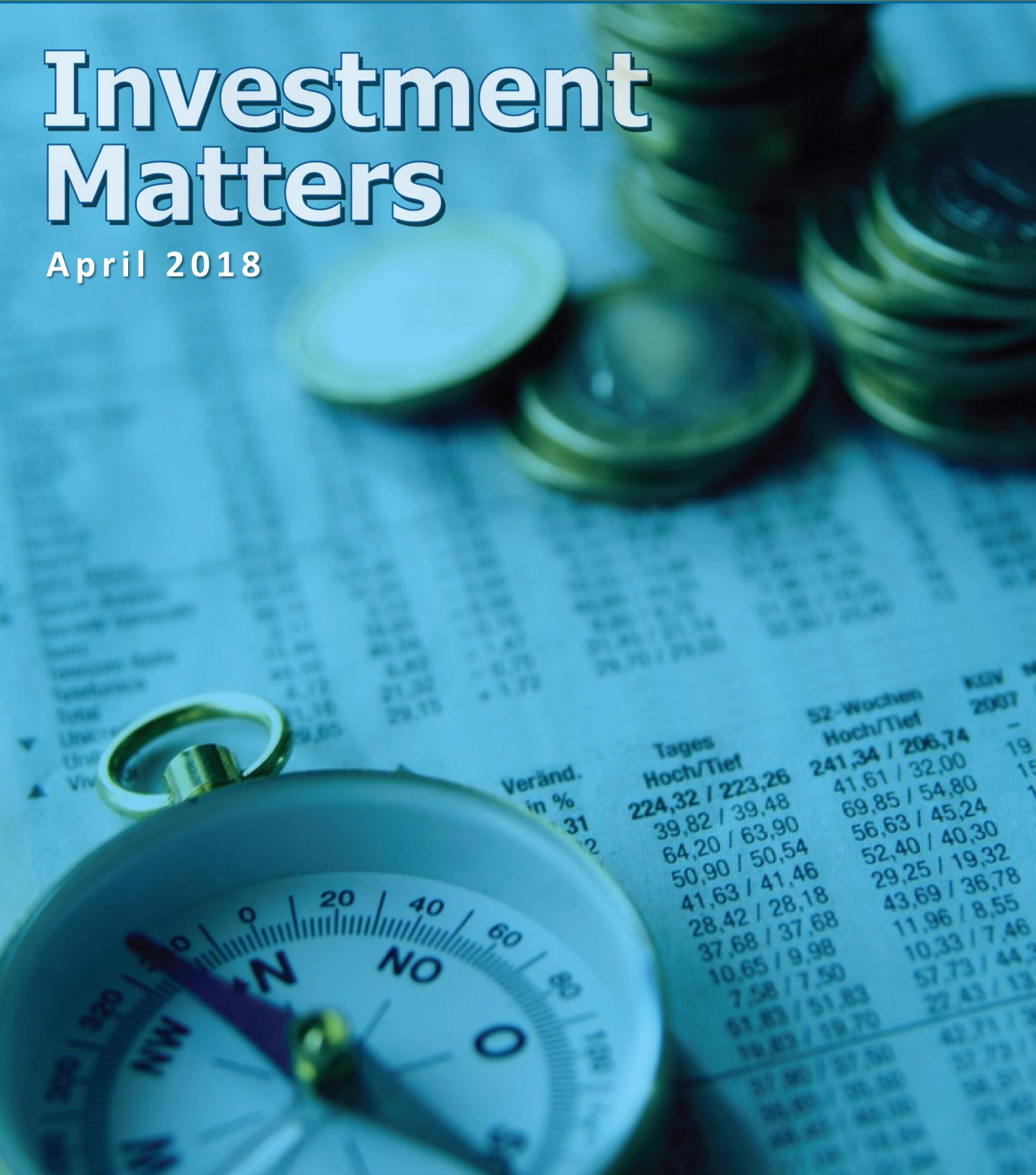


Investment Matters

April 2018



Veränd. in %	Tages Hoch/Tief	52-Wochen Hoch/Tief	KGV 2007
31	224,32 / 223,26	241,34 / 206,74	-
-2	39,82 / 39,48	41,61 / 32,00	19
	64,20 / 63,90	69,85 / 54,80	15
	50,90 / 50,54	56,63 / 45,24	1
	41,63 / 41,46	52,40 / 40,30	
	28,42 / 28,18	29,25 / 19,32	
	37,68 / 37,68	43,69 / 36,78	
	10,65 / 9,98	11,96 / 8,55	
	7,58 / 7,50	10,33 / 7,46	
	51,83 / 51,83	57,73 / 44,3	
	19,83 / 19,70	22,43 / 13	
	37,90 / 37,50	42,71 / 3	
	38,40 / 38,30	37,79 /	
	48,40 / 48,30	58,21	
	18 / 18,30	25,40	
	20,30	25,70	

EQUITY OUTLOOK

After a good 2017, Q1 2018 was quite tumultuous and volatile. As we had mentioned in our last communication, SMIDCAP valuations were at a significant premium to NIFTY on a trailing earnings basis and were reflecting unbridled optimism. Though volatility and corrections were experienced by all markets, the turning point for Indian markets came with the presentation of the Union Budget on Feb 1st 2018.

Union budgets in India are given undue importance given the constant tinkering in tax rates, both direct and indirect and for its signalling impact on policy direction. Given that GST had been rolled out in mid-2017, there was very little scope for tinkering on indirect taxes. Hence, most of the focus was on direct taxes. There was not much tinkering there either except for an imposition of LTCG (long term capital gains) tax on equity investments. India had removed LTCG on equities to zero in 2004 to encourage flow of savings to capital markets. 14 years later, it has been re-introduced. Imposition of LTCG has always been an emotive issue with investors, especially local investors, as FPI's were mostly exempt (though they will also start paying taxes from April 2018). In order to prevent bunching of selling to avail the opportunity to book tax-free gains in a short window, the government thoughtfully grandfathered the tax by marking the notional cost at the highest price achieved on January 2018. The strong inflows by domestic investors in equity markets since 2014 and perhaps a political signalling that rich need to be taxed, given Modi's pro-poor stance, seemed good alibi to introduce LTCG. Apart from the LTCG imposition the announcement of an ambitious healthcare plan for the bottom 500mn population and a promise to compensate farmers for their produce at 1.5X the costs got investors a bit rattled as the exact fiscal outlay was not clear and left open ended.

The subsequent hardening of bond yields, BJP losing some important Lok Sabha seats in a by-election, lower than expected GST revenues, the breaking out of the Nirav Modi- Punjab National Bank Scam, frontloading of provisions by banks due to revised RBI guidelines on NPA recognition and a correction in global markets all coincided to deliver a much anticipated and desired correction in markets.

We believe that bulk of the reforms by the Modi government are through – demonetisation, GST, the Bankruptcy code and NPA resolution mechanism through the NCLT process – are through. For the remainder of the year the government will get into stabilising the GST and focussing on social sector programmes in the run up to the elections. Our interactions with portfolio companies suggest that the initial hiccups in GST are getting settled, though exporters have seen delay in tax refunds. As the E-way bill gets into force from April, we may see a perceptible improvement in GST collections over the next few months. The economy is on the mend and is starting to pick up speed. If a few large and high profile cases of NPA's get resolved through the yet untested NCLT process, it will substantially enhance corporate sentiment. We also expect earnings to rebound in FY19.

EQUITY OUTLOOK

So while this year maybe noisier than usual, it is a great time for active managers like ourselves to focus on our portfolio companies and new opportunities amongst companies that we believe have the competitive advantage to grow ahead of competition and take away incremental market share as large swathes of unorganised players, leveraged competitors and companies whose business models were more dependent on being politically connected.

Hiren Ved

**Chief Investment Officer
Alchemy Capital Management Pvt. Ltd**

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