

Creating alpha in current market more challenging: JM Financial AMC's Satish Ramanathan

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Satish Ramanathan, CIO – equity, JM Financial AMC

The Indian market has re-rated and while it is trading at a much higher PE than the historical averages, funds are ready to bet on quality companies even though creating an alpha in the current market has become challenging, said Satish Ramanathan, CIO – equity, JM Financial AMC.

He added that while they recognize that the market is at a higher PE than a few years ago, and that they would prefer lower valuations, they are willing to pay a premium for quality leadership.

“We continuously monitor valuations and aim to invest in higher-quality names at reasonable prices, even if that means paying slightly more for market leaders,” said Ramanathan.

“In the renewable space, while some areas are overvalued, there are still opportunities to find companies that aren't expensive and yet can play a significant role in the same theme or sector. It's about balancing quality with price and ensuring we don't overpay for growth,” added Ramanathan.

On the all-important point of creating alpha — defined as returns over and above the benchmarks — in the current market, the fund manager said that it has become challenging as the markets have re-rated.

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Going forward as sector and stock rotations will be more frequent, and being on the wrong side of these rotations can lead to underperformance, the margin for error is narrow, and fund managers need to be agile, he said.

Meanwhile, explaining the rationale for his large portfolio allocation to capital goods and energy, he said that they anticipate that the economy will experience growth through infrastructure capacity building and modernisation.

Even on the energy side, he notes that most of our current energy comes from thermal sources, which are polluting the environment.

“To transition to a cleaner economy with lower carbon emissions, there will be a significant need for investments in new types of energy creation, transmission, and consumption. This is why our capex and energy themes are closely aligned,” said Ramanathan.

On his strategy for managing market volatility

The fund house, Ramanathan explains, actively monitors the portfolio's beta, keeping it below one to ensure lower volatility than the market.

“Additionally, we continuously assess the cash flows of businesses, adjusting our allocations to sectors like healthcare, pharma, and consumption, while reducing exposure to more expensive sectors,” explains Ramanathan.

On the large cap versus small- and mid-cap debate

Ramanathan adds that they don't strictly favour large caps or small caps. “Large caps are preferable in businesses where cost of capital and execution speed are crucial, while mid- and small-caps excel in building new businesses and growing faster. We prefer a flexi-cap approach, allowing us to adjust the mix based on opportunities,” he said.

On participating in QIPs of PSU banks

While there has been a surge in QIPs from public sector banks, Ramanathan notes that the journey of PSU banks has been remarkable.

“They have managed to reduce their non-performing assets and have also made strides in adopting new technology platforms. However, we are still cautious and prefer to wait and observe their sustainable growth strategies before making significant investments,” he explained, adding that their preference currently leans towards private banks and NBFCs with strong corporate backing rather than retail-focused banks.

Finding opportunities in platform companies

Ramanathan says that they are looking beyond traditional consumption sectors like FMCG and are focusing on modern platforms and newer consumption avenues that offer higher growth potential, such as online retailers.

Platform companies, he said, are redefining businesses as they are not bound by legacy and don't have physical assets. “Their profit growth can be non-linear once they cross the initial growth phase,” he says.

Ever evolving strategy

The mutual fund industry, Ramanathan said, has undergone significant changes in recent years with sustained growth contributed by both large and small fund houses.

“The industry itself is growing well,” he said, adding that there was a stage when the large fund houses were becoming larger and capturing greater market share. “I think investors have now realised that it's necessary to have a good blend between large funds and smaller paths as well, and that's given a breath of new life to the smaller fund houses.”

On his investment strategy, Ramanathan admits that earlier as an analyst he was much more focused on numbers. But over time, the softer touch and feel of companies and their managements have become far more important than the actual numbers themselves.

The shift in his approach has led him to place greater emphasis on management quality. “The numbers are a reflection of superior management. So that, I think, is the learning curve that I have had over the years as an individual - that you bet on finding the management delivering superior performance rather than just the numbers,” he said.

Longer-term growth, he adds, is actually done if you are efficient on a capital allocation basis. “We see many companies deviating from the path of becoming capital efficient and taking some capital-inefficient decisions,” he cautioned adding that is when you actually need to course-correct your portfolio.

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