6 March 22

Dear Partners:

"There are decades where nothing happens; and there are weeks where decades happen"
Vladimir Ilyich Lenin

This is a brief note to share our thoughts on the consequences of Putin's war on Ukraine. We will add more depth in the quarterly note we publish in the first week of April. We caution that this is an evolving situation.

We see the following global trends emerge due to this crisis

- Higher inflation across the world due to commodity volume and price shocks[1]
- Start of a new Cold War with high probability of a Russia/China bloc which allies against the West.
- Global de risking of supply chains will gather even more pace.
    - Businesses will act on geopolitical risks with more urgency.
    - Risks that raw material supply chains will be used as economic weapons.
- Further structural boost to Clean Energy; short term spurt in Oil and Gas spending.
- Tail winds for Gold
    - Freezing of Russian Central Bank reserves should prompt more Central Banks to diversify reserves from USD/Euros
    - Rising risks of even higher inflation down the road if Central Bankers delay interest rate increased due to current geopolitical events

Implications for India – head winds to growth and inflation

- Oil prices above USD 100/barrel for prolonged periods will be a head wind to inflation and growth.
- Manufacturing out of India is a theme which should continue to benefit.
- Tail risks (low probability, high impact) of sanctions on India. Reliant on Russia for defense[2] and potash.
- Long term, India will need to step up defense spending if Russia becomes a closer ally of China which has negative implications for growth as it takes away resources from Infrastructure and social spending.

[1] Russia supplies 45% of all Palladium, 15% of the World's Gas supply, 10% of Oil. Russia and Ukraine supply 30% of Wheat exports. Ukraine supplies 40% of Neon needed in semiconductor manufacturing. Ukraine is a large supplier of Wiring Harnesses to the Auto Industry in Europe.

[2] 65% of arms purchased by India between 1950 to 2020 are from Soviet Union/Russia

Solidarity stance

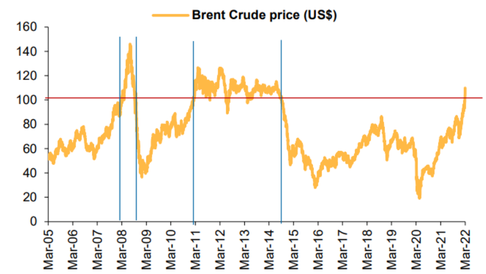
- "Cross the river by feeling the stones" – Be cautious, but don't freeze when we see opportunity.
- Recognize the new reality. We have lowered our fair valuation multiple assumptions and growth assumptions to reflect the new reality of higher inflation.
- No cash calls. As we shared before, the net impact of cash calls is <2% IRR over 5 years if you sell down 30% to buy at 30% lower prices. Emotive relief comes at the cost of long-term returns as you end up re-entering at higher prices. Need to accept draw downs with equanimity.
- Act when prices come in favour despite current uncertainty. For example, HDFC Bank, a bell weather resilient Earnings growth story is now at the lower band of its decadal historical trading range, with a lower valuation level achieved only during Covid. (Chart below is Trailing Market Cap/Net Worth). Panicked sellers can drive down pries well below fair value.

HDFC Bank

We buy well run companies that have resilience. Hence, we don't expect portfolio Earnings to be severely impacted unless inflation stays stubbornly elevated or increases sharply.

- For sure, some companies will be impacted by even higher input costs. However, most Manufacturing names we own pass on Raw Material costs with a lag with margins staying resilient despite rising commodity prices over time.
- Some companies we own will benefit from higher Oil and Gas prices eg Ratnamani Metals. Banks should benefit from higher inflation as it will result in margin expansion.
- Some companies that should be negatively impacted by higher Oil Prices eg Mayur Uniquoters, actually expanded their margins during the last period of high Oil prices. (product mix improvement, cost efficiencies, ability to pass on higher raw material prices with a lag)

Fig 10 The last time Brent crude sustained over US$100 for a prolonged period was in Mar'11-Sep'14...



Source: Bloomberg, Macquarie Research, March 2022

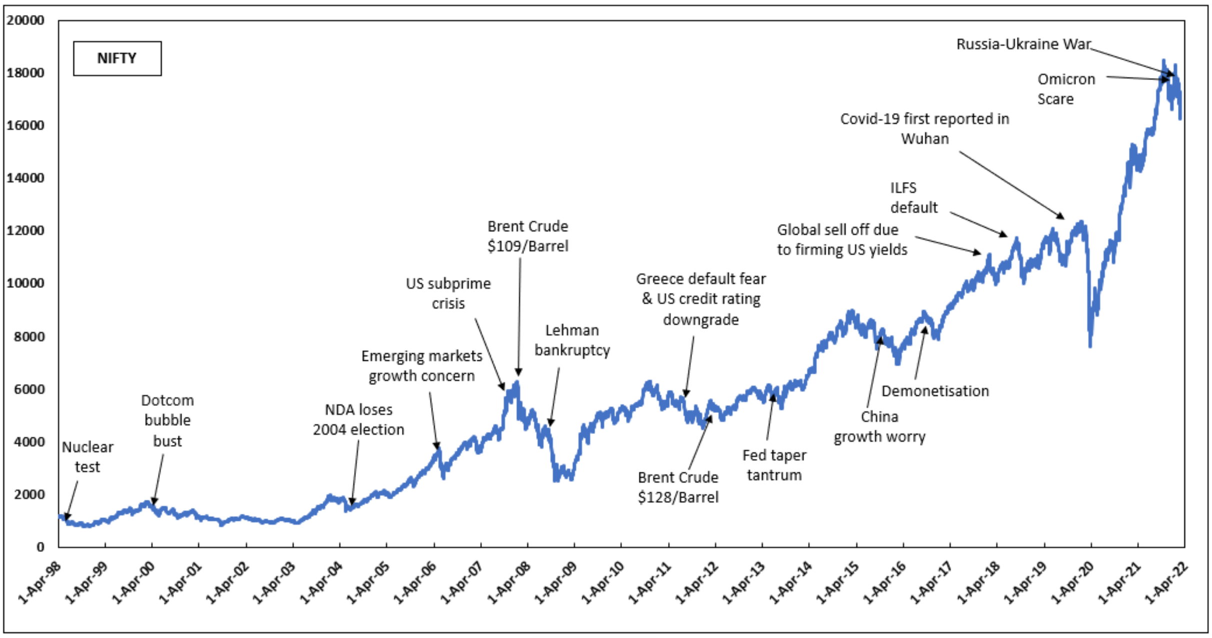
Mayur Uniquoters

Profit & Loss

Standalone Figures in Rs. Crores / View Consolidated

	Mar 2010	Mar 2011	Mar 2012	Mar 2013	Mar 2014	Mar 2015
Sales +	163	246	315	379	466	503
Expenses -	**136**	**204**	**262**	**309**	**372**	**401**
Material Cost %	73%	74%	74%	71%	68%	65%
Manufacturing Cost %	3%	3%	2%	4%	4%	6%
Employee Cost %	4%	3%	3%	3%	4%	5%
Other Cost %	3%	3%	3%	3%	3%	4%
Operating Profit	**27**	**41**	**53**	**69**	**94**	**102**
OPM %	16%	17%	17%	18%	20%	20%

THE MARKET CLIMBS WALLS OF WORRIES. DON'T INTERRUPT THE COMPOUNDING JOURNEY.



Recapping our recommendations to partners

- In the long term, stock prices are slaves to Earnings growth. This game is about control of behaviour.
- Don't ever be in a position where Equities need to be sold out of compulsion. Stretch time horizons when you consider Equity allocations.
- Realism on return expectations in Equities over what has been earned in the previous 5 years
- Plan for tail risks which fund Managers cannot protect portfolios from.
- Gold may be a better hedge at present vs short term debt, especially in light of freezing of Russia FX reserves.
- Invest in Equities via SIP – volatility is a friend of the long-term investor. There is always something that is deeply out of favour.

With our best wishes,

Manish Gupta	Manjeet Buaria	Anirudh Shetty
Chief Investment Officer	Partner	Senior Principal