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Bank of Baroda

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Economic Round-up: August 2026

Ongoing crisis in West Asia is showing no signs of cooling down. Military strikes between US and Iran continue and have once again engulfed neighbouring Middle Eastern countries in the war. Shipping traffic passing through the Strait of Hormuz is currently at its lowest since May'26. This has also led to international oil prices regaining momentum. They are currently trading near US$ 98/bbl (2nd highest level since end May'26) and have revived concerns regarding global inflation and monetary policy decisions of major central banks. Latest PMI data is also signalling continued pressure on input prices. As a result, this month, both ECB and BoJ are almost certain to hike their policy rates by 25bps. BoE may remain on hold, awaiting more information on second round of inflation impact. Domestically, high frequency indicators are showing that domestic growth fundamentals remain strong. Better than expected GDP growth in Q1FY27 reinforces that belief. In Q2 so far (Jul-Aug), indicators such as GST collections, auto sales, diesel consumption, bank credit growth, all are pointing towards continued momentum. As the festive season approaches, domestic demand will get further boost. However, risks persist. Weak monsoon and pressure on international commodity prices can impact rural demand and inflation. Food inflation also needs to be monitored more closely. We expect rate hike from RBI most likely in Dec'26, unless there is any material change in global situation.

Global central banks: All major central banks in their previous decisions have highlighted that risks to inflation still remain. Even though oil prices had cooled down for a brief period in end Jun-mid-Jul, they have increased considerably since then. With no resolution in sight between US and Iran, central banks are now forced to raise rates to manage inflation expectations before they become entrenched in the system. Investors are therefore almost certain that ECB and BoJ will be hiking their policy rates this month. In case of the US, there is currently a 60% chance of rate hike this month. UK is most likely expected to move in Nov'26, when it has more clarity on inflation trajectory. This month, central banks will also release their revised economic projections. CPI and GDP growth numbers will be critical to watch, for assessing future rate trajectory.

Key macro data releases: GDP growth in Q1FY27 surged to 7.8% from 6.9% in Q1FY26 on a YoY basis. Sharp acceleration was noted in investment spending as it registered a growth of 11.9% against a growth of 5.8% in Q1FY26. **GVA registered** a growth 8.2% in Q1FY27 compared with a growth of 7.0% in Q1FY26. Manufacturing sector continues to shine brightly as it registered a healthy growth of 9.2% in Q1 compared with 8.3%, supported by strong corporate earnings. **Headline CPI** inched up to 4.5% in Jul'26 from 4.4% in Jun'26. This was led by a further acceleration in food inflation. Within food, prices of onion, garlic and ginger showed significant upward momentum. **Core inflation** remained stable at 3.9%, suggesting that price pressure so far have remained contained. India's **balance of payments** registered a deficit (US$ 8.1bn) in Q1FY27 against a surplus noted in Q1FY26 (US$ 4.6bn). The West Asia conflict added to the ongoing challenges, with CAD widening to US$ 4.2bn (0.5% of GDP) against a deficit of US$ 3.4bn (0.4% of GDP). The higher deficit was on account of higher merchandise trade deficit. Goods trade deficit expanded to US$ 86.1bn in Q1 FY27.

Macro developments

Volatility in global financial markets persists

Following the breakdown of ceasefire between US and Iran in early Jul'26, tensions between the two continues persists and has now engulfed the Middle Eastern countries once again in the second phase of the war. In late Aug'26, tensions further heightened, as prospects of a peace deal diminished. Renewed attacks by the US on Iran and retaliatory attacks by Iran on US air bases, has brought back spotlight on Strait of Hormuz. Oil prices averaged US$ 90.9/bbl in the second half of Aug'26 versus US$ 85/bbl in the first half of the month. Currently, it is trading further higher near US$ 98/bbl. This volatility has added significant pressure on global yields. Germany's 10Y yield has risen by 16bps since end Jul'26, for UK it is up by 10bps and for Japan it is up by 10bps. In case of India, it has inched up by 10bps so far. US 10Y yield has seen a movement of 6bps, but more pressure is visible on the shorter end, with 2Y yield rising by 10bps. Equity markets of countries impacted by higher oil prices (UK, Germany, Japan, HK, India) have also fallen since end Jul'26 till now. Strength of US$ has declined between Jul and now, as DXY index has fallen by (-) 1.1%. As a result, other major currencies such as EUR (0.8%), GBP (0.4%), JPY (2.2%), CNY (0.6%) and INR (0.6%) have benefited. INR's appreciation is also linked to domestic factors, such as heavy capital inflows on account of FCNR (B).

State of the global economy

US macro-economic data is pointing towards K-shaped growth trajectory. Second estimates for GDP re-confirmed Q2CY26 growth at 1.5% for Q1 2026, slowing down from 2.1% in Q1. Estimates for private consumption were revised higher to 3.4% (3.2% earlier). Latest indicators for growth in Q3 show that both manufacturing and services sectors are holding ground. ISM manufacturing eased a tad to 54.6 in Aug'26 from 55.6 in Jul'26, led by slight slowdown in both new orders and employment. Price pressure registered acceleration. In Jul'26, factory order growth came in higher at 0.9% (MoM), following (-) 0.2% decline in Jun'26, first monthly increase since Apr'26. Orders excluding transportation rose by 0.6%, after registering (-) 0.1% decline in Jun'26. Durable good orders rose by 1.1% in Jul'26 (0.6% in Jun'26), supported by rebound in transportation equipment, machinery, and furniture products. Non-durable good orders were up by 0.7% (-0.9% in Jun'26), driven by petroleum & coal products, textiles, and chemicals. In case of services, the ISM index rose to 55.4 from 54.1 in Jul'26, supported by uptick in new orders. Employment continued to decelerate and price pressures were visible in this sector as well. CPI for Jul'26 remained broadly sticky at 3.4% versus 3.5% in the previous month. Given sticky inflation, and downside risks to employment, University of Michigan's consumer sentiment index for Aug'26 also slipped to 51.7 from 55.2 in Jul'26. Both current situation (51.9 versus 54.8) and expectations (51.5 versus 55.4) index fell. On the brighter side, 1yr-ahead inflation expectation moderated to 4% from 4.2% earlier but remains much higher than what it was before the outbreak of Iran war (3.4%). On the labour market front, initial jobless claims for the week ending 3 Sep 2026 rose marginally to 206k, from 204k in the previous week. Continuing claims (4-week moving average) also eased a tad to 1.78mn from 1.79mn previously. Non-farm payroll data shows 162k additions to job market (est.: +55k), following upwardly revised number of 21k in Jul'26. 80% of these additions were driven by leisure and hospitality (62k) and local government education (42k).

In case of **Eurozone,** final estimate for Q2CY26 GDP growth in Germany was revised upwards to 0.3% (QoQ) from 0.2% earlier and is broadly stable compared with 0.4% growth in Q1. The resilience was mostly on account of external trade. Goods exports rose by 2.6%, and imports were up by 2.1%. Private consumption remained subdued, rising by 0.1%. GFCF on the other hand fell by (-) 0.2%, dragged by capital formation in machinery & equipment (-1.4%). Despite continued tensions in the Middle East and declining water levels in the Rhine River, analysts remain optimistic about growth in CY26. This mood is also reflected in the IFO index, which has risen to 88.8 in Aug’26 from 86.7 in Jul’26, led by sharper improvement in expectations index (89.1 versus 86.8) compared with current assessment index (88.5 versus 86.5). participants expect growth to get a boost from government’s infrastructure spending, climate neutrality and defence. Industrial production and exports will continue to strengthen on the back of robust global demand. Accounting for all these push factors, Germany’s GDP growth estimated at 1.4% by the IFO institute. However, price pressures in Europe remain amidst the ongoing West Asia crisis. Eurozone inflation accelerated to 3.3% in Aug’26 from 2.9% in Jul’26. This has impacted service sector performance. Markit services PMI index for Aug’26 eased a tad t0 51.6 from 51.7 in Jul’26. Manufacturing sector’s performance on the other hand improved, with PMI index rising to 52.7 (more than 4 year high) from 51.9 in Jul’26, supported by pickup in activity in Germany and France.

In China, the official manufacturing PMI shows that activity continued to contract for the second consecutive month in Aug’26, albeit at a slower pace. PMI index rose slightly to 49.8 (est.: 49.5) from 49.2 in Jul’26, helped by pickup in new orders index (including export orders) and supplier delivery time index. Employment index fell further, while price index accelerated. Non-manufacturing PMI remained unchanged from last month at 49.0 The sub-index shows that new orders and employment continue to weaken, while price pressures were elevated. Even in Jul’26, industrial production had slowed, to 4.5% (est.: 5%) from 5.3% in Jun’26. Major drag came from mining sector (-4.2% in Jul’26 versus -2.2% in Jun’26). Manufacturing sector growth eased to 5.5% from 6% in the previous month, even as hi-tech manufacturing rose a faster pace (16.9% versus 14.1%). Retail sales also moderated to 0.6% (est.: 1.5%), from 1% in the previous month, signally weakness in domestic demand. This could have been aggravated due to seasonal factors (3 Typhoons in Jul’26). Investment growth contracted further as FAI was down by (-) 6.7% between Jan-Jul’26 (est.: -6.2%), after declining by (-) 5.7% H1CY26. Industrial profits too slowed, to 11.2% in Jul’26 (weakest level in CY26) from 15.1% in Jun’26. However, this year profits have been much better than last year (single digit growth), largely due to AI boom. Computing and storage chip manufacturers have registered 18.5% rise in profits (Jan-Jul’26), driving substantial profit growth in the electronics sector. Going ahead, pressure on government remains to provide fiscal stimulus to revive investment and domestic consumption growth.

Indian economy: High frequency indicators signal resilience

India’s manufacturing PMI eased to 5-year low of 52.8 in Aug’26 from 53.5 in Jul’26, dragged by softer demand, reflected in limited rise in new orders. As a result, employment index declined, for the first time in 2.5 years. Inventories inched up, given subdued sales. Participants noted continued to rise in input price pressures even as inflation index moderated to its lowest in 6 months. In contrast, India’s services PMI showed improvement, rising to 54.1 in Aug’26 from 53.3 in Jul’26, although the index is still at second lowest level since Mar’22. Pickup Aug’26 was led by rise in new orders, particularly new export orders from Australia, Brazil, Canada, Japan, Malaysia, Singapore, Sri Lanka and the UAE. As a result, job creation rose to 15-month high. Further, input prices continued to remain elevated and as a result, output prices too inched up. Other high frequency indicators are signalling pickup in activity in Q2FY27 so far (Jul-Aug). Indicators like GST collections, vehicle registrations, port cargo traffic, auto sales, bank credit, diesel consumption has improved compared with Q1. However, air passenger traffic is still reeling under pressure from rising oil prices. From mid-Aug’26 till now, oil prices have picked up pace again and will therefore also have a spillover effect on other components of services sector—trade, hotels, restaurant, and transportation services.

Monsoon: Southwest monsoon on a cumulative basis was under normal category with rainfall at 13% below LPA till 4 Sep 2026. This has resulted in lower sown area of kharif crops, which is drawing to a close soon. Rice and coarse cereals have registered lower acreage, while pulses sowing has improved. Out of 36, 17 sub-divisions (49% of the country) have received normal to excess rainfall during this period, while 16 states are in the deficient zone. Region-wise, a deviation has been noted across all the regions. Southern Peninsula reported deficient rainfall (-26%), followed by East and Northeastern India (-24%) while Northwestern (-9%) and central region (-5%) have reported normal rainfall. Moderate El Nino conditions are currently prevailing as per the IMD and are projected to strengthen in the remaining period of the season. As we head towards the last leg of the monsoon, the focus would be on spatial distribution which could have an impact on final kharif acreage and food inflation in the near term.

RBI on a temporary pause

The MPC unanimously decided to keep its policy rates on hold in Aug'26 meeting. Stance of the monetary policy was also retained at neutral, as it will allow the central bank to act as per evolving global situation. Noting strong domestic fundamentals and resilience in growth (as visible in high frequency indicators) despite global external shocks, RBI revised FY27 growth projection upward by 10bps to 6.7%. Further, given that Q1FY27 inflation was 30bps lower than anticipated, and that inflationary pressures are still not broad-based, the central bank also revised its inflation projection 10bps lower to 5% for FY27. Revisions to both growth and inflation have been primarily in H1FY27. Inflation is still expected to peak at 5.9% in Q3FY27, before easing in Q4 and Q1FY28. However, in these 3 quarters, if policy rate remains unchanged at 5.25%, then we are looking at negative real interest rates. We also believe that upside risks to inflation persist as monsoon remains in deficit so far and kharif sowing is currently lower than last year. Uncertainty around global oil and other commodity prices is also prevailing. Given these factors, we continue to expect at least 1 rate hike by the central bank in FY27, most likely in Dec'26, when there is more clarity available on growth, impact of El-Nino, and geopolitical tensions in West Asia.

Global central bank actions

US Fed in its Jul'26 meeting kept the policy rate unchanged at 3.5-3.75% with 9-3 vote. Three members who dissented voted for rates to be increased by 25bps. In the statement, the committee reiterated that "economic activity is expanding at a solid pace despite elevated uncertainty…productivity growth and capital investment are strong. Job gains have kept pace with the workforce…Inflation remains elevated in part reflecting supply shocks that have driven price increases in certain sectors, including energy". Minutes of the meeting reveal that "many participants assessed that policy tightening would likely be necessary if inflation did not decline. Some participants commented that financial conditions might not currently be sufficiently restrictive to facilitate a return of inflation to 2%. This has raised probability of a rate hike by Fed in Sep'26. A per CME Fedwatch tool, there are 60% chances that Fed will hike rates by 25bps in its Sep'26 meeting, as inflation remains sticky at 3.4% in Jul'26 (3.5% in Jun'26).

Bank of England (BoE) had held its policy rate steady at 3.75% in its Jul'26 meeting. Members cautioned that "(inflation) is expected to rise later this year as the effects of higher energy prices continue to pass through. The risk of material second-round effects in price and wage-setting, against which policy needs to lean, is greater the longer higher energy prices persist". They also added that "because the outlook is uncertain, the MPC needs to consider a range of possible outcomes and balance the costs of leaning too little against potential inflationary pressures and the costs of responding too much". Given that inflation began regaining momentum in Jul'26 as it rose by 2.9% from 2.6% in Jun'26, pressure on BoE has increased to raise rates. However, investors are still pricing in 15% chance of rate hike in Sep'26 and 70% chance in Nov'26, when there is more clarity on inflation trend amidst ongoing geopolitical uncertainty and stubborn oil prices.

The ECB kept its policy rate unchanged in its Jul’26 meeting, after raising rates for the first time in 3 years in Jun’26, considering that the “outlook for energy prices, while highly volatile, currently stands close to the baseline of the June Eurosystem staff projections and well above the levels recorded prior to the conflict in the Middle East”. However, minutes of the meeting revealed that members mostly agreed that they will have raise rates once more to contain the impact rising energy prices and its second-round effects. Data already shows visible impact on inflation as CPI rose by 3.3% in Aug’26 from 2.9% in Jul’26. As a result, investors are now pricing in 100% probability of a rate hike by ECB in its meeting tomorrow. Post that, ECB is expected to remain on pause for some time. If necessary, rates will be increased again in Dec’26 or otherwise next year. In the Sep’26 meeting, updated economic forecasts will also be made available, where slight upward revision to GDP number is expected.

Bank of Japan held rates steady in its Jul’26 meeting at 1%, passing the decision with 8-1 majority. One member who dissented, voted for immediate 25bps rate hike. In the summary of opinions, the central bank’s statement was more hawkish than expected as it focused pressures faced by inflation. Members noted that “underlying CPI inflation is likely to increase gradually, as the mechanism in which wages and prices rise moderately in interaction with each other is expected to be maintained…For prices, the situation in the Middle East, the expansion in AI-related demand, and the depreciation of the yen all exert upward pressure. Given factors such as the rise in domestic distribution costs and the increase in the prices of packaging materials and food trays, the price hikes in final consumer goods are expected to accelerate again toward early autumn”. It was also added that “considering factors such as the future pass-through of higher crude oil prices to consumer prices, and Japan's output gap, which indicates supply shortages and excess demand, risks to prices are significantly skewed to the upside…(and) given that underlying CPI inflation has been approaching 2% and financial conditions have been accommodative, it is appropriate for the Bank to continue to raise the policy interest rate and adjust the degree of monetary accommodation”. Following this, rate hike in Sep’26 policy meeting is now almost certain. More recently, Takuji Aida—economic advisor to the PM has indicated that BoJ is likely to hike rates in Sep’26 and Jan’27, following which rate hikes may be more gradual (once in 6 months).

Indian Economy (For detailed reports refer to https://bankofbaroda.bank.in/economic-scenario)

Corporate results Q1 FY27

India Inc.'s registered a resilient corporate performance in Q1 FY27. For a sample of 2,623 companies, net sales rose at a solid pace of 17.1% compared with a growth of 4.6% in Q1 FY26. Profit too improved to 12.5% this year, compared with 10% growth in the same period last year. Within this, the BFSI segment recorded stable growth in net sales, even as profit growth was significantly higher. Excluding the BFSI sector, while growth in sales shows a significant uptick to 20.5% in Q1 FY27 compared with just 3.3% in Q1 FY26, there is a sharp deceleration in profits. However, this deceleration can be largely traced back to a sharp decline in profits in the petroleum sector due to the increase in global oil prices. In fact, if we remove both BFSI and petroleum sector from the aggregate sample, the results show a marked improvement in financial performance. Net sales for the sample increased sharply from 5% in Q1 FY26 to 17.5% in Q1 FY27. Profit growth is also much higher at 23.7% in Q1 this year, compared with 7.3% in Q1 FY26.

Evolution of India's yield curve post government policy support

India's yield curve has exhibited considerable volatility this year. Both global and domestic factors resulted in the same. Most importantly, the debt outflow arising from global policy uncertainty further worsened the situation. The gap between India and US 10Y yield is at multi year low level and far below long run average. This may have further aggravated the FPI-debt outflow. Government policy measure to attract durable capital flows came at a very opportune time. The policy response was felt across the entire yield curve. The inclusion of new issuances for 15Y, 30Y and 40Y paper in the FAR route has resulted in significant downward correction in yields across these tenors. If we see the net market activity report of G-sec category-wise, there is a clear shift in pattern where foreign banks are gaining momentum post policy support to FPIs.

The short end part of the yield curve has also declined sharply. This may be on account of system liquidity remaining comfortably above the 1% NDTL level. Going forward, we expect steepness in India's yield curve as long end part of the curve might exhibit some upward bias anticipating rate action from RBI and tracking the war situation between US and Iran. Short end yields are expected to get some support from adequate system liquidity conditions post FCNR (B) deposit flows.

RBI dollar measures: Progress and impact

The US-Iran war created significant challenges for the Indian economy, as rising oil prices and persistent FPI outflows led to concerns over external stability given India's high dependence on imported oil. Fiscal concerns too emerged as expectations of government support increased. Hence, the narrative of "twin deficit" gained steam which led to considerable volatility in the domestic financial markets. To address the external challenges and strengthening its buffers, the government and the RBI announced a slew of measures to attract dollar inflows. While the government measures were more structural in nature and addressed longstanding issues with regard taxation of FPI's investment in India, RBI's measures aimed at providing incentives for attracting durable dollar liquidity in the system. RBI's measures to attract foreign inflows have been a resounding success with total inflows mobilized far exceeding the expected target. This will bolster India's external buffers, at a time of heightened external volatility. Despite the war related shocks, India's internal and external metrics have done well. GDP growth remained buoyant, and CAD remained in a comfortable range. The outlook too is promising as even though there is still uncertainty over the situation in the Middle East, India now is insulated to withstand any unfavourable external shock. We expect CAD at 1-1.25% of GDP, given the recent strength seen in services exports and remittances. At the same time, higher foreign inflows through the RBI measures would supplement the capital account surplus. We expect a BoP surplus of US$ 65-75bn in FY27. This will further strengthen India's forex reserves which currently stand at a record high.

How have freight rates moved?

In the event of ongoing war between US and Iran, oil prices and other global commodity prices have come under significant pressures in the last few months. As a result of volatile oil prices, and tensions in key shipping routes, freight rates have also been impacted. We have analysed data on how shipping freight rates, truck freight rates and air cargo volumes have performed since the outbreak of US-Iran war (Feb-Jul'26). We note that the freight rates for bulk dry carriers have increased more significantly than those for oil transporting carriers. Largest oil carrier (VLCC) has even seen decline in rates. This is driven mainly by tensions in the Middle East and attack on infrastructure of major oil producing countries, which has led to dip in demand for these carriers. Other smaller carriers (Suezmax and Aframax) have registered increase in freight rates. Domestically, truck freight rates have also increased since Feb'26. In case of air cargo volumes, domestic cargo is once again taking lead in driving the cargo volumes since Mar'26, as international airline routes have been curtailed. Due to higher ATF prices, domestic ATF consumption has also taken a hit. In the near-term, given continued tensions between US and Iran, volatility in oil prices is expected to remain, which in turn will impact freight prices and prices of other commodities as well.

State of capacity utilization

Capacity utilization is an important indicator of how output fares relative to the fixed assets in a company. This also gives a clue about potential future investment as companies which have surplus capacity are unlikely to invest unless they see demand rising at a quick pace. Data on capacity utilization, however, is limited and while RBI provides the same based on surveys on a quarterly basis, the same is not available for industries. A proxy indicator that can be used is the asset turnover ratio defined as ratio of sales to fixed assets. The patterns of movement in gross sales to gross fixed asset ratio is interesting as it varies across industries. There are some early signs of which industries could possibly be going in for higher investments based on the asset turnover ratio, which is broadly interpreted as capacity utilization rate. While those with higher ratios would be logically potential investors, those with declining ratios may not necessarily not be investing in future. It would depend on past investment patterns as well as the requirement of going in for product diversification.

There are certain industries that have witnessed improvement in sales to GFA ratio in FY26 after declining in FY25. In case of automobiles there was low demand in entry level segment which was compensated for by premium segment vehicles that boosted sales and hence production. For the IT sector the big push being given to Data Centres and AI is calling for higher investment, which is also reflected in the rising ratio. This is the future of investment in this sector. For chemicals and non-ferrous metals, it is a major push given to infrastructure which has led to improvement in ratios that could presage higher investment in the coming years. Diamonds and jewellery have been a volatile sector as the production is linked to exports too which has been buffeted by various factors. The encouraging part is notwithstanding the tariff issue last year, there has been a smart increase in output which can be translated to higher future investment depending, however, largely on how the export market fares.

Sectoral deployment of credit: Banks versus NBFCs

NBFC and Bank's overall credit picture shows that outstanding Bank credit as of Jul'26 is 3.7 times that of NBFC credit. The growth rate of Bank credit is also happening at a much steeper pace compared to NBFC credit offtake. However, sectoral picture gives some interesting insights. In terms of share, Banks are maintaining a well-diversified portfolio with share of retail loans, services and industry capturing the space. For NBFCs, the share is skewed towards retail loans especially vehicle loan space and infrastructure space. It is to be mentioned that Banks are also regaining their momentum in the infrastructure segment as can be seen from their rising share in incremental credit in the current fiscal. For some sectors such as commercial real estate and loan against gold jewellery, credit accretion in the current fiscal is happening at a faster pace for Banks.

GDP expand by 7.8% in Q1FY27

GDP growth in Q1FY27 surged to 7.8% from 6.9% in Q1FY26 on a YoY basis. This was higher than our expectation of 7.2%. Sharp acceleration was noted in investment spending as it registered a growth of 11.9% against a growth of 5.8% in the previous year of the same quarter. Additionally, strength was also noted in the consumer spending in Q1 as it clocked a growth of 7.1% against 6.8% in the Q1FY26. Exports registered growth as it expanded by double digit to 12% in Q1FY26 (6% earlier). Growth in government spending was tad lower at 4.3% against 4.5% growth last year. Some weakness was noted in imports with growth declining by (-) 1.1% against an expansion of 5.3% in Q1FY26.

GVA registered a growth 8.2% in Q1FY27 compared with a growth of 7.0% in Q1FY26. Strong growth was noted across a range of sectors. Manufacturing sector continue to shine brightly as it registered a healthy growth of 9.2% in Q1 compared with 8.3% in the same quarter of last year supported by strong corporate earnings. Electricity growth sprinted ahead with a growth of 8.9% after declining by (-) 1.8% in Q1FY26. Construction sector too strengthened with a growth of 7.7% against 5.2% growth in Q1FY26. Services sector rose led by expansion in financial services (12.1% from 8.8%) and public admin (7.5% from 4.6%) sector. Though, trade, hospital, transport registered marginally slower growth at 8.5% in Q1FY27 (from 9.8%). In contrast, tepid growth was noted for mining sector as it registered a contraction at (-) 2.4% after expanding by 12.4% in Q1FY26. Furthermore, sluggish pace of growth was noted in agriculture sector at 3.6% from 4.4% in Q1FY26 given aggravated heatwave conditions and delayed arrival of South-West monsoon

CPI inches up again

Headline CPI inched up to 4.5% in Jul'26 from 4.4% in Jun'26. This was led by a further acceleration in food inflation. Within food, prices of onion, garlic and ginger showed significant upward momentum. Core inflation remained stable at 3.9%, suggesting that price pressure so far have remained contained. Going ahead, the outlook on food inflation remains dependent on the rainfall activity. South-West monsoon has remained erratic, even as rainfall activity has picked up pace. The distribution of rainfall too has been uneven. This will have a bearing on food inflation outlook. As per latest available data, kharif sowing is 1.8% lower than last year. However, sowing of key crops such as rice and pulses has been much lower, which will need to be monitored going ahead. Core inflation has continued to be sticky but can inch up due to second-round effects and continued uncertainty over the war situation. We expect CPI inflation to average about 5-5.2% in FY27. This will however hinge on the evolving El-Nino conditions.

Industrial production remains at a healthy level

Industrial production registered a growth of 6.7% in Jul'26 against 5.4% growth in Jul'25. Compared with previous year (Jul'25), higher growth was noted primarily in manufacturing and electricity generation. Mining growth declined, while growth in output of water supply, and sewage management remained broadly steady. Manufacturing growth came in at 7.3%, supported by manufacture of wearing apparels, chemicals, computer and electronics, electrical equipment, motor vehicles, and other transport equipment. Output of capital goods, intermediate goods, and consumer durables also improved notably in Jul'26 compared with last year. Heatwave conditions have support demand for consumer durables so far. Going forward, as tensions between US and Iran remain escalated, and key shipping routes are still under threat, global commodity prices are volatile. Limited pass-through in output prices implies that margins can expected to remain under pressure for some more time, until shipping activity normalises. Hence, we maintain cautious view on our full year IIP growth forecast. However, domestic measures to boost manufacturing and limited impact of erratic monsoon on consumer demand, will help support growth.

India's CAD widens in Q1

Industrial production registered a growth of 6.7% in Jul'26 against 5.4% growth in Jul'25. Compared with previous year (Jul'25), higher growth was noted primarily in manufacturing and electricity generation. Mining growth declined, while growth in output of water supply, and sewage management remained broadly steady. Manufacturing growth came in at 7.3%, supported by manufacture of wearing apparels, chemicals, computer and electronics, electrical equipment, motor vehicles, and other transport equipment. Output of capital goods, intermediate goods, and consumer durables also improved notably in Jul'26 compared with last year. Heatwave conditions have support demand for consumer durables so far. Going forward, as tensions between US and Iran remain escalated, and key shipping routes are still under threat, global commodity prices are volatile. Limited pass-through in output prices implies that margins can expected to remain under pressure for some more time, until shipping activity normalises. Hence, we maintain cautious view on our full year IIP growth forecast. However, domestic measures to boost manufacturing and limited impact of erratic monsoon on consumer demand, will help support growth

India's balance of payments registered a deficit in Q1FY27 against a surplus noted in Q1FY26. The West Asia conflict added to the ongoing challenges, with CAD widening to US$ 4.2bn against a deficit of US$ 3.4bn for the same period of last year. Capital account registered net outflow for the 3rd straight quarter led by portfolio outflows. Even NRI deposit and ECBs were lower in this quarter compared with Q1FY26. Going ahead, external account may continue to witness headwinds on account of the geopolitical conflict and CAD can widen given the pressure on elevated oil prices and possible moderation in remittances. We expect CAD at 1-1.25% of GDP in FY27. However, recent measures by RBI through FCNR and ECBs have already pushed forex in a large surplus mode and will be positive for capital account and rupee this year.

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