

## Something's gotta give – September 2019 Newsletter

### Decent show amidst high volatility

We completed 2 years of active fund management this September. Since inception, NAV is up 18.1%, bettering benchmark BSE500, which was up 9.9%, and significantly ahead of small and mid-cap indices. During the first year, our performance was constrained by skewed exposure to small/mid-caps. Corrective action to a more balanced portfolio enabled us to deliver 9.4% post-tax return over the past 12 months (vs BSE Sensex up 7.7% and BSE 500 up 2.7%).

The quarter under review has been equally challenging. Markets confronted weak economic activity and a tepid budget with a sharp decline right through until mid-September. And when most market participants had more or less reconciled to continuing bearishness, the Finance Minister undertook a historic corporate tax related reform. Consequently, broader markets largely made up for earlier losses with the BSE Sensex/Nifty ending with a quarterly decline of around 1%. Our fund performance during the quarter, we dare say was exemplary (up 2.7%, also comfortably beating BSE 500 (down 1.8%).

Our AIF portfolio comprises 30 stocks and our investible cash surplus stood at 8.2% (down from ~18% in the previous quarter).

### Recovery delayed, but not stayed

Notable headlines which occupied mind space during the quarter were (1) sluggishness in the domestic economy, as reflected in macro data as well as cautious corporate commentary, and (2) continuing impasse in US-China trade war. Damage to oil facility in Saudi Arabia too briefly shook markets. The abrogation of parliamentary Act in the state of J&K was a significant development, but could have geo-political ramifications over the medium term.

Of the above, our markets were singularly influenced by domestic economic situation and the seemingly lack of government initiatives to deal with it. Which is why we consider the sharp reset on corporate tax rates as well as tax incentives for new capex to be a structural game changer in the long run. However, this doesn't alter the economic reality near term where industrial output continues to realign to subdued demand. We also believe that recovery will likely be delayed to end-FY20/early-FY21, as the benefits of lower interest rates and taxes should take a couple of quarters to materialize. Assuming global situation does not take a turn for the worse, our strategy would be to buy into all such possible dips to ride our expectations of much better economic environment in the coming years. Interim results in Oct/Nov will likely give us that opportunity.

### Hits outscored the misses

Our fund outperformance was aided by themes we have backed over the past year, (1) financials, and (2) consumption. While banking indices registered the largest quarterly decline in nearly 3 years, we managed to register marginal gains in our holdings, driven by a corporate bank in the private sector and couple of high quality NBFCs. We did however face reverses in an HFC as well as a corporate bank where asset quality disappointed. In the consumption basket, our holdings in durables and staples, both fared well, but in line with the respective indices. Our discretionary portfolio, mainly auto ancillaries, fared poorly as did investments in the pharma/healthcare space, but again this was in line with performance of respective sectoral indices. The sector to hurt us sizably was cement, as both demand and pricing turned adverse resulting in weak stock performances.

### Core portfolio unaltered, capex revival potential theme ahead

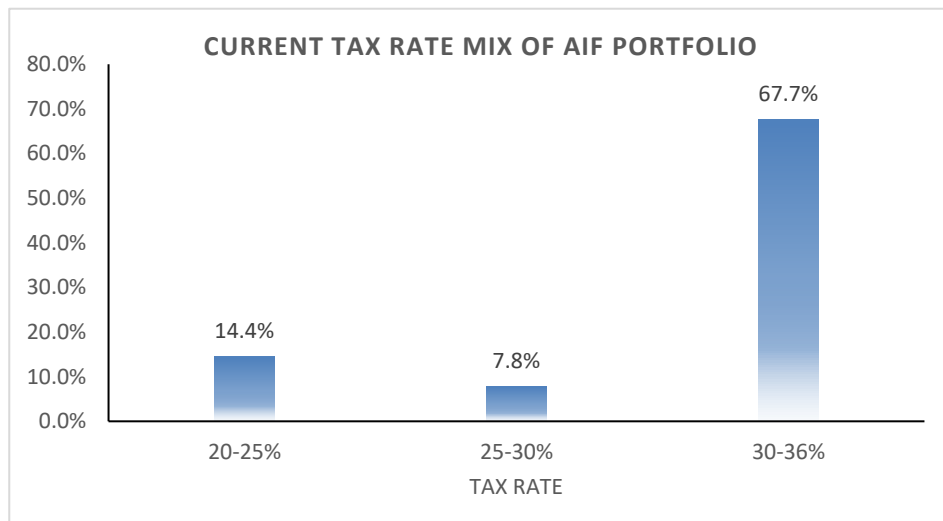
In the previous newsletter, we had indicated our intention to utilize cash surplus on market corrections to take advantage of likely economic recovery from H2 FY20. During the quarter under review, our portfolio evolved as we had strategized, with cash surplus being partially utilized for incremental investments - we would have invested more, but held back on revised expectations of recovery prospects. We had 5 net additions during the quarter, which mostly represent the tail end of our portfolio as of now. Portfolio alterations include:

1. Substitution of US dependent generic pharma company to couple of names catering mainly to the domestic market
2. Addition of a dominant player in the oral healthcare category of consumer staples, driven by diminishing competitive intensity and new product introductions
3. Exit of a corporate bank which had disappointed on asset quality, which in due course may be replaced by another segment in financials, either insurance or asset management space
4. Retaining exposure to cement and auto ancillaries, both near bottom of the economic cycle
5. In capital goods and construction companies, we continue to be represented by small/mid tier names but may look to move up to proxies after recent tax reforms which could encourage capex and investment in new factories.

**Our portfolio significant beneficiary to tax reforms**

The sharp spurt in markets recently was solely due to the direct tax benefits provided to the corporate sector. Recent announcements by government to cut corporate tax rates will lead to over a 10% upgrade in earnings expectations of our existing holdings. As seen from Chart 1 around two-third of our portfolio in terms of weightage have an effective tax rate exceeding 30%. Apart from benefit of lower tax, these companies will likely utilize excess free cash towards higher investments, leading to faster growth.

**Chart 1**



Source: Ampersand Models & Screener

**DISCLAIMER:**

*Ampersand Capital Investment Advisors LLP (Ampersand) is an Investment Manager of Ampersand Growth Opportunities Fund Scheme – I (Fund), a Scheme of Ampersand Capital Trust registered as a Category III – Alternative Investment Fund (AIF) under the SEBI (Alternative Investment Funds) Regulations, 2012.*

*This document is strictly for information and illustrative purposes only and should not be considered to be an offer, or solicitation of an offer, to buy or sell any securities or funds or to enter into any contribution agreements. Before anyone considers an investment, it is important to read through and understand the contents of the Disclosure and/or Offer Document.*

*This document does not constitute or is not intended to constitute an offer to buy or sell, or a solicitation to an offer to buy or sell financial products, units or securities. The information provided by Ampersand is obtained from sources believed to be reliable but is not guaranteed as to accuracy or completeness and expressly disclaims all warranties and conditions of any kind, whether express or implied.*

*This document is prepared by Ampersand strictly for the specified audience and is not intended for distribution to public and is not to be disseminated or circulated to any other party outside of the intended purpose. This document may contain confidential or proprietary information and no part of this document may be reproduced in any form without its prior written consent to Ampersand. If you receive a copy of this document and you are not the intended recipient, you should destroy this document immediately.*

*Any dissemination, copying or circulation of this communication in any form is strictly prohibited. In preparing this document, Ampersand has relied upon and assumed, without independent verification, the accuracy and completeness of information available from public sources. Accordingly, neither Ampersand nor any of its partners, employees, agents or advisors shall be liable for any loss or damage (direct or indirect) suffered as a result of reliance upon any statements contained in, or any omission from this document and any such liability is expressly disclaimed.*

*Investments in Shares and Securities are subject to market risks and investor's risk profile. In making an investment decision, Investor must rely on their own examination of the terms of the offering, including the merits and risk involved. Past performance may not be indicative of future results. Therefore, no current or prospective client should assume that the future performance will be profitable or equal to corresponding indicated performance levels. There is no assurance or guarantee that the objectives will be achieved. No client or prospective client should assume that any information presented in this document as the receipt of, or a substitute for, personalized individual advice from the registered adviser or any other registered investment professional.*

*All intellectual property rights emerging from this newsletter are and shall remain with Ampersand. This is for your personal use and you shall not resell, copy, or redistribute the newsletter or any part of it, or use it for any commercial purpose.*