



Issue 11 – Markets can jump 10-15% if consolidation happens now.

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Sanjay Sinha. CEO, L&T Mutual Fund

The past three days have been acting as dampeners to the fantastic September series. But Sanjay Sinha chief executive officer of L&T Mutual Fund feels there is more headroom to this market. "The sheer force of liquidity will continue coming into the markets. And, it would take something extremely unexpected to stop the bourses from crossing the previous high. There is room for 10-15% upmove in the markets from the current level."

However in an interview with CNBC-TV18's Udayan Mukherjee and Sonia Shenoy, Sinha cautions that if the rally is only because of liquidity, then it's a steroid injection which is going to take the markets high and then leave it high and dry. "But, if we are able to consolidate at 20,000 plus/minus 1000-2000 points for about three months or so, the valuation which today look stretched, would start looking a little more affordable. So it's important for the market to consolidate at the current levels and not just keep heading up. Here is the verbatim transcript of Sanjay Sinha's interview with Udayan Mukherjee and Sonia Shenoy on CNBC-TV18. Also watch the accompanying video.

**Q: What is your sense is there more headroom to this market?**

A: I think there is going by the sheer force of liquidity that has been coming into the markets. It would take something very unexpected to stop it from crossing the previous high.

**Q: What kind of retail participation are you seeing? Has it scaled up or is there still some bit of caution that exists at the retail level?**

A: If you look at the behaviour of the domestic investors, they have been either cautious or have kept out form the market for most parts of the rally that we have seen. That also gets reflected in the broader secondary market also because if you look at the put-call ratio in the market that is tilting very much on the side of people having bought puts rather than having bought calls. When you look at the mutual fund (MF) industry, the fact that the industry is sitting on current asset base of equity of about Rs 2.5 trillion, I think there has been a strong temptation to book profits once we have revisited the previous peaks.

**Q: What is your fundamental take on the market now? Are you worried about valuations or do you think the market deserves to be here or even a bit higher from here led by earnings and fundamentals liquidity aside?**

A: I think valuations are also a function of time. We have seen that compared to January of 2008, seven quarters have passed in which the companies' earnings have gone up. So on a like to like comparisons, the valuations at the current levels are not the same as what it was in January 2008. But at the same time are we now in an extremely cheap or affordable territory as far as valuation goes?—I think that cannot be defended. We are now in fair valuation range, probably tipping on the side of touching the upper end of the fair valuation range.

But what is important at this point of time is to see as to whether these valuations and the current market levels can be sustained for a period of time. If the rally in the market is only because of liquidity and it's a steroid injection which is going to take to a high and after that leave it high and dry, I think then there is a reason for us to be worried. But if we are able to consolidate at 20,000 plus minus 1,000-2,000 points for about three months or so the valuation, which today look stretched on the side of coming on the border line of expensive, would therefore with passing of every quarter start looking a little more affordable. I would say it's important for the market to consolidate at the current levels and not just keep heading up to levels

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which would be 10-15% above the current levels.

**Q: So how should one tactically approach the portfolio then in a market like this? Do you think booking out of sectors that have already given you significant benefits is the prudent thing to do or do you think staying invested is what one should stick to?**

A: As an asset class, equity still has steam and therefore there is reason to remain invested in equity. The only thing that we need to do is first change our horizon of investment. If you are looking at short-term return from equity, I think that might be slightly risky given the fact that the larger part of the rally is attributable to liquidity and we do not know as to whether the liquidity is going to stay with us for the next fortnight, next month or next quarter. We have a call, which is slightly longer. Equity would be a promising asset class to be there. But given the fact that the rally has been unequal across sectors in the last one year and therefore there is reason to revisit the relative valuation across sectors, I think calls for a sectoral reallocation. Some of the sectors which have not participated in the rally in the last one year or have probably not been keeping pace with the market, given the new emerging realities and the changing dynamics of the industries would call for reallocation across sectors.

**Q: Do you expect a meaningful correction at any point between now and the end of the year now and if yes, what could be the trigger for that correction aside of mapping liquidity and trying to figure out what might dry it out? Is there any other trigger that you see for inducing a reasonable correction to the market?**

A: I think apart from liquidity one of the other facts, which has kept the confidence in the markets alive, has been the global feel good factor as far as equity markets are concerned. Even if you look at the way Dow behaved yesterday—the statistical numbers were not good yet the Dow has closed in positive territory. There is a general risk appetite, which has gone up and if that appetite is not going to recede, then that would be one of the factors which would provide stability to the markets.

But what can also act as road blocks, not strictly road blocks, but something in the nature of probably causing retracement would, in my opinion, be quarterly performances which would fall far below expectations and we have seen that happen in other quarters also. Some of the sectoral leaders when they give you unexpected surprises then that becomes a ground for the markets to correct. In this quarter, I am not sure that that will play out exactly because the larger force which has kept the markets going has been the foreign portfolio money and therefore they may not necessarily react to individual companies' performance. But if that force is not going to be the primary driver and you also get the local participation who are keeping a much closer track of companies and sectors, then these disappointments could be one of the reasons which could cause the market to retrace.

**Q: The midcap end of trade has really opened up in many pockets' of value would you up your exposure in the midcap end and perhaps cut down on large caps?**

A: Midcaps have seen one phase of value discovery in the last quarter itself and therefore in the month of September, if you have seen the behaviour of indices, while the largecap index went up by close to about 11% the midcap index went up by just about 5-5.5%, which means, because the participation in the midcap segment is far more from the local participants, you will see that this skepticism as long as its there in the local participants, the midcaps may not rally as much as they have done in the last three-six or nine months.

The pockets of valuation that we are now discovering in midcap a) have one source, which is, the relative valuations between the largecap and the midcap. Therefore, it gets influenced by the broader market behaviour. The corollary to that is that when the market will turn, these midcaps might probably correct more than the markets will. But going by the fact that the Indian economy is likely to grow at 8 -8.5%, we cannot expect that this growth can be confined only to largecap companies, it has to cascade to small and medium enterprises and I think that is where the opportunity on the longer-term horizon lies. If you look at next 12-24-36 months, I would still believe that even from the current levels the midcap index will outperform the largecap index.

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**Q: You have been quite bullish on the entire IT space. What kind of out performance it at all are you expecting from that space?**

A: I think much of the out performance has already happened from the current levels. I will probably need to modify my stance and say that IT maybe a market performer from the current levels because this quarter the fact that the currency rates have moved by and large in favour of the IT companies, will get reflected in the optimism that we are seeing in the prices. Going forward, one would be slightly more subdued in terms of the optimism that you have on IT.

**Q: How do you approach the metals now because given the commodity rally globally metal stocks have started doing quite well?**

A: We actually had a contrarian call on that saying that while metals is high beta but it would reward you for the risks that you take for beta. I think if you see the growth projections which is not only for India, which is aggressive 8.5-9%, for most of the world economies, 2011 will be a much better year than 2009 or 2010. With such growth and the growth being now largely centered on the most populous nations India and China, the price for commodities and metals in particular should be going up and while therefore there is skepticism which is probably holding back the stock price performances in the short-term, I think if you look at medium to long-term the sector that one should play.

**Q: What would you do with some of the softer commodities like sugar now? Do you see some bit of resurgence in that space?**

A: The sector has actually performed quite well over the last one month but on a more enduring basis the current year's sugar production is expected to be about close to 26-27 million tonnes. We will probably not have a demand-supply gap in India and therefore I don't expect sugar prices to sustain at very elevated levels for long time. I think much of the rally in these stocks we have already had. But I expect that over the next one year or so, the entire space of commodities, natural resources including agri-commodities should do well. So sugar could be a participant in that theme.

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