

# BEYOND THE EFFICIENT FRONTIER



**2025: THE YEAR THAT WAS**

REFLECTIONS FROM THE EQUITY TEAM AT

**DSP**  
ASSET MANAGERS

In the summer of 1968, the world of track and field was governed by a "Frontier" that everyone thought was fixed.

For decades, if you wanted to jump high, there were only two "efficient" ways to do it: the Scissors jump or the Straddle. You looked at the bar, you stayed upright, and you cleared it face-first. Coaches, Scientists, and Olympic legends all agreed: these were the only two models that worked. The math of human biomechanics said so.

Then came a young man at the Mexico City Olympics. Instead of following the efficient rules of the time, he did something that looked like a mistake. He ran in a curve, turned his back to the bar, and leaped into the air backward. The crowd gasped. The commentators laughed. They called it the "Fosbury Flop."

But as he arched his back and cleared 2.24 meters to take the Gold Medal, the laughter stopped. The Fosbury Flop became a revolutionary high jump technique. He hadn't just won a race; he had proven that the "Efficient Frontier" of high jumping was not cast in stone. The old models had hit a ceiling. To go higher, he had to alter the traditional playbook and move into a space no one had dared to explore.

Today, in the world of capital markets and economics, we are facing our own "Fosbury Moment."

## BROKEN ECONOMIC RELATIONSHIP

When a 100-year playbook stops working

For almost a century, investors operated with a fairly reliable macro rulebook. Print too much money and inflation rises while the currency weakens. Hike interest rates aggressively and a recession follows, taking equity markets down with it. Run large fiscal deficits and bond markets panic. Start a war and oil prices spike as investors rush to safe havens.

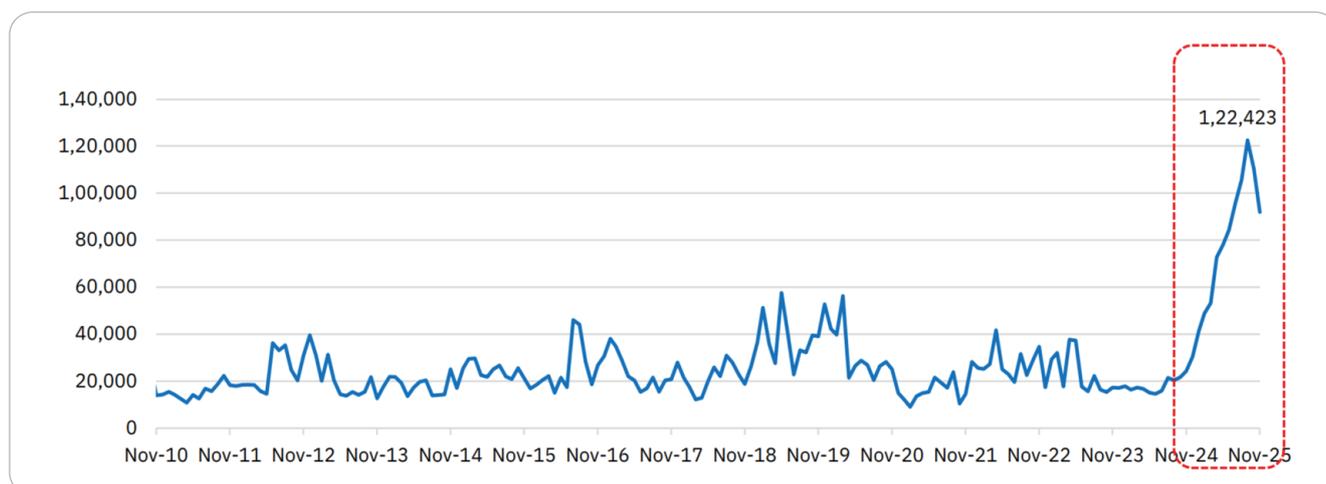
The system was never perfect, but it was predictable, like a compass. It didn't tell you exactly where you would land, but it gave a sense of direction. Post-COVID, that compass has stopped working.



Trillions of dollars in money creation did not weaken the US dollar for long stretches. The fastest post-COVID rate-tightening cycle neither triggered a recession nor caused a lasting collapse in equity markets. Major geopolitical shocks did not send oil prices soaring. Fiscal deficits that once invited “bond vigilantes” have often been met with surprising calm. In what is perhaps a rare moment in history, multiple asset classes—equities, bonds, and even precious metals—have risen together, defying traditional logic.

The World Uncertainty Index (WUI) developed by the World Bank to track economic, political, and social uncertainty across countries is currently near its highest recorded levels (refer chart below). We hardly needed the index to confirm it; the sense of uncertainty is visible everywhere. Our hope, however, is that this marks a peak and it gradually gives way to a more stable and predictable environment going forward.

### World Uncertainty Index



Closer to home, India reflects its own set of paradoxes. Record levels of foreign investor selling events that once destabilised markets are now being absorbed smoothly by domestic investors, many of whom have never experienced a true bear market. A large and sustained IPO wave, historically seen as a late-cycle excess, is being digested without visible stress.

Markets today are driven less by traditional economic logic and more by liquidity, AI (Artificial Intelligence) and geopolitics resulting in a shift away from traditional valuation discipline. Consider the Nifty 500 index, its overall PE (Price/Earnings multiple) has not changed materially over the past decade but its composition in terms of valuation has shifted significantly, refer to the chart below.

- Ten years ago, stocks with more than 50x trailing PE made up less than 5% of the index. Today, that figure has risen to approximately 23%.
- Conversely, stocks with less than 15x trailing PE used to be 30% of the index, which has now reduced to 13%.

### Nifty 500 weights in PE buckets

PE Buckets	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Below 15	30%	24%	20%	17%	33%	15%	15%	15%	15%	13%
Between 15-30	46%	47%	49%	49%	43%	48%	34%	53%	40%	43%
Between 30-50	19%	21%	18%	20%	9%	18%	27%	14%	20%	20%
Above 50	4%	6%	12%	12%	14%	19%	24%	18%	23%	23%
Nifty 500 Index PE	23	27	30	31	22	36	24	21	25	24

The post-COVID world is meaningfully different, marked by multiple dislocations that call for greater rationality, patience, and an acceptance that macro signals are far less reliable guides than they once were. In this environment, the objective is no longer to predict cycles, but to invest wisely as those cycles evolve faster than before, while staying firmly anchored to the core principles of fundamental investing. The journey may be volatile, but the destination remains promising—especially for a young economy scaling new highs.

What follows is our reflection on the themes that surprised us, challenged our assumptions, and forced us to distinguish between enduring structural shifts and trends that may simply fade away.

## FROM MOATS TO DISRUPTION

### Wallet share shifts rewriting India's consumption playbook

India's economy is driven by consumption. Out of India's Rs. 331 trillion GDP (USD 3.7 trillion) in FY24-25, Rs 203 trillion (USD 2.4 trillion) came from private consumption - about 62% of GDP. So, despite all the headlines about a slowdown, consumption hasn't collapsed.

(Source: DSP Research)

**The real story is not weak consumption - it's shifting consumption.**

Indian consumption is undergoing a rapid transformation. The most striking insight from the Household Consumption Expenditure Survey 2025 (HCES) is not how much Indians spend, but where that spending is shifting. Food now takes up a steadily smaller share of household budgets, while spending on discretionary goods has surged, marking a clear structural change in consumption patterns. Within consumer discretionary, the mix itself is changing. Products such as vehicles and air conditioners are no longer aspirational purchases reserved for a few but are becoming commonplace in both rural and urban households. The traditional line between “luxury” and “necessity” is fading. This broad-based move toward premium products reflects the powerful combination of rising aspirations, easier access to credit, stronger & more efficient supply chains, and deepening financial inclusion.

The chart below captures recent changes in consumption preferences of Indian households, as seen in the volume growth in select consumer categories:

**Changes in consumption preferences**

Category Volume Growth	Sep'24	Dec'24	Mar'25	Jun'25	Sep'25
Hotel Occupancy Rate	62.0%	66.0%	69.0%	62.0%	61.0%
Phoenix (LTL)	0.1%	18.6%	-19.0%	8.2%	1.6%
Smartphone	4.5%	-3.5%	-5.9%	5.7%	4.3%
Blinkit (GOV)	122.2%	120.2%	133.9%	140.1%	151.9%
NYKAA (Personal Care)	25.6%	24.8%	21.6%	17.0%	23.1%
Page Industries (Innerwear)	6.7%	4.7%	8.5%	1.9%	2.5%
Jubilant (QSR)	2.8%	12.5%	12.1%	11.6%	9.0%
Britannia Industries	8.0%	8.0%	6.0%	2.0%	-3.5%
Staples (HUL)	3.0%	0.0%	2.0%	4.0%	0.0%

Brand loyalties are becoming fluid; consumers are spoiled for choice, thanks to rising digital penetration and easier logistics. Companies must work harder to retain customers. Businesses that fail to adapt will see their relevance and valuations compress over time.

Digital and e-commerce are playing an increasingly central role in this shift, and the scale of change is remarkable:

- India has become the third-largest digital economy in the world with 84 crore internet users, double the number in 2016 as per the State of India's Digital Economy Report 2024
- UPI transactions have scaled to a massive size. First five days of this December '25 recorded 70 crore UPI transactions daily, surpassing transaction volume processed by VISA globally (65 crore transactions daily)
- The value of mobile phone sales in India is now higher than the value of passenger car sales. This would have been unimaginable 10 years ago.
- Apple entered India in 2008. In FY25, its India revenue crossed USD 9.5 billion, overtaking Hindustan Unilever, a company that has dominated Indian households for 70 years.

This shift is dramatic not only in daily life, but also for investors. Much of the wallet-share migration is happening outside the listed universe - into quick-commerce, digital-first and D2C businesses which are rapidly scaling without traditional distribution muscle. Slowly, as more of these companies list, the investment universe is widening. But evaluating them is tricky, they are still burning cash to win customers, and traditional valuation tools don't fit neatly.

Yet, given India's scale and early stage of penetration, some of these companies will eventually grow profitably. That is one of our key learnings and why we have selectively begun investing in new age businesses, where we see long-term potential for success.

## SHAKE-UP IN COMPETITIVE LANDSCAPE

### Real challengers have arrived

For many years, market leaders in a few key sectors like building materials, soft drinks and retail enjoyed a comfortable dominance. Strong pricing power, large market sizes and consistently high returns allowed them to generate exceptional profits and command premium valuations. Their leadership appeared stable.

But high returns sustained over long periods rarely go unnoticed. Over the past couple of years, credible and well-capitalised challengers have stepped in. They studied these businesses carefully and concluded that the opportunity was simply too attractive to ignore.

At the same time, corporate India has significantly strengthened its balance sheets over the past few years. Across sectors, leverage has come down with overall leverage in NSE 500 universe (excluding banks) reduced from 54% in FY19 to 42% in FY26 (trailing twelve-month basis).

With lower leverage and surplus capital, entering these attractive categories became the most logical and efficient use of their capital.

The table below shows how much debt a company has compared to its own

### Net Debt to Equity: Strengthening balance sheets

Sectors	FY19	FY20	FY21	FY22	FY23	FY24	FY25*	FY26*	FY26* vs FY25*	FY26* vs FY19
Information Technology	-39%	-29%	-33%	-30%	-27%	-29%	-31%	-33%	-2%	6%
ex TechM	-39%	-29%	-33%	-31%	-28%	-30%	-32%	-34%	-2%	5%
Energy	47%	56%	38%	35%	37%	29%	33%	28%	-5%	-19%
ex RIL	45%	70%	74%	57%	55%	40%	47%	37%	-10%	-8%
Consumer Staples	-6%	-12%	-9%	-6%	-9%	-9%	-9%	-6%	3%	0%
ex ITC	-1%	-8%	-8%	-3%	-8%	-6%	-5%	-4%	1%	-3%
Communication Services	132%	238%	839%	728%	854%	663%	487%	300%	-187%	168%
Materials	65%	63%	49%	33%	44%	48%	53%	53%	0%	-12%
Ex Metals	126%	138%	86%	40%	64%	70%	83%	80%	-3%	-46%
Consumer Discretionary	46%	56%	54%	59%	57%	43%	43%	33%	-11%	-14%
ex TAMO	37%	46%	36%	41%	43%	41%	41%	36%	-5%	-2%
Industrials	52%	59%	52%	48%	42%	39%	44%	43%	-2%	-10%
Utilities	137%	140%	136%	128%	120%	110%	101%	110%	9%	-28%
Health Care	16%	11%	4%	-2%	4%	-2%	-2%	-4%	-2%	-20%
Real Estate	52%	40%	33%	28%	29%	28%	20%	17%	-3%	-35%
Total, Ex BFSI	54%	59%	52%	47%	50%	44%	45%	42%	-3%	-12%
Ex Energy, Metals	63%	68%	65%	56%	60%	54%	55%	51%	-4%	-12%

\*Numbers are taken on TTM basis.

As a result, serious competition has emerged in sectors such as paints, cables and wires, soft drinks, building materials, grocery retail and value fashion. The impact has been felt on margins and valuations that have corrected sharply in several cases.

The question we are wrestling with: Will these incumbents regain their leadership, or is this an inflection point that causes lasting damage?

**Our view:** Some franchises may face structural challenges and see their dominance weaken. Others will adapt, innovate and return stronger. In some cases, the market itself may expand, creating enough room for both incumbents and new entrants to grow.

These periods of disruption are rarely comfortable, but they also create opportunity. We are closely tracking these shifts to invest selectively in beaten-down businesses where we believe strong franchises can navigate the competition and emerge resilient over time. At the same time, we are equally focused on companies willing to reinvent themselves, adopt new trends early, and build competitive advantages in the process.

## TARIFFS, TARIFFS, AND MORE TARIFFS

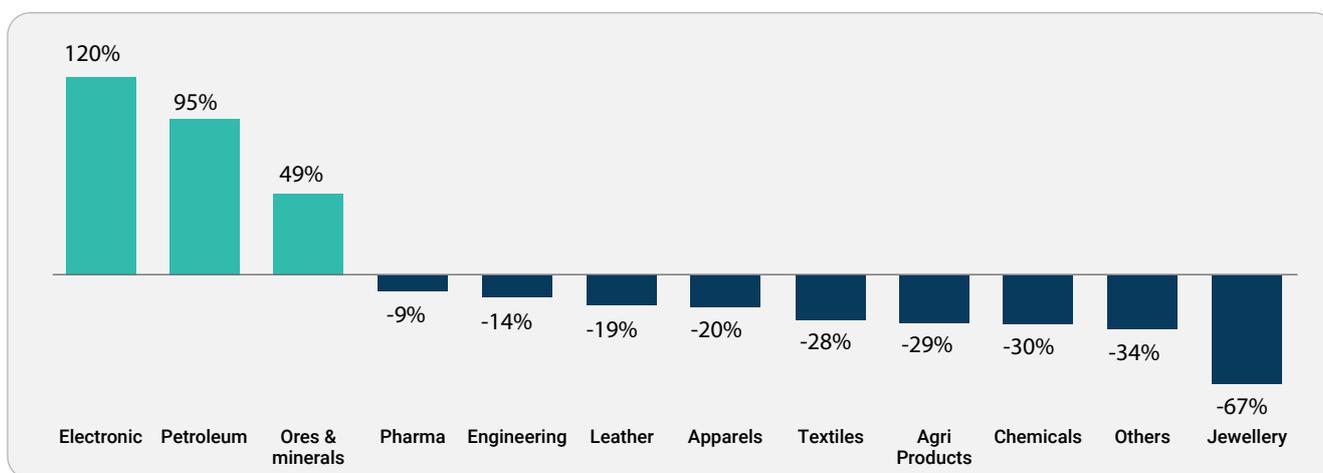
### The plot twist no one saw coming

What started as a confident belief that India would benefit the most from a global shift away from China has taken an unexpected turn. Instead of gaining from favourable tariffs and early bilateral engagement, India has found itself among the more affected countries. The US decision to impose punitive tariffs linked to India's purchase of Russian crude completely changed the narrative.

This episode captures the reality of the world we are operating in today - predictability is low, policy stability is fragile, and narratives can change overnight.

- The rupee slipped close to ₹90 per dollar, signalling rising nervousness.
- Labour-intensive export sectors such as jewellery, agriculture, textiles & apparels are already under pressure, a concern given these industries support over 50 million jobs directly and indirectly.
- Exports to US have slowed in some of the sectors, post tariff imposition

### India's Exports to US (Oct 2025, % YoY)



The scale of these tariff actions is unprecedented. The world has not seen tariff aggression of this magnitude in nearly a century, hence forecasting the outcome would be naïve - the playbook simply doesn't exist.

What we can say with confidence is this – High tariffs are inflationary and can cause economies to slow. In an already stretched global system, they limit the ability of central banks to cut interest rates during crises - a tool used extensively in 2008, 2020 and 2023. It is therefore not surprising that 30-year US bond yields remain elevated despite recent rate cuts. Markets are clearly pricing in risk.

Tariffs are never a one-way story. They trigger retaliation and paralyse long-term investment decision making. Businesses cannot plan capex confidently when policy direction flips every day. For now, the small relief is that Indian banks have not flagged any major asset-quality stress from MSMEs. But the risk is clear - if high tariffs persist, the pain will eventually surface.

We are closely tracking pertinent metrics across sectors to gauge the impact; however, we believe we have only seen the opening chapter, the aftershocks will reveal themselves over time. Nobody exactly knows what

### **How are we dealing with it in our portfolios**

If conditions were to turn significantly adverse, have we built a portfolio that is fully protected against every scenario? No, and realistically, no one can. Outcomes in situations like this only become clear with time. On the other hand, if tariff developments turn out to be benign or even favourable, constructing a portfolio purely for “defence against tariffs” would also prove to be the wrong strategy.

Instead, we prefer a more balanced lens.

We are evaluating risk primarily through valuations, asking how much downside protection a stock offers relative to its price and then adjusting exposures accordingly. In a world where certainty is rare and headlines change quickly, we believe this remains the most sensible and balanced way to invest.

## MARKET CAPITALISATION MYTH

### Asset allocation strategy or just a label?

We often get questions like “Are small & midcaps too risky now?”

There is no simple yes or no answer to this. Having seen multiple market cycles and sharp drawdowns ourselves, we know that giving a straight answer would be misleading. But this leads to a broader question: Is market-cap allocation genuinely a sound strategy, or is it simply a convenient way of grouping stocks?

To answer this, it helps to step back, examine the data, and understand the long-term trends shaping returns.

In CY25, returns (TRI) across market-cap segments were as below:

Nifty 50	Nifty Midcap 150	Nifty Smallcap 250
11.4%	5.5%	-6.3%

However, the picture changes when we zoom out to the last five years (CAGR):

Nifty 50	Nifty Midcap 150	Nifty Smallcap 250
14.6%	23.8%	23%

Market leadership does rotate over time, but short-term performance rarely captures the full picture. India’s listed markets have evolved significantly. With every new IPO, the small and mid-cap universe is growing, not contracting. Entirely new, relevant business segments have emerged in recent years, many of them sitting squarely within the small and mid-cap space.

Examples include:

- E-commerce platforms
- Pure-play EV players
- Value-fashion retailers
- Digital-first and D2C businesses
- Electronic manufacturing services
- Insurance platforms
- Niche engineering companies serving aerospace
- Hospitals & Diagnostics
- Hotels & Travel

These sectors are critical to India’s long-term growth story and ride on the changing consumption patterns that we mentioned earlier. While market-cap leadership may interchange in the short run, long-term wealth creation ultimately depends on three things: growth potential, size of opportunity, and the strength of a company’s competitive advantages.

## What about Valuations?

Yes - small and midcaps do appear expensive today. In many cases, that premium is partly justified, because several segments are delivering high growth, especially the sectors mentioned above.

But part of the valuation premium is not purely fundamental, it is also shaped by the regulatory structure. For example, the mid-cap universe in India is narrowly defined as companies ranked 101–250 by market capitalisation. When large pools of capital chase this limited basket, valuations can get pushed up almost mechanically.

This is why, in our view, the best response is time. It helps absorb volatility that comes along with the growth opportunities in small and midcap companies.

## What should investors do?

It depends on who you are (risk appetite) and how long you can be patient? (investment horizon)

For investors with a long-time horizon and the ability to tolerate volatility, exposure to small and midcaps can create tremendous wealth as it has done in past. A long investment horizon allows investors to look through periodic valuation excesses and play the compelling growth stories unfolding in this space.

For others who want to play relatively safe and have an investment horizon of less than three years, a diversified or hybrid approach may be more appropriate, especially with the market at a high valuation decile and uncertainty around.

The key takeaway is simple: Market capitalisation is a useful guide, not a rulebook. What ultimately matters is owning the right business at the right price regardless of labels keeping in mind your risk profile and investment horizon.

## OUR IPO INVESTING APPROACH

### Selective, Disciplined and Evolving

At DSP, we have always believed that not every IPO merit capital and the period since 2022 has only reinforced this discipline. Of the nearly 194 IPOs launched during this time (considering those with a pre-IPO market capitalisation of over Rs 2,000 crore), we have participated in just 49, or about 25% of the total universe.

### What matters more than participation is outcome

Across the entire IPO universe since 2022, 62% of companies have outperformed Nifty 500, six months after listing. In contrast, 84% of the IPOs we invested in have delivered outperformance during the same period. We believe this outcome reflects the robustness and consistency of our IPO selection framework.

*Source: DSP Research*

## Our IPO Framework

Since many IPO-bound companies have short operating histories, we apply even stricter filters than we do for listed businesses. Our approach remains anchored in a few fundamentals:

- Scalable business models with long runways
- Clear competitive moats that can withstand disruption
- Attractive return ratios or a credible path to reach them
- High-quality management teams

However, in recent years, the primary market is abuzz with new age businesses and rightly so, as India's changing demographics, smartphone penetration, and digital infrastructure have created entirely new business paradigms.

Many emerging companies operate on digital platforms, with early years focused on growth and customer acquisition rather than profitability. This makes analysis through a traditional lens more challenging. For such businesses, we go deeper and ask:

- Can this company eventually generate healthy profits?
- Are unit economics improving as scale increases?
- Is the business model resilient to disruption?
- Will return ratios eventually justify the valuations?
- Is the management team trustworthy, with sharp focus on execution?

The encouraging development is that many new-age founders are now becoming profit conscious, which strengthens the investment case.

### Profitability comparison FY 22 to FY 25

Company	IPO Year	Rev Growth (Since IPO)	Profit (FY 2022)	Profit (FY 2025)	Profitability (25 vs 22)
<b>Eternal</b>	2021	915.2%	-12.1	5.3	Turned Profitable
<b>Policybazaar</b>	2021	461.1%	-8.3	3.5	Turned Profitable
<b>Delhivery</b>	2022	29.8%	-10.1	1.6	Turned Profitable
<b>Nykaa</b>	2021	225.7%	0.4	0.7	Profits Increased
<b>Honasa Consumer</b>	2023	38.4%	0.2	0.7	Profits Increased
<b>Swiggy</b>	2024	35.4%	-36.3	-31.2	Losses Reduced
<b>Paytm</b>	2021	146.3%	-23.9	-6.6	Losses Reduced
<b>Ather Energy</b>	2025	28.6%	-3.4	-8.1	Losses Increased
<b>FirstCry</b>	2024	18.2%	-0.7	-1.9	Losses Increased
<b>Ola Electric</b>	2024	-9.9%	-7.8	-22.8	Losses Increased

In short, our IPO strategy is selective, disciplined, and evolving with the market. We participate only where we see long-term value and our results so far reaffirm this fact.

## WHY 2025 LOOKED DIFFERENT

2025 was a year of transition. Markets moved from strength to consolidation. After four straight years of strong double-digit earnings growth for the Nifty 50 (FY21–FY24), earnings slowed sharply to low single digits through FY25 and into the first half of FY26, the full year now looks similar.

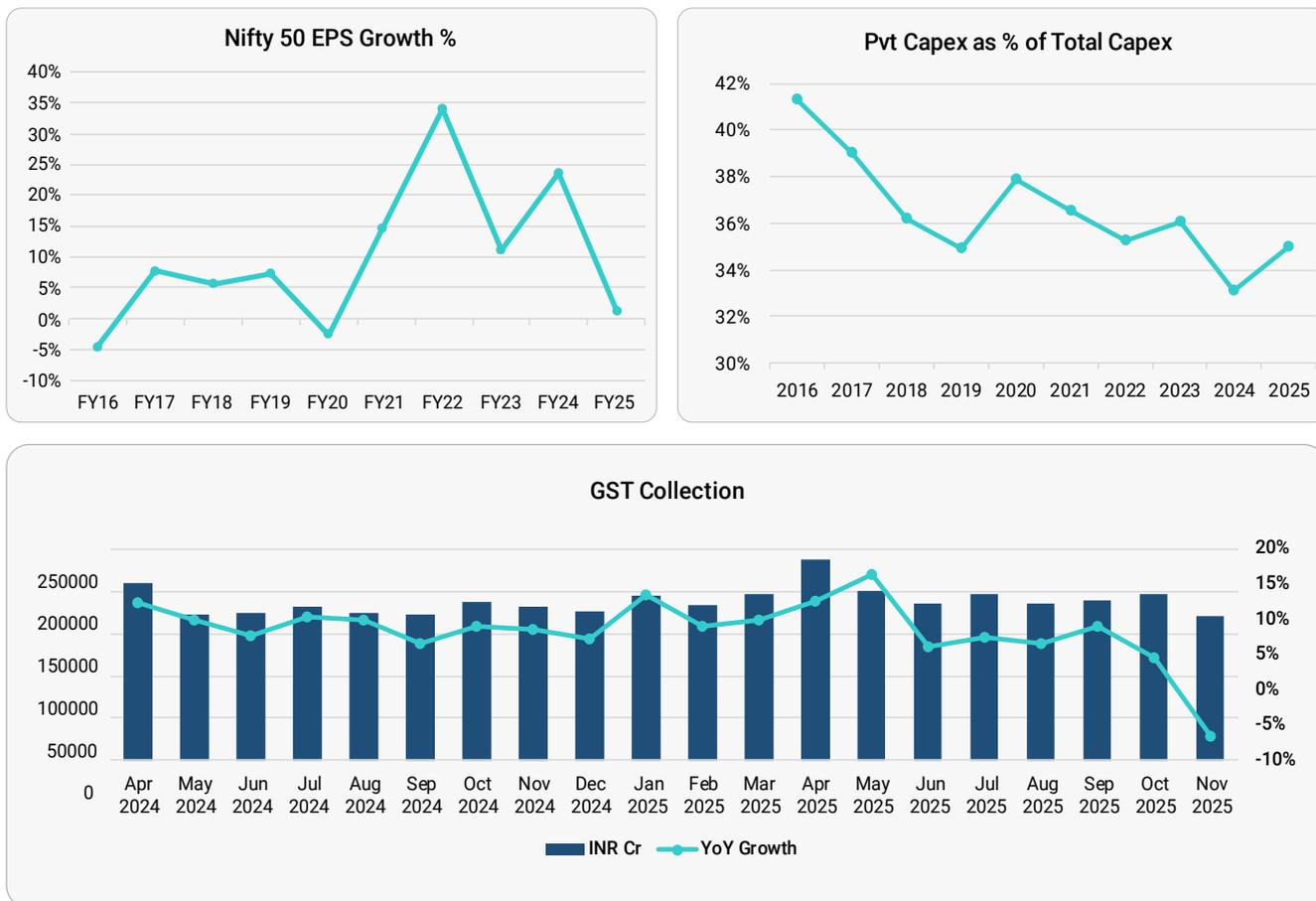
This slowdown wasn't driven by one factor; it was a combination.

Post-elections in May '24, government spending moderated and private sector capex did not fully step in to replace it. Banking liquidity tightened in early CY25, household consumption stayed soft, and uncertainty around US tariffs dampened foreign investor sentiment while hurting export oriented pockets such as textiles, gems & jewellery, and parts of engineering.

Globally, equity leadership turned extremely narrow, dominated by a handful of AI-driven technology giants - an area where India had fewer direct beneficiaries. Meanwhile, an extended monsoon disrupted agriculture and weighed on consumption categories.

(Source: DSP Research)

To sum up: In 2025 headwinds outweighed tailwinds, the following charts highlight this



The Government has clearly acknowledged the growth challenge and gradual steps are being taken to address them:

**Monetary Support:** RBI has eased financial conditions that have restored surplus liquidity and improved credit availability:

- Policy rate reductions of ~125 bps through CY25
- CRR cuts
- OMOs and dollar swaps

**Fiscal Impulse:** Government has announced stimulus worth ₹2.4 trillion, including:

- ₹1 trillion via personal income-tax relief
- ₹1.3 trillion through GST cuts
- Combined with lower interest rates, this puts more disposable income in consumer hands

**Structural Policy Reforms:** Government introduced a series of structural reforms to improve business confidence and support sustainable economic growth

- GST 2.0: Simplifies slabs, reduces costs on daily items.
- Labour reforms: Encourages MSMEs and manufacturers to hire, benefiting sectors historically vulnerable to labour disruptions.
- SHANTI Bill: Enables private participation in nuclear power - critical for long-term energy security.
- Free Trade Agreements: FTAs with the UK, EU and others diversify export markets and strengthen India's "China+1" positioning.
- Insurance Bill 2025: Expands penetration beyond Tier-1 cities, increases competition, and lowers premiums for households.

**What still needs attention:** Not everything is solved. We still need:

- Stronger private-sector capex
- Sustained job creation
- Clarity on US tariff policy

## OUR OUTLOOK FOR 2026

With a low earnings base, improving liquidity, targeted policy support and a gradual return of confidence, we see several credible catalysts for an earnings recovery ahead. Unlike other markets where performance is concentrated in a handful of AI-driven names, India continues to offer a broader structural growth story - multiple sectors, diverse drivers and meaningful room for long-term compounding. From a global investor lens, India may also be emerging from cyclical lows on both growth and the rupee, adding another layer of attractiveness.

**A few themes worth keeping an eye on:**

- **Banks & NBFCs:** Potential beneficiaries of rate cuts, steady credit growth and broadly stable asset quality.
- **IT Services:** Valuations are not demanding, this theme has underperformed the broader market in 2025. Any pickup in global tech spending, AI-led or otherwise can unlock upside.
- **Consumers:** Policy support and lower rates may help demand but shifting wallet shares and high competition call for selectivity.
- **PSUs:** Select PSU banks benefiting from same banking tailwinds and companies within the energy space that stand to benefit from low crude oil prices.
- **Power:** May benefit from stepped-up investments in renewables and a likely cycle improvement after last year's slowdown driven by extended monsoons.
- **Healthcare:** Hospitals, CDMOs (Contract Development and Manufacturing Organization) and pharmaceuticals may benefit from rising insurance penetration, improved access and greater health awareness.
- **Agri-inputs:** After weak earnings in H1 FY26, valuation corrections and a better Rabi outlook may support recovery.

These are broad themes - but disciplined, bottom-up stock selection remains the real driver of outcomes.

## Risk Backdrop

Risks exist everywhere, and markets will always have periods that test patience. Global slowdowns, delays in India's growth recovery, rupee depreciation, or prolonged uncertainty around tariffs can all trigger sharp drawdowns. Investors should be mentally prepared for such phases.

But it is equally important to remember context.

India has faced crises before – currency pressures, oil shocks, global financial turmoil, pandemics. But it has repeatedly emerged stronger, more resilient, and better positioned. That underlying resilience remains our biggest anchor for long-term equity investing.

We continue to believe in the power of equities as a wealth-creation asset. Setbacks will come, they are part of the journey, but staying anchored to long-term goals, rather than reacting to every short-term shock, remains the most powerful discipline an investor can practice.

**To sum up** – India has just emerged as the world's fourth-largest economy, and continued growth momentum puts it on track to become the third largest in the years ahead. A young population keeps the dependency ratio favourable for long, while global supply chains are actively seeking alternatives – positioning India's talent pool, manufacturing capacity and services ecosystem as key beneficiaries. When combined with structural reforms and improving productivity, it creates a compelling long-term opportunity. For patient investors especially with markets coming off a softer cycle India remains a powerful, durable wealth-creation story.

## STRENGTHENING OUR FOUNDATION

### Staying disciplined in an unpredictable world

From a business standpoint, it is satisfying to note that about 74% of our equity AUM now sits in the top performance quartiles (Q1 and Q2) as of December 2025 - on a 3-year basis. This is a meaningful improvement versus December 2024, when the figures stood at 61%. While it has not been an easy journey we are pleased with the progress.

We have navigated an environment filled with uncertainty, often building investment hypotheses only to see many of them fall apart. Several of the challenges discussed earlier in this note have tested our conviction as investors.

*Source: DSP Internal Research*

One such paradox is visible in the chart below wherein good quality businesses (High ROE) that have traditionally outperformed other businesses have struggled to do so for three straight years post-COVID. Such behaviour highlights the dominance of liquidity, momentum & narrative, and a clear shift away from traditional preference for quality businesses, which explains underperformance in a few of our funds during this period. But the good news is, the trend is changing again in favour of good quality businesses.

### Average CY return of NSE 500 stocks split in ROE buckets

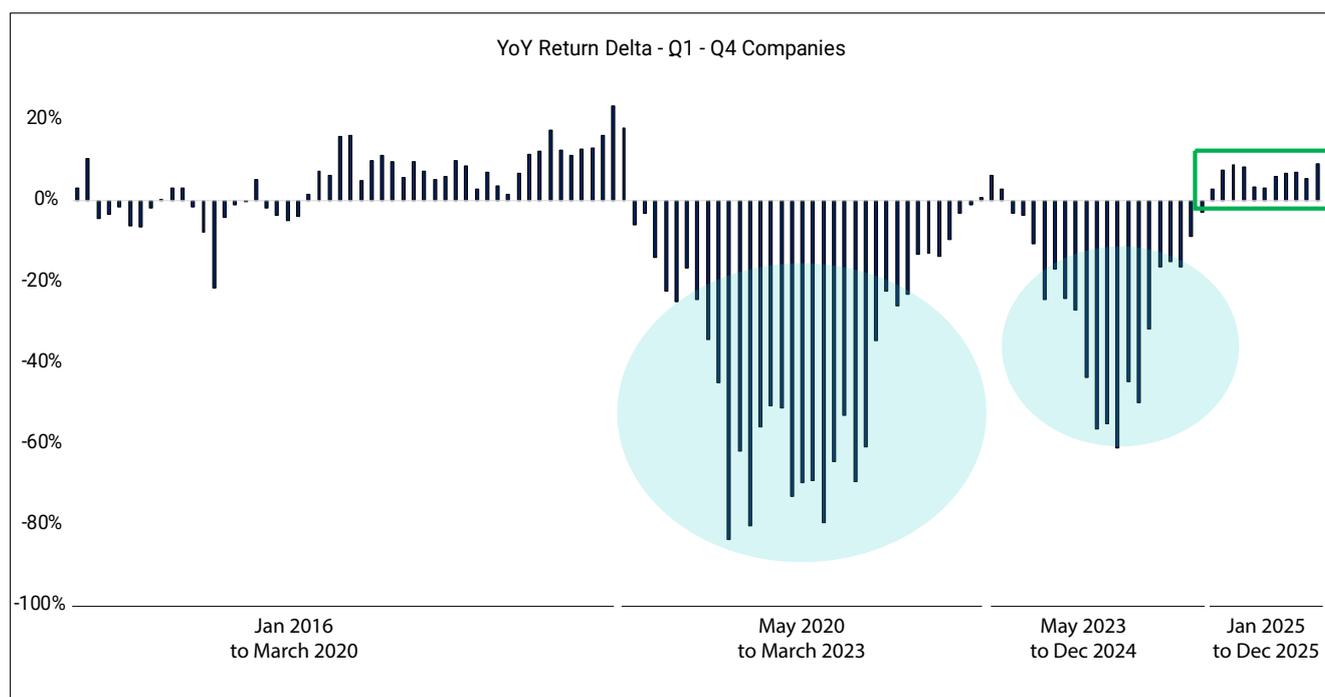
ROE Buckets	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
ROE Below 15	1	0	54	-24	-8	15	59	6	45	22	-3
ROE Above 15	15	9	55	-10	5	39	52	0	42	28	-2

Source: DSP ARQ. Nifty 500 Stock on equal weight basis

A similar trend is visible in our forensic accounting model which buckets Nifty 500 companies in quartiles based on accounting scores. Under this framework, Quartile 1 (Q1) represents companies with the highest transparency and strongest business practices, while Quartile 4 (Q4) identifies those with the most aggressive or laggard accounting policies.

In the last few years, Q1 companies have underperformed Q4 companies implying that the market was indifferent to accounting quality, ascribing higher value to "laggards" while failing to reward companies with superior governance. This defied the longer-term trend apparent in chart below. However, the tide is turning now in favour of Q1 companies again.

### Average return differential of Q1 and Q4 companies (bucketed on accounting score)



Source: DSP ARQ

## Strengthening our foundation, using ARQ

The Fosbury golden jump was not an overnight triumph. It was the result of years of perseverance, practice, and the courage to withstand widespread scepticism. He began refining his unconventional technique at the age of 16, long before it was understood or accepted.

In the same spirit, we are strengthening our foundations year after year by investing in better processes and more resilient frameworks, not as a reaction to change, but as a deliberate long-term commitment. Recognising how complex and unpredictable investing has become, we consciously choose to keep investing and strengthening our in-house research platform ARQ that helps us stay disciplined and anchored to our investment framework.

### Why does ARQ matter?

- It **analyses terabytes of data quickly** empowering us to fight narratives with data driven conviction, essentially bringing objectivity to decision making.
- It **brings valuation discipline** in our Buy/Sell decisions by reinforcing valuation checks like implied expectations in price, odds of making money at current valuations etc.
- Enhances our research by **bringing more evidence** and testing mere opinions in research, minimizing individual bias.
- Brings new or previously overlooked/ rejected ideas to the fund manager's desk by **monitoring relevant operating metrics** across sectors and companies through an alert mechanism.
- Applies a **forensic lens to all investment decisions** through an embedded forensic model, helping us prevent costly accidents.

We have adopted this distinctive approach keeping first principles of investing in mind and not with the sole aim of topping performance charts in every market cycle, though we would certainly welcome that outcome.

Our objective has been simple and consistent - to avoid large capital erosion from poor decisions, to learn from our mistakes, and to invest with care and conviction.

## OUR BELIEF SYSTEM

“Do the right thing consistently, outcomes are merely its echo.”

The Fosbury Flop underscores the enduring importance of process over immediate outcome. The breakthrough was built through sustained experimentation and refinement, not a single inspired leap. Early results were inconsistent and risky, but strong processes compound over time. The long-term payoff reshaped the sport entirely. Durable advantages often require patience through discomfort.

As markets evolve and new opportunities emerge, we believe that a strong framework, clarity of thought, and long-term orientation matter more than ever. **We remain committed to this approach across our equity offerings and invite investors to evaluate our equity funds through this lens - not as short-term trades, but as a long-term partnership in wealth creation.**

We do not promise to be the best-performing fund in every phase. What we do promise is this - we will remain disciplined, thoughtful, and focused on protecting and compounding your hard earned money in an increasingly complex world.

**That, we believe, is the most honest commitment we can make.**



**VINIT SAMBRE**  
HEAD - EQUITIES



**ROHIT SINGHANIA**  
CO-HEAD - EQUITIES



**VIPIN VIJAY**  
VP INVESTMENTS - EQUITY

**Disclaimers:**

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The investment approach / framework/ strategy mentioned herein are currently followed by the fund and the same may change in future depending on market conditions and other factors. 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).

Large caps are defined as top 100 stocks on market capitalization, mid caps as 101-250 small caps as 251 and above.

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