

Despite Brent retracing ~25% from its peak on hopes of a US-Iran deal, underlying oil market conditions remain tight. The key variable is inventory depletion; global inventories could approach critical levels by late-Jun/early-Jul-26, risking renewed price spikes unless SoH flows normalize. Even then, geopolitical risks, logistics frictions, and inventory rebuilding may keep prices elevated. Temporary buffers—including SPR releases, OECD/China inventory draws, refinery run cuts, and demand substitution—have so far contained prices. We raise our FY27E average Brent assumption to USD90/bbl (from USD80/bbl), before easing to USD75/bbl by Q4FY27E. Combined with El Niño risks, we trim FY27E GDP growth to 6.3% and maintain inflation at 5.1%. We view a broadly equal sharing of the oil shock across OMCs, government, and consumers as the least growth-damaging outcome, with net fiscal cost tracking ~0.2–0.3% of GDP. The bigger vulnerability lies in the external sector. We now expect CAD/GDP to widen to 2.3%, while FY27E BoP deficit could exceed USD75bn, absent credible measures to attract foreign capital. Policy trade-offs will increasingly revolve around inflation, growth, FX stability, and capital flows, with RBI likely using rates to anchor inflation rather than defend INR.

Oil realities are muddier; expect price stickiness amid physical imbalances

Hopes of a potential US-Iran agreement have pulled Brent prices back by ~25% from the crisis peak of USD125/bbl. However, we maintain that Iran has limited incentive to fully reopen SoH, absent a broader geopolitical settlement. Accordingly, our focus has shifted from headline-driven expectations around reopening toward the underlying physical balance of the oil market. In our view, it is ultimately the pace of inventory depletion that will determine when the market is forced into resolution. Our assessment suggests that by late-Jun/early-Jul-26, global inventories could fall toward critical threshold levels, materially tightening available energy buffers. Unless SoH throughput returns to pre-conflict levels, oil prices could reprice sharply higher. While similar concerns have surfaced throughout this conflict, there are buffers which have kept oil prices relatively contained, including i) US draining its SPR, and inventory draws more generally by OECD/China; ii) refinery run cuts; iii) the role of China in adding supply; and iv) substitution/demand reduction. Our core assumption is that accelerating inventory depletion will eventually force a normalization of SoH flows by end-Jun/early-Jul-26—gradually adjusting fundamental balances. Even then, price normalization may lag, as geopolitical risks, logistics friction, and the need to rebuild inventories keep premiums elevated, notwithstanding incremental supply from Iran and a lagged shale response.

FY27E growth trimmed to 6.3%; BoP risks outweigh stagflation concerns

We raise our FY27E Brent assumption to USD90/bbl (from USD80/bbl earlier), reflecting tighter markets in Q2 before easing to USD75/bbl by Q4. Combined with El Niño-related monsoon risks, we trim our FY27 GDP growth forecast by 30bps to 6.3%, though GVA growth should remain higher at 6.5% amid lower net indirect taxes. We forecast FY27 inflation at 5.1%, incorporating moderate El Niño, a Rs10/ltr fuel price hike in Q1FY27 (partly reversed by Q4 as oil falls sub-USD80/bbl), and second-round energy spillovers. Ultimately, the macro impact will depend on how the crude shock is shared between OMCs, government, and end-consumers. In a sustained high-oil-price scenario, we believe the least growth-damaging outcome would be a (near) equal pass-through among all economic agents. We think OMCs will be allowed to rebuild margins as oil prices correct later, while net fiscal hit is likely to be ~0.2–0.3% of GDP. While FY27 CAD/GDP may now widen to 2.3% of GDP (1.7% at Brent USD80/bbl), the bigger vulnerability lies in the capital account. Absent regulatory policy measures to attract foreign inflows, FY27 could see a BoP deficit of >USD75bn.

Policy choices unlikely to be easy: FX-rate trade-offs and long-term energy security

There is no simple playbook for policy responses to the energy price shock. As the pass-through of elevated energy costs to consumers is now underway, second-round effects via inflation expectations, growth shocks, tighter financial conditions, and FX management shape RBI's trade-offs. Any future rate hike would be aimed at curbing domestic demand pressures or anchoring inflation expectations, rather than defending INR. FX volatility will continue to be managed through reserves and regulatory measures. More broadly, policymakers have tended to prioritize growth-inflation objectives over FX stability over the year(s), keeping rates relatively accommodative despite periods of external outflows. While this may have made FX arbitrage/speculative INR trades cheaper, higher rates alone may not attract durable capital flows that eventually follow credible growth and sectoral innovations. Separately, from an energy security point of view, there is a case to use fuel taxation strategically and avoid broad-based fuel subsidies to encourage i) efficiency and lower oil intensity; ii) energy security; iii) push diversification toward EVs, public transport, and renewables; and iv) fiscal health. The additional fiscal revenue space can be used to reallocate resources directly to the vulnerable section of the economy that may feel disproportionately hit from higher taxes.

Key highlights:

- Oil market imbalances rise despite reopening noise; prices set to move higher than expected
- FY27E average Brent price raised to USD90/bbl; headline CPI at 5.1%
- Growth revised down to 6.3%; CAD/GDP at 2.3%, with BoP deficit of >USD75bn
- Any rate hike to target inflation and curtail demand, not defend the INR
- Need to enact policies toward long-term energy security

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Energy crisis: The end is not in sight

Nearly 14 weeks into the West Asia crisis and the largest energy shock in history (~15% of global oil supply), the oil market is remarkably sanguine. While Brent prices did hit an intraday high of USD126/bbl in April, they are currently hovering around USD95-100/bbl, which is far from predictions of >USD150/bbl being made pre-crisis in the event of the Strait of Hormuz (SoH) being closed. We have remained skeptical about both the trajectory and ultimate resolution of the US-Iran conflict. Since the outset, we have argued that market pricing was not fully reflecting the risk of a prolonged confrontation, instead assuming a short and highly asymmetric power conflict ([See: India amid the West Asia conflict – Caught in a squeeze, March 2026](#)). While the military balance has remained heavily tilted against Iran and the intensity of hostilities moderated following the ceasefire, we maintained that the endgame for both Iran and the US/Israel remained uncertain, pointing to a period of sustained tensions rather than a swift resolution.

While there are several factors (both structural and transient) which have led to the shock being cushioned so far, we believe that these buffers are rapidly running out. Importantly, even if the SoH was to reopen completely today, the pressure built up so far would mean that Brent prices would remain elevated for a few months (notwithstanding a drop in prices following any reopening announcement). Thus, we are increasingly looking through the timing of any impending announcement – the world faces a shot clock as inventories are depleted and minimum threshold levels are reached. SoH closure beyond end-June will lead to a sharp spike in oil prices as buffers are exhausted.

Additionally, we believe that a credible and stable US-Iran agreement is becoming increasingly difficult to achieve. The two sides remain far apart in terms of their respective positions, with little sign of a breakthrough in negotiations. While economics dictates that SoH will probably be opened, one way or another, by the end of June, the likelihood of this outcome being reached via military escalation is no longer trivial. Such an outcome would send energy prices spiraling, and probably lead to Brent breaching USD150/bbl. While it will take a few months for new oil supply (especially from US shale oil producers) to materialize in response to higher prices, the demand reaction will be far quicker, with large curbs in economic activity required to bring the oil market toward balance.

Thus, with oil (and gas) prices expected to remain elevated well into FY27, we also reassess the impact on India's macro dynamics, with a further hit to CAD, GDP growth, and inflation. We raise our FY27E Brent forecast to USD90/bbl (vs USD80/bbl earlier). This will feed into our economic cost models for India, both on external and internal accounts. We discuss below the key issues around fair oil pricing, macro impact, and policy prescriptions.

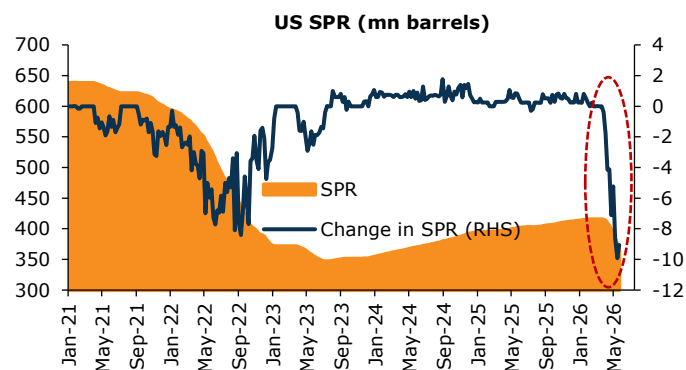
Global oil demand-supply dynamics have been manageable (so far)

Pre-crisis, flows of crude oil and condensates through SoH amounted to ~15mbd, with petroleum products adding another ~5mbd. This amounted to ~20% of global POL consumption. While most of this supply has gone off the market since the start of the crisis, the oil price response to this supply shock has been muted due to a few factors on both the demand and supply side. Some of these factors are structural, while most are temporary, and thus will fade as the crisis remains unresolved.

Global oil supply has had several buffers, but these are dwindling

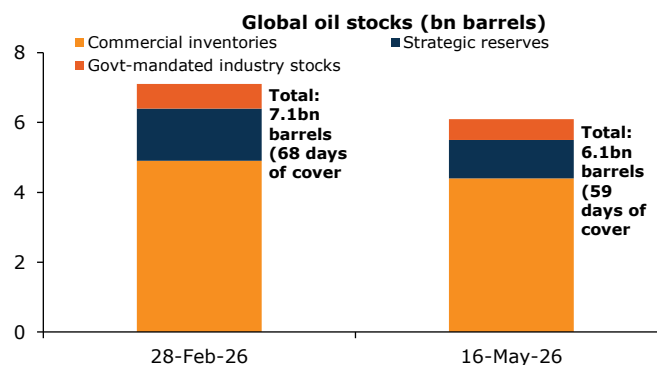
- **Reserve releases and inventory drawdowns (temporary):** This is among the largest factors keeping oil prices lower than estimated earlier. The IEA's announcement of 400mn barrels of emergency oil releases (of which ~300mn barrels are crude oil) amounted to ~2.5mbd over four months – a significant buffer. However, this buffer is limited as time passes, with any incremental releases drawing from depleted reserves. Additionally, global commercial inventories have dropped at record rates, with ~500mn bbl of drawdown estimated till mid-May. Understandably, going forward, similar rates of drawdown are unlikely.

Exhibit 1: US SPR has seen the highest weekly drawdowns in history, recently



Source: US EIA, Emkay Research

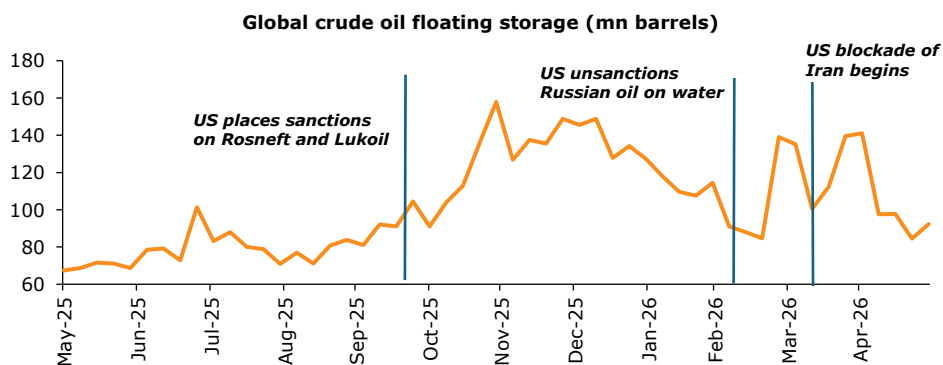
Exhibit 2: Global oil inventories have fallen sharply on the back of heavy drawdowns



Source: Oil 101, Morgan Downey, Emkay Research

■ **Sanction waivers and floating storage (temporary):** There were an estimated ~115mn barrels of crude oil stockpiled at sea just before the conflict began – largely driven by Russian oil after US sanctions on Lukoil and Rosneft in Oct-25. These were drawn down rapidly once the US issued (and extended) sanctions waivers for Russian oil already on water as supplies from SoH were choked. Similarly, Iran was also stockpiling barrels on water ahead of hostilities, which were depleted when a similar sanctions waiver was provided by the US in late March. Iran’s on-water stockpile began rising again following the US blockade which began on 13-Apr-26. Since then, floating storage has been depleted again as some SoH transits took place and countries drew on inventories on water to meet domestic demand.

Exhibit 3: Sanctions waivers and a supply glut had led to a large volume of floating oil storage

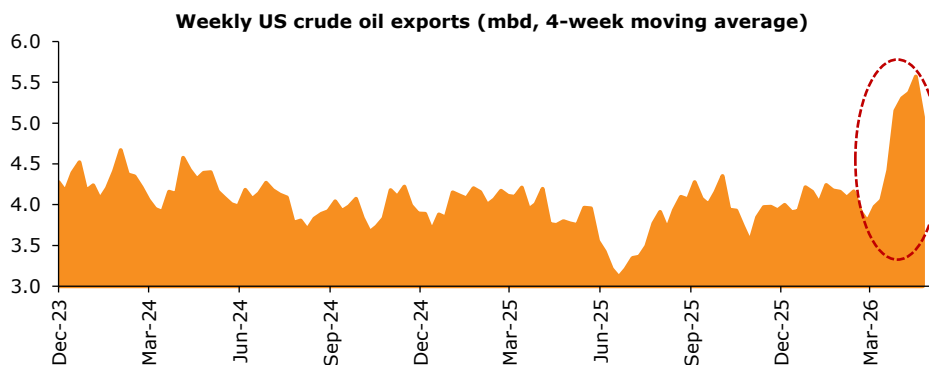


Source: Bloomberg, Emkay Research

■ **Pre-war surplus and higher non-Gulf exports (temporary):** The world was swimming in surplus oil prior to the conflict, which had led to Brent prices hovering around USD60/bbl. This had been led by a surge in supply from the Americas – US exports of crude had risen to 4mbd by Dec-25 vs ~3mbd in Jul-25, while Canada, Brazil, and Guyana also increased exports significantly. Notably, non-Gulf producers have also shipped far more exports in recent weeks compared to pre-crisis levels. US exports have shot up to ~5mbd, with other smaller producers (Canada, Norway, Venezuela, etc) also collectively adding over 0.5mbd in exports. These run-rates may not be sustainable; the US especially may see exports drop as refineries return from seasonal maintenance and crude oil is redirected (especially given the sharp drop in petrol and diesel inventories in the US).

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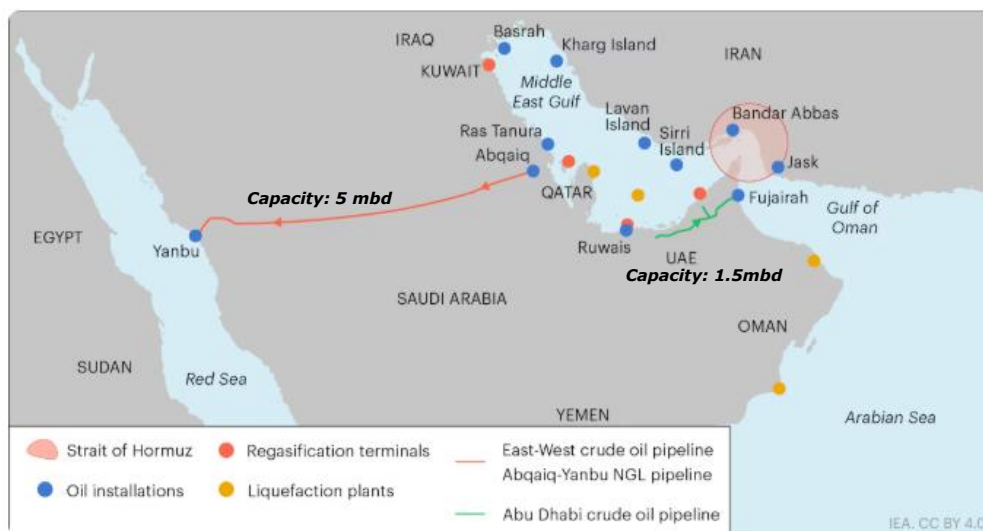
Exhibit 4: US crude exports have surged to >5mbd, helping offset some of the SoH supply shock



Source: US EIA, Emkay Research

- SoH bypass (structural):** Both Saudi Arabia and the UAE have pipelines which allow their oil exports to circumvent SoH. Saudi’s East-West pipeline (capacity: ~7mbd) runs to Yanbu on the Red Sea coast, while UAE’s Fujairah pipeline (capacity: ~1.5mbd) is to the Fujairah Port on the Gulf of Oman. With these pipelines running at some capacity before the crisis, it is estimated that 5.5-6mbd of oil is incrementally flowing since the crisis, and thus bypassing SoH entirely. This supply route is now likely to be permanent; both Saudi and the UAE are unlikely to move export volumes back from these pipelines to SoH even after reopening.

Exhibit 5: Saudi and UAE pipelines can only offset a fraction of lost SoH supply



Source: IEA, Emkay Research

Demand moderation has helped keep a lid on prices

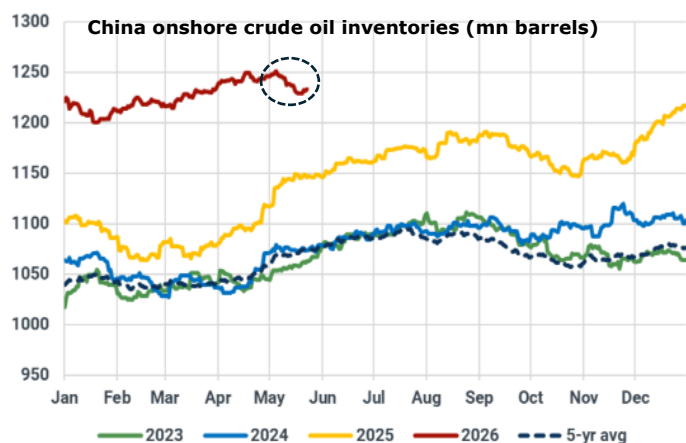
While the supply shortfall has been mitigated partially through the factors mentioned above, demand correction has also helped keep oil prices lower than expected with such a large supply shock. Global consumption is estimated to have fallen by 1.5mbd between Dec-25 and Mar-26 – however, the decline in oil imports by major consumers would have been much higher, with countries rapidly using reserves rather than imports to meet domestic demand. One of the largest factors here has been China’s absence from the global crude oil market. Data from Kpler shows that China’s crude oil imports fell to 6.4mbd in May-26, from 11.4mbd in Feb-26 – a drop of 44%.

This reflects sourcing challenges for China, with SoH being closed and unsanctioned Russian supplies going to India (and other countries). China has managed this situation by drawing down commercial inventories and cutting refined product exports – it has not yet meaningfully dipped into its own strategic oil reserves (estimated: 1.4bn barrels pre-crisis). Chinese refiners have also kept refinery run-rates low – thereby reducing crude oil demand. This has

been partly influenced by poor downstream economics – domestic fuel consumption in China has been dampened, as users accelerate towards renewables. As a result, despite multi-year low refinery run-rates, China’s commercial gasoline and diesel inventories remain just below two-year highs.

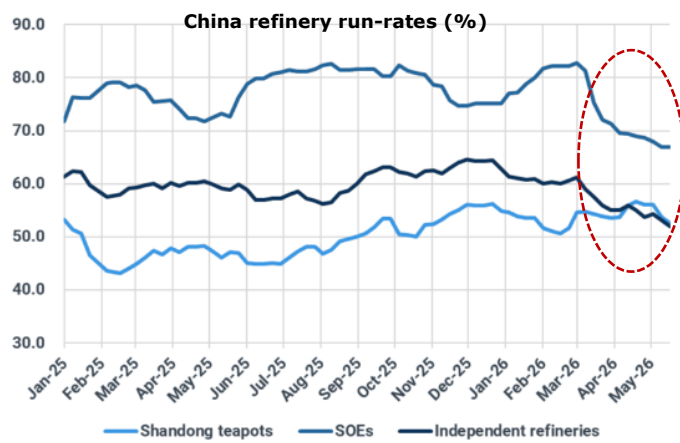
However, commercial stocks will not last long, meaning that China will have to do one or more of the following – increase crude imports, cut refinery output, or meaningfully tap its strategic reserves.

Exhibit 6: China’s crude inventories have started moving lower



Source: Kpler, Emkay Research

Exhibit 7: Refinery run-rates have dropped to multi-year lows



Source: Kpler, Emkay Research

There has been demand moderation elsewhere too, with various governments implementing austerity measures in the face of looming fuel shortages.

Exhibit 8: Several countries across Asia have put energy conservation measures in place

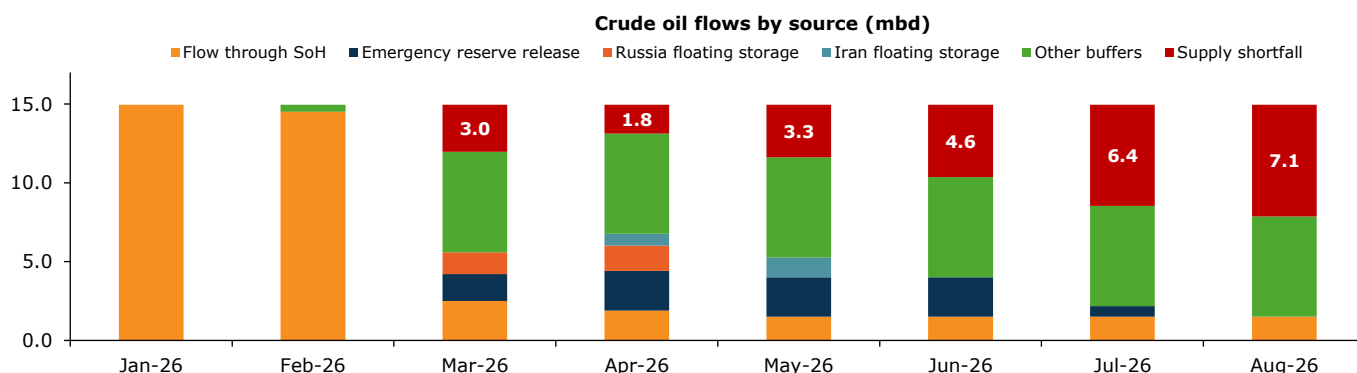
Country	Energy conservation	Consumer support	Structural policies
India	WFH encouraged; citizens asked to avoid foreign travel and use public transport; commercial LPG rationing; limits on govt travel; speed up shift from domestic LPG to PNG	Domestic jet fuel prices capped; petrol and diesel excise cut	Promote shift to electric cookstoves; instruct state-run FIs to transition to EVs
Thailand	WFH encouraged; overseas travel limited for govt officials; carpooling encouraged	Cooking fuel prices frozen; fuel subsidies	-
Indonesia	WFH on Fridays for civil servants; govt travel limited	Fuel subsidies; aviation fuel surcharge hiked but VAT on economy tickets cut	Accelerate shift to electric stoves, and conversion of ICE bikes to EVs; replace LPG with domestic PNG; convert diesel-powered plants to solar power
S Korea	WFH encouraged; 2-day odd-even driving mandated for public sector workers; private vehicles asked to not drive 1 day per week; public parking access limited based on license plates	Domestic fuel prices capped; fuel tax cuts; cash vouchers provided to bottom 70% of population	-
Vietnam	WFH encouraged; govt travel limited; public transport and carpooling promoted	Fuel import tariffs cut; fuel price stabilization fund boosted	Reduce taxes on EVs
Philippines	4-day work week for public officials; encourage AC temperature limit to 24 degrees; govt travel limited; free bus rides for students and workers in select cities	Fuel excise taxes cut; LPG excise taxes suspended; fuel for buses, taxis, delivery services etc to be subsidized; fuel and fertilizers for farmers subsidized	-

Source: IEA, Emkay Research

In total, the various buffers mentioned earlier, along with demand curtailment, have helped keep oil prices relatively contained since the crisis began. It is estimated that the oil market ‘adjustment’ ie supply shortfall was to the tune of 3.3mbd in May, with this rising to 4.6mbd in June. If SoH stays shut beyond June, the supply shortfall could be as high as 7.1mbd by August, as all temporary buffers are exhausted.

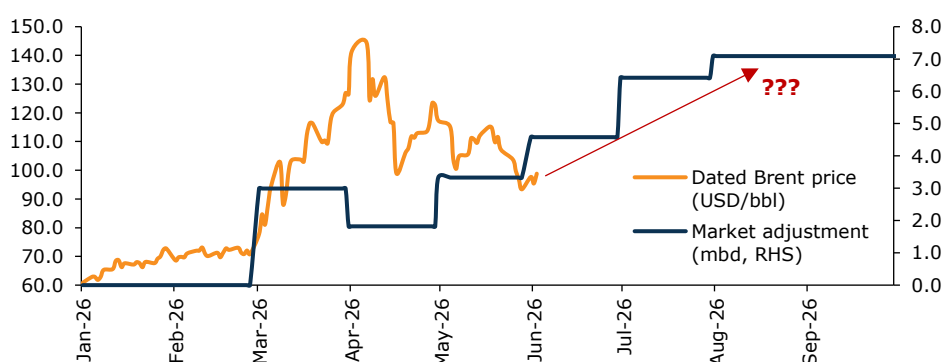
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Exhibit 9: The oil market may see a supply shortfall of ~7mbd by August if SoH does not open by then



Source: Brookings Institute, Emkay Research

Exhibit 10: Dated Brent prices have closely tracked the supply shortfall so far, implying a sharp move higher if SoH closure persists



Source: Brookings Institute, Emkay Research

The day after: Supply normalization delay and demand surge will keep prices elevated

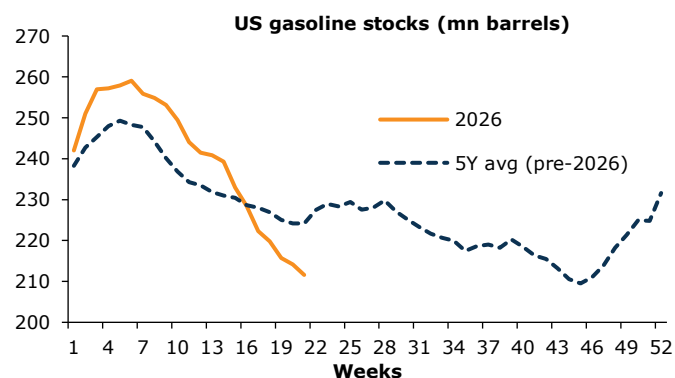
Even assuming SoH is reopened and free to use for all commercial shipping immediately, it will take weeks to months for exports through SoH to normalize to pre-crisis levels. Brent prices may fall sharply in reaction to any "SoH is open" announcement, but there are several factors which will lead to a supply-demand mismatch and thus cause prices to move higher in the short-term:

- Reopening ≠ immediate supply normalization:** It could take a few months for exports through SoH to normalize even after shipping conditions improve over time. Operational frictions like tanker availability, insurance costs, war-risk premiums, clearance of mines/security risks in SoH, buyers being cautious about loading cargoes etc. will linger. In short, while SoH reopening may gradually adjust fundamental balances, the geopolitical + logistics premium may linger for some time, while inventory normalization takes place, and possibly new supply also enters in the oil equation, led by Iran's entry into the formal market and lagged production ramp-ups by US shale producers.
- Inventory normalization:** The near-term inventory re-building will be painful, given the war intensity and broken infrastructure in the Middle East. Such inventory normalization after a major supply shock is usually not a neutral process for prices - it often requires the market to move into surplus, sometimes a sizeable one. OECD commercial inventories will likely normalize to pre-crisis levels by early CY27, while there is likely to be strong demand from China to replenish its commercial (and possibly strategic) reserves. We do maintain that SoH reopening is likely to unleash a strong supply response, with Gulf producers seeking to recover lost revenues, and other producers looking to maximize output in a high-price environment. This could push the

oil market into a surplus by late-2026, allowing OECD inventories to normalize in early 2027 and placing sustained downward pressure on prices.

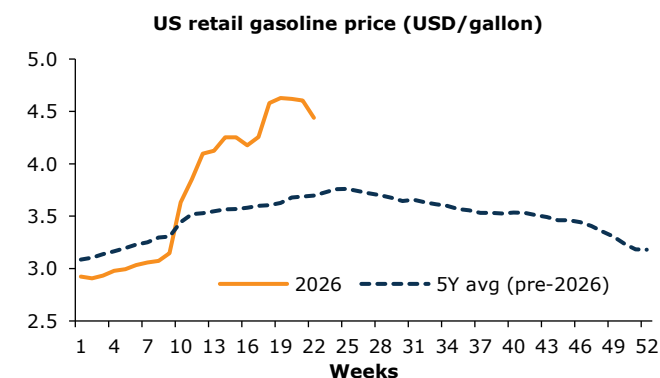
- **Timelines for restarting production:** Oil/gas refinery production typically does not snap back to full rates after a prolonged shutdown. Production may be restored gradually over roughly 1.5-2 months, or may even take longer. Given that Middle East refinery runs remain curtailed by ~3mbd, broadly matching prior export volumes, product exports are unlikely to rebound instantly. Instead, refiners are expected to bring capacity back online in stages, with throughput normalizing over the subsequent 4–10 weeks.
- **Natural gas:** Typically, natural gas is the quickest to recover, as gas remains in the well until production resumes. As per [EIA](#), immediately after restarting production, these wells often produce more natural gas than before the shutdown because of a temporary pressure build up.
- **Crude oil:** For crude oil, the ramp-up is often less immediate and often involves high restoration costs. (See, [BBG: Turning Oil Wells Back on Is Trickier Than Shutting Them Offs](#))
- **Refineries:** Meanwhile, refineries typically take the longest to restart. The EIA has highlighted the operational complexity of refinery turnarounds, noting that major units can remain offline for weeks to months and may require 1,500–2,000 specialized contractors to execute interrelated maintenance activities. As such, rapid restoration of refinery throughput following prolonged disruptions is unlikely.
- **US driving season demand:** As mentioned earlier, the US has been exporting record levels of crude oil (and refined products) over the last couple of months, which has helped cushion the blow from SoH closure. However, this buffer could vanish soon as the summer driving season approaches. Even with SoH reopening, it is likely that domestic demand for crude (by refineries returning from maintenance) will rise, to meet the seasonal surge in demand for petrol and diesel (especially with gasoline stocks at multi-year lows, and rising gasoline prices). In such a scenario, it is plausible that US exports of petroleum products will drop, which will put some upward pressure on global prices in the short-term.

Exhibit 11: US gasoline stocks are at multi-year lows...



Source: US EIA, Emkay Research

Exhibit 12: ...with prices spiking ahead of the driving season



Source: US EIA, Emkay Research

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Credible US-Iran deal remains some way off

While there has been plenty of noise (especially on social media) around an imminent US-Iran deal, the two sides remain some way apart in terms of their respective positions.

Exhibit 13: US and Iran still have crucial points of difference to resolve before a deal is agreed

	Iran position	US position
Traffic through Hormuz strait	Wants to control maritime traffic	Insists on free passage for vessels
Iran's frozen financial assets	Iran media says government wants \$12bn unfrozen with an interim deal	Unclear; pressure on Trump from Iran hawks not to release funds
Lebanon	Ceasefire must include Lebanon	Ally Israel reluctant to have its operations in Lebanon restricted
Iran's highly-enriched uranium	Says it wants to keep possession of its stocks; may accept them being sent to Russia or China	Trump wants HEU destroyed or sent to US

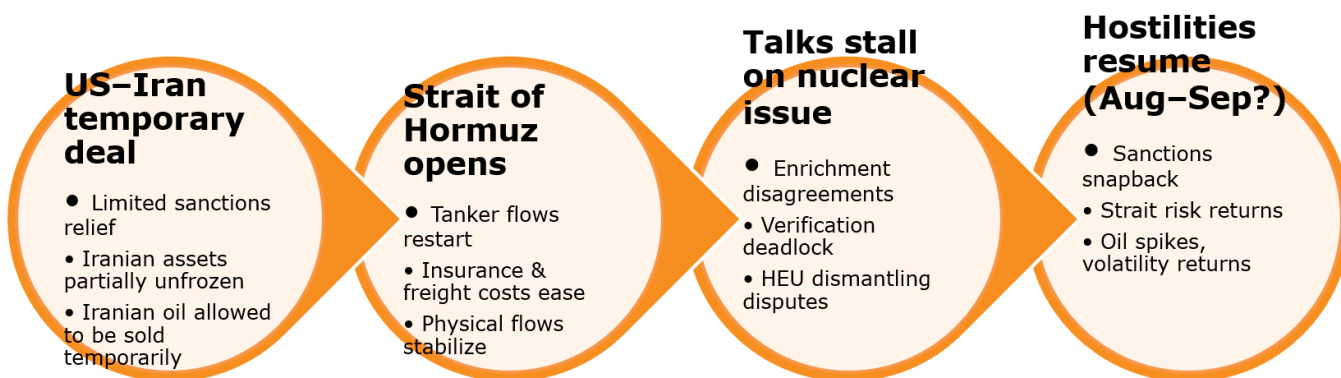
Source: Bloomberg reporting

Bloomberg

Source: Bloomberg, Emkay Research

As Exhibit 13 shows, there are fundamental differences between the two sides which have not been resolved, despite months of hostility and negotiations. The likelihood of a credible deal emerging from the current scenario remains remote. The chance of yet another round of 'escalation to de-escalate' is now material, in our view. Such an outcome would send energy prices spiraling and possibly lead to a global recession. We also believe that such an outcome may not take place immediately. The most likely framework is for a deal where the ceasefire is extended (say, for 60 days), with Iran being able to sell oil in that period, and receiving some of its funds frozen abroad, while the US and Iran negotiate the nuclear question in that period. It is plausible that these negotiations then flounder, as Iran will have even less incentive to give up its nuclear ambitions, and we could then see a return to conflict around August or September. Of course, logic dictates that the two sides come to a mutually beneficial agreement, but the events of the past three months have shown that logic (at least, economic logic), has been in short supply when it comes to this crisis.

Exhibit 14: Potential US-Iran negotiation and escalation timeline



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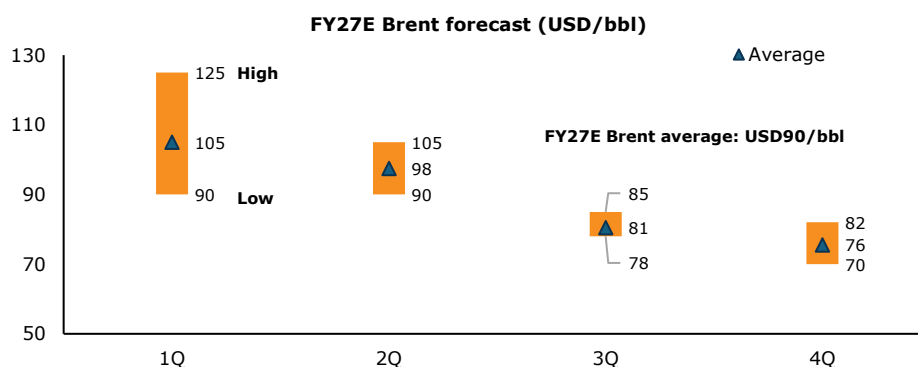
Source: Emkay Research

Economics of the energy supply shock

Energy costs pass through: Revisiting distributional hit and macro forecasts

The protracted disruption to global energy supply from the Iran conflict has slightly undermined our revised assumption in March-26 that oil prices would average USD80/bbl in FY27 (vs USD65-70/bbl earlier) and could meaningfully be lower from July. We revise Brent crude estimate further upwards by another USD10/bbl, with 1Q averaging USD105/bbl, while 2Q moderates only to around USD98/bbl. However, Brent could ease materially to USD75/bbl by 4Q. That said, oil markets have been patchy amid near-daily news updates. It is crucial not to get too hung up on the daily oil price fluctuations because they do not move the needle materially on our baseline forecast—the monthly and quarterly averages are more important for forecasts of macro variables.

Exhibit 15: Brent prices expected to be elevated until 3Q, before gradually falling by end-FY27



Source: Emkay Research estimates

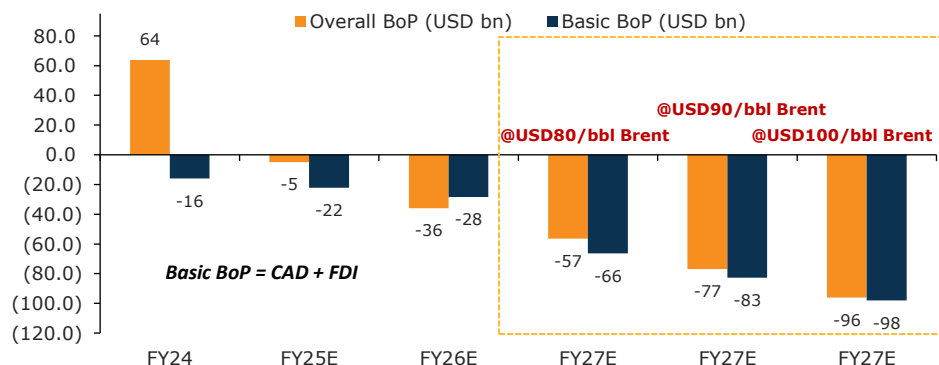
While it will take time to gauge the magnitude of the shock and its macroeconomic impact, we understand the impact of a lingering war could soon translate from being an economic issue to being a material risk to macro-financial stability. The longer the conflict drags on, the greater the risk that energy sector disruptions generate a nonlinear hit to growth, operating through prices, quantity constraints, and sentiment and financial channels. The only comfort lies in a stronger starting point, which equips us with buffers to navigate macro adjustments. Indeed, recent macro high frequency activity indicators are not showing signs of any material slowdown.

BoP hit: FY27 CAD/GDP may cross 2%; capital funding to stay difficult

- On a static basis, every USD10/bbl increase in crude prices is likely to widen the CAD/GDP by ~0.45%. However, economic variables and foreign capital flows are rarely static in dynamic stress situations. The impact on the current account would be significantly larger if remittances from the ME to India also come under pressure, while global/domestic demand slows. Besides, risk aversion would significantly influence the direction of foreign flows and gold demand/prices (a key hit to CAD this year)—although easing gold prices in this uncertainty cycle could actually act as a mild buffer.
- A sub-USD90/bbl case for crude appears manageable, through a combination of letting INR absorb the shock and using FX reserves effectively to prevent any disruptive adjustment. In contrast, if crude were to go much above that, the pressure would begin to rise sharply. With our new baseline Brent at USD90/bbl, we are tracking FY27E CAD/GDP at 2.3% (vs 1.7% earlier), while BoP is now tracking at ~USD75bn (vs USD40bn earlier).
- Our dynamic scenario analysis at average Brent at USD100/bbl for FY27E implies that CAD/GDP could widen to >2.5%, while BoP deficit could worsen to >USD95bn.
- We are estimating relatively stable service exports, assuming the current run-rate continues or improves and a mild hit to remittances.

Capital funding of CAD stays a concern and as we noted in our recent reports, any policy response to raise rates to offer higher India's risk premia may not be enough to sustain foreign flows. Higher rates alone may not attract durable capital flows that eventually chase credible growth and sectoral innovations. To that extent, the only way to adjust the external imbalances is via current account adjustments, FX adjustments and import demand reduction.

Exhibit 16: Our base case of USD90/bbl Brent would see BoP widening to USD77bn, while even higher oil prices would widen this further to nearly USD100bn



Source: CEIC, Emkay Research

Exhibit 17: CAD/GDP to widen to 2.3% of GDP in FY27E with average Brent at USD90/bbl

	Oil @83	Oil @78.8	Oil @66.5	Oil @80	Oil @90	Oil @100
(USD bn)	FY24	FY25	FY26E	FY27E		
Current account	(26)	(23)	(36)	(78)	(95)	(108)
CAB/GDP (%)	(0.7)	(0.6)	(0.9)	(1.9)	(2.3)	(2.7)
Trade balance	(245)	(287)	(333)	(394)	(410)	(424)
Trade balance/GDP (%)	(7.0)	(7.6)	(8.5)	(9.7)	(10.1)	(10.4)
- Exports	441	442	450	467	475	481
- oil exports	84	63	54	59	67	75
- non-oil exports	357	379	396	409	409	407
- Imports	686	729	783	861	886	905
- oil imports	179	186	174	211	235	262
- non-oil imports	508	543	601	644	644	637
- gold imports	46	58	72	74	74	72
Net invisibles	219	264	297	316	316	316
- Services	163	189	214	229	229	229
- software	142	160	176	186	186	186
- non-software	21	29	39	43	43	43
- Transfers	106	123	135	140	139	138
- Net Income	(50)	(48)	(52)	(53)	(53)	(53)
Capital account	90	17	0	21	17	11
% of GDP	2.7	0.4	0.0	0.5	0.4	0.3
Foreign investment	54	5	(11)	0	(4)	(10)
- FDI	10	1	8	12	12	10
- FPI	44	4	(18)	(12)	(16)	(20)
Banking capital	41	(10)	5	8	8	8
Short-term credit	(1)	7	18	5	5	5
ECBs	(0)	16	9	10	10	10
Others	(12)	(7)	(23)	(8)	(8)	(8)
Overall BoP	64	(5)	(36)	(57)	(77)	(96)

Source: CEIC, Emkay Research estimates

Burden sharing of energy cost slightly more proportionate now....

The eventual fiscal and inflationary impact hinges on how the burden is shared between the balance sheets of oil marketing companies (OMCs), government (via a cut in oil duties and increase in subsidies), and end-consumers (via price hikes). Price absorption by OMCs would also effectively constitute a fiscal cost, as it erodes the dividends these companies would otherwise transfer to the government. Conversely, if OMCs were to incur sustained losses,

they would likely be compensated by the government in some form, ultimately shifting the burden back onto public finances and impeding the Centre's spending ability.

Separately, **the greater the share of the oil shock absorbed by the government or OMCs, the smaller the pass-through to retail CPI inflation.**

The eventual fiscal and inflationary impact will hinge on how the burden is shared between the balance sheets of oil marketing companies (OMCs), the government (via a cut in oil duties and increase in subsidies), and end consumers (via price hikes).

However, we had argued in our last report as well that the **best fit in a protracted supply shock situation is near-equal distributional burden sharing by economic agents**, with OMCs bearing the first leg of pain, followed by the government and eventually the end-consumer. This is pertinent for growth, because if the fiscal deficit target remains unchanged, any oil shock absorbed through fiscal policy—directly or indirectly—would crowd out other categories of public spending on a one-for-one basis. In contrast, if the shock is allowed to pass through to CPI and reduces household real incomes, the adjustment in consumption is likely to be more gradual relative to the sharper contraction typically associated with fiscal compression. To that extent, a fair burden sharing is actually better for growth outcomes on net.

[\(See: India amid the West Asia conflict – Caught in a squeeze, March 2026\)](#) for detailed assessment of cost sharing mechanism of the current energy shock.

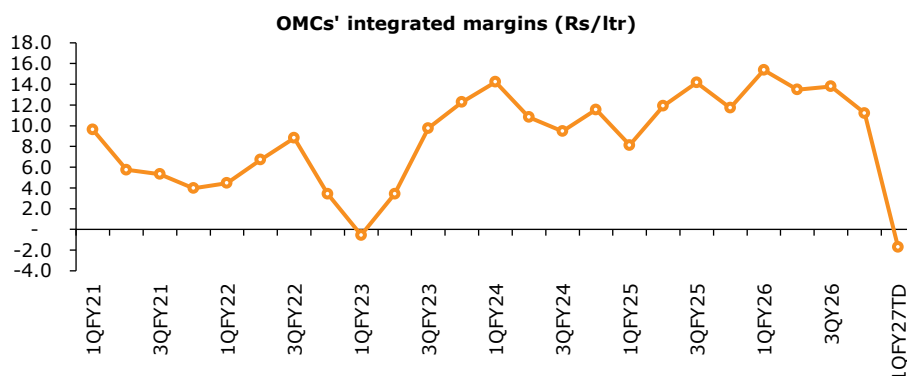
The current crisis now has consumers bearing the cost too, and fairly so

The first leg of the ongoing energy crisis was squarely borne by OMCs, as in the past crises, where OMCs typically run under-recoveries when crude oil prices rise, while periods of lower crude prices allow them to rebuild margins. For every USD1/bbl increase in Brent, we estimate an impact of ~Rs0.52/ltr on diesel and ~Rs0.55/ltr on petrol retail prices. With Centre stepping in with excise cuts of Rs10/ltr (offsetting some of its losses by export levies on petroleum products), part of the OMCs pain was shared by the Centre. End-consumers largely entered the equation more recently, with pump fuel prices and CNG prices finally raised by Rs7.5/ltr and Rs4-7/ltr, respectively.

The calculations of marketing margins auto fuels are dynamic in nature. Based on current oil prices and exchange rates, OMCs do not require a further increase in retail prices of petrol and diesel respectively. This implies that annualized deficit for OMCs on auto fuels at current level of Brent prices (USD95/bbl) and USD/INR exchange rate is negligible. Meanwhile, annualized deficit on cooking fuels is tracking ~Rs680bn, based on our energy price forecasts. This compares with the highs of ~Rs4.5trn of annualized OMC auto fuel losses and cooking fuel annualised losses of nearly Rs1-1.5trn during the peak of the crisis in Mar-26 (Brent at USD110/bbl). This of course was before the excise cut by the Centre and fuel price hikes, implying the total direct economic cost was tracking ~1.5% of GDP on an annualised basis in mid-March.

Consumers are now bearing a fair share (~28% of the current estimated direct cost of crisis), while the government still ends up taking the maximum hit, given it also gets indirectly hit by lower OMCs dividends/taxes and other fuel related subsidies, especially fertilizers. We do not assume further pump price hikes if prices dip to <USD90/bbl in coming months.

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Exhibit 18: OMCs are facing a heavy margin hit in 1QFY27

Source: Company data, Emkay Research. Note: Data for 1QFY27 is till date

The estimated cost sharing shows lower burden for OMCs in 2HFY27, while government bears the most, and peaks for consumers in 3Q

As we mentioned earlier, the cost assessment of economic agents is a dynamic exercise and thus a more realistic assessment could assume lower crude prices, albeit more towards the end of the year.

The estimated cost sharing mechanism ahead assumes crude prices come off in 2H, but meaningfully so only in 4QFY27E to ~USD75/bbl average, vs nearly USD102/bbl in 1HFY27E. While cooling oil prices may allow OMCs to rebuild margins, some pump prices cut and excise cut reversal may happen as well.

Exhibit 19: Evolution of direct economic cost of the energy shock assuming dynamic Brent prices through the year

	1QFY27	2QFY27E	3QFY27E	4QFY27E
Consumption of Petrol (bn ltrs)	13.4	13.4	13.4	13.4
Consumption of Diesel (bn ltrs)	25.1	25.1	25.1	25.1
Centre's loss on excise duty cut (Rs bn)	401	401	200	0
Centre's gains on SAED (Rs bn)	-100	-50	-50	-50
Net loss for Centre from auto fuels (Rs bn)	301	351	150	-50
Net loss for Centre from LPG subsidy (Rs bn)	271	172	137	102
Net total loss for Centre (Rs bn)	572	523	288	52
OMCs hit on Petrol and Diesel without fuel hike (Rs bn)	475	297	82	158
OMCs hit on Petrol and Diesel with fuel hike and reversal later (Rs bn)	362	51	-164	158
End-Consumer hit (Rs bn)	133	289	289	0.0
Total direct economic cost (excludes immediate indirect costs like dividend hit and fertiliser subsidy)	1,067	864	413	211
% of GDP	1.1	0.9	0.4	0.2
Brent price assumption (USD/bbl)	105	97.5	80.5	75.5

Source: Emkay Research estimates (Energy team); Note: Assume partial roll back of excise cut in 3Q; full roll back of excise and fuel hike in 4Q

Exhibit 20: Estimated fiscal hit based on Brent price evolution through FY27

Best fit case and fiscal math at estimated energy cost	Rs bn
Fiscal loss owing to energy crisis (estimated assuming 1H& 2H Avg Brent at USD101/bbl and USD78/bbl)	1,590
- Excise cut net of export windfall taxes	
- LPG subsidy	
- Dividend/corp tax hit from OMCs	
- Fertiliser subsidy (additional estimated)	1,000
Fiscal offsetting factors	
- Economic Stabilization Fund	1,000
- Non core capex cut	350
- RBI dividend extra	0
- Non core revex cut	450
Net fiscal slippage	-790
Net fiscal slippage (% of GDP)	-0.2

Source: Emkay Research estimates. Note: Assumes other revenue streams as budgeted

Growth-inflation headwinds persist in the near future

The impact of energy shock on GDP is generally assessed primarily through the private and government consumption channel, where higher inflation leads to an erosion of real incomes and weaker consumer spending or lower ability to do effective fiscal spending, leading to smaller growth multipliers. With burden sharing, the growth impact is relatively less severe than otherwise. If the shock is allowed to pass through to CPI and reduces household real incomes, the adjustment in consumption is likely to be more gradual relative to the sharper contraction typically associated with fiscal compression.

We had trimmed our growth forecast to 6.6% in late-March, with Brent averaging at USD80/bbl. With upwardly revised Brent prices and prospects of weaker monsoons amid El Niño effect, we trim our FY27E real GDP growth forecast further by 30bps to 6.3%. However, real GVA growth is likely to be higher at 6.5%, accounting for lower net indirect taxes, amid higher subsidies and possibly lower indirect taxes.

We expect FY27 headline inflation to average 5.1%, incorporating a moderate El Niño impact, and pump price hikes of Rs10/ltr in 1QFY27, to be partly reversed by end-FY27 as oil prices ease to <USD80/bbl. We also incorporate second order and spillover effect on generalised inflation due to higher energy prices. FY27E core inflation is estimated at 4.3%, reflecting mild energy-led supply-side price pressures on non-food goods and services.

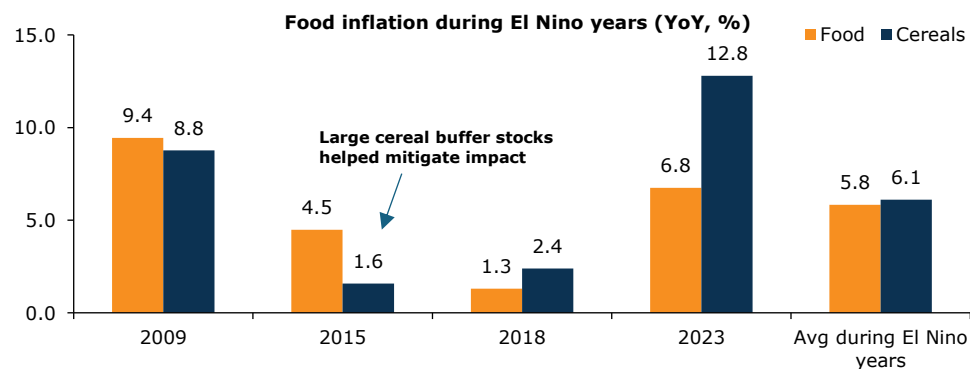
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Exhibit 21: Real GDP growth seen slowing to 6.3% in FY27E on account of the energy shock and weak monsoons

YoY, %	FY22	FY23	FY24	FY25	FY26E	FY27E
Real GVA	9.4	7.2	7.2	7.3	7.7	6.5
Agriculture and allied	4.6	6.3	2.6	4.2	2.4	2.0
Industry	12.2	2.5	10.9	8.3	8.8	6.8
Mining	6.3	3.4	2.4	11.7	4.3	7.3
Manufacturing	10.0	(1.7)	12.7	9.3	11.7	7.5
Electricity	10.3	10.8	10.7	2.9	1.3	6.2
Construction	19.9	9.1	9.9	7.3	7.0	5.5
Services	9.2	10.3	7.0	7.9	9.1	7.8
Trade, hotel, transport, communication	15.2	12.3	10.1	6.6	10.4	7.9
Financial, real estate, professional services	5.7	10.8	5.5	10.0	10.0	8.5
Public admin, defence, and others	7.5	6.7	6.8	5.0	5.6	5.9
Real GDP	9.7	7.6	7.2	7.1	7.6	6.3

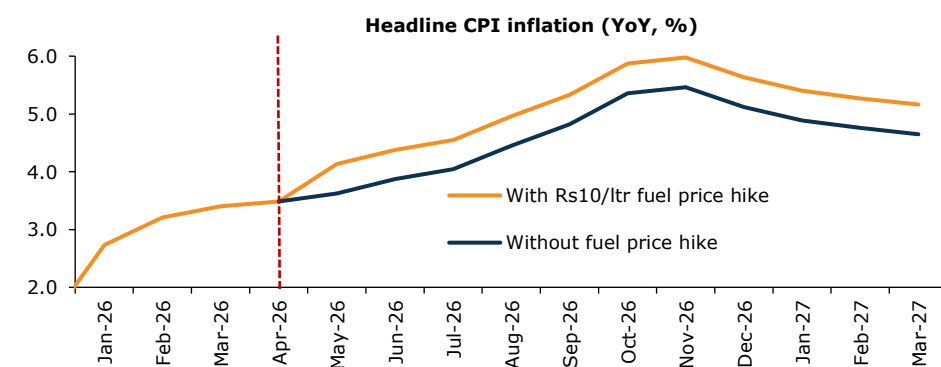
Source: CEIC, Emkay Research estimates. Data and estimates for FY24-FY27E are as per the new GDP series (base year 2022-23)

Exhibit 22: While El Nino hurts rainfall immediately, the impact on food inflation has been mixed



Source: CEIC, Emkay Research

Exhibit 23: FY27E headline CPI at 5.1% after Rs10/ltr fuel hikes and moderate El Nino impact



Source: CEIC, Emkay Research estimates

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RBI's battle unlikely to be easy: FX and rates trade-offs

There is no simple playbook for a monetary policy response to energy price shock. Amid benign inflation, the pre-war policy focus was on monetary policy transmission—especially in the bond market—via ample liquidity that kept overnight rates below the policy rate. While direct oil pass-through is visible via pump price hikes, second-round effects via inflation expectations, growth shocks, and tighter financial conditions now shape the RBI's trade-offs.

RBI MPC is likely to hold rates in June, it will still signal readiness to respond should inflation risks intensify and second-round pressures begin to emerge. While the percolation of the energy shock to the real sector is still unfolding, the RBI is likely to flag a cloudy Brent outlook amid a large drawdown in energy inventories and lingering geopolitical risks. This implies that if inflation pressures persist, rate hikes to the tune of 50-75 bps is not ruled out in the next one year.

The rate defense for INR?

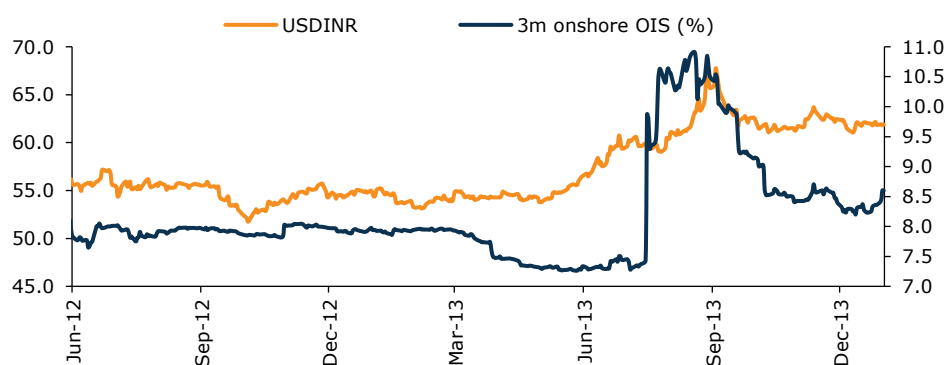
We do not expect the RBI to use rate hikes for FX management in the current juncture, given the MPC's inflation-targeting mandate. If rates are raised, the objective would be to curb domestic demand pressures or anchor inflation expectations rather than defend the INR. The 2013 experience highlighted the limits of interest-rate defense. Instead, we expect the RBI to continue managing FX volatility through reserves and regulatory measures, while potentially exploring incentives to boost USD inflows via external loans and other channels. A repeat of subsidized FCNR(B) schemes could be more costly in the current environment.

More broadly, policymakers have tended to prioritize growth-inflation objectives over FX stability in recent year(s), keeping rates relatively accommodative despite periods of external outflows. While this may have made FX arbitrage and speculative trades (short INR) cheaper, higher rates alone may not attract durable capital flows that eventually follow credible growth and sectoral innovations.

However, it needs to be seen if the RBI remains comfortable injecting abundant liquidity and sub-repo overnight rates. With INR under steady strain despite consistent FX intervention (largely via forwards), the associated liquidity drain is still being deferred, it needs to be seen if RBI keeps rates in check through bond purchases in FY27 as well.

(See, "India Strategy: Rupee defense – counting the cost", May 2026)

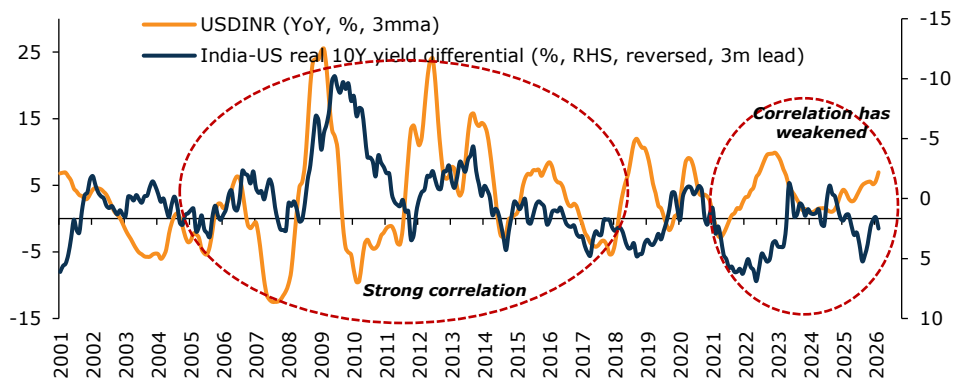
Exhibit 24: RBI's interest-rate defense of the rupee failed in 2013



Source: Bloomberg, Emkay Research

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Exhibit 25: Correlation between India-US real rate differential and USDINR has weakened post-Covid



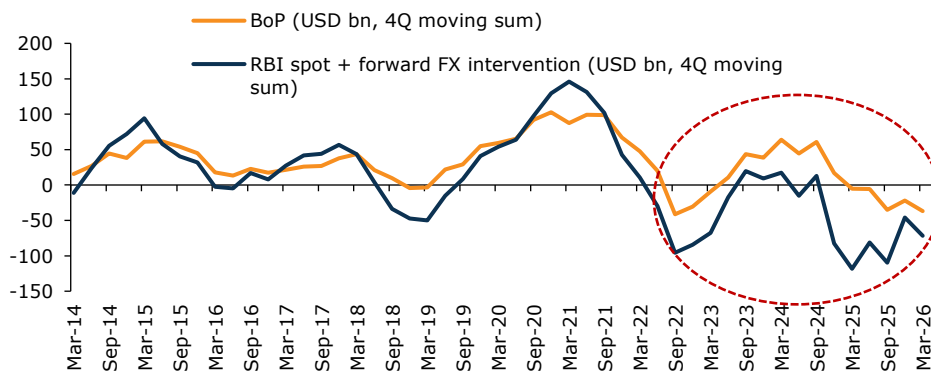
Source: Bloomberg, Emkay Research

Exhibit 26: India has been bearing the brunt of FPI outflows in Asia in CY26

Select Asia FPI flows (USD bn, latest available data)						
	MTD			CYTD		
	Debt	Equity	Total	Debt	Equity	Total
China	(18.9)	(64.4)	(83.3)	(29.4)	17.9	(11.5)
India	0.4	(4.1)	(3.7)	1.3	(28.2)	(26.9)
Indonesia	(0.1)	(0.2)	(0.3)	(0.8)	(3.2)	(4.0)
Japan	7.2	21.9	29.1	56.7	73.6	130.3
Malaysia	(1.3)	(0.5)	(1.8)	0.8	(0.2)	0.7
Philippines	1.4	(0.0)	1.4	3.1	(0.2)	2.9
S. Korea	0.4	(1.3)	(0.9)	30.6	(65.7)	(35.0)
Thailand	0.6	0.1	0.7	1.5	0.7	2.2

Source: Bloomberg, Emkay Research

Exhibit 27: RBI's FX intervention has recently been far higher than the BoP would warrant

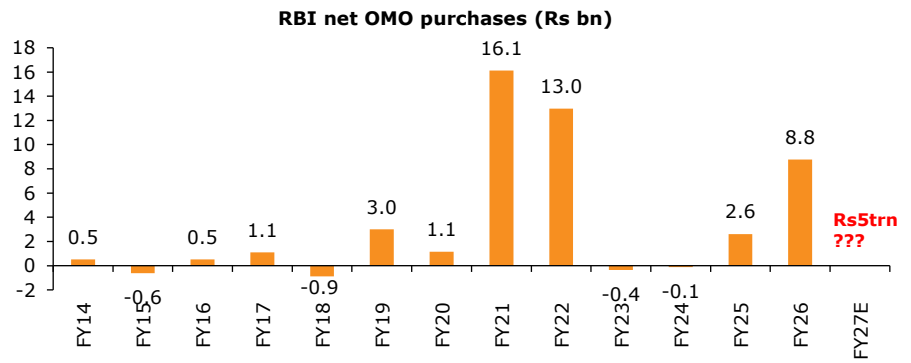


Source: CEIC, Emkay Research

RBI's FX intervention has generally been in line with the fundamental requirements of the economy (ie the BoP surplus/deficit). However, it has been intervening far more than the BoP would imply over the past couple of years, which contributed to keeping the INR relatively overvalued/undervalued. The BoP deficit for FY25 and FY26 combined would be <USD70bn, while FX spot + forward intervention over the same period has been >USD200bn, reflecting the RBI's need and intent to manage currency speculation.

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Exhibit 28: After Rs8.8trn of net OMO purchases in FY26, RBI may need to inject liquidity further to the tune of Rs5trn in FY27E



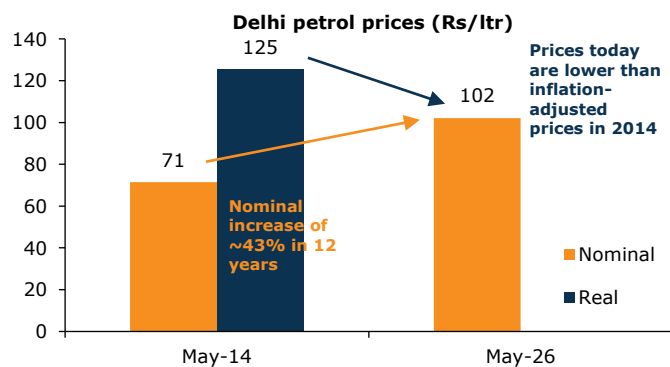
Source: CEIC, Emkay Research

Energy security management ahead requires some corrective policy measures

From an energy security and policy perspective, while better preparedness is crucial, what is more important is fairer fuel pricing and taxation.

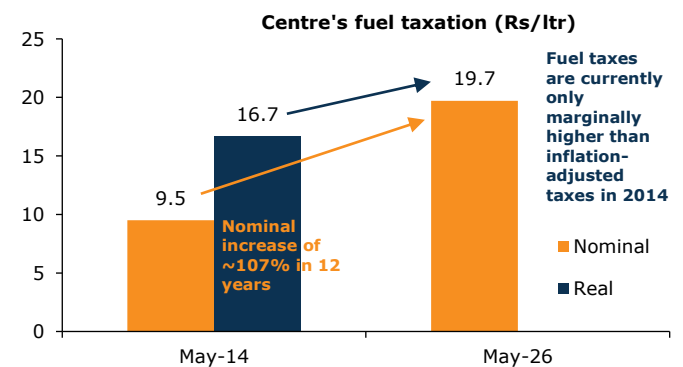
In fact, fuel prices and taxes should be viewed in real (inflation-adjusted) terms, not nominal terms. After adjusting for inflation, petrol prices are lower than in 2014 and the increase in fuel taxation is far smaller than headline numbers suggest. Union fuel taxes are largely specific levies denominated in rupees per ltr, whose real value steadily erodes with inflation. Therefore, nominal increase in the Centre’s levy over the years only shows inflationary adjustments.

Exhibit 29: In real terms, petrol prices are substantially lower than in 2014



Source: CEIC, Emkay Research calculations

Exhibit 30: Taxes on fuel are only marginally higher than in 2014 after adjusting for inflation



Source: CEIC, Emkay Research calculations

Fuel taxes are an energy-security instrument, and fuel consumption imposes socio-economic costs beyond the pump price in the form of air pollution, congestion, carbon emissions and higher import dependence on crude oil. Higher fuel taxes help internalize these costs and reduce excessive oil demand. For an oil-importing country like India, this is effectively an energy-security measure.

Under-taxation of fuel creates long-term disproportionate risks

India remains structurally vulnerable to imported oil. India is under-taxing fuel relative to the economic and environmental costs of oil consumption. This implies current pricing does not sufficiently encourage factors like fuel efficiency, EV adoption, public transport, and more importantly, energy diversification. By keeping fuel prices artificially low, India encourages higher petroleum consumption, which increases exposure to geopolitical shocks, keeps us gullible to oil shocks and worsens external vulnerabilities. Artificially low fuel prices (or even excessive FX management) can encourage higher oil consumption and delay necessary economic adjustment. We reckon a move to higher corrective fuel taxation would likely cause a one-time rise in prices rather than persistent inflation. However, higher fuel tax revenues would strengthen Centre/State finances, reduce dependence on borrowing, and create larger

fiscal buffers against future global and commodity price shocks. The additional revenue space can be used to reallocate resources directly to the vulnerable section of the economy that may see a disproportionate hit from higher taxes.

Net-net, fuel taxes are not merely revenue tools; they help moderate oil demand, improve efficiency, and reduce import dependence. India's energy security, thus, is best strengthened through appropriate price signals rather than price suppression. ([See: India Strategy: Energy security – India's policy options, Mar 2026](#))

Policy imperatives in the medium term

- **Maintain fuel price pass-through** and avoid broad-based fuel subsidies.
- **Use fuel taxation strategically** to encourage efficiency and lower oil intensity, energy security, and fiscal resilience
- **Compensate vulnerable households** directly with higher tax base amid higher energy taxes, while preserving the fuel price signal needed to curb excessive consumption.
- **Accelerate diversification away from oil** through EVs, public transport, renewables, and energy efficiency.
- **Strengthen export competitiveness** to better finance India's large energy import requirements.

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Emkay Rating Distribution

Ratings	Expected Return within the next 12-18 months.
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ADD	5-15% upside
REDUCE	5% upside to 15% downside
SELL	>15% downside

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