Dear Shareholders and Investors,

The Calendar Year (CY21 – Jan to Jun 2021) has been a strong year with the fund up 16.4% in the year. We continue to perform well against Nifty 50, outperforming the Nifty 50 by 4%. This puts our absolute performance of the fund since inception cumulatively at 174.8% beating the index by 82.8% on a cumulative basis.

At Itus, we have emphasized the importance of two things – sustainability of returns (which has a direct connection to our style of investing in growth companies which show cash flow growth) and quality of management (which comes through from capital allocation and balance sheet management).

Today, in a market where most balance sheets are de-levered, the tone of the management has moved towards saying the right things, which means, it becomes more important than ever to understand the sustainability of returns in our portfolio companies.

Portfolio Performance

	Fund Return (%)	Benchmark - Nifty 50 (%)	Excess Return (%)
2021	16.4%	12.4%	4%
2020	40.3%	14.9%	25.4%
2019	17.3%	12.0%	5.3%
2018	-7.3%	3.2%	-10.5%
2017	54.7%	28.7%	26.0%
Since Inception (Cumulative)	174.8%	92%	82.8%

	1Y	2Y	3Y	Since Inception
Itus IRR	58.20%	32.72%	25.47%	25.21%
Nifty 50 - Benchmark IRR	52.59%	15.44%	13.60%	15.61%

- The fund has outperformed Nifty by 9.6% on an IRR basis since inception (Our objective has been to beat Nifty by 6-8% measured in 5Y Buckets).
- Cumulatively the fund has outperformed the benchmark by 82.8% (1 Cr invested in the fund would be worth 2.74 Cr Today)

We measure our performance by our consistency – how often does the fund outperform the index during up and down markets – in order to minimize the drawdowns investors experience.

UP MARKETS		DOWN MARKETS	
Fund Return	Benchmark Nifty Return	Fund Return	Benchmark Nifty Return
9.48%	8.15%	-4.46%	-9.15%
Average Alpha	1.34%	Average Alpha	4.69%
Fund Return	9.48%	Fund Return	-4.46%
Benchmark Return	8.15%	Benchmark Return	-9.15%
Average Alpha	**1.34%**	Average Alpha	**4.69%**

- Our fund has outperformed Nifty on 8 out of 14 quarters where the benchmark return was positive in the quarter – the average out performance during this period was 1.34%
- Our fund has outperformed Nifty on 3 out of 4 quarters where the benchmark return was negative in the quarter – the average outperformance during this period was 4.69%

(The above table explains to investors the concept of downside protection the fund has provided during down markets).

Market View

In my opinion, there is very little standing in the way of the market moving higher, perhaps substantially higher, this year. My concern is not that the market is too expensive or that rising interest rates at the long end, if they continue, will put pressure on valuations. My concern is that stocks continue to go up making the vast majority of stocks unattractive even for the most ardent of bulls with long time horizons. I don’t think we are close to that yet since we can buy stocks out there that look quite attractive even on conventional valuation metrics such as multiples of Free Cash Flow.

The models that show the market is overvalued are not wrong with respect to their parameters, but they are not useful, in my opinion, because their parameters do not capture the complexity of what drives markets. Market or economic forecasts are forecasts not of variables ordered in particular ways, but forecasts of behavior. Today retail participation is high, bordering on leverage in pockets – which will always be a recipe for tail risk to hit the markets if things go south. On the margin though, the path for Indian equities appears to be higher.

Portfolio Construct

Though, we continue to be optimistic on the markets, our thought process is driven around managing risk if there is a risk of a correction (For us, downside minimization is a key aspect of how we run the fund during any given instance).

We have been reducing our exposure across private sector lenders (Refer our letter dated June 2020, where we had increased our exposure significantly across private sector banks, which has played out well so far in the portfolio). Our decision to reduce our private sector bank exposure is driven by:

- Reducing leverage in the book
- Front ended gains against Operating profit growth of the bank.
- Better risk-reward opportunities from an investment perspective

The cash generated from the sales alongside the cash in the portfolio was used to deploy into non-lending financials (an AMC, A financial infrastructure company and an exchange). We also increased our exposure to some of our existing portfolio holdings whose cash flow growth continues to be robust (though, at higher valuations).

Portfolio Quality

The earnings season for 4QFY21 was complete and our portfolio companies, showed a cumulative FCF growth of 157% on a yoy basis. This was the highest ever cash flow growth our portfolio has recorded over a year since inception.

There were two components to the FCF growth that we observed – a) Revenue increase (due to gain in market share) b) Working capital reduction as balance sheet improved drastically – focus on operational metrics and increased demand helped.

The below table breakdown the strength of the portfolio alongside the pricing power of the businesses we own:

	Itus FY21
GP Margin	54.23%
ROCE	22.62%
FCF growth	147.69%

Over the same period, our portfolio has moved up by 72%. This gives us a degree of valuation comfort around the fundamental health of our portfolio (measured by Cash Flow Growth) vs the Actual stock price move (Price change).

Over the last 4.5 years, the net return to investors has compounded at a similar growth rate to the FCF growth of the portfolio. The below Table (Table 1) gives a breakdown of how each of our portfolio companies grew in Q4FY21.

Table 1 : *Growth of portfolio companies during Q4FY21*

	Quarterly Growth		Annual Growth			
Company	Revenue (QoQ)	PAT (QoQ)	Revenue (YoY)	PAT (YoY)	GP Margin (%)	ROCE (%)
ALEMBIC PHARMACEUTICALS LIMITED	-2.47%	-14.31%	22.48%	42.14%	72.73%	25.50%
ALKEM LABORATORIES LIMITED	-7.29%	-46.27%	7.69%	40.76%	61.55%	24.02%
BALKRISHNA INDUSTRIES LIMITED	16.12%	16.88%	17.65%	22.70%	61.26%	25.00%
COMPUTER AGE MANAGEMENT SERVICES LIMITED	6.03%	6.58%	1.99%	19.43%	53.87%	43.09%
FINE ORGANICS INDUSTIES LIMITED	8.06%	12.13%	8.70%	-23.94%	36.20%	20.30%
GALAXY SURFACTANTS LIMITED	15.99%	-7.69%	7.52%	31.13%	36.43%	26.99%
HDFC ASSET MANAGEMENT COMPANY LIMITED	-8.29%	-13.32%	2.72%	5.22%	89.70%	36.14%
HDFC BANK LIMITED	5.47%	-3.83%	18.77%	16.80%	51.00%	-
HDFC LIFE INSURANCE COMPANY LTD	35.63%	21.11%	18.31%	4.89%	39.56%	-
ICICI BANK LIMITED	-3.17%	-10.87%	29.52%	104.17%	46.00%	-
ICICI LOMBARD GEN INSURANCE CO LTD	14.07%	10.25%	10.03%	23.40%	16.07%	-
INDIAMART INTERMESH LIMITED	-4.09%	-30.55%	6.88%	89.82%	72.86%	20.10%
INDIAN ENERGY EXCHANGE LIMITED	4.41%	4.90%	19.78%	17.28%	87.55%	45.20%
INFOSYS LIMITED	1.20%	-2.63%	9.70%	16.73%	45.90%	31.74%
L AND T TECHNOLOGY SERVICES LIMITED	1.77%	4.49%	-3.86%	-19.44%	40.13%	23.72%
LUPIN LTD	-5.83%	5.22%	-1.38%	407.13%	64.63%	11.97%
MCX INDIA LIMITED	-13.69%	-46.46%	-1.74%	-4.77%	84.80%	13.72%
ORIENT ELECTRIC LIMITED	30.16%	20.66%	-1.31%	52.30%	30.31%	35.61%
Route Mobile Ltd	-8.05%	-5.72%	46.90%	128.08%	20.61%	24.63%
SUMITOMO CHEMICAL INDIA PRIVATE LIMITED	-4.84%	-0.08%	9.36%	68.74%	37.85%	28.84%
SYNGENE INTERNATIONAL LIMITED	12.53%	34.41%	7.42%	-1.90%	76.59%	11.58%
TATA CONSUMER PRODUCTS LIMITED	-0.29%	-43.75%	20.25%	102.23%	41.12%	8.22%
UTI AMC	-17.25%	-4.51%	36.82%	79.81%	67.52%	17.45%

Portfolio Discussion

Currently we own 21 investments in our portfolio with 6 broad themes into which our investments fit into:

a) Private sector Lenders
b) Non Lending Financials
c) Exchanges / Platforms
d) IT / Tech
e) Pharma
f) Consumer Businesses (B2b and B2c)

Over the quarter, we exited our holdings in Sun TV and MCX (for all our investors who had portfolio exposure to the two companies – we also wrote a note on the reason for the exit and why we decided to exit the two businesses which was sent separately to the investors who owned the businesses)

New Portfolios Construct

It is important to spend some time to discuss how we think about deploying new money in the markets today. To set the context, it's evident that the markets are no longer cheap, in fact, I would put my hand up and say that the broad markets are fairly valued and, in many pockets, expensive.

We do not manage risk with the view that, it is fine to buy good quality businesses at any price and the shareholder returns will compound over the long term (atleast not at the 18-20% IRR we target for investors). Internally at Itus, we have maintained that it is important to own businesses at the right price. I will cover this aspect with an example (as there is no formula to define this mathematically).

We have owned Syngene (one of our portfolio companies) since early 2018. Many investors would find Syngene at a current allocation of excess of 10% in their portfolios (with gains). Our broad thesis on the company remains unchanged, however, for investors deploying capital today, the exposure in the company would be broadly between 5-6% of the portfolio.

Why this difference? Specifically with the company, I would want to see the company increasing its Fixed Asset Turns as the additional capex deployed sweats over the next few quarters – which is what I call 'execution monitoring'. I would not mind increasing the exposure over time as they execute (albeit at higher prices), but would not want to take that risk today. Effectively, the way we think about our exposure at every stage is, how much could this portfolio investment fall if the execution fails, and we size our investment appropriately. This defines how we size each of our investments and is one of the primary reasons we do not like model portfolios and believe it comes at the detriment of investor returns.

Defining our Risks

Equity markets while rewarding in the long term, can cause investors to take sub-optimal decisions in the short term (The sub-optimal decisions coming in the form of selling during panic, or buying frothy companies because momentum is supporting them during bull markets). I last heard the word multi-bagger in investor conversations in 2017 and am hearing them again used freely today. This does not mean we need to prime for a correction, but it means it's important to think about the risks to the portfolio more closely.

Today, when I look at the markets, it's hard to quantify a risk which I am worried about, which I feel is the biggest risk. The retail leverage in the system is increasing and the net retail longs is at the highest since 2014 (when our Prime Minister, Narendra Modi was elected for the first time). Again, this is not a cause for concern but an aspect to think about around how important a sound portfolio construct is, today, perhaps more important than ever.

We look forward to speaking with you on our call at **10 am** on **10th July 2021 (Saturday)**

From the desk of the CEO

Naveen Chandramohan