

Market Flash

March 17, 2008

A TALE OF TWO FIFTIES

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Indian equity markets have experienced two fairly different movements over the 100-day period from November 25, 2007 and March 4, 2008.¹ Even more interesting is that the divergence was split into two 50-day periods. Indian equity markets are currently causing widespread concern, as they seem to be falling faster than Asian markets, but investors must look at the full 100-day period to get the entire picture

Exhibit 1 shows how Indian equity markets have performed, versus Asia as a whole, over the 100-day period, while Exhibit 2 shows how the spread between the two has changed over the same time period.

Exhibit 1 - Indian Equities Versus Asian Equities



Source: Bloomberg as of March 4, 2008

Exhibit 2 - Spread between Indian and Asian Equities



Source: Bloomberg as of March 4, 2008

Indian equity markets have indeed fallen faster than the rest of Asia since mid-January, but it is also important to note how they performed before this time.

Between March and October 2007, Indian equity markets closely followed Asian markets. As Asian markets fell beginning in October 2007, India continued to rise until the middle of January. In fact, they outperformed Asia by nearly 55%. Since that time, the spread has reduced from 55% to 15%. This suggests that India was slower to react to the global market slowdown.

Why was India's equity market slower to react?

We believe there are a number of reasons why India's equity market did not fall at the same time as its regional counterparts.

- India was relatively insulated from the spillover of the U.S. subprime mortgage market crisis, as Indian companies had little or no exposure to this particular market.
- India is not a net exporter, and therefore, runs a current account deficit, rather than an account surplus. The impact of a global slowdown may not be as significant to a net importer.
- India was further supported by strong domestic investment demand.

So what has changed since that time?

Although it was slower to react, India did eventually experience losses. A number of drivers accounted for this loss:

- Several quarterly results released in January were more disappointing than the market had expected.
- Power utility stocks and those in certain other sectors such as real estate were discounting five-to-seven-year forward earnings. As is usually the case, these stocks fell by the greatest degree.
- The Indian government's annual budget was perceived as negative towards its banking sector, as it proposed waiving delinquent farm loans to the tune of US \$15 billion, and these loans were originally made by banks
- Global news and events typically related to subprime and credit added to the weak sentiment.

¹The 100-day period is from November 20, 2007 to March 4, 2008. The 50-day periods are from November 25, 2007 to January 14, 2008 and from January 14, 2008 to March 4, 2008. Past performance is not indicative of future results.

Bottom Line

The recent fall in the Indian equity markets means that some companies with significant competitive advantages are available below fair value. Although the market may continue to fall moderately in price, the underlying businesses are still as robust, if not better, than they were a few years ago. However, it may be a while before the market delivers positive results. Nevertheless, the long-term outlook for Indian equity markets is positive. ■

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