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o3 wealth & asset management

Sharing random thoughts

Dear Investor,

In this newsletter, we wish to share with you our thoughts on three or four different topics that are topical and relevant for you as investors.

Change in the name of our company.

We are pleased to share an important announcement with you. o3 Securities (o3 Wealth & Asset Management) has embarked on a new chapter in our journey to provide you with unparalleled financial services. As part of our continued commitment to growth and excellence, we are rebranding and will henceforth be known as **BUGLEROCK CAPITAL PRIVATE LIMITED.**

The name reflects not only our solid foundation and stability but also our forward-moving dynamism and innovation in wealth and asset management. Rest assured, this change symbolizes our evolution and dedication to enhancing your experience with us.

The name has changed, but what does not change is our commitment. We will continue to manage your portfolio in the same manner as we have been doing. We will run each investment approach strictly coordinated with its investment objective.

We firmly believe that managing your portfolios in a disciplined manner is far more important than trying to generate the "highest return," and this does not change with the change in name.

A no-surprise Interim Budget

The interim Budget presented on February 1st did its best not to upset any applecart. The continuation of policies of maintaining tax rates, further increase in capital expenditure budget (capex is now 3.4% of GDP) and focus on social welfare schemes were on expected lines.

Source: Budget Document

It is apparent that the government wishes to maintain the status quo mode for now.

We like the continued thrust on railway modernization, and the thrust on green energy.

Your portfolio has a collection of capital goods/industrial stocks that we think would benefit from the continued thrust on physical infrastructure and domestic manufacturing. That apart, we have to wait for the next full-fledged budget to see if there is a big shift in the direction of government's fiscal policy.

A new addition to the model portfolio

Recently we have added Life Insurance Corporation (LIC) to our model portfolio. Here are the salient points:

1) We had pointed out in our January 2024 newsletter an interesting piece of data, which we would like to reiterate here:

Financial sector among BSE 200 companies		
Year	**% of Profits**	**% of Market Cap**
2018	12.7%	24.3%
2023	38.0%	25.7%

Sources: (1) Bloomberg (2) ACE Equity

2) We think it is logical now to increase exposure to financial services, especially since some of the strong names are trading at attractive valuations.

3) While adding additional companies in the sector, we have to take care not to overload the portfolio with similar companies. We therefore now have this diversified exposure to financial services – one strong private sector lender, one strong public sector lender, one credit rating agency, one registrar company, and one insurance company. We had an exchange company, which has been removed from the model portfolio primarily for reasons of sharp price movement.

4) LIC is a 67-year-old behemoth, which still has 62.58% of the market share of new business premium, 20 years after private sector players have entered the fray. In terms of size, LIC's new business premium collection is nearly eight times the size of the second largest competitor.

5) It has a wide distribution reach covering 92% of all districts in the country, with 27.74 crore policies in force.

6) It has a market share of 51% of all insurance agents.

7) India's population in the year 2021 estimatedly had 58% in the age group of 20-64. This proportion is expected to rise to 61% in the year 2035, and we are talking of a population of 1.4 billion people. We have to juxtapose this point with the low insurance penetration, and the need to plan for the eventual retirement of this segment of the population in a few decades' time.

8) The penetration of Life Insurance products in India is estimated to be 3.2%, and the protection gap (the estimated difference between the extent of insurance needed, and the extent of insurance availed) is 83%, one of the highest in the world. We are therefore confident that the insurance market still has a lot of potential for growth.
Source: Company presentation

9) The Life expectancy in India has improved over the decades:

Year	Life expectancy (years)		
	Male	Female	Total
1950	42.6	40.8	41.7
1960	45.9	44.5	45.2
1970	48.9	47.6	48.2
1980	53.5	53.7	53.6
1990	57.9	59.5	58.7
2000	61.8	63.6	62.7
2010	65.3	68.6	66.9
2020	68.6	71.8	70.2
2023	70.5	73.6	72.0

Source: worldmeters info.

Longer expected post-retirement life expectancy means greater need for life insurance and pension products.

10) In other operating parameters such as persistency ratios and Expense ratios, LIC fares quite well:

Company	Persistency ratio (on the 61st month)
LIC	50.4
Max Life	49.0
SBI Life	58.1
HDFC Life	54.0
ICICI Pru Life	64.9

Source: Individual Company Presentations

Expense ratio (operating expenses + commissions paid as % of premium collected)

Company	FY 2021	FY 2022	FY 2023
HDFC Life	16.30	16.40	19.70
ICICI Pru Life	11.70	14.30	16.10
Max Life	20.80	19.70	20.50
SBI Life	7.50	8.30	9.10
LIC	15.00	14.50	15.50
ABSL Life	19.10	17.40	19.50
Tata AIA	25.10	29.30	31.10
Bajaj Allianz	20.90	23.00	26.20

Source of data : Individual company presentations.

11) In terms of valuation (market cap to embedded value), LIC is amongst the cheapest in the industry:

Market cap to declared embedded value (at the end of first half of 2023-24)

HDFC Life	2.90
SBI Life	2.70
ICICI Pru Life	1.90
Max	1.70
LIC	0.90

(note: Market cap as of 31st January 2024 and embedded value as of end of Sept 2023)

Source: Individual company presentations / NSE

Reiteration of our earlier commitment to some companies

HDFC Bank

Some of you had expressed some apprehensions about the prices of some of our holdings falling in a rising market, most notably the prices of HDFC Bank (which, incidentally, is now our largest holding), and Indraprastha Gas.

We have re-examined our investment case in both of them and we are confident that the risk-reward ratio in both cases is firmly with that of the investor.

Consider the following facts in the case of HDFC Bank:

Parameter	10-year avge (ending FY 2023)	Qtr ending Dec 2023
Net NPAs	0.33%	0.30%
Return on Assets	1.97%	2.00%
Capital Adequacy Ratio	17.03%	18.40%
Cost to Income ratio	40.98%	40.30%
Operating costs to assets	2.18%	1.90%
NIM %	4.02%	3.40%

Source: Ace Equity/Company Investor Presentation.

The bank's performance, definitely, has not weakened post the merger, as feared. The valuation today is at 1.63 times Book Value (on Bloomberg consensus estimates of 1-year forward BV) compared to a 10-year average of 3.0 (calculated on the same basis).

Indraprastha Gas Ltd

There are times when investors have to remind themselves that life does not follow the trajectory of an excel spreadsheet, where it is quite easy to extrapolate the numbers over several columns.

Some facts about Indraprastha Gas:

Parameter	FY 2014	FY 2023
Revenues (Rs. Cr)	4324.16	15603.02
PBIDT (Rs. Cr)	808.63	2258.94
Net profit (Rs. Cr)	360.26	1639.65
Free cash flow (Rs. Cr)	360.13	1527.83
Debt to Equity (x)	0.20	0.00
Return on Capital (%)	28.97	27.70
Receivable days	16.82	16.65
Inventory days	3.24	1.11
Total Volumes (MMSCM)	1383.9	2952.0
CNG spread (Rs/SCM)	8.30	17.10
PNG spread (Rs/SCM)	10.70	15.90

Source: Ace Equity/Company Investor Presentation.

- The company's products are bought by lakhs of consumers, on a daily basis, with repeat purchases every day.
- In all areas they operate, they have a 100% market share.
- They consistently generate high return on capital and free cash flow.
- In the December 2023 quarter results, they posted a 40% growth in net profits y-o-y. *Source: Ace Equity*
- The stock now trades at a valuation that is at a 20% discount to its 10-year average.

We think that IGL is a textbook case of perception being much weaker than reality. The recent proposal by the Delhi government to try and make fleet operators (who own more than twenty-five vehicles) convert to electric vehicles after 2025 has had a dampening impact on the sentiments around the stock.

We reproduce parts of our November 2023 newsletter in which we had explained our stance on this issue:

The salient features of the policy are:

(a) The policy is applicable to vehicle fleet aggregators who operate a fleet of twenty-five vehicles or more.

(b) It is envisaged by the policy that over the next five years after implementation of the policy, all Delivery Service Providers would convert their fleet to electric vehicles.

(c) There is no clarity about how the subsidy for purchase of Electric Vehicles (for those who wish to convert from petrol or CNG vehicles) would be funded.

(d) There is a mention in the policy that the Delhi Authorities can impose a penalty (after 1st April 2030) on vehicles that are not Electric Vehicles.

We have the following doubts about this policy:

(a) If a CNG or petrol vehicle (even if it is part of an aggregator's fleet) is compliant with the prevalent Bharat VI emission norms (or any other norm relevant at that time), on what basis would the penalty be imposed?

(b) What proportion of vehicles would come under the purview of this policy? As we understand, this policy is applicable for vehicle aggregators and their fleets that are more than twenty-five vehicles.

There was a conference call recently in which the management of IGL shed some light on some of these points:

(1) *Delhi contributes about 60% of the total CNG sales of IGL, but for our calculations for the risk analysis of IGL, let us assume that Delhi contributes 60% of the overall sales of IGL.*

(2) *It is the company's estimate that about 15% of the total volumes in Delhi would be taken up by vehicle aggregators and fleet operators.*

Therefore, even assuming that all vehicle aggregators and fleet operators have more than twenty-five vehicles (a highly unlikely scenario), we are talking of a situation where 9% of the CNG sales of IGL is likely to face a problem after 2025, provided the EV policy of the Delhi Government is fully implemented.

To conclude, dear investor, our approach is to keep accumulating stocks of strong companies when they are relatively unpopular. The unpopular phase gives us a good entry point. Both HDFC Bank and Indraprastha Gas fit into this theme perfectly. The important point is that neither of these companies has shown even the least indication that it has lost its ability to compete in the marketplace. We are confident that these will return to the "popular list." We shall wait for that to happen.

With warm regards,

Yours sincerely,

(E A Sundaram)
Chief Investment Officer and Portfolio Manager.

"You are neither right nor wrong because the crowd disagrees with you. You are right because your data and reasoning are right."
Benjamin Graham

Investment Objective:

The investment objective is to achieve capital appreciation through investment in a diversified portfolio of high-quality companies, purchased at reasonable valuation.

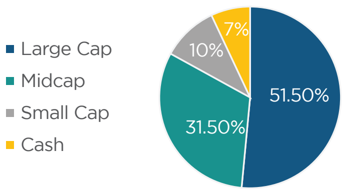
o3 Core Value Investment Approach

Name	GICS Sector	Weight
HDFC Bank Ltd	Financials	6.96%
ITC Ltd	Consumer Staples	5.24%
Maruti Suzuki India Ltd	Consumer Discretionary	4.52%
Indraprastha Gas Ltd	Utilities	4.45%
Infosys Ltd	Information Technology	4.41%
Oracle Financial Services Software Ltd	Information Technology	4.15%
Bosch Ltd	Consumer Discretionary	3.80%
Divis Laboratories Ltd	Health Care	3.70%
Asian Paints Ltd	Materials	3.67%
Honeywell Automation India Ltd	Information Technology	3.55%
		44.45%

Overweight/Underweight of Model Portfolio Compared to Benchmark

Sector	Underweight | Overweight
Consumer Discretionary	11.93%
Industrials	5.99%
Utilities	3.13%
Real Estate	2.32%
Health Care	1.29%
Information Technology	-0.99%
Consumer Staples	-1.98%
Communication Services	-2.84%
Materials	-5.38%
Energy	-8.71%
Financials	-11.75%

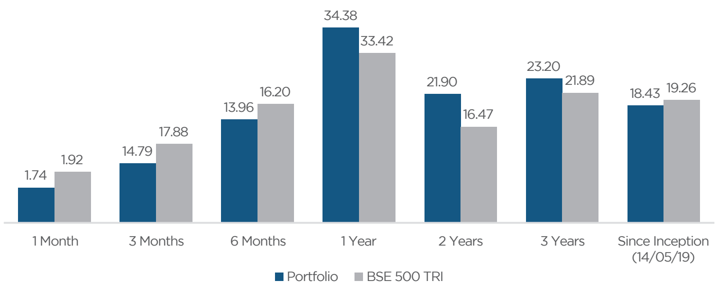
Performance Description	Regular	Concentrated	BSE 500 TRI
Largest Monthly Gain	12.51	11.41	14.63
Largest Monthly Loss	-20.53	-19.19	-23.85
Beta of Portfolio	0.76	0.73	
Standard Deviation (Annualised)	15.26	14.97	
Correlation	0.92	0.91	



Regular Model Portfolio Composition

Weighted Average ROCE	27.51%
Portfolio PE (1 year forward PE, based on FY25)	30.33
Portfolio Dividend Yield	1.27%
Average Age of companies	54 Years
Overlap with BSE 500 TRI	23.34%
Total Debt/Equity	0.26
Debt/Equity (Excluding Financial Stocks)	0.14
Sales Growth	22.64%
EPS Growth (FY25 over FY23)	14.05%

Consolidated Portfolio Performance of o3 Core Value Investment Approach Regular Option 31st January 2024



Consolidated Portfolio Performance of o3 Core Value Investment Approach Concentrated Option 31st January 2024

- *Benchmark is BSE 500 TRI, the portfolio is spread across different market capitalization, hence BSE 500 TRI is chosen as benchmark.*
- *Since inception date stated is considered to be the date on which the first active client investment was made under the investment approach.*
- *All the data are as of 31st January 2024. ROCE/ROE are average of last 5 years.*
- *Source: Internal, BSE, Bloomberg & Ace Equity.*

Disclaimer: Performance depicted is based on all the client portfolios existing as on such date, using Time Weighted Rate of Return (TWRR) of each client for the overall investment approach. Past performance is no guarantee of future returns. The above portfolio performance is after charging expenses. The above performance related information provided here is not verified by SEBI nor has SEBI certified the accuracy or adequacy of the contents of this Document. Beta, Standard Deviation & Correlation are from Since Inception period.