India Perspectives

Turn bullish on India Equities

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- India's economic momentum is getting stronger. India's economic and earnings growth is one of the strongest in Asia for this and next year. Economic indicators like the PMI are showing a very strong recovery while GST collections reflect a robust consumer rebound.
- Manufacturing in India is picking up. India's high-skilled exports, mobile phones and services exports are showing strong signs of recovery. The renaissance of manufacturing is due to government reforms like the Performance Linked Incentive (PLI) scheme, and the diversification of the global supply chain. Due to digitalisation, the informal economy spending is accelerating. India banks' balance sheets are healthier as credit growth has picked up.
- We are now overweight on Indian equities due to the improving earnings outlook. Furthermore, global investors are starting to reallocate into India.

India's economic momentum picking up

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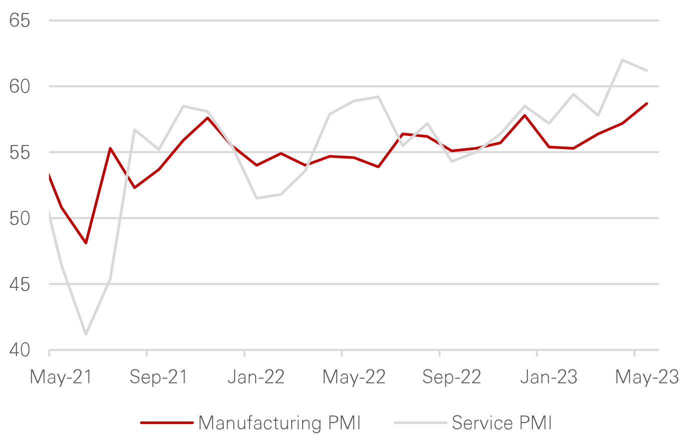
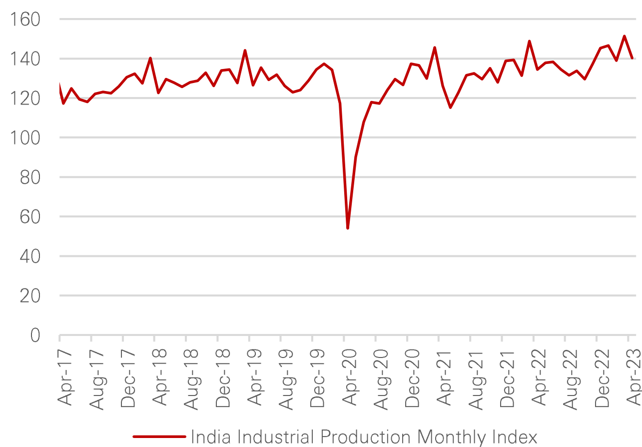
India PMIs



Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

India Industrial Production



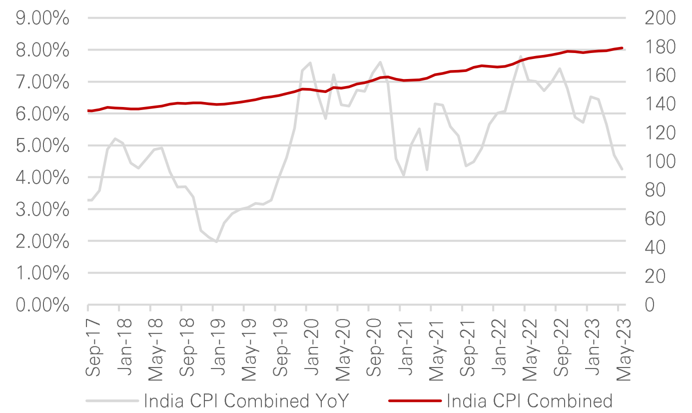
Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

Due to digitalisation, the informal economy spending is accelerating. India banks' balance sheets are healthier as credit growth has picked up.

Inflation stabilising

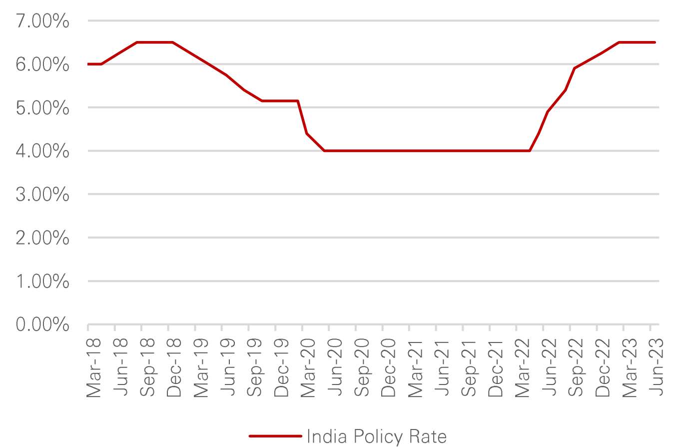
Headline CPI inflation declined to under 5% due to falling energy and food prices. Base effects also played a part. Encouragingly, core inflation is moderating as well. Core inflation is expected to stabilise. It will also be the third straight month that inflation remains within the RBI's target range. The Reserve Bank of India (RBI) is likely to pause policy for the rest of this year, and perhaps cut rates early-2024.

India Inflation



Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

India Policy Rate



Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

Bond market outlook

India's economy is on a firm footing, with high economic growth, declining inflation and a stable rupee. The recent move by the central government for fiscal consolidation is also supportive of the local bond market.

Internationally, with a weaker USD trend firmly in place, we expect the Indian Rupee to remain stable. All these factors together bode well for the Indian Local Currency (LC) government bonds. We are neutral on Indian LC debt.

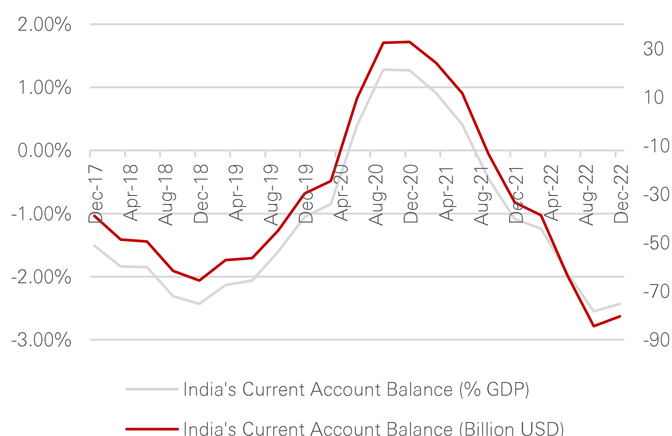
Overall, we have a neutral view on Indian HC bonds and LC bonds. The possible inclusion of India's bonds in JPMorgan's GBI-EM bond index sometime this year could be supportive of Indian bonds. Foreign interest in India's bond market should continue to grow strongly as India is one of the few markets with an attractive real rates carry.

Currency outlook

Fiscal consolidation will slow growth and lower India's current account deficit and improve the foreign reserves position. Import duty reduction will be supportive of the 'Make in India' theme, improving the prospects for high valued added tech exports and foreign direct investments.

INR is one of the few currencies with a yield that is higher than the USD. With an improving current account situation, and equity inflows, there could be more support for the INR

India Current Account



Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

In the near term, there could be some volatility for the INR. However, as the year progresses, the INR can recover someground. We think the USD-INR could end the year at 80.5.

USD/INR

Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

Equity outlook

We are now overweight on Indian equities due to the strong earnings outlook. Furthermore, global investors are starting to reallocate into India.

The most recent earnings results have been healthy, with more earnings beating expectations than misses. Consensus earnings is likely going to be robust in the months ahead. With inflation easing alongside a recovery in rural consumer demand, it is plausible for an earnings recovery in the months ahead. Therefore, the strong earnings trajectory will be the main driver for India markets.

India equity markets has one of the most profitable companies in the world with strong distribution channels that can tap on the rural population. As a result, such Indian companies have strong competitive advantage which generates superior margins. We like the India banks and IT companies. India's robust domestic demand, private investment and supportive policy provides solid earnings support.

India's equity valuation is now near its historical average. Compared to other Asia markets, India's valuation is higher because of the stronger return-on-equity and better margins.

Nifty 50 Price to forward earnings

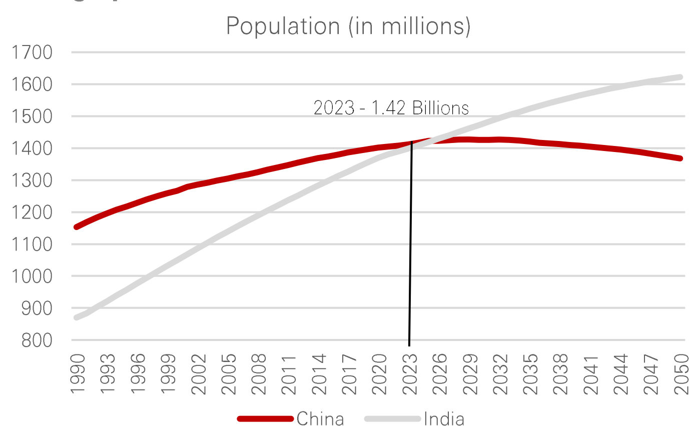
Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

India's structural growth opportunities – Rise of India TIGER

Due the unique characteristics of India's economy, an allocation to India can increase diversification for global investors. Indian equities have a lower correlation than other EM markets because of India's larger domestic economy. Moreover, its domestic companies are closely linked to its strong structural growth opportunities.

India has one of the strongest demographic dividends in the world. While most economies face an ageing population, India's working age population is projected to grow in the next decade. India's economy has elevated growth in the years ahead as the supply of labour increases.

Demographics: India vs China



Source: Bloomberg, HSBC Global Private Banking as at 30 June 2023.

For investors looking at India, the focus should turn to medium-term growth prospects. There are five themes that we think will drive India's growth potential in the years ahead. The themes are:

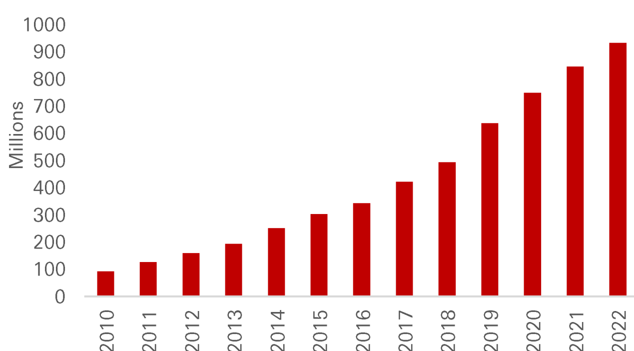
1) Technology - India's digital economy
2) Income - Rising income of the middle class
3) Green transformation
4) Energy infrastructure
5) Reforms in India

These five themes should serve as tailwinds for the India's growth dynamics over the medium term. They can also feed off each other to create a cycle that should generate more economic activity, and enable an upgrading of better infrastructure.

1) Technology - India's digital economy

The growth of a digital economy will permeate across the economy and boost productivity. The "Make in India" initiative encourages both foreign and domestic investment in the manufacturing sector; "Smart Cities" aims to eradicate urban squalor and "Digital India" targets an overhaul of government services with electronic identity, digital payments, and bank accounts. Additionally, the government has launched its Open Network for Digital Commerce (ONDC) in an attempt to deepen e-commerce penetration and foster innovation by start-ups with a special focus on small merchants and rural consumers.

Number of Internet users in India



Source: HSBC Global Private Banking, Statista as at 30 June 2023.

2) Income - Rising income of the middle class

In the next decade, Indian consumers are going to have more disposable income.
India's income distribution could flip over the next decade, and consequently overall consumption in the country could more than double to $4.9 trillion in the next decade.
Clearly, India has a rising middle class which will spend more of its transactions in the digital economy. India can become a $1 trillion digital economy in 5 years, unlocking its strength in digital innovation and cyber security. This young, digitally savvy, productive and growing work force provides a long runway for growth as the country propels forward.

3) Green transformation

India wants to reach net zero emissions by 2070 and to meet fifty percent of its electricity requirements from renewable energy sources by 2030. A transition to clean energy is a huge economic opportunity.

4) Energy infrastructure

Renewable electricity is growing at a faster rate in India than most countries, with new capacity additions on track to double in the next few years. A transition to clean energy is a huge economic opportunity. India is particularly well positioned to become a global leader in renewable batteries and green hydrogen. These and other low-carbon technologies could create a market worth up to $80 billion in India by 2030.

Globally, electric vehicles are expected to grow by 36% annually, reaching 245 million vehicles in 2030 – more than 30 times above today's level.

Coming from a low base, India is expected to see bigger exponential expansion. India has launched several initiatives to promote electric mobility, including the Faster Adoption and Manufacturing of Electric Vehicles (FAME) scheme, which provides subsidies to buyers of electric vehicles, and the National Electric Mobility Mission Plan (NEMMP), which aims to put millions of electric and hybrid vehicles on the roads.

Electric two and three-wheelers will represent the lion's share of the total electric vehicle fleet in India, as this category is most suited to rapid transition to electrification.

5) Reforms in India

With the "Make in India" strategy, India's manufacturing sector is at an inflection point. India should continue to benefit from global capital inflows, as trade tensions and the diversification of global supply chains are trends that are to persist in the medium term. Multi-national Corporations (MNCs) have committed large investments in areas like electronics manufacturing, and the Indian government has turned its policy agenda toward incentivising the localisation of manufacturing.

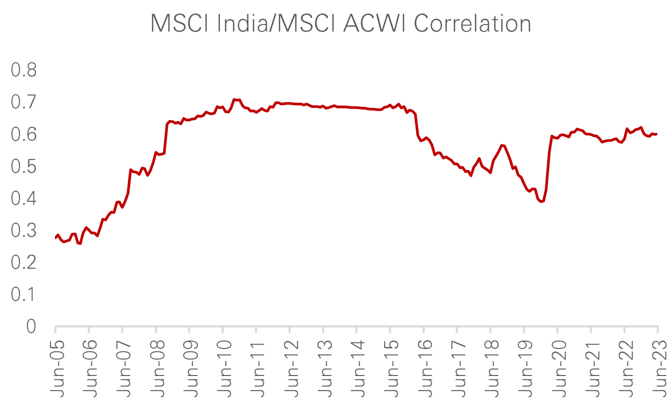
India's push for infrastructure like roads and ports will mean that there is significant scope for India to move up the value chain of manufacturing.

India can build on the comparative advantage it has in its IT sector to drive greater productivity.

India for global diversification

Due the unique characteristics of India's economy, an allocation to India can increase diversification for global investors. Indian equities have a lower correlation than other EM markets because of India's larger domestic economy. The lower correlation presents opportunities for investors to consider diversification by adding India to their portfolio, as demonstrated by the risk-adjusted returns over the past 20 years. A key reason for the diversification benefit stems from the resilience of its domestic economy, where its domestic companies are closely linked to its strong structural growth opportunities. In an environment where this growth is set to continue, choosing India as a means for diversification becomes even more crucial to consider.

India correlation with global markets



Source: HSBC Global Private Banking, Bloomberg as at 30 June 2023.

Risk Disclosures

Risks of investment in fixed income
There are several key issues that one should consider before making an investment into fixed income. The risk specific to this type of investment may include, but are not limited to:

Credit risk
Investor is subject to the credit risk of the issuer. Investor is also subject to the credit risk of the government and/or the appointed trustee for debts that are guaranteed by the government.

Risks associated with high yield fixed income instruments
High yield fixed income instruments are typically rated below investment grade or are unrated and as such are often subject to a higher risk of issuer default. The net asset value of a high-yield bond fund may decline or be negatively affected if there is a default of any of the high yield bonds that it invests in or if interest rates change. The special features and risks of high-yield bond funds may also include the following:

- Capital growth risk - some high-yield bond funds may have fees and/ or dividends paid out of capital. As a result, the capital that the fund has available for investment in the future and capital growth may be reduced; and
- Dividend distributions - some high-yield bond funds may not distribute dividends, but instead reinvest the dividends into the fund or alternatively, the investment manager may have discretion on whether or not to make any distribution out of income and/ or capital of the fund. Also, a high distribution yield does not imply a positive or high return on the total investment.
- Vulnerability to economic cycles - during economic downturns such instruments may typically fall more in value than investment grade bonds as (i) investors become more risk averse and (ii) default risk rises.

Risks associated with subordinated debentures, perpetual debentures, and contingent convertible or bail-in debentures

- Subordinated debentures - subordinated debentures will bear higher risks than holders of senior debentures of the issuer due to a lower priority of claim in the event of the issuer's liquidation.
- Perpetual debentures - perpetual debentures often are callable, do not have maturity dates and are subordinated. Investors may incur reinvestment and subordination risks. Investors may lose all their invested principal in certain circumstances. Interest payments may be variable, deferred or cancelled. Investors may face uncertainties over when and how much they can receive such payments.
- Contingent convertible or bail-in debentures - Contingent convertible and bail-in debentures are hybrid debt-equity instruments that may be written off or converted to common stock on the occurrence of a trigger event. Contingent convertible debentures refer to debentures that contain a clause requiring them to be written off or converted to common stock on the occurrence of a trigger event. These debentures generally absorb losses while the issuer remains a going concern (i.e. in advance of the point of non-viability). "Bail-in" generally refers to (a) contractual mechanisms (i.e. contractual bail-in) under which debentures contain a clause requiring them to be written off or converted to common stock on the occurrence of a trigger event, or (b) statutory mechanisms (i.e. statutory bail-in) whereby a national resolution authority writes down or converts debentures under specified conditions to common stock. Bail-in debentures generally absorb losses at the point of non viability. These features can introduce notable risks to investors who may lose all their invested principal.

Contingent convertible securities (CoCos) or bail-in debentures are highly complex, high risk hybrid capital instruments with unusual loss-absorbency features written into their contractual terms.
Investors should note that their capital is at risk and they may lose some or all of their capital.

Changes in legislation and/or regulation
Changes in legislation and/or regulation could affect the performance, prices and mark-to-market valuation on the investment.

Nationalisation risk
The uncertainty as to the coupons and principal will be paid on schedule and/or that the risk on the ranking of the bond seniority would be compromised following nationalisation.

Reinvestment risk
A decline in interest rate would affect investors as coupons received and any return of principal may be reinvested at a lower rate. Changes in interest rate, volatility, credit spread, rating agencies actions, liquidity and market conditions may have a negative effect on the prices, mark-to-market valuations and your overall investment.

Risk disclosure on Dim Sum Bonds
Although sovereign bonds may be guaranteed by the China Central Government, investors should note that unless otherwise specified, other renminbi bonds will not be guaranteed by the China Central Government.
Renminbi bonds are settled in renminbi, changes in exchange rates may have an adverse effect on the value of that investment. You may not get back the same amount of Hong Kong Dollars upon maturity of the bond.
There may not be active secondary market available even if a renminbi bond is listed. Therefore, you need to face a certain degree of liquidity risk.
Renminbi is subject to foreign exchange control. Renminbi is not freely convertible in Hong Kong. Should the China Central Government tighten the control, the liquidity of renminbi or even renminbi bonds in Hong Kong will be affected and you may be exposed to higher liquidity risks. Investors should be prepared that you may need to hold a renminbi bond until maturity.

Alternative Investments
Hedge Fund - Please note Hedge Funds often engage in leveraging and other speculative investment practices that may increase the risk of investment loss. They can also be highly illiq-

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uid, are not required to provide periodic pricing or valuation information to investors, and may involve complex tax structures and delays in distributing important information. Alternative investments are often not subject to the same regulatory requirements as, say, mutual funds, and often charge high fees that may potentially offset trading profits when they occur.

Private Equity - Please note Private Equity is generally illiquid, involving long term investments that do not display the liquid or transparency characteristics often found in other investments (e.g. Listed securities). It can take time for money to be invested (cash drag) and for investments to produce returns after initial losses.

Risk disclosure on Emerging Markets
Investment in emerging markets may involve certain, additional risks which may not be typically associated with investing in more established economies and/or securities markets. Such risks include (a) the risk of nationalisation or expropriation of assets;
(b) economic and political uncertainty; (c) less liquidity in so far of securities markets; (d) fluctuations in currency exchange rate; (c) higher rates of inflation; (f) less oversight by a regulator of local securities market; (g) longer settlement periods in so far as securities transactions and (h) less stringent laws in so far the duties of company officers and protection of Investors.

Risk disclosure on FX Margin
The price fluctuation of FX could be substantial under certain market conditions and/or occurrence of certain events, news or developments and this could pose significant risk to the Customer. Leveraged FX trading carry a high degree of risk and the Customer may suffer losses exceeding their initial margin funds. Market conditions may make it impossible to square/close-out FX contracts/options. Customers could face substantial margin calls and therefore liquidity problems if the relevant price of the currency goes against them.
The leverage of a product can work against you and losses can exceed those of a direct investment. If the market value of a portfolio falls by a certain amount, this could result in a situation where the value of collateral no longer covers all outstanding loan amounts. This means that investors might have to respond promptly to margin calls. If a portfolio's return is lower than its financing cost then leverage would reduce a portfolio's overall performance and even generate a negative return.

Currency risk – where product relates to other currencies
When an investment is denominated in a currency other than your local or reporting currency, changes in exchange rates may have a negative effect on your investment.
Chinese Yuan ("CNY") risks
There is a liquidity risk associated with CNY products, especially if such investments do not have an active secondary market and their prices have large bid/offer spreads.
CNY is currently not freely convertible and conversion of CNY through banks in Hong Kong and Singapore is subject to certain restrictions. CNY products are denominated and settled in CNY deliverable in Hong Kong and Singapore, which represents a market which is different from that of CNY deliverable in Mainland China.
There is a possibility of not receiving the full amount in CNY upon settlement, if the Bank is not able to obtain sufficient amount of CNY in a timely manner due to the exchange controls and restrictions applicable to the currency.

Illiquid markets/products
In the case of investments for which there is no recognised market,
it may be difficult for investors to sell their investments or to obtain reliable information about their value or the extent of the risk to which they are exposed.

Environmental, Social and Governance ("ESG") Customer Disclosure
In broad terms "sustainable investments" include investment approaches or instruments which consider environmental, social, governance and/or other sustainability factors to varying degrees. Certain instruments we classify as sustainable may be in the process of changing to deliver improved sustainability outcomes.
There is no guarantee that sustainable investments will produce returns similar to those which don't consider these factors. Sustainable investments may diverge from traditional market benchmarks.
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