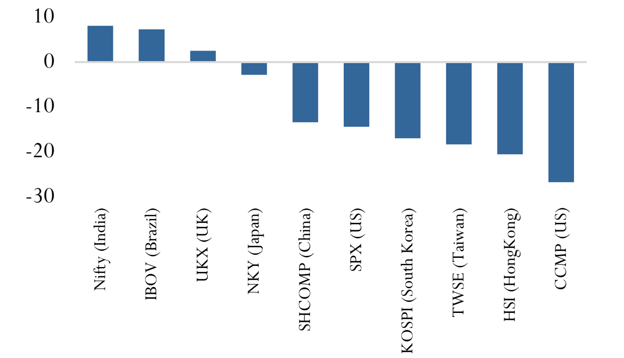
Resilient India

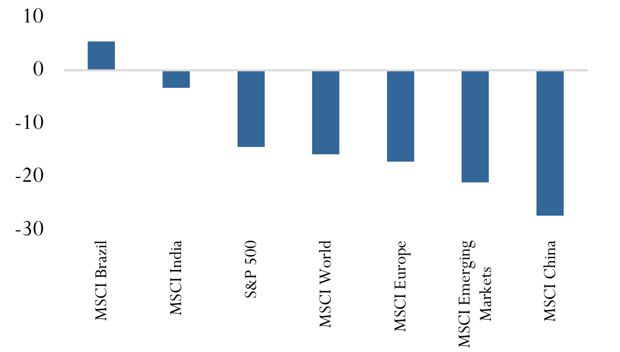
India has been a stand-out outperformer in 2022. This has prompted sharply divided views from amongst the opinion makers and observers. There is the chorus of India bulls who have announced that this is India's decade. And then there are the doubters. They aver that India will lag in 2023 itself as reality check kicks in and the valuation gap with other markets forces a lag.

First the numbers

Returns CYTD22 - Local Currency (%)



Returns CYTD22 - USD (%)

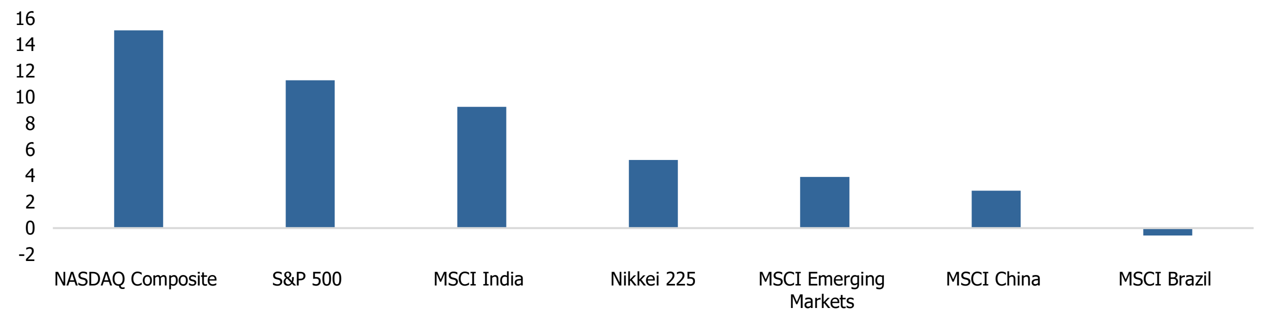


Source: Bloomberg, Spark Fund Research

By any account, India has done well.

Now, look at the longer run performance – from around the lows of the Global Financial Crisis in 2007-08

Annualized returns USD (%)



Note: Annualised returns from 31st Dec 2008 to 30th Nov 2022
Source: Bloomberg, Spark Fund Research

The Indian out-performance has also resulted in India's valuations running away to an all-time high premium over the EM peers. This is a potential risk but also reflective of growth dynamics at work.

Index	Trailing P/E (x)
Nifty Index (India)	23.6
SPX Index (US)	19.7
Nikkei Index (Japan)	18.9
SHCOMP Index (China)	14.1
MXEF Index (MSCI EM)	10.9

Note: P/E as on 30th Nov 2022
Source: Bloomberg, Spark Fund Research

The dreaded D - word

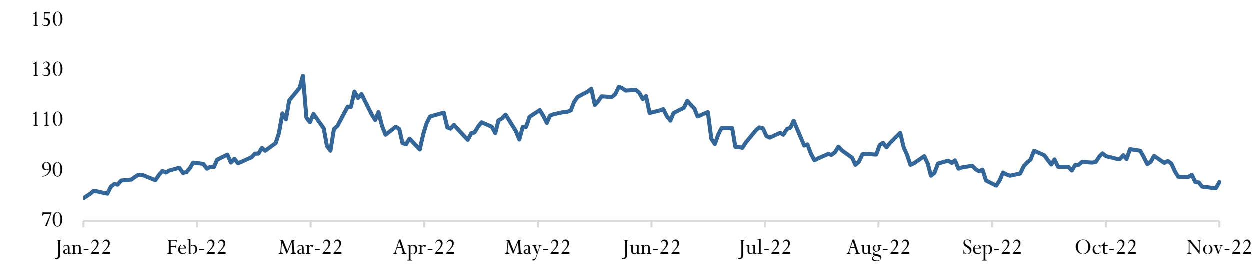
Has India de-coupled? To use the word de-coupling for India has been nothing short of blasphemous. The refrain is that we have been here in the past. It is a matter of time before this optimism blows up in our face. Therefore, hold your horses. Indian economy will somehow skid on its tracks so that we join the slow and not so steady.

Other than the self-defeating mantra that India is never as good as it looks, there is no logic to this argument. The D-word itself is the perfect way to befuddle the debate and miss the key point. No nation can de-couple and the debate should end there. **That said, India need not de-couple in order to deliver on its potential**. There are several tailwinds for India and India can achieve a consistent growth of 6-7% in the next several years with a possible upward bias as and when the global economy stabilises. That outcome is nothing to scoff at. India is well-positioned in a world hungry for growth drivers.

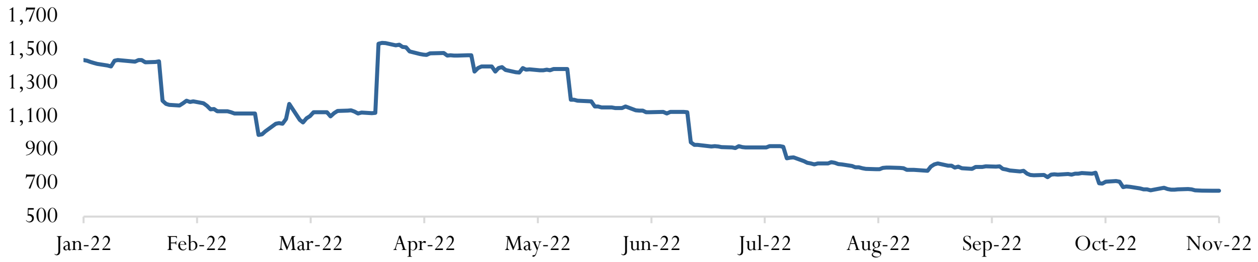
Lower global growth = Lower commodity prices = Advantage India

The world suffered a major energy shock earlier this year when Russia attacked Ukraine. Back in the 1970s, a conflict in the middle east rendered a body blow to global growth which took years to mend. Look at how various commodities have reacted to the supply shock during the current episode.

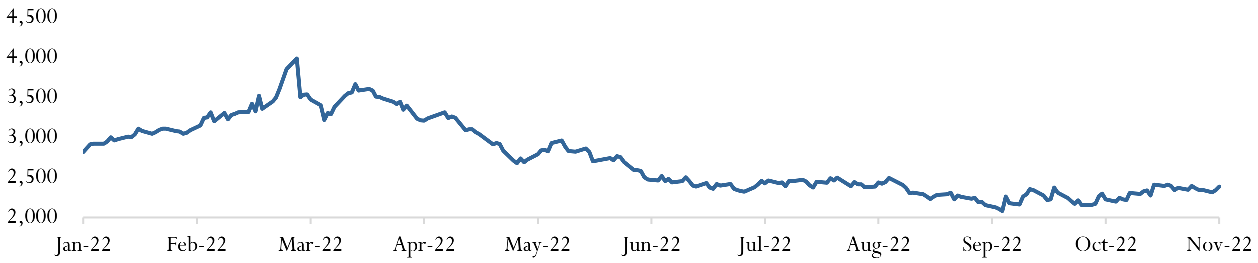
Brent Crude (USD/bbl)



US HRC Steel (USD/ton)



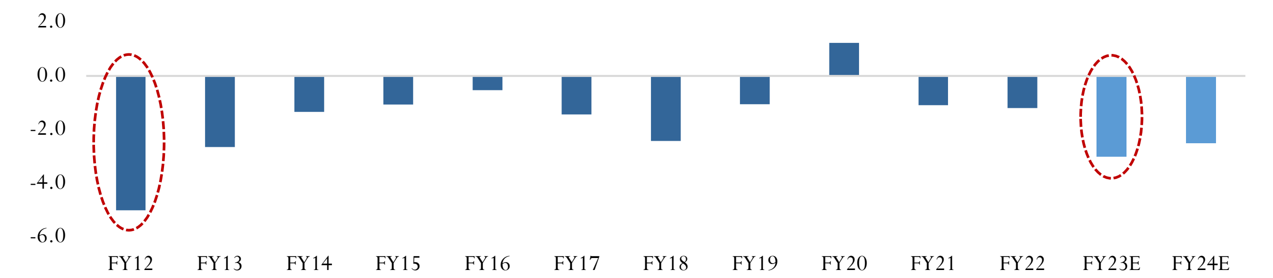
LME Aluminum (USD/ton)



Source: Bloomberg, Spark Fund Research

It is not out of place to mention that an analyst from a leading global investment bank predicted oil price to go as high as US$ 450. The rather unexciting outlook for China and the reduced dependency that the US has to import energy has resulted in crude oil going south instead. India is one of the biggest beneficiaries in this emerging situation. Look at the BOP position for India

Current account as % of GDP

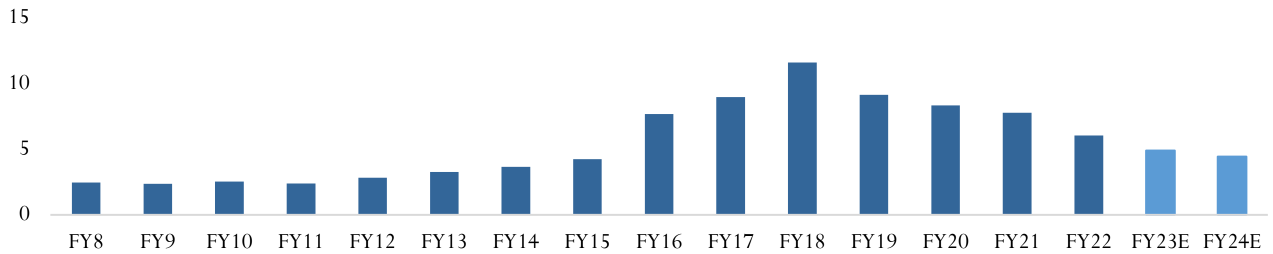


Source: GOI, RBI, World Bank, Spark Fund Research

It is clear that India has managed this crisis better than in the past.

Banking system is not under stress

Banking System - GNPA (%)



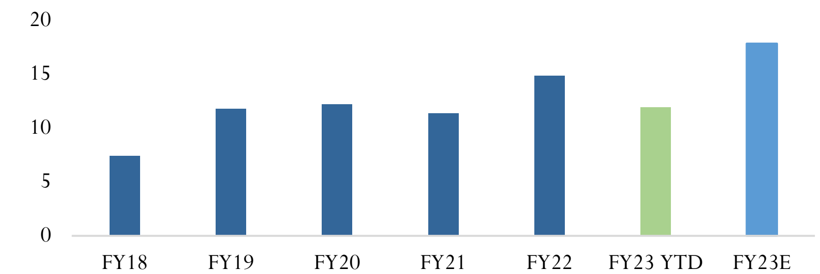
Source: RBI, Ace Equity, Spark Fund Research

Credit conditions are favourably placed for India despite rising rates and worsening global stress. We have made this point that economies coming out of recession often come out in great shape shedding excess flab. The fact that the Indian government did not resort to reckless pump-priming during the Covid crisis has contributed to a healthy recovery. The Indian financial system is well placed to finance a growth cycle and an incipient recovery in a moribund capex cycle.

Tax reforms are bearing fruit

When GST was introduced, it was envisaged that the economy will see the benefits with a lag. This has played out to perfection.

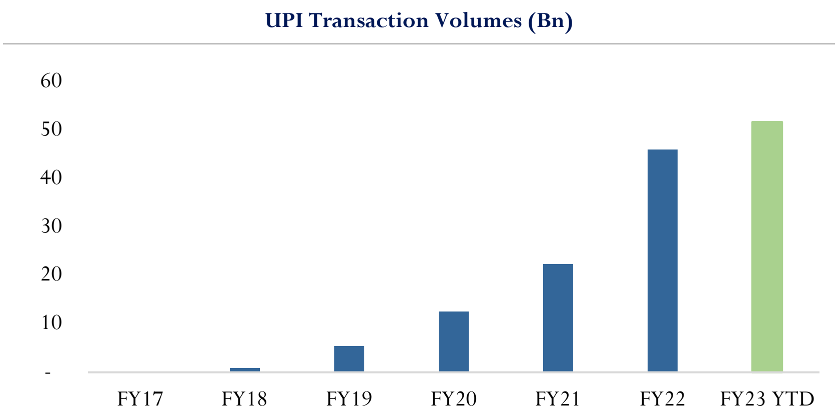
GST Collection (INR Tn)



Note: FY23 YTD is till 30th Nov 2022
Source: GST Council, Spark Fund Research

The direct tax collections have also been ahead of estimates and this means the fiscal deficit will be well contained below projections (though not at very comfortable levels on an absolute scale). India's deficit is funded largely from domestic savings and that helps in a world where capital is being sucked out.

Digital India



Note: FY23 YTD is till 30th Nov 2022
Source: NPCI, Spark Fund Research

India has emerged as world leader in micro-payments. Further, the direct benefit transfer and other initiatives at e-governance have led to efficiency gains which are driving a positive change whose echo may reverberate for the next several years.

Resurgence of manufacturing

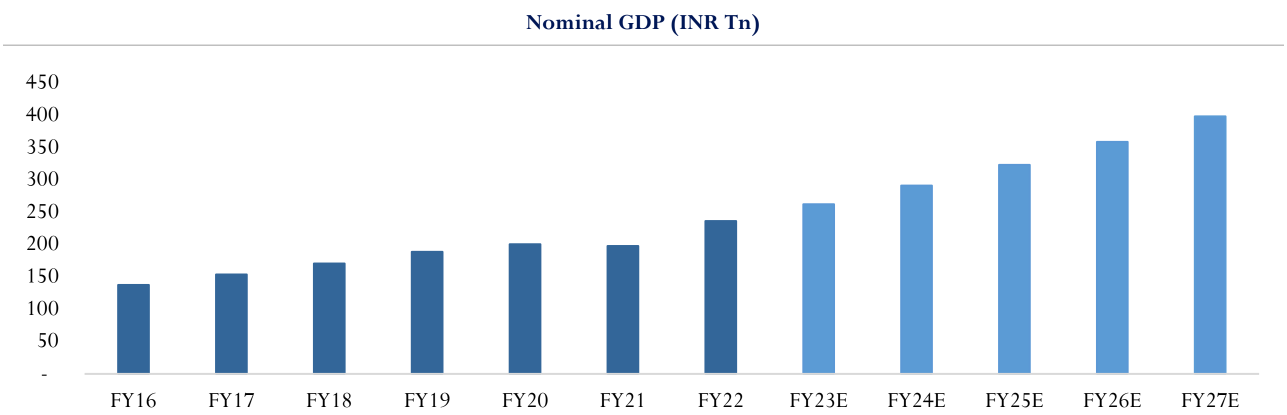
China's loss is India's gain. Indian manufacturing story may well turn out to be the biggest game changer for India in the next few years. Light manufacturing, chemicals, electronic goods, engineering, pharmaceuticals, automobiles, textiles…… the list is only expanding. Proximity to the large domestic market and increasing global competitiveness underpin a powerful theme which has not even started to play out. India may well repeat what it did in IT on the manufacturing front. Watch the space.

Is the GDP growth rate a matter of concern

Yes. It is

Slowing exports is the main culprit here. We have seen downgrades to FY23 estimates all the way from over 9% to a number which will possibly come in a bit less than 7%. The world at large has fared much worse. For FY24, expectations are getting anchored around 6-6.5% now. That may end up having an upward bias as we make our way forward.

Look at what a 6% GDP growth can do to nominal GDP over the next five years



Source: MOSPI, Spark Fund Research

India is on track to close in on US 5 trillion dollars of output and that will create opportunities in the market which are sizeable. We must look at prospects for the stock market from this perspective rather than from the prism of failed promises from yesteryears.

A parting thought on an expensive market

Indian valuations are high and there is no point in denying the obvious. And that is a risk. Caution is always in order when market rallies from such levels. That said, expensive markets are often that way for a reason. Japan and Taiwan remained expensive for long periods when they were uniquely positioned in the global context. Taiwan was the poster boy for tech and a China play. Japan was the original emerging market that rocked though for Nikkei, that did not end well. The point is that markets remain expensive for long periods in a certain context. India stands out with the promise of redemption of its demographic dividend and from a world looking to disengage from its China grip. India has emerged as the lone significant growth story in the context of capital hungry for alpha and beta. Which is possibly why we are at all-time highs on Sensex and Nifty. Curiously enough, no one seems to be happy let alone euphoric. There is all-around scepticism. The tone from pundits seems to suggest that they are even apologetic for the behaviour of the market. That actually bodes rather well for the overall health of the market in the medium term.

India's weight in emerging market indices has inched up to 15%. There is fear that capital will move out. Quite the contrary. Capital may look to flood the market. India's inability to absorb large doses of capital infusion may be the real handicap. No doubt there are many risks to this optimistic pitch for India. That is reflective of the times we live in. India will be presented with lots of opportunities to shoot itself in the leg. For a change, what if India declines to do so?

Warm regards,

P Krishnan (CIO) and Team Spark Fund