Cohesion MK Best Ideas

Investment Report

October 2022

Cohesion®
Accessing Superior Growth

Cohesion MK Best Ideas had an excellent quarter. With total returns of 13.45% in USD and 23.69% in GBP, we delivered strong performance in absolute terms and also relative to both Indian and global equity markets. This is especially pleasing against a challenging backdrop.

2022 continues to be an interesting year for all of the wrong reasons. As flagged in our previous newsletters, the eyes of all investors are focused on the global fight against inflation. For the first time in several decades, the world's central banks are fighting a recession without their favoured weapon, accommodative monetary policy. The world has become accustomed to, and perhaps even complacent of, the central banks riding to the rescue whenever trouble has been brewing. This time does feel rather different. Most of the problems facing the world are on the supply side; surging prices of oil and basic foodstuffs brought about by the Russia-Ukraine conflict, bottle necks of countless everyday items exacerbated by China's continued Zero Covid policy and dislocations in the labour market. Worryingly, all of these are on the supply side of the economy and immune to actions of the central banks. The actions of the US Fed, ECB or Bank of England will have no impact whatsoever on how quickly these supply side issues resolve themselves. Raising interest rates will have as much effect on the supply side issues as antibiotics will have on treating a cold. Therefore, the central banks have to rely on dealing with the demand side of the economy. By withdrawing liquidity, they are hoping to reduce demand. Tighter credit markets will doubtless help with this too. As will the higher prices of everything from petrol to restaurant staff wages. Economics tells us that eventually the reduced demand will have the desired effect on prices, even if supply remains inelastic. Nevertheless, that is likely to be a painful period for those ill-prepared for it.

We have been saying for some time that India is in a strong position, and it appears that investors are beginning to wake up to that. Whilst we recognise that India, in common with pretty much every country, has its risks, we believe that the perception of the relative risk was quite simply wrong. We are witnessing significant political turmoil taking place in many G7 countries currently and simultaneous struggles to maintain any level of economic growth with their government balance sheets stretched and debt interest payments rising. Witness the extraordinary events happening in the UK Gilt market at the moment. Long dated Gilts have lost more than 50% since December 2021 and index-linkers are often up or down by more than 10% in a single day. When some of the supposedly safest assets on earth are exhibiting the sort of volatility that should be reserved for cryptocurrencies, it should make investors question what risk really means. Against this backdrop, India looks well placed and certainly not deserving of any risk-discount. Amongst emerging markets, India's case looks even stronger. Many of you will remember Jim O'Neill's paper on 'BRICs' which soon became an acronym used around the world. Some investors chose to invest in only one or two of these countries. We often meet investors with direct exposure to China or Russia but not India. You can certainly be very happy to have made the right choice over the last two years!

Growing capital. Preserving capital

We have been very pleased by the defensive nature of our portfolio this year. Set against the continuing destruction of value in many asset classes, we believe this is testament to both our investment process and also the sound fundamentals of the Indian economy and market. We have now delivered GAV returns of 57.80% in USD and 84.85% in GBP since we launched two years ago in August 2020. What is even more pleasing is the consistent way we have added value since launch. We have gone to great lengths to explain to investors the absolute return mindset that we have when managing money. Although we operate as a long-only equity strategy without any hedging, we very much think as absolute rather than relative investors. When selecting investments, we pay no attention to whether we are under or overweight to an index. We are solely focused on maximising the upside that we can capture from stocks that we have extensively 'due diligenced' while at the same time giving ourselves every possible downside protection. We call these stocks our '**corks under water**', for obvious reasons.

Consistency of process has led to consistency of returns

This iron-willed focus on making absolute returns and the wide spectrum of ideas that are contributing to performance at different times has led to our strategy delivering positive returns on a very consistent basis. As Table 1 below shows, in the two years since launch, Cohesion MK Best Ideas has made money in 69% of all months in USD, and 81% of all months in GBP. We believe that this compares favourably with not only the broad Indian market (as represented by MSCI India) but also against major global equity markets. We don't set out to manage money on a month-to-month basis. We know that we are buying exceptionally attractive stocks, but we can't be certain as to when that latent value will be unlocked. Sometimes we have to be patient while we wait for other investors to identify the same value that is evident to us. Sometimes that value can emerge much more quickly. For this reason, there is always something interesting happening in our portfolio. There are stocks that have probably run ahead of our expectations and hence are being trimmed whilst others are bubbling along nicely and still others that remain pregnant with value and presenting us with the chance to top up our holdings at levels which we believe to be highly attractive. This mixture of mature and emerging ideas in the portfolio is probably a key component of the consistent performance delivered so far.

Table 1: Monthly returns from Best Ideas v local and international indices in USD and GBP

USD

*Month	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	Number of positive months	Percentage of months that were positive
Cohesion MK Best Ideas	**-0.3**	**0.1**	**-0.6**	**7.4**	**8.3**	**1.5**	**9.0**	**0.6**	**3.6**	**9.6**	**-2.2**	**9.7**	**1.1**	**2.0**	**2.2**	**-6.3**	**6.0**	**1.4**	**-7.3**	**4.0**	**2.0**	**-8.2**	**-7.4**	**7.3**	**6.8**	**-1.0**	**18**	**69%**
MSCI India	3.5	0.6	1.2	8.7	10.2	-2.3	5.3	2.3	-0.9	8.7	-0.7	0.9	11.0	0.6	-0.8	-3.0	3.8	-1.4	-4.0	3.7	-1.7	-5.8	-6.7	9.4	4.2	-6.3	**15**	**58%**
MSCI World GTR	6.7	-3.4	-3.0	12.8	4.3	-1.0	2.6	3.4	4.7	1.5	1.5	1.8	2.5	-4.1	5.7	-2.2	4.3	-5.3	-2.5	2.8	-8.3	0.2	-8.6	8.0	-4.1	-9.3	**15**	**58%**
S&P 500 GTR	7.2	-3.8	-2.7	11.0	3.8	-1.0	2.8	4.4	5.3	0.7	2.3	2.4	3.0	-4.7	7.0	-0.7	4.5	-5.2	-3.0	3.7	-8.7	0.2	-8.3	9.2	-4.1	-9.2	**15**	**58%**
MSCI Emerging Markets	2.2	-1.6	2.1	9.3	7.4	3.1	0.8	-1.5	2.5	2.3	0.2	-6.7	2.7	-3.9	1.0	-4.1	1.9	-1.9	-3.0	-2.2	-5.6	0.5	-6.6	-0.2	0.5	-11.7	**14**	**54%**
Nasdaq 100	11.2	-5.7	-3.2	11.1	5.1	0.3	0.0	1.5	5.9	-1.2	6.4	2.8	4.3	-5.7	7.9	1.9	1.2	-8.5	-4.5	4.3	-13.3	-1.5	-8.9	12.6	-5.1	-10.6	**14**	**54%**
MSCI China	5.7	-2.7	5.3	2.8	2.8	7.4	-1.0	-6.3	1.4	0.8	0.1	-13.8	0.0	-5.0	3.2	-6.0	-3.2	-3.0	-3.9	-8.0	-4.1	1.2	6.6	-9.4	0.2	-14.5	**13**	**50%**
Nikkei 225	6.3	0.7	0.0	15.3	4.9	-0.6	2.9	-2.9	-0.2	0.1	-1.7	-4.2	2.9	3.2	-4.0	-3.3	2.0	-6.3	-1.7	-0.5	-10.6	3.5	-8.4	7.1	-2.6	-11.6	**12**	**46%**

***Month 1 August 2020. All figures in USD.**

GBP

*Month	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	Number of positive months	Percentage of months that were positive
Cohesion MK Best Ideas	**0.9**	**0.1**	**-0.6**	**4.0**	**5.7**	**0.6**	**7.2**	**2.4**	**2.8**	**7.0**	**0.5**	**9.1**	**2.2**	**4.1**	**0.7**	**-3.6**	**4.2**	**2.0**	**-7.1**	**6.3**	**6.5**	**-8.4**	**-4.1**	**7.4**	**11.8**	**3.0**	**21**	**81%**
MSCI India	1.5	4.2	1.2	5.2	7.6	-2.8	3.4	3.7	-1.3	5.9	2.2	0.3	12.1	2.7	-2.4	0.5	1.4	-0.4	-4.0	5.6	3.1	-6.1	-3.2	9.2	8.9	-2.3	**18**	**69%**
MSCI World	4.6	0.0	-3.1	9.3	1.8	-1.4	0.8	4.8	4.3	-1.1	4.5	1.2	3.6	-2.1	4.0	1.4	1.9	-4.4	-2.5	4.8	-3.8	-0.2	-5.2	7.8	0.3	-5.4	**16**	**62%**
Nikkei 225	4.2	4.3	0.0	11.7	2.9	-1.5	1.1	-1.6	-0.5	-2.5	1.2	-4.8	3.9	5.4	-5.6	0.2	0.0	-5.7	-1.7	1.4	-5.4	2.1	-4.9	6.9	1.9	-7.8	**15**	**58%**
S&P 500	5.1	-0.4	-2.7	7.5	1.4	-1.5	0.9	5.8	5.0	-1.7	5.0	1.7	4.1	-2.7	5.3	2.9	2.1	-4.3	-3.0	5.7	-4.3	-0.2	-4.8	9.0	0.3	-5.4	**15**	**58%**
MSCI China	3.6	0.8	5.3	-0.5	0.4	6.9	-2.8	-5.0	1.0	-1.8	3.0	-14.4	1.0	-3.1	1.5	-2.6	-5.4	-2.0	-3.9	-6.2	0.6	0.8	10.7	-9.6	4.8	-10.9	**13**	**50%**
Nasdaq 100	9.0	-2.3	-3.2	7.6	2.7	-0.1	-1.8	2.8	5.5	-3.5	9.2	2.2	5.3	-3.7	6.2	5.6	-1.2	-7.6	-4.6	6.3	-9.1	-1.9	-5.5	12.4	-0.8	-6.8	**12**	**46%**
MSCI Emerging Markets	0.2	1.9	2.1	5.8	4.9	2.6	-1.0	-0.2	2.1	-0.3	3.1	-7.3	3.7	-2.0	-0.7	-0.6	-0.4	-1.0	-3.0	-0.4	-1.0	0.1	-3.0	-0.4	5.1	-7.9	**11**	**42%**

***Month 1 August 2020. All figures in GBP.**

It is also worth highlighting that the environment we have been in recently hasn't been helpful to our style. As at the end of September we have more than half of the portfolio dedicated to smaller companies and this weight has been steadily increased throughout the year as we have found far greater value here than in the mid-cap space. Smaller companies have performed poorly in 2022, but our stock selection has allowed us to comfortably outperform as Table 2 shows. When the wind is at our backs and we are able to enjoy a stock picking environment, we believe that our outperformance will be even more pronounced as we are holding many smaller companies that are truly exceptional and profoundly cheap.

Table 2: Stock selection has led to us outpacing the Indian market across the capitalisation spectrum.

30.09.22	USD	GBP
CMKBI	**YTD**	
Cohesion MK Best Ideas in USD (GAV)	**-3.77**	**16.58**
Indices	**YTD**	
Index : MSCI India Small Cap GTR in US	-11.46	7.43
Nifty 50 in US	-9.84	9.64
Index : MSCI India GTR in US	-9.35	9.99

It is not only in smaller companies that we have found value. We have maintained a weighting of circa 30% of our portfolio in large-cap companies for most of this year. Not only do these provide deep pools of liquidity but, in a vibrant country such as India, there is scope for strong returns. We would highlight the excellent returns from our holdings in financial service companies such as ICICI, SBI and Canara Bank. These have all represented meaningful positions in our portfolio at various times over the last year. Some, such as Canara Bank, we traded out because their prices had run ahead of our expectations. ICICI and SBI have been solid, steady performers. Nevertheless, one had to be selective as there have been plenty of poor performers in the financials sector and it should never be treated as a homogenous sector that can simply be bought for its beta contribution.

IIFL - a cork under water in the financials sector

We continue to find plenty of new ideas in the financial services sector and would highlight **IIFL Finance** as a prime example. We initiated a position in this company some months ago whilst its share price was treading water. We believe that the market is unfairly ignoring the excellent operational performance of this business that is going from strength to strength; increasing its Assets Under Management (AUM), improving its Return On Equity (ROE) and maintaining impressive credit controls and low exposure to non-performing loans. Operating from a network of more than 3500 branches across India, IIFL is well placed to benefit from continued expansion in the gold-loan and affordable housing markets, both of which are enjoying secular growth trends. Crucially, much of this growth is off-balance sheet and this gives IIFL scope to continue to grow in a very capital-efficient manner. It has incurred cost in the roll out of its branch network, but this is now behind the business and therefore we are expecting cost to income ratios to fall as AUM continues to rise. It might be expected that such a robust growth story must come with a premium rating, but we believe that it is currently trading on around 6x 2024 earnings and that in our eyes is manifestly too cheap.

Pharmaceuticals - due diligence can uncover exceptional value in this misunderstood sector

Another area that we would highlight is the pharmaceutical sector and in particular the ‘API/CRAMS’ (Active Pharmaceutical Ingredients/ Contract Research and Manufacturing Services) space. We have discussed companies such as Divis Laboratories, Sun Pharma and Gland Pharma in previous communications as we believe this is an exceptionally rich hunting ground for investors. Invexa has a deep understanding of this market built over many years and access to a wealth of specialist academics and business leaders. There is little coverage of this sector by sell-side analysts and even many buy-side managers devote little attention to it. We think this is because of a misconception that API/CRAMS is a highly competitive and commoditised world. However, we see similarities to how the Chemicals sector was viewed ten years ago before it set off on a long bull market. The API/CRAMS sector has suffered from a number of macro headwinds, most especially supply issues during Covid and the effects of higher oil prices. During all of this, the best companies in the sector got busy implementing large scale capital expenditure programs to make themselves more efficient and better able to cope with the expected growth ahead. We fully expect such companies to be able to deliver CAGR earnings of 25%+ per annum and yet some are trading on PE multiples that are barely in double digits.

An excellent example of the opportunity in this area is **Granules**. Granules has been a terrific stock to own for many years. It has what Warren Buffet would describe as a 'deep moat filled with sharks' around its business. As the acknowledged best in class partner with a spotless regulatory compliance history and highly efficient processes, it is hard to imagine a new competitor successfully attempting to muscle in on its markets. The markets that it is involved in are large and persistent covering such areas as analgesics (paracetamol, ibuprofen), diabetes, as well as more complex generics. This dominance has allowed it to grow its profits at almost 40% CAGR from 2011-21. A deeply impressive track record. What's more, that growth has actually accelerated from 2018-21. However, the supply side issues discussed earlier have dented Granules' growth over the last 12 months and given us the chance to buy their shares at a price that is rarely seen. Indeed, their shares have already started to recover considerably over the last few weeks giving us an earlier than expected profit. Some of the areas of concern are starting to lift. The key ingredient in paracetamol was subject to a massive supply shortage caused by a factory closure in China but that issue has now been resolved and Granules have taken this as an opportunity to open new supplies elsewhere and so turn a problem into a longer-term benefit. The business is also on the cusp of being elevated to mid-cap status with the commensurate increase in analyst coverage. We believe that the stars are aligning for Granules and are happy to own it in a meaningful way.

We have been preaching the benefits of India for many years, telling investors that India offers superior growth with similar or lower risk than found in NASDAQ or China. Despite the outperformance we have enjoyed so far, we believe that the investment case for allocating to India remains compelling as it has many drivers that can only be described as unique in a world which will struggle for growth over the next 1-2 years. We have a portfolio of well managed growth companies that we expect to deliver 20-25% earnings growth compounded over the next 3-5 years and yet our expected PE ratio is likely to be below that of the market. We are also holding around 9% of the portfolio in cash today as we feel sure that the current volatility will allow us to top up some of our favourite holdings and perhaps initiate new positions. We continue to look forward confidently.

Strategy Performance: Data as at 30th September (Q3) 2022

Discrete Performance** (%)							
		Q1	Q2	Q3	Q4	YTD	Since Launch: Aug 2020*
USD	2022	-2.22	-13.25	13.45	-	-3.77	57.80
	2021	11.31	11.01	13.13	1.58	42.00	63.98
	2020	-	-	-0.19	15.70	15.48*	15.48
		Q1	Q2	Q3	Q4	YTD	Since Launch: Aug 2020*
GBP	2022	0.71	-6.41	23.69	-	16.58	84.85
	2021	10.40	10.63	16.12	1.15	43.45	58.56
	2020	-	-	1.08	9.35	10.54*	10.54

*August 1st 2020
**net of taxes and fees, gross of performance fees

*Cash Deployed Cautiously During COVID-19 Outbreak		
	Equity	Cash
1st 6 months	45%	55%
1st 12 months	68%	32%
Since Inception	81%	19%

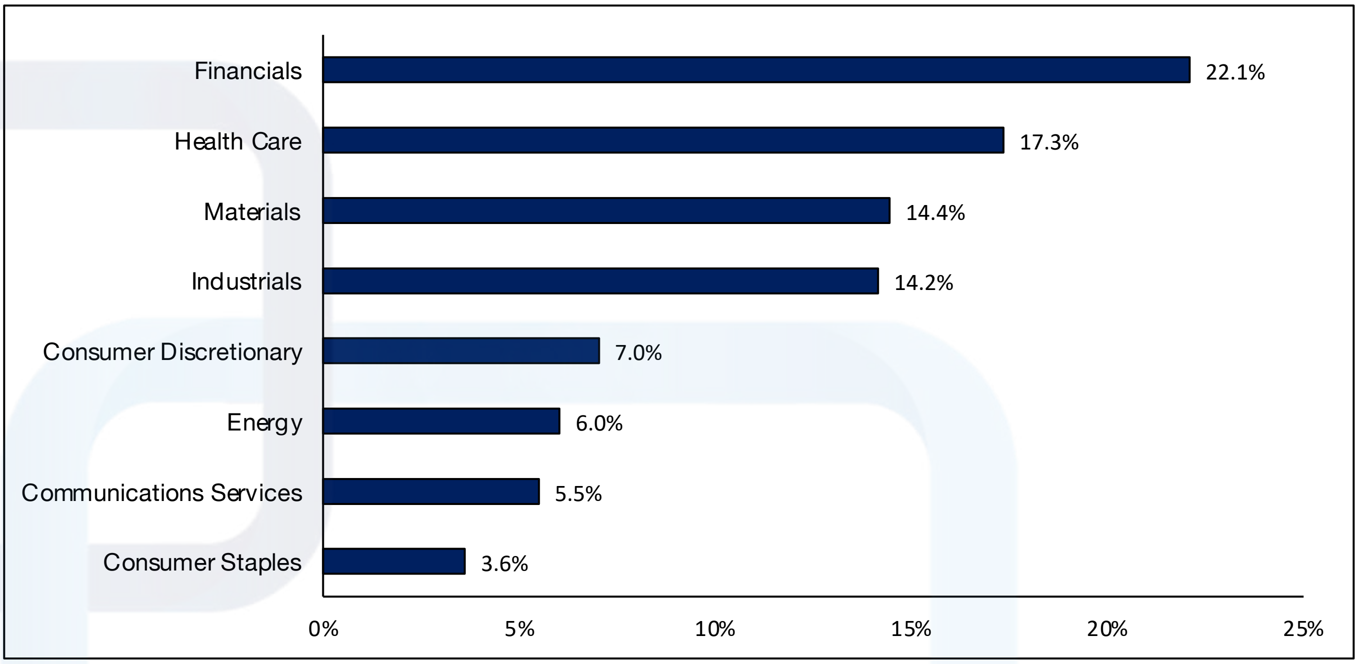
Portfolio – 30th September 2022

Top 5 Holdings

Security Name	% Holding of Portfolio
IIFL Finance	5.79%
Bharti Airtel	5.50%
Granules India	5.25%
Ambuja Cements	4.70%
Larsen & Toubro	4.63%

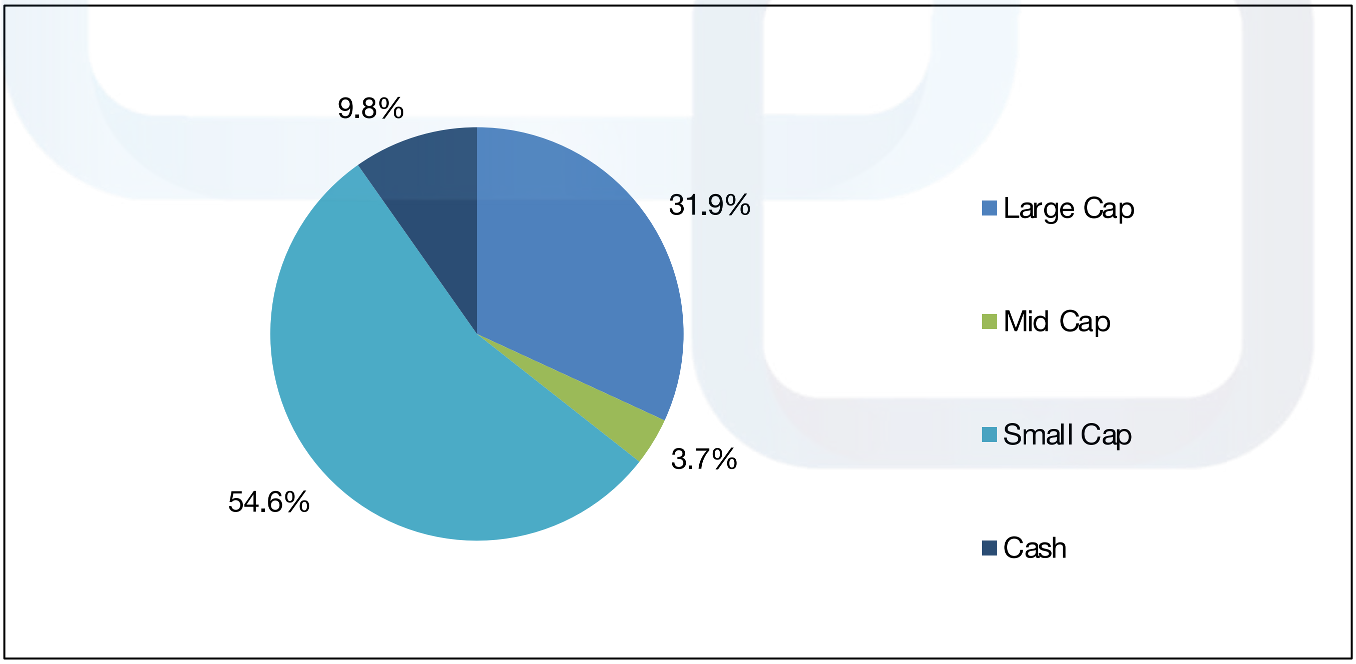
Portfolio – 30th September 2022

Sector Exposure



Portfolio allocations may not add to 100% due to rounding and cash holding

Market Cap Exposure



SEBI market cap breakdown – **Large Cap**: top 100 largest companies ranked by market cap,
Mid Cap: 101-250 companies ranked by market cap, **Small Cap**: companies ranked 251 and onwards

For further information:

Website: www.cohesioninvestments.com

Email: investor@cohesioninvestments.com

Mobile/WhatsApp: +971 555 102 622

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