MONTHLY Communique

November 2017

Stay the course...

Over the past 3 months most PMS products of Motilal Oswal AMC have been underperforming their benchmark indices. 3 months' sharp underperformance is enough to drag down the alpha going back to longer time periods. This note is aimed at updating investors and channel partners and guiding on our perspective.

Underperformance is caused by portfolio choices made in line with stated investment philosophy and also by shifts in the underlying markets. With change in expectations of performance of different sectors in the economy and shifting government policies there has been a rotation of "what's preferred in the markets". Bottom up index agnostic investment strategies seem lackluster when there is a risk seeking beta rally and rotation of style away from growth in the markets.

This does not take away the fact that we are holding companies with sustainable earnings growth. At a portfolio level our weighted average earnings growth ranges anywhere from 15 to 25% CAGR. Our focus continues to be centered around owning a portfolio whose earnings will double in about 3-4 years.

We prefer to focus on our bottom up understanding of such companies rather than attempting to gauge macroeconomic trends or government policies. Not only because these are usually hard to predict being dependent on extraneous factors beyond investors' control but also because we have never claimed this to be an area of expertise. On a more sustainable secular basis, market usually appreciates companies and sectors with a higher visibility enabled by long term growth prospects, favourable industry dynamics, and competencies of the companies along with execution capability of their managements. These are companies whose locus of control is as close to the company and its management execution as possible. Not that these companies are not impacted by the environment - all companies are impacted but some companies are relatively less than others. Companies whose locus of control tends to be in the macroeconomic or the policy environment depend heavily on shifts in these environments to reward investors; admittedly the reward may be sharp and swift at times and the backlash on disappointments can be equally harsh and prolonged as has been witnessed in the previous 5-6 years. Our focus on sustainability of earnings growth precludes investment into global commodities, cyclicals, highly leveraged companies, policy dependent companies and the like.

We maintain that there is no right or wrong way of investing in markets, we respect every strategy that produces results for investors but we have to practice what we believe in and what works best for us.

We have always believed and communicated that performance is an outcome. More specifically equity investing is all about highly variable and probabilistic outcomes. When outcomes are not controlled by participants, the only way to narrow the variability of outcomes is to ensure quality and consistency of inputs. Market moods or movements cannot be forecasted and managing portfolios as per market forecasts subjects investors to higher variability of outcomes.

(Continued overleaf)

Accordingly, we have always spoken about adopting a bottom up stock picking approach focusing on companies that meet our screeners and being sector or market agnostic, unmindful of what the index has or doesn't. Equity investing is a marathon and not a sprint and we continue to be disciplined in staying on the course. We select investment possibilities by applying ***uniform*** qualitative and quantitative variables through a ***repeatable investment process.***

Up until now our performance has been an outcome of a Q-G-L-P driven stock selection process and being 50-60% away from the index; we do not track or replicate index weights with few under / overweight positions. This is a result of our consistent belief in the "Buy Right : Sit Tight" philosophy of picking high growth quality stocks. In our kind of investing philosophy irrespective of what happens in the markets, we expect stock prices to track earnings on a sustainable basis. Not that markets have no role to play; markets do pre-pone and post-pone the translation of earnings into stock price movements and markets are the context in which we operate.
The long term track records, variability of returns vis-à-vis index and some surrogate mutual funds is presented below:

Scheme Name	1 Year Average Rolling Return	1 Year Standard Deviation	Average/Std Dev (1 year)	5 Year Average Rolling Return	5 Year Standard Deviation	Average/Std Dev (5 year)
Fund A	19.99%	10.92%	1.83	15.26%	13.97%	1.09
Fund B	17.95%	10.85%	1.65	16.20%	13.87%	1.17
Value Strategy	18.72%	11.52%	1.62	14.33%	14.31%	1.00
Fund C	16.53%	10.54%	1.57	13.09%	14.06%	0.93
Fund D	18.65%	12.06%	1.55	14.03%	13.42%	1.05
Fund E	15.92%	10.50%	1.52	12.02%	13.62%	0.88
Fund F	17.46%	13.45%	1.30	13.37%	16.94%	0.79
Fund G	12.95%	10.04%	1.29	15.65%	13.39%	1.17
Fund H	19.21%	14.96%	1.28	14.63%	17.18%	0.85
Fund I	14.61%	12.93%	1.13	11.51%	15.79%	0.73

Scheme Name	1 Year Rolling return Since Inception	1 Year Standard Deviation	Ret/Std Dev	5 Year Rolling return Since Inception	5 Year Standard Deviation	Average/STD Dev (5 Year)
Fund 1	26.31%	13.60%	1.93	10.26%	13.60%	0.75
NTDOP Strategy	29.50%	15.62%	1.89	12.98%	15.62%	0.83
Fund 2	25.51%	13.70%	1.86	10.54%	13.70%	0.77
Fund 3	23.69%	13.14%	1.80	10.04%	13.14%	0.76
Fund 4	21.91%	13.24%	1.66	9.36%	13.24%	0.71
Fund 5	24.93%	16.12%	1.55	9.14%	16.12%	0.57

Scheme Name	1 Year Rolling return	1 Year Standard Deviation	Return/Std dev (1 Year)
IOP Strategy	25.84%	15.39%	1.68
Fund 1	21.18%	15.88%	1.33
Fund 2	19.56%	15.16%	1.29
Fund 3	17.09%	13.42%	1.27
Fund 4	16.53%	13.93%	1.19
Fund 5	17.76%	18.31%	0.97

Source: Motilal Oswal AMC Internal Analysis & MFI Explorer. Data as on 31st October 2017

Please note that this data is of actual mutual fund schemes which are in the large cap and large + midcap domain having track record and AuM comparable or larger than the respective PMS Strategies. One can expect a PMS portfolio to outperform most mutual funds on returns because of buy and hold and concentrated exposures; but outperformance on risk adjusted basis too is an achievement because PMS is managed as a model portfolio. We don't have inflows and SIPs on daily or weekly or monthly basis, which can be used to rebalance the portfolio for all investors automatically. A PMS has to manage or rather maneuver a steady state portfolio as is without cashflow on daily or monthly basis. This is not the main agenda; the data is presented to demonstrate that irrespective of underperformance over some time frame, in a larger context consistent philosophy, stability of fund manager and growth oriented portfolios produce good risk adjusted returns.

Time Frame	Value Strategy	Nifty 50	IOP Strategy	Nifty Freefloat Midcap 100	NTDOP Strategy	Nifty Freefloat Midcap 100
3 Months	1.99%	2.56%	1.73%	5.75%	3.95%	5.75%
6 Months	9.92%	11.08%	7.45%	8.25%	11.80%	8.25%
1 Year	17.32%	19.82%	21.92%	23.04%	18.89%	23.04%
2 Year	14.00%	13.20%	33.17%	21.61%	24.61%	21.61%
3 Year	12.01%	7.49%	26.35%	18.25%	27.18%	18.25%
4 Year	21.77%	13.18%	29.23%	26.96%	36.82%	26.96%
5 Year	17.46%	12.96%	23.88%	20.32%	32.24%	20.32%
10 Year	10.86%	5.77%				
Since Inception	24.94%	17.24%	18.17%	13.75%	19.32%	8.82%

Data – MOAMC Internal Analysis as on 30th October 2017. Inception Dates: Value Strategy - 25th March 2003; NTDOP Strategy – 5th Dec 2007 & IOP – 15th Feb 2010

Disclaimer:

In the above table we have provided the returns of Mutual Fund Schemes and indices vis-a-vis our PMS Strategy to demonstrate the relative risk adjusted performance of PMS Strategies. The above tables are only for illustration purposes and for explaining the concept and are not sufficient and shouldn't be used for the development or implementation of investment strategies. It should not be construed as investment advice to any party. The Above returns of PMS Strategies are of a Model Client. Returns of individual clients may differ depending on time of entry in the PMS Strategies. Strategy returns shown above are post fees & expenses. All the returns above 1 year are annualized returns. Motilal Oswal AMC does not provide any guarantee/ assurance any minimum or maximum returns. Past performance may or may not be sustained in future.

Coming back to the current context, we continue to manage our portfolio index agnostic and currently too our portfolios stocks and allocations across 3 PMS strategies diverge vastly away from the index. There is a strong team of portfolio managers and analysts who are responsible for tracking corporate performance vis-à-vis internal expectations on earnings of these companies and wherever necessitated portfolio actions are being taken. Sectoral Allocations for the portfolio and the benchmarks are shown below.

Sectors	Nifty 50	Value PMS
Banks and Finance	35.70	40.51
Auto and Auto Ancilliaries	10.63	25.43
Petroleum Products	10.18	9.19
Consumer Non Durable	9.27	6.99
Transportation	0.86	5.77
Pharmaceuticals	3.99	5.46
Construction Projects	3.92	5.12
Softwares	11.18	-
Power	2.52	-
Metals & Mining	4.60	-
Cement	1.67	-
Oil & Gas	2.10	-
Others	3.38	1.53

Data as on 31st October 2017

Sectors	Nifty Mid Cap	NTDOP	IOP
Banks and Finance	20.72	33.33	26.87
Consumer Non Durable	-	19.68	4.61
Auto and Auto Ancilliaries	6.56	14.67	7.08
Consumer Durable	12.69	8.93	9.96
Oil & Gas	3.47	7.07	12.30
Industrial	6.46	4.06	1.94
Pharmaceuticals	9.52	3.96	10.33
Construction Projects	5.57	-	3.40
Cement	3.00	-	10.47
Softwares	6.31	-	-
Metals & Mining	4.44	-	-
Energy	8.03	-	-
Services	5.75	-	6.66
Others	7.48	8.30	6.38

Data as on 31st October 2017

As can be seen above, in IOP and NTDOP Strategies which are benchmarked against Nifty Free Float Midcap 100 Index sectors like IT, Metals, Energy and Telecom have no exposure in either portfolios combined even though the benchmark has 17% cumulative weightage in these sectors and sector like Consumer non-durables has high allocation as against no weightage in benchmark. Similarly, in our Value Strategy which is benchmarked against NSE 50, the portfolio has no exposure to sectors like IT, Metals, Power, Cement, Oil & Gas and Telecom even though the benchmark has 25% cumulative weightage in these sectors. Talking of oil and gas, we have exposure to Oil Marketing Companies which has rewarded us across portfolios in the last two years but since we generally do not invest in global commodities and conglomerates exposure to ONGC and RIL has been NIL.

Further, where our portfolios do have sectoral exposure in line with the index the underlying securities within such sector are away from the index. For Example in IOP PMS the banking exposure is 26% as compared to benchmark of 20.7%, however there is only 1 common stock DCB Bank (index weight of 0.61% and portfolio weight around 9%). The other banking stocks in the portfolio are out of the benchmark like Canfin Home Finance, Laxmi Vilas Bank, IIFL Holding and AU Small Finance Bank.

Another testament of our index agnostic approach lies in the number of stocks in the portfolio away from its benchmark. In Value PMS 5 stocks out of 16 are out of benchmark and similarly for NTDOP out of 24 stocks in the portfolio 17 stocks are outside benchmark and in IOP out of 20 stocks, 19 stocks are outside the benchmark. It is worth noting that there are multiple cases where stocks have been included in various indices like Nifty, MSCI India etc. much after our having held them; notable examples being Bajaj Finance, Eicher, Petronet LNG, Britannia, HPCL, Bosch, IndusInd Bank, etc.

We are answerable for relative performance but that is not the starting point or the modus operandi for our investments. Our endeavor is to generate absolute return with a target for portfolio companies doubling their earnings in 3 to 4 years on weighted average basis. There is no intent to tweak portfolios to chase high beta (not necessarily high quality stocks) only to ensure that the returns move in line with the benchmarks.

Quite a many active funds have a strong pro-cyclical element, and therefore, have “high betas” in their portfolios. This may not necessarily be only due to the fund managers' liking of High Beta stocks but also due to their investment approach of benchmark relative performance and not bottom up stock picking. It's more to ensure that the performance of these funds remain close to the benchmark which has some weightage to high beta stocks. We understand that an investor doesn't have 100% of their equity allocation with us. For sustainable performance at the clients' portfolio level a diversity of styles is a must and it is worth noting that in the entire market there are hardly any funds that follow a high quality high growth style of investing. Most investors preclude this style of investing as buying expensive while we put in our best to gain an edge into understanding drivers of growth and sustainability of growth; and turn willingness to hold into a distinct advantage in realising the entire growth cycle. This makes us unique and value accretive in client portfolios over a market cycle. We only chase Quality and Growth with Longevity of growth and the underlying science is tied to process and not to market conditions or macros. Interesting to note that with Q-G-L companies buying at wrong price can result in worst outcome of temporary drawdowns or time corrections as opposed to destruction of capital...hence Q-G-L-P with buy and hold and sharp focus on earnings trends is ideal. Also it is worth mentioning if one does insist on macro scenarios that within the next 18 months we are heading into an election season and usually such events are accompanied with higher spends, stimulus packages and a trickle down boost to consumption.

In our opinion, Value and Momentum factors are pro-cyclical with high market betas, while Quality factors are counter-cyclical with low market betas. A few quarters of earnings accumulation and eventually quality stocks prove counter-cyclical and afford downside protection, the likely trade-off in short term is a time correction and underperformance in a beta rally.

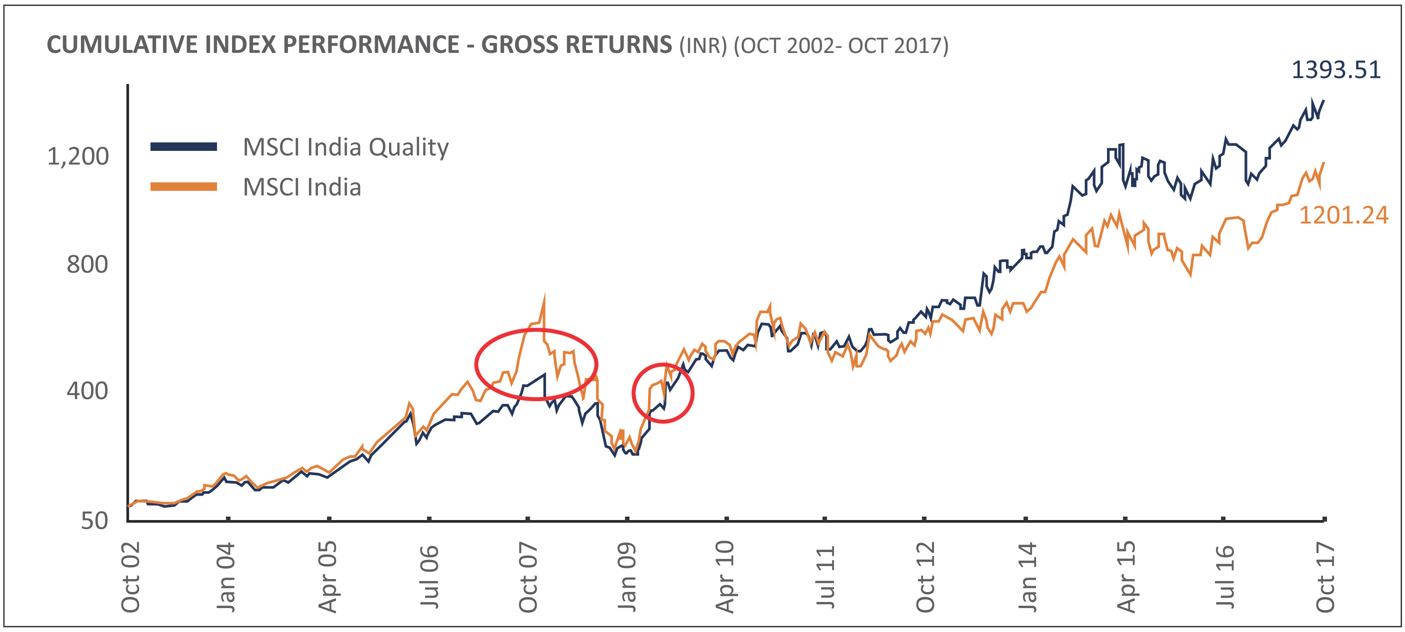
In the last few months, liquidity has been chasing high beta stocks and hence quality stocks have been underperforming. An analysis of the MSCI India Quality Index versus MSCI India Index throws some light on this phenomenon:

	1 Month	1 Year
MSCI India Quality	4.16	12.97
MSCI India	6.47	19.48

Source: www.msci.com Data as on: 31st October 2017

Past performance may or may not be sustained in future and should not be used as a basis for comparison with other investments.

However, if we compare the long term performance of quality with broader market we see a gross outperformance.



Source: www.msci.com Data as on: 31st October 2017

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For last 10 years the MSCI Quality Index has delivered 10.82% annualized return vs. 5.76% of MSCI India Index. During the same period an actively managed quality portfolio like NTDOP has delivered around 19% annualized return. During this long period the beta of Quality index and NTDOP has been around 0.8-0.85.

In previous bull runs (red circled area) marked by huge rise in index in a short time frame – mid 2006 - end 2007 and for some part of the sharp pull back in 2009, similar activity has played out in the markets where quality stocks have underperformed while high beta pro-cyclical stocks have outperformed albeit for short period of time. We at Motilal Oswal AMC have seen through and managed across similar periods eventually to see the market come back in line with earnings.

S&P BSE Index	Risk	Return	Return Risk Ratio
Sensex Index	23.00	15.00	0.65
LargeMidcap Index	24.00	15.90	0.66
Enhanced Value Index	33.90	17.80	0.53
Momentum Index	25.20	20.20	0.80
Quality Index	20.90	20.70	0.99
Low Volatility Index	19.80	19.80	1.00
Dividend Portfolio	29.80	19.10	0.64
Equal-Weighted Portfolio	28.20	17.40	0.62

Source: S&P Dow Jones Indices LLC

Table Source: Economic times Dt. 05 Dec, 2017

In the last one year we have observed that a large part of benchmark returns has been largely contributed by commodities, real estate and telecom despite very limited earnings visibility of these sectors. Also few stocks having large weightage drive index performance; managers staying away from index and not owning that stocks may lag. For example, Reliance Industries which has a Nifty index weight of ~ 8%, has generated ~75% absolute returns over the last one year thereby contributing 6.2% to overall Nifty Return of 31%.

In a liquidity driven bull rally, most stock rises (not merely quality); as liquidity chases high beta stocks. Market participants take huge bets on high-beta stocks (which move more than the overall market) as they seek quick returns.

Some of these stocks have shot up 50%-100% or even more in the last one year alone e.g. Reliance as mentioned above, Hindalco, Vedanta, Tata Steel, metals and commodities at large, most PSU Banks etc. A lot of this is reaction to mere change in "expectation", mind you, not actual doubling or some such rate of change in earnings. When a consumer facing company with unique advantages shows huge growth, markets re-rate such companies with expectation of new growth rates to last for some time in the immediate future. Similar re-rating may happen in case of cyclical or commoditized companies when the cycle turns but eventually market has to be discerning about sustainability and the demand-supply complex.

Our performance over the last one year may not be relatively high, but one needs to understand that we have purposefully not emulated the broader markets by strategically buying solid stocks at good prices that are not part of the current herd mentality. At various points in time investors have expressed concerns that quality stocks are trading expensive as is always the case, whereas in the last few months some of these stocks have seen depreciation in value – not only relative but also absolute depreciation – what with some investors selling quality to buy high beta and participate in the rotation. After all it's not always that Kotak Bank declares 22% earnings growth and sees the price fall 5% on the day! When was the last time (barring 2008-09) one saw HDFC Bank decline 4% in a single day? Similar examples abound. This phenomenon enables us to position our portfolios to take advantage of the dislocations between price and value and then we allow time to work. The bank recapitalization for instance does confirm that PSU Banks get a new lease of life and capital to fight back but it doesn't change the fact that while PSU Banks contribute 70% of outstanding stock of credit and only 30% of incremental credit. Statistics abound and the perspective for next 6 months to 1 year will always be different from the perspective to hold over next 5 years.

We continue to focus on such fundamental trends, the earnings growth of our portfolio companies and outperform the benchmark growth. Each of PMS portfolios has been generating strong earnings growth wherein the benchmark earning growth has been in lower single digits.

	TTM	FY18E	Fy19 E
Value Strategy	13%	10%	23%
NTDOP	18%	24%	22%
IOP	12%	29%	28%

Source: Bloomberg Consensus & Internal Research
Data as on: 31st October 2017

Past performance may or may not be sustained in future.

When emotions are high, making rational decisions becomes harder and that's where staying on course becomes more important. At Motilal Oswal AMC, our investment success comes from ***staying true*** to buying "High Growth Quality Stocks and holding them for long periods of time" ***without getting swayed.***

Happy Investing,

Yours Sincerely,
Aashish P Somaiyaa
Managing Director and CEO

Disclaimer:

The stocks mentioned herein are used for illustration purposes only and for explaining the concept. It should not be construed as recommendations from MOAMC. The stocks may or may not form part of our existing PMS Strategies. The Stocks those are part of existing PMS Strategies may or may not be bought for new client. Past performance may or may not be sustained in future and should not be used as a basis for comparison with other investments. The statements made herein may include statements of future expectations and other forward-looking statements that are based on our current views and assumptions and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. The above analysis has been prepared and issued on the basis of publicly available information and other sources believed to be reliable. Motilal Oswal AMC does not provide any guarantee/ assurance any minimum or maximum returns. Investment in Securities is subject to market and other risks and there is no assurance or guarantee that the objectives of any of the Strategies of Portfolio Management Services will be achieved.

Value Strategy

Strategy Objective

The Strategy aims to benefit from the long term compounding effect on investments done in good businesses, run by great business managers for superior wealth creation.

Investment Strategy

- Value based stock selection
- Investment Approach: Buy & Hold
- Investments with Long term perspective
- Maximize postt ax return due to Low Churn

Details

Fund Manager	:	Shrey Loonker
Co-fund Manager	:	Kunal Jadhwani
Strategy Type	:	Open ended
Date of Inception	:	24th March 2003
Benchmark	:	Nifty 50 Index
Investment Horizon	:	3 Years +
Subscription	:	Daily
Redemption	:	Daily
Valuation Point	:	Daily

Top Sectors

Sector Allocation	% Allocation*
Banking & Finance	40.51
Auto & Auto Ancillaries	25.43
Oil & Gas	9.19
FMCG	7.00
Airlines	5.77
Pharmaceuticals	5.46
Engineering & Electricals	5.12
Cash	1.53

Data as on 31st October 2017

*Above 5% & Cash

Top 10 Holdings

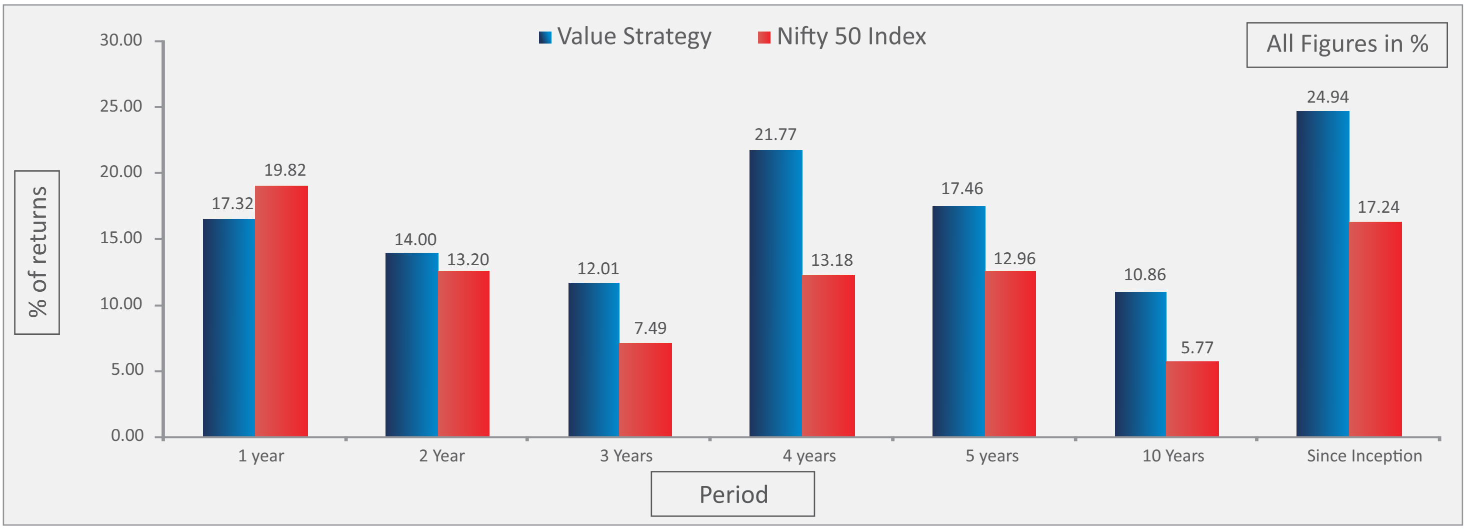
Particulars	% Allocation
HDFC Bank Ltd.	9.76
Bharat Petroleum Corporation Ltd.	9.19
Eicher Motors Ltd.	9.00
Kotak Mahindra Bank Ltd.	7.63
Bosch Ltd.	7.17
Asian Paints Ltd.	7.00
Housing Development Finance Corporation Ltd.	6.20
Bharat Forge Ltd.	6.15
AU Small Finance Bank Ltd.	5.81
Interglobe Aviation Ltd.	5.77

Data as on 31st October 2017

Key Portfolio Analysis

Performance Data (Since Inception)	Value Strategy	Nifty 50
Standard Deviation (%)	20.91%	23.15%
Beta	0.82	1.00

Data as on 30st September 2017



The Above strategy returns are of a Model Client. Returns of individual clients may differ depending on factors such as time of entry/exit/ additional inflows in the strategy. The Above returns are calculated on NAV basis and are based on the closing market prices as on 31st October 2017. Past performance may or may not be sustained in future. Returns above 1 year are annualized. Please refer to the disclosure document for further information.

Next Trillion Dollar Opportunity Strategy

Strategy Objective

The Strategy aims to deliver superior returns by investing in stocks from sectors that can benefit from the Next Trillion Dollar GDP growth.

It aims to predominantly invest in Small and Mid Cap stocks with a focus on identifying potential winners that would participate in successive phases ofGDPgrowth.

Investment Strategy

- Stocks with Reasonable Valuation
- Concentration on Emerging Themes
- Buy & Hold Strategy

Details

Fund Manager	: Manish Sonthalia
Strategy Type	: Open ended
Date of Inception	: 11th December 2007
Benchmark	: Nifty Free Float Midcap 100 Index
Investment Horizon	: 3 Years +
Subscription	: Daily
Redemption	: Daily
Valuation Point	: Daily

Top Sectors

Sector Allocation	% Allocation*
Banking & Finance	33.33
Auto & Auto Ancillaries	15.68
FMCG	15.57
Diversified	13.05
Oil & Gas	7.07
Cash	0.49

Data as on 31st October 2017 *Above 5% & Cash

Top 10 Holdings

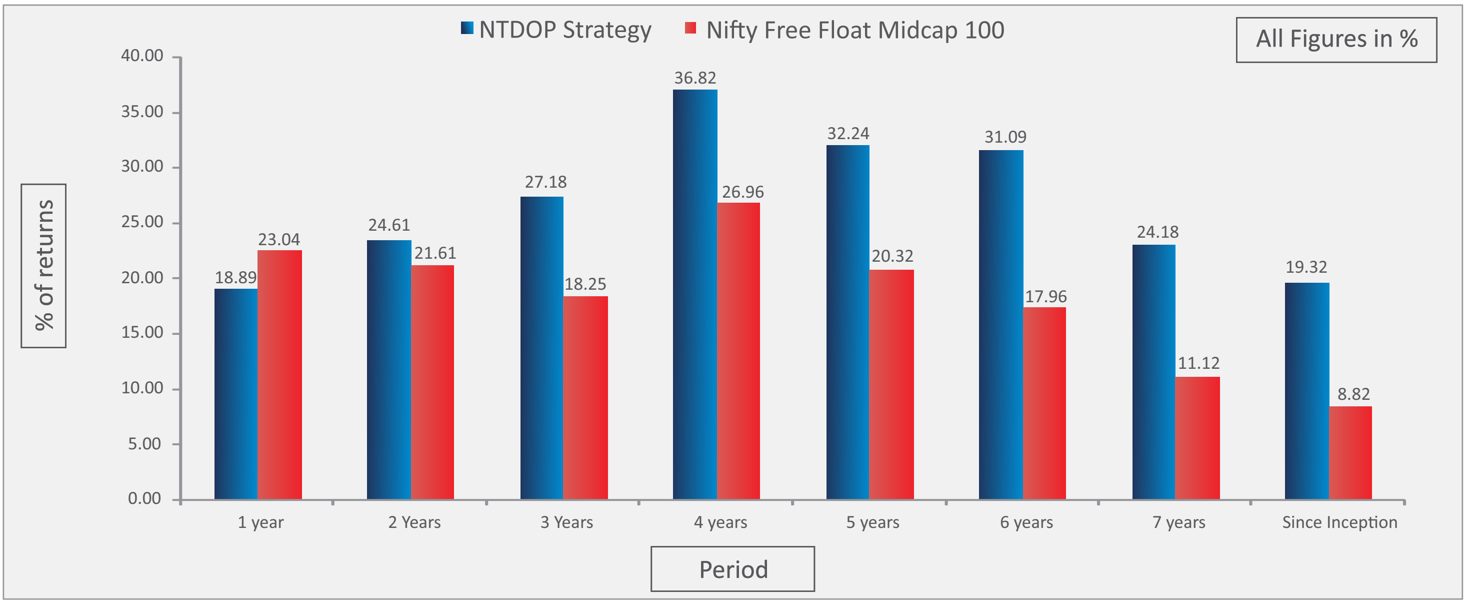
Particulars	% Allocation
Kotak Mahindra Bank Ltd.	10.79
Voltas Ltd.	8.93
Bajaj Finance Ltd.	8.85
Page Industries Ltd.	7.95
Eicher Motors Ltd.	7.03
Max Financial Services Ltd.	5.12
Bosch Ltd.	4.81
Hindustan Petroleum Corporation Ltd.	4.60
City Union Bank Ltd.	4.13
Godrej Industries Ltd.	4.11

Data as on 31st October 2017

Key Portfolio Analysis

Performance Data (Since Inception)	NTDOP	Nifty Free Float Midcap 100
Standard Deviation (%)	18.18%	22.10%
Beta	0.71	1.00

Data as on 31st October 2017



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India Opportunity Portfolio Strategy

Strategy Objective

The Strategy aims to generate long term capital appreciation by creating a focused portfolio of high growth stocks having the potential to grow more than the nominal GDP for next 5-7 years across market capitalization and which are available at reasonable market prices.

Top Sectors

Sector Allocation	% Allocation*
Banking & Finance	26.87
Cement & Infrastructure	13.86
Oil & Gas	12.30
Pharmaceuticals	10.33
Consumer Durable	9.96
Auto & Auto Ancillaries	7.08
Services	6.66
Cash	2.48

Data as on 31st October 2017 *Above 5% & Cash

Investment Strategy

- Buy Growth Stocks across Market capitalization which have the potential to grow at 1.5 times the nominal GDP for next 5-7 years.
- BUY & HOLD strategy, leading to low to medium churn thereby enhancing post-tax returns

Top 10 Holdings

Particulars	% Allocation
Birla Corporation Ltd.	10.47
Development Credit Bank Ltd.	9.15
Gabriel India Ltd.	7.08
Quess Corp Ltd.	6.66
Aegis Logistics Ltd.	6.16
Mahanagar Gas Ltd.	6.14
AU Small Finance Bank Ltd.	6.09
Canfin Homes Ltd.	5.49
Kajaria Ceramics Ltd.	5.12
TTK Prestige Ltd.	4.84

Data as on 31st October 2017

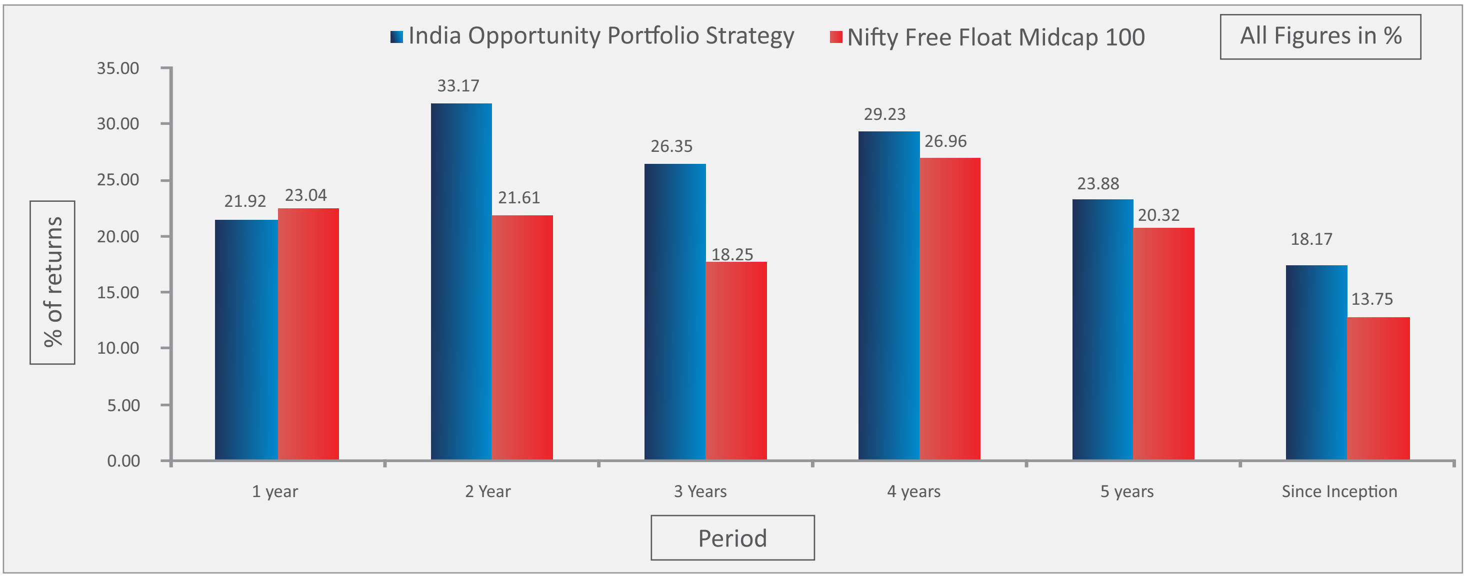
Details

Fund Manager	: Mr. Manish Sonthalia
Co-Fund Manager	: Ms. Mythili Balakrishnan
Strategy Type	: Open ended
Date of Inception	: 11th Feb. 2010
Benchmark	: Nifty Free Float Midcap 100
Investment Horizon	: 3 Years +
Subscription	: Daily
Redemption	: Daily
Valuation Point	: Daily

Key Portfolio Analysis

Performance Data (Since Inception)	IOPS	Nifty Free Float Midcap 100
Standard Deviation (%)	15.33%	16.98%
Beta	0.74	1.00

Data as on 31st October 2017



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