RBI on way to catching up with reality, globally rate hikes will be an overhang on asset prices: Devina Mehra

Mehra expects India to outperform the global markets this year, continuing its outperformance of last year but the rally will likely be more selective

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Moments after the Reserve Bank of India hiked the policy rate by 50 basis points, Devina Mehra, Chairperson, First Global, spoke exclusively to Moneycontrol on the impact of the hike and key risks to markets.

With this hike, has policy caught up with reality?

Of course, the RBI has been behind the curve on rate hikes. It took too long to react to inflation. Wholesale Inflation (WPI) was at a 30-year high for FY22. Many Emerging Market central banks had been raising rates multiple times for over a year. Therefore, on the way to catching up with reality is the way I would put it.

The government also doing some fiscal side and policy tinkering to cool down inflation—the reduction in duties on fuel. Wheat export ban. Some restrictions on sugar exports. Likely to happen on cotton also.

Still overall inflation will be an overhang on household budgets and demand—coming as it does on top of business and job losses. This will impact GDP numbers as well demand for goods and services.

On balance, do you expect to see further correction in the markets in the coming days?

I do not see substantial immediate downside risk in the markets. I expect global markets, especially the US, to see a sharp rally at least in the short-term given the recent fall, especially the 40-90 percent crash in a large number in individual stocks.

While India did not fall to that extent, it is nevertheless likely to participate in the rally. I expect India to outperform the global markets this year, continuing its outperformance of last year—it was in the Top 10 global markets after something like a decade.

Of course, I do not expect an across-the-board rally the way it happened in 2021. This time the rally is likely to be more selective than was the case last year.

What could be the worst-case downside?

The outcomes in the real world are only a range of probabilities. At present, I don't see a huge downside at least in the next few months. The markets are in a range where you should consider selective buying.

And the worst case is always something you can't anticipate.

No one obviously anticipated COVID or its impact at the beginning of 2020. At the start of 2022, the Russia-Ukraine conflict didn't even make it to the top 10 risk areas globally.

The biggest risk to markets from here?

As far as the Indian economy is concerned, demand destruction is likely to continue, especially below the premium end with inflation taking big chunks off the household budgets.

This is already showing up in volume declines across areas from FMCG products to two-wheelers. The only industries/ niches doing well are those catering to the creamy layer from premium cars/ SUVs to high-end real estate.

Globally, the rate hikes will be an overhang on asset prices. I do not expect central banks, especially the Fed, to pay attention to asset markets till they manage to force down inflation and inflation expectations.

What changes in terms of equity strategy?

The thing to remember is that you cannot hope to catch the absolute bottom in any market. Our data shows that if you were invested for the last 40 years and missed out on just the best day of the year each year, over time your returns would come down by more than 70 percent!

Given where the market is currently, it will be prudent to start the reinvestment process or at best split it over a couple of months.

Do you see FII selling abate or accelerate in the coming month?

One, from the point of view of market movements I never like to track FII flows because over the long term or even on a month-to-month basis there never has been any correlation between market movements and FII flows. That is clearly borne out by data.

Having said that, we must also understand that the moves in FII flows are generally to do with broader trends rather than India-specific reasons.

After all, India is less than 3 percent of the world's market cap and is hardly central to the decision making by asset- allocators.

Hence, the move in foreign portfolio investments is driven by other factors generally speaking. Looking at them through the Indian lens is futile.