DON'T BUY FANCY STOCKS

Investing requires a lot of self discipline says Parag Parikh, Chairman and CEO, PPFAS Asset Management Private Ltd, in this interview with Chirag Madia where he shares his view on the way to go with equity investing

Does your approach to investing such as stock picks and your portfolio vary as individual investor, manager of a PMS account and a fund manager?

No. It remains the same. My portfolio is quite similar to that of PPFAS Long Term Value Fund, as the scheme comprises the lion's share of my equity exposure. The same applied to the PMS too. The current value of my and my team's holdings in our scheme, is approximately ₹27 crores. We felt that investing in the scheme was the best way to demonstrate our intention of aligning our interests with those of our investors. I feel that a key failing of the mutual fund industry is its skewed incentive structure based on the amounts of assets managed. Hence the stress has often been on asset gathering, rather than asset management, as the remuneration of fund personnel depends more on the former, and less on the returns generated for investors. Also, their holdings in the schemes managed by them, are often miniscule. This erodes investor confidence even further. We are attempting to redress this, by not only investing, but by disclosing our holdings every month.

Also, we are very clear that, we are not here to chase assets under management (AUM). That is why we will not launch any equity scheme in addition to PPFAS Long Term Value Fund. As a mutual fund our job is to manage investors' money and make them wealthy over the long-term. We are the only fund house in the country which states that investors with an investment horizon below five years should stay away. As we want to dissuade those with a short-term outlook.

Does the macro economic or political outlook have a bearing on your portfolio? Does it impact the cash position)?

Rather than getting bogged down by macros, we prefer to focus on

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investing in fundamentally sound businesses at reasonable valuations. We like businesses that are run by credible management, have pricing power, have low debt and are relatively easy to understand.

This analysis is overlaid with the application of behavioural finance principles and strategies. My experience tells me that to be successful in the stock market one has to keep one's emotions under control and take a cue from other people's emotions so as to benefit from it. I would like to sum up in a quote by Warren Buffet that, "Be fearful when others are greedy and greedy when others are fearful"...Easier said than done, of course.

What are the essential dos and don'ts while managing your equity fund?

There are processes which we follow, as I said earlier. Apart from that, we don't chase fancy stocks nor are we dogmatic about having a fixed allocation to certain sectors. I strongly believe that, when you buy fancy stocks you have to pay fancy prices and soon you will end up with a fancy loss when the fancy ends. Warren Buffet sums it aptly when he says that 'Investing is simple, but not easy'. In other words, while investing is not rocket science it is tough, as it requires a lot of self discipline. The challenge for investors is to not get carried away by the noise in the market. Finally, while we will not purchase at absurd valuations, we also do not believe that there is any one perfect moment for a purchase. Hence, we do not place too much premium on market timing.

What kinds of stocks make inroads in your portfolio?

We look at companies that are innovative and having a sustainable business model. Take a simple example; we were buying fast moving consumer stocks (FMCG) way back in 2003 when others were busy buying IT stocks. That strategy resulted in dwindling in assets for our PMS as clients redeemed the money, as we didn't have exposure in IT. But that approach stood the test of time as we remained the beneficiary when the IT bubble burst.

We don't get an opportunity to buy fundamentally sound companies everyday. Hence one has to keep those stocks on the radar and strike it when they are trading at cheap valuations. As the aphorisms goes 'Fortune favours the prepared mind'. The market is made up of sentimental fools and you always get an opportunity to buy good quality companies. Opportunities will always comes one should never lose the patience in the markets.

What kind of stocks never enters your portfolio?

As a rule, we avoid companies whose managements have a history of being unfair to minority shareholders. Also, as stated above, we usually steer clear of stocks which are in vogue, and consequentially, overheated. As a steward of capital, we cannot justify investing in companies or sectors where we would not invest our own money. For instance, we feel that the financial statements of real estate companies hide more than they reveal. Hence it is hazardous to include them in the portfolio. For us, both, preservation of capital and reasonable return, are important. We have to go by the law of the farm, you can't reap tomorrow what you have sowed today.

Some of your value bets like Maharashtra Scooters and Noida Toll Bridge are testing the investor's patience. When in your view these bets are likely to fructify?

I don't know when it's going to fructify, but I know that Noida will be debt free in a year or so, and could begin distributing outsized dividends to its shareholders, soon thereafter. The bridge is already built. No further capex is anticipated. Maharashtra Scooters is a proxy on underlying Bajaj group companies, even assuming that the discount of 75 per cent does not close out, the shares will appreciate as the underlying companies appreciate. If the discount closes out or narrows it is a lottery in the offing. Both these have been testing the patience of investors for a while now, but we are convinced about their intrinsic attractiveness.

What is the basis of picking the foreign stocks for your portfolio?

Every foreign stock that we have purchased, has given our investors an opportunity to participate in a company which has a moat or unique proposition that cannot be obtained through the purchase of Indian companies or even the Indian subsidiaries of these same foreign companies. Sometimes (as in the case of Nestle) it is a valuation play, as the foreign parent can be purchased more cheaply than the Indian arm.

Buying a stake in parent companies eliminates the royalty and other transfer pricing issues that we have seen in Indian subsidiaries. Also, since the foreign parent has various global arms, any impending slowdown in the Indian market could be offset by compensatory performance in some other part of the world, which will be reflected in the global P&L account.

Finally, as 90 per cent of the foreign exposure is hedged through exchange traded currency futures contracts, instead of bearing a currency risk, our scheme actually earns 7-8 per cent. This is because, the USD-INR 'Forward' / 'Futures' rate is always higher than the spot rate in order to reflect the inflation or interest differentials between the two nations. Only the residual 10 per cent of the foreign exchange denominated portfolio is affected by prospective changes in the value of the USD-INR rate. On the whole, our scheme offers more economical and tax-efficient route to foreign investments as compared to the feeder funds offered by many other mutual funds.

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Following your approach which you believe in, what are the kind of opportunities you will miss?

It is difficult to say 'a priori' as to which opportunities we will miss. That will only be known in hindsight. While not jumping onto a particular bandwagon may lay us open to accusations of 'errors of omission', I am confident that over the longer term, our unit holders will be glad that PPFAS Long Term Value Fund was fearful when others were greedy. WI