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ECONOMY OBSERVER

Q3 2026

Overall Macroeconomic Context

India approaches Q3 FY2026-27 from a position of relative macroeconomic resilience, despite a more challenging external environment characterised by geopolitical tensions, volatile commodity prices and uneven monsoon conditions. The latest GDP release points to a firm start to the fiscal year, with real GDP expanding by 7.8% in Q1 FY2026-27, compared with 6.9% in Q1 FY2025-26, while nominal GDP growth stood at 10.3%. The upturn was supported by stronger production-side activity, investment momentum and resilient services-sector performance, even as the RBI's FY2026-27 growth projection of 6.7% implies some moderation over the rest of the year.

Economic activity during Q1 FY2026-27 was firmly investment-led, with Gross Fixed Capital Formation growing by 11.9% at constant prices, nearly double the 5.8% growth recorded in Q1 FY2025-26. Industrial production accelerated from 4.9% in Apr 2026 to 7.3% in Jun 2026, supported by manufacturing and capital goods, while construction and services activity also remained strong. High-frequency indicators continued to point to resilient domestic demand, with GST collections, digital payments and electricity consumption holding up, and labour market conditions remaining broadly stable as the unemployment rate eased to 5.1% in Jul 2026.

The inflation environment became less benign during the quarter. Headline CPI inflation rose from 3.9% in May to 4.4% in Jul 2026, moving above the RBI's 4% target for the first time in over a year, largely driven by food-price pressures. Wholesale inflation remained elevated at around 9.8%, reflecting higher food, raw-material and industrial input costs, even as fuel-related pressures moderated. Uneven rainfall patterns and evolving El Niño conditions have also increased uncertainty around the food inflation outlook heading into the second half of the fiscal year.

The external sector remained resilient but increasingly exposed to global developments. Merchandise exports recorded strong growth during Apr-Jul 2026-27, supported by petroleum products, electronics, engineering goods and chemicals. However, imports continued to expand at a faster pace, driven by petroleum, electronics and other intermediate goods, resulting in a wider trade deficit. Continued disruptions arising from the West Asia conflict, elevated freight costs and volatility in global commodity markets remain key risks for the external sector.

India's macroeconomic fundamentals nevertheless continue to provide an important buffer against external shocks. Foreign exchange reserves remained sizeable at around USD 692 bn in Jul 2026, while strong services exports and remittance inflows continued to support external stability. Going into Q3 FY2026-27, the key macroeconomic risks are likely to arise from food inflation, adverse monsoon outcomes, elevated energy prices and persistent geopolitical uncertainty. However, strong domestic demand, sustained public capital expenditure and healthy balance-sheet conditions should continue to support economic growth.

Parameters (MoM % change)	Dec-25	Jan-26	Feb-26	Mar-26	Apr-26	May-26	Jun-26	Jul-26	Aug-26
AGGREGATE DEMAND									
Consumption of Petroleum Products (Volume)	3.9	-4.6	-2.0	5.8	-11.5	3.5	-1.2	3.0	
Electricity Demand	11.4	3.2	-6.8	12.3	3.9	6.5	0.9	2.2	
Toll Collection via FASTag (Volume)	5.4	-0.2	-6.5	4.2	0.4	6.2	-2.8	-5.6	1.0
GST Revenue	-1.3	6.2	8.1	8.8	8.7	3.2	13.9	15.4	7.3
E-Way Bill Generated	6.5	-1.1	-3.1	6.0	-5.1	2.5	0.0	2.2	-0.5
UPI Transactions	5.7	0.3	-6.0	11.0	-1.3	3.8	-2.1	4.1	3.6
AUTOMOBILE SECTOR									
Passenger Vehicle Sales	-4.8	9.0	-5.5	5.6	-2.1	2.3	-11.7	15.5	
Tractor Sales	-21.9	22.6	-9.4	27.0	2.0	3.2	14.8	-36.6	
Two-wheeler Sales	-16.8	18.5	-0.8	1.7	-1.0	0.9	-0.3	3.5	
Three-wheeler Sales	-14.0	10.9	0.7	1.0	1.6	2.5	9.0	11.5	
EMPLOYMENT									
Unemployment rate (PLFS: All-India)	4.8	5	4.9	5.1	5.2	5.5	5.5	5.1	
Unemployment rate (PLFS: Urban)	6.7	7	6.6	6.8	6.6	6.4	6.6	6.7	
Unemployment rate (PLFS: Rural)	3.9	4.2	4.2	4.3	4.6	5.1	5	4.5	
Naukri JobSpeak Index	0.0	-12.1	22.6	-11.6	6.5	-6.9	6.7	6.6	-6.2
INDUSTRY									
PMI Manufacturing	-2.8	0.7	2.7	-5.3	1.5	0.5	-1.5	-1.3	-1.3
IIP-General	7.8	-0.4	-4.2	10.0	-8.9	3.6	1.9	0.0	
IIP-Capital goods	10.6	-5.1	7.6	23.0	-29.3	10.9	4.8	-2.2	
Index of Core Industries	9.1	2.1	-8.0	10.8	-7.7	4.2	0.5	0.4	
Index of Service Production									
Wholesale Trade	8.8	12.4	-8.0	7.5	-15.6	-1.6	4.1		
Retail Trade	13.4	4.8	-4.6	12.0	-11.5	0.4	-0.1		
Repair & Maintenance	6.4	10.3	-18.2	70.4	-36.0	2.1	-1.9		
Accommodation & Food	12.6	-10.0	-1.1	-0.1	-6.9	7.8	-5.2		
Rail Transport	4.8	1.7	-7.1	12.5	-11.4	7.7	-1.7		

Parameters (MoM % change)	Dec-25	Jan-26	Feb-26	Mar-26	Apr-26	May-26	Jun-26	Jul-26	Aug-26
Road Transport	12.0	-1.5	-3.1	22.6	-28.0	14.1	4.5		
Water Transport	2.9	1.7	-9.5	11.1	-7.7	5.4	-2.0		
Air Transport	0.0	3.5	-8.8	-4.7	-11.9	11.1	-8.7		
Warehousing & Logistics	11.9	-3.7	-4.2	25.1	-25.5	10.5	2.7		
Postal & Courier	11.9	-1.4	-5.6	20.5	-10.3	-1.3	5.3		
Telecom	7.7	0.5	-5.3	7.8	-1.7	-3.5	2.9		
Info & Broadcasting	39.0	-8.9	-8.9	42.4	-19.8	-11.6	24.1		
Banking	2.8	0.7	1.2	3.2	-0.9	0.3	0.9		
Insurance	20.7	0.8	-17.1	73.5	-34.0	-17.9	28.9		
Real Estate	12.5	0.8	4.4	9.7	-9.9	-5.4	5.0		
IT Services	27.6	-18.7	-2.2	34.2	-23.4	-2.7	19.8		
Professional Services	17.5	-14.2	-3.1	57.4	-36.3	5.1	9.9		
Admin & Support Services	18.2	-5.7	-8.0	46.8	-23.1	-11.8	14.6		
Arts & Recreation	33.9	-8.9	-8.1	34.1	-13.6	10.3	-15.2		
SERVICES									
PMI Services	-3.0	0.9	-0.7	-1.0	2.3	1.7	-4.0	-7.1	1.5
Foreign tourist arrivals	13.4	-6.9	-3.5	-24.9	-26.9	-3.2	13.0	23.8	
Dun & Bradstreet's Confidence Indices (QoQ)		2026 Q1			2026 Q2			2026 Q3	
Business Optimism Index- India		-6.1			4.2			-0.7	
Financial Confidence Index- India		-2.1			-0.4			1.8	
Investment Confidence Index- India		-7.0			3.7			-2.3	

Projected Outlook: Stable Growth, Emerging Risks

	Apr	May	Jun	Jul	Aug	Sept*	Oct*	Nov*	Dec*
Repo Rate (%)	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25
Reverse Repo Rate (%)	3.35	3.35	3.35	3.35	3.35	3.35	3.35	3.35	3.35
Bank Rate (%)	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50
General CPI (%)	3.48	3.93	4.38	4.45	4.82*	5.88	5.98	5.80	5.80
WPI (%)	8.36	9.88	9.87	9.78	9.33*	9.41	9.51	9.06	8.64
10 Year Government Securities (%)	7.05	7.02	6.89	6.78	6.86	7.00	7.00	6.90	6.80
91 days Treasury bill (%)	5.60	5.56	5.56	5.35	5.28	5.40	5.40	5.30	5.30
INR/USD Exchange Rate	93.55	95.60	94.97	95.82	95.47	95.5	95.4	95.2	95.2
Merchandise Exports (USD Mn)	43,713.0	45,438.1	40,384.4	44,243.9	40,482*	39,181	39,166	37,943	42,578
Merchandise Imports (USD Mn)	71,933.3	73,397.2	70,822.5	76,224.0	72,759*	73,260	73,368	73,222	73,031

Note: (*) implies forecasted values

Economic Developments in Focus

Introduction of the MSME Development (Amendment) Act, 2026

The MSME Development (Amendment) Act, 2026 marks a significant evolution of India's MSME policy framework, shifting the focus from enterprise classification and scheme-based support towards improving the overall business environment for micro, small, and medium enterprises. The amendment seeks to address persistent structural challenges faced by MSMEs, particularly delayed payments, limited access to working capital, lengthy dispute resolution processes, and high compliance burdens. The reforms align with the broader objective of improving formalisation, enhancing competitiveness, and creating a more efficient and digitally enabled MSME ecosystem.

A key feature of the amendment is the strengthening of payment and receivables mechanisms. The Act mandates Central Public Sector Enterprises (CPSEs) to settle procurement transactions with MSMEs through the Trade Receivables Discounting System (TReDS), while enabling state governments to introduce similar requirements for state-level public sector entities. This moves receivables financing from a facilitative mechanism to a more institutionalised framework and is expected to improve MSME liquidity by accelerating invoice realisation. The amendment comes at a time when invoice discounting through TReDS has expanded significantly, increasing from approximately Rs 400 bn in FY2022-23 to Rs 3.5 trn in FY2025-26, reflecting growing adoption of formal receivables financing channels.

The amendment also seeks to address one of the long-standing concerns of MSMEs, namely delays in resolving payment-related disputes. The Act empowers state governments to establish multiple Micro and Small Enterprises Facilitation Councils (MSEFCs) and strengthen their physical and digital infrastructure. It further introduces a time-bound process for dispute resolution, requiring mediation proceedings to be completed within 90 days, unresolved cases to be referred to arbitration within 30 days, and arbitral awards to be issued within 90 days after completion of pleadings. These provisions are intended to reduce delays in settlement, improve certainty of outcomes, and facilitate faster recovery of dues for MSMEs.

Another important change relates to the enforcement of payment claims. Under the revised framework, courts may direct the release of a reasonable portion of deposited amounts while challenges to awards remain pending. Further, where disputes remain unresolved for more than six months, courts are required to direct payment of at least 50% of the amount awarded to the MSME supplier. The amendment also enables mediated settlements and arbitral awards to be recovered as arrears of land revenue, thereby improving enforceability and increasing the likelihood of timely recovery. These provisions address one of the key weaknesses in the earlier framework, where MSMEs often faced difficulties in realising awarded amounts despite obtaining favourable rulings.

The Act further seeks to simplify regulatory compliance and promote greater formalisation. MSME registration has been made free and voluntary through a national digital platform, with provisions enabling states to establish complementary digital systems. In addition, the amendment decriminalises certain offences and replaces punitive provisions with warning-based and graded penalty mechanisms. This reflects a broader regulatory shift from enforcement through penalties towards facilitation through improved compliance frameworks, thereby reducing regulatory uncertainty and lowering compliance costs for smaller enterprises.

The MSME Development (Amendment) Act, 2026 represents a transition towards a more digital, rules-based and enterprise-friendly policy framework. Unlike earlier reforms that primarily focused on expanding eligibility for MSME benefits through revised classification thresholds, the 2026 amendment addresses operational bottlenecks that affect enterprise growth after formalisation. By strengthening payment discipline, institutionalising receivables financing, improving dispute resolution, and reducing compliance burdens, the Act has the potential to improve liquidity, business confidence, and productivity within the MSME sector. Its long-term effectiveness, however, will depend on implementation across states and the continued strengthening of digital and institutional infrastructure supporting MSMEs.

Introduction of Index of Services Production

The Index of Services Production (ISP) was introduced in Jul 2026 as a new high-frequency indicator to measure short-term changes in the output of India's services sector. As a counterpart to the Index of Industrial Production (IIP), the ISP seeks to address a long-standing gap in India's statistical framework by providing a regular measure of activity in the country's largest economic sector. The introduction of the index reflects the growing importance of services, which have accounted for more than half of India's Gross Value Added (GVA) over the past decade and continue to play a central role in growth, employment and exports.

A key feature of the ISP is its focus on measuring changes in the real volume of services output across a broad range of economic activities. The index has been developed with a base year of 2024-25 and initially covers 19 sub-sectors, including trade, transport, banking, insurance, telecommunications, real estate and professional services. Together, these sectors account for around 60% of the services economy.

The introduction of the ISP has been facilitated by significant improvements in India's statistical and administrative data ecosystem. The index draws on a combination of administrative datasets, GST information and the Annual Survey of Incorporated Services Sector Enterprises (ASISSE). In particular, the use of high-frequency GST data enables more timely measurement of service sector activity and expands the scope for evidence-based economic monitoring. The compilation methodology incorporates appropriate price deflators to convert nominal revenues into real output measures, thereby providing a clearer picture of underlying production trends.

The first trial release of the ISP suggests relatively broad-based momentum across the services sector. 14 of the 19 covered sub-sectors recorded double-digit growth in Apr 2026 compared with the corresponding period a year earlier, with particularly strong performance observed in accommodation and food services, retail trade, administrative and support services, real estate and telecommunications. While these results are preliminary, they demonstrate the potential of the index to provide timely insights into sectoral dynamics and short-term economic conditions.

FCNR(B) Deposits Scheme

In June 2026, the RBI introduced a special US Dollar-Rupee swap facility for fresh FCNR(B) deposits to support foreign currency inflows and strengthen external sector buffers. Under the framework, banks can access a concessional swap facility at par for fresh FCNR(B) deposits with maturities of three to five years, lowering hedging costs and exchange rate risk associated with mobilising foreign currency deposits. The scheme was made available only for fresh deposits, including renewals, and incorporates safeguards such as a one-year lock-in period and tenor matching between the swap and the underlying deposit.

The measure received strong market response, with FCNR(B) deposits mobilised under the facility rising to USD 65.4 bn as of 22 Aug 2026, accounting for most of the inflows raised through the RBI's special swap window.

Following the strong mobilisation, the RBI brought forward the eligibility deadline from 30 Sep to 31 Aug 2026. By encouraging relatively stable medium-term foreign currency liabilities rather than short-term capital inflows, the scheme has supported foreign exchange reserves, improved external sector resilience and augmented foreign currency liquidity in the banking system. During periods of external-sector pressure, FCNR(B) deposit mobilisation has been used as a policy tool to attract foreign currency inflows, ease pressure on the rupee and strengthen market confidence. The 2013 FCNR(B) scheme similarly attracted sizeable foreign currency inflows and helped stabilise external financing conditions during a period of rupee volatility. However, the concentration of repayments as deposits matured highlighted the need to monitor future rollover and redemption risks.

Base Year Revision of Wholesale Price Index, Index of Core Industries and introduction of Producer Price Index

India's revision of the Wholesale Price Index and the Index of Core Industries to the base year 2022-23 marks an important update to the country's price and industrial monitoring framework. The 2011-12 base year was updated to better reflect the evolving structure of the economy, including changes in production patterns, energy usage, industrial inputs, and the composition of economic activity over the past decade. Alongside the Wholesale Price Index (WPI) revision, the introduction of Producer Price Indices also signals a gradual move towards a more internationally comparable framework for measuring producer-level inflation.

The WPI, has been rebased from 2011-12 to 2022-23. The revised series expands the commodity basket from 697 to 957 items, allowing the index to capture a wider set of goods that are relevant to the current production economy. A notable change in the revised WPI series is the inclusion of renewable energy sources such as solar and wind power, reflecting the increasing contribution of clean energy to India's production and energy mix. The updated basket is therefore better aligned with the evolving structure of the economy and emerging sectors that were not adequately represented earlier. Another important methodological change is the adoption of Gross Value of Output (GVO) for deriving item weights. This approach links the index more closely to current production patterns and value generation across sectors, thereby enhancing its relevance as a measure of producer-level price movements and inflation trends.

A key feature of the revised ICI is the expansion and refinement of its coverage to better reflect the structure of India's industrial economy. The inclusion of iron ore as a ninth core industry broadens the representation of critical upstream inputs while strengthening the linkage between mining, manufacturing and infrastructure sectors. At the same time, methodological revisions, including the adoption of gross steel production data and the removal of overlapping coal categories, improve the consistency and accuracy of measurement. The revised weighting structure, aligned with the IIP 2022-23 series, further enhances comparability across industrial indicators and strengthens the ICI's role as a leading indicator of industrial activity.

The introduction of Producer Price Indices with base year 2022-23 is another significant development. The new framework includes Output PPI, Trial Input PPI for manufacturing and Service PPIs for selected service sectors. Unlike WPI, which mainly measures wholesale prices of goods, PPIs look at price changes from the producer's perspective and can cover both goods and services. This makes them better suited for tracking input cost pressures, output price changes and the transmission of inflation through the production chain.

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India's Export Growth Amid Global Trade Uncertainty

India's exports remained resilient during Apr-Jul 2026-27 despite disruptions arising from the West Asia crisis, elevated freight and insurance costs, and continued uncertainty in the global trading environment. Cumulative merchandise exports increased by 17.0% y-o-y to USD 173.8 bn, while total merchandise and services exports reached an estimated USD 316.4 bn, registering growth of 13.2%. Non-petroleum exports rose by 12.8% to USD 143.6 bn, indicating that export growth was not solely driven by petroleum products but was supported by a broader expansion across sectors and markets. Export momentum strengthened further in Jul 2026, when merchandise exports grew by 19.6% y-o-y to USD 44.2 bn.

The strong performance reflected both product and market diversification. Petroleum products, electronic goods, engineering goods and chemicals recorded robust growth, while exporters expanded their presence across East and Southeast Asia and Africa. Exports to China grew significantly during the period, highlighting India's ability to redirect trade flows and capitalise on emerging market opportunities amid a challenging global trade environment.

However, import growth continued to outpace exports. Merchandise imports increased by 19.3% to USD 292.4 bn during Apr-Jul 2026-27, driven by higher imports of petroleum, fertilisers, electronics and coal. Consequently, the merchandise trade deficit widened, reaching nearly USD 32 bn in Jul 2026, underscoring continued dependence on imported energy and intermediate goods.

El Niño and Weak Monsoon Heighten Agricultural Risks

India's agricultural outlook came under pressure during the early southwest monsoon season amid deficient rainfall and the emergence of El Niño conditions. Cumulative rainfall was initially around 43% below normal, with the delayed monsoon posing risks to kharif cultivation in rain-fed regions. The government identified 315 districts as potentially vulnerable to weak rainfall, including 111 high-priority districts with irrigation coverage below 25%, and introduced contingency measures focused on short-duration and low-water crops, water conservation, and the availability of seeds, fertilisers and fodder.

A major element of the strategy has been crop diversification away from relatively water-intensive crops such as tur, soybean and cotton towards crops including maize, bajra and moong, which are better suited to moisture-stressed conditions. Simultaneously, farmers were encouraged to adopt short-duration and drought-tolerant seed varieties, allowing production cycles to adjust to delayed or uneven rainfall. These interventions are intended to preserve acreage and yields despite adverse weather conditions. The government has promoted water conservation through farm ponds, check dams and local storage infrastructure while encouraging micro-irrigation, mulching, inter-cropping and balanced fertiliser use. From an economic perspective, these measures aim not only to address the immediate effects of a weak monsoon but also to improve resilience against future climate-related shocks.

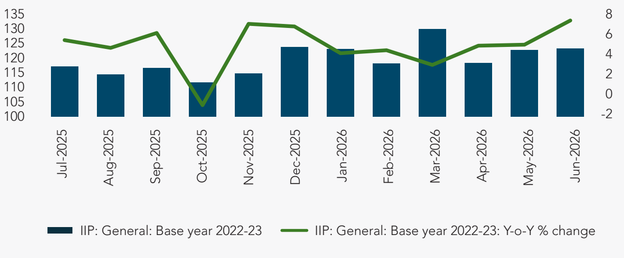
As the monsoon season progresses, the policy response appears focused on mitigating potential supply-side disruptions before they translate into lower agricultural output and higher food inflation. While rainfall uncertainty continues to pose risks for rain-fed crops, the emphasis on crop diversification, water management and contingency planning is expected to reduce the severity of production losses. Beyond its impact on agricultural output, a weaker monsoon could also affect rural incomes and consumption demand, particularly in districts with high dependence on rain-fed farming. Lower farm incomes typically weigh on spending on consumer goods, automobiles, housing-related products and discretionary purchases in rural areas.

Macroeconomic Performance

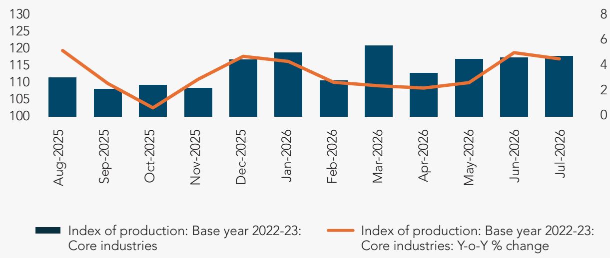
Industrial growth stays firm, led by manufacturing and investment activity

- IIP grew by 6.7% YoY in Jul 2026, moderating from 7.3% in Jun. The growth was primarily driven by the manufacturing sector, which expanded by 7.3%, while Electricity & Gas Supply registered an increase of 8.7%. Water Supply, Sewerage & Waste Management also grew by 7.4%, whereas Mining & Quarrying contracted by 0.9%.
- For IIP, capital goods remained the key growth driver of industrial production, expanding by 16.1%, reflecting sustained investment activity. Growth was also supported by Consumer Durables (10.5%), Intermediate Goods (10.0%), and Infrastructure/Construction Goods (6.9%). Meanwhile, Primary Goods recorded moderate growth of 4.1%, while Consumer Non-durables declined by 1.0%, indicating uneven consumption trends.
- The Index of Core Industries (Base: 2022-23) showed relatively moderate growth compared with overall industrial production. Core sector growth averaged 4.3% during Apr-Jul 2026, supported by strong performance in iron ore (25.2%), cement (9.9%), electricity (9.3%) and steel (4.5%), indicating continued momentum in construction and infrastructure activity.
- However, contractions in fertilizers (-5.2%), natural gas (-4.4%), crude oil (-4.3%) and refinery products (-2.5%) highlighted persistent weakness across parts of the energy sector. Nevertheless, ICI growth improved to 5.4% y-o-y in Jul 2026 following a revised 6.0% expansion in Jun.

IIP (Y/Y %)



Performance of Core Industries



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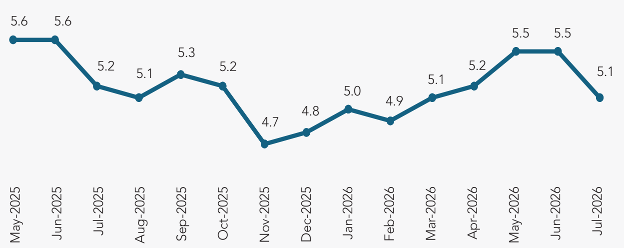
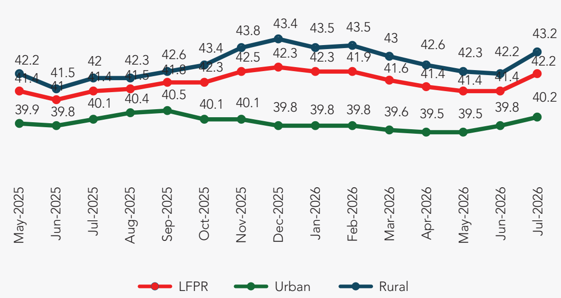
Labour market remains steady amid mixed trends

- Labour market conditions remained broadly stable through mid-2026. The unemployment rate (15+ years, CWS) increased from 5.2% in Apr 2026 to 5.5% in Jun before easing to 5.1% in Jul, suggesting some improvement in employment generation despite a challenging global environment.
- Labour market trends were mixed across regions. Urban unemployment remained largely stable at 6.6-6.7% during the quarter, while rural unemployment rose from 4.6% in Apr to 5.0% in Jun before moderating to 4.5% in Jul. Urban labour market conditions also improved on a year-on-year basis, with unemployment declining from 7.2% in Jul 2025 to 6.7% in Jul 2026.
- Labour force participation remained resilient, with the overall LFPR (15+ years) increasing from 54.4% in Jun 2026 to 55.4% in Jul 2026. Female LFPR rose to 34.4% from 33.3% a year earlier, indicating continued improvement in women's participation in the workforce.
- Employment quality showed gradual improvement, with the share of regular wage/salaried employment increasing in both rural and urban areas during Apr-Jun 2026. Non-farm employment also strengthened, reflected in a higher share of employment in the secondary sector and a rise in tertiary-sector employment, particularly in rural areas (21.7% to 22.7%).

Unemployment Rate



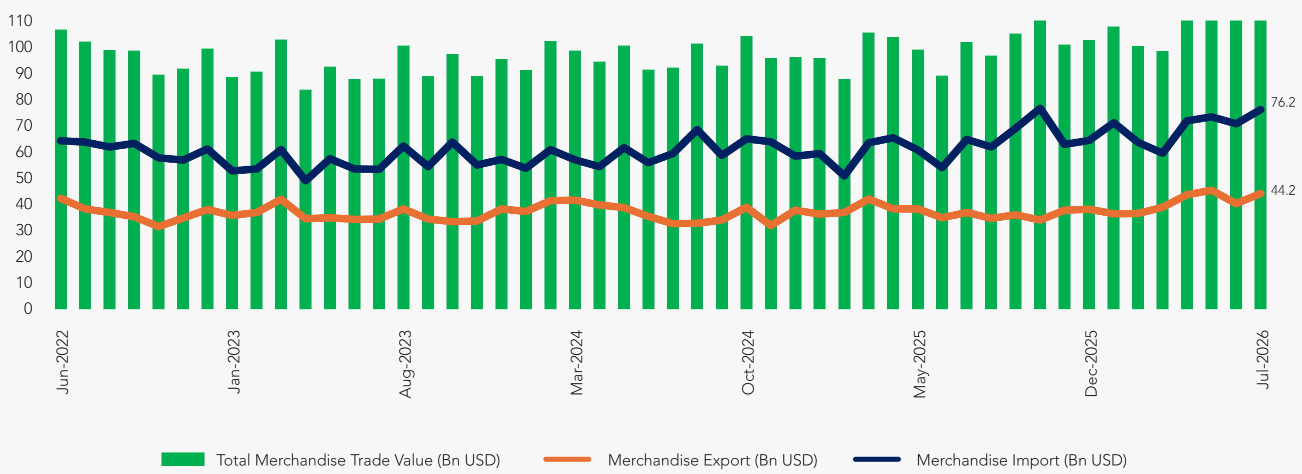
Trends in Labour Force Participation Rate (LFPR) Overall, Rural and Urban



External sector faces emerging headwinds

- India's external sector remained resilient despite global uncertainty. Total exports (goods and services) increased by 13.3% y-o-y to USD 80.1 bn in Jul 2026, while merchandise exports rose by 19.6% to USD 44.2 bn, supported by strong growth in petroleum products, electronic goods and engineering goods. Cumulative exports during Apr-Jul 2026-27 reached USD 316.4 bn, up 13.2% y-o-y.
- Imports remained elevated, reflecting strong domestic demand and higher commodity prices. Total imports increased by 15.8% y-o-y to USD 95.2 bn in Jul 2026, while merchandise imports rose to USD 76.2 bn. During Apr-Jul 2026-27, cumulative imports reached USD 365.9 bn, a growth of 17.3% over the previous year.
- As import growth outpaced exports, the trade deficit widened. India's overall trade deficit stood at USD 15.0 bn in Jul 2026, compared with USD 11.4 bn a year earlier, while the merchandise trade deficit widened to around USD 32 bn. Cumulatively, the trade deficit reached USD 49.4 bn during Apr-Jul 2026-27.
- Despite merchandise trade pressures, India's external position continued to benefit from strong services exports. Services exports were estimated at USD 35.9 bn in Jul 2026 against services imports of USD 18.9 bn, helping offset part of the merchandise trade gap and supporting current account stability.
- External buffers remained strong, with foreign exchange reserves continuing to provide a cushion against external shocks, commodity-price volatility and geopolitical uncertainty. Capital flows remained mixed amid shifting global risk sentiment, although banking capital inflows, NRI deposits and external commercial borrowings continued to support the capital account.

India's Merchandise Trade Value



Commodity Conditions Turn Mixed Amid Diverging Metal Trends

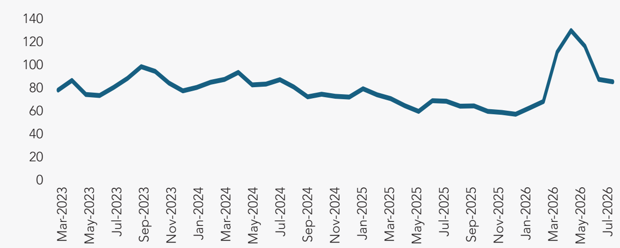
- Commodity market conditions remained mixed during May-Jul 2026. Prices of several commodities, including crude oil, aluminium, nickel and copper, rose in May amid heightened geopolitical tensions, supply-chain concerns and precautionary inventory building by buyers. As supply disruptions proved less severe than initially feared and market sentiment stabilised, many commodity prices moderated during Jun-Jul.

- Brent crude prices declined steadily from their Apr peak through Jul, representing a notable reversal from the sharp increase recorded earlier. The correction signals some moderation in pressures on India's oil import bill, fuel inflation and downstream input costs.

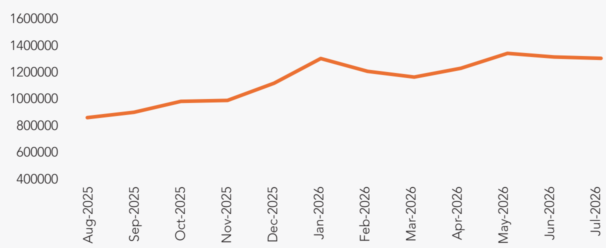
- Copper and zinc hit record highs in Aug-2026, rising 55.0% and 50.6% YoY respectively, signalling strong industrial-metal price momentum. Nickel and aluminium prices increased in Aug-2026, with aluminium showing the stronger price momentum.

- Coal production stood at 80.1 MT in Jul 2026, unchanged from Jun 2026 and reflecting a stable trend after the seasonal drop to 74.3 MT in Apr 2026, though still below the Jan–Mar 2026 levels of over 100 MT.

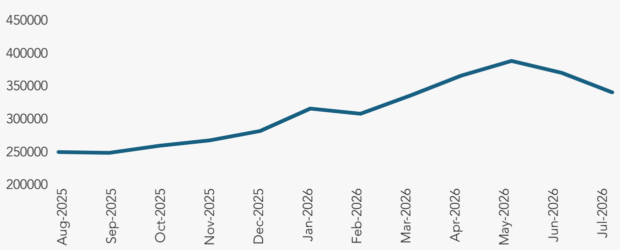
Brent Crude Oil



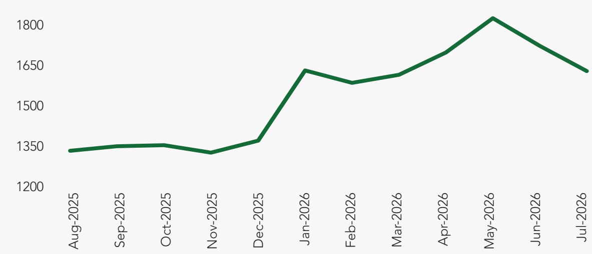
Copper Prices (Rs/Tonne)



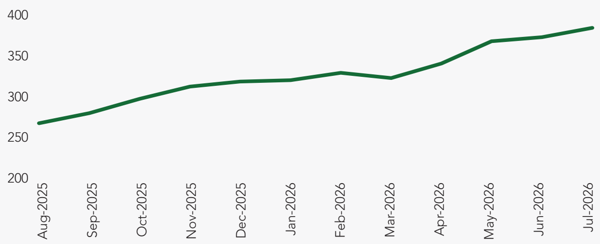
Aluminium Prices (Rs/Tonne)



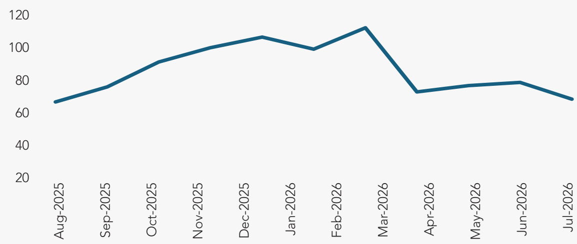
Nickel Prices (Rs/Kg)



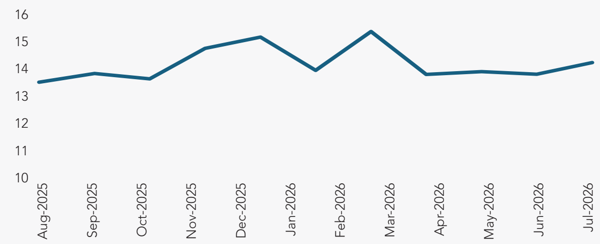
Zinc Prices (Rs/Kg)



Production of Coal (in MT)



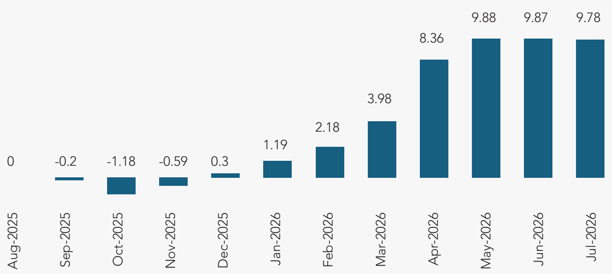
Production of Crude steel (in MT)



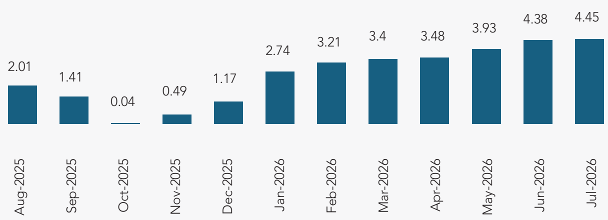
Food-led pressures push CPI above target; broader inflation remains contained

- Headline CPI inflation increased from 3.9% in May 2026 to 4.4% in Jul 2026, moving above the RBI's 4% target from June, though remaining within the tolerance band. Food inflation remained the principal driver, with CFPI inflation rising from 4.8% to 5.5% over the same period. Rural inflation continued to exceed urban inflation, reaching 4.8% in Jul compared with 4.0% in urban areas, reflecting higher food-price pressures in rural India.
- Food inflation remained uneven and concentrated in select horticultural commodities. While tomato prices moved into deflation by Jul, inflation accelerated sharply in ginger (83.6%), garlic (35.4%) and onion (22.5%). Potato prices remained in deflation, partially offsetting broader food-price pressures.
- Producer-side price pressures remained elevated, with WPI inflation hovering around 9.7-9.8% during May-Jul 2026. Although fuel and power inflation moderated from 30.3% in May to 20.1% in Jul, inflation broadened across primary articles, manufactured products and food items. Wholesale food inflation rose from 4.6% in May to 6.7% in Jul, indicating increasing pass-through of food, raw material and industrial input costs.

WPI (Y/Y%)



CPI (Y/Y%)

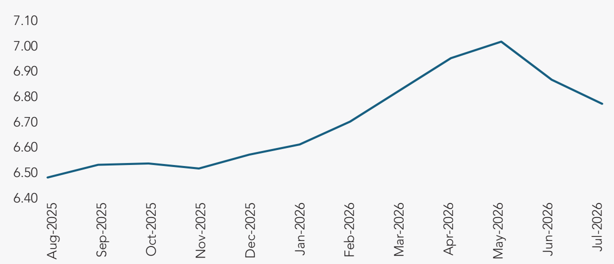


Note: From June 2026, WPI was rebased to 2022-23=100, replacing 2011-12, with DPIIT expanding the commodity basket from 697 to 957 items, adopting updated weights based on Gross Value of Output and introducing improved index-computation and data-imputation methods.

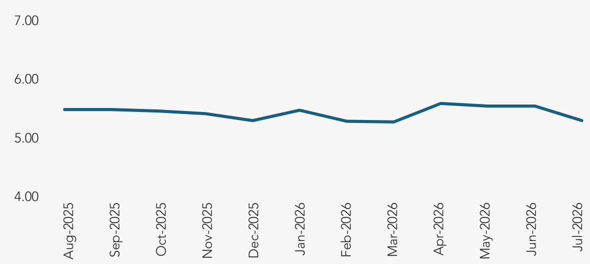
Policy Rate Steady Amid Moderating Liquidity and Firming Yields

- The RBI maintained the policy repo rate at 5.25% in the Jun 2026 review, with the MSF/Bank Rate at 5.50% and the monetary policy stance neutral. The continued pause reflected a cautious approach as elevated energy prices, supply-chain disruptions and monsoon uncertainty increased inflation risks, even as underlying domestic inflation pressures remained contained.
- The RBI continued to manage liquidity through variable-rate operations and a USD 5 bn forex swap, while introducing swap and regulatory incentives for fresh FCNR(B) deposits to support foreign-currency inflows amid volatile external conditions.
- Short-term money-market rates remained broadly aligned with the policy corridor, with the 91-day Treasury Bill yield near 5.3% in Jul. However, the 10-year G-sec yield hardened to around 6.8% by end-Jul, reflecting higher inflation-risk premia from elevated energy prices, global yield movements and uncertainty around the domestic inflation outlook.
- Domestic credit conditions remained supportive, with bank credit growing 16.2% year-on-year as of mid-May, led by services and retail credit, alongside strengthening flows to MSMEs and large industries. However, some hardening in deposit and lending rates, coupled with elevated input costs and long-term yields, could gradually raise borrowing costs for interest-sensitive sectors.

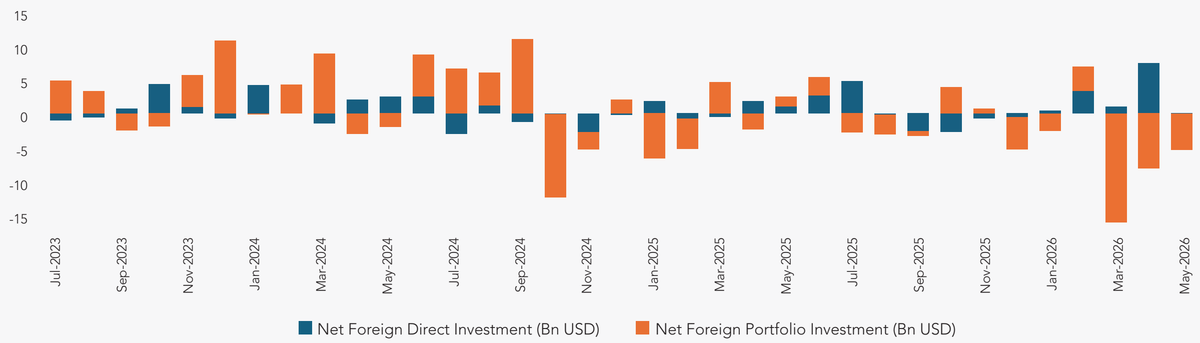
10-Year G-Sec Yield (%)



91-day Treasury bill



FDI & FPI



Economy Observer is a Quarterly report that shares an in-depth analysis on key macroeconomic developments in India and provides a monthly forecast of key economic indicators, providing insight into the expected direction of the Indian economy.

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