
DSP Focus Fund

An open ended equity scheme investing in maximum 30 stocks. The Scheme shall focus on multi cap stocks.

DSP Flexi cap Fund

Flexi Cap Fund - An open ended dynamic equity scheme investing across large cap, mid cap, small cap stocks

BHAVIN GANDHI'S INVESTMENT FRAMEWORK

Fund Overview – Key Differentiation

	DSP Focus Fund	DSP Flexi cap Fund
Category	Focused Fund	Flexi cap
Strategy	Flexi cap	Flexi cap
Benchmark	Nifty 500 TRI	Nifty 500 TRI
Style	Concentration	Diversified
No of stocks	Max 30 stocks	40-60
Large-Cap	No constraint	No constraint
Mid-Cap	No constraint	No constraint
Small-Cap	No constraint	No constraint

Key Differentiation

No restriction on market caps

Fund Manager have same stock selection framework for DSP Focus Fund & DSP Flexi cap Fund & can lead to significant overlap of stocks

The investment approach / framework/ strategy mentioned herein are currently followed by the scheme and the same may change in future depending on market conditions and other factors. Large caps are defined as top 100 stocks on market capitalization, mid caps as 101 - 250 small caps as 251 and above

FUNDAMENTAL BELIEF

Core Framework to assess “Value” for any stock

Fundamental Ratio used by fund manager to assess VALUE

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$$\text{Intrinsic Value} = \frac{\text{Cashflows} \times (1 - \text{Growth} / \text{Return on Invested Capital (ROIC)})}{\text{Cost of Capital (WACC)} - \text{Growth}}$$

Metric	Where does it appear in value equation		Relationship with Value
	Numerator	Denominator	
ROIC	✓	✗	Higher ROIC = Higher Value
Growth	✓	✓	Ambiguous*
WACC	✗	✓	Higher WACC = Lower Value

✓ Growth* creates value only when ROIC > WACC

The value of any business is driven by four key elements:

- 1) The company's ability to generate cash flows
- 2) Its capacity to grow these cash flows
- 3) The return on capital employed
- 4) The opportunity cost of capital

Expectation Investing >> Value or Growth investing

- ✓ Fund manager doesn't believe in value or growth style of investing
- ✓ Value of the company = Markets expectations of the companies future performance
- ✓ Markets expectation may be different from companies expectations

Performance vs Expectation	Outcome
Actual Performance < Expectations	Shareholder Returns < Cost of Capital
Actual Performance = Expectations	Shareholder Returns = Cost of Capital
Actual Performance > Expectations	Shareholder Returns > Cost of Capital

Critical to understand implied expectations

- A Great company may not be a great ~~A Great investment~~
- Fund Manager's goal is to identify mispriced opportunities—investing in businesses where the market hasn't fully appreciated their potential, leaving room for the company to exceed those expectations

Earnings Growth >> Return on Invested Capital Growth

- Return on Invested Capital (ROIC) has diminishing marginal utility.
- Company can get rerated faster with higher earning growth vs Higher ROIC

Theoretical Implied Price to Earning Ratio

Lets take an example of Company with 20% ROIC & 10% Earnings growth with implied PE ratio of 16.

- Company can get rerated to 28 PE ratio with just 10% change in expected earning growth.
- Company will need to increase ROIC from 20% to 100% to get rerated to 25 PE level

		Return on Invested Capital (ROIC)									
		12%	20%	30%	40%	50%	60%	70%	80%	90%	100%
Earning Growth	10%	8	16	20	22	23	23	24	24	25	25
	15%	8	21	27	30	32	33	34	35	35	36
	20%	8	28	38	43	46	48	49	50	51	52
	25%	8	37	52	60	65	68	70	72	73	74
	30%	8	49	73	85	92	96	100	102	104	106
	35%	8	66	101	118	129	136	141	144	147	150

Higher expected earning's growth is more important than higher ROIC for company to be rerated

Trees grow but not to the sky

PAT > Rs crores	Total No of cos	PAT doubling in the next five years (Rs crores)	No of cos making the transition	Success Rate	Cumulative Success Rate
0	95	0 to 25	53	56%	38%
25	46	25 to 50	22	48%	30%
50	137	50 to 100	53	39%	28%
100	148	100 to 200	57	39%	21%
200	125	200 to 400	38	30%	13%
400	78	400 to 800	24	31%	8%
800	49	800 to 1600	17	35%	5%
1600	33	1600 to 3200	11	33%	2%
3200	17	3200 to 6400	3	18%	1%
6400	16	6400 to 12800	3	19%	1%
12800	5	12800 to 25600	1	20%	0%
25600	2	25600 to 51200	0	0%	0%

Cumulative success drops sharply >1000 crore PAT

Preference is for smaller companies that can compound their earnings

INVESTMENT PROCESS

Factors driving Value Creation

A solid business ability to create value rest on four key pillars



1. Earnings Growth

- **Growth is the key differentiator between Equity and Bond**
 - If growth goes away = Equity becomes a bond with earnings yield = coupon
 - If growth goes away permanently: Equity < Bond

- **Quality of Growth matters:**

Preferred	Not Preferred
✓ Organic Growth	✗ Inorganic Growth*
✓ Non-Dilutive Growth	✗ Dilutive Growth
✓ Focus	✗ Unrelated

Inorganic Growth – Important Points considered

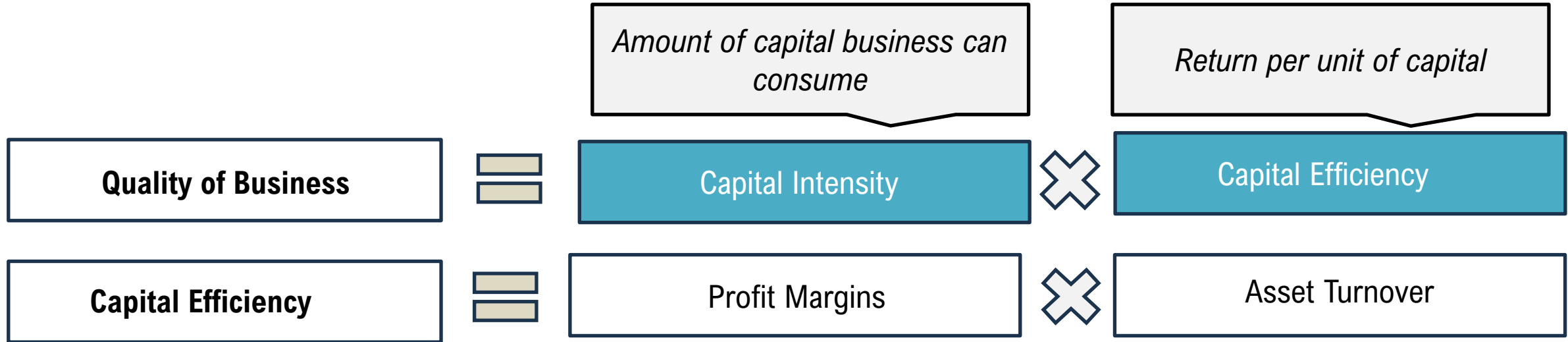


Bhavin Gandhi @bhavinjan1978 · Nov 27, 2022

When put through the five point test, most acquisitions fall short...

- ★ sole bidder (v/s Bidding War)
- ★ PVT target (v/s Public target)
- ★ All cash (v/s All stock)
- ★ small target (v/s Large target)
- ★ Cost synergies (v/s growth synergies)

2. Quality of Business

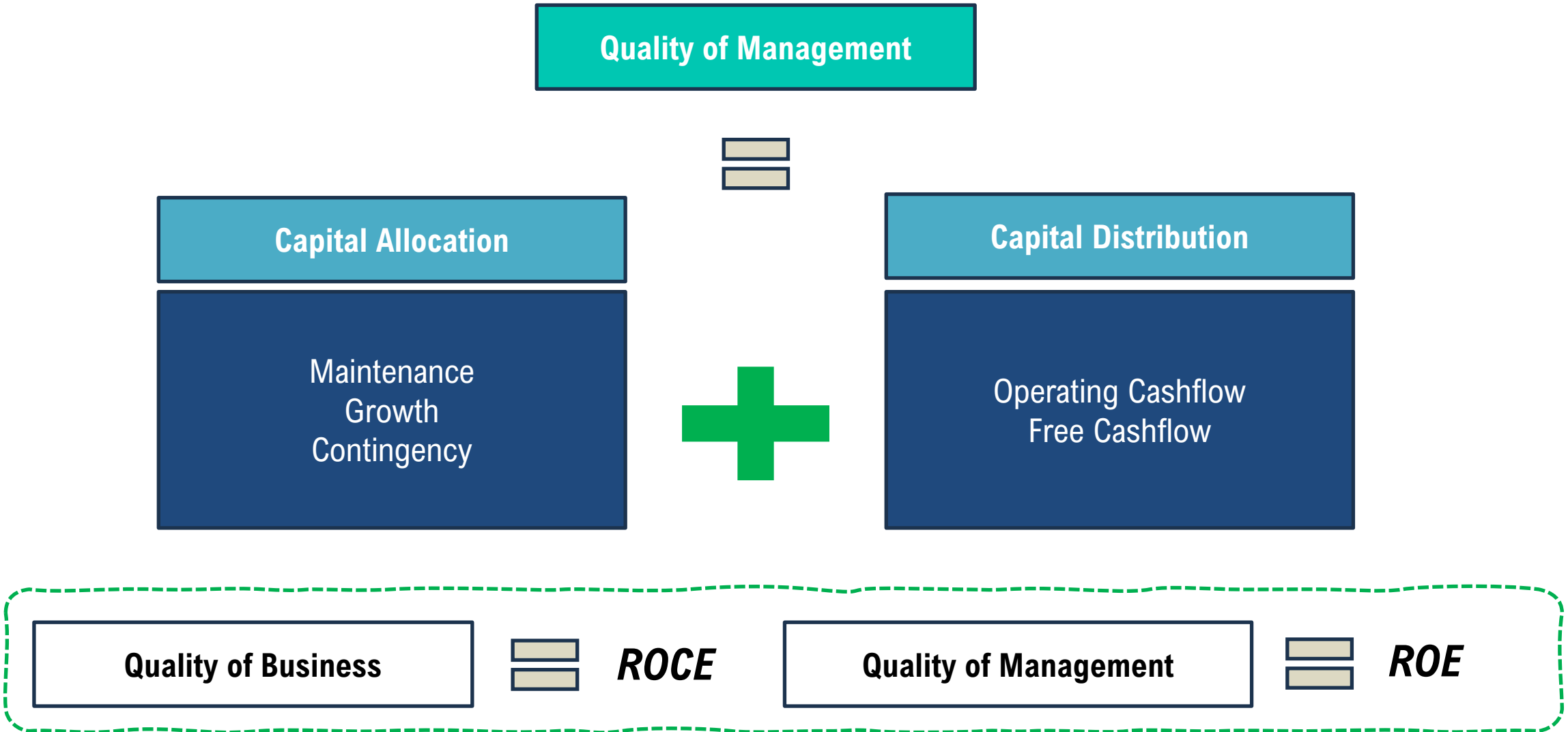


Business	ROCE	Profit Margin (%)	Asset Turnover (x)
1	50%	25	2
2	50%	10	5
3	50%	5	10

Business 3 is more preferable



3. Quality of Management



Capital Allocation: Can only be judged in hindsight

- Capital Allocation decision can be a key differentiator in overall returns.
- A company that experiences a decrease in overall Return on Equity (ROE) and Return on Invested Capital (ROIC) due to incremental capital allocation may not be preferred
- Example – Based on data of 3 Steel-Tube/Pipes sector companies, Peer-1 has been the most prudent in allocating incremental capital

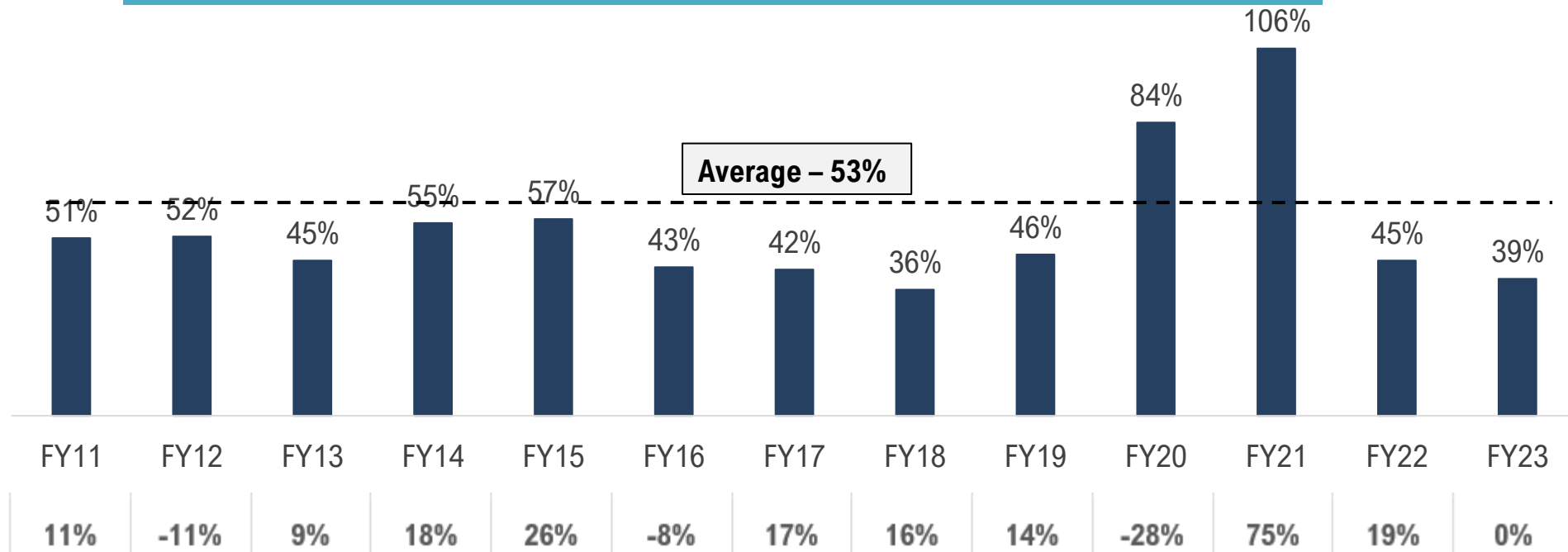
Peer-1				Peer-2				Peer-3			
CAGR	5 Yr	7 Yr	10 Yr	CAGR	5 Yr	7 Yr	10 Yr	CAGR	5 Yr	7 Yr	10 Yr
Revenue	13%	20%	14%	Revenue	8%	12%	6%	Revenue	16%	12%	10%
EBITDA	18%	20%	14%	EBITDA	20%	16%	8%	EBITDA	10%	12%	11%
PAT	21%	24%	16%	PAT	37%	34%	22%	PAT	37%	95%	10%
Avg ROIC	17%	16%	16%	Avg ROIC	13%	11%	8%	Avg ROIC	10%	9%	8%
Avg ROE	22%	21%	22%	Avg ROE	15%	14%	12%	Avg ROE	7%	6%	-1%

The investment approach / framework/ strategy mentioned herein are currently followed by the scheme and the same may change in future depending on market conditions and other factors. ROIC – Return on Invested Capital, ROE- Return on Equity. The sector(s)/stock(s)/issuer(s) mentioned in this document do not constitute any recommendation of the same and the Fund may or may not have any future position in these sector(s)/stock(s)/issuer(s). Above table is for illustration purpose only

Dynamically “Buy & Hold” Approach

- Long term 52W H/L gap for Nifty-50 is ~55%
- Each of these stocks have >30 analyst covering them
- Intrinsic value rarely fluctuate so widely, with other things remaining the same we prefer buy and hold

Median 52 Week High/Low for Nifty-50 stocks



VALUATION

Measuring Implied Expectations >> Other Valuation Approaches

Intrinsic Value: Discounted Cashflow

Estimating the future cashflows of business and discounting those cashflow back to their present value using an appropriate discounting rate

Pricing: Relative Valuation

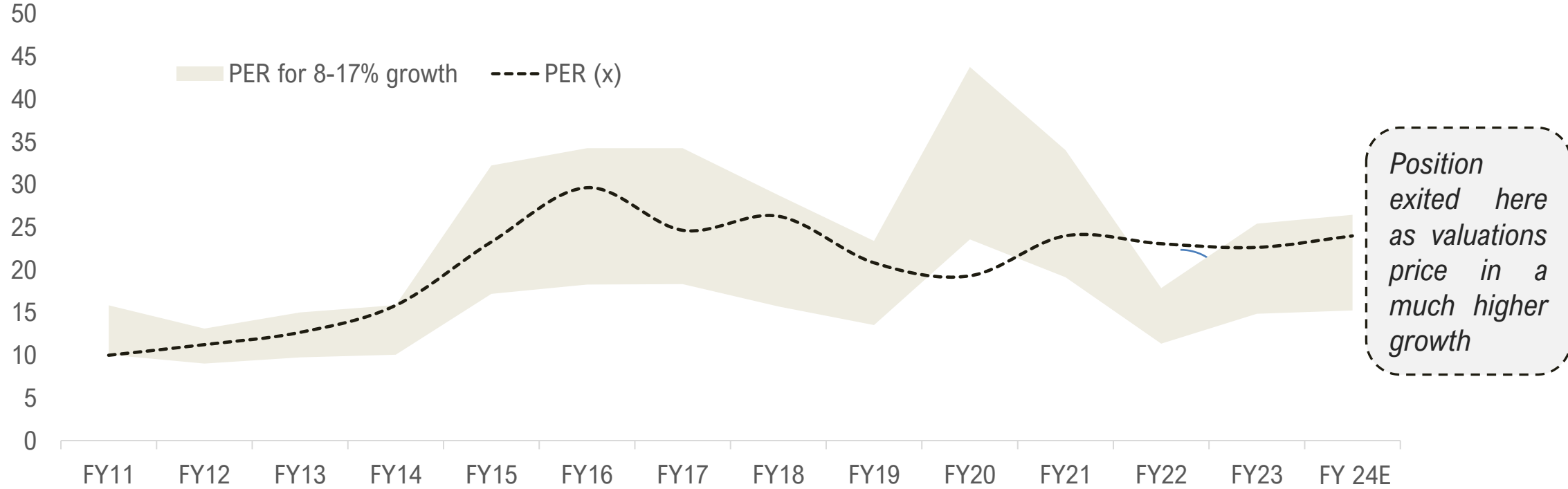
Valuation based on what the comparable peers are trading at by using valuation ratios such as Price to earnings, Price to book and Enterprise value to EBITDA

Measuring implied expectations

Judging the implied expectation in the stock by calculating the implied growth which is baked into the current stock price

Our preferred approach

Context Matters - Sometimes low valuations may not mean a bargain



Market Implied

ROE	21%	18%	20%	21%	34%	33%	33%	30%	26%	20%	18%	19%	20%	21%
COE	13%	13%	13%	13%	12%	11%	11%	12%	11%	9%	10%	12%	11%	11%

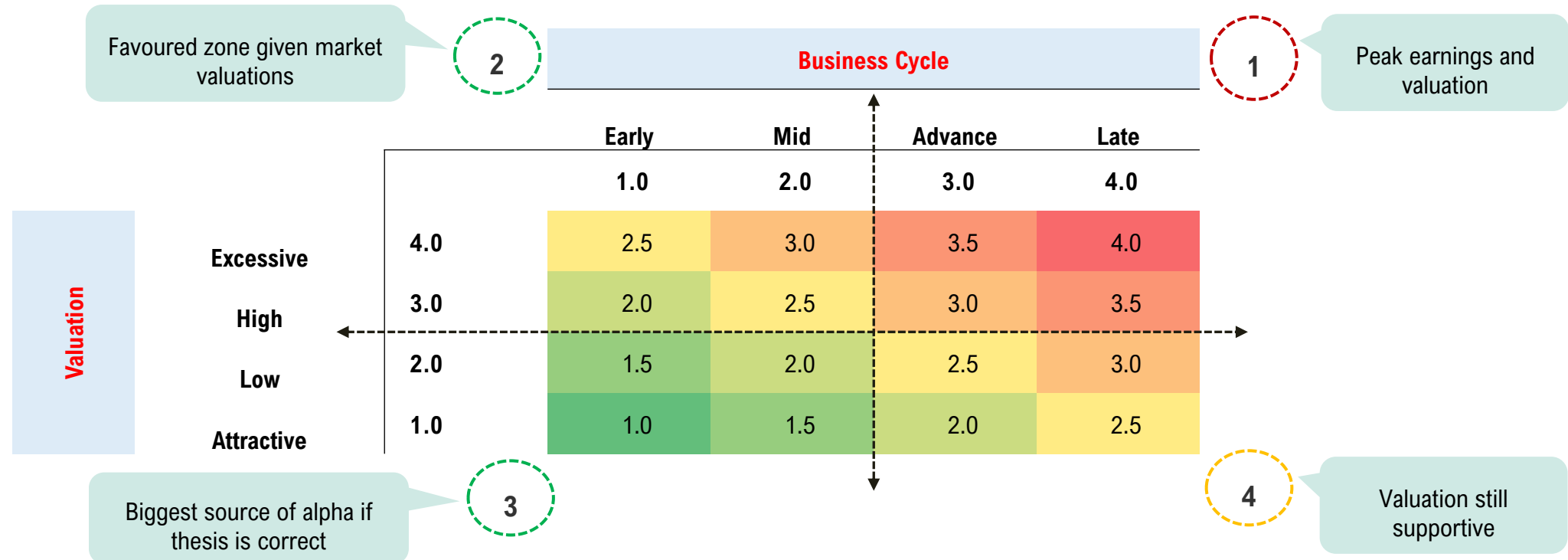
Reported

ROE Average 3yr	6%	18%	15%	19%	21%	31%	34%	32%	28%	24%	18%	15%	15%	18%
Earnings CAGR 3yr	LTP	LTP	-20%	81%	26%	60%	61%	47%	18%	3%	-12%	-9%	17%	39%

The stock should have traded at >70x on these metrics but it did not – because market knew a large part of the growth were from a particular new launch

Favorable Business Cycle + Favorable Valuations

- The characteristics of the investee companies chosen would mean valuation are unlikely to be in low bucket unless overall market valuations are undemanding
- We actively seek exposure to companies in early or mid cycle available at low to reasonable valuations

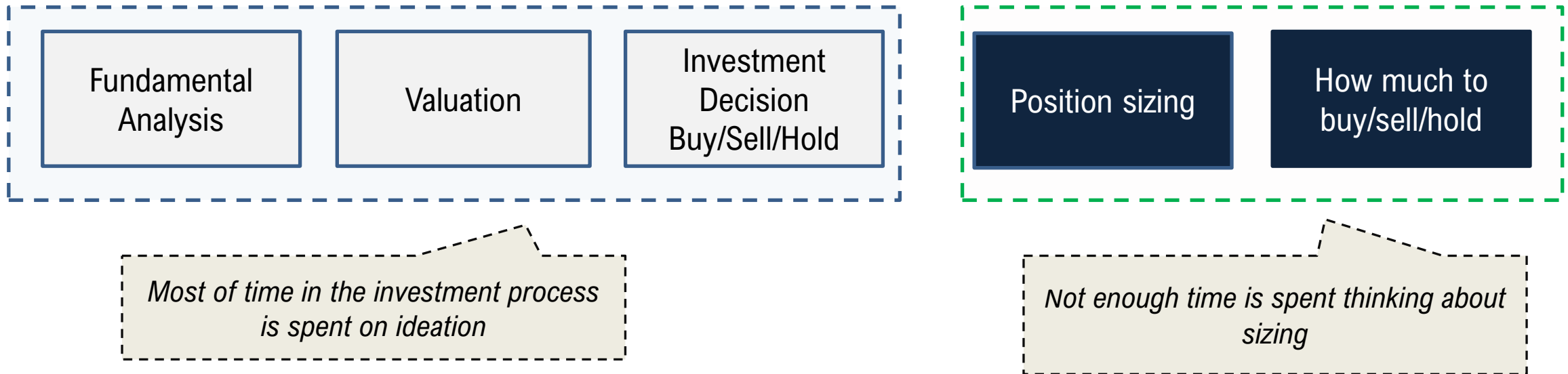


Position Sizing

Position Sizing - Integral to our investment process

- Portfolio objective: Generating adequate return while minimising the permanent capital loss
- A 10% position generating a 25% return is more valuable than a 1% position that doubles
- We focus on Position Sizing as much as we focus on Stock Selection

Investment Process



Position Sizing – Kelly Position Framework in Action

Position Size = Edge/Odds

	CMP >>	25	15	10	9	17	19	26
Probability	FV	Possible Upside (FV / CMP)						
33% (Worst Case)	10	-60%	-33%	0%	11%	-41%	-47%	-62%
33% (Base Case)	20	-20%	33%	100%	122%	18%	5%	-23%
33% (Bull Case)	30	20%	100%	200%	233%	76%	58%	15%
Expected Value (Edge)		-20%	33%	100%	122%	18%	5%	-23%
Possibility of Positive Outcome (Odds)		20%	67%	100%	122%	47%	32%	15%
Allocation Edge / Odds		0%	50%	100%	100%	38%	17%	0%

*When there is upside only in bull case
no allocation*

*When there is upside in base case
partial allocation*

*When there is no downside full
allocation*

The framework recognizes - “Don’t try to buy at the bottom and sell at the top”

Position Sizing – Increases margin of safety when variability is high

Scenarios	Probability	Scenario 1 @ High Risk			Scenario 2 @ Medium Risk			Scenario 3 @ Low Risk		
		50% Stdev	CMP	Allocation	25% Stdev	CMP	Allocation	15% Stdev	CMP	Allocation
Bear	33%	10	18	-0.44	15	18	-0.17	17	18	-0.06
Base	33%	20	18	0.11	20	18	0.11	20	18	0.11
Bull	33%	30	18	0.67	25	18	0.39	23	18	0.28
		Edge		11.0%	Edge		11.0%	Edge		11.0%
		Odds		38.9%	Odds		25.0%	Odds		19.4%
		Allocation		28.3%	Allocation		44.0%	Allocation		56.6%

Holding company Analysis, Public Sector Enterprise

Ideas matter, Labels not-so-much

Rather than using a labels-based approach we find it more useful to categorize or bucket ideas and pick the best ideas in each

- **Compounders** : Secular growth businesses

- **Fast Growers** : Recent growth acceleration

- **Slow Growers** : Fundamental good business growing less than GDP

- **Cyclicals** : High variability in earnings through cycles

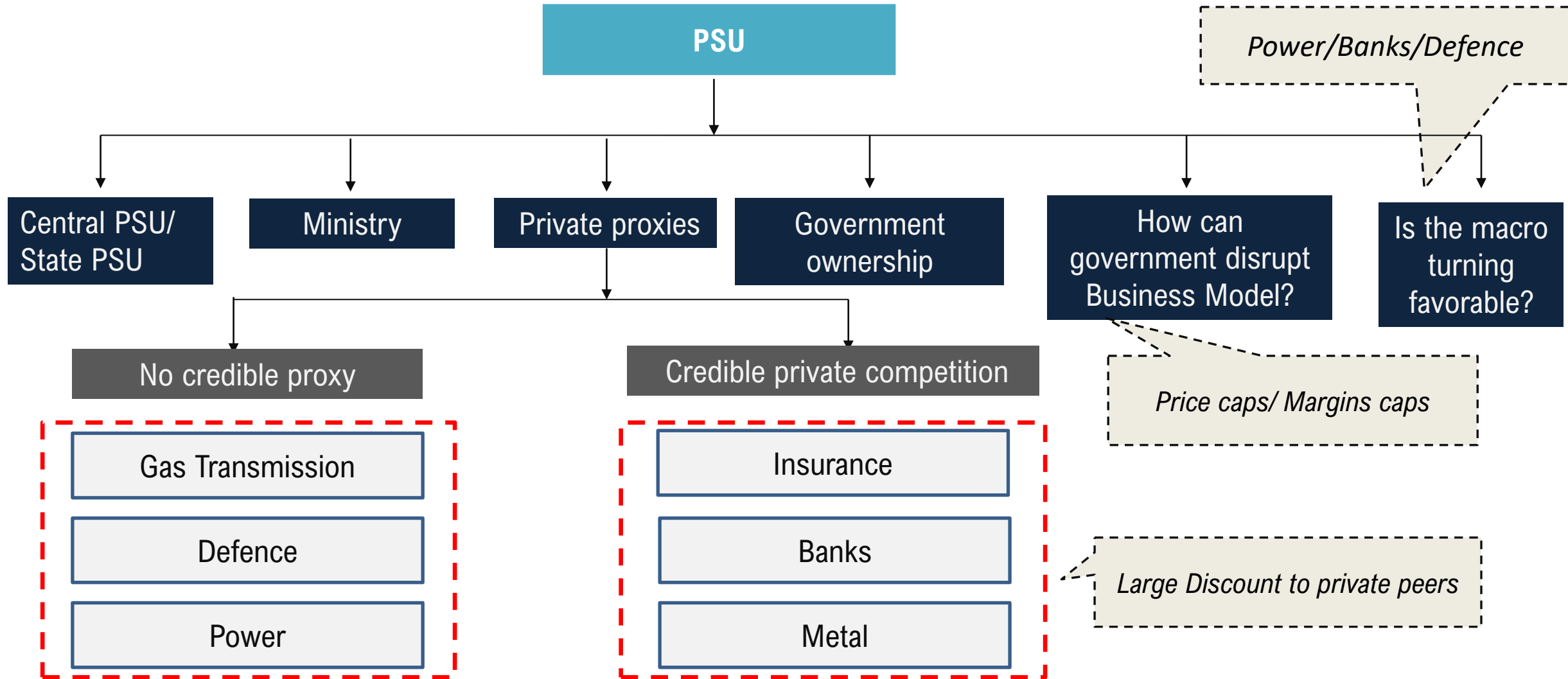
- **Commodities** : No product differentiation, price takers

- **Turnarounds** : Good businesses suffering due to Litigations, management, capital allocation

- **Hold Cos** : All kinds of holding companies

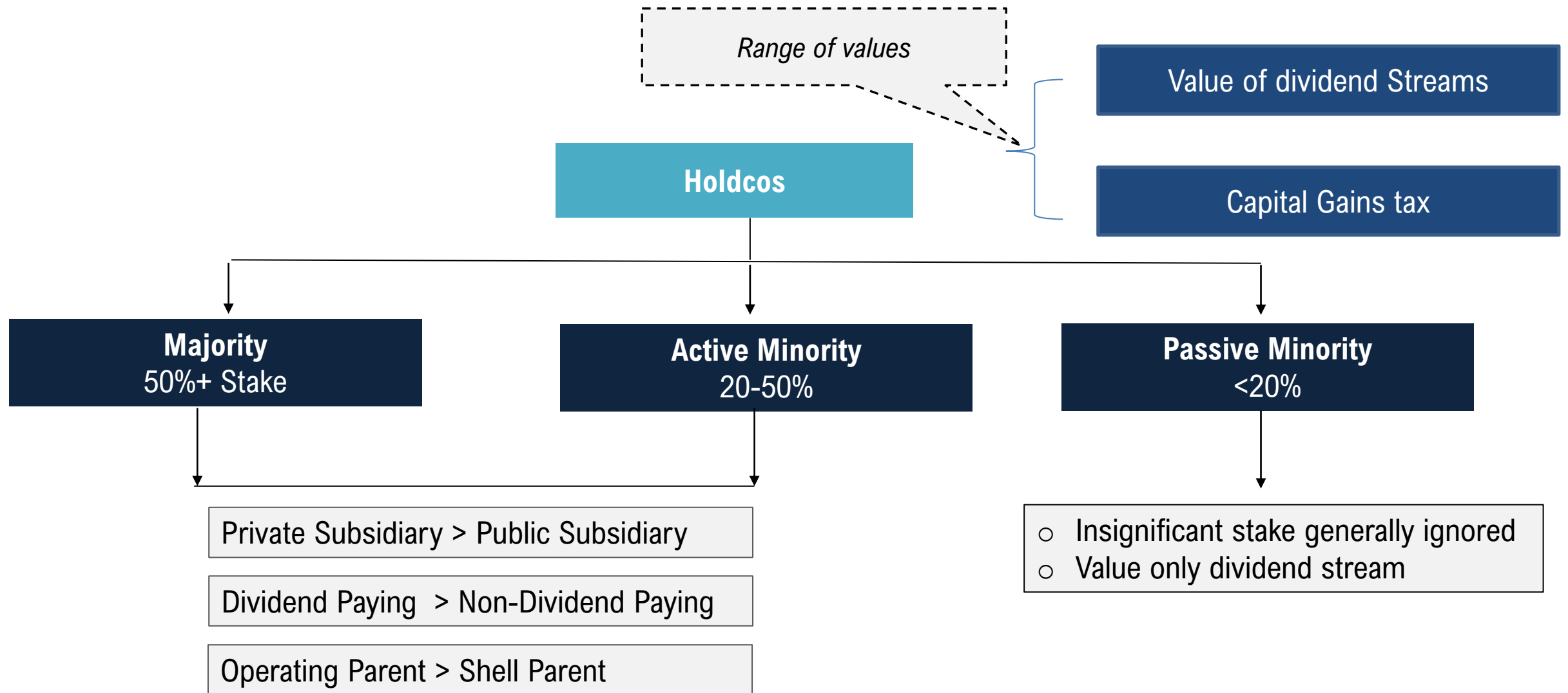
- **PSUs** : PSU need to be evaluated differently from privately owned companies

Public Sector Undertaking : Evaluation Framework



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Holdings Company (Holdco): Evaluation Framework



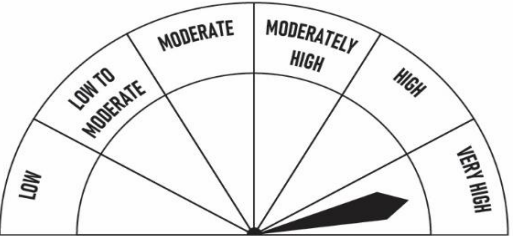
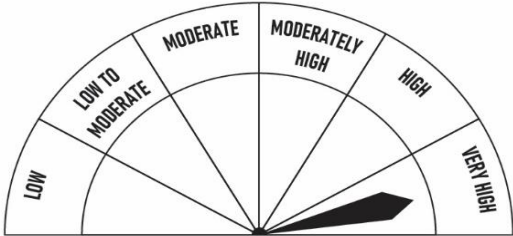
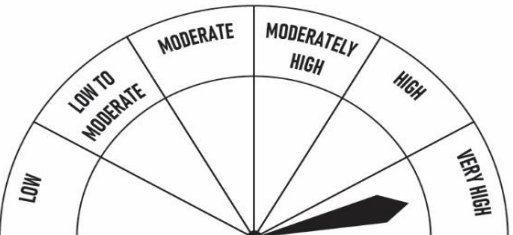
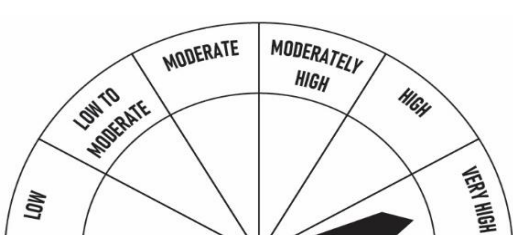
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Large-caps are defined as top 100 stocks on market capitalization, mid-caps as 101-250 , small-caps as 251 and above. The strategy mentioned has been currently followed by the Scheme and the same may change in future depending on market conditions and other factors

Mutual Fund investments are subject to market risks, read all scheme related documents carefully.

Product Labelling

<p>DSP Focus Fund</p> <p>(An open ended equity scheme investing in maximum 30 stocks. The Scheme shall focus on multi cap stocks.)</p>	<p>This Open Ended Equity Scheme is suitable for investors who are seeking*</p> <ul style="list-style-type: none"> • Long-term capital growth with exposure limited to a maximum of 30 stocks from a multi cap investment universe • Investment in equity and equity-related securities to form a concentrated portfolio <p>*Investors should consult their financial advisors if in doubt about whether the scheme is suitable for them.</p>	<p>SCHEME RISKOMETER</p>  <p>RISKOMETER</p> <p>INVESTORS UNDERSTAND THAT THEIR PRINCIPAL WILL BE AT VERY HIGH RISK</p>	<p>BENCHMARK [Nifty 500 TRI] RISKOMETER</p>  <p>RISKOMETER</p> <p>INVESTORS UNDERSTAND THAT THEIR PRINCIPAL WILL BE AT VERY HIGH RISK</p>
<p>DSP Flexi Cap Fund</p> <p>(Flexi Cap Fund - An open ended dynamic equity scheme investing across large cap, mid cap, small cap stocks)</p>	<p>This Open Ended Scheme is suitable for investors who are seeking*</p> <ul style="list-style-type: none"> • Long-term capital growth • Investment in equity and equity-related securities to form a diversified portfolio <p>*Investors should consult their financial advisors if in doubt about whether the scheme is suitable for them.</p>	<p>SCHEME RISKOMETER</p>  <p>RISKOMETER</p> <p>INVESTORS UNDERSTAND THAT THEIR PRINCIPAL WILL BE AT VERY HIGH RISK</p>	<p>BENCHMARK [Nifty 500 TRI] RISKOMETER</p>  <p>RISKOMETER</p> <p>INVESTORS UNDERSTAND THAT THEIR PRINCIPAL WILL BE AT VERY HIGH RISK</p>

DSP

MUTUAL FUND

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