'Managing investor behaviour is crucial to building long-term customer base'

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PPFAS Mutual Fund completed its seven-year anniversary in May. The fund has delivered a return of 15.49% CAGR since its inception (as of 10 June). Its novel structure of investing in Indian and foreign stocks in a 65:35 proportion gives investors the advantage of equity taxation and global diversification. In an interview with *Mint*, PPFAS Mutual Fund chairman and CEO Neil Parag Parikh spoke about the asset management company's (AMC) journey so far and what it delivers to investors. Edited excerpts:

What made you think of this India plus international structure when you launched in 2013? Can you give some background on the transition from being a portfolio management service (PMS) to an AMC?

Post the 2008 financial crisis, we thought valuations all over the world, especially in the US, were mouth-watering. We thought this would be a great time to invest in the US and wanted an investment vehicle to participate in global markets. By 2010-2011, we were opening overseas account for some of our clients, but this model was not scalable, tax-inefficient and time-consuming. We were running a PMS and the laws did not allow us to invest in overseas stocks using this structure. A mutual fund structure would allow us to participate in overseas securities in a tax-efficient and simple manner.

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We thought that long-term capital gains tax would be reintroduced and that the MF structure would work better than a PMS. We thought the MF will be a much better compounding machine as the individual will be taxed only once on redemption. In a PMS structure, the investor will be taxed on every buy and sell transaction. So, tax-efficiency of a MF was far superior to other structures.

The ease of onboarding clients and scalability of the MF structure were other reasons to transition to being an MF in 2013.

Of the returns you've generated in this period, was US outperformance a huge contributor? Does the US look overvalued now?

The US markets have outperformed the Indian markets in the recent past. Having around 30% of our portfolio outside India has surely contributed to the performance of the fund. But it is all about picking individual investments that have been the bigger contributors.

By following a bottom-up strategy, we look at each investment opportunity on its own merit. We want to buy innovative companies that we believe will thrive and increase the market share in the years to come, in addition to being available at a reasonable valuation.

So, even in the US there will be pockets of overvaluation and pockets of opportunity.

We consider the investments that we have made globally to be worthy and sound opportunities going forward.

Neil Parag Parikh, chairman and CEO, PPFAS Mutual Fund.

PPFAS Long Term Equity held 12.06% cash at the end of February 2020. It deployed cash as the market fell in March and April and as on 31 May, it holds 2.79% in cash. Are cash calls an important tool in your arsenal?

Ideally, we would want opportunities at all times and be 100% invested in equities. But that does not happen in reality. We have our investment universe of about 500 stocks (both Indian and global) that we track closely. This is our circle of competence. Within this, we want to be invested in 25-30 companies.

But sometimes valuations are stretched and we do not get the opportunity to invest at a price we feel comfortable with. So instead of chasing returns or valuations, we prefer to be patient and sit on cash.

As such we do not have a cash strategy. It's the residual position that remains if we do not find opportunities. These decisions can be unpopular in the short term like in 2007 or 2017. But I believe this process helps us limit the downside and avoid making big blunders of overpaying for investments.

How many investors have stuck with the fund since its launch? Would you say that managing investor behaviour is also an important task in the asset management business?

I do not have exact numbers, but I think the majority of our investors have stuck with us. We had transitioned most of our PMS clients to the MF structure, so a lot of them have been with us for 15-20 years.

Managing investor behaviour is crucial to building a base that trusts you. These investors will stick with you for the long term and not be too perturbed if sometimes there is an underperformance in the short term. For this, there has to be complete transparency in communication and honesty in action.

For this, we hold an annual meeting for our unit holders. Here we put ourselves up for scrutiny. Investors are free to ask us any question they might have. For us, it is an opportunity to communicate freely with our investors and also let them know our thought process on various issues. I believe this has helped create a two-way trust factor.

Do you see a sectoral rotation from banks to consumer goods and pharma in India? Which sectors do you think will drive the markets?

Sectoral rotation and which sector drives the market is hard to predict and obvious only in hindsight. The banking and the financial sector has been a large part of the index and the economy. The pharma sector, despite its issues in the recent past, has shown resilience along with other essential sectors. We need to wait and see how the current situation resolves globally; we will then see which sectors have the best chances of recovery.