

MONTHLY Communique

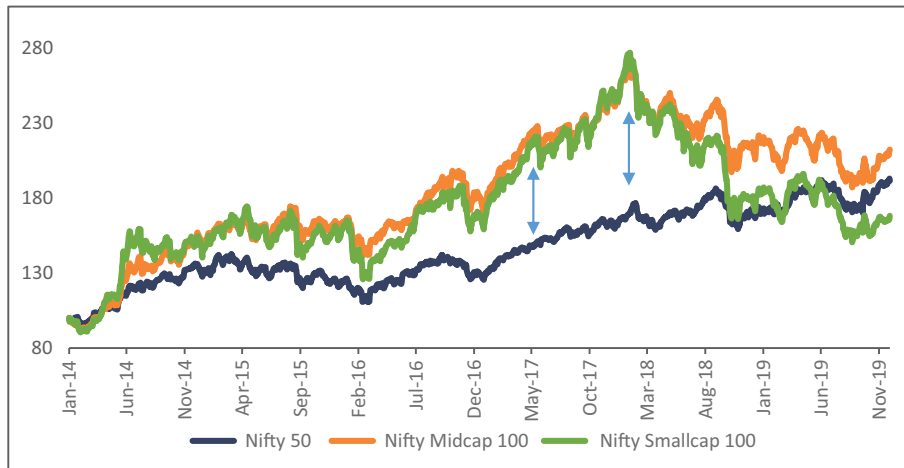
December 2019



Aashish P Somaiyaa
(MD & CEO)

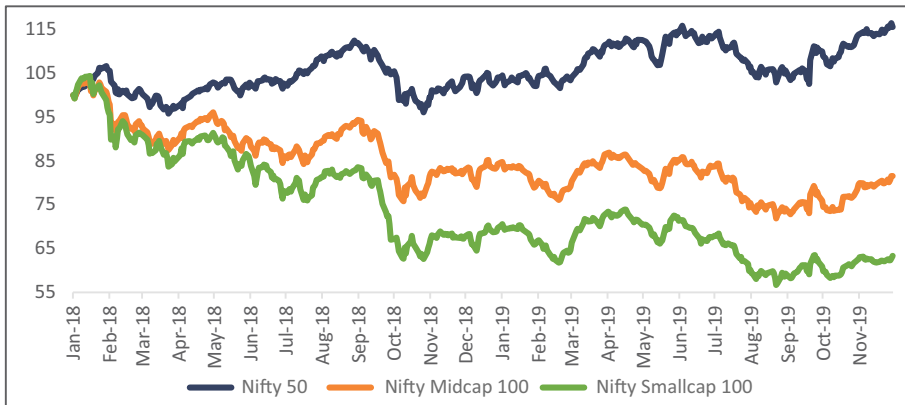
Dear Investors and my dear advisor friends,

The most common refrain I have heard in the last two years is, “Markets are at all-time high” and my portfolio is nowhere close” or “Markets are at all-time high and my portfolio is negative”. This depends on what you call as “market”. Usually most people form their impression of what is happening in the “market” by seeing what is happening in Nifty or Sensex. Up until 2018 usually the correlation of Sensex and Nifty with the broader market was not a concern because either everything moved in tandem or the midcaps and smallcaps actually did better than Sensex or Nifty. But since January 2018, the correlation between Nifty and the rest is broken. The below charts, one for the last 5 years and one since January 2018 respectively will illustrate pictorially what I am stating here.



Source: Motilal Oswal Asset Management Internal Analysis. Data as on 30.11.2019

Over a longer period of 5 years not only did the Nifty move in tandem with the midcap and small cap indices, infact the midcap and smallcaps outperformed Nifty very significantly.



Source: Motilal Oswal Asset Management Internal Analysis. Data as on 30.11.2019

(Continued overleaf)

THINK EQUITY
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MOTILAL OSWAL
Asset Management
PORTFOLIO STRATEGY

BUY RIGHT
SIT TIGHT



But since 2018, the rise of Nifty alone and the slump in midcap and smallcap indices has been a cause of great concern for investors.

Despite this experience, over the last nearly 2 decades of investing experience, we at Motilal Oswal AMC are strong believers in creating wealth by picking midcap stocks and holding them over a number of years. Let me explain why.

The picture below has 3 grids. The “x” axis has “FROM” and the “y” axis has “TO”. Each grid tells you that at the beginning of a 5 year period if you had started by buying the entire bouquet of small, mid and large cap companies and held them for the 5 years dispassionately, what kind of market cap migration (wealth creation / destruction) you would see.

The most potential migrations are related to midcap companies defined here as stocks from market cap ranking 101 till 300. While the recent regulatory definition last year calls rank 101 to 250 as midcap, we at Motilal Oswal AMC have been publishing these grids in every Wealth Creation Study published by our Chairman over the years. Anyway it is not so much about where the definitions and the ranks are cut at, because market capitalization ranks are a continuum and there is not much size difference between rank 250 and say 251 or 260. As per current numbers, roughly the top 100 companies (largecap) start at 10 lac crs and end at approx. 30,000 and from thereon till say 6,000 crs (300th rank) is midcap as per the below analysis. Everything from 6000 crs below is small (mini)cap. Small (mini)cap shows a huge number of companies and within that too one can cut-off at say 4,000 crs (400th rank) and still pick stocks applying filters for sector leadership, brands, RoEs, EPS growth, leverage ratios, cyclicity of business etc.

Coming back to the midcap discussion, take the grid on the extreme right for example. What one can see is that in the 5 years’ time frame out of 200 midcap companies 88 companies degenerated to becoming smallcap and delivered a negative CAGR of 19%. On the other hand 88 companies remained midcap and delivered 9% CAGR and 24 companies actually migrated upwards to becoming large cap and delivered average 33% CAGR. So about 50% odd midcap companies remained midcap or migrated to large cap and gave positive compounding. If you follow the same midcap migration column in the other grids you will find that for the period 2005-10 and 200-05 also, around 50% of the midcap companies remained midcap or migrated to becoming large cap. As per analysis done by us, this probability of success in the midcap universe holds true across any 5 year time frame. Now, let me capture a few learnings from these tables:

Mini, Mid, Mega crossovers - 2000-05, 2005-10, 2010-15 Note: Figures In brackets indicate number of companies

2000-05: Median return CAGR

Market return: 5%

To	Mega	158% (1)	55% (17)	21% (59)
	Mid	57% (58)	21% (90)	-4% (28)
	Mini	19% (1,039)	-3% (93)	-40% (13)
		Mini	Mid	Mega
		From		
Total stocks	1,098	200	100	

2005-10: Median return CAGR

Market return: 22%

To	Mega	76% (2)	46% (9)	27% (66)
	Mid	61% (25)	24% (89)	9% (32)
	Mini	11% (1,465)	4% (102)	-32% (3)
		Mini	Mid	Mega
		From		
Total stocks	1,492	200	100	

2010-15: Median return CAGR

Market return: 10%

To	Mega	68% (3)	33% (24)	11% (71)
	Mid	38% (64)	9% (88)	-13% (26)
	Mini	0% (1,841)	-19% (88)	-32% (3)
		Mini	Mid	Mega
		From		
Total stocks	1,908	200	100	

Source: Mid to Mega – 20th Wealth Creation Study by Raamdeo Agarwal

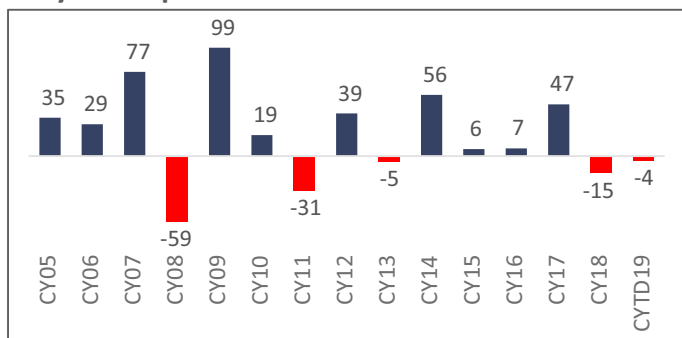
- 1) For any given 5 year period, maximum wealth is created when a small cap company becomes mid/ large cap and a mid-cap company becomes a large cap
- 2) If one invests in midcaps, the probability that a midcap will remain or become large cap in 5 years and rewards investors, is as high as ~50%

- 3) In any 5 year cycle when this plays out, there are 2-3 terrible years and 2-3 great years. 2000-2003 were very bad followed by 2004-05, 2005-07 were great followed by 2008-09, 2010-13 were terrible followed by 2014-15
- 4) Rather than getting stuck with definitions of small or midcap, one must look to understand probabilities and improve probabilities of success as a stock picker by applying appropriate quality (Q), growth (G) and longevity (L) filters. Since market cap ranks are a continuum and not distinct strata of companies, smallcaps as per above grid should still be invested into but by isolating the really small ones say below Rs 3,000 crs or Rs 4,000 crs (approx. 400-500th rank) and then applying fundamental filters.
- 5) It is estimated that if an investor invests for 5 years in midcaps and the higher market cap ranges of small caps they can make outsized returns irrespective of the journey in between; much like the quality of a seed can't be concluded upon until it is allowed to sprout. All the same, if one keeps digging to see the progress on a daily basis one can rest assured there will be no plant at the end of the process.
- 6) Stock picking is probabilistic in nature especially when dealing with smallcaps and midcaps but probabilities of picking right stocks are greatly enhanced when professionals apply certain filters on quality and growth orientation and corroborate via research processes. This is why philosophy and process are important to focus on what might work and weed out the obvious tripping points.

Hence, please do not worry about how your experience of investing in midcaps / smallcaps has been in the past 2-3 years. A 5 years' time frame is good enough for one to make good returns. If the first 2-3 years are great the rest of the period may be rocky and if the first 2-3 years are rocky the balance period tends to make up. It is worth thinking what the opportunity is for anyone who chooses to initiate investment in small and midcaps at this point in time. Let us not drive with eyes on the rear-view mirror! It's the large cap part of the market which is at highs, but the midcaps have corrected severely and all of them do not have fundamental performance issues. These are unusual times and we must take benefit of the same because capturing opportunity is what investing is about. What worked in the last 2 years was an opportunity 2 years back, what will work in future is the opportunity now and that is in midcap and quality small caps.

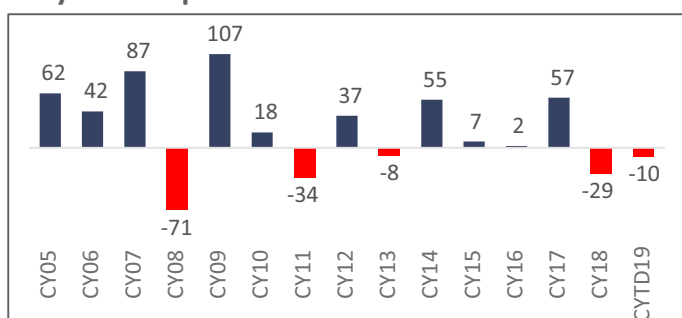
Those who invested 5 years back have made a reasonable returns despite last 2 years not being great, those who have invested two years back have a very high probability of seeing a good patch of next 2-3 years. Please do not get caught up in oversimplified arithmetic like, "if 100 has become 80 after two years how much does it need to go up for me to make great returns". Equity is not a linear asset class and returns never flow as per simple arithmetical calculations. A non-linear / geometric / exponential asset class always moves something like what you will see below:

Nifty Midcap 100 Index



- 1) Mid and Small caps tend to perform in extremes and revive sharply after bouts of negative returns
- 2) After the correction in the last 2 years, a significant revival in performance is a high probability event in next 2-3 years.
- 3) It has never happened that there are successive years of decline.

Nifty Smallcap 100 Index



Source: Motilal Oswal Asset Management Internal Analysis; Data as on 30th November 2019



Having noted this pocket of opportunity that has been created, see where mutual funds, insurance companies and other financial institutions are consistently piling investors' monies into. PMS portfolios have the distinct ability not to get straight-jacketed into definitions of midcaps and large caps which I like drawing a line in the sand but anathema to capitalizing on investment opportunities.

	Jun13-Jun14	Jun16-Jun17	Jun18-Jun19	(in ₹ crore)
Mutual Fund, Insurance and FI Investments	5,52,693	11,96,225	18,45,125	
Incremental Investment During the year	1,39,095	2,20,219	1,77,817	
FRESH INVESTMENT DIRECTED TOWARDS				
Top 50 companies	16%	36%	77%	
51 - 100 companies	15%	14%	7%	
101 - 200 companies	32%	21%	12%	
200 - 300 companies	13%	13%	3%	
300 - 400 companies	6%	6%	1%	
400 - 500 companies	16%	9%	-1%	

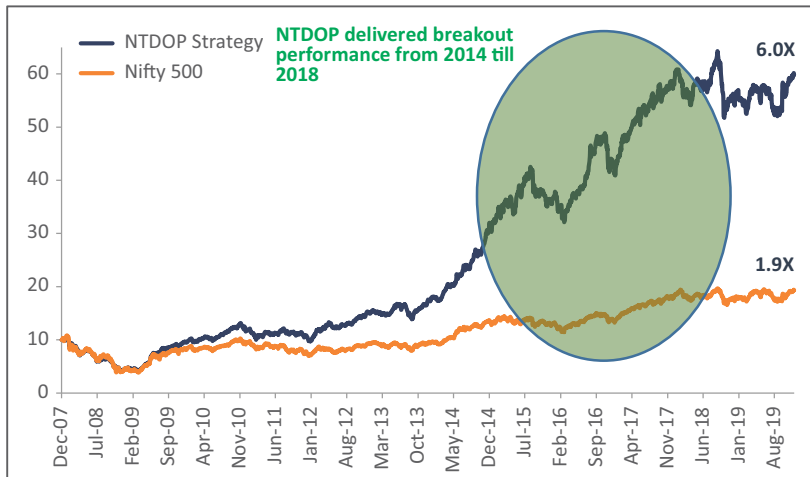
Source: Economic Times dated December 5, 2019.

We have mid and small cap exposure across NTDOP, IOP and IOP2. NTDOP is about 50% midcap and IOP portfolios are almost entirely mid and small cap. We have seen significant outperformance over index in 2016-2017, we have seen a fall in values in line with index in 2018 and we have seen a huge outperformance over corresponding index post the market bottom in October 2018. This is not to say that one must draw solace or that we draw solace in beating the index; we are here to create wealth for our investors and for our own investments alongside our investors.

But the first sign that we have something working for us is when we see that we are clearly breaking away from the rest of the market.

Rs. 1 cr invested in NTDOP Strategy at inception (5th Dec 2007) is worth Rs. 6.0 cr as on 30th November 2019. For the same period Rs. 1 cr invested in Nifty 500 Index is now worth Rs. 1.9 cr.

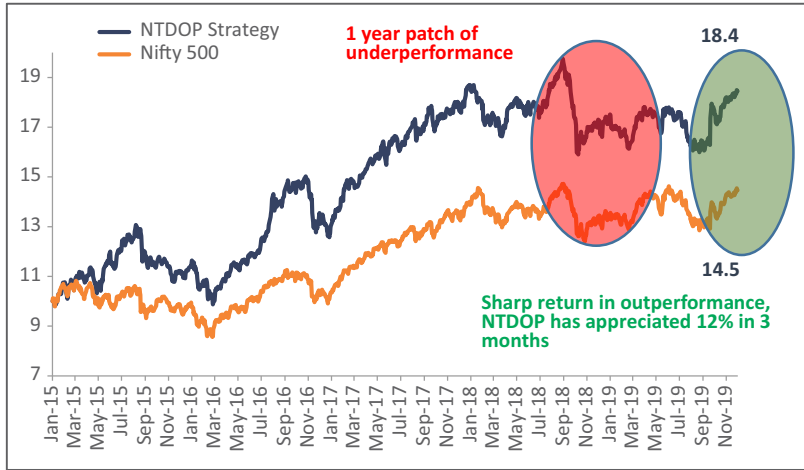
NTDOP (Since Inception)



Data as on 30.11.2019

Rs. 1 cr invested in NTDOP Strategy on 1st Jan 2015 is worth Rs. 1.84 cr as on 30th November 2019. For the same period Rs. 1 cr invested in Nifty 500 Index is now worth Rs. 1.45 cr.

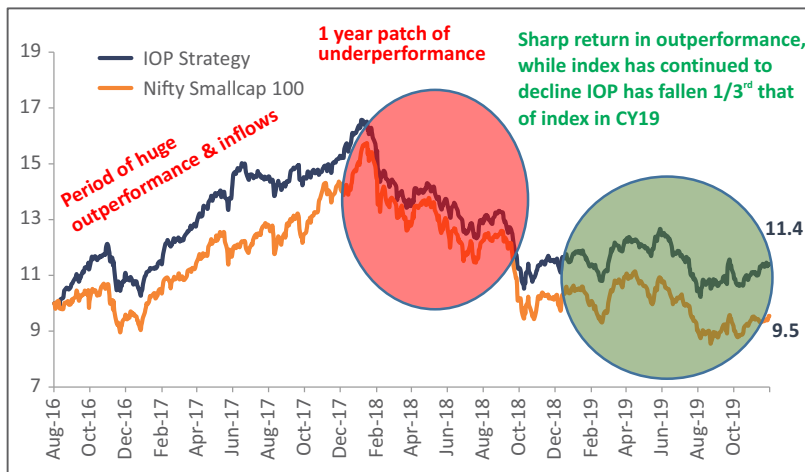
NTDOP (Since Jan 2015)



Data as on 30.11.2019

Rs. 1 cr invested in IOP Strategy on 1st Aug 2016 is worth Rs. 1.14 cr as on 30th November 2019. For the same period Rs. 1 cr invested in Nifty Smallcap 100 Index is now worth Rs. 95 lakhs.

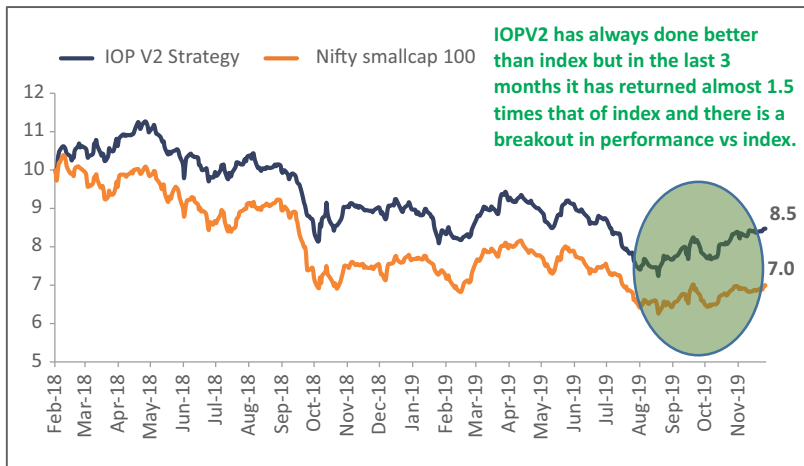
IOP (Since Aug 2016)



Data as on 30.11.2019

Rs. 1 cr invested in IOP V2 Strategy at inception (5th Feb 2018) is worth Rs. 85 lakhs as on 30th November 2019. For the same period Rs. 1 cr invested in Nifty Smallcap 100 Index is now worth Rs. 70 lakhs.

IOP V2 (Since Inception)



Data as on 30.11.2019

In closing, I would humbly urge, remain invested and don't dig to see the progress of the seed. And if you believe in being an astute investor who picks opportunities and doesn't indulge in rear-view mirror driving, you may invest further in your mid and small cap portfolios now.

Lastly, many investors and commentators are worried about prospects of economic growth. In my understanding these are times when one has to think away from the crowd and counter-cyclically. Legendary investor Howard Marks in his latest book has an interesting quote: "When economic growth is slow or negative and markets are weak, most people worry about the losing money and disregard the risk of missing opportunities."

Yours Sincerely,



Aashish P. Somaiyaa
(MD & CEO – Motilal Oswal AMC)

Value Strategy

Investment 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. Value is a large cap* oriented strategy where investments are made with long term perspective with industry leaders.

*The selection of the stocks will be based on the criteria of strategy at the time of initial ideation and investment made as per the model portfolio of the strategy

Details

Fund Manager : Shrey Loonker
 Co-Fund Manager : Susmit Patodia
 Strategy Type : Open ended
 Date of Inception : 24th March 2003
 Benchmark : Nifty 50 Index
 Investment Horizon : 3 Years +

Market Capitalization

Market Capitalization	% Equity
Large cap	74.7
Mid cap	20.5
Small cap	2.4

Top 10 Holdings

Particulars	% Allocation
HDFC Bank Ltd.	12.3
HDFC Life Insurance Company Ltd.	10.2
ICICI Bank Ltd.	8.8
Kotak Mahindra Bank Ltd.	6.7
Bajaj Finserv Ltd.	6.6
Max Financial Services Ltd.	5.5
Larsen & Toubro Ltd.	5.0
Maruti Suzuki India Ltd.	4.8
Bharat Petroleum Corporation Ltd.	4.7
Ipca Laboratories Ltd.	4.4

Data as on 30th November 2019

Top Sectors

Sector Allocation	% Allocation*
Banking	34.0
Insurance	22.2
Auto & Auto Ancillaries	14.1
Pharmaceuticals	8.5
Oil & Gas	8.0
Engineering & Electricals	7.4
Cash	2.4

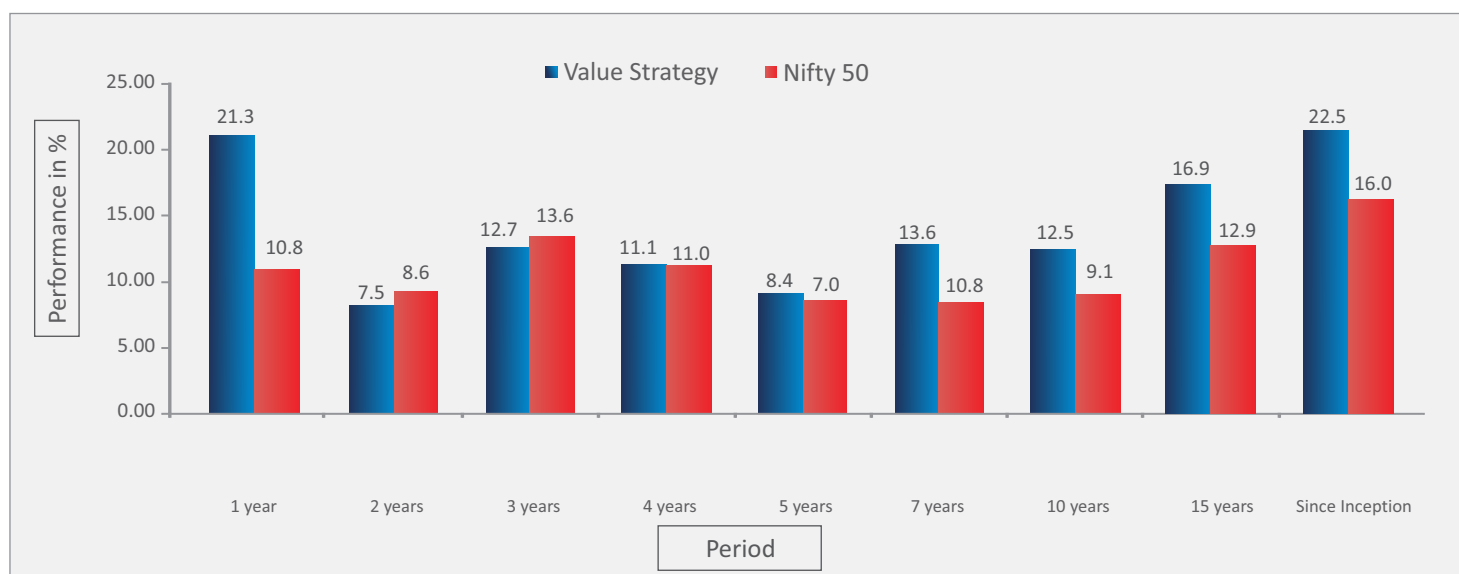
Data as on 30th November 2019

*Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	Value Strategy	Nifty 50
Standard Deviation (%)	20.2%	22.1%
Beta	0.8	1.0

Data as on 30th November 2019



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 30th November 2019. 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

Investment 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 of GDP growth. Focus is on businesses benefitting from growth in GDP.

*The selection of the stocks will be based on the criteria of strategy at the time of initial ideation and investment made as per the model portfolio of the strategy

Details

Fund Manager : Manish Sonthalia
 Strategy Type : Open ended
 Date of Inception : 05th December 2007
 Benchmark : Nifty 500
 Investment Horizon : 3 Years +

Market Capitalization

Market Capitalization	% Equity
Large cap	46.5
Mid cap	50.7
Small cap	2.7

Top 10 Holdings

Particulars	% Allocation
Kotak Mahindra Bank Ltd.	13.5
Voltas Ltd.	10.7
Page Industries Ltd.	7.8
ICICI Bank Ltd.	6.6
City Union Bank Ltd.	5.2
Eicher Motors Ltd.	4.9
Max Financial Services Ltd.	4.3
L&T Technology Services Ltd.	4.0
Ipca Laboratories Ltd.	3.7
Tech Mahindra Ltd.	3.6

Data as on 30th November 2019

Top Sectors

Sector Allocation	% Allocation*
Banking	27.6
FMCG	15.6
Auto & Auto Ancillaries	11.1
Consumer Discretionary	10.7
Infotech	7.6
Pharmaceuticals	6.0
Cash	0.1

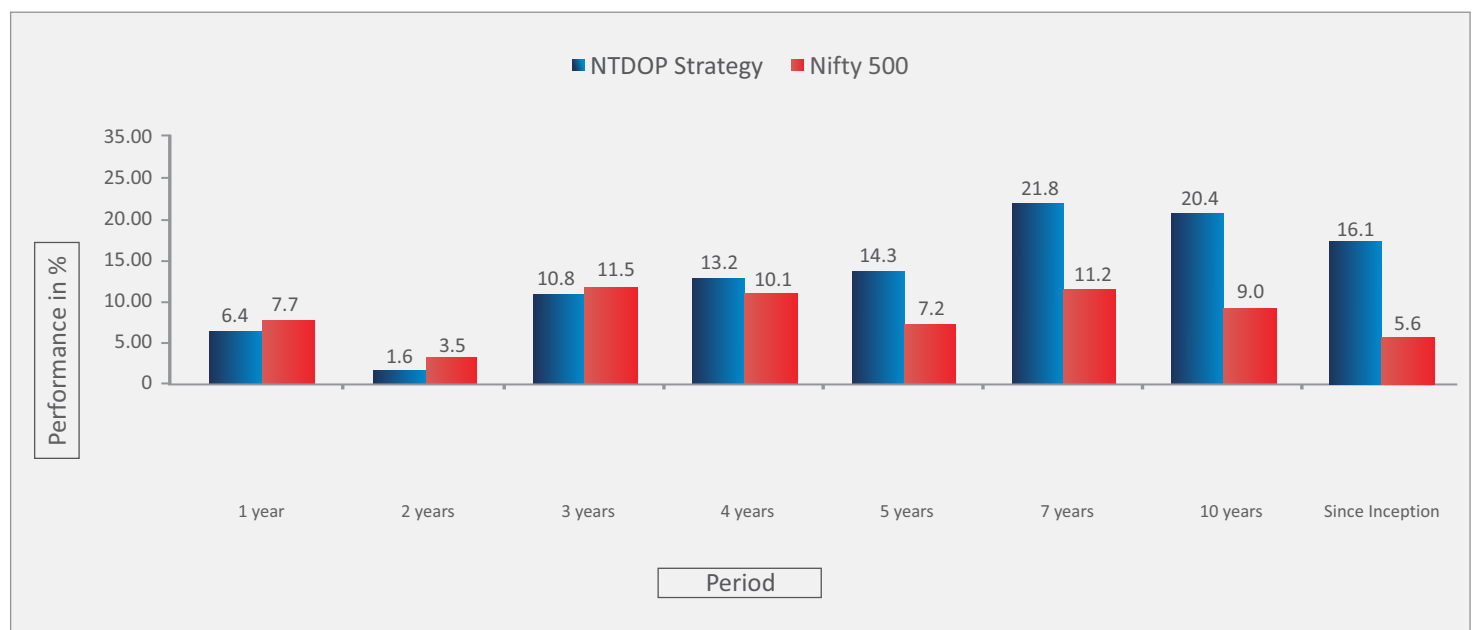
Data as on 30th November 2019

*Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	NTDOP	Nifty 500
Standard Deviation (%)	17.6%	20.8%
Beta	0.7	1.0

Data as on 30th November 2019



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India Opportunity Portfolio Strategy

Investment 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. The strategy is for investors who are keen to generate wealth by participating in India's growth story over a period of time.

The selection of the stocks will be based on the criteria of strategy at the time of initial ideation and investment made as per the model portfolio of the strategy

Details

Fund Manager : Mr. Manish Sonthalia
 Associate Fund Manager : Mr. Atul Mehra
 Strategy Type : Open ended
 Date of Inception : 11th Feb. 2010
 Benchmark : Nifty Smallcap 100
 Investment Horizon : 3 Years +

Market Capitalization

Market Capitalization	% Equity
Large cap	7.4
Mid cap	30.7
Small cap	61.4

Top 10 Holdings

Particulars	% Allocation
Development Credit Bank Ltd.	10.2
ICICI Securities Ltd.	9.3
Birla Corporation Ltd.	7.9
Aegis Logistics Ltd.	6.8
Mahanagar Gas Ltd.	6.7
TTK Prestige Ltd.	6.6
Dr. Lal Pathlabs Ltd.	6.1
Alkem Laboratories Ltd.	5.9
Blue Star Ltd.	5.9
ICICI Bank Ltd.	5.6

Data as on 30th November 2019

Top Sectors

Sector Allocation	% Allocation*
Banking	15.8
Oil and Gas	13.5
Consumer Durable	11.9
Cement & Infrastructure	9.5
Capital Markets	9.4
Pharmaceuticals	8.3
Engineering & Electricals	7.5
NBFC	6.4
Healthcare Services	6.1
Cash	0.4

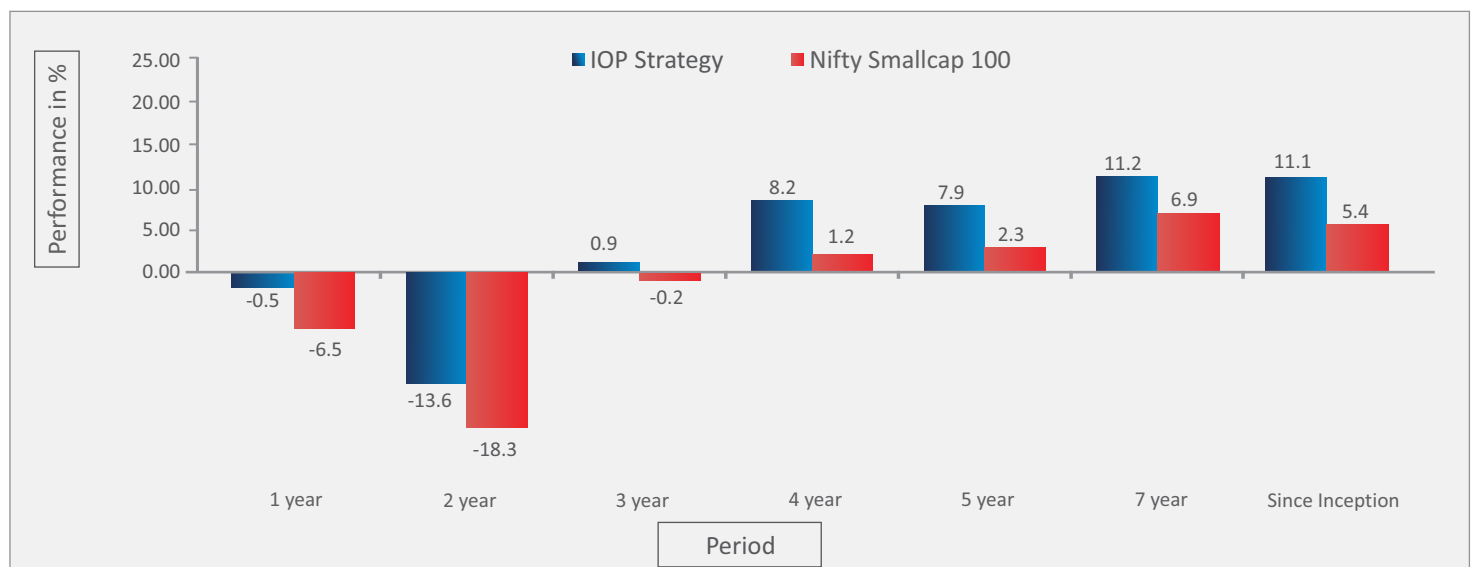
Data as on 30th November 2019

*Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	IOPS	Nifty Smallcap 100
Standard Deviation (%)	15.5%	19.6%
Beta	0.6	1.0

Data as on 30th November 2019



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India Opportunity Portfolio V2 Strategy

Investment Objective

The Strategy aims to deliver superior returns by investing in stocks from sectors that can benefit from India's emerging businesses. It aims to predominantly invest in Small and Midcap stocks* with a focus on identifying potential winners. Focus on Sectors and Companies which promise a higher than average growth.

*The selection of the stocks will be based on the criteria of strategy at the time of initial ideation and investment made as per the model portfolio of the strategy

Details

Fund Manager	: Mr. Manish Sonthalia
Associate Fund Manager	: Mr. Atul Mehra
Strategy Type	: Open ended
Date of Inception	: 5th Feb. 2018
Benchmark	: Nifty Smallcap 100
Investment Horizon	: 3 Years +

Market Capitalization

Market Capitalization	% Equity
Large cap	16.3
Mid cap	31.8
Small cap	50.9

Top 10 Holdings

Particulars	% Allocation
Cholamandalam Investment & Finance Company Ltd.	9.6
Reliance Industries Ltd.	9.0
Larsen & Toubro Infotech Ltd.	7.3
Godrej Agrovet Ltd.	7.0
Ipca Laboratories Ltd.	5.8
Avanti Feeds Ltd.	5.4
Sobha Ltd.	5.2
JK Lakshmi Cement Ltd.	5.1
Bata India Ltd.	4.9
KEI Industries Ltd.	4.8

Data as on 30th November 2019

Top Sectors

Sector Allocation	% Allocation*
Electricals & Electronics	12.5
Agriculture	12.4
Capital Markets	11.9
NBFC	9.6
Oil and Gas	9.0
Infotech	8.9
Pharmaceuticals	6.9
Real Estate	5.2
Cement	5.1
Cash	1.0

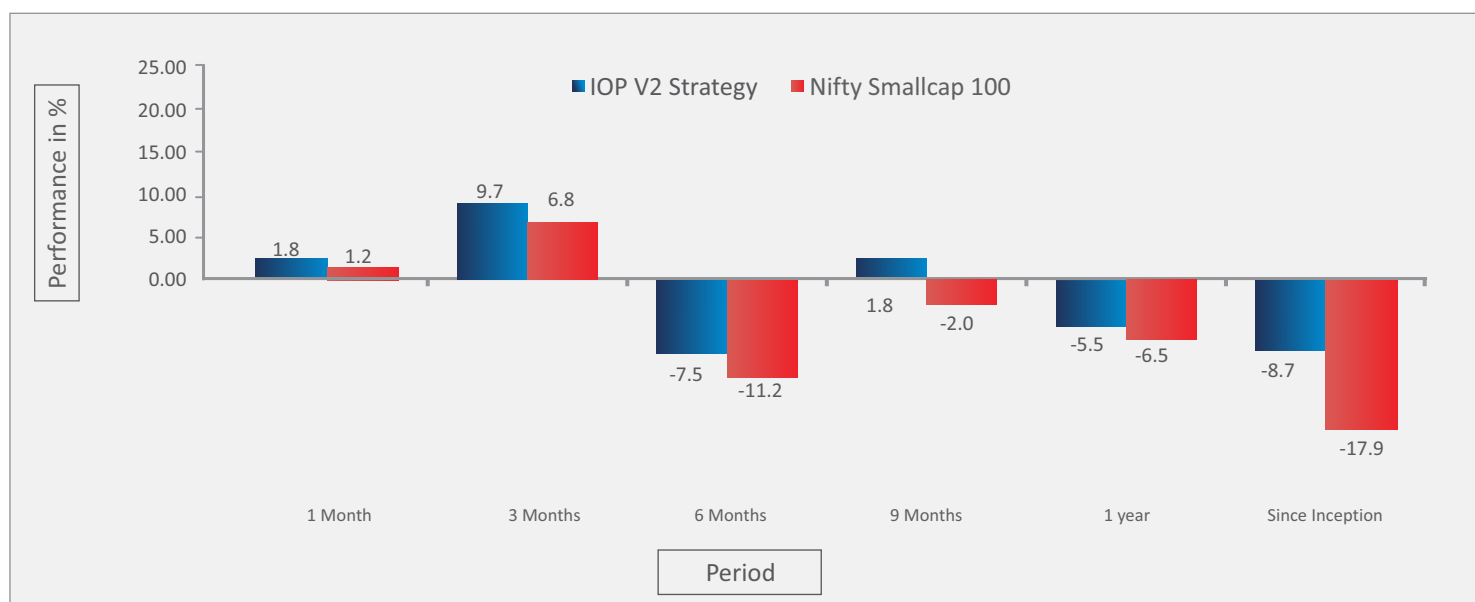
Data as on 30th November 2019

*Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	IOP V2	Nifty Smallcap 100
Standard Deviation (%)	17.8%	19.4%
Beta	0.8	1.0

Data as on 30th November 2019



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Business Opportunities Strategy

Investment Objective

The investment objective of the Strategy is to achieve long term capital appreciation by primarily investing in equity & equity related across market capitalization. It aims to predominantly invest in emerging themes with focus on themes like affordable housing, agricultural growth, GST and value migration from PSU banks to Private Sector Banks.

The selection of the stocks will be based on the criteria of strategy at the time of initial ideation and investment made as per the model portfolio of the strategy

Details

Fund Manager	: Mr. Manish Sonthalia
Strategy Type	: Open ended
Date of Inception	: 16th Jan. 2018
Benchmark	: Nifty 500
Investment Horizon	: 3 Years +

Market Capitalization

Market Capitalization	% Equity
Large cap	60.3
Mid cap	26.9
Small cap	12.5

Top 10 Holdings

Particulars	% Allocation
Hindustan Unilever Ltd.	9.1
Bata India Ltd.	8.0
HDFC Bank Ltd.	6.7
Kotak Mahindra Bank Ltd.	5.4
ICICI Bank Ltd.	5.0
Bajaj Finance Ltd.	4.9
Blue Star Ltd.	4.8
Container Corporation Of India Ltd.	4.6
Godrej Agrovet Ltd.	4.5
Kansai Nerolac Paints Ltd.	4.4

Data as on 30th November 2019

Top Sectors

Sector Allocation	% Allocation*
FMCG	22.8
Banks	17.1
Retail	14.3
Agriculture	7.3
Insurance	6.6
Construction	5.8
Engineering & Electricals	5.4
Cash	0.2

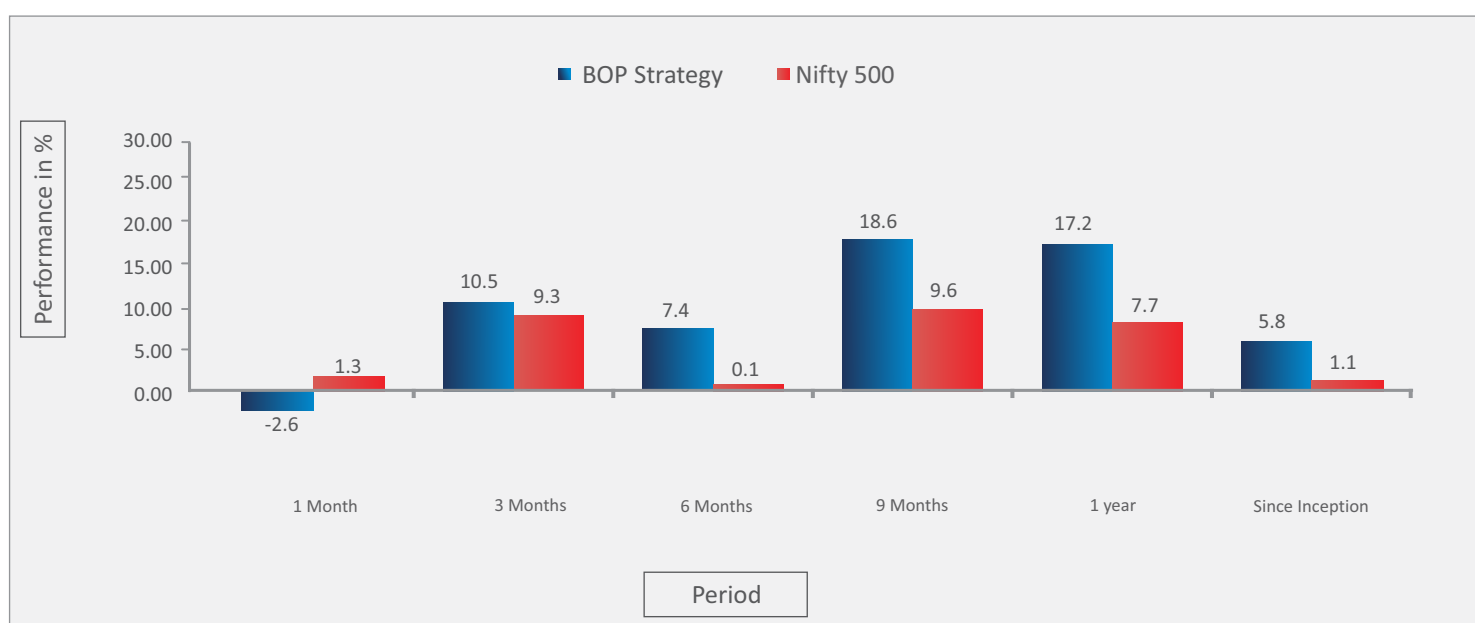
Data as on 30th November 2019

*Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	BOP	Nifty 500
Standard Deviation (%)	14.3%	13.6%
Beta	0.9	1.0

Data as on 30th November 2019



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