THE ECONOMIC TIMES

August 3, 2023

India will outperform and here are 3 sectors where weightage has gone up: Devina Mehra

Synopsis
Despite the recent downgrade by Fitch for the US outlook, it should have little impact on the markets. The issues referred to were already known, such as the high debt ceiling and deficits, even a global risk-free alternative to US treasuries has yet to be found. India is still expected to outperform, despite a possible pause or correction. First Global, which rebalances quarterly, has seen an increase in weightage in the healthcare sector on the pharma side, in addition to capital goods and industrial machinery alongside increased weightage also found in auto, auto components, and a couple of construction names.

Devina Mehra, Chairperson & MD, **First Global**, says "in March end, I had said this is the time to get in, when the index was sub 17,000. It has obviously run up from there. There might be a pause, there might be some correction here and there, but the broad trend still remains. We still like equities globally. We still think India will outperform."

Fitch has downgraded the US outlook. Their view is not having an impact on global markets per se. Do you think both global and Indian markets should ignore the latest rating change from Fitch?

As far as the rating change is concerned, it was not new information for the market. The rating does not really matter in the sense the issues that it referred to were already well known in the markets, whether the debt ceiling, which has not happened for the first time and obviously the debt to GDP is high. The deficits are high, which is, of course, separate from the ratings. This is the part that is at the back of the mind. We are a little worried that the current account deficit and the fiscal deficit in the US, the twin deficits remain high.

But none of the issues themselves were new news for the market, which is why probably it reacted a bit here and there but broadly, it was already known.

The fact is that even as we speak, if you talk of a global risk-free instrument, there is still no instrument which comes anywhere close to US treasuries in the minds of the world because what is the alternative? Do you want to buy a China treasury? And as far as even Europe is concerned, while they have navigated 25 years better than I thought they would, there are a lot of disparate elements that are being managed in terms of very different economies, very different fiscal situations. If you go back to the great financial crisis of 2008-09, some of those things can almost go to breaking point in a crisis.

Markets have had a good run up and some would argue that a lot of triggers have already played out. Adani stocks have revived. Monsoon has been okay. Margin pressure seems to be abating. So what is next for the market now?

I am not one for narratives and this happens on a day-to day basis, whatever happens in the markets and we like to fit a narrative to that that may or may not be correct. If the US market falls and India also falls, then we are falling because of global cues. If we do not fall, then we are decoupling. So even on a daily and weekly basis, I see that kind of commentary.

If I look at the broader outlook for India, for one, we had a very long period of underperformance in the 2010-2020 decade when we were far below the trend line. Instead of that 15-16% compounding that we expect from Indian equity markets, that whole decade, we compounded only 8% odd at a time when fixed deposit rates were 7-8%. So we were far below the trend line. That is why once the revival came post the Covid crisis, I expected it to last long and therefore also the risk of a crash goes down because the crashes really come when the markets are far above the trend line, and we are still not there yet.

While I do not necessarily like to look at index level PEs, again, we are not very stretched and numbers are within the 22-25 range, which is not horribly high. And margin pressures are easing but that has not come into the numbers completely yet. It is starting to come into the numbers.

And part of the reason, of course, is that the commodity prices have come down, particularly downstream from crude, though of course, now crude has bumped up a bit. But still compared to last year, we are down significantly. Some of the agri commodities also have come down from peak.

In all of those, I mean, the positives are still there. As I said, the market starts going up again, you will start hearing the India growth story and so on. So the narratives just follow exactly what is happening in the market.

Coming back to the market in March end, I had said this is time to get in, when the index was sub 17,000. It has obviously run up from there. There might be a pause, there might be some correction here and there, but the broad trend still remains. We still like equities globally. We still think India will outperform.

One space which is everyone's consensus buy is the healthcare sector and especially the diagnostics and hospital names. Would you agree with that view?

We have added healthcare but more on the pharma side from the beginning of the year. We rebalance every quarter. We have seen more healthcare names but more on the pharma side. There have been a couple of others also. So, among other sectors, that is one sector where our weightage has gone up in the last six, seven months.

What are the other sectors where the weightage has gone up apart from pharma?

Top down, capital goods and industrial machinery. I have spoken in the past that we have liked these since October 2021. There we have trimmed some because we have booked profits and because some of those stocks went up two-three, even four times. But we will still be the most overweight in that sector.

This calendar year where our weights have gone up have been auto, auto components, pharma, a couple of construction names. Interestingly for the first time in years, our systems in our last run which is the June end run are showing up with more FMCG names. It is not that the sector is a thumping buy, but for the first time we are seeing more stocks there. Of course, last year ITC was among our big winners and Britannia was also there, but we did not have a whole lot of FMCGs. Our systems are beginning to like those a bit more than they used to.

Banking is something which we compared to market weight which is a big, actually a positive vote, given where we usually are in banking about a year ago, a little more than a year ago. And that still continues as an outperformer sector. Again, there has been some internal juggling in terms of stocks but that would still be somewhat at least slightly more than market weight.

Over the years we have interacted, you have been very vocal that you do not like banks, financials. But for somebody who does not like financials, even going market weight, it is a big change in stance. What prompted you?

This is only the banks. In NBFCs, we still have negligible weight. What prompted me last year on banks a little over a year ago, was two or three things.

One, of course, again I am not wedded to any stance. In banking, we had very low weight in 2020 which worked out very well. In 2020, banking was the only sector index in the negative. In 2021, it was not negative, but the market went up 22% and the Nifty Bank went up 11%. So there was a big gap and it went up only half as much as the market.

In the middle of 2022, we thought that the trend was changing. If you look at the fundamentals also, there were a lot of positives. The NPA cycle was behind them in the sense they had already taken the hits and credit growth was accelerating. Again, one could see that interest rates were tightened and in the beginning of a tightening cycle, the banking margins go up simply because they raise interest rates on the loans first and on the deposits, the rates go up much more slowly, only when the deposits come for rollover and so on.

So there was the fundamental side as well as the fact that it had been a dog sector for a while and we thought that was changing. But yes, as you rightly pointed out, I am generally a nervous investor in banks because you do not know where the negative surprises are hiding as an outsider. You have no idea where the money would come back.

This morning, the big headline came in from Morgan Stanley wherein they have upgraded India to overweight. From number six, they have suddenly gone to number one and they are saying valuation is not that expensive, which you also said. But in the entire scheme of India versus China, do you think China will also see a bit of a reversal of trend? Because I think that is what your view was, that China could be the next big mover.

Yes. It is not India versus China. Both can go up and generally, in fact, when the emerging markets move at times, they move as a pack. India, as I said, talked about 2010 to 2020 as being below India's own historical compounding. But the other point also was that in that whole decade, we were generally an underperformer. We were always below the global averages. Again, that changed in 2021 was the first year that began to change.

That is why, the outperformance trend would continue because when that trend reverses it lasts a while. So last year, in dollar terms, while we were down, but we were still in the outperforming bucket. We did not do quite so well in the first half of the year but I think that will change again.

Again, India is among the countries that are in our outperformance bucket along with Germany, France, Mexico. Japan was a country which we watched for a long time in the market for a reversal. We made a big bet in May that now Japan will do well, which it has. As far as China is concerned, it is somewhere where it is on our watch list for an up move. So it is not clearly there yet, but the more likely move is up for China as well.