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investing ON THE go

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[INTRODUCTION]

Staci West (SW): Welcome back to the Investing on the go podcast brought to you by FundCalibre. India's long-term growth story is well known, but finding the companies capable of capturing it requires much deeper research. This episode explores what quality really means and how an extensive analyst team can uncover opportunities across the region.

Joss Murphy (JM): I'm Joss Murphy, today I've been joined by Ajay, manager of the UTI India Dynamic Equity fund. How you are Ajay?

Ajay Tyagi (AT): I'm good Joss, thank you for having me here.

[INTERVIEW]

JM: Well, great to have you here. Let's kick things off, shall we? Let's start really simply: Why India? We've spoken before about India's demographics, it's growing middle class and the long-term economic story. But for an investor looking around the world today, what makes the Indian equity market particularly interesting?

AT: We are presently living in uncertain times. I would say pretty much every morning we wake up to see what's happening, what's the president of the United States up to, you know, is there something which has completely changed the equation once again? So quite frankly we are living in, you know, a world which is pretty much living by the day. Now, in this entire framework, the Indian economy, which is predominantly driven by domestic consumption, is still relatively insulated.

So the economy is not dependent on whether there are tariffs being put on exports into the US. It's not dependent as much on what's happening on the AI front. Is the AI bubble getting pricked or are there more legs to the AI rally? This is an economy which, by the way, has always been over the last 30 years driven by domestic consumption, and that story hasn't changed.

It's all about billion and a half people, a young population which is hungry for consuming goods and services, and the improving per capita income is just enabling them to consume more and more. So yeah, to that extent, I would say that's something which hasn't changed for India, and that's going to be the very predictable India growth story into the next decade as well.

JM: Certainly some interesting points there. The fund is described as having a quality growth approach, build around quality growth and valuation. Those are three words that probably every fund manager would happily put on a PowerPoint slide. So what do they actually mean to you? What does a company need to do to demonstrate before you'd seriously consider owning them?

AT: Well, once again, you're absolutely right. I haven't heard any portfolio manager talk about having a portfolio of poor quality companies. Everybody feels that they have the best portfolio in terms of quality, but I would say you have to very objectively define quality. And for us, the objective definition is what's the business delivering in terms of its capital efficiency, by which I mean metrics like return on capital employed or return on equity. Secondly, is the business able to fund its future growth using its own internally generated cash flows, or is it really dependent on external sources of funding, which could be either equity or debt or a combination of the two? That's again, a very sure sign of trying to see whether the business has really those inherent characteristics to have its destiny under control.

Otherwise, if you are really dependent on external sources of funding, you will be, in a way, dependent and vulnerable to the economic environment around you. So I would say these are two very, very reassuring metrics for us. And, you know, you made a very good point earlier on. Nobody says that we have a portfolio of poor quality companies, but the best way to measure that is to see the fund characteristics in terms of return on capital employed, in terms of debt to equity rate, in terms of margin profile and so on. If you compare different funds on these metrics, I would say it will become very evident about the quality characteristics that, you know, the fund is holding.

JM: You have an enormous research resource behind you. How does that actually work? Can you take us behind the scenes a little bit? I know just for the listeners here that AJ's just flown over from India. So can you take us back home or what kind of resource you guys have?

AT: So I'll just dial back a bit. UTI is the oldest asset manager in the country. We started our existence in 1964, so we've been around now for more than 60 years. And being the oldest also means that we've built a very, very strong research capability through all of these last six decades. We also have one of the most experienced research team within India.

So we have a 18 strong member research team and these research analysts basically would be covering a couple of sectors and about 30 to 40 companies each. Our overall research universe is more than 450 stocks. So you can imagine, for most people looking at India from outside of India, they would have 50, 70, 100 stocks under coverage. We have 450 stocks, 18 analysts, eight very, very experienced portfolio managers.

So this is possibly, I would say in terms of team capabilities, this is as good as it can ever get. Now, in terms of how does this entirely function, I would say that the job given to our research analysts is to basically go deep into their sector, understand the nuances of the sector, and then help each portfolio manager in turn understand the entire sectoral landscape, as well as understand, you know, how different companies within each sector are really positioned. So I would say while the portfolio managers have the absolute freedom to construct their own portfolios, but they are being equally fed in by the research analyst in terms of understanding the landscape and therefore reducing the blind spots in the understanding of those portfolio managers.

JM: I've noticed that from speaking to you in the past, that meeting company management is an important part of your process, but presumably every CEO thinks their company has fantastic prospects. So how much can you really learn from meeting management?

AT: I think that's a great question. I would say I partly answered this question when we were talking about quality attributes of a company. So, we always look at historical data in terms of how every business has delivered in terms of some of the quality characteristics that are very dear to us. And then while, you know, history tells us how company has behaved through different economic cycles, meeting managements tell us whether they are changing the narrative or they are sticking to the narrative which they told us the last time we met them or two years back when we met them and so on. So I think what we look forward to in such kind of meetings is that, is the management continuing with their philosophy, which they spoke to us last time or the last time and so on. And secondly, are they looking at any adjacencies to add to their growth profile. So that's what we typically look at.

JM: So Ajay, you can invest across the market cap spectrum, although large-cap typically make up the majority of the portfolio. Does the process change as you move down the market cap scale? And is there potentially a bigger research advantage in smaller companies where there might be fewer analysts scrutinising every set of results?

AT: So I'll take the second part of your question first. Absolutely, yes. I think it's only obvious that having deep research capabilities does help us in terms of discovering these smaller gems. Obviously, these smaller gems become much more evident when they gain size and scale and when they become part of the widely tracked benchmarks. But in their very, very early years, these are businesses which people would not bother to track. But with an 18 member strong research team with around 450 companies under coverage, it obviously gives us an advantage to catch some of these businesses very, very early.

The first part of the question was, does anything change in terms of our philosophy? I would say no. We would use the same lens to evaluate the smaller companies, just like we're evaluating the longer companies. We don't want to give them a loose rope in terms of the economic characteristics that we desire from businesses that we wish to own. So, so that doesn't change. Ability to generate strong cash flows, ability to show capital efficiency right at the early stage of the lifecycle of a company is something we would still hold very dear in our process.

JM: And are there one or two industries or sectors where the combination of long-term growth, competitive advantage and valuation are particularly attractive in India at the moment?

AT: That's an interesting one. I would say yes. What looks very interesting to us at this juncture are, the healthcare sector and the overall consumption sector. Let me talk about healthcare a bit. This is a sector where, with improving per capita income and disposable income, we are seeing and witnessing that households are spending more and more towards, their healthcare expenditures. So India is an out-of-pocket market, unlike the UK and some of the other countries, we don't have a very strong medical aid system, so there is no NHS equivalent in India. There are, of course, primary hospitals, but then most people for their medical expenses have to go to private hospitals and pay out of pocket. Now, there are two trends which have emerged in the last 10 years.

One is that, with the increasing penetration of medical insurance, households have been enabled to spend more. And of course, with rising per capita income, people are getting more and more conscious about their wellbeing. So both these trends put together put India into a very high growth trajectory in terms of the healthcare industry. The other one is consumption, and I think this one is completely linked to the disposable

income and the growth in disposable income. And I think this has been one of the strongest pillars for India's growth over the last two or three decades. If I talk about numbers, India still is about $3,000 per capita income. Forget the developed world, even when you talk about emerging markets like Russia, China, Brazil, South Africa, all of these countries are between $10,000 to $15,000 per capita income. So, you know, while India has already become large in terms of its absolute size, but in terms of per capita income spends, it's still down there at the bottom of the pyramid, which means we have billions of people who are still hungry to try out different products and services. So that pattern of consumption will continue, and that's what makes it a very, very interesting industry at this juncture.

JM: Fascinating. I'm surprised that per capita income's that low. So a lot more growth to come. If you, just to delve into the process again a bit more, if you find a company with fantastic management, strong competitive advantages, and years of growth ahead of it, at what point does valuation simply become too expensive? And have there been businesses you've loved operationally but couldn't bring yourself to earn because of the price?

AT: That's an interesting one. I would say this happens to us very often, quality and growth doesn't come cheap, you're absolutely right. In fact, you know, quality and growth, if it happens together in any company, such companies typically would trade at very, very high valuation. So, you know, our job, and we keep reminding ourselves about this, is our job, first of all, is to find great businesses which can compound economic value. And as that economic value compounds, it does get translated into increase in market value of businesses. So the entire energy that we focus on is finding, such kind of high quality, high growth businesses.

Look, to our mind, valuation is the easiest problem to solve. I haven't known of any company which, despite being a darling on stock markets, doesn't go through disappointing quarters. And when I say disappointing quarters, such kind of high growth companies can get corrected 20-30% in no time. If you've done the homework well, if you've found out a great company, you just wait for such instances where, you know, perhaps one bad quarterly print can lead to massive correction in stock prices and you go all in at these stages.

So I would say the more difficult part of our job is to find great businesses. The not so difficult part is valuations. If you have that discipline and if you're really in for the long run, the markets give you know, I would say a lot of such kind of opportunities to solve for the valuation problem.

JM: And finally, Ajay, when you speak to investors here in the UK or elsewhere overseas, what do you think we tend to get wrong about India? Is there something that looks obvious from London, but looks completely different when you're actually meeting these Indian companies, consumers, and management teams every day?

AT: I would say the one thing which I've been hearing not just off late, but for the last couple of decades is the fact that there's a lot of concern and anxiety amongst global investors about India's R&D spend, India's technology spend, India missing the technology wave and so on. I heard that, 20 years back when packet software was coming in. I heard that 10 years back when cloud computing was the in thing. I heard once again 10 years back when electric cars was one of those great opportunities. And of late, I've been hearing this because India doesn't seem to be having, you know, any AI play, whether it's in terms of the LLMs or it's in terms of the infrastructure builders of today. So I think a lot of global investors always think about India not catching on to the latest technology wave.

But what I can tell you from my own experience, and of course meeting corporates, is that India is very good at adapting to the latest technology. So cloud computing came in, and I would say that most large corporates in India have started using cloud computing to improve their productivity. India was never there when the internet technologies were being evolved, but there have been so many successful businesses in the last 10 years, which have been built around, the internet technologies. And I would say AI wave would be pretty much the same.

So, you know, India is very good at adapting to new technology to eke out productivity gains out of such kind of technology waves. India may not be the innovator, but I think Indian companies by far do know how to take advantage of the latest technological innovations to actually improve their own productivity.

JM: Fascinating, Ajay. Thank you so much for coming on today. I really appreciate your time.

AT: Pleasure.

SW: UTI India Dynamic Equity invests across the market-cap spectrum, focusing on companies with a high potential for significant market outperformance. To learn more about the UTI India Dynamic Equity fund, please visit fundcalibre.com and don't forget to subscribe to the Investing on the go podcast, available wherever you get your podcasts.