2POINT2
CAPITAL

2Point2 Capital Investor Update Q3 FY17

Dear Investors,

This is the second quarterly letter to our Investors. Our letters to you will inform you of our activities, provide an update on our performance and present our views on issues we feel worth discussing. We reiterate our investment strategy below for first time readers.

INVESTMENT STRATEGIES

2Point2 Long Term Value Fund

The 2Point2 Long Term Value Fund (launched in end July 2016) is our only strategy under the PMS license granted to us by SEBI. This strategy focuses on generating long term returns by holding a concentrated portfolio of investments (~15 stocks). The typical company stock in this strategy will have the following characteristics -

- Strong competitive advantage
- High standards of corporate governance
- Available at a reasonable price

The NIFTY 50 and NIFTY Midcap 100 indices will be the benchmarks for the 2Point2 Long Term Value Fund. The performance track record is calculated by Orbis (PMS Custodian), audited half yearly and subjected to SEBI's review.

2Point2 Long Short Value Fund

The 2Point2 Long Short Value Fund (launched in August 2016) is our long/short equity strategy using **only** proprietary capital. The "long" part of this strategy is similar to our 2Point2 Long Term Value Fund portfolio. In addition to the long portfolio, this strategy also uses futures to "short" stocks on which we have a fundamental negative view. The typical stock in our short portfolio will have at least a few of the following characteristics –

- Structurally challenged/broken business models
- Frauds/Serious governance issues
- High valuations not justified by business fundamentals

The 2Point2 Long Short Value Fund is an absolute return strategy and does not have a benchmark.

PERFORMANCE

2Point2 Long Term Value Fund

	YTD Returns*	Outperformance
2Point2 Long Term Value Fund	1.59%	
Benchmark - NIFTY 50	-6.68%	+8.27%
Benchmark - MIDCAP 100	-4.94%	+6.53%

**Beginning 20th July 2016 till 31st December 2016. As mandated by SEBI, YTD Returns are calculated on a weighted average basis. YTD Returns are net of expenses and management fees but excluding performance fees and are on a pre-tax basis.*

As of 31st December, only 74.54% of the total capital was deployed in equities with the rest lying in interest earning assets and hedge positions. **Note:** YTD Returns of individual clients will differ from the above numbers based on the timing of their investments. The above returns are on the consolidated pool of capital.

2Point2 Long Short Value Fund

	YTD Returns*
2Point2 Long Short Value Fund	13.59%

**Beginning 4th August 2016 till 31st December 2016. YTD Returns are calculated on a weighted average basis on only the invested corpus (gross long + gross short). YTD Returns are net of all expenses and are on a pre-tax basis.*

COMMENTARY

We live in an uncertain world. In 2016, the Indian equity markets were shaken by several events that few had predicted beforehand – fear of China slowdown, no fear of China slowdown, Brexit, cross-border surgical strikes, demonetization, Trump win, etc. It is still unclear what long-term impact these events will have on India and the world. However, we are quite certain that 2017 will also have many such events that will impact the markets (positively or negatively).

In our view, such events do not materially impact the returns for long-term equity investors. The above chart represents the BSE Sensex over a 25-year period during which the index returned 11% CAGR (not including dividends). This period included major events which were expected to have a large impact on Indian equity markets such as (1) Indo-Pak Kargil war (2) Post-Pokhran economic sanctions (3) Harshad Mehta & Ketan Parekh scams (4) 2008 global financial crisis (5) Oil at 140 $ per barrel (6) Hung parliament/minority government (7) 10%+ inflation (8) rapidly depreciating rupee (9) 2G/Coal/Commonwealth scams. But today, most people will struggle to place the above events on the Sensex chart (except the 2008 global financial crisis). It is clear that the Indian equity markets have delivered reasonable returns over the long-term despite facing several periods of economic/political/military crisis.

This does not mean that nothing can impact the long-term returns of the Indian equity markets. However, we need to be cognizant of our (and the markets) tendency to exaggerate the long-term impact (positive or negative) of ~~major~~ minor events.

The fact that the world is uncertain also does not change the way we invest. Macro-forecasting does not form a large part of our investment process and is not particularly our area of competence (though it makes for some fun and lively conversations). Our investment process is primarily bottom-up driven with a large amount of on-ground diligence and with a margin of safety in valuations. We will continue to follow this process irrespective of whether the markets are gloomy or exuberant. We will use the market's exaggerated reactions as opportunities to buy or sell stocks.

Although our outperformance against the benchmark indices is large, it is premature to compare performance in this short period of two quarters. The outperformance against the benchmark indices was achieved by a combination of a) High cash position during periods of exuberance in valuations, b) Equity portfolio delivering positive returns against the negative returns delivered by the benchmark indices. In our last letter, we mentioned that the sharp run-up in the equity markets recently had significantly reduced the investment universe of good businesses available at a reasonable valuation, especially in the small and mid-cap space. In Q3 FY16, the Nifty 50 and Nifty Midcap 100 index fell by 4.9% and 6.9% respectively. The fall provided us an opportunity to invest in some quality businesses at attractive valuations, increasing our equity allocation to ~75% from the ~50% earlier. The rest of the portfolio is still invested in liquid funds (generating a modest return), and in futures (for hedging purpose).

We continue to value stocks on an absolute valuation basis, rather than a relative valuation metric. This has resulted in most of our portfolio remaining largely immune to the recent crash. However, the NBFC/bank stocks in our portfolio were affected by the impact on disbursement/collections due to the government's demonetization measure. We remain positive on the long-term prospects of these companies as we believe that the impact of demonetisation on these businesses is temporary and not structural.

We repeat that as investment managers, our primary goal is to protect capital followed by our goal to generate returns that exceed the benchmark index return over the long term. We will strive to achieve both these goals.

If you have any queries (about your portfolio, 2Point2 Capital or investing in general), do reach out to us at the below coordinates. We would love to talk.

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Thanks and Regards,
Savi Jain & Amit Mantri