

Please refer our report
Dated 23 June 2017



Contrarian Investing: Consensus Upgrade Analysis

Stocks with ratings upgrade beyond a threshold deliver spectacular returns

Contrarian Investing is a time-tested investment tool, which involves buying/selling stocks against the prevailing sentiment of the crowd or the market. In our thematic report, **Contrarian Investing**, dated 22 June 2017, we had covered two major themes based on consensus ratings (stock popularity) and valuation multiples, and had demonstrated the success of contrarian investing in India. In the sequel, **Contrarian Investing: Digging Deeper**, we extended our work on valuation multiples by providing evidence that out-of-favor low P/CF stocks had outperformed in-favor high P/CF stocks over the last decade and that margin of outperformance was higher on trailing multiple than on forward multiple.

Contrarian investing focuses on buying stocks dumped into the bargain basement. Some of the contrarian strategies highlighted in our notes are:

1. Buying neutral-to-moderately-popular stocks (popularity based on consensus ratings)
2. Buying stocks with low relative valuation multiples (P/E, P/B, P/CF)
3. Buying stocks with consensus upgrade from “net sell to net buy”

In this note, we further analyze the last theme of Consensus Upgrade. We highlight that a simple strategy of investing in stocks wherein analyst consensus has changed from “net sell to net buy” can deliver returns of 22.4% over the next one year. **We address the general case of consensus upgrade and how stock prices react when a stock is upgraded.**

A strategy of investing in stocks that have been upgraded (threshold of 0.7), with a one-year holding period, has delivered phenomenal returns of 34% over 2006-18.

Consensus rating and consensus upgrade

Bloomberg collects analyst recommendations on each stock and assigns a consensus rating based on these recommendations. We have set a benchmark of increase of at least 0.7 in consensus ratings to be a case of upgrade, therefore focusing only on significant upgrades.

Performance of Consensus Upgrade stocks

Our analysis of BSE-100 constituents’ consensus rating data over 2006-18 (till date) suggests that a strategy of investing in stocks that have been upgraded by at least 0.7, with a holding period of one year, has delivered phenomenal returns of 34% over 2006-18.

A stock is upgraded when some of the analyst ratings change from ‘sell’ to ‘hold/buy’ or from ‘hold’ to ‘buy’. Earnings surprise, improvement in news flow and stock correction leading to attractive valuations can be some of the factors contributing to a stock’s upgrade on the street.

We found this strategy to be effective across the entire time horizon. The lowest returns delivered by the strategy across the time period were (-8%) in 2012 and 4.3% in 2008.

Hit ratio and evidence from India

Our analysis focuses on BSE100 current and past constituents over the last decade. Among consensus upgrade stocks, roughly 55% have outperformed the market, but as evident in 34% return annually, the margin of outperformance is significantly higher for winners. In YTD CY18, we did not find a single BSE100 stock that satisfies our criterion of upgrade (change in consensus rating score by at least 0.7).

Exhibit 1: Roughly 55% stocks in Consensus Upgrades outperform the market, but the margin of outperformance is significantly higher for winners

Year	Companies from "Consensus Upgrade" List outperforming Nifty	"Consensus Upgrades" in an year	% of Companies outperforming market	Key Upgrades
2006	13	32	41	❖ Castrol
2007	11	16	69	❖ Apollo Tyres, KotaK Mahindra Bank
2008	19	23	83	❖ Eicher Motors
2009	17	28	61	❖ IndusInd Bank
2010	11	21	52	❖ Titan
2011	7	13	54	❖ Nestle
2012	4	15	27	❖ United Spirits
2013	8	9	89	❖ Ranbaxy
2014	8	18	44	❖ Ashok Leyland
2015	12	17	71	❖ NIIT
2016	5	14	36	❖ Monsanto
2017	6	12	50	❖ Jindal Steel and Power
		Overall	55	

Source: MOSL, Bloomberg

Consensus Upgrade Stocks: 34% return over 2006-18

“Net Sell to Net Buy” theme is a particular case of Consensus Upgrade

In our thematic, [Contrarian Investing](#) published in June 2017, we looked at instances of change in consensus rating from ‘net sell’ to ‘net buy’ over 2006-2017 across BSE-100 constituents. A change in consensus rating from ‘net sell’ to ‘net buy’ means a change in consensus rating from <3 to >3. We found that a strategy of investing in stocks with consensus rating change from <3 (net sell) to >3 (net buy) generates significant alpha over the benchmark BSE-100.

This is essentially a particular case of consensus upgrade. In this note, we have addressed the general case of consensus upgrade and how stock prices react when a stock is upgraded. By consensus upgrade, we refer to the change in consensus rating (popularity) of the stock.

What is consensus rating?

Bloomberg collects analyst recommendations on each stock and assigns a consensus rating based on these recommendations. It assigns 5 points for every buy recommendation, 3 points for every hold recommendation and 1 point for every sell recommendation. A consensus rating is arrived at by taking the average of these scores.

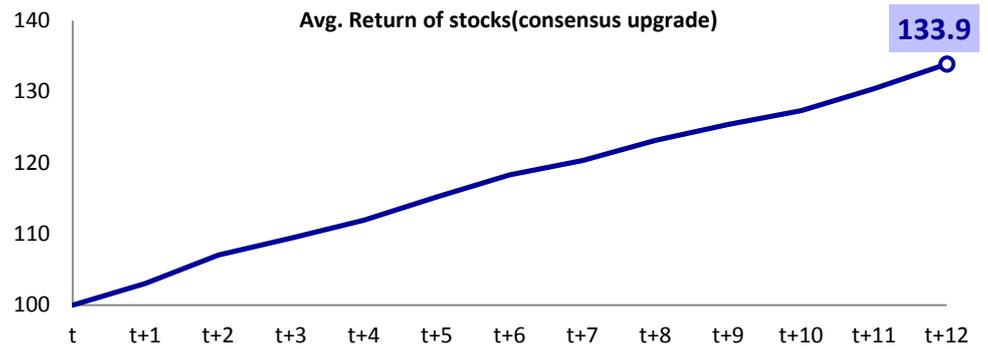
- A stock with a consensus rating of 5 would have all buy recommendations.
- A stock with a consensus rating of 3 would have an equal number of sell and buy recommendations, apart from hold/neutral recommendations.
- A stock with a rating change from <3 to >3 has a recommendation change from a net sell to a net buy.
- A stock with a consensus rating of 1 would have all sell recommendations.
- **We have set a benchmark of increase of 0.7 in consensus ratings to be a case of upgrade**, therefore focusing only on significant upgrades.

We looked at instances of consensus upgrades over **2006-18** across all BSE-100 constituents over the decade.

Our analysis of BSE-100 constituents’ consensus rating data over 2006-18 (till date) confirms our view. A stock is upgraded, when some of the analyst ratings change from ‘sell’ to ‘hold/buy’ or from ‘hold’ to ‘buy’. **A strategy of investing in stocks that have been upgraded by at least 0.7, with a holding period of one year, has delivered phenomenal returns of 34% over 2006-18.**

Earnings surprise, improvement in news flow, and stock correction leading to attractive valuations can be some of the factors contributing to a stock’s upgrade on the street.

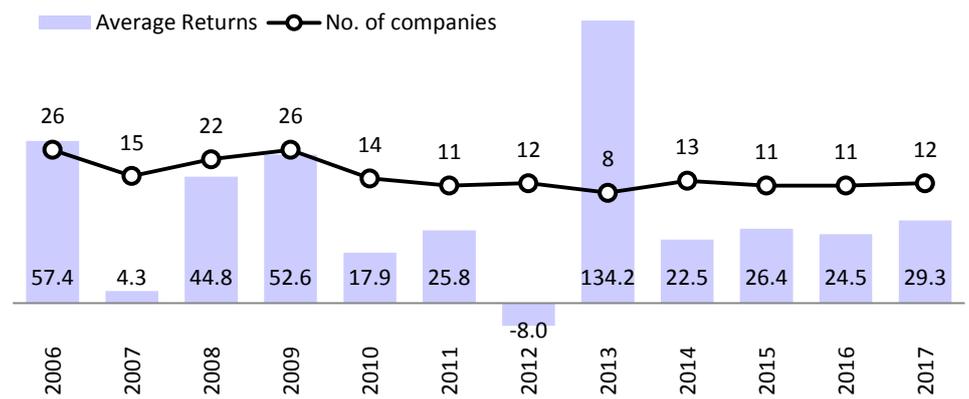
Exhibit 2: Indexed return over 12 months for Consensus Upgrade stocks



Constituents of BSE100 in past have also been included in analysis, Source: Bloomberg

We found this strategy to be effective across the entire time horizon. The lowest returns delivered by the strategy across the time period were -8% in 2012 and 4.3% in 2008.

Exhibit 3: Total returns for Consensus Upgrade Stocks have been significant across all years (2006-2018)



Source: MOSL, Bloomberg

Our analysis of consensus upgrade stocks suggests that roughly 55% of the stocks have outperformed the market, but as evident in 34% return annually, the margin of outperformance is significantly higher for winners. For 2018 YTD, there are no such stocks amongst the current BSE-100 constituents that satisfy our criterion.

Exhibit 4: Roughly 55% stocks in Consensus Upgrades outperform the market, but the margin of outperformance is significantly higher for winners

Year	Companies from "Consensus Upgrade" List outperforming Nifty	"Consensus Upgrades" in an year	% of Companies outperforming market	Key Upgrades
2006	13	32	41	❖ Castrol
2007	11	16	69	❖ Apollo Tyres, KotaK Mahindra Bank
2008	19	23	83	❖ Eicher Motors
2009	17	28	61	❖ IndusInd Bank
2010	11	21	52	❖ Titan
2011	7	13	54	❖ Nestle
2012	4	15	27	❖ United Spirits
2013	8	9	89	❖ Ranbaxy
2014	8	18	44	❖ Ashok Leyland
2015	12	17	71	❖ NIIT
2016	5	14	36	❖ Monsanto
2017	6	12	50	❖ Jindal Steel and Power
		Overall	55	

Source: MOSL, Bloomberg

Explanation of Investment Rating

Investment Rating

BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst becomes inconsistent with the investment rating legend, the Research Analyst shall within 28 days of the inconsistency, take appropriate measures to make the recommendation consistent with the investment rating legend.

Disclosures:

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

Motilal Oswal Securities Ltd. (MOSL) is a SEBI Registered Research Analyst having registration no. INH000000412. MOSL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Investment Advisory Services, Depository participant services & distribution of various financial products. MOSL is a subsidiary company of Motilal Oswal Financial Service Ltd. (MOFSL). MOFSL is a listed public company, the details in respect of which are available on www.motilaloswal.com. MOSL is registered with the Securities & Exchange Board of India (SEBI) and is a registered Trading Member with National Stock Exchange of India Ltd. (NSE) and Bombay Stock Exchange Limited (BSE), Metropolitan Stock Exchange Of India Ltd. (MSE) for its stock broking activities & is Depository participant with Central Depository Services Limited (CDSL) & National Securities Depository Limited (NSDL) and is member of Association of Mutual Funds of India (AMFI) for distribution of financial products. Details of associate entities of Motilal Oswal Securities Limited are available on the website at <http://onlinereports.motilaloswal.com/Dormant/documents/Associate%20Details.pdf>

Regulatory Enquiries against Motilal Oswal Securities Limited by SEBI:

SEBI pursuant to a complaint from client Shri C.R. Mohanraj alleging unauthorized trading, issued a letter dated 29th April 2014 to MOSL notifying appointment of an Adjudicating Officer as per SEBI regulations to hold inquiry and adjudge violation of SEBI Regulations; MOSL requested SEBI to provide all documents, records, investigation report relied upon by SEBI which were referred in Show Cause Notice. The matter is closed and MOSL had to pay Rs. 2 lakhs towards penalty for misplacement of original POA of client.

MOSL, its associates, Research Analyst or their relative may have any financial interest in the subject company. MOSL and/or its associates and/or Research Analyst may have beneficial ownership of 1% or more securities in the subject company at the end of the month immediately preceding the date of publication of the Research Report. MOSL and its associate company(ies), their directors and Research Analyst and their relatives may: (a) from time to time, have a long or short position in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.; however the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), or the recommendations made by the analyst(s) are completely independent of the views of the associates of MOSL even though there might exist an inherent conflict of interest in some of the stocks mentioned in the research report. Research Analyst may have served as director/officer, etc. in the subject company in the last 12 month period. MOSL and/or its associates may have received any compensation from the subject company in the past 12 months.

In the last 12 months period ending on the last day of the month immediately preceding the date of publication of this research report, MOSL or any of its associates may have:

- managed or co-managed public offering of securities from subject company of this research report,
- received compensation for investment banking or merchant banking or brokerage services from subject company of this research report,
- received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company of this research report.
- Subject Company may have been a client of MOSL or its associates during twelve months preceding the date of distribution of the research report.

MOSL and its associates have not received any compensation or other benefits from the subject company or third party in connection with the research report. To enhance transparency, MOSL has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report. MOSL and / or its affiliates do and seek to do business including investment banking with companies covered in its research reports. As a result, the recipients of this report should be aware that MOSL may have a potential conflict of interest that may affect the objectivity of this report. Compensation of Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

Terms & Conditions:

This report has been prepared by MOSL and is meant for sole use by the recipient and not for circulation. The report and information contained herein is strictly confidential and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of MOSL. The report is based on the facts, figures and information that are considered true, correct, reliable and accurate. The intent of this report is not recommendatory in nature. The information is obtained from publicly available media or other sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. The report is prepared solely for informational purpose and does not constitute an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments for the clients. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. MOSL will not treat recipients as customers by virtue of their receiving this report.

Analyst Certification

The views expressed in this research report accurately reflect the personal views of the analyst(s) about the subject securities or issues, and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations and views expressed by research analyst(s) in this report.

Disclosure of Interest Statement

- Analyst ownership of the stock

A graph of daily closing prices of securities is available at www.nseindia.com, www.bseindia.com. Research Analyst views on Subject Company may vary based on Fundamental research and Technical Research. Proprietary trading desk of MOSL or its associates maintains arm's length distance with Research Team as all the activities are segregated from MOSL research activity and therefore it can have an independent view with regards to subject company for which Research Team have expressed their views.

Regional Disclosures (outside India)

This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject MOSL & its group companies to registration or licensing requirements within such jurisdictions.

For Hong Kong:

This report is distributed in Hong Kong by Motilal Oswal capital Markets (Hong Kong) Private Limited, a licensed corporation (CE AYY-301) licensed and regulated by the Hong Kong Securities and Futures Commission (SFC) pursuant to the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) "SFO". As per SEBI (Research Analyst Regulations) 2014 Motilal Oswal Securities (SEBI Reg No. INH000000412) has an agreement with Motilal Oswal capital Markets (Hong Kong) Private Limited for distribution of research report in Hong Kong. This report is intended for distribution only to "Professional Investors" as defined in Part I of Schedule 1 to SFO. Any investment or investment activity to which this document relates is only available to professional investor and will be engaged only with professional investors." Nothing here is an offer or solicitation of these securities, products and services in any jurisdiction where their offer or sale is not qualified or exempt from registration. The Indian Analyst(s) who compile this report is/are not located in Hong Kong & are not conducting Research Analysis in Hong Kong.

For U.S.

Motilal Oswal Securities Limited (MOSL) is not a registered broker - dealer under the U.S. Securities Exchange Act of 1934, as amended (the "1934 act") and under applicable state laws in the United States. In addition MOSL is not a registered investment adviser under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act") and together with the 1934 Act, and under applicable state laws in the United States. Accordingly, in the absence of specific exemption under the Acts, any brokerage and investment services provided by MOSL, including the products and services described herein are not available to or intended for U.S. persons. This report is intended for distribution only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the Exchange Act and interpretations thereof by SEC (henceforth referred to as "major institutional investors"). This document must not be acted on or relied on by persons who are not major institutional investors. Any investment or investment activity to which this document relates is only available to major institutional investors and will be engaged in only with major institutional investors. In reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act") and interpretations thereof by the U.S. Securities and Exchange Commission ("SEC") in order to conduct business with Institutional Investors based in the U.S., MOSL has entered into a chaperoning agreement with a U.S. registered broker-dealer, Motilal Oswal Securities International Private Limited. ("MOSIPL"). Any business interaction pursuant to this report will have to be executed within the provisions of this chaperoning agreement.

The Research Analysts contributing to the report may not be registered /qualified as research analyst with FINRA. Such research analyst may not be associated persons of the U.S. registered broker-dealer, MOSIPL, and therefore, may not be subject to NASD rule 2711 and NYSE Rule 472 restrictions on communication with a subject company, public appearances and trading securities held by a research analyst account.

For Singapore

In Singapore, this report is being distributed by Motilal Oswal Capital Markets Singapore Pte Ltd ("MOCMSPL") (Co.Reg. NO. 201129401Z) which is a holder of a capital markets services license and an exempt financial adviser in Singapore, as per the approved agreement under Paragraph 9 of Third Schedule of Securities and Futures Act (CAP 289) and Paragraph 11 of First Schedule of Financial Advisers Act (CAP 110) provided to MOCMSPL by Monetary Authority of Singapore. Persons in Singapore should contact MOCMSPL in respect of any matter arising from, or in connection with this report/publication/communication. This report is distributed solely to persons who qualify as "Institutional Investors", of which some of whom may consist of "accredited" institutional investors as defined in section 4A(1) of the Securities and Futures Act, Chapter 289 of Singapore ("the SFA"). Accordingly, if a Singapore person is not or ceases to be such an institutional investor, such Singapore Person must immediately discontinue any use of this Report and inform MOCMSPL.

Disclaimer:

The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent. This report and information herein is solely for informational purpose and may not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. Certain transactions - including those involving futures, options, another derivative products as well as non-investment grade securities - involve substantial risk and are not suitable for all investors. No representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the information and opinions contained in this document. The Disclosures of Interest Statement incorporated in this document is provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. This information is subject to change without any prior notice. The Company reserves the right to make modifications and alternations to this statement as may be required from time to time without any prior approval. MOSL, its associates, their directors and the employees may from time to time, effect or have effected an own account transaction in, or deal as principal or agent in or for the securities mentioned in this document. They may perform or seek to perform investment banking or other services for, or solicit investment banking or other business from, any company referred to in this report. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting the document. This report has been prepared on the basis of information that is already available in publicly accessible media or developed through analysis of MOSL. The views expressed are those of the analyst, and the Company may or may not subscribe to all the views expressed therein. This document is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, copied, in whole or in part, for any purpose. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject MOSL to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction. Neither the Firm, nor its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information. The person accessing this information specifically agrees to exempt MOSL or any of its affiliates or employees from, any and all responsibility/liability arising from such misuse and agrees not to hold MOSL or any of its affiliates or employees responsible for any such misuse and further agrees to hold MOSL or any of its affiliates or employees free and harmless from all losses, costs, damages, expenses that may be suffered by the person accessing this information due to any errors and delays.

Registered Office Address: Motilal Oswal Tower, Rahimullah Sayani Road, Opposite Parel ST Depot, Prabhadevi, Mumbai-400025; Tel No.: 022-3980 4263; www.motilaloswal.com. Correspondence Address: Palm Spring Centre, 2nd Floor, Palm Court Complex, New Link Road, Malad (West), Mumbai-400 064. Tel No: 022 3080 1000. Compliance Officer: Neeraj Agarwal, Email Id: na@motilaloswal.com, Contact No.:022-30801085.

Registration details of group entities: MOSL- SEBI Registration: IN200158836 (BSE/NSE/MSE); CDSL: IN-DP-16-2015; NSDL: IN-DP-NSDL-152-2000; Research Analyst: INH000000412. AMFI: ARN 17397. Investment Adviser: INA000007100. Motilal Oswal Asset Management Company Ltd. (MOAMC): PMS (Registration No.: INP00000670) offers PMS and Mutual Funds products. Motilal Oswal Wealth Management Ltd. (MOWML): PMS (Registration No.: INP000004409) offers wealth management solutions. * Motilal Oswal Securities Ltd. is a distributor of Mutual Funds, PMS, Fixed Deposit, Bond, NCDs, Insurance and IPO products. * Motilal Oswal Commodities Broker Pvt. Ltd. offers Commodities Products. * Motilal Oswal Real Estate Investment Advisors II Pvt. Ltd. offers Real Estate products. * Motilal Oswal Private Equity Investment Advisors Pvt. Ltd. offers Private Equity products