Q4CY24 - Second Investor Letter

Oct - Dec 2024

SAURABH KHANDELWAL
JUL 01, 2025

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Dear Investors,

A very happy and prosperous New Year to you and your loved ones. We look forward to another year of growth in India amidst the cooling of geopolitical tensions globally.

Over the past quarter, we have navigated a dynamic market landscape where it was easy to be fooled into excesses on both sides of the spectrum - belief in the strength of the Indian story, or despondency of stretched valuations not being supported by fundamentals. The truth lies somewhere in between, and the value of equanimity is tested thoroughly. We believe it is important to remain dispassionate and patient through this period.

Our Outlook for the year

The new year is a time for reflection, planning, and developing an outlook for the year ahead. In that spirit, we would like to lay out our thoughts:

- *Change in leadership in the US is likely to de-escalate tensions*: As President-elect Donald Trump follows a US-first policy, there is likely an easing of geopolitical tensions especially Ukraine – Russia and the Middle East in the short term. However, the likelihood of trade wars and currency volatility, especially for developing economies, will go up significantly
- *Aggressive reduction in Government size likely to shore up US markets:* Inspired by the Argentinian success in reducing fiscal deficit through reducing the expenditure of the government, Trump has already announced the setting up of the Department of Governmental Efficiency led by the businessmen Elon Musk and Vivek Ramaswamy. Initial success in this domain is likely to cause a rally in the US equity markets Initial success in this domain is likely to cause a rally in the US equity markets
- *India continues to be resilient:* India should continue to display macroeconomic resilience this year. Key indicators such as the current account deficit, fiscal deficit, and inflation should stay under control, positioning the economy for sustainable growth for the next few years

Our view on the Indian Economy and Stock Market

GDP growth has recently slowed down due to decreased government and consumer spending. We believe this trend is cyclical and will improve in the coming quarters.

We previously discussed the Buffett Factor, or the market capitalization to GDP ratio, which compares the value of publicly traded companies in a country to its economic output. Warren Buffett popularized this measure, suggesting it can indicate whether the market is overvalued or undervalued. In India, the ratio currently exceeds 115%, signaling potential overvaluation and the risk of falling prices if company earnings don't meet expectations. Smaller and mid-sized companies seem more overvalued than larger ones.

The Indian stock market has shown resilience in recent years, despite global economic uncertainties. The broader market (Nifty 50) showed returns of 8.8% for CY24. The index was mostly bullish for the first 3 quarters reaching an all-time high of 26,277 in September, but then correcting nearly 9% in the last quarter on the back of selling by foreign investors primarily. The new year will be challenging as pockets of overvaluation, especially in small and mid-caps have been created because of the robust returns of more than 220% in those indices in the past 5 years, of which 24% came this year.

This year should see a return to fundamentals as investors start focusing on earnings growth and intrinsic value again. Pockets that underperformed this year like FMCG and private banks are likely to outperform this year as they offer better value than other sectors currently. Sectors like electronics manufacturing services (EMS) and hotels that are valued exorbitantly should see a moderation while real estate should continue to do well this year, though might not repeat the 37% index return from the year gone by. However, it is difficult to predict the short-term performance, so please do not rely on the above while investing.

Deployment strategy

We continue to be cautious in our deployment strategy due to the valuations still being stretched in most parts of the market. Our cautious approach involves maintaining high levels of cash and gradually investing over time. We deployed around 40% of the capital this quarter.

Conclusion

We look forward to 2025 with optimism, hopeful that the new year will bring respite in the international geopolitical situations and reignite the growth numbers for India, leading to another year of good returns for investors, who continue to remain subscribed to the Indian equity markets.

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