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How do we decide composition of small/mid/large caps in the portfolio.

The context of this question is to gauge the level of risk we are taking. Too low? Too high?

We manage your money as we manage ours. We are not attempting to deliver the highest returns in theshort term, rather we aim to deliver consistent returns that outperform the index over the long term. Hence, our guiding framework is resilience over speed.

Small/Mid/Large composition is misleading to gauge underlying portfolio risk. As a group, Small Caps tendto be more volatile with higher drawdowns during periods of market stress. However, Small Caps do notnecessarily equate with higher risk and Large Caps with lower risk. Some small caps dominate niches, aredebt free and high ROE businesses.

We do not track the traditional Mutual Fund Small/Mid/Large categorization. Rather, the portfolio is constructed by organizing companies in 4 phases of their evolution basis the maturity (and hence implicitrisk) of their business models and liquidity relative to our AUM.

- A ~10000-15000 Cr company (small cap in traditional MF definition) could be a large allocation forus (7-8%) in our context (1700 Cr AUM). Kama Holdings, India Mart are a few examples of Small caps with large weights.
- However, a ~2000 Cr Market cap company would never be more than a 3-4% weight as liquidity would be poor relative to our AUM. We would not hold more than 20% in relatively illiquid namesin aggregate.

The criteria used for categorization of companies across 4 phases is as follows:

	Phase 1	Phase 2	Phase 3	Phase 4
Category	Special Situation	Emerging Leader	Almost Clear Leader	Clear Leader
Rationale for inclusion in portfolio	Very cheap. But not compounding stories at present	Potential to become compounders. But still need to demonstrate the ability to execute at scale.	Strong business model and moat visible.	Strong moat and clear competitive edge. Growth fly wheelis spinning
Position size per company	~3%	~3-5%	~6-8%	~8%+
Aggregate weightage in SOL portfolios at present	< 4%	~25%	~32%	~40%

We design portfolios to have a mix of smaller positions in Phase 1 and 2 companies that are "Emerging" (~25-30% of portfolio) and larger positions in Phase 3 and 4 companies which are "Clear" leaders (~70- 75% of portfolio)

- We take smaller positions in Phase 1 and 2 companies (3-5% allocations) as there are higher

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- chances of errors here and it is not easy to exit without moving the price due to poor liquidity. Achange in environment could impact these companies more as they will be over-reliant on a fewproducts/customers or people. No amount of analysis can tell us which of these promoters will evolve from “Ranji players to playing for India” and those who will not make the transition. Oftenthe head and the heart are not in sync. For example, while a promoter will accept the need to attract talent, they may not be able to let go of micromanagement and hence not attract or retaingood people. One truly understands companies and promoters only after having invested in themfor a while post which the probability of future evolution becomes clearer.
- Phase 3-4 companies have more stable business models where there is more proven track-record.One can take bigger positions here as well as average down on price declines.
- Phase 3-4 will provide stability to the portfolio with Phase 1-2 providing the return kicker as theycan both grow faster and have potential for re-rating if they evolve into more robust business models. Good examples of Phase 2 to Phase 3 evolution in the recent year have been Axis Bank,RACL Gear Tech – where strong execution resulting in enhanced market credibility and hence higher valuation multiples.
- Our bias is to let our Phase 2 winners grow into higher position sizes while exiting Phase 1 and 2 companies where we see promoters not evolving at the appropriate pace and we can allocate capital into more promising ideas

Our key holdings mapped to this framework at present are as follows:

Themes	Phase 1	Phase 2	Phase 3	Phase 4
Banks			Axis Bank	ICICI Bank HDFC Bank
Manufacturing	MAN Industries	Mayur Uniquoters Shaily Engg. Hester Bio Yasho Industries	Kama Holdings RACL Gear Tech Neogen Chemicals	Garware Technical
Life Insurance		ICICI Pru Life		SBI Life HDFC Life
Health Insurance			Star Health Insurance	
Digital and enablers			Indiamart	Bharti Airtel
Consumption		Restaurant Brands Asia		

Based on the MF industry categorization, Large Caps are ~60% of the portfolio today. As we intend to allocate more capital to non-financials over time, we expect this ratio to gradually decline. However, it would depend on where we see the best opportunities.

Please note that the above names could change, and we will not be able to inform you till the changes are complete as that would be against the aggregate interests of the partnership