Monthly Letter Mar 2020

We were +0.8% in February versus -6.4% for the Nifty. Year to date for this financial year we are +9.1% versus -3.6% for the Nifty. The fall in the last week of February was severe, and wiped out most of our gains for the month. This was engendered by the news of the spread of the Coronavirus (Covid-19) to numerous geographies beyond China, especially to Europe and the US. With the detection of new cases in an increasing number of countries, the fear factor of a pandemic has resulted in global markets capitulating with the redemptions by global ETF investors gaining momentum (FPI selling in the last four days of February in India was over Rs 25k crores in both debt and equity markets). It is extremely difficult to make any prediction at the moment of how things are going to play out. Will this virus be contained in the near future? Or is it going to continue to spread? In which case all bets are off as to how deeply markets may fall as global economic growth gets impacted beyond the near term.

This event can be classified as a classic Black Swan. Just as things appeared to be improving for us, the sudden appearance and the deep impact of a completely unanticipated event, has taken the wind out of the sails of the global economy; which was just about recovering from issues like the trade war and Brexit. Should the spread of Covid-19 continue, our only option will be to start creating cash in the portfolios at every fall and wait for the blight to pass. Our hope is that it will be contained in the near future, like have all similar situations in the past.

As of this writing, new cases are down sharply in Wuhan, the epicentre of the problem. If it could be contained there, then hopefully it can be contained in the other hot spots too.

In all this, there is a silver lining for India. Global supply chains which have been severely impacted by the virus will feel the need to reduce the risk in future by diversifying to other geographies. In this, India may now have a fighting chance to be that other place, given the recent changes in tax rates on new entities and the elimination of dividend distribution tax. Commodity and crude prices have also fallen sharply, which is a temporary benefit to our economy.

Yesterday the US Fed has cut interest rates sharply by 50 basis points, in an emergency move, to combat the adverse economic effects of the virus. It would appear that the limits of monetary easing appear to have been hit, as this move could not prevent the US stock market slide from halting. One may expect other central banks to follow suit, in a globally co-ordinated effort to provide stimulus to a virus hit world.

As of now, the Nifty has once again fallen below its long-term average, a result of last week's sharp sell off. This implies that the secular trend may have turned negative as a result of the impending economic impact of the virus. When this happens, our processes predicate that we turn cautious, and if the fall continues then our risk management processes will kick in. As of now we will wait and watch before deciding our next step.

To conclude, we feel that as long-term equity investors, we need to look beyond the current crisis. In the past similar situations have ultimately passed, and this intervening period of fear has been one of opportunity. We shall be keeping this in mind as we tackle things on a day to day basis.

Thank you for your support in uncertain times.

RC

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