

September 15, 2011

## INSIGHTS

## India Strategy

### Keep the Faith, Investing is in Vogue

**Key Debate:** How have investors behaved with respect to their holding periods through the volatility and tepid equity returns of the past four years?

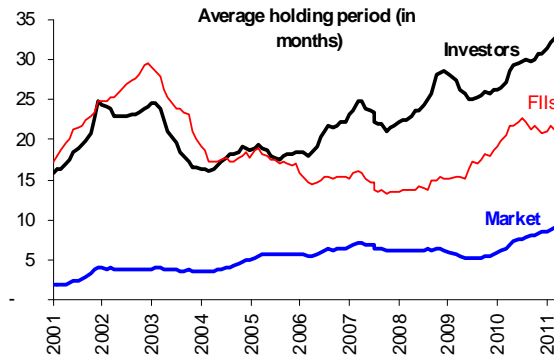
**The stock 'renting' culture of the previous decade seems behind us:** Contrary to popular belief, investing (vs. speculating) has not been abandoned. Indeed, the holding period of all market participants on aggregate has doubled in the last two years. 'Investors' are now holding stocks for an average of nearly three years. The shift of speculative trading from the cash market to the derivatives' market has helped.

**FII's appear more committed:** In the previous bull market, FII's bought stocks but reduced holding periods as the bull market matured. In the past three years, FII ownership has deepened and lengthened.

**Market still seeking safety of large caps:** Share of Sensex trading is still rising and this concentration of trading may mean that the broad market has not troughed if one uses just trading data as a guide.

**Winners trade less, not more:** The higher the trading velocity the poorer has been the performance of the stock over the past 12 months, we have found.

#### Holding Period Rises for All Investor Classes



Source: BSE, NSE, Morgan Stanley Research

MORGAN STANLEY RESEARCH  
Asia

Morgan Stanley India Company Private Limited+

**Ridham Desai**

Ridham.Desai@morganstanley.com  
+91 22 6118 2222

**Sheela Rathi**

Sheela.Rathi@morganstanley.com  
+91 22 6118 2224

**Utkarsh Khandelwal**

Utkarsh.Khandelwal@morganstanley.com  
+91 22 6118 2226

**Amruta Pabalkar**

Amruta.Pabalkar@morganstanley.com  
+91 22 6118 2225

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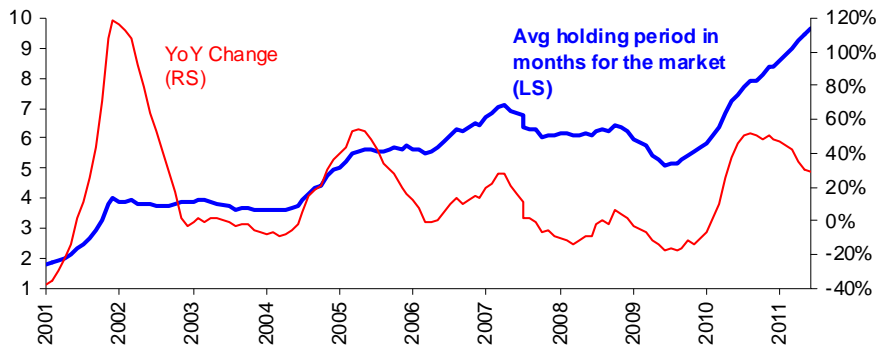
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## Investors are Going Strong

### Market Participants Holding Stocks for Longer

The renting behavior of the previous decade appears to be ebbing

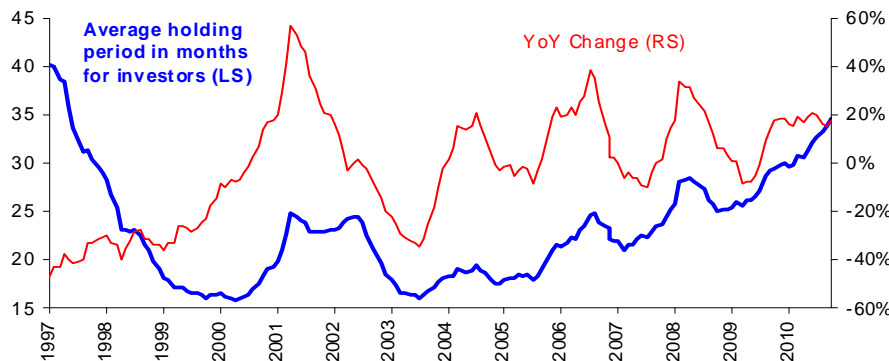


### Investor holding period rises

- Despite low returns from equities over the past two years, the average holding period for the market has surged from around 5 months to 10 months.
- It is even better for investors – the holding period has expanded from around 20 months during the 2003-2007 bull market to 35 months now.
- The evidence is that “renting” of stocks which was in vogue for the bulk of the previous decade is no longer the norm now.

### Investing Culture in Vogue

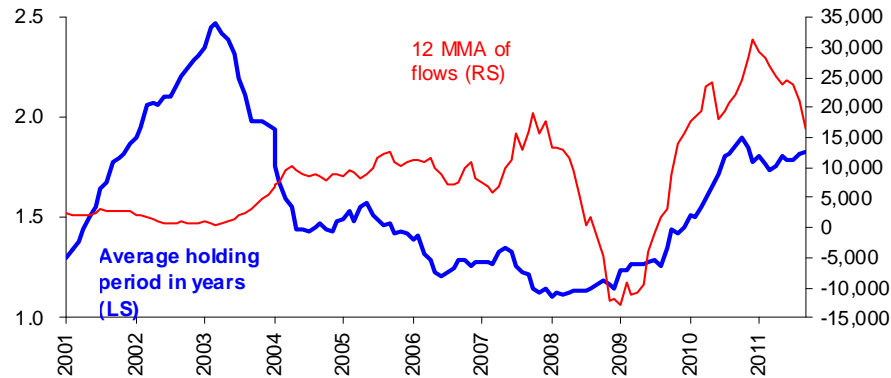
Average holding period has doubled



## FII's Appear More Committed Than Before

### Rising Ownership Accompanied by Longer Ownership

Average holding period has doubled from the 2008 low

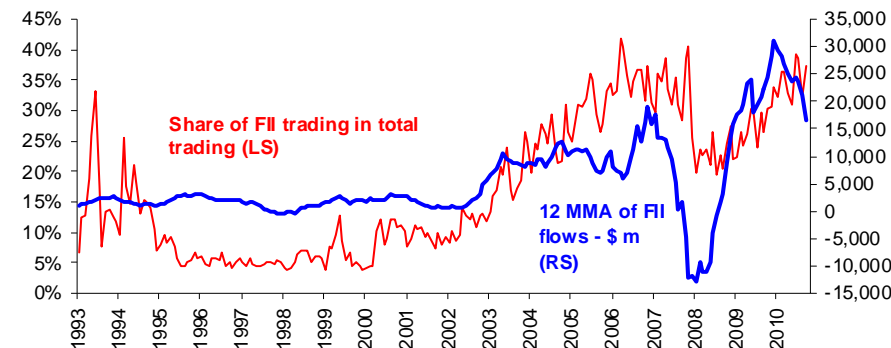


### FII's lengthen holding period

- There has been a dramatic change in the behavior of FIIs in recent months. Through the 2003-2007 cycle, FIIs bought stocks but held them for lower periods. At the end of the bull market, the average holding period had declined to just 14 months.
- This has changed since and, currently, the net buying of FIIs has been accompanied with higher holding period. The average holding period is at a multi-year high of 22 months.

### FII's are a Large Part of Cash Trading

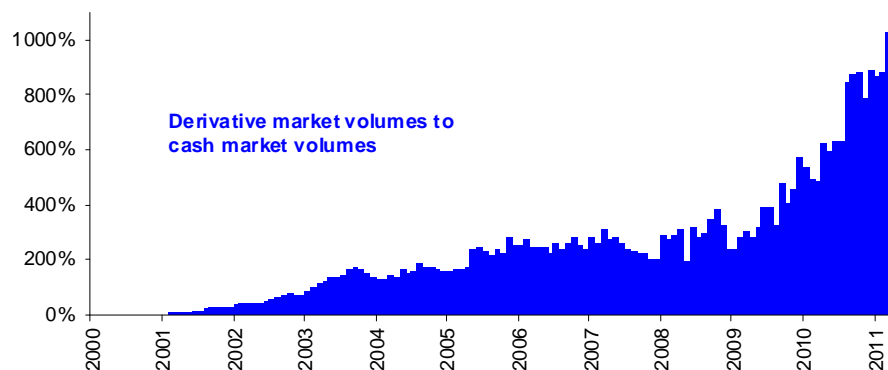
Trading share mirrors increase in net flows



## Speculative Activity Has Shifted to Derivatives

### Derivatives market accounts for bulk of stock market trading

The share of cash trading is less than 10% of total trading

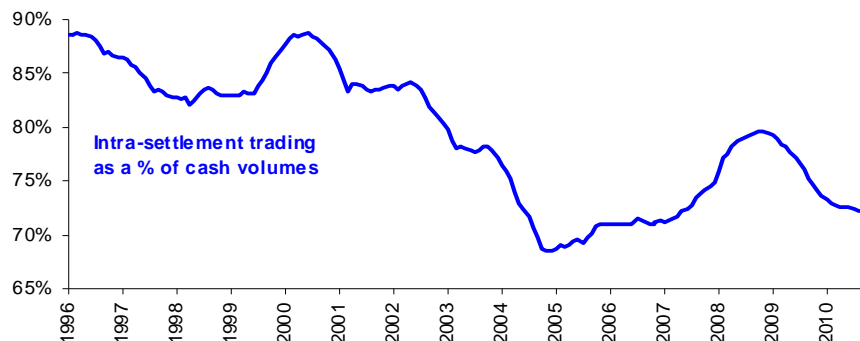


### Cash market has lost share dramatically in the past 3 years

- A large part of the speculative turnover has shifted out of the cash market into the derivatives market. Thus, intra-day trading has declined from its 2008 peak and is much lower than its 2000 peak.
- This shift of speculative activity from the cash to derivative markets may also be a driver for the increased holding period of actual stock.

### Intra-day trading is losing share in the cash market

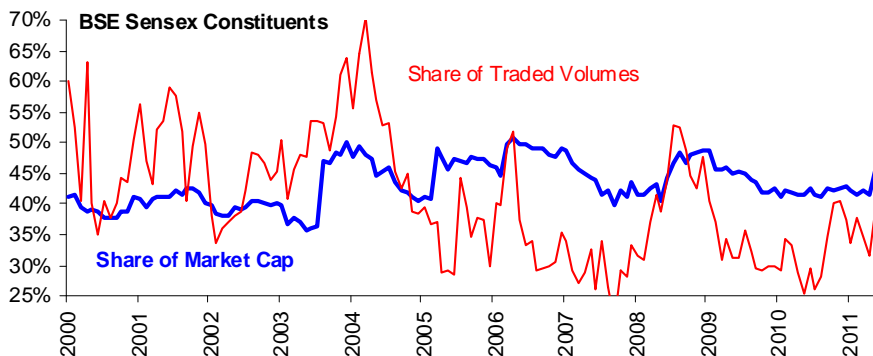
Consequence of growing "investing" activity



## Market Still Seeking Safety of Large Caps

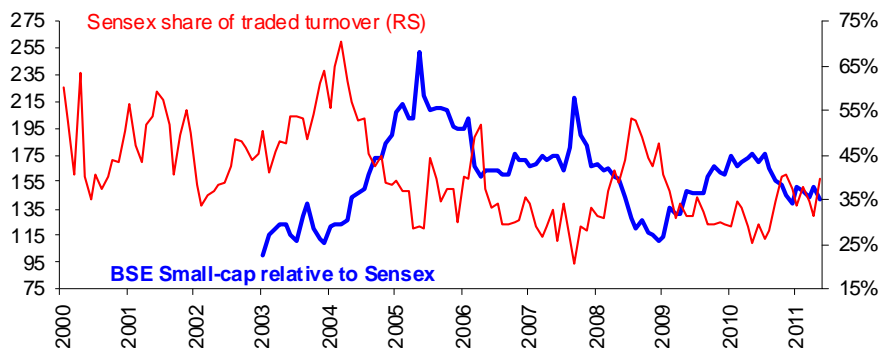
### Share of Sensex Constituents in Trading Rising

Concentration of trading turnover reminiscent of a bear market



### As Share of Sensex Trading Peaks, Broad Market Troughs

Based on the trading indicator, broad market may have relative downside



### Sensex trading volumes still off high

- The share of trading of Sensex stocks in total traded volumes is rising. Usually a peak in this number coincides with a relative low for the broad market to the Sensex.
- Given the rise in the share of trading of Sensex stocks, a relative trough in the broad market may be around the corner although we are not quite there if this indicator is a guide.

## Higher Stock Trading Has Implied Bad Stock Price Performance

### On An Average, the More A Stock Trades, the Worse it Fares

As usual there are exceptions

#### Trading Velocity of NIFTY stocks

	Trading Velocity	Trailing 12M Perf.		Trading Velocity	Trailing 12M Perf.
DLF	492%	-41%	ACC	97%	4%
Reliance Capital	480%	-49%	ICICI Bank	92%	-21%
Reliance Comm.	327%	-51%	Jindal Steel & Power	91%	-27%
Reliance Infra.	303%	-58%	Siemens	89%	17%
Jaiprakash	297%	-47%	TCS	89%	12%
SBI	256%	-41%	Kotak Mahindra Bank	87%	-1%
Sesa Goa	243%	-31%	ONGC	87%	-24%
Tata Motors	242%	-29%	Maruti Suzuki	86%	-19%
Tata Steel	236%	-24%	L&T	80%	-14%
Cairn India Ltd.	234%	-17%	Reliance Industries	79%	-19%
Reliance Power	181%	-51%	Cipla	78%	-5%
IDFC	175%	-43%	Wipro	77%	-19%
AXIS Bank	173%	-26%	Dr. Reddy's Lab	76%	0%
Ranbaxy Laboratories	172%	-4%	Ambuja Cements	74%	4%
Hindalco Industries	167%	-25%	GAIL	70%	-13%
Hero Motocorp	162%	-31%	Sun Pharma.	68%	39%
BPCL	155%	-12%	Infosys	67%	-25%
Power Grid	155%	-10%	Punjab National Bank	61%	-25%
SAIL	143%	-46%	HDFC Bank	61%	3%
Bhel	122%	-31%	HUL	60%	24%
M&M	113%	18%	HDFC	59%	-2%
Bharti	107%	11%	NTPC	58%	-22%
Sterlite Industries	106%	-24%	Tata Power	46%	-22%
HCL Tech	104%	-8%	ITC	38%	20%
Bajaj Auto	101%	7%	Grasim Industries	34%	1%

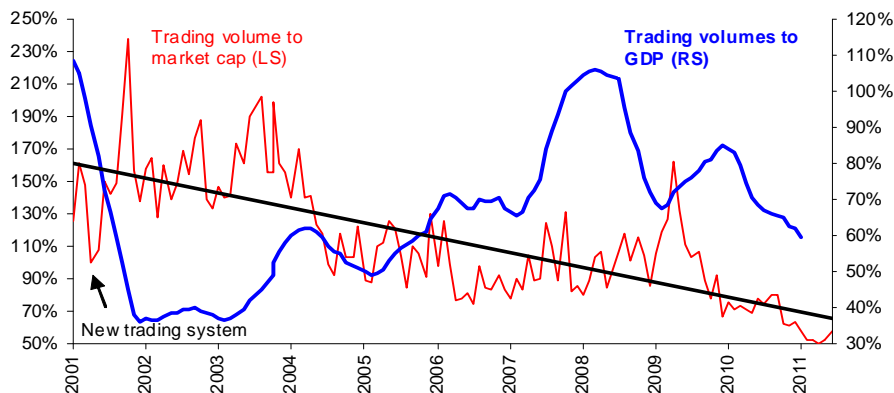
### 20% of Nifty constituents churn free float less than 5 months

- The more a stock trades, the worse has been its performance. The top losers of the past 12 months are also the stocks that have maximum turnover.
- There are several stocks in the Nifty which are witnessing a churn in their free float every quarter or more frequently.

## Sharp Decline in Cash Trading Volume

### Cash Trading Volume is at All-time Low

The decline trading relative to GDP is a bear market phenomenon

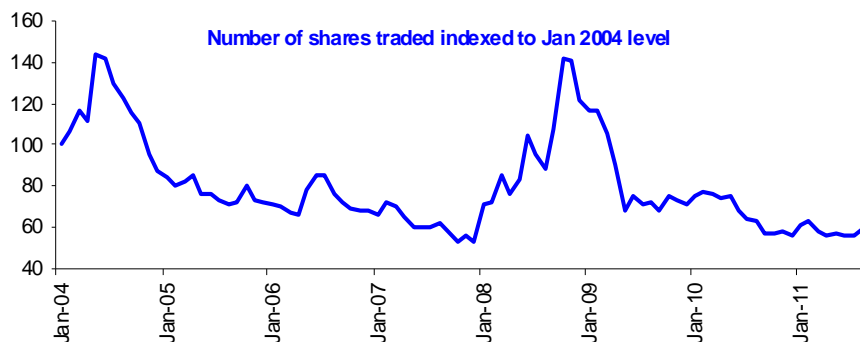


### Cash trading losing ground

- The bad news for brokerages is that cash trading volume has declined sharply over the past few years.
- The shift in trading system to derivatives has impacted cash trading over time. We may be in a new norm in terms of cash trading though there could be upside if a bull market ensued.

### Cash Trading Volumes has Halved in Six Years

This may be a new normal for cash trading activity





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Stock Rating Category	Coverage Universe		Investment Banking Clients (IBC)		
	Count	% of Total	Count	% of Total IBC	% of Rating Category
<b>Overweight/Buy</b>	<b>1120</b>	<b>41%</b>	<b>460</b>	<b>48%</b>	<b>41%</b>
<b>Equal-weight/Hold</b>	<b>1151</b>	<b>42%</b>	<b>389</b>	<b>40%</b>	<b>34%</b>
<b>Not-Rated/Hold</b>	<b>114</b>	<b>4%</b>	<b>21</b>	<b>2%</b>	<b>18%</b>
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New York, NY 10036-8293  
United States  
+1 212 761 4000

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20 Bank Street, Canary Wharf  
London E14 4AD  
United Kingdom  
+44 (0)20 7425 8000

## **Japan**

4-20-3 Ebisu, Shibuya-ku  
Tokyo 150-6008  
Japan  
+81 (0) 3 5424 5000

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1 Austin Road West  
Kowloon  
Hong Kong  
+852 2848 5200