MONTHLY Communique

August 2019

Aashish P Somaiyaa
(MD & CEO)

Dear Investors and my dear advisor friends,

In meetings with investors, private bankers and advisors over last few days, it is often quoted we are apprehensive on our existing equity positions and unsure of further investments despite an unexpectedly strong election mandate because:

1. Nifty has run up to all time high
2. Nifty PE is high
3. Earnings growth is not coming through
4. Everyone is expecting and hence awaiting a correction in the "markets". (We will revisit later why I chose to quote unquote the word markets!)

But let me tell you, the current scenario and the reaction of investors to this scenario is a very unique case of cognitive bias i.e. using mental shortcuts (heuristics) that the brain uses to make decisions or to make judgements. The specific biases here are related to "anchoring" and there is an interesting one I read while researching for this article. It's called "surrogation" i.e. losing sight of the strategic construct that a measure is intended to represent; and subsequently acting as though the measure itself is the construct of our main interest". Let me explain: the Nifty, Nifty PE, Nifty EPS are supposed to serve as guidance or a convenient tracker for the "markets" but they are not THE market; especially when we know what we own in our portfolios.

Coming back to the above observations, what I have written in point nos 1-4 is correct about Nifty and that's what makes everyone circumspect about investing.

But what is the other issue with investors that they are unhappy about currently?

1. They have underperformed the Nifty in the last one year
2. They don't own Nifty, more specifically the top stocks of Nifty which have done well; their portfolios have high midcap exposure and maybe small caps too
3. Their portfolios are nowhere near all-time highs although the Nifty is

Can we reconcile both of these things and understand where investors and advisors are in their thinking and why they are probably wrong in drawing sharp conclusions about the "markets' and market levels...

Let's recap some facts. The portfolios we run at Motilal Oswal AMC...

1. ...are small, mid or multicap or a mix (we actually don't have any pure large cap funds and surely we have nothing tracking the Nifty). In fact our portfolios have always been holding 60-70% active positions (away from underlying benchmark index) and this is what explained the significant outperformance from 2014 till October 2017 and this is what explains the underperformance from October 2017 till October 2018.

2. ...still have double digit (15-20%) year on year EPS growth at portfolio level (every portfolio at any time will have one or two stocks where the hypothesis hasn't played out as per plan but aggregate level portfolio holdings do stack up on these numbers)

(Continued overleaf)

3. ...they have corrected vis-à-vis index (meaning index has gone up but portfolios haven't) and they have corrected on absolute basis (meaning small and midcap may be 8-10% down on a one year basis and may have practically NIL returns on a 2 year basis.)

4. ...our portfolios have already started to beat the index convincingly post October 2018 – whether Nifty will correct or our portfolios will go up? Both will be called "correction", which "correction" are investors waiting for or staying away from fear of?

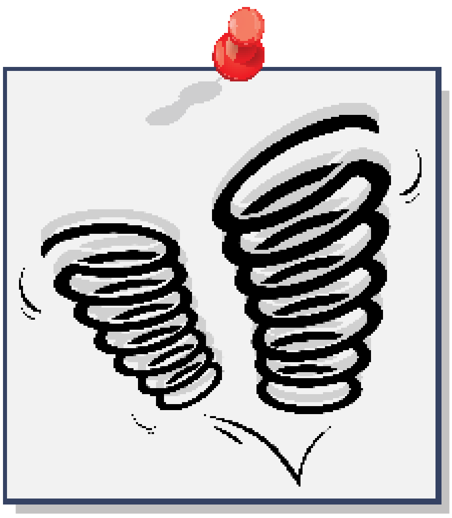
While most of 2019 has seen everyone pre-occupied with elections, not only has the election mandate been a huge positive surprise as a vote for continuity, in the background US policy, RBI policy, banks NPA accretion, oil prices – everything has changed. The RBI has announced yet another rate cut and changed the policy stance to "accommodative". The Government may cut GST rates, announce growth stimulus initiatives and with easing conditions and election out of the way the cyclical factors will be behind us and demand will come back.

I hope that all of us who are waiting for a "correction" realise that we are exhibiting "anchoring" or "surrogation" to Nifty while broad market has shown earnings growth (depends what you own), has corrected and is nowhere near all-time high.

Talking of heuristics and short cuts for the brains to make quick inferences; I would like to present a few of my own observations and I dare call them inventions. I have seen that time and again; investors are long term investors while signing up, but if returns turn negative the long term goes out of the window. What causes this kind of reaction? Its obvious that as an investor (even I am one) none of us want to see a negative in our portfolio because negative returns gives us a feeling of having lost and that's disappointing, a huge let down on our expectations.

Let me take a simple example. If someone has invested Rs. 100/- and the value is down to Rs. 80/- they are 20% down. The feeling is that of having lost 20% and the fear is that it will never come back. This is akin to visualizing that there are say 5 physical objections that one owns, and 1 out of these 5 is lost so its 20% gone and that 20% will never come back. Further, there are some arithmetically astute people who scare investors throwing about numbers like; if 100 becomes 80, its 20% down but for 80 to become 100 now you need 25% up! How will this happen?

This is where the right visualization is crucial. If you own an equity portfolio with underlying companies that are producing profits the correct visualisation is that of a spring.



If a spring is compressed 20%, it stores more energy than before. If a stock price declines even as it produces earnings, it becomes more valuable. Even as companies continue to produce profits, there is a limit to how much the spring can be compressed. Now let's say a spring is compressed 20% and then its released! How much will it recoil? 20% from the 80 or 25% from the 80 to come back to original length of 100? Of course this logic doesn't work if you own a portfolio full of junk, but that's not the case with us. The key message to remember is that equity is not a linear asset class, its an exponential asset class. The numbers don't follow linear progression, they follow geometric progression.

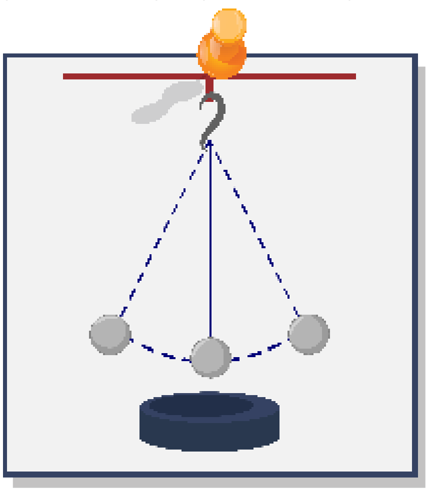
The other observation I have made in recent times is that equity mutual funds as an aggregate were witnessing inflows in right through 2017 and 2018 and now as we head into mid 2019, flows are not only slowing down but on the margins data shows some funds are witnessing outflows. How does this reflect upon us if as an aggregate we were buyers in 2017-18 and now we are sellers? Why does this happen? That's because there was lot of enthusiasm to invest back then but in Sep-Oct 2018 and then again in Feb 2019, we saw huge marked-to-market or I dare call them notional losses in portfolios. And from March through to May at least in case of large cap and multicap funds these values are now being restored. In my reading, as I said before, everyone is a long term investor when they sign up, but the first sign of negative returns results in the long term being forgotten. When 100 becomes 80 or 90 its bad, but when the 80 inches up slowly to 90-95 and 100 and capital is restored, the first instinct is to take the capital and bolt! Now, the correct visualisation for this situation is, imagine you are in an elevator looking to get up to the 20th storey of a building. As soon as you enter the elevator, you note that it was actually headed down from the ground floor where you entered so instead of taking you straight to the 20th storey, it makes a detour and takes you to Basement Level2 first. Unfortunately just as you hit B2, there's a power outage and you are stuck in the elevator for 20 mins.

Now, food for thought: after 20 mins if the power comes back and you find yourself at B1 or G, how many of you will rush out the moment the doors open and how many of you will calmly stand back and say, cool, I am headed to the 20th. Chances are, everyone will make a dash for the door and mind that 20th storey business some other day. Maybe that's the right response if you are stuck in an elevator unexpectedly, but no, that's not the right response if you are investing in equities. If you invest in equities and someone told you that you could double your money in 5-6 years, unfortunately which 2 years will be bad, which two years will be above average and which 2 years will make you a great deal of money is not easily predictable. So if you bolt out the moment the elevator door opens, let me tell you, you've lived the worst part and decided to bail out exactly before the good part starts playing out.

Similar analogy I remember from my early days working in Mumbai. I live in the Mumbai suburb of Goregaon and I had to be in Churchgate before 9 am each morning.

Taking a train from Goregaon headed to Churchgate meant that the train would be coming from Borivali and lesser mortals from Goregaon had to stand or probably even hang outside. And if the train was a fast one coming from Virar, you'd be looking to get a foot in the door at best. Eventually I realised that if I went 20 mins early, and from Goregaon I took a train in the opposite direction that train, I'd get to sit by the window, the train would end up in Borivali and eventually return back to Churchgate! Voila! In equities, it's not always possible to time the entry. Sometimes the market makes you take a detour. If you try to time the entry chances are, you won't catch the bottom. And if you don't catch the bottom, i.e. you try to get a fast train from Goregaon, chances are you won't get a foot in the door.

Moving on, as I said in my opening comments, one of the observations is that a lot of investors haven't done as well as the index in the last one year to 18 months specifically. This is because of having portfolios that are at huge divergence from Nifty or having portfolios anyway with a fair sprinkling of small and midcaps. I am reminded of...



Over a long period like 15-20 years, the Nifty MidCap 100 has delivered average 4% over and above the Nifty50 for any one year holding period. Currently, at the time of writing this newsletter, I can see that for the last one year the NiftyMidCap 100 has delivered, forget +4%, it's.. (-16%) as compared to Nifty50. So what's with the pendulum? Imagine a pendulum swinging, where the midpoint is +4 and currently the pendulum is at position of -16, what would you expect the pendulum to do? Maybe swing further away a little bit? But eventually? Well, either the Nifty50 corrects downwards or the NiftyMidCap100 corrects upward, the key is that both will be called "correction". Where would you like to be on the pendulum? You are better off with your small and midcap portfolios.

And lastly, like I wrote in one of my recent articles, don't be a "wiper". https://www.motilaloswalmf.com/blogs/ceo/what-windscreen-wipers-teach-you-about-investing-behaviour/119 There's no point in rushing into large caps because large caps did well last year and theres no point in buying index now because index did better than your mutual funds or PMS last year. If you want to shoot a rabbit, you got to shoot where the rabbit will be, not where the rabbit is or was.

To sum up, do not form impressions on how your portfolios are doing and when markets should correct by seeing the Nifty50. And if you have not done what Nifty50 has done in the past one or two years, all the more reason not to worry or wait for correction. Your portfolios have already "corrected" and a good investing experience awaits us over the next one to two years.

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	79.2
Mid cap	17.5
Small cap	-

Top 10 Holdings

Particulars	% Allocation
HDFC Bank Ltd.	12.51
HDFC Standard Life Insurance Company Ltd.	10.18
ICICI Bank Ltd.	7.36
Kotak Mahindra Bank Ltd.	7.28
Bharat Petroleum Corpn Ltd.	6.04
Larsen & Toubro Ltd.	5.98
Bajaj Finserv Ltd.	5.89
Ipca Laboratories Ltd.	4.24
Maruti Suzuki India Ltd.	4.19
Bharat Forge Ltd.	3.84

Data as on 31st July 2019

Top Sectors

Sector Allocation	% Allocation*
Banking & Finance	53.69
Auto & Auto Ancillaries	11.55
Oil & Gas	9.31
Pharmaceuticals	7.53
Engineering & Electricals	5.98
Cash	3.31

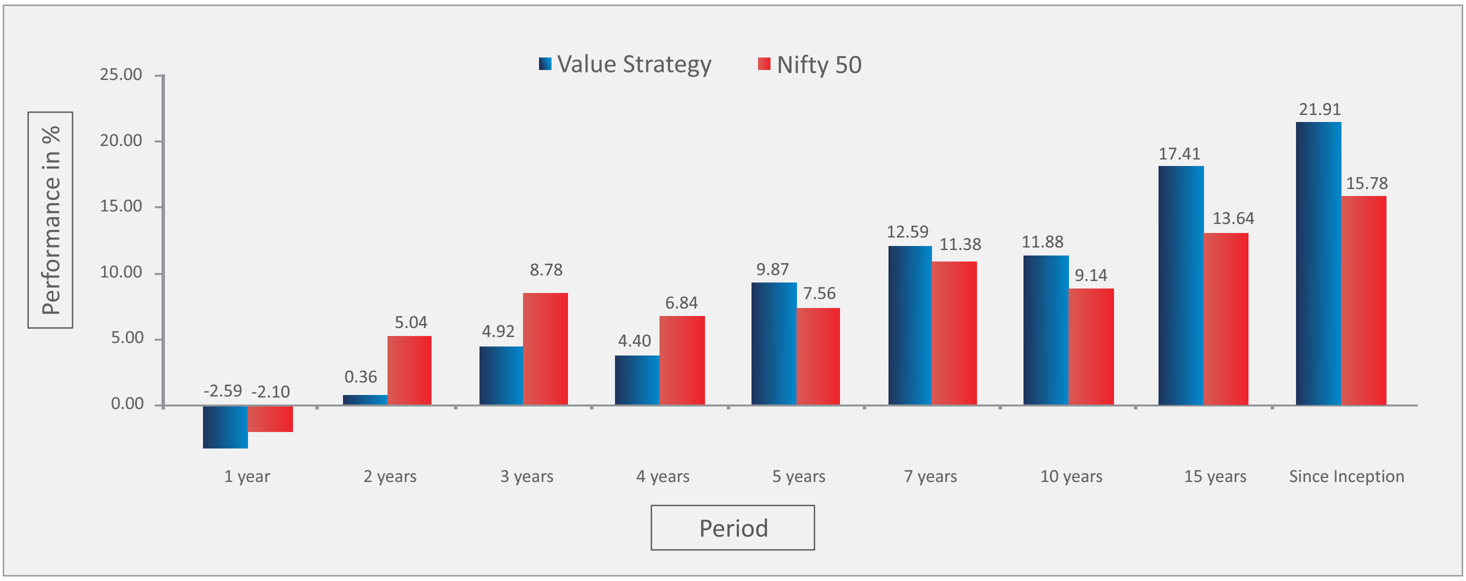
Data as on 31st July 2019

*Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	Value Strategy	Nifty 50
Standard Deviation (%)	20.23%	22.24%
Beta	0.82	1.00

Data as on 31st July 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 31st July 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	45.5
Mid cap	51.0
Small cap	3.4

Top 10 Holdings

Particulars	% Allocation
Kotak Mahindra Bank Ltd.	14.09
Voltas Ltd.	9.97
Page Industries Ltd.	7.27
City Union Bank Ltd.	5.03
ICICI Bank Ltd.	4.62
Bajaj Finance Ltd.	4.51
L&T Technology Services Ltd.	4.35
Max Financial Services Ltd.	3.95
Eicher Motors Ltd.	3.93
Godrej Industries Ltd.	3.49

Data as on 31st July 2019

Top Sectors

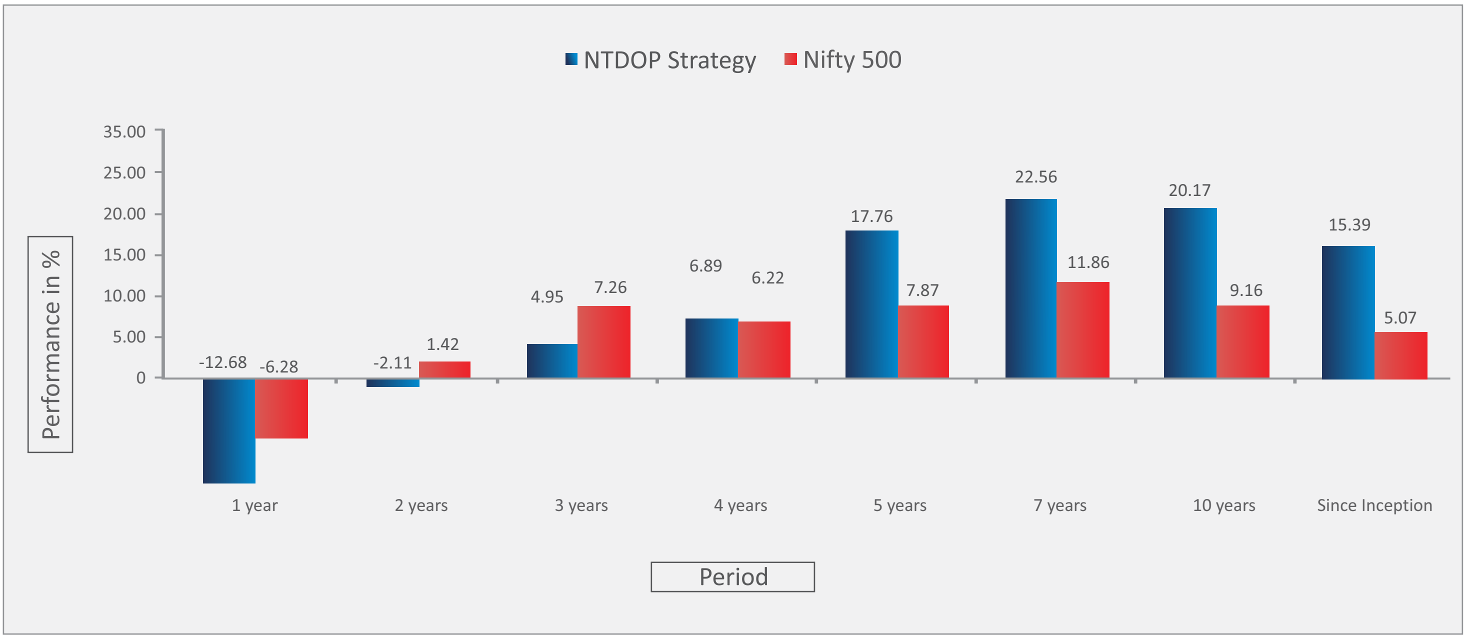
Sector Allocation	% Allocation*
Banking & Finance	35.41
FMCG	14.86
Diversified	13.46
Auto & Auto Ancillaries	10.26
Infotech	7.72
Pharmaceuticals	5.67
Oil and Gas	5.13
Cash	0.03

Data as on 31st July 2019 *Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	NTDOP	Nifty 500
Standard Deviation (%)	17.58%	20.91%
Beta	0.70	1.00

Data as on 31st July 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

Top 10 Holdings

Particulars	% Allocation
Development Credit Bank Ltd.	11.80
AU Small Finance Bank Ltd.	7.90
Birla Corporation Ltd.	7.56
Aegis Logistics Ltd.	6.99
TTK Prestige Ltd.	6.63
Can Fin Homes Ltd.	5.82
Mahanagar Gas Ltd.	5.60
Alkem Laboratories Ltd.	5.46
Blue Star Ltd.	5.44
Dr. Lal Pathlabs Ltd.	5.08

Data as on 31st July 2019

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 +

Top Sectors

Sector Allocation	% Allocation*
Banking & Finance	28.65
Pharmaceuticals	14.70
Oil & Gas	12.67
Consumer Durable	11.75
Cement & Infrastructure	9.67
Engineering & Electricals	5.48
Cash	0.03

Data as on 31st July 2019 *Above 5% & Cash

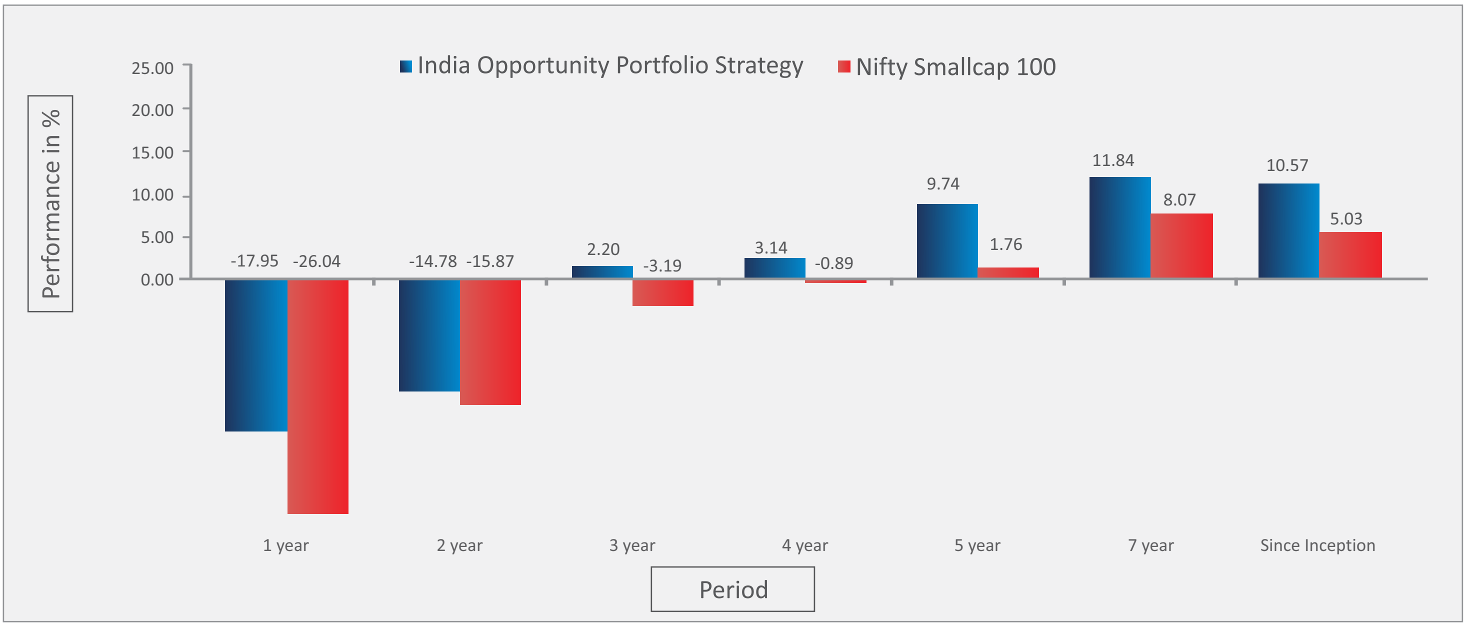
Market Capitalization

Market Capitalization	% Equity
Large cap	1.7
Mid cap	36.0
Small cap	61.6

Key Portfolio Analysis

Performance Data (Since Inception)	IOPS	Nifty Smallcap 100
Standard Deviation (%)	15.36%	19.63%
Beta	0.58	1.00

Data as on 31st July 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	7.3
Mid cap	38.7
Small cap	54.0

Top 10 Holdings

Particulars	% Allocation
Ipca Laboratories Ltd.	10.75
Cholamandalam Investment & Finance Company Ltd.	8.88
Sobha Ltd.	7.87
Bata India Ltd.	7.55
Larsen & Toubro Infotech Ltd.	7.28
Godrej Agrovet Ltd.	6.81
JK Lakshmi Cement Ltd.	6.48
Bajaj Electricals Ltd.	5.42
Sundram Fasteners Ltd.	4.69
KEI Industries Ltd.	4.48

Data as on 31st July 2019

Top Sectors

Sector Allocation	% Allocation*
Banking & Finance	16.12
Electricals & Electronics	13.00
Pharmaceuticals	11.73
Agriculture	10.43
Infotech	8.74
Real Estate	7.87
Retail	7.55
Cement	6.48
Cash	0.03

Data as on 31st July 2019 *Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	IOP V2	Nifty Smallcap 100
Standard Deviation (%)	17.65%	19.62%
Beta	0.75	1.00

Data as on 31st July 2019

Performance

Period	IOP V2	Nifty Smallcap 100
1 Months	-13.20	-10.94
3 Months	-15.74	-14.63
6 Months	-8.91	-9.97
9 Months	-14.18	-8.92
1 Year	-25.79	-26.04
Since Inception (5th Feb 2018)	-16.95	-24.13

Data as on 31st July 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	59.1
Mid cap	26.2
Small cap	14.7

Top 10 Holdings

Particulars	% Allocation
Hindustan Unilever Ltd.	8.95
Bajaj Finance Ltd.	7.96
ICICI Lombard General Insurance Company Ltd.	7.50
Bata India Ltd.	7.42
HDFC Bank Ltd.	7.16
Kotak Mahindra Bank Ltd.	5.88
Titan Company Ltd.	4.91
Blue Star Ltd.	4.80
Container Corporation Of India Ltd.	4.68
Godrej Agrovet Ltd.	4.55

Data as on 31st July 2019

Top Sectors

Sector Allocation	% Allocation*
Banking & Finance	35.09
FMCG	18.19
Retail	14.51
Agriculture	6.52
Engineering & Electricals	5.66
Construction	5.28
Cash	0.03

Data as on 31st July 2019 *Above 5% & Cash

Key Portfolio Analysis

Performance Data (Since Inception)	BOP	Nifty 500
Standard Deviation (%)	13.35%	12.95%
Beta	0.87	1.00

Data as on 31st July 2019

Performance

Period	BOP	Nifty 500
1 Months	-7.27	-6.35
3 Months	-3.54	-6.41
6 Months	1.99	0.46
9 Months	7.69	3.33
1 Year	-6.43	-6.28
Since Inception (16th Jan 2018)	-2.65	-3.88

Data as on 31st July 2019

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Risk Disclosure And Disclaimer

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or write to pmsquery@motilaloswal.com or visit www.motilaloswalmf.com