The Bottom Line... PLUTUS LEGACY

TRUSTPLUTUS
Wealth Management with a Conscience

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Dear Investors,

Greetings.

Just a few weeks into the coronavirus crisis, many are pointing to the contrast between what is happening in the real economy and financial markets. In a month in which Maruti reported zero sales, the Nifty 50 had one of its best ever months. While one is hard pressed to explain the rationale for what happened in April, it can be explained that some of the financials with large weights in the index were oversold and with the help of a conglomerate that was demonstrating a path towards deleveraging, a bear market rally helped the index recover some lost ground.

As we write this note, the index has corrected by over five percent and the index is now showing alignment with the challenges facing the real economy. While it is early days yet into the earnings season, it may just be that many companies may end up writing off this financial year in terms of business results. Consumer staples, Pharma, telecom and firms involved in the agricultural sector are likely to fare better than firms that deal in high ticket discretionary items, real estate and construction companies and firms in the capital goods sector.

Plutus Legacy, our long only large cap oriented advisory portfolio continues to perform very well. The portfolio returned 12.2 % in the month of April and is running at over twenty percent outperformance versus the Nifty since inception. We hold our view that in every sector, the leaders with their strong balance sheets, low leverage, high free cash flow and adequate return on equity will continue to gain share and deliver returns to their shareholders. In times like this when less privileged firms are running around for working capital and for business, our portfolio companies are lenders of the last resort, are providing credit to their dealers/vendors and are reporting relatively less portfolio stress (financials) when compared to their sector counterparts at large.

One of our large allocations in the portfolio is to Reliance Industries, which is the largest Indian conglomerate with diversified businesses across energy, petrochemical, digital and retail. While the core refinery and petrochemical businesses continue to generate free cash flow the weakening business environment in the last quarter has affected the overall profitability. While we do not believe that oil prices will remain lower forever, we believe that Reliance's integrated portfolio, cost-competitiveness, feedstock flexibility and product placement capabilities will continue to help the firm generate cash flow in a tough environment. The company has disclosed that the due-diligence by Saudi Aramco for the planned investment in the O2C business is on track and both the parties are committed and actively engaged. We believe that in a highly oversupplied market of crude, one of the best assets in refinery becomes the first choice for the companies like Saudi Aramco. We will be watching the development on the deal very closely, which may have a material impact on sentiments in short to medium term.

As per company disclosures, the growth engine for Reliance Industries in the future remains the consumer businesses; Jio and Reliance Retail, and both the segments continue to strengthen their leadership positions and recorded robust growth on all operating and financial parameters during the FY 2020.

Jio is now the largest network in India catering to 388 million subscribers and facilitating highest data usage in the world. Impact of tariff hike undertaken in December will continue to flow in the coming quarters and the platform will benefit from trends like work from home. In a strategic move, Facebook Inc. entered into a binding agreement for an investment of Rs 43,574 crore for 9.99% stake in Jio before the end of FY 2020. As we write, there is news of private equity firm Silver Lake announcing an investment of Rs 5,656 crore in Jio Platform for 1.15% stake at a premium of 12.5% to the valuation given by Facebook. The latest deal values the Jio Platform at nearly Rs 4.9 Lakh crore.

Reliance Retail delivered yet another year of highest ever revenue and ebitda, and expanded at a rate much higher than the competition and industry, thereby increasing their market share. In Consumer Electronics, Reliance Digital continues to maintain its leadership position; Fashion and Lifestyle category delivered a credible performance despite the shutdown. Grocery category witnessed strong growth led by SMART and Reliance Fresh sales were driven by store expansion and like for like growth in existing stores.

During the last AGM, Reliance had put up an aggressive target to become net debt free by end of FY 2021 and they seem to be on the path towards deleveraging. The steps to deleverage include

- sharp reduction in capex,
- binding agreement with Brookfield to monetize tower InvIT with total liabilities of ~Rs 42,400 Cr.,
- proposed investment of Rs 43,574 Cr by Facebook in Jio Platforms
- equity offering of Rs 53,125 Cr. and
- stake sale to Silver Lake for Rs 5,656 Cr.

The proposed transactions are expected to be complete during1QFY2021, subject to statutory approvals. The Company seems to be on track to meet its target of being net debt free by end of the current financial year.

We believe that Reliance should be looked at like a sum of the parts business. Some of the announcement(s) of private market deals have provided some sense of the valuation benchmark. The Aramco deal may value the core O2C business at $75 billion (~Rs 900 per share) and Silver Lake investment values Jio Platform at $68 Billion (~Rs 800 per share). The total net debt disclosed by company at ~$21 billion (~Rs 250 per share) means the current market price of ~Rs 1,435 is ignoring any value for the retail business and other investments of Reliance Industries. This provides enough margin of safety to the investors in the largest company in India and can provide further room for price appreciation should the deleverage get delivered on time.

Plutus Legacy allows the investor to hold a portfolio of the best companies in India in their demat with no complicated paperwork required at a fee that is less than what an equity mutual fund charges even for direct plan subscriptions. Please do let us know if you are interested to learn more about Plutus Legacy or any of our other investment offerings.

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