Global Investment Office | April 17, 2024

Global Insights

India: 10 Things We Have Learned So Far

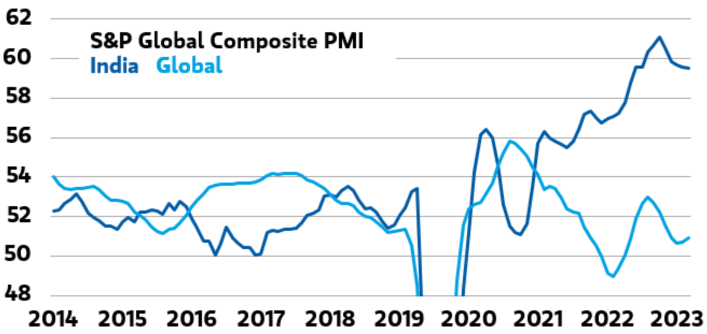
Christopher K. Baxter
Investment Strategist
Christopher.Baxter@morganstanley.com

Sonny Mendez
Investment Strategist
Sonny.Mendez@morganstanley.com

We believe India is on the rise and poised to become a major focal point for investors. Here are 10 things that we have learned.

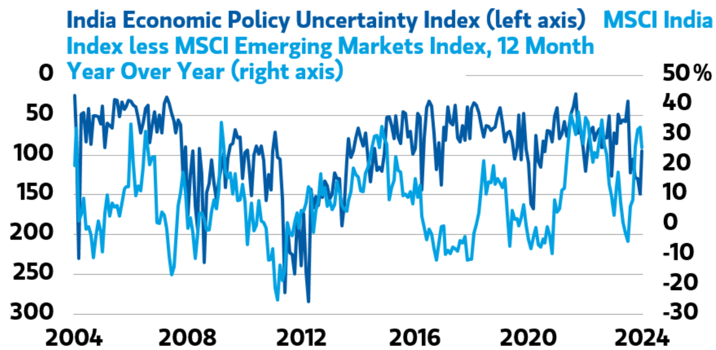
1. India's economic growth continues to surprise to the upside.
2. Policy certainty can exert a positive impact on India's stock market.
3. The middle class is India's fastest-growing major population segment.
4. Food is likely to have a smaller weight in India's consumer price index in the future.
5. Over the next decade, one-fourth of the world's incremental workforce will likely come from India.
6. India's stock market reflects confidence in the India growth story.
7. India's real estate sector could grow threefold from its current level, as residential and commercial demand increase.
8. India's renewed focus on capital expenditures will likely fuel its ambitious pro-growth agenda.
9. India's 2024-2025 budget reflects shifting priorities.
10. India is on track to become the world's third-largest economy by 2027.

1. India's economic growth continues to surprise to the upside. The S&P Global India Composite Purchasing Managers' Index (PMI), a survey-based measure of economic trends in India's manufacturing and services sectors, has been above 50 for 31 consecutive months. Although the current 60.6 level is below the July 2023 peak, the latest reading is positive for India's economy. The global picture, meanwhile, is less sanguine. While global activity accelerated slightly last month, the risk of recession in Europe is elevated, China's housing market faces strong headwinds and US inflation remains stubbornly high, which means that policy rates could remain in restrictive territory for some time—weighing on growth. We think that the setup for India remains compelling on both an absolute and relative basis, given its positive policy backdrop, macro stability and signs that its capex cycle is on the rise.



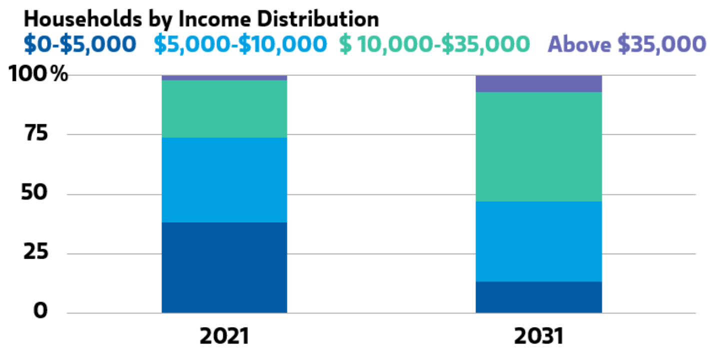
Note: Chart is truncated at 48 and based on a six-month moving average. A reading above 50 indicates an expansion in activity, while a reading below 50 indicates contraction.
Source: Alpine Macro, Haver, Morgan Stanley Wealth Management Global Investment Office as of Feb. 29, 2024

2. Policy certainty can exert a positive impact on India's stock market. The India Economic Policy Uncertainty Index declined to 94.5 in March from 148.8 in February—a favorable development. At the macro level, the index warns of the ramifications of economic policy actions. A lower level indicates policy "certainty," while a higher level indicates policy "uncertainty." This is important because uncertainty could weigh on India's equity markets. In fact, a broad 2015 International Monetary Fund study found that a one-standard deviation increase in uncertainty is associated with an almost 1.25% decline in output growth—depending on the measure used. All told, there is a great deal of optimism around India's economy. Forecasters predict Prime Minister Narendra Modi will secure a third five-year term, which should continue to drive upside surprises given his growth-oriented policy focus. We expect potential resulting continuity to foster market certainty, which could support India outperformance versus the broader emerging markets.



Source: Bloomberg, Morgan Stanley Wealth Management Global Investment Office as of March 29, 2024

3. The middle class is India's fastest-growing major population segment. In 2021, nearly 75% of Indian households had incomes below $10,000. Morgan Stanley & Co. Research predicts that by 2031, 46% of the population will fall in the $10,000-$35,000 range—nearly double the 2021 level. As India's middle class expands, consumption, which is essential for economic growth, will likely accelerate as well. Although we expect India's economic momentum to remain strong, its economy faces obstacles. For example, while India is the world's most populous country, its 55.4% labor force participation rate is one of the lowest in the world. That said, India's demographic dividend—economic growth that may result from a rapid change in a country's demographics—should boost future incomes. Further, as more people move to cities, where many of the country's manufacturing jobs are located, India's economy will receive a boost. Currently, only 36% of India's citizens live in cities, and meaningful improvement in that number could present a tremendous opportunity for growth.



Source: CEIC, Bloomberg, Morgan Stanley & Co., Morgan Stanley Wealth Management Global Investment Office as of April 6, 2024. Morgan Stanley & Co. estimates for 2031.

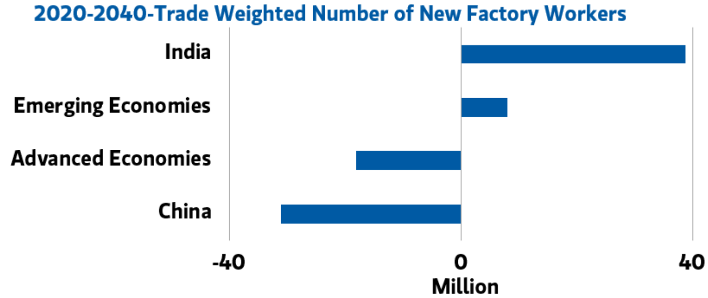
4. Food is likely to have a smaller weight in India's consumer price index in the future. Annualized inflation in India fell to 5.1% in March from 5.4% in December 2023. Food inflation, which has recently accounted for nearly half of India's consumer price index (CPI), is a major problem for the Reserve Bank of India; notably it has kept its benchmark rate unchanged for 15 straight months to guide inflation toward its 4% target. Compared to the US, food is a much bigger weight in India's CPI basket. In fact, the food and beverages category is only around 14% of US CPI. Indian policymakers are currently considering reducing food's weight in its CPI market basket. According to economists at Emkay Global, a financial services company headquartered in Mumbai, food could be reduced to 40% of the basket from 46% today. This is important because India ranks as the eighth largest global importer of agricultural and related products and because food prices are generally volatile. India has a history of implementing restrictive measures on the exports of key commodities to keep a lid on local prices.

CPI Basket Proportional Weightings

Note: Base year is 2012
Source: Government of India Ministry of Statistics and Program Implementation, Morgan Stanley Wealth Management Global Investment Office as of Feb. 29, 2024

5. Over the next decade, one-fourth of the world's incremental workforce will come from India. Bloomberg estimates that nearly 50 million medium-skilled workers will retire in China and other advanced economies from 2020 to 2040 and that India will add nearly 40 million over the same period. Prime Minister Modi has pledged to boost manufacturing during his third term. In fact, his "Make in India" initiative aims to promote India as the preferred global manufacturing destination. Already, India is reaping the benefits. According to Bloomberg, Apple produced $14 billion worth of iPhones in India over the past fiscal year. Further, as many as 61% of the 500 executive-level US managers surveyed by market research firm OnePoll said they would pick India over China if both could manufacture the same materials. India's demographic dividend should enhance its competitiveness and push it toward Prime Minister Modi's goal of raising the manufacturing sector's contribution from its current 15.8% of GDP to 25% by 2040.

2020-2040-Trade Weighted Number of New Factory Workers

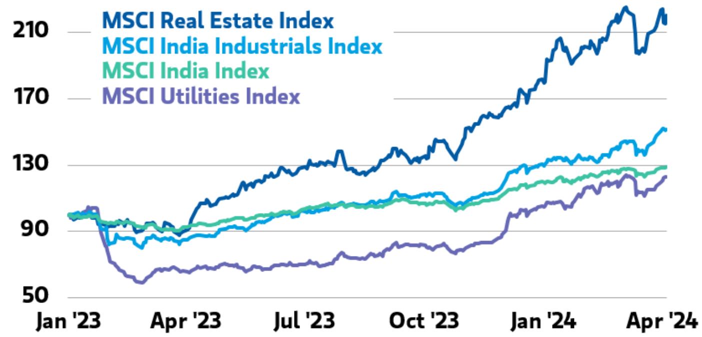


Source: Bloomberg, Morgan Stanley Wealth Management Global Investment Office as of April 7, 2024

6. India's stock market reflects confidence in the India growth story. Since December 2021, China's market capitalization has declined by $4 trillion—more than the current value of India's stock market. Still, the Indian National Stock Exchange is the third-largest in Asia and the fourth-largest in the world. The key point is that India's market cap as a percent of global market cap has doubled to almost 4% since the start of the COVID-19 pandemic. We think that it can grow further given important tailwinds. Specifically, India's promising growth outlook, policy support and revival of public/private investment may help it outpace Japan, which is the next-closest country in terms of market cap. Additionally, India's upcoming inclusion in the benchmark JP Morgan Emerging Market Bond Index will likely help attract more foreign investment. In fact, according to a press statement issued by JP Morgan, India will likely achieve its maximum 10% weight in the index by next year—leading to billions of dollars of inflows into local currency government debt. Although there will be little direct impact on equity markets, potentially lower bond yields and a more stable currency should support economic activity.

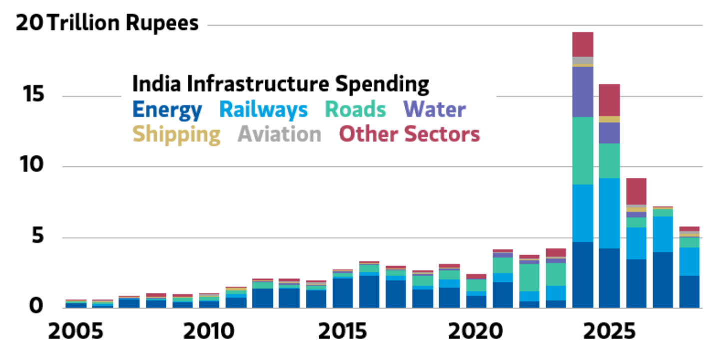
Equity Market Capitalization

Source: Bloomberg, Morgan Stanley Wealth Management Global Investment Office as of March 31, 2024



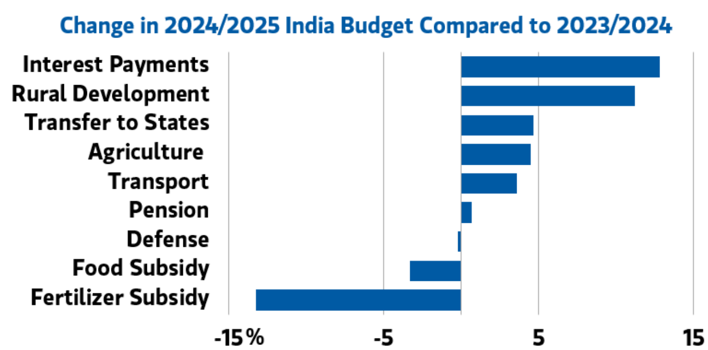
Source: Bloomberg, Morgan Stanley Wealth Management Global Investment Office as of April 5, 2024

7. India's real estate sector could grow threefold from its current level, as residential and commercial demand increase. The MSCI India Real Estate Index, which seeks to measure the performance of the real estate sector in India's equity market, has increased 120% since Jan. 2, 2023. Over the same period, India's utilities and industrials sectors have generated total returns of 23% and 51%, respectively, and the MSCI India Index has returned 28%. As investors sniff out ways to access India's growth, which has been driven mainly by strong domestic consumption, construction and manufacturing, real estate is at the forefront of those efforts. On an average annualized basis, foreign investors have invested $4 billion in India's property market over the past five years. While the largest allocations have come from the US and Canada, Asia Pacific investors are also looking to India's real estate market, with aggregate inflows from the Asia Pacific region surging to $1.8 billion in 2023—nearly double the 2019 level.



Source: Bloomberg, Morgan Stanley Wealth Management Global Investment Office as of April 8, 2024. Bloomberg estimates for 2024 and beyond.

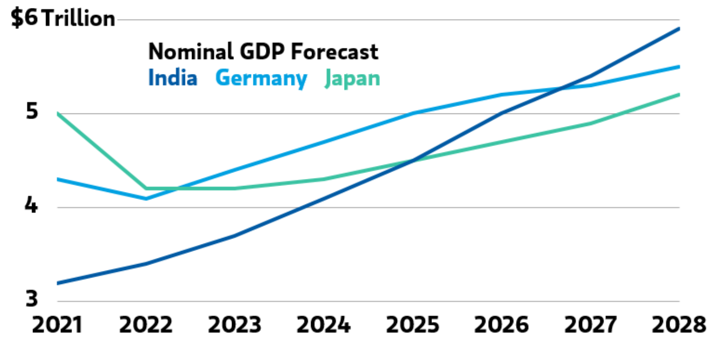
8. India's renewed focus on capex will likely fuel its ambitious pro growth agenda. When it comes to infrastructure, India is at the cusp of significant transformation. According to data collected by Bloomberg, Indian policymakers' allocation to infrastructure has more than tripled in the past five years. This is important because infrastructure growth is critical to India's development. This includes both hard infrastructure, such as shipping ports, airports, rail lines and freights, and soft infrastructure, such as that providing access to electric and fixed broadband services. Indeed, investment-driven fiscal strategies globally act as a 1.4x growth multiplier, according to Oxford Economics. This compares to 1x for public spending and 0.5x for tax cuts. That said, policymakers must be careful, as high debt burdens can lead to diminishing returns, especially if debt servicing costs are elevated.



Source: Reuters, Morgan Stanley Wealth Management Global Investment Office as of Feb. 1, 2024

9. India's 2024-2025 budget reflects shifting priorities. Overall, India's 2024-2025 budget increased 7.5% versus 2023-2024. Of the 10 major sectors with the highest allocation, rural development, agriculture and transport stand out to us. Notably, rural development includes affordable housing for low- and middle-income residents. India's finance minister and minister of corporate affairs, Nirmala Sitharaman, has committed the country to building 20 million affordable units over the next five years. At the same time, the government plans to reduce the deficit to 5.1% through increased taxes and asset proceeds. In 2023-2024, India saw its tax-to-GDP ratio rise to its highest level in a decade, as a result of a strong economy and strict enforcement of tax collections. The government expects tax revenue to rise by 11.5% in 2024-2025 due to ongoing growth in nominal GDP, which includes the impact of inflation. We believe India's economy will be supported by strong tailwinds from policies leveraging demographics, urbanization, public/private capex and manufacturing trends to power growth.

10. India is on track to become the world's third-largest economy by 2027. We see several factors contributing to its attractiveness. First, it is a popular destination for foreign direct investment (FDI). Second, a reconfiguration of global supply chains coupled with a young and highly skilled workforce could boost its economic outlook. Third, investments in infrastructure, which could serve as the backbone of India's economic growth, are projected to rise $1.7 trillion between 2024 and 2030. Fourth, its sizable equity market and its inclusion in benchmark bond indexes will boost its attractiveness to international investors. Finally, India has taken steps to tackle corruption. For example, its de-monetization campaign, which moved activity away from the informal economy, came with the longer-term benefit of improving tax collection.



Source: International Monetary Fund, Morgan Stanley Wealth Management Global Investment Office as of Feb. 12, 2024. IMF forecasts for 2024 and beyond.

Disclosure Section

Index Definitions

India Economic Policy Uncertainty Index reflects scaled monthly counts of articles containing 'uncertain' or 'uncertainty' or 'uncertainties' or 'uncertainties', 'economic' or 'economy', and one or more of policy-relevant terms listed for India.
The MSCI India/Industrials Index is a free-float weighted equity index. It was developed with a base value of 100 as of December 31, 1998. The parent index is MXIN.
The MSCI India/Utilities Index is a free-float weighted equity index. It was developed with a base value of 100 as of December 31, 1998. The parent index is MXIN
The MSCI India/Real Estate Index is a free-float weighted equity index. It was developed with a base value of 1000 as of August 31, 2016. The parent index is MXIN. GICS Level 1.

For other index, indicator and survey definitions referenced in this report please visit the following: https:/ www.morganstanley.com/wealthinvestmentsolutions/wmir-definitions

Important note regarding economic sanctions:

This report may involve the discussion of country/ies which are generally the subject of selective sanctions programs administered or enforced by the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC"), the European Union and/or by other countries or multi-national bodies. The content of this presentation is for informational purposes and does not represent Morgan Stanley's view as to whether or not any of the Persons, instruments or investments discussed are or may become subject to sanctions. *Any references in this presentation to entities or instruments that may be covered by such sanctions should not be read as recommending or advising on any investment activities involving such entities or instruments.* Users of this report are solely responsible for ensuring that your investment activities in relation to any sanctioned country/ies are carried out in compliance with applicable sanctions.

Risk Considerations

Investing in foreign markets entails greater risks than those normally associated with domestic markets, such as political, currency, economic and market risks. **Investing in currency** involves additional special risks such as credit, interest rate fluctuations, derivative investment risk, and domestic and foreign inflation rates, which can be volatile and may be less liquid than other securities and more sensitive to the effect of varied economic conditions. In addition, international investing entails greater risk, as well as greater potential rewards compared to U.S. investing. These risks include political and economic uncertainties of foreign countries as well as the risk of currency fluctuations. These risks are magnified in countries with **emerging markets and frontier markets**, since these countries may have relatively unstable governments and less established markets and economies. Yields are subject to change with economic conditions. Yield is only one factor that should be considered when making an investment decision.

Equity securities may fluctuate in response to news on companies, industries, market conditions and general economic environment.

Bonds are subject to interest rate risk. When interest rates rise, bond prices fall; generally the longer a bond's maturity, the more sensitive it is to this risk. Bonds may also be subject to call risk, which is the risk that the issuer will redeem the debt at its option, fully or partially, before the scheduled maturity date. The market value of debt instruments may fluctuate, and proceeds from sales prior to maturity may be more or less than the amount originally invested or the maturity value due to changes in market conditions or changes in the credit quality of the issuer. Bonds are subject to the credit risk of the issuer. This is the risk that the issuer might be unable to make interest and/or principal payments on a timely basis. Bonds are also subject to reinvestment risk, which is the risk that principal and/or interest payments from a given investment may be reinvested at a lower interest rate.

Bonds rated below investment grade may have speculative characteristics and present significant risks beyond those of other securities, including greater credit risk and price volatility in the secondary market. Investors should be careful to consider these risks alongside their individual circumstances, objectives and risk tolerance before investing in high-yield bonds. High yield bonds should comprise only a limited portion of a balanced portfolio.

Investing in smaller companies involves greater risks not associated with investing in more established companies, such as business risk, significant stock price fluctuations and illiquidity.

Yields are subject to change with economic conditions. Yield is only one factor that should be considered when making an investment decision. Credit ratings are subject to change.

Asset allocation and diversification do not assure a profit or protect against loss in declining financial markets.

Investing in commodities entails significant risks. Commodity prices may be affected by a variety of factors at any time, including but not limited to, (i) changes in supply and demand relationships, (ii) governmental programs and policies, (iii) national and international political and economic events, war and terrorist events, (iv) changes in interest and exchange rates, (v) trading activities in commodities and related contracts, (vi) pestilence, technological change and weather, and (vii) the price volatility of a commodity. In addition, the commodities markets are subject to temporary distortions or other disruptions due to various factors, including lack of liquidity, participation of speculators and government intervention.

Physical precious metals are non-regulated products. Precious metals are speculative investments, which may experience short-term and long-term price volatility. The value of precious metals investments may fluctuate and may appreciate or decline, depending on market conditions. If sold in a declining market, the price you receive may be less than your original investment. Unlike bonds and stocks, precious metals do not make interest or dividend payments. Therefore, precious metals may not be appropriate for investors who require current income. Precious metals are commodities that should be safely stored, which may impose additional costs on the investor. The Securities Investor Protection Corporation ("SIPC") provides certain protection for customers' cash and securities in the event of a brokerage firm's bankruptcy, other financial difficulties, or if customers' assets are missing. SIPC insurance does not apply to precious metals or other commodities.

Treasury Inflation Protection Securities' (TIPS) coupon payments and underlying principal are automatically increased to compensate for inflation by tracking the consumer price index (CPI). While the real rate of return is guaranteed, TIPS tend to offer a low return. Because the return of TIPS is linked to inflation, TIPS may significantly underperform versus conventional U.S. Treasuries in times of low inflation.

The returns on a portfolio consisting primarily of **environmental, social, and governance-aware investments (ESG)** may be lower or higher than a portfolio that is more diversified or where decisions are based solely on investment considerations. Because ESG criteria exclude some investments, investors may not be able to take advantage of the same opportunities or market trends as investors that do not use such criteria. The companies identified and investment examples are for illustrative purposes only and should not be deemed a recommendation to purchase, hold or sell any securities or investment products. They are intended to demonstrate the approaches taken by managers who focus on ESG criteria in their investment strategy. There can be no guarantee that a client's account will be managed as described herein.

Because of their narrow focus, **sector investments** tend to be more volatile than investments that diversify across many sectors and companies. **Technology** stocks may be especially volatile. Risks applicable to companies in the **energy and natural resources sectors** include commodity pricing risk, supply and demand risk, depletion risk and exploration risk. **Health care sector** stocks are subject to government regulation, as well as government approval of products and services, which can significantly impact price and availability, and which can also be significantly affected by rapid obsolescence and patent expirations.

Rebalancing does not protect against a loss in declining financial markets. There may be a potential tax implication with a rebalancing strategy. Investors should consult with their tax advisor before implementing such a strategy.

The **indices** are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment.

The **indices selected by Morgan Stanley Wealth Management** to measure performance are representative of broad asset classes. Morgan Stanley Wealth Management retains the right to change representative indices at any time.

Disclosures

Morgan Stanley Wealth Management is the trade name of Morgan Stanley Smith Barney LLC, a registered broker-dealer in the United States. This material has been prepared for informational purposes only and is not an offer to buy or sell or a solicitation of any offer to buy or sell any security or other financial instrument or to participate in any trading strategy. Past performance is not necessarily a guide to future performance. The author(s) (if any authors are noted) principally responsible for the preparation of this material receive compensation based upon various factors, including quality and accuracy of their work, firm revenues (including trading and capital markets revenues), client feedback and competitive factors. Morgan Stanley Wealth Management is involved in many businesses that may relate to companies, securities or instruments mentioned in this material.

This material has been prepared for informational purposes only and is not an offer to buy or sell or a solicitation of any offer to buy or sell any security/instrument, or to participate in any trading strategy. Any such offer would be made only after a prospective investor had completed its own independent investigation of the securities, instruments or transactions, and received all information it required to make its own investment decision, including, where applicable, a review of any offering circular or memorandum describing such security or instrument. That information would contain material information not contained herein and to which prospective participants are referred. This material is based on public information as of the specified date, and may be stale thereafter. We have no obligation to tell you when information herein may change. We make no representation or warranty with respect to the accuracy or completeness of this material. Morgan Stanley Wealth Management has no obligation to provide updated information on the securities/instruments mentioned herein.

The securities/instruments discussed in this material may not be appropriate for all investors. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives. Morgan Stanley Wealth Management recommends that investors independently evaluate specific investments and strategies, and encourages investors to seek the advice of a financial advisor. The value of and income from investments may vary because of changes in interest rates, foreign exchange rates, default rates, prepayment rates, securities/instruments prices, market indexes, operational or financial conditions of companies and other issuers or other factors. Estimates of future performance are based on assumptions that may not be realized. Actual events may differ from those assumed and changes to any assumptions may have a material impact on any projections or estimates. Other events not taken into account may occur and may significantly affect the projections or estimates. Certain assumptions may have been made for modeling purposes only to simplify the presentation and/or calculation of any projections or estimates, and Morgan Stanley Wealth Management does not represent that any such assumptions will reflect actual future events. Accordingly, there can be no assurance that estimated returns or projections will be realized or that actual returns or performance results will not materially differ from those estimated herein.

The summary at the beginning of the report may have been generated with the assistance of artificial intelligence (AI).

This material should not be viewed as advice or recommendations with respect to asset allocation or any particular investment. This information is not intended to, and should not, form a primary basis for any investment decisions that you may make. Morgan Stanley Wealth Management is not acting as a fiduciary under either the Employee Retirement Income Security Act of 1974, as amended or under section 4975 of the Internal Revenue Code of 1986 as amended in providing this material except as otherwise provided in writing by Morgan Stanley and/or as described at www.morganstanley.com/disclosures/dol.

Morgan Stanley Smith Barney LLC, its affiliates and Morgan Stanley Financial Advisors do not provide legal or tax advice. Each client should always consult his/her personal tax and/or legal advisor for information concerning his/her individual situation and to learn about any potential tax or other implications that may result from acting on a particular recommendation. This material is disseminated in Australia to "retail clients" within the meaning of the Australian Corporations Act by Morgan Stanley Wealth Management Australia Pty Ltd (A.B.N. 19 009 145 555, holder of Australian financial services license No. 240813). Morgan Stanley Wealth Management is not incorporated under the People's Republic of China ("PRC") law and the material in relation to this report is conducted outside the PRC. This report will be distributed only upon request of a specific recipient. This report does not constitute an offer to sell or the solicitation of an offer to buy any securities in the PRC. PRC investors must have the relevant qualifications to invest in such securities and must be responsible for obtaining all relevant approvals, licenses, verifications and or registrations from PRC's relevant governmental authorities.

If your financial adviser is based in Australia, Switzerland or the United Kingdom, then please be aware that this report is being distributed by the Morgan Stanley entity where your financial adviser is located, as follows: Australia: Morgan Stanley Wealth Management Australia Pty Ltd (ABN 19 009 145 555, AFSL No. 240813); Switzerland: Morgan Stanley (Switzerland) AG regulated by the Swiss Financial Market Supervisory Authority; or United Kingdom: Morgan Stanley Private Wealth Management Ltd, authorized and regulated by the Financial Conduct Authority, approves for the purposes of section 21 of the Financial Services and Markets Act 2000 this material for distribution in the United Kingdom. Morgan Stanley Wealth Management is not acting as a municipal advisor to any municipal entity or obligated person within the meaning of Section 15B of the Securities Exchange Act (the "Municipal Advisor Rule") and the opinions or views contained herein are not intended to be, and do not constitute, advice within the meaning of the Municipal Advisor Rule. This material is disseminated in the United States of America by Morgan Stanley Wealth Management. Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data. This material, or any portion thereof, may not be reprinted, sold or redistributed without the written consent of Morgan Stanley Smith Barney LLC.

RSI1713375318085 04/2024