

Rupee Stabilizes: The Worst May Be Over

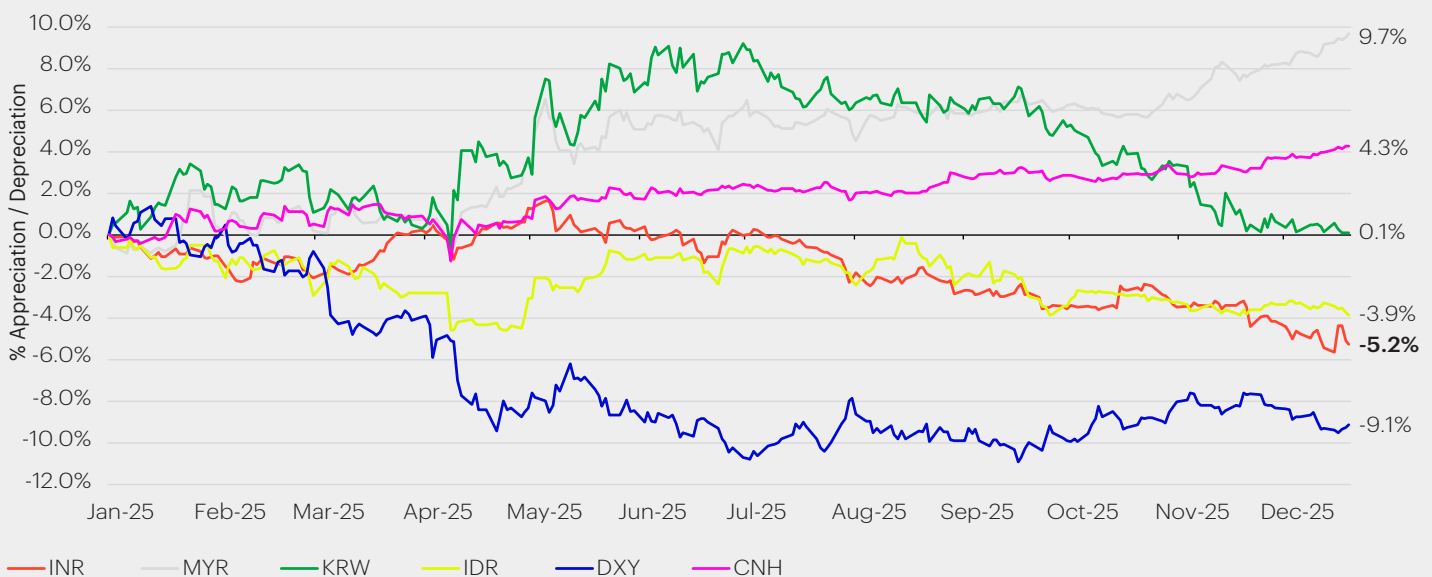


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The Indian rupee breached the psychological mark of 90 versus the US dollar in the first week of December'25 marking the quickest fall in recent times. The rupee has depreciated ~5.2% YTD (as of December 19, 2025) against the US dollar since December 2024, underperforming all other major Asian currencies. The rupee's depreciation beyond the 90 mark against the dollar has raised questions about the interplay between domestic economic fundamentals and external factors, sparking a nuanced debate.

On the surface, the macro-economic indicators appear supportive. Crude oil prices have softened. Brent crude oil prices fell to \$63.6 per barrel on average in November'25, 1.6% lower on-month and 14.5% lower on-year, providing relief on the import bill. Inflation has cooled to below 1%, easing pressure on households. The gross domestic product (GDP) has surprised on the upside, marking the strongest print in 6 quarters. Ideally, all these factors should have bolstered the currency. Yet, the local unit has been falling. At the current level, India has underperformed major Asian peers in 2025 and it will continue to face pressure without central bank intervention. This slide underscores a divergence in India's domestic and external macro economic position.

Rupee has underperformed most major Asian peers in 2025



Source: Refinitiv

Performance of Asian currencies vs. U.S. Dollar from January 01, 2025 till December 19, 2025.

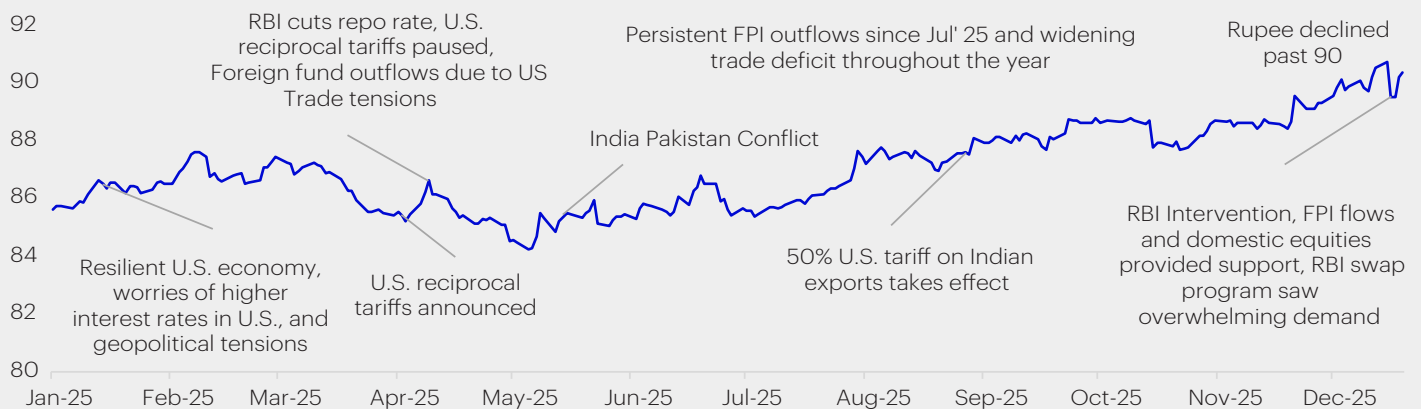
Currency codes: INR – Indian Rupee, MYR – Malaysian Ringgit, KRW – South Korean Won, IDR – Indonesian Rupiah, DXY – Dollar Index, CNH – Chinese Yuan Offshore

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A closer look reveals that a host of factors are also at play viz. Foreign Portfolio Investor (FPI) outflows, balance of payment disequilibrium, the RBI's forex strategy, continuing logjam on the Indo-US trade deal, interest rate differentials, risk sentiment, commodity prices (especially, elevated crude oil prices), capital flows, and geopolitical uncertainties, to name some, have piled on sustained pressure on the rupee.

The RBI's intervention and India's macroeconomic stability provide support, but global dynamics are dominating the short-term trend. We believe the local currency will continue to be under pressure until trade talks take centre stage, foreign money starts coming back and central bank intervenes.

Key Events for USD/INR-2025



Source: Refinitiv
Data as on December 19, 2025

After breaching the 90 mark against the dollar, the rupee staged a recovery, appreciating against the greenback from the third week onwards. The rupee has exhibited a modest rebound in recent sessions (89.5725 as of December 22), suggesting a slight easing of dollar strength and improved risk appetite. While it's too early to call a trend, this development hints at a potential stabilization in the near term.

The INR/USD Impact

The INR/USD exchange rate has far-reaching implications for various stakeholders. For businesses, fluctuations in the exchange rate can lead to increased costs of imported raw materials, squeezing profit margins and influencing investment decisions & supply chain management. Policymakers face challenges in maintaining low inflation, promoting economic growth, and ensuring financial stability. Meanwhile, households feel the pinch through increased costs of travel and remittances, as well as impacts savings, investments, and overall financial planning. A weaker rupee can have a ripple effect on the economy, making it essential to monitor this critical exchange rate.

Why did Rupee weaken despite strong fundamentals?

Uncertainty regarding Indo-US trade deal: Delays in finalising the trade agreement between India and the US have created doubts about future tariffs and export competitiveness, weakening confidence in India's external sector and mounting pressure on the rupee. US tariffs on Indian exports—some rising by 50%—have hit business confidence to a great extent.

U.S. tariff actions and prolonged uncertainty around a US-India trade deal weighed on the Indian rupee this year mainly through sentiment and capital-flow channels rather than direct trade losses. The lack of clarity on export access and sector-specific duties reduced confidence in India's

external balance outlook, prompting foreign portfolio outflows, slower inflows, and higher corporate hedging demand for dollars. At the same time, episodes of global risk aversion linked to trade tensions intermittently strengthened the U.S. dollar, amplifying pressure on USD/INR even though India's domestic fundamentals remained relatively stable. The RBI intervened to smooth volatility rather than defend a specific level, resulting in a gradual, controlled depreciation of the rupee—a slow grind weaker rather than a disorderly fall.

Strong demand for dollar from corporates: Indian corporates, which heavily rely on imports, such as oil, electronics and machinery require dollars in large sums to settle international obligations, boosting demand for the greenback. This persistent dollar demand has contributed significantly to the rupee hitting new all-time lows.

Higher trade deficit: A widening trade deficit (particularly record high deficit in October 2025) has exacerbated FPI outflows and further exerted pressure on the rupee. A trade deficit often means that exports are weak or growing slower than imports. This reduces the amount of foreign currency (US dollars) flowing into India from export earnings, which lowers the demand for the rupee in the international markets. The shortfall has to be covered, often by using a country's foreign exchange reserves or attracting capital inflows. When reserves are depleted or capital inflows are insufficient, it puts significant pressure on the rupee to weaken further.

Merchandise exports dropped 11.8% in October 2025, while imports surged 16.6%. With exports weakening and imports rising sharply, the trade deficit has widened, adding pressure on the rupee. However, after a widening of trade deficit in October, the month of November saw narrowing of trade deficit to a 5 month low after India's total exports (Merchandise and Services combined) for November 2025 registered a positive growth of 15.52% vis-à-vis November 2024.

Major drivers of exports growth include engineering goods, electronic goods, gems & jewellery, drugs & petroleum products. After two months of negative growth in exports to USA, the month of November saw a YoY 22.61% increase in exports amidst positive trade talks between the two countries.

High gold imports: Gold imports surged nearly 200% in October. Domestic high gold prices further worsened the import bill, and although rising prices boosted the value of gold reserves, it was not enough to offset the overall losses. Elevated gold imports have widened the current account deficit and led to further depreciation of the rupee in October. However, the month of November saw a 59% decline in gold imports compared to the month of October which saw higher demand amidst the festive season.

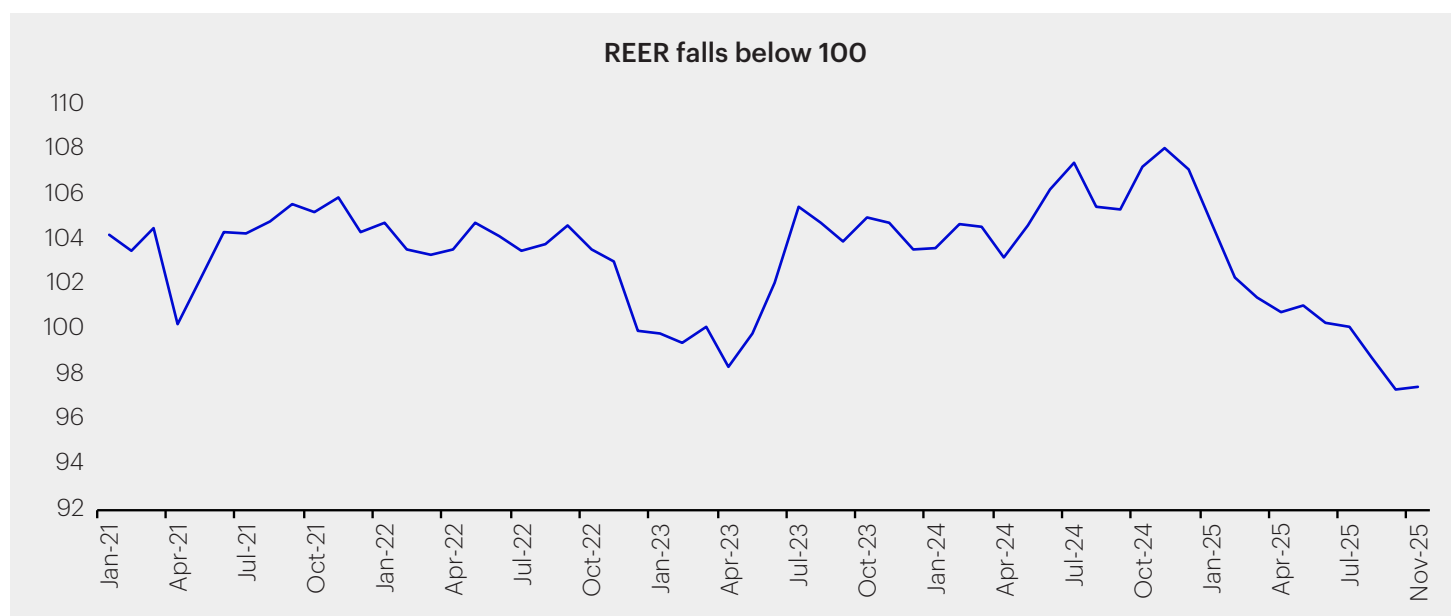
FPI flows: FPI pulled out Rs. 155,505 crores from Indian equities in this calendar year (till December 23, 2025) leading to weakening of the rupee. Higher valuations are being seen as another reason for FPIs to flock their capital to other economies where they could receive higher returns than in India, influencing portfolio flows. At the same time, global geopolitical risks have increased demand for the US dollar as a safe-haven asset.

Limited visible RBI intervention in the forex market: The RBI typically intervenes in the foreign exchange market to prevent a sharp or excessive fall of the rupee and curb volatility. It does not target any band for the rupee in the forex market and allows the domestic currency to find its own correct level. The RBI has been allowing gradual depreciation (a "crawl") rather than aggressively defending a fixed level. It also announced the three-year USD/INR Buy Sell swap of \$5 billion dollars this month to boost liquidity in the system.

The REER view

The real effective exchange rate (REER) is a way of checking whether the rupee is over-priced or cheap compared with the currencies of India's main trading partner after adjusting for inflation differences. Instead of solely looking at the dollar/rupee exchange rate, REER takes a basket of currencies, weights them by how much India trades with each country and then adjusts for how fast prices are rising in India vs. abroad.

Recent RBI data shows that the rupee's REER has dropped from the record high of about 108 in late 2024 to below 100 in 2025, which means it has moved from being overvalued to slightly undervalued, making exports more competitive and imports costlier. RBI has adopted a managed floating exchange rate policy allowing the rupee to float instead of showcasing instead of artificially protecting a predictable ceiling.



Source: RBI
Data as of November 2025

Economic implications for India

Imported inflation

The primary negative impact stems from India's high reliance on imports for essential goods.

A weaker rupee makes imports such as crude oil (India imports around 85% of its fuel), electronics, gold and fertilisers more expensive. This increases input costs for industries and transportation, which is passed on to consumers, leading to higher domestic inflation (cost-push inflation).

Widening current account deficit (CAD)

A higher import bill in rupee terms can widen India's trade and current account deficits, even if import volumes remain unchanged, putting further pressure on the currency.

Increased foreign debt burden

The cost of servicing foreign-currency-denominated loans increases in rupee terms, raising the debt burden for companies and the government.

Capital flight risk

Persistent rupee depreciation can erode foreign investor confidence, leading to further outflows of FPI capital from the Indian equity and debt markets, creating a cycle of further depreciation.

Higher costs for households and students

Everyday expenses, including fuel and cooking oil, become more expensive. For the large number of Indian students studying abroad, tuition fees and living costs rise significantly in rupee terms, increasing the burden of education loans.

Fiscal pressure

Higher cost of imported items such as fertilisers and LPG can increase the government's subsidy burden, potentially straining fiscal finances.

Benefits of weaker rupee remains limited due to India's high import dependence and rising global protectionism.

Boosts exports

A weaker rupee can directly increase rupee earnings, boosting margins. However, its positive impact is limited by rising costs of imported intermediates, weak global demand, and protectionism. These factors can undermine the advantages of a weaker currency, and deteriorating global conditions such as slowing growth and costlier inputs can offset the benefits, ultimately delivering uneven outcomes across sectors.

Investment push

A weaker rupee presents an attractive investment opportunity for foreign investors, enabling them to acquire Indian assets at a lower cost. This could lead to an increase in Foreign Direct Investment (FDI) inflows, as investors seek to capitalize on the depreciated currency and tap into India's growth potential.

Higher remittance value

The depreciating rupee has also created a temporary advantage for NRIs, as each dollar sent back to India can be converted into more rupees. This motivates NRIs to remit larger amounts, providing a financial boost to households and helping them meet essential expenses such as school fees, rent, and loan repayments, ultimately injecting more money into the economy.

Sector-wise impact

Negative: A depreciating rupee hurts sectors such as aviation, oil & gas, paints and Fast Moving Consumer Goods (FMCG) as they heavily rely on dollar-denominated imports (fuel, raw materials, components), making their operational costs soar and squeezing profit margins, forcing potential price hikes for consumers. While exporters gain, these import-dependent sectors face higher input costs, affecting profitability and stock performance, with aviation especially being hit by fuel/lease costs and FMCG by raw materials, such as edible oils. Also depreciating rupee makes it more expensive for Indians to pursue higher education and cost of educational materials also becomes expensive which adversely impacts the investment decision and human capital of the country.

Positive: A depreciating rupee is generally considered positive for sectors that rely heavily on exports and earn revenue in foreign currencies, such as the US dollar. Information Technology (IT) and Information Technology Enabled Services (ITES), pharma, leather and related products and textile industries are often cited as beneficiaries as they primarily export goods and services. These sectors benefit from higher revenue in rupee terms, competitive advantage and currency conversion gains. However, the positive impact can be partially offset by the cost of imported raw materials or components used in production, which become more expensive.

Mixed: Sectors such as Gems & Jewellery, chemical & chemical products have mixed impact of rupee depreciation due to increase in export revenues but elevated import costs erode the gains.

Disclaimer: The sectors referred above are for the purpose of explaining the movement of Rupee and should not be construed as recommendations from Invesco Asset Management (India) Pvt. Limited. Schemes of Invesco Mutual Fund may or may not have any present or future positions in these sectors.

Looking ahead

India may see improved inflows as global rates begin easing, risk appetite returns and domestic earnings remain resilient. Any positive development in the US-India trade discussions could also restore confidence.

While the rupee's breach of the 90-mark is undeniably symbolic, it is not a sign of economic distress as much as it is a reflection of a strong dollar, global risk aversion and temporary trade-flow imbalance. The slide past 90 is indeed an inflection point—but not a breaking point. The economy is fundamentally very strong, the reserve buffer is substantial, and the RBI has tools to attract capital and manage volatility.

The fundamentals of the Indian economy remain intact, and the RBI retains considerable firepower to curb sharp movements. In the weeks ahead, the currency will take its cues from global rate expectations, foreign investor flows and clarity on India's trade & geopolitical outlook.

The path forward will likely be one of gradual stabilisation as global conditions normalise and domestic strengths reassert themselves. In the larger scheme of India's growth story, the rupee's current weakness is a bump, not a bend in the road.

While the rupee's slide past 90 against the US dollar made headlines, its potential comeback could be a more significant story. A sustained recovery would ease inflation, boost purchasing power, and enhance India's attractiveness to foreign investors.

A stronger rupee would also underscore the resilience of the Indian economy and the effectiveness of the RBI's monetary policy. As market participants watch for signs of a sustained recovery, a comeback could be a significant milestone, indicating a shift in market sentiment and a potential reversal of the rupee's downtrend.

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