

India's Q2 GDP growth seen above RBI's 7% forecast, but data may contain some noise

Low inflation and tax cuts likely spurred consumption growth in July-September amid strong corporate profitability and capital expenditure by the government.

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The GDP is calculated by adding net indirect taxes — indirect taxes such as Goods and Services Tax (GST) minus subsidies — to GVA. (representational image)

The Indian economy is likely to have performed beyond expectations in the second quarter of FY26, according to economists speaking ahead of the November 28 release of official data by the Statistics Ministry. The upcoming release is likely to show the economy performing better than the Reserve Bank of India's forecast of 7 per cent growth, they said.

While possibly lower than the five-quarter high growth rate of 7.8 per cent in the April-June quarter, another 7 per cent-plus expansion in the July-September quarter — despite the 50 per cent US tariffs that came into effect in late August — would burnish India's growth story.

“Growth is tracking better than expected with Q2FY26 GDP growth at 7.3 per cent and Q3FY26 GDP getting support from GST cuts. Even before the GST cuts, rural recovery has become more broad-based in Q2, supported by stronger labour market conditions and good crop output. Urban demand has clearly responded to the GST cut with rise in consumer durable consumption expenditure,” Gaura Sen Gupta, IDFC First Bank's Chief Economist, said in a note on Monday.

Nominal growth slowdown

First, the caveats. The GDP data for April-June contained some noise that made reading the headline numbers difficult. For one, low inflation meant nominal growth — or growth without adjusting for price changes — was at a three-quarter low of 8.8 per cent even though the real growth number of 7.8 per cent painted a positive picture of the economy.

The nominal GDP growth rate needs to be monitored for two reasons. Firstly, it is not only tracking below the Finance Ministry's Budget assumption of 10.1 per cent, but economists are predicting it could be lower than 8 per cent growth — in both the July-September quarter and FY26 — that is required to meet the Budget estimate as per the latest GDP estimate for FY25. A lower than anticipated nominal GDP affects the Budget math, with tax collections not growing as hoped and fiscal deficit and debt-to-GDP ratios being higher than estimated.

GDP growth below GVA

Secondly, a slowdown in tax collections will also likely result in GDP growth being lower than the growth in overall Gross Value Added, or GVA. In April-June, GVA growth was 7.6 per cent, 20 basis points lower than the GDP growth rate.

The GDP is calculated by adding net indirect taxes — indirect taxes such as Goods and Services Tax (GST) minus subsidies — to GVA. So, if net indirect taxes fall or their growth slows down, GDP growth would be lower than the rise in GVA. Back-of-the-envelope calculations show the government's net indirect taxes fell on a year-on-year basis in Q2 compared to a 10 per cent rise in Q1. According to State Bank of India Research, GDP growth in the second quarter may be 7.5-8 per cent, while GVA growth is seen at 8 per cent.

The consumption quarter?

The reduced GST rates may have only come into effect towards the end of Q2 on September 22, but the surge in demand in the final few days of that month — in conjunction with other factors such as low inflation — may have lifted private consumption by 8 per cent, according to Paras Jasrai, Economist and India Ratings & Research. This would be the highest since the 8.1 per cent increase in Q3FY25.

In addition to retail inflation averaging a mere 1.7 per cent in Q2FY26 and rural agricultural wages growing by almost 6 per cent, Jasrai sees a potential boost in demand from the impact of the personal income tax cuts announced in the [Union Budget](#) for FY26 and a healthy 7.8 per cent rise in employee costs of over 500 listed companies. Private demand would have risen more than 8 per cent if not for households delaying purchases ahead of the GST cuts' rollout.

In Q1FY26, private consumption growth had risen to 7 per cent from 6 per cent in Q4FY25, although it was lower than 8.3 per cent in Q1 that fiscal.

Corporate over-performance

If households had a good three months in terms of their budgeting, so did companies, with Q2FY26 proving to be the best quarter in two years: HSBC analysts found that although sales of listed Indian companies were only 6 per cent higher year-on-year, their profits were up 13 per cent.

Here, inflation again played a big role. Even though retail prices rose 1.7 per cent year-on-year in Q2, wholesale inflation — which is indicative of the increase in inputs costs for producers — averaged zero over the same period.

“Q2 has witnessed quite a satisfactory financial performance from companies,” noted Bank of Baroda economists last week. “The tariff impact has been seen to a limited extent... It does look like that with continued subdued inflation profit growth will improve. This will help to also get reflected in higher value-added growth which will support GDP growth in the range of 7 per cent for FY26,” they added.

The RBI has forecast a GDP growth rate of 6.8 per cent for the full year.

Government capex continues

Despite the personal income tax and GST rate cuts, the private investment picture is not clear, with global trade uncertainty biting hard. But capital expenditure by the Central government remains robust. In Q2, the Centre's capex was up 31 per cent year-on-year at Rs 3.06 lakh crore.

However, data from investment monitoring firm Projects Today is suggestive of private firms showing greater interest in expanding capacities: 71 per cent of fresh investments in the first half of FY26 were by the private sector, up from 61 per cent in the year-ago period.

In Q1FY26, growth in gross fixed capital formation — a proxy for investments — had cooled to 7.8 per cent from 9.4 per cent in the previous quarter, although it was higher than 6.7 per cent in Q1FY25.

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