Liontrust India Fund

Q1 2023 review

Fund manager: Ewan Thompson, assisted by Ruth Chambers

Over the quarter, the Liontrust India Fund returned -6.5%, versus the MSCI India Index's -8.9% and the IA India return of -5.9%*^.

The first quarter of 2023 saw equity markets broadly rally − albeit with a high degree of volatility − in a continuance of the general up-trend established in the previous quarter. A continued fall in global energy prices eased inflationary pressures somewhat, although the quarter saw an ongoing uncertainty over the ultimate peak of US interest rates given the persistently resilient labour market. Moreover, the significant upwards move in interest rates over the last three years ultimately led to the collapse of Silicon Valley Bank in the US, triggering wider concerns over the health of the US financial sector and deposit flight, in turn driving a tightening of credit conditions beyond the actions of the Federal Reserve.

In China, the economy continued to rapidly open up following the abrupt relaxation of the zero-Covid policy that has so dramatically hampered China's growth rate in the past two years. Having significantly underperformed emerging (and wider global) markets since late 2020, China enjoyed a significant rally from early November and this continued in the first weeks of the quarter as investment flooded back into the country. Given India's huge outperformance of both China and emerging markets in the past three years, it was perhaps no great surprise that the market underperformed peers during this sudden market rotation. Indeed, India was one of only a small number of major markets that produced a negative return over the quarter. For the three-month period, India returned -8.9% in sterling terms, against emerging markets' +1.1% and developed markets' 4.8%. It should, however, be noted that the entirety of this underperformance came in January, with India's relative performance improving steadily through the rest of the quarter and into April.

Whilst a good degree of India's poor relative quarter was due to natural market rotation into China and out of the previous years' winners, there was one key development domestically that compounded the weaker performance, namely the much-publicised report from activist US research firm Hindenburg into the Adani empire. The market fall-out as a result of the negative report saw the Adani stocks suffering heavy losses − indeed due to the huge outperformance of these companies during recent years they had become a significant portion of the benchmark index, thereby weighing down the wider market even though fears of a wider market contagion were quickly dismissed.

Indeed, business was very much as usual across the Indian economy during the first quarter of the year with credit growth remaining in the 15-20% range, supported by the well-capitalised banking sector and resilient corporate demand for credit. Corporate health and earnings growth remained robust, in turn supporting healthy tax collections from the Goods & Services Tax. Despite the relative correction in markets, there was relatively little change in earnings per share forecasts. Interest rates continued to rise, from 4% a year ago to 6.5%, though the RBI paused somewhat unexpectedly in April, suggesting the peak of rates may well have been seen. Inflation in India has been elevated (as it has across all global economies), though India did not see the dramatic step change in inflationary pressures elsewhere − by the end of the quarter CPI had fallen back below 6% due to an easing in food prices.

Over the quarter the Liontrust India Fund enjoyed a strong period of outperformance, returning -6.5%, 2.4% ahead of the MSCI benchmark. The Fund is ahead of the benchmark by 3.5% over the past year and by 27.5% over three years, placing it at the top of the sector over this time frame. For the first quarter of 2023, the most significant outperformance came from having zero exposure to the sharply underperforming Adani stocks (which had until this moment been a significant cost to the Fund's performance given their parabolic rise in the previous years). Elsewhere strong single-stock performance came from the likes of KEI Industries, a producer of cables and wires for the building and construction industries − the company has been benefiting from significant public capex in the power transmission & distribution sector in order to support electricity generation capacity. Also in the industrials sector Blue Star, a manufacturer of air-conditioning units and commercial refrigeration systems has benefited from the unseasonably warm weather across India as well as the broader economic recovery. A degree of portfolio drag came from the hospitals sub-sector, where an expectedly seasonally weaker quarter for regional hospital chain Krishna Institute of Medical Sciences weighed on stock returns. This has entirely reversed in April it should be said.

New stocks over the quarter included insurer SBI Life, where we see the market in retail protection returning to growth after several years of anaemic sales, and where SBI Life's strong distribution network stands it in good stead against peers. Elsewhere in financials, a position was initiated in IndusInd Bank to complement existing positions in larger private banking peers. As industry growth is likely to moderate we expect IndusInd to remain robust with a cyclical recovery in its commercial vehicle and unsecured lending book. To fund these purchases profits were taken in auto player Eicher Motors where valuations had become extended and in Asian Paints where the increased capital expenditure plans of new entrants threatens to disrupt profitability in the paints market.

We are encouraged by the steady improvement of the Indian market throughout the first quarter and into the second. With valuations having corrected − India's premium to emerging markets is now below both five and ten-year averages − attention has returned to the reality of India's uniquely attractive medium- to long-term investment opportunity, with the property market moving from strength to strength despite higher mortgage rates and supportive government fiscal and regulatory policy.

Moreover, signs of strength in the hitherto lacklustre rural demand picture offer support to the economy as inflationary pressures ease, offering relief to wage pressures seen over the last year. Foreign selling of the market was acute in the first two months of the year, seeing $3bn of net outflows against a backdrop of persistent inflows into North Asian markets. However this turned around in March with foreign money returning to the market against a backdrop of peaking interest rates, crude oil below $80 (advantageous for India) and valuations back below average with earnings expectations still among the highest in the world. We remain of the belief that India presents one of the most attractive medium- and long-term investment opportunities within emerging markets, if not globally.

Discrete years' performance (%), to previous quarter-end:**

	Mar-23	Mar-22	Mar-21	Mar-20	Mar-19
Liontrust India C Acc GBP	-3.0%	22.5%	77.2%	-37.8%	0.5%
MSCI India	-6.5%	23.5%	58.5%	-27.3%	14.9%
IA India/Indian Subcontinent	-4.1%	18.7%	55.4%	-26.7%	7.2%
Quartile	2	1	1	4	4

***Source: FE Analytics as at 31.03.23**

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For a comprehensive list of common financial words and terms, see our glossary at: https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance is not a guide to future performance. The value of an investment and the income generated from it can fall as well as rise and is not guaranteed. You may get back less than you originally invested.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

The portfolio is invested in smaller companies - these stocks may be less liquid and the price swings greater than those in, for example, larger companies. Investment in the Fund involves foreign currencies and may be subject to fluctuations in value due to movements in exchange rates. The Fund may invest in emerging markets/soft currencies or in financial derivative instruments, both of which may have the effect of increasing volatility.