



MONARCH AIF

Scary part of 'Super Quality Stocks' hiding in plain sight?



QUARTERLY NEWSLETTER

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Scary side of 'super quality stocks' hiding in plain sight?

January 3, 2022

Dear Investors,

Hope you are keeping safe and healthy.

This is the fifth newsletter from the desk of Monarch AIF and we are glad to interact with you once again. We believe that some of India's best managed high-quality companies (called as 'Super Quality Stocks' hereon) have been trading at astronomical valuations for many years on the trot. Not enough has been said or analysed by professional investors on the possibility of underperformance from these companies in future if the companies fail to meet the lofty expectations of the market and if valuations were to normalise. We believe that the scary side of these stocks is being ignored by the market participants led by confluence of factors with recency bias probably being the chief reason. With i) global liquidity set to tighten, ii) interest rate hikes from FED a base case scenario for next 2 years, iii) commodity inflation likely to stay high due to under-investment in capacity creation globally & stiff decarbonisation goals and iv) several underperforming sectors of the last decade in India starting to do well, leading to more investment options coupled with plethora of new listings, we believe that the probability of valuations normalising is high, which could imply sharp underperformance of the 'Super Quality Stocks' in the coming years. Through this newsletter, we are taking a hard-analytical look at the probable **'Valuation Bubble' in 'Super Quality Stocks' in India** and provide a framework to analytically decide which stocks in these baskets could be *relatively safe* and which ones could well be *scary* to bet on currently. We are astonished to see several fund managers pushing thoughts which justify giving NO importance to valuations (for companies whose business is great and growth outlook is good) and this tendency is getting more acceptance led by performance of such stocks in the last few years, but that's how unsustainable "Bubbles" can get formed. To be sure, some of our well-established and highly respected peers have talked about this irrational behaviour of the market in the past, thereby doing great justice to the investor community at large, but we look to add our two cents to this discussion and hopefully make it interesting, different and not repetitive.

Super Quality is perceived Super Safe but it could well be Scary!

We believe that the market has moved from giving a **'High premium for Quality'** few years back (which was probably justified) to creating a **'Unsustainable Valuation Bubble in Quality'** now (which is most probably unjustified), and this trend has consistently gathered pace since FY16 (which happened to be an inflection point for this trend in our view) due to variety of structural, technical (flows) and regulatory reasons. Also, contrary to popular perception that this phenomenon of polarisation is confined to a handful of stocks, our analysis reveals that 'Super Quality Stocks' basket is as big as 55 stocks where 'Valuation Bubble' has got created in last few years, and provided hiding space to institutional investors. Also, while P/E multiple has got all the attention from the market, there has been strong and unprecedented expansion in the more reliable EV/EBITDA as well as EV/OCF valuation parameters too, which is noteworthy. We take stock of all these issues in this letter and identify a list of **'Scary' & 'Relatively Safe' stocks within the 'Super Quality Stocks' basket** based on Red/Green flag analysis, while also quantifying the expected returns from these stocks over the next 3 years based on some sane yet optimistic assumptions. *We hope the study below would act as a base for investors at large to think about investment decisions in a cogent manner which balances risk-reward suitably and doesn't keep them in an illusion that 'Super Quality' means 'Super Safe'. In fact, 'Super Quality' is appearing 'Scary' right now when analysed dispassionately, in our humble opinion!*

The key topics addressed by us in this note are as follows: -

- A. Tracking the valuation expansion of a basket of 55 'Super Quality Stocks' over the last 10 years on both P/E and EV/EBITDA basis. The 'Super Quality Stocks' basket has been identified based on few parameters of growth, return ratios and quality of business, being reflected in their high valuation multiples
- B. Identifying the inflection point (FY16) for the valuation for this basket and plausible reasons of why we think that FY16 was an inflection
- C. Million-dollar question – How should one look at 'Super Quality Stocks'?
 - a. Red/Green Flag based analysis of 'Super Quality Stocks' basket to identify 'Scary' and 'Relatively Safe' stocks from the basket
- D. Quantifying expected returns of 'Super Quality Stocks' over next 3 years based on optimistic yet sane assumptions
- E. What factors could lead to correction/normalisation in valuation multiples of 'Super Quality Stocks'
- F. Drawing a parallel to US NIFTY50 high quality stock basket of 1970s which famously went into bubble and underperformed in the next 10 years
- G. Multiples of top companies in India are ahead of US and better franchises are available there at nearly half the valuations of 'Super Quality Stocks' basket

Disclosure Note: *Our objective at Monarch AIF is not to signal/suggest a Buy or Sell on any stock mentioned in this note, and we have tried to just analytically discuss our thoughts on the prevailing scenario in the market for 'Super Quality Stocks', and we try to reason for a possible case of irrationality which is apparent in their valuations. We would also like to categorically state that at Monarch AIF we may have had a position in past or may have a position today or may have a position in future in any stock mentioned in this note based on various other reasons/factors if it fits our overall investment strategy.*

A -- Identifying the ‘Scary’ part of ‘Super Quality Stocks’ – The unprecedented valuation expansion!

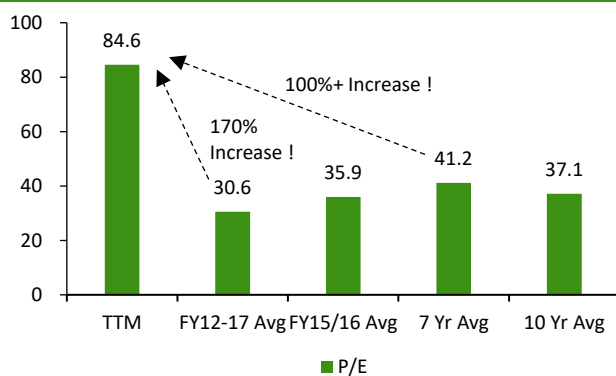
We undertake a simple exercise to measure the magnitude of valuation expansion in high quality stocks in India in the last 7-10 years and try to ascertain if there is an inflection point in this relentless up-move. Our analysis shows that while the valuation expansion of the entire high quality stock basket has been continuous in the last decade, there has been a strong move since FY16 (which according to us is also the inflection point), which has pushed the valuation from “High premium for quality” to “Unsustainable valuation bubble in quality”!

We form a bucket of ‘Super Quality Stocks’ which have the following characteristics: -

1. 7Y EBITDA and 7Y PAT CAGR both above 10% which signifies good growth consistency
2. 7Y Avg ROCE of 15%+ which signifies good capital allocation history
3. TTM P/E of 40x+ and TTM EV/EBITDA of 25x+ (both metrics should clear) which signifies that market has liked these businesses for their quality, governance and growth
4. Mcap above Rs5000cr and reported financial history of at least 10 years

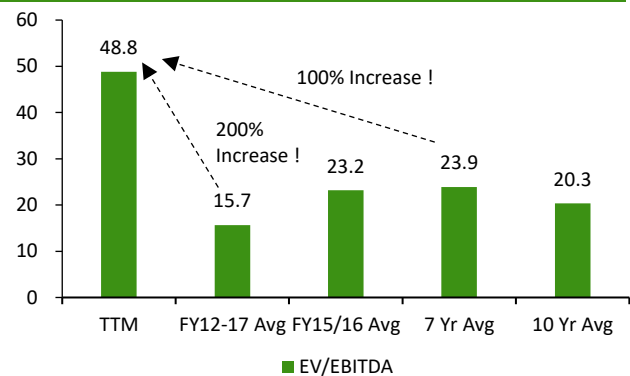
This gives us a basket of 55 ‘Super Quality Stocks’ which is spread across sectors as well as market cap range (Refer Exhibit 13 in Annexure on page 14 for the complete list). These companies have strong governance, solid businesses with good financial track record, decent growth, consistently strong return ratio and high TTM valuation multiples. We track the valuation trajectory of this ‘Super Quality Stocks’ basket and the findings of analysis are self-explanatory in below exhibits.

Exhibit 1: P/E – ‘Super Quality Stocks’ basket



Source: Bloomberg, Monarch AIF

Exhibit 2: EV/EBITDA – ‘Super Quality Stocks’ basket



Source: Bloomberg, Monarch AIF

Key findings: -

1. The 55 stock ‘Super Quality Basket’ is trading at average TTM P/E of 84x and TTM EV/EBITDA of 48x, which is the scary part, and please note that this is not for a small bunch of handful stocks but for a big basket of 55 stocks spread across several sectors (if this doesn’t make your jaw drop to the floor, then be sure that bubble has taken its effect of no valuation looking pricey enough!). As expected, the average multiples for the basket are well above historical averages – this is obviously a well-known fact now in markets, only that it refuses to correct and instead keeps stretching itself as we write this.
2. More importantly, as can be seen in charts the valuation expansion since FY16 has been very sharp whereas FY15-FY16 average multiple as such was more in tune with 7yr/10yr averages. Current valuations for the basket are at a premium of ~100% to their own 7Y averages as well as FY15-16 average, while the premium is even more stark at 170-200% vs. the FY12-17 average valuations for the same basket. **We call FY16 as an inflection point** for the unprecedented expansion of valuation multiple for ‘Super Quality Stocks’ basket and discuss the reasons for the same in Part B of this note below.

3. While we fully appreciate that trailing earnings-based valuation multiples can sometimes be misleading and stocks with even high valuation multiples can still deliver multibaggers returns, investors must be reminded that extremely high valuation multiples do imply very high expectations built by the market on the near as well as long term future earnings potential of the businesses. Many a times those expectations are unrealistic to be met (at least by a large % of the companies in the basket). We have countless instances in the past of stocks correcting even on solid earnings print when the valuations were irrational or out of sync with reality.
4. *Most importantly, no company in this set is a 'new-age' company such as internet businesses/SaaS business and none is a recent listing. These are all well-established businesses with a lengthy track record. Not a single company in the list would warrant a completely different, unconventional valuation paradigm in our view.*

B -- Are there any plausible reasons for FY16 being an inflection point for 'Super Quality Stocks' basket valuation expansion?

We firmly believe that there are some plausible reasons for the large valuation up-move and the overall enormity of unprecedented events post FY16, coupled with strong flows may have led to the creation of valuation bubble in 'Super Quality Stocks' in the last 5 years. We believe that the market as a whole (and more so institutional flows) moved towards large and safe stocks due to following events, which took place in an remarkably synchronised fashion after FY16:

- 1. Demonetisation – Nov 2016** – Large scale disruption in businesses across sectors, thereby triggering flight to safety for institutions to 'Super Quality Stocks', as these businesses were thought to be best placed to tide over the cash crunch crisis and manage supply chains effectively.
- 2. GST Implementation – July 2017** – Expectation of disproportionate benefit for large, organised businesses led by formalisation of the economy and hence flight towards large 'Super Quality Stocks' which were expected to gain market share in the coming years.
- 3. SEBI MF Re-classification – Oct 2017** – Large cap mutual funds required to hold minimum 80% assets in top 100 stocks, while other types of funds retained flexibility to have 35%+ assets in large cap (top 100) stocks if they wished so. This triggered a massive shift to top 100 stocks across funds. Sustenance of strong equity inflows across schemes thereafter made purchases in large stocks more intense in the period that followed. This benefitted the valuations of large and 'Super Quality Stocks'.
- 4. NBFC-IL&FS Crisis – Sep 2018** – Liquidity issues for various businesses and panic in markets triggering another round of institutional buying into perceived safe 'Super Quality Stocks'. *By now the 'safe' word was more of an oxymoron as price-value gap was beginning to be largely unfavourable in these stocks.*
- 5. Covid crisis since March 2020** – Covid crisis led shutdowns and sharp slowdown in GDP meant that market feared sharp fall in growth rates for broader businesses and hence preferred only all-weather safe 'Super Quality Stocks'.

Since the above events were big in magnitude and were uncannily synchronised and closely spaced, the market's flight to safety was relentless (almost forced in some ways), and since the covid crisis is still very much underway, the trend has continued till date! *Hence, while valuations of 'Super Quality Stocks' basket moved only upwards, the earnings of many businesses in this basket became both volatile as well as subdued (as these businesses were also impacted by above macro events). This disconnect has now reached historical proportions and taken shape of a classical bubble marked by extreme irrationality of the market.* Thus, we believe that the strong move since FY16 (inflection point) has pushed the valuation from "High premium for quality" to "Valuation Bubble in Quality"!

Note that we have not even added the impact of MF/PMS industry’s fear of underperformance which has ensured that they don’t avoid these stocks. This in turn has made the valuation matters worse, with short-term performance looking impressive and thus their love for these stocks have reached a new crescendo. *Many fund managers now advocate that valuations don’t matter anymore for some businesses (akin to saying that some Trees can grow to the sky). We as well as some of our saner peers call this “BAAP advice – Buy at any Price advice” which smacks of conformity bias as well as recency bias.*

‘Bubbles are always born with a perfectly rational reason’ – Seth Klarman

C -Million Dollar Question – How should one look at ‘Super Quality Stocks’?

We understand that as money managers we need to have a framework to tackle the issue of w the optimum strategy towards this ‘Super Quality Stocks’ basket, and hence we analytically tackle this issue. While one may feel tempted to advise that the whole basket of ‘Super Quality Stocks’ is untouchable on just valuations alone, **we undertake a detailed analysis based on red flags and green flags** assigned to each stock based on 9 different parameters (which in turn is based on growth, valuations & ROE). The flags are designed to judge the magnitude of valuation excess and not for defining the business quality. The flags used by us are based on below metrics:

Exhibit 3: Flags used for analysis of stocks in ‘Super Quality Stocks’ basket

| Parameter | Comparison Basis* | Red Flag | Green Flag | Remarks |
|--------------------|-------------------------|----------|------------|---|
| P/E Increase | TTM vs 7Y Avg | > 1.4x | <1.15x | More than 40% Expansion in Multiple is Red Flag and less than 15% expansion is Green Flag |
| | TTM vs FY15-16 avg | > 1.4x | <1.15x | |
| EV/EBITDA Increase | TTM vs 7Y Avg | > 1.4x | <1.15x | More than 40% Expansion in Multiple is Red Flag and less than 15% expansion is Green Flag |
| | TTM vs FY15-16 avg | > 1.4x | <1.15x | |
| Earnings Growth | 5Y EBITDA CAGR | <10% | >20% | Earnings CAGR of below 10% for FY17-22* is considered poor and a red flag. Earnings CAGR above 20% is considered a green flag |
| Earnings Growth | 5Y PAT CAGR | <10% | >20% | |
| PEG (x) | TTM PE / 5Y EBITDA CAGR | >4x | <2x | PEG above 4x is considered very high and hence a red flag while PEG below 2x is fair and considered green flag |
| EV/Sales (x) | Current EV/TTM Sales | >5x | <3x | EV/Sales above 5x is considered as red flag |
| Return Ratios | 5Y Avg ROE | <20% | >25% | Quality premium is for very high ROE consistently and hence below 20% avg ROE is taken as Red flag |

*Source: Monarch AIF, *Note – 5Y Earnings CAGR & 5Y Avg ROE as well as TTM ratios are based on FY17-22 Financials where FY22 is based on TTM nos thus factoring H1FY22 results and good TTM earnings instead of the subdued FY21 earnings)*

Based on the above flag-based analysis, we identify two categories of stocks within the basket of 55 ‘Super Quality Stocks’. These are Scary Super Quality Stocks and Relatively Safe Super Quality Stocks.

1. Scary Super Quality Stocks – These stocks have 6 or more RED flags out of 9 parameters used by us, and hence could remain highly susceptible to de-rating, thereby providing low returns and/or time correction. We note that majority of stocks in this category have delivered EBITDA CAGR below 15% in the last 5 years, though they trade at extremely high valuations.

Exhibit 4: Scary Super Quality Stocks – Based on Red Flag Analysis (6 or more Red Flags out of 9)

| Stock | CMP (Rs) | Mkt Cap (Rs Cr) | TTM P/E (x) | TTM EV/EBITDA (x) | Magnitude of Multiple Expansion (Times, x) | | | | 5Y EBITDA CAGR % | 5Y PAT CAGR % | PEG (x) (TTM PE/5yr EBITDA CAGR) | EV/Sales (x) | 5Yr ROE Avg - % | No. of Red Flags |
|-----------------------------------|----------|-----------------|-------------|-------------------|--|-----------|-------------------|-----------|------------------|---------------|----------------------------------|--------------|-----------------|------------------|
| | | | | | TTM vs FY15/16 avg (x) | | TTM vs 7Y Avg (x) | | | | | | | |
| | | | | | P/E | EV/EBITDA | P/E | EV/EBITDA | | | | | | |
| Avenue Supermarts Ltd. | 4,689 | 302,496 | 220 | 137 | 2.8 | 3.1 | 2.2 | 3.3 | 17 | 23 | 12.6 | 10.8 | 22 | 6 |
| GMM Pfaudler Ltd. | 4,905 | 7,121 | 189 | 34 | 10.3 | 3.3 | 6.2 | 1.9 | 33 | 4 | 5.6 | 3.7 | 25 | 6 |
| Qess Corp Ltd. | 850 | 12,646 | 170 | 29 | 2.7 | 0.8 | 1.6 | 1.6 | 13 | (9) | 12.7 | 1.1 | 19 | 6 |
| 3M India Ltd. | 25,094 | 28,538 | 127 | 84 | 2.2 | 2.4 | 1.7 | 1.9 | (2) | (1) | NM | 8.9 | 31 | 8 |
| Relaxo Footwears Ltd. | 1,309 | 32,591 | 112 | 66 | 2.9 | 2.7 | 2.4 | 2.5 | 16 | 19 | 6.8 | 12.3 | 28 | 6 |
| Indian Energy Exchange Ltd. | 253 | 22,718 | 88 | 71 | 2.5 | 3.1 | 2.9 | 3.2 | 17 | 18 | 5.1 | 58.9 | 68 | 6 |
| Page Industries Ltd. | 40,430 | 45,095 | 102 | 68 | 1.8 | 1.7 | 1.6 | 1.7 | 10 | 11 | 10.4 | 13.3 | 62 | 7 |
| Asian Paints Ltd. | 3,391 | 324,396 | 99 | 65 | 2.2 | 2.2 | 1.9 | 2.0 | 10 | 11 | 9.7 | 12.3 | 39 | 6 |
| Pidilite Industries Ltd. | 2,465 | 125,142 | 93 | 62 | 2.4 | 2.4 | 1.9 | 1.8 | 10 | 9 | 9.6 | 13.5 | 37 | 8 |
| Berger Paints India Ltd. | 772 | 74,940 | 89 | 55 | 2.0 | 2.0 | 1.6 | 1.7 | 13 | 14 | 6.6 | 9.1 | 29 | 6 |
| Honeywell Automation India Ltd. | 42,148 | 37,265 | 87 | 67 | 1.9 | 2.2 | 1.7 | 2.0 | 14 | 21 | 6.3 | 12.2 | 29 | 6 |
| Tata Elxsi Ltd. | 5,868 | 36,543 | 80 | 56 | 2.9 | 3.0 | 3.2 | 3.5 | 19 | 21 | 4.3 | 16.8 | 53 | 6 |
| Navin Fluorine International Ltd. | 4,175 | 20,745 | 83 | 62 | 6.5 | 5.0 | 4.2 | 4.1 | 16 | 13 | 5.4 | 15.4 | 21 | 6 |
| Havells India Ltd. | 1,399 | 87,507 | 73 | 48 | 2.2 | 1.9 | 1.7 | 1.7 | 17 | 16 | 4.2 | 7.0 | 27 | 6 |
| Grindwell Norton Ltd. | 1,865 | 21,207 | 75 | 52 | 2.4 | 2.7 | 2.3 | 2.7 | 16 | 18 | 4.8 | 11.0 | 24 | 6 |
| Minda Industries Ltd. | 1,213 | 34,996 | 91 | 39 | 7.6 | 5.8 | 3.5 | 3.5 | 20 | 18 | 4.5 | 4.7 | 19 | 6 |
| Solar Industries India Ltd. | 2,406 | 21,918 | 62 | 37 | 2.0 | 1.8 | 1.9 | 1.8 | 13 | 13 | 4.7 | 7.3 | 23 | 6 |
| L&T Technology Services Ltd. | 5,600 | 59,062 | 71 | 47 | 3.7 | 3.1 | 3.4 | 4.1 | 17 | 14 | 4.2 | 9.8 | 62 | 6 |
| Vinati Organics Ltd. | 1,989 | 20,384 | 69 | 54 | 3.8 | 4.3 | 2.5 | 2.9 | 11 | 16 | 6.0 | 16.0 | 34 | 6 |
| Natco Pharma Ltd. | 904 | 16,486 | 64 | 48 | 1.6 | 2.1 | 2.2 | 2.3 | (13) | (12) | NM | 11.0 | 23 | 8 |
| Sheela Foam Ltd. | 3,234 | 15,735 | 60 | 41 | 1.5 | 1.5 | 1.4 | 1.9 | 14 | 16 | 4.3 | 5.4 | 31 | 6 |
| Kansai Nerolac Paints Ltd. | 590 | 31,826 | 60 | 36 | 2.0 | 1.6 | 1.4 | 1.3 | 3 | 1 | 17.8 | 5.2 | 23 | 7 |
| Voltas Ltd. | 1,219 | 40,346 | 59 | 52 | 2.5 | 2.8 | 2.0 | 2.2 | 6 | 5 | 10.7 | 4.8 | 20 | 7 |
| Syngene International Ltd. | 619 | 24,841 | 61 | 35 | 2.0 | 1.5 | 1.7 | 1.5 | 13 | 7 | 4.9 | 10.0 | 18 | 8 |
| PI Industries Ltd. | 3,034 | 46,031 | 58 | 44 | 2.2 | 2.2 | 1.9 | 2.0 | 13 | 11 | 4.3 | 9.5 | 29 | 6 |
| Marico Ltd. | 515 | 66,214 | 54 | 40 | 1.5 | 1.4 | 1.3 | 1.4 | 7 | 8 | 7.6 | 7.3 | 44 | 6 |
| Godrej Consumer Products Ltd. | 972 | 99,032 | 56 | 40 | 1.6 | 1.4 | 1.4 | 1.3 | 6 | 6 | 10.1 | 8.5 | 21 | 7 |
| Aarti Industries Ltd. | 1,006 | 36,475 | 56 | 33 | 4.4 | 3.4 | 2.7 | 2.5 | 12 | 15 | 4.6 | 7.3 | 18 | 7 |
| Century Plyboards (India) Ltd. | 594 | 13,257 | 47 | 29 | 2.2 | 1.8 | 1.8 | 1.8 | 9 | 8 | 5.5 | 5.0 | 21 | 8 |

Source: Bloomberg, Monarch AIF, 5Y EBITDA & PAT CAGR is based on FY17-22 where for FY22 TTM Nos are considered

We note that many great businesses like Avenue Supermarts, Havells, Asian Paints, Voltas, Pidilite, Berger Paints, Relaxo and many more fall in this category, as they have 6 or more red flags (out of 9), and hence they could be highly susceptible to de-rating, given their astronomical valuations, or they may have to churn higher growth or much higher ROE's soon enough to turn their red flags to green flags. As can be seen in table above, the growth rates for most of these stocks in last 5 years are well below 15% levels, not impressive by any standard. The expected returns from these stocks over the next few years could be humbling (refer section D for some calculations for expected returns based on sane assumptions).

2. Relatively Safe Super Quality Stocks – These stocks have 5 or more GREEN Flags out of 9 parameters used by us and hence could be less susceptible to de-rating. However, they are could only be termed as ‘Relatively safe’ and not completely safe (nothing in the market is, in fact). This list is innocuously small with just 3 stocks qualifying within our ‘Super Quality Stocks’ basket.

Exhibit 5: Relatively Safe Super Quality Stocks – Based on Green Flag Analysis (5 or more Green Flags out of 9)

| Stock | CMP (Rs) | Mkt Cap (Rs Cr) | TTM P/E (x) | TTM EV/EBITDA (x) | Magnitude of Multiple Expansion (Times, x) | | | | 5Y EBITDA CAGR % | 5Y PAT CAGR % | PEG (TTM PE/5yr EBITDA CAGR) | EV/Sales (x) | 5Yr ROE Avg % | No. of Green Flags |
|-----------------------|----------|-----------------|-------------|-------------------|--|-----------|-------------------|-----------|------------------|---------------|------------------------------|--------------|---------------|--------------------|
| | | | | | TTM vs FY16 (x) | | TTM vs 7Y Avg (x) | | | | | | | |
| | | | | | P/E | EV/EBITDA | P/E | EV/EBITDA | | | | | | |
| TTK Prestige Ltd. | 987 | 13,719 | 44.3 | 32.4 | 1.0 | 1.2 | 1.1 | 1.1 | 13.9 | 15.1 | 3.2 | 5.2 | 22.8 | 5 |
| Eicher Motors Ltd. | 2,588 | 70,812 | 44.3 | 29.1 | 1.0 | 1.1 | 1.1 | 1.1 | (0.3) | 1.0 | NM | 6.3 | 38.9 | 5 |
| APL Apollo Tubes Ltd. | 992 | 25,004 | 41.8 | 28.1 | 3.8 | 3.7 | 2.4 | 2.9 | 22.4 | 31.5 | 1.9 | 2.5 | 22.1 | 5 |

Source: Bloomberg, Monarch AIF, 5Y EBITDA & PAT CAGR is based on FY17-22 where for FY22 TTM Nos are considered

Note: The above flag-based analysis done is just for comparison and understanding and in no measure is a recommendation of what investors should do or not do with these stocks. Naturally and more importantly analytically, there are more stocks in the scary category than relatively safe category. We would also like to categorically state that at Monarch AIF, we don’t ignore any stock just because it may land up in the scary category and we may invest in that stock based on various other reasons/factors if it fits our overall investment strategy.

‘Buy not on optimism, but on arithmetic’ – Benjamin Graham

D -- Quantifying expected returns of ‘Super Quality Stocks’

As investors, we understand that valuation is an art and depends on the longevity of growth and ability of businesses to allocate incremental capital for growth at high return on capital. But we also appreciate that the market’s ability to make a very solid judgment on longevity of growth for any business would always remain a constraint in a fast-paced world full of disruptions and high competition. Investors would do well to recall that a 1% increase in WACC in a DCF based valuation could make the fair value of stocks drop by large double-digit magnitudes, and hence the role of multiple based valuations on the medium-term forecastable earnings can’t be shunned altogether to judge the risk-reward in investing.

We estimate expected returns (over next 3 years) from the basket of ‘Super Quality Stocks’ based on optimistic yet sane assumptions. We use EV/EBITDA as valuation tool for our analysis as we believe that it is a more robust parameter vs P/E, since it factors in the EV of the business and less volatile EBITDA on the earnings front. We derive expected 3 year CAGR returns for stocks assuming 20% EBITDA CAGR (for next 3 years applied on TTM EBITDA) and reversion of EV/EBITDA multiple to a level of 10% premium to its 7Y average multiple by end of next 3 years. *The reversion of multiples to those levels is not a pessimistic assumption by any means (one may ask that why multiples would correct at all – we list some plausible factors for that in next section).* We appreciate the fact that some companies might deliver higher than 20% EBITDA CAGR over next 3-5 years and hence could see better sustenance in multiples but that set could be small.

Exhibit 6: Expected returns from ‘Super Quality stocks’

| Stock (Rs Cr) | TTM EBITDA | 3Y Fwd EBITDA@20% CAGR | Ascribed 3Y Fwd EV/EBITDA - 10% premium to 7Y avg | 3Y Fwd EV | 3Y Fwd Mcap | Current Mcap | 3Y Expected Stock Price CAGR - % | No. of Red Flags (out of 9) |
|---|------------|------------------------|---|-----------|-------------|--------------|----------------------------------|-----------------------------|
| Scary Super Quality Stocks | | | | | | | | |
| Avenue Supermarts Ltd. | 2,195 | 3,792 | 46 | 172,554 | 173,587 | 302,496 | -16.9 | 6 |
| GMM Pfaudler Ltd. | 201 | 348 | 20 | 6,969 | 7,166 | 7,121 | 0.2 | 6 |
| Qess Corp Ltd. | 448 | 774 | 20 | 15,526 | 15,263 | 12,646 | 6.5 | 6 |
| 3M India Ltd. | 334 | 577 | 50 | 28,869 | 29,302 | 28,538 | 0.9 | 8 |
| Relaxo Footwears Ltd. | 495 | 855 | 29 | 24,451 | 24,563 | 32,591 | -9.0 | 6 |
| Indian Energy Exchange Ltd. | 317 | 548 | 24 | 13,187 | 13,478 | 22,718 | -16.0 | 6 |
| Page Industries Ltd. | 664 | 1,147 | 45 | 52,004 | 51,907 | 45,095 | 4.8 | 7 |
| Asian Paints Ltd. | 4,924 | 8,509 | 37 | 311,096 | 315,243 | 324,396 | -0.9 | 6 |
| Pidilite Industries Ltd. | 1,999 | 3,454 | 37 | 128,805 | 130,821 | 125,142 | 1.5 | 8 |
| Berger Paints India Ltd. | 1,343 | 2,321 | 36 | 83,638 | 84,115 | 74,940 | 3.9 | 6 |
| Honeywell Automation India Ltd. | 541 | 934 | 37 | 34,414 | 35,537 | 37,265 | -1.6 | 6 |
| Tata Elxsi Ltd. | 641 | 1,108 | 17 | 19,363 | 19,858 | 36,543 | -18.4 | 6 |
| Navin Fluorine International Ltd. | 327 | 565 | 17 | 9,404 | 9,984 | 20,745 | -21.6 | 6 |
| Havells India Ltd. | 1,819 | 3,142 | 31 | 97,696 | 98,320 | 87,507 | 4.0 | 6 |
| Grindwell Norton Ltd. | 399 | 689 | 21 | 14,813 | 15,089 | 21,207 | -10.7 | 6 |
| Minda Industries Ltd. | 940 | 1,625 | 12 | 19,790 | 18,477 | 34,996 | -19.2 | 6 |
| Solar Industries India Ltd. | 603 | 1,042 | 23 | 24,046 | 23,794 | 21,918 | 2.8 | 6 |
| L&T Technology Services Ltd. | 1,236 | 2,135 | 13 | 26,973 | 27,512 | 59,062 | -22.5 | 6 |
| Vinati Organics Ltd. | 374 | 646 | 21 | 13,390 | 13,601 | 20,384 | -12.6 | 6 |
| Natco Pharma Ltd. | 339 | 586 | 22 | 13,176 | 13,434 | 16,486 | -6.6 | 8 |
| Kansai Nerolac Paints Ltd. | 871 | 1,505 | 30 | 45,523 | 45,932 | 31,826 | 13.0 | 7 |
| Voltas Ltd. | 742 | 1,281 | 27 | 33,965 | 35,884 | 40,346 | -3.8 | 7 |
| Syngene International Ltd. | 695 | 1,200 | 26 | 31,217 | 31,677 | 24,841 | 8.4 | 8 |
| PI Industries Ltd. | 1,044 | 1,804 | 24 | 43,166 | 42,762 | 46,031 | -2.4 | 6 |
| Marico Ltd. | 1,636 | 2,827 | 32 | 91,321 | 91,705 | 66,214 | 11.5 | 6 |
| Godrej Consumer Products Ltd. | 2,502 | 4,323 | 33 | 143,962 | 142,842 | 99,032 | 13.0 | 7 |
| Aarti Industries Ltd. | 1,169 | 2,020 | 15 | 29,359 | 27,543 | 36,475 | -8.9 | 7 |
| Century Plyboards (India) Ltd. | 470 | 811 | 17 | 13,936 | 13,782 | 13,257 | 1.3 | 8 |
| Relatively Safe Super Quality Stocks | | | | | | | | |
| TTK Prestige Ltd. | 418 | 722 | 30 | 21,791 | 21,978 | 13,719 | 17.0 | 4 |
| Eicher Motors Ltd. | 2,139 | 3,697 | 29 | 105,545 | 114,034 | 70,812 | 17.2 | 5 |

| | | | | | | | | |
|-----------------------|-----|-------|----|--------|--------|--------|-------|---|
| APL Apollo Tubes Ltd. | 915 | 1,582 | 11 | 16,931 | 16,192 | 25,004 | -13.5 | 5 |
|-----------------------|-----|-------|----|--------|--------|--------|-------|---|

Source: Bloomberg, Monarch AIF

From the above table, we note the possible returns of both category stocks: -

- i. 'Scary' basket might give single digit to negative CAGR over the next 3 years for a majority of stocks
- ii. 'Relatively Safe' basket could be a mixed bag, but is also highly susceptible, since the future exit multiple assumed (based on past) is yet very high
- iii. **44 stocks out of 55 in our overall super quality stocks basket end with return CAGR of less than 10% despite these aggressive assumptions (Refer exhibit 14 in annexure)**

'When prices are high, it's inescapable that prospective returns are low (and risks are high)' – Howard Marks

E -- What factors could lead to correction/normalisation in valuation multiples of 'Super Quality Stocks'

We believe that just as there were strong reasons (led by unprecedented events in synchronised manner) for the continuous increase in valuations for 'Super Quality Stocks', there would be similar reasons for its normalisation towards its long-term averages or even towards a new normal. These could be:

1. **Repeated earnings disappointments vs lofty expectations** – Earnings growth expectations for 'Super Quality Stocks' would remain very high (given the valuations) and there could be a time when all types of earnings (low as well as high) would just appear disappointing to the market leading to de-rating. This disappointment could be on account of in-built multiple led high growth expectations, in our view. As it happened with the IT sector during 2002-05, growth of 25-30% during certain periods used to lead to stock corrections (due to higher expectations and multiples). We note that Zoom video communications in US has gone down substantially in the last 6 months despite earnings coming at record every quarter, as valuation normalisation has begun in those type of stocks in the US.
2. **Tightening of liquidity conditions at global level and FED interest rate hikes leading to restricted inflows, particularly the passive ETF flows** – We believe that 'Super Quality Stocks' have been a great hiding place for both FIIs and DIIs alike in the last 5 years, with low risk of big disappointment in earnings, and generally sound corporate governance. Additionally, since majority of 'Super Quality Stocks' are among the top 250 stocks in the listed universe, they have further benefitted from passive ETF flows into various indices. However, as the world exits the easy liquidity conditions and interest rates get hiked globally in next 2 years, the inflows would be forced to make an intelligent choice of being deployed with more risk-reward objectivity and not just in great hiding places. The broad basing of the Indian economy and opening of new investment options in the listed space by way of listing of new businesses, as well as revival of traditional sectors across manufacturing, infra, capital goods, logistics, power and financial services could also lead to more options for the flows to get absorbed, and lead to the much-awaited normalisation of multiples of 'Super Quality Stocks'.
3. **Market mood swing towards value stocks and/or other quality stocks at lower valuations** – Market mood could gradually swing towards value stocks within the top 200/500 stocks, and once 'Super Quality Stocks' start faltering in returns, the vice-versa loop could accelerate the normalisation on the way down. Markets are also beginning to note that many other solid businesses, with high-quality financials and capital allocation are available at much cheaper valuations, and could see shift towards those names. There could even be a shift within the quality names from the current breed of "Super Quality" to another section of quality at relatively better valuation.

'Mean reversion is one of the great truism of capitalism' – Anthony Bolton

F -- Drawing parallel to US NIFTY50 high quality stock basket of 1970s which famously went into bubble and underperformed in next 10 years

About NIFTY50 stocks of 1970s in US

The 50 stocks in US identified by Morgan Guaranty Trust represented some of the fastest-growing high quality large-sized companies in existence in the latter half of the 1960s. Their popularity among institutional and individual investors sparked a radical shift from “value” investing to a “growth at any price” style of investing. One of the most important reasons for the popularity of these companies was that they had strong business franchises which would earn them high returns on capital for the foreseeable future. Also, they were displaying an above-average growth track record.

To quote the Forbes magazine: *“The delusion was that these companies were so good, it didn’t matter what you paid for them; their inexorable growth would bail you out. Obviously, the problem was not with the companies but with the temporary insanity of money managers — proving again that stupidity well-packaged can sound like wisdom. It was so easy to forget that no sizable company could possibly be worth over 50 times normal earnings.”*

The Nifty Fifty bubble was marked by its high P/E. By 1972 when the S&P 500 Index’s P/E stood at a then lofty 19x, the Nifty Fifty’s average P/E was more than twice that at 42x. Remarkably, the 55 stock bucket selected by us trades at an even higher TTM P/E of 84x while NIFTY index trades at a TTM P/E of lofty 25x too! The similarity is striking, to say the least.

What happened to US NIFTY50 stocks – Correction, of course (both time and value)

The long bear market of the 1970s which began with the 1973–74 stock market crash and lasted until 1982 caused valuations of the nifty fifty to fall to low levels along with the rest of the market, with most of these stocks underperforming the broader market averages. The next 10 year returns were low single digits for majority of stocks of the NIFTY50 basket.

Exhibit 7: NIFTY 50 Stocks in US in 1970s

| "Cheap" Nifty Fifty Stocks | | | | | | |
|----------------------------|--------|--------------|-------------------------------------|--------|--------|--------|
| Company | Symbol | Starting P/E | Subsequent Annualized Total Returns | | | |
| | | | 10-yr | 20-yr | 30-yr | 40-yr |
| Philip Morris | MO | 25.9 | 6.85% | 18.71% | 16.94% | 16.53% |
| Bristol-Myers | BMJ | 27.6 | 5.35% | 13.10% | 11.76% | 10.17% |
| Pfizer | PFE | 29 | 2.63% | 11.41% | 14.45% | 10.40% |
| Pepsico | PEP | 29.3 | 2.83% | 13.55% | 13.63% | 11.42% |
| Procter & Gamble | PG | 32 | -1.59% | 8.57% | 10.76% | 9.50% |
| IBM | IBM | 37.4 | -2.53% | 1.95% | 6.14% | 7.20% |
| Dow Chemical | DWDP | 25.5 | -0.85% | 8.50% | 8.74% | 7.22% |

| "Expensive" Nifty Fifty Stocks | | | | | | |
|--------------------------------|--------|--------------|-------------------------------------|--------|--------|--------|
| Company | Symbol | Starting P/E | Subsequent Annualized Total Returns | | | |
| | | | 10-yr | 20-yr | 30-yr | 40-yr |
| McDonald's | MCD | 85.7 | 1.75% | 12.06% | 11.53% | 12.17% |
| Int'l Flavors & Fragrances | IFF | 75.8 | -5.24% | 6.93% | 5.50% | 5.87% |
| Walt Disney | DIS | 81.6 | -3.78% | 10.81% | 9.40% | 9.12% |
| Johnson & Johnson | JNJ | 61.9 | 1.72% | 10.48% | 13.38% | 10.62% |
| Coca Cola | KO | 47.6 | -6.93% | 11.83% | 11.52% | 9.98% |
| Eli Lilly | LLY | 46 | -0.72% | 8.26% | 11.17% | 7.99% |
| Merck | MRK | 45.9 | -0.23% | 14.31% | 13.11% | 9.75% |

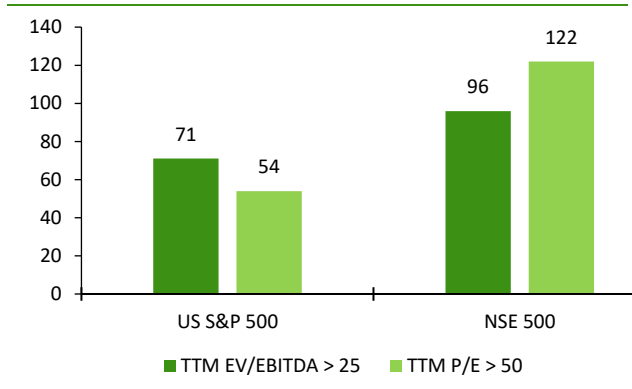
Start date 6/1/72 Sources: Brooklyn Investor; Morningstar

Source: Media articles, Monarch AIF

G – Multiples of top companies in India are ahead of US and better franchises are available there at nearly half valuations of ‘Super Quality Stocks’ basket

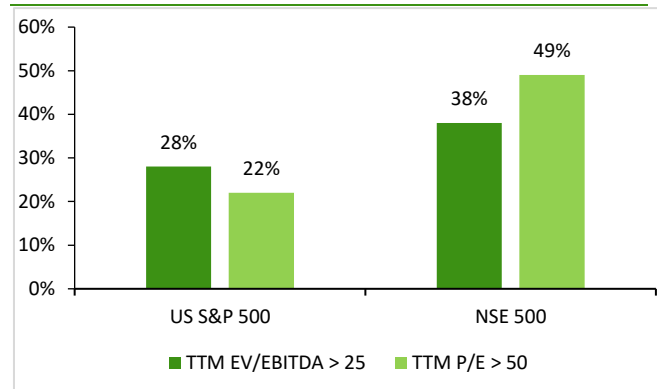
We note that valuations of top 250 non-financial companies in India is well ahead of top 250 non-financial companies in US despite the strong winning streak of S&P500 in US for the last 3 years. Also, if high quality businesses with good moats and sustained high growth can be bought at any valuation for 5-10 years holding period to get handsome returns at low risk, then one would be better off taking exposure to some of the best franchises in US, which would grow earnings at 10-20% annually in all probability for next 5-10-15 years. We further note that some of the best investors of US (Buffett/Munger) have been sitting on ever increasing cash pile in the last 6-7 years and not given into this buying at any price (BAAP) philosophy for good companies. *This is worth a mention since the idle cash yields very little in US and the ‘Super Quality Franchises’ available in US are in many cases much better global brands, have stronger business models, have better growth track records and available at half the valuations (EV/EBITDA basis) at which some of the India’s ‘Super Quality Stocks’ are selling at.* As can be seen in charts below, some of the best companies in US are available at less than 25x EV/EBITDA (which is almost half of average valuation of our ‘Super quality stocks’ basket) and same principles of longevity of earnings and high quality are applicable to them.

Exhibit 8: Valuation of Top 250 non-fin stocks – India vs US



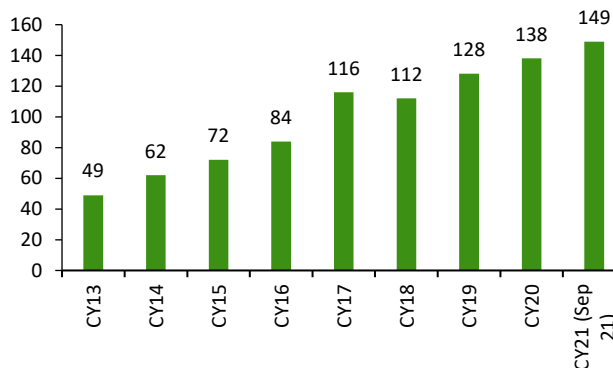
Source: Bloomberg, Monarch AIF

Exhibit 9: Larger % of top 250 non-fin stocks trade at high valuations in India vs US



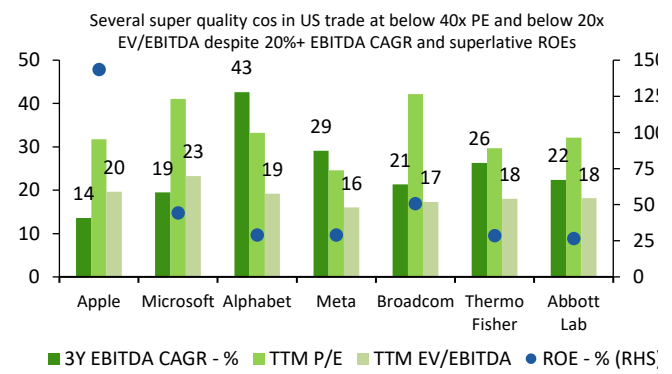
Source: Bloomberg, Monarch AIF

Exhibit 10: Berkshire’s cash pile keeps rising (USD bn)



Source: Bloomberg, Monarch AIF

Exhibit 11: Valuations of few high-quality stocks in US



Source: Bloomberg, Monarch AIF

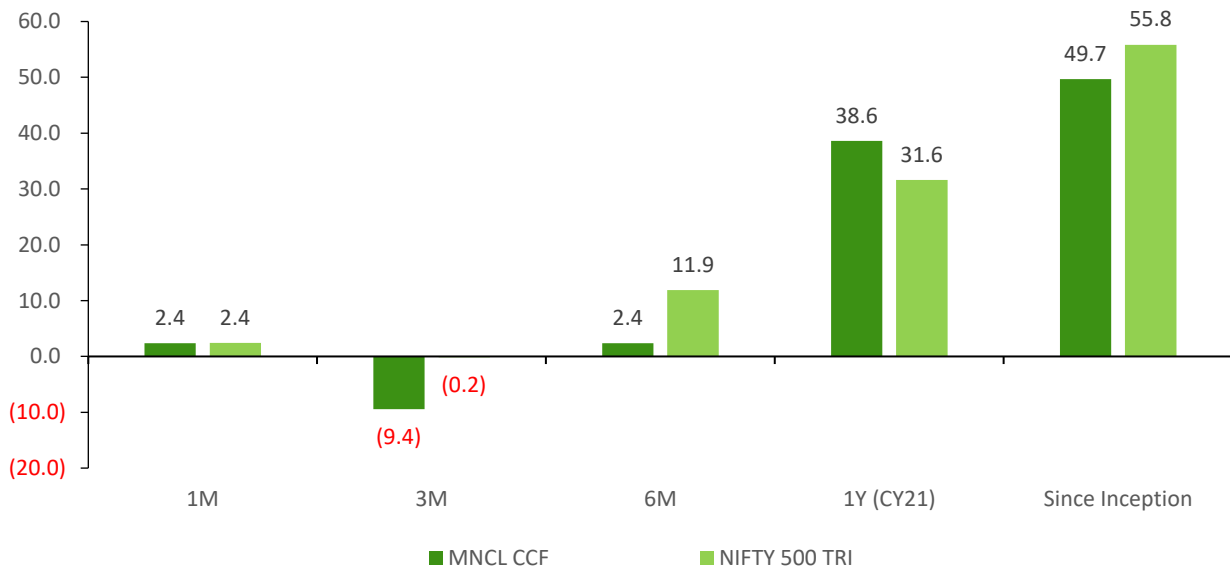
‘In investing, what is comfortable is rarely profitable’ – Robert Arnott

H -- Portfolio performance – MNCL Capital Compounder Fund

We present the performance of MNCL Capital Compounder Fund below. As at end-Dec 2021, the fund was 91% invested into equities and the balance 9% was held in liquid/cash instruments. The fund mix in terms of large cap/midcap/small cap stocks stood at 23%/28%/41% as per SEBI classification. We have increased our allocation to BFSI stocks in the last few months, driven by continuous improvement in asset quality metrics, recovery in economy post pick-up in vaccination rates and expected strong pick-up in growth ahead led by credit cycle recovery, NIM expansion and lower credit costs. We also see valuation multiples across the BFSI space being more comfortable vs. the broader market, providing a good margin of safety.

We admit that the fund performance in the last 3 months has been lacklustre and the fund's absolute returns since inception have dropped from 65.3% at Sep-end to 49.7% at Dec-end. While this is partly due to correction in some of the stocks that we hold (particularly BFSI stocks) but it is also due to the charging of annual performance fees by the fund in October (upon completion of one year). We remain highly confident on the portfolio positioning which consists of growing good quality businesses trading at attractive valuations. As at Dec-end, the aggregate TTM P/E for the portfolio stood at 18.4x and FY23E P/E stood at 16x with expected EPS CAGR of 20%+ over FY21-24E for the portfolio on aggregate basis.

Exhibit 12: Portfolio Performance (as at end-Dec 2021 - % change)*



*Source: CAMS FA, Monarch AIF, Note: i) Inception date is 23 Oct 2020, ii) Returns as on 31 Dec 2021, iii) Returns are net of fees and transaction costs and includes dividend income, iv) NIFTY 500 total return index considered for comparison, *Please refer the disclaimer*

We once again thank you for your investment and trust in Monarch AIF. We immensely value your collective belief in our ability to make the optimal investment decisions on your behalf through our fund.

Please refer our previous newsletters below:

October 2021: The formal engine is beginning to whizz - <https://bit.ly/3B0nHyA>

July 2021: The mine or the axe – playing the commodity sweepstakes - <https://bit.ly/3h6qheU>

April 2021: The eye of the Tiger – On deals in listed space - <https://bit.ly/2OihEIT>

January 2021: Terra Mollis vs Terra Firma – separated by data – <http://bit.ly/2WVvmzd4>

We would be happy to hear your feedback and/or any queries.

Warm Regards
 Abhisar Jain, CFA
 Fund Manager
 Monarch AIF

Annexure

Exhibit 13: List of 'Super Quality stocks' basket of 55 stocks

| S.No | Stock Name | Sector | CMP (Rs) | Mkt Cap (Rs Cr) | TTM P/E (x) | TTM EV/EBIT DA (x) | 7 Yr EBITDA CAGR % | 7 Yr PAT CAGR % | 7 Yr Avg ROCE % | (X) times | |
|----------------------|--|--------------------------|----------|-----------------|-------------|--------------------|--------------------|-----------------|-----------------|---------------------------------|---------------------------------------|
| | | | | | | | | | | P/E Expansion - TTM vs 7 Yr Avg | EV/EBITDA Expansion - TTM vs 7 Yr Avg |
| 1 | Hindustan Unilever Ltd. | FMCG | 2,364 | 554,445 | 65.9 | 45.1 | 13.7 | 11.5 | 104.4 | 1.3 | 1.3 |
| 2 | Asian Paints Ltd. | Chemicals | 3,391 | 324,396 | 99.0 | 65.0 | 13.5 | 14.0 | 39.3 | 1.9 | 2.0 |
| 3 | Avenue Supermarts Ltd. | Retailing | 4,689 | 302,496 | 220.2 | 137.4 | 26.2 | 31.5 | 21.7 | 2.2 | 3.3 |
| 4 | Larsen & Toubro Infotech Ltd. | IT | 7,349 | 128,406 | 60.8 | 44.5 | 14.7 | 15.7 | 45.4 | 3.4 | 3.3 |
| 5 | Pidilite Industries Ltd. | Chemicals | 2,465 | 125,142 | 93.3 | 61.6 | 14.0 | 13.9 | 36.5 | 1.9 | 1.8 |
| 6 | Divi's Laboratories Ltd. | Healthcare | 4,680 | 124,189 | 58.1 | 39.6 | 16.0 | 14.4 | 29.3 | 2.0 | 2.0 |
| 7 | Godrej Consumer Products Ltd. | FMCG | 972 | 99,032 | 56.3 | 40.0 | 10.8 | 11.4 | 21.0 | 1.4 | 1.3 |
| 8 | Britannia Industries Ltd. | FMCG | 3,605 | 86,874 | 55.0 | 38.2 | 21.9 | 24.6 | 52.0 | 1.2 | 1.2 |
| 9 | Havells India Ltd. | Capital Goods | 1,399 | 87,507 | 73.4 | 47.8 | 11.5 | 12.9 | 26.8 | 1.7 | 1.7 |
| 10 | Mindtree Ltd. | IT | 4,786 | 78,777 | 56.8 | 40.3 | 15.3 | 13.7 | 31.5 | 2.9 | 3.3 |
| 11 | Berger Paints India Ltd. | Chemicals | 772 | 74,940 | 88.8 | 55.4 | 15.6 | 16.5 | 29.5 | 1.6 | 1.7 |
| 12 | Eicher Motors Ltd. | Automobile & Ancillaries | 2,588 | 70,812 | 44.3 | 29.1 | 14.0 | 14.0 | 38.9 | 1.1 | 1.1 |
| 13 | Marico Ltd. | FMCG | 515 | 66,214 | 54.3 | 40.2 | 11.6 | 13.1 | 43.6 | 1.3 | 1.4 |
| 14 | Mphasis Ltd. | IT | 3,412 | 63,691 | 48.1 | 32.5 | 22.7 | 21.7 | 20.8 | 3.1 | 3.3 |
| 15 | L&T Technology Services Ltd.* | IT | 5,600 | 59,062 | 71.2 | 47.4 | 15.9 | 13.5 | 34.3 | 3.4 | 4.1 |
| 16 | Jubilant FoodWorks Ltd. | FMCG | 3,606 | 47,382 | 115.6 | 45.3 | 17.5 | 10.0 | 32.4 | 1.4 | 1.5 |
| 17 | PI Industries Ltd. | Chemicals | 3,034 | 46,031 | 58.3 | 44.5 | 19.6 | 21.5 | 29.4 | 1.9 | 2.0 |
| 18 | Page Industries Ltd. | Textile | 40,430 | 45,095 | 102.3 | 68.1 | 10.9 | 12.0 | 61.7 | 1.6 | 1.7 |
| 19 | Astral Ltd. | Plastic Products | 2,299 | 45,901 | 88.3 | 58.3 | 22.6 | 26.7 | 23.3 | 1.7 | 2.0 |
| 20 | Voltas Ltd. | Consumer Durables | 1,219 | 40,346 | 58.8 | 51.8 | 13.4 | 14.3 | 20.3 | 2.0 | 2.2 |
| 21 | Abbott India Ltd. | Healthcare | 19,472 | 41,377 | 57.7 | 40.7 | 19.3 | 19.5 | 38.0 | 1.6 | 1.7 |
| 22 | Honeywell Automation India Ltd. | Consumer Durables | 42,148 | 37,265 | 86.5 | 66.8 | 26.2 | 27.0 | 29.4 | 1.7 | 2.0 |
| 23 | Aarti Industries Ltd. | Chemicals | 1,006 | 36,475 | 56.1 | 32.8 | 13.6 | 19.7 | 17.7 | 2.7 | 2.5 |
| 24 | Tata Elxsi Ltd. | IT | 5,868 | 36,543 | 79.6 | 56.2 | 24.5 | 26.2 | 53.3 | 3.2 | 3.5 |
| 25 | Minda Industries Ltd. | Automobile & Ancillaries | 1,213 | 34,996 | 90.8 | 38.6 | 42.9 | 75.6 | 18.8 | 3.5 | 3.5 |
| 26 | Dixon Technologies (India) Ltd. | Consumer Durables | 5,524 | 32,724 | 175.3 | 96.8 | 41.7 | 42.4 | 29.8 | 3.3 | 5.8 |
| 27 | Kansai Nerolac Paints Ltd. | Chemicals | 590 | 31,826 | 60.4 | 36.1 | 13.0 | 14.1 | 23.4 | 1.4 | 1.3 |
| 28 | Relaxo Footwears Ltd. | FMCG | 1,309 | 32,591 | 111.7 | 65.7 | 19.0 | 23.7 | 27.8 | 2.4 | 2.5 |
| 29 | Dr. Lal Pathlabs Ltd. | Healthcare | 3,808 | 31,859 | 77.5 | 53.0 | 17.8 | 20.5 | 41.7 | 1.6 | 1.7 |
| 30 | 3M India Ltd. | Diversified | 25,094 | 28,538 | 127.3 | 84.1 | 12.8 | 20.9 | 30.8 | 1.7 | 1.9 |
| 31 | Hatsun Agro Product Ltd. | FMCG | 1,262 | 27,193 | 102.7 | 35.7 | 23.5 | 17.1 | 17.5 | 1.3 | 1.7 |
| 32 | Crompton Greaves Consumer Electricals Ltd.* | Consumer Durables | 439 | 27,445 | 42.0 | 35.3 | 9.6 | 18.1 | 59.6 | 1.2 | 1.7 |
| 33 | Schaeffler India Ltd. | Automobile & Ancillaries | 8,790 | 27,480 | 47.4 | 29.2 | 16.5 | 13.2 | 22.7 | 1.5 | 1.6 |
| 34 | APL Apollo Tubes Ltd. | Iron & Steel | 992 | 25,004 | 41.8 | 28.1 | 22.4 | 31.8 | 22.1 | 2.4 | 2.9 |
| 35 | Syngene International Ltd. | Miscellaneous | 619 | 24,841 | 61.1 | 35.1 | 17.3 | 16.1 | 18.2 | 1.7 | 1.5 |
| 36 | Indian Energy Exchange Ltd. | Power | 253 | 22,718 | 87.9 | 70.8 | 11.9 | 12.1 | 68.0 | 2.9 | 3.2 |
| 37 | Solar Industries India Ltd. | Chemicals | 2,406 | 21,918 | 62.2 | 36.8 | 14.0 | 11.3 | 22.6 | 1.9 | 1.8 |
| 38 | Navin Fluorine International Ltd. | Chemicals | 4,175 | 20,745 | 83.4 | 61.7 | 24.7 | 23.3 | 21.1 | 4.2 | 4.1 |
| 39 | Grindwell Norton Ltd. | Abrasives | 1,865 | 21,207 | 75.5 | 52.5 | 12.4 | 15.9 | 24.0 | 2.3 | 2.7 |
| 40 | Vinati Organics Ltd. | Chemicals | 1,989 | 20,384 | 68.6 | 54.0 | 12.7 | 17.7 | 34.3 | 2.5 | 2.9 |
| 41 | Alkyl Amines Chemicals Ltd. | Chemicals | 3,526 | 18,117 | 58.5 | 41.1 | 26.1 | 31.6 | 31.8 | 3.8 | 4.2 |
| 42 | Natco Pharma Ltd. | Healthcare | 904 | 16,486 | 64.3 | 47.9 | 19.0 | 24.0 | 23.3 | 2.2 | 2.3 |
| 43 | Sheela Foam Ltd. | FMCG | 3,234 | 15,735 | 60.4 | 41.4 | 24.8 | 36.0 | 30.9 | 1.4 | 1.9 |
| 44 | Timken India Ltd. | Automobile & Ancillaries | 1,988 | 14,954 | 66.2 | 39.9 | 19.8 | 18.1 | 22.9 | 1.6 | 1.7 |
| 45 | TTK Prestige Ltd. | Consumer Durables | 987 | 13,719 | 44.3 | 32.4 | 10.0 | 11.4 | 22.8 | 1.1 | 1.2 |
| 46 | Century Plyboards (India) Ltd. | Construction Materials | 594 | 13,257 | 46.8 | 28.6 | 11.3 | 17.8 | 20.8 | 1.8 | 1.8 |
| 47 | Zydus Wellness Ltd. | FMCG | 1,888 | 12,005 | 41.8 | 36.6 | 21.2 | 11.2 | 18.0 | 1.2 | 1.2 |
| 48 | Qess Corp Ltd. | Miscellaneous | 850 | 12,646 | 170.1 | 28.8 | 41.7 | 18.7 | 18.6 | 1.6 | 1.6 |
| 49 | Saregama India Ltd. | Media & Entertainment | 5,282 | 10,125 | 77.9 | 64.9 | 33.3 | 31.2 | 20.2 | 3.0 | 2.5 |
| 50 | V-Guard Industries Ltd. | Capital Goods | 222 | 9,553 | 41.3 | 25.5 | 14.3 | 16.3 | 30.3 | 1.0 | 0.9 |
| 51 | Poly Medicure Ltd. | Healthcare | 970 | 9,179 | 62.8 | 42.7 | 16.2 | 19.8 | 24.9 | 2.0 | 2.4 |
| 52 | HLE Glascoat Ltd. | Capital Goods | 5,811 | 7,941 | 127.5 | 79.3 | 37.2 | 45.8 | 29.3 | 8.2 | 9.4 |
| 53 | GMM Pfaudler Ltd. | Capital Goods | 4,905 | 7,121 | 188.6 | 34.4 | 22.6 | 24.0 | 24.7 | 6.2 | 1.9 |
| 54 | TeamLease Services Ltd. | Miscellaneous | 4,169 | 7,109 | 340.9 | 61.8 | 29.1 | 24.3 | 18.1 | 5.7 | 1.3 |
| 55 | Johnson Controls - Hitachi Air Conditioning India Ltd. | Consumer Durables | 1,979 | 5,380 | 97.7 | 34.9 | 13.1 | 19.7 | 19.7 | 1.2 | 1.1 |
| Total Average | | | | | 84.6 | 48.8 | 19.2 | 20.8 | 31.3 | 2.3 | 2.3 |

Source: Bloomberg, Monarch AIF, *CAGR is 6 years for L&T Tech & 5 years for Crompton, 7Yr data is FY14-21, TTM is 12M ending Sep'21, CMP is 31 Dec 2021

Exhibit 14: Expected returns of 'Super Quality stocks' basket based on 20% EBITDA CAGR

| Stock (Rs Cr) | TTM EBITDA | 3Y Fwd EBITDA@20% CAGR | Ascribed 3Y Fwd EV/EBITDA - 10% premium to 7Y avg | 3Y Fwd EV | 3Y Fwd Mcap | Current Mcap | 3Y Expected Stock Price CAGR - % | No. of Red Flags (out of 9) | No. of Green Flags (out of 9) |
|--|------------|------------------------|---|-----------|-------------|--------------|----------------------------------|-----------------------------|-------------------------------|
| TeamLease Services Ltd. | 115 | 198 | 54 | 10774 | 10796 | 7109 | 14.9 | 5 | 2 |
| Avenue Supermarts Ltd. | 2,195 | 3,792 | 46 | 172554 | 173587 | 302496 | -16.9 | 6 | 3 |
| GMM Pfaudler Ltd. | 201 | 348 | 20 | 6969 | 7166 | 7121 | 0.2 | 6 | 2 |
| Dixon Technologies (India) Ltd. | 338 | 584 | 18 | 10670 | 10657 | 32724 | -31.2 | 5 | 3 |
| Qess Corp Ltd. | 448 | 774 | 20 | 15526 | 15263 | 12646 | 6.5 | 6 | 2 |
| HLE Glascoat Ltd. | 102 | 176 | 9 | 1625 | 1511 | 7941 | -42.5 | 5 | 3 |
| 3M India Ltd. | 334 | 577 | 50 | 28869 | 29302 | 28538 | 0.9 | 8 | 1 |
| Jubilant FoodWorks Ltd. | 1,030 | 1,781 | 33 | 57930 | 58648 | 47382 | 7.4 | 2 | 3 |
| Relaxo Footwears Ltd. | 495 | 855 | 29 | 24451 | 24563 | 32591 | -9.0 | 6 | 3 |
| Hatsun Agro Product Ltd. | 783 | 1,354 | 23 | 31445 | 30656 | 27193 | 4.1 | 4 | 1 |
| Indian Energy Exchange Ltd. | 317 | 548 | 24 | 13187 | 13478 | 22718 | -16.0 | 6 | 3 |
| Page Industries Ltd. | 664 | 1,147 | 45 | 52004 | 51907 | 45095 | 4.8 | 7 | 1 |
| Johnson Controls - Hitachi Air Conditioning India Ltd. | 155 | 268 | 35 | 9323 | 9282 | 5380 | 19.9 | 5 | 2 |
| Asian Paints Ltd. | 4,924 | 8,509 | 37 | 311096 | 315243 | 324396 | -0.9 | 6 | 1 |
| Pidilite Industries Ltd. | 1,999 | 3,454 | 37 | 128805 | 130821 | 125142 | 1.5 | 8 | 1 |
| Astral Ltd. | 787 | 1,361 | 31 | 42688 | 42660 | 45901 | -2.4 | 5 | 3 |
| Berger Paints India Ltd. | 1,343 | 2,321 | 36 | 83638 | 84115 | 74940 | 3.9 | 6 | 1 |
| Honeywell Automation India Ltd. | 541 | 934 | 37 | 34414 | 35537 | 37265 | -1.6 | 6 | 2 |
| Tata Elxsi Ltd. | 641 | 1,108 | 17 | 19363 | 19858 | 36543 | -18.4 | 6 | 3 |
| Navin Fluorine International Ltd. | 327 | 565 | 17 | 9404 | 9984 | 20745 | -21.6 | 6 | 2 |
| Saregama India Ltd. | 156 | 269 | 28 | 7644 | 7660 | 10125 | -8.9 | 5 | 4 |
| Havells India Ltd. | 1,819 | 3,142 | 31 | 97696 | 98320 | 87507 | 4.0 | 6 | 3 |
| Grindwell Norton Ltd. | 399 | 689 | 21 | 14813 | 15089 | 21207 | -10.7 | 6 | 3 |
| Dr. Lal Pathlabs Ltd. | 591 | 1,022 | 34 | 34665 | 35200 | 31859 | 3.4 | 5 | 3 |
| Minda Industries Ltd. | 940 | 1,625 | 12 | 19790 | 18477 | 34996 | -19.2 | 6 | 2 |
| Solar Industries India Ltd. | 603 | 1,042 | 23 | 24046 | 23794 | 21918 | 2.8 | 6 | 1 |
| L&T Technology Services Ltd. | 1,236 | 2,135 | 13 | 26973 | 27512 | 59062 | -22.5 | 6 | 2 |
| Vinati Organics Ltd. | 374 | 646 | 21 | 13390 | 13601 | 20384 | -12.6 | 6 | 2 |
| Timken India Ltd. | 370 | 640 | 25 | 16117 | 16282 | 14954 | 2.9 | 5 | 3 |
| Hindustan Unilever Ltd. | 12,153 | 21,000 | 39 | 812891 | 819727 | 554445 | 13.9 | 4 | 1 |
| Poly Medicare Ltd. | 218 | 377 | 20 | 7459 | 7316 | 9179 | -7.3 | 5 | 3 |
| Natco Pharma Ltd. | 339 | 586 | 22 | 13176 | 13434 | 16486 | -6.6 | 8 | 1 |
| Sheela Foam Ltd. | 376 | 650 | 24 | 15718 | 15891 | 15735 | 0.3 | 6 | 2 |
| Kansai Nerolac Paints Ltd. | 871 | 1,505 | 30 | 45223 | 45932 | 31826 | 13.0 | 7 | 1 |
| Voltas Ltd. | 742 | 1,281 | 27 | 33965 | 35884 | 40346 | -3.8 | 7 | 1 |
| Syngene International Ltd. | 695 | 1,200 | 26 | 31217 | 31677 | 24841 | 8.4 | 8 | 0 |
| PI Industries Ltd. | 1,044 | 1,804 | 24 | 43166 | 42762 | 46031 | -2.4 | 6 | 1 |
| Divi's Laboratories Ltd. | 3,078 | 5,318 | 22 | 118560 | 120864 | 124189 | -0.9 | 5 | 3 |
| Marico Ltd. | 1,636 | 2,827 | 32 | 91321 | 91705 | 66214 | 11.5 | 6 | 1 |
| Britannia Industries Ltd. | 2,229 | 3,852 | 35 | 133878 | 135495 | 86874 | 16.0 | 3 | 1 |
| Abbott India Ltd. | 972 | 1,680 | 26 | 44200 | 46023 | 41377 | 3.6 | 5 | 3 |
| Larsen & Toubro Infotech Ltd. | 2,829 | 4,888 | 15 | 71736 | 74387 | 128406 | -16.6 | 5 | 3 |
| Godrej Consumer Products Ltd. | 2,502 | 4,323 | 33 | 143962 | 142842 | 99032 | 13.0 | 7 | 1 |
| Aarti Industries Ltd. | 1,169 | 2,020 | 15 | 29359 | 27543 | 36475 | -8.9 | 7 | 0 |
| Mindtree Ltd. | 1,926 | 3,328 | 14 | 45255 | 46415 | 78777 | -16.2 | 5 | 3 |
| Alkyl Amines Chemicals Ltd. | 443 | 765 | 11 | 8262 | 8200 | 18117 | -23.2 | 5 | 4 |
| Century Plyboards (India) Ltd. | 470 | 811 | 17 | 13936 | 13782 | 13257 | 1.3 | 8 | 1 |
| TTK Prestige Ltd. | 418 | 722 | 30 | 21791 | 21978 | 13719 | 17.0 | 1 | 4 |
| Mphasis Ltd. | 1,920 | 3,318 | 11 | 36078 | 37391 | 63691 | -16.3 | 5 | 1 |
| V-Guard Industries Ltd. | 366 | 633 | 32 | 20321 | 20546 | 9553 | 29.1 | 1 | 4 |
| Zydus Wellness Ltd. | 366 | 632 | 33 | 20620 | 19250 | 12005 | 17.0 | 3 | 3 |
| Eicher Motors Ltd. | 2,139 | 3,697 | 29 | 105545 | 114034 | 70812 | 17.2 | 4 | 5 |
| Schaeffler India Ltd. | 913 | 1,578 | 20 | 31456 | 32294 | 27480 | 5.5 | 4 | 4 |
| Crompton Greaves Consumer Electricals Ltd. | 767 | 1,326 | 23 | 31100 | 31458 | 27445 | 4.7 | 5 | 2 |
| APL Apollo Tubes Ltd. | 915 | 1,582 | 11 | 16931 | 16192 | 25004 | -13.5 | 4 | 5 |

Source: Bloomberg, Monarch AIF, TTM is 12M ending Sep 2021, Current Mcap is 31 Dec 2021

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