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Forget gold, look at fixed income as an asset class to hedge your portfolio: Suresh Soni

Suresh Soni, Chief Executive Officer of DHFL Pramerica Asset Managers Private Ltd, said equities remain an attractive asset class for the long term and a systematic investment in equities would deliver attractive returns for investors.

Gold has to be viewed more as a “store of value” than a tool for wealth creation, and I personally would choose fixed income as a safe haven which continues to offer a very attractive real rate of interest, Suresh Soni, Chief Executive Officer of DHFL Pramerica Asset Managers Private Ltd, said in an exclusive interview to *Moneycontrol*.

Excerpts:

Q) Geopolitical concerns continue to weigh on D-Street, which seemed to have climbed the wall of worries. What should be the ideal strategy for investors?

A) Stock prices are the slaves of corporate earnings, and the ability of the company to compete in the market place. However, in the short term, markets are subject to fluctuations due to a variety of reasons, many of which are transient and short term in nature.

You should indeed be looking at selling your shares if you see a sustained impact on your company’s earnings due to a potential US/North Korea conflict.

Time and again the markets’ reaction to events has given opportunities to acquire stocks at attractive valuations. As equity investors, we will keep reading headlines like Brexit, Greek crisis, Fed moves, potential war etc. None of these can be forecast beforehand nor are they likely to have any direct impact on corporate earnings. Investors will do well to ignore these events and stay focused on their long term investment journey.

Q) Gold has caught the fancy of investors in 2017 amid rising geopolitical concerns. What are your views? Should investors start allocating some amount of their portfolio towards these safe havens?

A) Over the last 30 years, about half of the returns that gold has delivered has come due to currency depreciation and the other half due to rise in international prices of gold.

As Indian Rupee has been strengthening over the last few years and international prices of gold have remained weak, gold has failed to deliver to investors. I think gold has to be viewed more as a “store of value” than for wealth creation.

I personally would make my safe haven allocation to Fixed Income which continues to offer a very attractive real rate of interest.

Q) The gap between the Nifty’s PE and economic growth is at a 12-year high. Is it time to turn cautious about valuations?

A) The last quarter GDP at 5.7 percent is one of the lowest readings that we have seen in recent times. However, this period coincides with post- demonetisation and pre-GST phase of the economy.

We believe that economic growth is expected to bounce back to 6.5-7 percent for the next 12 months.

Q) The Sensex trades at a 12-month forward P/E of 19.2x, at an 11 percent premium to a long-period average of 17.4x. Sensex P/B of 2.8x is at 4 percent premium to its historical average. How should investors read through this information?

A) While on PE ratio the market is clearly trading above long term averages, on a number of other parameters, valuations appear somewhat reasonable.

The last few years have seen relatively weak margins, poor corporate earnings growth, and low capacity utilisation. Going forward, with declining interest rates and margins normalising one would expect earnings growth to recover to 15-18 percent for FY18-FY20 as compared to around 5 percent per annum over the last three years.

Current valuations of the market are factoring in a significant part of the hope of this earning recovery. We believe the valuations are no longer compelling and give a little room for disappointment in near-term.

That said, the market is not a monolithic entity. It is the average of all sectors. As investors, we ought to avoid stocks or sectors that have reached exorbitantly high levels of valuations.

Equities, however, remain an attractive asset class for the long term and a systematic investment in equities would deliver attractive returns for investors.

Q) What is your call on small and midcap stocks which saw double digit cuts in August? Is it time to bring down holding in these stocks because GDP growth is unlikely to recover soon amid GST implementations?

A) It is hard to generalise small and mid-cap stocks in a single basket. Even as some stocks have suffered recently, we have seen a number of stocks rise too.

In general, the midcap index is trading at significant premium to its history and also relative to large cap indices. Indeed, there are a large number of mid-caps where valuations appear stretched.

We would advise, on an average, investors to favour largecaps as opposed to mid and small cap at this stage.

Q) Why are FPIs fleeing India? They have already taken close to $2 bn from India equity markets in the month of August. Is it temporary or will the trend continue?

A) Fleeing is a very strong word. FPI's have been big buyers of both bonds and equities throughout the year. We don't think a one-month withdrawal can be termed as "Fleeing" and nor does it represent a trend.

One also needs to factor that in the recent times, the aggregate investment by domestic MFs exceeds FII flows, on the back of growing retail interest.

Q) Indian equities are trading at 21.2x FY18E earnings. All key markets globally continue to trade at a discount to India. However, India's RoE remains superior to most EMs, an important differentiator for valuation premium. Is it a bullish or a bearish sign?

A) At this point of time, most of the international equity markets are trading above their long-term valuations. India remains a promising market with strong macro, political stability and expected earnings recovery.

This explains the interest of international investors and premium valuations for India. In the past also, India has enjoyed a premium relative to international markets. We believe that the premium valuation of Indian market may sustain in future.

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