SBI RESEARCH

ECOWRAP

LOOKING BEYOND FCNR(B): FOCUS ON RBI EXCHANGE RATE MANAGEMENT & GLOBAL UPHEAVAL MUST TAKE CENTRESTAGE: FED BUYING YEN DURING ASIAN CRISIS AS WELL AS NOW & US 30-YEAR TREASURY YIELDS AT RECORD HIGHS ARE SIGNALS HARD TO IGNORE

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The RBI has decided to close the FCNR(B) scheme one month ahead of the scheduled closure on 30th Sep'26. The decision to close it early comes as a surprise to market participants even as in the last media interaction the RBI Governor had clearly indicated that there was no intention to close the scheme early in response to a pointed question in the media interaction. While there may be valid reasons to justify an early closure, the most likely reason could be that the target for FCNR(B) mobilization has already been achieved with inflows at $57 bn. And another $25-30 bn could easily flow in the remaining days of August **taking the total collections to around $85 bn**. The balance of payment will be in surplus of around $50 bn with CAD at 1% of GDP.

We don't believe that the cost of swap could have been a constraining factor. Our estimates show that **the cumulative cost would amount to around 15% of the corpus, or $10.5 billion**. While this appears sizeable in absolute terms, it needs to be viewed against the scale of India's foreign-exchange reserves rather than the FCNR(B) corpus alone. With current reserves at around $700 billion and incremental reserve accumulation assumed at roughly $20 billion annually, **the five-year cumulative hedging cost of $10.5 billion would amount to only 1.45% of the current reserve stock and around 1.27% of the projected reserve stock**. **This is minimal.**

The other crucial question is what is going to happen post 31st Aug'26, specifically to Rupee movements?

We believe that the impact on rupee post the announcement of FCNR(B) measures has been surprisingly minimal. In 2013, Rupee was at 65.70 on 31 Aug'2013 and appreciated to Rs 62.45 on 29 Nov 2013 (4.9% appreciation). Post the closure of FCNR(B) scheme, rupee settled at 59.89 (**8.8% appreciation from Aug 2013**). In contrast, rupee appreciation currently has been only 0.1% from the opening levels when the FCNR(B) scheme started. It is important that while the magnitude of appreciation may differ from 2013 given the substantially different global and domestic macroeconomic environment, the direction of the impact must remain supportive for the rupee. **The RBI should look into activist and surprise intervention strategies to ensure that somehow the market bias that exchange rate has only a depreciating bias right now must be corrected.**

An exchange rate appreciation bias is important given the likely global market upheavals. There are 3 clear signals of such.

Firstly, Long-term US Treasury yields is under significant pressure following the July FOMC meeting, with 30-year Treasury yield rising to nearly 5.3%, its highest level since 2007, amid heightened concerns over US fiscal outlook with no attempt by US Government to embark on a path of fiscal consolidation. The jump in US yields is really disconcerting as US inflation numbers have continued to surprise on downside.

Secondly, the U.S. Treasury's decision to sell Euros from its reserves and buy yen was an unusual step to support Japan's currency, after the yen weakened to around ¥164 per dollar, its lowest level in four decades. The intervention pushed the yen up sharply to around ¥156 per dollar, although it later weakened back towards ¥159. It may be noted that during 1998 Asian Financial crisis, The Yen had also collapsed and this resulted in the Federal Reserve selling a reported $ 2 bn dollars to halt the slide of the Yen. The key question is that Japan is also the largest foreign holder of US Treasuries, with more than $1 trillion. If Japan had to sell some of these assets to raise dollars for further yen intervention, it could have pushed treasury prices down and US yields higher.

Thirdly, Brent crude could rise towards $100 per barrel with geopolitical tensions remaining elevated and disruptions around the Strait of Hormuz posing risks to global oil supplies, the upside risks to crude prices remain significant. Our estimates suggest that Brent crude could move beyond $100 per barrel for a while putting pressure on rupee.

We would also advise that RBI can use this opportunity to further diversify its foreign exchange reserves to bring in more portfolio resilience by buying gold.

FCNR(B) SWAP COST IS JUST 1.2% OF FX RESERVES!

- On August 14, 2026, the RBI announced that the window for fresh FCNR(B) deposits under the special swap facility would close prematurely on August 31, 2026, one month earlier than the original September 30 deadline. **We believe that this would lead to a total of 60-65 $bn inflows and $ 80 -85 bn including OFCB's and ECB's.**
- **The potential FCNR(B) mobilisation of $65–70 billion, combined with an average USD/INR hedging cost of around 3% per annum, implies an annual notional hedging cost of about $2.1 billion on a $70 billion corpus.**
- If this cost were to remain at 3% over the five-year maturity of the deposits, **the cumulative cost would amount to around 15% of the corpus, or $10.5 billion**. While this appears sizeable in absolute terms, it needs to be viewed against the scale of India's foreign exchange reserves rather than the FCNR(B) corpus alone. With current reserves at around $700 billion and incremental reserve accumulation assumed at roughly $20 billion annually, the reserve stock could rise to around $800 billion over five years.
- **On this basis, the five-year cumulative hedging cost of $10.5 billion would amount to only 1.45% of the current reserve stock and around 1.27% of the projected reserve stock**. Thus, even under a constant 3% hedging-cost assumption, the notional cost of the FCNR(B) swap remains relatively small compared with the size of the reserve buffer being built, suggesting that the cost is unlikely to represent a significant trade-off against the broader objective of strengthening India's external liquidity and reserve position.
- Though RBI has recouped its Foreign Currency Assets by $31.2 billion (by 07 Aug), i.e., 55% of total amount mobilized, we believe that the RBI may use a part of this amount to invest in US securities given higher yields. As of May 2026, India's holding of US securities was $181 bn . This is a decline from $235 bn a year ago. Thus, there is a need for India to increase its holdings by further investment.

Amount Mobilized ($ Bn)			
	17 July 2026	31 July 2026	13 Aug 2026
FCNR(B) Deposits	17.4	36.7	52.3
OFCBs	2.0	2.6	2.8
ECBs	1.3	1.5	1.7
Total	**20.7**	**40.8**	**56.8**
Memo:			
Rs/$	**96.28**	**95.39**	**95.42**
Incremental FCA	**7.6^**	**21.2**	**31.2***

Source: RBI; P: SBI Projection; ^since 08.06.26 *till 07.08.26

Swap Cost Calculation	
Total FCNR(B) mobilization	$65–70 billion
Annual average USD/INR hedging cost	3.00%
Implied annual hedging cost on $70bn	$2.10 billion
Five year cumulative cost rate	15%
Five-year cumulative hedging cost	$10.5 billion
Current FX reserves	~$700 billion
Average incremental reserve accumulation (FCA) (last 20 years)	~$20 billion per year
Projected FX reserves in 5 years	~$800 billion
5-year hedging cost / current reserves	1.45%
5-year hedging cost / projected reserves	1.27%

Source: SBI Research, RBI

IMPACT ON RUPEE

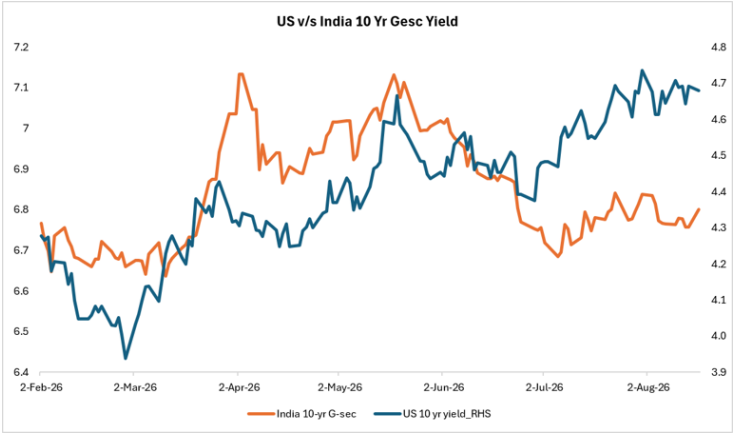
- The experience of the previous FCNR(B) swap window in 2013 provides cues that going forward the Rupee should appreciate. **Although, the impact of FCNR(B) on Rupee in 2026 is clearly not as expected, we believe that going forward the Rupee could appreciate in the range of Rs 95-Rs 95.5 till 31st Aug and beyond thereafter if we draw parallels with the 2013 scheme.**
- In 2013, Rupee was at 65.70 on 31 Aug 2013 and came back to Rs 62.45 on 29 Nov'2013 (4.9% appreciation) and settled at Rs 59.89 (8.8% appreciation from Aug 2013). While the magnitude of appreciation may differ from 2013 given the substantially different global and domestic macroeconomic environment, the direction of the impact is likely to remain supportive for the rupee.

Period	USD INR	% of Appreciation (+) /Depreciation(-)
FCNR(B) Swap in 2013		
31-Aug13	65.70	
23-Oct-13	61.59	6.3%
6-Nov-13	62.40	-1.3%
11-Nov-13	63.24	-1.3%
20-Nov-13	62.58	1.0%
30-Nov-13	62.45	0.2%
30-11-2013 (Cumulative)	62.45	4.9%
28-03-2014(Cumulative)	59.89	8.8%
FCNR(B) Swap in 2026		
8-Jun-26	95.71	
17-Jul-26	96.28	-0.6%
31-Jul-26	95.39	0.9%
13-Aug-26	95.42	0.0%
17-Aug -26 (Cumulative)	95.60	0.1%

THE GLOBAL SITUATION

US TREASURY YIELDS REFLECT CHANGING RATE EXPECTATIONS

- Long-term US Treasury yields came under upward pressure following the July FOMC meeting, with 30-year Treasury yield rising to nearly 5.3%, its highest level since 2007, amid heightened concerns over inflation and US fiscal outlook.
- Market concerns were driven by uncertainty over the Federal Reserve's commitment to maintaining price stability, coupled with persistent fiscal deficits and the rising cost of servicing the US $36 trillion federal debt, which increased the risk premium demanded by investors. While the US-10 year Treasury yield continues to hover near 4.7%, as structural fiscal pressures offset easing expectations of further Federal Reserve tightening.



Source: SBI Research, Bloomberg

US INTERVENTION TO STRENGTHEN YEN

- The U.S. Treasury's decision to sell euros from its reserves and buy yen was an unusual step to support Japan's currency, after the yen weakened to around ¥164 per dollar, its lowest level in four decades.
- The intervention pushed the yen up sharply to around ¥156 per dollar, although it later weakened back towards ¥159.
- The key question is why the US chose to step in. One reason could be the growing link between the yen and US financial markets.
- The large gap between US and Japanese interest rates was encouraging investors to borrow in yen and invest in higher-yielding US assets, putting further pressure on the yen.
- At the same time, volatility in the US Treasury market had increased. Japan is also the largest foreign holder of US Treasuries, with more than $1 trillion. If Japan had to sell some of these assets to raise dollars for further yen intervention, it could push Treasury prices down and US yields higher. In this way, a sharp fall in the yen could eventually create additional pressure in the US bond. market, giving Washington a reason to support the yen.

RBI ASSET DIVERSIFICATION SHOULD CONTINUE

- The Global Financial Crisis of 2008 marked a turning point in reserve management, with central banks increasingly diversifying reserve portfolios towards gold amid heightened financial market uncertainty.
- In 2009, the RBI purchased 200 MT of gold from the IMF for around $6.7 billion, increasing its gold holdings from 357.75 tonnes to 557.75 tonnes.
- Reflecting this strategic shift, gold's share in India's total reserves increased from 3.8% in FY09 to 6.45% in FY10, further rising to 9.18% in FY12, highlighting the growing role of gold in India's reserve management framework.
- After remaining broadly stable between 5% and 8% for over a decade, the RBI accelerated gold accumulation in recent years amid heightened geopolitical tensions, inflation risks and increasing uncertainty in global financial markets.
- **Consequently, gold's share in India's total reserves reached a record 16.70% in FY26, before moderating marginally to 15.38% (as on 7 Aug 2026), underscoring the RBI's continued focus on reserve diversification and portfolio resilience.**

BRENT CRUDE COULD GO UP T0 $ 100 PER BARREL

- With US Treasury yields remaining elevated, the global macro environment continues to reflect persistent inflation and geopolitical risks, while the oil market remains exposed to supply disruptions in the Middle East. Brent crude is currently around $88 per barrel, and with the Strait of Hormuz still facing disruption, the risk of a further rise remains significant. Our estimates **suggest that given this the oil could touch $100 per barrel and move even further up.**

Source: RBI, Data as on end of Financial Year

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