

Nepean Capital

4Q CY25/3Q FY26 Quarterly Newsletter

The Nepean Long Term Opportunities Fund II is an open-ended, multi-cap India fund. It has given a return of +24.8% (in US\$, net of fees) at an IRR of 5.4% since the first close (Oct 14, 2021). It has underperformed the benchmark NIFTY500 by -310 basis points since. Since inception, Nepean Capital's funds have delivered a US\$ IRR of +10.7% vs. the benchmark of +6.7%.

Performance in US\$, Net of Fees as of December 31, 2025

Period	Fund I*				Fund II**				
	CY18^	CY19	CY20	CY21	CY21^^	CY22	CY23	CY24	CY25TD
Fund	+5.3%	0.0%	+35.1%	+32.3%	+1.3%	-1.8%	+35.6%	+2.6%	-9.9%
Benchmark	-7.0%	-11.8%	+18.6%	+31.7%	-3.0%	-7.3%	+25.3%	+11.8%	+1.6%
Performance vs. Benchmark (bps)	+1230	+1180	+1650	+60	+430	+550	+1030	-920	-1150
Since Inception				+84.1%					+24.8%
Benchmark				+28.2%					+27.9%
Performance vs. Benchmark (bps)				+6020					-310
IRR				+24.0%					+5.4%

*Benchmark NIFTY Small Cap Index

^First close Sep 18, 2018

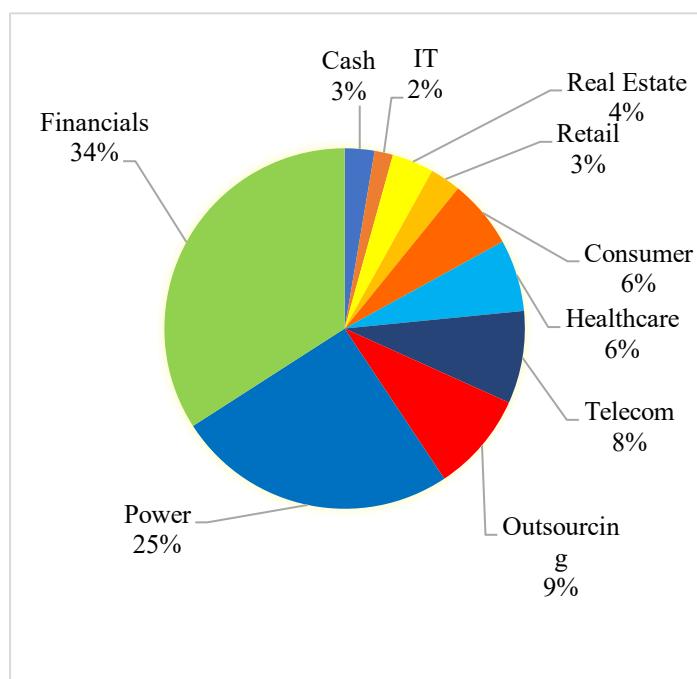
NAV is calculated monthly

**Benchmark NIFTY500 Index

^^First close Oct 14, 2021

Fund I was closed in May 2021

Sectoral Break-up



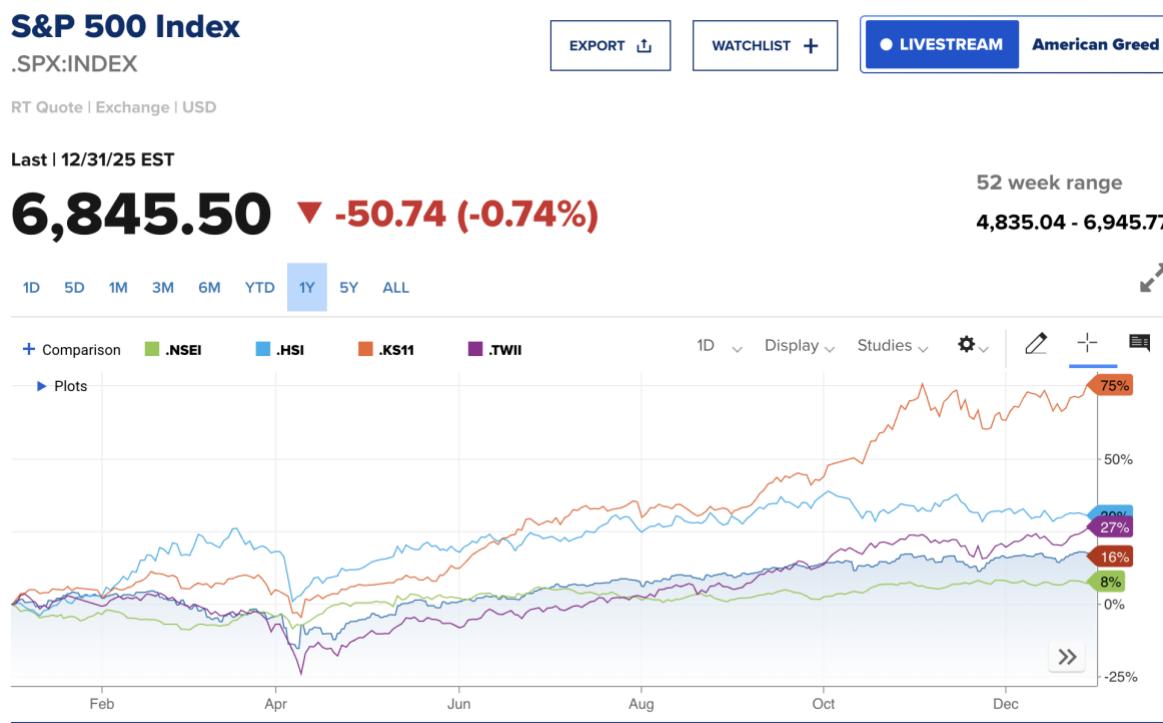
Top 10 Holdings

Manappuram Finance Ltd.	10.37%
Bharti Airtel Ltd.	8.30%
TD Power Systems Ltd.	8.28%
Piramal Finance Ltd.	8.15%
Aadhar Housing Finance Ltd.	7.30%
Aster DM Healthcare Ltd.	6.44%
JSW Energy Ltd.	6.21%
Adani Energy Solutions Ltd.	6.11%
Kotak Mahindra Bank Ltd.	6.08%
Amber Enterprises India Ltd.	5.30%

2025 Was a Year of Records: Record domestic inflows, foreign outflows and IPOs

Despite a record \$88 Bn of retail flows into domestic mutual funds and insurance companies, the last 15 months have been very challenging for the Indian equity markets. While the benchmark NIFTY50 rose 2% in US\$ terms, it masked the severe correction in the broader market. As many as 765 stocks of the Top 1,000 have fallen 25% or more from their respective 52-week highs; 108 have halved.

FPIs (foreign portfolio investors) also created a record in terms of net selling of \$18.5 Bn and the highest among Asian markets in CY2025; they have sold an additional \$4.5 Bn in January so far. IPOs and QIPs (follow-on equity offerings) soaked up a record \$28 Bn in capital, that included foreign companies' Indian arms, i.e. Hyundai Motors and LG Electronics; Coca-Cola India is planning an IPO this year too. Hence less than half of the retail flows made it into the secondary market. While FPIs mostly exited large caps, domestic family offices and HNIs sold off mid & small caps. Stocks with high valuations were punished the most. India ended the year as the worst performer in the region as investors favored tech-oriented markets like Korea (+75% US\$ returns), Taiwan, China/Hong Kong (in that order).



As a result, since hitting a high in Sept 2024, the fund's NAV ended 2025 down 15%. Consequently, we had two years of underperformance after five consecutive years of outperformance. This can be attributed to two stocks that rose to 32% of AUM, i.e. *Varun Beverages* (the bottler for Pepsico) and *Inox Wind* (India's second largest wind turbine manufacturer). Both stocks performed very well gaining 282% and 172% respectively, over the time that we held them. However, when the market corrected starting October, Varun and Inox fell by 28% and 37% respectively, severely affecting performance. Though both are strong long-term stories they were hurt by unfavorable short-term events and high valuations. Varun was impacted by the aggressive pricing and go-to-market strategy of *Campa Cola* re-launched by Reliance Retail. (*Campa* was a brand of cola popular in the 1970s and '80s before Coke and Pepsi returned to India). On the other hand, Inox Wind was hurt by short-term execution and order win challenges leading to lower growth than estimated by the street. We have since sold our positions in both stocks and restructured the portfolio.

In October I visited the U.S. where I met a cross section of fund managers and allocators who were underweight India relative to its MSCI weight by 200-250 bps. Historically, India's high valuations were not that much of a concern (23x CY2026 P/E), but factor in an earnings slowdown and *Houston*,

we have a problem. Moreover, consensus earnings growth for the S&P500 this year is 15% (same as in India), 23% for the NASDAQ 100 and 19% for the S&P Mid Cap 400. Given such high growth in their backyard, we can understand the reluctance for U.S. investors to venture overseas. That said, India remains a bottom-up stock picker's market offering opportunities in several sectors.

EMERGING SECTORS IN INDIA:

Data Centres + Power

While India doesn't offer any direct listed AI plays, India's power infrastructure is entering a structurally higher demand phase driven by the rapid global scale-up of artificial intelligence and hyperscale data centers. India has 2% of the world's compute capacity but 20% of the world's data. With over 800 Mn smartphones in use riding on 4G/5G networks and ARPU's as low as \$2.50, data consumption has grown sharply to 40 GB per month. Moreover, ChatGPT Go, Perplexity Pro and Gemini Pro are being offered free to resident Indians for the next 1-2 years. Indians will soon be among the highest users of AI in the world.

According to the International Energy Agency, electricity consumption from data centers has grown at a 12% CAGR over the past five years to approximately 415 terawatt-hours (TWh) and is projected to more than double to around 945 TWh by 2030, growing over 4x faster than overall electricity demand across other sectors. Investments in data centers in India have exploded with \$50 Bn committed to increase capacity 8x from the current 1GW. Google announced that it will invest \$15 Bn in building AI hyperscalers in the southern state of Andhra Pradesh.

Watch our podcast with Rachit Mohan, the APAC head of Data Centers at JLL:

<https://www.youtube.com/watch?v=xsLMO3DH8zI>

In the US alone, incremental data centre demand is expected to add nearly 100 GW of power capacity by 2030, with AI-driven workloads materially increasing power density, uptime requirements, and backup generation intensity. This shift has placed reliable, uninterrupted power supply at the core of global AI and data centre capex, materially expanding demand for high-capacity generators and mission-critical power equipment. The WSJ reports that data centres consumed less than 2% of U.S. electricity before 2020, but by 2028 could consume as much as 12%. We are seeing similar trends in power demand in India, across generation, transmission and distribution. In fact, power is the second highest sector allocation in our fund.

Our investee company *TD Power Systems* benefits from this capex cycle by being embedded in the power generation equipment layer, which captures a significant share of value creation beyond grid connectivity and downstream power distribution. As hyperscale data centers grow towards 100–150 MW per site, diesel-based solutions become uneconomical. This structurally favors gas turbine and gas engine-based generators, where *TD Power Systems* has strong engineering capabilities. The global generator market is estimated to expand from about \$52 Bn in 2025 to roughly \$73 Bn by 2029, driven primarily by data centres, gas-based power generation, and clean energy applications.

Semiconductors

India's semiconductor industry is moving into a sustained scale-up phase, with Budget 2026 (to be announced on Feb 1) projected to reaffirm a long-term policy commitment to domestic manufacturing, advanced packaging and equipment localization. Under the India Semiconductor Mission, around 10 projects spanning fabs, OSAT and advanced packaging have already been approved, with cumulative investments of roughly Rs.1.6 lakh crores/\$18 Bn and additional proposals under evaluation, creating a multi-year capex cycle anchored by electronics, EVs, data centres and AI. India's domestic semiconductor consumption is projected to cross \$100 Bn by the end of the decade, while the country is targeting a meaningful share of global semiconductor manufacturing alongside its already strong position in chip design.

We recently invested in *ASM Technologies*, which benefits from India's semiconductor capex by being embedded in the equipment, subsystem and services layer that captures a meaningful share of

fab and OSAT spending. As global OEMs are pushed to localize supply chains and Chinese suppliers exit India, ASM's pre-qualified status, local manufacturing footprint and long-standing relationships with leading semiconductor equipment players will allow it to mine higher wallet share. Its design-led manufacturing model, focused on customized, high-precision machines and subsystems, aligns well with the high-mix, low-volume nature of the early semiconductor capacity build-out which supports structurally higher margins.

The Rapid Growth of Global Capability Centers (GCCs)

India has emerged as the world's leading hub for GCCs. These are captive units established by multinational companies to deliver core technology, innovation, and business capabilities for their global operations. They have evolved far beyond traditional back-office functions with many global enterprises today running mission-critical platforms, product engineering, AI/ML models, cybersecurity, and innovation hubs directly from India. Also, GCCs can be found in a wide variety of sectors from technology and banking to healthcare and life sciences, to name a few.

There are around 1,900 GCCs operating across India representing over 50% of all global GCCs. They now employ over 2 Mn people, approaching 50% of the people working in the Indian software sector. By some estimates GCCs generate over \$60 Bn worth of annual economic value and this number is set to grow to \$100 Bn by 2030. India dominates this market because it has a unique combination of:

- Talent depth at scale: The world's largest STEM workforce with strong mid-to-senior leadership capability
- Cost efficiency: 30–50% advantage versus Western markets, though now secondary to value and speed
- Mature ecosystem: Experienced GCC leaders, service partners, real estate, legal and compliance infrastructure
- Policy and infrastructure support: SEZs, state-level GCC incentives, and robust digital infrastructure

Given the above key advantages, we expect this segment to continue to grow as more companies and higher tasks get outsourced to India. Although there are no listed GCCs companies, we believe the co-working and managed services market will be a clear beneficiary of this trend. We are thus playing it through *WeWork India*, the leader in this space.

Hospitality

India's hotel industry is entering the fifth year of its post-COVID upcycle, with momentum driven by rising disposable incomes, increased investment in travel infrastructure, ongoing recovery in foreign tourist arrivals, and growth in corporate travel and niche tourism segments including spiritual and wedding tourism. India's chain affiliated hotel room sector is underpenetrated compared to global markets, with 0.3 keys per 1,000 people vs. 22.1/2.7/2.2 keys per 1,000 people in the US/China/globally. HVS Anarock projects that nationwide occupancy and average daily room rates for India's hotel industry will reach 70% and cross the Rs.10,000/\$110 mark respectively in 2026 (in 2024, nationwide occupancy was 64% and average room rates ranged from Rs.7,800 to Rs.8,000).

These projections are supported by an imbalance between the industry's supply/demand CAGRs, which various estimates peg at 5-6%/10% through FY30. According to data from Hotelivate, 12,000 to 15,000 branded hotel rooms are expected to open in India each year through 2030. Segmental and geographic diversification of India's hotel room supply is a continuing trend; Horwath HTL estimates that the upper midscale and below segments account for more than 50% of the country's pipeline, while its top 8 cities only account for 41%.

Management commentary from leading domestic and international operators is optimistic. According to Rajeev Menon, Marriott's President for Asia Pacific (excluding China), "In 2-3 years, India – where we currently have 187 operational hotels and 200 in the pipeline – will rise to the third spot (third largest market for the company globally), with only the US and China ahead of it." With over

33,000 operational rooms, Marriott is the largest hotel company in India by room count, though Tata Group's Indian Hotels (Taj Group) has more operational properties (268).

Indian Hotels plans for significant growth in the years ahead. In a recent interview with ET Now, Indian Hotels CEO Puneet Chhatwal stated, "We are already at 610 (operational + pipeline properties), and each acquisition (referring to recent inorganic expansion in midscale, wellness, and boutique luxury segments) strengthens a brand or creates a new category. That's what will take us beyond 700 hotels (operational + pipeline properties) by 2030."

Check out our podcast with Puneet Chhatwal, the CEO of Indian Hotels (TAJ Group) held in May last year: <https://nepeancapital.com/news-and-insights/podcasts>

Over the past 2 months, the Nepean Capital team has travelled extensively across India for both work (company and plant visits) and personal (weddings, long weekends). This includes New Delhi, Bangalore, Ahmedabad, Kolhapur, Jaipur, Surat, Goa & Kolkata. Highlights:

1. Flights were mostly full, and hence not surprised when the country's largest airline, Indigo, announced a load factor of 84% for the month of December.
2. Notwithstanding pollution, hotels across the cities were pretty much fully booked. Of the hotel companies that have declared results so far (for 3Q FY26), ARRs are up a robust 10-12% YoY and RevPar +15%.
3. While foreign tourist arrivals have been tepid, domestic tourism has exploded and now accounts for 80% of total tourism revenue. Moreover, the number of listed hotel companies have sharply risen from four a decade ago to over 10 now.
4. Besides the palaces of Rajasthan or the beach resorts of Goa and Kerala, new wedding destinations have emerged such as Amritsar, Dehradun and Daman. We attended a wedding in Jaipur, Rajasthan in mid-December. As we were checking out of the Leela Palace hotel at around 10 am, guests for the next wedding were already arriving. The General Manager of the hotel told me that this has been an exceptionally strong wedding season.

Conclusion:

India is entering a reflationary credit upcycle, with fiscal-led demand stimulus (GST and income-tax cuts) combining with RBI's easing (rate cuts, CRR cuts, liquidity infusions) to support a sustained improvement in bank credit growth into CY26. GST Reforms 2.0 along with the income tax cuts are estimated to free up roughly 1.7–1.8% of GDP in household spending power for CY26, materially lifting consumption. These cuts are considerably boosting sales in aspirational categories like vehicles and other consumer discretionary.

Since early 2025, RBI has cut the repo rate by 125bps to 5.25%, cut CRR by 100bps and conducted OMOs and FX swaps, marking the most significant easing cycle since 2019. Non-food bank credit growth has accelerated to around 11–12% YoY from a low of 9% in May-25, with momentum driven by MSMEs, vehicle loans and NBFC on-lending. We expect systemic credit growth to continue its expansionary momentum due to the improving credit demand/supply situation, improving asset quality trends at banks (reviving their risk appetites), and a recovering rural economy.

The current earnings season is shaping up to be one of the most anticipated in recent times given the above fiscal measures. Moreover, the street is waiting to see if the GST cuts that have made products cheaper and left people with more disposable income will translate into earnings growth. While the free trade agreement (FTA) with the U.S. is stuck due to political maneuvering, the FTA with the EU was signed this week. As of FY25, the EU accounted for 17%/8% of India's total exports/imports (1.9%/1.6% of GDP). India's export basket with the EU has also moved up the value chain over time, with high value exports (electronics, machinery, chemicals) gaining share over traditional labor-intensive goods (textiles, jewelry, footwear).

The President of the European Commission, Ursula von der Leyen said:

.....Some call it the mother of all deals. One that would create a market of 2 billion people. "

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):

How five students used education to change their families' destiny

http://timesofindia.indiatimes.com/articleshow/124209120.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

Who is Bodhana Sivanandan? 10-year-old Indian-origin chess prodigy becomes youngest player to beat a world champion

https://www.financialexpress.com/world-news/who-is-bodhana-sivanandan-10-year-old-indian-origin-chess-prodigy-becomes-youngest-player-to-beat-a-world-champion/4016896/?ref=hometop_hp

How India can turn its food waste into value

https://www.indiatoday.in/india-today-insight/story/how-india-can-turn-its-food-waste-into-value-2811441-2025-10-31?utm_source=newsletter&utm_medium=story_link&utm_source=Netcore&utm_campaign=INSIGHT:+INDIA+TODAY+MAGAZINE&utm_medium=Email&utm_content=

Married at 12, Faced Abuse, Lived in a Slum — What She Built Next is Worth Rs.1,000 Crore/US\$113 Mn

<https://www.moneycontrol.com/education/married-at-12-faced-abuse-lived-in-slum-what-she-built-next-is-worth-rs-1000-crore-article-13673426.html>

MEDIA

<https://www.youtube.com/watch?v=EfuvmaFc09o>



In a wide-ranging discussion with CNBC, Gautam Trivedi of Nepean Capital comments on the US-India trade deal and reveals how he intends to play the AI theme through India's public markets.

IMPORTANT DISCLOSURE

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