



Tapping Into the Indian Consumer Market

The India-Europe Investment Forum

28 June 2007

HOW WILL INDIA'S CONSUMER MARKET EVOLVE IN THE FUTURE?

India's economy has been growing rapidly ...

- What impact has growth had on Indian incomes and how quickly will they grow in the future?
- How is the distribution of income changing? When will its middle class take off?
- How is income growth effecting urban versus rural areas?
- How much of rising Indian incomes will be spent versus saved?
- What will Indian consumers spend their newfound wealth on?



What does this mean for business and investment opportunities?

How should companies compete for the "new Indian consumer"?



OUR PANEL



- **Prashant Desai** – Group Head, Investor Relations and New Ventures (PE), Pantaloon Retail (India) Limited
- **Richard Fairgrieve** – Director of Global Emerging Markets, WestLB Mellon Asset Management
- **Dippankar S. Haldar** – Chief Executive Officer, Wadhawan Food Retail (P) Limited
- **A.P. Parigi** – Managing Director and Chief Executive Officer, Entertainment Network (I) Limited
- **R. Subramanian** – Managing Director, Subhiksha Trading Services

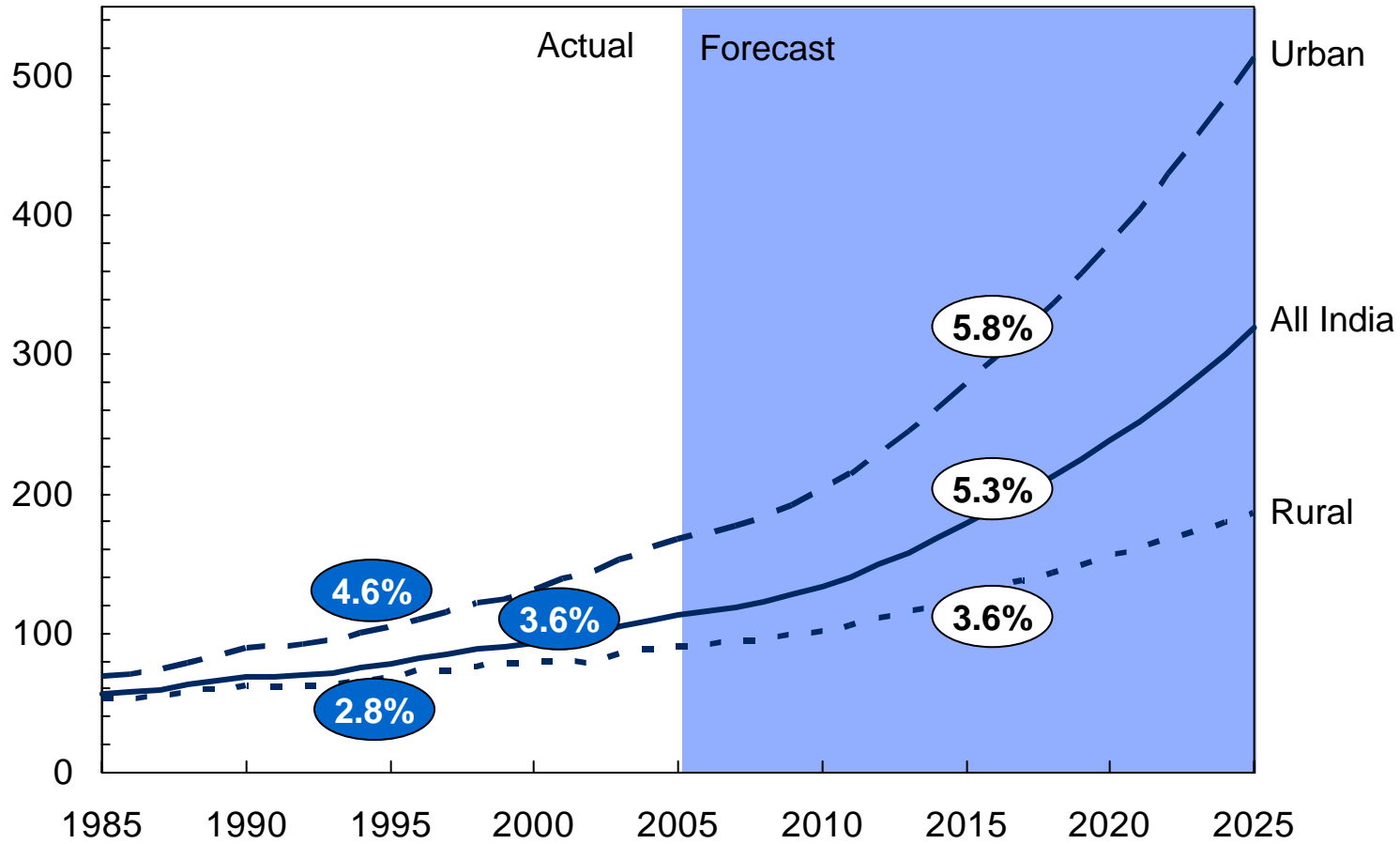
KEY FINDINGS FROM MCKINSEY GLOBAL INSTITUTE RESEARCH

- Indian incomes will triple over the next two decades, significantly reducing poverty
- India will emerge as the world's fifth largest consumer economy
- A large urban middle class will develop, but rural areas will benefit too
- Patterns of consumption will shift rapidly towards discretionary spending
- Income and consumption growth will create opportunities and challenges for business and government

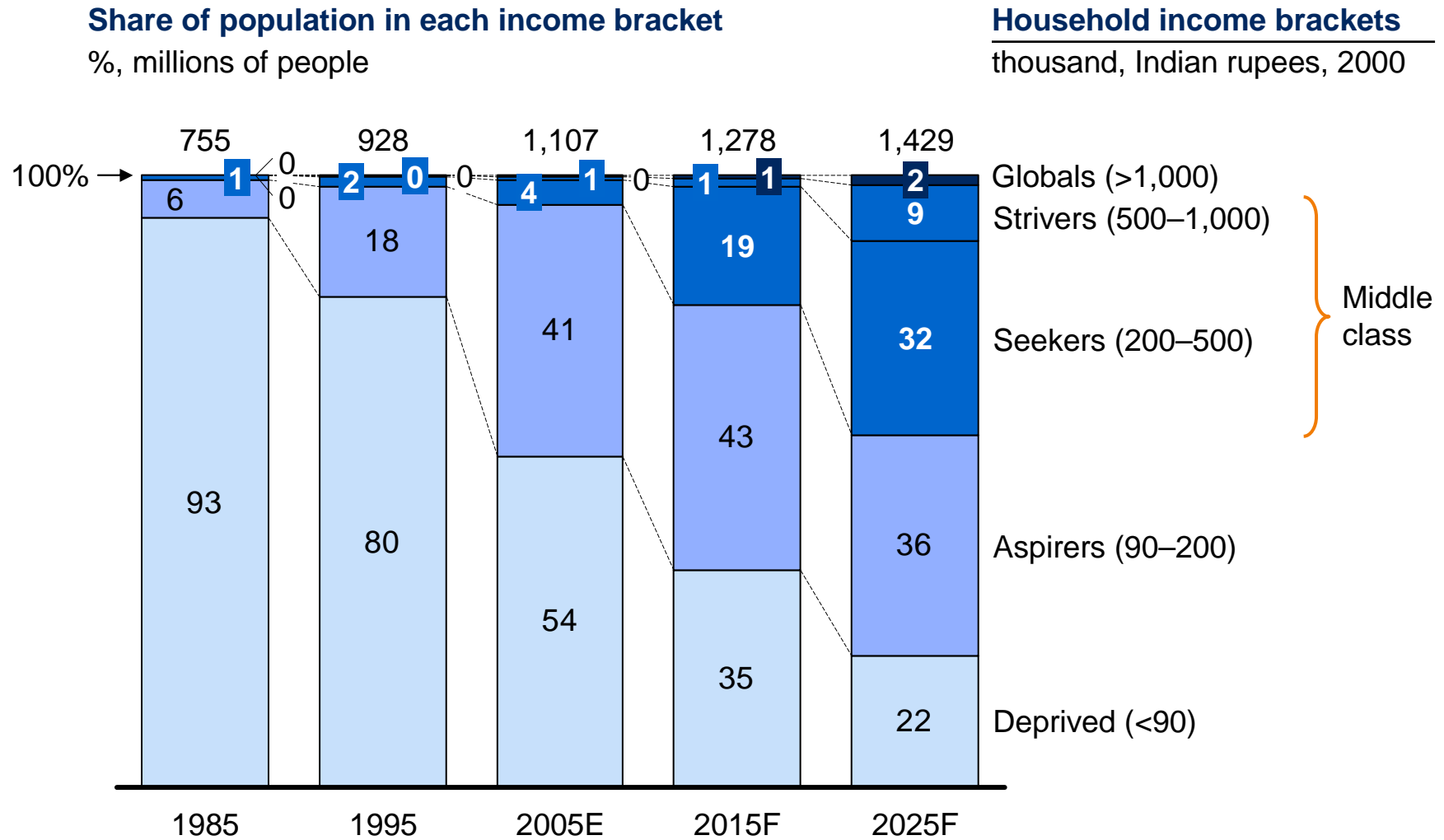
HOUSEHOLD INCOME GROWTH WILL ACCELERATE ACROSS INDIA

Average household disposable income
thousand, Indian rupees, 2000

Compound annual growth rates
 1985–2005
 2005–2025



INDIA WILL SEE CONTINUED REDUCTION IN POVERTY AND GROWTH OF ITS MIDDLE CLASS



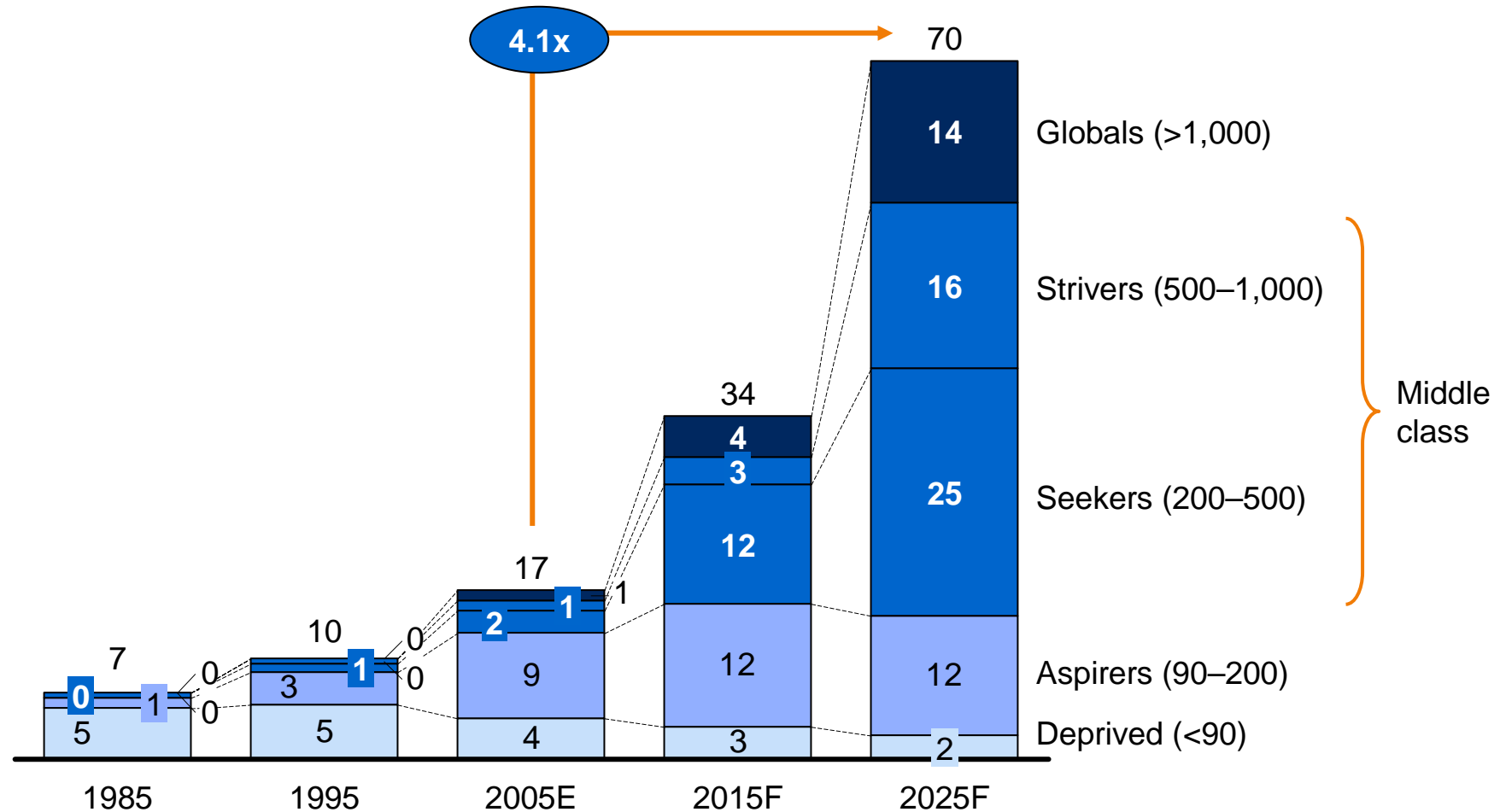
Note: Figures are rounded to the nearest integer and may not add up to 100%.

Source: McKinsey Global Institute

INDIA'S AGGREGATE CONSUMPTION WILL QUADRUPLE OVER THE NEXT 20 YEARS

Aggregate consumption across income brackets
trillion, Indian rupees, 2000

Household income brackets
thousand, Indian rupees, 2000



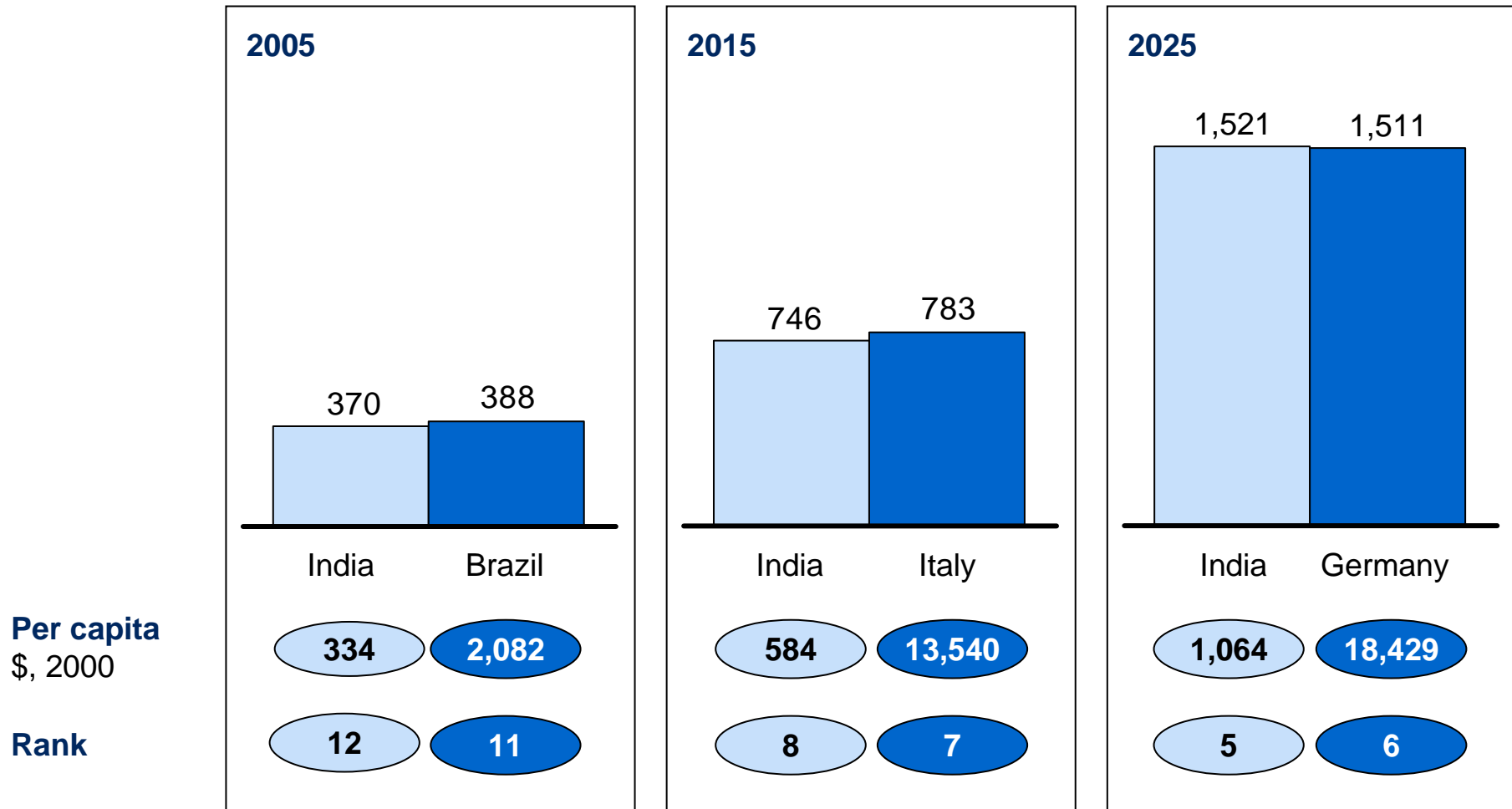
Note: Figures are rounded to the nearest integer and may not add up exactly to column totals.

Source: McKinsey Global Institute

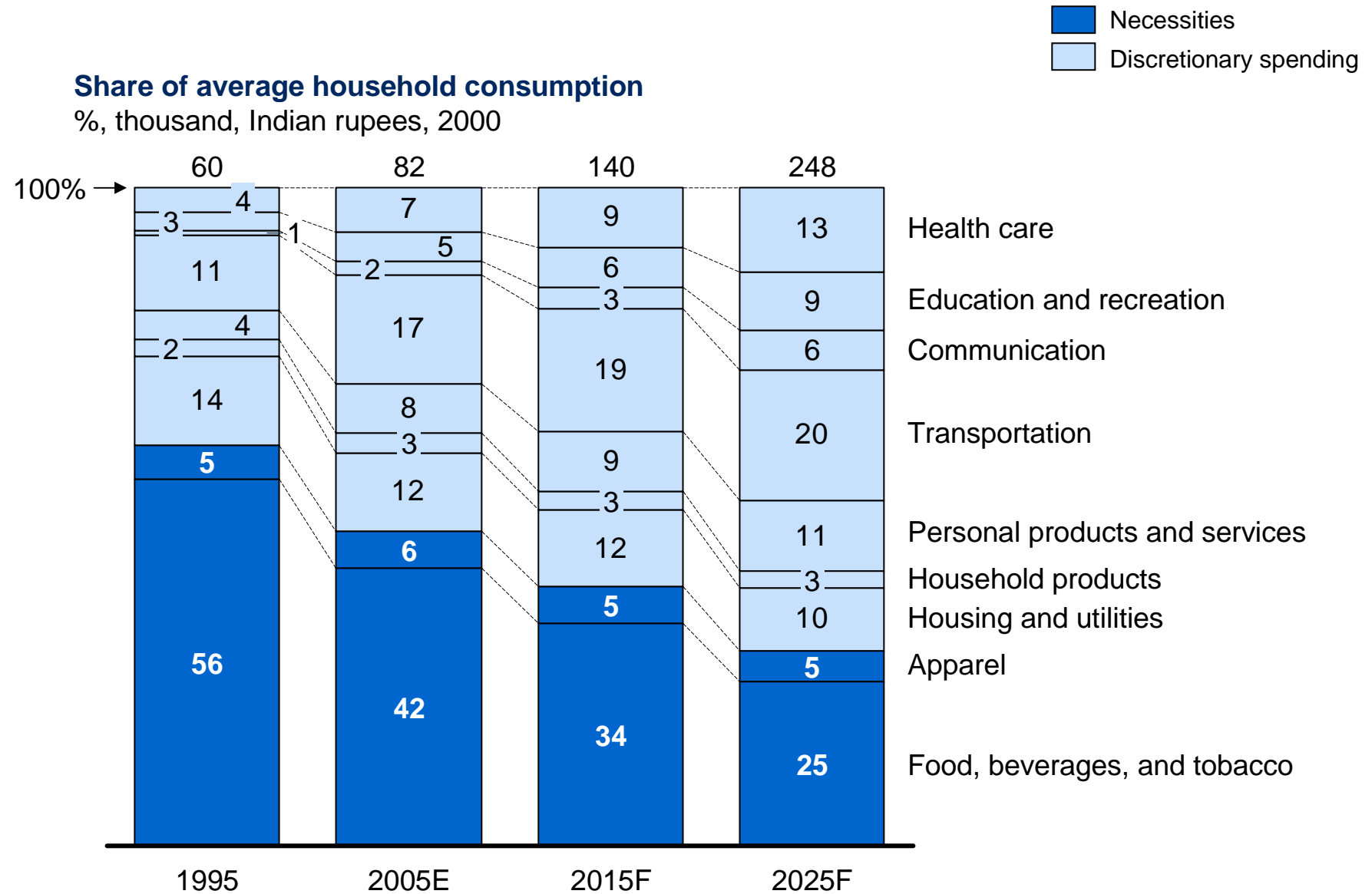
INDIA WILL BECOME THE FIFTH LARGEST CONSUMER MARKET IN THE WORLD BY 2025

Aggregate private consumption, 2005–2025

billion, \$, 2000



INDIA'S SHARE-OF-WALLET IS SHIFTING AS INCOMES RISE



Note: Figures are rounded to the nearest integer and may not add up to 100%.

Source: McKinsey Global Institute



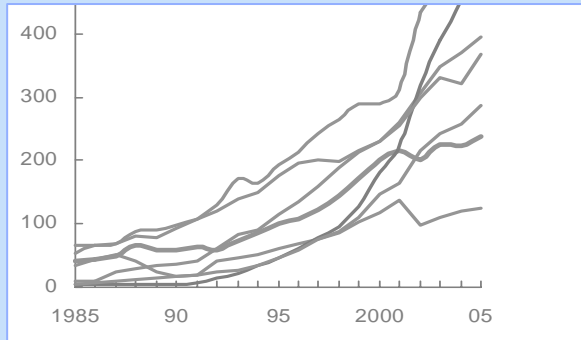
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Back-up

THE MCKINSEY GLOBAL INSTITUTE (MGI) HAS SPENT THE PAST YEAR EXAMINING THE FUTURE OF THE INDIAN CONSUMER MARKET



Proprietary database 1985–2005

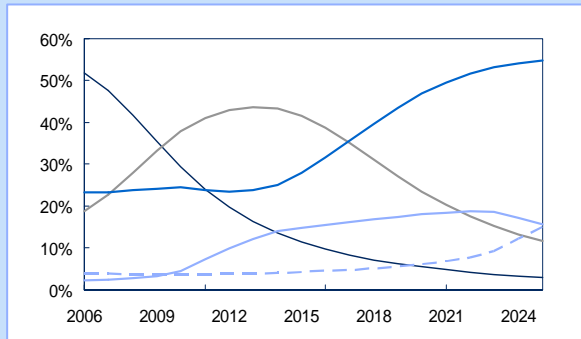
- Exclusive access to NCAER 300,000 household MISH survey
- Government NAS, NSS, and RBI data
- Other sources, e.g., UN, World Bank, Oxford Economics



Econometric forecasting model 2006–2025



On-the-ground insights from McKinsey experience



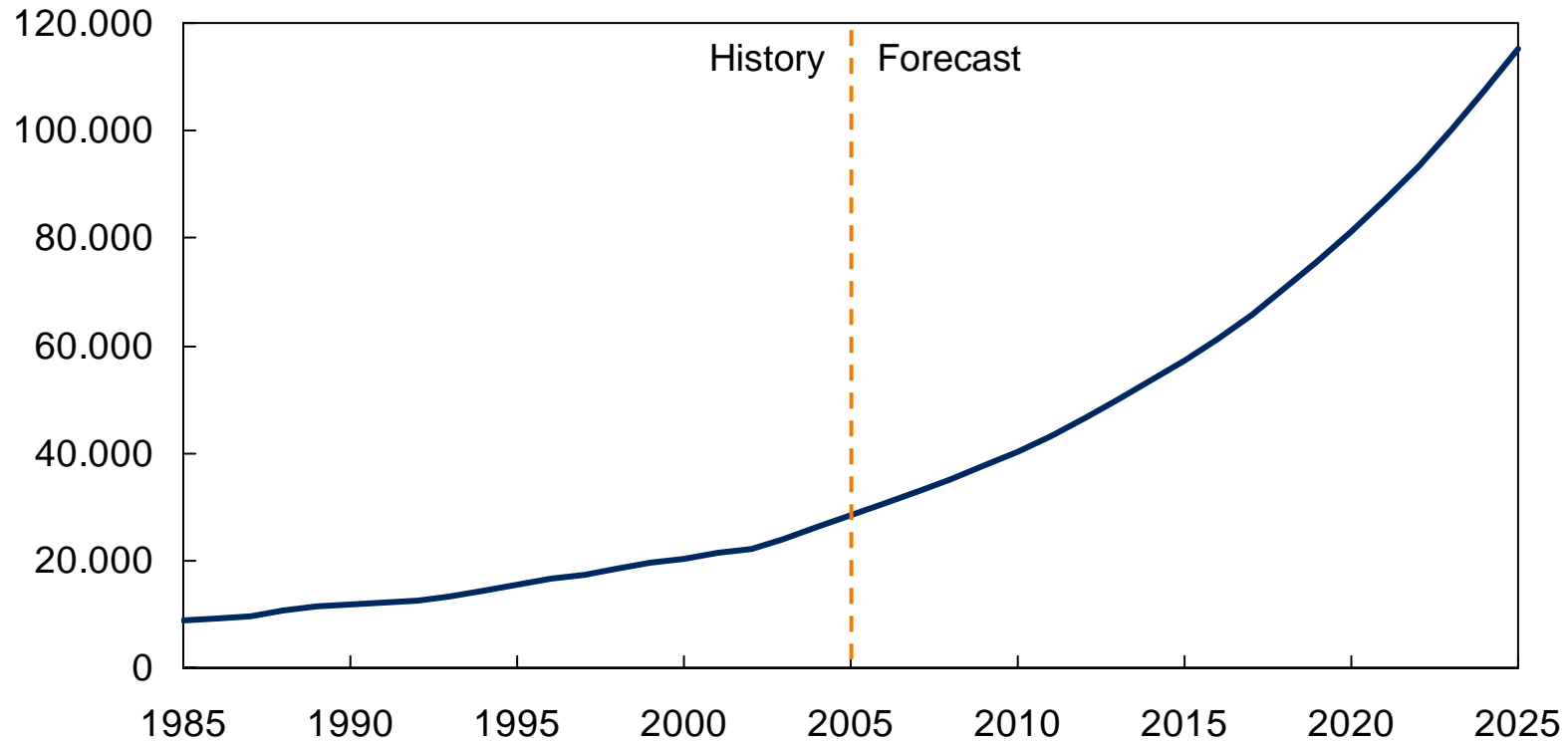
What makes our work unique?

- Focuses on future consumption
- Covers 100% of demand
- Includes detailed income distributions
- Integrates macroeconomic scenarios

MGI's FORECAST ASSUMES 7.3 PERCENT COMPOUND ANNUAL GDP GROWTH

Real GDP

billion, Indian rupees, 2000



Overall compound annual growth

6.0%

7.3%

Per capita compound annual growth

4.0%

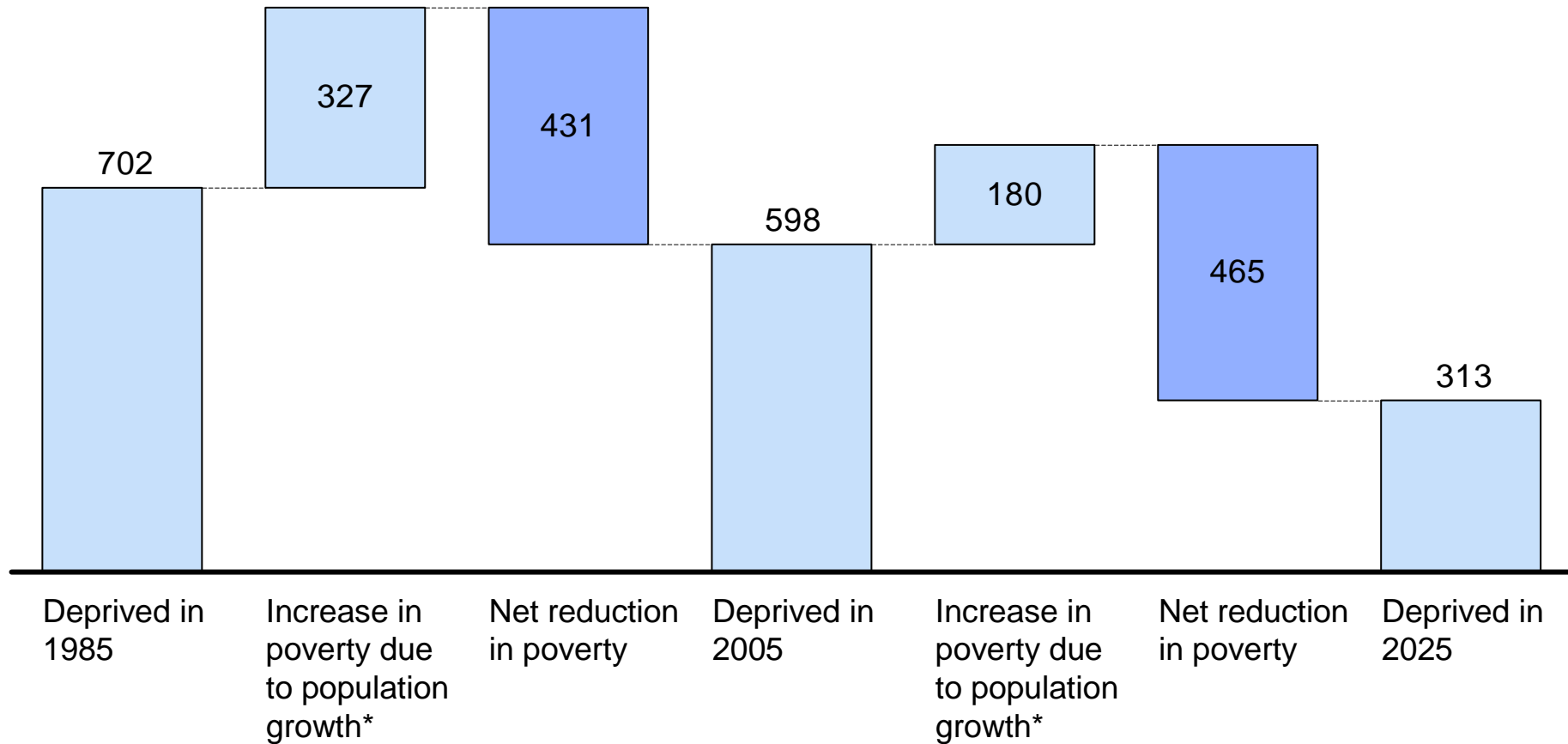
5.9%

KEY FINDINGS

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- Income and consumption growth will create opportunities and challenges for business and government

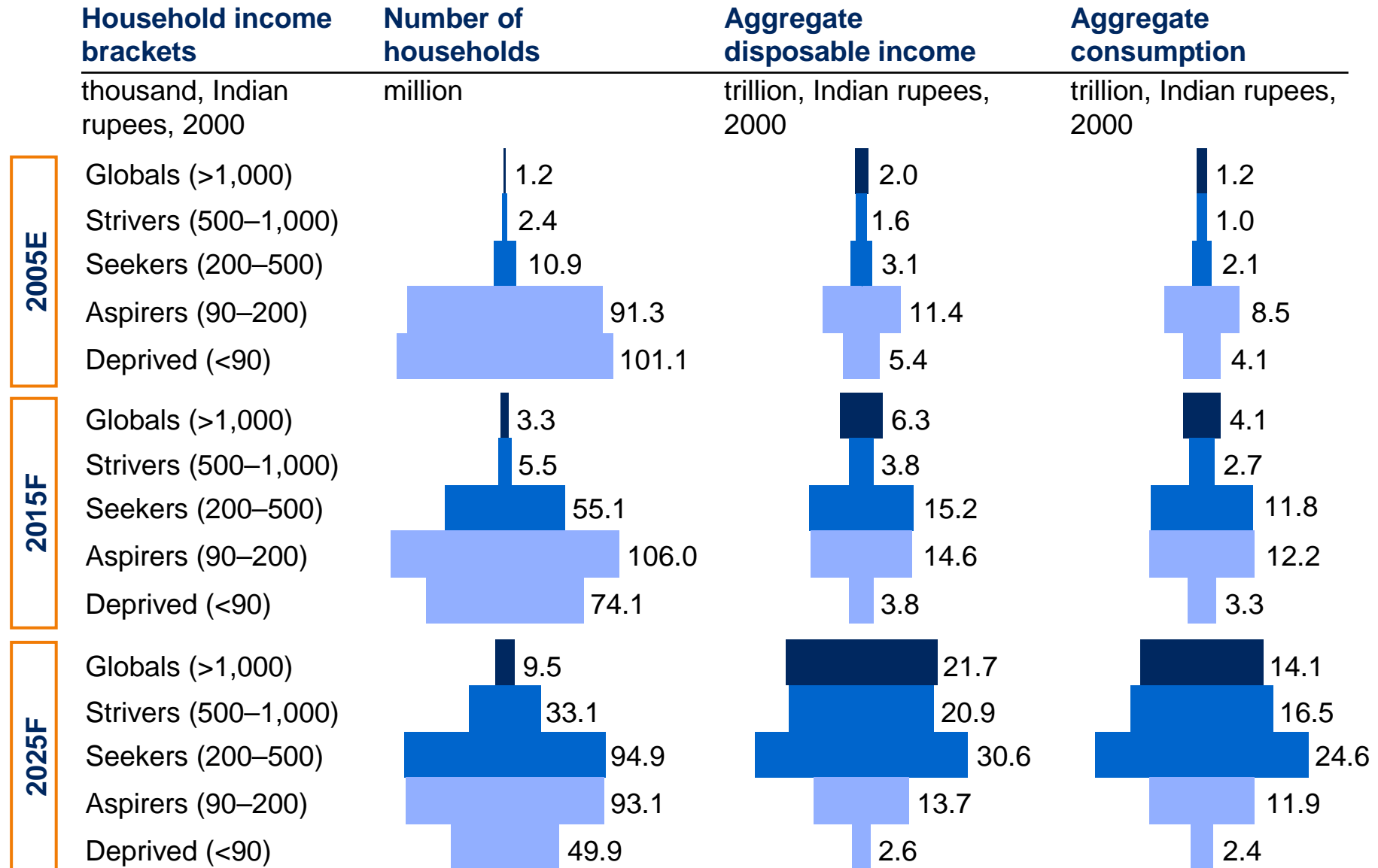
GROWTH HAS LIFTED 431 MILLION FROM POVERTY AND COULD LIFT 465 MILLION MORE

Population in households with annual disposable income less than 90,000 Indian rupees, 2000
millions of people



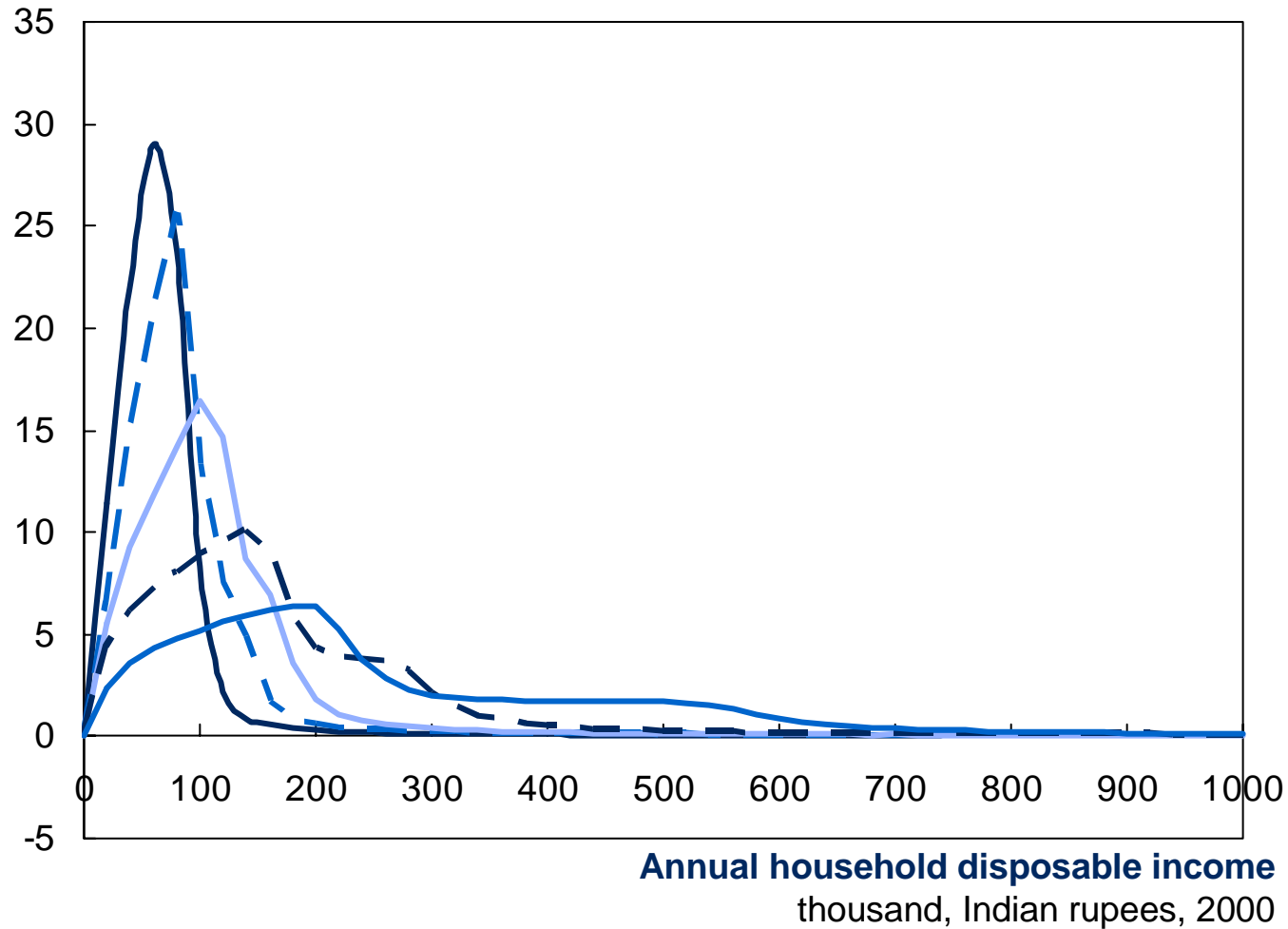
* Number added to deprived if poverty remained at 1985 and 2005 rates respectively

THE SHAPE OF INDIA'S INCOME PYRAMID WILL CHANGE DRAMATICALLY AS INCOMES GROW



THE INCOME DISTRIBUTION IN THE COUNTRY WILL WIDEN AS POVERTY FALLS AND THE MIDDLE CLASS GROWS

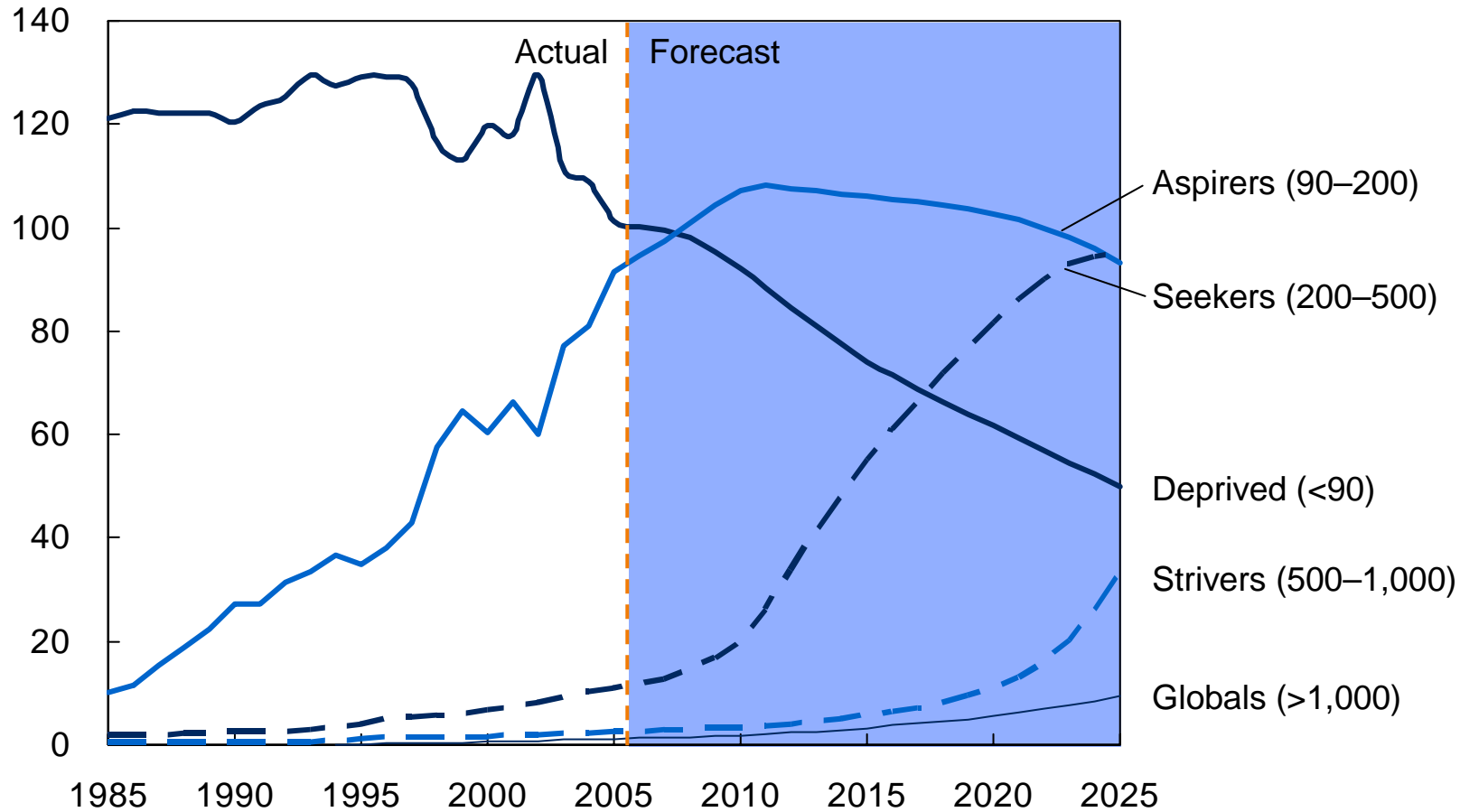
Distribution of household income
% of households



FIRST ASPIRERS AND THEN SEEKERS WILL BECOME THE LARGEST INCOME BRACKETS

Number of households in each income bracket
millions of people

Household income brackets
thousand, Indian rupees, 2000

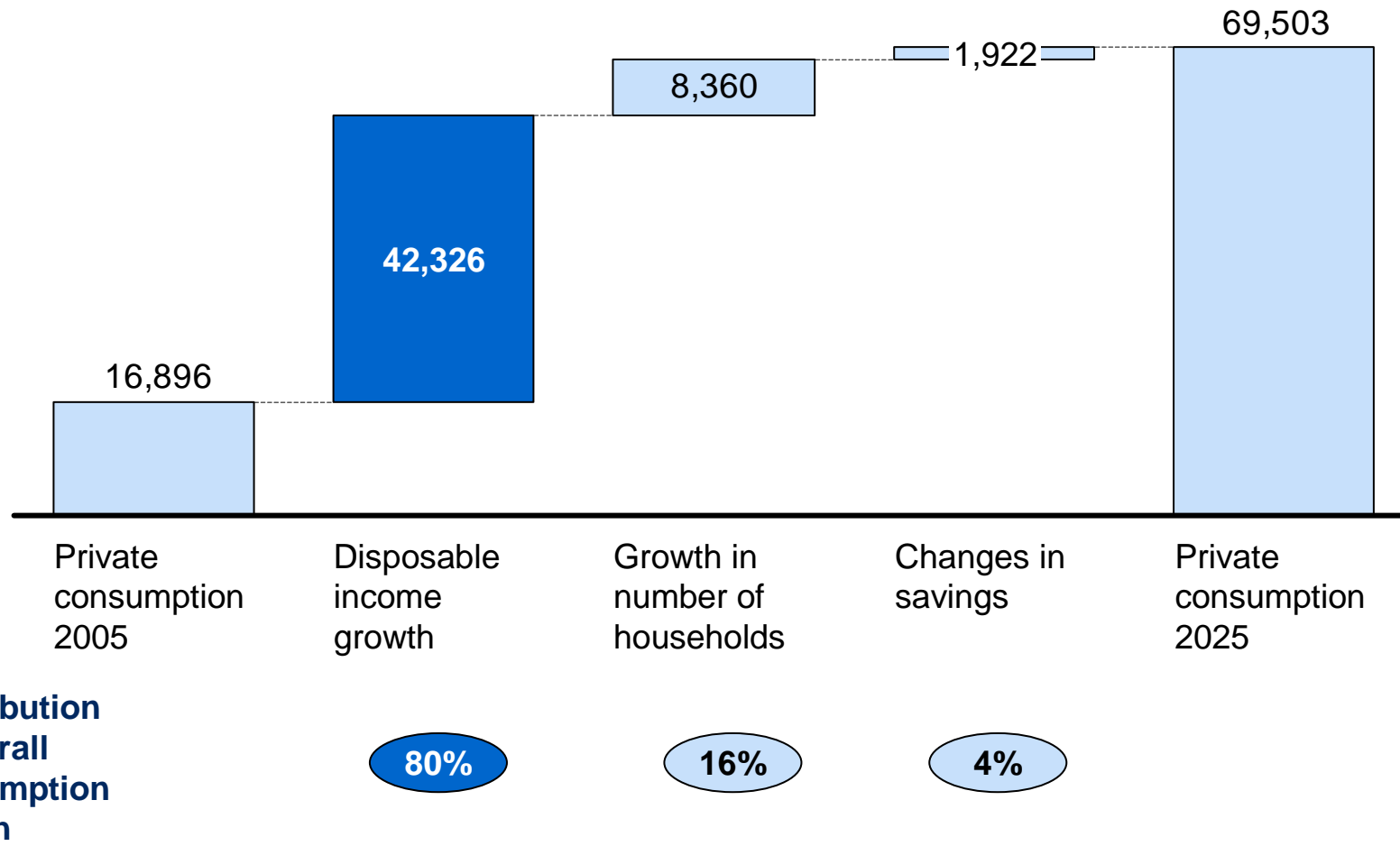


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RISING HOUSEHOLD INCOMES WILL BE THE KEY DRIVER OF CONSUMPTION GROWTH NOT CHANGES IN SAVINGS

Sources of growth in private consumption 2005–2025
billion, Indian rupees, 2000



Note: Figures are rounded to the nearest integer and may not add up to 100%.

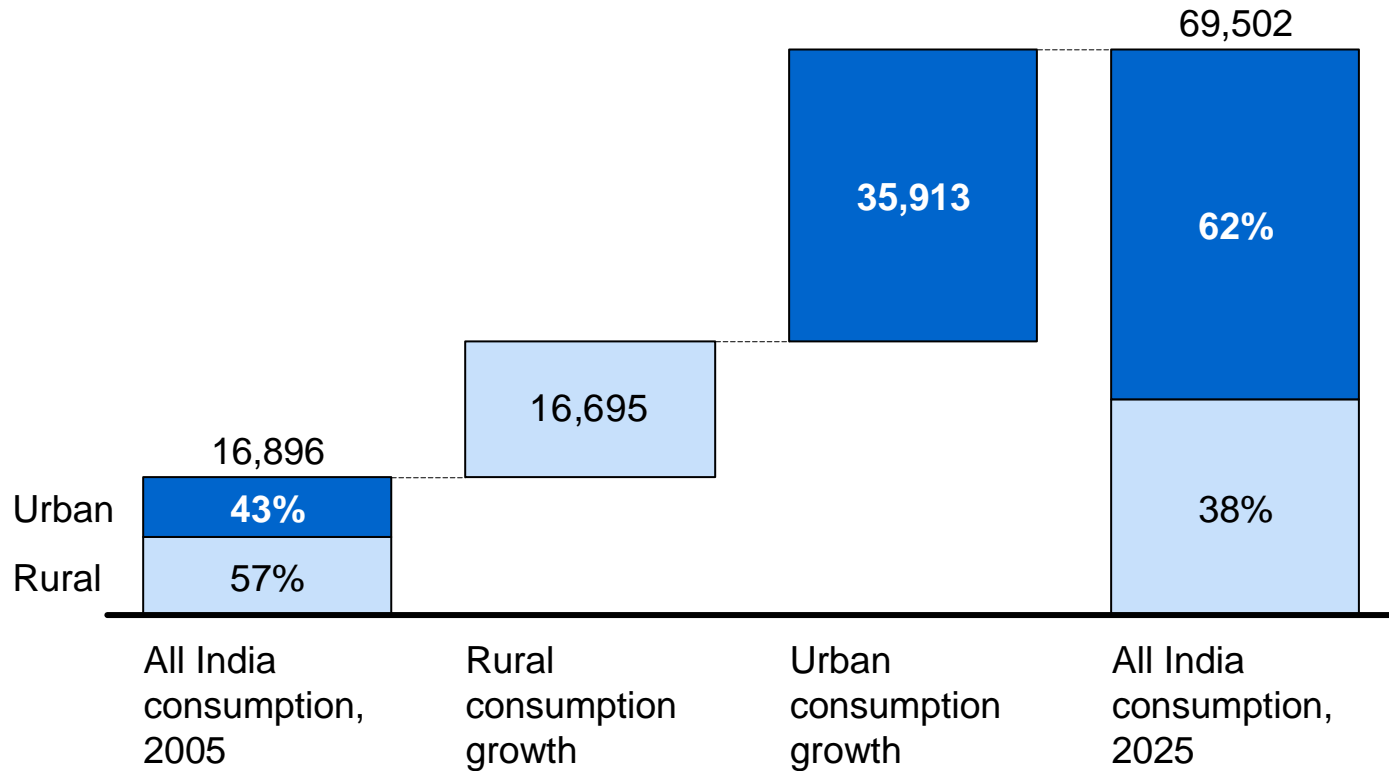
Source: Oxford Economics; UN; McKinsey Global Institute

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URBAN INDIA WILL ACCOUNT FOR MORE THAN TWO-THIRDS OF CONSUMPTION GROWTH OVER THE NEXT 20 YEARS

Aggregate annual consumption
billion, Indian rupees, 2000

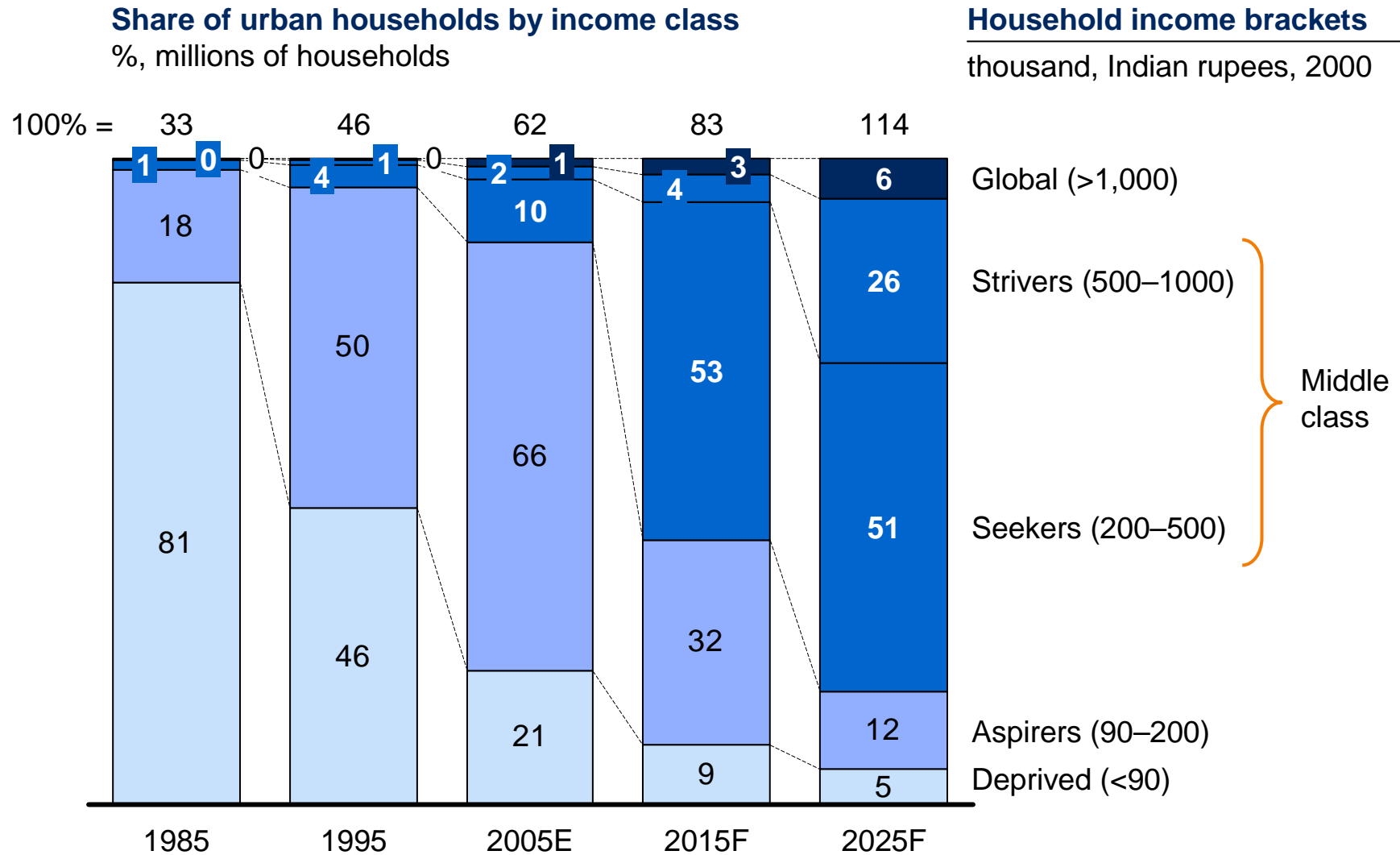


Contribution to consumption growth

32%

68%

MIDDLE CLASS HOUSEHOLDS WILL DOMINATE URBAN INDIA



Note: Figures are rounded to the nearest integer and may not add up to 100%.

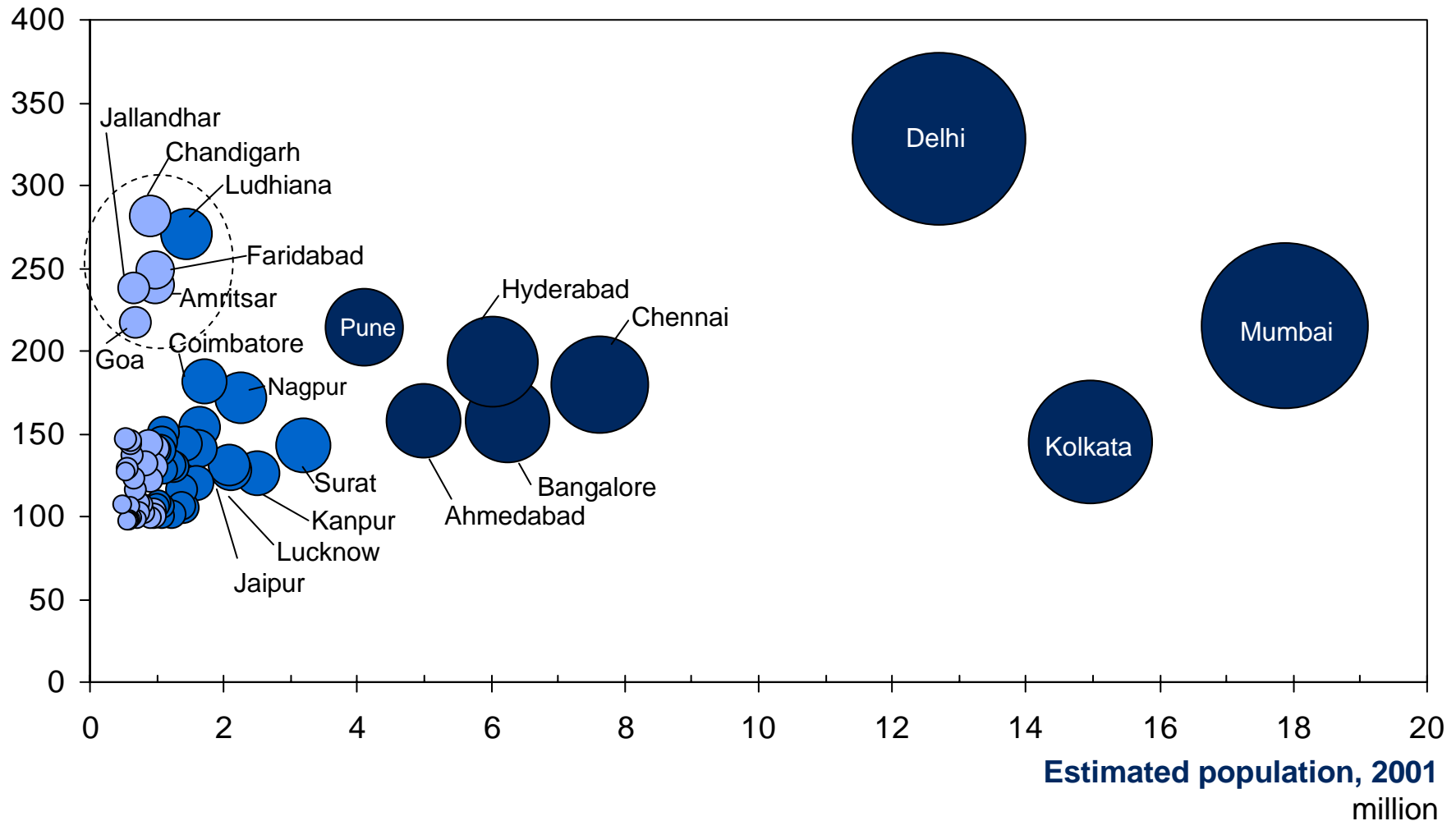
Source: McKinsey Global Institute

LARGE CITIES TEND TO HAVE HIGHEST INCOMES, BUT SMALL 'NICHE' CITIES PROSPERING TOO

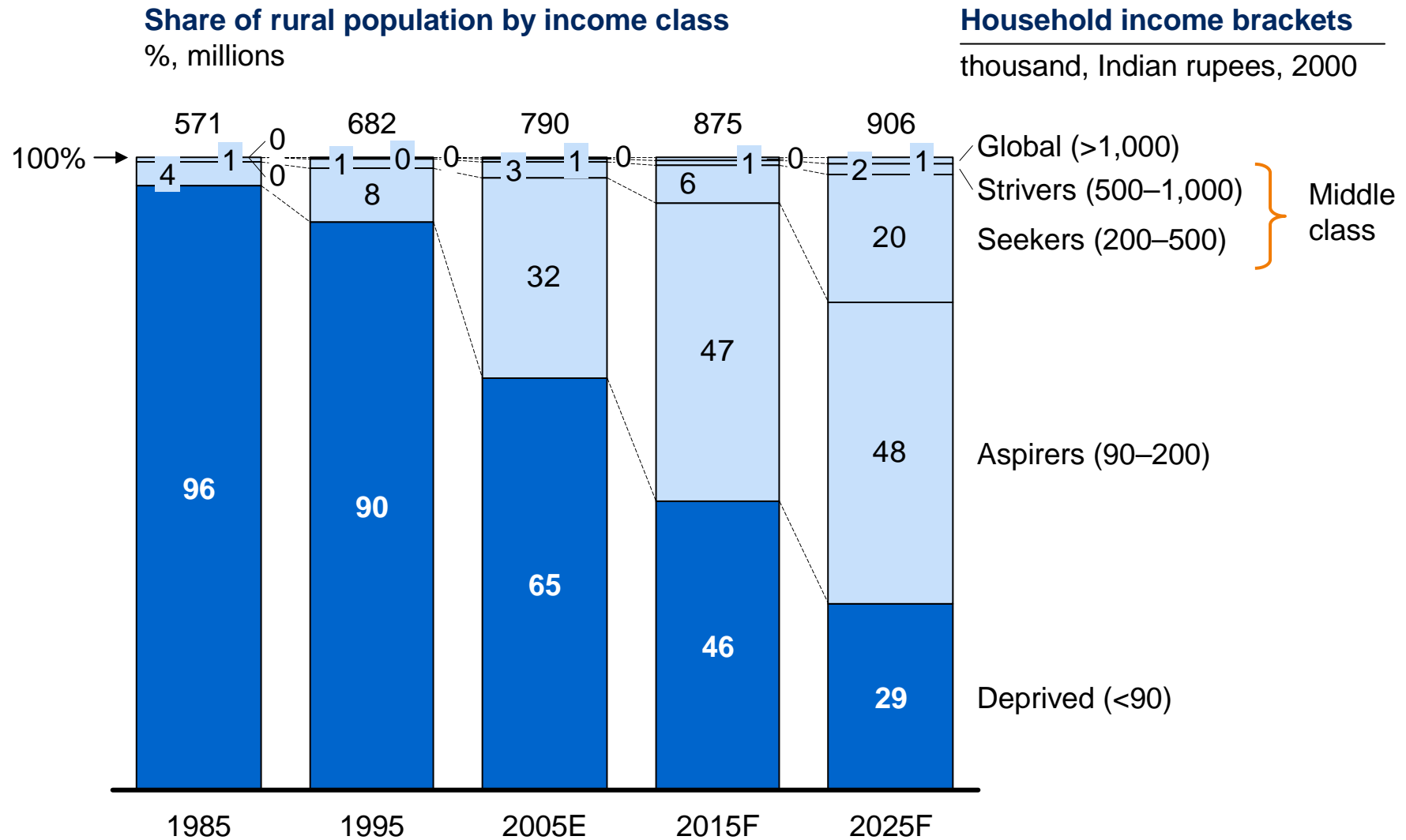
Average annual household disposable income, 2001
thousand, Indian rupees, 2000

Total disposable income
billion, Indian rupees

- Tier 1
- Tier 2
- Tier 3
- Niche cities



RURAL POVERTY WILL DECLINE SIGNIFICANTLY BY 2025

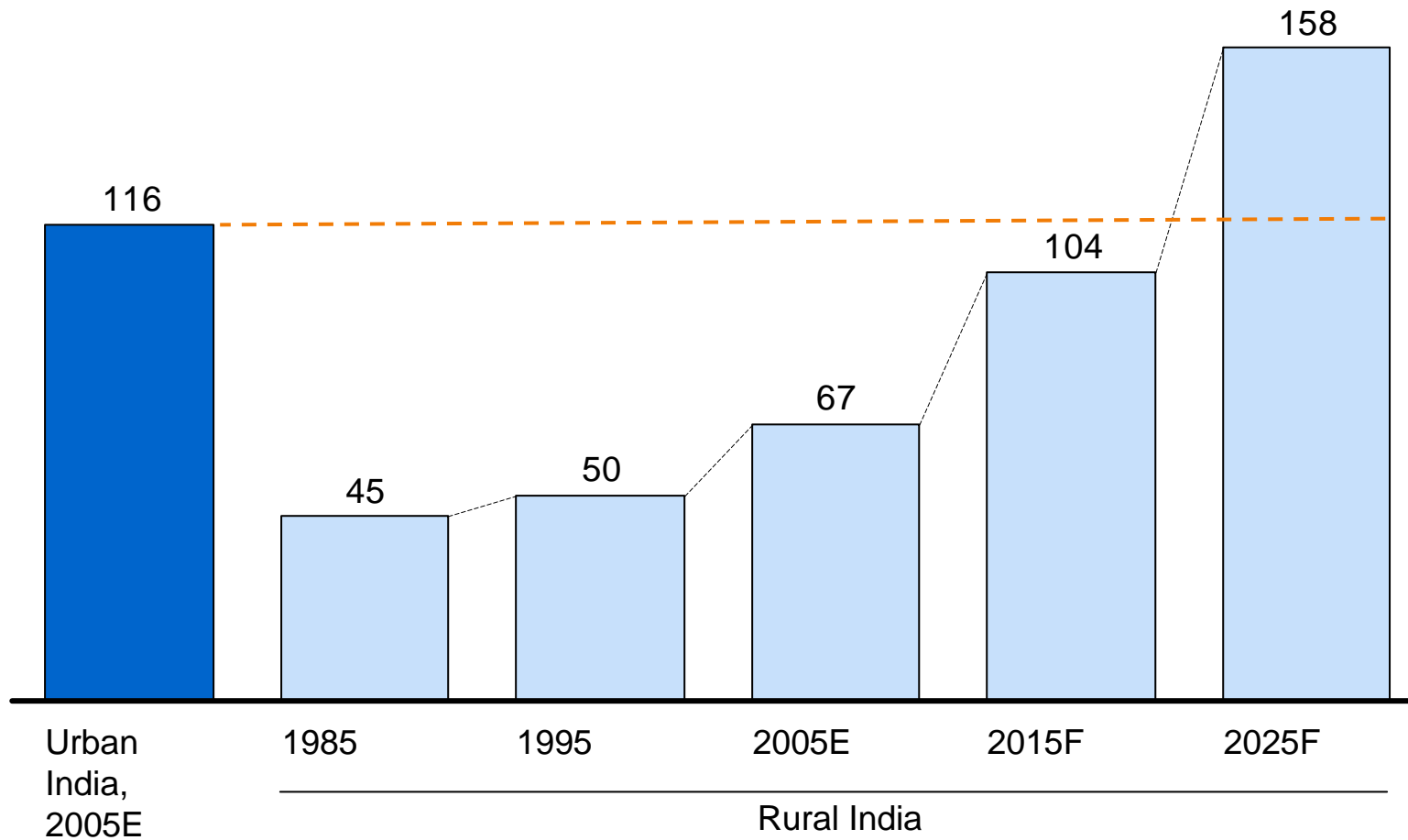


Note: Figures are rounded to the nearest integer and may not add up to 100%.

Source: McKinsey Global Institute

PER-HOUSEHOLD CONSUMPTION IN RURAL INDIA WILL REACH TODAY'S URBAN LEVELS BY 2017

Average consumption per household
thousand, Indian rupees, 2000

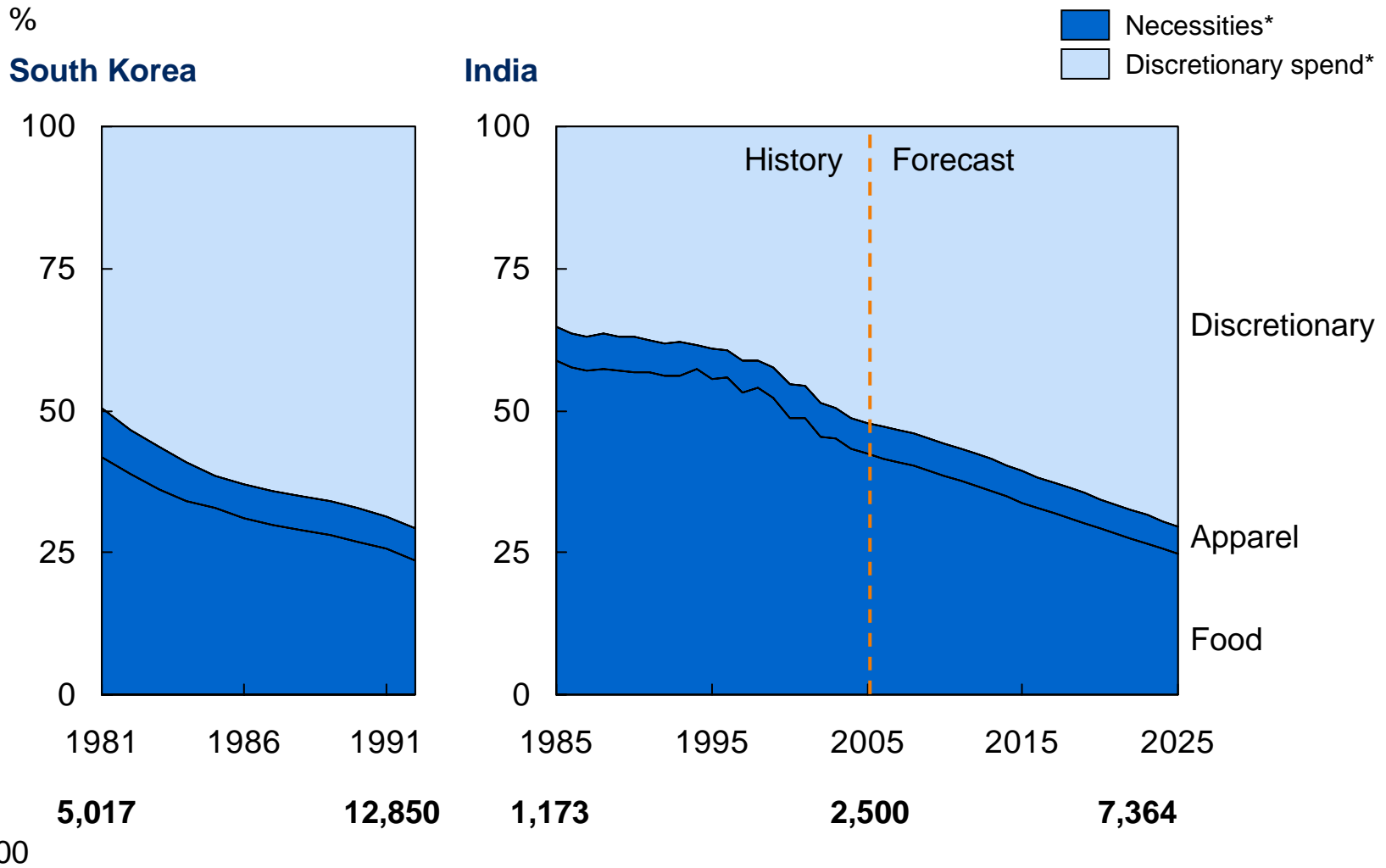


KEY FINDINGS

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FALL IN SHARE OF SPENDING ON NECESSITIES IN INDIA IS COMPARABLE TO SOUTH KOREA'S DURING ITS HIGH-GROWTH PHASE

Share of average household spending



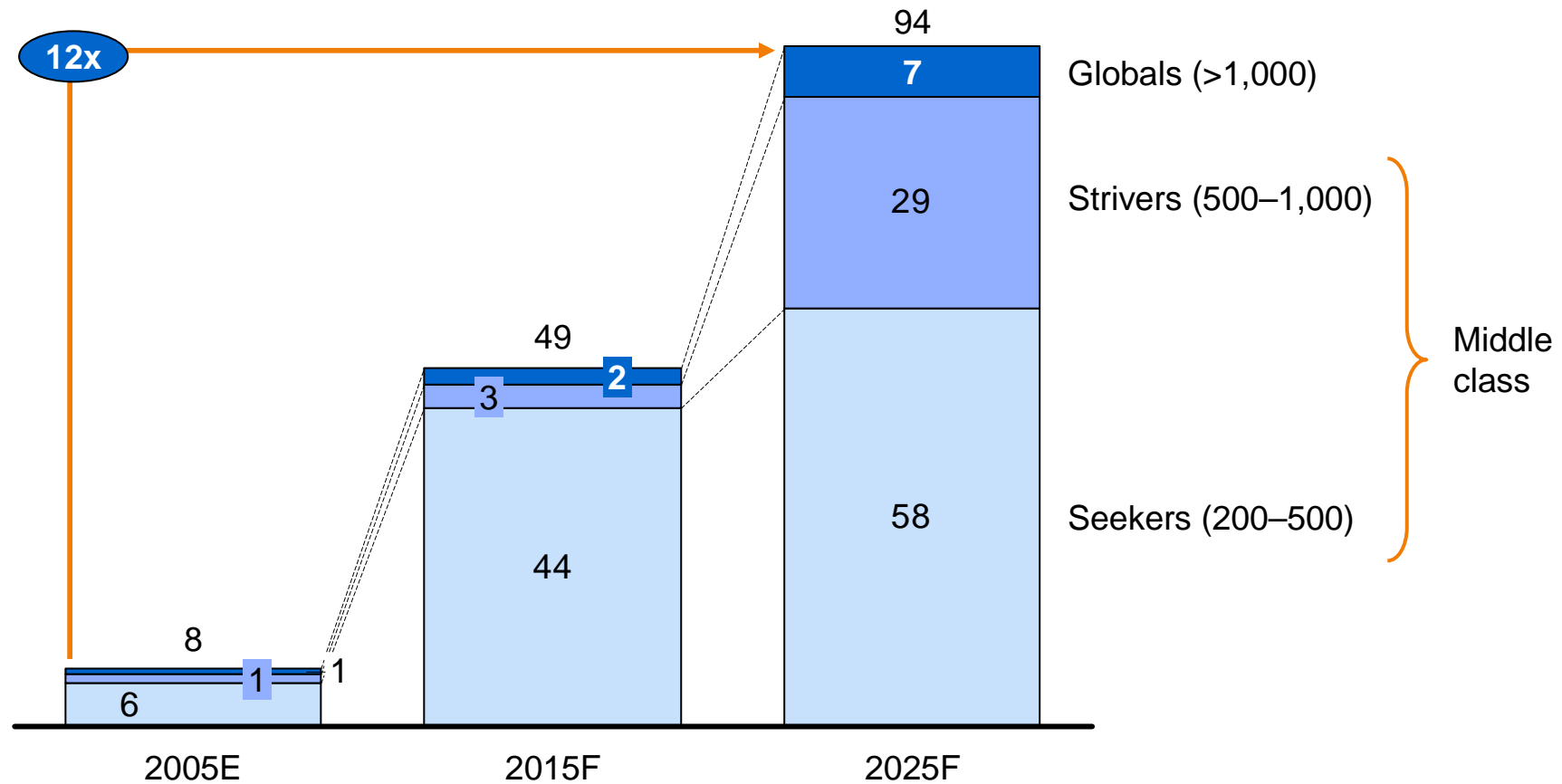
* Necessities include food and apparel; discretionary spending includes all other household spend categories.

Source: Euromonitor; India data from McKinsey Global Institute

NUMBER OF URBAN HOUSEHOLDS WITH DISCRETIONARY SPENDING POWER TO MULTIPLY TWELVE TIMES

Number of urban households with 'true' discretionary spending power* million








Household income brackets thousand, Indian rupees, 2000



* Consumers with sufficient budget to have significant levels of choice-driven spending (beyond categories such as food, housing, health care, education, fuel and transport services)

INDIAN SPENDING PATTERNS WILL BE UNIQUE

Share of total consumption, %

Consumption category	U.S. 	Germany 	Brazil 	South Korea 	China 	India (2005) 	India (2025) 
In line with benchmarks							
• Food beverages and tobacco	15	21	19	23	35	42	25
• Apparel	4	5	6	4	11	6	5
• Personal products and services	14	10	8	13	4	8	11
Less than benchmarks							
• Housing and utilities	19	27	22	18	9	12	10
• Household products	5	7	9	4	6	3	3
• Education and recreation	12	8	13	16	15	5	9
More than benchmarks							
• Transportation	11	17	13	12	6	17	20
• Communication	1	1	4	2	7	2	6
• Health care	19	4	6	8	7	7	13

Note: Figures are rounded to the nearest integer and may not add up to 100%

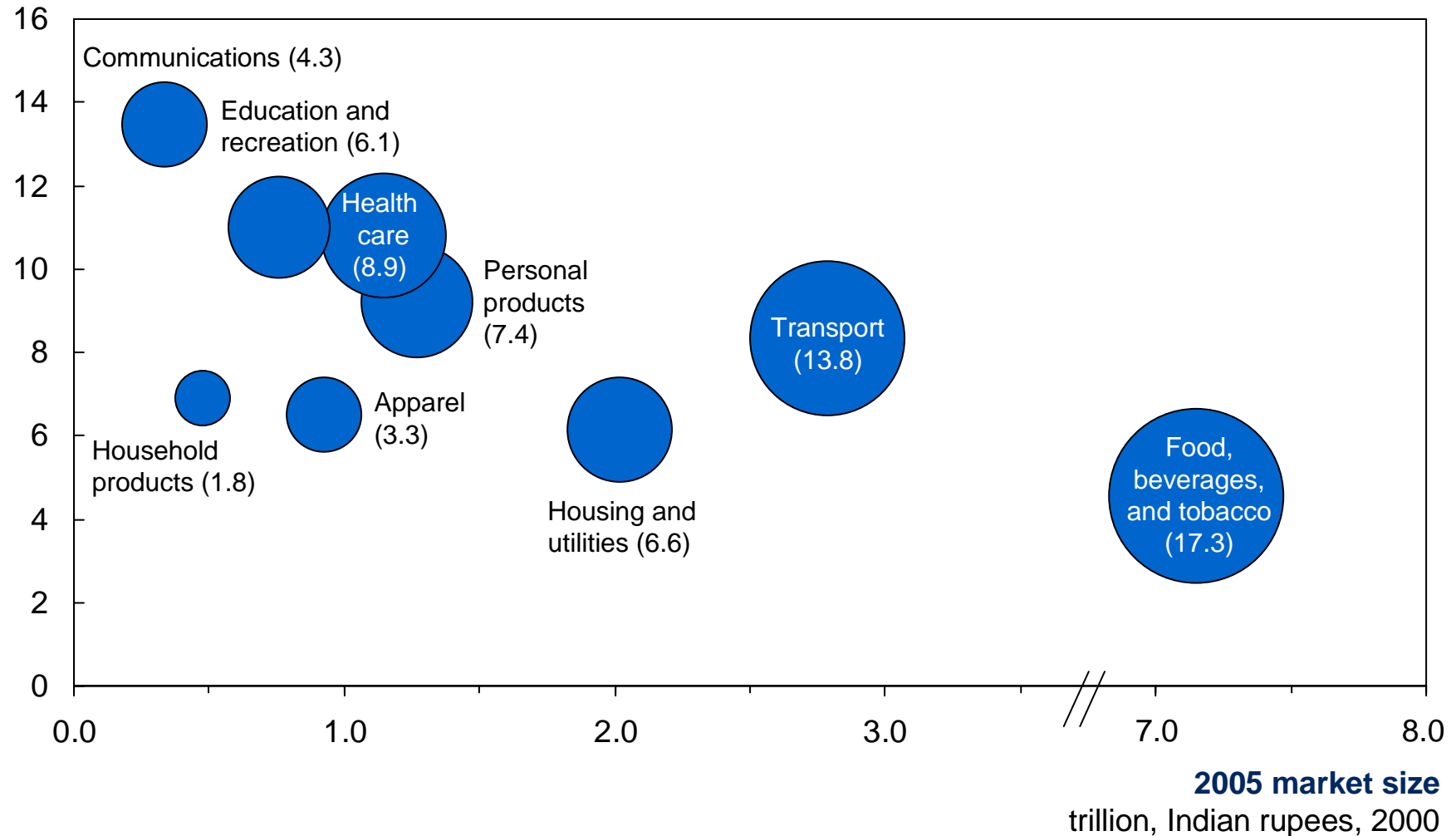
Source: Euromonitor, MGI China Consumer Demand Model v2.0, McKinsey Global Institute

FOOD WILL REMAIN THE LARGEST CONSUMPTION CATEGORY WHILE COMMUNICATIONS WILL GROW THE FASTEST

● Market size in 2025 trillion, Indian rupees, 2000

2005–2025 compound annual growth rate of aggregate consumption

%



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- **Income and consumption growth will create opportunities and challenges for business and government**

OPPORTUNITIES AND CHALLENGES FOR BUSINESSES

Opportunities

- Along with China the fastest growing of world's large consumer markets over next two decades
- Major discontinuity, winners have yet to be determined – \$1.1 trillion of new market growth not yet owned by anyone
- Most accessible market – upper income urbanities – will grow twelve times
- Almost half of middle class will be 'new consumers' at any point in time – loyalties up for grabs

Challenges

- Indian companies
 - Retaining existing customers and market shares
 - Adapting rapid pace of change
 - Innovating to capture new growth opportunities
 - Educating new consumers
- Multinationals
 - Meeting middle class aspirations at Indian price
 - Adapting products and services to meet Indian needs and task points
 - Building brands
 - Overcoming infrastructure, regulatory, and distribution hurdles

OPPORTUNITIES AND CHALLENGES FOR GOVERNMENT

Opportunities

- A chance to make further significant inroads in poverty reduction
- Domestic demand growth will spur further domestic production and employment – particularly in higher value-added industries
- An opportunity to attract FDI to serve Indian consumers
- The potential to improve the material well-being of hundreds of millions of people

Challenges

- Long-term growth must be maintained
- Infrastructure issues need to be addressed
- Regulatory constraints on business need further reform to enable businesses to meet growing demand and improve productivity
- Financial system needs reform to efficiently allocate investment, re-balance savings away from households and provide consumer credit
- Significant investments in human capital required (education, health care) in fiscally constrained environment

INCOME BRACKET CONVERSIONS

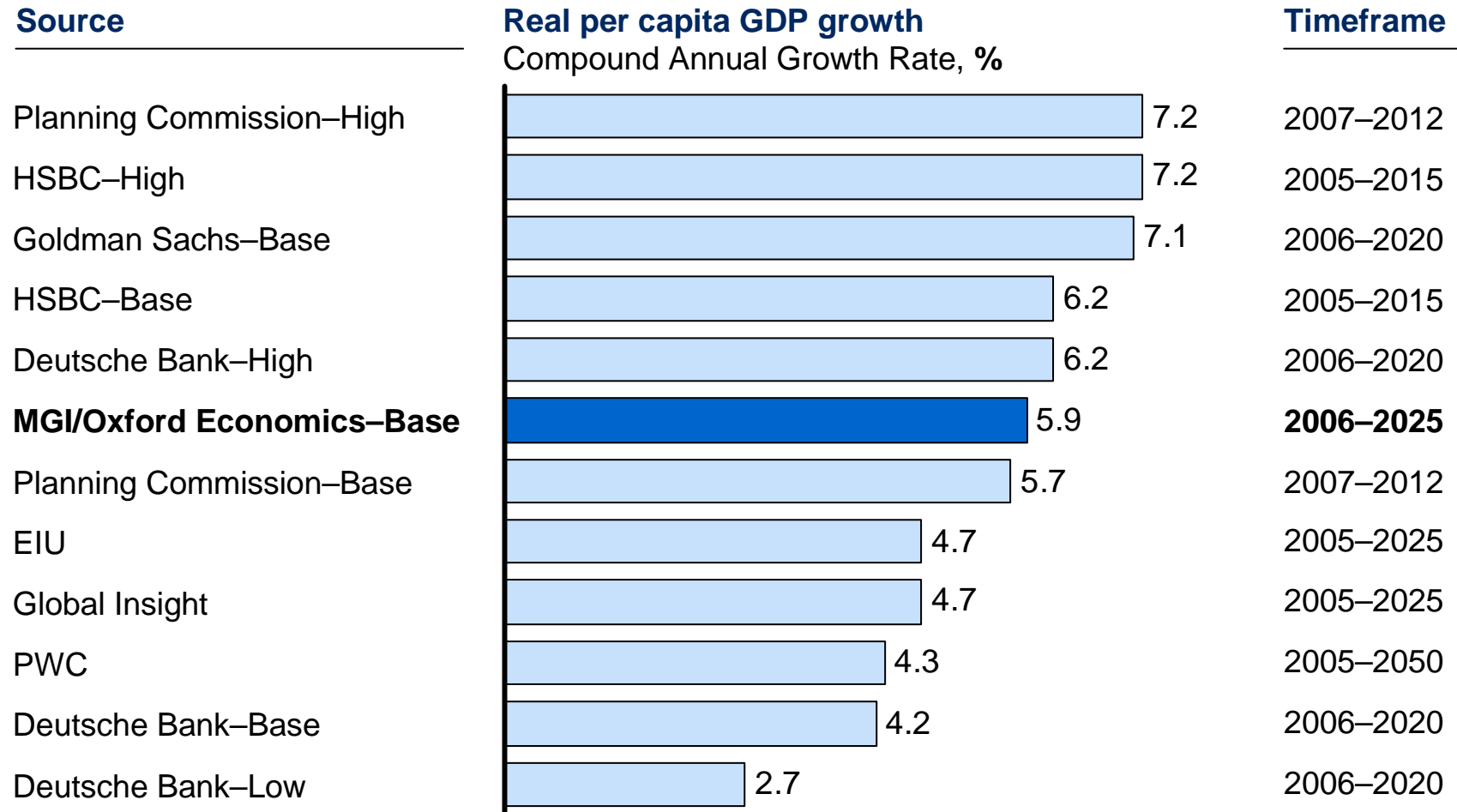
Household annual disposable income, real 2000

Bracket	Indian rupees	U.S. dollars non-adjusted	U.S. dollars PPP adjusted	
Globals	1,000,000 plus	21,882 plus	117,647 plus	
Strivers	500,000–1,000,000	10,941–21,882	58,823–117,647	} Middle class
Seekers	200,000–500,000	4,376–10,941	23,529–58,823	
Aspirers	90,000–200,000	1,969–4,376	10,588–23,529	
Deprived	Less than 90,000	Less than 1,969	Less than 10,588	

BACK-UP

- **Macroeconomic base case**
- Urbanization, rural growth and education
- Additional results

MGI'S BASE-CASE GDP FORECAST IS MIDDLE OF THE RANGE

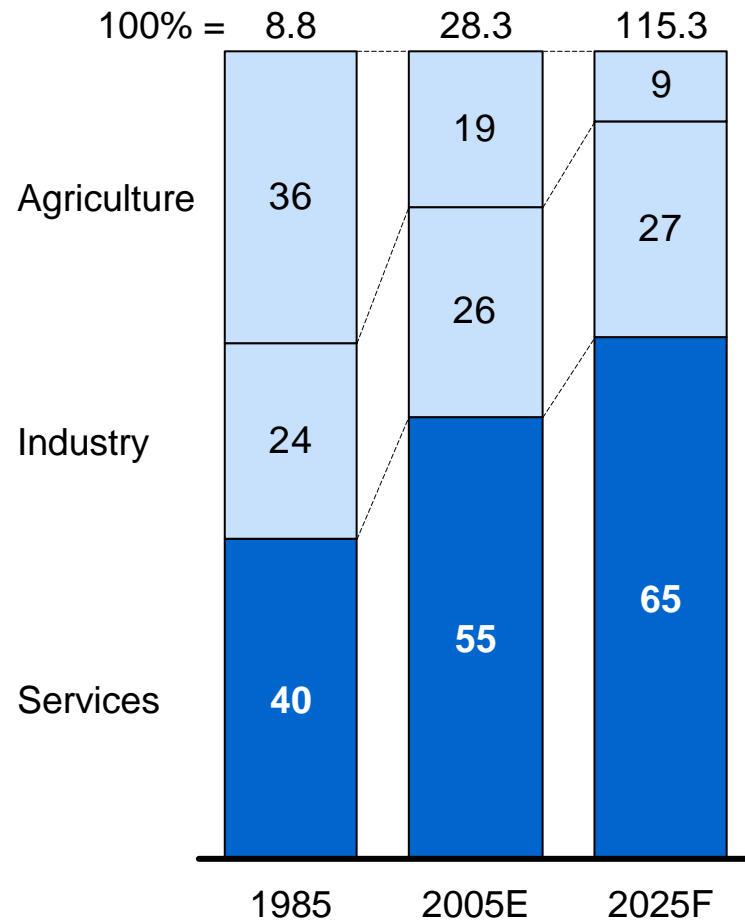


Source: Oxford Economics; *India: Pitfalls and Possibilities*, HSBC, July 2006; *India's rising growth potential*, Goldman Sachs, Jan 2007; *India Rising: A Medium-Term Perspective*, DB Research, May 2005; *Towards Faster and More Inclusive Growth: An Approach to the 11th Five Year Plan*, Planning Commission, Government of India, June 2006; *The World in 2050: How Big will the Major Emerging Market Economies Get and How Can the OECD Compete?*, PWC, 2006

SERVICES WILL CONTINUE TO BE THE MAIN DRIVER OF GDP GROWTH OVER THE NEXT TWO DECADES

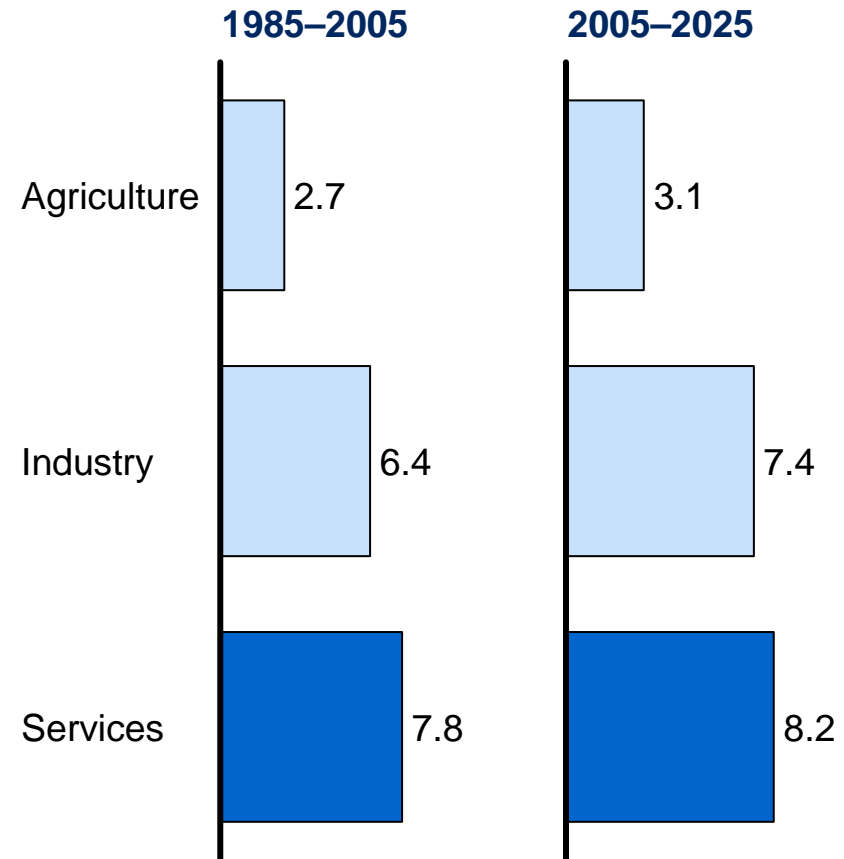
Share of GDP

%, trillion, Indian rupees, 2000



Growth by sector

Compound annual growth rate, %



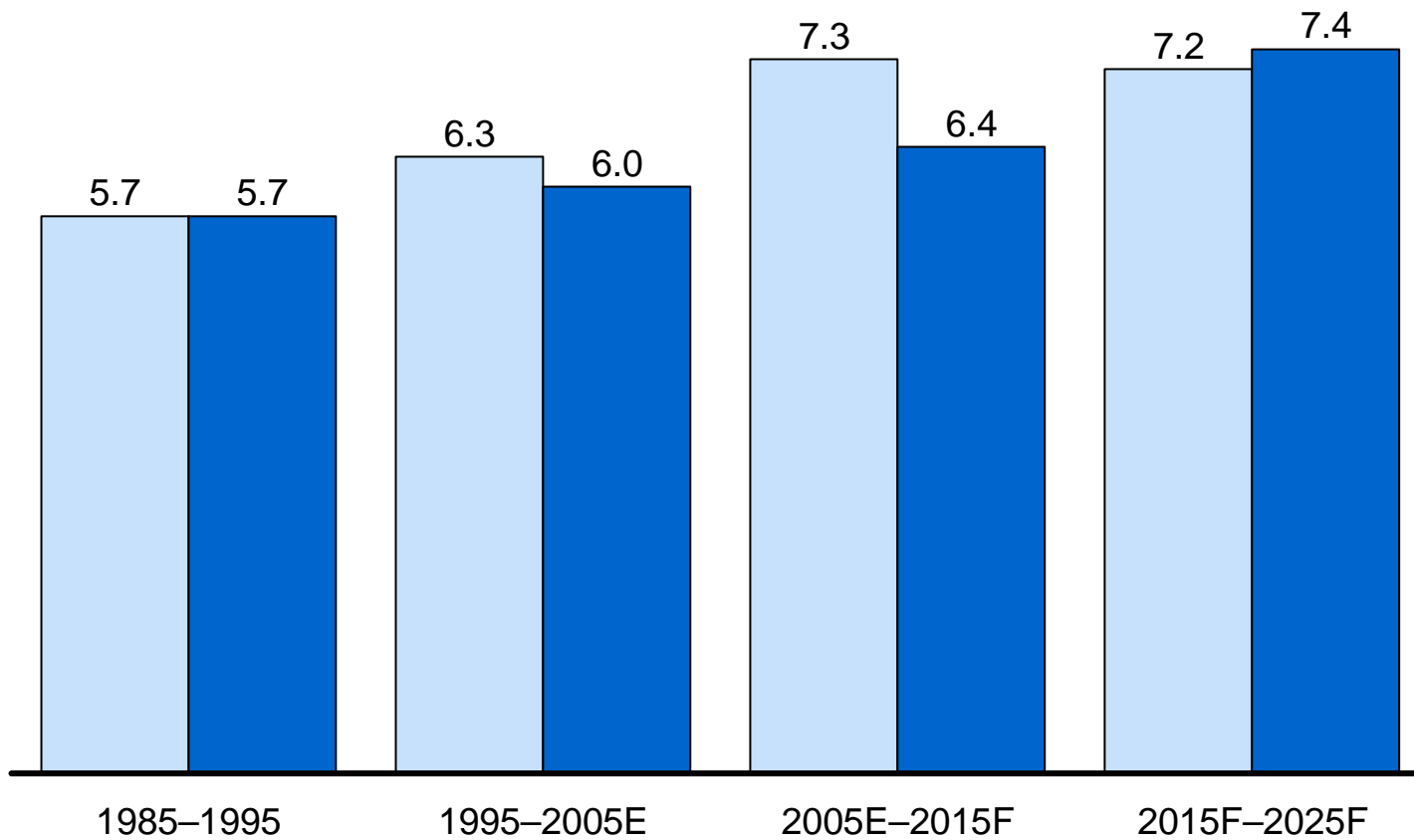
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Source: McKinsey Global Institute

INCOME GROWTH WILL ACCELERATE WITH ECONOMIC GROWTH

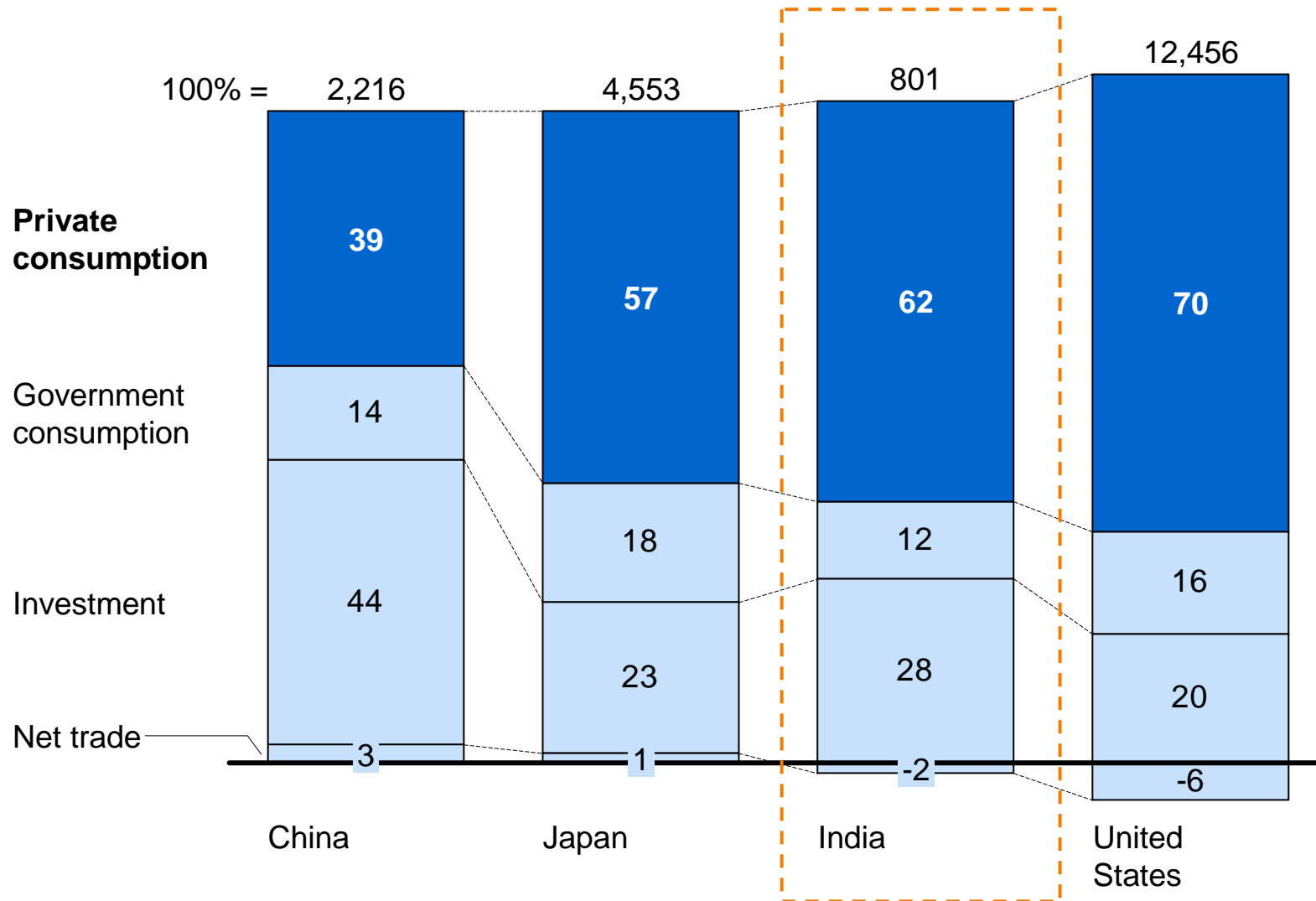
■ GDP
■ Household disposable income

GDP versus household disposable income growth
compound annual growth rate, %, Indian rupees, 2000



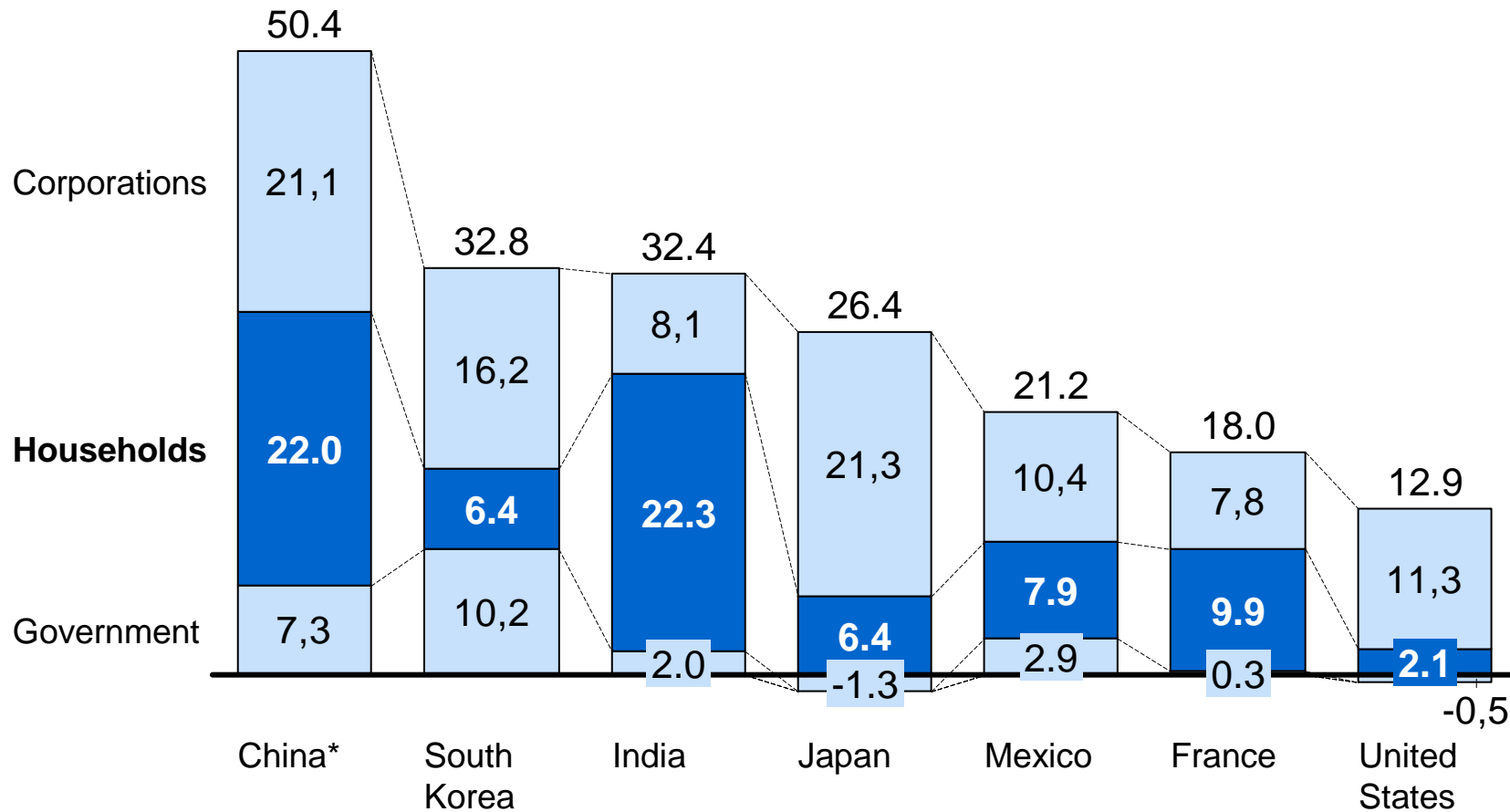
INDIA'S CONSUMPTION SHARE OF GDP IS CLOSER TO JAPAN AND THE UNITED STATES THAN IT IS TO CHINA

%, billion, nominal \$, 2005



INDIA HAS A RELATIVELY HIGH NATIONAL SAVINGS RATE COMPARED WITH OTHER COUNTRIES

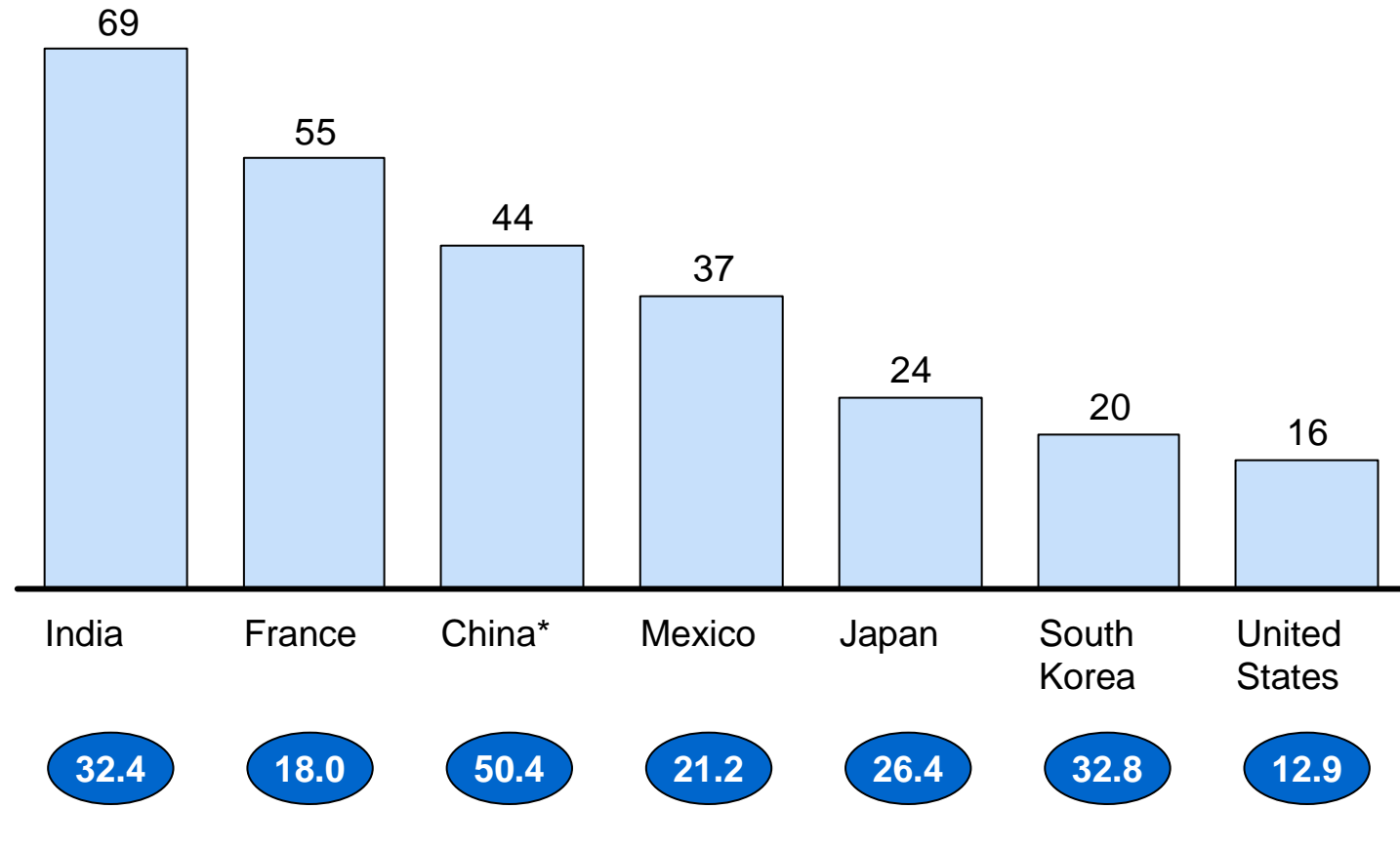
Gross national savings rates
% of nominal GDP, 2005



* MGI estimate based on 2005 GDP and estimates of flow-of-funds information.

INDIAN HOUSEHOLD SAVINGS ACCOUNT FOR A DISPROPORTIONATE SHARE OF NATIONAL SAVINGS

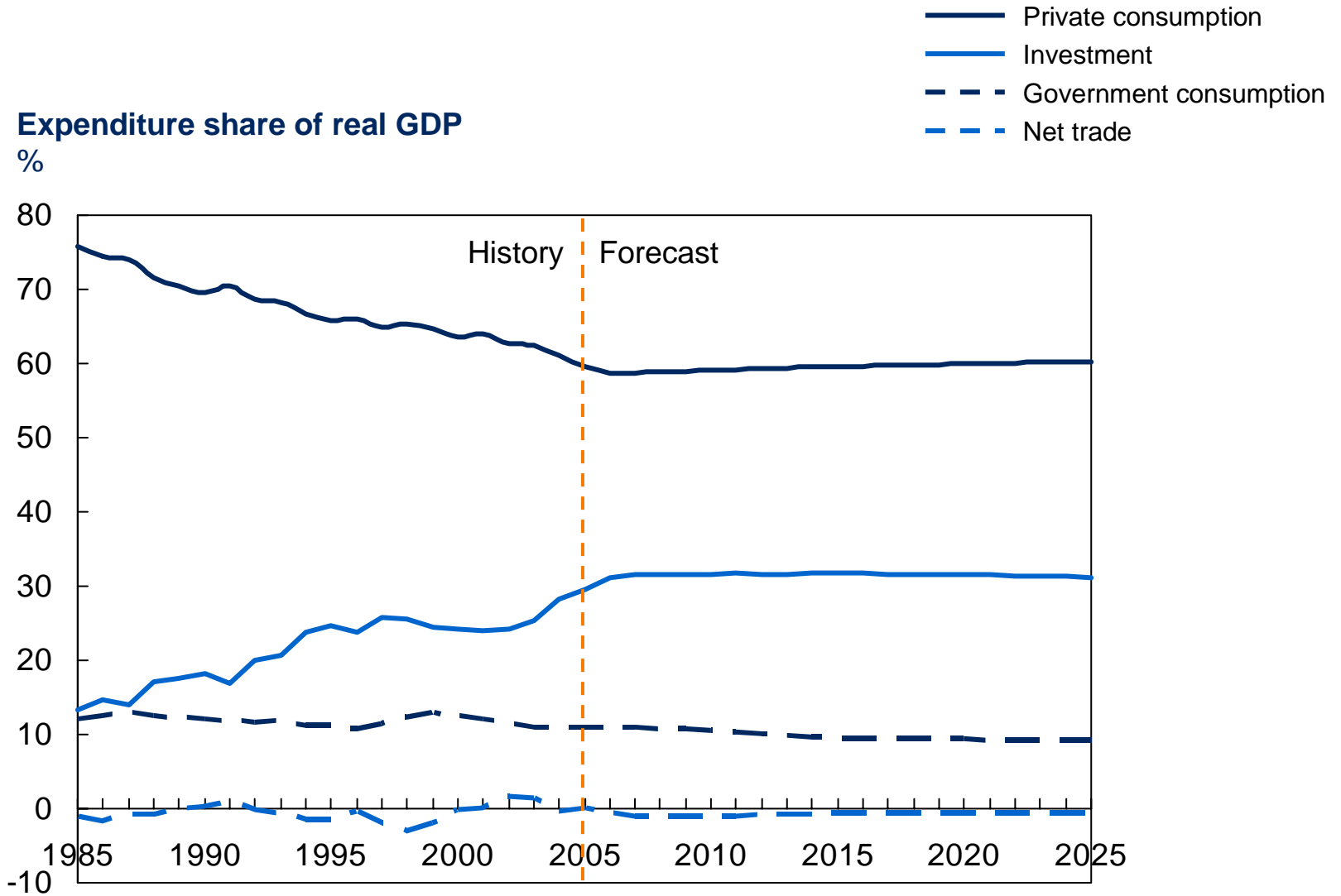
Household savings as a share of gross national savings rates, 2005
%



* MGI estimate based on 2005 GDP and estimates of flow-of-funds information.

Source: Country National Accounts; IMF; McKinsey Global Institute

INVESTMENT WILL GROW APPROXIMATELY IN LINE WITH GDP



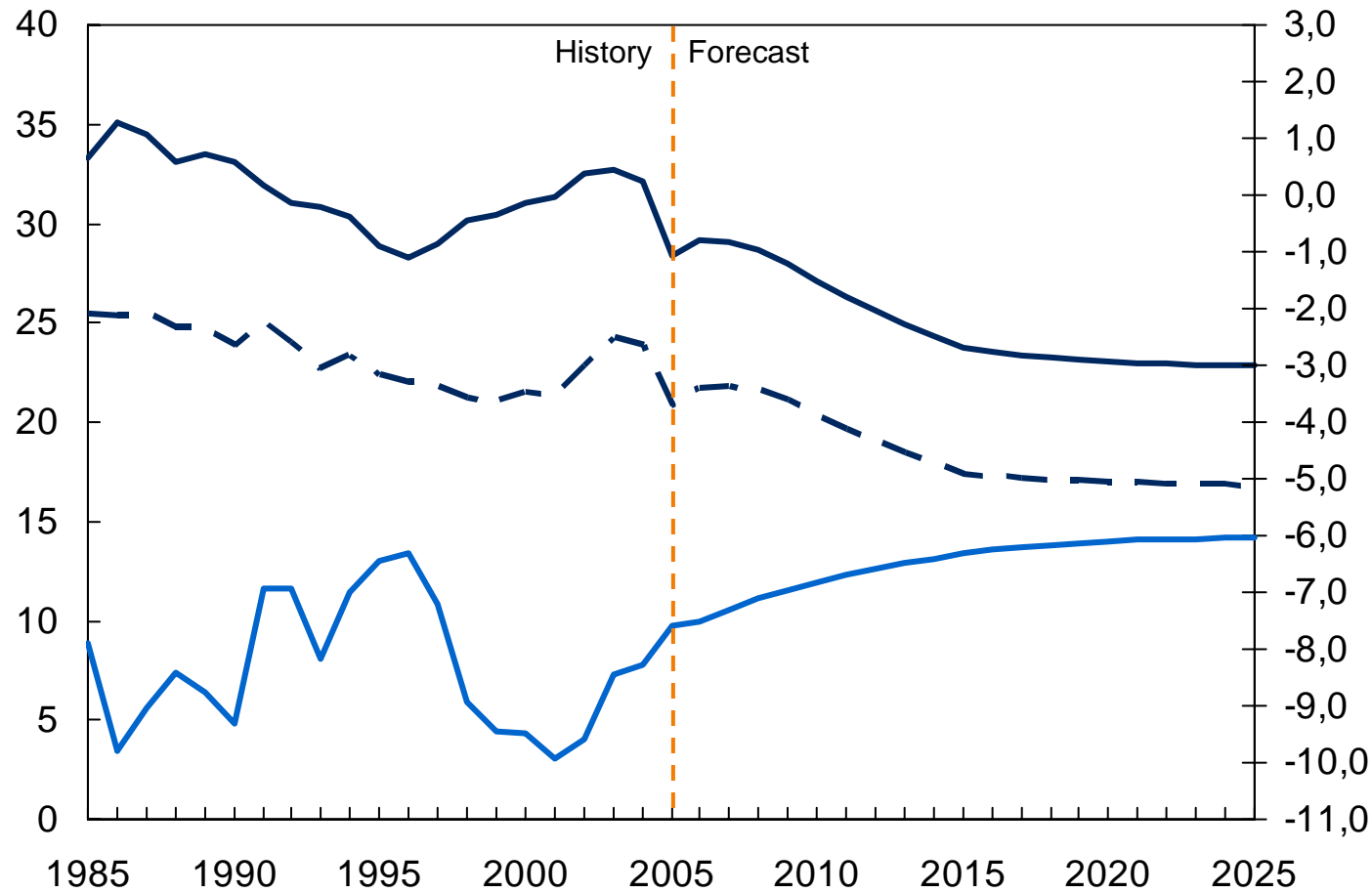
GOVERNMENT SPENDING AND DEFICIT WILL GRADUALLY DECLINE AS A PROPORTION OF GDP

% of GDP

- Expenditures (left scale)
- - - Revenues (left scale)
- Deficit (right scale)

Government expenditures and revenues*

Government budget deficit

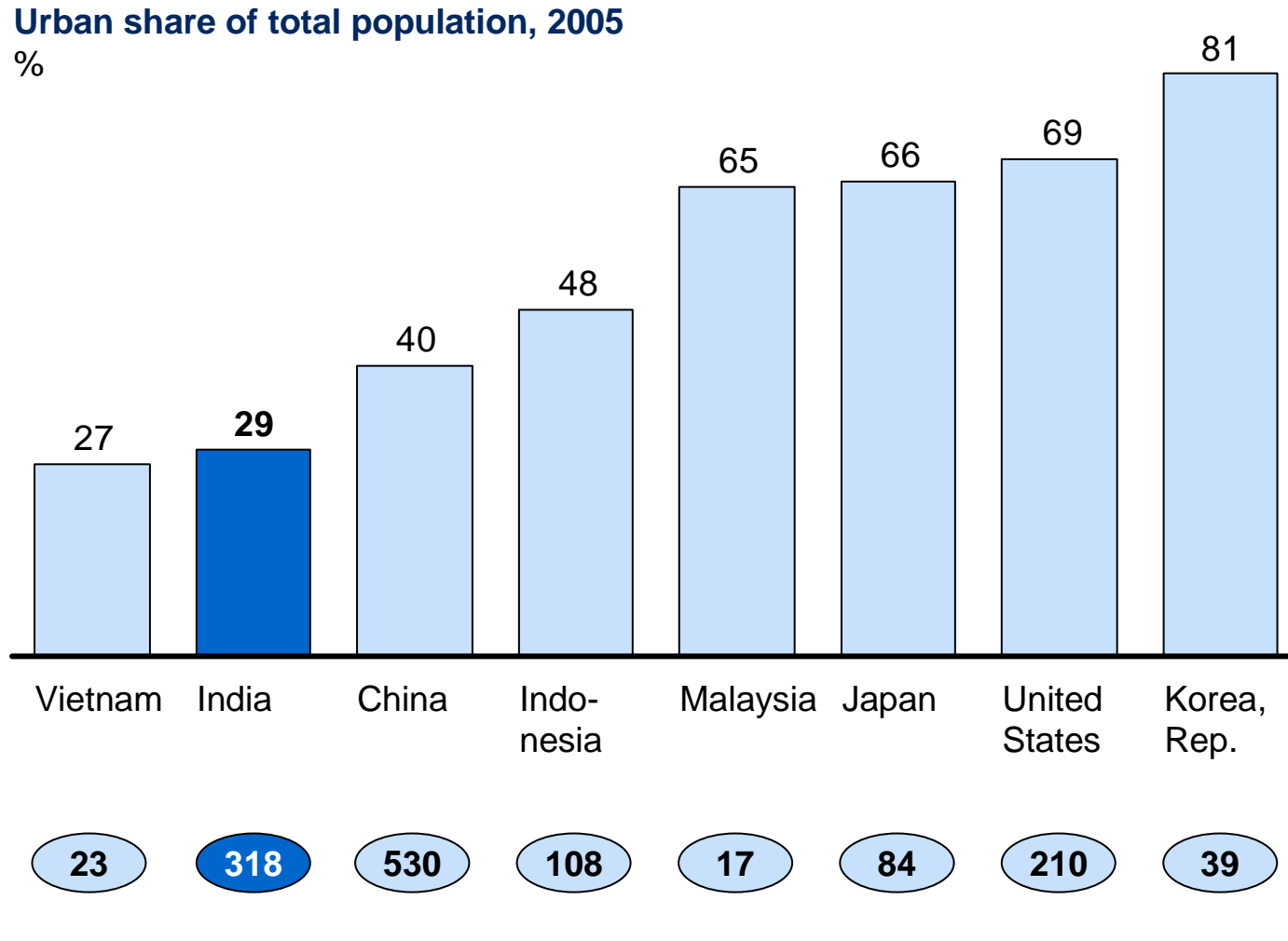


* Government expenditure figures are available through 2005.

BACK-UP

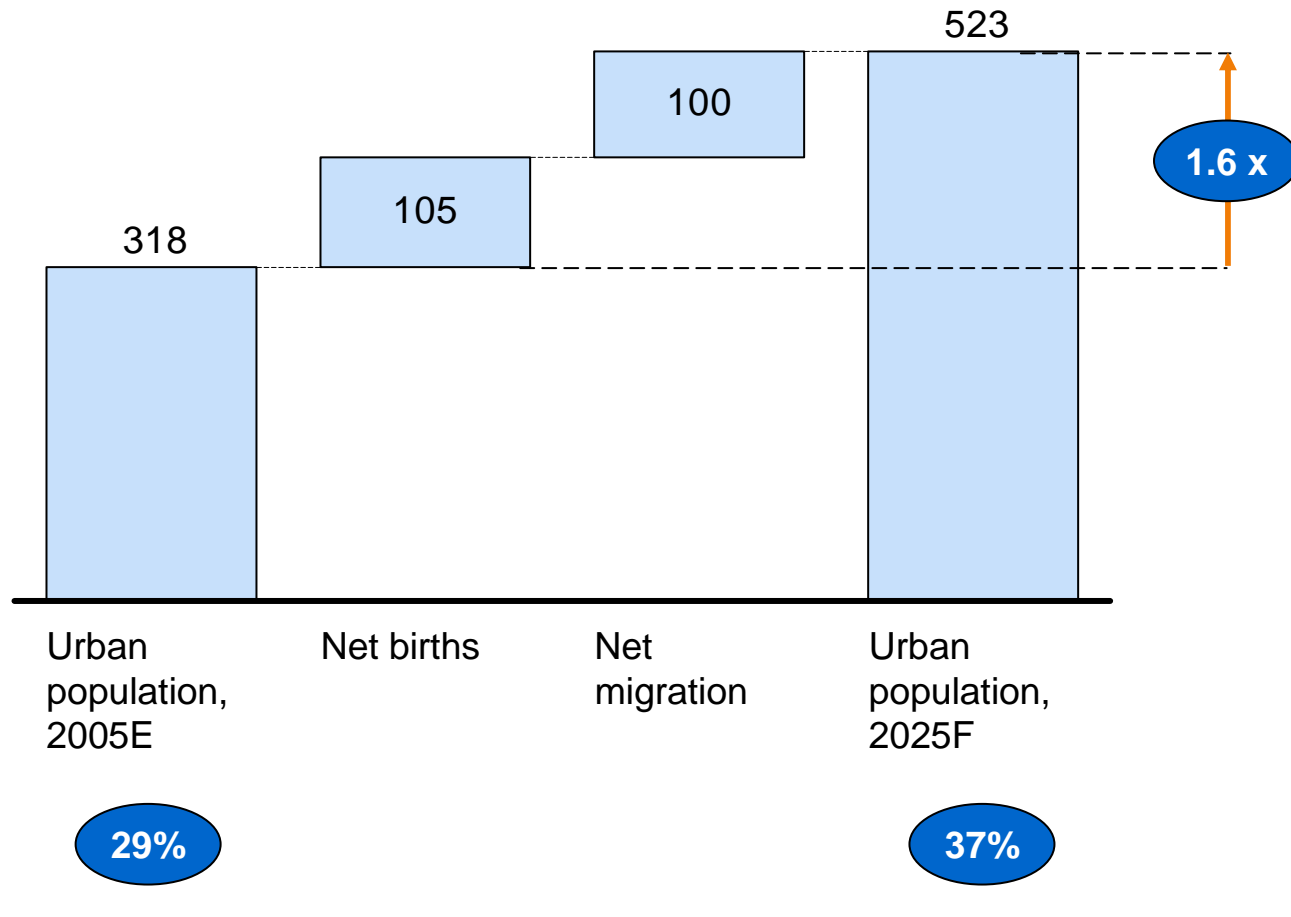
- Macroeconomic base case
- **Urbanization, rural growth and education**
- Additional results

INDIA REMAINS LESS URBAN THAN ITS COUNTERPARTS IN ASIA, BUT DEFINITIONS VARY



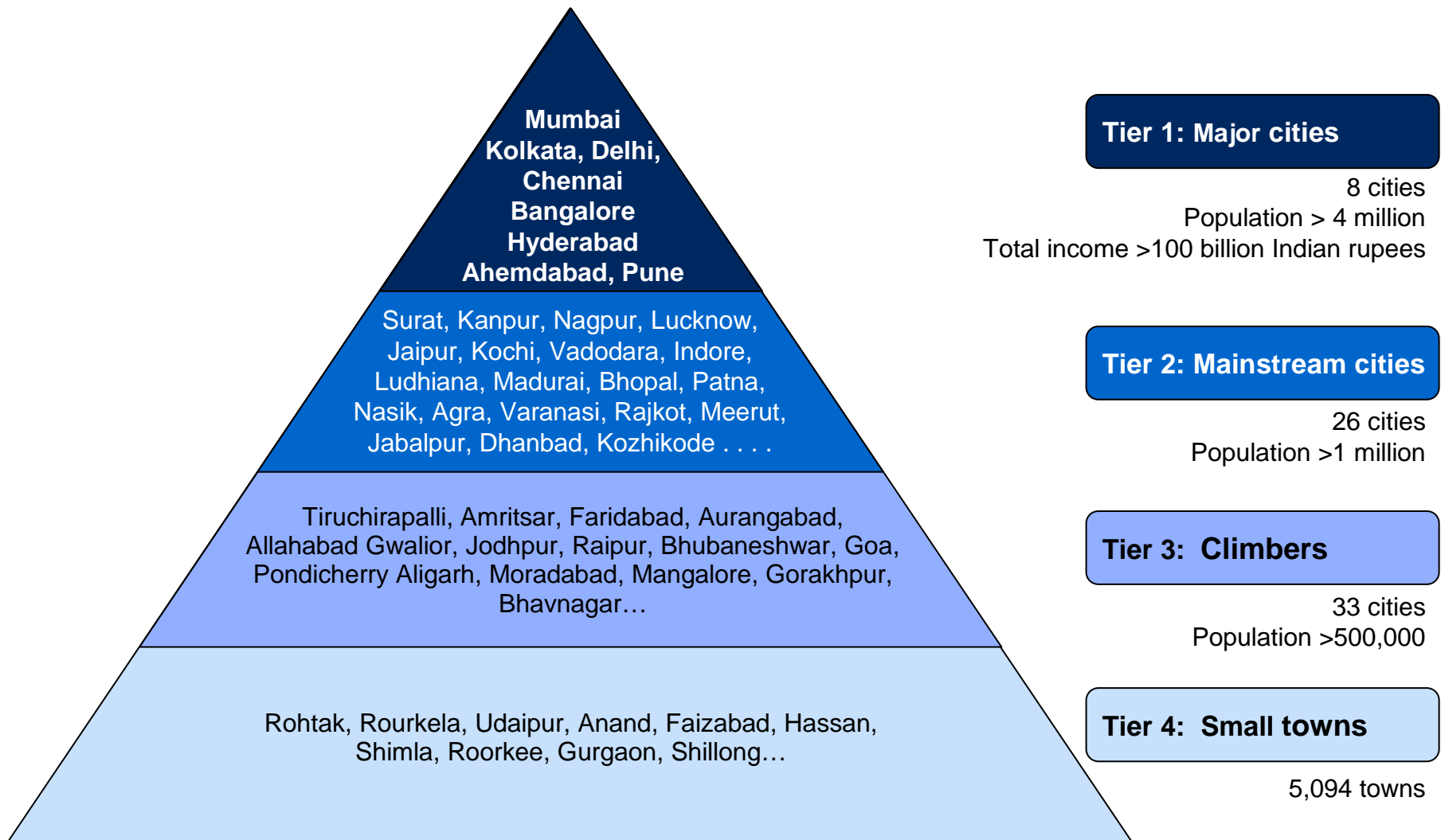
BIRTHS AND MIGRATION WILL DRIVE URBAN POPULATION GROWTH

Urban population, 2005–2025*
million



* Estimate of birth versus migration split assumes urban birth rate = 19 per 1,000 and death rate = 6 per 1,000

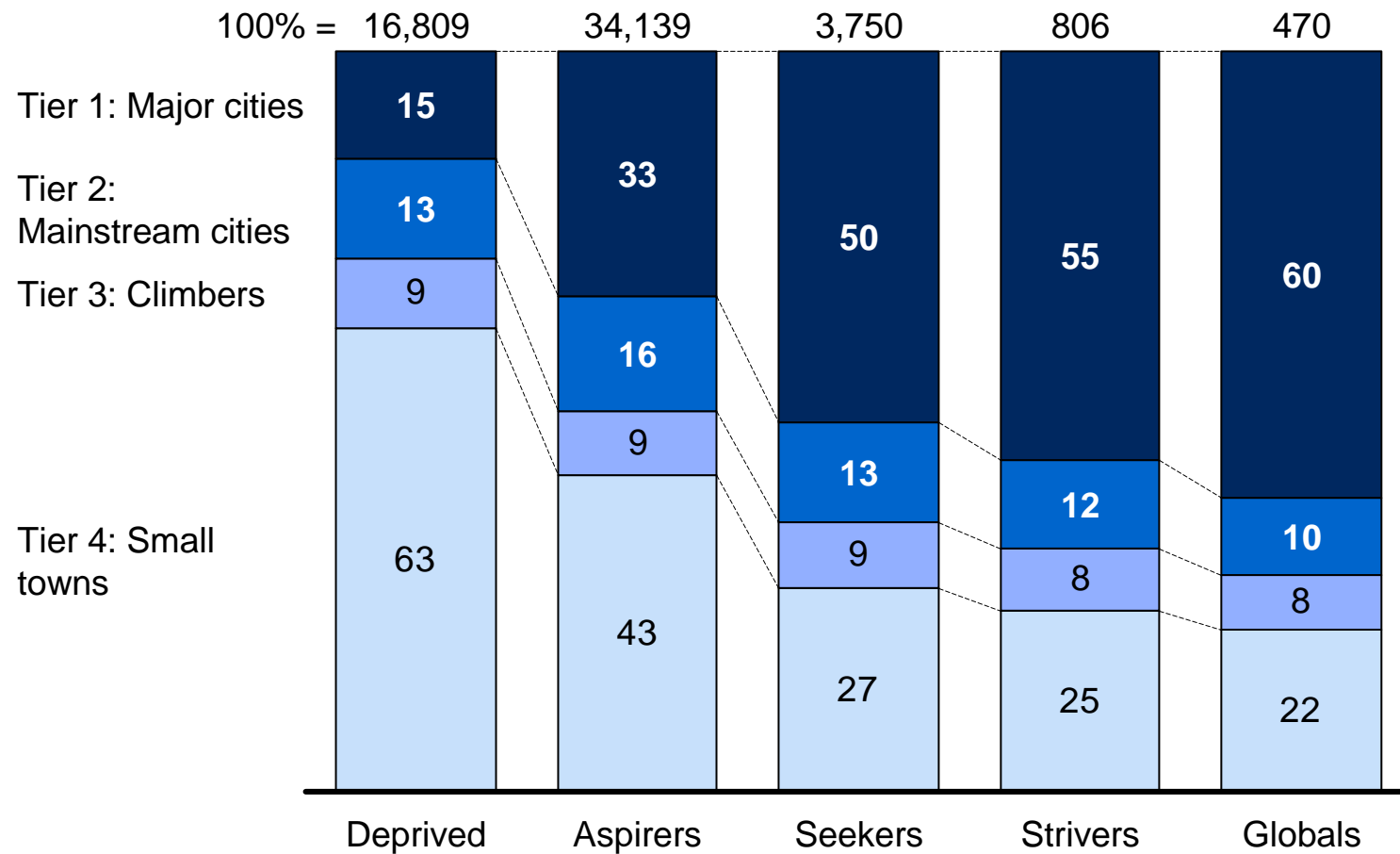
CLASSIFICATION OF CITIES AND TOWNS



* Population for each city estimated using the average urban household size (from MGI model) and the estimated number of households in each city from NCAER (in the year 2001).

HIGHER INCOME HOUSEHOLDS CONCENTRATED IN LARGE CITIES, POOR IN SMALL TOWNS

Proportion of households in each income class across city tiers, 2001
%, thousand, households

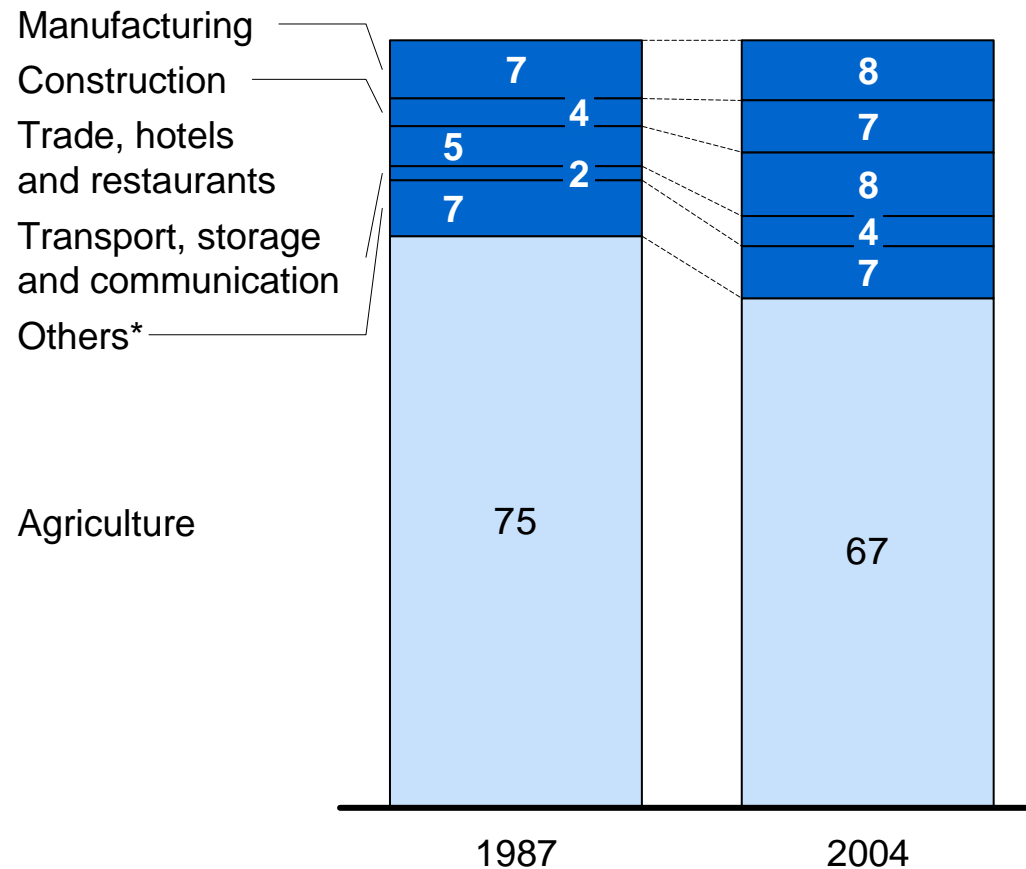


Note: Figures are rounded to the nearest integer and may not add up to 100%.

Source: *The Great Indian Middle Class*, NCAER; McKinsey Global Institute

RURAL EMPLOYMENT HAS BEEN GRADUALLY SHIFTING AWAY FROM AGRICULTURE

Distribution of rural male workers by economic activity
%




* Sectors with minimal shift in this period (6% in other services, 1% in mining, quarrying, electricity and water).

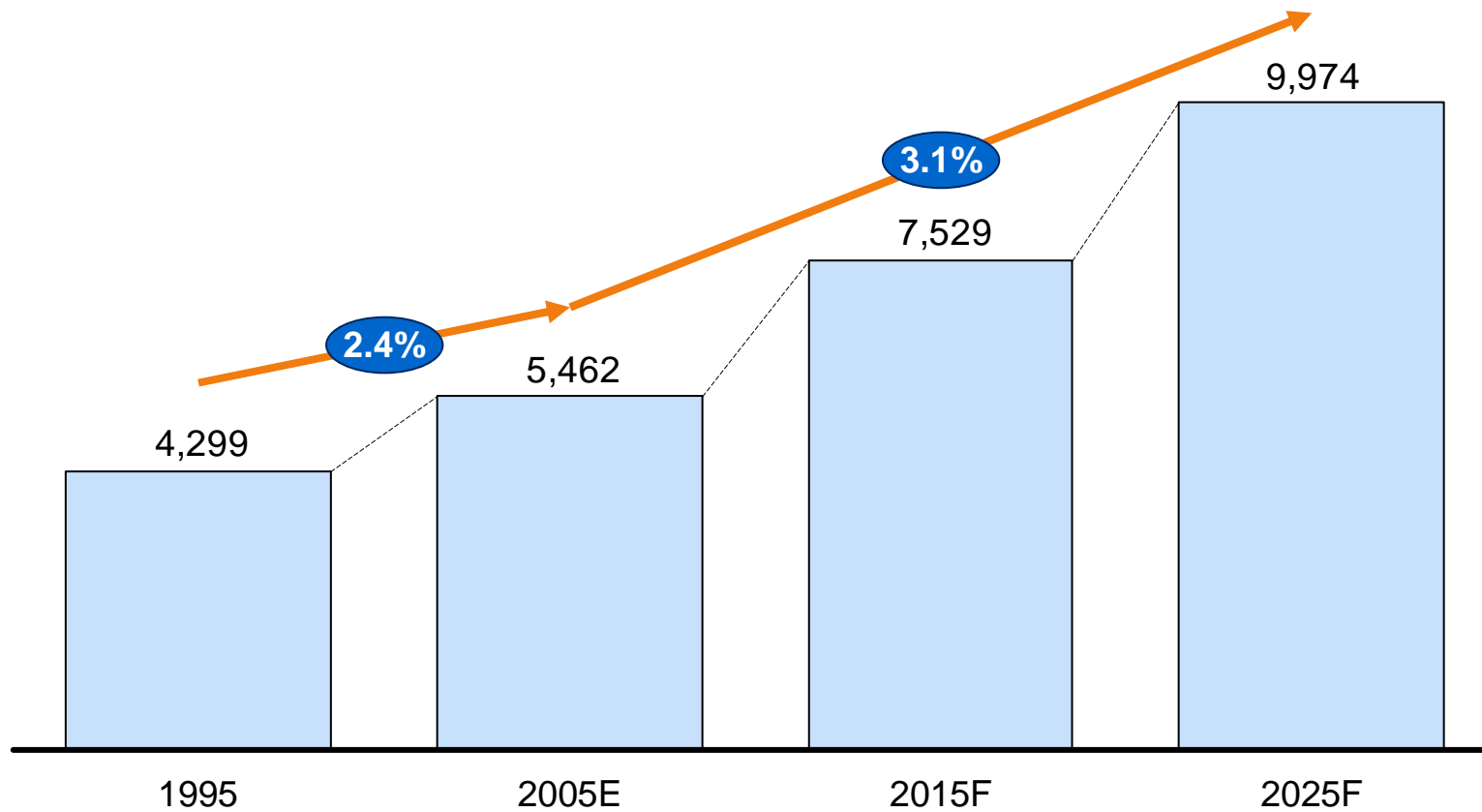
Note: Figures are rounded to the nearest integer and may not add up to 100%.

Source: *Employment and unemployment situation in India (2004–05)*, NSSO; McKinsey Global Institute

AGRICULTURAL GROWTH IS FORECAST TO ACCELERATE FROM ITS RECENT HISTORICAL RATE

 Compound annual growth rate

Agricultural value added in GDP
billion, Indian rupees, 2000

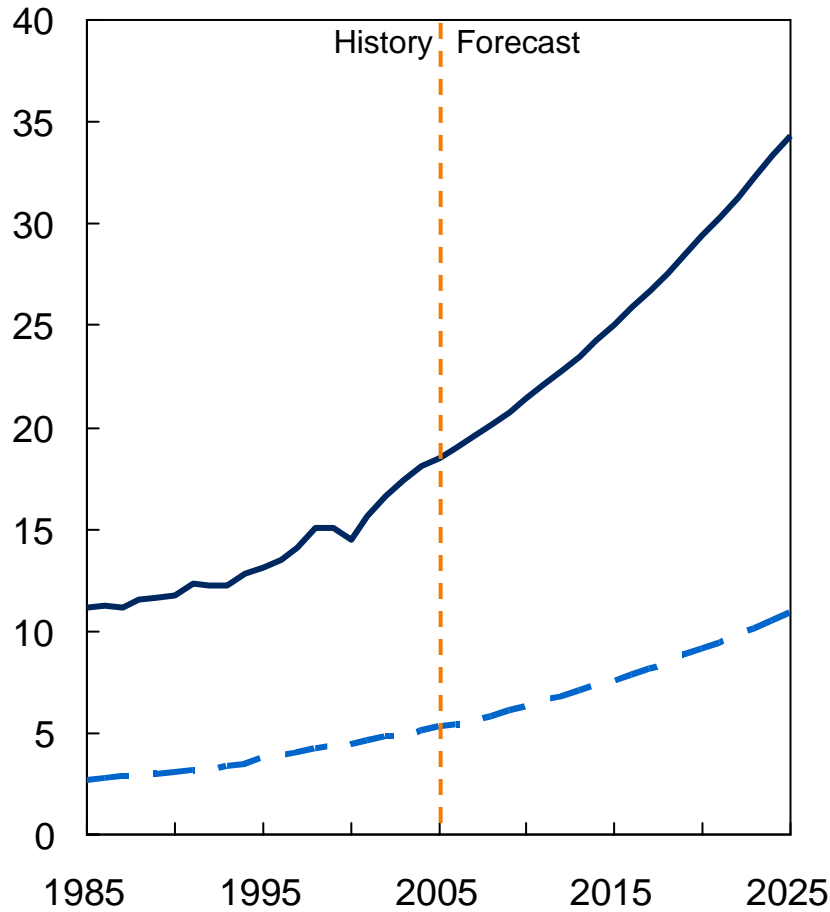


ACHIEVEMENT IN HIGHER AND SECONDARY EDUCATION WILL CONTINUE TO BECOME MORE WIDESPREAD

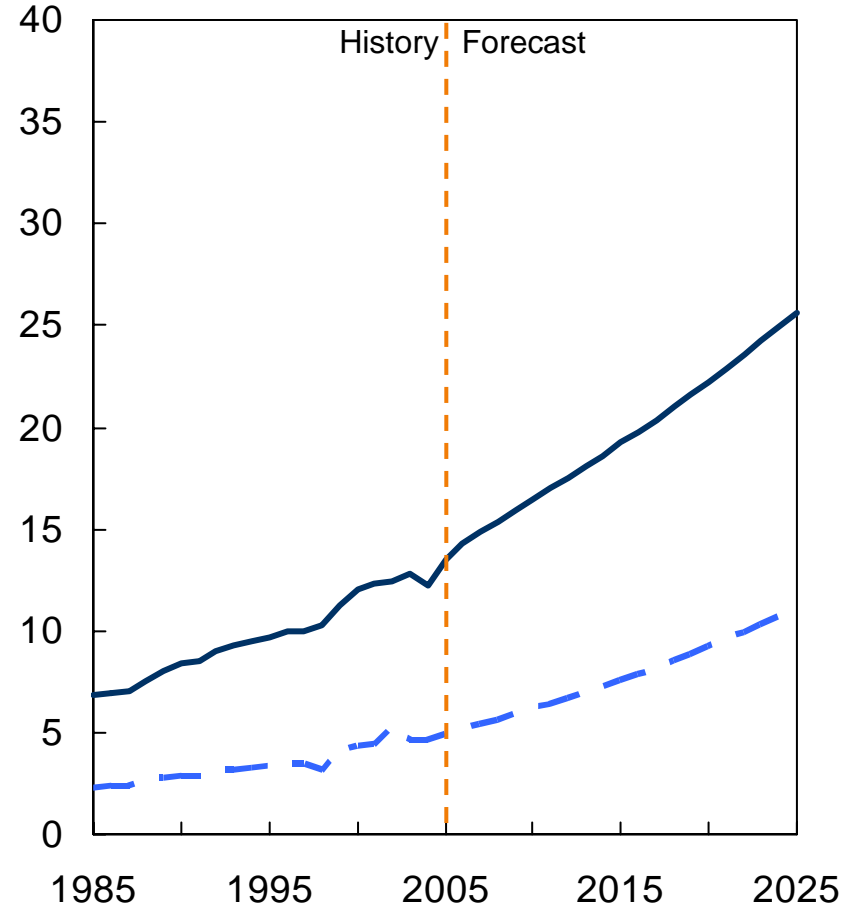
% of relevant population groups*

— Secondary
- - - Higher

Rate of secondary-school and higher-education enrollment



Rate of secondary-school and higher-education attainment

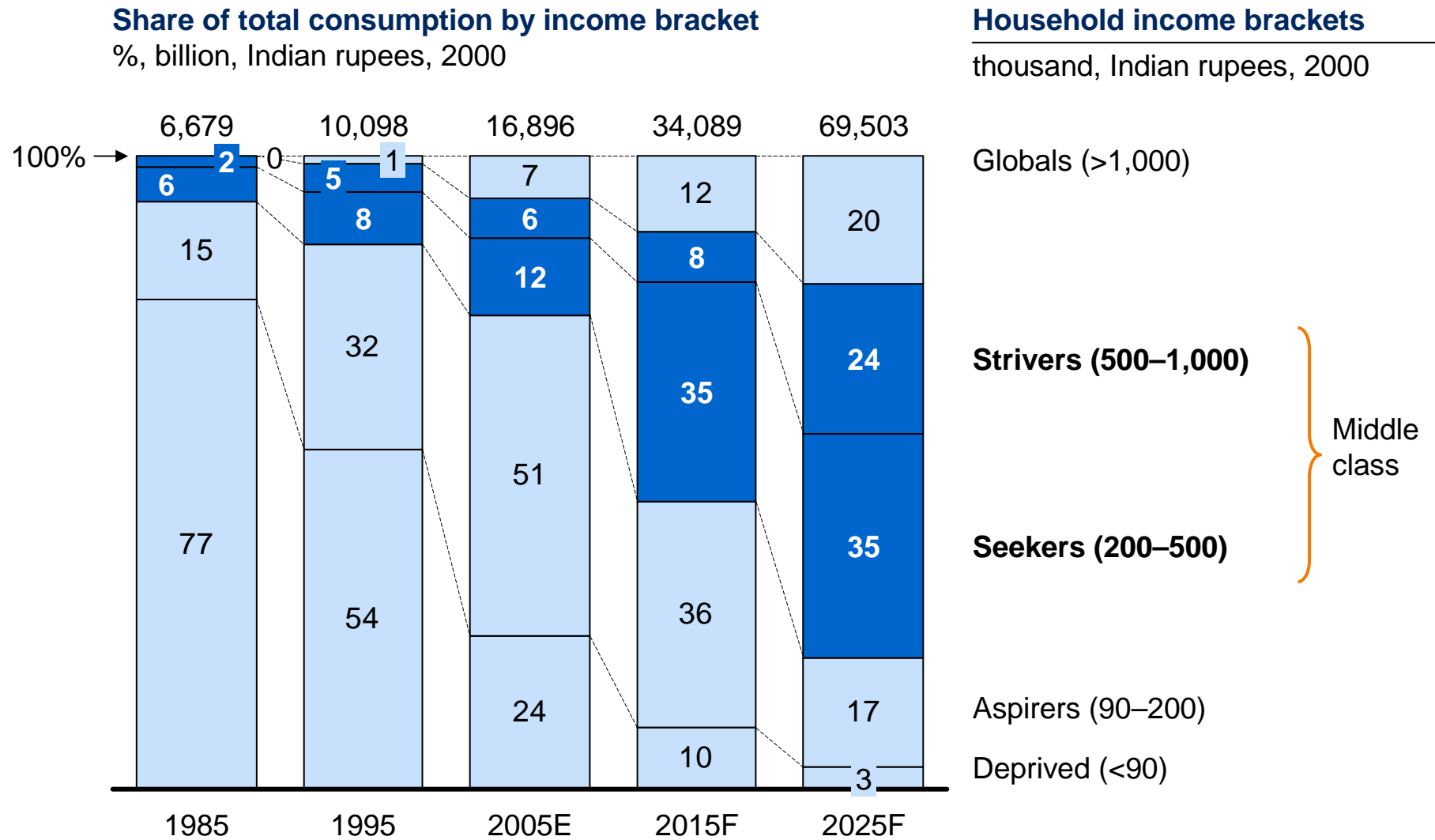


* Enrollment is measured as a percentage of 15 to 24 year old population; attainment is measured relative to 15 and above population.

BACK-UP

- Macroeconomic base case
- Urbanization, rural growth and education
- **Additional results**

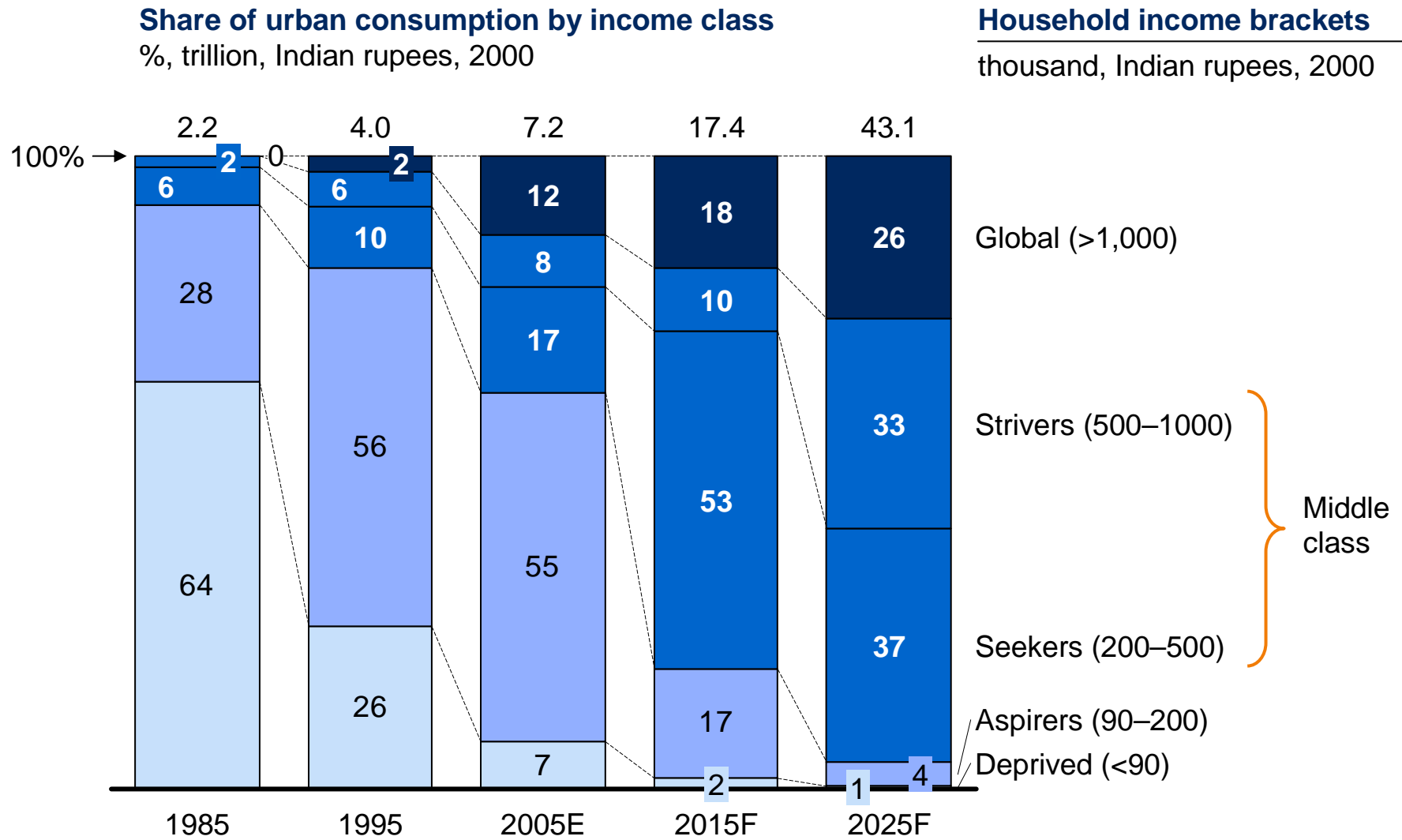
INDIAN CONSUMPTION WILL BE DOMINATED BY THE MIDDLE CLASS



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Source: McKinsey Global Institute

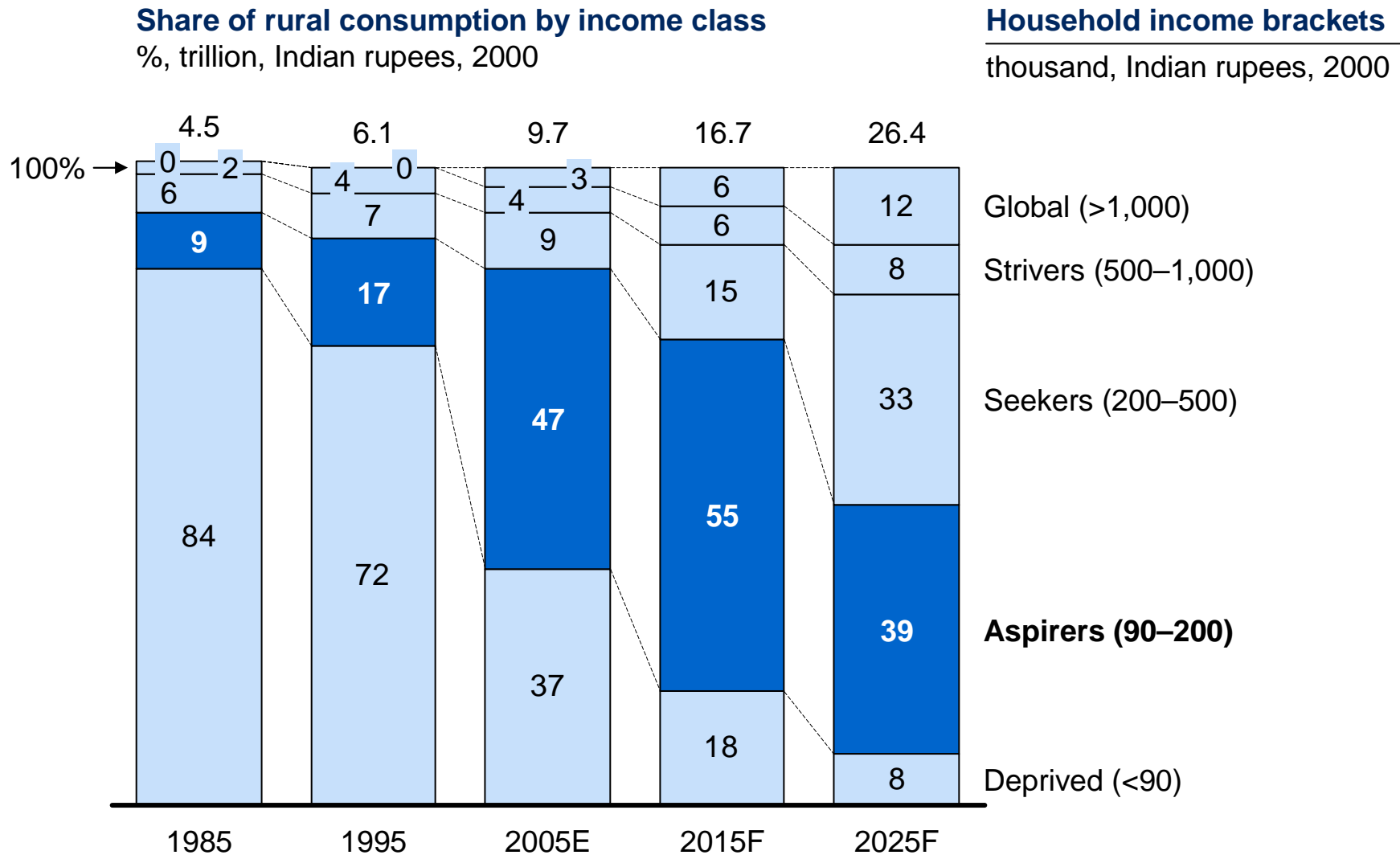
HALF OF URBAN CONSUMPTION WILL COME FROM UPPER INCOME STRIVERS AND GLOBALS



Note: Figures are rounded to the nearest integer and may not add up to 100%.

Source: McKinsey Global Institute

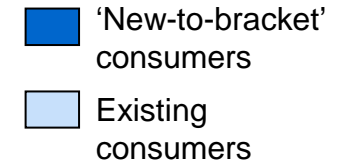
ASPIRERS WILL DRIVE RURAL SPENDING OVER THE NEXT TWO DECADES



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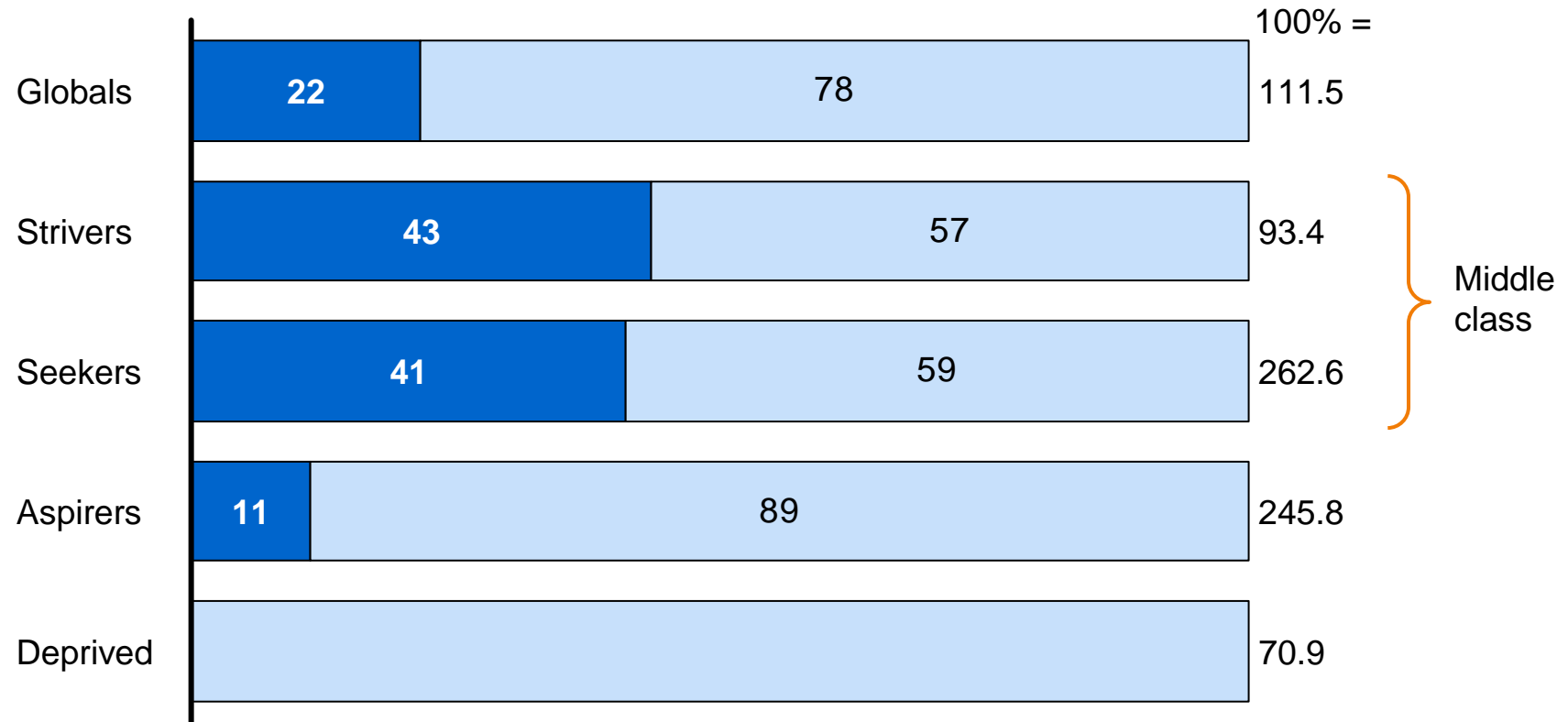
Source: McKinsey Global Institute

CONSUMPTION BY 'NEW-TO-BRACKET' CONSUMERS WILL BE SIGNIFICANT, ESPECIALLY IN THE MIDDLE CLASS



'New-to-bracket' share of cumulative consumption 2005–2025*

%, trillion, Indian rupees, 2000

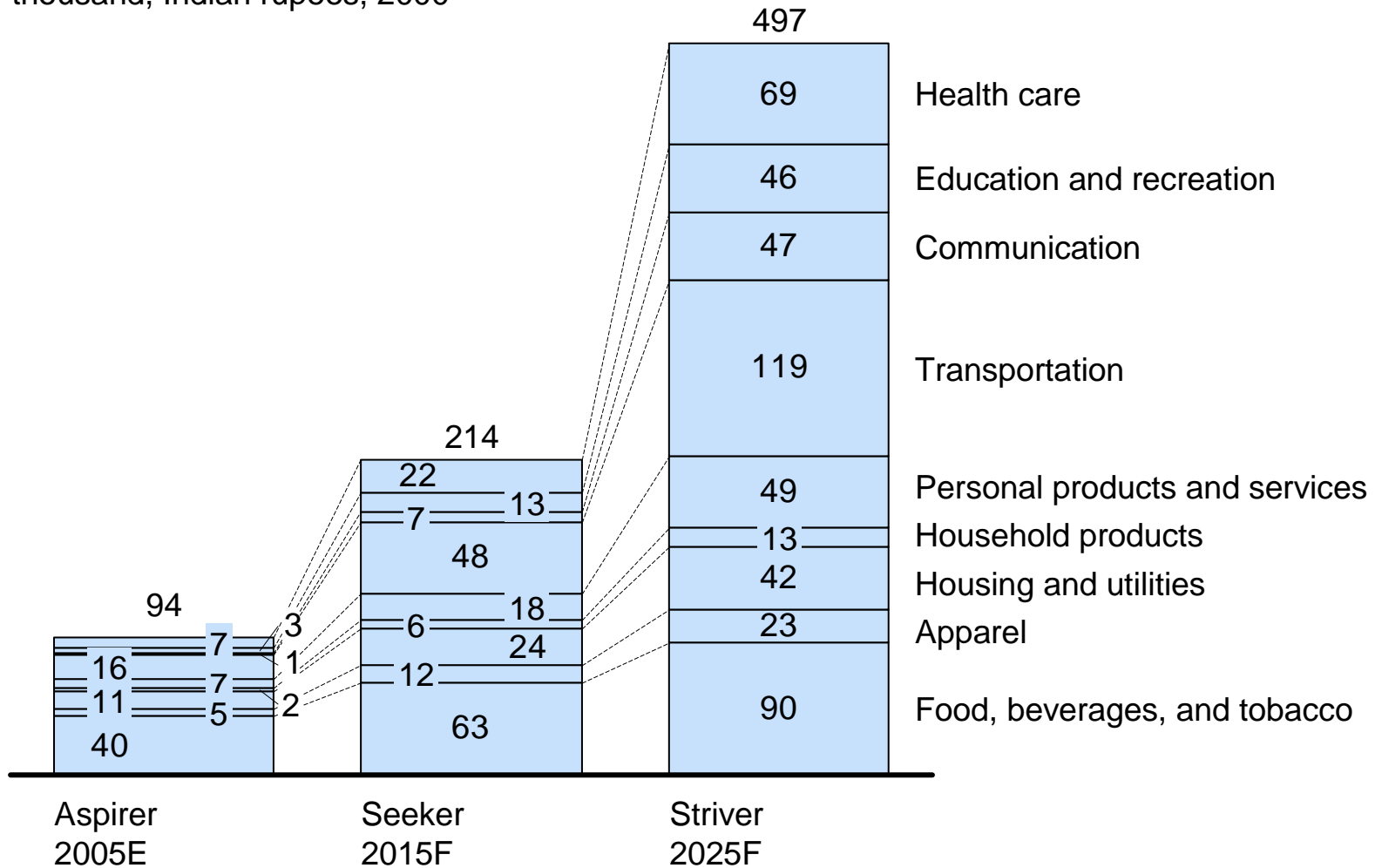


* Calculated by determining the number of households that have shifted income class, assume they consume at new bracket levels in the first year, and then consider them 'new' to that bracket for three years.

FROM ASPIRER TO STRIVER – THE EVOLUTION OF SPENDING FOR A TYPICAL HOUSEHOLD

Average household consumption

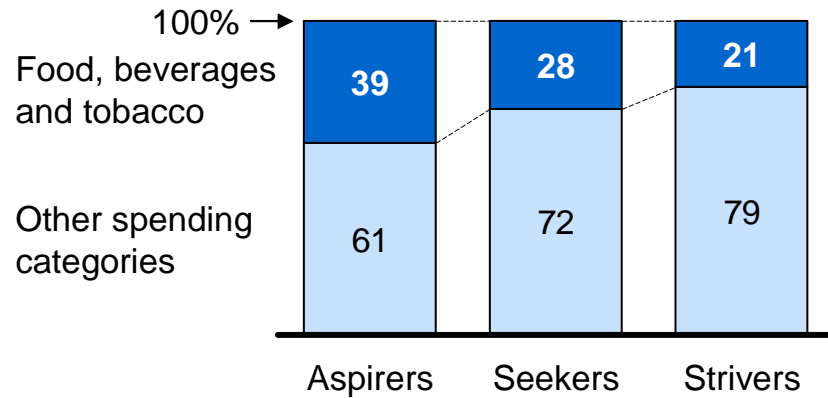
thousand, Indian rupees, 2000



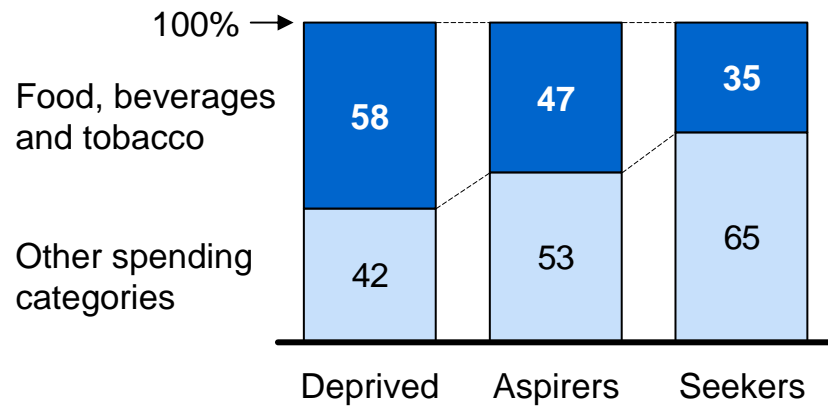
SHARE-OF-WALLET ON FOOD IS ALREADY LOW IN MIDDLE- AND UPPER-INCOME BRACKETS

%

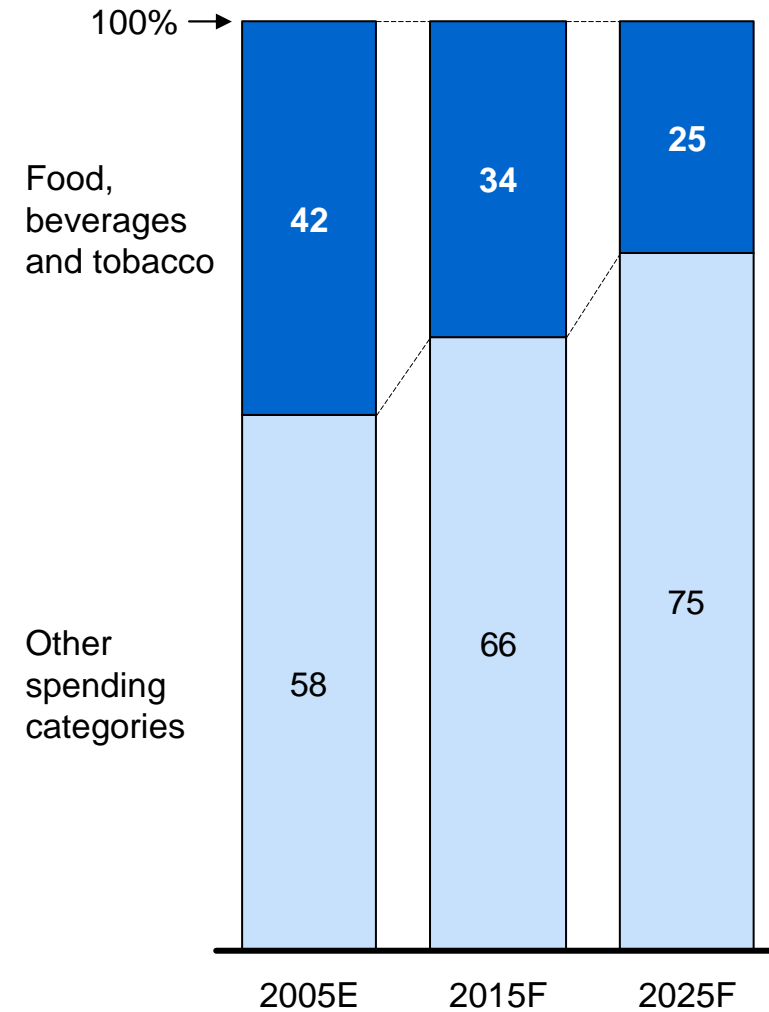
Share-of-wallet of urban households in 2005E



Share-of-wallet of rural households in 2005E



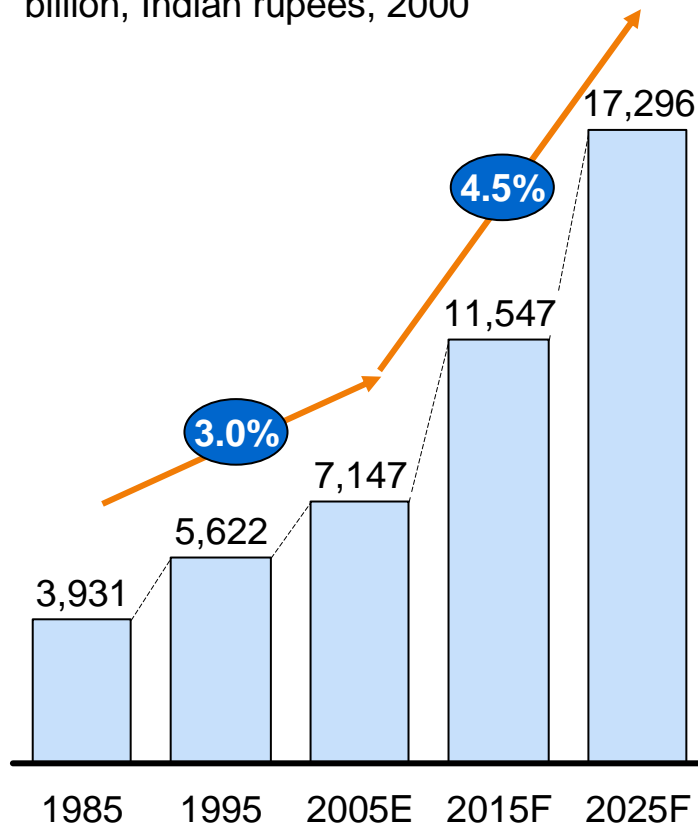
All India average share-of-wallet evolution



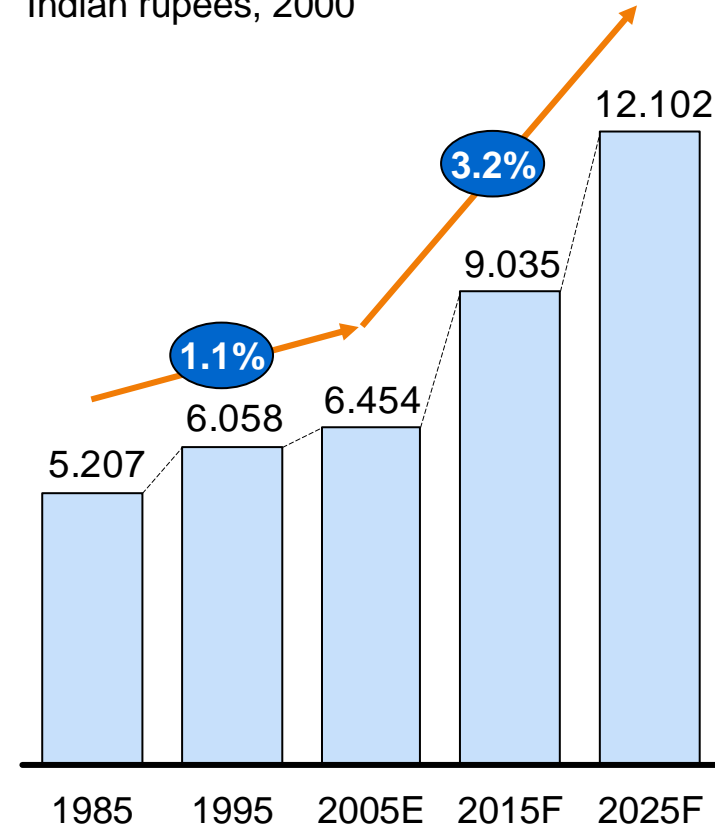
FOOD CONSUMPTION WILL ACCELERATE SIGNIFICANTLY EVEN AS ITS RELATIVE SHARE DECLINES

 Compound annual growth rate

Total consumption of food, beverages, and tobacco*
billion, Indian rupees, 2000



Per-capita consumption of food, beverages, and tobacco*
Indian rupees, 2000



Share of total consumption %

Year	Share of total consumption %
1985	59
1995	56
2005E	42
2015F	34
2025F	25

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* Approximately 90% of spend on the broad category “food, beverages, and tobacco” is on food.

FIVE CATEGORIES WILL ACCOUNT FOR MORE THAN 80 PERCENT OF CUMULATIVE CONSUMPTION OVER THE NEXT 20 YEARS

Breakdown of total cumulative consumption across categories (2005–2025)

trillion, Indian rupees, 2000

