India: The missing piece in a sophisticated global equity portfolio

Highlights

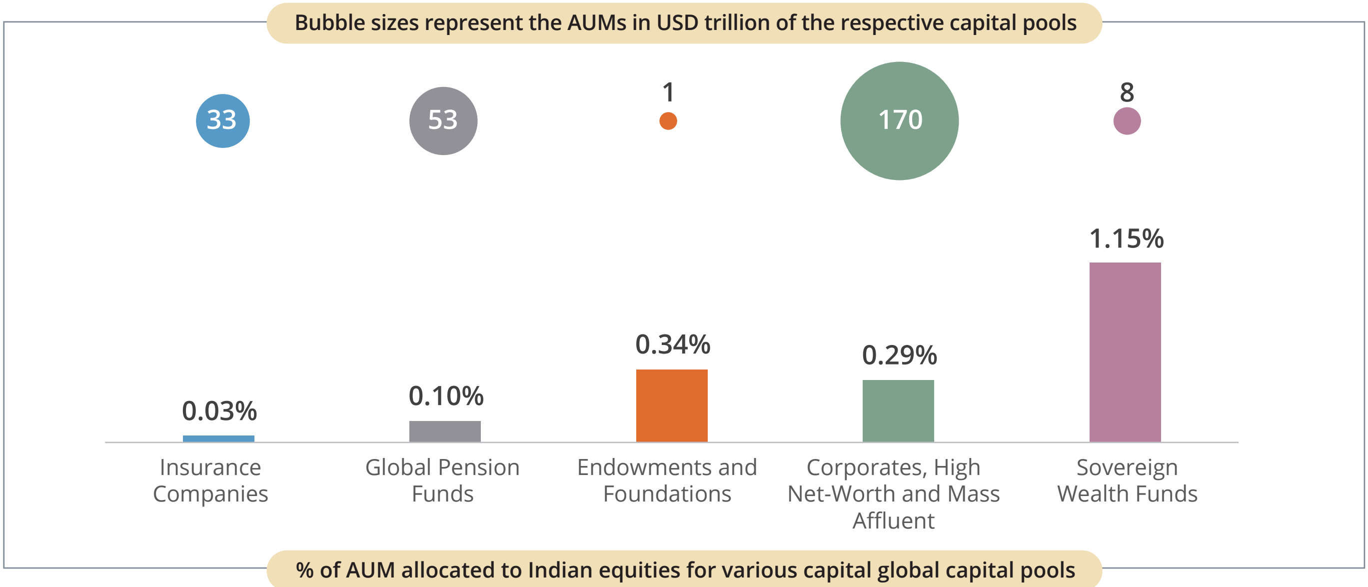
- India; world's 3rd-largest economy by 2030; yet only 0.25% of global equity portfolios.
- India's consumption growth fuelled by 1.4+ billion population, brimful of aspirations and talent.
- Reforms & Infrastructure are beginning to drive growth - typically a 2.5-3x GDP multiplier.
- Manufacturing and Digital are early-but-delivered successes.
- Huge opportunity ahead, and the time to participate is now!

India is currently the world's 5th largest economy with a gross domestic product (GDP) of $3.7[1] trillion. It is projected to be the third largest by 2030, surpassing Germany and Japan, and behind only the U.S. and China. *But is this juggernaut-called-India adequately reflected in global portfolios?* Hardly.

Following are our three key observations

First, **current portfolio allocations.** India's 3+% share of global GDP should more than double over the next two decades. Despite this, global funds are heavily underinvested in India at present, with only a 0.25%[2] share of Indian equities as a percentage of their aggregate Assets Under Management (AUM). This is further detailed in Figure 1.

Figure 1: Global pools of capital are heavily under-allocated to India

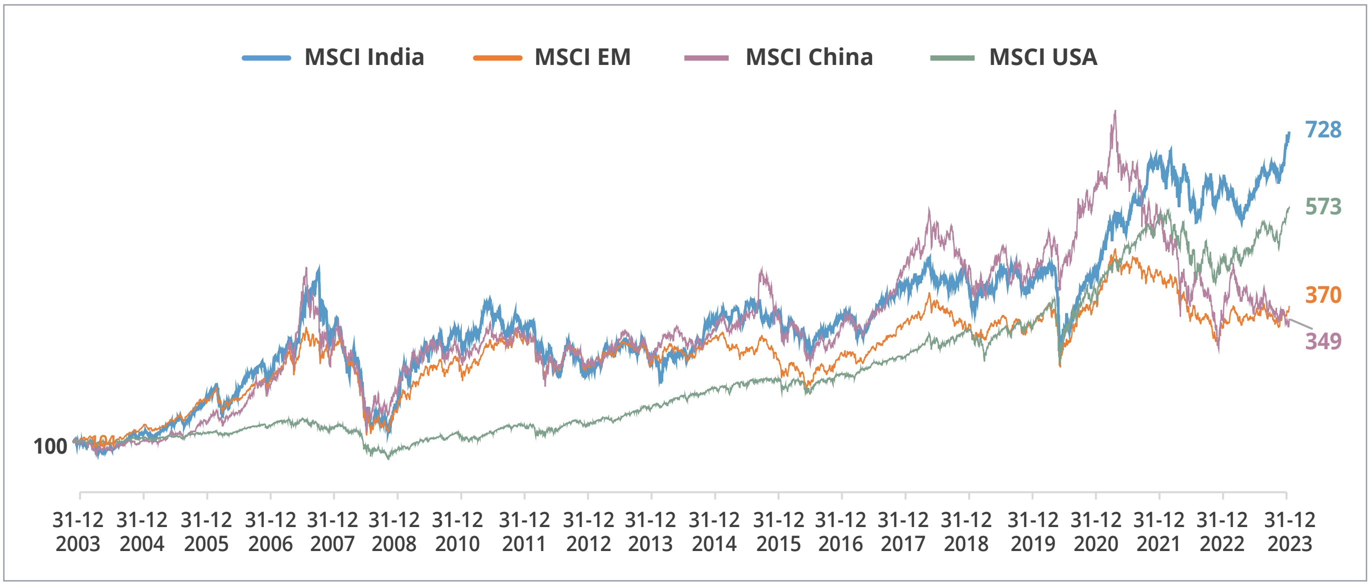


Note: % indicates weight of Indian equities in global equity portfolios

Source: PWC Global Wealth study, Willis Towers Watson (Global Pension Study, 2022), Credit Suisse report (Credit Suisse Single Family Office Index 2022)

Second, the **risk-return profile**. Historically, Indian equity markets have outperformed comparable economies across most periods. Please see Figure 2 for a 20-year comparison of India versus the U.S., Emerging Markets and China. Equally important, are the potential benefits of diversification that India offers to a global portfolio. As Figure 3 shows, the correlation of Indian markets with US, EMs and China has been falling, which should enthuse investors looking for uncorrelated return streams.

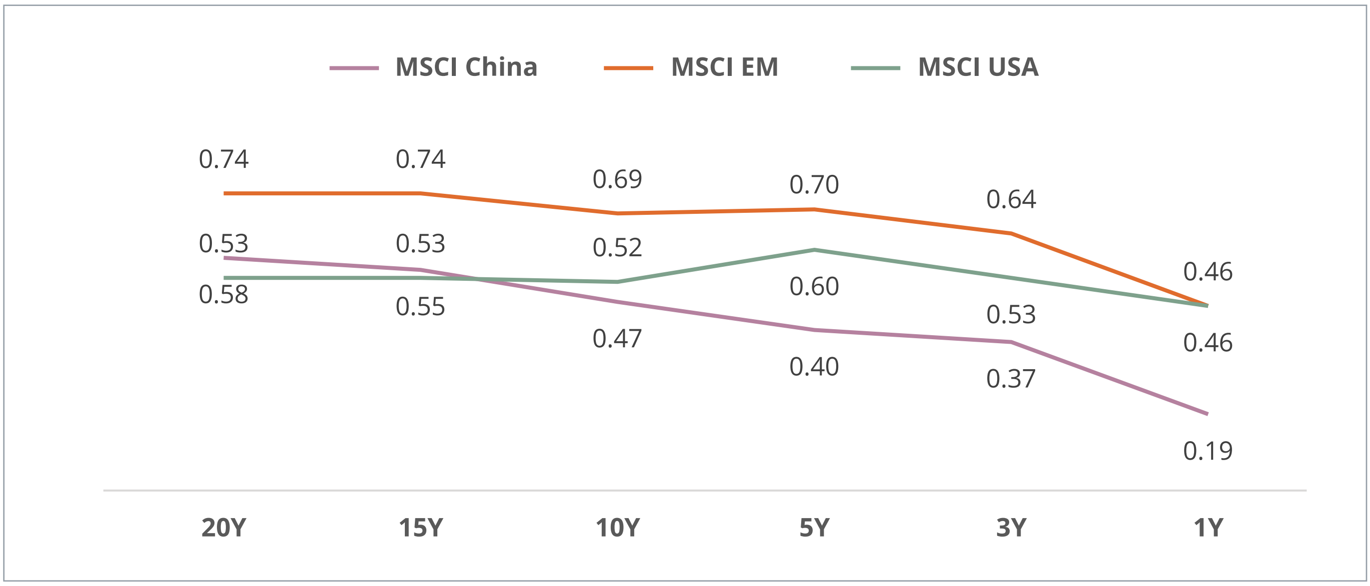
Figure 2: Indian equity returns have outpaced other major markets (2004-2023)



Note: Above trends represent movement in MSCI index for respective countries, rebased to 100

Source: Morningstar data for MSCI Indices; Total Return Indices (Net Returns) considered between 31-Dec-2003 and 31-Dec-2023

Figure 3: Long-term correlations of Indian equities versus China/EM/USA - reflective of potential portfolio diversification benefits

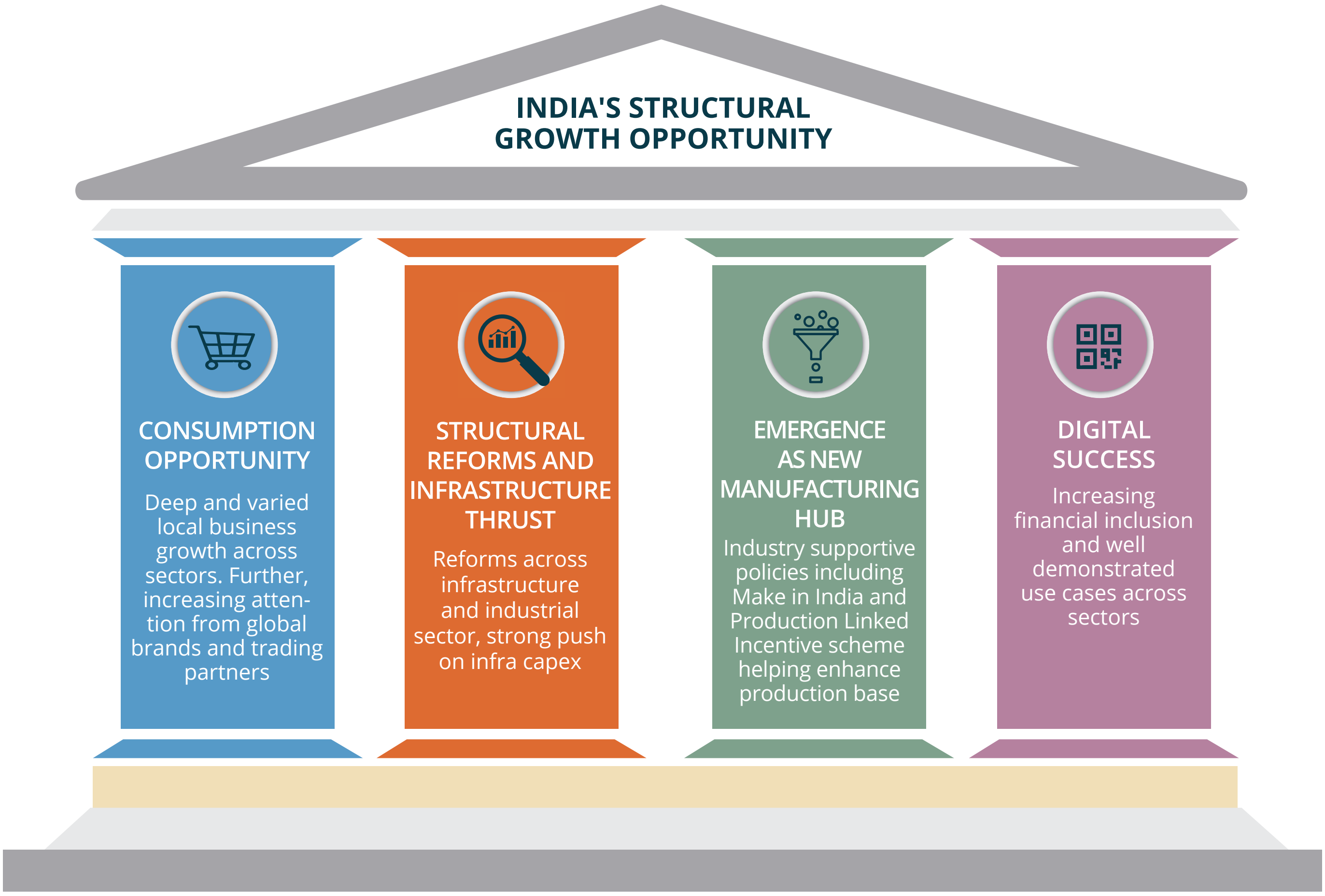


Source: Morningstar Direct, using cross-correlations of weekly index returns, 31 Dec 2023

India has world-class, capital-efficient companies across multiple sectors, and this means that growth translates to share price performance over time. Those investors who are aware of India's outperformance sometimes cite expensive valuations. For the record, India in recent years has always traded at a premium due to its structural long-term growth profile. **How many countries with $3.7 trillion GDP can realistically grow 6-7%+ annually in real terms for the next few decades or more?** Probably no other. India's equity index P/E multiple[3] is ~18 times 1-year forward. This multiple is not low but is still below its 20-year average of ~20x. We strongly believe that a robust earnings profile as well as deleveraged balance sheets will provide support to corporate India's underlying profit growth, which should in turn support stock prices.

Third, **long-term and impactful reforms** will continue to drive India's structural progress. 'Star performer'[4] India's growth momentum is expected to be 6.4+%* for the next five years, making it one of the fastest-growing large economies. As Figure 4 shows, the four structural pillars that will drive this growth and attract more foreign funds to India are a) consumption, b) reforms and infrastructure, c) manufacturing hub and d) digitization.

Figure 4: Four structural pillars that will support India's structural growth



Source: CRISIL MI&A Research

*Source: Crisil Research and Analysis

Why are we so excited by each of these growth engines?

Pillar 1: Consumption opportunity

With a 1.4+ billion population, India surpassed China as the world's most populous country in 2023 and now accounts for >17%[5] of the global population. India's demographic dividend is driving significant consumption and the trend is just getting started. **Visualize an aspiring population, but 4x the size of the U.S.**! Some of India's largest states are comparable to entire countries in terms of population. For instance, if Uttar Pradesh, India's largest state, were a standalone country, it would be the 5th largest in the world! Maharashtra, India's second most populous state, is comparable to Japan (122+ million)*. Ditto for Karnataka and Gujarat, which are comparable to the U.K. and Thailand, respectively. That said, India ranks much lower in terms of per capita income, which stands at only $2,610[6]. In comparison, China and Japan's per capita income are 4.8x and 12.9x of this, respectively. Clearly, there is a significant runway with an extensive opportunity that underpins the structural growth potential.

Out of India's total GDP, 60%[7] comes from consumption, which is growing rapidly as India has one of the world's largest youth populations. The median age is just 28 years, while China is at 39 and Japan at 49. It is estimated that 64%* of India's population is between 15-59 years of age. The large share of India's working population, coupled with rapid urbanisation and rising affluence, will support consumption and economic growth over multiple decades. An aspirational middle class continues to drive sales momentum across key sectors, such as fast-moving consumer goods, real estate, automobiles, as well as travel and tourism. Also, India's younger demographic base will help to reinforce its competitive edge for the next few decades. **For instance, in 2023, 9 million[8] iPhones were sold in India. Of this, 60% were sold outside Tier 1 cities!** Similarly, spending on online retail is spread across urban and rural India.

With growing brand awareness, people are ready to spend on global products as their discretionary incomes grow. More than two dozen international brands, including Balenciaga, Shein, Gap's Old Navy and Banana Republic, Armani Caffe, Maison de Couture from Valentino are exploring a foray into the Indian market, encouraged by the surge in consumption. Early entrants such as Zara, Mango, H&M, and Levis are already benefiting from healthy sales growth in the country. There is significant opportunity across a wide range of price points. For instance, luxury brands entering India are buoyed by rapidly increasing millionaires. A Credit Suisse Global Wealth Report forecasts that the number of Indian millionaires will double from 796,000 in 2021 to 1.6 million[9] in 2026.

Pillar 2: Structural reforms and Infrastructure thrust

India's economy witnessed a series of structural reforms since 2015, which were implemented by the current pro-development Modi government. Key reforms include Goods and Services Tax (unifying and streamlining dozens of central and state taxes into just one), Jan Dhan Yojana (opening 500+ million[10] bank accounts in five years), labour reforms (merging and updating 29[11] archaic central laws into four codes), and the Insolvency and Bankruptcy Code to name a few. The infrastructure arena is gaining considerable traction in India, with the central government doing the heavy lifting. Infrastructure capex has a significant GDP multiplier effect (2.45x* in the first year and 3.14x* in the following year for every rupee spent), as it opens growth avenues for other sectors. For instance, **since Independence (in 1947) to 2014, the country had only 65[12] airports, which in the last 10 years has doubled to 140[13] and is further set to hit ~220+ by 2030 - a truly staggering number!** Furthermore, India's road and transport budget had a nine-fold increase in the last decade. Infrastructure investments are likely to remain firm, ensuring healthy GDP growth over the next five years. Growing funding needs will present investors with new investment vehicles, such as infrastructure investment trusts, unlocking asset monetisation and fresh investment opportunities.

Pillar 3: Emerging as a new manufacturing hub

India's industrial sector is projected to grow from USD ~480 billion* currently to USD ~675 billion* (i.e., 1.4x) over the next four years. It's still tiny compared to China at USD ~5,100 bn*, which augurs well for India's strong growth ahead. The country's manufacturing potential is already benefitting from the central government's push via programmes such as 'Make in India' and 'Production-Linked Incentives's (PLI). These aim to incentivise companies for setting up production bases and supply chain integration in India.

Take for instance, the success of mobile manufacturing in India. Of the 14 sectors identified, PLI for mobile phones (announced in 2020) has seen the highest momentum. **It helped transform India from being a net mobile phone importer to a strong global exporter (USD 0.85 billion imported in FY[14] 2021-22 vs. USD 11.2[15] billion exported in FY 2022-23).** Mobile phones are expected to contribute more than $50[16] billion worth of exports by 2026. In fact, as per recent reports, Apple's contract manufacturers Foxconn (Hon Hai) and Pegatron, as well as the Tata Group, are expected to start developing the iPhone 17 in 2024, marking a significant milestone in Apple's efforts to diversify its supply chain. The Indian government set a target of achieving $300[17] billion worth of electronic (including mobiles) manufacturing by 2026, with $12016 billion expected to come from exports.

In addition, with the approval of the $9 billion[18] 'Semicon India Programme', the semiconductor sector and its related ecosystem will also grow. Investments under such programmes will help India increase its share of manufacturing in GDP, which currently stands at 18%[19].

Pillar 4: Digital success

Along with the physical economy, the digital economy is also playing a major role in promoting India's economic growth. At more than 880 million[20], the country has the second-highest number of internet users globally, and at one of the lowest data prices (~15 cents per GB)*. In the past decade, India has seen a spate of digital innovations, enabling various entities, including governments, businesses, and individuals, to interact and conduct transactions electronically. These innovations are transforming payment patterns and encouraging skill development.

A standout example is the Unified Payments Interface (UPI), which is a locally developed peer-to-peer instant payment system that is free for the end-user. **UPI is ubiquitous today and is used by Indians to pay for everything, including vegetables from a street vendor, an Uber ride or even food and grocery deliveries.** Simply whip out one's phone, scan a QR code, and pay instantly as one's mobile phone is linked to a bank account and biometric ID. Over the last two years, UPI transactions have logged a CAGR of 94%* in volume and 84%* in value. In just the one month of December 2023, UPI payments touched ~12 billion* in volume and ~USD 220 billion* in value. India's industry is developing into an innovative digital ecosystem with online transactions growing by 70%* vs. cash withdrawals, which have stagnated at growth of 7%*.

A significant increase in e-commerce across geographies, together with rising digital literacy are supporting financial institutions to target new segments such as by cross-selling with lending services, shopping, education, and tourism to name a few. Improvement in both digital and physical infrastructure has enabled e-commerce companies to deliver products to all serviceable pin codes across India, with 97+%* of pin codes receiving their deliveries within two days of placing an order.

The rocket ship has launched, and investors should get onboard.

India is still viewed by some global investors as a tactical trade, while other investors elect not to have any allocation to India at all. Some others consider their India exposure via MSCI All Cap World Index (ACWI) or MSCI Emerging Markets Index to be sufficient. But with India making up just ~1.7% of the former and ~16.7%[21] of the latter, such an allocation is likely suboptimal. The four growth pillars detailed above will shape India's long-term growth trajectory – and provide an exceptional long-term opportunity for alpha-seeking foreign investors. Thus we strongly believe that India should be a **dedicated stand-alone allocation** in every global portfolio.

To learn more about ASK's investment strategies, Please write to us at
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