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While There Is Life (Energy) The Pendulum Will Swing

I spent several recent weeks (summer 2011) in India and I met many people involved in investing, in business, entrepreneurs, and it seemed that pretty much everyone seems to be involved in real-estate. My key take-away from these meetings is that the sentiment is that the Indian economy is doing well; but the mood is a little more muted than it was a year ago. Yet, Indians are generally bullish on the India story, and rightly so.

A little surprising was the very offhanded dismissal of the U.S. and its investment opportunities. As a professional investor, I look for the good and the bad in every situation, but then try to take a dispassionate view. The near universal dismissal of U.S. investments, suggested that there was "blood in the streets" – which I believe is an excellent time to invest. And I think that based on fundamentals, U.S. investments are quite attractively priced.

But emotions and dogmas are not reliable allies for making good investment decisions which must be supported by realities. So as I refreshed my thinking about the current investment scenarios, especially in light of the Aug 2011 equity markets sell off, here are some interesting things I (re) learned.

India VS U.S. – The story

I have been a strong proponent of the India story since 2000. The country found its moorings and has taken advantage of opportunities to become a player on the world stage. Indeed the future does look bright (if not in a purely linear manner). The fundamental story of growth remains good.

However, this does not negate an equally compelling story called the U.S. It's a different story; one not of growth, but one of successfully being able to manage its unfathomably vast resources and expectations. The U.S. is far from being a "basket case" - the view so strongly held by my Indian contacts.

I also feel that a debate as to which is the better story will be a very long (measured in years) and inconclusive one.

As a professional investor, the critical question when faced with two compelling opportunities is: Which opportunity is priced more correctly? And as a Value investor, the question is even simpler: Which opportunity is cheaper and safer today?

India VS U.S. – The stock market(s)

At a very high level, here are some interesting return numbers to consider:

	India SENSEX*	U.S. SP500**
Price Return - Last 5 years (ended 8/31/2011)	+32.0%	-5.9%

This supports the popular notion that the U.S. markets have been dismal and not worthy of any serious investment consideration. And, were that the final answer, I would also be empathic with my Indian friends.

But digging a little more:

	India SENSEX*	U.S. SP500**
Price Return - Last 2 years (ended 8/31/2011)	-0.5%	+18.5%
Price Return - Last 1 year (ended 8/31/2011)	-11.9%	+14.5%
Price Return - Year to date (ended 8/31/2011)	-22.7%	-3.1%

NOTE: all these numbers are price based only, not total return. This means that dividends are not included. Including dividends will improve the numbers, but not change the story. Moreover, the end date of 8/31/2011 is quite arbitrary – I happened to be writing this note in early Sept 2011; different time periods will show different results. And of course one cannot invest in an index directly and any fund that enables investment in an index will have fees and transaction costs associated with it. I believe that including fees and costs will strengthen the U.S. numbers, since these costs are considerably lower in U.S. products than in Indian products.
** BSE SENSEX Index is a well regarded and popular benchmark of the Indian stock market.*
*** SP500 Index is a well regarded and popular benchmark of the U.S. stock market.*

So it gets a little harder to dismiss the U.S. stock market as a "basket case" if more recent history is looked at. This is not surprising. Indeed, I am sure if a good analyst with enough time on his hands were to sit and torture the data, they could make it say anything they want it to. But to my mind the central point is that the opportunity pendulum keeps swinging – sometimes favoring one view and at other times favoring the opposite.

Market timing is hard, but conceptually an Investor who invested in India in the earlier part of the last five years and then diversified (into U.S. investments) in the latter part had a chance of doing better. Making a decision like this is very hard, but keeping one's mind open to possibilities is within our control. However, having a dogma that one market (be it U.S. or India or any other) is a clear winner or loser and will forever stay that way is simply too injurious to your wealth. As long as there is life (energy) the pendulum will swing.

India VS U.S. – Real Estate.

Interestingly a similar case can be made for real-estate, the (current) absolute darling of Indian investors. While I do not have any reliable data on Indian real-estate, the vast majority of anecdotes I heard, talk of the huge (but largely un-quantified) returns, and the conviction that these will last for many years to come. This belief comes with an accompanying sentiment that like the U.S. stock market, U.S. real-estate is not the place to be after the recent meltdown.

This caused me to review some information on U.S. real-estate complied and published by NAREIT.

A history of REIT (Real Estate Investment Trusts) returns for the last 10 years is:

	FTSE NAREIT All REITs
Year	Total Return (%)
2000	25.89
2001	15.50
2002	5.22
2003	38.47
2004	30.41
2005	8.29
2006	34.35
2007	-17.83
2008	-37.34
2009	27.45
2010	27.58

REITs: These are specialty companies set up to invest primarily in real-estate ventures. A REIT typically buys, manages and sells real-estate. Investors do not have a direct ownership of real-estate as they may have in the homes they own; but they have shares in a company whose sole objective is to operate in the real-estate space and whose assets are pre-dominantly real-estate.

The FTSE NAREIT US Real Estate Index is calculated by FTSE International Limited ("FTSE"). NAREIT® is a trademark of the National Association of Real Estate Investment Trusts. All data are derived from, and apply only to, publicly traded securities. As is the case with any index, one cannot invest directly in it and any fund that enables investment in an index will have fees and transaction costs associated with it.

Clearly the losses for 2007 and 2008, seem to have made all the headlines and the deep impressions. But on balance the picture is not entirely dismal, if an investor looks at the longer trends.

The FTSE NAREIT Index represents very broad investments in Real Estate including: Industrial / Office, Retail, Residential, Lodging and Resorts, Storage, Timber and other diversified types of real-estate. Nor is the Index centered on a few marquee areas like New York or the West Coast, but represents holdings across the U.S. If marquee areas were cherry picked (as they often are in India: Mumbai, New Delhi, Gurgaon etc.) I suspect the picture would be even more dramatic.

Moreover, the real-estate investment possibilities come with fewer restrictions: REIT's are valued daily and can be traded on the open markets. Investments can be made in very modest amounts often as low as a thousand dollars. Investments can typically be deployed within three days and can be liquidated within three days. They don't need real-estate brokers, lawyers, property papers, dealing with governmental friction, currency of different colors etc. – all of which reduce the money that the investor actually makes. And REITs offer far more diversification than holding a few properties does.

Parting Thoughts

This note is not intended to make a case for investing either in the U.S. or India. Rather its point is that capital, in astute hands, is unemotional and seeks the best opportunities. To find the fertile areas at any point in time needs an open mind and an ongoing review and analysis of opportunities. Yesterday's barren field is often today's fertile one. Indeed while there is life the opportunity pendulum will swing.

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