Dear Investor,

June 11, 2025

"Finance is an industry moulded by disaster." – The transformation of Wall Street, The Economist, May 31, 2025, pg.3

Chanakya PMS is now two months short of seven years of investments. Your trust has made our journey, so far, highly enriching, in terms of learning; fine-tuning our investment processes, and finally discovering that after three years of investment, your portfolio acquires a high degree of stability, in performance. We have recently received permission to open our branch office in the Gift City, Gandhinagar. This will allow us to channel offshore funds in our proposed AIF there with convenience and tax efficiency. Chanakya would be able to invest your money in stocks of companies outside India. We will shortly be in touch with you on the 'why and how' of it. We always evaluate any investee firm in comparison to the global best companies, in the same business. Hence, in this Newsletter we are sharing a bit of the 'context' of our investment mind.

Time, Society, and Context - Black Swan Event/ Structural Shift/Unsystematic Risk?

Big events in our life ought to be evaluated with respect to time, society and context. The two recent big events impacting us are Operation Sindoor and tariff negotiations with the USA. Both these events have genesis in recent political shifts in the two countries Pakistan and USA, ideology of the respective ruling classes, and a broader context of international stature of the two nations. In recent decades. China and India have rebounded as great nations. Their present persona are shaped by their respective historical as well as recent socio-cultural developments.

"China was always centralised with the Dragon throne in Forbidden City seeking tributes from the rest of the world. India, by contrast, is based on the Mandala model, first described by Chanakya, a set of intersecting spheres of power that are endlessly pulsating, contracting and expanding over time. No centralisation. The Chinese have always been suspicious of radically different ideas. China, like India, was hit hard by industrialisation. The Europeans conquered the Mandala states of India realising that the Indian way (even after 600 years of Muslim rulers) involved endless negotiation and not compliance. Conquering China was tougher. They had walls to keep out foreigners. So, the British flooded the markets with Indian-grown opium and took away their vast stocks of silver. China has never forgiven the world for the resulting 'century of shame'. It reimagined itself with Communism, then with Capitalism, determined to get the world to tremble and obey once more. The idea of domination is alien to the dharmic way, the arguments about Brahmanism notwithstanding made by generations of Marxist and westernised academicians. They miss the point. The Dharmic way is about collaborating with different communities in different ecosystems, keeping Brahmins on top. It is what led to creation of circular Mandala states in the river valleys from South Asia to Southeast Asia. These states were eternally fragmented and competitive and collaborative, bound by a common story of solar and lunar kings. Centralisation has never been an Indian idea. Mauryas never controlled the river basins of Godavari or Kaveri. Mughals controlled only North India." – Why India won't tremble and obey: A civilisational contrast with China, Devdutt Pattanaik, The Economic Times, May 24, 2025

Over time, external context changed a lot for these two nations. While the core socio-economic values of these two societies have changed considerably in recent decades, but didn't get imported or transplanted. The cause and context for any long-term shifts in gear for a nation could be global, industrial or new innovations in science and technology. Both China and later on India unleashed their animal spirits after a big churn in their respective political economy. In the context of India, our special 'Moments' in a way are outcome of the societal transformation India has seen since 1992. In case of China, the process began in mid – 1970s with Mr. Deng Xiaoping becoming the leader of the nation.

What lessons we may derive for our investment strategy from such changes all-around? Almost always, Black Swan events become visible in the hindsight. Hence, we choose to focus on anti – fragility and innovations in case of our investee companies. For us, the question always remains whether our investee firm would emerge stronger during phases of turmoil.

Performance measurement – Context

A good performance measurement system helps an entity to precisely formulate its long-term strategy and implementation tactics. We see it as a key issue in case of the firms we appraise. We think this to be equally applicable in case of nations and societies, as each one of these also have to have an overall purpose, as any firm has. A recent article in The Economist has an interesting view about the recent political churn in the USA.

"The parties have become so weak that whoever becomes their nominee can dominate them. Mr Biden's vanity, and that of his family and closest aides, overrode common sense about whether he should seek a second term. Few Democrats spoke up about his infirmity while he was in office. This may not be merely a story of the decline of a man, his party and the media. It may turn out to be about the decline of American democracy itself."– Joe Biden did not decline alone, David Simonds, The Economist, May 20, 2025

The recent shifts in the international trade and economic environments are going to change our understanding of what performance means over time in the context of a society and economy. In this Newsletter, we have tried to look at what these recent developments could imply for the Indian economic environment, and your investee companies in the steel business.

Psychologically, many people seem to be lacking sufficient clarity about risk in, and objective of their investment program. Often, it is due to lack of adequate financial literacy. As per David Kahneman, this also may be attributed a lot to psychological biases human beings inherently have. That's why precise performance measurement of a fund becomes vital for prosperity of an investor.

The world has always been a risky place.

Covid-19 was the last Black Swan event we encountered. It evoked varied responses from different nations. Covid-19 hurt a large percentage of Indian population in terms of life expectancy as well as economic well – being. It doesn't look like that the consequent losses have been fully recouped in case of many places and families in India. CR2, a top-end recreation mall at the most premium CBD area at Nariman point in Mumbai, saw two major restaurants and a few high-end shops closed during the Pandemic. These remain shut till date. Scars of the Pandemic can even now be seen in weakened indicators like life expectancy, employment rate, and income level of a large number of Indians. However, it also led to a creative societal response. New efficiently calibrated financial support system for the weaker section of the Indian society, adoption of work-from-home, quick and e-commerce type of delivery systems, and a big step-up in digital transformation of the Indian society have improved life for a high percentage of the Indian population. It has also helped to improve overall efficiency and wider reach of many commercial services. The overall macro of India has considerably improved since the Pandemic. In contrast, many economically advanced nations are yet to normalize high governmental debt levels incurred during the Covid-19 period for cash support extended to citizens.

The world always has been a risky place, in its politics, economics, behaviour of human race and industrial and technological advancements. We must emphasize here that risk does not necessarily reflect a negative connotation. In fact, many times surprising innovations in societal, economic, industrial, technological, and financial spheres enhance productive capability of mankind, unforeseen by almost anyone. Much more than that, the ability of the human race to navigate through tough times, helped by its innovativeness, keeps on propelling economic growth of humanity. It is our proposition that human ingenuity, aided by market forces, would ultimately see us through various unforeseen risks and help the world to become a less risky place. Let us not get depressed by possibility of 'n' – type of Black Swan events. In Chanakya, we focus on firms which may come up with creative responses for their customers during phases of uncertainty and disruption. Let us be aware of the fact that in our lives, there is no scope for half – measures.

In fact, could Operation Sindoor represent more of structural shift in the strategic thinking process of India? We believe this to be the case. In our reading, India has now arrived as a major economic and military power at the world – stage. India could now be viewed close to emerging as the third-strongest nation in the world. This are not a function merely of economic strength. This also requires visibility of future growth, moral stature, and a democratic value system shared by the people and institutions. We would like to add that recent announcements by President Trump, in case of US academia as well as tariff, also ought to be evaluated against the same measures. The litmus test could be whether recent actions unite and strengthen the overall Society. We leave it to your judgement.

<u>AI is disruptive, but could add to size – related advantages of a firm.</u>

The range of disruptions that AI could potentially generate are yet not visible, much less understood. In case of our own business of asset management, we have begun wondering whether financial analysts may be needed in the future. Already, we have done away with services of transcribers, and a gamut of clerical and data-related services. We are becoming increasingly aware that in the medical field, physics and AI potentially might replace many of the diagnostics so far undertaken by doctors. In fact, many of the medical procedures could be largely undertaken by well-designed intelligent programmes and machines. On the positive side, reliability, speed and precision in any service could go up significantly due to the well-thought-out application of AI and other new tools in science.

We have been seeing that information – intensity and service capability are becoming increasingly more critical for large firms. Compared to smaller firms, large size firms often have higher bureaucratic rigidities. If applied thoughtfully, AI helps larger firms to become more agile by improving customer-level information, and customer-connect, thereby getting customers come closer to key decision makers in the organization. In addition, recent organizational structure – related innovations, like ESOPs, precisely defined performance measurement metrics, and 360° feedback have enhanced customer-connect and agility of large organizational, especially of the likes of large banks. A recent article in The Economist analysed how AI adds to size – related advantage of a firm.

"For all the unwieldiness it entails, scale has always brought enormous benefits in business. Fixed costs are set against more revenue, raising profits and supporting investment. Heft brings

bargaining power with suppliers and financiers. From the early 2000s, the advantages of scale became more pronounced. Intangible assets, including software and intellectual property, gave the upper hand to companies that could afford to invest in them. Globalisation provided big companies with more room to grow, as well as access to larger—and cheaper—pools of labour. In America, the gap in profitability between big and small firms widened. Economists began to speak of "superstar" firms racing further ahead of the competition.

Now size is conferring advantages in new ways. Artificial intelligence (AI) is reinforcing the dominance of big firms over small ones. Start with AI. You might imagine that lumbering leviathans would be too tied up in bureaucracy to make use of the technology. In fact, their scale allows them to invest far more in it than smaller rivals. getting AI to work well is proving more expensive than for other types of digital technology, as it requires companies to organise their data and tinker with models. Big firms have the added advantage of larger data sets that can be used to refine the AI systems they build. Larger firms, though, tend to be more resilient to such shocks. That means they are less likely to get into financial trouble during a downturn. It also allows them to bounce back more quickly, as happened following the covid-19 pandemic. Bigness tends to also bring greater supply-chain resilience—as important amid a trade war as it was amid covid-19. It helps, too, that big companies tend to have more suppliers in more places. Last, with scale comes an increasingly valuable asset: political capital."– Why it has never been better to be a big company, The Economist, May 26, 2025

In Chanakya, we have been observing e–commerce and digital marketing helping new marketers to erode competitiveness of established large FMCG firms arising from brand image and distribution. Increasingly, tech-savvy and agile fintech have become complimentary to large banks. In the future, a bank will need to tie -up with fintechs, acquire them as well other innovative smaller businesses in order to remain agile.

<u>An illustration, risk – return equation of your investment in steel stocks</u>

Steel is a commodity that keeps on getting impacted by every macro -level disturbance in the globe: tariff changes by any major country, disruption in shipping, flooding in Australia coking coke mines, etc. Visibly, levels of systematic as well as unsystematic risk are quite high in case of the steel business. Key success factors in this business include access to low – price inputs, access to capital and size. However, presently China accounts for over 60% of global production of steel, despite not having access to low price inputs. The consequence has been significant distortions in pricing and profitability of steel firms across the globe.

Despite all this, around 9% of your investment portfolio has been invested by us in steel and related stocks. We understand the inherent risk. We also realize that steel is going to be there forever. We see rationalization occurring in the steel business in India and across the world. Just now, the USA government has allowed acquisition of US Steel by Nippon Steel of Japan. This acquisition represents further consolidation and rationalization of the global steel industry. We don't find it surprising that a seemingly highly protective USA Government has favoured this deal. The Biden government had put this deal on hold. Nippon Steel has emerged as the leading technology and process inventor in the steel business in the world. We believe that our investee companies in this sector will be moving significantly up the value chain in the long-term. Steel and related stocks in your portfolio, like Tata Steel, SAIL, Vesuvius, and Sarda Energy are becoming increasingly more competitive at the global level. These are led by management with clarity of vision, good corporate governance and access to low-cost inputs. Hence, any volatility in price of steel as well as steel stocks provides us attractive investment opportunity for the long term. Moreover, our investments at a high margin of safety in your this sub-portfolio have already yielded good return over time.

<u>Investment performance acquires consistency at the end of three years.</u>

There has been a saying among traditional Indian businesspeople that business is a matter of thousand days. As an entrepreneur in two start-ups, including your Chanakya PMS, we are the empirical proof of this. For each one of your individual portfolios, we have seen that at the end of three years, a portfolio begins to exhibit consistency in risk-return profile. Your PMS accounts are customized, not standard recipes, which is a major plus point of a PMS. This has also allowed us to observe long-term behaviour of a somewhat diverse portfolio, thereby gradually fine-tune investment parameters.

Why does it happen so?

Because every thousand days, cycle might be changing in case of economy/businesses/entrepreneurs. We have seen that any turn – around of a business organization actually begins to concretize in 2–3 years' time. In fact, in my prior experience, while working with premium Indian financial institutions, I saw that a newcomer required two years to establish his or her credibility in the organization. The best of turn-around managers got truly empowered after this trial phase of two years, and then over the next one year, they were able to deliver wonderful results. Building of new systems and processes and harmonizing these with the people and DNA of any organization also requires 2–3 years' time. Each one of your investee companies, in our view, has been passing through a turn-around phase. We have been a witness and student of this phenomenon over the last nearly seven years of investments by Chanakya PMS. Personally, I had the good fortune of being a part of this process in UTI/Axis Bank, where we enable around 125-130 Indian firms in the process of their significant transformation.

What does it imply for your investment Portfolio.

Table -1 below presents CAGR over a three-year period in case of overall investments made by Chanakya PMS on a rolling basis.

<u>Table – 1: Chanakya PMS – CAGR of Return and Rolling NAV over years</u>

CAGR % *(As on 31st May 2025)*	0 Yr	1 Yr	2 Yrs	3 Yrs	4 Yrs	5 Yrs
Money Invested and end of the period value	100	115.16	156.85	200.09	214.65	402.82**
CAGR		15.16	25.24	25.97	21.10	32.87
Nifty 50 TRI		11.08	16.88	15.56	13.60	22.32

Source: HDFC Fund Accounting

*Net of all expenses and fee

****** This seemingly excellent return was boosted by a base effect due to Covid–19. However, our performance of Nifty 50 during a volatile period was noticeable.

As may be seen in Table 1 above, your initial investment rose by 100% over past three years of rolling investment period. A PMS stipulates minimum investment of ₹50 lakhs. Except for the three-years spanning the Covid-19 period, at the end of three years, this creates a big cushion for our investors as it enables them to be able to tide over even high volatility in the future. Much more than that, this solid cushion allows our investors to indulge in their life and related passions, could be buying a new house, going abroad with family every year, pension type income, financing children's education, taking care of healthcare expenses, and much more than anything else, not to fear any unforeseen worsening of economic environment. Hence, we would recommend our investors to entrust their money with us for three years. Since we don't levy any exit fee, you can redeem your hard-earned money even during the first three years. Most likely at the end of three years, your financial status would have switched to higher orbits.

Performance measurement of an investment portfolio

While performance is about capability, in India performance measurement in investments appears to be more about eliminating noise. Wealth managers focus on the relationship aspect with an investor, often neglecting a scientific risk – return calibration. A lot of sales are based on satisfying emotional needs of an investor. We would like to delineate a framework for measurement of performance of an investment portfolio for any investor on the following lines:

1. Define the following precisely – time frame, performance compared to an appropriate benchmark, alpha of returns based on an appropriate risk measure, liquidity, and quality of portfolio

2. Assess suitability of a given investment product for an investor

3. Look at selection efficiency of a portfolio over three years or more. Shorter – term measure could be excessively affected by recent volatility in the stock market.

In case of Chanakya PMS investment portfolio, we would like to illustrate the above aspects in Table – 2 below.

Table 2: Chanakya PMS – Select Performance and Risk measure

Time Frame	1 Yr	2 Yrs	3 Yrs	4 Yrs	5 Yrs
Return *(As on 31 May 2025) (%)*	15.16	25.24	25.97	21.10	32.87

Time Frame *(As on 31st May 2025)*	3 Yrs
Beta	0.97
Jenson Alpha	9.43
Stock Selection efficiency	10.37

* Source: FINALYCA PORTAL and HDFC Fund Accounting

Obviously, there is no scope for half measures in investment performance. In our opinion, an investor should evaluate performance – generation capability of a fund based on previous five years performance. One should also look at performance over the last three years as it would indicate whether the fund has been able to adapt to new developments in economy and businesses in recent years. Performance over the last one year would be helpful to ask whether underperformance is due to the fund thinking ahead of the rest of the market, or being a laggard in its thought process.

Portfolio Composition and Risk

In our overall portfolio, top 15 stocks currently account for 84% of total investment. The overall sectoral break up of our investment portfolio is given in Table 3.

Table 3: Chanakya PMS - Portfolio Sectoral Allocation as on May 31, 2025

Sector	Allocated Portfolio %
Banks & NBFCs	48%
Holding Companies	17%
Metals & Minerals	9%
Industrials	8%
Auto & Auto components	7%
Consumer Goods	2%
Logistics	2%
Others	7%

Source: HDFC Fund Accounting

Compared to portfolio composition on Feb 2025, weights of holding companies has gone up by 3% and weights of banks has gone up by 1%, while weights of industrials and others, has come down by 2% and 1% respectively. These shifts are primarily due to movement of prices of stocks.

Table 4: Chanakya PMS - Investment Performance* as on June 10, 2025

Over the last 6 years and 10 months of our investments, the overall performance of our portfolios is given below in Table 4.

Period	Portfolio (In %)	Nifty 50 TRI (In %)
1 Month	13.52	4.87
3 Months	18.39	12.12
6 Months	5.51	2.57
1 Year	14.97	9.15
2 Years	26.31	17.61
3 Years	28.81	17.04
5 Years	31.66	21.36
Since Inception (13.08.2018)	17.16	13.53

Source: HDFC Fund Accounting
*Net of all expenses and fee

A dissection of the composition of the investment portfolio of Chanakya PMS reveals:

a. High concentration in financial stocks, especially banks. We believe that Indian banks represent a leveraged bet on the growth of the Indian economy in the long-term.

b. A 9% allocation to steel and related stocks

c. 17% investment in holding companies: the shares of our investee holding companies have been quoting at a discount of 60–80% to the value of underlying shares. We believe that over time this large discount would narrow down significantly as market pricing becomes more efficient.

d. 8% investment in select industrial shares: Companies like Motherson Sumi are the global market leaders in its business. They have been quite cost-competitive as well as innovative over time. The managements have been agile and long-term thinker. As Indian economy becomes more sophisticated and globalised, select Indian industrial companies would become globally competitive.

The above return numbers validate efficacy of our long-term investment process. In light of the longer period performance figures above, we think that your investment portfolio is becoming more resilient to economic as well as market shocks, though not insulated to these.

With best regards,
Rajesh Tiwari

And on behalf of the new world out there,
Gautami Desai and Team Chanakya