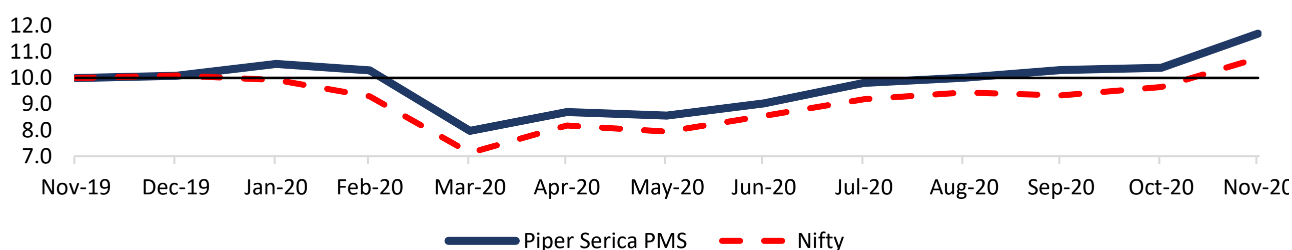
First Things First

PMS level aggregate absolute return for the three-month period ending November 2020 was 16.9%[1&2] against 14.2% for Nifty, 14.3% for BSE Sensex and 13.7% for multi-cap mutual funds. Nifty 500 index returned 14.6% during the same period. Trailing one-year return for the PMS is 16.9% compared to 8.7% for Nifty, 8.2% for BSE Sensex and 4.0% for average of multi-cap mutual funds. The annualized TWRR for the PMS since inception is 19.4% compared to 7.3% for the Nifty.

Nifty vs Piper Serica PMS monthly return (trailing 12 months)



Source: Piper Serica PMS, Thomson Reuters

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

Portfolio Activity

We completely exited the two alcohol based beverages companies. While we are positive in the long-term prognosis of the businesses we believe that they will face severe headwinds in the near future. The biggest headwind is in the form of excessive and arbitrary government control at each stage of the business. State governments tightly control the retail distribution thereby making it impossible for these companies to access their customers directly. In addition there are arbitrary taxes and prohibitions. The on-line distribution opportunity has turned out to be a damp squib. We were of the view earlier that government control over this industry will get diluted but the reality has turned out to be *au contraire.*

We replaced these companies with two companies that we had in our portfolio earlier but we exited at the time of Covid-19 peak fearful of lasting damage to their business. Both the companies, one the leader in residential real estate and the other the leader in specialised structural steel products, saw a remarkable jump in their Porter model score after the recent quarterly results. Both companies invested aggressively through the lock-down period, reduced costs and further improved their dominant market share. We ended the month with a comfortable cash holding of ~7.0% (*this is the average cash holding for the entire PMS and individual accounts may have different levels of cash*).

Top 5 Stock Holdings	Allocation*
Dixon Technologies	7.7%
Apollo Hospital Enterprises	7.0%
HDFC Bank	6.3%
Titan Company	5.8%
ICICI Lombard	5.8%

**including cash in the portfolio*

Top 5 Sectors	Allocation*
Financials	33.1%
Consumer Discretionary	15.9%
Healthcare	11.9%
Consumer Staples	10.1%
Industrials	7.7%

Large Cap	Mid Cap	Small Cap	Cash
54.8%	16.4%	21.7%	7.0%

Risk Adjusted Performance *(since inception in June 2019)*:

	Annualized Return %	Ann. Std. Dev.	R-Squared	Sharpe Ratio	CAPM Beta	Treynor ratio	Jensen's Alpha
PMS	19.4%	24.7	0.9	0.8	0.9	24.1	11.3
Nifty	7.3%	27.4	1.0	0.4	1.0	10.8	0.0

Note: Risk adjusted performance gives a complete picture of the PMS performance by measuring the amount of risk taken for the return generated.

© 2020 Piper Serica Advisors Pvt. Ltd. | www.piperserica.com | Private and confidential, not for public circulation.

The emerging Goldilocks scenario

What a difference a month makes. There was the month of March when the Nifty fell 23.3% and investors could not wait for the month to get over. Now investors reluctantly bade farewell to November after the Nifty gained 11.4% and hit its all-time high. There are multiple reasons for this sharp rise in the markets and many of them will continue to play out in 2021.

1. FPI inflow at USD 8.2 billion was the highest ever in a month. We expect that these flows will continue to be strong as the amount of global debt with negative yields has more than doubled to $16.3 trillion in the past seven months and is driving a massive chase for yields. Rotation of funds from Developed Markets to Emerging Markets has already started, and we expect it to pick up pace over the next couple of quarters. EM's have seen their highest ever increase in total value by USD 8.3 trillion since the March lows. The MSCI EM index has outperformed the DM index. It is a given that the DM central bankers will continue on their stimulus path. Unless inflation kicks in, this will keep global yields at their historical lows and drive further flows to EM's in search of yield.
2. The sudden announcements related to Covid-19 vaccines have forced a massive rotation of funds from risk-averse to risk-on. Defensive assets like precious metals have sold off as funds moved into equity funds. Unlike the US and the Europe, India has so far not witnessed a big second wave despite mass-scale opening up across the country.
3. Quarterly results for quarter ending September have been significantly better than expected. Profitability growth has out-stripped sales growth as the companies focused on cutting costs and improving balance sheets by reducing debt and improving the working capital cycle. Left with no choice, customers have rapidly adopted digital channels.
4. Improvement in macro data has been better than expected. The GDP growth forecasts have been hiked across the board. INR has strengthened despite RBIs constant USD purchase. Trade deficit has narrowed. Employment situation has improved and various industry verticals like autos and real estate have witnessed a sustained pick-up in demand.
5. Support by the government through policy measures like the PLI scheme that will give Indian manufacturers, across industries, a level playing field and help them build the scale and track-record that is needed to compete at the international level. The support provided to MSME's through moratorium and other measures went a long way in stabilizing this extremely sensitive part of the economy that not only generates the largest employment but also drives the consumption engine.
6. Rural economy has bounced back much faster than the urban economy. It has not been ravaged by Covid-19 and benefitted from one of the best monsoon seasons. It has also got access to cheap capital as banks and NBFC's have made further inroads into rural areas through digital channels.
7. While Indian equity market has rallied hard in the last couple of months, it is still not overvalued by historical standards. It is currently trading at ~20x FY2022 estimated EPS. The earnings are now being upgraded and this has led to many foreign brokerages upgrading the Nifty targets.
8. An interesting data point that all long-term investors in India should consider is the change of weightage of China in the MSCI Emerging market index. Korea and Brazil had the highest weightage in this index till 2014 when China took the top spot. From 2007 to 2014 the weightage of China grew from 10.6% to 14.8%. From then the weightage has jumped to more than 40% eclipsing all other countries in the Index. The weightage of India has increased from 6.6% in 2007 to 9% now. Korea and Taiwan are ahead of India with a weightage of appx. 12% each. As India starts firing its growth cylinders, and its capital markets become deeper, more liquid and more transparent we believe that the weightage of India will rise rapidly over the next couple of years to close to 15% and this will ensure index-driven FPI flows into India.
9. The last point is controversial because a lot more people believe that India will never be able to replicate China's economic performance. India's recent economic performance, hit by three disruptive events – demonetization, GST and Covid-19, has been well below par. However, so was the case with China before it hit its growth curve. Now, for the first time, there are more Fortune Global 500 companies based in Mainland China and Hong Kong than in the U.S. – 124 vs. 121. This is significant because when the Global 500 list first came out in 1990, there were no Chinese companies on the list. In the intervening three decades, the Chinese economy has skyrocketed. China's share of world exports hit an all-time high of 14.2%

in August. It contributed 30% of global economic growth in 2019 and is one of the few countries that will report a positive growth in 2020.

It is indeed a massive leap of faith to believe that growth of Indian GDP can follow the last 15-year growth of the Chinese economy. However, we cannot ignore that there are two similarities. Firstly, we have similar demographics – a young population that is ambitious and looking to improve its standard of living. Secondly, China's collapse has been predicted multiple times by the Western commentators but China has always emerged stronger from each crisis and has increased its share of the global GDP.

What can derail this emerging 'Goldilocks' scenario:

1. Re-emergence of wide-scale lockdowns in case Covid-19 spirals out of control. This is a risk till the vaccine is made widely available. Probably by mid-2021.
2. A black swan event that leads to a global liquidity squeeze. We saw this happen in 2008 when the US sub-prime market blew up and froze the global financial system. This kind of event is difficult to predict.
3. Escalation of situation at any geo-political hot spot. The world is currently infested with zones where wars can erupt at any point of time. In an inter-connected world, it is unlikely that these wars will be limited to only the two warring countries.
4. Emergence of sharp inflation due to continuous stimulus to drive demand and a simultaneous shortage of commodities. It will lead to roll-back of stimulus and will impact the importers of commodities in an extreme manner. It will have a very negative impact on trade balance and exchange rates of emerging market countries.

What should investors do?

1. Market volatility will remain high for the next 2-3 months. There will be days when the markets will swing 2-3% either way. Investors will do well to not take any knee-jerk action and maintain their asset allocations.
2. Ensure that portfolios are optimally diversified. Better to have diversified rather than concentrated portfolios in times like these.
3. Ensure there is adequate liquidity in the portfolio. Illiquid investments lose value more rapidly when markets freeze.
4. Remove all underperforming investments that have significantly underperformed the recent rally. These investments hardly ever catch up later and continue to pull-down portfolio returns.
5. Increase allocation to equity by 5-10% by shifting from low return fixed income investments to high quality equity portfolio that will yield a much higher return.

The team at Piper Serica wishes you a great holiday season. 2020 has been a tough year for everyone, despite the recent performance of the markets. We hope that the festive month of December will bring all the happiness and cheer that was missing from the rest of the year!

Abhay Agarwal, Founder & CIO	Rajni Agarwal, Director, Research

© 2020 Piper Serica Advisors Pvt. Ltd. |www.piperserica.com | Private and confidential, not for public circulation.