

'Many mid- and small-caps in euphoric zone, poised for correction'

After a sharp rally in 2017, the markets are now banking on a normal monsoon. Any disappointment on this can be a negative, says **SUNIL SINGHANIA**, chief investment officer – equity investments at Reliance Mutual Fund, in a conversation with Puneet Wadhwa. Excerpts:



SUNIL SINGHANIA

Chief investment officer, equity investments at Reliance Mutual Fund

Are markets factoring in the likely disruption to the economy and earnings from the goods and services tax (GST) implementation?

The GST rates are more or less in line with expectations. The government has ensured minimum deviation from the existing rates. In every country where GST has been implemented, there were challenges for one-two quarters. In India, too, this is expected. But over the medium-to long-term, there is no doubt that GST is a most awaited reform and can add almost one percentage to GDP (gross domestic product) growth.

Your takeaways from the March quarter earnings?

The earnings season has been a mixed bag. Earnings of auto, metals, and oil and gas companies have surprised positively. While results of information technology companies were in line, Hindustan Unilever's numbers came in as a bit of a surprise. Banks, on the other hand, have been mixed, with the larger ones being in line with estimates.

Are the markets being over-optimistic on the likely growth in earnings?

After a long time, the yearly earnings growth overall for Nifty stocks is trending in double digits. We expect it to pick up (15-18 per cent growth in FY18 and FY19), led by a good monsoon, huge government expenditure, better demand, low interest rates and recovery in GDP growth rates. Our belief is the economy will double to \$4 trillion in the next six to eight years. Thus, we will create nearly \$2 trillion of additional wealth over the next six to eight years, equivalent to what we have created over the past 70 years.

Key risks to the rally and your market outlook for the next 12 months?

The markets are trading slightly above long-term trend rates. However, many mid- and small-caps are trading much beyond their fair valuation, and maybe even in the euphoric zone. This can lead to some correction. Having said that, the markets are banking on a normal monsoon. So, any disappointment there might be a negative. Crude oil prices look weak but any surge beyond \$65 a

barrel can be a negative. And, geopolitical concerns anywhere in the world, particularly with Pakistan, can be a concern. However, in the past we have seen such events are the best time to invest; eventually, the markets recover.

In which sectors do you find valuation comfort?

We continue to be positive on private sector financials. We are also positive on niche financials like insurance companies. That apart, we are overweight on the capital goods, engineering, cement and consumer discretionary sectors.

Your assessment of the measures for the banking and infra sectors?

Infrastructure, including housing, has huge potential and the government focus and push can only improve that. However, as an investor, one has to be careful and analyse the fundamentals of individual companies before making a big bet only because the theme is interesting. Banking, again, has great potential and it is a sector where growth can be structural over a long period of time.

Concerns regarding the health of public sector banks (PSBs) have resurfaced. What's your view?

The larger PSBs are still okay. It is the

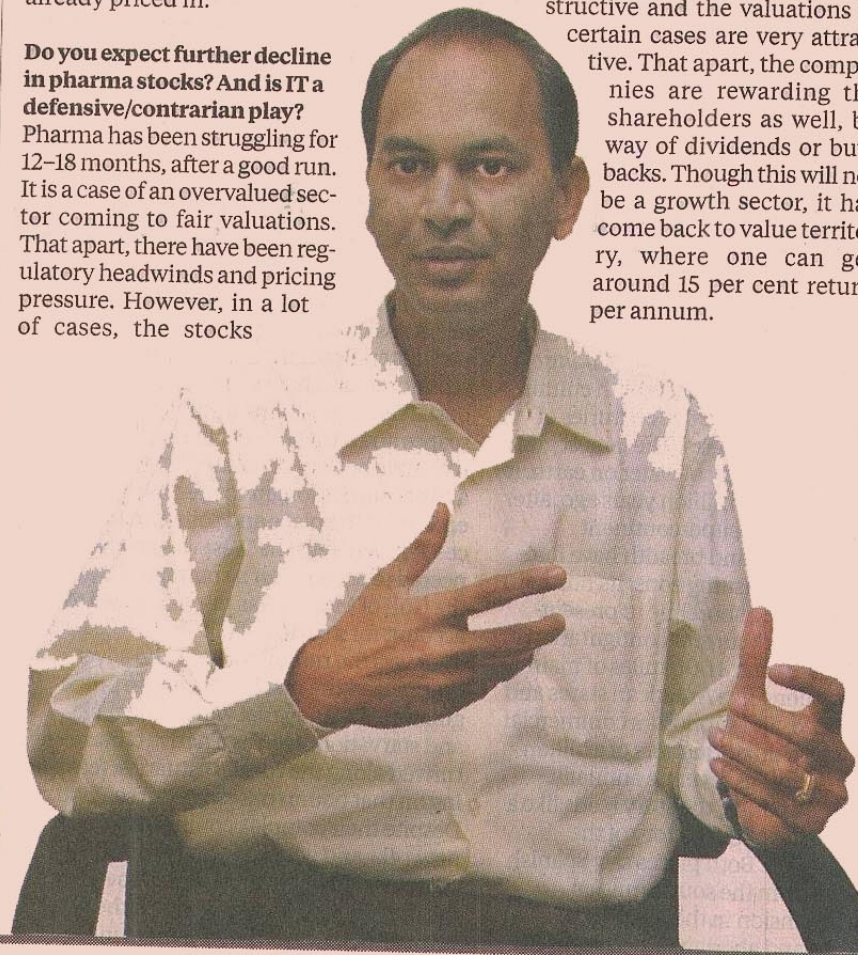
smaller banks that are still under pressure, as they don't have the balance sheet to withstand huge losses. In such cases, they will have to raise capital. Though non-performing assets are an issue, most of the negative news is already priced in.

Do you expect further decline in pharma stocks? And is IT a defensive/contrarian play?

Pharma has been struggling for 12-18 months, after a good run. It is a case of an overvalued sector coming to fair valuations. That apart, there have been regulatory headwinds and pricing pressure. However, in a lot of cases, the stocks

have reacted very sharply. The sector is worth tracking at these levels, though we are not overweight on it now.

On the other hand, growth in the information technology sector has been slow. Despite this, we remain constructive and the valuations in certain cases are very attractive. That apart, the companies are rewarding the shareholders as well, by way of dividends or buy-backs. Though this will not be a growth sector, it has come back to value territory, where one can get around 15 per cent return per annum.



AFTER A LONG TIME, ANNUAL EARNINGS GROWTH FOR NIFTY STOCKS IS TRENDING IN DOUBLE DIGITS. WE EXPECT IT TO PICK UP TO 15-18 PER CENT IN FY18 AND FY19, LED BY A GOOD MONSOON, HUGE GOVERNMENT EXPENDITURE, BETTER DEMAND, LOW INTEREST RATES AND RECOVERY IN GDP GROWTH