

## INDIAN ECONOMY

# Crisil Insights

May 2026

Through the monthly Crisil Insights Indian Economy series, we delve into how India's growth dynamics are expected to change in the fiscal. In this issue, we look at the impact the West Asia conflict is having on India's macros.

## Price tentacles amid growth moderation

Crisil expects India's gross domestic product (GDP) to grow 6.6% this fiscal, with the average Consumer Price Index (CPI)-based inflation at 5.1% as the West Asia conflict extends to the third month with no lasting solution in sight.

The revised outlook is based primarily on an upward revision in our average crude oil price forecast and its spillover effects for this fiscal—to \$90-95 from \$82-87 per barrel—and lingering geopolitical uncertainties.

Inflationary pressures are gradually increasing, with a noticeable impact on the Wholesale Price Index (WPI) than the retail gauge.

Inflation based on WPI rose to 8.3% in April, while that based on CPI remained benign at 3.5%. Over the past four months, core CPI inflation has remained stable at 3.7%.

The current spike in WPI is directly linked to the West Asia conflict compared with the CPI, adversely impacting commodities and production processes.

We expect CPI inflation to rise and average 5.1% this fiscal for three reasons:

- Rising input costs, as indicated by the spike in WPI, will gradually pass through as producers want to protect their margins, leading to higher core inflation
- Increases in crude oil prices are being gradually reflected in the pump prices of petrol and diesel, which together carry a 4.8% weight in CPI
- Below-normal rainfall expected amid weather disruptions could negatively impact agricultural production and put an upward pressure on food inflation

Over the past two years, capital inflows have been insufficient to finance even a small current account deficit (CAD). At the same time, capital outflows have intensified, while the West Asia conflict has added to India's vulnerability.

CAD is projected to rise to 2.2% of GDP this fiscal from an estimated 0.8% in fiscal 2026. A wider CAD and weakening capital inflows have weighed on the rupee, which has depreciated 6.7% since the beginning of calendar year 2026.

It remains to be seen if the Reserve Bank of India (RBI) will raise rates to support the domestic currency on the lines of Bank Indonesia.

We expect the RBI to adopt a wait-and-watch approach for now and observe whether the supply-side pressures on inflation are transitory or durable.

The Monetary Policy Committee is likely to maintain the repo rate and stance in the upcoming meeting. Risks to inflation are tilted to the upside and likely to increase with the duration and intensity of the West Asia conflict. Currently, retail and core inflation remain well within the comfort zone.

## Financial conditions

Liquidity relief

## Industrial production

The first hit

## Inflation

Shielded by policy, so far

### Financial conditions

- Systemic liquidity improved, with surplus reaching a four-year high of Rs 5 lakh crore in mid-April driven by higher government spending and maturity of government securities
- Liquidity improved despite headwinds from foreign portfolio investment (FPI) outflows of \$7.6 billion against \$1.4 billion average in the past 12 months, high credit-deposit ratio of 82.01 April-end vs 81.4 March-end and a pause in open market operations
- The RBI net-absorbed an average Rs 3.8 lakh crore under its liquidity adjustment facility (1.4% of net demand and time liabilities or NDTL) compared with Rs 1.6 lakh crore (0.6% of NDTL) in March
- Average cash balances with the RBI declined to Rs 0.8 lakh crore in April from Rs 3.5 lakh crore in March. Typically, government spending rises at the start of the new fiscal
- The surplus lowered money market rates: the six-month commercial paper, certificate of deposit rates and 91-day Treasury bill. The weighted average call rate was 5.31% vs 5.21%. Bank credit was strong at 16% on-year in April vs 16.1% in March
- Domestic inflation is expected to rise significantly this fiscal and GDP growth is expected to soften, narrowing the space for monetary policy in India. The West Asia conflict has constrained monetary policy space globally

### Industrial production

- The Index of Industrial Production (IIP) slowed to 4.1% on-year in March from 5.1% on-year in February amid the critical input shortage of crude, petro products and natural gas in the first month of the West Asia conflict
- Weaker growth in manufacturing and electricity dragged headline IIP, while mining rose. IIP growth was weak in three of six use-based sectors. The sharpest fall was in intermediate goods, infrastructure and construction goods and consumer durables
- While intermediate goods was affected the most by declining IIP for chemical products and textiles, which depend on crude and natural gas, higher growth in capital goods, primary goods and consumer non-durables capped the fall in the IIP
- Amid major export-oriented sectors, the IIP was hit for electronic products, readymade garments, textiles and chemical products. The slowdown in consumer durables was driven by readymade garments and electronic products that cater to global demand too
- With the West Asia conflict extending, the cost of production is seen escalating and existing inventory buffers are likely to deplete. The government is restoring supply of energy and critical inputs to industry, but the conflict has kept commodity prices elevated
- Net-net, higher input costs and weak export demand are expected to hit industrial growth, at least in the first quarter of this fiscal

### Inflation

- CPI inflation rose mildly to 3.48% in April from 3.40% in March. Despite the West Asia conflict in its second month in April, the upside risks to retail inflation seem to be materialising at a snail's pace
- The food basket saw impact in categories such as vegetable oils and ready-made food. Inflation in electricity, gas and fuels eased, while that in transportation fuels remained unchanged owing to pump prices of petrol and diesel remaining steady April-end
- The expected pass-through of higher energy and other input prices to consumers of various products and services is yet to play out in the aggregate core inflation, which remained unchanged at 3.7% for the fourth consecutive month
- On the other hand, inflation based on the WPI surged to a 42-month high of 8.3% in April, from 3.9% in March, as the West Asia conflict began to impact prices across categories
- We expect CPI-based inflation to average 5.1% this fiscal as against 2.0% in fiscal 2026, driven by a low-base effect and expectations of price pressures in major segments as prices of retail fuels are hiked and producers pass through higher costs
- Crude prices are expected to average 32% higher on-year at \$90-95 per barrel in the current fiscal. The government has already begun to hike pump prices. Producers are expected to pass on the rise in the cost of energy and other inputs to consumers
- Expected below-normal monsoon rainfall amid likely El Niño conditions and the ongoing heatwaves can hurt agricultural production and exert pressure on food inflation, which is normalising from its lows

**Interest rate**

Risk-off reigns

**Rupee**

Ceding more ground

**Trade**

Lengthening shadows

- West Asia kept investors wary and drove up government security (G-sec) yields in April. The benchmark 10-year paper (6.48% GS 2035) rose 21 basis points (bps) to 6.96% vs 6.75% average in March, and 56 bps on-year, the highest average yield since July 2024
  - The upward drift persisted for five reasons: continuing rise in crude oil prices; apprehensions around government finances; rising US Treasury yields; FPI outflows; and the RBI pausing G-sec purchases via open market operations
  - G-sec yields tend to surge during crude price spikes, as typically, higher crude prices impact India's macros, including government finances, current account deficit, inflation and growth
  - The weakening domestic outlook and rising yields in advanced economies because of higher-inflation expectations, led to FPI outflows that added to the upward pressure on G-sec yields. Rising borrowings pushed the sovereign curve up at the longer end
  - We expect the benchmark 10-year G-sec yield to rise to average 7.0% in March 2027, up from 6.7% in March 2026, driven by crude prices, pressure on government finances, tighter global financial conditions and volatile foreign capital flows
  - A prolonged conflict will add to the pressure on government finances, while a slowdown in domestic growth will impact tax collection. Globally, expectations of higher inflation and tighter monetary policy are likely to constrain foreign capital flows
  - With domestic inflation on the rise, the monetary policy space is likely to shrink this fiscal. In the near term, the duration of the West Asia conflict and policy responses thereof will bear watching
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- Even a weaker US dollar could not stem the rupee's depreciation in April as the local currency averaged 93.6 to the greenback vs 92.8 in March. The rupee corrected at the beginning of the month following the RBI's regulatory actions
  - However, in the second half, the rupee depreciated sharply—crossing the 95-per-dollar mark for the first time—driven by FPI outflows (net outflows of \$7.6 billion in April vs \$13.6 billion in March), a wider trade deficit and elevated crude oil prices
  - Advanced and emerging market currencies showed a mixed trend, with the euro and pound appreciating against the dollar, while the yen, the Indonesian rupiah and the Turkish lira weakened. The US Dollar Index averaged 98.8 in April, down 0.7% on-month
  - With the West Asia conflict extending beyond April, the risks to our previous forecasts have materialised. We now expect the rupee to average 93.5 per dollar in March 2027. A higher current account deficit in fiscal 2027 will likely put pressure on the rupee
  - A prolonged West Asia conflict and escalating geopolitical uncertainties could keep FPI flows volatile, adding to the pressure. As a result, the rupee is expected to remain volatile in the near term
  - We expect the rupee to strengthen from its current lows by fiscal-end, assuming the conflict abates. This aligns with the historical trend in currency volatility, where sharp depreciations are typically followed by a correction
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- A 34.7% on-year surge in petroleum exports helped India's goods exports rise 13.8% on-year in April to \$43.6 billion (vs a 7.4% contraction in March). Core exports were resilient but exports of gems and jewellery declined on-year for the second month
  - The surge in petroleum exports reflected the rise in crude oil prices. Exports to Saudi Arabia and the United Arab Emirates continued to contract on-year in April, by 2.9% and 36.4%. Exports to the US rose, reflecting the positive impact of lowered tariffs
  - The import bill climbed 10% on-year to \$71.9 billion in April, reversing direction from a 6.5% contraction in March. This was led by a pick-up in core import growth, partly reflecting increased price pressures as well as a surge in imports of gems and jewellery
  - Crude imports saw an on-year decline of 10%, reflecting the supply disruptions. The rise in exports and fall in imports narrowed the oil trade deficit to \$9 billion from \$13.6 billion a year ago but higher crude prices widened the deficit in April from March
  - India's merchandise trade deficit widened to \$28.4 billion in April 2026 from \$27.1 billion a year ago and \$20.7 billion in March
  - Higher oil prices are expected to exert greater pressure on the CAD. Global trade disruption and weakening demand will likely hit exports and affect regional growth. Hence, remittances coming to India could get squeezed
  - For the current fiscal, we project the CAD to rise to 2.2% of GDP from an estimated 0.8% in fiscal 2026

Interest rate

Rupee

Trade

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