Monthly Letter

October 2024

prodigy INVESTMENT MANAGEMENT

Invest well. Celebrate life.

We were up +1.7% for September vs +2.3% for the NIFTY50 TRI. While the rate cut by the US Federal Reserve of 0.5% in mid-September was not totally unanticipated, it was the events that occurred towards the end of the month and in early October that have been of significance and are likely to impact markets and our portfolios in the coming months. The escalation in the Middle East and the surprisingly bold stimulus package by the Chinese Government have triggered a sell-off and a rapid rotation of funds from India to China by Foreign Portfolio Investors (FPIs). The escalation of the conflict in the Middle East has been a known risk for many months, though it is only now that it has actually transpired, and opened a Pandora's box as to how far and deep it will spread. Thus, in the near term while we can see pain ahead, the India story remains alive and kicking, and after the near-term excesses are purged, we believe a recovery will set in.

Returns*	NIFTY50 TRI	Prodigy Growth Strategy
1 Year	33.0%	42.6%
3 Years	14.9%	24.1%
5 Years	19.0%	33.1%
Since Inception (1-Mar-12)	14.7%	26.0%

*Figures are annualised, are as of 30th September 2024, and are not verified by SEBI. The portfolio returns are post-fixed and performance fees. In line with SEBI guidelines, all the portfolio and benchmark returns are calculated using the TWRR method.

Post the return to socialist principles by the ruling party and the bursting of the Chinese property bubble over the last few years, Chinese stocks have been trading at abysmally low valuations. The stimulus package is a desperate attempt by their Government to turn things around. Given how oversold the Chinese market has been, this has resulted in the market rallying 25% in just a few days, and our market falling by 5%. The valuation gap, in p/e terms, between the Indian and Chinese market, which had expanded over the last few years to 70%+, has immediately shrunk closer to the long-term average of ~50% (the world has more faith in our democratic and market-oriented systems than those of a communist party). Thus, while there may be some further shrinkage, the big correction in the valuation gap has already occurred. The questions for the moment are, will there be a follow-through stimulus from the Chinese Government which will revive the flagging real estate sector, the real drag on their economy? Will foreign investors feel sufficiently confident to redeploy long-term money into the country, after they have been burnt badly by the policy flip-flop in the recent past? Will the feel-good sentiment injected into Chinese consumer fade away after a brief rally, as has happened many times post covid? Is the bounce in the market just a trading opportunity or likely to sustain? One thing is certain, FPIs cannot trust a country being run on the whims of an overly powerful leader. Thus, while the rally may continue in the near future, the glory days of the Chinese stock market and its ability to attract the billions it once did, are in the past. The real estate sector's problems are too entrenched to be resolved easily or quickly, and the demographics of the Chinese nation and its fiscally over-leveraged situation are a drag on its revival.

In the near term, while the rotation of funds towards China can continue to cause a severe sell-off, the counterbalance of continuing strong domestic flows (and the fact that FPI holding now is at just ~17% of overall equity holding in India) should cushion the fall. The pipeline of domestic initial public offerings is also swollen and likely to divert funds away from the secondary market in the coming months, and slow its recovery. In the long term, these new listings give further depth to the Indian market and will attract more foreign investors; this process also aids in much-needed capital formation for the country. It also prevents the market from becoming too overvalued and is a self-regulating mechanism.

The final leg of the run-up to the US presidential election is underway and remains too close to call. We believe the Democratic candidate would be a better choice for global stability. A Trump presidency could be more inflationary and hurt our ability to lower interest rates. Fingers crossed.

The earnings season for quarter two of FY 2025 is just about to kick off. As of now, we hold approximately 8% of portfolios in cash. With so many moving parts at the moment, and risk levels extremely elevated, it is likely that cash levels will continue to slowly rise till we find risk levels have eased. We have held back on some selling as we feel we would rather wait for earnings to be announced and absorb the new data before taking a decision based purely on price action. Consumer demand in the upcoming festive seasons promises to be strong, and may give the right signals for a market revival.

The India story remains strong, and sell-offs like the one we are traversing, are viewed by us as an opportunity to reposition ourselves and align with the new leadership in the market, whenever the recovery sets in. FPI money should start returning to India, once the euphoric rally in the Chinese market fades. India remains the best long-term bet for foreign investors in a world starved of secular growth opportunities. For investors, this correction will be an opportunity to increase allocation to our market.

Warm regards.

RC

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