Daily Voice | Recovery unlikely to be swift, prepare for more volatility in near term, says Nikhil Chandak of JM Financial

The reopening theme is one space that has outperformed. There is a COVID and lockdown fatigue in India and globally. So, companies in segments like hotels, multiplexes, travel, etc have the benefit of a huge pent-up demand, says Chandak

SUNIL SHANKAR MATKAR

MARCH 14, 2022 / 08:38 AM IST

Nikhil Chandak, MD & Head Investments, JM Financial, thinks it is better to have a Test mindset than a T20 one in these volatile times. If one can take a medium-term view, a crisis is the best time to buy “resilient bluechips”, he says.

A chartered accountant by training, Chandak has more than 21 years of experience across companies like Arthur Andersen, E&Y, Kotak, Landmark Group Family Office (Dubai) and JM Financial.

Chandak tells Moneycontrol in an interview that he expects the market to remain volatile in the very near term, with pricey commodities, inflation and rising interest rates weighing on sentiment in a risk-off environment. Edited excerpts:

Do you expect a quick recovery once Russia-Ukraine hostilities ease?

The key issue for the global economy currently is the significant spike in commodity prices across the board, leading to higher inflation and resultantly, higher interest rates.

RELATED STORIES

Nikhil Chandak

MD & HEAD INVESTMENTS|JM FINANCIAL

Russia is a significant global player in commodities like oil and gas, metals and agri commodities. Even if the war between Russia and Ukraine stops, it is unlikely that the sanctions imposed on Russia would be reversed anytime soon, which will keep global commodity prices elevated.

It's an uncertain economic environment and the recovery is unlikely to be swift. The world is already battling a high inflation scenario and with these geopolitical concerns, we have to be prepared for more volatility in the markets in the near term.

Also read: Government has till May 12 to float LIC issue without fresh Sebi nod

Several sectors will feel the pain of rising oil prices. Should one stay away from these sectors or is it time to buy?

It depends completely on the investment horizon of the investor. If one is a short-term investor, with a view, for example, of six-12 months, one should stay away from sectors negatively impacted by high commodity prices.

With India importing close to 85 percent of its crude oil requirements, oil prices in excess of $100 a barrel will lead to higher inflation across the economy and negatively impact both end consumer demand and corporate sector margins.

However, if one has the bandwidth of taking a medium-term view of say three-five years, then a crisis is the best time to buy into resilient blue chips. But unlike the broad-based rally in the last two years, picking the right companies which can gain market share and protect margins will be critical, going forward.

Analysts are worried that the oil shock could disrupt the credit cycle. What is your view?

After a tepid credit growth in low single digits in the last few years, credit growth was poised to pick up in the post-COVID phase. So, in a way, the oil price shock couldn't have come at a worse time for India. If oil and other commodity prices continue to stay elevated for a long time, there is a risk of persistently high inflation in the economy, forcing the RBI to hike interest rates, which can impact the end-demand. Commodity prices become a very important monitorable going forward.

Also read: FPI selling continues for 6th straight month; net outflows at Rs 45,608 crore in March so far

Are we moving towards a bear market?

We may not be in a full-blown bear market yet but, on the whole, in the very near term, the market has more headwinds than tailwinds.

Valuations before the war and before the first signs of the Fed tightening were clearly elevated, both globally and in India, and the markets needed an excuse for a healthy correction.

In the very near term, there are multiple issues the market has to grapple with including high commodity prices, inflation, rising interest rates and pressure on foreign flows due to a general risk-off environment. More volatility is on the cards.

Is India still a highly valued market even though foreign institutional investors continue to sell?

While valuations are on the whole a lot more reasonable than they were a few months back, one has to evaluate each sector in detail to get comfort on how resilient earnings will be for the next few quarters.

For example, valuations are still elevated in sectors like consumer staples but have corrected in sectors like private financials. We also have to brace ourselves for earnings downgrades in sectors which get impacted by high commodity prices.

Also read: Morgan Stanley cuts India's GDP growth forecast to 7.9% for FY23

In the current market, which are your three best bets in terms of sectors?

Good sectors to be in include private financials due to reasonable valuations and given the fact that the worst of the asset quality pressure is behind us, the IT services space, which continues to see strong demand tailwinds and has companies with high free cash flow generation, and also stocks benefitting from revival in the housing space.

Also read: Explained: How will crypto taxation work in India?

Which is the one space that has seen less pain than others and why?

The reopening theme is one space that has outperformed in the current market correction. There has been a COVID and lockdown fatigue in India and globally. So, companies in segments like hotels, multiplexes, travel, etc have the benefit of a huge pent-up demand from consumers. This space should see strong earnings growth for the next couple of years and hence has held up well in the current turmoil.

History suggests that war never hurts equity markets in the medium to long term and corporate earnings and economic growth are market drivers. What do you think?

Of course, history over several years has shown that in the longer run, one of the key drivers for the markets is earnings growth. Whenever the geopolitical situation normalises, the focus will once again boil down to the companies that have the best earnings outlook.

The key is to identify and invest in those sectors and companies in these tough times and especially at a time when valuations get more reasonable, so that one can reap the benefit once the situation normalises.