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AMBIT ASSET MANAGEMENT

October 2020

MONTHLY NEWSLETTER

GOOD & CLEAN by AMBIT

Ambit Good & Clean Portfolio

COFFEE CAN PMS

Ambit Coffee Can Portfolio

EMERGING GIANTS by AMBIT

Ambit Emerging Giants Portfolio

EQUITY INVESTMENTS & PMS ARE SUBJECT TO MARKET RISKS,
READ ALL SCHEME RELATED DOCUMENTS CAREFULLY BEFORE INVESTNG

Invest in companies with…

Dear Investor,

1A) Mid & Small cap potential and valuations

While one needs to have a well-diversified approach to investing across asset classes (fixed income, equity, real estate) we would like to specifically address allocations under the subset of equities.

Large Cap + Mid & Small Cap = Balanced Portfolio

While we have spoken about the importance of diversification amongst stocks, sectors and importance of drawdowns in the past ***we think the time is most apt to talk about the importance of holding investments across a variety of companies limited not just to large caps but also mid and small caps.***

Besides the conventional arguments for diversification this is supported by:

1. Leading small and midcaps are trading at attractive valuations vs their large cap peers. For many of these smaller companies business case has not deteriorated over the long term. The false perception of higher risk in leading franchises simply by virtue of them being a small or midcap allows better entry valuations.

2. We conduct a study of the top 1000 listed companies across market capitalisation to find that companies that are able to grow and upgrade to a higher category over the past decade (e.g. from Mid cap to Large cap or from Small cap to Midcap for instance) are likely to substantially generate outstanding returns ***(Ref to Exhibit 1)***

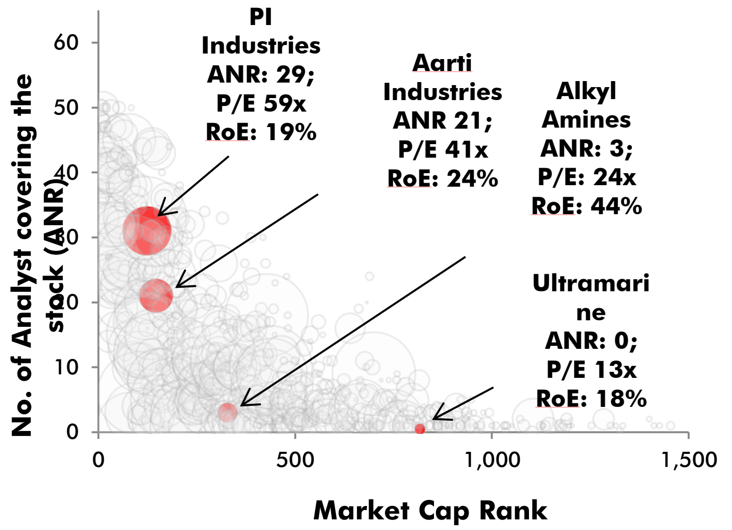
3. One of the key reasons for this superior return is consistent earning over the long term aided by better discovery of the smaller stocks which leads to a rerating of the PE multiples for these stocks. ***(Ref to Exhibit 2)***

Exhibit 1: Identification of companies that can upgrade to a higher category leads to disproportionate returns

Avg. Performance CAGR %		March 2010			
		1-100	101-250	251-500	501-1000
March 2020	1-100	6%	21%	34%	
	101-250	-6%	9%	21%	37%
	251-500	-20%	-34%	6%	22%
	501-1000	-32%	-18%	-9%	5%

Source: Ambit Asset Management, Large cap= companies 1-100th , Midcap= companies 100-250th ,Smallcap= companies 250th -1000,

Exhibit 2: Ignore short term pains to focus on the long term return journey, better discovery leads to better multiples



Source: Ambit Asset Management

1B) The Core-Satellite approach in theory

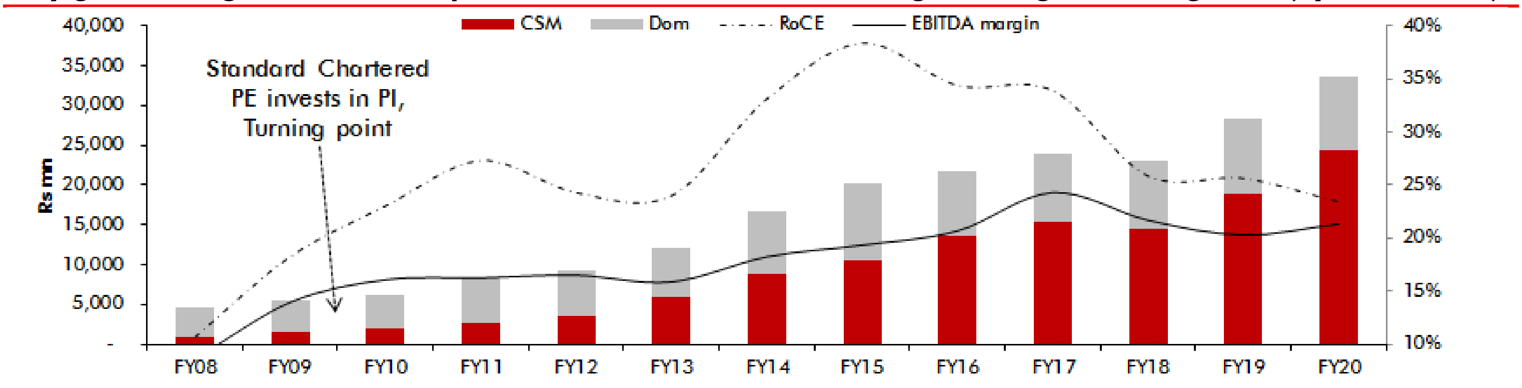
Consistency + Alpha = Wealth creation

The core-satellite approach provides an opportunity to access the best of all worlds. Better- performance, limited volatility, and cost control. In the simplest form it can be defined as an approach to Investing which has two parts- a core, which helps build stability on account of liquidity and lower costs as a result of lower churn (we propose large cap investments over long time horizons) and a satellite or a smaller part of the portfolio which helps prop up returns (we propose mid and small caps to improve return profile given favourable valuations vs. long term average)

While large caps have run up, they surely cannot be ignored; they lend a stability like no other to portfolio returns over the shorter term and provide liquidity. Small and Midcaps on the other hand might be more volatile but this volatility is really what allows for better entry prices for Investors. Today this sort of opportunity exists in small and midcaps and investors would be well advised to improve or increase exposure to funds with such schemes.

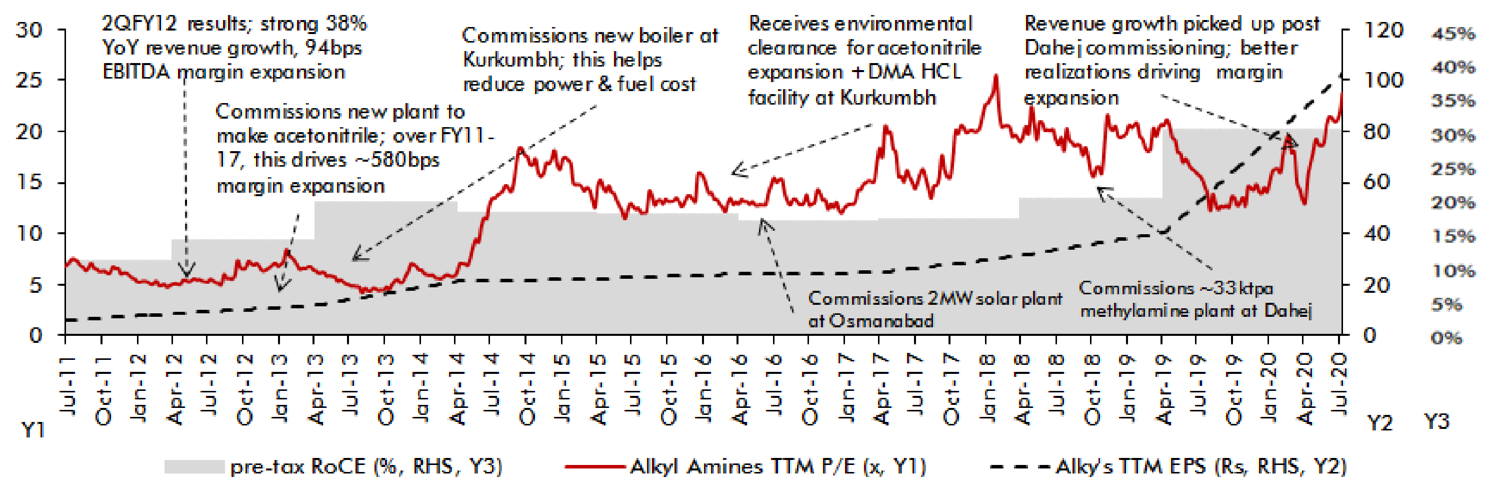
1C) The Core-Satellite approach in practice

Exhibit 3: Adding larger companies to your portfolio (PI Industries) assists in giving stability to your portfolio as they grow through continuous improvements and consistent earnings leading to stable growth (5yr CAGR 25%)



Source: Ambit Asset Management, Note: 5 yr CAGR from 30th Sep, 2015 to 30th Sep, 2020

Exhibit 4: ...While adding smaller companies which were less discovered but show good aptitude for growth helps adding to portfolio returns substantially over 3-5 years. As these companies get discovered and their capabilities are proven these companies grow earnings and multiples re-rate too (Alkyl Amines 5yr CAGR 60%)



Source: Ambit Asset Management, Note: 5 yr CAGR from 30th Sep, 2015 to 30th Sep, 2020

2) Right to Win

In the first section of this note we see how as part of an equity portfolio approach it makes the most sense to have a portion of your investment capital assigned to large caps and a portion of it assigned to mid and small caps. While that may be a higher level classification the stock specific approach is equally relevant. ***In this section*** we argue that one must identify companies with a "Right to win"

A precondition to pinpoint and include such companies is the clear identification of characteristics of such companies with The Right to Win ***(Ref to Exhibit 5).***

Having identified such companies for our client portfolio schemes which we believe to have winning abilities or what some might consider strong market positioning, we go on to segregate these companies based on **Positioning** (formidable challenger, segmental/regional leader or an Industry leader) and **Peer dynamics** (Monopoly, Duopoly, Oligopoly and Fragmented Industry) ***(Ref to Exhibit 6,7 & 8)***

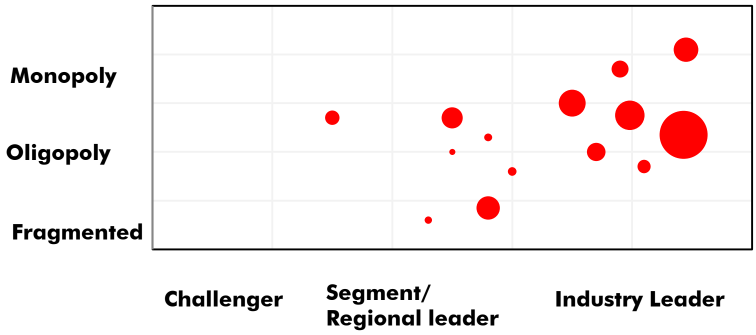
This helps us have a better grasp on picking companies with winning traits so as to create portfolios which deliver superior risk adjusted returns. We take the view that market leaders are likely to be beneficiaries of the prolonged pain in the economy as there exists, a flight to safety, preference for strong balance sheet companies and fondness for those with competitive moats in consolidating industries. ***These Leaders are present across the equity investing universe and not limited to large caps but also extend to mid and small caps.***

Exhibit 5: Characteristics we identify of companies with winning traits

Winners	Losers
Strong balance sheet	Weak balance sheet
Low D/E	High debt
Strong brand equity	Limited ability to raise funds
Strong distribution	Low scale and limited reach
Leadership position will help garner market share	Unorganised segment
Adaptability to changes	Low competitive advantage

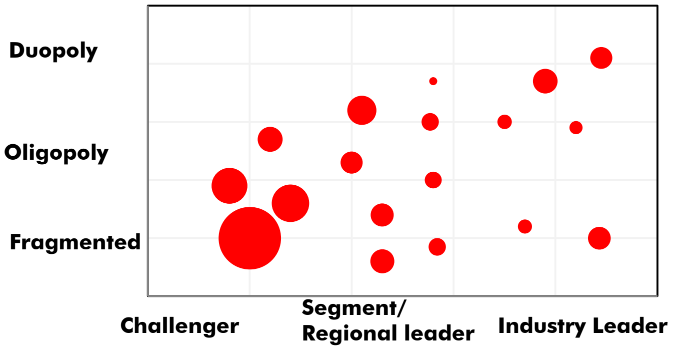
Source: Ambit Asset Management

Exhibit 6: Coffee Can portfolio (CCP) Right to Win Positioning +Peer dynamics



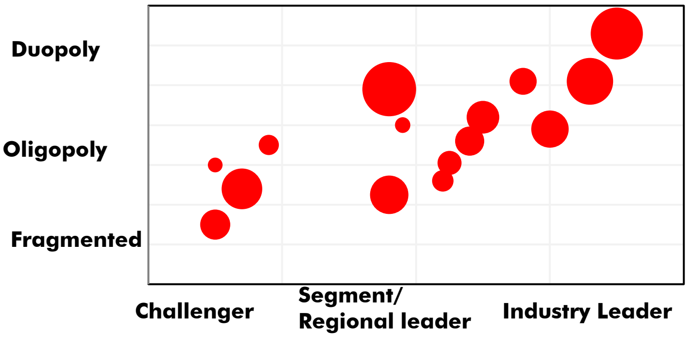
Source: Ambit Asset Management, Note: Size of Bubble=Market cap

Exhibit 7: G&C Right to Win Positioning+Peer dynamic



Source: Ambit Asset Management, Note: Size of Bubble=Market cap

Exhibit 8: EG Right to Win Positioning +Peer dynamics



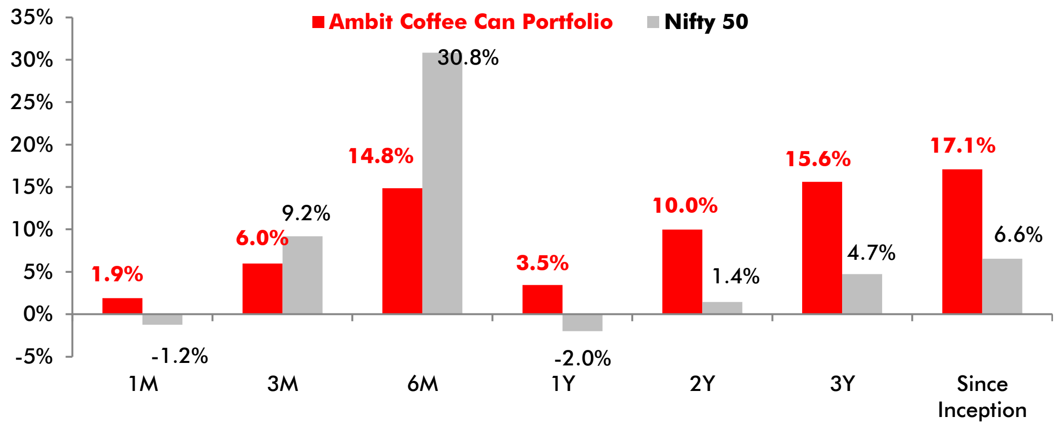
Source: Ambit Asset Management, Note: Size of Bubble=Market cap

Conclusion: Firstly, An equity investor must look to Invest in a combination of small and midcap stocks to improve portfolio performance. While large caps have a role to play in wealth creation and stability it is the mid and small caps which lend qualities beyond diversification and at better valuations. ***Secondly,*** The Balanced approach (Core satellite approach) is the one that can have best risk reward profile in the coming times and should be actively considered by investors.***Thirdly,*** Investing in a portfolio of companies with a right to win is extremely important and it is increasingly of significance given the pain points in the economy presently.

Ambit Coffee Can Portfolio

At Coffee Can Portfolio, we do not attempt to time commodity/investment cycles or political outcomes and prefer resilient franchises in the retail & consumption oriented sectors. The Coffee Can philosophy has unwavering commitment to companies that have consistently sustained their competitive advantages in core businesses despite being faced by disruptions at regular intervals. As the industry evolves or is faced by disruptions, these competitive advantages enable such companies to grow their market shares and deliver long-term earnings growth.

Exhibit 9: Ambit's Coffee Can Portfolio performance update



Source: Ambit; Portfolio inception date is March 6, 2017; Returns as of 30th Sep, 2020; All returns are post fees and expenses; Returns above 1 year are annualized; ***Note:*** *Returns prior to Apr'19 are returns of all the Pool accounts excluding non-aligned portfolio, and returns post Apr'19 is based on TWRR returns of all the pool accounts.*

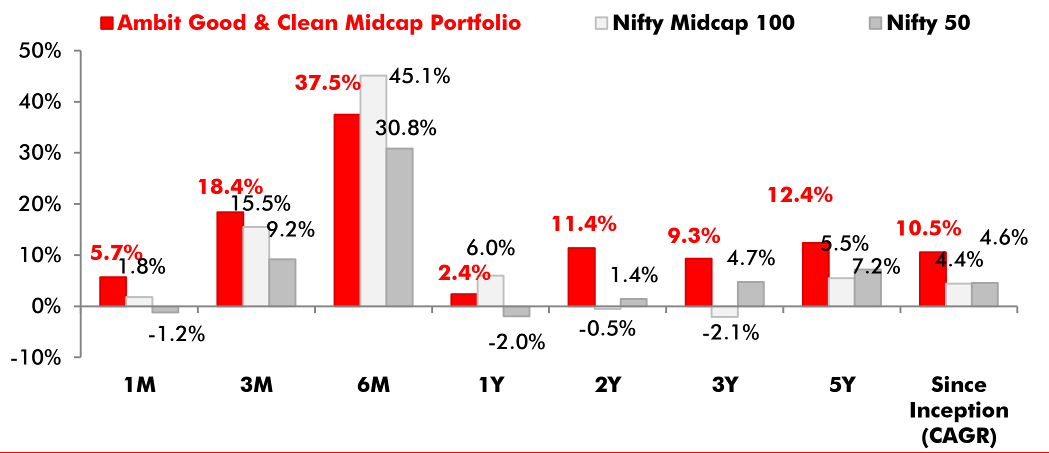
Ambit Good & Clean Portfolio

GOOD & CLEAN by AMBIT

Ambit's Good & Clean strategy provides long-only equity exposure to Indian businesses that have an impeccable track record of clean accounting, good governance, and efficient capital allocation. Ambit's proprietary 'forensic accounting' framework helps weed out firms with poor quality accounts, while our proprietary 'greatness' framework helps identify efficient capital allocators with a holistic approach for consistent growth. Our focus has been to deliver superior risk-adjusted returns with as much focus on lower portfolio drawdown as on return generation. Some salient features of the Good & Clean strategy are as follows:

- **Process-oriented approach to investing**: Typically starting at the largest 500 Indian companies, Ambit's proprietary frameworks for assessing accounting quality and efficacy of capital allocation help narrow down the investible universe to a much smaller subset. This shorter universe is then evaluated on bottom-up fundamentals to create a concentrated portfolio of no more than 20 companies at any time.
- **Long-term horizon and low churn**: Our holding horizons for investee companies are 3-5 years and even longer with annual churn not exceeding 15-20% in a year. The long-term orientation essentially means investing in companies that have the potential to sustainably compound earnings, with this compounding earnings acting as the primary driver of investment returns over long periods.
- **Low drawdowns**: The focus on clean accounting and governance, prudent capital allocation, and structural earnings compounding allow participation in long-term return generation while also ensuring low drawdowns in periods of equity market declines.

Exhibit 10: Ambit's Good & Clean Portfolio performance update



Source: Ambit; Portfolio inception date is March 12, 2015; Returns as of 30th Sep, 2020; All returns above 1 year are annualized. ***Returns are net of all fees and expenses***

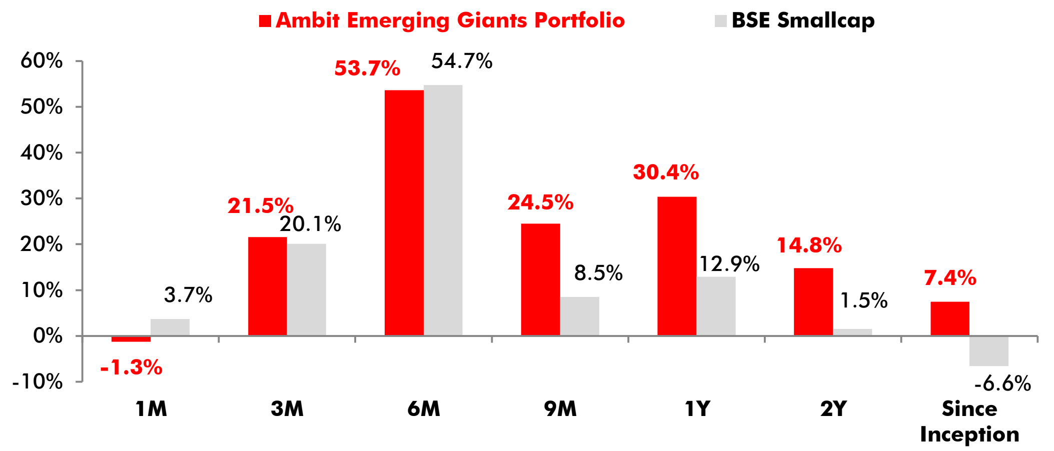
Ambit Emerging Giants

Smallcaps with secular growth, superior return ratios and no leverage

EMERGING GIANTS by AMBIT

Ambit's Emerging Giants portfolio aims to invest in small-cap companies with market-dominating franchises and a track record of clean accounting, governance and capital allocation. The fund typically invests in companies with market caps less than Rs. 4,000cr. These companies have excellent financial track records, superior underlying fundamentals (high RoCE, low debt) and ability to deliver healthy earnings growth over long periods of time. However, given their smaller sizes these companies are not well discovered, owing to lower institutional holdings and lower analyst coverage. Rigorous framework-based screening coupled with extensive bottom-up due diligence lead us to a concentrated portfolio of 15-16 emerging giants.

Exhibit 11: Ambit Emerging Giants performance update



Source: Ambit; Portfolio inception date is December 1, 2017; Returns as of 30th Sep, 2020; All returns above 1 year are annualized. ***Returns are net of all fees and expenses***

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