India's Case for a Dedicated Global Investment Mandate

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Abstract

Arvind Chari has spent close to five years pushing one central idea: global institutional investors need to stop viewing India through the lens of "emerging markets" or "Asia" allocations, and instead treat it as a dedicated mandate. Most global capital pools, whether pension funds, sovereign wealth funds, or endowments, allocate money in broad regional or thematic buckets. India's flows rise and fall based on decisions made about emerging markets as a whole, even though India's growth story, in Arvind's view, is structurally different from peers like Brazil or Russia where GDP growth does not reliably translate into shareholder returns.

Arvind lays out the numbers behind India's current under-allocation. Global assets under management sit around 300 trillion dollars, of which India's public markets account for less than a trillion dollars and private markets perhaps another trillion, a combined weight far below India's roughly 3.5 percent share of global GDP. He connects this gap to India's own growth arithmetic: sustaining 8 percent real GDP growth requires an investment-to-GDP ratio of 38-40 percent, well above the current 30-34 percent, and domestic savings alone cannot close that gap. Foreign capital, he argues, has to fill the difference, and policy has not yet been framed around that need.

The conversation moves from the scale of the opportunity to the practical reforms that could unlock it, including tax treatment of foreign investors, ease of market access, and the distinction between "financial FDI" and genuine multinational manufacturing investment, drawing a comparison to Vietnam's experience with China-plus-one manufacturing flows.

Supplementary Resources

- **India Deserves a Dedicated Investment Mandate** by Quantum Advisors India (Resource) [1]
- **The Great India Under-Allocation** by Quantum Advisors India (Resource) [2]

Contents

Introduction **3**

India as a dedicated global mandate **3**

Linking GDP growth to market returns **4**

Sizing India's global capital allocation **5**

Policy reforms to attract foreign capital **8**

Lessons from other emerging markets **10**

Introduction

[00:00:09] Arvind Chari: Thank you, Sanjita. Thank you for having me.

[00:00:24] Arvind Chari: Can you tell us about the big idea you'd like to talk about here?

India as a dedicated global mandate

[00:00:27] Arvind Chari: So the big idea that I have spoken about for the last, at least for the last four, five years, is how I want global institutional investors to think of India as what I call a dedicated mandate. The way global investors invest is most of them are based in a region. So they are a US pension fund or a Middle East sovereign wealth fund or a university endowment foundation in the US or Europe.

[00:02:07] Arvind Chari: And they all have assets. They all have large pools of capital, which they deploy. So typically they deploy a large amount of their assets in their home country, because there's always regulations or there's always what we call home country bias. But there are large investors who also deploy that capital and spread that capital around the world.

[00:02:19] Arvind Chari: When they do that, they will always think mostly in what we call regions or buckets. So some of them will have a home country. So a US pension fund will have a US allocation, and then they'll have something called a global or international allocation. Or some of them will say developed market versus emerging market.

[00:02:19] Arvind Chari: So they will do developed market equities, developed market bonds, and then emerging market equities, emerging market bonds.

[00:02:45] Arvind Chari: So India then gets bracketed in that allocation. So the flows to India then depend on: do they invest in global, or do they invest in emerging, or do they have an Asia allocation, or in the decade of two thousand, the silliness of BRIC — Brazil, Russia, India, China. A lot of them had BRIC funds and BRIC allocations. So then India is subject to those aspects.

[00:03:11] Arvind Chari: And over time, the allocation to emerging markets might go up, and then India will get higher flows. The allocation to emerging markets goes down, and then India will get lesser flows. So that's where we are tied up. So my idea has always been that you try to think about India from a dedicated allocation.

[00:03:11] Arvind Chari: So you don't look at India from an emerging market lens, you don't look at India from an Asia lens, but try and look at India from a dedicated allocation.

Linking GDP growth to market returns

[00:03:39] Arvind Chari: And the reason for that is very simple: since the nineteen eighties — that's when India kind of opened up to private sector, foreign investments happened in nineteen ninety, ninety-one — since then the Indian real GDP growth has been averaging about six point three percent. The nominal GDP is in double digits. And you've seen that growth gets reflected in nominal revenues and earnings on a cyclical basis, and then gets reflected in India's stock market.

[00:04:10] Arvind Chari: So Indian stock market returns are very closely linked to the GDP growth. We can't say that about many other countries. I've run charts on many countries depending on whether they are authoritarian or democratic, whether they are single party or coalition, developed or emerging. It's in very few countries that this link between GDP growth and market return is very visible.

[00:04:35] Arvind Chari: And you can take a very long series of that in India. I've run charts from twenty-five, thirty years ago, and that link is very close. Which is why then I make a point saying that because India has that predictable link between GDP growth and market returns, you can potentially look at what I would call a GDP-weighted allocation. Now in academic circles, this would be, how will that happen?

[00:05:00] Arvind Chari: But in the late nineties and early two thousands, this was a reasonably simple way of looking at allocations. And many investors started doing that, saying that if GDP growth is happening in emerging markets and GDP growth creates opportunities, then should we have a higher allocation? That was the basic idea. It hasn't worked because there are governance reasons for why GDP growth might happen in say Brazil, but it is concentrated in resource, commodity sectors and the equity markets do not see a benefit.

[00:05:32] Arvind Chari: Or in Russia, where it's just crony capitalists who are capturing the GDP growth, and there is no growth that comes, no earnings that remain for financial investors or minority shareholders or other companies. So there are various reasons for that. But India is different. We have a semblance of rule of law, we have a democratic process, and the economy and the markets are diversified.

[00:04:56] Arvind Chari: So it kind of works in India. And that's been my major idea — saying that investors should not bracket India as part of an emerging market or Asia. The growth opportunity has been significant and will continue to remain for the next decade or two, given our demographic transition. We can continue to have that same six percent real GDP growth, double-digit nominal GDP growth over a long period of time.

[00:04:56] Arvind Chari: And hence investors should look at India on a dedicated basis as compared to trying to play it through a global or emerging market allocation, which has potentially not worked for them.

[00:05:31] Arvind Chari: Which is why they've also pulled money out of emerging market allocations, and so allocation to emerging markets has fallen. So that's my idea.

Sizing India's global capital allocation

[00:05:40] Arvind Chari: So if this was possible, an India-specific allocation, what do you think the size of the capital pool we'd be looking at would be, and how do we improve access to it?

[00:05:50] Arvind Chari: So the way I frame global assets under management — UBS does a global wealth report which puts total global wealth at about four hundred trillion. There are a lot of studies on this. I think the way I frame it for my research and my analysis is that the global AUM is about three hundred trillion, just about around that.

[00:06:18] Arvind Chari: And if I break it into what we call asset owners — sovereign wealth funds, some central banks also act as sovereign wealth funds, pension funds, global pension funds, insurance companies, and then endowments and foundations. So these are your typical asset owners. And then there are asset management companies, global AMCs, who either manage their own money or manage individual money.

[00:06:46] Arvind Chari: So if I add all these up, and I say what is global AUM, that's about three hundred trillion. So that's the pool of money available for investment in the global world. Of that, if I look at India — public markets, right — if I look at equities and debt, at market value, that number as of end December was about nine hundred billion dollars. I think the recent numbers have gone down because the rupee has depreciated, the market has fallen, so the number would have come down to about eight hundred, eight fifty.

[00:07:19] Arvind Chari: So that's the total market value out of the three hundred trillion. This is the way you work out that less than a trillion dollars is in India in the public market. That's less than thirty basis points. If I add what we also know as private investment — foreign investors also invest in India in private equity, venture capital, infrastructure and real estate.

[00:07:19] Arvind Chari: So if I add that, it's very difficult to get market values for that.

[00:07:47] Arvind Chari: But I would assume that in gross flow, it's about five hundred billion dollars. So you assume that it has returned two x. So that's another trillion dollars. So if you add both, about say two trillion dollars out of the three hundred trillion, that's about sixty basis points of total allocation.

[00:07:47] Arvind Chari: Now, you should argue rightly that that three hundred trillion is not available to be allocated for everybody, because as I said, people have home biases.

[00:08:10] Arvind Chari: So even if you assume that the investible AUM out of the three hundred trillion is a third, so one hundred trillion is available from these global institutional investors to be allocated to other countries — if you take that perspective, so the two trillion, one trillion of public markets and one trillion of private allocation, divided by the hundred trillion as investible AUM, it's decent. It comes to about two percent.

[00:08:38] Arvind Chari: But the way to think about India from that perspective is that India's weight in global GDP is already about three and a half percent, close to between three and four percent. India's weight in global market cap is also somewhere around that region. So technically, from an opportunity perspective, India's already higher, and India's weight in the MSCI All-Country World Index, which is the most commonly used benchmark for global allocation, is about one and a half percent now. It used to be about two percent in September twenty twenty-four; since the Indian market has, so to speak, come down, it's come down to about one and a half percent.

[00:09:10] Arvind Chari: So India has allocations but it can be a lot higher. And as an investor, you're looking for future growth. You don't invest on past returns or past growth. So because India has that ability to keep growing at that double-digit nominal GDP if possible, and that reflects in returns, then the allocation should reflect what could be India's potential size in the global economy in say five, ten, twenty years, because these are long-term investors.

[00:09:38] Arvind Chari: They don't invest for a year. They invest for decades. So if they frame it from that perspective, then the actual allocation to India should have been say three to four to five trillion, as compared to the one trillion in public markets and another trillion in private. This is the way I frame it.

[00:09:38] Arvind Chari: And I will say that India is under-allocated in global portfolios. Some of that is because of their own ability of how they allocate, and home country bias, and emerging markets, and how much risk they want to take.

[00:10:09] Arvind Chari: Most of them don't make country allocations. Now think about an individual as an allocator in a US pension fund working on a government salary. They make an India allocation, it's dedicated, and then you see the last eighteen months that India has completely underperformed. And they could potentially get fired for that.

[00:10:09] Arvind Chari: So why would they take career risk? That is an aspect that happens, and their governance has to change and their allocations have to be broader, and they have to make that call to make a dedicated allocation to India.

[00:10:40] Arvind Chari: And there are aspects in our country in terms of, I don't think that policymakers are even thinking that this could be the potential opportunity — that India should be getting four to five trillion dollars of global capital, which could also mean that if that's spread over say ten, fifteen years, that's two hundred, three hundred billion dollars of annual capital flows. When they think like that, the way they think will be very different, I would assume.

Policy reforms to attract foreign capital

[00:11:08] Arvind Chari: Yeah, so if we want investors to be thinking about India in this way, to get to this kind of ideal allocation, then we'd have to be looking at the policy side in India as well, right? Do you think the government right now is working towards this as an objective? Or what do you think some of the changes we need to see on the policy regulatory side are?

[00:11:28] Arvind Chari: I think, since the nineteen nineties, we've come a long way. From right from RBI and SEBI and the government, they have opened up many sectors, many parts of the economy, public markets, private markets to foreign investors. So they seem to be understanding, and we've understood over policy, that money is required. And the way I frame it is that you also need that money for growth.

[00:11:55] Arvind Chari: If India has a desire to grow at eight percent real GDP growth, that should be at least the bare minimum that we should be able to give, given our current demographic transition, the demographic dividend as we call it. And if you want to do that, you need investment to GDP at about thirty-eight, forty percent. Current investment to GDP is about thirty to thirty-four percent, and domestic saving is already kind of maxed out. Which means you need foreign capital.

[00:12:18] Arvind Chari: You need four to five percentage points of annual capital flows as a percentage of GDP into India. This year it's zero. We know net capital flows are zero this year. So that's the gap.

[00:12:18] Arvind Chari: So if you want to attract four to five percent of annual global capital flows into India across public markets and private markets and infrastructure and real estate, you need to do everything. Everything should be focused from that perspective, whether it is taxation, whether it is the silliness that we have in terms of capital gains tax on foreign investors.

[00:12:50] Arvind Chari: If you go to any OECD country, they may tax the domestic investors in a different way because they want to balance the domestic tax rules. But no one taxes the foreign investor. The foreign investor is taxed at his home country. India is different from that perspective, that we tax foreign investors in our country.

[00:12:50] Arvind Chari: And that has a huge impact not only on operational aspects, but it increases the threshold rate of return that foreign investors need to allocate capital to India.

[00:13:15] Arvind Chari: At a time when you need more capital, at a time you need capital for growth, at a time you need capital to build your own markets, why would you do something like that? And tax is only a small part. There are so many other policies in terms of access, entry, registration. They can review the entire thing if they frame it from this perspective — that globally investors can actually deploy two, three trillion dollars more global capital to India.

[00:13:41] Arvind Chari: And that will help us grow at eight percent real GDP. If that is the policy framing, I think the outcomes from the policymakers, government, RBI, SEBI will be very different, and they will be a lot more welcoming of the foreign investor. They will listen more to the investors in terms of what are their pain points, why are they not allocating? For example, we've started to do something on the bond index.

[00:14:04] Arvind Chari: Like the bond index inclusion — we've realized, okay, we want to get included, and there are certain changes that need to be made, and we've done that. As you open up and frame it in this perspective that two, three trillion dollars can come and that can help us grow faster, I think the framing and the policy will be very different from all regulators.

Lessons from other emerging markets

[00:14:21] Arvind Chari: So we know that a lot of other EMs have also been working to open up their economies, make themselves more attractive to investors. So here, you are arguing that India should actually stand out from the EM pack. Do you think there are any lessons we can take away from these other EMs though, and how things have been changing over the last maybe two decades?

[00:14:41] Arvind Chari: Yeah, from a flow perspective — what we get in India is portfolio flows in equities, and now we'll get a lot of flows in debt because if India gets included in the Bloomberg Global Aggregate bond index, it will be sizable passive flows. It can go out when things go bad. So it's not always your good friend, but still, you get included and you get flows.

[00:15:07] Arvind Chari: In what gets categorized as FDI, foreign direct investment, a large part of that foreign investment that comes to India is what I call financial FDI, which means it comes from financial investors. So it comes into private equity, venture capital, infra, real estate. They might go and build factories, they might go and build new businesses, but mostly we know that it's financial sector, it's healthcare, it's been in fintech and consumer tech.

[00:15:36] Arvind Chari: Anything in tech, consumer, education, and finance. So it's mostly been that. We don't get as much what I call MNC FDI — a global corporate coming and setting up a base in India, manufacturing or services. In services, we've got significant traction on the GCC.

[00:15:36] Arvind Chari: But in manufacturing, either manufacturing for the Indian market or manufacturing in India and exporting as well, we don't get a lot of that.

[00:16:03] Arvind Chari: Whereas, for example, Vietnam has had a very different approach. The China plus one story on manufacturing and sourcing has basically been Vietnam. We've got very little — maybe Apple is one test case for us, one success case. Otherwise, it's been Vietnam.

[00:16:03] Arvind Chari: So they get a lot more FDI as a percentage of GDP than India, and they get that from these global corporations. So maybe one aspect could be, we need financial investors and we need a lot more of them, and I told you the total AUM available there.

[00:16:32] Arvind Chari: But we also need global corporations to come and set up their manufacturing or their basing or their sourcing in India. That will actually diversify the source, and that can potentially be a lot bigger flow, because corporates don't think the way investors do. Investors might still consider India an emerging market and never make a dedicated allocation, whereas given the size of the market in India, many corporates will say, no, I want to be in India for supplying to India and also as a base for my global exports.

[00:17:06] Arvind Chari: So that can actually change quite dramatically if India — again, the policies are even more important. It might be easier to tweak on the capital markets and access, but on land, labor, factor markets, as you must have researched a lot on, it's very difficult to do that. So take examples from Vietnam and other emerging countries who have got these kinds of corporate MNCs, global MNCs, to come and set up capacity, and maybe you'll see a lot more.

[00:17:34] Arvind Chari: On the capital market, apart from access and taxation, I think Indian capital market infrastructure, access infrastructure, ability to allocate capital — you can always reform some of the KYC or entry access. Like if you're a global pension fund, why do you even need to register in India as a foreign portfolio investor? Or you do that, but make it seamless. Make it automatic.

[00:17:34] Arvind Chari: You can do things like that.

[00:18:02] Arvind Chari: Yeah, thanks for speaking with us today. I think it was great, among all this panic we've been having about foreign investors in India, to get some specifics on what could actually change in the landscape. Again, thanks for speaking with us today, Arvind.

[00:18:15] Arvind Chari: Thank you so much. Thanks.

References

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