

Recent developments in your portfolio

Dear Investor,

The month of June saw some developments in the o3 Core Value portfolio.

- (a) One development that we were waiting for has come closer to fruition.
- (b) One development that we hoped would happen has met with a further delay, and
- (c) One development we think would happen has triggered a change in the portfolio.

The merger of HDFC Ltd and HDFC Bank has come closer to fruition

In the last week, there was an announcement from the respective companies that the merger between HDFC Ltd and HDFC Bank would be completed in the beginning of July 2023.

We started buying HDFC Ltd in the second half of 2021, well before the initial announcement about the merger in April 2022. The logic that was applied in late 2021 and early 2022 is still very relevant:

- HDFC is a pioneer and one of the strongest companies in housing finance.
- The company, over the last 40 years, has developed an innate understanding of the home-loan customer.
- The company has a very good reputation for proper appraisal systems.
- Net of the value of their investments in HDFC Bank, HDFC Life Insurance Company and HDFC Asset Management Company (all listed entities), plus a reasonable assigned value to their holding in HDFC Ergo, the residual valuation of the standalone home finance business was unbelievably cheap in late 2021 and early 2022.

The merger would create a financial behemoth, and one of the largest banks in the world. The combined bank, we are confident, would continue to have a strong retail franchise, high CASA deposits, higher-than average Net Interest Margins (NIMs) and higher than average Return on Assets (RoA).

There were some fears about the problems around the merger. While no merger of this size is going to be without problems, or people issues, we are confident that the systems and processes in these two institutions would make the entities withstand the problems well. And the valuation (which, incidentally, is now lower than what the stock was trading at the time of the Lehman crisis in 2008, provides us the comfort).

Delay in implementation of the new trading software at MCX

The second development that happened in June 2023 was a disappointing one.

We hold shares of Multi Commodity Exchange (MCX). The reasons to buy were the following:

- The company has an overwhelming market share of commodities futures trading in India, with 96.8% market share.
- We were confident that commodities trading in India would rise in the years to come, with greater institutional participation, and a greater number of contracts being added to the platform.
- In 2021, the company had engaged Tata Consultancy Services (TCS), a leading software services company, to create a new trading software, to replace the existing software provided by 63 Moons.

- The implementation of the new software by TCS was delayed beyond the deadline of December 2022, and because of that, MCX had extended the services of 63 Moons at a cost of Rs.80 crores per quarter, for a further period ending June 2023.
- We estimated that since the company involved is TCS, there would be no further delay beyond June 2023 in implementing the software (there had already been a delay earlier) and estimated that with the implementation of the new trading software, MCX would save the Rs.80 crore per quarter that they paid to 63 Moons.
- It has turned out the implementation of the new trading system by TCS has suffered a further delay, and worse, MCX had to extend the contract to 63 Moons for a further 6 months, paying an even higher cost of Rs.125 crores per quarter.
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This clearly is a setback. The expectation that I had that the successful implementation of the new TCS software would not be delayed beyond June 2023, has not been met.

After the news of this delay came out, the stock sharply corrected on 30th June.

We do not wish to change the holding in MCX now (although we have temporarily stopped fresh purchases until we meet the company). The primary reasons why we bought MCX are still very much relevant. Here are the respective market shares enjoyed by MCX in various categories of commodities trading:

- 99.99% market share in precious metals trade
- 100.00% market share in Energy trade
- 99.86% market share in base metals trade
- 9.34% market share in agricultural commodities trade
- 94.62% market share in Index futures

(Source: MCX company presentation)

We are disappointed at the delay in implementation of the new software (and the consequent cost saving it would bring), but we do not think it is right to sell the position in a strong competitor when the chips are down.

A recent change in o3 Core Value portfolio – the entry of Oberoi Realty

Let's consider the following facts:

There was a recent report in the Financial Express newspaper (March 21 2023) that the contribution of the real estate sector to India's GDP is around 11%.

This sector's share in the Nifty 500 index (as of 31st May 2023) is 0.88%. The real estate sector has 0% weight in the Nifty 50 index, and 0.31% weight in the Nifty 100 index.

In comparison, the other popular indexes around the world have this exposure to real estate:

| Index | Weight of real estate sector (%) |
|-------------------|----------------------------------|
| S&P 500 | 2.50 |
| MSCI World Index | 2.70 |
| MSCI Asia Pacific | 3.54 |

Why do we think that the residential real estate sector will get more important in the years to come?

The implementation of the RERA Act was an important milestone in the way the real estate sector operated. It made way for the stronger companies to get stronger, and weaker players slowly getting marginalized.

India's inexorable move towards increased urbanization



India's Real Estate Industry To Touch \$1 Trillion By 2030

| | GDP Contribution to World (%) | Urbanization Rate (%) | Urban Housing Shortage (Mn) | Urban Homeownership |
|--------------------------|-------------------------------|-----------------------|-----------------------------|---------------------|
| India | 3.30 % | 35% | 29 | 69% |
| China | 18.50 % | 63% | NA | 87% |
| United States of America | 23.90 % | 83% | 38 | 65% |
| United Kingdom | 3.30 % | 84% | 8.4 | 64% |
| Brazil | 1.70 % | 87% | 7.7 | 67% |

Note: Data is an financial year for India, Data for 2021 Source World Bank, Industry Estimates, ANAROCK Research

Why Oberoi Realty?

In Oberoi, we found a company which is very strong in the Mumbai region, with the ability to source tracts of land with a clean title (from very reputed parties), the ability to develop a proper living ecosystem for the residents, the ability to charge a premium over other builders in the locality, and good prospects for the foreseeable future.

Land tracts secured

| Land | Seller | Year | Price Mn | Name of Project |
|-----------------------|--|---------|----------|--------------------|
| Goregaon East | Novartis / Ciba Specialty Chemicals | FY00-05 | 1,068 | Oberoi Garden City |
| Andheri West | Excel Industries and Shroff Family Trust | FY05 | 317 | Oberoi Springs |
| Andheri East | Madhu Fantasy Land and Avinash Bhosale | FY06 | 1,060 | Oberoi Splendor |
| Mulund West | GSK owned Burrough Wellcome | FY06 | 2,210 | Eternia and Enigma |
| Worli (I-Ven JV) | GSK | FY07 | 1,080 | Yet to launch |
| Worli (Oasis JV) | JV with Skylark Build and Shree Vrunda Enterprises | FY09 | 3,000 | 360 West |
| Boriwali East | Tata Steel | FY15 | 1,155 | Sky City |
| Pokhran Road, Thane | GSK | FY18 | 9,000 | Yet to launch |
| Pokhran Road-2, Thane | Blue Star | FY23 | 1,923 | Yet to launch |
| Pokhran Road-2, Thane | NRB Bearing | FY24 | NA | Yet to launch |
| LBS Marg, Bhandup | Debt Recovery Tribunal | FY 22 | 1,190 | Yet to launch |

The table above gives an indicator that the land deals secured by the company have been with impeccable sellers, giving us the confidence that the titles to the land would be clean. For instance, the three recent plots of land in Thane (adjacent plots) were purchased from GlaxoSmithKline, Blue Star and NRB Bearings, respectively.

Developing a full residential ecosystem

We are impressed with the record of the company of developing a proper residential ecosystem for its residents. In Goregaon for instance, the company has developed a mall, a school, commercial towers in the same vicinity, thus creating a mini township. Given this sort of capabilities, it is not surprising that in almost all areas where Oberoi operates, they are able to command a premium pricing compared to the average rates in the area:

| Project Name | Average price in Rs per square feet | Locality | Average price in Rs per square feet |
|------------------|-------------------------------------|-----------------|-------------------------------------|
| Oberoi Springs | 47,100 | Andheri West | 34,850 |
| Oberoi Exquisite | 52,700 | Goregaon East | 28,750 |
| Oberoi Esquire | 50,950 | Goregaon East | 28,750 |
| Oberoi Splendor | 40,800 | Jogeshwari East | 28,900 |
| Oberoi Sky City | 38,150 | Borivali East | 27,600 |

Source: www.99acres.com

Given the changes in the accounting standards for realty companies, they can account for revenues and profits only after the full handover of the property to the buyers. We are confident, given the status of their upcoming projects in Worli (Three Sixty West) and their commercial properties (Commerz III), that the revenues and profits of the company would see a decent upward trajectory in the next couple of years.

Oberoi Realty Ltd. - Financial Highlights-Consolidated-[INR-Crores]

| DESCRIPTION | Mar-14 | Mar-15 | Mar-16 | Mar-17 | Mar-18 | Mar-19 | Mar-20 | Mar-21 | Mar-22 | Mar-23 |
|-----------------------|--------|--------|---------|---------|---------|---------|---------|---------|---------|---------|
| Inc / Exp Performance | | | | | | | | | | |
| Total Income | 863.4 | 976.6 | 1,492.3 | 1,171.4 | 1,292.0 | 2,661.3 | 2,286.0 | 2,090.6 | 2,752.4 | 4,293.2 |
| PBIDT | 491.9 | 531.3 | 719.1 | 617.4 | 701.8 | 1,234.1 | 1,096.3 | 1,038.4 | 1,239.8 | 2,212.3 |
| PAT | 311.1 | 317.1 | 434.0 | 375.4 | 455.2 | 810.0 | 683.4 | 739.3 | 1,047.1 | 1,904.5 |
| Debt to Equity(x) | 0.02 | 0.19 | 0.09 | 0.15 | 0.28 | 0.20 | 0.18 | 0.16 | 0.27 | 0.32 |
| PBIDTM(%) | 61.60 | 57.59 | 50.78 | 55.43 | 55.46 | 47.79 | 48.99 | 50.59 | 46.02 | 52.77 |
| PATM(%) | 38.96 | 34.37 | 30.64 | 33.71 | 35.97 | 31.37 | 30.54 | 36.02 | 38.87 | 45.43 |
| Adjusted EPS | 9.48 | 9.66 | 12.84 | 11.15 | 13.51 | 22.47 | 18.96 | 20.33 | 28.80 | 52.38 |

Source: ACE Equity

We have a policy of not holding more than twenty-five stocks in the portfolio. Therefore, in order to accommodate Oberoi Realty, we had to sell United Breweries. This is not a reflection of our view of United Breweries. It is just that, given the mix in the portfolio, there was no other company with which we could have replaced Oberoi Realty.

Warm regards

Yours sincerely,

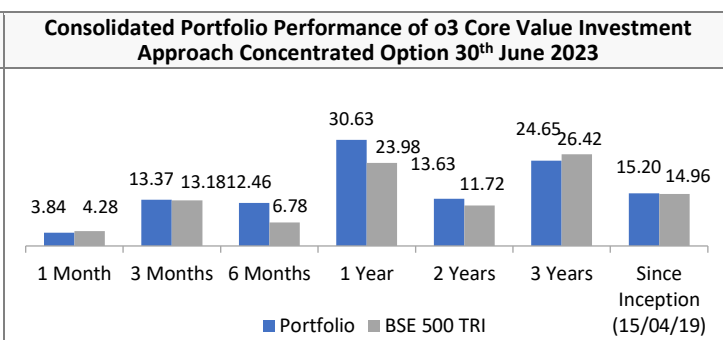
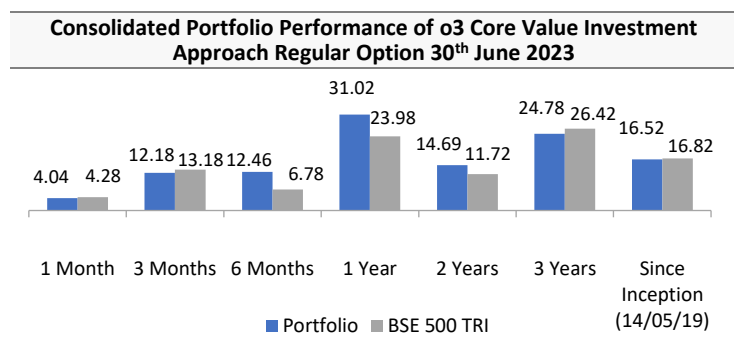
E A Sundaram

Chief Investment Officer and Portfolio Manager

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 | | | Overweight / Underweight of Model Portfolio Compared to Benchmark | | |
|-----------------------------------|------------------------|---------------|---|--|--|
| Name | GICS Sector | Weight | | | |
| ITC Ltd | Consumer Staples | 5.71% | | | |
| HDFC Ltd | Financials | 5.29% | | | |
| Indraprastha Gas Ltd | Utilities | 4.05% | | | |
| Infosys Ltd | Information Technology | 4.04% | | | |
| Maruti Suzuki India Ltd | Consumer Discretionary | 3.84% | | | |
| Asian Paints Ltd | Materials | 3.69% | | | |
| Divis Laboratories Ltd | Health Care | 3.65% | | | |
| Sun Pharmaceutical Industries Ltd | Health Care | 3.65% | | | |
| Bosch Ltd | Consumer Discretionary | 3.61% | | | |
| Titan Company Ltd | Consumer Discretionary | 3.56% | | | |
| | | 41.09% | | | |

| Performance Description | Regular | Concentrated | BSE 500 TRI | Regular Model Portfolio Composition | |
|---------------------------------|---------|--------------|-------------|---|----------|
| Largest Monthly Gain | 12.51 | 11.41 | 14.63 | Weighted Average ROCE | 23.49% |
| Largest Monthly Loss | (20.53) | (19.19) | (23.85) | Portfolio PE (1 year forward PE, based on FY25) | 23.90 |
| Beta of Portfolio | 0.76 | 0.73 | | Portfolio Dividend Yield | 1.44% |
| Standard Deviation (Annualised) | 15.93 | 15.57 | | Average Age of companies | 51 Years |
| Correlation | 0.93 | 0.91 | | Overlap with BSE 500 TRI | 19.91% |
| | | | | Total Debt/Equity | 0.49 |
| | | | | Debt/Equity (Excluding Financial Stocks) | 0.16 |
| | | | | Sales Growth | 19.76% |
| | | | | EPS Growth (FY25 over FY23) | 13.59% |



- 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
- Industry Classification as recommended by AMFI, all the above data are as of 30th June 2023

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 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.*

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