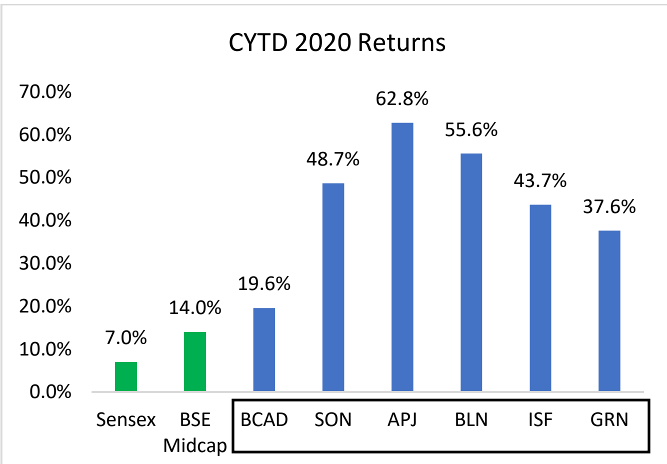
The year so far

In March this year when markets (and cities) emptied out, we made the decision to go against the then prevailing conventional line of thought, and aggressively added to our positions in select equities. We grounded that decision in a rigorous analysis of the *variety of perceptions*, and combined that with our core principle of seeking the most favorable balance of risk and reward in an investment. In the process, we have delivered one of our best years ever as fund managers.



TWRR returns, CYTD, as on 30th November, 2020

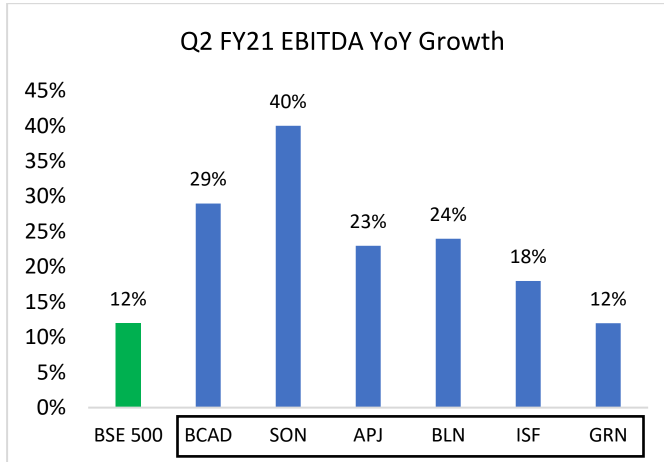
Unifi's Investment Strategies
BCAD- BCAD Fund; SON – Spin Off Fund; APJ- APJ Fund; BLN- Blend Fund; ISF- Insider Shadow Fund; GRN- Green Fund

[For those inclined, in the field of decision theory, there is such a thing as the Ellsberg Paradox. It suggests that most people hesitate to act in a circumstance where the odds of a situation have a guaranteed positive outcome, with the magnitude being unknown. They prefer taking risks in situations where the odds of the situation are known, but have lower outcomes. Investing in times of stress is a very similar proposition].

Never waste a good crisis

Corporate results from Q2-2021 have dispelled lingering concerns, if any, on the economic linkage between the core of the Indian economy and larger listed firms. As GDP for Q2-FY2021 *shrank by -7.5%*, the trend of consolidation sharply accentuated across sector leaders, and our portfolio companies. In a sense, survival instincts seem to have come to the fore as *sector leaders* seized the opportunity to consolidate market share [from weaker peers], and strengthened several aspects of their operating metrics, and in the process delivered significant corporate and shareholder value. Under normal circumstances, such endeavors and the resultant outcomes may have been difficult to practice, and execute.

While the universe of BSE-500 delivered EBIDTA growth of 12% [in the backdrop of a -7.5% decline in GDP], the core holdings of our portfolios delivered significantly ahead of their peers, as they capitalized on the crisis, and strengthened their proposition, as well as their operations.



BSE-500 ex BFSI, OMCs

Make no mistake, this does not mean the recovery is all pervasive. Frontline indices only cover the formal industry, with an overwhelming weight on those who are significant market leaders, while India's industries are overwhelmingly unorganized. What we are witnessing today is a strong phase of consolidation from the informal to the formal sector. While we anticipated this cycle of consolidation post the implementation of demonetization and GST, it has taken a social pandemic to enable this shift. While a significant part of this performance is attributable to the normalization of supply-chains, a deeper examination suggests signs of a new structural normal among the sector leaders, which will see them deliver materially ahead of the pre-Covid era.

Beneath the surface

As a parallel to this phase of consolidation among the leaders, there is a sharp improvement in the macro-environment underway.

- GST collections crossed the Rs.1 lakh crore mark in October & November, and is now marginally higher YoY, indicating a return activity across the breadth of the economy
- India's power consumption [YoY] registered growth of 4%, 12% & 5% during September, October & November respectively, indicating a firm bounce back in the industrial activity while energy consumption [petrol & diesel] has registered growth of 5% & 7% for the month of October, indicating normalization of industrial activity, in spite of the continued momentum on WFH in select industries
- Total number of E-way bills generated in October at 64.1 mn., is the highest tally recorded since the system was introduced

more than two years ago, indicating strong mercantile traction across the economy

- Manufacturing PMI rose to 58.9 on Oct-19 [the highest since 2008] implying strong expansion in manufacturing activity ahead

India's recovery is on a self-sustaining path

As the macroeconomic data indicate, India's industrial risk appetite has not only remained healthy, but has come back strongly. The point to note here is, while liquidity has significantly entered certain asset classes, and the markets, it is yet to fully permeate all parts of the economy [read brick and mortar, physical retail, leisure travel, F&B, and others that have a significant multiplier effect on the economy]. In the post-vaccine world [c.2-3 quarters from today], we expect these untouched parts of the economy to significantly increase their economic participation, and in the process, significantly strengthen the pace of economic recovery. As the markets discounted these developments, India recorded its highest ever monthly inflows of USD7bn [November-20], and in the process delivered a broad-based rally across the breadth of the markets. Given the stated objective of all global central banks to keep the *system* flush with liquidity, the intensity of flows is expected to sustain over the medium term.

Given the resilient private sector where the leaders have emerged stronger, and a flourishing rural economy that will abet domestic consumption, we believe India Inc is set to deliver a positive earnings surprise for FY2021 and the forthcoming fiscal FY-2022.

We have navigated this period of an uncertain environment with success, by staying true to our core principles of seeking the right mix of risk and reward in each of our bottom-up investments. Our approach for the times ahead remains similar, and steadfast. Thank you for your trust in Unifi, and we look forward to touching base with you in the new year. Stay safe, and our best wishes for a healthy and prosperous 2021!

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 FY21. 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 seven 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 Dec 04, 2020	FY 21E
Wt. Avg PE^	21.6x
Wt. Avg PB	5.1x
Wt. Avg ROE	24.4%
Wt. Avg Mcap	Rs.52,628cr

^ex- BFSI

BC AD

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 Dec 04, 2020	FY 21E
Wt. Avg PE^	33.2x
Wt. Avg PB	10.7x
Wt. Avg ROE	29%
Wt. Avg Mcap	Rs.41,930cr

^ex- BFSI

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 Dec 04, 2020	FY 21E
Wt. Avg PE^	14.1x
Wt. Avg PB	4.4x
Wt. Avg ROE	22%
Wt. Avg Mcap	Rs. 32,150cr

^ex - BFSI

Spin Off

The spin off fund seeks to generate superior risk adjusted returns relative to market indices by investing in stocks of companies that are undergoing a corporate demerger. Typically, in a transaction such as this, the sum of the parts of valuation of the different companies that are undergoing a separation is higher than the market cap of the de-merged entity. The fund's proposition is to gain from the fundamental asymmetry linked value-price mismatch, by closely tracking the entire Spin-Off process and investing in such companies, subject to a comfort from bottom up fundamentals.

As on Dec 04, 2020	FY 21E
Wt. Avg PE^	17.4x
Wt. Avg PB	5.4x
Wt. Avg ROE	20%
Wt. Avg Mcap	Rs. 13,713cr

^ex- BFSI

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 Dec 04, 2020	FY 21E
Wt. Avg PE^	17.8x
Wt. Avg PB	2.8x
Wt. Avg ROE	17%
Wt. Avg Mcap	Rs.19,123cr

^ex – BFSI

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 Dec 04, 2020	FY 21E
Wt. Avg PE	15.7x
Wt. Avg PB	3.2x
Wt. Avg ROE	17%
Wt. Avg Mcap	Rs.6,879cr

^ex – BFSI

Risk

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. How long it takes for sentiment to return in consumption remains to be seen. 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 long period of time thereby impacting their profitability.
Geo-political risks	The Galwan incident at the Sino-Indian border has increased tensions on both side of the LAC. Even though talks are continuing though the diplomatic channels, both the countries have mobilized troops close to the border. Any flare up can escalate into a full-scale military action between two of the biggest armies of the world, and disrupt supply chain in the region.
Raw material inflation	Indian 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 (Corona Virus, and 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 spanning Brexit, US-China trade war, OPEC related developments, and other geo-political issues. 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.
Governance risk	We avoid investing in companies with a known history of corporate governance issues. Further, in case 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 single 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

Baidik Sarkar
Head - Research

CHENNAI:
11, Kakani Towers
15 Khader Nawaz Khan Road
Nungambakkam High Road
Chennai - 600 006. INDIA
Ph: +91-44-3022 4466, 2833 1556
Fax: +91-44-2833 2732

HYDERABAD:
H No. 6-3-346/1, Road No. 1
Banjara Hills
Scotia Bank Building
Hyderabad – 500 034. INDIA
Ph: +91-40-6675 2622/23

BANGALORE:
1109, 11th Floor
Barton Centre
84, M.G. Road
Bangalore - 560 001. INDIA
Ph: +91-80-255 9418/19

MUMBAI:
Shiv Sagar Estate,
A-Block, 8th Floor,
Dr. Annie Besant Road
Worli, Mumbai - 400 018.
INDIA
Ph: +91-22-2492 7671

DELHI:
No.818, International Trade
Tower, Nehru Place.
Delhi - 110 019.
INDIA
Ph: +91-8800333799