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CRISIL EquityInsight

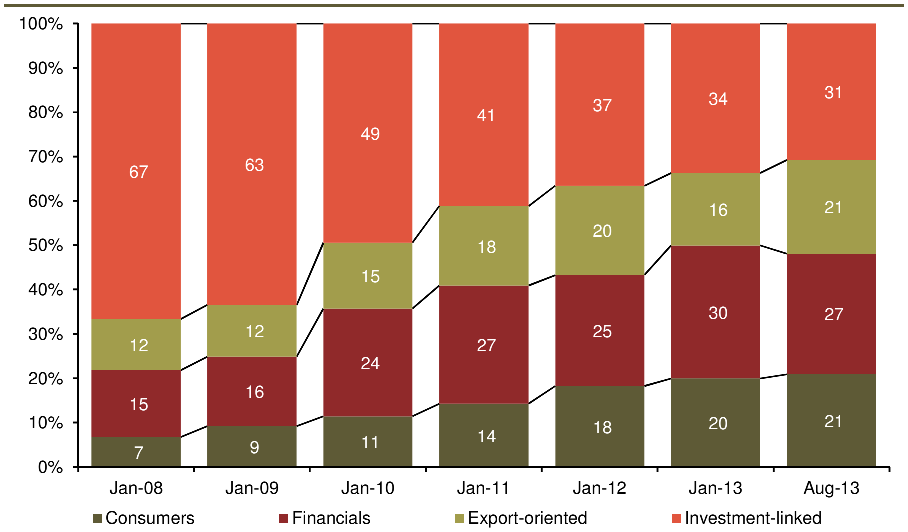
2008 to 2013: A tale of two Nifty(s)

Shift in sectoral weightages responsible for holding up of index levels

Between January 1, 2008, and July 31, 2013, the CNX Nifty posted a loss of 6.5%. Today, while the index seems to be holding up to 2008 levels, it is less reflective of the economy and does not seem to convey the worsening macro-economic situation. The GDP growth rate has fallen from sub-9% in FY08 to 5% in FY13 and CRISIL Research expects FY14 GDP growth to be at a moderate 5.5%. There is a general sense of gloom over the stock performance of most of the listed companies, with 550+ stocks among the actively traded ones listed on the National Stock Exchange (NSE) tumbling by more than half over the past five years. Even within the CNX Nifty index, the price to book (P/B) valuation has dropped from 7.1x in 2008 to 5.1x in 2013. Then, what is driving the index to almost January 2008 levels? The answer lies in the changing dominance and outperformance by a few sectors such as consumer staples, consumer discretionary, private sector financials and export-orientated sectors such as IT and pharma.

In January 2008, investment-linked sectors such as materials, industrials, energy, utilities and telecom dominated the CNX Nifty with a weightage of 66%. The weightage of any company/sector in the index is determined by the relative (to other companies/sectors) free-float market capitalisation of the constituents. The current slowdown has resulted in poor performance of these sectors, shrinking valuation multiples and consequent steep drop in the stock prices; thereby lowering of cumulative weightage to 31% by July 2013. The aggregate earnings of companies in these sectors remained almost flat during the period. On the valuation side, the weighted average P/B multiple of companies shrank from 7.3x in 2008 to 1.7x in 2013. As many as 22 out of 27 companies in these sectors (among 2008 Nifty constituents) displayed negative returns.

Figure 1: Movement of sectoral weightages over the past five years



Consumers: consumer staples and consumer discretionary; **export-oriented:** IT and pharma; **Investment-linked:** industrials, materials, utilities, telecom and energy

Source: CRISIL Research, NSE

Over the past five years, strong financial performance and increase in valuations of consumption and export-orientated sectors led to rebalancing of the weightage in their favour. These performing sectors—consumer staples, consumer discretionary, private sector financials and export-orientated sectors such as IT and pharma—now command 65% weightage in the index compared to 29% in 2008. Consumer-orientated sectors and private sector financials have benefitted from the consumption boom and government policies, while IT and pharma have received support from recovery in the global economy and weakening domestic currency. Among the biggest gainers of the pack are Lupin (599%) and Sun Pharma (372%). During the past five years, aggregate PAT of the companies in these performing sectors has grown at a CAGR of 21.9%.

Along with reconstitution of the Nifty, the concentration of top-10 stocks too has changed—it is at a five-year high of ~59.1% weightage currently, compared to 53.3% in January 2008. Further, six companies among the top-10 of 2008 have now been replaced. The polarisation towards a few sectors and among the top-10 stocks signifies increasing risk aversion among investors. While the consumption and export-linked sectors have provided resilience to the index, CRISIL Research believes that policy impetus towards investment-linked sectors is now critical for any sustainable uptick to the markets at large.

Analytical Contacts:

Mohit Modi
Director, Equity Research
Email: mohit.modi@crisil.com
Phone: +91 22 4254 2860

Vishal Rampuria
Associate Director, Equity Research
Email: vishal.rampuria@crisil.com
Phone: +91 22 3342 3525

Media Contacts

Priyadarshini Roy
Manager, Communications and Brand Management
Email: priyadarshini.roy@crisil.com
Phone: +91 22 3342 1812

Jyoti Parmar
Assistant Manager, Communications and Brand Management
Email: jyoti.parmar@crisil.com
Phone: +91 22 3342 1835

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CRISIL Limited
CRISIL House, Central Avenue, Hiranandani Business Park,
Powai, Mumbai – 400076. India
Phone: +91 22 3342 3000 | Fax: +91 22 3342 8088
www.crisil.com