Honesty and Integrity Investment (HNI Investment)

Email for March 2018

Dear Friends,

Here are the details of performance of HNI investment based on the share prices as on 31st March 2018.

Annualised Returns (IRR) (1) (2) (3)	HNI Portfolio	Nifty	Sensex
FY13	-10.6%	-5.3%	-3.7%
FY14	112.2%	21.1%	21.3%
FY15	21.6%	25.0%	23.0%
FY16	86.0%	-7.0%	-7.7%
FY17	168.3%	21.9%	20.1%
FY18	***66.4%***	***17.0%***	***18.8%***
Q4FY18	***-47.0%***	***-15.3%***	***-12.5%***
From Inception till 31st Dec. 2017	**86.1%**	**13.9%**	**13.0%**
From Inception till 31st March 2018	***84.0%***	***12.8%***	***12.1%***

(1) For all HNI clients and promoters (2) Inception was in August 2012 (3) Gross IRRs excluding the impact of HNI investment fees

You need to take note of three important things about our returns.

First we have reported returns generated for the fourth quarter of FY18 in the above table. We have a reporting policy under which we report, returns generated *during the quarter* only when the performance is adverse i.e. negative **or** lower than Nifty/Sensex. This is to ensure that bad news reaches clients as early as possible. Else because of short term nature of quarterly returns, we do not report these numbers when the results are favourable. We report just *yearly returns and returns since inception* on regular basis. For FY18 as a whole we have performed very well.

Second, because we report IRRs, which is by far the best measure of reporting, the numbers tend to be overblown on a quarterly basis. For example during the quarter portfolio value has decreased by 14.3% but in IRR terms it would be 47.0%. Hence it's better to concentrate on long term returns.

Third, we have significantly liquidated our portfolio over last 2 years, hence returns generated on the current portfolio during the quarter has very limited impact on our long term performance.

At this juncture given the significant liquidation of the portfolio over last 2 years, it's appropriate to look back granularly in our returns and see what we have achieved and where are the possibilities of improvements. So here are the details.

	IRR Generated	Cash Multiple(1)	Holding Period(Years)(2)
Stock 1 (Exited)	48.3%	2.3x	2.1
Stock 2 (Exited)	97.4%	2.4x	1.3
Stock 3 (Exited)	48.9%	3.1x	2.0
Stock 4 (Exited)	166.4%	1.7x	0.5

Stock 5 (Still Holding)	60.5%	4.1x	3.0
Stock 6 (Exited)	126.8%	2.7x	1.2
Stock 7 (Exited)	39.2%	1.5x	1.2
Stock 8 (Still Holding)	6.0%	1.1x	2.1
Stock 9 (Exited)	220.8%	3.4x	1.1

(1) Total realizations or current market value divided by total cost of investment (2) Calculated reversely from IRR and cash multiple

Now there are many ways to look and analyse these numbers. I will try to cover the ways I think are the most relevant. But more suggestions are always welcome.

First and most important aspect is to see what portion of the long term returns generated are attributable to our capabilities and what portion is attributable to luck. *What returns we generate is one thing and what returns we deserve is another*. Over your life, you may or may not get what you wish/want but there is a very high chance that you will get only what you deserve. Hence it's important to know what you deserve and work relentlessly to improve that. As per my conservative assessment, I can say with reasonable confidence that, we deserved at least around 1.5x to 2.0x return in our overall portfolio over maximum of 5 years holding period. Out of the rest what is luck and what is capability is hard to judge and we will never know. It's more of an art than science to dissect returns like that. Hence it's prudent to be conservative and also prudent to work in a broad range.

Second important aspect is to see protection of capital in our stock holdings because that's what we aim for when we make a decision to buy. It's good to see that we have neither lost money nor deserved to lose money in 8 of our 9 stock holdings. In one of the stock (stock 7), I believe we should have lost money but for the bullish sentiment, we ended up with a decent return. But nevertheless it was a mistake to buy this stock.

Thirdly you must have noticed that our holding period is considerably shorter than the stated policy of 3-5 years. This is just an unintended outcome probably of the bull market. Whenever we buy something, we should be mentally prepared to hold it for at least 5 years. Market can provide us opportunity to exit early and we will capitalise on it whenever such an opportunity is available. But that's neither we should nor we have, planned/aimed for.

Fourthly, it's also important for you to know that none of our stocks at the time we bought it, was in the holdings of well-known public market investors. We have stayed away from the widely accepted method of buying a stock just because a well-known investor has bought it. It does not mean that we are not open to buy those stocks but it just means that we have a very different mindset and way of buying stocks. Going forward as it is now, we will keep evaluating all those stocks and will buy it only if our independent thinking reaches to a buy conclusion. Being this way, I believe is more sustainable. We should be ready to eat food given by others (avoid egos always), only if a) we are hungry b) we are sure it's healthy and c) we are sure that our body is suitable to digest the kind of food being served. Else it's better to cook our own food.

Lastly, as apparent from the above table, we have invested in a very limited number of stocks over a period of time. It's mainly because of the two reasons a) broader market conditions b) time (8-10 hours per working day) and intellectual limitations on capabilities of the promoters. While we cannot control the broader market situation, the impact of time and intellectual capabilities of promoters should fade away with the passage of time and continuous effort to accumulate knowledge of more and more businesses and companies. In this aspect, I am very sure that the next five years will be significantly different than the last 5 years if headwinds from worsening broader market conditions do not increase. After all, we will buy a stock only if we see reasonable probability of capital protection else we will have no option but to wait. And wait we will as we have been since last 2 years.

That’s it for this quarter from my side. Please feel free to get in touch with me if you have any feedback/queries on investment performance.