ETMarkets Smart Talk: Railways and FMCG could turn out to be a dark horse in 2023: Amit Nadekar

Synopsis

Bloomberg data indicates CRB Commodity Index rose more than 15% by 3rd week of February when the second shock hit. Russia invaded Ukraine and war was announced, pushing commodity prices further up with CRB Index climbing another 15% by early March 2022 (source: Bloomberg).

"Railways and FMCG could turn out to be a dark horse in 2023. Railways is embarking on the growth, renovation, and safety CAPEX which could have the longevity which could run into a decade," says Amit Nadekar, Senior Equity Fund Manager, LIC Mutual Fund Asset Management Ltd.

In an interview with ETMarkets, Nadekar said: "FMCG which has been an underperformer since the Covid-19 lows could see a comeback at least in the first half of 2023 if demand stays resilient and operating margins normalize," Edited excerpts:

How do you sum up the year 2022 and where do you see markets headed in the year 2023?
Trouble doesn't come alone. The year 2022 was out there to prove the proverbial wisdom.

It started with commodities. The first shock came right at the start of this year. While the world was thinking for supply chains to be restored and central banks to be proven right on inflation being transient, commodity prices started spiking.

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The world expected the military power of Russia to help conquer Ukraine in few weeks and normal business to be resumed sooner than later. However, as we know today, the war still continues.

The third rude shock to the capital markets came when suddenly US Fed announced that inflation is not transient and large doses of rate hikes would be required to bring price stability.

US economy has already recorded one negative print of GDP and talks about US slipping into recession has already commenced. Fed's preference towards price stability over economic growth stability became loud and clear in it's June 2022 meeting when for the first time since 1994 it delivered the largest rate hike of 75 basis points (federal reserve.gov).

This sounded alarm bells for the investors and recessionary talks became louder and louder.

Bloomberg US recession forecast which was 15% in early March grew to 40% by end July 2022.

Since May'22 meeting US Fed has raised the benchmark Fed Fund rates by a whopping 400 basis points (federal reserve.gov). To sum up, all through 2022, the corporate and financial world is fighting many battles – supply chain uncertainties, high inflation, high cost of capital, geo-political instability, weakening demand outlook, rising operating cost with continued tightness in labour market.

No wonder, equity markets globally could not withstand the gravitational pull of rising cost of capital and receding growth prospectus. Globally, equity markets have corrected by 16.1% in 2022 (From dec 2021 to Dec 2022) (source: Bloomberg). Indian equity market has withstood this global storm remarkably well and has outperformed most countries by a wide margin.

I believe, till the above concerns get meaningfully addressed, markets could remain in a state of flux. The year 2023, therefore, could turn out to be a story of two halves.

The first half could remain challenged as most of the above concerns still remain unaddressed.

The second half could see, elevated prices responding to weakened consumer and industrial demand, central banks meaningfully softening their stance, and equity valuations attracting investors back.

Of course, the risk is always of unknown and that would be the caveat for the 2023 second-half positive outlook.

Do you see the bull run continuing in 2023. Which are the headwinds that one should be aware off?
Like mentioned above, year 2023 could a story of two halves. Currently the market (Nifty 50) is going through a period of consolidation through both time correction (returns over the last 12 months are merely 5% up compared to last 10 years average of 14% up) and price correction (average price correction for Top 200 stocks by market capitalisation from their 52 week peak is 13.7% (source: NSE)).

The price correction could continue getting into 2023. The key headwinds or rather the downside risk for the market would come from earnings disappointment.

Most of the headwinds of 2022 seem to be fairly understood and well-priced in. Investors expect both demand improvement and margin improvement in most of the sectors be defensive like IT, Pharma or FMCG or cyclical sectors like Financials, Auto and Industrials.

However, if incremental demand weakens, then there could be disappointment on both growth expectations as well as margin expectations as ability of companies to pass on commodity inflation gets challenged.

New Year will also mark the beginning of Budget 2023 preparations. What are your expectations from Budget 2023?
If one observes, the last several budgets of the NDA government, one can say that the Budget has lost its significance as a single tool to announce big-bang policy changes or drive economic reforms or make a political statement.

One would rather like to see the continuity and stability of reforms through budget allocations and initiatives.

Also, use of the budget as a political statement has receded and therefore despite central elections in 2024, we don't expect the Budget 2023 to be a populist one.

In fact, similar to the strong growth focus of the 2022 Budget of capital expenditure, we expect continued higher allocations to capital expenditure despite the challenges on fertilizer subsidies which are a fallout of the Russia-Ukraine war.

Which sectors will be in focus ahead of the Budget? We have already seen some rally playing out in sectors like Infra, Rail etc.
We don't expect any one sector to be a disproportionate or specific beneficiary of the upcoming budget. Rally in sectors like infra and railways is driven by the strong order inflows and improving P&L and balance sheet of the companies in this sector.

Yes, the improved visibility for these sectors, through higher budget allocations to infrastructure and railway projects can definitely further build up on the prospects of these companies.

Which themes will do well in 2023 and why?
We are constructive on sectors/companies which offer better visibility and predictability of growth through strong order books backed by strong execution skills or though the granular and repetitive nature of demand.

Auto, industrial, and banking sectors which are coming out of the long spells of drought stood out on these counts and also offer good entry points from a valuation perspective. We expect these themes to do well in 2023.

COVID is rising again – do you think it could well turn out to be the next trigger for the selloff in equity markets?
Covid is definitely a risk to watch for as the same can again strangle and stagnate global business flow.

However, after going through 3 waves of Covid, both investors and businesses have understood this risk very well and would not act as a trigger of sell-off unless it really springs into an event of six sigma proportions.

Amid recessionary fears across the globe how do you see India stack up against all odds?
India has withstood all odd of 2022 including recessionary fears much better than most of the countries in the world and we expect 2023 to be no different. With a large population base of 1.4bn India offers a strong market for staples as well as discretionary consumption.

With a large domestic industrial demand, strong engineering skills base, and relatively stable sensible political, legal and regulatory environment India continues to thrive and prosper as a global outsourcing hub be IT, Pharma, Chemicals, Auto or Industrial Manufacturing.

The drivers like the recent thrust on manufacturing by GOI through schemes like PLI, China+1 movement for global companies have only further accelerated this process.

To cut the long story short, India is in a sweet spot given both domestic and global opportunities and it's a structural story that will continue to unwind over the coming decades.

Any sector according to you that could turn out to be a dark horse in 2023?
Railways and FMCG could turn out to be dark horse in 2023. Railways is embarking on the growth, renovation and safety CAPEX which could have longevity which could run into a decade.

FMCG which has been a underperformer since the Covid-19 lows could see a comeback at least in first half of 2023 if demand stays resilient and operating margins normalize.

Your message to investors for 2023?
Year 2022 has been a character test for the Indian equity markets which it passed with flying colors.

Year 2023 could well turn out to be a character test for Indian equity investors.

2023 won’t be a volatile and painful journey but it’s your character that will decide how you come out of it. I would only say that it would help to have a long-term goal orientation.

(Disclaimer: Recommendations, suggestions, views and opinions given by the experts are their own. These do not represent the views of Economic Times)