
INDIA'S GROWTH MAY BE THE STRONGEST OF ALL LARGE ECONOMIES OVER THE NEXT 10 YEARS

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Frequently, we tend to hear about the unfavourable demographic shifts occurring within developed markets. Japan is one of the world's "oldest" societies, and both the US and Europe have large numbers of soon-to-be retirees planning to leave the workforce in coming years.

If there are challenges associated with large numbers of people retiring, one logical question to ask is whether there are countries on the opposite side of this trend, with younger populations that are poised to enter the workforce in the near future.

These countries certainly do exist, and in our view, it's India that represents one of the best overall demographic opportunities when looking at the global economy today.

India is a long-term opportunity

Yet, one of the most important things to understand about India, is that it is a long-term opportunity. Performance over the next three, six or 12 months, or over the 2018 year for those who prefer to think in calendar years, could be quite volatile, with strong moves up or down. Those that will have the greatest appreciation for India as an investment will tend to have a portion of their assets in longer time horizon ideas, looking up to 10 years into the future.

Quantifying the long-term potential for India¹:

The investment case for India is compelling. Nominal gross domestic product (GDP) may grow at double-digit rates for the 10-year period to 2027. On a per-capita basis, India's citizens could see growth rise from \$1,702 to \$4,135 - a strong increase that would significantly boost internal consumption demand.

In 2014, India's government launched an initiative to provide a bank account for every household and over the last three years, approximately 285 million bank accounts have been opened. Furthermore, a project that has been underway for the last seven years has led to 1.2 billion Indian citizens becoming identifiable with either finger prints or retinal scans. Going forward, this could facilitate biometrically-driven payment systems, as well as the creation of individualized consumer profiles to help firms better understand their customers.

It is estimated that India already has 800 million mobile users—a number only slightly

below the total population of the United States and the European Union combined². Approximately one-third of these users are on the internet, and it is estimated that within 10 years, India may have more than 900 million unique internet users.

India's equity market capitalization, driven by both earnings growth as well as price multiple expansion, may also grow at double-digit rates over the next 10-year period. Note that this would be on average - we wouldn't expect double-digit market capitalization growth each year.

India's equity experience

One of the most challenging aspects of India as an investment allocation relates to the connection of these impressive numbers and strong growth prospects to the country's actual investment returns. As a market, relative to the broader MSCI Emerging Markets Index, India certainly hasn't always outperformed. Instead, it has had cycles of both outperformance and underperformance.

Measuring the cyclicity of India's relative performance against the MSCI Emerging Markets Index (31 Dec. 1998 to 13 Apr. 2018)



Source: Bloomberg. You cannot invest directly in an Index. The ratio of cumulative returns is calculated (MSCI India Index / MSCI Emerging Markets Index); therefore rising trends mean India is outperforming. The MSCI Emerging Markets Index began live calculation on 1 Jan. 2001, so prior returns represent backtested history.

Past performance is not indicative of future results.

Downward arrows in the chart above show periods in which India has underperformed the broader MSCI Emerging Markets Index. Since 1999, there have been three such periods. The first, from 21 February 2000 to 23 May 2002, was largely related to the bursting of the tech bubble in the late 1990s. The MSCI India Index lost 34.2% per year, while the MSCI Emerging Markets Index lost 13.6% per year. The second period was from 16 January 2008 to 3 September 2013, where the MSCI India Index lost 24.9% per year but the MSCI Emerging Markets Index lost 1.2% per year. The last period was slightly different, as returns were positive. From 11 Jan. 2016 to 19 March 2018, the MSCI India Index rose 14.16% per year, however, the MSCI Emerging Markets Index increased 29% per year.

Upward arrows show the periods in which India outperformed the broader MSCI Emerging Markets Index. From 23 May 2002 to 16 January 2008, the MSCI India Index returned 46% per year, while the MSCI Emerging Markets Index returned 26.1% per year. From 3

September 2013 to 11 January 2016, the MSCI India Index returned 15% per year, while the MSCI Emerging Markets Index fell 8.2% per year.

Using factors to construct a better equity investment within India

What’s clear here is that investing in India’s equity market in the past has been volatile, and that there have been sweeping trends in which Indian equities have both outperformed and underperformed the broader emerging market equity universe.

Of late, discussions of equity factor premia have become more prevalent, so how could this relate to India?

India: Factor Index Returns & Performance Relative to the MSCI India Index

Index	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	YTD 2018	Full Period
WisdomTree India Quality Index	25.95%	31.73%	80.45%	61.42%	101.51%	22.63%	-29.50%	21.07%	3.78%	32.56%	-2.83%	-2.37%	35.65%	-5.98%	10.16%
MSCI India Momentum Index	40.78%	49.99%	121.35%	69.60%	77.68%	28.45%	-32.50%	27.85%	-1.66%	18.78%	-6.29%	-2.56%	59.07%	-11.79%	11.41%
MSCI India Small Cap Index	47.24%	31.88%	95.90%	72.51%	125.94%	20.18%	-48.16%	36.31%	-14.18%	56.91%	2.39%	0.31%	66.99%	-12.13%	11.16%
MSCI India Value Index	38.32%	61.90%	90.04%	69.89%	105.08%	19.10%	-41.51%	23.92%	-9.88%	22.18%	7.75%	0.92%	39.23%	-7.50%	10.46%
MSCI India Index	37.57%	61.00%	73.11%	64.63%	102.81%	20.95%	-37.17%	25.97%	-3.83%	23.87%	-6.12%	-1.43%	38.75%	-6.95%	9.95%
Excess Returns vs. MSCI India Index															
WisdomTree India Quality Index	-11.62%	-19.28%	-12.68%	3.21%	-1.30%	1.67%	7.67%	-4.50%	7.61%	8.69%	3.30%	0.94%	-3.11%	0.97%	0.21%
MSCI India Momentum Index	3.21%	-1.01%	48.24%	-4.97%	25.12%	7.90%	4.66%	1.88%	2.17%	-5.09%	-0.18%	-1.13%	20.32%	-4.84%	1.47%
MSCI India Small Cap Index	9.67%	-19.33%	22.79%	-7.89%	23.14%	-0.77%	-10.99%	10.34%	-10.35%	33.04%	8.51%	1.74%	28.23%	-5.17%	1.22%
MSCI India Value Index	0.75%	0.89%	16.93%	4.74%	2.27%	-1.85%	-4.34%	-2.05%	-5.85%	-1.71%	-1.63%	2.35%	0.49%	0.85%	0.52%

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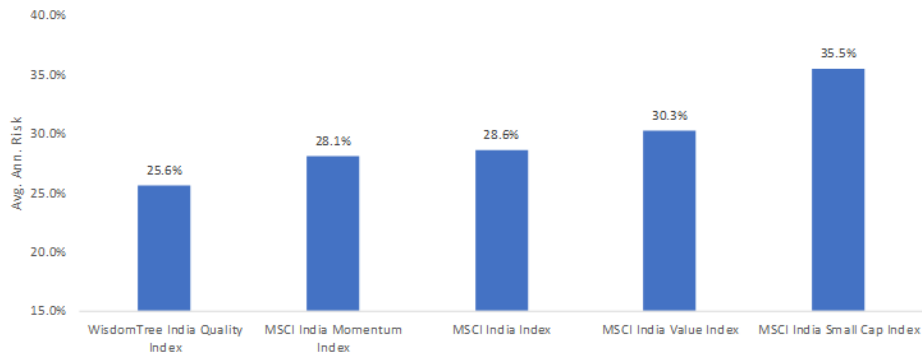
Sources: MSCI & Bloomberg, with period from 31 Dec. 2004 selected to indicate the maximum number of calendar years to illustrate. Analysis includes backtested returns. Indexes began live calculation on the following dates: WisdomTree India Quality Index: 1 Dec. 2016; MSCI India Momentum Index: 11 Dec. 2013; MSCI India Small Cap Index: 1 Jun. 2007. If an index is not mentioned, it does not contain backtested history in this analysis.

Past performance is not indicative of future results. You cannot invest directly in an Index.

It is always interesting to see returns of factor-focused indexes on a calendar-year basis because it reminds us that no factor is likely to outperform in every period, but that most factors have generated long-term outperformance. India’s case is no different, as the four factor-focused indexes shown above did, in fact, outperform the MSCI India Index over this full period.

It’s also worth considering the returns of the factor-focused indexes relative to the MSCI India Index. The WisdomTree India Quality Index generated its strongest excess returns, at least relative to the other indexes, during periods in which India’s market faced challenges and experienced negative returns. This is congruent with the results of other research we have carried out, and indicates that while “quality” may not outperform a market benchmark on the upside, it’s the capability to decline less in a downturn that often leads to strong results over a longer cycle.

Average Annual Risk of Indian Indexes



Sources: MSCI & Bloomberg, with period from 31 Dec. 2004 selected to indicate the maximum number of calendar years to illustrate. Analysis includes backtested returns. Indexes began live calculation on the following dates: WisdomTree India Quality Index: 1 Dec. 2016; MSCI India Momentum Index: 11 Dec. 2013; MSCI India Small Cap Index: 1 Jun. 2007. If an index is not mentioned, it does not contain backtested history in this analysis.

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Some may have looked at our factor data and concluded that India’s small caps offer the most potential. We think that, if the prognostications we mentioned earlier in this piece bear out and are at least close to accurate, India’s small caps may absolutely deliver strong returns going forward. However, the average annual volatility of the MSCI India Small Cap Index is approximately 10% higher than that of the WisdomTree India Quality Index, which leads us to believe that a “complete” allocation to India might involve pairing both quality and small-cap strategies.

Conclusion: Don’t forget about India over the next decade

Demographic trends may be one of the most fundamental drivers of global markets in coming years. For those looking to incorporate this theme into their asset allocation, we’d emphasize that India is an important market to consider.

1 “The Next India: India’s Digital Leap, the Multi-Trillion Dollar Opportunity.” [Morgan Stanley Research Bluepaper](#). 26 Sept. 2017.

2 Statistic for the European Union and U.S. population levels is the CIA World Factbook, with data based on July 2017 population estimates for each market.

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