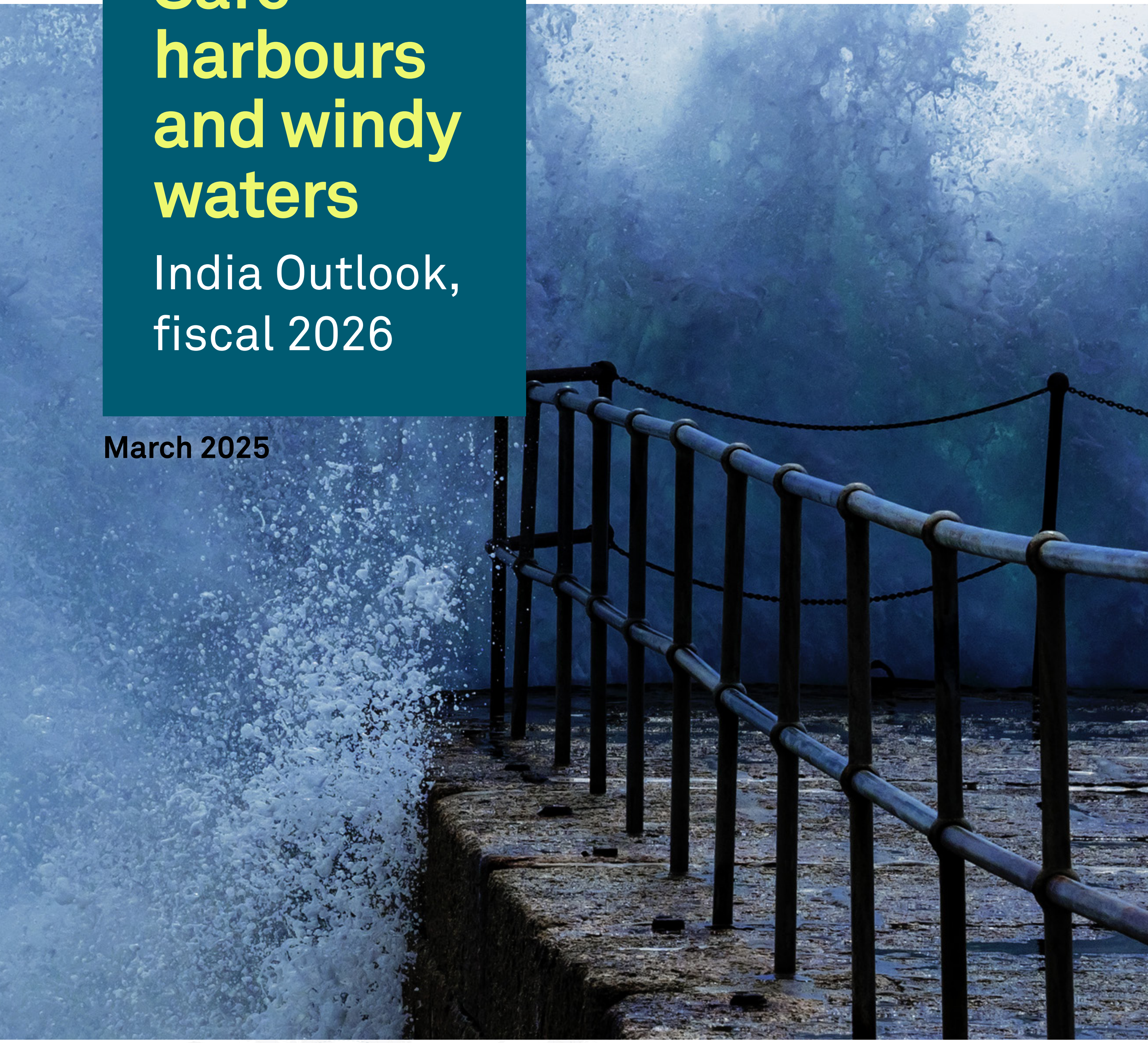
Crisil Intelligence

Safe harbours and windy waters

India Outlook, fiscal 2026

March 2025



by S&P Global

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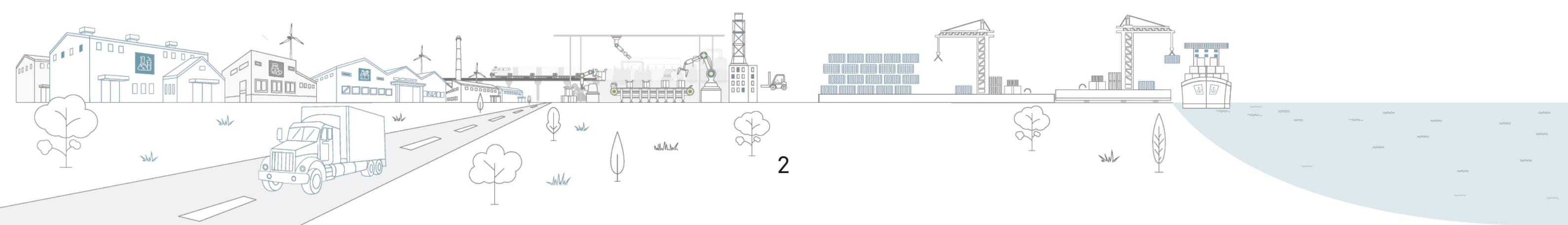


Crisil Intelligence

Foreword

Amish Mehta
Managing Director & CEO

Once again, India's resilience is being tested.

This time, by a new set of uncertainties stemming from geopolitical and trade-related issues led by US tariff actions.

Their impact can play out via direct and indirect channels, potentially altering trade dynamics, disrupting well-established supply chains and keeping uncertainty elevated.

To its credit, India has built a few safe harbours against exogenous shocks over the past few years.

Healthy economic growth, low current account deficit and external public debt, and adequate forex reserves provide ample policy latitude.

But given the very windy waters, the buffers do not completely insulate the country from adverse global developments — at least in the short term.

All the same, we retain our view that India will remain one of the fastest-growing large economies until the end of the decade.

The recent focus on ease of doing business through deregulation, aimed at igniting domestic growth drivers, can create an upside for growth.

In fiscal 2026, we expect the economy to maintain a growth rate of 6.5%, same as estimated for fiscal 2025, driven by a relatively balanced set of domestic drivers. However, the ongoing geopolitical and trade-related uncertainties pose some downside risks to this forecast.

India's economic growth rate is normalising towards its medium-term trend and, in fiscal 2026, will be supported by factors such as lower food inflation, lower borrowing costs and higher disposable income of the middle class.

We expect healthy domestic consumption, particularly in fast-moving consumer goods, consumer durables, two-wheelers and discretionary segments such as tourism.

Supported by the growth of consumption-related sectors, we anticipate corporate revenue growth to be 7-8% in fiscal 2026, a tad higher than the previous year.

Corporate margins, on their part, should improve ~50 basis points (bps), thanks to lower energy and commodity prices, and lower food inflation.

Improved profitability, along with an uptick in domestic demand, will support investments in the industrial sectors.

On the fiscal front, government capex is budgeted at 3.1% of gross domestic product (GDP), akin to last fiscal. The government's commitment to infrastructure development is evident from the consistent allocation to key sectors such as roads, renewable power, ports and urban development, which will create employment and improve logistics efficiency.

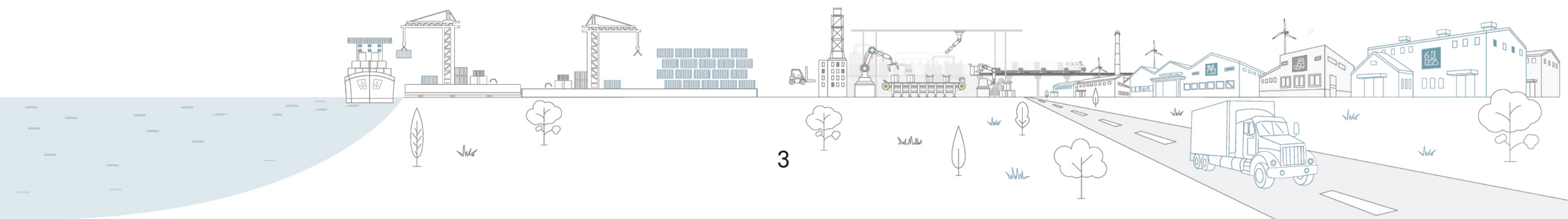
Over the medium term, we expect India's GDP to grow at 6.7% per year, with capital or investments playing a dominant role, and a bigger push from efficiency gains.

With trade dynamics evolving, supply-chain diversification has ramped up in recent times.

That has led to sharper focus of industry stakeholders on competitiveness. India ranked 25th and 53rd in global competitive ranking in 2024, as against 32nd and 49th in 2020, on business efficiency and infrastructure, respectively. China ranked 15th on both parameters.

A robust manufacturing sector is not only an economic driver but also a strategic lever to boost exports and foreign exchange earnings and fortify India's position in the global value chain. With innovations and sector-specific strategies, a thriving manufacturing industry can act as a catalyst for overall development.

In India, despite reforms and related initiatives, the



manufacturing ecosystem continues to face challenges on key investment criteria because of low labour productivity, high logistics and power costs, and limited innovation.

As a result, manufacturing growth has lagged services. Between fiscals 2011 and 2020, gross value added (GVA) in services grew at an average 7.7% per year as against 6.0% average growth in manufacturing GVA.

The tide, however, seems to be turning.

Over the medium term, manufacturing GVA is likely to grow at 9% on average, much higher than a 6.8% average for services. This will help India ramp up the share of manufacturing in GDP to ~20% by fiscal 2031, from 17.2% in fiscal 2025.

The improvement will ride on a focused approach in sunrise sectors such as solar photovoltaics, battery manufacturing and semiconductors.

In our view, largely led by the private sector, these sectors could witness capex worth Rs 8-10 lakh crore through fiscal 2030. The continuation of last fiscal's duty cuts, renewed focus on sectors such as solar, battery storage, wind and high-voltage transmission will support backward integration efforts.

Calibrated joint action through non-trade barriers and trade policy, along with PLI incentives, give visibility to the private sector for long-term investments.

While government policies, capex incentives, periodic industry consultation and a favourable business cycle have helped achieve success so far, it is imperative for the government to ensure this capex momentum continues. Tax breaks, lower lending rates and welfare schemes can support consumption and capacity utilisation.

Overall, a gradual improvement in corporate investments is anticipated, but with lingering global uncertainty.

This report captures all these, providing a comprehensive overview of the Indian economy and its growth prospects.

It would be a valuable resource for decision-makers, businesses and investors looking to navigate the complexities of the Indian economy and capitalise on its growth opportunities.

I am sure you will enjoy going through the insightful analyses and forecasts inside.

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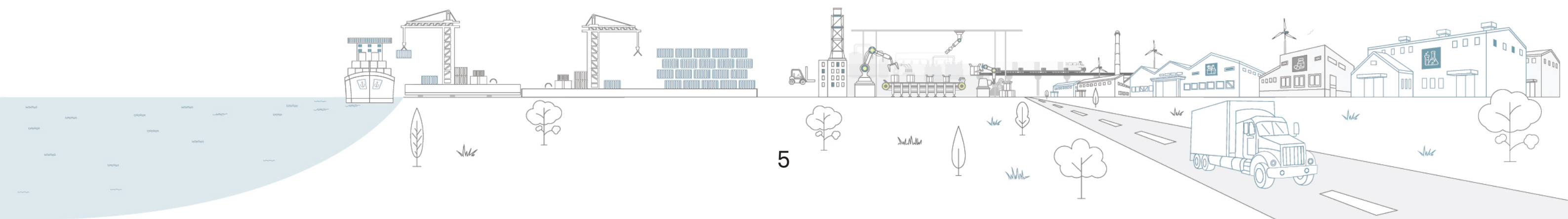


Macroeconomic outlook for fiscal 2026

Growth drivers

- We expect India's economy to maintain the growth rate of 6.5% in fiscal 2026, assuming the upcoming monsoon season is normal yet again and commodity prices remain soft
- Cooling food inflation, the tax benefits announced in the Union Budget 2025-2026 and lower borrowing costs will drive discretionary consumption
- Risks to the outlook are tilted to the downside given elevated uncertainty due to the tariff war led by the United States (US)

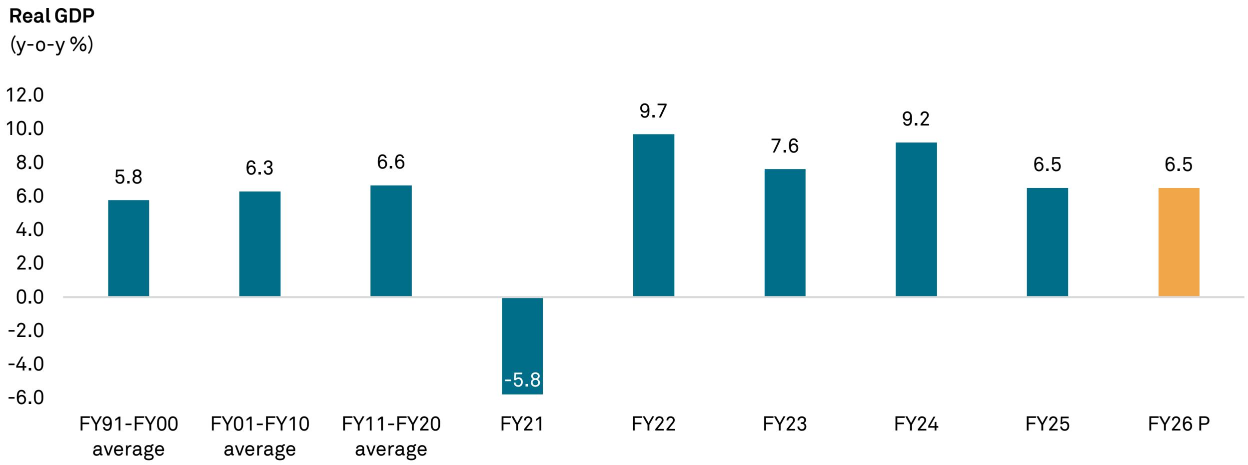
Since the economic reforms of 1991, India's growth has trended up every decade. The economy expanded 8.2% on average between fiscals 2022 and 2025, rebounding sharply after the Covid-19 pandemic in fiscal 2021, and became the fifth largest in the world by fiscal 2023.

Agreed, the expansion was on a low base. Yet, there is no gainsaying the role of government policy support and resilient balance sheets of borrowers and lenders in the faster-than-expected rebound amid global turmoil.

Growth is now returning to pre-pandemic rates as fiscal impulse normalises and the high-base effect wears off.

Even with that, the high-frequency Purchasing Managers' Index (PMI) data reveals that India maintains its pole position among major economies.

Growth has now normalised to pre-pandemic levels



P – projected
Source: National Statistical Office (NSO), CEIC, Crisil

India's resilience is evident in the PMI data

	Composite PMI					
	India	US	Eurozone	UK	China	Japan
Jan-24	61.2	52.0	47.9	52.9	52.5	51.5
Feb-24	60.6	52.5	49.2	53.0	52.5	50.6
Mar-24	61.8	52.1	50.3	52.8	52.7	51.7
Apr-24	61.5	51.3	51.7	54.1	52.8	52.3
May-24	60.5	54.5	52.2	53.0	54.1	52.6
Jun-24	60.9	54.8	50.9	52.3	52.8	49.7
Jul-24	60.7	54.3	50.2	52.8	51.2	52.5
Aug-24	60.7	54.6	51.0	53.8	51.2	52.9
Sep-24	58.3	54.0	49.6	52.6	50.3	52.0
Oct-24	59.1	54.1	50.0	51.8	51.9	49.6
Nov-24	58.6	54.9	48.3	50.5	52.3	50.1
Dec-24	59.2	55.4	49.6	50.4	51.4	50.5
Jan-25	57.7	52.7	50.2	50.6	51.1	51.1

Note: PMI data is a factual indicator of global economic health based on monthly surveys of business executives covering 45 economies and 30 sectors. A PMI reading over 50 represents economic expansion and below 50 represents contraction compared with the prior month
Source: HSBC, Caixin, Hamburg Commercial Bank, au Jibun Bank, S&P Global, Crisil

In fiscal 2026, growth will be supported by easing monetary policy and government measures to boost private consumption. The budgeted 10.1% increase in government capital expenditure (capex) will also be supportive.

Growth will be steady compared with fiscal 2025 despite overall lower fiscal impulse as the government reduces its fiscal deficit target to 4.4% of gross domestic product (GDP) from the revised estimate of 4.8%. Emerging global risks are a key monitorable as they could dent export growth and keep uncertainty levels high, which is detrimental to a broad-based private sector investment revival.

Crisil expects real GDP growth at 6.5% in fiscal 2026

Why private consumption is expected to hold up in fiscal 2026

- **Income tax cuts:** The government has reduced income tax rates under the new tax regime[1], which will increase the disposable incomes of the middle class. The tax rebate limit has been raised to Rs 12 lakh from Rs 7 lakh, leading to tax savings of ~Rs 80,000 annually for an individual earning Rs 12 lakh. Tax slabs have also been revised, which will reduce the tax burden across income levels. These measures will durably support spending by the middle class beyond fiscal 2026 as well, though some of the increase in disposable income can also go towards savings and debt repayment
- **Government welfare spending:** In the recent budget, the government has earmarked increased spending on key asset- and employment-generating schemes in fiscal 2026. The allocation for Pradhan Mantri Awas Yojana (PMAY) is budgeted to rise 64.1% on-year and that for Pradhan Mantri Gram Sadak Yojana (PMGSY), 31% on-year. And allocation for the Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS) has been maintained. Overall, spending on the mentioned schemes is budgeted to rise 23.7% on-year after being stagnant in fiscal 2025. This is also higher than the 14% average growth in spending in the four years preceding the pandemic (fiscals 2017-2020)
- **Lower food inflation:** We foresee food inflation cooling in fiscal 2026 on expectation of a normal monsoon. Food inflation has soared in recent years and has

[1]About 72% of taxpayers had adopted this regime as of July 2024 for assessment year 2024-25

been constraining households. The share of food in total consumption is the highest among lower-income households. So, softer food inflation should create space in household budgets for discretionary spending

- **Policy rate cuts:** We expect the Monetary Policy Committee (MPC) of the Reserve Bank of India (RBI) to cut the repo rate further in fiscal 2026, following a 25 basis points (bps) cut in February 2025, on expected further easing of domestic retail inflation. We expect 50-75 bps of rate cuts in fiscal 2026. Lower interest rates are expected to mildly support consumption as these will gradually get transmitted to other interest rates in the economy, thereby lowering borrowing costs

Increased private sector participation is necessary for balanced and sustainable investment momentum

The government's post-pandemic strategy of providing extraordinary support to investments via budgetary spending has paid off, with fixed investments the key driver of GDP growth until fiscal 2024. Now, there is a greater shift in policy strategy towards incentivising private corporate investments.

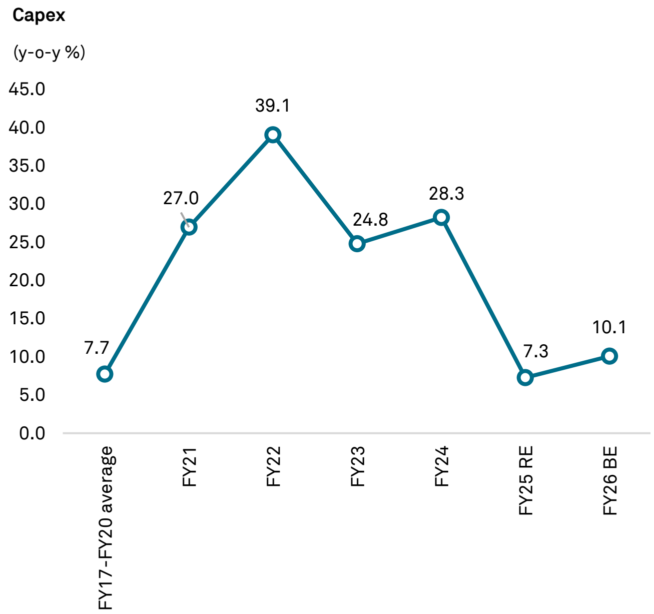
After having risen from the pre-pandemic average of 1.7% of GDP, central government capex is budgeted to stabilise at 3.1% of GDP in fiscal 2026, same as fiscal 2025.

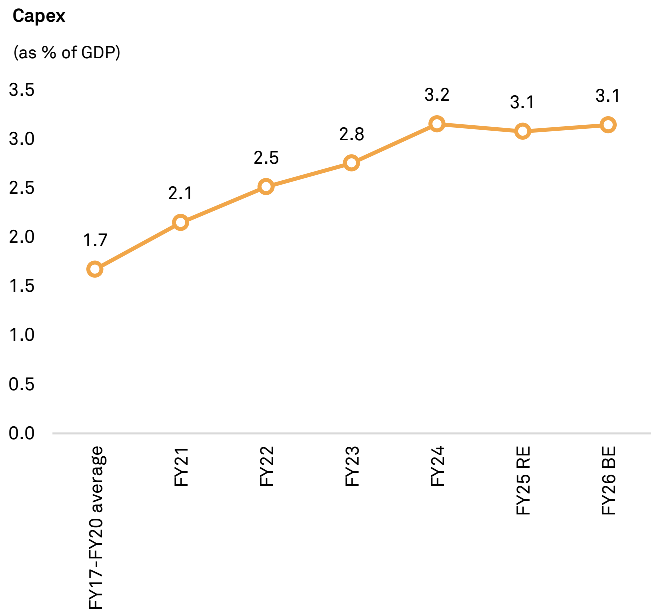
While central government capex remains supportive, the focus should also be on reducing cost and time overruns. As of December 2024, 63.7% of central sector projects totalling Rs 150 crore and above had time overruns, higher than the 29.8% of projects on time. And 41.1% of projects faced cost overruns. Here, creating a pipeline of shovel-ready projects and better coordination with states will help get the best bang for the buck.

Reducing time and cost overruns will be critical for meeting the capex target. As per the revised estimates, the central government missed its capex target for fiscal 2025 by 8.3%. State capex has also lagged in fiscal 2025. During the first nine months of fiscal 2025, capex of 16 major states stood at Rs 4 lakh crore, which is 47.4% of the budget target.

> Although the government is normalising capex growth after an extraordinary push post pandemic, it will remain growth-supportive due to multiplier effects

Centre's capex as a percentage of GDP has been maintained in fiscal 2026





RE – revised estimates; BE – budget estimates
Source: Budget documents, CEIC, Crisil

With the government normalising capex, it is time for the private sector to take the lead in furthering the investment momentum. The ability of private corporates to invest is supported by their deleveraged balance sheets, the healthy balance sheets of lenders, and turning of the interest rate cycle.

The government is also taking steps to encourage investments by the private sector. Total allocation for the Production Linked Incentive (PLI) schemes is budgeted to rise 87% on-year in fiscal 2026, particularly in sectors such as electronics, textiles, automobiles and components. Efforts at deregulation will help, too.

That said, heightened global uncertainty and uneven private consumption demand conditions have been the key hindrances to a revival in corporate investment so far (refer to 'Tracing the investment story' for details on why private sector investment is yet to pick up).

Trade is facing headwinds

With domestic private consumption expected to hold up, imports should remain healthy in fiscal 2026, while export growth could be subdued. As a result, India's merchandise trade deficit is expected to come under some pressure.

Slowing global growth (3.0% in calendar 2025 from 3.3% in calendar 2024, as per S&P Global's November 2024 forecast) — particularly of the US (2.0% vs 2.7%), our largest export destination — could hit India's exports. Global trade volume growth is also expected to moderate to 3.2% in calendar 2025 from 3.4% in calendar 2024, according to the United Nations[2].

Risks to trade have increased due to the tariff war set off by the US. Thus, changes in the US tariff policy and, subsequently, retaliatory tariffs bear watching. India is vulnerable to US tariff actions as it runs a trade surplus with the country and taxes imports from there at a higher weighted average tariff rate (9.5%) than Washington's taxes on imports from India (3%). (Refer to 'Navigating global turbulence' for details)

That said, services trade, which has proven to be more resilient and where India runs a surplus, will provide some cushion.

Easing food inflation to move headline CPI closer to the RBI's target

We expect inflation to moderate to 4.4% in fiscal 2026 from an estimated 4.7% in fiscal 2025 on easing food inflation

Headline inflation, based on the Consumer Price Index (CPI), is slowly easing towards the RBI's target of 4% after having shot up in the wake of supply constraints caused by the pandemic and geopolitical tensions in Europe.

The cooling has been on account of slowing non-food inflation (core plus fuel), which hit record lows in fiscal 2025 owing to benign global commodity prices and impact of the RBI's past rate hikes, even as food inflation remained in the red zone.

Food inflation intensified for the third straight year, with its contribution to headline CPI rising each year — to 66% in fiscal 2025 (April-January) from 55% in fiscal 2024, 39% in fiscal 2023 and 27% in fiscal 2022.

High food inflation in fiscal 2025 was led by a surge in vegetable prices owing to multiple supply shocks. Food, which has a weightage of 39.1% in the CPI, tends to influence the trajectory of headline inflation in India. Towards the end of fiscal 2025, though, lower food inflation has begun pulling headline inflation down.

In fiscal 2026, we expect food inflation to soften further and pull down the headline number.

[2]United Nations Department of Economic and Social Affairs, January 2025, 'World Economic Situation and Prospects'

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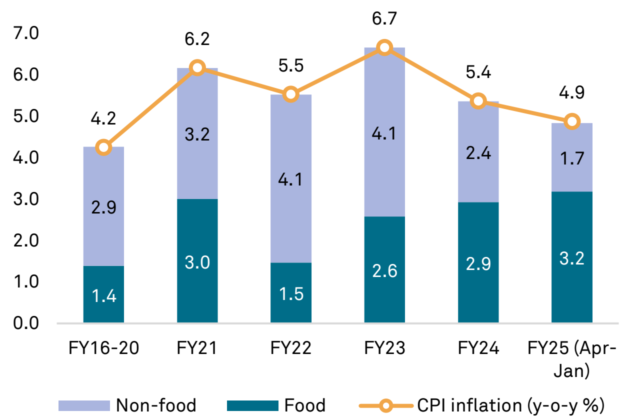
Rising contribution of food to headline inflation

Contribution to CPI inflation

(Percentage points)

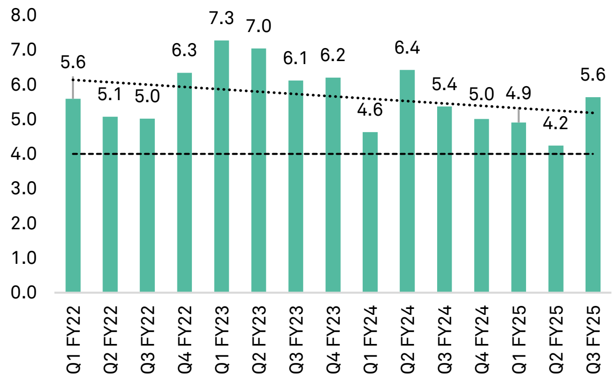


Source: NSO, CEIC, Crisil

Inflation has been above the RBI's 4% target in every quarter post-pandemic, but has trended down

CPI inflation

(y-o-y %)



Source: NSO, CEIC, Crisil

Why we expect inflation to ease in fiscal 2026

- **Robust rabi sowing:** Rabi sowing has progressed well so far and was up 1.5% on-year as on February 4. This augurs well for food supplies in fiscal 2026
- **Bearish global commodity price outlook:** The downturn in prices of crude oil and other key commodities will keep core inflation within the RBI's comfort zone. Crisil Intelligence expects crude oil prices to average $70-75 per barrel in fiscal 2026, down from $78-83 per barrel in fiscal 2025. The World Bank has projected[3] overall energy prices to decline 6.2% on-year in calendar 2025 and prices of metal and minerals to remain relatively stable (-0.9%). That said, we believe core inflation will rise, given fiscal 2025's low base
- **Expectation of a normal monsoon:** A normal southwest monsoon will be key for lower food inflation in fiscal 2026. Kharif production, which accounts for about half of foodgrain production in India, depends on the monsoon. Hence, a favourable monsoon will augur well for prices of major crops, including rice, pulses and sugarcane
- **Easing global food prices:** Global food prices are expected to decline 4% on-year in calendar 2025, according to the World Bank

Key risks to easing inflation

- **Weather shocks:** Food inflation is susceptible to climate risks and has been impacted by rising frequency of heatwaves, uneven monsoon and excess rainfall in the recent past (discussed in 'Food prices have been adversely impacted by climate change in recent years'). Indeed, any unusual weather pattern could push up food prices
- **Geopolitical uncertainty:** Global shocks, particularly a broader trade war, is a key risk for core inflation. The US-led tariff war has put pressure on capital flows and the rupee in recent months. Sharper rupee depreciation will have to be monitored as it adds to the risk of imported inflation. India imports items such as crude and edible oils, which become costlier in rupee terms when the currency weakens. Energy price volatility cannot be ruled out, given ongoing conflicts in major crude oil-producing regions

[3]World Bank Commodity Markets Outlook, October 2024

Food inflation projected to moderate after surging for three consecutive fiscals

	Weights (%)	FY21	FY22	FY23	FY24	FY25 (Apr-Jan)	FY26 P
Headline	100	6.2	5.5	6.7	5.4	4.9	4.4
Food and beverages	45.9	7.3	4.2	6.7	7.0	7.4	4.6
Fuel	6.8	2.7	11.3	10.3	1.2	-3.0	2.5
Core	47.3	5.5	6	6.1	4.3	3.5	4.5

P – projected
Source: NSO, CEIC, Crisil

Lower food inflation to support discretionary consumption

The impact of inflation varies across income groups as consumption patterns differ by income levels. Essential items such as food and fuel take up a greater share of the consumption basket for lower-income households.

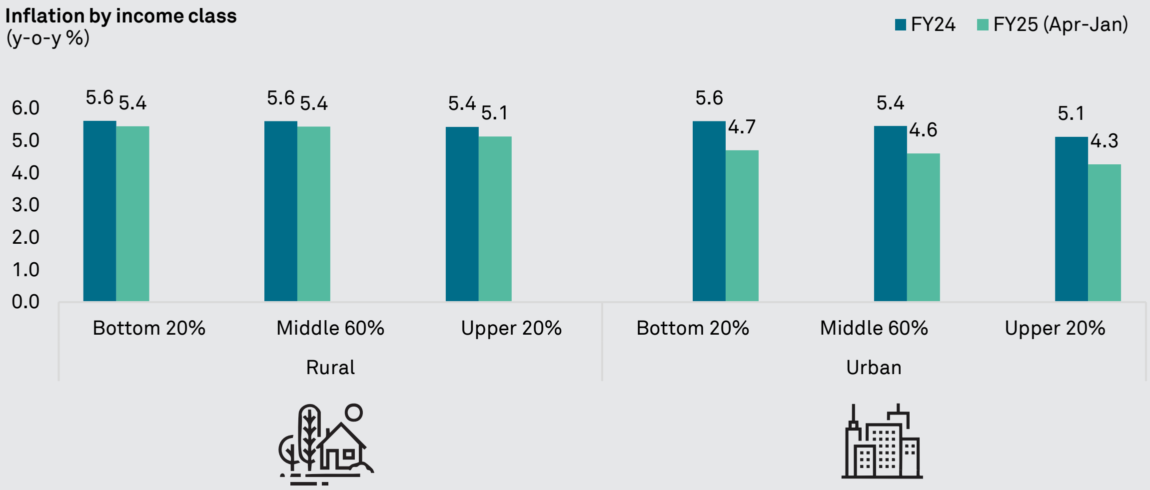
Crisil has mapped the expenditure baskets of the three broad income groups — bottom 20%, middle 60% and upper 20% of the population — with inflation trends, based on data from the National Sample Survey Office (NSSO), for a better gauge of the impact of inflation.

Our key findings for fiscal 2025 are:

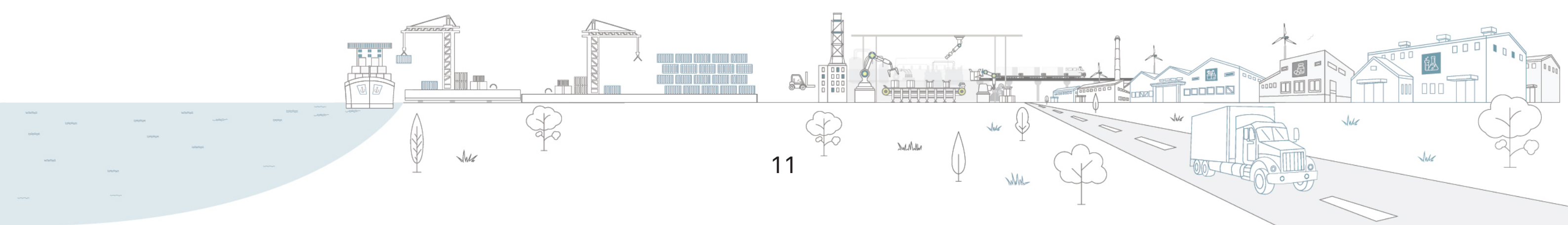
- Elevated food inflation has particularly impacted lower-income households in both rural and urban areas. Food comprises a larger share of the consumption basket of those in a lower-income bracket, whereas core items make up a larger share of the top income class
- The inflation rate among the urban rich was the lowest, as core items, which saw record low inflation in fiscal 2025, make up ~60% of their consumption basket
- The gap in the inflation rates among the relatively poorest and the richest widened to 1.1 percentage points in fiscal 2025 from 0.5 percentage point in the previous fiscal

Hence, our forecast of lower food inflation in fiscal 2026 bodes well for lower-income classes and should support consumption in this segment.

Urban residents have seen a larger respite in inflation in fiscal 2025



Source: NSO, NSSO, CEIC, Crisil



Food prices have been adversely impacted by climate change in recent years

Supply shocks, driven by unusual weather, have been the key reason behind higher food inflation in the past three years[4].

The world is getting hotter. A 2020 report by the Ministry of Earth Sciences noted that the mean temperature in India rose 0.7 degree Celsius over 1901-2018[5]. More recently, 2024 was the warmest year on record. Other recent years also saw close to record-high temperatures.

The frequency of heatwaves has increased in the past three years. The Economic Survey for 2024-25 notes that the percentage of heatwave days rose to 18% in 2022-2024 vs 5% in 2020-2022. This has affected crop yields.

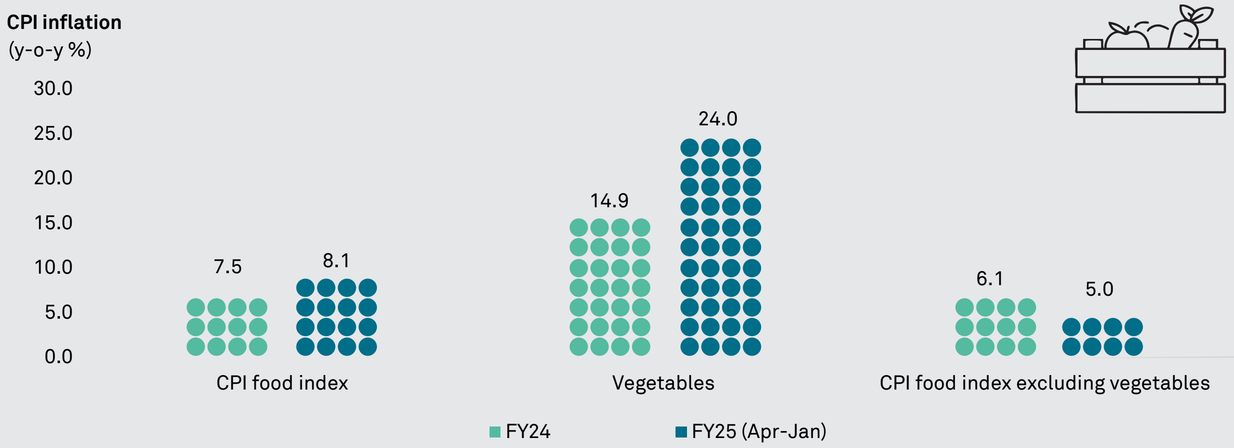
Climate change has also altered the monsoon pattern in India, and incidences of deficient and excess rains have increased[6].

Even when the monsoon has been broadly normal, the change in spatial and temporal weather patterns has hit crops across different stages of production, exacerbating food inflation.

In fiscal 2024, the monsoon was broadly favourable, supporting lower foodgrain prices. Yet, uneven distribution of rains in major vegetable-producing regions led to supply shocks in key vegetables. In fact, surging vegetable prices have been the primary factor behind higher food inflation in fiscal 2025. Excluding vegetables, food inflation eased to 5% in fiscal 2025 (April-January average) from 6.1% in fiscal 2024. This clearly demonstrates that even in years with a normal monsoon, vegetable prices can keep headline inflation on the edge.

Taking steps to tame vegetable price volatility, such as improving cold-storage infrastructure, increasing food processing capacity and promoting use of climate-resilient seeds, will be important as risks associated with climate change rise.

Vegetables lifted food inflation in fiscal 2025



Source: NSO, CEIC, Crisil

[4]For more, refer to Crisil Insight, 'Time for structural strike on inflation: Slower food output growth calls for more fiscal policy measures, reforms', December 2024
[5]Assessment of Climate Change Over The Indian Region, Ministry of Earth Sciences, 2020
[6]Shravan and Vishwas Chitale. 2024. Decoding India's Changing Monsoon Patterns – A Tehsil-level Assessment. New Delhi: Council on Energy, Environment and Water

Rate cuts have begun, but path could be bumpy amid global challenges

With easing inflation, we expect the MPC to cumulatively cut rates by 50-75 bps in fiscal 2026. However, slowing US Federal Reserve (Fed) rate cuts and weather-related risks could influence the timing and quantum of the RBI's rate cuts

Easing inflation and fiscal consolidation have opened doors for rate cuts

After an extended pause of 23 months, the MPC cut policy rates in February 2025. A large reason for the cut was CPI inflation easing closer towards 4% (the mid-point of the MPC's 2-6% target range) in fiscal 2025. The expected easing of inflation in fiscal 2026 opens doors for further rate cuts. The government's non-inflationary fiscal policy further creates a conducive environment for monetary easing.

However, weather shocks to inflation and slowing rate cuts by the Fed remain risks to rate cuts.

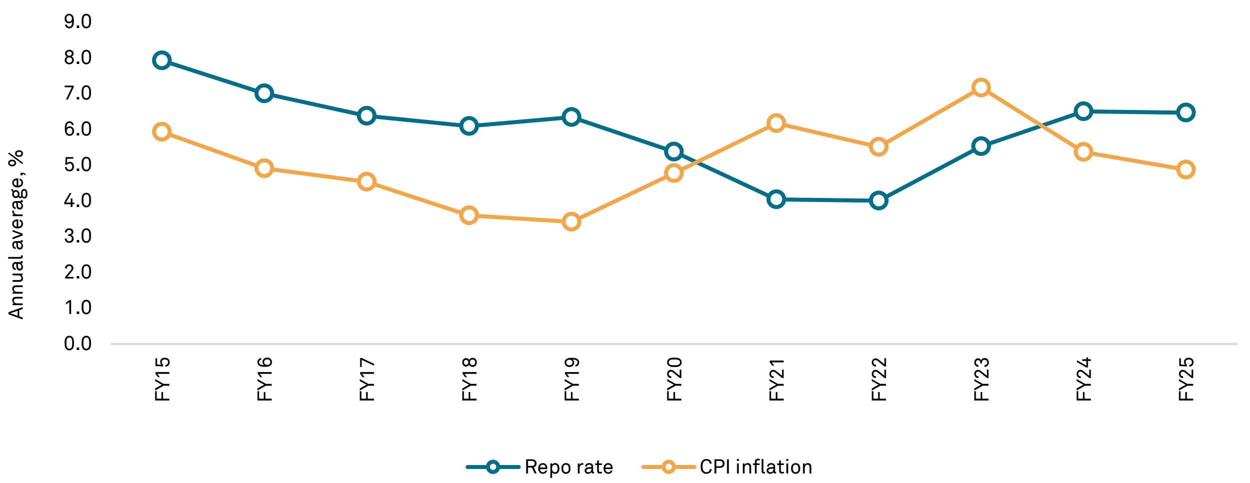
US monetary easing is expected to slow down due to inflation risk from US tariff hikes. Higher-for-longer Fed rates can constrain the space for monetary easing for other central banks. However, it is not likely to be the main driver of the latter's monetary policy actions. (Refer to 'Spillovers of US tariff hikes on monetary policy'.)

Also, the MPC began its rate cut cycle later than the advanced economy central banks. The Fed had cut rates by 100 bps between September and December 2024.

That said, the MPC has a neutral stance, which provides flexibility to keep rate actions dependent on incoming data.

We expect the RBI to remain proactive in using its liquidity and forex tools to support domestic financial conditions. Easier liquidity conditions are particularly needed to transmit the MPC's rate cuts to broader market interest rates.

Repo rate cuts expected ahead with easing inflation



Note: FY25 data is until February 2025 for the repo rate, January 2025 for inflation
Source: RBI, NSO, CEIC, Crisil

Spillovers from US tariff hikes to monetary policy

Tariff risks have disrupted Fed's rate cuts

Tariff hikes announced by the Trump administration have disrupted the Fed's monetary easing journey.

Higher tariffs are likely to add to US inflation in the short term due to higher cost of imported goods. While the timing and extent of tariff hikes are uncertain, the Fed is likely to err on the side of caution and watch how inflationary pressures evolve.

The Fed had already hit pause on its rate-cutting cycle in January, after reducing rates by 100 bps between September and December 2024.

S&P Global expects only one Fed rate cut in the first half of calendar 2025. The next rate cut is not expected before the second half of 2026.

The higher-for-longer Fed rate has contributed to a rise in US interest rates and a stronger dollar. This has put pressure on currencies of other economies. Tighter global financial conditions have curtailed monetary easing in other economies.

But other economies are tracing their own path on monetary easing

The European Central Bank (ECB), Bank of England and Bank Indonesia cut rates between January and February 2025 despite the Fed's pause.

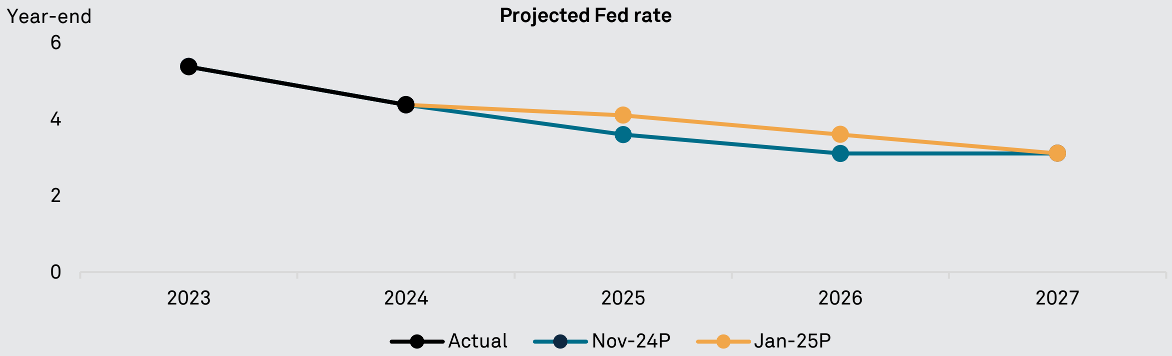
While a strengthening US dollar has put pressure on currencies of other major economies, their central banks are largely responding to their own growth-inflation dynamics. Growth is either slowing or is below trend across major economies such as the European Union (EU), China and India. On the other side, Japan has hiked rates due to rising domestic inflation.

Central banks are deploying tools other than interest rates to tide over market volatility. China, for instance, intervened in January to support the currency[7].

India, too, has used its forex reserves to curb excessive rupee depreciation. It has ample forex reserves to tide over short-term volatility (refer to the following section on CAD and currency outlook).

While global market volatility will not be the main influencer of domestic monetary policy decisions, it can impact the timing and quantum of rate cuts. Monetary policy is likely to remain data-dependent with an eye on maintaining financial stability.

Fed rate cuts delayed



Note: Projected Fed rate is based on S&P Global's forecasts. Nov-24P refers to S&P Global's forecast in November and Jan-25 is the revised forecast. All forecasts are for Q4 of the given CY.
Source: S&P Global, Bank for International Settlements, Crisil

[7] S&P Global (February 2025). Liquidity Outlook 2025: Five Questions, Five Answers

CAD in the safe zone, rupee volatile because of global shocks

- India's CAD is expected to rise mildly to 1.3% of GDP in fiscal 2026
- Rupee to remain volatile and settle at around 88/$ by March 2026
- India's external vulnerability remains low, but global shocks have intensified

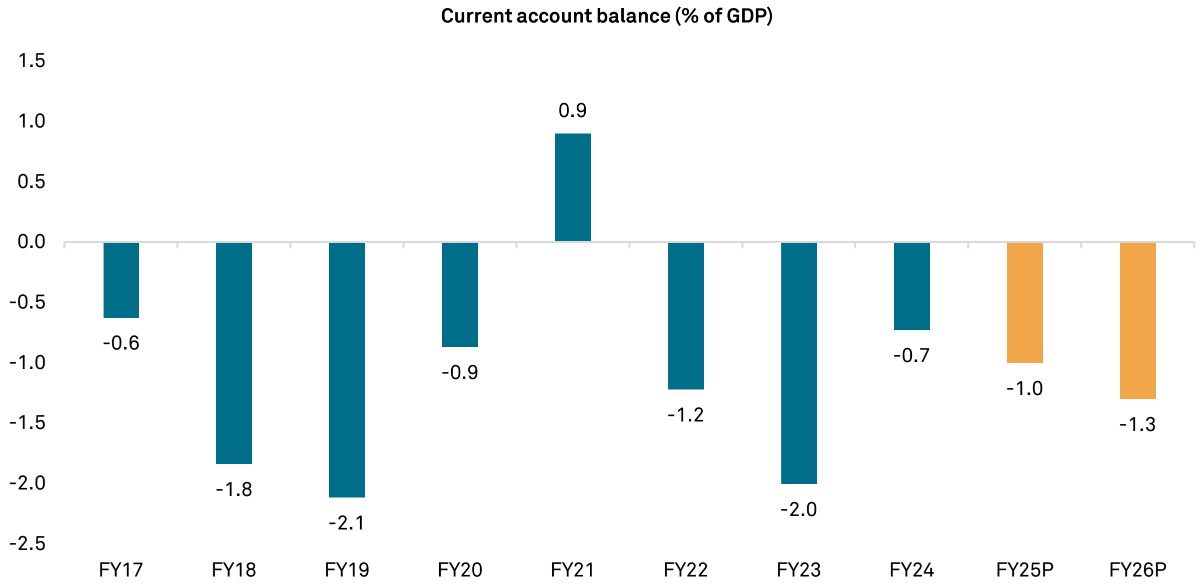
India's current account deficit (CAD) is expected to rise mildly to 1.3% of GDP in fiscal 2026. Given the tariff war initiated by the US, and the subdued global growth environment, India's goods exports are expected to face further headwinds in fiscal 2026. However, due to relatively strong on-year domestic growth and a supply glut in international markets, due to US tariff hikes, goods imports are likely to stay high. Together, this suggests pressure on the merchandise trade deficit.

However, a healthy services trade balance and robust remittance growth will limit the widening.

We expect the rupee to remain volatile and settle at 88 per dollar by March 2026. While geopolitical shocks could keep the rupee volatile, a manageable CAD would mean pressure on the rupee would remain contained.

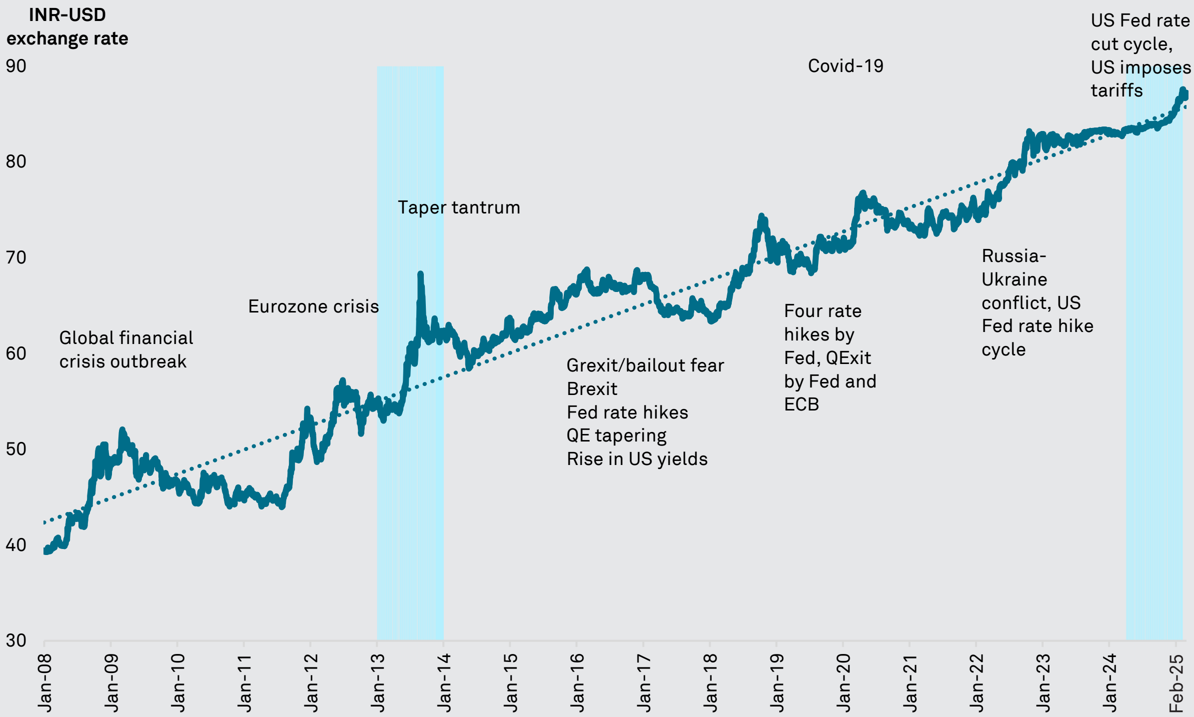
We believe the pressure on the rupee will ease once the uncertainty around US tariffs reduces and an extraordinary surge in the US dollar index normalises. A manageable CAD will help. We anticipate the RBI continuing to intervene in the forex markets to curb excessive volatility.

India's CAD to remain in the safe zone



Note: P - projected
Source: RBI, CEIC, Crisil

Global shocks and the rupee



Source: RBI, CEIC, Crisil

With the rupee coming under pressure in fiscal 2025, we compare the hit with one of the previous prominent periods of rupee depreciation during fiscal 2014.

The currency stress episodes can be expressed as a simple function of shock and vulnerability.

Currency stress = f (shock, vulnerability)

- **2013-14 depreciation:** This episode was characterised by high domestic vulnerability and a single shock of relatively low magnitude. The shock was the US Fed's announcement of a possible tapering of its quantitative easing programme. The vulnerability domestically was high following a high CAD, high fiscal deficit, elevated CPI inflation and low real GDP growth. India was a part of 'fragile five' then. The impact: India saw sharp foreign portfolio investor (FPI) outflows, which, together with a strengthening of the dollar index, caused extreme rupee depreciation. The rupee-dollar exchange rate moved from 58.5 to 63.8 between June and September 2013. In fiscal 2014, the rupee depreciated 11.2%.
- **2024-25 depreciation:** This episode involved reduced vulnerability but more frequent and bigger shocks. Today's macroeconomic situation is much better compared with 2013, with the CAD in a safe zone, inflation lower and an improving fiscal situation. Yet the rupee is depreciating. In fiscal 2025 (April-February), the rupee depreciated 4.4%, with pressure rising significantly after October 2024, driven by a strengthening dollar. Additionally, the outflow of foreign investments from Indian markets since October 2024 and the widening trade deficit have contributed to the rupee's weakness and volatility.
- A regular pattern noticed in currency volatility is that each episode of extraordinary weakening of the currency is followed by a correction. During the 'taper tantrum', the rupee touched 68 in August 2013, but corrected to 60 by March 2014. A similar pattern of depreciation and recovery was noted during and after the Global Financial Crisis.

Global outlook for calendar 2025 and 2026

Significant uncertainty regarding the nature and timeline of tariffs to be imposed by the US has complicated the global outlook. While growth in the US and China is expected to slow down in 2025, the Eurozone, the United Kingdom (UK) and Japan are expected to see a growth uptick.

Protracted uncertainty related to tariffs and other policies poses downside risks to S&P Global's November 2024 baseline scenario for GDP growth presented below[8].

US: S&P Global expects growth to moderate to 2.0% each in 2025 and 2026 from 2.7% in 2024, as per its baseline. However, it cautions that the proposed tariffs on China, Mexico and Canada can reduce 2026 GDP by 0.6% from baseline. This will be a result of reduced household purchasing power, increased investment uncertainty and adverse impact on US exporters.

China: As per its baseline, S&P Global expects China's GDP growth to moderate to 4.1% in 2025 and 3.8% in 2026, from 4.8% in 2024, driven by the imposition of an additional 10% tariff on goods imported into the US from China (taking the effective weighted average tariff from 14% to 25% from the second quarter of 2025).

Eurozone: As per its baseline, S&P Global expects 1.2% growth in 2025 and 1.3% in 2026 vs 0.8% in 2024, as lower interest rates strengthen household purchasing power. While tariffs on the EU have not yet been explicitly announced, S&P Global's scenario analysis assumes a 10% tariff on all merchandise exports to the US beginning in the second half of 2025. In such a scenario, the EU's growth would be below the baseline in 2026 because of reduced trade with the US, as well as increased imported inflation stemming from a weaker currency.

Japan: As per its baseline, S&P Global expects Japan to grow 1.3% in 2025 and 1.0% in 2026, a reversal from the 0.3% contraction in 2024 as household consumption is expected to rise given a pick-up in wage growth.

UK: As per its baseline, S&P Global expects the UK economy to grow 1.5% in 2025 and 1.6% in 2026, up from 0.9% in 2024, with public spending expected to push up growth.

Source: S&P Global

[8] S&P Global Ratings, February 2025, 'Macro Effects of Proposed U.S. Tariffs are Negative All-Around'

Navigating global turbulence

> Anticipated shift in global trade and tariff policies has unsettled emerging markets

In the post-pandemic world, policymakers, particularly in the advanced countries, have been focusing more on resilience than efficiency, leading to a gradual increase in tariffs and insular policies to promote domestic production. Under the leadership of the new US administration, these policies are being implemented with unprecedented vigour.

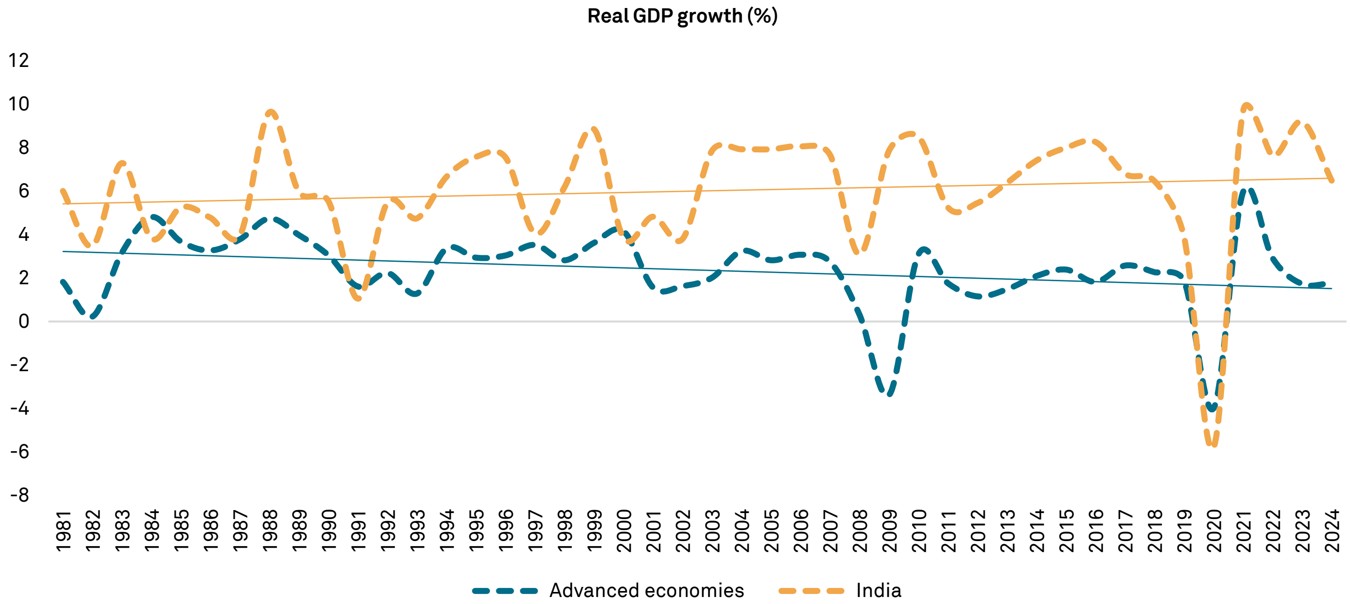
The anticipated shift in global trade and tariff policies, following the US imposition of trade barriers, has unsettled the emerging markets, including India.

However, India has built defences to combat global shocks. Healthy growth, low CAD and external public debt, and adequate forex reserves provide policy flexibility, but do not insulate the country from adverse global developments.

Synchronised cycles, divergent trends

The external shocks of yesteryears may have caused near-term pain but have not dislodged the Indian economy from its upward trend path. Notably, India has continued to raise its growth premium over advanced countries via economic reforms, infrastructure buildout and process improvement.

India's long-term growth path divergent from advanced economies



Note: For India, 2023 means 2023-24
Source: International Monetary Fund (IMF), Crisil

Near-term pain

Case of an outsized shock, in a more integrated world

With the Indian economy becoming integrated into the global market, its exposure to external shocks has increased, particularly through its reliance on imported oil, foreign capital and export markets. India's exports stood at 21.5% of GDP and financial flows at 12.9% of GDP in fiscal 2024.

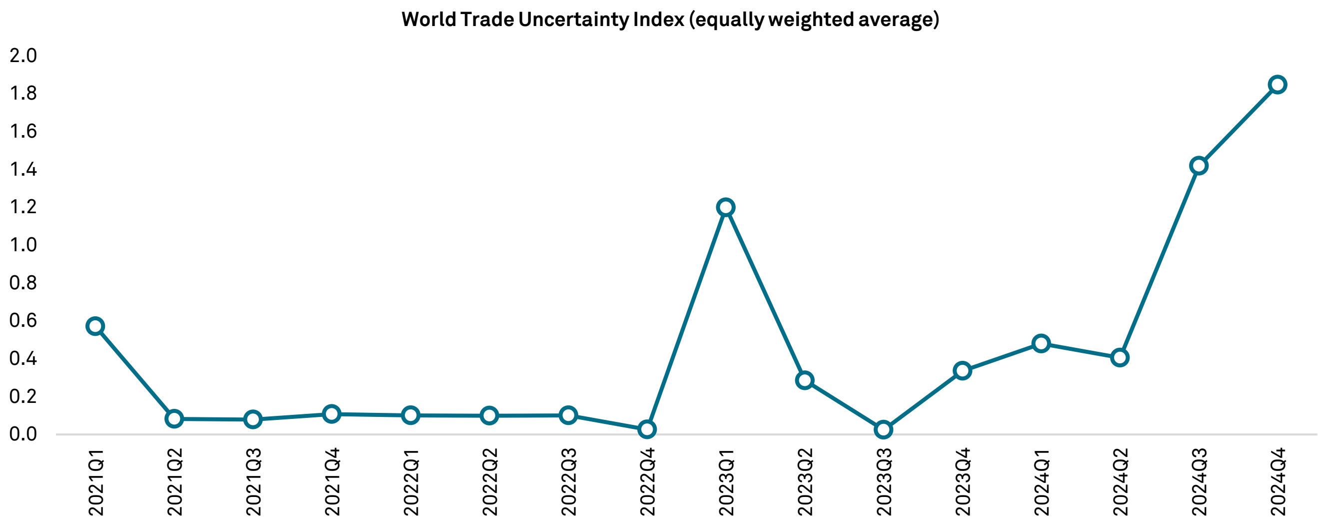
A new set of shocks from current and potential US tariff actions is again testing India's resilience. Such actions can alter trade dynamics, disrupt well-established supply chains and increase uncertainty. Even countries not directly affected by these actions see collateral impact.

The impact can play out via direct and indirect channels — direct via US tariff actions on India and indirect being the collateral damage from uncertainty that the US policy shift has created.

Trade uncertainty spikes

In the December 2024 quarter, the World Trade Uncertainty Index jumped 19.5 times on-year and 3.8 times on-quarter.

World Trade Uncertainty Index (GDP weighted average)



Source: Ahir, Bloom and Furceri (2022), World Uncertainty Index, NBER Working Paper

In fiscal 2026, too, the external environment is expected to be turbulent. A sluggish growth outlook for global trade, increased trade protectionism and a potential threat from increase in imports of cheaper Chinese goods could adversely impact India's merchandise trade balance. Meanwhile, persistent volatility in foreign capital flows could undermine a crucial buffer needed to finance the CAD, maintaining pressure on the rupee.

India is vulnerable to US tariff actions as it runs a trade surplus with the country, which has been steadily increasing over time. In calendar 2023, it amounted to $33.6 billion (goods and services). To boot, with the effective applied weighted average tariff rates levied by India on the US (9.45%) being higher than what the US imposes on India (2.99%), India can face tariff actions[9].

India's trade surplus with the US has been increasing and amounted to $33.6 billion (goods and services) in calendar 2023

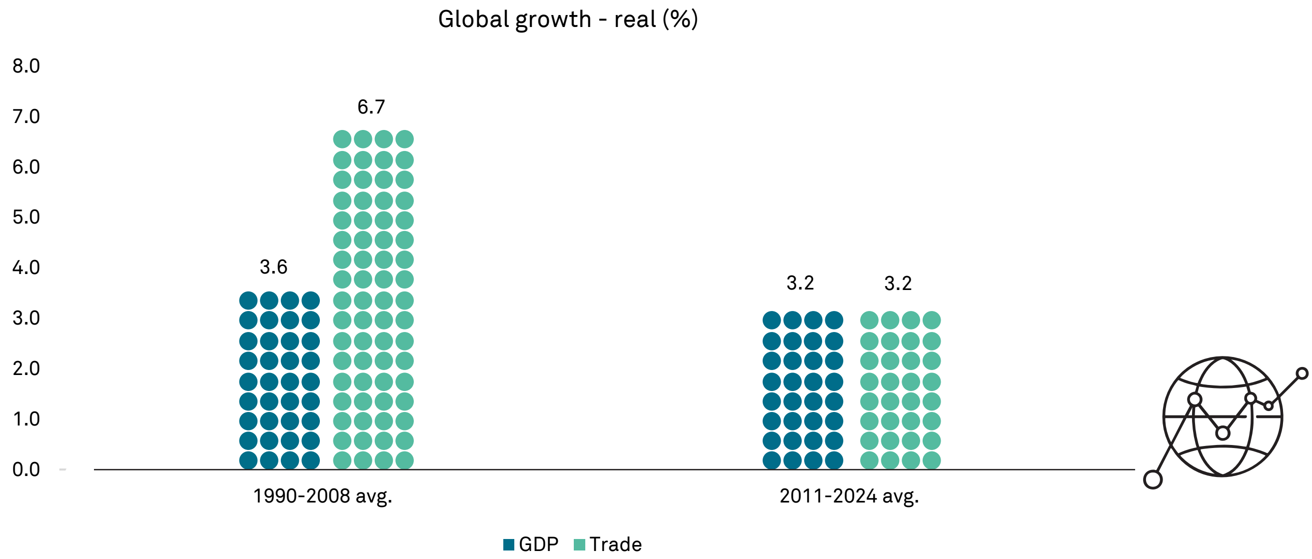
[9]Tariff rates are as of CY 2022

How tariff changes and global turmoil can impact India

I) What will shape the trade outlook in CY 2025

- The United Nations[10] expects global trade volume growth to moderate to 3.2% in calendar 2025 from 3.4% in 2024. The World Bank[11] also expects trade growth to be below the pre-pandemic average (2010-19 average) with about two-thirds of economies experiencing growth below their respective pre-pandemic averages
- This comes on the heels of global trade growth slowing sharply after the 2009 Global Financial Crisis, as countries looked inward and began enacting more protectionist barriers

Global trade growth underwhelmed post the GFC

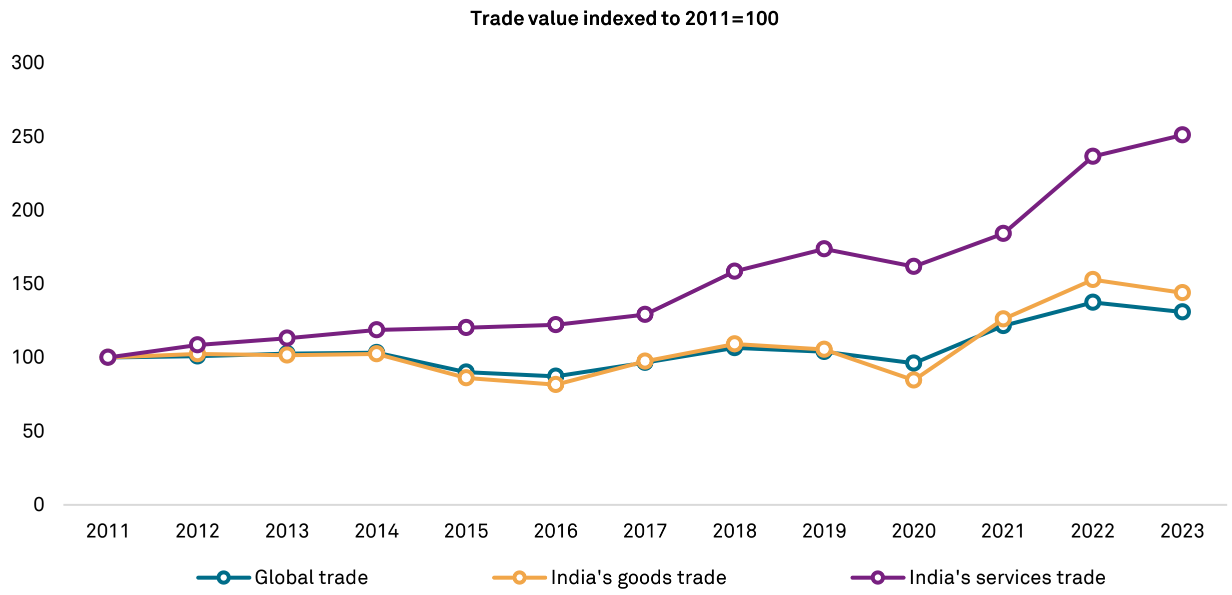


Note: CY 2009 and CY 2010 have been excluded in the above chart due to GFC-related disruption
Source: IMF, Crisil

- According to the aforementioned report by the World Bank, calendar 2024 was marked by a recovery in goods trade, which included the impact of a pick-up in trade in anticipation of higher tariffs
- Services trade, which now represents a quarter of global trade, is expected to see some continued normalisation in 2025, as indicated by proxy parameters such as the global services PMI for new export orders as well as tourist arrivals[12]
- Downside risks, especially to goods trade, arise from complicated geopolitics and increasing trade restrictions

[10]United Nations Department of Economic and Social Affairs, January 2025, 'World Economic Situation and Prospects 2025'
[11]World Bank, January 2025, 'Global Economic Prospects, January 2025'
[12]World Bank, January 2025, 'Global Economic Prospects, January 2025'

India's goods trade sensitive to global fluctuations; services trade provides cushion



Note: Data is for calendar years
Source: World Trade Organization (WTO), Ministry of Commerce and Industry, CEIC, Crisil

- India's goods trade has closely tracked global trade movements in the past. Therefore, any sluggishness in global trade growth could have a negative impact on India. Further, global goods trade itself is more volatile than services trade, partly reflecting the variations in commodity prices

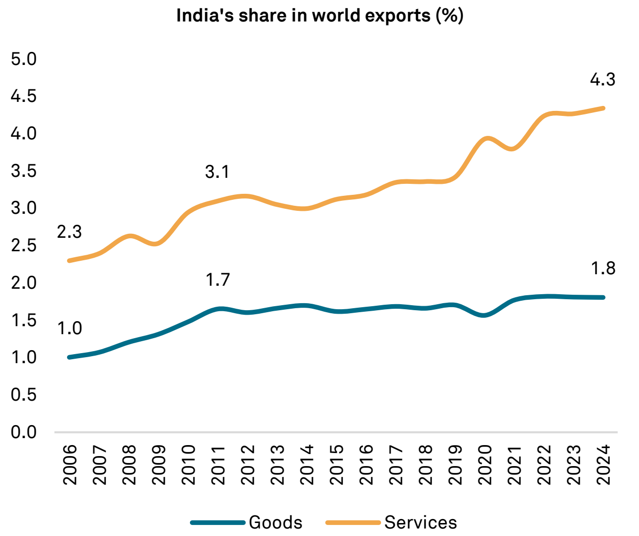
- Although Indian services trade is also mildly impacted by a slowdown in global trade, it has demonstrated greater resilience and remains a crucial buffer for India's export growth, given the rising share of the country's services exports in both global services exports and India's total exports

- While India's share in global goods exports has stagnated at 1.7-1.8% over the past decade and a half, its share in global services exports rose about 1.5 times, from 3.1% in calendar 2011 to 4.3% in 2024. Other than India's lead in software services exports, over the past few years, the contribution of professional, management and consulting services exports has also risen sharply, buoyed by the rapidly rising number of global capability centres (GCCs) in the country

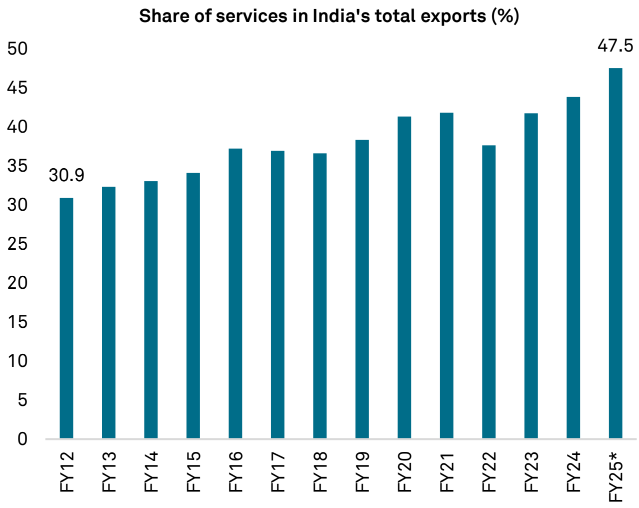
- The share of services in India's total exports has also been on the rise, increasing from 30.9% in fiscal 2012 to 47.5% in fiscal 2025. In January 2025, services exports were higher than goods exports

India's services trade is more resilient to global shocks than its goods trade and, thus, provides a significant buffer for export growth

The rise in India's services exports



Note: Data is for calendar years
Source: UN Trade and Development, Ministry of Commerce and Industry, Crisil



*For Apr-Jan period
Source: Ministry of Commerce and Industry, Crisil

II) Rising tariff and non-tariff barriers

Why is India vulnerable to US tariff actions?

a) India sees a steadily rising trade surplus with the US

- Recent research[13] by Crisil shows that India's merchandise trade with the US has doubled over the past two decades and the merchandise trade surplus has widened 9.8% on average annually over the past decade

India runs a merchandise trade surplus with the US, which amounted to $31.2 billion in calendar 2023. It also records a surplus in services trade, which stood at $2.4 billion in calendar 2023, taking the total trade surplus to $33.6 billion.

India's goods trade surplus with the US has been rising steadily

$ billion	CY06-10 average	CY11-15 average	CY16-20 average	CY21	CY22	CY23	CY24
Goods exported to the US	20.5	38.1	48.4	71.2	80.0	75.7	80.7
Goods imported from the US	15.3	23.0	28.9	41.3	51.3	44.4	42.6
India's merchandise trade surplus with the US	5.2	15.1	19.4	29.9	28.7	31.2	38.1
Services exported to the US	11.5	20.9	28.1	29.0	33.0	36.4	NA
Services imported from the US	8.6	13.2	20.9	18.4	26.5	34.0	NA
India's services trade surplus with the US	2.9	7.7	7.2	10.6	6.5	2.4	NA
India's total trade surplus with the US	8.1	22.8	26.6	40.5	35.2	33.6	NA

Note: Services data has been reported by the US, while goods data has been reported by India; NA is Not Available
Source: WTO, Ministry of Commerce and Industry, CEIC, Crisil

[13]November 2024, Crisil Quickonomics, 'Tale of two trade partners'

b) India currently imposes higher tariffs on the US

- As shown in the table below, on average, India imposes higher tariffs on the US
- India's tariffs on the US are also considerably higher than those imposed on the US by Malaysia (1.84%), Vietnam (2.85%) and China (7.13%)[14], which could lead to further reciprocal tariffs by the US on India

India applies higher tariffs on US merchandise imports

2022 applied weighted average tariffs	All products (%)	Top 10 products imported (%)
India on US	9.45	15.17
US on India	2.99	5.28

Note: The top 10 products have been determined at the Harmonized System (HS) six-digit level. The weighted average tariff rates for the top 10 products have been calculated using the 2022 trade and tariff data. Tariff data on smartphones (HS code: 851713) and one category of diamonds (HS code: 710491) was not available on WITS and has been updated from a United States International Trade Commission website
Source: World Integrated Trade Solution (WITS), International Trade Centre (ITC) Trade Map, United States International Trade Commission, Crisil

c) India's existing non-tariff measures could also come under radar

According to the United Nations Conference on Trade and Development (UNCTAD), "non-tariff measures (NTMs) are policy measures other than tariffs that can potentially have an economic effect on international trade in goods". These include measures such as sanitary and phytosanitary measures and technical barriers to trade. As per UNCTAD database, agriculture, manufacturing and natural resources have been the most affected sectors globally[15].

The debate about what policies come under NTMs has gained traction lately, with the US administration's recent rhetoric indicating taxation such as value-added taxes (imposed by many countries) should also be considered under this category as it allegedly discriminates against imports. The administration has indicated it would impose reciprocal tariffs on countries based on tariff and NTMs such as value-added taxes, extensive regulatory requirements and currency undervaluation. Importantly, given their subjective nature, it becomes difficult to assess impact of such NTMs and steps taken in response.

India's tariffs on the US are higher than vice versa. They are also higher than those imposed on the US by Malaysia, Vietnam and China

III) The indirect impact of tariff wars: The threat of cheaper imports from China

As the US imposes higher tariffs and raises trade barriers on imports from China, these commodities could be diverted to other countries, including India, which already imports heavily from China. According to S&P Global[16], if the US weighted average effectively applied tariff on China increases from 14% (current) to 25%, its growth will decelerate to 4.1% in CY 2025, and inflation will decline as excess capacity in China rises. While cheaper input could benefit Indian manufacturers, those competing with cheaper imports of intermediate and finished goods could see an adverse impact on their sales and margins.

According to Crisil Intelligence, Indian flat steel prices slipped almost 10% in fiscal 2024 as a result of a flood of steel imports from China. Steel prices could see further downside going forward (refer to the 'US reciprocal tariffs could potentially impact exports and price dynamics of key sectors' box in the 'Steady infra spending by Centre to continue' chapter). India's trade deficit with China is already expanding at a rapid pace and stood at $65.2 billion in fiscal 2025 (Apr-Nov) — the largest India had with any partner. Over the past decade (fiscal 2014 to fiscal 2024), imports from China have doubled, led by electrical equipment, electronics, machinery, organic chemicals, plastic and steel. Meanwhile, India's exports to China have stagnated[17].

[14] Tariff rates for Malaysia, Vietnam and China are also applied weighted average rates
[15] UNCTAD cited in the Economic Survey 2024-2025, Government of India
[16] November 2024, S&P Global Ratings, 'Economic Research: Economic Outlook Asia-Pacific Q1 2025: U.S. Trade Shift Blurs The Horizon'
[17] November 2024, Crisil Quickonomics, 'Tale of two trade partners'

IV) Capital flows to remain volatile

Increased uncertainty around the nature and impact of the new US administration's policies and potential retaliation from other countries have strengthened safe-haven sentiments. This has led to capital outflows from the emerging markets back to the US, adversely impacting emerging-market currencies.

According to an RBI study[18], the CBOE Volatility Index, also called the VIX Index (a proxy for market volatility and, hence, investor uncertainty), impacts the rupee exchange rate volatility. The index rose to an average of 17.0 in February 2025 from 12.7 in June 2024 (lowest monthly average of 2024).

Capital outflows from India (particularly in the equity segment) have been driven by steadily climbing yields on the US 10-year Treasury bonds, increasing from an average of 3.72% in September 2024 to 4.45% in February 2025. The risk of rising inflation and slower rate cuts from the Fed have pushed the US yields up, and risk aversion has triggered capital flight out of emerging-market equities, including in India.

With foreign direct investment (FDI) already seeing weakness, the recent spike in FPI outflows raises concern given that the latter provides a significant cushion for the CAD.

The impact so far (November 2024 to February 2025)

- **Capital outflow:** Foreign capital inflows (net) totalled $21.6 billion in April to September 2024, but then saw outflows of $23 billion in October 2024 to February 2025
- **Rupee volatility:** The rupee, which stood at 83-84 per US dollar, crossed 87 per US dollar in recent months
- **Existing domestic buffer:** During April to December 2024, the RBI net-sold dollars worth $36.1 billion to smoothen currency movements as the dollar gained strength. Interventions have continued, and forex reserves are lower at $640.5 billion as on February 21, 2025, compared with $656.6 billion in November 2024

India's external sector is resilient, given comfortable external debt servicing commitments, improving domestic macroeconomic situation and sufficient forex reserves

V. How resilient is India to global shocks?

India's external vulnerability is low and reasonably well covered by existing forex reserves:

- **Forex cover:** Robust forex reserves (covering 10-11 months of imports) provide a crucial buffer against external shocks, despite the recent decline
- **India's short-term external liabilities:** CAD and external debt are low and within comfortable levels
- **High growth premium:** India is the fastest-growing large economy, projected to expand 6.7% per year until the end of the decade. The recent focus on ease of doing business through deregulation should be thoroughly implemented to ignite domestic growth drivers and create an upside for growth
- **Fiscal prudence:** Sustained fiscal restraint is helping tame the fiscal deficit and has put debt on the path of consolidation. This is critical as India has a high debt ratio vis-a-vis similarly rated countries

[18] January 2025, Patra, M.D., Kumar, S., John, J. and Acharya, A., RBI Bulletin, 'Foreign Exchange Intervention: Efficacy and Trade-offs in the Indian Experience'

Healthy external markers create buffer

		Taper tantrum	US-China trade tiff	Covid	Wars			Trade tiff
Indicator		**FY13**	**FY19**	**FY21**	**FY23**	**FY24**	**FY25F**	**FY26F**
External liabilities	CAD (% of GDP)	4.8	2.1	-0.9	2.0	0.7	1.0	1.3
	External debt (% of GDP)	22.4	20.1	21.4	18.6	18.8	18.5#	
	- Short-term external debt (% of GDP)	5.3	4.0	3.8	3.8	3.5	3.4#	
Adequacy of forex reserves	Months of import cover	7.2	9.4	18.0	9.7	11.4	10.6^	
	Reserves/(short-term debt + CAD)	1.6	2.5	7.5	3.0	4.2	4.1#	
Domestic macroeconomic health	GDP growth (% y-o-y)	5.5	6.5	-5.8	7.6	9.2	6.5	6.5
	CPI inflation (% y-o-y)	9.9	3.4	6.2	6.7	5.4	4.7	4.4
	General† govt deficit (% of GDP)	7.5	7.8	8.8	9.2	7.8	7.3	7.0
	General† government gross debt (% of GDP)	67.7	76.5	84.7*	84*	83.7*	82.9*	81.7*

Note: F - Crisil forecast, †Combines Centre's and subnational fiscal position, adjusting for duplications
^As of January 2025, #as of September 2024, *estimates by S&P Global (December 9, 2024)
Source: RBI, NSO, Ministry of Commerce, S&P Global, Crisil

Vulnerability indicator

- High
- Neutral
- Low

VI. Need to strengthen trade buffers

Clear tariff policy

- India should have a clear long-term import tariff policy for inputs, intermediates and final products. This will create a predictable tariff regime and positively impact investment sentiment, particularly in the manufacturing sector, which India is trying to leverage as its key growth engine
- Lower tariffs on imports of raw materials and components have benefited sectors such as electronics and pharmaceuticals in India. This strategy will remain significant for value-added manufacturing

Fostering trade alliances

- India has already signed trade agreements with Mauritius, the United Arab Emirates, Australia and the European Free Trade Association in recent years, while negotiations with several others, including the EU and the UK, are ongoing
- With the trend of developing regional supply chains, India could benefit from joining regional trading blocs, especially the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). Competition from low-cost Chinese imports is not a concern, as China is not part of the CPTPP

Trump tariffs, global inflation and interest rates

By **Paul Gruenwald**
Global Chief Economist
S&P Global Ratings

The Trump administration has made an aggressive start in the area of tariffs.

The first action taken was to raise tariffs on Chinese imports by an additional 10%. Tariffs of 25% on imports from Canada and Mexico were put on the table at the same time, but have been paused for now; if implemented, these are likely to cause recessions in both economies.

Subsequently, President Trump levied tariffs on all steel and aluminum imports into the US, but these will not move the overall macro needle in our view, although they will hit the auto and construction sectors. Most recently, the Trump administration has proposed reciprocal tariffs (equalising tariff rates) against all trading partners as well as an additional 10% tariff on China.

Needless to say, the situation regarding tariffs is in flux.

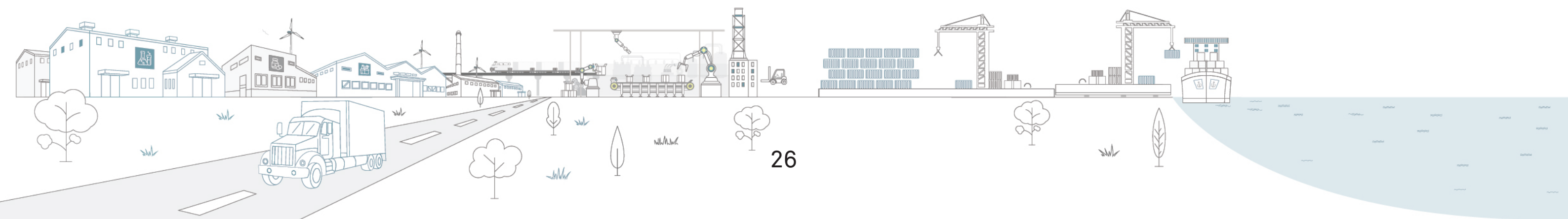
Markets have begun to weaken as elevated policy uncertainty takes hold. The US dollar is 7% higher than end-September 2024, after rising by 10%. The benchmark 10-year Treasury yield is up 40 bps (to around 4.2%) but has fallen by half a percentage point in the past few weeks. Finally, equity markets have fallen as well of late after a 7% post-election rise. US policy uncertainty (measured by the Fed) has jumped levels last seen during the Global Financial Crisis and the Covid-19 pandemic. The consensus view is for rising downside risks.

Inflation continues to trend towards central bank targets in the major economies. But progress has stalled or even reversed in recent months. Services inflation has eased a bit, but now goods inflation is starting to rise again. Slowing growth and demand, including due to tight financial conditions, should drive inflation pressures lower in 2025. US inflation came in surprisingly strong in January, reflecting prices of energy and eggs, providing further evidence that achieving the 'last mile' of inflation reduction (from 3% to 2%) will be challenging.

Central banks continue to reduce their policy rates, albeit gradually. The Bank of Canada leads the pack with an accumulated 200 bps of cuts since the middle of 2024. The European Central Bank follows at 125 bps. Central banks for Canada, the Eurozone and the UK all cut rates in their first meeting of 2025, while the US Federal Reserve held rates steady. We think the window for Fed rate cuts this year is closing. The Reserve Bank of Australia is the outlier, with a first rate cut in February 2025.

We are watching the growing gap in the US between the steady sentiment, or deteriorating data and the activity-based, or hard data.

How the gap resolves will be the key to our outlook for the remainder of 2025.



Global disquiet, local drivers

By Neelkanth Mishra
Chief Economist, Axis Bank
Head of Global Research and
Wholetime Director, Axis Capital

As the world moves from multilateralism to bilateralism, geopolitical alliances, some going back several decades, are getting disrupted.

The switch from global to local optima in general is net negative for the global economy. Further, the first salvos in the trade wars have just been fired, and the cycle of strikes and counterstrikes is likely to take several years and could widen to involve currencies and other tools of industrial policy.

This uncertainty itself is likely to be a drag on global growth, slowing down investments. The advent of artificial intelligence holds promise, despite it being yet another front for geopolitical conflict, but economic gains may be several years away.

Disruptions often provide opportunities, and India can and should try to take advantage of the reset in global value chains, especially as its current share of global goods trade is very low.

However, as India rethinks its economic roadmap, it must keep in mind that it would be domestic demand that drives a large part of economic growth in the next decade or two.

When the economy expands from around $4 trillion to $20 trillion (whenever it achieves that milestone), of the $16 trillion dollars of incremental GDP, not more than $1 trillion would be from a change in net exports.

Even today, despite being the largest manufacturing economy the world has ever seen, China's goods trade surplus is only around 1 trillion dollars annually. For the rest, it relies on domestic demand.

Trade openness, after all, is most effective through the productivity channel — being forced to compete with imports and in export markets makes domestic firms more efficient.

A large part of the capital stock in developed economies comes from housing and infrastructure, and India has a long distance to cover on both fronts.

Policymakers would need to manage the real-estate cycle better, not just because it is a large source of domestic demand, but also as it is an important driver of economic cycles, and mortgages are the most potent channel through which monetary policy works.

Similarly, the financing and construction of urban infrastructure may not be possible without significant shifts in political, fiscal and administrative systems.

Nearer-term, recovery from the recent economic slowdown is also dependent primarily on local factors.

Prolonged liquidity stress, which is depressing credit growth, is intensifying, as visible in the high and rising cost of liquidity and exacerbated by deposit shocks generated by lumpy currency market interventions.

Research shows that such shocks lower credit supply and hurt economic growth.

Global studies show only a rise in non-borrowed reserves (for example, through open market purchases of government bonds) can help in such situations.

As currency volatility is likely to persist, a stronger signal on liquidity may be needed for credit growth to pick up, which is critical for economic revival.

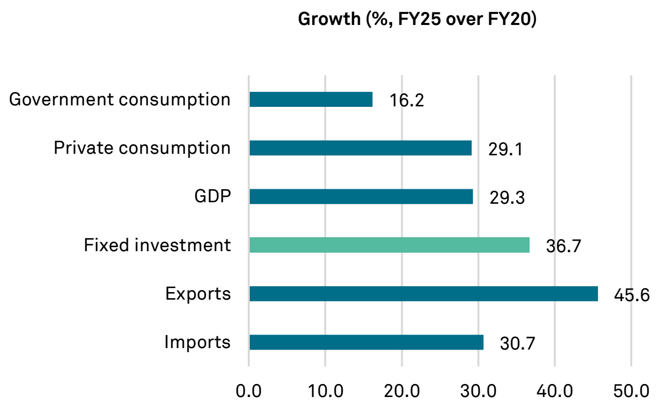
Tracing the investment story

Changing strategies and shifting gears crucial to unlocking investment potential

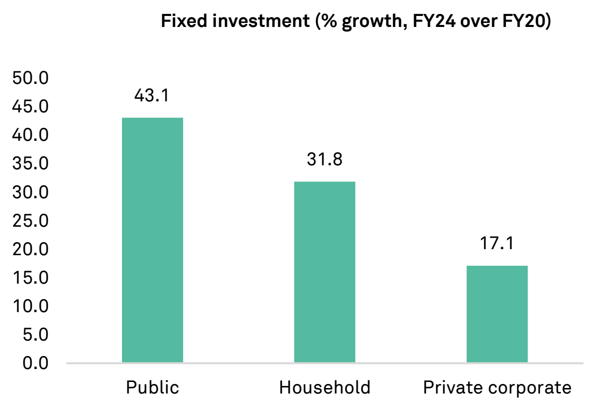
Fixed investments by households and the government have driven the post-pandemic investment recovery in the country. But it is time for the private sector to play a larger role. There are four reasons why:

1. The pick-up in investments has supported GDP growth of 8.8% in the past three fiscals, i.e. fiscals 2022-2024.. But the overall investment ratio is now stagnant at 33-34% following the initial lift. To achieve the 'Viksit Bharat' goals, the country needs higher growth and investment rates.
2. The government, which has been the other key driver, is now normalising its capex to trim its debt burden. Central-government capex is budgeted to grow at the same pace as nominal GDP in fiscal 2026. During fiscals 2022-2024, budgetary capex allocations had exceeded nominal GDP growth.
3. Household investments in residential real estate are also a prominent driver of fixed investments in the country. Several cyclical factors during and post the pandemic — income growth in certain segments, stamp duty relaxations in select states, low interest rates and a push to lending — drove up the share of households in total fixed investments to 41% during fiscals 2022-2024. Other drivers will also need to step up investments.
4. Private corporate investments have been sluggish so far. For a full-fledged and sustainable revival in overall capex, the private corporate sector will need to regain its position as a key driver of investments. A vibrant private corporate sector helps build competitiveness and drives innovation, which is critical given the current challenges posed by technology and the uncertain global environment. A sustained rise in corporate capex is, therefore, critical to unlocking India's long-term growth potential. A shift in the government's strategy to deregulate the economy has been promised in the budget, which needs to be thoroughly implemented. The intent is to ease restrictive regulations in identified sectors to foster entrepreneurship, competition and efficiency and provide the private sector a level-playing field with global competitors. This can not only help attract FDI but also usher in domestic investment.

Investments have driven the recovery...



...led by households and the public sector



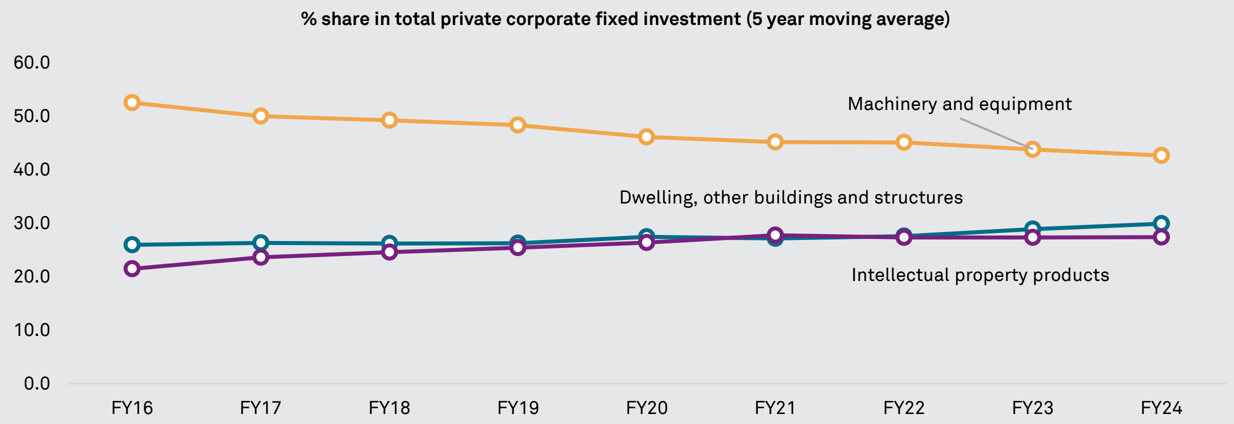
Note: Charts indicate cumulative growth over the indicated period. Growth rates are in real terms
Source: NSO, Crisil

What ails private investment?

The share of private corporate investment in total fixed investment saw a sustained decline to 34.4% in fiscal 2024 from its peak of 41% in fiscal 2016, following a steady climb from ~33% in fiscal 2012. The nature of private corporate investment has also seen a shift in recent years, which the Economic Survey 2023-24 notes as an 'unhealthy mix' (see box below: 'Changing trend in private corporate investment').

A revival in private corporate investment will need to be accompanied by faster growth in machinery and equipment (or capacity addition) and intellectual property creation (or innovation).

Changing trend in private corporate investment



Source: NSO, Crisil

- Investments in machinery and equipment and intellectual property products have slowed, while those in real estate or dwellings, other buildings and structures have accelerated
- Such an adverse change in the mix, the Economic Survey notes, "can delay India's quest to raise the manufacturing share of GDP, delay the improvement in India's manufacturing competitiveness, and create only a smaller number of higher-quality formal jobs than otherwise"

A Crisil Ratings analysis[19], based on data from 900 companies, finds that capex intensity, measured as capex over Ebitda,[20] remains moderate, averaging 50% over fiscals 2024 and 2025, as against the decadal high of 72% during fiscal 2016. This, together with lean corporate balance sheets, implies that India Inc has significant financial headroom to support broad-based capex as utilisation levels rise.

What works and what does not for private corporate investments?

The willingness to invest does not match the ability to invest. The ability to invest is influenced by the balance-sheet position of the borrower and lender, whereas the willingness is defined by factors such as demand conditions and global uncertainty.

[19]Crisil Ratings Round-up: First half, fiscal 2025, October 2024
[20]Ebitda: Earnings before interest, taxes, depreciation and amortisation

Ability to invest is high

- **India's private sector is in a better position to invest, compared with a decade ago**
  - Secular deleveraging by private corporates has significantly strengthened their balance sheets and provided financial flexibility. This improvement has been broad-based, facilitated by low capex, the government's strong focus on infrastructure push, new issuances in the equity market (which also supported balance-sheet strengthening), some improvement in capacity utilisation (from the lows), and ploughing back profits to retire debt
  - For Crisil-rated entities, the median gearing ratio —which is defined as the ratio of a company's debt to its net worth — has improved from 1.05 times in fiscal 2015 to an estimated 0.50 times in fiscal 2025 across corporates, indicating there is more than enough headroom in the corporate balance sheets to undertake debt-funded capex
  - Meanwhile, India Inc's revenue and profitability have also seen a sustained improvement
- **The position of lenders is healthier**
  - As stressed assets in the corporate sector increased, gross non-performing assets (GNPA) in the banking sector peaked to 11.2% by March 2018. Hence, banks turned cautious in lending to this segment
  - Over time, the GNPAs have declined, supported by lower slippages, recoveries from legacy stressed assets as well as write-offs. They are expected to touch a low of 2.5% of advances as of March 2025, facilitating better credit availability to industry and private corporates
  - Between fiscals 2017 and 2021, the central government recapitalised the public-sector banks by over Rs 3.3 lakh crore, which helped them clean up their balance sheets as well as strengthen their capital position. This, too, has played a key role in improving the banking sector's ability to lend
  - The monitorable, however, remains the deposit growth of banks
- **Policy intervention has been supportive**
  - The government has played a crucial role in incentivising industrial capex through the PLI scheme. This is in addition to the Make in India initiative (liberalised FDI in India), reduction in corporate tax rates, creation of large-scale infrastructure (aimed at building logistical efficiency and reducing costs), implementation of goods and services tax (GST) and setting up of digital public infrastructure

Stifled willingness

- Uneven consumption demand recovery, a constraint for investment revival
  - In the post-pandemic period, private consumption has been the slowest growth component to recover. Additionally, the uneven pick-up has kept the private sector cautious about investments
  - The RBI's Consumer Confidence Survey, which captures urban sentiments, dipped below the 100 mark in June 2017 and has seen a sluggish recovery since then.
  - The dip in private consumption growth to 5.6% in fiscal 2024 was on account of weak rural demand. In fiscal 2025, the recovery to 7.6% was facilitated by a low base, improved rural demand (due to healthy agriculture incomes) and a decline in consumer price inflation. Urban demand, in contrast, felt the heat due to higher interest rates and tighter lending norms, mainly for unsecured loans
  - Capacity utilisation in the manufacturing sector has stagnated at ~74% since fiscal 2023, as per RBI data
- **Global policy uncertainty — a headwind for domestic investments**
  - Globally, geopolitical tensions and uncertain trade conditions — including the new US administration's tariffs — have led to shocks to global demand, supply chains, and energy and commodity prices, resulting in postponement of investments
  - The Global Economic Policy Uncertainty Index[21], which has been rising steadily since 2010, peaked during the pandemic and has risen again following a rise in global trade uncertainty
  - The most recent of the shocks is the ambiguity and heightened uncertainty caused by accentuation of tariff actions by the US administration. The

[21]Source: 'Measuring Economic Policy Uncertainty' by Scott Baker, Nicholas Bloom and Steven J. Davis at www.PolicyUncertainty.com

- direct impact of this shock will play out once the affected countries implement reciprocal tariffs. But it has already resulted in capital outflows from the emerging markets, weakening of currency and fear of dumping from China. This has made the environment highly uncertain, which jeopardises investment decisions in the short term as private corporates await clarity

Corporate investments to improve gradually

Corporate investments will increase gradually as the government has taken steps to address domestic demand and ease conditions for the private sector to invest, amid heightened global uncertainty.

The tax breaks introduced in the budget for the middle class will continue to play out over the years and bolster domestic discretionary consumption. Lower lending rates and softer inflation, too, will support purchasing power. Welfare initiatives that provide employment under schemes such as the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) scheme, PMGSY and PMAY will cushion incomes for low-income households. These, together, will help consumption to hold up and improve capacity utilisation rates for manufacturers.

That said, a sustained increase in private consumption over the medium term will require a durable rise in employment opportunities and household permanent incomes.

Importantly, supportive policy intervention, in the form of easing bottlenecks created by restrictive regulations, will reduce bureaucratic delays and improve transparency. The Economic Survey 2024-25 batted for deregulation as a crucial component to unlocking the true potential of domestic-led growth over the medium term, which the budget reiterated. A thorough implementation of these is necessary to provide stable support to private investment.

But uncertainty arising from global geopolitical developments/tariff actions will keep private corporates cautious about investments.

A balancing act between manufacturing and services

Over a seven-year period (fiscals 2025-2031), we expect India to sustain average GDP growth of 6.7%. This, over a similar growth rate seen in the pre-pandemic decade (fiscals 2011-2020), is expected to compound the gains for the economy (refer to Crisil Intelligence report titled, 'Growth marathon: Emerging sectors, investments, efficiency gains priming India's medium-term pace', March 2024).

Despite faster manufacturing growth, services will remain the primary growth driver

- We expect manufacturing growth to average 9.0% per year over the medium term (fiscals 2025-2031), up from 6% average in the pre-pandemic decade
- Compared with manufacturing, the services sector is expected to grow at a slower pace over fiscals 2025-2031, at an average of 6.8% per year. This growth will also be slower than the 7.7% average of the pre-pandemic decade
- As per our estimates, the share of manufacturing in GDP will rise to ~20% by fiscal 2031 from an estimated 17.2% in fiscal 2025. The share of services is forecast to be stable at ~55%. In contrast, the agriculture share is projected to fall to ~12% from 14.4%
- The speed with which India's manufacturing grows will critically hinge on:
  - Pace of development of its logistics
  - Improvement in its ease of doing business via deregulation
  - Its stance on global tariff wars
- Services today find a plug-in into most economic activities, but in different proportions. Among these, interlinkages between services and industry are significant. Therefore, services sector inputs will see higher demand as the manufacturing sector grows
- The rise of the digital platform and gig economy with digitalisation has also increased the scope for growth of the services sector. In particular, the development of Aadhaar, India Stack and payments infrastructure has aided growth of new private-sector companies and startups in the financial and other services segments

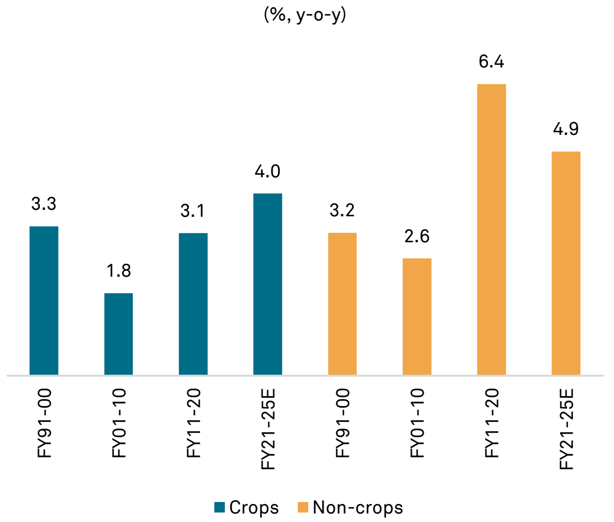
Composition of agriculture to change despite a falling share

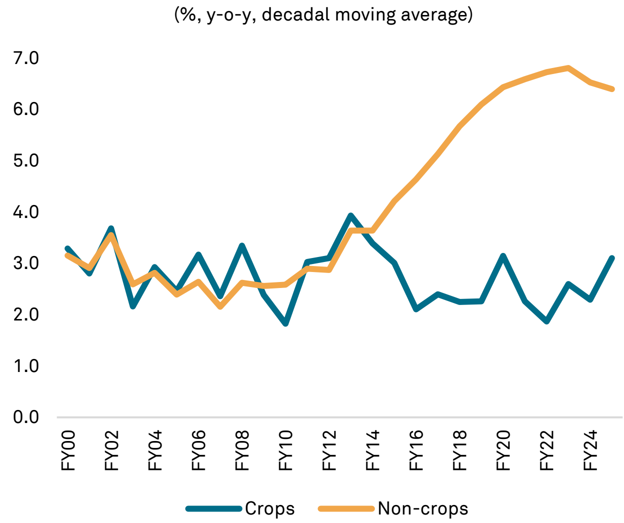
- The contribution of agriculture and allied sectors to overall gross value added (GVA) stood at 15.2% for the last decade, down from over 20% two decades ago. As agriculture growth trails overall growth, its share will decline to ~12% by fiscal 2031
- India's foodgrain production grew at an average of 2.8% during agriculture years 2021-2024, slower than 4.3% in 2017-2020. That was also slower than the decadal average of 3.3% during agriculture years 2011-2020. Horticulture production growth was relatively low at 2.5% during agriculture years 2021-2024 versus 2.8% in 2017-2020 and 3.7% in 2011-2020 (refer to Crisil Insight titled, 'Time for structural strike on inflation: Slower food output growth calls for more fiscal policy measures, reforms', December 2024)
  - Weather shocks are the prime factor behind slower yield and production growth. Even in years when monsoons have been broadly normal on average, the erratic distribution of rainfall, both in terms of time and geography, has affected production. Depleting groundwater levels due to heatwaves and higher temperatures have also impacted yields
- Interestingly, the sub-components of this sector have seen shifts that suggest rural folks have been cushioning incomes from disruptions in the agriculture sector by diversifying away from traditional crop agriculture

– The allied sectors, which include livestock, fishing and forestry, are now playing a larger role in driving total agriculture GVA, while the share of traditional crop farming is declining. Average growth of 6.4% in allied sector GVA during fiscals 2011-2020 is strikingly higher than growth of 3.1% in crop GVA. A decade ago, the share of crops in agriculture GVA stood at 62.2%, which dipped to 54.6% in fiscal 2024, according to the latest available data

A distinct decline in dependence on crops cultivation while allied activities gain prominence

Agriculture and allied sectors GVA





Note: E - estimate
Source: NSO, Crisil Intelligence

- Fiscal policy and reforms that increase agricultural yields, productivity and supplies are crucial to raise the contribution of this sector to the economy
  – India needs faster growth in crop yields to boost agricultural productivity and catch up with the rest of the world. But changing weather patterns in recent years have played spoilsport
  – The agriculture sector can combat climate change only by building resilience in the production, logistics and transport stages
  – Weak private-sector investment and participation in agriculture make it imperative for the government to step in and boost productivity

How reforms can boost medium-term growth

If India wants to raise its growth potential, addressing structural inefficiencies of the economy is important. This is where reforms play a role, as they address issues hindering economic activity. The resultant productivity gains can raise GDP growth. Reforms can also boost animal spirits and ‘crowd in’ private investments.

The Economic Survey 2024-25 talked about deregulation as the way to spur medium-term growth. It has provided a comprehensive list of areas, including land, labour and construction, where there is scope to ease regulation. The list is large, requiring efforts from both the Centre and states.

We briefly take stock of the trajectory of reforms in India so far. The graph below gives a timeline of big economic reforms implemented since 1991. It shows the maximum intensity of reform implementation happened in two periods — calendar years 1991-1995 and 2016-2020.

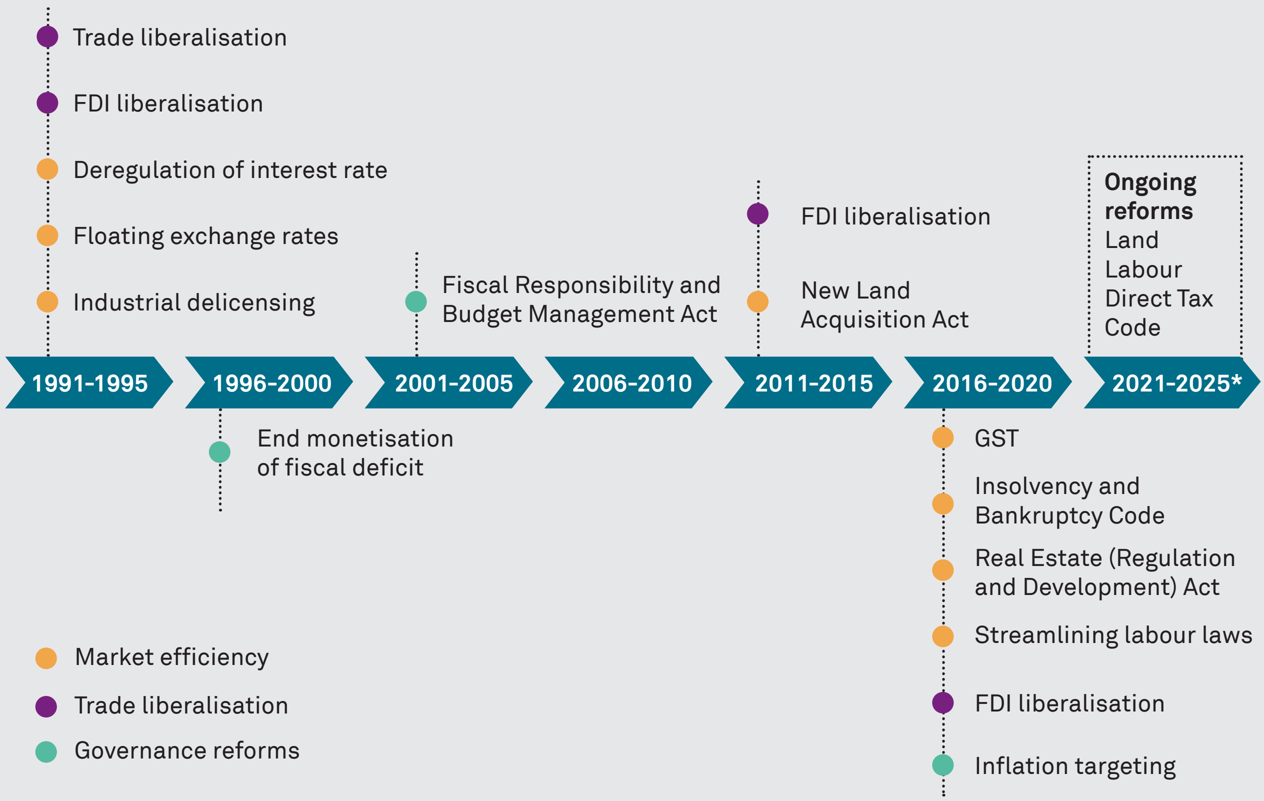
Post-pandemic, the government’s focus has been on improving infrastructure, which helped increase logistical efficiencies. Some steps have been taken to reduce compliance burden, such as the introduction of the new

Income Tax Code. Ground is being prepared for the next stage of reforms in land (by improving rural land records with the Swamitva Scheme) and labour (by streamlining labour laws into four codes).

However, significant inefficiencies persist in doing business due to high land costs, changing regulations, weak contract enforcement and high cost and time of dispute resolution. Hard reforms on agriculture, administration and judiciary are pending as well.

Relentless efforts in this direction will boost efficiency gains for India.

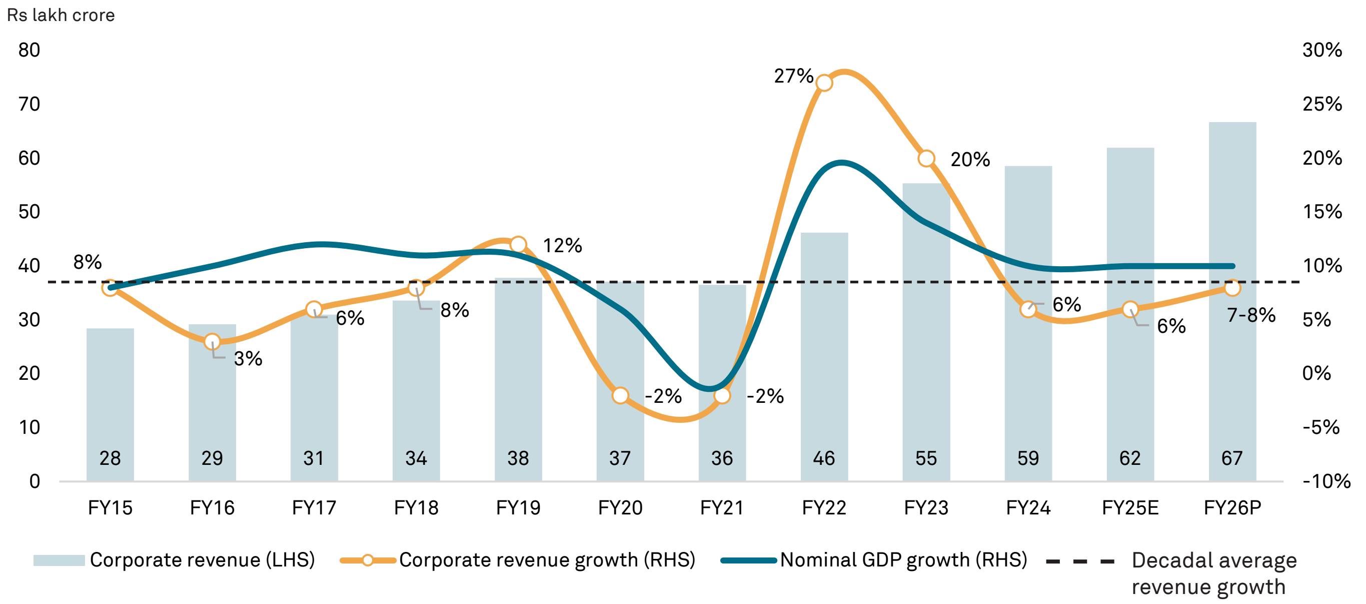
Timeline of key economic reforms in India



Note: 2025 data is until February
Source: Crisil Intelligence

Consumption sectors to drive revenue growth in fiscal 2026

Corporate revenue to grow 7-8% in fiscal 2026, a tad higher than the previous year



E – estimated, P – projected
Note: 1. Analysis based on 798 listed corporates, excluding oil and gas and banking, financial services and insurance (BFSI) companies, representing ~65% of the market cap of all companies that traded on BSE on April 1, 2024
2. Black dotted line represents decadal average annual corporate India revenue growth rate from fiscals 2016 to 2025
Source: Quantix, company reports, Crisil Intelligence

Corporate India's revenue growth is expected to improve to 7-8% on-year in fiscal 2026 vs ~6% in fiscal 2025, closing in on the decadal average of ~8% growth as seen during fiscals 2016 and 2025. This will be led by healthy growth in consumption sectors such as organised retailing, fast-moving consumer goods (FMCG), consumer durables, airlines and two-wheelers.

Aggregate growth of consumption sectors (with a 21% share in corporate revenue) is expected to outpace nominal GDP growth, led by the twin effect of revised tax slabs announced in Union Budget 2025-26, which will increase disposable income, and a 25 bps rate cut announced by the RBI in February. Notably, rural demand will support growth of consumer staples. The growth in these sectors will be largely volume-led.

Commodity sectors, especially metals, will continue to drag down growth due to prevailing pricing pressure. Also, growth in the construction sector will remain tepid.

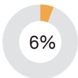
Key risks to corporate performance in fiscal 2026 are as follows:

- Our base case scenario factors in a normal monsoon and, thus, La Niña will remain a monitorable. The La Niña effect, an extreme weather pattern, persisting through early calendar year 2025, can impact crop yields. In such a case, most of India may see above-normal rainfall, except the extreme north and northeast regions, where below-normal rainfall is likely, as announced by the Ministry of Earth Sciences in December 2024
- Given the tariff war initiated by the US and the subdued global growth environment, India's goods exports may face further headwinds in fiscal 2026. This may add downside risks to revenue of sectors such as textiles, pharmaceuticals and solar modules (refer to page 52)

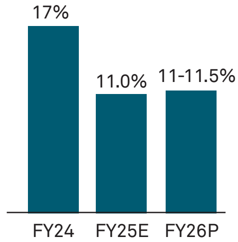
Sector-wise revenue outlook

Consumption sectors, accounting for ~21% of revenue, will continue to outpace nominal GDP growth in fiscal 2026

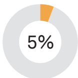
Consumer discretionary products



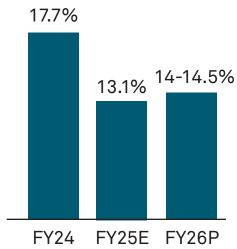
Revenue of the cars and UVs industry will be driven by higher realisation growth of 5% because of a favourable product mix and the continuing shift to sport utility vehicles and premium variants of vehicles. However, volume growth will remain muted owing to high inventory. Volume growth of 9% will drive two-wheeler revenue growth as rural sales remain healthy and deferred replacement demand kicks in. Together, these industries account for about three-fourths of the sector's revenue.



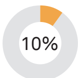
Consumer discretionary services



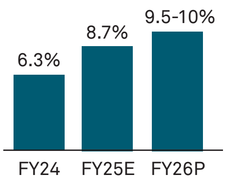
The organised retail industry (~60% of the sector's revenue) is expected to witness healthy revenue growth because of rising penetration into Tier 2 and 3 cities and improved consumer spending. The airline industry, which accounts for about a fourth of the sector, will continue to be driven by strong traffic growth, led by international passenger traffic and increase in supply as fleet availability improves. This will result in volume growth of ~10% for the airline industry in fiscal 2026.



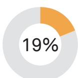
Consumer staples



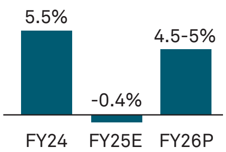
After witnessing sluggish volume growth in fiscal 2025, the FMCG industry, accounting for ~40% of the consumer staples sector revenue, is poised for a demand rebound, driven by increased consumer spending. Volumes are expected to increase 6% on-year, spurred by tax cuts and the revival in rural consumption owing to better rabi harvest and increased government outlay towards farmers in the form of rural and welfare schemes.



Commodities

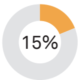


The steel industry revenue is anticipated to rebound, driven by robust demand. While pricing pressure may continue till the imposition of safeguard duties to restrict imports, overall revenue in fiscal 2026 will be driven by 10% volume growth. For the cement sector, demand momentum is set to improve in fiscal 2026 with traction from infrastructure and rural housing segment, leading to ~7% on-year volume growth. After a decline of 1% in fiscal 2024 and 6% in fiscal 2025, prices should grow ~3% on-year in fiscal 2026, supporting revenue growth.



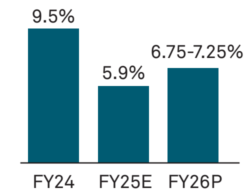
● Revenue growth ● Share in revenue

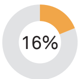
Note: 1. Analysis based on 798 listed corporates, excluding oil and gas and BFSI companies, representing ~65% of the market cap of all companies that traded on BSE on April 1, 2024
2. Consumer discretionary products: Cars and utility vehicles (UVs), consumer durables, ready-made garments (RMGs), two-wheelers
Exports: IT, exports segments of cotton yarn, gems and jewellery, pharmaceuticals, RMGs
Consumer discretionary services: Airline services, hotels, media, organised retailing
Commodities: Cement, non-ferrous metals, steel
Consumer staples: FMCG, hospitals, pharmaceuticals, sugar, telecommunications (telecom)
Construction: Ceramics, construction, power generation, distribution and transmission, real estate
Industrial: Auto components, chemicals, chlor alkali, commercial vehicles (CVs), paper, power equipment, tyres
Others: Cotton yarn, edible oil, gems and jewellery, packaging, tractors
Source: Quantix, company reports, Crisil Intelligence



Construction

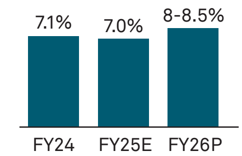
The construction sector's revenue growth is expected to be steady because of increased demand for housing and commercial spaces. This will be led by continued focus on project completion by developers. To be specific, the top seven cities of India will likely witness 8-10% growth in housing absorption. While the roads and railways sectors are likely to maintain moderate pace, sectors such as power, urban infrastructure and irrigation will support growth.

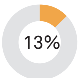




Exports

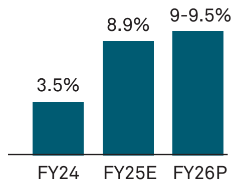
The information technology (IT) services industry's revenue, three-fourths of the export industry, is projected to increase ~100 bps to 5-7% in fiscal 2026. Resumption of deferred IT transformation projects across key sectors such as BFSI was already visible in the third quarter of fiscal 2025. Additionally, with over 60% of revenue denominated in US dollar, a weakening rupee will further support growth in fiscal 2026. However, global growth is likely to moderate after fiscal 2026 and will bear watching. Pharmaceutical export revenue growth will be driven by continued easing of pricing pressure and new product launches. With companies focusing on complex generics and specialty products, pricing pressure is expected to abate.





Industrials

In industrials, revenue growth momentum will sustain on the back of auto components and chemical industry. Auto component revenue is forecast to grow 10-12%, the same pace as in fiscal 2025, owing to healthy demand from original equipment manufacturers (OEMs), followed by replacement and export markets. Chemical sector revenue growth will increase a moderate ~100 bps to 9%, driven by a shift in global supply chains, domestic demand and proximity to the Middle East's petrochemical feedstock.



● Revenue growth ● Share in revenue

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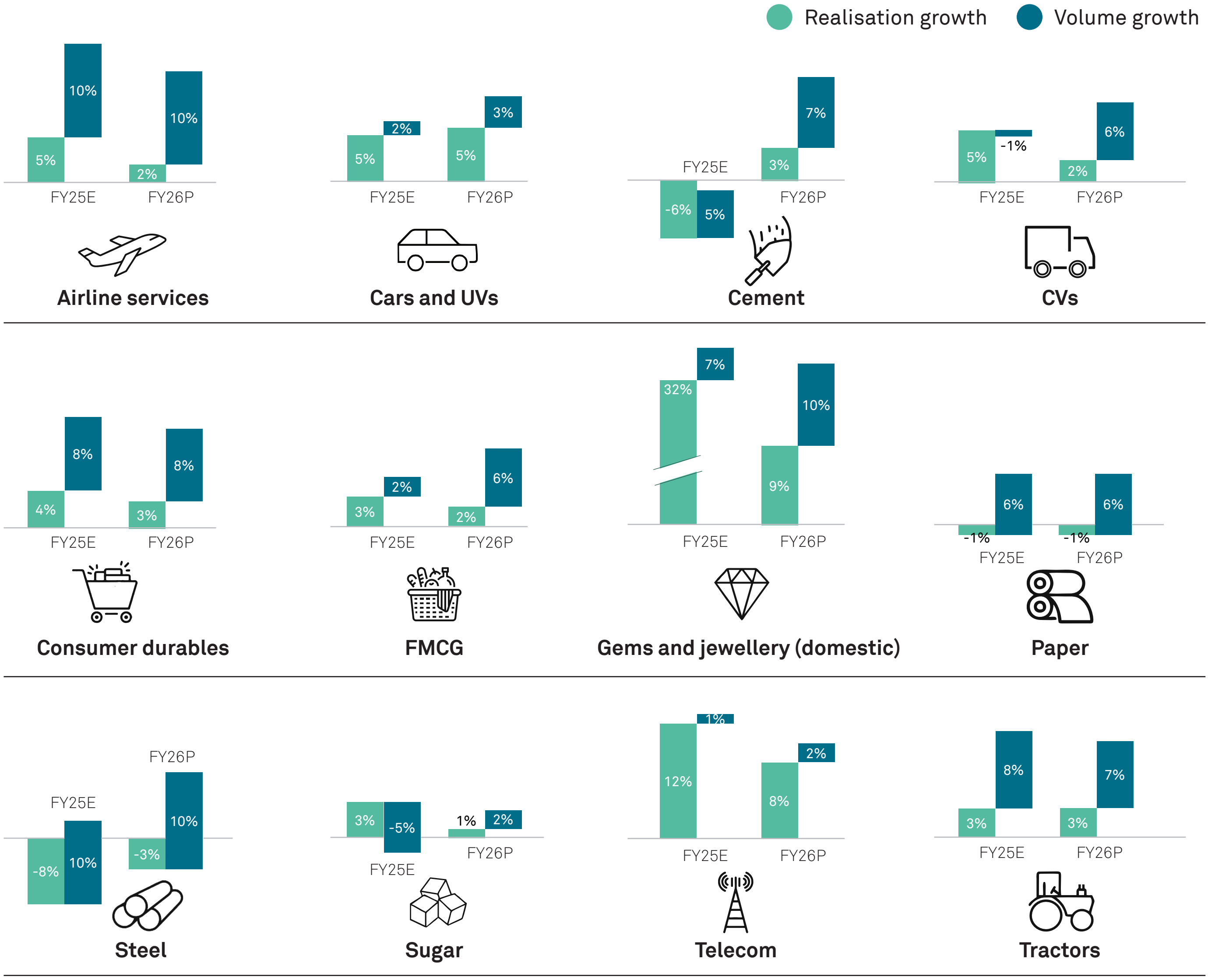
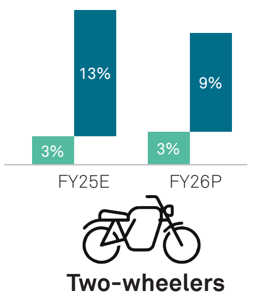
Construction: Ceramics, construction, power generation, distribution and transmission, real estate
Industrial: Auto components, chemicals, chlor alkali, commercial vehicles (CVs), paper, power equipment, tyres
Others: Cotton yarn, edible oil, gems and jewellery, packaging, tractors
Source: Quantix, company reports, Crisil Intelligence

Revenue growth to be largely volume-led

Corporate revenue is likely to be fuelled by volume growth in fiscal 2026, with 11 out of 13 key sectors (as shown in the chart below) poised to experience volume-driven expansion, outpacing price increases.

The two exceptions are the telecom and passenger vehicle sectors. In telecom, revenue growth will be fuelled by an 8% increase in realisations, driven by rising adoption of 5G services and a 15-25% tariff increase implemented in July 2024, leading to higher average revenue per user. Meanwhile, the passenger vehicle sector will see revenue growth driven by a shift in product mix, which will lead to higher realisations.



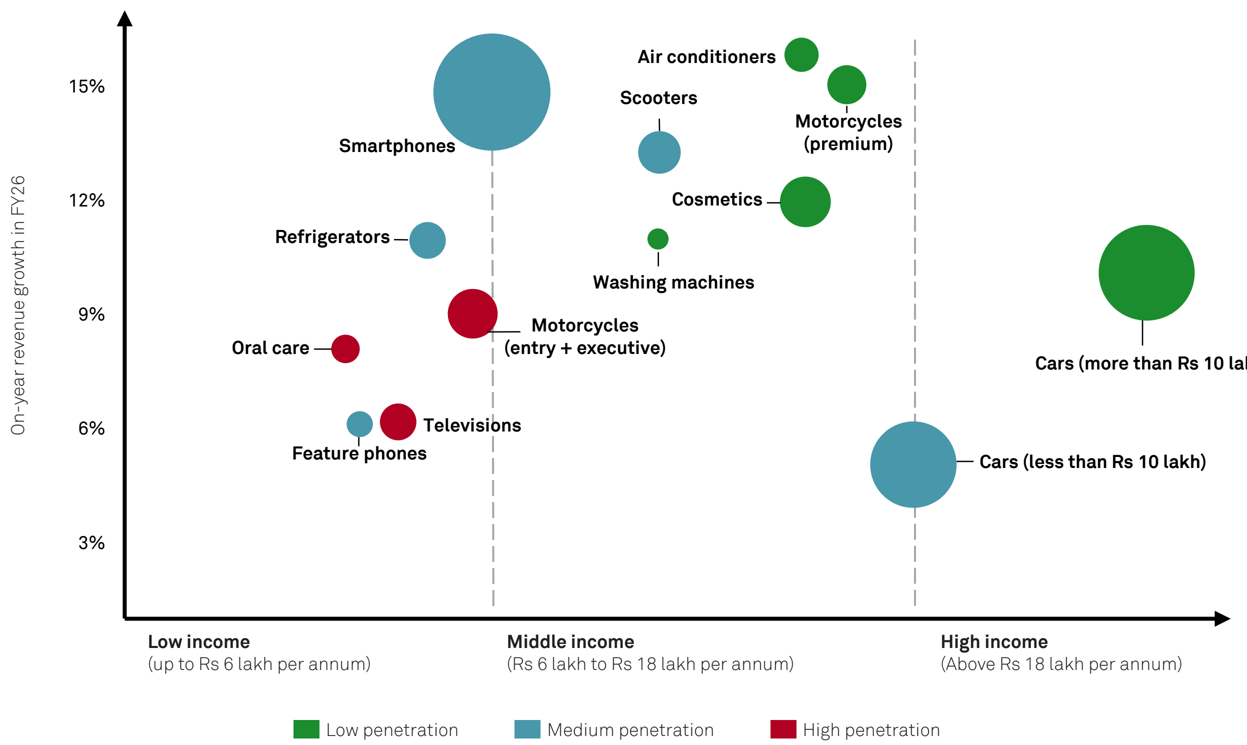


Note: For the steel sector, the pricing outlook for fiscal 2026 will depend on the imposition of safeguard duties to restrict imports. Timing and quantum of duty is a monitorable.
Source: Crisil Intelligence

Mid-income goods to gain the most from tax cuts

Private consumption accounts for more than 55% of the country's GDP. However, over the past two years, the twin pressures of high inflation and elevated interest rates have taken a toll on private consumption, as reflected in the subdued average growth rate of 4.7% over the past eight quarters through the second quarter of fiscal 2025. This is significantly lower than the 6.5% recorded over the preceding decade, up to the second quarter of fiscal 2023. In this context, the revised income tax slabs under the new regime, along with lower inflation and interest rates, are expected to aid middle-income households, potentially boosting urban demand in segments such as ACs and two-wheelers.

Underpenetrated products to fly as middle-income consumers demand more



Note: Bubble size represents the relative market size. Income bracket definitions are aligned to the thresholds used by the government for core schemes such as PMAY. Bubble's position represents the typical threshold income at which consumption starts.
Source: Crisil Intelligence

The maximum percentage increase in disposable income due to the tax cuts is for mid-income consumers (annual income ranging from Rs 6 lakh to Rs 18 lakh), which will benefit product categories that are largely consumed by this segment of households. For instance, within automobiles, the expected volume growth for two-wheelers is much higher compared with passenger cars, where the target buyers are largely from the high-income category.

Another factor that determines the growth delta on account of tax cuts is the existing penetration levels of the product. If one compares within consumer durables, ACs will grow much faster than refrigerators and washing machines. Domestic penetration of ACs is significantly low at ~10% as against ~90% in developed economies such as the US. In contrast, refrigerators have a higher existing penetration level of 42% and threshold income level observed for refrigerator purchase is much lower compared with ACs.

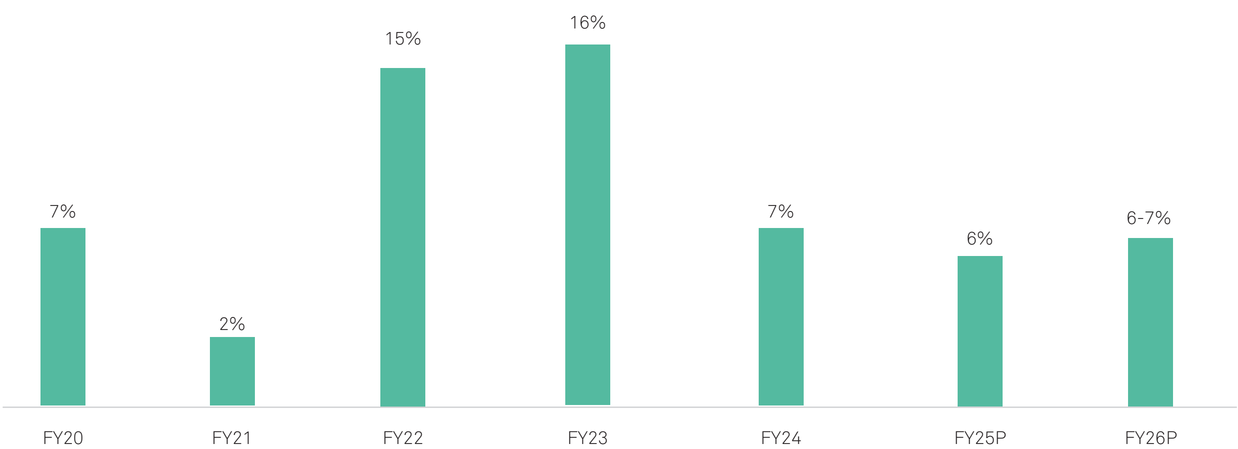
Growth beyond the top cities

The Indian consumer market is evolving, driven by factors such as increasing purchasing power of consumers in non-metropolitan cities, mushrooming of start-ups, rapid growth of digital platforms and increasing importance of rural consumption. The focus on geographies beyond the top 10 cities is providing volume impetus as players see growth beyond metros because of the rising appetite for discretionary spending in these regions, improving job market as well as lower land and labour costs. This is evident from the expansion of supermarts — store count increased 3x over fiscals 2018-2024, with over 70% of stores in Tier 2 cities and beyond. Digital access and wider online reach have also boosted demand. Tier 2 and smaller cities accounted for ~60% of e-commerce companies' demand in fiscal 2024 (vs 40% in fiscal 2017).

Slightly better staff payouts to support consumption

Staff costs for corporates, a proxy for corporate salaries, which are projected to rise 6-7% in fiscal 2026, could support consumption growth, driven by the middle-income group. Recent announcements on tax bracket changes are likely to support the middle-income group the most with maximum additional savings up to 6% for individuals with annual income between Rs 7 lakh and Rs 18 lakh per annum.

India Inc employee expenditure likely to inch up in fiscal 2026

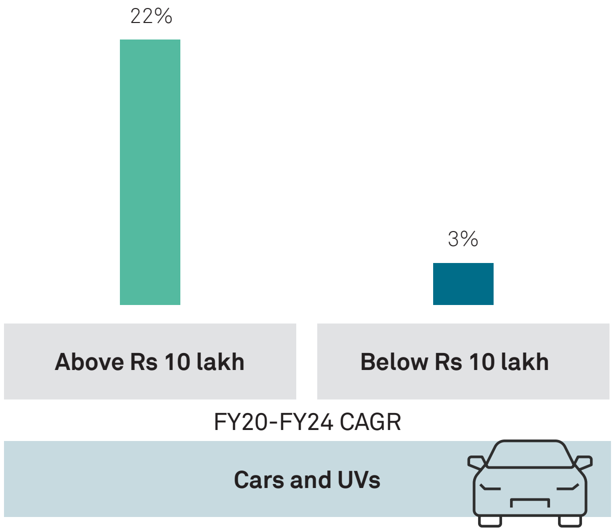


Source: Quantix, company reports, Crisil Intelligence
Note: Employee expenditure has been determined through a bottom-up approach by combining staff expenses of 798 corporates, excluding oil and gas and BFSI companies.

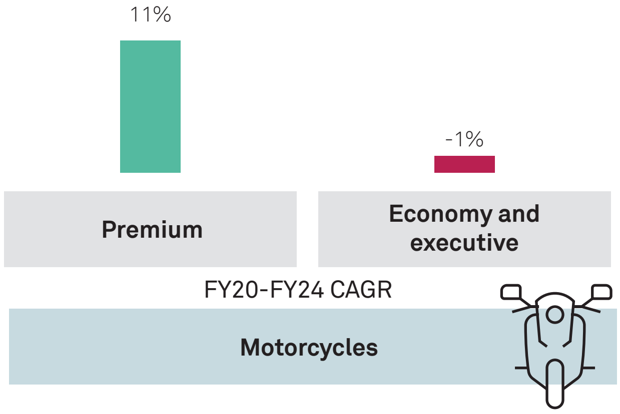
Shift towards premium products continues

Consumers seeking more value and convenience are opting for premium products, a trend which is expected to continue. A notable example is the surge in demand for premium cars (priced above Rs 10 lakh), which witness longer waiting periods compared with lower-priced ones. Similarly, in consumer durables, the low penetration of air conditioners is driving premiumisation in the segment, unlike smaller appliances such as fans that have higher penetration levels. This benefits corporate India as higher revenue contribution from premium products aids a company's profitability.

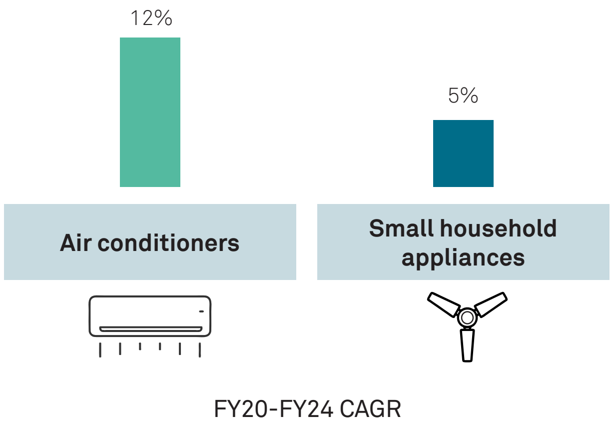
Consumers are opting for premium products across sectors



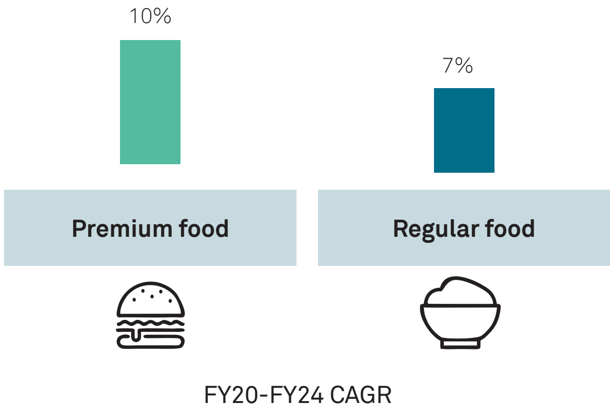
The chart represents the sales volume growth of passenger vehicles
Source: Industry, Crisil Intelligence



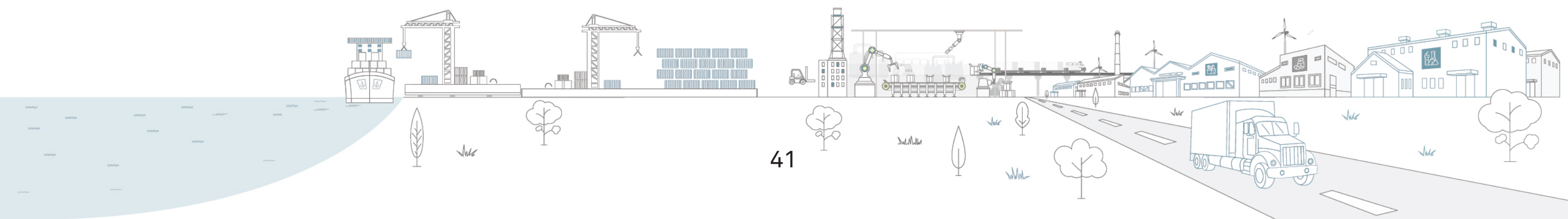
The chart represents the sales volume growth of motorcycles
Source: Industry, Crisil Intelligence



The chart represents the revenue growth of a sample set of companies
Source: Company reports, Crisil Intelligence

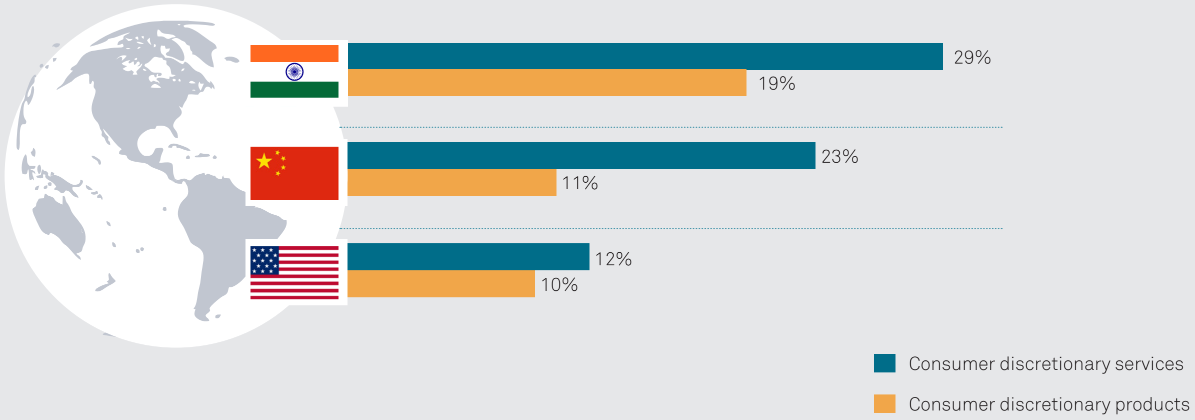


Premium food includes categories such as ready to eat/ ready to cook, cream & cookies, and chocolates, while regular food includes segments such as traditional snacks and glucose-and milk-based biscuits
The chart represents the revenue growth of a sample set of companies
Source: Company reports, Crisil Intelligence



Globally, consumer discretionary services have outpaced products and staples

Global comparison of revenue growth



Source: Crisil Intelligence
Note: Average annual revenue growth from calendar year 2021 to 2023; Figures for India correspond to fiscals between 2022 and 2024

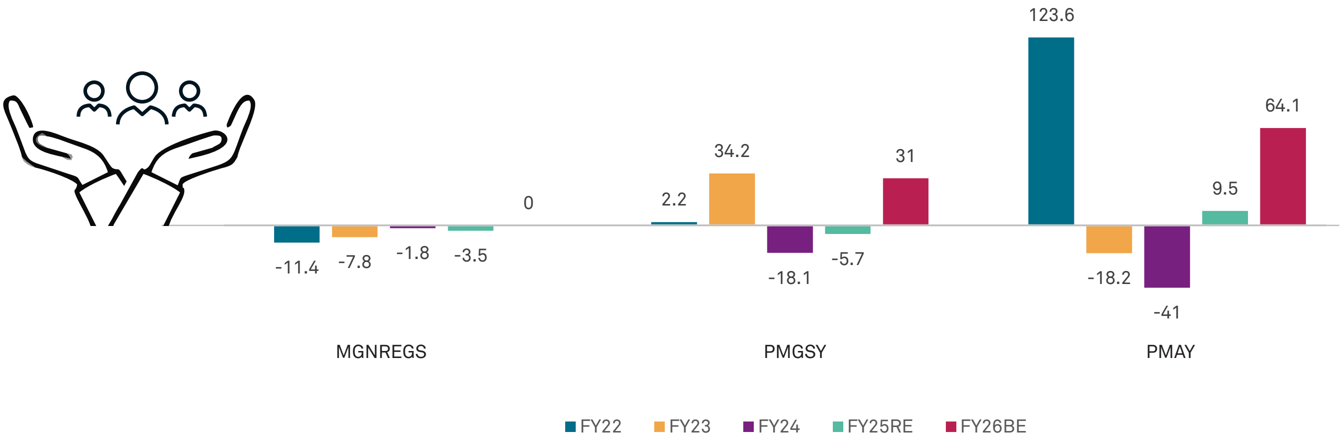
Growth of consumer discretionary services continues to outpace consumer discretionary products — a trend observed in advanced economies such as the US and China. This shift is expected to continue as consumers prioritise recurring experience-related spending. On the other hand, when a consumer purchases a product, it often has a replacement cycle, reducing the need for frequent repurchases.

Positive momentum in rural consumption to sustain

An expected normal monsoon, healthy farm income and government support are expected to boost rural consumption in fiscal 2026. As farming is a significant portion of rural household income, a positive agricultural sector outlook will aid the broader rural economy.

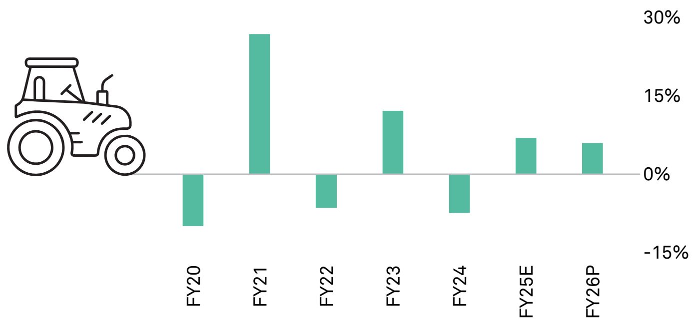
- While support under MGNREGS and PM-Kisan schemes will sustain, an increased loan limit under Kisan Credit Card will enhance cash flow for about 7.7 crore farmers, enabling them to adopt better farming practices, leading to higher crop yields
- Higher allocations for key central infrastructure and employment-generating schemes such as the PMAY and PMGSY should support incomes and consumption, with a 23.7% total allocation increase, primarily benefiting lower-income households that will utilise the increased cash for consumption
- Agriculture GVA is expected to rebound with 3.5% growth in fiscal 2025, leading to robust demand for two-wheelers and tractors. The trend should continue in fiscal 2026, contingent on a favourable monsoon
- As small and marginal farmers control 86% of land holdings, timely and adequate monsoon remains key to earnings and, in turn, spending

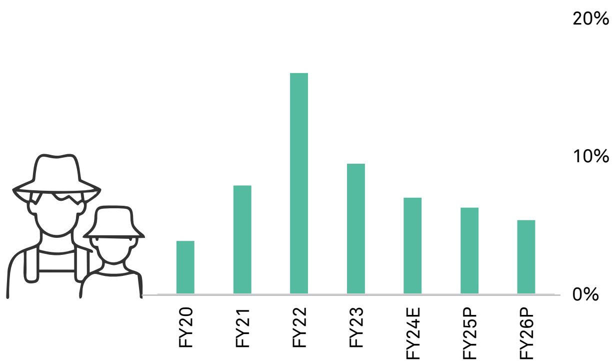
Allocations for key welfare schemes in fiscal 2026 higher on-year



Source: Budget documents, Crisil Intelligence

Tractor sales and farm family income projections indicate sustained growth in fiscal 2026





Source: Quantix, company reports, Crisil Intelligence
Note: Farm family income indicated above captures 50-55% of it from cultivation of crops, dairy and MGNREGA scheme

Steady infra spending by the Centre to continue

The Centre has been the bulwark of investments over the past five fiscals, building infrastructure to stoke and sustain long-term economic growth.

After the Covid-19 pandemic, such investments have driven overall capital formation as well. The Centre's capex has risen continuously from 1.7% of GDP during fiscals 2016-2020 to 3.1% of GDP budgeted for fiscal 2026. The government is investing in rural roads, highways, airports and railways to improve physical connectivity, reduce logistics costs and enhance competitiveness. As a result, gross fixed capital formation has improved from 27.3% of GDP in fiscal 2021 to 30.1% in fiscal 2025.

Capex for fiscal 2026 is budgeted at Rs 11.2 lakh crore, up 10% from Rs 10.2 lakh crore in fiscal 2025RE, indicating the government has maintained its capex support at 3.1% of GDP, the same as in fiscal 2025.

Within this, the Ministry of Railways and the Ministry of Road Transport and Highways have been allocated the highest share of capex in the budget, though the amount is the same as last year. These sectors are a catalyst for demand for related industrial sectors. For instance, according to a National Institute of Public Finance and Policy study, every rupee allocated to capex has a multiplier effect of 4.8 on the economy, as against just 0.96 for revenue expenditure.

Strategic initiatives such as Bharatmala, Sagarmala and the National Infrastructure Pipeline, along with Gati Shakti, have played pivotal roles. Other interventions, including the implementation of the E-way bill system and digitalisation of toll plazas, have reduced documentation and waiting times, boosting efficiency.

Spending by states has not kept pace

While the central government provides most funding for road and railway projects, state governments take the lead in executing projects related to irrigation, water supply and sanitation, urban development, and housing across the country.

However, states' share of general government capex has declined from an average of 61% between fiscals 2016 and 2020 to 48% between fiscals 2021 and 2024. In fact, the share was at its lowest point of 46% in fiscal 2024 and is likely to remain stable but low, given the estimated 7-8% growth in fiscal 2025.

As a result, the capital-to-revenue expenditure ratio, a measure of expenditure quality, is expected to decrease from a seven-year high of 21.2% in fiscal 2024 to 20.7% this fiscal for states, although it remains higher than the average of 18.8% over the previous 14 years.

Nevertheless, there is significant disparity between states, with large states such as Gujarat, Rajasthan and Tamil Nadu budgeting for capex growth of 24-30%, while other large states, including Bihar, Madhya Pradesh and Maharashtra, are budgeting for a contraction in fiscal 2025.

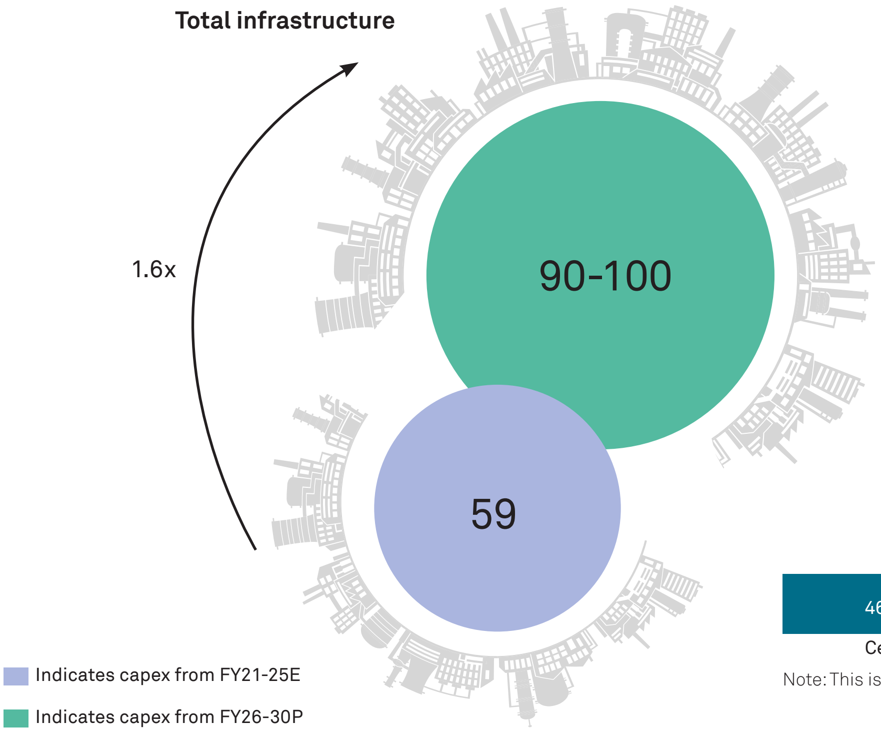
Infrastructure spending to grow 1.6 times in five years

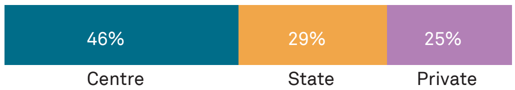
Infrastructure spending in the country, which includes investments from the centre, states and the private sector — led by roads and power — will help push investments through fiscal 2030, with total capex likely to increase 1.6x to Rs 90-100 lakh crore.

Private sector involvement in infrastructure, which has been increasing, is poised to intensify with the government's renewed emphasis on the build-operate-transfer (BOT) model in roads. The power sector continues to attract substantial private investment, driven by a sharper focus on non-fossil fuel energy generation. The government's National Monetisation Pipeline is also expected to play a key role in boosting private sector participation by facilitating its greater involvement in infrastructure development.

Infrastructure spending set to surge 1.6 times over next five years

In Rs lakh crore

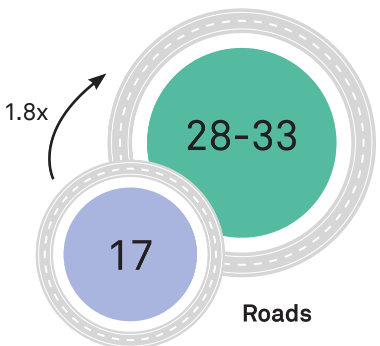




Note: This is for the projected period FY26-30

Source: Quantix, company reports, Industry, Crisil Intelligence

Roads and power to drive infrastructure investments

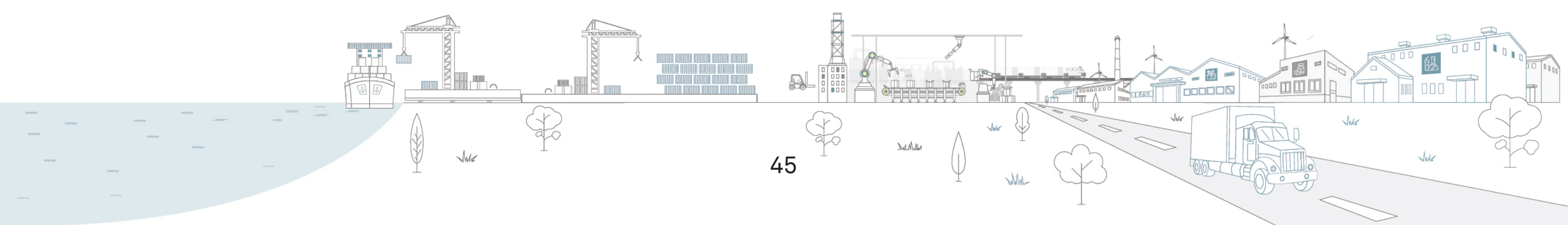


Investments in roads to continue strong momentum and grow at 11% CAGR from FY26 to FY30

- Private sector participation to increase with policy reforms and government's restored focus on BOT model
- Better execution and a robust pipeline of projects to pave the way for strong capex growth
- Steady budgetary allocation to aid execution through the engineering, procurement and construction mode, and new avenues to finance projects such as investment trusts and the National Investment and Infrastructure Fund will help deal with financing constraints

Note: This is for the projected period FY26-30

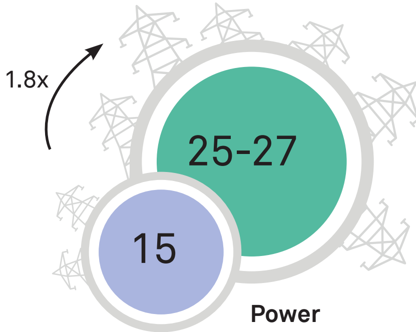
Source: Industry, Crisil Intelligence



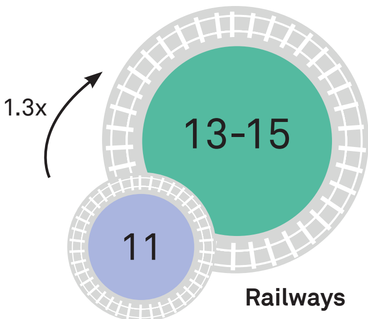
Green investments to have a higher share in power sector capex

- Private sector to account for half the investments. Furthermore, Centre's share to fall due to the increase in state activity in the transmission and distribution segment
- Power generation capex to be led by renewable energy with a target of 500 GW capacity by 2030
- Rise in per capita power consumption and push for manufacturing will aid further investments

Note: This is for the projected period FY26-30

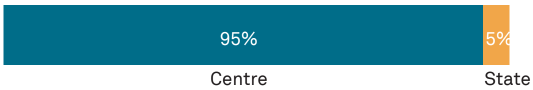


Source: Quantix, company reports, Industry, Crisil Intelligence



Investments in railways to moderate

- Investments would be led by doubling, track renewals, network expansion, dedicated freight corridor, station development and high-speed rail
- Implementation of high-value projects such as the Mumbai-Ahmedabad bullet train, increasing traction in station redevelopment and completion of the freight corridors to boost near-term capex

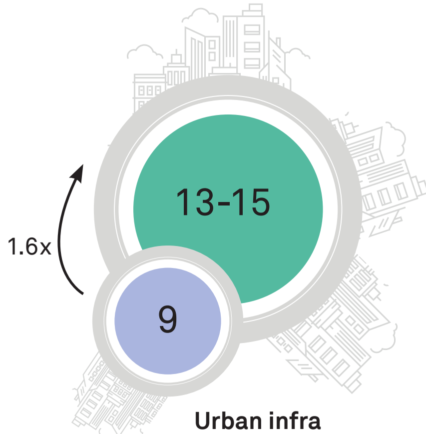


Note: This is for the projected period FY26-30

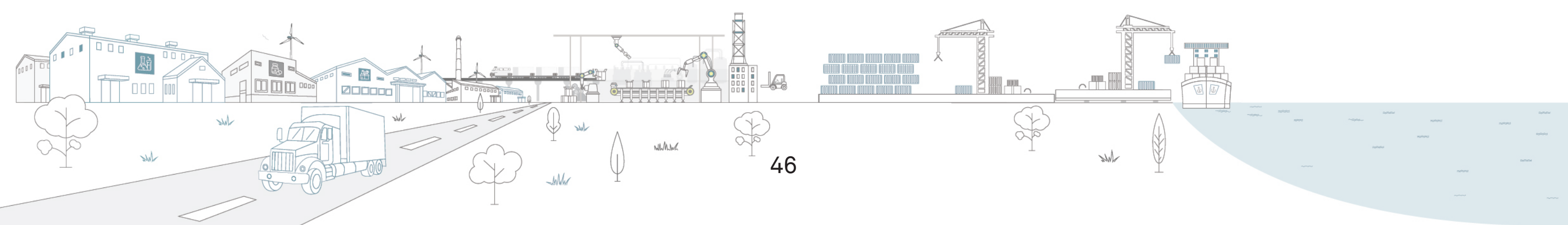
Rising urbanisation to support urban infra investment

- Water supply and sanitation projects to account for nearly half of investments until fiscal 2030, driven by state governments and centrally-sponsored programmes
- Metro construction to be the second-largest urban infrastructure investment, with newer cities emerging as key destinations for metro infrastructure development

Note: This is for the projected period FY26-30



Source: Crisil Intelligence
Note: E- estimated, P- projected
Other infrastructure includes ports, airports, irrigation, telecom towers, warehousing
Urban infrastructure includes metro, water supply and sanitation and smart cities



Emerging sectors and green investments to drive growth in industrial capex

Between fiscals 2021 and 2025, household demand and infrastructure development have been at the forefront of India's capex, primarily bankrolled by central and state governments. Now, industrial capex is expected to grow as private sector investments also step up in conventional industries and emerging sectors, providing a critical boost to the capex cycle.

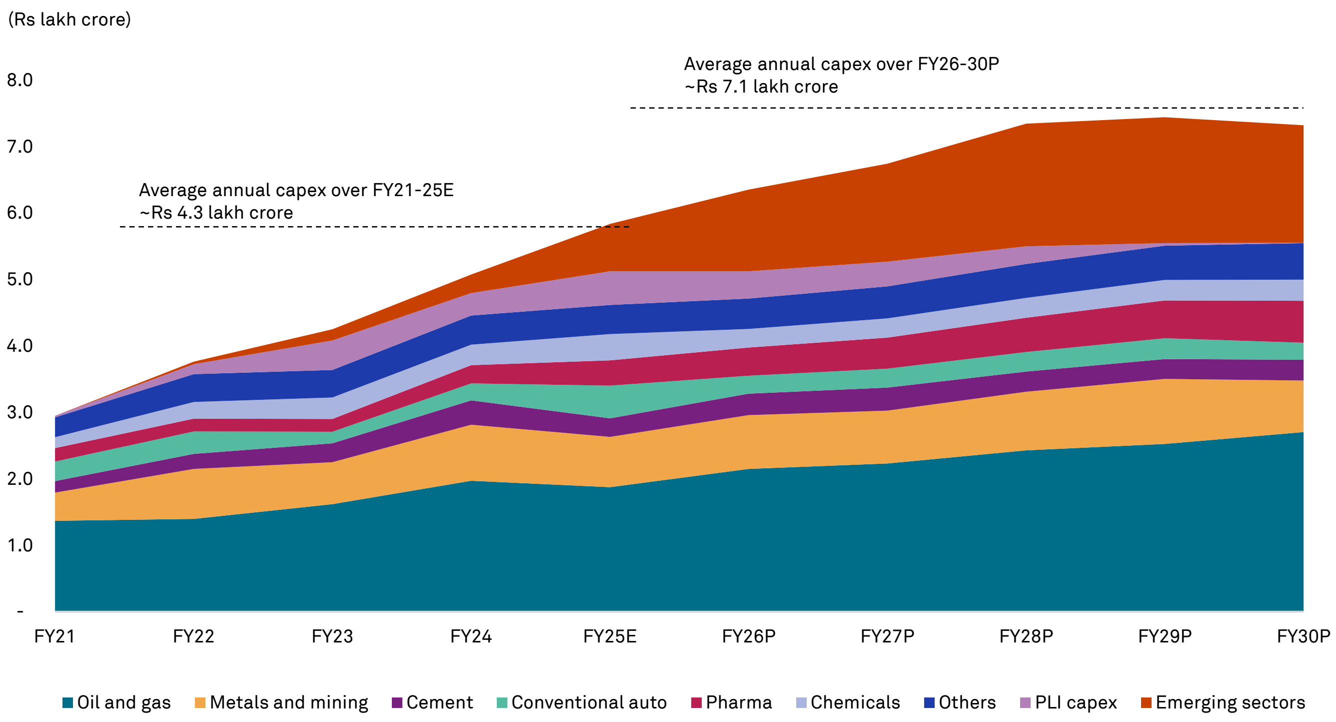
Industrial capex averaged Rs 4.3 lakh crore per annum in fiscals 2021-2025E. Investments are expected to reach ~Rs 7.1 lakh crore by fiscal 2030, marking an average annual increase of 1.6x, driven by higher capacity utilisation, strong corporate balance sheets and the PLI schemes targeting multiple sectors.

As India transitions to value-added manufacturing, emerging sectors, such as electric vehicles (EVs), semiconductors and electronics, are poised to become the main drivers of industrial capex. These are projected to account for ~27% of the industrial capex between fiscals 2026 and 2030 from 6% over fiscals 2021 and 2025, underscoring the country's shift towards sustainable and technology-driven growth.

Over fiscals 2026-2030, the PLI scheme and emerging sectors are set to account for a quarter of the country's capex from 12% in fiscals 2021-2025, emphasising the growing importance of these sectors in India's industrial landscape. PLI-driven capex is expected to peak by fiscal 2026 as approved projects aim to fulfil commitments to avail incentives. Investments in emerging sectors will simultaneously strengthen India's manufacturing capabilities to achieve self-reliance and make local production globally competitive.

Focused capex in the infrastructure and industrial sectors over fiscals 2021-2030 reflects not only India's economic growth objectives but also a strategic commitment to sustainable development.

PLI and emerging sectors contribute 27% of industrial capex

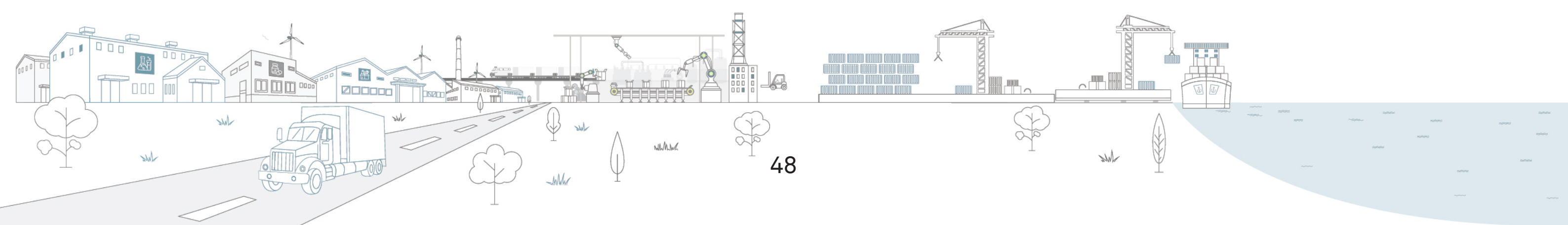


Source: Crisil Intelligence

Capex seen at Rs 125-135 lakh crore and share of green investments at ~20% over fiscals 2026-2030

	Total investments			Green investments
Capex	**FY21-25E**	**FY26-30P**	**FY26-30P/FY21-25E**	**Green as % of total**
Industrial	21.7	33-38	1.6 X	20%
Conventional sectors	19.0	23-28	1.4 X	12%
Oil and gas	8.2	10-15	1.5 X	22%
Metals and mining	3.3	4-4.5	1.3 X	3%
Cement	1.3	1.5-1.7	1.2 X	8%
Conventional auto	1.6	1.3-1.5	0.9X	0%
Pharma	1.2	2.5-2.7	2.1 X	4%
Chemicals	1.4	1.4-1.6	1.0 X	0%
Others*	2.0	2.4-2.6	1.3 X	4%
PLI capex	1.4	1.2-1.4	0.9 X	0%
Emerging sectors	1.2	7.5-8.5	6.8 X	50%
Semiconductors and electronics	0.2	3-3.5	15.4 X	0%
EV capex*	0.6	2-2.5	3.7 X	100%
Battery manufacturing	00	1.7-2.2	52.1 X	100%
Solar photovoltaic (PV)	0.3	0.5-1	2.3 X	0%
Infrastructure	59.4	90-100	1.6 X	19%
Power	14.6	25-27	1.8 X	70%
Others*	44.8	65-70	1.5 X	0%
Overall capex (Including industrial and infrastructure)	81.1	125-135	1.6 X	20%

Source: Crisil Intelligence
* Other conventional sectors include FMCG, textiles, paper etc
* EV capex includes charging infra
* Other infrastructure segments include roads, railways, ports, airports, irrigation, telecom towers, warehousing, metro, water supply and sanitation, and smart cities

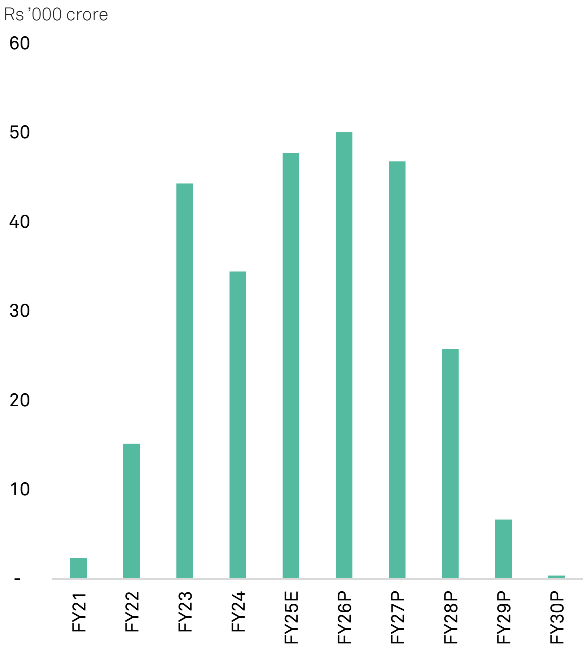


While the infrastructure and corporate sectors are expected to be funded predominantly by banks and the corporate bond market, emerging sector capex, dominated by multinationals and large Indian companies, is expected to be funded by the domestic and international corporate bond markets.

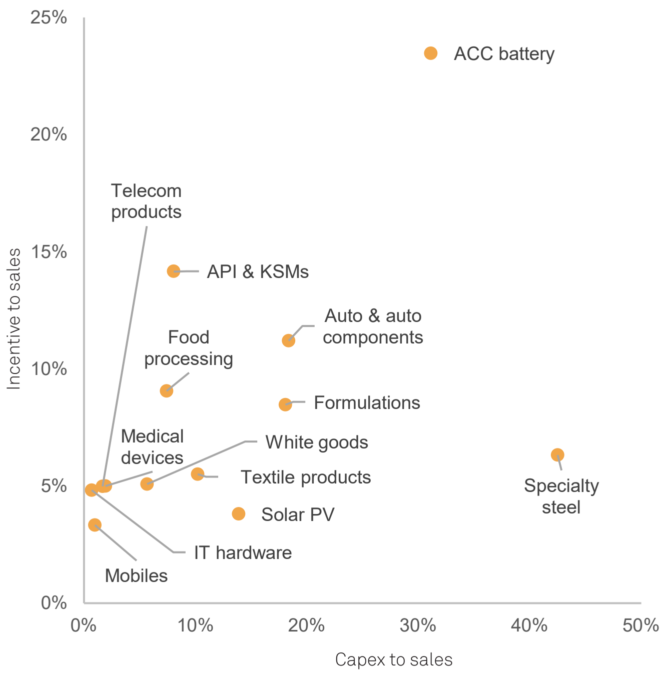
PLI scheme boosts manufacturing, reduces reliance on import

The PLI scheme, which aims to drive industrial capex of Rs 2.6-2.8 lakh crore during the scheme period, is projected to contribute ~5% to capex in key sectors. The incentives, totalling Rs 1.8-1.9 lakh crore, are expected to generate incremental revenue of Rs 30 lakh crore. Launched in March 2020, the scheme, as of August 2024, has attracted investments of Rs 1.46 lakh crore, highlighting healthy momentum in key targeted sectors.

Capex-intensive sectors to gain momentum over three years starting FY25



Low capex-to-sales ratio shores up mobile revenue



Source: Scheme documents, Press Information Bureau

The PLI scheme is poised to drive significant growth in India's manufacturing sector over the next two years, particularly in capital-intensive segments. The scheme has already made considerable strides in reducing India's reliance on imports and boosting export revenue in 14 key sectors, including electronics, textiles, and automobiles. Historically, these sectors have struggled with a substantial 20% cost disadvantage compared with Chinese imports. However, the scheme has yielded promising results in sectors such as mobile, telecom and pharmaceuticals.

As high-intensity sectors such as ACC batteries, solar PV modules and specialty steel come online over the next three fiscals starting from fiscal 2025, meaningful results are expected to emerge.

The mobile sector, for instance, has generated an impressive revenue of Rs 12 lakh crore during fiscals 2021-2024, with 23% of this being exported, on account of a relatively low capex-to-sales ratio.

Nevertheless, the extent of value addition has increased only up to 20%, indicating that there is still room for improvement. To build on this momentum, the government has introduced an additional scheme to encourage mobile component manufacturing, aiming to increase India's domestic value addition (DVA) in the mobile ecosystem to over 30%. This strategic move is consistent with global manufacturing hubs' experiences, where moving up the value addition ladder is crucial for sustained growth.

In contrast, capital-intensive sectors such as ACC batteries and solar PV modules account for nearly a quarter of the capex envisioned under the scheme. Players in these sectors are expanding cautiously, given the high capex to sales ratio of over 30%, in stark contrast to the mobile sector's 1%. Over the three years starting from fiscal 2025, these sectors will deploy significant capital, leading to an expected DVA of over 50%.

The success of the PLI scheme in the medical devices sector is a notable example of its potential. The Medical Devices PLI scheme has enabled companies to diversify their product portfolios and venture into high-end medical devices, which were earlier imported. This success has led to the government approving the National Medical Device Policy, aiming to reduce import dependency and establish India as a global manufacturing hub for medical devices.

However, despite the progress made, challenges persist, including high power and logistics costs, as well as limited market access due to lack of Free Trade Agreements (FTAs). Industry interactions across sectors suggest that the PLI scheme will aid the establishment of ecosystems, though certain areas could remain a work in progress. Considering these sectors are nascent, India may lag behind peers in scale of operation. To address these challenges, a calibrated approach combining non-trade barriers, trade policy and PLI incentives will provide the necessary visibility to make long-term investments in these sectors.

Green investments to experience multi-fold growth in key sectors

Large investments in the power sector are likely to be supported by India's commitment to meet emission targets by 2030. Under the Panchamrit action plan, the government has defined a glide path of achieving net zero emission target by 2070, involving investments in two verticals.

First is the renewable energy sector. We believe renewable segments will have 60-65% share in the country's installed capacity by 2030, which will entail strong investments in solar, wind and storage systems.

Second is the EV segment, where rapid transition and increase in penetration levels would encourage OEMs to build capacity or expand into battery and components. Under the PLI scheme, manufacturing capacity of 40 giga watt hours (GWh) of batteries with an incentive outlay of Rs 18,100 crore was approved in fiscal 2021 with Rs 25,000 crore capex. With these investments, India will be able to move up the value chain from battery assembling to cell production and also towards electrode production.

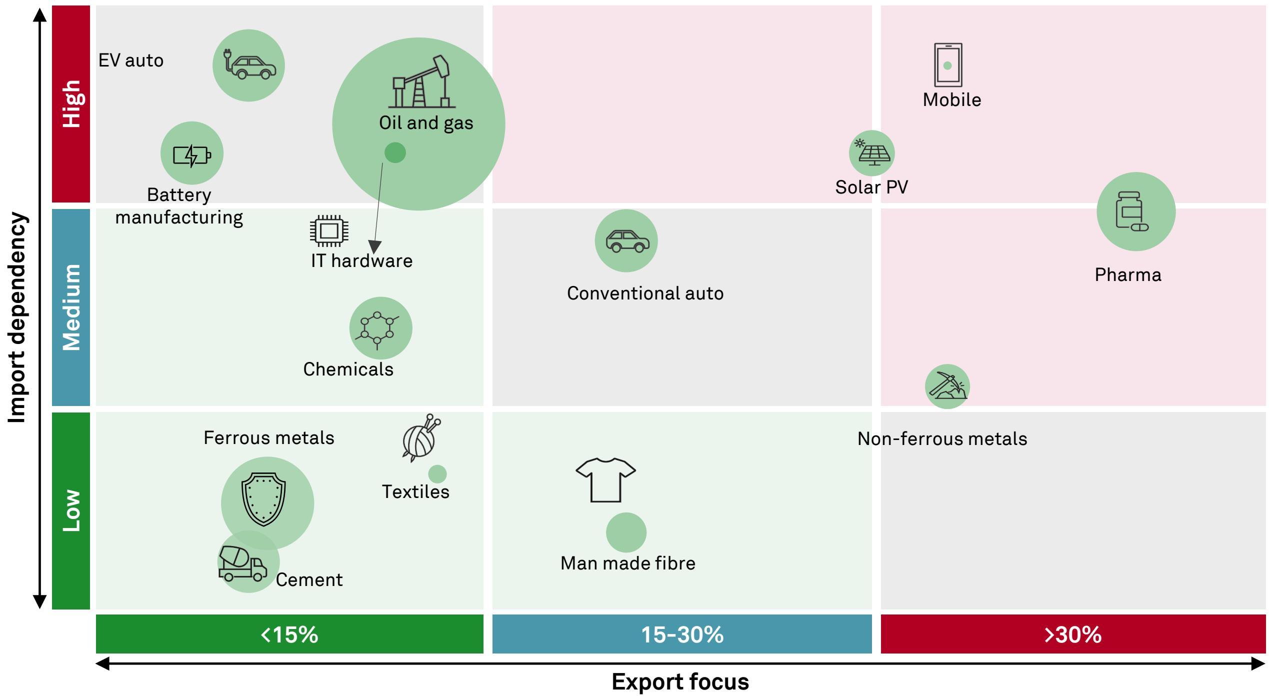
Investments in energy-efficient technologies, supported by regulatory incentives, will significantly save green transition costs across industries. The electrification of key sectors, including transportation and industry, is driven by the growing demand for clean electricity and policy-driven transitions, creating opportunities for investments in low-carbon power generation. Expanding and modernising the grid is crucial to integrate renewable energy sources, and support decentralised energy systems and smart grid technologies. In addition, an investment boost in energy storage solutions and grid flexibility is vital to balance supply and demand, ensuring reliable and clean energy supply across the country.

Almost half of industrial capex exposed to global trade uncertainty

With merchandise exports contributing ~12% to India's GDP, evaluating the sectoral impact of moderating global growth and heightened trade uncertainties is essential. It is estimated that almost half of the planned industrial capex is exposed to risks related to global trade – either due to dependence on imported raw materials, technology or reliance on export markets. This vulnerability stems from the potential impact of events, such as EU climate policies, increased tariffs from the US and over-reliance on China, which could disrupt business continuity and expansion plans. The uncertainty linked to such events might lead companies to delay, or in some extreme cases, defer their expansion plans.

For instance, in mobiles, electronics and solar PV modules, we depend on China for import of components and the US for a substantial portion of our exports. This makes these segments vulnerable to trade uncertainties on both ends, though government support and incentives provide comfort. On the other extreme, a sector such as cement is least exposed to external vagaries and completely dependent on domestic demand. Hence, there is very little possibility that changes in tariffs would derail expansion plans.

Increasing shift towards global protectionism poses greater risk to new-age sectors



Source: Crisil Intelligence
Note: Export focus indicates exports' share in overall production
Size of the capex bubble is the sector's planned capex from FY26 to FY30
Import dependency is assessed using a 10-point scale, which indicates value chain's reliance on imports
Listed sectors contribute more than 80% of the planned industrial capex

As India continues to develop its sunrise sectors, including electronics, renewable energy and EVs, the pace of technological advancements presents opportunities and challenges. The prices of PV modules have reduced significantly over the past decade, benefitting developers, but companies aiming for integrated manufacturing face challenges in achieving cost economies. Similarly, the EV sector's rapid technological changes require persistent support through the PLI scheme to ensure India can scale up its domestic manufacturing capabilities and stay competitive on the global stage.

Given the increasing global uncertainties and sector-specific risks, it is crucial for businesses to prioritise financial resilience in their capex plans. As external pressures mount, being frugal and globally cost-competitive allows companies to remain resilient, safeguard profitability and effectively navigate disruptions. For this, achieving critical scale and maintaining financial strength are essential for securing long-term success.

US reciprocal tariffs could potentially impact exports and price dynamics of key sectors

US President Donald Trump's reciprocal tariffs can affect exports, which account for ~22% of India's GDP, adding to the pain from moderating global trade growth and heightened trade uncertainties.

India's share in global merchandise exports doubled to 1.8% in 2023 from 0.9% in 2005, whereas its share in services exports rose faster to 4.3% from 2.0%.

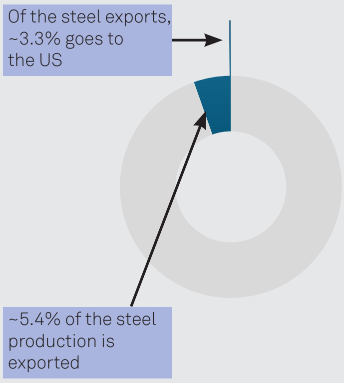
Among India's export destinations, the US accounted for ~18% share in fiscal 2024, underscoring its importance in India's trade expansion. Indeed, in the past five years (fiscals 2019 to 2024), while India's merchandise exports logged a 5% compound annual growth rate (CAGR), exports to the US grew faster, clocking a 7% CAGR. Exports to the UAE, another key trade partner, rose slower, at 3% CAGR.

Within exports, gems and jewellery, pharmaceuticals, RMGs, smartphones and solar PV modules are some of India's key products with high concentration risk to the US market.

We have analysed the potential impact of higher US tariffs on key manufacturing sectors. However, we have not looked at service sectors as the possibility of tariffs appears lower. The reason is India runs a larger trade surplus with the US on merchandise exports, while on services it is more even. Additionally, imposing tariffs on services is more difficult to implement

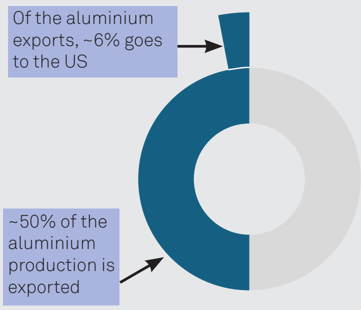
Sectoral assessment

Steel



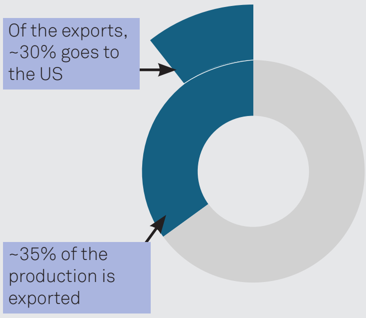
- The US move to impose a flat 25% tariff on steel imports from March 12, 2025, compared with multiple lower levies previously, will have minimum impact on the Indian steel industry. That is because only ~2% of India's finished steel exports in the first nine months of this fiscal were to the US.
- That said, incremental production by US mills to make up for lower imports due to tariffs would mean a reduction in exports of steel scrap by the US. For the record, ~70% of the US steel production is via recycling scrap. Lower exports of steel scrap by the US will impact India, which sources 14-15% of its scrap requirement from the US.
- Meanwhile, lower US imports of steel will result in diversion of exporter inventory to other importer nations at aggressive prices, especially in a milieu of rising global competition. That could lower the price of steel in India, which is already trending at four-year lows.
- The Indian government may thus have to step in with a safeguard duty to support domestic capacities.

Aluminium



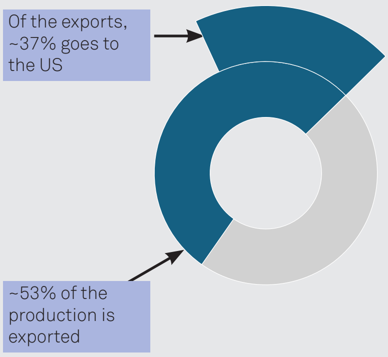
- The US's move to impose a flat 25% tariff on aluminium imports from March 12, 2025, compared with a raft of lower levies now will have a negative impact on Indian manufacturers of the metal. Half of their production is currently exported, of which ~6% is to the US
- The US imports majority of its aluminium requirement from Canada, which, if diverted towards global markets, will create competition for the Indian metal
- With users of primary aluminium in the US expected to reduce imports after the 25% tariff kicks in, end-users in the US would prefer using locally manufactured aluminium, which is predominantly produced by scrap recycling. This, too, will have a bearing on India, as ~26% of the aluminium scrap it imports is from the US. Consequently, we foresee some impact on domestic secondary aluminium and alloy producers

Gems and jewellery



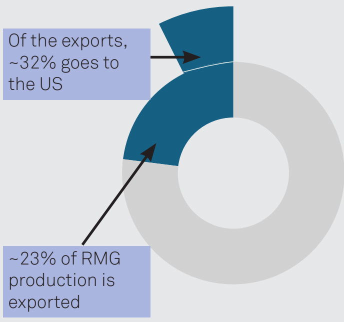
- The gems and jewellery sector in India relies heavily on exports, with unmounted diamonds and jewellery articles forming a substantial portion of the outbound trade. Notably, India is the world's largest producer and exporter of cut and polished diamonds, and it plays an irreplaceable role in the global diamond supply chain
- As of fiscal 2024, unmounted diamonds, which are exempt from duty in the US, accounted for ~56% of the gems and jewellery export in value to the US and 1.3% of India's export value. During the period, the US received 33% of India's unmounted diamond exports by value
- The export of gems and jewellery has been declining over the past three fiscals, primarily because of subdued discretionary demand in the US. However, an uptick is expected in fiscal 2026. In the event of an increase in US tariffs, demand sentiment could be affected, although the impact on India's export share by value is likely to be moderate

Pharmaceutical products



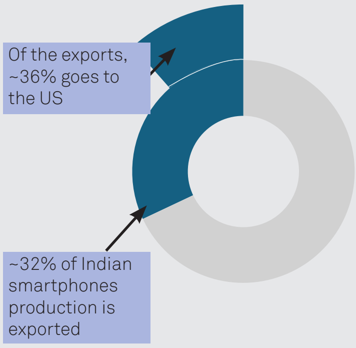
- The recent indication by the US to impose reciprocal tariffs on its trading partners is likely to have a limited impact on India's pharmaceuticals sector. An increase in tariffs could moderately raise the prices of Indian products, which are prominently generic formulations. Notably, some industry stakeholders expect generic pharmaceutical products to be exempt from tariffs, given the US government's initiative to 'Make America Healthy Again', which includes keeping healthcare costs under control. Stakeholders indicate that even if tariffs are imposed, bulk of the cost is likely to be passed on to customers, thereby mitigating any potential impact on the generics segment

RMGs



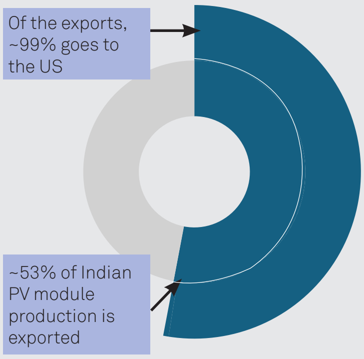
- If the US imposes tariffs on Indian RMGs, the volume and profitability of the domestic players would be affected
  - Impact on volume: Although the US is a significant market for India's RMG exports, the imposition of duties is likely to have a moderate impact on the volumes. The country's position as a major supplier is unlikely to be threatened, as competing countries such as China and Bangladesh, which hold 22% and 9% market shares, respectively, face their own challenges. China is already subject to higher duties, and a significant increase in exports from Bangladesh is unlikely due to the political instability there. Furthermore, a depreciating rupee could reduce costs for importers in the US, partially mitigating the impact of increased duties on India's exports to the US
  - Impact on profitability: The profitability of RMG players may be affected due to the increased tariff, as they will be forced to price their products more competitively, which will ultimately impact their bottom line
- The imposition of tariffs is expected to also lead to a decline in export volume from China to the US. China may then look to sell its excess products in other countries, intensifying competition for Indian RMG players in some export markets

Smartphones



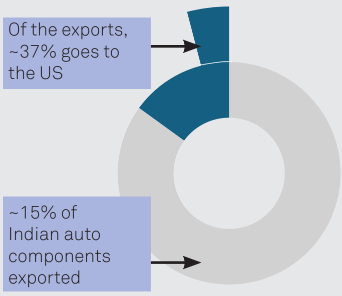
- The US administration has proposed 25% additional tariff on imports from Canada and Mexico and 10% additional tariff on imports from China. The duties on China became effective from February 4, 2025. Nearly 75% of US smartphone imports by value are from China. India's contribution is about 10%
- Reciprocal tariffs on smartphones have a potential to nullify the benefits Indian assemblers get under the PLI scheme and will make exports to the US challenging. However, an increase in disposable income due to tax cuts in India can help partially offset a decline in export demand

Solar PV modules



- A reciprocal increase in duties on imports of solar modules from India (India exported 7-8 GW in fiscal 2024) will increase the cost of solar installations in the US, which could impact annual solar capacity additions
- Major solar module exporters, such as China, Thailand, Malaysia and Indonesia, have additional tariff and non-tariff barriers to navigate. Hence, the duties on Indian solar PV module exports to the US will not significantly impact volumes
- However, the margins of module manufacturers may see a moderate impact due to high concentration on the US market

Auto components

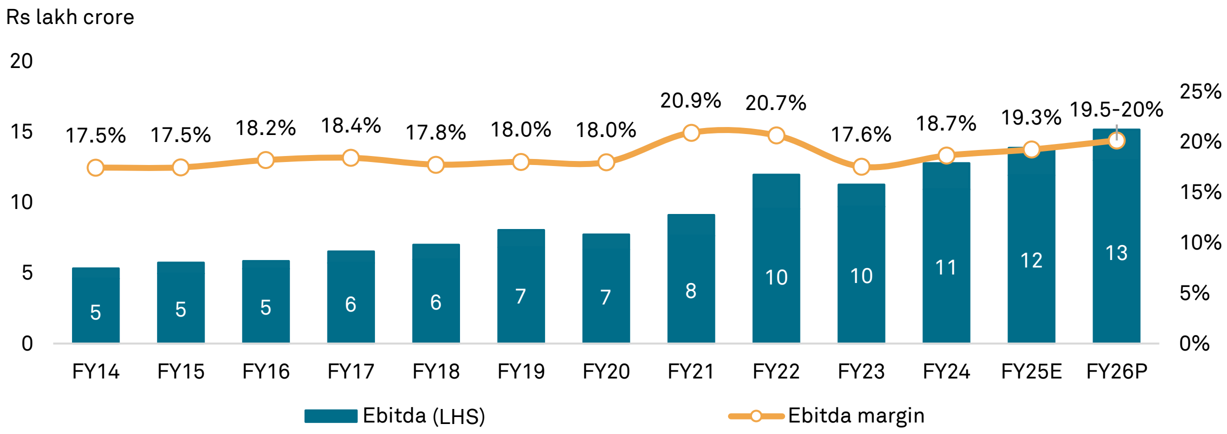


- Trump's announcement to impose 25% tariff on auto components from India would reduce the competitiveness of these products in the US market
- However, the impact is expected to be limited to a few key exporters, as the domestic OEM and replacement market accounts for ~83% of the market. Demand from OEMs is expected to outpace that from exports and the replacement market, providing a cushion for the sector

All figures are in value terms
Source: Industry, trade data, Crisil Intelligence

Benign commodities to push profitability near decadal highs

Profiting on commodities



E – estimated, P – projected
Note: Figures are for 798 listed corporates and excludes oil and gas and BFSI companies, representing ~65% of the market cap of all companies that traded on BSE on April 1, 2024
Source: RBI, company reports, Crisil Intelligence

Despite expectations of moderate revenue growth, corporate India's Ebitda margin is expected to improve ~50 bps in fiscal 2026 due to benign commodity prices.

As European nations realign their supply chains and move towards higher natural gas consumption, pressure on demand for crude oil and coal has decreased. Parallelly, fewer supply-side issues are anticipated in crude oil and coal supply. This is expected to reduce the cost of energy for industries, boosting margins. In the metals space, global overcapacity and stagnant demand will keep steel prices low. However, the imposition of safeguard duty by India remains a key monitorable; it has the potential to reduce imports and increase domestic steel prices. Base metal prices are expected to rise due to the shift towards renewable energy. In the agricultural space, a healthy monsoon and better-than-expected crop yields in the rabi season are expected to keep prices in check.

Consumption, commodities and export industries are expected to drive margin expansion in fiscal 2026. The cars and UVs industry is anticipated to see a shift in the product mix towards more profitable UVs and premium variants, while the two-wheeler industry is likely to see higher operating leverage, aided by an uptick in volumes driving margin expansion. A gradual increase in tariffs in the telecom industry will improve margins.

In the commodities sector, margin expansion is expected to be supported by the steel and cement industry volumes. Supportive raw material prices, along with healthy volume growth, driven by allied sectors such as construction and infrastructure, will improve the steel industry's margins. Improvement in Ebitda margin in the cement industry is expected to be driven by recovery in demand and prices, along with easing of cost pressures.

In exports, IT services' margins are expected to improve in fiscal 2026, driven by a pick-up in projects and healthy utilisation levels.

In fiscal 2026, while aluminium prices could remain elevated, prices of copper and zinc would be stable or decline, leading to ~450 bps fall in the non-ferrous industry margin.

Low energy, commodity and staple prices to bolster corporate margins in fiscal 2026

Crude oil

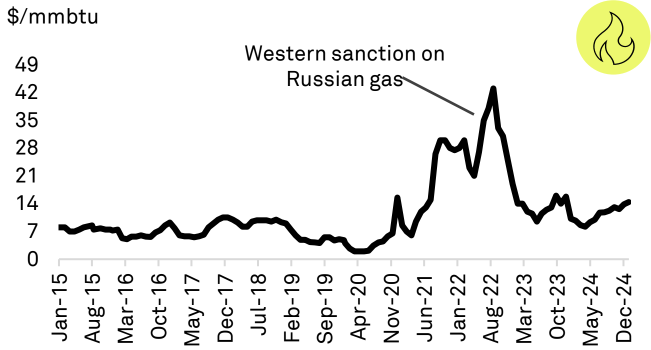
- Fiscal 2026 is likely to see a downward price trajectory riding on the plans of the US administration and the Organization of the Petroleum Exporting Countries and others (OPEC+) to boost production, outpacing demand growth
- However, OPEC+'s repeated delays in reversing production cuts could exert upward pressure on prices. Steady non-OPEC supplies should mitigate potential spikes, while sanctions on Russian and Iranian exports and geopolitical tensions remain key risks that could influence prices

Note - Dated Brent prices
Source - Crisil Intelligence

LNG

FY24 **(55)%** | FY25E **(0-2)%** | FY26P **25-27%**

- The upward price trajectory of spot liquefied natural gas (LNG) in the past few quarters was driven by strong European demand and growing imports from South Korea and Taiwan due to stockpile requirements and demand from gas-based power producers
- China's demand, though, remains uncertain due to trade tensions. Also, Russian supply is constrained by sanctions. But new supplies from North American projects and potential Middle East exports may offset upward price pressure in fiscal 2026

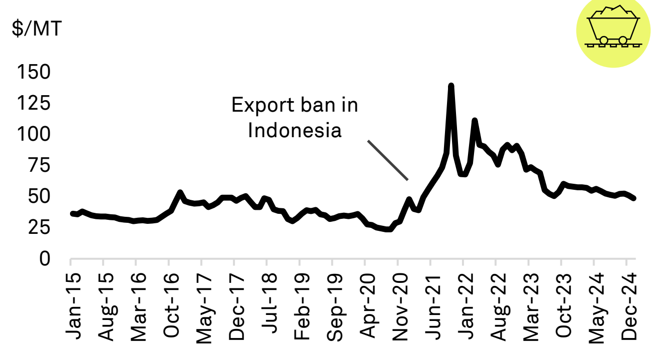


Note - Spot LNG prices, India
Source - Crisil Intelligence

Thermal coal

FY24 **(31)%** | FY25E **(11-13)%** | FY26P **(2-4) %**

- No inclement weather phenomenon is expected for the full year, with the exception of La Niña, thereby supporting prices in fiscal 2026
- With the new US administration in office, trade tariffs on Chinese imports could affect its industrial power demand, resulting in lower thermal coal demand
- Heavy rainfall in Indonesia's key mining regions remains a monitorable



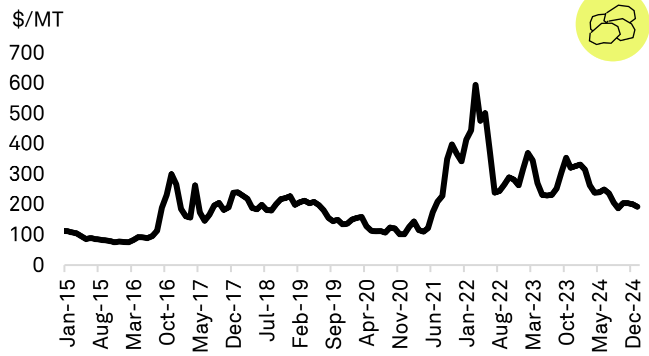
Note: Indonesian thermal coal prices, FOB TBCT
Source - Crisil Intelligence

Crisil Intelligence

Coking coal

FY24 (13.3)% | FY25E (25-27)% | FY26P (1-3) %

- In fiscal 2025, while production improved and there was no major disruption, demand remained muted. Thus, prices declined ~26% in line with declining steel prices
- Coking coal prices to remain soft in fiscal 2026 amid lack of supply concerns and weak global steel production growth
- As India, the largest consumer of sea-borne coking coal, continues to diversify its coking coal sourcing to mitigate concentration risk, pressure remains on Australian coking coal prices

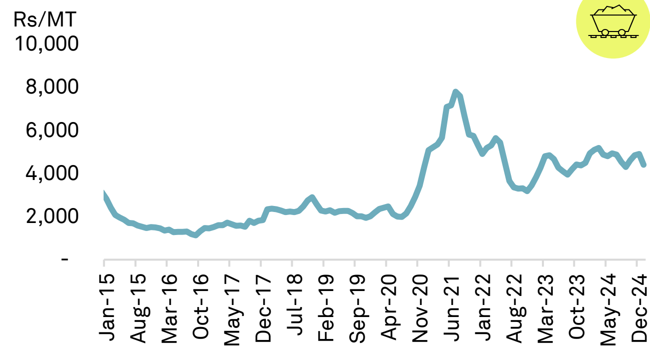


Note: Premium low volatility coking coal prices, FOB Australia
Source - Crisil Intelligence

Iron ore

FY24 11.9% | FY25E 1-3% | FY26P (1-3) %

- While global iron ore prices saw a 25% decline in fiscal 2025, Indian iron ore prices stood ground as high auction premium kept costs higher for miners
- In fiscal 2026, lower differential with global iron ore prices will restrict export opportunities, while increasing production from new mines will result in ample supply. Prices are expected to moderate by 1-3%



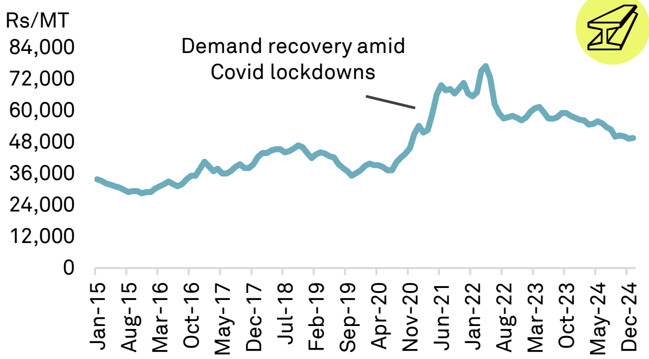
Note: Iron ore fines, 62% Fe, India
Source - Crisil Intelligence

Steel

FY24 (5)% | FY25E (10-12)% | FY26P (6-8) %

- In fiscals 2025 and 2026, major integrated players are anticipated to add 17-20 million tonne of primarily flat steel capacities. Hence, despite healthy demand from allied segments in fiscal 2026, hot-rolled-coil steel prices are expected to decline
- Prices are also going to be under pressure from weak global trade dynamics
- Safeguard duty on steel imports, as a result of ongoing Indian investigation, can potentially nullify the expected downward price movement

Note: For the steel sector, the pricing outlook for fiscal 2026 will depend on the imposition of safeguard duties to restrict imports. Timing and quantum of duty is a monitorable

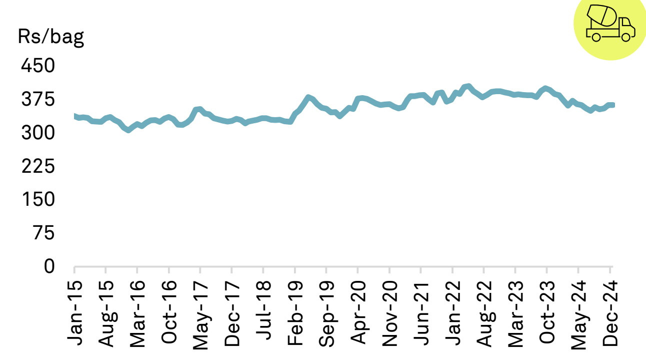


Note: Flat steel- hot rolled coil prices
Source - Crisil Intelligence

Cement

FY24 (2)% | FY25E (5-7)% | FY26P 1-3%

- In fiscal 2025, prices declined 5-7% on-year due to moderation in demand growth, softening costs and ramp-up in capacity additions
- Prices are expected to rise 1-3% on-year in fiscal 2026, in line with an increase in demand. However, lower fuel costs are expected to limit the rise

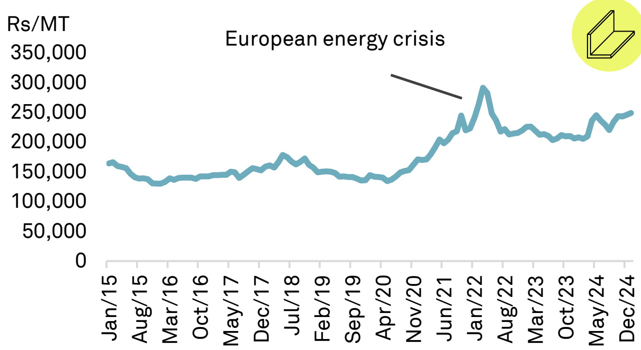


Note: 50 Kg bag, Cat -A prices
Source - Crisil Intelligence

Aluminium

FY24 (9)% | FY25E 13-15% | FY26P 5-7%

- Fiscal 2025 saw global aluminium prices rise on-year (April-January), driven by elevated spot alumina prices, which surged ~62% vs the previous fiscal
- In fiscal 2026, aluminium prices are likely to trend higher amid turbulent global trade and downward revision of production outlook by global players

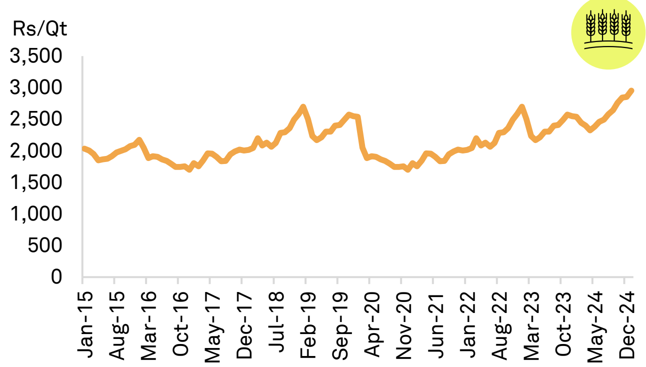


Source - Crisil Intelligence

Wheat

FY24 3% | FY25E 9-11% | FY26P (1-3)%

- Ending stock for fiscal 2025 is projected to be marginally higher than buffer norms
- Hence, prices are expected to fall on-year in fiscal 2026, assuming the current export ban remain in place
- However, if the ban is lifted, which is unlikely, prices are expected to surge to historically high levels

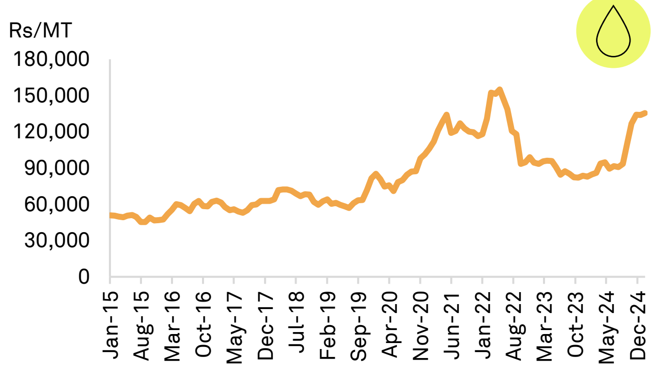


Source - Crisil Intelligence

Edible oil

FY24 (23)% | FY25E 31-33% | FY26P 8-10%

- Prices increased in fiscal 2025 after an increase in import duty, which set a new normal price range for the year
- In fiscal 2026, prices are set to continue their ascent even as major palm-oil-producing countries enter the flush season, as higher bio-diesel production globally and increasing oil demand in India will support domestic prices

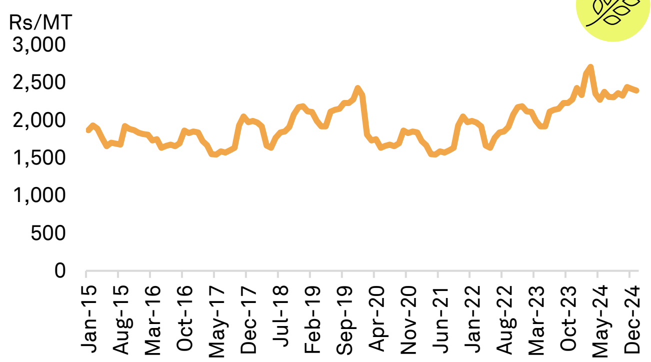


Note: Palm oil prices
Source - Crisil Intelligence

Paddy

FY24 16% | FY25E 5-7% | FY26P (1)-1 %

- Beginning stock of paddy is up 10% on-year, owing to higher production and lower exports (-27% on-year) on account of the government's export ban
- Competitive export prices are expected to boost demand, with exports projected to rise 7-8% on-year in fiscal 2026

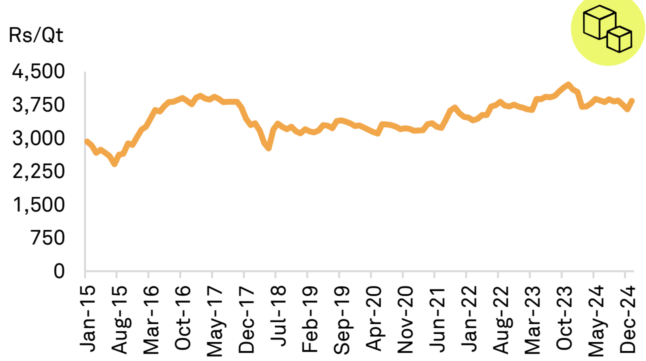


Source - Crisil Intelligence

Sugar

FY24 5% | FY25E 9-11% | FY26P 3-5%

- Sugar prices are likely to surge in fiscal 2026 amid lower production and regulatory curbs by the government
- Consumer-centric policies of the government, limiting exports and use of sugarcane for ethanol production in case of any steep price rise, will keep prices in check



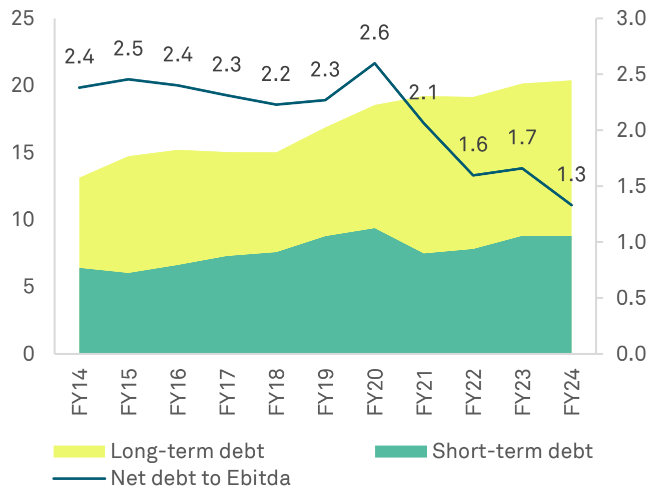
Source - Crisil Intelligence

Net debt-to-Ebitda ratio at nearly half from a decade ago

India's corporate sector has been through a period of deleveraging, which, combined with lower key commodity prices, has contributed to better financial health. Corporate earnings clocked a CAGR of 14% over fiscals 2019-2024, supported by efforts to enhance operational efficiency and manage costs.

- Fiscals 2021 to 2024 saw a muted 2% CAGR in long-term debt to ~Rs 21 lakh crore vs an Ebitda CAGR of 15% during the period, contributing to healthier balance sheets, while short-term debt logged 6% CAGR
- Net debt-to-Ebitda ratio continued to decline 5% on-year in the first half of fiscal 2025
- Improved financial health is expected to provide a cushion to corporates for the next round of the capex cycle. With reduced debt levels, companies will have more flexibility to allocate resources for strategic initiatives, such as expansion, innovation and new growth opportunities

Higher profitability, driven by cooling commodity prices, keeps net debt-to-Ebitda ratio below 1.5



Note: Net debt-to-Ebitda ratio is based on the performance of 811 companies (barring BFSI companies)
Source: Quantix and Crisil Intelligence

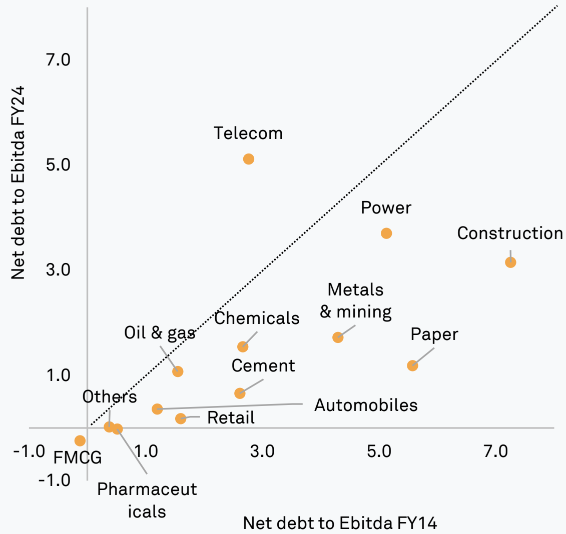
Net debt-to-Ebitda ratio of key sectors, except telecom, improves over fiscals 2014 to 2024

The net debt-to-Ebitda ratio in the paper sector saw the sharpest drop from 5.6 in fiscal 2014 to 1.1 in fiscal 2024 owing to improved profitability.

In the construction sector, it reduced to 3.2 in fiscal 2024 from 7.3 in fiscal 2014 on account of a significant increase in orders from the government and private sectors, led by infrastructure development, real estate growth and lower borrowing costs. These factors allowed construction companies to reduce their debt levels.

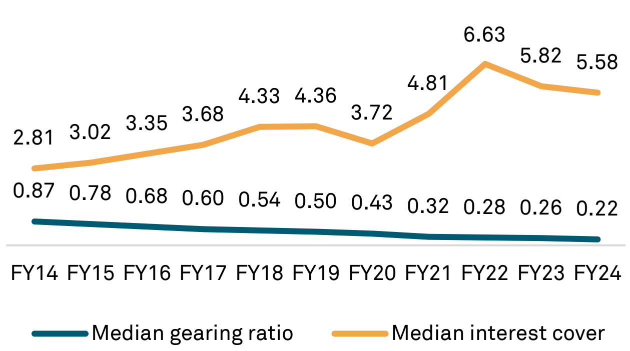
Elevated commodity prices — because of the pandemic-induced supply shortages and subsequent disruptions in the wake of the geopolitical turmoil in Russia and Ukraine — allowed companies in the metals and mining sector to lower their net debt-to-Ebitda ratio.

The telecom sector, on the other hand, saw an increase in its net debt-to-Ebitda ratio during the decade because of a substantial increase in its debt-funded capex following the launch of 4G and 5G services, to set up towers and purchase spectrum at auctions.



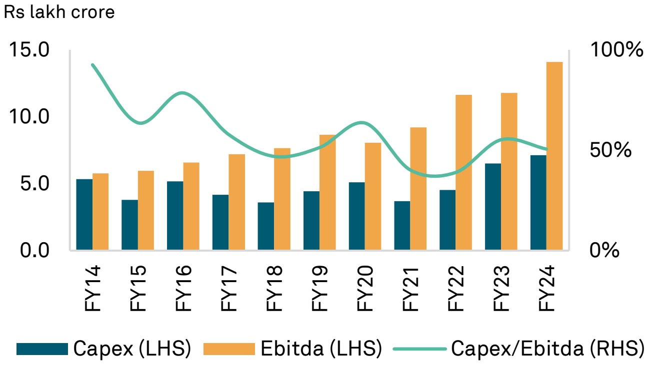
Note: Net debt-to-Ebitda ratio is based on the performance of 811 companies (barring BFSI companies)
Source: Quantix and Crisil Intelligence

Gearing ratio at decadal lows



Note: Based on the performance of 811 companies (barring BFSI companies)
Source: Quantix and Crisil Intelligence

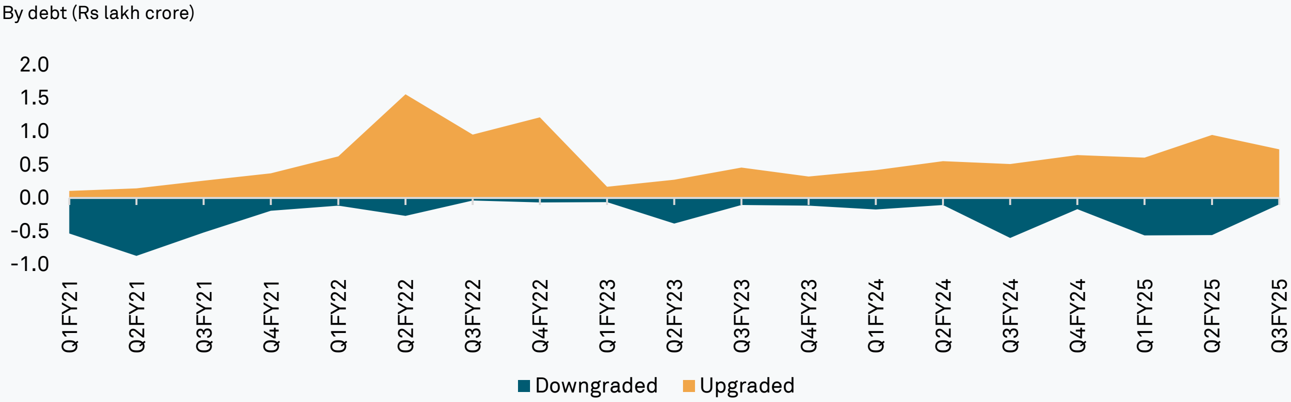
Capex intensity



Note: Based on the performance of 811 companies (barring BFSI companies)
Source: Quantix and Crisil Intelligence

While the industry's capex is rising in absolute terms, its intensity, measured by capex as a percentage of Ebitda, remains moderate, averaging ~50% in fiscal 2024. The industry is poised to explore growth opportunities, underpinned by robust credit fundamentals, steady demand and increasing capacity utilisation. Additionally, even as capex picks up, the sector's leverage is expected to remain at healthy levels.

Strong financial profiles support credit metrics of Indian corporates



	FY21				FY22				FY23				FY24				FY25		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
By debt	0.2	0.2	0.5	2.0	5.6	5.9	24.5	18.3	2.7	0.7	4.5	2.8	2.4	5.2	0.9	3.9	1.1	1.7	7.7
By count	0.1	0.6	0.6	1.2	3.0	3.0	3.4	2.1	5.1	3.1	1.9	1.1	1.0	1.3	1.1	1.0	1.3	2.1	3.8

Note: Based on the performance of 811 companies (barring BFSI companies). Figures in table represent upgrade to downgrade ratio.
Source: Quantix and Crisil Intelligence

Improved financial profiles support the credit metrics of corporates, with the ratio of upgrades to downgrades remaining well over 1.

India Inc needs debt of ~Rs 120 lakh crore

Corporate India will need to raise ~Rs 115-125 lakh crore of debt between fiscals 2026 and 2030 to meet private and public sector capex, working capital, and debt for non-banks (NBFCs[22]).

Of this, Rs 45-50 lakh crore will be for capex, while Rs 70-75 lakh crore will be for non-banks and meeting working capital requirements.

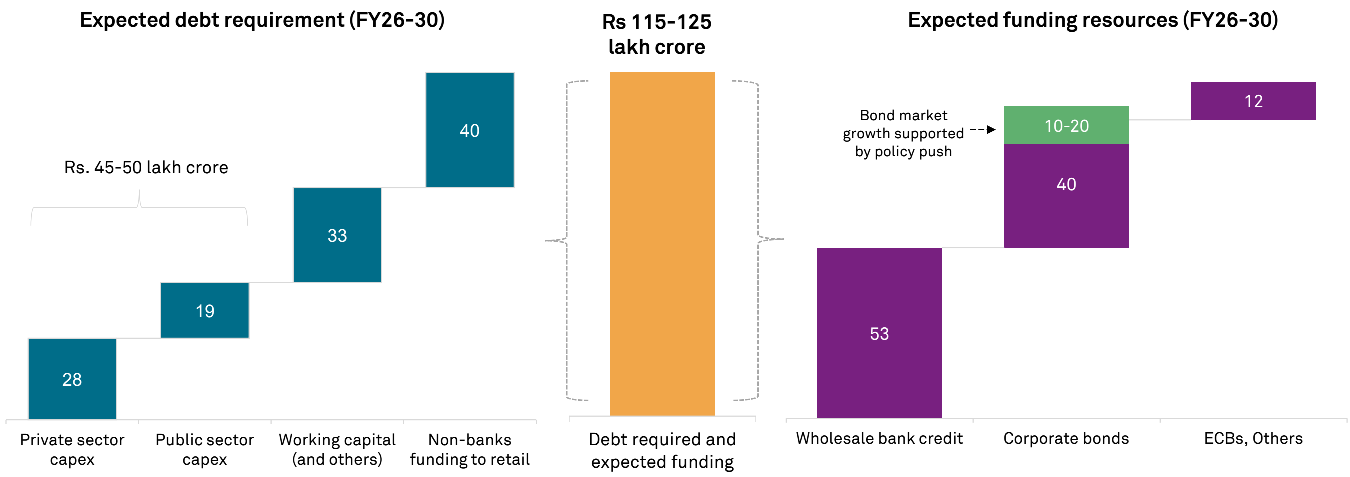
The infrastructure sector, expected to account for ~three-fourths of the capex and ~55% of the overall debt requirement in five fiscals through 2030. Over the medium term, the sector will continue to be the driver of capex.

With corporate India's leverage at a decadal low and credit profiles of infrastructure assets improving, the stars are aligned for continuing capex thrust.

On the funding side, the overall financing ecosystem, comprising banks, corporate bond market and external commercial borrowings, is expected to grow at a modest annual rate of 10% by fiscal 2030, which would leave a funding gap of Rs 10-20 lakh crore.

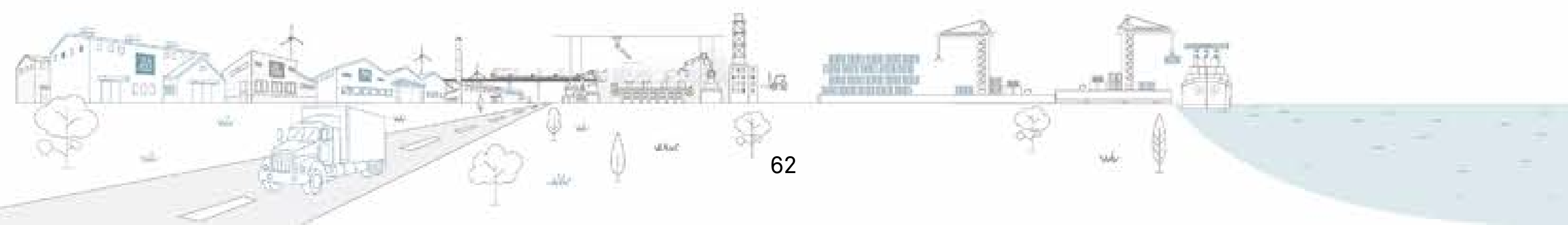
However, if there are appropriate regulatory and policy measures, the corporate bond market has the potential to step up its funding contribution and help bridge this gap.

Financing ecosystem likely to fall short of required debt by Rs 10-20 lakh crore



- Financing ecosystem likely to contribute ~Rs.105 lakh crore, leaving a gap of Rs. 10-20 lakh crore as compared to the debt requirement of Rs. 115-125 lakh crore
- Corporate bond market has the potential to bridge the gap if there are appropriate regulatory and policy level measures

[22]Non-banking financial company – private NBFCs, including housing finance companies (HFCs), government NBFCs and all India financial institutions (AIFIs)



Banks to continue to lead corporate debt financing, driven by strong fundamentals

Wholesale bank lending is expected to add Rs 50-55 lakh crore to the overall credit landscape by fiscal 2030. The current base is ~Rs 90 lakh crore (fiscal 2025 estimate), growing at a healthy ~10% annually.

Healthy capital buffers have meant India's banking system is well-placed to meet the rise in credit demand over the medium term. Scheduled commercial banks had a wholesome capital adequacy of 16.7% as of September-end 2024.

Asset quality trends are benign, with gross non-performing assets (GNPAs) trending down from a peak of ~11% in fiscal 2018 to 2.8% in March 2024, and further to a 12-year low of ~2.4% as of December 2024. GNPAs are expected to decline to ~2% this fiscal owing to stronger risk management and underwriting norms.

For banks, the improvement in the asset quality has translated to better profitability. That, coupled with the high existing provisioning cover ratio (PCR), has reduced incremental credit costs, thereby enhancing return on assets (RoA) to 1.3% in fiscal 2024 from 0.1% in fiscal 2020. The RoA is expected to stay stable in fiscal 2025. This also supports the capital position of banks.

In fiscal 2026, net interest margins (NIMs) and return on assets (RoA) are foreseen declining — led by a rising proportion of floating rate loans being benchmarked to external rates — by over 40% of the total loan book, which are expected to move in tandem with the repo rate.

Consequently, the assets' side will see a quicker downward repricing overall compared with the liabilities side. The extent of NIM and RoA compression will depend on further rate cuts.

Nevertheless, asset quality and profitability of the banking sector is expected to stay healthy over the medium term and should support a faster growth rate of ~10% for wholesale credit compared with 8% between fiscal 2020 and 2025(E).

Deposit growth remains monitorable and must not lag too far behind credit growth. The differential between credit growth and deposit growth has narrowed to ~100 bps in January 2025 from ~600 bps in March 2023 as deposit rates continue to inch up.

Banks are likely to walk the tightrope between growing their deposit base and protecting profitability, depending on their ability to mobilise cost-effective deposits. Supplementary funding avenues such as asset securitisation can be explored by banks in case deposit growth lags credit demand for too long.

Corporate bond market needs to step up to the plate

The corporate bond market saw a CAGR of ~11% over the past five fiscals, from Rs 38 lakh crore outstanding in fiscal 2020 to Rs 64 lakh crore in fiscal 2025[23]. It accounted for a ~ third of the corporate credit landscape as of fiscal 2025.

With the financing ecosystem likely to come up short of the debt requirement, policy push will be essential to increase the contribution of the corporate bond market and fill the potential gap.

The corporate bond market will have to grow at a faster ~11-13% annually between fiscals 2025 and 2030 to be able to meet the expected debt requirement.

While financialisation of savings will support the growth of managed investments, policy nudge for large investor categories such as insurers, pensions and mutual funds to channel more investments into corporate bonds will be necessary.

Both supply-side and demand-side factors favourable

On the supply side, factors such as lean balance sheets of corporates and improved credit quality of infrastructure assets are likely to boost corporate bond issuances.

The risk profiles of infrastructure assets have improved, as underscored by the median ratings in the Crisil Ratings portfolio of such assets rising from 'BBB+' in fiscal 2018 to 'A+' in fiscal 2024.

The loss given default (LGD) for infrastructure assets was found to be in the 20-60% range[24], well below the typical 60-65% factored in by lenders, as per a Crisil Ratings study.

Moreover, a Crisil Ratings study on India's top 500 corporates shows that the top non-financial corporates (public and private sector) source only 20-30% of their domestic borrowings from the corporate bond market.

The potential for non-financial private corporates to

[23] Fiscal 2025 numbers are estimates as per YTD figures. Includes ~Rs.11 lakh crs of commercial papers (CPs) and certificate of deposits (CDs)
[24] https://www.crisilratings.com/en/home/our-analysis/reports/2024/10/the-different-shades-of-lgd.html

tap into the corporate bond market remains vast. The recent 25 bps repo rate cut by the MPC and an expected moderation in interest rates with inflation remaining under control, are supportive for potential corporate bond market issuers in the medium term.

The inclusion of Indian government securities (G-secs) in global bond indices remains an enabler. This should continue to direct the flow of foreign capital into domestic G-secs, creating more space for corporate bond issuances. The government's steadfast commitment to prudence with fiscal deficit for 2025 estimated at 4.8% and the 2026 number being budgeted at 4.4% are supportive for the market.

On the demand side, rising financialisation of household savings and the consequent growth in managed investment products[25] should continue to drive demand for corporate bonds.

The managed investment industry has more than doubled in the past five fiscals, led by superlative growth in the assets under management (AUM) of mutual funds, alternative investment funds and pension funds. The high growth in managed investment products is expected to continue over the medium term because of factors such as increasing financial literacy, rising investor sophistication in terms of retirement planning, higher awareness and use of insurance, investment objective aimed at beating inflation, and a growing middle-income population.

Key segments	Expected AUM growth	Key growth drivers
Retirement funds	Moderate to high	• Rising awareness of retirement planning, tax benefits • Flexibility to have 50-75% exposure to equity (NPS)
Insurance funds	Moderate	• Higher awareness and use of insurance products • Rising cost of private medical services
Mutual funds	High	• High returns of past attracting investors • Tax cut leading to more disposable income • Marketing of mutual fund products

Policy push required to enable the bond market to contribute more

While the pace of growth in assets under management (AUM) of the managed investments industry is expected to continue driving demand for corporate bonds, supportive policies are critical for a trajectory change. A large and diversified corporate bond market will also complement banks, especially during times when deposit growth is not keeping pace with credit growth.

Measures necessary to increase the contribution of the corporate bond market:

1. **Patient capital investors should be encouraged to invest down the rating curve:** Regulators should facilitate relaxing investment restrictions for below 'AA' rated issuances allowing investments into all investment grade rated papers from A to BBB. Currently, pension and insurance funds invest predominantly in "AA" and-above rated issuances, driven by rating floors prescribed by their regulators.

   While the Pension Fund Regulatory and Development Authority (PFRDA) has allowed National Pension Scheme to invest in 'A' rated papers, these investments between 'A' and 'AA-' rated securities are restricted to 10% of their overall debt portfolio. The insurance regulator also allows a maximum of 5-8% of debt investments into exposures rated 'A' or below for insurance companies.

2. **Patient capital investors can be encouraged to calibrate their risk taking in A and BBB rated infrastructure papers by using Expected Loss (EL) rating along with probability of default (PD) ratings:** Infrastructure assets are suitable for the risk appetite of patient capital investors requiring long tenure. Regulators can encourage lenders and issuers to use EL-based ratings, which factors both PD and LGD for efficient risk pricing of infrastructure assets.

[25] Insurance funds, mutual funds, retirement funds (PF and NPS), alternative investment funds (AIFs), and portfolio management services

3. **Investment limits for insurance companies linked to issuer's equity for infrastructure companies should be relaxed:** For insurance companies, investment exposure to infrastructure companies is linked to the project cost and the balance sheet parameters of the issuer and its parent.

   While exposure limits are essential for risk management, limits linked to the project cost and balance-sheet parameters of the issuer and its parent limits the ability of these companies to tap investments from insurance companies for take-out financing. Such limits need a revisit.

4. **Regulatory push for corporates to tap bond market can add to its depth and diversity:** A Crisil Ratings study on India's top 500 corporates by market capitalisation shows the top non-financial corporates (public and private sector) source only 20-30% of their domestic borrowings from the corporate bond market.

   The Securities and Exchange Board of India (SEBI), the capital market regulator, requires listed corporates with a credit rating of 'AA' or higher and long-term borrowings exceeding Rs 1,000 crore to meet 25% of their annual incremental borrowings through bond issuance (over a contiguous block of three years) reckoned from fiscal 2025. The RBI also mandates that all corporates with aggregate sanctioned credit limit from the banking system greater than Rs 10,000 crore meet 50% of their annual incremental funds through the capital market.

   The thresholds for defining large corporates can be revised downwards over the medium term, and the rating coverage can be expanded to all investment grade rating levels from 'AAA' to 'BBB-'. Revision of regulatory mandates of SEBI and the RBI can come a long way in deepening India's corporate bond market.

5. **Credit enhancement structures such as securitisation and partial guarantee also salutary:** Securitisation can enable lenders to churn their assets in the capital market, giving them more space to fund capex. Currently, the securitisation market in India forms ~1.3% of GDP, much lower than the US, where it's at 53% of GDP. The domestic market has to evolve to increase credit flow in the economy and enhance efficiency of the overall lending ecosystem. While private sector banks have actively participated in securitisation market as investors and also at times tactically issued pass-through certificates (PTCs), public sector banks have played a limited role, both as investors and issuers. Hence, government should create enabling policy and infrastructure in public sector banks to invest and issue PTCs.

   India also needs an enabling regulatory framework for covered bonds, which can act as a game changer in the securitisation market. Covered bonds are debt securities secured by a ringfenced pool of assets (cover pool), providing dual recourse (issuer and the cover pool) to the investors. The dual recourse feature acts as a credit enhancement with the credit risk profile of the covered bonds being superior to that of the issuer.

   Credit enhancement in the form of partial guarantee for infrastructure assets can help in bridging the risk appetite gap between capital markets and infrastructure bonds, thereby enabling these bonds to tap the capital market.

6. **Aligning taxation of debt mutual funds with other asset classes[26] can boost the short-to-medium tenure segment of the debt capital market:** Mutual funds have been a key investor segment in the bond market as they contribute nearly a sixth of the total outstanding bond market corpus. Mutual funds play a major role in the short-to-medium tenure segment of the bond market (commercial papers, certificates of deposit).

   The government revised the tax treatment of debt mutual funds in 2023. The changes included removal of the indexation benefit applicable for long-term capital gains and revision of tax rates applicable for long-term capital gains. Moreover, as per the new Income Tax Bill, 2025, all gains on debt mutual funds are now to be taxed at the slab rates with no indexation. These changes to tax treatment have impacted the competitiveness of debt mutual funds. Relaxing taxation on debt mutual funds can channel higher investments into these funds which has slowed down as compared to the overall AUM growth of the industry.

[26] A tax rate of 12.5% applicable for listed and unlisted securities (excluding debt instruments), and equity mutual funds

Assessing India's strengths in trade and manufacturing

India has long aspired to be a manufacturing powerhouse, integrated with global supply chains, in order to boost its exports, forex and growth.

However, success has been limited – the share of manufacturing in GDP has remained between 15.2% and 18.4% over the past three decades – and the country continues to be a service-driven economy.

Asian peers such as Korea, China, Malaysia and Vietnam have tasted far more success through timely reforms, policy push and trade agreements. What worked in favour of these economies was the globalisation push and increase in trade when they were reforming.

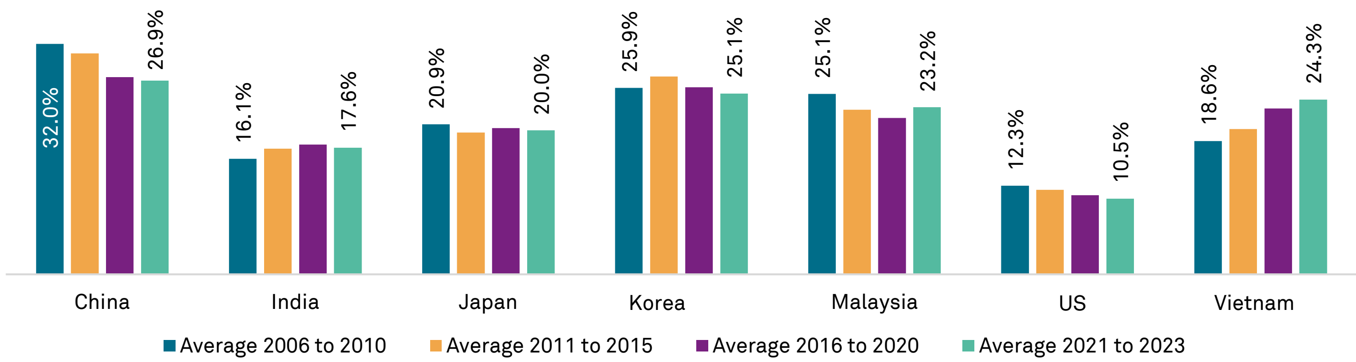
In India, there is sharp government focus today on expanding capabilities in new-age sectors, achieving higher localisation and driving backward integration in key value chains. Reforms, including the Make in India initiative, the phased manufacturing programme and the PLI scheme, are showing green shoots across sectors.

Riding on timely interventions, imposition of import duty and stringent quality control measures, sectors such as electronics and toys have become net exporters from being net importers five years ago.

While the government continues to push in this direction, the global environment presents many headwinds. The uncertainty around trade and tariffs makes it that much more difficult to acquire technology, scale up, and drive exports.

At ~17%, India's manufacturing share has headroom to grow, but exports need to navigate global headwinds

Value addition in manufacturing ($)



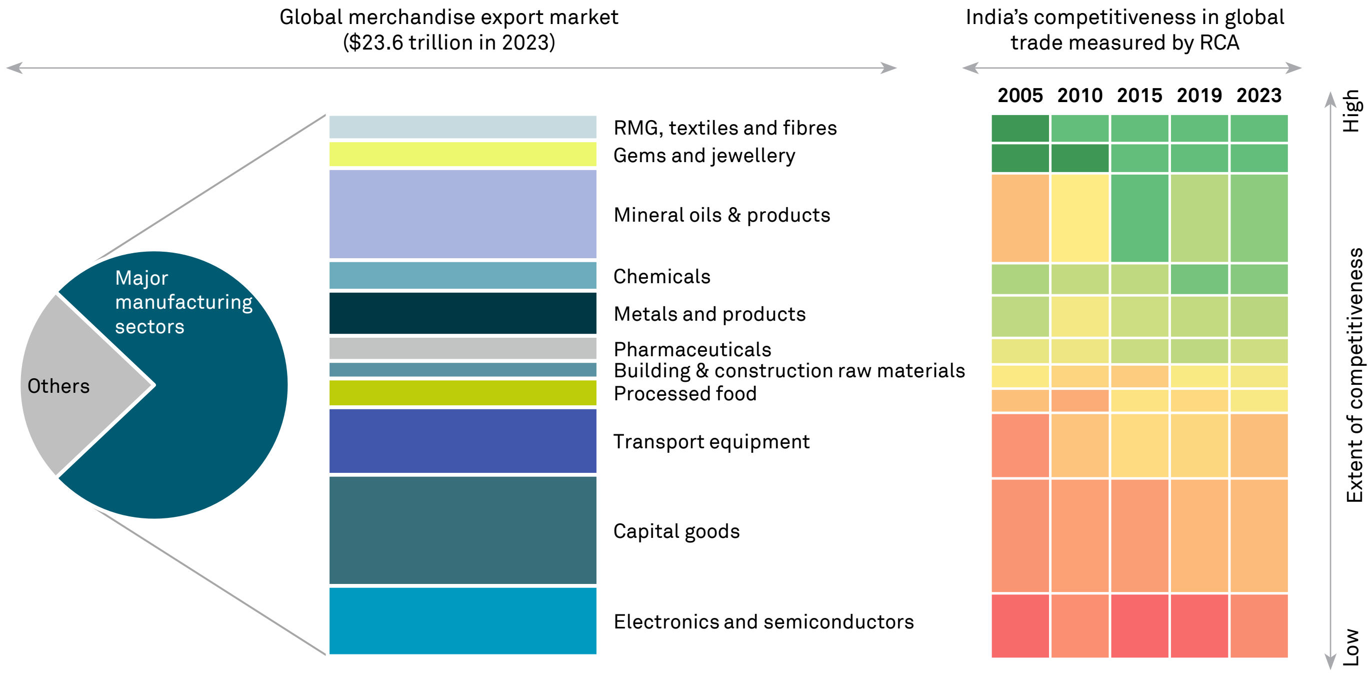
Note: Value added by economic activity at current price in US dollars for the US in 2021, Japan in 2022 and other countries in 2023
Source: World Bank Group

In this context, we have evaluated India's manufacturing capability, competitiveness and position in global trade for seven key sectors that account for a bulk of global merchandise trade.

As a starting point, we have used Revealed Comparative Advantage (RCA) as an indicator of India's core strength in a sector and then dived deep to dissect the strengths and inhibitors.

RCA compares the share of a commodity in a country's merchandise exports with the global share of the commodity's exports in merchandise exports. RCA measures a country's export share in a specific product or sector relative to the world's export share in it. An RCA value greater than 1 indicates that a country has a comparative advantage in that sector, meaning it is relatively more specialised in producing and exporting those goods.

India's comparative advantage[21] is improving in select sectors, albeit slowly



Note: RCA measures a country's export share in a specific product or sector relative to the world's export share in the same product or sector. An RCA value greater than 1 indicates that a country has a comparative advantage in that sector, meaning it is relatively more specialised in producing and exporting those goods.

- RCA of 0 to 0.2, i.e. negligible Indian exports compared with the global averages, indicating lack of competitiveness
- RCA of 0.2 to 0.6, i.e. ratio of Indian exports lower than the global average for the segment
- RCA of 0.6 to 1, i.e. share of Indian exports for the segment is on a par with the global average exports
- RCA of 1 to 2, i.e. share in Indian exports for the segment is higher than the global average, indicating an underlying competitiveness
- RCA above 2, i.e. the segment is more competitive compared with other Indian exports

Source: ITC Trade Map, Crisil Intelligence

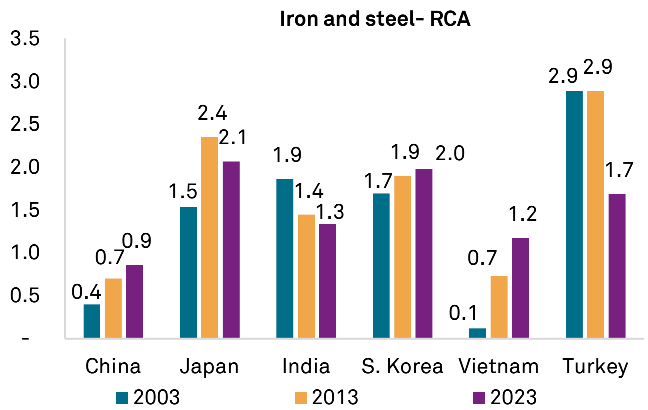
- Traditionally, India has been strong in exports of textiles and natural fibres such as cotton. However, a growing preference for man-made fibres and fast fashion has led to the emergence of RMG hubs such as Bangladesh, Vietnam and Cambodia
- In the mineral oil and derivatives segment, despite lacking domestic crude oil reserves, India's refining industry has achieved global competitiveness in exporting refined petroleum products. This is thanks to private refiners operating in special economic zones building the capability to produce Euro-V/VI grade fuel, suited for the global markets
- Chemical production has emerged as a new star in domestic manufacturing. Indeed, it is the fastest-growing segment of manufacturing GVA, driven by export substitution for bulk chemicals
- In food processing, which is predominantly an MSME sector, digital proliferation has led to a better understanding of consumer preferences, cultural

[21] RCA measures a country's export share in a specific product or sector relative to the world's export share in that same product or sector. An RCA value greater than 1 indicates that a country has a comparative advantage in that sector, meaning it is relatively more specialised in producing and exporting those goods. By combining import/export analysis with RCA, we can gain deeper insights into sectoral competitiveness. For instance, a sector with high exports and a high RCA suggests strong international competitiveness. Conversely, a sector with high imports and a low RCA may indicate a lack of competitiveness and potential reliance on foreign production. This combined approach helps identify sectors where India excels, those that need improvement and those with a potential for future growth.

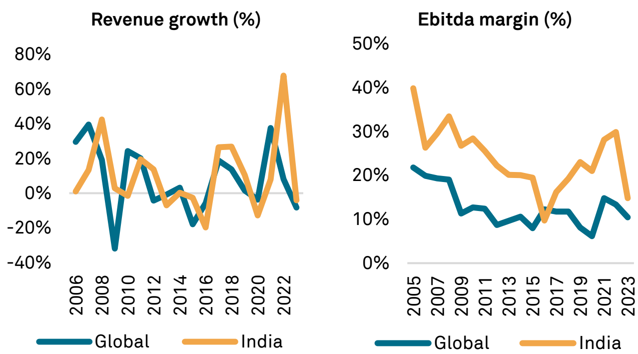
nuances and regulatory requirements in target markets. The government's efforts to support MSME exports are starting to show results

- In new-age sectors such as semiconductors, communication equipment and electronics, India is developing manufacturing capabilities, starting with assembly. The country's imports in these segments are currently thrice the value of its exports. As observed from global markets over the past few decades, low-value assembly is triggered by policy support and incentives. The next phase emphasises critical sub-assemblies, which are widely imported and have high value addition. This eventually creates an ecosystem of indigenous product development and manufacturing

India's competitiveness in key sectors

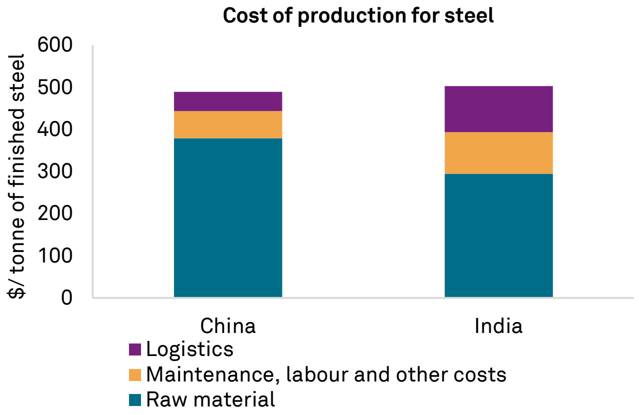


Source: ITC Trade Map, Crisil Intelligence



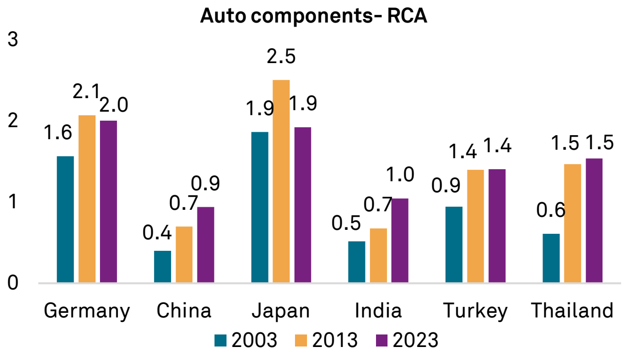
Note: Four prominent global steel manufactures in East Asia are compared with four major steel manufacturers in India.
Source: Company disclosures, Crisil Intelligence

- India is the second-largest steel producer in the world, albeit significantly behind China, in terms of absolute production volume. Notably, ~95% of steel produced in India is consumed domestically, which limits its influence in the global market
- The global steel industry is characterised by overcapacity, creating a highly competitive market that squeezes export margins. As a result, Indian steel mills face challenges in exporting to destinations beyond controlled markets such as Europe
- Indian steelmakers benefit from access to domestically sourced iron ore that is 20-30% cheaper than international benchmarks. However, this advantage is partially offset by higher logistics and manufacturing costs
- The Indian steel industry's focus on the domestic market is a strategic response to the challenging conditions in the global market. By prioritising domestic sales, Indian steelmakers capitalise on growing demand and mitigate the risks associated with exports to less-profitable destinations

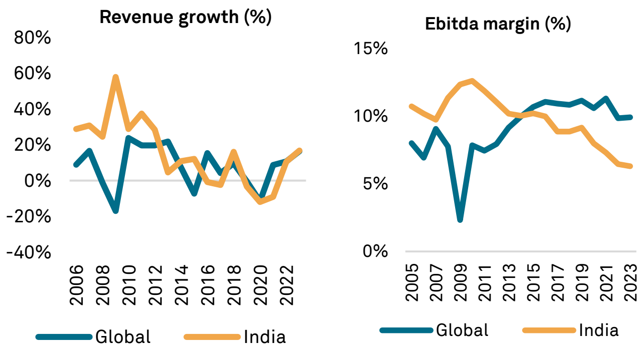


Note: Cost of production of hot-rolled flat steel via the blast furnace-basic oxygen furnace route is considered for fiscal 2024.
Source: Crisil Intelligence

- Despite the global oversupply in steel, India remains a region of interest for investments in new steel production, driven by growing domestic demand. However, global investment in new steel production is generally lower due to challenging market conditions
- Given the low per capita penetration of steel in the domestic market, at 93 kg compared with the global average of 219 kg, there is a significant headroom for demand growth in India

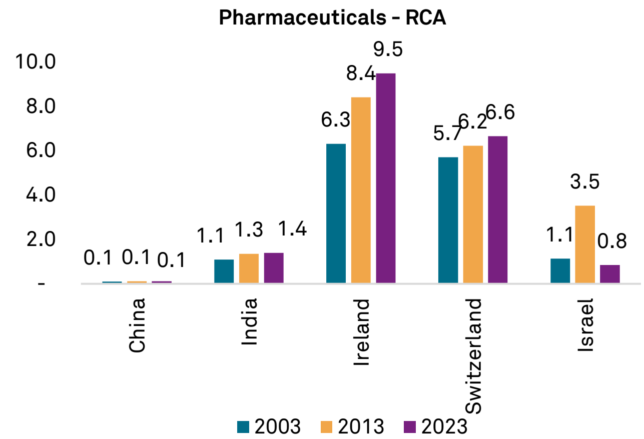


Source: ITC Trade Map

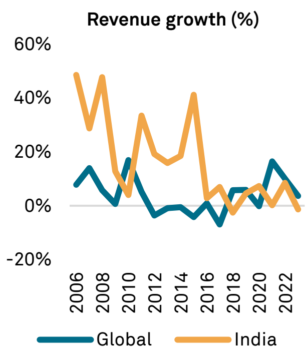


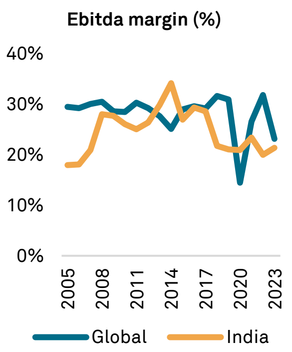
Source: Company disclosures, Crisil Intelligence

- India's auto component industry has undergone significant transformation. The domestic market accounts for 80-85% of the annual production. Exports are traditionally focused on low-value, non-critical components. However, with foreign players investing in India, OEMs localising parts, and government regulations driving change, auto component localisation has reached 85%. Critical components such as engines and transmissions now make up over 65% of exports, with developed countries accounting for more than 50% of the export mix
- The shift towards electrification has led to an increase in EV-specific components. The Indian government's push for electric mobility, supported by schemes such as FAME, PM e-Drive, and PLI, is driving the localisation of critical EV components such as lithium-ion batteries and power electronics. This trend is expected to enhance India's cost-competitiveness and position it as a key supplier in the global EV value chain, leveraging its strength as the largest 2- and 3-wheeler market and an emerging hub for passenger vehicle exports
- As Indian auto component manufacturers integrate into global supply chains, they are leveraging their cost advantages and the convergence of regulatory standards. Deepening localisation of critical components, including semiconductors, high-performance alloys, and EV components, will reduce India's dependence on imports and strengthen its supply chain resilience. This, in turn, will make Indian firms more attractive to global OEMs, further solidifying India's position in the global automotive industry



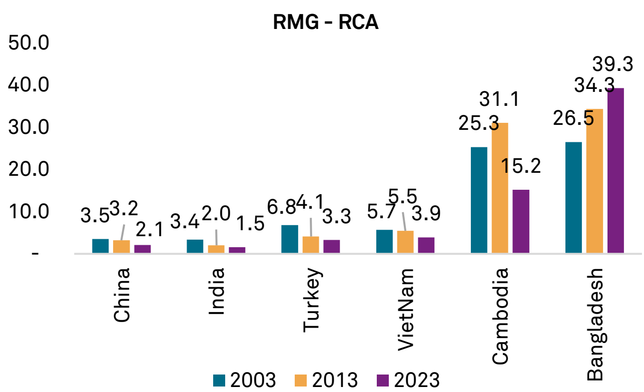
Source: ITC Trade Map





Source: Company disclosures, Crisil Intelligence

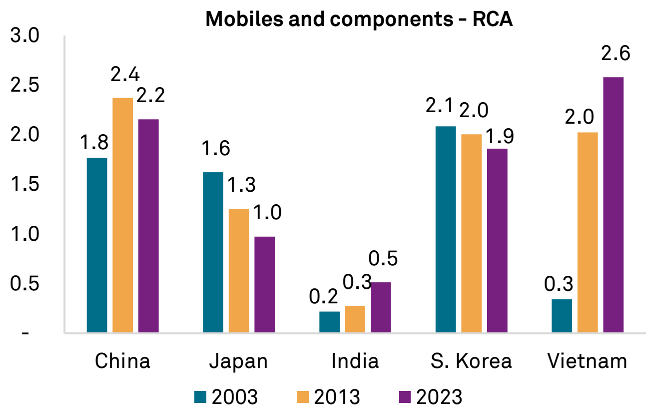
- India is the global leader in generic pharmaceutical production, with a significant hold in developing markets such as Africa and Latin America and developed markets such as the US
- Revealed competitiveness of Indian pharma sector is significantly higher than its Asian peers. However, some nations have invested significantly in drug discovery and research to get ahead
- India is dependent on imports for key inputs such as active pharmaceutical ingredients (APIs) and key starting materials (KSMs)
- Even with imported APIs and KSMs, the margins of Indian producers are in line with those of global innovators
- Through PLI schemes and large-scale domestic capacity expansion, there is a shift towards production of raw materials in the country. This move enhances supply security and cost-competitiveness in the global pharmaceutical landscape
- A growing number of Indian companies are securing approvals from regulators, such as the US Food and Drug Administration and European Medicines Agency for high-margin segments such as complex generics, biosimilars, and injectables. This is expected to improve India's positioning in the global pharmaceutical market
- Indian companies are increasing investments in R&D for biologics and precision medicine, shifting from a generics-dominated to innovation-led growth model. Collaborations with global biotech firms and contract research are further enhancing India's competitiveness in the sector



Source: ITC Trade Map

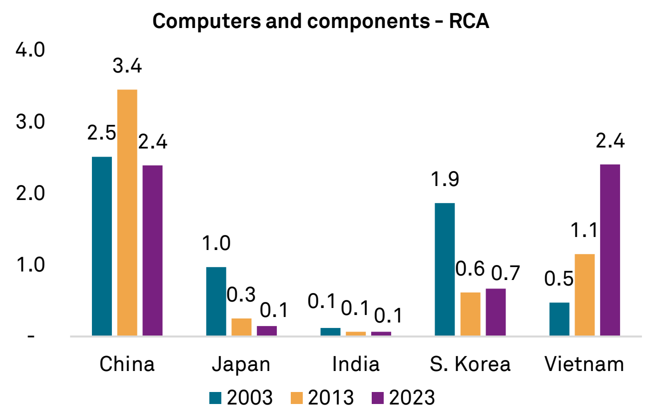
- The RMG industry, estimated at Rs 5.5 trillion, is one of India's largest employers in the unorganised and non-agrarian segment and contributes 2% to the GVA
- The strength of India's exports lies in cotton and natural textiles and products thereof, which keep the country competitive in a highly cost-conscious market
- In the last decade, competition from Asian and East European countries in the fast fashion market kept India's export growth in check, while competitors such as Bangladesh and Vietnam grew ~2x by adopting man-made and technical textiles faster

- The key challenge is that competitiveness declines as we move up the value chain from fibres to basic textiles to garments
- Nearly 60% of global textile consumption is driven by man-made fibres. But India has just 5% of the man-made fibres market. This provides an opportunity for growth in the segment. PLI for man-made fibre apparel and fabrics, as well as technical textiles, supports the segment
- The government's 5F — farm to fibre to factory to fashion to foreign (export) — push is expected to revitalise the traditional textiles sector



Source: ITC Trade Map, Crisil Intelligence

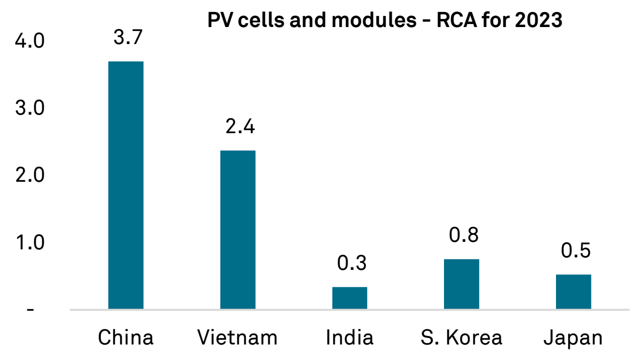
- India's electronics export market is dominated by smartphones, which account for over 40% of its exports
- In the past 10 years, there has been significant growth in mobile assembly. Large global players are setting up shop in the country to cater to both Indian and export markets
- As assemblers, industry players face lower margins because they are still importing the components. Growth in assembly operations and governments support via PLI scheme has created the right environment for India to move up the value chain
- Component manufacturing, together with focus on semiconductor manufacturing, will reduce dependence on imports
- The industry is expanding rapidly and the increasing revenue growth compared with global players indicates a faster pace of adoption of PLI schemes for both components and mobile phones



Source: ITC Trade Map, Crisil Intelligence

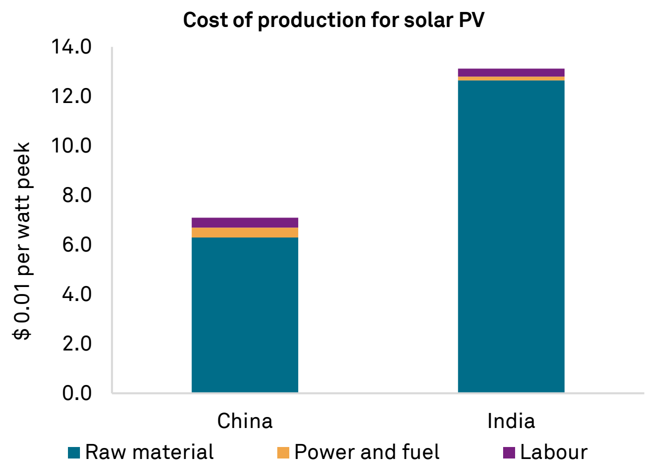
- India is not a major player in the IT hardware export market. But the situation is about to change as the government is replicating the steps it took to make India a mobile manufacturing hub
- India has raised duties on laptops, personal computers and components to push local assembly and reduce reliance on imports, especially from China. This, coupled with a Rs 17,000 crore PLI scheme, is attracting global players to set up shop in the country. At the same time, global firms are now looking to set up manufacturing bases outside China, too. All these position India as an attractive alternative for IT hardware production

- An increase in local assembly will push suppliers to set up printed circuit board, battery and semiconductor units in the country, strengthening the value chain
- With policy support, the sector is expected to reduce a significant portion of its imports, valued at ~Rs 1 lakh crore in fiscal 2024. However, it remains to be seen whether India can replicate the success seen in mobile exports



Source: ITC Trade Map

Cost comparison between Indian and Chinese PV modules

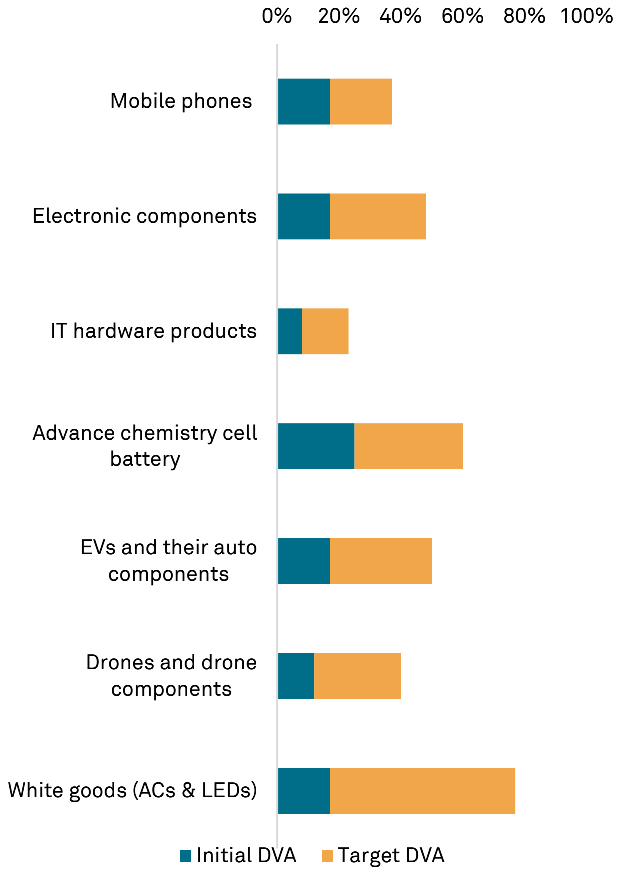


Note: Cost of a solar PV module assembled in China is compared with the cost of a module assembled in India.
Source: Crisil Intelligence

- As the solar PV and cell industry is younger than other manufacturing industries, China's concentration in the industry is significantly high. However, domestic demand is expected to boost manufacturing in India
- The country's power demand is likely to log a 5-7% CAGR till fiscal 2030 on the back of the manufacturing push, increase in per capita power consumption and vagaries of the weather. This demand is expected to be met by renewable energy generation, where solar PV modules are the front runner
- Significant safety nets have been put in place to keep the solar PV ecosystem viable, including the Approved List of Models and Manufacturers (ALMM), higher duties on assembled modules, domestic demand creation through the National Solar Mission and other schemes
- The cost of manufacturing in India is higher since most module manufacturers use imported PV cells — an intermediate product — during assembly. Global manufacturers with in-house cell manufacturing capabilities use silicon wafers as the starting point
- The technological changes and dynamic market for PV modules make it apt for exports
- Over the next five years, we expect almost quarter of India's module facilities to be backward integrated with solar chip manufacturing facilities

Increase in DVA to reduce import dependency and improve competitiveness

Domestic value-add targets for PLI scheme



Source: Crisil Intelligence, PLI scheme documents

Of the Rs 1.95 lakh crore under the PLI scheme, half is being invested to strengthen domestic manufacturing and exports and the rest is being channelled toward localising imports.

As was seen in the last two Union Budgets, the government has taken efforts to rationalise the customs duty structure for industrial goods — reducing duties on inputs and raising them on final products. The recent announcement to promote DVA for LED panels and investment in electronics was in line with this.

Through these interventions, the government aims to improve DVA and build an ecosystem for solar PV cells, EV batteries, motors and controllers, electrolysers, wind turbines, very high voltage transmission equipment and grid-scale batteries to aid India's backward integration efforts in clean energy.

For example, the PLI scheme for the automotive and auto component industry requires a minimum 50% DVA. A testing agency of the Ministry of Heavy Industries will certify DVA in the eligible products before disbursing incentives.

The results of such policies in stimulating the manufacturing sector are becoming increasingly evident, though the fast-evolving global, technological and commodity dynamics will require close monitoring.

As India transitions to value-added manufacturing, emerging sectors such as EVs, semiconductors and electronics are poised to become the main drivers of industrial capex. These segments are projected to account for more than 70% of the non-PLI emerging sector capex, underscoring the country's shift towards sustainable and tech-driven growth.

India has long aspired to be a serious contender in the hi-tech and electronics manufacturing industry and become a credible alternative to China in this space. However, it has been unable to replicate its success in services exports in the manufacturing sector. An important reason for this is its lower rank on key investment criteria. India was placed 25th and 53rd in the World Competitiveness Ranking 2024 on business efficiency and infrastructure, respectively. China ranked 15th on both parameters.

Despite the progressive reforms and pro-business initiatives, India's ecosystem continues to face challenges on account of low labour productivity, high logistics and power costs, and limited innovation.

India's manufacturing sector holds considerable potential for driving economic growth and enhancing global influence. A sophisticated strategy, encompassing the following interconnected pillars, is crucial to achieve the target:

Strategic import substitution and deepening of DVA

- India is moving beyond simply replacing imports. The focus is on strategically developing domestic capabilities that enhance value addition and create globally competitive products, including photovoltaic module manufacturing and advanced chemistry cell batteries. This involves a transition from replicating imported goods to innovating and developing indigenous technologies and designs
- A nuanced approach is being adopted, tailoring interventions to address specific sectors and their unique challenges. For instance, the semiconductor industry, a key focus area of the Semiconductor Mission, is receiving substantial capital investment and targeted skills development initiatives. The textile sector, with potential benefits from schemes such as the PLI scheme, is receiving support in areas such as design and branding
- In the defence sector, developing strong domestic supply chains and ancillary industries is a priority, which involves fostering collaboration between large global enterprises and Indian companies, promoting technology transfer, and creating a conducive environment for innovation
- While strategic protection of nascent industries is considered where necessary, it is being implemented judiciously and for a limited time. For example, it has been actualised for solar and semiconductor manufacturing. The goal is to nurture such industries until they can compete globally but not create long-term dependence on government support

Navigating the transition to premium export markets

- India is moving beyond competing solely on price. The strategy emphasises quality, innovation, and brand building. Indian manufacturers are investing in R&D, design capabilities, and marketing to create products that appeal to discerning consumers in premium markets. The shift from the Association of Southeast Asian Nations and Africa to Europe and North America markets in automobile and component exports aptly demonstrates this trend
- In food processing, the priority is to develop a deep understanding of consumer preferences, cultural nuances, and regulatory requirements in target markets. This involves market research, cultural sensitivity training, and building relationships with local partners
- In textiles, instead of attempting to compete across the board, India is focusing on specialisations. This could involve targeting specific product segments or catering to specialised needs. A case in point is natural fibre-based fabrics, where it has a competitive advantage

Cultivating targeted export-oriented manufacturing

- The focus is on sectors that have high export potential and where India has advantages. Food processing, with potential benefits from initiatives such as the Pradhan Mantri Kisan Sampada Yojana, along with pharmaceuticals and textiles are prime examples, with other sectors such as automotive components and specialty chemicals also under consideration
- The challenges unique to each sector are gradually reducing. For food processing, cold chain infrastructure and food safety regulations are critical areas of focus. For pharmaceuticals, regulatory harmonisation and intellectual property protection are important considerations
- Integrating Indian manufacturers into the global value chain is a key strategy to gain access to new markets, technologies and expertise. This involves creating partnerships with multinational corporations and promoting participation in international trade fairs and exhibitions

Strengthening four pillars to boost manufacturing

India is building a strong domestic manufacturing ecosystem by focusing on four interconnected pillars: infrastructure for a solid foundation, technology for modernisation, skill development for a capable workforce, and market access to drive demand and growth. These pillars synergistically create a fertile environment for success in manufacturing.

Skill development: Empowering the workforce

- Focusing on vocational training, expanding and modernising industrial training institutes and vocational training centres via Skill India Mission
- Developing programmes to promote skills relevant to industry needs
- Implementing upskilling/reskilling programmes for workforce to adapt to new technologies
- Incentivising industry for apprenticeships and practical training

Infrastructure: Foundation for efficiency

- Investing in projects for efficient roads (Bharatmala), ports (Sagarmala) and freight corridors for smooth movement of goods
- Ensuring consistent power supply and competitive pricing
- Developing industrial parks and SEZs offering ready infrastructure and clearances

Technology: Driving modernisation and competitiveness

- Supporting domestic R&D in manufacturing technologies
- Facilitating access and absorption of global technologies vis-à-vis technology transfer
- Ensuring targeted tech support for MSME-led sectors such as textiles and food processing to adopt best practices

Market access: Creating demand & opportunity

- Promoting Make in India and encouraging procurement of local goods
- Focusing on FTAs, support for accessing international markets
- Implementing a judicious trade policy that can balance competition and strategic protection
- Simplifying regulations and reducing bureaucracy for smooth trade operations

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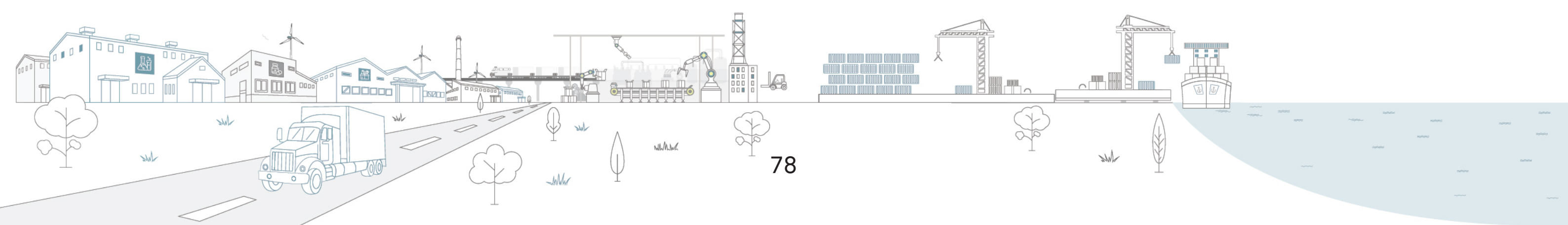

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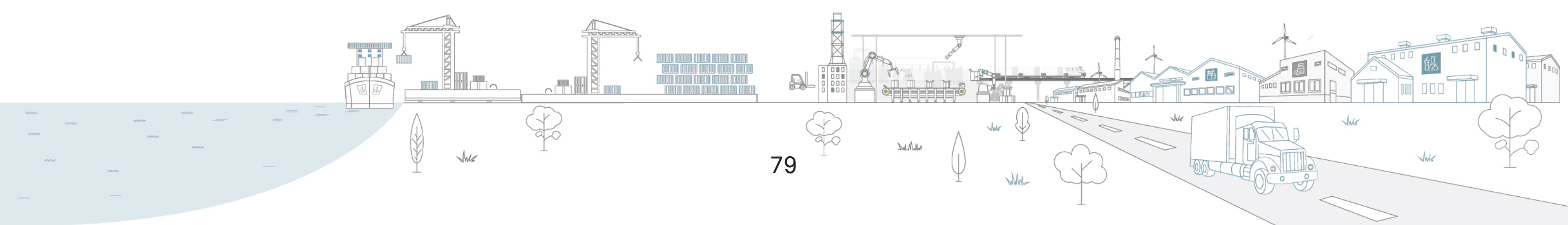

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