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AMBIT ASSET MANAGEMENT

September 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

Calling your inner Captain Cool!

Dear Investor,
Our fund managers often lay emphasis on the importance of EQ (Emotional Quotient) in fund management over the traditional parameter of IQ which only gauges ones intelligence. The last 6 months have been the ultimate test. The extreme volatility tested investor ability to handle extreme pressure and calmly act without being influenced by external factors. While data might tempt one to time the market, returns suggest remaining invested was the best strategy.

We all need to invoke our inner Captain Cool, it could also be a great idea to take a lesson or two from the life of the real Captain himself, India's ex-Captain MS Dhoni, who hung up his boots recently. In this newsletter, we draw attention to 'Captain Cool's' qualities for winning in running a business or Investing.

Bumpy road to the top...

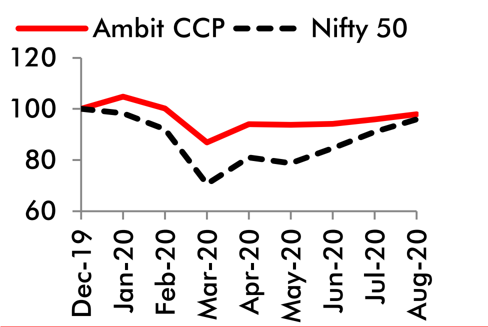
The time and the extent of both the fall (Till Mar-23) and the recovery (up till now) was unprecedented. While we refrained from acting impulsively to short term data points and making numerous changes, we continued to calmly spend the time on studying change in risk reward arguments of our portfolio companies (if applicable) and trying to identify new contenders which may throw us some opportunity in the recent volatile market environment.

Exhibit 1: Ignore short term pains to focus on the long term return journey

	Net Sales YoY%		EBITDA YoY%		PAT YoY%	
Coffee Can PMS	**4QFY20**	**Q1FY21**	**4QFY20**	**Q1FY21**	**4QFY20**	**Q1FY21**
Weighted avg	-3%	-18%	-2%	-24%	-14%	-24%
Median	-3%	-21%	1%	-46%	-6%	-26%
Nifty	-5%	-30%	-4%	-12%	-20%	-32%
Good & Clean PMS	**4QFY20**	**Q1FY21**	**4QFY20**	**Q1FY21**	**4QFY20**	**Q1FY21**
Weighted avg	-2%	-14%	-6%	-25%	-11%	-34%
Median	-2%	-15%	-2%	-23%	-13%	-15%
Nifty Midcap 100	-3%	-33%	-15%	-49%	NM	NM
Ambit Emerging Giants PMS	**4QFY20**	**Q1FY21**	**4QFY20**	**Q1FY21**	**4QFY20**	**Q1FY21**
Weighted avg	-6%	-11%	5%	19%	12%	35%
Median	-11%	-14%	2%	-30%	-11%	-32%
BSE smallcap	-13%	-31%	-71%	-89%	-43%	-9%

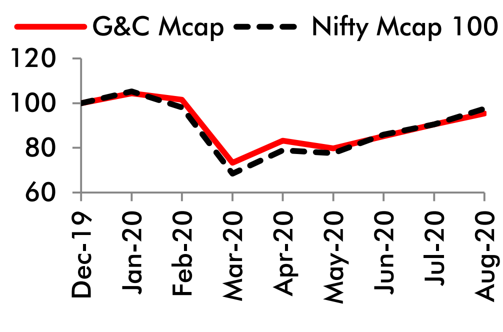
Source: Ambit Asset management, Indices data is taken from Bloomberg, NM=Not meaningful

Exhibit 2: Ambit CCP returns CYTD



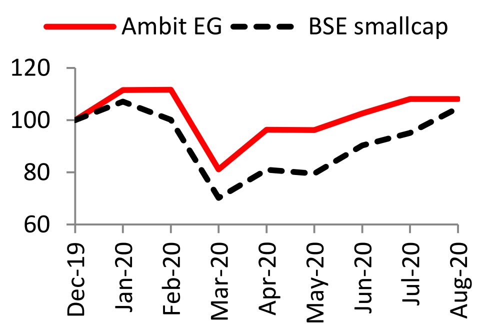
Source: Ambit Asset management

Exhibit 3: Ambit G&C returns CYTD



Source: Ambit Asset management

Exhibit 4: Ambit EG returns CYTD



Source: Ambit Asset management

All three portfolios have not only outperformed Index in the long run but also defied gloom and doom to show resilience. In your journey to long term wealth creation it is important to choose quality and consistency as it leads to lower drawdowns and downside protection. This means that all your portfolios not only protect your principal and returns on the way down but also reduce volatility. The ability to protect downsides can be profound on portfolio performance over the combined periods of fall and recovery.

This is directly observable below:

1. 1st Jan-31st Mar: **Fall period**
2. 1st Apr-31st Aug: **Recovery period**
3. 1st Jan-31th August: **Fall & Recovery period combined**

Ambit Coffee Returns: ~4% outperformance

- **Fall period**: -13% vs. Nifty's -29%
- **Recovery period**: 12.7% vs. Nifty's 32.4%
- **Combined (F+R)**: -2% vs. Nifty's -6.4%

Ambit Good & Clean Returns: ~ (-2)% almost in line performance

- **Fall period**: -27% vs. Nifty Midcap 100's -32%
- **Recovery period**: 30% vs. Nifty Midcap 100's 42%
- **Combined (F+R)**: -5% vs. Nifty Midcap 100's -3%

Ambit Emerging Giants Returns: ~21% outperformance

- **Fall period**: -19% vs. BSE smallcap's -30%
- **Recovery period**: 56% vs. BSE smallcap's 49%
- **Combined (F+R)**: 26% vs. BSE smallcap's 5%

That's the way, Mahi way...

A. Lessons for Investors from MSD's innings

1. Those who lead well always stay calm:

- Dhoni is named as Captain Cool because he controls his emotions better than others. He is able to handle stress and take decisions with a cool and calm mind. It is one of his universally respected traits by fans and critics alike and it should be what every investor should aspire to move towards.
- *A Calm mind and a clear head allow for well thought out decisions based on logic and reason rather than emotional and reactive decisions triggered by fear and greed.*

2. Detail oriented & flexible:

- During the World Cup 2011, when India lost 3 wickets early on, Dhoni who usually comes in at 5th or 6th down, decided to change up the batting order. Given the target to chase was tough and more important the man at the crease was a left handed Gautam Gambir, Dhoni made the quick decision to go in place of a left handed Yuvraj Sigh (who was already padded up and rearing to go). He accounted for the new and existing information and took a call given Dhoni's own batting style, ability to give stability at a tough juncture and also make the opposing teams bowlers life much harder by playing a combination of Right & left handed batsmen together (tough combination to bowl to).
- *In investing too it is important to focus on the details (knowable and important), account for new information delivered in terms of actions, announcements, price or other considerations (fundamental or otherwise). A fixed approach does not work every time in investing or in cricket. It is important to be receptive and stay flexible.*

3. Identify and Invest into Quality, Returns will follow:

- Dhoni invested time to nurture talent. Few of the talents bright young stars he nurtured included the likes of Virat Kohli, Suresh Raina, R. Ashwin, Ravindra Jadeja, Rohit Sharma and Bhuvneshwar Kumar.
- *Stock picking follows a similar process of looking for the right business through hard work, research and continuous tracking and involves patiently investing the time to see your investments grow. If stock picking is done diligently from a choice of quality companies with strong differentiating characteristics, the returns will follow.*

4. Hone your skills, build expertise and focus on your circle of competence:

- Dhoni was passionate about cricket since childhood and spent every waking hour to either play cricket or when not playing he spent his time on ways to improve his game or self-reflect. He focussed on his passion and circle of competence, built his expertise and scaled from there to become one of the most successful cricketers in the world.
- Dhoni started his career with ODI Cricket (2004) & later Test (2005). He became captain of the Indian Cricket team in 2007 and in 2008 went on to receive Rajiv Gandhi Khel Ratna Award, ICC ODI player of the year. Notable in 2009 Dhoni was awarded with the Padma Shri and ofcourse in 2011 he went down in history when India bagged the World Cup under his leadership.
- *As an investor it is important to identify your circle of competence. It allows you to believe whole heartedly in your investments, work hard on understanding their "right to win" and to keep your investment arguments razor sharp allowing you to withstand periods of negative return or low return. Having this focus and clarity allows us to achieve our investment goals (World cups and Padma Shri's if you will) successfully.*

5. Getting the right mix:

- M.S. was a team captain like no other, he brought in the right mix of players, eased out some senior (older) players and looked for a winning mix rather than a winning player. All the matches that India won under Mahi, none were attributable to just batsmen or just bowlers, India won under Mahi as a team!
- Similarly the approach that works best while investing is a well-diversified portfolio approach. If you invest all your hard earned money in a single stock, and if it fails, you will be in trouble, if you identify 1-2 multibaggers but lose money in all your remaining stocks too you will be in trouble. It is your overall portfolio returns (team performance) that makes a big difference eventually.

B. Companies that succeed the Mahi way!

1. Those who lead from the front: Avenue Supermart

- Avenue Supermart found itself in a difficult spot during the sudden lockdown when employees were unable to show up for work considering the safety risks and logistical challenge. When faced with a challenge the company took up an unconventional, long term and cool headed approach rather than the reactive stick approach many peers used.
- These initiatives highlighted the company's ability to lead from the front and take tough decisions which helped it whether the toughest of times while caring for all its stakeholders. D-mart batted on the front foot and announced:

a) ***A hardship allowance for all frontline workers*** who continued to work during the lockdown, covering ~95% of all personnel be it from direct and indirect stores, distribution centers or packing centers. While others were busy cutting salaries, many D mart employees (warriors) earned more than double their usual wage.

b) ***Additional COVID-19 leave for employees*** with symptoms and created a backup for every office working team so that if one had to be quarantined, the other could take over.

c) ***Online delivery was started*** at most of the stores and DMart on Wheels project was taken up where local store teams set up a mini store with a small assortment of essential products in a large housing complex for 6-8 hours.

2. Calmness / handling of pressure: Britannia Industries

- Britannia was faced by a crisis when the Indian government launched a nationwide lockdown. The Britannia team was as shocked as everyone else perhaps but that did not lead to any feeling of regret or helplessness. The team saw the opportunity and went after it. Britannia anticipated the situation and expected increase in In-home Packaged Foods consumption compared to peers and took the necessary steps.

a) ***The company was the first to restart operations*** with better availability vs. competition through the lockdown. Britannia delivered 24% volume growth in April & May together, highest in the FMCG.

b) ***Britannia also grabbed market share*** and expanded distribution Britannia used the opportunity to expand into Hindi hinterland by increasing reach to 22,000 Rural preferred dealers (up 16% QoQ) as smaller companies faultered to fulfill the demand. This also encouraged it to announce a capex of Rs700cr for next 2-3 years for 5 new facilities

- The management's agility, decision making process, flexibility to alter path to suit the current environment were all possible through a calm and composed approach in handling pressure.

3. Those who are detail oriented and flexible: CIFC (Chola)

- While Mahi exhibited this above trait both on and off the field as we saw in the previous section we also found a company that made a name for itself, consistently showcasing this trait.

- CIFC (Chola) is a company that understands CV cycles better than peers. The company does so by having a detail oriented focus which allows the company to identify trends before they occur. The company also knows that the same approach does not work every time. It is flexible, for instance CIFC slowed disbursement to HCV & MHCV when the forecasted the CV cycle slowed down & focused growth on Tractors and LCV instead, departing from the norms it may have earlier set for itself.

4. Identify and take sensible risks, Returns will follow: Asian Paints

- The mastermind that he was, Dhoni took bets on and nurtured new talent within the Indian cricket team, a strategy which paid off well. One great example was Mahi's usage of part-time spinners like Yuvraj Singh, Virender Sehwag and Suresh Raina, who helped him add an additional batsmen rather than a full time bowler. We all know the magic which Yuvraj Singh demonstrated with his bowling skills in the 2011 world cup. This solved two purposes; the batting line had depth with an additional batsman & part-time spinners eventually turned out to be good bowlers.
- One such corporate mastermind is Asian Paints, a paints based leader, constantly taking bets on and nurturing new and promising segments. The company entered the water proofing segment despite the presence of a strong and existing market leader. Today in many markets pockets, Asian Paints has surpassed peers and become a leader itself while expanding the category. The company identified a sensible risk worth taking and went on to execute a calibrated approach to meeting its goal, the strategy paid off handsomely.

5. Hone skill expertise+focus on circle of competence: Aavas financiers

- Aavas, an affordable housing financier, dealing in self-employed segment is a classic case on how seemingly easy systems & processes on paper become difficult to replicate in real life.
- Aavas is one of the few companies who have cracked the self-employed lending space by following templated tech based lending through 100% in-house sourcing team, deeper penetration into semi-urban & rural geographies and a robust 4 layered collection team, a commendable feat given the tough operating segment. This has all led to industry-leading asset quality, with NPAs even better than peers dealing in 'low-risk' salaried segment.

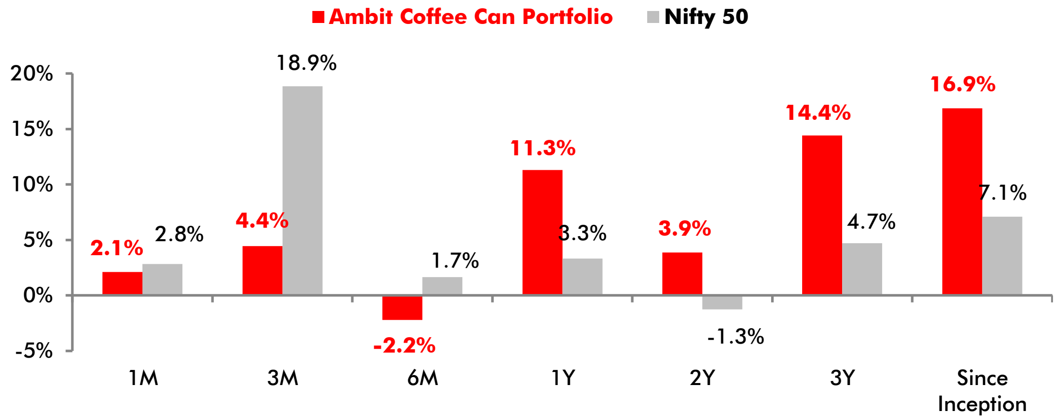
6. Getting the right mix:

- As is applicable to our Investing analogy (Section A), so is it applicable to the characteristics required of successful companies. MS brought in the right mix of players, eased out some senior (older) players and looked for a winning mix rather than a winning player. India won under Mahi as a team!
- The key to growth, be it for team India or a successful company is backing new products (players) and winning as a company (team). Similar to Dhoni, Pidilite's success has come from banking on new products, leading to a virtual monopoly status in many segments like Fevicol, Fevikwik & M-seal. While new and promising products are given a push, less successful ones are phased out. It is from such an approach that successful products and brands get launched from time to time and contribute to the overall companies success.
- One such example is Pidilite's Dr. Fixit brand, which was one of its pioneer products earlier, now contributes substantially to its current's growth trajectory and is synonymous with water-proofing in India. Pidilite nurtures new products/categories, so the company has better odds of winning tomorrow. While current Revenue mix for Pidilite of Adhesive: Others stand at 75:25 over the next 3 years Pidilite aspires to make it 50:50.

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 5: Ambit's Coffee Can Portfolio performance update



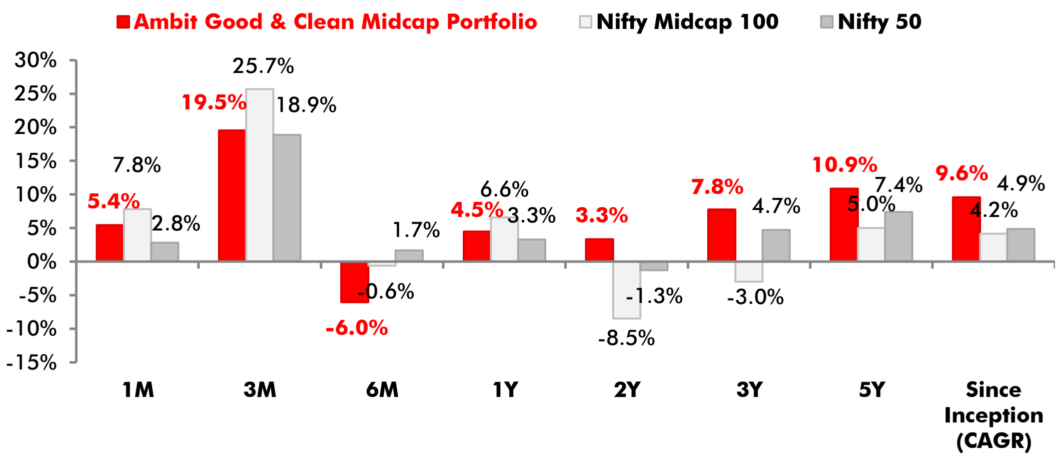
Source: Ambit; Portfolio inception date is March 6, 2017; Returns as of 31st Aug, 2020; All returns are post fees and expenses; Returns above 1 year are annualized; ***Note:*** *Returns prior to Apr'19 are returns of all the Pool accounts excluding non-aligned portfolio, and returns post Apr'19 is based on TWRR returns of all the pool accounts.*

Ambit Good & Clean Portfolio

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 6: Ambit's Good & Clean Portfolio performance update



Source: Ambit; Portfolio inception date is March 12, 2015; Returns as of 31st Aug, 2020; All returns above 1 year are annualized. ***Returns are net of all fees and expenses***

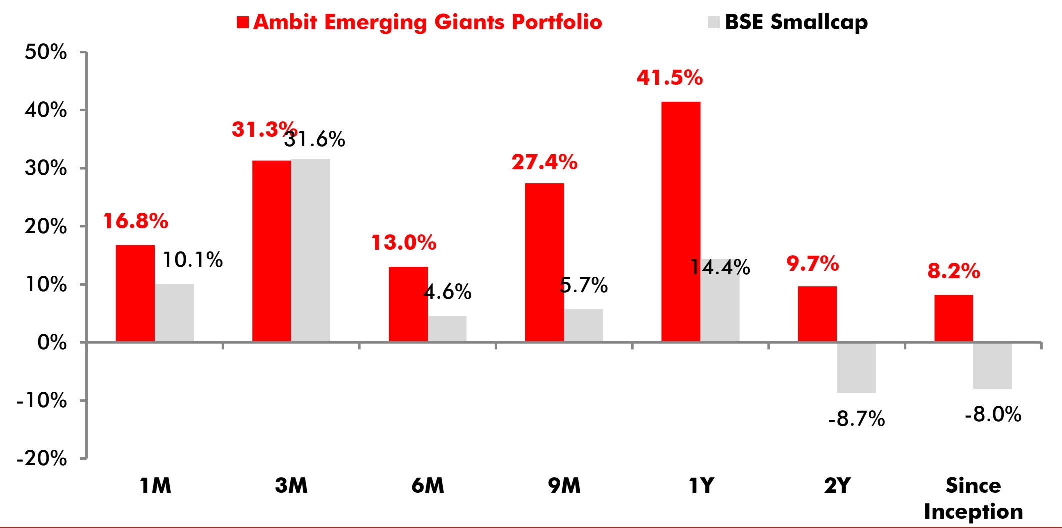
Ambit Emerging Giants

EMERGING GIANTS by AMBIT

Smallcaps with secular growth, superior return ratios and no leverage

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 7: Ambit Emerging Giants performance update



Source: Ambit; Portfolio inception date is December 1, 2017; Returns as of 31st Aug, 2020; All returns above 1 year are annualized. ***Returns are net of all fees and expenses***

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