

ETMarkets Smart Talk- Double digit earnings growth! Indian market likely to outperform peers in 2023: Rakesh Parekh

Synopsis

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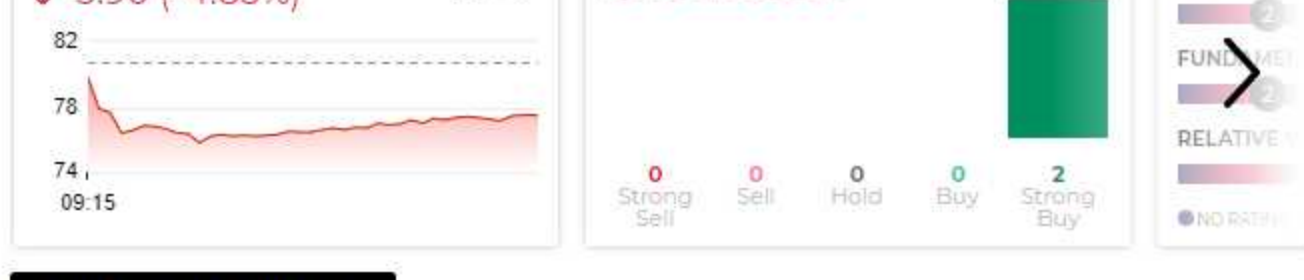
In these cases, we suggest investors should remain focused on the fundamental strengths and long-term structural opportunities of these businesses combined with realistic valuation perspectives to generate risk-adjusted Long-term returns.

"We are trading close to the last 5-year averages of around 20x forward P/E. Our expected earnings growth will be around 15% CAGR in the next two years, which is clearly on the upswing compared to the rest of the world," says Rakesh Parekh, MD and Co-Head, Portfolio Management Services, JM Financial Ltd.

In an interview with ETMarkets, Parekh said: "We expect India to continue to relatively outperform its peers during the remainder of CY2023 and possibly beyond" Edited excerpts:

We are seeing some nervousness at record highs for Mr Market. How do you see things moving – have we hit the top for the moment?

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It is true, that on absolute valuations, Indian markets have now crossed all-time highs, so we are at peak index level; hence, there is bound to be some nervousness amongst investors.

However, we are trading close to the last 5-year averages of around 20x forward P/E. Our expected earnings growth will be around 15% CAGR in the next two years, which is clearly on the upswing compared to the rest of the world.

Hence, we believe strong investor interest in India would remain high. As the run-up has been sharp since March 2023, especially for Mid & Small Cap names, we could also expect a breather in the short-term.

Nevertheless, we expect India to continue to relatively outperform its peers during the remainder of CY2023 and possibly beyond.

In case the US undergoes a stronger-than-expected recession, Indian markets would also come off, or we will have a time-wise correction. However, we do not expect it to be significant due to the stronger growth outlook in India.

Additionally, India is attracting an incrementally higher share of FPI flows and over time India's weightage in EM indices are expected to rise as India's growth outshines other markets.

We believe this would also continue to be a strong growth driver for Indian equities. FII Equity inflows since 1st April to date are around \$18bn US dollars alone.

(Source: Bloomberg, JM Financial)

Interestingly the US Fed is open for further rate hikes. Do you see that could dampen the bulls party on D-Street?

We believe markets have already priced in one more rate hike by the US FED for the remainder of 2023. The bullish sentiment across markets is on account of the resilience of the economic data with falling inflation, thus increasing the odds of the soft landing of the US economy.

The Indian economy and Corporate earnings have consistently remained resilient and have been outperforming expectations.

With cumulative monsoons having held up reasonably well until July-23, the odds of a rural recovery have improved substantially.

While it's natural that markets could consolidate after the strong run up since end-March, the broader sentiment should remain buoyant.

(Source: JM Financial)

Large Caps dominated the party on D-Street - do you think one should now look at going overweight on small & midcaps?

Indian earnings in our view would be dominated by Capex-related and Domestic facing sectors. These sectors will have much higher growth than the financial sector incrementally.

Intuitively these industries are represented largely by mid and smaller-cap oriented stocks and hence we believe as has been the case over the last 4 months -- mid and smaller-cap stocks could continue to outperform larger caps.

There was a phase in the last three years in which financials which are mostly large cap and account for over 30% weightage in the indices contributed to over 40% of earnings.

This was partly aided by the provisions which banks had made during Covid reducing and normalizing their earnings. During this time large caps had an upper hand over mid and small caps.

(Source: JM Financial)

How do you see the recent Corp announcement made by the house of Reliance Industries as well as M&M expanding their business empire in different fields?

Companies are thinking more Longer-term about how to enhance their business opportunities and growth prospects. Reliance, after expanding in the Retail & Telecom sectors, is now betting big on Green Energy & Financial Services.

It is imperative for Reliance to invest in green energy to reduce its dependence on the O2C business, investments in financial services is logical as it utilises their retail & digital presence and scales up the business in lending & fee-based areas aggressively.

In the case of M&M, since they already have a large NBFC, they may be looking at ways to enhance some cross-selling partnerships. For this reason, that could have been behind their decision to take a small investment in RBL Bank.

(Source: JM Financial)

Commodity prices have bounced back. Do you think it could lead to a spike in inflation?

Yes, it is the case that commodity prices have bounced back in the short term (last 1-2 months). However, commodity prices are inherently volatile and as long as they don't rise disruptively in a sustained manner, for e.g. oil prices move beyond \$100/bbl in a rapid space of time; we believe global inflationary pressures would remain contained.

Seasonal variations in food prices may also cause inflation readings in some months to flirt with the upper end of the comfort range of RBI; however, overall inflation should remain range bound in India.

(Source: Bloomberg, JM Financial)

What is your take on the earnings trajectory for the rest of 2023? What is your take on the management commentary? Does the consensus sound cautious just like the IT pack?

Earnings trajectory for the rest of 2023 should be decent given the macro backdrop, progress of rain, infrastructure building, revival of capex as well as rural & urban consumer demand.

Demand from the external facing sectors are subdued as reflected in IT services & Chemical sector performances so far, Healthcare and Pharma has started to improve though.

However, management remains cautiously optimistic about urban demand, also rural demand is slowly picking up as the impact of high inflation slowly subsides and rains have been plentiful in recent weeks across India.

Infra & industrial demand is buoyant as reflected in order inflows of many capex & industrial goods companies so far.

So far in the first quarter of the FY24 results period, domestic-focussed sectors such as Financials, Consumer, Industrials, Building Materials etc., have done significantly better than export-facing sectors and we believe these trends would continue for the remainder of FY24.

Management commentaries have also been encouraging in anticipation of a gradual pick-up in growth as we head into a General Election year in 2024.

Margin improvements have also been seen across many domestic facing sectors as raw material inflation has been contained.

From an IT sector perspective, a broad range of larger & mid-size IT stocks have already corrected substantially from peak valuations witnessed towards the end of 2021.

We believe caution is warranted as recent 1QFY24 results of major IT companies still highlight a continued slowdown in growth and the pace of new deal wins.

The outlook for the US economy also continues to remain uncertain at least for the remainder of 2023; therefore, in this scenario despite their softer valuations, it is unlikely IT stocks would outperform in the near future.

Things which investors should avoid doing especially when the market is trading at record highs?

There are certain investments/stocks which have become very expensive, or where the business fundamentals & outlook continue to remain weak.

Additionally, at times like this when hope is running high, fundamentals can have lesser resonance than the "story". Investor expectations can become unrealistic, especially in sectors that are more thematic in nature and could have a very long gestation period for generating meaningful returns, e.g. Fin-Tech, Clean-Tech, Green Energy, etc.,

It is then paramount in these situations to have a very clear fundamental framework and process in place to maintain discipline toward stock selection.

In these cases, we suggest investors should remain focused on the fundamental strengths and long-term structural opportunities of these businesses combined with realistic valuation perspectives to generate risk-adjusted Long-term returns.

(Disclaimer: Recommendations, suggestions, views, and opinions given by experts are their own. These do not represent the views of the Economic Times)