



Why India: A favourable macro environment

One may conclude from the past decade that India is likely to remain a low-growth economy. We disagree. Many ingredients are now in place for a revival in economic growth and sustainable development. Below are some of the macro-economic tailwinds that contribute to this view.

A lower-carbon future

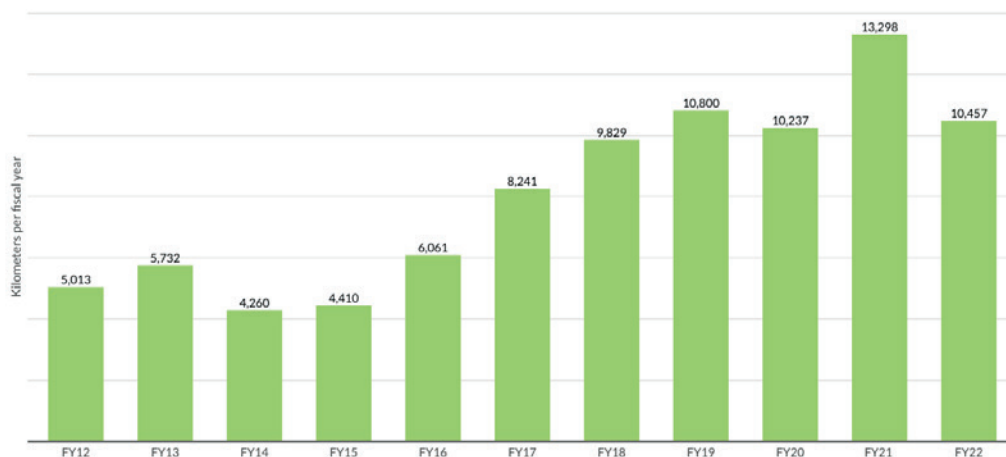
India has only produced 3% of total carbon dioxide emissions historically¹. The United States, Europe and China have together contributed 60%¹. As a signatory to the Paris Agreement, India has committed to reduce carbon intensity by 33-35% by 2030². As part of this journey, 175 gigawatts (GW) of renewable-generation capacity was already commissioned or in construction by 2022, up from just 34 GW in 2014³. Falling solar prices could help India reach its target of 500 GW by 2030 or 60-65% of total generation capacity³. Changes in vehicle emission norms to European standards, rapid evolution of electric vehicle (EV) technology and the introduction of scrappage vehicle policies should further reduce emissions intensity and improve the country's finances. These are sound reasons to believe India will not follow a similar carbon-intensive development path as the West or even China. Mahindra & Mahindra is the largest maker of EV three wheelers in India, with three wheelers an important

part of urban mobility, both for passengers and small freight. The group has started evolving its automotive business to EVs with the commitment of significant capital to this journey.

Early signs of a revival in infrastructure investment & the manufacturing sector

Infrastructure investment has been India's Achilles heel. It could well be its champion in the next decade. For instance, construction of new roads has continued behind the scenes at a good pace. Private investments and participation have now begun to improve in areas such as airports, gas and power distribution, renewable energy and even parts of the railways. The government has embarked on many difficult but essential reforms in agriculture and labour markets. The pace of reforms is likely to be dictated by acceptance from various stakeholders. This is necessary to ensure the benefits of development are widespread and equitable.

Road construction in India

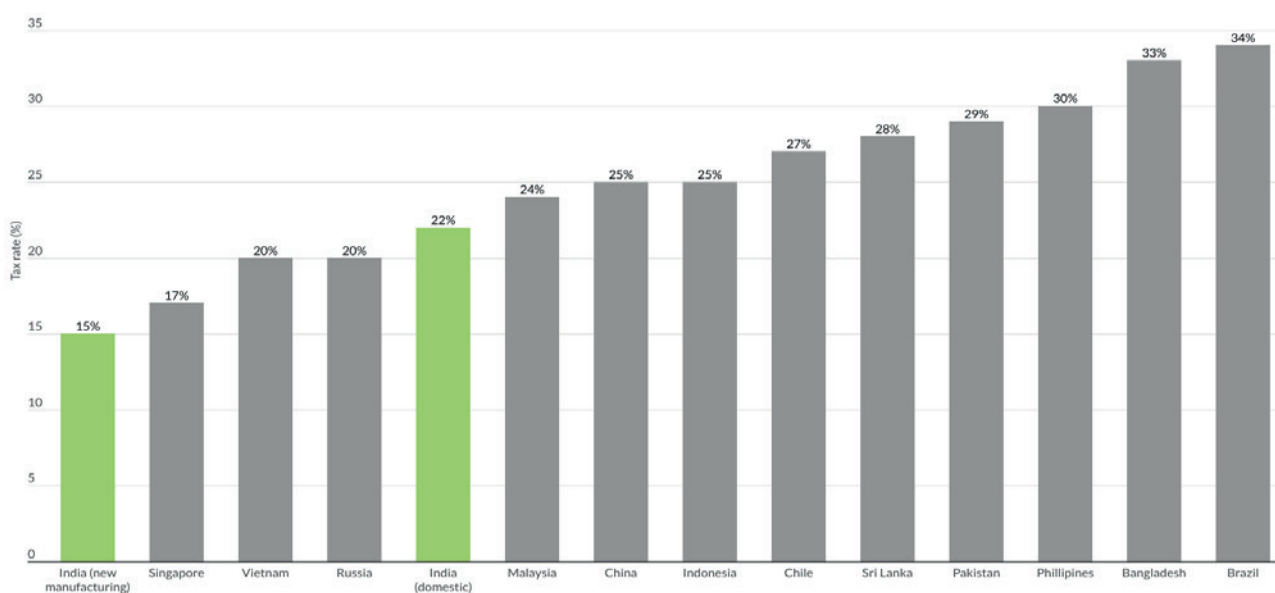


Source: Ministry of Road Transport and Highways, Indian government.

Funding availability and lower interest rates are necessary ingredients to fuel an investment cycle. The previous cycle was overly dependent on the state banking system as a funding source. Today, insurance companies, infrastructure investment trusts, corporate bond markets and large well-capitalised private banks can participate in financing infrastructure. Unlike what we see elsewhere, corporate and bank balance sheets have been slow to repair in the last decade. The insurance industry's assets have grown to USD600bn from just USD200bn a decade ago⁴ If India keeps the long-term inflation genie in the bottle, it could become an attractive destination for long-term debt capital.

India's manufacturing sector is showing early signs of promise. While the government encourages investment in local manufacturing through attractive taxation and labour reforms, the case is becoming stronger from the bottom-up via productivity improvements. A large domestic market, improving infrastructure and the increasing need to diversify global supply chains add wind to India's manufacturing sails. Apple's suppliers have invested close to a billion dollars to set up manufacturing units in recent years⁵.

Corporate tax rates



Source: Country government statistics and OECD, 2020.

An emerging quality healthcare ecosystem

COVID has put the spotlight firmly back on India's poor healthcare system. India has only 16 healthcare professionals per 10,000 compared to the 23 prescribed by the WHO⁶. The problem is made more acute as only 3% of India's doctors reside in rural areas where much of India's population resides⁷. More than 70% of Indians pay for healthcare costs out of their pockets⁸. A government plan, launched in 2018, to cover 500 million underprivileged people through health insurance is an important step in the right direction⁹. The program, intermediated by the private insurance sector, is helping improve the quality of affordable healthcare. More than 20,000 hospitals have empanelled themselves to address patients under this scheme¹⁰.

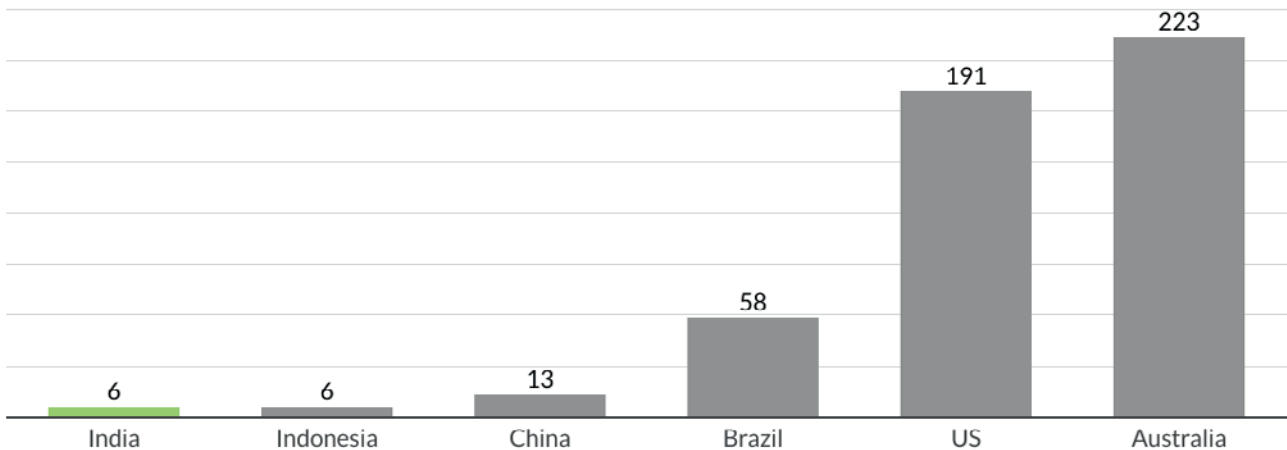
Evolution of diagnostic services is an example of how the private sector can deliver quality healthcare intervention at scale. Diagnostics represents a small percentage of total spends but has an outsized impact in reducing healthcare costs through prevention and early detection. The diagnostics industry in India is underpenetrated, and there is a need to formalize the sector and improve quality of service. This means leading, organized players such as Dr. Lal PathLabs are extremely well positioned.

In 2021 Dr. Lal PathLabs served 27 million patients at a cost of US\$ 10 per patient¹¹. Keeping their services affordable means the company addresses a large section of society without compromising on profitability. The presence of family stewards with long-term horizons, and a rock-solid balance sheet, gives them the strength to withstand periods of intense competition.

"We continue to drive our business on the back of high patient volumes and a favourable test mix. We have been able to grow our volumes consistently through the years, without compromising on our margins, nor increasing prices of tests"

Dr. Arvind Lal (Chairman & Founder of Dr. Lal PathLabs – Annual Report 2022)

Diagnostics spends per capita (USD)



Source: Spark Capital estimates 2022.

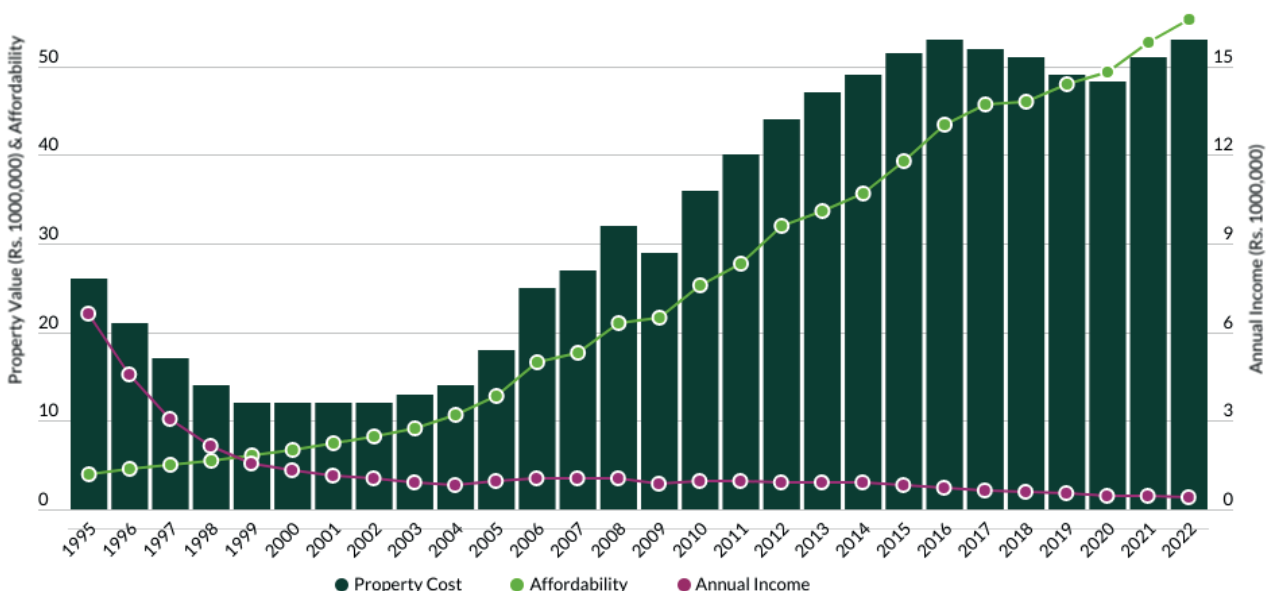
Early signs of revival of the property cycle

“Over the past two years, I have been on record several times stating that I have never been as optimistic about the demand for home loans as I am currently. Despite the recent headwinds in the global macro landscape, I continue to maintain this stance. India is on the cusp of an economic transformation”

Deepak Parekh (Chairman of HDFC - Annual Report 2022)

Structural changes are afoot in how people view homes and the need for work spaces within homes. And property is more affordable today than at any time in the last 25 years¹². Tax incentives for affordable housing materially reduce the cost of servicing mortgages. India remains one of the most attractive mortgage markets in the world due to low home ownership, low mortgage penetration, and a young population. Mortgages would have to grow at twice the rate of GDP in the next 10 years just to catch up with China. Aavas Financiers, a provider of mortgages for rural India, operates in a space where mortgage penetration is just 1% of GDP¹³. Aavas has built a high-quality credit risk culture which is difficult to replicate through capital or technology. Aavas aims to improve home ownership by women in the communities it operates in, with an aspiration to reach 40% of women borrowers in the coming decade¹⁴. Aavas is also working with the government to introduce regulations around better and greener building standards for rural areas¹⁵. These are the qualities of a leader, and a high-quality company that is addressing many human development challenges through their service.

Improved affordability



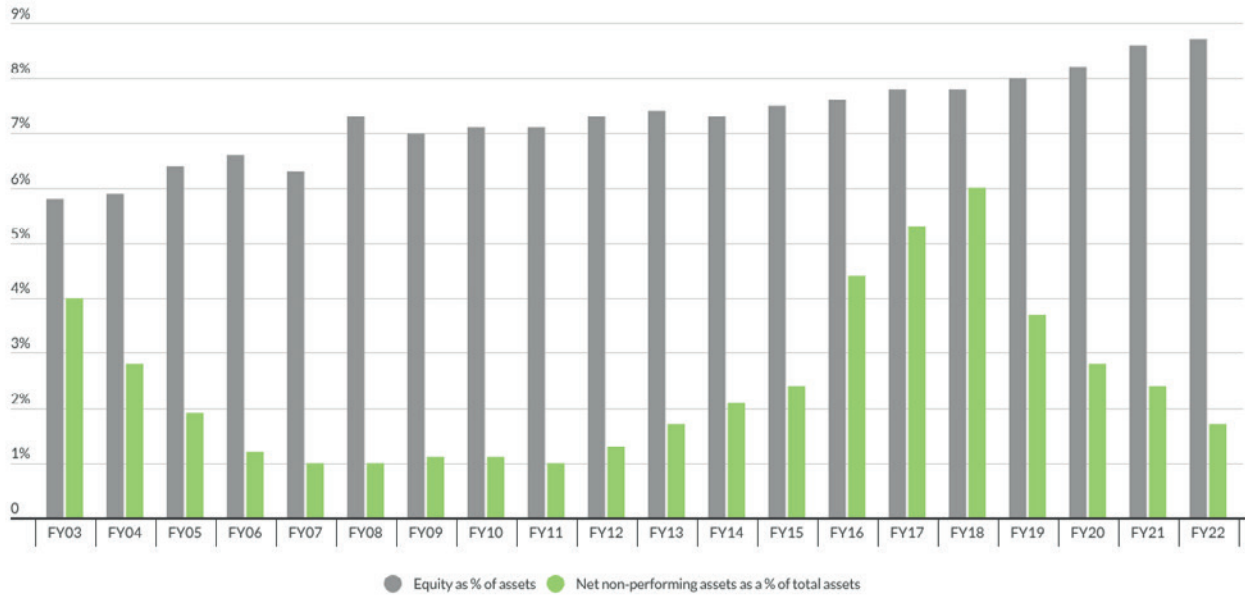
Source: HDFC. Data reflective of HDFC’s customer base.

An emerging quality financial services ecosystem

India has been dealing with a banking crisis unleashed by the excesses of the financial bubble leading up to 2008. The correction process has been helped by the introduction of the IBC (Insolvency and Bankruptcy Code) in 2016, a much-needed reform to speed up the resolution of insolvent businesses. The acquisition of

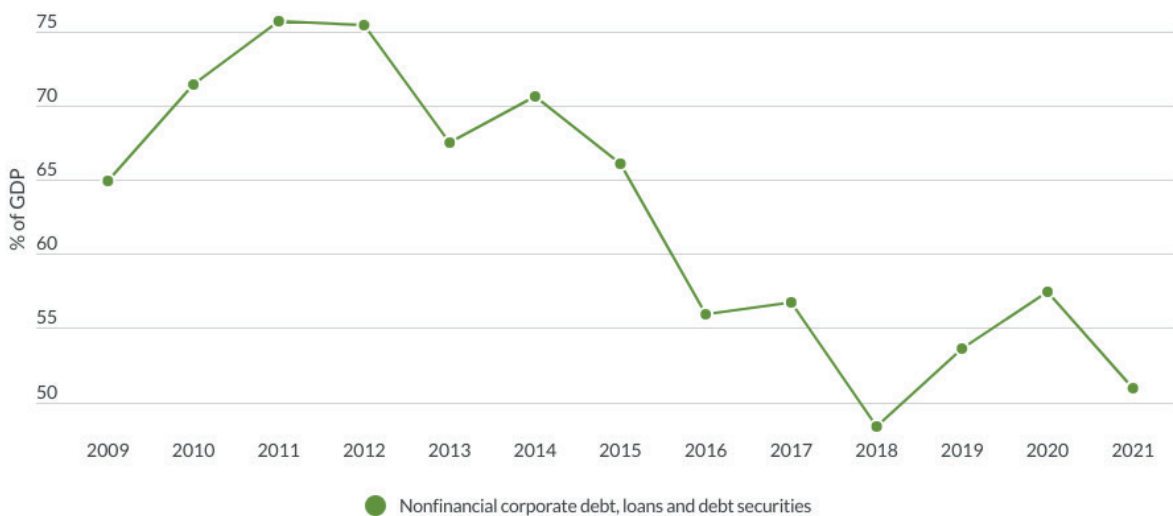
CG Power by Tube Investments was evidence of the IBC at work. Many bank failures and multiple rounds of capital raising and corporate deleveraging have occurred in the last decade. As a result, India's banking system is in a much healthier shape with fewer, but stronger, institutions. Low leverage in the system adds sail to the capex-cycle winds.

Banks in good health: Indian banking sector



Source: Centre for Monitoring Indian Economy (CMIE), Spark Capital estimates for 2022

India's corporate debt sector at historic lows



Source: International Monetary Fund (IMF), 2022

UPI (Unified Payments Interface) is an open payments platform built and owned by the Indian government. A common architecture socialises an important digital railroad. Currently, 376 banks and payment service providers use this railroad to offer easy and low cost payments and transfers for society¹⁶. In other markets, this infrastructure is often owned by private entities such as Visa and Mastercard, leading to higher costs for the ecosystem and slower adoption. UPI was conceived by the previous government in 2009 and launched in 2016 by the current government.

Today roughly 376 banks and payment providers are building their services on this platform. As a result, India currently processes 260 million digital transactions per day. This is more than any other country and is well ahead of developed market peers¹⁷. We are excited for the technology's ability to accelerate financial inclusion. A similar social digital infrastructure for retail e-commerce is currently being built by the government.

A noisy democracy

India is a noisy democracy but there is a strong underlying desire for reform and progress. External shocks can introduce obstacles in this development path, but the direction of travel is clear. It is a region which demands patience but rewards patient investors through steady compounding of returns. In our opinion, a large domestic market, evolving macro tailwinds, a clear confluence between sustainable development opportunity and investment returns, an accountable system with checks and balances and a universe of high-quality companies makes India an attractive destination for long-term capital.

¹ Source: Our World in Data based on the Global Carbon Project. Share of global cumulative carbon dioxide emissions, 2019. Hannah Ritchie and Max Roser (2017) - "CO2 and Greenhouse Gas Emissions". Published online at OurWorldInData.org. Retrieved from: '<https://ourworldindata.org/co2-and-other-greenhouse-gas-emissions>'.

² Source: [United Nations Climate Change](#).

³ Source: [United Nations Climate Action Summit 23 September 2019](#).

⁴ Source: Motilal Oswal Financial Services Limited.

⁵ Source: Reuters, 28 September 2020.

⁶ Source: [National Library of Medicine](#).

⁷ Source: [The World Health Organisation](#).

⁸ Source: [The Wire](#), Apr, 2018. [Who is paying for India's healthcare?](#)

⁹ Source: Ahmad, Hassan, 2018. [HPHR, Health Care for India's 500 Million: The Promise of the National Health Protection Scheme](#).

¹⁰ Source: [National Library of Medicine](#).

¹¹ Source: Dr Lal PathLabs Annual Report 2022.

¹² Source: Stewart Investors and company data.

¹³ Source: Aavas Financiers presentation 2022.

¹⁴ Source: Aavas Financiers Annual Report 2022.

¹⁵ Source: [IFC Org](#).

¹⁶ Source: [Live members, NPCI at 23 December 2022](#).

¹⁷ Source: [Product statistics, NPCI at 23 December 2022](#).

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