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Nifty, Sensex lag Asia on Rupee fall and valuation woes as investors look past GST cheer



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Article Content:

Persistent foreign portfolio outflows, potential impact of US tariffs and stretched valuations are being cited as some of the reasons behind Indian stock markets' underperformance.

Indian equities are underperforming Asian peers, which ended higher after US President Trump formalised a sharply lower automotive import tariff on Japan, with Nifty and Sensex lower by nearly half a percent on September 5 as investors looked past the recent GST reform cheer and hopes of a rate cut by the Federal Reserve.

Sensex dropped nearly 0.42 percent while Nifty 50 fell 0.38 percent to trade below 24,650-mark, even as Japan's Nikkei gained nearly a percent and Hong Kong's Hang Seng ended more than 1.4 percent higher.

Equity analysts have cited several factors to explain the Indian stock markets' weakness despite strong domestic and global cues.

Foreign Outflows

Persistent foreign portfolio outflows, potential hit of US tariffs on India's growth and stretched valuations have capped upside momentum, said Ajit Mishra, SVP of Research at Religare Broking. "While autos have benefited from tax cuts, weakness in IT and banking has offset the gains. Investors are also booking profits quickly, reflecting skepticism on the sustainability of the move amid mixed economic cues. Add to this a weak rupee, relative underperformance versus cheaper peers like China, are also weighing on the sentiment. In short, India's domestic reforms are positive, but global headwinds, valuation concerns, and sectoral pressures are keeping the market's rally more muted than its Asian counterparts," he added.

India's equity markets are reflecting caution. Compared to regional peers, Indian indices are underperforming not because fundamentals are weak, but due to a confluence of macro and sentiment factors, said Bhavik Joshi, Business Head, INVasset PMS.

"Foreign investors remain cautious, evidenced by continued outflows—prompted by concerns over sluggish banking margins, rising consumer credit stress, and dampened export competitiveness

following US tariff threats. These withdrawals have weighed on financials and tech sectors, dribbling into broader market weakness even as domestic flows remain active," he said.

"Foreign portfolio investors have been heavy sellers this year, with financials seeing record outflows. Many global funds are shifting allocations to cheaper markets like Taiwan, South Korea, and China, which offer better valuations and exposure to high-growth sectors such as AI, which are opportunities that many Indian equities are missing," said Ross Maxwell, Global Strategy Lead at VT Markets.

How Much Can GST Cuts Drive Demand?

Bhavik Joshi said that while GST reforms are structurally positive and could bolster consumption over time, short-term skepticism persists about the translation of tax cuts into actual demand - especially in rural and low-income segments where wage growth has been muted.

He added that positioning around a Fed rate cut too has been tempered. "Though markets expect easing, uncertainty around timing and global growth trajectories has capped exuberance, keeping Indian equity momentum more measured than in other Asian economies where investor rotation may be more aggressive," he said.

The GST revamp was expected to streamline compliance and boost market sentiment, but it failed to excite Dalal Street as investors found limited immediate relief for businesses, said Pranay Aggarwal, Director and CEO of Stoxkart. "While structural changes may improve efficiency in the long run, the absence of significant tax rate cuts or sector-specific incentives meant muted short-term impact. Markets typically respond to measures that directly influence earnings visibility or consumption demand. As these were largely unchanged, the Street remained cautious. Overall, the move is seen as an administrative improvement rather than a near-term catalyst," he said.

"Domestically, the initial rally from GST 2.0 reforms was quickly erased by profit booking, and much of the optimism is already priced in. Weak urban consumption and cautious corporate sentiment have further weighed on confidence," said Ross Maxwell, Global Strategy Lead at VT Markets.

Rupee Weakness

Macro pressures, including a falling rupee, US tariff are reflecting as vulnerabilities, said Siddharth Maurya, Founder & Managing Director, Vibhavangal Anukulakara. "Though GST changes offer a critical consumption boost, markets require recovered FPI confidence and enduring earnings recovery before matching regional rallies," he added.

Valuation Discomfort

Shravan Shetty, Managing Director at Primus Partners said valuations are a key reason for the downturn. "The Indian market had outperformed most of its Asian peers in 2024, riding the China plus one narrative and having a higher growth rate. This has led Indian markets to be overvalued as compared to other Asian peers," he said.

"We believe the relative overvaluation, combined with the uncertainty of the tariffs, has a negative impact on sentiment towards Indian markets. In addition, the falling rupee is also impacting the return in dollar terms," he added.

What Should Investors Do?

India is navigating a transitional phase, where its macro engine remains intact, said Bhavik Joshi, however, global risk sentiment and FPI behaviour may be weighing on the near-term direction, he added. As GST-driven consumption gains traction, companies' margins stabilize market returns may improve, Joshi said.