

India Macro & Market Note

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India was among the most favoured markets in global finance for much of the past decade, yet it has not delivered over the last two years. The Nifty is roughly flat-to-down over this period — an unremarkable outcome to seasoned practitioners, but a jarring one for the many newer investors who had been promised rich gains from Indian equity. This note sets out my view on why India underperformed, how the macro backdrop has genuinely shifted, what the last quarter tells us about both, and what we should realistically expect from the market over the next five to ten years. It is a considerably less pessimistic view than the one I have argued for over the past few years — though still far from optimistic for those who continue to perpetuate the India-exceptionalism narrative.

This note is best read as an outsider's view. I don't approach markets in the traditional, bottom-up sense. I wear two hats — a macro and policy hat, from my background in rates trading, and a credit-market hat, from what I do for a living today. What follows is simply a different lens on markets — one I have used reliably over the years to compound returns. Decently well.

PART ONE — WHY INDIA DIDN'T DELIVER

1. Two Years of Flat Returns

Corporate profit growth, *ceteris paribus*, comes from four sources: change in fiscal deficit spending, private capex, household dis-saving (leverage), and current account surplus, or net exports. This is the Kalecki profit equation. Run India through 2024-26 on each engine and none of them fired together: fiscal consolidated rather than expanded, private capex never accelerated, household leverage rose but saw both its acceleration and its deceleration inside these same two years, and the current account stayed listless until high oil prices made it worse. In that setup, earnings had no real chance of surprising to the upside — and they didn't.

And if earnings disappoint, investors could still make money if the market was cheap. India wasn't. Nifty traded through most of this period at a premium to its own history and a steep

premium to EM peers, justified — at the time — by ‘quality’ and ‘growth visibility’ narratives. When earnings undershot and the premium didn’t fully unwind, we got the arithmetic result: flat-to-negative returns for two years, dressed up by commentary blaming FII flows, global rates, or China-plus-one delays. The truth is simpler — an investor paid a growth multiple for growth the underlying engines couldn’t produce.

2. The World No Longer Gives India a Growth Premium

India Market cap-to-GDP is at 134% versus a long-term average around 95% — meaningfully elevated. Nifty 1-year forward P/E is at 18x against a long-term average near 16x — a premium, though less extreme than the market-cap read suggests.

The case for India market investors was never ‘India is cheap’ — it was that India offered growth plus capital discipline: rising ROCE, deleveraging balance sheets, promoters behaving. In a world starved of growth, investors were happy to pay up for that combination. Particularly, FIIs.

What’s changed is the growth-scarcity premise itself. I’m watching the US, and now Korea and other East Asian markets, deliver earnings growth that dwarfs anything India can offer, at multiples that are, frankly, cheap. Bankers have revised S&P 500 2026 EPS growth up to roughly 25-30% YoY, with the index trading around 20-21x forward — an acceleration on the back of \$700-750bn of hyperscaler AI capex this year alone. Korea is the more extreme case: KOSPI earnings are forecast to grow around 45-50% in 2026 on the memory-chip supercycle, and the index still trades at roughly 7-8x forward earnings. That is stupendous earnings growth at a reasonable, in Korea’s case almost silly-cheap, multiple. I’m not arguing for buying either market — much of this growth is cyclical and unlikely to sustain — but it makes the point: India isn’t competing to be the growth market right now, because materially better growth prospects exist elsewhere.

This is exactly the frame that killed the ‘bond proxy’ quality-compounder trade (remember BAAP) five or six years ago when rates first started moving — when a market can get real growth cheaply, it stops paying a premium for someone else’s discipline in the absence of growth. India’s ROCE story, capital allocation discipline, promoter governance — genuinely valuable things — were valuable specifically because growth was scarce everywhere and India offered a rare, well-managed sliver of it. **When Korea hands investors 50% earnings growth at under 10x, and the US delivers 30% growth off an AI-capex supercycle at 20x, India’s ‘I grow steadily and I don’t waste capital’ pitch is competing against ‘I grow extraordinarily and you’re not even paying much for it.’**

The case for India isn't dead, but it has to be made on its own terms now — not 'pay up because growth is scarce everywhere else,' because it demonstrably isn't. As I will argue later, if you are looking for some decent risk premium, India will likely deliver that now. So far I am only discussing why India didn't deliver — the next part is about what has actually changed underneath.

3. Growth Is Still 6-7% — Not the Source of the Disappointment

India growth is still tracking 6-7%. FY25's headline 7.1% was flattered by the deflator, not by real momentum. Many of my economist friends argue that real growth is far lower — perhaps close to 5% — though several of them have always leaned bearish. **My only takeaway is that nothing suggests India's growth is accelerating. It is the same old 6-7%. That is not a bad outcome; it is simply that some of the post-Covid bullishness was misplaced. Growth is hard. Acceleration is harder.**

A brief word on how expected GDP growth and equity returns are linked. The obvious channel is that growth drives earnings growth. The more important one is valuation: when the market prices in an acceleration in growth that then fails to arrive, the result is a sustained undershoot in returns. That is arguably what played out over the past two years — the growth economists expected did materialise, but the growth equity investors had priced in did not.

To be fair, Indian growth has held up for a remarkably long stretch since Covid. It never slowed meaningfully, absorbing first the Ukraine shock and, more recently, the Middle East shock. Last year's GST and income-tax cuts helped sustain momentum, but no major stimulus was required — most of the growth was organic. The implication is that we know how to get to 6-7% growth, but not how to get to 8-9%.

PART TWO — HOW THE MACRO IS DIFFERENT NOW

4. A 2013 Moment Without 2013's Causes

In 2013 the rupee crisis had two clean causes: high inflation and a wide, poorly-funded current account deficit. Fix those, and the currency stabilises — which is roughly what happened over the following decade.

Today we don't have those causes, and yet the country is getting the currency stress anyway. Inflation, until this recent oil-driven WPI move, was low by historical standards. The CAD has been comparatively contained over the past three years — genuinely better-behaved than the pre-

2013 period. And yet USD/INR has moved from roughly 82-83 three years ago to about 96 today, a depreciation of roughly 15% over three years, and from around 86 just fifteen months ago (June 2025) to 96 now — roughly 11% in a little over a year. That is not a currency behaving the way a country with low inflation and a contained CAD is supposed to.

2013 was two years of a 4-5% current account deficit. This cycle is two years of a balance-of-payments deficit despite a low CAD — a different imbalance producing the same stress, and drawing the same FCNRB-style policy response, but without the rate hike this time, because inflation wasn't the proximate cause.

The mechanism behind it is capital account, not trade account — which is why the pressure is hitting Asia broadly despite generally good fundamentals. The US equity market has pulled in roughly \$900bn of inflows over the last year; US equity inflows now effectively fund the entirety of the US goods trade deficit, which is why the dollar has stayed flat rather than fallen despite the tariff actions. Korea is the clean proof point: its trade balance has swung from 2% to 9% of GDP on AI-related exports, and the won is still under serious pressure, because capital-account dynamics — equity flooding into the US AI trade — are overwhelming a strong trade position. The CNY is the exception only because China's capital account isn't open the same way. Plus, its just China!

Even starting from this comparatively clean position, the RBI and government still had to run major policy measures — the FCNRB mobilisation, the CAD-narrowing steps. The one saving grace is that these were executed without a rate hike, genuinely better than 2013's playbook. But we shouldn't mistake 'no rate hike' for 'costless.' These interventions carry real costs — they commit forward FX liabilities, they consume reserves optically even when book-managed — and critically, they aren't durably fixing the underlying problem. **That problem, I'd argue, isn't really India-specific anymore: the world has less capital available and less appetite to fund EM current account deficits than it used to, full stop, regardless of how well-behaved the deficit is. It's a supply-of-capital problem sitting on top of India's demand for capital, not solely an India credibility problem. And I'm not arguing that there's suddenly less capital in the world — only that there's a powerful new claimant on it in the hyperscalers and their capex. What they absorb has to come from somewhere.** What one deployment taketh, another must giveth.

The implication I want to sit with: the country will have to learn to grow with a lower CAD tolerance than we've been used to — not because India's fundamentals demand it, but because the world simply won't fund the CAD levels we ran comfortably in the past. That means a structurally higher real rates than the pre-GFC-unwind era gave us, which mechanically means a lower growth impulse than trend GDP numbers alone would suggest. It is precisely in this context that RBI's

hands are tied on the loosening side: cutting rates into a currency already under this kind of structural pressure, with WPI elevated on sticky oil, is not something the central bank can responsibly do right now, however much the domestic slowdown might otherwise argue for easing.

5. The US Real Rate Has Genuinely Re-Rated

The US 10-year TIPS yield — the cleanest read on the real, inflation-adjusted cost of long-duration capital — is around 2.4% as of late July 2026. The nominal 10-year is trading near 4.7-4.75%, a 19-month high. Back out the difference and the 10-year breakeven inflation rate is roughly 2.3% — close to normal, not blown out. That arithmetic is the whole point: if inflation expectations haven't moved much, and the nominal yield has risen sharply, the real rate is doing almost all the work.

This matters enormously in context. For most of the post-GFC decade, the US 10-year real yield ran negative or barely positive — it hovered around -1% for much of 2013-2017, and dived to roughly -2% in 2020. A real rate near 2.4% today isn't a return to some extreme historical high; it's closer to the pre-2008 historical norm than to anything market got used to in the 2010s zero-rate world. **The post-GFC 'low-for-long,' negative-real-rate regime that every valuation model, every DCF, every TINA equity argument was built on for fifteen years is over. What market is reverting to is arguably the more historically normal regime of positive, meaningful real rates.**

Why has this happened without a commensurate inflation move? I think it's a term-premium and capital-demand story, not a Fed-credibility-on-inflation story: massive AI-driven private capex issuance, structural US fiscal deficits that persist even in non-recession years, and a market simply demanding more compensation for holding long-duration government paper given how much competing demand for capital exists elsewhere in the economy. That's the mechanism, not inflation fear per se — which is exactly why it shows up as a real-rate move rather than a breakeven move.

This recycling also differs from the 2000s global-imbalances era in a way that matters for yields. Then, Asian central banks recycled trade surpluses into US Treasuries — official-sector recycling that mechanically held bond yields down. Today the recycling is private-sector and runs through equity rather than bonds, which is part of why yields haven't fallen the way one would otherwise expect. On the supply side, hyperscalers' bond issuance has scaled dramatically (\$200-250bn — a genuinely new, large slug of private, non-government paper competing for the same capital.

If the global risk-free real rate has structurally reset higher, every risk asset's required return resets higher with it, independent of anything happening domestically in India. And this compounds directly with the currency and CAD-funding argument above: a world with higher real rates is a world with less patience for funding EM current account deficits on easy terms.

It's also worth remembering how India handled a world of high real rates the last time it faced one. We ran financial repression. You couldn't take money out of the country. Banks were compelled to hold government bonds, giving the sovereign a captive source of cheap funding. Imports were hemmed in by tariffs and licensing. Over the past two decades much of that apparatus was dismantled, bit by bit — the capital account opened up, the Liberalised Remittance Scheme (LRS) window widened, trade barriers came down. **But liberalisation only runs one way until the cost of capital forces a rethink, and I'd argue that rethink is now beginning. The pendulum starts to swing back. Taking money out of the country will get harder, not easier.** How can a country keep widening the LRS window while it's borrowing expensive money from the rest of the world? Something has to give.

6. America's Tribute System Doctrine

Sitting on top of the real-rate story is a second US-centred force worth naming explicitly. Washington is increasingly monetising its structural leverage — market access, dollar centrality, technology, security guarantees — as explicit bargaining chips rather than public goods extended for free. I'd call this America's tribute system doctrine. **If Trump's overtures and threats-by-tweet have puzzled you, this is the frame that makes sense of them. They aren't noise; they're the operating logic of a new mercantilism in which the superpower charges rent for services it once extended as a matter of course. Nothing comes for free anymore.** You can't take US security or open markets as a given — there's no ideological backstop, no benefit of the doubt. Everything has a price. This is a genuinely different world from the one we grew up investing in, and it's tempting to wave it away as commentary rather than something that moves markets. It isn't. The rent is real, and it is ultimately paid in growth — every dollar of tribute extracted is a dollar that doesn't compound in the real economy.

And what happens if you don't pay the tribute? They can make refusal expensive — pull back from a security arrangement, slap tariffs on you, choke the supply of essential commodities, sever an undersea cable or two. Whatever a rogue superpower can do to raise the cost of non-compliance, it will. So in practice you don't have much of a choice. And if you're tempted to think we aren't already paying, look again at the conflicts underway — the tariff war included. That is the tribute, being collected as you read this!

The risk isn't the policy itself; it's temporal. Every time this leverage gets used as a lever, it reveals exactly where the leverage lives and how much of it can be extracted before the counterparty routes around it. That's not a one-time repricing, it's an ongoing one.

For a market like India that depends on foreign capital goodwill to fund even a comparatively well-behaved CAD, this is a genuine, hard-to-model source of episodic shock — tariff actions, capital-flow restrictions, security-linked conditions — layered on top of everything else.

That said, India is better positioned on this front than almost any country outside China and Russia. Our scale, our domestic market and our relative self-sufficiency mean we can largely look after ourselves — an option most emerging economies simply don't have. But better positioned is not the same as exempt. It only lowers the size of the tribute we owe; it doesn't waive it. We still pay — just a little less.

7. Political Power Transition

Power transfer periods are, almost by definition, volatile — factions jockey, policy continuity weakens, institutional guardrails get tested. India has had an unusually peaceful run for 12 years now. I'm not predicting a major turnover of power. I'm saying that, directionally and slowly, I think the country is heading toward a messier power structure than what we've gotten used to. That transition — whenever and however it plays out — is the kind of regime change that lowers the risk premium investors are willing to extend, induces more volatility in policy and markets both, and is more prone to deliver inflation, because messier politics generally means less fiscal discipline and more populist spending as competing factions try to buy legitimacy.

I think most people get Modi's actual win wrong. The popular narrative credits him with growth — a great infra boom, a great profit boom, a step-change in India's development trajectory. The data doesn't support that: India's per capita income (PPP) grew at 4.8% real CAGR over 2015-25 versus 4.95% for 2000-25 — the 'decisive government' decade actually delivered more or less the same growth as the past quarter century. **What he actually delivered — and I think this is underappreciated precisely because it's boring and doesn't show up in a GDP print — is macro stability.**

The country sat through a CAD and currency setup this cycle that in many ways mirrored 2013 — and it did not get a 2013. When we had to run the FCNRB exercise this cycle, we did it without a rate hike, unlike the blunt tools used last time. When oil spiked, domestic inflation didn't spiral the way it has in past oil shocks. During Covid, when the West went through a major inflation shock, India's inflation stayed comparatively calm. And the clearest, most measurable proof of this stability dividend: India's interest rate differential versus the US is lower today than it has

historically been — a direct market verdict that India is perceived as a materially more stable, better-managed macro economy than it used to be.

So here's the point I actually want to sit with: Modi's real legacy is a macro-stability premium, not a growth premium. And a messier power transition — which I think is where the country is headed, gradually — is precisely the kind of event that erodes a stability premium, not a growth premium. If the next phase of Indian politics is noisier, more factional, less disciplined, the risk isn't that trend growth suddenly falls. The risk is that the stability dividend — the thing that's actually kept India's rate differential low and kept us out of a 2013-style crisis this cycle — starts to erode.

8. The AI Trade

Broadly speaking, AI/LLMs winning is India losing, via two channels: labour arbitrage (the core value proposition of Indian IT for three decades), and global disinterest, as capital and attention rotate to frontier AI infrastructure and away from labour-arbitrage geographies. The central question is whether AI is labour substitution or labour acceleration. I think it's substitution.

Separate from the India point, this is also, broadly, an incumbent-losing trade globally. This is how tech has always worked: it transfers profit pools from incumbents to whoever sits at the frontier, not to whoever had the biggest distribution yesterday. Watch what happened to media — the profit pool didn't stay with publishers, it transferred to Google. The same mechanism will play out again, and geographies and sectors that were incumbents in the old profit pool — which includes chunks of India's services economy — need to ask honestly whether they're the Google of this cycle or the newspaper. I expect major losers among incumbents in BFSI and other services businesses. Much of the workflow will be automated, and a new set of players will win handsomely, even as the incumbents struggle to embrace the new technology.

So what is India's actual AI trade? It would be unfair, and frankly delusional, to expect India to build a frontier model. India's AI trade is the picks-and-shovels and application layer: data centre build-out, energy (data centres are fundamentally an energy story before they're a compute story), GCCs, infrastructure components, and the application layer sitting on top of frontier models built elsewhere. India is genuinely good at this layer — GCC work is a real, durable competency.

9. India Is a Dual-Engine Economy, Inside a Deglobalizing World

India runs on two engines simultaneously. A frontier economy sits on top of a backward one. Urban infrastructure genuinely sucks.. And yet India excels at GCC work, defence manufacturing,

IT services, banking, and financial services. It's decent at core manufacturing, and weak at value-add manufacturing. This duality means the standard bull-bear binary doesn't apply: I can't be too pessimistic, because the frontier engine is real and growing. I can't be too bullish, because the backward engine is the base the frontier engine sits on, and it isn't closing the gap fast.

On manufacturing specifically, the direction of travel is wrong, contrary to the China-plus-one narrative. Machinery and industrial-equipment imports from China have sharply accelerated over the last six quarters. Historically, that kind of import surge went hand in hand with a genuine domestic capex cycle taking hold; here it looks more like deepening import dependence than manufacturing capability being built. India's FTA history is a cautionary data point for the friend-shoring thesis more broadly: the FTAs signed with Korea, ASEAN, and Japan over 2007-2011 didn't meaningfully improve India's export performance, but import growth from those partners exploded. That's a real vulnerability — India runs a consumption-economy model that global producers can access without having to build reciprocal export capacity of their own.

Layered on top of this is the global polity setup. The great globalisation trade is off the table, and I don't think this reverses in this cycle. The US, as global policeman, is disinterested in the role it played for three-plus decades. The most likely outcome from here is 'many wars forever' rather than any single decisive conflict — regional, persistent, unresolved frictions rather than Cold-War-style bipolar stability, with each nation increasingly on its own. Supply chains stay disturbed, semi-permanently, not as a transitory post-Covid hangover. **The rational response to that world is everyone building larger reserves of everything — commodities, semiconductors, food, currency reserves, energy. From a pure markets standpoint, that's an inferior outcome: redundancy and reserve-building are a tax on global efficiency and capital returns, not a source of growth.**

PART THREE — LAST QUARTER

10. Q1FY27: Has the Tide Turned?

Some genuinely good news arrived last quarter. BSE500 (ex-OMCs) posted 22% YoY PAT growth in Q1FY27 — a three-year high, comfortably ahead of estimates. But a large part of it is one-off: low base, INR depreciation, high commodity prices, and the FY26 consumption stimulus (GST cuts, RBI's regulatory and rate easing). Metals and energy topline surged on a supply shock and an AI-capex-driven commodity spike, not domestic demand. Auto and durables growth was substantially base-effect. Chemicals and IT benefited from currency depreciation lifting INR-denominated revenue, not real volume acceleration. Strip these one-offs out and the outcome is lot less rosier.

It's worth isolating how much of this quarter's topline was simply the rupee. INR depreciation is contributing roughly 8-10 percentage points to reported topline growth, so in constant-currency terms topline grew only around 10-11%. That currency contribution collapses toward zero in H2 if the rupee holds flat near 96. On profits, about half the pool is dollar-linked — chemicals, pharma, IT, metals — so currency-neutral profit growth is probably 10-12%, maybe a touch better once inventory-gain effects fully play through in Q2. SMIDs are far less dollar-exposed, so this FX flattery doesn't apply to them the same way.

Tailwinds fade from H2FY27, while the headwinds — weak household incomes, a subdued credit multiplier, El Niño risk to farm incomes, general government tax revenue growth stuck near a decade-low ~8% — persist. Consensus is still underwriting mid-teens Nifty EPS growth for FY27E and FY28E. Margins have nowhere further to expand in most pockets, so the risk into H2FY27 is asymmetric to the downside. Big picture, there is very little space for a positive surprise on margins — though it's not very unlikely that markets simply get what they are already baking in.

Investors should keep a few points in mind. First, an input-price lag: companies ran on low-cost inventory this quarter and booked inventory gains, and that cushion is exhausted by next quarter. Second, the price hikes already taken (paints etc) may start denting volumes in H2. Third, the normalisation of MFI and unsecured-NBFC credit costs was a one-time base-effect tailwind to profit growth, not a repeatable one.

Small and Midcap firm beat is almost entirely margin-driven: the AI-capex-proxy industrial segments (cables and wires, transformers, T&D) firing hard, plus a handful of previously loss-making companies swinging into profit. Why hasn't the 'margins are elevated and must roll over' call played out yet? I predicted exactly that, and it never came.

Banking deserves a specific note, because its topline weakness is a competitive-intensity problem, not a growth problem. Credit growth is running 18-19%, but NII-plus-other-income growth is only around 10% — margins compressed by intense competition, with PSU banks in particular aggressive in gold loans and housing, a symptom of 'too good a balance sheet' pushing into price competition.

One hard data point worth flagging on its own — as it really matters for growth prospects: listed real-estate companies' pre-sales have gone into contraction on a trend basis for the first time ever. This basically suggests that the household leverage cycle isn't backed up by asset creation — a bad kind of leverage that RBI will not be comfortable with. I think regulatory tightening in the personal loan segment, particularly for high-APR NBFC lending, is coming. Soon.

So, Q1FY27 was a beat — driven by currency, commodities, and a stimulus-and-base-effect combination that mechanically cannot repeat. But a beat is a beat. We all have a habit of

dismissing numbers like these, without realising that even one-off beats, if sustained for two or three quarters, tend to grow roots and can become the start of a trend.

Which brings me to the part everyone actually wants to know: what does all of this mean for what I should expect the market to return.

PART FOUR — RETURNS FOR THE NEXT FIVE TO TEN YEARS

11. Putting a Number on It

So what does all of this actually mean for returns? My honest answer is a low double-digit number, something like 10-12%. That's not as pessimistic a stance as I held for the past couple of years, but I can't be too optimistic either, for all the reasons above. Against a 7% bond, that's an excess return of roughly 4% — a little weaker than the market's historic spread, but not dramatically so.

Almost all of that 10-12% now has to be earned, not re-rated into. If earnings compound at the honest low-teens pace I've argued for — not the mid-teens consensus is underwriting — and the multiple does nothing, that plus a dividend-and-buyback yield of roughly 1.5% gets me to the low-double-digit number. The catch is the multiple probably doesn't do nothing: the growth-scarcity premium that carried the last decade is eroding, so if anything I'd budget for a mild de-rating drag rather than a re-rating tailwind. The decade where multiple expansion did a lot of the work of returns is behind me; from here the index earns its return the hard way, through profits and payout.

And that's the rupee return. For the dollar investor I'm competing with for capital, strip out even a normalised 2-3% a year of rupee drift, and 10-12% becomes high single-digits in USD — which is precisely why the foreign bid has gone missing, and why the marginal buyer of Indian equities is now domestic. That is the quiet, important fact underneath the last two years: the SIP-fed savings surplus absorbed a record ~\$29bn of foreign selling and the market still didn't break. **The un-levered domestic saver is the floor under this market now, not the foreign allocator — and an un-levered floor is a far sturdier one than the leveraged bids that have broken other markets before.**

Whether investors have fully internalised the message of lower expected returns, I'm not entirely sure. But the past two years have been a good teacher, and the fact that the industry absorbed such a poor stretch of returns without major disappointment or redemption pressure tells me the underlying savings pool is real and un-levered — which is itself a good outcome.

I'd hold 10-12% as a base case with an honestly asymmetric distribution around it. The left tail is fatter than the right: a messier political transition eroding the macro-stability premium, global real rates staying higher for longer, an AI cycle that is structurally India-losing, and a world of reserve-building and 'many wars forever' that taxes returns everywhere. The right tail — global AI capex broadening out and pulling India's exports with it — is real but low-probability on today's evidence. The central number is fair, but I'd underwrite it knowing the surprises are, for now, more likely to disappoint than to delight. **So why not simply avoid equity altogether? Because we as fund managers are not trained to think in terms of avoid — we think in overweight, neutral, and underweight. For a good while I argued that equity was an underweight against assets like credit, and that call has largely played out: credit has compounded handsomely while equity has gone nowhere. But that is precisely why I am now changing my mind at the margin. With the underperformance behind us and some of the excess valuation worked off, the argument for staying underweight has thinned considerably. On the evidence today, it is fair to upgrade equity to at least neutral.**

This is my view. Not of my firm. This is not even advice. General speculations.