



India: Q1-FY26 GDP growth
'front' loaded, yet
'back'ward looking &
unsustainable

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Q1-FY26 GDP growth at 7.8% came in way higher than our above consensus estimate of 7%. In this note, we attempt to resolve the mysterious GDP puzzle - a key topic of debate even though the data is backward looking and growth was frontloaded in a world where activity gained pace ahead of the end of the 90-day pause on the reciprocal tariffs while election qtr base effects also provided a boost.

A. Unravelling the GDP puzzle

The growth spike can be explained by 2 key factors: 1/ One-offs and 2/ Data inconsistencies prone to revisions

First, the One-offs:

- 1/ Drop in GDP deflator to lowest levels since Sep-2019 qtr (*the unknown*)
- 2/ Pickup in manufacturing GVA growth despite slowdown in earnings as per RBI data (*the unknown*)
- 3/ Spike in public admin growth to ~10% on favourable base effects given elections last year (*the known*)

Second, Data inconsistencies prone to revisions

- 1/ Large role of discrepancies in GDP growth at (+)1.8 percentage points flagging possibility of data revisions later
- 2/ Recovery in consumption GDP & trade GVA despite mixed lead indicator performance & slip in agri (rural demand metric)

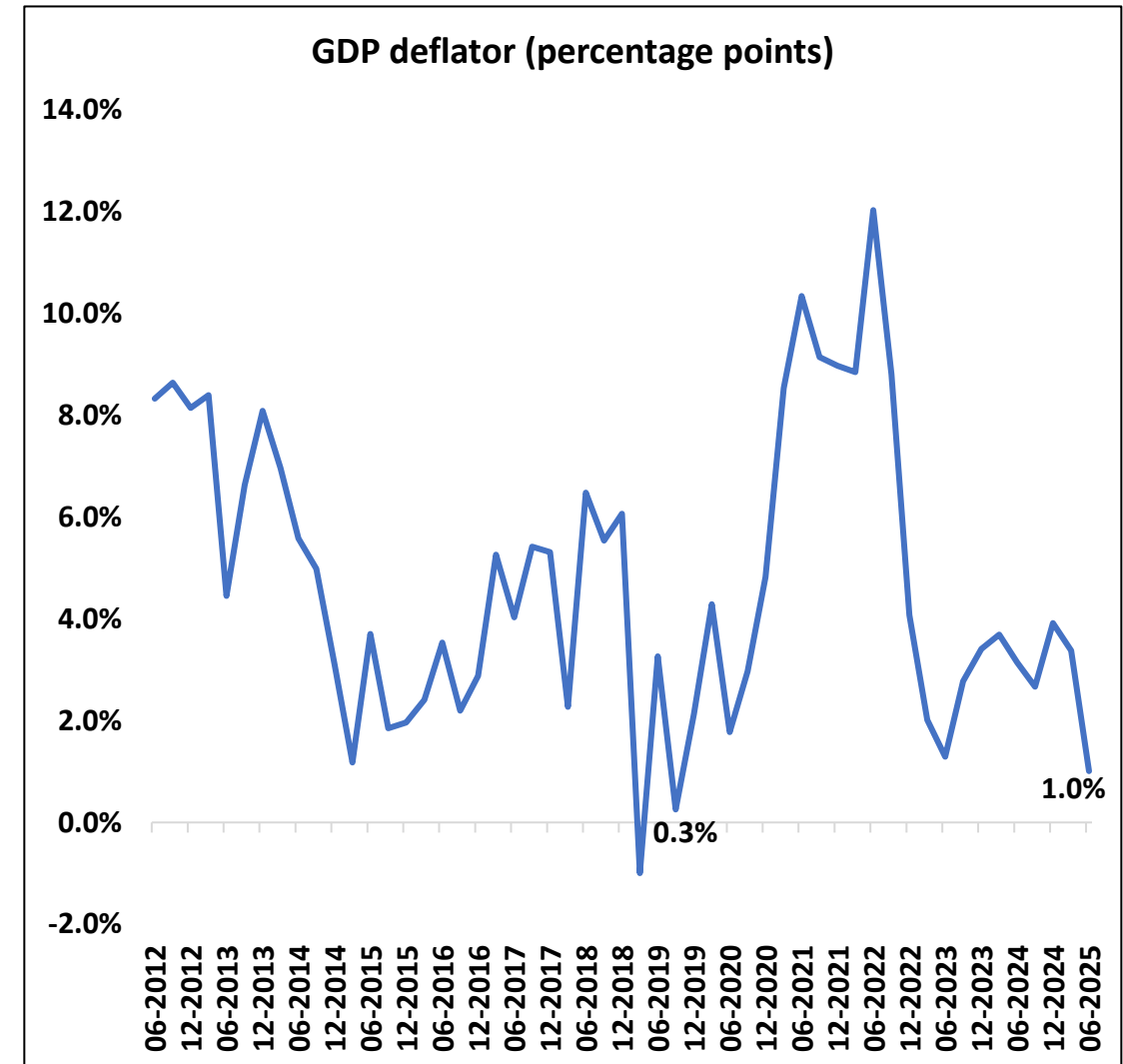
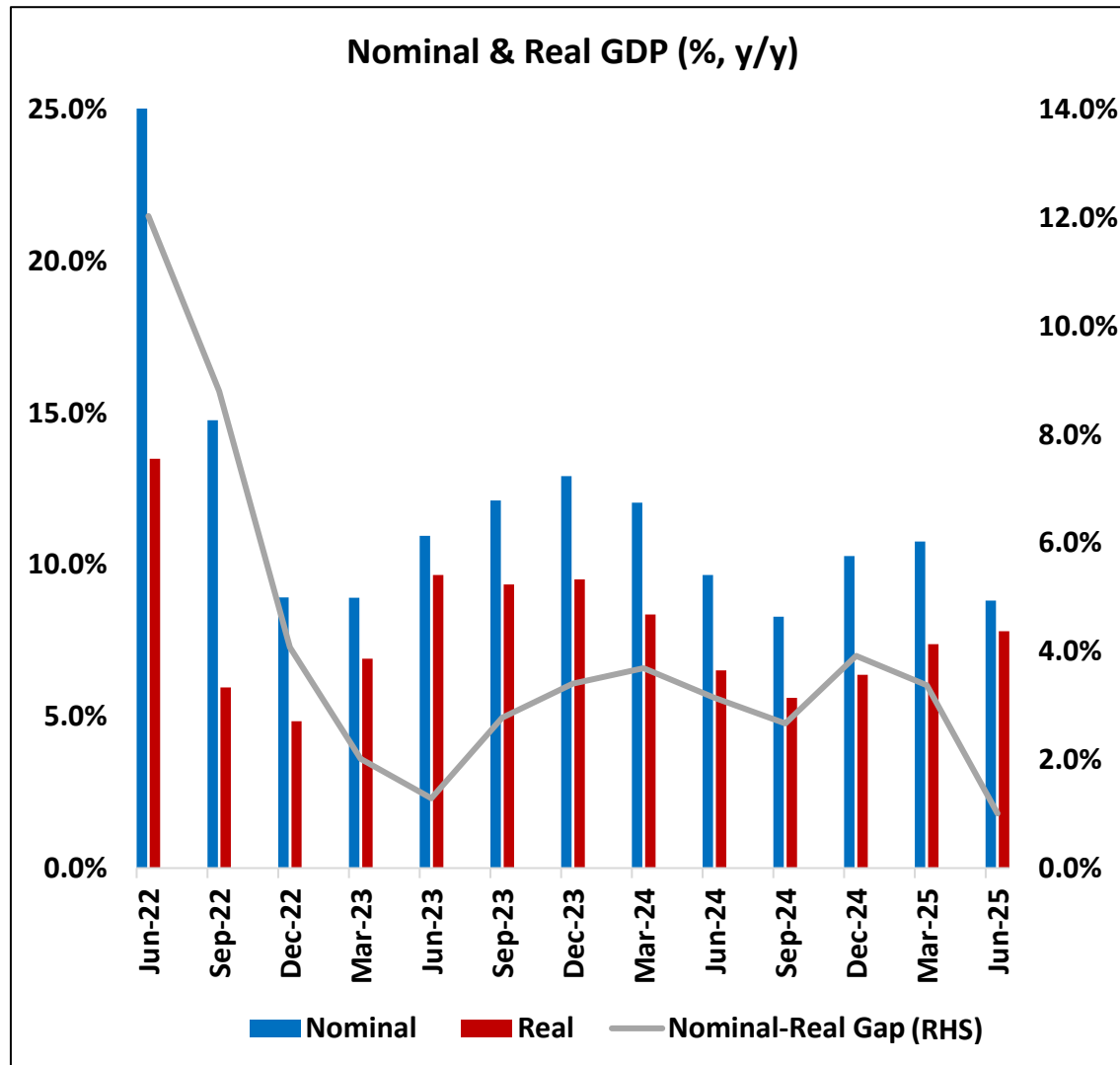
B. Is it the right time to revise GDP growth numbers for FY26? We align with MPC's 6.5% forecast yet many moving parts

We estimate the impact of 50% US tariff hike of at least ~50bps on GDP growth as 1% of GDP (non-exempt exports by India to US) affected. Going forward, FY26 growth arithmetic has many moving parts like uncertainty over 50% tariffs, impact on capex entitlement and growth boost from GST reform in H2-FY26. Yet with qtrly avg improving post Q1-FY26 data, we revise up our FY26 growth forecast by 20bps to 6.5%.

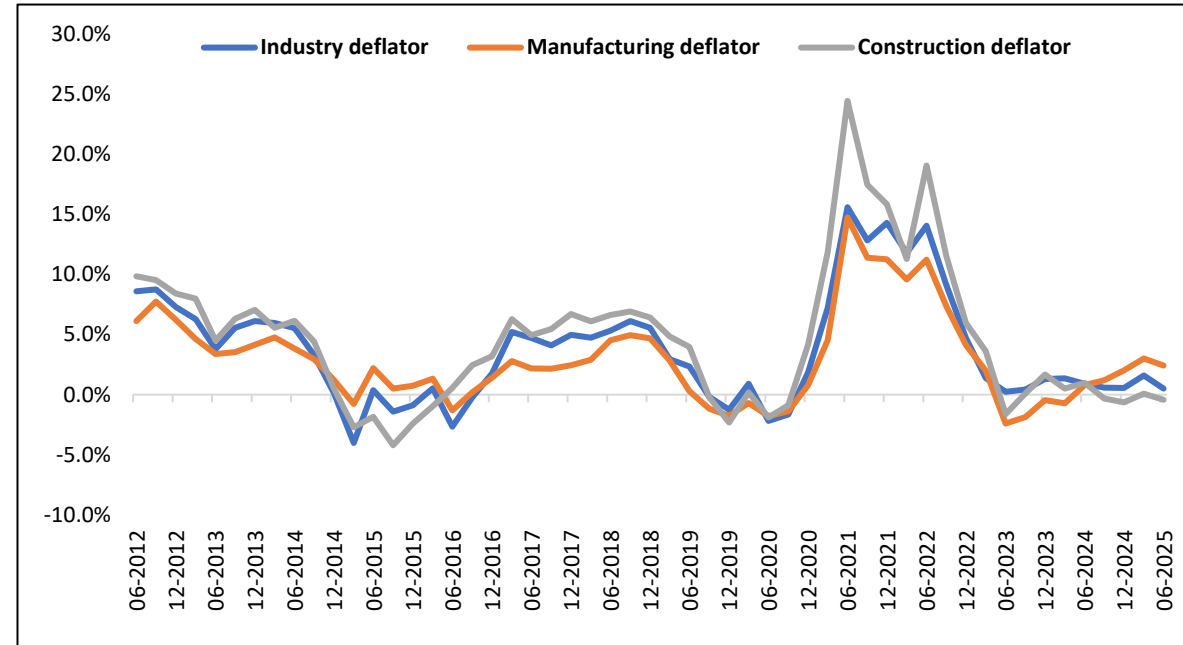
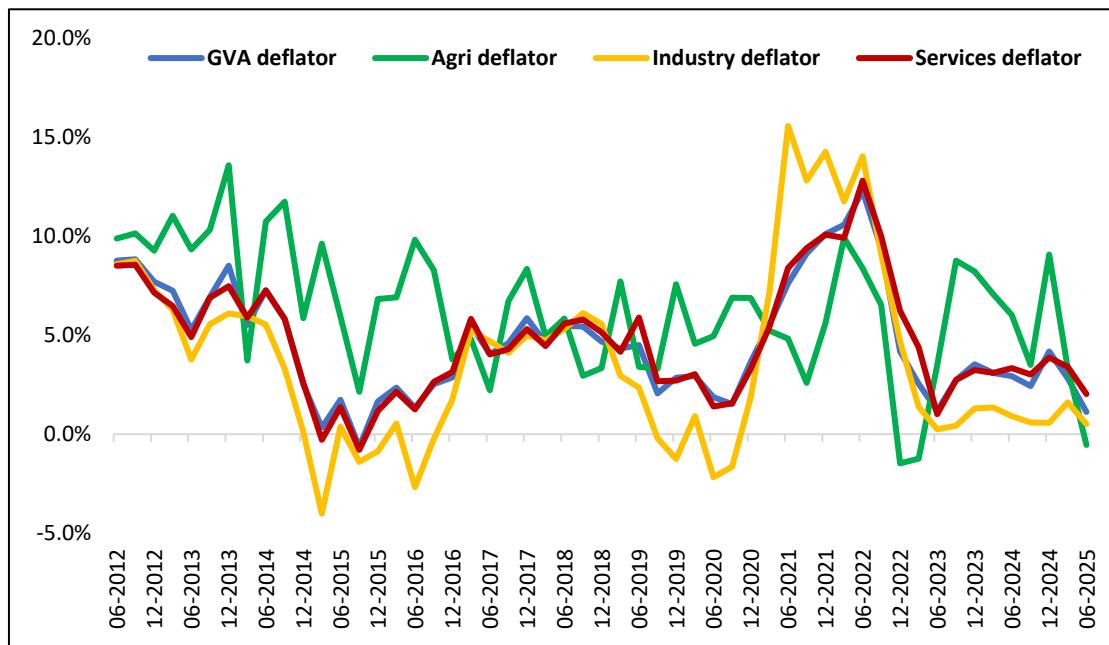
C. Will this data affect proposed policy measures to save tariff impact on growth? We don't agree & propose urgent stimulus efforts

We believe in urgent stimulus for affected sectors like textiles, gems & jewellery, shrimps etc. with a combination of direct support, credit guarantees, interest subvention etc to limit the impact on fiscal dynamics. Also, while there have been receding rate cut expectations, we maintain our call of a token 25-50 bps rate cut(s) in H2-FY26 apart from steps like credit restructuring, liquidity steps etc.

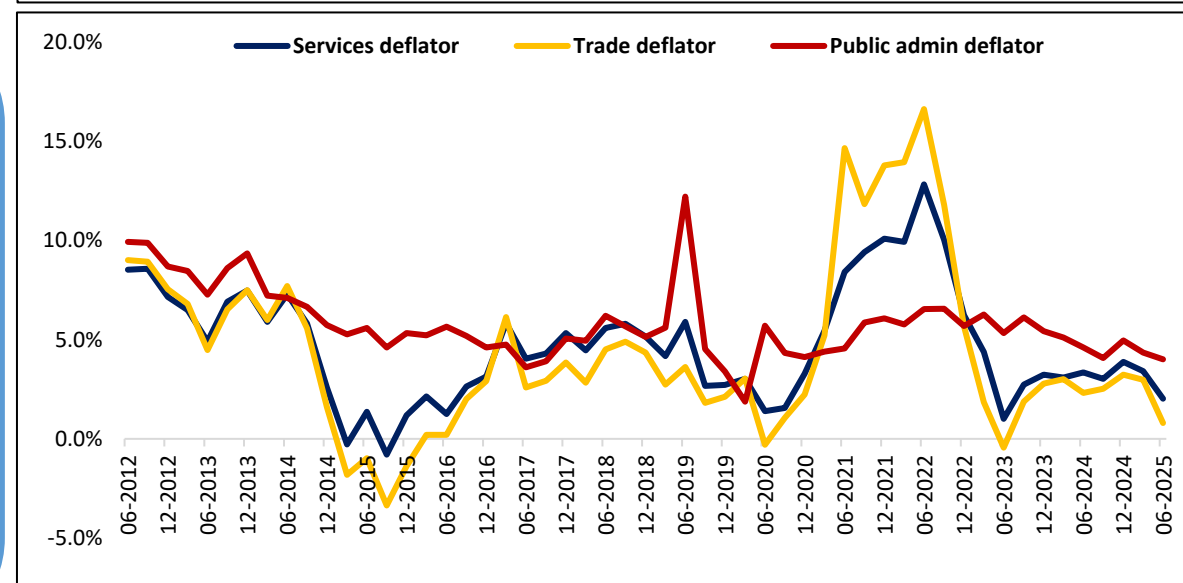
While nominal growth saw a drop as expected, real growth was propped up by fall in GDP deflator to ~6-year lows



Deflator showed a marked divide across sectors and propped up real growth somewhat



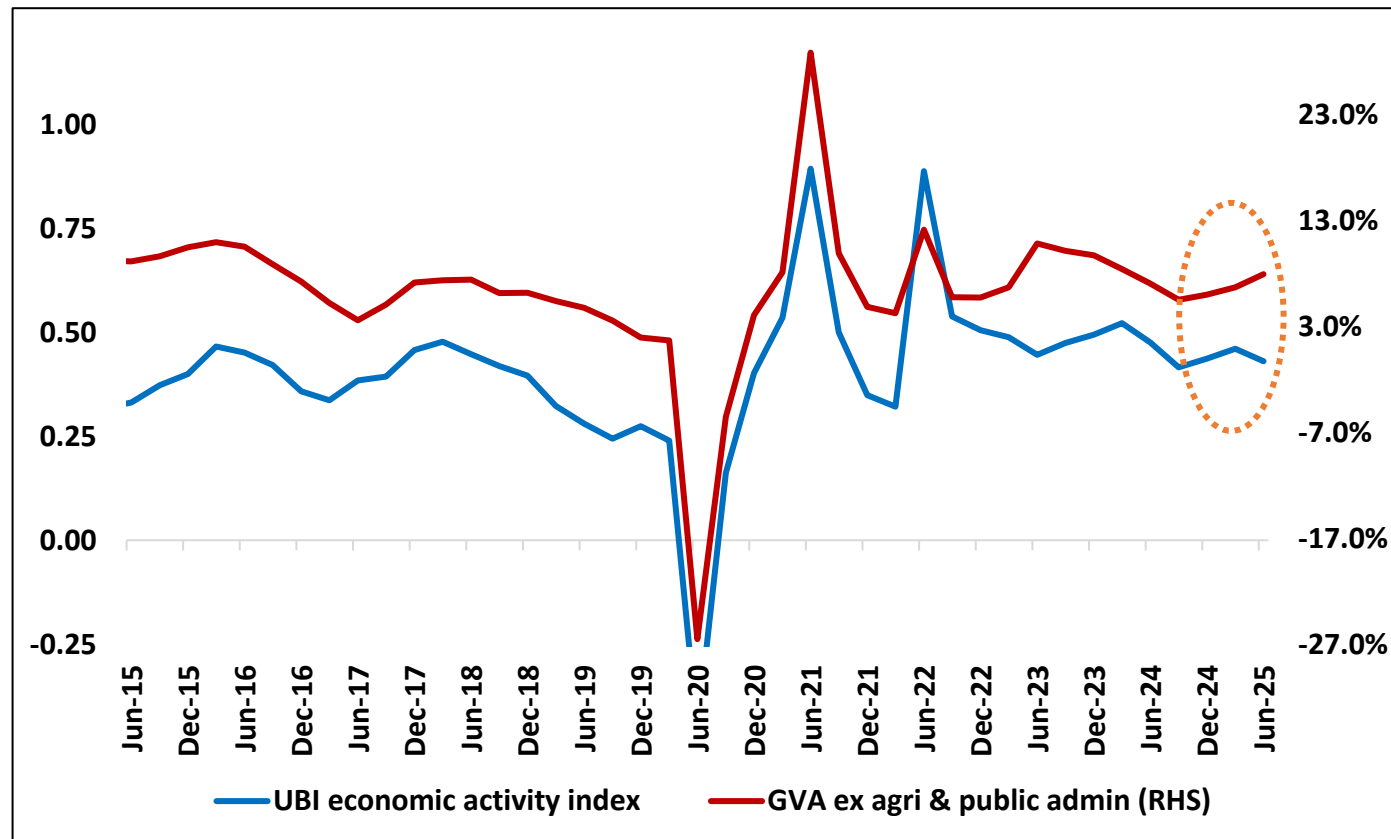
- While GVA deflator (simply estimated as gap between nominal and real GVA growth) has slipped to 1ppt (percentage points) in Q1-FY26 vs 3.4% last qtr, it varied widely across sectors
- Deflator was (-)0.5ppt for agri, keeping real growth muted while it was (+)0.5ppt for industry (& 2.4ppt for mfg showing limited role of deflator in explaining real growth spike)
- Within services, variation was even more stark, with overall deflator at +2ppt, led by only +0.8ppt in trade (explaining real growth spike), +1.6ppt in fin & real est and +4ppt in public admin showing growth spike was led by other factors



Real GVA growth data surprises were primarily seen in manufacturing, trade & transport and Fin. & real est. sub-sectors

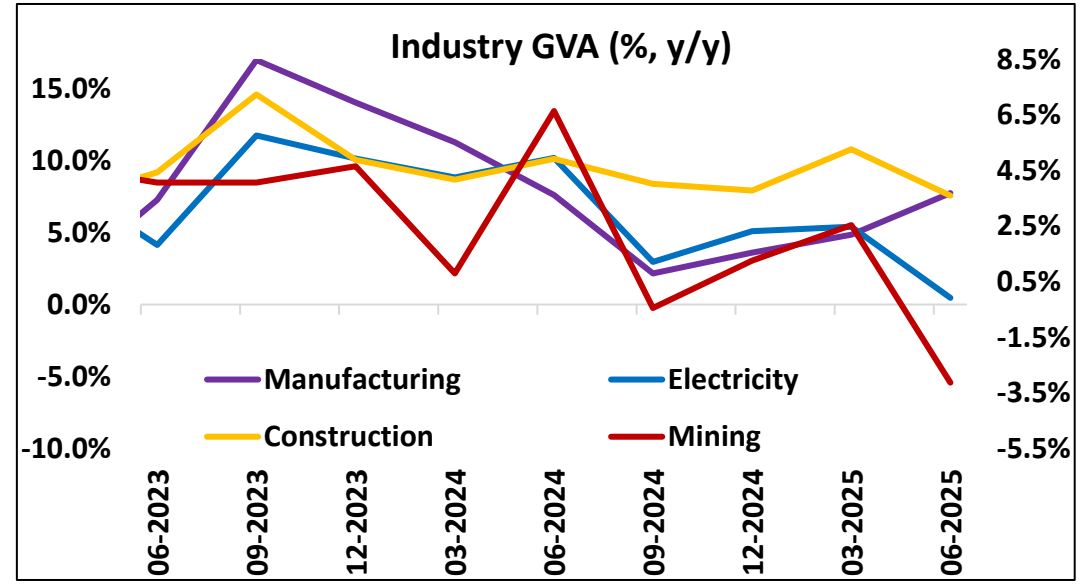
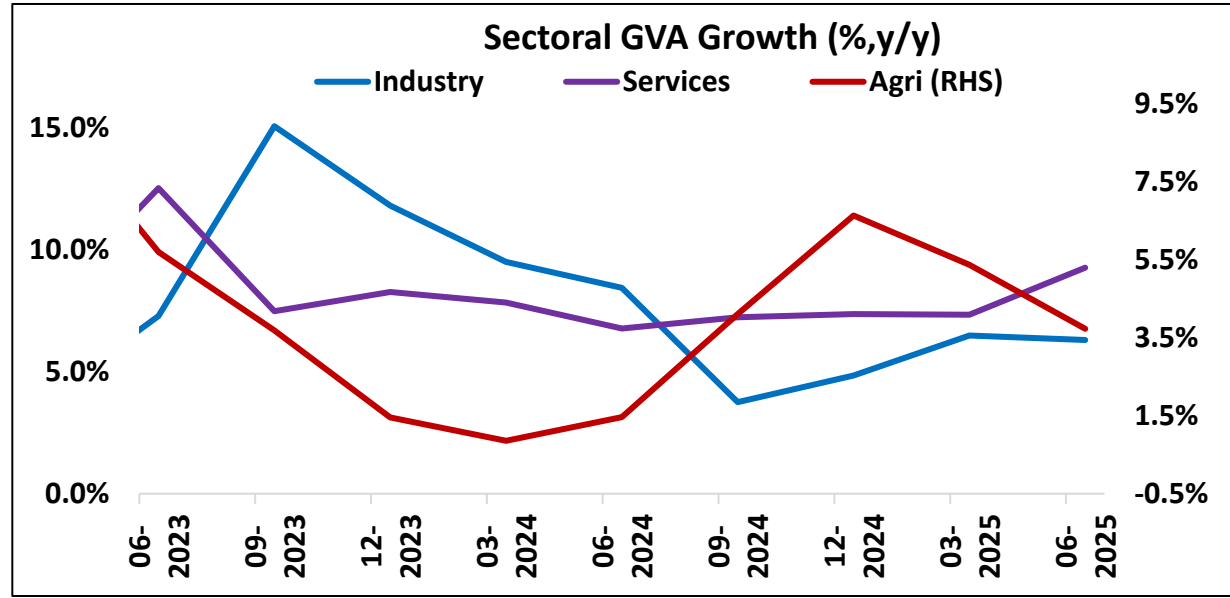
Q1 FY26 (UBI vs actuals)

	GVA	Agri	Industry	Mining	Manufacturing	Electricity	Construction	Services	Trade & Transport	Fin. Services & Real Estate	Public Admin	GDP
Actuals	7.6%	3.7%	6.3%	-3.1%	7.7%	0.5%	7.6%	9.3%	8.6%	9.5%	9.8%	7.8%
UBI Proj.	6.7%	6.0%	4.9%	-2.5%	4.1%	-2.0%	10.1%	7.8%	4.5%	8.8%	10.2%	7.0%

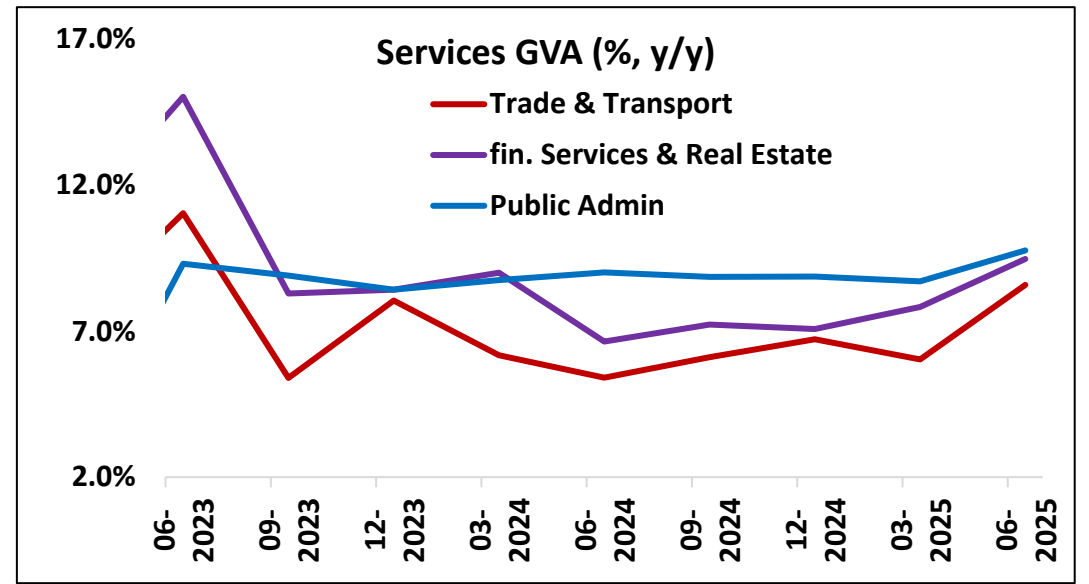


- While our economic activity indicators was signaling a slowdown, the growth numbers saw a pickup with GVA ex agri & govt. (a metric of private sector activity) rising to 8% levels
- The key +ve surprises was led by the spike in growth for manufacturing, trade & transport GVA and financial services & real estate sub-sectors
- However, lower than expected growth in agri (a disconnect from spike in trade as it signals rural demand strength) & construction (despite robust steel, cement prodn. nos) were a surprise too

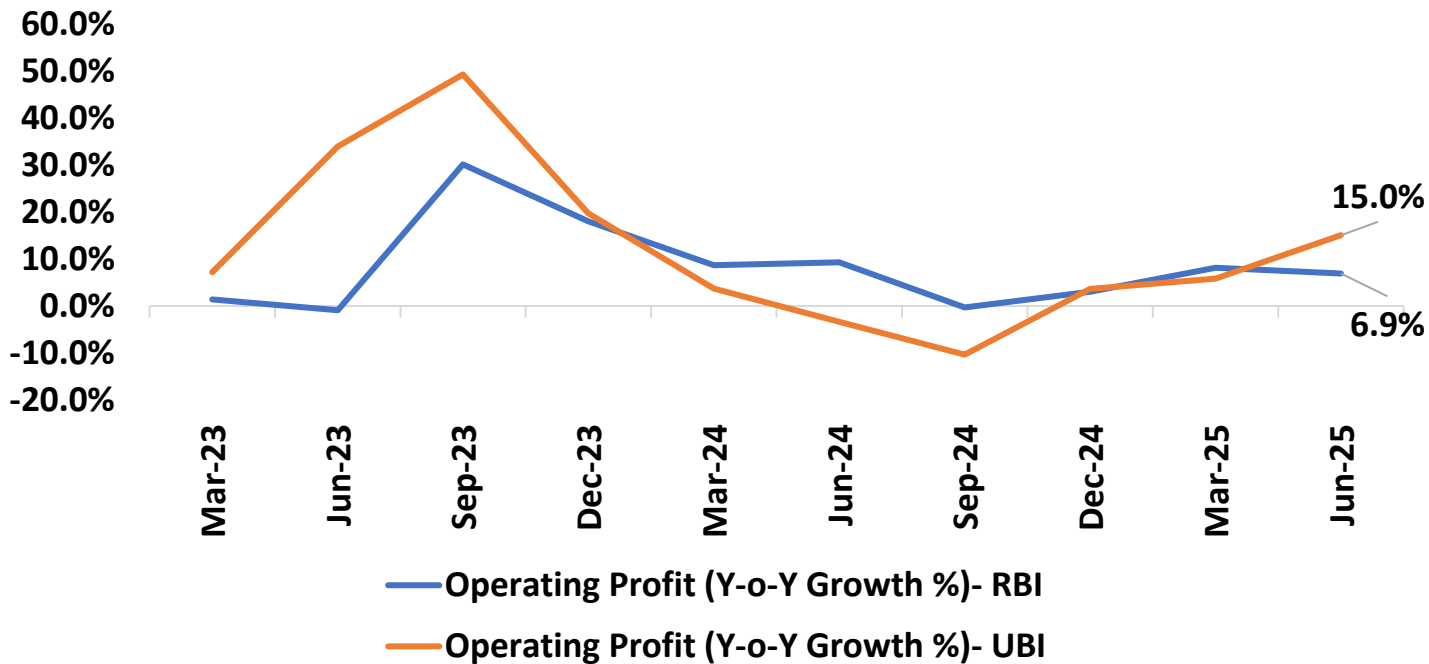
Real GVA growth nos saw a broad-based pickup across sectors except mining, electricity and agri



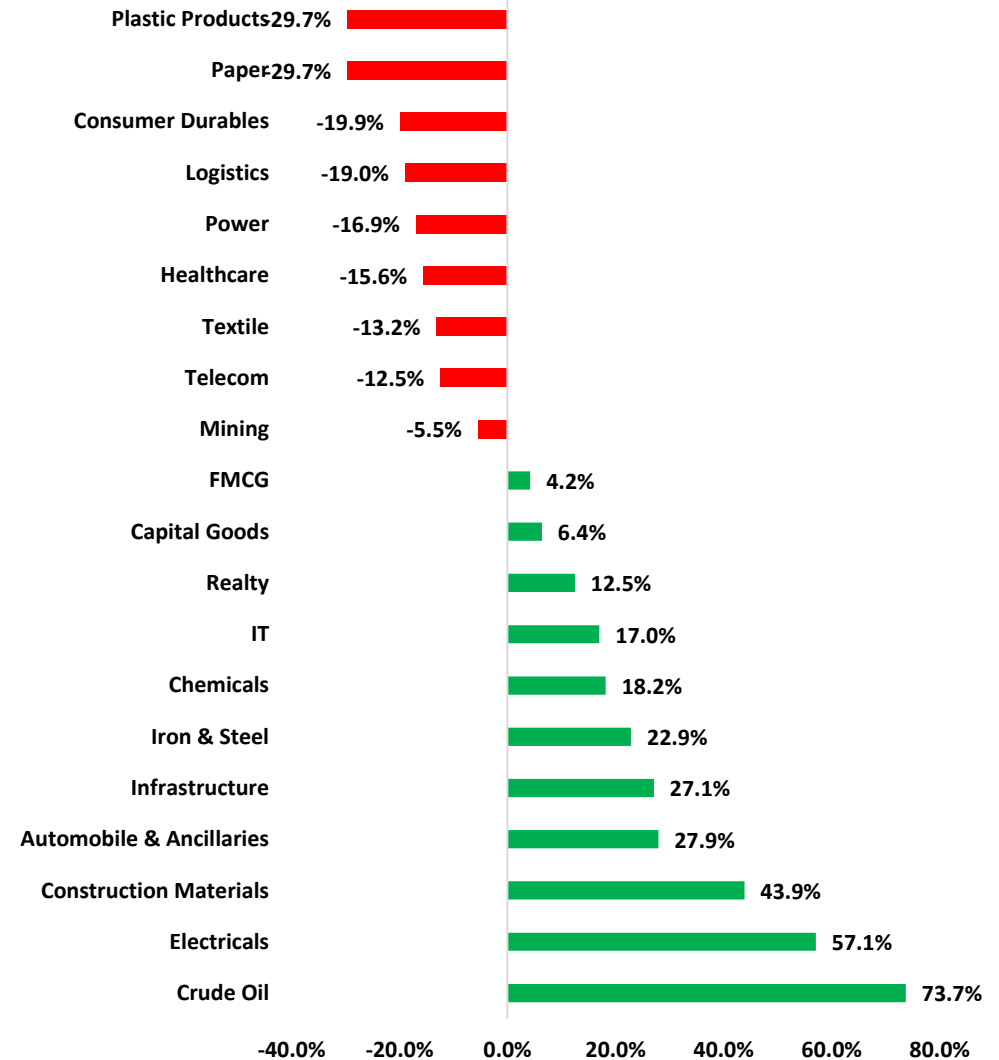
- The pickup in GVA growth was led by services while industry was flat and agri saw some easing
- Services saw a broad-based pickup across public admin (base effects), financial & real estate (led by latter as credit/deposit momentum has slowed) and trade & transport (a big surprise)
- Within industry, while mining and electricity contracted as expected on early onset of monsoon, manufacturing was a +ve data surprise while construction was lower than expected



Operating Profit Y-o-Y (%) for Manufacturing sector RBI vs UBI est.

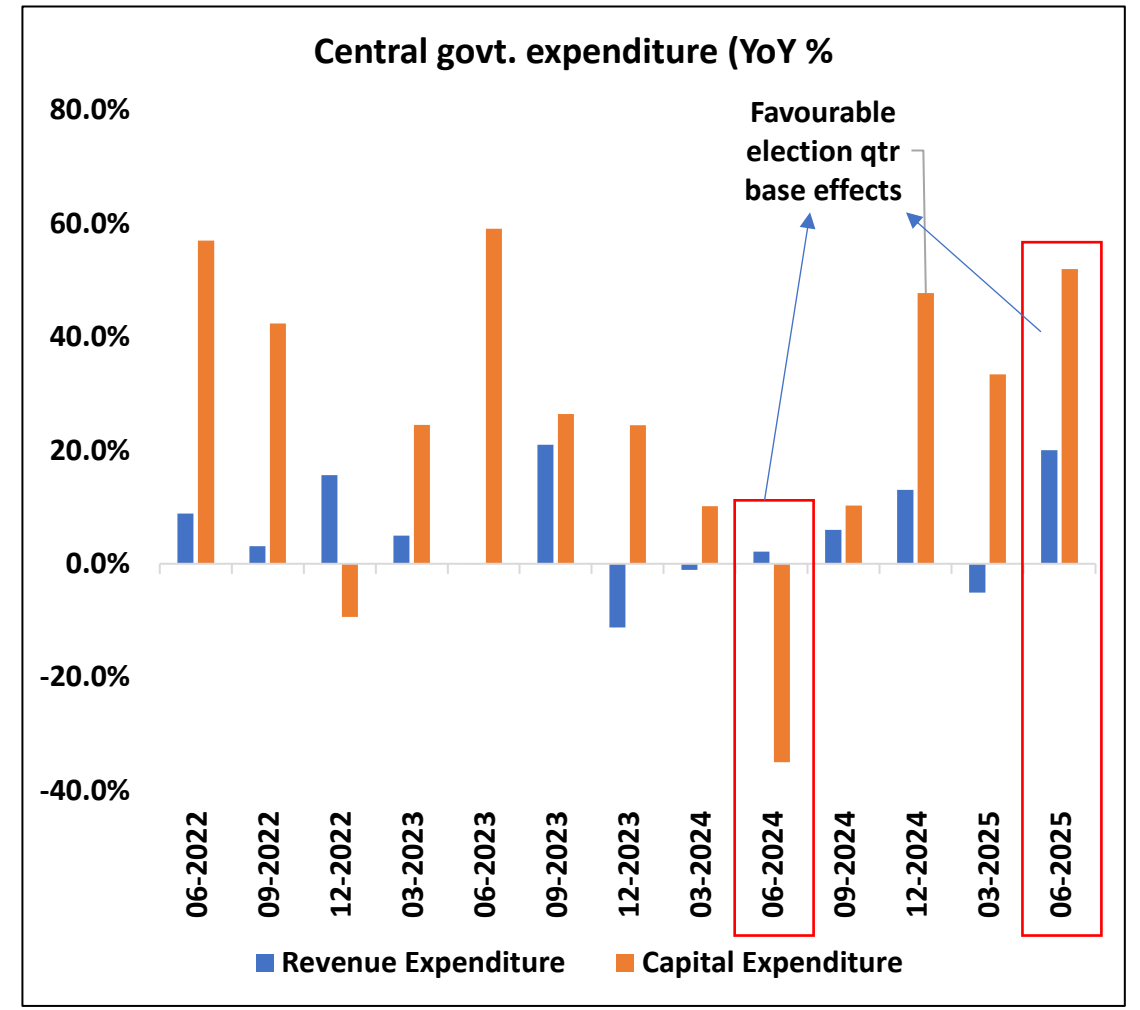
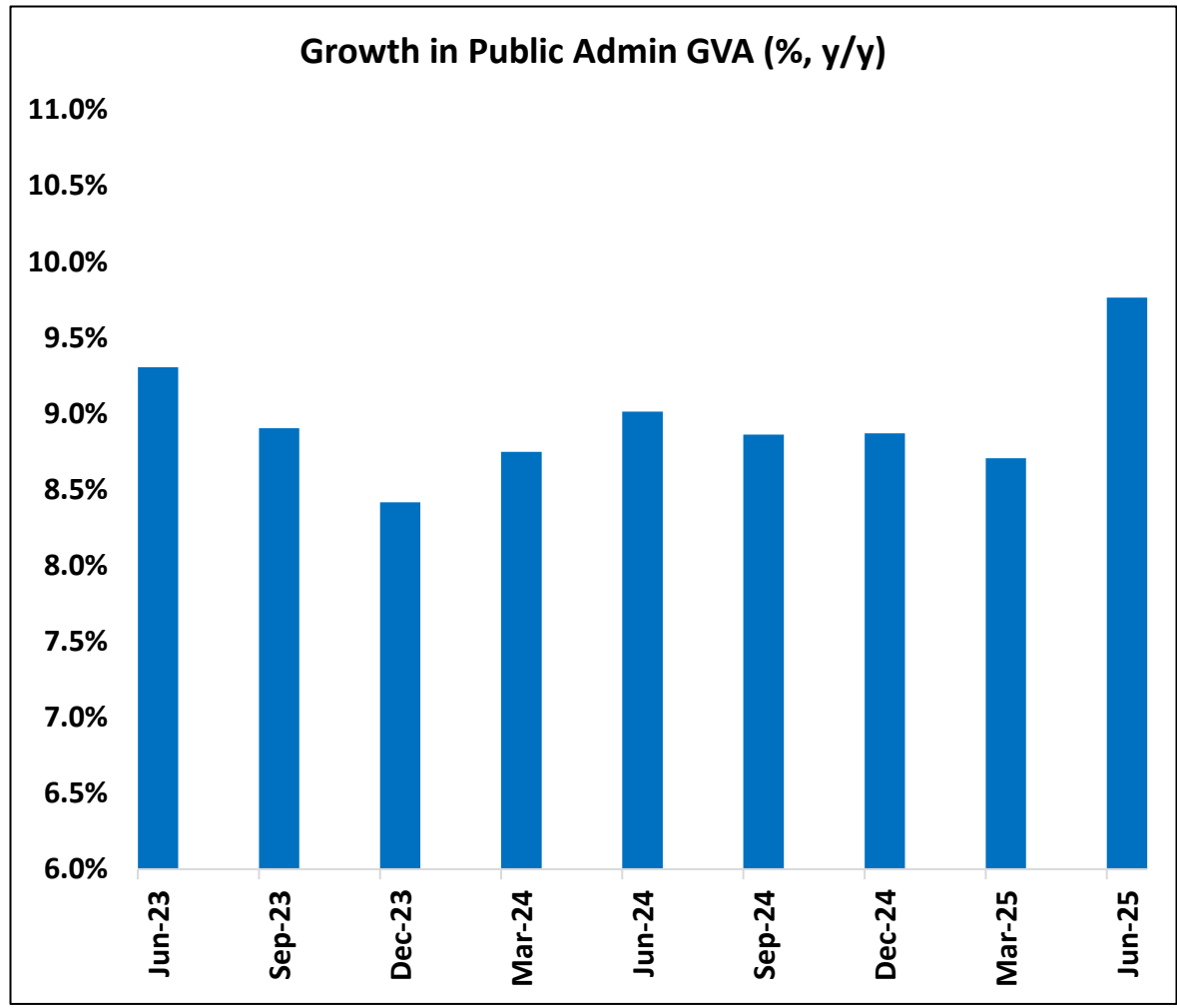


Winners & Laggards In terms of Operating Profit Y-o-Y (%) June '25



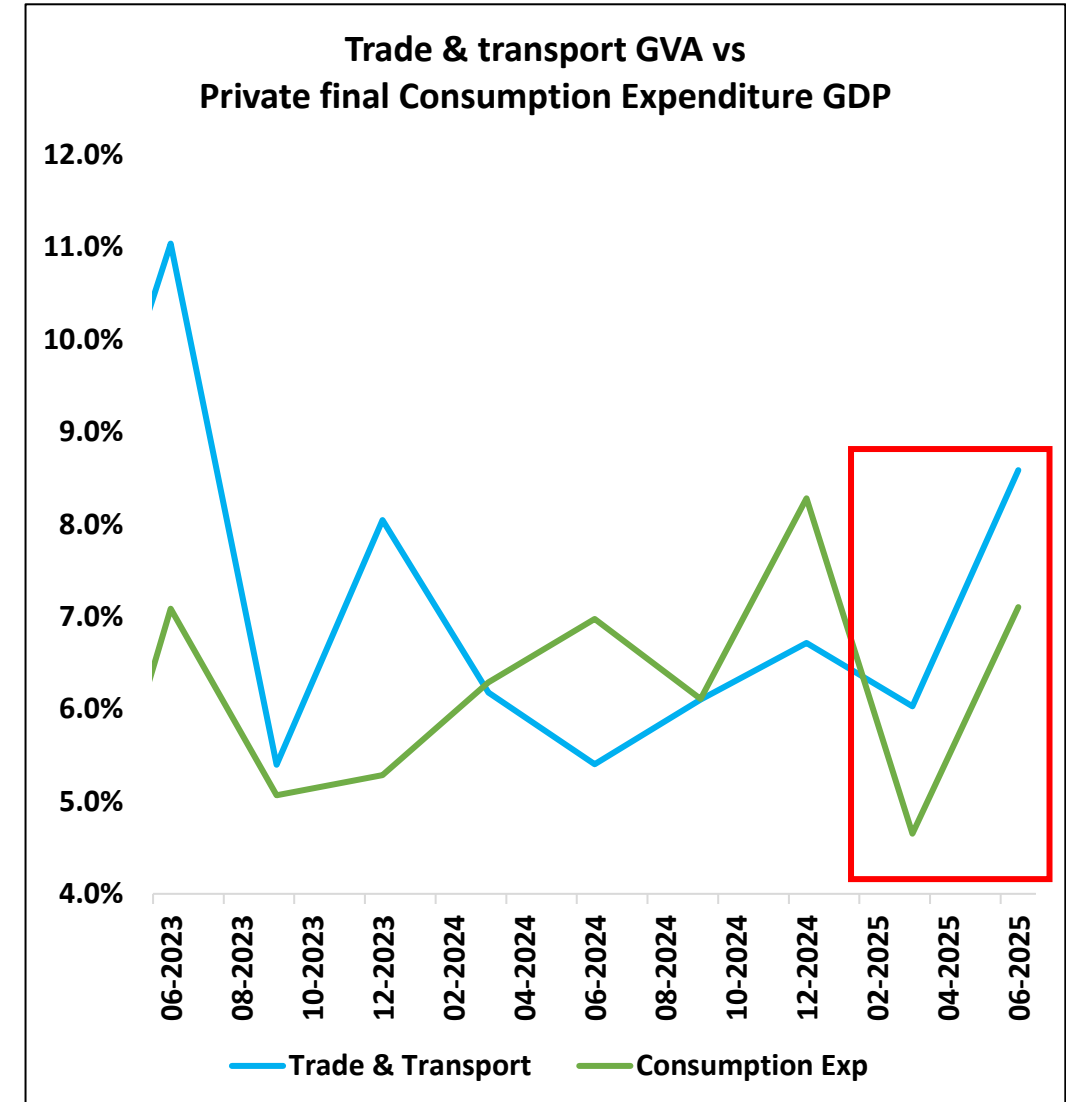
- The divergence seen in operating profit estimates by RBI and our (Union Bank of India) analysis for Q1-FY26. Manufacturing GVA data for Q1-FY26 was better aligned with our analysis
- This is probably attributed to difference in sample composition: RBI's analysis includes 1,736 non-financial private companies excluding government firms, while our study covers 1,760 companies encompassing both public and private sectors, leading to variations in results

As expected, public admin growth jumped led by election qtr base effects in government spending



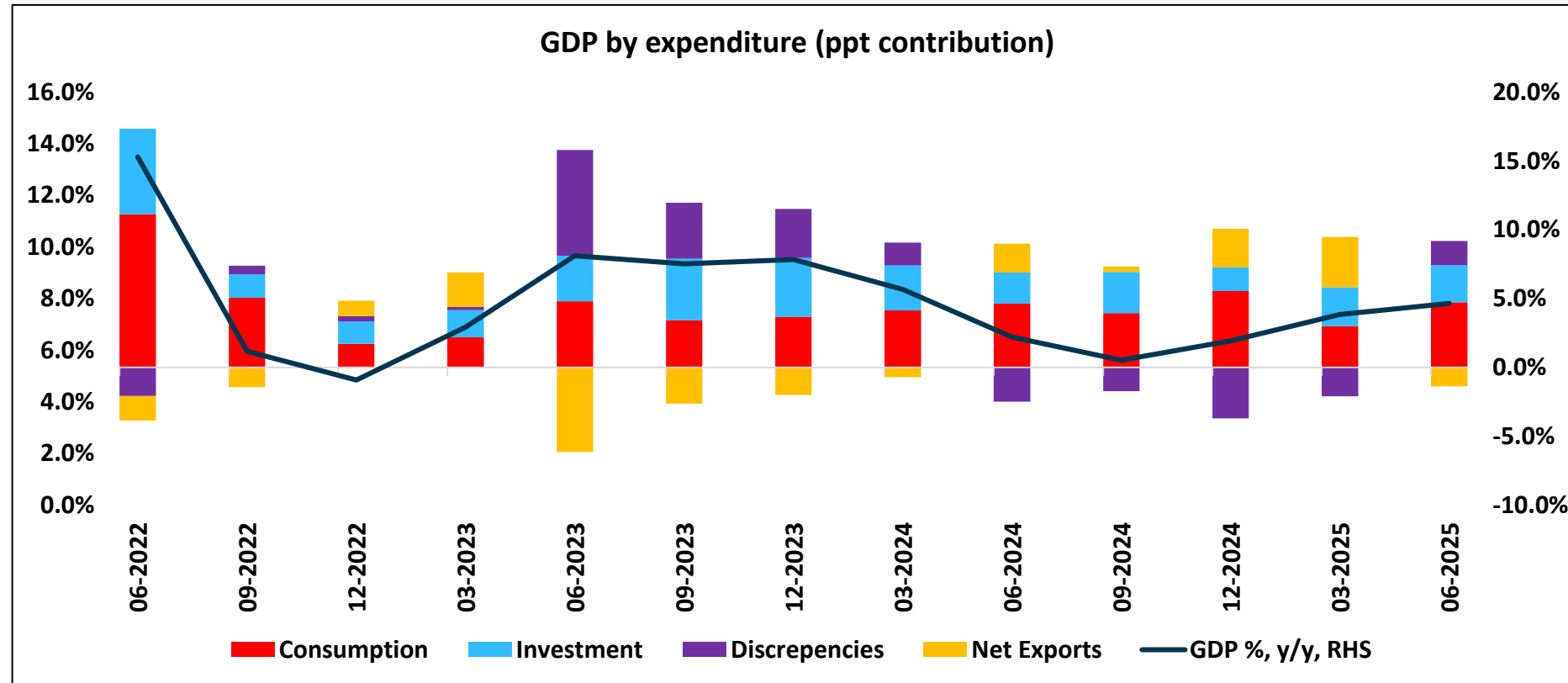
However, trade GVA surprised with a growth spike despite mixed performance of lead indicators

Sector (% y/y)	Indicator	Q1FY25	Q2FY25	Q3FY25	Q4FY25	Q1FY26
Urban Demand	Passenger Vehicle Sales	2.8%	-1.9%	5.0%	2.4%	-1.4%
Rural Demand	Two Wheeler Sales	20.7%	12.5%	1.4%	1.5%	-6.0%
	Three Wheeler Sales	13.8%	6.8%	1.2%	8.4%	0.4%
	Tractor Sales	0.2%	-0.2%	11.7%	24.2%	9.1%
Trade, Hotels, Transport, Communications	Commercial Vehicle Sales (Qtrly)	3.3%	-11.0%	1.2%	1.8%	-0.5%
	Railway Freight Traffic	5.2%	0.4%	1.5%	-0.6%	3.6%
	Port cargo Traffic	4.0%	6.2%	-1.7%	9.0%	5.7%
	domestic Air Cargo Traffic	7.0%	7.8%	4.5%	3.1%	9.4%
	International Air Cargo Traffic	18.3%	21.9%	15.0%	1.4%	7.7%
	Domestic Air Passenger Traffic	5.6%	7.2%	11.4%	12.0%	6.1%
	International Air Passenger Traffic	14.3%	10.3%	10.0%	8.5%	9.0%
	GST E-way Bills (Total)	15.9%	16.9%	16.9%	19.4%	20.5%
	Hotel Occupancy	-2.6%	1.6%	1.5%	-3.2%	3.2%
	Average Revenue per room	6.8%	5.5%	12.6%	11.7%	9.0%
	Tourist Arrivals	2.3%	-1.7%	-2.7%	-7.5%	
	Construction	Steel Consumption	15.3%	11.8%	7.9%	11.8%
Cement Production		0.4%	3.4%	8.9%	12.4%	8.4%
PMI Index*	Services	60.50	59.63	58.73	58.00	59.30



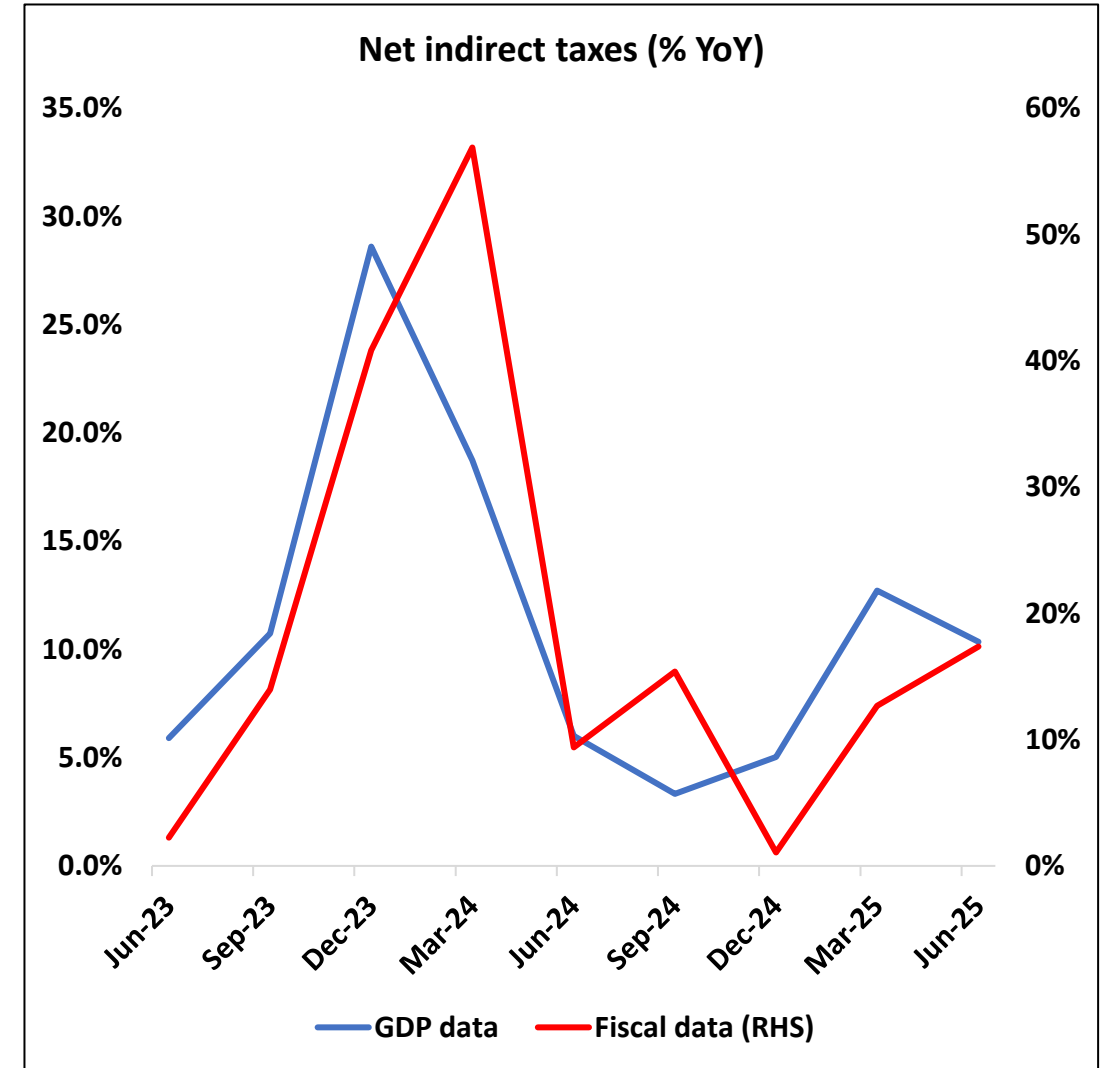
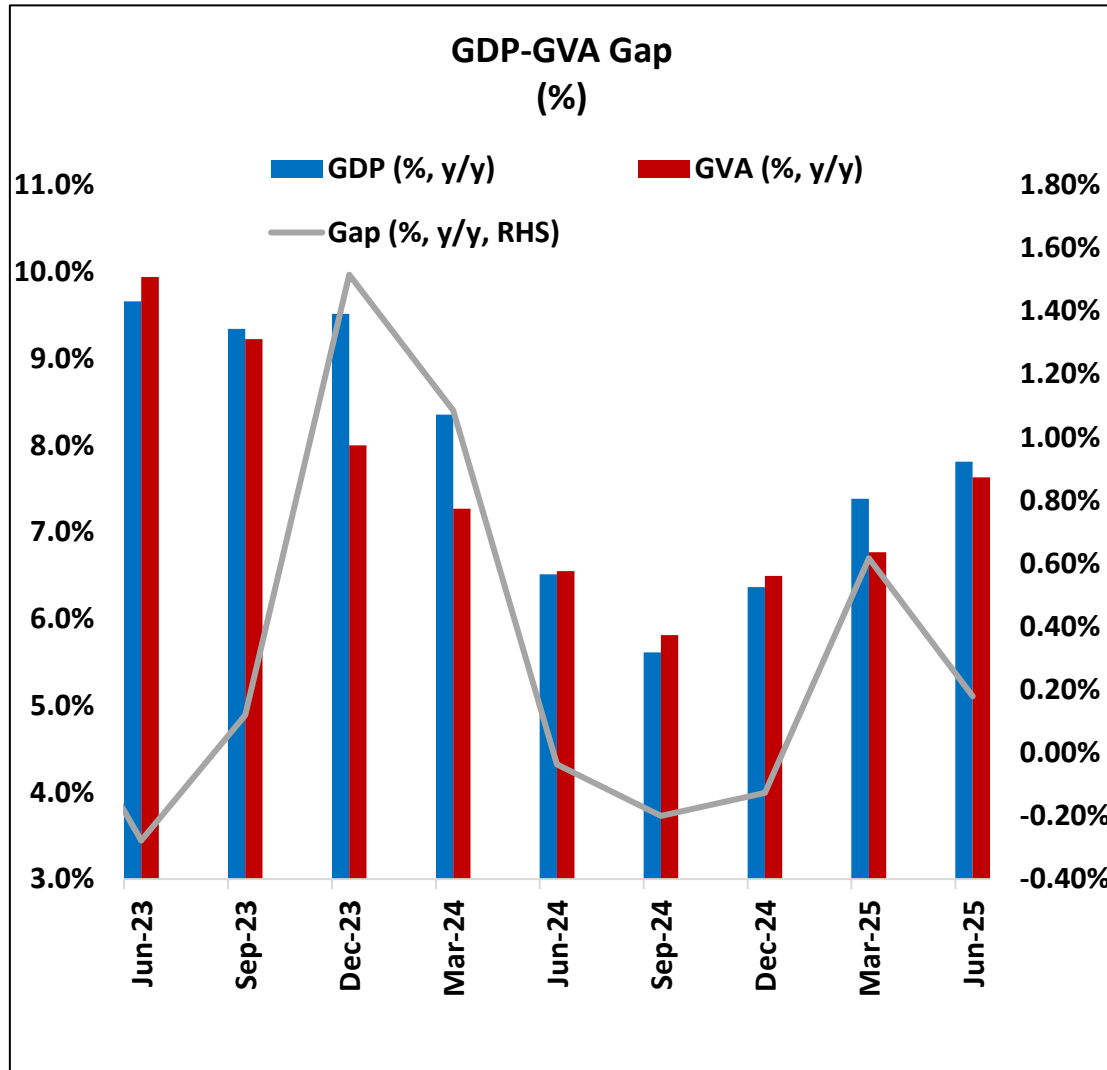
*levels, Source: RBI, CEIC, SIAM, HVS Anarock, UBI Research

Discrepancies played a significant role in explaining growth pickup in Q1-FY26 versus Q4-FY25



- An analysis in GDP contribution by sub-segments clearly showed a spike in contribution of discrepancies from (-)2.1 ppt in Q4-FY25 to +1.8ppt in Q1-FY26. This is a key issue with respect to the GDP data and signals high tendency for revisions
- Interestingly, while the frontloading of exports ahead of expiry of 90-day deadline on pause on reciprocal tariff was seen as a strong growth driver, it needs to be noted that the contribution of 'net exports' switched to negative zone in Q1-FY26
- While capex contribution to GDP growth was nearly flat, that for consumption spiked and has been a source of data surprise

GDP-GVA growth gap normalised back to ~20bps on slowdown in net indirect taxes growth



1. Sector specific package for exporters (immediate fiscal incentive esp. for labour intensive sectors):

- Exporters in the sectors at high risk viz. shrimps, textiles, gems & jewellery, chemicals etc would need direct government intervention as export orders are being cancelled and payments held up.

Lesson to learn from Brazil's stimulus plan:

- Liquidity:** R\$30bn export-credit lifeline to cushion firms hit by 50% U.S. tariffs.
- Cash-flow relief & risk cover:** Tax payment deferrals, R\$5bn SME tax credits through 2026, and expanded insurance for cancelled orders.
- Demand & cost support:** Public procurement to absorb diverted output and extended **drawback** (tax credits on imported inputs used for exports).
- **Govt. may consider reviving the Interest Equalisation Scheme**, which was discontinued last year. It may be relaunched with an annual budget of Rs 15,000 crore and a five-year commitment. This would provide subsidized credit to exporters, especially MSMEs, lowering borrowing costs and improving their immediate competitiveness.

2. Specific steps to provide immediate financial relief:

- For fresh credit support to affected sectors
- **Credit guarantee scheme for affected exporter MSMEs and allied entities for a certain proportion (say 20%) of the export working capital sanction limit** (*already in works as per media sources*)

- Schemes related to interest subvention and/ or credit restructuring etc for worst affected sectors from tariff hikes along with credit guarantees for loans overdue by up to 90 days to support small businesses and exporters hit by higher US tariffs.
- **For existing credit exposures:**
 - Extending NPA threshold from 90 to 180 Days to better align with working capital cycle
 - **MSMEs often face delays in receivables** especially from large buyers or government departments. To resolve the issue, IRAC norms can be modified by increasing the recognition period from 90 to 180 days. This provides MSMEs more time to resolve temporary financial stress and cash crunch.
 - Similarly, SMA-0, 1, 2 classification to be aligned with the working capital cycle of MSMEs like Textile sector facing presently.
- **Credit restructuring scheme for affected sectors**
 - **Framework for Revival and Rehabilitation of MSMEs:** To encourage Banks as well as MSMEs to adopt the FRR (Framework for Revival and Rehabilitation of MSMEs). The accounts restructured through FRR may be allowed to keep the same asset class instead of downgrading to Sub Standard.
 - **Specific credit restructuring provisions:** During down cycle of a sector like current tariff issue), specific restructuring scheme (without asset classification change like Agri loan during natural calamities) to be introduced.

Key Statistics Table

YoY growth %	FY25	Q1FY25	Q2FY25	Q3FY25	Q4FY25	Q1FY26
GDP	6.5%	6.5%	5.6%	6.4%	7.4%	7.8%
GVA	6.4%	6.5%	5.8%	6.5%	6.8%	7.6%
Agri	4.4%	1.5%	4.1%	6.6%	5.4%	3.7%
Industry	5.9%	8.5%	3.8%	4.8%	6.5%	6.3%
<i>o/w Manufacturing</i>	4.6%	7.6%	2.2%	3.6%	4.8%	7.7%
<i>Construction</i>	9.3%	10.1%	8.4%	7.9%	10.8%	7.6%
Services	7.2%	6.8%	7.2%	7.4%	7.3%	9.3%
<i>o/w Trade & transport</i>	6.1%	5.4%	6.1%	6.7%	6.0%	8.6%
<i>Financing & Real estate</i>	7.2%	6.6%	7.2%	7.1%	7.8%	9.5%
<i>Public admin</i>	8.9%	9.0%	8.9%	8.9%	8.7%	9.8%
Pvt final consumption expenditure GDP	7.2%	8.3%	6.4%	8.1%	6.0%	7.0%
Gross fixed capital formation GDP	7.0%	6.7%	6.7%	5.2%	9.4%	7.8%
Nominal GDP	9.5%	9.5%	8.3%	10.7%	9.6%	8.8%
Real GVA ex agri ex govt.	6.4%	7.1%	5.6%	6.0%	6.7%	8.0%

High frequency lead indicators showed a mixed picture

Industrial Sector	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25	May-25	Jun-25	Jul-25
IIP (YoY Gr%)	4.9	5.0	0.0	3.2	3.7	5.0	3.7	5.2	2.7	3.9	2.6	1.9	1.5	3.5
Mining (YoY Gr%)	10.3	3.8	-4.3	0.2	0.9	1.9	2.7	4.4	1.6	1.2	-0.2	-0.1	-8.7	-7.2
Manufacturing (YoY Gr%)	3.5	4.7	1.2	4.0	4.4	5.5	3.7	5.8	2.8	4.0	3.1	3.2	3.7	5.4
Electricity (YoY Gr%)	8.6	7.9	-3.7	0.5	2.0	4.4	6.2	2.4	3.6	7.5	1.7	-4.7	-1.2	0.6
Core Infra Growth (YoY Gr%)	5.0	6.3	-1.5	2.4	3.8	5.8	5.1	5.1	3.4	4.5	1.0	1.2	2.2	2.0
Capital Goods Production (YoY Gr%)	3.6	11.7	0.0	3.5	2.9	8.9	10.5	10.2	8.2	3.6	14.0	13.3	3.0	5.0
PMI Manufacturing	58.3	58.1	57.5	56.5	57.5	56.5	56.4	57.7	56.3	58.1	58.2	57.6	58.4	59.1
PMI Services	60.5	60.3	60.9	57.7	58.5	58.4	59.3	56.5	59.0	58.5	58.7	58.8	60.4	60.5
Banking Sector	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25	May-25	Jun-25	Jul-25
Bank Credit (YoY Gr%)	17.3	13.6	13.6	13.0	11.5	10.6	11.2	11.4	11.0	11.0	10.3	9.0	9.5	10.0
Agriculture Credit (YoY Gr%)	17.4	18.1	17.7	16.4	15.5	15.3	12.5	12.2	11.4	10.4	9.2	7.5	6.8	7.3
Industry Credit (YoY Gr%)	8.1	10.2	9.7	8.9	7.9	8.0	7.2	8.0	7.1	7.8	6.6	4.8	5.5	6.0
Services Credit (YoY Gr%)	17.4	14.5	13.9	13.7	12.7	13.0	11.7	12.5	12.0	12.4	10.5	8.7	9.0	10.6
Retail Credit (YoY Gr%)	25.6	14.0	13.9	13.4	12.9	13.3	12.0	11.8	11.7	11.6	11.9	11.1	12.1	11.9
Bank Deposits (YoY Gr%)	11.1	10.6	12.7	10.4	11.5	11.2	9.8	12.1	12.0	10.3	9.8	9.9	10.1	10.2
Inflation	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25	May-25	Jun-25	Jul-25
CPI (YoY Gr%)	5.1	3.6	3.7	5.5	6.2	5.5	5.2	4.3	3.6	3.3	3.2	2.8	2.1	1.6
Core CPI (YoY Gr%)	3.1	3.4	3.4	3.5	3.7	3.6	3.6	3.7	4.0	4.1	4.1	4.2	4.4	4.1
WPI (YoY Gr%)	3.4	2.1	1.2	1.9	2.8	2.2	2.6	2.5	2.4	2.2	0.9	0.1	-0.1	-0.6
Consumer	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25	May-25	Jun-25	Jul-25
Electricity Consumption (YoY Gr%)	8.0	4.0	-5.0	-0.8	-0.4	3.7	5.1	1.3	2.4	5.7	2.8	-4.8	-2.3	2.6
Petroleum Consumption (YoY Gr%)	9.0	7.4	0.3	-10.6	8.4	2.0	4.0	1.4	-11.3	3.7	-4.1	6.4	-0.1	6.4
Consumer Durables (YoY Gr%)	8.8	8.2	5.4	6.3	5.5	14.1	8.1	7.1	3.7	6.9	6.2	-0.9	2.8	7.7
Consumer Non Durables (YoY Gr%)	-1.0	-4.2	-4.4	2.2	2.8	0.6	-7.1	0.1	-2.1	-4.0	-2.7	-1.0	-0.9	0.5
Trade	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25	May-25	Jun-25	Jul-25
Merchandise Export (YoY Gr%)	2.4	0.6	-9.9	-0.3	16.6	-5.3	-1.5	-2.6	-11.1	0.7	8.6	-2.8	-0.1	7.3
Merchandise Import (YoY Gr%)	4.6	11.2	10.0	7.8	1.9	16.1	2.3	10.3	-16.3	11.4	19.1	-1.7	-3.7	8.6
Service Export (YoY Gr%)	3.2	16.6	5.7	14.6	22.7	14.2	16.9	12.1	11.7	18.7	8.8	9.6	12.0	10.3
Service Import (YoY Gr%)	-3.1	16.0	9.1	13.5	28.0	26.1	13.9	12.6	-4.7	5.3	1.0	-1.0	5.1	8.5
Fiscal	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25	May-25	Jun-25	Jul-25
GST Collection (YoY Gr%)	7.6	10.3	10.0	6.5	8.9	8.5	7.3	12.3	9.1	9.9	12.6	16.4	6.2	7.5
Govt. Expenditure (YoY Gr%)	-18.4	0.1	20.9	2.6	31.7	3.6	22.1	12.4	-17.7	9.7	10.0	40.3	37.4	3.3

Thank You !

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