

Current risk-reward unfavourable; interest rates could be higher for longer: Asit Bhandarkar of JM Financial AMC

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Mid-cap stocks in India have surged over 30 per cent in the past year due to a P/E re-rating. While caution is advised in the short term, long-term growth potential remains optimistic due to infrastructure upgrades and consumption trends.



Asit Bhandarkar
Senior Fund Manager – Equity,
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Asit Bhandarkar, Senior Fund Manager – Equity at JM Financial Asset Management (Mint)

In an interview with Mint, **Asit Bhandarkar**, Senior Fund Manager – Equity at **JM Financial Asset Management** pointed out that over the past year, mid-cap stocks have surged more than 30 per cent, mainly due to a P/E re-rating.

He advised caution in the short term due to rapid price and valuation increases, global challenges, and pre-election volatility, but remain optimistic about India's long-term growth potential driven by infrastructure upgrades and consumption trends.

Edited excerpts:

What is your assessment of the current market conditions? Are we in a long bull phase?

We have seen a sharp up move in excess of 30 per cent in the mid-caps versus nearly 20 per cent for large caps in the last 12 months. Data suggests that a significant portion of this return has come from P/E (price-to-earnings ratio) re-rating.

At JM Financial Mutual Fund, we draw more comfort from earnings-driven stock price appreciation. The impact of transient factors such as geopolitics, risk aversion, capital flows and excessive liquidity, then, gets mitigated.

Given the rather rapid rise in prices and valuations, we believe the market needs some time to digest the new prices in the context of the global macro challenges and likely pre-election volatility and some caution may be warranted in the short term.

Longer term, we are very excited about the growth prospects for the Indian economy.

Over the next decade, we expect a rapid rise in the stature of the Indian economy and businesses amidst the global peers driven by massive infrastructure upgrades and improving consumption trends.

Are we out of the woods? US inflation is still high above the Fed target. In India, we have the risk of El Nino and poor monsoon. Can the market get a rude shock in the next 4-6 months?

Markets are on a tear globally, while cheering the trend of lower inflation in the USA and India as well. Partial credit for the inflation readings goes to a higher year-on-year base.

Data on employment, housing starts, rental housing, industrial production, energy consumption, etc. have been noisy and it is difficult to forecast any trend forward.

Only in the second half of the fiscal will we have more clarity on whether the inflation genie has been safely bottled or not.

India faces volatility due to not only monsoons but an election as well as we get in the second half of the financial year 2024 (H2FY24).

With higher valuations, the current risk-reward appears more unfavourable than in the past.

How do you see the Q1FY24 earnings of India Inc. so far? Could you please highlight some of the positive and negative surprises?

It's too early to comment on Q1FY24 earnings as the bulk of the results have yet to come. While momentum in the economy is strong, it is also true that expectations are too high.

We are looking at tempering high expectations all across as we go through this result season and the expectations to get more realistic into H2FY24.

More than absolute disappointments, it could be a case of markets being disappointed by the lack of significant upside given the rich valuations.

The financial and auto sectors have recently witnessed a strong inflow of foreign funds. What is your view on these sectors?

We are positive on the financials given the pick-up in credit growth along with improving asset quality cycle which is likely to sustain over the next couple of years.

We do see high competition from fintech and hence companies with higher tech edge could grow at a higher pace.

Autos have seen a good run as the 'SUV-fication' and 'electrification' continues. Margins are seeing dual tailwinds of strong pricing driven by healthy order books and raw material price reduction.

We do see a technology challenge where market caps may move to companies, which hold promise in EV or other green energy-capable technologies.

If one has to buy now, what sectors would you recommend to bet on for the next one-two years? Why are you bullish on those sectors?

We are seeing a strong possibility of a resumption of a capex cycle driven by low investments over the last decade and increasing utilisation rates currently. Banking and autos also appear to be favourable. Rural recovery may bring interest back in staples.

When do you expect the Fed and the RBI to start cutting rates?

We are seeing inflation reducing month on month due to the effect of higher interest rates and a higher base last year. We would think that a substantial part of the rate hike cycle is behind us globally.

However, for rates to reduce, there may be more evidence required of a sustained reduction in the inflationary outlook.

Currently, we are inclined to believe that interest rates could be higher for longer as the inflationary trends appear sticky globally.

The reason why we remain sanguine on interest rate hikes, is that some tremors are already being felt in the private debt market, mid-sized banks, and housing.

These issues may become entrenched creating more problems than inflation itself, and hence we believe that central banks will be more cautious in interest rate hikes from here on.

Higher interest rates may dissuade corporates from investing which is what developed economies want and also reduce investments in much-required housing and infrastructure. So, we are at an interesting crossroads here and need to watch central bank actions carefully.

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