



5 YEARS OF ECIP

The Good, the Bad and the Ugly

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Dear Investors,

Performance

Below is the performance of the Emerging Corporates India Portfolio (ECIP) for Q4FY22 and as of March 31, 2022.

Portfolio Performance	Total Portfolio Returns	New Benchmark	Old Benchmark
CAGR since Inception (<i>Annualised</i>)	16.2%	13.7%	13.0%
FY22	8.6%	26.2%	29.2%
FY21	79.2%	94.0%	104.7%
FY20	-13.2%	-30.3%	-33.0%
FY19	13.3%	1.2%	-6.5%
FY18 (<i>Since Inception - April 28, 2017</i>)	9.7%	10.2%	10.5%
Q4FY22	-1.2%	-2.1%	-3.6%

- *New Benchmark is an average of the BSE Smallcap Index, BSE Midcap Index and Nifty*
- *Old Benchmark is an average of the BSE Smallcap Index and BSE Midcap Index*
- *Returns are time weighted and after management and performance expenses.*
- *Management and performance fees are deducted as and when due*
- *The actual returns of clients may differ from client to client due to different portfolio and timing of investment*
- *Past performance is no guarantee for future performance*
- *Benchmark calculations reflect total returns (including dividends)*
- *Returns for less than 1 year are not annualised*
- *Inception Date is 28th April 2017*

H1FY22 was a period of significant underperformance for our scheme. We have elaborately delved into the possible causes in our past newsletters. In H2FY22, our relative performance has been similar to the benchmark. While FY22, overall, was a difficult period for us, we are reasonably optimistic of the prospective returns of our current portfolio. We believe we have a good balance of compounders and special situations (*corporate action or management change*). Compounders (*high quality lenders; insurance companies*) in our portfolio have delivered no returns to investors for the last 2 years despite their intrinsic value growing at 15-18% leading to a meaningful drop in valuations. For an investor with an absolute return mindset, compounders at price points where the risk of multiple de-rating is low are a good entry point because even if the multiple does not expand, healthy intrinsic value growth provides good absolute return. Two years ago, these compounders were at expensive valuations and possibly offered lesser prospective return than the broader market, which was cheap (*something that we've only realised with the benefit of hindsight*). However, we have strong reasons to believe that the reverse is true today. Further, we also have a healthy mix of special situations in our portfolio which are, in our understanding, relatively less co-related to the broader market giving us further room to have a differentiated performance from the indices.

Today, i.e., April 28, 2022, our scheme completes 5 years. We think it's a good time to look back and do a hand on our heart analysis of what worked for us and what did not. In this newsletter, we present key statistics of our 5- year performance (*while we generally avoid stating stock names, this analysis will lack meaning if we present it without stating any names; as an exception, we are stating names here – except for the recently bought companies*).

Over five years of managing money under Emerging Corporates India Portfolio, we have taken 38 decisions. Of those, 5 decisions are relatively new for us to judge them on a win: loss metric. That leaves us with 33 decisions. These are further broken down into 20 closed decisions (*we do not own these stocks as of today*) and 13 open decisions that have been with us for at-least one year (*we own these stocks today*).

If we only look at the 20 closed decisions, 4 have been mega-winners (>100% total return) and 6 have been meaningful winners (between 40% to 100% return) – implying a hit-rate of 50% of at-least a meaningful win. We have had 4 losers, out of which only one has lost more than 30%. Amongst the 13 old open positions, we've had no losers and about 25% of positions being at-least meaningful winners. 9 old open decisions in the between "10%-30%" category reflects these stocks have lagged over the last two years.

Overall, we have a 20% hit-rate of scoring a mega-winner; 40% hit-rate of scoring at-least a meaningful winner and 73% hit-rate of scoring at-least a winner.

	Closed	%	Open - Old	%	Total	%	Cumulative Total
Mega-winners (>100%)	4	20%	2	15%	6	18%	18%
Meaningful winners (between 40% to 100%)	6	30%	1	8%	7	21%	39%
Winners (between 10% to 40%)	2	10%	9	69%	11	33%	73%
Neutral (-10% to +10%)	4	20%	1	8%	5	15%	88%
Losers (between -10% to -30%)	3	15%	0	0%	3	9%	97%
Mega Losers (worse than -30%)	1	5%	0	0%	1	3%	100%
	20		13		33		

A pertinent variable missing in the above analysis is holding period. One can look at this data scrip-wise through the lens of XIRR to understand how we fared in each stock (*a mega-winner over a very long time might not lead to a very high XIRR and a meaningful winner over a short-time could lead to a very high XIRR*).

Sr. No	Company	Total Return	XIRR	Period of holding (could be multiple entries/ addition/ reduction/ exits)
Closed Positions				
1	P I Industries Ltd	271%	59%	Oct'18 to Dec'21
2	Avenue Supermarts Limited	200%	57%	Oct'18 to Dec'21
3	L&T Technology Services Limited	121%	199%	Aug'20 to Dec'21
4	VIP Industries Ltd	120%	64%	Mar'20 to Jan'22
5	Vinati Organics Ltd	85%	52%	May'17 to May'19
6	Info Edge India Ltd	81%	52%	Aug'17 to Feb'19
7	Tata Elxsi Ltd	55%	38%	May'17 to Oct'20
8	Natco Pharma Ltd	49%	24%	Oct'19 to Dec'21
9	Interglobe Aviation Ltd	48%	33%	Sep'17 to Nov'20
10	Syngene International Ltd	48%	26%	Jun'17 to Jul'20
11	Hexaware Technologies Ltd	24%	251%	Jul'20 to Sep'20
12	Ashiana Housing Ltd	17%	4%	Jan'18 to Mar'22
13	Ajanta Pharma Ltd	1%	3%	Jun'18 to Feb'19
14	IDFC BANK LIMITED	-2%	-3%	Dec'17 to May'19
15	Mayur Uniquoters Ltd	-2%	-2%	Sep'17 to May'19
16	Thyrocare Technologies Ltd	-5%	-5%	Nov'17 to Dec'18

17	Persistent Systems Ltd	-14%	-6%	Apr'17 to Aug'19
18	Matrimony.com Ltd	-19%	-39%	Sep'17 to Sep'18
19	Bajaj Finance Ltd.	-22%	-36%	Aug'19 to Jun'20
20	Disa India Ltd	-42%	-22%	Jan'18 to Jun'20
Open Positions – Old (Completed > 1 Yr)				
21	Suven Pharmaceuticals Ltd.	134%	109%	Dec'17 to Today
22	Oberoi Realty Ltd	124%	45%	Dec'18 to Today
23	Tata Consumer Products Limited	66%	45%	Oct'20 to Today
24	Gland Pharma Ltd	33%	60%	Feb'21 to Today
25	Kotak Mahindra Bank Ltd.	28%	19%	Jul'20 to Today
26	HDFC Asset Management Company Ltd	27%	30%	Aug'18 to Today
27	Bandhan Bank Limited	22%	19%	May'18 to Today
28	Nesco Ltd	18%	11%	Dec'17 to Today
29	DFM Foods Ltd.	15%	12%	Sep'19 to Today
30	ZF Commercial Vehicle Control Systems India Ltd*	14%	24%	Sep'19 to Today
31	HDFC Standard Life Insurance Company Limited	12%	12%	Nov'17 to Today
32	SBI Cards and Payment Services Limited	10%	11%	Mar'20 to Today
33	ICICI Lombard General Insurance Company Ltd.	9%	7%	Feb'20 to Today
Open Positions – New (Completed < 1 Yr)				
34	xxxx xxxxx (IT Services Company)	37%	109%	Oct'21 to Today
35	xxxx xxxxx (Consumer Products Company)	20%	80%	Oct'21 to Today
36	xxxx xxxxx (Consumer Products Company)	18%	67%	Oct'21 to Today
37	xxxx xxxxx (Housing Finance Company)	6%	16%	Oct'21 to Today
38	xxxx xxxxx (Life Insurance Company)	6%	70%	Mar'22 to Today

*ZF Commercial Vehicle Control Systems returns includes our holding between Sep'19 to Jul'20 as an arbitrage position (quasi-cash). We re-entered the Company as an active investment in Mar'21 and are holding it till date. Our total returns are 39% and XIRR returns are 37% in the stock if one excludes the arbitrage position.

** Data as of Apr 14, 2022

*** This study is done for the account that was opened on Day 1 - April 28'2017 with INR 25 lacs. Between April 27'2020 and April 29'2020, additional corpus of INR 22 lacs was infused. On March 8'2021, there was a withdrawal of INR 12 lacs and on Dec 2'2021, there was an infusion of INR 5 lacs. XIRR performance of this account since inception till April 28'22 (5 Years) is 21.44% versus New Benchmark of 20.4% and Nifty of 19.05% (IRR for the benchmark index is computed by simulating portfolio cashflows into respective benchmarks).

What are the takeaways for us and for investors from the above analysis?

1. We have had a very favorable “win: loss” ratio and have not been dependent on a single stock or very few stocks to drive returns. We think “win: loss” ratio is an important determinant of ability to have recurring returns and also helps to assess whether performance has been owing to skill or luck.
2. On balance, we have been good sellers. Our returns in stocks like HDFC AMC; Bandhan; HDFC Life; Nesco largely stem from exiting and booking profits in an earlier round when these stocks became very expensive. Most of these stocks from a point-to-point basis have been laggards and have had massive U-turns from their peak prices, but we have still managed to eke out returns due to disciplined partial/ full selling at points where we thought we were being heavily compensated.
3. Interestingly, even in our losers, we had two mega-bagger potential stocks after we sold (*Persistent Systems is 7x from our selling price and Bajaj Finance is 3x from our selling price*). For Persistent Systems and Disa India, our learning has been to not sell stocks at cheap valuations and be patient with them until we believe that our fundamental thesis still holds and performance is delayed but the foundation is still in place for delivery in the

future – cheap valuations bring with them low expectations of performance and if we continue to trust the management and the business capability, it's better to wait it out, howsoever painful it may seem at that time. In the case of Bajaj Finance, we do not consider selling a mistake as we thought the stock was expensive even when we sold it and we could not convince ourselves of its competitive advantages versus Banks (*and Banks were available at less than ½ its valuations*); buying Bajaj Finance at expensive valuations was a mistake we think; we now realise we were sub-consciously chasing price momentum not believing in the fundamental thesis; and the mistake of buying it half-heartedly shook us out of our position when the stock corrected massively (*if you don't have strong conviction when you buy, price action can easily shake you out; you become very vulnerable to price action*). In Matrimony.com, we erred on our thesis of margin expansion ignoring the industry structure with two well-funded competitors who had much less to lose in a price war and thus, we do not consider selling a mistake as we lost conviction in the fundamental thesis (*it's important to be truthful about your motivation to sell – are you selling because you are losing patience or because you think you are wrong – if the latter, be brutal and do not look at valuations; having said that, making this distinction is often very difficult*).

4. Because we have a “reduce/ sell” on high valuation mindset, we have also sold a stock like Tata Elxsi early (*very early!*). This stock went up 5x in 15 months post-sale, giving us a lot of heart burn. When a stock is beginning to look expensive, we generally need to feel confident of sustained earnings momentum to hold. One way to assess sustainability of earnings momentum is to understand the nature of contracts and the inherent visibility that they provide. Given that Tata Elxsi has had short-term contracts historically, its q-o-q growth has been volatile. As it started reported strong growth for a few quarters, we were reminded of the pattern we had seen in the past of contracts/ projects ending without immediate ability to replenish revenue from new contracts/ projects, leading to disappointments versus expectations and massive U-turns in stock price. We had no reason to believe that this time was any different. While we were bullish on the ER&D space from a top-down perspective, lack of growth visibility was a concern, especially when markets started factoring high and sustained growth momentum in its valuations. It just so happened that growth momentum has sustained longer this time, margins are at 500-600 bps above long-term averages and the stock has gone to astronomical multiples, currently trading at ~70x FY23E. It is a concoction of the best of everything. It's very difficult to assess what one can learn from this. One out of 100 stocks would have the fate of Tata Elxsi and to learn excessively from this experience might not enhance our process. Nevertheless, we are trying to equip ourselves with better selling techniques to capture more upside when we get something right (*however, we do not intend to become compulsive “buy and hold” because we do think “buying low” and “selling high” is something we have done reasonably well and it's important to do so to have healthy returns over a 3–5-year time horizon*).

To summarise, we would like to think we have had reasonable success at the process level, but there is meaningful scope for improvement. Having a strong conviction when buying, giving companies enough time to deliver, being patient through periods of stock underperformance as long as we think we are not wrong and being more sensitive to technical and earnings momentum while selling have been the key takeaways of this study for us. It's also important to acknowledge that one cannot have purely outcome-based learnings in a 5-year period because in a relatively short span of time, “good decisions” could have had bad outcomes and vice versa.

In the end, we would like to state that we are deeply committed to a continuous improvement in our process and if we can achieve that, we strongly believe that sustained long-term performance will follow.

Thank you for a patient reading.

Regards

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Note:

1. All cash holdings and investments in liquid funds, is considered for calculating the performance.
2. All performance data are reported net of all fees and all expenses (including taxes).
3. The above performance numbers are not verified by the SEBI

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The Composite representing the Emerging Corporates India Portfolio was created on 28th April 2017. Performance has been compared with Total Return of the Index. For Emerging Corporates India Composite, blended benchmark of BSE 500 (50% weight) and BSE Mid Cap Index (50% weight) were used previously, and the Benchmark has been revised to BSE Smallcap Index (33.33%), BSE Midcap Index (33.33%) and Nifty (33.34%). The Gross Return (wherever mentioned) is before all expenses (except Brokerage). Net Return is after all actual expenses. A complete list of composite descriptions, policies for valuing portfolios and calculating performance fees are available on request.

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- d. As with any investment in securities, value of the Client’s Portfolio can go up or down depending on the factors and forces affecting the capital market.
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