
INDIA: STABILITY AMID GLOBAL POLITICAL UNCERTAINTY

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[Ahead of the monthlong Indian elections, we held a “Behind the Markets” podcast preview](#) with Gaurav Sinha, Associate Director of [Modern Alpha](#)[™] and Asset Allocation at WisdomTree, and Srinivas Thiruvadhanthai, director of research at the Jerome Levy Forecasting Center. Our discussion, which suggested Modi was going to stay in power with a 70% probability, was quite prescient.

Thiruvadhanthai sees the global economy in a precarious spot with uncertainties due to the ongoing trade war. In his view, the U.S. is in the late phase of an expansion but would remain in decent shape amid a more synchronized global slowdown.

Nonetheless, some risks remain. Even though the U.S. is not a major exporter, many U.S. companies have a global footprint. Furthermore, [volatility](#) in the stock market flows through to the economy. Thiruvadhanthai said the top 5% of income producers (who are large equity holders) contribute 40% of consumption in the U.S., so equity price falls like we saw in the fourth quarter of 2018 heavily weighed on retail sales.

A Bright Spot of Political Stability

Incumbent Prime Minister Narendra Modi was elected to a second term in the latest elections. Putting the victory in context, Modi’s party won a clean majority, which was the first time this happened since 1971. India’s political system is unlike the primarily bipartisan one that we are familiar with in the U.S. Sinha mentioned that over 300 political parties participated in this latest election. This victory is a clear choice for Modi’s party and the measures it enacted in his first term.

Many of Modi’s reforms were designed to fight corruption and encourage economic growth. The new [Goods and Services Tax \(GST\)](#) was implemented to mitigate tax burdens, and a surprising [demonetization](#) initiative made 90% of India’s currency no longer in use. These were difficult reforms but likely good decisions in the long run.

Sinha predicted Modi will read his success in this election to continue pushing for even more bold reforms. There are more market-friendly reforms that economists and the general population want to see. This might come via labor market reform or land acquisition reform because it can cost more to acquire land in India than in the U.S.

Indian companies purposely stay small in India because it is difficult to fire workers if you have more than 100 employees, and there are even more benefits from less onerous regulations if you have fewer than 20 workers. People have been discussing labor market reforms for 25 years and no one has touched this area given the sensitivities, but Modi

has shown a tendency to tackle these difficult reforms.

Sinha believes there are more fiscal and monetary reforms that will help boost growth in the near term, such as continuing to simplify the tax code, privatizing state-run companies, and boosting capital injections in stressed banks.

While global trade continues to dominate headlines, India stands out in all the research as having the least connection to Chinese trade. India, like the U.S., runs a big trade deficit with China, as it is a net importer of goods from China. India's economy is built on domestic consumption more so than exportation, which is one of the reasons it trades at a premium to most emerging markets.

Sinha was more cautious on India at the end of 2017 into 2018 with much of the uncertainty around short-term disruptions to economic activity caused by demonetization and GST. But with those out of the way and Modi still in power, Sinha thinks now is a good time to add exposure to India.

Please listen to our full podcast on India and the global economy below.

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

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Modern Alpha: Modern Alpha® combines the outperformance potential of active with the benefits of passive—to offer investor strategies that are built for performance.

Volatility: A measure of the dispersion of actual returns around a particular average level.

GST Bill: India's Goods and Services Tax Bill aimed at streamlining the country's tax system.

Demonetization: The act of stripping a currency unit of its status as legal tender..