WoS – 2 Jyoti Prakash **24-Jan-2012**

In the second part of our series of interviews with stock market leaders, we talk with Mr. Jyoti Prakash, Senior Fund Manager with AEGON Religare. A graduate from the prestigious IRMA in Anand, he has worked in renowned organizations like Amul and Sahara India. He is amongst the first batch of graduates of the Indian CFA and has been a money manager for nearly 8 years.

Q When was your first encounter with stock markets?

A I did my MBA in 1984-86 when Management as a field in India was still up-coming and the country had only 6-7 institutes. I graduated from the Institute of Rural Management, Anand and worked with AMUL for 3 years before moving into Consultancy. In 1992, after liberalisation era kicked in and financial wave had hit India, I was in the first graduation batch of the Indian Chartered Financial Analyst (CFA). Post that I started working with Sahara India and that's where I first encountered stock markets. Since then I have remained in the industry.

Q What attracted you to capital markets?

A It's all about being competitive. It's about efficient allocation of capital.

Q What has been your learning from stock market over the years?

A I have been managing public money for 7-8 years now; one of the most important things that I have learned is not to get carried away. You do your own research. Read others' research, but have your own conviction. **Things will not always work the way you want them to, particularly in the short term**. In such cases, it is very important to back your judgement. To give you an example, last Diwali, market was very bearish about Bharti Airtel. However I had my conviction. I knew the market was overselling it. Since then, over the last one year markets have fallen by around 15%, while Bharti is up by over 20%. If you have a method to this madness and believe in it, even though markets may beat you over 3 months, but over the long term you will beat the markets.

Q What's your philosophy or strategies for stock market? What technique do you use? How has your technique changed over a period of time?

A It's all about Margin of Safety. Today what margin of safety Maruti offers compared to, say M&M? I believe Maruti, with its strong Japanese value systems, will learn from its mistakes. Therefore I think we will see positive outcome of all this, maybe 6 months down the line. I am not at all into momentum play. If something is going up, I don't blindly get into it only because of that.

Q How do you typically evaluate a stock? What kind of things do you look at it, in any order? Can you highlight 3-4 key things that every analyst should look at?

A The most important thing for me is, a company should not come back to shareholders for money all the time. The company should grow from internal accruals. That is one of the reasons why I don't like financials. For banking to survive and grow, it will need capital all the time and you don't get capital every time you try to raise funds. The second important thing for me is the kind of recurring income that a company has. Let's say BHEL is supplying equipment and probably has maintenance contract also. Now if the share of the latter is higher in the total revenue, I would like it. That way, the business model would be more sustainable. Similarly in Exide, replacement market over time would become much bigger than the OEM market. Now that is something that would interest me. Third is of course the free cash flows that the company is generating. That is something to look at as against just book profits, which may not get converted into cash. And finally RoE, that's what my investor/clients ask me to do.

Q How do you decide when to sell the stock?

A As I have said, I work on the rule of margin of safety. So I keep evaluating if the stock has any upside. If not, why should I keep it in the portfolio? Sometimes, people rush to buy a stock because till now they didn't have it and they believe that's why they were underperforming and they end up buying the stock when they ought to be selling it. **So if you are bit of contrarian and you bought the stock when everybody was dumping the stock because you had longer time horizon and had faith in management and you knew things would turnaround after sometime.** The whole idea of selling is to buy something that has a higher margin of safety.

Q How many market cycles have you seen? How was your experience during that time? Can you share anecdotal stories of your success or failure?

A Today you look at research, where a stock is covered by 30-40 analysts, which was not the case earlier. If you go back in time and look at a stock, let's say XYZ, with a target price of Rs3,500, it was tracked by 4 analysts. Today the same stock is available at 1/10th the price. So I don't know what the analysts saw then and what they see now. At Rs3,500, you felt the stock was expensive. Now it has come down to Rs1,800. You get tempted to make money. You think the stock is cheap now. So it is good that you didn't get carried away by the momentum. However if you bought at Rs2000 you have still lost money. Now let's say you had only 5 stocks in your portfolio and one of them was this XYZ. Imagine the loss you would have made. However if you had 25-30 stocks in your portfolio, your loss would not be as high. You can cover that loss in some other stock. **So, it always pays to diversify wisely**. The major change that has happened is that today when you look at a stock, you look at the quality of the research available and then you take far more judicious decision than you would have 3-5 years back.

Q What makes a successful analyst different from others?

A Again it is about **maintaining balance, not chasing prices**. Raising your target price because stock price has gone up or reducing it because stock price has come down - that is something I have never understood. The other problem an analyst has is that he/she is looking at a particular sector. So the overall context may be lost. For instance, he/she might be bearish on a particular sector but in the overall context one need not be bearish about a stock. For example, there are sectors on which all the analysts are bearish. However I find there is good margin of safety in particular stock. **The other thing is that most analysts focus on the income statement aspect. However, they do not focus on the balance sheet.**

Q What are the major misconceptions that people have about stock market in general and about analyst/ fund managers in particular?

A **It might sound odd, but most people think stock market is very risky. It is very risky if you don't learn you lessons.** If you know, market tends to move between 12x to 20x forward earnings. So if you are buying at valuations of 12x it is much safer than buying at 20x. **I think debt can be equally risky - recent EU crisis is an evidence of it.** I don't think equity is very risky, if one gets the sector right, the sectoral rotation right, right companies in the portfolio and sticks to it and does not get carried away. **Don't get into momentum, don't trade and don't leverage.** General public doesn't like a change in view just because of price movement. That's where people have lost faith. Analyst and fund managers come on the TV talking positive one day and a few months down the line when prices crash, they turn negative. Then people lose faith. Many big brokerage houses have lost creditability due to such acts. One has to be consistent and stick to one's conviction.

Q What do you expect from newcomers to the stock markets? What are the qualities that new participants, especially students should possess for being successful in the stock markets? How should one go about acquiring those qualities?

A **In terms of knowledge of tools, Excel (MS Excel) is something newcomers *must* know.** You have to be very good at it. To become successful in the stock markets, **you have to put in extreme hard work** - you have to sit and study, sit and study. See what is happening around you, internationally. We might be at a stage where international markets were few years back. See how they have evolved. **Continuous reading is the most basic requisite** for success in the stock market. **Stock market is not just about EPS & P/E multiples.** It is much more than that. Try and anticipate things. For example, let's say monsoon is over. What can you make out of it? The swing pattern, which crops will do good and bad – all this will unfold in 6 months' time. But if you can anticipate it, you would be ahead of the curve. Another example is that you look at fiscal deficit numbers. The government is hell bent on doing something about it. So what steps can the government take, how will PSUs get impacted, will minority shareholders get impacted? If you can figure that out, your portfolio would be that much better. Another example is rupee depreciation. If you had looked at the structure of our reserves, structure of debt etc., you could have seen it coming. If you could see that coming and you were geared-up for it, your outperformance would have been unbelievable. So there are a lot of things that move the markets and their knowledge would come only by studying. Many times you read an article for an hour and you say it was a waste, but how do you in advance without reading that? You would realise it later this is not useful because you have already read it earlier. So read and study continuously. That way you would be less surprised by the market and you would know how to react when a situation arises. I read 10 newspapers daily - 6 Indian and 4 international.