4 sectors where stocks may double in 3 yrs: Aishvarya Dadheech

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"India will continue to remain a very attractive investment destination. The FIIs who have turned around will possibly continue this trend of investments into this country. The resilience of the Indian market is here to stay," says ***Aishvarya Dadheech****, Director & Fund Manager,* ***Ambit Asset Management***

How is your portfolio doing?
I think the time for us has been really nice. We are happy that the resilience of India's market is playing out and especially in the broader markets. In the last month or so, in spite of all the volatility that we have witnessed globally, somehow the broader market in India is showing very strong resilience, possibly supported by earning growth. The whole slowdown story in the US or possibly the drawdown story in Europe and even China being going slow on the growth pedal, will lead to India being seen as a completely different animal, growing 6-7% and possibly the biggest contributor would be the higher earnings growth.

This resilience is showing that the market is possibly much ahead of what Fed or the commentary have been. We have seen that Fed is trying to get back some of its lost credibility by announcing whatever they had to last week but a lot of these risk-off sentiments, whether the dollar index or possibly the US 10-year hasn't moved much post that commentary.

We are concerned about global recession and high oil prices, but that is not showing too much volatility and India reported very strong growth last quarter and is possibly poised to see really strong growth in FY23. I think India will continue to remain a very attractive investment destination. The FIIs who have turned around will possibly continue this trend of investments into this country.

We believe resilience is here to stay. It is very surprising, it has never happened in the past. In the last 15-20 years, whenever Fed has raised rates or whenever risk-off sentiment has prevailed, India has been impacted the most. This time, things are really looking different and that is what the resilience is about.

Can name some good stocks or themes which you have added in the last three-four months? What are the triggers and earnings potential of those themes?

We have been very heavy on banking space. We believe that even the midsized banks or the midsized NBFCs will start participating now. In the last quarter, our credit growth was almost at 15% though the deposit growth was slacking at almost 9.8%. But the trajectory looks very promising.

I believe the BFSI segment will continue to do really really well but what catches our eye and the recent investments that we have done is more into API or chemical companies because in Europe, capacities are shutting down, especially on ammonia nitrite phosphate. We believe a lot of these chemical companies and even API intermediate companies should do really well.

We believe
Suven Pharma
,
Neogen Chemicals
,
PI Industries
and
Aarti Industries
have shown a strong resilient margin last quarter and the demand growth for the next couple of quarters looks very attractive.We believe that these kinds of companies should do really really well.

Another area which we do not invest in because that does not clear our stringent investment filter requirement but which we believe possibly would do really well is the capex story. The capex outlook is the highest in the last 8-10 years. If you look at the order book of a lot of EPC companies and even the order book of Larsen & Toubro, that clearly says that the trend is picking up.

I would believe that private capex is a theme which one can look at for the next couple of years. So, that is one segment. Even most of this FII money when they have turned around will initially buying more of this capex theme. Capex could be an area which looks very attractive from the current scheme of things because there are certain areas which from a macroeconomic perspective were lacking. One was credit growth. Six-seven months back, rural demand was another one; capex story on the private side was not picking up; inflation was a problem. Now, we are seeing a turnaround happening in this area. Credit demand is showing very good resilience, capex activities are picking up.

Initially we were witnessing only capex announcements in chemicals, pharma or some consumer discretionary names but in the last three-four weeks, we have heard a lot of big announcements happening and both central and state capex spending will continue. That is why we believe capex intensity will pick. These are some of the sectors or segments which look very interesting to us.

Out of all of these things, where is the high conviction on earnings? Which is the basket because where in the next two-three years, one can expect around 25% earnings growth because that is where the stock will double in three years?
We are in that camp which believes stock prices are slave to earnings and we invest with the thesis that earnings can go to double in the next three-three and a half years and stock prices obviously will follow that. We believe that consumer discretionary is one part which possibly will be able to see an earnings growth of north of 20%.

I personally believe that this will be one of the best festive seasons that we have recently seen and that trend is going to continue. Similarly, a lot of these chemicals and API pharma companies should be able to manage 20%-25% earnings growth. Mid-sized banks and NBFC is one category which also looks very attractive.

A lot of those companies are trading at even less than price to book or at times 1.1-1.2 times price to book. For them, 20% growth is very doable because they do not have to bother about credit costs. Obviously there has been certain opex which has hit the results in the last couple of quarters but over the next six-eight quarters, that will normalise and will eventually help them to grow 20% or more.

So that is one of the segments which should do well apart from consumer discretionary and capex. Building materials should be able to show us 12-15% kind of revenue growth and we will be able to manage the margin. They should also be able to do almost 20% growth. So players like

Kajaria Ceramics
or Astral should be able to do more than 20% growth.

What are the risks in this market? Is valuation a risk in certain pockets or is it early to say that valuations have got stretched?
One has to look both from domestic as well as the global side. More than the interest rate hike, what worries me is the quantitative tightening. We are sitting at almost $9 trillion

on the Fed balance sheet. The quantitative tightening so far was supposed to happen at $47 billion a month. It is happening at less than $20 billion. So far we have done not more than $100 billion and if the quantitative tightening takes place, it will possibly have a negative impact on the global equity markets.

Second, one of the biggest assumptions of our bullish case scenario is a very strong earnings growth. If you look at the various macroeconomic indicators – whether it is tax collection, GST, PMI and even rural demand side, good monsoon indicates that India should be able to do almost 7% kind of a growth and 12-13% EPS growth. If that takes a back seat for whatever reason, the market can possibly see a correction there, but if I look at it from a valuation perspective, Nifty 50 is trading close to around 20 times one year forward, which is more or less in line with the long term average.

So, markets are not cheap but there are pockets where we have a lot of opportunity. Even though the midcaps are trading in line with the Nifty 50 market valuations, one has to choose the right sector where one can see that kind of a strong growth and businesses which can protect their margin in an inflationary environment, businesses which are not levered and in a rising interest rate situation, they do not have to worry much about their EPS being cut. One can also look at businesses which will be the beneficiary of the formalisation theme.
I think there are a lot many names available which will be able to not only report those 20% plus earnings but also fit into that category. Given that valuations are not very cheap, one has to be really sure where they are putting their money.

Can you give us some feedback on investor sentiment? You along with your team would be meeting HNIs as part of your fund management efforts. Are people adequately invested? Have they raised their equity allocations in the last one year? Are they looking at buying the dips like the one that happened yesterday?
We have been meeting investors all through the time when the FIIs were selling and everybody was in a wait-and-watch mode. I would say there would be only a handful of investors who were more disciplined, who continued to participate, but a large part of investors' fraternity, especially the family offices or the HNI ones were waiting for deeper cuts post the war and the inflationary environment and all that and majority of them were surprised to see it moving up almost 15-17% in no time.

That is why we always say that the time in the market is more important than timing the market. But now in the last one month also, we have seen heightened interaction where they are trying to chase us and ask us what to do next, where to invest etc.

We believe that a lot of people are sitting with a good pile of cash on the sidelines for the market to correct. That is why we believe the market has turned from sell on rise earlier to buy on dips now and that is what is supporting the market. Another thing is that interest for the majority of the HNIs and high family offices are more towards the broader market because the broader market is showing very uncanny resilience given the discussions we were having earlier.

So, that is a high area of interest. I would say there are also certain investors who have been pretty disciplined and who have been investing at every dip into the market and I think they are very happy at this current juncture.

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(Originally published on Aug 30, 2022, 04:04 PM IST)
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