

**There has been a significant chatter and excitement amongst the investors of small cap companies post a circular released by SEBI yesterday.** The implications of the same are still being debated upon but there is an expectation of about 25-35 thousand crores of money that can flow into small cap companies and move away from large caps. Though such actions by SEBI cripple the freedom of fund managers and creates arbitrary spikes and we aren't a fan of such moves by SEBI, but we can't deny the fact that the funds managed under our advisory benefit hugely by this move as we always have chosen to run a small cap oriented strategy even after headwinds emerging post SEBI's circular in 2017.

While, one may argue that the tailwind experienced by this move is only for the medium term over which the readjustment happens, but we believe it's another setback for the sector which is already experiencing multiple tailwinds off late due to several factors like low interest rates (borrowing costs), low crude oil (raw material costs), low wage growth and a stable rupee. Small caps had already been outperforming their large cap peers in the past 5-6 months due to these factors. Although we don't base our investments on such technical events but this is a windfall opportunity that we will take in with open arms.

While the situation sounds very exciting for small cap investors, one should take cognizance of the risks that the mutual fund industry might try to get some relaxations or try to circumvent the regulation itself by changing category of their funds which we have discussed later.

### **Let's understand the circular and its implications in detail.**

In a circular released on 11<sup>th</sup> September 2020 by SEBI, they issued guidelines regarding categorization and rationalization of multi-cap mutual fund schemes. Now, multi cap schemes must invest at least 25% of their portfolios in large, mid and small caps each.

### **New guidelines of SEBI –**

Minimum investment in equity & equity related instruments - 75% of total assets in the following manner:

- Minimum investment in equity & equity related instruments of large cap companies - 25% of total assets
- Minimum investment in equity & equity related instruments of mid cap companies - 25% of total assets
- Minimum investment in equity & equity related instruments of small cap companies - 25% of total assets.

**Time limit for compliance** – All the multi-cap funds shall ensure compliance with the above provisions within one month from the date of publishing next list of stocks by AMFI in Jan, 2021.

**Classification of Large, Mid and Small cap stocks** - Large-cap stocks are defined as the largest 100 stocks by market capitalization, mid-caps as the next largest 150 stocks and small-caps are all the stocks below the top 250 in size.

**Classification according to list of stocks published by AMFI in June, 2020**

Category	Range (6 month Avg Total Market Cap)
<b>Large Cap</b>	Market Cap Above – 26,667 Crore
<b>Mid Cap</b>	Market Cap in range of 6,955 - 26,594 Crore
<b>Small Cap</b>	Market Cap below 6,955 Crore

**How will it affect equity markets?** Multi-cap funds have total assets under management of around Rs. 1.5 lakh crore. Currently, on average top 10 multi-cap schemes have allocation of around 7% in small cap equities and 17% in mid cap equities. Hence, for realignment to the new guidelines, such funds can shift Rs. 36,000 cr from large cap to small and mid cap equities.

Flow of 36,000 crore is huge for mid and small cap stocks, especially for small cap where the flows expected are Rs. 27000 crore and the companies have very shallow liquidity. In the short term, lack of liquidity in small and mid cap stocks can give huge upside.

Scheme Name (Top 10 multi cap Schemes)	AUM (Rs in Cr)	Mid cap Holding (%)	Small cap Holding (%)	Mid Cap Buying (Rs in Cr)	Small Cap Buying (Rs in Cr)
<b>Kotak Standard Multicap Fund</b>	29714.07	22.5%	1.5%	743	6974
<b>HDFC Equity Fund</b>	19797.98	8.4%	3.9%	3290	4171
<b>Motilal Oswal Multicap 35 Fund</b>	11239.87	10.1%	4.7%	1678	2286
<b>Aditya Birla Sun Life Equity Fund</b>	11023.35	23.9%	6.5%	117	2044
<b>UTI Equity Fund</b>	10982.95	35.7%	8.2%	-1170	1850
<b>SBI Magnum MultiCap Fund</b>	9063.31	10.7%	11.7%	1297	1204
<b>Franklin India Equity Fund</b>	8591.33	11.1%	7.0%	1198	1549
<b>Nippon India Multicap Fund</b>	8053.29	27.8%	16.7%	-223	671
<b>Axis Multicap Fund</b>	6434.07	7.0%	0.8%	1156	1554
<b>ICICI Prudential Multicap Fund</b>	5593.74	11.8%	11.1%	740	778
<b>Total of All Listed Multi Cap Schemes</b>				<b>10291</b>	<b>27122</b>

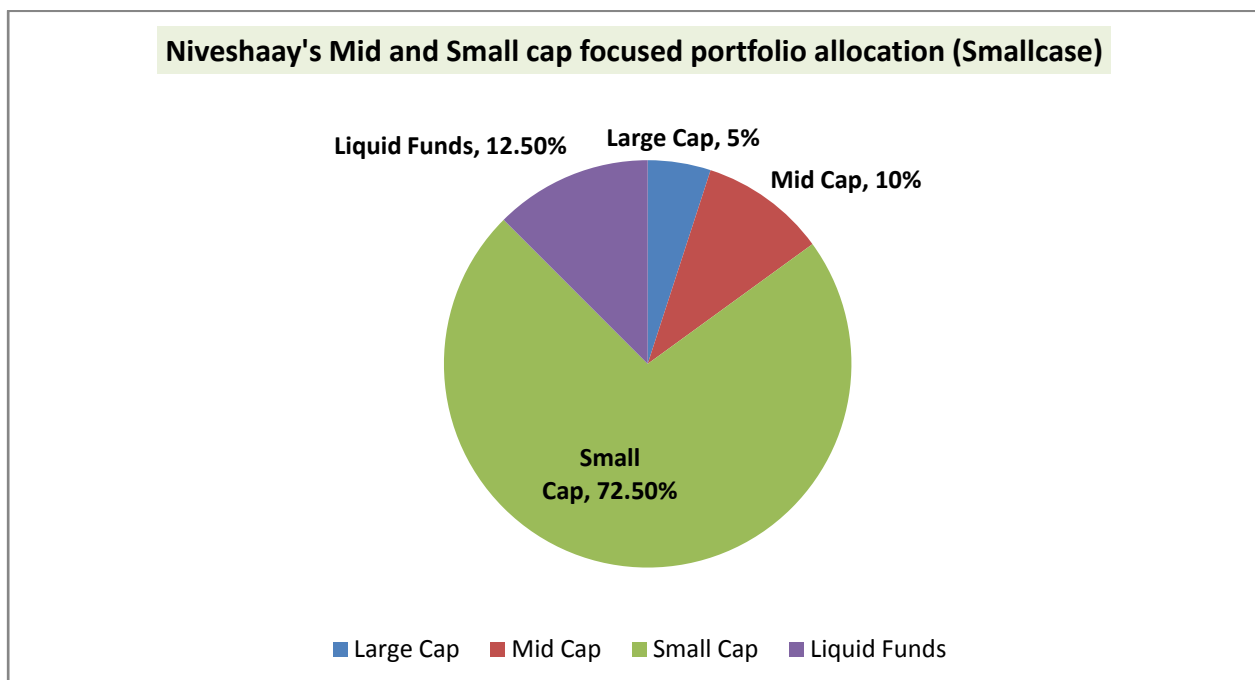
**How will mutual funds comply with these regulations? 3-4 different scenarios can emerge -**

1. Intra change in same funds – First, all mutual funds will try to adjust allocation by intra change adjustments in different schemes of the same mutual fund house. E.g. If they have larger allocation in mid and small caps in other schemes, they will try to do intra scheme adjustments.
2. Time Demand – Mutual funds can demand time flexibility from SEBI.
3. Change in scheme objective – Mutual funds can apply for change in objective of the scheme.
4. Request for a smaller allocation to small caps in the range of 10-15%

**Niveshaay’s Smallcase Portfolio** - In this portfolio, we have covered small and mid cap stocks which are available at reasonable valuations and have huge earning potential upside.


To know more about the strategy you can watch video on following link  
[https://www.youtube.com/watch?time\\_continue=7&v=ut-dB\\_bAWSo&feature=emb\\_logo](https://www.youtube.com/watch?time_continue=7&v=ut-dB_bAWSo&feature=emb_logo)

**Niveshaay’s Smallcase Mid and Small cap focused portfolio allocation** – Our smallcase portfolio is focused on mid cap and small cap stocks only. 72.5% of our total portfolio is invested in quality small cap equities only.



**Subscription Plans** – We are celebrating September as our launch month on the Smallcase platform. We are giving a 40% discount on our 1 year Smallcase subscription plan in the month of September.

**simple pricing for everyone**

	1 MONTH	3 MONTHS	6 MONTHS	12 MONTHS
 Mid and Small Cap Focused ...	—	₹ 1,999	₹ 3,499	₹ 2,999 <del>₹ 4,999</del>

**About Niveshaay** - Niveshaay is a SEBI Registered Investment Advisory Firm with a Dedicated Research Team specializing in unearthing high quality undervalued stocks. We focus on few high conviction stocks that exhibit chances to outperform and have out sized impact on the portfolio.

**SEBI Registration No. INA000008552**