# PERSPECTIVE

## DECEMBER 2020

**Date: 05/01/2021**

Our internal data mining indicated that **final expansion can be explosive and can take Sensex to 41,500** but interestingly Sensex **exceeded everyone expectation and closed at 47500** for Calendar year 2020. **From 'aur kitna neeche jayega' to 'aur kitna upar jayega'** tells that **in bull markets, we are blind to risks** and **in bear markets, we are blind to opportunities.**

**So with above note, let's understand current market Scenario:** Central bankers are **pumping in money at a mind-boggling rate of $1bn+ every hour**. Free money **led to negative yields ($18 trillion of global bonds) which led to more equity participation**. **Stimulus is like drugs!** More you give more people wants but finally it take the person either to rehabilitation center or ruin people's life. **Similarly extreme stimulus has worked well** on the way in **but exiting will prove harder to do & for that the first signs of rising inflation** will be a test. After election result and **Biden win, only green shoot visible is Falling DXY** (Dollar index against basket of 6 developed economy currencies) which will keep the fund flow intact in Emerging markets. Remember, **one can't run a marathon on one leg.**

**March 2020: Use more courage; Dec 2020 onwards: Use more knowledge.**
Valuations don't matter are winning the argument right now. However, **eventually we always realize that "Valuations do matter"**. Over **the short run, markets are driven** by multiple factors such as **fund flows, headline-grabbing news, and sentiments**. Over the **long run, equity returns** are **driven largely by fundamentals**. Either earnings will have to go up substantially or markets will have to correct for these overstretched valuations to revert to mean/fair value. **Corporate earnings are slaves to Nominal GDP (GDP + INFLATION)** in long run. With **Nominal GDP growth of 8-9%** one **can't expect 18-20 % earnings growth** to justify current higher valuation.

**In a nutshell: "Fundamentals" market ko jeene nahi dega aur "Liquidity" Market ko marne nahi dega**. **Low interest rates** justify high valuations in equities; remember they **also justify low future returns**. **Investing at high valuations** tend to reduce long-term returns and also **increases the probability of making losses** and their extent.

**Balancing out all above views, here are the numbers:** We have seen in 2020 **price action is two steps ahead of fundamentals. Media focus upon mood** and chase price action but **our major focus is on studying underlying value** through statistical analysis of wide array of valuation metrics. Our valuation implied forecasts indicates that **fair value of Sensex has risen from 33,000 to 37500-38000** (**Overweight@ Equity**).Reason behind for the same is earning growth in last quarter and coming quarter due to pent demand (Demand which was suppressed due to lockdown)and various cost cutting/saving measure across industry.
**Our guesstimate based on internal prop** model tells that **valuation band during – Harshad Mehta scam** (which too driven by liquidity) translates today into **51000-52000** (Best case scenario – **Underweight@ Equity**).

**Action plan for investor:** Focus on minimizing drawdown. **Not losing Capital is more important than not participating in Upside** when markets are in irrational euphoric zone. **Following process** in ups & downs **requires complete detachment from emotions** arising out of Gaining or Loosing. Our internal Model asset allocation (Valuation-based framework) **currently shows 45-50% max towards Equity for Aggressive investor. Ideal/prudent allocation** at this elevated valuation should be **25-30%**.Do not get carried away by looking/chasing quick and easy money. Apply logic and stay cautious.

**Summing it all:** Markets have random environment hence **focus on process, everything else is noise. Sticking to well back-tested strategy** in irrational times yields better experience & outcome over time. Liquidity has helped us to **fly high like aeroplane** but **keep Asset allocation model as Parachute & safety kavach. When cheap: Buy and wait; when expensive: Wait and buy.**