

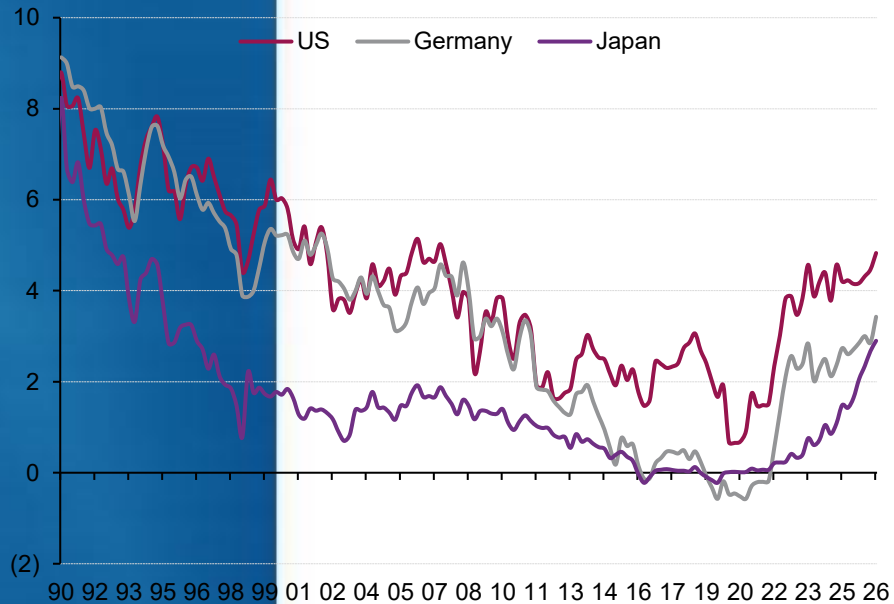
Adapting to higher costs of capital

Institute of Actuaries of India

11th September 2026

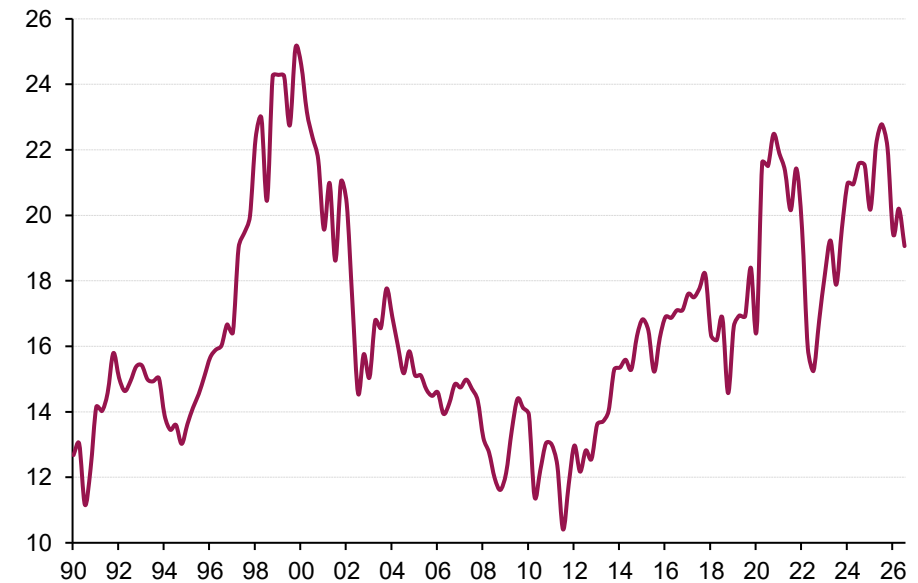
Globally, costs of capital are higher

10y government yields were falling until now



Source: Bloomberg, Axis Bank Research

With equity PE ratios also coming lower from peaks

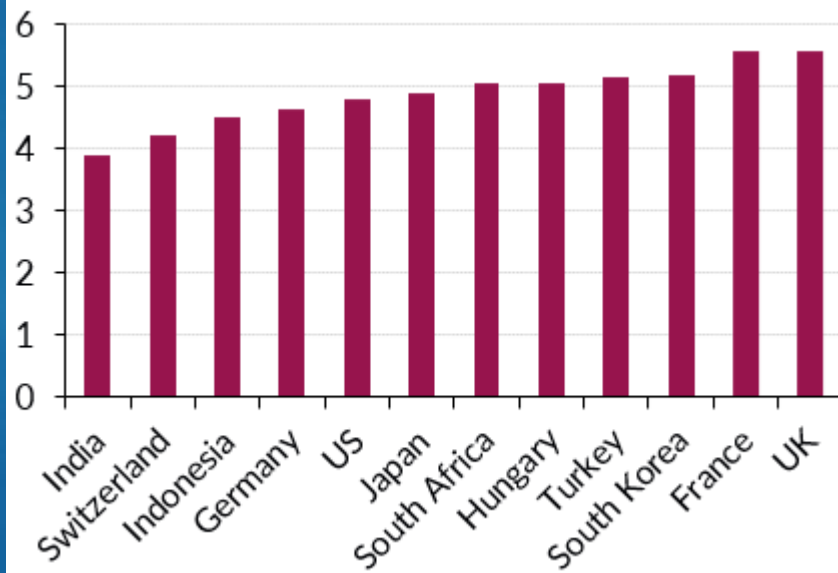


Source: Bloomberg, Axis Bank Research

❑ Costs of capital in both equity and bond markets are rising – this is across countries

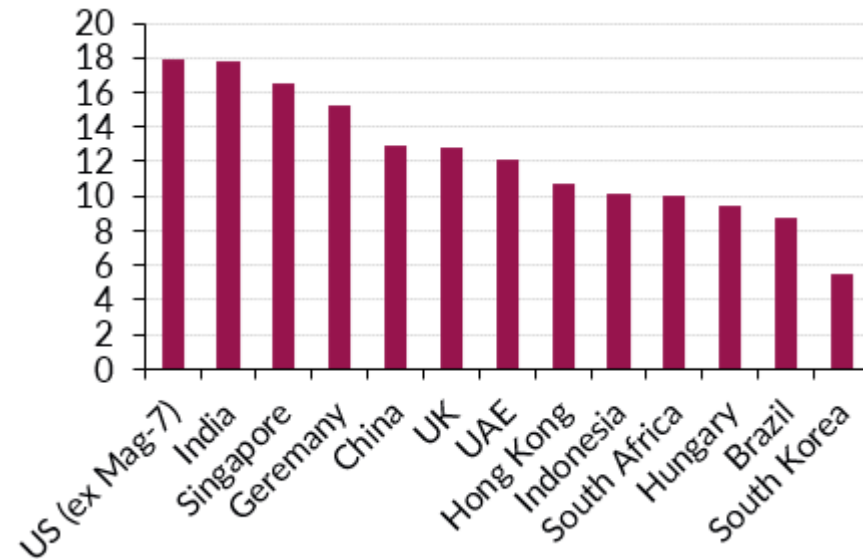
This has yet to fully transmit to India

Fully swapped (in USD) 10y government bond yields



Source: Bloomberg, Axis Bank Research

PE ratios of main equity benchmark index

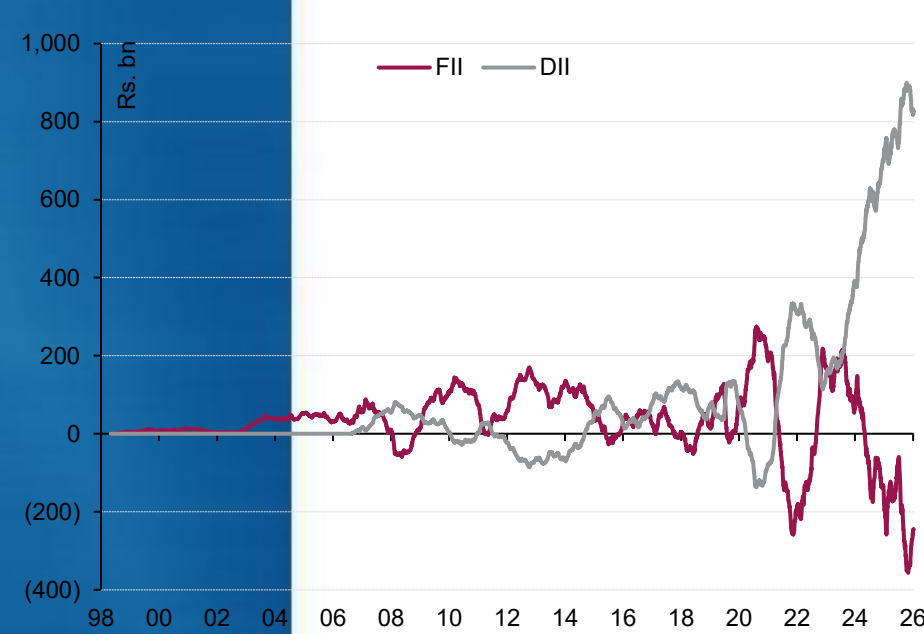


Source: Bloomberg, Axis Bank Research

- ❑ Global costs of capital have reverberated, but adjustment might still be incomplete for India
- ❑ 10y G-sec yields 3.90% on a fully swapped basis – much less attractive than others
- ❑ India equity valuations are also high

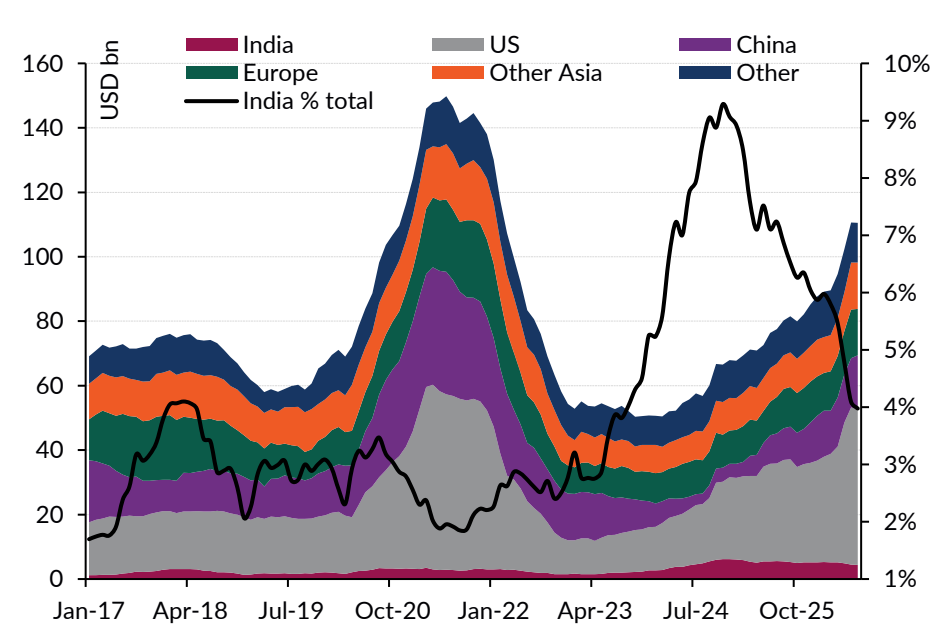
Domestic money is inflating valuations

12m rolling FPI and DII equity flows



Source: Bloomberg, Axis Bank Research

Global IPOs, PE driving



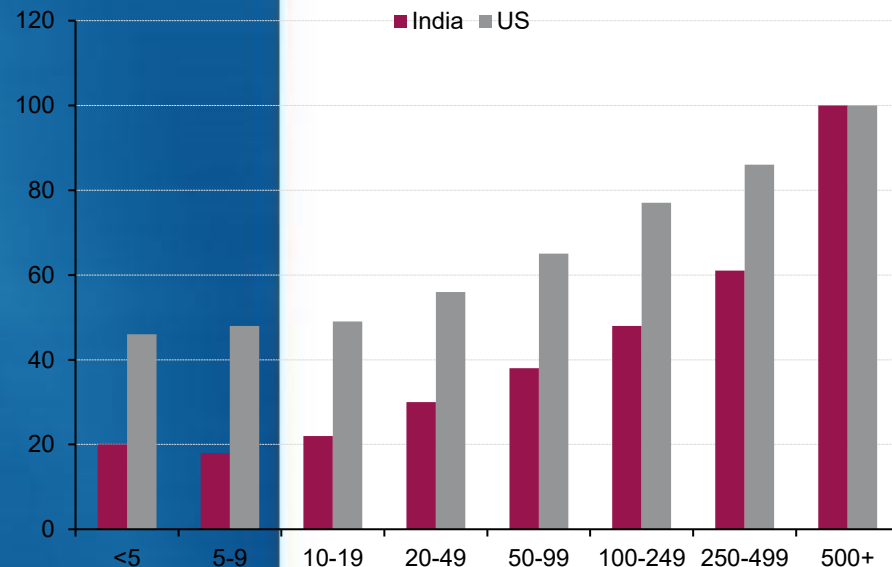
Source: Bloomberg, Axis Bank Research

Period	PE/VC linked IPOs USD bn
31-Jul-26	3.68
31-Mar-26	12.60
31-Mar-25	0.88
31-Mar-24	0.14
31-Mar-23	2.05
31-Mar-22	0.72
31-Mar-21	0.24
31-Mar-20	3.22
31-Mar-19	1.86
31-Mar-18	5.35
31-Mar-17	6.21
31-Mar-16	1.12

- ❑ With the valuation mismatch, foreign investors are selling India assets across the board
- ❑ However, domestic institutions are buying

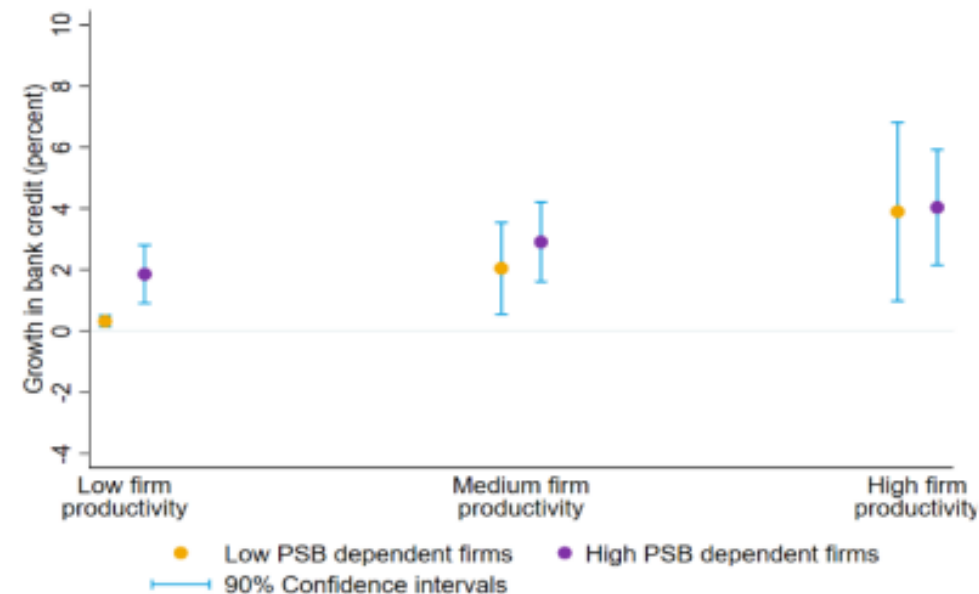
Asset supply domestically is also constrained

Productivity of firms by size, India vs US



Source: IMF, Axis Bank Research

PSBs supply funds to low productivity firms

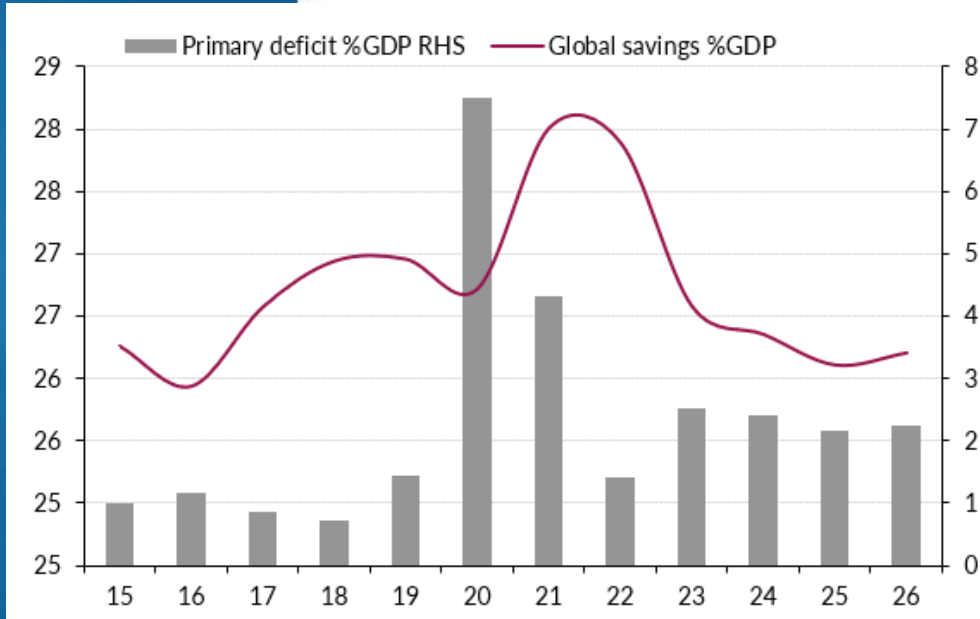


Source: IMF, Axis Bank Research

- ❑ Domestic policy disincentivizes MSMEs from investing for growth – large firms are as productive as in the US, but smaller firms lag – 75% of manufacturing firms employ fewer than 5 workers, compared to 38% in the US. 2% have 100+ workers.
- ❑ Low productivity firms have credit incentivized – limiting equity issuance

Defence drives increases, unlikely to reverse

Global savings have fallen with government spending



Source: Bloomberg, Axis Bank Research

This reflects increase in defence spending, %GDP



Source: Bloomberg, Axis Bank Research

- ❑ The reason global costs of capital are higher is that savings have been consumed in government spending
- ❑ This is defence-driven: given current geopolitics, unlikely to reverse

Thucydides Trap: Rising and established powers drift to conflict

Definition

Coined by Graham Allison from Thucydides' account of the Peloponnesian War. When a rising power threatens to displace a dominant power, fear, mistrust and rivalry can increase the risk of conflict.

Classic Example

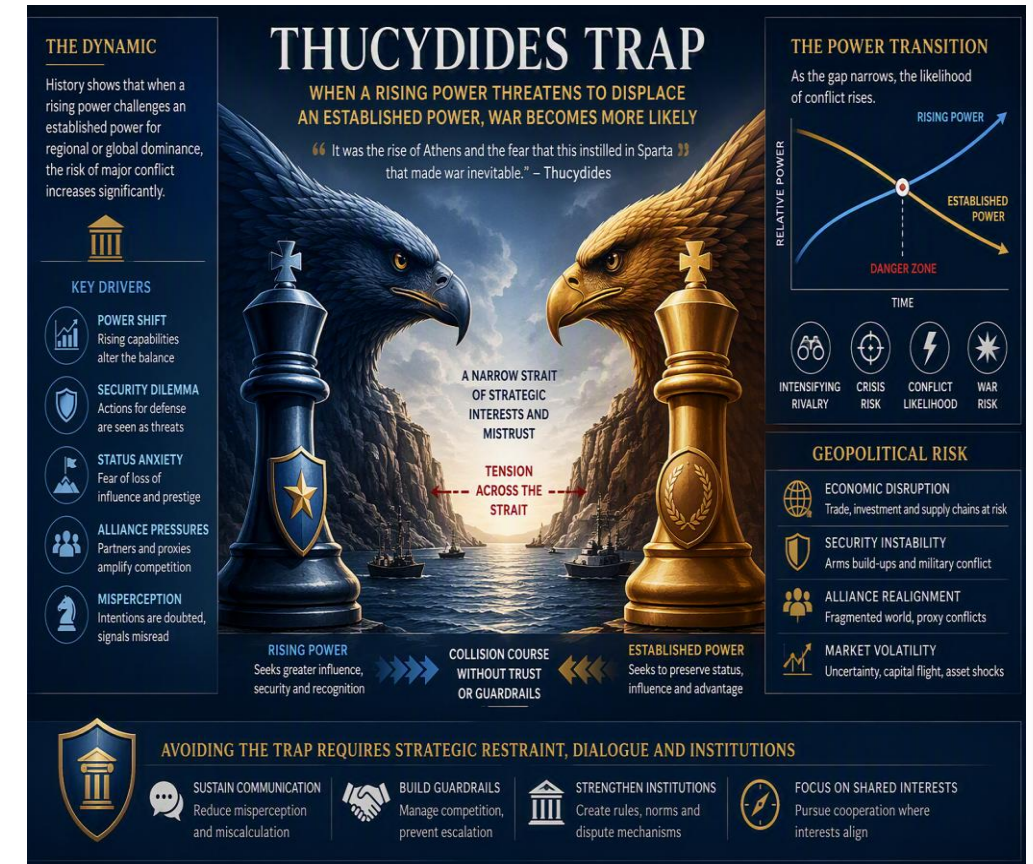
Athens (rising power) vs Sparta (established power)

Key Mechanisms

- Power transition
- Security dilemma
- Misperception and nationalism
- Alliance pressures and arms races

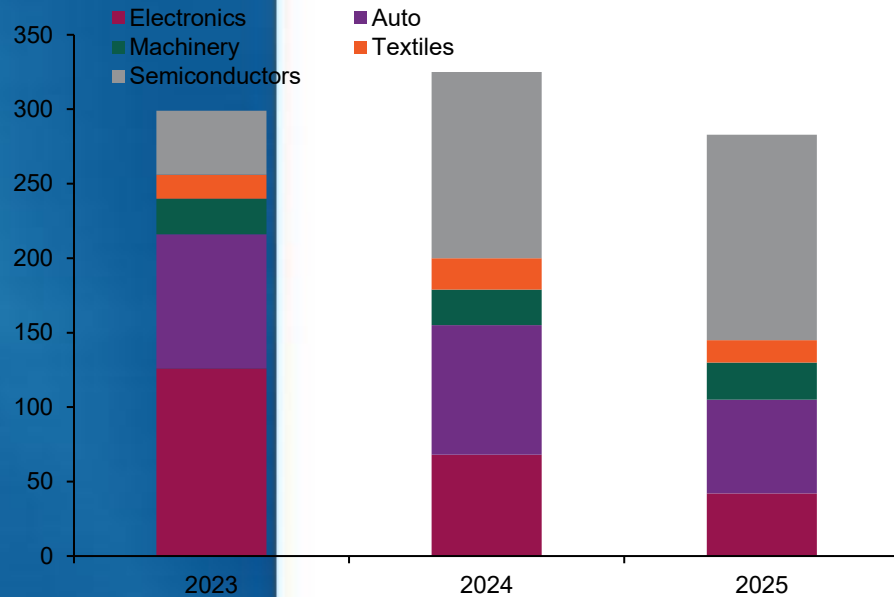
Modern Relevance

Often used to analyze U.S.-China strategic competition. The theory does not predict war is inevitable; strong institutions, economic interdependence and diplomatic guardrails can reduce risk.



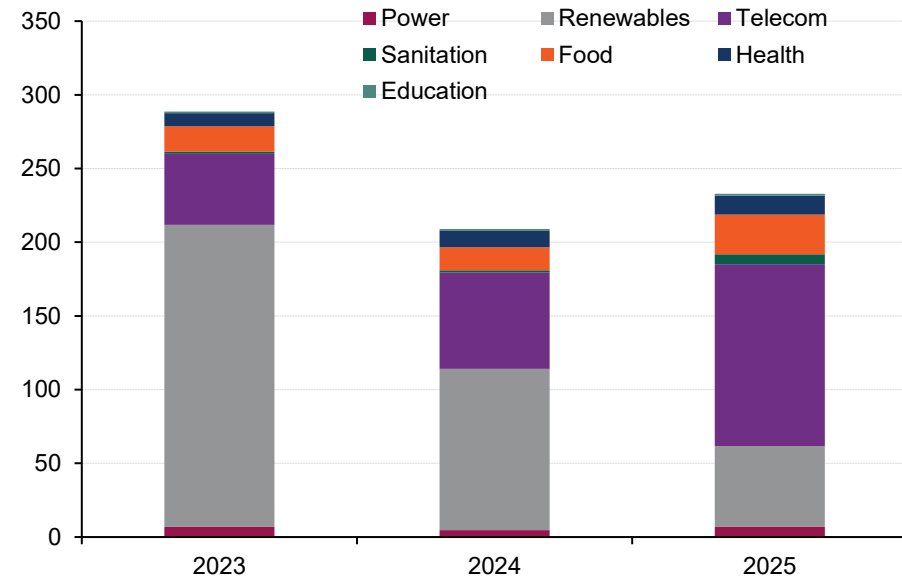
FDI pivoting away from India

Greenfield GVC also pivoting away from India's strengths



Source: UNCTAD, Axis Bank Research

Developing country SDG greenfield also skew towards telecom

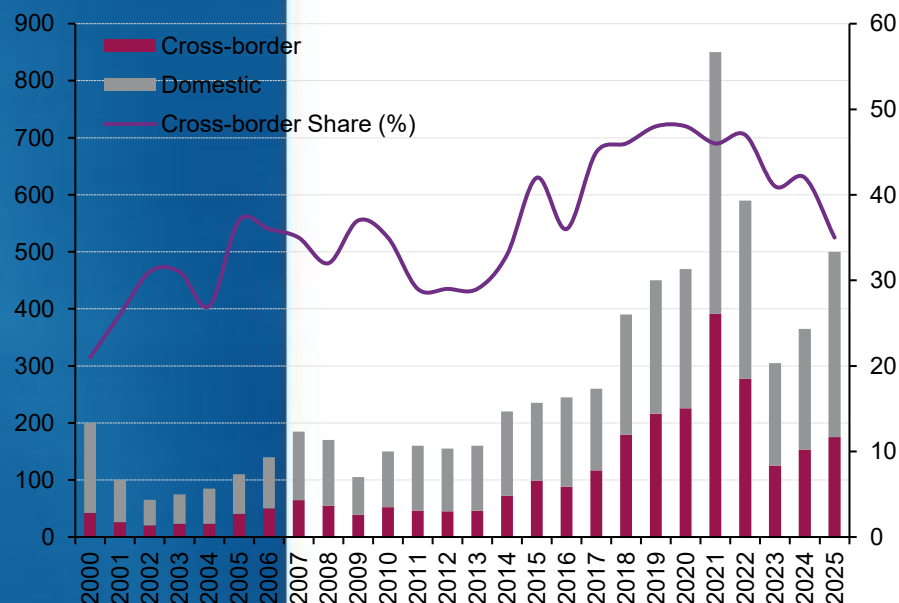


Source: Axis Bank Research

- ❑ The Greenfield GVC universe is shrinking, and even here the pivot is away from electronics and auto, towards semiconductors
- ❑ Sustainable Development Goal (SDG) projects in developing economies are also seeing greenfield flows away from renewables and towards health

The PE investment universe is shrinking

Cross-border PE investment is also below peak



Source: UNCTAD, Axis Bank Research

With the share (USD bn) of middle income countries now lower

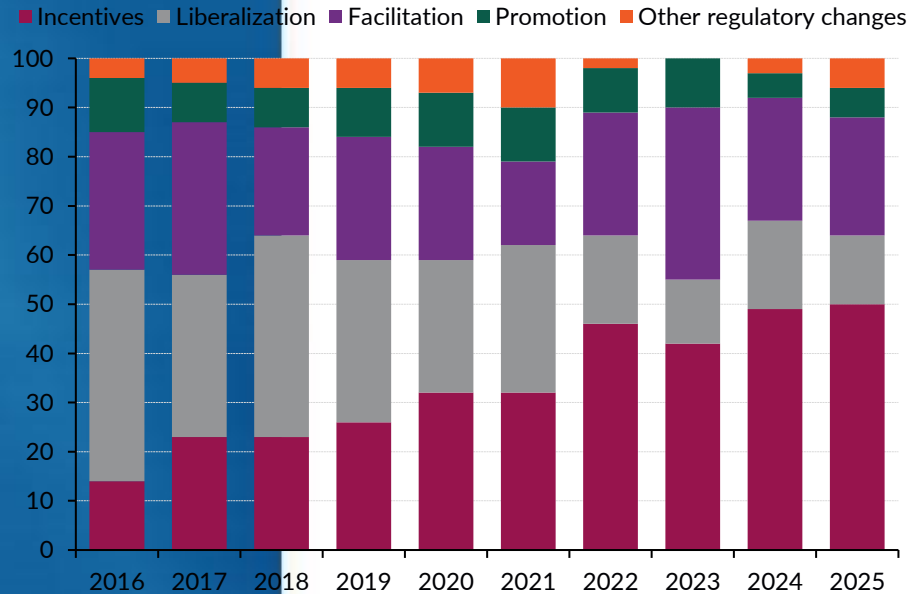
Period	High income	Upper middle income	Lower middle income
2017-2019	71%	19%	10%
2020-2022	75%	11%	14%
2023-2025	86%	6%	8%

Source: UNCTAD, Axis Bank Research

- ❑ PE investment flows are down, with the share of cross-border PE flows also lower
- ❑ Within this, the share of cross-border flows received by middle income countries like India is even more squeezed

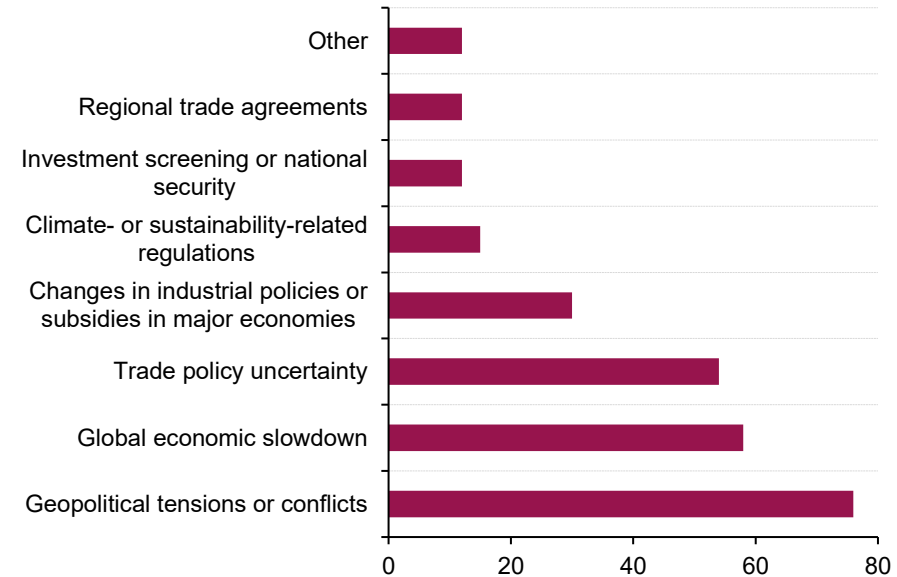
Why? PLI is now a hygiene factor, global uncertainty also at play

Incentives now make up half of favourable FDI measures



Source: UNCTAD, Axis Bank Research

While surveys show uncertainty a large factor of flow slowdown

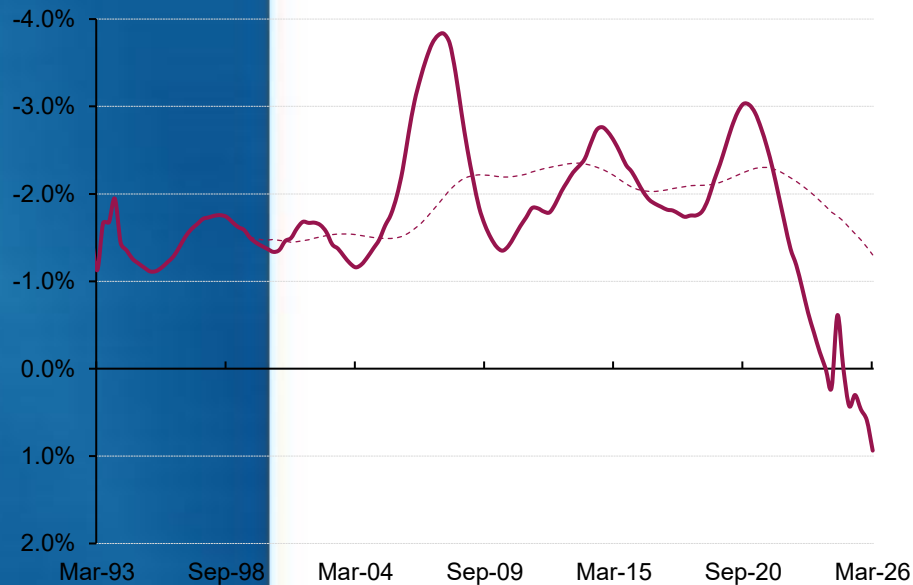


Source: UNCTAD, Axis Bank Research

- ❑ PLI was innovative earlier on, with most countries relying on liberalization rather than specific incentives (WTO rules)
- ❑ However, with these rules now less followed, the share of incentives is now much higher, making PLI-like schemes a hygiene factor
- ❑ Simultaneously, cross-border flows, especially to EMs where policy can be volatile, are held back by uncertainty

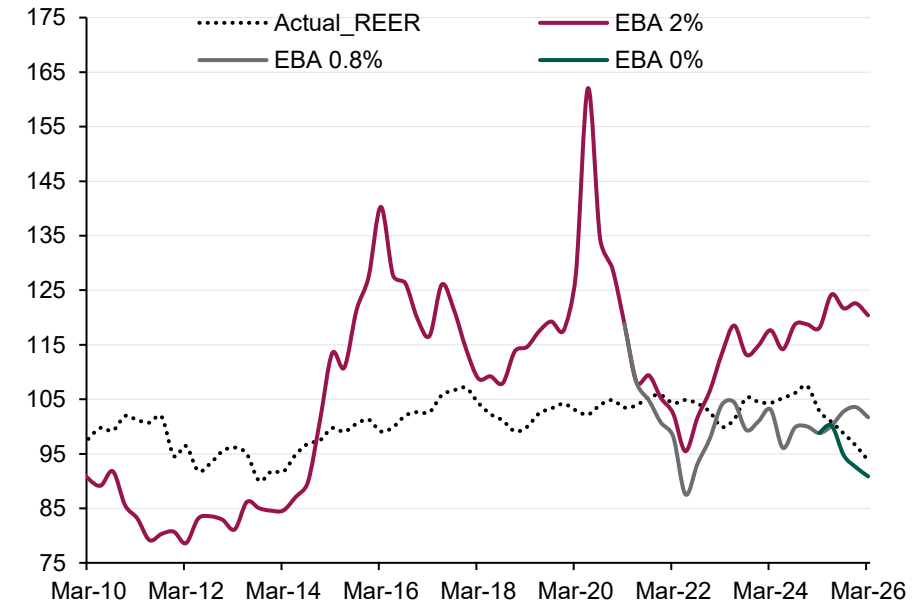
Shifts in global capital have led to a change in sustainable CAD

Sustainable CAD – at 2% for years, is now lower at 0



Source: RBI, Axis Bank Research

A 0% CAD requires a much weaker INR

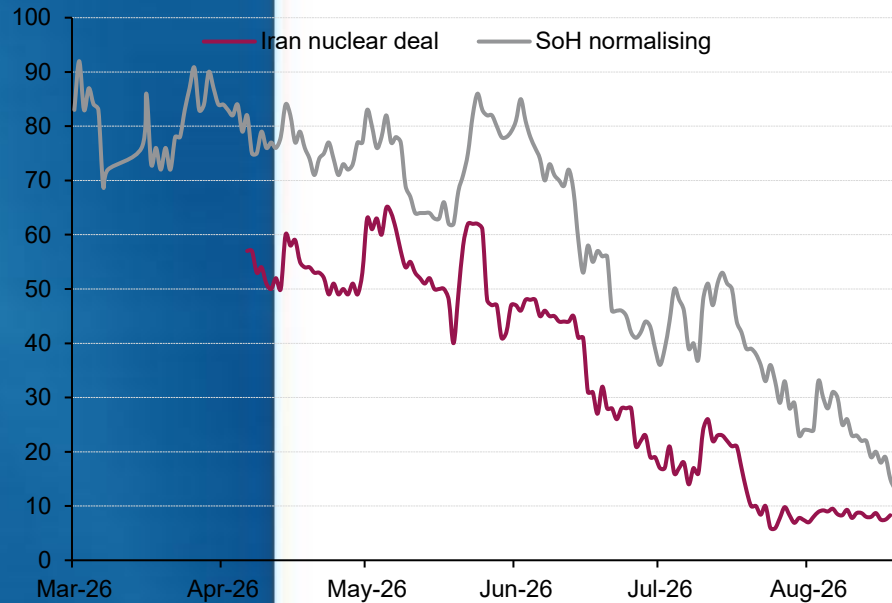


Source: RBI, IMF, MOSPI, Axis Bank Research

- ❑ Capital flow strike has driven sustainable CAD towards 0% of GDP
- ❑ For this to work, the REER has to be markedly weaker – this is the FEER model, suggesting INR at current levels is close to fair
- ❑ But fair value is also driven by long-term productivity – absence of AI can hurt

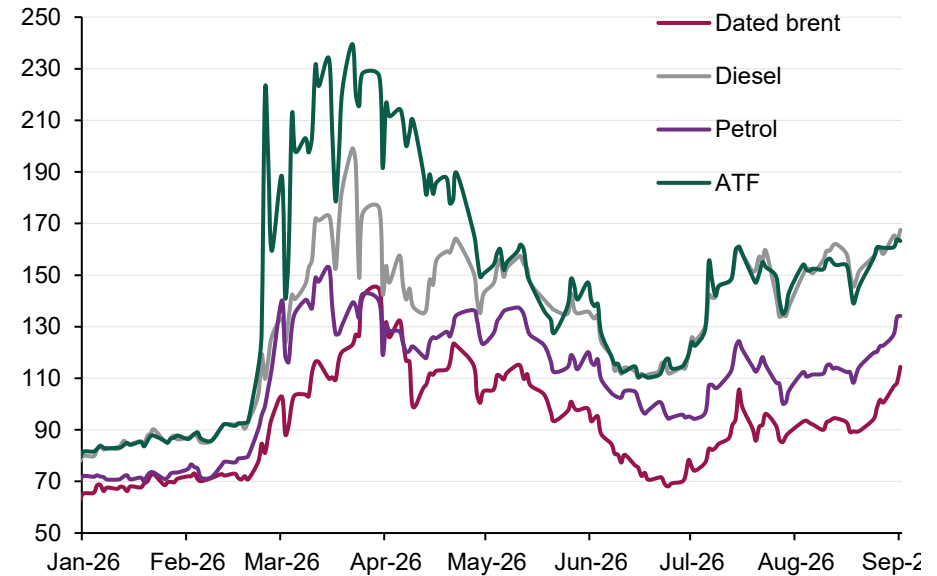
Disruption is also physical

Prediction market probability of events this year



Source: Bloomberg, Axis Bank Research

Petro and product prices, USD/barrel

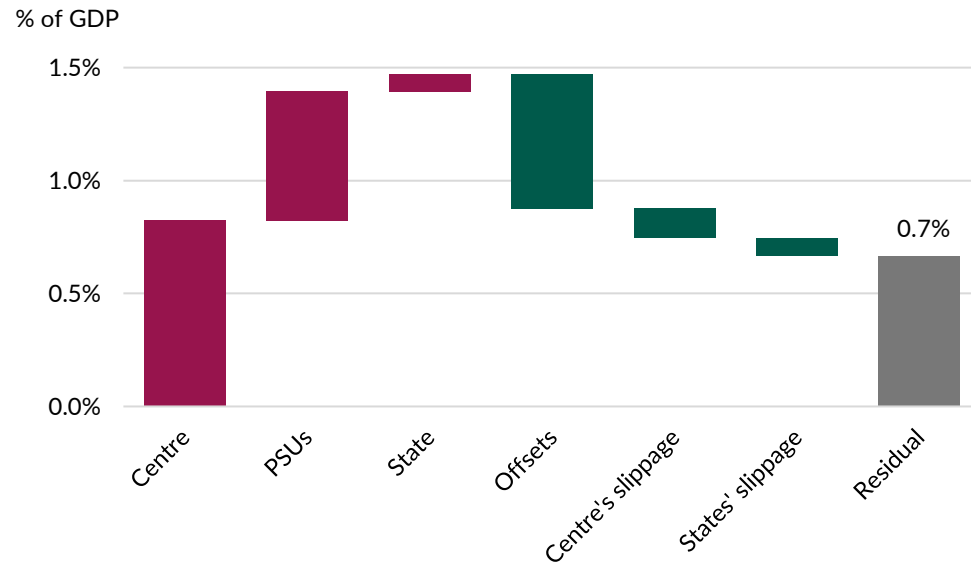


Source: Bloomberg, Axis Bank Research

- ❑ Markets are now bracing for a prolonged conflict – with more to come as predicted by Thucydides' trap
- ❑ Crude oil just the tip of the iceberg, other prices (Cooking gas, shipping, ATF increasingly feeding into inflation)

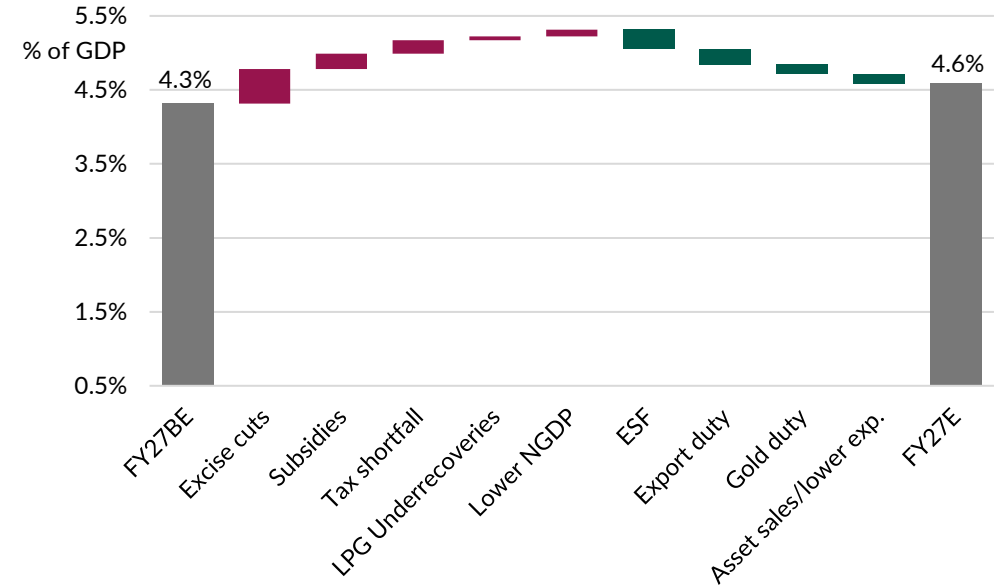
The government is absorbing the impact

Public sector support of around 1.5% of GDP so far



Source: CGA, CAG, company reports, Axis Bank Research

Translating into slippage of 30 bps for the centre

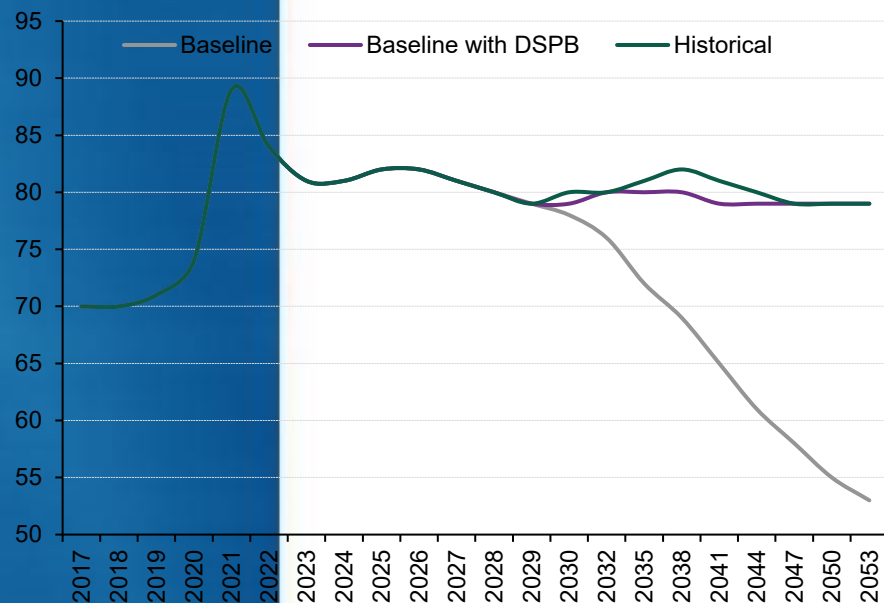


Source: CGA, Budget documents, Axis Bank Research

- ❑ The public sector is providing 1.5% of GDP as support across energy and fertilisers, in addition to GST rate cuts of last year
- ❑ This is not fully translated to fiscal this year, but might pose future headwinds – might also mean another pump price hike

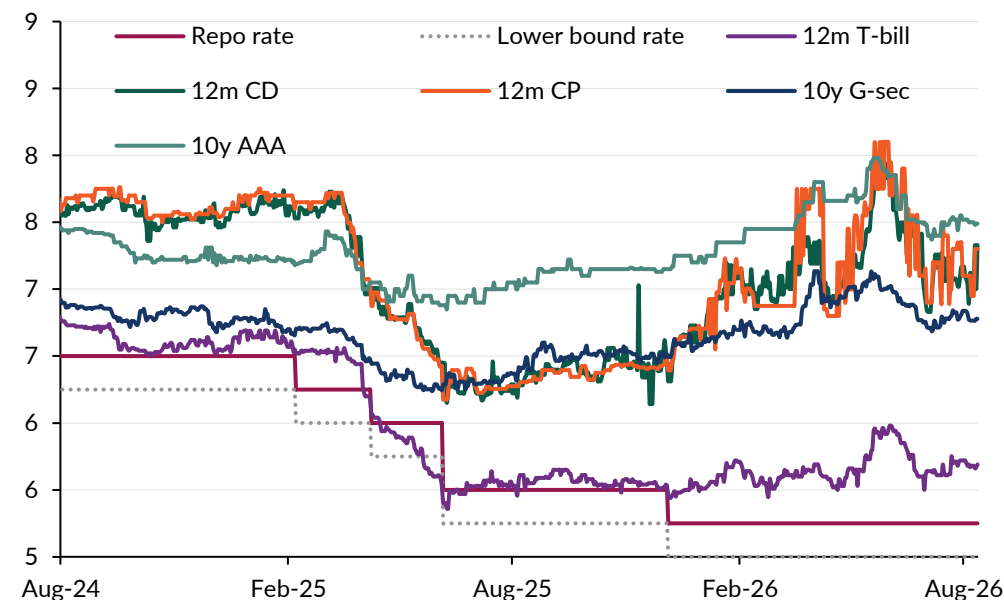
Fiscal* is an open question – especially if monpol ineffective

There is a path to reducing debt over time



Source: IMF, Axis Bank Research

But is monetary policy an effective alternative?



Source: Bloomberg, Axis Bank Research

- ❑ IMF projections show ample scope for gradual debt reduction – but this is in an environment of growth slack
- ❑ Despite monetary easing, de-facto rates are higher. Should fiscal policy act to boost growth and bring value out of rates that are higher anyway?

But efficacy of spending is most important

Capex is highly efficient

Spending Category	Fiscal Multiplier
Capital Expenditure	2.45
Transfer Payments	0.98
Other Revenue Expenditure	0.99
Tax Multiplier	~ -1.0

Spending Type	Long-Term Effect
Roads/Railways/Ports	High
Irrigation	High
Power Infrastructure	High
Education & Health	High
Administrative Spending	Low
Untargeted Subsidies	Low

Source: NIPFP, Axis Bank Research

With longer lasting results, especially at state ends

Category of Capex	Impact on Productivity
Transport Infrastructure	Positive
Power Infrastructure	Positive
Social Infrastructure	Positive
Human Capital Spending	Positive

Years After Fiscal Shock	Revenue Spending Effect	Capital Spending Effect
Year 1	Positive	Strong Positive
Year 2	Near Zero	Positive
Year 3	Near Zero	Positive
Year 4	Near Zero	Positive

Source: NIPFP, Axis Bank Research

- ❑ Any increase in fiscal spending must consider efficiency – capex at state levels has been proven to be most effective
- ❑ Design of schemes is now tailored towards this, with evidence of saturation of central capacity

Thank you



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