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NEWSLETTER

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ANKIT KANODIA

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❖ "THE THREAT OF DISRUPTION FOR INVESTMENT ADVISORY"

Marc Andreessen, founder of the first internet browser Netscape and now a billionaire venture capitalist, wrote an essay in 2011 titled "Software is eating the World." He argued that in the next few decades there wouldn't be any industry that will not be disrupted by software. His claim is unsettling and undeniable.

Since the onset of scientific revolution in 14th century, humans have harboured the dread of a future when machines will take over the reins. And many recent events have fueled that anxiety. In 1997, IBM's Deep Blue supercomputer defeated world chess champion Garry Kasparov. Then, in 2015, Google's DeepMind AlphaGo defeated the world's number one Go player.

Google's driverless car project WayMo is already operational on US roads. In spite of the threat of millions of human-drivers becoming unemployed, the promise of reducing road fatalities by 90% has made proliferation of autonomous cars inevitable.

In the medical industry, computer-powered robots have been performing complicated surgeries for quite some time. And now, IBM's Watson is outsmarting experienced doctors in making the diagnosis.

The rise of artificial intelligence is increasingly encroaching human activities. So what does this mean for the financial services industry?

The financial services industry has been visibly transformed by software over the last 30 years, wrote Andreessen. "Practically every financial transaction, from someone buying a cup of coffee to someone trading a trillion dollars of credit default derivatives, is done in software. And many of the leading innovators in financial services are software companies."

Today, an investor can start investing in mutual funds within a few minutes with an amount as low as Rs. 100. A whole gamut of intermediaries including brokers and agents have already been made redundant by the technology. Not a week goes by without an announcement of a new startup raising funds to build platforms that will democratize the investing solutions for small investors.

Chatbots have already started replacing a large part of the customer support teams across the industries. Will chatbots replace your investment advisor too? Will fund management industry be disrupted like digital cameras disrupted Kodak?

Investment advisory is a profession tightly coupled with human expectations from two directions. First, finding investment opportunities in businesses run by humans. Second, the source of investment capital is again from humans, i.e., clients who entrust their money with the investment advisors. And at the intersection of humans and money, you'd find strong emotions — fear, envy, greed.

How will an artificial intelligence algorithm wrap its head (or rather bytes) around the unpredictability arising out of irrational human behaviour? Sure, the computer algorithm can detect patterns and raise flags but taking the final call whether to accept or reject that flag will require human intervention.

The software is indeed eating the world including the finance industry. But when it comes to investing, technology would rather augment than disrupt.

There certainly will be a class of money managers and investors who would continue to see the computers as competitors rather than collaborators. As a result, those who choose to compete head-on will be disrupted. But there would be another group who would be intelligent enough to learn to collaborate with the technology. They will know when to trust the insights spit out by an algorithm and when not to leave it to the computer.

There's another aspect of professional money management where modern automations can't match the human talent. Communication.

Investing is not the study of finance. It's the study of how people behave with money. And the gap between what people know and what they eventually do could be miles wide.

The secret to long-term superior performance of an investment manager isn't always tied to his stock-picking skills. If his clients pull out the money at the wrong time, there isn't much he can do. Which means a more important factor in determining the long-term success of a money manager is the quality of the clients he attracts. And how does one attract the right clients? By being good at

communicating his investment philosophy and setting the right expectations. I am not sure how well artificial intelligence can do that job.

This is why, we at SSIAS, communicate to our clients about our investment rationale, whenever we take an investment decision. We share our investment philosophy and performance with our clients on a regular basis. In the next section we share our performance as

SSS MODEL PORTFOLIO PERFORMANCE

Let us have a look at the table below to see how our model portfolio has performed as against the major indices.

PERFORMANCE OF SSS AS AGAINST MAJOR INDICES (Starting from 01.08.2017)				
PARTICULARS	**31.12.2017**	**30.06.2018**	**30.09.2018**	**31.12.2018**
Nifty	4.11%	5.88%	8.10%	7.39%
S&P BSE Midcap	15.29%	-0.10%	-4.54%	-0.21%
S&P BSE Smallcap	19.63%	-0.26%	-10.21%	-8.41%
SSIAS Model Portfolio	**16.71%**	**-0.26%**	**1.95%**	**4.53%**

If we look closely, losses which were occurring on a quarterly basis were notional and not actual. We have booked profits of 20% in the 17 months of our operations. So the current portfolio status of 4.53% returns is after deducting the notional losses of around 15.47% from booked profit of 20%. Model portfolio returns were showing only 1.95% in the last quarter, but have increased to 4.53% as some of our holdings have shown resilience even in this volatile market.

We said this in our last quarterly newsletter:

"Whenever the market recovers we will see these notional losses getting erased."

We have already witnessed a glimpse of the same in this quarter. Our notional loss has come down and hence model portfolio returns have inched up.

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.

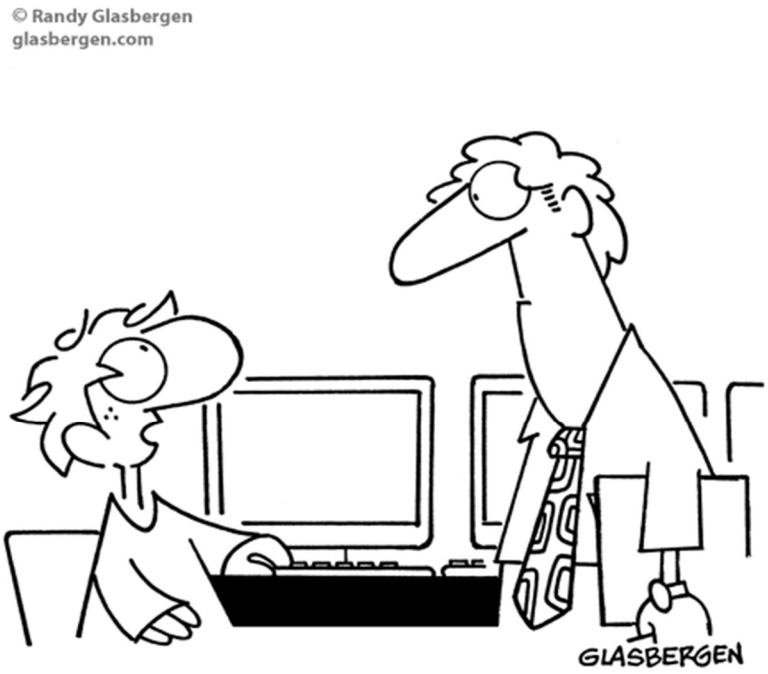
SIGNING OFF

We might not be so sure about artificial intelligence and its impact in varied fields, but we are very sure about human intelligence, its inspiration and aspiration to make the present of today better than the future of tomorrow. This trust in human cognitive capacity led us to collaborate with a deep thinker, a great writer, well respected expert of behavioral models in finance/ investment, technology savvy engineer from IIT Bombay (with good pedigree in working with some of the leading companies like PayTM, Symantec, Atul Ltd. etc.) and above all a great human being- All in One.

We welcome Anshul Khare as Team member of Smart Sync Services and Strategic Advisor to our parent company Synconic Solutions & Services Pvt. Ltd.

Periodically, we do review the stocks in our portfolio, but do not take action purely based on price-movements. We follow our investment rationale for each company and take decisions based on those rationales. The whole purpose of constantly communicating our investment philosophy with our clients is to set the right expectations.

An intelligent software, however robust, will eventually need our human touch to set that right expectation.



"I won't be impressed by technology in the classroom until you figure out how to install Google directly in my brain."

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