# INVESTOR GUIDE

October 2023

## DISCLAIMERS

The information provided on this document is meant only for general reading purposes and does not have regard to specific investment objectives, financial situation and the particular needs of any specific person and therefore should not be construed as i) an offer or recommendation to buy or sell securities, commodities, currencies or other investments referred to herein; or ii) an offer to sell or a solicitation or an offer for purchase of any of the funds or products offered/managed by Helios Capital Asset management (India) Private Limited ("AMC")/Helios Capital Asset Management (India) Pte. Ltd. ("Sponsor"); or iii) an investment research or investment advice; or iv) as guidelines, recommendations or as a professional guide for the readers. Investors/prospective investors should seek personal and independent advice regarding the appropriateness of investing in any of the products, securities, other investment, or investment strategies that may have been discussed or referred herein and should understand that the views regarding future prospects may or may not be realized.

In no event shall the Sponsor, the AMC, their respective directors, employees, affiliates or representatives, etc. (hereinafter referred to as "Helios") shall be liable in any way for any direct, indirect, special, incidental, consequential, punitive or exemplary damages, including on account of lost profits arising from the information provided herein.

The details, views, suggestions, illustrations, strategies, investment philosophy, etc. are collectively stated as 'Information" in this document which is subject to changes from time without any prior intimation to the readers. Information gathered used herein is believed to be from reliable sources. The AMC/Sponsor however does not warrant the accuracy, reasonableness and/or completeness of any information. If the said Information contains any mistakes, omissions, inaccuracies and typographical errors, etc. Helios assumes no responsibility thereof. Any action on your part on the basis of the said Information is at your own risk and responsibility. The AMC/Sponsor reserves right to correct any part of the said Information at any time as and when required at its sole discretion. The Information contained in this document shall not be reproduced, stored in a retrieval system, or transmitted, on any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, in part or whole without the prior written permission of the AMC/Sponsor.

### Specifically, please note:

- This document is informational and does not constitute an offer to sell or the solicitation of an offer to purchase any security or investment product.
- Past performance is not necessarily indicative of future results.
- An investor could lose all or a substantial amount of his or her investment in funds.

**MUTUAL FUND INVESTMENTS ARE SUBJECT TO MARKET RISKS, READ ALL SCHEME RELATED DOCUMENTS CAREFULLY.**

## Message from the Founder and Group CIO

*When I, along with my co-founders set up Helios Capital in 2005, we were fired-up and excited about what lay ahead. It has been quite a journey since, of many ups and some downs, in both life and business, for all of us at Helios. I am sure it has been the same for all of our readers - our friends in the industry and outside, and our investors - past, current or prospective.*

*I am proud to say that we stand today stronger than we have ever stood. There is fire burning in every team member, our culture – painstaking built and preserved – gives us cohesion and focus, and our experience – of each senior investment team member having spent over 25 years in markets – brings to the table a lot of cumulative learning, from the mistakes that we have made over our long careers, and otherwise. Today, from this vantage point, we look to the future with confidence, as we make the push to build a truly institutional quality fund management house focused on India.*

*We have relatively quietly, and in a methodical and planned manner, pushed on to invest in our teams, systems, and processes over the past few years. In early 2020, we started expanding our footprint by entering the fund management business onshore in India under PMS/AIF regulations (we have had our research team in India since Day 1). We took a second step in that direction, when, in August 2023, we received approval from the Indian capital markets regulator, SEBI, for a Mutual Fund licence. The launch of our onshore India mutual fund business will further diversify our investor base, which we believe will add further to the resilience of our business whilst providing a more vibrant pathway for learning and growth for our expanding investment and non-investment teams, the vast majority of which is in India.*

*As we expand to serve different investor pools, it is important to note that our investment philosophy, research framework, the entire research team and research input continue to remain common across our offshore, onshore PMS/AIF and onshore mutual fund investor pools.*

*Our investment philosophy, has stood the test of time. It had its genesis in the first few years after I moved back to India in 1993 to set up Alliance Capital's operations, and has over time been further refined in light of the experience and learnings over the team's long tenure at Helios.*

*We hope to give you a deeper insight into our investment philosophy and processes in this document. We hope you find it informative, interesting and thought provoking.*

**Samir Arora**
*October 2023*

In this guide, we discuss many topics of general interest to investors, as well as those that give an insight into our unique perspective to investing.

The guide is structured along the following chapters:



**Note that past performance is not necessarily indicative of future results.*

# 1. Introduction to Helios Capital

## 1.1 Company overview

Helios Capital Asset Management (India) Pvt. Ltd. (Helios India) is an asset management company, headquartered in Mumbai. Helios India is licensed by the Securities & Exchange Board of India (SEBI) to offer Portfolio Management Services (PMS) and Alternative Investment Funds (AIF), and it also acts as an Investment Manager to the Schemes of Helios Mutual Fund.

Our parent, Helios Capital Management Pte. Ltd. (Helios Singapore), is an India focused Singapore based asset management company. Helios Singapore holds a Capital Markets Services License from the Monetary Authority of Singapore and is registered as a Foreign Portfolio Investor with the Securities and Exchange Board of India. Helios Singapore is the Sponsor of the Helios Mutual Fund.

Helios (the Helios group companies referred to collectively) was founded in 2005 by Samir Arora, (Group CIO and Portfolio Manager of Helios Strategic Fund since inception in 2005), Dave Williams, and Karan Trehan. Each of the three founders have long standing experience in senior positions in asset management, and were pioneers in the Indian asset management industry, having jointly set up one of India's first private sector AMCs in 1994 (Alliance Capital).

Samir Arora has one of the longest track records as a fund manager in Indian equities (28+ years in long side investing). Uniquely, he is also one of the most experienced India fund managers with short side investing experience (18+ year formal track record in shorting stocks). We believe Samir's long experience and proven success in shorting equities over a long period of time provides Helios with an advantage in discerning good stocks from bad stocks, that is not usually available for investors with a less holistic approach to investing.

We pride ourselves in the long tenure of the senior team at Helios. Helios launched in 2005 with 4 employees, and all 4 are still with Helios, reflecting our culture and our shared value system and ideologies.

Helios today employs over 50 employees, predominantly across our two main offices in Singapore and Mumbai, all sharing in the Helios culture and its "can-do" spirit, alongside the high standards of conduct that we aspire to live up to.

We also believe we have one of the most experienced investment teams in the Indian Fund Management Industry. Each of our seniors have over 25 years of investing/research experience and are backed up by a team of portfolio managers and analysts.

The team at Helios is bound together by our shared belief that India is a great equity market, fated to achieve even greater heights, and that with hard work, intellectual honesty, and Helios' time tested investment philosophy, we can deliver competitive returns for our investors, whilst holding ourselves to the highest standards of conduct.

## 1.2 Mission, Guiding Principles, and our promise to you.

**Mission:**

Our aim is to build an asset management business that delivers excellence in performance for our clients, each of whom is a priority for Helios, leading to long term wealth accretion. We strive to do this by putting our guiding principles outlined below, in action:

**Guiding Principles:**

1. **Be honorable, ethical and respectful** in our conduct with clients, partners, employees, in management of the business and in markets.
2. **Make client centricity core to our operation**, as this is the group that we ultimately serve as asset managers.
3. **Aim for excellence in research and Portfolio Management (PM),** on the back of a deep bench of PMs and research analysts, applying Helios' investment philosophy and processes with consistency.
4. **Ensure the "Helios" process is as important as the "Helios" people**, in order to maintain repeatability, consistency, and adherence to our standards, whilst retaining the entrepreneurial flair in our DNA, and ensuring effective backups for our roles
5. **Ensure longevity of the business**, through good business practices, strong operational processes, prudent risk management, and commitment of internal capital
6. **Maintain a cohesive and incentivized team**, bound together with common goals and in a performance-oriented environment, alongside our growth.
7. **Focus on environmental, social and governance related factors** in a practical and prudent manner.

***"Our commitment to our investors is straight forward: 'We will not let our investors down knowingly'. … we will first do whatever is right for our investors."***

Our commitment to our investors is straight forward: 'We will not let our investors down knowingly'. We consider our relationship with our investors as sacred. We will always be open and fair. On any thing where we have control, we will first do whatever is right for our investors.

# 2. India – robust investment returns*

**"For the past 25+ years … NSE500 Index and MSCI India Index has given higher returns than one would have got from investing in shares of Berkshire Hathaway[1] (and yes, in US$ terms)."**

*1 Berkshire Hathaway is an American multinational conglomerate holding company headquartered in Omaha, Nebraska, United States of America. The company has been overseen since 1965 by its chairman and CEO Warren Buffet and (since 1978) by its vice chairman Charlie Munger, who are known for their advocacy of value investing principles.*

- *Note that past performance is not necessarily indicative of future results.*

## 2.1 India versus Berkshire Hathaway and other global indices:

Let us look at a couple of simple yet mind-blowing facts:

- For the past 25 years (August 31st, 1998, to August 31st, 2023) Indian indices like MSCI India and NSE500 have delivered higher returns than one would have got from investing in shares of Berkshire Hathaway (and yes in USD terms).

  Here we are comparing the performance of Mr. Warren Buffett, one of the most respected investors in the world, with India's unmanaged / passive index over a reasonably long period!

- Over this period in USD terms MSCI India Net Total Return Index and NSE500 Index have compounded at 11.50% and 12.93% p.a. respectively, while shares in BRK/A have yielded 9.20% p.a. *(source: Bloomberg).*

Twenty-five years is a long time even by Mr. Buffett's standards and so this is quite impressive considering how lucky investors of Berkshire believe themselves to be!

Some investors will immediately and for good reason point out that this is a wrong comparison, for this is like comparing apples and oranges, and that these numbers are not risk adjusted. We agree with that, but now at least we have your attention!

It is important to note that Mr. Buffett himself defines risk as *permanent loss of capital*. So, if the Indian market (NSE500 Index) has delivered 12.93% return per annum in USD over 25 years *(source: Bloomberg),* it obviously means that there has not been any permanent loss of capital (at the market level). It should also be noted that here we are comparing Mr. Buffett's returns with the unmanaged / passive Indian index and not with active Indian funds that have outperformed the Indian benchmark by a very wide margin.

When we look at the MSCI India and NSE 500 returns in INR terms (for our onshore Indian investors), the returns are even higher!

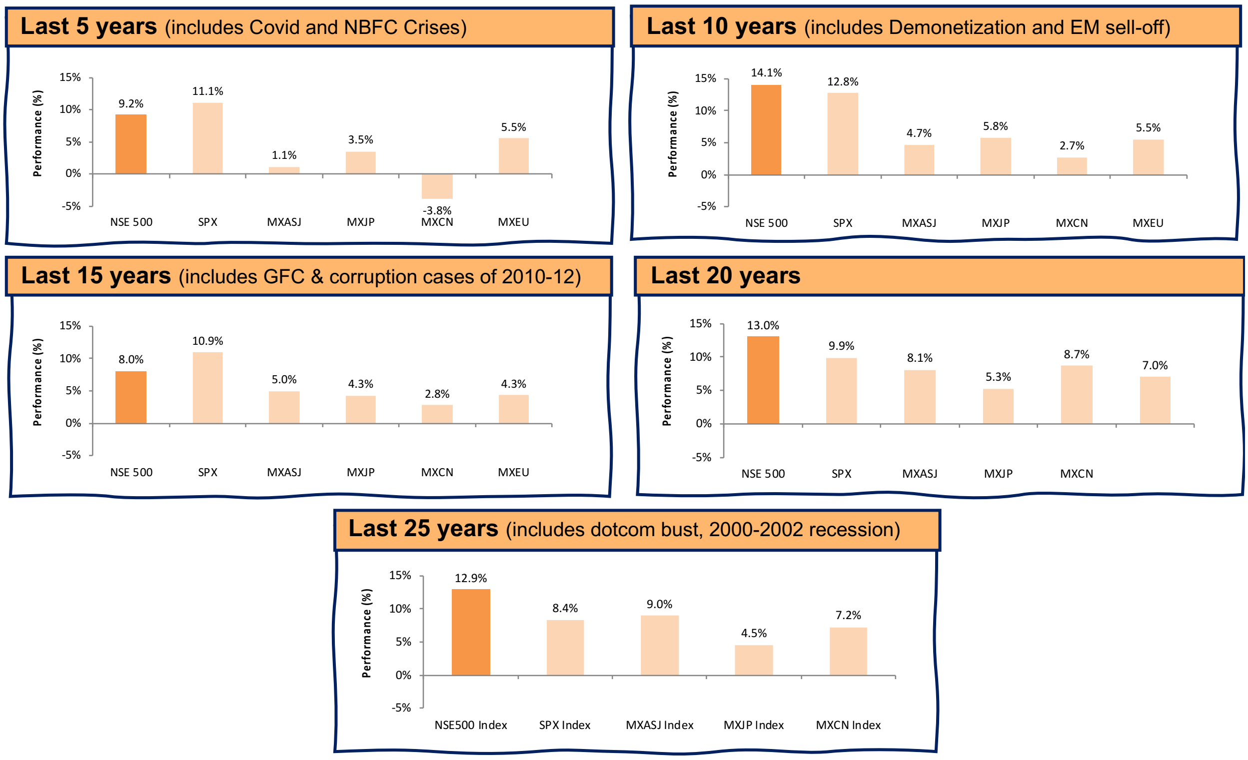
Now having said that, if someone wants to suggest that the Indian market is generally more volatile, we agree totally.

But here as well Mr. Buffett has guidance to offer. He says that volatility is the best friend of the unemotional, patient, debt-free investor and sees volatility as a way to occasionally find solid businesses at irrationally discounted prices. If one follows Mr. Buffet therefore, one understands that volatility is not a problem, although permanent loss of capital (achieved via over-leverage or poor stock selection processes) is a problem.

This also means that if investors in Indian funds had chosen volatile times to add more rather than redeem, their returns would have been even higher (buy / add at dips).

The performance of the Indian indices – over reasonably long periods - has been impressive not only in comparison with the world's best investor but also in comparison with most peer markets. The charts below show the performance of various peer markets across different time periods (all performance is in USD).

***Exhibit 1 – Annualized performance of India versus regional market indices***




*Source: Bloomberg (All numbers are with dividends reinvested. All performance is annualized in US$ terms). Data as of end August 2023. For illustrative purposes only. Past performance may or may not be sustained in future.*

So, although India has been a more volatile market over these periods than developed world markets, it has compensated better those investors who have kept their faith in her through the turbulent times. The reason for this much overlooked fact of India's outperformance is India's growth rate, of GDP and of earnings, that is higher than for almost all other meaningfully sized markets.

It is important to note that the volatility of the overall Indian market has been declining over the recent years, alongside the growth in the number of market participants and the structural upturn in domestic money flows into mutual funds (especially via Systematic Investment Plans (SIPs)). This domestic flow dynamic has also countered the effect from FII redemptions (as was in evidence in 2022) and has overall been supportive for equity market returns. Opportunities to make money have continued to grow, alongside the growth in the number of liquid and tradeable listed companies, regular stream of IPOs, and trends like innovation, disruption, and consolidation, cyclicality of various business models, and volatility in market price of individual stocks.

## 2.2 Reforms in India – setting the stage for a bright future.

We have always maintained that the biggest risk in India is that one does not know the next risk. In the past 2+ decades, the Indian indices have done well despite every possible risk playing out, and without much positive macroeconomic support (except over the 2004-07 period). India's resilience in the face of all of these crises has been stark, and the clean-up and reforms alongside various crises have set the stage for India to outperform over the coming decades.

***Exhibit 2 – Political, market and other crises and events in recent Indian history.***

**A. Episodes of Domestic Political Uncertainty**

- 8 coalition governments
- 3 different governments between 1996 and 1998
- A government that lasted only 13 days in 1996
- 17% fall in market in a day due to surprise change of government in 2004

**B. Other India Specific Events from 1998 to 2015**

- US sanctions after India's nuclear tests, May 1998
- Limited war with Pakistan in Kargil in 1999
- Serious stock market scandal in 2001
- Terrorist attack on Indian parliament in 2001
- 26/11 terrorist attacks in Mumbai in 2008
- Corruption cases & arrest of billionaires/ministers /senior bureaucrats in 2011/12
- Back-to-back drought years in 2014 and 2015 (for only the 4th time since 1900)

**C. Global Market Crashes and Crises since 1997**

- Asian Crisis in 1997
- Russian crisis in 1998 (India has had historically strong trading ties with Russia)
- Bursting of technology bubble in 2000
- 9/11
- Global Financial Crisis in 2008
- Tech sell off, end of QE and rising inflation (since 2022)

**D. Recent Key Events Since 2016**

- Demonetization (2016)
- NBFC Crises (2018/2019)
- COVID (2020-2022)
- Lockdowns (2020-2022)
- Rate hikes globally

Since 1991, India has carried out many major and minor reforms that have opened up the economy and capital markets, reduced policy risk, lowered taxation, and fanned the flames for rapid growth and thriving private enterprise, ultimately resulting in strong equity market returns.

**The first stage of reforms,** initiated in early and mid-1990s were largely focused on liberalization, privatization and globalization of the Indian economy:

**A) Liberalization:**
- a) Reduction of controls and restrictions
- b) De-licensing of industries
- c) More liberal trade and foreign exchange policy
- d) Lower corporate and personal taxes
- e) Reduction of import tariffs

**B) Privatization:**
- a) Initiated privatization of sectors (rather than of companies)
- b) Allowed private sector in areas previously restricted to state and state-owned companies.
- c) Divested government equity/listing of state-owned companies

**C) Globalization**
- a) Increase in foreign direct investments in select sectors
- b) Allowed Indian companies to raise foreign currency funds

c) Opening domestic equity markets to foreign investors
d) More liberal policy to allow Indian companies to invest abroad

**The second stage of reforms** initiated over the past decade or so deals with improvement in productivity, reduction of subsidies, better targeting of subsidies, reduction of corruption, improvement in infrastructure, reduction of fiscal deficit, strengthening tax collections and financialization and formalization of the Indian economy:

**A) Governance:**
a) Focus on controlling corruption
b) Natural resources allocation to corporates no longer at govt discretion (only via open auctions)
c) Planning Commission, from the era of Soviet Style Planning, scrapped
d) Ease of doing business

**B) Financial Sector Reforms:**
a) Major emphasis on financial inclusion
b) Modern bankruptcy law
c) Pension Funds allowed to invest in equity markets

**C) Demonetization:**
a) Increases in cost of evading taxes – higher tax collections in future as more businesses and people come into tax net
b) Benefits formalization of economy as cost of compliance increases for unorganized, small companies
c) Shrinking of cash economy has led to higher share of financial savings (at the cost of gold and real estate) and record inflows by domestic investors into equity mutual funds.

**D) Common India market:**
a) Goods and Service Tax
b) Unified National tax on goods and services that reduces cost of doing business / better logistics
c) Eliminates multiple taxation by allowing offsets
d) Makes it difficult to stay out of tax system, helping the formal sector which already pays taxes

**The third stage of reforms**, much of which we expect will happen in the new term of the government post 2024 elections, will focus on some of the even tougher reforms related to labor flexibility, land acquisition, privatization of state-owned banks etc.

**A) Recently implemented.**
a) Divestment of Air India
b) Corporate tax cuts in lieu of lower exemptions, and lower taxes for new companies

**B) Some day in the next few years, hopefully**
a) Restructuring of state-owned companies
b) Privatization, consolidation, sell-off of state-owned banks
c) Labor reforms
d) Land reforms
e) Tax reforms

In its reforms India has not employed rapid restructuring or shock therapy and none of these reforms have individually been big enough or headliners or ultra-radical in nature such that they hit international headlines. Instead, continuous small steps have accumulated over time and the direction of reforms has been quite positive.

In the meantime, India has many other dynamics working for it which make us optimistic about the future trajectory of the Indian economy and the Indian equity market. A number of macro trends are currently aligned in India's favor – these include attractive demographics, geopolitical position that is growing stronger by the year, tailwinds due to supply chain diversification away from China, rapidly improving local physical infrastructure, widespread digitization and a much-improved external account (e.g. rising FX reserves) that are laying the ground for sustained future economic growth.

### 2.3 Megatrends in India

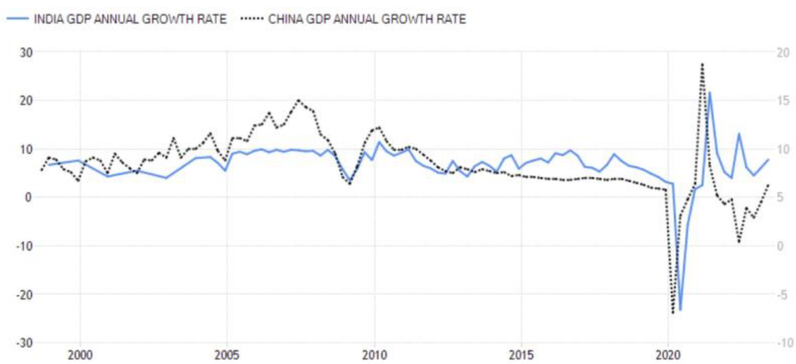
***India is seeing an alignment of macro tailwinds alongside secular growth***

India is largely a bottom-up driven market, that has traditionally delivered returns on the back of secular growth in its economy and earnings of companies, rather than due to overarching policy decisions or global macro tailwinds of the type seen in the US post the Global Financial Crises (QE, cheap money, buybacks) or in China (joining the WTO, inclusion in indices, policy backing of ecommerce until the recent turnaround by the government).

We believe we are now entering the phase where both India specific micro factors (secular growth, quality of growth, quality companies) are aligning with macro factors (India demographics; pivot away from China; supply chain transitions; infrastructure development) that should provide a tailwind for growth and deliver outsized market returns from India. Over our history of investing in Indian equities since the early 90s, we feel a similar decisive alignment of micro and macro factors has happened only once earlier, over the 2004 to 2007 period.

**2.3.1 High GDP Growth Rate:** India today stands as the fastest growing large economy in the world. In fact, India has had a higher annual GDP growth rate compared to China since 2014.

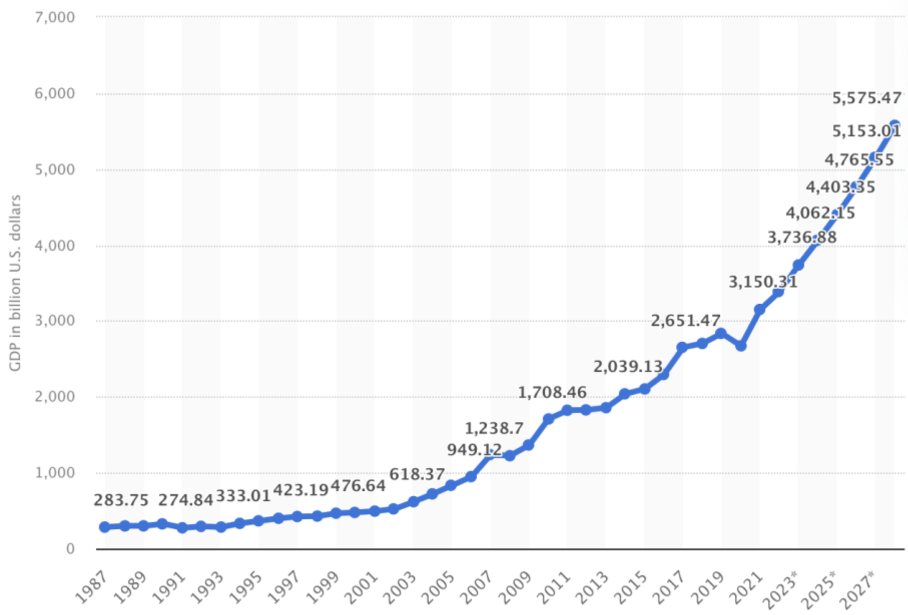
***Exhibit 3 – Annual GDP Growth Rate (%)***
*India is the fastest growing economy of meaningful size*




*Source: www.tradingeconomics.com*

As a result, the size of the Indian economy has rapidly expanded over recent years to become over USD3tn, which makes India the fifth largest economy in the world. India's GDP is expected to cross USD5tn by 2027, and it will become the third largest economy in the world well within the next decade. In that context it is incredible how under-invested and under-appreciated is the opportunity to participate in India's rapid rise. Therein lies the opportunity for investors, as foreign capital warms up to India, especially as geopolitical tensions between the western world and China lead investors away from China to other EM markets. The fact also is that others emerging markets like Russia and South America present even greater challenges for any risk conscious investor. India is in a sweet spot.

***Exhibit 4: India's total GDP (USD bn) – taken-off and accelerating***




**Projected.*

*Source:* [www.statista.com](www.statista.com)

**2.3.2 Megatrend - Demographics:** India is the most populous country in the world. It is also inhabited by a people that are industrious, enterprising, hard-working, ambitious and hungry to succeed. It's top 10% of about 150m affluent citizens, a fast-expanding group, is not far from the size of the current population of Western Europe that stood at 198m at May 28, 2023, per UN estimates. And although much needs to be still done to lift a lot of our country's citizens out of poverty, there is already a 400m plus strong and growing middle class. In short, India has a demographic tailwind that will be hard to stop. It also has a large, and fast growing domestically driven economy that can stand and grow on its own, although its rising interconnectivity to the world will be the icing on the cake.

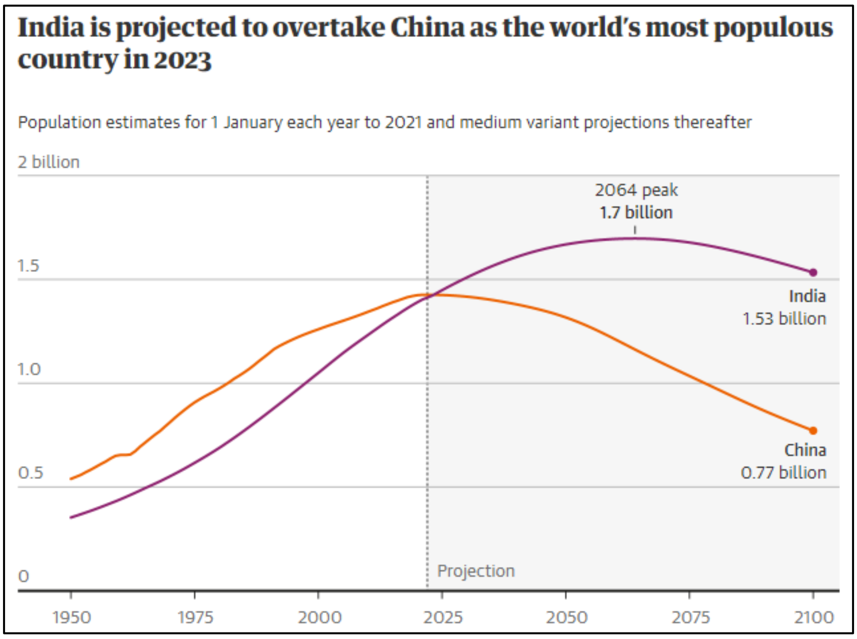
***Exhibit 5: India's unstoppable demographic strength***

**Demographic dynamics**

- 42.7% of population (c. 600 million) are below the age of 25
- Globally, one in 5 people below 25 years old are from India
- Population expected to peak by 2064 at 1.7bn (as per medium variant estimate provided by the UN)
- 400m and rising core addressable market
- Top 10% or 150m affluent, also expanding (current population of Western Europe 198m at May 28, 2023; UN est.)

*Source:* [www.pewresearch.org](www.pewresearch.org)

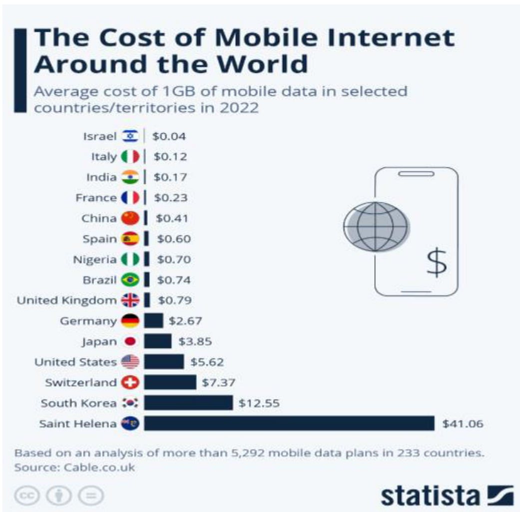
***Exhibit 6: India and China Population Growth Trend***




*Source: [www.theguardian.com](http://www.theguardian.com)*

**2.3.3 Megatrend – Digitization:** India is also now benefiting from an unprecedented degree of formalization, financialization and digitization of the economy. India today has the 3rd cheapest cost of data in the world, and its per capita consumption of mobile data is now greater than that of China plus USA combined *(source: campaignindia.in)*. This rapid pace of digitization is setting the stage for a more informed population, productivity gains, upending traditional ways of doing business, and creating entirely new businesses, many of which we have or expect to have in our portfolios.

***Exhibit 7: Low cost of mobile internet in India***
*Fueling growth*




**2.3.4 Megatrend – Infrastructure Build-out:** India is also building infrastructure at a frenetic pace, in part helped by stronger trend in tax collections resulting from tax reforms and greater emphasis on tax compliance. This growth in infrastructure will prove to be an important element in India's push to benefit from the diversification underway of production and supply chains away from China. This will have significant positive effects on employment, consumption and India's external balance.

***Exhibit 8: Physical infrastructure build-out in India***

**Infrastructure growth in India – brief highlights**

- Union Budget for 2023-24 has capital outlay for infrastructure at USD122 billion, an increase of 33% year on year. At 3.3% of GDP, the absolute outlay is 3x that of 2019
- USD29 billion to be spent on Railways in 2023-24, 9x that of 2013-14
- Airlines: Over 400,000 flyers per day in August. 100 million passengers carried by domestic airlines over Jan-Aug 2023
- 3196 km of highways built over Apr-Aug 2023

*Source: livemint.com; moneycontrol.com; Union Budget 2023-24*

**2.3.5 Megatrend – China plus 1 diversification:** Over time, we expect parts of the supply chain for various items from cars to iPhones, garments, chemicals and hundreds of other items to partly move out of China due to the need to ensure robustness in supply, hedge bets, search for a second source – in effect, "the need to not put all your eggs in one basket". We believe India will be one of several relative beneficiaries of this trend. A small shift in market shares within the supply chain pie is enough for India to create sustained growth and job creation for years. The impact of this would be huge and will show up across all sectors of the Indian economy.

***Exhibit 9: China + 1 diversification of supply chains***

**India – diversification of supply chains away from China is already underway**

- India now produces 7% of Apple phones, up from 1% in 2021
- Plan is for Apple to be producing 25% of iPhones in India by 2025
- Samsung has its second biggest manufacturing facility and its biggest R&D center in India
- India received USD52 billion of FDI in 2022 (China received USD189 billion)
- India has introduced PLI (Production Linked Incentive) scheme covering mobile manufacturing, auto components, pharmaceuticals, IT hardware, textiles, telecom equipment, medical devices etc. giving incentives of 4% to 6% of value for new production
- Cheap labor, huge domestic market ("Make in India for India" to begin with), government incentives, and infrastructure build-out all converge to position India for an increasingly important role in global supply chains

*Source: Reuters; Bloomberg; Economic Times; Macrotrends; MeitY*

**2.3.6 Megatrend – Increasingly advantageous geopolitical position:** In an increasingly bipolar world India finds itself in a strategically advantageous position that is proving to be hugely positive for the economy. The well-executed diplomatic offensive of the current government is now paying dividends as can be seen in India pushing though hard-headed national interest-based policies in its global engagement. As China and USA compete for technological and economic leadership, India is not seen as a threat, but rather a potential counterweight to China. Simultaneously India is able to maintain its good relationship with Russia, buying oil (including over the recent period), with Western governments largely looking the other way (note: India's purchases have been a small proportion of EU's purchases of energy from Russia). India also, despite the issues, continues to do business with China, where the intent will increasingly be to make the business exchange more advantageous to India than it has been in the past.

India's focus has been on building an important strategic partnership with the USA, rather than enter a formal alliance. This partnership is based on shared interests and mutual cooperation, and also entails membership of Quad. This development can only be a positive for India.

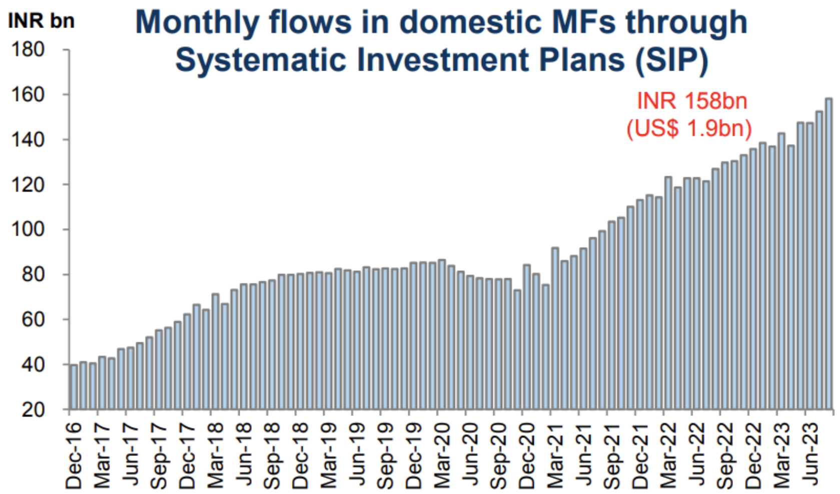
***India's approach to international issues takes a page out of Henry Kissinger's playbook:***

***"Mr. Kissinger's model for pragmatic thinking is India...foreign policy should be based on non-permanent alliances geared to the issues..."***
***(Economist, 20th May 2023)***

The net result of these initiatives is greater number of economic and strategic partnerships, further opening up of the country and a greater share of global trade-flows, leading to job creation, poverty alleviation and greater consumption.

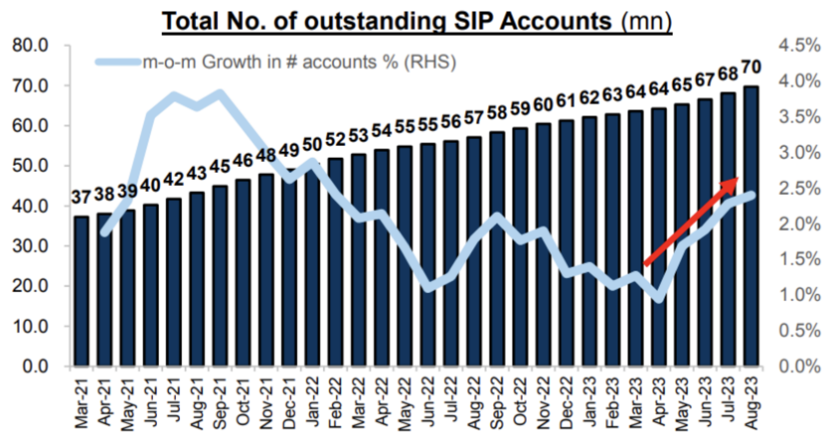
**2.3.7 Megatrend - Emergence of the domestic investor:** The Indian market benefits from a number of its own favorable dynamics. The emergence of the domestic equity buyer is an important factor to note and has positive implications for the direction and the volatility of the Indian equity market, looking ahead. This can be seen in the uptrend in monthly inflows into SIPs and the continued growth in number of new SIPs accounts (see below). There is an equity culture surely and steadily taking hold amongst India's individuals and families.

**Exhibit 10 - Monthly inflows into SIP plans (INR bn)**




*Source: Goldman Sachs; AMFI*

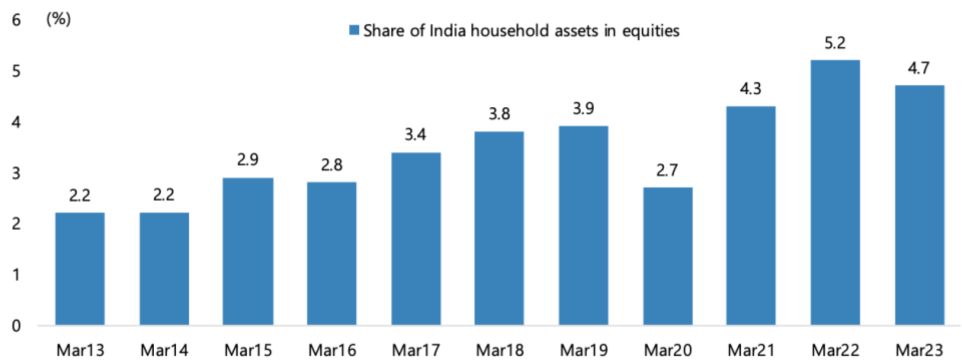
**Exhibit 11 - Total number of outstanding SIP accounts (millions)**




*Source: Goldman Sachs; AMFI*

As a result, equities' share of household assets has been rising over the past few years. However, as of March 2023, equities still only accounted for 4.7% of household assets. We expect continued fund flow into equities over the coming years as the importance of equities in household exposure increases.

**Exhibit 12 – Equities' share of Indian household assets (%)**




Source: RBI, Jefferies

# 3. India in MSCI – underweighted for now, upside likely

## 3.1 Rich and expanding opportunity set across sectors in India

Returns from Indian equities have also been helped by the breadth and quality of companies listed in the Indian market. Ultimately, investors invest in individual companies and for future earnings delivered by these companies, the rapid growth of which may derive from factors like continued GDP growth, specific reforms and demographics.

Opening of new sectors, that were previously reserved for state owned companies, to private sector companies, and various reforms related to formalization and financialization of the economy have led to emergence and rapid growth of hundreds of companies across infrastructure, financial and consumer sectors in India. India has also taken advantage of labor arbitrage in areas like software and pharmaceutical sectors to set up world scale businesses.

It is a fact that India (and Indian indices) have a better sectoral mix of listed companies than most of India's peer markets. For example, India has nearly a hundred subsidiaries of multinational companies (MNCs) listed in the Indian market. This means one can buy (say) companies like Nestle India, Unilever India, Pfizer India, ABB India, etc. which would rarely be available to investors in other emerging markets where their MNC parents operate (for they would be 100% subsidiaries of their global parent or private JVs with local players, and rarely listed on the local stock exchanges). These companies provide direct access to the vast opportunity of the Indian economy and its growth, from a setting that has the technology, focus and management standards of the multinational parent.

Looking at the exhibit below one can see that unlike Brazil (which has 39.8% of its market in global cyclical sectors) or Taiwan (which has almost 71.5% of its index represented by tech companies, which are mainly low(er) P/E technology hardware companies in B to B businesses often with cyclical, capital intensive businesses, that also are reliant on a few, much bigger and stronger global companies as their customers) or Korea (dominated by similar capital intensive technology companies that are exposed to global market conditions and sector cyclicality), India has a good mix of companies from sectors representing structural growth of India as well as cyclical sectors that are also currently seeing an upturn. In short, India has a good representation of sectors including consumer, financials, industrials, cyclicals, and information technology (the last, in India's case, happen to be mostly capital light models).

***Exhibit 13: Distribution of sectors across various Emerging Markets***

**Distribution of Sectors across MSCI Country Benchmarks**

| EM (EMERGING MARKETS) | CHINA | INDIA | TAIWAN | KOREA | BRAZIL | SAUDI ARABIA | SOUTH AFRICA | MEXICO | INDONESIA | THAILAND | EM Overall |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Global cyclical sectors** | | | | | | | | | | | |
| ENERGY | 3.1% | 10.6% | 0.3% | 1.4% | 21.3% | 9.5% | 1.1% | 0.0% | 4.2% | 15.2% | 5.2% |
| MATERIALS | 3.4% | 8.6% | 4.7% | 9.5% | 18.5% | 21.5% | 22.0% | 17.9% | 8.1% | 9.2% | 8.0% |
| | **6.5%** | **19.1%** | **5.0%** | **10.9%** | **39.8%** | **31.0%** | **23.2%** | **17.9%** | **12.3%** | **24.4%** | **13.2%** |
| **Steady growth businesses** | | | | | | | | | | | |
| FINANCIALS | 15.9% | 27.2% | 14.2% | 9.2% | 25.8% | 44.1% | 36.7% | 16.9% | 57.4% | 7.5% | 22.2% |
| CONSUMER STAPLES | 5.5% | 9.0% | 1.6% | 2.2% | 8.3% | 3.1% | 8.6% | 38.7% | 8.4% | 12.7% | 6.2% |
| CONSUMER DISCRETIONARY | 30.4% | 11.4% | 2.2% | 8.6% | 2.4% | 0.8% | 18.6% | 0.0% | 3.6% | 7.5% | 13.7% |
| HEALTH CARE | 5.6% | 5.1% | 0.3% | 4.5% | 3.0% | 3.5% | 1.7% | 0.0% | 1.9% | 10.1% | 3.7% |
| | **57.3%** | **52.7%** | **18.2%** | **24.5%** | **39.4%** | **51.5%** | **65.7%** | **55.6%** | **71.3%** | **37.8%** | **45.8%** |
| **Other businesses** | | | | | | | | | | | |
| INFORMATION TECHNOLOGY | 5.7% | 13.5% | 71.5% | 46.0% | 0.8% | 2.5% | 0.0% | 0.0% | 0.0% | 7.2% | 20.4% |
| COMMUNICATION SERVICES | 20.0% | 2.7% | 2.3% | 5.9% | 1.8% | 10.3% | 6.8% | 11.5% | 10.2% | 9.3% | 9.5% |
| UTILITIES | 2.3% | 4.0% | 0.0% | 0.4% | 9.3% | 3.9% | 0.0% | 0.0% | 0.0% | 7.7% | 2.6% |
| INDUSTRIALS | 5.3% | 7.3% | 2.8% | 12.3% | 8.9% | 0.0% | 2.1% | 12.1% | 6.3% | 9.3% | 6.7% |
| REAL ESTATE | 2.9% | 0.6% | 0.2% | 0.0% | 0.0% | 0.8% | 2.3% | 2.8% | 0.0% | 4.4% | 1.7% |
| | **36.1%** | **28.1%** | **76.8%** | **64.6%** | **20.7%** | **17.5%** | **11.2%** | **26.5%** | **16.5%** | **37.8%** | **41.0%** |
| **TOTAL** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** |

*Source: RIMES, MSCI, Morgan Stanley Research*

*Data as of 25-Sep-2023*



Depuis 2005

### 3.2 Upside from global investors recognizing India's "fair" weighting.

The weighting of India in MSCI AC World index is only 1.66%, and in MSCI Emerging Markets Index 15.7% (as of 25th Sept. 2023). A good question to ask is why this weighting is so low and whether there is an investment opportunity due to this low weight itself?

We believe that the MSCI Indices are structurally flawed and therefore investors making decisions off these indices end up making sub-optimal decisions, and in India's case, by under-allocating to India. This will change over time, bringing foreign inflows into India, as the weight of India rises in MSCI indices and as investors move to actively allocate to the Indian opportunity.

Let us look at MSCI Emerging Markets Index and its constituents:

***Exhibit 14: Major Country Weights in MSCI Emerging Markets Index***

| Major Country Weights in MSCI EM (Emerging Markets) Index | | | | | |
|---|---|---|---|---|---|
| **Country** | **Weight %** | **Current Market Cap. (US$ Bn)** | **Free Float Market Cap. (US$ Bn)** | **GDP (US$ Bn 2022e)** | **Free Float % Market Cap.** |
| **CHINA** | 29.7% | 9,541 | 1,949 | 18,100 | 20.4% |
| **INDIA** | **15.7%** | **3,704** | **1,027** | **3,386** | **27.7%** |
| **TAIWAN** | 14.8% | 1,804 | 971 | 762 | 53.8% |
| **KOREA** | 12.4% | 1,731 | 813 | 1,665 | 47.0% |
| **BRAZIL** | 5.4% | 793 | 354 | 1,924 | 44.7% |
| **SAUDI ARABIA** | 4.1% | 2,976 | 266 | 1,108 | 8.9% |
| **SOUTH AFRICA** | 3.1% | 291 | 203 | 406 | 69.5% |
| **MEXICO** | 2.5% | 447 | 163 | 1,414 | 36.6% |
| **INDONESIA** | 2.0% | 670 | 131 | 1,319 | 19.6% |
| **THAILAND** | 1.9% | 511 | 125 | 536 | 24.5% |

*Source: RIMES, Bloomberg, IMF, Morgan Stanley Research*
*Data as of 25-Sep-2023*

We can see from the above table (data as of 25th Sept 2023) that India's weighting in MSCI Emerging Markets is not representative of its market capitalization or size of GDP:

- Taiwan's GDP is 22% of India's and its market cap. is approx. 49% of India's, but its weight in Index is almost the same as India's weight.
- Korea's GDP is 49% of India's and market cap. is 47% of India's, but it's weight in Index is 79% of India's weight.

The MSCI methodology in essence penalizes companies that grow without diluting shareholders and therefore are more likely to have a lower free float!

India's weight in indices is low because its free float factor is very low. The main reason for India's low free float factor is that founders own a large stake in their companies or because in some cases the companies have reached foreign ownership limits. In the latter case it is amusing that MSCI methodology removes the company from its indices if it reaches foreign ownership limit (i.e. when it is presumably a favorite of the foreign investor) leading some foreign investors to sell, and as they subsequently sell then MSCI looks to add the same company back in the indices (after a few quarters) as the company is then no longer at foreign ownership limit. We cannot imagine anyone other than a stockbroker benefiting from this regular change in constituents of index.

***"… A less obvious (but a more insidious) negative is how free float factor-based index hurts index investors as it artificially reduces the weight of good companies/countries."***

A less obvious (but a more insidious) negative is how free float factor-based index hurts index investors as it artificially reduces the weight of good companies/countries. It is generally good, capital efficient companies that end up with large insider ownership (as they do not need to dilute as they grow) but the index as a result assigns them a lower weight. By the same logic, companies where owners have been diluting their stakes are viewed positively by MSCI (for it will lead to increase in free float) although any bottom-up investor would view this dilution of stake as a negative development relative to companies that achieve the same level of growth and market capitalization without diluting their shareholders.

Has any investor ever invested in a country or company only because its free float factor is high? However, this is essentially what one does when investing in an index fund or a fund that invests off this benchmark. Due to a systematically flawed MSCI Index that gives too much weight to the free float factor, foreign funds do not invest on the basis of the size of the opportunity or the scale of the transformation of an economy but based on a non-economic free float calculation by an index provider.

The bottom line is that foreign investors have more capital invested in countries like Taiwan and Korea which cannot be justified by the scale of the opportunity. The size of opportunity and the expected transformation of India are much bigger and therefore investing in proportion to the free float rather than in proportion to the opportunity harms investors.

We expect this to change with time as more and more investors understand this issue.

# 4. Elimination Investing: Helios' unique investment philosophy

Our investment philosophy has its genesis in the first few years after Samir Arora moved back to India in 1993 to set up Alliance Capital's operations (an erstwhile Asset Management Company). Samir Arora was the CIO and Fund Manager for various schemes managed by Alliance Capital. Over subsequent years the investment philosophy has been further fine-tuned in light of Samir (and each of the senior team's) 25+ years of experience and learnings in the market. This investment philosophy is today ingrained across our entire investment team and across all our investment processes.

The past 25 years have proven to us the that the core tenets of our investment philosophy continue to be timeless and repeatable. These form the foundations of our investment processes that, we believe, have helped deliver consistent performance. This is evidenced in the track record of erstwhile Alliance Capital's funds when these were under Samir Arora's management, and over the past almost two decades of track record of funds managed by Helios Singapore. Hence, we do not take it lightly when we say investing with Helios is investing **"Har Term Ke Liye!"**

***"Helios' investment philosophy and process - "Har Term Ke Liye!"***

## 4.1 Core tenets of our investment philosophy:

The overarching tenets of our investment philosophy are:

1. **Invest in steps of 1-3 year terms:**

   We seek long term winners but invest for a series of 1-3 year terms.

   We believe it is easier to analyze the companies over shorter time frames of 1-3 years. Industry trends, disruption, company strengths, government policies, etc. are visualized more easily over such shorter horizons, and investing over such time frames allows us to adjust the portfolio and its positions as investment cases evolve.

   Few companies do very well over the long term. However, a large number of stocks do well, relative to the market, over shorter time frames of 1-3 years, which makes investing easier when implemented for such shorter time frames.

   We believe the long term is a series of 1-3 terms executed right.

2. **Pursue Elimination Investing approach utilizing out unique EI™ framework:**

   It is easier to know what is bad than to know what is good. Rejecting bad companies increases the chances of arriving at the good companies, reduces errors, and reduces cost of errors.

   Elimination Investing is a unique approach that uses 8 fundamental factors to eliminate (ex-ante) poor performers and narrow down to a buy list of "good" stocks that "Cannot Be Eliminated on Any Factor."

   Our research shows that even after rejecting stocks liberally and refusing to make trade-offs, there are plenty of good stocks still left to choose from.

3. **Avoid permanent loss of capital:**

   This is an overarching objective at every stage of the investment process, at stock level and at portfolio level. This is achieved by limiting leverage, respecting valuation, and screening out stocks with potential to permanently derate, stagnate or go to zero, using our EI™ framework.

4. ***Invest with Tailwinds:***

   *It is always better to invest with a tailwind, rather than be left fighting headwinds.*

   *We are fundamental bottom-up investors who believe an investing strategy must be cognizant of, adjust to and take advantage of changing dynamics of macroeconomics, market conditions, industry trends and thematic tailwinds.*

There are also other important beliefs that define our investment philosophy and process:

1. ***Deep Fundamental Research***

   **Fundamental research must underpin all stocks in Buy List.** We seek to conduct intensive, 360-degree, research with internal models and research reports. A good research process entails mentoring from seniors, sector specialization, and multiple levels of reviews on research output.

2. ***Knowledge Based Investing***

   **We seek and apply knowledge.** We believe that the real difference amongst investors is no longer information, it is knowledge! Accessing information through a 360-degree coverage of the space is important. How to interpret information and to put it in a consistent framework is even more important than the information itself.

3. ***Seek the Truth***

   **All information must be questioned.** This stands whether it comes from the market or managements.

4. ***Sensible Diversification over Concentration***

   **Diversification beats over-concentration**. No one knows everything, and it is impossible to know anything for certain beyond a point. It pays to not put one's eggs in too few baskets.

5. ***Risk Management is a Core Value***

   **Risk management in order to minimize losses is central to the entire investment process.** It allows for allows compounding over better times.

## 4.2 Our investment style and investment convictions – a discussion

### 4.1 Knowledge based investing – learning counts

With strong sell side coverage from 100s of brokers (local and international), multiple financial and business channels, quarterly results and conference calls, large number of conferences and management road shows and social media and blogs, most sophisticated market participants end up with more or less the same information. **The real difference between investors is no longer information, it is knowledge.** Accessing information through a 360-degree coverage of the space is important. How to interpret information and to put it in a consistent framework is far more important than the information itself.

> ***"… everyone has more or less the same information and the real difference between investors is no longer information, it is knowledge."***

It is here that the collective experience (and knowledge) of the investment professionals in our team counts the most, for as we all know "What you see depends on what you have seen". And we have seen a lot. We have made lots of investment mistakes in our long careers, but we do not make the same mistake too many times and try and make sure the cost of each mistake is small. Everyone has to pay the cost of education in markets, and we have more than paid our share in the past two decades.

### 4.2 Long term investing, but not LAZY investing

We are bottom-up long term investors but with a few twists. Our view is that the long term is in reality a series of short terms, even though we aim to invest for the long term. This means that even though we are willing to (and in practice do) hold many stocks for the long term, we evaluate them continuously to confirm that our original hypothesis in buying the stock is intact. ***And whilst we aim to be long term investors, we are NOT lazy investors.*** We also sell dispassionately when we have to.

Continuous bottom-up research work allows us to adjust as we move ahead in time. It also gives us the conviction to stick with our investment convictions when market prices move contrary to our positioning. Holding a performing stock for a long time is easier than holding a stock where the market really tests your conviction when the stock goes down a lot (could be for technical factors for example) or goes nowhere for several quarters/years. We have had many such experiences in our career and in most cases, we have backed our convictions (based of course on fully updated, real-time research) which has paid off for the long term.

### 4.3 Myth and reality of high conviction-based investing

We believe that "we own high conviction stocks" is one of the most overused statements of investment strategy/philosophy. In our view, decisions are not taken in this way in real life (and should not be taken either!). The reality is that one shows even higher conviction in things one DOES NOT pursue or rejects. In the investment world these are ideas one chooses NOT to invest in, as we explain below.

***"we own high conviction stocks" is one of the most overused statements of investment strategy/philosophy.***

If Mr. Buffett says that he does not invest in technology companies, that, in fact, is his highest conviction idea. He is so convinced of it that he does not see the need to investigate these companies any further, and therefore does not engage in follow up analysis or due diligence. He rejects them out of hand (more or less) because he has "high conviction" that these companies are not for him. In general, our higher conviction (rightly or wrongly) is in things we decide not to do. As we narrow down our options towards "what to do", we reject along the way other options where we have (higher) conviction that they are not for us. Conviction is higher in the paths we chose not to follow because those decisions were made before we chose the ultimate course. This is true of everything we do in life; in every decision we make.

This difference between what we think we do (i.e., choose something) and what we actually do (reject options available along the way to arrive at that final choice) is not just academic - this is real life. If our "higher conviction" is in ideas we reject, we need to ensure that there is a process that rejects ideas properly and synchronizes what we think we do with how decision making is actually done in real life.

Instead of conducting extra-detailed due diligence on all stocks in our broader universe to look for "reasons to buy", we work with a much higher conviction FIRST looking primarily for "reasons to eliminate" stocks based on our initial fundamental work, to arrive at a "**cannot be eliminated on any factor**" universe. It is on this short list of stocks that we undertake the most detailed work, and from which we look for stocks to ultimately buy. In practice, this process of investing leads us to a position where we are making choices from amongst a universe of good (and perhaps less good, but definitely not bad) stocks. In effect, we are minimising (if not fully eliminating) chances of failure.

### 4.3.1 Historical perspective – not many companies do very well in the long term!

Investing is not as easy as it looks.

Before one adopts an investment philosophy (or strategy) one needs to understand the weaknesses and strengths of other prevalent philosophies (and strategies) for it may not be necessary to develop a new philosophy if the existing ones work well.

All successful investors talk about how they made money "buying good companies and holding them for the long term". **Questions that arise are:**

1. ***How to identify good companies ahead of time?***
2. ***How to know what will happen in the long term?***

Classification of a company as a "good" company is normally done in hindsight when a company does well for a long time and is then labelled as a good company ("**Halo Effect**"). For example, if a bank (say XYZ Bank) has done well in the stock market for 20 years, it is normally shown as an example of how holding a good company over long term can lead to hefty returns, *without discussing* how one would have known 20 years ago that it is a good company and that it would perform well in the long term. Reality is that there would be tens of other examples of companies that would have been perceived as being "good" twenty years ago, but investing in them for the long term may have proved disastrous. History is indeed written by (and written on) the winners!

***The reality is that very few companies do well in the long-term and it is very difficult to identify these in advance***

The reality is that very few companies do well in the long-term and it is very difficult to identify these in advance. In fact, calling a potential investment a "long term" idea is itself a red flag. In most cases it means that the idea cannot be justified on valuations or current prospects, and one is being asked to rely on the, generally more hazy, long term outlook and potential. This does not mean that every "long term" idea should be rejected out of hand, but a clear understanding is needed of where exactly the investment fails on (say) "medium-term" and "shorter term" prospects and what assumptions are being used to arrive at the "long-term" prospects.

As a thumb rule, we should consider rejecting companies where we find the need to justify why these companies would do well over the long term based on an extrapolation of their long-historical track on key attributes e.g. "very long term" track record of growth of business or "very long term" tenure of quality management team. There is much more to a good investment case, and the investment case itself evolves in an ever-changing environment.

***Looking into the far future - a tough ask:***

Evaluating managements and companies over a long period of history in order to identify attributes that help predict the future is never an easy task and many formal detailed studies (that are much more detailed than what can be conducted by investors generally) have completely failed at this. For example, the famous New York Times bestseller book "**Built to Last**" (published in 1994) talked about successful habits of visionary companies by taking as a sample those companies that had massively outperformed the markets from 1926 through 1990. After lots of research and interviews, the authors identified, among others, the following "habits" of successful companies:

a) Clock building, not time telling.
b) No tyranny of the "or".
c) More than profits.
d) Big hairy audacious goals.
e) Home grown management, etc.

All these habits look and sound good and therefore one can try to find managements and companies with these habits. When the authors applied these factors to identify companies where management had these qualities, they came up with names like Motorola, Citi, Ford, GE, HP, Nordstrom, etc. which have done very poorly since then. Obviously, they could not identify the real wealth generators of the last 20-30 years like Amazon, Apple, Alphabet, Netflix, and Tesla for these companies did not even exist at that time. So much for identifying good managements for the purpose of long-term investing!

Similarly, the book "**Good to Great**", published in 2001, asked the question "Why some companies make the leap… and others don't". The authors employed a large number of researchers, studied more than 6,000 articles and generated more than 2,000 pages of interview transcripts and identified habits like "confront the brutal facts", "culture of discipline", and "Technology Accelerators" in successful companies. After this detailed study of the past, the authors came up with "great" companies with these characteristics, many of which have done very badly since then (Circuit City, Fannie Mae, Kimberly-Clark, Kroger, Nucor, Pitney Bowes, etc.).

The message is that it is not correct to study only successful companies to identify desirable management qualities for it is quite possible that unsuccessful companies also had the same management qualities. For example, someone might conclude that a successful new age company has done well because it shared ESOPs widely amongst its staff without realizing that many unsuccessful companies had done the same but still had poor outcomes.

Daniel Kahneman, Nobel Prize winner, in his book "**Thinking Fast and Slow**" states:

*"The basic message of Built to Last and other similar books is that good managerial practices can be identified and that good practices will be rewarded by good results. Both messages are overstated. The comparison of firms that have been more or less successful is to a significant extent a comparison between firms that have been more or less lucky."*

***Looking to the past - an equally tough ask:***

If we can't choose stocks by assessing the strengths of managements to manage the long term or by predicting growth rates of businesses long into the future, perhaps we can choose stocks by looking into their past. If we are looking at (say) past 10-year history to get comfortable with a stock, we have to take into account that strong returns may have been made in these companies because, inter alia,

a) *they were trading at much lower valuations at the start of the period;*
b) *did better than expectations;*
c) *were starting from a smaller base;*
d) *were in an environment with less competition; and*
e) *delivered strong performance due to both earnings' growth and re-rating.*

Not all these factors may still be valid looking forward!

Studying the past is important, but life would be very easy if all one needed to forecast the future was to study the past. Do note the widely used disclaimer: "**Past performance is not an indicator of future performance**".

In simple terms, the number of companies that do well in the long term are very few and therefore the odds of finding them in one's portfolio are very low.

Warren Buffett in his 2022 annual letter of Berkshire Hathaway says that "Our satisfactory results have been the product of about a dozen truly good decisions – that would be about one every five years..."

If the strike rate is so low even for Mr. Buffett, it makes sense for us to **not** bet on the strategy of simply looking for a few long-term winners and over-concentrating in these positions.

### 4.3.2 Investment horizon of 1-3 years at a time; analysing the markets.

Our investment philosophy dictates that we do something to make the odds of ending up with long term winners more favorable to us. We also need to reconcile our desire to see the long term with clarity, with the reality that it is very difficult to do so for anyone (including the management) beyond the next few years, if at all. Longer term winners normally surprise everyone - themselves, their managements and their investors - with their growth and success.

***Longer term winners normally surprise everyone - themselves, their managements and their investors - with their growth and success.***

We can improve our odds of taking the right decisions if we view the future as a series of "1 to 3 years" views. One can visualize industry trends / disruption / company strengths / govt. policies, etc. more easily over this horizon, rather than try to predict 20-year winners. This allows for course correction and minimises the intensity and duration of pain should things not go well. **Investing on "hope" that the long term works out is not a strategy!**

*Imagine you are being offered a deal where you can buy stakes in different businesses. You can buy the stake anytime or add to the stake anytime or reduce the stake anytime or eliminate the stake anytime at market prices. You also know (from the discussion above) that the base case reality is that only a handful of businesses compound wealth in a serious way over the long term.*

*With this background, why would anyone choose a structure where you divide your funds in only a few such investments, or buy your full share of the partnership at one go and then wait for the long term for things to develop. Although many companies do well in hindsight, these are a low percentage of all the companies in the investable universe, and companies that grow on to become giants over the long term can generally NOT be identified well in advance with a high degree of confidence.*

*Instead, if you look at the investments with a 1-3 year time horizon at a time, and buy a smaller stake in a slightly larger number of partnerships, and then increase/decrease your stakes as the future unfolds, you should end up much better off.*

We know that it is obvious that one has much better visibility over a 1-3 year time horizon than looking into the future 20 years ahead. However, something else very powerful happens as a bonus when you look at shorter time horizons of 1-3 years. The number of stocks that do very well (the quantum of their outperformance), relative to the market, increases dramatically over these shorter time periods. Since our endeavour is to build a portfolio of stocks that are likely to do better than the market, our probability of doing so also increases dramatically when we look at 1-3 year time horizons.

Since the Index return is the average return of the constituents (weighted by market capitalization), the number of stocks on the two sides of the average (index) return are more or less evenly balanced. To understand this better, let us see the performance of the constituents of S&P 500 and NSE 500 over time.

The exhibit below gives the distribution of returns for the top 250 best performing stocks of S&P 500 Index, year by year, over the past 20 calendar years. The last column gives the returns of the index in the calendar year. Second last column gives the number of stocks from the index that outperformed the index in the same year. It is easy to see that on average broadly half the stocks did better than the market each year. Even in years that had narrow breadth (say 2020), 168 stocks did better than the index whereas in other years where there was larger breadth between 203 and 290 stocks did better than the index.

**_Exhibit 14: Performance of 250 best performing stocks in the S&P 500 index, by year_**

| 1 YEAR DATA | S & P 500 INDEX MEMBERS | | | | | | |
|---|---|---|---|---|---|---|---|
| | 50th Best | 100th Best | 150th Best | 200th Best | 250th Best | # >Index | S&P 500 INDEX |
| 2003 | 88.1% | 61.7% | 47.2% | 38.2% | 31.2% | **258** | **28.7%** |
| 2004 | 46.0% | 32.9% | 24.0% | 17.6% | 12.9% | **264** | **10.9%** |
| 2005 | 39.9% | 27.3% | 16.1% | 9.1% | 4.7% | **245** | **4.9%** |
| 2006 | 42.3% | 31.0% | 24.1% | 18.7% | 14.4% | **234** | **15.8%** |
| 2007 | 38.3% | 23.7% | 14.5% | 5.9% | -1.2% | **203** | **5.6%** |
| 2008 | -8.3% | -18.3% | -26.7% | -33.4% | -39.8% | **229** | **-37.0%** |
| 2009 | 100.0% | 68.2% | 52.1% | 42.8% | 33.1% | **290** | **26.4%** |
| 2010 | 53.1% | 39.4% | 31.2% | 23.8% | 18.3% | **276** | **15.1%** |
| 2011 | 28.7% | 19.2% | 13.1% | 8.0% | -0.5% | **228** | **2.1%** |
| 2012 | 43.2% | 30.6% | 23.9% | 18.7% | 14.6% | **229** | **16.0%** |
| 2013 | 69.1% | 57.0% | 46.6% | 40.0% | 34.3% | **255** | **32.4%** |
| 2014 | 40.6% | 30.2% | 23.8% | 19.6% | 14.5% | **257** | **13.7%** |
| 2015 | 25.4% | 17.4% | 10.1% | 3.5% | -1.6% | **223** | **1.4%** |
| 2016 | 38.5% | 30.3% | 23.0% | 17.5% | 12.8% | **254** | **12.0%** |
| 2017 | 50.2% | 39.2% | 31.0% | 23.7% | 17.9% | **213** | **21.8%** |
| 2018 | 19.5% | 9.4% | 3.6% | -2.6% | -8.2% | **218** | **-4.4%** |
| 2019 | 57.6% | 45.6% | 39.8% | 33.7% | 29.1% | **227** | **31.5%** |
| 2020 | 43.7% | 30.9% | 22.4% | 14.1% | 8.1% | **168** | **18.4%** |
| 2021 | 62.4% | 49.4% | 41.1% | 33.3% | 26.6% | **234** | **28.7%** |
| 2022 | 21.9% | 8.9% | 0.0% | -6.9% | -13.9% | **283** | **-18.1%** |
| **Cumulative** | **129709.9%** | **19425.8%** | **4870.2%** | **1459.7%** | **432.2%** | **239** AVG | **547.7%** |

*Source: Bloomberg and Helios*

An interesting point to note in this data is that if approximately half the stocks outperform the market, then 40% of the stocks do even better and 30% (or 150 stocks) do really well (compared to the index), and the performance of top 20% (100 stocks) and top 10% (50 stocks) is just phenomenal (see also cumulative compounded performance in the last row).

There are many stocks therefore that do well in any year, and a smaller sub-set of them do extremely well. But if one could get the performance of even the 150$^{th}$ best performing stock of the year each year, it would be phenomenal outcome. The fact remains that we have not seen any equity strategy delivering performance (and certainly not with any level of consistency) that is anywhere close to the performance of the 150$^{th}$ best performing stock of the index each year.

***The fact remains that we have not seen any equity strategy delivering performance (and certainly not with any level of consistency) that is anywhere close to the performance of the 150th best performing stock of the index each year.***

A logical response to the above analysis would be that this somehow suggests that the whole portfolio should be changed every year, and that would be impractical to achieve. We are certainly not suggesting one does that. However, when you look at the data over cumulative 2 year or 3 year periods (see tables below), we see that one third of the stocks still continue to outperform the benchmark significantly, although the extent of outperformance comes down due to normalization of returns over the two year time frame, and even further on the three year time-frame.

Extending this analysis to longer timeframes, one would note that approximately 30% of companies continue do much better than the overall market over all periods, although their extent of out-performance declines over longer time horizons. This is because although companies may significantly out-perform the overall market over some periods, reversion to mean (including factor and sector reversals) and general inability of many companies to scale up successfully means the same level of high annual out-performance logged over shorter timeframes is impossible to maintain over longer periods of time.

For our purposes, the important point to note is that a large number of companies outperform over 1-3 year periods, and many outperform by quite a margin, and this is where we would like as much as possible of our long book to be.

***Exhibit 15: Performance of 250 best performing stocks in the S&P 500 index, over successive two-year periods***

| 2 YEAR DATA | S & P 500 INDEX MEMBERS | | | | | | |
|---|---|---|---|---|---|---|---|
| | 50th Best | 100th Best | 150th Best | 200th Best | 250th Best | # >Index | S&P 500 INDEX |
| 2003 & 2004 | 82.5% | 50.2% | 38.2% | 25.7% | 18.1% | **255** | **42.7%** |
| 2005 & 2006 | 64.2% | 49.0% | 36.7% | 26.6% | 20.6% | **241** | **21.5%** |
| 2007 & 2008 | -0.7% | -11.7% | -22.0% | -30.3% | -39.8% | **220** | **-33.5%** |
| 2009 & 2010 | 161.9% | 110.7% | 89.7% | 70.3% | 53.6% | **281** | **45.5%** |
| 2011 & 2012 | 55.6% | 40.8% | 31.3% | 22.4% | 15.2% | **228** | **18.4%** |
| 2013 & 2014 | 105.1% | 83.4% | 71.9% | 57.8% | 48.5% | **237** | **50.5%** |
| 2015 & 2016 | 42.8% | 30.6% | 22.4% | 16.2% | 9.7% | **218** | **13.5%** |
| 2017 & 2018 | 50.3% | 35.2% | 25.5% | 15.7% | 5.2% | **194** | **16.5%** |
| 2019 & 2020 | 102.3% | 79.5% | 62.1% | 48.5% | 33.7% | **172** | **55.7%** |
| 2021 & 2022 | 62.3% | 41.1% | 27.7% | 18.2% | 9.9% | **274** | **5.4%** |
| **Cumulative** | **17437.4%** | **4704.6%** | **1907.0%** | **761.8%** | **281.8%** | **229** AVG | **547.7%** |

*Source: Bloomberg and Helios*

***Exhibit 16: Performance of 250 best performing stocks in the S&P 500 index, over successive three-year periods***

| 3 YEAR DATA | S & P 500 INDEX MEMBERS | | | | | | |
|---|---|---|---|---|---|---|---|
| | 50th Best | 100th Best | 150th Best | 200th Best | 250th Best | # >Index | S&P 500 INDEX |
| 2003, 2004 & 2005 | 186.2% | 121.8% | 90.9% | 67.3% | 51.3% | **251** | **49.7%** |
| 2006, 2007 & 2008 | 18.8% | 4.4% | -9.9% | -22.7% | -37.2% | **200** | **-23.0%** |
| 2009, 2010 & 2011 | 167.2% | 117.3% | 90.8% | 71.8% | 50.1% | **257** | **48.6%** |
| 2012, 2013 & 2014 | 161.4% | 119.5% | 99.8% | 86.0% | 73.0% | **247** | **74.5%** |
| 2015, 2016 & 2017 | 87.1% | 65.1% | 50.9% | 38.9% | 24.9% | **202** | **38.3%** |
| 2018, 2019 & 2020 | 63.1% | 44.8% | 34.2% | 24.6% | 16.2% | **148** | **48.8%** |
| * 2021 & 2022 | 62.3% | 41.1% | 27.7% | 18.2% | 9.9% | **274** | **5.4%** |
| **Cumulative** | **11662.63%** | **3623.1%** | **1596.3%** | **745.0%** | **293.9%** | **218** AVG | **547.7%** |

*Source: Bloomberg and Helios*

Similar observations can be seen from the three tables below for NSE 500 stocks: i) one third of the index constituents significantly outperform the benchmark over one year, two year or three-year periods; and ii) the amount of outperformance is lower the longer the time period.

### Exhibit 17: Performance of 250 best performing stocks in the NSE 500 index, by year

| 1 YEAR DATA | NSE500 INDEX MEMBERS | | | | | | |
|---|---|---|---|---|---|---|---|
| | 50th Best | 100th Best | 150th Best | 200th Best | 250th Best | # >Index | NSE 500 INDEX |
| 2003 | 255.6% | 197.9% | 152.4% | 120.6% | 94.7% | **228** | **104.8%** |
| 2004 | 99.8% | 73.7% | 45.8% | 32.7% | 23.3% | **264** | **21.1%** |
| 2005 | 149.7% | 95.2% | 69.8% | 49.5% | 35.8% | **236** | **38.8%** |
| 2006 | 88.8% | 52.7% | 34.0% | 19.4% | 5.6% | **143** | **36.2%** |
| 2007 | 186.1% | 117.1% | 86.6% | 62.7% | 47.6% | **194** | **64.6%** |
| 2008 | -32.0% | -46.3% | -55.4% | -61.6% | -66.0% | **157** | **-56.5%** |
| 2009 | 254.4% | 194.4% | 163.3% | 131.6% | 105.0% | **297** | **91.1%** |
| 2010 | 79.0% | 54.8% | 38.2% | 26.0% | 16.9% | **257** | **15.7%** |
| 2011 | 5.3% | -9.0% | -17.3% | -25.5% | -34.4% | **204** | **-26.2%** |
| 2012 | 97.1% | 72.8% | 55.3% | 43.2% | 31.5% | **235** | **34.1%** |
| 2013 | 40.6% | 18.7% | 5.8% | -2.5% | -9.9% | **153** | **5.4%** |
| 2014 | 153.9% | 102.0% | 83.3% | 62.9% | 44.8% | **274** | **40.0%** |
| 2015 | 46.4% | 30.4% | 18.1% | 10.0% | 2.2% | **260** | **0.6%** |
| 2016 | 46.6% | 28.9% | 17.2% | 9.0% | 1.2% | **214** | **5.3%** |
| 2017 | 114.6% | 79.6% | 64.0% | 51.6% | 39.6% | **260** | **37.7%** |
| 2018 | 21.1% | 1.6% | -7.9% | -15.8% | -21.9% | **120** | **-2.1%** |
| 2019 | 40.0% | 18.7% | 7.2% | -1.1% | -7.1% | **141** | **9.0%** |
| 2020 | 73.7% | 52.7% | 35.7% | 25.4% | 14.1% | **231** | **18.3%** |
| 2021 | 119.7% | 85.0% | 63.9% | 49.2% | 38.3% | **279** | **31.8%** |
| 2022 | 51.8% | 32.5% | 16.3% | 7.0% | -2.3% | **213** | **4.4%** |
| **Cumulative** | **13860152.3%** | **420648.4%** | **36521.4%** | **4791.1%** | **654.5%** | **218** Average | **2645.9%** |

*Source: Bloomberg and Helios*

### Exhibit 18: Performance of 250 best performing stocks in the NSE 500 index, over successive two-year periods

| 2 YEAR DATA | NSE500 INDEX MEMBERS | | | | | | |
|---|---|---|---|---|---|---|---|
| | 50th Best | 100th Best | 150th Best | 200th Best | 250th Best | # >Index | NSE500 INDEX |
| 2003 & 2004 | 473.2% | 343.1% | 263.5% | 197.2% | 142.3% | **241** | **148.1%** |
| 2005 & 2006 | 252.2% | 157.1% | 103.3% | 73.0% | 48.3% | **172** | **89.0%** |
| 2007 & 2008 | 11.0% | -7.0% | -21.7% | -36.7% | -46.5% | **172** | **-28.5%** |
| 2009 & 2010 | 349.4% | 277.1% | 229.3% | 187.0% | 151.8% | **305** | **121.1%** |
| 2011 & 2012 | 58.8% | 31.8% | 11.1% | -4.1% | -15.6% | **191** | **-1.0%** |
| 2013 & 2014 | 158.9% | 112.1% | 79.7% | 57.3% | 35.7% | **221** | **47.5%** |
| 2015 & 2016 | 79.6% | 51.5% | 29.1% | 16.1% | 3.4% | **238** | **5.9%** |
| 2017 & 2018 | 87.9% | 57.9% | 41.9% | 25.9% | 11.1% | **168** | **34.8%** |
| 2019 & 2020 | 90.8% | 54.6% | 34.0% | 17.8% | 4.5% | **162** | **29.0%** |
| 2021 & 2022 | 160.2% | 108.9% | 80.8% | 60.8% | 42.9% | **264** | **37.7%** |
| **Cumulative** | **693970.14%** | **86145.2%** | **16770.4%** | **3801.0%** | **850.4%** | **210** AVG | **2645.9%** |

*Source: Bloomberg and Helios*

### *Exhibit 19: Performance of 250 best performing stocks in the NSE 500 index, over successive three-year periods*

| 3 YEAR DATA | NSE500 INDEX MEMBERS | | | | | | |
|---|---|---|---|---|---|---|---|
| | 50th Best | 100th Best | 150th Best | 200th Best | 250th Best | # >Index | NSE 500 INDEX |
| 2003, 2004 & 2005 | 916.4% | 568.2% | 437.5% | 329.2% | 250.7% | 251 | 244.4% |
| 2006, 2007 & 2008 | 35.0% | 7.0% | -13.7% | -27.2% | -41.1% | 116 | -2.6% |
| 2009, 2010 & 2011 | 305.6% | 194.3% | 132.3% | 98.8% | 68.2% | 257 | 63.2% |
| 2012, 2013 & 2014 | 322.9% | 194.4% | 142.6% | 109.9% | 80.8% | 221 | 97.8% |
| 2015, 2016 & 2017 | 224.1% | 132.3% | 104.1% | 69.1% | 48.1% | 254 | 45.7% |
| 2018, 2019 & 2020 | 102.7% | 34.3% | 9.8% | -5.7% | -22.9% | 110 | 26.3% |
| * 2021 & 2022 | 160.2% | 108.9% | 80.8% | 60.8% | 42.9% | 264 | 37.7% |
| Cumulative | 402174.78% | 40292.6% | 10492.3% | 3242.2% | 925.8% | 210 AVG | 2645.9% |

*Source: Bloomberg and Helios*

Just like the top performing one third of stocks in an index do really well over any time period, the bottom one third of stocks do really badly and significantly underperform the index (see table below). In our view, it is comparatively more important to make sure that the book is NOT populated with stocks that end up underperforming the market, and most certainly not with stocks that feature amongst the bottom third of the market. We believe that the Helios approach of Elimination Investing allows us to have a disproportionately fewer number of stocks in the underperforming half (and more relevantly, the bottom third) of the market, which should help skew returns to the upside versus the benchmark.

### *Exhibit 19: Performance of 250 worst performing stocks in the NSE 500 index, by year*

| 1 YEAR DATA | NSE 500 INDEX MEMBERS | | | | | |
|---|---|---|---|---|---|---|
| | 300th Best | 350th Best | 400th Best | 450th Best | # >Index | NSE 500 INDEX |
| 2003 | -3.6% | 36.3% | -5.2% | | 228 | 104.8% |
| 2004 | -3.6% | 0.4% | -13.7% | | 264 | 21.1% |
| 2005 | -3.6% | 6.6% | -8.2% | -28.5% | 236 | 38.8% |
| 2006 | -3.6% | -13.4% | -24.3% | -38.2% | 143 | 36.2% |
| 2007 | 31.6% | 15.4% | 1.3% | -11.8% | 194 | 64.6% |
| 2008 | -70.1% | -74.5% | -79.1% | -83.4% | 157 | -56.5% |
| 2009 | 89.9% | 75.8% | 60.2% | 32.6% | 297 | 91.1% |
| 2010 | 6.6% | -4.3% | -14.1% | -27.9% | 257 | 15.7% |
| 2011 | -41.4% | -49.6% | -57.2% | -66.7% | 204 | -26.2% |
| 2012 | 21.5% | 11.6% | 3.1% | -9.8% | 235 | 34.1% |
| 2013 | -17.0% | -24.3% | -36.6% | -44.8% | 153 | 5.4% |
| 2014 | 32.7% | 20.0% | 7.4% | -8.6% | 274 | 40.0% |
| 2015 | -5.5% | -14.3% | -23.9% | -37.5% | 260 | 0.6% |
| 2016 | -5.2% | -13.9% | -23.3% | -35.3% | 214 | 5.3% |
| 2017 | 30.9% | 20.7% | 10.5% | -4.9% | 260 | 37.7% |
| 2018 | -28.9% | -35.2% | -43.0% | -55.5% | 120 | -2.1% |
| 2019 | -14.7% | -24.4% | -33.3% | -50.6% | 141 | 9.0% |
| 2020 | 4.6% | -3.6% | -13.7% | -23.4% | 231 | 18.3% |
| 2021 | 25.7% | 15.8% | 2.4% | -8.0% | 279 | 31.8% |
| 2022 | -10.2% | -16.4% | -24.3% | -34.6% | 213 | 4.4% |
| Cumulative | -54.6% | -87.0% | -99.2% | -100.0% | 218 Average | 2645.9% |

*Source: Bloomberg and Helios. Note: Price data not available for certain stocks in Bloomberg, in particular over 2003 and 2004, as a result of which the numbers for the 450th best stocks are not shown.*

The other great thing about India when compared to the US market is that India tends to be a market with greater dispersion and volatility in returns (see data above), which allows for potentially higher returns from the Indian market so long as one has the process that successfully eliminates exposure to the big underperformers and populates most of the portfolio with stocks that outperform to varied degrees.

### 4.3.3 ELIMINATION INVESTING or EI™ (the "Helios" approach)

**Key points to note:**

a) Over a 1-3 year type period, approximately forty odd percent of the stocks in the index do better than the index. In the longer term this statistic becomes difficult to analyse as the index itself goes through many changes;

b) Approximately 1/3rd of the stocks do really well, compared to the market, so that in most cases even owning the last stock from the top 1/3rd list would add to an investor's returns;

c) Approximately 1/3rd of the market does really badly relative to the market.

Understanding the market structure as shown above, one can more easily arrive at the strategy one should follow to invest profitably in the markets. The following are the salient points and observations about this strategy:

a) The first goal is to have as much of the portfolio in the outperforming part of the market over a 1–3-year time horizon. This is difficult as it requires (amongst other things) a proven process, considerable market experience and deep fundamental work. However, this is not as difficult as finding 20-year winners. As we saw earlier, approximately 40 odd percent of stocks outperform the market, over any 1, 2 or 3 year period i.e. plenty of stocks out-perform.

*b)* It is easier to know what is bad than to know what is good. It is also our contention that finding bad stocks is easier than finding good stocks as a single factor may make a stock "bad" but a host of positive factors may not be enough to declare a stock as "good".

   *For example, if the management of a company is known to be short sighted or conflicted (both red flags) it is enough to remove the stock from contention but a management being far sighted or free from conflicts is not enough of an individual factor that can make the stock "good."*

c) Having observed and analyzed why stocks underperform or end up in the bottom third of the market in any given year, we have identified a list of eight fundamental factors that have tended to be triggers for this underperformance. These factors are used by Helios to eliminate stocks to arrive at a Buy List of stocks that Cannot be Eliminated on any Factor.

d) Knowing that a large number of stocks do better than the market, we can be liberal in eliminating stocks: *e.g. if a company is good but expensive, we will eliminate it for being expensive, and if it has poor management but cheap valuation we will eliminate it for its management quality.*

   **We believe we do not need to do trade-offs between factors. One "bad" factor is enough to veto the stock since the investment universe is big enough for us to eliminate stocks liberally.**

e) Starting the investment process by first trying to eliminate ideas makes our final potential investment pool "good" to start with. This is not as easy to achieve as it sounds, as markets (and life) do not always offer black and white choices, and the collective wisdom and past experience of our entire investment team (led by the lead analyst) is required and utilised by us to eliminate stocks.

f) We believe that there is a lot of value in differentiating between good and bad stocks but not so much value (and success in monetary terms) in differentiating between two good stocks (particularly if they are in different sectors and therefore are driven by different dynamics and cannot be compared directly - though we still need to differentiate amongst them as part of our process).

   The main point is that to overly differentiate between good and good (particularly in different attractive sectors) is many times merely a theoretical exercise, often subject to too much randomness and forced selection, and brings relatively lower incremental benefits in performance terms.

g) Since 1/3rd of the market does very poorly, the easiest first step is to try and reduce the number of such stocks from your short-listed universe (and therefore portfolio) or essentially reduce the "errors" and the "cost of errors".

h) We are not unique in the way we think even though we thought of it independently. In his book "**Skin in the Game**" Nassim Nicholas Taleb says "We know with much more clarity what is bad than what is good" and that "via negativa" (acting by removing) is more powerful and less error-prone than "via positiva" (acting by addition)".

***In summary,*** *a large part of the market (over 40 percent typically) does better than the market due simply to the fact that the market is an average of the same pool of companies.*

*1/3rd of the universe does significantly better than the market over 1, 2 or 3 years periods but most of these outperformers are not able to sustain this level of outperformance over multiple years and decades. Not only are the long-term outperformers very few but it is also difficult to assess long term potential of companies and managements as "No one knows everything, and it is impossible to know anything for certain beyond a point". In other words, no one knows everything, and it is in fact impossible to know everything, or be confident that one knows everything, in particular as we extend the time horizon into the future. That is why buying stocks with a very long-term view is difficult and one has to be more lucky than smart to get it right consistently.*

*The easier and the correct way is to look at stocks with a 1-3 year rolling view. Over 1 to 3 years, the probability of getting stocks on the outperforming side is much higher and over this period one can assess the management/strategy/environment/financials more easily. If the company continues to do well and is expected to do well there is no reason to NOT continue to hold the company for years, but this is always done with a 1–3-year type view at a time.*

*We know that if we have a randomly selected portfolio of (say) 50 companies from the index, we can expect 30% of companies to do very well relative to index and 30% of companies to do fairly badly, over time, as we have seen in the tables above on S&P500 and NSE500. Our endeavor is to have a portfolio in which the number of stocks that do well can be increased and the number of stocks that do badly can be reduced. If we can end up with a portfolio which has more "good" stocks or at the very minimum fewer "bad" stocks than the market, a large part of our job (of trying to outperform the market) is done.*

*We believe that this is the best way to invest in order to reduce "errors" and "costs of errors" and be able to outperform in a consistent and repeatable manner.*

### 4.3.4 Implementing the Helios Elimination Investing approach.

As discussed above, we believe that in markets "What to do" comes after knowing "What not to do". We believe that reducing errors and the cost of errors is an important first step in building a portfolio. Our philosophy of Elimination based Investing/Rejecting Stocks based on an identified list of fundamental factors helps us achieve the same.

We have identified eight factors that are ex-ante most likely to lead to underperformance of any stock over the next 1-3 years. We have found that the presence of even one of these fundamental factors can lead to a stock underperforming the market or faring poorly. It is not necessary that such stocks will do badly each year (there may be factor and sector reversals at play), but if any of these factors are negative it typically pays (sooner or later) to avoid such companies.

The factors that we have identified are:

***Permanent-type rejection factors:***

1. *Bad theme (limited size of opportunity)*
2. *Unfavourable industry dynamics*
3. *Potential for disruption*
4. *Chinks/weakness in management / background / strategy*
5. *Poor corporate governance*
6. *Low quality accounting*

***Temporary-type rejection factors:***

1. *Negative medium-term triggers (in most cases projected financial performance)*
2. *Unreasonably high valuations*

The first 6 factors are more permanent in nature, whereas factors 7 and 8 are related more to results, price, valuation etc.

The elimination process works as follows:

a) Each company is rated on each of the factors above **as "Bad", "Not Bad"** or **"Good"**

b) If a company is classified as **"Bad"** on even one of the top 6 factors, it will be rejected and put in the **"Not Willing to Buy Bucket"**. This is akin to a permanent rejection

c) If a company passes the top 6 factors but ranks **"Bad"** on any of factors 7 or 8, it gets rejected and enters the **"Willing to Buy, but Not Now"** list

d) The investable long companies therefore **must be** ranked **"Good"** or **"Not Bad"** on each of the 8 factors

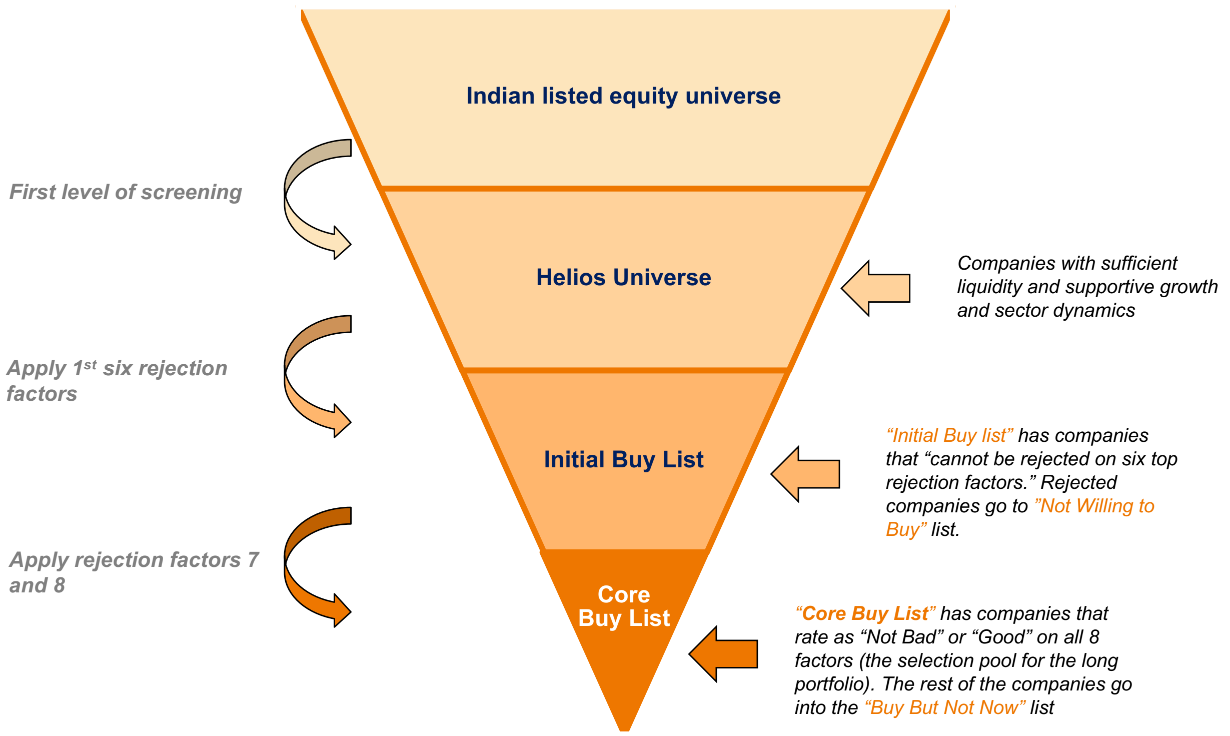
e) Very rarely does any company have all 8 factors classified as **"Good".** Therefore, we will accept companies that rate **"Not Bad"** on some factors

   *e.g., an exceptional company that ranks **"Good"** on all factors other than valuation, on which it ranks **Not Bad** i.e., its valuation is not so high that it gets rejected on the "unreasonably high valuation" factor*

f) If a factor ranks as **"Not Bad"** as opposed to "**Good,"** in practice it means that the factor is not the main influencer in the ultimate decision to buy or not buy

g) There is no trade off amongst factors. Each factor is like a Veto if the rank is **"Bad".**

Pictorially, the process of narrowing down to the core buy list of companies that "cannot be rejected on any factor" works as follows:




Running alongside the above process is a parallel process that ranks sectors as 1, 2 or 3 (team effort) and companies within each sector / area of coverage of analysts as 1, 2 or 3 (ranked by analyst in conjunction with head of research). For reference, 1 is the best and 3 the lowest rating. It would be normal to assume as that if a company rated 1 and 1 along this methodology this would tend to show up in the Core Buy List using the Elimination methodology.

In his book "**Seeking Wisdom: From Darwin to Munger**" the author Peter Bevelin quotes Munger "*It is remarkable how much long-term advantage people like us have gotten by trying to be consistently not stupid, instead of trying to be very intelligent."* Our Elimination based methodology is fully aligned with this statement.

The four steps of the Helios investment process up to this point can be summarised as follows:

1. **Idea Generation:** This entails ongoing coverage of our universe of companies comprising companies with sufficient liquidity and supportive growth and sector dynamics, including companies in new growth areas. New ideas can come from analysis of quantitative screens, company meetings, broker conferences, broker research, peer activity, supply chain analysis and conversations with industry experts. New ideas are discussed within the research team as well as in the Daily Investment Calls that include the full senior investment team and the analysts.

2. **Initial Fundamental Research:** Ongoing research activity is maintained on companies under coverage and research is conducted on new ideas through a process of industry analysis, company meetings, channel checks, and conversations with industry experts. Analysts rate all companies under coverage on each of the eight

Elimination Factors and rank each company under their coverage on a rating scale of 1 (highest), 2 or 3 (lowest). Research reports and models are prepared as appropriate.

3. **Rejection Based Screening:** Based on the ratings on the eight Elimination Factors, the investment universe is reduced to a shorter list of companies on the Initial Buy List (using the first six elimination factors) and then further reduced to a short list of companies in the Core Buy List (using the last two elimination factors). The ratings are implemented by the analysts in conjunction with the Head of Research, although the collective experience and knowledge of the broader investment team is brought to bear into the process, as appropriate (the Helios senior investment team each brings over 25 plus years of experience and accumulated knowledge of companies and markets).

4. **Deep Dive Research:** The companies on the Core Buy List (as well as many of the companies on the Initial Buy List but not on the Core Buy List) are subject of deep fundamental research that entails preparation of financial models and research notes, as well as ESG analysis and price targets. The Head of Research is the first level of challenge for the analysts. The research team is also open to information and feedback from the various Senior Investment Team Members to whom the research is made available in our Daily Investment Meetings, which we believe provides a second level of challenge to in the research process.

The next two steps in our investment process, Portfolio Construction and Risk Management, are discussed in the next section.

# 5. Portfolio Construction and Risk Management

***Turn the advantage to the market developed in research into a bigger advantage through astute portfolio construction***

We believe our fundamental research and our Elimination Investing approach gives us an edge over the market. We aim to convert that into a larger and more sustained advantage through astute portfolio construction. This entails the answering the following questions:

1. Do we have the right level of diversification, and avoidance of over-concentration in positions, pockets and clusters of risks?

2. Do we have an all-weather portfolio that we have a high confidence will deliver excess-returns over the cycle and across different market environments?

3. Does the portfolio have the right distribution of names across different stages of growth and delivery of returns i.e. some that are delivering well and some that are beginning to get to the stage where these will be delivering well?

4. Are we focused on pro-actively minimizing any laziness in the portfolio i.e. are we dispassionately rotating out of names where return expectations are now lower?

**Bar-bell approach to portfolio construction:**

The portfolio is constructed using a bar-bell approach with two kinds of stocks:

***1) "Good Stocks" or Stocks that offer "High confidence in reasonable returns":***

i) These are stocks where the confidence is high due to proven track record and good history and quality of management. However, the market is also aware of these factors, and the main factors we have to focus on are future growth and the valuations we are willing to pay for these "already discovered" stocks.

ii) This group has higher quality, consistently performing companies with clear strengths (moat), size of opportunity and high visibility in earnings.

iii) We do not expect these companies to get (further) re-rated but are happy with their expected growth for the next few years.

iv) We sell these stocks if valuations become too high or if there are some fundamental changes which make us reconsider our case for the company.

v) These companies comprise the lower turnover part of the long book.

vi) Differentiation for these stocks versus peers comes mainly from timing of buy/sell and sizing.

vii) We normally strive for 40-60% of our portfolio to be in such companies with approx. 3% to 7% per position.

***2) "Emerging Good Stocks" or Stocks that offer "reasonable confidence in high returns"***

i) These are companies where we expect higher returns from a combination of earlier discovery (or re-discovery) of stock and re-rating of company if it delivers on its potential.

ii) Some of these stocks are mid-caps (sometimes small caps) but they could also be large cap companies where we see trigger for sustained recovery or re-discovery by market.

iii) This second group of stocks has potential to offer significant alpha whereas the first group offers smaller, but more consistent alpha i.e. the first group has higher certainty of alpha.

iv) These stocks comprise the more active part of the long book.

v) Differentiation vs. peers for these stocks is via early discovery or timing of buy/sell and sizing.

vi) We normally expect to have between 40-60% of the portfolio in such companies, with average initial weight of 1.5% to 3% per name.

We believe one should have the wisdom and humility to never label a company as "high confidence in high return"! This is the zone where a lot of mistakes happen.

**We reject a concentrated portfolio strategy (owning 10-15 stocks) for a number of reasons:**

i) By the time one develops enough conviction to have a very high allocation to a stock (and concentrated portfolios have high allocations per position), one would typically have missed the larger part of the appreciation in most such stocks. For most investors, consistent and strong performance of the stock is itself one source of conviction, and by the time conviction develops, a lot of the performance is behind them.

ii) We only hear of winners that have followed such concentrated strategies, but not of the many investors that happen to mistakenly concentrate on the wrong stocks, and in effect disappear from the industry. Therefore, the perceived success of this strategy is much higher than its actual success due to "survivorship bias," as the winners/survivors distort the picture about actual returns realized from concentrated strategies.

iii) We know that a number of companies (approx. 30%) do really well over any period (relative to market). Placing smaller bets of 1.5% to 3% on a larger number of "well selected" stocks allows one to improve the odds of hitting it big without the accompanying downside if one or more bets go wrong.

iv) Even if some funds are concentrated, investors in such funds are rarely so. This is because investors rarely put their entire allocation in only one concentrated fund, whatever be their level of conviction about concentrated strategies. Investing in concentrated strategies may on the face of it reduce the obvious problem of look-through diversification at the end of the investor, but it also reduces the odds of overall success.

Knowing that many stocks do well each year (but not exactly knowing whose turn it is next), we are comfortable holding a well populated basket of well selected stocks at any point of time. Our bet is that if we choose these stocks from attractive themes/sectors, reject what we don’t like and then work to arrive at BUY list (that cannot be rejected on any factor) from which we select stocks, we have a fair shot at outperforming consistently, and by a margin.

We expect to have 7-10 new stocks each year that are then held for 1-3 years, while another 10-15 stocks are likely to be held for very long time. The stocks that will be held for the long term are not identified in advance as such, but if the company and the stock continues to do well there will be no reason to not hold that company/stock for a longer period of time.

We believe, our portfolio mix of “high confidence in reasonable returns” and “reasonable confidence in high returns” companies will help us deliver consistent performance over the years, cycles and phases of the market, without taking excessive idiosyncratic risk that comes with concentrated portfolios (especially where higher risk positions are sized aggressively).

We have been investing in India since the early 1990s (at Helios and prior to Helios). Over this period, we have seen hundreds of companies rise and fall, and hundreds disappear due to liberalization and globalization. We believe we have done well across nearly all market cycles and periods primarily because we refused to get carried away by our confidence in our stock picking abilities and always had a well-constructed, diversified portfolio of well-selected companies. We are also helped by the fact that we believe in investing where there is tailwind, and most certainly do not wish to be fighting headwinds.

**Sell discipline:**

Our research process is continuous and thorough and takes a 360-degree approach to a company’s ecosystem. It entails detailed fundamental analysis, and even though we invest in a series of 1–3-year time horizons, we pay attention to all news-flow, corporate developments and quarterly earnings announcements. We aim to be dispassionate, research oriented, and knowledge based in our holding of companies and in the sell discipline.

As such we would trim or sell our holdings were we to be confronted with the following:

a) Deterioration in fundamentals or unexpected negative development – position will normally be sold to zero.

b) Stock significantly outperforms underlying earnings growth over an extended period (i.e., reducing upside to price target) – weight would be trimmed along the way, and/or stock sold completely.

c) More attractive opportunities arise elsewhere – weight would be trimmed, or stock sold.

d) Risk control or stock near/at risk limits – stock would be sold or trimmed.

We believe high valuations are acceptable up to a point for quality companies with structural growth, but we do not believe in "Buy/Hold at any valuation”.

**Risk Management:**

Risk management is embedded throughout the investment process. In fact, our investment philosophy (i.e. Elimination Investing) and research process are geared towards minimising downside risks, and, in particular, avoiding situations that can cause permanent loss of capital.

In our analysis of companies, the Helios research team maintains a keen focus on assessment of downside risks versus upside expectations.

Some of the main features of the Helios risk management process are:

a) monitoring of position sizes/beta, sector, market cap and liquidity risks,

b) ongoing review of stock fundamentals, thesis, price targets, and upside to price targets,

c) questioning of stale positions, and

d) investigations, thesis review and action (as required) upon unusual price movements.

All portfolio drawdowns are evaluated and may trigger exposure adjustments and reshuffle of positions/sectors.

Helios has dedicated risk management personnel and compliance officers independent of the investment team, that provide another level of checks and balances.