



SKG
INVESTMENTS & ADVISORY

2026 : Outlook

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Intro & Key Drivers

Indian equity markets enter 2026 after a year of consolidation and structural reset, setting the stage for a more earnings and fundamentals driven cycle. The prior year was characterised by resilient macro stability but uneven market participation, with leadership narrowing to large caps and quality franchises, while mid and small caps underwent valuation compression. This backdrop is important because it lowers excesses and improves the risk reward setup for 2026, provided earnings recovery broadens beyond a few sectors

Key Drivers For CY2026

1. Strong Macro Growth Differential

India remains the fastest growing major economy, with real GDP growth expected in the ~7% range, providing a stable topline environment for corporate earnings and sustaining investor confidence

2. Disinflation Creating Policy Space

Sharp moderation in CPI inflation through late 2025 created room for monetary easing, reducing the macro risk premium and improving equity valuation comfort via lower discount rates

3. Monetary Easing and Liquidity Support

A cumulative 125 bps policy rate cut, combined with proactive liquidity operations, has eased financial conditions, supported credit growth and improved transmission to rate-sensitive sectors.

4. Fiscal Discipline with Capex Continuity

Adherence to the fiscal deficit glide path alongside sustained public capex has preserved macro credibility while supporting infrastructure, manufacturing and investment linked sectors.

5. Structurally Strong Domestic Consumption

Consistently high GST collections signal resilient nominal growth, strong domestic consumption, formalisation of the economy and fiscal headroom, reducing risks of growth disruptive policy tightening.

6. Domestic Flows as Market Stabiliser

Persistent SIP led mutual fund inflows have offset foreign selling, lowered market volatility and anchored equity demand, especially during global risk off phases.

7. Improving Financial Conditions for Capex Cycle

Lower rates, easing input costs and strong order books have improved visibility for a corporate capex upcycle, benefiting industrials, capital goods and related value chains.

8. Managed External Vulnerabilities

RBI's focus on smoothing currency volatility, supported by high FX reserves, has contained external shocks despite INR weakness, limiting spillover risks to equities.



What Will Shape 2026?

1. Domestic Demand & Earnings Compounding

India enters 2026 with domestic demand as the primary growth anchor. Private consumption contributes ~56-57% of GDP, supported by rising formal employment, steady real wage growth and structurally high household financial savings channeled via SIPs (~₹26-30k crore/month through late-2025). Corporate balance sheets are deleveraged (net debt/EBITDA for listed non financials at multi year lows), enabling capex without stressing cash flows, supportive for earnings compounding in banks, consumer discretionary, autos and building materials

2. Artificial Intelligence as a Strategic Power Variable

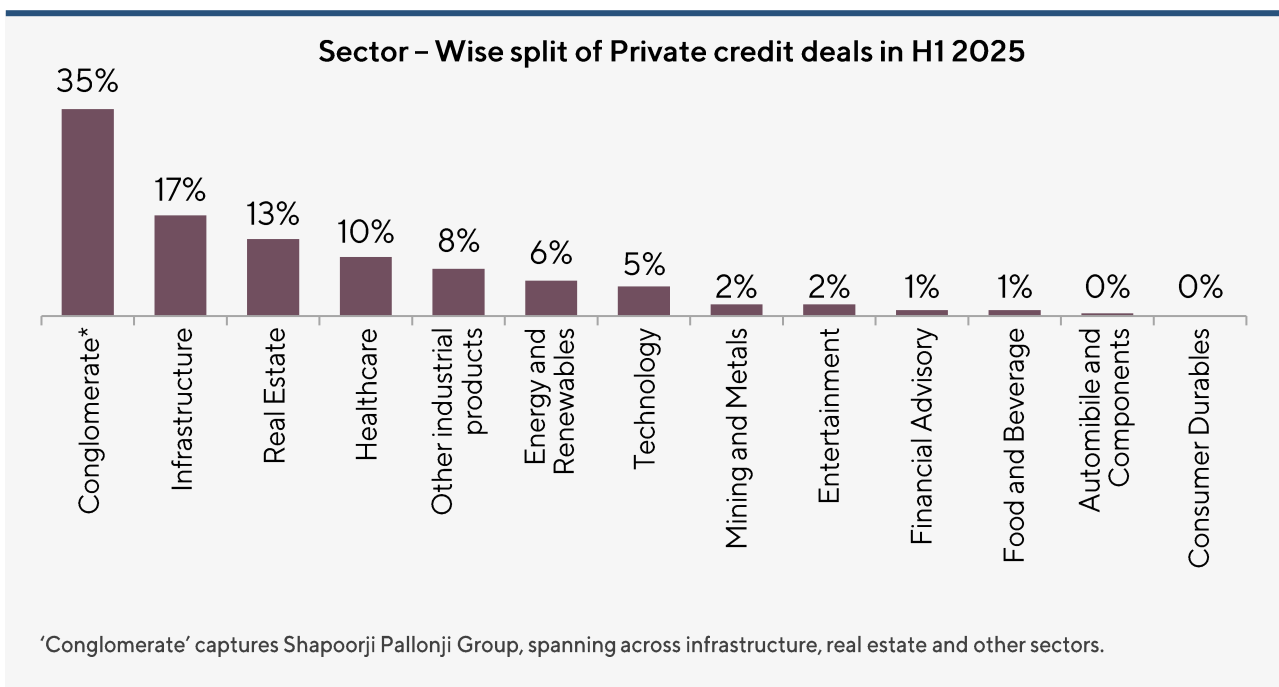
AI is increasingly emerging as a new currency of global competitiveness, influencing productivity, defense, supply chains and capital allocation. While direct monetisation in Indian equities may be selective, AI led capex, digitisation and efficiency gains will shape sectoral winners over the medium term

3. Unlisted Markets Moving Mainstream

A structural shift is underway from niche to core allocation in Unlisted markets. After the 2022-24 reset, growth capital is returning with more realistic valuations, lower public private market correlation and access to new age and unlisted themes not easily available in public markets

4. Rise of Private Credit as a Structural Capital Source

Private credit is set to play a larger role in 2026 as bank credit growth remains concentrated and risk selective, creating funding gaps for mid market corporates, infrastructure, real estate and structured finance. India’s private credit AUM crossed ~US\$20-22 billion by H12025, growing at a 20%+ CAGR, supported by higher yields (~12-16% IRRs), tighter bank regulation on long tenor lending and rising institutional participation from insurers, pensions and global allocators. As balance sheet light lenders scale and deal sizes deepen, private credit is likely to become a durable complement to banks and public markets, shaping capital formation and return opportunities in 2026



5. Geopolitics as a Persistent, Not Cyclical, Variable

Trade fragmentation, supply chain reconfiguration, sanctions and climate linked trade measures are now structural features rather than episodic risks. These forces will shape sector level outcomes and capital allocation decisions through 2026 and beyond

6. Higher Dispersion, Lower Beta Markets

With easy liquidity driven gains behind, 2026 is likely to reward stock selection over index beta. Dispersion across sectors, market caps and business models will remain high, making earnings quality, balance sheet strength and governance the key determinants of returns

7. Great Power Rebalancing & Global Capital Flows

Global capital allocation is gradually shifting as growth in developed markets normalises and relative opportunities improve across select emerging markets. Equity risk premia are becoming more differentiated, favouring countries with macro stability, domestic demand depth and policy credibility. China remains volatile but relevant through policy driven stimulus pockets, while geopolitical competition increasingly influences capital allocation decisions

8. India's Shift from Valuation Led to Earnings Driven Cycle

After a valuation heavy rally in earlier years and consolidation in 2025, 2026 will be shaped by earnings delivery rather than multiple expansion. India stands out as a structural growth story supported by resilient macro fundamentals, manufacturing push and domestic consumption. Broader market participation, especially in mid and small caps, will depend on earnings breadth rather than liquidity alone

9. Domestic Institutions as the Market Backbone

Domestic institutional investors continue to play a stabilising role, cushioning global shocks and reducing volatility driven by foreign flows. SIP led allocations and rising household financialisation are shaping market behaviour, supporting drawdowns but also enforcing discipline and selectivity in stock performance

10. Easing Real Yields and Financial Conditions

As inflation moderates and policy rates ease, real yields are expected to soften, improving the relative attractiveness of risk assets. This environment supports equity valuations and enhances the appeal of assets such as gold and long-duration growth investments, provided earnings visibility improves



Opportunities

1. Manufacturing & Capex Upswing (PLI & China+1)

India's manufacturing cycle continues to strengthen as the Production Linked Incentive (PLI) schemes across electronics, autos & EVs, pharmaceuticals, chemicals and specialty manufacturing convert policy intent into on ground capacity creation. As of FY25, PLI schemes across 14 sectors have attracted committed investments of over ₹1.2 trillion and generated incremental production exceeding ₹9 trillion, with electronics accounting for the largest share. India's electronics exports have risen from ~US\$6 bn in FY15 to over US\$29 bn in FY24, lifting India's share in global electronics exports from <1% to ~3%.

On the domestic front, capital goods companies continue to report healthy order inflows, supported by railways, power, defence, renewables, and industrial capex, with industry order books at 2.5–3.0x trailing revenues, indicating multi year revenue visibility. Public sector capital expenditure has been sustained at ~3.2–3.4% of GDP in recent Union Budgets, while private capex intentions have improved as capacity utilisation remains above 74%. This combination positions industrials, EPC, ports, logistics and manufacturing ancillaries as key beneficiaries through CY2026

2. Financials: Credit Growth with Balance Sheet Strength

India's banking system continues to deliver steady credit growth, with non food system credit expanding at ~13–15% YoY through FY24–FY25, driven by retail, MSME and services linked demand. Asset quality has improved materially, with gross NPAs for scheduled commercial banks declining to ~3.0%, the lowest level in over a decade, supported by recoveries, write offs and restrained underwriting during the previous cycle.

Improving liability franchises, particularly growth in low cost CASA deposits and term deposits, alongside rapid digital sourcing, are driving operating leverage. Large private banks continue to deliver RoEs in the 15–18% range, while PSU banks have structurally improved profitability with RoAs turning positive after several years. NBFCs focused on consumption finance, MSME lending and infrastructure funding remain well positioned as liquidity transmission improves and funding spreads stabilise during the easing phase of the monetary cycle

3. Energy Transition & Power Ecosystem Specifically Nuclear

India achieved its target of 50% installed power capacity from non-fossil sources in 2025, well ahead of its 2030 commitment, driven by rapid solar and wind additions. Electricity demand continues to grow at ~6–7% annually, reflecting industrial expansion, urbanisation and rising per capita consumption. This dual dynamic creates parallel opportunities across renewables (solar, wind, storage, grid equipment) and conventional power segments such as coal logistics, transmission infrastructure and balancing capacity.

The resulting capex cycle across generation, transmission and power equipment offers multi-year earnings visibility, with power sector capex projected at over ₹9 trillion between FY25–FY30. Importantly, the government's recent policy push to allow greater private sector participation in the nuclear power ecosystem, covering reactor manufacturing, fuel cycle services and project execution, is expected to accelerate capacity addition beyond the current ~7.5 GW installed base and crowd in long duration private capital, creating a structural growth opportunity for capital goods, EPC and specialised engineering companies

4. Digital Public Infrastructure & Services Exports

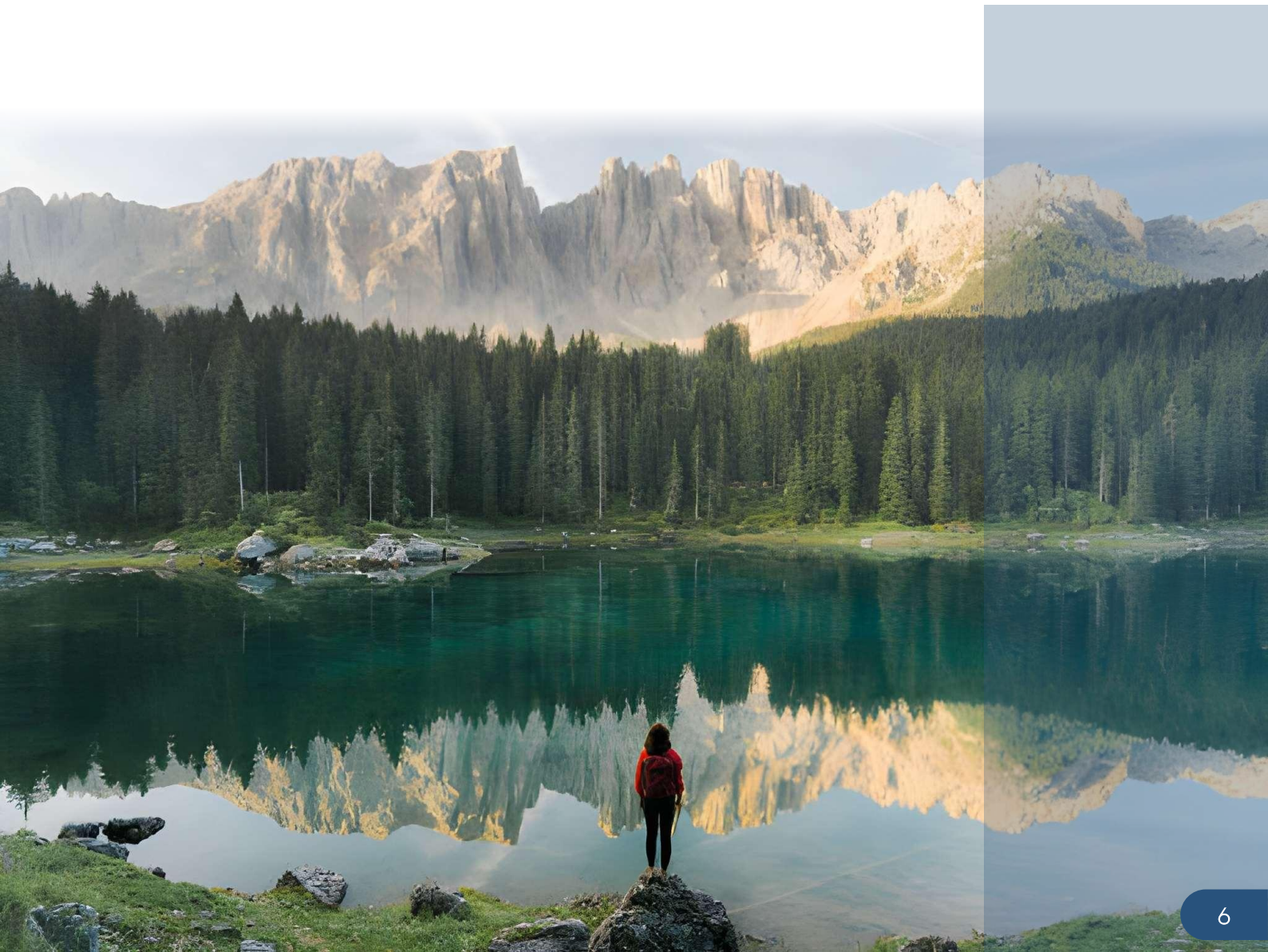
India's Digital Public Infrastructure (DPI) stack anchored by UPI, Aadhaar and ONDC continues to lower transaction costs and accelerate formalisation. UPI transactions crossed 117 billion in CY2024, with transaction value exceeding ₹180 trillion, reinforcing India's position as the world's largest real time payments market. This has structurally benefited fintech, logistics, SaaS and consumer internet platforms through scale driven monetisation and data led credit underwriting.

Services exports remain resilient despite global growth moderation, with India's services exports exceeding US\$340 bn in FY24, driven by IT services, BPM, global capability centres (GCCs) and engineering R&D. India hosts over 1,600 GCCs employing more than 1.6 million professionals, reinforcing long term cost and talent advantages that underpin earnings resilience for export oriented services companies

5. Valuation Dispersion & Selective Alpha

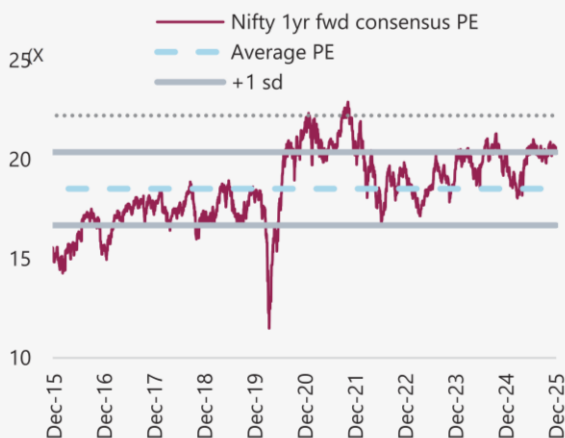
Following the correction across segments of the mid and small cap universe during 2025, valuation dispersion within Indian equities has widened meaningfully. While headline indices corrected modestly, several quality midcaps witnessed 25–40% drawdowns despite stable earnings trajectories, creating selective entry opportunities. Large cap valuations remain relatively reasonable on a historical basis, trading near long term average multiples and offering liquidity and earnings stability amid global uncertainty.

This environment favours bottom up stock selection rather than broad based beta exposure. Companies with visible earnings growth, strong cash flow conversion and governance discipline are positioned to deliver alpha as capital allocators become more valuation sensitive in 2026

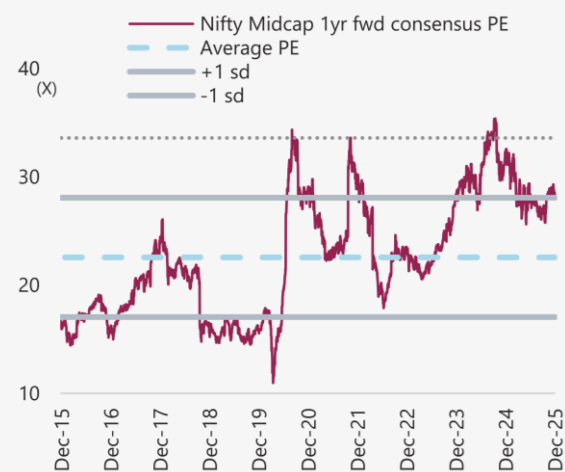


Valuations

Nifty 1yr fwd PE at 20.3x – almost at +1 SD



Nifty Midcap 1yr fwd PE at 28x – above +1SD



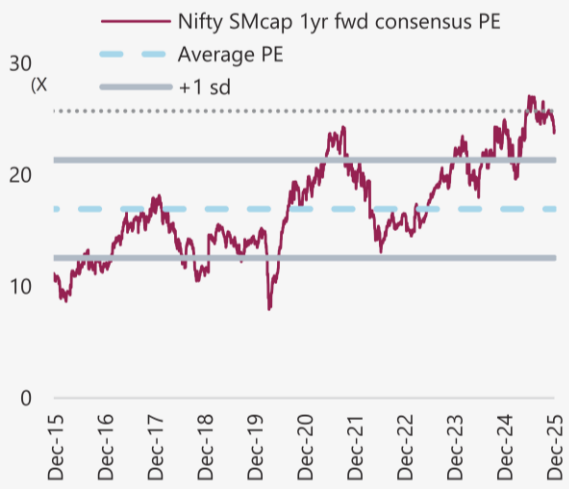
1. Large Caps - Reasonable Valuations with Earnings Stability

Large cap valuations entered 2026 at relatively balanced levels after a period of time correction rather than sharp derating. The Nifty 50 traded around 19-21x 1-year forward P/E and ~3.0-3.2x P/B, broadly in line with its long term averages. Earnings visibility remains strong, supported by banks, financials, energy and select industrial leaders that account for a majority of index profits. Importantly, large caps continue to command valuation support due to superior liquidity, high institutional ownership and balance sheet strength. In a global environment marked by growth uncertainty and volatile capital flows, this valuation comfort positions large caps as the relative 'earnings compounders' rather than re-rating stories in 2026

2. Mid Caps - Valuation Reset, Selective Opportunity

Mid cap valuations corrected meaningfully through 2025, driven by a mix of earnings downgrades, profit booking and tighter liquidity conditions. By end 2025, the Nifty Midcap 150 traded closer to 24-26x forward P/E, down from peaks above 30x, though still carrying a premium to large caps. This premium is increasingly justified only where earnings growth visibility is strong (industrials, capital goods, select manufacturing, healthcare). The dispersion within mid caps is high, quality franchises with cash flows and return ratios remain expensive, while cyclicals and leveraged names have seen sharper de-rating. For 2026, mid caps offer stock specific alpha, but broad based valuation expansion appears unlikely without a clear acceleration in earnings growth

Nifty Small Cap 1yr fwd PE at 24x - above +2SD



3. Small Caps - Valuations Improved, Risks Remain

Small caps witnessed the sharpest valuation compression in 2025. The Nifty Smallcap 250 de rated from elevated levels (>35x forward P/E at peaks) to roughly 22-25x forward P/E by late 2025. While this correction has improved headline valuations, they still sit above long term averages when adjusted for weaker balance sheets, lower institutional ownership and higher earnings volatility. Many small caps continue to face a valuation earnings mismatch, with profitability normalization lagging price correction. In 2026, valuation comfort in small caps is selective, favoring companies with net cash balance sheets, scalable business models and clear earnings visibility rather than broad index exposure



Earnings Outlook



Earnings growth entering 2026 is expected to remain earnings led, selective and execution dependent, as consensus forecasts point to Nifty 50 EPS growth of ~11-13% over FY26-FY27, broadly in line with nominal GDP growth and well below the post COVID rebound phase, signalling normalization rather than reacceleration.

At the index level, profit concentration is likely to persist, with financials expected to continue contributing ~35%+ of Nifty 50 PAT given sustained credit growth, benign asset quality and operating leverage, implying that index earnings resilience will remain disproportionately linked to banking and financial services performance.

Margin support is expected to fade gradually in FY26, as commodity disinflation benefits taper off and wage, freight and compliance costs normalize, shifting the earnings driver mix toward volume growth, utilization improvement and execution efficiency, especially in manufacturing and discretionary consumption.

Forward earnings visibility is relatively stronger in capex linked sectors and services, supported by public capex maintained at ~3.2-3.4% of GDP and improving private investment intentions, which should support multi year revenue pipelines in capital goods, infrastructure, power equipment, defence and select industrial services

However, the higher earnings base and normalising margins imply that aggregate earnings growth is unlikely to surprise meaningfully on the upside. With the Nifty trading close to long term average forward multiples, 2026 index returns are expected to track actual earnings delivery plus dividends, limiting scope for broad based re rating and reinforcing a stock selection driven market

Small Cap Outlook

Small caps enter 2026 with elevated sensitivity to earnings delivery, as forward returns are increasingly shaped by fundamentals rather than liquidity driven beta. Even after the correction, Nifty Small Cap 250 forward P/E remains above long-term averages, implying that earnings misses or balance sheet stress could still trigger sharp valuation derating.

Forward performance is therefore expected to be highly selective, with investor preference skewed toward companies demonstrating visible cash flows, conservative leverage, scalable business models and pricing power, while weaker balance sheet names face a structurally higher cost of capital and refinancing risk.

Liquidity conditions remain a key swing factor for small caps in 2026. While domestic institutional flows and SIP inflows provide a structural demand backstop, they are increasingly being allocated selectively rather than indiscriminately across the segment, amplifying dispersion between quality and non quality cohorts.

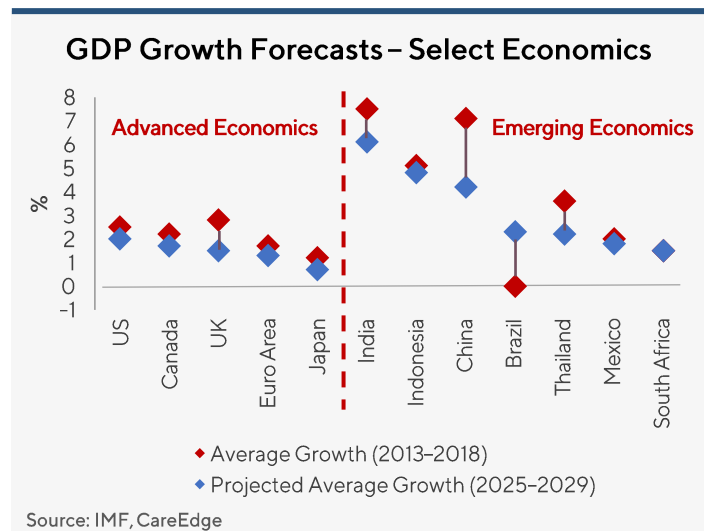
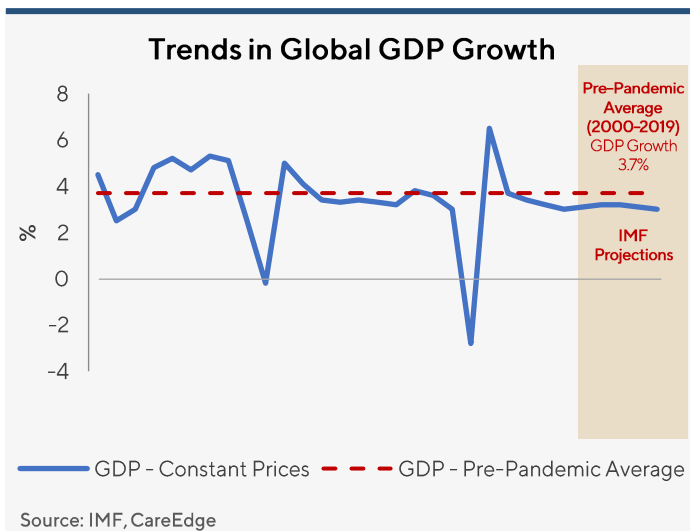
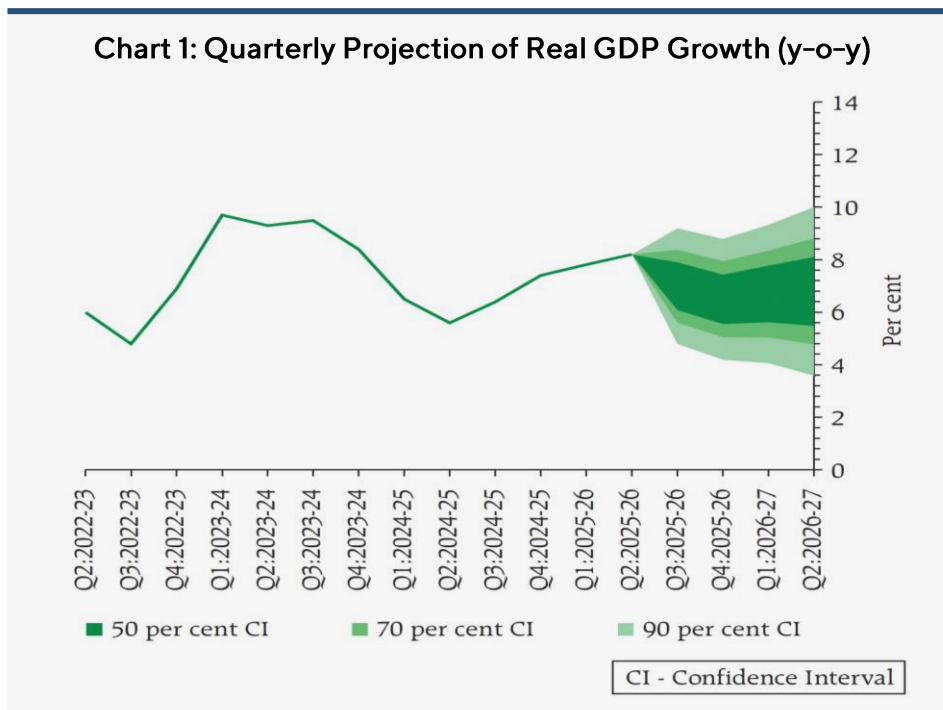
As a result, small cap returns in 2026 are likely to be earnings driven rather than multiple driven, favouring bottom up alpha from stock selection over broad index exposure, with volatility remaining structurally higher than large caps during periods of earnings downgrades or liquidity tightening



Macro Outlook

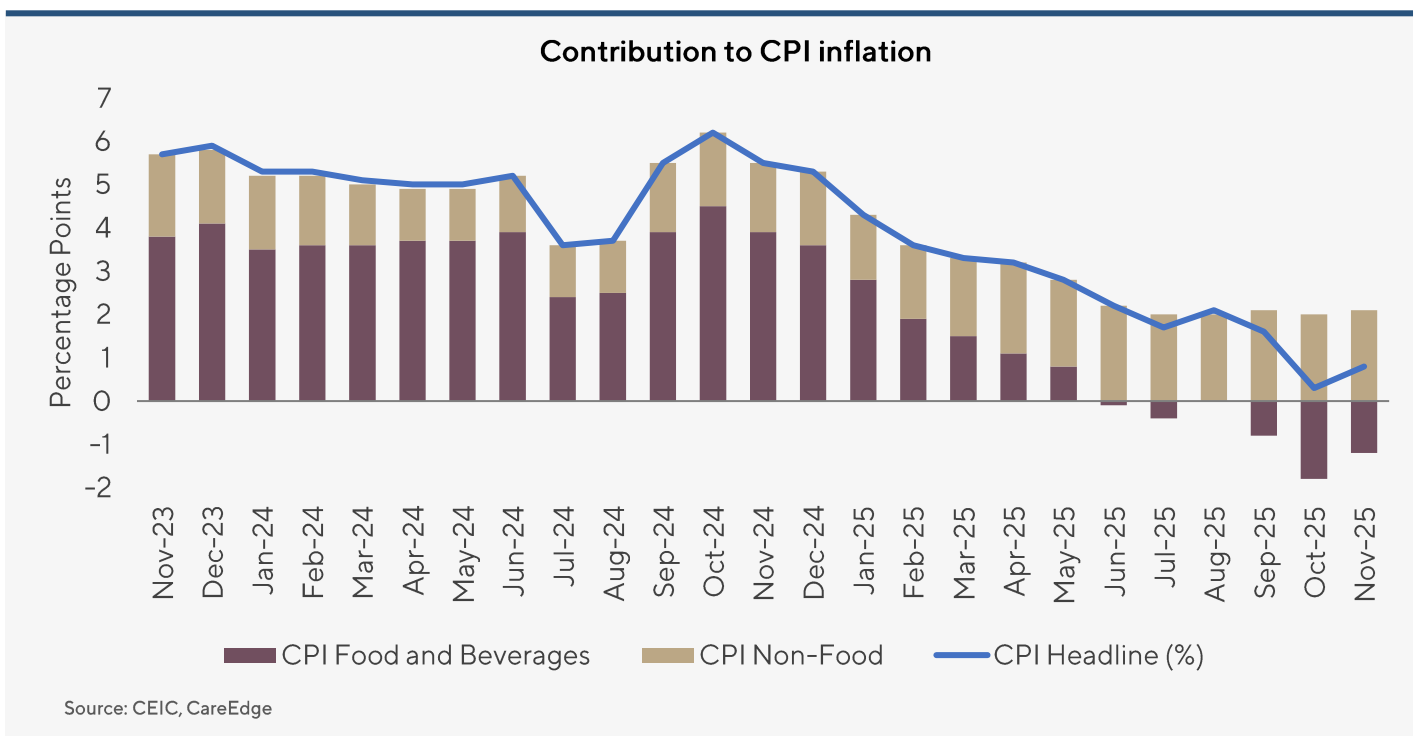
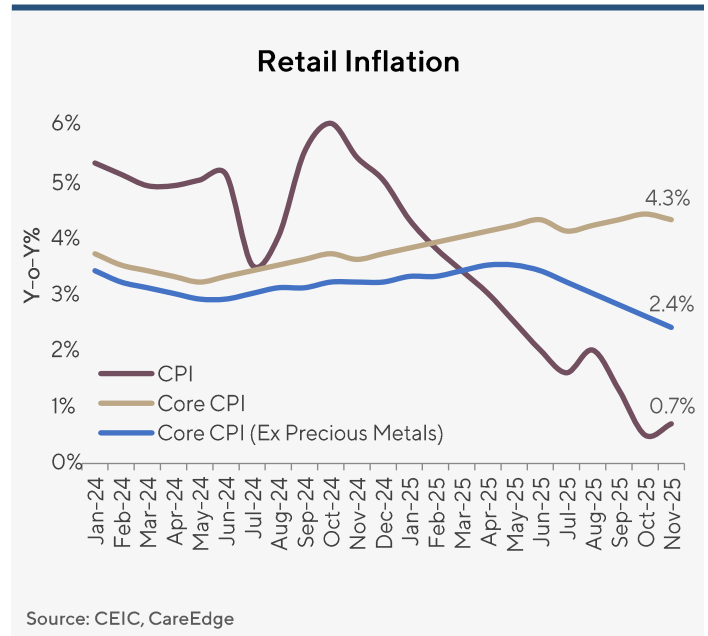
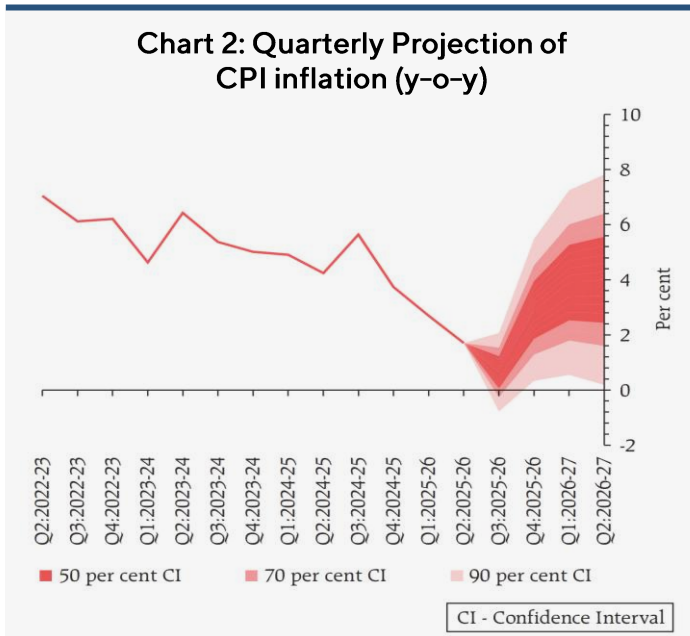
1. GDP Prediction

India's growth path is projected to remain strong but moderating: GDP ~7.5% in FY26 and ~7.0% in FY27. The FY27 growth mix is expected to broaden, with industries accelerating to ~7.2% while services normalise to ~7.7%; agriculture ~3.3%. On the demand side, consumption ~7.3%, investment ~6.9% and government expenditure ~7.2% are projected for FY27. Nominal GDP is projected at ~8.3% in FY26 and ~10.1% in FY27 (deflator normalisation)



2. Forecast

The baseline macro track suggests low inflation in FY26, normalising in FY27: avg CPI ~2.1% in FY26 and ~4.0% in FY27. External balance is projected contained with CAD ~1% of GDP in both FY26 and FY27. Fiscal consolidation continues with fiscal deficit ~4.4% of GDP (FY26) and ~4.2-4.3% (FY27). Market variables in the baseline: 10Y G-sec ~6.4-6.6% by end-FY26 and USD/INR ~89-90 by end-FY27



3. Global Macro

The global backdrop remains ‘slower but stable’ and expected to continue doing so; world growth 3.2% (2025) → 3.1% (2026). Major economy 2026 projections: US ~2.1%, Euro Area ~1.1%, Japan ~0.6%, China ~4.2% (and India shown at ~6.2% on a fiscal-year basis in that same table).

Entering 2026, nominal policy rates remain elevated but real policy rates are positive across major economies, reflecting inflation moderation. With policy rates around 3.50-3.75% in the US, ~2.0% in Europe and ~0.50% in Japan and inflation near ~3.0%, ~2.1% and ~2.8% respectively, real rates range from mildly restrictive to neutral. This keeps the easing bias intact, but future rate cuts remain conditional on sustained disinflation rather than growth alone

4. India Macro Outlook

India’s macro outlook for 2026 remains constructive, supported by a broad based growth recovery and stable fiscal dynamics. The first advance estimate pegs FY26 real GDP growth at 7.4% (vs 6.5% in FY25), with services growth accelerating to 9.1% and industry expanding by 6.0%, led by a rebound in manufacturing at 7.0%. On the demand side, growth is underpinned by a recovery in gross fixed capital formation at 7.8%, higher than last year, alongside steady private consumption growth of 7.0% and government consumption growth of 5.2%, cushioning external headwinds. While imports grew faster than exports in real terms, the overall macro balance remains manageable, with the fiscal deficit for FY26 estimated at 4.4% of GDP, unchanged despite lower tax buoyancy, aided by stronger non tax revenues. Overall, the data points to resilient domestic demand, improving investment momentum and contained macro risks heading into 2026

GDP Growth Rates (YoY%) at Constant Prices (Base:2011-12)					
Particulars	FY 26			FY25 (PE)	FY24 (1RE)
	FY 26 (1AE)	H1	H2*		
1. Agriculture, Forestry & Fishing	3.1	3.6	2.7	4.6	2.7
2. Industry	6.0	7.0	5.4	5.9	10.8
2.1 Mining & quarrying	-0.7	-1.8	0.3	2.7	3.2
2.2 Manufacturing	7.0	8.4	5.7	4.5	12.3
2.3 Electricity, gas, water supply & other utility services	2.1	2.4	1.7	5.9	8.6
2.4 Construction	7.0	7.4	6.7	9.4	10.4
3. Services	9.1	9.3	9.0	7.2	9.0
3.1 Trade, hotels, transport, communication & services related to broadcasting	7.5	8.0	7.1	6.1	7.5
3.2 Financing, insurance, real estate & bus services	9.9	9.9	10.0	7.2	10.3
3.3 Public administration, Defence & Other services	9.9	9.7	10.1	8.9	8.8
Total GVA at Basic Prices	7.3	7.9	6.8	6.4	8.6
GDP	7.4	8.0	6.9	6.5	9.2

Source: NSO, MOSPI, SBI Research; *SBI Calculation based on AE

Conclusion

Indian equity markets enter 2026 after a necessary phase of consolidation that has reset valuations, narrowed leadership and shifted the market decisively from a liquidity and valuation driven cycle to one anchored in earnings quality and balance sheet strength. Macro fundamentals remain supportive, India continues to lead global growth with real GDP in the ~7-7.5% range, inflation has moderated meaningfully and monetary easing alongside liquidity support has improved financial conditions without compromising fiscal discipline. This macro stability, combined with resilient domestic consumption, sustained public capex and deleveraged corporate balance sheets, provides a durable foundation for earnings compounding rather than speculative excess.

At the market level, dispersion is likely to remain high in 2026. Large caps offer relative earnings stability and liquidity support, while mid and small caps present selective opportunities rather than broad beta plays. Earnings growth is expected to moderate from FY25 highs but remain structurally healthy, driven by financials, capex linked sectors, manufacturing and services, with returns increasingly tracking profits and dividends rather than multiple expansion. Domestic institutional flows, particularly SIP led participation, continue to act as a stabilising force, cushioning volatility but also enforcing discipline. Overall, 2026 appears positioned as a selective, fundamentals led year, rewarding patient capital, bottom up stock selection and alignment with earnings visibility rather than momentum driven exposure





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