UNIFI QUARTERLY REVIEW

Q2 FY22

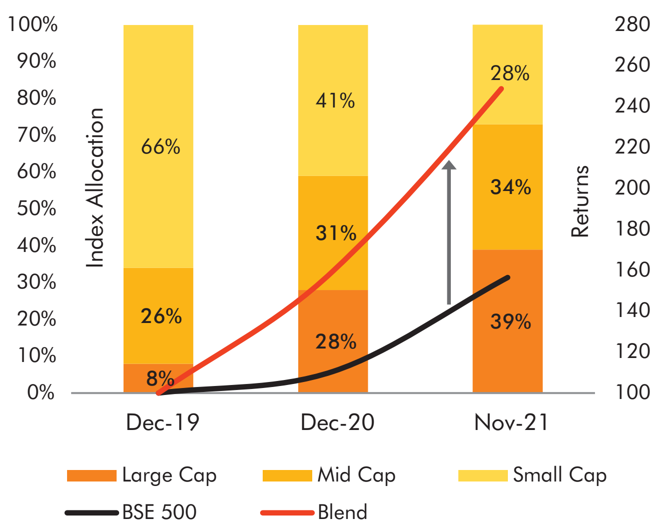
HOW ARE WE THINKING?

How are we thinking?

Unifi's approach to investment management has always shunned the comfort of consensus in pursuing absolute returns. As India's equity stack continues to scale all-time highs, our underlying principle of seeking absolute growth at reasonable valuation remains a constant. Resultantly, we have re-looked all our positions and right sized them, given how the risk/reward has changed over the past few months. We have taken the gains where our thesis has played out and re-allocated them to positions where we believe the risk/reward is more favorable.

A key trend visible across your portfolios today is the build-up in exposure to significantly larger firms. How did we think about this? Was this seeking comfort in the wisdom of the crowds? Or a bottom-up conclusion similar to that of our traditional approach? In our industry, oversimplification is a gross challenge as it concludes without the depth required to build a significant position and stay the course of that thesis. For example, there are a few ways of looking at a firm like State Bank of India. You could look at it as a large cap that is likely to move with the index and, to that extent, participate in what the market gives you. Or look at it as a cyclical that is poised for recovery. Or select the same name bottom-up, through layers of research, drawing insights from the fundamental strengths that SBI has demonstrated over its past, with an eye on its weakness. This strength of conviction shows up in allocation, and Allocation x Upsides = Absolute Returns.

The following chart depicts the change in capitalization of Unifi's Blend portfolio, along with how returns have followed in the same cycle.



The similar infographic for the other strategies is included in the respective sections.

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In most cases where we have booked our gains, prices continue to remain at elevated levels. Why have we then increased the prospect of our own reinvestment risk? Warren Buffet summed this up in the best manner possible: the line between investment & speculation becomes blurred when most investors have recently enjoyed triumphs. Nothing sedates rationality like large doses of effortless money. After a heady experience like that, normally sensible people drift into behavior akin to overstaying their welcome, which seldom ends well.

Since ideas are invisible, people underestimate the extent to which they can go in and out of fashion. Accordingly, we don't risk overstaying our thesis.

Review, Q2 FY-2022

While asset pricing is based on smooth parabolic models [Gaussian], prices do not represent linearity in the real World. They are more like bird scrawl. Recent price moves in commodities (across Oil, Coal, Iron ore, Copper, and Aluminium to name a few) can anything but be captured by traditional approaches to modeling. The resultant decline in their underlying equity value is sharp, severe and the portfolio impact acute. In cases where we had exposure to the commodity basket, we have right sized our allocation.

On the lending side, we are looking at the beginning of a new credit cycle. The incremental impact of restructurings and big-name corporate defaults is largely behind us. With leaner corporate balance sheets on the back of strong cash flow generation, improved collection efficiency, and faster pace of recoveries vis-a-vis slippage, the lenders in your portfolios are well-capitalized to now focus on growth with improved margins.

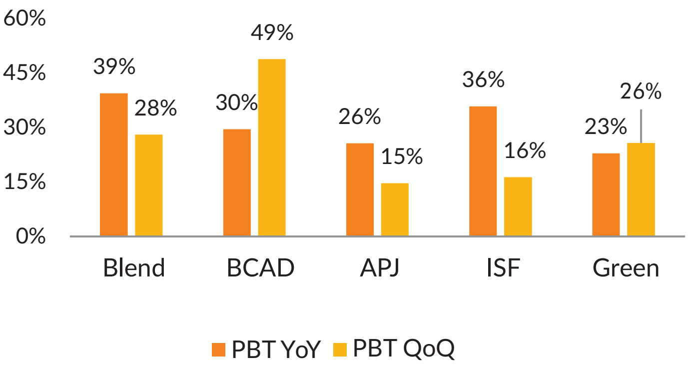
With the benefit of reforms, decade low interest rates, multi-year unit price stagnation, pandemic related tailwinds and rising incomes, the residential real estate space has seen increased sales velocity. At the same time the commercial office real estate with pedigreed landlords and multinational tenants has been able to withstand the covid related work from home headwind and is well placed to make a strong comeback. The resulting growth in these sectors has been well captured in your portfolios.

Increasing per capita computing power at an enterprise and consumer level continues to take technology spending higher. Deep computing around the current generation of the technology stack is re-architecting traditional system architecture to cloud-native applications. We see sustained tailwinds in these areas for a lot more time to come.

India's households continue to consume with enthusiasm. [Relatively speaking] Despite acute commodity inflation, consumer majors have shown remarkable resilience in cost pass-throughs, and demand salience has not been an issue. While we are cautious of supply-chain challenges and the persistence of inflation, we believe the medium-term impact on the portfolios is transitory. We remain optimistic about the consumer-facing names in your portfolio.

Our underlying principle of demanding growth at reasonable value has held us in good stead and we continue to stand by those tenets. We have moved out of names where our investment thesis played out and valuations ran ahead of fundamentals. As you can see in your portfolios, we have switched to names that are likely to deliver strong earnings growth in the current cycle, including those benefiting from a broader regulatory and policy environment, irrespective of where the benchmark indices trade. Overall, we are comfortable with the earnings salience of our portfolio companies and what they are doing to seed leadership for the times to come. Our portfolios continue to build concentration in seeking such leadership.

YoY and QoQ PBT Growth [Ex - BFSI]

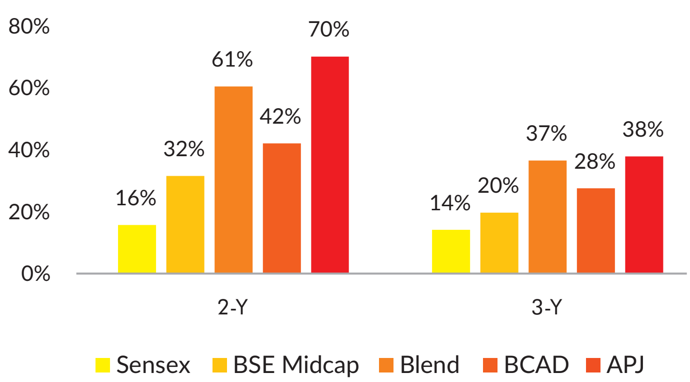


Adjusted for one-offs

In closing

We rate the ability to re-think, unlearn, and not falling for first instinct fallacies very highly. It is not as much seeking new answers that are important but staying with the question. It helps us unravel newer dimensions. This is more important than ever as narratives de-emphasize the quality of information over the desire to be entertained. We continue to be driven by doing what is right, backed by data, and diligently being at the question as a process. Everything else is an opinion.

TWRR Returns



As of 24th Nov 2021
Since inception time weighted returns for ISF is 37% compared to 33% for the BSE Midcap

An outline of each of our investment strategies has been presented in the following sections with a summary of performance for Q2 of FY22. Individual portfolios will vary in holdings and proportion based on the timing of your investment with Unifi. For a detailed review of your portfolios, please do not hesitate to contact your relationship manager.

Review of Strategies

We have captured an outline of each of our investment strategies in the following sections with a summary of how the fundamentals of our key holdings have played out in Q2 FY22. Tail positions which are on their way out of the portfolios have not been discussed. Individual portfolios will vary in holdings and proportion based on the timing of your investment with Unifi. For a detailed review of your portfolios, please do not hesitate to contact your relationship manager.

DVD / Blend

The DVD / Blend fund strategy continues to cherry pick ideas from across the six distinct themes managed by Unifi, thereby investing in "the best of our best" and participating in opportunities across the breadth of the market. The ideas represent a mix of emergent themes, corporate actions, and fundamentally attractive bottom-up opportunities. We continue to focus on delivering superior risk adjusted returns from an absolute perspective.

As on Nov 30, 2021	FY 22E
Wt. Avg PE*	20.2x
Wt. Avg PB	5.4x
Wt. Avg ROE	26%
Wt. Avg Mcap	Rs.1,03,346

* Adjusted for one-off to make figures representative

BCAD

The fund continues to invest in sectors that are currently witnessing a shift in market share from the unorganized to organized players. While the lockdown related disruption can impact the near-term demand for consumption-based themes, as market leaders with strong net-debt free balance sheets, a majority of our investee companies are likely to see an increase in their market share, as marginal players find it difficult to operate in the new environment.

As on Nov 30, 2021	FY 22E
Wt. Avg PE*	26.8x
Wt. Avg PB	6.6x
Wt. Avg ROE	25%
Wt. Avg Mcap	Rs. 77,014cr

* Adjusted for one-off to make figures representative

APJ

The fund seeks to deliver absolute returns over a five-year horizon through investments in sectors that will benefit from the next stage of India's growth on the back of improvement in India's infrastructure, and policy climate. The APJ fund continues to focus on firms delivering manufacturing excellence broadly across technology, chemicals, pharmaceuticals, materials, and infrastructure in general.

As on Nov 30, 2021	FY 22E
Wt. Avg PE*	25.4x
Wt. Avg PB	6.6x
Wt. Avg ROE	30%
Wt. Avg Mcap	Rs. 93,291cr

* Adjusted for one-off to make figures representative

ISF

The Insider Shadow Fund invests in fundamentally sound companies where there has been an increase in the promoter holding. Typically, such an action by the controlling shareholder demonstrates their conviction that the company's growth prospects, or inherent value is not captured in the stock price at that moment. Unifi's proposition is to gain from the eventual balancing of the value-price mismatch in the market by identifying and investing in such companies after a detailed review of their fundamentals and corporate governance standards.

As on Nov 30, 2021	FY 22E
Wt. Avg PE*	18.4x
Wt. Avg PB	2.3x
Wt. Avg ROE	19%
Wt. Avg Mcap	Rs. 70,426cr

* Adjusted for one-off to make figures representative

Green

The fund continues to invest in sectors that will benefit from India's evolution towards a more "sustainable economy". The investment universe would comprise of well managed businesses offering best in class solutions to address challenges in the areas of Energy, Emissions, Waste and Water.

As on Nov 30, 2021	FY 22E
Wt. Avg PE*	22.4x
Wt. Avg PB	4.5x
Wt. Avg ROE	21%
Wt. Avg Mcap	Rs.47,317cr

* Adjusted for one-off to make figures representative

Disclosure of Underlying Risks

Risk	Mitigants
Coronavirus Impact	The impact from the ongoing Coronavirus outbreak in India and rest of the World can be multifold. The lockdown related slowdown in consumption can affect several sectors. Our investee companies have product & category leadership along the financial wherewithal to withstand temporary phases of demand slowdown and lead consolidation of demand. The BFSI sector could have heightened stressed assets for a certain period of time thereby impacting their profitability.
Geo-political risks	Any geo political tensions between India and neighboring countries can disrupt supply chain in the region. This might have a non-linear impact on business.
Raw material inflation	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.
Liquidity risk (in case of NBFCs)	The NBFC led liquidity crisis in India has had a systemic effect on the entire economy. Our investee companies have been able to tap diversified sources of liquidity on the back of their long-term track record of comfortable asset quality and asset-liability-management (ALM). However, sustained deterioration of the asset quality can continue to affect our holdings in Banks and NBFCs.
Foreign Exchange risk	The foreign exchange system continues to be guided by global developments. Our investee companies in the IT sector are subject to sharp movements in the USD and GBP. They mitigate the same via hedging, but there remains a portion of revenues that continue to be subject to the vagaries in fx movements. Most of our non-IT exposure is to companies that derive their revenues from the domestic market. The revenue from exports would be minimal for each strategy as a whole, and where relevant, are adequately hedged. A sharp depreciation in the INR will affect the import of feedstock (higher prices) which can lead to a brief moment of earnings-related volatility.
Leverage risk	Except for financial companies, most of the operating 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.Technology Obsolescence Technological changes can render the products/services of a company obsolete and thereby hurt its profitability and valuation. Such a risk is generally minimized by limiting the aggregate exposure of portfolio to such investments to less than 10% of value.

Risk	Mitigants
Governance risk	We avoid investing in companies with a known history of corporate governance issues. If such issue arises in an existing investment, we stop additional purchases and start optimally exiting the investment.Concentration risk At the portfolio level, such risks are minimized by limiting the aggregate exposure of portfolio to such investments to less than 10% of value at the time of investment.
Stock Illiquidity risk	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, size of the investment and trading strategies to minimize the costs due to illiquidity.
Key Man Risk	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 portfolio to such investments is limited to less than 10% by value.
Slowdown in global consumption	The wallet-share of the investee companies in the global manufacturing value chain, does not pose a significant risk of loss of business to their vendors. New and high growth areas such as Lithium-Ion batteries, EV vehicles are in relative infancy stage and have a strong growth curve ahead of them.
Softness in IT product spends	The convergence to digital software solutions is a 'must do' proposition and our investee companies have exhibited significant traction in competing in this space. A combination of their recent deal wins, and current bid pipelines bode well for their future.

Thank you for placing your trust in Unifi.

Sincerely

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