TANTALLON CAPITAL

November 2017

TANTALLON INDIA FUND

The Tantallon India Fund is a fundamental, long-biased, India-focused, total return opportunity fund, registered in the Cayman Islands and Mauritius. The Fund invests with a 3-5 year horizon, in a concentrated portfolio (25-30 unlevered positions), market cap/sector/capital structure agnostic, but with strong conviction on the structural opportunity, scalable business models, and in management's ability to execute.

Tantallon Capital Advisors, the advisory company, is a Singapore-based entity, set up in 2003, holding a Capital Markets Service License in Fund Management from the Monetary Authority of Singapore.

The Tantallon India Fund closed +6.79% in November, after expenses. The Moody's upgrade, a surprisingly resilient +6.1% GDP post for the September quarter (suggesting the start of 'normalization' post demonetization and GST implementation), and a broadly positive outlook on revenues and margins/earnings for the companies in our portfolio following the release of the September quarter earnings, all contributed to the tailwinds driving portfolio results.

The sell-off over the last few days on the uncertainty over the outcome of the Gujarat state elections in the middle of December, is a tad surprising. However, we would continue to urge investors to **prepare for those moments of market uncertainty, and to systematically increase exposure to Indian equities.**

- ***Modi has delivered on substantial economic and policy reforms.*** *He is not done.* As we look ahead to the next General Elections in 2019, we should expect meaningful new policy initiatives driving rural uplift, industrialization, infrastructure development, job creation, and the digitalization of the real economy.
- Looking out into 2018/2019, and having re-tested our macro/micro assumptions, ***we retain strong conviction in our portfolio companies, and their ability to deliver on high quality revenue growth, margin accretion, and sustainable earnings.***
- ***Sustained flows into domestic equity mutual funds will be supportive of multiples/potential multiple expansion*** for companies that can deliver on sustained earnings and cash flow growth.

In mid-November, Moody's upgraded India's local and foreign currency issuer ratings to Baa2 from Baa3, and India's short-term local currency rating to P-2 from P-3.

- ***The upgrade is an acknowledgment of the significant positive changes that have taken place post the 2013 'taper-tantrum,'*** and in particular, of RBI Governor Rajan's foresight in ensuring Central Bank independence, and establishing an explicit inflation-targeting discipline in setting monetary policy, and of Modi having delivered on the promise of policy reforms since taking office in May 2014.
- ***The upgrade is reflective of a stable macro framework that is now in place:*** structurally low(er) inflation, high real interest rates, large FX reserves, strong political commitment to fiscal discipline, a stable rupee, and a positive growth outlook.
- ***The upgrade and the Modi government continuing to signal its commitment to fiscal prudence*** will have extremely positive implications for sentiment in the domestic bond markets, on domestic borrowing costs, and for flows (long-term investments into infrastructure, as well as into debt and equity capital markets).
    - *We believe the Moody's upgrade will allow the Reserve Bank of India to remain on an "extended hold," explicitly supportive of growth, and of investments.*
    - *Additionally, macro stability and the case for sustained capital flows does suggest that our current expectations of the rupee trading closer to Rs.67/US$ over the next 12 months (given the risks of higher energy prices), might be just a tad too cautious.*

Gujarat has gone through an unprecedented period of stability and economic prosperity under Modi and the BJP. It has been therefore been quite interesting to reflect on the recent uncertainty in the build-up to the Gujarat State Elections in the middle of December.

- No question, given the disproportionate share of the economy in the hands of small traders and businessmen, Gujarat was among the worst impacted economically over the last 12 months by demonetization and the implementation fo GST.
- It is also reflective of the Congress Party and Rahul Gandhi's concerted efforts to re-build image/credibility, and to take

Performance, in USD

(*Inception on September 1, 2015*)

	Tantallon India Fund	MSCI India($)	Over/Under Full Performance
November 2017:	+6.79%	-0.78%	+7.57%
2017 YTD:	+52.71%	+30.61%	+22.10%
2016:	-5.79%	-2.90%	-2.89%
2015:	+0.24%	-7.53%	+7.77%
Inception:	+44.21%	+25.88%	+18.33%

Compound Returns	+17.67%	Volatility	+20.54%
3 month US T-bill	+1.26%	Sharpe Ratio	0.80

FUND DETAILS

The Tantallon India Fund

AUM USD 36,000,000

Investment Advisor: Tantallon Capital	**Minimum Investment:** USD 5,000,000
Administrator: Trident Trust Company (Mauritius) Ltd	**Fees:** 1.5%pa Management fees 12.5% on annual returns in excess of 7.5% US$ hurdle rate compounding annually
Domicile: Mauritius	**Dealing:** Monthly
Feeder funds US Feeder and Non-US Feeder (Cayman Islands)	**Lawyers:** Maples & Calder; Shearman & Sterling LLP; Rajah & Tann Singapore LLP
Auditor: KPMG	**Contact:** Alex Hill (alex@tantalloncapital.com)

YEAR	RETURNS	JAN	FEB	MAR	APR	MAY	JUN	JULY	AUG	SEP	OCT	NOV	DEC
Inception	+44.21%												
2017	+52.71%	+8.34%	+8.73%	+6.73%	+6.54%	-1.20%	+0.23%	+4.30%	-1.47%	-0.69%	+5.64%	+6.79%	
2016	-5.79%	-8.33%	-9.98%	+11.86%	+2.10%	+1.89%	+5.44%	+6.40%	+1.66%	-0.74%	-1.69%	-9.26%	-2.83%
2015	+0.24%									-0.14%	+1.36%	-2.09%	+1.14%

advantage of the recent dis-satisfaction with the Modi government, and the perceived weakness in a BJP/Modi stronghold.

Bottom-line, given the market's insistence on treating the Gujarat election as yet another referendum on Modi's reformist agenda, and his ability to continue to drive through transformative policy initiatives, we should expect short-term sentiment on the markets to be driven by the outcome of the Gujarat elections.

- *We actually expect the BJP to retain a legislative majority (albeit, a smaller majority than in the past) in Gujarat.*
- *Additionally, we do expect that Modi, irrespective of the election outcome, will remain steadfast in pushing through reforms to encourage investments in infrastructure and manufacturing, job creation, and the digitization of the real economy to eliminate wastage, and to minimize corruption.*

The stock we would like to highlight this month is ***Kolte-Patil Developers Ltd,*** a well-established, professionally-run, Pune-based property developer with an enviable, decades old reputation for on-time/on-budget delivery of high quality real estate projects.

- Kolte-Patil has a 10% market share in Pune with a quarterly run-rate of 600,000 square feet of residential property sales. Pune currently accounts for 90% of the company's revenues, and will likely continue to account for 80%+ of revenues over the next 3 years.
- In addition, opportunistically, taking advantage of cash strapped competitors, the company has committed to 2 projects in Bangalore, and 10 re-development projects in Mumbai.

Kolte-Patil is a prime beneficiary of the new Real Estate Regulatory Act (RERA), which enforces extremely strict new project approval requirements, explicit restrictions on the marketing/sale of new property projects in order to protect consumers, and strict guidelines on revenue/cash flow recognition on customer deposits in escrow accounts. Importantly too, RERA imposes extremely harsh penalties (including jail terms) for developers who fail to meet their contractual commitments on project specs and delivery time-tables.

- RERA has effectively eliminated the highly disruptive unorganized sector, as well as balance sheet constrained developers who lack the capital to invest upfront in land acquisition and infrastructure development.
- The shrinking supply, and the limited pipeline of new product launches, has allowed excess inventory to be absorbed over the last three years, while stabilizing/improving pricing on new product launches.

We expect consolidated revenues to conservatively compound at 25% annually over the next three years to Rs.25bn (versus market expectations anchored to a much more sedate 8.5% CAGR in revenues).

- Kolte-Patil currently has land title and project approvals in hand, to deliver a minimum of 50m square feet of residential projects over the next three years.
  - *The government's "Housing for All" policy initiatives, and the focus on affordable housing, has catalyzed demand for new projects that is likely to substantially surprise us on the upside.*
- In addition, the market does not seem to be giving the company much credit for the 10 re-development projects in Mumbai, which we expect ought to deliver on another 3.5m square feet of finished product at an average price of Rs.20,000/square foot.
- At this point, given the much slower ramp-up in Bangalore, we are assigning zero revenue recognition from the two Bangalore projects over the next three years. Perhaps, we are being too conservative.

We expect consolidated profits to compound at a 35%+ run-rate over the next three years, versus the market's expectations of earning growth of about 15% annually.

- We anticipate significantly higher price realizations in Pune (relative to the average of the last three years), averaging Rs.4,000/square foot.
- We expect much higher margin realization in the Mumbai projects to drive 400bp of consolidated EBITDA margin improvement over the next three years.
- The company is currently free cash flow positive, and given the cash flow profile that we have modeled from the existing projects in Pune, we expect net gearing (and therefore interest costs) to decline substantially from the current level of 0.5x.

To conclude:

- *Yes, the markets have done well, recovering from last November's shock demonetization event.* However, **we believe that current valuations do not reflect the potential upside from a multi-year growth cycle** on the back of urbanization, consolidation, financial intermediation, digitization of the real economy, enhanced agricultural productivity, and growth in rural incomes and discretionary spending.
- We have strong **conviction in our portfolio delivering on earnings and cash flows compounding at 15%+ annually over the next three years.**
- **We believe that Modi's commitment to further structural reforms and fiscal discipline, will continue to attract fresh investments, anchoring a strong growth outlook, and a positive re-set in market expectations/multiples.**

On a final note: from our families, to yours, Happy Holidays! We wish you Much, Joy, Good Health, Peace, and a Prosperous New Year!

Please do let us know if you would like a follow-up conversation, or a catch-up in the next few days.

Portfolio Overview

Top 5 Positions	Sectoral Break-down:	As % NAV	Sector Performance	MTD Performance
Apex Frozen Foods Ltd	Financials:	29%	Financials:	+0.50%
Titan Co Ltd	Consumer Discretionary:	19%	Consumer Discretionary:	+1.09%
Vakrangee Ltd	Consumer Staples:	11%	Consumer Staples:	+2.78%
Natco Pharma Ltd	Materials:	10%	Materials:	-0.19%
Bajaj Finance Ltd	Health Care:	10%	Health Care:	+0%
	Industrials:	7%	Industrials:	+0.09%
	Retail:	5%	Retail:	+1.07%
	Real Estate:	4%	Real Estate:	+1.37%
	Energy:	3%	Energy:	+0.01%
	Utilities:	2%	Utilities:	+0.07%