

Indian equities: improving outlook

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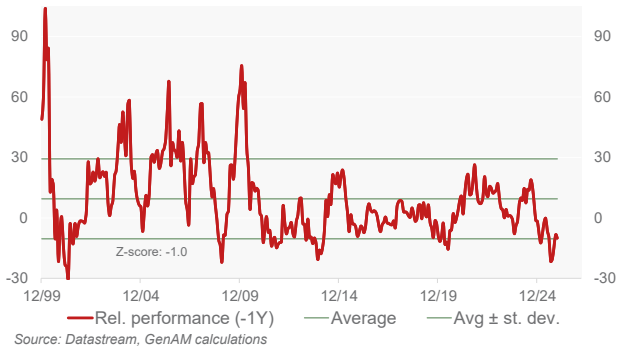
Our Focal Point series explores topical issues on macro, markets and investment

- Indian equities underperformed globally, rising only 6.5% YTD versus 26% for EMs and 17.5% for US and MSCI EMU. In year-on-year terms, returns lag historical averages by 1 standard deviation versus MSCI World and nearly two versus MSCI EM.
- This disappointing performance stems from 1) global trade and tariff tensions, including largest U.S. tariffs in the region impacting exporters, 2) domestic economic weakness, and 3) geopolitical uncertainty (Middle East conflicts, India-Pakistan frictions).
- Indian GDP has recently surprised on the upside and should accelerate in 2026, supported by stronger domestic demand, monetary easing, and reforms. Risks remain primarily external. Inflation is near a 50-year low; downside risks remain, and the RBI is likely to maintain accommodative stance despite nearing end of easing cycle.
- We have started to observe early signs pointing to a rebound in earnings as pro-growth measures - income tax relief, Goods and Services Tax (GST) rationalisation, and a recent 25 bps rate cut to 5.25% - begin to take effect.
- Positioning is supportive. India's equity markets experienced large foreigner outflows — US \$ 17 bn YTD, comparable to 2022 when global MSCI EM fell by 22%. We expect renewed inflows as the macro and earnings outlook improves.
- We are overweight on Indian equities, as accelerating GDP growth, supportive monetary and fiscal policies, and improving earnings momentum are expected to drive stronger market performance after recent underperformance.

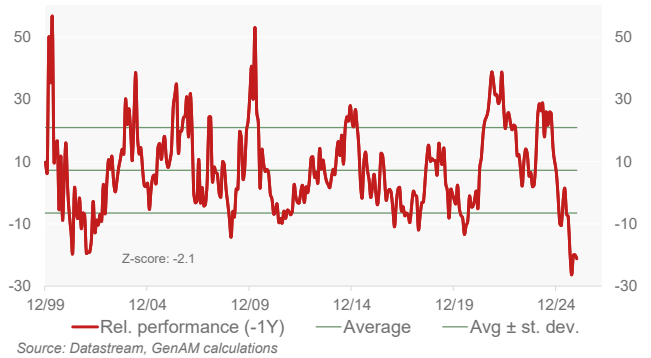
Year-to-date, Indian equities have delivered a modest 6.5% gain, **significantly trailing global benchmarks**. EM equities surged 26%, while U.S. equities and MSCI EMU advanced by an average of 17.5%, underscoring India's relative weakness. In particular, since end of June, the MSCI India has barely gained. The Indian market has recorded its worst year of underperformance versus EMs in three decades: the average annual relative underperformance since 1995 is -8pp. On a year-on-year basis, the Indian market performance stands one standard deviation below its historical average compared to MSCI World and nearly two standard deviations behind MSCI EM.

This lacklustre performance reflected a confluence of headwinds reducing its high valuation premium based on price/earnings and CAPE: 1) global trade and tariff tensions, including the largest U.S. tariffs in the region, weighing on exporters. 2) Domestic economic softness, dampening investor sentiment. 3) Geopolitical uncertainty, from Middle East conflicts to India-Pakistan frictions, adding to risk aversion.

Delta in yoy price change: INDIA vs WORLD



Delta in yoy price change: INDIA vs EM

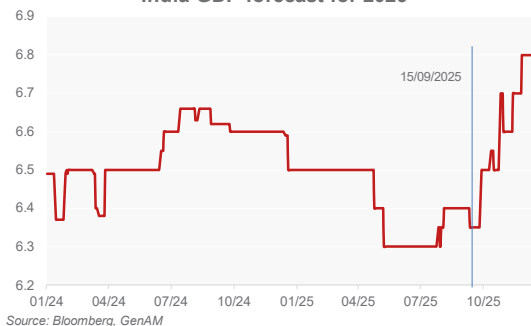


Since June 2024, analysts have drastically reduced earnings expectations for the MSCI India: by 12% for 2025 and by 10% for 2026. That said, India is characterised by highest past and projected GDP growth globally, with the expected 2026 growth differential vs EM and the world at 2.3pp and 3.7pp, respectively.

Improving macroeconomic backdrop

In a cyclical macro sweet spot. India’s economic backdrop has been improving recently after early-2025 disappointments. The country is experiencing a combination of growth acceleration, inflation at twenty-year lows, and supportive monetary policy, and new regulatory reforms. Punitive US tariffs of 50% are weighing on the Indian economy, but we some relief via a deal with the US in 2026 seems likely as negotiations progress. This environment should have a positive impact on future corporate revenues and, consequently, on upcoming earnings, which would put an end to the earnings downgrade cycle that began in July 2024.

India GDP forecast for 2026



Declining inflationary pressures



Growth re-acceleration. Growth has accelerated recently, highlighted by a surprise Q3 GDP print at 8.2%, and further momentum is expected. Consensus for GDP growth

in FY26 now stands at 6.8%. A broad-based pickup across domestic indicators is evident, including agricultural and industrial production, auto sales, and credit growth. Domestic demand is benefiting from a milder monsoon and regulatory easing. For instance, several GST (goods and services tax) cuts totalling nearly R1.5 trn (skewed towards mass consumption) have supported discretionary demand. Upcoming light-touch regulatory reforms (e.g., 8th Pay Commission) may further boost demand in autos and consumer durables. Based on the latest election results, the NDA (National Democratic Alliance) has significant political space to accelerate its reform agenda, focusing on bank deregulation and privatisation.

Supportive monetary policy. Inflation has been on a sharp downward trend, reaching a new low of 0.3% y/y. Core inflation has also weakened, impacted by the monsoon and imported Chinese disinflationary forces. Inflation is now more than 100bp below the latest RBI forecast and the official target of 4% ±2%, leaving room for a final rate cut in early 2026. The next rate hikes are likely only in FY27–28.

Neutral fiscal policy with some risks of easing. India has room to meet its fiscal deficit target of 4.4% of GDP in FY 2026. Recent trends show a contained deficit versus historical norms, though weaker tax receipts pose a risk of marginal fiscal slippage. The Union Budget in February 2026 could reaffirm India’s path towards a balanced primary fiscal position. For FY27, the fiscal anchor shifts from deficit/GDP to debt/GDP, with the government aiming for a debt-to-GDP ratio of 56%. This target appears achievable amid stronger nominal GDP growth next year, without requiring a deficit reduction.

Emerging evidence of earnings turnaround

Overall, India’s macroeconomic landscape looks supportive for earnings. There are early signs pointing to a rebound in earnings as pro-growth measures - income tax relief, GST rationalisation, and a recent 25 bps rate cut to 5.25% - begin to take effect.

Thus, in the Q3 reporting season, yoy growth in profits for Nifty 100 (top 100 companies listed on the NSE) increased from 19.7% in Q2 to 27% - with only Financials showing slightly negative yoy growth at -5.5%. The earnings beat for the index was significantly above the average over the last nine quarters (16.2% vs 1.0%). For the top 50 companies (Nifty 50), earnings growth increased from 9.7% in Q2 to 47% in Q3, with earnings surprise surging to 44.3% vs 2.8% in Q2 and 5.9% over the past nine quarters. The median stock has also shown overall improvement both in terms of growth and surprise, even though to a lesser extent for top50 than for top100.

Sector	100 reported		100 reported		margin trend *	
	earnings growth, yoy		sales growth, yoy		margin trend *	
	Q2 2025	Q3 2025	Q2 2025	Q3 2025	Q2 2025	Q3 2025
Energy	19.7%	144.9%	-2.8%	11.1%	23%	134%
Materials	-2.5%	61.9%	11.1%	12.4%	-14%	49%
Industrials	70.5%	61.0%	13.7%	17.1%	57%	44%
Consumer Discretionary	27.7%	25.5%	22.6%	19.6%	5%	6%
Consumer Staples	12.1%	11.3%	16.4%	14.6%	-4%	-3%
Health Care	13.0%	28.8%	12.3%	23.3%	1%	6%
Financials	117.2%	-5.5%	9.1%	2.6%	108%	-8%
Information Technology	-5.5%	13.7%	16.8%	25.0%	-22%	-11%
Communication Services	16.9%	32.7%	6.6%	5.9%	10%	27%
Utilities	19.7%	19.4%	6.2%	9.7%	13%	10%
Real Estate	59.2%	33.9%	11.1%	12.4%	48%	21%
Market	19.7%	26.7%	-2.8%	12.1%	23%	15%
Median (all sectors)	16.9%	28.8%	11.1%	12.4%	6%	16%
Median, ex. Energy	18.3%	27.1%	11.7%	13.5%	6.6%	13.6%
Median, ex. Energy & Materials	19.7%	25.5%	12.3%	14.6%	7.5%	10.9%
Median, ex. Financials	18.3%	30.8%	11.7%	13.5%	6.6%	17.2%

Source: Bloomberg, GenAM calculations
Note: proxy for margin trend = earnings growth - sales growth

Analysis of the median stock

Index	Earnings Growth		Sales Growth		margin trend *	
	Q2 2025	Q3 2025	Q2 2025	Q3 2025	Q2 2025	Q3 2025
	Nifty 50	9.6 %	10.9 %	9.7 %	10.4 %	(0.0)%
Nifty 100	16.1 %	19.1 %	10.1 %	10.3 %	6.0 %	8.9 %

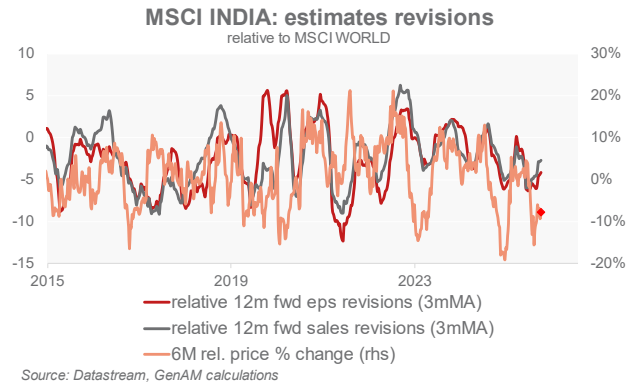
Index	Earnings Surpr		Sales Surpr		margin trend *	
	Q2 2025	Q3 2025	Q2 2025	Q3 2025	Q2 2025	Q3 2025
	Nifty 50	0.1 %	1.3 %	1.3 %	0.7 %	(1.2)%
Nifty 100	0.7 %	3.7 %	0.3 %	1.7 %	0.5 %	2.0 %

* For India, the financial year ends in March

Note: numbers for Q2 are calculated only for the companies which have so far reported in Q3
proxy for margin trend = earnings growth - sales growth

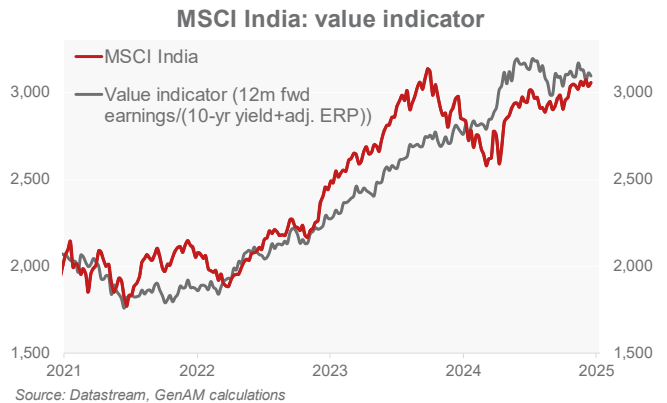
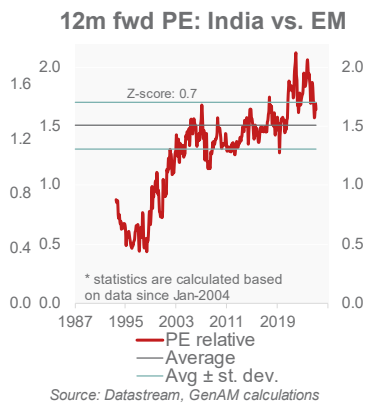
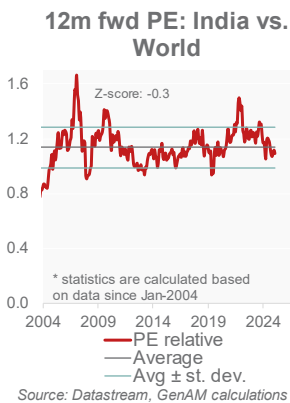
Source: Bloomberg, GenAM calculations

Twelve-month forward earnings expectations have already started to increase for one month, while the price has not fully kept pace. In relative terms, the six-month relative price change follows relatively closely the relative 12-month forward earnings and sales revisions (which are smoothed using a three-month moving average to reduce short-term volatility in estimates). While the relative price has already started to react to the improvement in relative revisions, the positive gap is still far from being closed.



Rich valuations to be underpinned by strengthening EPS growth breadth

The 12-month forward PE of the Indian market, though off its extremes, is still rich: the MSCI India trades at around 22x – slightly below that of the S&P500 but above most of other markets. Relative to MSCI World, it is just 0.3 standard deviations below its historical average since 2004 and 0.7 standard deviations above the MSCI EM. India’s higher current PE is, however, justified by a structurally higher earnings outlook: as the fastest-growing major economy globally, it offers a longer runway for profit growth than most EMs. That growth backdrop — combined with the RBI’s recent policy easing amid declining inflation — reduces risk aversion and improves sentiment, possibly supporting higher valuations. Furthermore, MSCI India includes large private banks, leading consumer brands, and tech services that typically command premium multiples. Lastly, India’s rising weight in the MSCI EM index (e.g., an increase to ~16% in October 2025 from 8% in 2015) also channels passive flows toward these higher-quality names, further underpinning valuations.



In terms of market multiples (PE, PB, PCF, and DY) since 2004, Indian stocks trade at a premium of 22% vs their history, compared with 48% for the US, 22% for MSCI EMU, and 18% for MSCI EM. The PEG ratio (PE divided by long-term earnings growth) for the MSCI India is at 1.3, in line with MSCI EMU and the S&P 500 (1.2), although higher than MSCI EM at 0.7 (dominated by China and Korea, both are OW as well). Over the short-term, the MSCI India is supported by its value indicator (12-month forward earnings divided by 10-year government yield). The better economic trend should reinforce earnings recovery, enhance the breadth of EPS growth, and provide additional support for multiples.

Index	2024 EPS growth	2025 EPS growth	2026 EPS growth	EPS Long-Term growth	12m fwd PE	Avg 12m fwd PE since 1995	% diff	Avg PEG FY3
S&P500	10%	13%	14%	18%	22.4	17.0	32%	1.2
MSCI EMU	0%	-2%	15%	12%	14.7	14.4	2%	1.3
Russell 2000	12%	39%	58%	15%	25.4	22.7	12%	0.9
MDAX	15%	-6%	27%	8%	14.1	15.4	-9%	1.2
MSCI India	6%	12%	17%	15%	22.4	15.8	42%	1.3
MSCI Korea	91%	31%	38%	25%	10.2	10.1	0%	0.4
Japan (TOPIX)	12%	5%	11%	13%	15.6	15.0	4%	1.4
MSCI EM	21%	12%	17%	18%	13.3	12.0	11%	0.7
MSCI China	14%	3%	13%	9%	12.7	12.0	5%	1.1
MSCI China IT	-33%	68%	36%	35%	23.0	20.4	13%	0.4

EPS growths are based on calendar years. EPS long-term growth refers to next 3 - 5 years eps growth. Avg PEG FY3 = avg PE using FY3 EPS over 3-5y EPS growth and over FY3-FY0 EPS CAGR. Topix avg 12m fwd PE is from 2003.
Source: LSEG Datastream, GenAM Calculations. Estimates are IBES.

The India–US tariff wild card

The US has imposed a 50% tariff rate, leaving India with one of the highest effective rates at 34%, with no backpedalling so far. Economic activity has coped relatively well: India’s exports to the US are down 25% cumulatively, but exporters have redirected shipments elsewhere. There is a strong likelihood of tariff reductions following signs of warming relations with the US (e.g., the 10-year defence framework agreement). Bilateral arrangements are under discussion and could eventually result in an overall tariff of ca. 15%, similar to other Asian economies. India has complied with US demands to reduce Russian oil purchases. Timing remains uncertain, but President Trump indicated in November that tariffs would be lowered. A realistic scenario would be easing in Q1 2026.

India’s equity markets experienced large foreigner outflows — US \$ 17 bn YTD, comparable to 2022 when global MSCI EM fell by 22%. This leaves leeway for renewed inflows as the macro and earnings outlook improves.

Conclusion

We are overweight on Indian equities, as accelerating GDP growth, supportive monetary and fiscal policies, and improving earnings momentum are expected to drive stronger market performance after recent underperformance. Among the risks we see mainly external factors stemming from adverse global growth, tariffs, and geopolitical tensions.

 **IMPRINT**

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