Valtrust Momentum June 2023:

Markets Aren’t Cheap but Aren’t Expensive Either.

When markets are down, the worry is if it can go down further. When the markets are hitting all-time highs, the worry is, is this the end of the bull market. In other words, there are hardly any times when everyone believes it's a good time to invest.

A year back when markets were lower, the fear was that of a catastrophe due to the Russian invasion of Ukraine. By the time that subsided came the news of the collapse of a few banks in the US and Credit Suisse in Switzerland. This brought back fears of the collapse we saw of Banks and Financial Institutions in 2008.

Inflation and rising interest rates were then seen as the biggest issue and one that could bring down the markets. Inflation has started to fall and interest rates have stopped moving higher.

If you torture the data long enough, it will confess to anything. This phrase has the largest application in stock markets thanks to the fact that one can use data that can be presented to showcase one’s view being right.

If one is bullish in markets, there are enough indicators that showcase why the bull run can continue for long. Same for bears who have even better ability to forecast doom at every turn for there is always something that seems the market is overlooking.

Even a broken clock is right twice and anyone making enough bear calls is bound to be right one time or the other. But in the longer term, the drift of the markets has always been to go up. This is primarily because of growth in population. A growing population has growing needs that need to be met and the only way is through higher growth.

In the long term, markets are very efficient. In a 10 year plus time frame, a stock generally has gone up only as much as its earnings. Both earnings and stock price movements can be lumpy and yet the twain can meet. Adani Power for example has compounded its profit at 21% per annum over the last 10 years while the stock which has delivered a similar return.

Of course, at times like these when markets are at new highs, the number of companies where profit growth equals market capitalization growth are less. Reliance Industries stock price has compounded at a far higher percentage vs its Profit. But this has come through PE expansion.

This brings us to market valuations. BSE Sensex currently trades at 24 times last four quarters trailing earnings. While this looks expensive, if you were to see the valuations Sensex has traded in the past, this is well in the middle of the range.

Markets aren’t cheap. They aren’t expensive either. At the end of 2007, Sensex was trading at 27 times earnings. While 27 is just 12% above current prices, that 27 came at the peak of an earnings cycle unlike this time around. Earnings season starts in July. Strong earnings would dampen the PE ratio without the markets having to see a fall.

India sees a National Election in another 10 months. Historically unless one has been swept aside by global factors such as in 2008, markets tend to be bullish. With no expectations of a change of government as of now, markets should be steady to bullish as we approach the election.

Having said that, it is very much possible that markets can correct 10% from any levels and an all-time high could be one such trigger. The odds though for now Favor a continuation without any serious reversal in the offing. We aren't where we were at the end of 2017 let alone where we were at the end of 2007.

In other words, there is more space to go higher before we reach the level of unreasonableness.