The right analyst for the job

AIE's extensive analyst expertise has helped deliver strong outperformance for the trust...

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At the end of September, just under 40% of the **Ashoka India Equity (AIE)** portfolio was invested in small caps. That was almost four times the weighting the sector has in the trust's benchmark, the MSCI India IMI Index.

In part that is a sign of just how broad the opportunity set is in India for investors. More than 5,000 companies are listed on the main exchanges in the country. In contrast, the London Stock Exchange has fewer than 2,000 companies trading on it today.

Those companies are also spread fairly evenly across a wide range of sectors, so this is not a case of firms being highly concentrated in a few areas. For example, at the end of September, financials – with a 24.8% weighting – was the only sector that made up more than 12% of the MSCI India IMI's total market cap.

There are a couple of positives that result from this. One is that the Indian market has both breadth and depth – there are a lot companies to invest in and they are spread across a range of industries.

The other is that it means there is more opportunity for active investors to gain an informational advantage. The sheer number of companies means India, a market that already receives less coverage than developed markets, is hard for analysts to produce comprehensive coverage on.

Moreover, the wide range of industries present in the country's stock market means that having sectoral specialists can provide another source of alpha generation for fund managers.

This is more than just theoretical. A comprehensive study carried out by the Wall Street Journal in 2019 found that India was the market where active fund managers delivered the highest level of average outperformance / underperformance over five and ten year periods.

Managers investing in India also had the highest consistency level, meaning the largest proportion of top performers in the first five-year period the WSJ looked at were also top performers in the subsequent five-year period as well.

AIE is arguably a more recent example of this dynamic. Since its IPO in 2018, the trust has been the top performing investment trust focused on India. At the end of September 2023, the trust had delivered NAV annualised total returns of 17.3%. This was 6.13% ahead of the equivalent returns produced by the trust's benchmark.

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The trust's success is arguably the result of its strong, on the ground research team. AIE has the largest India-focused analyst team in the investment trust specialist space, with close to 30 analysts covering the country. Most of the team are based in country, with a small number in Singapore.

Having such a large analyst team means that the AIE managers are better equipped to screen and analyse the huge number of companies that are listed in India. This goes some way in explaining the large overweight position the trust has to small caps today, as these often have no analyst coverage at all.

Aside from this, one of the core components of the AIE investment process is a focus on corporate governance. A key part of this means that the AIE analyst team typically carry out several thousand company meetings every year. This process has paid off, with the trust avoiding several company blow ups that have impacted the wider market since IPO in 2018.

Another strength of the team is its sector-specific expertise. For example, healthcare constituted 11.3% of the AIE portfolio at the end of September, an overweight position compared to the 6.2% weighting the sector has in the MSCI India IMI Index. Those investments have been supported by specialists in the analyst team, who have both strong experience working in the industry itself but also a long track record as analysts investing in the sector.

To top all of this off, AIE is unique in the investment trust sector as it does not receive a management fee. Instead the trust receives a 30% performance fee over three year periods.

This also filters down to the analyst team, who are rewarded for making good stock picks. They are also paid in shares with three-year lock in periods for half of them, meaning they are incentivised to deliver long-term outperformance for shareholders, rather than just benefitting from any short-term blips in the market.

Taken as a whole, this means that AIE has a strong analyst team, operating in a market where there is arguably greater opportunity to generate alpha, compared to more developed economies. At the same time, that team is strongly incentivised to deliver long-term returns for shareholders, with the management team arguably sharing in some of the downside if they fail to outperform by receiving no fees at all.

So far it's a process that has worked. As noted, AIE has delivered impressive long-term outperformance since its IPO in 2018. Although there are no guarantees that will continue, as long as the Indian stock market remains poorly researched, AIE's strong analyst team is a clear asset.

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