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USD/INR

USD/INR pair to trade between 85 and 86 till the FY2026 Union Budget

DECEMBER 2024

Highlights

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USD/INR pair crossed the 85-mark for the first time on December 19, 2024.

ICRA expects the pair to trade between INR 85 and INR 86 in the near term.

- The USD/INR pair crossed the 85-mark for the first time on December 19, 2024, following the paring of rate cut expectations for 2025 by the US Federal Reserve. The pair has recorded a mild depreciation of 1.8% in FY2025 so far (till December 18, 2024), amid intervention by the Reserve Bank of India (RBI), which has also aided in curtailing volatility over the last 15 months.
- The US Fed members now expect just 50 bps rate cuts in 2025 as against 100 bps earlier. This, along with the likelihood of a continued rise in the Dollar Index (DXY), owing to potential policy actions in the US, poses concerns for emerging market (EM) currencies. However, sharp upticks in the DXY in the past have not necessarily led to a large depreciation in the USD/INR pair, which is also linked to India's macro fundamentals.
- The INR has outperformed most EM currencies since March 2023, triggering concerns about India's export competitiveness. However, a sharper depreciation against the USD, vs. other currencies, has not led to corresponding increase in export market share in the past. While the USD/INR pair fell by ~26% during CY2013-23, sharper than most Asian countries, India's share of global exports rose by a meagre 15 bps in this period.
- Going forward, the projected CAD of ~$40-43 billion (1.0% of GDP) for FY2026 is likely to be adequately financed, even though a potential dip in capital flows could lead to a lower accretion to reserves. Moreover, with India's weight in global bond index reaching its peak by end-March 2025, the favourable impact of index inclusion on FPI debt inflows is likely to fade in FY2026, after the large inflows seen in FY2024-25.
- The proposed tariffs on China under the second Trump administration are likely to exert pressure on the Yuan and other EM currencies. However, any retaliatory actions by China would also have a bearing on currency outcomes. Overall, this would create considerable uncertainty in financial and currency markets, and healthy macroeconomic fundamentals will be key to limit volatility, and spillovers into the real sector.
- Prior episodes wherein the currency was under pressure, such as the taper tantrum, US-China trade war, and Russia-Ukraine war, suggest that healthy macroeconomic fundamentals are paramount to limit adverse currency outcomes. With India's macros appearing favourable, ICRA expects the USD/INR pair to trade between 85 and 86 till the FY2026 Union Budget in early-February 2025, amidst heightened global volatility.

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Thank You!