

Investment Note



14 March 2017

Investment note: India State Election Result Update

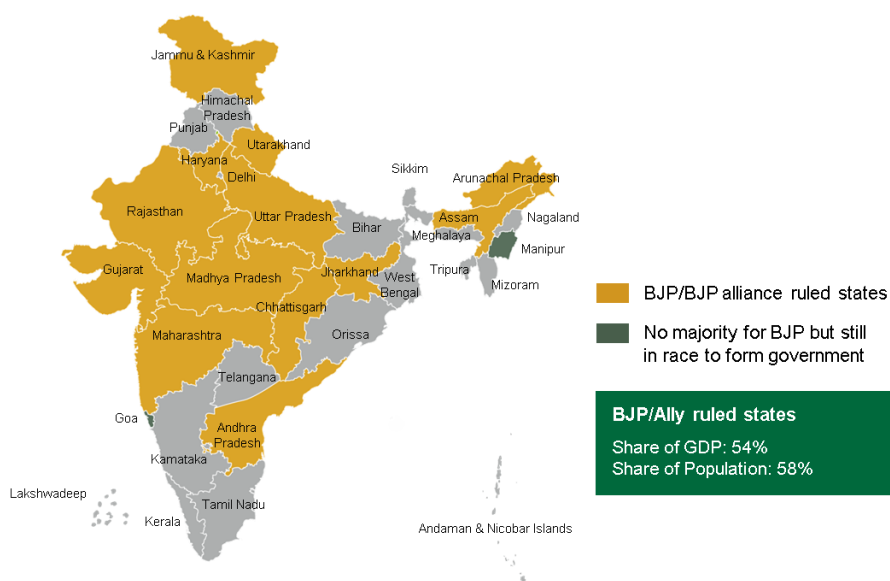
Recently, results from State Assembly elections in India were announced. Prime Minister Modi and his Bharatiya Janata Party (BJP) outperformed expectations by winning in Uttar Pradesh, as well as placing high in other state elections. Manulife Asset Management Indian equities specialist Rana Gupta believes the BJP's performance will help strengthen policy continuity and improve Modi's and the party's position for central government elections in 2019. The results affirm our existing investment convictions in financials, sectors with a large informal business presence, and infrastructure.

There are three main takeaways from the recent Assembly elections.

The ruling BJP in the ascendant

The BJP, the ruling party of the central government, surprised analysts by winning more than 80% of seats, a thumping majority in Uttar Pradesh (UP): India's largest state and a politically important one. BJP also won the neighboring state of Uttarakhand. Although the BJP did not emerge as the single largest party in other state assemblies such as Goa and Manipur, it will help form a state government in these states with the help of political allies. The opposition National Congress Party won Punjab. Overall, 54% of India's GDP and 58% of India's total population will be under a BJP-led state government. This is the first time since the 1990s that a single political party in India has ruled the central government and this many state assemblies.

A thumping victory for the BJP in India's state election¹



¹ Source: Manulife Asset Management, CLSA, March 2017.

India's policy continuity strengthened

Although the BJP was expected to do well in the Assembly elections, the scale of victory exceeded expectations. Indeed, the BJP's performance will cement Prime Minister Modi's authority in the party and government. It will also be positive for the implementation of the central government's agenda of anti-corruption policies, indirect tax reform, and state spending on infrastructure/ housing/ rural development.

This augurs well for policy continuity, as the government will have no elections for the next eighth months- this will be a crucial time period for implementation. Political experts forecast that with substantial momentum behind the BJP, it looks like they will retain a majority in the central government election to be held in 2019.

Investment convictions re-confirmed

We remain constructive and overweight on our favorite investment themes.

First, we see increased household savings being put in financial institutions due to positive real interest and government efforts to formalize the economy (increasing banking through digital, demonetisation, indirect tax reform). Sectors that will benefit from these trends include: mid-sized banks, insurance companies, and wealth and asset managers.

Second, we see the formalised sectors of the economy gaining market share from the informal sectors due to formalisation policies. Sectors that will benefit from this trend include: food, jewellery, apparel, light electricals where the informal sector used to play an outsized role.

Third, continued government focus on infrastructure investment. The cement sector will be the main beneficiary of this trend.

Overall, we will continue to watch for the introduction of populist policies in the run up to the central government election in 2019. Although it is not our base case, given the economic stress present in rural India, the possibility cannot be ruled out. We are currently underweight on sectors linked to rural demand, but we will continue to assess this position if there are new policy developments.



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