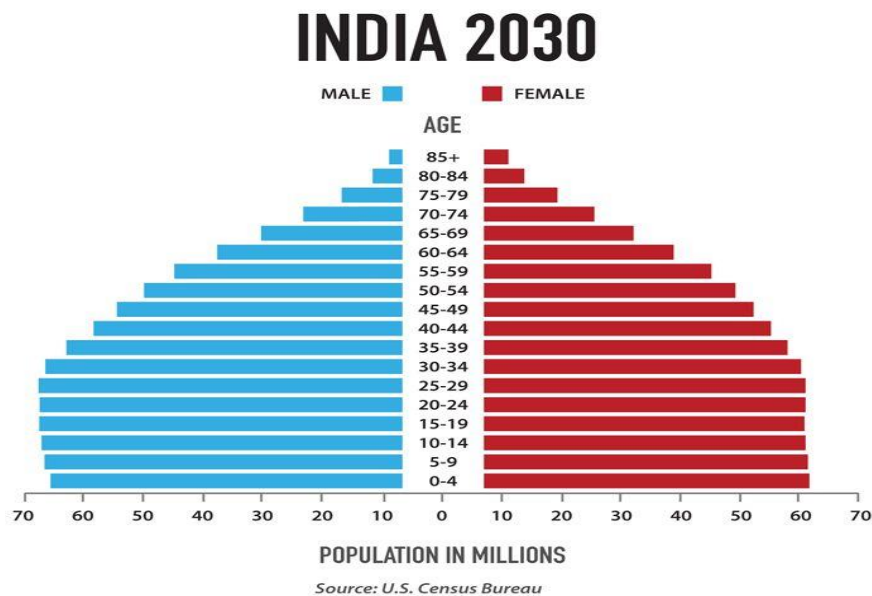
India Avenue
Investment Management



The Why, How, What and When of Investing in India

In this paper we reflect on some of our client discussions when engaging on investing in India. These discussions range from retail, high net worth to institutional clients. Commonly asked questions are:

1. Why should I even consider India as an investment option – it is not on the radar
2. Shouldn't I just leave it to my Global and EM portfolio managers
3. I assume with exposure to companies like Google, Apple, Amazon, Nestle etc., that I am getting exposure to countries like India?
4. How do I go about implementing exposure, if I were to consider it – wont an ETF do the job?
5. I am not sure when I should invest - wait for a market pullback as India seems expensive?
6. How much is appropriate?

In this paper we seek to provide answers to those questions. These answers are the reason we set up our fund four years ago and decided to focus on advice, knowledge and portfolio management for investors seeking India as a growth component in their portfolios.

Today, simple mathematics will tell you that India's GDP is targeted to be US$5tn by 2027, which will lead its market size to double from current levels if it maintains its market-cap-to-GDP ratio of 0.75. Several quality companies will benefit much more than the level of market growth.

Why do I need exposure to India?

India over the course of this decade will go close to being the world's third largest economy (behind the US and China). As a country, it has one of the best fundamentals globally through its significant, youthful and productive population. India is likely to take leadership in having one of the lowest dependency ratios globally.

With India undergoing significant structural changes through economic and financial reforms and significant financialisation (400m new bank accounts opened in the last 5 years) and digitialisation (1.2bn with a mobile phone, 700m internet users) occurring, it is inevitable that wealth will rise and the requirement for infrastructure and services will rise significantly locally – especially with 400m set to urbanise over the next few decades.

Additionally, as the rest of the worlds seeks to diversify its supply chain and reduce reliance of China's stranglehold on manufacturing, India will receive increased attention as a manufacturing location of choice. Its export base is also set to rise given existing scalability benefits and a structural low-cost labour advantage, coinciding with a young, employable population.

For Australian investors it makes a lot of sense given the low correlation to the Australian equity market and currency. Australia is a commodity exporter, whilst India will be a significant importer over time. India provides all the needs for an investor seeking growth and diversity benefits in their portfolio – in fact far better than an Emerging Market Fund (which includes Brazil, Russia, South Africa and a very high exposure to China of over 40%). Institutions are not going there because of business risk, career risk and being too big to be nimble. However, India presents an ideal investment for retail clients, high net worth investors, family offices and small institutional investors.

How do I get exposure to India?

An investor can seek to gain exposure to India via various instruments. We have outlined some of them below and presented a picture of what you get within each package.

Factors to Consider	Balanced Fund	Global ACWI	Emerging Market	Asia	India ETF	Indian Active Fund
Exposure to India	<1%	<3%	<20%	<30%	100%	100%
Underlying investments	Top 20 stocks	Top 10 stocks	Top 20 stocks	Top 50 stocks	Top 50 stocks	Top 500 stocks
Indian Sectors	Energy, Financials	Energy, Financials, Consumer	Energy, Financials, Consumer	Energy, Financials, Consumer Pharma	All	All
Capitalisation	Mega	Mega	Large	Large	Large	All Cap
Liquidity	Reasonable	High	Good	Good	Good	Good

Over time, the best outcome for investors has been via investing in actively managed funds when it comes to India. The track record of local investors has been significant relative to market cap weighted exposure to stocks. Additionally, an actively managed fund provides diversified exposure to all aspects of India – not just large, liquid and already wonderful in terms of market cap and valuation!

What type of exposure should I have?

Typically, what happens in funds with a specific benchmark i.e. MSCI ACWI, MSCI EM, MSCI Asia ex-Japan is a focus on aligning the active risk to the areas where the investment acumen lies. In most cases investment teams are organised into sectors and thus analysts and PM's choose across the best companies across in the world in their various sector groupings.

Additionally, liquidity is a big issue given the size of funds. This means they generally try to identify companies which play the India theme that are large and liquid. This generally means an Indian Bank like HDFC Bank or a conglomerate like Reliance Industries. Its unlikely that most will hold an Indian manufacturer, pharma or fast-growing mid cap company. Most technology exposure will be driven by China, Korea or Taiwan i.e. Alibaba, Tencent, Samsung, Taiwan Semiconductors.

It is our view that if you want a strategic long-term overweight position to India, the best way to achieve it is to have an India dedicated exposure, with your EM, Asia funds moving more tactically in and out of India based on views of everything else in their investment universe. A dedicated focus allows you to buy and hold companies from an early stage which is the true India thematic of growth and entrepreneurship.

For most investors an allocation to India should be focused on providing growth and diversity to the portfolio. The allocation no doubt sits in their equity portfolios as a growth play. Ideally the exposure to India should focus on a mix of structural compounding growth companies (existing success stories that have leading market share driven by significant barriers to entry thriving from a fast growing market.) and emerging businesses which are dominant in a segment which is growing faster than GDP growth.

Industries in which India should be more dominant globally include Pharmaceuticals, Auto/Ancillaries, Engineering and Manufacturing, Additionally, Consumption, Communications and Financials will continue to benefit from the local demographics – unique and distinct to the rest of the world.

Can't I just buy US stocks with Indian exposure?

The common thought process of getting exposure to India's demographics and growth story via companies listed overseas with perceived better governance and transparency can be a bit of a myth as its debateable whether global companies like Facebook, Amazon, Walmart etc. will provide the same exposure. Companies like Hindustan Unilever and Nestle India (the local businesses of the global business) have provided a much more direct and rewarding play on the Indian consumer, than getting diluted exposure through the group company. Both divisions of Unilever and Nestle in India have become their most profitable regions globally – why dilute this?

This method also does not necessarily provide exposure to some of India's growth thematics:

- India's pivot to manufacturing
- Financialisation of local savings
- Value-added exports (pharmaceuticals, engineering)
- Local consumption trends

When should I Invest?

This is a common question for investors. However, timing is fraught with danger as it is usually induced by fear of missing out when markets are moving upwards and fear of capital loss when markets are moving down. When investing in a regional market with a niche positioning, this risk can be accentuated by the following factors:

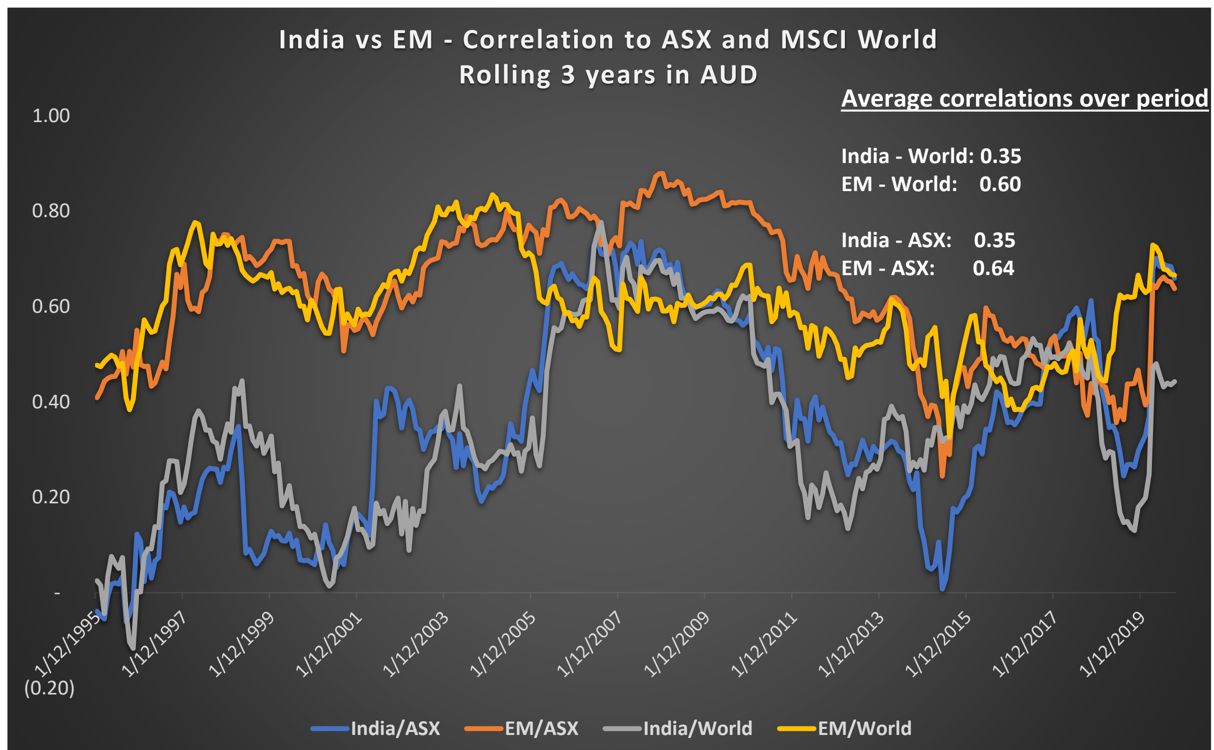
- Lack of information and insight leading to a focus on price
- Career and business risk for individuals and groups seeking to differentiate from consensus if the trade goes wrong
- Perceived heightened political and currency related risks of investing in emerging and frontier markets

We advocate a dollar cost averaging approach when investing in markets like India to take away concerns of timing, valuation and volatility. Too often investors invest at peaks and sell out at low points and then blame the underlying investment thesis rather than their behavioural aspects.

A portfolio approach to investing in Indian equities

Another common mistake we make is isolating each investment we make as a line item when looking at our overall investment portfolio. However, simplistically with adequate diversification comes the potential that some investments must be down whilst some are up.

Part of the attraction of having a slice of India in the portfolio is the diversity benefits it brings. For Australian investors, the low correlation of India's equity and currency markets offers some portfolio benefits. In fact, allocating to India is more additive to a Balanced portfolio than is allocating to Emerging Markets – that may be hard to believe, but is the case for an Australian domiciled investor.



In most cases India as a niche investment leads to a 3% position in client portfolios depending on their risk profile and investment horizon. There is no science to that – its more a function of the size of a satellite investment that may not be significant now but could have the potential to be.

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A futurist's outlook

- ✓ To become the 3rd largest economy in the world behind USA and China
- ✓ India will become a manufacturing option for the world and an alternative to China. Manufacturing to move towards 25% of GDP, allowing employment/productivity gains
- ✓ By 2030 India will have a low dependency ratio. In fact, far lower than China's
- ✓ GDP-per-capita is set to rise as experienced by China in the last 30 years.
- ✓ Reforms will improve livelihoods and will lead to efficiency and productivity gains
- ✓ Massive financialisation of savings will occur in India leading to gains for the equity markets
- ✓ Entrepreneurial and tech capabilities allow for unicorns to emerge given scale
- ✓ GDP to reach US$5tn, corporate profitability to rise from a low point and further investment to occur (financialisation of savings) leading to the tailwinds for equity market gains

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