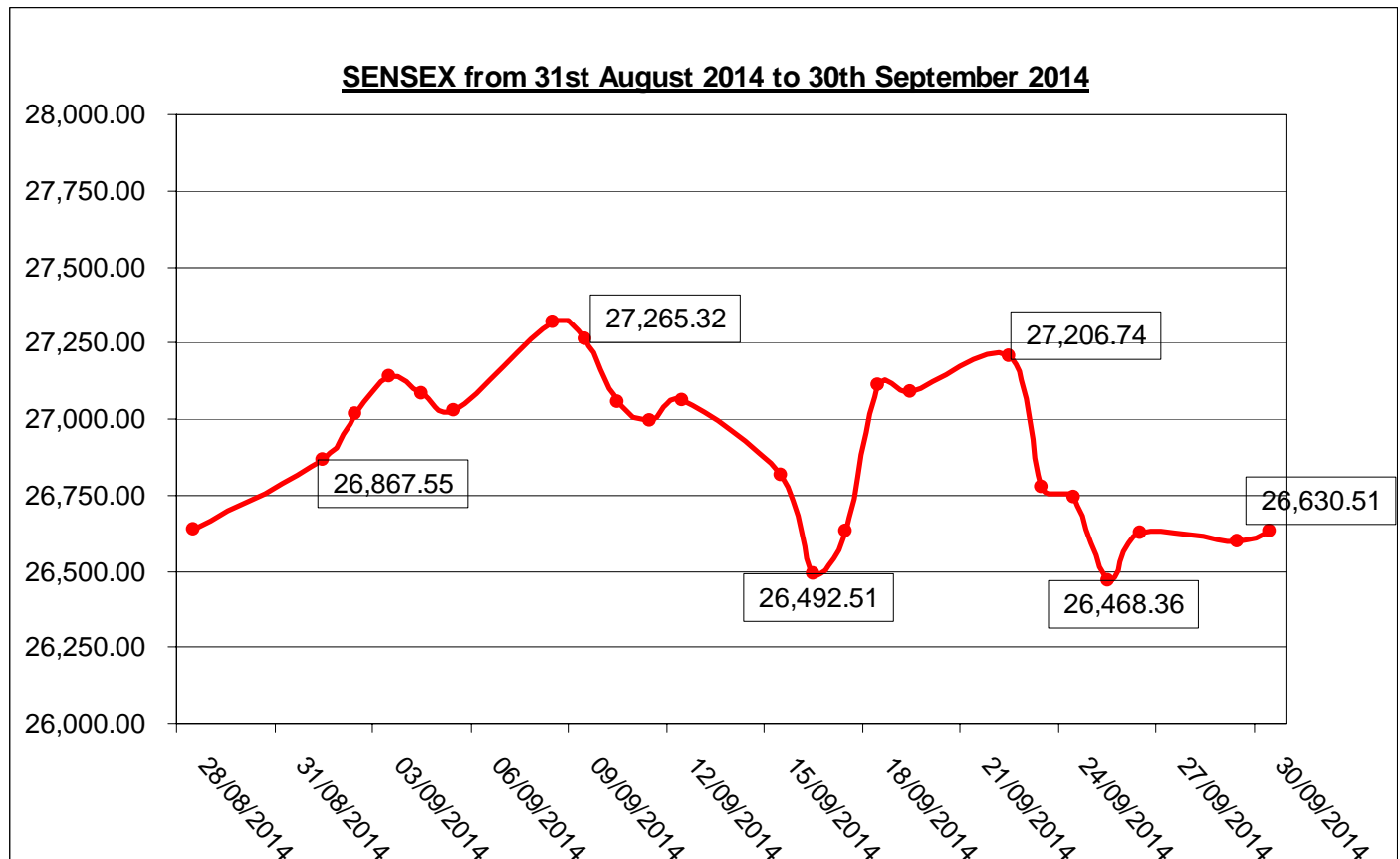




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## A Range Bound September



### Stocks Range Bound in September

September turned out to be a flat month for the stocks. Corporate news flow was light as media focused on Prime Minister Modi's efforts to boost ties with other superpowers. First, was his trip to Japan, then the Chinese Premier's visit to India and that was followed by his much acclaimed trip to the US. Apart from these high profile events, the Prime Minister of Australia visited India and our PM has visited Brazil, Nepal and Bhutan in the past four months since he took office. Foreign policy experts have termed each of these bilateral meets as successful and there is no doubt that India's image has climbed up a few notches in the international community. But the question we ask is whether all of this was necessary at this juncture?

### Focus on Foreign Policy

India's trade with the world has scope to improve. There is also the need to attract foreign investments. But is it not better to improve the environment here in India before laying out the red carpet for foreign companies? Even if an MNC does decide to set shop here, the going is not easy. There are hurdles in land acquisition, labour laws are archaic and infrastructure is a disaster with erratic power supply and poor road / railway connectivity. There are also the plethora of licenses and registrations which are required to start and operate a venture in India. Shouldn't all of these be given attention rather than trying to generate excitement about India abroad?

**Tepid Start of  
the New  
Government**

In our previous newsletters, we have expressed disappointment at the way the new government has begun its term. There are several areas which need urgent attention but these are not being taken up. While the new government remains in a honeymoon period, this situation will not last much longer. Sooner or later, they will have to account for what has been accomplished. Managing the elevated expectations of the nation of the size and diversity of India can be extremely challenging and this euphoria we are experiencing can quickly turn to gloom. These foreign jaunts and inviting world leaders to India, deflect the serious work which needs to be done internally. Moreover, the window of opportunity to bring about serious change is only for the next 4 years and 8 months; till there is a stable government at the centre.

**Stocks  
Awaiting  
Government  
Action  
Languishing**

Focusing on the markets, there is an interesting trend which needs to be highlighted. The types of stocks which have declined / underperformed since Narendra Modi has taken charge are the ones which are in dire need of government action. A list of such stocks is as per the table given hereunder. Stocks with market capitalisation of more than Rs.10,000 crores have been considered. These stocks have corrected despite a Sensex gain of 9.96 % in the same period.

Sr. No.	Company Name	Market Cap	Price on 30th May, 2014	Price on 30th September, 2014	%chg
1	JP Associates	16,187.97	72.95	26.55	-63.61%
2	GMR Infra.	13,000.62	33.40	17.55	-47.46%
3	Jindal Steel	27,603.74	298.00	172.95	-41.96%
4	IDBI Bank	14,988.82	93.45	61.00	-34.72%
5	Oriental Bank	10,164.92	339.00	230.05	-32.14%
6	DLF	37,377.97	209.80	150.85	-28.10%
7	Adani Power	17,317.68	60.30	43.40	-28.03%
8	Reliance Power	26,592.63	94.80	70.25	-25.90%
9	Bank of India	19,836.20	308.85	231.75	-24.96%
10	UCO Bank	10,563.13	104.10	79.80	-23.34%
11	REC	31,554.28	319.55	249.70	-21.86%
12	NHPC Ltd.	27,455.26	24.80	19.50	-21.37%
13	S A I L	36,142.14	87.50	69.60	-20.46%
14	Tata Power Co.	28,094.57	103.85	83.00	-20.08%
15	Power Fin.Corp.	38,584.79	292.30	234.45	-19.79%
16	Central Bank	10,141.80	75.10	61.10	-18.64%
17	B H E L	59,268.63	242.15	200.95	-17.01%
18	Canara Bank	19,149.21	415.15	350.25	-15.63%
19	Reliance Infrastructure	18,191.02	691.70	585.15	-15.40%
20	NTPC	131,803.68	159.85	138.65	-13.26%
21	Neyveli Lignite	15,887.91	94.70	82.85	-12.51%
22	Reliance Inds.	344,332.70	1,065.15	945.35	-11.25%
23	Union Bank (I)	12,987.33	206.05	188.60	-8.47%
24	Coal India	234,431.70	371.15	341.35	-8.03%
25	SJVN	10,217.45	24.70	22.80	-7.69%
26	Cairn India	64,392.05	337.55	311.60	-7.69%
27	Punjab Natl.Bank	34,184.84	944.15	887.30	-6.02%
28	Larsen & Toubro	143,646.38	1,548.90	1,457.45	-5.90%

The stocks which have done well are the ones which require minimal government action. Their list is also given hereunder:

Exporters and  
Quality  
Businesses  
Rally

Sr. No.	Company Name	Market Cap	Price on 30th May, 2014	Price on 30th September, 2014	%chg	Price Earnings
1	Eicher Motors	18,089.35	6,677.50	11,987.40	79.52%	50.33
2	Bharat Forge	11,683.07	501.85	822.20	63.83%	40.99
3	Cipla	30,843.40	384.15	625.70	62.88%	22.64
4	Britannia Inds.	10,552.60	879.75	1,396.85	58.78%	32.96
5	Emami	10,535.07	464.10	697.40	50.27%	31.35
6	Lupin	41,979.40	936.10	1,394.95	49.02%	25.36
7	Castrol India	14,579.66	294.80	429.80	45.79%	38.00
8	Aurobindo Pharma	19,463.46	667.70	966.85	44.80%	14.26
9	Ranbaxy Labs.	18,952.60	447.20	639.70	43.05%	35.60
10	Cadila Health.	19,069.48	931.40	1,323.80	42.13%	25.89
11	Torrent Pharma.	10,352.03	611.75	868.25	41.93%	16.37
12	Divi's Lab.	16,887.79	1,272.15	1,799.30	41.44%	26.87
13	Sun Pharma Inds.	125,804.69	607.40	857.30	41.14%	30.69
14	P & G Hygiene	12,476.81	3,843.75	5,381.00	39.99%	57.63
15	Havells India	12,079.46	193.55	264.70	36.76%	35.17
16	Maruti Suzuki	68,557.06	2,269.50	3,064.35	35.02%	28.21
17	Bajaj Fin.	10,132.54	2,020.85	2,711.00	34.15%	15.13
18	Motherson Sumi	26,315.90	298.40	395.25	32.46%	27.60
19	Bajaj Finserv	13,573.05	852.90	1,129.50	32.43%	9.35
20	Dr Reddy's Labs	41,642.18	2,448.10	3,227.65	31.84%	19.87
21	Pidilite Inds.	15,518.97	302.75	397.30	31.23%	40.65
22	Titan Company	27,588.39	310.75	407.65	31.18%	43.91
23	Glenmark Pharma.	14,931.21	550.50	720.65	30.91%	23.01
24	Tech Mahindra	44,746.41	1,915.35	2,487.65	29.88%	17.81
25	Essar Oil	13,731.43	90.85	116.80	28.56%	142.02
26	TCS	419,984.45	2,144.20	2,738.20	27.70%	23.60
27	Bharti Infra.	43,743.31	231.50	295.45	27.62%	31.20
28	Marico	15,696.87	243.40	310.15	27.42%	33.61
29	Infosys	168,912.70	2,941.50	3,747.65	27.41%	18.40

Source : Cline

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From the above distribution of gainers and losers, one could conclude that markets are factoring in very little policy initiatives or reforms on the part of the government. A decline in interest rates is also not being anticipated as interest sensitives have also lagged.

Expensive  
Valuations,  
Stock Picking  
a Challenge

Under normal circumstances, this would not be a cause for concern, as diversity of our stock markets is a key strength. However, the massive liquidity infusion of the past few months, has expanded Price Earnings (PE) multiples. Several companies (in table 2)

have become quite expensive, considering their long term growth potential and many quality companies are trading at the higher end of the valuation band. The price earnings ratio is mentioned against the scrip and it is based on the trailing 12 months earnings per share. Stocks with high PE multiples have appropriately been highlighted. No doubt valuing companies purely on a PE multiple basis is not the best method but this ratio does offer a simple data point to judge if the stock is cheap or expensive.

The underlying philosophy behind sensible investing is to buy into quality businesses at reasonable valuations and that is where there are challenges. There are several quality businesses listed on Indian bourses and many more have upgraded themselves to investment grade. However, valuations are on the higher side and there is not enough margin of safety.

Our Forecast  
and Strategy

This situation may play out in either of the following manner:

- I. Stocks continue to rally and become more expensive and then what we have is a bubble on our hands. This scenario is most likely if retail investment buying picks ups.
- II. There is an extended period of sideways movement as earnings catch up. The scenario appears most probable provided there are no external or internal shocks. It could also be that earnings surprise on the upside and valuations become more reasonable i.e. PE multiples contract.
- III. Stocks correct by 15-20 % with the index itself correcting by about 10 %. For this to take place, a catalyst / negative event has to occur. Without a reason, this scenario will not materialize.

Irrespective of what eventually happens, we maintain our cautious view and advice investors to stay on the sidelines for the time being. FII buying has slowed down and for the month it was at Rs. 5,374 crores; the least since February. Domestic institutional flows have turned negative (Rs. 1,573 crores) after being positive in the previous month.

A most appropriate investment strategy would be to buy on declines or if there is a sizable earnings improvement. Another earnings season will commence in October and that could be quite interesting with new ideas for investment.

We take this opportunity to wish all investors a Happy Diwali and a Prosperous New Year.

*Dipan Mehta*