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India | Theme Update

Q2 2026

In a Nutshell

Self-help and hidden resilience defy energy-shock bears

Summary

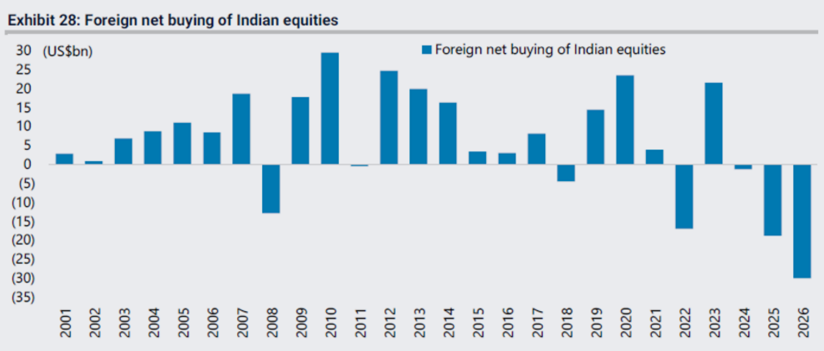
The Xtrackers MSCI India swap ETF gained 10.0% in USD terms during the second quarter (Q2), lagging an AI-led 14.8% rally in the FTSE All World. While a relative laggard, India displayed striking resilience set against the backdrop of the US-Iran war and an AI-takes-all market environment.

The rebound in performance marks a sharp reversal from a bruising first quarter, which had catalysed our investment. Though cyclical headwinds remain, our structural thesis remains intact. India is too big and too digitally enabled to fail. There are signs of optimism. Record foreign selling of Indian equities might have exhausted in June, with $2bn in net inflows, while corporate earnings evidenced a domestic insulation and an underestimated macroeconomic resilience.

As markets have rapidly concentrated into a group of 'AI winners', and their volatility risen to multi-year highs, the downside risks of a reversal are growing. Taiwan and Korea now comprise over 50% of the MSCI Emerging Market (EM) index and three companies account for over 30% of its weight. If the AI trade reverses, 'AI loser' is a moniker the Indian market may finally be happy to take.

Industry Developments

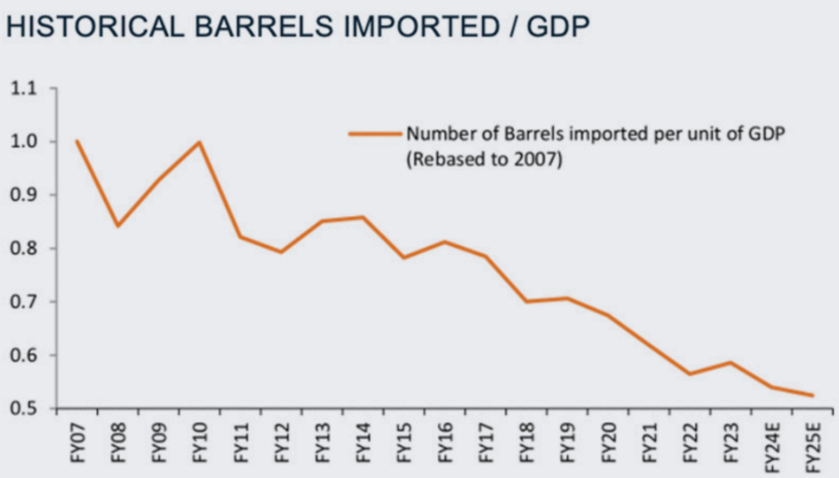
The global oil shock sparked by the closure of the Strait of Hormuz in Q1 led analysts to cut their earnings estimates for India's corporate sector and catalysed record investor outflows.



Source: Jefferies

Foreign investors have sold a record net $30.1bn of Indian stocks in 2026 (to 10 June) to fund flows into AI-dominated markets, such as Taiwan and Korea

However, Indian companies have defended profitability far better than feared in 2026, particularly in the refining and services sectors. Non-commodity sectors are on track to deliver a healthy 12% profit growth in Q2. India's transition to a tech-enabled economy has created a 'perception versus reality' gap, particularly in energy security, where renewables penetration is underappreciated.



Source: Morgan Stanley

A halving of oil imports per unit of GDP since 2007 highlights India's improved energy resilience, insulating corporate margins from external shocks

India's at-home battery network has been crucial for keeping the lights on. With scarcity the mother of invention, Indian households are better equipped than most. Charged during a day-time solar surplus, India's 'hidden' 100GWh battery fleet is estimated to be ten times the size of the UK's.

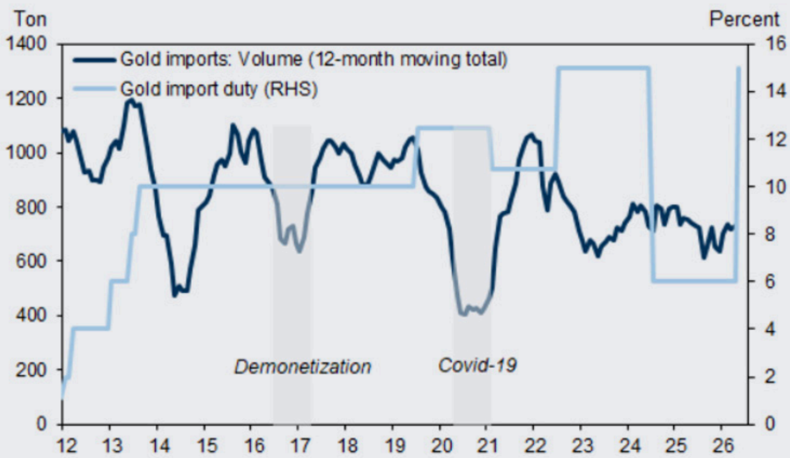
India's Hidden Battery Fleet Can Keep the Lights On

June 9, 2026 at 9:00 PM GMT+1

Source: Bloomberg

India's battery network is keeping the lights on and helping defy India's energy shock 'doomers'

India has also implemented aggressive self-help measures to support its capital markets. Indian import duties for gold and silver were hiked by a record amount in May. As the world's largest consumer of silver and second-largest consumer of gold, this intervention contributed to a recovery in local markets, but presents a material near-term headache for precious metals investors.



Source: Bloomberg

India enacted a record rise in gold and silver import duties in May; historical precedents indicate volumes weaken one month post-hike, with the full impact materialising over six months

An unfolding "Godzilla" El Niño remains a key variable for India. A severe event constitutes a definitive macroeconomic headwind, as associated supply-side inflationary pressures could force the Reserve Bank of India to tighten monetary policy, weighing on growth in the short term.

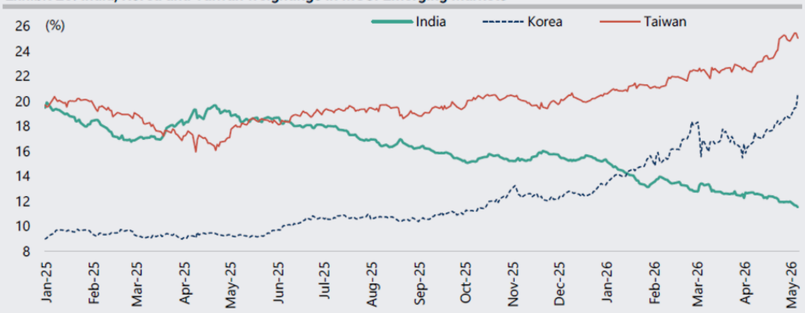
However, taking a long-term view, India's recent deployment of targeted self-help underscores its capacity to proactively shield itself from external shocks. This resilience increases the probability of an idiosyncratic recovery that is funded from domestic, not foreign, capital flows.

Performance

The Xtrackers MSCI India Swap ETF rebounded by +10.0% in USD terms during Q2, trailing a +14.8% rally in the FTSE All World. If India has been out of favour as a reverse AI trade, neighbours Taiwan and Korea have been standout AI winners. Indeed, the EM index has undergone a remarkable metamorphosis, resulting in the duo's weight rising to 50.8% at the end of Q2.

As the World and EM indices become more concentrated in a small number of AI stocks, the downside risks of a reversal and the forward-looking role of safe havens become ever greater.

Exhibit 25: India, Korea and Taiwan weightings in MSCI Emerging Markets



Source: Factset, MSCI, Jefferies

TSMC, Samsung and SK Hynix accounted for 30.7% of the MSCI EM index at the end of Q2, almost three times India's 11% weight in the index

While India's lack of AI plays has been a major hurdle in recent years, it offers safe-haven appeal for global investors. As the volatility of Korea's Kospi and EM has risen toward all-time highs (alongside semiconductor indices), India's volatility is largely unchanged, even amidst the oil shock turmoil.

Investors Looking for Shelter From AI Storm Are Turning to India

By Savio Shetty and Samie Modak

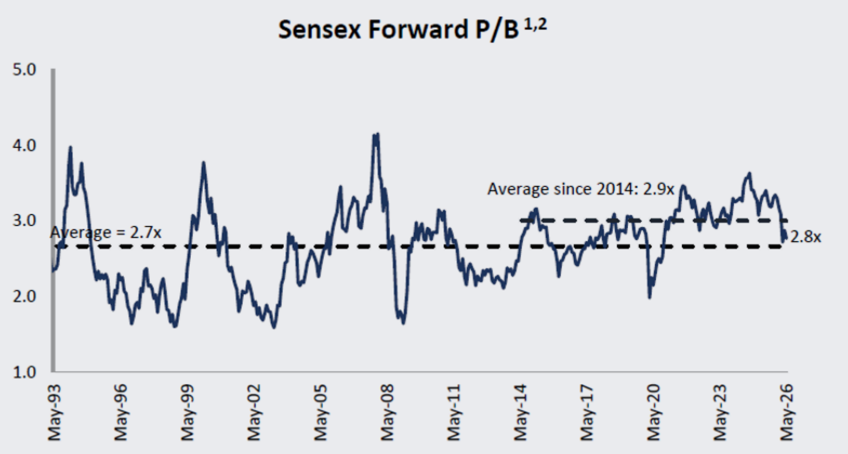
July 5, 2026 at 3:00 AM GMT+1

Source: Bloomberg

Rising volatility in AI and semiconductor names is driving investors back into the shelter of India's domestic-led market

Valuation

Since a peak in 2024, India's underperformance has led to a material compression in valuations.

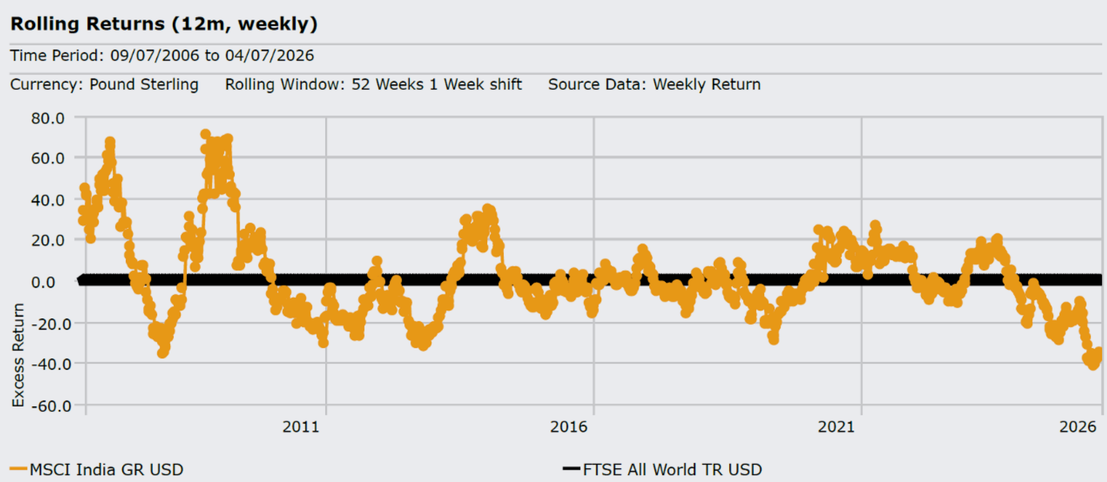


Source: WhiteOak

India's absolute valuations have fallen to their long-term averages. However, relative to surging World and EM peers, India's valuation has fallen to multi-year lows

One measure of India's attractiveness is its rolling performance relative to the FTSE All World index.

As India has trailed the FTSE All World index by a record -35.6% YoY (to 30 June 2026), this measure has collapsed to a historic low in its rolling 12-month performance range. Its future looks brighter than its past.



Source: Morningstar, Bentley Reid

Positioning

We access the India theme via the Xtrackers MSCI India Swap ETF, the cheapest available Indian equity ETF (0.19% annual fee).

The fund invests in 164 companies listed in India. Top holdings in this market-cap-weighted index include HDFC Bank, Reliance Industries and ICICI Bank (at 30 June 2026).

The fund's swap structure avoids India's onerous capital gains tax (CGT), which ranges from 12.5% to 20.0% on physical transactions and drags heavily on physically implemented competitor funds.

Top 10 index constituents

Issuer	ISIN	Weight
HDFC BANK LTD	INE040A01034	6.91%
RELIANCE INDUSTRIES LTD	INE002A01018	6.59%
ICICI BANK LTD	INE090A01021	5.24%
BHARTI AIRTEL LTD	INE397D01024	3.80%
INFOSYS LTD	INE009A01021	3.31%
MAHINDRA AND MAHINDRA LTD	INE101A01026	2.28%
AXIS BANK LTD	INE238A01034	2.22%
LARSEN AND TOUBRO LTD	INE018A01030	1.93%
BAJAJ FINANCE LTD	INE296A01032	1.90%
TATA CONSULTANCY SERVICES LTD	INE467B01029	1.73%

Source: DWS

The fund invests in large- and mid-cap companies listed in India, covering approximately 85% of the free-float Indian market capitalisation

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