India Market Pulse: 31st December 2025

Wishing you a very Happy New Year.

As we enter the year ahead, concerns around **currency weakness - particularly the Indian Rupee** - have once again moved to the forefront of investor conversations. This note aims to address those concerns directly by placing USD/INR in its **proper historical, cyclical, and equity-market context**, and by outlining what this means for Indian assets going forward.

USD/INR Over 25 Years: Depreciation Is Structural, Instability Is Not

Over the past quarter century, USD/INR has moved from approximately **₹47 in 2000 to ~₹90 in 2025**, implying a **~2.5-3% annual depreciation**. This outcome is neither surprising nor destabilising- it largely reflects India's inflation differential, productivity convergence, and a well-managed floating exchange rate regime. Importantly, INR depreciation has **not been linear**. The bulk of the move occurred during **short, global risk-off episodes** - not during periods of domestic macro stress. Episodes such as **2008-09, 2011-13, 2020, and 2022** account for a disproportionate share of the long-term adjustment. Outside these windows, INR behaviour has been **remarkably stable**. **The key message:** A depreciating currency over decades is normal for a fast-growing economy; **currency instability is not** and India has largely avoided the latter.

The Missing Link in the INR Narrative: Equity Cycles and Capital Flows

While inflation differentials explain the long-term trend, **equity capital flows explain short- and medium-term INR movements**. Historically, a clear pattern emerges:

- **Large FPI outflows** coincide with INR overshooting on the downside
- These phases are **almost always followed by sustained equity inflows**
- The result is **INR stabilisation or gradual appreciation**, even without explicit macro tailwinds

This creates a **mean-reverting loop between equities and FX**, which is often overlooked during periods of heightened currency anxiety.

What History Tells Us?

Bull Equity Phases: INR Stability or Appreciation

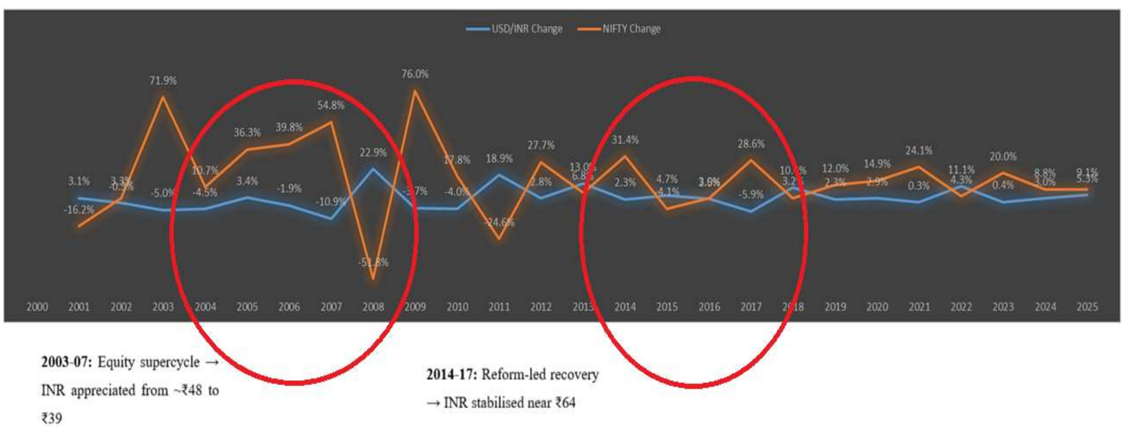
- **2003-07:** Equity supercycle → INR appreciated from ~₹48 to ₹39
- **2014-17:** Reform-led recovery → INR stabilised near ₹64

Risk-Off Phases: INR Overshoots

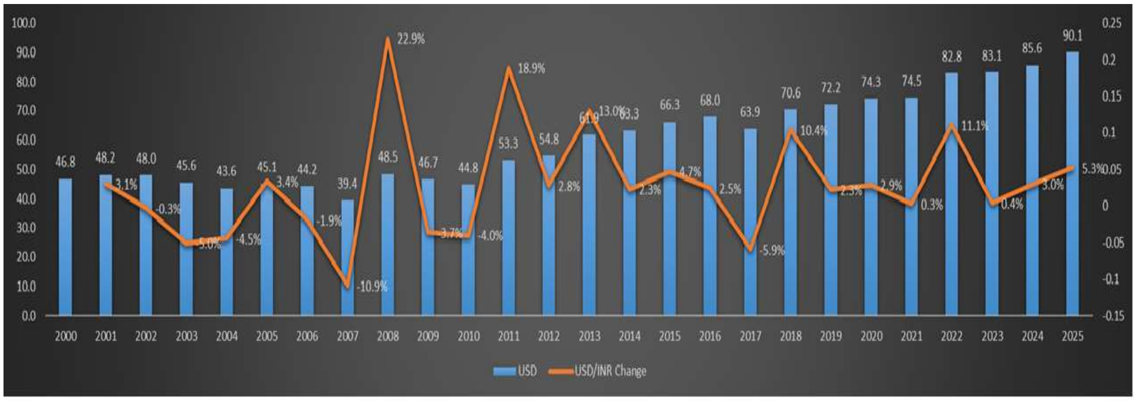
- **2008-09, 2011-13, 2022-23:** Sharp FPI outflows led to visible but contained INR weakness

A critical insight from these episodes is that **currency weakness typically precedes equity recoveries**, not the other way around.

<u>Outflows are fast and emotional; inflows are slower, earnings-led, and persistent</u>.



INR Cycles: From One-Way Weakness to Mean Reversion



A key insight from the long-term USD–INR data is the *cyclical* nature of currency moves. Historically, episodes of sharp INR depreciation have been followed by phases of consolidation or gradual appreciation. This pattern is clearly visible post the stress years of **2007, 2009-10 and 2017**, where risk-off shocks gave way to macro normalization and currency stability.

What stands out in the current cycle is the **break from this historical rhythm**. Since **2018**, the INR has depreciated almost continuously, without a single meaningful year of consolidation or appreciation an outcome driven more by global dollar strength and repeated external shocks than by domestic macro fragility.

This prolonged, one-directional move has now **front-loaded much of the adjustment**. With India's macro fundamentals stronger than in prior cycles credible monetary policy, contained external imbalances, improving earnings visibility, and resilient capital formation the setup increasingly resembles past inflection points rather than the start of a new stress phase.

For investors, this matters. Periods where INR depreciation exhausts itself have historically coincided with improving risk appetite, stronger equity performance, and a more supportive environment for foreign capital. The absence of INR consolidation over the past several years arguably sets the stage for **currency stabilization**, rather than further disorderly weakness - providing an underappreciated tailwind to Indian assets as the earnings cycle turns.

What the Current Setup Is Signalling

The **2024-25 period marked one of the largest FPI outflow phases in India's market history** driven by global monetary tightening and EM de-rating. Much of this adjustment is now reflected in:

- Valuations
- Currency levels
- Risk premia

Notably, despite briefly crossing **₹90**, USD/INR has **struggled to sustain levels above it**. This behaviour is more consistent with **dollar-cycle exhaustion** than with the onset of a new phase of INR stress. In past cycles, such stabilisation has tended to coincide with **late-stage outflows and early-stage equity flow reversals**.

What This Means for Investors Concerned About INR Risk

1. INR downside risk appears increasingly capped- Post major outflow phases, history suggests **limited scope for sustained further depreciation-**unless accompanied by a fresh global shock**.**

2. Strong equity returns do not require INR appreciation- India has repeatedly delivered strong USD equity returns during periods of stable, "boring" INR**, rather than during sharp appreciation phases.**

3. The best equity regimes coincide with INR stability - The most durable bull markets have occurred when:

- Earnings visibility improved
- Capital flows normalised
- INR volatility compressed

This is precisely the regime India appears to be transitioning toward.

Key Takeaway: Reframing the INR Narrative

The INR should be viewed **less as a source of fear and more as a confirmation signal** of **where we are in the equity cycle**.

- Sharp INR weakness often signals **late-stage FPI outflows**
- INR stabilisation confirms **capital flow turning points**
- INR appreciation typically **follows**, rather than leads, equity rallies

The loudest currency fears often emerge closest to the best forward equity opportunities.

Closing Thought

As the new year begins, the alignment of:

- improving earnings visibility,
- stabilising global liquidity, and
- a maturing domestic capital base

suggests that Indian equities are entering a phase where **returns are likely to be driven by fundamentals rather than fear** - with the currency acting as a *stabiliser*, not a headwind. We believe this context is essential when assessing INR-related risks and positioning portfolios for the cycle ahead.