

# THE SCANNER

## What Happened and What's in Store for 2026



## What the year 2025 taught investors

It reminded markets of a few investment truths, such as the fact that expectations have a way of catching up with prices.

Several sectors entered the year riding confident narratives. Growth did not disappear, but it slowed enough for valuations to adjust, often through gradual shifts in multiples rather than earnings. Structural growth remains intact, yet rarely moves in straight lines. When valuations start high, even steady execution can feel underwhelming.

Looking ahead, the task is simple to state: identify growth already priced in versus growth that still leaves room for upside.

## Expensive Sectors

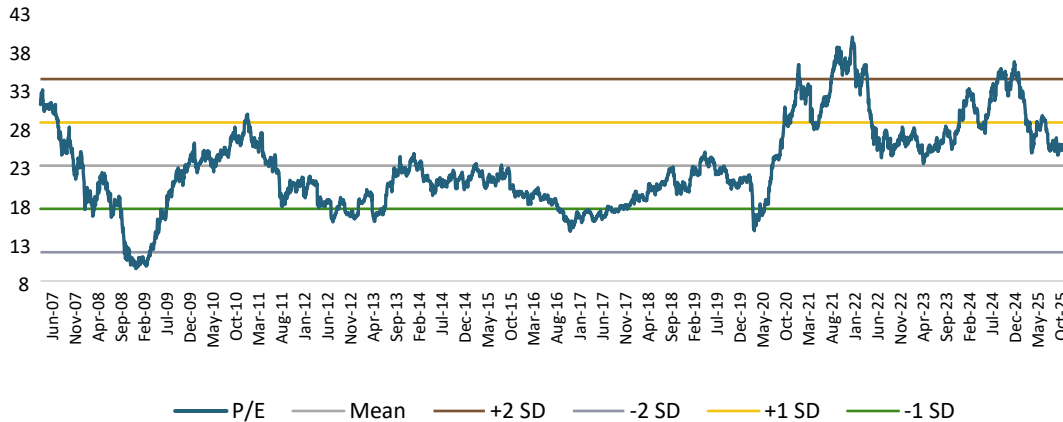


### Information Technology (IT)

Last year, Nifty IT valuations were trading close to the +2 standard deviation band, firmly in expensive territory. As global technology spending slowed, deal decision cycles elongated, discretionary budgets were curtailed, and revenue growth moderated across key verticals, the sector underwent a meaningful de-rating. Valuations corrected toward long-term average levels, offering some relief. However, the recent rebound in stock prices has pushed multiples back toward the +1 SD band, which, from a historical perspective, does not represent a compelling valuation comfort zone.

While early green shoots such as stabilising attrition, improving utilisation, margin bottoming, and the long-term structural opportunity from cloud migration and GenAI adoption are encouraging, near-term risks remain elevated. Deal conversions continue to be slow, discretionary IT spending in the US remains subdued, and pricing pressure could intensify as automation and AI-driven efficiencies increase commoditisation risk. A sustainable re-rating from current levels would likely require clear evidence of sustained revenue acceleration and durable margin expansion, rather than valuation-led optimism alone.

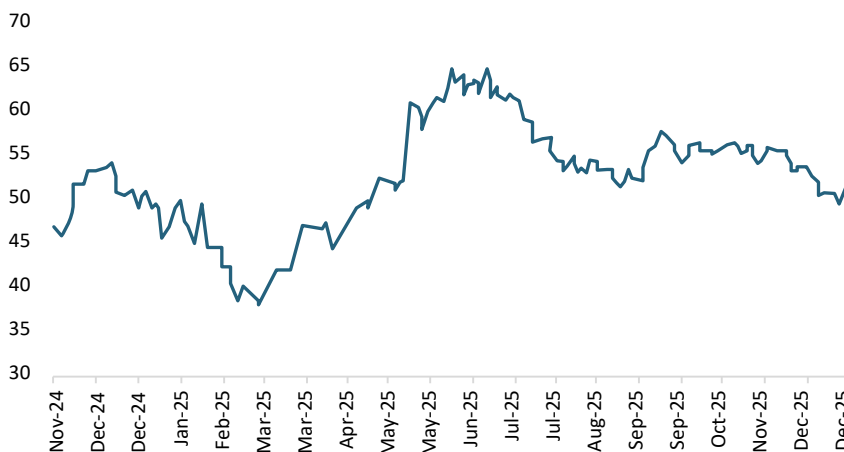
**Exhibit: Nifty IT PE**




**Defence**

The Nifty Defence Index, which comprises 10 defence-focused companies, is currently trading at over 50x P/E, a level that leaves little room for error. In simple terms, investors are paying Rs.50 today for every Rs.1 of current earnings, implying strong confidence in sustained, multi-year growth in revenues, margins and execution.

**Exhibit: Nifty India Defence PE**



Such valuations reflect expectations of robust order inflows, flawless execution, operating leverage and long-term policy support. However, the risk-reward becomes asymmetric at these levels. With expectations already priced in, even a temporary slowdown in earnings growth, margin pressure, execution delays, or policy-related hiccups can trigger a sharp valuation de-rating. Importantly, this downside risk exists even if the underlying businesses continue to grow, but at a pace lower than what the market is discounting today.

At current valuations, the sector offers limited margin of safety, making future returns highly sensitive to earnings delivery rather than incremental positives. Sustainable upside from here would require earnings growth to consistently outperform already-elevated expectations, which raises the bar meaningfully for investors.

# Which sectors look attractive?



## Private Sector Banks

Private sector banks are trading at relatively attractive valuations compared to their own history. The Nifty Private Bank index is currently hovering around the -1 standard deviation band of its long-term Price-to-Book (P/B), implying valuations are meaningfully below the historical average. This suggests that a large part of the concerns around Net Interest Margin (NIM) compression, elevated deposit competition, and moderation in loan growth have already been discounted by the market.

**Exhibit:** Nifty Private Banks PE



Importantly, the valuation comfort comes at a time when fundamental indicators remain largely intact. Asset quality across private banks continues to be strong, with Gross Non-Performing Asset (GNPA) and Net Non-Performing Asset (NNPA) ratios near multi-year lows and credit costs well under control. While margins are expected to normalise as deposit costs reprice faster than loan yields, balance sheets remain robust, capital adequacy is comfortable, and loan growth though moderating is still running above nominal GDP growth.

From a medium-term perspective, the current setup offers a favorable risk-reward. Any stabilisation in deposit costs, improvement in CASA ratios, or visibility on NIM floor could trigger mean reversion in valuations. Additionally, a revival in credit demand from retail, SME, or capex-linked segments could act as a catalyst for earnings upgrades. Key risks to monitor remain sharper-than-expected NIM compression, aggressive deposit pricing, and a slowdown in credit growth, but at current valuation levels, downside appears relatively better protected.

# Is the PSU Banking segment also attractive?

**Exhibit:** Nifty PSU Banks PE





PSU banks are now trading at elevated valuations relative to their own history. The Nifty PSU Bank index is currently positioned close to the +1 standard deviation band of its long-term P/B multiple, indicating that valuations are no longer cheap and are approaching levels that have historically limited upside. This marks a sharp shift from the earlier phase of re-rating, which was driven by balance sheet clean-up, sharp improvement in asset quality, and strong earnings recovery from a low base.

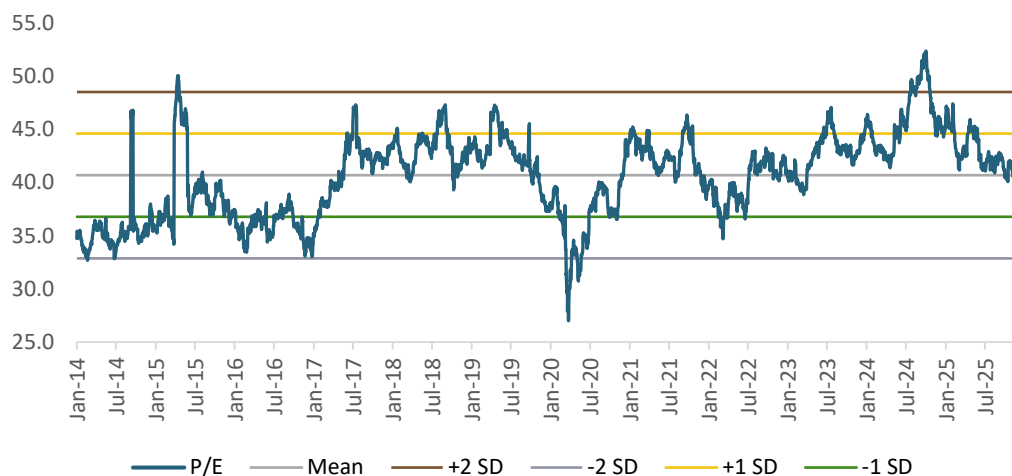
From a relative perspective, PSU banks now look less compelling compared to private sector banks, which are trading below historical averages and offer better risk-adjusted upside. Going forward, PSU bank performance is likely to be driven more by earnings delivery rather than valuation re-rating, with higher sensitivity to macro factors such as interest rates, government borrowing, and economic slowdown risks.

## What about the FMCG sector?

FMCG valuations have historically commanded a premium, supported by the sector’s defensive characteristics, strong brand franchises, and predictable cash flows. Currently, valuations are trading broadly around long-term mean levels, indicating that much of the sector’s inherent quality is already reflected in prices. Volume recovery has been gradual, rural demand remains uneven, and urban demand has been muted, constraining near-term growth visibility.

At these levels, upside from further multiple expansion appears limited, and performance is likely to be driven primarily by earnings delivery. However, any meaningful correction that pushes valuations below historical averages could create attractive entry opportunities, particularly in high-quality FMCG names with strong balance sheets and long-term pricing power.

**Exhibit:** Nifty FMCG PE



At Multi-Act, we continue the task of scanning markets through this lens - for investors and with investors.



## Sarvajeet Bodas, CFA

Advisor, Client Servicing  
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### What explains the sharp correction seen in railway-focused stocks despite healthy order books?

Railway-linked stocks rallied sharply on the belief that government capex would keep rising at a steep pace, translating into sustained, outsized order inflows. This optimism pushed valuations to expensive levels. As Budget expectations normalised and markets reassessed the trajectory of future railway capex, sentiment shifted. Investors began factoring in sector realities such as lumpy revenue recognition, regulated or competitive margins, and long working capital cycles. While fundamentals remained intact, growth expectations moderated, leading to valuation de-rating rather than any meaningful deterioration in business performance.

### What lessons do railway stocks offer on valuations and market expectations?

The railway episode highlights how quickly high valuations can unwind when expectations are extrapolated too far into the future. Even strong businesses can see sharp price corrections if growth

assumptions soften. In capital goods and policy-driven sectors, stocks often price in multiple years of aggressive growth upfront. When that growth is merely delayed or normalised, the adjustment happens through lower multiples, not collapsing earnings. This underscores the importance of margin of safety and the risks of paying peak-cycle valuations for businesses with cyclical or policy-linked drivers.

### Why did EMS stocks correct sharply after trading at very high multiples?

The Electronics Manufacturing Services (EMS) sector saw several stocks trading above 100x P/E, reflecting extremely optimistic assumptions around scale, margins, and sustained growth. At such valuations, even minor disappointments like slower execution, margin pressure, or lack of incremental buyers, can trigger sharp corrections. This phase also coincided with promoter stake sales, indicating monetisation at perceived peak valuations. Additionally, a portion of the growth narrative is policy-led via Production Linked Incentive (PLI) incentives. If markets begin to view these benefits as tapering or non-recurring, valuation frameworks reset quickly, even if operations remain stable.

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