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India Playbook 2024: Aiming for a trillion dollars in forex reserves by 2029

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Synopsis
India's economic trajectory for global investments is driven by stable macroeconomic environment, robust earnings growth, and significant contributions from software services and remittances. Inclusion in MSCI EM index and prominent Emerging Market Bond indices enhances India's investment landscape.

Representative image

India's economic trajectory over the next five years positions it as a prime target for global investments. This outlook is driven by a stable macroeconomic environment, robust earnings growth among Indian corporations, and increasing weightage in the MSCI Emerging Markets (EM) index. The inclusion of Indian debt in prominent Emerging Market Bond indices further enhances the attractiveness of India's investment landscape. With software services and remittances significantly contributing to foreign exchange (forex) inflows, India's forex reserves have reached unprecedented levels, setting the stage for ambitious future targets.

Capital Account Inflows and Remittances:

India's forex reserves stood at an all-time high of $646 billion as of April 1, 2024, marking an impressive increase of $68 billion from the previous year. Forex reserves have doubled in the last 10 years. A key driver of this growth has been remittances, which now exceed $100 billion annually, outpacing capital account inflows. Looking ahead, capital account inflows—including Foreign Direct Investment (FDI), Foreign Portfolio Investment (FPI) in equities and debt—are projected to surpass $100 billion annually starting from FY2025E. This surge in inflows is expected to bolster the corporate capital expenditure (CAPEX) cycle and reinforce the strength of the dollar, propelling forex reserves towards the trillion-dollar mark by 2029E. (Source: JM Financial, Kotak)

MSCI EM Index and Equity Inflows:
India's prominence in the MSCI EM index has grown substantially, with its weightage increasing from 9.2% in 2020 to 18% in 2024. In contrast, China's weightage has decreased from 39% to 25% over the same period. Despite this shift, Foreign Institutional Investor (FII) ownership in India has declined to a decadal low of 16.6%. However, this trend is expected to reverse following the upcoming Indian elections, assuming the establishment of a stable government. In such a scenario, FII flows could potentially double from $25 billion in FY2024 to US$ 50 bn in FY2025E and remain elevated for a couple of years. (Source: JM Financial, Kotak)

Debt Market Inflows:

The inclusion of Indian debt in the JPMorgan and Bloomberg EM indices has already resulted in substantial foreign inflows. FY2024 alone witnessed $15 billion in foreign debt inflows, a significant increase from virtually negligible levels in preceding years. This trend underscores the growing confidence of global investors in India's debt market. (Source: JM Financial, Kotak)

Foreign Direct Investments (FDI):

Over the past decade, FDI inflows into India have averaged $32 billion annually. Although there was a dip in FDI in FY2024, it is anticipated that FDI levels will return to their historical averages in the coming years, further supporting capital account inflows and economic growth. (Source: JM Financial, Kotak)

Government CAPEX Initiatives:

The Indian government, led by the Bharatiya Janata Party (BJP), has significantly increased its proposed CAPEX spending for FY2025E to INR 1.6 trillion. This amount equals the total CAPEX investment in FY2014, reflecting a seven-fold increase. Such robust government spending is expected to revive India's CAPEX growth, attract additional capital inflows, and stimulate overall economic development.

(Source: JM Financial, Union Budget, Kotak)

Current Account Surplus Projection:

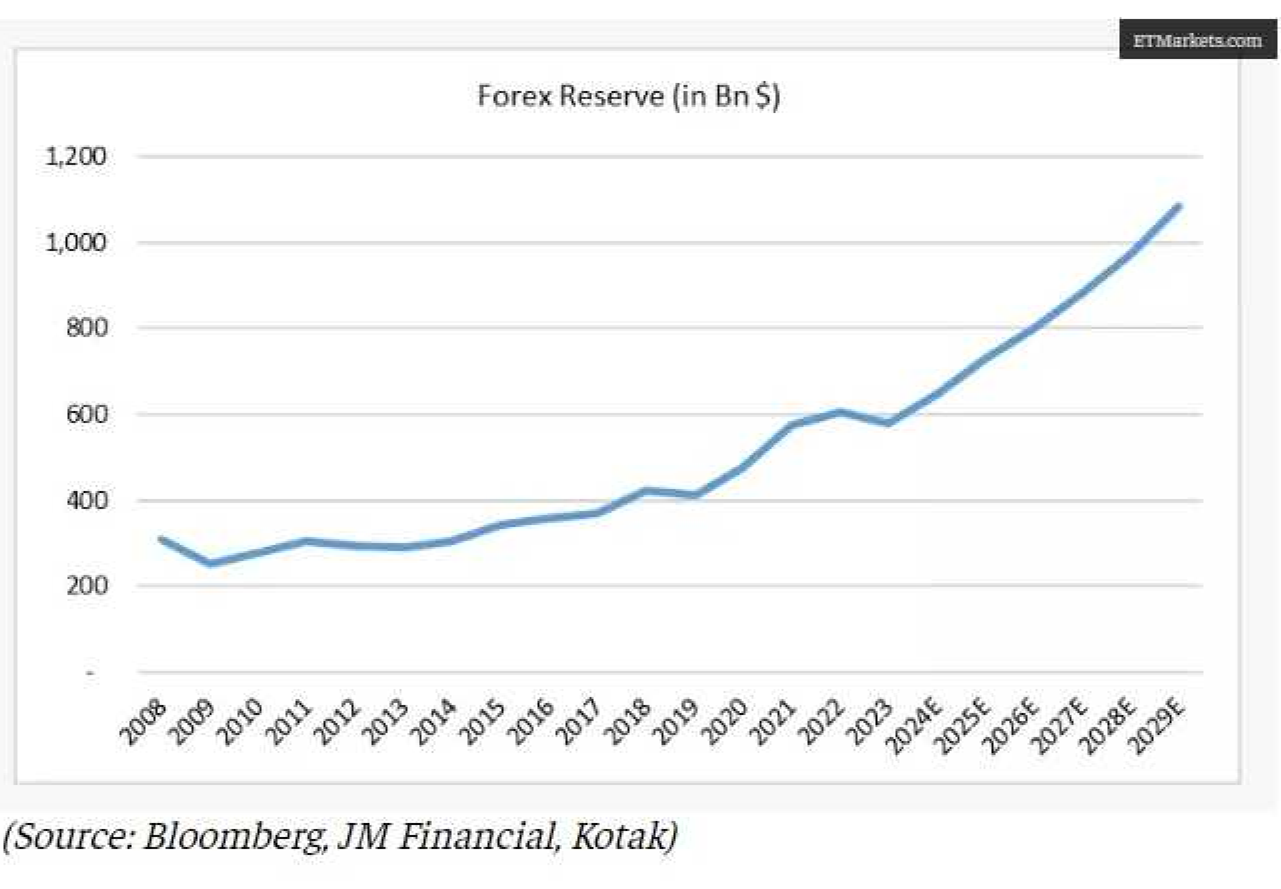
India's current account deficit has improved markedly, shrinking from 4.8% of GDP in 2013 to under 1% in 2024. This improvement has been driven by a strong software sector and rising remittances, which have increased by 180% over the past decade. Additionally, favourable oil import terms with Russia have helped manage the oil import bill. Reduced imports intensity due to thriving domestic manufacturing, especially in Electronics and Semiconductors, will lead to lower imports - 19% of GDP in 2019 to 13% in 2029E, thus aiding the Current Account improvement by 2.5% of GDP over the 2019-29E period. These factors contribute to the projection that India could achieve a current account surplus by FY2028E. (Source: JM Financial, Kotak)

Forex Reserves Target:

Based on a bottom-up analysis of anticipated inflows, India could see incremental reserves increase by $80-90 billion annually, potentially reaching $1 trillion by FY2029E. This influx of foreign currency is likely to strengthen the Indian rupee, reduce corporate borrowing costs, and enhance the profitability of Indian businesses. Consequently, India is poised to become a manufacturing hub with a competitive edge in the global market. (Source: JM Financial, Kotak)

Conclusion:

India's strategic economic initiatives and a favourable investment climate are set to drive substantial forex inflows over the next five years. Achieving $1 trillion in forex reserves by 2029E is not only a realistic target but also a milestone that will further solidify India's position as a global investment destination. This growth will support a stronger rupee, lower capital costs for businesses, and foster increased corporate profitability, thereby enhancing India's economic stature on the world stage.
(Source: JM Financial, Kotak)



(Source: Bloomberg, JM Financial, Kotak)

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Rs in Bn $	2014	2019	2024E	2025E	2029E
Current account balance	**(32.3)**	**(57.3)**	**(27.3)**	**(26.9)**	**22.5**
CAB/GDP (%)	-1.7	-2.1	-0.8	-0.7	0.4
Exports	319	337	442	453	498
Imports	466	518	686	703	777
Invisibles (net)	115	123	216	223	302
- Services	*73*	*82*	*163*	*169*	*244*
- software	*67*	*78*	*139*	*141*	*184*
- non-software	*6.1*	*4*	*24*	*29*	*60*
- Transfers (Remittance)	*65*	*70*	*102*	*103*	*107*
Capital account	**49**	**54**	**81**	**112**	**87**
- FDI	***22***	***31***	***16***	***32***	***32***
- FPI	***5***	***(1)***	***40***	***65***	***40***
- Equities	***13***	***3***	***25***	***50***	***30***
- Debt	***-8***	***(4)***	***15***	***15***	***10***
Forex reserves	**304**	**413**	**646**	**731**	**1,086**

(Source: JM Financial, Kotak)