Piper Serica Leader Portfolio Strategy™

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Portfolio performance

The since-inception (June 2019) TWRR for the PMS is 15.8%. This compares favorably with our benchmark Nifty that returned 12.2% over the same period. Our standard deviation is at the same level and CAPM beta is well below that of the benchmark and our Sharpe ratio is well above, as detailed in the factsheet.

We are happy to inform you that after a brief period of underperformance compared to our benchmark, our portfolio performance has picked up. The PMS generated a return of 14.8% compared to 8.3% for the Nifty during the last quarter.

Our monthly factsheet can be downloaded here.

Markets update

Last month saw a correction in markets across the world. Largely due to continued high inflation, especially in the US. Central banks, led by the Federal Reserve, have aggressively increased rates and are maintaining a hawkish stance. It is clear now that the central banks will prefer to risk recession if that is needed to tame the price rise. RBI also took the cue and announced a sharp increase in rates. The result of this increase, especially in the US, is that yield curves have inverted after a long time. This means the short-term rates are higher than the long-term rates. In classic economics, this is a strong indicator of an upcoming recession. It is a moot point how long and deep will the recession be, but it will negatively impact the customer demand, especially for the premium and high-priced products, as customers trade down.

With an aggressive increase in interest rates, the USD exchange rate index hit a 20-year high. There was sharp and deep fall in many leading currencies against the USD, notably the GBP and the Yen. The Chinese Yuan also traded below a critical sentimental level. While the INR also hit an all-time low, its depreciation has been 5% lesser than the depreciation of other currencies.

Only fixed income savers welcome an increase in interest rates. Other than that, rate hikes are not very popular, especially with businesses that see their cost of capital go up. With consumers, there is lesser inclination to go for discretionary spends with borrowed money. Therefore, very sharp rate increases can lead to a demand shock and may materially impact the emerging economies that depend on export-led growth.

The good news is that supply chains are getting back to normal. There are some hot spots like Ukraine and China but overall, there is faster and more efficient movement of goods around the world. The global trade is normalizing as the freight rates fall sharply across the board. This will help further reduce the inflationary pressures.

We expect that global investors will watch the yield curve in the US very closely for assessing the risk of a long recession. We believe that a smoothening of this inversion over the next couple of months will bring investors back into risk assets, especially emerging markets, as the narrative will change from recession to growth.

More importantly, India has weathered the storm exceptionally well. Almost all our markets have significantly outperformed our peers. There is a school of thought that says that this outperformance will not last. We differ. We believe that India has a lot going for it and should be seen as a long-term growth story. Other than very favorable demographics there are many factors that will drive this growth. Our domestic consumption is just starting to pick up. While our services exports have always been robust, our manufacturing exports are also becoming competitive. We believe that the share of India in the MSCI Emerging Markets index will continue to increase leading to large passive FPI flows. The inclusion of India in the global bond index will be another big trigger for flows from global bond funds thereby reducing the cost of capital for Indian companies.

Our view on Indian markets is more sanguine than most market commentators. Our view is based on the on-ground reality that we see as we engage with various distributors and retailers of our portfolio companies. There is optimism about sharp recovery in consumer demand based on enquiries. Discretionary demand for real estate and autos is recovering sharply. Business travel is back with full intensity. Private sector capex is picking up and credit demand has hit multi-year high. This gives us the confidence that economic activity levels in India will stay elevated over the next year and beyond. There are various other trigger points for growth that include launch of ONDC, expansion of PLI schemes, implementation of the National Logistics Policy, launch of 5G network etc. Each of these will add to the growth momentum.

Portfolio update

During the month we added a PVC pipes and fittings company to the model portfolio with a 3% allocation. The industry itself is expected to grow at a >15% CAGR over the next 5 years with increased demand from sanitation, sewage, plumbing, irrigation, water distribution, bath fitting and infra industries. The company is the smallest player in the industry but also the fastest growing. It is expanding its footwork across the country and is using the distribution network of its sister company that is a leader in the structural steel pipes. We are already familiar with the business group since we have the sister company in our portfolio for a very long time. Based on our research, we are quite confident that this company will be able to increase its market share from low single digit to double digits within next 4 years. We expect the company to grow from a small-cap to a mid-cap during the same period.

To make room for this company in the model portfolio we have marginally reduced the allocation to an ultra large cap and a mid-cap company. We believe that the returns from these two companies may be lower than other portfolio companies since their valuations are in the 'rich' zone already.

Other than that, we have marginally increased allocation to a large cap IT services company and a private bank. Both are undisputed leaders of their industry are attractively priced for the long term.

Our cash position at PMS level is down to 6.4%. We are not expecting any significant portfolio churn soon.

Best wishes from our team for the most auspicious month for Hindus. We wish you a very auspicious Vijaya Dashami and a very Happy Diwali and New Year. May the Lord remove all darkness from our life and fill it with long-lasting brightness!

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