PFC will usually be the lead lender on any power project. Any project that PFC does not lend on will be a tricky loan to get done, because the other lenders will look to PFC—and they have a couple of thousand specialists working for them—to give a lead in terms of, 'Is this project feasible, doable, quantifiable in terms of money and time?'"

Operating under the sovereign umbrella, PFC is a low-cost lender, Thorn adds. For the same reason, it tends to get repaid. Then, too, "you're almost guaranteed top-line growth, because they're lending into a fast-growing sector, i.e., power projects."

Peligal pressed Thorn for the bear story; no company trading at four times the estimate is without one. Thorn replies that the market is worried about credit stresses. It is concerned that, in case of a meltdown of the rupee, PFC's foreign borrowings would become crippling (though the currency has rallied by 15% from last summer's lows). Finally, some fret that the government will coerce the company into lending against bad projects for political reasons. "So far it has not done this," Thorn says. "Why would it start now?"

"I recently had a meeting with one of my ex-investors," Thorn says in conclusion, "and he gave me a 35-page report from Credit Suisse saying how the Indian banking system is going to hell and back—and actually wasn't coming back at all without a lot more capital. I sat there and told him that all this was completely wrong. There are plenty of people out there who will tell you radically, diametrically the opposite story to our view. I think our investors, who have suffered with having 50% exposure to banks when nobody wanted to own banks—everyone wanted to own software, pharma and consumer staples (we don't own any of these)—our investors would say to us, 'When will the banks start to work?' And our answer is that they never stopped working, it's just that nobody has noticed. So the question we often get is, 'Why do you have this extreme portfolio allocation?' And the simple reason is that it's the best and cheapest growth in the market. Where else can you go to find something at four times earnings trading for less than book and yielding more than 5%? Those are not the characteristics of Blue Dart Express [at 52 times the estimate]—never have been, never will be."

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Upside breakout on heavy volume

(May 30, 2014) "Bullish" isn't a word that suits every vegetarian, but it fits the new prime minister of India to a "T." Narendra Modi, who won the world's largest election not so much in a landslide as in an earthquake, has already achieved the seemingly impossible. "For the first time ever," to quote Sadanand Dhume in the May 19 *Asian Wall Street Journal*, "India's traditionally left-leaning politics has moved decisively to the right." The meaning of this signal event for the readers of *Grant's* is the subject at hand.

We would say, skipping down to the bottom line, that the Modi triumph is bullish for India's stocks, bonds and currency. It is bullish for the long run as well as for the medium run. As for the short run, Power Finance Corp., the Indian non-bank finance company featured in these pages on April 4, has rallied by 56%. Since May 9, when a leaked exit poll tipped the prospect of a transformation of India's politics, the broad Indian market has rallied by almost 7%. Taking a broader view of the situation, we would call the election results bullish for even that 83% of the world's seven billion people who do not happen to carry an Indian passport. India may or may not redeem your editor's hopes of becoming the world's next big growth story. At least now—perhaps more than at any time since independence—it has the opportunity.

Inconsiderately, the British left behind their ideological baggage when they sailed away in 1947. Adopting the Brits' Fabian socialism as its own, India's Congress Party proceeded to govern for all but 13 of the next 67 years according to the doctrine that the state knows best. More than a personal achievement, Modi's election was a triumph for the idea that the individual can—or may or at least could—know better than politicians, ministers and license-dispensing bureaucrats set over him to rule.

What the term "right" may mean in practice in Indian politics remains to be seen. At a minimum, it means not left: not the incentive-quashing and initiative-dampening statism of the Nehrus and Gandhis, still less the aspirational collectivism of the once-influential (now happily marginalized) Indian communists. Candidate Modi promised that, if elected, he would achieve "more governance, less government." Hopeful words, perhaps, but still only a slogan.

Americans, ever prone to see the world through the narrow prism of their own experience, will likely draw comparisons between Narendra Modi and Ronald Reagan—bullish comparisons, if the Gipper is your cup of tea. Modi in 2014, like

Now less cheap

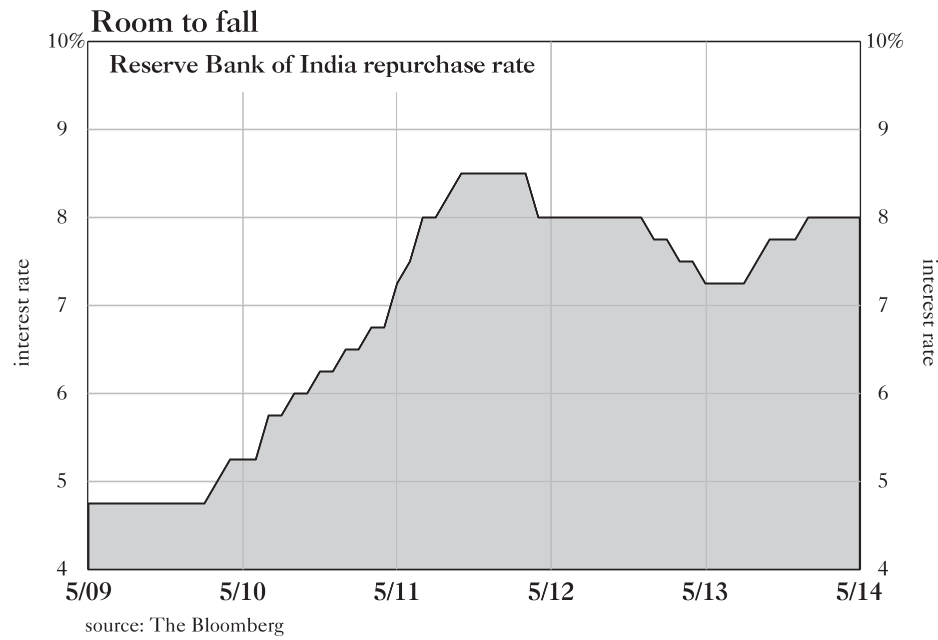
source: The Bloomberg

Reagan in 1980, ran against the government and resoundingly won. India today, like America in 1980, was beset by inflation, slow growth and constricting interest rates. Come the moment, come the man.

In America, the moment painfully dawdled. Between the end of January 1981 and the end of July 1982, the S&P 500 dropped by 17.3% (dividends cushioned the blow to a decline of only 10.1%). Interest rates did eventually fall, but first they rose, the 30-year Treasury bond reaching its alpine high in yield—no less than 15%—and low in price at the close of September 1981, eight months after the District of Columbia's sanitation workers finished sweeping up the inaugural confetti.

Harmony was not the outstanding interpersonal characteristic of the Republican band of brothers. The supply-siders quarreled with the fiscal conservatives and the monetarists with both. The Treasury sniped at the Federal Reserve (which would not lower interest rates as fast as the administration wished them to fall). The fondest hopes of the conservatives were never realized: President Reagan did not slay the federal bureaucracy, much less balance the budget or institute a new monetary regime based on the Hamiltonian precepts of gold and silver convertibility. And yet, over the course of the often fractious, ideologically impure eight Reagan years, the S&P logged a compound annual rate of growth of 14.9% (with dividends reinvested), the GDP of 3.5%.

As we go to press on Day 2 of the Modi incumbency, the Indian stock market has started to pull back from its furious pre-election rally. The prime minister's new finance minister, Arun Jaitley, has met with the governor of the Reserve Bank of India, Raghuram Rajan, who gave no immediate sign of concurring with many in the Mumbai investment community that India's inflation is not a monetary problem but rather a political and legal and infrastructure-related one. Anyway, the central bank's repurchase rate, which Rajan has thrice boosted since taking office last year, remains just where it was before he and Jaitley shook hands—i.e., 8%—not far from the measured rate of Indian consumer price inflation.



Recalling the long elapsed time in America between the electoral results of 1980, on the one hand, and the subsequent economic and financial payoff, on the other, this publication is inclined to be patient with India. Besides, a number of positive trends are already in place. The fiscal deficit has fallen to 4.1% of GDP from a high of 5.8% in fiscal year 2012. The current account deficit has plunged to less than 1% of GDP from 6% in December 2012. Bullish we are.

Perhaps more so is Jon Thorn, manager of India Capital Fund, a London-based private partnership (*Grant's*, April 4). The elections, Thorn observes, were well and truly momentous. "Firstly," he says, "it's the highest turnout ever—66.4% participation. If you get a higher percent of turnout than even the first election after independence, that's pretty remarkable. Secondly, it's the first time that any single party has crashed through the 272 number of [parliamentary] seats to be an absolute majority. That hasn't happened for 30 years. Thirdly, outside of the statistics of this election, what you have is a very unusual demographic event. Because this is a thing that many people misunderstand about India. Everyone talks about the so-called demographic dividend, and this is absolutely right. What that means is that you get an ever larger percentage of the population who works—as opposed to a higher dependency ratio, where you get a lower one."

Another demographic wrinkle, Thorn points out, is that the age of the average Indian voter is falling, not rising, as it is in Japan and Europe and the United States. What the young want is work and opportunity, not—at least for the time being—a fat government pension. Modi is a most unusual politician, all concur. For Thorn, he is a kind of Hindu Napoleon: "Napoleonic in a very good sense of what he wants to achieve—in the sense that he has a constructive mission to transform India. Mr. Modi is now campaigning for five years from now. He wants to go into that election, in 2019, with the ability to say, 'This is what I've achieved for you. Vote me back.' . . . [B]ecause he has the extraordinary mandate that he has, it's impossible at this point for anyone to say, oh no you really can't do that, because it's not the Indian way, it's not the Hindu way. It's not the way we do it in this region, in this culture, it's not the way we've done it in this ministry for the last 60 years. Because he has a mandate the likes of which nobody has had before, to change pretty much everything, there's a real sense, coming back to the Napoleon part of it, the positive construction, he sees himself and he has been seen by many as a historically transformative figure."

A curious feature of Indian business, Thorn winds up, is that, while ROEs are high (15.3%, according to Morgan Stanley), profit margins sit at decade lows. Indeed, because pharmaceuticals, IT services and consumer staples enjoy relatively stable margins, the effective ratio of earnings to sales for the more volatile kind of Indian enterprise must be deeply depressed. "There's no reason why profit margins can't continue to grow through the other side of the trough," says Thorn—"i.e., in three to five years. That's why, in my view, we're only at the beginning of a secular recovery. Most people's assumptions about GDP growth, which has come down from 11% to 5%, and about revenue and earnings—they're all in my view far too low. I can't prove that to you; we can only see the actual results and I'll either be right or wrong. But in my view, everything is too low. All of our assumptions are too low. I just think this is one of the classic recovery stories."

We shall meditate on that.

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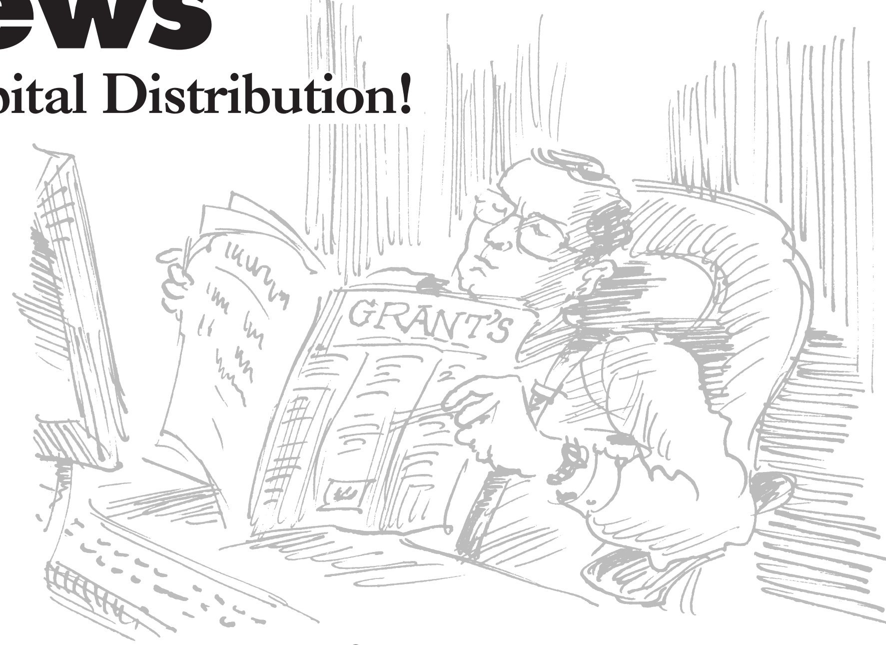

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