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Stability Achieved, Reforms a Must: Why Budget 2026 Must Convert Macroeconomic Strength into Structural Growth



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Article Content:

India enters the run-up to Budget 2026–27 from a position of macroeconomic strength that would have been difficult to imagine just a few years ago. Growth has remained resilient, inflation has moderated, public finances are credible, and the financial system is stable.¹ What makes the current moment distinctive, however, is that this stability has now persisted across two consecutive fiscal years—FY 2024–25 and FY 2025–26—with translating into a higher growth trajectory. The economy is stable, resilient, and growing close to its medium-term potential. Yet, that very clarity exposes a deeper concern: the growth model has not decisively shifted gears.

This allows a sharper diagnosis. The constraint on India's growth is no longer macroeconomic. It is structural.

The Economic Survey 2024–25 framed this challenge clearly: sustaining and accelerating growth beyond the 6–7 per cent range would depend on private investment, productivity gains, and deregulation, not fiscal stimulus.² With most FY 2025–26 data now available in realised or provisional form, it is possible to test that diagnosis against outcomes—and to draw clear lessons for Budget 2026.

Macroeconomic Stability: No Longer Episodic, Now Embedded

The strongest message from FY25 and FY26 is the durability of macroeconomic stability. In FY 2024–25, real GDP growth came in at 6.4 per cent, close to India’s decadal average.³ In FY 2025–26, quarterly outcomes so far and official projections point to a similar trajectory. The Reserve Bank of India has consistently retained a full-year FY26 growth projection of around 6.5 per cent across successive monetary policy reviews.⁴ This consistency is itself revealing: downside risks have been managed, but upside momentum has not materialised.

Inflation trends reinforce this picture. After easing through FY25, headline CPI inflation in FY26 has remained within the tolerance band, with food inflation lower than historical peaks despite periodic volatility.⁵ This moderation has occurred alongside stable growth, suggesting that India has exited the post-pandemic inflation-growth trade-off phase.

External sector performance has reinforced resilience. The current account deficit has stayed close to 1–1.3 per cent of GDP, financed comfortably by a robust services trade surplus and steady remittances.⁶ In FY26 so far, services exports—particularly IT and business services—have continued to offset weakness in merchandise exports, cushioning the economy from global manufacturing slowdowns.

The impact of rising tariffs and trade restrictions on India’s exports has been managed through adaptation. Faced with trade fragmentation, exporters have increasingly diversified destination markets, reducing excessive dependence on a few geographies and expanding presence in emerging regions across Asia, Africa, Latin America, and the Middle East. On the policy side, the government has complemented this adjustment through a calibrated strategy—pursuing trade agreements to secure preferential access, extending production-linked incentives to strengthen cost competitiveness, and investing in logistics and trade facilitation.

Fiscal outcomes complete the stability narrative. Provisional FY26 data show Union government capital expenditure remaining elevated, while deficit indicators are tracking budgeted paths despite higher tax devolution to states.⁷ Tax buoyancy has held up, even as higher devolution to states has limited growth in net Union revenues. Markets have responded accordingly: sovereign yields have remained broadly stable, reflecting confidence in fiscal discipline.

Financial sector indicators underline how far the system has come. Gross non-performing assets are at multi-year lows, capital adequacy ratios are well above regulatory norms, and credit growth in FY26 continues without signs of systemic stress.⁸ Two years of growth without financial fragility is not an accident; it reflects institutional strengthening.

Growth Drivers: Momentum Without Acceleration

If stability is the success story, growth drivers tell a more nuanced tale.

Consumption is Resilient, but Narrowly Based

Private consumption has been the primary stabiliser across both years. In FY25, Private Final Consumption Expenditure grew by over 7 per cent, pushing its share of GDP to nearly 62 per cent, the highest in over two decades.⁹ In FY26 so far, consumption has remained supportive, aided by rural demand, easing food inflation, and continued welfare support.

However, the composition of consumption reveals limits. Rural demand has been the main driver, backed by strong agricultural output and MSP operations, while urban discretionary demand has been uneven. Urban FMCG growth has been modest Passenger vehicle sales growth moderated in FY25 and has remained subdued in FY26, indicating restrained urban sentiment.¹⁰ This suggests that consumption resilience is being sustained more by policy cushioning than by broad-based income acceleration.

Investment remains the critical missing link

Gross Fixed Capital Formation growth slowed to about 6.4 per cent in FY25, and early FY26 data suggest no decisive re-acceleration.¹¹ RBI surveys show capacity utilisation hovering around 74–75 per cent through FY26, only marginally above long-term averages and below levels that typically trigger a strong private capex cycle.¹²

This is not for lack of intent. Order books in capital goods sectors expanded sharply in FY24 and remained healthy in FY25. Yet execution has lagged, reflecting regulatory friction, demand uncertainty, and risk aversion. FY26 outcomes confirm that translation from intent to execution remains a work in process.¹³

Public capital expenditure has done much of the heavy lifting—and continues to do so in FY26. But two years of elevated public capex without a decisive private response indicate that the crowding-in mechanism has limits unless structural constraints are addressed.

Employment: Improving Participation, Uneven Quality

Labour market indicators have improved across FY25 and FY26, including higher labour force participation and a rise in female participation. This is a positive structural shift, but employment growth remains concentrated in construction and services. Manufacturing employment has lagged, constrained by weak export demand and cost pressures.¹⁴

FY26 data so far does not suggest a change in this pattern. Without stronger manufacturing and tradable-sector growth, employment elasticity will remain limited, even if headline growth stays respectable.

The Structural Gap is now Evidence, Not Inference

What distinguishes the current moment from earlier post-pandemic phases is that the reform gap is now visible in data, not inferred from projections.

Despite two years of macro stability:

- capacity utilisation remains at near 75 per cent,
- private capex execution has not accelerated materially,
- merchandise exports remain weak, and
- food inflation moderation owes more to favourable supply conditions than to structural fixes.¹⁵

Food inflation illustrates the challenge. FY25 and FY26 benefited from good agricultural output, but fragmented supply chains, limited cold storage, and uneven market integration remain unresolved. As climate variability increases, reliance on favourable monsoons becomes increasingly risky.¹⁶

Export competitiveness tells a similar story. The emphasis to combat the tariff issue has been

on preserving export resilience through market diversification, supply-side competitiveness, and incremental institutional support. External balances remain stable largely because of services exports and remittances. Merchandise exports have struggled across FY25 and FY26 amid global tariffs and domestic cost pressures. Without logistics reform and trade facilitation, this imbalance will persist.¹⁷

While the current approach has cushioned the immediate impact of global trade disruptions, FY25 and FY26 outcomes suggest that sustaining export growth in a tariff-heavy world will ultimately depend on deeper domestic reforms that reduce logistics costs, improve regulatory predictability, and raise productivity across manufacturing and tradable services.

The Economic Survey 2024–25 was explicit that deregulation, compliance reduction, and trust-based governance were essential to lift medium-term growth. FY 2025–26 did make incremental progress on these fronts, and FY26 outcomes to date suggest that incrementalism is not enough.

What FY26 Confirms—and What Budget 2026-27 Must Do

With FY26 data now in hand, three conclusions stand out:

- First, India's current policy mix reliably delivers around 6.5 per cent growth with stability. This is an achievement—but it is also a plateau.
- Second, macro tools have largely run their course. Fiscal prudence, monetary credibility, and financial stability are necessary conditions, but they are no longer sufficient to raise growth.
- Third, the binding constraint is structural.¹⁸ Deregulation, productivity enhancement, and private investment de-risking are now the decisive levers.

Budget 2026 must therefore shift from preservation to conversion—converting stability into scale. This requires:

- Moving decisively on compliance reduction and regulatory simplification, especially for MSMEs and investors. India's regulatory approach must decisively move from "Guilty until proven innocent" to self-certifications and "Innocent until proven guilty".
- Creating credible mechanisms to de-risk private capex, particularly in manufacturing, and in infrastructure with PPP mechanisms based on real-world risk-sharing frameworks
- Addressing structural food inflation through logistics, storage, and market integration
- Renewed push on export competitiveness through trade facilitation and cost reduction¹⁹

Conclusion: The Moment of Choice

India enters Budget 2026–27 stronger than it has been in years. Growth is steady, inflation is manageable, the external account is stable, and public finances are credible. FY25 proved this was possible. FY26 confirmed it is repeatable.

But repetition is not transformation. The 2024–25 Economic Survey's warning remains salient: without decisive structural reform, stability alone will not lift India's growth trajectory.

The data now leaves little room for ambiguity: without structural reform, 6.5 per cent risks becoming the new normal. With reform, it can become the floor.²⁰ The choice is not between prudence and reform. The challenge is to use prudence as the platform for reform.

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