RIGHT HORIZONS **Risks Foreseen by The Portfolio Manager** -April'20

1. Equity Portfolios: IBL Portfolio, Flexi Cap Portfolio & Super Value Portfolio

Global Risks:

- Unprecedented volatility amid the Corona virus outbreak and oil-market conflict can have significant impact on both equity and debt markets. Such an outbreak, with its rapid spread is unprecedented and thus can have a significant impact on market sentiments.
- With shutdowns on a global scale, and with restrictions on travel/transportation, supply chains will be adversely impacted for many manufacturing companies.
- Earnings forecasts and market outlook can swing widely in coming months as emotions (fear) have taken over the fundamentals
- While it is also too early to assess the full-blown economic impact of lock-down, as one is unable to accurately predict when the infections peak, there is a good chance of a recessionary situation emerging in Europe and America over the next two quarters.
- Also, it might be possible that the stimulus package passed by Governments is not enough; and an additional stimulus could highly burden the Governments with debt.
- While central banks have gone for a coordinated monetary policy easing and now that G7 central banks have set a policy rate around zero, it does not leave them much room to handle a prolonged slowdown or another black swan event in near future.
- Demand contraction due to lock down, job losses and disruption in supply chain has already impacted consumption trends and has impacted manufacturing activities, further shocks due to pandemic can prolong the risks to consumer demand.
- Slowdown of growth in the US, Europe and China is going to hurt the overall Emerging Markets that are exporting either commodities or goods to these geographies
- Capital outflows during pandemic will pose another challenge for emerging economies, due to a flight to safety.
- Crude prices have already plummeted more than 45% in March amid price war between Russia and Saudi Arabia, and declining oil revenues for OPEC countries can lead to an unparalleled balance-of-payment crisis for oil exporting countries.
- The political risk has also heightened in the last one month, especially between US and China.

Domestic Risks:

- Corona virus related risk factors listed above would hold true for India as well. Extensions of the lockdown can adversely impact the economic scenario in India and the corporate earnings in coming quarters.
- Stimulus package announced by the government and RBI can adversely impact the fiscal deficit for the year
- Any FII/FPI outflows can continue to put pressure on domestic markets
- Midcap and Small-cap stocks normally face higher volatility as compared to large-cap peers when negative events materialize. Continued polarisation in the market will lead to wealth erosion from mid & small-cap companies.
- Weak nominal GDP growth forecast for FY21 could drive further tightening of credit conditions and stress upon Banking and NBFCs
- Recently observed Corporate Governance concerns from NBFCs and Banks can create further stress in Financials
- Weakness in credit from non-bank financial companies is expected to linger resulting in the business slowdown
- Corporate Earnings and Government policies will be a major influencer for equity portfolio performance.
- Government missing on its year-end fiscal deficit targets can impact the country's credit rating and can be viewed negatively by institutional investors
- The weak fiscal position can impact government spending and investment on infrastructure, much needed to boost the economy
- The government's future income will depend a lot on divestment, spectrum sales and dividends leading to instability to the fiscal framework. Lower tax collections can further deteriorate the country's rating and investment suitability for foreign investors

2. Debt Portfolios: Capital Protection Portfolio, Fixed Income Portfolio

- Moratorium to borrowers could create an ALM mismatch for some companies adding further pressure on yields.
- Also, the reported asset quality by banks may not reflect the true picture due to moratorium provided to borrowers.
- During this period of demand tightening, there is a cause for concern on leveraged companies and leveraged promoter-groups, that could increase defaults. NBFCs would also face pressure on their asset quality and their yields could go up.
- The flight to safety on the back of the closure of debt schemes by Templeton could further result in a spike of yields of lower rated papers and also impact the liquidity of these papers further. The redemption pressure on lower rated debt schemes further puts pressure on debt fund managers. The global environment can also lead to increased redemption pressure from FIIs.
- Bond market risks seeing a spike in case RBI don't go for bond buying operations of lower rated securities.
- Low volumes can further lead to large swings in the bond market and increase risks for a credit freeze
- Yields offered by the overnight lending market has plummeted as funds and corporate treasuries have moved into cash
- Given our fiscal deficits and debt monetisation, rupee is expected to be volatile which will put pressure on forex reserves
- Further rate cut and ongoing withdrawals from equity and debt markets by overseas portfolio managers may lead to a continued rupee depreciation. Currency depreciation could impact India's already stressed fiscal deficit by making imports more expensive.
- Long duration, dynamic and guilt funds can see relatively higher volatility in returns going forward

3. Balanced Portfolio Portfolios: Alliance and All-Seasons Portfolio

- This portfolio would be impacted by both debt and equity market risks as outlined above to the extent of the debt: equity composition.
- Alliance Portfolio also has inherent model risk wherein portfolio needs to be rebalanced periodically.
- Gold prices can also be impacted by developments including demand in India and global demand.
- Gold prices may also be impacted by change in risk appetite of investors; especially if global economic conditions improve.

4. Multi Asset Portfolio: Mix of Equity, Debt, MFs, Bonds, and Gold ETFs

- This portfolio would be impacted by both debt, equity and gold related market risks as outlined above to the extent of the asset allocation in client's portfolios

5. Yield Multiplier Portfolio: Unlisted Debt

- Unlisted debt securities could be exposed to the risk of default in challenging economic conditions. This risk is higher than listed debt and rated debt instruments
- Various large-scale defaults and frauds that we have seen recently can cause the further tightening of liquidity for the developers.
- Default from DHFL and other realty players have already stressed the liquidity in the sector. Going forward, if payment is not received from issuer, selling projects to third party can result in significant haircut for lenders.
- Regulatory changes can impact the sector adversely over short to medium term.
- Governmental approvals and interventions are higher for this sector. This could result in delays and possible defaults.

CONTACT US*:*
Anil Rego *anilrego@righthorizons.com*
Rachna Rego *rachna@righthorizons.com*
Right Horizons Financial Services Pvt Ltd.
No 6, Arekere, II Main,
Bannerghatta Road,
Bangalore – 560076
Tel: +91-80-65687503 to 65687518 [Bangalore]