ASK Hedge Solutions

The Reform Foundation Is Set, Time to Build Growth.

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Wishing you a very Happy New Year. It's the time of the year when we pencil in our thoughts on important aspects of markets and what we expect for economy and markets.

Global Overview

In 2025, global central banks transitioned to monetary easing, reversing the tightening cycle observed in the preceding years. Major developed economies and the Reserve Bank of India reduced interest rates to their lowest levels since July 2022. Conversely, Japan among developed markets and Brazil within emerging markets, increased their policy rates to address inflationary pressures. In addition to rate reductions, central banks maintained supportive liquidity conditions. Looking ahead to 2026, we anticipate the current easing cycle will conclude, with many central banks signalling a slower pace of future rate cuts or potential pauses.

Bond yields remained elevated despite the rate cuts, as markets expected inflation to rise due to the imposition of tariffs. We foresee bond yields continuing at higher levels until tariff negotiations progress or there is a pronounced economic downturn, though the latter is not our base case scenario.

Key investment themes in 2025 included artificial intelligence and precious metals. Markets such as the United States, Korea and Taiwan saw upward movement led by AI-related stocks, and U.S. GDP growth exceeded expectations largely due to AI-driven capital expenditures. However, India did not participate in this trend to a significant extent.

We expect AI-related investments to persist into 2026, however investors should monitor whether these investments are effectively monetised and assess if valuations have reached their peak in the near to medium term. Broad adoption of AI by IT services would be beneficial for India.

Additionally, a weaker U.S. dollar and the ongoing de-dollarisation contributed to exceptional returns in precious metals, as central banks globally increased gold reserves. We anticipate that precious metals will remain resilient, with the de-dollarisation theme likely to continue through 2026 till we see evidence of trade deals with China and India.

India Macros

India remains fastest growing economy in the world, however what was concerning was the slowing corporate revenue growth, weak nominal GDP growth and the cut in EPS estimates for broader market. Both central bank and Government taking note of the same announced series of fiscal and monetary measures.

Government's demand-side measures from 2025 (Income tax cuts and GST rationalisation) which are projected to boost discretionary consumption going forward. Liquidity strain at the bottom of the pyramid due to asset quality issue in low ticket personal loans and MFI is now bottoming out. We expect fiscal stimulus to continue with Eighth Pay Commission announcement and increase in minimum wages. This makes us constructive on consumer discretionary space. Though there was a fiscal stimulus, the government intends to keep fiscal deficit under check.

Monetary Policy:

An accommodative stance is expected to persist, although rate cuts are expected to end in the first half of 2026. Unless we have tariff negotiations with the U.S. (tariff below 15%), liquidity support will continue from the RBI. Regulatory tightening which we noticed in 2024 and first half of 2025, has now been highly accommodative which is a positive for growth.

Corporate Performance:

Earnings downgrade cycle continued in 2025 and market is staring at a single digit earning growth versus the earlier expectation of low double-digit growth. Going forward, we see reasonable earnings expectations and valuations, supported by early signs of recovery in the earnings cycle. While minor downward revisions are possible, double-digit earnings growth remains likely.

Balance Sheets:

Corporate balance sheet remains healthy while households have seen increase in leverage especially in the lower income category. Now seeing that the household leverage issue is largely behind, we may see consumption improving.

Flows to Improve:

Despite record IPOs/OFS and FII outflows, India market flows were largely supported by financialization of domestic savings. 2026 is estimated to have higher IPO pipeline than 2025 which is likely to make India market broad based and indicates an appetite for good quality corporates.

Considering the India premium to global markets correcting to average levels and earnings cycle bottoming out, we expect FII outflows to ebb. FII flows may turn positive in case there is a fatigue in the AI trade, though there is evidence of initial signs it is not conclusive enough. We expect AI theme to have some more legs to go. This may lead to better than earnings growth return from the India market .

Diplomacy and Economics:

While the U.S.- India trade spat is in the spotlight, it is difficult to assign any timeline for a resolution. However, in 2025 India signed 3 major trade pacts: FTA/CETA with UK, the CEPA with Oman and the FTA with New Zealand and expanded the total FTA's network to around 16-18 agreements. This will provide trade diversification and will lower reliance on one economy.

INR was one of the weakest currencies and the sharp depreciation in 2025 was mainly due to heavy FII selling in India equities and bonds, a widening trade deficit and an uncertainty over a potential India-U.S. trade deal.

Key Themes to Watch for

- **Pause on easing interest rate cycle:** This will be positive for banks earnings.

- **Data centre and energy:** We believe data centre investment to increase, and this will lead to increase in energy requirement. Hence, power sector, chilling machines, as well as EPC companies could be the initial beneficiaries.

- **Fatigue AI trade**: While AI investment is expected to continue but given the current valuations, we believe investors will look for alternate trade in 2026 which will make India an attractive destination.

Outlook 2026

The macro environment remains conducive for sustained economic and market growth, underpinned by policy support, improving fundamentals, and stable political conditions, though continued monitoring of policy shifts and election outcomes is advised. Continued fiscal and monetary measures globally are set to underpin growth, while positive developments in trade agreements may bolster the Indian Rupee and support liquidity. Reform foundation is set, now it is time to deliver on growth which could be back-ended.

We expect broad market to deliver low double digit return in CY26 which should be in line with earnings growth. Financials and Consumer discretionary are expected to outperform markets. We are turning neutral on IT services considering the correction in valuation in the last 12 months.
