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Macro Pulse

JUNE 2026

Summary

The global macroeconomic environment continues to be shaped by the Middle East conflict, though sentiment has shifted decisively towards de-escalation following the US-Iran MoU signed on 19th Jun, which envisages a cessation of hostilities and the reopening of the Strait of Hormuz. After averaging around USD 95 pb in early Jun-26, Brent crude has corrected sharply to around USD 80 pb currently. However, depleted crude supply buffers, inventory rebuilding, and residual regional instability argue against assuming a quick return to the pre-war level of oil prices. We now work with a lower FY27 crude price assumption of USD 80-85 pb, compared with USD 95 pb earlier. Notably, the correction in oil prices has not impacted the hawkish pivot within the FOMC, with market participants now expecting two rate hikes from the Fed by Mar-27.

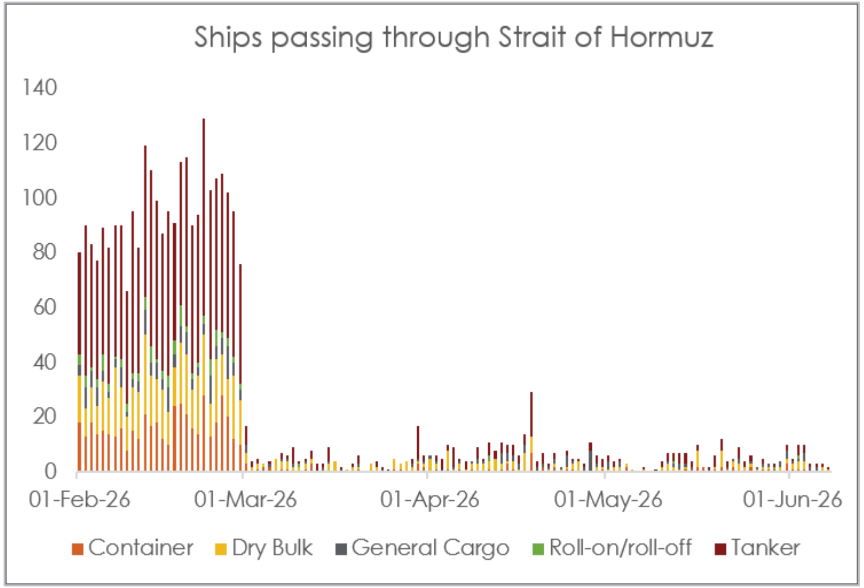
India's economy has held up better than feared, with Q4 FY26 GDP growth at 7.8% and high-frequency broad activity indicators still signaling stability. The near-term macro mix, however, remains uneven. Higher fuel prices, rising input costs, weak consumer confidence, delayed monsoon onset and a likely 10% rainfall deficiency point to moderation in consumption and rural demand through FY27. We revise FY27 GDP growth up marginally by 20 bps to 6.4%, reflecting lower crude price assumptions, while retaining caution on monsoon-linked downside risks. Meanwhile, inflation risks remain the key domestic macro challenge for now. WPI inflation surged to 9.7% in May-26, while CPI has begun to reflect fuel pass-through and early second-order effects through higher transport, dining-out and food prices. Core inflation is likely to adjust higher with a lag, aided by firm input costs, rupee depreciation and elevated household inflation expectations. However, softer crude prices post the US-Iran MoU prompt a downward revision in our FY27 CPI forecast to 5.1% from 5.5% earlier.

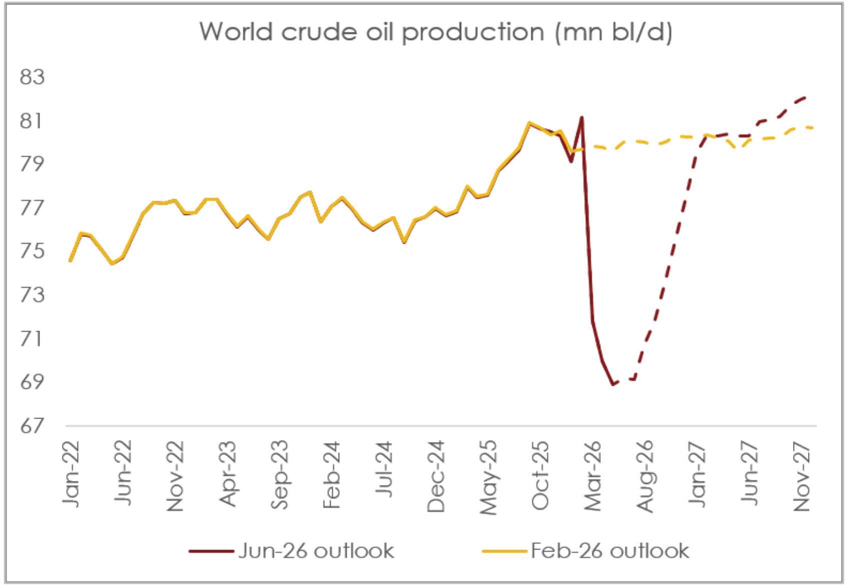
The fiscal position has started FY27 under pressure from weak receipts and higher subsidies - though a record RBI dividend and H2 expenditure calibration should help defend the 4.3% of GDP target. Coordinated GoI-RBI measures have improved the external outlook, with the FY27 BoP now seen at a USD 70 bn surplus and the CAD at 0.9% of GDP. These steps have aided INR, which we expect to strengthen towards 92 by Sep/Dec-26 before stabilizing around 95 by Mar-27. For rates, abundant liquidity and FPI debt inflows should support 10Y g-sec yields near 6.75% by Sep-26, before domestic inflation, supply risks and global tightening push yields towards 7.25% by Mar-27.

US/Israel-Iran: Peace returns, risks linger

Shipping through the Strait of Hormuz has remained severely impaired over the past three months. Following the much-awaited US Iran MoU signed on 19th Jun-26, the expected restoration of normal vessel traffic over the course of next 30 days through the Strait will be a key variable to watch.

The EIA* estimates global oil production to have declined by ~12 mb/d in May-26 relative to Feb-26 levels. Even as output levels gradually normalise, depleted crude supply buffers and anticipated inventory drawdowns could lend support to Brent price in the near-term.



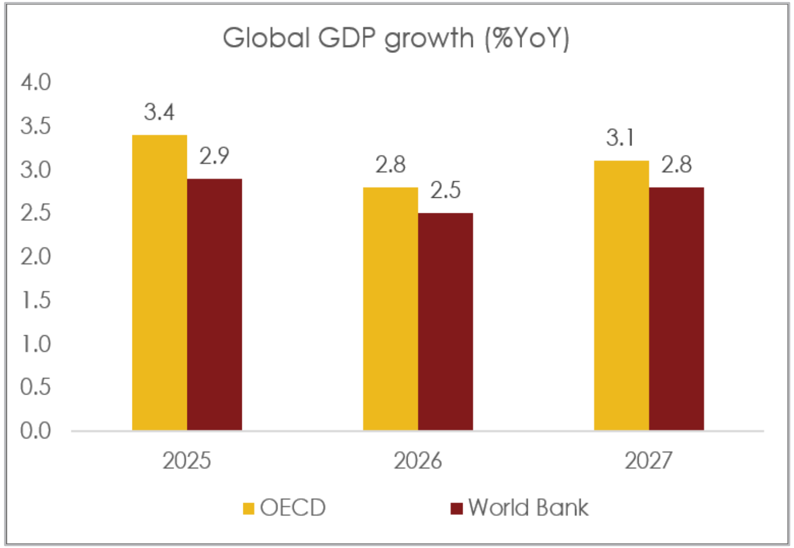


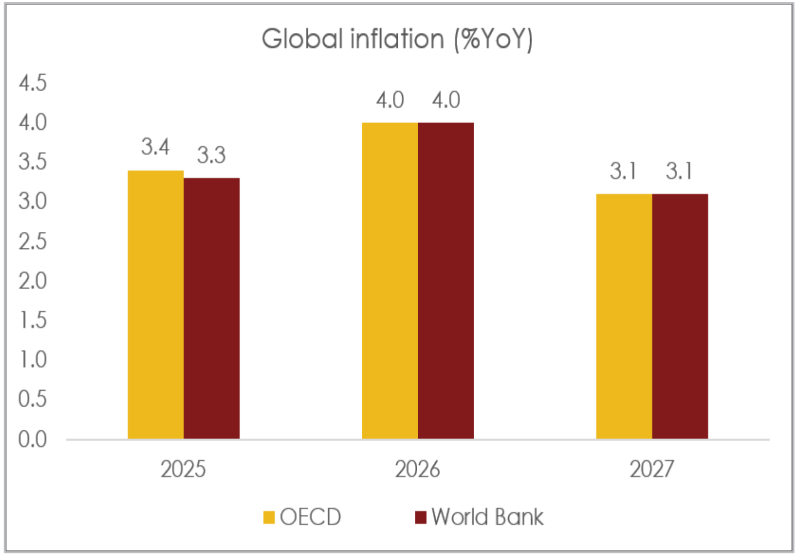
*Source: US Energy Information Administration (EIA) June-26 outlook

2026: A tougher macro mix

The World Bank projects global growth in 2026 at its weakest pace since the pandemic, dragged by energy-importing and conflict-affected economies. The OECD expects a 60 bps deceleration in growth, assuming a gradual return of Gulf-led energy production from Q3 CY26.

Global inflation is expected to overshoot in 2026, before returning below pre-conflict levels in 2027, aided by normalisation of energy flows and a relatively restrictive monetary policy by major central banks.



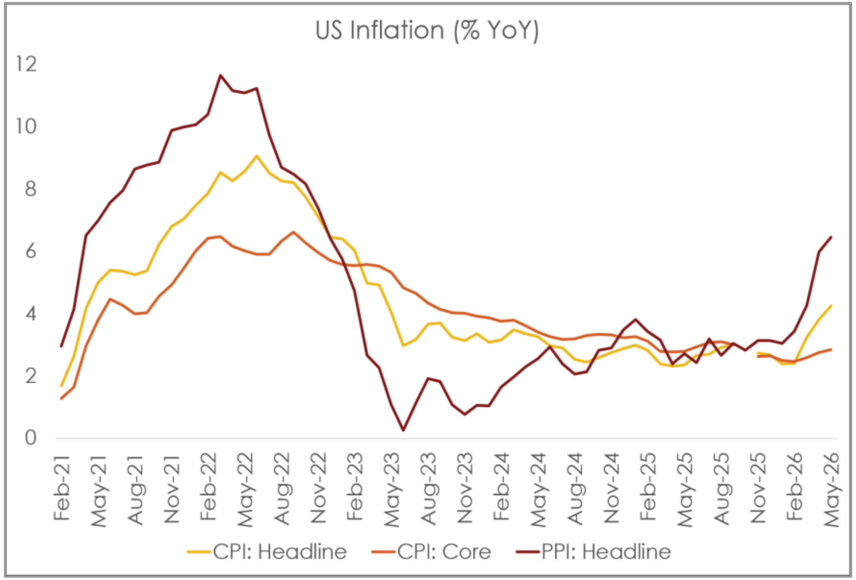


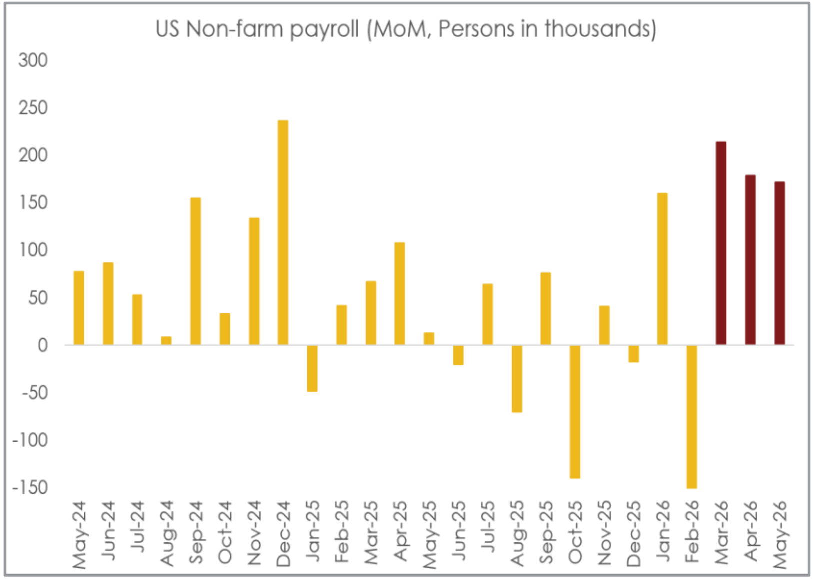
Note: Projections correspond to baseline scenario assumptions for crude prices.
For 2026, OECD: USD 92 pb ; World Bank: USD 94 pb
For 2027, OECD: USD 80 pb ; World Bank: USD 76 pb

US Economy: Prices catch fire, labour holds firm

Inflationary pass-through from the Middle East oil shock is now visible in the US economy, with PPI inflation at a 42-month high (6.5%) and headline CPI at a 36-month high (4.2%) in May-26. Underlying price pressures are also firming, with core inflation reaching a 7-month high of 2.9%.

Momentum in labour market continues to remain intact. Payroll gains averaged 188,000 during Mar–May-26, a marked improvement from the average monthly increase of 11,000 over the 12 months through Feb-26.





Warsh's first FOMC: Hawkish Reset, Less Guidance

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Policy Stance
FFR held 3.50–3.75%; price stability explicitly prioritized over labor.

SEP Revision
Median 2026 core PCE revised up to 3.3% from 2.7%.

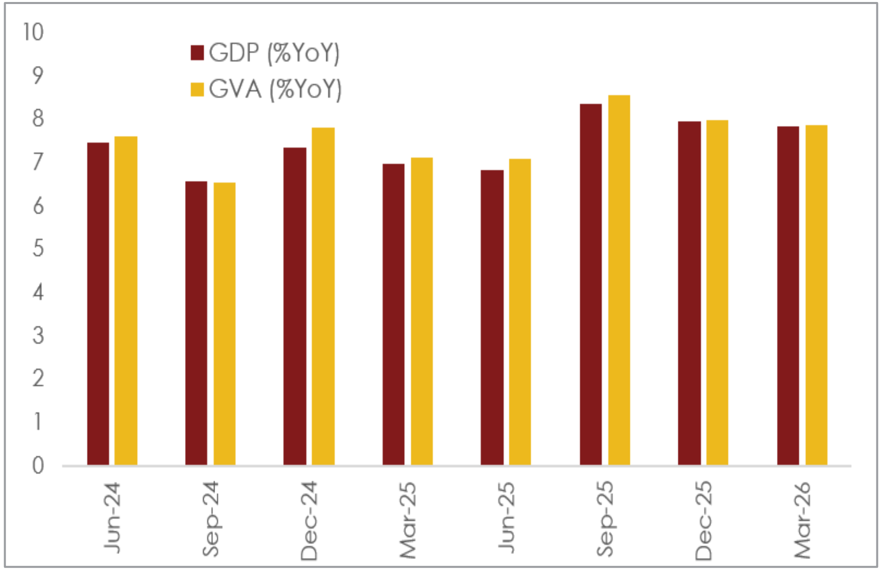
Forward Guidance
No dot (plot) submitted; timing promises replaced by tightening optionality.

Operational Reset
Five task forces: communications, balance sheet, data, productivity/AI, inflation frameworks.

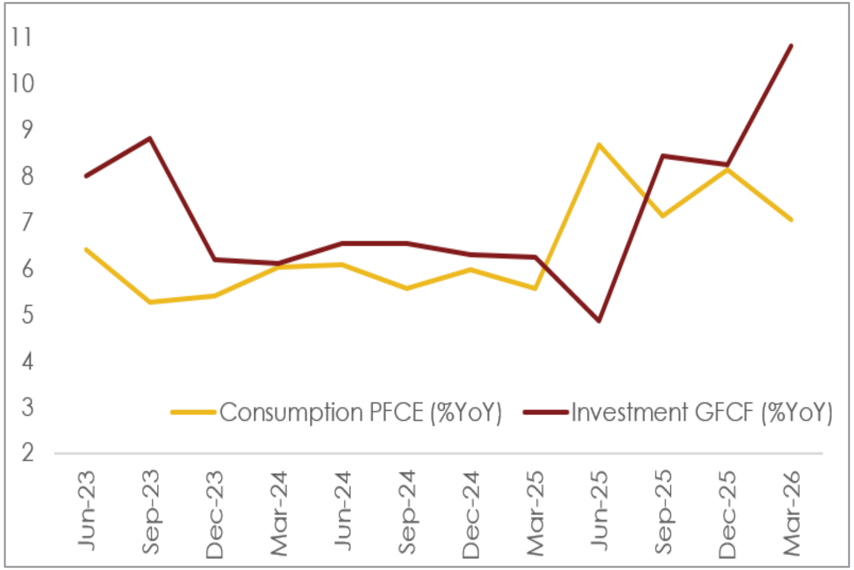
Communications
Statement trimmed to ~130 words; boilerplate removed.

India Q4FY26 GDP: Holds ground despite Middle East crisis

India's GDP growth displayed notable resilience in Q4 FY26, easing marginally to 7.8% from an upwardly revised 8.0% in Q3 FY26. Economic activity remained largely insulated from initial spillover effects of Middle East conflict, as momentum was supported by lower US tariffs, sustained government-led capex, and residual benefits of GST rate rationalization.



Internally, the downside in consumption was more than offset by strength in GFCF, growing at a record pace of 10.8%. Q4FY26 reflected a robust investment cycle, underpinned by sustained capex by Central & State governments, alongside a pickup in project completions in public and private sector enterprises, as per CMIE data.



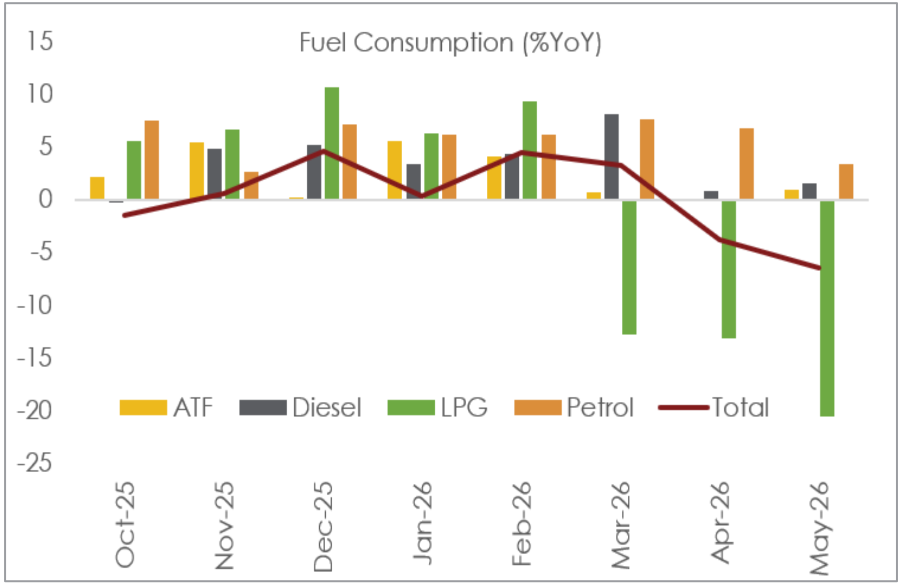
Domestic high-frequency indicators remain a mixed bag in early FY27

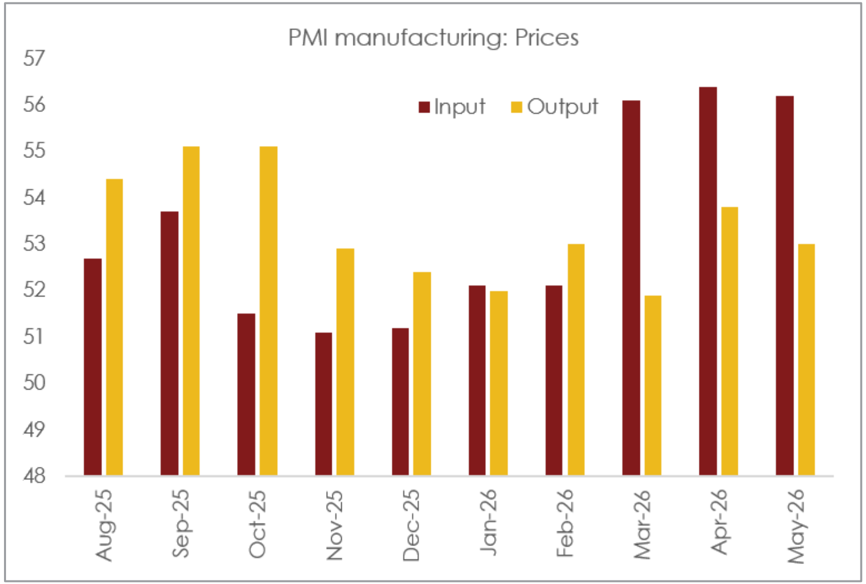
Key economic indicators: Industry														
	Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25	Jan-26	Feb-26	Mar-26	Apr-26	May-26
IIP (%YoY)	5.8	4.7	3.0	5.0	3.6	5.5	0.0	6.5	5.8	4.4	5.2	3.2	4.9	
PMI Manufacturing (index)	58.2	57.6	58.4	59.1	59.3	57.7	59.2	56.6	55.0	55.4	56.9	53.9	54.7	55.0
PMI Exports (index)	57.6	56.9	60.6	57.3	56.1	56.5	54.7	54.1	54.0	54.1	53.2	55.0	56.3	53.7
Core Industries (%YoY)	1.0	1.2	2.2	3.7	6.5	3.3	-0.1	2.1	4.7	4.7	2.8	1.2	1.7	
Steel consumption (%YoY)	6.0	8.1	9.3	7.3	10.0	8.9	2.4	6.0	5.4	4.9	12.8	13.7	8.1	9.2
Cement production (%YoY)	6.3	9.7	8.2	11.6	5.4	5.0	5.2	14.6	13.7	11.3	8.9	4.7	8.2	8.4
Government capex (%YoY)	61.0	38.7	43.7	-10.5	113.1	30.9	-28.3	-13.8	-24.5	-24.5	59.6	-41.8	18.8	
Tractor production (%YoY)	20.5	9.1	9.8	11.5	9.4	23.0	13.0	37.5	57.9	14.6	80.0	28.6	18.1	15.5
Commercial vehicle sales (%YoY)	-0.1	-3.7	6.6	0.2	8.6	2.7	21.1	17.0	24.6	15.1	28.9	15.1	18.8	5.3
Credit to industry (%YoY)	6.6	4.8	5.9	6.0	6.5	7.3	10.0	9.6	13.3	12.1	13.5	15.0	15.1	
Exports (goods) (%YoY)	-3.8	-1.2	-1.3	13.3	5.7	6.0	-12.5	18.6	1.1	0.4	-0.8	-7.4	13.8	18.0
Services														
PMI Services (index)	58.7	58.8	60.4	60.5	62.9	60.9	58.9	59.8	58.0	58.5	58.1	57.5	58.8	59.8
Exports (services) (%YoY)	8.9	9.6	12.0	10.4	2.8	12.6	2.2	6.7	13.0	9.8	9.7	7.3	12.7	13.2
Credit to services (%YoY)	10.5	8.7	9.2	10.6	10.6	10.2	13.0	11.7	15.3	15.5	16.3	19.0	18.6	
Air passenger traffic: domestic (%YoY)	9.7	2.6	3.7	-2.5	-0.5	-2.5	3.5	7.0	-4.9	3.1	-0.1	-1.3	-2.8	
Air passenger traffic: international (%YoY	13.0	5.0	3.4	5.5	7.7	7.3	9.7	7.5	6.0	7.1	3.0	-18.5	-16.1	
Port cargo (%YoY)	7.0	4.4	5.5	4.0	2.5	11.5	12.0	14.6	12.8	7.6	3.8	0.4	2.4	6.6

Impact of Middle East crisis visible in select indicators in May-26

The pass-through of higher global prices to domestic consumers is incrementally impacting fuel consumption, that contracted by a sizeable 6.5%YoY in May-26. LPG consumption recorded double-digit contraction for the third consecutive month.

Input prices continued to see a strong acceleration, for the third consecutive month in May-26. In comparison, output prices have seen limited upside, indicating a deterioration in producer margins.

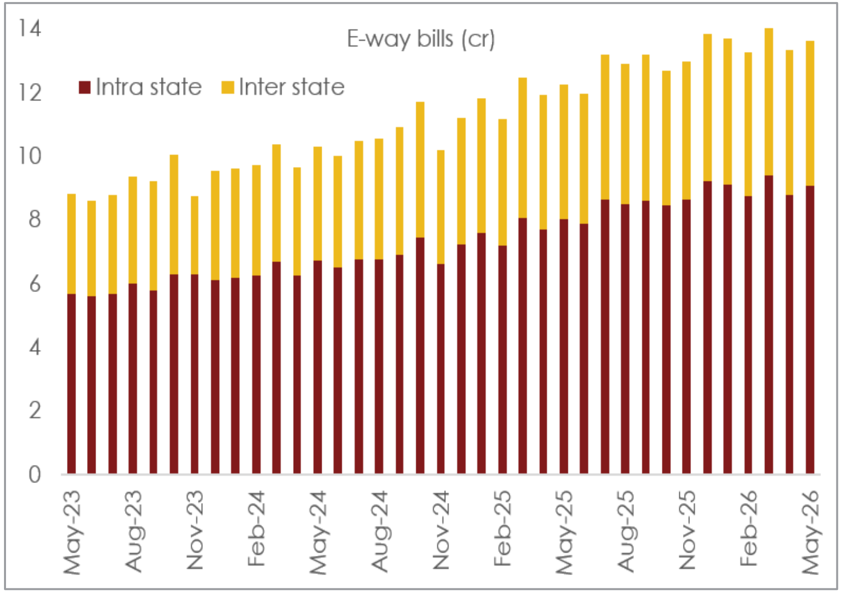


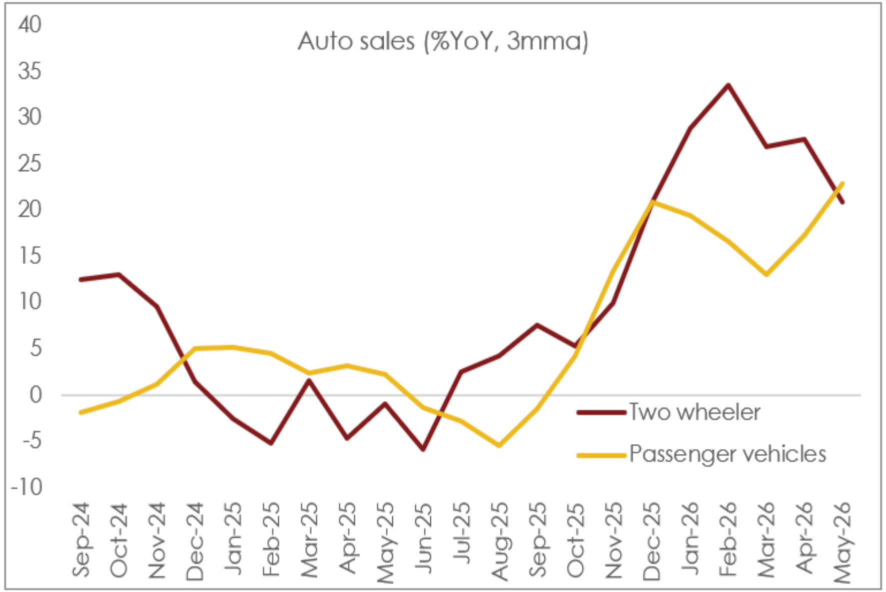


Broad growth momentum however remains stable

E-way bills generated in May-26 rose marginally to 13.6 lakh units compared to 13.3 lakh units in Apr-26, continuing to underscore stability in movement of goods across the country.

Passenger vehicle and two-wheeler sales continue to remain robust. Growth in PVs sales rose to a 27-month high of 27.3% in May-26, while that of two-wheelers recorded a double-digit expansion of 14.9%. Two-wheeler sales remain strong, albeit on a moderating trend now.

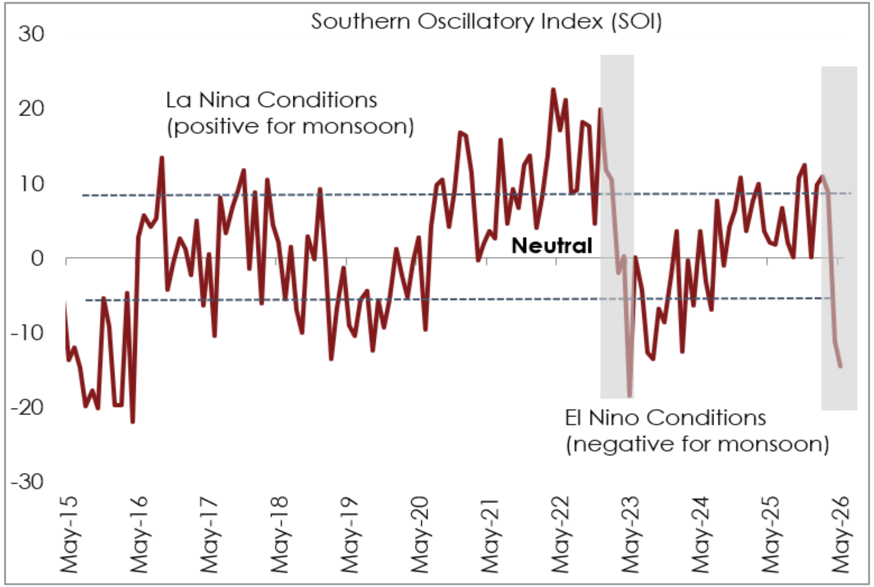


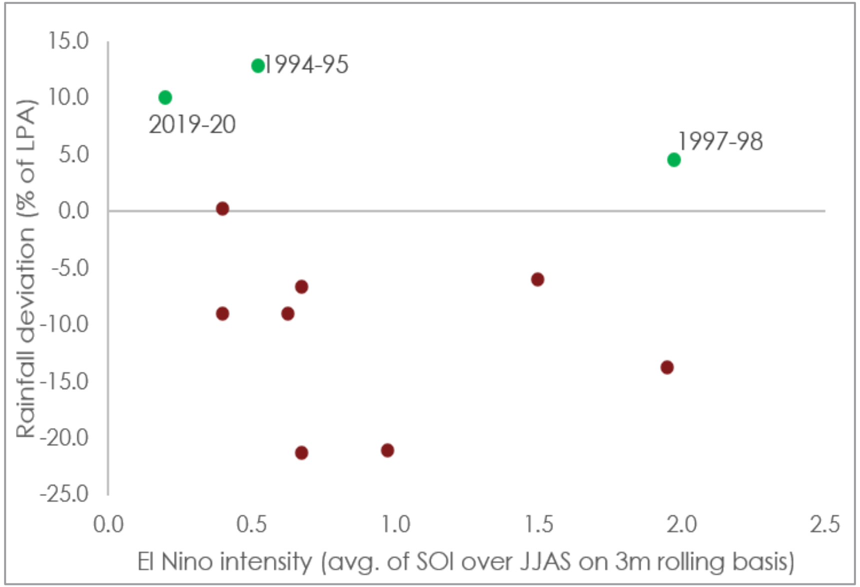


Monsoon deficiency, emerging as a key risk

The South Oscillatory Index (SOI) plunged deeper into negative territory in May-26, validating the presence of El Nino phenomenon globally, which is typically associated with monsoon deficiency in India.

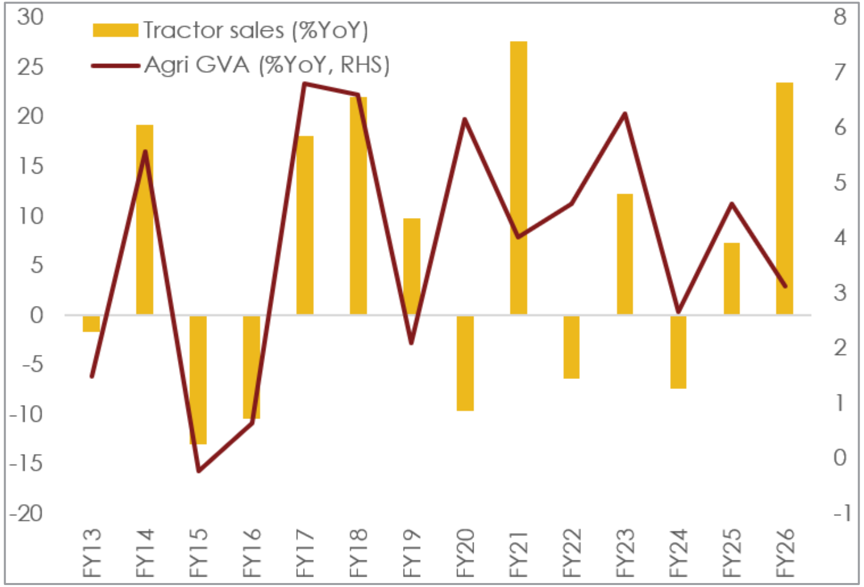
In the past 8 episodes of El Nino, with an exception of 2019-20 (when El Nino had developed late in the year), both Southwest monsoon rainfall as well growth in GVA for crops was seen to be below trend.



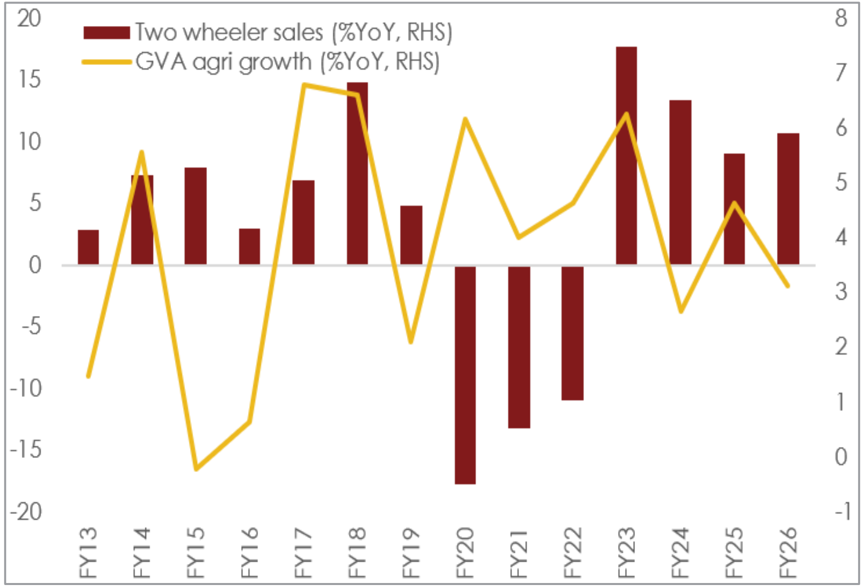


…especially for rural consumption

Historically, agri GVA and tractor sales show a positive correlation, though the relation appears to have weakened post COVID. After growing by 23.5%YoY in FY26, tractor sales could weaken in FY27 amidst rainfall deficiency, hike in tractor prices and rising input costs, particularly those of diesel and fertilizer costs.

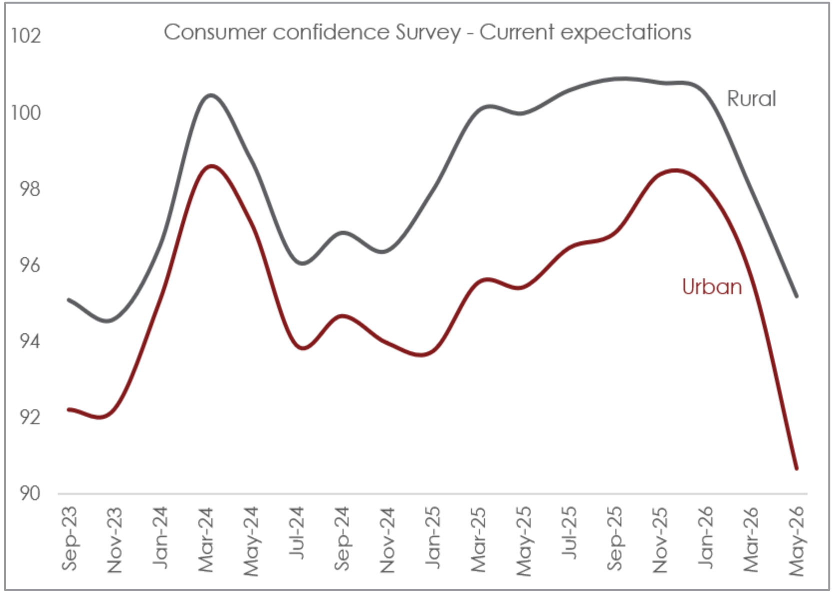


Having grown at a strong pace over 4 consecutive years i.e., FY23-FY26, two-wheeler sales could slowdown in FY27 amidst rainfall deficiency, coupled with an increase in fuel costs, hike in vehicle prices and rise in generalized inflation. The impact could be the highest on entry-level two-wheeler sales.

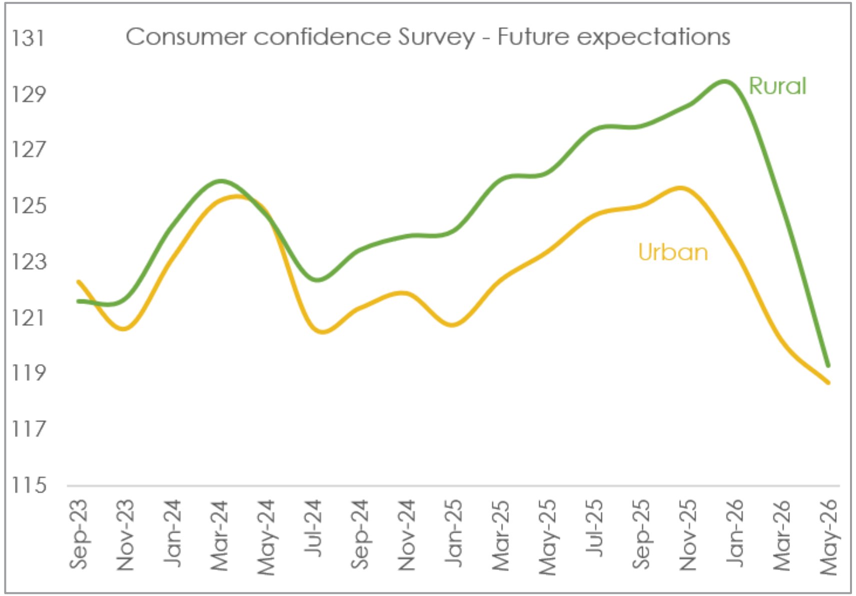


Consumer confidence turns shaky in May-26

Urban consumer confidence, as per RBI's survey, declined for the 3rd consecutive round with the Current Situation Index coming in at 90.7 as of May-26 – the lowest level since Jul-23. This marks the biggest sequential fall since May-21.



Rural consumer confidence, as per RBI's May-26 survey, has already taken a hit even before the onset of the monsoon season. The Current Situation Index (CSI) weakened further to 95.2 – the lowest level since Jan-24, compared to 98.0 in the previous round as of Mar-26.

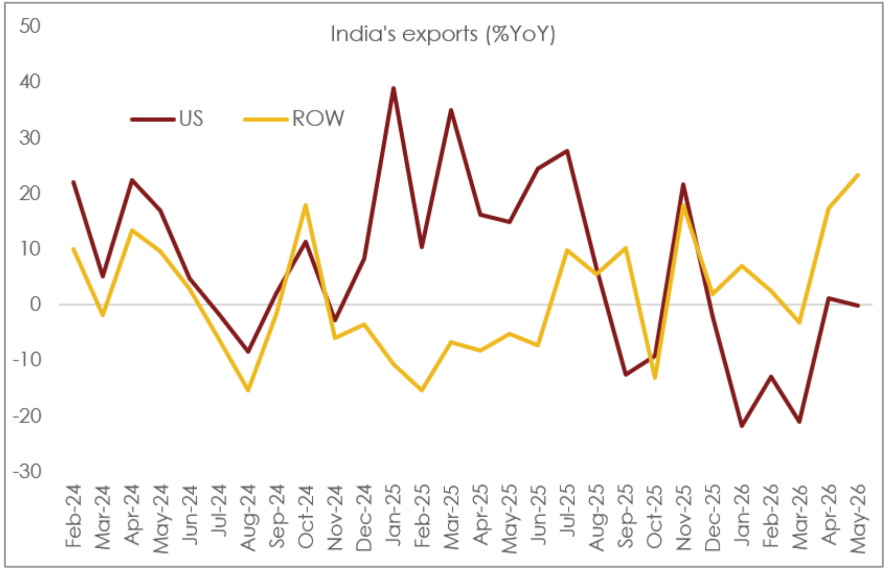


RBI Consumer Confidence Survey, May-26 round, was conducted during 2nd-11th May-26, i.e., before the start of retail fuel price hikes.

Exports hold up owing to geographical diversification

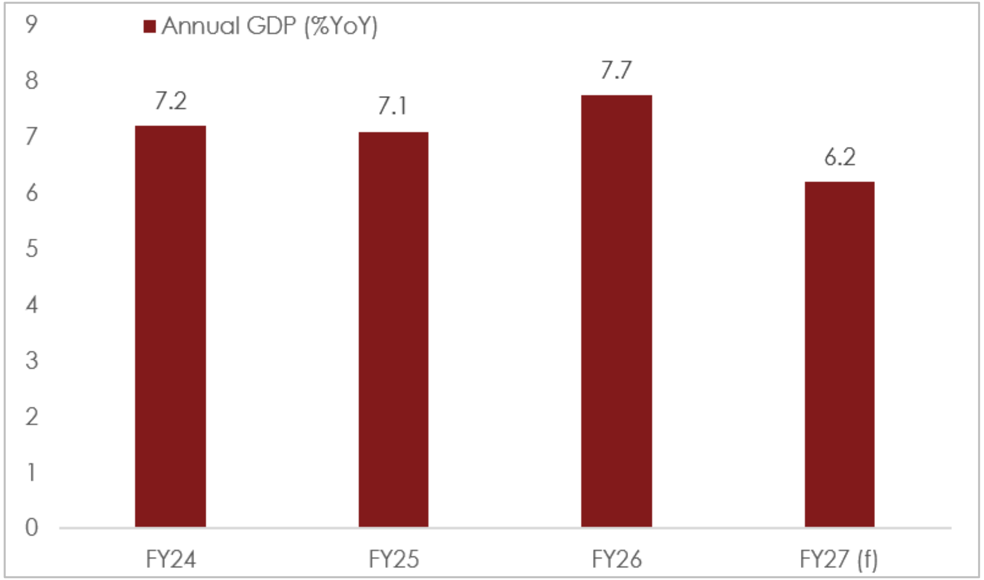
Notwithstanding the moderation in May-26, on a trend basis, PMI export orders continue to recover vis-à-vis recent lows, possibly owing to rationalization of tariffs imposed by US on India. Growth of India's exports to US also appears to have moved past the trough seen in Q4 FY26.

India's exports to Rest of the World (i.e., excluding US) continue to outperform. Geographical diversification is playing a critical role to support export momentum. We notice share of India's exports to South Africa, Singapore, Taiwan, Philippines recording a sizeable increase over the last 1 year.



FY27 GDP growth: Revised up by 20 bps to 6.4%, on lower crude prices expectation

The global geopolitical environment continues to remain fluid. The recently signed MoU between US and Iran, aiming to include a full cessation of hostilities, reopening of the Strait of Hormuz and easing of naval restrictions, offers hope. This has had a positive knee-jerk impact on Brent crude price. From an average of USD ~95 pb in the first two weeks of Jun-26 the Brent is trading lower below USD 80 pb (at the time of writing).



While we believe that crude prices are unlikely to revert to pre-war levels of <USD 70 pb in a hurry (owing to drained inventories, re-building of strategic reserves by countries, pick-up in crude demand from China), the opening of Strait of Hormuz will be watched closely. Working with the assumption of crude price averaging in the range of USD 80-85 pb (vs. USD 95 pb earlier) in FY27 and a 10% deficiency in monsoon, **we revise our FY27 GDP growth marginally by 20 bps to 6.4%.**

WPI surges to a record high (2022-23 series) CPI edges higher, shy of 4.0%

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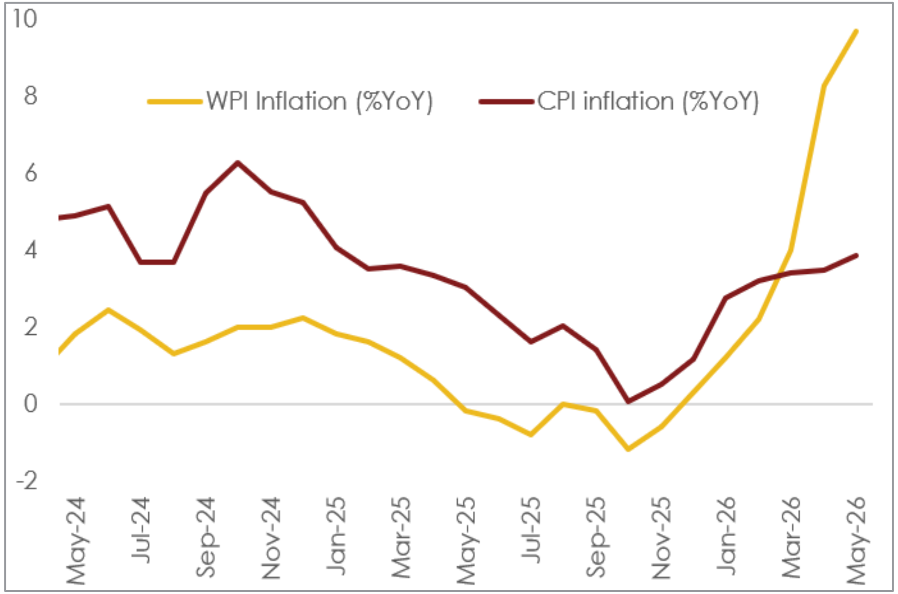
WPI inflation, as per the new series with base year 2022-23, rose to a record high of 9.68% YoY in May-26, from an elevated level of 8.62% in Apr-26. The upside was led by 30.3%YoY gain in Fuel & light inflation along with manufacturing inflation that climbed to 7.48% in the month.

In comparison, CPI inflation edged higher to 3.9% in May-26, from 3.5% in Apr-26, beginning to reflect partially the direct and second-order impact of fuel hikes, along with sequential increase in select food prices amidst severe heatwaves.

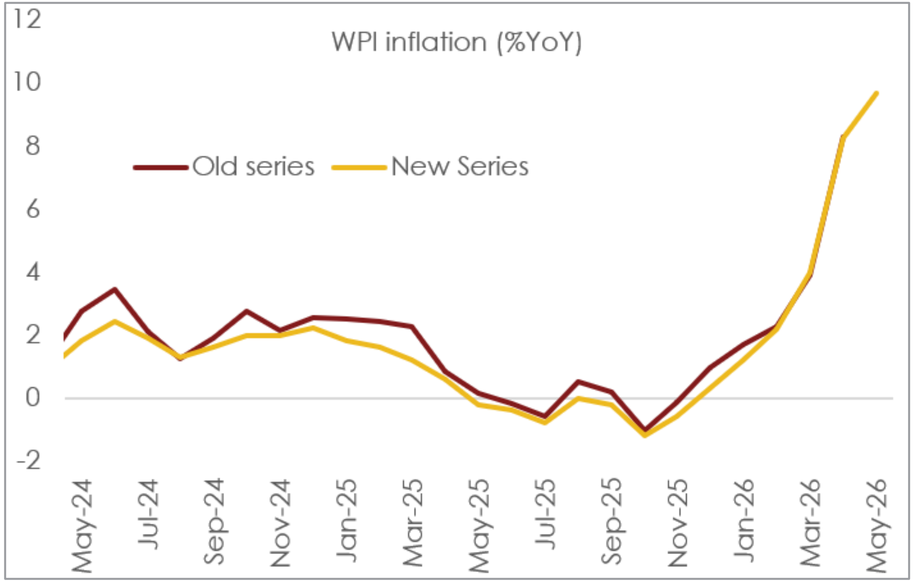


CPI Inflation (%MoM)			
Sub-category	**Mar-26**	**Apr-26**	**May-26**
Food & Beverages	0.24	0.22	0.87
Paan, Tobacco & Intoxicants	0.87	0.85	0.47
Clothing & Footwear	0.25	0.43	0.53
Housing, Water, Electricity, Gas & Other Fuels	0.59	0.16	0.25
Furnishings, HH Equipment & Routine HH Maintenance	0.25	0.45	0.49
Health	0.11	0.14	0.13
Transport	0.04	0.11	1.87
Information & Communication	0.09	0.16	0.18
Recreation, Sport & Culture	0.13	-0.16	0.05
Education Services	0.07	0.46	0.27
Restaurants & Accommodation Services	0.36	1.55	1.78
Personal Care, Social Protection & Misc	-0.27	-0.07	1.22

New WPI series, but with only 5 years shelf life

The new WPI series (base 2022-23) incorporates methodological improvements (computational as well as estimation of weights) and wider coverage of items (957 now vs. 697 under the old series). The same has been made available from Apr-23 onwards.

The 2022-23 upgrade, will be the last WPI revision, that will continue over the next 5 years. Thereafter, WPI will cease to exist, and will be completely replaced by output PPI (Producer Price Index) – in line with global best practises.



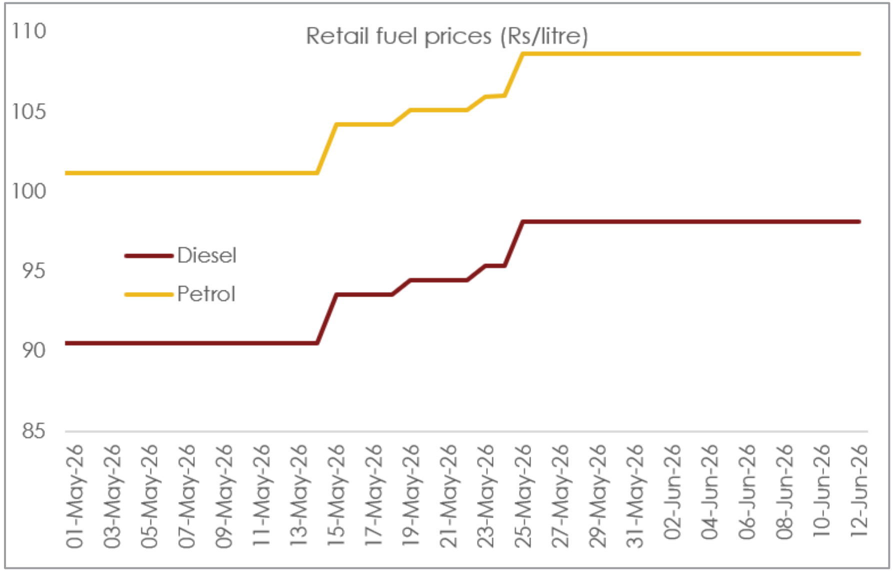
Divisions	Weights in major groups of WPI	
	Old series	New series
WPI	100.00	100.00
Primary articles	22.62	22.76
Food & Light	13.15	14.11
Manufacturing	64.23	63.13

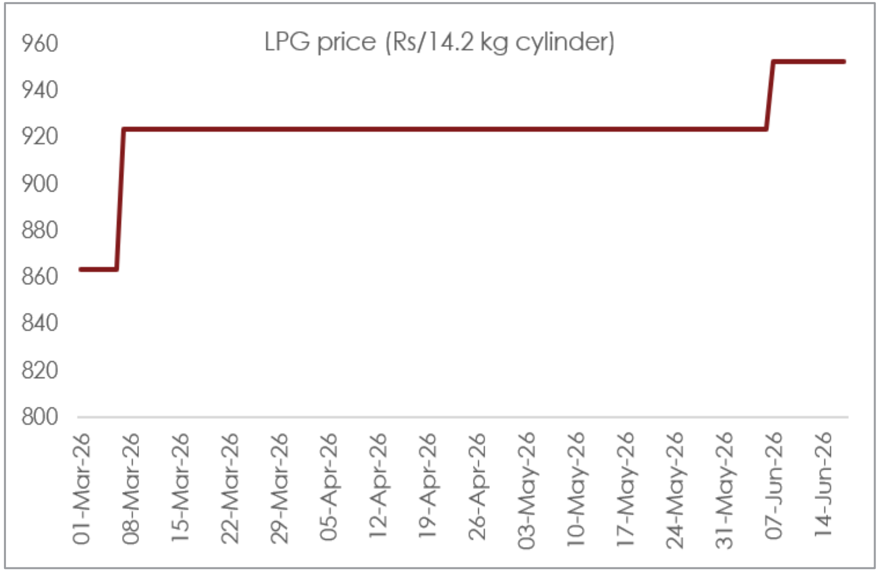
Divisions	No. of items in major groups of WPI	
	Old series	New series
WPI	697	957
Primary articles	115	129
Food & Light	18	25
Manufacturing	564	803

CPI Inflation: First order impact getting palpable…

The partial impact of ~Rs 7.5 per litre increase in petrol and diesel price announced beginning mid-May-26 in four tranches, added ~15 bps to headline CPI inflation in May-26. Another 15-20 bps is expected to reflect in Jun-26 CPI reading.

In similar vein, the Rs 29 hike announced for domestic LPG cylinder in early Jun-26, will add ~5 bps to headline inflation directly.

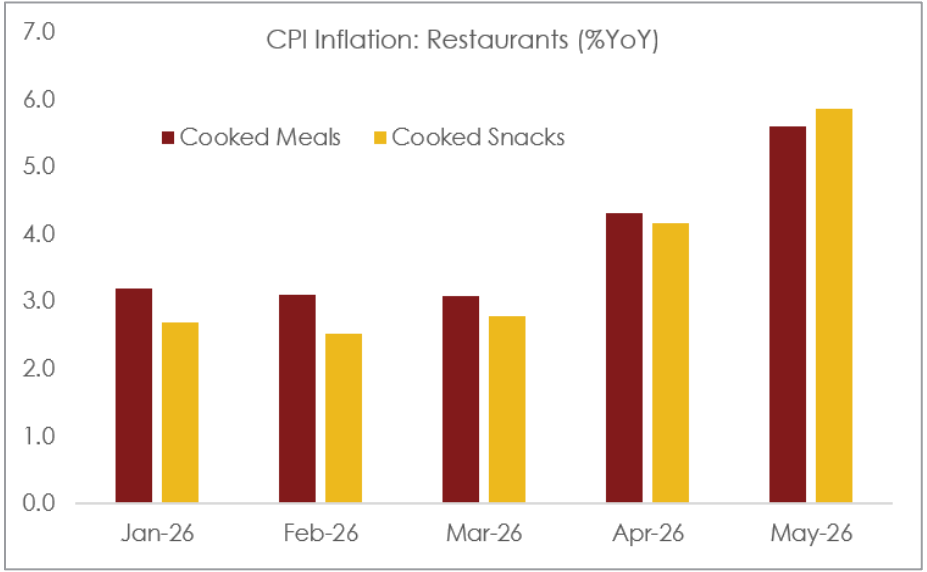


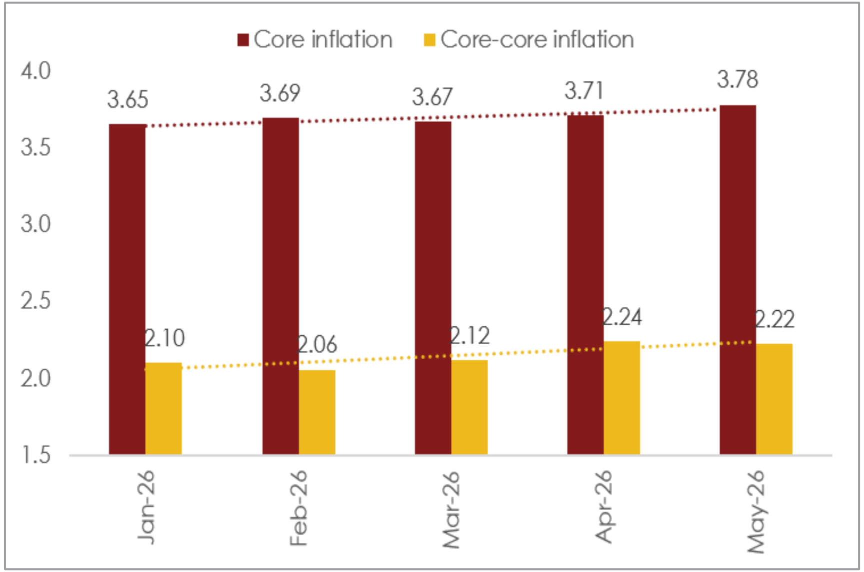


...along with second-order impact

The steep hike in commercial LPG cylinder price, by close to 80% since Mar-26, is being passed on to consumers, as seen in sharp escalation in CPI for restaurants, under the category of both cooked meals and cooked snacks.

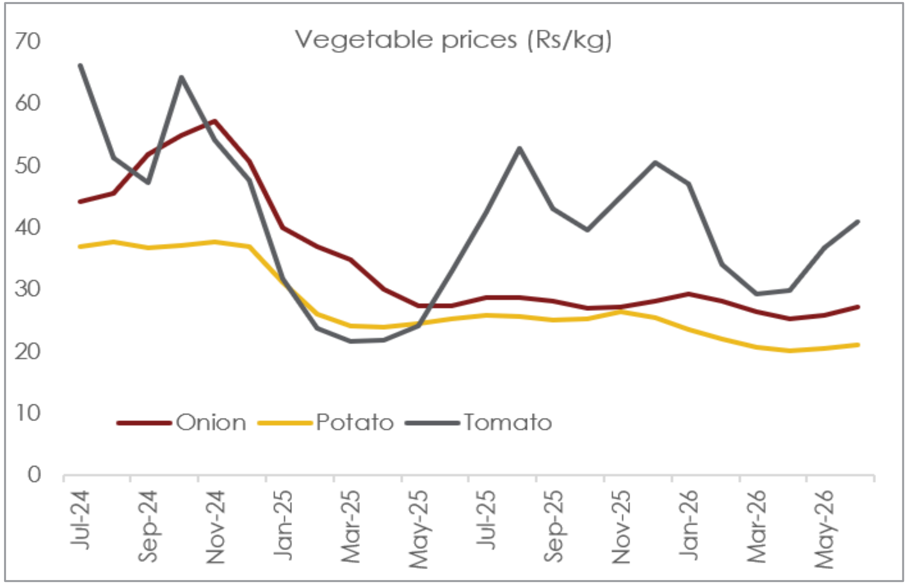
Core and core-core inflation have both begun to trend higher over the last three months, capturing the second-order impact of energy price changes.



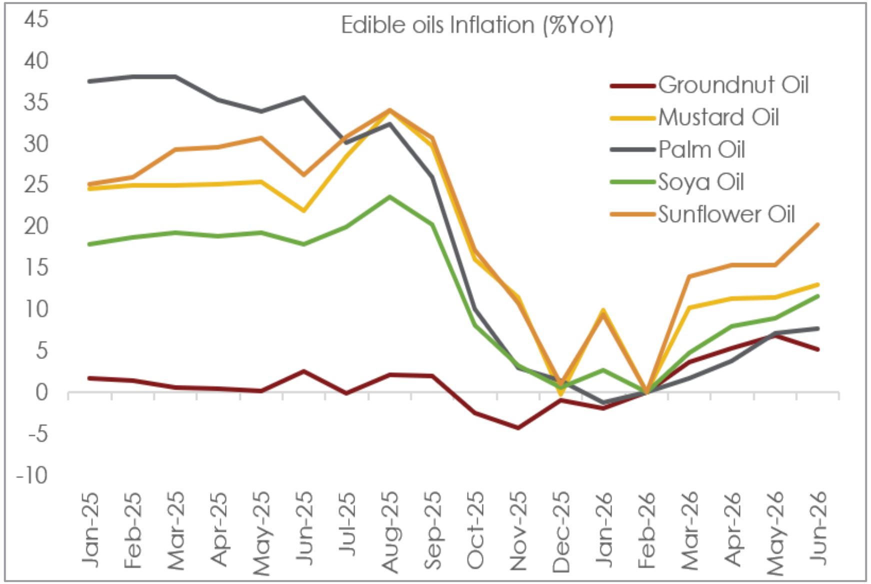


Food price pressures building up

Summer heatwaves, accentuated by El Nino, are weighing on price of perishables. Select vegetables (such as tomato, cauliflower) and milk prices have seen an escalation.



Price of edible oils continues to firm up, led by Sunflower oil - reflecting possibly higher global freight rates and Rupee depreciation impact. A sub-normal monsoon could weigh on domestic oilseeds' production, thereby exacerbating price pressures.

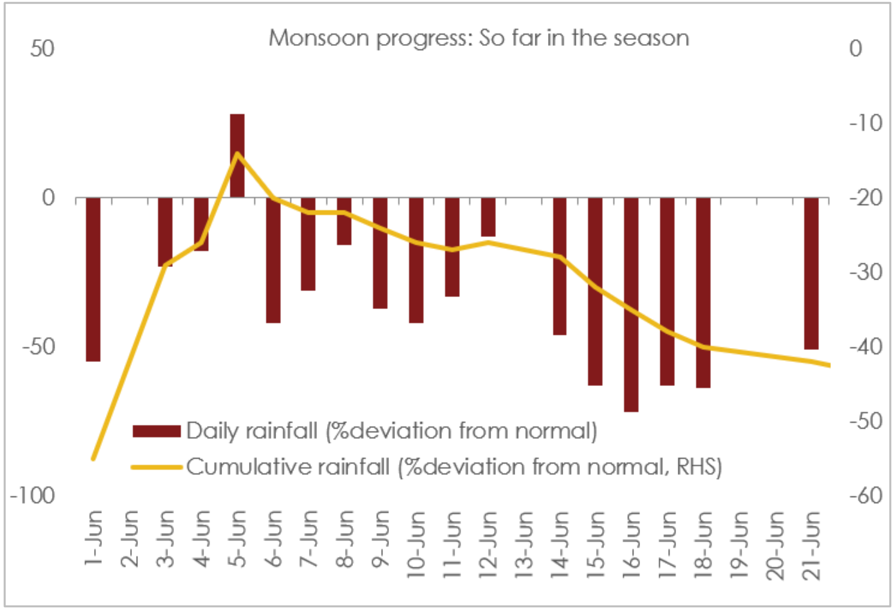


Delayed onset, slow progress of monsoon in Jun-26 remains worrying

Southwest monsoon made landfall in Kerala on 4th Jun-26, three days after its normal onset date of 1st Jun-26 and nearly a week later than the IMD's earlier forecast of 26th May-26.

Since then, the advancement has been slow, clocking a cumulative deficiency of 42% below normal as of 23rd Jun-26.

Southwest Monsoon Onset Date			Gap (in days)
Year	Actual	Forecast	
2018	29-May	29-May	0
2019	08-Jun	06-Jun	2
2020	01-Jun	05-Jun	-4
2021	03-Jun	31-May	3
2022	29-May	27-May	2
2023	08-Jun	04-Jun	4
2024	30-May	31-May	-1
2025	24-May	27-May	-3
2026	04-Jun	26-May	9



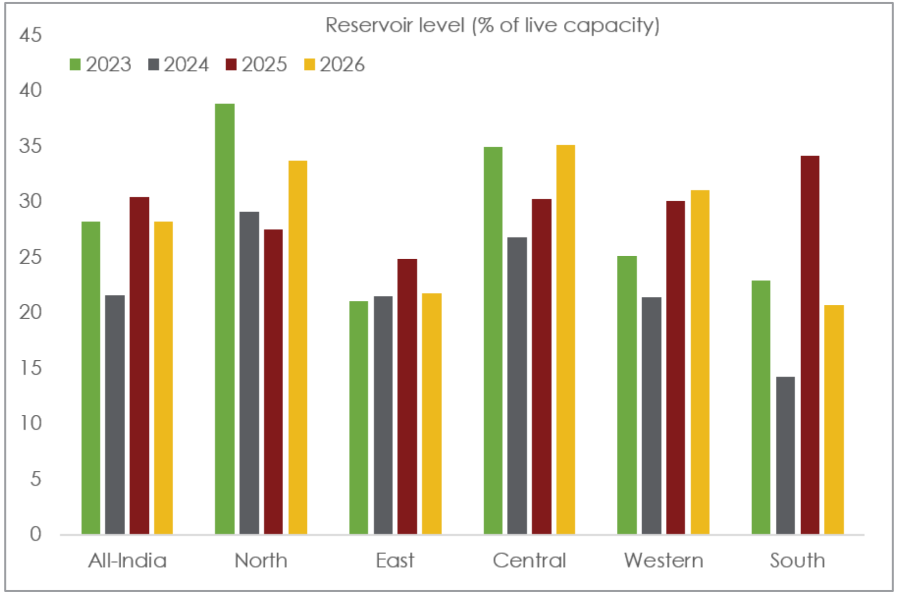
Kharif sowing onto a slow start, Reservoir levels depleting fast

The start of the sowing season for Kharif crops has been on a subdued note, unsurprisingly owing to the late onset and slow progress of monsoon, so far in Jun-26. For all the crops, area sown as of 19th Jun-26, stood 1.6% higher on an annualised basis.

Amidst a slow progress of monsoon in Jun-26 so far, reservoir levels have slipped in recent weeks. As of 18th Jun-26, current capacity as a % of total capacity stood at 27.7%, lower than 34.3% as of end May-26 as well as 31.8% a year ago. In terms of geographical spread, the widest gap vis-à-vis last year's levels, is seen for Southern India.

Progress of area coverage under Kharif crops as on 19th Jun-26

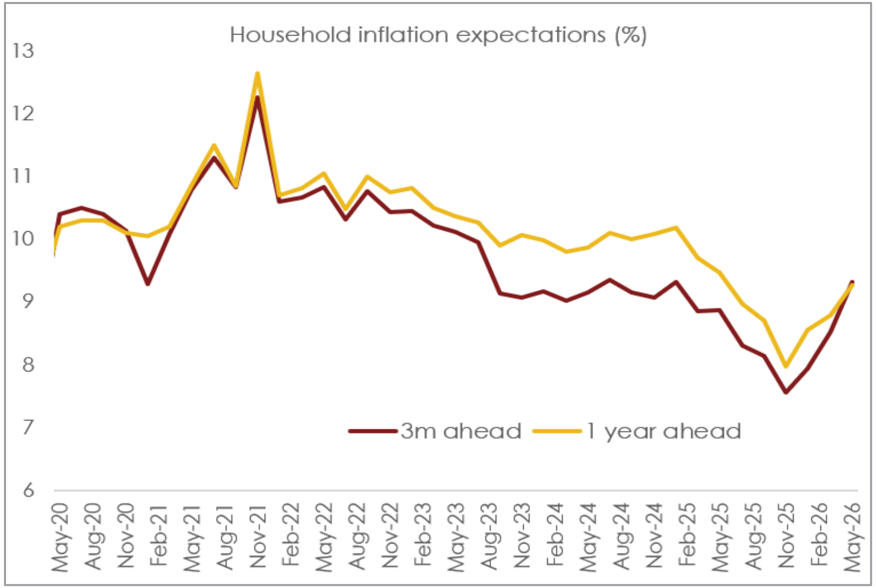
Crop	2025	2026	%YoY
Rice	8.09	12.36	52.8
Pulses	6.39	7.21	12.8
Coarse cereals	9.82	12.43	26.6
Oilseeds	8.11	7.24	-10.7
Sugarcane	56.64	57.31	1.2
Jute & Mesta	6.09	6.22	2.1
Cotton	22.82	17.13	-24.9
Total	**117.96**	**119.9**	**1.64**

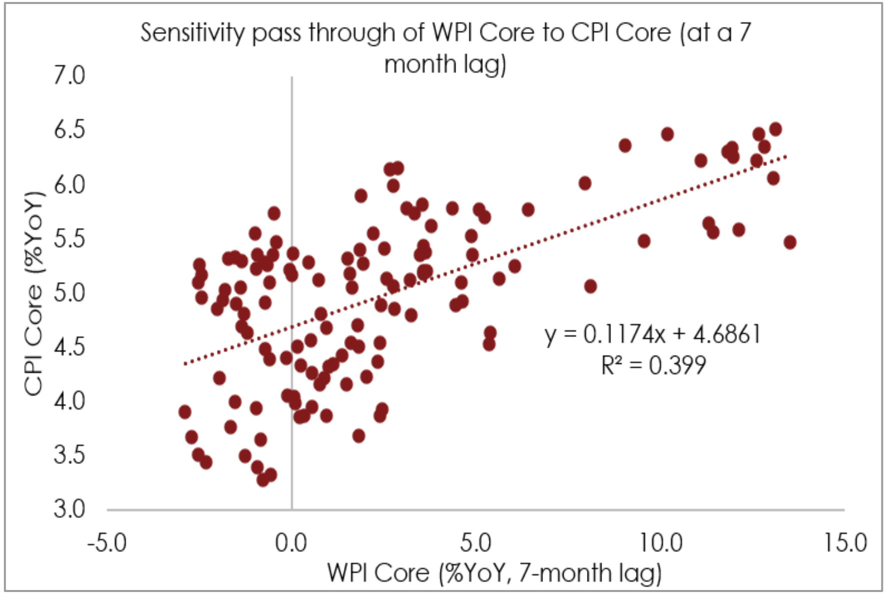


Core CPI to adjust upwards with a lag

As per RBI's Inflation Expectations Survey, 3m and 1 yr ahead median inflation perception of households rose by 80 bps and 50 bps respectively, reaching 9.3% for both – the highest level since Mar-25 and Jul-25 respectively.

The firming up of input cost accompanied by depreciation in Rupee on an annualised basis, along with hardening of inflation expectations is likely to see a stronger pass-through to core inflation in coming months. Our sensitivity analysis does validate a reasonable pass-through from WPI core to CPI core inflation, albeit with a two-quarter lag

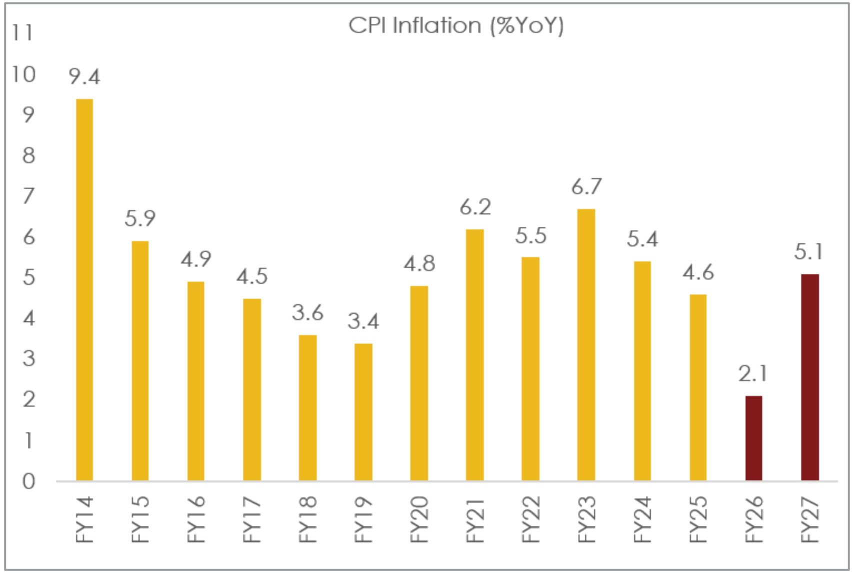




FY27 CPI forecast revised lower to 5.1%

Keeping in mind the anticipated 10% shortfall in Southwest monsoon, hardening of food prices that has already begun, delayed pass-through of higher energy price in May-Jun-26, as well as input costs to consumers (amplified by 10%YoY depreciation in Rupee), we believe that FY27 CPI inflation is likely to see a sizeable upside vis-à-vis 2.1% in FY26

- However, the softening of crude prices to below USD 80 pb post the US Iran MoU, prompts us to revise our FY27 global crude price outlook lower to USD 80-85 pb, vis-à-vis USD 95 pb earlier.
- We also do not expect the Government to cut petrol or diesel prices in H1 FY27.
- **Taking on board these assumptions, we have revised our FY27 CPI inflation lower to 5.1% from 5.5% earlier.**



Snapshot of April FY27 fiscal performance

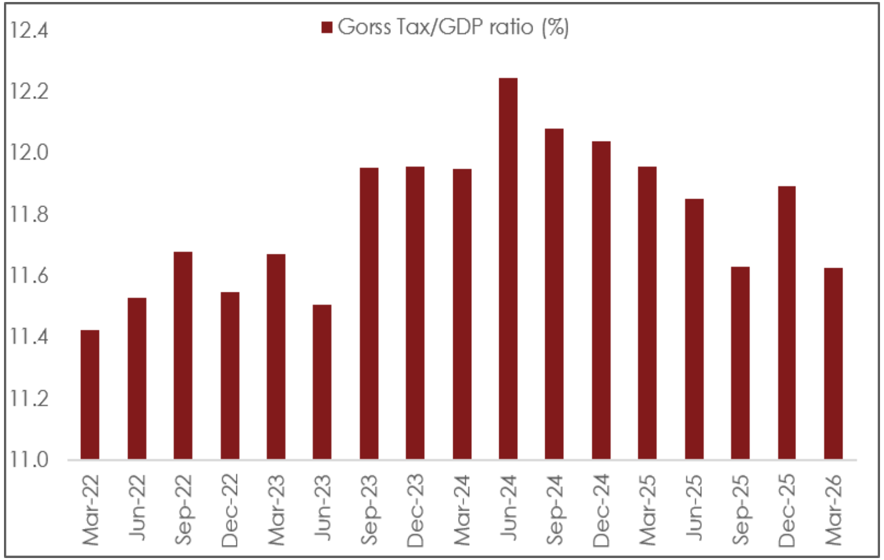
The fiscal deficit for April FY27 stood at 21.4% of the budget estimate (BE), much higher than 12.3% of actuals in April FY26. This is due to a relatively low realization across all major receipt types, even as the pace of both revex and capex disbursements picked up.

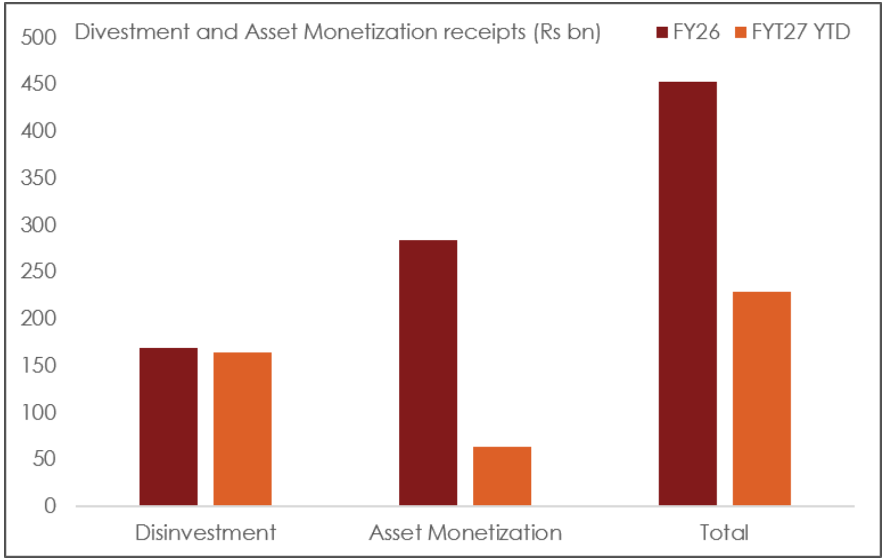
Key Fiscal Variables (Cumulative position, as of April)				
	% of FY Actual/Target		%YoY	
	FY26 YTD	FY27 YTD	FY26 YTD	FY27 YTD
Revenue Receipts	7.8	5.7	21.0	-21.0
Net Tax	7.2	6.2	2.5	-5.9
Non-Tax	9.9	3.6	146.1	-63.8
Non-Debt Capital Receipts	26.8	8.4	2057.4	-55.9
Total Receipts	**8.2**	**5.8**	**30.9**	**-23.8**
Revenue Expenditure	8.0	9.3	-5.7	25.9
of which, Interest Payments	*7.5*	*7.8*	*-27.1*	*17.2*
of which, Major Subsidies	*6.4*	*10.6*	*49.2*	*50.7*
Capital Expenditure	14.9	15.5	61.0	18.8
Total Expenditure	**9.5**	**10.8**	**10.0**	**23.5**
Fiscal Deficit	**12.3**	**21.4**	**-11.3**	**94.4**

Tax revenue moderates, but other forms of revenue could support

On a 4q rolling basis, gross tax revenue (GTR) slipped to 11.6% of GDP in Q4 FY26. GTR has made a subdued start in FY27, with April clocking -1.9% YoY, largely due to slow traction in GST revenue realization. Various tax relief measures announced in FY27 (excise, customs, WHT, capital gains) so far will result in tax collection undershooting the BE.

On the other hand, other forms of revenue are showing improvement. The RBI transferred a record high dividend of Rs 2866 bn to the government, which is estimated to be modestly higher than the BE. Additionally, the disinvestment/asset monetization run rate in FY27 so far has raised the likelihood of overshooting the BE.

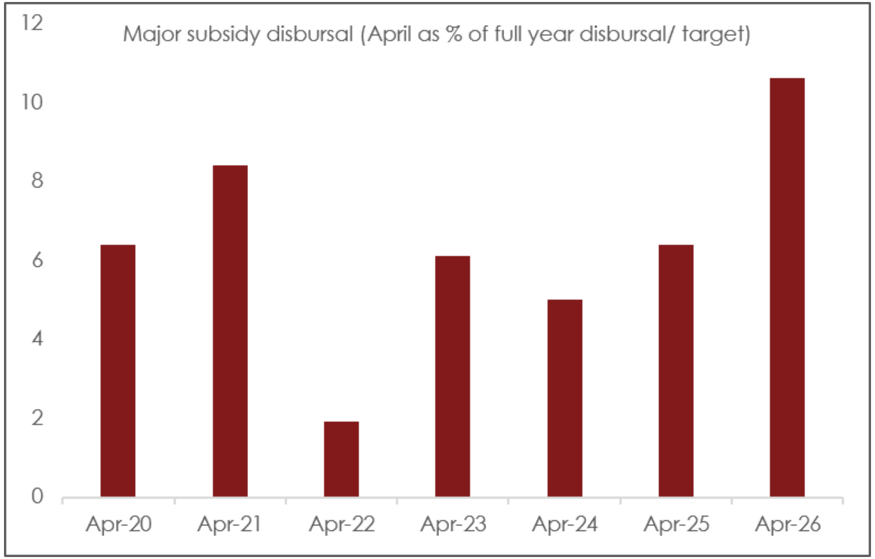


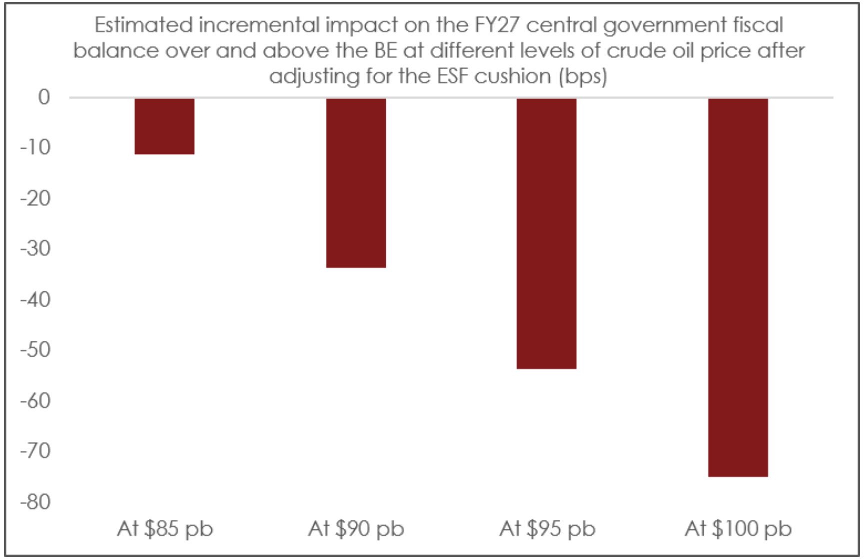


Meeting the FY27 target will require expenditure calibration

For Apr-26, the subsidy disbursal stood at its highest level in the last 7 years. Fertilizer subsidy is likely to exceed its BE by a fair margin, while food and petroleum subsidy could also witness a moderate overshooting. However, if the US-Iran peace deal results in a durable de-escalation of Middle East tensions, then the incremental subsidy burden could be modest.

Fiscal risks in FY27 could be partially addressed by the Economic Stabilization Fund (having a corpus of Rs 1 tn) and a marginally higher RBI dividend. The FM has reiterated her commitment to meet the fiscal deficit target of 4.3% of GDP. Meeting the headline FY27 fiscal target would require expenditure rationalization in H2.





G-secs recoup their FYTD loss

The 10Y g-sec yield has corrected by 16 bps since the RBI policy review on Jun 5th and is currently trading around 6.80% levels, the lowest in FY27 so far.

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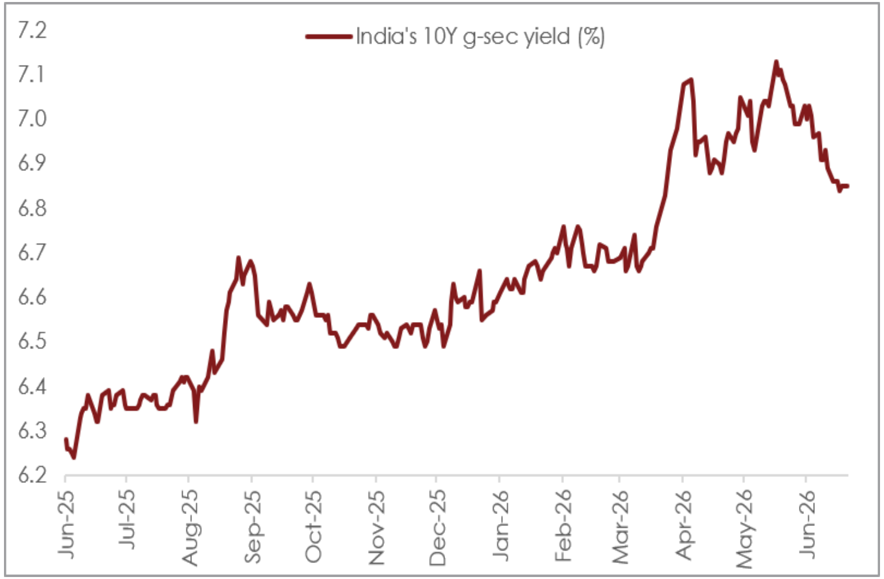
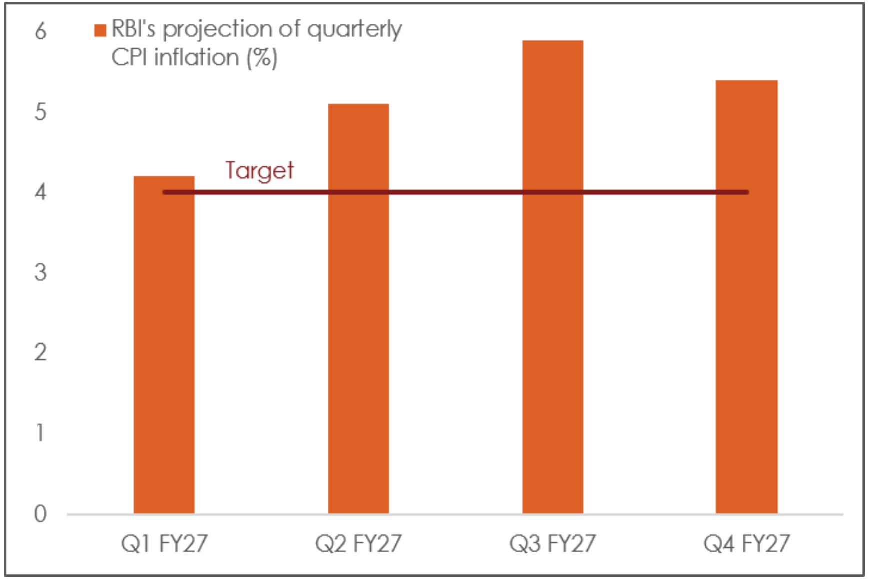
Although the RBI projected average CPI inflation at 5.5% over Q2-Q4 FY27, the urgency to use monetary policy to stem inflationary pressures has abated after the announcement of BoP supportive measures and the recent correction in crude oil prices

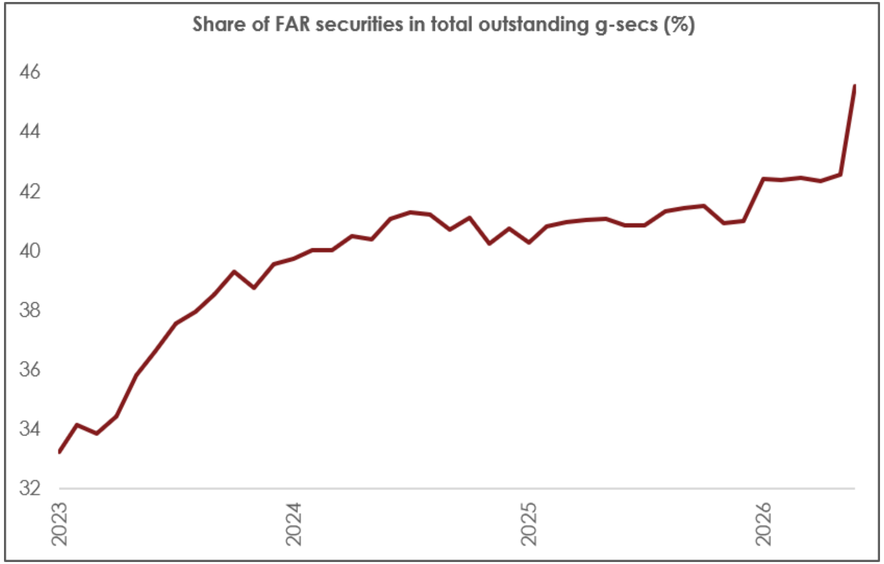


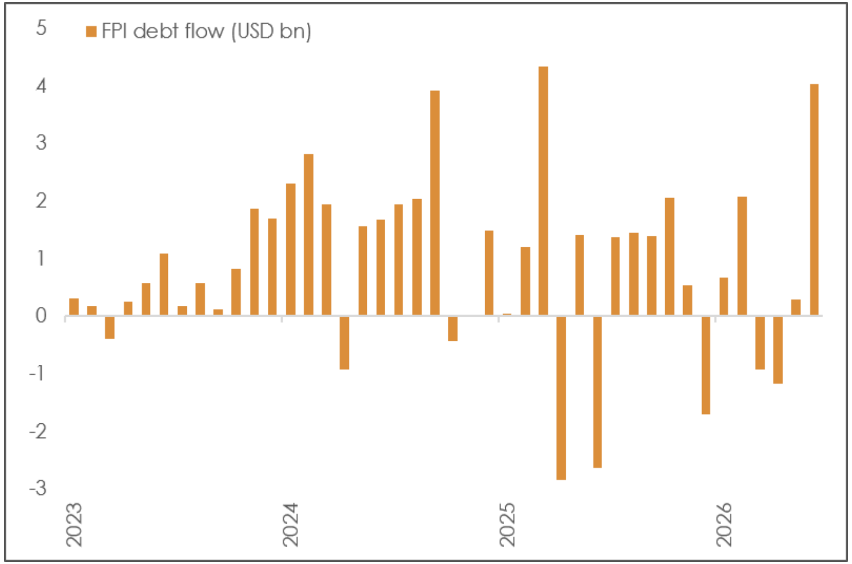


Decisive policy support aids sentiment

From a bond market perspective: (i) the removal of capital gains/ withholding tax on g-sec investments by FPIs, (ii) the widening of the FAR (Fully Accessible Route) basket by inclusion of fresh issuances of 15Y, 30Y, and 40Y securities, (iii) and the removal of limits on short-term investment, concentration and individual securities on FPI investment under the General Route, has turned sentiment positive.

As a result, debt investment by FPIs has shot up to USD 4.2 bn in Jun-26 so far, the highest in 15 months. With INR stability and declining hedging costs, FPI debt investments could remain supportive in the near term.

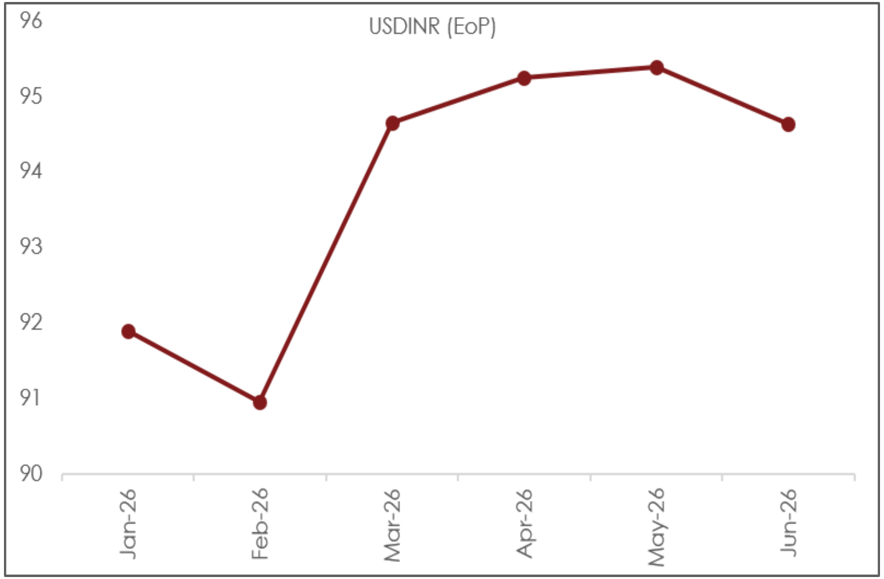


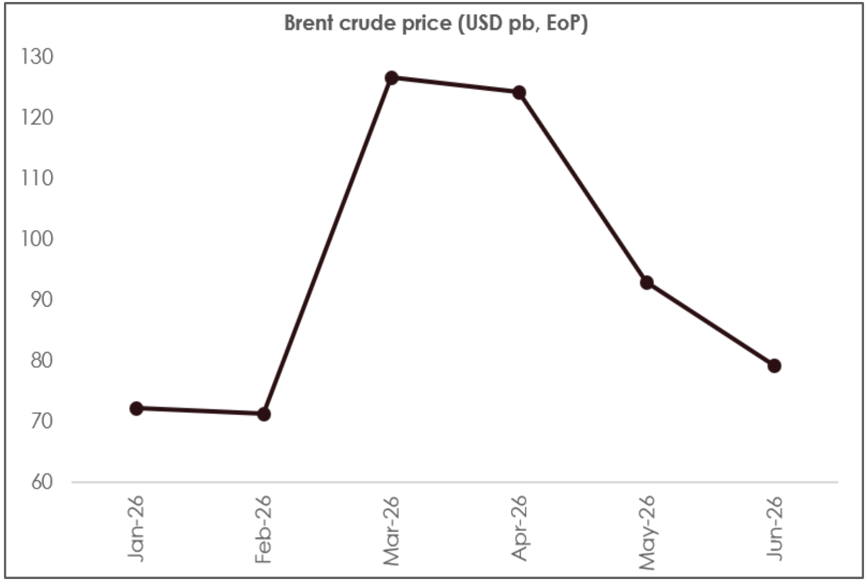


Meanwhile, global concerns ease

The combination of BoP-supportive measures unveiled by the GoI-RBI provided relief to the INR. The currency is currently trading around 94.7 levels, similar to the levels seen in end Mar-26.

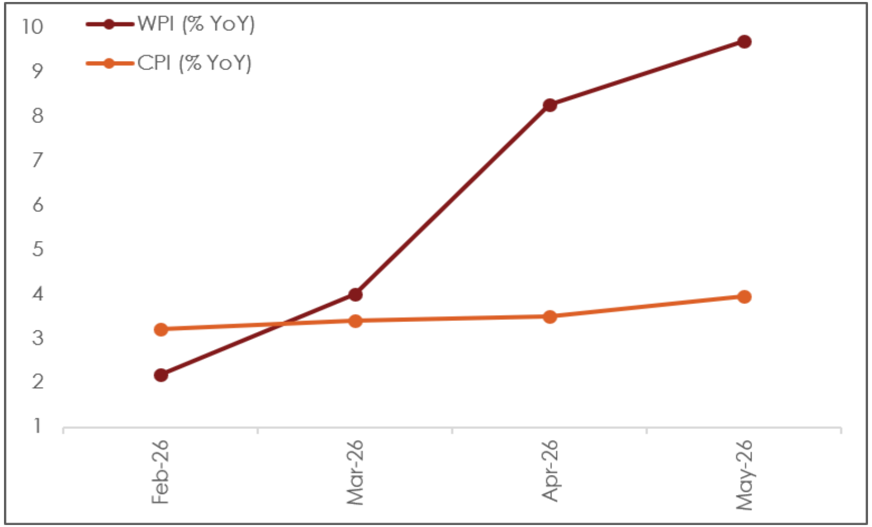
The signing of the US-Iran MoU has de-escalated the Middle East tensions for now. Both countries are expected to formalize this into a peace deal within the next 60 days by addressing mutual concerns diplomatically. The price of Brent crude has corrected sharply to USD 80 pb levels.



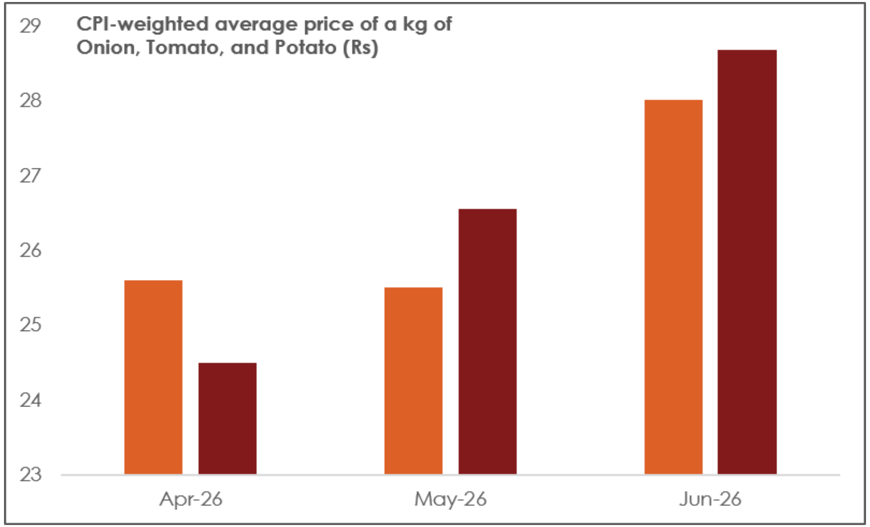


However, inflation risks continue to loom…

WPI inflation has accelerated from 2.2% YoY in Feb-26 to 9.7% in May-26 on account of a sharp rise in energy prices, along with other commodities like chemicals, rubber & plastics, textiles, basic metals, wood products, etc. In comparison, the rise in CPI from 3.2% YoY in Feb-26 to 3.9% in May-26 appears moderate.



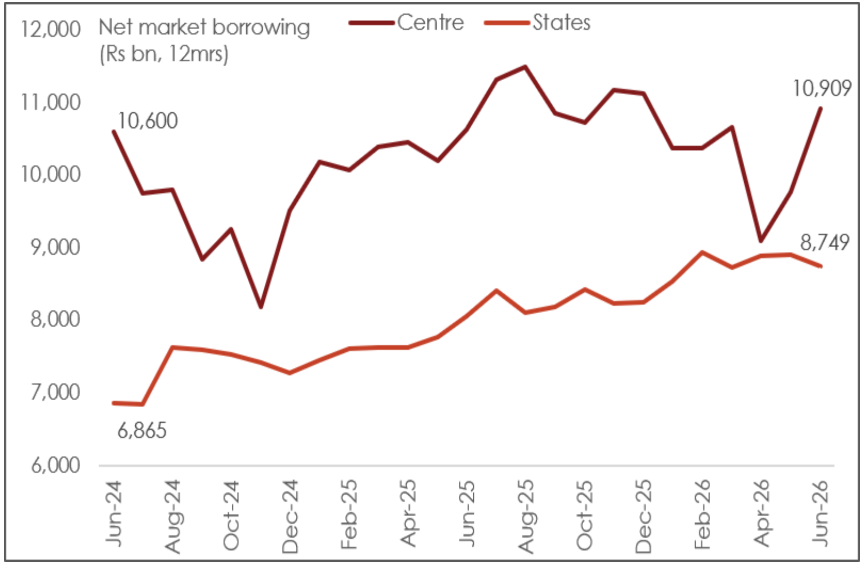
However, CPI inflation is expected to pick up sharply in H2 FY27 on account of monsoon deficiency and GST-related unfavourable statistical base effect. Early indicators show price pressures for food items are building up.



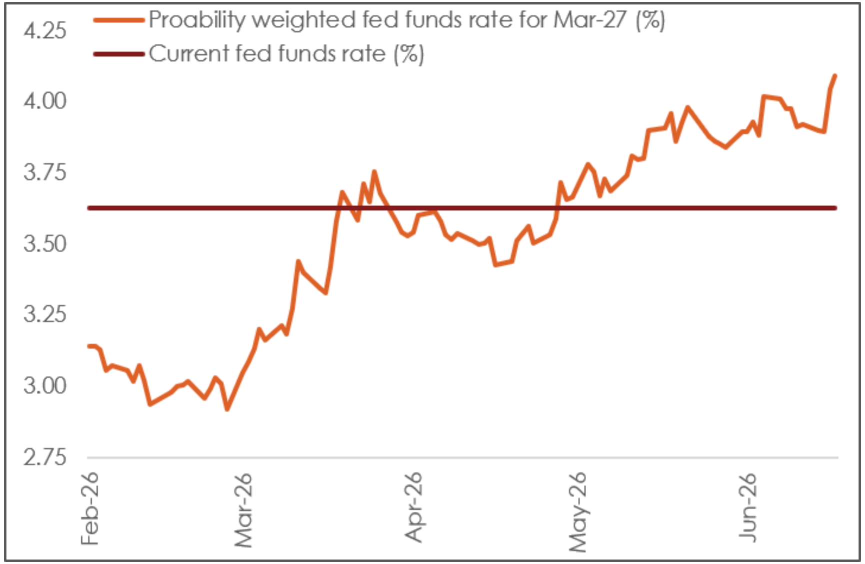
With both headline and core inflation projected to move up in H2 FY27, we see scope for a 25-50 bps rate hike in H2 FY27 to normalize the real interest rate, which otherwise would appear excessively low.

And so do supply risks and global rates outlook

In the last 2 years, while g-sec issuances have been broadly stable (net annualized issuance has become just 1.03x), it has picked up for SDLs (net annualized issuance has become just 1.27x). As per provisional accounts, while the central government consolidated its fiscal deficit by 50 bps to 4.4% in FY26, for states, the cumulative fiscal deficit widened by 30 bps to 3.3%.



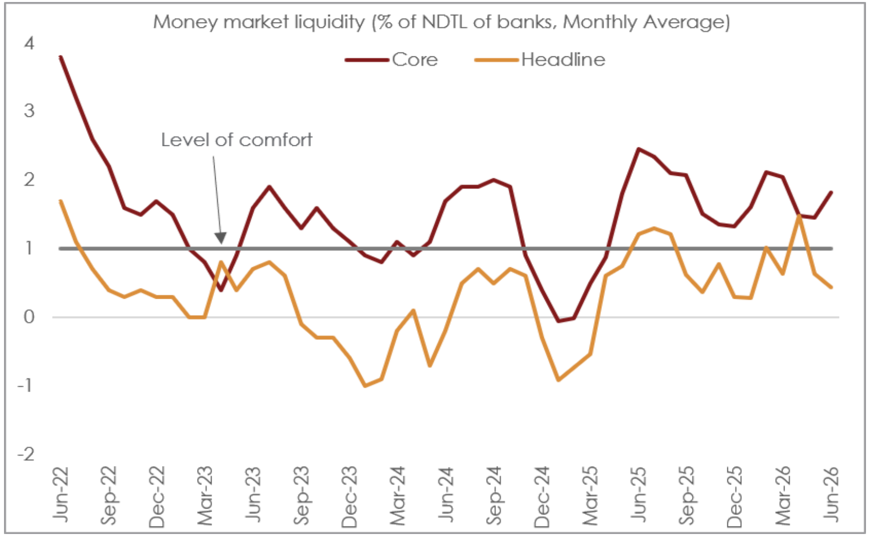
The US fed funds futures market is pricing in 2 rate hikes from the Federal Reserve by Mar-27 on underlying strength in the economy, along with rising inflationary pressures. It should be noted that the recent slide in crude oil prices has not impacted the market expectation of the projected fed rate trajectory much.

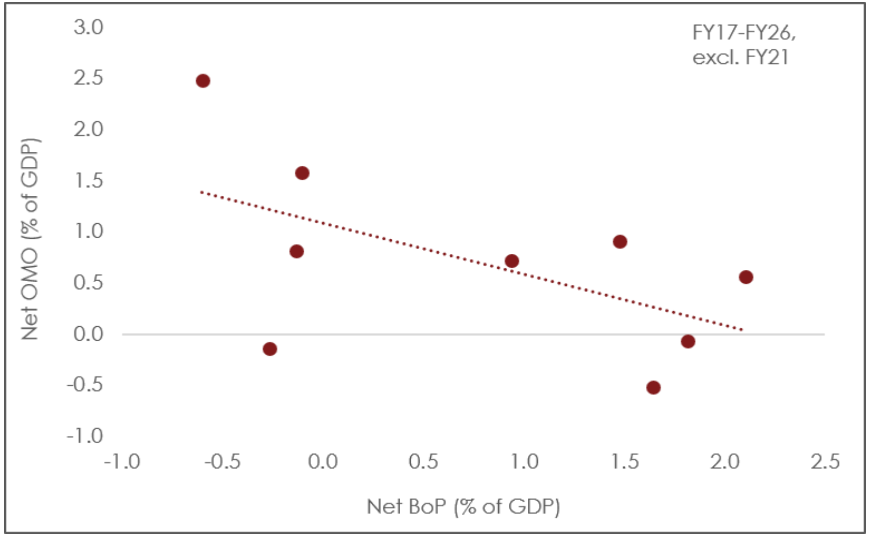


Rates outlook

The recent policy interventions to support the BoP will significantly augment domestic liquidity. With BoP projected to have a surplus of USD 70 bn, vis-à-vis the expectation of a neutral position earlier, we now see core liquidity in the Rs 9-10 tn range by Sep-26, before it moderates towards Rs 7 tn by Mar-27.

Excess liquidity surplus will obviate the need for RBI to carry out OMO purchases in FY27 (for reference, RBI conducted a net OMO purchase of Rs 8.8 tn in FY26, which effectively mopped up ~81% of net g-sec supply).



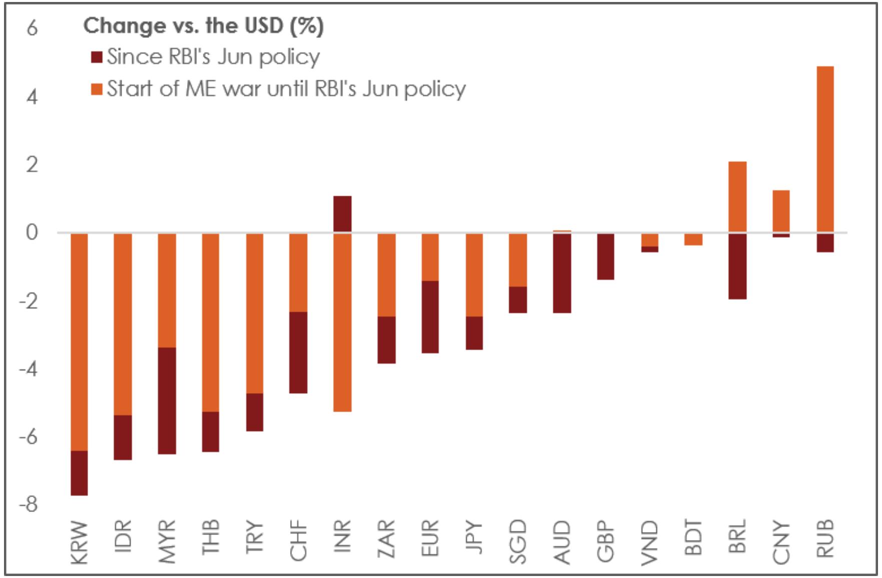


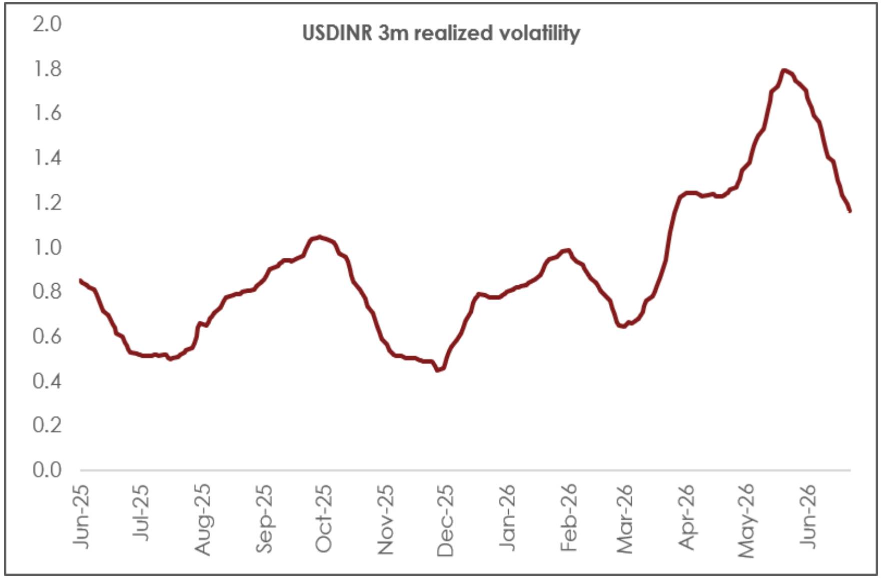
We expect the 10Y g-sec yield to remain supported in the near term (6.75% by Sep-26), before it inches up towards 7.25% by Mar-25 on domestic and global monetary tightening and focus on fiscal concerns later in the year.

INR posts a relief rally

INR had weakened by 5.3% since the start of the Middle East crisis until the RBI's Jun 5th monetary policy review. During this period, INR was one of the worst-performing currencies amongst its major peers. However, since the policy review, INR has strengthened by 1.1% and emerged as the best-performing currency amongst major peers.

After peaking in May-26, INR volatility has moderated, especially following the announcement of BoP-supportive measures by the GoI and the RBI.





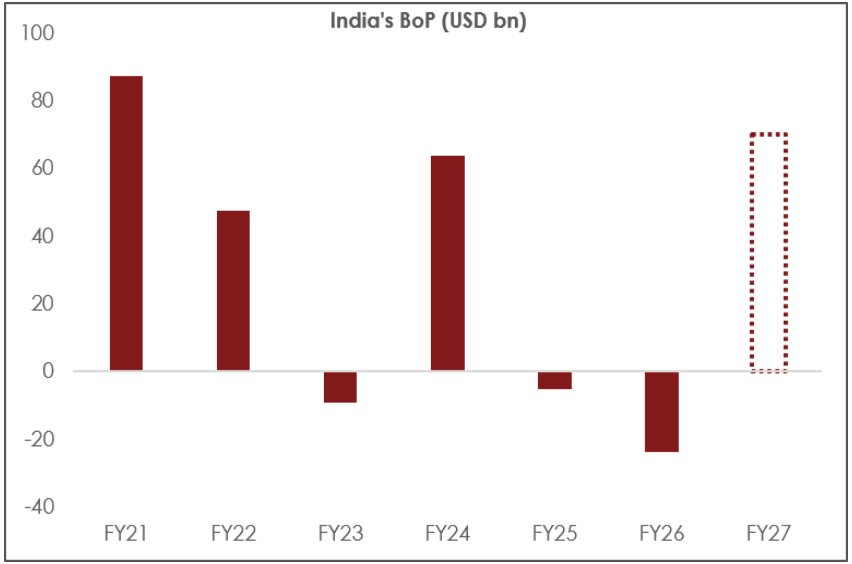
Policy intervention changes the BoP outlook

RBI came out with a series of measures on Jun 5th to incentivize capital flows. In addition, the GoI, besides taking steps to curb the pressure on CAD (import duties on precious metals and hike domestic fuel prices), provided tax relief to FPI investors on their g-sec investments.

With coordinated steps taken to address both the current and capital accounts, we now estimate FY27 CAD and BoP at 0.9% of GDP and USD 70 bn surplus.

Key policy announcements to augment capital flows

For	Measure	Time
G-Secs	Fresh issuance of 15Y, 30Y, 40Y g-secs included under FAR. Limits on short-term investment, concentration and individual securities on FPI investment under General Route removed.	Structural
Equities	Increased investment limits by NRIs/OCIs in equity instruments traded on the stock market without SEBI registration.	Structural
ECBs	Concessional forex swap provided for PSUs and Banks	Till Dec 31, 2026
FCNR(B) Deposits	Concessional forex swap provided to AD banks for raising fresh 3–5Y FCNR(B) deposits	Till Sep 30, 2026
Export Proceeds	Restored time for realization of export proceeds to 9m from 15m	One-time

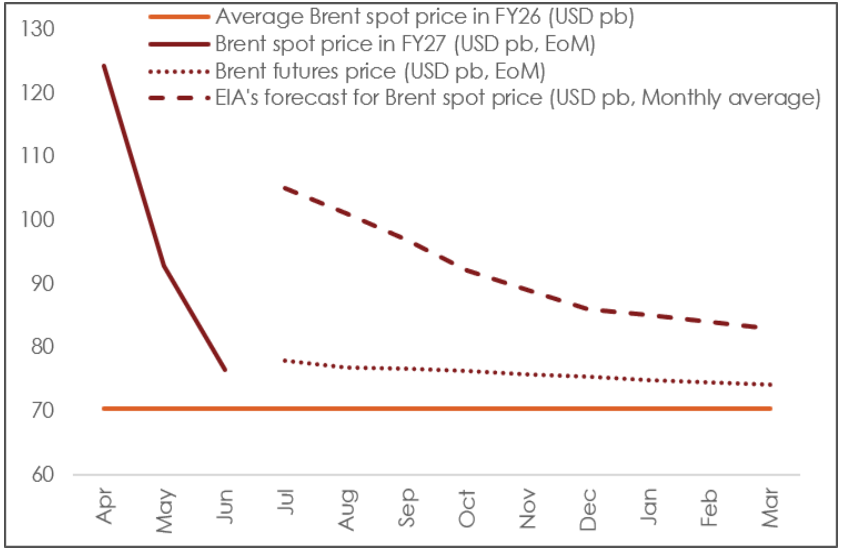


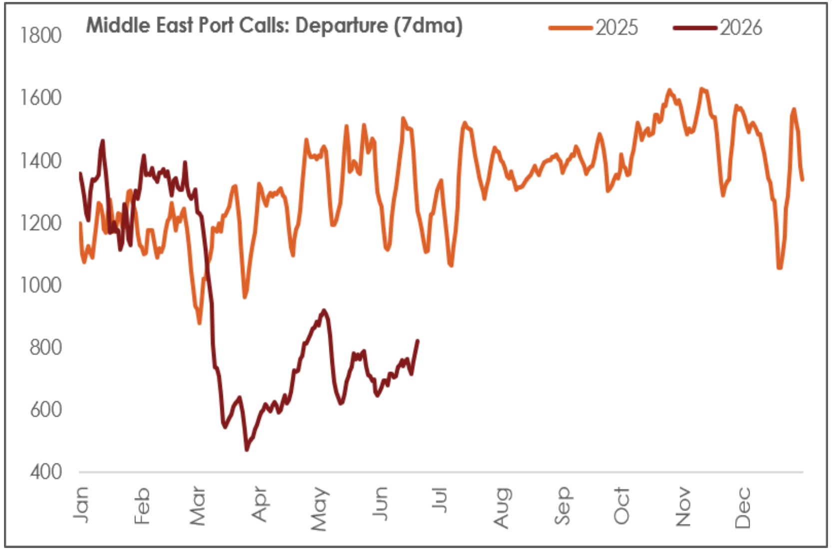
Note: The targeted measures on ECBs and FCNR(B) deposits are expected to result in USD 75 bn inflow by Dec-26.

Geopolitical concerns ease, for now

The signing of the US-Iran MoU has led to optimism with respect to a likely de-escalation of the Middle East tensions. Successful diplomatic negotiations in the next 60 days could lead to the signing of a peace deal between the two nations. Crude prices have responded favourably, with likelihood of Brent now averaging at USD 80-85 pb on average basis in FY27 vs. our earlier estimate of USD 95 pb.

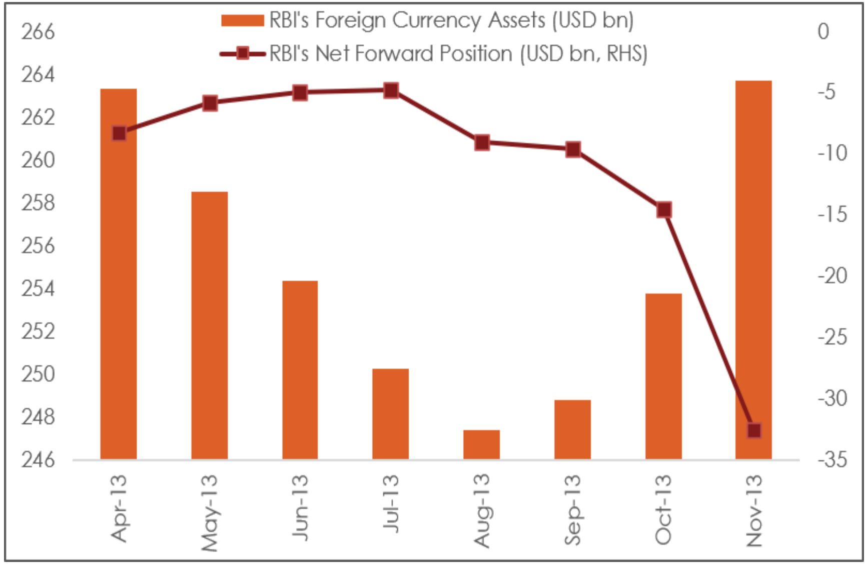
Maritime traffic in the Middle East has started to move up, albeit tentatively. The skirmishes involving Israel and Lebanon continue to cast a residual shadow on regional stability, for now.



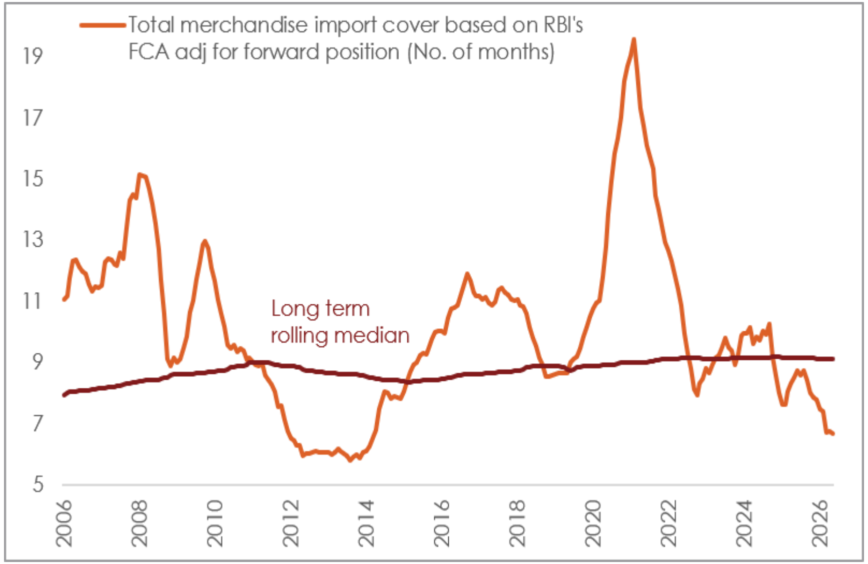


Spot FX reserves will see a build-up

With approximately USD 75 bn of targeted foreign debt inflow expected by Dec-26, we expect the RBI to aggressively rebuild its FX Reserves. While RBI's spot reserves will show a spike in the next 6 months, the forward reserves will show a concomitant dip, similar to the 2013 experience.



India's adjusted import cover (based on RBI's FCA adjusted for its forward position) has dipped below 7 months. While the USD 75 bn expected inflow will be neutral for the adjusted import cover, it will help to shore up spot reserves, which will boost the RBI's FX intervention capability in the near term.

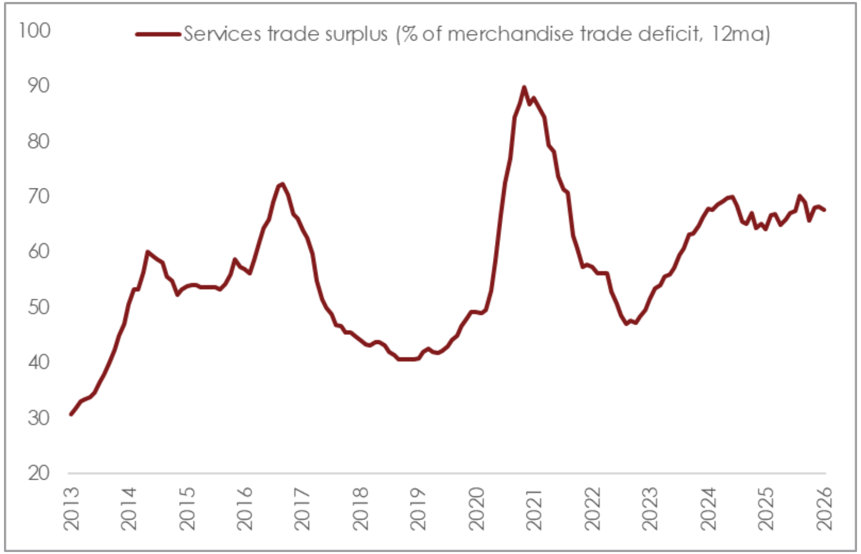


Policymakers are hedging against trade uncertainties

India signed 4 bilateral FTAs (with the UK, Oman, New Zealand, and the EU), while laying the mutual framework for a trade and investment deal with the US* in FY26. Taken together, these economies had a share of ~40% and ~18% in India's merchandise export and import in FY26.

	Exports (USD bn)	Imports (USD bn)	Trade Balance (USD bn)	Total Trade (USD bn)
UK	13	12	2	25
Oman	4	7	-3	11
NZ	1	1	0	1
EU	73	66	6	139
US	87	53	34	141
Total	**442**	**775**	**-333**	**1217**

On a trend (or smoothed) basis, the services trade surplus helps to fund ~68% of the merchandise trade deficit, thereby reducing the structural pressure on India's current account deficit.

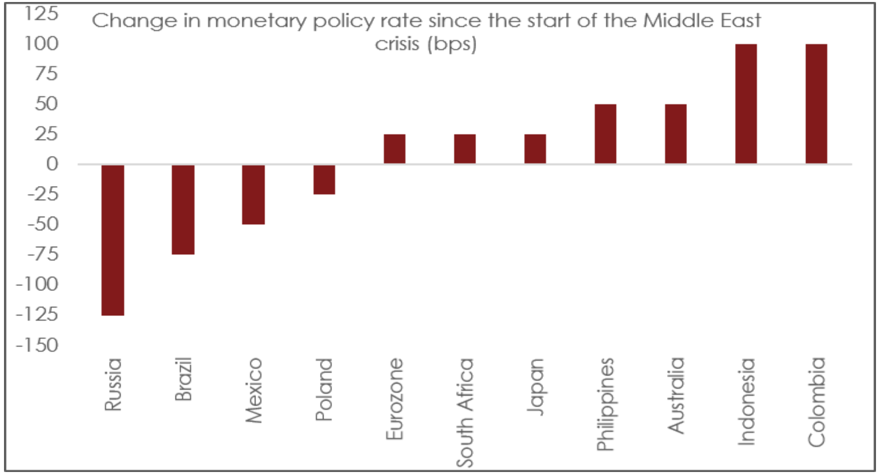


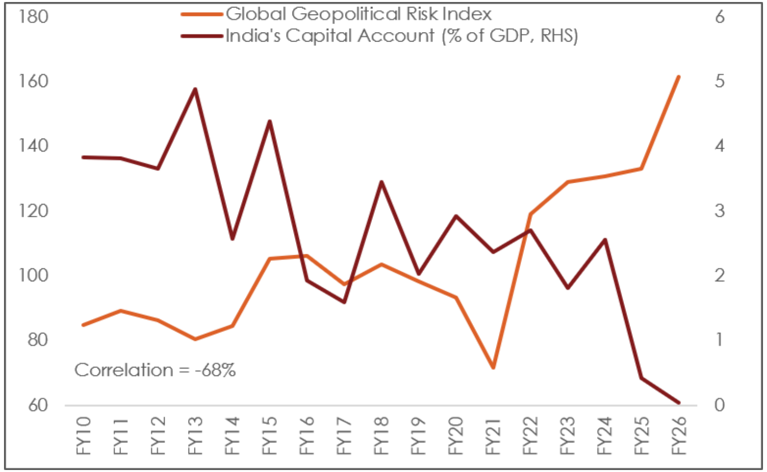
** India and the US are back at the negotiating table to finalize the trade deal shortly*

Rupee outlook

Although INR has found support from the sharp pivot in the FY27 BoP outlook, its outlook will also be impacted by the USD trajectory. Key DM and EM central banks have tightened monetary policy since the start of the Middle East crisis. For the US, market participants expect 1 rate hike in Sep-26, followed by another one in Mar-27. This is likely to keep USD on a firm trajectory.

A palpable increase in geoeconomic and geopolitical uncertainty in recent years has weighed down global capital flows. This has kept India's capital flows subdued.





We project a USDINR to touch 92 by Sep-26/Dec-26 on heavy forex inflows. Thereafter, it is expected to move towards 95 by Mar-27. Geopolitical factors will continue to warrant close attention.

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