



Discretionary Consumption – A Structural Growth Opportunity

India has been a consumption-led economy for multiple decades (currently running at around 59% of GDP) and this is unlikely to change over the next few decades given the drivers in place.

The continuing strength in consumption can be attributed to a mix of socioeconomic factors including the demographic dividend, with declining age dependency, and a steady rise in per-capita income. In addition, rapidly emerging organized retail formats, digital and technology adoption including the ONDC, rising urbanization and increased access to financing are reorienting the consumption basket.

While the share of discretionary items in India’s consumption basket has risen over the past two decades, it still remains significantly below the global average. As is typical of most low-income countries, the Indian consumption basket today is dominated by food and other essentials. However, with rising per capita income, increasing urbanization and enhanced access to credit, the structural drivers are in place to further accelerate the shift towards discretionary spending.



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Chief Investment Officer

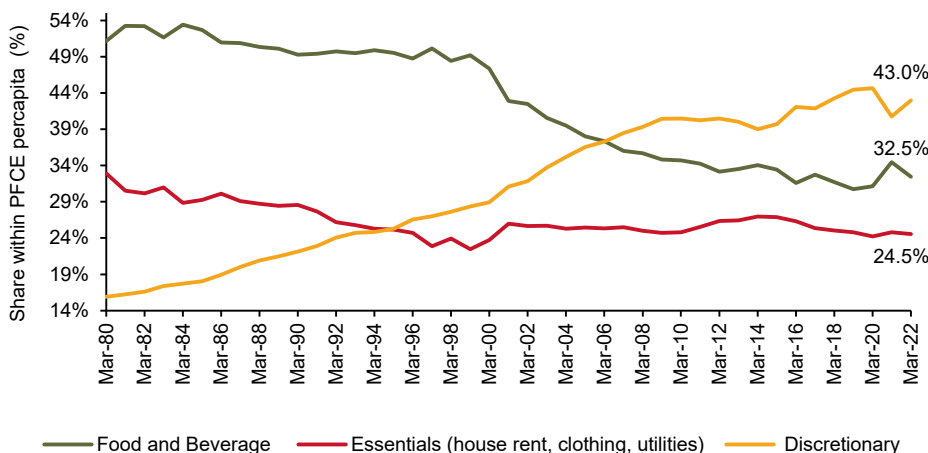


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Share of Discretionary Categories Rising in India



Source: ISec

Indian Retail Basket: Discretionary spends to outpace staples

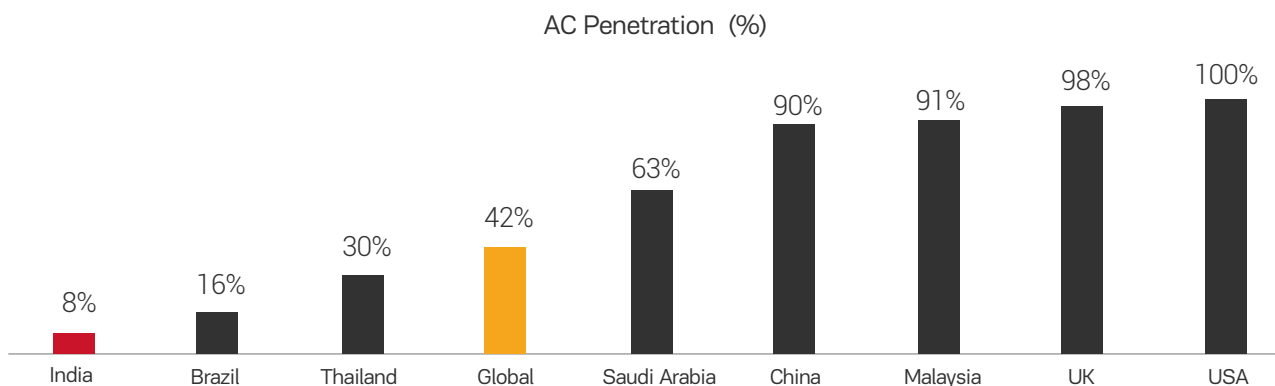
	Retail size (US\$bn)			Share (%)			CAGR
	FY15	FY20	FY25F	FY15	FY20	FY25F	FY15-25F
Food & Grocery	328	526	681	66.6%	66.1%	63.3%	7.6%
Jewellery	36	60	91	7.3%	7.5%	8.4%	9.7%
Apparel & Accessories	41	66	100	8.4%	8.3%	9.3%	9.3%
Footwear	6	10	14	1.3%	1.2%	1.3%	8.8%
Pharmacy & Wellness	15	23	36	3.0%	2.9%	3.3%	9.1%
Consumer Electronics	29	51	77	5.9%	6.4%	7.1%	10.3%
Home & Living	22	34	47	4.5%	4.3%	4.4%	7.9%
Others	15	26	31	3.0%	3.3%	2.9%	7.5%
Total	492	796	1,077	100.0%	100.0%	100.0%	8.1%

Source: JPMorgan

Discretionary Categories Remain Underpenetrated in India

Most discretionary categories remain underpenetrated in India.

The household penetration rate for Air conditioners, for example, is currently only at 8%, compared to the global average of 42%.

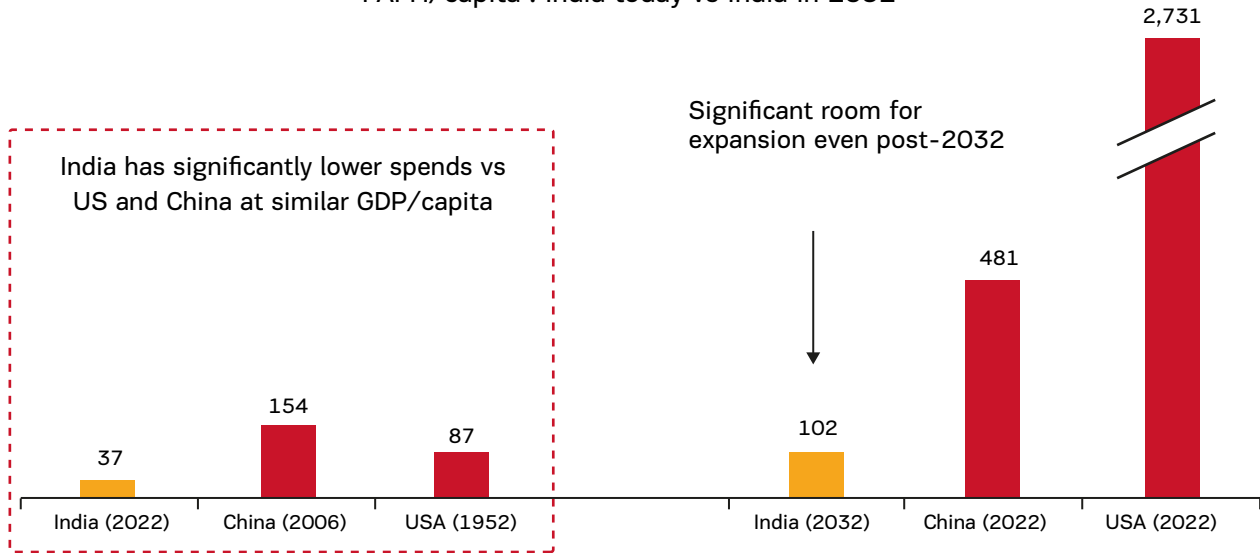


Source: ABSLAMC Research

Similarly, in the food service sector, India's per capita spending on food away from home is not only lower than in more affluent economies such as the US and China today, but lower than their per capita spends when they were at similar income levels.

India's FAFH/capita spends lags behind US and China's FAFH/capita spends at similar GDP levels, indicating a room for a much accelerated catchup over the long-term

FAFH/capita : India today vs India in 2032



Source: Euromonitor, Bernstein analysis

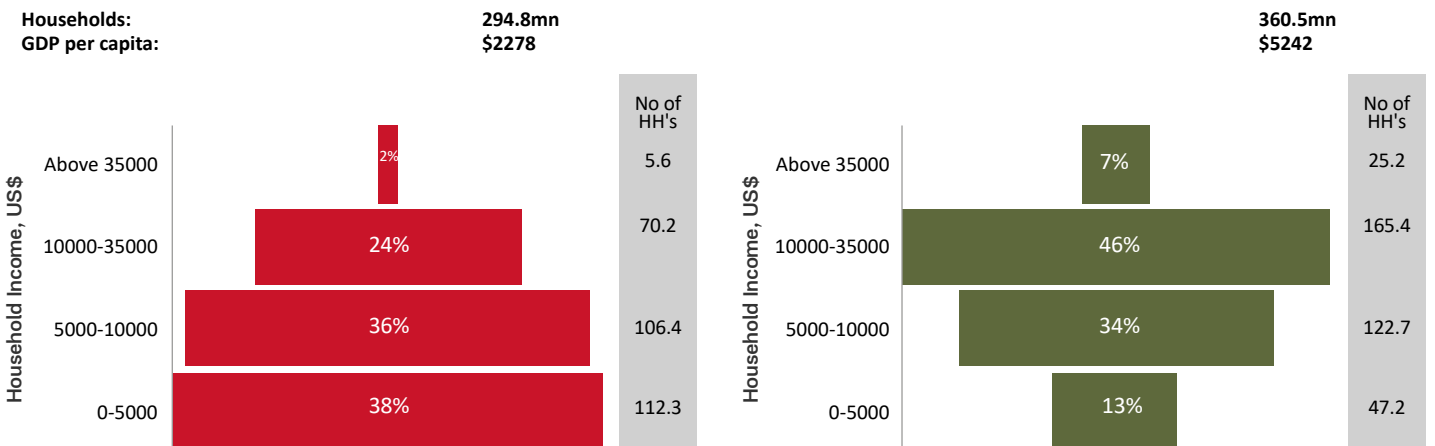
Rising income to change consumption patterns

India is projected to become the third largest economy by 2030. The number of households (HH) earning in excess of US\$35,000/year is likely to rise fivefold in the coming decade, to over 25 million.

Major shift coming in India's income pyramid

2021 Households by Income Distribution

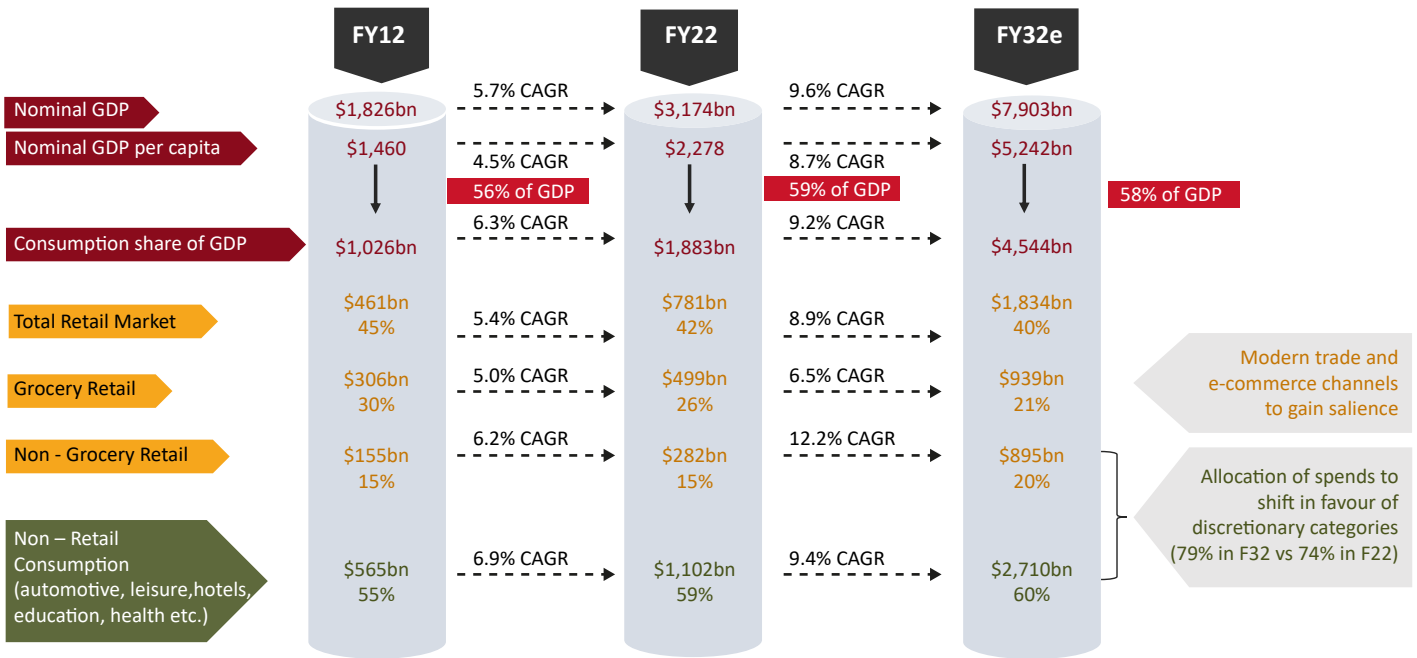
2031 Households by Income Distribution



Source: Morgan Stanley Research estimates

The breadth of India's income pyramid will lend further momentum to consumer spending, which is likely to benefit India as it crosses the crucial US\$2,500 per-capita GDP level.

A discretionary spending boom is on the horizon



Source: Morgan Stanley Research estimates

The combination of underpenetration of the discretionary consumption categories and rising income levels is likely to translate into exponential growth for these categories over the coming decade.

As overall consumption more than doubles during the next decade, non-grocery retail share in consumption is projected to rise to about 20% as compared to 15% currently (illustration above). Apparel and accessories, which is the largest retail category, is likely to see the fastest growth.

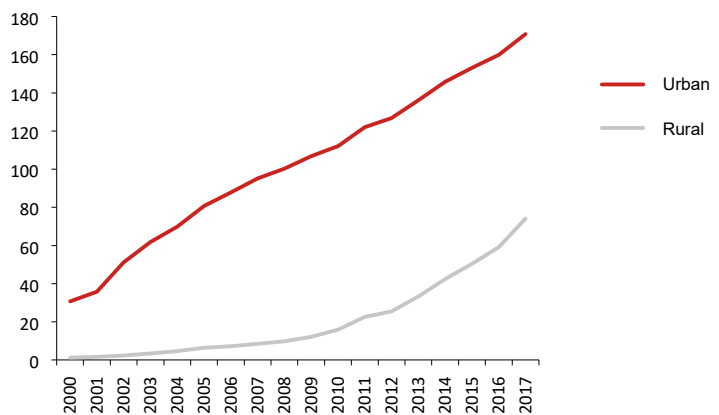
Other discretionary categories that will benefit from the income acceleration include leisure & recreation, hotels & catering, household goods & services, education, health goods, and medical services.

Urban Indian to Lead the Way

As has been seen during the rise of other major economies, in India too, the urban consumer is likely to lead the way in terms of greater penetration of consumer categories.

In the case of China, the urban consumer was at least a decade ahead of the rural consumer in terms of buying new consumer durable products such as ACs.

AC Penetration in China – Urban vs Rural



Source: Nomura

While Urbanization in India has not been as rapid as in China, it continues to occur steadily. Given that productivity gains and the consequent rise in income occur first in urban areas, it is natural that the urban consumer would be the first to spend on discretionary categories. The urban share of the population in India is set to grow from 31% in 2010 to 40% by 2030.



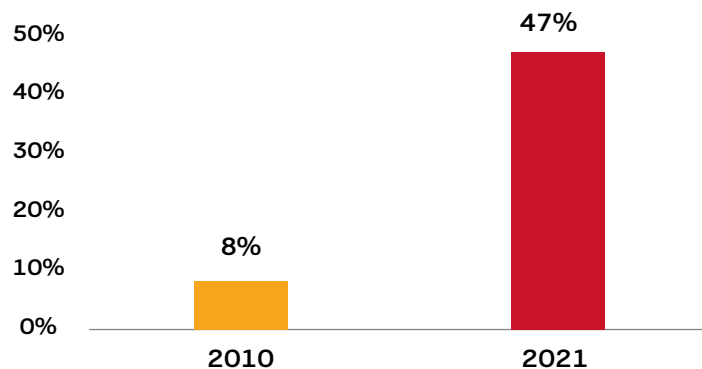
Credit Access: A Key Catalyst

Restricted access to credit has been a key barrier to the Indian middle class being able to spend on discretionary items. The Indian household sector remains one of most underleveraged in the world.

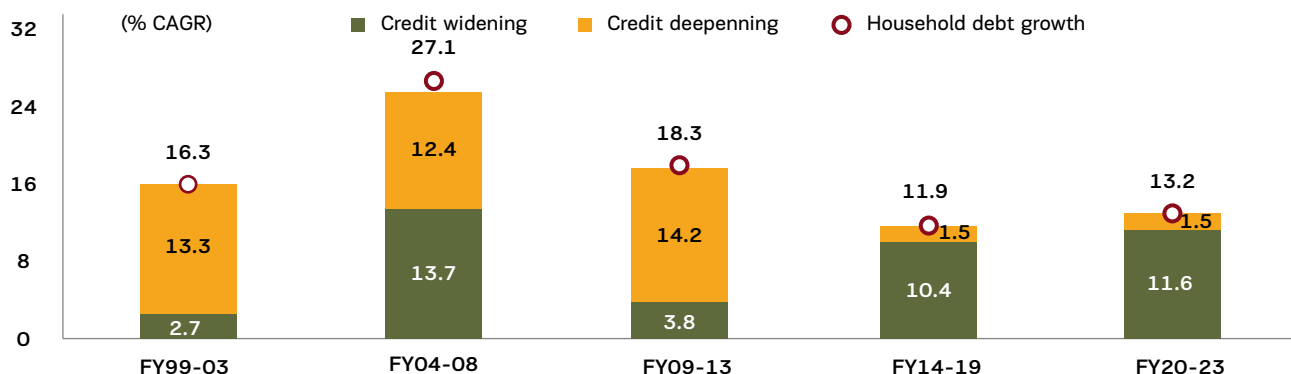
However, increasing internet and banking penetration has led to a sharp pick up in retail credit in India. During the current business cycle, it is retail credit that has been driving growth, while industrial credit remains somewhat sluggish.

Furthermore, the credit growth is coming from “credit widening” (more consumers gaining access to credit) rather than “credit deepening” (the same consumers increasing leverage). During the current cycle, 90% of the loan growth has come from credit widening, compared to only ~20% the FY99-03 and FY09-13 period. The democratization of credit is likely to be a key catalyst in increasing consumer access to discretionary consumer goods and services.

India Internet Penetration



Majority of the growth in banks' household debt was owing to credit widening in the past decade



Shift from Unorganized to Organized

Within consumer discretionary categories, the unorganized sector continues to have a significant share. However, with the implementation of GST and rising consumer aspirations, the organized sector has been gaining share at the expense of the unorganized sector. We expect this trend to continue.

Organized players to gain more salience									
	Share of unorganized retail			Shar of organized B&M			Share of E-commerce		
	FY15	FY20	FY25F	FY15	FY20	FY25F	FY15	FY20	FY25F
Food & Grocery	97%	95.5%	91.0%	2.5%	4.0%	5.0%	0.5%	0.5%	4.0%
Jewellery	73%	68.0%	60.0%	25.0%	28.0%	33.0%	2.0%	4.0%	7.0%
Apparel & Accessories	77.0%	68.0%	55.0%	19.5%	14.5%	23.0%	3.5%	17.5%	21.8%
Footwear	91.0%	70.0%	62.0%	5.5%	14.0%	15.0%	3.5%	16.0%	22.0%
Pharmacy & Wellness	95.0%	90.0%	80.4%	4.5%	7.8%	11.2%	0.5%	2.2%	8.4%
Consumer Electronics	74.0%	68.0%	55.0%	16.5%	4.7%	9.0%	9.5%	27.3%	36.0%
Home & Living	91.0%	85.0%	70.0%	7.6%	7.7%	11.0%	1.4%	7.3%	19.0%
Others	89.0%	85.0%	78.0%	10.4%	5.3%	11.0%	0.6%	8.7%	11.0%
Total	91.7%	88.1%	80.4%	7.1%	7.2%	10.0%	1.2%	4.7%	9.6%

Source: JPMorgan

India Consumer Discretionary: Segments with low-mid teens MT revenue growth potential for organized players					
Category	Category size (US\$bn)	Organized share	Penetration	Competitive Intensity	Pricing Power
Grocery Retail	526	Very Low (~5%)	High	High	Low to Medium
Jewellery Retail	60	Low (~30%)	High	Medium	High
Fashion/Apparel Retail	66	Low (~30%)	High	High	Low to Medium
Quick Service Restaurants	63	Low (~35%)	Low	Medium	Medium to High
Paints	10	Medium (~67%)	Medium	Hlgh	High
Consumer Durables	22	Medium	Low	High	Low to Medium

Source: JPMorgan

Outlook

While there may be cyclical downturns in discretionary spending, structurally, we believe the consumer discretionary space is poised for robust growth over the next decade and the urban consumer will likely lead the way.

While the growth opportunity for consumer discretionary companies remains attractive, there are also risks that the sector faces, including rising competitive intensity and increasing protectionism.

We view elevated competitive intensity in the industry as the key risk to the profit pool of the industry. Hence, high-involvement consumer categories, such as jewellery, where brand loyalty and consequently pricing power is much higher, might be better placed. Furthermore, companies benefiting from the shift from unorganized to organized, such as QSR, also look attractive.

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