

INVESTOR NEWSLETTER – QUARTER ENDED SEPTEMBER 2024

A. PAST PERFORMANCE:

Period:	Last 3 Months	Last 6 Months	Last 1 Year	Last 2 Years	Last 3 Years	Since Inception Jan-20 to Sep-24
Cumulative Returns						
Portfolio	13.7%	25.6%	39.7%	85.9%	80.3%	366.9%
Sensex	6.7%	14.5%	28.1%	46.8%	42.6%	104.4%
Outperformance	7.0%	11.1%	11.6%	39.1%	37.7%	262.6%
Annualized Returns						
Portfolio			39.7%	36.4%	21.7%	38.3%
Sensex			28.1%	21.2%	12.6%	16.2%
Outperformance			11.6%	15.2%	9.1%	22.1%

Notes:

- 1) Performance details for the Portfolio are before taxes, fees and expenses to make it comparable to Sensex
- 2) AIF license received in Q3 C21. Assets have been transferred into AIF as of 01/11/2021. Returns from Nov-21 onwards are for assets in the AIF
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We had a strong quarter. Our Portfolio returned 13.7% this quarter, more than double that of Sensex which returned 6.7%. This was despite having 19% cash on average through the quarter.

On the one hand it feels like nothing much has changed since the last quarter to report back. On the other hand, everything is a little less good around the edges. Indian macro remains strong, albeit with risks emerging with the political mandate for the BJP having weakened. The local demand environment for companies remains strong, but with many sectors showing signs of softening after the strong multi-year growth witnessed post COVID recovery. Market sentiment and domestic flows remain very bullish, but again with cautious overtones given the heady valuations: Sensex remains richly valued at 22.5x forward P/E, more than 1 standard deviation higher than its historical levels. And the NSE Small Cap Index remains in near bubble territory at 23.8x, more than 2 standard deviations above its historical levels. Global macro risks remain high with the continuing wars in Russia and the Middle East, somewhat overshadowed with the positive effects of a Fed cutting rates. China is looking to provide aggressive stimulus to stabilize its economy which is causing offshore money to look to China again from its emerging market allocation, which may come out of their current India allocation. Given this backdrop, and the high valuations, we are witnessing more volatility and more sizable down days when any risk comes to the forefront.

We continue to focus on delivering superior risk adjusted returns by buying companies where there is a margin of safety in valuations. This disciplined approach has caused our Sharpe Ratio (on a 3-year basis) to be 145% as against 46% for the Sensex. Our Portfolio fell less when the markets fell (low Down Capture Ratio of around 60%) and our Portfolio rose materially more when markets rose (high Up Capture Ratio of around 160%). We believe that this is principally because when you buy market leading companies when they are already cheap, they fall less in market shocks as they find fundamental support at even lower valuation levels.

Key outperformers:

- Shriram Finance: Up 23% this quarter, and almost 80% from election day when we increased this position to max.
- PNB Housing: Up 25% this quarter. Another name that we increased substantially when it fell on election day. Benefited recently from the market realizing how cheap it was when Bajaj Housing Finance listed.
- Life Insurance stocks: Up 24% on average this quarter. Partly recovering from a poor showing last quarter, and partly benefitting from regulatory overhang on surrender values going away.



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- Yatharth Hospitals: Up 36% this quarter. We just invested last quarter. Strong operating performance continues.
- SJS Enterprises: Up 28% this quarter. Again, we just invested 6 months ago. Strong operating performance continues.
- CMS Info: Up 21% this quarter. We exited partly.
- Quess: Up 29% this quarter. Strong business momentum, and now will benefit from the demand cycle swinging back in its favor.

Key underperformers:

- Cash: We had 19% cash on average this quarter which was a drag on returns.
- Big Banks: HDFC Bank, Axis Bank and Kotak Mahindra underperformed this quarter

Key changes to the Portfolio:

- Reduced our position in Emami: Green shoots in rural demand recovery have been visible for the last 2 quarters across many rural facing sectors. This had started the process of rerating for Emami, which had otherwise underperformed within the portfolio. With the elections providing a weaker mandate to BJP the market is probably correctly expecting a more populist agenda from the new government. This narrative, more so than the underlying performance, has caused their sharp rally in rural facing stocks, Emami included. With Emami trading at 40x+ forward P/E, higher than historical P/E levels now, we have started the process of reducing our exposure.
- Reduced our position in CMS Info: Our original thesis here was that the RBI's regulatory requirement for additional work at existing ATMs would give it 3-4 years of revenue boost. This is playing out, drowning out the fears of reduced cash usage across the system, and hence a low terminal value for the business. The company has also been diversifying into newer lines of business, like retail cash management and remote management services, which have longer growth trajectories. However, valuations are now no longer supportive at 22x forward P/E and we have started reducing our exposure.
- Reduced our position in SIS: This is one of the few positions where the operating performance of the company did not play out as we anticipated. The facility management and security services sectors are now witnessing gradually improving margins, but SIS has struggled to benefit from this with margins unable to sustainably move to pre COVID levels. We have started reducing our exposure.
- Entered Karnataka Bank: Karnataka Bank is cheap relative to both the sector and itself at 0.7x P/B NTM. It benefits from its strong liability franchise in a market environment where deposits are at a premium given the overall stretched banking Loan-Deposit Ratio. And new management, which are ex-HDFC Bank, are working through a culture change which could lead to further rerating. If both parts of our thesis play out then this could be a GARP style long term investment, but if only the liability franchise element of rerating occurs then this could be a tactical investment.
- Entered Updater Services: We have been bullish on the business services sector and have studied many of the players here, entering Quess and SIS. Updater is another such name that we entered this quarter. We believe the demand environment for the sector has found its bottom and will be on an improving arc going forward, helping both topline growth and margins. We like the diversification of Updater's business between facilities management services and business support services. And we have been impressed by its ability to buy adjacent businesses at reasonable valuations, and more importantly, to integrate them well. Our entry price is at 8.3x forward EV/EBITDA, a sharp discount to its sector.

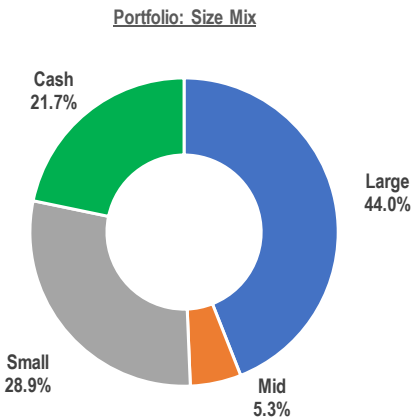
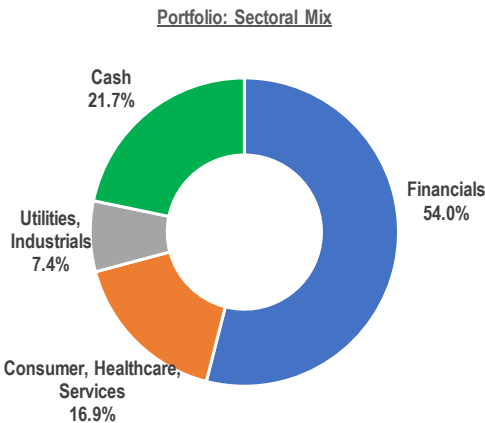


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Portfolio characteristics:

	P/E (forward)	12m EPS Growth (consensus)	PEG Ratio	P/B (forward)	RoE % (forward)	Sharpe Ratio (3 yr)	Beta (3 yr)
Portfolio	18.5x	15.8%	1.2x	2.9x	16.3%	146%	0.5x
Sensex	22.5x	15.2%	1.5x	3.8x	16.1%	46%	1.0x

Note: Portfolio details are ex Life Insurance



Top 10 positions: (of 20 total positions)

Shriram Finance	PNB Housing	SBI Life	Axis Bank	Yatharth Hospital
HDFC Bank	ICICI Pru Life	HDFC Life	Federal Bank	Cipla

Annualized Performance:

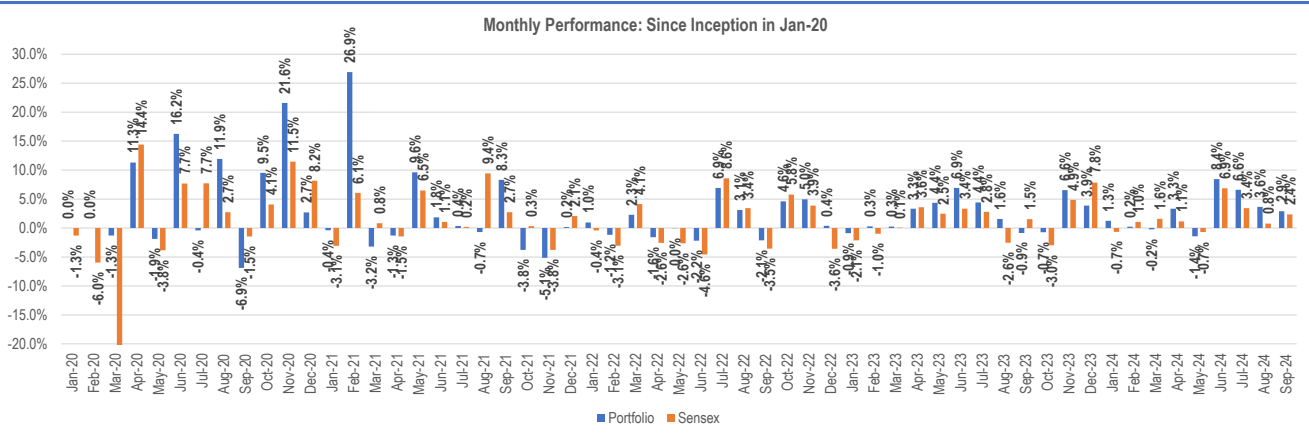
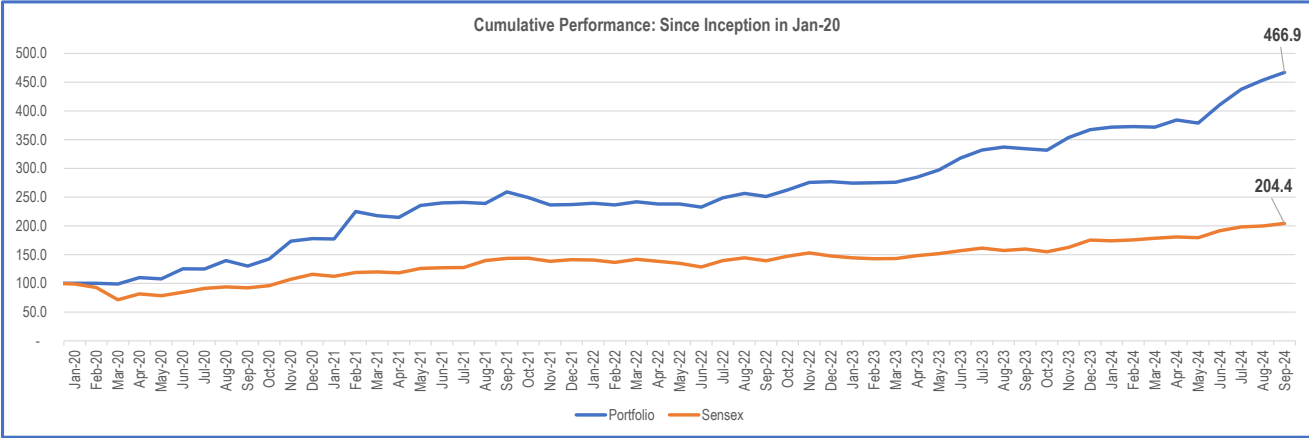
Period:	CY24 YTD	CY23	CY22	CY21	CY20
Cumulative Returns					
Portfolio	27.2%	32.7%	16.8%	33.2%	77.9%
Sensex	16.7%	18.7%	4.4%	22.0%	15.7%
Outperformance	10.5%	13.9%	12.4%	11.2%	62.2%

Period:	FY25 YTD	FY24	FY23	FY22	FY21
Cumulative Returns					
Portfolio	25.6%	34.8%	14.0%	11.1%	120.6%
Sensex	14.5%	24.9%	0.7%	18.3%	68.0%
Outperformance	11.1%	10.0%	13.3%	-7.2%	52.6%



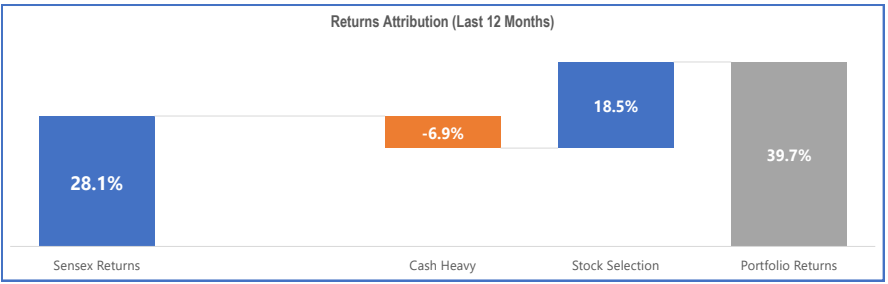
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Monthly performance charts:

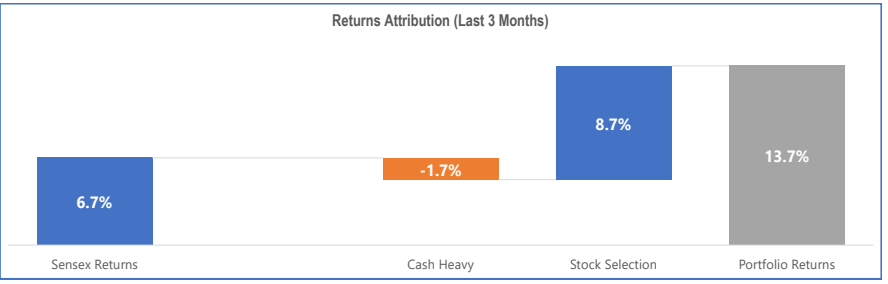


Returns attribution:

Outperformance
For Last Year:
+11.6%



Outperformance
For Last Quarter:
+7.0%



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Superior Risk Adjusted Returns:

High Up Capture Ratio of ~160%

- Our performance during up phases of the market has been strong, driven by stock selection
- Mar-20 to Oct-21: 151% Up Capture Ratio
 - Sensex up 101%
 - Our Portfolio up 153%
- Jun-22 to Sep-24: 171% Up Capture Ratio
 - Sensex up 59%
 - Our Portfolio up 101%



Low Down Capture Ratio of ~60%

- Defensive positioning through portfolio construction and cash on books helped our Portfolio fall less than the market during down phases of the market
- Oct-21 to Jun-22: 63% Down Capture Ratio
 - Sensex down 11%
 - Our Portfolio down 7%
- Election day (4th June 2024): 63% Down Capture Ratio
 - Sensex down 6%
 - Our Portfolio down 4%
 - More aggressive indices down a lot more (BSE Cap Goods Index down 12%!)



High Risk Adjusted Returns

- Our rolling 3yr Sharpe Ratio has consistently been 120-150%
- Best in class risk adjusted returns relative to peers. We created a peer group list using Finalyca data of funds that had at least 60% large cap composition – about 30 such funds. Our performance relative to them (as of last qtr):
 - Highest 3yr Treynor Ratio of 24.8
 - 3rd Highest Sharpe Ratio of 123%
- Given fully priced markets it is now even more important to balance risk and reward in portfolio construction

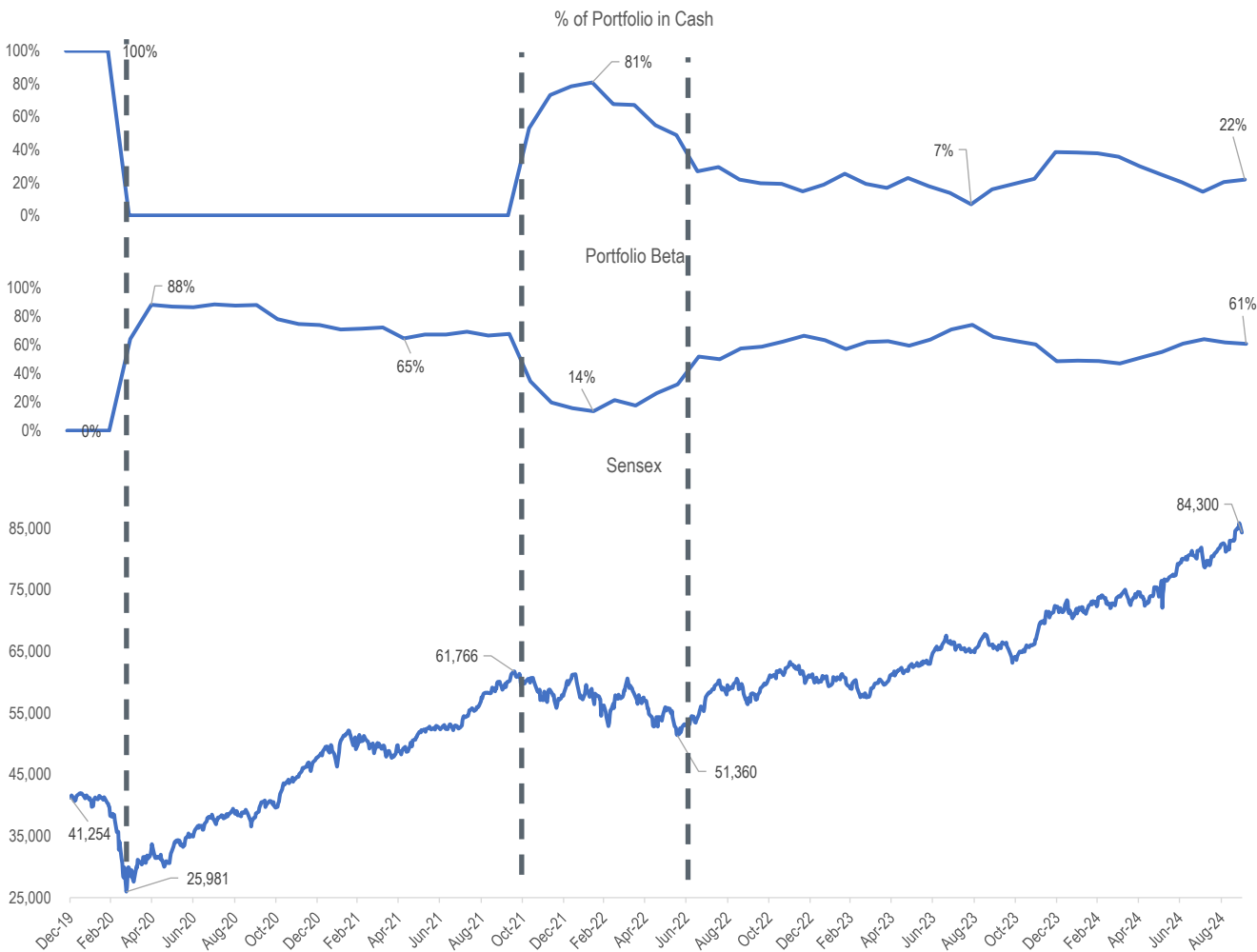


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Our strategy in action:

Our strategy is to buy good companies if they are cheap, and ONLY if they are cheap. If they are not cheap, we stay on the side-lines in cash for periods. Especially for large cap companies we buy them when they trade at discounts to their long-term average valuations and exit them when they start trading above long term average valuations without waiting for peak valuations.

This allows us to capture up market moves (High Up Capture Ratio), reduce our risk positions when markets are expensive, and wait in cash for opportunities when markets become cheap. We have been able to remain in cash for 2 down markets because of this strategy: i) before Covid, and ii) From Oct-21 to Jun-22. This ensures that in down market moves our Portfolio falls less than the market (Low Down Capture Ratio). A high Up Capture Ratio and a low Down Capture Ratio combine to provide our Portfolio with meaningfully higher returns than the market and a high Sharpe Ratio.



Pre-Covid (Jan-20 to Mar-20)	100% in cash before Covid Down Capture Ratio = 0% = Fall in Portfolio / Fall in Sensex = 0% / -29%
Market Bounce Back (Mar-20 to Oct-21)	100% in equity, with Portfolio beta gradually reduced as the markets rallied Up Capture Ratio = 151% = Rise in Portfolio / Rise in Sensex = 153% / 101%
Market Correction (Oct-21 to Jun-22)	Up to 80% in cash Down Capture Ratio = 63% = Fall in Portfolio / Fall in Sensex = -7% / -11%
Market Bounce Back (Jun-22 onwards)	24% in cash on average Up Capture Ratio = 171% = Rise in Portfolio / Rise in Sensex = 101% / 59%



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B. OUTLOOK:

Our portfolio positioning continues to remain defensive as few sectors are priced below fair value. The Portfolio is more concentrated with 20 stocks now (but 3 are in the process of being sold). And we continue to remain cautious on Small Caps. Our Portfolio continues to be primarily concentrated in lending financials, life insurance companies and business services companies, all of which offer margin of safety in an otherwise fully valued market.

This positioning is an outcome of high valuations in the market, which has been ignoring and / or quickly digesting potential risks. Some of the key risks which we are thinking about include:

- Coalition politics: Both the smaller parties supporting BJP in forming a coalition government are leaders from cash hungry states. India's history with coalition politics suggests that there could be a substantially noisier next 5 years relative to the last 10 years of single party majority. Near term state elections will continuously provide the noisy environment within which we could see markets overreact presenting opportunities
- Elections in the west: The US election is this quarter and could create near term market reactions especially on India's exporting sectors.
- Geopolitical risks: It is easy to forget that 2 large scale geopolitical conflicts are ongoing. We have recently seen a flare-up in Middle East situation.
- US recession: Another risk remains US recession / slow down. Data on this remains choppy, and in many ways could work into a reverse Goldilocks outcome, where good news on the unemployment front could mean less Fed cuts, which could mean less reason for equity to cheer. We continue to watch closely.

On the flip side, inflation and interest dynamics in the west could allow the RBI space to cut rates through the next 12 months given the lower inflation dynamics in India.

We remain constructive in our research studying names in the business services, healthcare, and auto component sectors. We have added in these sectors already in the recent past but there are more names where our private equity style work continues.

We remain patient and remain committed to not chasing high valuations.

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Sector	P/E Sep-24	P/E Sep-23	P/E 10 Yr Avg	vs Sep-23	vs 10 yr Avg	Our View
Auto	26.7x	20.9x	27.4x	28%	-3%	2W seeing increasing competitive intensity in the top end, PV and CV cycle topping out. We are instead spending time on auto comps
Banks - Private	16.5x	15.3x	21.1x	8%	-22%	This is our largest sectoral position in the fund. Continues to offer opportunities even though market is expensive overall
Cement	35.5x	28.7x	27.0x	24%	31%	Still expensive both on a absolute and relative basis
Consumer	49.5x	41.7x	41.3x	19%	20%	Very expensive, but we have a position in one of the cheaper names benefitting from margin improvements given rural demand recovery
Healthcare	34.6x	27.0x	26.7x	28%	30%	We entered last year when opportunities existed. Fewer opportunities now. Working on hospital names
Infrastructure	25.8x	16.9x	11.4x	53%	126%	Very expensive, we are staying away
Media	21.4x	20.2x	25.3x	6%	-15%	While it looks cheap we have studied the companies here and have decided to pass due to risk in business models and / or due to corporate governance
Metals	12.5x	11.1x	10.9x	13%	15%	We are beginning to focus on steel and we expect further softening in both prices and margins which could give us opportunities in the future
Oil & Gas (ex RIL)	9.6x	5.9x	8.6x	63%	12%	We have positions in O&G consuming / distributing companies as beneficiaries of normalizing commodity prices. This has largely played out.
Specialty Chemicals	38.3x	32.5x	24.0x	18%	60%	The market mixed China+1 thematic with upswing in commodity prices. Further downside in many names despite correction. We are watching keenly
IT Services	28.5x	23.2x	20.7x	23%	38%	Had corrected a lot, but then moved up. We spent a lot of time researching the sector. We are tracking but opportunity has moved further away

Data Source: Motilal Oswal