



## This too shall pass: June 2022 Newsletter

### Toughest quarter since onset of Covid

India stock market declined sharply during Apr-Jun 2022. An early indication of this possibility was provided when broader markets started to correct in the previous quarter. Inflation and fears of possible recession were the most talked about issues, even as the Russia-Ukraine conflict lingered on.

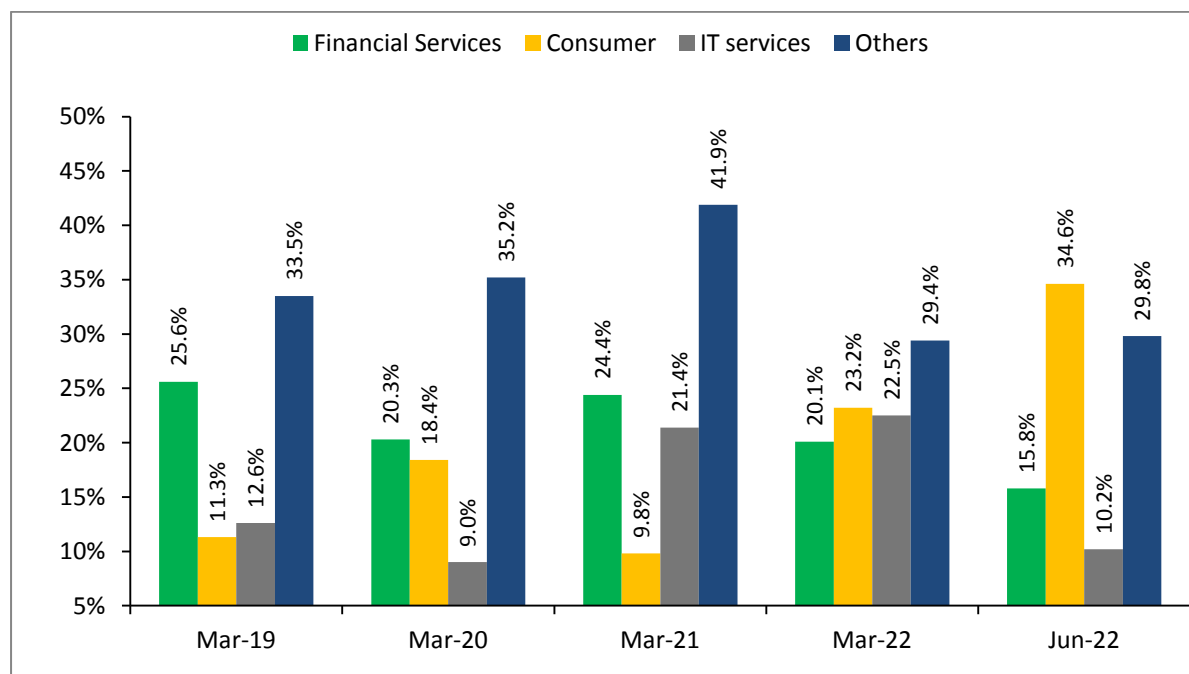
Ampersand bettered most indices during the period under review, including Nifty and Mid caps. Fund NAV was down 8.5%, benchmark BSE 500 declined sharper at 10.0%. Our fund has delivered cumulative returns of 95.5% since inception in Sept 2017, ahead of all major indices.

As on June 30, 2022, our fund consists of 26 stocks and a cash surplus of 9.6%.

### Portfolio positioning aided our relative outperformance

Our relatively stronger performance in an all-round declining market, is attributed to (1) dilution of our overweight position in IT to neutral stance, (2) absence in metals, (3) higher cash levels compared to the previous quarter. Also, we managed to partially re-deploy cash closer to the June lows. Still, the portfolio was not immune to sharp market correction, which ensued during the quarter under review.

Chart 1: Portfolio rebalanced in favour of Consumer sector



Source: Ampersand Fund Data



## Recession concerns overdone

Most economists are ascribing a 30% probability of US recession in 2023, and even Governor Powell isn't ruling out the same. In our view, barring a dramatic escalation of Russia-Ukraine conflict, chances of protracted recession appear remote. However, we are building a base case scenario of much slower growth, with moderate inflation outlook over next two years.

During 2018 and 2019, USA GDP grew 2.9% & 2.3% respectively with Fed fund rate in the 1.4%-2.4% range, similar to fund rates being targeted for next one year.

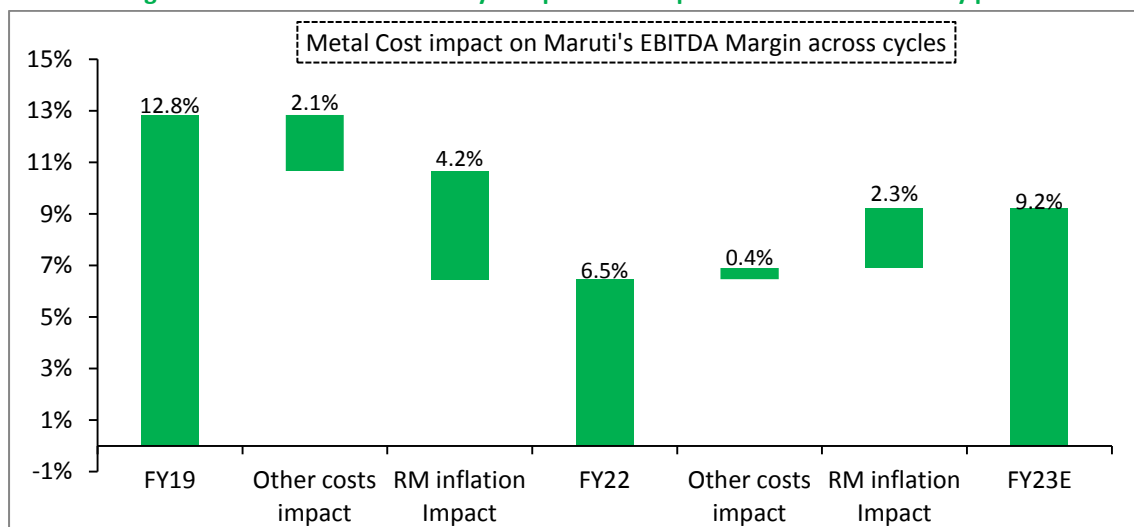
Sharp hike in interest rate by Fed in recent months is already driving down commodity prices. Global supply chain is easing considerably, reflected in falling shipping rates. This should enable inflation to soften to targeted levels over the next few months. As such, one need not fear excessive hawkish policy from Fed than already articulated. An indication of this is evident through peaking of 10 year bond yields.

India markets in recent times are strongly correlated to developments in the US, so will likely recover along with return of risk appetite. Considering India's macro fundamentals, we expect relative outperformance to sustain in the recovery phase as well.

## Domestic consumption sector supported by tailwinds

Typically, easing of inflationary pressures should be positive for consumer related sectors, both from a margin and demand perspective. Sectors which bore the brunt of dual impact were mostly discretionary such as Autos and Building materials such as Cement, Paints etc. Demand situation is now looking good given robust jobs growth in urban India, as reflected in rise in personal tax collections, fresher hiring by IT companies and surge in new EPF subscribers. On the other hand, non-durables i.e. FMCG companies should benefit from lower input costs due to softening of palm oil, chemicals etc. So collectively, consumer and related sectors could emerge as growth leaders, while commodities should lag. Ampersand made a strategic shift from IT to the Consumer space during the period under review.

**Chart 2: Margins of Consumer Discretionary companies to expand on lower commodity prices**



Source: Screener.in, Ampersand Research Estimate



## Dynamic portfolio management needed still

Several imponderables could influence inflation as well as demand, so linear extrapolation of drivers of macro-trend is a key risk. For instance, an early end of Covid could significantly ease supply chain logistics, and thereby bring down inflation faster than being currently feared. Similarly, further escalation of the Russia-Ukraine conflict can aggravate energy costs and lead to certain recession. Under such circumstances, investment strategies would necessitate constant monitoring and frequent tweaking. In order to minimise such an eventuality, diversity has been a constant feature of our portfolio construct this year. We believe this could make our portfolio more resilient to global turmoil.



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