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Why Devina Mehra is bearish on fin tech companies

Synopsis
"I do not even try to predict FII flows into India let alone China so because I do not think that is a relevant metric to track ."

In 2021 when that trend changed and after a very long time India moved to the outperforming end of global markets, I was quite clear that the trend would continue this year which it has so that clearly has happened, says Devina Mehra, Chairperson, MD & Founder, First Global.

Do tell us now where you see the strength in the Indian markets. Are you as bullish as some of the experts we have been speaking to?

Actually I have been bullish for longer than these experts have been, from the beginning of the year and actually since last year itself I had been saying that India will be an outperformer this year relative to global markets which you have seen has been quite dramatic. Not so much in the absolute movement, if you look at relative to all global equity markets, India has done very well.

And the reason for that was that it had not done so well in the 2010 to 2020 decade relative to other markets when it was almost consistently in most years an underperformer. Out of 42 indices it would be 21, 24, 25 like that and for that entire decade also Indian equity markets compounded only some 8.5% as against a longer term average of 15-16% and that time the fixed deposit rates were also around 8%. So it pretty much gave no extra return at all.

In 2021 when that trend changed and after a very long time India moved to the outperforming end of global markets, I was quite clear that the trend would continue this year which it has - so that clearly has happened. Of course I had also said at the beginning of the year that it is not going to be 2021 where everything goes up together, it is going to be a more selective market where you have to be choosier.

In June this year again I think on your channel itself with Nikunj I had made a very clear call that it was time to be back in the markets because you were in danger of missing out a up move. Because again long term data: Rs 100 invested when the Sensex started to now had become 44000 but if you missed out on the 10 best days of the market, that 44000 goes down to 15000 and this is over 40 years. So 40 odd years you miss out 10 days and two-thirds of your returns go. You miss out 30 best days and almost all your returns go - instead of 44000 you are left with 3900. So I was clear that in June we were in that range and later on I checked the day I had spoken on your channel the index was 15293 so you have got that big 18% move in two months and then of course you know obviously the market cannot keep going on at that pace, so you had that sideways down movement which again now has come out.

But the factors that are working for the markets right now softened commodity prices, there are chances that the Russia Ukraine war could end, there is the big focus on green energy solutions something we were discussing on ET Now - which are the sectors you think that are going to lead the forward charge into calendar 2023 because like you said the market is going to move in pockets it is not going to happen all at once that is what you predicted back then is that something that you still believe and if so which are the pockets do you think that will actually lead the charge now?

I mean in general since you were talking about corporate profits and margins, one really interesting thing which has come out is that if you looked at wholesale prices last in the financial year, the WPI kept going up and the CPI was a long way behind. Although it is not a one to one comparison, but wholesale price index kind of captures the producers cost and that was going up especially with the commodity prices going up so

much but because the consumer did not have purchasing power, that was not getting passed on.

There was this big gap between the WPI and CPI and now you see that gap closing which essentially means that the margin pressure would ease and which is also of course there if you look at commodity prices from January to now most commodities have given up their gains so most commodities are the input side for most industries be- of course, not all.

So of course, at a broader level I see some margin pressures easing.

In terms of sectors we like, our number one sector still that is overweight which has been overweight for over a year has been capital goods and industrial machinery which came out of 2009 to 2020 kind of slump of very poor fundamentals and poor stock performance so that still continues to be overweight may not last a whole of 2023 obviously because many stocks have already gone up two times-four times but for now that still remains overweight. In the last quarter or two we have added on some auto components, auto four wheelers.

We have increased our weights in banks which again was a dog sector in 2020, it was the only sectoral index in the negative, and in 2021 it went up only half as much as the market and that is a sector I generally do not like but now for once we are market weight - may be marginally above also because of the price movement now.

Textiles and chemicals I will not say as a sector but there have been stocks to pick in those sectors so that is also there in general when we did our October rebalance we found our systems are liking small and midcaps better than they used to, so little bit of weightage increases there though we are always careful because we always say that investing is a losers game so first make sure you do not have big draw downs, you do not have big losses, so within that framework you have to play.

What about fintech and the new age tech companies? They have had it really rough this last calendar year. Do you see them coming out of the woods now?

Well that is the risky end of the market and you know again last year when all these IPOs were coming I remember being on a show with Nikunj where he asked me that if I put a gun to your head which one would you buy and I said even with your gun to my head I will not buy any because none of the valuations and in many cases, even the businesses did not make sense.

There were a whole range of reasons why I did not like them and you know we call them as a shorthand as new age tech but these are not really tech companies. The entry barrier in these businesses is not the technology, it is they are either direct to consumer companies like Nykaa or they are platform companies. Now in this, the entry barrier is brand which essentially means how much money are you willing to spend and a listed company actually has a constraint vis-à-vis unlisted competitors that it has to show its bottom line either a profit or reduce loss so it becomes difficult to just throw money at it to gain market share. In fact going into an IPO itself most of them lose market share because they cut back on marketing so there are whole lot host of issues.

Of course you know you may see once something is very beaten down you might get a technical bounce and if you are in that kind of game you can play it but as I said our first focus is having a resilient portfolio that does not see big draw downs.

You mentioned the Russia Ukraine war. On the day of the war the markets went down 5% our portfolios went down 1.6% so that is what I mean by having a more protected portfolio rather than trying to play every game in town.

I am not saying that you should necessarily avoid. As I said that at some points you get these opportunities but we are very careful about playing these.

Still not time to completely avoid risk but you would play these markets cautiously also since you mentioned some external factors like the Russia Ukraine war what do you make of the Chinese protest there has been some amount of easing in COVID related protocols by the authorities in some of those Chinese cities and if that continues do you see FIIs flowing back to China?

I do not even try to predict FII flows into India, let alone China! Because I do not think that is a relevant metric to track and the other thing is that I mean you mentioned the Russia Ukraine war I mean on the day of the war, on the day the war broke out I was I think also on your channel and some other channels where I said that this will not show up in the stock market charts after six months to one year because that has been the history of every geopolitical conflict in the world that when it happened it creates agitation in the markets but other than direct impact that if some commodity prices are impacted or something like that it does not show up in the stock market charts.

Therefore, always look at data. FIIs do the same thing, if you look at data there is no correlation between FII flows and what happens to markets so I do not waste my time.

By the same logic would you say the Fed and its interest rate moves because right now they find themselves in a quandary if you consider the employment data that has come in because unemployment is not rising at the level at which perhaps the Fed was banking on at some level so what would the impact of the Fed's moves the slowing down the pace of interest rates do you think that could have a bearing on how Indian equities do.

The Fed has a bearing overall because interest rates are directly the discount rate at which you will discount cash flows so that has an impact. Now also it depends on relative movements between countries so because the Fed tightened earlier that is why you saw the dollar strength this year. Now of course the Fed rates will, as is expected, it will continue to rise but at a slower pace but we are not at the peak of the Fed rate still.

I am quite clear about that that we are not close to the peak - it will continue to rise for a while. Of course with inflation there are many adjustments to be made like for example shelter inflation is high there but the proxy that is used for this is basically housing related inflation is a lag indicator and actual housing related cost are falling faster than what is captured in the CPI there but I am not banking on a quick pivot.

I still think India will be one of the outperforming markets. India, Canada, Mexico, Indonesia that is what we like. Also in the US we like non-tech more than tech because the higher interest rates basically hurt companies which have cash flows further out into the future so our systems now are liking more traditional businesses the cash flow consumer brands that kind of businesses than they used to.