October 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.

Performance, in USD

(*Inception on September 1, 2015*)

	Tantallon India Fund	MSCI India($)	Over/Under Full Performance
October 2017:	+5.64%	+7.24%	-1.60%
2017 YTD:	+43.00%	+31.63%	+11.37%
2016:	-5.79%	-2.90%	-2.89%
2015:	+0.24%	-7.53%	+7.77%
Inception:	+35.04%	+26.86%	+8.18%

Compound Returns	+14.87%	Volatility	+20.55%
3 month US T-bill	+1.13%	Sharpe Ratio	0.669

FUND DETAILS

The Tantallon India Fund

AUM USD 34,000,000

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)

The Tantallon India Fund closed +5.64% in October, after expenses. The market has been supported by continued flows into domestic mutual funds, and the fact that *the current earnings season has been a positive surprise for the market, especially in the small and mid-cap space where we are seeing clear evidence of recovering revenue momentum, and margin resilience.*

Having just returned from spending several days visiting companies in Mumbai, Delhi, Pune, Bangalore, and Hyderabad, we would like to re-iterate our conviction in looking to take advantage of periodic bouts of market uncertainty to intentionally increase exposure to Indian equities.

- ***We are enthused by the underlying quality in revenue growth, margin improvement, and earnings visibility*** as we look out into 2018/2019.
- Modi has shifted into election mode; with the next General Elections scheduled for May 2019, ***we expect Modi to meaningfully deliver on policy initiatives*** encouraging infrastructure development, rural uplift, industrialization, job creation, and the ongoing digitalization of the real economy.
- ***We expect that the continued flows into domestic equity mutual funds will sustain,*** and potentially, make the case for a re-rating of the high-quality companies that can deliver on sustained earnings and cash flow growth.

Among the positive take-away's from the trip, we would highlight the following:

- Despite the market's concerns on aggressive fiscal pump-priming, ***our expectation is for Modi to remain steadfast in looking to contain inflation in the 4% +/- range, and to remains fiscally prudent.***
- Having ***delivered on a slew of structural reforms, and having absorbed the short-term drag on growth*** (reducing government subsidies, enforcing recognition of non-performing loans, re-capitalizing the government banks, Aadhaar implementation, demonetization, GST implementation, and enforcing transparent/on-line government tendering of telecom and DTH spectrum, mining leases, and infrastructure projects), ***Modi is now unambiguously in election mode.***
    - We expect a pick-up in **government infrastructure spending,** with a specific focus on rural and rail infrastructure, affordable housing, and irrigation.
    - We expect significant focus on **rural uplift** (in terms of both job creation and rising real incomes).
    - In addition, we expect **industrialization and the ramp-up in the digital economy to under-pin growth and job-creation** over the next 3-5 years.
- Half way into the current fiscal year (ending March 2018), ***credit growth is reviving, reflecting the start of the normalization of business activity post demonetization and the implementation of GST,*** with credit growth accelerating from +6% in FY2017, to +7.5% in 1H 2017.
- ***The bottom-of-the-pyramid is now bankable.*** Digital platforms and increasingly sophisticated and timely data analytics allows for the "democratization of credit," and deliberate and relatively low-cost customer outreach/acquisition/servicing.
- ***Renewable/clean energy remains a clear policy thrust:*** a stated intent to increase LPG penetration in the country to 100% by 2020, the goal of electrifying 60,000 km of rail lines (where the pay-back period has dropped to under two years), and explicit measures to continue to increase wind/solar in the country's overall energy mix.
- **The 'financialization' of savings post demonetizations is a durable thematic.**
    - Inflation expectations have been reined-in (one-year fixed deposit rates have fallen to under 6%), and

YEAR	RETURNS	JAN	FEB	MAR	APR	MAY	JUN	JULY	AUG	SEP	OCT	NOV	DEC
Inception	+35.04%												
2017	+43.00%	+8.34%	+8.73%	+6.73%	+6.54%	-1.20%	+0.23%	+4.30%	-1.47%	-0.69%	+5.64%		
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%

specific measures clamping down on illicit purchases of bullion and on nominee holdings in real estate, has encouraged sustained flows into fixed income and equity mutual funds.

- **There is significant focus on 'modernizing' the armed forces,** upgrading both the navy's blue-water, and the air force's first strike capabilities, as well as remote-delivery weapons systems. *It certainly does reflect the geo-political realities and the obvious tension points with China, as well as much closer ties with the US military complex.*

Reflecting on some of the negative take-away's from the trip:

- ***GST implementation has not been smooth, and in particular, as it pertains to the stress on short-term working capital requirements for the small and medium scale enterprises (SMEs).*** Given the greater availability of SME credit facilities, our expectations are for industrial activity to normalize over the next 3-4 months.
- ***The IT services sector remains under significant stress.*** Reflecting the political compulsions to re-locate jobs back to the US and Europe, IT services firms are being forced to cut back on local hiring and compensation packages in order to manage the P&L.
- ***Our expectations are for the rupee to be closer to Rs.67/US$ over the next 12 months.*** With reserves in excess of US$400bn, the RBI would prefer an orderly depreciation of the rupee, in-line with inflation differentials, encouraging greater export competitiveness.
- ***Higher crude prices will hurt. Is $65/barrel the "new normal?"*** The simple math is that a $10/barrel increase in crude prices will increase the current account deficit by 0.3% of GDP, the fiscal deficit potentially by 0.08% of GDP, and underlying inflation by about 45bp.

The stock we would like to highlight this month is **Max India Limited,** an entrepreneur-driven healthcare company, uniquely focused on the intersection of opportunities between branded multi-specialty hospitals in northern India, healthcare insurance, and assisted senior living facilities. Max India is a genuinely structural opportunity, and we would anticipate a substantial re-rating of the stock as the market starts to calibrate the company's growth footprint, the ability to cross-sell, leveraging brand and customer database, and importantly, significantly improved profitability as utilization rates increase, and operating leverage kicks-in.

We expect consolidated revenues to conservatively compound at 18%+ annually over the next 3 years to Rs.38bn, the with market projecting a more anemic 10% CAGR in revenues. *Quite frankly, we would not be surprised to see revenues grow significantly ahead of our current estimates on the back of new facilities/business-lines ramping-up faster than we are currently modeling.*

- Max Hospitals will add 1,000+ operating beds over the next 5 years (to get to close to 3,500 beds in total). *Management's goal is to deliver on Rs. 45bn in revenues from the hospital chain alone, by March 2022.*
- The recent strategic tie-ups with Bank of Baroda and South India Bank will significantly enhance Max Bupa's pan-India distribution capability.
- The Cancer Day Care Outpatient centers have broken even, and we would expect to see 5-7 new oncology centers being set-up across the NCR region in key catchment areas over the next three years.

We expect profits to compound at a 30%+ run rate over the next three years, while the market's expectations are anchored around a more muted 12%-15% growth-rate.

- We expect to see a minimum of 150bp of margin improvement at the EBITDA level over the next three years given mix improvement, higher utilization rates, and strong operating leverage.
- Enhanced distribution, strong branding, and product innovation at Max Bupa has translated to sustained volume growth, and higher premium pricing, and we do expect to see the health insurance business break-even in the next 24 months.
- We expect the market to continue to be surprised by the intentionality and significance of management's cost saving initiatives (Rs.400m in the current fiscal year alone) – operating efficiencies, lower energy consumption, purchasing leverage with suppliers of drugs, medical devices, and medical supplies, and savings realized on minimizing waste and pilferage.

To conclude:

- ➢ We continue to re-validate our conviction in our portfolio holdings, and have **good visibility on our portfolio delivering on earnings and cash flows compounding at 15%+ annually over the next three years.**
- ➢ **We believe that the markets have yet to price-in a multi-year growth cycle,** under-pinned by durable thematics of urbanization, consolidation, financial intermediation, digitization of the real economy, enhanced agricultural productivity, and growth in rural incomes and discretionary spending.
- ➢ **We believe that Modi in election mode, will catalyze both a cyclical recovery in the economy, as well as a re-set in market expectations/multiples.**

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
Natco Pharma Ltd	Consumer Discretionary:	19%	Consumer Discretionary:	+1.13%
Bajaj Finance Ltd	Consumer Staples:	10%	Consumer Staples:	+1.31%
Eicher Motors Ltd	Energy:	3%	Energy:	-0.02%
Kotak Mahindra Bank Ltd	Financials:	28%	Financials:	+0.11%
Shree Cement Ltd	Health Care:	11%	Health Care:	+1.22%
	Industrials:	8%	Industrials:	+0.65%
	Materials:	11%	Materials:	+0.33%
	Retail:	4%	Retail:	+0.53%
	Utilities:	2%	Utilities:	+0.01%
	Real Estate:	4%	Real Estate:	+0.37%