International Journal of Engineering Technology Science and Research
IJETSR
www.ijetsr.com
ISSN 2394 – 3386
Volume 4, Issue 10
October 2017

Value Vs Growth - The intelligence of Investing in Capital Market

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Abstract

Investors inevitably face a fundamental question: Do you believe more in value stocks or in growth stocks?The concepts of "value" and "growth" investing have a long history in financial economics. This paper focuses on the link between the Value and Growth investments in the Capital Marketin terms of a simple theoretical and empirical literature framework. Researchers hold diverse opinions regarding the importance of stock markets playing a significant role in economic growth processes. Growth versus value is one of the oldest investment styles known. The evidence suggests that, taking into account the experience of past ten years, growth investing generates superior returns. Common measures of risk do not support the argument that the return differential is a result of the higher riskiness of growth stocks. Over the past Ten years, growth stocks have outperformed value stocks six times and value stocks have outperformed growth stocks four times. .

Keywords: Investment, Value Investing, Growth Investing, Capital Market, Indian Economy

Introduction

Value is often discussed in contrast with growth, but sometimes the lines between the two approaches become quite fuzzy in practice. The best way to define value investing is to contrast it to growth investing. The value investor is looking for a company with sound fundamentals that may trade below its "intrinsic value" for some reasons. The market should eventually correct its inaccurate valuation and send stock prices sharply upward when that correction occurs. The value stocks are characterized by low multiples and high payout ratios and strong yields.

Value-buying stocks that are under-priced, according to some fundamental metric, such as price-to-book ratio, gained fame under Ben Graham and David Dodd, whose 1934 text "Security Analysis" is generally viewed as the bible of value investing, even though they never explicitly used the phrase "value investing."

Growth investors tend to focus more on the company's value as an ongoing concern. Factors like the quality of the management, industry growth prospects, the company's positioning in the industry, operations in a niche area, favorable demographics, increasing affluence, the domestic construction growth and the outsourcing story are major drivers of growth stocks. The stocks that are bought by growth investors often appear expensive at first glance but such stocks must be looked at from a future perspective. Growth stocks are characterized by high multiples, low payout ratios and low yields.

Investors who buy stocks typically do so for one of two reasons: they believe that the price will rise and allow them to sell the stock at a profit, or they intend to collect the dividends paid on the stock as investment income. Of course, some stocks can satisfy both objectives at least to some extent, but most stocks can be classified into one of three categories: growth, income and value. Those who understand the characteristics of each type of stock can use this knowledge to grow their portfolios more efficiently.

A number of philosophies and strategies guide how investors view the purchase of shares in a company. The two schools of thought most investors abide by are growth and value.

In general, value investors concern themselves with buying stocks deemed "cheap" with respect to their earnings or net assets while growth investors place more weighting on a company's prospects for strong future earnings growth. The primary risk for growth investors is that the expected earnings growth, which was used to justify a premium valuation, does not come to fruition. In these instances, investors often suffer from both the reduced earnings power and from valuation multiple contractions. Conversely, the primary risk to a value-oriented strategy is that the investor purchases companies that trade at low valuations for very good reasons and are poised to become even more "cheap." This of course is why it is important to make a concerted effort to understand the financial soundness of a company and its competitive position within its industry. Value investors generally believe they are much better equipped to assess these elements than they are to forecast the earnings of a company many years into the future and then discount those earnings back to the present at an appropriate rate of interest.

Value investors attempt to put the odds of success in their favor by focusing on the underlying business and demanding an appropriate margin of safety. The margin of safety required should not be static, but rather it should be dependent upon the idiosyncratic risk and return profile of each subject company and how those risks interplay with the risk profile of an overall portfolio. For instance, an investor should demand a larger margin of safety for a micro-cap company with more than a trivial amount of financial leverage than he or she should reasonably expect to receive when taking a position in a regulated utility.

Year	Growth Stocks	Value Stocks
2007	10.97% ✓	1.84%
2008	-37.49%	-36.62% ✓
2009	36.88% ✓	16.98%
2010	15.02%	16.56% ✓
2011	-0.66%	3.74% ✓
2012	16.9% ✓	14.56%
2013	34.97% ✓	30.24%
2014	13.95% ✓	13%
2015	3.54% ✓	-0.79%
2016	8.97%	15.44% ✓

Simply put, growth investors seek out stocks with above-average growth potential, with little regard to the current share price. Value investors, on the other hand, look to buy stocks trading at a discount or well below what is believed to be the actual value of the shares. Though objective experts believe neither philosophy is better than the other, each school of thought has its own legion of staunch, single-minded supporters.

Relevant literature

The topic of value and growth investing offers a shining example of the fruitful exchange of ideas between academic research and investment practice. The explosion of academic interest in value and growth investment strategies can be traced back to Fama and French (1992), and Lakonishok, Shleifer and Vishny (1994). The results of Fama and French delivered a stunning blow to the explanatory power of the Capital Asset Pricing Model, and sparked debates about the “death of beta.” In the wake of this study, academics shifted their attention to the ratio of book-to-market value of equity, and firm size as the leading explanatory variables for the cross-section of average stock returns. In turn, this work built on earlier studies of stock market “anomalies.” Basu (1977), for example, showed that stocks with low price-to-earnings ratios subsequently tend to have higher average returns than stocks with high ratios. Chan, Hamao and Lakonishok (1991) study Japanese data and find strong support for the superior performance of value investment strategies.

Value investing was first developed in the 1930s by Graham and Dodd (1934). In the early 20thcentury, investors were guided mostly by speculation and insider information. Graham believed, however, that the true value of a stock could be determined through research

Yet another explanation for the returns to value investing rests on methodological issues of data selection bias (see Kothari, Shanken and Sloan (1995)). A careful study by Chan, Jegadeesh and Lakonishok (1995), however, suggests that any such bias cannot explain the differential performance of value and growth investing. Levine and Zervos (1996) examine whether or not there was a strong empirical relationship between stock market development and long-run economic growth. They found a strong correlation between overall stock market development and long-run economic growth. Demiurgic-Kunt and Levine (1996) found that different measures of stock exchange size are strongly correlated to other indicators of activity levels of financial, Banking, Nonbanking institutions as well as to insurance companies and pension funds.

The academic work on value investing has had a strong impact on professional investment management. Value and growth are now widely recognized distinctive specializations adopted by money managers. Additionally, the research studies have been instrumental in the development of style-specific benchmarks which have proliferated in performance evaluation and attribution analysis. Many such benchmarks are based on a variable that has been extensively used in academic studies, namely the ratio of book to market value of equity, and this has become an important indicator of a portfolio’s orientation toward either growth or value.

Ekundayo (2002) argues that a nation requires a lot of local and foreign investments to attain sustainable economic growth and development. The capital market provides a means through which this is made possible.Osaze (2000) sees the capital market as the driver of any economy to growth and development because it is essential for the long-term growth capital formation. It is crucial in the mobilization of savings and channelling of such savings to profitable self-liquidating investment.

Of late there was a growing concern on the role of stock market in economic growth, Levine and Sara (1996); Demirguc-Kunt and Roos (1996); Oyejide (1994); Nyong (1997); Obadan (1998); Onosode (1998); Emenuga (1998); Osinubi (1998), The stock market is the focus of economists and policy makers because of the perceived benefit it provides for the economy.

Most importantly from the perspective of academic research, one of the most debated issues in the past several decades is the deferential returns of investments in value versus growth stock portfolios the value premium debate (e.g., De Bondt and Thaler (1985), Fama and French (1992, 1993, 1996), Lakonishok, Shleifer, and Vishny (1994), and Daniel and Titman (1997))

While the evidence on returns is relatively uncontroversial, the situation is far less settled when it comes to providing an explanation for the differences between the performance of value and growth portfolios. Fama and French (1996) argue that stocks with high ratios of book equity to market value are more prone to financial distress and hence riskier. They employ a version of the Merton (1973) multi-factor asset pricing model to account for value stocks’ higher risk exposures to a financial distress factor, and hence their higher returns. This argument, however, stretches credulity. Lakonishok, Shleifer and Vishny (1994) argue against this “metaphysical” approach to risk, whereby higher average returns on an investment strategy must necessarily reflect some source of risk.

This paper provides an empirical research on value and growth investing. We begin by surveying the evidence on the performance of value investment strategies. The underlying reasons for the performance are more controversial, so we also give an overview of the evidence on various explanations for the returns on value strategies. Finally we provide some updated evidence.

The role of capital markets in stimulating economic progress is less debatable as there are well established theoretical frameworks for aprori expectations to be in the affirmative. However, there are considerable debates about the findings and empirical evidence across countries and the arguments are quite inconclusive and with mixed results. For example Grilli and Milesi-Ferretti, (1995), Kraay, (1998) and Rodrick, (1998) found that capital market does not affect growth, while others stood their ground that the effect is positive (Levine, 2001, Bekaert et al., 2003 and Bonfiglioli and Mendicino, 2004), others noted that it is negative (Eichengreen and Leblang, 2003). Certain studies show the effects to be heterogeneous across countries at different stages of institutional and economic development (Bekaert et al, 2003, and Edwards, 2001) and countries with different macroeconomic frameworks (Arteta, Einchengreen and Wyplosz, 2001). Rancière, Tornell and Westermann (2006) observed that we could expect the growth effect of capital markets to be smaller in high-income than in middle-income countries.

Investors often debate the merits of value and growth investing. Holt says that he's a little like Warren Buffett in that he thinks growth and value are equally important and somewhat joined at the hip. Valuation is also important. The Hansberger International Fund is a core fund, holding both value and growth companies. As the world headed into the market crisis, Holt and his team started moving up the quality ladder. Companies that were larger, had very strong balance sheets, had pricing power and market position were becoming cheaper.

Capital Market

All long-run growth theories imply that a country can grow faster by investing more, in human or physical capital or in R&D. A promising way forward is to integrate the capital market into a general macroeconomic framework following Blanchard (1981) and Gavin (1989).

According to Al-Faki (2006), the capital market is a network of specialized financial institutions, series of mechanisms, processes and infrastructure that, in various ways, facilitate the bringing together of suppliers and users of medium to long term capital for investment in socioeconomic developmental projects".

Capital markets are markets for buying and selling equity and debt instruments. Capital markets channel savings and investment between suppliers of capital such as retail investors and institutional investors, and users of capital like businesses, government and individuals. Capital markets are vital to the functioning of an economy, since capital is a critical component for generating economic output. Capital markets include primary markets, where new stock and bond issues are sold to investors, and secondary markets, which trade existing securities.

Capital markets are a broad category of markets facilitating the buying and selling of financial instruments. In particular, there are two categories of financial instruments that capital in which markets are involved. These are equity securities, which are often known as stocks, and debt securities, which are often known as bonds. Capital markets involve the issuing of stocks and bonds for medium-term and long-term durations, generally terms of one year or more.

The term "capital" refers to markets for financial instruments of long-term investment tools with maturities of one year or more and where equity instruments are traded. Capital market securities, such as stock and long-term bonds, are often held by financial intermediaries, insurance companies and pension funds, which have little uncertainty about the amount of funds which they will have available to deal with in the future. The most significant chrematistic tools of this market's shares and bonds in long-term debt are:

- A capital market linked within long-term securities
- An effective role in financing long-term productive projects
- A capital market more structured than other markets because dealers are agent specialists
- Investment in the capital market is far more risky and bears less liquidity than the money market
- The returns are high on capital compared with investment in other markets.

Stimulating economic growth and development requires long term funding, far longer than the duration for which most savers are willing to commit their funds and this constitutes a barrier to economic growth. In this regard, the capital market provides an avenue for the mobilization and utilization of long-term funds for development and hence it is referred to as the long term end of the financial system. Over the past few decades, globally there has been an upsurge in capital market activity, and emerging markets have accounted for a large amount of this boom. This suggests the growing recognition of the capital market as a tool for fast-tracking economic progress in developing economies. However, critics have argued that the capital market might not perform efficiently in developing countries and that it may not be feasible for these countries to promote stock markets given the huge costs and the poor financial structures (Singh, 1999). In principle, capital markets are expected to accelerate economic growth by providing a boost to domestic savings and increasing the quantity and the quality of investment, provide individuals with additional financial instrument that may better meet their risk preferences and liquidity needs (Levine and Zervos, 1998). This study evaluates capital market and developing economies, challenges to capital market growth, the capital market in Nigeria, capital market and economic growth in Nigeria and policy directions for promoting capital market growth in developing countries.

Other than the distinction between equity and debt, capital markets are also generally divided into two categories of markets, the first of which being primary markets. In primary markets, stocks and bonds are issued directly from companies to investors, businesses and other institutions, often through underwriting. Primary markets allow companies to raise capital without or before holding an initial public offering so as to make as much direct profit as possible. After this point in a company's development, it may choose to hold an initial public offering so as to generate more liquid capital. In such an event, the company will generally sell its shares to a few investment banks or other firms.

Capital markets have numerous participants including individual investors, institutional investors such as pension funds and mutual funds, municipalities and governments, companies and organizations, banks and financial institutions. While many different kinds of groups, including governments, may issue debt through bonds (these are called government bonds), governments may not issue equity through stocks. Suppliers of capital generally want the maximum possible return at the lowest possible risk, while users of capital want to raise capital at the lowest possible cost.

The size of a nation's capital markets is directly proportional to the size of its economy. The United States, the world's largest economy, has the largest and deepest capital markets. Because capital markets move money from people who have it to organizations who need it in order to be productive, they are critical to a smoothly functioning modern economy. They are also particularly important in that equity and debt securities are often seen as representative of the relative health of markets around the world.

Investment

The investment decision making process of individuals has been explored through experiments by Barua and Srinivasan (1986, 1987a, 1991). They conclude that the risk perception of individuals are significantly influenced by the skewness of the return distribution. This implies that while taking investment decisions, investors are concerned about the possibility of maximum losses in addition to the variability of returns. Thus the mean variance framework does not fully explain the investment decision making process of individuals. Gupta (1991b) argues that designing a portfolio for a client is much more than merely picking up securities for investment. The portfolio manager needs to understand the psyche of his client while designing his portfolio.

Value investing

Value investors love a bargain. The philosophy is pretty simple: Find stocks that are low priced as a result of a company's temporary difficulty or its industry's having fallen out of favor, or a bear market- and buy. Value devotees look at the "intrinsic value" of the stockthe actual value of the company-and compare it with the value that investors have given its shares in the market. Intrinsic value is the value of the business including its assets, earnings, and dividends: this may differ considerably from the amount that might be paid to purchase the company outright.

The term *value* suggests that the investor is buying stock that is relatively less expensive, as opposed to stock that is relatively more expensive. The stock of a company that is classified as a “value stock” typically has a lower price-to-earnings ratio, which simply means that the stock currently has a lower price per share relative to the company’s earnings per share.

Value investments are defined as companies whose stock prices do not necessarily reflect their worth. Value investors actively hunt for shares they believe are undervalued by the market but still have a strong potential upside. These stocks are analyzed by comparing the company’s intrinsic value to its current market value. A businesses’ intrinsic value is determined by evaluating the fundamental aspect of the company including its business model, management, financial statements and competitive situation. When a company’s intrinsic value is higher than its current market value, the stock is considered a value.

Earlier this year, Fit Bit released a quarterly report showing a 50 percent year-to-year increase in revenues and a prediction of continued revenue growth in 2016. However, because the company had invested heavily in R&D, earnings per share dropped on a year-to-year basis. This resulted in a 19 percent drop in Fit Bit’s stock price, which created the perfect opportunity for value investors to buy a strong value stock at a considerable discount.

Undervalued companies can often provide long-term profits for those who do their homework. A value stock trades at a price below where it appears it should be based on its financial status and technical trading indicators. It may have high dividend payout ratios or low financial ratios such as price-to-book or price-to-earnings ratios. The stock price may also have dropped due to public perception regarding factors that have little to do with the company’s current operations. For example, the stock price of a well-run, financially sound company may drop substantially for a short time period if the company CEO becomes embroiled in a serious personal scandal. Smart investors know that this is a good time to buy the stock, as the public will soon forget about the incident and the price will most likely revert to its previous level.

Value Investing focuses on selecting stocks that are undervalued by the stock market in relation to their fundamental strengths and growth potential. The approach was pioneered by Benjamin Graham and David Dodd in the year 1934 in Security Analysis, a book which they co-authored. Well known practitioners of this strategy today include Warren Buffet, and PremWatsa.

Salient principles of Value investing

- Assessment of the growth of the company based on the track record of the company and investor estimation of future performance.
- Value investors identify stocks that are being traded at market prices lower than their intrinsic value;
- A margin of safety becomes important because of future uncertainty. Value investors make purchases only if the current market price is at a substantial discount to their evaluation;
- The strategy is built on the understanding that you are not just purchasing a stock, you are investing in the future of a company. A long term horizon is an essential feature of value investing;
- Patience is a key quality in value investing. The price of a stock may double within a year after purchase but staying invested and allowing time for growth and maturity could give even better returns;

Of course, the definition of what exactly is a good value for a given stock is somewhat subjective and varies according to the investor’s philosophy and point of view. Value stocks are typically considered to carry less risk than growth stocks because they are usually found with larger, more-established companies. However, their prices do not always return to their previous higher levels as expected.

So, how do value investors define a bargain? How low is "cheap," and how high is "too expensive?" "It's a difficult thing to do, but the best value investors are able to look very clearly when stocks are out of favor," says Eric McKissack, CEO of Channing Capital Management, That is, in part, because value investors take a very disciplined approach to scouting out stocks.

A value investor seeks out bargains, and chooses investments that have low prices in relation to such factors as earnings, sales, net current assets, and the book value of the issuing companies. A value investor might reject a popular blue chip stock because the price per share is too high, even though the issuing company is stable and has a record of steady growth. Instead, the value investor seeks to buy stock of a solid company that is temporarily out of favor or bargain priced for some other reason. In doing so, the value investor predicts that the share price will eventually return to a higher level when the stock comes back into favor, and the market drives the stock price back up. A mutual fund manager may specialize in growth investing, value investing, or some combination.

"They are generally looking backward-they're almost like historians," says QuintanoDownes, CEO of Haven Financial Services. "Value investors examine financial statements of the company over the years." They may also calculate a company's price-earnings ratio, or P/E, to see if the current stock price is lower than the value of the company. A price-earnings ratio divides a company's current share price by its earnings per share-otherwise known as the profit the company makes per outstanding share. Here's a simple example: If a company is currently trading at $50 a share, and earnings over the last 12 months were $2 per share, the P/E ratio for the stock would be 25 ($50/$2).

Growth Investing

“The purpose of business is to create and keep a customer”,Peter F. Drucker

While growth stocks have the potential to offer higher returns, when compared to value stocks, they tend to have more volatility. The risk is a sudden price drop in the stock due to negative earnings or bad news about the company. So remember, volatility is part of the growth game — higher potential upside comes with higher risk of downside but wild swings are part of the ride.

Growth stocks have higher price-to-earnings ratios; thus, an investor who purchases a growth stock is paying a higher price per share because he or she believes the stock price might go even higher.Thomas Rowe Price, Jr. has been called "the father of growth investing", because of his work defining and promoting growth investing through his company. "Growth investing has to do with name recognition," says Douglas Coe. Managing partner and chief investment strategist at Moody Reid Financial Advisors "These are companies that everybody knows are making money. They're offering leading services, or their product is in demand." Growth lovers tend to ignore higher P/E ratios. If a growth investor believes a company's share price hasn't yet hit its peak and still has potential for rapid growth, he or she will purchase shares, hoping to sell at a later date at a much higher price.

As the name implies, growth companies by definition are those that have substantial potential for growth in the foreseeable future. Growth companies may currently be growing at a faster rate than the overall markets, and they often devote most of their current revenue toward further expansion. Every sector of the market has growth companies, but they are more prevalent in some areas such as technology, alternative energy and biotechnology.

Most growth stocks tend to be newer companies with innovative products that are expected to make a big impact in the market in the future, but there are exceptions. Some growth companies are simply very well-run entities with good business models that have capitalized on the demand for their products. Growth stocks can provide substantial returns on capital, but many of them are smaller, less-stable companies that may also experience severe price declines.

An investor looking to commit a portion of their portfolio for a very long term should look into growth investing. These investments won’t give quick returns but when they do pay off, it can be well worth the wait. Growth stocks are shares in companies with strong momentum, using every resource to expand their product

International Journal of Engineering Technology Science and Research
IJETSR
www.ijetsr.com
ISSN 2394 – 3386
Volume 4, Issue 10
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or service to generate more revenue and dominate that particular market. Investors buy these stocks with the expectation they will steadily increase in price and net a tidy profit when sold.

Two current examples of these stocks are Amazon and Netflix. Both companies prioritize technological advancement and infrastructure expansion over profit in an effort to dominate their categories. Their success has driven the value of their shares upward over the past two decades. These businesses can see higher price-to-earning ratios and price-to-book ratios which indicate the market's certainty in a company's ability to continue increasing profits.

To repeat, growth investors must keep in mind that these stocks should be part of a long-term strategy. When buying your shares, choose companies with products or services you believe in and stick with them when the market swings.

When you invest for growth, you are typically seeking capital appreciation over the long term. You will likely choose investments that you believe will exhibit a faster-than-average increase in share price over the coming years. Growth stocks have the potential to outperform slower-growing investments, such as income stocks, because gains are generally reinvested in the company to achieve further growth rather than distributed to shareholders as a dividend. Growth stocks can be volatile. One way to minimize the impact of that volatility on your portfolio is to purchase shares of a growth mutual fund. You'll enjoy instant diversification (though diversification alone cannot guarantee a profit or ensure against a loss). And an actively-managed mutual fund also offers professional management expertise.

Buying and selling these stocks based on downturns in the market will cost you money in either actual losses or in profits from future appreciation of the stock. As with any investment and before you buy any stock, be sure to research all aspects of the company to make smarter investment decisions for your portfolio.

Investment in India

Nearly two decades of economic liberalization, coupled with robust domestic demand, a growing middle class, a young population and a high return on investment, made India a credible investment destination. In the new global dynamics, India has assumed the role of a lead player on the economic stage. India's economic growth in the last two decades has garnered immense investor interest.

With a growth rate of around 8 percent, the decade of 2000 was the shining decade for India that caught the attention of global investors and global institutions alike and opened the gateways for opportunities in several sectors. At this juncture is of crucial importance as, while the world economy has been pushed in a slow lane post the global financial crisis, the Indian economy is also going through a phase of consolidation. Today, with the structural shift in world economy towards the "Emerging Economies", India has not lost its sheen as its growth fundamentals remain strong. Going forward, the country is expected to move on a higher growth trajectory supported by its strong domestic demand, dynamic service sector, improving infrastructure, and a youthful population.

Though investment declined in FY09, it was an impact of global slowdown. Positively, investment recovered in the following year. In FY13, the external sector of the country has witnessed a strong impetus, which is indicative of the global confidence in India's growth. FI in India picked up momentum and was recorded at $ 50.2 billion in FY 13, higher than FY 11 and FY 12. Going forward, this is expected to improve as the global economy gains strength. The total FDI inflow into India from April 2000 to June 2013 amounted to $ 199 billion, with Mauritius, Singapore and the UK being the three largest sources of FI, accounting for a share of 58 percent.

The economic reforms carried out by the government has emphasized on creating an investor friendly environment which includes opening up foreign direct investment in most sectors. India is committed to carry forward the economic reforms to ensure the fulfillment of developmental aspirations of its people. Through our bilateral and multi-lateral trade and investment agreements we have been working to bring our economic engagement in complete alignment with the intent of increasing investment in the country. India has also emerged as a significant investor abroad which is a reflection of the growing maturity of its economy.

Value Investing In India.

Value investing is one of the most popular investment themes globally. For instance, the proportion of assets in Value Funds and Growth Funds is nearly equal. As against this, in India, the proportion of assets in Value Funds is merely 10% of assets invested in Growth and other strategies. While most investment gurus would proclaim India to be a growth market where growth investing is the most suited investment style, the truth is that Indian markets offer a good opportunity to use value investing. In fact, value investing can be successfully applied in all types of markets – developed or high growth ones such as India or China. The contention for this view is that the investing strategy is not impacted by the type of market in order to be successful but by factors such as market sentiment, knowledge levels, industry life cycles, etc.

Value picking is an art which is acquired with long term investment experience. This necessitates retail investors to preferably use the mutual fund route to invest in value funds to profit from this investment strategy. However, investors should keep in mind that the fund manager of a value fund expects the fund's investors to stay invested for the long term till the market recognizes the value of the stock and price discovery takes place. This requires patience, which would eventually lead to reasonable gains. In conclusion, value investing focuses more on the investor's cost; lower the cost, higher the margin of safety. The key to profit from this investment style is to stay with the investment for the long term.

Growth Investment in India

Fresh investments by the corporate sector hit a new low in fiscal year (FY) 2016-17. The combined capital expenditure (capex) by the country's top 1,000 non-financial firms, in terms of revenue, was up just 5.8 per cent in FY17, growing at the slowest pace since 1992. The previous low of capex growth was in FY1999-00, after the dotcom bubble in Year 2000. In all these, the top 1,000 companies made fresh investments of Rs 2.07 lakh crore in the last fiscal year, down from Rs 2.9 lakh crore in FY16, and an all-time high of Rs 5.7 lakh crore in FY14.

Analysts attribute this decline to a poor demand in the economy and reluctance by banks to lend to new projects. "It's in line with a near-collapse in banks' credit growth in the last fiscal year. Public sector banks have put a virtual freeze on fresh lending to risky projects, fearing bad loans hitting funding for large industrial projects," says G Chokkalingam, founder & managing director, Equinomics Research & Advisory.

The incremental capex by listed private sector companies nearly halved to around Rs 1.1 lakh crore in the last fiscal year, against Rs 2.15 lakh crore a year ago. The amount is the lowest in 10 years and a third of record high reached in FY12. In contrast, private sector companies have accounted for 80 per cent of all incremental capex by listed non-financial and non-oil public sector undertakings (PSUs) in the past decade. In absolute terms, private sector companies have cumulatively invested around Rs 26 lakh crore in fixed assets (net of accumulated depreciation) in the past decade, against Rs 32 lakh crore invested by all listed companies during the period.

Current Investment scenario of India

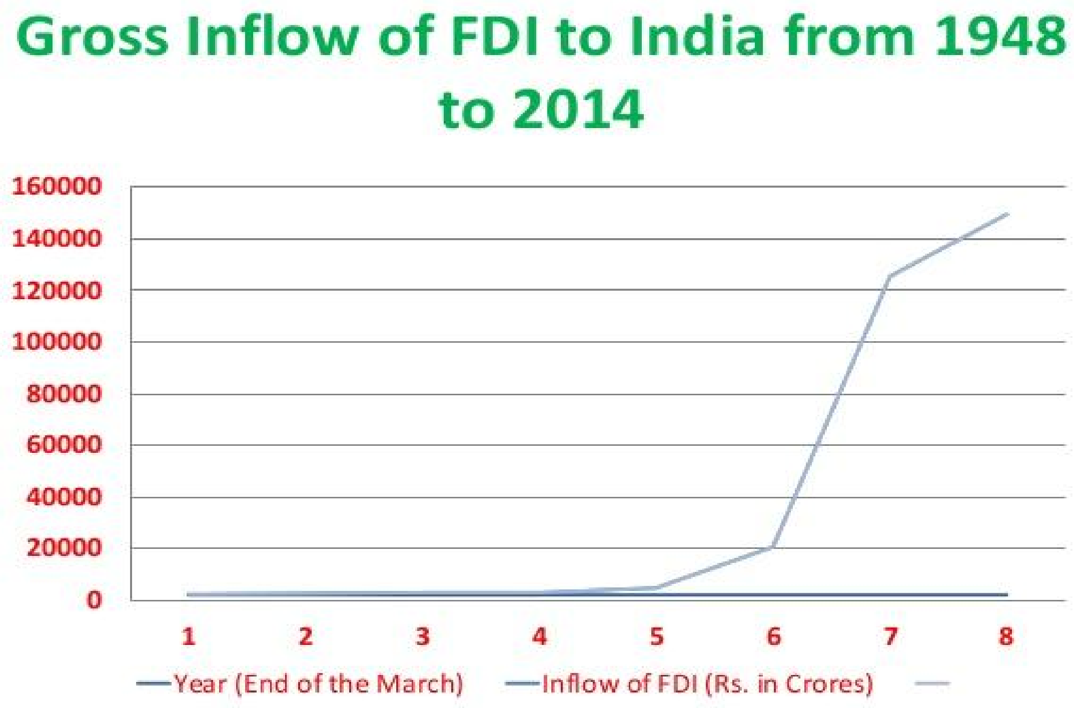
The analysis is based on the annual finances of a common sample of 728 companies that are part of BSE 500, BSE MidCap and BSE SmallCap index. The sample excludes banks and financials, and public sector energy companies such as Oil and Natural Gas Corporation, IndianOil and Hindustan Petroleum. FY17 figures were taken based on unaudited financials, which may not include subsidiaries' data of some companies, while capex refers to annual incremental growth in fixed assets defined as gross block minus accumulated depreciation plus capital work in progress.

CPSEs seem to have been least impacted by the slowdown, while MNCs reported an uptick in capex growth, though their investments are too small to move the needle. The capex growth by private sector companies was down 320 basis points (bps) on a year-on-year (YoY) basis, against a 90-bps decline in capex growth by CPSEs on a YoY basis.One basis point is one-hundredth of a per cent. Some examples of private sector companies include Tata Motors, Mahindra & Mahindra, Reliance Industries, ITC, Grasim Industries, Hindalco, UltraTech Cement, Hero MotoCorp, among others.The combined capex of all listed companies - excluding banks and financials and oil PSUs - grew by 6.2 per cent in FY17, growing at the slowest pace in over a decade. In absolute terms, incremental investment in fixed assets declined to Rs 1.71 lakh crore in FY17, against Rs 2.77 lakh crore in FY16. The amount was the lowest since FY07.

Economists say that the data corroborates the trend of a steady decline in the share of investments in the country's gross domestic product (GDP). "If you look at the expenditure side of GDP, investment growth is now down to single digits. Whatever investment growth is happening is largely due to incremental spending by state and central governments," says Devendra Pant, chief economist and head-public finance, India Ratings. Others flag the issue of falling return on existing investments. "There is little economic incentive for companies to make fresh investment when return on existing assets is less than the risk-free return or that of bank deposits," says Dhananjay Sinha, head-research, economist and strategist at Emkay Global Financial Services.   The return on assets for the private sector companies declined to 5.1 per cent in FY17, down 2 bps on a YoY basis. It used to be around 12 per cent prior to the 2008 capex boom. In comparison, the yield on the 10-year government bond is around 6.5 per cent, while a State Bank of India five-year fixed deposit earns around 8.5 per cent.

Gross fixed capital formation (GFCF), which indicates investment demand in the economy, is forecast to grow by 3.3% in FY17, jump to 6.8% in FY18 and overtake private consumption (7.4%) in FY19 with 8.8% growth to become the major growth driver. This is due to the key reform steps taken by the government such as implementation of bankruptcy law and goods and services tax, higher infrastructure push and continued inflow of foreign direct investment. Abolition of Foreign Investment Promotion Board will further support investment growth. Moreover, RBI efforts to reform banking sector in addition to a higher steady state of banking sector deposits post-demonetization will eventually allow credit growth to recover robustly and sustainably.

International Journal of Engineering Technology Science and Research
IJETSR
www.ijetsr.com
ISSN 2394 – 3386
Volume 4, Issue 10
October 2017



Experts don't foresee any meaningful turnaround in the corporate capex cycle in the near-term, given poor return on existing investments and tepid demand growth across sectors. India now faces a structural problem, with lack of demand depressing returns across sectors. Exports are not helping, with flat- to low-single digit growth in software and pharmaceutical exports. The only way out is a large fiscal stimulus, which looks difficult, given financial commitments towards entitlement programmes such as farm loan waivers.

Private investment continues to face impediments in the form of corporate debt overhang, stress in the financial sector with rising bad loans, excess industrial capacity, and regulatory and policy challenges, putting downside pressures on India's potential growth. In February, the industrial production index for capital goods contracted 3.4%, while credit to industry contracted 5.2%, suggesting a meaningful recovery in private investments is unlikely until later in FY18.

On the positive side, consumption will remain robust, given declining inflation and solid household credit growth, and pick-up in trade is likely to endure at least through the first half of the fiscal year, helping lift investment. Private investment, which accounts for three quarters of total GFCF, has not been forthcoming despite the promise of crowding-in by public sector investments and government efforts to improve the business environment and facilitate foreign direct investment (FDI). GFCF contracted by 2.1% in the fourth quarter and GFCF as a percent of gross domestic product (GDP) stood at 28.5% during the same quarter compared to a medium-term average (5 year) of 32.4% of GDP. This weakness in private investment has been attributed to local and global excess-capacity, leveraged corporate and bank balance sheets, and remaining domestic bottlenecks.

International Journal of Engineering Technology Science and Research
IJETSR
www.ijetsr.com
ISSN 2394 – 3386
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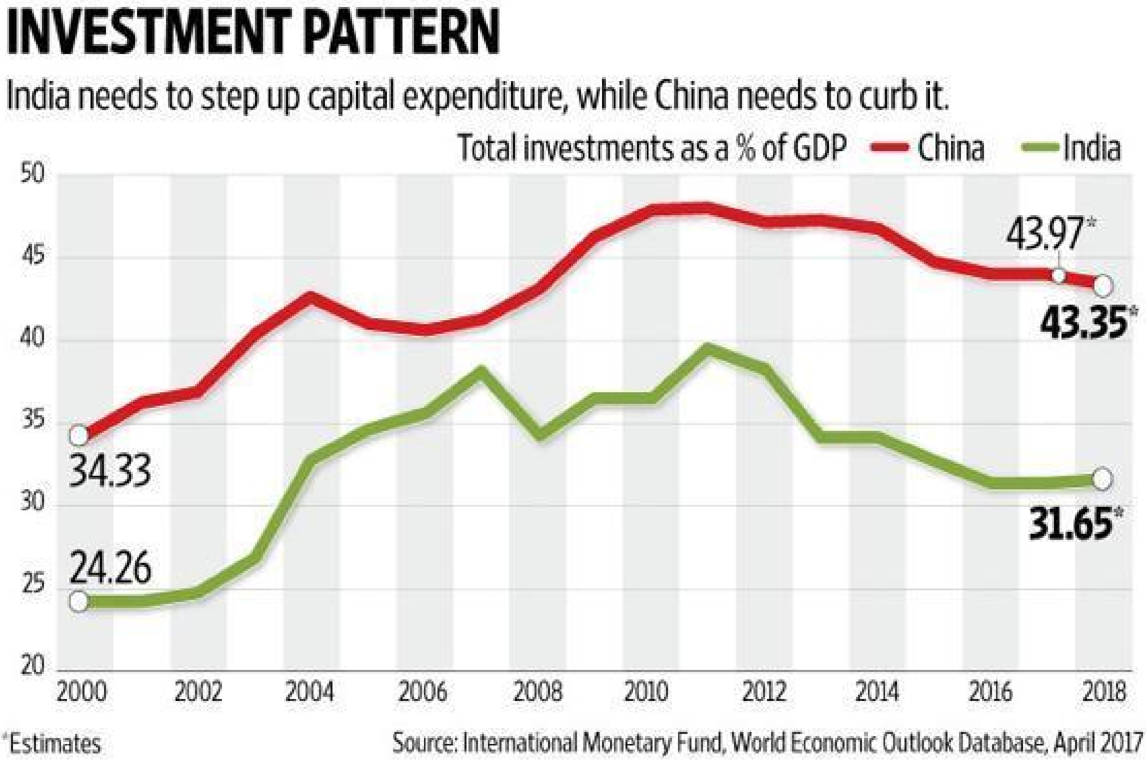

Supporting the view of an incipient pick-up, production of capital goods expanded by 6.8% in January 2017 after 13 consecutive months of negative growth, imports of machinery rose by 13.5% in March, and FDI expanded by 10.9% in Q3 FY17 driven primarily by investments in the telecommunications sector. At a time of weakness in investment growth, private consumption remains a stable growth driver, expected to range between 7.2% and 7.5% between FY17 and FY20. The minor deceleration in FY17 is offset by higher rural incomes from favourable agricultural growth, revisions to civil servants' pay by an average of 24%, and declining inflationary expectations.

Sunil Kant Munjal, chairman, Hero Enterprise agreed with the World Bank's assessment that next year could see a revival in private investments. "Companies do not invest because they see little scope for return. Now capacity is getting absorbed and consumption is increasing, companies are looking at investing in the months to come," he adds. The Bank expects government to maintain its momentum in public infrastructure spending, with government capital expenditure budgeted at 3% of GDP in FY18, flat from previous year. Private investment is expected to pick up, but only gradually as recovery may be protracted, in part due to relatively longer-term effects of demonetization on cash-reliant construction activities (household investment, largely housing, accounts for approximately 1/3 of total investment), corporate leverage and the persistent weakness in credit growth, which suggest that the financial sector may require more time to adjust.

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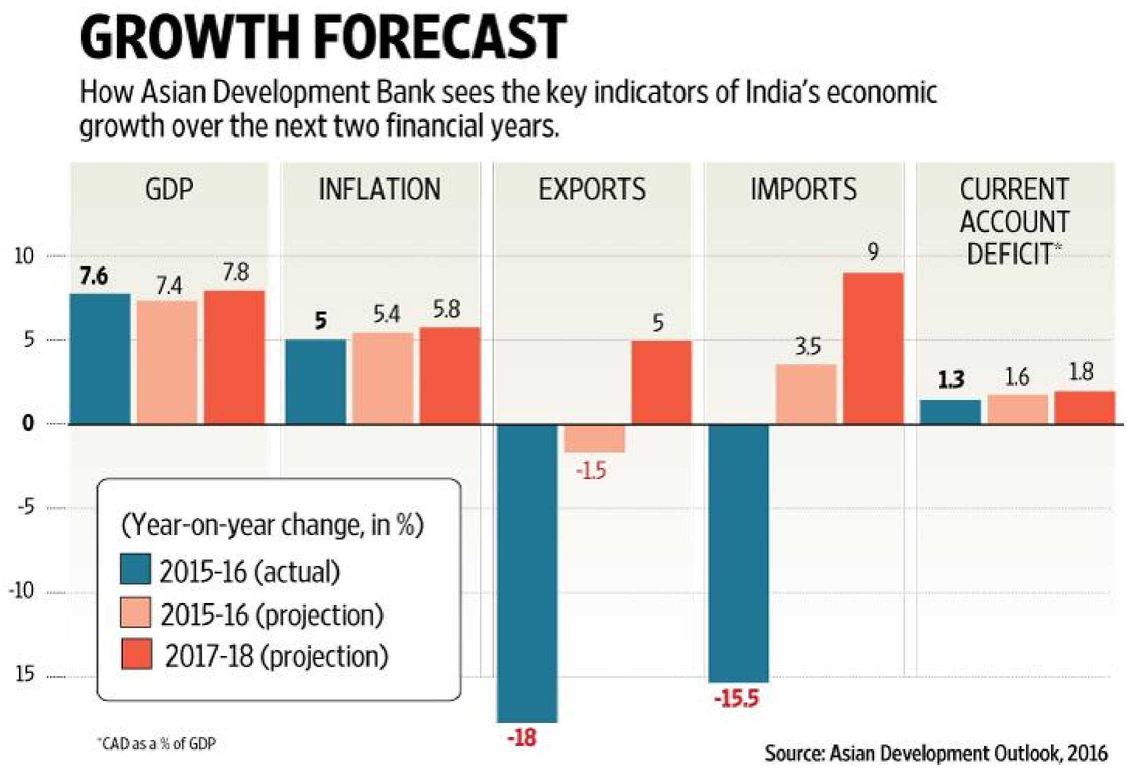

Asia's two giant developing economies, India and China, are heading in opposite directions, with China—in the midst of a structural shift towards more sustainable growth—slowing down while India is set to pick up, ADB said. ADB has projected China's economic growth to slow to 6.5% and 6.3% in 2016-17 and 2017-18, respectively, against 6.9% in 2015-16.

In India, structural reform intended to attract more foreign direct investment is gradually moving forward, but further reform is needed to raise private investment and lift potential growth," the ADB report added. Public investment will continue to be an important driver of growth, as the government is expected to use savings from oil to further boost government investment. The finances available to ramp up investment in FY17 will be considerably smaller than in FY16, given the sharper pace of fiscal tightening and increased outgo on account of a higher public sector wage bill.

Private consumption growth is estimated to have picked up to 7.6% in 2015-16 from 6.2% a year earlier. These estimates are likely to be optimistic, as achieving them would require private consumption to grow at 11.7% in the fourth quarter of 2015-16, nearly double the 6.1% growth rate achieved in the first three quarters. Much of the improvement in private consumption stems from a pick-up in urban consumption, while rural consumption has remained subdued as a result of two consecutive weak monsoons. After two years of decline, the consumer inflation to accelerate to an average of 5.4% in 2016-17 and 5.8% in 2017-18 as global oil prices firm up and domestic demand strengthens.

Conclusion

Capital markets are increasingly interconnected in a globalized economy, ripples in one corner of the world can cause major waves elsewhere.Stocks can provide a return on capital from future growth, current undervaluation or dividend income. Many stocks (such as AT&T) offer some combination of these, and smart investors know that dividends can make a substantial difference in the total return they receive. Over the past 10 years, growth stocks have outperformed value stocks six times and value stocks have outperformed growth stocks four times. A large body of empirical research indicates that growth stocks on average earn higher returns than value stocks. The reward to growth investing is more pronounced for small stocks but it is also present in the larger stocks. Growth stocks rocketed in value, prompting speculation that value investors were an endangered species. A more careful examination, however, suggests that the differences across the performance of equity classes in the past ten years were not grounded on fundamental patterns of profitability growth.

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