Nepean Capital
1Q CY2024/4Q FY24 Investor Newsletter

The Nepean Long Term Opportunities Fund II is a multi-cap India Special Situations fund. It has given a return of 28.4% (US$) since the first close (Oct 14, 2021), and outperformed the benchmark NIFTY500 by 1140 basis points. Below is the performance, net of fees in US$ as of March 31, 2024:

	Fund 1*				Fund 2**			
Period	**CY18^**	**CY19**	**CY20**	**CY21**	**CY21^^**	**CY22**	**CY23**	**CY24 YTD**
Fund	5.3%	0.0%	35.1%	32.3%	1.3%	-1.8%	35.6%	-4.9%
Benchmark	-7.0%	-11.8%	18.6%	31.7%	-3.0%	-7.3%	25.3%	3.9%
Outperformance (bps)	1230	1180	1650	60	430	550	1030	-880
Since Inception				84.1%				28.4%
Benchmark				28.2%				17.0%
Outperformance (bps)				6020				1140

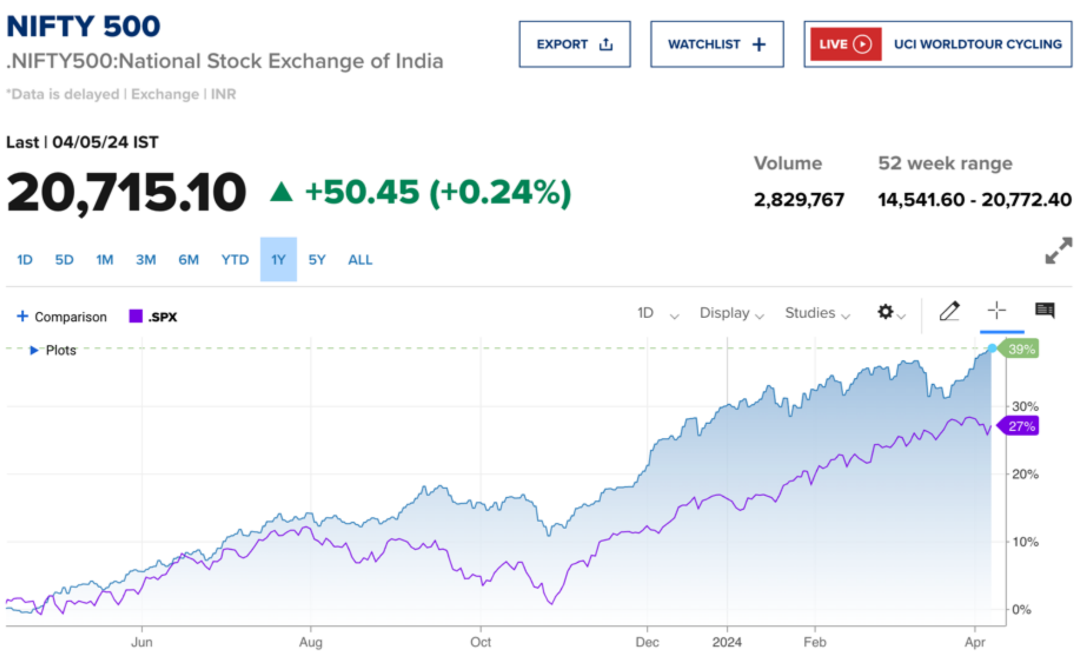
*Benchmark NIFTY Small Cap Index
^First close Sep 18, 2018
NAV is calculated monthly

**Benchmark NIFTY500 Index
^^First close Oct 14, 2021
Fund 1 was closed in May 2021

The fund's performance in the last quarter was impacted by two stocks, Zee Entertainment and Spandana Sphoorty. Zee's proposed merger with Sony's India media business, which would have significantly re-rated the stock, was called off. We have since exited our position. In Spandana's case, the street was concerned with asset quality for the microfinance industry due to farmer protests in the state of Haryana (0.4% of Spandana's loan book) and floods in the southern state of Tamil Nadu. Nepean Capital's Leadership Series fireside chat with the CEO, Shalabh Saxena, reinforced our conviction in the lender. *Please see the link to the fireside chat on page 4 below.*

Positive economic data in fiscal 2023-24 continues to drive the Indian equity market to new highs:

- India's total market cap surged by $1.6 Tn in the past 12 months to $4.7 Tn, +391% over the past 10 years. It's now the 4th largest in the world (clubbing China and Hong Kong as one).
- GDP growth for the quarter ended Dec 31, 2023 rose to 8.4%, highest among large economies.
- March PMI Manufacturing Index jumped to 59.1 (from 56.9 in February), a 16-year high. The index has remained above the 50 mark for the past 33 consecutive months.
- GST collections for the month of March were up 11.5% YoY to Rs.1.78 lakh crores/$21.5 Bn, the second highest on record. As a result, total GST collections for FY24 were Rs.20.18 lakh crores/$24.3 Bn, +65% over the past five years and surpassing the budgeted estimate of Rs.18.10 lakh crores/$21.8 Bn.
- 5G subs crossed 175 Mn, with Reliance JIO at 100 mn and Bharti Airtel at 75 Mn.
- Estimated earnings growth for the NIFTY50 is 16% and 15% for CY24 and CY25, respectively.
- Mumbai, India's largest real estate market by value, clocked sales of 14,145 properties (+7.5% YoY) and the second-best March ever. Over 80% of these sales were residential.
- Last month, UPI transactions rose to Rs.19.78 lakh crores/$2.4 Bn (+41% YoY).
- According to HVS Anarock, February was another strong month for the hotel industry with industry RevPAR of Rs.6,497/$78 (+10% YoY) and occupancies +200 bps YoY at 72-74%.
- In the past 10 years, the number of companies with a market cap of more than $1 Bn has risen to 515 from 175.



The NIFTY500 outperformed the S&P500 by 10% (in US$) over the past 12 months

Like last year, Bitcoin (+63%) remains the best performing asset class globally YTD, followed by crude oil (+23%). The S&P500 is up 8% this year vs. EMs which are up a mere 3%. The Top 10 S&P 500 companies are expected to grow sales by 15% YoY and post EPS growth of 32%. In contrast, the remaining 490 firms are expected to grow revenues by just 2% YoY and deliver EPS growth of -4%. While the U.S. equity market is near its highest concentration in a century, the rally in Indian stocks has been more broad-based. This year, India's benchmark index the NIFTY50 is up 3.55%, but the broader NIFTY500 is up 6.4%.

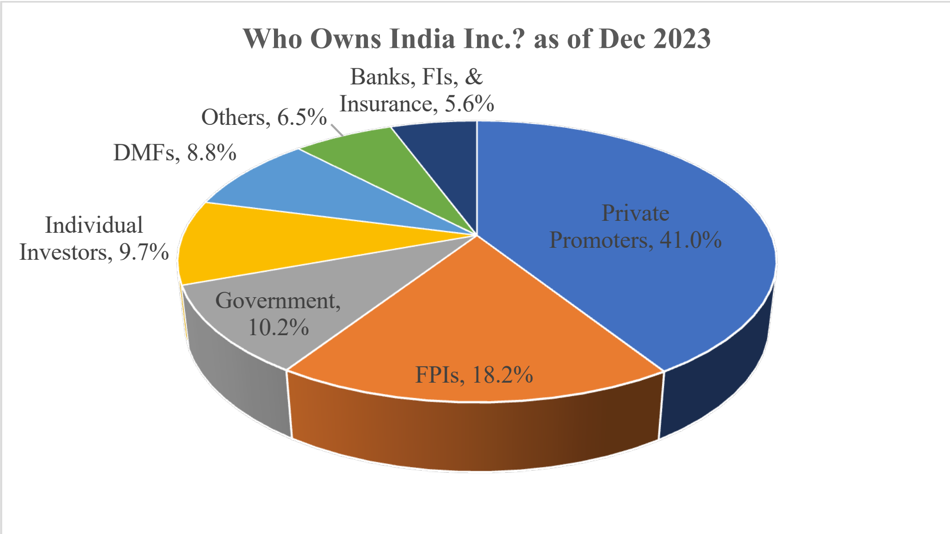
Unlike year 2023, when India took in the most foreign flows (+$21.4 Bn) in Asia (ex-Japan), YTD flows have been tepid. Korea with +$13.5 Bn, China (+$9 Bn) and Taiwan (+$4.5 Bn) have attracted far larger foreign flows than India (+$1.2 Bn). FPIs (foreign portfolio investors) do find India more expensive (at 23.4x CY24 and 20.4x CY25 P/E) than its EM/Asian peers. India's weight in MSCI EM has surpassed Taiwan and is now the second highest after China. In fact, over the past eight years, it has risen from 7% to 17.5% currently (vs. China's 26.6%). While EM funds have been investing in India for decades, global funds are underinvested. If the robust flows from domestic investors continue causing the weight to increase, foreign ETFs and passive funds will invariably have to invest more in India.

The Rise and Rise of the Indian Retail Investor
On the other hand, domestic investors seem unfazed by valuations or geo-political issues and continue to pour money into the markets, month after month. February saw Rs.26,860 crores/$3.2 Bn of net inflows into domestic mutual funds, +23% MoM. Of that, SIPs (systematic investment plans*) hit a record Rs.19,186 crores/$2.3 Bn. The NSE reported that as of Feb end the number of unique investors crossed 90 Mn, of which the last 10 Mn were added in the last five months alone.

Flush with inflows, domestic mutual funds have net invested $14.5 Bn YTD, dwarfing FPI flows of $1.2 Bn. Domestic mutual funds invested a record net Rs.45,298 crores/$5.4 Bn in March, taking the 12-month total to Rs.2.11 lakh crores/$25.4 Bn. In the last two years, MFs have net invested a staggering Rs.4 lakh crores/$48.2 Bn in the Indian equity markets.

** An SIP is a facility offered by mutual funds to investors that enables them to invest a fixed amount of money at pre-defined intervals, usually monthly*

The third pool of investors, i.e. individual investors, invested Rs.3.5 lakh crores/$46 Bn in equities directly into the markets between 2020 and 2024. As a result, retail investors now own 9.7% of India's market cap vs. 7.9% ten years ago. Interestingly while Maharashtra remained the top state in number of new investors over the last two years, Uttar Pradesh (India's largest state by population, 241 Mn people) saw its share increase from 10% in FY23 to 15% in H1FY24.



The emergence of retail investors in India as a formidable asset class has been a remarkable story. It all started with the launch of Reliance Industries (RIL)'s JIO mobile services in late 2016. JIO is an all 4G network with free domestic calls (on-net and off-net) and all you can eat data plans priced at the lowest ARPU in the world, $2.20. Add to that the advent of smartphones (now 900 Mn in use), eKYC and a young population (the average age of an investor is 29), which has spawned a whole generation of tech companies in e-commerce, fintech and online trading. Today online brokers are seeing 90% of their incremental customers coming from Tier 2, 3 and beyond towns, with more than 80% of trades placed via smartphones.

The street has been waiting for a correction, but it's been elusive given the strong domestic flows. This begs the question, what can slowdown the flows ? A potential general election upset (though at this stage it seems very unlikely), a poor monsoon and/or high oil prices for a sustained period (Brent is already at $90/bbl). The one risk to the market is the explosive growth of retail participation in the equity derivatives market. Today, futures and options account for 99% of the daily traded volumes. A vast majority of the investors are new to the capital markets from Tier 2, 3 towns and haven't ever experienced a correction. Having said that, we believe that 2024 will be yet another strong year of economic growth for India. We expect the return of private sector capex as capacity utilizations reach an average of 72-75% across industries. Other factors in India's favour include benign inflation leading to potential rate cuts by the RBI (tailing cuts by the Fed), revival of rural India, 16% corporate earnings growth and stronger tax collections as the country continues to formalize its economy.

Elections 2024

The Battle for India has begun with the Election Commission announcing the dates for the 18th Lok Sabha elections (the Lower House of the Parliament). The party or a coalition of parties that win/s a majority in the Lok Sabha (274 seats out of a total 543) gets to form the government and elect the next Prime Minister of India. Key points:

- The General Elections to the 18th Lok Sabha, held once every five years, will be the world's biggest electoral exercise.
- It will be spread over seven phases, i.e. on April 19th, April 26th, May 7th, May 13th, May 20th, May 25th and June 1st. The counting will be held on June 4.
- 969 Mn Indians are eligible to vote (vs. 168 Mn registered voters in the U.S.), more than the population of all the countries in Europe combined.

- 18 Mn people are first time voters. 198 Mn are between the ages of 20-29.
- 5.5 Mn electronic voting machines (EVMs) will be used at over a million polling stations.
- Around 2 Mn will vote through postal ballots.

The ruling BJP won the semi-finals in December with a clean sweep of the three heartland states (Rajasthan, Madhya Pradesh and Chhattisgarh). That has significantly improved the odds of Prime Minister Modi winning a third term, ringing in continuity and more economic reforms. PM Modi wants to better the win for the NDA (the BJP led National Democratic Alliance) from 352 seats in the Lok Sabha to 400. This means that the NDA will have to improve its vote share from 45% in 2019.

The main opposition is from the Congress party led coalition of 28 regional allies who call themselves the I.N.D.I.A., short for the Indian National Developmental Inclusive Alliance. This coalition has been stitched together by Congress party leader Rahul Gandhi, whose father Rajiv Gandhi (1984-89) and maternal grandmother Indira Gandhi (1966-77 & 1980-84) were former Prime Ministers.

Below are the YouTube links on the Nepean Capital page of the fireside chats held recently. You can also access them from our website: www.nepeancapital.com

Tirthankar Patnaik, Chief India Economist of the National Stock Exchange (NSE)
He discussed India's macro challenges and opportunities and the Rise of the Retail Investor
https://www.youtube.com/watch?v=Pex2IwD2R70

Shalabh Saxena, CEO of Spandana Sphoorthy (SPANDANA IN)
(India's third largest microfinance lender)
Shalabh discussed the turnaround at Spandana, the Indian Microfinance industry and Spandana 2.0
https://youtu.be/XVQS8mZ4CFo

Devansh Jain, Executive Director, INOX Wind (INXW IN)
(India's second largest wind turbine manufacturer)
Devansh discussed the turnaround of INOX Wind and the Rise of the Wind Energy Industry in India
https://youtu.be/UzZoTkn45ys

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