UPFRONT

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▶ RUPEE

A TEST OF RESILIENCE

The rupee's slide towards 100 to the dollar is raising concerns over the economy, even as the RBI steps up efforts to arrest its fall. But intervention comes at a cost

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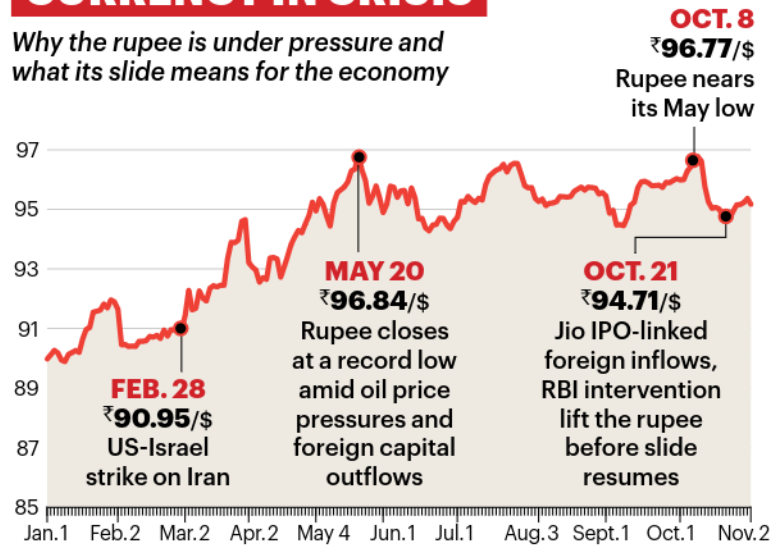


ON NOVEMBER 2, THE RUPEE CLOSED AT 94.86 TO THE DOLLAR, within the band it has occupied for five months. Crude prices had eased on hopes that a draft proposal from Qatar could pause the US-Iran war. Foreign investors offered a rare reprieve, buying a net Rs 3,600 crore of Indian shares on October 30 after nearly two years of selling. However, the calm has come at a cost. The Reserve Bank of India's (RBI) forward book—the outstanding net amount of dollars it has committed to sell at future dates—reached a record $239.2 billion at September-end. Reserves fell for a seventh consecutive week to $719.75 billion on October 23, around $66 billion below their September 4 peak.

RBI governor Sanjay Malhotra says the central bank does not target any specific exchange rate level and steps in only to smooth excessive swings. Since May, however, it has sold dollars, mobilised overseas deposits, raised interest rates and tightened currency market rules to prevent further slide.

CURRENCY IN CRISIS

Why the rupee is under pressure and what its slide means for the economy



↘ Foreign outflows: **Foreign portfolio investors have been pulling money out of Indian equities since late 2024, weakening dollar inflows and putting pressure on the rupee**

↘ Oil shock: **The US attack on Iran pushed crude prices higher. With 85% of its crude imported, India faces a larger import bill and greater inflationary pressure**

↘ US rate pressure **Higher Fed rates are drawing capital towards American assets, weakening emerging-market currencies and raising India's external debt-servicing costs**

For Indian businesses, the psychological threshold of Rs 100 to the dollar has already been breached. On May 20, when the spot rupee touched a record intraday low of nearly 97, the one-year forward rate crossed 100 for the first time. A forward contract lets businesses lock in a dollar exchange rate for future payments, protecting them against rupee depreciation. Forward rates exceed spot rates partly because Indian interest rates are higher than US rates, but also because of demand for dollar hedging and market liquidity. The one-year forward premium rose from an average of 2.9 per cent between January and August to 4.57 per cent on October 30. Consequently, although the spot rupee recovered to around Rs 95, the one-year forward rate stood at Rs 99.2 on November 2.

THE SLIDE AND ITS RISKS

Pressure pre-dated the war. Foreign portfolio investors put $18.4 billion into Indian stocks and bonds in 2024 but turned sellers that October, citing US tariffs, high valuations and increases in capital gains tax and securities transaction tax (STT). Within two years, the rupee weakened from 83 to 91.

The US-Israel strikes on Iran on February 28 turned the slide into a crisis. Brent crossed $100 a barrel, while foreign investors withdrew a record $12.7 billion from Indian equities in March. Net outflows reached $21.4 billion between January and September. For a country that imports 85 per cent of its crude, the twin pressures of higher oil prices and capital flight threaten to widen the current account deficit—the gap between the foreign exchange India earns from exports of goods and services, and what it spends on imports and other payments to the rest of the world.

The US monetary policy has added to the strain. The Federal Reserve raised interest rates on September 16, its first increase in over three years. When it held rates on October 28, two members voted for another increase. Higher US rates draw capital towards dollar assets.

Nor has the weaker rupee improved trade. Between April and August, imports grew faster than exports, widening the trade deficit to $147.1 billion. Further depreciation would make buying crude oil, servicing India's external debt of over $700 billion, and importing components for sectors such as electronics, pharmaceuticals, automobiles and renewable energy more expensive. At $110 a barrel, crude would cost around Rs 11,000 if the rupee touches 100 to the dollar—nearly double its cost 18 months ago, and a significant psychological threshold for the rupee. For a family sending a child to the US for higher studies, an annual university bill of $50,000 would rise from Rs 41.5 lakh just two years ago to Rs 50 lakh.

Inflation is another concern. Retail inflation stood at 4.8 per cent in August; further rupee depreciation could push it towards the RBI's 6 per cent upper tolerance limit, forcing rate hikes that could slow growth without easing oil prices. In 2013, an 11 per cent fall in the rupee pushed retail inflation into double digits.

A SERIES OF INTERVENTIONS

India's defence of the rupee has echoes of 1991, when the Gulf war sent oil prices soaring and non-resident Indians (NRIs) withdrew deposits. By mid-year, reserves covered barely two weeks of imports. India raised around $600 million by selling or pledging 67 tonnes of gold abroad; the rupee was then devalued by about a fifth. During the 2008-09 global financial crisis, the RBI sold $34.9 billion. In 2013, it mobilised around $34 billion through currency swap windows during the 'taper tantrum', when signals that the Fed would scale back its bond-buying programme triggered capital outflows from emerging markets.

The current defence dwarfs these interventions. The RBI sold a record $53 billion in FY26 and another $24.8 billion this March-May. A special deposit scheme launched for NRIs in June brought in $133 billion by August-end. In October, the central bank raised the repo rate by 25 basis points to 5.5 per cent, seeking to support the rupee by making domestic assets more attractive

to investors. It also revived a facility to supply dollars directly to state-run oil companies for their import payments and introduced, for the first time, a 20 per cent cash reserve requirement on certain large currency derivative contracts, making such transactions more expensive for banks. No defence since 1991 has involved comparable resources. India is choosing to spend its reserves.

THE COST OF DEFENCE

But headline numbers do not tell the whole story. Some of the decline in reserves reflects lower gold prices, but a larger concern is the RBI's future obligations: forward contracts require it to deliver dollars later, while NRI deposits must be repaid between 2029 and 2031. A report by New Delhi-based LEAP Insights Foundation, *Defending the Rupee*, accounts for these commitments to estimate the reserves effectively available to the RBI—$551.7 billion in August, down from $650.8 billion in February, when the war began.

The pressure is evident in both the cost of currency hedging and government borrowing. With the one-year forward premium at its highest in nearly four years, companies may cut back on hedging because protection has become too expensive, leaving them more exposed if the rupee weakens further. Government bonds, meanwhile, fell for 10 consecutive weeks until late October—their longest losing streak in 30 years—pushing the 10-year yield to 7.47 per cent.

For the finance ministry, the damage is primarily to revenue. Petroleum taxes account for around 12 per cent of the Centre's and states' combined gross tax revenue, says Pinaki Chakraborty, former director of the National Institute of Public Finance and Policy. Every fuel excise cut, therefore, eats into an important source of revenue. A Rs 10 reduction per litre alone is estimated to cost Rs 1.7 lakh crore annually, against a fiscal deficit target of 4.3 per cent of GDP. This is unfamiliar territory for the Narendra Modi government. When it took office in May 2014, Brent crude was around $110 a barrel; two years later, it averaged about $47. The government used the windfall to raise excise duty nine times, more than doubling collections. Now, the reversal in oil prices is a drain on the exchequer.

HOLDING THE RUPEE

↘ Spending reserves: RBI sold a record $53 bn in 2025-26 and continued selling after the US-Iran war began, offloading $24.8 bn in March-May

↘ Raising deposits: Special deposit schemes for NRIs brought in $133 bn. But these deposits must be repaid in dollars between 2029 and 2031

↘ Future commitments: RBI's outstanding commitments to sell dollars at future dates hit a record $239.2 bn in September, up from $200 bn in August

↘ October interventions: RBI raised the repo rate, revived direct dollar supplies to oil PSUs to meet their import needs; introduced a 20% cash reserve requirement on certain large currency derivative contracts

THE AGENDA AHEAD

Economists broadly agree on what went wrong. But they differ on what the RBI should do next. One camp wants the defence to continue. Chakraborty believes inflation should remain the priority and favours an orderly movement in the exchange rate. Charan Singh, a former RBI official who heads the public policy-oriented EGROW Foundation, points out that reserves still cover around 10 months of imports, compared with seven in 2013. He believes the RBI can plan for repayments, as it did in 2016.

Others want the RBI to step back. Arvind Panagariya, chairman of the 16th Finance Commission, argued in May that "100 is just a number, like 99 and 101", warning that continued attempts to defend the rupee could bleed reserves. The International Monetary Fund offered similar advice on October 21. Ahmed El Safty, a former economist at the Central Bank of Egypt, points to Cairo's limited intervention during its currency crisis in early 2026. When a shock persists, he told INDIA TODAY, defending the currency "only invites the market to test you".

A third view is that the exchange rate is a symptom, not the problem. Gopal Krishna Agarwal, the BJP's national spokesperson on economic affairs, says the RBI's mandate doesn't prescribe "any level for the rupee". The balance of payments, he argues, has to be fixed through trade and more competitive manufacturing. Agarwal wants STT and capital gains tax recalibrated, alongside reforms in land and corporate debt markets. Union finance minister Nirmala Sitharaman has said she will consider the tax arguments before the next Union budget. Foreign investors have withdrawn more than Rs 3 lakh crore from Indian equities this year; lower taxes may not offset higher US rates, but could remove an investor grievance.

The dilemma is whether foreign capital must return to stabilise the rupee, or whether depreciation must first make Indian assets cheaper. Much will depend on how the conflict in West Asia unfolds. Iran has identified Gulf energy facilities as potential targets, putting at risk supplies from Iraq, Saudi Arabia, the UAE and Kuwait. If the conflict disrupts supplies, the RBI's dollar window could leave it financing state refiners' purchases at whatever prices the market demands.

Having defended the rupee so visibly, the RBI may find it harder to let it cross the 100 mark without triggering fresh anxiety. In 1991, India had no choice once reserves ran out. Today, intervention is a choice, but each round creates commitments and reduces room for the next shock. The Budget 2027-28, due on February 1 next year, will test the government's response. The task is to steady the currency and make it less dependent on central bank support. ■