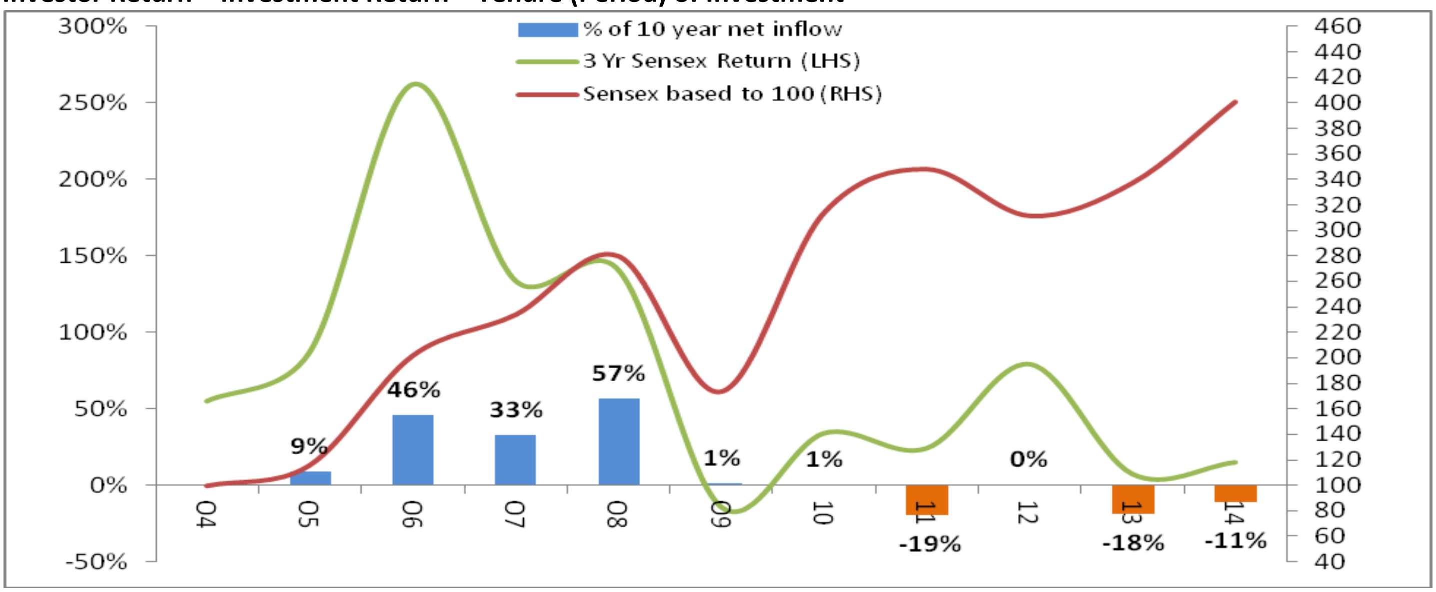
30th April 2014

Hi,

My previous communications usually began with performance tables, this time I would like to push the numbers for FY14 to last page. Don't worry; the numbers look decent both in absolute and relative terms. But, any judgment you take based purely on past performance may blur your vision of future return. I would like to communicate to you the merit of considering additional allocation to Indian equities and may be part of that to our themes, without camouflaging your thoughts with last year's performance numbers.

Let me begin with one simple but important observation about equity investing behavior in India. Last 10 years, ie between 1st April 2004 and 31st March 2014, Sensex has risen from 5590 to 22386, precisely 4 times. Including dividends, 100 invested have become 464 in 10 years, about 16.6%p.a. How much do you think, all investors in all equity schemes across all mutual funds have earned cumulatively during the period. I have answered this question below; pat yourself if you had answered it correctly. About 90% of the investors, wealth managers, banks I asked this question, answered it wrongly.

Investor Return = Investment Return * Tenure (Period) of Investment



Though the graph depicts the collective investment behavior of investors in Indian equity mutual funds, it is safer to presume the trend is similar across all equity products like PMS. When Investment return (Sensex) during the above period was about 300%, the investor return (IRR) was only 77%. Based on the equity AUM of Rs. 24,000 Cr as on Mar'04 and the cumulative investment of Rs. 72,000 crore spread over 10 years at different time intervals and the Mar'14 AUM of Rs. 1.65 Lakh crores, the investor's return (IRR) was arrived at 5.89%p.a. With daily AUM and dividend statistics, we can calculate the accurate IRR. Should investor's IRR be the same 16.6%p.a as in Sensex, the current AUM should have been Rs.4 Lakh Crores. At an average annual cost of 3%p.a including AMC, NFO costs, entry/exit loads that were prevalent during major part of the period, the cost incurred would have been about Rs.40,000 Cr to fund managers and brokers for value addition of fund selection or market timing over a simple index fund

While the fund manager is accountable for Investment Return, investor is responsible for his own return as he decides the timing, type and duration of the fund. The fund management industry shall also take a part of the blame in failing to advice the investor and help him make sensible choices. Like giving him a choice to invest by launching a mid cap theme in 2007 when previous 5 year BSE midcap index return was 300% and next 5 year return was NIL. Like launching Gold based schemes in 2012 when the previous two years return in Gold was 200% and next two year return was NIL, Like focusing on product launches in debt category in 2013 just before the cusp of a major equity up move coinciding with a fall in debt returns.

We are happy to share with you that Unifi's gross and net investor sign-ups in equities in 2013 was more than that of 2007, an usual number in the industry. We were fortunate as majority of our clients like you acted smartly by topping their commitment last year. Thank you.

Alignment of Interest: The only way an investor can help himself/herself is to ensure that there is alignment of interest while dealing with advisors. If you consider stock broker as an advisor and his revenue is only a small % of transactions you do, he will be keen to make you as active as possible. His income is directly proportional to your activity level and size of trades, not profits. If you expect fund/ wealth manager (whose revenue is a fixed % of funds) to advise you on entry or exit, there is an indirect conflict. They would be keen to accept your capital all the time and try to retain as long as possible. They are good when you make long term investments in a systematic way. But your income and life changes require dynamic asset allocation based on prevailing market conditions and hence won't you be better off dealing with independent financial planners who have more at stake with your long term total portfolio returns than brokerage?

Institutional Language: When the year began (Apr'13), one of the top 3 fund management company sent newsletter with an ad in the first page where a daughter was proudly talking about her dad how he planned for her college fees by investing in debt funds. We all know how the year turned to be a disaster for most of the debt funds; I don't know whether the daughter still feels proud about her dad. The next page in the newsletter begins with the equity outlook like this: Economic indicators of USA were positive, Euro area continued to be in recession, Fitch has cut Italy's sovereign rating to BBB, how Cyprus deal is worked out, hostility between South Korea and North, the lack of clarity on the reforms in China after the NPC (National's People Congress) session, how DMK's exit from UPA and RBI's hawkish tone is keeping investors risk averse. Believe me there was not a single mention about pending election.

Out of 1475 words in the outlook, 55 words were about earnings. So much so for the belief that equity mutual funds are for long term and in long term, equities track earnings. I reproduced on cover of the book compiling essays of Warren Buffet: "The basic ideas of investing are to look at stocks as business, use the market's fluctuations to your advantage and seek a margin of safety in your purchase price. There seems to be a perverse human characteristic that like to make easy things difficult".

Macro opinions & Surveys: Nowadays talking about consensus estimates of earnings, interest rates, fund manager surveys etc. have become fashion statements. Find below some of the queries in a survey conducted around beginning of the year and how majority was wrong:

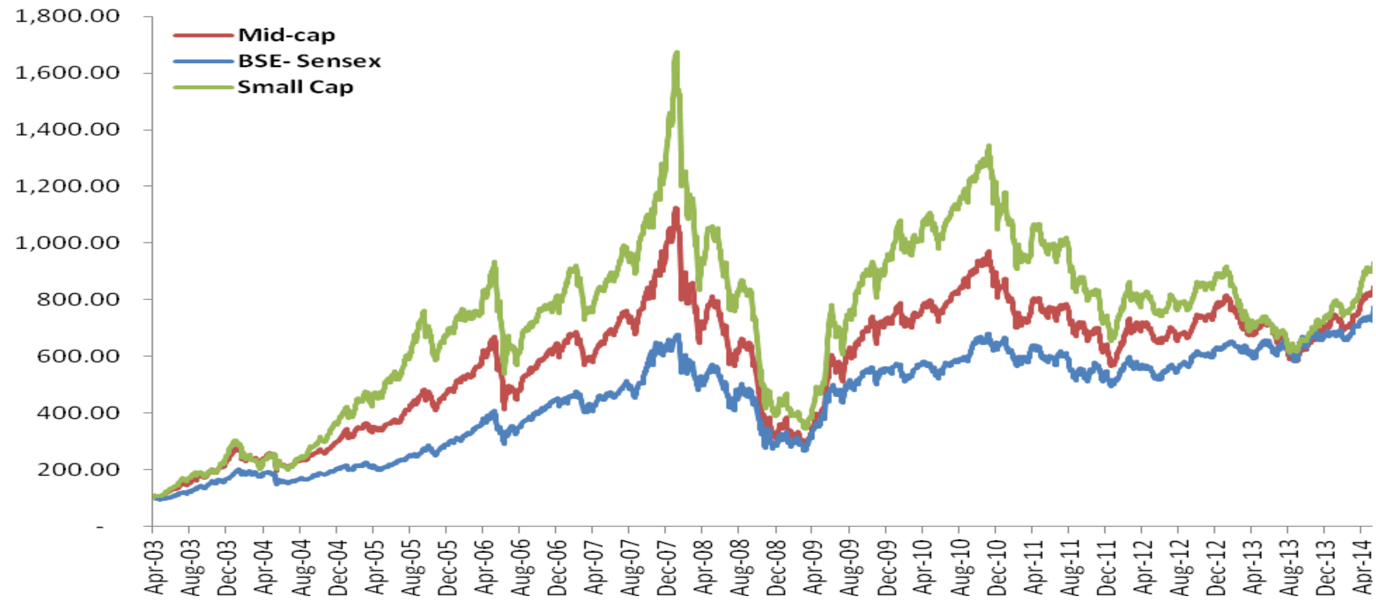
Query	Majority View	Majority Margin (%)	Actual	Correct (%)
GDP growth for FY14	Between 5% and 6%	48%	Below 5%	9.80%
WPI Inflation for FY14	Between 6% and 7%	41%	Below 6%	23.80%
10 Year G Sec Yield	Between 7% and 8%	55%	Above 8%	17.10%
Crude Brent Price	$90 to $100	36%	Above $110	13.10%
Gold Price	$1400 to $1600	42.70%	Below $1400	6.40%
INR/USD	Between 52 to 54	37%	Above 60	14%

To give credit to the survey, their views on equity specific queries were not as off the mark as in macro economics. For those who are curious about knowing geographical presence of the majority of participants: About 60% were from Mumbai. Professional backgrounds of the participants are: 30% are fund management firms, about 20% brokerage and rest are others. It was interesting to note that for a query like " What growth in your Income/Profits do you forecast for FY14, the majority (about 84%) were wrong in expecting a growth of 0% to 20% when actually the industry profitability shrank (only 1.8% were correct). Those who could not estimate their own Income for a year were busy bringing estimates on every business under the sun for many years.

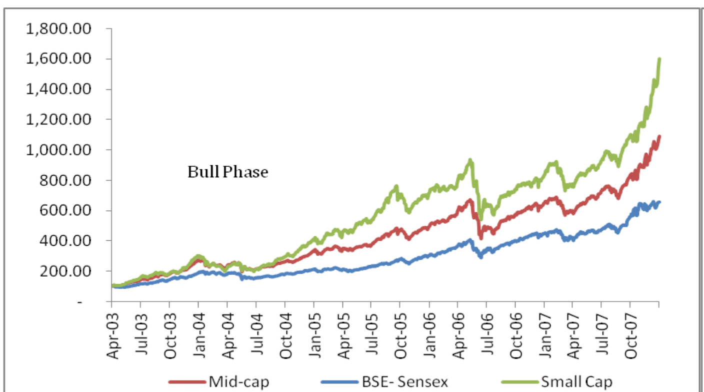
Next time when you happen to read any expert review or consensus estimate of macro economy variables, price pattern of commodities, interest rates etc, take them for amusement value but never let them direct your investment decisions. How true what Warren Buffet said: "Forming macro opinions or listening to the macro or market predictions are a waste of time. Indeed, it is dangerous because it may blur your vision of the facts that are truly important".

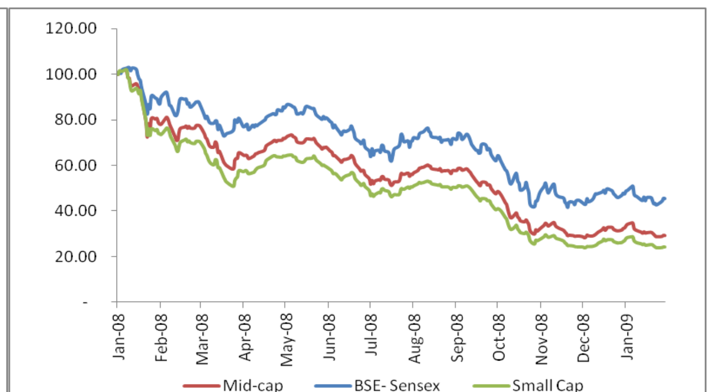
Contrarians: There are only two classes of shareholders who as a whole class have been consistently successful, coincidentally they are contrarians. One is an investor who systematically invests at regular intervals, even when majority is selling equities. The other is "Promoters/Insiders". In the midst of all the uncertainty surrounding our economy over the last 3 years, there has been consistent buying by promoters. In fact last year, one in three companies in BSE 500 have seen promoter stake increase. The promoter holding in corporate India in September 2013 was at 12 years high, as much as 2002 which was the year big bull market began. The contrarian's numbers validate the value investors' belief that we are in a cusp of a major bull market and it is time to disregard the short term noises that emanate from the consensus views and earnings estimates. We will look forward to an exit opportunity when consensus view turn optimistic and then euphoric and promoter dilute through record number of IPOs/FCCBs/Institutional Placements. Till then sit tight with what you have in equities and look forward to add as well.

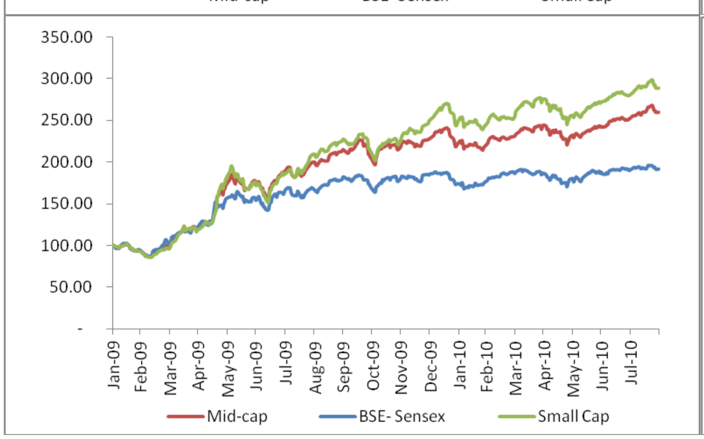
Sensex @ 22K but broad markets?

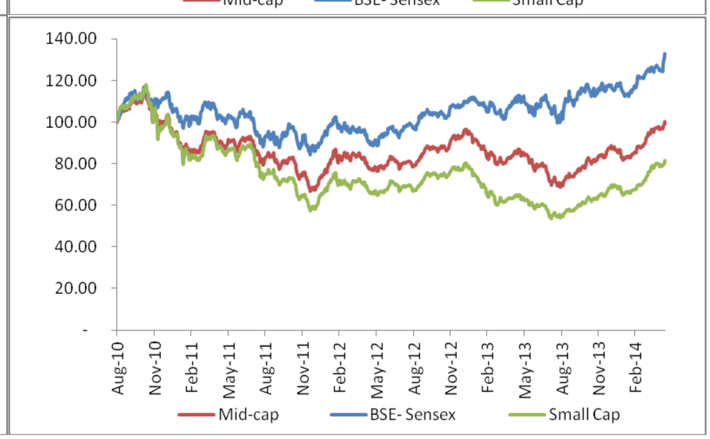


The relative performance of small caps and midcaps vis-à-vis the Sensex (largecaps) can be observed from the following graphs:



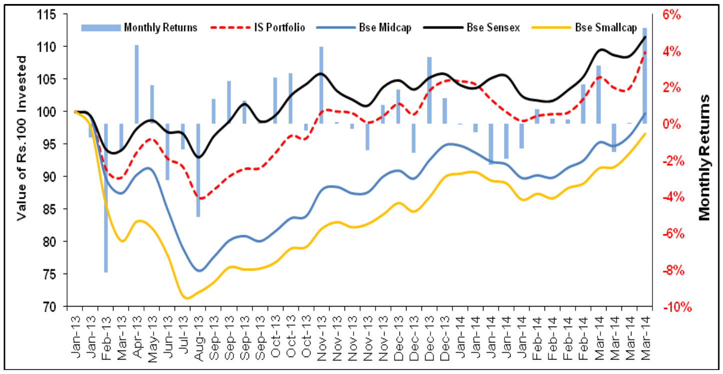


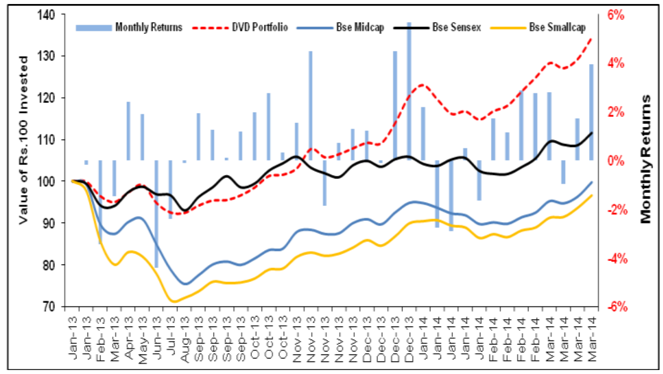


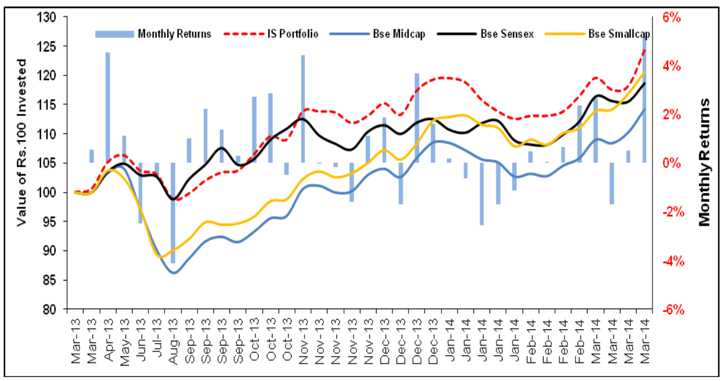


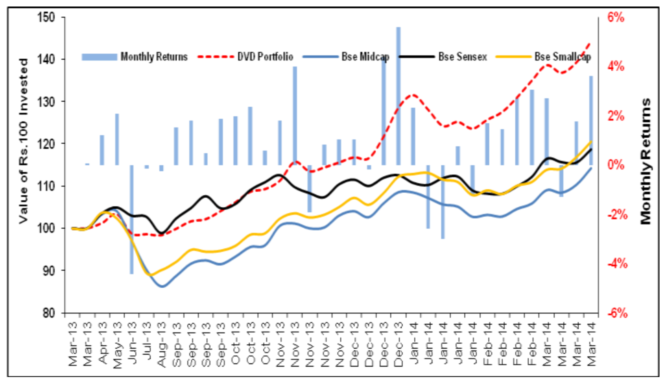
Even though we are agnostic to size while investing, it is safer to assume ISF will have more stocks of Mid caps and DVD will have more of Mid & Small caps.

Our Portfolio Review:









Returns From 23-Jan-13 to 31-Mar-14		
	Absolute Returns	CAGR
Insider Shadow	9.10%	7.69%
DVD	34.40%	28.60%
Sensex	11.55%	9.75%
Midcap	-0.21%	-0.18%
Smallcap	-3.42%	-2.92%

Returns from 1-Apr-13 to 31-Mar-14		
	Absolute Returns	CAGR
Insider Shadow	24.27%	24.27%
DVD	44.15%	44.15%
Sensex	18.60%	18.60%
Midcap	14.14%	14.14%
Smallcap	20.58%	20.58%

Instead of performance numbers, it would be useful to discuss the bottom table. Portfolio discussion can be qualitatively better if we focus our attention on growth and the value we get for the price we pay.

Parameters	Sensex	ISF	DVD
Number of Stocks	30	20	10
Market Cap (In Cr)	125,000	6,500	3,200
Forward PE Ratio	16.5	12	10
Debt /Equity Ratio	0.6:1	0.3	0.3
Dividend Yield	1.1%	1.6%	1.8%
Price /Book Value	2.7	1.9	1.7
Earnings growth	9%	15%	20%
Return on Equity	17%	16%	18%

Annual Review: Our portfolio companies have done reasonably better last year and for many companies annual results will get announced only in June'14. As usual, we will organise a "portfolio companies results review" session around middle of August for all our clients. Our last annual session in Aug'13 as well as mid-year review in Feb'14 attracted interesting array of questions from the clients who participated. Most of the fund managers/analysts of Unifi were there taking each question from every investor client. On few stocks that belonged to businesses our clients understand, the quality and depth of the conversation was fantastic. Most clients's commented "How pleasant it is to discuss a stock idea or a strategy without PPTs and booklets of reports".

New Themes In Waiting: A strong market performance, new peak in Nifty, fantastic portfolio performance, many happy investors are common causes why fund launches peak out near peak market valuations. While we are conscious of it, we believe the peak is far away and hence are keen to raise further investor equity now. There are few niche investment strategies that would benefit from market rally driven by the return of investor crowd gradually, after the initial round of index movement. While most of them are in "Work in Progress" stage, we are ready to launch a new style called "**HoldCo**" that would focus on Holding Companies. "Insider Shadow Fund" that tracks only those companies where promoters have bought will have another variant soon likely to be named as "**ISF Mini**" that would focus only in relatively smaller companies. We believe there is a window of opportunity today that didn't exist before by a confluence of many factors to benefit these strategies and that explains why now.

Review Meeting: As usual I would like to conclude with Sir John Templeton's quote: "Bull markets are born in Pessimism, Grows in Skepticism, Matures in Optimism and Die on Euphoria". I believe we crossed over Pessimism early last year and current market growth is still viewed with skepticism. It helps us to commit to equity a significant part of our portfolio before optimism shows up in price soon. I would ensure we exit when euphoria brings crowd back.

Our investment idea flow has grown and valuations remain attractive in spite of the recent run-up. While equity allocation level within your portfolio is a function of "your risk tolerance", I would urge you to consider additional capital into niche themes like ISF & DVD within your overall equity allocation. It would be my delight if you could refer your friends or family who might be interested in meeting us.

Yours Sincerely

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