TANTALLON CAPITAL

May 2019

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
May 2019:	+3.14%	+0.12%	+3.02%
2019 YTD:	+4.67%	+7.49%	-2.82%
2018:	-22.79%	-8.63%	-14.15%
2017:	+59.14%	+36.84%	+22.30%
2016:	-5.79%	-2.90%	-2.89%
2015:	+0.24%	-7.53%	+7.77%
Inception:	+21.45%	+29.53%	-8.08%

Compound Returns	+5.32%	Volatility	+20.12%
3 month US T-bill	+2.33%	Sharpe Ratio	+0.149

FUND DETAILS

The Tantallon India Fund

AUM USD 32,000,000

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)

The Tantallon India Fund closed up +3.14% in May, rebounding sharply off the mid-May jitters, buoyed by Modi's decisive mandate in the General Elections. Amidst stark geo-political uncertainty, and the growing risk of protracted trade conflicts exacerbating a fragile global growth outlook, **Modi's victory is a clear positive, bolstered by strong corporate earnings, and in particular for the small and mid-cap universe, continuing to surprise positively on the upside.**

With the BJP alone winning 303 seats, and the BJP-led National Democratic Alliance (NDA) winning 353 seats (out of 542 seats in the Lower House) with an unprecedented 50% share of the votes cast, the Indian electorate's messaging was unambiguous:

- This is only the second time an incumbent Indian government has been re-elected with an even larger majority – with the BJP/NDA exceeding the 2014 tally of 282/336 seats.
- **67% voter-turnout (603 million people actually voted!) and the highest recorded participation by women mark the Elections as a vote for continuity, stability, security, further reforms, investments, and job creation.**
- **This was a vote for Modi,** explicitly rewarding him for his unrelenting anti-corruption agenda, and the commitment to continued reforms – *despite the significant near-term pain wrought by the messy implementation of both GST and demonetization.*

Having criss-crossed the country over the past three months, we did want to take a moment to reflect on the General Elections:

- ***The electorate voted decisively for stability and continuity at the Center*** and deserves an awful lot of credit for the sophistication shown in distinguishing between their vote for the BJP in the General Elections, and the ***checks and balances*** they achieved by voting for the Opposition in the State Elections held this past December in Karnataka, Madhya Pradesh, Rajasthan, and Chattisgarh.
- Historically, the BJP depended on India's populous Hindi-speaking states in the north for its support base. ***Since Modi came to power five years ago, the BJP has forged, in Modi's image, a true national identity touting national security, an anti-corruption crusade, reforms, development, and job creation, affirmed by the electoral gains in the Southern states, the North Eastern states, West Bengal, Maharashtra, and Gujarat.***
- The parallels with Reagan and Thatcher are striking: once the pariah, ***Modi is now "larger" than his Party*** thanks to his personal charisma, an aura of personal incorruptibility, an unmatched ability to communicate a heady 'cocktail of development, targeted welfare schemes, and nationalism,' and crucially, the complete absence of a credible alternative as the Opposition self-imploded amidst petty regionalism, egos, and arcane caste Arithmetic.

Partly by default, and partly by design, **Modi's new cabinet reflects not just his call for continuous change and reform, but a commitment to deliver on explicit development goals.**

- *The 'inner circle' of Amit Shah (Home Minister), Rajnath Singh (Defense Minister), Nirmala Sitharaman (Finance Minster), and Subrahmanyam Jaishankar (Foreign Minister) does engender confidence given their track-record as extremely capable, driven technocrats.*
- *Even more encouraging is the continuity provided by universally well-regarded 'performing ministers' continuing in their earlier ministries* - Gadkari in Roads and Highways, Goyal in Railways (and incrementally, Commerce and Industry), Pradhan in Petroleum and Natural Gas (and incrementally, Steel), Prasad in Law and Justice, R.K. Singh in Power, Gowda in Chemicals and Fertilizers, and Puri in Housing and Urban Affairs.

YEAR	RETURNS	JAN	FEB	MAR	APR	MAY	JUN	JULY	AUG	SEP	OCT	NOV	DEC
Inception	+21.45%												
2019	+4.67%	-6.16%	+1.05%	+9.08%	-1.89%	+3.14%							
2018	-22.79%	-1.87%	-7.58%	-1.07%	+3.20%	-4.66%	-5.58%	+1.29%	-2.30%	-12.87%	-2.31%	+9.47%	+0.46%
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%

Bottom-line, we went into the General Elections virtually fully invested: ***as we have frequently articulated over the last several months, our expectation was for a Modi victory, and we are genuinely pleased that the Modi mandate has so handily exceeded our expectations.***

- **We expect that Modi's new mandate will (1) accelerate his reform and development agenda, (2) catalyze a new investment cycle, and (3) deliver on sustained, inclusive growth, and job creation.**
  - *Modi's focus priorities (investments, job creation, infrastructure, industrialization, and farm distress) and his new Cabinet does inspire confidence in the ability to deliver on explicit development goals in a growth-challenged world, sustaining a tailwind for Indian equities.*
- **Our significant convictions remain in financial services, consumer discretionary, and real estate, while remaining significantly under-exposed to the sectors most vulnerable to a global slow-down, i.e., IT Services, energy, and generic pharmaceuticals.**

The Key risks we continue to assess:

1. Messy geo-politics, protracted trade conflicts, and custom-union break-downs negatively impacting **global growth and risk appetite.**
   - *Please note: with the US accounting for just about 15% of India's total exports (pharma, agri-goods, plastic, leather, textile, marine products, gems and jewelry), we are not particularly concerned by Trump's recent rhetoric on terminating the preferential trade access extended to India.*
2. **Higher energy prices** potentially weighing on the rupee, on the government's ability to deliver counter-cyclical fiscal stimulus to catalyze a new capex cycle, and on the Reserve Bank of India's instinct to further ease monetary policy;

The stock we would like to highlight this month is ***Chalet Hotels,*** the hospitality arm of the K Raheja Group, operating in the business and luxury hotel segments in the high traffic / high entry barrier markets of Mumbai, Bangalore and Hyderabad. Given the demand/supply dynamics in Chalet's micro-markets, we have strong conviction projecting rising occupancy levels and improving average room rates as India's hotel industry inflects off a ten-year recession brought upon by over-building, excessive leverage, falling occupancy levels, and falling room rates.

We expect Chalet Hotels to deliver on organic revenues compounding at 15%+ annually over the next three years, versus the market projecting a more modest 12% CAGR.

- The Marriott and Hyatt brands and loyalty programs (50% of current inventory is booked by international business and leisure tourists), and strategic locations in the growth markets of Mumbai, Bangalore, and Hyderabad, are key to our assumptions on higher occupancy levels improving room rate realizations.
- Over the next two years, we expect the commercial launch of three new hotels (a Westin branded property in Hyderabad, and a W, and a Hyatt branded property in Mumbai), and two new commercial developments in Mumbai and Bangalore.
- We are currently not modeling any in-organic expansion. However, given the balance sheet strength, and the new intent and resolve behind India's new bankruptcy code, we do expect several potential distressed acquisition opportunities in key new markets/locations

We expect earnings compounding at 65% annually over the next three years, versus the market's more modest expectations of a 20% CAGR.

- On the back of scale (occupancy levels improving by 100bp annually) and improving mix (a combination of higher average room rates, the up-selling of re-branded properties, and higher food and beverage sales), we expect EBITDA margins to expand by 800bp+ over the next three years to 45%.
- Continued deleveraging of the balance sheet, and hence, significant interest cost savings.

To conclude:

- We expect that **Modi's decisive new mandate will accelerate a strong reform / development agenda** to deliver on sustained, inclusive growth, and job creation.
  - *In a growth-challenged world (underscored by recent price action in gold and US Treasuries), India's structural reforms and domestic economy stand poised to deliver on sustained real GDP growth compounding at 7%+ annually over the next 3-5 years*
- On the ground, we continue to renew our **conviction in India's idiosyncratic growth opportunity** translating to sustained rural consumption, a nascent capex cycle, infrastructure development, industrialization, urbanization, and the digitalization of the real economy.
  - *We expect our portfolio companies to deliver on earnings and cash flows compounding at 15%+ annually over the next three years.*
- **Valuations and the risk/reward are compelling** (and especially in the small and mid-cap space) given *our expectations of sustained revenue and earnings growth, the likelihood of further easing by the Reserve Bank of India, and improving systemic liquidity.*

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
Bajaj Finance Ltd
HDFC Bank Ltd
Kotak Mahindra Bank Ltd
Titan Co Ltd
Housing Development Finance

Sectoral Break-down:	As % NAV
Financials:	39%
Consumer Discretionary:	22%
Materials:	9%
Real Estate:	7%
Consumer Staples:	7%
Technology:	6%
Industrials:	5%
Energy:	3%
Retail:	2%
Health Care:	0%
Utilities:	0%

Sector Performance	MTD Performance
Financials:	+2.97%
Consumer Discretionary:	-0.36%
Materials:	+0.18%
Real Estate:	+0.37%
Consumer Staples:	-0.34%
Technology:	+0.34%
Industrials:	+0.25%
Energy:	+0.37%
Retail:	-0.64%
Health Care:	+0.00%
Utilities:	+0.00%