D-Street could move 2% on either side on Thursday's Fed outcome

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NEW DELHI: Market participants across the world, including India, will keep a close watch on the outcome of the US Federal Reserve meeting, which will be out later on Wednesday. The Indian market would be able to react only on Thursday, when the market opens for trading after the overnight announcement.

Most analysts say markets have already factored in a rate hike by the US Fed, but a 2 per cent move on either side in kneejerk response to the outcome cannot be ruled out, depending on what the US central bank has to say about its future rate policy.

In all likelihood, the domestic market would see a kneejerk reaction if the US Fed hikes rate on Wednesday night. The quantum of rate hike could be in the range of 15 bps to 25 bps.

"It is highly likely now that the Fed would go for a rate hike. The expected quantum of rate hike is 25 bps. Some people say the rate hike will not happen because of the problems in Greece," said Vikas Gupta, Executive Vice President and Chief Investment Officer at ArthVeda Capital.

"In our view, even if they develop cold feet, then it could be a 15 bps rate hike. But the Fed agenda is to clearly signal that the rates have to be increased now, and will continue in the upward direction over the next two to three years," he said.

The Nifty50 reclaimed its crucial psychological level of 7,700 in Tuesday's trade. The index has strong support at 7,500 level, in case it starts drifting southwards.

"A likely interest rate hike in the US, the first in nearly a decade, could have a symbolic impact on markets across the globe. I would personally guess that with all the talk that has been in the news over the past few months, most of the impact has already been factored in," said Nikhil Kamath, Director for Trading & Risk, Zerodha.

"Whether there is any action or not, we do not expect the market to move more than 2 per cent on either side. After the initial knee jerk reaction, markets are likely to withstand the impact and move back to status quo status shortly," he said.

If the index plunges towards the 7,500 level on Thursday, which is roughly equivalent of a 2 per cent drop from the current level, the slide will halt because of two factors; one, strike price 7,500 has maximum Put OI buildup, which will lend support, and two, FIIs have short positions worth about Rs 6,000 crore in Nifty50 futures.

Out of the Rs 6,000 crore worth of short positions that FIIs have in Nifty50 futures, Rs 2,000 crore has been added in the December series alone, said a report in ET.

In case the market start drifting southward, it may witness short covering at lower levels, as this has typically been the case whenever significant short positions are being built, experts said.

"The US Federal Reserve has already indicated its intention of increasing rates, and the market has discounted the event. We do not expect a very big fall, though a gap-down opening and a kneejerk reaction can be seen in the market," said Rohit Gadia, Founder & CEO, CapitalVia Global Research.

"In case of an interest rate hike in the US, Nifty50 is expected to show a bearish movement, as it would mean a drop in liquidity because of large pullout of funds, or reduction in investment by FIIs," he said.

Gadia expects Nifty50 to breach the support level at 7,550. If Nifty50 sustains below this level, it might show further downside up to 7,200 level, he said.

Deploy 'buy on dips' strategy:

Analysts say investors can use any adverse move in the market to accumulate stocks to build a long-term portfolio. Even though US Fed rate hike does pose a big risk to emerging markets (EMs) per se, India should be least affected because of robust macros.

Large emerging markets that are likely be affected the most include Brazil, Russia, Turkey and, to some extent, South Africa, where severe domestic challenges have contributed to instability in exchange rates and financial markets, Moody's said in a report.

"We expect the Fed to raise interest rates by 25 bps this quarter on improving data coming out of the US. Investors should not get affected by short-term volatility surrounding this event and remain invested in the long-term India growth story," said Vaibhav Agrawal, VP & Head of Research, Angel Broking.

"We believe equities will be the best asset class to remain invested in over the next few years. India remains the most preferred investment destination led by favourable macro cues, such as declining interest rates and falling inflation, cheaper global commodities and a strong government at the Centre, which are likely to drive corporate performance over the next 18-24 months," he said.

Most emerging markets, including India, have been undergoing the process of realignment ahead of the US Fed event. A rate hike by the US central bank may force global funds to withdraw from emerging markets, including India, which may cause the stock markets to decline.

Most FPIs have realigned their portfolios. They have purchased stocks worth Rs 11.22 lakh crore, but sold shares to the tune of Rs 11.07 lakh crore, resulting in net inflows of Rs 15,136 crore ($2.8 billion) for 2015. But, flows from domestic institutional investors have kept the momentum going in the domestic market.

"For Indian investors, this is a great opportunity to buy stocks as the market presents a great opportunity to investors to buy some fundamentally strong stocks at lower levels," said Gadia of CapitalVia Global Research.

"For investors who already have positions, it is advisable to hedge their portfolios for the time being to safeguard against market volatility," he said.