

WHY INDIA REPRESENTS AN OPPORTUNITY TODAY

Gaurav Sinha — Associate Director, Asset Allocation and Modern Alpha
07/25/2016

I recently had an opportunity to speak with Morgan Stanley's Head of India Research, Ridham Desai. We discussed a range of issues covering India's macroeconomics in the wake of global events such as [the resignation of Dr. Raghuram Rajan](#) and Brexit. Clearly, there has been no shortage of excitement with respect to India. **Current Market Cycle** Desai believes India is in great structural shape from a medium- to long-term perspective. He said the current growth cycle in India is turning around, though it is still weak and spotty. There has been a sharp turnaround in [capital expenditures](#), engineered by the government, especially in the infrastructure sector. Private sector [capex](#) still appears weak, and India's industry has been facing global headwinds. Overall, Desai described India as experiencing a U-shaped recovery and believes it will take more than 12 months for private capex to pick up, as current capacity utilization is in the low 70% range. The cause of this is partially related to weak global demand for exports. Desai believes that the service sector, which accounts for nearly 60% of India's [gross domestic product \(GDP\)](#) (manufacturing represents 25% and agriculture the final 15%), would continue to push growth higher. Retail loan growth, measured at 20%, is at a multiyear high, leading to sharp pickup in consumer infrastructure—construction of shopping malls, multiplexes and auto showrooms. Job indexes are also up by 25% year-on-year. **Resignation of Dr. Rajan 'Rexit' and the Future of India's Monetary Policy** Since India's prime minister, Narendra Modi, took office two years ago, he and Rajan have worked as a tag team, leading to first stabilize the rupee and then to India becoming an outperformer in emerging markets (EM). What's next? When these two gentlemen started their respective jobs, India's macro situation was very fragile, with a large [current account deficit](#), high [inflation](#), high deficit and low growth. Since then, the Reserve Bank of India (RBI) and the government have worked in tandem, keeping [real rates](#) low and later compressing the fiscal deficit, which led to an enormous improvement in the macro fundamentals of India. Desai also believes that the RBI has a strong track record with a much longer history compared to past governments, and thus a current change in leadership is not surprising. Desai's initial worries of a knee-jerk reaction by the market proved unfounded, and markets have remained steady since Rajan's exit news broke. Fortunately, current deputy governor Urjit Patel, a key member in policy making, has extended his term for three more years. The new governor will most likely be a macroeconomist, according to Desai. Thus, we should expect a similar monetary policy while the government continues to focus on [foreign direct investment \(FDI\)](#), liberalization and other reforms. Further, Morgan Stanley believes another 50 [basis points \(bps\)](#) in rate cuts between now and March of next year is possible, subject to a decent monsoon season. **Building on an Effective Track Record of Collaboration: The Story of Food Prices** A large part of the decline in inflation can be attributed to the decline in food prices—and the government played a key role. Desai explained why negative real rates and increasing food prices were responsible for high inflation. The RBI was effective in controlling the first issue while government fixed the second. **Infrastructure, Infrastructure, Infrastructure: Progress Being Made!** In Desai's assessment, the current government has been working at a phenomenal scale in building public infrastructure. Last year, India completed 6,000 km (approximately 3,700 miles) of highway construction, about three times the annual pace of the last 10 years. The target for this year: 15,000 km (more than 9,300 miles). If only 80% of the initial target were to be achieved, it would still be equivalent to the amount of highway construction done in the previous six to seven years in a single year. Railroads are another sector in which massive public sector capex has occurred over the last year. **Time to Take Action: What Equity Over-Weights Make Sense?** Throughout our conversation, Desai emphasized how retail loans could be one of the key drivers of growth. Private banks have a key exposure to the retail segment and thus would be a market segment that stands to outperform. Desai also highlighted India's household-credit-to-GDP ratio, currently at 13% (among lowest in the world), which could double in the next few years, potentially leading to 20% [CAGR](#) growth for retail banks. [Read our analysis of private banks in India.](#) In Desai's opinion, the Consumer Discretionary sector had favorable [valuations](#), and cyclically near-term earnings look stronger. Finally, he thinks Industrials engaged in building infrastructure could be attractive too. Overall, Desai and I agreed that getting 7.5% growth in the current global environment is difficult. India

currently stands out as a beacon of growth for investors who are willing to stomach some [volatility](#) and potentially would be rewarded with strategic growth, driven by vibrant demographics and low debt ratios. ***Unless otherwise noted, data sources are Bloomberg and Morgan Stanley, as of July 8, 2016.***

Important Risks Related to this Article

Investments focused in India increase the impact of events and developments associated with the region, which can adversely affect performance.

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, Kara Marciscano, Jianing Wu, Brian Manby and Scott Welch 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

Capital expenditures : Spending by a company typically made to enhance longer-term productive capacity.

Capex : Funds used by a company to acquire or upgrade physical assets such as property, industrial buildings or equipment. This type of outlay is made by companies to maintain or increase the scope of their operations.

Gross domestic product (GDP) : The sum total of all goods and services produced across an economy.

Monetary policy : Actions of a central bank or other regulatory committee that determine the size and rate of growth of the money supply, which in turn affects interest rates.

Current account deficit : Situation where a country has a greater level of imports than exports.

Inflation : Characterized by rising price levels.

Real interest rate : Interest rate accounting for the impact of inflation. From the nominal interest rate, which does not account for the impact of inflation, the rate of inflation is subtracted to get to the real interest rate.

Foreign direct investment (FDI) : An investment made by a company or entity based in one country into a company or entity based in another country.

Basis point : 1/100th of 1 percent.

Compound Annual Growth Rate (CAGR) : The mean annual growth rate of an investment over a specified period of time longer than one year.

Valuation : Refers to metrics that relate financial statistics for equities to their price levels to determine if certain attributes, such as earnings or dividends, are cheap or expensive.

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