

“The most important quality for an investor is temperament, not intellect. You need a temperament that neither derives great pleasure from being with the crowd or against the crowd”

Warren Buffett

Dear Sir/Madam,

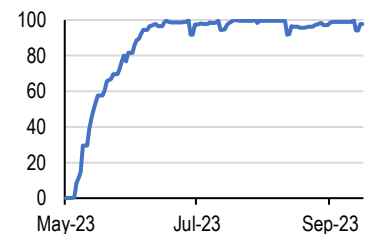
We are pleased to share the second update of the 3P India Equity Fund.

You would recall, 3P India Equity Fund 1 units were allotted on 4th May 2023. Nifty on 4th May 2023 closed at 18,256.

Given the 2-year time correction in markets before May 23, the Fund was invested quickly. By June 23 the Fund was ~100% invested and has remained 97-100% invested since then (fig 1).

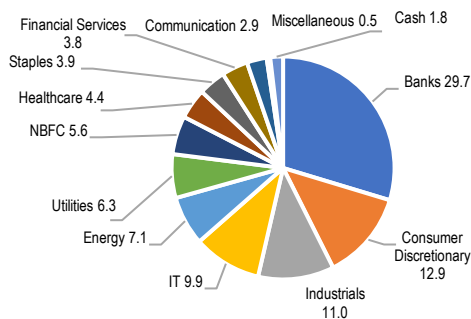
The key portfolio characteristics of the Fund as of September 29th are presented below (fig 2).

% Aum in equities



Note: Equity portion declines on 15/30th due to Inflows | Source: 3PIM
fig 1

Exposure by Sector (%)



Exposure by constituents (%)

Constituents	Weight
Top 5	35
Top 10	54
Top 20	79
Top 30	91
Top 40	97

Total number of Stocks: 48

Note: ETFs are distributed into respective sectors | Total number of stocks includes 2 ETFs

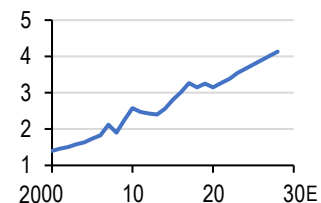
fig 2

Improved Growth Outlook of India

India has grown at an average of 6% CAGR (real GDP) for the last four decades. This was driven by demographics, opening up of the economy, availability of skilled, educated and cost-competitive manpower, abundant natural resources (ex-oil and gas), a stable social and political environment etc.

As highlighted in April - June quarterly, in our judgement, a likely simultaneous increase in the global export share of services and manufacturing should accelerate India's GDP growth from 6% to 7-8% CAGR for the current and next decade. As per IMF's forecast, India should be world's 3rd largest economy by 2027. India's share of global GDP should rise to 4.0% by then (fig 3).

India share of world GDP (%)



Source: IMF

fig 3

The 3P way. Simple but not easy.

1P

Prudence of creating a portfolio of sustainable and reasonably valued businesses.

2P

Patience with businesses and markets. Risk in equities reduces as investment horizon increases.

3P

Performance is the outcome.

Improving Infrastructure: A growth enabler

Our generation has grown up complaining about infrastructure. We think that the next generation is less likely to do so. Over the past decade, India has seen considerable improvement in infrastructure development.

- Major Indian airports are now comparable to the world's leading airports.
- Highways/Roads connectivity has sharply improved.
- Average freight train speed has increased from 24kmph to 37kmph since 2014.
- Turn round time at ports has reduced from 92hrs to 53hrs.
- Access to electricity has improved from 85% to ~100% of population.
- Power availability in rural areas has improved from 12:30 hrs in 2014 to 22:30 hrs presently.
- Wireless connectivity is amongst the cheapest in the world and is widely available.
- Digital transactions have increased from less than 4% of GDP in 2016 to more than 75%
- Waiting times for various government services have reduced meaningfully.

Source: Skytrax, Indian Railway annual report, Ministry of Port, Shipping and Waterways, IBEF, World Bank, Morgan Stanley

While physical infrastructure in India has improved, it is the digital infrastructure where India is probably at the forefront. JAM Trinity and UPI are key enablers for this. According to the World Bank “In just six years, India has achieved a remarkable 80% financial inclusion rate that would have taken nearly five decades”. Digital infrastructure has improved tax compliance, reduced leakages, improved access to government services and fostered innovation, accelerated technological advancement & job creation. Some of the achievements of Digital India are listed in the adjoining table (fig 4). India’s digital stack is now going global and a number of countries are implementing their own version of India’s digital infrastructure.

Digital India - Achievements

- Highest real-time payments by volume globally
- 10bn UPI transactions in Sep-23
- Over 137 Cr Aadhaar enrolments
- 1745 e-Services at UMANG
- 700 Digital villages
- 1022 on-boarded e-Hospitals
- 7 Cr beneficiaries of Digital literacy

Source: ACI Worldwide, Ministry of electronics and IT, PIB

fig 4

In addition to improving physical and digital infrastructure, India has also undertaken reforms to improve its business climate. These reforms, some of which are listed in the adjoining table (fig 5), have increased formalization, improved compliance, promoted ease of doing business, reduced bottlenecks in infrastructure development and incentivized manufacturing. Interestingly, the budget speech by Honourable Finance Minister mentioned that India has reduced 39,000 compliances and decriminalized over 3,400 legal provisions. Additionally, Honourable Prime Minister stated that the government intends to draft laws in a simple and easy-to-understand language.

Key reforms of last decade

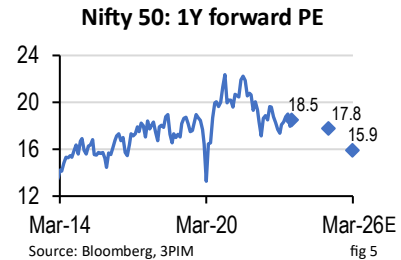
- GST + Digitisation of payments
- Simplification of laws
- Make in India / PLI
- Corporate tax cut
- RERA and IBC
- Gati Shakti
- Social reforms
- JAM trinity

fig 5



Markets outlook

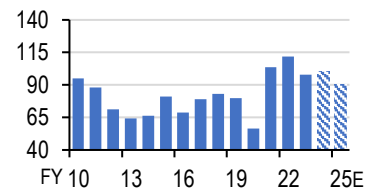
While markets continue to do well (YTD Nifty is up 7.9%), two-year Nifty CAGR at 4.9% is lower than nominal GDP growth. As a result, India's market cap to GDP and 1Y forward PE multiple have declined from 115% to 106% and from 23.2x to 18.5x respectively (fig 5,6). Currently, Nifty 50 is trading at 17.8x FY25 and 15.9x FY26 PE.



While FY25 multiple is marginally higher than long-term average, in our opinion, the following factors are supportive of higher multiples.

- **Improved growth prospects:** As discussed earlier and in April - June quarterly, India's economic growth is expected to improve from 6% to 7-8% for the current and next decade.
- **Lower cost of capital:** A result of lower inflation and volatility (fig 7).
- **Higher domestic equity flows:** India has witnessed a significant and structural increase in local equity flows.

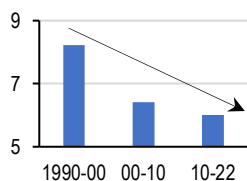
India market cap to GDP (%)



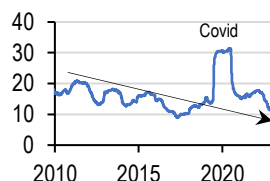
Note: Market cap and GDP for the end of the financial year. For FY24,25 IMF GDP estimates and current market cap are considered | Source: MOSL, 3PIM

fig 6

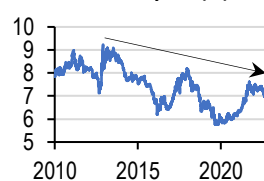
India's Decadal[^] inflation (%)



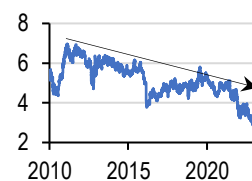
Nifty 50 volatility* (%)



India 10Y yield (%)



India - US 10Y yield (ppt)



Note: [^]Decadal inflation is CAGR, *Annualized standard deviation of daily returns of Nifty 50 | Source: Bloomberg, RBI, 3PIM

Over the past two years, CAGR of small and mid-cap stocks (SMIDs) is ~15% vs ~5% for large caps (fig 8). In our opinion, large caps now offer a better risk-reward over the medium to long term. This is reflected in the portfolio, which is 76% in large caps.

(%)	6M	1Y	2Y
NIFTY 50	12.5	15.8	4.9
Nifty Midcap 100	33.5	33.4	15.7
Nifty Smallcap 250	38.3	34.9	14.4

Note: 2Y returns are annualized | Source: Ace Equities, 3PIM

fig 8

Risks

Indian economy has secular growth characteristics. It has grown every year in the last four decades, except in 2020 due to lockdowns. Given the additional tailwinds of manufacturing and services, the risks to economic growth are low in our opinion.

➤ However, equities are prone to volatility. In the past, markets corrected in periods of FPI selling. While it is hard to forecast FPI outflows, the impact should now be less because of strong local flows. **Evidence of this was visible when markets held steady in Oct 21 – Aug 22, despite significant FPI outflows, equivalent to 0.8% of market cap** (fig 9).

Nifty and FPI flows

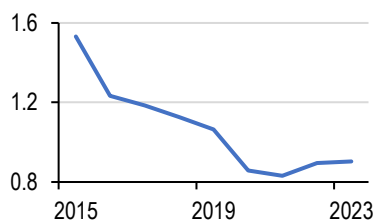
	FPIs Outflows as		
	outflows (Cr)	% of Mcap	Nifty (%)
May06 - Jun06	-6,829	0.21	-30
Jan08 - Oct 08	-51,754	0.72	-60
Mar15 - Feb16	-27,979	0.27	-23
Jan20 - Mar20	-48,030	0.31	-38
Oct21 - Aug22	-2,01,636	0.80	-4

Source: KIE, Bloomberg

fig 9

➤ Oil prices have risen from \$75 to \$95 in the last three months. As we have been highlighting, investments in conventional energy have declined in recent years given the likely shift towards renewables (fig 10) ; should the supply of conventional fuels fall faster than demand, it could result in sustained high prices. Fortunately, India is now more resilient to higher oil prices, due to rising non-software business services exports and lower growth in oil consumption vs GDP (fig 11,12).

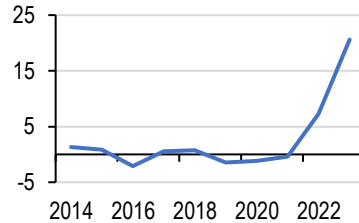
World conventional Energy Investment % of GDP



Source: IEA

fig 10

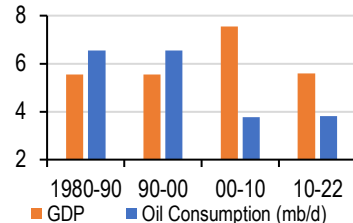
Non-software business services* exports (USD bn)



*R&D, consulting, technical, trade etc | Source: KIE

fig 11

India: GDP and Oil consumption (CAGR)



Source: Bloomberg, 3PIM

fig 12

➤ US yields at 4.8% are at their highest since GFC. This is generally negative for Emerging Markets. However we believe, the impact should be moderate for India :

- Indian economy has done well in the past even during high US rates.
- At -1.5% (FY24E), CAD/GDP is one the lowest in the last 20 years.
- India is a favoured destination for foreign capital. JP Morgan bond index inclusion is also indicative of this.
- Local flows to equity markets are strong.

➤ A sharp increase in the supply of equities. ₹1.8 lac Cr raised* in the last 6 months!

(*from IPO, NFO, QIP, promoter/PE sale etc, source: Antique Equities)

"At its root, risk is about mystery. It focuses on the unknown, for there would be no such thing as risk if everything were known"

- Peter Bernstein

Sector Valuations and Corporate Profitability

As John C Bogle said “**Reversion to mean is the iron rule of financial markets**”. In the last 2 years, richly valued sectors have underperformed and sectors with low multiples have outperformed (fig 14). The divergence across sector valuations has thus reduced.

Corporate profitability has recovered in both aggregate terms and across sectors (fig 15).

Bank NPAs are now at a 10-year low, commodity prices are reasonable and capex is strong. Given normalization in corporate profitability, CAGR of corporate profits should be 12-15%, in-line with nominal GDP growth, in our opinion.

Conclusion

Outlook for economic growth and corporate profitability is strong. Corporate leverage is low and bank balance sheets are healthy. Local flows are resilient and valuations are close to fair.

We believe that it is reasonable to expect ~12% CAGR from Nifty 50 over the long term. These returns broadly comprise of 6-8% real growth and 4-6% inflation. **These markets thus offer a compounding opportunity and are suitable for Long Term investors.**

Portfolio Strategy and Positioning

Our approach to investing is succinctly captured in our name: 3P. The first P stands for **Prudence**. We are focused on investing in sustainable and reasonably valued businesses and will remain effectively diversified to manage risk. The second P in our name represents **Patience**. In investing, patience is a big advantage and its role over the long term is often unappreciated. Our third and final P is **Performance**, a likely outcome of the first two Ps.

As also highlighted in April - June quarterly, in our view, ~90% of the portfolio is in companies that enjoy leadership/strong positions in respective businesses and should be able to increase/maintain their market share. The portfolio currently has ~48 companies (including 2 ETFs). 76% of investments are in large caps, ~13% in mid caps and ~9% in small caps.

Sector Valuations

	Sept-21 (PE)	Current (PE)	15y Avg. (PE)	2Y returns (%)
Cons. Disc.	77.8	60.0	40.5	-0.5
Cons. Stap.	41.1	38.2	30.2	4.0
Pharma	26.4	25.3	21.5	0.6
IT services	30.0	22.6	18.6	-24.6
Autos	24.0	18.8	16.4	27.7
Nifty	23.2	19.4	16.4	5.0
Oil & gas	16.3	12.3	11.6	-1.4
Pvt banks (PB)	2.8	2.4	2.5	20.6
Cont. Mat.	31.6	34.0	20.4	-7.4
Cap. goods	28.3	33.3	22.3	64.1
Metals & mining	7.7	9.8	9.8	-4.3
Electric utilities	10.4	12.4	13.2	37.0
PSU banks (PB)	1.1	1.1	1.2	27.1

Note: 1Y forward PE, Data till Aug 23 | Source: KIE estimates

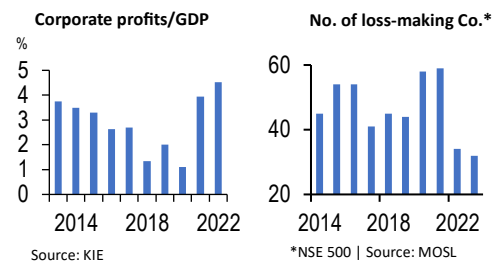


fig 15

Interestingly, the journey of Sensex from 100 in 1979 to 59,000 in FY2023 (44 years), is one of doubling ~9 times i.e. once every ~5 years

The portfolio is well diversified across sectors and key economic variables. The Fund is overweight financials, consumer discretionary, industrials, utilities and is underweight IT, oil and gas, consumer staples and materials. **Given the recent outperformance of small and mid caps, the portfolio is tilted towards large caps.** We will look to increase exposure to small and mid caps meaningfully during market downturns.

The number of companies in the portfolio has increased as some small cap companies rallied before we could complete our purchase and because of lower allotment in IPOs due to oversubscription.

The 3P India Equity Fund 1 continues to perform well. Fund returns from 4th May to 29th September are 16.77% (pre-tax, pre-management fees) vs Nifty 50 TRI returns of 8.38%. The Fund NAV is on a post-tax, post-management fees basis. Currently, the provision for tax on gains is on short term basis. We expect the provision for tax to moderate as short term capital gains convert to long term capital gains over time. Presently the Fund size is ~₹5,800 crores (including 29th September flows).

In our endeavour to not only avoid conflict of interest between customers and 3P but to align their interests, the sponsor has invested ₹101 crores in this Fund. Further, under normal conditions, the 3P team will not purchase direct listed equities in the secondary market.

Annexure A details the Fund Portfolio as of September 29th 2023, sectoral composition and a brief rationale for the same. Annexure B contains regulatory disclosures.

We thank you for your continued support to the 3P India Equity Fund. We are grateful for your trust and partnership. As the saying goes, "Success doesn't come from what you do occasionally. It comes from what you do consistently." We are committed to managing your investments with a long-term focus, discipline, low costs and complete alignment of interest.

We plan to share the next Fund update around New Year 2024. We wish you and your family a happy and prosperous festive season.

Kindly note that 3P India Equity Fund 1 is an open-ended Fund with no entry or exit load. The Fund is available for transactions on every 15th/last working day of the month.

Please feel free to reach out to the undersigned or services (services@3pim.in) for any clarifications, feedback or suggestions.

Warmly,

CIO and Fund manager



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