FX weekly: From U.S. Payroll Shock to Hormuz Risk; Rupee Stays Anchored

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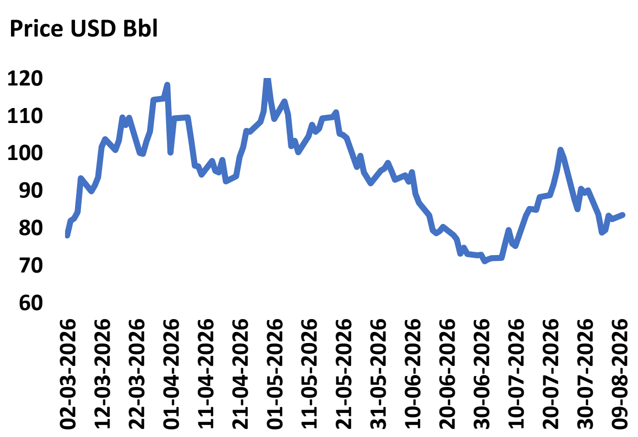
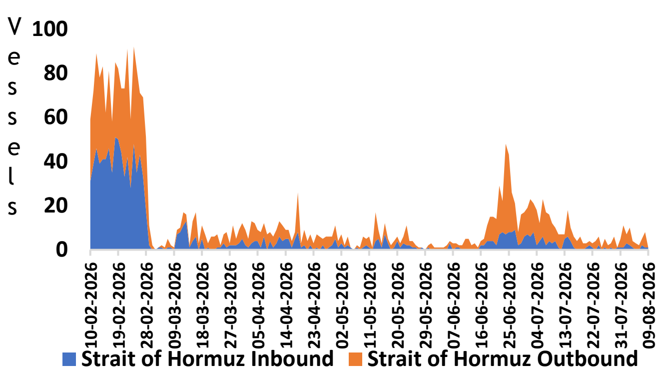
Oil prices remains firm amid confusion over Gulf peace talks (Brent Crude) (Fig 01)



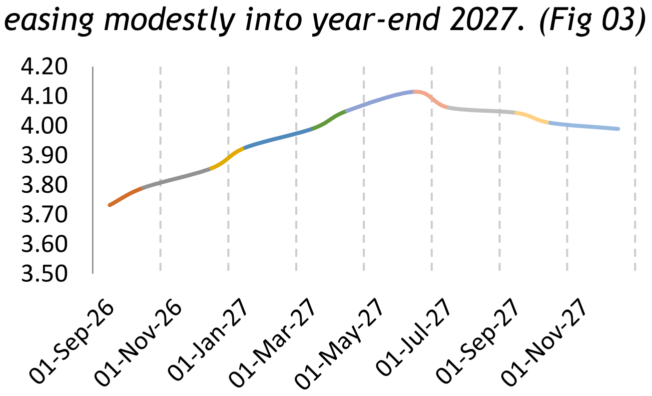
Source: Refinitiv

Vessel Daily Transit via the Strait of Hormuz (Fig 02)



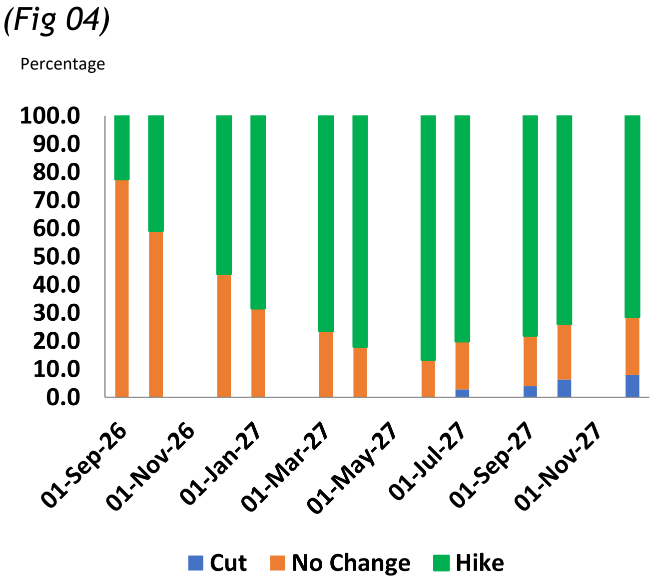
Source: Refinitiv

Fed implied policy rate path, the implied rate path peaks around 4.11% in June 2027 before easing modestly into year-end 2027. (Fig 03)



Source: Refinitiv

Near-term Fed pricing remains cautious: September still favours no change, but the probability of a hike rises above 50% by December and peaks above 85% by June 2027. (Fig 04)



Source: Refinitiv

The week centered on a single jarring data point and its aftershocks. US July payrolls report showed the US economy shed 23,000 jobs – the weakest print since the pandemic era – with the prior two months revised down by a further 103,000. The soft print reinforced the disinflation narrative the Fed has been reluctant to embrace, pulled the Dollar Index below the 100-handle and dragged Treasury yields lower even as the curve continued to steepen. Fed funds futures pricing for a September hike – which had drifted higher through the week on hawkish signalling from Chair Kevin Warsh was cut back sharply on the print, only to be partially unwound over the weekend as per media reports Fed Chair Warsh remains privately prepared to hike if inflation readings released in coming weeks runs hot. That whipsaw, with September-hike odds swinging from the low-60s to close to 50:50 and back above 50% within days, is itself the story: policy uncertainty under the new Fed leadership is now a standalone risk factor, distinct from the underlying data, and it is keeping the long end of the curve elevated even as front-end pricing turns more dovish.

That backdrop provided the setting, but not the headline, for the week's most consequential market event: the first coordinated US-Japan yen-buying intervention since 1998. The move came as the case for further Bank of Japan tightening strengthened, with the summary of opinions from its July meeting showing a more hawkish tilt. The BOJ had kept policy unchanged at its July 31 meeting after raising rates in June, but signalled that another increase could come relatively soon. This reinforced expectation of a possible September hike, with markets pricing around a 50% probability of a September move, rising to 71% by October and 83% by December.

The intervention followed renewed pressure on the yen, which had weakened beyond 163/$ in July after an earlier round of intervention between April 30 and May 6 had helped strengthen it from around 160.7/$ toward 155/$. This time, Japan acted in coordination with the U.S., with central-bank data suggesting around US$59bn may have been deployed on July 30 and a further US$36.6bn on July 31. If confirmed, this could represent the largest yen-buying intervention on record, with official Ministry of Finance figures due on 28 August.

Treasury yields, for their part, are not cooperating with the dollar-bearish narrative in a straightforward way. The steepening move reflects rising term premium and eroding confidence in the Fed's reaction function under its new chair, not falling near-term rate expectations – the two are moving in opposite directions, and that divergence is unusual enough to warrant close monitoring into the September FOMC.

Rounding out the risk picture, the Middle East remains an unresolved cross-asset variable. Oil fell through the week on reports of an Iran-Oman "understanding in principle" on Strait of Hormuz transit rules, but the underlying terms reportedly barring US and Israeli vessels and demanding compensation from "hostile" nations – look considerably less workable than the initial headlines implied, and Washington has not signalled acceptance. Physical shipping activity (FIG2) also remains severely depressed: during 3-9 August, inbound traffic averaged just 1 vessel per day and outbound traffic around 4 vessels, versus roughly 37 inbound and 34 outbound vessels per day before the disruption. With roughly a fifth of global oil trade transiting the strait, any relapse would hit precisely the two variables that are already the swing factors for the September Fed decision – energy-driven CPI prints and Fed credibility. Net-net: we enter the week ahead long volatility on the Fed reaction function, structurally cautious on a durable USD/JPY breakdown, and watching oil as the tail-risk pivot for the whole complex.

What to Watch This Week: The July U.S. CPI print on Wednesday is the key event, with consensus expecting headline inflation at 3.4% y/y and 0.1% m/m, and core CPI at 2.5% y/y. Given the market's heightened sensitivity to the Fed outlook, an upside surprise could quickly revive September hike expectations. Thursday's PPI, followed by Friday's retail sales and University of Michigan sentiment, will help assess whether demand remains resilient despite a softer labour market. The RBA meets Tuesday and is widely expected to hold rates at 4.35%. Geopolitics remains the main event risk: any sign that the Iran-Oman Hormuz understanding is breaking down or being formally accepted by Washington could quickly move oil, inflation expectations and Fed pricing ahead of the CPI release.

Rupee holds its range as reserves swell and oil claws back the risk premium

Improving FPI flows, stronger reserves should keep USD/INR broadly contained, with crude oil and global risk sentiment remaining the key upside risks to the pair

USD/INR remained range-bound through the week, moving from 95.39 on 31-Jul to a low of 95.12 on 5-Aug before edging back to 95.28 on 10-Aug. Softer US payrolls weakened the dollar and LIC-linked FPI equity inflows supported the rupee early in the week, while Brent's three-day rebound later revived oil-import concerns. The net effect is a rupee that remains firmly range-bound between roughly 95.10 and 95.40, with dollar selling by bank, a modestly unwinding forward book, and FCNR(B) flows – continuing to compress volatility rather than defend a specific level, exactly as Governor Malhotra has repeatedly signalled.

The week's flow and policy signals were constructive on balance. FPI flows swung back to a $1.34bn net inflow (from -$211mn), reserves jumped by $10.51bn to a nine-month high of $692.87bn on the back of FCNR-driven FCA accretion, and the RBI both held rates unchanged and explicitly closed the door on premature FCNR(B) withdrawal – removing a specific tail risk that had been circulating in the market through late July. Working against that: cumulative FY27 FPI flows remain net negative, the RBI's forward book continues to skew toward longer-dated dollar shorts even as it unwinds at the front end, and Brent's climb back above $84/bbl. on renewed Hormuz-reopening doubts is the swing factor most capable of reversing this week's calm. We expect the pair to hold a 94.80-95.70 band into this week's US CPI print and the ongoing Strait of Hormuz headline risk.

Fig 5: FCNR (B), ECB and OFCB inflows ($ Bn)

Instrument	As of 17 July, 2026 ($Bn)	1 August 2026 ($Bn)	Growth (%)
FCNR(B) deposits	**17.41**	**36.70**	**111**
ECB's	**1.34**	**1.50**	**12**
OFCB's	**1.97**	**2.57**	**31**
Total mobilisation	**20.72**	**40.81**	**97.0**

RBI's FX FWD maturity profile (Fig6)

Period	Fwd Maturity profile at the end of	
	Jun-26	May-26
Up to 1 month	-8.97	-19.82
1-3 Months	-5.73	-8.86
3 months- 1 year	-24.42	-21.9
More than 1 year	-64.21	-56.07
Total	-103.33	-106.65
		Values in USD Bn.

Key metric	May-26	Jun-26
Total net short ($bn)	-106.66	-103.33
>1Y share of total	52.6%	62.1%
MoM unwind ($bn)		3.33

Drivers: What Helped, What Didn't

+	FPI flows turned net positive at $1.34bn (week to 7-Aug) vs. -$211mn prior week, led by equities ($1.36bn) partly on LIC OFS-linked institutional demand.
+	FX reserves jumped $10.51bn to $692.87bn (week to 31-Jul), led by FCNR(B)/swap-driven FCA accretion; headline reserves closing in on the $700bn mark.
+	RBI kept the FCNR(B) incentive scheme running with no early-closure plan for now; the concessional swap window runs to 30-Sep (swap facility to 16-Oct), removing a flagged near-term tail risk to the NRI-deposit inflow pipeline.
±	RBI held the repo rate at 5.25% for a fourth straight meeting with a neutral stance; Governor Malhotra's tone signalled no urgency to hike, anchoring near-term rate-differential expectations.
±	RBI's forward book: mixed signal. Net short eased to $103.33bn at end-Jun (from $106.66bn), easing the near-term dollar overhang, but the beyond-one-year leg widened to $64.21bn (>60% of the book) – a deferred liability for later.
–	Debt flows stayed marginally negative (-$12mn) and FY27-to-date FPI flows remain net sellers at -$4.70bn, with cumulative equity outflows of -$11.60bn still to be worked off.
–	Brent rebounded for a third straight session to ~$84/bbl on renewed doubt over the Strait of Hormuz reopening – India's oil-import bill sensitivity is the single biggest swing factor on the rupee.
–	A still-uncertain Fed path (Warsh's hawkish private guidance vs. the July payrolls miss) keeps the broad dollar volatile, transmitting two-way pressure to EM Asia FX including INR.
±	INR's move broadly tracked the region – KRW outperformed on exporter dollar-selling, CNY stayed anchored near 6.75 on a resilient trade surplus – so INR is not being singled out by flows, itself a mildly reassuring signal.

Oil, FCNR Inflows and RBI's Growing Room to Manage the Rupee

Brent has risen for three straight sessions to trade near US$84/bbl, reversing part of the previous week's sharp pullback, when prices fell more than 7%. Iran and Oman have reported an "understanding in principle" on Strait of Hormuz transit rules, although Tehran has cautioned that this does not imply an immediate reopening and has, for now, rejected direct talks with Washington. For India, sustained moves in crude feed directly into the import bill and rupee sentiment: US$80-85/bbl remains broadly consistent with rupee stability near current levels, while sustained prices above US$85-90/bbl would pose greater pressure.

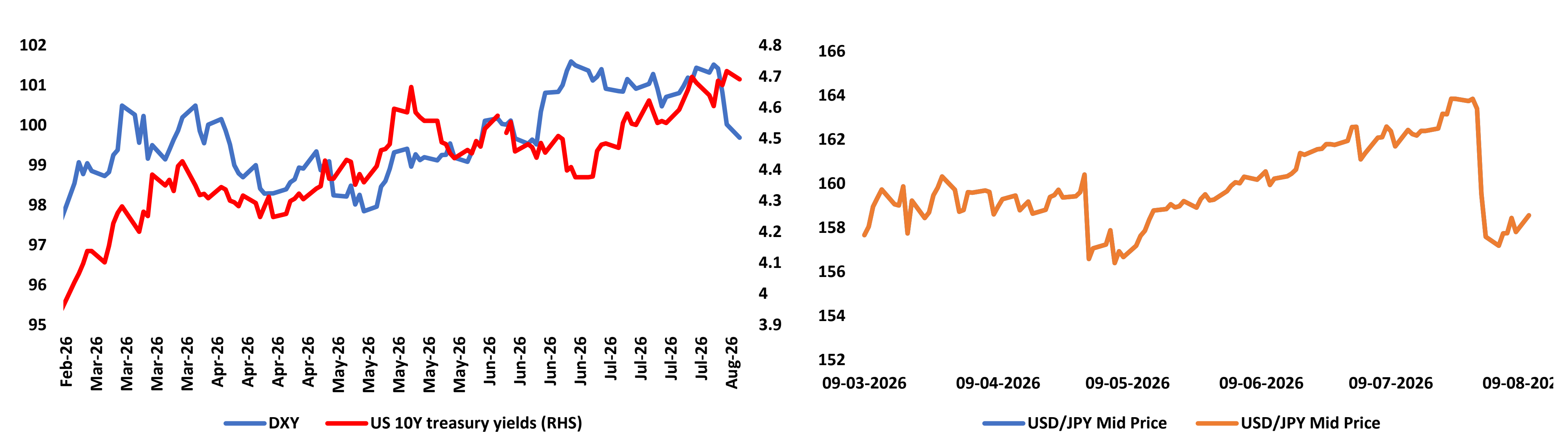
Against this backdrop, the MPC kept the repo rate unchanged at 5.25% for a fourth consecutive meeting on 3-5 August, while retaining a neutral stance. Governor Malhotra's press-conference tone was viewed as unhurried rather than dovish. Addressing market speculation that the RBI could prematurely close the FCNR(B) incentive scheme and zero-cost USD-INR swap window, he said there was currently no proposal to close the scheme early, while adding that the RBI would keep markets informed if inflows accelerated further preserving policy optionality. The concessional window therefore remains open through its original 30 September deadline, with the swap facility available until 16 October, and no formal mobilisation target has been set.

We expect rupee to trade in a range of 94.80/$-95.70/$

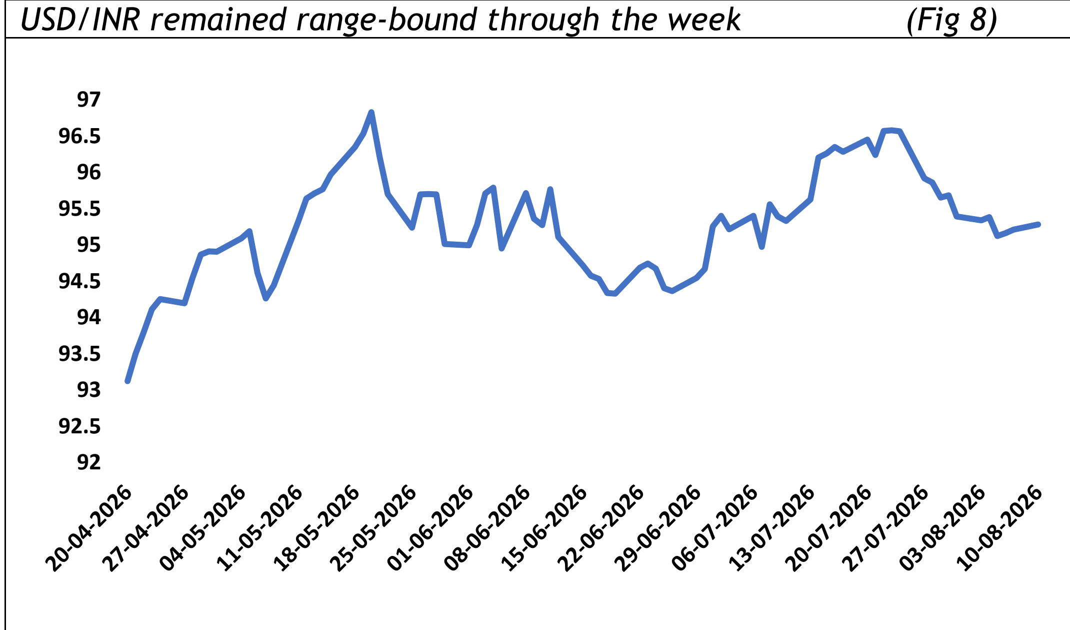
Fresh FCNR(B) deposits, ECBs and OFCBs, supported by the incentives announced in June, have generated sizeable dollar inflows. As of 31 July, banks had mobilised around US$40.8bn under the broader window, including roughly US$36.7bn through FCNR(B) deposits, strengthening the external-sector cushion and adding to expectations of a healthy balance-of-payments surplus this year. Governor Malhotra also reiterated that the RBI remains prepared to act in order to contain excessive exchange-rate volatility and prevent the build-up of self-fulfilling expectations.

Outlook: *We expect USD/INR to stay range-bound between 94.80 and 95.70 over the coming week, with the RBI's reserve cushion (approaching $700bn), the FCNR(B) window and a modestly unwinding forward book all working to cap two-sided volatility. The balance of risks is tilted by two swing factors that could move the pair outside this band in either direction: a hawkish surprise in Wednesday's US CPI print, which would firm the dollar broadly and revive September Fed-hike pricing, and any further escalation – or, conversely, a credible resolution – in the Strait of Hormuz standoff, given oil's outsized and immediate pass-through to India's external accounts. India's own July CPI print is a secondary catalyst that should reinforce, rather than challenge, the RBI's current wait-and-watch stance. On balance, we retain a range-bound bias into month-end."*

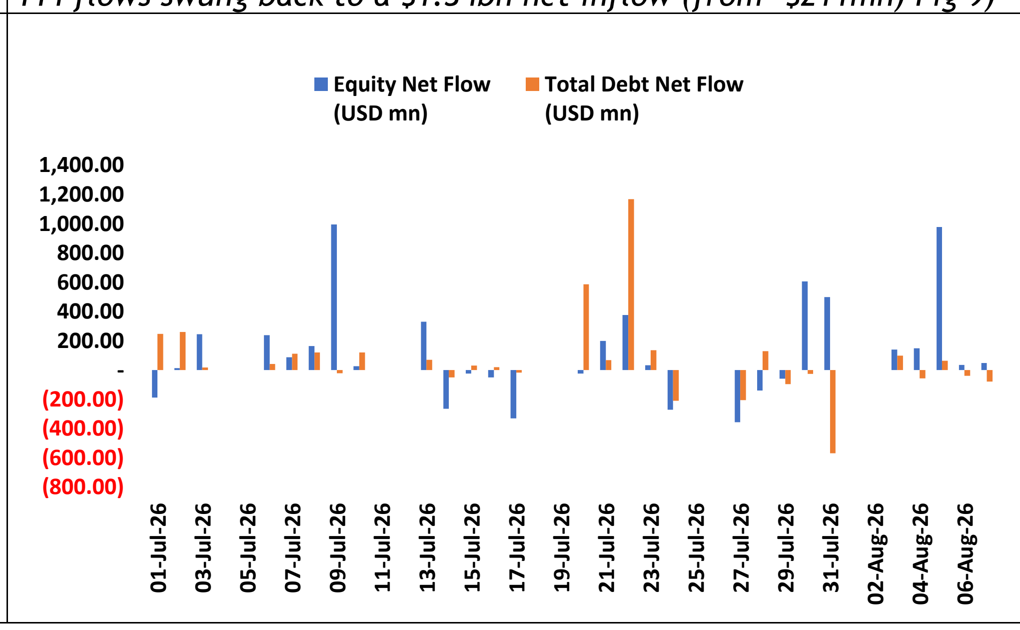
The DXY ended the week below 100, while Japan and the U.S. conducted coordinated yen-buying intervention. *(Fig 7)*



USD/INR remained range-bound through the week *(Fig 8)*



FPI flows swung back to a $1.34bn net inflow (from -$211mn) Fig 9)



Source: LSEG Workspace, & UBI Research

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