QUEST PMS PORTFOLIO UPDATE – NOV 2020

QUEST INVESTMENT ADVISORS
SEBI Registered PMS & AIF managers

Dear Investor,

Hope my letter finds you in the highest of spirits and best of health as we bid adieu to a memorable year for all of us. Would want to take this opportunity to thank all our investors who have entrusted their wealth creation journey with us and have trusted us for delivering on the said goals and stood by us during this trying year. We began this year with a promise to ourselves and our investors that we would emerge stronger post the upheaval and we are glad we have been able to deliver on the same as the year comes to an end.

"In the end we only regret the chances we didn't take, the relationships we were afraid to have, and the decisions we waited too long to make"- Lewis Carroll

From our interactions with most participants in the market we realised that **the biggest regret of 2020 for most is that they froze in their decision making during the months of March-April 2020** and thereafter fear gripped them and they failed to act rationally. Though this was not the first time they were seeing a crash and they knew that sooner or later markets would rebound, but the shear scale of fear spread globally during pandemic took the better of the decision making. However since those initial months, **we have been again and again asking our clients to not let this opportunity go and keep deploying fresh allocations into equity** as per their comfort level without waiting for the next big fall. Even deployments done in last two months have yielded double digit mid teen returns in the market. As we have a couple of weeks left in this year, we are happy that we have been able to build confidence in our investors for their portfolios managed by us. Below is a summary of performance of the strategies as of Nov end:

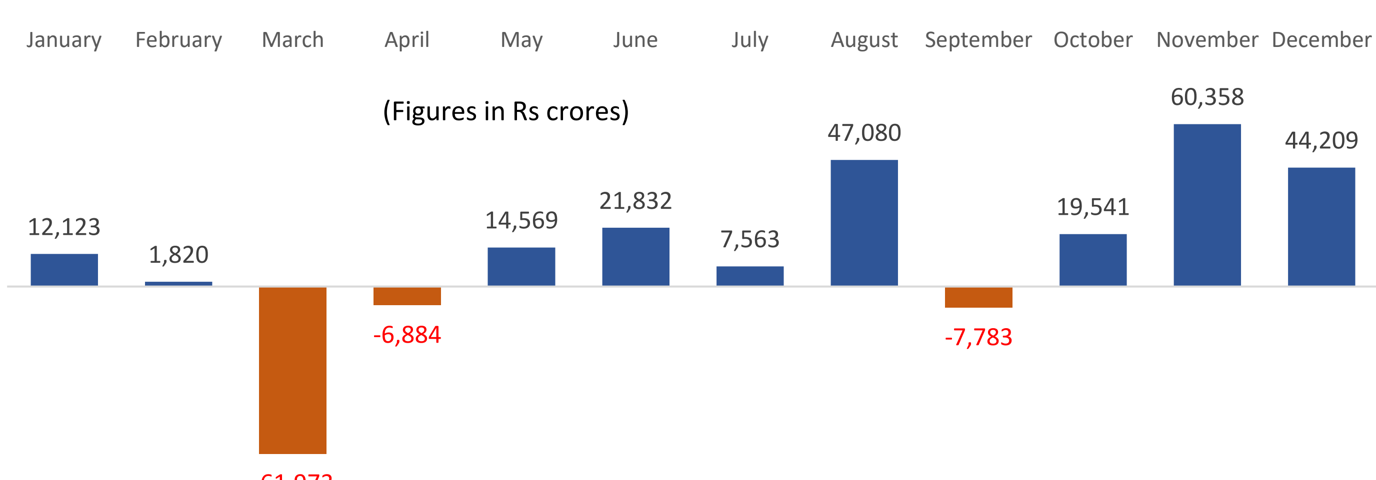
As on 30th Nov 2020	1 month	3 months	6 months	1 year	2 years	5 years	Since Inception
Quest Flagship PMS	12.7%	15.3%	40.1%	17.7%	9.5%	9.9%	16.1%
NIFTY-50	11.4%	13.9%	35.4%	7.6%	9.2%	10.3%	6.8%
NIFTY – 500	11.9%	14.4%	37.0%	9.2%	8.5%	9.9%	6.9%
Quest Multi PMS	11.3%	14.2%	49.0%	21.6%	11.1%	10.6%	13.0%
NIFTY-50	11.4%	13.9%	35.4%	7.6%	9.2%	10.3%	8.6%
NIFTY – 500	11.9%	14.4%	37.0%	9.2%	8.5%	9.9%	9.1%
Quest Focus PMS	13.8%	14.6%	35.1%	6.7%	3.5%	-	10.8%
NIFTY-50	11.4%	13.9%	35.4%	7.6%	9.2%	10.3%	12.1%
NIFTY – 500	11.9%	14.4%	37.0%	9.2%	8.5%	9.9%	11.7%

Note: These are TWRR returns as on 30th Nov'20 of all clients taken together of the individual schemes and individual client performance can be higher or lower than this depending on their joining dates and corpus in dates.

Liquidity train driving straight ahead into Emerging Markets (EM)

There are no prizes for guessing what this graph below depicts. These are the monthly net inflows from FPI into Indian equities in 2020 so far till 16th of December.

A falling Dollar Index and better than expected recovery in most economies continues to attract fresh flows from FPI



Source: www.nsdl.co.in

Global Fund managers are net 55% overweight on emerging market equities (highest allocation to EM equities since Nov 2010), as per the recent survey done by a global research agency. **This makes EM equities the top preferred investment asset class globally. One of the key factor contributing to the rising popularity of EM equities is a "weak dollar"**. The Dollar Index has been on a declining trend since March'20 falling around 9%, thanks to the trillions of dollar of liquidity infused by the US Fed, ECB and stimulus by the US government. Hopes of a fresh coronavirus aid package by the new US government are likely to keep the USD on a weak footing. This makes EM equities more attractive compared to developed market stocks.

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Valuations are not expensive as they optically seem to be and has enough room for upside

At the same time with **emerging markets being a high-beta play on the global earnings cycle,** and with the global cycle now in an early expansion mode, one could see good earnings growth out of selective emerging markets like India. Also, **MSCI Asia-Ex Japan index is trading at a one a year-forward PE multiple of 16X, much lower than the 21X valuation multiple of the MSCI World index**. So you can say on a relative basis EM equities looks attractive too even after this rally. One big risk with EM equity is the possibility of a gradual withdrawal of the stimulus by central banks as green shoots of economic recovery are emerging. Easy money has driven markets up, and liquidity tightening may well lead to a reversal at some point but then sitting out of the market in the fear of some correction happening at some point is hara-kiri in itself. Also, with improving demand, inflation could make a comeback, especially commodity linked inflation. However **as of now it seems growth is the objective and inflationary concerns can take a back seat.**

So is this rally going to end soon or there is more to it than just liquidity?

For last few months the common question plaguing everyone's mind is should you be trimming your exposure to equity and stay in cash or add up on to equity allocation even now. In this regard I would like to reiterate what we have been saying in the last few months – **trying to time the market is one of the most futile exercise which many a great minds have not been able to do over ages.** Hence it becomes our responsibility as your portfolio managers to **ensure the risk is minimized in the portfolios** when such sharp rallies happen **and also at the same time ensure participation in the market** continues by looking for deep value ideas which provide better risk reward payoffs. In line with this **we have been increasing our allocations to Value segment of the market** more and **reducing our exposure from Growth segment of the market** where we are seeing some amount of excess valuation having crept in. As we have time and again mentioned, we try to balance Value and Growth and at this point of time we are definitely finding decent upside alpha creation ideas in the Value segment of the market.

Now coming back to our original thesis of why we continue to like Indian markets and are not worried for valuations with a longer term time frame is that corporate India is giving us that confidence. The first half of FY21 was an absolute pandemonium with almost every macro and economic number painting a gloomy picture. Surprisingly, **economic recovery has been faster than expected helped by gradual demand recovery, supply chain restoration and higher cost efficiencies**. The pandemic has ensured improved housing affordability in terms of fall in asset prices/discounts being offered and interest rates being low – the only **missing trigger is income confidence** which is still not broad-based. Around a third of capex in India is led by household sector, of which 60-70% (~20% of all investment) is in housing. Hence, an uptick here would certainly help in firing one of the long missing engines of the economy. So, recovery is faster than expected and **there are some clear consumption shifts caused by the pandemic with 'safety and comfort' being primary motives** which are leading to higher vehicles, durables sales and potentially higher housing sales as well.

Corporates have strengthened their balance sheets, improved margins, reduced leverage, improved cash flows; stage set for quality growth in next cycle

India Inc in last couple of years has been in need for a reset and 2020 turned out to be that year. Corporates have used this lockdown to **strengthen their balance sheets, improve their operational efficiencies, improve their margins, reduce leverage and improve cash flows**. Visible expansion in gross margins across India Inc in H1FY21 coupled with better control over production costs to operating overheads have driven ~300-400 bps expansion in EBIDTA margins on an average. With capex on tight leash and lower interest costs, PBT growth has been strong across board. While the entire cost efficiency gain is not permanent, overall costs will still be lower and operating margins are likely to better than the earlier cycle. Clear **improvement in terms of trade is visible which is driving higher Operating Cash Flows** (OCF) growth for most companies. Similar trend seems playing out across smaller businesses with most getting more stringent with their policy on receivable days. **Whenever growth sets in, the quality of earnings is expected to be better**. This makes us more confident for Indian equities outperforming all other asset class in the next 18-24 months based on pure fundamentals.

We continue focusing on our task that we need to deliver the best risk adjusted return for our investors across different market cycles. Balancing risk with return and ensuring minimum drawdowns in a falling market is what would set us apart from the crowd. Looking forward to some exciting times for stock selection and wealth creation ahead. Happy Investing and be safe and stay healthy! Wishing a Merry Christmas to you and your family.

Aniruddha Sarkar
Chief Investment Officer & Portfolio Manager

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