MULTI-ACT

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PMS NEWSLETTER | Sept-2020

Moats & Special Situations Portfolio

NARROWING ROOM FOR A NEGATIVE SURPRISE

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Date: 5th Oct 2020

Dear Investors,

Below is the performance of the Moats & Special Situations Portfolio (M&SSP) as of 30th Sep 2020.

Portfolio Performance	Equity Allocation as on 30-09-20	Total Portfolio Returns	Benchmark Returns
Since Inception (annualised)		13.5%	9.0%
Sep 2020 Quarter	74%	8.9%	12.0%
1 Apr 2020 – 30 Sep 2020		31.5%	37.2%

- Benchmark is an average of the BSE 500 and BSE Mid Cap index. Benchmark Performance is calculated using Total Return Indices.
- Equity allocation mentioned above is for older accounts.
- The above returns are consolidated for all clients, time weighted and post management and performance expenses.
- The actual returns of clients may differ from client to client due to different portfolio and timing of investment.
- Past performance is no guarantee for future performance.
- Inception Date is 27th January 2011.

The strong rally that started in April continued in the current quarter. While it would be too early to say that markets have turned frothy, there is certainly a sense of complacency that we are seeing in the market. We have witnessed this rally despite consistent increase in Covid cases over the months. The active Covid case count has started declining only in the later part of September. In September most independent research organisations and rating agencies have downgraded India GDP outlook for the full year. The revisions were due to sharp GDP contraction in June quarter. The revisions indicate that economic impact of the lock down could be far worse than anticipated earlier. But while most agencies lowered GDP estimates, market touched the highest point in the current quarter, a few percentage points away from January peak. This indicates that market is no longer concerned about the health crisis and is assuming the worst in terms of economic impact is behind us. High frequency data certainly has been encouraging and is indicating that the economic activity is recovering from the crisis. But there is a disconnect in the extent of market recovery and economic recovery.

India Full Year GDP Growth Estimate:

Organisation	Earlier	Latest
OECD	-3.7%	-10.2%
S&P	-5.0%	-9.0%
Moodys	-4.0%	-11.5%
Fitch	-5.0%	-10.5%
Nomura	-6.1%	-10.8%
Crisil	-5.0%	-9.0%
ICRA	-5.0%	-9.5%
India Ratings	-5.3%	-11.8%

One reason for this, which we have also discussed in our June Quarter Newsletter, is liquidity. There is abundant liquidity globally due to massive monetary stimulus that has been unleashed by US Federal Reserve and other Global Central Banks leading to asset price inflation. This is one of the driving force of the rally upto August. But it was surprising to see resilience in the market even though both FIIs and domestic Mutual Funds were net sellers in Equities in month of September.

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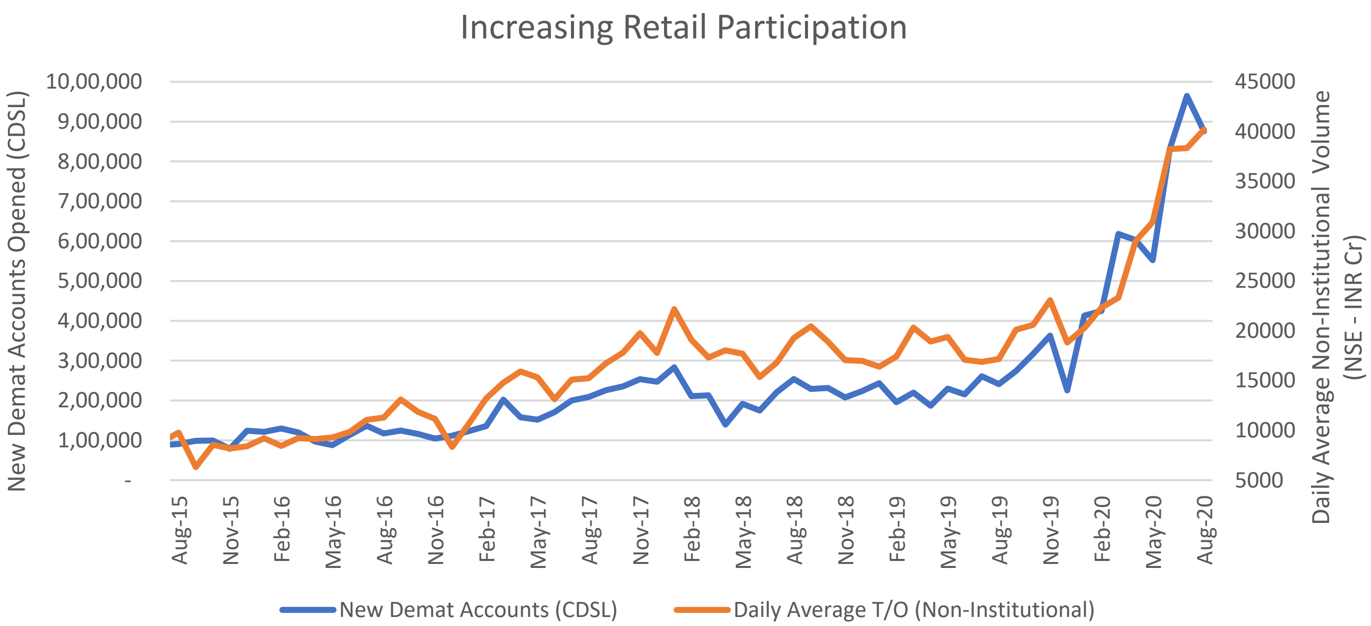
The reason for such resilience could be attributed to increasing participation of non-institutional (retail) investors in the market. There has been a sharp jump (~3x) in new Demat account openings recently (refer to blue line in the chart below) due to proliferation of discount brokers and the easing of account opening process during the lockdown. The share of non-institutional investors in the average daily volumes is at multi-year high and has seen a sharp increase (~2x) in absolute terms as well (refer to orange line in chart below).



The exuberance amongst retail investors is also visible in the IPO market where we have seen strong subscription rates from retail investors across IPOs. These data points indicate that risk aversion has certainly taken a back seat.

Narrowing room for a negative surprise

The risk for an investor in Equities does not come from what is known and factored by the market, but from a negative surprise that is not being factored. It may sound counterintuitive, but we believe today the risk to an Equity investor is far higher than in March 2020.

As discussed in our March Quarter Newsletter (When All You see is Risk), valuations had started to reflect the possible worst case scenario and thus it was the best time to focus on opportunities while everyone was focused on risk. Even if worst case would have played out, the downside would have been limited. The reward vs risk was extremely favourable at that point in time. But the rally that we have seen in the last six months is narrowing the room for negative surprises. If the positive developments that are being factored by the market continue, the upside could be limited. But if we lose economic momentum or we witness a second wave or any other negative surprise, we could see a meaningful correction either in terms of price or time. Thus, Reward vs Risk is increasingly turning unfavourable.

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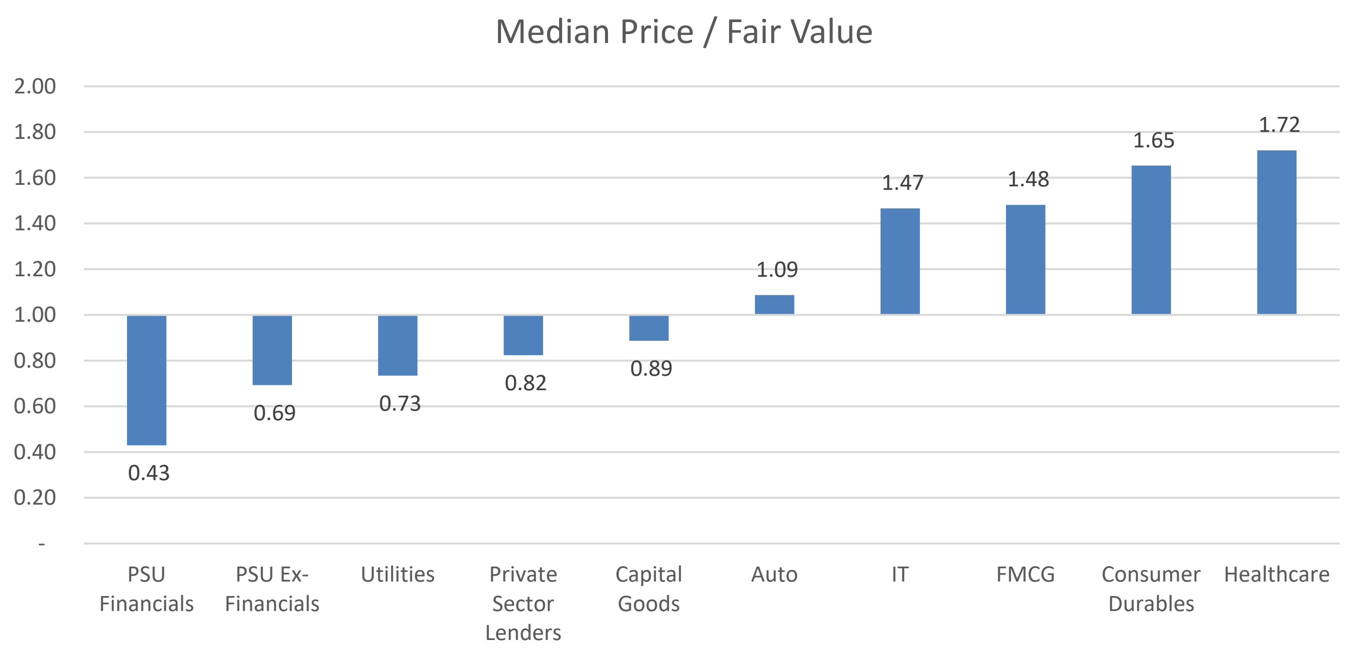
There is also a divergence in the market that we are observing in terms of valuation. There are certain sectors where valuations have crossed pre-covid levels and some sectors where valuations are still below pre-covid levels. Below chart shows the Median Price/Fair value of NSE 500 companies in each sector based on valuation done by



Multi-Act Research Team. This divergence in valuations has allowed us to build a portfolio with businesses that are available at attractive valuations without sacrificing on quality. We are comfortable committing capital to those sectors where reward vs risk is still favourable (e.g. Private Sector Lenders). The valuations in this sector indicates the anxiety of investors with respect to potential stress that the industry would go through with respect to asset quality. But we have added those lenders that have proven track record of asset quality across cycles. These companies would not only survive this crisis but bounce back much stronger than their peers. We have been reducing our exposure to sectors where valuations have turned a bit frothy leaving very limited room for negative surprises (e.g. Healthcare). And while this may tilt our portfolio away from consensus trades, we take comfort in following our valuation discipline rather than following the crowd.

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Asset Allocation:

Our overall equity weights stand at around 74% for older accounts. For new accounts our initial weight is around 40%.

Portfolio Activity:

Business Model and Sector Allocation:

Moat/Limited Moat	Dec-19	Mar-20	Jun-20	Sep-20
Moat	30%	33%	31%	22%
Limited Moat	44%	39%	42%	46%
Moat + Limited Moats	***74%***	***72%***	***73%***	***68%***
Special Situations	22%	24%	23%	28%
Regulated Utility	4%	4%	4%	4%
Grand Total	**100%**	**100%**	**100%**	**100%**

Sectors	Dec-19	Mar-20	Jun-20	Sep-20
Financials	16%	22%	26%	28%
FMCG	8%	14%	14%	15%
Financial Services	4%	9%	8%	12%
Information Technology	16%	11%	8%	11%
Materials	10%	8%	8%	9%
Pharma	15%	10%	11%	8%
Utility	4%	7%	8%	7%
Auto & Auto Ancillaries	17%	12%	13%	6%
Capital Goods	8%	6%	5%	5%
Media	3%	2%	-	-
Grand Total	**100%**	**100%**	**100%**	**100%**

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Portfolio Activity during the quarter:

We recently added HDFC AMC to the portfolio. Net flows into Equity Mutual Funds have turned negative in the last two months. And since most of the Equity Schemes of HDFC AMC have underperformed the market and peers, the equity schemes have lost market share. These concerns seem to be behind the recent weakness in the stock. We believe recent weakness in the equity flows is a temporary problem rather than something structural for us to be concerned about. The long-term tail wind for the industry continues to be strong as proportion of financial savings increases and within that the share of MFs increases. The company has taken cognizance of the underperformance of its schemes and is addressing it. The company has hired new fund managers who would help in reducing the concentration on a particular style of investing (value). Having different investing styles would make sure that all schemes don't underperform at the same time.

We added a company in the Engineering R&D space. ER&D industry has long term tailwind as cost conscious customers would like to get the best out of their constrained R&D budgets. In the near term this industry could face headwinds as clients cut down or postpone projects. But experience of current environment (work from home) would give confidence to customers to increase the offshore component of their spends over time. This is second company that we have added in the ER&D space.

In the beginning of the quarter we had added Hexaware Technologies which had announced the promoters intention to delist. As the Delisting process completed during the quarter, we exited.

We exited Wabco which we had bought last year as an arbitrage position for the open offer with an upside possibility if the promoters would have decided to delist. As the promoters did not announce their intention to delist, we decided to exit closer to the open offer price.

Regards,

Rohan Samant	Rohan Advant
Sr. Portfolio Manager &	Sr. Portfolio Manager &
Associate Director	Associate Director

Statutory Details: Portfolio Manager – Multi-Act Equity Consultancy Private Limited (Registration No. INP000002965)

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Disclosure as per Global Investment Performance Standards (GIPS®) –

Multi-Act Equity Consultancy Pvt. Ltd. claims compliance with the Global Investment Performance Standards (GIPS®). You can refer to the GIPS Compliant performance presentation here. Multi-Act Equity Consultancy Pvt. Ltd. has been independently verified by M/s. M. P. Chitale & Co., Chartered Accountants for the periods April 1, 2011 through March 31, 2019. The verification is available upon request. MAECL has claimed GIPS compliance for the Financial Year 2020 and is yet to complete the GIPS audit. The GIPS number shall be made available once the verification is completed

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.

The Composite representing the Moats and Special Situations portfolio was created on 27th January 2011. Performance has been compared with Total Return of the Index. For Moats & Special Situations Composite, blended benchmark of BSE 500 (50% weight) and BSE Mid Cap Index (50% weight) has been used. The Gross Return is before all expenses (except Brokerage). Net Return is after all actual expenses. A complete list of composite descriptions, policies for valuing portfolios and calculating performance fees are available on request.

Multi-Act Equity Consultancy Pvt. Ltd. is an independent SEBI registered Portfolio Manager. The firm maintains a complete list and description of composites, which is available upon request. This MSSP Composite includes all discretionary fee paying portfolios that are being managed with the objective of generating capital appreciation by investing in companies that in the opinion of the Portfolio Manager are of high quality Moat or Limited Moat businesses at fair value or discount to fair value OR in Non Moat businesses at deep discount to fair value as special situations. The portfolio manager has also the discretion of not being fully invested if he is not able to find ideas that meet the above criteria along with valuation criteria, thus, indirectly taking an asset allocation call between Equity and Cash (& Cash Equivalents).

The information provided in this document should not be construed as a recommendation to purchase or sell any particular security. There is no assurance that any securities discussed herein will remain in the composite or that the securities sold will not be repurchased. The securities discussed do not represent the composite's entire portfolio. Actual holdings will vary depending on the size of the account, cash flows, and restrictions. It should not be assumed that any of the securities transactions or holdings discussed will prove to be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein.

Risk factors
General risk factors
a. Securities investments are subject to market risks and there is no assurance or guarantee that the objective of the investments will be achieved.

b. Past performance of the Portfolio Manager or its affiliates does not indicate its future performance.

c. Investors are not being offered any guaranteed or assured returns i.e. either of principal or appreciation on the Portfolio.

d. As with any investment in securities, value of the Client's Portfolio can go up or down depending on the factors and forces affecting the capital market.

e. The Portfolio Manager is neither responsible nor liable for any losses resulting from the operations of the Portfolios.

f. The investments made are subject to external risks such as war, natural calamities, and policy changes of local / international markets which affect stock markets.

g. The Portfolio Manager has renewed SEBI PMS registration effective November 24, 2017 and has commenced its portfolio management activities with effect from January 2011. However, the Portfolio Manager has more than 10 years of experience in managing its own funds invested in the domestic market.

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