February 2015 – Ocean Dial Investor Trip to India

Highlights from our recent investor trip are below; however the main takeaway from the week is that the Government is making deep rooted changes to the way India operates. Whilst the journey will be a bumpy one, the trip reinforced our confidence that the economy is set to undergo a structural recovery and the long term outlook for the country is positive.

State of the Economy

- Demand is yet to recover - support prices capped and social spending halted, wage growth outside the organised labour market (80% of the workforce) is stagnant. Retail lending is starting to improve but corporate lending remains a concern
- An economic revival must be driven by infrastructure investment to prevent inflation - private sector still cleansing itself through the sale of assets to clear excess capacity and mend broken balance sheets. The Government has allocated substantial funding to capex to provide the initial catalyst*
- The consensus was that the Government's start has been positive but the economy is still on the mend and it will take time for reforms to gain traction

The Positives

- **Sentiment** from corporates has recovered due to a seesaw shift in attitude at all levels of the Administration
- **Macroeconomic sweet spot** – improved current account deficit, inflation, fiscal discipline, global commodity prices, a turning interest rate cycle
- **Strong Government** - Modi has tapped into a growing younger, aspirational vote bank that prioritises social mobility over subsidies. Delivering on their ambitions is essential to fulfilling his political legacy
- **Competitive federalism** - the Centre has empowered the States with greater discretionary spending. Clear evidence of traditionally "business hostile" States jostling for inward investment
- **Technology** - shift of Government processes online is increasing efficiency, accountability and transparency by reducing scope for human interaction

What to watch out for

- BJP's minority position in the Upper House has led to contentious legislation being blocked. A joint sitting of the two House expected this year to pass key bills reforming land, insurance and coal mining
- Approval and implementation of GST - Estimated reduction of tax burden on production from 30% to 20%, minimises opportunities for extortion from revenue collectors, creation of a true common market with the free flow of goods between States. Once passed, the issue will be execution risk in terms of IT infrastructure
- Execution of Government capex spending. The time taken from choosing a project to action on the ground will determine the speed of recovery in investments

Long term changes to modernise India

- **Financial intermediation** - savings rate down from 38% to 30%. Needs to recover and be channelled into the financial system to provide future funding for growth. Positive real rates, 125m new bank accounts since September and the monetisation of gold savings is a good start
- **Infrastructure** - corporates eventually need to be able to pass on higher costs to the consumer. The recent re-auction of coal mines is the first time resources have been allocated in a transparent manner
- **Corruption** - now at the forefront of the political discourse. Improvements at the top of Government through use of technology are encouraging but it will take time for this to filter down the system

*Click here for a link to out recent note on the Government's 2015 budget

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