Notes from Interview of Sankaran Naren

- Compiled my Venkatesh (@SuccessProject_)

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Important Update

- These notes were made to understand investing insights by fund managers and famous investors
- This work is an ongoing work, where I updated it periodically as and when I listen to/read new interviews.
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2018: A B C D E - S. Naren's 5-point investment philosophy and views on the NFO

https://www.youtube.com/watch?v=X0AqXmF0JQ8

December 31, 2018

ABCDE of Investing

Asset Allocation:

Here a certain amount of money is put in equity, debt, real estate and gold. By doing this properly you would have made more money than whatever else you did. In 1992, when the Harshad Mehta scam happened, you would have sold equities when all were buying. In 1994 when FIIs came in was the time to sell equities. In 1998, many big companies raised money at 16% interest rates. People moved to debt instead of undervalued asset class equities. In 2007, there was a big boom. In this period asset allocation would have told to sell equity and buy Gold. In 2012-13, this would have told you to buy equities and sell real estate. All these decisions on asset allocation are very easy on paper. But in practice was the other way round. In the Mutual fund industry, most of the money came in 1992, 94 and 2007. While all say that they did asset allocation, they always did the opposite of it.

Bubble and Bust:

In 2012, I was lucky to chair Warren Buffet in Mumbai and Delhi. People asked about his lessons from 40 – 50 years of investing. He said: Bubbles and busts are common once a decade. In these 40 – 50 years, you will see 4 – 5 bubbles and 4 – 5 busts. During those times, you have to be rational. In 1999 was an article in Barron that Warren Buffett lost his touch as he plays bridge game with Bill gates, but does not know to invest in Microsoft. It was end of Buffet's investing era. But from 1999 to 2018, he continues to be the greatest investor. 1999 was the time there was a NASDAQ or the Technology bubble. Avoiding bubble by selling and buying in the bust is an easy way to make money. This is what I call as B. India also periodically has bubbles. In India, there was a bubble in 2011, 12 and 13 in Real estate. The boom started in 2002 and went on for nearly 9 years. Bitcoin is a bubble, why is it a bubble? Because no one knows how to value it. It was very mysterious in the case of Bitcoin. To stay out of a bubble is one of the biggest challenges for an investor. Because in a bubble, everyone around you is making money and you are not. So B stands for avoiding bubbles and investing in Busts.

Cycle

Most people do not realize that investing is a cycle. To handle cycles, Howard Marks is my guru. Markets are as old fashioned clocks with Pendulum. They move from one end to another. One end is extreme fear and another end is extreme greed. Being aware of the cycle is the biggest problem in investing. FAANG stocks were predicted to go up 6 months back… in Media. But now it is corrected nearly 20%. This was due to the cycle. Stocks like Amazon and Apple were worth 2/3rd of the Indian stock market. The cycle happens every time. You will be able to identify a cycle when people are very positive about something. In the same way, you can identify the cycle when things are very bad to the extent that all want to run away from it. For cycles you don't need to know about finance or models, you only need to know what people around you are doing. Based on this you can understand a cycle pretty easily.

Debt

Most important asset class in a person's portfolio. Debt gives you stable existence. In my career of 29 years, there were 14 years, when the equity did not go anywhere. You are comfortable at all points of time. In 1998 and 2002, Markets were very cheap. When you have debt, you will have resources to invest at the bottom of the market, whenever it happens.

Equity

It is a great asset class over the next 10, 20 or 30 years. Globally it has made very one wealthy. The richest people in the world, most of them have made money in equities. The best way to invest is by the way of SIP. In 2004, when the election result came, the market came down by 10 – 12% in 2 days. If invested at this time, you would have made huge money in the next 3 years. 2009 was just the inverse. If you have invested a huge sum of money before the elections, you would have made huge money after the elections. Anyone who invested in 2014, had a very good investment experience. Everybody predicted what would happen if the election results came a particular way. The result came in a particular way but markets behaved exactly the opposite way. It is very difficult to predict: in 2004, the congress win led to a 10% down in the market, while in 2009 the win by the same congress, led to a rally in the market. Everyone thinks they can predict how the market will move after elections. The same government, the same results produced two opposite results. We take special situations as a team. It is one of the interesting long term methods of investing. Reason: Periodically companies go through problems, E.g. Nestle had a Maggi quality control issue. You could buy Nestle then. Similarly, Maruti had a strike and the stocks fell substantially. In 2005 – 2007, one of the companies went for a split. Whoever brought before the split made a huge amount of money, as they got many shares of the split companies. PSU does not do well, and Private banks and NBFC gain. Recently NBFC had a problem, and Private banks gained. Periodically problems happen in different companies and sectors. The biggest advantage in this special situation is to buy cheap. If you keep on buying cheap in different stocks for different reasons, you tend to make a good amount of money.

When to invest? In good or bad times? One of the interesting things about equities is that bad times are the best time to invest.

2019: Learnings from my investment career | S. Naren @ Value Investing Pioneers Summit | CFA Society India

https://www.youtube.com/watch?v=Pt1JOctt5Og

28 December 2019.

Experiences in Japan

- In 2015, I made 5 visits to Japan. The meetings were at lunchtime. The average age of the attendees was in the range of 70 – 90. All of them were having Japanese interpreters. I checked with someone to know that they are the richest people in Japan.

- Every year they are breaking down houses, as the number of people is going down. They are closing a few schools as the population is going down.
- Entire economic theory is built upon an increase in population. If it is decreasing, there is no economic theory available at this point.
- As long Japan has a CAD surplus and the population is decreasing their interest rates are not going to go up. They will remain 0.
- Here you do not .eed investment, but disinvestment in the form of breaking down houses, schools

My investing career

- My goal is not to give all the answers but to create questions
- Investing is about **b**uying, **s**izing and **s**elling.
    - The irony is that 98% of investment literature in India or the world is on buying.
    - Less than 2% is focused on sizing and selling.
- I do not have all the answers on sizing and selling.
    - For sizing, you must know how much to size based on your conviction, the risk associated and the kind of detailed work you have made on the company
    - In my view, most people who are investing, make a mistake in sizing.
    - I am also yet to get enough literature on sizing.
    - In selling, I have seen very little work
    - A friend suggested changing the name to "Switching" instead of selling
    - Think of every selling decision as a switching decision and then evaluate that switch
    - If an investor spends a bit more time in sizing and selling than buying then his returns will be much better
- Why do people associate me with a contrarian?
    - When working MF, you will get a lot of money
    - In 2007 – 08, I realized that the moment you become a contrarian, you need not worry about money.
    - Flows will come always at the wrong time, you will have to find a way to manage them.
- In my opinion, contrarian is the easiest way to invest in.
- The problem with the whole contrarian approach is that people started thinking that I was going to buy junk infrastructure stocks.
- One key thing to keep in mind when following the contrarian approach is that you have to be very careful in leverage stocks (Quotes Bill Miller of investing in highly leveraged financials)
- One useful thing is cyclical, as cycles help you to sell
- In cyclical you do not suffer the entire problem of leverage
- It is important for a contrarian to know the other side of the trade / Why is the other side selling
- If you cannot do risk management, contrarian is not the style for you.

Things I Believe

1. Cycles

- Everything cycles, like a Pendulum moving from one end to another.
- Cycles come all the time.
- One end of the spectrum, you will find it very very careful and for another end of the spectrum, you have to be reasonably aggressive.
- For the long term, it is important to know about cycles.
- It is not arithmetic, where you never get clarity.
- You never know what is the top and what is the bottom.
- At the same time, you will have a good reasonable judgement.

2. Charts:

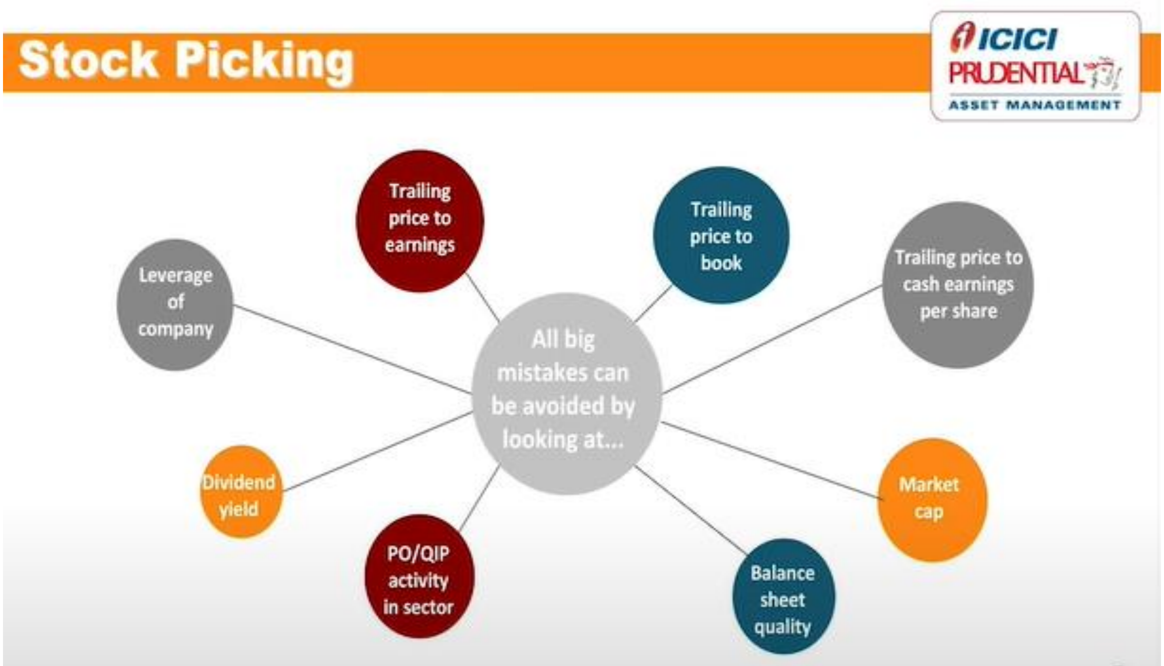
- Antony Bolton said to look at the charts before buying and selling.
- If you look at the charts you realize how many other people are (or are not) on the same campus you are.
- Fundamentalists are not inclined towards charts.
- The only purpose of charts here is to see how many other people are thinking like you.
- All you need to do is spend one minute. Today it is very much easy, there was a time when getting a chart was difficult. The entire chart is available on phone.

3. Common sense

It is easy in retrospect. But in this situation to evaluate it with common sense is much more difficult

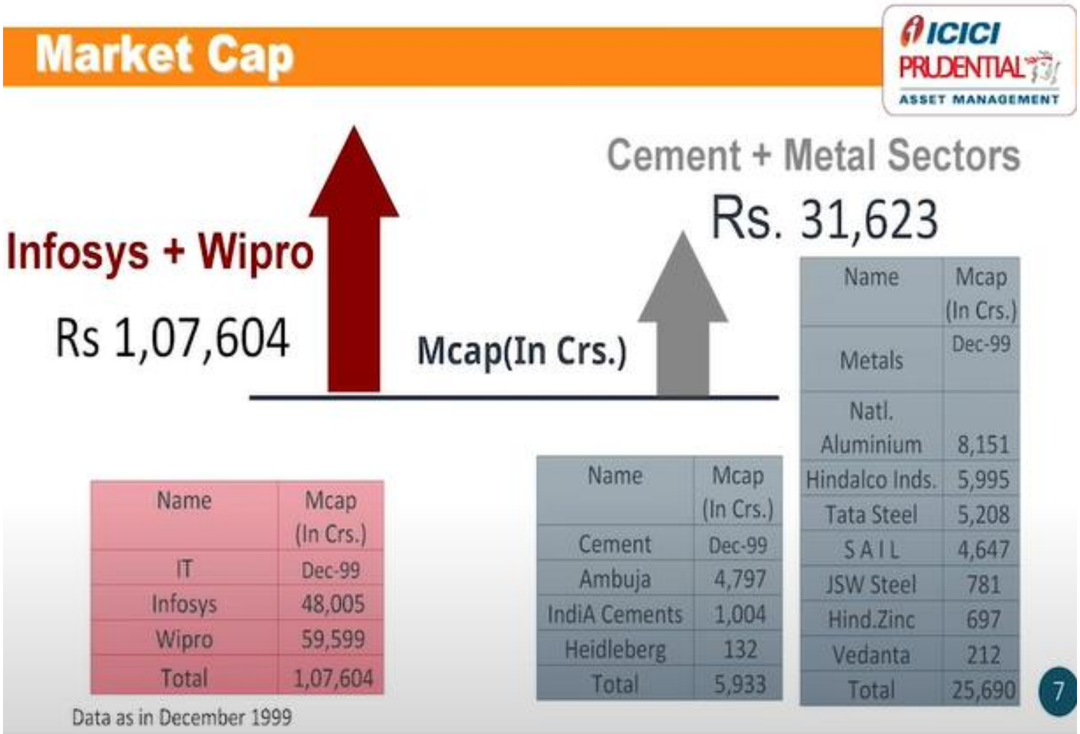
Cash a Residual asset class is very important: One important lesson that I had from my career in fund management is the ability to have cash as how Warren Buffet says. The presence of cash improves the quality of decision making significantly. The ability to have cash at the right time is the most important ability to make money. Warren Buffet could invest in 2008 when others could not as he had cash. Howard marks could invest in a special situation as he collected cash in 2007 and left it undeployed. The role of cash in long term investment returns is very important, which is severely understated. You do not need to have cash at the bottom of the market but need it at the top of the market.

Stock Picking

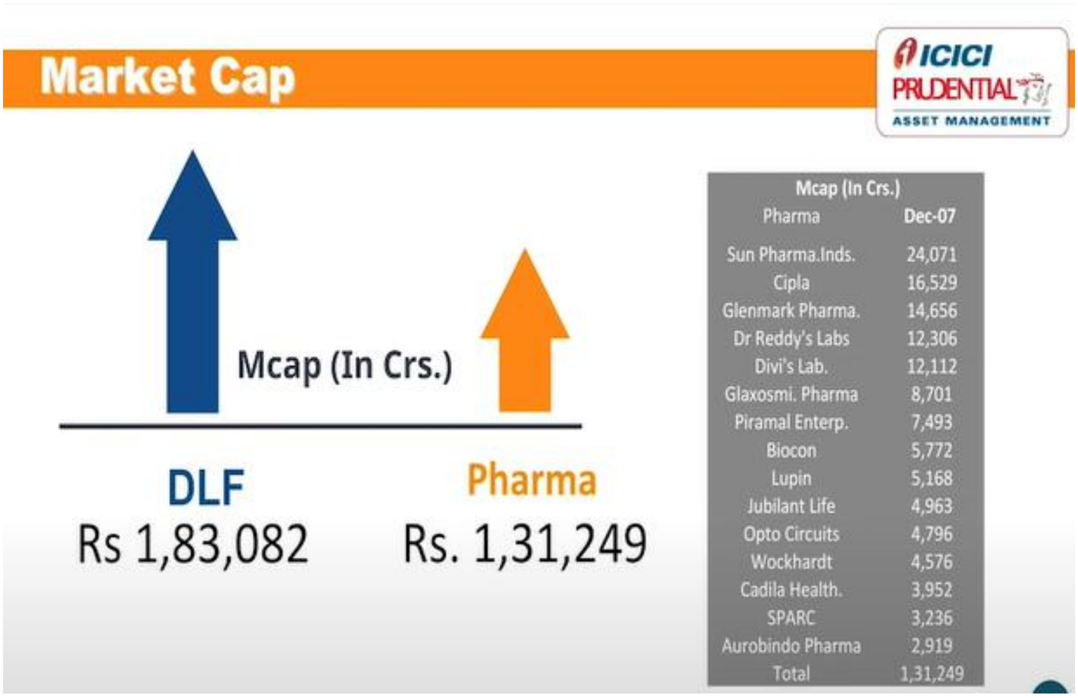


At this point, these don't seem working. But if you have longer investment cycles this works very well.

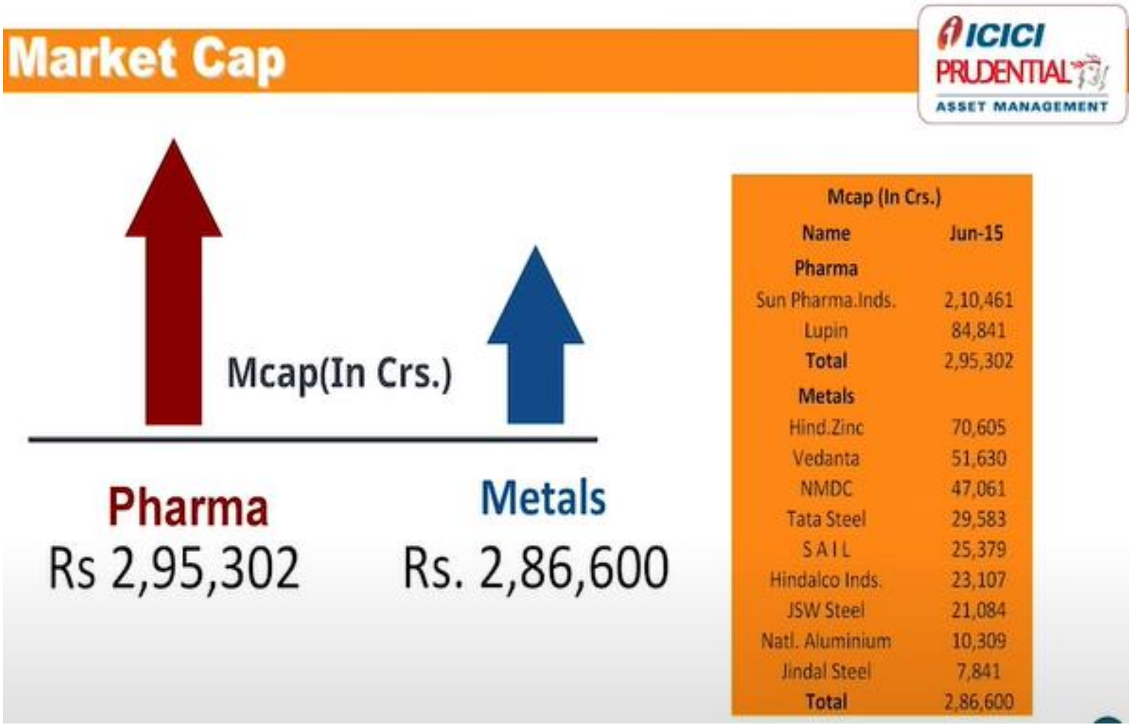
One Indicator that I found very useful is Market Cap. In 1999, Infosys and Wipro together had a Mcap greater than the Mcap of the entire cement and metal sector. You are getting the entire sector for the market cap of a single company. Market cap is one of the best indicators, which works at the extremes.



There was a repeat in 2007 when the DLF market cap was greater than the entire Pharma industry. It is very clear from the extreme point of view.



The same sector in 2015 had a different dynamic. Two pharma stocks (Sun and Lupin) were greater than the entire metals sector. Then 4 years later, Pharma did very badly.



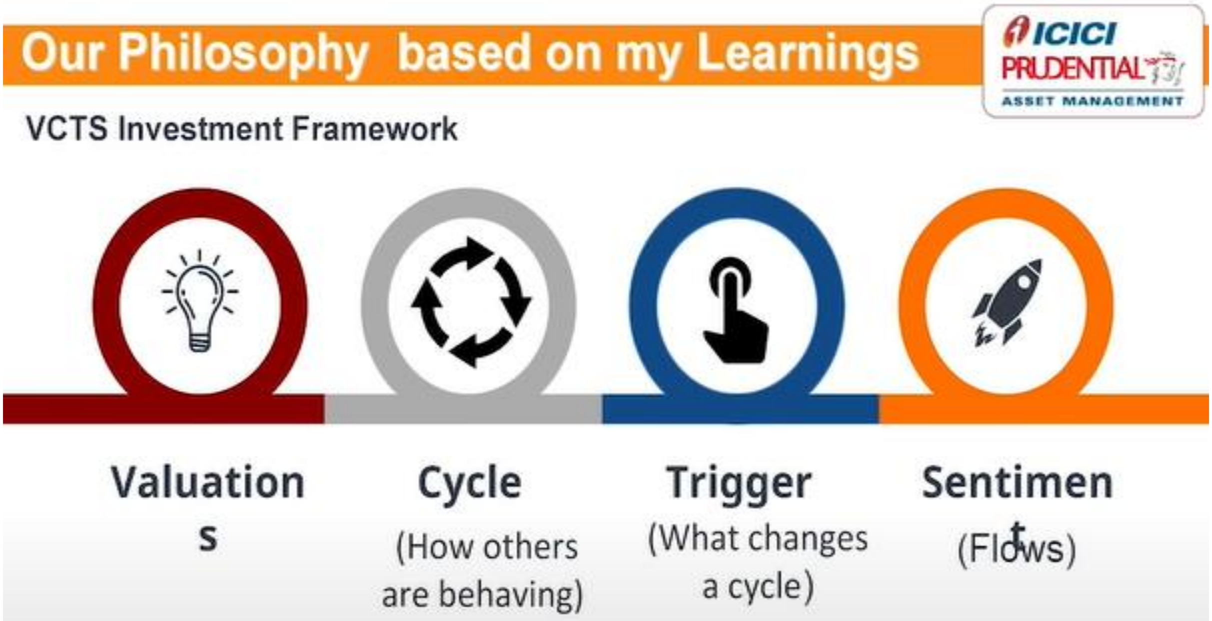
HUL's Market cap is higher than that of the entire healthcare sector.

This market cap difference helps a fund manager to take a call for the next 5 years. This may not work in the next 3 months. Such extremity is not as easily identified as any other single metric other than Mcap.

Whether this approach works in all situations? No, some companies work in completely disruptive sectors like Google, Apple, Facebook etc. However, in India, we do not have companies which are at the cutting edge of innovation. So this approach in a company like Apple or Google will fail. So, you should not apply this globally, particularly in American Tech companies.

This is the lesson from the experience of using Market caps. This will not be used every day. It works better in a country like India than in the US, because you don't know if Tesla is going to take over.

Creating wealth across asset classes



- Valuation is a number, which you can judge and arrive at more easily. But the other 3 are much more important.
- Cycle: How other people are handling the asset class. How do your neighbour and the rest of the community behave? It is not about how you behave, but how others behave.
- Trigger: This is the toughest word. For anything to change, a trigger is required. Nobody knew why the real estate market that was absurdly valued till 2013, stopped. Maybe his 3% interest rate hike. NBFC was having a boom time year. New companies were coming with start-up money. But the trigger for the NBFC to go down was ILFS failure.
- Sentiment: Are people putting money in that asset class? How are flows?

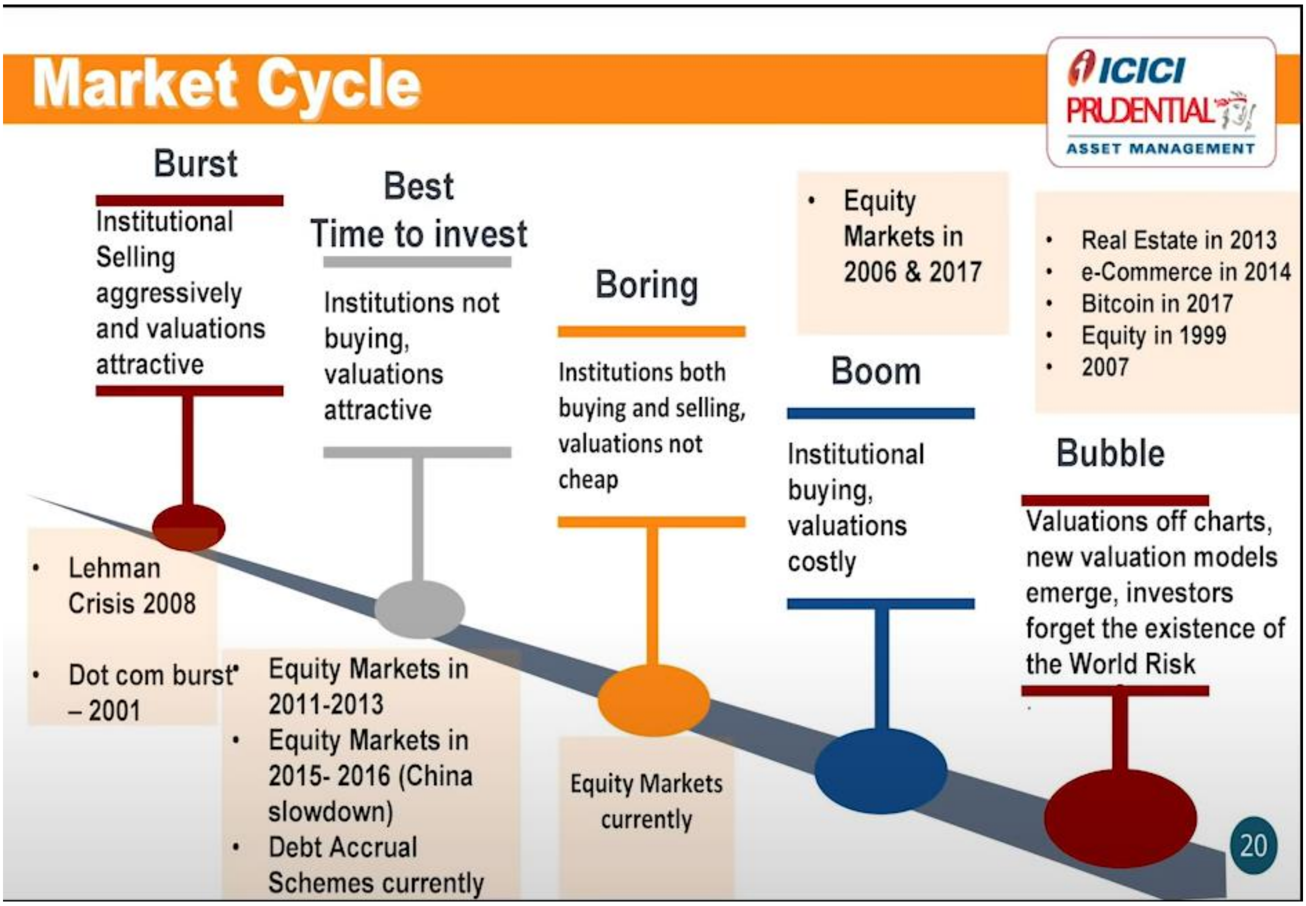
If there is madness in the form of cycle, sentiments and elevated valuations. You cannot wait, but act. The trigger is something that you think will know, but will never know. The trigger is controllable. So you need to see only the remaining three. As long as flows are very low, valuations are low, and people are scared of an asset class, you should not worry about when the trigger will happen.

One other lesson we learnt, is not to use one indicator, as it can be distorted due to some reason. But 4 indicators cannot be. Take 4 indicators and see a composite view.

Valuation of other assets

- Gold and cash are residual asset classes based on the valuation of the other asset classes. When all other asset classes are costly, Gold and cash are cheap and vice versa. If everything is cheap, do not keep any money in Gold or cash. This gold and cash cannot be analysed. Evaluate based on how other asset classes are.
- Real estate: The gap between the home loan rate and rental yield. The day the gap is 4% you need to buy real estate. Take it on current prices and not past prices

Market Cycles



Shankar Naren added a few components over the Howard Marks, market cycle idea.

- *Bubble:* This is the easiest: You have new valuation models. In the 2000 dot com bubble, you had eyeballs based valuation. In 2015 for E-commerce companies it was EV/Sales. These are non-earnings based models. In a bubble, you will never have a valuation model made on cash flow and earnings. It will be built on the top line. When equity is in a bubble, it becomes difficult to be rational.
- *Boom:* Expensive valuations and money coming in a big way. You make money in the boom if you take out money. But if you invest in a boom, you don't make money.
- *Boring:* Valuation is not cheap. One money everyone is buying and next month, everyone is selling. You cannot make or lose big money in this part of the cycle. Maybe you can make some money
- *Best Time to Invest:* Valuations are attractive.

- *Burst:* Phenomenal times. But how to gather the guts. There were only two such situations: (1) the WTC bombing in 2001 and (2) the Lehman failure. There is big global negative news, cheap valuations and institutional selling. If you have the guts to put money, you will make huge money. But only 1 out of 100 may succeed.

As Howard Mark says, ask yourself, "Where are you in the cycle"? Are you trying to make money or save money?. Ask yourself if you are in burst or best or bubble or boring? That will help you to take eventual investment decisions in any asset class. This is not arithmetic, but more complicated. Judgement is involved. If everything is crystal clear and if all are acting then the opportunity does not exist. Because every trade happens as there is a buyer and a seller.

My Challenges

- Each investor has its challenges. You need to be aware of your challenges and stay with them.
- If everyone has a consensus, I find it difficult to hold that stock. Sometimes consensus can work.
- You will not meet a fund manager who does not have a weakness
- For 98% of people, an average way of investing is good enough: (1) SIP, (2) Index fund / ETF and (3) Asset allocation
- Everyone things that everyone cannot achieve above-average return / Achieving average return itself is very good
- The rest 2% wanting above-average return has to do a lot of things

Key Traits of an Investor

- *Time management*: Successful individuals need to know how to manage time. WB says that if you do not find time to read, you are not going to succeed as an investor. You need time to read and think

- *Thinking time*: People need a separate thinking time. This is very important, but many people miss it. They take time to read but do not think. We have one advantage in our country, a long time to commute. These commute times are a superb time for thinking.
- *Temperament:* Important aspect – Courage to buy at the bottom and sell at the market top
- *Reading:* A must-have habit for investing.

When you have time to read and think and with a good temperament you are going to be a great investor.

Truisms

- The fund managers are unnecessarily given positive views.
- Bill miller a value fund manager got demoted.
- Anthony Bolton retired after opening a China fund
- The wealth management industry is such that people will keep giving you money, till you fail
- The more successful you are the more they give you money and the more money that give you money, the make the set to fail.

This is a challenge in the mutual fund industry all over the world. The problem is that there is nothing called consistency in performance. But what I can do? I can do it consistently in the process. By this, I can deliver huge long term returns by not short term returns. Consistency in performance is not possible, consistency in the process is all that is possible. If this is told to customers, they will laugh at you. That has become one of the biggest challenges.

It is impossible for any fund manager or investor not to make mistakes. It is not possible to be correct all the time, not possible to deliver performance all the time. But it is possible to deliver performance in the long run with a sensible process.

If you get more and more money at the top of the cycle, you are setting up yourself for failure.

Advantages and Disadvantages of being an investment Professional

Advantages

- If I had not taken fund manager as a profession, I don't care about Trump Impeachment or BREXIT or what is happening in Greece.
- As a fund manager, I am interested in so many things in the world. I am interested in every election which happens.
- Charlie Munger at the age of 90, speaks like he is in 40 with clarity. This is a job that if you are mentally fit can do longer.
- Warren Buffet had long shared all this theory with the world, but still in Oct 2008, there was only 1 WB. Because theory is easy to share but the practice is much more difficult. In 2008, WB wrote an article that markets are cheap and still people did not buy into it. Because the problem is that the gap between theory and practice is driven by one's emotion. It is enjoyable that I can share my theory and ways of investing and not worried that someone can copy me.
- There are many ways to make money. Each one of us can have our way of making money. In a recent interview, Raamdeo Agrawal was telling his way of making money and I was telling the opposite of it. This way works for him and works for me. You need to improve your way of making money based on your introspection and thinking. The way you work and I work will be different. If you try to copy me without the right temperament, it becomes a big failure.

Disadvantages

Read Mark Sellers' speech every 6 months. This speech was given in 2005 and the hedge fund that he ran in 2008 blew up.

Can my temperament improve? Can I look more openly into 70 PE stocks? I may not have an answer, but I believe that you need to do some amount of learning and change. The PE that we used to give to some companies earlier cannot be given now, so there is continuous learning we all have to do. I am a public servant handling public money, which puts additional demands on me. I always ask myself if I am doing the right thing for my investors.

If you don't enjoy the joy of handling public money, then it is very tough as an investment manager. Market irrationality is a part of the stress of this job. It is very important that irrationality stays and goes away.

My Market Gurus

- James Montier – The tenants of investing article to be read
- Atul Gawande – Checklist approach.
- Howard Marks
- Michael Mauboussin – Postmortem is about who made the mistake. But in Premortem, we are not worried about "Who", but what mistake can happen.

Ideas from the Q & A Session

- Ask yourself, whether you are running other people's money the same way you run your money?
- We cannot control the timing and how long it will take for a particular thought to play out.
- 2007 was much more extreme than today, maybe 25 times more difficult than what it is today
- At times contrarian ideas take time to play out… During such time where do you get pressure? Investors, administration or distributors?
    - The pressure comes from you first… after some time only it comes from the system.
    - You should have the ability to write your view.
    - If you can write your views to internal colleagues, it gives you the capability to hold on to your position.
    - If am not able to write, I need to change my view. As something is bothering me in writing a note to my colleagues.
- As you grow larger, does not your investment world shrink?
    - In a contrarian approach, you happen to buy small and mid-caps when they are failing
    - We have the resource base to cover 400 stocks.
    - If there is redemption coming in Mid/Small caps, I will buy more aggressively
- Why MFs are investing in more than 70 – 80 stocks, instead of a few good stocks.
    - The large-cap fund needs more diversification
    - I don't think there is over-diversification
    - It is a function of size and nothing wrong with diversification

- Peter Lynch used to run his fund with 1400 stocks
    - We are managing 1.4 Lakh Crore of equity / Investors with a small ticket should not over diversify / There are cases where people invest in 50 Mutual fund schemes
- When your contrarian approach does not play out, in what interval do you validate your stand?
    - When you decide that you will sell at one pre-determined price then the problem becomes bigger
    - Telecom had multiple greed and fear cycles over the last 10 - 12 years. I made use of greed
    - I look at greed and fear in individual stocks
    - We have not tried this cycle in NBFCs and HFCs / I believe that when leverage is there, you need to keep contrarian investing very careful. It is like an electric current
    - High dividend stocks, I don't worry much / 5 – 6% dividend yield is more than the deposit rate
- Be cautious in newly listed companies from a new promoter. We do not know how the promoter is thinking and we get more insights only after one complete cycle. Deccan Chronicle and Manpasand have given lessons. Once you find a company with a 25-year history, you have insights into how a promoter behaves over some time. If a management transition has happened from the original promoter to their son or daughter, then you have to re-evaluate the company afresh. Because the children can be far superior to the original promoters or they can be worse.
- History repeats: The same set of companies which had NPA trouble in 1999 – 2002, ran into problems in the next cycle.
- Mutual funds cannot create Alpha out of the Sub 1000/2000 crore category, while an individual or retail investor can. The smaller the company, the more the potential to create Alpha.

2020: A Contrarian's Checklist: Asset Classes & Stocks with S Naren / Edelweiss Wealth Management

December 15, 2020

https://www.youtube.com/watch?v=6HdrEEZlwTo

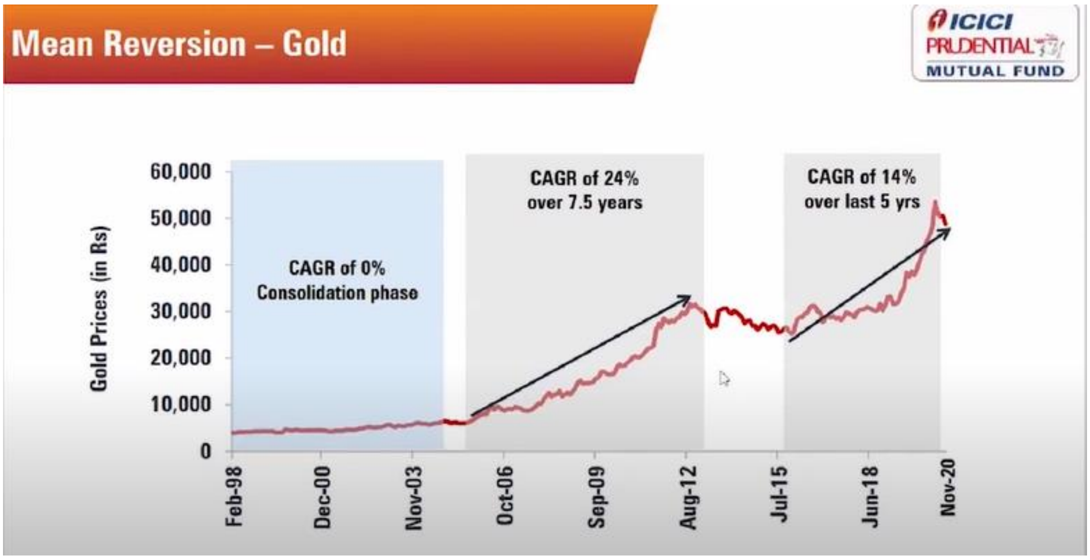
Started working in 1989 and had the advantage of watching the Harshad Mehta Scam within 3 years of my working career. In 1994, I had the privilege of seeing FII entering India within 5 years of my working career. In 1998, when markets went down, I emerged as a contrarian after being in markets for 10 years. At the end of the day, what is the purpose of investing? To make money post Tax in the long run. With this goal, I realized that the contrarian way is the best way to make money in the long run. Many things have happened since 1998. This year has been a contrarian investor's delight. March 2020, was the best opportunity for a contrarian to invest.

Warren Buffet wrote a cheque for 1 Lakh crore after the Lehman crisis, which is a contrarian delight. He is a contrarian is a reason why he makes so much money.

Being a contrarian, at a point in time, you are seen as an idiot. If you were to be in equities on 23, March 2020, it was considered to be very dangerous. Anyone wanting to invest in equities a day after the Lehman crisis, would be considered as being out of mind. A problem that a contrarian has to face is… once a decision is taken, you are seen to be crazy. Contrarian best investment comes, when other people think it is crazy. Contrarian is not necessarily a short seller. Many in the US claiming to be contrarian shorted Tesla while it slowly became 630 BUSD MCap. Now they are biting their wounds. Do not use short selling as a contrarian technique.

How do different asset classes behave over some time?

Asset classes consolidate. Once you have a long consolidation phase, there is a period of high returns after that. You must enjoy asset classes which have consolidated, rather than the ones, which have zoomed. This happens across asset classes. The same thing has happened in Gold. No return for a long period followed by a 24% return in the subsequent 7.5 years.



Once there is a huge return, everyone starts talking about that asset class. In 2003 – 04, there were articles that Gold is a dead asset class. Whereas in 2012, people say that Gold is the best asset class.

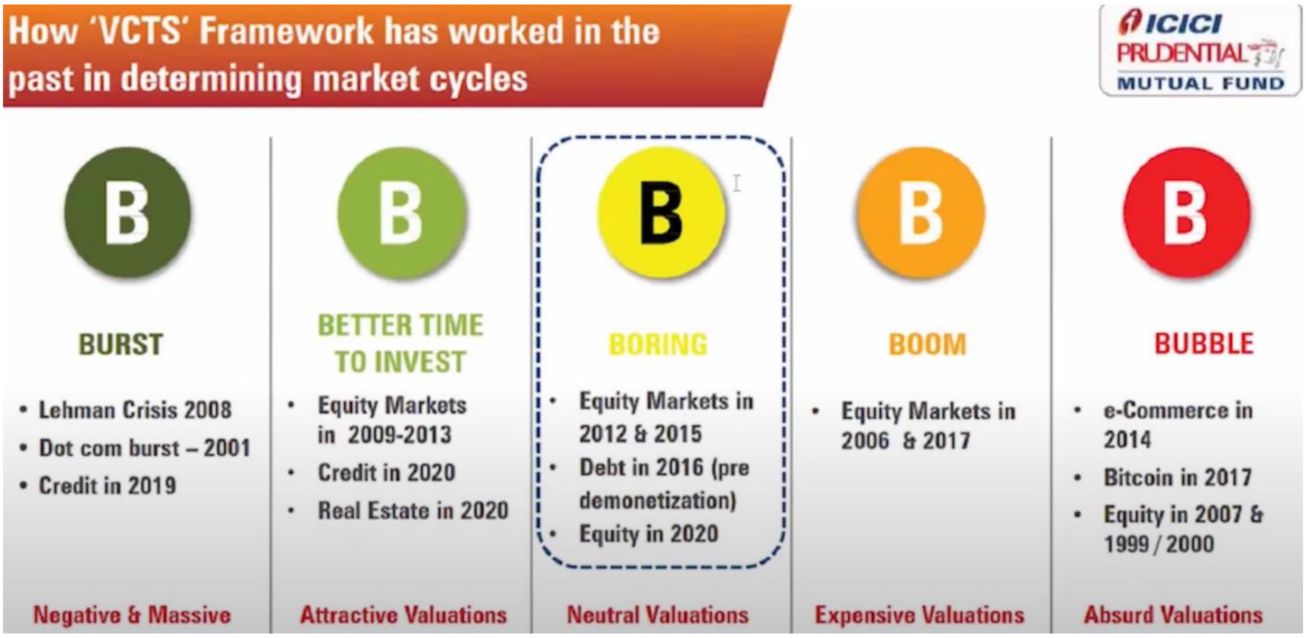
After 7 years of no returns in real estate, it is an asset class which is contrarian.

All asset classes will be cyclical and unpredictable. Once the returns are fabulous, you have to be careful in the asset class. On the other hand, when there are periods where an asset class has delivered pathetic returns, you have to be very positive. This is what people find very difficult to accept. If 9 years there are no returns, you should be positive and if it becomes 10 years, you should be even more positive. Because if the asset classes continue to do very very badly. They tend to improve. Is it always true? It has failed in one or two cases, e.g. Japanese equities.

Our Basic framework

- Valuation – Indicator if the market is expensive or cheap
- Business cycle – We discussed in detail above / Buy when the cycle is weak and sell when it is strong
- Triggers – This is something that is needed for an asset class to change.
- Sentiments – Understanding of investors' affinity towards the market.

Now equities are going up and will continue to go up. When will it go down? The moment the US increases the interest rates. But I don't know when this will happen. The reality is that valuation does not determine when the market cycle turns. Trigger help there. For example, in 2016, 2017 and 2018 NBFC were going up, even when it was known that it will come down. It went up till ILFS happened. Now market valuations are going up every day. You need US FED to say that we need to reduce liquidity and increase the interest rates. If today evening, Powel says this, tonight US market will fall 8 to 10%. Valuations are important but the trigger is even more important.



In a Boom market, you have to be a trader to make money. If you are in a bubble market, you are sure to lose money. Currently, in equity, we are in a Boom market. Boring markets are the best times to invest. Investing in Burst needs a lot of emotional balance, which is very difficult

Contrarian investing is very simple, Take money from an asset class doing well and put money in an asset class that is doing badly.

Checklist for contrarian investing

- Low/Muted past returns
- Declining flows
- Low valuations

Contrarian investing works well with assets, but not the same way in stocks. If you want to use this approach in stock investing, ask yourself if you are using the product? Do you plan to increase the use of the product? Contrarian investing works best in sectors/stocks with the potential to invert & innovate on a going basis

- We will not go back to Nokia phones
- We will not go back to the Yahoo search engine
- We will not go back to the Kodak camera

As an asset class, real estate could come into the favour or go out of favour. Same with Gold. But Nokia phones will not come back. Be careful, that what is true across asset classes is not true across the level of stock.

Power and Telecom are two sectors, where I have made a contrarian bet. Even during COVID, there was no way I could have lived without power and telecom. Similar is the case with Pharma. We cannot live without it and it has done beautifully in COVID times. There was no power for a few hours and the whole city broke down. This also shows how dependent we are on thermal power. All the thermal power companies will become solar power companies in future.

Q & A

Q: In earlier interviews, you have hinted that this is a central bank bull market. Is it the free money, that causes this? How does it end?

- I call this a developed world central bank bull market.
- Till 2008, stock markets and these banks were running separately.
- Now stock market exists at the whims and fancies of the developed world central bank.
- If they want to bring down the stock market by 20% tomorrow, they can do it.
- They only need to make one statement in the US.
- This is the problem for all of us, as we are managing other people's money.
- The whole market is not controlled by Fund Managers but by developed world central banks.
- These banks try to avoid big bear markets / They have not allowed any big bear markets after 2011.
- When was the last time the markets fell by 25%? I think these banks do not want a big fall in the markets.
- This year (2020) when the market fell, they ensured that the markets went up and caused a massive bull market.
- We are talking about a lot of things, but we need to remember that the entire stock market is a creation of the developed world central bank.
- One day it falls, it will not be because of us, but due to these banks - I am worried about this.
- Investors will later blame us, but I am equally not responsible for this bull market also.
- We did not get many inflows. Over the last 3 months (This interview is as of Dec 2020) there are net outflows.
- With the net outflows, why did the market go up 25%?
- Finally we get blamed as and when bear markets happen in future.
- Equity investors must have an income stream to take care next 2 – 3 years of their life.
- If they completely leverage on equity, Powel gives a statement, the market falls 20%, they then should not blame Edelweiss or any Mutual fund.
- Markets may not necessarily fall tomorrow itself… Nifty could go to 16,000 or even 18,000. The bull market can last a few more years also.
- It is 24 Trillion dollars unleashed by the central banks.
- In the next year, this is going to become 28 Trillion / I cannot even tell you how many 0's are there.
- Nothing about the future can be predicted.. i.e. Fall or crash in future. But people only should know the risk of a bull market.

Q: Do you have any Time horizon in mind, when you are doing contra bets.

Many stocks have sustainable dividend yield which is higher than FD. Why worry about what is happening in stock price. That is how I look at it. 2020 has been the most difficult year to predict share prices even for smart people like you. None of us could have predicted such a share price today, back in June 2020.

Q: Where are we in the cycle looking at different parameters.

Continuous mutual fund outflow is positive. If that was also not there, I would have been very very worried at this point. This means there are enough negatives, sceptics, and people willing to take out money. In India and many other parts of the world, the old economy stocks are still very cheap. Even today there are stocks with a good dividend yield of 5%. At this point, we need to watch inflation, and what happens to crude oil. If crude oil stocks shoot up, that should be my biggest worry.

Q: One sector that you talk about is real estate. Is investing in real estate stocks a proxy for investing in real estate?

May real estate companies were raised in 2007 – 09. Many of them have disappeared also. There are 2 – 3 good companies which are part of our portfolio with big holdings. There are very few companies in real estate where the corporate governance are good. A few of their valuations are big high and hence not part of the portfolio. We also have invested in 2 of the REITs. There is confusion here if the commercial real estate will do as well.

Q: What is your take on the overall PSU pack?

We are big believers in PSUs, particularly in the non-banking area. Many have corrected in the last 10 years and have dividend yields higher than FD. There is a good value at this point. To what extent it will get re-rated needs to be seen.

Q: Do you see an opportunity in the NBFC space?

NBFC whose ratings are getting upgraded, those stocks are likely to do well and people will invest in them. With better ratings, they have access to very cheap money. That is how I broadly see it at this point.

Q: Commodity inflation is picking up across the globe. In a country like India, will this not have an impact on inflation?

During inflation, equity tends to do much better than any asset class. One risk that plays is if crude starts to shoot up. This will be one risk for the Indian economy. We are seeing inflation in plastics and other commodities. That is the reason why we are more positive on equities, particularly on commodities and metal stocks.

Q: IT has a sector that has done well in the past in both India and abroad. When compared to US companies the Indian Tech leaders still have a gap in market valuation. Will this give Indian players, good returns from current levels due to valuation re-rating?

I do not think, Indian IT companies can see a further PE increase. If they manage to increase the market share significantly, their shares can go up to the extent of growth. Can their PE go up, No is my view. Consumer companies I used to be bearish at 45 PE, now they went to 70 PE. Can happen like that also. I don't know why people are paying 70 PE to some of these companies. At 70 PE, they refuse to go down, even if growth is low. My personal view is No, but I can be wrong. Luckily in recent times Pharma also got rerated. We were a contrarian and Pharma did very well. Last 1 year, Pharma has done better than consumer companies.

Q: What is the exit strategy for a contrarian? How do you know that you have gone wrong?

This happens when the management does stupid things. It normally does not happen, as you are investing after a big problem and substantial underperformance. Sometimes you get the numbers wrong. Remember as a contrarian, you are investing after a huge underperformance. Here if you go wrong in numbers, you will end up in a bankrupt company. That is why you need to size it properly. You cannot invest some 40% of your net worth in a contrarian bet.

Q: As a fund manager, how do you manage sector allocation within this framework. Is there a philosophy or process behind it?

We look at the macro side, which sometimes gives you a lot of benefits. From 2011 – to 2013, we were worried about the economy as CAD was very high. Now you are not worried about the economy as CAD is coming down. Sometimes you get signals from the macro side, that something is seriously wrong. Macros may show NPA are shooting up, then we get worried about the banking sector. Sometimes we get sectorial benefits by looking at the macro side.

I also look at cycle and value. The macro approach tells that we need to be careful in PSU banking, and construction, at one point in time.

You need to use the combination of macro + contrarian + value cycle. You need to adequately diversify as well.