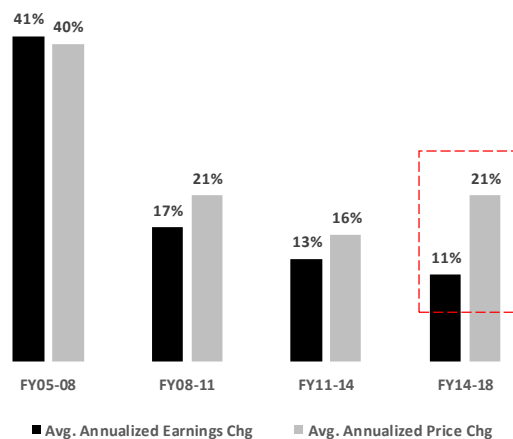


Dear Investors:

As we write this, there is a distinct feeling on the street that we are on the middle of an ‘indiscriminate selling’ and that it’s apparently overdone. As is often the case, the street was largely mum last year when the ‘buying was decidedly ‘indiscriminate and overdone’. Street (then) was consumed with potential goldilocks of margins expanding further on historically high bases, growth accelerating despite a muted jobs market, and continued depressed material costs. Predictably, the re-adjustment to reality has been hard, as it should have been. As always, despite the long-only orientation, your managers distinguish themselves during such periods and have largely avoided the drawdown in broader markets. In C3Q18, *India Under-served* was down **-4.8%** vs. **-10%**, **-4.6%**, and **-0.6%** declines in *BSE Smallcap*, *BSE Midcap*, and *BSE 500* respectively. Your strategy has further bounced back strongly in October (up about +2.5% on preliminary numbers even as broader markets continue to drawdown). C2018 YTD, the strategy is now down around **-5%** vs. **-20%** decline in *BSE Midcap* and **-27%** decline in *BSE Smallcap*. For the year, we are realistically aiming to retain nearly our entire gains from C2017.

Decade long multiple expansion cycle coming to an end. While earnings-stock disconnects have partly unraveled, it’s critical to appreciate that we have just come off of a decade long cycle of multiple expansion. Midcaps were already trading north of 20x earnings at the end of FY08 (Mar) on a solid earnings base, which certainly can’t be argued as patently cheap to begin with. Over the next decade, multiples continued to expand further with stocks sharply disconnecting from underlying earnings over FY14-FY18 (see **Exhibits 1a** and **1b**). Typically, *India Under-served* strategy’s best periods are during market drawdowns and post draw-down catch-ups. Given the large underlying earnings-valuation disconnects, we expect to deliver material alpha vs. the broader markets over the next 2-4 years.

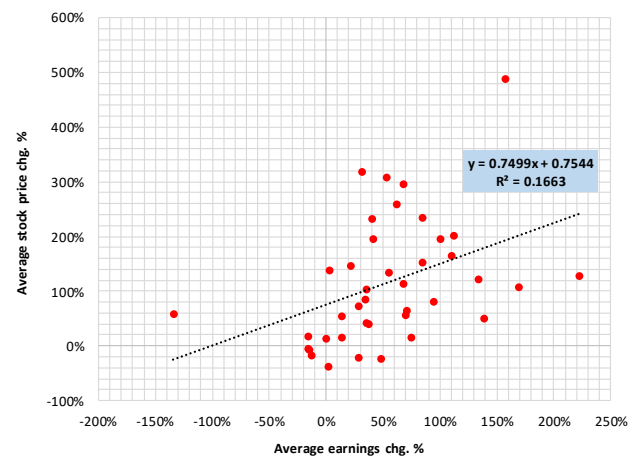
Exhibit 1a – Extended midcap multiple expansion cycle....



Source: Company Reports

Note: Above data is for current constituents of Nifty Midcap 50 (ex-financials)

Exhibit 1b - was aided by sharp disconnects over FY14-FY18



We increased our allocation to our biggest position; we see potentially lumpy but highly likely substantial value capture over next 3 years at this paper holding. Lockout announced by few contractual workers¹ in August led to a 9-day shutout at our paper holding’s flagship plant in Eastern India. We utilized declines over this period to further add on to this position.

¹ About 2/3rd of the plant’s workers are contractual.

Importantly, this paper holding of ours acquired a Telangana based paper facility off of NCLT proceedings. As things stand, we expect the acquired facility to hit full capacity within 3 years of commencement. Our holding would spend little over INR 4 Bil to restructure the operations of this facility² – this would happen over a 3-yr period, with the first phase of 6-8 months absorbing about 3/4th of the restructuring budget. The second phase (executed over 8-9 quarters) would involve raising cogeneration of power from 60% currently to 100% of requirement. Overall, these acquired ops have every shot of reaching high-teens EBITDA margin within 3 years.

We conservatively value the overall current business at INR 300/share and the acquired facility in the INR 20-25/share range. Separately, we estimate that the value of planned packaging board expansion (150K tons and pulping facility of 140K tons; likely start in C2021) at between 60-80/share. We note that over the next 3-4 years, another 300K tons of packaging board capacity would come into market. This includes ~200K tons from *Emami*³ in Gujarat (likely to begin in late F2021) and about another 100K tons from *ITC*. Incrementally (also not priced) is our estimate of another 1.5-2% margin expansion as sourcing radius reduces further over the next 2-3 years (from current 2/3rd being sourced from <200 km to ~80% sourced from <200 km).

We estimate that in the very near-term, there might be a slight drag on margins because of the lag in pass-through of material INR depreciation⁴. Given the supply environment however (industry-wide, packaging board utilization is running in the 85-90% range), they are in a comfortable position to pass through most of the impact. We note that F2019E (Mar) YTD, they have already raised board pricing by nearly 8%.

Excluding the acquired entity, we expect at-least low-teens revenue growth for F2019E (Mar), and at least high-teens/low-20s EBITDA growth. Given that annual debt-paydown of at least INR 3 Bil is a near certainty, we conservatively expect this holding (excluding the acquired entity) to report earnings growth at least in the mid-20s. We also expect the acquired ops to get earnings accretive in about 2 years.

We also increased exposure in an auto parts name. Our investment in this name has suffered previously as their LED Luminaires business got hurt as EESL tenders got bid on aggressively towards end of C2016. With cash earnings drag having coming to an end and only depreciation optically dragging headline earnings, our most conservative valuation on the name suggested no less than 70% upside in early September. We have gradually increased this exposure to ~5% of the book. While there is typically a 2 quarter lag in escalating material inflation, we note limited scale elsewhere in this part sub-category for material costs to be a sustainable headwind. With several potential catalysts on the horizon (1. LED Luminaires capacity could be utilized for retail LED sales by leveraging existing warehouses across 10 states; 2. Assuming full conversion to LEDs, lighting content per vehicle can nearly double to INR 1.4-1.5K per vehicle from just over 0.8K per vehicle currently; and 3. Increasing traction in after-market within a category that practically call their own), our conviction on this exposure has grown meaningfully in recent times.

We added a new exposure in a solid cash-engine of a serial entrepreneur. While most investors would balk at names that expand in areas other than their core businesses, occasionally deep-value opportunistic plays require that we jettison that thought process, without compromising anywhere else of course. In the last quarter, we initiated exposure in a name that was nurtured by a serial entrepreneur who took advantage of the growth of payday-loans industry in the US - The core product (used for sourcing, risk management, portfolio sales etc.) sold to the organized payday-loans originators in the US would account for ~40% of the

² The deal was closed for INR 3.7 Bil, of which 45% was in cash (INR 340 Mil paid to operational creditors and INR 1.4 Bil paid to financial creditors). Of the rest, INR 1.6 Bil was in 0.01% preferreds issued to creditors, and INR 430 Mil is in new stock, which can be repurchased within a year.

³ Emami's current board capacity, second highest in the industry, stands at 180K tons. ITC is the largest with ~500K tons. Our holding owns about 10% share of the packaging board market.

⁴ In F2018 (Mar), this business imported about a fifth of its material requirement (primarily BCTMP pulp).

business in F2019E (Mar) and would report revenue growth in the mid-teens⁵. This cash cow has funded growth in an IT services business (characterized by small projects that are executed by 5-10 people over 2-3 months) and a hospital network that would account for little over a third of the business in the current fiscal. We conservatively expect this position to more than double within 6-8 quarters as technology and hospitals businesses continue to gain traction.

Inventory cuts at a radio holding have led to listenership share gain at our radio holding. We note significant pullback in a radio holding of ours, despite extremely solid earnings traction as newer stations continue to ramp up. Our recent discussions with media agencies suggest that premium pricing can presently only be justified by allocations to the #1 station in any market. As this holding of ours has cut ad inventory over the past year, its listenership share clearly seems to be on an uptrend in top-3 markets – RAM listenership share up from 12.1% to 13.4% in Delhi YTD, from 12.9% to 13.8% in Mumbai YTD, and from 16.4% to 17.4% in Bangalore YTD. We strongly believe that within a market where pricing has largely been stagnant for nearly a decade (and well-priced into stocks), improved content and listenership may surprise our consensus expectations on this name.

Please let us know if you have any questions.

Thanks,

Piyush Sharma

⁵ Driven by storefront expansion at the largest industry originator. 3/4th of the revenue increase will fall into the EBITDA line.

Meet your investment manager

Piyush Sharma, born and raised in India, is investment manager of Right Horizons Minerva Funds. Having spent time with Citigroup and Bombay Stock Exchange in India, he moved to United States in 2002, where he covered stocks within Business Services, Autos, Consumer Products and Financials with Sanford Bernstein, Longbow Research, and Avondale Partners, working in teams that received accolades from leading institutional research arbiters, including Institutional Investor (II) and Greenwich Associates. Piyush received an MBA from University of North Carolina at Chapel Hill, MS from MNNIT, and BS in Accounting from University of Allahabad.

OFFERING DESCRIPTION: Right Horizons Minerva Funds are the PMS investment offerings of Right Horizons Financial Services Pvt Ltd, a SEBI-registered portfolio manager. Any reference to “Minerva” in this document refers to the proposed investment offering managed by a registered portfolio manager. All fees mentioned in this introduction are indicative and subject to change. Final terms and their computation will be clearly detailed in the portfolio manager-client agreement.

DISCLAIMER: The information, opinions, estimates and projections contained in this fund brief were prepared by managers of Right Horizons Minerva Funds and constitute its current judgment as of the date of this note. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Right Horizons makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Right Horizons does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this fund brief or any changes in its opinion, estimates or projections. Prices and availability of securities are also subject to change without notice. This is not a prospectus and does not constitute investment advice or an offer or solicitation to buy or sell any designated investments discussed herein. Neither Right Horizons, nor its officers, directors, agents, employees, Minerva Funds’ managers makes any warranty, express or implied, as to the suitability of any fund as an investment or of any kind whatsoever, or assumes any responsibility for, and none of these parties shall be liable for, any losses, damages, costs, or expenses, of any kind or description, arising out of this brief or your investment in any fund. You understand that you are solely responsible for reviewing any fund, its offering and any statements made by a fund or its manager and for performing such due diligence as you may deem appropriate, including consulting your own legal and tax advisers.

CONTACT US:

Piyush Sharma piyush.sharma@righthorizons.com
Ashish Kodnani ashish.kodnani@fundzstreet.com

Right Horizons Financial Services Pvt Ltd.

No 6, Arekere, II Main,
Bannerghatta Road,
Bangalore – 560076
Tel: +91-80-65687503 to 65687518 [Bangalore]
Tel: +91-124-4696636 [Gurgaon]
Tel: +91-9833855875 [Mumbai]
Tel: +1-919-360-0359 [United States]

