1. Fund Managers Commentary

The Girik Multicap Growth Equity Strategy is inspired by the CANSLIM philosophy of stock picking developed by American investor William J. O'Neil. The goal of this strategy is to identify leading companies from leading industry groups that show sharp acceleration in earnings, newness in products or change in management and suggests buying them at the right price with enough margin of safety ahead of the company's major stock price advance.

The markets across the world continued to be in a corrective mode during the month weighed down by geopolitical tensions. The resulting spiralling up of already high commodity prices will make the job of the Fed even tougher as it starts to fight record-breaking inflation across the board. Too little action and the inflation remains out of control but too much action and the economy might tip into recession! Local markets largely followed the global markets in the correction. The broader market indices underperformed the headline indices, giving away some of the gains from the rally of the last 2 years.

The industry leadership got a lot narrower, dominated by metals, industrial goods and power. The textile and sugar sector took a little breather while IT completely fell off the leadership charts. As the markets are witnessing a pullback from its unabated run of the past two years, portfolios are now being realigned to the new reality. Such realignment always causes churn in the portfolio. Generally, a portfolio churn is looked at with a skeptical lens as too much churn can destroy portfolio returns. However, not all churn is bad. When things change materially, a portfolio needs to be aligned to reflect the new circumstances. Some churn therefore becomes necessary to manage portfolio risk, reduce opportunity cost and boost portfolio returns.

Let's address the risk management and opportunity cost perspective of the churn today.

In investing, you would be wrong half the time and most of your performance will come from a handful of bets while the other bets, especially the losing ones, will act as some kind of a drag. If you are fearful of the churn and let the draggers be, you will be at the risk of immensely diluting the portfolio returns. Worth mentioning here, there will be other opportunities that you would end up missing while looking after the duds in the portfolio. Worst case, you may end up averaging the duds, which will be akin to watering the weeds and ignoring the flowers. Even if you continue holding the bets that are not loss-making but refuse to perform for long periods, you would risk losing on newer opportunities that could have added to your portfolio returns.

Now imagine what would happen when we proactively kill the draggers and find enough performers for the portfolio. This will not only protect the portfolio downside but also increase the probability of getting on big winners that would have otherwise passed by.

To be fair, most portfolio managers understand the issue at hand and work on it in their own different ways. The problem however is that most of the workarounds are subjective and specific to the managers. Some have a low tolerance for duds and they cut their losers and non-performers proactively, while others take a more patient view and end up sacrificing returns. The best way to ensure the positive outcome of a churn is to have certain exit rules for non-performing stocks. The exit rules should be designed in a way that does not choke your investing bets and gives them enough time and room to perform. If you are fearful of the stock's comeback, design specific rules to re-enter if it fulfils a predetermined criterion. This will help keep the human ego at bay and ensure objective rule-based investing.

At Girik, we have limited tolerance for draggers, which is why we have reasonable exit rules in place that we keep bettering. These rules contain a mix of technical and fundamental parameters that come together to give exit signals. This process also helps create liquidity that we can use to pursue newer ideas that our screeners throw up. As a result of following the carefully crafted process, we churn our portfolios as systematically as possible to ensure a constructive outcome.