The Indian Economy – A Story of Sustainable Growth

Why India?

India is one of the world's strongest economic growth opportunities. Growth in consumption, a structural upswing in investment and a huge demographic advantage has seen gross domestic product (GDP) grow by on average 7% per annum for the last decade. Many commentators are forecasting India's rate of growth to surpass that of China in the coming decade.

Complementary to Australian portfolios

Indian equities could work as a complement for Australian investor's existing portfolios. Australia's share market (and indeed Australia's economy) is heavily dependent on the performance of the mining sector, which in turn is dependent on economic growth in China. One could argue that Australian investors holding stocks such as BHP Billiton, Rio Tinto and Fortescue, get indirect exposure to the China growth story.

India on the other hand, is quite resource rich itself, particularly in terms of iron ore, thermal coal and natural gas. It is self-sufficient when it comes to the latter two resources and from time to time, will also export iron ore to China. In other words, investing in Australia's mining stocks does not provide exposure to the growing Indian economy to the extent that it has done to the Chinese economy.

The Indian economy performs better when commodities prices are declining, whereas the Australian economy does the opposite. The huge infrastructure spend that is currently taking place in India demands significant quantities of steel and concrete. Car and motorcycle manufacturers are growing sales volumes rapidly, while energy requirements are doubling every five years or so, all of which requires oil and other natural resources. As we have seen over the last year, commodity prices in general have started trending lower (iron ore prices for instance are now around the USD147/tonne mark, as opposed to over USD170/tonne for much of 2011), which could benefit the Indian economy and many Indian companies. Many are forecasting this trend to continue given the number of mining projects that are expected to come on-stream in the coming years, which could put further downward pressure on commodities prices. The current Australian government's mineral resources tax and carbon tax, combined with the strong Australian Dollar also pose headwinds for Australia's resources sector and wider economy.

Indian Economy

India's economy is at a very early stage of development and unlike many other Asian economies, it is a services driven economy, with almost 56% of its GDP sourced from the services sector. A good means of getting access to this part of the Indian economy is investing in Indian equities. As the wealth effect begins to play its part in India, more and more people will start demanding basic services that Australians have had access to for decades, such as opening bank accounts, taking out insurance policies and obtaining medical and health services, will all become part of day-to-day life in India. There is a huge opportunity to provide such services given the population of 1.2 billion.

Long Term Story: Strength in Numbers

Besides the growing population (see Figure 1), the ratio of workers to dependents is expected to continue to improve over the next two decades, while for much of the Western world it is expected to decline. At India's last census, literacy ratios had improved from 65% to 74% over the decade to 2011. If this trend were to continue, then it can be expected that India's labour force quality will improve as well.

Figure 1: Continued Population Growth (millions added to population per annum, Source: IMF)

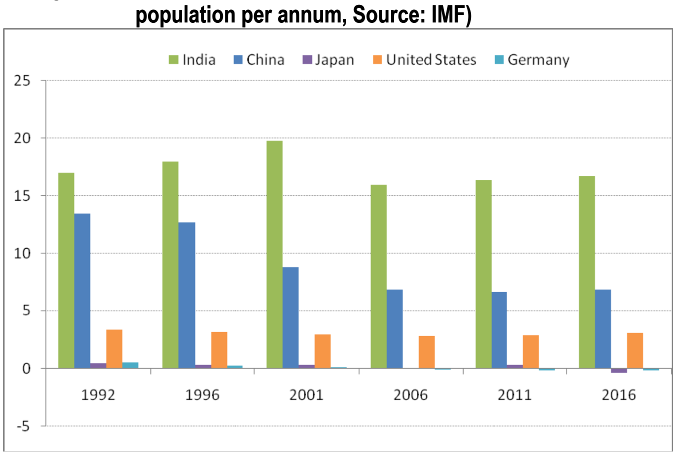
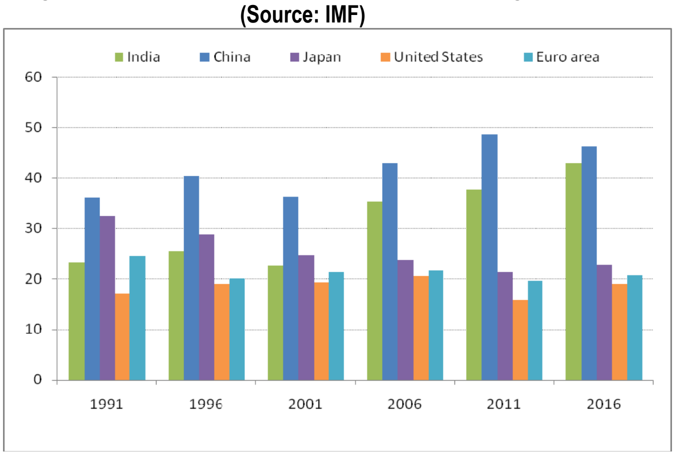


Figure 2: Investment as % of GDP - India approaching China (Source: IMF)



Long Term Story: Investment Growth

India's investment as a percentage of GDP growth has steadily improved since the turn of the century, and the IMF is forecasting that this growth is expected to continue (see Figure 2). Increased investment in infrastructure could lead to improving industrial productivity, which could see India's manufacturers become more competitive with their international counterparts. The IMF is forecasting that the gap between China and India will continue to narrow.

Long Term Story: Domestic Consumption

Domestic consumption contributes almost 70% towards India's GDP, while investment expenditure contributes approximately 38% (estimates for the 2010/11 financial year; Source: Reserve Bank of India, Sept 2011). India is in fact a net importer, which means that India's net exports (exports minus imports) make a negative contribution to GDP (contributing approximately -7% to GDP). Among the Asian economies, India is one of the least dependent on exports, with exports contributing less than 23% to India's GDP. As a result, the economic slow-down in Europe is not expected to have a significant impact on the Indian economy.

How has the Indian share market performed relative to other parts of the world?

The Indian share market has performed remarkably well in the last 10 years. Rolling returns for the Indian share market, the Fiducian India Fund and various other indexes all in Australian Dollar terms are as follows:

Table 1: Returns to end March 2012 (net of fees)

	3 months	6 months	1 Year	3 Years (p.a.)	5 Years (p.a.)	10 Years (p.a.)
Fiducian India Fund	18.4%	-4.0%	-14.4%	6.7%		
BSE 100 (AUD)	17.4%	-5.3%	-22.2%	6.8%	-1.9%	**9.6%**
ASX 300 Acc	8.6%	10.8%	-6.3%	11.4%	-2.1%	6.9%
Hang Seng (AUD)	8.6%	8.4%	-13.3%	0.2%	-3.7%	-0.3%
S&P 500 (AUD)	10.3%	16.1%	5.3%	16.8%	-5.6%	-5.0%
MSCI World ex Aust (AUD	10.5%	12.7%	0.7%	5.1%	-5.6%	-2.2%

Source: Iress Market Technology

The Fiducian India Fund is a great tool for investors who apply a satellite approach of investing in specific high growth economies such as India or China to actively diversify existing broad based international or emerging markets exposure. Note that all investments have risk. A good first step is to contact your Financial Adviser.