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India's CAD comfortable; risks remain

India's balance of payments situation remained comfortable in FY26. While external headwinds impacted growth in merchandise exports, import growth was resilient. Oil imports were lower largely due to lower prices, on the other hand, gold imports surged due to elevated prices. Services and remittances receipts offered support, thus keeping CAD largely in check. Capital account surplus moderated in the year, led by FPI outflows, even as FDI inflows recovered. Going ahead, pressure on CAD is likely due to higher oil prices, lower merchandise exports, and moderation in remittances. Services exports are expected to be steady. Our estimate for CAD stands at 1.8-2.2% of GDP in FY27. More importantly, recent measures by the RBI would lead to greater inflows, which would offset the shortfall in the current account. Thus, we can expect India's overall BoP to record a positive balance in FY27. This should offer some support to INR.

India's BoP in Q4 FY26

India's current account recorded a surplus of US$ 7bn (0.7% of GDP) in Q4 FY26. This was lower than a surplus of US$ 13.7bn (1.4% of GDP) in the same period last year.

- The lower surplus was on account of higher merchandise trade deficit. Goods trade deficit expanded to US$ 83.4bn in Q4 FY26 versus US$ 59.3bn in Q4 FY 25. This reflects a marginal decline in exports (-2.8% YoY) and a sharp acceleration in imports (up by 11.8% YoY). Within imports, while oil imports declined, non-oil imports increased. Incidentally, gold imports jumped by over 137% in Q4 FY26. This can be attributed to an increase in gold prices which noted an increase of over 70% in Q4 FY26 on a YoY basis.
- Other components of current account offered support. India's net services receipts increased to US$ 60.4bn in Q4 this year, compared with US$ 53.3bn in the same period last year. Within services, while software net services receipts continued to grow at a steady pace, traction was also noted in travel and insurance services.
- Apart from this, services related to professional and management consulting too have seen greater momentum.
- Net transfers increased by 9.7% to US$ 41.2bn in Q4 FY26. This was led by a 28.2% increase in inward remittances.
- Outgo on account of interest income moderated marginally to US$ 11.1bn in Q4 FY26 compared with US$ 11.9bn in the same period last year.

In the capital account, support came from an increase in FDI inflows.

- Compared with inflows of US$ 0.4bn in Q4 FY25, FDI inflows increased to US$ 4.2 bn in Q4 FY26. However, FPI outflows almost doubled to US$ 12bn this year versus US$ 5.9bn in the same period last year, bringing the capital account surplus lower.
- Further, while NRI deposits improved, net inflows under ECB route were lower.
- Hence, deficit on account of capital account moderated to US$ 1.1bn in Q4 FY26, versus US$ 5.6bn in the same period last year.

Overall, India's balance of payments recorded net accretion of US$ 7.2bn in Q4 FY26 versus an accretion of US$ 8.8bn in Q4 FY25.

<u>India's BoP in FY26</u>

- India's current account deficit (CAD) as a % of GDP remained steady at 0.6% in FY26. In absolute terms, there was a marginal increase in CAD to US$ 25.4bn in FY26 versus US$ 23.1bn in FY25.
- Merchandise trade deficit rose by US$ 50bn to US$ 337.3bn (8.6% of GDP). Growth in merchandise imports accelerated, even as goods exports remained muted amidst external headwinds.
- Net services increased at a growth rate of 18.2%, rising to US$ 216.6bn.
- Net transfer receipts increased to US$ 143.5bn in FY26 from US$ 123.4bn in FY25. Within this, inward remittances rose to US$ 151.7bn in FY26 (US$ 132.1bn in FY25). On the other hand, net outgo on the primary income account was steady at ~US$ 48bn.
- India's capital account surplus narrowed sharply in FY26, primarily due to FPI outflows. While FPIs recorded net inflows of US$ 3.6bn in FY25, FPI outflows in FY26 rose to US$ 16.4bn.
- NRI deposits too were marginally lower at US$ 14.4bn compared with US$ 16.2bn in FY25. Similarly, ECB inflows too witnessed some moderation.

India's BoP recorded a depletion of US$ 23.6bn in FY26, largely due to a lower capital account surplus.

<u>Outlook for FY27</u>

The global trading environment has changed markedly in FY27. The continuation of geo-political tension in the Middle East and the resulting supply chain issues can have a negative impact on India's external position. Global oil prices have continued to remain elevated, even though the current trading range is below US$ 100/bbl. Oil imports accounted for about 22% of India's total imports in FY26, while oil deficit accounted for about 36% of total merchandise trade deficit. Hence, higher oil prices can inflate the import bill and trade deficit. At the same time, growth in merchandise export will be under pressure due to weak external demand. Further, about 14% of India's total exports to the West Asia are also directly at risk. Hence, we can expect the merchandise trade deficit to widen.

Services exports have continued to grow at a healthy pace, and commentaries by major tech companies suggest healthy demand in key markets, driven by need for AI related infrastructure development. However, there will be some pressure on inward remittances as despite diversification, a large part of India's remittances still originate from the Gulf countries. Given the ongoing conflict and reports of losses in oil infrastructure, workers' incomes can get impacted, leading to lower remittances.

Overall, we expect India's CAD to expand to 1.8-2.2% of the GDP in FY27.

The impact on foreign exchange reserves is unlikely to be much as the government has taken several measures to improve capital inflows such as relaxation in norms for foreign investments in government debt securities, concessional forex swap facilities for ECBs and covering hedging costs on 3-5 year FCNR (B) deposits etc..,. This should help ease some pressure on the INR at the margin as a large part decline in INR was driven by weakness in foreign inflows.

We can expect INR to trade with an appreciating bias in the short-term with a trading range of 95-96/$. Over the medium term, worsening fundamentals and pressure on twin deficits can lead to renewed pressure on the currency pushing it towards the 96-98/$ range.

Table 1: India balance of payments snapshot

(US$ bn)	Q4FY25	Q4FY26	FY25	FY26
Current account	**13.6**	**7.0**	**-23.1**	**-25.4**
CA/GDP (%)	**1.4**	**0.7**	**-0.6**	**-0.6**
Trade balance	-59.3	-83.4	-286.9	-337.3
- Merchandise exports	116.4	113.3	442.1	446.1
- Merchandise imports	175.8	196.6	729	783.4
Net Services	53.3	60.4	188.8	216.6
Transfers	31.5	41.2	123.4	143.5
Other invisibles	-11.9	-11.1	-48.3	-48.2
Capital account	**-5.6**	**-1.1**	**16.7**	**2.0**
% of GDP	**-0.6**	**-0.1**	**2.3**	**0.3**
Foreign investments	-5.5	-7.8	4.5	-9.4
- FDI	0.4	4.2	1.0	6.9
- FII	-5.9	-12	3.6	-16.4
Banking capital	-9.0	5.4	-9.8	6.4
Short-term credit	-4.4	-3.4	7.2	13.7
ECBs	8.0	2.5	15.9	11.1
External assistance	2.1	1.6	6.3	2.6
Other capital account items	3.2	0.7	-7.4	-22.5
E&O	0.8	1.3	1.4	-0.1
Overall balance	**8.8**	**7.2**	**-5.0**	**-23.6**

Source: CEIC, Bank of Baroda Research

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