NETRA

Early Signals Through Charts

September 2025

Released on 5th September 2025

Driver of India’s Premium Valuations, A Foreign Flows Proxy and The Momentum Factor.

DSP

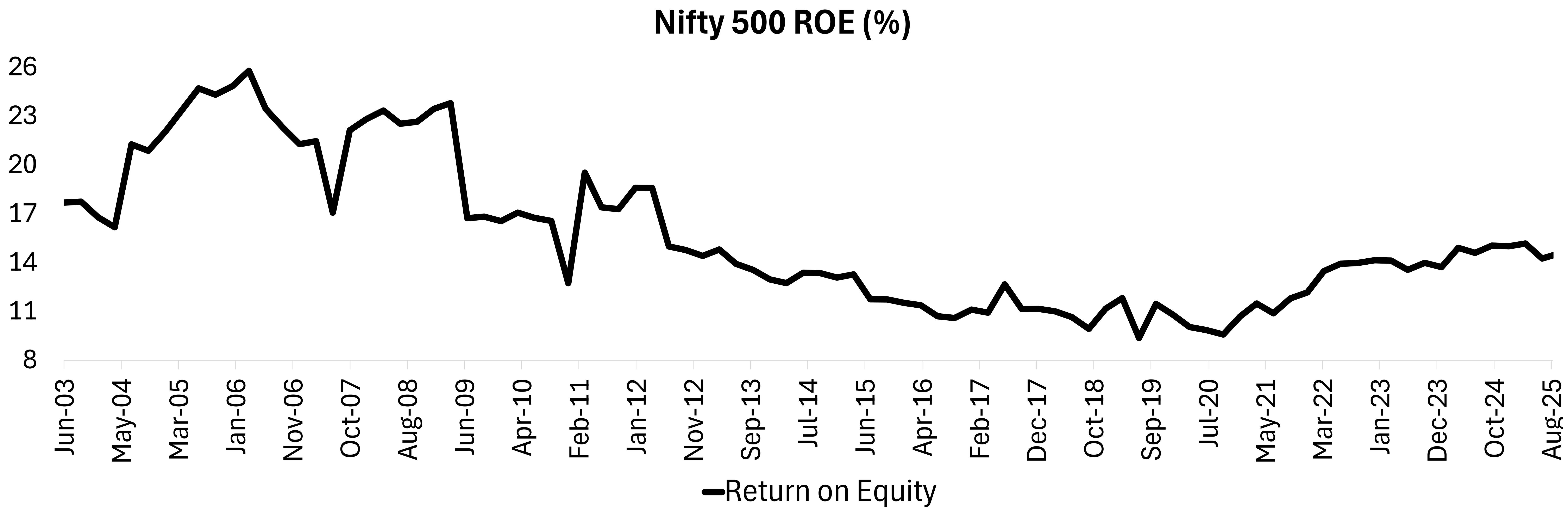
Why Return On Equity (ROE) Isn't Higher?

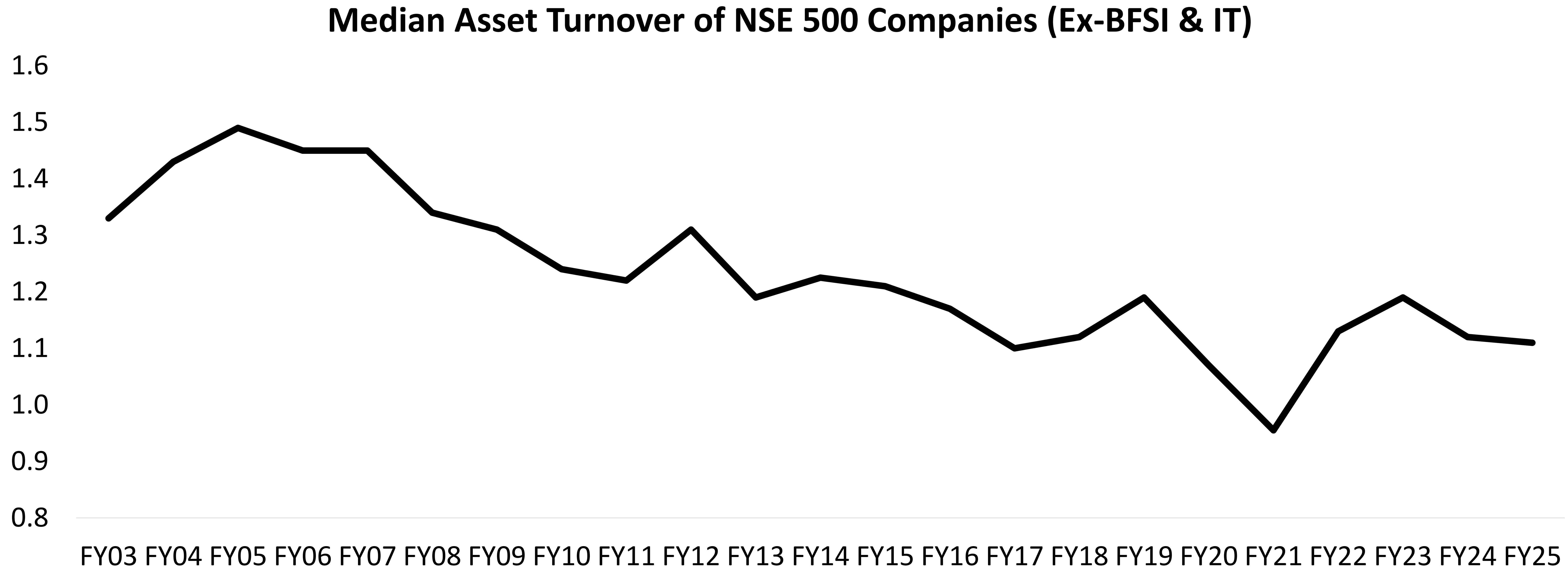
During the 2003–07 upcycle, Indian corporates consistently delivered ROE in the range of 20–25% and ROA of 4–6%. Post-Covid, corporate India has witnessed a similar returns phase; characterized by strong topline growth, peak margins, and robust profit expansion.

The key question, however, is: if the operating environment today appears stronger like in the past, why are return ratios not higher? Where are the ROEs?

One reason is the declining asset turnover. In the earlier upcycle, for instance, every ₹100 of assets generated roughly ₹150 of sales. Today, the same investment yields only ₹120-130. At the same time, leverage levels have declined, which means that these assets are not levered leading to an increase in the equity base. With intensifying competition, companies face mounting pressure to sustain profitability. Another reason for this is the slowdown in the nominal growth.

As a result, while the current ~15% ROE may appear healthy, it is meaningfully lower than previous upcycles. Moreover, there is little assurance that this level will hold. Corporations may leverage up to improve asset turns, but that needs visibility of demand aka faster nominal growth.





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Source: Capitaline, DSP, Data as of Aug 2025. Nifty 500 current constituents used.

Why India Trades At Premium Valuation?

FMCG, IT, Auto, O&G, and Consumer Durables are among India's most consistent high-ROE sectors. A core high-ROE cohort of FMCG, IT, O&G (ex RIL), and Consumer Durables makes up over one third of market cap and earns ROEs about 50% above the rest. This is the source of India's premium valuation over the long term.

But since the pandemic, cyclicals such as metals, mining, and construction materials have rerated sharply despite weaker long-term ROEs. Meanwhile, earnings momentum in the high-ROE cohort has cooled: revenue growth is slowing, and margins look late cycle. The source of India's premium valuation in this cycle is the weak ROE cohort, not the high-quality names. Yet the market still trades at an overall premium, buoyed by cyclicals and lower-quality names.

Bargains will be available, sooner or later, in the high quality (high ROE) cohort when valuations cool. The high multiples for low quality businesses present a challenge for the broader market.

This is a constructive setup for value investors who stay focused on quality.

Sector Name	Weight as per Total Market Cap	Average ROE	Average ROE since GFC	Average PE	Average PE since GFC	Avg PE premium / discount	Average 3 Year EPS CAGR
Fast Moving Consumer Goods#	8%	35.5	45.4	59.9	46.1	30%	9%
Information Technology	13%	28.8	28.6	23.9	21.0	14%	3%
Automobile and Auto Components@	8%	22.2	22.8	26.5	27.5	-4%	40%
Oil, Gas & Consumable Fuels	12%	19.7	22.3	13.3	13.9	-4%	8%
Financial Services	28%	13.3	15.9	41.6	39.8	5%	22%
Healthcare	4%	17.8	15.1	36.3	50.9	-29%	26%
Consumer Services*	3%	16.5	-22.6	566.1	290.3	95%	84%
Services	1%	19.0	20.2	24.9	27.8	-10%	27%
Telecommunication	6%	22.0	11.3	39.1	105.3	-63%	83%
Power	3%	14.5	14.1	14.9	13.6	10%	6%
Construction	3%	16.0	15.5	32.0	26.0	23%	23%
Consumer Durables	3%	25.5	31.2	74.7	60.8	23%	12%
Metals & Mining	4%	8.0	9.6	43.4	31.5	38%	-3%
Construction Materials	3%	6.5	13.1	49.1	24.3	102%	-13%

Heavy weights
Cyclicals
Defensive
Sensitive

Average ROE and PE Skewed by HUL acquisition of Glaxosmithkline Consumer

@ Base effect is causing high EPS growth

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Source: Capitaline, DSP, Data as of Aug 2025.

*ROE and P/E since Apr 2009 or since data is available. **Only Nifty 50 stocks are considered. For Broader market, froth will be much higher.**

Current Growth Trend Is One of The Weakest

FY25 ended with sub 10% nominal growth, FY26 began with sub 9%. The stock market is priced for 20% earnings growth!

	CAGR				YoY Change					
	FY90-FY25	FY00-FY10	FY20-FY25		FY2021	FY2022	FY2023	FY2024	FY2025	Jun-25
Nominal Gross Domestic Product	12.8%	12.3%	10.5%		-1.2%	18.9%	14.0%	12.0%	9.8%	8.8%
Private Final Consumption Expenditure (PFCE)	12.4%	10.8%	10.6%		-0.9%	18.6%	14.9%	9.7%	12.0%	9.2%
Govt Final Consumption Expenditure (GFCE)	12.3%	11.7%	8.4%		4.2%	7.2%	11.5%	12.6%	6.4%	9.7%
Gross Fixed Capital Formation (GFCF)	13.4%	14.7%	11.6%		-5.2%	28.7%	20.3%	9.2%	7.9%	8.3%
Exports of Goods and Services	16.4%	19.0%	13.3%		-1.1%	36.1%	23.8%	3.3%	8.3%	8.1%
Exports of Goods*		17.6%	10.8%		-2.7%	45.8%	15.1%	-0.1%	2.3%	4.3%^
Exports of Services*		18.5%	16.8%		1.1%	24.2%	37.9%	7.9%	16.1%	
Imports of Goods and Services	16.2%	20.0%	12.7%		-11.3%	49.7%	27.2%	-1.7%	9.5%	5.9%
Imports of Goods*		22.2%	12.6%		-13.2%	56.8%	25.7%	-2.3%	8.4%	6.9%
Imports of Services*		17.8%	13.1%		-4.2%	25.8%	33.5%	0.9%	13.8%	

^Frontloading of exports before tariffs kicked in added to GDP growth in June'25

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Source: CMIE, DSP. Data as of August 2025.
*FY05-FY10 CAGR instead of FY00-FY10

India's FX Reserves – A Proxy For External Troubles

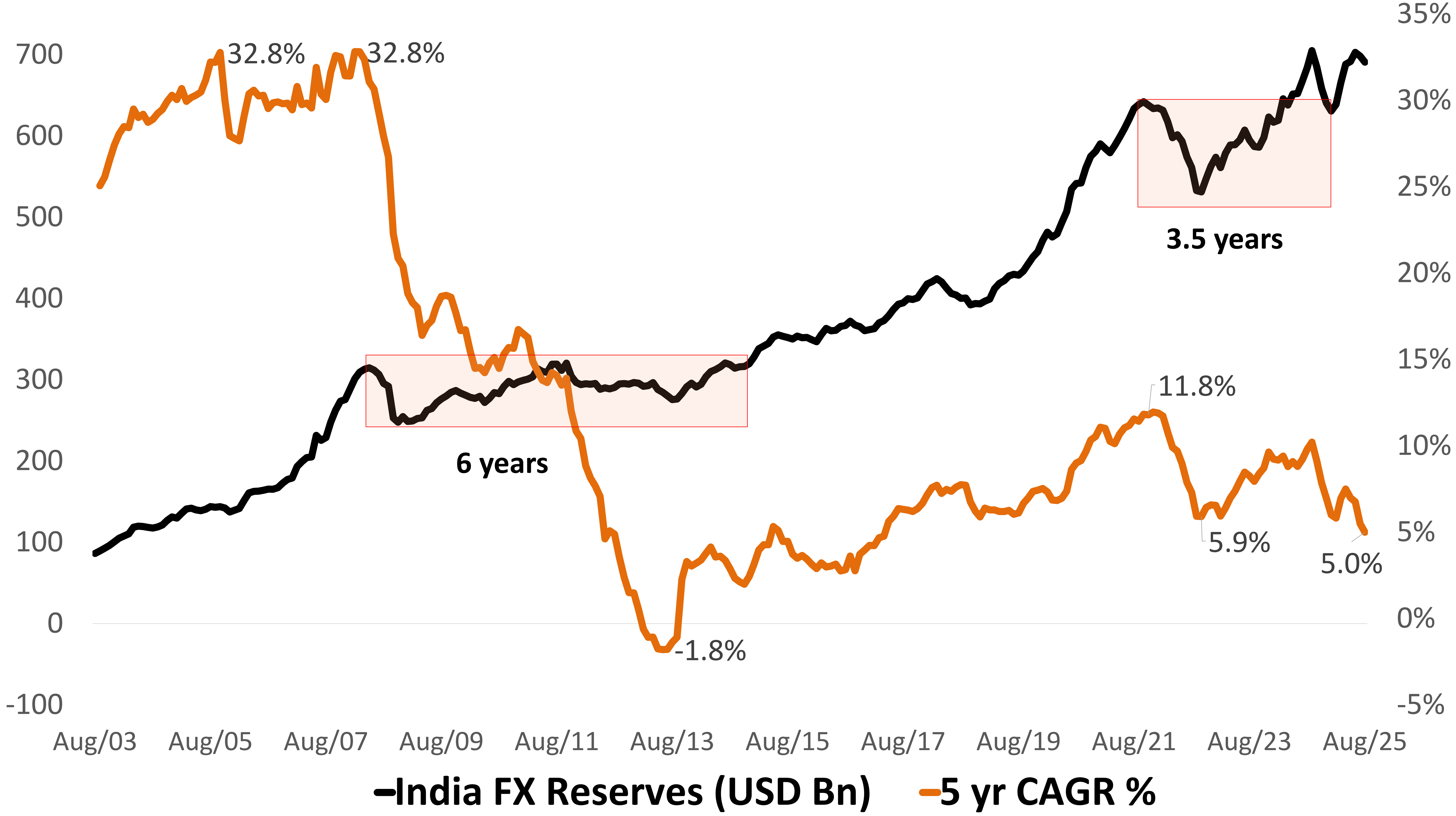
If you ignore pricey equity valuations and markets stay irrational, your mistake may be hidden for a while. You can also dilute risk through cross-asset allocation. If you are a bond investor who buys long duration just before rates rise, you can still hold to maturity and collect the promised coupons. In short, errors in stocks and bonds can often be managed by staying conservative.

Ignoring a lifetime low on a currency is different. It is a serious mistake.

FX markets involve a wide mix of real and financial participants. A currency that breaks a lifetime low does so despite the central bank, the biggest counterbalancing force.

The Indian rupee has hit a lifetime low against the USD at a time when the US Dollar Index is not particularly strong. We have discussed many drivers of this trend. A clear tell is the failure of FX reserves to rise. This is a signal to remain vigilant to spillover into bonds & stocks.

India's FX Reserve Accretion has Slowed To 2013 Crisis Era



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Source: CMIE, DSP. Data as of August 2025

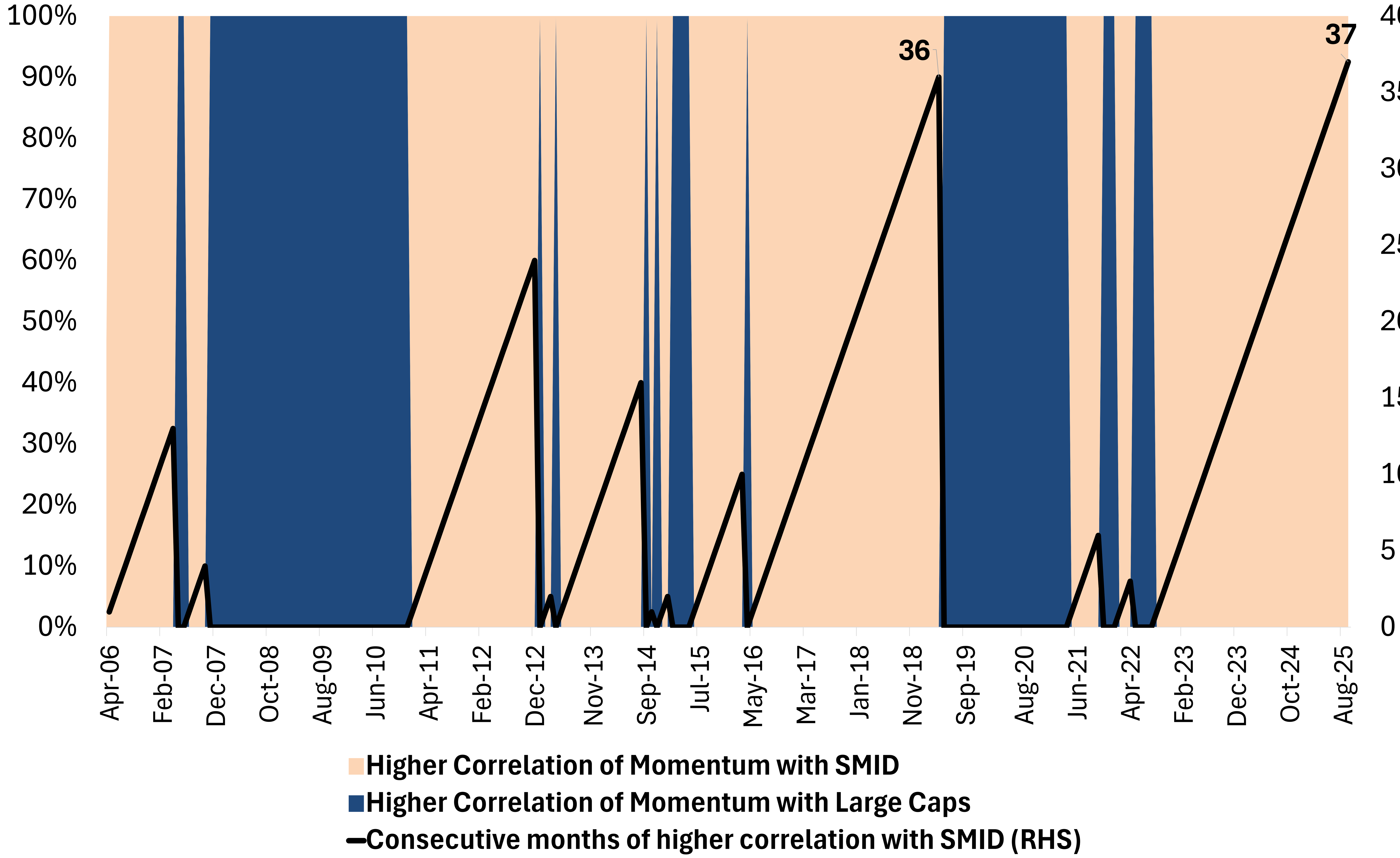
SMIDs Are The Momentum Factor. All Factors Mean Revert

The chart illustrates the relative correlation of the momentum factor across market segments. The blue area indicates that the momentum factor has a stronger correlation with large caps compared to the SMID (small- and mid-cap) segment, while the orange patch reflects the opposite.

Historically, nearly two-thirds of momentum performance has been driven by mid- and small-cap stocks, largely due to higher portfolio allocations toward this space. At the peak of market cycles, exposure tends to concentrate in SMID stocks; however, when a downcycle begins, these strategies are hit the hardest as widespread profit-taking and selling pressure emerge in prior winners.

Over the past three years, momentum has consistently favored the SMID segment, a trend that itself is unprecedented. Yet, this tilt has also contributed to significant underperformance versus broader indices in the past year. With SMID valuations already elevated and momentum still biased toward this segment, the forward outlook for the momentum index appears challenging.

Momentum factor driven by SMIDs is now at it's longest streak.



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Source: Bloomberg, DSP, Data as of Aug 2025.

For Momentum we have considered Nifty 500 Momentum 50 TRI. For Large Caps we have considered Nifty 100 TRI and for SMID we have considered Nifty Midsmall 400 TRI.

The correlation is 1 year rolling of monthly returns.

Tariff, Gold Hoarding, Gold Mining.

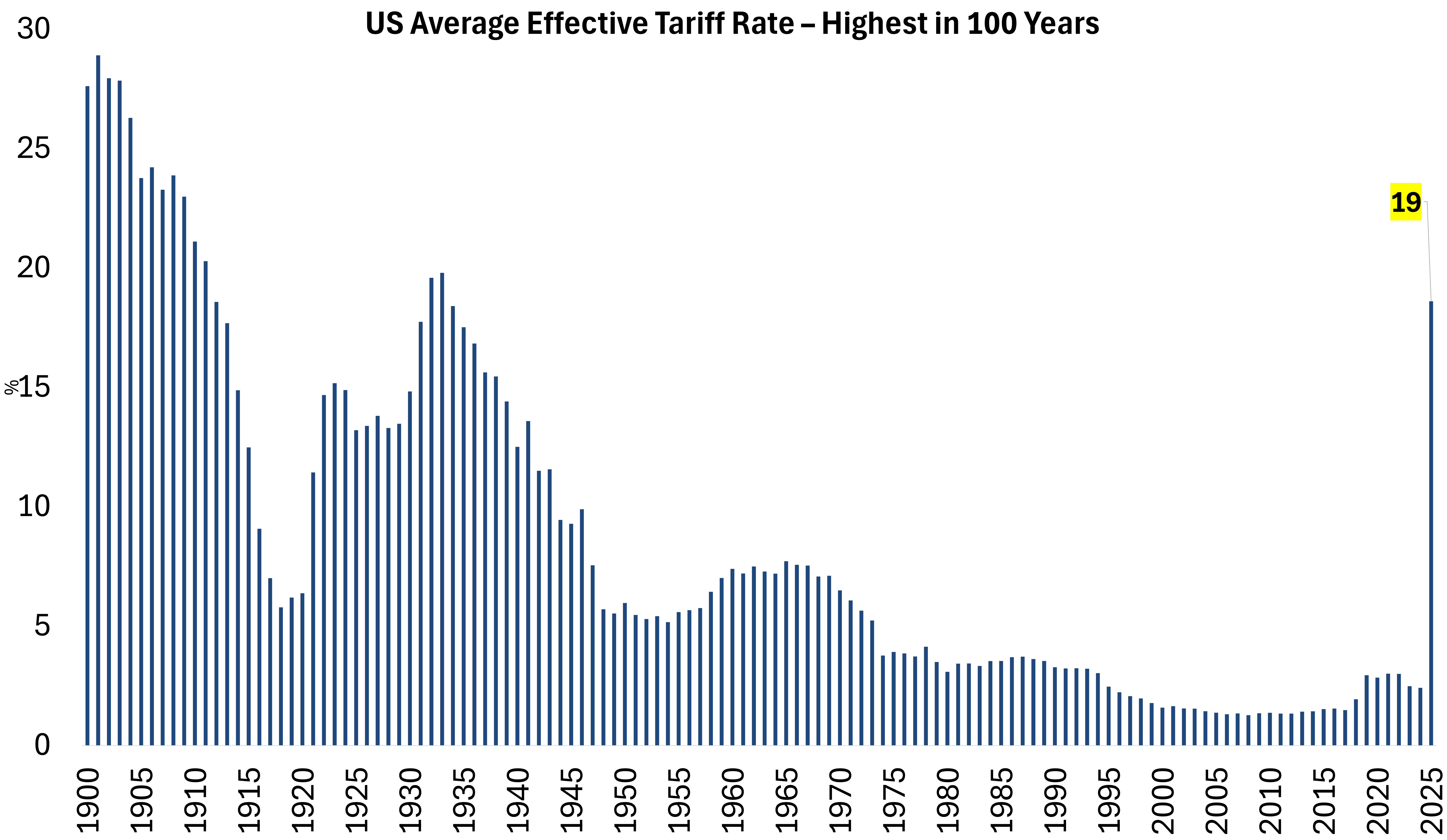
Tariff Impact Is Beginning To Show In Data

US tariffs have jumped from a 2–3% weighted average in 2024 to the high-teens today, while the USD is 8–10% below its peak over the last 6–7 months.

This double squeeze raises import prices (unlike 2018, when a stronger USD had offset China tariffs), with the burden skewed to lower-income households (goods-heavy baskets) amid reduced freebies/transfers.

High-frequency data signal cooling demand: real PCE has been flat for ~6 months, home inventories are near record highs, construction is stalling, and NFP gains are <50k on a 3-mma. Tariffs may spur select capex, but the US CAD should narrow. This would be potentially deflationary for global imbalances.

The negative impact from tariff will likely intensify if they continue to remain in force.



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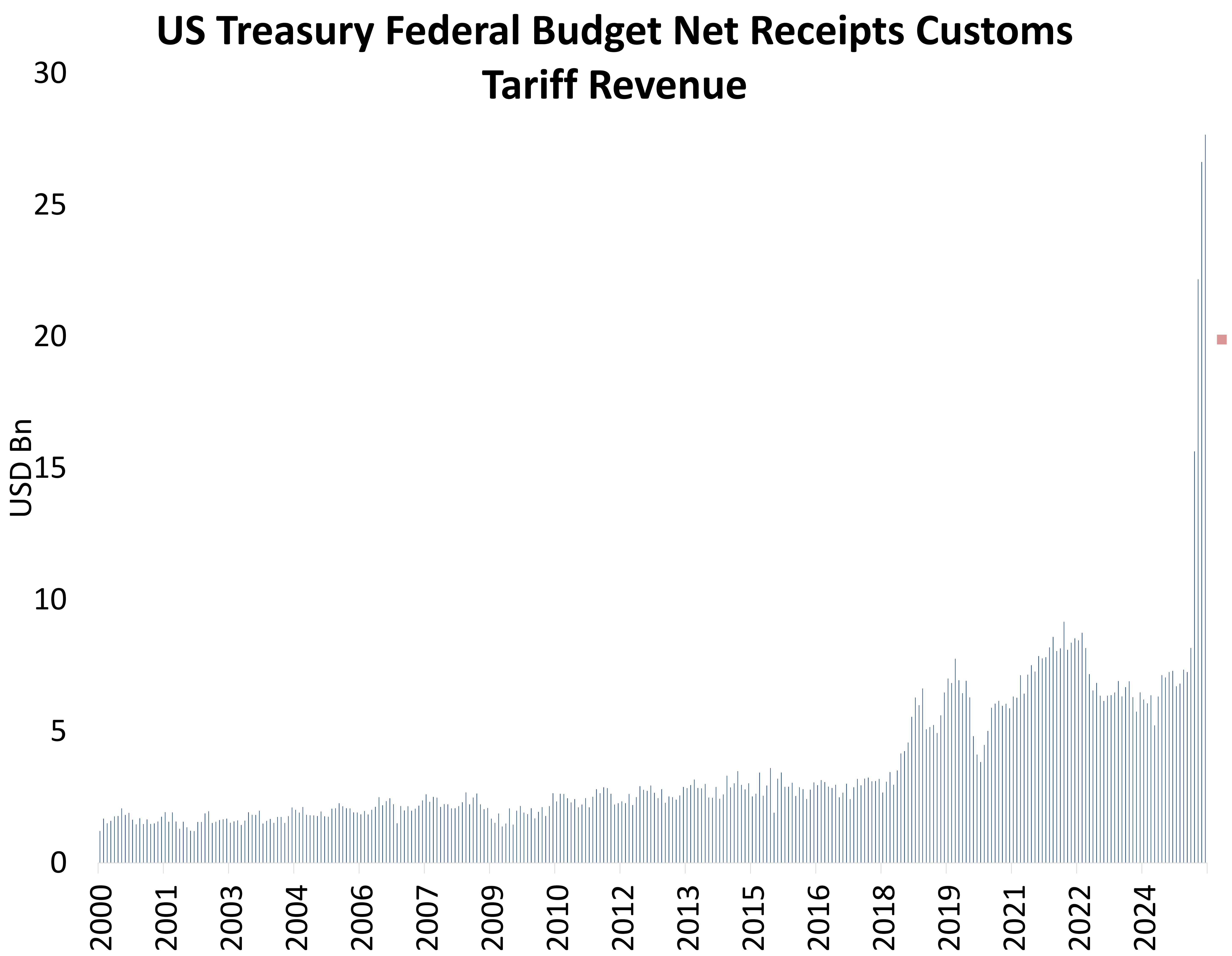
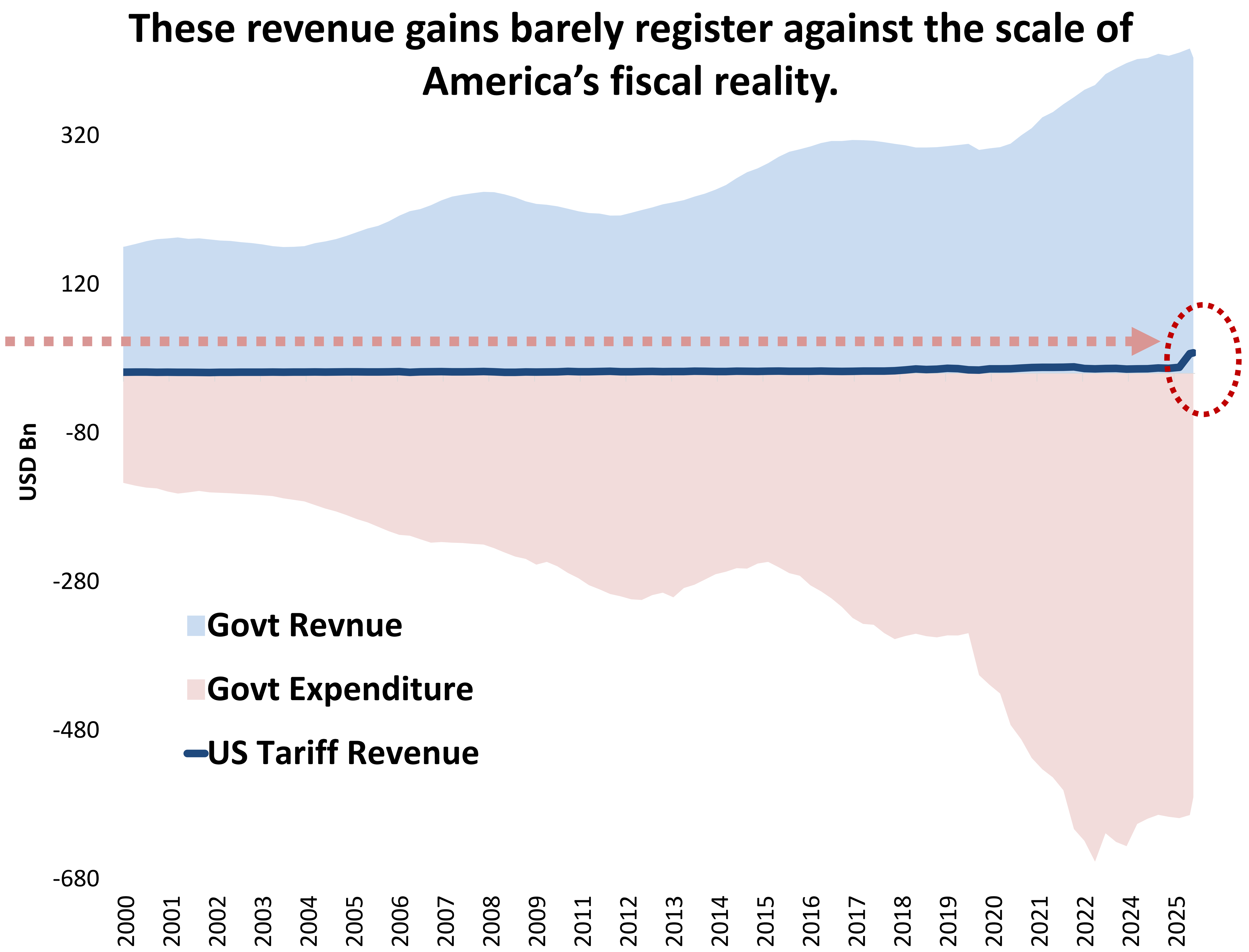
Source: Yale Budget Lab, Bloomberg, DSP. Data as of August 2025. NFP – Non-Farm Payroll.

Tariff Revenues Are Doing NOTHING To Cure US Fiscal Imbalance





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Source: Yale Budget Lab, Bloomberg, DSP. Data as of August 2025.

India's Tariff Could Become A Problem If Trade War Becomes Multilateral

India's exports to the US make up 20% of total exports, the single largest share. The top 10 destinations together account for half of India's exports. Within that, the US stands out as critical.

Some numbers highlight the scale of impact:

- Electronics: One of the few segments to have grown meaningfully over the past decade. Within this, smartphones – about one-third of electronic exports to the US – face 0% tariffs and remain exempt.
- Manufactured Goods: Chemicals, textiles, leather goods are under pressure from tariffs.
- Gems & Jewelry: Of the $30 billion India exports, 40% goes to the US, where the average tariff is a massive 52%.

The key risk is not just the tariff imposition by US. Trade wars are seldom bilateral. If this continues, the trade war can become multilateral, and the tariffs can broadly increase.

Tariff Imposition by US to have insignificant impact until it becomes multilateral

	India Merchadise Exports				
	To USA			To Rest of the World	
	2023	2025		2024	
		$87 Bn		$438 Bn	
Export Product	Tariff (2023)	Tariff (Jul'25)	Export Revenue (2024)*	Tariff (2024)^	Export Revenue (2024)
Petroleum products	0.0%	1.1%	3.1	1.3%	60.2
Agricultural & allied products	2.1%	51%	11.0	4.4%	40.3
Ores & minerals	0.4%	40%	0.3	1.2%	5.0
Manufactured goods	2.7%	32%	54.1	3.2%	257.4
Leather & leather manufactures	7.9%	56%	0.5	2.9%	4.1
Chemicals & related products	1.3%	24%	16.5	1.7%	45.5
Engineering goods	1.4%	36%	17.0	2.8%	92.6
Electronic goods	0.5%	16%	10.5	1.7%	30.3
Textiles (ex readymade garments)	6.6%	54%	2.2	4.2%	17.3
Readymade garments	12.1%	64%	0.9	6.0%	15.1
Other manufactured goods	2.8%	51%	6.5	3.0%	22.6
Gems & jewellery	1.9%	52%	11.5	1.9%	18.4
Other commodities	0.0%	34%	3.6	1.3%	2.7

Source: Global Trade Alert, WITs, CMIE, DSP. Data as of August 2025.

*Breakdown of Export Revenue adds to $83.6Bn. The remaining $3.3Bn is unclassified and can be counted under others

^Based on top 10 export partners

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Gold Hoardings Have Preceded Major Economic Downturns

Gold Event Start	End Date	Gold Event	Gold Hoarding / Price Rise	Economic Downturn	Downturn End	Economic Event	Lag From Gold Hoarding Start (Years)
1797	1821	UK Bank Restriction (gold convertibility suspended)	Hoarding/suspension	1819	1821	Panic of 1819 (US)	22
1834	1836	US Coinage Act 1834 shifts gold-silver ratio; gold inflows	Policy/gold shock	1837	1843	Panic of 1837 & Depression (US)	3
1861	1862	US specie hoarding suspension of gold payments (Dec 1861)	Hoarding/suspension	1873	1879	Long Depression (US NBER contraction)	12
1869	1869	US 'Black Friday' gold panic (Gould & Fisk)	Gold panic	1873	1879	Long Depression (US NBER contraction)	4
1893	1895	US Treasury gold reserve crisis & Morgan bond rescue	Hoarding/run	1893	1897	Panic of 1893 (US)	0
1914	1918	WWI gold hoarding; many suspend gold standard	Hoarding/suspension	1920	1921	1920 to 21 Recession (US/UK)	6
1933	1934	US EO 6102 bans hoarding; dollar devalued to $35/oz	Policy/gold shock	1937	1938	Recession of 1937/38 (US)	4
1968	1971	London Gold Pool collapses; two-tier market Nixon Shock	Policy/gold shock	1973	1975	1973 recession (US)	5
1971	1980	Secular gold bull market to $850/oz (Jan 1980)	Bull market	1973	1975	1973 recession (US)	2
2001	2011	Secular bull: $250 to $1,900/oz	Bull market	2007	2009	Great Recession (Global/US)	6
2018	2025	Renewed bull to fresh records (2020 to 2025)	Bull market	2020	2020	COVID-19 recession (US)	2

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Source: DSP. Data as of August 2025

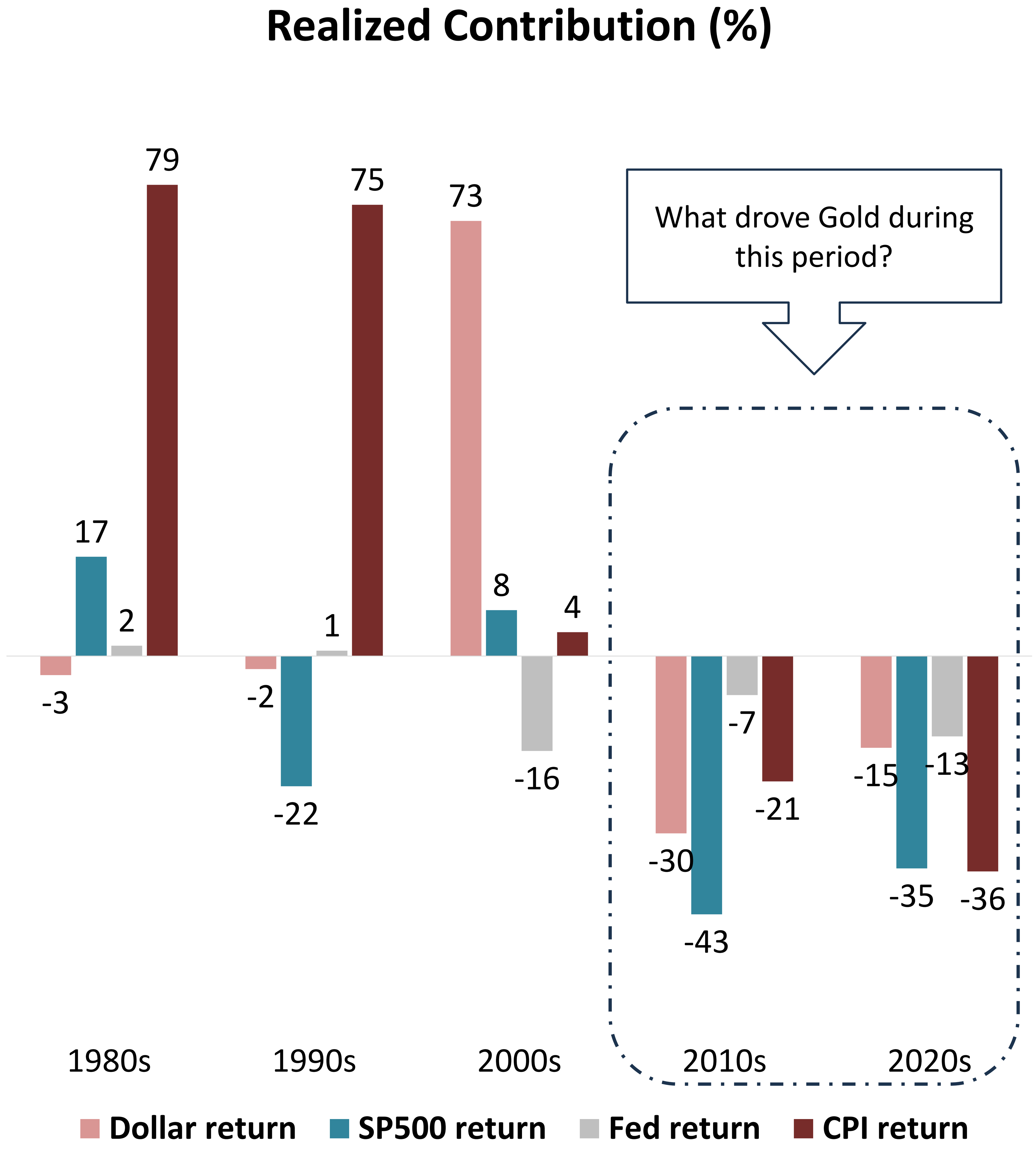
This Bull Market In Gold Is Driven By The 'Gold Put'

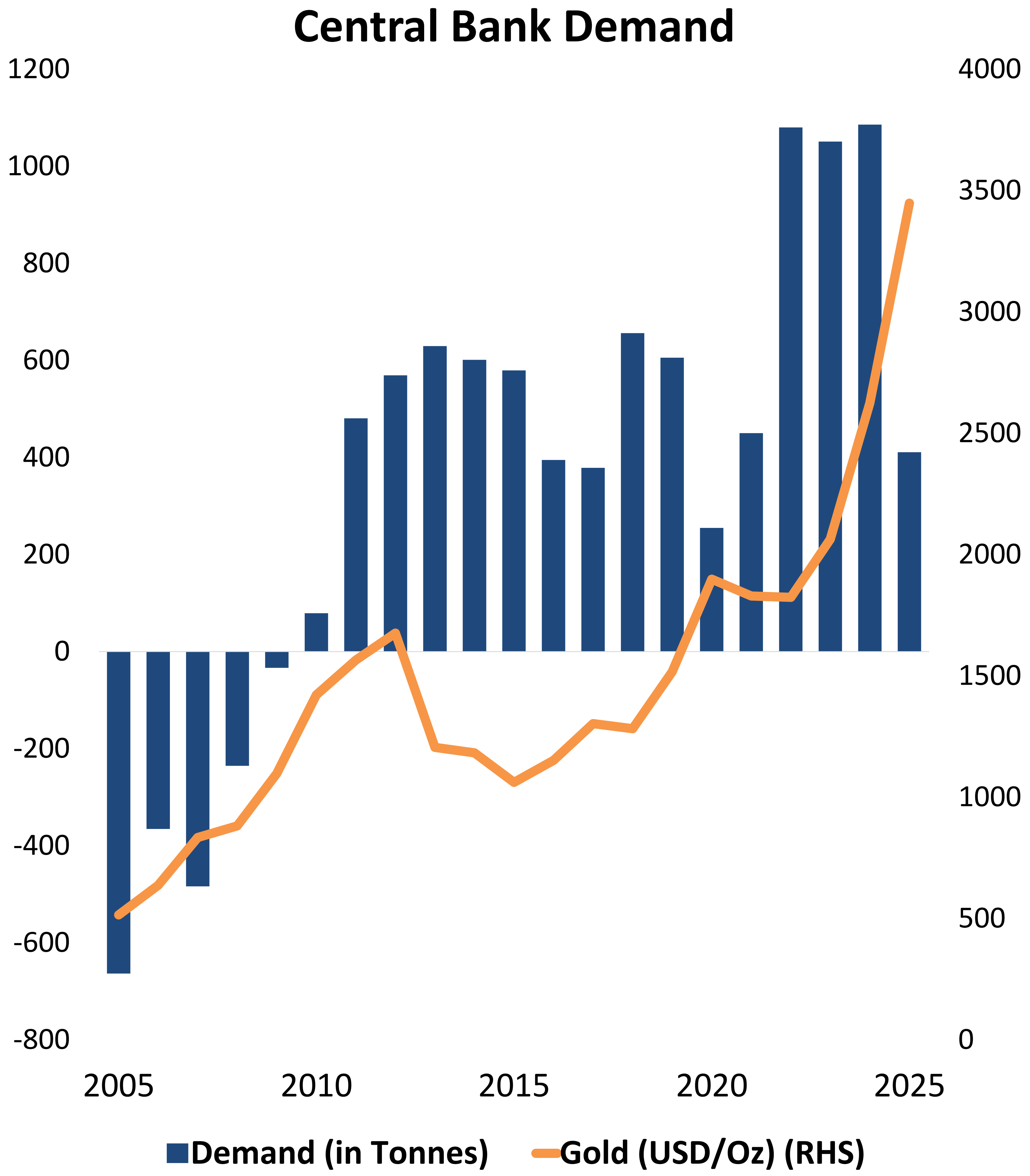
The chart on the left panels examines the realized contributions of key factors influencing gold returns: the US dollar, S&P 500, Federal Reserve policy rates, and consumer price inflation e.g., in 2000s the Gold rally was largely attributed to weakening dollar.

Over the decades, these drivers have shifted in importance, with traditional financial variables such as the dollar, equities, and Fed rates often acting as headwinds to gold's performance in recent years.

Despite these pressures, gold has remained resilient, supported by a structural surge in central bank demand since 2022. Especially after the Russia-Ukraine war where US used the USD as an instrument to sanctions other countries. This lead to the emergence of the 'Gold Put'. Gold Put is the consistent, less price sensitive, Gold hoarding by central banks of various countries as an alternative to US Treasuries. These holdings are part of their reserve asset, an attempt to create an alternate to USD in FX reserves by various central banks. For now, there are no signs of 'Gold Put' being abandoned.

Gold Put – Massive Central Bank Buying Driving Gold Even When Most Factors Aren't Supportive





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Source: FRED, Bloomberg, World Gold Council, DSP. Data as of August 2025.

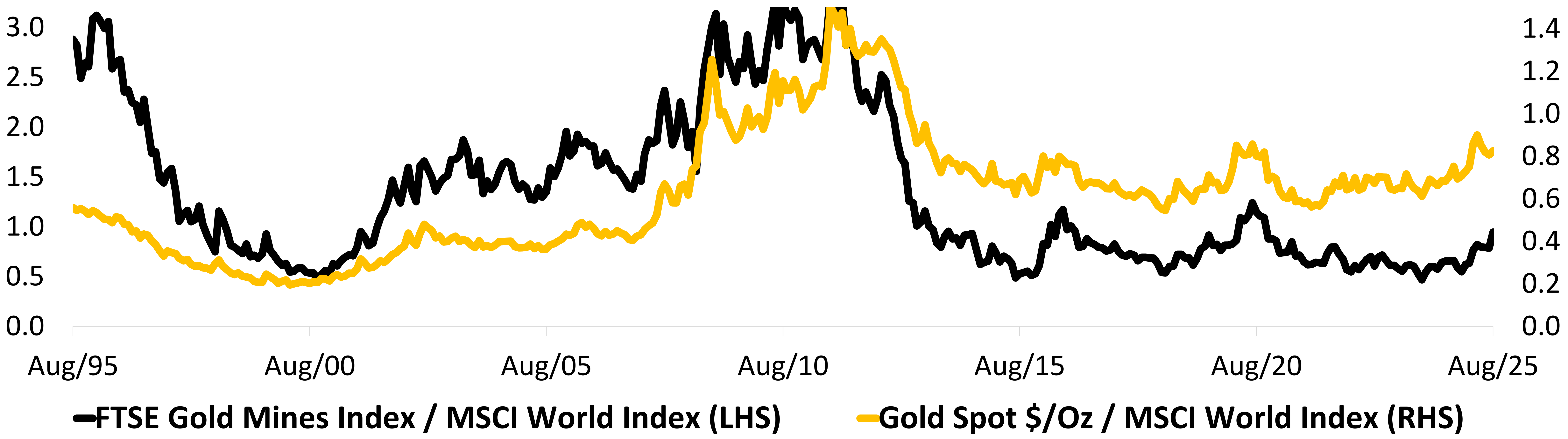
Gold Miners – Where Are We Now?

Gold mining firms and Gold, both underperformed stocks over the last 10 years, until April 2024 when we wrote about them. Gold mining firms had their own 'dot com' bubble at the peak of the last cycle in 2011.

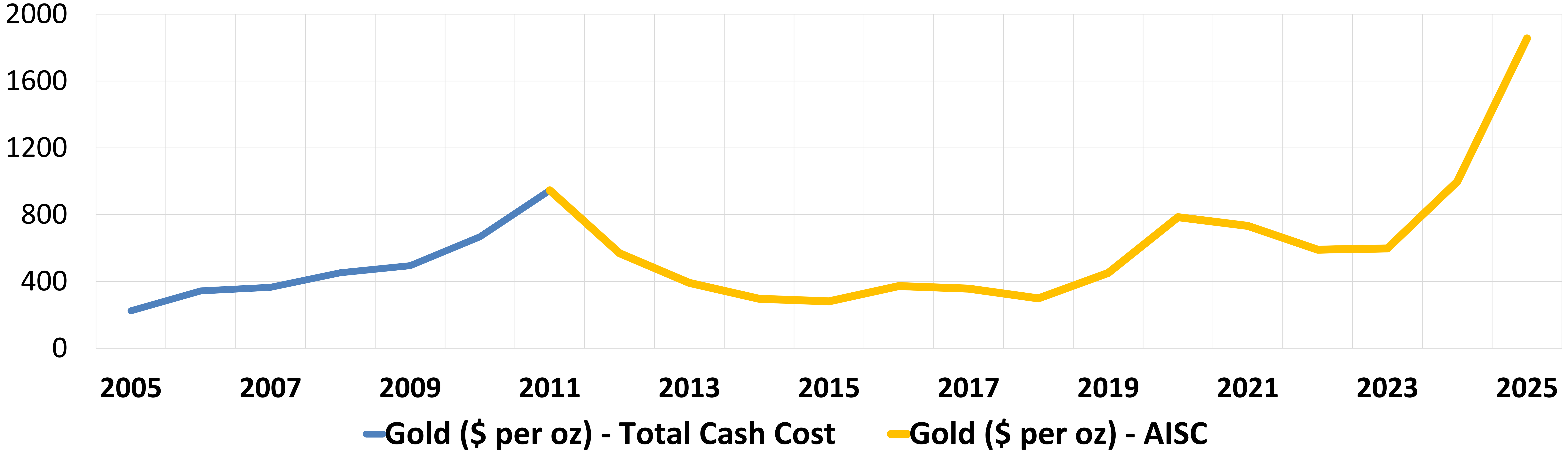
The firms were deep neck in debt, were doing record capex and guiding for higher Gold prices, forever. Anybody who had seen the 1999 to 2011 Gold bull run would have made similar assumption. But Gold peaked and miners were left with huge debt to service amidst declining top line, challenged profit margins and to hurt the sector more, Crude oil prices traded over $100 for the next 3 years. This was sort of 'worst of all worlds' scenario for this sector. The sector went through a derating over the next decade. The market leader, Barrick Gold, rerated from 40x PE to 16x PE through the cycle.

Over the past one year, a massive rally in Gold prices, stable oil prices and disciplined CAPEX by miners have brought them to record profitability. The current Gold price minus All in sustaining cost is at a level where miners continue to look attractive.

Gold Miners Have Begun To Outperform The Broader Markets Based On Improving Profitability And Balance Sheet Strength.



At $3400 Gold Miners Profitability Has Gone To Levels Never Seen Before



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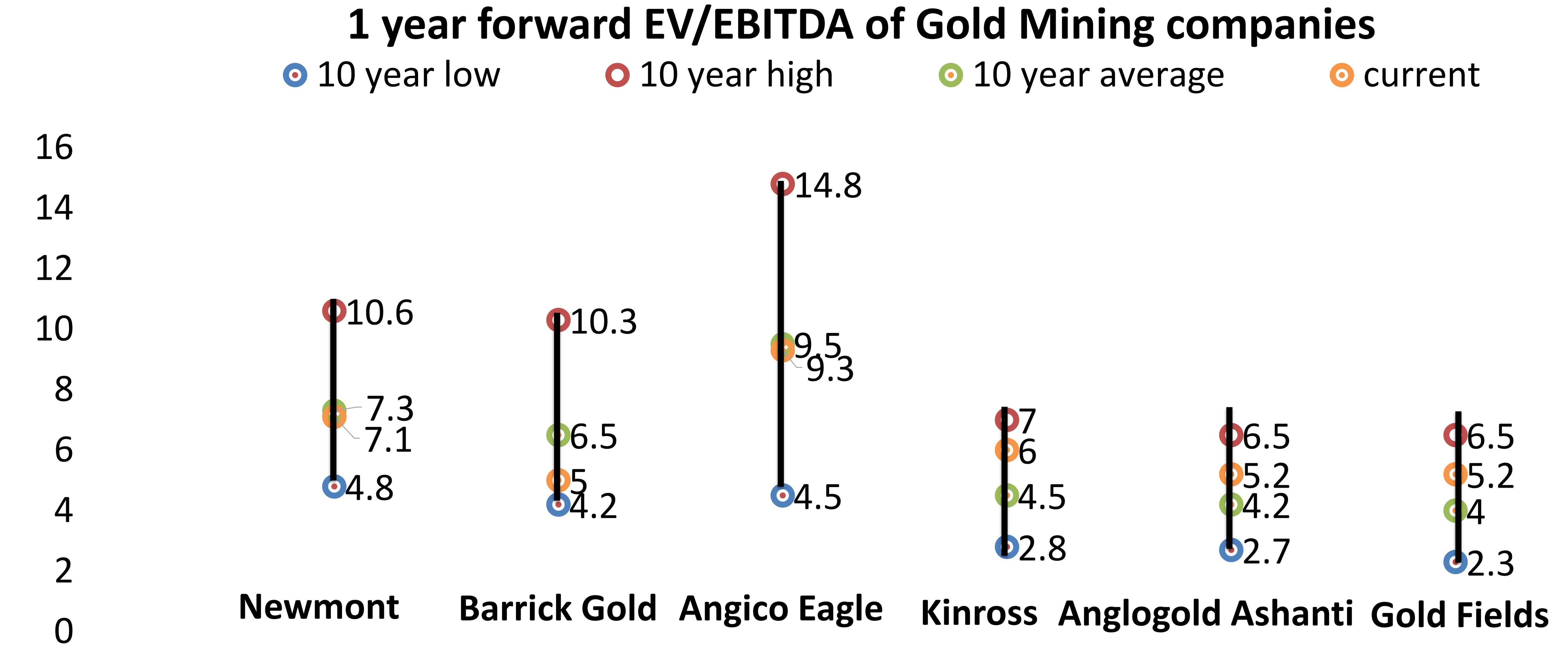
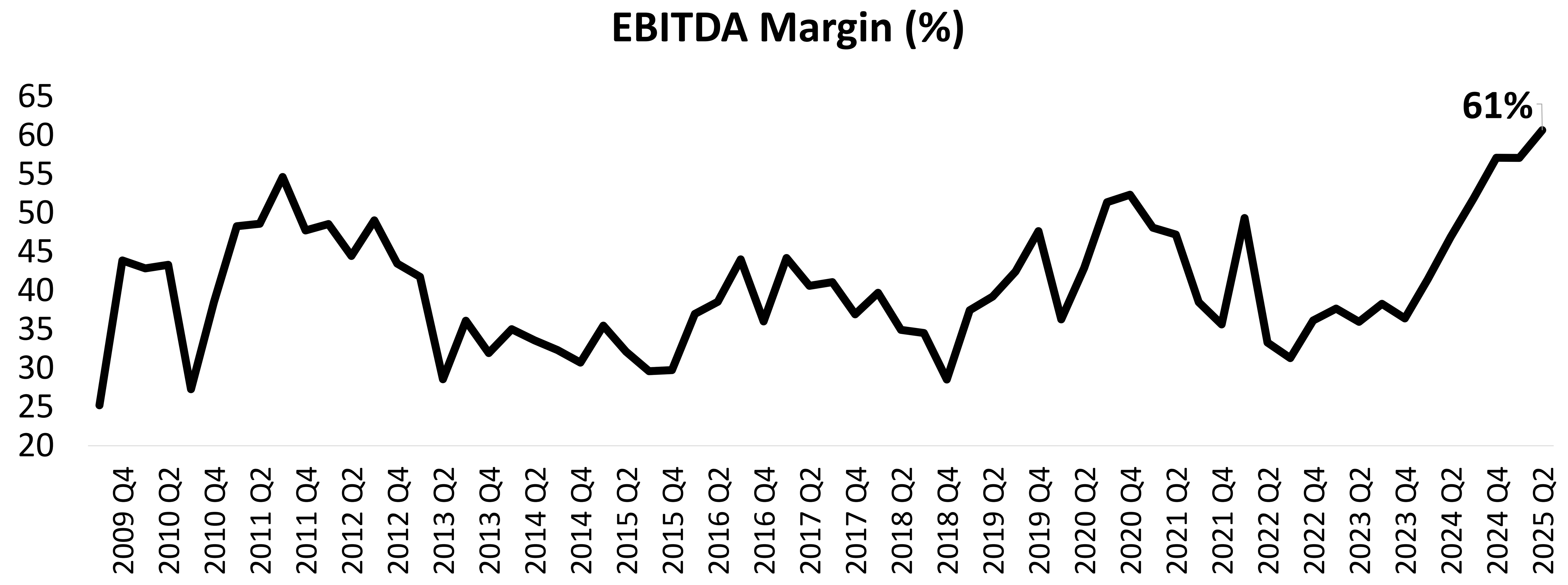
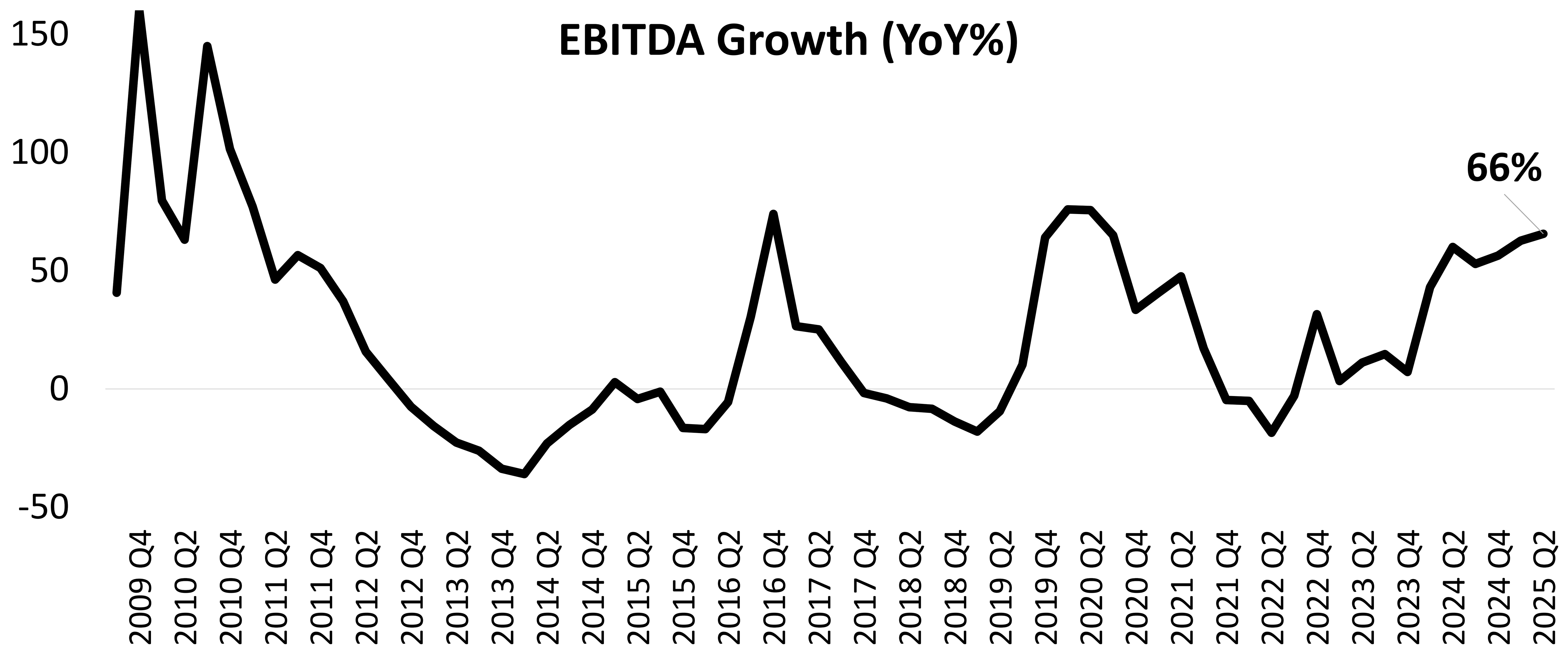
Source: DSP, GFMS, WGC, Bloomberg Data as of August 2025. TCC is Total Cash Cost (GFMS), AISC is Industry Average All In Sustaining Cost (Read: TCC & AISC)

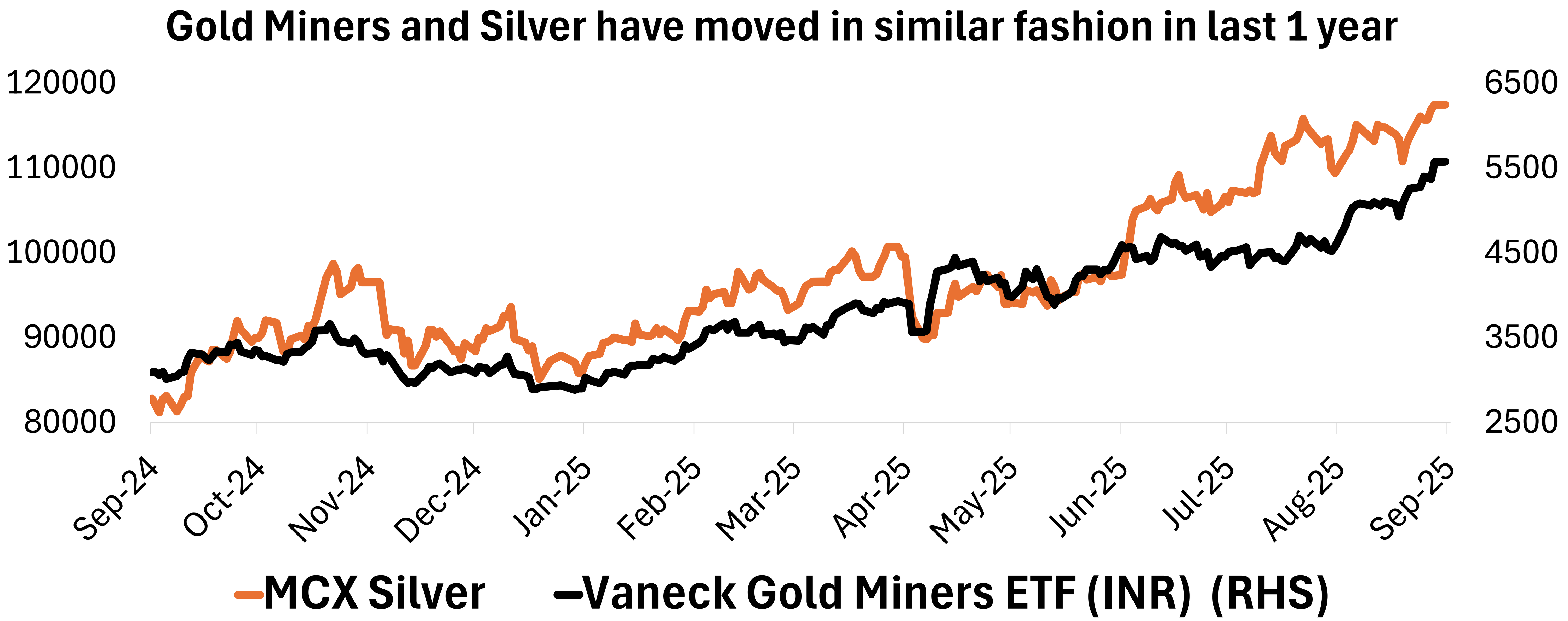
Gold Miners – Valuations & A Proxy Play

Gold Miners Are No Longer At Cheap Valuations But Are Still Close To Average. Investors Should Allocate Based On their Portfolio Weights.









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Source: Bloomberg, DSP, Data as on Aug 2025. All data is of senior gold mining companies.

Technology Sector Dwarfs Others

Tech Isn't Capital Intensive? What Economic Value Is AI Capex Creating?

Tech now dwarfs Oil & Gas in CAPEX. If utilization and cost curves keep improving, AI spend becomes the digital economy's infrastructure. But at what cost?

Are the economic gains from ~US$1T in AI build-out greater than the tangible, visible gains from Oil & Gas? Oil & Gas still accounts for over 50% of world energy consumption by source. What does AI drive at a commensurate scale?

On S&P 500 definitions, Oil & Gas—the so-called "sunset" sector carries ~US$1.6T in market cap, while Technology, the anointed "future", stands near ~US$28T. Has the market prepaid too much for that future? Perhaps many times over. The answer hinges on testable unit economics: rising utilization of deployed compute, falling $/inference, reliable power, and proof that AI productivity lifts diffuse beyond tech vendors into the broader economy. Until those show through the P&L, the valuation spread is a bold assumption, priced as inevitability.

As sceptics, we are watching.

CAPEX in USD Billions for Technology Leaders

Year / USD Bn	Apple	Microsoft	NVIDIA	Meta	Alphabet	Amazon	TOTAL
2020	7	15	1	15	22	35	**96**
2021	11	21	1	19	25	55	**131**
2022	11	24	1	31	32	58	**157**
2023	11	28	2	27	32	48	**148**
2024	9	45	1	37	53	78	**223**
2025 YTD	9	65	3	37	53	78	**245**
	59	**197**	**9**	**166**	**216**	**352**	**999**

CAPEX in USD Billions for Oil & Gas Majors

Year / USD Bn	Saudi Aramco	Exxon Mobil	Chevron	Shell	BP	PetroChina	TOTAL
2020	27	21	9	17	12	36	**122**
2021	32	17	8	19	11	41	**127**
2022	38	23	12	23	12	36	**143**
2023	42	26	16	23	14	40	**161**
2024	50	25	16	20	16	42	**170**
2025 YTD	25	12	8	9	7	16	**76**
	214	**125**	**69**	**110**	**72**	**210**	**799**

DSP

Source: Bloomberg, DSP. Data as of August 2025

Technology Market Cap Share Approaching That of The 'DotCom' Bubble

The technology sector market capitalization is now approaching $30 trillion in MSCI ACWI Index. This is equal to the combined valuations of the following 'Sleeping 7' sectors combined:

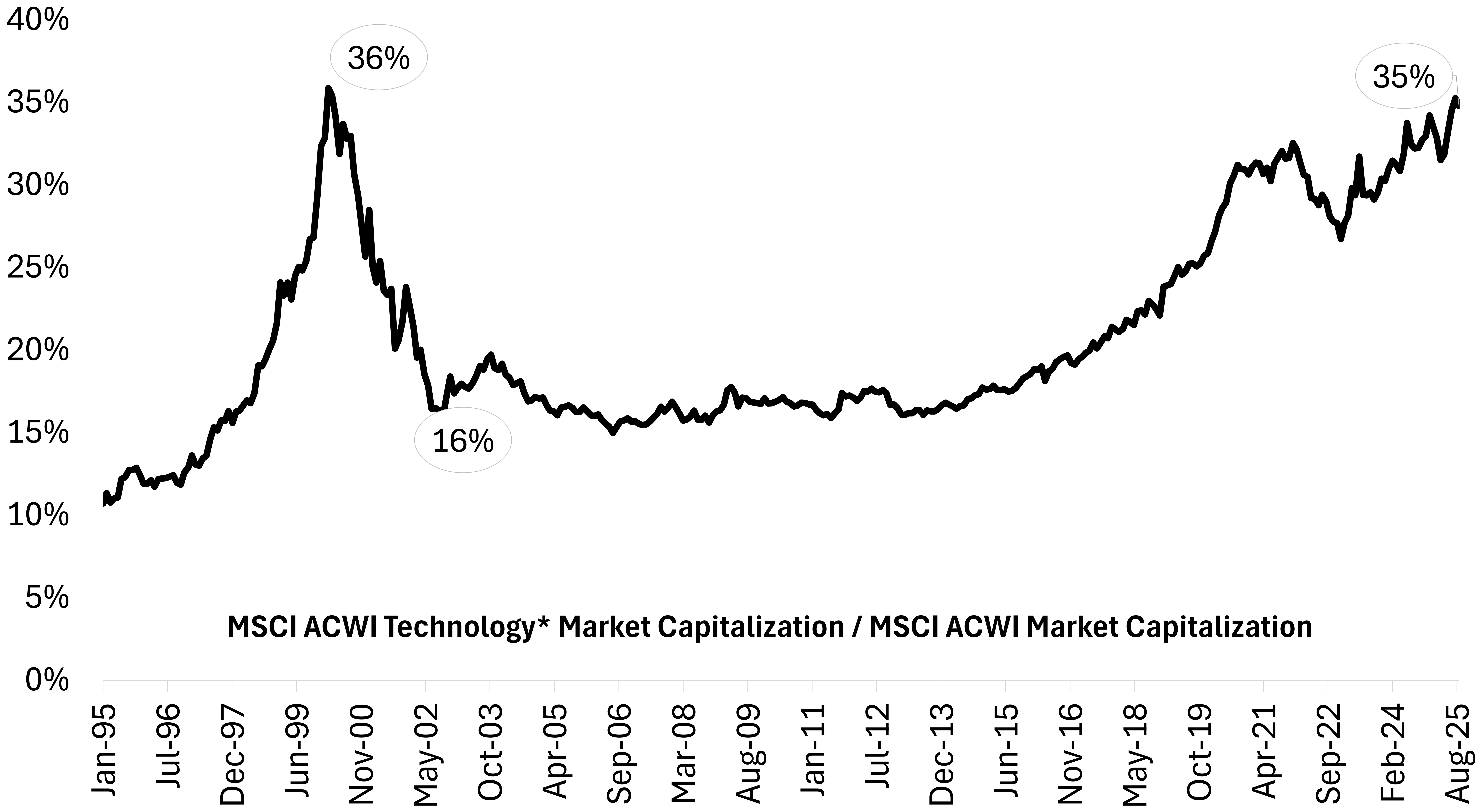
1. Consumer Staples
2. Energy
3. Materials
4. Utilities
5. Real Estate
6. Consumer Discretionary
7. Industrials

The tech sector's implied earnings are about $600 Bn while the 7 sleeping sectors make about $1.5 trillion in net income. The tech sector trades at about 38x trailing earnings while the sleeping 7 trade at about 22x.

The reason is of course the huge differential in ROEs. Tech sector operates at a whopping 25% ROE while the sleeping 7 are at 12%.

The problem is, at extremes, the extremities look very likely to continue. Extrapolation of extremes cause mistakes. Beware.

Technology Market Capitalization Is Rising Towards A Record



Source: Bloomberg, DSP, Data as on Aug 2025.
*Technology includes IT and Communication Services Sector.

Silicon Valley's Secret: Made in China & Taiwan

We often attribute the premium valuation multiples of the "Magnificent 7" to their consistently high ROEs. While it is true that these companies deliver superior ROEs, it is important to recognize that a significant driver of this performance lies outside U.S. borders, in the supply chains and manufacturing bases of China and Taiwan.

In the 1990s and early 2000s, China undertook a strategic push to become the world's manufacturing hub. Supported by government incentives and state-led infrastructure investment, factories were established at scale. For global brands, this meant they only needed to focus on product design, marketing, and distribution, while production was handled cheaply and efficiently by offshore suppliers. This dynamic allowed American companies to compress the margins of their Chinese partners and, in turn, expand their own profitability and ROEs.

However, this model has also created a structural vulnerability. The heavy reliance on Chinese and Taiwanese suppliers means that any disruption whether geopolitical, regulatory, or economic can materially impact margins and profitability across these leading U.S. firms. In the pursuit of higher margins, the most capitalist companies in the world have become overly dependent on the supply chains of a few countries.

Magnificent 7 Companies	ROE*	Operating Margins*	Biggest Supplier	Country of Origin	% of COGS	ROE of Supplier	Operating Margins
Apple	157%	32%	Foxconn	Taiwan	32%	10%	3%
Microsoft	33%	46%	Foxconn	Taiwan	18%	10%	3%
Alphabet	33%	32%	Foxconn	Taiwan	7%	10%	3%
Amazon	24%	11%	Foxconn	Taiwan	8%	10%	3%
NVIDIA	119%	62%	TSMC	Taiwan	33%	30%	46%
Tesla	10%	7%	Contemporary Amperex Tech	China	10%	23%	15%
Meta	37%	42%	GoerTek	China	11%	8%	3%

DSP

Source: Bloomberg, DSP, Data as on Aug 2025.
*Green highlight is where the ROE and Operating Margin is higher than the Supplier's. The ROE and Margins are of the latest Financial Year.

India Large Cap IT: An Emerging Relative Opportunity

As the global IT landscape appears overheated, Indian IT companies seem relatively better positioned. Several large-cap IT stocks have corrected meaningfully over the past three years, despite their fundamentals remaining largely intact. Current ROE for many of these firms is at or above long-term averages, while valuations have reverted closer to historical norms.

For industry leaders such as Infosys and TCS, earnings growth over the past three years has actually outpaced the shareholder returns generated during the same period, a clear indication of significant de-rating in their valuations.

This disconnect stems largely from the absence of any “AI Froth” in Indian IT majors. Unlike global peers, they have seen removal of frothy valuations and have played a pivotal role as enablers of Generative AI and maintaining strong Total Contract Value (TCV) pipelines.

The IT sector can become an absolute play if price correct further and ‘margin of safety’ emerges. For now, IT is a relative play.

	ROE		PE		EPS Change		Total Returns	
Name	Current*	Average Since GFC Bottom	Forward^ PE	Average Since GFC Bottom	Last 3 Years#	Since GFC Bottom	Last 3 Years	Since GFC Bottom
Infosys	30.6	27.3	22.7	18.1	7%	10%	5%	17%
TCS	50.7	39.1	22.9	21.1	9%	15%	4%	24%
HCL Tech	24.6	25.6	23.2	14.8	8%	19%	21%	31%
Tech Mahindra	15.7	21.8	30.1	15.4	-5%	6%	18%	23%
Wipro	16.3	20.3	19.5	16.6	7%	10%	10%	16%

DSP

Source: Capitaline, DSP, Data as on Aug 2025. GFC Bottom is considered as March 2009. *Green highlight is where Current ROE is higher than Average since GFC Bottom. ^1 Year Forward PE Considered. #Green highlight means EPS growth was higher than Total returns of that Stock. Total returns includes Dividends.

Beyond Averages: What Skewness Reveals About Investing

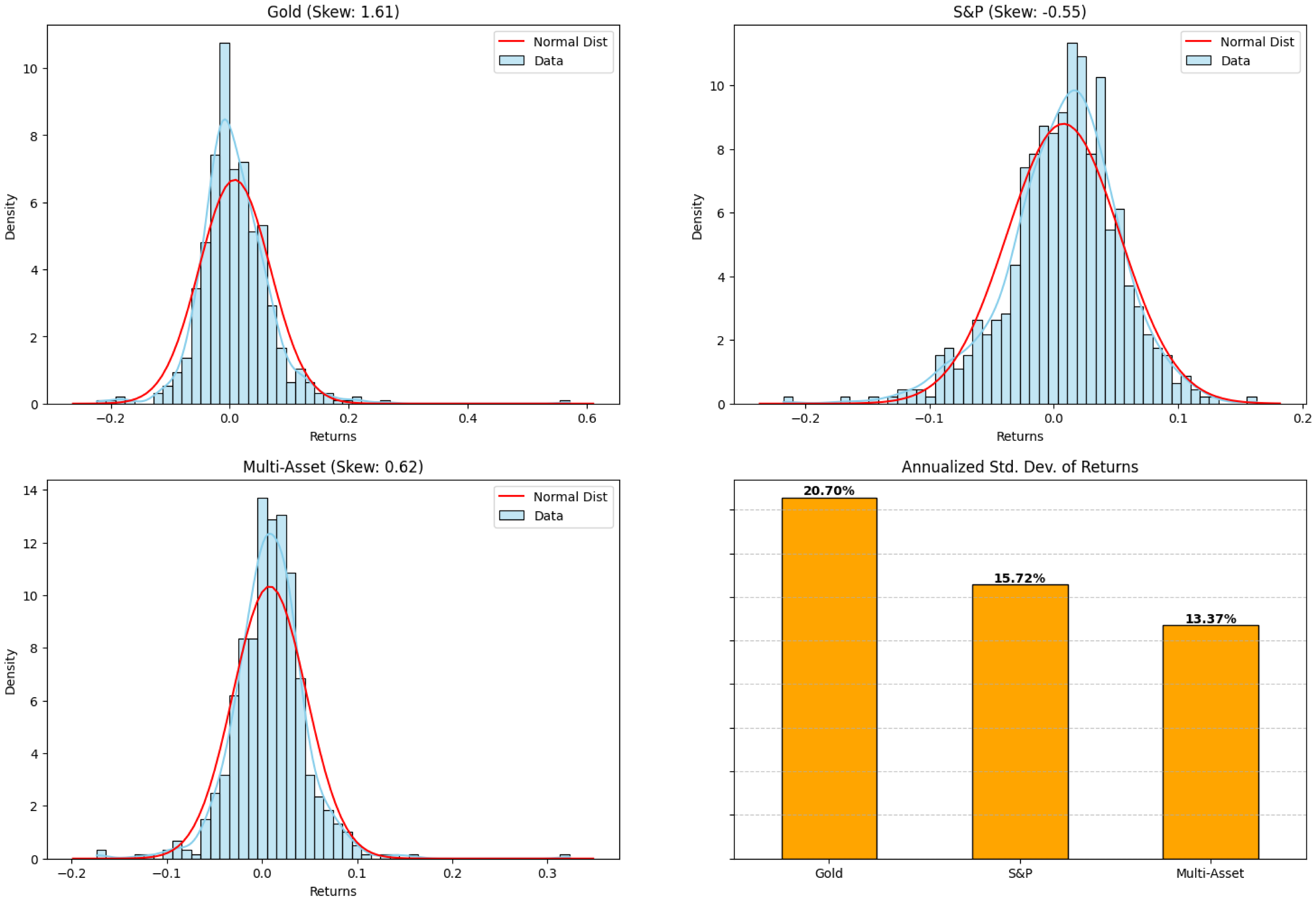
Over the past five decades, asset classes have displayed very different risk and return profiles.

Gold shows positive skewness (1.62), meaning it occasionally delivers outsized upside returns, especially during times of uncertainty, but this comes with relatively high volatility (20.7%).

The S&P, on the other hand, exhibits negative skewness (–0.55), reflecting vulnerability to sharp drawdowns despite lower volatility (15.7%).

A multi-asset portfolio combines these characteristics to achieve a more balanced return distribution, shifting toward positive skew (0.63) while also lowering volatility to just 13.4%.

For investors, this is critical: portfolios exposed only to negatively skewed assets risk being dragged down by sudden market shocks. By blending asset classes with complementary return profiles, diversification not only reduces risk but also creates a smoother, more resilient path to long-term wealth creation—limiting extreme losses while preserving meaningful upside.



Source: Bloomberg, DSP. Data as of August 2025. Data in USD from 1973, Multi-Asset calculation is done based on annual rebalancing (50% each).

DSP ASSET MANAGERS

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