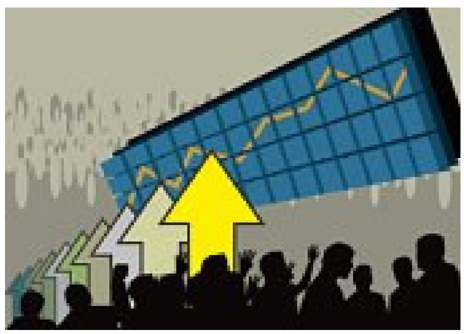
Market wisdom INVESTOR EMPOWERMENT SERIES
LESSON NO. 31 FROM THE HOUSE OF ASIT C. MEHTA INVESTMENTS

Index 15600 ↑↑↑↓↓↓ ?

The question that is top most in the minds of most investors is - Where do we go from here? Though Index does not and should not impact the fortunes of a particular stock or an investment strategy, still each rise and fall of the index does spark several questions. Every rise creates a kind of mental barrier in taking an investment decision as to whether we should sell-off our entire holding since the index is all-time high or should the investor buy at this price. If you understand share valuations then these questions are hypothetical but nonetheless we should take a look at how indices have behaved world over and what is likely to happen in India.



A study of world markets, as shown in the chart below, indicates that large movement in Index is not something, which is unusual. Hence, what is happening in India is not just "India Story" which is driving the Index and is unique to India but a phenomenon that has been experienced even in mature markets of the world.

Some Great Bull markets in History			
Asset Class	Lows	Highs	Times
Dow (1922-29)	60	380	6x
Dow (1949-66)	162	995	6x
Nikkei (1960-89)	1357	38916	29x
Gold (1972-80)	35	850	24x
Dow (1982-00)	1000	11722	12x
NASDAQ (1991-00)	350	5000	14x
Sensex (1989-92)	685	4500	6.5x
Sensex (2001-07)	2595	15600	6x

(Compiled by Ramesh S Damani)

Hence, the Indian market does not appear to be overheated. The rise is six times, which is the lowest rise as compared to the ones happened amongst the big bull runs. If the Index was to reach 25000, then the rise would still be less then 10 times. So, anything is possible.

We need to examine the reasons why markets may continue to go up. Famous Investment Guru Mr. Marc Faber has said, "Bull markets are born in the depths of depression and are reared on declining interest rates and rising corporate profits". In India after the recent spurt in interest rates and increase in inflation caused concern that the economy is in trouble. But the government has managed to control the inflation and interest rates are again likely to come back to 2-year-old levels. Hence, corporate profits will continue to be the single biggest driver for markets to do well.

A study of quarterly results of some leading companies shows that many of our companies have performed consistently over the last 4 years. Despite rise in interest rates during January - April, Indian companies were able to report better earnings. According to data available of the 3650 companies 329 have reported their Q1 earnings. These companies were able to report year-on-year (Q107 v/s Q108) 24.33% rise in their incomes and were able to report 41.21% rise in their net profits. If this growth story continues then the markets will continue to reward such companies. Hence, the argument that Indian stocks are expensive does not hold much merit if the company has proved consistently over 16 quarters that growth is a way of life. The signals for down turn of the market will also come from the quarterly results only. If a company starts showing negative growth for 2-3 quarters then a reexamining of your investment in the company is due.

The GDP growth is another important indicator of economic growth. A compounded growth of 9 % p.a. for 7 years will lead to doubling of the economy. Economy grows, savings grow and so does the investible surplus. This leads to enhanced liquidity and more purchasing power. Investors look for avenues to invest and different class of assets are experimented with. Investors vary of shares make humble beginnings and enter the stock market through the mutual fund route. This is happening today with the growth of Mutual Funds AUMS. A slackening of GDP growth will be another important indicator of downward turn in the market.

The concerns that could slow down the growth of the markets are few. The full capacity utilization is one primary bottleneck in many industries. Other concern being the structure of derivatives market; absence of deliveries in the settlement of derivatives trades can trigger a technical fall since traders can irresponsibly sell. Since there is no obligation to deliver, they can take advantage of the panic. Another concern is due to nature of speculators. Day trading culture makes the entire market hollow since the participants in the market are not monetarily strong to wither a fall, and this could lead to further accentuate the fall.

New investors would like to enter the markets, but their knowledge levels are low which leads to fear for participating in stock markets. As there is no visible concentrated attempt to educate the investors, it further compounds the problem. There is unhealthy competition amongst the brokers in terms of price wars who almost try to lure the investors into day trading. Instead of expanding the market, there is a fight for the same set of investors and volumes.

Sensitivity to global markets is another blind area, which can trigger a fall. But history has shown that such falls are only temporary and markets bounce back to the local fundamentals in the medium-term. Soft entry barriers in the form of huge paper work and cost, reduces the ease of investing. Signing at 35 places to open a trading and demat account is a major mental block for the paper work wary Indian citizen.

The choice of companies available for investing also needs to be considerably increased. Government must take advantage of this Bull Run and make the PSU company shares available to Indian investors. This will give depth to the stock markets. Over heating of markets due to lack of quality paper must be addressed by the largest issuer of our country namely the Government.

The strengthening of the rupee is another factor that is a concern for export-oriented companies though it is company specific. Companies, which are having debt in Dollars, have in turn benefited in a big way, as they have to repay less sum in Rupee terms. Well-managed companies are known to learn how to manage the currency fluctuation risk. In the short run if there is a sudden fall then quarterly results may be impacted, but over a period of time these risks are built into the company projections and better contracts are negotiated in order to take care of fall in earnings or new markets are tapped since some markets may find our goods and services too expensive. Ultimately rewards are for good management and are growing despite adverse circumstances.

Great Booms have ended in great busts. The fall has been as high as 80% from peak levels and it takes the market as much as 20 years to recover.

Asset Class	Bull Highs	Bear Lows	% Decline	New Highs in months
Dow (1922-29)	380	41	89	300
Dow (1949-66)	995	580	41	192
Nikkei (1960-89)	38916	7607	80	NR
Gold (1972-80)	850	150	82	NR
Dow (1982-00)	11722	7286	38	78
NASDAQ (1991-00)	5000	1114	77	NR
Sensex (1989-92)	4500	1980	56	132
Sensex (2003-07)	15600	???	???	???

(Compiled by Mr. Ramesh S Damani)

In the end, I would like to say that these are challenging times. A lot is happening around us. There is ample opportunity to make money but risks are also there. Still, there are more positive factors If you have invested in good governance and growing that can fuel the growth be it economy or corporate results. The only comfort is that things will not happen overnight. companies, they will not fall overnight. Learn about investing, risk diversification and the companies that you invest in. Remember selling is as important as buying. Have no greed and you will have no fear!!

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