Portfolio Management Services

Monthly Newsletter

This document is of 4 pages and should be read in it entirety.

Pramerica

Dear Investor,

We are delighted to introduce our first Newsletter to our Portfolio Management (PMS) clients. We launched the PMS business in June 2013, amid significant degrees of negativity about the equity markets in general, and the PMS platform in particular. However, rather than a hindrance, this was an unprecedented opportunity. Negative sentiments for equities meant buying opportunities in many high quality companies which were trading at deep discounts to their intrinsic worth. And negativity surrounding the PMS platform meant that we had the opportunity to change it into a better proposition for investors.

We started with a survey to understand investor & distributor complaints and set ourselves the task of addressing these in the product design itself. At the top of this list were,

1) Sub - optimal performance and adverse Tax treatment: On further study, it became clearer that the root cause for both was the same; high levels of churn. Increased transactions costs and tax treatment of short term capital gains resulted in huge gaps between the performance of the 'model' portfolio which excludes both, and actual investor portfolios. Also, high portfolio turnover statistics enabled the tax authorities to classify this 'investment' activity as a business, further increasing the tax burden. Our portfolio strategy was devised to consciously reduce the levels of churn. How we make this possible is detailed in the Portfolio Manager's commentary.

2) Usurious fee structures: The PMS platform offers an evolved form of investing with significantly higher levels of transparency and privacy. However, while its benefits for large – ticket seasoned investors are numerous, it also lends itself to fee structures which can be potentially damaging to investor interests. Our fee structure is simple and straightforward. We charge a reasonable annual fee and no profit sharing. This ensures that all investors are treated fairly at all times. Also, since fees are often excluded when calculating the performance of 'model' portfolios, a flat and consistent fee structure reduces the gap between 'model' performance and investor performance further.

These are just a couple of examples of the initiatives we have taken to ensure that our PMS platform is truly investor & distributor friendly. There are many more which, at the moment, are held back since they challenge common market practices and require deep, sometimes regulatory, changes. We continue our efforts with the singular aim of ensuring that you, our investors, benefit.

Rajiv Shastri
Business Head

E. A. Sundaram
Portfolio Manager

Dear Investor,

At the outset, we take this opportunity to articulate how exactly we intend to manage your money.

Pramerica Deep Value Strategy is positioned in such a way that it offers a genuine diversification compared to open-ended mutual funds. The portfolio presently (31/10/2013) has only a 3.7% matched position with the NIFTY index, and this signifies the creation of a completely different type of portfolio.

Also, we make it clear at the outset that our intention is NOT, repeat NOT, to maximize the returns generated. Our intention is to create a portfolio of solid companies with sound businesses and balance sheets, purchased at a time when the stocks are not extravagantly priced, and hold them for a sufficiently long period so as to generate a good after-tax return to you, the Investor.

A good business is available at a reasonable or attractive price only when the company is going through a difficult period. If the times were good, the enthusiasm with which such a company would be viewed in the stock market would also make the stock expensive; and therefore unattractive from an investment point of view. So our intention is to pick such businesses that are going through a rough patch, after doing careful research to satisfy ourselves that the difficulty is indeed temporary.

Of course, care is taken to see that we don't buy a stock just because it is cheap. For this reason, we buy companies with a long track record (sometimes running into several decades) of profitability and shareholder friendliness. Almost all of our companies are either market leaders or a strong No.2 in their respective businesses.

We will be unable to predict when the stock will perform, but we are quite confident of the reason why it should perform. We are also confident that the price at which it is purchased would compensate for any waiting period that you as an investor may need to endure.

Dear Investor, to sum up, our intention is to give you a portfolio of "good" companies; a portfolio that we are confident would earn you a decent return over time without taking on unnecessary risks. We don't, and never will, intend to be "the best" in terms of "highest returns" generated.

Consolidated Portfolio Performance as on 31st Oct 2013

Period	Pramerica Deep Value Strategy	CNX Nifty
1 Month	5.12%	9.83%
3 Months	8.64%	9.70%
Since inception date 03/07/2013	9.35%	7.54%
	Pramerica Deep Value Strategy	CNX Nifty
Daily Volatility	0.63%	1.47%
Beta	0.31	
	Pramerica Deep Value Strategy	CNX Nifty
Weighted average P/E multiple	16.94	18.18
Dividend yield	2.10%	1.46%

The NIFTY matched position as on 31/10/2013 is 3.69%

Performance depicted above, as at Oct 31, 2013, is based on all the client portfolios under the strategy existing as on such date, using time weighted average methodology. Past performance is no guarantee of future returns. The above portfolio performances are before charging of any expenses. Please read page no. 3 for the complete text of the disclosure

An example from the existing portfolio

In any company that is in a cyclical business, the stock becomes attractive from an investment point of view if

a. The present financial indicators such as margins are significantly below long term average

b. There is no reason, based on reasonable research, to believe that the long-term prospects for the company are permanently impaired, and

c. The stock, reflecting the short term fundamentals, is quoting at levels that are close to its historically low valuations.

All three parameters are valid in the case of Blue Star Ltd.*

For the last 20 years, the average EBIT margin (Earnings before Interest and Tax as percentage of sales) for Blue Star was 7.2%. It turned negative in March 2012 and recovered to 3.7% in 2013. The company, in its consecutive conference calls, has expressed its intention to take it back to long-term average levels over the next year or so.

Blue Star (similar to Voltas) is a company engaged in Mechanical, Electrical, Plumbing and Firefighting equipment installation for all sorts of buildings. Therefore, their business success depends upon something new being built. They are not dependent upon any single industry and cater to the IT, ITES, Banking, Insurance, Retail, Entertainment, Commercial Buildings, Industrial Buildings, Hospitals, Hotels, Restaurants, Cold storages, Airports, and also to other infrastructural projects like Metro Railways,etc.

The last 2-3 years (especially the last year and a half) have been a very bad period for the entire industry, with new construction activities virtually coming to a standstill.

The bet is that this situation is not the new permanent situation, and India's industrial activity will recover. Only the timing is uncertain.

The company has an average RoCE (Return on capital employed) of 34% for the last 15 years. In 2012 this was -2% and has since improved to 12% in 2013.

The stock is now quoting at a market capitalization/sales ratio of 0.5 times, compared to a peak of 2.5 times in 2007 and nearly 2.4 times in 2010.

Subjective assessment

Blue Star is not in a business that affords the company to have significant pricing power. It is very much subjected to the vagaries of the business cycle. However, it is in a position where the future growth of the company does not depend upon massive capital infusions. The company's asset turnover ratio has been quite comfortable at greater than 4.

The company has got into the present difficult position because of a combination of (a) poor economic fundamentals (b) some poor business decisions and (c) bad luck.

The management is, in our opinion, trustworthy, and is taking specific steps to bring back the company to financial health. Already, signs are visible, and the margins in the recent quarters are showing signs of improvement.

* For illustration purpose only. Please read page 3 for the complete text of the disclaimer.

Important Disclosures regarding the consolidated portfolio performance

Performance depicted on page no. 2, as at Oct 31, 2013, is based on all the client portfolios under the strategy existing as on such date, using time weighted average methodology. Past performance is no guarantee of future returns. The above portfolio performances are before charging of any expenses. Please note that the actual performance for a client portfolio may vary due to factors such as expenses charged, timing of additional flows and redemption, individual client mandate, specific portfolio construction characteristics or other structural parameters. These factors may have impact on client portfolio performance and hence may vary significantly from the performance data depicted above. Neither the Portfolio Manager, nor its directors or employees shall in any way be liable for any variation noticed in the returns of individual client portfolios. The Portfolio Manager does not make any representation that any investor will or is likely to achieve profits or losses similar to those depicted on page no. 2.

Return for period upto 1 year is absolute. Since inception date stated is considered to be the date on which the first client investment was made under the strategy.

Disclaimer for the example from the existing portfolio

The stock specific comments are for informational purposes only and the same is not intended as an investment recommendation or investment advice. The above comments do not constitute a solicitation to purchase or sell securities or any investment strategy. The analysis or viewpoints, if any, regarding the future of the markets or securities should not be construed as recommendations of any specific security or specific investment advice. Investors should always consult an investment professional before making any investment. The analysis provided is based on both technical and fundamental research and is provided "as is" without warranty of any kind, either expressed or implied. Although some of the information provided above is derived from sources which are believed to be reliable, the same is not guaranteed

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