2008

GREENWICH ADVISORS

[NOT ANOTHER BRIC IN THE WALL]

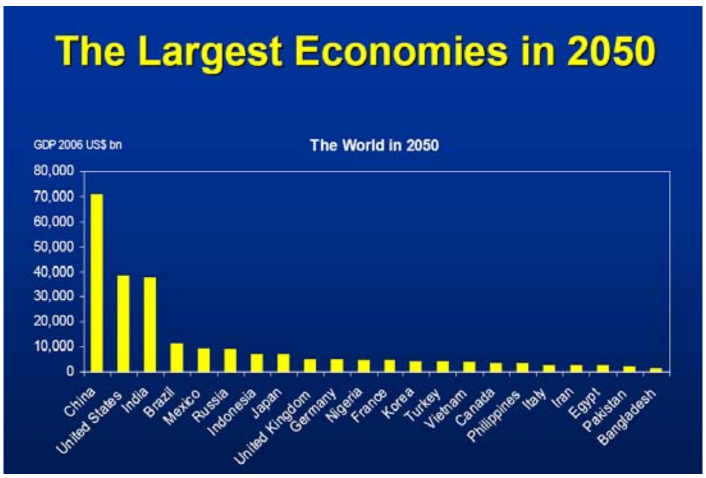
[By: Suhas Kundapoor, Portfolio Manager Greenwich Advisors India Select Fund, January 10, 2008]

Not Another BRIC in the Wall

India's Rise Above the Rest

It is widely accepted theory among economist that the 21st century is going to be a BRIC century, and will see the emergence of not one but four economic powers. But does this mean that the components of BRIC (Brazil, Russia, India, and China) all offer the same level of opportunity over the next few decades? The answer is decidedly no.

Goldman Sachs coined the acronym BRICs to describe the combined economic potential of these four emerging powers. However, in terms of sheer size and potential for growth, the four economies are very different.



Graph 1

"China, India and the New Balance of Economic Power" Jim O'Neill, Managing Director and Head of Global Economic Research, Goldman Sachs – Presentation, May 2007

According to Goldman Sachs' projections, the Gross Domestic Product (GDP) of China and India are expected each to exceed $25 trillion by 2050, making them about 5 times larger than those of Brazil and Russia. In terms of real growth, however, India is expected to outperform all of the other BRIC nations: over the next 40 years, India's economy is projected to grow an impressive 5% per annum. As noted in the 2004 Goldman Sachs study, "One highlight of our findings was the remarkable and largely underappreciated growth potential for India. While investors and corporations have focused intensively on China, India could potentially be a bigger growth story over the long run." [1]

Three Megatrends make India the most exciting BRIC country today from our point of view. These trends are:

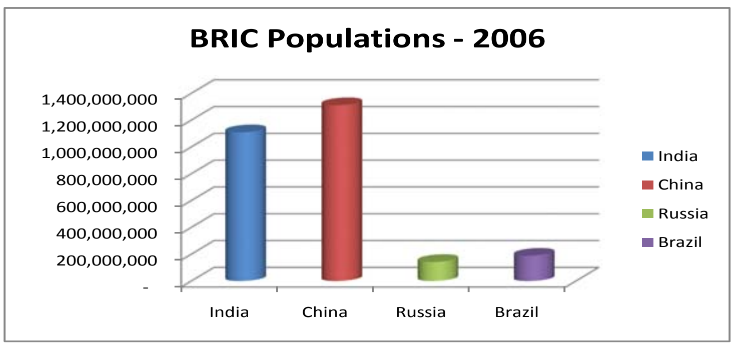
- Demographics

- Consumer Spending
- Capital Infrastructure

When you look at this list you will notice that India's growth is expected to be driven by factors very similar to those that made the United States an economic powerhouse in the 20th century, which is why we think India is a country worthy of special attention now.

Demographics

In sheer size, India and China are about 5 times larger in population than the next largest BRIC country, Brazil, giving their economies large captive markets, a necessary requirement to creating economic powerhouses.

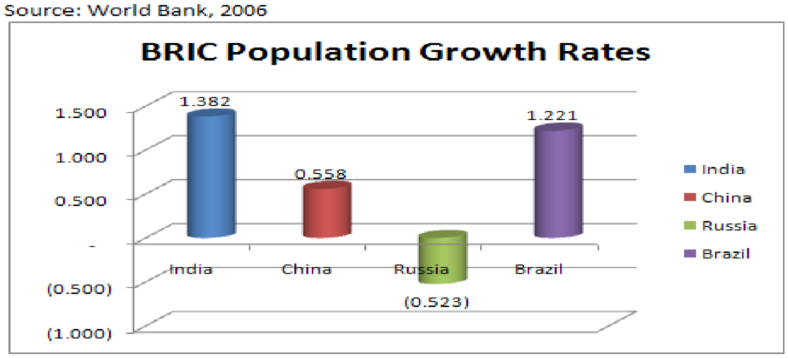


Graph 2

Source: World Bank, 2006

However, significant population growth is now seen only in India and Brazil. Population growth in these

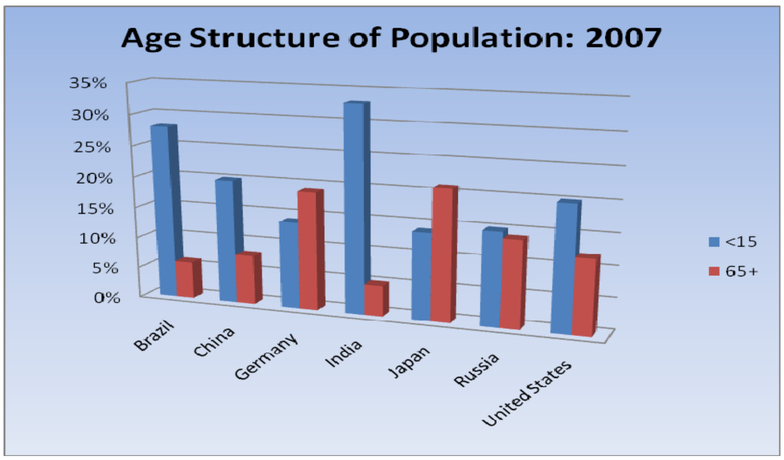
Source: World Bank, 2006



Graph 3

two nations is exceeding 1% per year, with India's growth rate the greatest in both percentage increases and on an absolute basis. While the population in China is still the largest in the world, China's growth rate is slowing down quickly due to its "one child" policy, and Russia is actually experiencing negative population growth. These slowdowns in population growth translate into rapidly aging populations for both China and Russia. On the other hand, Brazil and especially India have very young populations, a typical precursor to strong economic growth.

According to 2007 Population Reference Bureau data, India has the smallest percentage of people aged 65 and over among BRIC nations. Russia clearly has an aging population, with the largest percentage of people over age 65 (15%), followed by China with 8%. Both China and Russia thus have a built-in demographic problem that is expected to create a shortage of workers in the future – an important prerequisite to support economic growth. On the other hand, more than 33% of India's population is below age 15. As a result, India is expected to see a surge in the working age population over the next few years, which should have a positive impact on savings rates and consumption.



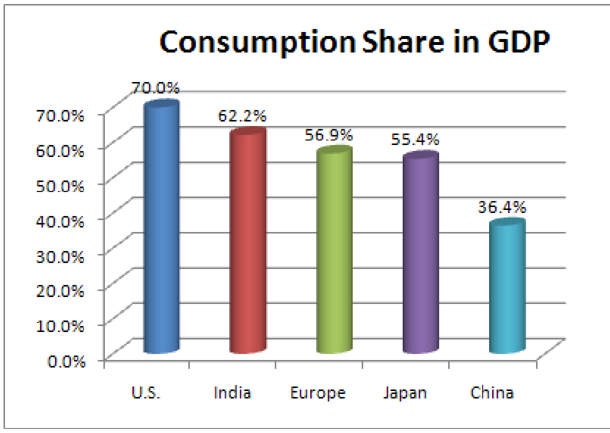
Population Reference Bureau, 2007 World Population Data Sheet Graph 4

India's "Baby boomers" are just now coming of age, and like the U.S. in the 50's and 60's this is expected to be a significant propellant for economic activity. In short, India has both the smallest percentage of people over age 65 and the largest percentage of people under age 14 among the emerging BRIC nations, creating an ideal demographic scenario for future economic growth.

Consumer Spending

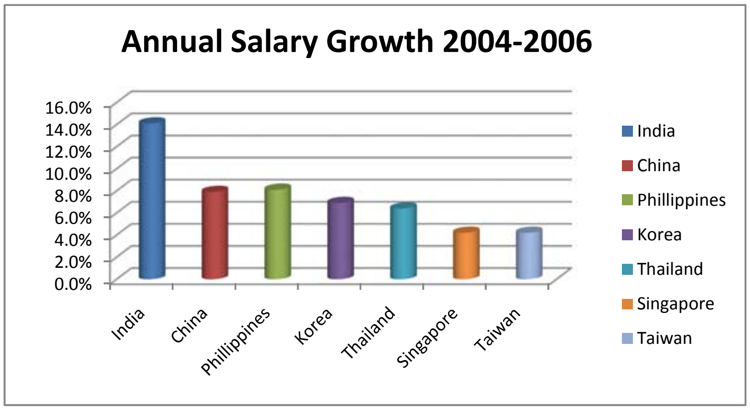
One of the key differences between the rise of America and the other economic powerhouses of the 20th century, like Japan, was the fact that America's GDP and its economic growth were driven primarily by consumer spending, which allows for longer term and more self- dependent growth.

Growth in China is largely driven by manufactured exports, while GDP growth in Brazil and Russia are mostly driven by commodities exports. In contrast, India's GDP construct is very similar to that of the United States. Notwithstanding apocryphal reports on outsourcing and services driving GDP growth in India, a large percentage of India's expected long-term economic growth is expected to come from local consumer spending. India's consumption share in GDP is among the largest in the world: it is larger than Japan and Europe and second only to the United States.



Source: Morgan Stanley Research, June 2007

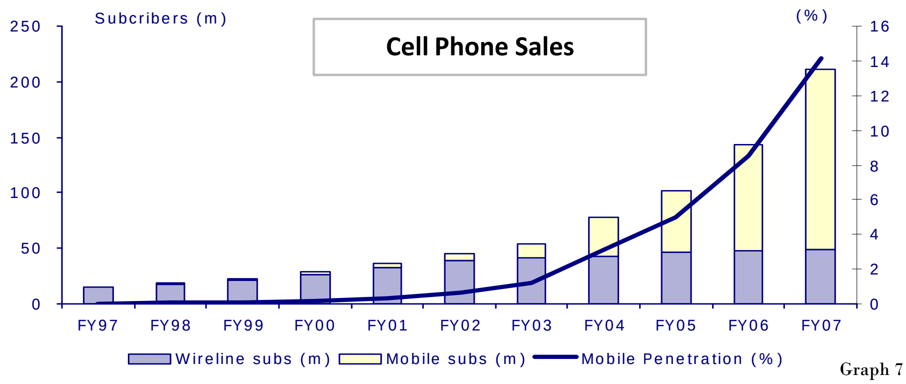
This is a particularly compelling statistic when coupled with the fact that salary growth in India is one of the fastest of any BRIC country, and roughly twice that of China.



Source: International Business Times, May 2006

Graph 6

These factors create a rapidly expanding middle class that is expected to spur on future GDP increases generally. But there are many subtleties that must be considered as one analyzes how expected consumption growth will impact specific industries. After all, "middle class" is a relative term that is understood in the context of an entire population. As an example, mobile phone penetration is expanding swiftly in India. In the United States the market could be considered saturated, but in India it is just beginning its product cycle. Thus, despite rapidly growing salaries, cell phone market penetration rates are still very low, and are set to increase quickly from what is currently a very low base.



Graph 7

Source: Deutsche Bank, June 2007

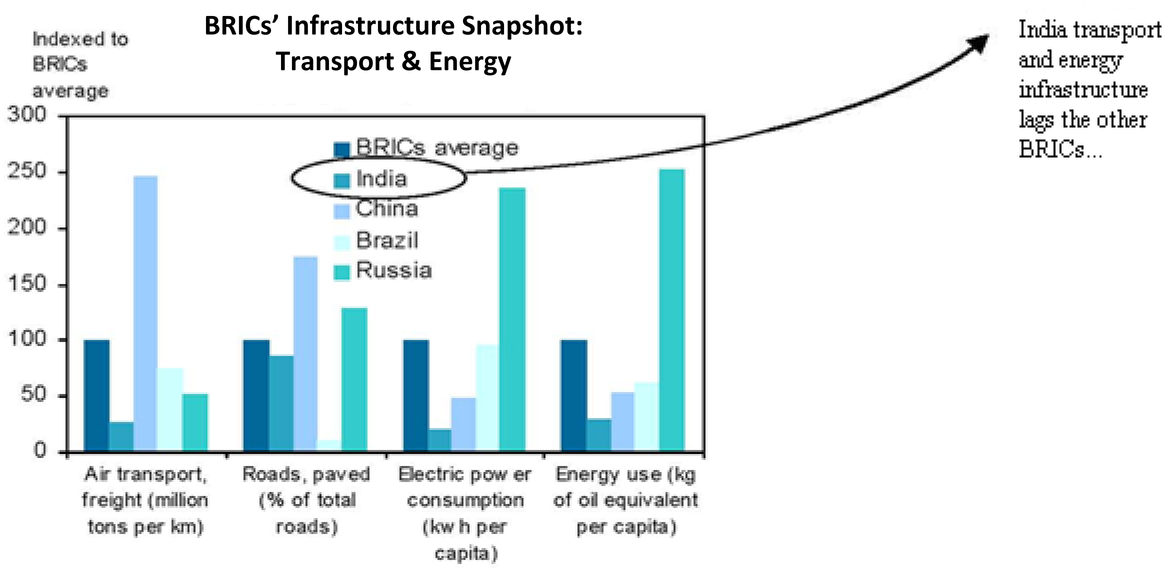
Despite booming cell phone sales (India is one of the fastest growing markets for cell phones) more than 4 in 5 Indians currently do not own a cell phone

Capital Infrastructure

Among the BRIC countries, India's transportation and energy infrastructure lags the other BRIC economies. In our view this makes India possibly one of the most exciting macroeconomic plays among the BRIC countries.

At first glance this view may seem to be counter-intuitive. However, GDP growth typically lags infrastructure investments, and the best time to invest in an economy is usually just before major investments have been made. China, and to a lesser extent Brazil and Russia, have already benefited from sizeable infrastructure investments. In many ways this is what makes the BRIC economies attractive, but India may be better positioned to benefit economically due to the return on investment (ROI) of its future infrastructure spend.

It is important to note here that India's growth thus far has come in spite of, rather than due to, its infrastructure. The government of India has planned an outlay towards infrastructure of about $500 billion over the next 5 years [2], which is by far its most ambitious expenditure dedicated to modernization. Again, it is worthwhile to show the parallels to the United States in the 1950's. India's infrastructure outlay is similar in relative magnitude to that made during the Eisenhower presidency. Ultimately, this infrastructure investment was a significant driver of America's economic growth for decades. Utilizing a proven macroeconomic blueprint, India's unprecedented planned investment is purposely mimicking the American strategy of the Eisenhower era and should serve as a catalyst for future growth.



Source: BRIC Layers, Issue No: 05/03, 1st March 2005, Goldman Sachs

Graph 8

BRICs are garnering more attention by the media and by institutional investors looking for growth. With its youthful population and expanding workforce, growth in salaries and consumer spending, and its commitment to infrastructure investment, India is a fascinating part of the BRIC growth story that deserves consideration as you look strategically at building any growth-oriented portfolio.

1- Dreaming with BRICs: The Path to 2050 Goldman Sachs 2003

2- http://www.ciionline.org/full_story.php?menu_id=79&news_id=811, Confederation of Indian Industries, November 15, 2007

3- Bloomberg, November 2007

Graphs:

1. *"China, India and the New Balance of Economic Power", Presentation by Jim O'Neill, Managing Director and Head of Global Economic Research, Goldman Sachs, Slide 8, May 2007*

2. *World Bank, 2006*

3. *World Bank, 2004*

4. *Population Reference Bureau, 2007 World Population Data Sheet*

5. *Morgan Stanley Research, June 2007*

6. *International Business Times, May 2006*

7. *Deutsche Bank, June 2007*

8. *BRIC Layers, Issue NO: 05/03, 1st March 2005, Goldman Sachs*

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