UNIFI Capital

THE GREEN FUND

QUARTERLY REVIEW - JUNE 2021

UNIFI AIF 2 – The Green Fund

The Green fund targets capital appreciation by investing in the next generation of winners arising from India's evolution towards a more *sustainable economy.* The investment universe comprises of well managed businesses offering best in class solutions to address challenges in the areas of Energy, Emissions, Waste and Water.

Asymmetric

Most people think in stories instead of numbers. They construct a narrative of how they expect things to play out, with perhaps not the best definition of what constitutes risk, as it is something that may derail that narrative. But risk means different things to different people, and by that extension to different firms, and the idea that there is an equilibrium in what constitutes risk is a mistake. In our line of practice of seeking favourable investment outcomes, it is important to appreciate why risk is a factor in constant disequilibrium. So, while the relationship between the raging pandemic and financial markets seem intuitively risky and symmetric, is it so? The numbers are unequivocal in suggesting otherwise in the last financial year.

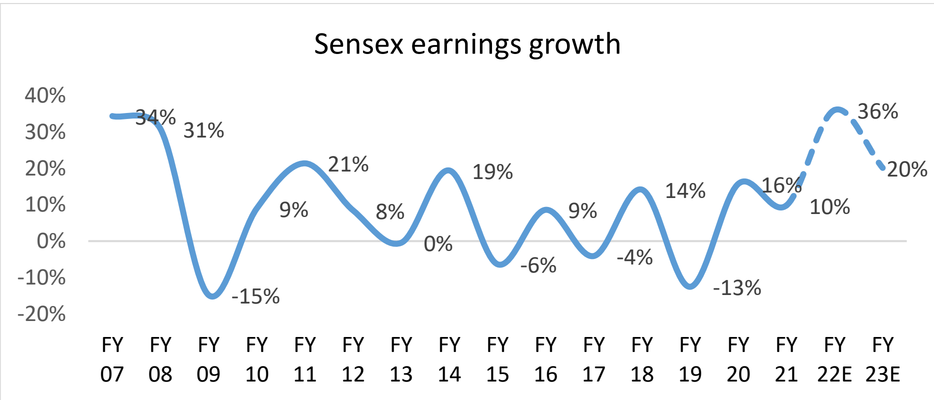
The outperformance of our portfolio companies and those outside our coverage is testament to how quickly markets have reimagined the business models of the leaders over the followers. What broke one end of the long tail in most industries, has led to the consolidation of leaders in the same industry. And fundamental performance of this nature represents one of the most intriguing facets of financial markets where the upside skew can be extraordinary.

The old maxim that financial markets are a barometer of the economy long stands modified. Markets have signified a regime change in the new world, representing industry leaders who are consolidating their dominance, and a new monetary policy framework of low interest rates around the World that is repricing equities. So, while there is pain among smaller businesses [organized or otherwise], the leaders have benefited by virtue of their ability to withstand this phase of disruption. Remember, it is an asymmetric world.

At Unifi, we are in a constant state of regression, acutely aware of the changing marketplace, rethinking business models, financial models, the right forecasting horizon, and valuations across the horizons. While individuals are worried about how bad this phase of the pandemic is, the Street is focused on how good things will be for the leaders after the storm passes. And as is the case with most of our companies, and leaders outside our universe, we find that the immediate economic loss is negligible relative to their intrinsic value given the opportunities that lie ahead.

It is Organic

Corporate India is amid its finest earnings growth cycle witnessed in the last 12 years.



FUND DETAILS

Launch Date:
31 July 2017

Scheme AUM:
INR 1.65 bn

Theme AUM[1]:
INR 3.05 bn

Firm AUM:
INR 90 bn

No. of Investors:
71

Investment Manager:
Unifi Capital Pvt Ltd.

Tenure:
5 Years or 200% absolute return whichever is earlier

Custodian
BNP Paribas

Reporting:
Quarterly Review

Hurdle Rate:
12% Per annum compounded

Fees:
1% per annum of AUM payable monthly and 20% of profits earned above the hurdle rate. The management fee would be offset from our share of Profits.

[1]AUM under Green Fund in PMS as well as AIF.

The last time corporate India enjoyed this fundamental strength was more than a decade back, fuelled with the multiplier effect of capex across the entire spectrum of Indian infrastructure. Today, the confluence of growth drivers are more organic, and sustainable. (A) Strong rural sentiment driven by healthy increase in support prices and two consecutive seasons of bountiful produce have lent strength to all areas of consumption; (B) India is advancing as an alternative sourcing destination to China across a broad spectrum of manufacturing industries [furniture to complex chemicals]. In the process this is also abetting India's decadal effort at import substitution. The multiplier effect of this development across the ecosystem is very healthy and likely to abet enterprise investments in the times to come. Importantly, the Government's willingness to do what it takes to support domestic industry though generous incentivization of new capacities across sectors is commendable and is setting on course a part of the investment cycle. This confluence has resulted in an abundance of consumer and enterprise sentiment, and the confidence to kick start a new cycle of expansion.

A significant difference from the previous cycle is that corporate balance sheets today are in significantly better shape, and have greater cognizance to capital allocation and governance, and to that extent making the cycle more sustainable.

Tail Risk

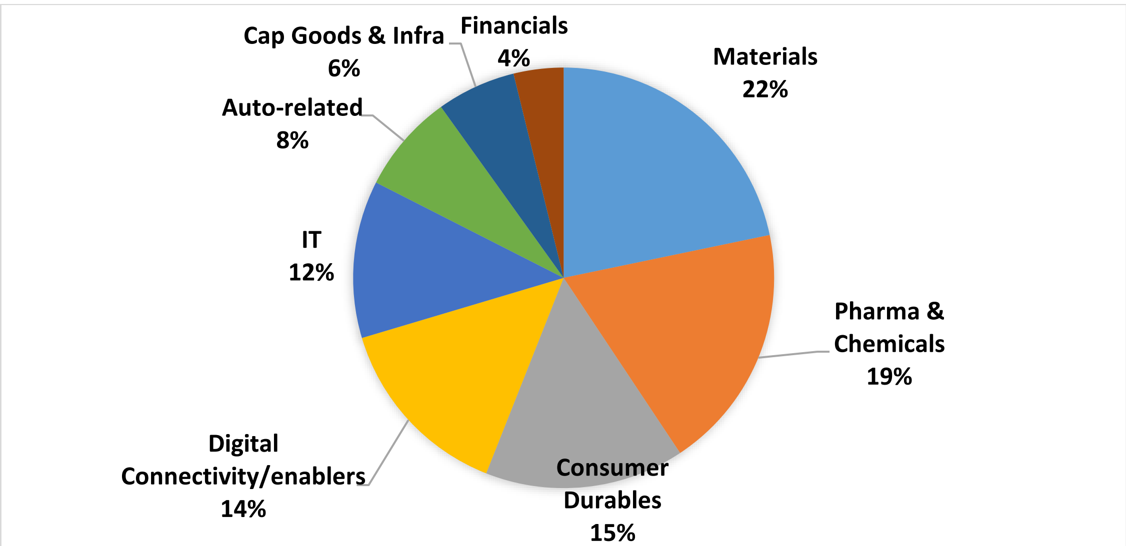
Data suggests that there is a less than 0.04% chance that a carrier passing through the Suez Canal will face any issues. Entrusted with handling a significant portion of the World's International trade, the controls at Suez have a highly structured approach to underlying risk management. This came to naught earlier this year, as one of the World's largest ships, MV Ever Given, collapsed under its own weight*. Apparently, the Suez is not designed to host a vessel as large as the MV Ever Given under non-routine circumstances. And neither the Ship, nor the Suez, is designed to manage risks from non-routine events. And it is the non-routine events that define the course of nature and markets; from a virus escaping a lab to the sheer unpredictability of modern monetary policy theory and everything in between.

As professional investors, every investment decision is fraught with non-routine risks. As we construct your portfolios for times to come, this is a good time for us to re-iterate that we are acutely conscious of the probabilities of such non-routine risks affecting our investment outcomes. As a result, [a] the market caps we are present in today, [b] sectors we have exposure to and [c] our management of absolute exposure is a function of our constant assessment of routine and probability of non-routine risks. These are unlikely to be apparent in a simple evaluation of your portfolios, and a conversation with your relationship manager may enable deeper appreciation of this facet.

As you may have noticed from your portfolios, the stocks that have performed in the 2020 cycle have largely made way for newer investments that are likely to benefit from the new normal and keeping in mind newer kinds of risks. At Unifi, we are aligned with each of the above trends, but at the same time stay true to our core principles of seeking the right mix of risk and reward in each of our investments.

**[For the curious, Fat ships are prone to something known as the bank effect, where in shallow waters, the bow and stern of the boat drift in opposite ways. What followed was an unmitigated supply chain disaster, briefly plunging the World into a moment of vulnerability].*

Sector Exposure



Summary of results from the quarter Q4-FY 2021

I Materials: The Green fund has an exposure of 22% to this segment with various investments detailed below.

HIL delivered Revenue, EBIDTA and PAT growth of 31% / 98% and 175% YoY growth with continued recovery in all the business segments. Roofing, Parador and Polymer segments have delivered YoY revenue growth of 50%, 12% and 94% respectively. A buoyant rural economy has led to strong demand for the roofing business along with significant market share gains, while the flooring business in Europe continues to deliver ahead of the market. Each of HIL's segments continue to face the prospect of significant growth in the times ahead led by strength in core demand, and consolidation within the industry. Cost optimization, better pricing environment and de-leveraging, have led to margin expansion of 450bps YoY.

Key risks may emanate from poor rural sentiment for the year ahead, higher competitive intensity, and inability to procure raw materials at favourable prices.

JK Paper reported revenue growth of 22% YoY to Rs. 898cr. EBIDTA and PBT increased by 29% YoY and 41% YoY to Rs. 228cr and Rs. 194cr, respectively. The key highlight of Q4FY21 performance was strong turnaround of their subsidiary - Sirpur Paper Mills which broke even at the EBITDA level.

JK Paper is play on revival on domestic paper consumption driven by reopening of offices and educational institutions. Further the company is increasing its capacity from 4.36 lakh tonne to 7.42 lakh tonne driven by green field packaging board expansion in Gujarat with capacity of 1.7 lakh tonne and addition of 1.36 lakh tonne from inorganic acquisition of Sirpur paper mills. The medium-term earnings growth would be driven by volume increase, cost optimisation and better realisation.

Key risks would be delay in capacity addition, decline in realisation and extended impact of COVID-19.

Mahindra EPC reported revenue decline of 13% YoY to Rs. 72cr. Driven by lower gross margin, the EBITDA/PAT decline was steeper at 59%/58% YoY to Rs. 6cr and Rs.4cr, respectively. Overall micro irrigation industry declined by 20% in FY21 vs 10% decline in revenue reported by MEPC. A major reason for this decline was zero business activity in the state of Andhra Pradesh which makes 20% of overall industry and this should come back in FY22.

The company is now actively pursuing selling of non-ISI products in retail market. Selling of these does not require subsidy from government and hence would reduce overall working capital. This initiative began in FY21 and contributed 7-8% of sales in the first year. Going forward, it is expected to contribute significantly. The collapse of market leader in the micro irrigation industry, favourable government support towards irrigation and low penetration levels in India, makes the company well poised to capture incremental demand in the sector.

Key risks would arise from delay in subsidy release from the government, higher raw material prices and extended impact of COVID-19.

II Pharma & Chemicals: The Green fund has an exposure of 19% to this segment with major investments detailed below.

JB Chemicals reported revenue growth of 19% YoY to Rs.528cr. EBITDA and Operating PBT registered growth of 35% YoY and 44% YoY to Rs.124cr and Rs.107cr, respectively. Domestic business delivered growth of 9% YoY driven by key chronic segments - cardiovascular/anti-hypertensive. MR Productivity had improved from Rs. 3.6 Lakh in FY20 to Rs. 4.4 Lakh in FY21. Exports grew by 31% YoY. Exports Growth was driven by US and South Africa formulations business. Growth in Russia continues to remain muted due to covid as anti-infectives accounts for the major part of Russia business. The company registered 23.4% EBITDA margin as against 20.7% last year on the account of operating leverage and cost optimization initiatives by the new management.

We like the company due to the strength of its 4 key brands (Cilacar | Nicardia | Rantac | Metrogyl) and the potential for KKR to accelerate its growth momentum.

Key risks: Supply chain disruptions, Pricing pressure in Domestic Business and unexpected regulatory developments.

Suven Pharma reported good in-line results w.r.t Q4FY21. Sales and EBIDTA were up 38% and 19% on a YoY basis. Standalone PAT grew by 27% YoY. The impressive revenue growth was broad-based with CDMO pharma and CDMO specialty chemicals growing 51% and 37% YoY respectively. US Formulation business is gaining traction gradually. Margins were impacted because of steep rise in the cost of key starting materials [KSMs] due to supply disruption. The company has the option to go back to innovators and pass on the cost. Suven's strategy has been to look at long term relationships and not mechanically pass on any short-term cost increases. If the prices continue to go up, they will certainly use their option to pass-on. The nature of Suven's research services segment and campaign based commercial supplies necessitates tracking its annual progress rather than quarter-wise. From that standpoint, the FY21 numbers indicate a growth of 20% and 15% YoY in terms of revenues and profits which is as per our expectations.

Suven currently has seven commercially launched intermediates and specialty chemicals and is looking to add one more in FY-2022. In addition, the company 3 phase-3 candidates where at least one could see a commercial launch in the next 12-18 months. Suven has also diversified into formulations by building appropriate capacities and obtained USFDA approvals. Company has launched 4 ANDAs (formulation drugs) in FY21. It also targets to launch 3-4 ANDAs every year over the next 5 years. The company has filed 11 ANDAs till the end of FY21 and targets to file more 5 in the next financial year. The pace of additions to research projects has seen slowdown due to the second wave. The performance of Suven's associate Rising Pharma (USA) is progressing well and opportunities for commercial contracts could arise in the future from them.

Key risks - Management bandwidth (COO hiring delayed), slow acceptance of products in US formulation business and low traction in research activities due to covid are the key concerns.

DCM Shriram reported Revenue, EBITDA and PBT YoY growth of 14%, 5% and 24% respectively. The revenue growth in this quarter was primarily driven by Plastics (due to higher realisation) and sugar segments. This was a seasonally weak quarter for Agri-segment, and this resulted in the decline of consolidated EBITDA margin by 140 bps YoY. The PBT was higher on account of decreased interest expenses and greater other income leading to 120 bps growth to 14.1%. Overall, FY21 saw 7% revenue growth largely driven by the sugar business, which grew by 34%. But chlor-vinyl segment degrow by 12% due to lesser volumes of caustic and realisations, which are expected to bounce back in coming years. The earnings for FY21 had degrowth of 7% at Rs. 673cr.

DCM Shriram is predominantly present in chlor-alkali and sugar segments along with agriculture products like fertilizers, bio seeds and other farm solutions. The demand for caustic soda is now coming back to pre-covid levels and this is expected to result favourably on numbers in the times to come. Sugar segment consists of sale of sugar, ethanol and power which has hit stable demand through the year with improved realisations. Further, the company has announced entry into chlorine/hydrogen downstream products like Epichlorohydrin, Hydrogen peroxide and Aluminium chloride. These are value added segments within the chlorine value chain and hence will contribute positively towards overall profitability.

Key Risk: Unexpected regulatory developments in Sugar/Ethanol business and decline in caustic soda prices in the international market.

III Consumer Discretionary: The Green fund has an exposure of 15% to this segment with major investments detailed below.

Stovekraft reported revenue growth of 53% YoY to Rs. 235cr. The revenue growth was largely led by pressure cookers and cooktop segments. Company reported EBITDA of Rs. 25cr vs loss of Rs. 2cr in Q4 FY20. Higher operating leverage resulted in sharp EBITDA turnaround. Against a loss of Rs. 11cr, company reported PAT of Rs. 20cr in this quarter. The Covid induced lockdown has resulted in higher in-house food consumption, providing tailwinds for the kitchen appliances sector. Stovekraft has its presence largely through 'Pigeon' brand and as company has in-house manufacturing, it has a cost advantage over its peers. Their exports to retailers like Walmart is growing at healthy rate. We expect company to benefit from the sector tailwinds.

Key risks include entail steep increase in raw material prices, competitive intensity.

Crompton Greaves Consumer delivered revenue, EBIDTA and adjusted PAT growth of 48% / 61% and 66% YoY respectively, and reported sharp improvement on all parameters, led by structural efficiency initiatives, core demand and a good pricing environment. Both the segments, Lighting (up 15% YoY) and Consumer durables (up 61% YoY), delivered ahead of industry growth led by consolidation of the larger players. In each of the key product segments [Fans (59% YoY), Lighting, Pumps, and other Electric Appliances (74%YoY)], the company delivered ahead of industry growth rates, on the back of product innovation, premiumization and market reach initiatives. For the full year, the company delivered revenues of Rs. 4,800cr (6% YoY) and earnings of Rs.540cr (22% YoY). We expect this trend to continue, along with headline growth that is ahead of the industry. Crompton is amongst India's most profitable players in the consumer durables space with best-in-class growth, margins, and capital efficiency. We continue to like the company as we expect it to benefit from this phase of consolidation.

Key risks to the investment could emanate from drop in consumer sentiment, and steep inflation in raw materials.

IV Digital connectivity/enablers: The Green fund has an exposure of 14% to this segment with investments detailed below.

Tata Comm's 4QFY21 revenues were slightly lower in both the Data and Voice segments. Voice segment revenue was down 17.2% QoQ to Rs. 5600cr while Data segment revenue was down 1% QoQ at Rs 3520cr. The latter was impacted on account of on account of slower deal conversion cycles and moderation in UCC (Unified Communications and Collaboration) traffic.

EBIDTA was down 3% QoQ to Rs 1020cr on account of 4.6% decline in the data segment to Rs 980 cr. Voice segment EBIDTA came in at Rs 36cr. Net debt declined by Rs 190cr QoQ to Rs. 7800cr. FY21 revenue at Rs 17,100cr was flat YoY while the EBIDTA increased 30% YoY to Rs. 4,300cr. Full-year FY21 capex was at Rs 1420 cr, down 11% as against Rs 1600cr in FY20

The company has pretty much resolved its legacy Balance Sheet issues and we are confident that the company should deliver on its double-digit growth targets with steady margins as the economy opens given strong demand in most of the segments that the company operates in including high quality internet connectivity, network transformation/connectivity, voice solutions, cloud hosting related offerings, security solutions, IoT etc.

Key risks would be slower to negative growth in the data segment on account of covid related stress and lower usage of Tata Comm's services e.g., data streaming of live sports or reduced international travel or delays in deal conversion.

IEX delivered revenue growth of 35% on the back of strong volume growth across products to Rs.94cr. DAM and TAM volumes were up 20% and 31% YoY respectively. RTM, launched in June-20, formed 17% of volumes in Q4 FY21 growing at more than 30% on a sequential basis. EBITDA and Operating PBT registered a growth of 48% YoY and 54% YoY to Rs.77cr and Rs.64cr respectively on the account of favourable operating leverage.

IEX is India's largest electricity exchange, and we believe it will be at the core of India's Power sector in the times to come. The company introduced many products such as Real-Time, Green Term Ahead Market, Cross Border Contracts and Gas Exchange during the year, which has helped the company gain market share from other short-term market players. In addition, the company plans to launch long duration contracts in the next financial year. With the government's commitment towards power sector reforms to reduce the role of DISCOMs and optimize the cost of energy, IEX is likely to see a multi-year encouraging growth.

Key risk: Unexpected regulatory environment and slowdown in industrial activity

V Information Technology (IT): This segment constitutes about 12% of the fund's total investments with major exposure to the following companies.

Sonata Software delivered revenue growth of 16% YoY driven by products division that grew 25% YoY growth, while the IT services segment recovered 6.8% sequentially. Overall EBIDTA margins improved sequentially by 170 bps to 9.6% with services business reporting 28.4%. As a result, earnings at Rs.83cr was up 34% YoY and 54% QoQ. Overall, in FY21, the company delivered revenue growth of 13% YoY and earnings of Rs.243cr (-12% YoY) due to a truncated Q1-21. The outlook for each of their segments in the times to come are good driven by normalization in the European travel industry, traction in Microsoft's core business, and enterprise investment in new age cloud and IT products.

Sonata is a key partner to Microsoft in their global product development initiatives and has strong domestic products re-selling business. With the worse of the pandemic induced stress in their travel business behind them, we expect the traction in earnings to return sequentially over the next few quarters. There is a trend of better off-shoring that is being witnessed on the back of industry wide work-from-home initiatives, and this is likely to be margin accretive in the times to come.

Risks: Slower than expected economic recovery in Europe and cuts in discretionary IT spends by enterprise clients.

VI Auto-related: The Green fund has an exposure of 8% to this segment with various investments detailed below.

Mayur delivered 36% YoY revenue growth, on the back of strong volume growth in the auto segment. Gross margins improved by 70 bps YoY to 48.4% on account of price hikes and a better product mix. EBITDA was up 60% YoY to Rs.52cr, aided by margin expansion and operating leverage. Overall, PAT was up 38% YoY to Rs.34cr. The company started servicing orders of Mercedes through exports and saw some traction for their production at the new PU plant. Mayur also added new clients like Volkswagen and BMW and is looking to tie-up with a Korean company to increase global footprint. This augurs well for revenue growth through exports, which is a higher margin business. The volume recovery in the footwear segment, ramp up of PU plant and business from new clients provides good visibility for earnings growth going forward.

Key risks would be sharp increase in PVC prices, delay in ramp up of the PU plant and logistic issues for exports.

Honda Power India reported revenue growth of 51% YoY to Rs.296cr, however gross margin declined from 37% in Q4 FY20 to 32.6% in Q4 FY21 due to higher raw material prices. EBITDA margin at 7% was higher YoY due to truncated sales in Q4 FY20. PAT increased by 200% YoY to Rs. 15cr. Overall, company posted 11% revenue growth in FY21 and is expected to maintain similar growth path in FY22 with better margin takeaway leading to recovery in PAT. We expect growth to come from improved exports as Honda Power benefits from India as a manufacturing base to supply various other Honda operations globally and margin contribution is greater in exports.

Key risks would arise from delay in subsidy release from the government and extended impact of COVID-19.

VII Cap Goods & Infra: The Green fund has an exposure of 6% to this segment with investment of Triveni Turbine.

**Triveni Turbine is yet to declareQ4 FY21 results.*

VIII Finance: The Green fund has an exposure of 4% to this segment through Karur Vysa bank (KVB) detailed below.

KVB reported AUM growth of 9% YoY & 1% QoQ at Rs.52,820cr. However, NII growth was lower at 4% YoY to Rs.612cr due to interest reversals. The operating costs were stable on a QoQ basis at Rs.579cr and operating profit was flat QoQ at Rs.249cr. The covid related slippages and restructuring were lower than guided at 1.8% & 1.9% respectively, on the back of strong collection efficiency. Bulk of restructured accounts were in the retail segment comprising of homeloan / LAP, where the loans are secured, and the bank carries 8% coverage on the same. Overall, asset quality improved with GNPA & NNPA at 7.8% and 3.3% respectively.

KVB is a play on the upcoming recovery in the credit cycle within the economy. The bank's deposit franchise is strong with total deposits of Rs.63,278cr and CASA of 34%, which have been improving every year. KVB has an AUM of Rs 52,820cr spread across corporate segment (23%), Commercial segment (32%), Retail (23%) and Agriculture (22%). Gold loans forms 24% of the entire book and is spread between Retail and Agri loans. With much of the provisioning done for the past stress and credit cycle being at the cusp of a strong recovery, the bank would be able to get back to its earlier return ratios, thanks to its long-standing market position and 780 strong branch networks.

Key risks would include deterioration of asset quality, higher than expected credit cost and decline in NIMs due to falling yields.

Investment Exits: The fund exited its investment in KEC International, Tech Mahindra, Wipro, Symphony and Halydn Glass. Most of the exits were carried out for better incremental risk reward opportunities. Few exits were considered in lieu of performance not being up to the expected levels or due to unfavourable macro conditions for growth in coming quarters.

Financial Details of Portfolio Companies

Green	Exposure *(18th June 2021)*	Market Cap *(Rs.cr)* *(18th June 2021)*	PBT *(Rs.cr)*		YoY *(%)*	PAT *(Rs.cr)*		P / E	RoE *(%)*
			Q4 FY20	Q4 FY21		FY 20	FY 21	FY 21	FY 21
Sonata Software	12.4%	7,418	82	109	33%	277	244	30	31%
HIL Ltd	12.1%	3,384	28	81	100%	106	260	13	25%
JB Chemicals	9.4%	11,805	50	101	102%	272	448	26	25%
Suven Pharma	8.1%	12,308	89	105	18%	317	362	34	31%
Stovekraft	7.8%	1,801	3	19	100%	34	112	16	27%
Tata Communications	7.3%	36,368	-282	386	0%	-87	1254	29	-
CG Consumer	7.2%	26,516	137	231	69%	440	541	49	32%
IEX	7.0%	11,131	58	80	38%	176	205	54	47%
Triveni Turbine*	5.8%	3,737							
JK Paper	5.7%	2,905	137	194	42%	475	240	12	10%
Mayur	5.1%	2,166	33	47	42%	80	90	24	16%
KVB	3.8%	4,101	72	178	147%	235	359	11	5%
Mah EPC	3.1%	437	13	6	-54%	23	19	23	13%
Honda Power	2.7%	1,195	6	20	233%	67	49	24	8%
Eclerx Services	2.5%	5,810	55	99	80%	209	283	21	20%
DCM Shriram	1.6%	11,282	201	232	15%	717	673	17	8%

Portfolio Characteristics

Valuation Parameters (As of June 18th, 2021)	FY21	FY22e
P/E Ratio	26.3x	21.4x
P/B Ratio	6.4x	5.2x
Earnings Growth (%)	25%	26%
Debt Equity Ratio	0.08	0.06
ROE (%)	21%	21%
Wt. Avg Mcap (cr)	Rs.9,426 cr	

Triveni Turbine is yet to declare Q4 FY21 results

Annexure:

Information on Fund Risk Management

i) *<u>Price Risk:</u> Stock markets are volatile and may decline significantly in response to adverse issuer, political, regulatory, market or economic developments. Different parts of the market and different types of equity securities may react differently to these developments. For example, small cap stocks may react differently than large cap stocks. Issuer, political or economic developments may affect a single issuer, issuers within an industry, sector or geographic region, or the market as a whole. Unifi AIF 2 – The Green Fund adopts a bottom-up approach towards investing. Also, various macro events and its implications are considered to reduce the overall negative impact on portfolio.*

ii) *<u>Loss of Capital:</u> All investments in securities present a risk of loss of capital which is an outcome of various events like macro events or something internal to the company. The Fund would seek to moderate this risk of loss of capital through a careful selection of investments.*

iii) *<u>Liquidity Risk:</u> This represents the possibility of not honouring redemptions upon closure of fund due to illiquidity of the portfolio. Also, it is possible that the realised price from selling the security might be lesser than the valuation price as a result of illiquid market. The Fund would ensure that at a significant portion of its investments can be liquidated at prevailing market prices.*

iv) *<u>Risk of Key Personnel:</u> This represents loss of one or more key personnel of the Fund Management team who are responsible for managing the Fund's portfolio. The process of investment and fund management is institutionalised and hence procedure driven. This reduces the risk of loss of key personnel.*

v) *<u>Concentration Risk:</u> This represents risk of concentration of investments in few opportunities. This risk is minimalised as individual position weightage isn't allowed to go beyond 10% of the Investible Funds.*

vi) *<u>Leverage Risk:</u> This represents risk of leverage risk at the investee company level. This risk is minimalized through prudent selection of investments.*