Built by investors for investors

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Emerging Corporates India Portfolio

Multi-Act Equity Consultancy Pvt. Ltd.

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Dear Investors,

Performance

Below is the performance of the Emerging Corporates India Portfolio *(ECIP)* for Q4FY23 and as of March 31, 2023.

Portfolio Performance	Total Portfolio Returns	Benchmark
CAGR since Inception *(Annualised)*	11.6%	11.1%
FY23	-8.9%	-0.7%
FY22	8.6%	26.2%
FY21	79.2%	94.0%
FY20	-13.2%	-30.3%
FY19	13.3%	1.2%
FY18 *(Since Inception - April 28, 2017)*	9.7%	10.2%
Q4FY23	-8.3%	-5.1%
Q3FY23	0.6%	3.3%
Q2FY23	11.8%	13.0%
Q1FY23	-11.6%	-10.2%

- *Benchmark is an average of the BSE Smallcap Index, BSE Midcap Index and Nifty*
- *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*

The ECIP portfolio continues to struggle both in absolute terms and relative to the markets. The ECIP scheme is a style focused scheme prioritising fundamental momentum over valuations and investing only in the quality space *(in-case of non-lenders - quality as defined by historical evidence of at-least high teens return on capital metrics; cash-flow generation and preferably net-cash companies AND in case of lenders: quality as defined by at-least mid-teens return on equity; extremely strong track record on asset quality across cycles and preferably some advantages on the cost of funds side)*. Additionally, we selectively allocate to what we think are credible special situations as well *(for e.g.: value creation owing to ownership change)*.

Let us look at what the market rewarded in the last one year. We have done a simple exercise of sorting the 1 year mean and median returns of the Top 500 companies by market capitalisation based on their 5 Year Average Return on equity *(Source: Screener.in; Data as on April 14, 2023)*.

5 Year Average RoE	Count of companies	Median 1 Yr Return	Mean 1 Yr Return
greater than 25%	59	-15.1%	-8.8%
between 10% to 25%	267	-0.9%	3.9%
less than 10%	174	1.9%	7.7%
Total	**500**		

Admittedly, there's more to quality than just Return on Equity (RoE). But this data nevertheless tells you the flavour of the market. The best performing segment of the market has been Companies that had an average 5 Year RoE less than 10%. And the worst performing segment has been Companies with average 5 Year RoE above 25%. Since our universe and allocations tend to be more in the high RoE companies, we suffered relative to the benchmarks on two counts - we had negligible to small allocation to the best performing segment and a large allocation to the worst performing segment. While we think that quality making a comeback is more a question of "when" and not "if", it nevertheless tests one's patience. Further, it would be foolhardy on our part to go into a universe which has not proven to be a long-term wealth creator and is full of landmines *(though can have patches of few months to few years of good performance)*. Ultimately, over the long-run, higher ROE universe will generate better returns relative to a lower ROE universe. While it is true that the best returns might emanate from companies whose starting point is low ROE (and thus are cheaply valued at this point) and can transition to a structural and sustainable high ROE and one is rewarded with a massive valuation kicker, one needs to understand that such transitions are very rare and fraught with extremely high risk (most fail!). There could be periods when markets are in the mood to reward such transformation stories and this can create intermittent multi-baggers, but we believe that this is not the way to have sustainable returns. When stories fizzle out and these stocks have to face the test of reality, one realises that the MTM gains soon evaporate *(we will very selectively participate in transition stories which are more led by change of ownership/ management than use this as our core investment strategy)*.

Over and above this general flavour of the market in FY23, we were badly hit on account of stock specific news as well.

Few stock-specific events that affected the quarterly performance of the scheme on the negative side:

— Life insurance companies were at the receiving end of taxation changes announced in the recent budget. Two changes announced were removal of tax exemptions for policies where annual premium exceeds INR 5 lacs and nudging taxpayers to move to the exemption-free new tax regime. These changes were unexpected and took us by surprise. We have always believed that Insurance is a push product *(the best-case scenario is that you never need to use the product)* and there needs to be some additional incentive that needs to be given to the customer to motivate him/ her to buy the same. This added incentive came in the form of it being packaged as a savings product where people insure themselves by primarily investing in a savings product *(the tax benefit now stands removed for policies above INR 5 lacs)* or in the form of section 80C/ 80D tax benefits *(which the government is now trying to do away with by nudging taxpayers to be in the new regime).* After the budget announcements, we thought that the growth rate of the life insurance industry would be structurally hit by a few hundred bps. And if this were true, the multiples should de-rate. When we worked with the revised numbers, we did not find these stocks to be attractively valued anymore. And thus, we decided to exit them.

— We also own one of largest AMC in the country. This AMC had seen a streak of underperformance and had resultantly lost market share. Our thesis was that underperformance should normalise and the market share should start improving. This thesis, in-fact played out quite well. However, we were hurt by a significant overhang on the stock as SEBI announced that it would re-look at the expense ratios for the mutual fund industry. There is uncertainty around sustainability of the profitability metrics of the business *(in terms of bps/ AUM)* owing to this overhang. And this, further caused price damage to a stock where the story was developing favourably otherwise. We have not sold the stock with the belief that SEBI would want to put an end to malpractices but will not bring in regulations that kills the attractiveness of the business completely *(a lot of possible negatives are also already in the price, in our opinion)*.

— We have a significant allocation to a south-based kitchen appliances player that was acquired by a fans major in Feb'22. We were very encouraged by the new management appointments in this investee company and believed that the fans major would scale this business up meaningfully, both on the revenue and profitability front. However, towards the end of the Mar'23 quarter, the fans major announced a merger of the kitchen appliances player into itself at a swap ratio that, we think, is unfavourable for the minority shareholders of the kitchen appliances player. When the swap ratio was announced, the stock fell owing to this overhang. This merger, in order to be passed, will require that the majority of minority vote in its favour. Time will tell if it goes through. We have not sold the stock but have taken a drawdown on this account.

An important development possibly on the positive side

- We have a significant allocation to a Housing Finance Company with the best asset quality track record over the years. In the last year, the Company faced fraud allegations and a CEO resignation. Thereafter, it underwent an audit of all its branches without any material adverse findings. The market was sceptical of the ability of the Company to attract good talent post the resignation of its CEO. Since our investee company is owned 30% by a PSB, the fear was that the incoming CEO could be from the public sector. However, announcement on the incoming CEO *(made in Mar'23)* has been very encouraging *(private sector employee with most of his career in India's best financial services group)* and should soothe the nerves of the market.

Other stocks that continue to have an overhang:

- Credit card Company – The RBI is yet to come out with the final circular on merchant discount rate and interchange fees.
- Private sector Bank – In the process of identifying a successor to the founder promoter who has been at the helm for more than twenty years.
- General Insurance Company – The promoter of this Company *(which is a Bank)* needs to sell 18% stake in the Company by Sep' 24 *(date recently extended from Sep'23)* to comply with RBI norms.

We have also added three new companies to our portfolio:

- We invested in an auto ancillary which is the second largest player in the fasteners space *(nuts and bolts).* While fasteners seem like a basic product, margins in this product are at the top-end of the auto ancillary industry and return metrics are strong. Further, this company has cracked a very interesting product in the EV space through a technical collaboration with a Chinese Company - the motor control unit – which constitutes 10% of an EV - it has a very high market share in high-speed EV 2Ws. This gives meaningful optionality to the idea.

- We invested in India's largest artificial leather (PVC leather) company that has, after a long process, obtained approvals to supply to North American automakers. Our understanding is that while at the surface, this might look like a commodity business, a deeper study reveals that only a few Companies have cracked global quality, process efficiency in terms of low rejection rates, the design spread, scale-led cost benefits and most importantly, global customer approvals. In our understanding, this Company is likely to see a meaningful scale up in its export revenues owing to model launches in the next 24 months for which its supplies are approved – which should lead to a meaningful profit growth.

- We invested into a leading lighting supplier with 95% exposure to the 2W space. The 2W volumes have been at cyclical lows and even a recovery to 2019 volumes by 2025 would result in a meaningful growth here onwards. We think this Company is a beneficiary of 5 factors:

- Uptick in 2W volumes.
- Content per vehicle led growth owing to shift from conventional lighting to LEDs (2x realization).
- Recent entry into India's largest 2W player could provide growth surprise possibilities over the next 3 years.
- Growth tailwind from EVs (higher market share in EVs relative to non-EVs)

Every portfolio, in any timeframe, goes through its own shares of wins and losses. And every year, some seeds sowed in the past translate into small/big winners while a few turn into small/big losers. If you look at FY23 though, we have had more than our share of small/ big losers but they were not accompanied by the small/big winners. When we study our long-term win: loss ratio, it continues to stay healthy. Unless we have suddenly lost all our skill, we believe that this is only a phase where we are hitting significantly below our long-term average and as we mean revert, our performance should start looking better. A lot of the overhangs that we talk about should see some finality in the next 12 months *(not everything should go against us!)*. Further, if one looks at the recent rate pause by RBI, it augurs very well for our credit card company and housing finance company *(both can see meaningful margin tailwinds if the rate cycle peaks out and then reverses).* There are asymmetric payoffs, we believe.

Thank you for a patient reading.

Regards

Rohan Advant, CFA	Rahul Picha
Sr. Portfolio Manager and Associate Director	Portfolio Manager

Statutory Details: Portfolio Manager – Multi-Act Equity Consultancy Private Limited (Registration No. INP000002965)

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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

Disclosure as per Global Investment Performance Standards (GIPS®) –

Multi-Act Equity Consultancy Pvt. Ltd. claims compliance with the Global Investment Performance Standards (GIPS®). You can refer to the GIPS Compliant performance presentation here. Multi-Act Equity Consultancy Pvt. Ltd. has been independently verified by M/s. M. P. Chitale & Co., Chartered Accountants for the periods April 1, 2011 through March 31, 2019. The verification is available upon request. MAECL has claimed GIPS compliance for the Financial Year 2022 and such performance numbers shall be made available upon request.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.

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.

Multi-Act Equity Consultancy Pvt. Ltd. is an independent SEBI registered Portfolio Manager. The firm maintains a complete list and description of composites, which is available upon request. This ECIP Composite includes all discretionary fee-paying portfolios that are being managed with the objective of generating capital appreciation by investing in companies that in the opinion of the Portfolio Manager are “Advantage Period Companies” which are enjoying a “competitive advantage period” that is likely to last for at-least 5 years and are available at a valuation that offers margin of safety relative to the growth opportunity landscape. The portfolio manager has also the discretion of not being fully invested if he is not able to find ideas that meet the above criteria along with valuation criteria, thus, indirectly taking an asset allocation call between Equity and Cash (& Cash Equivalents).

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Risk factors
General risk factors

a. Securities investments are subject to market risks and there is no assurance or guarantee that the objective of the investments will be achieved.
b. Past performance of the Portfolio Manager or its affiliates does not indicate its future performance.
c. Investors are not being offered any guaranteed or assured returns i.e. either of principal or appreciation on the Portfolio.
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.
e. The Portfolio Manager is neither responsible nor liable for any losses resulting from the operations of the Portfolios.
f. The investments made are subject to external risks such as war, natural calamities, and policy changes of local / international markets which affect stock markets.
g. The Portfolio Manager has renewed SEBI PMS registration effective December 04, 2020 and has commenced its portfolio management activities with effect from January 2011. However, the Portfolio Manager has more than 10 years of experience in managing its own funds invested in the domestic market.