APIR Code: ECL0339AU

Ellerston India Fund

Monthly Newsletter, July 2022

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	$1.1722
Net Asset Value	$1.1693
Redemption Price	$1.1664
Liquidity	Daily
No. of Stocks	28
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

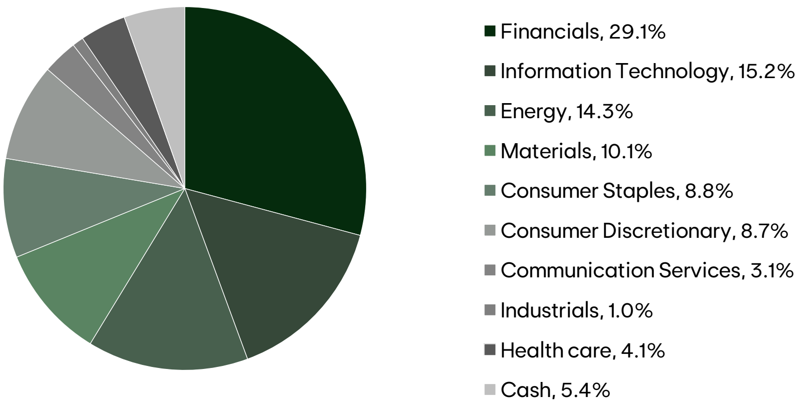
Period	Gross+	Net Before Tax*	MSCI India Net Pre Tax	Net After Tax^
1 Month	7.3%	7.2%	7.7%	6.0%
FYTD	7.3%	7.2%	7.7%	6.0%
1 Year	2.5%	1.4%	8.7%	1.3%
3 Years (cumulative)	32.8%	28.3%	40.7%	22.2%
Since Inception^^ (cumulative)	62.9%	53.0%	64.9%	45.2%
Since Inception^^ (p.a.)	9.7%	8.4%	10.0%	7.4%

^ 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	14.3%
Infosys	Information Technology	9.0%
ICICI Bank	Financials	9.0%
Housing Development Finance	Financials	7.5%
Bajaj Finance	Financials	4.5%
Hindustan Unilever	Consumer Staples	4.4%
Maruti Suzuki India	Consumer Discretionary	4.1%
Tata Consultancy Services	Information Technology	3.3%
State Bank of India	Financials	3.2%
Bharti Airtel	Communication Services	3.1%



Source: Ellerston Capital.

Commentary

The Ellerston India Fund (EIF) was up 6.0% (net after tax) in July versus the MSCI India Index (MXIN) which was up 7.7%. We note that the Indian market was up a very strong 9.6% in local currency terms, but a weakening Indian Rupee against the Australian Dollar (AUD) meant that the AUD was a headwind for absolute returns.

The Indian market was buoyed by: (i) the recent pullback in oil and commodity prices; (ii) the return of foreign institutional investors (FIIs) buying (+US$200m in July); (iii) stabilization of the INR against the USD on expectations that the US Federal Reserve (Fed) will moderate its pace of rate hikes; and (iv) a better than feared 1QFY23 reporting season. These factors supported a risk-on rally in domestic demand beneficiaries within the consumer, financial and materials sectors. Post the July rally, the MXIN is now back to within 6% of its all-time highs.

The Indian economy has weathered the inflationary (July CPI at 6.7%YoY) and monetary tightening cycle (policy rate +140bps YTD) surprisingly well. Rising GST revenues (+24% YoY in the past 12 months) and a more stable currency (US$600bn in FX reserves) and access to cheaper oil from Russia has helped to alleviate macro pressures. In addition, the Government has proactively introduced ad hoc measures to better manage its twin deficit and inflation headwinds. For instance, in the past 3 months the Government has introduced a 15% export duty on steel, imposed a windfall tax on diesel and gasoline exports and increased the import duty on gold. We view the pragmatic approach by the Government positively as it is intended to support end consumers by mitigating the impacts of inflation.

The resilience of the domestic economy was further evident in the 1QFY23 reporting season where large consumer focused names such as Hindustan Unilever, Nestle and Asian Paints recorded solid volume growth despite the pass through of higher raw material costs. Similarly, Banks reported strong numbers with industry leaders like ICICI Bank, SBI, HDFC and HDFC Bank recording >15% YoY loan growth with stable NIMs and asset quality. The strength of the domestically focused companies is supportive of consensus expectations for 15% earnings growth in FY23 for the Indian market. The market meanwhile is trading on a FY23 PE of 23x, which is reasonable given the structural high earnings growth relative to the rest of the world.

Within the EIF portfolio we are most positive on the outlook for the domestic demand focused companies and in particular the industry leaders with pricing power across the consumer and financials sectors. We continue to have a decent weighting towards the IT services sector given the healthy top-line growth (+15% YoY on average in 1QFY23) driven by the ongoing focus on digital transformation by clients. However unlike the domestic focused companies, IT services firms have thus far struggled to protect margins due to significant wage cost pressures. Much of the wage pressure has been a result of hiring in order to fulfill strong order books. Indeed Indian IT services firms have hired over 300,000 new staff over the past 12 months. We believe that the margin pressure facing the sector is likely to trough in the next couple of quarters due to improved employee utilization and better control on non-employee costs.

Portfolio Performance

Turning to July performance, Financials and Materials were the biggest contributors to performance, whilst Energy and Communication Services were our biggest detractors.

At company level, Star Health, Bajaj Finance and ICICI Bank were the key alpha contributors. Star Health had been a detractor last month due to market speculation that the regulator could allow life insurers to sell health insurance products. This concern however has not played out. Meanwhile, Star reported stellar quarterly results with a lower than expected loss ratio and better strategic outlook on increasing agency share, higher retail insurance, increased rural push and strong premium growth. Bajaj Finance reported very strong numbers with 30% AUM growth, 40% net interest income growth and improved asset quality. The company's growth engine has continued to surprise the market positively leading to outperformance. Finally ICICI Bank reported very strong 1QFY23 results with loan growth and net interest income growing 21%YoY respectively and core operating profit growing 19%YoY. We continue hold a positive view on ICICI Bank given its ability to consistently deliver quality high-teens earnings growth driven by macro tailwinds in India and strong operational execution.

Conversely, Reliance, Maruti Suzuki and not owning Adani Group companies were the key detractors. The Reliance share price was negatively impacted by the Government announcement of a windfall export tax on petrol and diesel products. We estimate the tax could impact Reliance gross refining margins (GRM) by ~US$5-10/bbl. This would reduce the Reliance GRMs from the recent peak of >US$20/bbl down to ~US$10-15/bbl, which is in-line with the normalized upcycle average. However, this windfall tax has since been removed in August following the recent correction in crude oil. The Maruti Suzuki share price was sold off following a weaker than expected 1QFY23 result due to lower margins as higher raw material costs were not fully passed through during the quarter. The company's order book remains strong with a backlog of ~350k vehicles (or ~2 months volumes). We remain positive on the outlook for Maruti due to recent model upgrades (Brezza) and the launch of its much awaited Grand Vitarra SUV.

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

Regulatory Guidelines (RG240) Fund Disclosure Benchmark – Periodic Reporting (monthly)

- **Net Asset Value of the Fund and Redemption Price of Units**

Please refer to details on page one.

- **Any changes to key service providers including any change in related party status**

There have been no changes to key service providers, including any change in related party status.

- **Net returns after fees, costs and relevant taxes**

Please refer to details on page one.

- **Any material changes to the Fund's risk profile and strategy**

There have been no changes to the Fund's risk profile and strategy.

- **Any material changes related to the primary investment personnel responsible for managing the Fund**

Please refer to details on page one; there have been no changes to the primary investment personnel responsible for managing the Fund

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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