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Business Standard, Delhi
Monday 6th January 2014, Page: 9
Width: 25.27 cms, Height: 25.37 cms, a3, Ref: pmin.2014-01-06.30.44

Rising market caps are a sign to watch

Many sectors gained in market capitalisation last year, while some lost out

CLIFFORD ALVARES

If there's one aspect of the market that often gets overlooked, it's the sectors that generate the most market capitalisation for shareholders. Last year was challenging for the market, given that it started with slow gross domestic product (GDP) growth. But despite the weak economic numbers, several sectors made strong increases in their market capitalisation.

Market capitalisation measures a business entity's value and factors that affect it include changes in the value of shares, either upward or downward. If there's a high demand for the stock, driven by greater profitability, market capitalisation is likely to move higher, while weaker demand with lower profitability and growth will hurt a company's value. Says Daljeet Singh, head of research, India Nivesh: "A market capitalisation increase is good for shareholders. Companies that do well see an increase in their market capitalisation and that could be seen across a lot of individual companies and sectors last year. But a lot of sections of the market also saw an erosion in market capitalisation."

Stock markets are near their peak levels but the market capitalisation to GDP ratio is lower than its previous peak in 2008. In 2013, the rally was largely concentrated in frontline stocks and indices, which did not lead to an all-round increase in market capitalisation to GDP ratio. The current market capitalisation to GDP level is around 60 per cent. Says Singh: "Market capitalisation is nowhere near the peak level of 80 per cent to GDP as the broader market has not participated in the rally."

The investor perception about a sector's or company's likely performance is a strong influence on market capitalisation. Other triggers for changes in market capitalisation could be structural, like those of the information technology (IT) sector last year, which saw the sector scale new peaks. Sometimes, the capitalisation is affected by bad news and macroeconomic conditions, as happened with the infrastructure sector last year.

THE WEALTH GAINERS AND LOSERS

IT sector saw the biggest gain in market value in 2013

Sector	M-cap (₹ cr)	y-o-y chg (%)
IT-software	370,380.00	64.1
Pharmaceuticals	68,263.00	21.9
Telecom services	46,462.00	26.3
Automobiles	32,900.00	10.5
FMCG	29,286.00	10.2

Banks made the biggest losses in 2013

Sector	M-cap (₹ cr)	y-o-y chg (%)
Cement	-17,161.00	-12.7
Steel	-18,205.00	-12.2
Finance	-30,360.00	-9.07
Power generation & distribution	-54,510.00	-16.6
Banks	-91,825.00	-11.2

Note: y-o-y change is for 2013

Says Mehraboon Irani, head, private client group, Nirmal Bang Securities: "It's all a question of money flow. People were looking to protect themselves last year, which saw money flow out from capital investment sectors into IT, Fast-moving consumer goods (FMCG) and pharmaceuticals. That's why you have seen the capitalisation of these sectors rise significantly."

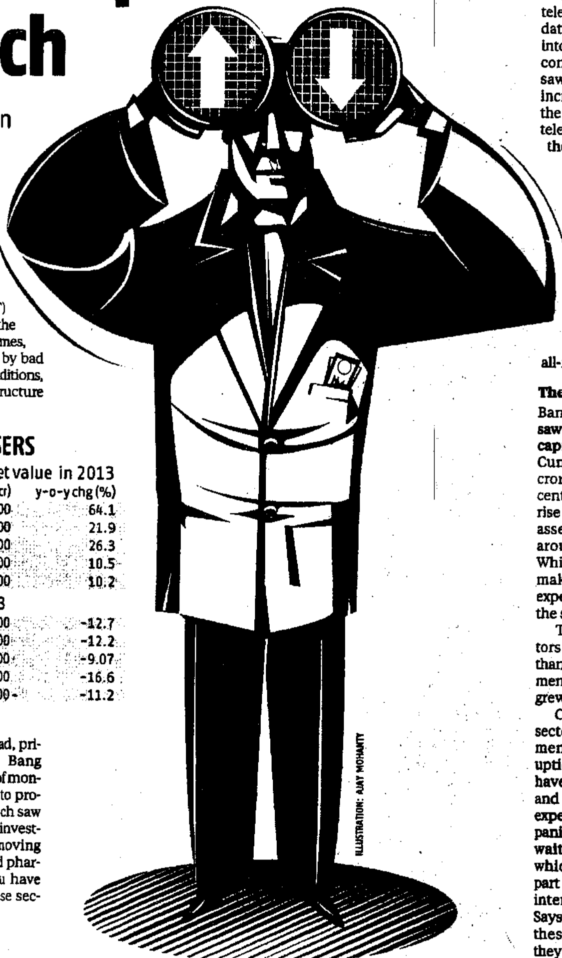

ILLUSTRATION: AJAY MOHANTY

Pillars of the market

The big pillar of strength for the market, despite a weak economy, has been IT, which gained a whopping 64 per cent in 2013. In absolute terms, the sector added ₹3.7 lakh crore in shareholder wealth last year, more than six times the second largest market capital gainer, pharmaceuticals.

Primary factors behind the strong performance were a weak rupee, strong growth in the US and Europe, and major IT deals coming India's way. In the next few years, the IT sector is expected to gain significantly, as its competitiveness is high, though the gains in capitalisation might not be as high as last year's. Says Singh: "The basic reason is that the US economy is improving, and technology spends will increase from the US. Indian vendors will benefit from the weaker rupee."

With the rupee around 62 against a dollar, the other sector that has gained tremendously over the past year has been pharmaceuticals. The sector gained ₹68,000 crore in market capitalisation last year, driven by expansion in operating profits. Many companies have seen top line growth of a little over 20 per cent, with expansion in earnings before interest, taxes, depreciation, and amortisation (Ebitda) margins to around 22 per cent last year.

Rising penetration of mobile telephony and increasing spends on data usage have begun to translate into capitalisation gains for the telecom sector. Telecom companies saw their market capitalisation increase by ₹46,000 crore last year, the third highest gainer. Experts say telecom companies will do well on the back of increasing penetration.

Growth in a few automobile companies led to a lift for the sector, especially for two-wheeler and select four-wheeler companies. The FMCG sector made decent market capitalisation gains last year on strong domestic spending, driven by decent volume growth. Despite the sector having higher valuations, in excess of 25 times the earnings, all-round growth has been visible.

The laggards of the market

Banking was among sectors that saw a significant erosion of market capitalisation last year. Cumulatively, banks lost ₹91,000 crore last year, a decline of 11 per cent. The fall was largely due to a rise in gross NPAs (non-performing assets) of public sector banks to around 5.5 per cent of the total. While some public sector banks are making significant changes now, experts say it's best to be selective in the sector.

The utilities, steel and power sectors all underperformed last year, thanks largely to lower capital investments, due to of which order books grew at a slower pace.

Over the next few years, these sectors could see a revival if investment in the capex cycle sees an uptick. Given that the larger names have more diversified businesses and are more likely to win orders, experts say it's best to buy into companies that are well-entrenched and wait for an economic recovery, which could take off in the latter part of the second half of the year, as interest rates could ease by then. Says Irani: "Money can flow back to these beaten-down sectors and they could see better relative market capitalisation gains next year than the frontline IT. It will be rebound faster if the economy picks up somewhere in 2014."

Due to slower sales and higher interest rates, the realty sector lost considerable market capitalisation last year. The sector is typically interest rate-sensitive. As rates rose, sales began to slow. As the rates are still high, the sector is likely to take some time to recover.