

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 down -2.30% in August, after expenses. The rupee weakness is the primary culprit (the rupee, -10% y-t-d versus the US\$, is now Asia's worst performing currency this year), caught up in contagion risk across Emerging Markets broadly, framed against the backdrop of US\$ strength, and market concerns over higher energy prices being manifest in rising inflationary expectations, and Central Banks globally being forced to raise rates as the Fed continues down its path of "normalization."

Somehow, lost in the general market malaise and the currency taking it on the chin, is the fact that India's real economy grew 8.2% in the April-June quarter, the best quarter posted in the last nine, well ahead of consensus expectations of around 7.6% growth!

Our conviction stands that growth in India is structurally accelerating.

- Despite the market's skepticism (given the upcoming election cycle), **India's policy environment has remained growth-supportive without forsaking inherent fiscal discipline.**
- Importantly, corporate confidence is at a decade-high, and corporate profitability (which, relative to GDP, is at an all-time low) has inflected positively; as corporate profitability mean-reverts from a decade of sub-trend growth, **our conviction remains that the profit up-cycle ahead of us will surprise meaningfully on the upside.**
- **India's yield curve is steepening – the yield curve has historically correlated positively with stocks.** Domestic equity/bond correlations are breaking out of their post 2010 trendlines (when India's earnings recession commenced), to the upside, affirming conviction in the growth/earnings uplift.
- **Domestic equity flows are in the midst of a structural uptrend:** despite continued foreign institutional selling (in equities and bonds, with foreign institutional holdings in the markets now testing 2011-lows), there is a consistent bid for domestic stocks from domestic funds, focused for now on the large cap universe, but increasingly starting to nibble in the smaller and medium sized companies.

The key risks that we continue to monitor:

- **Contagion risk** (be it from interest rate and risk-dislocations as the Fed steadfastly raises interest rates, or from the growing uncertainties in China, or from significant global supply-chain disruptions triggered by retaliatory tariffs, or from messy Brexit-type alternatives, or from fraught geo-politics) is real; in the short-term we should expect that any potential 'panic' will reverberate, as flows will set a negative tone/direction for the markets.

Performance, in USD

(Inception on September 1, 2015)

	Tantallon India Fund	MSCI India(\$)	Over/Under Full Performance
August 2018:	-2.30%	+0.66%	-2.96%
2018 YTD:	-17.52%	-1.77%	-15.75%
2017:	+59.14%	+36.84%	+22.30%
2016:	-5.79%	-2.90%	-2.89%
2015:	+0.24%	-7.53%	+7.77%
Inception:	+23.95%	+29.56%	-5.61%
Compound Returns	+7.42%	Volatility	+19.31%
3 month US T-bill	+2.08%	Sharpe Ratio	0.277

FUND DETAILS

The Tantallon India Fund

AUM USD 35,000,000

Investment Advisor:
Tantallon Capital

Minimum Investment:
USD 1,000,000

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)

- Given the significant slippage in the rupee versus the US\$, and rising inflationary expectations (thanks to the spike in energy prices), **the Reserve Bank of India might be forced to raise rates sharply.**
 - *Having front-loaded two rounds of rate hikes in June and in August, the RBI has reiterated its inflation targeting credentials – and is fully cognizant of the balancing act between containing rising inflationary expectations (from higher energy prices), and remaining growth-supportive.*
- The **uncertainties of the upcoming General Elections** (which need to be held by May 2019), both in terms of potentially populist policy actions in the near term, as well as whether or not Modi will retain a Parliamentary majority.
 - *We are more sanguine than most on Modi's commitment to fiscal discipline, staying on-point with his pro-reform, anti-corruption agenda, AND his retaining a Parliamentary majority.*
- **Domestic equity valuations** (on consensus estimates) would seem to be at the top of their historical trading range relative to bonds.

YEAR	RETURNS	JAN	FEB	MAR	APR	MAY	JUN	JULY	AUG	SEP	OCT	NOV	DEC
Inception	+23.95%												
2018	-17.52%	-1.87%	-7.58%	-1.07%	+3.20%	-4.66%	-5.58%	+1.29%	-2.30%				
2017	+59.14%	+8.34%	+8.73%	+6.73%	+6.54%	-1.20%	+0.23%	+4.30%	-1.47%	-0.69%	+5.64%	+6.79%	+4.21%
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%

- *We would make the point that we are substantially more constructive than consensus estimates on profit up-cycle ahead of us, on sustained top-line growth, margin uplift, and very strong earnings/cash flow growth.*

The stock we want to highlight this month is **Bajaj Auto**, India's largest manufacturer and exporter of two-wheelers and three-wheelers, with well-branded and differentiated product offerings in the entry-level, economy, and premium segments. The three wheeler business (in which Bajaj enjoys an 85%+ domestic market share) is the cash cow, allowing for industry-leading margins and profitability. Further, the global partnerships with KTM (which is today, a 48%-owned associate company of Bajaj Auto), Kawasaki, Triumph, and Husqvarna, round-out the portfolio, providing access to technology, marketing muscle, and scale, enabling Bajaj to start to compete in the 350cc+ premium and sports bike segments.

We expect revenues to compound 12%+ CAGR over the next three years, ahead of consensus expectations looking for sub-10% growth.

- Bajaj's explicit commitment to grow domestic volumes and market share across all three segments is likely to surprise the market positively given management's historic focus on protecting margins at all cost.
 - *We are particularly enthused by the feedback from the dealership networks on the launch of a slate of new models from KTM, Triumph, and Husqvarna, nicely complementing the existing entry-level and economy models, and the re-positioning of the Pulsar as a key volume driver in the executive premium segment.*
- The export franchise (currently tracking at 40% of consolidated revenues) is poised for significant volume growth in Africa, Latin America and Asia (and in particular, in the ASEAN give the recent opening of the Malaysian plant allowing for exports across the ASEAN without tariffs).
 - *We would make the point that unlike the competing Chinese exports, Bajaj's export offerings are not low-priced warriors – a decade of consistent investments in product, dealership and distribution networks, and the brand, has translated to a brand associated with reliability, safety, high quality service, and importantly, high residual values in the second-hand markets.*

We expect earnings to compound at 18%+ annually over the next three years, well ahead of consensus looking for earnings growth in the sub-10% range.

- The growth and the profitability in the three wheeler segment (EBITDA margins of 28% versus blended EBITDA margins of 18%), will largely insulate the margin pressure in the short-term from the explicit focus on growing volumes and market share in the domestic markets.
- The product launches from KTM, Triumph, and Husqvarna will drive a structural uplift in margins on the back of mix improvement and significant scale benefits.
- The depreciation of the rupee will be a significant driver of export profitability.

To conclude, in the face of significant market uncertainty, and the portfolio down-draft over the last several months, we would urge investors to look to structurally increase their allocation to Indian equities.

- **Largely insulated from the risk of tariff wars, India's domestic economy is structurally accelerating relative to the rest of the world.** *Underpinned by Modi's structural reforms, a nascent CapEx cycle, and a strong rural uplift, India will deliver on GDP growth compounding at a 7%+ run-rate over the next three years.*
- *Corporate confidence in India is at a multi-year high* given the growth-supportive policy framework and risk capital being allocated to industrial capacity and infrastructure development, as industry utilization rates trend off decade lows, and revenue growth and profitability inflect decisively to the upside. **We have strong conviction on our portfolio holdings delivering on earnings and cash flows compounding at 15%+ annually over the next three years.**
- **Valuations are compelling** given our benign outlook on Indian inflation/interest rates, and the long runway opportunities in industrialization, urbanization, consolidation, financial intermediation, digitization of the real economy, enhanced agricultural productivity, and growth in rural incomes and discretionary spending.

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
Bajaj Finance Ltd	Financials:	38%	Financials:	-1.53%
Kotak Mahindra Bank Ltd	Consumer Discretionary:	16%	Consumer Discretionary:	-0.76%
HDFC Bank Ltd ADR	Consumer Staples:	11%	Consumer Staples:	+0.31%
Titan Co Ltd	Materials:	10%	Materials:	-0.22%
Shree Cement Ltd	Technology:	7%	Technology:	+0.68%
	Health Care:	5%	Health Care:	-0.36%
	Industrials:	5%	Industrials:	-0.25%
	Real Estate:	4%	Real Estate:	+0.06%
	Energy:	3%	Energy:	-0.27%
	Utilities:	1%	Utilities:	+0.14%
	Retail:	0%	Retail:	-0.10%

The Fund has appointed Hugo Fund Services SA, 6 Cours de Rive, 1204 Geneva, Switzerland, as its Swiss Representative. Banque Heritage SA, 61 Route de Chêne, CH-1208 Geneva, Switzerland is the Swiss Paying Agent. In Switzerland shares shall be distributed exclusively to qualified investors. The fund offering documents, articles of association and audited financial statements can be obtained free of charge from the Representative. The place of performance with respect to shares distributed in or from Switzerland is the registered office of the Representative.

TANTALLON CAPITAL, 137 TELOK AYER ST #03-05, SINGAPORE 068602. T: +65 6327 3920 F: +65 6327 3924
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