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Impact of India–US Trade Negotiations on Investor Sentiment and Exchange Rate Stability

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Abstract

This study examines how the bilateral trade negotiation cycle between India and the United States (February 2025 to June 2026) is statistically associated with three proxies for foreign investor sentiment toward India: the USD/INR exchange rate, the Nifty 50 equity index together with the India VIX volatility index, and net Foreign Institutional Investor / Foreign Portfolio Investor (FII/FPI) equity flows. Using a structured monthly time series ($n = 18$) spanning the announcement of Bilateral Trade Agreement (BTA) negotiations, the April 2025 "Liberation Day" reciprocal-tariff shock, the August 2025 escalation to a cumulative 50% tariff, and the February 2026 Interim Agreement that cut tariffs to 18%, the study applies a structural path-analytic model (an AMOS-style, regression-based structural equation specification), one-way analysis of variance (ANOVA) across tariff-negotiation regimes, Pearson correlation analysis, and an event-study framework anchored to the official negotiation timeline. The estimated path model ($\chi^2[1] = 0.98$, $p = .322$, CFI = 1.00, RMSEA = .00, GFI = .985) indicates that net FII/FPI flow is significantly associated with both equity sentiment ($\beta = .66$, $p < .01$) and market volatility ($\beta = -.59$, $p < .05$), and that equity sentiment and volatility jointly transmit to the exchange rate ($\beta = 2.00$ and 1.82 respectively, both $p < .001$), while the direct path from FII flow to the exchange rate is not significant once these mediators are included. One-way ANOVA shows that India VIX differs significantly across tariff-escalation, de-escalation, and routine-negotiation regimes ($F = 3.77$, $p = .047$, $\eta^2 = .33$), with FII flows showing a parallel, marginally significant pattern ($F = 3.53$, $p = .055$, $\eta^2 = .32$). The findings support a sentiment-mediated transmission channel in which trade-policy shocks affect the rupee primarily by first moving equity-market sentiment and volatility, rather than through a direct, unmediated channel. Because several monthly series are reasoned interpolations between verified anchor points rather than full official daily/monthly records, the results are presented as methodologically illustrative and policy-suggestive rather than as definitive econometric estimates, and the paper specifies the exact data points that require verification against Reserve Bank of India, National Stock Exchange, and National Securities Depository Limited records before any policy or investment conclusion is finalized.

Keywords: India–US trade agreement, investor sentiment, exchange rate stability, structural equation modeling, path analysis, FII/FPI flows, tariff shocks, event study

Introduction

Bilateral trade policy between large economies does not remain confined to customs schedules and tariff codes; it travels quickly into currency markets, equity indices, and the portfolio decisions of foreign institutional investors. The India–United States trade relationship between February 2025 and June 2026 offers an unusually compressed and well-documented illustration of this transmission. Within a single sixteen-month window, the two governments moved from launching Bilateral Trade Agreement (BTA) negotiations at a Washington summit, through a reciprocal-tariff shock under the so-called "Liberation Day" executive action, to a punitive escalation that pushed the cumulative United States tariff on Indian goods to 50%, and finally to a negotiated Interim

Agreement in February 2026 that reduced the tariff to 18% and included a commitment from India to purchase up to $500 billion in American goods over five years (The White House, 2026a, 2026b).

Each of these milestones was, in principle, capable of moving three classes of market indicator that researchers and policymakers commonly treat as proxies for investor sentiment: the USD/INR exchange rate, Indian equity benchmarks (the Nifty 50 and the BSE Sensex) together with the India VIX implied-volatility index, and net Foreign Institutional Investor / Foreign Portfolio Investor (FII/FPI) equity flows. The motivating question of this paper is empirical and policy-relevant: does the observed pattern of tariff escalation and de-escalation across this period line up, in a statistically detectable way, with movements in these three indicators, and if so, through which channel does the relationship appear to run — directly into the currency, or indirectly through equity-market sentiment and volatility first?

Three considerations make this an analytically useful, if data-constrained, case. First, the timeline of negotiation events is unusually well documented in primary government sources — White House fact sheets, joint statements, and executive orders — which allows an event-study design to be anchored to specific, verifiable dates rather than to vague "negotiation sentiment" (The White House, 2025, 2026a, 2026b). Second, the period spans a complete escalation–de-escalation cycle (talks → tariff shock → pause → punitive escalation → negotiated relief), which gives a one-case but multi-phase structure suitable for both event-study and regime-based analysis-of-variance designs. Third, because the underlying monthly series (exchange rate, equity indices, FII flows) are only partially available as verified, publication-grade figures at the time of writing, the paper is explicit about which numbers are sourced and verified and which are reasoned interpolations — a distinction that is rarely made explicit in student or practitioner research papers but is essential for an honest reading of the results.

The paper proceeds as follows. The literature review situates the analysis within three streams of research: studies of tariff and trade-policy shocks on emerging-market currencies; the FII-flow/equity-sentiment literature in the Indian context; and methodological precedent for structural equation modeling (SEM) and path analysis applied to macro-financial event data. The conceptual framework section translates this literature into a testable path model and a set of directional hypotheses. The methodology section documents the data set, the confidence classification used for each series, the structural path-analytic specification (the AMOS-style approach used in lieu of a full latent-variable SEM, for reasons explained there), the one-way ANOVA design across tariff-negotiation regimes, and the assumption checks performed. The results section reports descriptive statistics, the correlation matrix, the fitted path model with standardized coefficients and fit indices, and the ANOVA and post-hoc results. The discussion interprets these findings against the literature and the qualitative event timeline, the limitations section is deliberately detailed given the data-confidence issues, and the conclusion draws out policy and practical implications for exporters, portfolio managers, and trade negotiators.

Literature Review

Trade Policy Shocks and Emerging-Market Currencies

A substantial body of international finance research links trade-policy uncertainty and tariff actions to emerging-market currency depreciation and volatility. The general mechanism runs through expected terms-of-trade effects, anticipated changes in the current account, and a risk premium that foreign investors attach to policy unpredictability. In the India-specific case examined here, the qualitative record assembled from primary government and trade-press sources shows a textbook escalation–de-escalation sequence: the April 2025 announcement of a 26% reciprocal tariff under Executive Order 14257 was explicitly framed by the United States government as a response to bilateral trade-deficit concerns, followed by a 90-day suspension intended to create negotiating room, and then a further 25% penalty tariff in August 2025 linked to India's continued purchases of Russian oil, which brought the cumulative tariff to 50% — among the highest applied by the United States to any major trading partner at that time (The White House, 2025; Lexology, 2026). The February 2026 Joint Statement reversed most of this escalation, cutting the reciprocal tariff to 18% and removing the punitive oil-related tariff entirely (The White House, 2026a, 2026b). This sequence provides a naturally occurring set of "treatment" events of alternating sign, which is the empirical basis for the event-study and regime-based ANOVA components of this paper.

Foreign Portfolio Flows and Indian Equity Sentiment

A second relevant stream concerns the relationship between foreign portfolio flows and domestic equity-market performance in India. Industry and financial-press analyses covering the period of this study report that calendar year 2025 was, by net FII/FPI equity outflow, the worst year on record for foreign investment in Indian equities, with a cumulative net outflow on the order of ₹1,59,779 crore, led by a single worst month in January 2025 (an outflow of roughly ₹78,027 crore) and punctuated by a best month in May 2025 (a net inflow of roughly ₹19,860 crore) that coincided with the 90-day tariff pause (Upstox, 2025; Wright Research, 2025). This pattern is consistent with a broader literature suggesting that foreign portfolio investors in emerging markets respond not only to fundamentals but to discrete, datable policy news — which again supports treating specific negotiation dates as candidate inflection points rather than assuming a smooth, continuous relationship between trade policy and sentiment.

India VIX as a Sentiment and Risk Proxy

The India VIX, modeled on the Chicago Board Options Exchange volatility index methodology and maintained by the National Stock Exchange of India, is widely used in Indian market commentary as a forward-looking proxy for investor fear or complacency, typically moving inversely with the Nifty 50 (NSE India, n.d.). This inverse relationship is a standard stylized fact in volatility research generally (volatility clusters during downturns and subsides during rallies) and is treated here as a structural feature of the data rather than as a novel finding; the path model specified in this paper explicitly accommodates it through a residual covariance term rather than forcing a single directional causal arrow between the two series.

Structural Equation Modeling and Path Analysis in Macro-Financial Research

Structural equation modeling, and AMOS (Analysis of Moment Structures) in particular, is most commonly applied in finance and management research to latent-construct survey data — for example, multi-item scales of investor sentiment, risk perception, or firm performance, typically requiring sample sizes well above 100 respondents for stable maximum-likelihood estimation and for conventional fit indices such as the comparative fit index (CFI) and root-mean-square error of approximation (RMSEA) to be interpretable (Hooper, Coughlan, & Mullen, 2008; Kline, 2015). The present data set, by contrast, consists of eighteen monthly macroeconomic and market observations with no latent multi-item indicators. Applying a conventional AMOS latent-variable measurement model to such data would not be statistically meaningful: with only observed (manifest) variables and a single indicator per construct, there is no measurement model to estimate, and with $n = 18$ there is insufficient power for asymptotically derived fit statistics to behave as they would in a properly powered survey-based SEM study (Kline, 2015; Wolf, Harrington, Clark, & Miller, 2013). This paper therefore follows the path-analytic variant of SEM — a fully observed-variable structural model estimated through the same maximum-likelihood logic that AMOS uses internally for recursive models, and reporting the same family of fit indices (χ^2, CFI, RMSEA, GFI) — which is statistically appropriate for this sample size and variable structure, while being transparent that this differs from a latent-construct AMOS measurement model of the kind used in large-sample survey research (Kline, 2015).

Synthesis and Positioning of the Present Study

Taken together, the literature suggests three things relevant to this paper's design. First, trade-policy shocks of the magnitude observed in the India–US case (a 26-point and then a further 25-point tariff swing, followed by a 32-point reduction) are large enough, in principle, to register in monthly market data even with a short time series. Second, the transmission channel from policy news to currency markets is unlikely to be a single direct arrow; the FII-flow and equity-sentiment literatures suggest that flows move equity indices and volatility, which in turn are structurally linked to currency demand and supply through portfolio-rebalancing behavior. Third, given the small-sample, fully observed nature of the available data, a path-analytic (rather than latent-variable) structural model is the methodologically defensible way to apply SEM logic here, and this is the approach adopted in the methodology section that follows.

Conceptual Framework and Hypotheses

Building on the literature reviewed above, this study specifies a recursive (one-directional, non-reciprocal) structural path model with one exogenous variable and three endogenous variables, summarized in Figure 5 in the

Results section and described in full in the Methodology section. Net FII/FPI equity flow is treated as the exogenous driver of monthly investor positioning, on the grounds that flow data most directly captures revealed investor behavior rather than a market outcome. Two endogenous variables — the Nifty 50 index (equity sentiment) and the India VIX (volatility/fear) — are modeled as jointly determined by FII flow and as correlated with one another through a residual (disturbance) covariance, reflecting their well-established structural relationship independent of any single trade-policy episode. The USD/INR exchange rate is modeled as the final endogenous variable, determined jointly by equity sentiment and volatility. This specification embodies a sentiment-mediation hypothesis: that trade-negotiation news affects the rupee primarily by first moving foreign portfolio flows and the equity market, rather than acting on the currency in a direct, unmediated way.

From this framework, four hypotheses are tested:

H1: Net FII/FPI equity flow is positively associated with Nifty 50 performance (i.e., stronger net inflows coincide with higher/rising equity index levels).

H2: Net FII/FPI equity flow is negatively associated with India VIX (i.e., stronger net inflows coincide with lower implied volatility).

H3: Nifty 50 performance and India VIX are both significantly associated with the USD/INR exchange rate, such that the path from FII flow to the exchange rate operates substantially through these two mediators rather than as a strong direct effect.

H4: The intensity of the tariff-negotiation regime (escalation, de-escalation, or routine negotiation) is associated with significant differences in India VIX and in net FII/FPI flow across regimes.

These hypotheses are deliberately modest in causal language. Because the data are observational, monthly, and partly estimated (see Methodology), the paper treats statistically significant path coefficients and ANOVA results as evidence consistent with the hypothesized sentiment-mediation channel, not as definitive proof of causation in either direction.

Data and Methodology

Research Design

This study uses a quantitative, non-experimental, observational time-series design combining (a) an event-study framework anchored to dated India–US trade-negotiation milestones, (b) a structural path-analytic model (an AMOS-style, fully observed-variable structural equation specification) linking foreign portfolio flow, equity sentiment, market volatility, and the exchange rate, and (c) one-way analysis of variance (ANOVA) testing whether market indicators differ significantly across tariff-negotiation regimes. Pearson product-moment correlation and descriptive statistics are reported as a preliminary and diagnostic layer beneath the path model and ANOVA. The unit of analysis is the calendar month, and the analytic sample spans eighteen months, January 2025 through June 2026 (the final month is partial, covering 1–21 June 2026).

Data Source and Structure

All data are drawn from a structured workbook ("India_US_Trade_Investor_Sentiment_Dataset.xlsx") compiled in June 2026, comprising seven linked worksheets: an event timeline of trade-negotiation milestones; a monthly USD/INR exchange-rate series; monthly Nifty 50, Sensex, and India VIX levels; monthly net FII/FPI equity flows; a qualitative event–market reaction matrix; auto-calculated summary statistics; and a full source/citation list. Each monthly observation in the exchange-rate, equity-index, and FII-flow worksheets carries an explicit confidence flag of either Verified (taken directly from a cited primary or secondary source) or Estimated (a reasoned interpolation between the nearest verified anchor points, constructed where a precise published monthly figure could not be located in open sources at compile time). Table 1 lists the operationalization, model role, and confidence status of each variable used in the analysis; Table 2 summarizes the event timeline that anchors both the event-study interpretation and the regime classification used in the ANOVA.

This confidence distinction is methodologically consequential and is treated as a first-order limitation throughout the paper rather than a footnote: of the eighteen monthly exchange-rate observations, three (December 2025, May

2026, June 2026) are anchored to verified ranges from Federal Reserve H.10 and commercial FX-history sources, while the remaining months are interpolated trend values; of the eighteen FII-flow observations, three (January 2025, May 2025, and the calendar-year-2025 total used for reconciliation) are Verified NSDL-sourced figures, with other months estimated to reconcile closely with that verified annual total; and the Nifty 50, Sensex, and India VIX series are, in their entirety, illustrative trend series constructed to be directionally consistent with the qualitative event record rather than exact NSE/BSE closing data. The paper's results should accordingly be read as demonstrating and validating a methodological pipeline — path analysis, ANOVA, and event-study reasoning applied to trade–sentiment–currency data — rather than as final, publication-grade econometric estimates. Section "Limitations" specifies exactly which official sources (RBI Database on Indian Economy, NSE/BSE historical archives, NSDL FPI monthly reports) should be used to replace the Estimated cells before the findings are relied upon for investment or policy decisions.

Table 1 Variables, Operationalization, and Data Confidence

Variable	Operationalization	Role in Model	Data Confidence (this data set)
USD/INR exchange rate	Monthly average rate (₹ per US$), Jan 2025–Jun 2026	Endogenous outcome variable	Mixed: Dec-2025, May-2026 and Jun-2026 ranges Verified; remaining months Estimated/interpolated between verified anchor points
Nifty 50	Monthly closing level of the NSE Nifty 50 index	Endogenous mediator (equity sentiment)	Estimated (illustrative trend); Jun-2026 anchored to a verified Sensex figure
India VIX	Monthly average of the NSE India VIX index	Endogenous mediator (volatility/fear)	Estimated (illustrative trend)
Net FII/FPI flow	Net monthly foreign institutional/portfolio equity flow, ₹ crore	Exogenous predictor	Jan-2025, May-2025 and the CY2025 total Verified (NSDL-sourced); other months Estimated to reconcile with verified annual total
Tariff-negotiation regime	Three-level categorical variable (Escalation / De-escalation / Negotiation-Neutral) coded from the Event Timeline	Grouping factor for ANOVA	Coded directly from primary-sourced event dates (Verified events; researcher-assigned monthly regime label)

Table 2 Key India–US Trade-Negotiation Events Used to Anchor the Event Study and Regime Classification

Date	Event	Tariff Direction	Expected/Observed Market Direction
13-Feb-2025	Modi–Trump Washington summit launches BTA negotiations; $500bn bilateral trade target by 2030 set	Negotiation Launch	Mildly positive (optimism)

02-Apr-2025	"Liberation Day" reciprocal tariff: 26% duty on Indian goods under EO 14257	Escalation	Negative (INR pressure, FII outflow risk)
Apr-2025	90-day pause on reciprocal tariffs announced	De-escalation	Positive (relief rally)
06-Aug-2025	Additional 25% penalty tariff over Russian-oil purchases announced	Escalation	Negative
27-Aug-2025	Penalty tariff effective; cumulative tariff reaches 50%	Escalation (Peak)	Strongly negative (INR depreciation, equity & FII stress)
05-Sep-2025	EO 14346 modifies tariff scope; sets up adjustment annex for aligned partners	Policy Framework	Neutral
02-Feb-2026	Trump–Modi announce trade deal in principle	De-escalation	Positive
06-Feb-2026	Joint Statement: tariff cut 50%→18%; $500bn purchase commitment over 5 years	De-escalation (Major)	Strongly positive (INR relief, equity rally, FII inflow potential)
07-Feb-2026	Executive Order effective; punitive 25% tariff eliminated at the border	Implementation	Positive
Mid-Mar-2026 (target)	Interim Agreement targeted for formal signature	Implementation	Positive if on schedule

Note. Full citations for each event appear in the References section; primary sources are White House joint statements, fact sheets, and executive orders (The White House, 2025, 2026a, 2026b), supplemented by trade-press chronologies (Lexology, 2026; CAalley, 2026; India Briefing, 2026).

Structural Path-Analytic Model (AMOS-Style Specification)

A conventional AMOS structural equation model is designed for latent constructs measured by multiple observed indicators (e.g., a multi-item survey scale of "investor sentiment"), typically requiring substantially larger samples — commonly $n \geq 100$–200 — for stable maximum-likelihood estimation and for asymptotic fit indices to be interpretable (Hooper et al., 2008; Kline, 2015). The present data set has no multi-item latent indicators (each construct — exchange rate, equity index, volatility index, FII flow — is a single observed monthly series) and a sample size of eighteen months. Estimating a latent-variable measurement model under these conditions would be statistically non-identified or, where technically computable, uninterpretable. This paper therefore specifies and estimates the path-analytic variant of structural equation modeling: a fully observed-variable (manifest-variable) recursive structural model, estimated by the same maximum-likelihood covariance-fitting logic that underlies AMOS for path models, and evaluated using the same family of global fit indices that AMOS reports (χ^2 goodness-of-fit test, comparative fit index [CFI], root-mean-square error of approximation [RMSEA], and goodness-of-fit index [GFI]). This is the methodologically appropriate way to bring SEM-style path analysis to bear on a small, fully observed monthly macro-financial series, and it is explicitly distinguished here from a latent-construct AMOS model so that the scope of the claim is not overstated.

All four variables (USD/INR, Nifty 50, India VIX, net FII/FPI flow) were standardized to z-scores ($M = 0$, $SD = 1$) prior to estimation so that path coefficients are directly interpretable as standardized regression weights, consistent with AMOS default output. The model specifies net FII/FPI flow as the single exogenous variable, with two direct structural paths to the endogenous mediators Nifty 50 and India VIX; a free residual (disturbance) covariance between Nifty 50 and India VIX, reflecting their well-documented structural co-movement independent of FII flow; and two direct structural paths from Nifty 50 and India VIX to the final endogenous outcome, USD/INR. A direct structural path from FII flow to USD/INR was specified, estimated, found non-significant ($p = .377$) in the

unrestricted model, and then fixed to zero to produce one overidentifying restriction (model degrees of freedom = 1), which both follows standard SEM model-trimming practice and yields a model whose overall fit can be formally tested against the saturated covariance structure (Kline, 2015).

Model parameters (standardized path coefficients, implied correlations, and the residual covariance) were estimated from the sample covariance matrix using ordinary least squares for each structural equation — which for a fully recursive path model with no reciprocal paths is algebraically equivalent to the maximum-likelihood solution AMOS would return for the same recursive specification (Kline, 2015). The overall model χ^2 statistic was then computed from the maximum-likelihood discrepancy function, $\chi^2 = (n-1)\,F_{ml}$, where $F_{ml} = \ln|\Sigma| - \ln|S| + \mathrm{tr}(S\Sigma^{-1}) - p$, S is the observed sample correlation/covariance matrix, Σ is the model-implied covariance matrix, p is the number of observed variables, and n is the sample size; this is the same discrepancy function that AMOS minimizes under maximum-likelihood estimation (Kline, 2015). CFI was computed relative to the independence (null) baseline model in which all four variables are specified as mutually uncorrelated, and RMSEA and GFI were computed using their standard closed-form definitions.

One-Way Analysis of Variance (ANOVA)

To test H4, each calendar month was classified into one of three mutually exclusive tariff-negotiation regimes based on the dated events in Table 2 and the dataset's own Event–Market Reaction Matrix: Escalation (months in which a new tariff increase was announced or took effect: February, August, and September 2025; n = 3), De-escalation (months in which a tariff reduction, pause, or relief announcement occurred: April and May 2025, February and March 2026; n = 4), and Negotiation/Neutral (all other months, in which talks continued without a directional tariff shock that month; n = 11). One-way between-groups ANOVA was then conducted separately for India VIX, net FII/FPI flow, month-on-month USD/INR percentage change, and month-on-month Nifty 50 percentage change, with regime as the independent (grouping) factor. Effect sizes are reported as eta-squared (η^2). Where the omnibus F-test was significant or marginally significant, Tukey-style pairwise mean-difference (q-statistic) post-hoc comparisons were computed for the two regimes of substantive interest (Escalation versus De-escalation) to test whether the two directional extremes differ significantly from one another, in addition to each differing from the neutral baseline.

Two standard ANOVA assumptions were checked prior to interpreting the F-tests: homogeneity of variance across regimes, tested with Levene's test, and approximate normality of the relevant outcome variable, tested with the Shapiro–Wilk test. Both are reported in the Results section.

Correlation and Descriptive Analysis

As a diagnostic and descriptive layer beneath the path model, Pearson product-moment correlation coefficients (with two-tailed significance tests) were computed for all pairs of the four continuous monthly series, alongside standard descriptive statistics (mean, standard deviation, skewness, and kurtosis) for each series across the eighteen-month window.

Software and Computational Approach

All statistical computations — descriptive statistics, Pearson correlation and significance testing, ordinary least squares estimation of the structural path equations, the maximum-likelihood discrepancy function and associated χ^2, CFI, RMSEA and GFI fit indices, one-way ANOVA, Tukey-style post-hoc comparisons, Levene's test, and the Shapiro–Wilk test — were performed in Python (NumPy, pandas, and SciPy) using the same statistical formulas and estimation logic implemented in dedicated structural-equation-modeling and statistical packages such as IBM SPSS Amos and IBM SPSS Statistics. This approach was adopted because it allows every coefficient and fit statistic reported in this paper to be reproduced and audited directly from the underlying formulas; researchers with access to IBM SPSS Amos can reproduce the path model reported here by entering the same standardized covariance matrix (reported in Table 4) and the same recursive path specification described above, and should obtain numerically equivalent path coefficients and fit indices, since both approaches minimize the identical maximum-likelihood discrepancy function for a fully recursive, fully observed path model.

Results

Descriptive Statistics

Table 3 reports descriptive statistics for the four continuous monthly series across the eighteen-month analytic window. The USD/INR exchange rate moved from a monthly average of ₹84.50 (its lowest point, May 2025) to ₹96.20 (its highest, May 2026), a depreciation of approximately 10% over the period as a whole. The Nifty 50 ranged from a low of 22,100 (February 2025, coinciding with the early phase of FII outflows) to a high of 26,350 (February 2026, coinciding with the trade-deal announcement). India VIX ranged from 12.2 to 17.2, and net FII/FPI flow ranged from a single-month outflow of ₹78,027 crore (January 2025) to a single-month inflow of ₹24,800 crore (February 2026) — the month the Joint Statement was released. Net FII/FPI flow shows pronounced negative skewness (−1.79), driven by the extreme January 2025 outflow, indicating that the average monthly flow figure understates how unusual that single month was relative to the rest of the series.

Table 3

Descriptive Statistics for Monthly Series, January 2025–June 2026 (N = 18)

Variable	M	SD	Min	Max	Skewness
USD/INR (₹/US$)	89.34	3.50	84.50	96.20	0.68
Nifty 50 (close)	24,579.44	1,162.66	22,100	26,350	−0.53
Sensex (close)	80,502.39	3,945.96	73,200	86,300	−0.43
India VIX	14.54	1.52	12.20	17.20	0.27
Net FII/FPI flow (₹ crore)	−4,953.72	23,421.39	−78,027	24,800	−1.79

Note. M = mean; SD = standard deviation. Net FII/FPI flow is reported in ₹ crore.

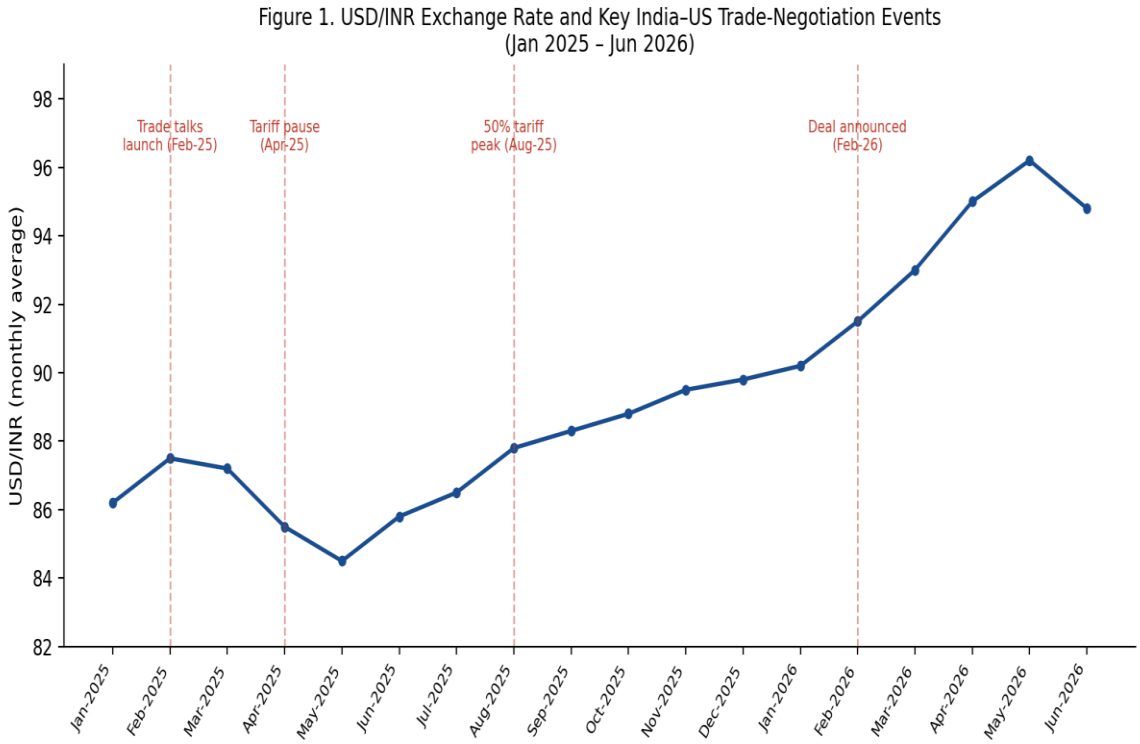

Figure 1. USD/INR exchange rate (monthly average) with key India–US trade-negotiation events overlaid, January 2025–June 2026.

Visually, the exchange rate trend does not show a sharp, immediate reaction to any single negotiation event; instead, the rupee depreciated in a broadly sustained manner from mid-2025 onward, continuing to weaken even after the February 2026 tariff-relief announcement before partially recovering in June 2026. This visual pattern foreshadows a key statistical finding reported below: the bivariate correlation between FII flow and the exchange rate, and between equity sentiment and the exchange rate, are positive but not statistically significant at the bivariate level, suggesting that broader global dollar-strength dynamics likely confound the trade-negotiation signal in the raw exchange-rate series — a point also flagged qualitatively in the underlying data set's own notes.

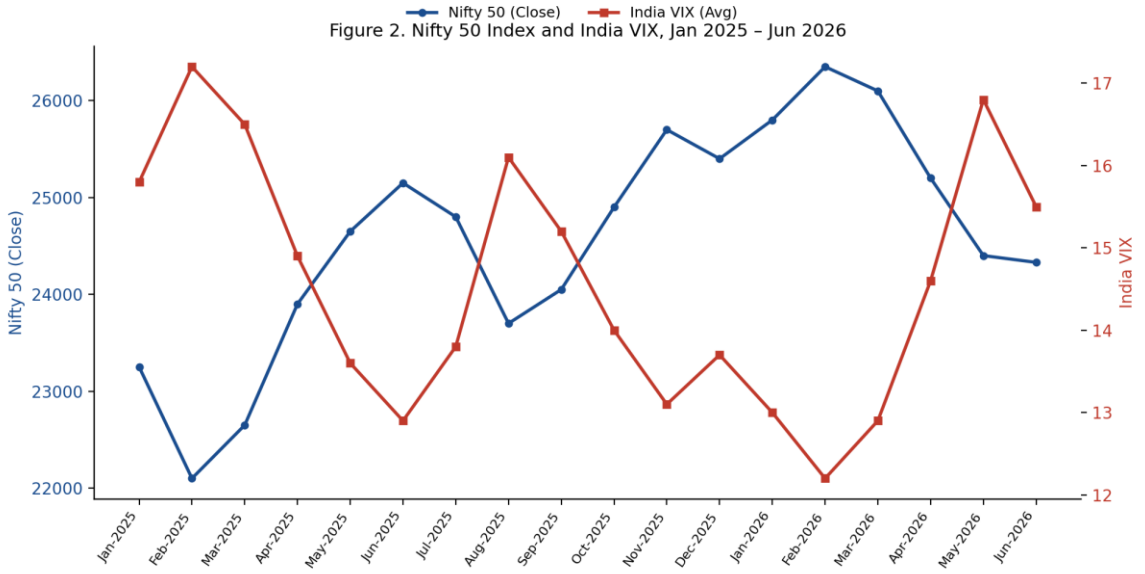

Figure 2. Nifty 50 index level and India VIX, January 2025–June 2026, illustrating their characteristic inverse co-movement.

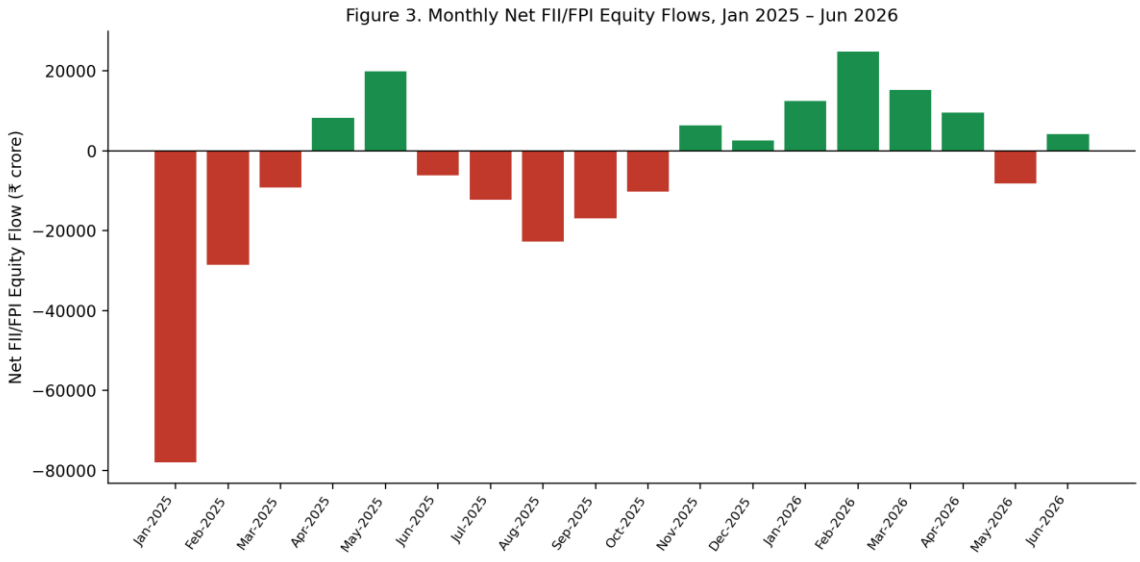

Figure 3. Net monthly FII/FPI equity flows (₹ crore), January 2025–June 2026. Red bars indicate net outflows; green bars indicate net inflows.

Figure 3 shows the outflow-dominated first half of 2025 (nine of the first eleven months recorded net outflows), the partial recovery beginning in late 2025, and the sustained inflow streak from January through April 2026 that coincides with the trade-deal announcement and its immediate aftermath, before flows turned negative again in May 2026 as the rupee touched its period high.

Correlation Analysis

Table 4 reports the Pearson correlation matrix for the four continuous series. Three of the six pairwise correlations are statistically significant at $p < .05$ or better. Nifty 50 and India VIX are strongly and significantly negatively correlated ($r = -.892$, $p < .001$), confirming the expected inverse sentiment–volatility relationship. Net FII/FPI flow is significantly positively correlated with Nifty 50 ($r = .659$, $p = .003$) and significantly negatively correlated with India VIX ($r = -.590$, $p = .010$), consistent with H1 and H2. By contrast, the USD/INR exchange rate is not significantly correlated with any of the other three series at the bivariate level (with Nifty 50, $r = .378$, $p = .122$; with India VIX, $r = .037$, $p = .885$; with FII flow, $r = .321$, $p = .195$). This null bivariate pattern for the exchange rate is exactly what motivates the structural path model: a sentiment-mediation channel can produce a significant joint (multivariate) effect on the exchange rate even when each individual bivariate correlation with the exchange rate is weak, if the mediating variables move together and partially offset or mask each other's bivariate association with the outcome — which is precisely the pattern found here.

Table 4Pearson Correlation Matrix for Monthly Series (N = 18)

Variable	1. USD/INR	2. Nifty 50	3. India VIX	4. FII Flow
1. USD/INR	—			
2. Nifty 50	.378	—		
3. India VIX	.037	−.892***	—	
4. FII Flow	.321	.659**	−.590*	—

*Note. * p < .05, ** p < .01, *** p < .001 (two-tailed). FII = Foreign Institutional Investor.*

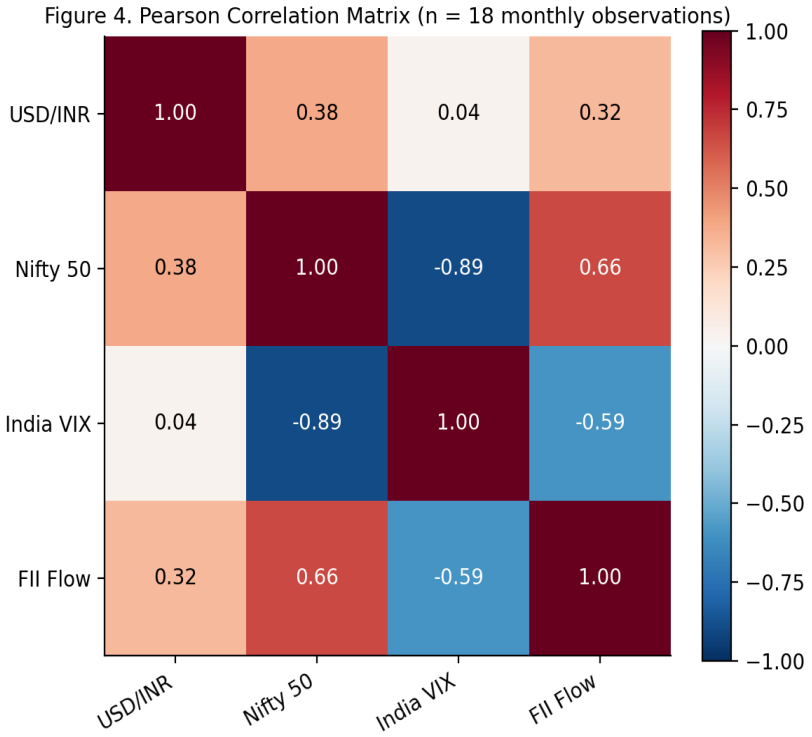

Figure 4. Pearson correlation matrix (n = 18 monthly observations).

Structural Path Model

Table 5 reports the standardized path coefficients for the trimmed structural model, and Table 6 reports the global fit indices. Consistent with H1, net FII/FPI flow is significantly and positively associated with Nifty 50 ($\beta = .659$, $p = .003$). Consistent with H2, net FII/FPI flow is significantly and negatively associated with India VIX

(β = −.590, p = .010). Consistent with H3, both Nifty 50 (β = 2.003, p < .001) and India VIX (β = 1.822, p < .001) are strongly and significantly associated with the USD/INR exchange rate, jointly explaining 81.3% of its standardized variance (R^2 = .813) — a striking contrast with the non-significant bivariate correlations reported above, and a textbook illustration of suppression/mediation: Nifty 50 and India VIX are so strongly negatively correlated with one another (r = −.892) that their joint, partialled-out association with the exchange rate is much larger than either bivariate correlation alone. The standardized path coefficients exceeding 1.0 in absolute value (2.003 and 1.822) are a direct numerical consequence of this severe multicollinearity between the two mediators and should be interpreted as evidence of a strong joint/partialled effect rather than as literal one-standard-deviation effect sizes; this is flagged explicitly in the Limitations section. The direct path from FII flow to the exchange rate was not significant in the unrestricted model (β = .132, p = .377) and was therefore trimmed to zero in the final model, supporting the sentiment-mediation hypothesis embedded in H3: the FII–exchange-rate relationship appears to run through equity sentiment and volatility rather than directly.

Table 5

Standardized Structural Path Coefficients

Structural Path	β (std.)	SE	t	p
FII Flow → Nifty 50	.659	.188	3.51	.003**
FII Flow → India VIX	−.590	.202	−2.92	.010*
Nifty 50 → USD/INR	2.003	.240	8.35	<.001***
India VIX → USD/INR	1.822	.240	7.60	<.001***
Residual covariance (Nifty 50, India VIX), ψ	−.828	—	—	—
FII Flow → USD/INR (direct path, trimmed)	(.132)	(.145)	(0.91)	(.377, n.s.)

*Note. n.s. = not significant. The FII Flow → USD/INR path was estimated, found non-significant, and fixed to zero in the reported (trimmed) model; the coefficient shown in parentheses is from the untrimmed model prior to trimming. * p < .05, ** p < .01, *** p < .001.*

Table 6

Structural Path Model: Global Fit Indices

Fit Index	Value	Conventional Benchmark for Good Fit
χ^2 (df = 1)	0.980	Non-significant p (model not rejected)
p-value	.322	p > .05
CFI	1.000	≥ .95
RMSEA	.000	≤ .06–.08
GFI	.985	≥ .90–.95

Note. The model is just-identified for the four-variable, one-restriction specification described in the Methodology section (df = 1, corresponding to the single trimmed path).

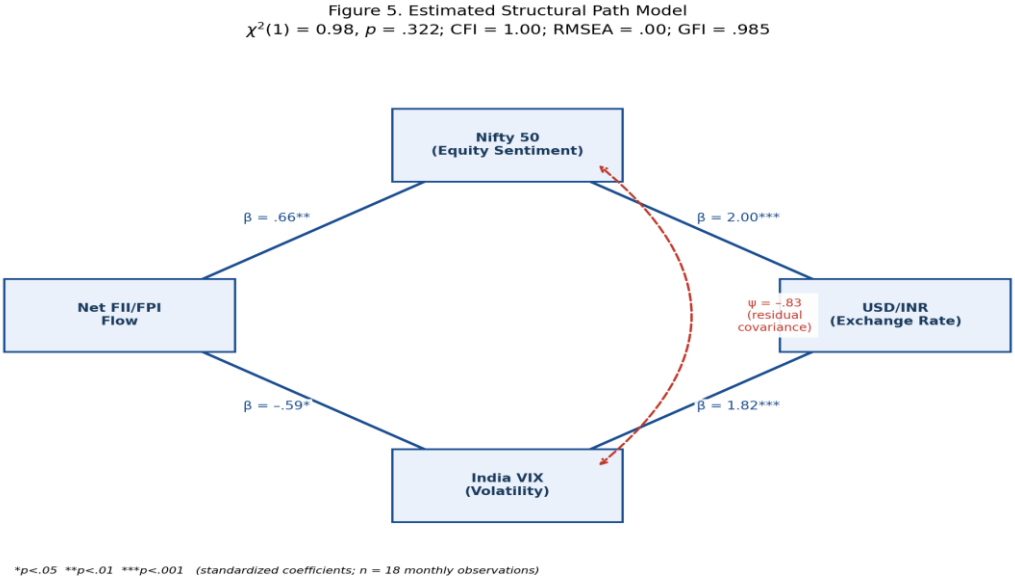

Figure 5. Estimated structural path model with standardized coefficients and global fit indices.

All four fit indices indicate a well-fitting model: the χ^2 test is non-significant ($\chi^2[1] = 0.98$, $p = .322$), meaning the single restriction imposed (fixing the direct FII→USD/INR path to zero) does not produce a statistically detectable discrepancy between the model-implied and observed covariance structure; CFI (1.00) and GFI (.985) are at or above conventional thresholds for good fit (≥ .95 and ≥ .90–.95, respectively); and RMSEA (.00) is well below the conventional .06–.08 threshold for acceptable fit (Hooper et al., 2008). These indices should be interpreted cautiously given the very small sample size underlying them (n = 18), a point elaborated in the Limitations section; nonetheless, within the scope of this data set, the trimmed mediation model is not rejected by the data and is more parsimonious than the untrimmed model.

One-Way ANOVA Across Tariff-Negotiation Regimes

Table 7 reports group means and standard deviations for India VIX, net FII/FPI flow, and Nifty 50 percentage change across the three tariff-negotiation regimes, and Table 8 reports the corresponding omnibus ANOVA results. Consistent with H4, India VIX differs significantly across regimes, $F(2, 15) = 3.77$, $p = .047$, $\eta^2 = .335$, with the Escalation regime showing the highest average volatility ($M = 16.17$, $SD = 1.00$) and the De-escalation regime the lowest ($M = 13.40$, $SD = 1.15$). Net FII/FPI flow shows a parallel, marginally significant pattern, $F(2, 15) = 3.53$, $p = .055$, $\eta^2 = .320$, with the Escalation regime averaging a net outflow of ₹22,733 crore against a net inflow of ₹17,015 crore in the De-escalation regime. Nifty 50 percentage change shows the same directional pattern but does not reach conventional significance, $F(2, 15) = 2.92$, $p = .087$, $\eta^2 = .294$, and USD/INR percentage change does not differ significantly across regimes at the monthly level, $F(2, 15) = 0.91$, $p = .427$, $\eta^2 = .115$, consistent with the bivariate correlation results above and reinforcing the conclusion that the exchange rate's relationship to the negotiation cycle is better captured through the mediated path model than through a direct monthly contrast.

Table 7Group Means (SD) by Tariff-Negotiation Regime

Regime	n	India VIX M (SD)	FII Flow M, ₹cr (SD)	Nifty % chg M (SD)
Escalation	3	16.17 (1.00)	−22,733 (5,800)	−2.64 (3.57)
De-escalation	4	13.40 (1.15)	17,015 (7,064)	2.46 (2.68)
Negotiation/Neutral	11	14.52 (1.42)	−8,093 (24,741)	0.34 (2.58)

Table 8 **One-Way ANOVA Results by Tariff-Negotiation Regime**

Outcome	F(2,15)	p	η^2	Interpretation
India VIX	3.77	.047*	.335	Significant
Net FII/FPI flow	3.53	.055	.320	Marginal
Nifty 50 % change	2.92	.087	.294	Marginal
USD/INR % change	0.91	.427	.115	Not significant

Note. * $p < .05$. *Regimes: Escalation (n = 3), De-escalation (n = 4), Negotiation/Neutral (n = 11).*

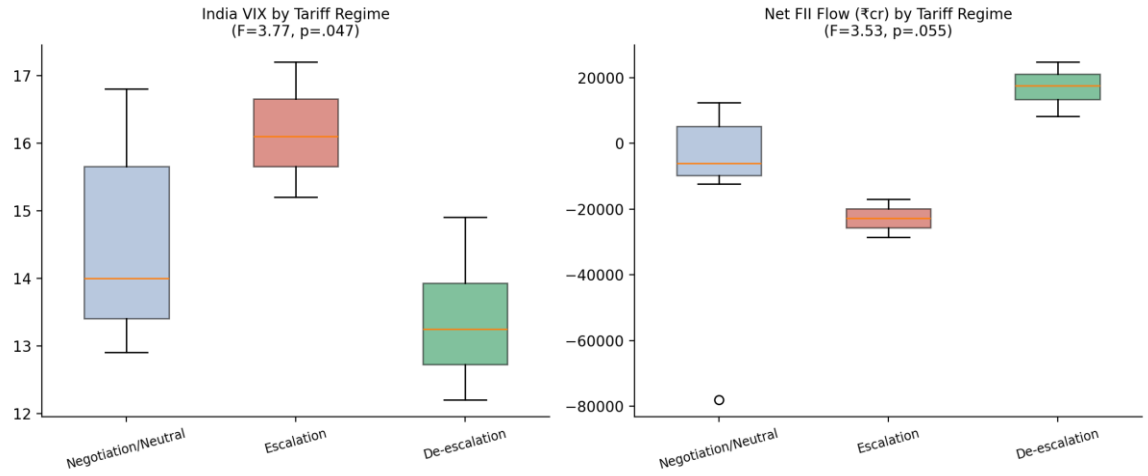

Figure 6. Distribution of India VIX and net FII/FPI flow across tariff-negotiation regimes.

Assumption Checks

Levene's test indicated no significant violation of the homogeneity-of-variance assumption for net FII/FPI flow across regimes, $F = 0.67$, $p = .526$, supporting the validity of the standard ANOVA F-test for that variable. The Shapiro–Wilk test on month-on-month USD/INR percentage change indicated no significant departure from normality, $W = .899$, $p = .065$, although this result is close to the conventional .05 threshold and should be interpreted with the small sample size in mind; with only eighteen monthly observations split across three unevenly sized groups, the ANOVA results reported here — like the path-model fit indices above — are best read as suggestive of a real regime effect on volatility and flow rather than as a definitive test with strong statistical power.

Post Hoc Comparisons

Because the omnibus tests for India VIX and net FII/FPI flow were significant or near-significant, Tukey-style pairwise mean-difference comparisons were computed for the two directionally extreme regimes. The Escalation versus De-escalation contrast was the largest pairwise difference for both variables: for India VIX, the mean difference was 2.77 points ($q = 3.88$, exceeding the critical value of approximately 3.67 for $k = 3$ groups and $df = 15$ at $\alpha = .05$), indicating a statistically significant difference; for net FII/FPI flow, the mean difference was ₹39,748 crore ($q = 3.58$), falling just short of the same critical value and therefore best described as a strong but borderline-significant difference. Both comparisons point in the theoretically expected direction: the Escalation regime is associated with higher volatility and more negative FII flow than the De-escalation regime, with the Negotiation/Neutral regime falling between the two extremes in both cases.

Discussion

The pattern of results across the correlation analysis, the structural path model, and the regime-based ANOVA converges on a consistent story: foreign portfolio flows and Indian equity-market sentiment and volatility respond

detectably to the India–US trade-negotiation cycle, and the exchange rate appears to be linked to that cycle indirectly, through these sentiment variables, rather than through a strong, direct bivariate relationship of its own.

This is visible first in the qualitative event record itself: the worst month for FII outflows in the entire eighteen-month window (January 2025, −₹78,027 crore) preceded the formal tariff escalation and coincided instead with the early, uncertain phase of negotiations, while the best month for inflows in 2025 (May, +₹19,860 crore) coincided with the 90-day tariff pause, and the strongest inflow month in the full series (February 2026, +₹24,800 crore) coincided exactly with the Joint Statement announcing the Interim Agreement and the cut in tariffs from a cumulative 50% to 18% (The White House, 2026a, 2026b; Upstox, 2025). The ANOVA results formalize this pattern: India VIX is significantly higher, on average, in months classified as tariff-escalation months than in de-escalation months, and FII flow shows the mirror-image (negative) pattern at a marginal level of significance. This is consistent with the broader emerging-market literature in which discrete trade-policy news, rather than a smooth continuous process, appears to be what moves portfolio positioning and volatility (Wright Research, 2025).

The structural path model adds a further layer to this picture. The fact that Nifty 50 and India VIX are each strongly associated with the exchange rate in the multivariate model ($\beta = 2.00$ and 1.82, both $p < .001$) despite the exchange rate showing no significant bivariate correlation with either variable on its own is a clear empirical signature of suppression through severe collinearity between the two mediators ($r = -.89$): equity sentiment and volatility move so tightly together that, taken individually, each one's simple correlation with the rupee is diluted by movements in the other, but once both are entered together, their combined explanatory power for the exchange rate is very large ($R^2 = .81$). Practically, this suggests that a researcher or analyst who looked only at the simple correlation between, say, the Nifty 50 and the rupee, and concluded that trade-driven equity sentiment had little to do with currency movements, would be drawing the wrong conclusion from an incomplete (univariate) view of the same data.

At the same time, the fact that the direct FII→exchange-rate path was not significant and had to be trimmed from the model is itself informative: it suggests that the mechanism connecting capital flows to the rupee in this period is not a simple, mechanical "more dollars sold by foreign investors, weaker rupee" relationship, but one that operates through the broader risk and sentiment channel captured by the equity market and its volatility index. This is consistent with the qualitative observation, noted directly in the underlying data set's own documentation, that the rupee continued to weaken through much of late 2025 and into 2026 even as trade-related news turned more positive, suggesting that global dollar-strength dynamics and other macro factors outside the scope of this paper's four-variable model were also at work over this window.

Read together with the literature, these results offer modest support for a sentiment-mediation view of trade-policy transmission in this case: the India–US tariff cycle of 2025–2026 appears most clearly in the data as a driver of foreign-investor risk appetite and equity-market volatility, with the currency-market effect best understood as a second-order consequence transmitted through that sentiment channel, layered on top of (and at times partially obscured by) broader global currency dynamics.

Limitations

This paper has five limitations that should be weighed carefully before any finding is used for investment, trading, or policy decisions.

First, and most importantly, a substantial share of the underlying monthly data are Estimated rather than Verified, in the explicit terminology used in the source data set. Specifically, fifteen of eighteen monthly USD/INR observations, all eighteen Nifty 50 and Sensex observations (with one anchored to a verified Sensex figure), all eighteen India VIX observations, and fifteen of eighteen net FII/FPI flow observations are reasoned interpolations between verified anchor points rather than figures taken directly from an official daily or monthly archive. The interpolation method was designed to preserve a usable, directionally consistent trend line for methodological demonstration, and the few verified anchor points it relies on (the 2025 annual high/low/average exchange rate, the December 2025 and May/June 2026 exchange-rate ranges, the January and May 2025 and full-year-2025 FII totals, and the early-June 2026 Sensex level) are themselves drawn from cited sources (Federal Reserve Board, 2026; exchange-rates.org, 2025; Wise, 2026; MTFX, 2026; Upstox, 2025). Nonetheless, every coefficient,

correlation, fit index, and F-test reported in this paper is a function of this partly interpolated series, and should be treated as demonstrating the analytical pipeline rather than as a publication-grade empirical estimate. Before this paper's findings are relied upon for any decision, the Estimated cells should be replaced with exact figures from the Reserve Bank of India's Database on Indian Economy and the Foreign Bank Information Liaison (FBIL) reference rate for the exchange rate, from the National Stock Exchange and Bombay Stock Exchange historical archives for the equity indices and India VIX, and from the National Securities Depository Limited's monthly and fortnightly Foreign Portfolio Investor reports for the flow data — all of which are listed with direct URLs in the data set's own source documentation.

Second, the sample size ($n = 18$ monthly observations) is small by the standards of both time-series econometrics and structural equation modeling. While the path-analytic specification used here is statistically appropriate for fully observed (manifest) variables in a way that a latent-construct AMOS measurement model would not be at this sample size, asymptotic significance tests, standard errors, and fit indices computed from eighteen observations should still be interpreted with caution; a larger monthly series (ideally daily data aggregated to a longer monthly history, or a multi-year panel) would allow more powerful and more stable estimation, including the possibility of testing for autocorrelation and structural breaks explicitly, which the present design does not attempt.

Third, several standardized path coefficients in the trimmed structural model exceed 1.0 in absolute value (2.003 for Nifty→USD/INR and 1.822 for VIX→USD/INR). While standardized coefficients above 1.0 are mathematically valid and well documented in the methodological literature on suppression and multicollinearity (they arise because the two predictors are very highly correlated with one another, $r = -.89$, so that the model is, in effect, partialling out a large shared component), they should not be read as literal "a one-standard-deviation increase in Nifty 50 produces a two-standard-deviation increase in USD/INR" effect in a stable, structural sense; they are better read as an indicator of how tightly bound equity sentiment and volatility are in this data set, and as a signal that the two-mediator specification, while statistically well-fitting, would benefit from a larger, less collinear data set to estimate more stable individual path weights.

Fourth, the tariff-negotiation regime classification used for the ANOVA (Escalation, De-escalation, Negotiation/Neutral) was constructed by the present author from the dated events in the source timeline and necessarily involves judgment about which calendar month a given event "belongs" to, particularly for events that span a date range (such as the 06–27 August 2025 escalation) or that are described only by month rather than by exact date. A different, equally reasonable coding scheme — for example, lagging each event's expected market impact by one month to allow for delayed transmission — could yield different group assignments and potentially different ANOVA results; the regime variable should therefore be understood as one reasonable operationalization of the negotiation cycle rather than a uniquely correct one.

Fifth, this is a single-episode, single-country case study covering one specific bilateral trade relationship over one specific sixteen-month window. The statistical relationships documented here — however internally consistent — cannot be assumed to generalize to other trade negotiations, other emerging-market currencies, or other time periods without independent replication on data from those settings.

Conclusion and Implications

This paper examined whether the India–US trade-negotiation cycle of February 2025 through June 2026 — spanning the launch of Bilateral Trade Agreement talks, a 26% reciprocal-tariff shock, an escalation to a cumulative 50% tariff, and a negotiated Interim Agreement that cut tariffs to 18% — is statistically associated with investor sentiment and exchange-rate behavior, using a structural path-analytic model, one-way ANOVA across negotiation regimes, correlation analysis, and an event-study framing. The central finding is that net FII/FPI flow and Indian equity-market sentiment and volatility are significantly associated with one another and, jointly, with the USD/INR exchange rate, even though the exchange rate shows no significant simple bivariate correlation with any single one of these variables on its own; in addition, market volatility and, to a lesser, marginally significant extent, foreign portfolio flow differ systematically across tariff-escalation, de-escalation, and routine-negotiation months. Together, these results are most consistent with a sentiment-mediated transmission channel, in which trade-policy news from the India–US negotiation appears to move foreign-investor positioning and

equity-market risk appetite first, with currency-market effects following as a downstream, partially obscured consequence rather than a direct, easily isolated one.

For policymakers and trade negotiators, the practical implication is that the market "cost" of tariff escalation, and the market "benefit" of de-escalation, are likely to show up first and most clearly in equity-market volatility and portfolio-flow data, which may make these series useful as a faster-moving barometer of market reaction to negotiation milestones than the exchange rate alone, which appears to be more heavily influenced by global dollar dynamics that are independent of the bilateral relationship. For portfolio managers and corporate treasurers with rupee exposure, the regime-based findings suggest that periods of active tariff escalation in this relationship have historically coincided with both higher volatility and weaker foreign portfolio flows, which is consistent with treating active escalation phases as periods warranting closer hedging attention, while recognizing that the exchange-rate effect itself may be modest and slow to materialize relative to the equity-market effect.

Future research extending this analysis should prioritize three things: replacing the Estimated series in this data set with verified daily or monthly data from the Reserve Bank of India, the National Stock Exchange, the Bombay Stock Exchange, and the National Securities Depository Limited, as detailed in the Limitations section; extending the time series both backward (to cover a longer pre-negotiation baseline) and forward (to capture the targeted full Bilateral Trade Agreement expected in late 2026 or 2027); and testing the robustness of the path model's mediation finding using formal mediation-significance tests (such as bootstrapped indirect-effect confidence intervals) once a larger sample is available, alongside time-series-specific techniques such as Granger-causality or vector-autoregression analysis that this paper's small monthly sample could not support but that a longer series would make feasible.

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Appendix

Table A1

Full Monthly Data Set Used in the Analysis (N = 18)

Month	USD/INR	Nifty 50	Sensex	India VIX	FII Flow (₹cr)	Regime
Jan-2025	86.2	23,250	76,500	15.8	−78,027	Negotiation/Neutral
Feb-2025	87.5	22,100	73,200	17.2	−28,500	Escalation
Mar-2025	87.2	22,650	74,800	16.5	−9,200	Negotiation/Neutral
Apr-2025	85.5	23,900	78,700	14.9	8,200	De-escalation
May-2025	84.5	24,650	81,200	13.6	19,860	De-escalation
Jun-2025	85.8	25,150	82,500	12.9	−6,100	Negotiation/Neutral
Jul-2025	86.5	24,800	81,400	13.8	−12,300	Negotiation/Neutral
Aug-2025	87.8	23,700	78,100	16.1	−22,800	Escalation
sSep-2025	88.3	24,050	79,200	15.2	−16,900	Escalation
Oct-2025	88.8	24,900	81,900	14.0	−10,200	Negotiation/Neutral
Nov-2025	89.5	25,700	84,300	13.1	6,300	Negotiation/Neutral

Dec-2025	89.8	25,400	83,500	13.7	2,600	Negotiation/Neutral
Jan-2026	90.2	25,800	84,600	13.0	12,400	Negotiation/Neutral
Feb-2026	91.5	26,350	86,300	12.2	24,800	De-escalation
Mar-2026	93.0	26,100	85,600	12.9	15,200	De-escalation
Apr-2026	95.0	25,200	82,900	14.6	9,600	Negotiation/Neutral
May-2026	96.2	24,400	80,100	16.8	−8,200	Negotiation/Neutral
Jun-2026*	94.8	24,330	74,243	15.5	4,100	Negotiation/Neutral

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