EQUITY OUTLOOK

Harish Krishnan
Chief Investment Officer - Equity
Aditya Birla Sun Life AMC Limited

Global Markets: Geopolitical Risk Recedes, Capital Rotation Remains the Missing Piece

Global markets entered June with a significant reduction in geopolitical uncertainty following the US-Iran ceasefire and the reopening of the Strait of Hormuz. The sharp correction in crude oil prices, normalization of energy supply chains, and improving currency stability have removed one of the largest macro overhangs that had weighed on financial markets over the previous three months.

Despite the improvement in macro conditions, leadership across global equities continues to remain highly concentrated. AI-led markets, particularly Japan, Taiwan and South Korea, continue to outperform, supported by strong technology earnings and sustained investor enthusiasm around artificial intelligence. India, meanwhile, remains one of the weakest-performing major equity markets on a CY26YTD basis, reflecting continued foreign capital outflows despite improving domestic fundamentals.

India Macro: External Pressures Ease as Domestic Fundamentals Reassert Themselves

Indian equities recovered during June after three months of heightened volatility. The recovery was primarily driven by the sharp fall in crude oil prices, a stabilizing rupee, and moderation in foreign institutional selling. These developments have materially reduced concerns around imported inflation, corporate margin pressure and external sector vulnerability.

The improvement in crude prices is particularly significant for India. Oil below USD75/bbl provides meaningful relief across multiple macro variables, including inflation, the current account deficit and fiscal balances. While the June quarter is likely to continue reflecting the impact of elevated input costs experienced earlier in the year, the benefits of lower energy prices should begin to emerge from the second quarter of FY27 through improved corporate margins and stronger earnings delivery.
At the same time, India's domestic growth drivers remain intact. Healthy domestic liquidity, resilient consumption trends and continued government-led investment provide a supportive backdrop as external risks gradually diminish.

Liquidity: Domestic Flows Continue to Anchor Markets
One of the defining features of the current market cycle remains the divergence between domestic and foreign investor behaviour.

Domestic institutional investors continue to provide a powerful structural anchor for Indian equities, extending an unprecedented multi-year period of sustained inflows. Although foreign institutional investors remained net sellers during June, the pace of selling moderated meaningfully, suggesting that the worst phase of capital outflows may be behind us. The resilience of domestic liquidity has fundamentally altered market dynamics. Unlike previous cycles, external shocks are increasingly being absorbed without triggering prolonged market dislocations. Nevertheless, a meaningful rerating of Indian equities will likely require a return of foreign capital, particularly as global investors remain heavily concentrated in AI and semiconductor-driven opportunities.

Earnings Outlook: Margin Pressures Should Peak in 1QFY27

The sharp decline in crude oil prices significantly improves the earnings outlook over the remainder of FY27.

While first-quarter earnings are expected to continue reflecting elevated commodity and logistics costs, these pressures should progressively ease as lower input prices flow through corporate cost structures. Sectors with meaningful exposure to energy and imported raw materials are likely to witness the greatest margin recovery during the second half of the year.

Accordingly, we continue to believe that the Nifty's FY27 earnings growth expectation of approximately 14% remains achievable, provided geopolitical conditions remain stable and commodity prices do not witness another significant spike

Cond

Macro Outlook: Risks Have Shifted Rather Than Disappeared

Although geopolitical risks have moderated materially, the market's attention is now shifting toward a different set of macro variables.

Domestically, the possibility of an El Niño event remains an important monitorable, given its potential implications for agricultural output, rural demand and food inflation.

Globally, monetary policy continues to represent an important source of uncertainty. Any shift in market expectations from eventual US Federal Reserve rate cuts toward a prolonged higher-for-longer interest rate environment could delay the recovery in global liquidity and postpone a meaningful return of foreign portfolio flows into emerging markets.

These risks are fundamentally different from those that dominated earlier in the year. Instead of energy security, investors are increasingly focused on growth durability, policy normalization and capital allocation.

Valuation: Large Caps Offer Better Risk-Reward

The valuation reset witnessed over recent months has significantly improved the attractiveness of large-cap Indian equities.

The Nifty now trades at approximately 18.6x one-year forward earnings, representing an 11% discount to its long-term average. This moderation in valuations provides a more balanced risk-reward profile, particularly given improving macro conditions and expectations of stronger earnings growth during FY27.

In contrast, mid-cap and small-cap segments continue to trade at meaningful premiums to their historical averages despite recent corrections. While structural growth opportunities remain attractive, future returns in these segments are likely to depend increasingly on earnings execution rather than further valuation expansion.

Conclusion: Improving Macro Conditions Support a More Constructive Outlook

The investment backdrop has improved meaningfully over the past month. The easing of geopolitical tensions, correction in crude oil prices and stabilization of the rupee have reduced several of the macro risks that dominated market sentiment during the previous quarter.

However, the next phase of market performance is unlikely to be driven solely by improving macro conditions. A sustained recovery will require stronger earnings delivery, continued domestic liquidity support and, importantly, a gradual return of foreign institutional capital.

While risks remain, the balance of probabilities has shifted in a more constructive direction. With valuations now closer to long-term averages and earnings expected to strengthen through FY27, the foundation for a more durable market recovery is steadily taking shape.

Source: ABSLAMC Internal Research

DEBT OUTLOOK

Kaustubh Gupta
Chief Investment Officer - Fixed Income
Aditya Birla Sun Life AMC Limited

The West Asia conflict and the disruption to shipping through the Strait of Hormuz remain the most important monitorable for Indian markets and the economy. Global crude prices corrected sharply following the MoU signed between US and Iran. However, that improvement has so far proved temporary with the ceasefire unravelling and disruptions/blockage returning to traffic via Strait of Hormuz. Crude has already jumped by more than 20% from the recent lows. For India, this reversal is clearly adverse after the brief relief seen following the June agreement. A sustained rise in crude prices would pressure the current account, the rupee and inflation, while also increasing the cost of LNG, LPG, fertilisers, petrochemicals and edible oils. The government's ability to adjust excise duties and the regulated nature of some domestic fuel prices provide a degree of cushioning, but prolonged disruption would eventually involve a trade-off between fiscal absorption, consumer inflation and the profitability of oil-marketing companies.

The monsoon remains the second domestic uncertainty. A severely deficient June was followed by an improvement in early July, helping the cumulative rainfall deficit narrow and supporting a recovery in kharif sowing. As of July 10, total kharif acreage was only 3.3% below the normal area, although it remained around 16% below last year; pulses, oilseeds and cotton continued to lag normal sowing levels. The latest rainfall distribution, however, remains uneven, and the IMD expects subdued rainfall across the plains of northwest India, west-central India and southern peninsular India during the next six to seven days. The evolving El Niño conditions therefore remain an important upside risk to food inflation, even though foodgrain stocks, reservoir storage, improving irrigation and improved supply-management capacity provide some protection.

India's June 2026 CPI (Consumer Price Index) inflation rose to 4.4% YoY from 3.9% in May, crossing the RBI's 4% target for the first time in 17 months. The increase was supply side driven, led by food inflation and the full pass-through of May's petrol, diesel and LPG price hikes, which lifted transport inflation sharply. Underlying inflation remains contained, with core-core inflation near 2.5% after excluding fuel and precious metals. Notably, inflation in Q1 FY27 remained below RBI forecasts, supporting expectations of an extended RBI pause by RBI. From a monetary-policy perspective, MPC (Monetary Policy Committee) is unlikely to respond mechanically to a first-round supply shock. Further rate action will depend on the persistence of crude prices, the degree of pass-through to core inflation and inflation expectations, the monsoon outcome and the effect of tighter external conditions on domestic growth. RBI has shown that it prefers external-account pressure to be addressed through targeted capital-flow, liquidity and foreign-exchange measures than through a policy-rate response, unless the shock begins to generate broad-based and persistent inflation

The other key monitorable for the markets has been the inflows related to FCNR (Foreign Currency Non-Resident)/ECB (External Commercial Borrowings) concessional swap windows announced by RBI. Recent media reports suggest US$10bn of inflows till now, which is decent. However, there are some concerns regarding the quantum of leverage which banks can provide to NRIs for FCNR deposits and rising global rates which reduce attraction to FCNR(b) deposits especially for leverage. We expect total inflows from both FCNR/ECB window to be closer to US$60bn. Market is also keenly awaiting some announcements with regards to addition of Indian GSec to Bloomberg Aggregate Bond index.

With our expectation of long pause from RBI, decent inflows due to RBI concessional swap window, likely addition to Blomberg bond index and elevated yields, we remain constructive on the markets. The key risk we see is related to West Asian conflict and South West Monsoon. We recommend investors with 1 month+ horizon to invest in our 3-6M Financial Services Index fund, 3 months+ to invest in our ultra short or low duration fund. 1-5 year corporates provide a good risk-adjusted entry point at current levels given the likely inflows from RBI swap windows, and hence investors looking to benefit from it can look to invest in our Corporate Bond Fund and Banking & PSU Fund. Investors having a 2Y+ horizon should look at our Income Plus Arbitrage FOF given tax efficiency

Source: ABSLAMC Internal Research.