Monthly Letter July 2013

Last month was one marked by enhanced levels of volatility and the emergence of a ‘risk off’ sentiment globally, which impacted our markets substantially. While the Nifty fell 2.4%, we were impacted a little more falling 3.4%, given some of our exposure is in the broader market as well. However, for the first quarter of this financial year we were up 6.7% versus the Nifty which was up 2.8%. To put things further in context the CNX Mid Cap index was down 0.8% and the CNX Small cap index was down 7.2% in the just concluded quarter! Thus we managed to well in a difficult environment. We are paying out 2.5% of corpus back to you this quarter, our highest pay out to date (for those who have opted for pay outs).

FIIs after pumping in around Rs 80K crs in the first five months of this calendar year into equities, withdrew approx Rs 11K crs in June. There was a significant sell off in the debt market as well by FIIs, which is what really impacted the rupee. As a result, our market once again fell to the 5550 level towards month end, and the rupee fell to 60.71 to the usd. This fall was the result of Ben Bernanke (the US Fed) indicating that as the US economy was showing good signs of improving the QE program would be throttled back starting September 2013. In fact all markets globally; equities, commodities, debt as well as currencies, experienced a sell off simultaneously, leaving investors with no place to hide, but the usd, which appreciated. Such an across the board sell off was seen last in 2007, though the magnitude then was more severe.

This intention of tightening by the Fed co-incided with a tightening by the Chinese Government as well in order to engineer a slow down of sorts in an economy that was not responding any more to easy money. This exacerbated the situation.

However, as investors realized that the tightening by the Fed was only to recognize that the US economy was improving quite well over the past few months and that liquidity would be ample as other central banks were still easing, the markets rebounded strongly at month end.

As always, pushed to the wall, our Government adopted the long pending reform on the raising of gas prices and made some effort to kick start long pending projects in the infrastructure space. This has had a short term salubrious impact on sentiment. However, the fall in the rupee has pushed back the easing cycle in interest rates by the RBI, and this has had an impact on the market, especially on the financials. More reforms on the FDI front are expected from the Government as it tries to stabiles the rupee.
Once again fears of the European crisis flaring up, this time getting triggered off from Portugal, has caused ‘risk off’ to rear up and a strong rally to suddenly reverse. The levels of market volatility have risen to levels where predicting anything in the near to medium term has become very difficult. Civil unrest in Egypt over the last few days has once again caused crude oil prices to harden. Rising bond yields globally also threaten the financial stability of already weak banks. In such a situation we manage only because of our confidence in the quality of what we own in the portfolio, having jettisoned almost all economy sensitive sectors. As of now we seem stable in an otherwise volatile market.

We continue to like ‘good and clean’ businesses which will be able to grow steadily even in the most difficult of environments. Our experiments with investing in economy sensitive businesses in the recent past has not worked, and we believe that till the next union election is over, the investment cycle is unlikely to perk up. Thus we hold very specific businesses that we feel confident will hold up over the coming quarters with a steady growth, and low incremental capital needs.

To point out the underlying positives in such an environment almost seems futile. However, the good monsoons, the secular fall in gold and other commodities, the improvement in the current account deficit to 3.6% of GDP in the just concluded quarter; all augur well. Notwithstanding all the negatives that have pounded the market over the last six months, the Nifty has not broken below the 5550 levels. This is good reason to remain invested even though the news flows are as challenging as they are.

Thank you for your support.

Warm regards

RC