Monthly Letter February 2021

We were -1.4% vs the Nifty, which was -2.5%. (12 month return +31.5% vs +14% for Nifty). January saw the consolidation of the market ahead of the Union Budget, after the sharp run up witnessed in the last quarter of CY2020. FPI fund inflows, the key driver of this rally, also slowed down from the deluge witnessed in the previous months, but remained healthy. With the secular fall in COVID-19 numbers in India, it would appear that the worst, for the country, appears to be behind us and this is generating tremendous confidence amongst consumers and investors.

The Union Budget for fiscal year 2021-22 was very positive, in that it signaled a huge shift in government thinking from its past Budgets. Indeed, sometimes a crisis is what it takes for the mind to clear. Rather than once again tinker with tax rates and policy, the Government has made a full out attempt to go for growth and move the economy into a virtuous cycle, which if successfully pulled off, would induce much higher levels of growth and thus allow for higher revenue levels and an automatic return to acceptable fiscal deficit levels in the future. For an economy to really take off, the return of 'animal spirits' and belief in the future is the most important 'X' factor. This Budget gives us a very high chance of rekindling it. The change in attitude towards growing the pie, rather than merely redistributing it; as well as replacing the nagging fear of ever new imposts in the minds of industry and investors with confidence of policy support and stability, is the real achievement of this Budget.

The Budget was a realistic one, in terms of what the revenue and deficit levels would be in fiscal 21-22, and also a transparent one when it came to fiscal accounting, thus creating confidence in the document. The measures announced and outlays towards infrastructure investment could restart the investment cycle, which has been comatose for too many years. Hopefully India and our financial system will not see another unexpected crisis, as has been the case ever so often in the past few years. This will allow the cumulative benefits of the reforms of past years and those announced in the Budget to gain traction and propel growth rates back to historic levels. We are optimistic.

The earnings season for last quarter has been extremely positive once again, indicating a sustained momentum in the recovery. As mentioned in our earlier Monthly Letters; aggressive cost cutting, a shift to the organised sector, robust rural demand, and a sustained demand recovery, have resulted in this and now most industries have returned to pre-COVID-19 demand levels, with many surpassing it. With such earnings numbers from a swathe of sectors, it would appear that the rally has strong underpinnings.

While the rally initially was in the defensive sectors, it is now clearly manifesting in the economy sensitive and cyclical sectors, reflecting the strong economic recovery. We have been steadily shifting allocation to capture this, but will now do so more markedly as the Budget has created the right environment for economy sensitive sectors to gain momentum. We believe many cyclicals appear attractively valued at the moment and many mid-caps that would benefit from India's secular growth in consumption demand appear attractive as well.

The outbreak of a new variant of the virus in India remains the main known unknown risk, but that is not something we can plan for or worry about. We have to work with what is happening at the moment, which is very positive. Hopefully the vaccines will prove to be effective against new strains as well.

While markets globally are sustaining with the continuous flow of liquidity from Central Banks, as has been the case in India, we believe that the stage is set for domestic investors to also return in a big way, given the low returns in debt instruments and significant under allocation to equities in the Indian asset basket. Interest rates may rise somewhat given the higher levels of government borrowings expected this year to fill the Budget deficit, and they may have bottomed out for now. As long as this Budget does indeed re-ignite growth, this should not be a major concern. High growth rates should make most problems shrink. The key is getting into a virtuous cycle of growth.

In case you have funds to allocate to equities or are under allocated to equities, we would encourage you to add the same to your corpus with us.

Thank you for your support.

RC

Disclaimer

4th Floor, Oricon House, K. Dubash Road, Fort, Mumbai–400 001, India Tel :(+91 22 22875801)