NETRA

Early Signals Through Charts

February 2025

History's Handbook

DSP

How the World's Best Markets Look at Their Worst

For an extended period, we have experienced only the favorable side of the markets. However, markets do not rise indefinitely—cycles are an inherent part of the financial landscape. During euphoric phases, narratives, noise, and speculative stories dominate, reinforcing a sense of complacency. It is often in these moments that we hear—or even begin to believe—the four most dangerous words in investing: "This time, it's different."

At their worst, equities earn bond-like returns with volatility similar to that of a common stock. This is because, during a bull market, participants end up overpaying for stocks. The promise of stellar earnings growth or pure stock price speculation causes stocks to become mispriced and deliver low returns, at times underperforming even the bond market. These are also the moments when stocks become cheap enough to once again be attractive investments.

At Their Worst, Equities Earn Bond-like Returns With Volatility Similar To That Of A Common Stock.

India

Date	1 Year	3 Year	5 Year	10 Year	FD 10 Year Returns*
26-04-1993	-54%	37%	35%	25%	11%
04-12-1996	-10%	-5%	8%	19%	12%
21-09-2001	-39%	-5%	-5%	4%	12%
09-03-2009	-49%	-8%	7%	8%	10%
23-03-2020	-32%	-4%	-2%	4%	8%

1990 to 1994 cyclical numbers are off the charts due to the scam of 1992

USA

Date	1 Year	3 Year	5 Year	10 Year	US treasury Returns#
26-05-1970	-34%	-9%	-5%	2%	4%
01-10-1974	-41%	-14%	-7%	-3%	4%
19-10-1987	-6%	10%	10%	9%	8%
03-04-2001	-27%	0%	11%	11%	8%
23-07-2002	-33%	-16%	-3%	7%	7%
09-03-2009	-48%	-19%	-10%	-6%	5%
23-03-2020	-20%	-2%	1%	7%	4%

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Source: National Savings Institute, Bloomberg; Data as on Jan 2025. *5 Year Maturity FD rates are considered. #Returns from holding US Treasury 10 Yr Bond

It's Not Easy to Outperform Gold, A Hedge Against 'Sovereign Stupidity'

Developed Markets (returns in 21st century)*	Equity Market Returns (In Local currency)	Gold Returns (in Local Currency)	Gold's Excess Returns over Equity Market
Japan	4.6%	11.3%	6.7%
UK	4.3%	10.6%	6.3%
France	4.2%	9.3%	5.2%
Canada	7.3%	9.4%	2.1%
USA	7.8%	9.4%	1.6%
Indonesia	12.6%	13.1%	0.5%
Australia	9.8%	9.7%	-0.1%

Country	Index	Gold Returns in 20 Years	No. of stocks outperforming Gold	% of stocks outperforming Gold#
India	NSE 500	13%	193	43%
USA	S&P 500	10%	54	11%
UK	FTSE 100	12%	1	1%
Japan	Nikkei 225	12%	3	1%
China	CSI 300	9%	79	29%

Emerging Markets (returns in 21st century)*	Equity Market Returns (In Local currency)	Gold Returns (In Local currency)	Gold's Excess Returns over Equity Market
Turkey	21.1%	29.3%	8.2%
Brazil	8.2%	14.6%	6.4%
Poland	4.4%	9.3%	4.9%
South Korea	5.6%	10.5%	4.9%
Chile	7.7%	12.2%	4.5%
Argentina	39.8%	44.4%	4.6%
Malaysia	6.4%	10.0%	3.7%
China	5.6%	8.8%	3.2%
Mexico	10.5%	12.8%	2.4%
Hungary	9.4%	11.4%	2.0%
South Africa	13.2%	14.4%	1.1%
India	13.4%	12.5%	-0.9%

 # Percentage of stocks outperforming gold, excluding adjustments for mergers and acquisitions.
Note: Change in market cap is considered for stock's outperformance. Indices portfolio taken from Bloomberg.

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Source: Bloomberg, DSP. Data as on Jan 2025. All Market returns are TRI using TRA Function on BBG. *Data since 31-12-1999

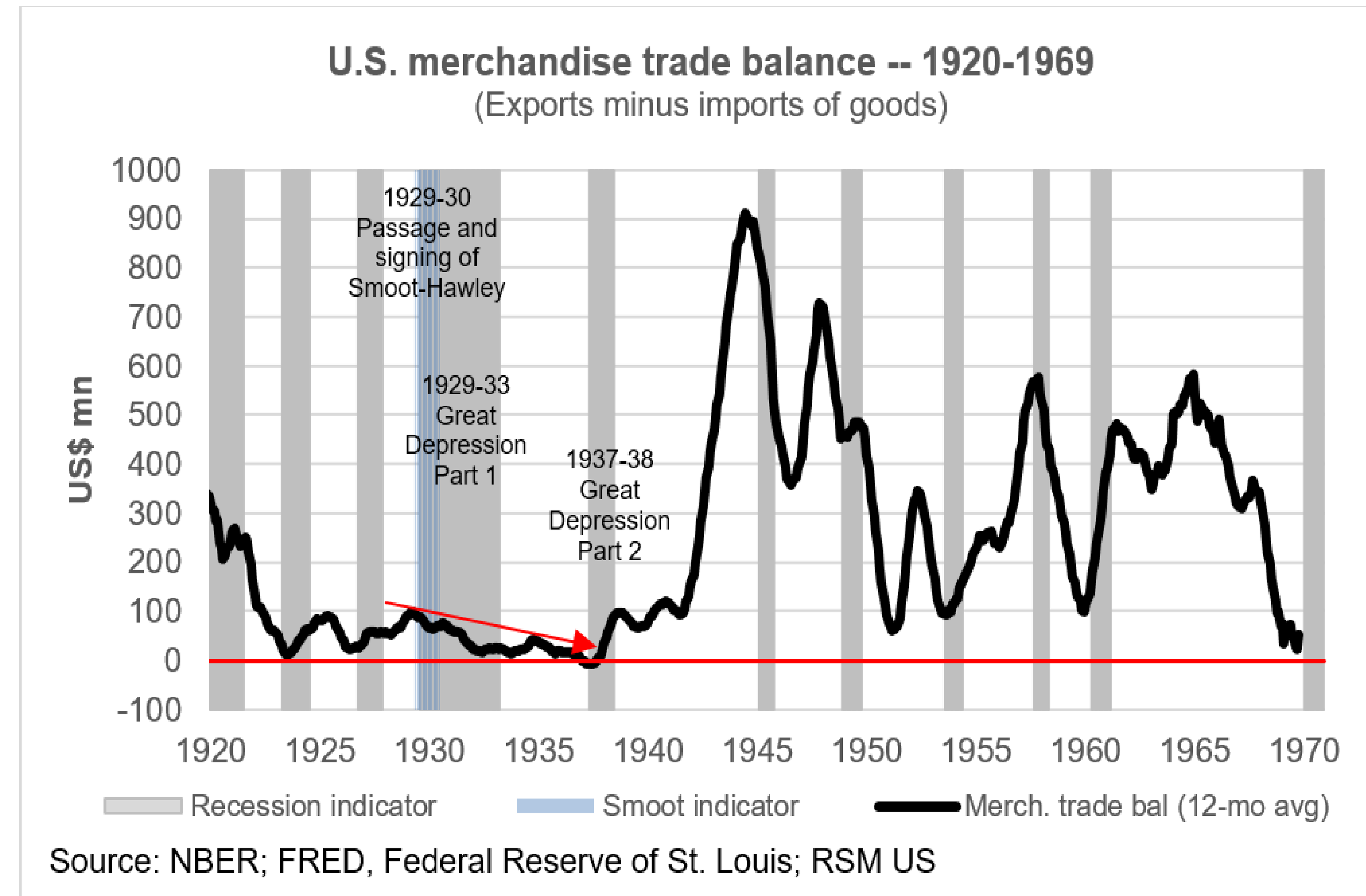
The Smoot-Hawley Tariff Act: When Protectionism Backfired

The Smoot-Hawley Act of 1930 was a U.S. law that raised tariffs on 20,000 imported goods to protect American farmers and industries during the Great Depression. It aimed to make foreign products more expensive to encourage domestic consumption in US.

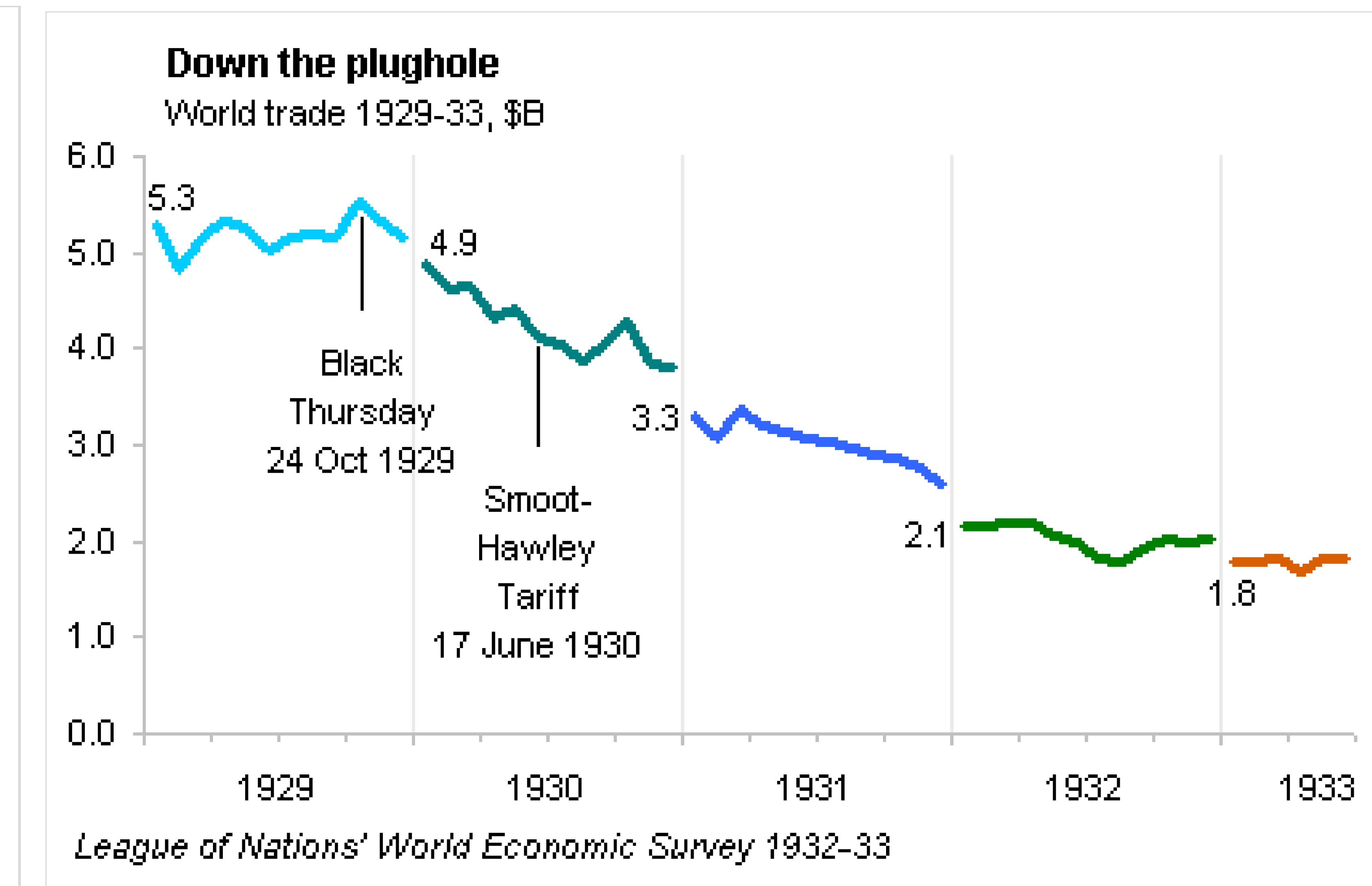
It was signed into law on June 17, 1930, by President Herbert Hoover. However, instead of reviving the U.S. economy, it triggered a global trade war. Many countries retaliated by imposing their own tariffs on American exports, leading to a sharp decline in international trade. Major economies like Canada, Britain, France, and Germany imposed counter-tariffs, worsening the economic downturn worldwide. The act may have contributed to the Great Depression, as global trade collapsed by over 60% between 1929 and 1934. U.S. agricultural and industrial exports suffered, and unemployment surged.

Trade wars, like those sparked by Smoot-Hawley, are dangerous because they reduce economic efficiency, disrupt global supply chains, and increase consumer prices. They often escalate, causing economic slowdowns and worsening diplomatic relations, making economic recovery harder.

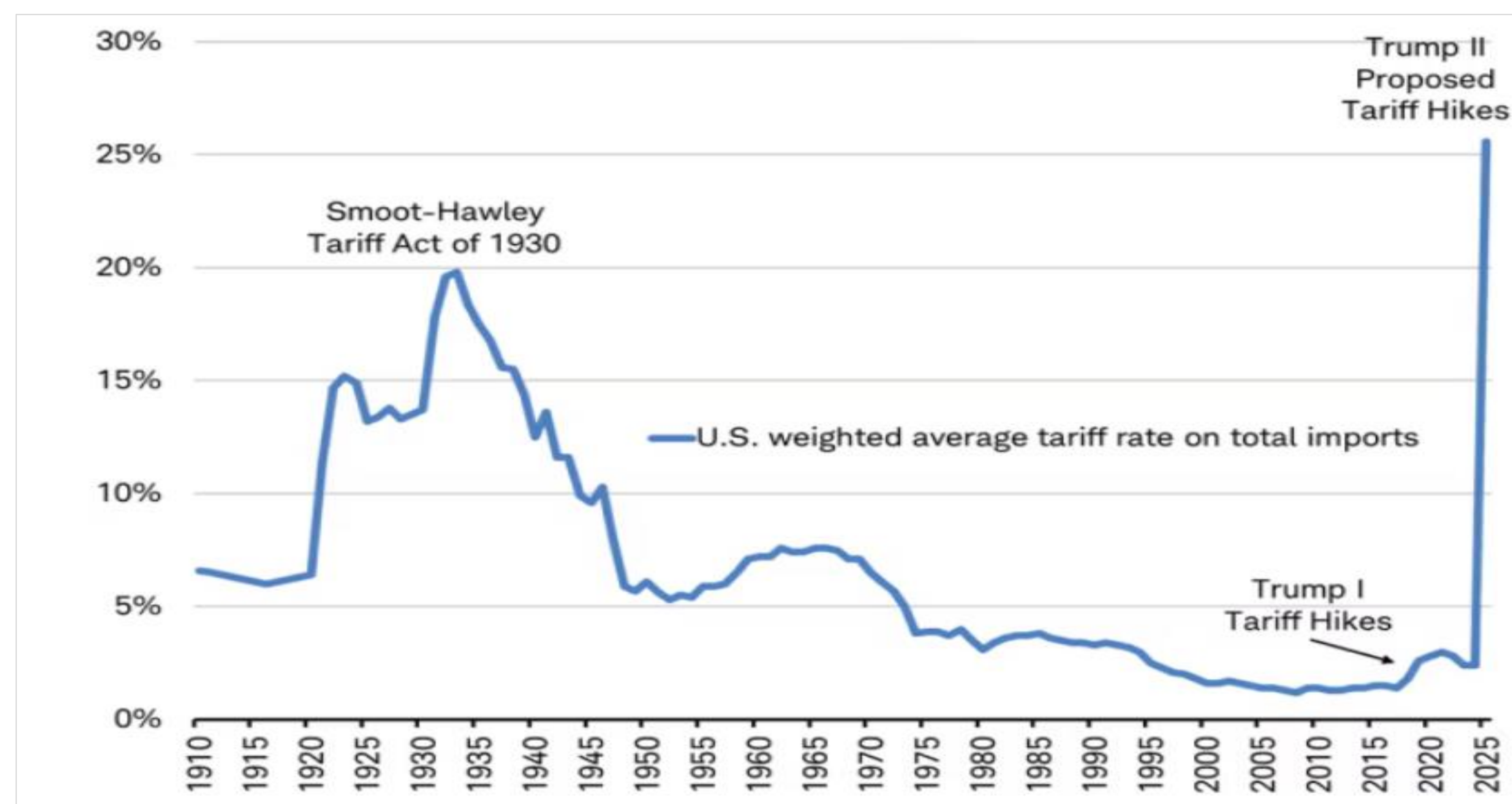
US International Trade Worsened Due To Trade War



World Trade Plunged Due To Great Depression & Trade War



US Weighted Average Tariffs On Imports May Hit A Record



Trade Wars Aren't New

Tariff Legislation	Average Ad Valorem Equivalent
Act of 1913	21.08
Act of 1922	34.61
Act of 1930	42.48

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Source: NBER, FRED, The Economist, USITC, DSP (Graphs taken from reports from various agencies)

Cautious Signs for U.S. Equities

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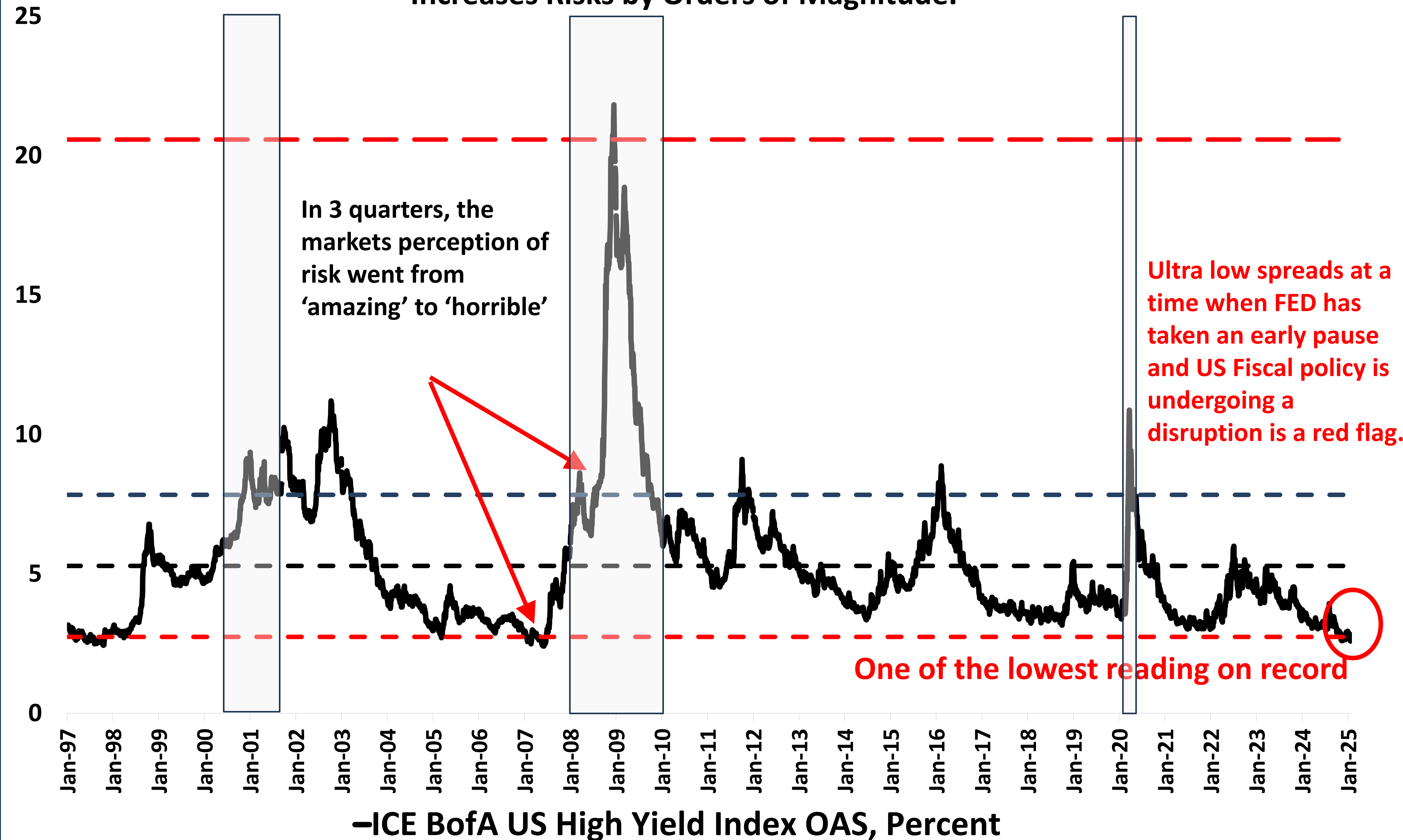
Junk Bond Yield Indicates Unprecedented Complacency in U.S. Credit Markets

The ICE BofA U.S. High Yield Index represents the performance of U.S. dollar-denominated, below-investment-grade corporate debt publicly issued in the U.S. domestic market. These bonds are also colloquially called "junk bonds."

The ICE BofA Option-Adjusted Spreads (OASs) measure the calculated spreads between a computed OAS index of all bonds in a given rating category and a spot Treasury curve. The lower the spread, the "easier" credit conditions are. When markets become apprehensive about the solvency of the underlying firms, the spreads jump. These jumps often coincide with broader economic turmoil because the index represents a collection of many firms.

Currently, yield spreads are close to an all-time low. This indicates that markets are extremely confident in lending to below-investment-grade firms and are comfortable accepting only 2.7% higher yields than Treasury securities. The risks associated with such low spreads are non-linear, meaning that as yields drop further, complacency—or risk assessment—declines at an accelerating rate. History shows that periods of low volatility are often followed by high volatility and, at times, financial accidents.



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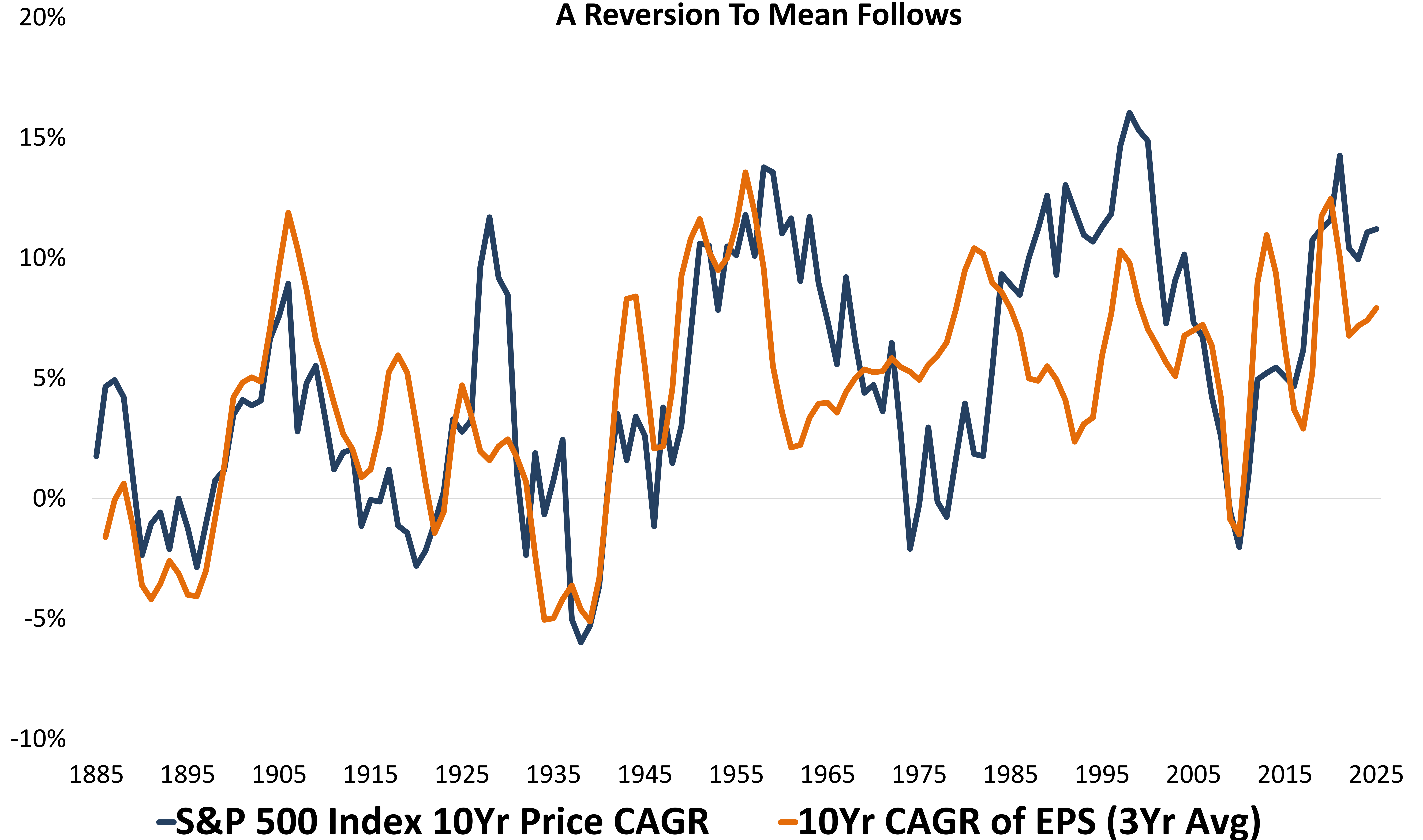
Source: FRED; DSP Data as on Jan 2025

US Stocks Have Rallied Ahead Of The Earnings, Reversion To Mean Ahead?

U.S. stocks have outperformed all other markets globally. In fact, the U.S. now accounts for more than two-thirds of the world's equity market capitalization. Historical data for the S&P 500 Index and its earnings per share (EPS), going back to 1871, reveals a fundamental rule of stock prices: over the long term, stock prices follow earnings. However, market sentiment, investor behavior, and other factors can cause stocks to outperform or underperform underlying earnings trends. During periods of exuberance, stock prices rally harder and rise beyond earnings growth. This leads to an expansion in the price-to-earnings (P/E) ratio. For instance, the S&P 500 Index currently trades at a trailing twelve-month (TTM) P/E ratio of 24x, compared to its long-term (1871–2025) average of 16x.This hasn't happened without reason. Over the last 10 years, S&P 500 EPS has grown at a compound annual growth rate (CAGR) of 10%. However, stock price growth has outpaced earnings growth by 1.5 percentage points. This means U.S. stocks are now pricey and heavily dependent on the continuation of double-digit earnings growth.



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Source: Bloomberg; Data as on Jan 2025

India’s Economic Growth Check

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Growing At 8% Isn't Easy

For India to reach a $30 trillion GDP (assuming a stable US Dollar to Rupee exchange rate), it will take 25 years at a growth rate of 8.5% CAGR.

Why is the 8.5% rate up for discussion?
At the RBI's inflation target of 4%, with an 8.5% real GDP growth, nominal growth would be close to 12.5% CAGR. Indian corporate earnings grow slightly slower than long-term nominal GDP growth. Hence, corporate earnings may grow at or below 12.5% under the best-case scenario (since this doesn't hold true in most countries). How easy is it to grow at 8.5% YoY?

The table on the right shows that India hasn't seen two consecutive years of 8% GDP growth since 1971. As the size of the GDP increases, growing at a faster rate will become even more challenging. In fact, except for China, no other country has ever grown at an 8.6% CAGR for 25 years.
Hence, dial down growth, earnings, and, therefore, returns expectations.

This Is How Often India Has Grown at 8% YoY GDP Growth

FY71	5.2	FY81	6.7	FY91	5.5	FY01	3.8	FY11	8.5	FY21	-5.8
FY72	1.6	FY82	6.0	FY92	1.1	FY02	4.8	FY12	5.2	FY22	9.7
FY73	-0.6	FY83	3.5	FY93	5.5	FY03	3.8	FY13	5.5	FY23	7.0
FY74	3.3	FY84	7.3	FY94	4.8	FY04	7.9	FY14	6.4	FY24	8.2
FY75	1.2	FY85	3.8	FY95	6.7	FY05	7.9	FY15	7.4	FY25e	6.4
FY76	9.2	FY86	5.3	FY96	7.6	FY06	7.9	FY16	8.0		
FY77	1.7	FY87	4.8	FY97	7.6	FY07	8.1	FY17	8.3		
FY78	7.3	FY88	4.0	FY98	4.1	FY08	7.7	FY18	6.8		
FY79	5.7	FY89	9.6	FY99	6.2	FY09	3.1	FY19	6.5		
FY80	-5.2	FY90	6.0	FY00	8.9	FY10	7.9	FY20	3.9		

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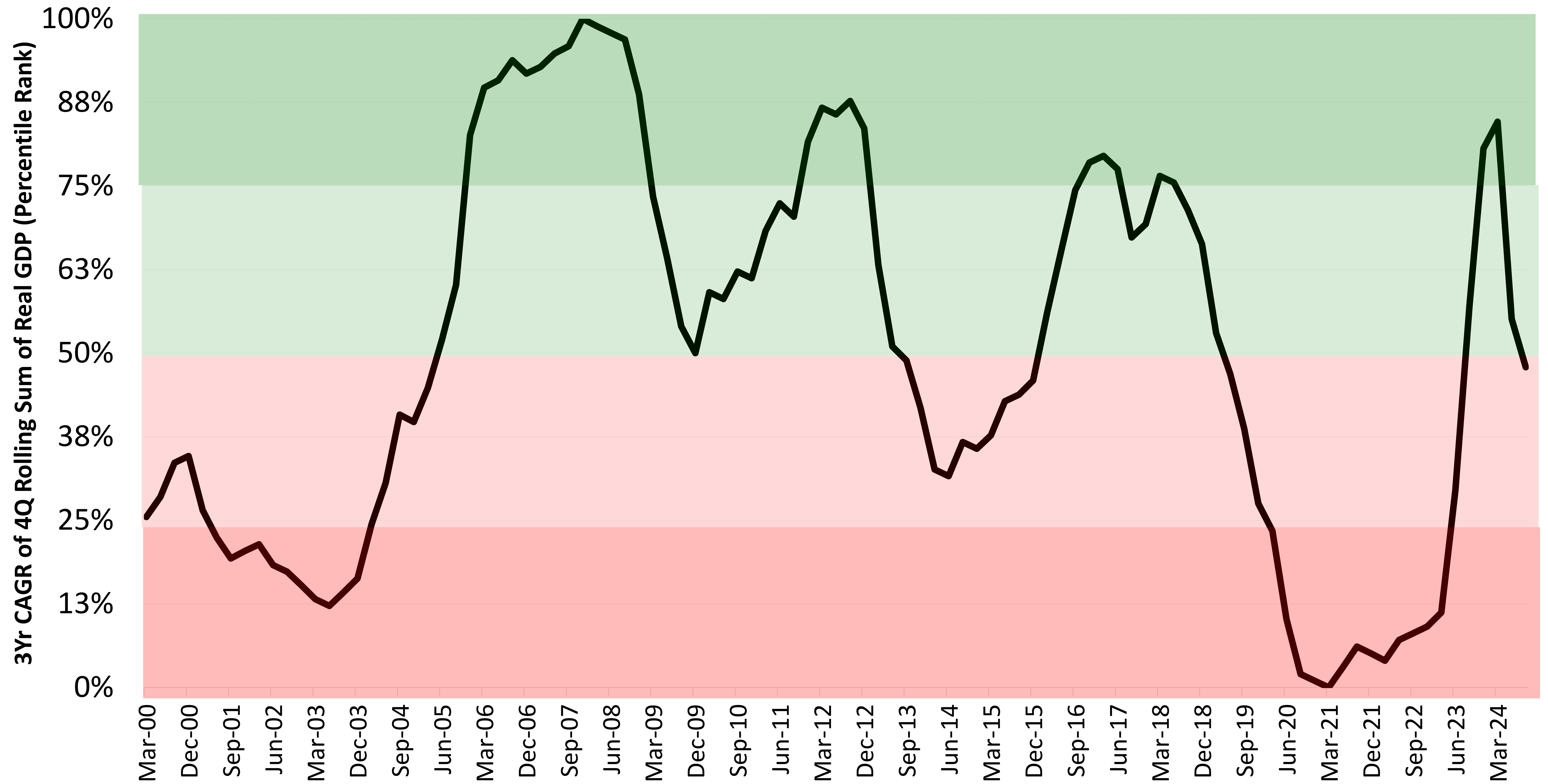
Source: Bloomberg; Data as on Jan 2025

Where Are We In The Growth Cycle?

The Indian economy has seen a steady revival from the deep contraction during the pandemic. Growth has recovered to reach the 86th percentile rank compared to its own history, indicating that the economic rebound has gained momentum. High growth rates are not sustainable. The growth trajectory has returned to its normal average pace of around 6% to 6.5%. Whether this growth rate is sufficient or not is debatable. Whether India can grow faster, or needs to grow faster, is also debatable, although the data on the previous slide highlights how difficult it is to grow at a faster pace.

What's not debatable is that investors would either want a higher growth rate or would need to expect corporate earnings to outpace GDP growth continuously. This is possible, but not easy. The dynamics of sales growth, profit growth, and the role of margins will be critical in gauging this trend.



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Source: CMIE; Data as on Jan 2025

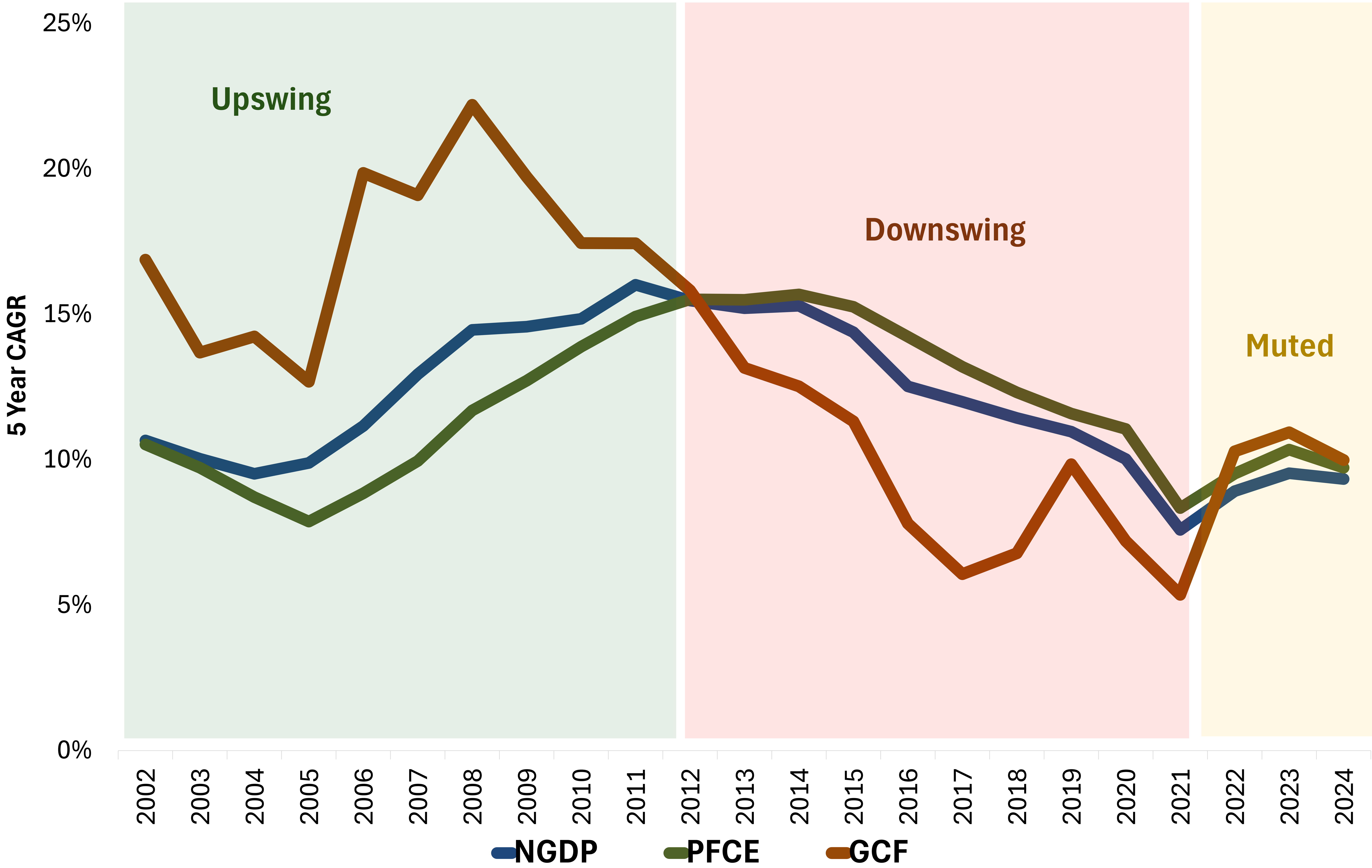
The ‘Cycle’ Is Missing

One of the reasons for GDP growth’s inability to stick to higher rates is the absence of cyclicality or a clear leader for this cycle.

In economic growth cycles, the faster phase of growth is usually dominated by either private final consumption expenditure or gross capital formation. As the chart on the right shows, in the 2002 to 2011 cycle, gross capital formation outpaced growth in private consumption and nominal GDP.

In the current cycle, since the depth of the pandemic, there has been a ‘cycle-less’ recovery, with both private consumption and investment growth similar to nominal GDP growth.

This makes the outlook for demand uncertain and dampens private business sentiment. This uncertainty can weaken private businesses' commitment to higher incremental capex. At a time when the government’s ability to spend is limited (we already have a 4.5% to 5% fiscal deficit), the growth spurt needs a new engine.



Source: Nuvama Research, CMIE, DSP. Data as on Jan 2025

NGDP- Nominal GDP, PFCE- Private Final Consumption Expenditure, GCF- Gross Capital Formation

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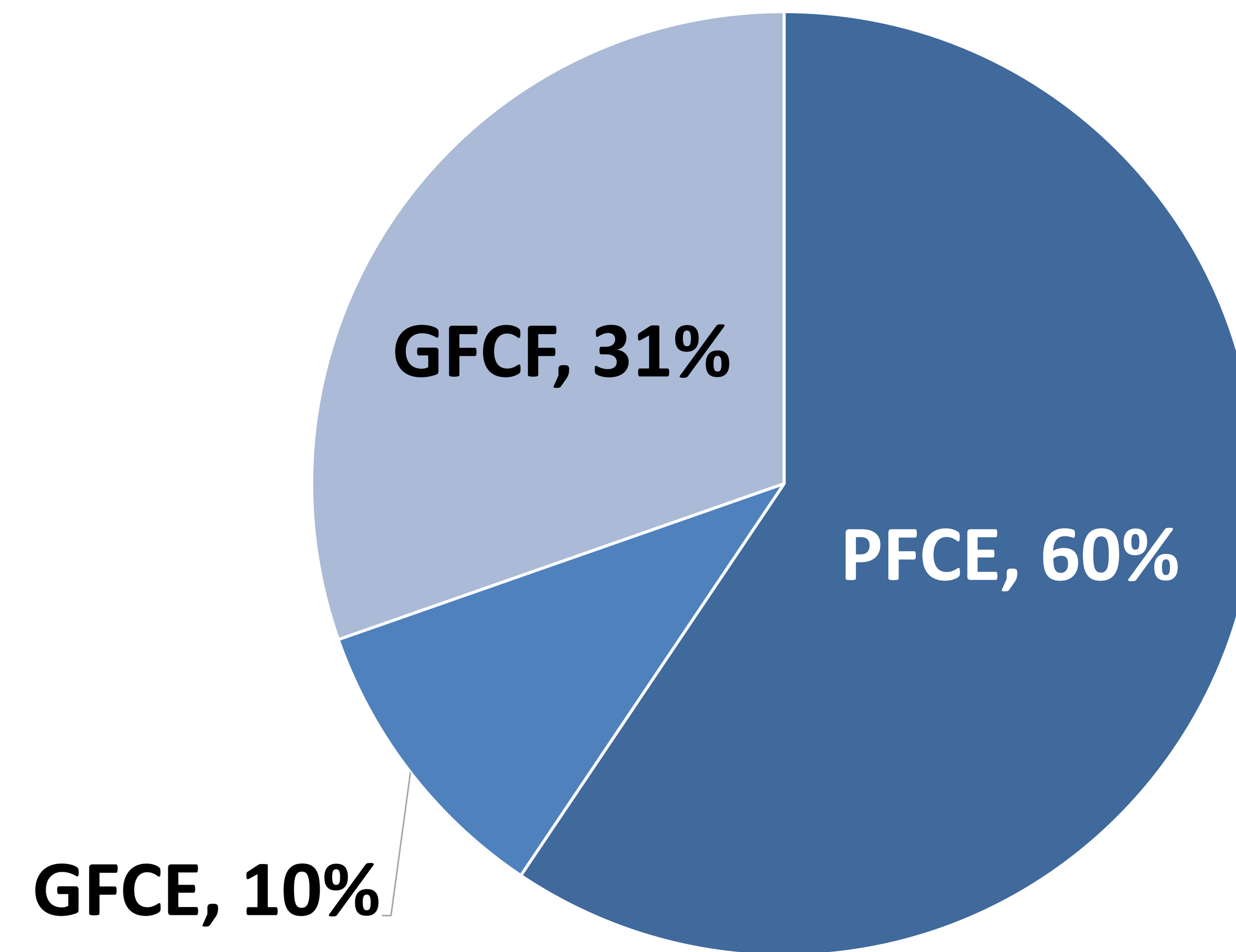
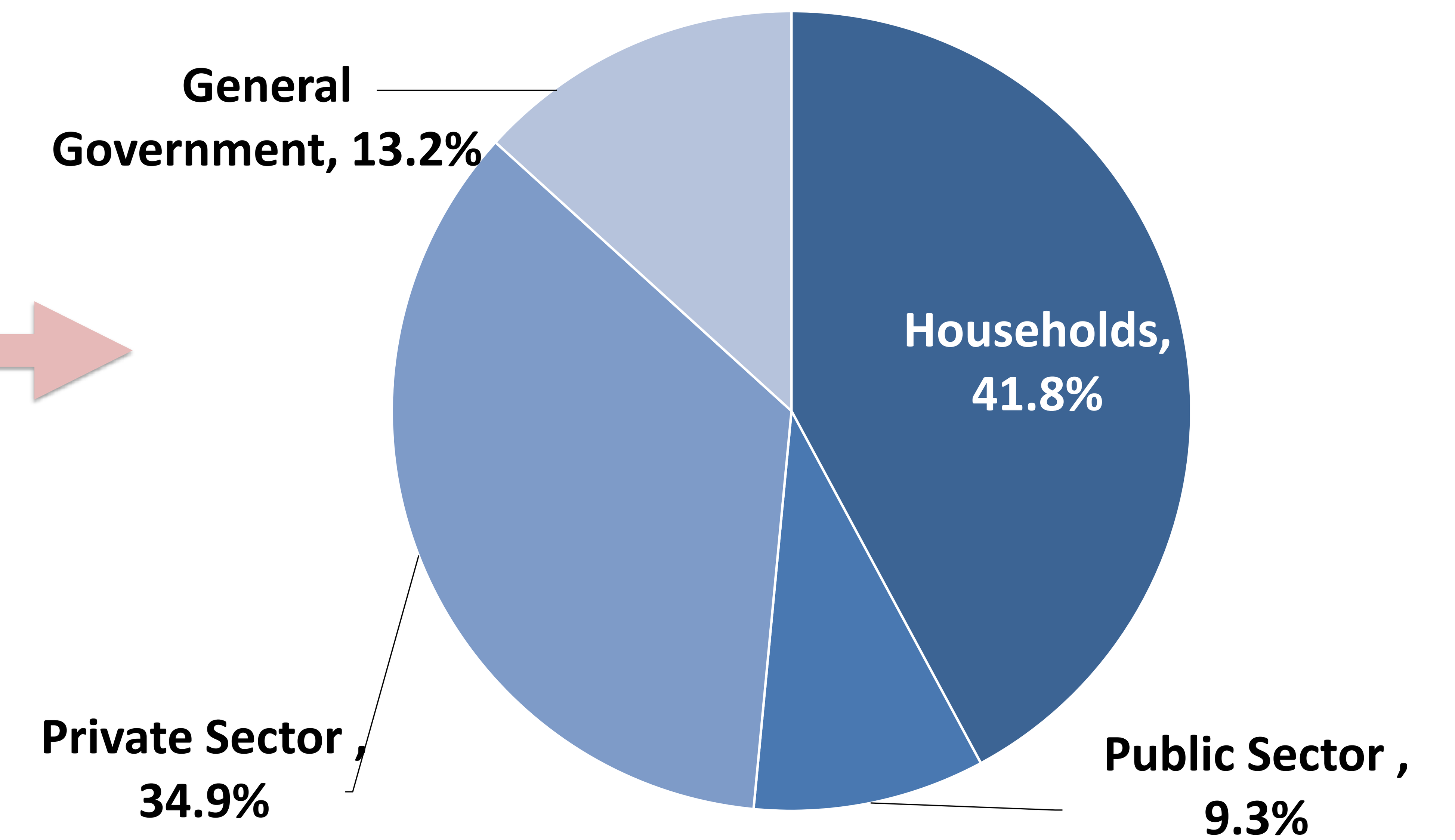
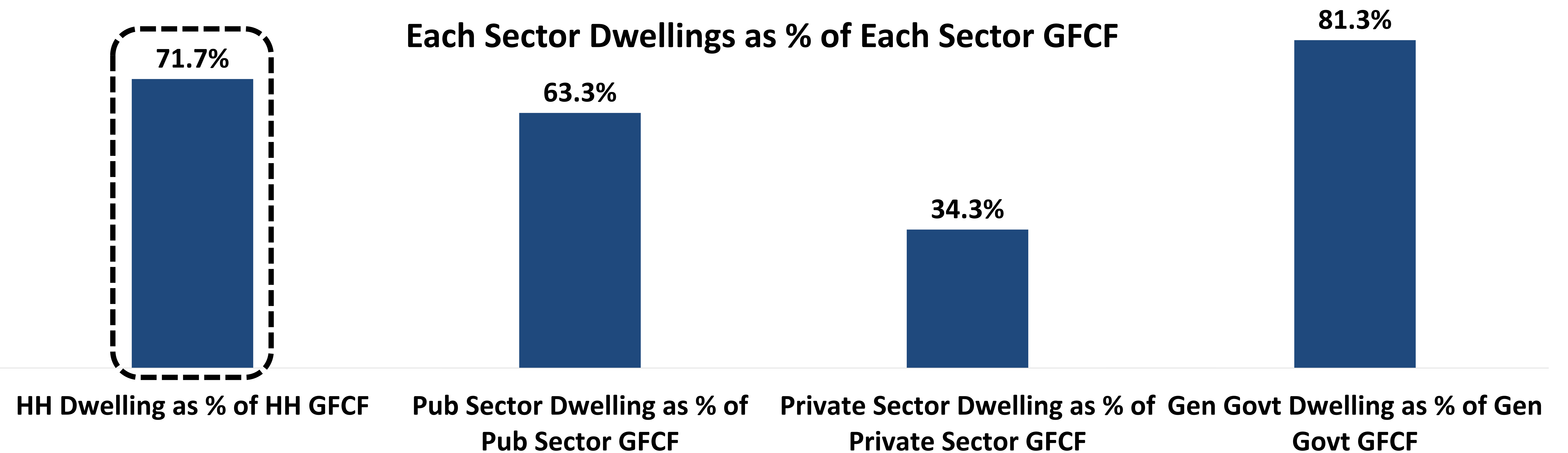
Home Construction Is A Major Economic Driver

In FY25, India's GFCF (Gross Fixed Capital Formation) will be close to Rs. 98 to Rs. 100 trillion. Of this, nearly 40% comes from households, with dwellings (or home) construction accounting for more than 70%. This means that, in the best years, home construction by households can account for nearly a third of all investments in India. This is equivalent to more than 10% of our GDP—a sizeable number, given that the ancillary effects of home construction can be enormous.

At the peak of the previous cycle, in 2011, one-third of investments were a result of home construction and improvement in India. For the Indian economy to do well, this number could be a significant source of strength. Post-pandemic, the trend in this number, as measured by home sales and declining inventory, is encouraging. However, there is a major disconnect or lack of understanding (on our part) as to what is driving this trend.







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Source: CMIE, DSP; Data as of Jan 2025

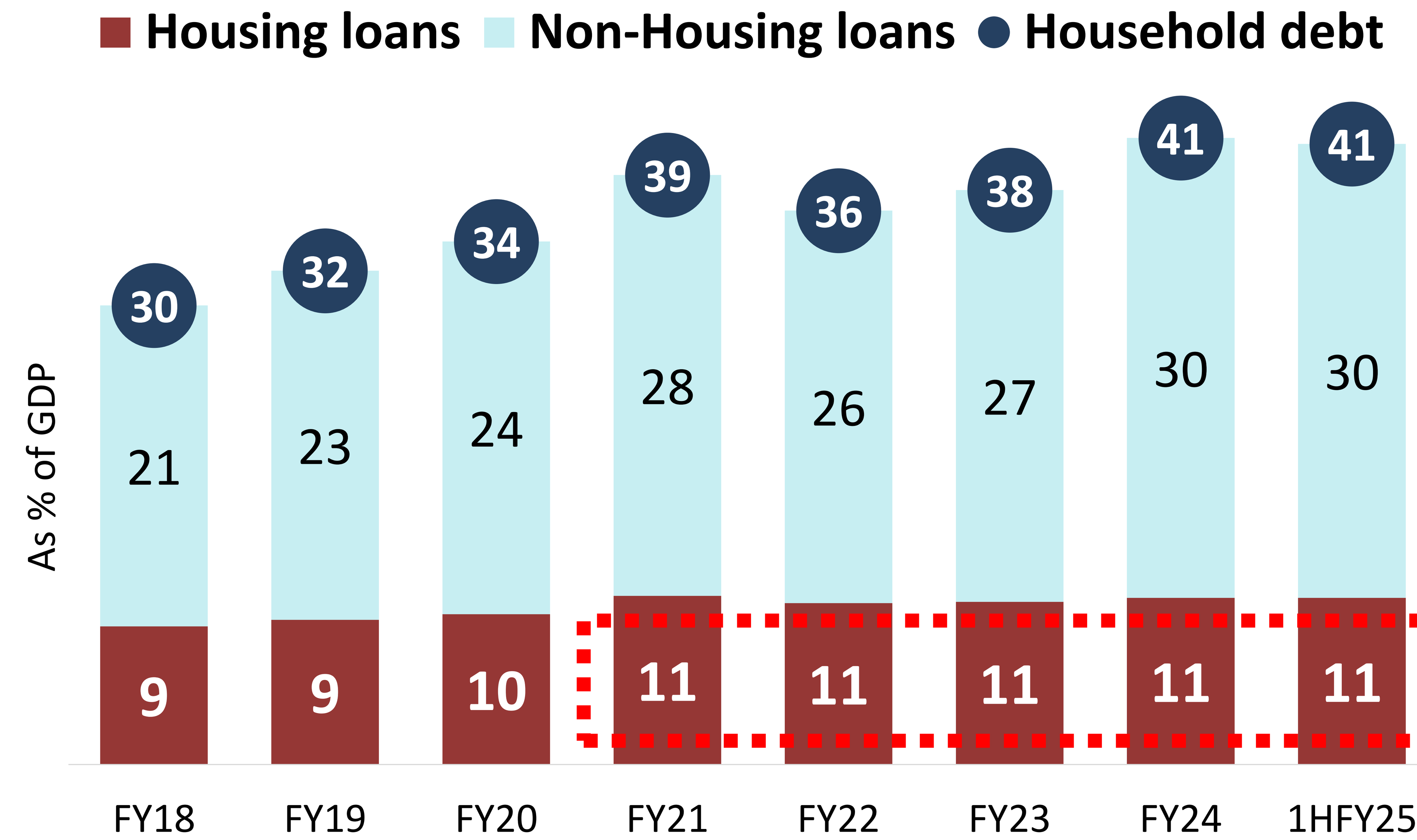
HH- Household, GFCE- Government Final Consumption Expenditure, GFCF- Gross Fixed Capital Formation

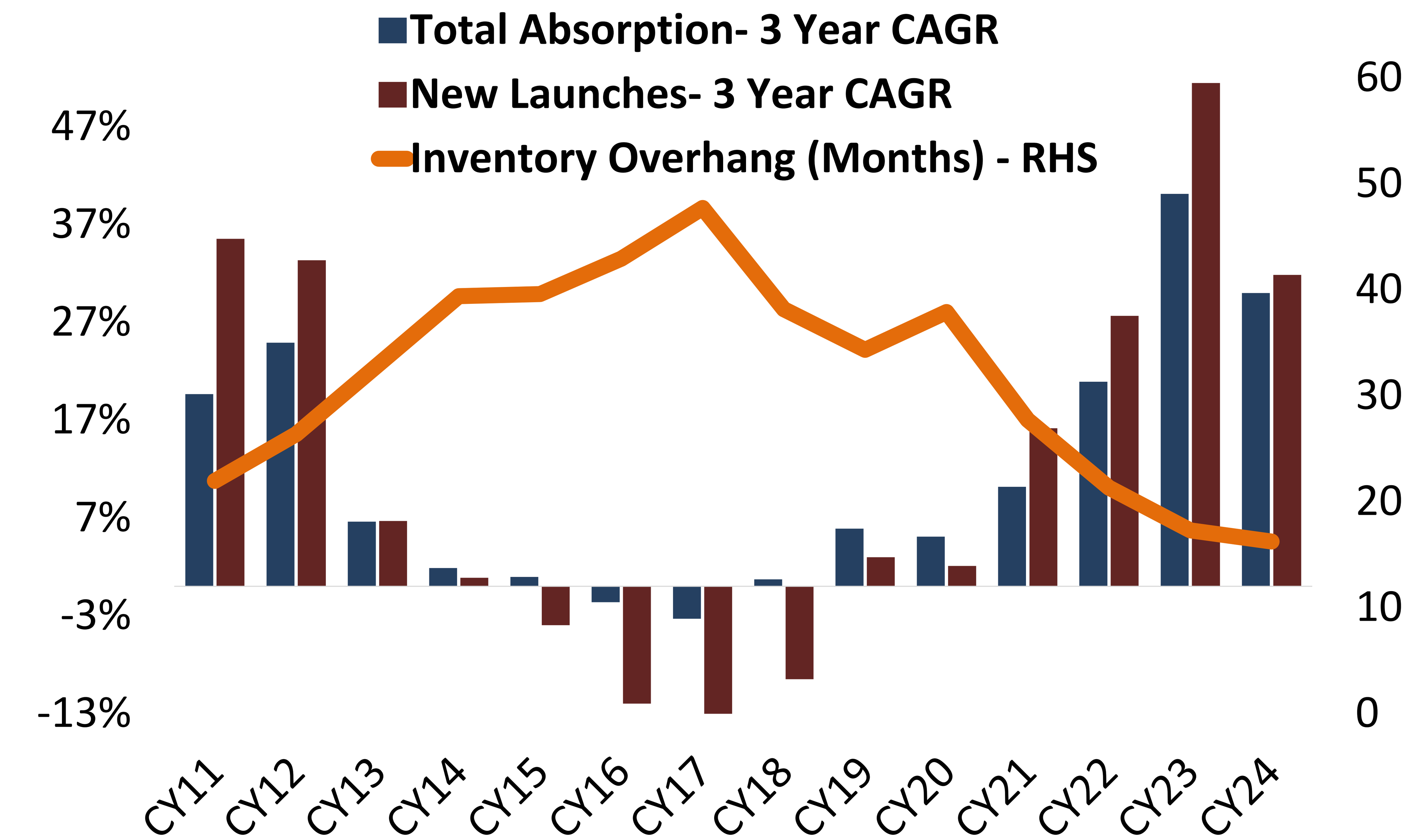
Can A Stock Market Decline Sour The Housing Sector?

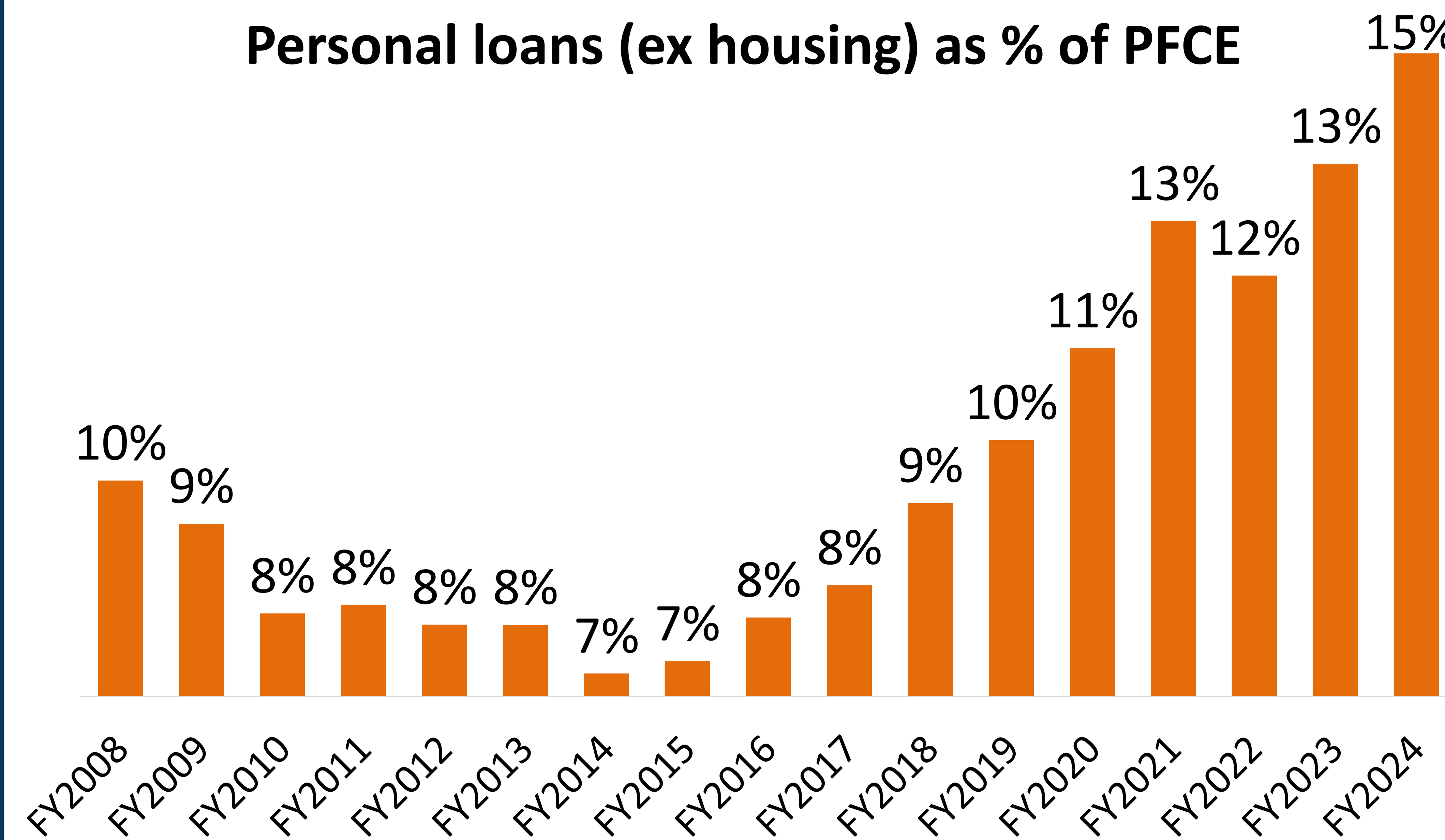
Is the stock market the key driver of housing sales in this cycle?

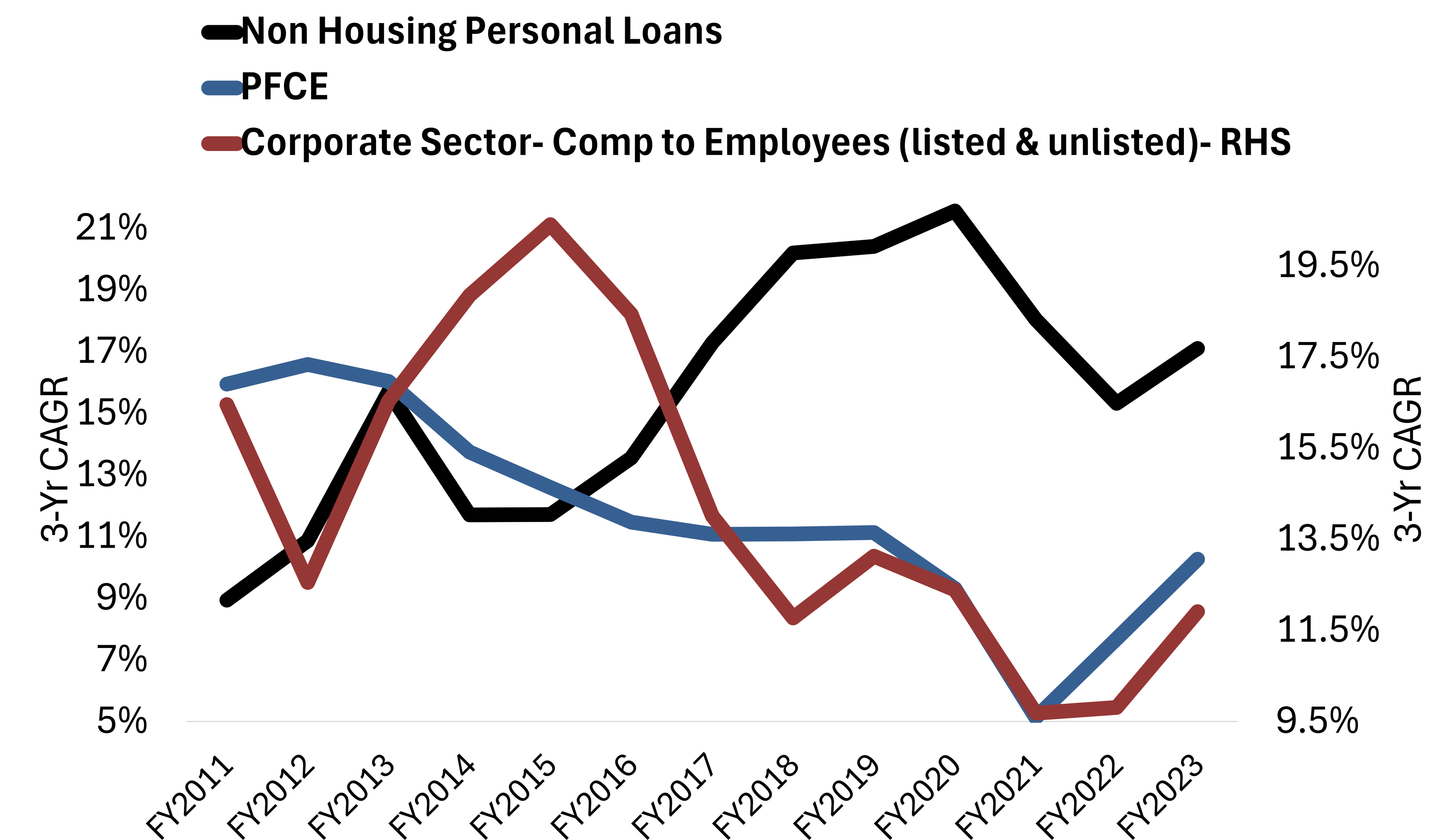
"There is no hard data establishing that funds from unsecured loans are significantly entering the stock market, but anecdotal indications suggest this could be happening... We are very watchful of that segment. Estimating the exact amount is very difficult." – RBI Governor, Nov 2024

The post-pandemic economic revival has seen a steady improvement in housing sales in India. However, at the same time, the housing loans component has failed to rise. A large part of transactions, anecdotally, is being done without the use of credit. There is no commensurate rise in incomes to account for this increase in housing sales. This opens the possibility of profits from stock markets being funneled into real estate, particularly housing. A large decline in stock markets could also put this sector under stress, which is a significant driver of India's growth. This is a fragile node and needs monitoring.









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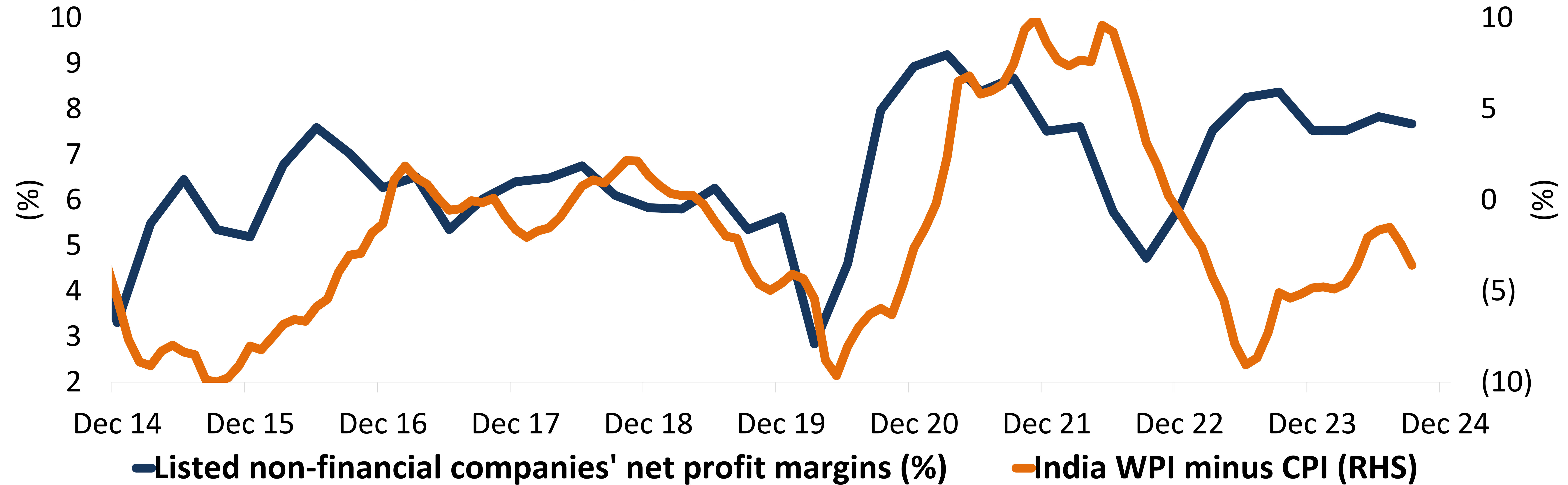
Source: Motilal Oswal Financial Services, Nuvama Research, CMIE, DSP. Data as on Jan 2025
PFCE- Private Final Consumption Expenditure

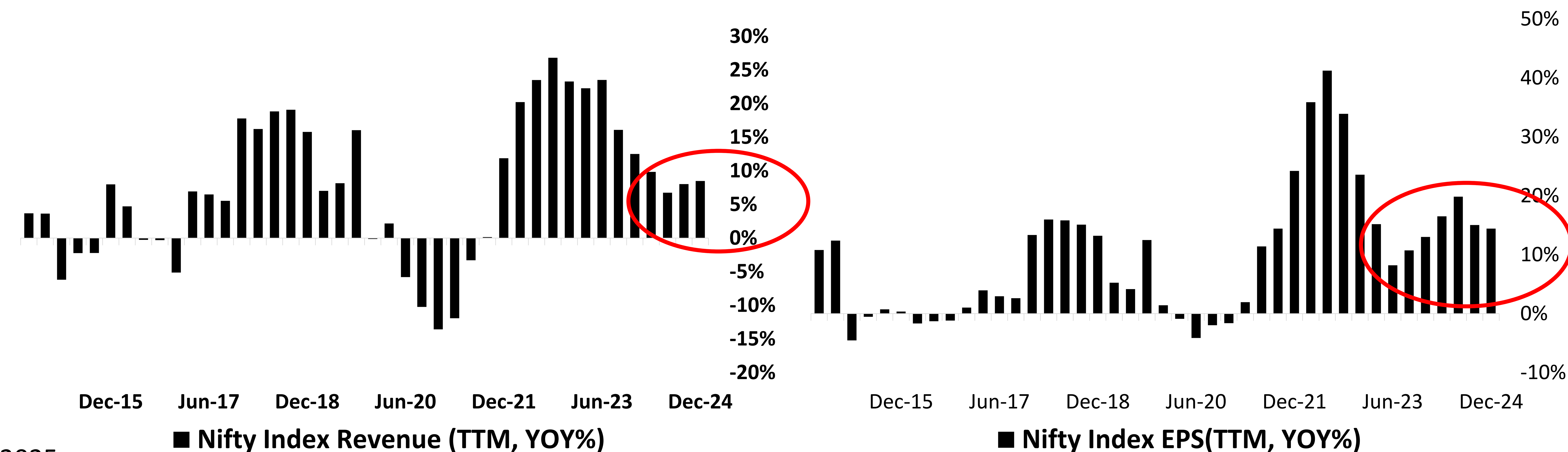
Margins Can Drag Earnings Growth

Revenue growth has slowed to single digits. Margins are peaking at one of the highest levels and beginning to decline.

Consumption demand and high-frequency indicators are sluggish or decelerating, signaling cyclical headwinds for domestic earnings. The global exports cycle is weak, with tepid growth due to a patchy global environment.

The result: Earnings visibility is suffering, and the likelihood of slower profit growth continues to remain high. Meanwhile, stock prices have seen some decline, but valuations remain above long-term median levels. For the Small and Midcap universe, valuations are still higher than the previous major valuation and price peaks. This suggests that caution is warranted, especially in the SMID space. The largest-cap stocks may hit the valuation comfort zone the earliest.





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Source: Bloomberg; Data as on Jan 2025
WPI- Wholesale Price Index, CPI- Consumer Price Index

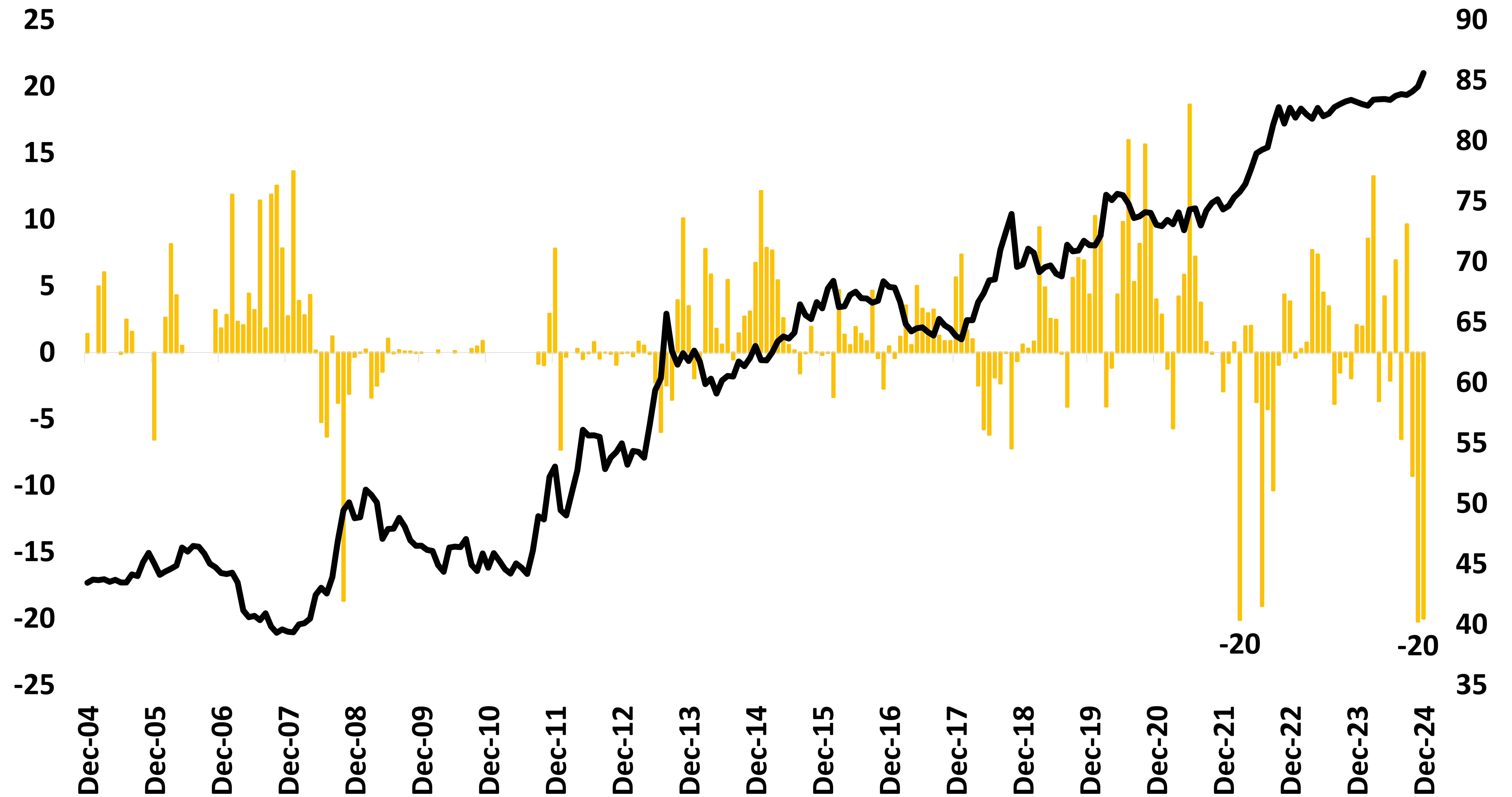
Rupee Exits Its Own 'Unsettling Calm' Phase

From October 2022 to the beginning of October 2024, the Indian Rupee depreciated by only 0.6% annually. In fact, for a year and a half, USDINR barely budged a percent around the 83 mark, recording one of the most non-volatile periods of the 21st century.

The absence of FDI inflows, large sales by FPIs in equity markets, and a patchy trade balance coincided with a stronger US Dollar. The RBI ended up selling nearly $50 billion in the last three months of 2024 to stem the fall in the Rupee.

The Indian Rupee remains overvalued and prone to weakness if the US Dollar were to strengthen globally. This is one factor that will keep foreign investment flows tentative.

The Indian Rupee is a key monitorable for the next few months.



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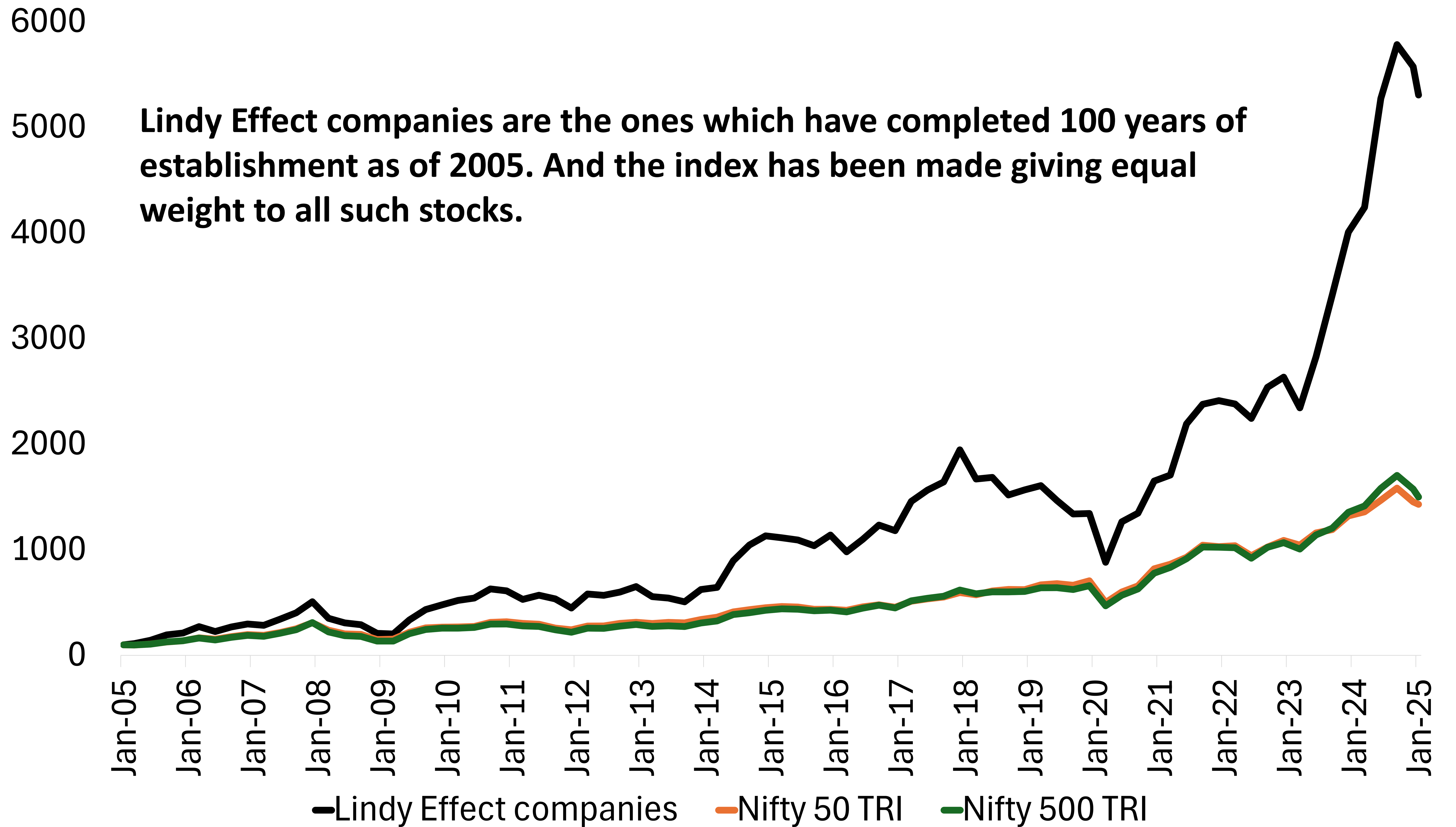
Source: Bloomberg; Data as on Jan 2025

Why the Oldest Ideas Outlive the Newest Trends

Lindy Effect is a statistical tendency for things with longer pasts behind them to have longer futures ahead.

“If a book has been in print for forty years, I can expect it to be in print for another forty years. But and that is the main difference, if it survives another decade, then it will be expected to be in print another fifty years. This, simply, as a rule, tells you why things that have been around for a long time are not "aging" like persons, but "aging" in reverse. Every year that passes without extinction doubles the additional life expectancy. This is an indicator of some robustness. The robustness of an item is proportional to its life.” – Nassim Nicholas Taleb (Book: Antifragile: Things That Gain from Disorder)



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Source: DSP, Bloomberg.

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