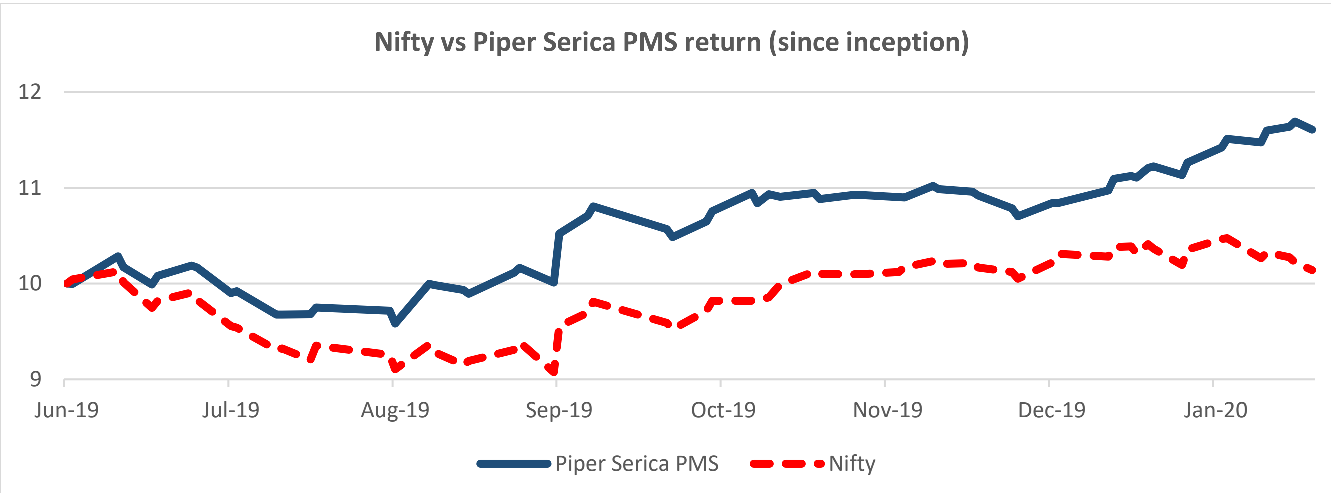
Piper Serica Leader Portfolio Strategy PMS
Investor Letter Vol. IX
February 2020

First Things First

PMS level absolute return for January 2020 was 4.5%[1&2] against -1.3% for BSE Sensex, -1.7% for Nifty and -1.6% for mutual funds. This significant outperformance was due to better than expected quarterly performance by our portfolio companies including United Spirits, Jubilant Foodworks and Westlife Development.

The last eight-month absolute return (since inception) of the PMS is 16.1%, significantly higher than broad market indices (3.3% for BSE Sensex and 1.4% for Nifty) and average of Mutual Funds (3.1%). With our portfolio companies continuing to beat earnings estimates we remain confident that we will continue to outperform the broad indices.



Portfolio Activity

The portfolio is well-diversified and top holdings continue to do well. Nine of our portfolio stocks hit 52-week high in January. We have increased allocation to both the leading QSR companies after excellent operating performance. We also increased allocation to an auto major and two leading beverage companies. We fully exited the depository where we think the growth will be lower than its unlisted competitor. We also exited a leading consumer durable manufacturer after its Porter model score fell below seven in the quarterly update. Our cash holding is at 2.5% of the total AUM and we have no plans to increase it. We continue to see ample long-term opportunities to deploy incremental capital.

Top 5 Stock Holdings	Weightage
Info Edge India	5.7%
ICICI General Insurance	5.4%
Apollo Hospital Enterprises	5.3%
HDFC Life Insurance	5.3%
Interglobe Aviation	4.8%

Top 5 Sectors	Weightage
BFSI	18.4%
Consumer Discretionary	17.6%
FMCG	10.3%
Healthcare	9.2%
Industrials	8.8%

Large Cap	Mid Cap	Small Cap
48.5%	23.9%	27.6%

Note:
1. This is the average absolute return for the entire portfolio. Individual portfolio returns will vary because of timing differences.
2. Calculated by an independent fund accountant on a TWRR basis after taking into account all fees and expenses.

Short- and long-term impact of Union Budget

Stock market has recovered almost fully from the knee-jerk reaction to the Union Budget as we send out this letter. This shows that the budget should be seen only as a statement of government finances and not as a policy tool. The typical but unnecessary over-reaction to budget announcements only creates anxiety and panic for retail investors. Now that the fine print has been read and clarifications provided, investors can focus on the longer-term impact which, according to our analysis, is more positive than negative. Government finances have not deteriorated to the extent it was feared. There are no new populist subsidies. Disinvestment target has been doubled and it will be a challenge for the government to achieve it unless the valuation of PSUs improves significantly. There is no further increase in market borrowing by the government and this has already led to a fall in yields. Overall, in a low growth environment we would say “no bad news is good news”.

Impact of Coronavirus on global markets

The full negative impact of Coronavirus on global businesses, the Chinese economy and global markets will remain uncertain till the virus is contained and number of new cases comes down. Till then, companies that import critical components and raw material from China will see disruption in their production schedules. A slowdown in Chinese economy will have massive cascading downward impact on prices of commodities. Central banks are likely to react by increasing the supply of money to ensure there are no shocks to their economy. While we would never look for a silver lining in a life-threatening epidemic, Indian businesses that are not dependent on Chinese supply chain may actually become more competitive as international buyers look to reduce their dependence on China. However, Indian companies will still have to do a lot of hard work to convert this short-term opportunity into a long-term competitive advantage. The fall in commodity prices, especially oil, will also help reduce our import bill. But these advantages may be fleeting, till the cure to the virus is found and normalcy returns in China. We can only pray that a cure is found quickly, and the virus is contained.

Adding a new analytical tool

We are adding a new methodology to our analytics arsenal. The Porter model has helped us analyze the competitive position of our portfolio companies and make excellent forecasts of short- and long-term business performance. We are now working on overlaying the Brand Asset Valuator (BAV) methodology developed by Young and Rubicam to analyze the brand strength of our portfolio companies. Through this model we will be able to interpret brand patterns through a progression of four primary measures – differentiation, relevance, esteem and knowledge. We will be happy to discuss this tool and its impact on our analysis in greater detail when we get an opportunity to meet you.

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