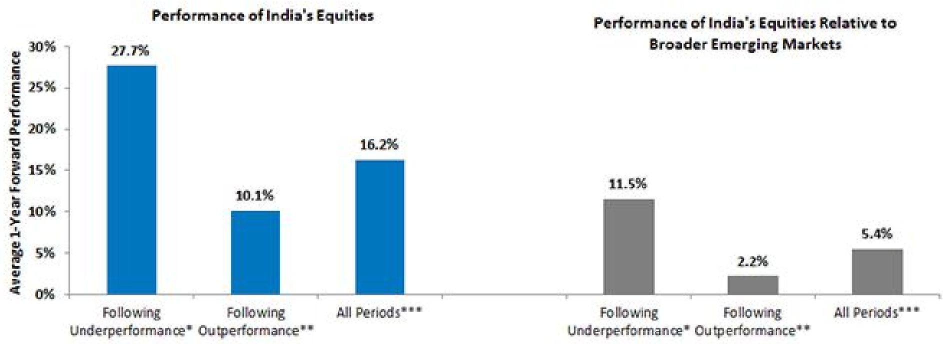
IS INDIA A BRIGHT SPOT FOR EMERGING MARKETS IN 2014?

Christopher Gannatti — Global Head of Research
03/24/2014

Anyone who follows emerging markets has been disappointed with the returns they have seen in these equity markets[1] over the past few years. There have been lackluster returns and downward-trending rates of economic growth, which is the opposite of what we've seen in developed markets, especially the U.S. While some will surely consider increasing allocations to developed market equities, we believe that contrarians out there may also be wondering about the potential for attractive entry points into certain emerging markets. Based on my research below, I believe India presents such an interesting opportunity. **Unlocking India's Potential** The story of India as both an economy and an equity market is one that tends to focus on the longer term. The country's massive population, coupled with a favorable demographic picture, definitely points to the potential for a growing consumer class in the future. However, in the recent past, what have investors in India gotten? In a word: volatility. India's markets tend to be more volatile than the broader spectrum of emerging market equities[2], so they have the potential to capture swings in sentiment that impact emerging markets, which of course can be both positive and negative over time. **A Simple Look at Mean Reversion** In evaluating India's equities, we looked for a framework to utilize the available return history to better understand if there were any simple trends that occurred in years after: • The MSCI India Index (India's equities) **underperformed** the MSCI Emerging Markets Index (broader emerging markets) for one year • India's equities **outperformed** the broader emerging markets for one year 2013 was a tough year for India's equities, which underperformed the broader emerging markets. The key question: Does history suggest India is likely to bounce back for 2014? Early indicators for the first few months have been pointing in that direction. Of course, no matter what our result, there is never any guarantee that past performance can indicate a future result, but the following analysis shows how India's equities did after one-year periods of both out- and underperformance compared to the broader emerging markets. **India's Equities Performed More Strongly *After* Underperforming Broader Emerging Markets**



Source: Bloomberg. Past performance is not indicative of future results. You cannot invest directly in an index.
* Following Underperformance: As specified, average performance of India's equities and average performance of India's equities compared to the broader emerging markets for one-year periods following underperformance against the broader emerging markets.
** Following Outperformance: As specified, average performance of India's equities and average performance of India's equities compared to the broader emerging markets for one-year periods following outperformance against the broader emerging markets.
*** All Periods: The average one-year return following all periods. In this case, 20 calendar years of data were used (12/31/1993-12/31/2013).

Looking at the Performance of India's Equities: In our three categories, India's average performance following underperformance of broader emerging market equities is stronger than following outperformance or just looking at the average of all one-year periods. In particular, India performed 27.7% on average in years following periods of underperformance, which was more than 11 percentage points better than its average return of 16.2% per year. • To give some individual examples of strong periods—one of the best returns came following the 2008 downdraft: the 2009 return was 102.8%. Two other strong years, 2005, with a return of nearly 40%, and 2012, with 26%, also followed years of India's equities underperforming the broader emerging markets. 1996 was the only year where the performance of India's equities was negative, following underperformance of broader emerging markets. • On the other end of the spectrum, in 2007 India's equities outperformed broader emerging markets by 33% but were down about 65% the following year. • In short, it does appear that India's equities have exhibited the potential to snap back after periods of outperformance or underperformance against the broader emerging markets, but of course this can offer no guarantees of what the future may hold. **Looking at India's Performance Compared to Emerging Markets:** There has also been increased outperformance of India's equities compared to broader emerging markets following underperforming years. There were seven times where India's equities underperformed broader emerging markets, and it was only during in 1996 where they continued to underperform in the following year, lagging by 8.2%. The higher end of the range was encompassed by 1997 (outperformance by about 23%) and 2009 (outperformance of about 24%). **Appropriate to Consider Entry?** Of course, the answer to this question is different for everyone, but we believe these simple statistics indicate that India should be of interest in 2014. One crucial consideration involves the relationship between equity performance and macroeconomic drivers, which have the potential to influence the currency and have provided headwind for U.S. investors making allocations to India in recent years. In a future blog post on India, we'll take a look at the impact India's currency has had on the equity market performance for U.S. investors and what the outlook is there. [1]Refers to the MSCI Emerging Markets Index. [2]Refers to the MSCI Emerging Markets Index.

Important Risks Related to this Article

Investments focused in India are increasing the impact of events and developments associated with the region, which can adversely affect performance. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Investments in currency involve additional special risks, such as credit risk and interest rate fluctuations. Investments in emerging, offshore or frontier markets are generally less liquid and less efficient than investments in developed markets and are subject to additional risks, such as risks of adverse governmental regulation and intervention or political developments.

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.

For more investing insights, check out our Economic & Market Outlook

View the online version of this article here.

IMPORTANT INFORMATION

U.S. investors only: Click here to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages (www.msci.com)

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Jianing Wu, and Brian Manby are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only.

You cannot invest directly in an index.

DEFINITIONS

Contrarian : Practice of seeing what the majority of market participants are focused on and attempting to look in the complete opposite direction.

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

Mean reversion : The concept that a series of returns has a tendency to return to its average level over longer periods, even if shorter periods can exhibit wide swings.

MSCI India Index : A market capitalization-weighted index designed to measure the performance of the Indian equity market.

MSCI Emerging Markets Index : a broad market cap-weighted Index showing performance of equities across 23 emerging market countries defined as “emerging markets” by MSCI.

Headwind : challenges to performance or expectations of performance.