

NEWSLETTER
JULY 2021



PI SQUARE
INVESTMENTS

US equity and bond markets posted contrasting pictures in July as the S&P 500 hit new all-time highs while US Treasury yields slumped to lows last seen in February. While such a sharp decline in yields would normally imply a significant downgrade to the growth outlook, there appears to be a different set of stories behind the move. The unexpected spread of the Delta variant in low vaccinated states has amplified talk of the US economy moving past the peak point of growth, and the Federal Reserve's hawkish tone since June has indicated that there is a limit to how hot the central bank is willing to run the economy. Yet technical factors seem to have had a much larger influence on bond prices compared to the traditional laws of economics. Demand has been unusually strong due to a combination of Fed purchases, institutional investors looking to rebalance following a strong period of equity gains and elevated cash balances across the private sector. This strong demand has overwhelmed bond supply, as the US Treasury has opted to use up some of the huge cash pile that it built up at the height of the pandemic instead of issuing larger amounts of debt. The current level of Treasury yields appears inconsistent with the strength of the recovery, and in our base case we expect yields to move higher in the second half of the year with many of the technical factors noted above set to fade.

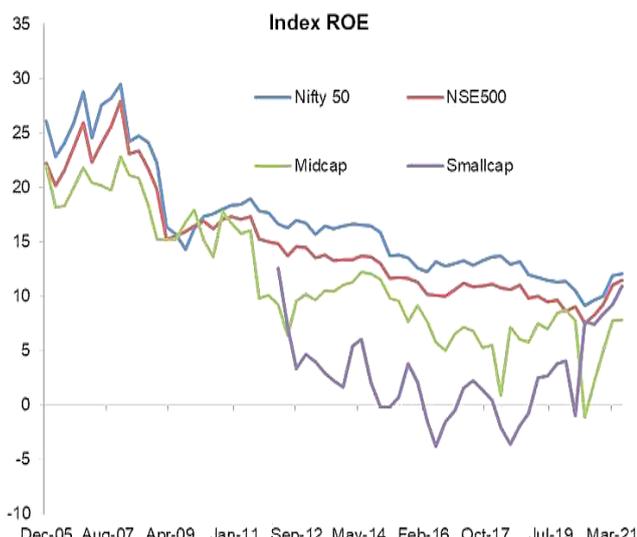
Back home in India, Nifty Index (+0.3%) was flat despite some bouts of volatility, in July 2021. In the absence of any major economic news or events, markets focused on quarterly earnings and management commentaries. Markets followed the strong momentum play and kept putting additional money on strong growth sectors such as construction materials, chemicals, IT services and metal companies. Small Cap (+8.1%) and Mid cap (+3.1%) indices continued to outperform wider indices. For the month of July, FIIs were net sellers at INR -23,000 cr., while DIIs were net buyers at INR +896 cr. The majority of the market volatility was driven by the retail and HNI investors. Turnover of top 50 stocks in India has gone down from 70%+ in May 2020 to 35% in July 2021. Majority of retail investors have focused on cyclical names and bottom of the pyramid names to benefit from valuation mismatch. For the CY 2021, Nifty is up by +12.7% while FIIs were net buyers at INR +12,000 cr. Indian corporates recorded one of the highest revenue and profit growth for the quarter of Jun-21. For the 353 companies that have announced their results so far, the sales growth was 83% and profits grew 108%. (refer to the table below)

Quarter	Nifty500 companies			
	Total Sales Growth	Sales Growth Ex-BFSI	Total PAT Growth	PAT Growth Ex-BFSI
Jun-21	35.8%	38.8%	83.2%	108.3%
Mar-21	17.6%	17.0%	107.3%	101.8%
Dec-20	4.3%	3.7%	60.5%	71.1%
Sep-20	-1.4%	-1.9%	21.1%	29.5%
Jun-20	-23.1%	-25.2%	-41.6%	-47.8%
Mar-20	-3.7%	-3.6%	-30.9%	-26.8%
Dec-19	0.6%	-0.4%	-10.6%	-14.7%
Sep-19	2.3%	1.1%	8.9%	4.6%
Jun-19	7.8%	7.2%	5.7%	5.5%
Mar-19	20.1%	19.0%	61.4%	65.5%
Dec-18	29.8%	29.2%	14.5%	13.9%

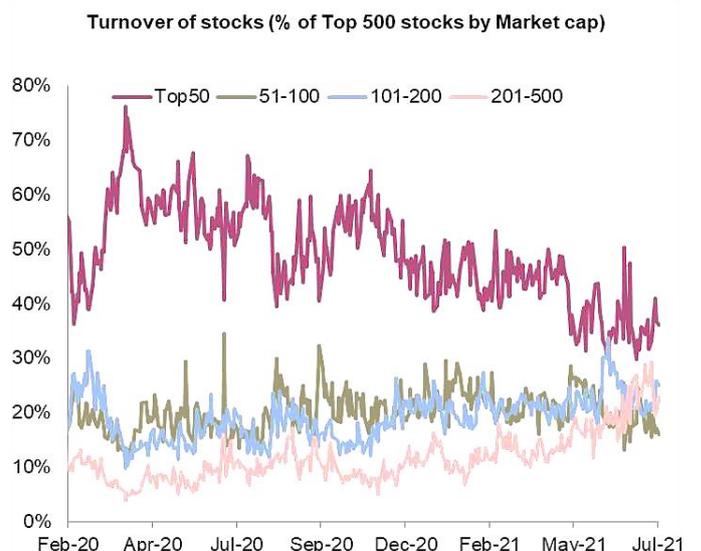
(Data Source: Ace Equity, June-21 comprises data of 353 companies)

All 3 of our India Equity strategies have continued to outperform wider markets for the year. In India Equity solutions, we have increased our allocation to mid-cap IT names as well as quality mid-cap and small-cap names. Some of our cyclical names in Metals and Cements have gone up by 15-20% in the last 2 months. For our India market leader portfolio (Quant portfolio), June was the month of changes. We have structured our portfolio based on our strong quant matrix focused on creating smart-alpha compared to volatile markets. Auto and Banking names were the laggards in our Quant portfolio. For India Edge portfolio, our small cap chemicals and FMCG names have posted strong outperformance for the year.

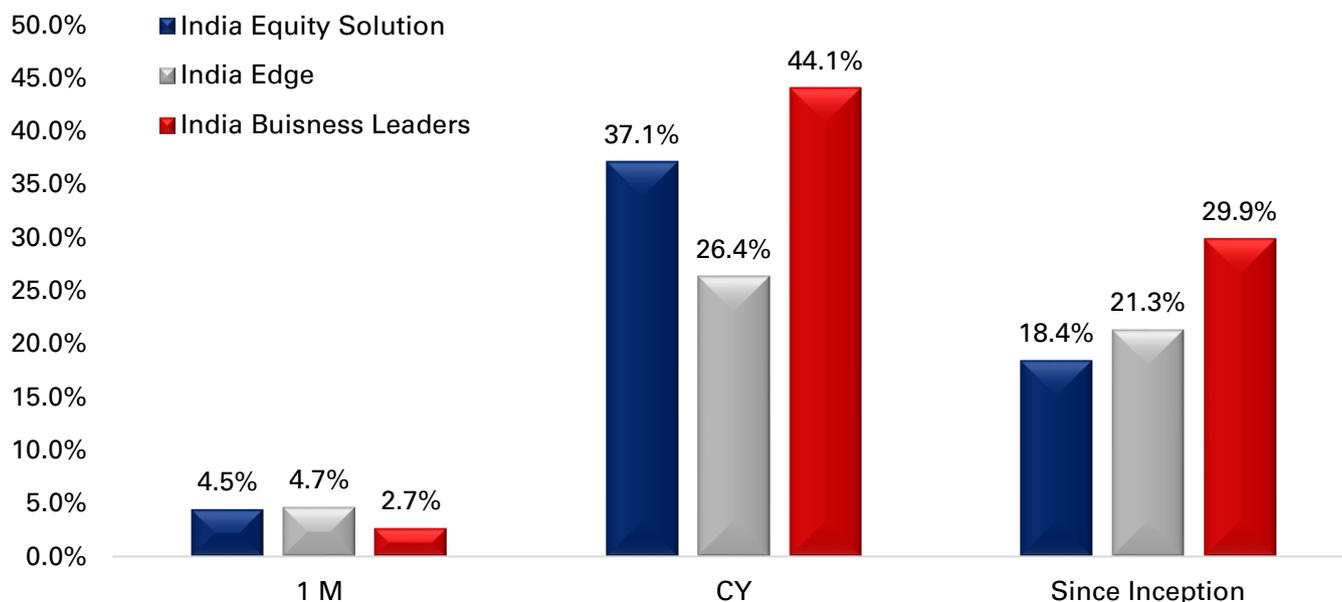
At current levels, Nifty-50 is trading around 22.4x on FY22E and around 19.5x on FY23E. At Pi Square, we expect Nifty earnings to grow by 29% in FY22E and by 18% in FY23E. As covid cases go down and the economy opens up (supported by the vaccination drive), we shall expect strong numbers for the economy as well as domestic consumption in the second half this fiscal. Biggest concern for the equity markets is the high inflation and low interest rate, we are keeping an eye on the Federal bank policies to see at what point they will cut down their bond purchase plans and start increasing the rates. On a valuation basis, some sectors are trading at the highest-ever valuations where investors need to be careful, but there are also some great businesses with a strong moat at reasonable valuations. At Pi Square, we have always believed in the bottom-up approach and have looked at investing with great management. Since our first purchase of Bajaj Finserv in 2011 at 550, stock has corrected above 30% from the top multiple times in the last decade but as we have always evaluated the business as a partner and not just a mere shareholder, we have managed to create a great multi-bagger in the process (CMP: 14222). We continue to focus on the businesses that have consistent sales and earnings growth, high return on equity, and strong management pedigree. As top management continue to deleverage their balance sheets in last few quarters, we expect Return on Equity to grow from 11-12% (Mar-21) to 17-18% ROE in the coming years (not seen since FY09-10).



Source: Bloomberg



Strategy	1 M	CY	Since Inception
India Equity Solution (Incep. date: Jan 2011)	4.5%	37.1%	18.4%
Nifty 50	0.3%	12.7%	9.5%
India Edge (Incep. Date: Jan 2011)	4.7%	26.4%	21.3%
Nifty 50	0.3%	12.7%	10.2%
India Business Leaders (Incep. Date: May 2011)	2.7%	44.1%	29.9%
Nifty 50	0.3%	12.7%	10.7%



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