



## Indian Economy- Looking Ahead 2026-27

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Global economy continues to be affected by trade tensions, policy uncertainty, possibility of sanctions and arbitrary tariff escalation. In the absence of rule based multilateral institutions risks to global trade and investment have increased. The supply chains have become more volatile 'just in time' has to get supplemented by 'just in case', so costs of operating a global business has gone up. Rule based multilateral trading systems is getting replaced by bilateral and regional treaties, which could often be less optimal in the long run. Global headwinds have impacted the Indian economy in 2025, similar conditions would continue to prevail in 2026 too. Notwithstanding regional conflicts, Trump tariffs and fragmentation of trade, re-routing via third countries etc., both global and Indian economies have been quite resilient. OECD economic outlook is of the view that 2025 global growth will be around 3.2%, this may come down marginally to 2.9% in 2026 due to decline in growth rates of large economies like USA (from 2% in 2025 to 1.7% in 2026) and China (from 5% to 4.4%). The tailwinds from AI related investments which supported the US economy and spike in market capitalisation, could be less overwhelming in 2026.

Much to the dismay of naysayers, the Indian economy continues to stride on. In the first half of 2025-26 the economy grew at 8%, for the entire year 2025-26 GDP growth estimates is marginally above seven percent. According to the RBI, it can touch 7.3%. The sectoral growth have been impressive in the first half of 2025-26, industry grew at 7.6% and services by 9.3%. Inflation has remained in check in the first half of 2025-26, for the rest of the financial year no major surge in prices is anticipated. Average headline inflation for 2025-26 can be contained at around 2%, very much within RBI threshold of 2 to 6%. However, when one takes core inflation, that is inflation rate excluding food and fuel, the volatile elements, then price growth is 4%. This may require some monitoring. Food prices in 2026 can rise marginally compared to 2025, when there was a decline. India continues to have record wheat stock and rabi crop too is expected to be good based on sowing data.

The crude prices are expected to remain soft, the IEA estimates show demand for global oil could grow at a lower rate than the supply. This could lead to softening of prices. In 2025 world oil supply was 106.1 mln barrels/day in 2026 it is expected to reach 108.5 mln barrels/day, demand was 103.84 mln barrels /day in 2025 it is expected to touch 105.54 mln barrels/day in 2026. Both price and supply scenarios can be more benign if Venezuela joins supply mainstream. Resolution of Russia-Ukraine conflict, whenever it happens along with removal of sanctions can further add to supplies.

Both monetary and fiscal policies till date have been supportive of higher growth, there is no reason why the direction should change in 2026-27 when inflation is expected to be modest. Major changes in Repo rate cuts have already taken place, there is a limited scope left for further reduction. Looking ahead, liquidity management will remain a key issue in 2026-27 specially when the economic growth is picking up. RBI has recently provided three trillion rupees

through open market operations, to this has been added long tenure dollar rupee swaps. Both the measures are supposed to offset the impact of intervention in foreign exchange market and seasonal demand spike in liquidity. In 2026-27, banking system needs to ensure liquidity does not dry up periodically, should that happen then loan rates can harden irrespective of the quantum of repo rate cut and transmission may start faltering. Both private consumption expenditure and gross fixed capital formation grew at 7.9% and 7.3% respectively year on year, in the second quarter of 2025-26. In this context, reasonably priced liquidity is important to support growth momentum.

On the fiscal side, it is becoming increasingly clear that the gross tax revenue collection is likely to be lower than the budget target. The shortfall in tax revenue collection will be met by savings on revenue expenditure by various ministries and robust non-tax revenue collection, which includes dividends from public sector undertakings and RBI. As a result, the 4.4% fiscal deficit target could be met without difficulty. Reforms in personal tax and GST rates have contributed to lower than budgeted collection. However, as demand improves with sustained consumption and investment growth the tax collection should improve. Some recent revenue increasing steps have been taken by the government, these are excise duty on tobacco products and national security and public health cess. What is indeed remarkable is the Government continues to maintain the capital expenditure growth and the target set in the budget is likely to be met. Consequently, the part of private expenditure which is tethered to Government capital expenditure will continue to grow too. From the funding point of view no crowding out is visible in the immediate future. Government of India's debt to GDP ratio is steadily coming down. However, the State debt position needs stricter monitoring in 2026-27.

Notwithstanding the tariff and trade restrictions, sanctions etc., the current account deficit is very much within control at 1.3% of GDP at the end of the second quarter of 2025-26. The strong growth in net services exports and remittances have helped in mitigating the deficit created by merchandise trade. If crude and petroleum product prices are contained as discussed earlier then a major component of inelastic import would be under control in 2026-27. Further, a weaker rupee can make exports more competitive and imports costlier. This will put a strain on imports of items which have elastic demand.

However, net outflows of funds through the FPI route is a matter of concern, this has the potential to affect exchange rate significantly. According to unofficial estimates around \$18 billion have been withdrawn from the country by the FPIs in 2025. Rupee in 2025 depreciated by 5% which is more than its historical average. However, at the moment real effective exchange rate of rupee is in the 95-97 range showing distinct undervaluation. This should get corrected in 2026-27. A downward slide in the rupee in 2026 is unlikely. India's foreign exchange reserves at the end of December 2025 touched \$696 bln, which is equivalent to eleven months of imports. In a scenario, where India's projected growth performance is at around 7% in 2026-27, its burgeoning market supported by higher private consumption expenditure and higher gross fixed capital formation, along with supportive Government policies, can attract both FDI and FPI. The availability of skilled manpower and introduction of labour market reforms would strengthen the attractiveness of Indian market vis a vis other emerging countries. Major investments in GCCs (Global Capability Centre) have already started. Further market valuations have already got largely corrected, the revenue growth of corporates are following nominal GDP growth and corporate earnings have picked up. A supportive budget along with positive actions in the area of capital gains tax can make India an attractive destination for FPI in 2026-27. With the right kind of policy signals in the 2026-27 budget, the economy can bring in foreign funds, this will also provide the necessary correction in the rupee exchange rate.

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