Subdued core inflation allows room for easing cycle: MER

OTHER ISSUES. The report flags concerns over slow credit growth, weak private investment

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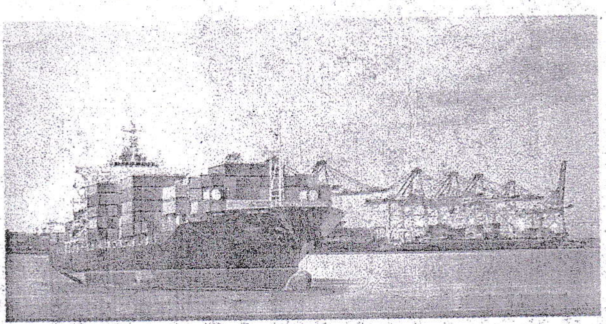
Ahead of the Monetary Policy Committee meeting (MPC), a Finance Ministry report said that comfortably lower inflation gives 'affording room for the easing cycle to be sustained'.

Meanwhile, the report stated that no decision has yet been made on the trade agreement, and India's external trade is likely to be affected in the coming quarters. It also cautioned about lower credit growth and private investment, which could impact economic momentum.

Retail inflation based on Consumer Price Index (CPI) dipped to a 76-month low of 2.1 per cent in June. This has initiated a debate on whether the MPC, in its next meeting – August 4 to 6 – will cut the policy interest rate again, although many economists believe there will be no cut after a 1 per cent cut in the last three policy reviews.



TARIFF THREAT. Continued uncertainty on the US tariff front may weigh on India's trade performance in the coming quarters

INFLATION OUTLOOK

Meanwhile, the Monthly Economic Review, as prepared by the Economic Affairs Department of the Finance Ministry, said: "Core inflation remains subdued, and overall inflation is comfortably below the RBI's 4 per cent target, affording room for the easing cycle to be sustained," the RBI has projected headline inflation at 3.4 per cent for the Q2 of FY26, while in Q1, actual inflation came below the Q1 target of the RBI.

"It appears likely that the full fiscal year inflation rate would undershoot the central bank's expectation of 3.7 per cent," the MER said.

It also noted that global crude oil prices are expected to remain subdued, following a larger-than-anticipated production hike by OPEC and its allies, who raised output by 548,000 barrels per day in August, on top of the production increases announced for the previous months. Meanwhile, MER stated that, despite a broadly positive outlook, downside risks remain.

"While geopolitical tensions have not elevated further, the global slowdown, particularly in the US (which shrank by 0.5 per cent in Q1 2025), could dampen further demand for Indian exports. Continued uncertainty on the US tariff front may weigh on India's trade performance in the coming quarters," it said. It may be noted that the US has set a deadline for concluding the trade deal, but as of now, there is no clear indication of when the deal will happen.

Talking about other risk factors, MER said: "Slow credit growth and private investment appetite may restrict acceleration in economic momentum." Further, given the deflationary trend in the wholesale price index, one has to observe economic momentum in nominal quantities. Measured in constant prices, economic activity may appear healthier than it is.

DOMESTIC SUPPLY

All that said, the economy has the look and feel of "steady as she goes" as far as FY26 is concerned. In the medium term, "given the ongoing momentous shifts in global supply chains in the areas of semiconductor chips, rare earths and magnets, India has its task cut out."

The review also said that overall, the first quarter of FY26 presents a picture of resilient domestic supply and demand fundamentals.

"With inflation remaining within the target range and monsoon progress on track, the domestic economy enters the second quarter of FY26 on a relatively firm footing," it said.

While the growth numbers for the April-June quarter (Q1) will be formally released on August 29, and for the July-September quarter (Q2), they will be out on November 28.