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Market-Implied Path (Fed-Funds Futures snapshot) Meeting	Implied Rate	(Table 1) Cumulative Change
28 Jan 2026	3.62%	-01 bp
18 Mar 2026	3.58%	-06 bp
29 Apr 2026	3.54 %	-10 bp
28 Oct 2026	3.21 %	-42 bp
09 Dec 2026	3.17%	-46 bp

Next meeting probabilities: **No change 97 %**, **25 bps cut 3 %**

Global markets were shaped by two dominant forces this week: **persistent uncertainty around U.S. tariff policy and renewed speculation over coordinated FX intervention involving U.S. and Japanese authorities**. Together, these dynamics undermined confidence in the U.S. dollar, pushed real assets higher, and reinforced currency divergence across Asia.

The U.S. dollar extended its decline (-2.3%) for a fourth consecutive session, sliding toward its weakest level since 2022 as investor sentiment toward the greenback deteriorated. Market participants trimmed dollar exposure ahead of the upcoming Fed meeting, amid rising political uncertainty surrounding the appointment of the next Fed Chair and renewed concerns over a potential U.S. government shutdown. **Meanwhile, U.S. data are holding up for now, suggesting U.S. dollar selling is likely to pause heading into the Fed’s policy decision.**

FX volatility intensified late in the week as speculation grew around potential Japanese yen intervention, following reports that the U.S. Treasury had been engaging market participants. USD/JPY fell to low of 153.30 (-2.3% fall). Meanwhile the Bank of Japan held rates steady with one dissenting vote, upgrading both growth and inflation forecasts adding complexity to the policy outlook and reinforcing market focus on Japan as a global catalyst.

Attention then shifted decisively to Japan’s bond market, where a historic selloff sent shockwaves through global rates. Japan’s 30-year government bond yield recorded its largest single-day jump on record, while the 10-year yield climbed to its highest level since 1999.

U.S. Treasury yields reflected these cross-currents. Early in the week, yields eased modestly amid ongoing geopolitical and trade uncertainty, with the 10-year yield currently at 4.21%, the 2-year at 3.59%, and the 30-year at 4.80%. However, the broader bias remained upward.

Meanwhile, strong U.S. economic data continued to reinforce confidence in near-term growth, while simultaneously validating the Fed’s reluctance to rush into rate cuts. Consumer sentiment rose to a five-month high, supporting the view that U.S. economic momentum remains resilient. At the same time, investors increasingly acknowledge the risk that inflation may prove more persistent into 2026, particularly against the backdrop of fiscal expansion and tight labor conditions. This tension between solid growth and sticky inflation remains central to market pricing.

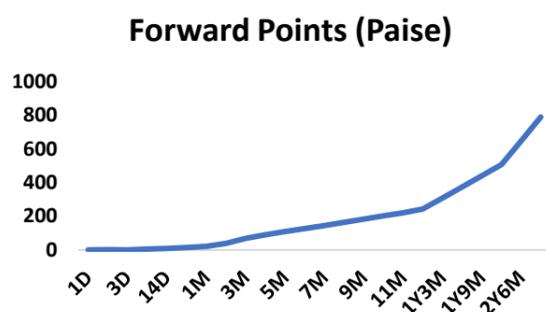
Against this backdrop, the Fed is widely expected to remain on hold at its upcoming meeting, emphasizing patience and data dependence rather than offering clear guidance on the timing of rate cuts. Meanwhile prediction markets repriced sharply around the race for the next Fed Chair. The field has widened beyond the initial “two Kevins” narrative, with BlackRock’s Rick Rieder surging to an implied 50% probability on Polymarket.

In Asia, alongside ongoing India-U.S. trade engagement, **India and the EU concluded a landmark free trade agreement**. Covering an economic bloc representing ~25% of global GDP and nearly one-third of global trade, the pact complements India’s agreements with the UK and EFTA and creates a combined market of nearly two billion people at a time when global trade links are under rising geopolitical strain.

Looking ahead, markets face a dense calendar of catalysts, including the Fed’s first policy decision of the year and key global forums. The central question remains whether strong growth, trade tariff and fiscal expansion will keep inflation sticky forcing markets to accept structurally higher long-term yields or whether productivity gains ultimately allow rates to ease without reigniting inflation. For now, confidence in the U.S. remains intact, but increasingly conditional. Bond markets are watching fiscal discipline closely, term premia are rising quietly. Also watch for legal clarity on tariff authority and the President’s power to remove Fed Governor Lisa Cook, as well as U.S. PPI, consumer confidence, productivity, and factory orders this week.

Rupee faces a make-or-break week after ₹91.95/\$ lows, with Fed cues, Budget expectations, FPI outflows and trade-deal signals deciding a pullback toward ₹90/\$

USD/INR forward curve (fig1)



Source: Refinitiv workspace

REER fell to 95.30 in Dec'25 from 97.51 in Nov'25, remaining undervalued despite RBI net FX sales of \$9.71bln in Nov'25.

Rupee: Downside Cushioned by Strong Buffers and Policy Support

The rupee remained under pressure last week, extending its weakness to a low of 91.98 per dollar, taking its January depreciation to over 2% and adding to a 5% decline in 2025. The persistent drag has come from weak foreign capital inflows, with steady importer hedging amid downside fears and exporters delaying dollar sales, keeping flows skewed against the currency.

However, the tone improved at the start of this week as risk appetite picked up after India and the European Union agreed to a free trade agreement touted as the “mother of all deals” while broader dollar weakness provided additional relief. The dollar index slipped to 96.81 on Monday, its lowest level since September 17. Sentiment was further supported by comments from U.S. Treasury Secretary Scott Bessent, who signalled the possibility of removing an additional 25% tariff on India following a sharp cut in Indian imports of Russian oil.

USD/INR forward premiums remain structurally elevated, even as near-term tenors saw a modest pullback following RBI liquidity measures. Forward points eased after the RBI announced fresh INR liquidity infusion, including a \$10bn 3-year buy/sell swap and INR 1 trillion in bond purchases, though declines were limited by strong corporate hedging demand. The 1-year implied yield briefly dipped to a three-week low near 2.55% before stabilising around ~2.6%, as importers stepped in to lock covers on dips.

The forward curve (Fig 1) continues to steepen beyond one year, reflecting term risk premia and cost-of-carry dynamics rather than a directional forecast for spot. Longer tenors remain well supported, with 2-year forwards (~507 paise) implying ~3.0% annualised carry and 3-year forwards (~758-790 paise) closer to ~3.1-3.2%, pricing duration risk, balance-sheet constraints, and uncertainty around global rates and INR liquidity conditions.

Overall, forward premiums continue to function as a hedging-cost and liquidity signal rather than an outright INR depreciation call. RBI FX swaps and bond purchases have helped cap volatility and prevent sharp spikes, but persistent corporate dollar demand keeps the curve firm. Markets now look to upcoming RBI swap auction outcomes and the February policy decision for confirmation on whether the recent softening in far-forward premiums can extend or proves temporary.

For rupee near-term bias remains data-dependent and externally driven, with global yield dynamics, portfolio flows, and evolving trade-policy signals continuing to outweigh domestic fundamentals in determining currency direction. That said, the 92.00 level continues to act as a key near-term pivot. Despite some support from a softer dollar and easing geopolitical tensions around Greenland, the currency remains vulnerable amid a persistent FPI exodus, with foreign investors having pulled out over \$3.5 billion so far this month.

Foreign Portfolio Investors (FPIs) have pulled out \$3.71bln (CY26) from Indian equity markets as of 23rd Jan'26. Even though, we saw the trend reversed in Oct'25 with positive inflows but turned negative again in Nov'25 & Dec'25 and continues in Jan'26. FPIs aggressively sold *in equities* ~\$1191mln vis-à-vis *outflows of* ~\$466mln on a WoW basis. Debt markets also turned outflows to the tune of ~\$231mln vis-a-vis ~\$219mln inflows a week ago. FAR flows, at \$717mln (CY26), including a ~\$280mln inflow so far last week.

The rupee's REER (2015-16=100) fell further to 95.30 in Dec'25 from 97.51 in Nov'25, extending the sharp correction from the Nov'24 peak of 108.08. Despite the currency being undervalued (REER <100), the recent weakness has been driven more by sentiment around US trade-tariff dynamics than by fundamentals. The RBI continued to smooth volatility, recording net FX sales of \$9.71 bln in Nov'25, compared with \$11.88 bln in Oct'25. Any positive progress on an India-US BTA could lift the REER back toward the neutral 100 level, suggesting scope for a real-value correction in the months ahead.

India's foreign exchange reserves climbed back above the \$700 billion mark in the week ended Jan 16, recording the largest weekly increase in over 10 months and crossing this threshold for the first time since October. Reserves remain just below the lifetime high of \$704.89 billion recorded in the week ended Sept 27, 2024. The rise was led by a sharp increase in foreign currency assets, which jumped \$9.65 billion WoW the biggest gain since March to \$560.52 billion. Gold reserves also rose \$4.62 billion WoW to a record high of \$117.45 billion.

Brent crude traded in the low-to-mid \$60/bbl range, easing after a >2% rebound in the prior session as markets reassessed supply risks from U.S. winter storms and geopolitical tensions involving Iran. Prices were capped by ample global supply and larger-than-expected U.S. inventory builds, keeping sentiment cautious amid mixed demand signals. Brent settled at \$65.59/bbl (-0.4%), while WTI closed at \$60.63/bbl (-0.7%). Near term, Brent is expected to remain range-bound, with direction driven by U.S. inventory data, geopolitical developments, and any fresh cues from OPEC+ or China demand. On a WoW basis, prices are up ~1% but remain ~17% lower YoY.

India-US Trade Deal: Key Developments

Date	Development (Key Point)
06 Jan 2026	The US administration reiterated that existing and proposed tariffs on trading partners, including India, remain under review as part of a broader trade-policy reset.
10–12 Jan 2026	India sharply reduced imports of Russian crude oil, aligning more closely with Western sanctions and easing bilateral frictions with the US.
17 Jan 2026	US Treasury Secretary Scott Bessent stated that the US could consider removing the additional 25% tariff on India following changes in India's energy import strategy.
22 Jan 2026	U.S. President Donald Trump, speaking at Davos, adopted a conciliatory tone on India-US trade relations and highlighted the scope for a mutually beneficial trade agreement.
25 Jan 2026	Officials on both sides indicated that discussions around a potential India-US Bilateral Trade Agreement (BTA) are gaining momentum, though no formal timeline has been announced.

Source: Various Media articles

Outlook (INR - ₹ view):

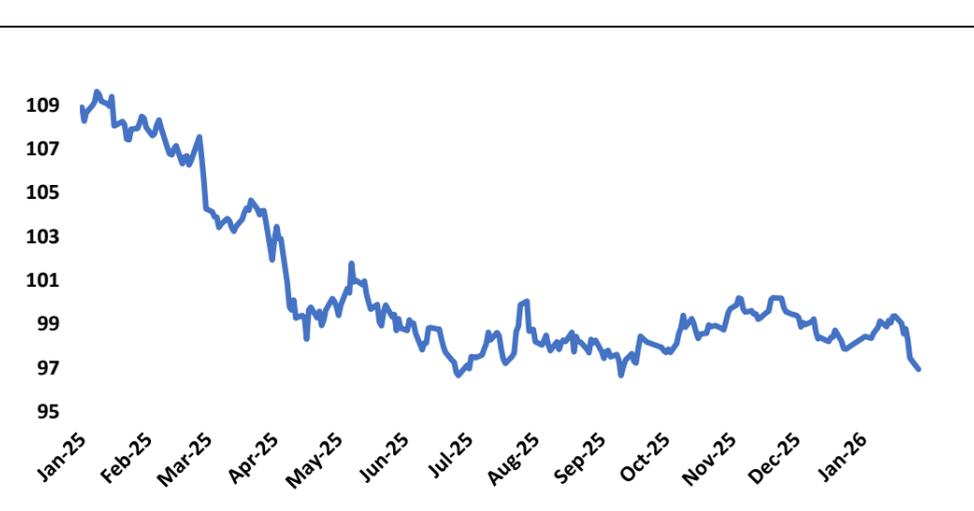
Looking ahead to the next week, the Rupee's direction will be dictated by high-impact events: the US Fed Policy decision (Jan 28-29), which will set the tone for the Dollar Index, and the pre-Budget positioning in India as markets anticipate the February 1 Union Budget. A robust primary market pipeline is expected to provide a crucial buffer of dollar inflows. With the US-India trade deal entering a hopeful phase following Trump's warm rhetoric at Davos, any concrete announcement next week could be the catalyst needed to decisively pull the Rupee back.

From a technical standpoint, the rupee is expected to trade between ₹89.90-91.90/\$ throughout the next month. Sustained domestic equity inflows or tangible progress in India-US trade negotiations could strengthen the INR toward ₹89.20/\$, with ₹89.50/\$ acting as a key interim support. If an India-US BTA is finalized; the appreciation threshold for the rupee could shift meaningfully. Conversely, any bearish catalysts such as delays in resolving US-India tariff issues are likely to face strong resistance near fresh all-time lows of ₹91.75/\$, a break above this zone could trigger a move toward ₹91.90/\$. Overall, geopolitical and tariff developments will remain central drivers of market sentiment.

We have consistently noted that the rupee's recent weakness reflects overshooting due to negative sentiment rather than fundamentals. Based on the Real Effective Exchange Rate (REER), the currency is now undervalued by ~5%. Our analysis indicates that over a three-year horizon, the rupee typically adjusts via an average annual depreciation of 3-4%, aligned with India-US inflation and interest rate differentials. Given that the rupee has already weakened by ~7% this FY26, we do not expect significant or runaway depreciation pressures to continue.

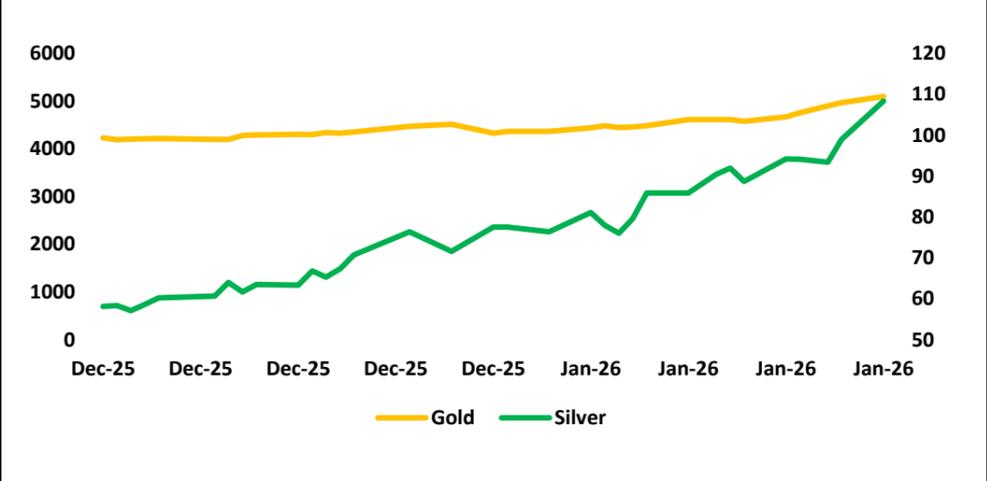
The rupee's downside appears limited, while any Fed-driven dollar softness or concrete progress on the India-US trade deal could trigger a stabilisation-led rebound rather than further depreciation.

The US dollar sank for a third session, nearing its weakest level since 2022, as sentiment continues to sour on the greenback. (Fig 2)

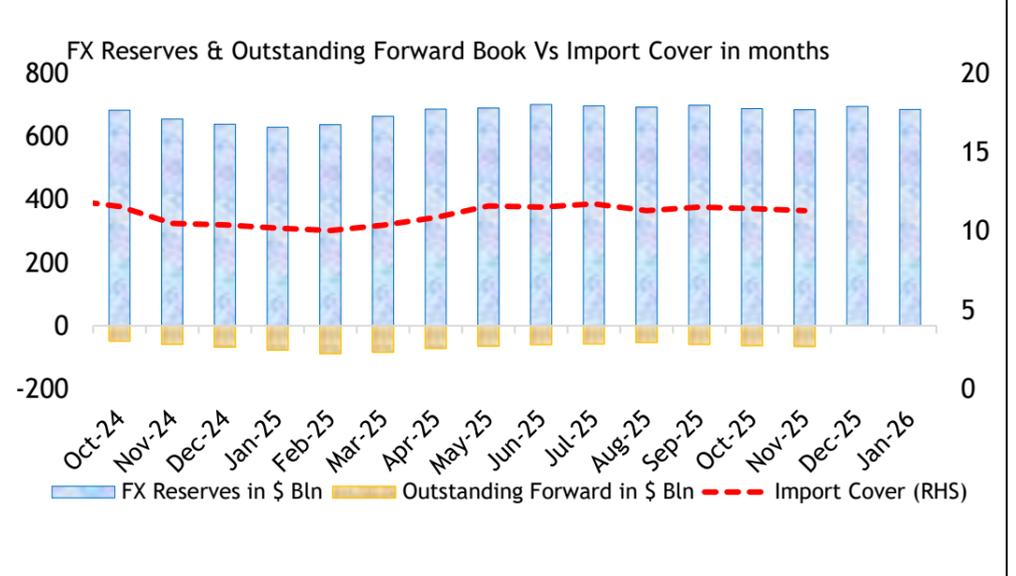


Source: LSEG, UBI research

Gold prices climbed to a fresh all-time high, crossing the \$5,100/oz level on extending its record-breaking amid rising geopolitical tensions and global fiscal risks (Fig 3)

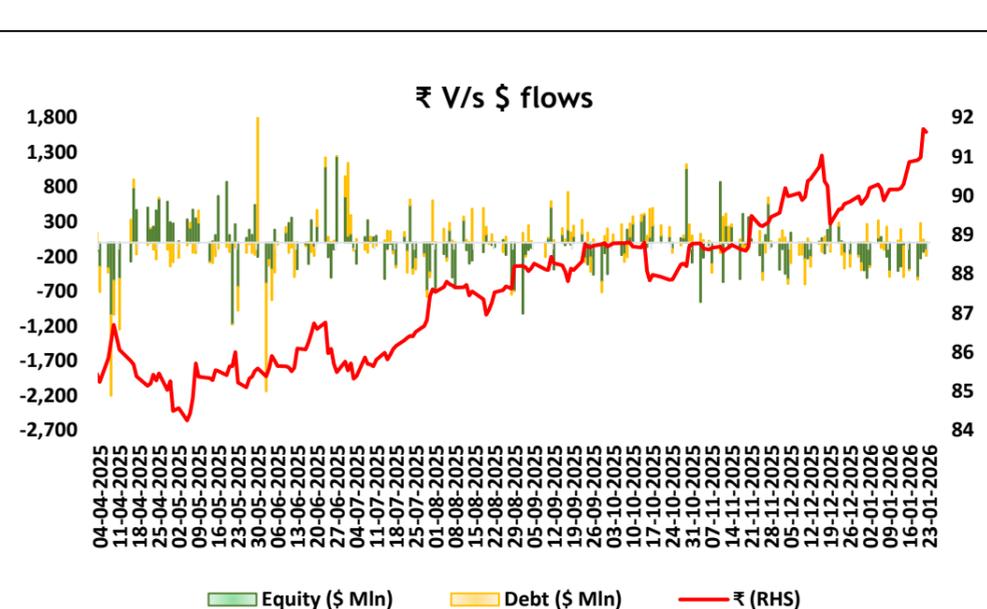


India's foreign exchange reserves climbed back above the \$700 billion mark (Fig 4)



Source: DPIIT, Bloomberg, LSEG Workspace & UBI Research

Rupee weakens amid major FPI outflows (Fig 5)



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