Asian takeaways

Masala musings

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India has been one of the hottest markets in the region in 2023, capturing investors' attention and making significant gains year-to-date, with the MSCI India Index up 19%[1].

However, travelling to the country in the last quarter of the year, we found it in a state of cooling. In one sense, this was quite literal, as in the post-monsoon months the temperature drops and the usual humidity dissipates.

Yet, speaking more metaphorically, in the aftermath of the Cricket World Cup the country was consoling itself, following its loss against long-standing rival, Australia. The tournament marked the first defeat since 2011 for the world's most populous nation and was a particular blow given India's status as host, dashing the hopes of the 120,000 supporters in Ahmedabad's Narendra Modi stadium and beyond.

Whilst disappointment from fans was evident, it was perhaps felt more keenly by Prime Minister Modi himself. There had been much talk of the World Cup having been conveniently set up ahead of April 2024, when Modi faces re-election for a potential third term, as leader of the Bharatiya Janata Party ("BJP"). It seems that the Australians were not paying close attention to the BJP's master plan...

However, luckily for the BJP, its popularity means that it appears to be weathering the storm, with regional elections demonstrating strong support across the Hindi heartland. It is worth noting that these elections are not necessarily strong indicators for the national election result, as they focus on local issues, with regional power players having more influence, however they are demonstrating a solid backdrop for the party in the run up to April's election. It would certainly be a huge surprise to us, and to the market, if anything but a strong showing from the incumbent were to result.

[1] Bloomberg, as at 30 November 2023.

Thinking ahead to 2024 more generally, investor attention is turning to what is in store for India's stock market, following its recent strong performance. Over the past few years, certain Asian markets have surprised in January, often in the form of a reversal of events in the months or quarters leading up to year end. In this vein, investors are currently focused on the polarised performers of 2023, India and China, and whether we can expect to see a reversal in terms of their performance relative to each other (Figures 1 and 2).

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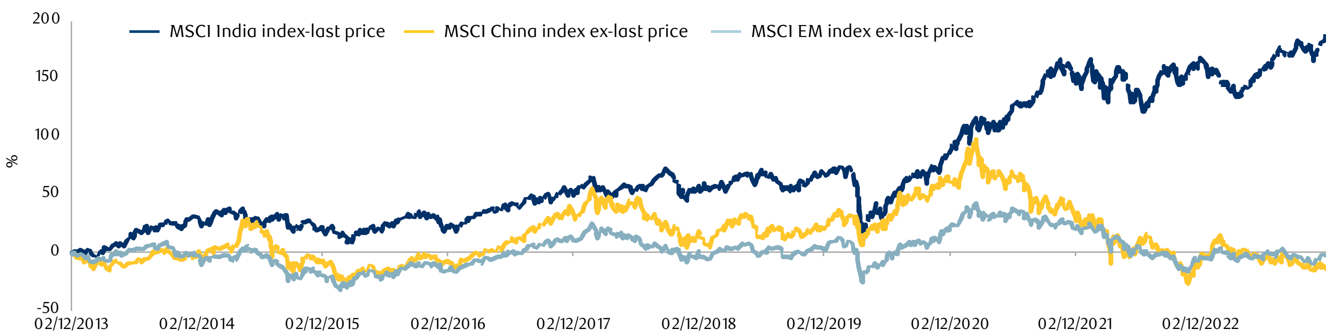
There does seem to be some substance behind this prediction, given China's historically cheap valuations and more supportive measures being touted for the country's embattled property sector. China looks to be on track for a potential value rally in early 2023, in contrast to India's historically high valuations across most, if not all, sectors. However, our view is that this consensus oversimplifies the outlook for these two countries.

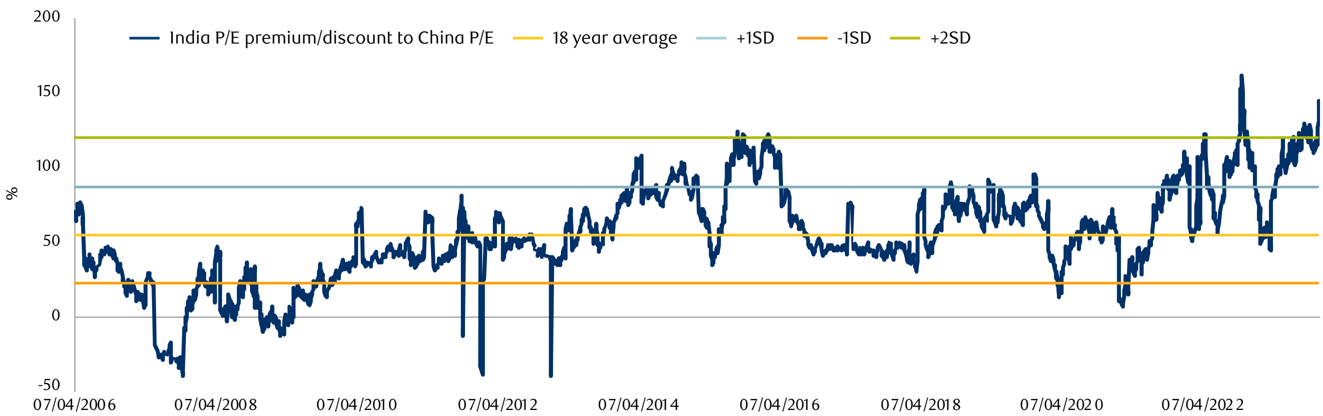
Pride and confidence in India's future shine through, even in the wake of a disappointing World Cup defeat.

Figure 1: Indian stocks have outperformed China and EM peers since the post-pandemic rally



Source: Bloomberg , as at November 2023.

Figure 2: India's valuation premium to China is now at extremes



Source: Bloomberg, as at November 2023.

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For China, a reversal is unlikely to be plain sailing. Global investors continue to be preoccupied with the moral quandaries that come with investing in the region, whether that be the country’s support of Russia in recent years, or concerns surrounding supply chains. For those with an outlook more driven by realpolitik, the loss of confidence amongst domestic consumers is concerning and will likely take some years to rebuild.

For India on the other hand, the good times are rolling, and in our view, it is hard to find many negatives. Whilst this in itself is likely to raise some red flags for investors, the long-term potential for the country is certainly appealing. Meetings with company management during our visit were largely optimistic across all areas of the market, from financials to CapEx plays, and consumer companies to cyclicals. Even the management of staples names that have seen consumption stymied in recent years, as a result of higher inflation, were offering positive outlooks.

Special economic zones help improve the ease of doing business for both local and foreign companies.

India’s position as a key global player has also been bolstered over the course of the year, not least by hosting the G20 leadership summit in New Delhi in September. From our own experience, the international attention on the country was evident at the investor conference attended by David Soh, our Portfolio Manager and Head of Research, with investors from all over the world flying into Mumbai for three days of meetings and presentations with Indian businesses. Taking place at the Trident hotel, Nariman Point, the atmosphere was buzzing, and it was hard to recognise it as the same place that witnessed the Mumbai terrorist attacks back in 2008.

Elsewhere in the city, evidence of the country’s rapid evolution is tangible. India’s digital transformation is well underway, with businesses of all sizes adopting modern technology. Walking around the city, credit card machines have replaced cash payments, and even street food stands now accept digital payments via QR codes.

This global focus and modernisation is by no means confined to Mumbai, and a visit to Chennai, the ‘Gateway of South India’, demonstrated the strength of the country’s offering as an industrial hub. Chennai has a broad industrial base across numerous sectors, as well as being a large global outsourcing destination for IT and business processes. Chennai’s industrial parks play host to both Indian and multinational businesses and are situated within special economic zones, improving the overall ease of doing business.

Modi’s ‘Make in India’ initiative seems to be playing out, with manufacturing industries growing fast and India continuing to establish itself as a frontrunner in the ‘China +1’ model. Exports in newer industries, such as electronic hardware, are seeing strong growth, bolstered by government recognition and policy support, with companies such as Apple already investing heavily in the country.

Manufacturing industries in India are booming. A tour of a production line at a leading electronics manufacturing services (“EMS”) company.

Blending in at the entrance to an EMS factory assembly line.

'Make in India': a supportive policy environment creating new growth opportunities across industries.

That said, traces of China's dominance in regional supply chains are still very much present and easy to observe in production lines, with key parts (lithium batteries, for example) and manufacturing and testing equipment still being heavily sourced from China.

Nonetheless, it is clear that prospects are looking bright for India. Whilst present valuations are unsupportive and over the near term there is a strong likelihood of India underperforming China in the lead up to the elections (especially if China welcomes renewed interest following a difficult 2023), a decade of improvements in taxation frameworks, legislation and policy means that the country is in a strong position to reap future rewards. Even with India's supply chains somewhat tethered to China's, the potential for development across various sectors is huge, and we are already seeing strong evidence of multinationals turning to India as an alternative to China.

> **"With India's market depth and supportive environment, we believe the country still has much to offer."**

It is likely that political stability will add succour to the long-term optimism, but even a surprise loss would not derail continued strong performance over the medium to long term, in our opinion.

Ultimately, the investment case for India has not been weakened by its already stellar performance, and whilst India and China are often mentioned in the same breath, we don't believe their relative merits and future performance are dependent on one another. This is even more the case for bottom-up stock pickers, and with India's market depth and supportive environment, we believe the country still has much to offer.

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