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INVESTMENT PERSPECTIVE

India : Outperforming Nation for the Decade

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In fundamental sense, Earnings and Valuations are the prime determiners of Price of a Company. As earnings do not change on day-to-day basis, valuations play an important role in price formation in the short term. Aggregate for a country's valuation, Market capitalization to Gross Domestic Period (Market Cap to GDP) popularly known as ***The Buffet Indicator*** is commonly used to compare valuations of a country over a period of time or of various countries at a particular time.

The Market Cap to GDP for India is around 78% on FY24E as against its long term average value of 80%. The Market Cap to GDP of US is 179% on FY24E basis against its long term average of 150%. Also, keep in mind the historical long term average for the World is 125%.

There are two inferences that come out:

1) India itself is trading lower to its historical average of Market cap to GDP

2) India is trading lower to US and many other growth countries of the world

There is no universal fixed range of Market Cap to GDP which can be attributed as the standard. The figure ranges from 1490% for Hongkong, 300% for Switzerland, South Africa etc to 0.2% for Algeria to 21% for Pakistan and so on. This means that the ratio ranges widely amongst different countries. Also, different countries have had different ratios at different times of history.US market cap to GDP, once traded in the range of 40 to 80% until 1990 and thereafter the range moved upwards and settled around 100 to 150%. There is always a context to which any of the valuation multiple trades at. Market cap to GDP of every nation has traded based on Corporate Profit as % to the GDP. For long till 1995s, when US corporate profit to GDP was lower than 7%, the valuation ratio remained subdued under 100 and as the corporate profit percentage moved up to 10%, there was an upward shift in the valuation ratio from 100s to 150s.

India's corporate profit since 2008 fell from 7.8% to recent 2.8% in 2019 and further low at 1.6% in FY20 as there were many one offs in the earnings of various companies. Banks and NBFCs went through turbulent phase of NPAs and reduced loan growth and manufacturing companies were suffering from high debt burden. However, now we are out of NPA cycle (since 2018) and capex cycle is improving as capacity utilization for companies are nearing 70-80%. There is double digit growth in loan book of banks/ NBFCs. The corporate profit to GDP has already risen to 4% in FY22 and is expected to move much further up during the current decade.

So this decade would be a good decade for Indian investors, the current valuations of India provides enough opportunity for price appreciation as India by itself is trading lower than average market Cap to GDP and as the share of corporate profit increases in GDP, the average itself should move upwards from level of 80.

There are other statistical trends too that suggest the thesis of India being an outperforming nation this decade. There is an interesting pattern that in a cycle of 8 to 10 years, developed Markets and Emerging markets have outperformed each other alternatively. In a period of 1985 to 1993, MSCI EM IDX gave a return of 390% vs 118% return by S&P 500 SPX then between 1993-2002, S&P 500 outperformed MSCI EM IDX by 187%. In the period of 2002 to 2010, again Emerging market Index outperformed by 300% and in the recent period 2010-2020, Developed market gave a return of 200% against Emerging market performance of -2%. Going by this trend of alternating performances, this decade from 2020-2030 should belong to the Emerging market, and there are various fundamental reasons to support this assumption. One important visible trend is in Bond Yield rates. This all should help Nifty 500 to outperform US S&P 500.

To get benefitted from the underlying improvements in India and the Equity Markets, it is important to stay invested with the market or top up your investment.

HAPPY INVESTING!

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