



# GROWTH WOES & RBI FOLLY

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**Do you feel that the India growth story has gone down the drain? Or is it just a cycle that we are going through - high inflation leading to high interest rates....?**

It will eventually all come around. The 'India growth story' has not gone away forever, but it has hit a bump on the road. We are already talking of less than 7 per cent GDP growth this year. The problem is that when you break the momentum of growth, it is hard to recreate it.

**What led to that?**

Primarily the policies of the RBI. When you have double digit interest rates, you cannot be competitive in any business. One of the main reasons we had a bull market was that interest rates were low in 2002-03. So corporate India could compete. And of course, when interest rates are low, equity as an asset class becomes more attractive. Both those factors have worked against the stock market. And ill conceived movements like Anna Hazare's is also paralyzing decision

making, even among honest ministers and bureaucrats.

**Did the RBI not have to act to control inflation?**

Inflation cannot be controlled by the RBI. There is no co-relation. From the time this tightening cycle began I have been very vocal about it. I have said this dozens of times. I do not understand the purpose of this. All factors that are causing inflation are market determined. Nothing that can be controlled.

The only thing that has been controlled is growth. Now the issue is that if you do not have growth, you do not end up creating purchasing power. Think about it. Oil prices went from \$20 to \$100/barrel over the past 10 years. Did it curb consumption of fuel? Or, for that matter, affect the sales of cars? On the contrary. There was a quantum growth in the Indian auto industry during this period. The economy was doing well. If the economy is growing, the inflation gets accounted for. Salary hikes and rising wages and job opportunities takes care

of it. If there is no growth, then even \$20/barrel is too much.

So my point is that only through growth can the problem of inflation be solved. Because it is growth that will increase the purchasing power at the hands of the consumer. Now when you have inflation and growth is killed, it will have an adverse affect in terms of pay hikes and job opportunities.

In my view, the RBI has taken a very Western perspective which does not make sense in this country at this point of time.

Growth is so precious in this world today. Countries are fighting for 1 per cent growth. Here we had 8.5 per cent growth and we do not like it. It is just absurd. Subbarao will go down in history as the RBI Governor who derailed the growth story for a period of time.



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#### **What in your view is the cause of the inflation levels we are seeing today?**

Global commodity prices. Agricultural products, commodity prices, crude, all of them have been high.

#### **The government stimulus post the 2008-crisis aided consumption while nothing was done on the supply side. This too resulted in inflation. Is this not so?**

In theory - yes. But you cannot change the supply side overnight. It takes time. The fact of the matter is that due to increased prosperity we are consuming more.

#### **There is a view that the downturn we are facing is all to do with homegrown issues and not the global crisis. Do you agree?**

But one cannot deny that we are facing a very tough global macro environment and we are correlated with the world markets. Go back into history and see the linkage from the mid-90s of the bull and bear markets in India and the world.

#### **Do you think India needs to spend much more on infrastructure?**

I don't think we should be spending excessive-

ly on infrastructure. Every country that spends heavily on infrastructure goes bust.

#### **Is that your view on China? Going bust?**

Yes. Countries are not like companies that can go bust in a few quarters - its takes time.

Japan, USA, China - all have gone bust. China is technically bust whether it is going to be known tomorrow or a year later.

#### **So what is your view on building infrastructure then?**

The point I am making is that we should not be forced into building infrastructure simply for the sake of building infrastructure. We should spend on infrastructure but it should be done in its course. It would be stupid to blindly emulate the other countries that have gone over-

board by spending heavily on infrastructure for the sake of it. The reason I am saying this is because we do not have that kind of purchasing power in India to support that infrastructure. You need the purchasing power to use those roads and airports and ports and bridges.

#### **What is working for India?**

What's working for India is our Gods, 33 crore Gods - one God for every four Indians. It prevents us from doing stupid things.

#### **The reason for your sarcasm?**

I am not being sarcastic.

#### **Do you feel much more needs to be done on the reforms front?**

I think India is doing just fine and we are fundamentally in good shape.

The government has done a phenomenal job of stimulating rural demand. They are of the view that urban demand can take care of itself, we do not need to do much there. So they have gone out and stimulated rural demand. The government has done a lot to empower the poor and that is where the consumption story over the past few years has come from. Not

## COVER STORY

because of urban demand but rural demand. That has not just happened because the Gods willed it. The government made it happen.

We have a power policy where companies can go and set up a plant. We have a right to education bill. We have the UID.

The only problem I see is the RBI policies. And the Anna movement.

### How worrying is the fiscal deficit?

The fiscal deficit is always something to worry about but I don't think it is a make-or-break issue. The real worry is the external situation - the current account deficit, the BoP. That might become a problem, I think the internal deficit is not too worrisome right now.

### A while back you gave an interview in the media on why you believe the India growth story has



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### gone down the drain. You seemed to have changed your view.

Let me be clear. My view on the GDP number is negative. What this means is that I am negative on growth prospects which translates into corporate profitability. But if you ask me about the government policies, whether they are good or bad, I am saying that I find no fault with them.

### What do you feel is the biggest problem facing corporate India today?

High interest rates. The high interest rates are killing demand and hitting profitability. Lack of fund raising. These are the issues. But then again, corporates have grown substantially in the past 7-8 years. So there is a cyclical angle to this entire slowdown in corporate profitability. No company can keep expanding profits by 20 per cent for 20 consecutive years. No company has done it before barring Microsoft. So it has to slow down. There could be many reasons but the core reason is that cyclically it is due for a slowdown. Which is what we are experiencing.

### Where demand is concerned, do you see a drop in volumes?

There will always be a lag effect. You raise rates today, demand will not fall tomorrow. It will take a while for that impact to manifest. There is some growth momentum which continues. But when it is done continuously over a year it will hit profitability.

### What is your view on earnings in the next few quarters?

Going by this quarter, I do not see any hope of a revival. Commodity prices softening will help certain parts of the industry for sure. But on the hand that softening will hurt the suppliers of commodities. Overall, corporate profitability won't see a rise.

### Around a month ago, you had made a statement saying that it will not be smart to invest in large caps.

That would have not been a blanket statement, there would have been a context to that. But broadly, large caps appeared expensive while mid and small caps were absolutely decimated at 1x PE. So that is where I would rather go. Hunt for mid- and small-cap companies that would survive the downturn. Large caps in that sense have no value.

But of course such picks need a lot of work in terms of analysis and understanding of the business etc. And then one can find some gems that will turn out to be multi-baggers.

**You have said that you do not look at valuations but you look at momentum. Can you be more explicit?**

Valuations are vague. What is cheap? What is expensive? It is hard to define. Typically I look at momentum because when there is momentum of earnings then a so-called expensive stock will also do well. If there is momentum in the stock price, that has a life of its own. But just buying a cheap stock will not tell me whether the stock is going to go up or not. So I find this entire theory of value investing to be slightly misplaced. If there is value plus momentum, then it is a good trade. Value without momentum is not a necessarily a good trade. The momentum will tell you that others

market will go up by, say, 10 or 20 per cent. Someone smart enough to play this will make some trading money. But buy-and-hold investors have a long wait.

**Are you invested in the market right now?**

I don't have a single rupee in equity right now.

**In that case, where do you advise investors to invest?**

I would advise them not to. At least in a fixed deposit they will get their money back. The focus is now on return of capital, not return on capital.

**When do feel is a good time to get into the market?**

I think a sell off of another 25 per cent off the index will be a good time to get in which means in stocks, the fall could be another 35-40 per cent.



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also believe there is value in that stock. If I am the only one believing that there is value in a stock but the rest of the market ignores it, what is the point of such a trade?

**How do you define a bear market and going by your definition, are we in one?**

We most certainly are in one. I define one as when the market falls 50 per cent off the peak.

**You see more pain?**

A lot, lot more pain.

**So is it a good time to get into the market now and hold?**

No.

**The coming year won't see any market revival?**

I don't see any money to be made now. And I really doubt there will be money to be made next year too. Occasional trading moves will take place where a trader can make money, but not an investor. Twelve months down the road, we should be lower than where we are right now. The trend is down though there will be the occasional sharp rallies where the

**If an investor told you that he had to compulsorily get into the market right now - what would you suggest?**

There are just around 10 stocks that look good right now. For instance, Tata Motors and Mahindra & Mahindra. Some consumer companies look good from a defensive perspective such as Unilever and ITC. I don't know how much more room they have to run on the upside, but on the downside they look good. Some pharma companies look good. Banks don't look good.

**Over the long term, would you still bet on India?**

In the short term and medium term, it will be tough. There is no easy way out of the situation we are in. Next year this time I see the market even lower than what it is now. But from a long-term perspective I am happy to be invested in India. We will be the only guys left standing. On a 10-year basis, India will be the country to take a bet on for sure. ■

*GDP: Gross Domestic Product / RBI: Reserve Bank of India / BoP: Balance of Payments / UID: Unique Identification / PE: Price to Earnings ratio*