



Does a 5.3% Treasury matter for Indian stocks?

What US yields do, and do not do.

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US yields: do they drive Indian stocks?

The US 10-year is at 5.3%, the highest since 2007, and the Indian earnings yield is below it. This section asks how a US yield could reach an Indian stock.



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The worry

US government bonds now pay more than large Indian companies earn on their share price

Indian earnings yield vs US 10-year yield, 2011–2026



Earnings yield = $1 \div \text{price-to-earnings multiple (trailing 12-month consolidated earnings)}$ of the top 100 companies by market value: size-weighted (20.3x, 4.9%) and median company (30.3x, 3.3%); Vyapti weekly data, drawn through its turning points, to 1 October 2026. US: 10-year Treasury constant-maturity yield, monthly average (FRED); last point is the close of 1 October (5.30%). Gap = size-weighted earnings yield minus US 10-year yield.

5.3%

what a US government bond pays today. The highest since 2007.

3.3%

what the typical (median) large Indian company earns on its share price. Weighted by size, large caps earn 4.9%.

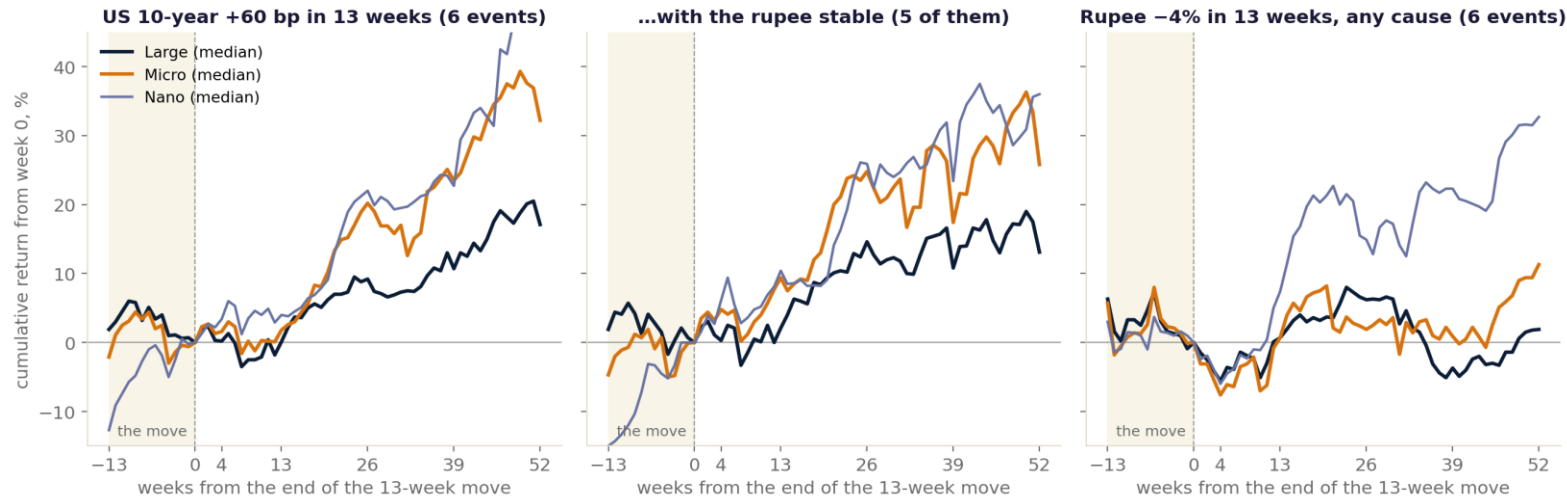
-0.4 pts

Indian earnings yield (size-weighted) minus the US yield. Normal since 2011: +2.4. Below zero only since 2023.

The fear: with safe US bonds paying more, foreign money leaves India and Indian shares fall.

1 Historically, the damage comes from falling Rupee

What stock prices did from the week a US rate shock



-8%

in the first month after a rupee fall.

+25%

six months after a US rate jump with the rupee steady

After...	1 month	3 months	6 months	1 year
US rates jump, rupee steady	+5%	+9%	+25%	+26%
US rates jump, rupee falls too	-8%	-3%	+11%	+50%
Rupee falls 4%, any reason	-8%	+1%	+2%	+11%

Lines are the median cumulative return across events, from the first week each condition appeared (events at least 26 weeks apart; week 0 = end of the 13-week move). US-yield events: Jul 2013, Nov 2016, Feb 2021, Mar 2022, Aug 2023, Nov 2024; five of them with the rupee within 2%, two with it down 3% or more; six separate rupee falls of 4%.

- The hit lands in the first four weeks and is rupee-led, not rate-led.
- After that every path is positive, but a rupee fall leaves returns below normal for a year: +2% at six months and +11% at one year, against about +10% and +20% in an average period.

Watching Rupee is critical! If the rupee is steady, do nothing. If it breaks, the first month is the risk; after it, returns have been positive.

1 Every "US rates" scare rose from its low. Four recovered in full in 6 months

The six sharp falls since 2013 that were blamed on US rates. What fell, and what happened next, measured from the low

The scare	Rupee	Large (top 100) fell	Small (501–1,000) fell	Small, next 6 months
Taper tantrum (24 May–30 Aug 2013)	-17.8%	-18%	-18%	+27%
Fed, oil, IL&FS (31 Aug–26 Oct 2018)	-3.5%	-19%	-20%	+4%
Inflation hikes (14 Jan–17 Jun 2022)	-5.3%	-19%	-21%	+23%
5% scare (15 Sep–27 Oct 2023)	-0.1%	-5%	-1%	+24%
Dollar surge (27 Sep 2024–28 Feb 2025)	-4.6%	-25%	-26%	+18%
Oil, West Asia (27 Feb–27 Mar 2026)	-4.2%	-10%	-10%	+27%

- Five of the six came with a falling rupee and heavy foreign selling. The one without a rupee move (October 2023) was barely a dent.
- The next six months were positive every time, by 4% to 27%, but that is measured from the low, which is known only afterwards. The pre-fall level was regained within six months in four of the six.
- Neither the size of the rate move nor the size of the rupee move ranked the damage: 2018 was a 0.2-point rise with a 3.5% rupee fall, 2013 a 17.8% rupee fall, and both cost about 20%. What the falls share is foreign selling with the rupee weakening.

Rupee = change in rupees per dollar over the window. Large = top 100 companies by market value; Small = ranks 501–1,000 (equal-weight). "Next 6 months" = return over the 26 weeks from the last date of the window, which is the low. Time to regain the pre-fall level and "record valuations" are measured on the equal-weight panel of 1,565 stocks.

Six scares, six rises from the low. Four full recoveries inside six months.

1 Every such scare gives a buying opportunity

Weeks since 2014 sorted by foreign flow over the previous 26 weeks (basis points of market value), and what the average stock did before and after. 615 weeks

Foreign flow, previous 26 weeks	Weeks	Market, previous 26 weeks	Foreign flow, next 26 weeks	Market, next 26 weeks (share up)
Heavy selling (–40 bp or worse)	59	–7%	–8 bp	+15% (93%)
Moderate selling (–40 to –5 bp)	241	+6%	–18 bp	–1% (48%)
Flat (–5 to +20 bp)	138	+11%	–9 bp	+14% (71%)
Buying (above +20 bp)	177	+26%	–1 bp	+17% (89%)
All weeks	615	+11%	–8 bp	+10% (69%)

- By the time foreigners have sold 40 bp of the market in six months, the price is already paid: the average stock is down 7% over those months (normal: +11%) and the median P/E is down 13%.
- That pace does not last. In 93% of these weeks the next six months' selling was lighter (median –64 bp to –8 bp), while domestic funds kept buying. Foreigners did not need to return: where they went on selling more than 20 bp, the market still rose 4%, and was up 80% of the time.
- It fails when prices have not fallen first: within 5% of the high (January 2022) the next six months returned 0%. Moderate selling is the poor state, because it tends to get worse before it ends. Five episodes (2016, 2020, 2022, 2025, 2026): read the ordering, not the decimals.

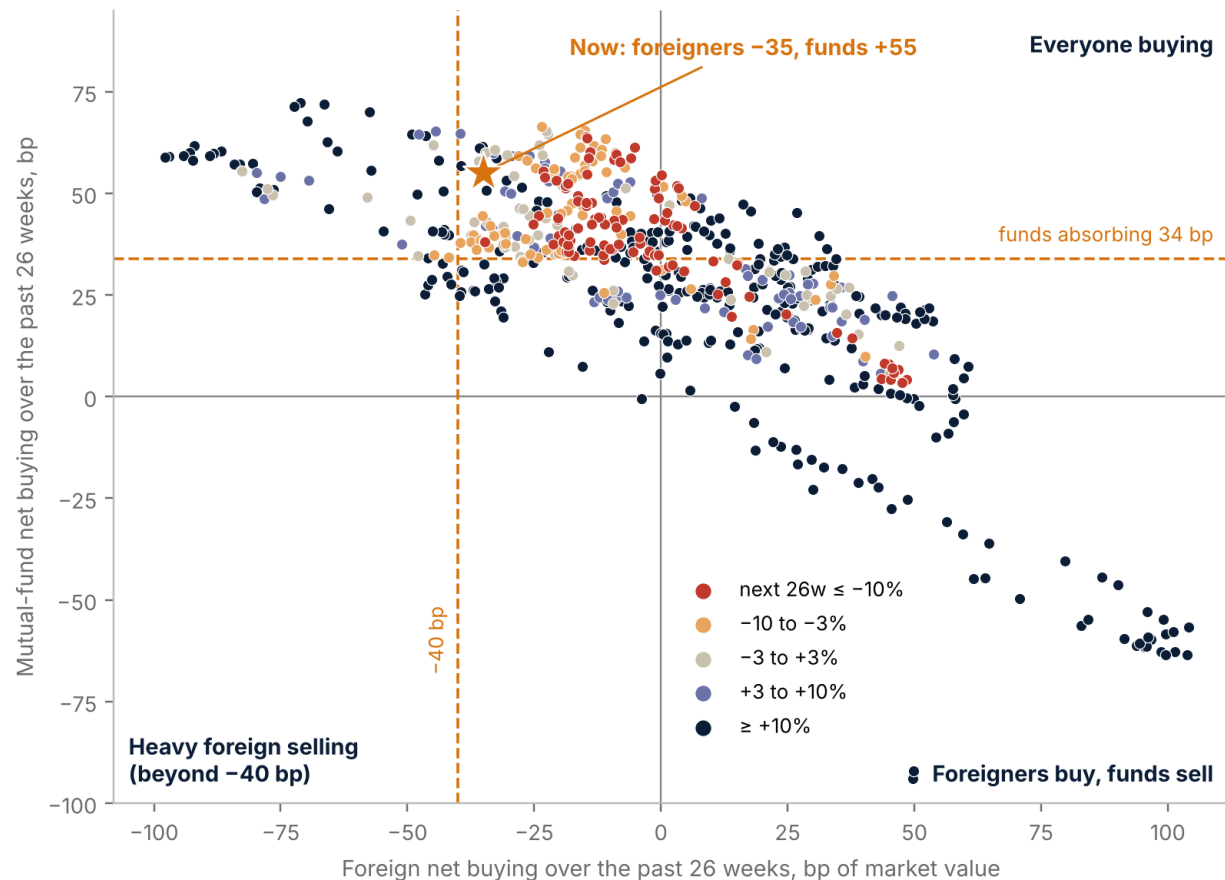
Foreign flow = net purchases on the exchange by foreign portfolio investors (NSDL, daily), summed over 26 weeks and divided by total market value; 1 bp = 0.01%. Market = equal-weight index of 1,565 stocks. Figures are medians across weeks; "share up" = share of weeks followed by a positive 26 weeks. 615 weekly readings, January 2014 to March 2026 (later weeks have no outcome yet). The latest reading uses NSDL's report of 30 September 2026.

The signal is the size of the selling with prices already down. It last fired in March 2026 (market +27% since). At –35 bp on the latest data (30 September), we are in the moderate selling zone.

1

How to think through on timing and flows

Each week since 2014 placed by what foreigners and mutual funds had done over the previous 26 weeks; colour is what the average stock did next



- Foreigners buying while funds sell (bottom right, 53 weeks): the average stock rose every time, by a median 38%.
- Moderate foreign selling with funds absorbing more than 34 bp (217 weeks): median -4%, up only 39% of the time. Most of the reds sit here, chiefly 2018 and 2019, then late 2024 and 2025.
- Heavy foreign selling, beyond -40 bp (59 weeks): median +15%, up 93% of the time. Prices were already down and the pace of selling faded (previous page).
- Now (star): foreigners -35 bp to 30 September, funds about +55 bp to 21 September. Just inside the weak zone, a few basis points from the strong one.

Foreign flow: NSDL. Mutual-fund flow: SEBI. Both are net purchases on the exchange over 26 weeks + total market value (1 bp = 0.01%). Colour: return of the equal-weight index of 1,565 stocks over the following 26 weeks. 615 weeks, 2014 to March 2026. Dashed lines: -40 bp of foreign flow; +34 bp of fund flow, about the median week. The weak zone is mostly one stretch, 2018-19, so it is far fewer independent episodes than 217 weeks.

Markets carried by domestic funds against moderate foreign selling have been the weak ones. That is where we are, by a few basis points.

2

What is inside the US yield, and why it matters for India

A Treasury yield is a real yield plus expected inflation. The two halves send the dollar, the rupee and foreign money in opposite directions. This section shows which half is moving today, what is holding it up, and what each path has meant for Indian stocks.



2 US growth looks strong, and it rests on one engine

The Fed expects 2.3% growth

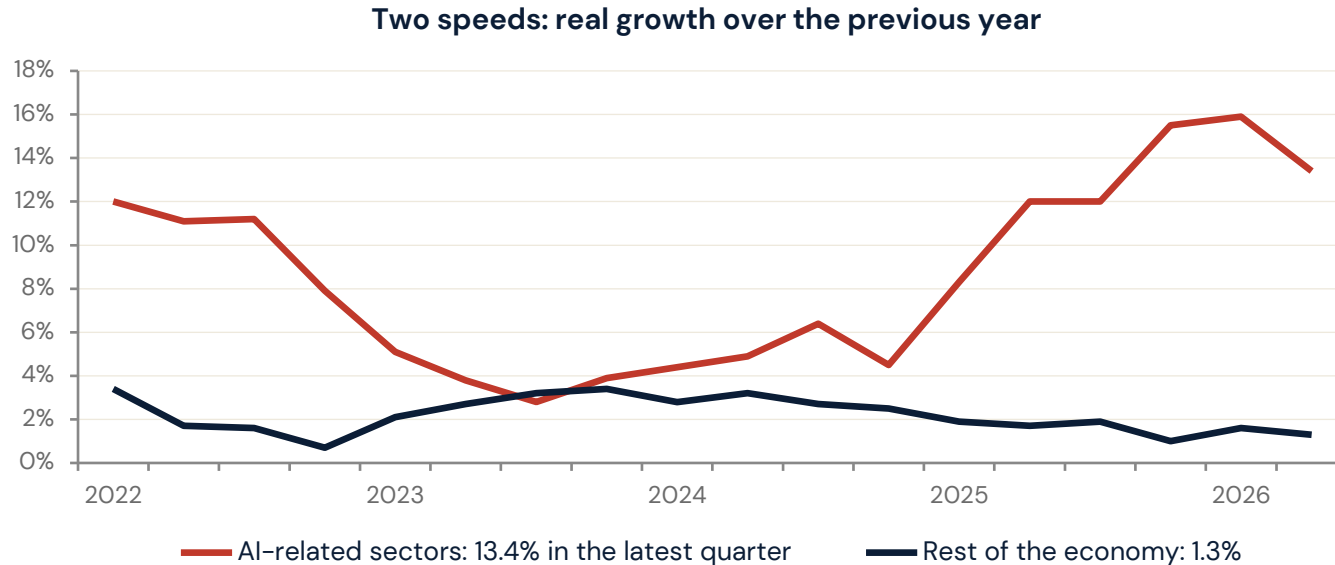


Chart: year-on-year real growth, quarterly, Q1 2022 to Q2 2026 (the latest published). AI-related sectors = private investment in information-processing equipment, software and research and development, 8% of GDP; the rest = real GDP less that. BEA data via FRED, our calculation; it is gross investment, so imported equipment is not netted off. EPB Research, who first drew this comparison, get 13.8% and 0.8% on their own measure. Jobs: BLS via FRED, to September 2026; full-time employment is from the household survey and is volatile. Bond spreads: ICE BofA, July 2026, read from a published chart.

47%

of the past year's US growth came from AI-related sectors, which are 8% of the economy. They grew 13.4%; everything else grew 1.3%

41,000 a month

jobs added over the past year; 29,000 in September. Full-time employment is 0.8 million below December

If the AI build-out slows

Growth forecasts fall
and the Fed stops raising rates

The US real yield falls

India: better
Led by foreigners buying

Today's US real yield is priced for strong growth. That growth is one investment boom wide.

2 Two inflations: US expectations help us, a rising Indian CPI hurts

Indian CPI is what the RBI reacts to. Both tables show what moved together or followed

US inflation expectations, 13w move	Weeks	Large	Small	Micro	Nano	Micro +26w	Nano +26w
Up 30 bp or more	67	+8%	+12%	+11%	+14%	+24%	+25%
Down 30 bp or more	66	-4%	-2%	-3%	-1%	+3%	+12%

India CPI, as known then; next 26w	Weeks	Large	Small	Micro	Nano	Micro up %
CPI falling (6m change < -1 pt)	232	+6%	+12%	+13%	+16%	72
CPI below 4%	186	+1%	+2%	+4%	+8%	56
CPI 4–6%	294	+4%	+6%	+7%	+21%	63
CPI above 6%	321	+3%	+5%	+5%	+9%	59
CPI rising (6m change > +1 pt)	177	-3%	-4%	-6%	-3%	36

US expectations +30 bp	Brent	FPI 13w	Large	Micro	Nano	Micro +26w
2011-12	0%	n/a	-11%	-23%	-18%	+14%
2012-09	+19%	n/a	+4%	+5%	+3%	-5%
2013-09	+9%	n/a	-1%	-8%	-4%	+25%
2016-04	+32%	+22	+5%	+1%	-5%	+22%
2016-11	-8%	0	-4%	+5%	+17%	+22%
2020-06	+18%	-13	+4%	+2%	+11%	+40%
2021-11	+16%	-8	+12%	+7%	+13%	-14%
2022-03	+45%	-53	-8%	-6%	+15%	+9%

- US inflation expectations: they rise when markets price stronger global growth, and Indian small caps rise in the same quarters (Micro +11%).
- Indian CPI: the level does not matter (Micro +4% to +7% over six months whether CPI is below 4% or above 6%). The direction does: after CPI had risen a point or more in six months the next 26 weeks were negative in every tier (Micro -6%); after it had fallen a point they were the best state in the study (Micro +13%, Nano +16%). The rising-CPI result rests on a handful of episodes, chiefly 2017–19: a caution, not a rule.
- Today: US breakevens are flat (2.36%), so there is no reflation signal. Indian CPI has gone from 0.2% last October to 4.8% in August; the six-month rise peaked at 3.3 points in April (2012 and 2019 saw larger) and is 1.6 now. The last rebound of this kind, from 1.1% in June 2017 to 5.1% in January 2018, was followed by RBI rate rises in 2018.

US inflation expectations = 10-year breakeven (Treasury yield minus inflation-protected Treasury yield, FRED), change over 13 weeks. Left tables: median tier return in the same 13 weeks (top) and over the following 26 weeks (bottom, by Indian consumer-price inflation, year on year, as known at the time with a six-week lag; "6m change" in percentage points). Right table: the eight separate episodes, with the change in Brent, foreign flow (bp of market value, available from 2014) and tier returns in the same 13 weeks. Weekly readings overlap: 67 weeks are 8 episodes.

2 Fed's Hobson's choice | US Inflation is the only real option

US 10-year +40 bp in 13 weeks...	Weeks	Events	FPI, bp	Large	Micro	Nano	Micro +26w	Nano +26w
...dollar down	26	9	+1	-2%	+4%	+10%	+9%	+24%
...dollar up	100	11	-12	-1%	-0%	+8%	+14%	+19%
...led by US inflation expectations	29	6	-6	-1%	+2%	+13%	+22%	+17%
...led by the US real yield	97	13	-2	-2%	+1%	+7%	+12%	+19%
...dollar down, FPIs buying	14	4	+8	+2%	+10%	+14%	+24%	+42%

- The dollar and the 10-year are unrelated quarter to quarter (correlation 0.04). What matters is the mix: a rise in the US real yield lifts the dollar (+0.28), a rise in US inflation expectations lowers it (-0.37). One rise in five has come with a falling dollar, and those were the reflation quarters: March 2012, February 2018, February 2021, July 2023.
- Dollar down: foreigners kept buying (+1 bp), Micro +4%, Nano +10% in the quarter. Dollar up: foreigners sold 12 bp, Micro flat. **The dollar, not the yield, carries the foreigner's decision**
- Would higher US inflation change how foreigners treat India? Yes, in India's favour on the evidence: with the dollar falling and foreigners buying (4 episodes) Micro was +10% in the quarter and +24% over the next six months.
- **Rising US inflation with a soft dollar is the one yield scenario in which the India small tiers have done best.**

Rows are weekly readings in which the US 10-year yield had risen 40 bp or more over 13 weeks. Dollar = the Fed's broad dollar index over the same 13 weeks. FPI = median net foreign purchases over those 13 weeks, bp of market value. Large, Micro, Nano = median return in the same 13 weeks; "+26w" = over the following 26 weeks. Events = separate episodes.

The Fed's Hobson's choice

The Fed holds its short-term interest rate at 3.88%. The US government's 10-year borrowing cost is much higher, at 5.29%, and has risen 1.3 percentage points this year. So, lenders want more return for lending long-term to a government that borrows heavily, issues a lot of new debt, and faces oil at \$110+.

The Fed has two options.

Option 1: Keep rates high, or raise them. This slows an economy already strained by expensive home loans, and it raises the government's own interest bill. Growth weakens, and the debt becomes heavier relative to the size of the economy. The pressure to let inflation shrink that debt grows.

Option 2: Cut rates to support growth. Lenders then expect more inflation and demand even higher long-term rates, while the dollar weakens. This leads to inflation directly.

Either way, the road ends in higher US inflation, because **inflation is the easiest way to shrink a large debt. A period of rising inflation and a weaker dollar is the one scenario in which smaller Indian companies have done best.**

2 India Market returns in different scenarios

Six-month windows since 2014, sorted by what moved the US 10-year yield. Medians.
Green = better for India than a typical six months, red = worse

	Real yield rising (today)	Inflation expectations rising	Inflation expectations falling	Real yield falling	All months
US dollar	+1.6%	+1.1%	+5.1%	-0.6%	+0.9%
Rupee	-3.4%	-0.5%	-4.2%	+0.9%	-1.7%
Foreign flow into Indian shares	-21 bp	-1 bp	-21 bp	+31 bp	-8 bp
Indian stocks, same six months	+8%	+15%	-2%	+1%	+11%
Indian stocks, next six months	+10%	+20%	+3%	+12%	+10%

- What hurts India is the US real yield rising relative to inflation expectations: either the real yield goes up or inflation expectations come down. Both bring a firmer dollar, and the rupee and foreign money follow it.
- Today we are in 1st column.
- We can move quickly move to 2nd column i.e. from Real Yield rising to inflation expectation increasing with mounting US Fiscal debt situation. This in turn **will trigger a deflation trade, which is positive for Indian stocks.**

Real yield rising: US 10-year up 50 bp or more in six months, more than half of it from the real yield. Inflation expectations rising: the same, more than half from inflation expectations. Inflation expectations falling: down 30 bp or more while the 10-year is not rising. Real yield falling: down 40 bp or more with inflation expectations steady. The four columns hold 22, 12, 19 and 14 months; each month sits in one column at most and 80 of the 147 are in none. "Faster than usual" = the rupee lost more than 1.8%, its average six-month fall. Indian stocks = equal-weight index of 1,565 stocks (page 3). Flow in bp of market value (NSDL). Today = August–September 2026.