

Indian equities – Emerging from the West Asia crisis



Manoj Menon
*Head - Institutional
Research*
ICICI Securities Ltd.



Vinod Karki
Equity Strategist
ICICI Securities Ltd.

The West Asia crisis has laid bare India's external-sector vulnerability, with nearly 87% of the nation's annual crude oil requirement being met through imports. While India also manufactures and re-exports petroleum products, the net oil import bill stood at ~USD 122bn in FY25 (3.1% of GDP). The external sector seems to be bearing the brunt, with a wider trade deficit, amplified risks to Gulf remittances and potential FPI outflows weighing on the country's current account and clouding the broader BoP outlook. Also, it begins to restrain demand as prices rise. Corporate profitability also takes a hit, as fuel and raw material costs for most companies surge. The spike in crude oil would also be inflationary, as the assigned weight of petrol, diesel and LPG is higher in the new CPI series, at 6.8% (3.6% in earlier series); although, the impact hinges on the extent of pass-through of global oil prices to domestic fuel prices.

The West Asia crisis is, at its core, an energy shock. Evaluating the sources and uses of energy

is, therefore, central to gauging its impact on sectors and stocks. India's total final consumption (TFC) – aggregate energy consumed by end users – reached 25,480 petajoules in FY25, with oil products and natural gas making up 40% and 9%, respectively, of the energy supply; coal and electricity contributed the remaining ~51%. TFC excludes the consumption of energy producers and transmission losses. Industrial, transport and residential sectors are the dominant end-consumers of oil products, while transport and non-energy use like fertilisers drive natural gas consumption. So far, the conflict has disrupted supply rather than demand; therefore, against escalating oil prices, companies highly dependent on oil and gas inputs bore the heaviest toll. From a supply perspective, demand for coal and electricity will likely rise, alongside higher realisations for upstream oil companies.

Opportunity in crisis: Indian equities have a strong negative correlation with oil prices, as it spikes above the USD 90–100/bbl level. The previous instance of the negative correlation between crude prices and NIFTY50 was witnessed in 2022, when oil prices shot past and stayed beyond USD 100/bbl for 3–4 months, spurred by the Russia-Ukraine conflict, which threatened to take away Russia's oil from the global supply. The resulting volatility (NIFTY50 fell ~10%) created the foundation for the big equity rally seen over CY23. Similarly, during the West Asia crisis, the NIFTY50 dropped ~12% and is again creating grounds for ascension.

Despite overarching macro headwinds, recent data points have been pleasantly surprising. These include: 1) RBI announcing a slew of measures to attract foreign flows into debt instruments. 2) Q4FY26 GDP growth of 7.8%, led by gross fixed capital formation. 3) Q4FY26 current account surplus driven by services exports and remittances. 4) Crude oil prices receding to below USD 90/bbl due to positive developments in US and Iran negotiations.

Profit cycle continues to expand as profit after tax (PAT)/GDP rises to 5.7% in FY26

Reported PAT in FY26 for the listed space approached the INR 20trn mark, or 5.7% of GDP, with loss pools shrinking to a record 0.2% of GDP. **Aggregate market cap (MCAP) to GDP ratio has largely tracked the PAT/GDP line, going by data for more than two decades; thus, indicating that the profit trajectory is the strongest signal for stock prices amidst the noise created by conflicting news flows—especially in the current environment of heightened geopolitical risks.** For Q4FY26, the NSE500 universe's profit growth was ~12%, driven by broader markets, while for the NIFTY50, profit growth stood at ~5%. From an outlook perspective, the NIFTY50 index's FY27 profit growth could be ~14%, potentially riding on industrials, commodities, financials and discretionary consumption.

Overall, Q4FY26 results have been better than expected, with robust volume and credit growth for manufacturers and lenders. Demand outlook has also been largely positive despite the conflict in the west.

Profit/GDP likely to breach the previous peak of 6.4%

Along with improving earnings growth, the lower nominal GDP number for FY26 in the revised base year (2022-23) series helped boost the PAT/GDP number. PAT/GDP of 5.7% in FY26 was at a 15-year high and approaching the previous peak of 6.4% of GDP seen in FY08.

A combination of high financial leverage and operating leverage going into an economic recession is the 'perfect storm' for peak corporate profit levels as seen during FY08, which is not evident currently.

From a credit cycle perspective, corporate re-leveraging appears to be in the nascent stages of a recovery and is unlikely to peak anytime soon. In parallel, India Inc's NPAs and net/debt equity sit at historical lows. Also, there is scope for further operating leverage, as capacity utilisation—though improved—could gain further.

Formalisation of economy allows sustained higher peak for PAT/GDP: Drawing on examples in advanced economies like the US, the corporate profit/GDP ratio—while exhibiting cyclical moves—continues to hit new highs over time, as the corporate sector captures an incremental share of the overall economy.

Banks are already at higher PAT/GDP levels compared to the previous peak – aside of the early stages of a credit cycle recovery and NPA being at historical lows. The share of NBFCs and other financial services is on a structural uptrend.

Corporate capex approaches INR 13 trn, transforming from maintenance to growth

Listed corporate capex (excluding financials) for FY26 stood at ~INR 12.6trn, which includes cash spent on plant, property and equipment (PPE), plus net acquisitions (acquisitions minus divestitures). Excluding acquisitions and divestitures, which tend to be lumpy, core capex on PPE stood at INR 12trn (YoY 14% growth vs. nominal GDP growth of 9%). Another encouraging trend is that the aggregate 'capex/depreciation' ratio has reached ~1.9x, indicating that capex has now moved beyond the maintenance capex range of ~1x. Separately, the 'CFO (cashflow from operations)/capex' ratio is still elevated at 1.5x. Although this is down from its peak of 2x, it indicates that India Inc is still generating ample cashflow to fund its capex requirements. However, the corollary to this is that credit demand for funding capex growth will likely continue to be lacklustre until the 'CFO/capex' ratio drops closer to the 1x mark.

AI infrastructure capex euphoria largely missing in the listed space—a potential hedge, if AI euphoria dissipates

Largest capex driving sectors (> INR 1trn) in the listed corporate space continues to be dominated by utilities (INR 2.3trn), energy ex-Reliance (INR 1.5trn), industrials (INR 1.3trn), Reliance (INR 1.2trn), metals (INR 1.1trn) and auto (INR 1.1trn).

New-age sectors' capex outlook remains bright

Data centre capex outlook continues to look bright, driven by a mix of domestic listed companies and global hyperscalers, such as Bharti, L&T, Reliance, AdaniConnex, Microsoft and AWS. Other areas of high growth in investments include quick commerce, EVs, green energy and GCCs.

Broad-based corporate capex

The number of companies with a capex of more than INR 10bn reached an all-time high of 168 stocks vs. the previous peak of 91 companies in 2012.

However, in USD terms, while the number of companies with a capex of more than USD 100mn has also reached an all-time high of 190 companies, the figure remains close to its earlier peak of 174 seen in 2012. Furthermore, from an aggregate capex perspective, while the figure in INR terms has more than doubled from its previous peak in 2012 (~INR 6trn), the aggregate capex in USD terms—currently at USD 143bn—is not significantly higher than the previous peak of USD 131bn in 2012.

Sectors leading the rise in the number of companies with a minimum capex of USD 100mn include not only asset-heavy sectors such as industrials, metals, energy and utilities, but also relatively asset-light sectors such as automobiles and components, consumption, healthcare and IT.

FPI casting a wider net, but likely being drowned out by selling in concentrated holdings

Aggregate FPI holding of Indian stocks has ebbed to ~15% currently, compared to ~20% a decade ago. Bulk of the retreat was triggered post 2022 (Russia-Ukraine conflict), and coincided with the bottom formation of US Big Tech stocks. **Upon closer examination of the FPI flows, we observe a peculiarity – during this drawdown phase in India holdings, there has been an expansion in the number of stocks, from ~900 to ~1,300 currently; where, FPIs have invested more than 1%.** On the other hand, the top stocks held by FPIs in 2022, which contributed ~41% to their India portfolio, have seen that contribution dip sharply to 21% currently. **Anecdotally, FPIs have sharply increased their holdings in high-growth avenues, cutting across legacy and emerging sectors.**

The aforementioned trends indicate that FPI investments in India are becoming broad-based driven by growth opportunities. But, the copious selling in the erstwhile concentrated positions is skewing the overall picture. **Nevertheless, recent trends indicate that the overall selling is also abating, as the West Asia crisis recedes.**