Ellerston India Fund

Monthly Newsletter, December 2021

Investment Objective

To outperform the MSCI India Net Return Index (AUD) with a focus on risk management and capital preservation.

Investment Strategy

The Fund's investment strategy is to construct a concentrated portfolio with exposure to Indian companies using the Manager's high growth, high conviction, benchmark independent investment approach. The Fund has identified a number of core thematics that will drive returns in the Indian market in the medium term. The focus is on investing in Indian companies that benefit from these fundamental drivers.

Key Information

Strategy Inception ^^	4 May 2017
Portfolio Manager	Fredy Hoh
Application Price	$1.3599
Net Asset Value	$1.3565
Redemption Price	$1.3531
Liquidity	Daily
No Stocks	34
Management Fee	1.10% p.a.
Performance Fee	15%**
Buy/Sell Spread	0.25% on application/ 0.25% on redemption
Minimum Investment	$10,000
Minimum Additional Investment	$10,000
Distribution Frequency	Half Yearly (June & December)

*** Of the investment return above the benchmark, after recovering any underperformance in past periods*

Performance Summary

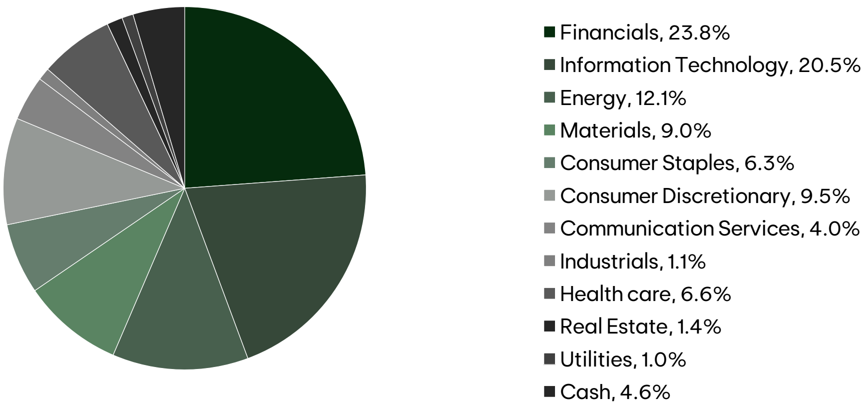
Period	Gross+	Net Before Tax*	MSCI India Net Pre Tax	Net After Tax^
1 Month	1.6%	1.5%	1.2%	1.1%
FYTD22	14.6%	14.0%	16.0%	12.5%
1 Year	29.4%	28.0%	34.0%	22.9%
3 Years (cumulative)	51.6%	46.4%	51.9%	38.0%
Since Inception^^ (cumulative)	76.4%	66.8%	70.8%	57.0%
Since Inception^^ (p.a.)	12.9%	11.6%	12.2%	10.2%

^ The net return figure is calculated after fees, expenses and taxes. Past performance is not a reliable indication of future performance. All returns shown in AUD.
+References to the gross fee and pre-tax contribution to the total Net After Tax and Fee return.
*Net return figure is calculated after fees and expenses.

Portfolio Characteristics

Top 10 Holdings

Company	Sector	Weight
Reliance Industries	Energy	12.14%
Infosys Limited	Information Technology	9.46%
Housing Development Finance Corp	Financials	7.86%
ICICI Bank	Financials	7.58%
Bajaj Finance	Financials	4.02%
Tech Mahindra	Information Technology	4.02%
Hindustan Unilever	Consumer Staples	3.48%
UltraTech Cement	Materials	3.24%
Tata Consultancy Services	Information Technology	3.18%
Bharti Airtel	Communication Services	2.79%



Source: Ellerston Capital.

Commentary

The Ellerston India Fund (EIF) was up 1.15% (net after tax) in December versus the MSCI India Index (MXIN) which was up 1.17%.

As highlighted in the performance summary table, tax and currency continue to have a material impact on portfolio performance.

The Indian market rebounded sharply in the second half of December driven by further improvements in economic indicators and strong local mutual fund inflows (at US$4bn – highest on record). The solid market performance in December rounded off an exceptional year for Indian equities with the MXIN up 27.3% in local currency terms, which made it the best performing market in Asia. Heading into 2022, we are cautiously optimistic on the outlook for the Indian market with a number of secular tailwinds helping the continued cyclical recovery. These secular tailwinds such as attractive demographics (440m millennials), technological leapfrogging, rising incomes, strong job growth across services and manufacturing and historically low interest rates provide a positive investment backdrop for multiple sectors such as consumer, property, financials and IT services. We are currently overweight these four sectors.

Despite our optimism, there are a number of risks in the coming months that will need to be closely monitored. First is the spread of the Omicron COVID variant across India. The earliest case of Omicron in India was recorded in mid-December. Since then, daily COVID cases have risen to over ~200,000 in early January. Despite the surge in cases, the hospitalization rate thus far is half the level seen during the recent second wave. There has also not been a noticeable step-up in the case mortality rate over the past month. This gives us optimism that India will follow the South Africa, UK and Denmark examples where Omicron has proven to be more infectious, yet less deadly than previous mutations. Nonetheless, there is the possibility that localized restrictions are re-implemented to contain the spread of Omicron. We however expect any such restrictions, if enacted, to be much shorter in duration and have less economic impact than previous episodes. We will therefore opportunistically look to add to our existing core positions on any COVID-related pullbacks.

The second risk we see is the prospects of an interest rate hike by the Reserve Bank of India (RBI). Although inflation currently sits within the central bank's 2-6% target band (December at 5.59%YoY), the prospects of an interest rate increase by the US Federal Reserve could force the RBI to also act. Higher interest rates in the US could put upward pressure on the USD and lead to outflows from Emerging Markets as an asset class, including India. This in turn could force the RBI to also lift interest rates in order to stabilize the INR. The EIF portfolio is overweight beneficiaries of rising interest rates such as ICICI Bank, HDFC Bank and State Bank of India.

The final risk we see to our market outlook is the outcome of elections in 5 key states. In particular, the election in Uttar Pradesh, India's most populous state, is seen as a referendum on Prime Minster Modi and the BJP Party halfway through his second term. Highlighting the importance of these elections was Modi's decision to repeal three contentious farm laws in November. These laws were an important part of the Government's rural reform agenda and would have introduced market based dynamics to help revive the country's long struggling agricultural sector. A poor election outcome could see Modi backflip on other structural reforms, which would likely be viewed negatively by the market.

Portfolio Performance

Turning to performance, Healthcare and Information Technology were the biggest contributors to performance during the month, whilst Consumer Discretionary and Industrials were our biggest detractors.

At a company level, Tech Mahindra and Max Healthcare were the biggest alpha contributors for the Fund. Tech Mahindra was helped by positive read-throughs from the Accenture 1QFY22 results which showed a strong demand environment for outsourced IT services. Max Healthcare meanwhile continued to perform well following its positive 2QFY22 result announcement in November. Conversely, HDFC and Reliance were the biggest drags on alpha. HDFC came under some selling pressure during the month on concerns that an imminent interest rate increase could negatively impact margins. We however remain positive on HDFC given its high exposure to the Indian housing market upturn. The Reliance share price weakness meanwhile reflected volatility in global refining margins and also profit taking from investors. Reliance continues to be the largest holding in EIF as we believe it is the best proxy for India's consumption, technology innovation and decarbonisation thematics.

As always, if you have any questions regarding any aspect of the Fund or the portfolio, please feel free to contact us at info@ellerstoncapital.com.

Kind regards,
Fredy Hoh

Contact Us

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Find out more

Should investors have any questions or queries regarding the Fund, please contact our Investor Relations team on **02 9021 7701** or info@ellerstoncapital.com or visit us at **ellerstoncapital.com.**

All holding enquiries should be directed to our register, Link Market Services on **1800 992 149** or **ellerston@linkmarketservices.com.au.**

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