

This is a moment of reckoning for new investors, but no rate hike risk now: Devina Mehra

Synopsis

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have to be careful and as rates go up, that has a direct impact on the comparison with the earning yields. But I do not see a very big move, at least in India, for some time given all our growth concerns, says **Devina Mehra**, *Chairperson & MD, First Global*.

Markets have been keeping us on our toes after a grand September and early October. Now there is a bit of shakeout. How would you read into last week's price action?

I had said last time that while I did not think a great bear market was coming simply because 10-year rolling returns show the market is still below the trend line rather than well above the trend line, which is when you expect a big bear market to come. But then after this kind of runup, one expects some correction which also I had spoken about and that is what has happened and it has been very widespread.

I was looking at the data and last week only 20% of the stocks were in the positive and less than a third even outperformed the market. So two-thirds of the stocks were even below the index numbers fall. That has been quite a widespread carnage and more so in the midcap and small cap rather than in the large caps. This is a moment of reckoning probably for all the people who entered markets for the first time post the Covid lockdown and who have seen only good things up until now.

How real are the cost pressures? Do you think inflation is transitory like the central banks are saying or we could be staring at a definite change of stance and change of policy?

I do not think inflation is very transitory. Even before the results started coming out and people started talking about it, the cost pressures were clear and on all fronts -- oil, metals, agri commodities, which are inputs for many of the FMCG companies. I had seen this coming that there would be margin pressure so that the input suppliers do better and the users do not do as well, especially since on the demand side, there is still weakness that customers are without jobs or without a business and still struggling.

It is not that easy to pass on the price increases whether you are talking consumer durables or staples and as we had predicted early in the year, only the US can control inflation by managing the dollar, for the rest of the world, the pressures will be there.

A lot of emerging markets have been increasing rates. There have been markets where central banks have raised rates not just once but three, four, five times even - mostly in emerging markets. Within the developed world, there are still smaller ones and there have been pockets where there has been either raises or talk of raises like in some of the

smaller European markets, Australia, New Zealand, etc.

We all look only at the US to see whether they have raised rates or not. In India, I do not think we will raise rates in a hurry and that is my outlook.

In that case, could there be currency pressure, especially since rupee has been in a range for a long time? If you look at the history of the rupee, either it declines slowly every year or when it is range bound for a long time, the currency moves can be fairly sudden. It remains a risk area because India is lagging its peers on the rate side.

So what happens to this adjustment? If rates start firming up or if they are likely to move up in next coming months or quarters, do you see a situation where some of these so-called high quality stocks with PE multiples of 70, 80, even 100 times run the risk of price correction?

As I said, in India I do not see the rate hike risk right away and if there is a marginal increase, that does have an impact on the PE, but it is not quite so straightforward. But a different case can be made on whether something should be trading that high in the first place you always have to get that balance right.

Like last year, around that time, FMCGs were loved so much and people said you can buy at any price and you will make money on it. But that is never the case. In fact, at that time we had identified IT services as the counter trade which also has predictable earnings and which had decent margins and returns, It is not as high as the FMCG but still pretty good and it was also a dollar hedge and predictable. Yet the PEs were a fraction of the FMCG. We thought there was a relative re-rating right there and that played out.

So, one has to be super careful when you are buying very high PE stocks in any case. Which is why I said that investors who have not seen anything else, thought everything just keeps going up but unless you have a very specific case for that stock, you have to be careful and as rates go up, that has a direct impact on the comparison with the earning yields. But said I do not see a very big move, at least in India, for some time given all our growth concerns.