

Nepean Capital

4Q FY25 Quarterly Newsletter

The Nepean Long Term Opportunities Fund II is an open-ended, multi-cap India Special Situations fund. It has given a return of +45.2% (net of fees) at an IRR of +11.4% since the first close (Oct 14, 2021). It has outperformed the benchmark NIFTY500 by 870 basis points since.

Performance, Net of Fees as of March 31, 2025

	Fund I*				Fund II**				
Period	CY18^	CY19	CY20	CY21	CY21^^	CY22	CY23	CY24	CY25TD
Fund	+0.8%	+2.6%	+38.4%	+31.3%	+0.2%	+9.2%	+36.1%	+5.7%	-7.8%
Benchmark	-11.0%	-9.5%	+21.5%	+30.7%	-4.1%	+3.0%	+25.8%	+15.2%	-4.6%
Outperformance (bps)	+1180	+1210	+1690	+60	+430	+620	+1030	-950	-320
Since Inception				+87.9%					+45.2%
Benchmark				+27.9%					+36.5%
Outperformance (bps)				+6000					+870
IRR				+26.0%					+11.4%

*Benchmark NIFTY Small Cap Index

^First close Sep 18, 2018

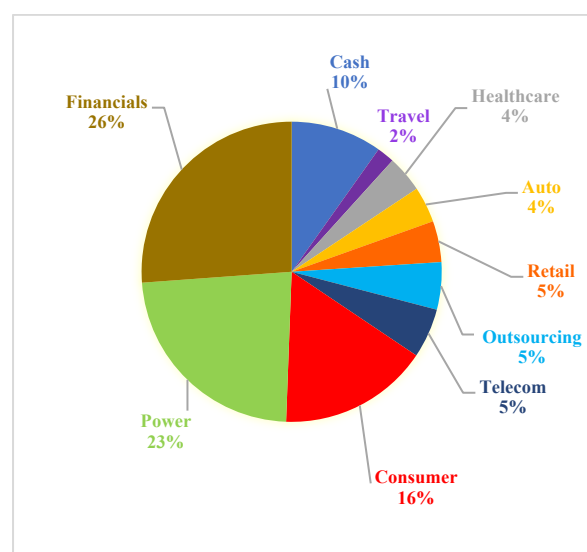
NAV is calculated monthly

**Benchmark NIFTY500 Index

^^First close Oct 14, 2021

Fund I was closed in May 2021

Sectoral Break-up



Top 10 Holdings

Script Name	% Allocation
Varun Beverages Ltd.	13.88%
Aadhar Housing Finance Ltd.	9.47%
INOX Wind Ltd.	8.47%
Manappuram Finance Ltd.	8.17%
Transformers and Rectifiers India Ltd.	5.44%
Bharti Airtel Ltd.	5.34%
Kotak Mahindra Bank Ltd.	4.69%
Adani Energy Solutions Ltd.	4.06%
Aster DM Healthcare Ltd.	3.95%
Bajaj Auto Ltd.	3.87%

Last quarter's events were eclipsed by last week's *Tariffs Wars* when on April 2 U.S. President Donald Trump announced (as promised) reciprocal tariffs on as many as 90 countries. He declared a national emergency by invoking his authority under the International Emergency Economic Powers

Act of 1977 (IEEPA). The media release pointed out that in 2024, U.S. trade deficit in goods exceeded \$1.2 trillion, a number that was not sustainable. In 2023, U.S. manufacturing output as a share of global manufacturing output was 17.4%, down from 28.4% in 2001.

<https://www.whitehouse.gov/fact-sheets/2025/04/fact-sheet-president-donald-j-trump-declares-national-emergency-to-increase-our-competitive-edge-protect-our-sovereignty-and-strengthen-our-national-and-economic-security/>

A baseline tariff of 10% would apply to all countries (except Canada and Mexico), effective April 6. Secondly, most major trading partners, excluding Canada and Mexico, would face an additional tariff that equals half the ratio of the US bilateral trade deficit with the country divided by US imports from that country.

Between April 2-8, the U.S. equity markets fell off a cliff, with the S&P500 down ~12%, annihilating as much as \$7.7 Tn of wealth, a new record. (The previous loss of market was when \$4.4 Tn of stock market value evaporated in the two days ending March 12, 2020, i.e. as word of COVID started to spread). The week saw the third largest spike in 5-day realized volatility since the crash of 1987, trailing only the GFC and COVID. So, no surprise that last week investors poured \$60 Bn into U.S. money market funds, taking the total to a record \$7.4 Tn. The yield on the 10-year U.S. treasuries spiked to 4.49%, up 50 bps in just a week. Looks like all these events drove President Trump to defer the reciprocal tariffs for 90 days, i.e. upto July 9, except for China.

Investment banks have slashed GDP growth forecasts for the U.S. (from 2.8% in 2024 to 1.8% in 2025), with some economists fearing a global recession. At 5363 the S&P500 is still not cheap, trading at 19x one year forward P/E vs. bottoming at 14x in 2018, 13x in 2020 and 15x in 2022. President Trump seems to be counting on the expectation that most countries will heel and lower tariffs on American goods. Last week the world watched as the U.S. and China attempted to outdo each other on tariffs. The final score: China has hiked tariffs on U.S. goods to 125% in retaliation to the U.S. imposing 145% tariffs on Chinese goods (smartphones, laptop computers, memory chips and other electronics are exempt).

Can India turn this Crisis into an opportunity ?

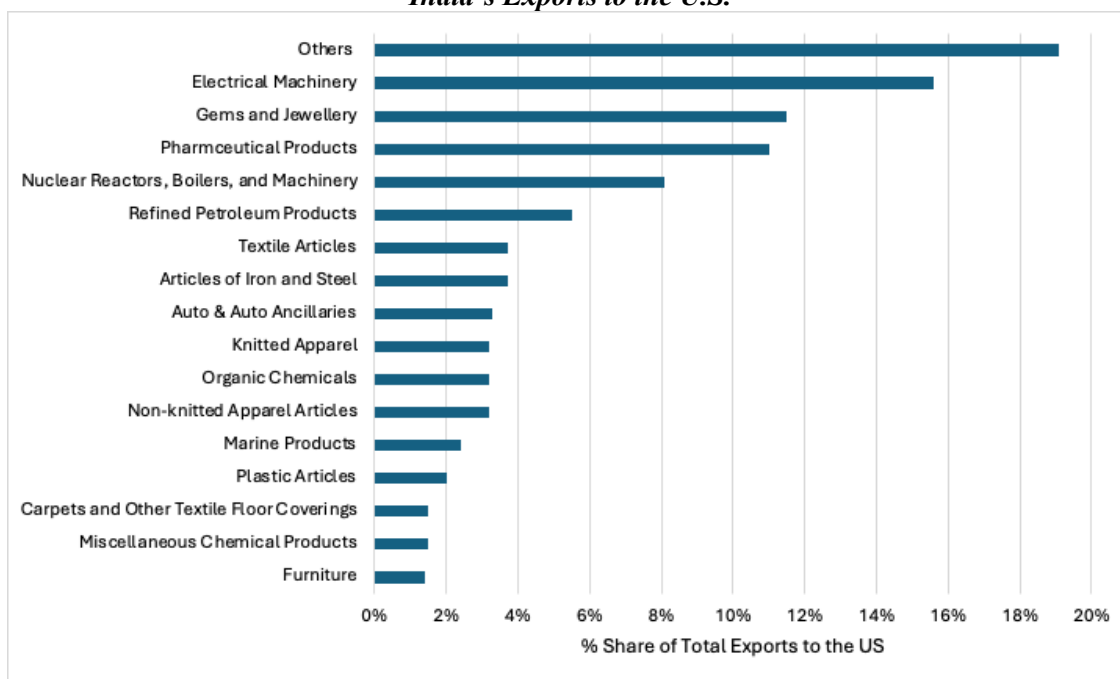
Last year, India's merchandise exports to the U.S. were only \$80 Bn (or 18% of total goods exports of India and a mere 2% of GDP). India's trade surplus with the U.S. was \$46 Bn, much less than China's \$292 Bn and Vietnam's \$123 Bn. Unlike China, India hasn't responded as yet to US tariffs. The Ministry of Commerce & Industry said that it is examining implications and studying opportunities.

That said, we believe that this is an opportunity for India to gain export market share from China, Vietnam and Mexico by playing the tariff arbitrage in industries ranging from footwear to garments to electronics. The Modi government is focused on improving the ease of doing business, tax laws and infrastructure. The poster child is Apple which last year made \$22 Bn worth of iPhones in India, +60% YoY. Today one in five iPhones sold globally are *Made in India* prompting the below meme:

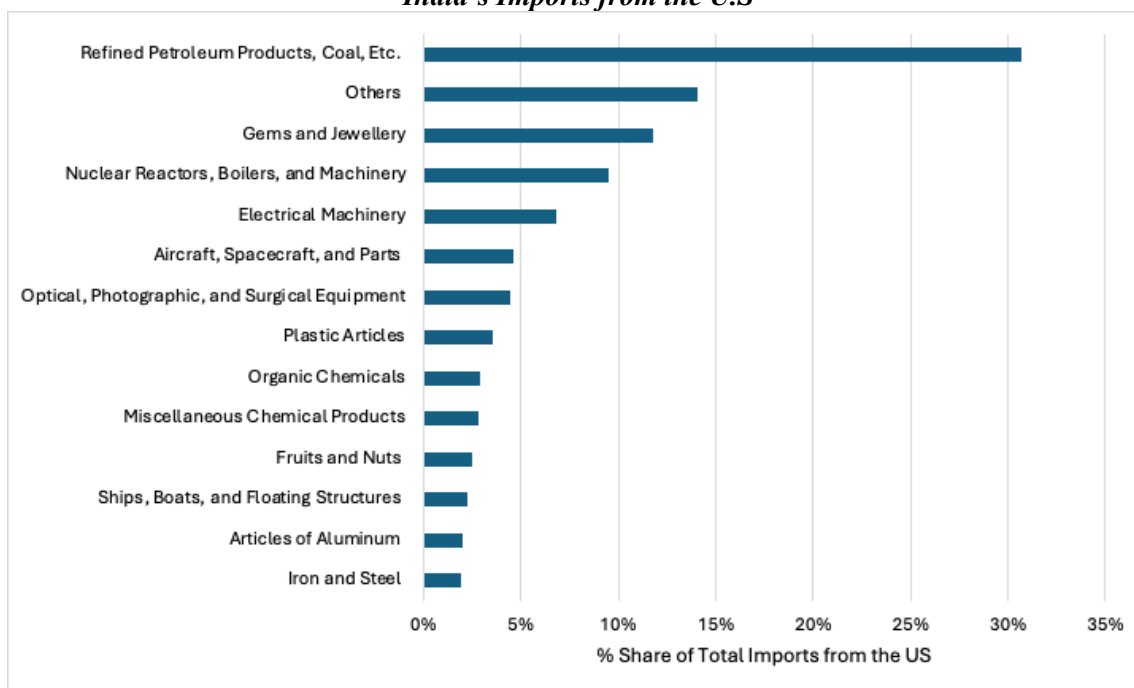


India is strengthening its position as a global manufacturing hub, with value addition in electronics manufacturing having increased from 30% to around 70%. For example, it has cut down its imports of fully built air conditioners from 35% in FY19 to just 5% in FY25. Key parts like compressors, copper tubes, and aluminum coils are now being made in India. The two sectors that have been spared from tariffs, for now, are Pharma (11% of India's exports to the U.S.) and IT services (not counted in merchandise exports). But if economists' forecasts of a recession in the U.S. do come true, then revenues of Indian IT companies will be impacted as American companies cut back on spends. India's largest IT company, TCS, just reported tepid results for the March quarter with net profit down 2%, EBIT margins down 30 bps and full-year FY25 US\$ revenue growth of 3.8% vs 4.1% in FY24.

India's Exports to the U.S.



India's Imports from the U.S.



There's been much talk over the past month that Tesla will be finally enter the Indian market. Currently among American auto manufacturers, only Chrysler's JEEP is sold in India; GM and Ford shut their Indian operations several years ago. However, in India Tesla will face competition from Chinese EV makers like BYD and MG Motors, both of which have a four-year head start.

Meanwhile on the ground in India

The first quarter of this year saw India's benchmark NIFTY50 correct 8.5% (the NIFTY500 -13%, NIFTY Small Cap -16%) led by persistent selling by foreign portfolio investors (FPIs). YTD they have net sold \$16.5 Bn, the second highest in Asia after Taiwan (-\$17.6 Bn). That's more than offset by net inflows into domestic mutual funds of \$24.5 Bn by retail investors, in addition to the +\$60 Bn in CY2024. But YTD, the index is still down 4% implying that the third pool of capital, i.e. *direct* retail, family offices and alternative funds (flows not captured in the domestic institutional numbers) remain net sellers. The tepid returns over the past 12 months in the Indian markets have finally begun to impact monthly equity flows into mutual funds. Last month, net inflows fell to Rs.25,082 crores/\$2.91 Bn, down almost 40% from the peak in Dec 2024. SIPs (systematic investment plans) stoppage ratio surged to 128%, demonstrating that more mutual fund investors either stopped their SIPs or they did not renew them after their tenures ended. The Indian market has been resilient only thanks to domestic flows and any weakness could cause the correction to intensify.

Conclusion

After the recent correction, the NIFTY50 is trading at 18x FY26. The good news from the U.S. tariff fallout is that the impact on India is likely to be marginal. A second order impact is that the price of Oil (Brent) has fallen 12.5% to \$65/bbl, a large positive for a country that imports 80% of its annual needs. That said, we hope that U.S. tariffs become a catalyst for much needed reforms on trade and reduce import duties that compel Indian companies to be more competitive globally. It will also hasten the Indian government's efforts to sign FTAs (Free Trade Agreements) with the EU, UK and other countries/trading blocs.

We believe that the current slowdown in consumption will improve with falling interest rates (last week the RBI cut 25 bps) and lower inflation. S&P estimates that India's GDP will grow at 6.5% in the current fiscal year, strongest among the large economies. We remain structurally bullish on India and believe that it should outperform its EM/Asian peers given its low dependence on exports. Hence, our portfolio reflects more domestic plays such as Bharti Airtel, Trent, Kotak Mahindra Bank, Aster DM Healthcare (a play on the merger with Blackstone's India hospital's business), Manappuram Finance (India's second largest gold loan company that just got a large investment from Bain Capital) and Interglobe Aviation (India's largest domestic airline with a 64% market share). Moreover, we are betting on India's power industry (23% of AUMs), which offers multi-decadal growth, with stocks like Transformers & Rectifiers, Inox Wind, TD Power and Adani Energy Solutions.

Here are some of the top *non-financial* stories emerging from India that I send out every week (let me know if you want to be added to the mailing list):

For most of history, India was the world's richest region: William Dalrymple

<https://www.indiatoday.in/india-today-insight/story/for-most-of-history-india-was-worlds-richest-region-william-dalrymple-2695927-2025-03->

From viral yoga guru to flourishing apple biz, four people tell us how a lockdown pivot changed their lives

http://timesofindia.indiatimes.com/articleshow/119343135.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

Husain auction record may be the big breakthrough moment for Indian art: Gram Yatra, was sold last week by Christie's for \$13.75 million

http://timesofindia.indiatimes.com/articleshow/119343993.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

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