

IOP – The opportunity's still there

October 2020

IOP ... in just one minute

➤ **Small Caps in an extreme trough**

3-years of successive underperformance unprecedented

➤ **IOP has a successful performance track record ...**

Canfin, Dhanuka, Mahanagar Gas, Alkem, Birla Corp; 4% alpha since inception

➤ **Our key learning**

QGLP for small caps can be nuanced

➤ **We have high conviction in our holdings**

AU Bank, Aegis Logistics, Dr. Lal, Bayer Cropscience, Qess, ITD

➤ **The opportunity's still there**

FY22 Portfolio earnings growth of 36%; Valuations attractive

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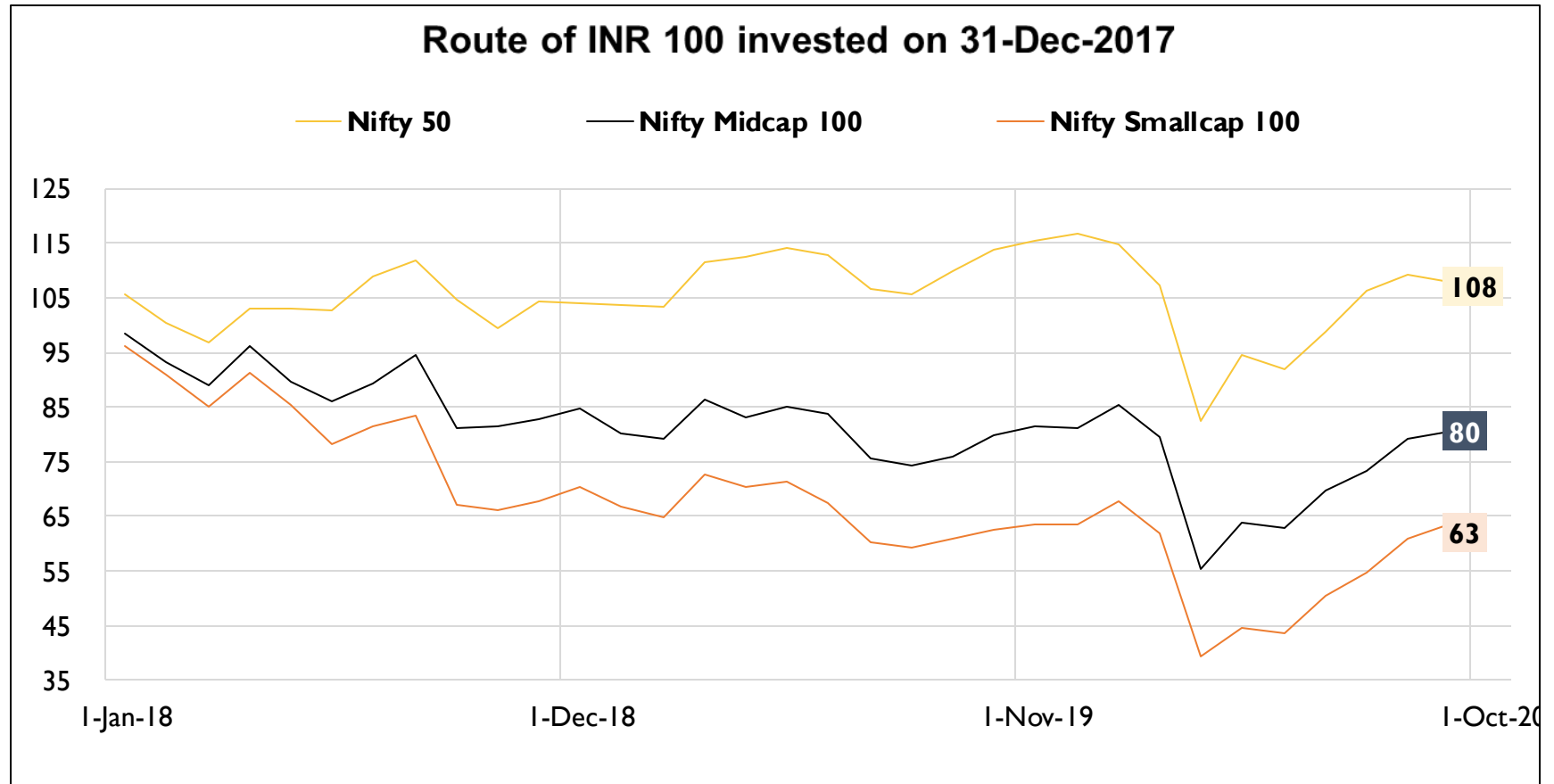
Small-caps in an extreme trough

3-years of successive underperformance unprecedented

Small caps have been underperforming large and mid-caps for over 2 years now ...

...this is unlikely to sustain

Over the last 2-year period, small caps have underperformed both large caps and midcaps

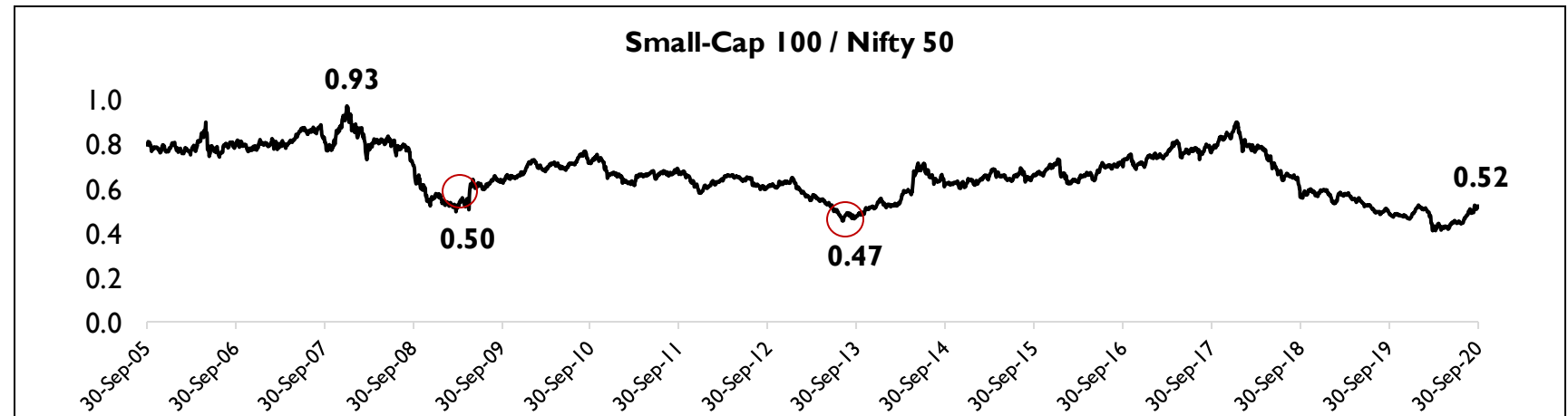
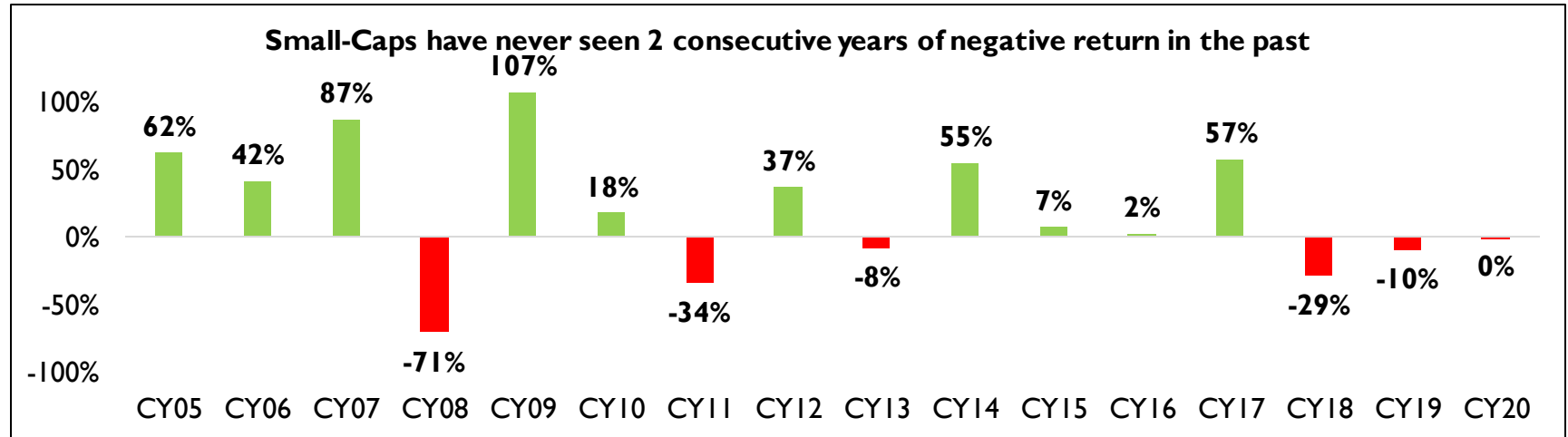


Source: MOAMC Internal Research, Data as on 30.9.2020

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...but now is not the time to exit

- *Small caps have never seen three consecutive years of negative return before 2018*
- *The long term relationship between Small Cap 100 and Nifty 50 indicates that we are at or nearing a trough*



Source: MOAMC Internal Research, Data as on 30.9.2020

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IOP has a successful performance track record ...

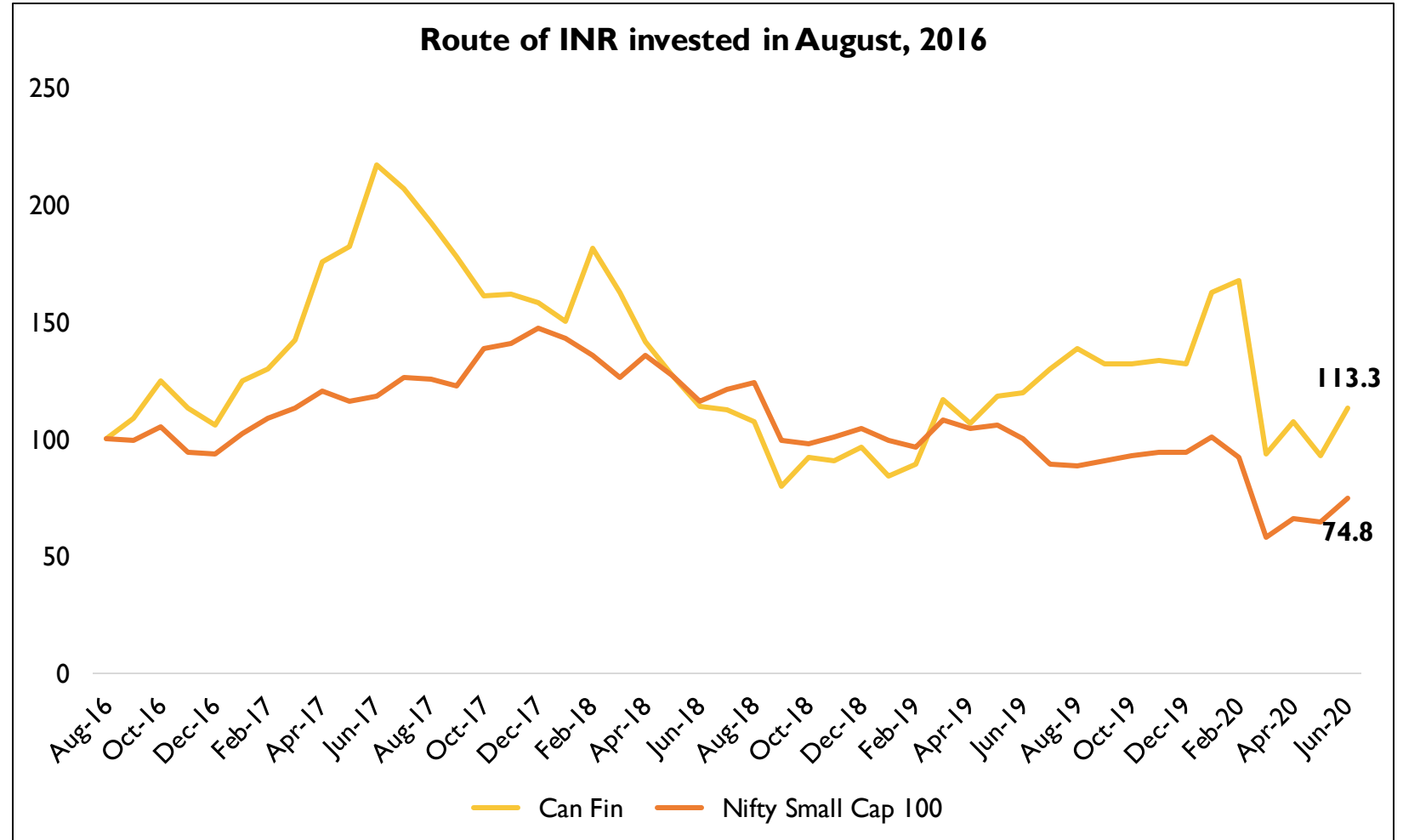
Canfin, Dhanuka, Mahanagar Gas, Alkem, Birla Corp; 2% alpha since inception

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Can Fin Homes: 10% alpha over the benchmark

Sector:
NBFC

Key numbers	
	FY17-20
Average RoE	21%
PAT CAGR	17%
Price CAGR	3%
Nifty 500 TRI	-7%



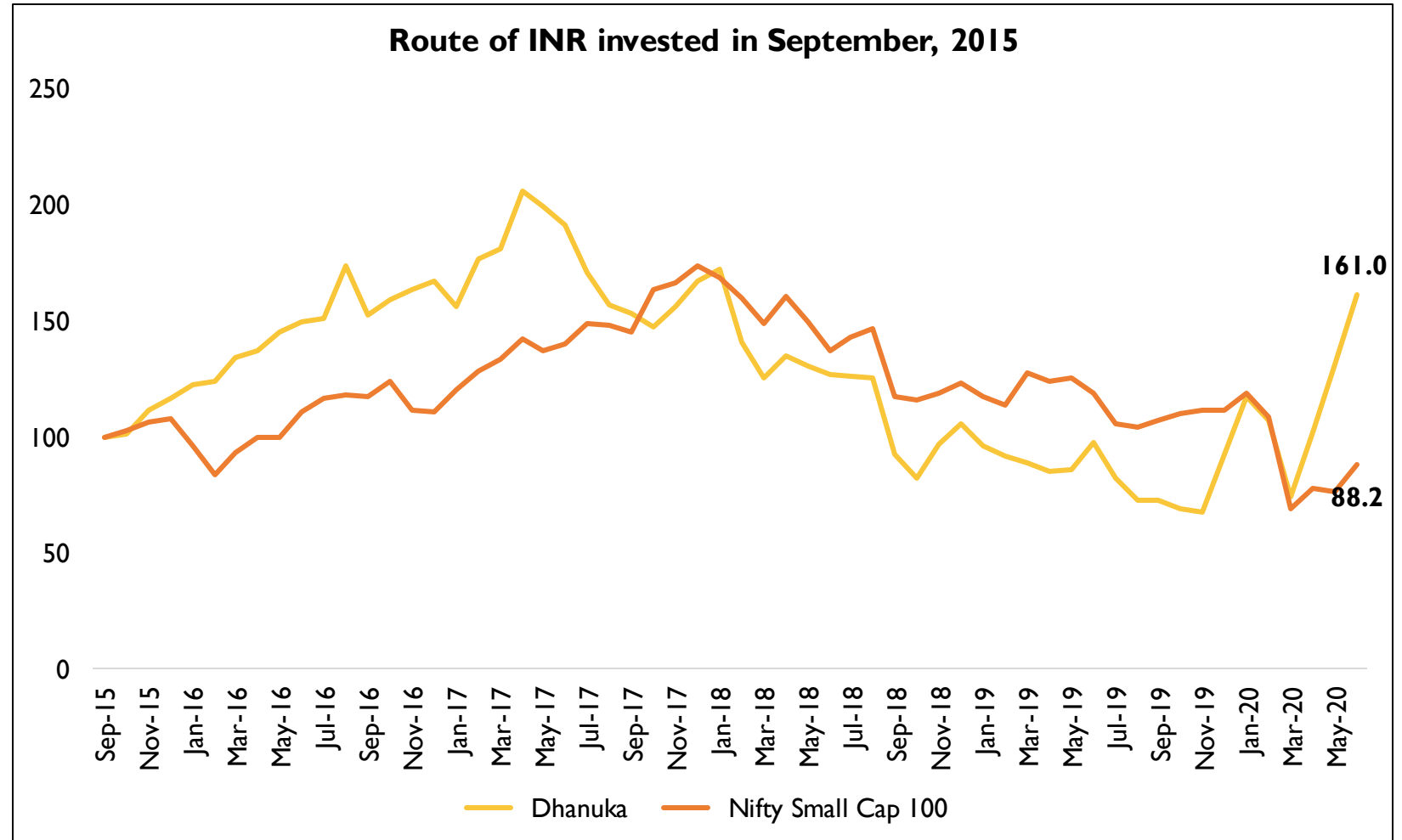
Source: MOAMC Internal Research

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Dhanuka Agritech: 14% alpha over the benchmark

Sector:
Agro-chemicals

Key numbers	
	FY16-20
Average RoE	22%
PAT CAGR	10%
Price CAGR	11%
Nifty 500 TRI	-3%

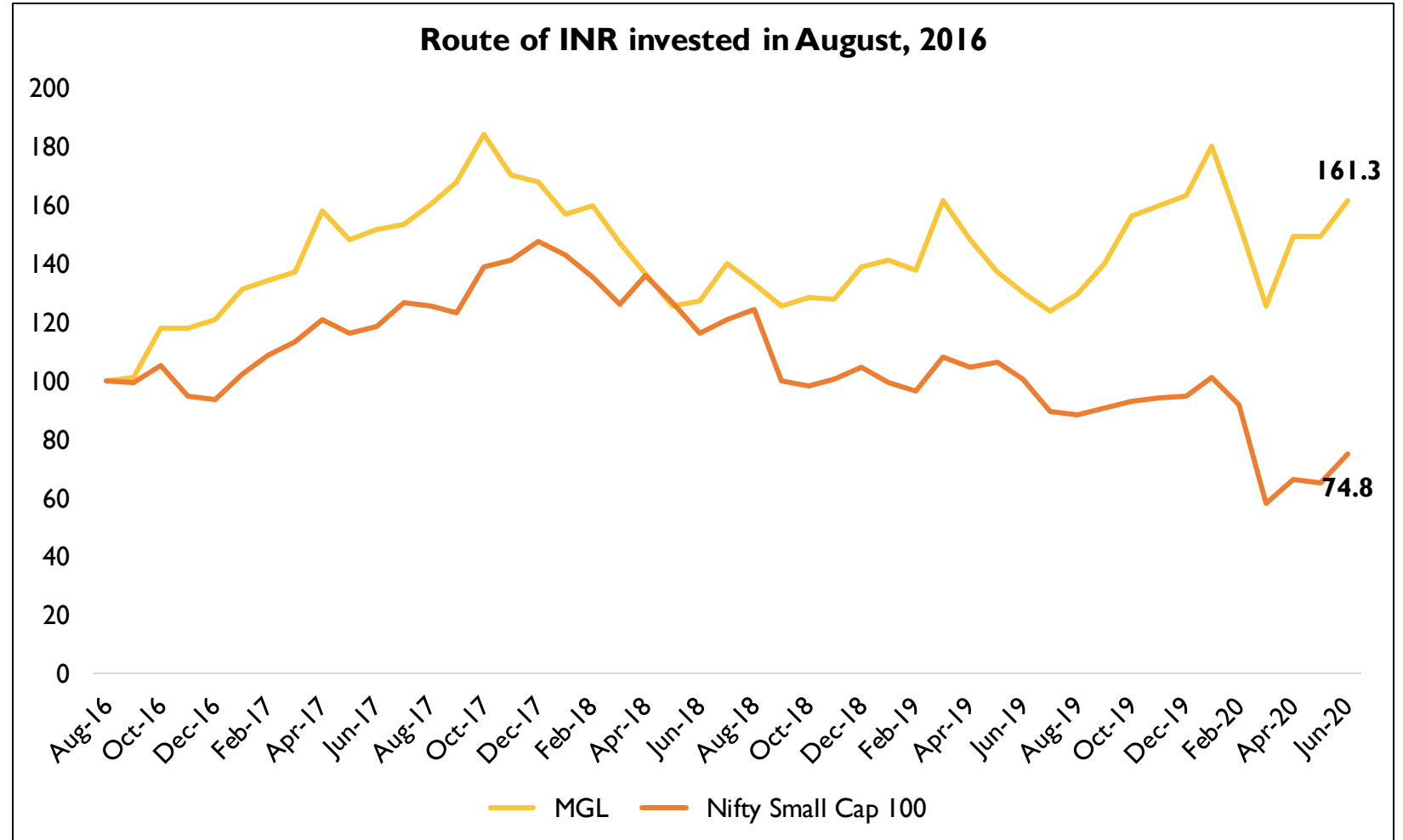


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Mahanagar Gas: 21% alpha over the benchmark

Sector:
Energy

Key numbers	
	FY17-20
Average RoE	24%
PAT CAGR	26%
Price CAGR	14%
Nifty 500 TRI	-7%



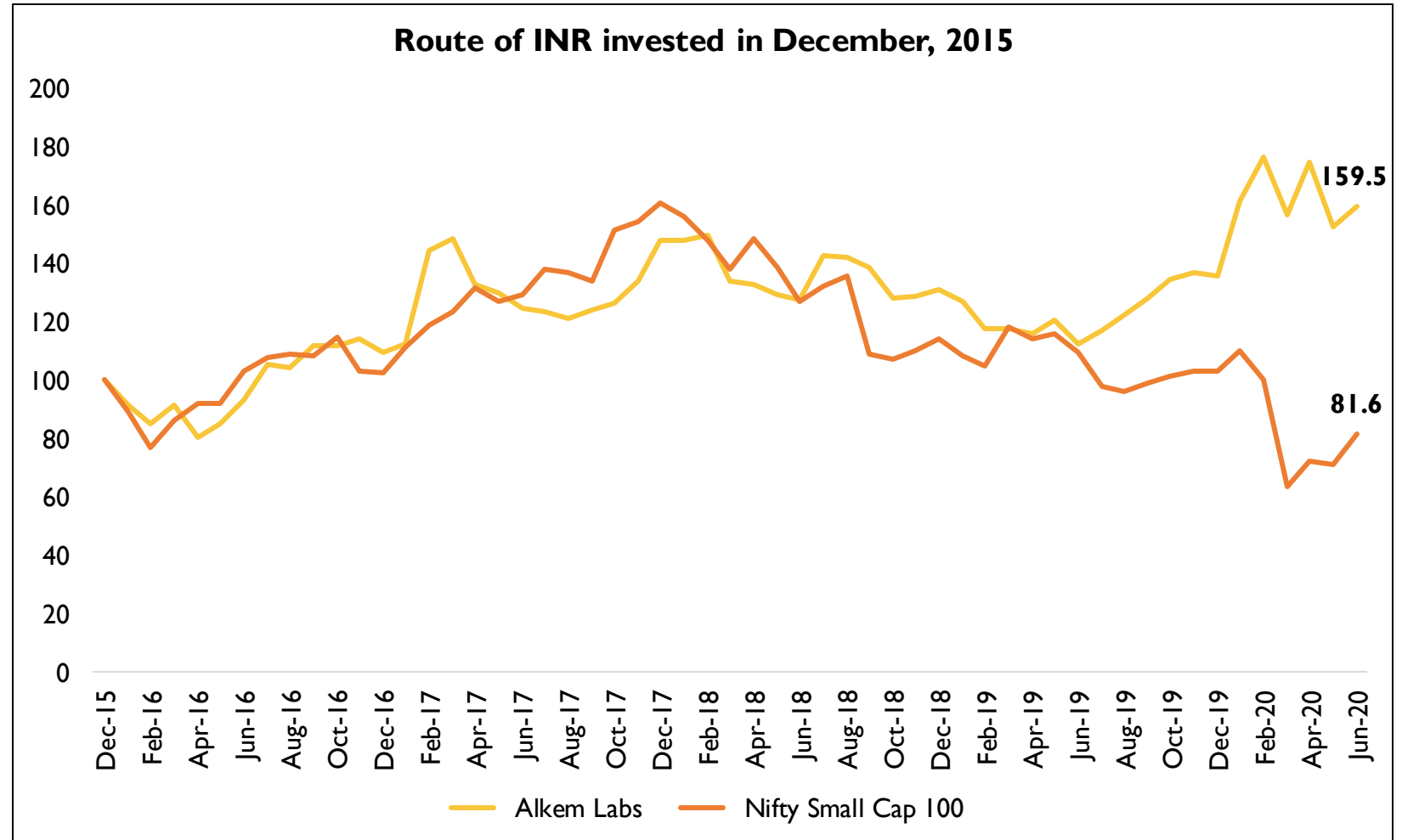
Source: MOAMC Internal Research

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Alkem Labs: 14% alpha over the benchmark

Sector:
Pharmaceuticals

Key numbers	
	FY16-20
Average RoE	18%
PAT CAGR	15%
Price CAGR	11%
Nifty 500 TRI	-3%

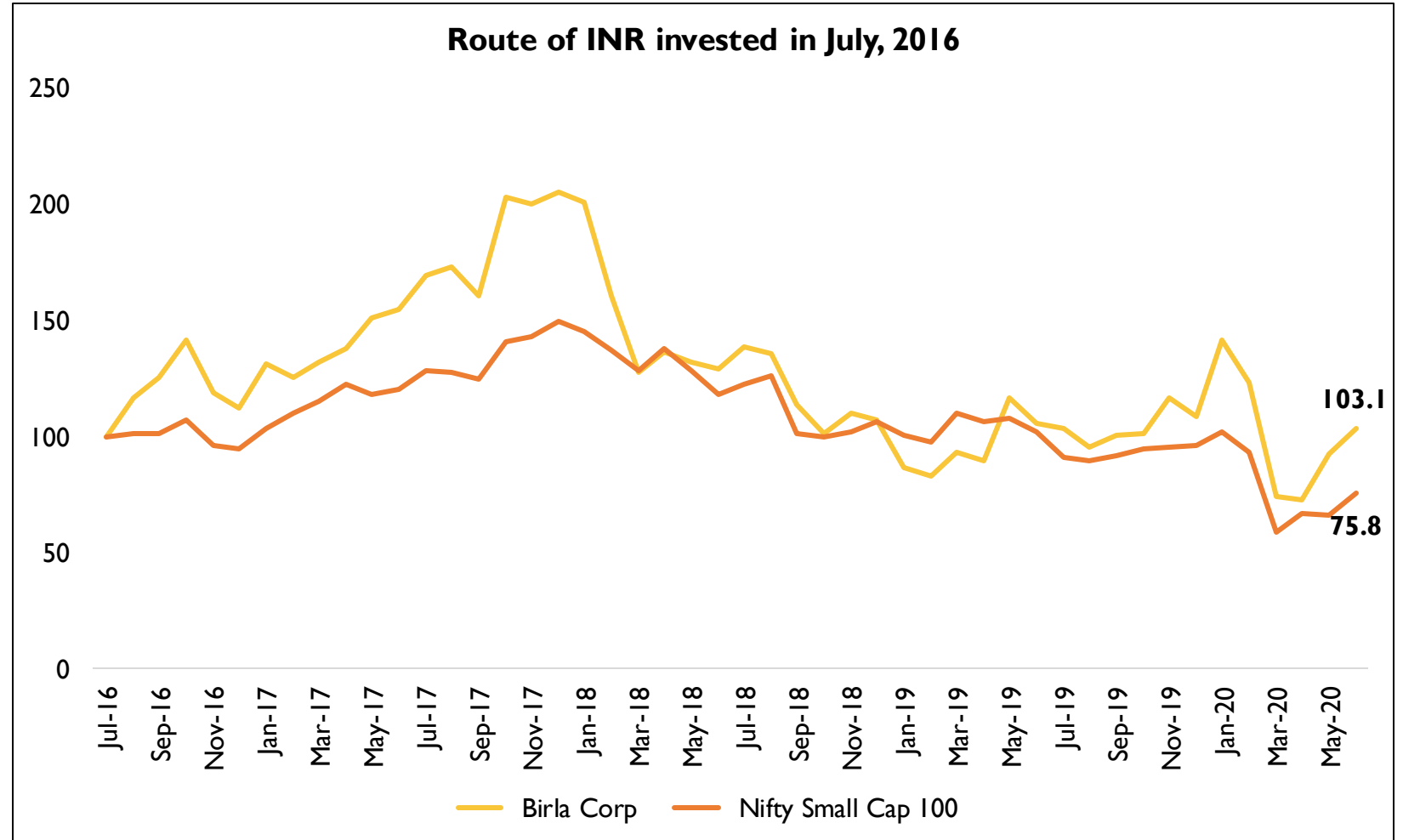


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Birla Corporation: 8% alpha over the benchmark

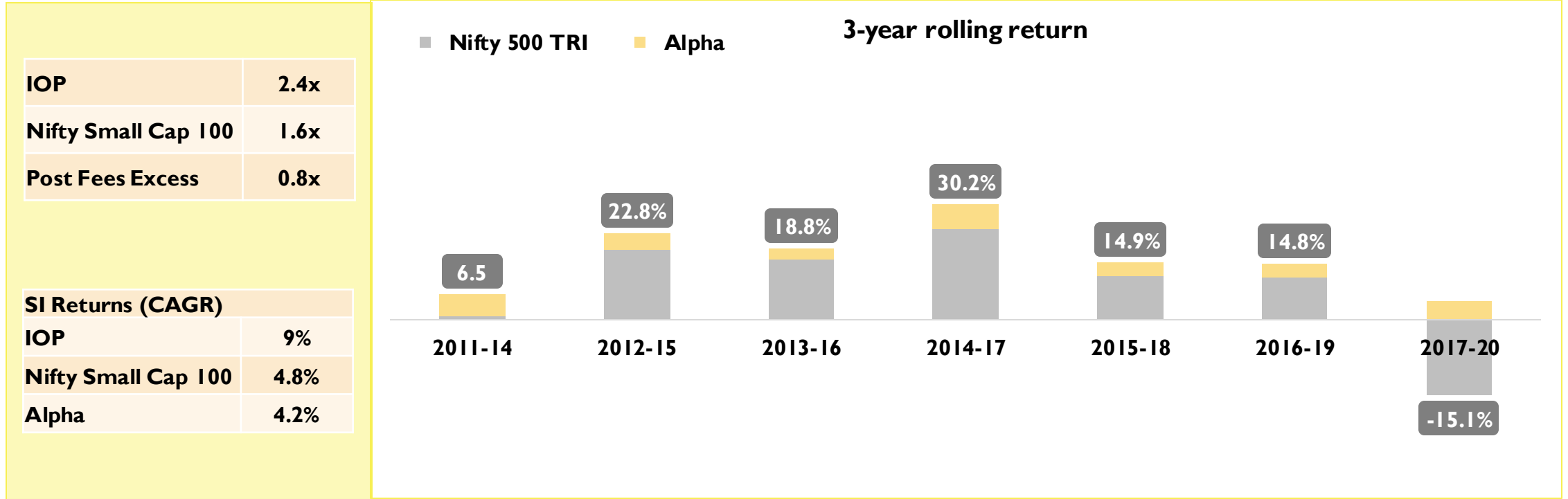
Sector:
Cement

Key numbers	
	FY17-20
Average RoE	7%
PAT CAGR	32%
Price CAGR	1%
Nifty 500 TRI	-7%



Source: MOAMC Internal Research
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Unbroken positive 3-yr rolling returns till Mar-19

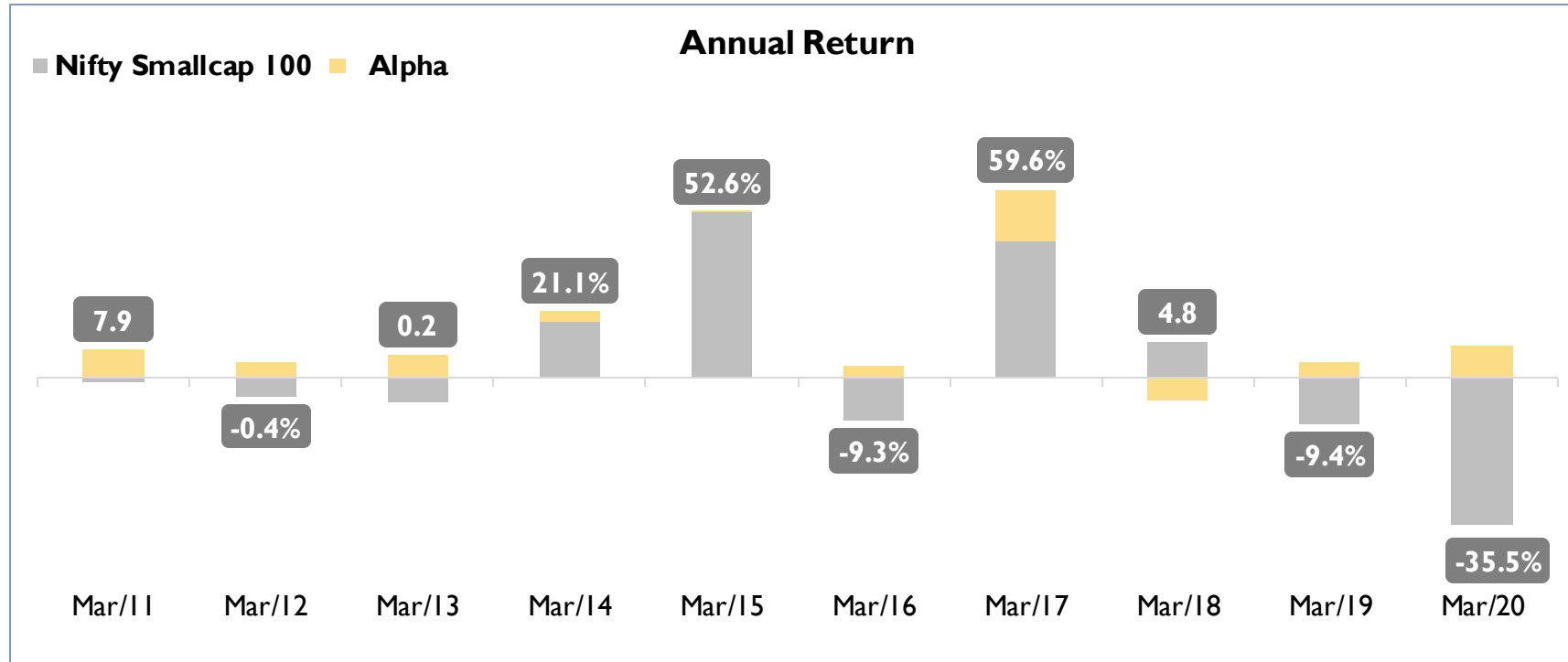


Multi-decadal opportunity to buy into small caps

Source: MOAMC Internal Research

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Positive alpha in 9 out of 10 years



Multi-decadal opportunity to buy into small caps

Source: MOAMC Internal Research, Data as on 31.8.2020

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ASSET MANAGEMENT

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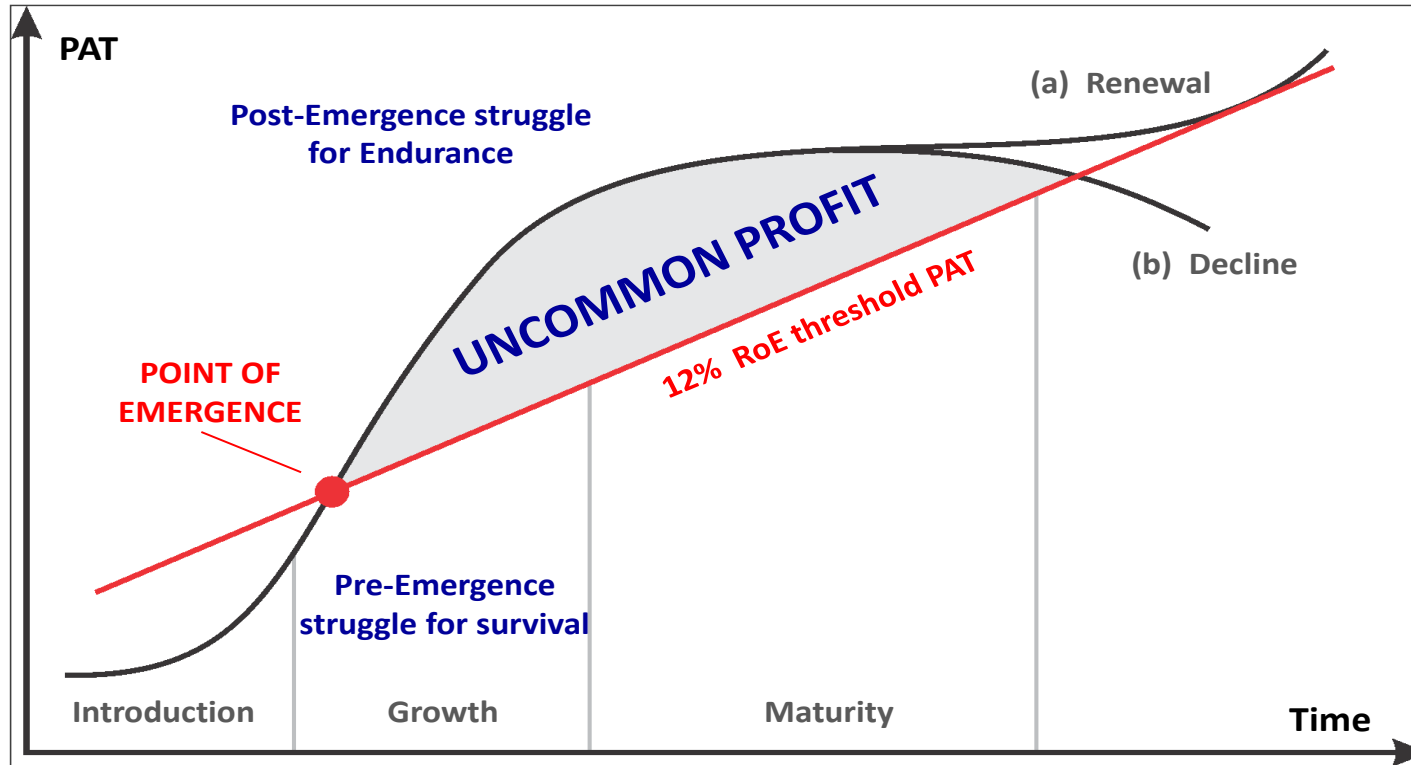
Our key learning: QGLP for small caps can be nuanced

Key learning: QGLP for small caps is somewhat nuanced

- **Q** : In some cases, for small caps, quality is not necessarily proven but emerging
- **G** : Growth of small caps is strongly correlated to economic growth
- **L** : Small caps have a long growth runway, given huge opportunity and small size
- **P** : P stands for both, Price and Patience

Q : In some small caps, Quality not necessarily proven but Emerging

Emergence : When a company's Return on Equity (RoE) exceeds Cost of Equity (CoE)



Source: 18th Motilal Oswal Annual Wealth Creation Study, 2013

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What happens when companies Emerge and then Endure

Endurance : Companies sustaining RoE higher than CoE, post Emergence

Company	Year of Emergence	5-year post emergence (%)			
		PAT CAGR	Avg RoE	Price CAGR	Rel Perf.
Manappuram Finance	2007	123%	28%	70%	64%
Shriram Transport	2001	56%	28%	85%	60%
Shriram City Union	2004	45%	24%	70%	58%
Accelya Kale	2008	36%	31%	60%	56%
Titan Industries	2003	53%	33%	85%	46%
Emami	2007	31%	35%	33%	27%
GRUH Finance	2003	33%	24%	60%	22%
Asahi India Glass	2002	25%	43%	51%	21%
Blue Dart Express	2001	22%	23%	45%	20%
Cera Sanitaryware	2008	36%	24%	29%	17%
Source: 18th Motilal Oswal Annual Wealth Creation Study, 2013					

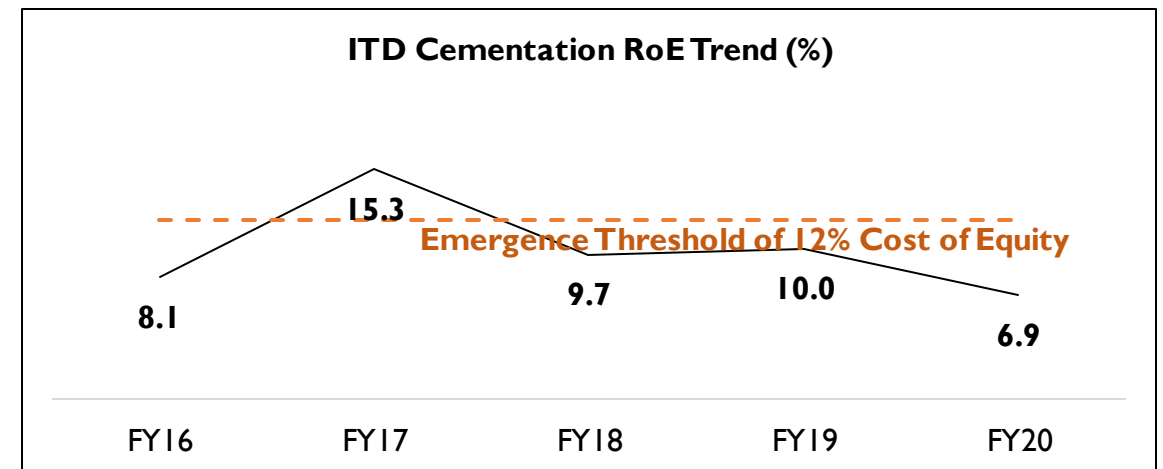
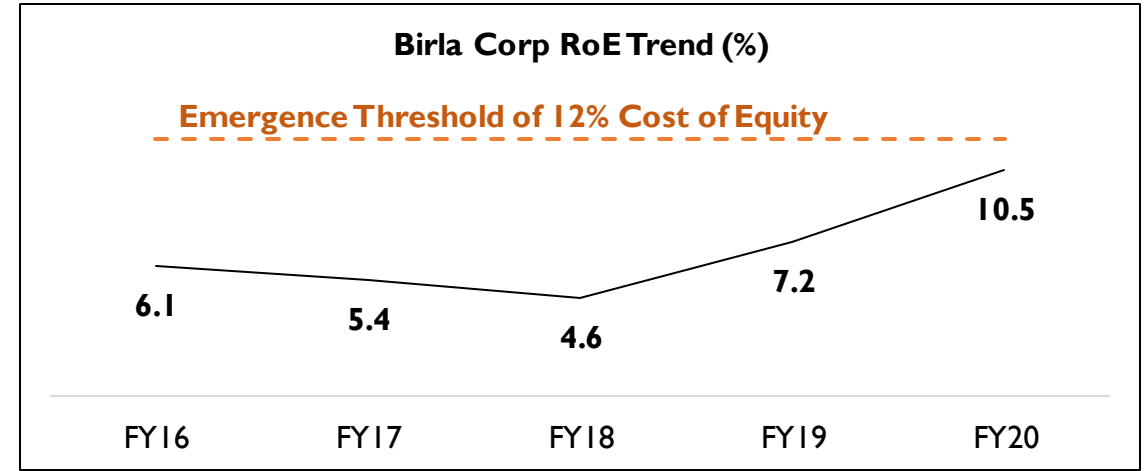
Source: MOAMC Internal Research, Data as on 31.8.2020

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Some IOP companies on the verge of Emergence

➤ **Birla Corp** likely to cross Emergence threshold soon on the back of robust cement demand

➤ **ITD** has already done it once; it should repeat with economic recovery

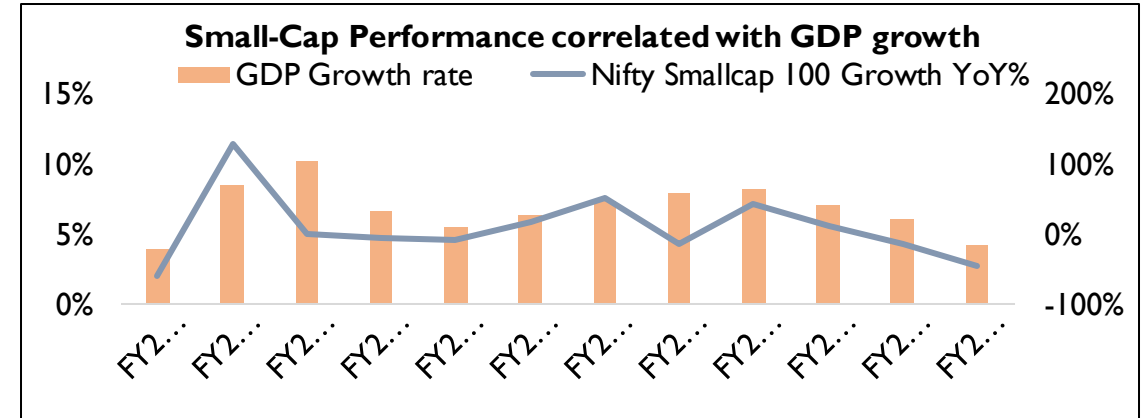


Source: MOAMC Internal Research, Data till FY20

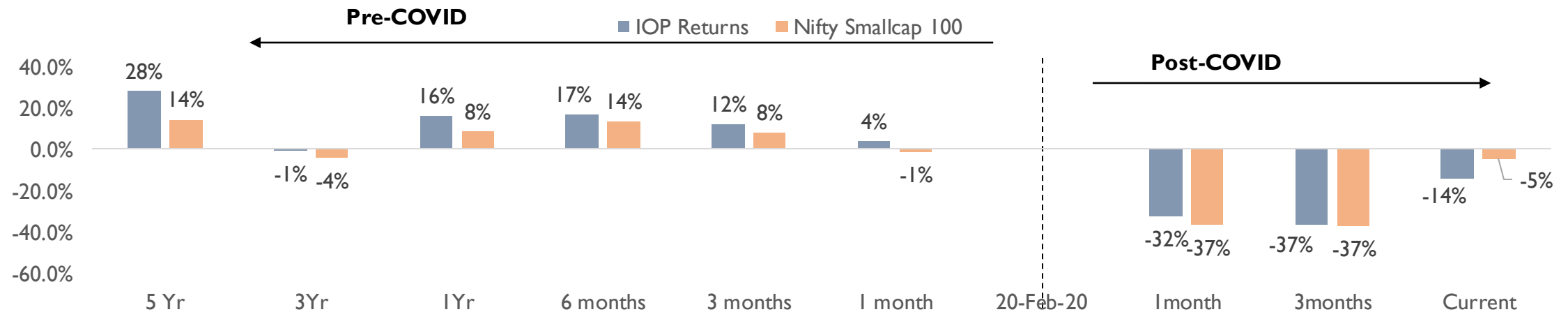
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G : Small caps growth is strongly correlated with GDP growth

- Pre-Covid economic recovery saw IOP beginning to outperform.
- However, Covid has significantly set back both the economy and IOP
- Post-Covid green shoots of economic recovery visible
- FY22 should see full impact



Absolute Returns Pre and Post COVID

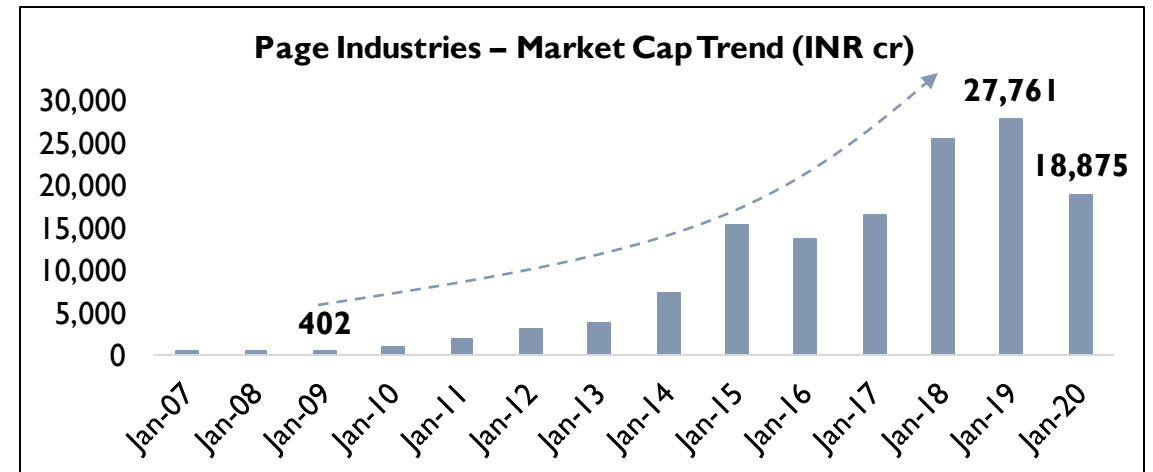
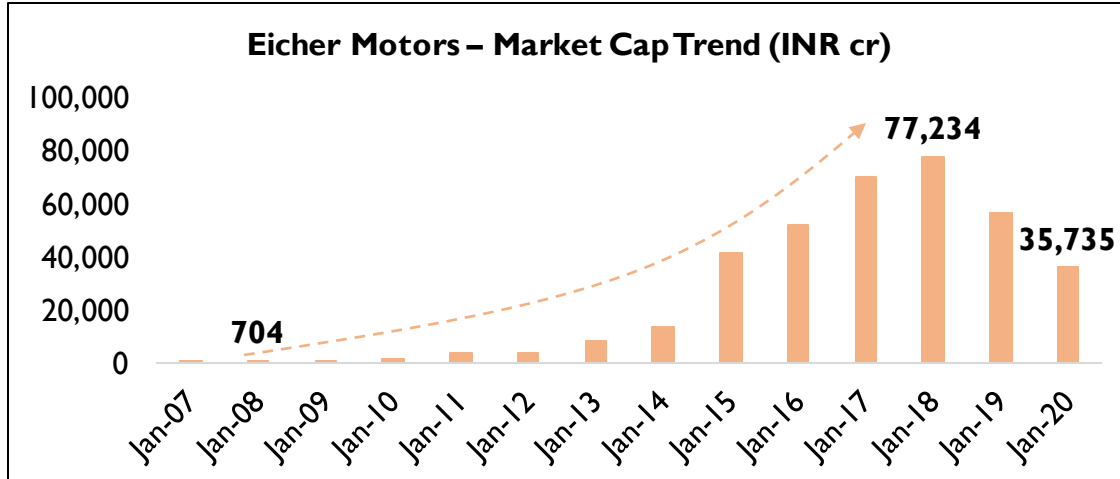
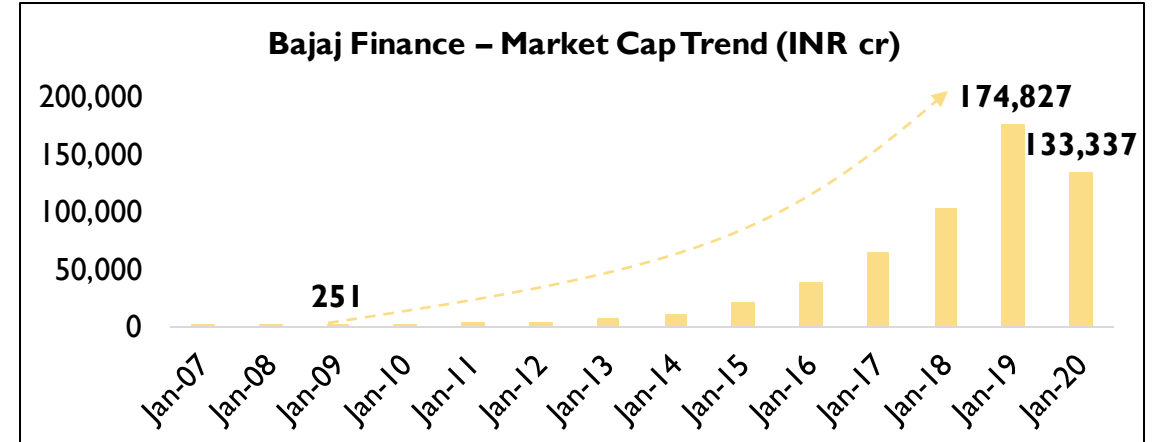


Source: MOAMC Internal Research, Data as on 30.9.2020

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L : Small caps can grow 100x in 10 years

- Many businesses in India offer huge growth potential
- Small caps, given their size, have a long runway for growth
- The full benefit of this is reaped by those investors who hold for the long term
- The key – high quality of management

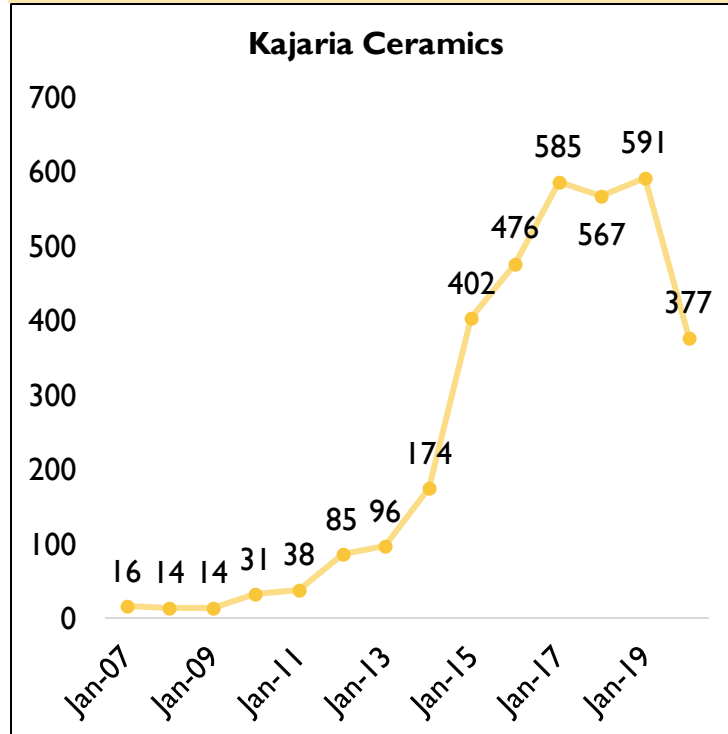


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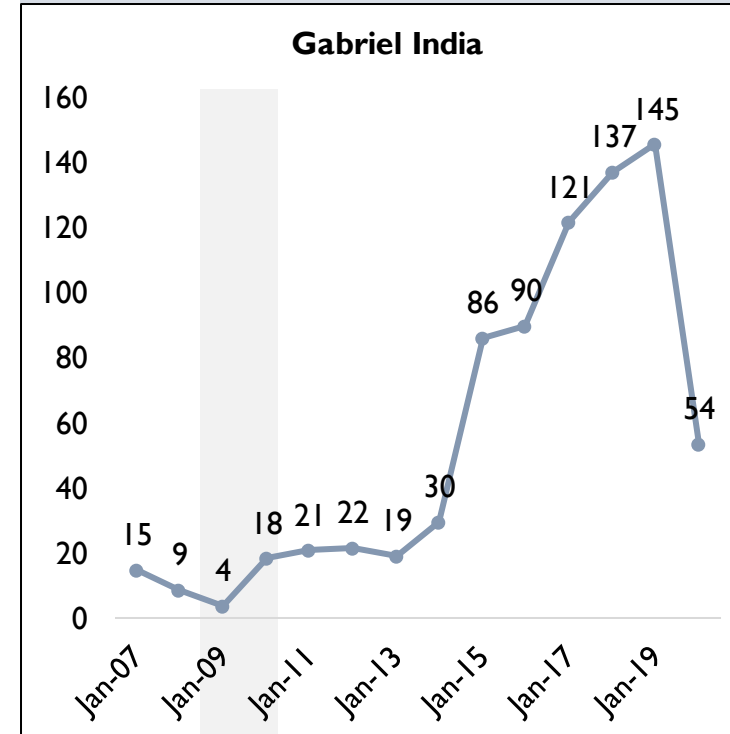
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P : Stands for both Price and Patience

Rarely do small caps rise steadily one way like Kajaria Ceramics...



... or Gabriel (down 60% in 2009), before rising handsomely



Making money in small caps needs the vision to see, courage to buy and patience to hold

Source: MOAMC Internal Research

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Key stocks of our holdings

Kajaria, Aegis Logistics, Alkem, Qness, ITD

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High conviction stocks

Aegis Logistics

- Increase LNG imports due to increased demand
- Competition unlikely to eat into volumes
- Underpenetrated market
- Capacity expansion

Alkem Labs

- Shift from acute to chronic would improve margins over the long term
- company aims to maintain its pace of 10-12 launches per year over the next 3-4 year
- ALKEM's US sales are likely to deliver 16% CAGR at ~USD420m over FY20-22E

Mahanagar Gas

- Volume Growth:4-6% in the medium term
- Sustainable margins
- Monopoly
- Strong dividend payout of 55%

Birla Corp

- Capacity expansion to enable higher growth than industry
- Profitability on an overall basis expected to remain strong; Premium sales in trade segment grew 41% in FY 20
- Additional revenue streams launched

ICICI Securities

- Beneficiary of regulatory led consolidation
- 27% of NSE active client base and 20% of market turnover up for grabs
- Low risk to distribution yields
- Cost to Income ratio can come go below 50%

Kajaria Ceramics

- Net cash balance sheet and superior brand, will help capitalise on market share gain
- Earnings estimates have been revised, given the commentary by management on production and demand traction

High conviction stocks

Qess Corp

- Poised to benefit from labour reforms.
- The sharp bounce back in the urban unemployment (to 11% from COVID-19 peaks of 31%)
- Staffing firms tend to gain during phases of job market recovery
- Addressing key investor concerns in areas of capital allocation, balance sheet and governance
- Stock is currently trading at ~13x FY22 EPS at ~40% discount to Teamlease
- Cheap valuations also provide adequate margin of safety.

ITD Cementation

- Bright mid to long-term prospects: Significantly de-levered balance sheet
- Blended efficiency of 50% across operational work-sites - Significant recovery expected by Q3.
- Cost control measures: Negative operating leverage | HFY21 will result in PAT breakeven for FY21E.
- Stands to benefit from the strong upcoming order pipeline in Roads, Marine and Urban infrastructure projects
- ITD has won new orders worth INR 60 bn in FY20 taking total order book to INR 107 bn.
- Strong B / S and strong order book will limit downside

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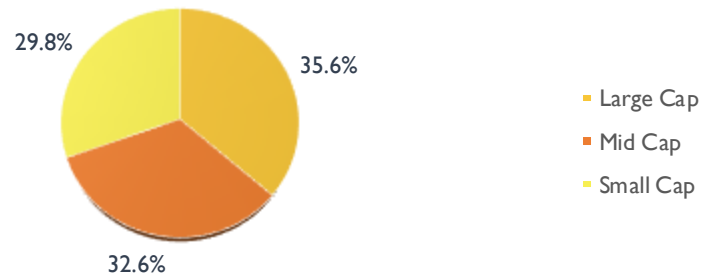
Portfolio Performance

Alpha of 0.5% CAGR since inception

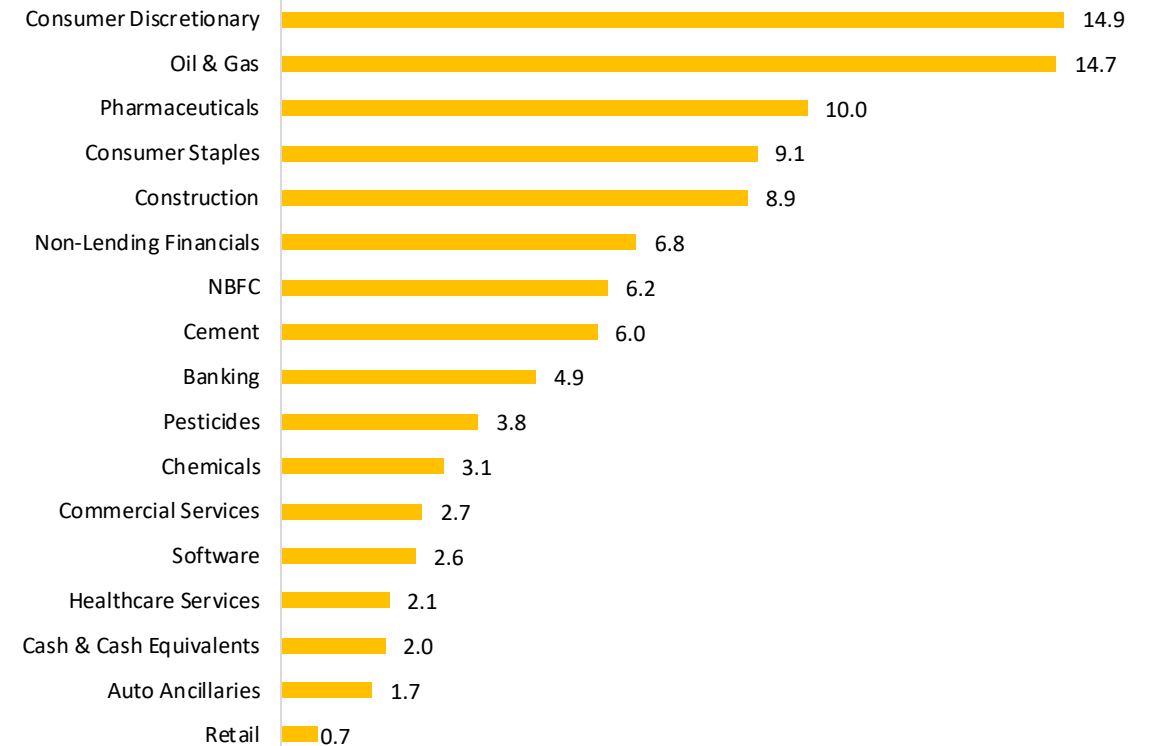
Portfolio Allocation

Top 10 Holdings & Market Capitalization

Scrip Name	% Holding
Reliance Industries Ltd.	9.1
Alkem Laboratories Ltd.	8.4
Kajaria Ceramics Ltd.	7.6
TTK Prestige Ltd.	7.5
ICICI Securities Ltd.	6.8
ITC Ltd.	6.7
Can Fin Homes Ltd.	6.2
Birla Corporation Ltd.	6.0
Mahanagar Gas Ltd.	5.6
Blue Star Ltd.	4.9

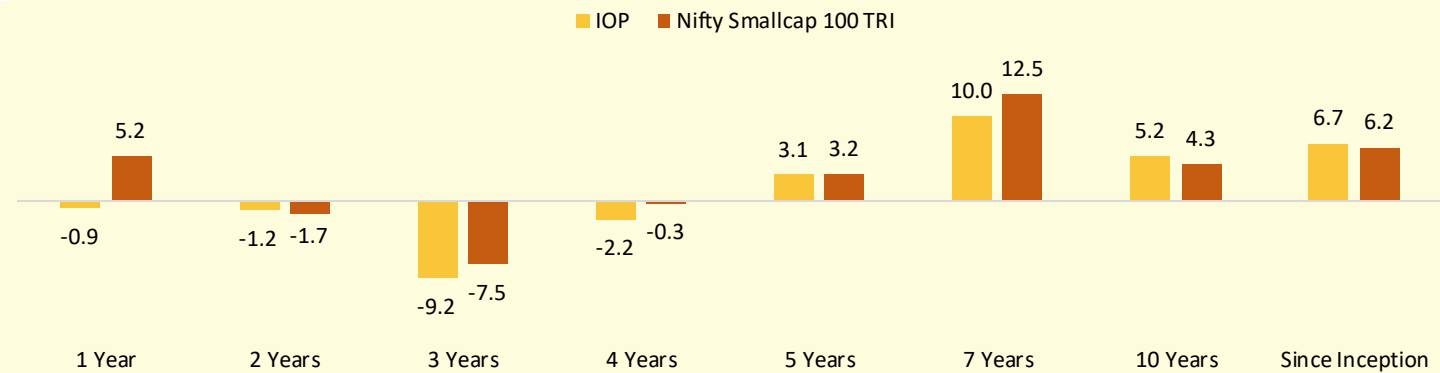
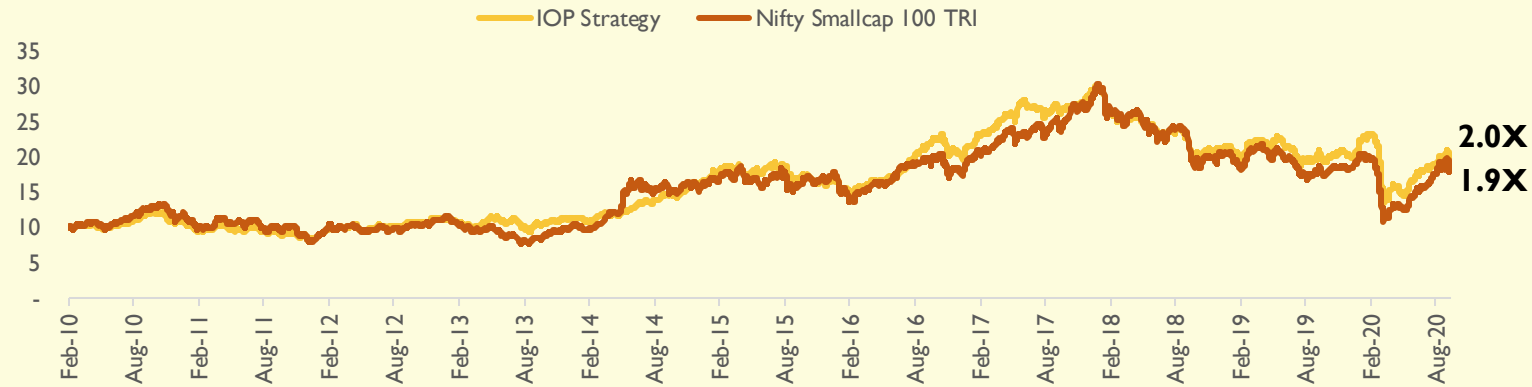


Sectoral Allocation



IOP Strategy Inception Date: 15th Feb 2010; Data as on 30th September 2020; Data Source: MOAMC Internal Research; RFR: 7.25%; *Earnings as of June 2020 quarter and market price as on 30th September 2020; Source: Capitaline and Internal Analysis; Please Note: Returns up to 1 year are absolute & over 1 year are Compounded Annualized. Returns calculated using Time Weighted Rate of Return (TWRR) at an aggregate strategy level. The performance related information is not verified by SEBI. All portfolio related holdings and sector data provided above is for model portfolio. Returns & Portfolio of client may vary vis-à-vis as compared to Investment Approach aggregate level returns due to various factors viz. timing of investment/ additional investment, timing of withdrawals, specific client mandates, variation of expenses charged & dividend income. Past performance may or may not be sustained in future and should not be used as a basis for comparison with other investments.

Portfolio Performance



IOP Strategy has delivered a CAGR of 6.7% vs. Nifty Smallcap 100 TRI returns of 6.2%, an outperformance of 0.5% (CAGR) since inception (15th February 2010)

IOP Strategy Inception Date: 15th Feb 2010; Data as on 30th September 2020; Data Source: MOAMC Internal Research; RFR: 7.25%; *Earnings as of June 2020 quarter and market price as on 30th September 2020; Source: Capitaline and Internal Analysis; Please Note: Returns up to 1 year are absolute & over 1 year are Compounded Annualized. Returns calculated using Time Weighted Rate of Return (TWRR) at an aggregate strategy level. The performance related information is not verified by SEBI. All portfolio related holdings and sector data provided above is for model portfolio. Returns & Portfolio of client may vary vis-à-vis as compared to Investment Approach aggregate level returns due to various factors viz. timing of investment/ additional investment, timing of withdrawals, specific client mandates, variation of expenses charged & dividend income. Past performance may or may not be sustained in future and should not be used as a basis for comparison with other investments.

The opportunity's still there

FY22 Portfolio earnings growth of 38%; Valuations attractive

IOP estimates – FY22 PAT growth of 38%; FY22 P/E at 16x

Company	Weight	PAT YoY		P/E (x)
		FY22E	FY20-23E CAGR	
Birla Corpn.	9%	4%	-12%	11
Mahanagar Gas	8%	42%	0%	13
Alkem Lab	8%	8%	12%	19
TTK Prestige	8%	24%	-1%	40
Aegis Logistics	8%	41%	107%	14
AU Small Finance	7%	65%	16%	18
Dr Lal Pathlabs	7%	43%	13%	45
Can Fin Homes	6%	22%	8%	10
DCB Bank	5%	43%	2%	7
Kajaria Ceramics	5%	67%	9%	21
Gabriel India	5%	98%	7%	13
Blue Star	4%	413%	5%	31
Dhanuka Agritech	4%	10%	19%	17
Bayer Crop Sci.	4%	12%	31%	33
Qess Corp	3%	60%	L to P	21
PORTFOLIO	100%	38%	12%	16

Investors who invest in the good times and hold back in the bad times can never make above average returns.

Small Cap stocks are a volatile and unpredictable lot...

...but may provide the greatest opportunities for upside

To earn super-normal returns with small cap stocks:

- **Be patient**
- **Never exit looking at rear-view performance**
- **Double up at extremes if possible**

Thank You!

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ASSET MANAGEMENT

BUY RIGHT
SIT TIGHT

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