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India still in structural bull-run, here's how to pick value stocks: Experts

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NEW DELHI: After a massive rally of about 30 per seen in the previous calendar year, benchmark indices might now be trading near their key support levels, but analysts say that the structural bull run still remains intact.

The S&P BSE Sensex has fallen about 3,000 points from their record high of 30K. It has actually erased gains made so far in the year 2015, both in rupee as well as in dollar terms. So, is this the right time to enter the markets? Definitely yes, sayexperts.

"The growth story in India is strong and consistent, and the Indian markets are in astructural global bull run. So with that background, India is poised to do well," says D K Aggarwal, CMD, SMC Investments and Advisors Ltd.

"Therefore, it is advised to investors to accumulate stocks. They should buy on every dip. They can enter the markets at current levels, but for a long term," he adds.

The recent slide in the stock market has resulted in several shares seeing prices last seen before May 2014 - when the Narendra Modi-led BJP government was elected.

More than 180 stocks on the BSE 500 index have declined in dollar terms below the levels seen before the election as hopes of a speedy revival in the economy recede and corporate earnings growth struggles to pick up, ET reported.

Both domestic as well as global factors have weighed on the Indian markets. Long-term investors should actually use the current weakness to buy into quality stocks, to build a long-term portfolio.

"The basic thing you (investors) have to go by is the trend in the economy. Indications are that India will move up, but it will take time. We are in a structural bullmarket. So, sensible investors will remain bullish for a long time," says Porinju Veliyath, Equity Intelligence India.

"But because of the time factor, you will have to pick the right stocks - those that are futuristic in business. I am talking of stocks which may be facing hurdles today, but which are deep-value choices over the longer term," he adds.

After the correction in the past few days, there are certain stocks which are currently at very attractive valuations and thus provide downside protection, say experts. Although, near-term weakness is likely to keep the benchmark indices under pressure, but most global fund managers do believe that India has become more of a long-term story.

They are not yet changing their view on India despite underperformance, but some portfolio churn/shift to other EMs cannot be ruled out.

The earnings growth has disappointed, major reforms have to still see the light of the day and other emerging markets have started outperforming. These are some of the factors which are weighing on the markets.

"We have seen the market come down almost 10%, largely due to the concern of one-off factors about where this economy is heading, concerns about taxation and its implementation, and also the poor monsoon and its impact on rural demand. But at the same time, there has been a noticeable shift from growth to value and we have seen that across the region," says Medha Samant of Fidelity Worldwide Investment.

"Market such as India or some of the ASEAN markets, which were considered to be the growth-driven markets, have underperformed and there has been a shift towardsvalue. We believe in the long-term potential for India and one reason is that when we look at earnings, these earnings have been downgraded. So we are now looking at a more normalised EPS growth for the market," she adds.

Samant is of the view that at 12.8 times PE, India is looking very attractive compared to its own historical averages and any correction historically has always proved to be a good entry point.

Experts advise investors to buy good quality stocks which are trading below their intrinsic value. Investors should evaluate each stock as per their own analysis, and start betting on all which are significantly undervalued.

"We do not support the notion of timing the markets based on anticipating when it will go down further or go up. Our approach is that one should buy when one is convinced that a stock is below intrinsic value," says Dr. Vikas Gupta, EVP. Arthveda Fund Management Co Ltd.

Here is a list of steps highlighted by Dr. Vikas Gupta of Arthveda Fund Management Co Ltd, which will help in filtering out low-quality companies which might not be a 'value' even at low price to book ratios.

Further, it also allows high quality companies, which might be a good valueeven at seemingly higher price, to book ratios.

The screening process by which we can create a pool of better companies is as follows:

Step 1: Filter our all companies with sales less than INR 250 crore. Companies with sales lower than this are very small companies and might not have business stability and access to finance that is required for a safe investment. So we will select companies with sales equal to or greater than INR 250 crore.

Step 2: Filter out all companies with debt to equity greater than 30%. Companies with low leverage are safer.

Step 3: Filter out all companies with interest coverage ratio of less than 4. Companies with high interest coverage ratio are good.

Step 4: Filter out all companies with ROE less than 15% since they are earning less than their cost of capital.

Step 5: Filter out all companies with PE ratio greater than 25 since they are too expensive even for a high quality company.

From the remaining pool of companies, one can now start evaluating one by one. However, if this pool is still very large, one can start making the filters more stringent.

One can look at companies larger than sales of INR 500 crore or even 1000 crore. One can look at zero debt companies. One can look at ROE which is greater than 20% and one can look at PE ratio less than 20 and price-to-book less than 1.5.

From a pool of about 25 or so companies, one can start picking companies by reading their annual reports and their corporate profiles on their websites.