ELIXIR EQUITIES PRIVATE LIMITED

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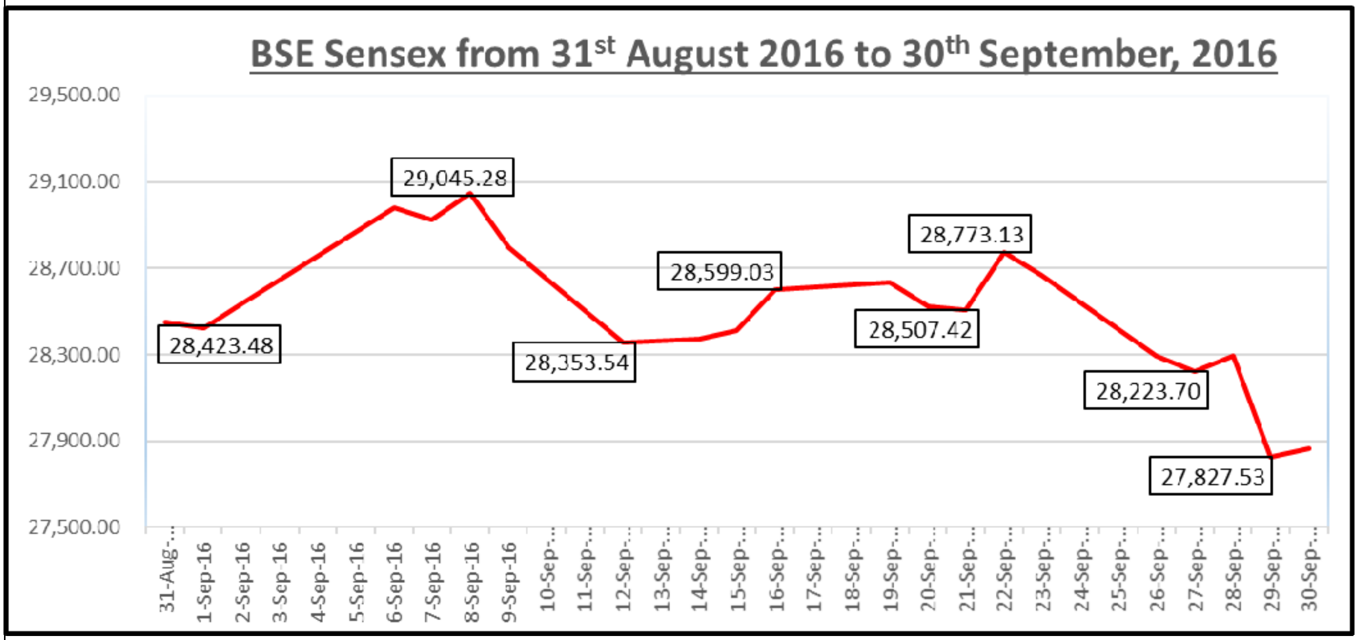
Sideways September Ending in Fireworks



Two months of Sideways Movement

The sideways trends seen in August, spilled over to September with the Sensex declining by 2.06 % to 28,292.81. Had it not been for the 465.28 point drop on the second last day of the month (29-09-2016), when news of surgical operations in PoK hit the markets, the Sensex would have been down by just 0.56%. FII and DII buying remained strong at a positive Rs. 9,336.60 crores and Rs. 1999.22 respectively for the month, with the MF share in DII net purchase at Rs. 1518.10 (up to 27-09-2016) crores.

Financial news flow was scanty during the month with newsworthy events such as the FOMC meet, where US interest rates were left unchanged, were on expected lines. There was progress on the GST front with the formation of the GST council and key decisions being taken at its first meeting which was encouraging. The government is putting up a valiant effort to launch the GST by April 2017 and we applaud this endeavor. Monsoons, at negative 3% of the long term average, was concluded as normal (+/- 6 % is considered as normal) as against earlier forecast of above normal. With sowing at high levels, there is excitement over rural demand in the upcoming festive season. The Seventh Pay commission is also expected to have a favorable impact on consumer spending. The new RBI Governor Urjit Patel took office and with inflation likely to ease post-harvest, there is every likelihood that interest rates may be cut by ¼ to ½ % by end of this calendar year.

All these trends suggest that consumption in India is going to be the driving force behind the economy. Businesses which are focused on domestic consumption will benefit significantly as the cumulative impact of lower taxes through GDP, higher demand led by good monsoons / Seventh Pay Commission and lower EMIs (as interest rates come down) will put more discretionary money in the pockets of the average household for additional expenditure.

Sample of Companies Directly Benefiting from Rising Domestic Consumption	
Company	Trailing 12 month PER - Times (*source Cline*)
Apollo Hospitals	62.18
Asian Paints	60.65
Bajaj Auto	26.29
Century Ply.	34.51
Dr Lal Pathlabs	71.89
Eicher Motors	53.55
Havells India	47.08
Hero Motocorp	26.38
Interglobe Aviation	17.12
Kajaria Ceramics	42.79
Maruti Suzuki	38.75
Narayana Hrudayalaya	155.90
Page Industries	70.39
Pidilite Inds.	44.96
PVR	50.80
Symphony	68.28
Titan Company	56.10
Trent	152.55
TTK Prestige	46.81
United Breweries	80.58
United Spirits	105.82
Voltas	30.93

Unfortunately, there are few listed businesses which are available for investors to ride this trend and the listed ones are expensive (see table).

The traditional FMCG companies are not included in this list, not that they are cheap, but consumption patterns are changing. There is only so much toothpaste, detergent and hair oil which can be consumed. The spending trends are more towards mobile phones, luxury cars, weddings, overseas holidays, online ordering of food, clothing and electronics, streaming entertainment, high end home appliances and interior designing. Only a fraction of these products and services, are in the listed space and therein lies the investor's dilemma. Companies where there is secular and high growth are either very expensive or just not available for investment.

Another aspect to consider is that even in the listed space, few companies are large enough to merit inclusion in the Sensex and Nifty and most are in the mid and small cap space which explains the significant outperformance of the mid and small cap indices over the past three years (see graph below). One could argue that investing in small and midcaps is sensible in times like these, as they are delivering the desired returns, but there is the inherent risk in investing in small / mid-sized businesses and that cannot be ignored. When the market tanked on news of surgical strikes by the Indian army, the BSE Midcap (-3,60 %) and Small cap indices (-4.02 %) fell much more than the Sensex (-1,64 %) and Nifty (-1,76 %).

This peculiar structure of the present market is the primary reason for our cautious outlook.

While we remain extremely enthusiastic about the India growth story, finding businesses with high growth at reasonable valuations, which facilitate riding this story is a major challenge. Chasing stocks which have already appreciated manifold is not advised which is why we suggest buying at corrections or postpone purchasing towards end of this year when there will be more clarity on FY18 earnings. The IPO market is also turning interesting with new generation businesses being listed and that may increase investor choice. Alternatively, the capex cycle could pick up stream and that may increase the numbers of companies growing rapidly and therefore offer better returns.

The average returns of portfolios under our management are as follows:

Date From	31/08/2016	01/07/2016	31/03/2016	01/10/2015	01/10/2014	01/10/2013	02/10/2011
	1MONTH	3 MONTH	6 MONTHS	1 YEAR	2 YEAR	3 YEAR	5 YEAR
Elixir Equities Portfolio Performance	0.99%	10.74%	21.63%	17.31%	19.66%	29.95%	23.47%
SENSEX	-1.67%	3.16%	9.89%	7.87%	3.38%	10.25%	9.29%
NIFTY	-1.50%	3.87%	11.23%	9.81%	5.16%	12.03%	10.19%
Out Performance	2.49%	6.87%	10.40%	7.50%	14.50%	17.92%	13.28%

The topic of discussion in this month's Smart Investing Series is "*Strategy for Bear Markets*". We understand that this is not a priority subject for investors at this point. However, bull and bear markets are two sides of the same coin just as night and day and one will follow the other. Strategies followed in Bear Markets will determine wealth creation in Bull markets and investors must take cognizance and be prepared for all eventualities.

Dipan Mehta

SMART INVESTING – XI
- Strategy in Bear Markets

In the initial stage of a bear market, it is a no brainer that investors must sell. The weaker businesses first and then even the stronger ones. The challenge is to ascertain that a bear market has in fact begun and it is time to exit. Shaking off the bull market excitement and reconciling that the party is over is difficult for even for the most astute professional investors. We have all heard the phrase, "*Markets slide on the ropes of hope*"; and hope is what prevents investors from selling. The first fall of a bear market is generally termed as a correction in bull market. It is only in retrospect that players realize that the first decline was the beginning of a bear market and that while there may be bear market rallies, the longer term trend is downwards.

Since identifying bear markets is very tricky (as the slide could be a mistaken for a bull market correction), Smart Investing has a rule which may guide investors. If share prices are falling and growth is also flagging, then the bear market has well and truly begun. This principle may not work every time are markets tend to look ahead and values may fall even before the fundamentals deteriorate. However, in some situations, this may aid in early detection of a bear market.

Ideally, one would like to have zero exposure to stocks in a bear market, but that is neither sensible nor practical as savvy investors know that times do change and a bear markets will eventually pave way for a bull markets. Only if the investor is invested in a bear market will he / she be able to enjoy the fruits of a bull market. Therefore, once the initial flurry of selling is over and done with and share prices have already corrected in a significant manner, it is better to ride out the balance of the bear market and that is where the perseverance and conviction of an investor will play a major role.Unlike other assets such as gold, land or real estate, which have a physical form, stocks are only an entry in the demat account and to remain interested in this asset class requires confidence and firm belief that equites will deliver superior returns over the long term. Bear markets are when this faith is tested to the maximum. As values drop, fear does engulf the investors and there is a tendency to dump the holdings to avoid further losses. Bad news and negative rumors will keep surfacing and that may drive investors to sell blue chip holdings at lows. Such fears must be kept in check. The one mistake which investors must not make is panic liquidation. If the quality of portfolio is good, then all that is required is patience to ride out the bear market. When markets turn, portfolio values will shoot up and returns will become positive and in line with long term averages.

Bear markets are when great businesses are available at a massive discount. Stocks which could not be bought due to expensive valuations in bull markets must be bought at declines. Purchasing must be spread out and there should be no urgency in buying. Stocks selected for acquisition must be chosen carefully and only those businesses which have stood the test of time and remain in secular growth mode should be targeted. Novice investors must avoid cyclicals, although industry insiders may consider buying them if they are convinced that the worst is over for the industry.

Bear markets, which generally coincide with low economic activity and stress in the debt and commodity markets, bring out the worst in corporates. Mistakes and excesses of the years prior to the onset of the bear market now get exposed and there is heightened risk of complete destruction of businesses which are over leveraged or have poor corporate governance standards. Investors invested in such companies should sell at the first given opportunity and those on the sidelines must not get tempted to invest just because they have corrected significantly.

As regards portfolio composition, emphasis must be on safe stocks such as consumer staples (FMCG), pharmaceuticals, utilities etc. which will be consumed irrespective of the broader economic trends. Businesses which depend on consumer discretionary spending will be affected the most when there is an economic downturn and such businesses must be avoided as earnings may remain depressed during such periods. In an economic downturn, Capex cycle reverses as businesses curtail capacity expansion and capital goods manufacturers will find the going tough as orders dry up, these stocks should not be bought. Commodity companies will witness depressed earnings as commodity prices are low and these too should be on the avoid list. The only exception is that if that if there are specific companies still doing well despite adverse sectoral trends, then these must be studied and their shares acquired for the long term. If an enterprise is able to sustain growth even in down markets, then when the cycle turns, their growth rates will levitate to the higher level and that could be a great investment opportunity.

Even in a bear market, there will be a few outliers i.e. stocks which move against the tide and appreciate even when majority of the stocks are declining. Identifying such stocks requires quality research which may not be available to the average investor. Under such circumstances, as a thumb rule, if the company, whose stock price is appreciating, is a well-respected name with good corporate governance standard, strong balance sheet and decent *year-on-year* quarterly financial performance, then investors may consider investing in a gradual manner. Surviving a bear market is all about patience and discipline. Every individual, company and organization goes through bad times. Conventional wisdom is to ride out these bad times with minimal damage so that maximum advantage can be taken when the trend reverses.

Dipan Mehta