



**MIRAE ASSET LENS ISSUE 7**      **PART III**

**India: An Exciting Consumption Story in Asia**

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**Contributors**

Mirae Asset Global Investments  
(Hong Kong) Limited  
Asia Pacific Investment/Research

**Sol Ahn**  
Senior Investment Analyst

## India: An Exciting Consumption Story in Asia

### India's Consumer-led Renaissance

Indian consumers are forming one of the most fascinating growth stories in Asia, with low penetration of branded consumer goods and rising incomes creating an exciting business and investment opportunity.

Only around 12% of Indians currently purchase branded consumer packaged goods.<sup>1</sup> Even more surprising is that less than 10% of fast moving consumer goods (FMCG) are branded.<sup>2</sup> For example, 2015 per capita food consumption in India was USD 303, of which only 10% was spent on packaged food while the rest was spent on fresh food, according to Goldman Sachs. Meanwhile, the number of Indian households with annual income of at least INR 240,000 (USD 3,500) is predicted to rise to more than 60 million by 2020, from 33 million households in 2015, assuming India's gross domestic product (GDP) grows at 6.1% CAGR during that period.<sup>3</sup>

India's consumer growth will be driven not only by per capita consumption growth but also by consumers trading up from unbranded to branded goods. The topline story and our in-country channel checks have renewed our conviction that it is a great time for new brands and consumer categories in India.

<sup>1</sup> Industry Experts, Mirae Asset Global Investments (2016)

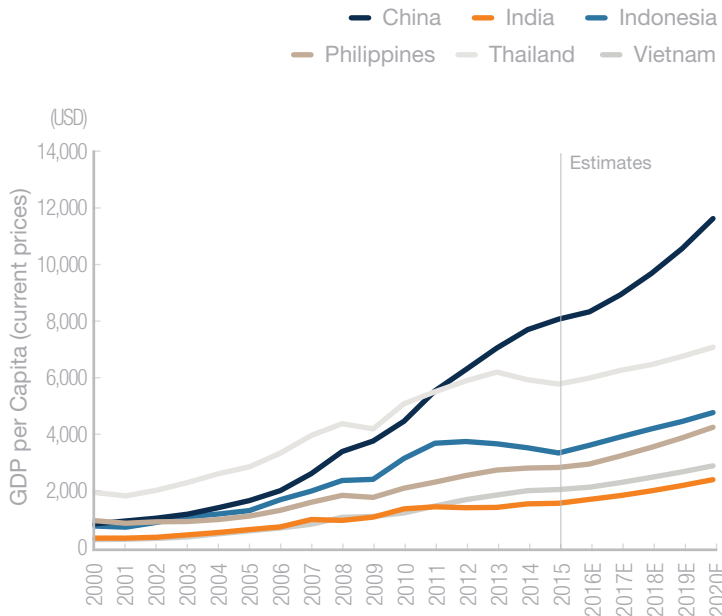
<sup>2</sup> Industry Experts, Mirae Asset Global Investments (2016)

<sup>3</sup> UBS Investor Conference; Mumbai, India (2016)



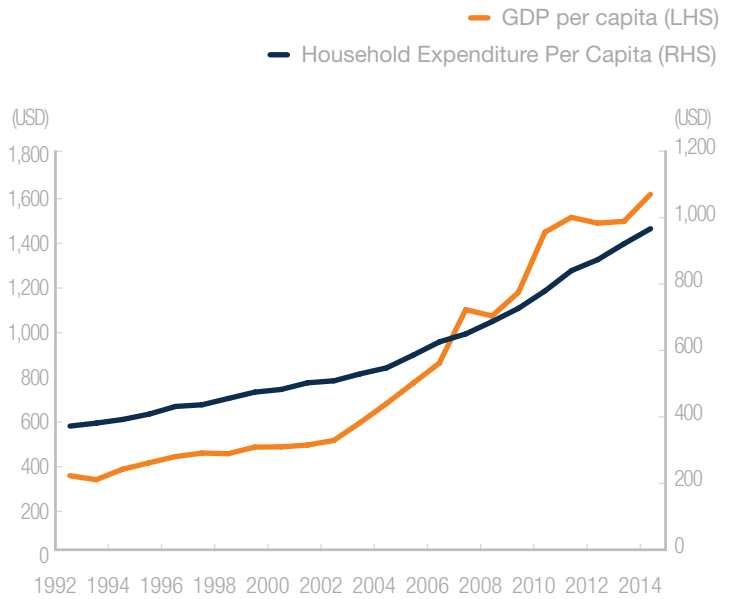
## The Indian Elephant...

Source: International Monetary Fund, World Economic Outlook (April 2016)



## ...Awakens from its Slumber

Source: World Bank, International Monetary Fund, Mirae Asset Global Investments (2016)



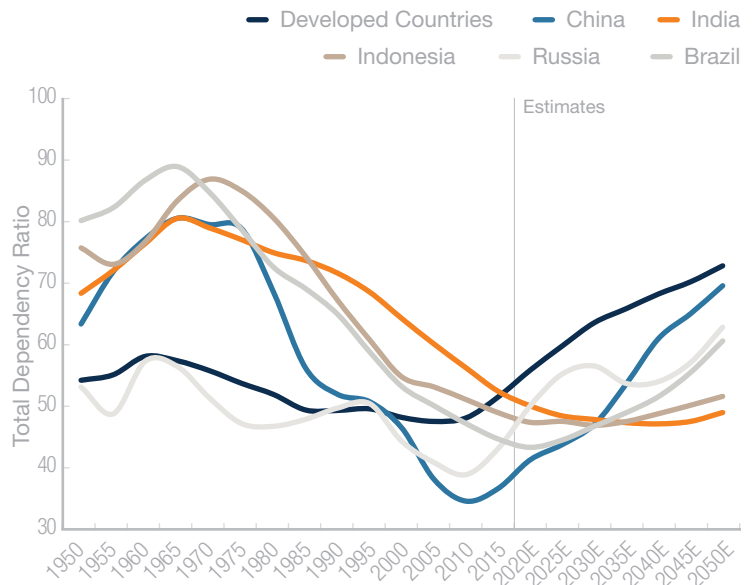
## A Rapidly Changing Market

India is young with 440 million Millennials and 390 million in Generation Z (born in the 1990s and early 2000s).<sup>4</sup> These young people may have small wallets, but they have huge aspirations. Young Indians are not adopting their parents' brands and are eager to try new products and brands. Consumer companies need to remain relevant for young consumers through innovation. In developed countries, innovation can take some time because brands need to get onto the shelves of major retail outlets before they can reach consumers in large scale. Global brands have been reducing their number of products while traditional retailers are downsizing their store sizes.

India is the exact opposite. The branded consumer market is at an early stage of development, thus innovation is a key factor for success for consumer companies. Some local companies are

## Preferential Working Population of India

Source: United Nations, World Population Prospects: The 2015 Revision



<sup>4</sup> United Nations, World Population Prospects: The 2015 Revision



doing a good job of it. For instance, Godrej Consumer Products' innovation rate\* doubled from 7% to 14% in three years.<sup>5</sup> Patanjali Ayurved is a unique example of taking something old – India's traditional holistic healing system – and turning it into new, branded products. There are many excellent consumer companies in India with a high return on capital and a dominant position in their respective categories. Godrej is a dominant leader in household insecticides, while Marico leads the coconut hair oil market, and Colgate Palmolive (India) dominates oral care.

From a corporate perspective, private companies and multi-nationals have underpinned consumer sector growth without much direct government support. India's high cost of capital has led companies to be more disciplined in making investment, compared with those in China. Indian companies also tend to avoid head-to-head product competition with each other, enabling a greater variety of category leaders, who in turn are more profitable than if they were in direct competition. Another key factor in their high return on capital is that they make their money through working capital, not margins. They have a low asset base because many use outside suppliers, and even help their suppliers cut costs and share the savings.

India's fragmented retail structure also gives brands greater bargaining power. Organized retail accounts for only 8% of India's market, due to restrictions on foreign direct investment (FDI) and the low 33% rate of urbanization, although this can be as high as 40% in big cities such as Bangalore and Gurgaon.<sup>6</sup> We expect competition will increase with category and product proliferation, but there is still room for new entrants to share in the growing pie.

## The Rise of Rural Consumers

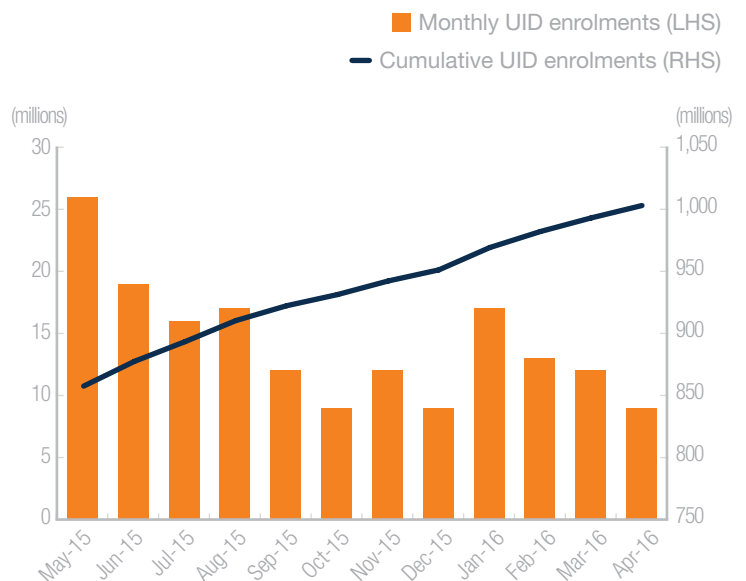
India's rural population is catching up with their big-city neighbors in terms of spending power. In 2007 the government hiked the minimum support price (MSP) and implemented National Rural Employment Guarantee (NREGA), the 100-day household

employment guarantee scheme to support rural citizens. This helped accelerate rural income growth to 8.1% CAGR from 2007-2012, up from 4.0% before the changes, putting it just behind urban income growth, which remained at about 8.5% CAGR.<sup>7</sup> The rural consumption growth rate was 1.5-2.0 times that of urban growth during this period. Since then, rural and urban consumption have grown roughly at the same rate.

It hasn't been all smooth sailing for rural Indians. Firstly, rural inflation has been higher than urban inflation due to market structure, poor transportation and oil benefits that have not been transferred. Secondly, rural government spending, particularly on NREGA, has slowed since the Modi administration came to power in 2014. Thirdly, lower agricultural prices and a drop in export volumes have hit farm incomes, while two consecutive years of poor monsoons resulted in low yields. The agricultural sector employs nearly half of India's workers and its products are the country's fifth largest export category, so the impact was widely felt.<sup>8</sup> The fourth and final blow against Indian consumption has been the slowdown in construction and its accompanied ripple effects, which has undermined job creation.

## Unique Identification (UID) for 87% of Population

Source: UIDAI, IIFL Research (April 2016)



<sup>5</sup> Company disclosures, Mirae Asset Global Investments (2016) \* Innovation rate denotes new product launches

<sup>6</sup> World Bank (2016)

<sup>7</sup> Ministry of Finance, Government of India (2016)

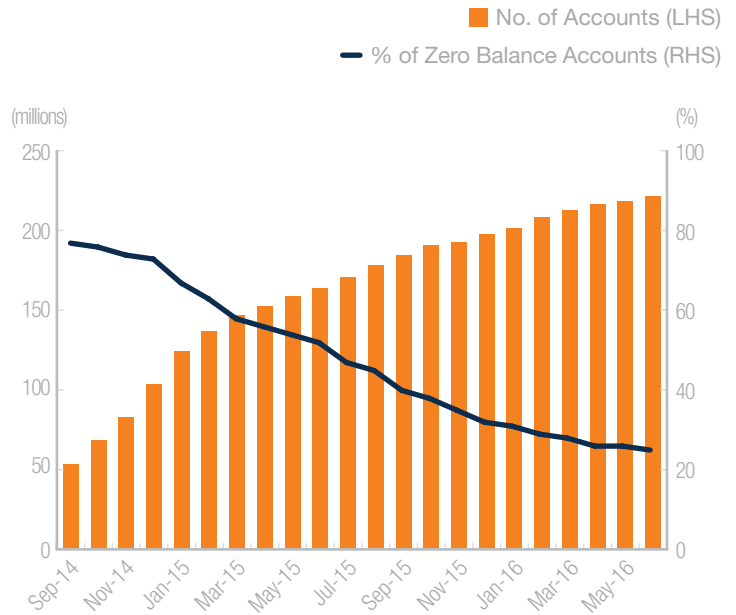
<sup>8</sup> Ibid



The Indian government remains focused on productivity improvement, which, if executed well, will ensure that India remains a beacon of demand stability in today's deflationary world. Measures such as expanding Aadhar, India's identification system, to nearly 1 billion citizens helps rural financiers such as Mahindra Financial Services introduce EKYC (Electronic Know Your Customer). Equally impressive is the progress made on the government's goal of electrification for all villages by mid-2018. Further measures such as the opening of nearly 210 million bank accounts – nearly one per household – and digitizing land records and the agricultural sector through the online National Agriculture Market will all encourage consumption in India's semi-urban and rural areas.

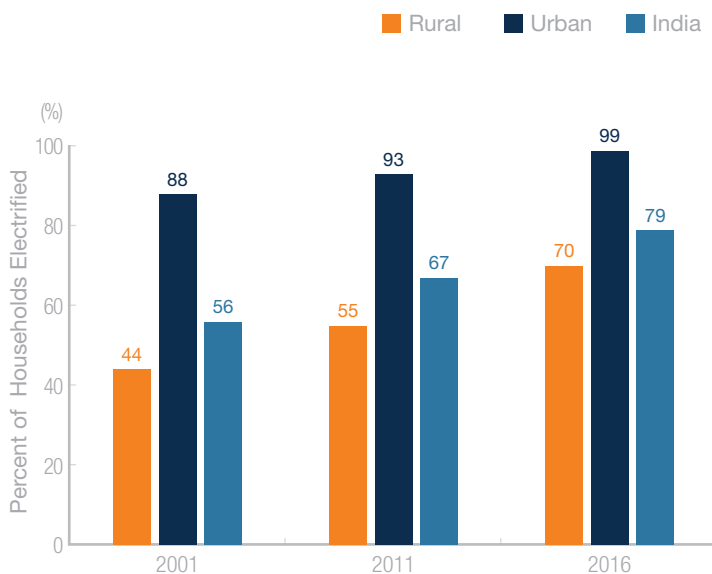
### Substantial Gains in Banking Penetration

Source: pmjdy.gov.in, Credit Suisse, Mirae Asset Global Investments (2016)



### Electrification: Remarkable Progress

Source: Census 2011, State Budget Speeches, Credit Suisse (June 2016)



### Facing up to the Challenges

The urban economy is still constrained by weak wage growth due to manufacturing overcapacity, and demand for consumer goods produced by listed companies is also being undermined by the growth of largely unlisted e-commerce companies. India's biggest challenge is to create nearly 10 million jobs a year to keep its young people employed. The IT sector, traditionally a strong employment generator, has matured to 10% growth levels in terms of revenue. Financial services have become less labor intensive due to automation.

National and state governments are also under pressure to attract FDI to kickstart the investment cycle. The central government has launched a competitiveness index to rank states on ease of doing business in order to foster healthy competition.

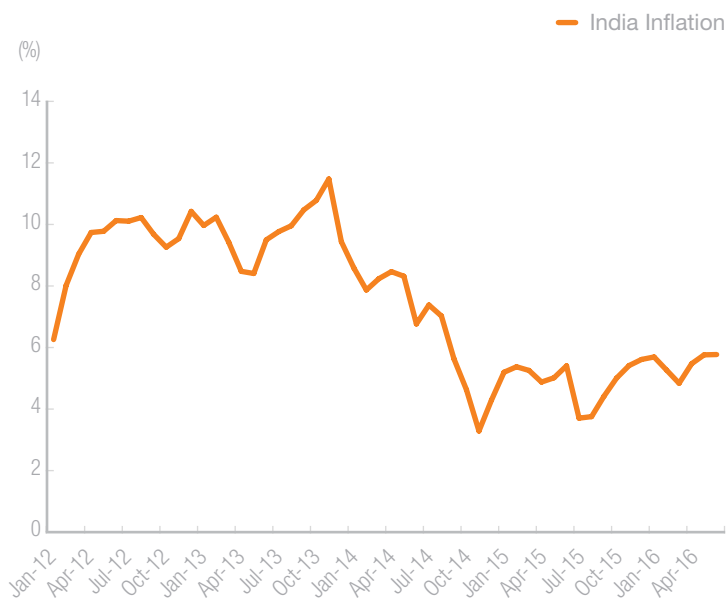
It appears to be working, if an anecdote from Maharashtra State is any indication. The state's Chief Minister Devendra Fadnavis courted Foxconn management for a USD 5 billion investment by offering them fast-track clearances while taking pains to keep negotiations secret from other competing states — the sort of story previously heard only in China.

## New Initiatives Produce Results

While the Indian growth story has slowed, monetary easing, a rise in government expenditures and a fall in inflation have helped put growth back on track in recent quarters. Consumer product companies tell us they have seen an improvement in demand since last October's festive season, although the recovery remains volatile. Good monsoons and the passage of the GST Bill should help rekindle the economy.

## India CPI Inflation Under Control

Source: Bloomberg, Mirae Asset Global Investments (2016)



Our portfolio companies, including Godrej, automaker Maruti Suzuki, food company Britannia Industries and watchmaker Titan Industries have been consolidating their position by focusing on product innovation, deeper channel penetration and better consumer engagement through social media and e-commerce channels.

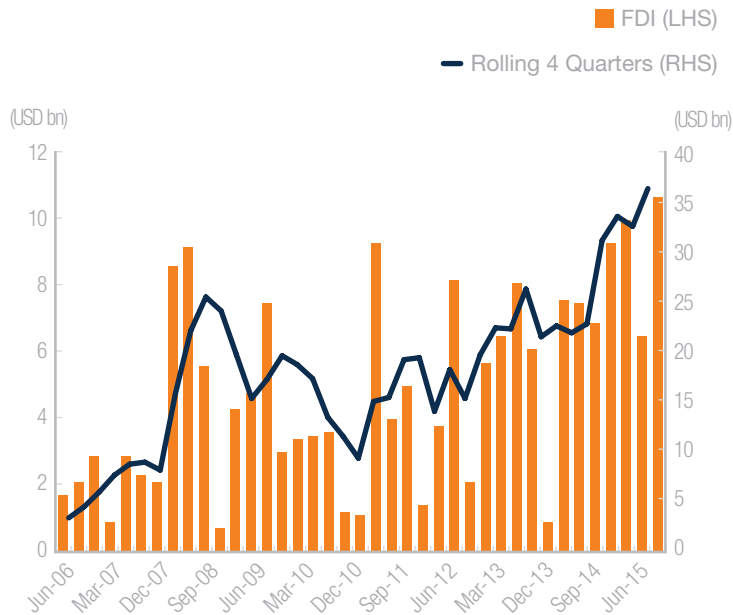
For the urban Indian consumer, the biggest respite comes in the form of lower inflation, which has nearly halved to 5% while the introduction of the 7th Central Pay Commission should boost salaries for government employees. Imminent measures such as scrapping commercial and passenger vehicles that are more than 10 years old will also generate replacement demand.

Another key initiative in increasing FDI is the “Make in India” program spearheaded by Indian consulates around the world. India's FDI was up nearly 50% to USD 55 billion in FY16 (April-March) through investments in e-commerce, car hailing apps such as Uber and Ola and smartphone and automobile manufacturing. However, a lot more needs to be done for GDP growth to be sustained at 7% for next five to seven years.

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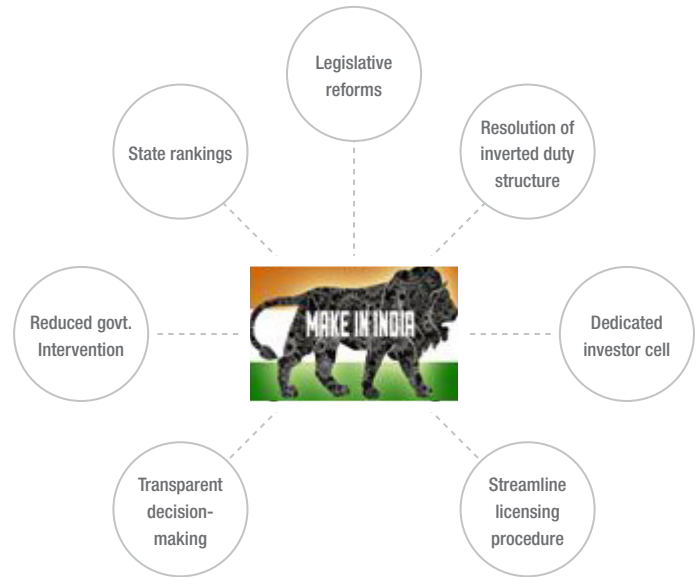
## FDI Net Inflows at Record High Level

Source: RBI, Credit Suisse, Mirae Asset (June 2016)



## Holistic Make in India Campaign

Source: Mirae Asset Global Investments (2016)



## Consumers Create Opportunity

India is not without its challenges, but the government has put in place many new initiatives to modernize and improve the economy, and the results have been positive. Importantly, India's rural population is becoming part of the growth story rather than holding back the country's progress. Rising incomes and low brand penetration will continue to give Indian consumers more choice and buying power, and with each rupee they spend they create new opportunities for businesses and investors alike.



## Global Offices

### Mirae Asset Global Investments

East Tower 26F, Mirae Asset CENTER1 Bldg,  
67, Suha-dong, Jung-gu,  
Seoul, Korea (100-210)  
Tel.+82-2-3774-8200

### Mirae Asset Global Investments (HK)

Level 15, Three Pacific Place, 1 Queen's  
Road East, Hong Kong, HK  
Tel.+852-2295-1500

### Mirae Asset Global Investments (UK)

4-6 Royal Exchange Buildings,  
London, EC3V 3NL, United Kingdom  
Tel. +44-20-7715-9900

### Mirae Asset Global Investments (USA)

1350 Avenue of the Americas,  
33<sup>rd</sup> Floor, New York, NY, 10019, USA  
Tel. +1-212-205-8300

### Mirae Asset Global Investments (Taiwan)

6F, NO. 42, Sec.2 Zhongshan N. Rd.,  
Taipei City 10445, Taiwan (R.O.C)  
Tel. +886-2-7725-7555

### Mirae Asset Global Investments (India)

Unit No. 606, 6th Floor, Windsor Building  
Off. C.S.T Road, Vidyanagari Marg.  
Kalina, Sanatacruz (East), Mumbai  
400 098, India  
Tel. +91-22-6780-0300

### Mirae Asset Global Investments (Brazil)

Rua Olimpíadas, 194/200,  
12 Andar, CJ 121, Vila Olímpia  
São Paulo, CEP 04551-000, Brazil  
Tel: +55-11-2608-8500

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