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WEALTH MANAGEMENT

Editor's pick: Is India the new China?

September 26, 2023



Indian consumers are the largest collectors of gold worldwide. Image credit: Shutterstock

By STAFF REPORTS

Here is an interesting point of view on how India looks set to overtake China as a promising investment alternative. Several factors play into this assumption: India's new rank as the world's most populous country with digitally savvy youth, rising middle class, developing infrastructure, export focus and diversified economy.

Simon Hobbs, a Palm Springs, California-based independent financial advisor affiliated with California Financial Partners Inc., could not have articulated India's challenge to China more cogently. Here is his take:

India has emerged as a compelling economic growth story and an increasingly attractive alternative to China within the emerging markets complex.

A growing population with a robust and young workforce, significant infrastructure spending and an ongoing digital transformation have been key catalysts to India's outperformance over China.

India has also benefited from the de-globalization trend as manufacturers move production away from China.

While we may not go as far as officially calling India the new China, the economic and technical trends suggest the country may be set for a prolonged period of outperformance.

Growing population and robust workforce

An impressive growth story has propelled India into a major powerhouse across the global economic landscape.

Over the last two decades, the country has made impressive strides in reshaping its economy by leveraging its growing population and improving its outdated infrastructure.

At the core of the growth story is the largest consumer base in the world based on its population size of nearly 1.5 billion people, according to United Nations (UN) estimates. This places India as the most populous country in the world, overtaking China for the first time since the data series started in 1950.

Of course, poverty remains a key issue among the Indian population, but significant progress has been made since 2005.

According to UN data, the number of people living in multidimensional poverty based on monetary poverty, education and basic infrastructure services fell to 16.4% of India's population in 2021 from 55% in 2005.

While the sheer population of India is impressive, the growth rate and age of its working population stands out, especially when compared to China.

For example, over the last 20 years, India's population has jumped 36 percent, widely outpacing China's population growth of only 8 percent during this timeframe.

Perhaps more importantly, the UN reported that more than 40 percent of the population is younger than 25, while the estimated median age in India is 28, marking nearly a decade younger population base than China's.

The data also shows adults aged 65 and older only comprise 7 percent of India's population, compared with 14 percent in China.

In comparison, the percentage of China's working-age population is expected to peak over the coming years.

From an economic standpoint, India has a robust, young and sustainable working-age population to support future growth. Real wages are also rising rapidly.

According to ECA International's Annual Salary Trends Report, real wages in India are expected to climb 4.6 percent this year, marking the highest salary growth rate in the Asia-Pacific region.

India gaining investor attention

India's growth story continues to gain investor attention.

Attractive earnings, GDP growth and the economy's relatively successful recovery from the COVID-19 pandemic have attracted steady inflows into Indian equities.

As shown in Figure 1, the MSCI India Index has recently broken out from a two-year consolidation range after rallying over 20 percent since March.

The breakout was supported by bullish momentum and broad participation, suggesting more upside likely lies ahead.

The lower panel of the chart compares the MSCI India Index to the MSCI China Index.

A rising ratio chart indicates India's outperformance over China, and vice versa for a declining ratio chart.

As you will notice, India has been outperforming China since December 2020, and based on the steady string of higher highs and higher lows and the ratio chart holding above its rising 40-week moving average, we expect the trend of India's outperformance to continue.



India is breaking out and outperforming. Source: LPL Research, Bloomberg

Inflows return

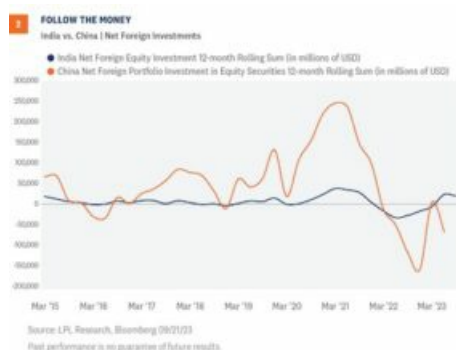
Inflows from abroad have contributed to India's outperformance over China.

As shown in Figure 2, India recorded \$18.9 billion of net inflows from foreign equity funds over the last 12 months

as of Sept. 21.

The pace of inflows from foreign equity investments has also been climbing steadily since March 2022.

In stark contrast, years of steady inflows into China have turned mostly negative over the last year as the country deals with deteriorating economic conditions and elevated geopolitical tensions.



Follow the money: India vs. China, net foreign investments. Source: LPL Research, Bloomberg

Growth engines

While a growing population of nearly 1.5 billion people makes a compelling growth story, India has several other drivers of growth.

The country carved out around \$120 billion for infrastructure spending on improving railways and roads in its budget for this fiscal year, marking a 37 percent increase over the previous year and more than double the budget allocation in 2019.

In total, India's government has amassed an infrastructure pipeline from 2019 to 2025 of nearly \$2 trillion.

Progress is being made as the country has now doubled its national highway system to 90,000 miles over the last decade and added more electrified rail than the United Kingdom or France, according to an Organization for Economic Cooperation and Development report.

More recently, at the G20 summit in New Delhi, global leaders, including U.S. President Joe Biden, announced a memorandum of understanding on the India-Middle East-Europe Economic Corridor, or IMEC.

The IMEC corridor, a counter to China's Belt and Road initiative, is "expected to stimulate economic development through enhanced connectivity and economic integration between Asia, the Arabian Gulf and Europe," according to the White House.

In addition to infrastructure upgrades, India has undergone a digital transformation over the last several years.

India has nearly 900 million Internet subscribers, second to China's 1.1 billion.

India's development of its digital public infrastructure program, which provides an identity and payment interface, has helped significantly drive its digital economy.

Growing domestic consumption, rising real wages, increased infrastructure spending and the continued digital transformation in India have driven GDP growth estimates over the next few years to 7-8 percent.

As shown in Figure 3, India has surpassed China in terms of GDP growth, a trend that is forecasted to continue over the next several years.



A new growth story: India vs. China, GDP comparisons

Another factor behind India's growth has been its increased popularity as a supply source alternative to China, making it a more export-driven country that is less reliant on domestic consumption.

The rise of de-globalization following the pandemic and escalating trade tensions between the U.S. and China have made India a near-shoring beneficiary.

As shown in Figure 4, India's exports as a percentage of GDP have climbed to 22.4 percent, now outpacing China's exports as a percentage of GDP rate of 20.7 percent.



Source: LPL Research, Bloomberg 09/21/23
Past performance is no guarantee of future results.

Near-shoring tailwinds boosting Indian exports: India vs. China, exports as a percentage of GDP. Source: LPL Research, Bloomberg

Investment conclusion

While LPL's Strategic and Tactical Asset Allocation Committee (STAAC) maintains an underweight recommendation for emerging markets (EM), India has become an increasingly attractive alternative to China within the EM space.

The technical setup for India has turned bullish as capital from foreign investors continues to flow into the country.

A growing population, rising domestic consumption due to an improving middle class, significant infrastructure spending, a digital transformation and increasing exports have transformed India into a growth story that many investors believe could be the next China.

LPL Research is also comfortable with Latin American equities within EM.

The STAAC still slightly favors developed international equities over the U.S. on the upbeat outlook in Japan, while maintaining an underweight recommendation for emerging markets (EM).

More broadly, the STAAC recommends a neutral tactical allocation to equities, with a modest overweight to fixed income funded from cash.

The risk-reward trade-off between stocks and bonds looks relatively balanced to us, with core bonds providing a yield advantage over cash.

Within equities, the STAAC recommends being neutral on style, favors large caps over small, and suggests overweight allocations to the energy and industrials sectors, where appropriate.

Within fixed income, the STAAC recommends an up-in-quality approach with benchmark-level interest rate sensitivity.

Core bond sectors (U.S. Treasuries, agency mortgage-backed securities and short-maturity investment grade corporates) are currently more attractive than plus sectors (high-yield bonds and non-U.S. sectors), with the exception of preferred securities, which look attractive after having sold off due to stresses in the banking system.



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