THE ECONOMIC TIMES | Markets
English Edition ▾ | 05 June, 2025, 01:07 PM IST | Today's ePaper

How is India benefiting from supply chain diversification away from China? Morgan Stanley's Chetan Ahya explains

ET NOW Last Updated: Jun 04, 2025, 09:11:00 AM IST

Synopsis
Morgan Stanley's Chetan Ahya highlights India's growing advantage over China due to tariff differences. American companies are considering increased imports from India. Government policies are significantly boosting manufacturing and exports. Electronics manufacturing is expanding beyond mobile phones. Infrastructure development will further strengthen India's manufacturing exports. Optimism in Indian equity markets aligns with positive economic fundamentals.


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***Chetan Ahya**, Chief Asia Economist, Morgan Stanley, says India is gaining advantage due to tariff differences with China. American companies are considering increased imports from India. Government policies are boosting manufacturing and exports. Electronics manufacturing is expanding beyond mobile phones. Infrastructure development will further strengthen India's manufacturing exports. Optimism in Indian equity markets aligns with positive economic fundamentals. The organization maintains a bullish outlook on India.*

You have often talked about India's capex cycle and that you see it picking up. How do you see it shaping up and the kind of divide between private and government capex evolving?

Chetan Ahya: We think that the government capex has been the key anchor of the capex cycle and to the extent to which India has been embarking on this focus on manufacturing capex, the government's focus on infrastructure would be an important anchor to that private capex eventually improving as well.

Right now, it is still the government capex and we had seen a bump down or a small slowdown period for government capex post general elections last year. But we have seen that in the last three-four months, there has been a meaningful pick up in government capex. In March, we saw that both central and state government capex growing at a very high pace and that has now taken the 12-month trailing centre plus state combined capital expenditure to close to the peaks that we had seen right before the general election.

We have seen this strength in government capex coming back again. As far as private capex is concerned, we were expecting that would have picked up a lot more by this time, but to the extent to which we have seen this trade tensions emerge from early this year that is going to affect the capex outlook not only in the region, but also in India, despite the fact that India has lower exposure to global goods cycle.

The reality is that it still has a meaningful exposure of 12% of GDP being its goods exports to GDP. We are expecting private capex to be going through a bit of an adjustment period in the environment of global trade tensions and then, over the next calendar year, that is, in 2026, we should see a pick up in private capex because by that time, the damage out of this global trade tensions would have been behind us.

Talk about the China angle here and to what extent is India benefiting from the supply chain diversification away from China because this is something that has come up time and again for many years now.
Chetan Ahya: India is benefiting on account of it. Right now, during a period where tariffs on China, even after having come down, are still at a very high run rate of 30% and from the 2018 period, you also have about 11% weighted average tariff on imports from China that the US has imposed. Cumulatively, we still have a 41% tariff rate for import from China for the US and that does give some sectors an advantage over China in terms of pricing and even sort of thinking about a bit more from a medium-term perspective.

The corporate sector in America is beginning to think about importing more from India. India is probably benefiting on account of that. Then, from a medium-term perspective, we have always argued that look, it is not just about taking away market share from China, but just getting rightful market share for India in the global goods exports and for that India's policies that were important and the government has been taking the right policies to boost that manufacturing sector exports.

We have seen electronics manufacturing getting a leg up. We are going to see that expand into more and more products within the electronic segment apart from mobile phones and laptops. And at the same time, we think that from a medium-term perspective, this whole push towards infrastructure will really strengthen India's manufacturing exports. It is really a lot of the domestic policies that will be important from the long term apart from the short-term benefit that it may get on account of differential tariff rates between India and China.

Do you think the current optimism in the Indian equity markets is aligned with your view when it comes to economic fundamentals or do you see any areas with overheating or correction risk?
Chetan Ahya: Both our regional and India strategists have been very constructive on India. So, we are aligned up as a house on being bullish on India.