

Ideas @ Edelweiss Multi Strategy Funds – Short Selling – Part II



This is Part 2 of 2 where we discuss short selling. In last month's Ideas @ Edelweiss Multi Strategy Funds, we discussed the many challenges of short selling in India. In this month's piece we will discuss why this forgotten art is actually easy.

For one, the potential universe of stocks to short only covers those 163 names that are in the futures and options (F&O) segment. If you filter out well-run firms, you have a universe of only ~50 names to cover. In contrast, a portfolio manager on the long-side has to cover and track hundreds of ideas. The fear that stocks will rise to infinity is often unfounded because as Jim Chanos so eloquently put, there are many more stocks at 0 than there are at infinity. Especially in a country like India where we have a high cost of capital and a business environment that is ranked 142th in the world for entrepreneurs. The odds are stacked against companies succeeding. India is also home to some of the biggest corporate crooks - some of whom are widely acknowledged as being so.

From a pure investment perspective, India's high dispersion of stock prices and the abundance of long-only capital makes it an ideal hunting ground for short-ideas. Short-selling is a pure public game because management and the sell-side are often structurally bullish on the economy, their industry and especially on their company's prospects. In light of this, having timely, accurate and electronic disclosures are an asset to any short-seller.

Lastly, a forensic accounting approach to short-selling can also lead you to find asset bargains and/or turnarounds that are unconventional long ideas or expose flaws in existing long holdings. So even, if a short-selling strategy does not work out for all the reasons mentioned in last month's Ideas @ Edelweiss Multi Strategy Funds, it can add significant value in a portfolio context.

We expect that short-selling will become a meaningful part of savvy investor's portfolios in the year's to come either on a standalone basis or when commingled with other strategies as part of a long-short equity offering.