STRATEGY COMMUNIQUE
Q2-CY 2023

SUSTAINABLE & PRODUCTIVE

Over the last many years, and especially post-Covid, India's growth drivers have notably changed. While several factors have driven this transformation, we examine two vital areas of change: (A) India's systemic need for low leverage [low debt/GDP] and (B) Gradual improvements in productivity. Sustainable levels of debt and productivity are among the crucial factors of a nation's economic sustainability, ultimately reflected in corporate earnings. Today, India's standing on both these fronts provides an environment for delivering sustained economic growth in the times to come. This translates into the necessary framework to attract equity capital and deliver positively.

India's growth is organic, not levered.

Does optimal debt-to-GDP ratio result in better investment outcomes?

While excessive caution on debt will limit a nation's potential for growth, excessive debt is not a sustainable proposition. The optimal level of debt lends itself to the rate and quality of economic growth and vice versa. Higher debt [and interest payments] leave little space for productive spending on growth and crowd out the necessity for productive investments. Once consensus builds around excessive debt, the concern about a financial crisis generally weakens the investment climate and percolates to a systemic level in an economy, eventually hurting the country's ability to invest and re-invest optimally.

India's optimal debt-to-GDP

India's national debt is around 170% of GDP, roughly distributed equally between the government and the private sector (households + corporate). A comparison of the national debt of major nations in the World reveals that India's debt of 170% of GDP is among the lowest, compared to about 270% of GDP in China and the US and more than 400% of GDP in Japan.

% of GDP	Household Debt /GDP	Corporate Debt /GDP	Government Debt/GDP	Total Debt/GDP
CY10	37.5	77.1	68.2	182.8
CY11	35.8	77.2	66.5	179.5
CY12	35.2	77.8	66.8	179.8
CY13	34.5	69.6	67.1	171.2
CY14	33.8	72.1	66.4	172.3
CY15	33.7	67.9	68.3	169.9
CY16	33.3	57.5	68.8	159.6
CY17	34.5	58.3	69.6	162.4
CY18	34.9	48.9	69.4	153.2
CY19	37.0	54.5	74.3	165.8
CY20	40.2	59.2	88.7	188.1
CY21	36.0	53.0	85.1	174.1
CY22	36.4	53.6	82.6	172.6

[Source: Bank for International Settlements, MOSL]

Between 2012 and 2023, India’s nominal GDP has risen by $2 Trillion or 10.7% CAGR.

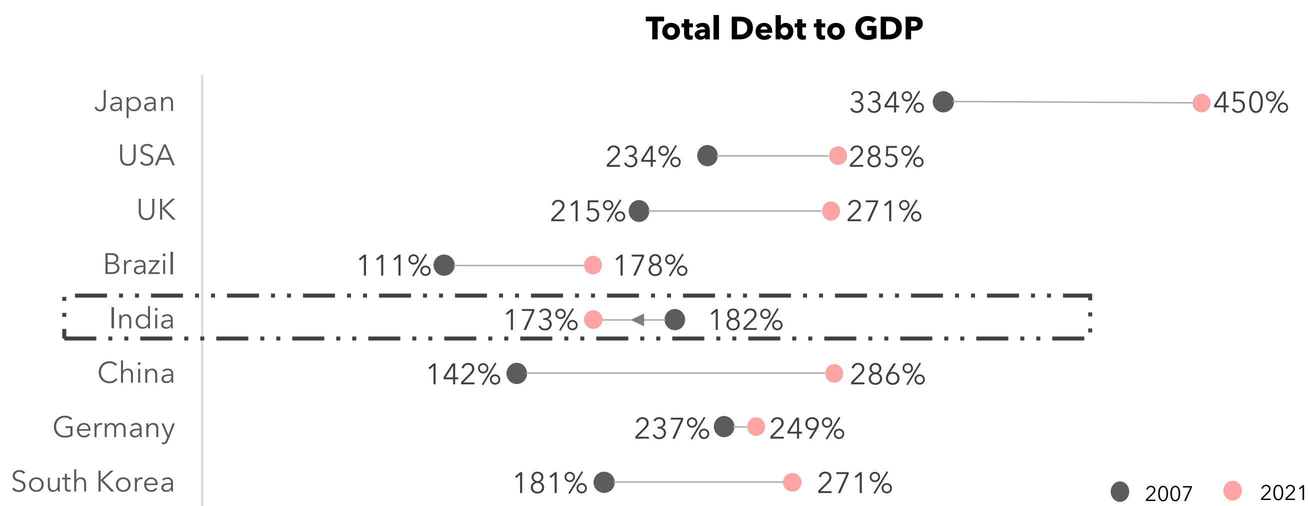
This is translated to equity returns of 11.9% CAGR; as growth has been funded organically, and not through financial leverage.

India's private debt is among the lowest, with a household debt of just 35% of GDP and corporate debt of 50%. This is an important metric for investors, indicating that India's consumption-oriented economy is funded through sustainable end-user demand and not financially amplified. This structure is also sustainable at a national [government] level. As per a recent paper [click for link] by the Asian Development Bank (ADB), in the event of a possible triple shock, i.e., real GDP growth is 1 std deviation lower, while the primary deficit and interest rates are one std deviation higher than the baseline, India's debt would still fall from 89.6% of GDP in FY23 to 86.7% of GDP by FY27.

Why is this important?

This is critical in today's environment, as India's growth momentum is not subject to monetary policy outcomes. As a domestic consumption-oriented economy that is incrementally more self-reliant, *India's ability to grow depends on factors within its control*. As investors in India, this is an important variable to consider. This frees India's monetary authority to determine interest rates as the environment demands, enabling it to manage an economy's key risks -- systemic financial stability and inflation. From an investor's perspective, these arguments are pivotal to the macroeconomic stability of India and its ability to attract and deliver returns on capital. Over the previous two decades, this has been an enabler of India's quartile-one equity returns relative to global markets.

As India's debt to GDP has declined over the last fifteen years, it has risen significantly for several other nations. India's resilient economic growth has led to a positive growth-interest rate differential and sustainable Government debt to GDP levels.



Source: IMF

Productivity

Productivity growth is one of the most critical indicators of an economy's health: it drives real incomes, inflation, interest rates, profits, and, ultimately, equity returns. While the value or risk in any investment lies in determining its ability to stay continually 'productive' [or innovative], the template is no different for a country. America's culture of productivity has driven its economic strength; its buoyant equity markets are an outcome. In contrast, European economies have been relatively less productive, given their policies and demographic limitations. As investors in India, we evaluate India's progress across a few enablers of productivity parameters. This will assist in appreciating probable outcomes a few years from here. For the sake of simplicity, we distill them into two broad areas:

A. Infrastructure

a) *Social, Education, and Health:* Over the next two decades, India's working-age population [25-64] will rise significantly, against a decline in all major economies, implying a significant improvement in competitiveness and consumption. Strides in better education and healthcare will abet incrementally better social and economic outcomes.

b) *Digital:* India's progress in creating a unique digital infrastructure of scale has been substantial. The ability of Aadhar and UPI to solve for authentication and allow the entire cycle of transactions to be virtually enabled has birthed a massive new transaction economy that has aided businesses across India. This has given companies that can consolidate demand, and market share, a competitive advantage.

c) *Physical:* India has rapidly expanded all forms of its physical infrastructure and continues to invest significantly in the same, creating one sizeable unified market. [Expanded further in the next section].

B. Policy

a) Manufacturing-led reforms, the key to furthering India's structural strengths
b) Others that abet increased economic activity across several sectors

Why is understanding the drivers of infrastructure and manufacturing essential? An expanding manufacturing base has been the most crucial driver of a nation's growth throughout modern economic history. The development of post-war Japan, ASEAN economies, and China indicates this without uncertainty. However, with its demographic and cost advantages, India has not fulfilled its manufacturing potential, primarily due to the absence of reforms. Limited investments in infrastructure and poor connectivity have hampered the efficiencies needed for industrial growth.

Infrastructure | Infrastructure is critical to linkages of an economy and widening the market size. Today, India is rapidly experiencing an infrastructural change, broadening the economy for all market participants. This is reflected across a broad spectrum, such as high-speed train connections, new freight corridors, new ports, and highways. The 50,000+km of national highway India has added in the past ten years is twice as much as it managed in the previous decade, while the number of airports with civilian flights has grown from 74 in 2014 to 148 this year, bringing one unified market closer to every participant.

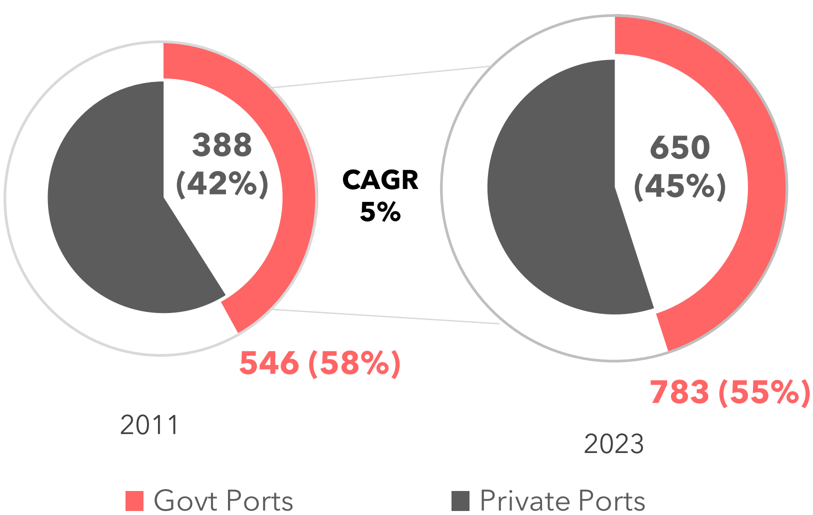
Road to Growth

Roads constructed/day (No. of Kms)

Targeted Logistics cost is <10% of GDP by 2030 from the current 14%

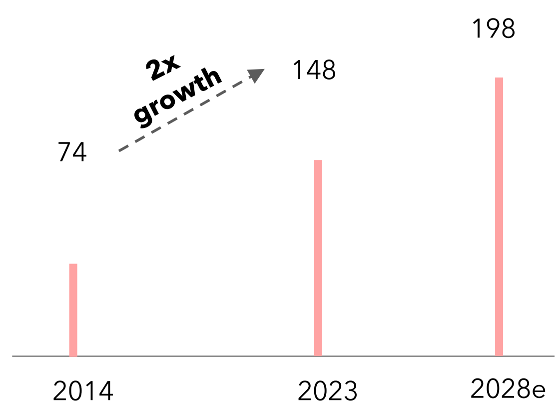
Port Infrastructure

Volumes in Indian Ports (MMT)



Airport Infrastructure

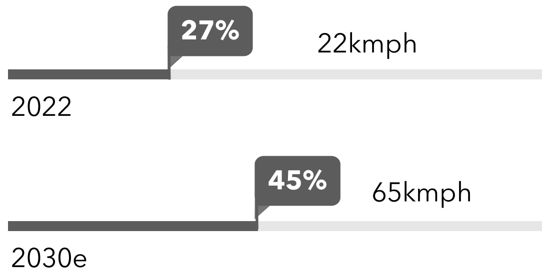
Number of airports



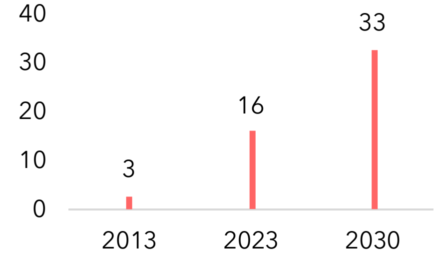
The number of domestic passengers has more than doubled from 60 Mn in FY14 to about 137 Mn in FY23

Rail Infrastructure

Share of railways in freight transportation



Number of Indian cities with metro rail connectivity



Dedicated Freight Corridor: 24hrs-48hrs lesser freight travel time between northern India & ports in western India

[Rs.10 lakh crore (3.3% of GDP) allocation towards infrastructure in the 2023-24 budget is an increase of three times from 2019; while the Ministry of Railways received its highest-ever allocation of Rs.2.4 lakh crore, approximately nine times the allocation in 2013-14]

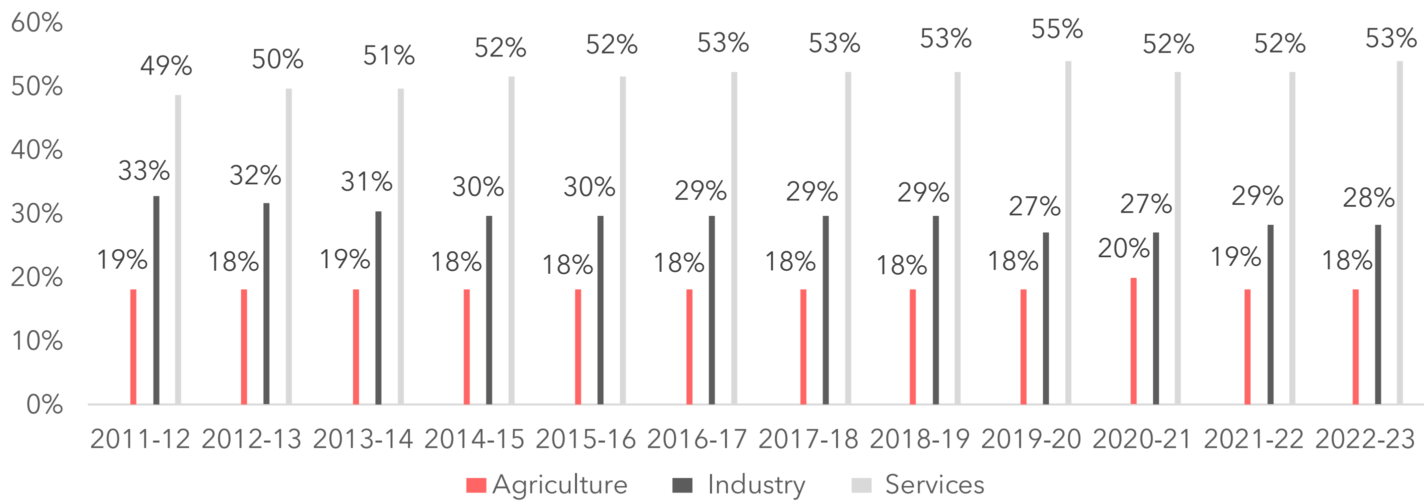
The consequence of lowering the cost of logistics, economies of scale, and access to markets are significant. The logistics cost in India, at 13% of GDP compared to 8% in the rest of the World, has made it difficult for Indian exports to compete globally and locally. With the support of significantly better infrastructure today, the ability to better India's growth rates is significantly robust. This has been bolstered by strides in India's digital economy -- UPI & Aadhar. The birth of a new transaction economy has accelerated momentum at a scale that many have not been possible before. This has given companies that can consolidate demand, and market share a competitive advantage.

Developments in these areas have led to increased logistics needs across the country, and players across the roadways, railways, and airway ecosystem are benefiting. Unifi has investments in this space via industry and cost leaders, who are driving efficiency for the sector as a whole.

Manufacturing productivity | A structural transformation in any economy witnesses a reallocation of growth drivers across its three main components: agriculture, manufacturing, and services. This transformation occurs in two stages: firstly, labour moves out of agriculture into manufacturing and services; and then labour moves out of agriculture and manufacturing into services. India's transformation on this count has been in the middle, where services took off firmly while manufacturing stagnated.

Since 2012, India has added $2 trillion to its GDP to become the fifth-largest economy in the World today. While India has played well to its strengths in the services sector, the share of manufacturing within the country has stagnated. As a result, India's share of global trade has dropped. At the same time, the increase in import reliance has resulted in an opportunity cost for the economy.

India, Share of GDP



Today, India is reworking its effort to accelerate the manufacturing mix via a Production Linked Investment scheme to make India more self-reliant. This is among the most significant policy tailwinds of recent times and an inflection point for the nation, if executed well, given its ability to increase employment and gain from the multiplier effects of domestic industry. This is beginning to result in an expansion of economic activity for several industry players, expanding the scope of their operations and re-investing at a profitable scale.

Sectors/Industry	Total outlays [INR Bn]	Expected/Actual investments [INR Bn]	Expected/Actual job gains
Mobile Manufacturing and Specified Electronic Components	410	110	2,00,000
IT Hardware	74	25	36,066
Critical Drug Intermediates; Active Pharmaceutical Ingredients (APIs)	69	54	12,140
Medical Devices	34	9	4,212
White Goods	62	62	5,522
Solar PV Modules	45	172	30,000
Food Processing	109		2,50,000
Telecom and Networking Products	122	33	40,000
Pharmaceuticals	150	150	1,00,000
Auto and Auto Components	261	799	7,60,000
Advanced Chemistry Cells	181	150	
Textiles	107	191	2,40,000
Steel	63		
Total	**1,687**	**1,754**	**16,77,940**

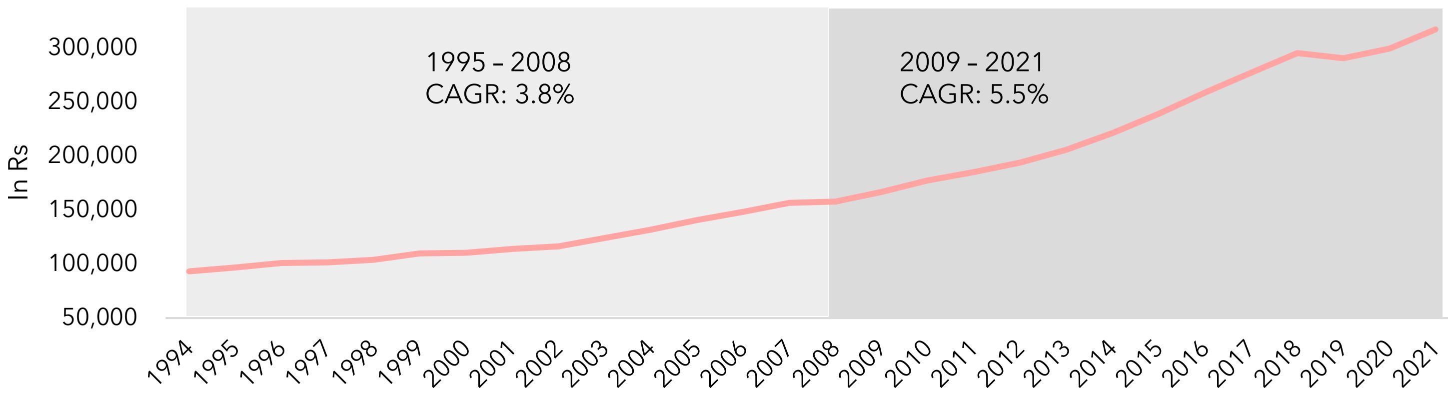
[Source: Motilal, PLI]

The overarching focus here is to encourage a combination of high-end manufacturing and import substitution to move the manufacturing sector's contribution to GDP to 25%. This will significantly affect all parts of the economy and show up as investment opportunities across sectors.

Unifi continues to evaluate investment opportunities in this space closely; and has exposure to pick-and-shovel players in the building products industry who benefit from the pace of new project developments. It is important to note that the financing needs of these developments percolate to various parts of the value chain, and the credit growth cycle in India is a beneficiary of this.

Demographic productivity | Over the past decade, India has made progress in labour productivity. Given its favourable demographics, the recent structural reforms around infrastructure and manufacturing will continue to aid productivity per capita.

Labor Productivity



Source: World Bank, RBI; Labour Productivity = Real GDP / Labour Force

Particulars	1995	2021	Growth
Labour force(Cr)	33.1	47.1	1.6X
Real GDP(Rs. Tn)	32.2	149.3	5.9X
Labour productivity, Rs.	96,712	316,698	3.7X
Per capita income USD	374	2257	6.1X

Why is labour productivity important? With increased access to higher education, India is expected to have a bigger tertiary-educated population than China and a significant rise in urbanization. As a result, income levels in India are expected to rise significantly, leading to a corresponding increase in consumer demand, further strengthening India's consumption-based economy. Beyond consumer goods, the other sectors that stand to gain from an acceleration in structural reforms include financials, discretion, and healthcare.

High productivity helps accomplish more with less. Over time, it has a powerful impact on all metrics, notably inflation, and lower interest rates, ultimately driving capital efficiency at a national and corporate level. This is eventually reflected in investment returns.

Others | Over the years, there has been a spate of reforms that have contributed to improving rates of systemic growth across several industries. We draw reference to the two most important ones.

Real Estate Regulation Act (RERA) Bill, passed in May '16, is among the most significant reforms in India. Among many others, updated construction information for home-buyers and separate bank accounts for construction costs are a few benefits of the Act. This was followed by SWAMITVA, a little talked-about reform aimed at providing rural citizens with the right to document their residential properties to be used for economic purposes. This has led to buoyancy across the construction industry per se, reflecting improved prospects for the building materials industry and off-take of credit linked to properties as collateral. These measures have led to buoyancy in the building materials industry and the retail lending segment, and Unifi has significant exposure to both these emergent areas.

Further, the Insolvency and Bankruptcy Code, enacted in May 2016 against mounting non-performing loans, has significantly bettered underwriting standards in the banking industry. Today, the systemic levels in asset quality are at an all-time low, along with healthy traction in the off-take of credit. This and better retail economic conditions have birthed a new credit cycle, providing the macroeconomic backdrop to Unifi's exposure to credit as an industry.

From an investment point of view, the beneficiaries will be those that execute well in the current phase of India's structural growth, improve the penetration of their products and services across India's markets, and gain market share from lesser efficient peers. A significant part of Unifi's investments shares these overarching attributes across strategies, apart from having fundamental bottom-up drivers of growth.

In our next quarter's communication with you, we look forward to continuing this dialogue and touching upon the other facets of India's productivity and economic sustainability.

Portfolio Construction

While Unifi's portfolio construction advice is an outcome of the bottom-up, it has drawn from a favourable macroeconomic environment. We reference the key components of the portfolio here, while quarterly performance of some companies is reviewed in the later sections.

Credit | c.25 % of the Strategy

Post-COVID, India has witnessed a sharp rebound in credit demand led by strong consumption demand, government-guaranteed loans to MSMEs, and higher working capital requirements by corporates. Over the past two years, retail loans have grown almost by almost 2x of overall loan growth. Early trends in FY24 signal strong system credit growth for FY24 as well. The health of the Indian banking system is robust and evident in decadal low non-performing loans and adequate capitalization. Successful implementation of the Insolvency and Bankruptcy Code has led to improved financial discipline

in the corporate sector. Overall, the profitability of the banking industry is trending to a cyclical high, aided by marginal credit costs. Credit costs are currently running lower than normalized levels, led by higher recoveries, and most of the banks have sufficiently provided for their NPAs.

Unifi's advice for exposure to larger banks augurs well with the improving outlook for the sector. Despite having a larger balance sheet, the investee banks have gained loan market share gains in FY23. In addition to the systemically best underwriting practices, their asset quality performance during COVID was better than the industry. We also advised to have exposure to a few small and mid-sized retail heavy banks. These banks are gaining incremental market share due to their size and product offerings (primarily retail). These banks have largely provided for their existing stressed loans. As these banks scale in balance sheet size, their profitability will improve significantly over the next 2-3 years. During FY23, the investee banks have gained market share and have exhibited loan growth in the range of ~17-28% vs. systemic loan growth of ~15%, while the net NPA of most of these banks is largely below systemic net NPA of 1%.

Building and Consumer products | c.25% of the Strategy

To enhance the country's growth potential and aid job creation, the government's thrust towards physical and digital infrastructure development has seen a multifold increase in the last decade. Residential development, construction of Metro's, and upgrade in the technology cycle are at highs. In 2023, India's top seven cities delivered the highest sale of units in over a decade [c.215,000], while railways and roadways have been beneficiaries of increased budgetary allocation. This has a significant flywheel effect on several players in the building value chain, from cables & wires, electrical durables, sanitary ware, and other building materials.

Unifi advised exposure to the largest cables and wires firm in the country, which has scaled revenues [almost 2x of peers], growing ahead of the competition and gaining market share. This is in addition to one of India's most profitable players in the consumer durables space with best-in-class margins and capital efficiency amid a change in management and improved execution. Given the execution and leadership of these firms in their respective categories, we expect them to benefit from this consolidation phase and growth in household & enterprise consumption. We also have advised a leading global IT products distribution company that addresses diversified IT product needs of retail and enterprise. The company's dominant and financial positioning gives it a significant competitive advantage in a business with high entry barriers. They are benefitting from the sector tailwinds of technology modernization.

Healthcare | 7-10% of the Strategy

At 1500 beds per million people, India is underinvested in healthcare, with structural deficiencies in supply, resulting in hospital infrastructure lagging the global median. Inversely, the industry has structural demand drivers with an increasing burden of lifestyle diseases in Urban India, rising insurance penetration, and improved affordability. This has created a supply-demand gap, reinforcing the need and providing potential for private hospital chains to put up appropriate infrastructure with the necessary investment. And as a result, it provides an opportunity for large players to scale up pan-India & consolidate market share.

Several pan India hospital chains expanded capacities significantly between FY13 to FY19 and are now treading a path of consolidation, focusing on sweating existing assets and adding capacities selectively through brownfield expansion. Considering the business's asset-intensive and long gestation nature to achieve optimum unit economics, the profitability growth lagged the volume and revenue growth in the CAPEX phase due to low occupancies in the new assets. Unifi's recommendation in the sector is with one of India's largest affordable healthcare providers, which will benefit from the consolidation phase. With an emphasis on advanced medical care and procedures, better utilization, and sweating of the existing asset base, the company has improved Average Revenue per Occupied bed [ARPOB] at 10% CAGR in the last 3 years with a negligible increase in the cost of healthcare services. The business has the longevity to grow with a strong and principled management team at the helm.

IT Services and Products | c.10% of the Strategy

Increased digital adoption in India has seen robust demand for cloud space from all hyper scalers [Microsoft, Amazon, Oracle, etc.]. As an annuity business, the prospects for re-sellers of cloud products in India are recurring. Globally, while there are pockets of a slowdown in discretionary IT spending, the development of digitally native applications continues to rise and is expected to be so for the next many years.

Unifi advised exposure to a firm with legs in the IT products space in India and the global IT services space. IT product re-selling contributes to about 25% of the firm's earnings and has grown 2x over the last two years. While in the IT Services space, they have grown from strength to strength, growing revenues by 50% over the last two years, supported by organic and inorganic initiatives. A change in their management in FY23 has paved the way for increased market share on the small base, and early signs are visible.

Others

The key components of Unifi's recommendations are diversified across firms benefiting from the financialization of savings, a key player in the defense sector aiding the forces' technical capabilities, and select firms in Chemicals, Consumption, Realty, and Hospitality that are poised to gain from investments made behind their execution in FY2023.

In Closing

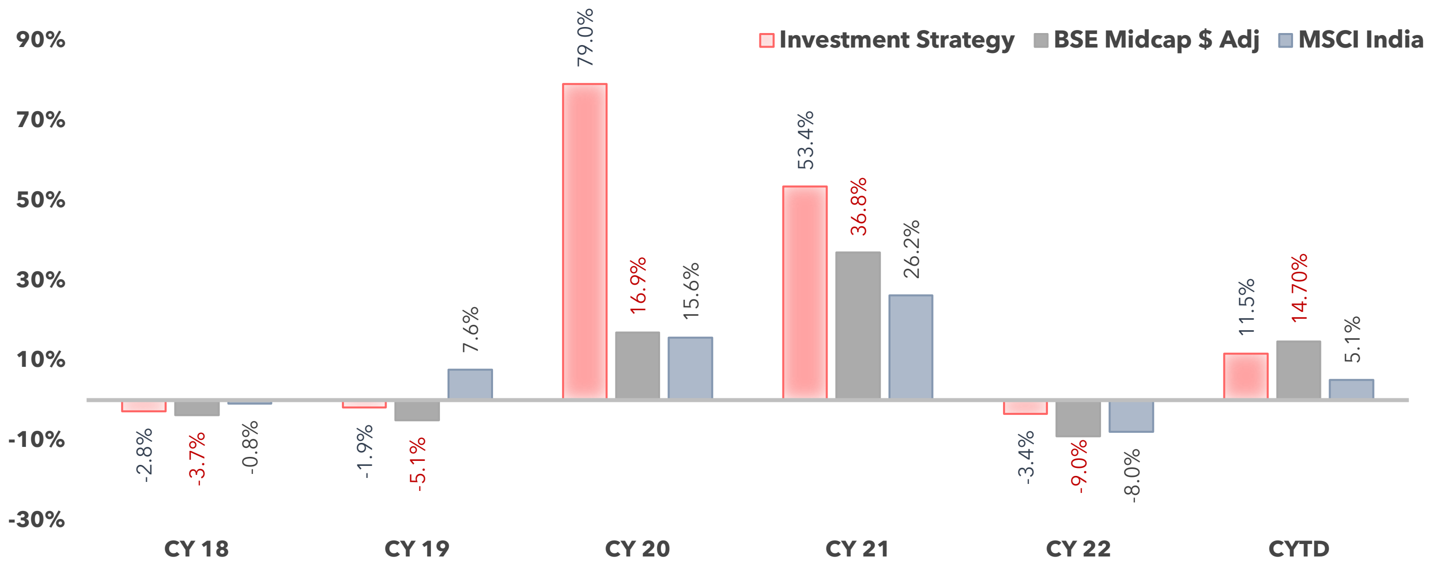
As we write this, India's equity market has scaled to all-time highs. Our approach of demanding growth at reasonable value has held us in good stead across cycles, and we continue to stand by those tenets. Resultantly, we continue to re-look at all our positions and right-size them, given how the risk/reward has changed over the past few months. We have advised to take the gains where our thesis has played out and reallocate them to positions where we believe the risk/reward is more favourable. While the exposure to larger firms has grown significantly, our framework of seeking value has remained steady.

Review, Q4 FY-2023 results and Q1 FY-2024 expectations

India follows a financial year from April to March. During the June quarter, the majority of the companies announced the annual results for FY 2023, except few exceptions where companies follow different FY. The absolute reading of the numbers suggests strength in the franchise of the leaders. The earnings salience of our recommended companies is broadly on expected lines, along with their initiatives in seed leadership for the times to come.

During the Q1 FY 2024, we continue to see mid-double-digit growth in credit and contraction in WPI inflation and thus the consolidation of interest rates with a softening bias. This should benefit the sectors consuming raw materials impacted by hyperinflation post covid led supply chain disruption. Further, as cost management in the developed world is gaining momentum, we are looking for opportunities which can benefit from outsourcing either manpower or manufacturing. We remain positive about the earning growth of the companies in our coverage and will continue to evaluate the changing scenarios.

RETURNS



Investment Strategy
BSE Midcap $ Adj
MSCI India
90%
70%
50%
30%
10%
-10%
-30%
CY 18
CY 19
CY 20
CY 21
CY 22
CYTD
-2.8%
-3.7%
-0.8%
-1.9%
-5.1%
7.6%
79.0%
16.9%
15.6%
53.4%
36.8%
26.2%
-3.4%
-9.0%
-8.0%
11.5%
14.70%
5.1%

Summary of results from the quarter Q4 - FY 2023

Company	Brief background and Investment rationale
Narayana Hrudayalaya	Narayana reported strong revenue growth of 29% YoY to Rs. 1,222cr, driven by both India and Cayman operations. India Business ARPOB continued to see an upward trend (21% YoY growth in Q4 ARPOB) due to change in the case mix, bed mix and improved productivity. The 3 new hospitals in India made a cumulative EBITDA Margin of 8.5% and the margin trend here is expected to further improve in the next few quarters. The Cayman business also had a strong revenue growth of 20% YoY with EBITDA Margin being stable. Consolidated EBITDA Margin came in at 22.6% in this quarter vs 18.6% in Q4FY22. Strong revenue growth coupled with margin expansion resulted in PAT of Rs. 174cr in this quarter vs Rs. 70cr in Q4FY22 (growth of 151%). The company has recently commissioned its Oncology block in Cayman, and this is the first full-fledged oncology department in Cayman. This will lead to higher revenue and improved profitability for the Cayman business. The company is also adding a 50-bed hospital in Cayman which would be operational by Q1FY25. On the domestic front, it is adding a green field hospital in Kolkata and debottlenecking Bangalore hospital. For Cayman and India, it would be incurring Rs. 1,100cr capex in FY24 and this would give the growth for the mid-term. Key risks include government policies in India and Cayman, margin contraction in the interim period of high capex.
Axis Bank	Axis Bank reported a loss of Rs 5,728cr as the bank written off entire goodwill from Citi Acquisition. Excluding this one-time impact, the bank would have reported a PAT of Rs. 6,761cr vs Rs. 5,853cr in Q3FY23 and Rs. 4,118cr in Q4FY22. Credit growth excluding Citi was strong at 7.5% QoQ / 15.8% YoY. Margins (excluding one-offs) improved by 1bps QoQ to ~4.2%. Management indicated that they have passed on the entire improvement in repo rates, have not booked new business at the expense of yields and there may be some lag effect in yields compared to other banks. The cost to asset ratio remained elevated at ~2.4% (+7bps QoQ) as the bank remains committed to investing in focused business segments over the medium term. Asset quality continues to improve with moderation in GNPAs & NNPAs. The bank now has one of the lowest nets NPAs across all major banks. The bank has been reporting normalised gross slippages of ~1.9-2% for the past 4 quarters. However, net slippages continue to be running below normalized levels led by higher recoveries. Credit cost came to merely 15bps vs 77bps in Q3FY23. Axis Bank carries unutilised provisions of ~60bps of loan book. The credit growth has been strong for the industry with market leaders growing at a higher than industry rate in FY23. We expect industry credit growth to be strong in FY24 and Axis to benefit from the same. Key risks would include a deterioration in asset quality leading to higher-than-expected credit costs and lower-than-expected loan growth.
Sonata Software	Sonata's IT Services revenue came in at $66mn (the acquisition of Quant was integrated for 20 days), up 4.5% QoQ and 18% YoY. The segment's operating margins, at 21.7%, were flat QoQ, after absorbing a large part of the wage increases (senior management increment is due in Q1). Their India business continued high growth (+21% YoY) on the back of healthy demand for cloud and cloud native applications and products. The company won a landmark $160m (10-year) deal in Retail CPG/Manufacturing which will ramp up partially in Q1 and then fully in Q2, keeping the growth rates robust for FY24 as well.

	Sonata won three large deals (including the one discussed above) in the quarter and expects momentum to remain strong. Supply side pressures have also eased, benefiting Sonata in executing assignments at high margins. In Q4 attrition slid to 12%, close to pre pandemic levels. Sonata's strength lies in three verticals: Hi-Tech/TMT (31% of revenue), Retail CPG/Manufacturing (42% of revenue), and Healthcare (11% of revenue). This will support margins for the year, and helped by falling attrition which is a sector phenomenon today. Sonata has aspired to achieve $500mn in revenues by FY 2026 with margins of early 20s, which if executed well, will place them in the top quadrant of the industry. Key risks: Slowdown in the USA and Europe and cuts in discretionary IT spending by enterprise clients.
State Bank of India	SBI's 4QFY23 results were better than expected largely due to higher treasury gains, higher miscellaneous income (should be recovery from w/o acs) and lower credit cost. PAT came at Rs 16,695crs vs Rs 14,205crs in 3QFY23 and Rs 9,114crs in 4QFY22. Credit growth improved sequentially to 4.6% QoQ. SBI reported loan of 17% YoY which is higher than system loan growth of ~15% for FY23. Margins improved by 10bps QoQ to ~3.6% led by better spreads. Management endeavors to maintain margins at the current level in the near term despite some pressure from deposit rates as the bank has some excess liquidity and headroom for higher C-D (Credit-Deposit) ratio. However, we continue to build on some margin contraction in FY24 led by headwinds from higher cost of deposits. SBI's asset quality further improved with sequential moderation in GNPAs & NNPAs. SBI has been reporting one of the lowest gross & net slippages across the banks over the past 6-7 quarters. The bank reported gross slippages of ~0.4% and net slippages of -0.1% for 4QFY23. SBI reported credit cost of ~40bps vs 77bps in 3QFY23. Key risks would include lower-than-expected loan growth, deterioration of asset quality leading to higher-than-expected credit costs and higher treasury losses.
Redington	Redington is a global distribution company with presence across 40 markets and covers the entire gamut of IT products, Smartphones, and offers service & solutions across Managed, Cloud, Logistics. The company partners with 290+ brands associations and services 43,000+ channel partners. Redington reported strong revenue growth of 26% YoY at Rs. 21,849cr. Gross margins were marginally higher sequentially at 5.8% vs 5.7% in the last quarter. However, this was offset by higher Opex leading to a lower EBITDA margin at 2.5%. The higher Opex sequentially was on account of higher investments towards building capabilities in cloud/services space and towards forex losses. The working capital cycle has normalized at 36 days for FY23. Higher Opex and higher tax resulted in a decrease in PAT to Rs.310cr YoY. The tax outgo was higher at 28%. From a capital allocation standpoint, the company's return ratio is healthy with ROCE being more than 25% and the company continues to pay out 40% of PAT as dividends which results in a dividend yield of c.4%. We like Redington given that they are amongst the top 2 ICT distributors across the markets it operates in. The company's dominant positioning and financial muscle give it a significant competitive advantage in a business that has high barriers to entry. Redington has created a strong services business - both in the 3rd party logistics business and the high margin cloud business. These businesses as they continue to gather scale have the potential to be valued

	separately too. Redington' broad portfolio and relationships with vendors across segments allows for balanced growth and reduces vendor concentration. Redington has demonstrated robust risk management practices over the years that helps better manage credit, inventory, and currency risks. Key risks would arise from high interest costs in a rising interest rate environment, slowdown/delays in the high margin enterprise business and lower than expected margins.
ICICI Securities	ICICI Securities' revenue at Rs. 885cr in Q4 FY23 were flat yearly and sequentially. Cash ADTO volumes were lower by 21% YoY and lower by 6% QoQ which impacted overall broking revenues by -5% QoQ (ISec' broking revenues are more dependent on cash volumes). The focus continues to grow derivatives volumes and gain market share. The broking allied offerings such as margin trading, prime and other fees supported revenue growth supported the decline in broking segment decline. To ensure the lending book AUM remains stable, Isec deliberately did not pass on the complete interest rate hike to customers and chose to absorb the impact. This resulted in the lending book revenues growing 1% QoQ while the interest expense was up 14% QoQ. The benefit of this strategy has resulted in a ~4% QoQ growth in customers. The total retail and allied income were Rs.492cr, marginally lower than the previous quarter. Distribution revenue at Rs.193crs for the quarter was up 14% YoY and 16% QoQ on back of healthy growth across Mutual Funds and Life Insurance. Isec continues to focus on building the distribution revenues to reduce cyclicality. Corporate finance revenues are dependent upon primary issuances and stood at Rs.13cr for the quarter. This segment is cyclical. Overall, higher interest expenses led to a PAT of 263cr. ISec continues to make investments in technology and branding and expects to gain market share in the derivative segment that has benefited the discount brokers. The market share improvements in derivatives are visible quarterly, but the pace needs acceleration. Profitability for the quarter was slightly impacted as the increase in interest cost has not yet been fully transmitted to customers. The transmission of rate hike to customers is expected to take place in the subsequent quarters. We like the business resilience given the improving share of non-brokerage revenues in sales, technology leadership, continuing consolidation of the user base, high RoE of c.40% and dividend yield of c.4%. Key risks would arise from a downcycle in equity markets leading to lower volume turnover and lower deal flow for corporate finance. The near-term risk across the industry remains SEBI' pending decision regarding total expense ratio (TER) - this may impact distribution revenues and institutional brokerage. This is a work in progress yet.
Hindustan Aeronautics	HAL reported revenue growth of 8% YoY to Rs. 12,495cr. EBITDA increased by ~30% YoY to Rs. 3,245cr. Over the last few quarters, the company's Repair & Overhaul [ROH] business has grown at 20%+ while the manufacturing business execution has been weak. In FY23, ROH business grew by 28% from Rs. 17,077cr to Rs. 21,894cr while manufacturing business declined from Rs. 7,375cr to 4,740cr. Q4 23 Gross margins was at 62% vs 60% YoY due to the change in mix towards ROH. Reported PBT was up 10% while the reported PAT was down 9% YoY to Rs. 2,830cr due to higher one-off take refunds in the base quarter. HAL's primary role today is as an assembler of aircraft to develop a domestic eco-system of defense Aircraft manufacturing vs just import reliance. HAL does this via the transfer of technology (ToT) agreements. Over years of handling various ToT, and with the support of India's own Aeronautical Development Agency, HAL has built good domestic manufacturing capability now. The government's stance to indigenize the manufacturing of defense

	equipment will lead to HAL's manufacturing business growing at a healthy rate post-FY24. The company has an order book of Rs.81,000cr as of Mar-23 with an inquiry pipeline of ~Rs. 90,000cr worth of orders in the next 18 months. In addition, there has been indication of building an export business as well which has negligible contribution as of now. Key risks to investment could be any policy changes relating to the Defense sector and delay in the execution of key platforms.
Godrej Consumer	Godrej Consumer reported revenue growth of 10% YoY to Rs. 3,200cr. India business reported 12% YoY revenue growth and Indonesia business witnessed a turnaround with 8% YoY growth. Africa business growth has been weak in this quarter at 7% YoY revenue growth, and this is due to elections impact in Nigeria. Consolidated gross margin improved sharply to 52.9% vs 51.1% in the last quarter as the key raw material prices corrected (palm oil and crude). The company has used part of its gross margin benefits in higher A&P spends and accordingly reported EBITDA margin of 20% in this quarter. The company registered PAT growth of 24% YoY to Rs. 473cr in this quarter vs Rs. 383cr in Q4FY22. Godrej Consumer always had great brands (Good Knight, Cinthol, Godrej No.1, Hit, Godrej Expert and Aer) but the execution was weak in the last few years as management focused more on international business. The company appointed Sudhir Sitapati as new CEO in 2021 and he comes with rich experience in HUL. The new CEO has been working on various initiatives like filling the gaps in the product portfolio, cutting down unnecessary SKUs, cost efficiencies etc. and this is playing out now and we expect the turnaround in the business to continue. Key risks include a steep increase in raw material prices, demand slowdown and any changes in the senior management.
Oberoi Realty	The residential real estate market is divided into 3 segments: a) Affordable Housing (Real estate players make 10-15% EBITDA Margin); Mid segment (20-25% margin); Premium (>40% margin). Oberoi is present only in the premium segment and makes 40-50% EBITDA Margin (highest in the industry). Till now the company is present only in the MMR region and has key projects in Goregaon, Mulund, Borivali and Worli. Oberoi reported areas sales of Rs. 673cr in this quarter i.e., a decline of 6.7% QoQ and 26% YoY. The area sales for this quarter and FY23 got impacted due to no new launches in second half. The company didn't have any new launches in H2FY23, and this impacted the sales numbers. For the full year (FY23), company registered sales of Rs. 3,200cr i.e., a decline of 17% compared to FY22. The company has land parcel in Thane to develop 15 Mn sqft and this is expected to be launched in phases starting from FY24. Company would also be launching additional towers in Goregaon and Borivali in FY24. Given the launch momentum and strong industry demand, we expect the company to register higher sales in this year. The success of Thane would provide the company with multi-year growth opportunity as it has huge land parcels. The P&L for real estate companies has a lag effect as revenue must be recognized only after handing over the property to customer. Accordingly, the company reported revenue of Rs. 4,193cr and PAT of Rs. 1,905cr for FY23. Key risks: Delayed projects launches, slowdown in the demand.

ICICI Bank	ICICI reported PAT of Rs 9,122crs vs Rs 8,312crs in 3QFY23 and Rs 7,019crs in 4QFY22. ICICI Bank continued to gain loan market share in FY23 as well. The bank reported a loan growth of 4.7% QoQ / 18.7% YoY. During FY23, ICICI's retail book grew by ~21%, higher than any other large private bank. During 4QFY23, margins further improved by 25bps QoQ to 4.9% in 4QFY23 led by repo rate hikes, better yields on the GSec book, and repricing of the floating rate bond portfolio. Cost ratios have been increasing steadily over the past 4 quarters. Management indicated that there is good market opportunity, and the bank will continue to invest for the future. The bank continued to witness moderation in GNPA & NNPA led by higher recoveries. Gross slippages moderated to 1.8% vs 2.4% in 3QFY23 while net slippages declined to Nil vs 0.5% in 3QFY23. The bank has been reporting minimal net slippages for the past 6-7 quarters leading to lower NPA provisions and this has enabled them to make contingent provisions to strengthen the balance sheet for future uncertainties. The bank has been providing such contingent provisions in the range of Rs 1,000-1,500crs (20-25bps of loans) over the past 5 quarters. The bank now has the highest contingent provision across all PSU & private banks at ~1.4% of the loan book which is higher than the expected credit cost for FY24. Key risks would include lower-than-expected loan growth, deterioration of asset quality leading to higher-than-expected credit costs, and higher treasury losses.
DCM Shriram	DCM Shriram reported flat revenue at Rs. 2,849cr. EBITDA and PAT recorded a YoY degrowth of 45% and 53% at 346cr and 187cr, respectively. The revenue and profitability decline in the current quarter were primarily driven by the Chloro-alkali segment. The fall in construction activities and recession worries globally continue to impact the PVC demand. The same has been reflected in global PVC price which has witnessed a decline of ~35% on a YoY basis. Also, a significant capacity addition for Caustic soda in the domestic market coupled with low global demand has impacted ECU caustic realizations, which have declined 17% on a YoY basis. Hence, the current unfavorable demand-supply dynamics and elevated energy costs have led to a decline in profitability for the Chloro-alkali segment. The sugar segment registered a 25% expansion in volumes with the rebase of opening inventory and allotment of export quota. The distillery business delivered volumes of 3.5cr liters vs 3.3cr liters YoY. As a result, the operating profitability in the sugar segment was strong with ~20bps yield improvement in the current sugar season and record high sugar export prices. The rest of the next season will continue to be better for the sugar segment in terms of volumes and profitability with global sugar prices at record levels, domestic prices inching up, and as the company commercializes new ethanol capacity. Agri-business had performed steadily across verticals. Fenesta's exceptional business performance has continued while the Cement was a drag due to input cost inflation. The company is placed for a sustained growth trajectory with an improved balance sheet and cumulative capex of Rs. 3500cr to be commercialized in the next 9-12 months. Key risks: Unexpected regulatory developments in Sugar/Ethanol business and a decline in the strong Caustic Soda cycle in the international market.
Kewal Kiran Clothing	Kewal Kiran delivered revenue growth of 18% YoY to Rs.200cr, aided by strong sales of the top wear category. The company delivered well across the retail and MBO channel, with 40% & 7% YoY growth respectively. They added 15 new stores in the quarter and are on track to double their store count to 700 stores in the next three years. EBITDA margins improved to 19%

	compared to 18% YoY, on account of operating leverage. As a result, EBIDTA was up by 21% YoY to Rs.39cr. Overall, PAT was up by 27% YoY to Rs.32cr. We like the business as it stands out on the retail spectrum, with control over manufacturing and branding, enabling them to keep most of the margins at their end. In the last decade, they have followed financial prudence and capital allocation discipline and returned 75% of earnings to shareholders. We believe that the rise in household incomes will keep up the demand for discretionary clothing allowing the branded players to grow higher and gain market share. Key Risks: Competitive Intensity from MNC brands and private labels of large format stores.
Infosys	Infosys reported a 3.2% QoQ decline in revenue in Constant Currency after marginally increasing its full-year revenue growth guidance in the prior quarter. During the quarter, Infosys saw unplanned project ramp-downs for some clients and delays in decision-making, which resulted in lower volumes during the quarter. The weakness persisted through January and February followed by some stabilization in March. For the year ahead, the broad assumption around growth is in the range of 4-7%, implying a 1.7-2.9% compounded quarterly growth rate. The top end of the band assumes closure of multiple cost take out mega deals. As consumption of digital products and services around the world continue to remain reasonable, it is believed that earnings are close to bottoming out. Key risks: Slowdown in the USA and Europe and cuts in discretionary IT spending by enterprise clients.
Crompton Greaves Consumer	Crompton Greaves Consumer reported a revenue growth of 4% YoY to Rs.1,604cr, on account of the performance of ECD division, which grew at 8% YoY. This was offset by the weakness in the lighting segment, which dropped 12% YoY. Gross margins were up 80 bps YoY to 30.7% on account of premiumization and material cost cutting. However, EBITDA margins were down 250 bps YoY as the company spent more on advertising to gain market share. As a result, EBITDA fell 14% YoY to Rs.197cr. Overall, PAT came at Rs.132cr vs Rs.176cr YoY [down 25%]. The potential recovery in the lighting segment and ramp-up of the appliance's portfolio post the acquisition of Butterfly, provide good visibility for earnings growth going forward. Crompton is amongst India's most profitable players in the consumer durables space with best-in-class margins, and capital efficiency. We continue to like the company given their execution and expect them to benefit from this phase of consolidation and growth in household spending on durables. Key risks to the investment could emanate from a drop in consumer sentiment, and steep inflation in raw materials.
NIIT learning	NIIT's business has been demerged into two separate entities NIIT ltd (Skilled & Careers Group-SCG) and NIIT learning systems ltd (NLSL-corporate learning group -CLG) effective 24th May'2023. NLSL to get listed separately. NIIT ltd revenue dropped 36%/26% QoQ/YoY to Rs.60cr as attrition fell back to pre-Covid levels, fresh intake and re-training needs have fallen steeply. And reported EBITDA loss of Rs 95cr vs breakeven YoY. Training volumes are expected to pick up gradually during FY24. The NLSL reported revenue of Rs 386cr, up 6%/30% QoQ/YoY with organic growth of 6% YoY. EBITDA came to Rs 95cr with a margin of 25%, up 70/3 bps QoQ/YoY. PAT came at Rs 54cr, up

17% QoQ and flattish YoY. Given existing contracts in hand and outlook, there is visibility of about 20% growth in CC terms in FY24. The revenue mix by sector is 26%-Tech & Telecom, 17%-Consulting, 10%-Healthcare, 9%-Energy, 8%-BFSI, 9%-Aviation, 21%-others.

Post the de-merger, capital efficiency of NLSL emerges at RoE of 30% and earnings growth visibility of around 20%. The result of NIIT ltd (domestic business) was muted in this quarter but the outlook is to deliver 10% growth with mid-single digit margins.

Key risks: Global economic slowdown and cuts in discretionary spending by enterprise clients.

SUMMARY OF PORTFOLIO VALUATION

As on June 30'2023	FY 24E
Wt. Avg PE	21.5x
Wt. Avg PB	4.0x
Wt. Avg ROE	22%
Wt. Avg Mcap	$ 19,918 mn

Rangoli India Fund	Market Cap (USD Mn)	PBT (USD Mn)		YoY	PAT (USD Mn)		P / E	RoE (%)
	As on 30th June	Q4 FY22	Q4 FY23		FY 23	FY 24E	FY 24E	FY 24E
Axis Bank	**37,067**	**720**	**(384)**	**-153%**	**2,690**	**2,971**	**12.5**	**18%**
CG Consumer	2,258	26	21	-20%	58	62	36.2	19%
DCM Shriram	1,716	71	35	-51%	114	127	13.5	16%
Godrej Consumer	13,475	47	68	45%	214	264	51.0	15%
HAL	15,457	314	348	11%	543	648	23.9	23%
ICICI Bank	79,696	1,292	1,674	30%	3,888	4,470	17.8	17%
ICICI Securities	2,395	55	43	-22%	136	145	16.5	37%
Infosys	67,552	919	1,032	12%	2,939	3,158	21.4	32%
Kewal Kiran	405	4	5	27%	15	17	24.2	24%
Narayana	2,474	15	26	80%	72	82	30.0	27%
Oberoi	4,364	40	48	18%	232	226	19.3	14%
Polycab	6,487	52	70	33%	156	182	35.6	25%
Redington	1,772	54	55	2%	170	180	9.8	22%
SBI	62,315	1,689	2,857	69%	6,123	6,654	9.4	18%
Sonata	1,725	17	18	10%	55	67	25.9	43%

The positions discussed here constitute the key investments under the strategy. Please do not hesitate to contact your relationship manager or advisor to discuss any of these stocks in further detail and our rationale behind the same.

RISK MANAGEMENT

While the environment is buoyant for India in the longer term, in the shorter to medium term, the aftereffects of unforeseen economic linkages from a recessionary West may be a risk. While India remains a largely domestic consumption-oriented economy, a rapid worsening of the economies in the West may affect their balance of trade with the World [including India] in the immediate to medium term. India's Current Account Deficit and foreign exchange reserves may be under pressure if energy prices remain elevated and rise. The recent softening of energy and commodity prices will assist India's macroeconomic case, but there remains the prospect of second or third-order impact from global macroeconomic and geo-political shocks.

Risk	Level	Mitigants
Concentration Risk	Fund	At the portfolio level, such risks are minimized by limiting the aggregate exposure of the portfolio to such investments to less than 10% of the value at the time of investment.
Foreign Exchange Risk	Fund	Fund has invested in only Indian Listed companies and hence the fund's investments do not face any foreign exchange risk at the Fund level.
Leverage Risk	Investee Company/Fund	Fund has not taken any leverage at the Fund level. Except for financial companies, most of the investee companies in the strategies carry nil to moderate debt on their balance sheets with a track record of having managed leverage well in the past. Their leverage is monitored regularly.
Realization Risk	Investee Company/Fund	High Impact cost, due to thin trading at the time of buying or selling is endemic to small & mid-caps. We plan our investment decisions, the size of the investment and trading strategies to minimize the realization risk.
Strategy Risk	Investee Company	Investments are evaluated from a bottom-up and top-down perspective. The fund investments align with the segments of the economy that are emerging and companies that have characteristics which make them the dominant participants in their industry. The investments are assessed through a detailed financial model that captures historical performance and forward estimates based on publicly disclosed documents. The investment team rigorously undertakes quarterly diligence for any change in the investment thesis.
Reputation Risk	Investee Company	Company selection starts with rigorous fundamental analysis and a historical performance review supported by a detailed financial model constructed internally. We have an internally designed governance framework vetted over many years. This governance framework helps us in evaluating companies that meet our internal guidelines. We evaluate the investee companies both at an absolute and relative level. Periodic maintenance diligence of management/ financials has been done for Investee companies.

Extra Financial Risk	Investee Company/Fund	We avoid investing in companies with a known history of corporate governance issues. If such an issue arises in an existing investment, we stop additional purchases and start optimally exiting the investment. Our governance framework helps us in identifying any lapses in corporate governance. We actively monitor all publicly disclosed documents regarding ESG [Environmental, social, and corporate governance]. Any reported misconduct is evaluated by the investment committee for further action.
Geopolitical risks	Investee Company	Geopolitical tensions globally can disrupt the supply chain in the region. This might have a non-linear impact on business.
Raw material inflation	Investee Company	India continues to be dependent on the supply of feedstock whose pricing is global in nature. Key categories would be crude, metals, minerals, and natural commodities. Sharp movement in their underlying prices will have a short-term financial impact on the companies. The situation in China [political] has the potential to disrupt the supply chain of a few of our investee companies.
Key Man Risk	Investee Company	Small and mid-caps are frequently managed by a key promoter/person on whom the business is completely reliant and without whom the business would be materially inferior. We generally avoid such names and in cases where we make any exceptions, the aggregate exposure of the portfolio to such investments is limited to less than 10% by value.