Print This P

'Bull market? No one cheering except TV anchors; 70% of NSE stocks below 200-DMA'

In good old days, the stock market was considered as a barometer of the economy but it no longer appears to hold true in modern times as the stock markets across the globe are defying the gravity.

Excess liquidity in the global economy for decades has skyrocketed the prices of financial assets beyond their fundamental justification. Even Indian markets appear to be no exception.

A handful of the stocks managed to pull the value of the benchmark indices to new highs, in which, ironically the majority of the investor portfolios still bled whereas television anchors of business channels got a reason to celebrate with new T-shirts while the majority of the individual stocks traded lower.

This clearly points at the defects in the index composition and weights allotted to individual scrips. To support this argument we ran queries on 1,850 stocks listed at the National Stock Exchange (NSE).

Shockingly, we have found 1,329 out of 1,849 stocks are below 200-day moving average whereas 1,096 out of 1,849 have either slipped or are trading below the equivalent level of Nifty October 2018 lows of 10,000.

Besides, 1,177 stocks out of 1,849 registered a death cross suggesting a strong bearish sentiment. This clearly points at how Sensex and Nifty paint a misleading picture of the broader market.

In fact, when the market veteran, Deepak Mohoni coined the phrase Sensex, he explained the reason as the movement of broader markets being sensitive to the movement of a small group of main stocks.

So, it looked very appropriate to look at the benchmark index called Sensex to gauge the broader direction of the market.

But, unfortunately in the current scenario, broader gauges have failed to present the real outlook of the markets, which perhaps also highlights not only the defects present in the index composition but also stresses the need to seriously look into bringing sea changes in the composition of the broader gauge to present a realistic picture of the market.

How indices are composed

At present indices are computed by following a free float market capitalisation methodology. Hence, top 50 counters by market capitalisation whose impact cost is less than 0.5 percent usually make into the Nifty50 (in-depth explanation of these concepts is beyond the scope of this article).

This can be the prime reason why financial services alone got a weight of 39.8 percent in the Nifty50 while their real contribution in the GDP is around 20 percent.

Though, energy sector that enjoys the second highest weight of 14.74 percent and accommodates laggards like ONGC, NTPC and GAIL, has failed to drag the index. This is largely because Reliance Industries alone enjoys a weight of 9.47 percent in the Nifty50.

IT and consumer goods, which have a weight of 13.76 percent and 10.74 percent, respectively, have been outperformers, aiding the benchmark index to reach new heights.

Though 13 sectors have a representation in the Nifty50, the index is heavily skewed towards above mentioned four sectors, which enjoy a cumulative weight of 79.1 percent.

Other sectors, which though are critical for real economy— PSU banks, autos, construction, pharma, telecom, etc—carry only 21 percent weight in the index. Hence, their underperformance is not being captured in the index due to their underrepresentation.

This is the reason why nobody in the market is cheering for the new milestones being recorded on the bourses except our TV anchors.

There is a real need to address this problem by recomposing the index. Recomposing the index would not only help represent the real economy but should also be able to present the real picture of the broader market as we can't consistently have a situation in which handful of stocks keep hitting new highs whereas remaining 60 percent of the market keeps going down and out.

The author is Chief Strategist – Technical Research & Trading Advisory, Chartviewindia.in.

Disclaimer: *The views and investment tips expressed by investment expert on Moneycontrol.com are his own and not that of the website or its management. Moneycontrol.com advises users to check with certified experts before taking any investment decisions.*