

The risks are rising for India

The long-term story is compelling, but after a spectacular bull run, warning signs are starting to show



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“India: too expensive or the world’s best growth story?” asked one of the attendees during the emerging-markets session at MoneyWeek’s reader conference earlier this month, concisely summing up the dilemma for investors. India has one of the simplest and most compelling narratives of any long-term bull market: young demographics, vast potential for catch-up growth, unusually large and high-quality stockmarket by EM standards, and a record of considerable progress in recent years. Yet it’s still hard to feel entirely comfortable about paying 25 times earnings for it.

This is not a new dilemma. India has long been an expensive market relative to peers. The chart shows the price/earnings ratio for the broad market stretching back almost 30 years: ignore the trough and spike in 2020/2021 – caused by the pandemic panic and subsequent impact on earnings – and note that the market actually looks cheaper than it did at the end of the last decade, even though it has more than doubled since then. It has rarely dropped below 15 since the start of the 2000s, meaning that it has usually been at the upper end of the EM peer group.

There have been weak patches, accompanied by the kind of events that always worry EM investors: the market struggled in the early 2010s amid high inflation and a series of political and corruption scandals, and again towards the end of the decade amid a sharp economic slowdown and problems in the shadow banking sector. Yet in both cases, earnings growth eventually came through and the market went on to new highs.

A few warning signs

Still, there are growing reasons to wonder if another tricky spell could be on the way.

India always looks expensive

Trailing price/earnings ratio for Nifty 500



The government did unexpectedly poorly in the general election in June, which could hurt the prospects for further economic reforms. Company earnings suggest that weak consumption growth is spreading from the rural poor (who have benefited least from the boom of the last few years) to urban residents – exactly the opposite of what we would hope to see. Rising delinquencies at microfinance lenders may be a sign the credit cycle is souring. Now the decision by US prosecutors to lay bribery charges against billionaire Gautam Adani (see page 10), a close ally of prime minister Narendra Modi, recalls those early 2010s scandals that helped shuffle the previous government out of power.

It’s impossible to say what the consequences of the Adani case will be. There is no prospect of him facing any direct legal risks within India. However, the country depends heavily on a handful of large business groups, of which Adani’s is the newest, to undertake major projects. This requires a lot of foreign capital. The charges may make it harder for Adani to raise funding overseas and potentially affect the speed and cost of financing for other projects as well. Less investment will hinder growth. That may mean weaker earnings, which would surely take some momentum out of the market. It’s too soon to call the top, but after such a strong run, the odds of a setback are clearly rising.