Market seems to be ignoring a possible recession in FY21: Sampath Reddy

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India has been one of the most attractive markets for FPIs due to good growth and better return on capital employed (ROCE) as compared to emerging market peers, says **SAMPATH REDDY**, chief investment officer at Bajaj Allianz Life in an interview with **Swati Verma**. If the economic recovery continues to gather momentum and does better-than-expected, Reddy expects stocks from the capital goods sector to outperform. Edited excerpts:

How long will the markets continue to ignore the reality of economic contraction in India?

The market seems to be ignoring a possible recession in FY21 and is factoring in a quicker recovery. We have seen a healthy recovery in high-frequency economic indicators since the economy started opening-up, although it remains to be seen if the momentum continues going forward and is not due to pent-up demand.

Another factor that has primarily contributed to the market rally is strong global liquidity, which has been fueled by the large monetary/fiscal stimulus around the world. They are also anticipating an improvement in corporate earnings from Q2FY21 onwards and progress on vaccine trials has also contributed to positive sentiment and buoyancy in markets.

Foreign portfolio investors (FPIs) have invested over Rs 47,000 crore so far in August. Do you expect the trend to continue?

India has been one of the attractive markets for FPI investments due to good growth and better return on capital employed as compared to emerging market peers. Given the healthy long-term fundamentals for India, we may continue to see strong FPI equity flows over the years, even though at times some of the risk-off events may lead to moderation in the pace/quantum for a short period. Some of the factors that will decide the trend of FPI flows into India will be the monetary policy stance of global central banks, geopolitical tensions, the pace of economic recovery, and if the second wave in Covid cases happens.

How do you view Q1FY21 earnings?

Given the muted expectations for Q1 FY21 corporate earnings due to the stringent lockdown for most of the quarter, the market has not been paying much attention to the Q1 earnings. However, the commentary from the corporate sector has been encouraging, with many companies quickly adapting to the work-from-home (WFH) method wherever possible, and have also taken cost-cutting initiatives. Most companies have also been focusing on conserving capital, and have raised liquidity levels. Overall, the commentary is positive and companies have taken many steps to tide over the slowdown.

Information technology (IT) and pharma stocks have given healthy returns this year. Do you see more upside in these stocks?

We have been positive on both the IT and pharma sectors. Given the cash-rich balance sheet, high return on equity (RoE), and attractive valuation multiples, the IT sector is likely to be better placed in the current uncertain environment. The pharma sector is coming out of the long down cycle, led by easing of pricing pressure for generics in the US market. Further, the companies have shifted the focus to profitable domestic pharmaceutical market along with exports. Cost rationalisation, especially on research and development expenditure, on fewer complex generics have also been adding to recovery in the profitability of the pharma companies. Also, the clearance of plants by the US FDA will support earnings for the sector, which was a concern earlier.

Which other sectors are you bullish on?.

Apart from IT and pharma, we are positive on fast-moving consumer goods (FMCG). The sector may do well selectively as demand remains strong, even though valuations are elevated in the sector. We are also positive on telecom where average revenue per user (ARPU) has bottomed out and the sector will benefit from increased digital adoption. Select stocks in agriculture/rural space have been resilient to the pandemic and should continue to do well.

One sector/theme that can emerge as a dark horse this year?

If the economic recovery continues to gather momentum and does better than expected, then stocks of capital goods companies may outperform. The utilities sector has also been trading at attractive valuations. Capital goods sector has been an underperformer this year due to the economic slowdown, and especially the slowdown in investments. Valuations are relatively attractive within this space. The government's focus has been on infrastructure, and it earlier had announced a large outlay of Rs 110 trillion under the National Infrastructure Pipeline (NIP) over the next five years. For the recovery of the economy, public/government expenditure or investment is quite critical in the initial phase, and when the economy gathers momentum, then private investment starts to pick-up—which will benefit the sector.