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Our key views for 2025		
FX Crosses	View in 2025	Key Risk for FX crosses
EURUSD	↓	Trump less aggressive on trade tariffs towards Eurozone
GBPUSD	→	UK economy deteriorates to put pressure on BoE to cut aggressively
USDJPY	↓	BoJ maintain its Dovish tone
USDINR	↑	FII inflows
USDCNY	↑	PBoC intervenes in its FX markets

Although Trump has not ordered any immediate tariff increases, drastic measures may be expected over the medium term.

FOMC may keep rates on hold until the second half of the year.

The US Dollar has responded positively to the prospect of a second Trump term but there is still a huge amount of uncertainty about how and when the new administration's policies will be rolled out. Uncertainty is inducing volatility in FX and can be seen since mid-2024 and is likely to continue in 2025 as well. Although the US dollar and yields have corrected since Trump resumed office on 20th Jan'25 as his announcements were looked by markets as gradualist rather than the aggression he vowed during his election campaign.

While the anticipation of tax cuts and deregulation of policies are supporting US growth expectations, the implementation of tariffs may support the safe haven demand for the US dollar. At the same time, the Fed is adopting a more cautious approach to the monetary policy outlook and is likely to keep rates higher for longer. The recent announcement by Chinese start-up DeepSeek of a more affordable AI model to rival US tech giants has shaken highly valued US tech stocks and has raised concerns that whether US exceptionalism can continue?

In our view, US Dollar's recent dominant performance relative to its major currency peers may continue in near term. While US exceptionalism is expected to be the primary source, monetary policy divergence is also likely to play a role. Also slowing growth in Asia & Europe relative to the US, adds to the fundamental headwinds for major currencies.

All eyes will be on FOMC meet of 29<sup>th</sup> January although markets have fully priced in that the Fed may hold the rate at current juncture but the comments from J. Powell will be closely watched, especially after recent Trump's comment that "I'll demand that interest rates drop and likewise, they should be dropping all over the world. Interest rates should follow us all over immediately". Also markets awaits the final announcements on trade tariffs implemented by Trump administration.

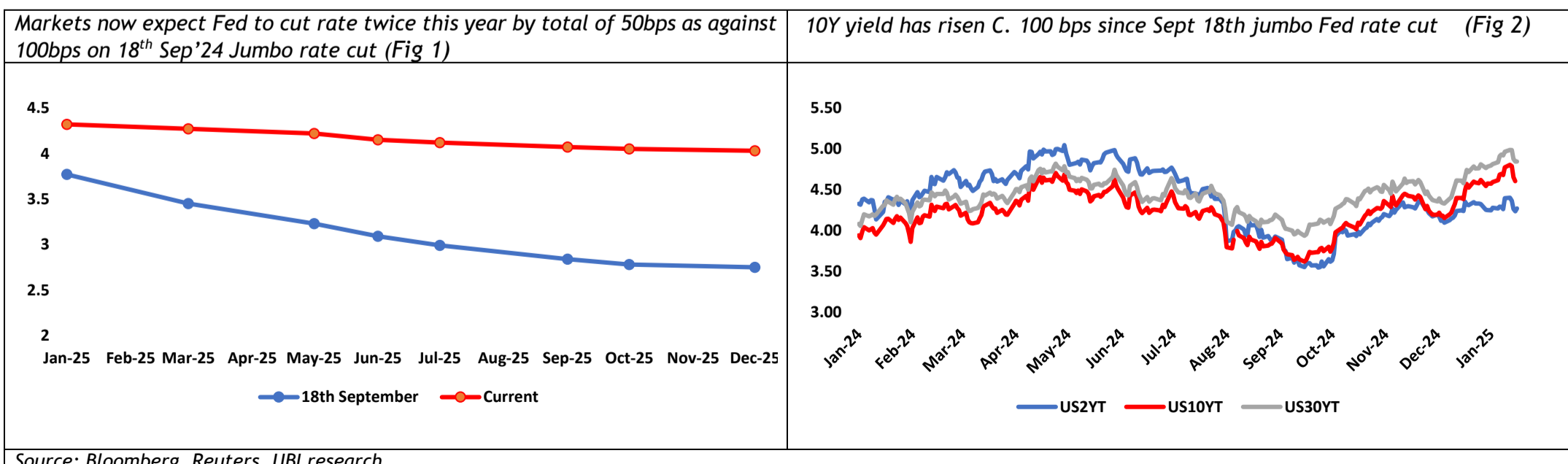
The key themes for our Uni-Fx are outlined below.

**Key Themes:**

- ♣ Trump threatens tariffs by no action yet, markets see it as gradualist approach
- ♣ BoJ hikes its policy rate, timing of next hike remains to be seen
- ♣ Euro bounces back on weak US Dollar; does the rally have further legs?
- ♣ GBP was the best G10 pair after US dollar in 2024, can it repeat its performance
- ♣ Rupee sees respite after hitting all-time lows; Trump's actions on watch

**Trump threatens tariffs by no action yet, markets see it as gradualist approach**

The DXY has corrected c.1% since 20<sup>nd</sup> Jan'25 as markets have viewed Trump's initial announcements as gradualist in nature. Some of his major announcements include imposing 10% tariff on goods from China as compared to 60% stated during his election campaign and 25% tariffs on goods from Mexico and Canada both of which may be implemented as early as 1<sup>st</sup> Feb. Tariffs on goods from Eurozone was also mentioned as they enjoy trade surplus with the US along with 2.5% tariffs on global goods.



*A resilient US economy may keep the US Dollar supported*

*5% yield on US10Y on cards in H1 of 2025*

*America first policy may likely support US exceptionalism*

On commodity oil continues to fall as Trump stated that he would ask Saudi Arabia and other OPEC nations to “bring down the cost of oil”. Gold continues to trade higher due to safe haven demand and global uncertainty. On war he has threatened to impose strong sanction on Russia if Putin do not reach a settlement to end war against Ukraine. While tariffs are likely to disrupt US demand, as market participants could also direct capital toward safe-haven assets as opposed to the riskier emerging markets.

**Headwinds for strong US Dollar**

As stated above the US Dollar dominance may likely to continue in near term as well, less dovish Fed, U.S. economic outperformance, and investors likely seeking safe-haven assets as tariffs are imposed should all push the greenback stronger against G10 and emerging market currencies. Although there are many factors limiting its strength. The market has already priced in significant tariffs under Trump’s term, as early signs suggest a more measured approach is been followed by his administration. Also, robust immigration policy could strain US growth, leading to higher wages and inflation. Tax cuts and increased national debt may raise concerns about fiscal sustainability thus this all factors may lead to weakness in US dollar.

**Is yield on US10Y approaching 5% mark?**

The yields on US 10Y and 30Y continue to rise even after the Fed has cut rates by 100bps since Sept’24. The US10Y has risen by c.100 bps since jumbo rate on 18<sup>th</sup> September but have fallen by 20bps since 13<sup>th</sup> Jan’25 and may be approaching the 5% mark in near term as which was last seen in Oct’23 a scenario seen during 2008 global financial crises. As strong growth of the U.S. economy has undermined investors' optimistic expectations for a Fed rate cut, also Trump may prioritize economic growth over concerns about debt. While historically, rising 10-year U.S. Treasury yields have signalled economic turmoil, such as during the 2008 crisis but this time it might not be the case.

**December data continues to remain strong, labor market improves while inflation remains sticky**

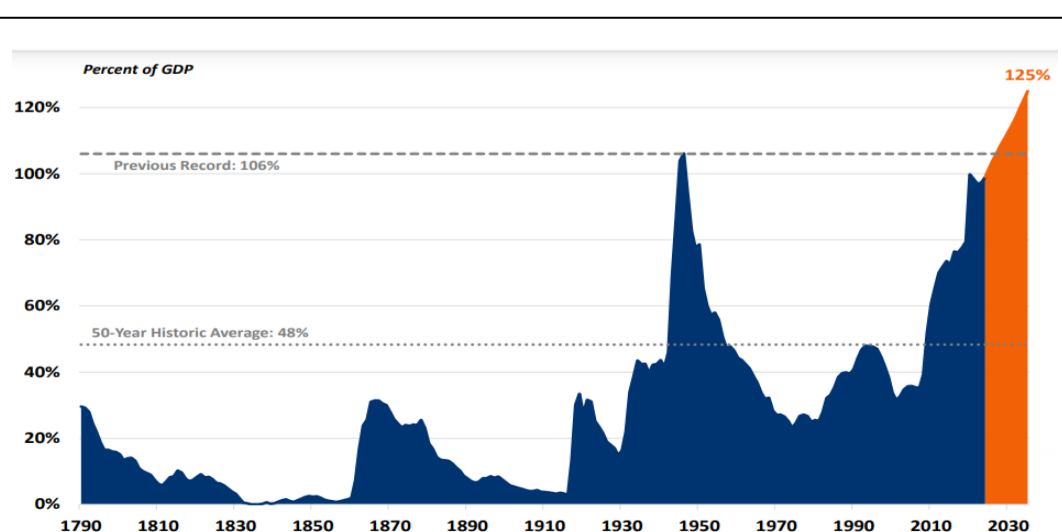
The highlight for December month was US jobs data which closed the year with a strong gain. The US jobs report shows non-farm payrolls rose by 256k in December versus the 165k consensus figure. Revisions to the past two months were -8k. The unemployment rate has fallen to 4.1% from 4.2% - the consensus was for it to hold at 4.2%. Wage growth was 0.3% mom with the YoY rate slowing to 3.9% from 4%.

The Consumer Price Index ended the year at 2.9% YoY, which is a minor improvement from its 3.1% rate in Jan’24 and points to stalled progress on the road back to the Federal Reserve's 2% inflation target. On monthly basis, the headline CPI rose 0.4% in December and core CPI rose by 0.2%.

US industrial production jumped 0.9% MoM in December vs the 0.3% consensus while November's growth rate has been revised up to +0.2% MoM from an initially reported -0.1%. This points towards ongoing improvements while there might finally be signs of a turn in the sector. Markets will be watchful of January NFP data on 7<sup>th</sup> Jan’25 and CPI on 12<sup>th</sup> Jan’25.

*Rising US yields continues to put pressure on debt*

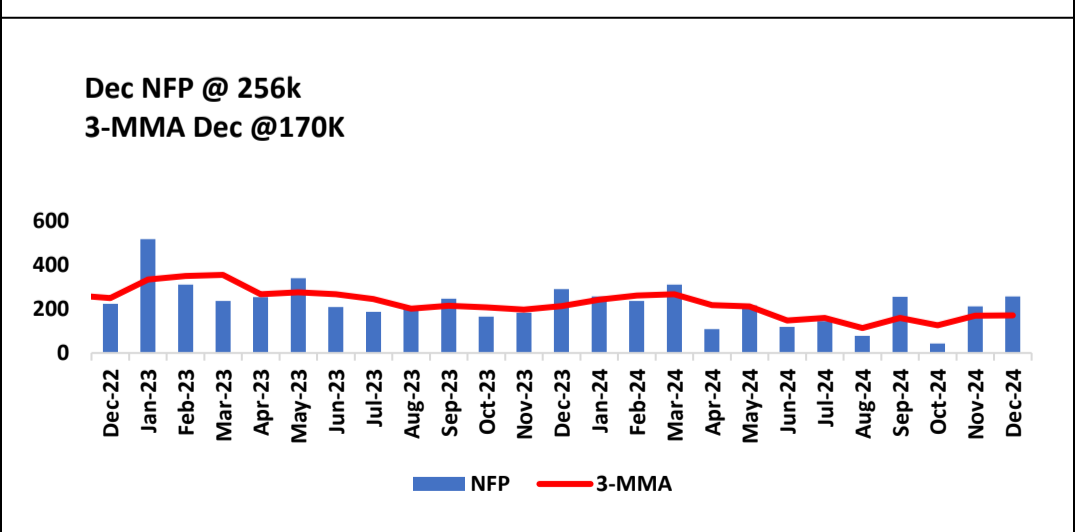
*(Fig 3)*



Source: Bloomberg, Reuters, CRFB.org, UBI research

*December NFP data has pared back rate cut by Fed in 2025*

*(Fig 4)*



Rising yields weigh on debt affordability

Hawkish comments from Ueda hints at higher terminal policy rate

Markets are pricing in another 25bps rate hike by BoJ for this year

**High funding cost remains a key challenge**

When interest rates remain low over time, interest expense on the debt paid by the federal government will remain stable, increases in interest rates and inflation are now resulting in an increase in interest expense. The data from US Treasury shows as of Dec'24 it costs \$308 billion to maintain the debt, which is 17% of the total federal spending in fiscal year 2025.

Recently US Treasury yields have increased sharply, and the rollover of existing debt into higher yielding bonds has nearly doubled the debt service burden which remains cause for concern for US and will keep the global cost of capital elevated.

**BoJ hikes its policy rate, timing of next hike remains to be seen**

The BoJ on expected lines hiked its policy rate by 25bps and raised its target rate to 0.5% highest level since 2008. The market reaction was muted as compared to last hike in July'24 which led to carry trade unwinding, as this time ground work for this rate hike was already laid down by Ueda and co. Governor Ueda's comments made clear that the Bank is not in a hurry to raise rates again. While there was sharp upward revision to inflation outlook. Policymakers now expect inflation at 2.4% (up from 1.9%) in 2025.

On raising interest rates, the BoJ stated that growth and inflation have been developing generally in line with its forecasts. Also, with wages continuing to rise, there has been an increase in moves to reflect higher costs, such as increased personnel expenses and distribution costs, in selling prices.

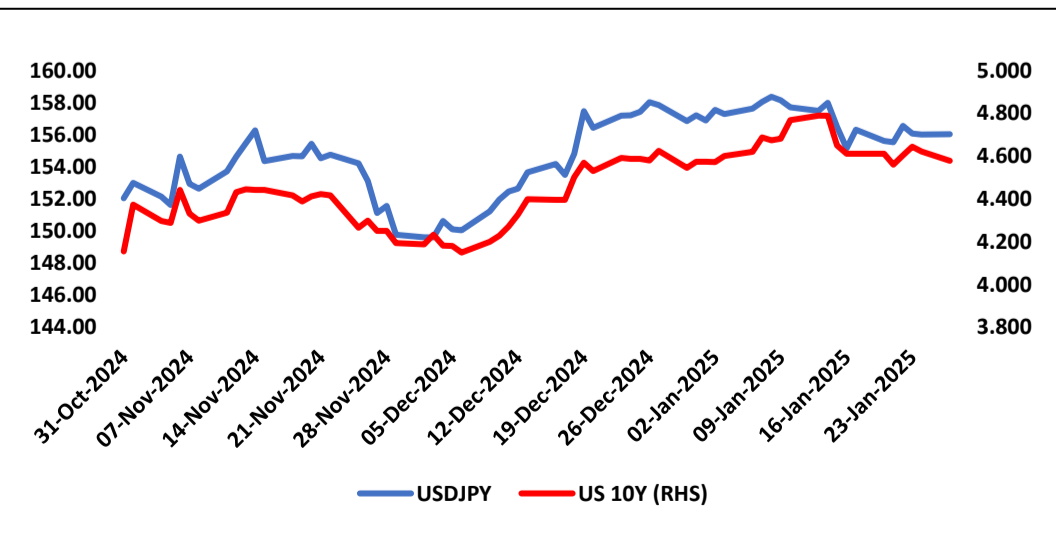
The Bank of Japan also noted relative stability in global financial markets, saying "while attention has been drawn to various uncertainties, global financial and capital markets have been stable on the whole, as overseas economies have followed a moderate growth path."

Ueda also suggested global markets have been relatively calm in the initial days of President Trump's administration. Interestingly, Ueda mentioned that even after rate hike, the current policy rate is still far from its "neutral" level, and that he was not considering some specific rate level as a barrier. He indicated that BoJ analysis suggested the neutral rate could be somewhere between 1.00% and 2.50%.

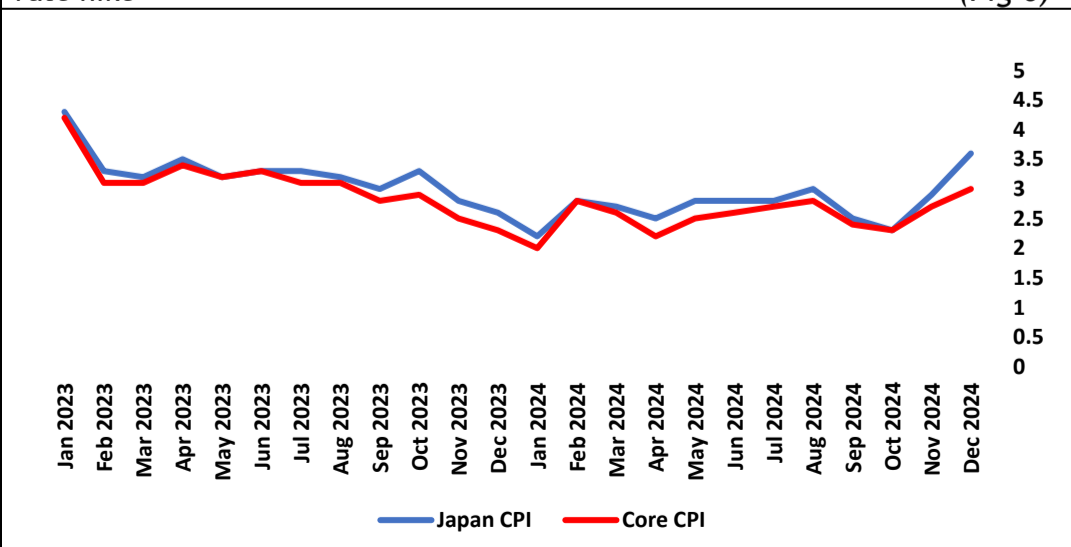
**JAPANESE YEN (¥ - JPY):**

The JPY is moving in range of 153 to 158.88 since last one month. The current OIS market is pricing in just over one rate hike by the end of the year. Market participants are cautious about adjusting rates more due to uncertainty surrounding the early stages of Trump's second term. If Trump triggers higher US rates and pushes the USD/JPY higher, it could increase the chances, for the BoJ to hike rates again. Technically the 155.00 level appears to be solid support for now, and while the Bank of Japan's tone in its policy seemed to support a lower USD/JPY, there isn't any strong enough catalyst as of now to push the pair lower. For USD/JPY to break lower, US short-term yields would need to go lower. Overall, the BoJ's policy outlook is becoming more supportive for the yen. Technically we expect USDJPY pair to trade in 153.50 to 158 range in near term.

Yields on US treasury remains critical for the performance of Yen (Fig 5)



The Dec'24 core CPI has hit 16-month high which continues to support BoJ rate hike (Fig 6)



Source: Bloomberg, Reuters, UBI research

## Euro bounces back on weak US Dollar; does the rally have further legs?

On Trump's inauguration day of 20th January'25, EUR surged 1.4%, highest gain in about 14 months. A lack of serious tariff threats in Trump's inauguration speech was taken as a green light to sell the dollar. Although he stated that European union should buy more oil and gas from the US to avoid tariffs which was seen as a gradual approach followed by Trump.

The euro in near term could strengthen in FX if Trump refrains from mentioning Europe in his tariff comments for a few more days. However, this support may be temporary, as protectionist measures can quickly change, as seen with Canada and Mexico.

In December, Eurozone CPI inflation came in as expected, with the headline rate rising to 2.4% YoY and core inflation remaining steady at 2.7%, same as November. Services inflation, important to ECB policymakers, increased to 4.0%. While these readings show some acceleration in price growth, the overall outlook supports the expectation of gradual ECB rate cuts in 2025. This is due to a weaker growth environment in the region and inflation continuing its return to the 2% target.

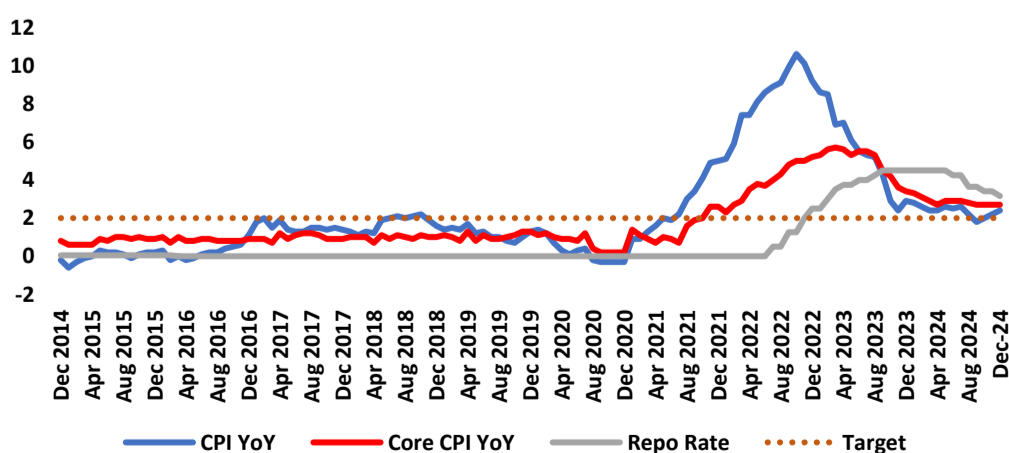
The European Central Bank (ECB) policy on January 30 where markets expect the ECB to cut rates by 25bps the probability of which currently stands at 95% and a total of 100bps by end of 2025. The tone of Lagarde will be closely watched as markets expects Lagarde to maintain a dovish tone, as the ECB views Trump's tariffs as greater threat to eurozone's growth and inflation will closely watch for any announcement regarding the same.

### EURO (€ - EUR) view:

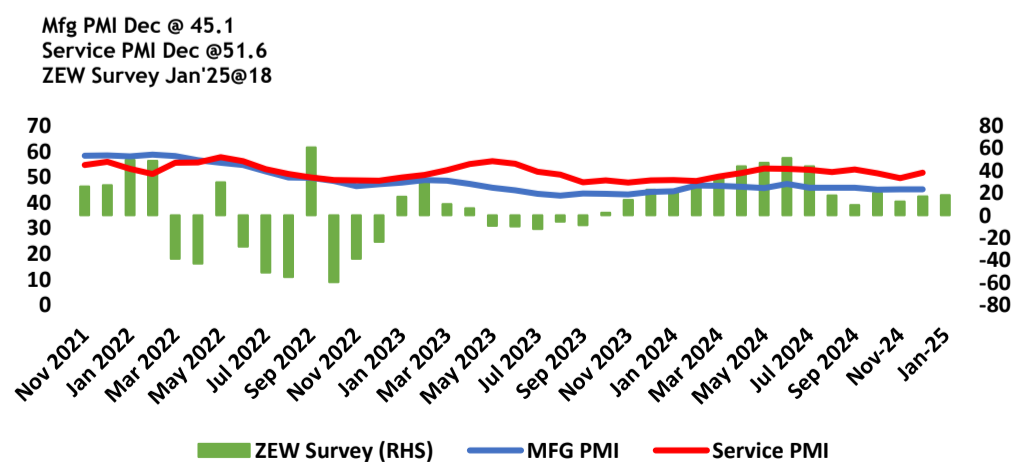
As stated in our last Dec'24 Uni-FX the next resistance for EURUSD pair lies at 1.0610 level the pair made a high of 1.0531 in Dec'24 and started its downward journey. Going forward, the Euro's overall appeal is limited by weak macroeconomic fundamentals, meaning any rebound is unlikely to push EUR/USD above 1.0500 levels. Also, the monetary policy divergence is likely to persist between Eurozone and US where the EU is likely to cut by 100bps while Fed is likely to cut by just 50bps this year adds another headwind to EURUSD pair. Technically the next support for EURUSD pair lies at 1.0350 levels a breach of which expose the pair to test the 1.0250 level. Resistance comes at 1.0500 followed by 1.0610 levels.

*Paring back of tariff fear by Trump administration helps support the Euro*

ECB likely to cut rates in Jan'25, while remain cautious about Trump's policy and its effect on inflation (Fig 7)



Eurozone Manufacturing, Service PMI along with Zew data remains flat (Fig 8)



Source: Bloomberg, Reuters, UBI research

Deteriorating job market conditions and rising price pressure are expected to add more trouble for BoE

Rupee depreciating trend continues for 10<sup>th</sup> straight week

REER cooled down from all-time highs

### GBP was the best G10 pair after US dollar in 2024, can it repeat its performance

The British pound (GBP) made a high of 1.2360 following Trump's inauguration on 20th Jan'25 but since then it is consolidating in a narrow range and awaits any fresh announce on trade tariffs from Donald Trump. Although he confirmed that the proposal for universal tariff hikes is still under consideration, but "We are not ready for that yet." UK is less likely to be affected Trumps' trade tariff as UK's exports to US are largely in services sector and Trump has yet not spoken anything about tariffs on services.

Rising global yields over recent months have inevitably shone the spotlight back on the UK government's decision to dramatically ramp up spending in its Autumn Budget. It saw big tax rises but even bigger increases in day-to-day spending (c.1.5% of GDP) the has led to the 10Y yields to highest level of 4.89 levels last seen in 2008.

The data this month revealed an unexpected slowdown in inflation and weaker than anticipated economic growth. Wage growth accelerated to a six-month high in the three months leading up to November, in line with expectations. However, the unemployment rate unexpectedly rose to 4.4%, accompanied by the sharpest drop in payroll numbers since November 2020, indicating potential softening in the labor market.

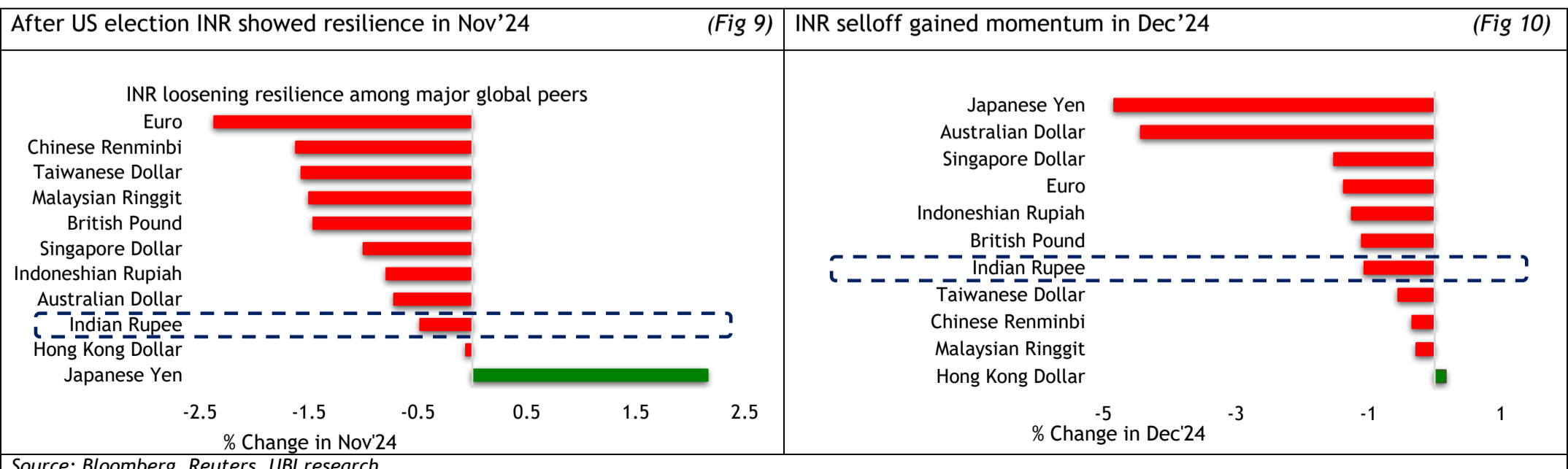
Against this backdrop, the Bank of England may reduce the key interest rate by 25 basis points to 4.5% on 6th Feb'25 BoE policy meet and a total to 75bps by end of 2025.

### Rupee sees respite after hitting all-time lows; Trump's actions on watch

The rupee slipped around 1.11% this month dragged by the strength of Dollar and logged a 10th consecutive weekly losses to hit all-time lows of 86.71/\$ (14<sup>th</sup> Jan'25). Dollar has maintained an upward bias on US exceptionalism and uncertainty over Trump's policies. This in turn has strengthened Dollar and all the major global currencies took a hit. However, markets have taken relief after Trump joined Office as there were no major tariff announcements since then.

In recent scenario, INR was not only pressurized by external global factors but internal issues were adding fuel to it. In Nov'24, when most of the major global-market currencies depreciated against Dollar, Rupee has relatively been less affected among the Asian peers and depreciated marginally until US elections outcome. But, in Dec'24 rupee sell-off gained momentum which was mostly due to the change in regime in the central bank. The depreciation trend continues in jan'25 which shows INR took a major hit and was the worst performing currencies among Asian peers but largely better than compared to the global major FX peers. The rupee came under further pressure after media reported [RBI Governor Sanjay Malhotra indicated an openness to a more flexible rupee.](#)

REER has seen an overvaluation bias persists (107.20 in Dec'24 down from 108.13 in Nov'24 versus 5-yr. avg. of 103.99 levels) reflecting pending depreciation pressure in the currency pair. Pace of overvaluation has reduced in Dec vs Nov as Rupee move was relatively better aligned versus global peers. However, in Jan'25, the pace of fall in over-valuation would have increased as Rupee was one of the worst performing currencies amid global FX peers. (Ref fig 9,10 &11)



Sharp loss in Q3 & Q4 will dampen BoP dynamics

FPIs turned negative in Jan'25 again

FX reserves at 10-month low

REER overvaluation to contract after major depreciation already hit

The local currency sentiment got marginal support after the dismal trade data shocker for Nov'24 was revised later to \$31.83bln, where Gold was adjusted to \$9.84bln vis-à-vis \$14.86bln. However, the latest trade numbers for Dec'24 show sharp narrowing to \$21.94bln. Despite this, our analysis shows that BoP dynamics stayed under pressure in December at \$9.89. FYTD25 Balance of Payment (BoP) is tracking negative c.\$24.32bln (Q1: \$6.37bln, Q2: \$27.65bln, Q3: -\$42.27bln & Q4 till date: -\$16.07bln) with sharp loss in BoP seen in Q3:FY25. Historically, there is a close correlation between FX reserves (adjusted for valuation effects) and BoP. Additionally, FX reserves declined for the 7<sup>th</sup> consecutive week to reach a 10-month low to \$623.98bln for the week ended 17<sup>th</sup> Jan'25, though it is down by \$80.90bln from all-time highs of \$704.86 (\$58.34bln fall was adjusted after valuation effects). This shows central bank has persisted with its efforts to curb FX volatility. (Refer our report: [2025: A year to stay "nimble and humble" amid global volatility](#))

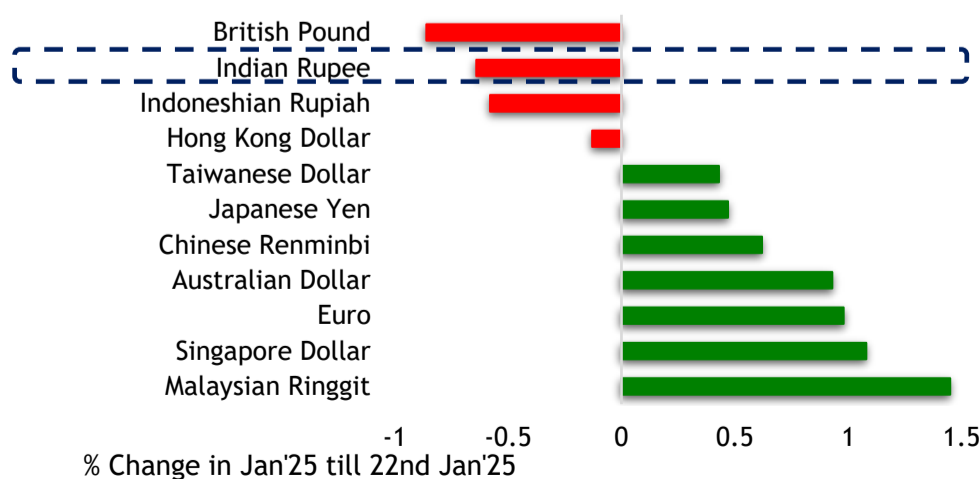
FPIs net withdrew \$11.12bln (highest in a decade) in Oct'24, while outflows moderated to \$2.56bln in Nov'24. In equity segment flows turned positive in Dec'24 to \$2.37bln but turned negative again in Jan'25 to \$7.44bln. Also, the debt segment has turned negative; outflows to the tune of \$8.2bln vis-à-vis inflows of \$1.27bln from the previous month. Moreover, the FAR related flows have turned flat as well to \$275mln in Jan'25 vis-à-vis inflow of \$1136mln in Dec'24. Going forward, Dollar inflows are also expected from Jan'24 month-end on inclusion of India FAR bonds in the Bloomberg Emerging Market (EM) Local Currency Government Index and related indices, starting 31st Jan'25.

Another key factor that gave a psychological boost to Rupee move was the fall in global oil prices (touched a high of \$81.68/bbl. on 13th Jan'25; levels last seen in Aug'24; current levels: \$77.11/bbl) after Trump in his recent speech in the World Economic Forum in Davos stated that he will ask OPEC nations to "bring down the cost of oil" which will be impacting India's oil trade deficit to a great extent - Sensitivity of C/A deficit to oil prices stays high with every \$10/b move in oil price affecting annual C/A balance by close to \$15bln. Already, US President has declared National Energy Emergency on his first day in his office to accelerate permitting projects of oil, gas and power. He stated; "We will bring prices down, fill our strategic reserves up again right to the top, and export American energy all over the world". His comments have cooled Brent crude oil prices below \$80/bbl.

As per media sources, the premium on the dollar/rupee forward contracts fell across most tenures as major PSBs are likely to have sold forward dollars for maturity in near and far maturities. These Buy-Sell swaps are used to replenish liquidity, along with buyback of securities and Daily VRR as the net liquidity conditions have deteriorated sharply in recent weeks.

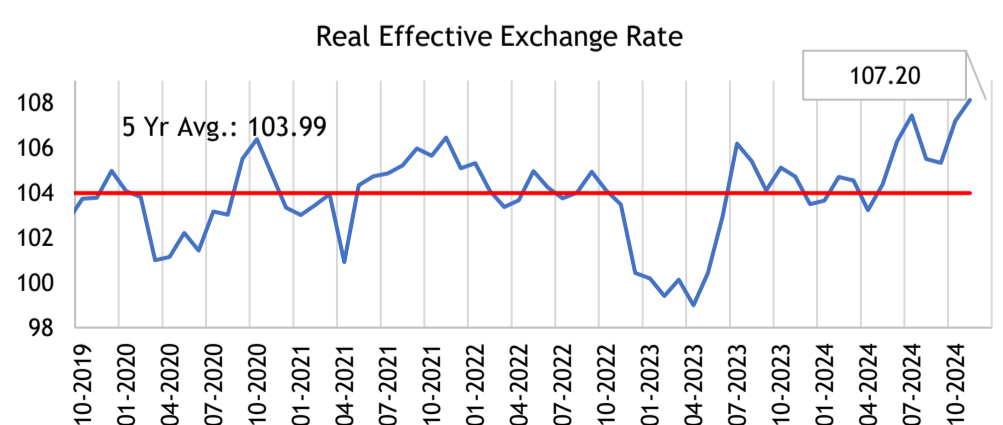
Based on the current global scenario, volatility to reign on uncertainties after Trump joined White House on 20th Jan'25 and we expect cooling down of DXY to continue momentarily. The Dollar Rupee pair has respected our previous technical levels and now technically we feel INR should take support of 86.20 followed by 85.90 levels and will find resistance around 86.80, breach of which will test 87.20 levels. However, going forward, we closely watch for a scenario of possible overshoot in DXY, probably a breach of current technical level.

Rupee seen sharp depreciation pressure after US NFP data in Jan'25 (Fig 11)

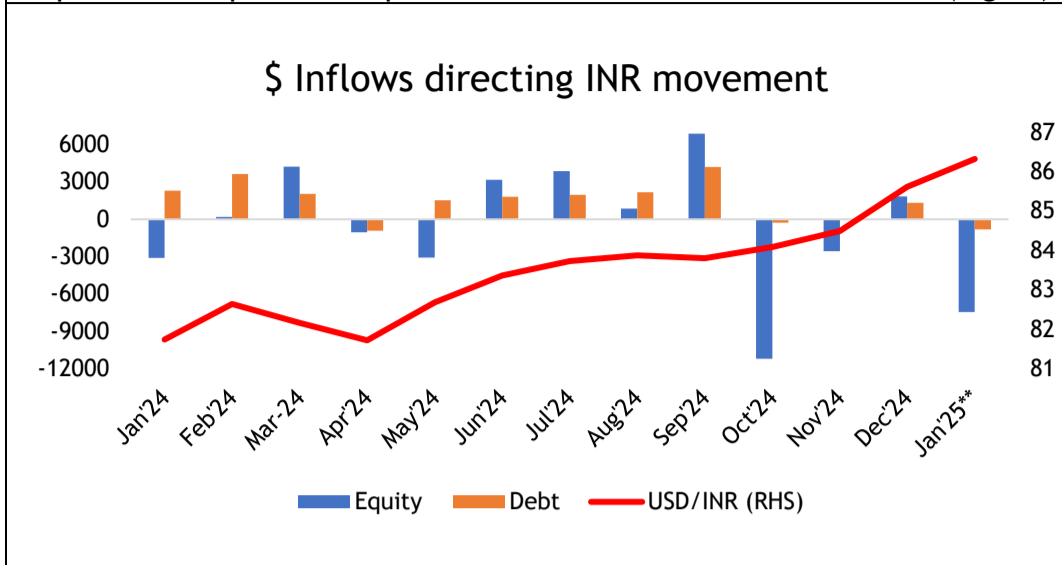


Source: Bloomberg, Reuters, UBI research

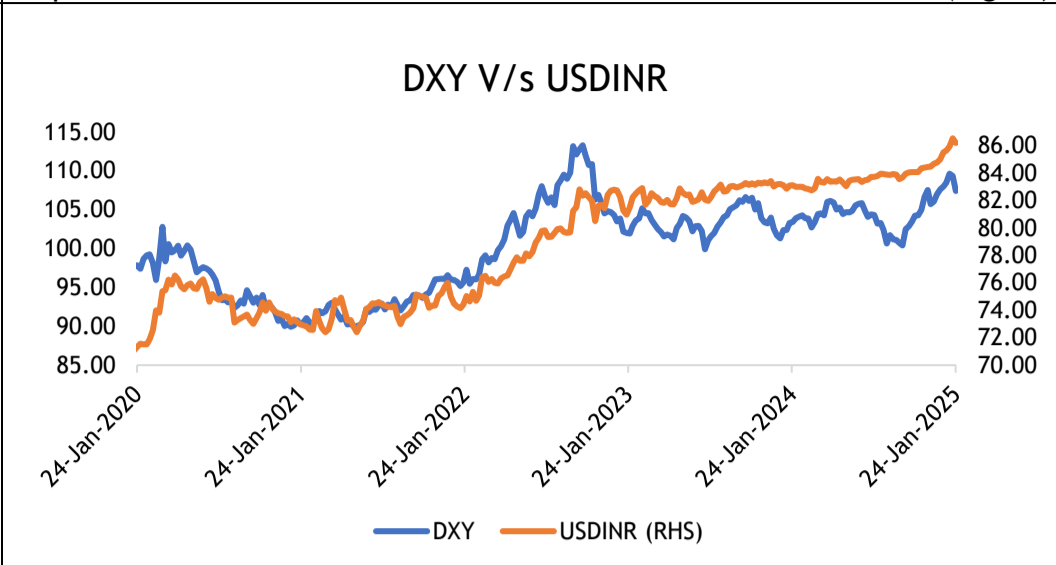
REER has likely corrected towards the 5 yr avg. in Jan'25 (Fig 12)



Rupee seen depreciation pressure amid continuous FPI outflows (Fig 13)

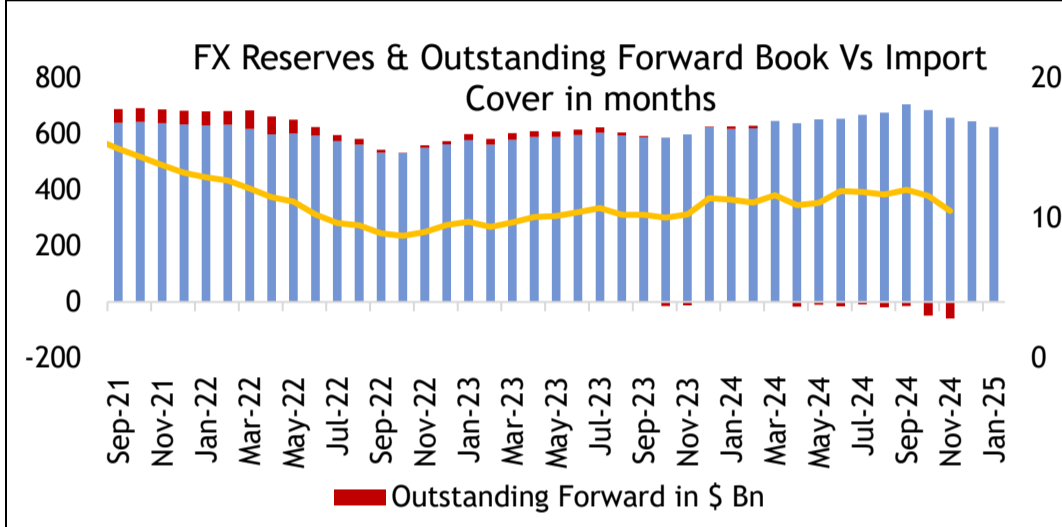


Rupee movement has shown correlation with DXY movement (Fig 14)

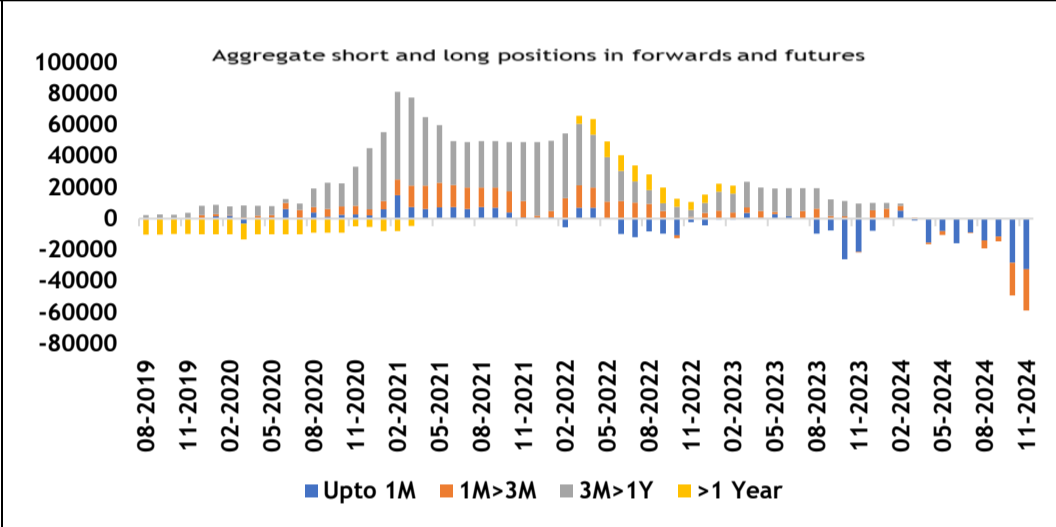


Source: Bloomberg, Reuters, UBI Research

Depleting FX Reserves and reducing import cover (Fig 16)



RBI forward position at record short levels (Fig 16)



Source: Bloomberg, Reuters, UBI Research

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