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"THE THREAT OF DISRUPTION FOR INVESTMENT ADVISORY- PART 2 "

History can teach us a lot of things. Historian Yuval Harari, in his book Homo Deus, describes the three important agendas that have kept the humans busy for past the few millennia.

For thousands of years, writes Harari, "the same three problems preoccupied the people of twentieth-century China, of medieval India and of ancient Egypt. Famine, plague and war were always at the top of the list. Generation after generation humans continued to die in their millions from starvation, epidemics and violence."

Sample this:

In France between 1692 and 1694, famine killed 15 percent of the population (that's about 2.5 million people). The infamous Black Death pandemic killed between 75 and 200 million in Eurasia in the 1330s. And in ancient agricultural societies, human violence caused about 15 percent of all deaths.

By the end of the 20th century, humans had tamed these three problems to a large extent. In today's world, more people die from old age than from infectious diseases; and more people commit suicide than are killed by soldiers, terrorists, and criminals combined.

So what projects will replace famine, plague, and war at the top of the human agenda in the twenty-first century? Harari speculates that humanity's next targets are likely to be immortality, happiness, and divinity.

"Having reduced mortality from starvation, disease and violence, we will now aim to overcome old age and even death itself. Having saved people from abject misery, we will now aim to make them positively happy. And having raised humanity above the beastly level of survival struggles, we will now aim to upgrade humans into gods, and turn Homo sapiens into Homo Deus."

That's a tall order and sounds a little too ambitious. Doesn't it?

The giant strides that technological advancements have offered to humankind in the last few decades has turned the impossible into inevitable.

Technology is the common thread between all these new frontiers that humankind is aiming for. An unintended consequence of these technological disruptions is the threat of people losing their jobs. In the past few decades, in the US the share of agricultural jobs have gone from 40% to just 2%. The manufacturing jobs have gone from 60% to merely 10% today. Automation, computers, and robots have replaced human labour. Will robots take all our jobs and people will live on universal basic income?

Today, the threat of job loss extends to almost every field of human endeavour including the business of investing and investment advisory. So the question I want to investigate today is this — will you need an investment advisor tomorrow or will it also be outsourced to Artificial Intelligence? I had written about this theme in the last newsletter but this time I want to highlight a different nuance of this topic.

But before we get into that, let's acknowledge the three breakthroughs that technology has brought about for small investors.

Until a few years back, the availability of information was restricted to those who had deep pockets, i.e., large institutional investors. Thanks to the internet, that informational edge has largely been democratized. With the advent of zero brokerage and very low-cost mutual funds, the cost of transacting in equities has raced to the bottom. That's good for the investors. And finally, with the digitization of stock market exchanges, the transparency has gone up many fold. An investor doesn't have to worry when he would receive the delivery of his equity shares or if those shares are genuine. This increased trust between the stock market and small investors has brought in more and more people to stock markets.

So what is next on the agenda for the technology as far as investing is concerned? Some pundits speculate that protecting the investor from the pitfalls of his own behaviour is going to be the next problem that technology will solve. Let me explain.

With the three challenges — information, trust, and cost — out of the equation the only thing that can bring down the returns of an investor is his own behaviour. Knowing that markets swing between excessive greed and extreme fear is one thing and turning it into an advantage is another. Statistically, a big chunk of those who directly invest in the stock market ends up losing money. That's because most investors aren't emotionally ready to deal with the vicissitudes of the markets. Plus, it's hard for them to acknowledge it.

Professional investors who do well over the long term don't just have the right skills but they're also mentally wired in a way that gives them an edge against others who are unaware of the role emotions play in investment decisions.

I argued in my post titled The Rise of Investing Centaurs that the professional money managers who would be willing to embrace the technological advancements selectively will do better than others. However, the same technology will probably run into a dead end when it comes to helping the common investor directly. The inability of the majority of small investors to accept and appreciate the role of human behaviour in investing decision makes it hard for artificial intelligence to democratize above-average investment returns.

You might argue that our views are biased because SSIAS is in the business of investment advisory and we don't want our bread and butter to be disrupted by technology. Perhaps yes. But are we in a denial mode like an ostrich hiding its head under the sand? Definitely no. We strongly believe that investment advisors will continue to be relevant and even more useful for those investors who want to beat the markets and don't have the skills to study the markets.

The daily tasks of an investment advisor may change a lot but the fundamental role that an advisor plays for an investor — to assist in protecting the capital and growing it at an adequate rate — will not be disrupted by technology.

~ Anshul Khare ~

SSS MODEL PORTFOLIO PERFORMANCE

As per Anshul's above ideas, we at SSIAS always keep in mind our fundamental role of protecting your capital and growing it adequately. This is why we write to you on a quarterly basis and communicate our thoughts and investment philosophy. While we write to you, we not only present our performance but also internalize as to what has worked and what has not. Hence, the whole process of writing to you actually helps us in improving our investment thesis. Please find below the performance of SSIAS model portfolio against major market indices.

PERFORMANCE OF SSS AS AGAINST MAJOR INDICES (Starting from 01.08.2017)				
PARTICULARS	**31.12.2017**	**30.06.2018**	**31.12.2018**	**31.03.2019**
Nifty 50	4.11%	5.88%	7.39%	14.92%
S&P BSE Midcap	15.29%	-0.10%	-0.21%	0.09%
S&P BSE Smallcap	19.63%	-0.26%	-8.41%	-6.49%
SSIAS Model Portfolio	**16.71%**	**-0.26%**	**4.53%**	**5.19%**

If we look at SSIAS performance and compare it with NIFTY 50, BSE Midcap and BSE Smallcap indicies, we find that as on 31.03.2019, SSIAS model portfolio has outperformed the smallcap and midcap index with a fair margin. However, we have significantly underperformed the NIFTY 50. Why did this happen?

We analyzed the NIFTY 50 performance and found something interesting. While the NIFTY 50 has generated a 14.92% return in the period, we would like you to have a look at the table below.

Top Nifty Contributors	**Weight in Nifty**	**Return**	**Weighted contribution**
Reliance Industries	9.98%	71.02%	7.09%
HDFC Bank	10.67%	30.35%	3.24%
Infosys Ltd	6.04%	49.10%	2.97%
TCS	4.50%	61.03%	2.75%
ICICI Bank	5.52%	31.08%	1.72%
Axis Bank	3.25%	48.54%	1.58%
Kotak Mahindra Bank	3.81%	31.92%	1.22%
HDFC	6.94%	10.25%	0.71%
L&T	3.66%	19.29%	0.71%
ITC	5.45%	1.71%	0.09%
Return contribution in Nifty 50			**22.06%**

Please take note of the following points to understand the above table better:

1. Return is for the period starting from 01.08.2017 up to 31.03.2019.

2. Weighted contribution are indicative and not exact as the exact weights of each stock in the nifty gets changed every day. For keeping things simple we have taken the weight of the above stocks in NIFTY as on 31.03.2019.

If we take the weighted contribution of the top three stocks- Reliance, HDFC Bank and Infosys, they contribute to almost the entire return of NIFTY during the above period. This means that the remaining 47 stocks of the NIFTY put together has contributed nearly nothing to the performance of the NIFTY 50.

This clearly shows the polarized nature of the NIFTY performance. While we are no good at forecasting how the market will behave in the near term, we believe this lopsided performance cannot carry on for long. So, some sort of index re-balancing is due.

Either the NIFTY non-performers will catch up on valuation.

Or the high performing stocks in the NIFTY will lose their steam.

One of the above would surely happen. We don't know which one. Or maybe, we can have a combination of both.

The polarization, which we see now, cannot last for long. Hence, we shall not lose our sleep on the basis of NIFTY returns for the last one year and focus more on identifying the right businesses at right valuation and sticking to our investment philosophy. The price will eventually follow the earnings of the companies we are invested in.

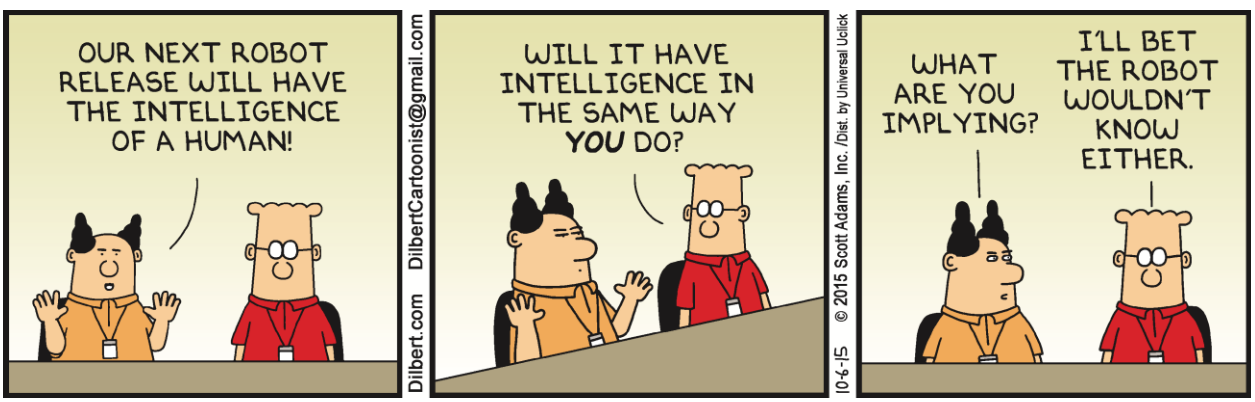
In our last newsletter we said this:

"In the long run, all portfolios reflect the sum total earning power of all the companies in it. Hence, we don't get swayed by the temporary and excessive rise and fall of prices of securities."

We continue to stand by that. We also believe that while we cannot control the movement of market, we can control our own behavior. Writing to you on a regular basis helps us in doing that.

SIGNING OFF

While we are on the verge of concluding this edition of SSIAS quarterly, we cannot avoid thinking about the threat of artificial intelligence for Investment Advisors about which Anshul has penned his thoughts in the beginning. We do not know for sure how AI will change the investing world five or ten years from now.



However, we know ourselves.

We know what we can do and what we cannot.

And we know that we can adapt.

And we know that we can regularly communicate to you about our evolution as investment advisors as the investing landscape changes with technological disruption.

And finally, we know that you will continue to trust us.

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