained foreign capital outflow.

Fig 1: INR movement



Source: Bloomberg, Bank of Baroda Research

The dollar index too remained under pressure through the year, though performed better than INR this year. The range of factors responsible for dollar movement included as uncertainty on tariffs, fiscal pressure given the risk of widening deficit, concerns over Fed independence as well as the unprecedented US government shutdown this year.

One-month in to the West Asia conflict has brought forth the fears of supply chain disruption and energy woes, which became more prominent as the currency breached the 94/\$ mark and closed at 94.83/\$ a record low. The crude oil prices surpassed the 100\$/bbl mark as tensions flared up, surging by more than 60% during this last 1-month. With higher oil and closure of the strait of Hormuz the risk of higher imported inflation became more imminent. As part of spillover effect, the downside risk to exports that was already under pressure through the year heightened further, across sectors in the face of ongoing crisis. This has impacted global markets, including India.

RBI measures

RBI this year was clear in its mandate wherein it stated with immense clarity that they rely on efficiency of markets and do not target any specific price band for rupee, thereby allowing market to determine the prices. However, they will work towards addressing any excess volatility. Based on the same, RBI pulled in various measures through the year to support rupee. These included the announcement by the RBI Governor back in Oct'25 to allow authorized dealers- banks to lend INR to non-residents from the neighboring countries such as Bhutan, Sri Lanka and Nepal as part of cross border transactions.

In order to support rupee, RBI came up with revised guidelines for External Commercial Borrowing (ECB) framework. The ECB policy was revised to increase the automatic route limit to US\$ 1bn (from US\$ 750 mn) or 300% of net worth whichever is higher. A uniform MAMP (minimum average maturity period) at 3 years have been standardized from the earlier which carried a range of 3-10 years. Specifically for currency, the ECB proceeds will be credited in a rupee account by the end of the month. The rupee denominated loans or bonds can be used for capex. Borrowers will be allowed to convert from rupee to foreign currency which was previously restricted. Thereby helping companies manage their currency exposure and providing currency flexibility.

Amidst growing concerns of capital flight and in order to manage the speculative bet against the currency, RBI stepped in to defend the ongoing weakness in the currency, specifically since the onslaught of the US-Iran war. The Central Bank instructed the banks to limit their foreign currency exposure to US\$ 100mn by the end of each business day. The banks have to comply with this directive by 10 Apr 2026. This is more of regulatory tightening than direct intervention, in order to better manage the forex reserves. This announcement acted as an immediate respite, with a temporary pause noted in the free fall of the currency.

Outlook

FY26 was the turbulent year for the global financial market. Indian markets too suffered from the evolving global geopolitical dynamics, as it kept investors on the edge with uncertainty at play. INR was under deep pressure this year, as it absorbed one shock after another. The currency has suffered on the back of sustained FPI outflows, fall in exports and lower BoP.

Going ahead, we expect that given the challenging global environment, RBI may not actively intervene just as it did last year; and can even take a step ahead and stop with trimming its forward book. This can be a double edged sword as it will indeed lead to further depreciation, but will also be positive for exports which is expected to have an adverse impact due to the ongoing geopolitical conflict. Overall, we expect rupee to trade in the range of 93-95/\$ in the near term, with downside risks.

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