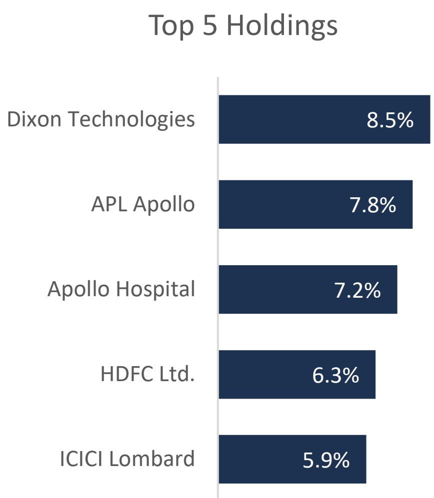
Piper Serica Leader Portfolio Strategy™

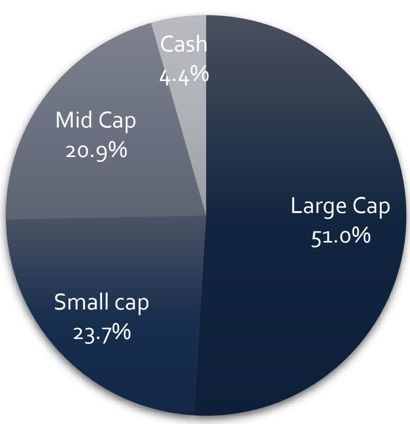
Investor Letter Vol. XXIII

April 2021



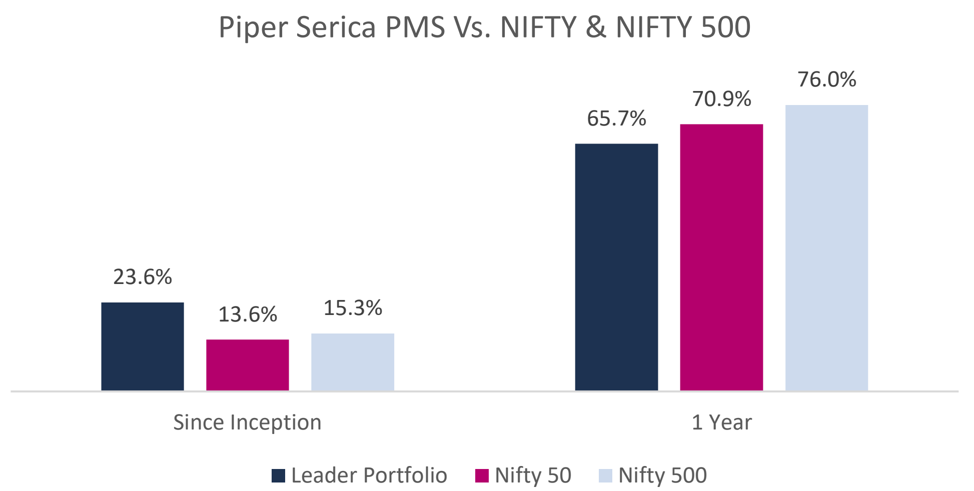
Top 5 Sectors	Allocation*
Financials	29.3%
Consumer Staples	15.8%
Technology	11.1%
Consumer Discretionary	10.1%
Industrials	8.5%

**including cash in the portfolio*



First Things First

PMS level aggregate absolute return for the month of March 2021 was -0.3%[1&2] against 1.1% for Nifty and 0.8% for BSE Sensex. Nifty 500 index returned 1.1% during the same period. Trailing one-year return for the PMS is 65.7% compared to 70.9% for Nifty, and 68.0% for BSE Sensex. The annualized TWRR for the PMS since inception is 23.6% compared to 13.6% for the Nifty.



Source: Piper Serica PMS, Thomson Reuters

1.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 considering all fees and expenses.

Portfolio Activity

There were no major changes to the portfolio in March. We have reduced allocation to certain large cap defensive stocks and increased allocation to Internet based companies.

We have started adding two new companies to the portfolio – India's only listed depository and India's largest contract staffing company. We see a very long runway of growth for both these companies based on a very strong business franchise and rapidly growing demand for their services. Both have excellent management and corporate governance. Their services model generates positive cash flow that they are able to reinvest in their business at high ROCE. Both companies score high on our Porter model analysis.

Our cash balance at PMS level is 4.4%, though it is much lower in older accounts that are almost fully invested. We do not plan to increase our cash allocation.

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	23.6%	23.8	0.9	1.0	0.9	27.2	9.9
Nifty	13.6%	25.7	1.0	0.6	1.0	15.9	0.0

A look-back at FY 2021

FY 2021, with its high volatility, was quite an experience for our firm. It tested and then rewarded our temperament, discipline and investment process. While March 2020 was a month of extreme uncertainty the recovery from thereon was something that none of us expected. We normally do not take cash calls but when we realized by mid-March that Covid-19 was becoming a serious threat we fully exited some of our holdings like Interglobe Aviation, PVR, Phoenix Mills, Jubilant Foodworks and VIP that we thought were most exposed to lockdown related consumption slowdown. As a result, by end of March and for most of April our cash holding was more than 30%.

We deployed these funds equally quickly into companies that we thought will successfully transition their business models and will emerge stronger from the lockdown. We increased our allocation to Apollo Hospitals, HDFC Life Insurance, ICICI Lombard, MCX and Info Edge. We added new stocks like Dixon and Indiamart.

While we were cautious because of the rising number of Covid-19 cases we were also encouraged by the response to the lock-down by our portfolio companies. We saw almost all of our portfolio companies use their balance sheet strength and leadership position to invest in supporting their supply chains and distribution networks through the lock down. We more than doubled our research activity by engaging with industry stakeholders – distributors, suppliers, bankers, competitors etc. of each of our portfolio companies. We realized two important things. First, our portfolio companies were gaining tremendous loyalty from industry stakeholders by supporting them through the time of stress and second, a mindboggling rise in digitization was redefining old business processes. Both these key takeaways encouraged us to stay invested and ignore the market volatility. This decision has played out well as almost all our portfolio companies have increased their market share as demand has picked up.

Equally importantly, we got great support and encouragement from our investors who not only held on to their positions but also used the opportunity to increase allocations. As a result, we out-performed the indices on a cash adjusted basis while having much better risk-return ratios.

Interestingly, our investment process did not fail even once through the extreme volatility. In fact, the only mistake we made was when we did not adhere to it fully at times of panic. Our biggest learning over the last year is that we should not try to over-ride our investment process that has a built-in risk management system, and which has worked very well for us for more than a decade.

A mistake that we corrected mid-year was our investment in alcoholic beverage companies. We exited them after they rated poorly on the Porter model for two quarters consecutively. While they have great brands, management and customer demand, the industry is over-regulated right from the raw material procurement stage to distribution stage. With such regulatory hostility it is difficult to see how these companies will create value for shareholders.

Our average cash holding has been well under 10% for the last year and churn was about 25%. We expect the cash levels to be about 5% going forward and churn to reduce further. We will continue to look for companies that are using digital tech to grow and are disrupting their own industries. We are very positive on healthcare, consumer Internet, insurance, financial services and outsourced manufacturing industries.

Impact of second wave of Covid-19 on markets

We believe that the Covid-19 second wave will negatively impact the market sentiment for the next couple of months and will provide another good entry opportunity for long term investors. While the numbers are rising rapidly, the new strain is believed to be twice as contagious but only half as lethal. It is quite standard for a weakening virus to infect a lot more people in the second wave and then gradually lose its potency. With rapid vaccination and more testing, we believe that the numbers will rise in the month of April and will then start dropping again. While the numbers are rising, one can expect localized restrictions and maybe even some lock downs.

On the other hand, the near-term economic data is quite encouraging. GST collections and issuance of e-invoices are at their highest ever. Direct and indirect tax collections have exceeded estimates. Exports and imports are rising fast. Financial services are getting digitized rapidly as evident from record breaking UPI transactions. Real estate sales are breaking records supported by stamp duty breaks and all-time low borrowing costs. Auto sales have picked up after the slump. Consumer electronics, especially under-penetrated categories like air-conditioners, are seeing robust sales. At the same time, we expect inflation to pick up in the near term due to a very rapid rise in prices of basic commodities.

We encourage the long-term investors to use the market volatility as an opportunity to increase their equity allocation. There will always be red herrings like Covid-19 second wave, increase in interest rates, inflation etc. However, almost all of these have a way of working themselves out. We expect the interest rate on small savings will fall despite the recent roll-back. Small savers will be forced to increase allocation to equity to increase their overall returns. We also expect foreign investors to continue to invest in India as the weightage of India increases in MSCI indices.

With that, we wish our investors the best of returns in the new financial year.

Abhay Agarwal,
Founder & CIO

Rajni Agarwal,
Director, Research