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India

Millennials to Anchor India's Growth Story

Millennials will bolster India's growth story. In this report, we evaluate the impact that India's millennials will have on the telecom, financials, property, and auto industries.

What's New? For telecom, we expect a surge in data consumption. In financials, momentum in consumer loans and financial saving should persist, while property purchases may not be an immediate priority for millennials. The low penetration of shared mobility and desire to buy a car augur well for auto demand.

Millennials are key to India's growth story: Our AlphaWise survey shows that 57% of India's working millennials are already the chief wage earners, accounting for 70% of overall household income. They are also likely to spend more, reinforcing our view of sustained high growth in both income and consumption.

Market implications: This economic growth is likely to translate into earnings growth, and, thus, equity returns. We remain constructive on Indian equities with a 12-month view, driven by a likely turn in the growth cycle, tolerable valuations, and a strong domestic appetite for equities.

Themes to own based on our survey: 1) Strong discretionary consumption including premium bikes, cars, entertainment, leisure, and personal grooming; 2) Internet access primarily through mobile phones drives a desire for data and data speed; and 3) Eventual plans to own property, but current means are missing. There is willingness to own equities as incomes rise. Key trades include:

- Bike premiumization: Prefer Eicher Motors, Bajaj Auto; avoid Hero
- Car demand: Prefer Maruti Suzuki
- Brick and mortar retailing: Prefer Future Retail
- Food-ordering habits: Prefer Jubilant
- Impact of digital influence: Prefer MakeMyTrip; avoid Hindustan Unilever
- Broadband and data: Prefer Reliance Industries, Bharti Infratel; avoid Bharti Airtel
- Consumer Finance and Financial Saving: Prefer Bajaj Finance, ICICI Prudential, Kotak

We remain overweight consumer discretionary and financials in our Model Portfolio. Eicher, Maruti, Jubilant, Reliance, and Bajaj Finance remain in our Focus List. We add Bajaj Auto to our Focus List at the expense of Tata Motors.

ALPHAWISE α
Evidence-based research

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Related research

The Next India: Technology: The Millennials Series: The Disruptive Wave in the World's Seventh Largest Economy (19 Feb 2017)

India – Consumer: The Millennial Series: Unique Insights into the Future of Indian Consumption (23 Mar 2017)

India Autos & Shared Mobility: Millennials Series: Two-wheelers: Premiumisation Lends Strength (05 Apr 2017)

Economics and Strategy

The millennials – India's key demographic segment...

Millennials (defined as those born after 1982, i.e., between the ages 18 to 35 years) have become the key demographic segment in India's population and labour force. As of 2016, there were 411mn millennials in India, according to UN's Population database, accounting for 30.6% of the country's total population, well ahead of any other age group. Their presence is felt even more strongly within the labour force, comprising 46.4% of India's working age population. Indeed, millennials will remain as the key demographic segment, accounting for more than 40% of India's working age population until 2037 as projected by the UN .

India's strikingly young population is in sharp contrast to that of other large economies such as China, the US, and Europe. As of 2017, its millennial group is larger than that of China (379mn, 37.8% of the country's working age population) and the US (80mn, 37.4%). Moreover, as per UN's population data India's millennial population is expected to keep growing at an average of 0.5% YoY until 2032, while it expects the US' millennial population to decline from 2027; China's millennials population growth is already contracting.

...and the strongest wage earners

This demographic trend has been and will remain one of the most important factors supportive of higher potential growth in India. Moreover, those aged between 18-35 tend to be the highest wage earners within the economy. This was corroborated by the results of our AlphaWise survey, which shows that 57% of the working millennials are already the chief wage earners, contributing nearly 70% of overall household income.

With millennials accounting for the bulk of the working age population and continuing to do so until 2037, we believe this trend will be positive for overall income growth. As was the experience in other economies, periods when the proportion of the 18-35 year working age population rises usually coincide with accelerating growth rates. In this context, we remain constructive on India's longer-term growth trajectory.

Favourable demographics associated with strong GDP growth trends

The cycle of falling age dependencies (with a rising share of the working age population) typically leads to a virtuous cycle of improving saving (and investment) to GDP and long phases of strong GDP growth. Indeed, India will continue to benefit from improving age dependency ratios until 2040.

What did other countries see with rising share of millennials?

Favorable demographics, riding the wave of globalization, and implementing policy reforms have been the key factors in sustaining growth in Asia. Throughout the region, a virtuous cycle of falling age dependencies (rising share of the working age population), improving saving (and investment) to GDP led to long phases of strong GDP growth. Within the region, Japan was the first to experience a positive demographic wave, followed by the former Tiger economies (i.e., Hong Kong, Singapore, Taiwan, and Korea) and then by China. We believe India will be the next economy in the region that is likely to experience this phase of rapid growth.

As we saw in the experience of other economies, a rising proportion of the 18-35 year age group is usually accompanied by a rising trend in saving and investment to GDP. A rise in investment to GDP is needed to create the virtuous cycle of higher investment – job growth – higher income, and higher saving. At the same time, while the share of consumption to GDP may decline, the rate of growth in consumption is likely to still be sustained at high levels.

As evidenced by our AlphaWise survey, an increase in per capita income levels is likely to be accompanied by higher spending growth. The higher income is likely to be spent more in the entertainment and restaurant categories, followed by personal grooming (apparel / accessory) and electronics. This further reinforces our base case assumption of sustained high growth in the overall consumption pie.

Reviving the private capex cycle is key

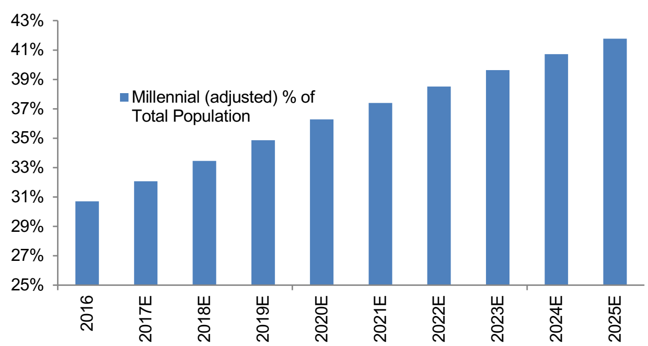
The demographics factor alone is not sufficient to accelerate GDP growth. It is important that the working age population is adequately skilled to participate in a globalized competitive environment. The next leg of harnessing this young and better-skilled population would require the creation of adequate employment opportunities. Indeed, this is both an opportunity and a challenge for India.

A critical input to generate employment opportunities will be the pace of government reforms. This will involve efforts to kickstart a private capex cycle. We believe that, with an increasingly young and connected population, the government's agenda is likely to be driven in the direction of productivity-enhancing reforms and job creation.

On its part, the government has been working on creating an enabling environment by streamlining investment approval processes and increasing public capex and taking up efforts to improve the ease of doing business in India. At the same time, implementation of broad initiatives such as the implementation of the Goods & Services Tax, and government initiatives such as Make in India and Skill India will also help to incentivise corporates to invest in India. To be sure, more efforts will be needed in the areas of resolving the legacy issue of impaired loans in the banking system and systematic efforts to ease regulations related to land / labour.

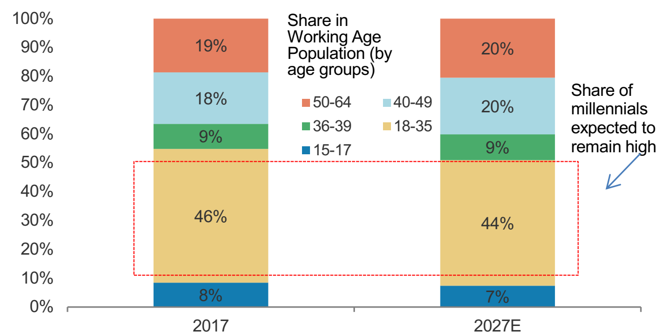
In our base case we expect private capex to recover in 2018, following six years of a declining trend. We believe that a supportive external demand environment, along with domestic demand growth, will improve capacity utilisation levels and create a basis for private capex to pick up. Indeed, over the medium term (i.e., over the next 10 years), we expect the share of investment to GDP to rise supported by a cycle of favourable demographics and rising income and saving rates. Indeed, this virtuous cycle will propel growth rates higher, making India one of the few economies in the world with a high productive growth trajectory.

Exhibit 1: Millennials (adjusted to include current millennials) are expected to account for more than one third of India's total population



Source: United Nations (UN), Morgan Stanley Research. E=UN estimates.

Exhibit 2: Millennials are expected to account for the bulk of India's working age population



Source: UN, Morgan Stanley Research. E=UN estimates

Market implications

There are three key conclusions to draw from a stock market perspective:

1. **India's burgeoning millennial population lends credibility to our growth forecasts in the medium to long term:** This economic growth is likely to translate into earnings growth for Indian companies. In turn, this drives returns from shares.

2. **From a saving perspective, there are three things we draw from the survey:** In summary, we think that millennials will commit a greater share of their saving into equities as their incomes rise. This is consistent with our view that we are in the midst of a domestic super liquidity cycle.

   a. Equities currently account for just 10% of millennials' saving, which we think suggests they are underinvested in equities.
   b. Millennials recognize equities as a source not only of higher returns but also higher risk or lower safety.
   c. As their income rises, so does their risk appetite, signaling a desire to own more equities. .

3. **Three key sectoral themes emerge from the survey:**

   a. Rising and varied demand for discretionary consumption, including premium bikes, cars, entertainment, leisure, and personal grooming.
   b. Mobile phones are the primary device for Internet access. There is a desire to gain greater data speed and propensity to consume data.
   c. Millennials plan eventually to own property, although the current means to do so is missing. In the meantime, there is willingness to own to equities as incomes rise.

AlphaWise survey overview

We surveyed 3,110 millennials across 24 cities in India. Our survey represents the Internet-using urban middle-class and upwards millennial population, and excludes the rural and the non-Internet-using millennial population. Although the survey does not cover the millennial population in India in its entirety, we believe the survey provides interesting insights into the consumption & investment preferences of an important demographic segment – the educated, Internet-savvy urban millennials. For more details on the survey please see AlphaWise Methodology & Respondent Profile.

Key takeaways from our survey

Consumer discretionary

- Premiumization of bikes

- Low penetration of shared mobility and latent aspiration for car ownership, entertainment/eating out, and personal grooming (apparel and accessories) are key categories where millennials will increase spending if their family incomes were to increase.

- Brick and mortar retailing remains a relevant channel - millennials place emphasis on product touch-and-feel and the social connection of shopping with friends and family.

- Competition from food aggregators may be less of a concern than the market believes. 78% of the millennials surveyed say that they order food either from nearby outlets or restaurants that they visit regularly.

- Digital influence is an important driver of brand preference for millennials; it may affect brand loyalty for large consumer staples companies. 66% of the respondents who shop online may end up buying brands/products that are very different from what they had planned. One key driver of millennials' online shopping is access to products/brands that are not available offline.

Telecom & Technology

- Mobile/smartphone is the primary device for internet usage among millennials.

- India's data usage is at an inflection point.

- 67% of the millennials are not content with either data speed or data limit or both, and 61% are fungible across service providers.

- Millennials are promoting internet usage to their parents/elders.

- Millennials are interested in convenience and instant gratification and are willing to pay for them.

Household balance sheet

- As millennials' incomes rise, property purchase appears to be an important avenue for investment for this population. We note that, outside of this survey, millennials represent a small portion of overall property demand. We continue to expect an improvement in volumes in the years ahead driven by strong macro factors – rising discretionary spend, job creation in urban centres, strong demographics, upgrade cycle, family nuclearization, strong retail balance sheets, and credit availability.

- As incomes rise, the appetite for risk increases and therefore demand for equities.

Key trades

- Bike premiumization: Prefer Eicher Motors, Bajaj Auto; avoid Hero MotoCorp

- Car demand: Prefer Maruti Suzuki

- Brick and mortar retailing: Prefer Future Retail

- Food-ordering habits: Prefer Jubilant

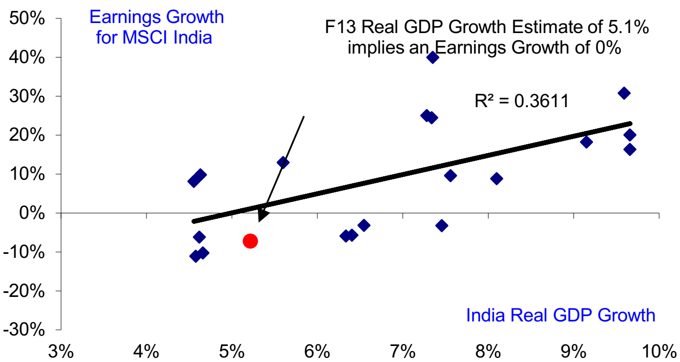
- Impact of digital influence: Prefer MakeMyTrip; avoid Hindustan Unilever

- Broadband and data: Prefer Reliance Industries, Bharti Infratel; avoid Bharti Airtel

- Consumer finance: Prefer Bajaj Finance

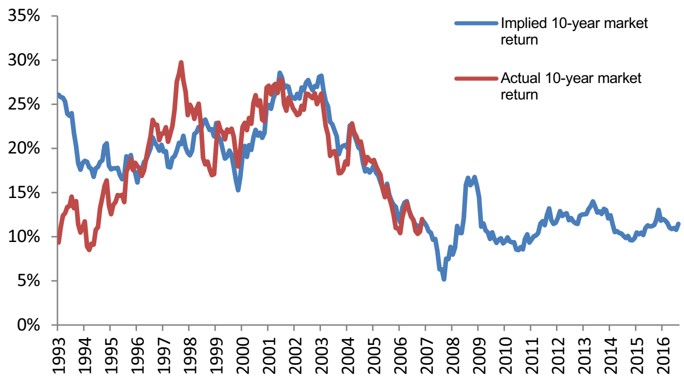
- Rising financial savings: Prefer ICICI Prudential, Kotak

Exhibit 3: Macro growth drives earnings growth



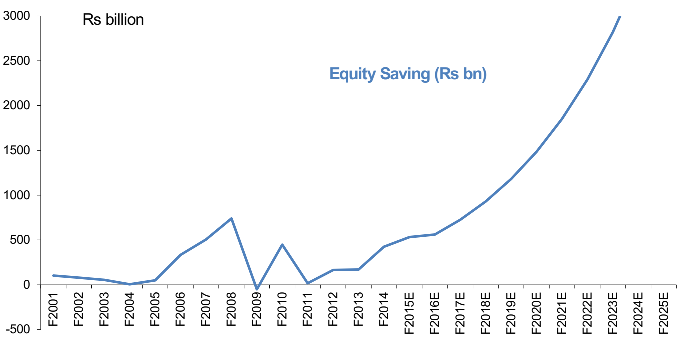
Source: RIMES, CEIC, Morgan Stanley Research

Exhibit 4: Expected rate of return is lower than it has been in the past but is still reasonable



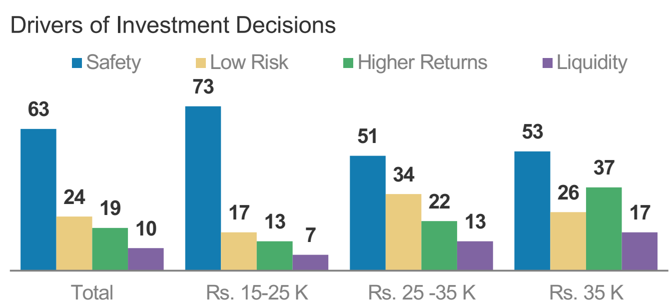
Source: RIMES, CMIE, CEIC, Morgan Stanley Research

Exhibit 5: The coming domestic saving boom



Source: RBI, Morgan Stanley Research. E=Morgan Stanley estimates

Exhibit 6: Safety of returns is important to millennials' saving decisions; the higher the income the higher the risk appetite



Source: AlphaWise, Morgan Stanley Research

Exhibit 7: Sector model portfolio

Sector	OW/ UW (bps)	(YTD)	(12M)
		Performance relative to MSCI India	
MSCI India		**10%**	**10%**
Consumer Disc.	500	-3%	6%
Consumer Staples	-600	1%	0%
Energy	-200	7%	16%
Financials	500	9%	19%
Healthcare	-200	-8%	-17%
Industrials	-200	10%	12%
Technology	400	-14%	-26%
Materials	0	6%	27%
Telecoms	0	-3%	-22%
Utilities	-200	-4%	13%

Source: RIMES, MSCI, Morgan Stanley Research

Exhibit 8: Focus list

Stocks	Sector	Rating	Price as on Apr 18, 2017	MCap ($ bn)	Rel to MSCI India		2Y Fwd EPS Growth
					YTD Perf	12m Perf	
Bajaj Auto	Cons. Disc.	OW	2,824	12.8	-3%	0%	9%
Jubilant Foodworks	Cons. Disc.	OW	1,008	1.0	7%	-27%	19%
M & M	Cons. Disc.	OW	1,263	12.2	-3%	-15%	13%
Maruti	Cons. Disc.	OW	6,137	28.7	5%	49%	29%
Titan	Cons. Disc.	OW	471	6.6	31%	18%	21%
Reliance Industries	Energy	OW	1,370	70.2	15%	17%	3%
Bajaj Finance	Financials	OW	1,236	10.7	33%	53%	34%
Bharat Financial	Financials	OW	735	1.6	13%	16%	109%
HDFC Bank	Financials	EW	1,447	57.1	9%	20%	18%
Indusind Bank	Financials	OW	1,432	13.3	17%	31%	26%
Shriram City Union	Financials	OW	2,250	2.3	12%	29%	22%
Glenmark Pharma	Healthcare	OW	892	3.9	-9%	2%	45%
Adani Ports	Industrials	NR	319	10.3	8%	25%	NA
Eicher Motors	Industrials	OW	25,533	11.0	6%	14%	30%
Havells India	Industrials	OW	483	4.7	28%	28%	19%
JSW Steel	Materials	OW	187	7.3	4%	27%	70%
UPL	Materials	OW	761	5.8	7%	36%	24%
Ultratech Cement	Materials	OW	3,972	17.0	11%	6%	18%
HCL Tech	Technology	EW	808	17.9	-12%	-14%	11%
Infosys	Technology	EW	923	32.8	-17%	-33%	7%

Source: RIMES, Morgan Stanley Research.

Note: Prices as on April 18, 2017. Past performance is no guarantee of future results. Results shown do not include transaction costs.

Autos (Binay Singh)

Two-wheelers: We saw that 21% of Indian households aim to buy a two-wheeler in the next two years, with aspirations moving toward premium bikes. The trend towards premium is in-line with our expectations, but the potential strength of the shift was a surprise – 4% of respondents already own a premium cruiser bike, but a surprising 11% plan to buy one. Aspiration may not always convert to purchase, but the results still suggest significant potential for premiumization.

Another interesting trend we saw was that first-time buyers increasingly prefer scooters, while replacement buyers of motorcycles trade up to a higher cc; given more than half of two-wheeler sales in the coming years will be driven by replacement, this trend also supports premiumization.

Four-wheelers: While the number of users of app-based taxi services are growing fast due to a low base, their penetration rates are still low (only 18% of those surveyed use these services at least once a month). Millennials do aspire to purchase their own cars and app-based taxi service providers have mostly replaced the public transport option.

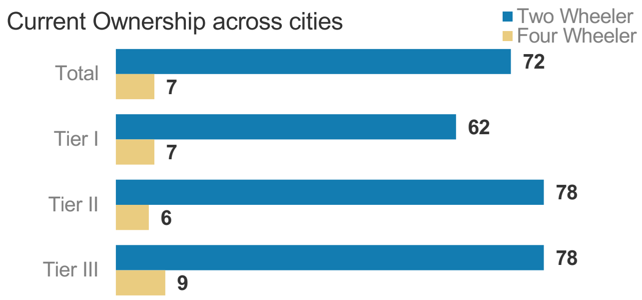
Stock implications: Within our coverage, we believe Eicher Motors, which owns the Royal Enfield brand, followed by Bajaj Auto are best placed to benefit from the premiumisation wave in two wheelers, while Hero MotoCorp, a leader in the mass segment, should see volumes lagging industry growth. The trends on the four-wheeler side augur well for Maruti Suzuki.

The spending power of India's millennials was US$180bn in 2016, and our economics team estimates this will to grow to US$330bn by 2020. Overall, millennials are becoming a key consumer segment, and, to understand their aspirations and spending trends, our AlphaWise team surveyed 3,110 urban millennials with an annual household income of at least US$2,800.

Detailed takeaways for four-wheelers: In line with our expectations, our AlphaWise survey indicates that car penetration in India is low and tends to rise as incomes expand. Further, while the number of users of app-based taxi services are growing due to a low base, the majority of millennials surveyed still would prefer to own at least one car for personal use.

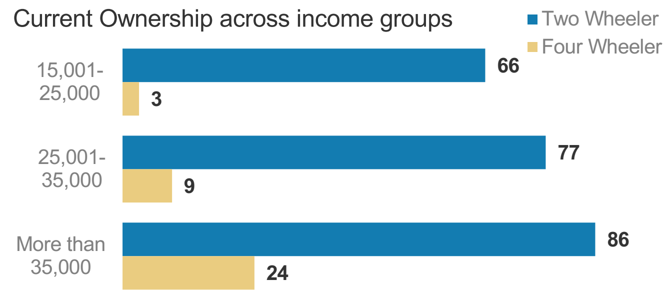
(1) Low current passenger vehicle (PV) penetration leaves ample headroom for vehicle parc growth in India: Our AlphaWise survey shows that, while two-wheeler penetration is at 72%, car penetration is much lower at 7%. More importantly, as incomes rise, both car and two-wheeler penetration rises but the change in car penetration is much stronger in cars versus two-wheelers. As incomes rise in India, we believe we will enter a multi-year car upcycle, and project an 11% PV volume CAGR, F2017-25.

Exhibit 9: Four-wheeler penetration is low in India ...



Source: AlphaWise, Morgan Stanley Research

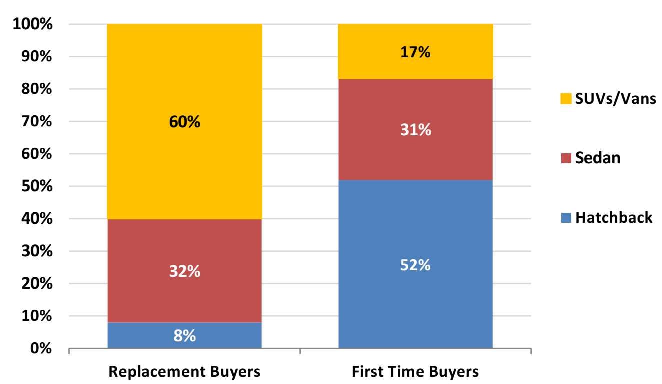
Exhibit 10: ... however, PV penetration rises sharply as we move up the income bracket



Source: AlphaWise, Morgan Stanley Research

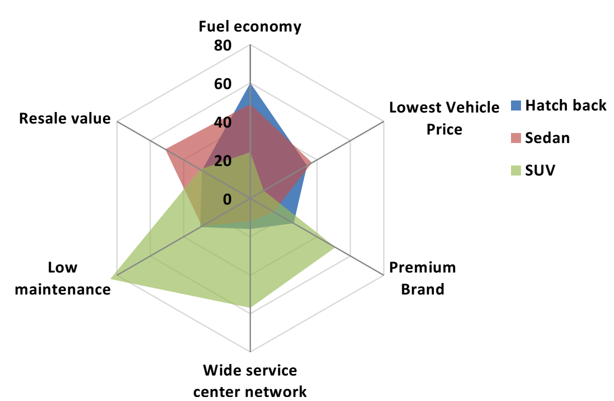
(2) First-time buyers prefer to purchase hatchbacks; replacement buyers go for SUVs: 5% of those surveyed intend to buy a PV in the next 24 months. In-line with our expectations, first-time buyers overwhelmingly prefer to buy small hatchbacks (52%), while replacement buyers overwhelmingly prefer SUVs (60%). We further analyze the reasons for owning a particular type of vehicle, and find that product quality and low maintenance are key drivers for choosing a particular SUV, while fuel efficiency and vehicle cost are key drivers for buying lower-priced hatchbacks. This implies opportunity for OEMs to come up with high-quality models that will sell well even at more premium price points, for example, the Hyundai Creta, which, despite the premium price point of Rs1-1.5 mn, has been selling an average of 8k units per month in F17.

Exhibit 11: Interesting contrast between purchase intentions of first-time buyers and replacement buyers of PVs



Source: AlphaWise, Morgan Stanley Research

Exhibit 12: Stark difference in what's important to SUV buyers vs what's important to hatchback/sedan buyers; SUV buyers tend to focus more on "quality" vs "value"

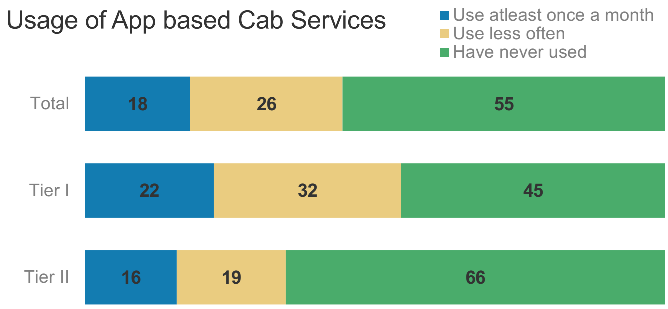


Note: Each axis in the chart above represents the percentage of respondents who believe that factor is one of the Top 3 factors when they decide which PV to buy.
Source: AlphaWise, Morgan Stanley Research

(3) Usage of app-based taxi services is not a threat to PV demand growth in India; at least not any time soon: We also analyzed respondents' usage of app-based taxi services, their experience so far of using such services, and their views on how this could potentially impact car ownership. We find that such services do not threaten PV ownership, given the following:

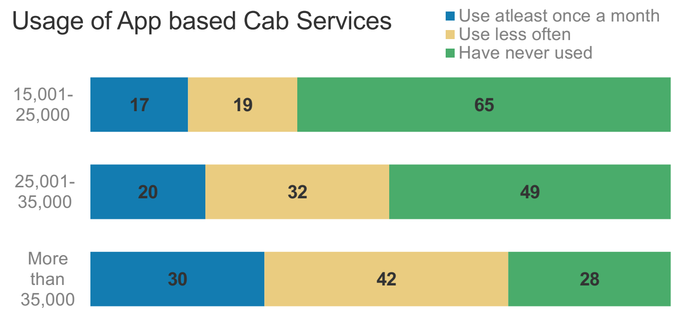
(i) Usage of app-based taxi services remains low in India: Only 18% of millennials surveyed report using such services at least once a month. Even if we were to define a regular user of such services as one who uses it once a week, then the ratio falls to just 13%.

Exhibit 13: Adoption of app-based taxi services remains low even in tier I cities



Source: AlphaWise, Morgan Stanley Research

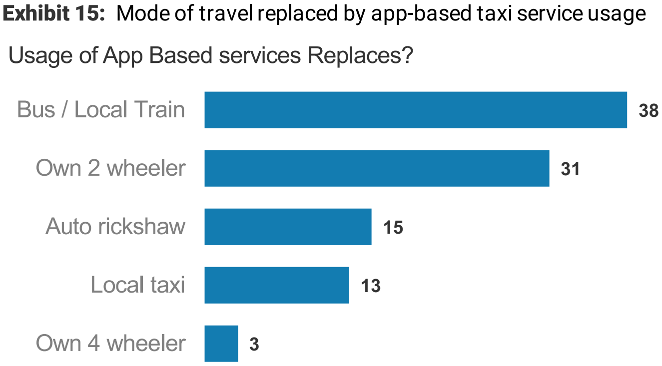
Exhibit 14: Adoption of app-based taxi services increases with rising incomes



Source: AlphaWise, Morgan Stanley Research

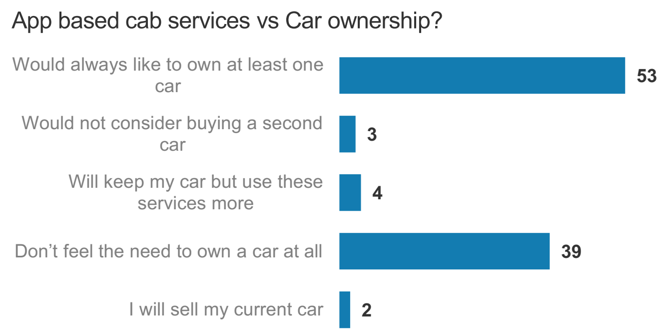
(ii) App-based taxi services are replacing the use of public transportation more than personal car usage: For those respondents who use app-based taxi services once a week, these services have, in most cases, replaced the use of public transportation more than their personal car usage. It has replaced the use of buses/local trains for 38% of the respondents, versus replacing PV purchases for only 3% of the respondents (refer exhibit 10) When they were asked what about they thought about car ownership given they have the alternative option of using app-based taxi services, 53% said they would still want to own at least one car. On the other hand, 39% said that they don't feel the need to own a car now. Overall, we believe that app-based taxi service providers will post strong growth on a low base, but car demand will still expand as car penetration rates in India remain low.

Exhibit 15: Mode of travel replaced by app-based taxi service usage



Source: AlphaWise, Morgan Stanley Research

Exhibit 16: Views on car ownership of those who use app-based taxi services at least once a week



Source: AlphaWise, Morgan Stanley Research

Consumer (Nillai Shah)

Discretionary consumption is the key millennial trade

India's millennial population is likely to emerge as a critical target audience for consumer companies, in view of their scale, spending power, and influence on household consumption patterns. Our AlphaWise survey shows that with rising incomes, Indian millennials are likely to increase spending on discretionary consumption segments such as entertainment/restaurants and personal grooming (apparel and accessories). Consumer staples companies, on the other hand, may face challenges in recruiting highly digitally influenced and yet price-conscious consumers.

We see three key themes from the AlphaWise survey:

1. **It's not just online; millennials remain tied to brick-and-mortar retail stores**
2. **New food delivery options/concepts, old habits**
3. **Not stapled to staples; digital influence may erode brand loyalty for large consumer staples companies**

Stock picks: Jubilant Foodworks and Future Retail are beneficiaries; Hindustan Unilever is less preferred.

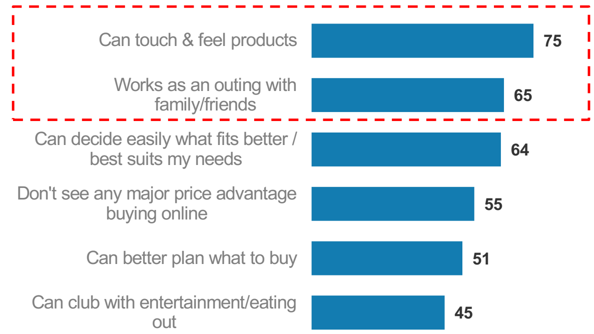
Theme #1: Brick and Mortar retailing remains a relevant channel

Contrary to investor concern, the shift to online retailing is likely to be more gradual than the market expects. Survey evidence indicates that the offline sales channel remains relevant for millennials. 57% of respondents in fashion (apparel and accessories) and 63% in personal products (PP) still prefer the offline channel for purchases – they place emphasis on product touch and feel and the social connection of shopping with friends/family. For online shopping, one key driver of millennials' preference is access to products/brands. It's not just about lower prices any more.

Exhibit 17: Top five reasons to shop online

Source: AlphaWise, Morgan Stanley Research

Exhibit 18: Top five reasons to shop offline



Source: AlphaWise, Morgan Stanley Research

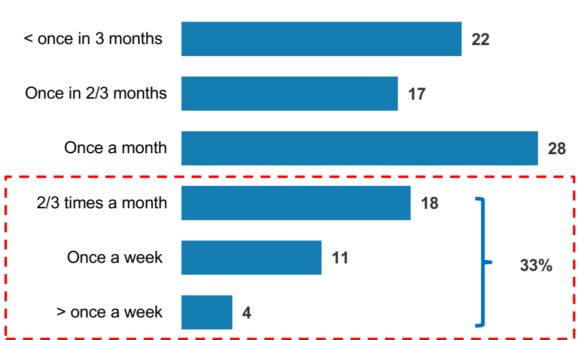
There may be an underappreciated opportunity for omni-channel retailing in India.

Which stock is affected? We expect Future Retail to perform well. We cite its strong brands, first-mover advantage, scale benefits, private label brands, and robust product sourcing capabilities.

Theme #2: Competition from food aggregators may be less of a concern than the market believes

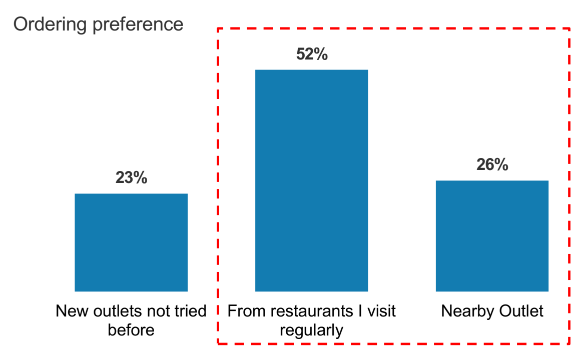
Investors are concerned that rising competition, especially from food aggregators, is likely to blunt Domino's competitive edge of timely home delivery. Survey evidence suggests that the market for home ordering/eating out is relatively nascent in India. Only one-third of millennials order at home or eat out at least 2-3 times a month. Further, 78% of the millennials surveyed say that they order home either from nearby outlets or restaurants that they visit regularly, suggesting that a first-mover advantage and wide store network are critical for success in the QSR market in India.

Exhibit 19: 33% respondents eat out/order food home more than once a month. Only 15% respondents do so at least once a week



Source: AlphaWise, Morgan Stanley Research

Exhibit 20: 78% respondents order either from nearby outlets or restaurants that they visit regularly



Source: AlphaWise, Morgan Stanley Research

We believe market concerns about increased competition from new brands and food aggregator may be exaggerated in the near term.

Which stock is affected? Evidence from our survey indicates that concerns about rising competition may be exaggerated, boding well for Jubilant Foodworks. The evidence helps allay concerns about rising competition from new formats/brands and food technology companies. We expect the brand to benefit from rising consumer incomes, potential improvement in urban discretionary consumption, large store network, established brand and competitive edge of 30 minutes or free home delivery promise.

Theme #3: Digital influence is an important driver of brand preference for millennials; it may affect brand loyalty for large consumer staples companies

Survey evidence suggests that millennials are highly digitally influenced – on average spending over 17 hours on the Internet every week, with nearly one-fourth of this time spent searching for information. 66% of millennials who shop online may end up buying brands/products that are very different from what they had planned. It is likely that brand loyalty among millennial consumers is lower than it is for older generations. 51% of respondents also rely on online product reviews for their purchase decision. However, cost remains an important criterion – 56% of these respondents seek to remain within the intended budget.

Which stock is affected? Hindustan Unilever – risk to brand loyalty = risk to market share and operating margins. HUL faces risk from millennials' influence in the near term. We believe HUL, – with an intense focus on innovations, go-to-market strategies, supply chain, distribution, digital & mobile marketing, and consumer access – is one of the best companies to back in the long term in India. In the near term, however, we believe the life cycle of HUL's business in India is at a threshold. It will look to recruit new consumers and millennials in particular for growth across multiple nascent categories. This may need upfront investments supported by extensive education and sampling. Millennials are digitally influenced, price-conscious, and inclined to alter their buying behaviour based on product reviews. As their influence on overall consumption rises, we see risks to current record high operating margins for large consumer staples companies, with increased competition from brands that may be perceived to offer more compelling consumer value.

Property (Sameer Baisiwala)

Attractive industry view – from the lens of millennials

1. The home buying age in India typically is between 34-55 years. Millennials are largely out of this age bracket.

2. Nonetheless, our AlphaWise survey gives good insights into how millennials are thinking about property ownership.

3. In summary, in the near term, they are not planning to invest in property (probably because of flat prices over the last few quarters). However, in the medium term, when their incomes rise, property ownership appears to be an important investment avenue.

4. We maintain an Attractive industry view in light of the structural demand drivers – rising discretionary income, urbanization, upgrade cycle, strong retail balance sheet, and easy credit availability

Millennial survey: We segment the AlphaWise survey data by age and salary to derive the relevant millennial sample relevant to the property industry. 18% of Tier I millennials earn more than Rs35k a month and 53% of respondents are 25-35 years old (roughly 10% of the surveyed sample is 33-35 years of age). Therefore, on the basis of age and income, we estimate that 2-4% of the surveyed millennials (33-35 years of age and Rs80k per month or more salary) are in the home buying bracket and hence relevant to the property industry.

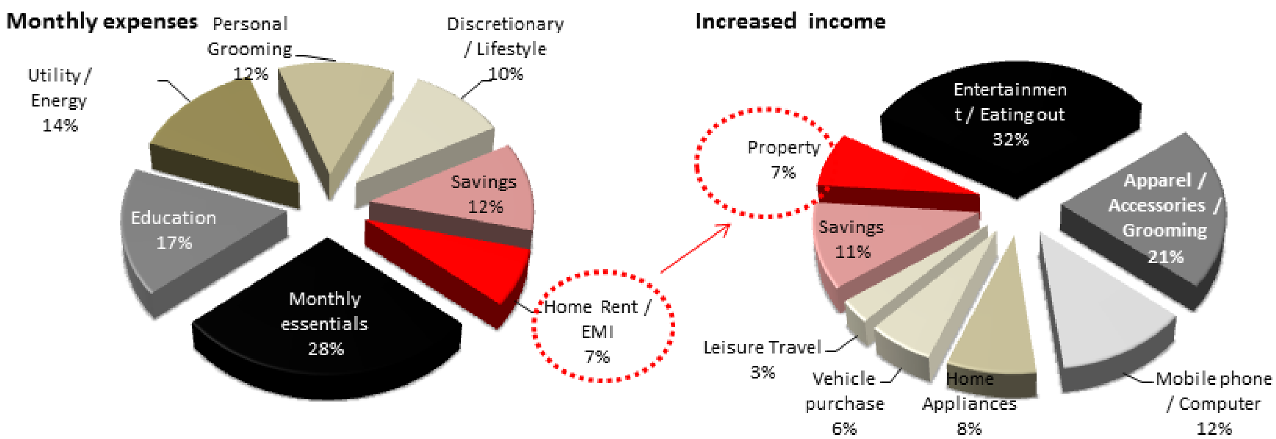
In the near term (i.e., over the next year), property purchase is not a priority for millennials: Based on survey results, their preference for property purchase is nil over the next few months. This is understandable in view of the lackluster trailing property price performance – flat to mid-single-digit rises over the last two years. Also, the outlook for property prices is modest: 2-4% growth p.a. for next one to two years, in our view, making near term property purchase less attractive for millennials as they expect higher return on their investment.

Tier I millennials have the largest share – i.e., 46% of their total investments – in bank deposits (including provident fund), followed by almost equal shares of 16% in real estate, insurance, and bullion. Equity investments are less than 10%. Tier I millennials have high risk appetite – they plan to reduce their deposits and invest more in equities in the next 12 months.

However, on a medium term basis, as income levels rise, property purchase appears to be a prominent investment option: According to the survey results, as their income rises, 7% of the surveyed sample plans to invest in property. This is significantly ahead of leisure travel (3%) and a notch above vehicle purchase (6%). To note, this property preference by 7% of the sample is meaningful (roughly one-third), when combined with the overall investment preference of 18% (including 11% savings). The remaining 82% is largely for consumption spending, including eating out and entertainment (31%), apparel and accessories (21%), electronics (12%), etc.

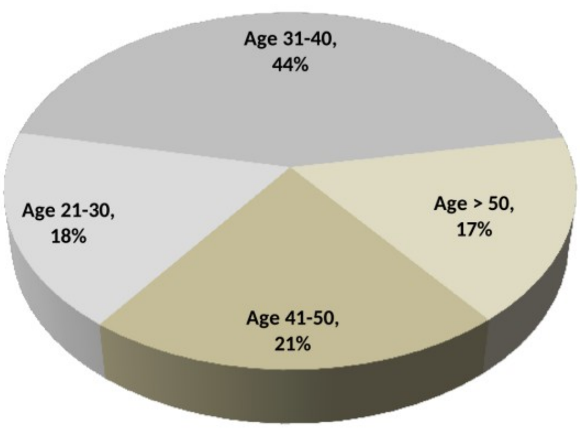
Our outlook: Millennials represent a small portion of overall property demand. We continue to expect improvement in volumes in the years ahead (from people in the 35-55 age group) driven by strong macro factors – rising discretionary spending, job creation in urban centers, strong demographics, upgrade cycle, family nuclearization, strong retail balance sheet, and credit availability.

Exhibit 21: Millennials plan to invest in property with incremental income – they rank it significantly higher than leisure travel and a notch above vehicle purchase



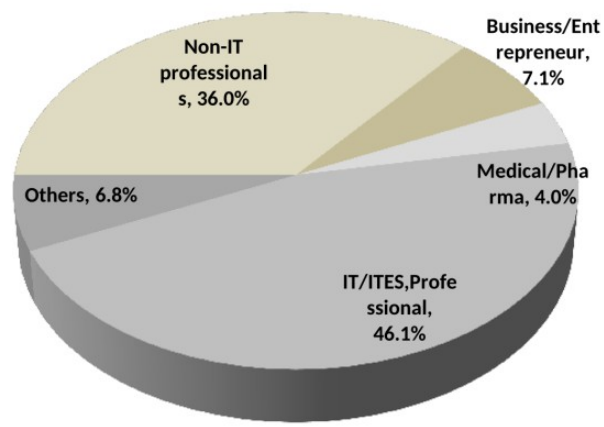
Source: AlphaWise survey, Morgan Stanley Research

Exhibit 22: Sobha: 20%+customers are in the millennials age bracket



Source: Company data, Morgan Stanley Research

Exhibit 23: Sobha: 46.1% of its customers are IT professionals, who are largely in the millennials age group



Source: Company data, Morgan Stanley Research

Telecoms (Parag Gupta)

Data on the cusp of powerful growth – a longer-term opportunity for the telecom industry

We believe India's data usage is at an inflection point: High adoption of mobile broadband within the millennial sample was one of the strongest highlights from the survey. At 84% 3G/4G penetration, this was significantly higher than the 17% on a pan-India basis (as of December 2016). Rising availability and affordability of smartphones, improving data coverage, declining data prices, growing online content, and ease of technology adoption among youth are some of the key drivers, in our view. With ~94% of Internet access coming from smartphones, we believe massive data growth in the country is beginning.

Overall mobile broadband penetration could touch 50% by 2020: This reflects the fast uptake of mobile broadband among millennials and the increasing proportion of 4G LTE-enabled phones. We assume that new Internet-using millennials will represent 70% of all new mobile broadband users in India.

Key takeaways from the survey:

1. **Millennials demonstrate healthy Internet usage:** They spend over 17 hours on the Internet in a week. 35% of that time is spent on emails/social media, 30% on online entertainment, and 23% searching for information.

2. **~85% of the millennials were 3G/4G users and data speed is important:** Suitable content followed by higher Internet speeds were the top two factors for improving their overall Internet experience.

3. **67% of the millennials were not happy with data speed, data limit, or both; 61% were fungible across service providers.** Millennials with higher family incomes (>35K monthly family income) were most unhappy (75%) with current data speed, data limit, or both. They indicated a higher preference (72%) for switching to another provider only for data while retaining their current provider for voice.

4. **Airtel's market share was the highest at 26%, but RJio made a grand entry with 19% share:** That was ahead of Vodafone and Idea. We believe this appears logical in view of point 3 above, since RJio's offerings are currently unmatched in the industry (in terms of per unit pricing). RJio ranked #1 along with Airtel in Tier II cities with 26% share, though it was much lower in Tier I cities (at 13% vs. 28% for Airtel).

5. **83% of the millennials were willing to spend more on data for better speed:** On average, millennials were willing to spend ~Rs200 more per month on data. 90% of the sample was willing to spend up to Rs300 more on data.

Stock implications

Usage trends suggest that India will show significant data growth. However, the need for better speed/data limits and the willingness to pay suggests that millennials are also looking for the best value for money and hence are ready to switch, if required. That could be disruptive for the industry.

- **This supports our Underweight call on Bharti Airtel:** We believe competitive price offerings from RJio (as compared to current offerings from the incumbents) will exert pricing pressure on the incumbents.

- **On the other hand, we like infrastructure providers such as Bharti Infratel (OW) and TCOM (OW):** They shou;d benefit as operators aggressively roll out capex to meet the growing data needs of consumers.

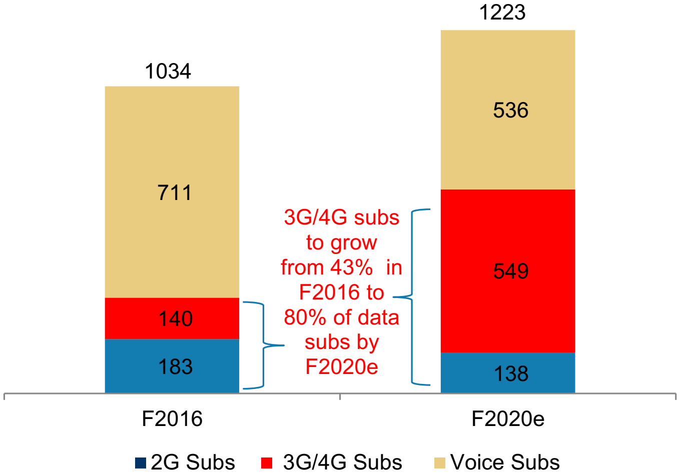
Two key drivers are required for data growth, in our view:

1. **Rise in 4G smartphone penetration:** Smartphone penetration in India was 22% of the country's population as of December 2016, versus the 67% Asian peer average. We expect 4G smartphone penetration to reach 33% by C2018 and ~51% by C2020. There are ~120mn 4G smartphones in the market, which are ~40% of the total smartphones as on December 2016, incrementally adding ~9mn to 10mn each month.

2. **Rise in 4G subscribers, with developing handset ecosystem and cheaper data pricing:** As seen in China, 4G data users consume 6x-7x more data, on average, than do non-4G users. Incrementally, since 2H F16, over 85% of the smartphones shipped are 4G in India – a positive for data consumption in the long term. We expect overall wireless data users to reach 678mn in F20, 80% of whom will be 3G/4G users, thus representing ~40% penetration, with each user consuming ~1.3GB/month of mobile data by F20.

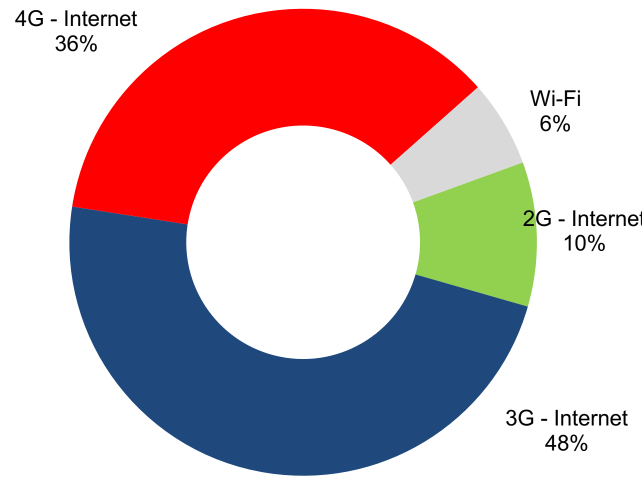
Morgan Stanley & Co. International plc ("Morgan Stanley") is acting as financial advisor to Vodafone Group plc ("Vodafone") in relation to a proposed merger of Vodafone India Limited (excluding Vodafone's 42% stake in Indus Towers) and Idea Cellular Limited as referred to in Vodafone's press release published on 20 March 2017. There is no certainty that any transaction will be agreed, nor as to the terms or timing of any transaction. Vodafone may pay fees to Morgan Stanley for its financial services. Please refer to the notes at the end of the report.

Exhibit 24: Data subscriber growth to be driven by 3G/4G users, F16-F20 (mn)



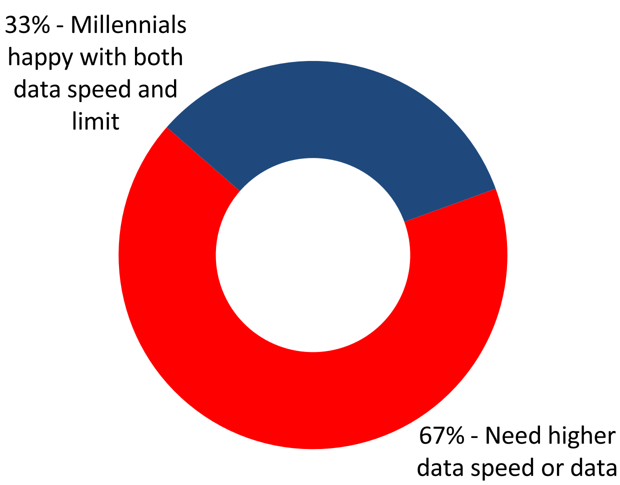
Source: Company Data, Morgan Stanley Research, e= Morgan Stanley estimates

Exhibit 25: ~85% of the millennials use 3G/4G Internet, clearly demonstrating the preference for speed



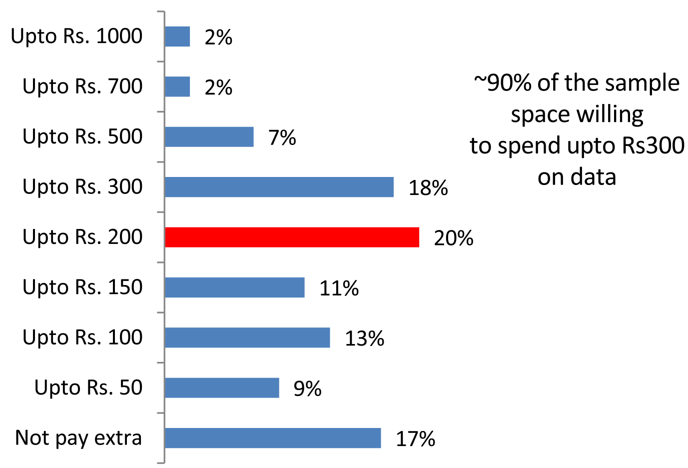
Source: AlphaWise, Morgan Stanley Research

Exhibit 26: 67% of the millennials need higher speed or higher data benefit or both…



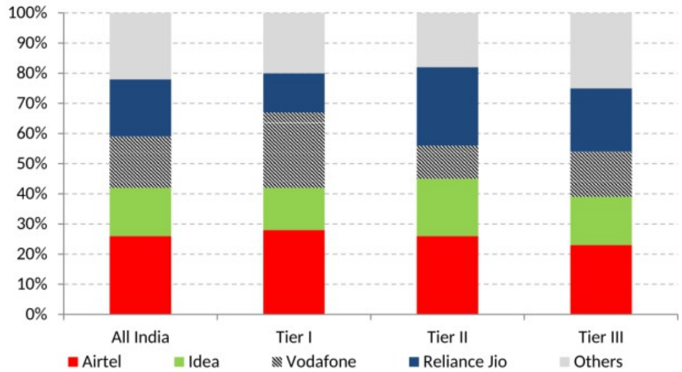
Source: AlphaWise, Morgan Stanley Research

Exhibit 27: …and 83% of the sample is willing to pay more for better mobility experience



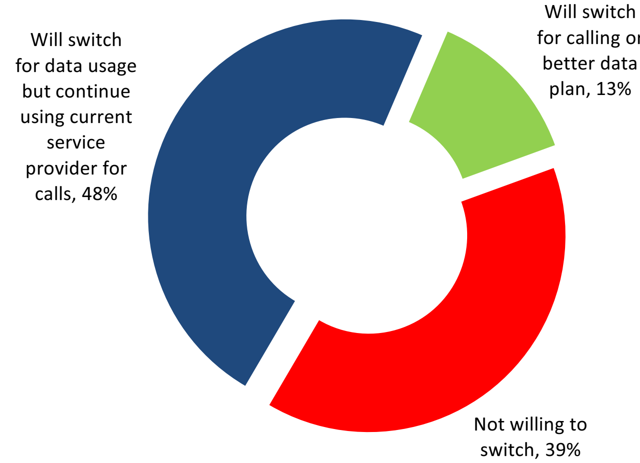
Source: AlphaWise, Morgan Stanley Research

Exhibit 28: 26% of the millennials were on Airtel, 19% on RJio, followed by Vodafone at 17% and Idea at 16%



Source: AlphaWise, Morgan Stanley Research

Exhibit 29: 61% of the respondents were willing to switch service provider



Source: AlphaWise, Morgan Stanley Research

Technology (Parag Gupta)

India's millennials (including past millennials) will comprise 61% of the nation's Internet population and 78% of online shoppers by 2020: India's millennial population of 400mn is the largest in the world and is armed with around US$180bn in spending power. By 2020, we estimate that 61% of India's Internet base will be millennials (including those that are currently millennials but will be beyond the age of 35 by then) and that 78% of the online shopper base of 330mn will be millennials.

Our AlphaWise survey of India's millennials shows positive trends in online shopping adoption: The survey results were exciting – online shopping adoption within millennials was 35-45% for key product groups such as fashion, electronics, and personal/health products. Further, from the survey we can conclude that the activity of millennials across different city tiers and income groups is healthy and points to a sustained increase in engagement and spending.

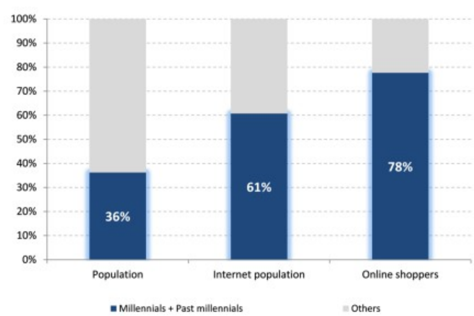
Listed investable opportunities are limited – but we have an OW rating on MakeMyTrip: We see significant headroom for online penetration in domestic hotels and potential market share gains for the company.

Exhibit 30: Key macro takeaways from the millennial survey from a technology/Internet standpoint

Millennial population (2016)	407mn
Spending power - 2016 *	US$180bn
% of consumption economy	14%
Millennial population (2020e)	504mn (incl ~80mn of current millennials that are beyond 35 years of age then)
Spending power - 2020e *	US$330bn
% of consumption economy	17%
Smartphone ownership (as per AlphaWise survey)	100%
Internet access on smartphone (as per AlphaWise survey)	89.50% of time spent
3G/4G adoption (as per AlphaWise survey)	84%
Time spent on the internet (as per AlphaWise survey)	17 hours per week
Online shopping adoption (as per AlphaWise survey)	~40%

Source: AlphaWise, Morgan Stanley Research; e = Morgan Stanley Research estimates. * this is the amount of income available to millennials after meeting essential requirements

Exhibit 31: India's millennial (including past millennials) population by 2020 will be 36% of total population but will be a much larger force to reckon with in terms of Internet and online shopper population.



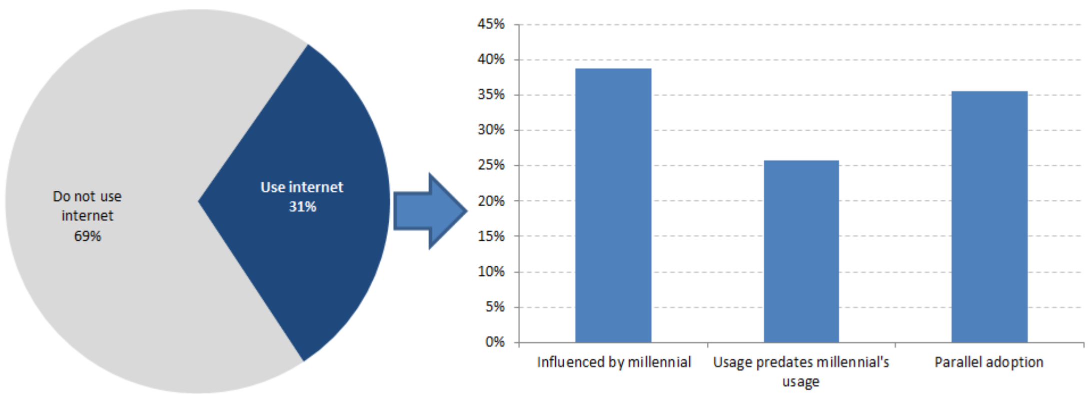
Source: Census of India (2011 data), Morgan Stanley Research; e = Morgan Stanley Research estimates. Note: 2011 census; UN population database; percentage of Internet users and online shoppers that are millennials are Morgan Stanley Research estimates

Some key themes emerged from the survey

1. Mobile/smartphones are the primary devices for Internet usage among millennials: According to our survey, Indian millennials are spending an average of over 17 hours on the Internet every week, carrying out varied activities such as social media, searching, entertainment (music, movies), online banking, and online transactions. Of interest, mobile devices are the primary means to access the Internet. The level of engagement is encouraging, but, as noted, still below that in China and the US. This provides further headroom to grow.

2. Millennials are promoting Internet usage among their parents/elders: Only 31% of millennials surveyed said their parents were connected to the Internet, but the real insight was a layer below – about 40% of these older Internet users had been influenced by millennials while another 35% had adopted the Internet at the same time as their kids had. This portends well for Internet usage among the Gen X and baby boomer population.

Exhibit 32: Internet penetration within parents and in-laws was found to be low at 31%. However, millennials have played a role in promoting usage among elders who are on the Internet.



Source: AlphaWise, Morgan Stanley Research

3. Millennials are interested in convenience and instant gratification and are willing to pay for it: This can be corroborated by a few data points in our survey:

- Uptake of premium subscriptions (such as Amazon Prime) or the likelihood of taking one up was 51%.
- Usage of app-based taxi services at 18% was driven by comfort and easy availability.
- Low prices/discounts did not figure among the top three reasons for buying online.

Our top Indian Internet pick is MakeMyTrip: Lower online penetration, dominant market leadership and strong balance sheet drive our positive view on the stock. Following closure of the MakeMyTrip-Ibibo merger, the combined entity is the largest online travel agent (OTA) in India. Online penetration within the Hotels & Package segment remains low (at ~14%, by our estimate), and we expect the combined entity to continue to drive share gains and emerge as a dominant market leader across each of the respective key business segments within the OTA market.

Key risks: Our survey highlighted a negative data point that online penetration for hotel bookings was low at 19% and % of hotel walk-ins was extremely high at 63%. We believe

OTAs will need to bring a larger number of hotels on to their platform, drive innovation in the form of last-minute booking deals, and continue to incentivize customers.

Non-Bank Financial Companies (NBFCs) – Consumer Finance (Subramanian Iyer)

We believe discretionary consumption finance will take off over the next decade: This should accompany higher discretionary consumption, which our consumer team believes will increase driven by millennials – also reinforced by our recent AlphaWise survey.

Bajaj Finance (BJFN) is the leading player in this market and we view it as the best way to invest in this theme: In our view, India's growing millennial population and the sheer addition to the workforce every year will sustain high multiyear retail credit growth for retail-focused lenders like BJFN. It has made significant investments and possesses a pan-India network, experience, and service delivery channels.

Further, our Autos team believes that Bajaj Auto is a key beneficiary of the premiumisation that is under way in two-wheelers (a conclusion derived from our recent AlphaWise survey). As a captive financier to Bajaj Auto, BJFN is again an indirect beneficiary.

Its growth prospects should also support valuation – we rate the stock OW: BJFN' s high multiples (P/E of 28x for F2018e and 20x for F2019e) are factoring in strong medium- to long-term earnings growth prospects – the Millennials theme is central to this, in our view.

Though we don't assume that BJFN can re-rate given the high starting point, strong EPS and BVPS compounding should drive multiyear stock returns. For F2017-19, we forecast 38% EPS CAGR and 25% BVPS CAGR.

According to our Consumer and Autos teams, the rising population of millennials in India will have two key offshoots:

- **Higher discretionary consumption:** Our Consumer team believes that with rising incomes, millennials are likely to increase spending on discretionary consumption segments like entertainment/eating out and personal grooming (apparel and accessories).
- **Premiumisation of two-wheelers:** Our Autos team notes that while consensus expects a broad recovery in all two-wheeler segments, evidence from our AlphaWise survey of millennials leads us to anticipate a sharp move up in mix towards premium bikes and slower mass segment growth. They see Bajaj Auto as one of the beneficiaries given meaningful exposure to the premium segment. They expect an 11% CAGR in two-wheeler segment sales over F2017-19 after CAGRs of 4.9% over the last two years and 5.6% over the last five years.

BJFN, being a key financier in these segments, is a beneficiary – it is our preferred play on this theme.

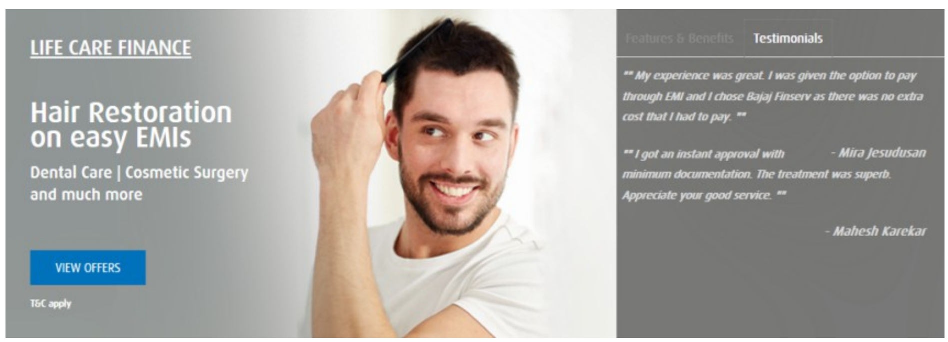
Both these businesses are of strategic importance from a customer acquisition perspective and also generate ROA higher than the enterprise average.

a) BJFN is arguably the best operator in the discretionary consumption finance segment. BJFN has been at the forefront in tapping the financing opportunity in discretionary consumption. It finances >20% of all consumer durables (white goods) sales in India. It has also been consistently and aggressively increasing its footprint across channels (both physical and digital). In addition, it has been adding products. This has driven strong growth in customer acquisition as well as repeat business with existing customers.

Rising share and incomes of millennials will result in demand for newer products and services. In addition to consumer durables, BJFN has been innovative in identifying opportunities and adding verticals like digital financing (mobile phones, etc.); lifestyle financing (furniture, etc.); and life care financing (dental care, hair restoration, laser eye treatment, stem cell preservation, etc.)

This segment forms about 15% of overall AUM for Bajaj Finance – but more importantly, is key to acquiring customers, to whom BJFN cross-sells more products (personal unsecured loans, home loans, fee income products, etc.). Tie-ups with manufacturers, service providers, and vendors also create opportunities to provide financing solutions to them.

Exhibit 33: Bajaj Finance has been innovative in identifying discretionary consumption financing opportunities



Source: Image from Shutterstock.com

b) Being a captive financier to Bajaj Auto will enable BJFN to participate in Bajaj Auto's higher sales in the premium two-wheeler segment: BJFN has consistently financed more than 30% of Bajaj Auto's two-wheeler sales. Two-wheeler financing constituted ~8.5% of overall AUM as of F3Q17.

Exhibit 34: Consistent and strong buildup in distribution...

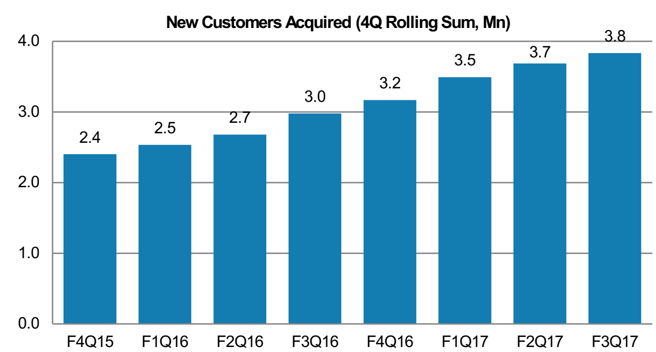
Branches	FY11	FY12	FY13	FY14	FY15	FY16	F3Q17
Consumer durable	79	82	91	114	161	193	304
SME business	23	31	57	80	119	262	296
Rural Branches	0	0	0	14	50	90	NA
Rural Spokes	0	0	0	56	182	307	NA
Total Rural locations	0	0	0	70	232	397	519
Distribution POS							
Consumer durable	2500+	2800+	3500+	4900+	7000+	9400+	14000+
Digital	0	0	850+	1600+	2650+	5200+	5900+
Lifestyle	0	0	0	0	1,150+	3200+	3900+
2W Dealer/ASCs	1500+	2,200+	2,600+	2,600+	3,000+	3000+	3000+
SME Partner	250+	250+	400+	700+	700+	800+	1000+
Rural Consumer Durable	0	0	0	0	1,500+	3200+	3900+
Retail EMI Dealer							4600+

Source: Company Data, Morgan Stanley Research

Exhibit 35: ...and launch of new products

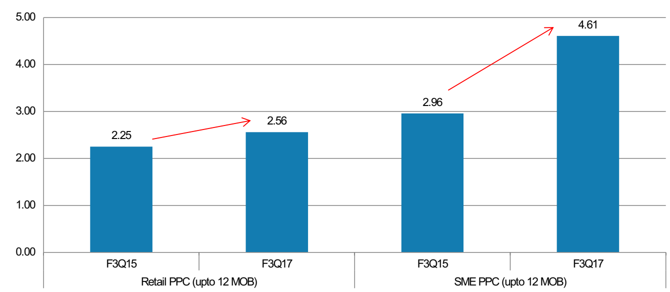
Source: Company Data, Morgan Stanley Research

Exhibit 36: Strong new customer acquisition



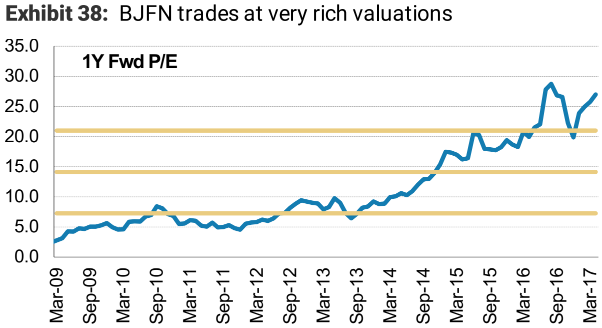
Source: Company Data, Morgan Stanley Research

Exhibit 37: Focus on cross-selling



Source: Company Data, Morgan Stanley Research

Exhibit 38: BJFN trades at very rich valuations



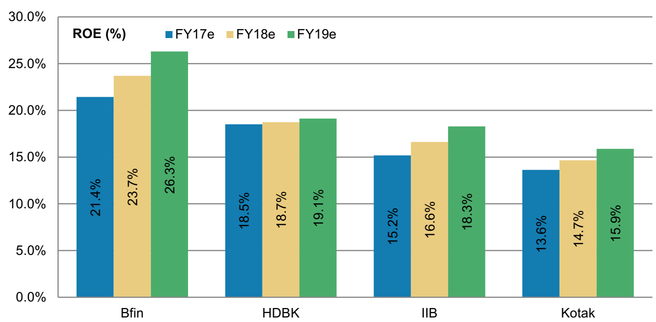
Source: Company Data, Thomson Reuters, Morgan Stanley Research

India's multi-year discretionary consumption growth story, driven by millennials, is one of the core drivers of our OW rating on the stock – despite premium valuations. A key point of investor pushback on our OW rating on BJFN is the stock's high valuations. The debate is whether the company can sustain 30%+ asset and earnings growth over the next three years and 20%+ growth even thereafter.

Our view is that the company can indeed sustain high growth. India's retail credit penetration is much lower that of other Asian emerging countries and the developed world. We believe this can take off significantly in this decade given the sheer proportion of the population entering the workforce. This augurs very well for consumer financiers like BJFN that have made significant investments in this business and spent significant effort in developing risk management systems and service delivery channels.

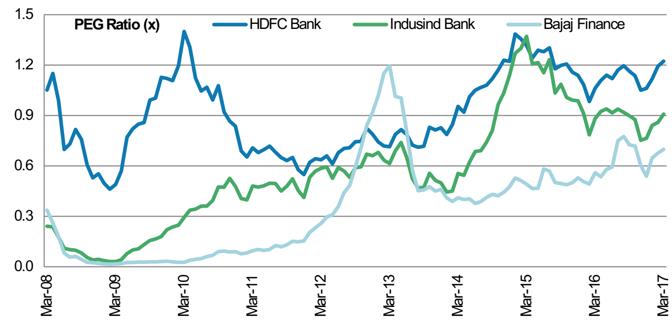
BJFN has a track record of delivering superior products and service with a quick turnaround time. This requires significant organisational focus. While a large part of the system (public sector banks and corporate-focused private lenders) will be left playing catchup, BJFN and the retail private banks should take disproportionate market share.

Exhibit 39: BJFN screens higher on ROE profile than retail private banks...



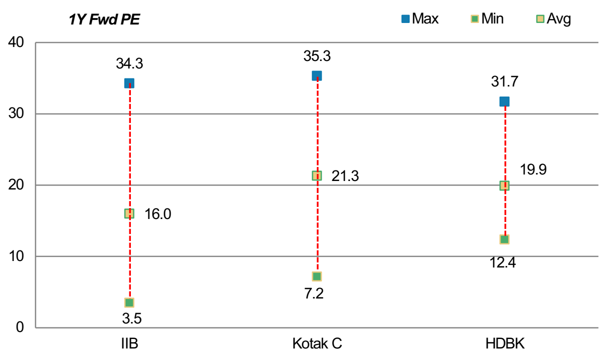
Source: Company Data, Morgan Stanley Research

Exhibit 40: ...and on earnings growth; PEG ratio at BJFN is lower than private retail banks at 0.7x



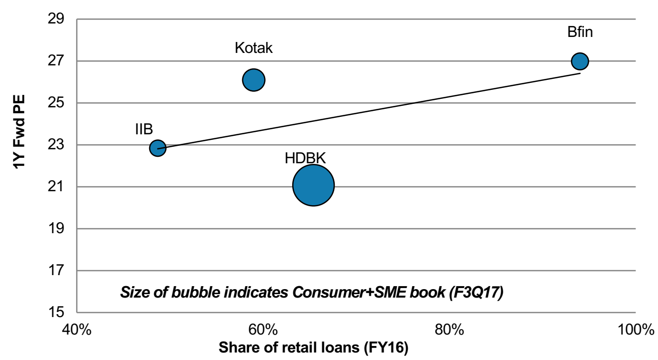
Source: Company Data, Thomson Reuters, Morgan Stanley Research

Exhibit 41: P/E band during the past decade – retail private banks have commanded P/Es of >30x



Source: Company Data, Morgan Stanley Research

Exhibit 42: Share of consumer loans + SME in loan book (~85%) is much higher than retail private banks



Source: Company Data, Morgan Stanley Research

AlphaWise Methodology and Respondent Profile

Survey Objective:

Through the survey, we have sought to understand the preferences and behaviour of the most active Internet user base in India – i.e., the millennials in urban India, The survey covered a wide range of topics including:

1. Impact of the Internet on media usage and shopping behaviour
2. Impact of millennials' Internet usage on elders
3. Preferences for discretionary consumption – vehicle ownership, product purchase, eating out, etc.
4. Personal and Household Financial behaviour & outlook

Survey Design:

Coverage: The survey was conducted in 24 cities across city tiers. We classify the surveyed cities as under:

1. Tier I: 5 M+ population (Top 8 cities in India)
2. Tier II: 1.5-3 M population (Top 9-25 cities in India)
3. Tier III: 0.5-1 M population (Top 26-75 cities in India)

Sample Size & Respondent Profile: The survey was conducted among 3,110 millennials. All survey respondents are in the 18-35 age group from middle class / upper middle class households (socioeconomic classes A, B, C) and are active Internet users

Survey Methodology: The survey was conducted using face to face survey methodology during December 2016 and January 2017.

Survey Representation & Limitations:

1. The survey represents the online urban millennials population in India. We maintained quotas for age, gender, socioeconomic class, education, and occupation to ensure that the survey represents the profile of Internet-using urban millennial population in India.
2. Since the objective was to understand impact of Internet usage on millennials behaviour – we excluded millennials not using Internet and from the lower socio-economic classes.
3. *Statistical Margin of Error:* Findings based on total sample have low margin of error of +/-1.47ppt at 90% confidence level. Findings based on sub-groups will have higher margin of error.

Survey Sample Profile:

Exhibit 43: Town Class (%)

Source: AlphaWise, Morgan Stanley Research

Exhibit 44: Age (%)

Source: AlphaWise, Morgan Stanley Research

Exhibit 45: Gender (%)

Source: AlphaWise, Morgan Stanley Research

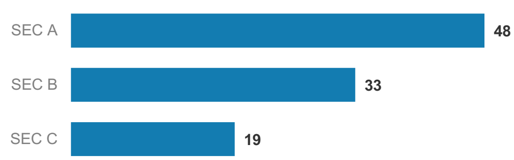
Exhibit 46: Education (%)

Source: AlphaWise, Morgan Stanley Research

Exhibit 47: Occupation (%)

Source: AlphaWise, Morgan Stanley Research

Exhibit 48: Socio-Economic Class (SEC) (%)



Source: AlphaWise, Morgan Stanley Research

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Sector	Analyst	Date
Hardlines	Simeon Gutman	March 29, 2017
Survey Says: Home Furnishing Spending Solid, But Online Taking Share; Expect a Q4 BBBY Comp Miss; Lower PT to $38: Our latest AlphaWise survey among home furnishings shoppers points to continued solid spending; consumers are increasingly shopping the category online		
Multi-Industry	Nigel Coe	March 29, 2017
Survey Says...This Recovery Is On: Our latest US pulse check is bullish with broad based acceleration through March and supportive inventory and capex fundamentals. Part of the acceleration we have been seeing is due to inventories and our survey supports the message that the destocking phase is over.		
Enterprise Software	Keith Weiss	March 24, 2017
Tax Season Update: Gaining Momentum After a Slow Start – Will It Be Enough?: AlphaWise web research suggest a potentially weaker tax season for online and desktop software tax service providers compared with last year.		
Internet/New Media	Brian Nowak	March 23, 2017
What's in Your Wallet? Amazon?: Our AlphaWise survey shows a new credit card for a major online retailer presents a potential threat to other retailers, as card adopters intend to shift more spend toward the major retailer. There is also a potential new risk to retailers' wallet share and profit and an intensified promotional environment for retailers and card companies.		
Consumer	Nillai Shah	March 23, 2017
The Millennial Series: Unique Insights into the Future of Indian Consumption: Our second report in India Millennials Series using AlphaWise evidence - with rising incomes, millennials are likely to increase spending on discretionary consumption segments like entertainment/eating out and personal grooming. Consumer staples companies, on the other hand, may face challenges in recruiting highly digitally influenced and yet price-conscious consumers.		
Russian Retail and Macro	Nida Iqbal Ahmed	March 21, 2017
Green shoots of recovery but competition mounting: Why have the Russian food retailers underperformed YTD? Our fifth annual AlphaWise survey suggests a consumer stabilisation, with a glimmer of recovery. However, our proprietary AlphaWise store mapping suggests competition is hotting up.		
Enterprise Software	Keith Weiss	March 21, 2017
4Q17 Preview: Will Q4 Strength Carry Forward to FY18 Guidance? Survey Says No: Our latest quarterly survey among resellers of subscriptions for the support, training, and integration services of open source software shows a weaker outlook for FY18		

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	COVERAGE UNIVERSE		INVESTMENT BANKING CLIENTS (IBC)			OTHER MATERIAL INVESTMENT SERVICES CLIENTS (MISC)	
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Overweight/Buy	**1168**	**36%**	**303**	**43%**	**26%**	**556**	**37%**
Equal-weight/Hold	**1403**	**43%**	**307**	**44%**	**22%**	**692**	**46%**
Not-Rated/Hold	**59**	**2%**	**9**	**1%**	**15%**	**8**	**1%**
Underweight/Sell	**620**	**19%**	**83**	**12%**	**13%**	**264**	**17%**
TOTAL	**3,250**		**702**			**1520**	

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