August 2021

MARKETS & MORE

Monthly Communiqué by PRSSB LTD

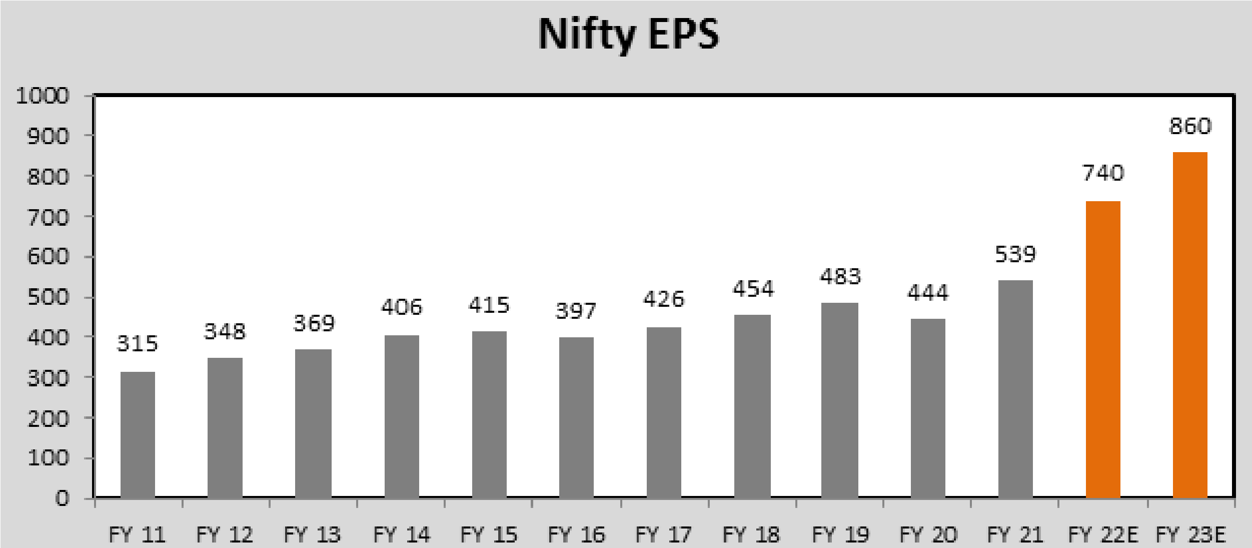
THE REASONS BEHIND THE RESILIENT MARKETS & MORE

Greetings from PRSSB!

Starting this month, we would be bringing to you some of the important insights about the markets, in a simple and easy to understand way. One question that we have been getting for a while now is -

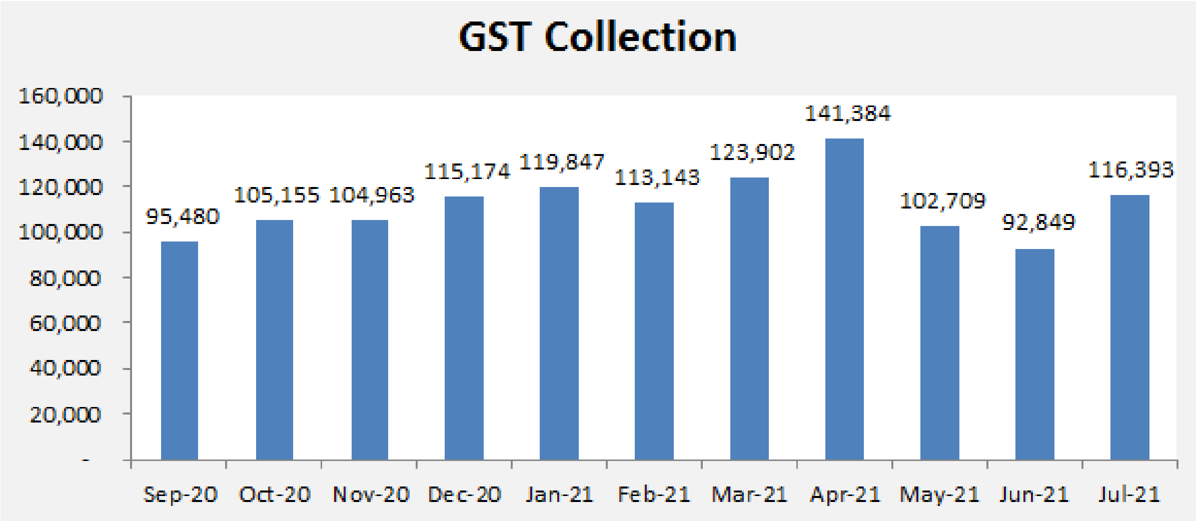
Why Markets are at so HIGH levels in spite of the Economy not performing? Also, **why are Markets not taking into account the GDP estimates in its valuation?**

To this, we have a very simple narrative. **Markets always follow Earnings**. If the earnings are resilient, Markets will continue to remain at elevated levels. Look at this 10 year chart of NIFTY EPS -



If you take a careful look at the Nifty EPS from FY14 to FY20, it remained in the range of Rs 400-500 but was never able to cross 500. **And in FY21, the Nifty EPS surprised all analysts to end at Rs 539. This was despite the fact that 3 months of the Fiscal 21 were completely washed out due to the nationwide lockdown imposed due to COVID-19. Hence, the earnings not achieved in a normal year were achieved in a year where 1 quarter of earnings was completely washed out.** The Bloomberg consensus estimate for the NIFTY EPS for FY22 and FY23 continues to remain high. This, of course, has also to do with the fact that the composition of the Nifty during these years has changed in favour of High PE stocks. Hence, looking at the above data, **we believe that an approach of waiting for the markets to come down to begin investing may not work in your favour.**

One must remember that Markets are forward looking machines that discount the future cash flows to the present in order to arrive at a fair value. While one may wonder as to why are Markets performing but the GDP continues to give subdued figures, one must understand that **GDP is a lag measure that continuously gets revised. Some of the more accurate metrics of gauging the level of economic activity include GST collections, Electricity consumption, E-Way bills, PMI Manufacturing, PMI Services etc. These provide a realtime measure of the economic activity rather than GDP** that is estimated and revised continuously. Hence, Markets continue to perform inspite of the fact that GDP for the economy is at a subdued level. Plus, different agencies have a different measure of GDP and it continuously gets revised. Hence, Markets, in our opinion consider other measures of the Economic activity as a better measure than GDP.



A careful look at the GST Numbers would suggest that the level of economic activity has picked up quite substantially. **Barring June 2021, GST collections starting from October 2020 have crossed the Rs 1 Trillion mark. This is despite the fact that sectors like Hospitality, Tourism, Entertainment have not opened up fully. Similarly, the E-Way bill collections was at its peak in March 7.12 crore.** The **Exports number for July 2021 came in at $35.17 Bn**, which is a fairly high number. The **PMI Manufacturing index came in at 55.1** for July which shows a lot of optimism in the Markets. Hence Markets have stayed up and are factoring in a very healthy Earnings growth despite the fact that GDP has contracted. **Corporate India has reduced Debt substantially** in the past few months.

One more factor that is keeping Markets at elevated levels is the **Low Interest rate environment**. Interest rates are at an all time low with the Repo Rate at 4% and the Reverse Repo rate at 3.35%. **1 quarter of washout of Earnings can impact valuation of a company by 3-4% but a 1% drop in the Discounting factor can lift valuations by 15% and is very favourable for surviving companies**. Hence strong companies with dominant franchisees are commanding a high multiple.

With the economy gradually opening up, a lot of pent up demand is likely to come that may translate into a very healthy earnings growth. Due to these factors we believe that the Markets can sustain the current valuations unless the Delta variant creates a havoc in the economy.

We hope that you enjoyed this read. If you have any queries/suggestions/comments, you may write to us on rushabh@prssb.com

Thank you and Happy Investing!

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