

Letter One – Ground Rules

Dear Partners,

Thank you for choosing to invest with us in the Bay Capital India First UCITS. This is our first letter, and we would like to use it for something more important than just a launch announcement or a market outlook.

This letter is about *ground rules* and *alignment*.

Decades ago, before Warren Buffett became synonymous with Berkshire Hathaway, he gathered his first seven partners for dinner at the Omaha Club. The legal documents were almost an afterthought. What he really cared about was making sure his partners understood *how* he would invest, *what* they should expect, and *how* to judge him over time. He called these his “ground rules” and revisited them regularly through his partnership letters.

This letter is our attempt to do the same for our UCITS fund.

In our experience, the success of any investment franchise rests on one simple but demanding foundation: the expectations of the investor and the behaviour of the fund manager must be aligned – not just in good years, but through full market cycles.

What follows is a clear articulation of:

- *Our investment objective and philosophy*
- *The process we follow – what to buy, at what price, and in what size*
- *How we construct and risk-manage the portfolio*
- *The ground rules for performance, time horizon, and how to judge us*

Our hope is that, after reading this, you will either feel deeply aligned with how we operate or realise that this is not right for you. Both outcomes are perfectly acceptable; misalignment is not.

Our Objective: Compounding with Quality, Not Chasing Headlines

The objective of the Bay Capital India First UCITS is straightforward to state but hard to execute:

To compound capital over long periods of time by owning a concentrated portfolio of high-quality Indian businesses, and to outperform broad Indian equity indices over rolling 3-year and longer periods, after fees.

There are three deliberate choices embedded here:

- **We are long-term.** Our focus is measured in *years and decades*, not quarters. Short-term price moves and calendar-year rankings will be noisy and often uncomfortable.

- **We define quality in business terms, not marketing terms.** We focus on franchises with enduring competitive advantages, strong cultures, and the ability to reinvest capital at attractive rates.
- **We are benchmark-aware, not benchmark-driven.** We want to do materially better than Indian equities over time, but we will not run the portfolio to look like an index or to minimise short-term tracking error.

We cannot – and will not – guarantee any rate of return. What we can commit to is a disciplined, transparent process applied consistently over time, with our own capital invested alongside yours.

Investment Philosophy: High-Quality Franchises, Infinite Game

Our philosophy has evolved through multiple market cycles, but its core has remained remarkably stable.

Ownership mindset

We do not approach listed equities as “tickers” to be traded, but as fractional ownership stakes in real businesses. What excites us most is not the share price but the underlying business model: how it makes money, why customers keep coming back, how culture supports execution over decades.

Long-term value, in our view, accrues to franchises with enduring competitive advantages whose cultures allow their “moats” to deepen over time. These are the businesses we want to partner with.

Narrow universe: we avoid more than 90% of the market

Because the quality bar is high, very few companies qualify.

- Out of over 7,000 listed companies in India, we focus on a much narrower universe of high-ROCE, high-growth franchises.
- We deliberately avoid businesses with weak balance sheets, poor capital allocation, questionable governance, or structurally low returns on capital.
- We also avoid “fashionable” themes where the primary attraction is recent share price performance rather than economics.

In practice, this means we are comfortable ignoring most of what makes headlines. We would rather underperform an index temporarily than dilute the quality of the portfolio for a short-term “trade.”

Leadership businesses in their categories

Within our filtered universe, we strongly prefer leadership businesses – companies that are number one or among the clear leaders in their niche. There are several India-specific reasons for this:

- Achieving leadership in India is unusually difficult given the country’s complexity; sustaining it is even harder.
- Once established, leaders benefit from strong brands, superior distribution, better data on consumers, and the ability to attract and retain the best talent.

- Scale and balance sheet strength allow them to invest through downturns, gaining share when weaker competitors pull back.

Leadership tends to translate into longevity of earnings, which is essential for compounding.

The infinite game

We see long-term investing as an infinite game. The goal is not to “win” a single year or cycle, but to stay in the game – rational, liquid, and invested – across many cycles.

Given the choice between:

- A *great* outcome in a very narrow set of scenarios, and
- A *good* outcome across a wide range of scenarios,

We will choose the latter. Our north star is longevity and resilience over maximising any single period’s return.

Our Process: What to Buy, At What Price, and How Much

Our day-to-day investing work is organised around three questions:

1. **What to buy?**
2. **At what price?**
3. **How much to buy?**

These are the only variables we truly control when we initiate an investment.

What to Buy – Historical ROCE and Leadership

- **Filtering by long-term ROCE** – To separate the exceptional from the ordinary, we use historical Return on Capital Employed (ROCE) as a primary quantitative filter. ROCE, defined as EBIT divided by net operating assets, combines the income statement and balance sheet to reflect the true economics of a business.
 - Sustaining ROCEs above ~20% over a decade is extremely rare in any market.
 - When a company achieves this, it usually reflects a strong moat, good capital allocation, prudent risk-taking, and a management team that understands its craft.

From the 7,000+ listed companies, this filter leaves us with a much smaller investable universe. We then remove any franchise with a history of poor governance or capital allocation. Only after this do we spend significant time on deep, fundamental work.

For newer “asset-light” or digital businesses, we complement reported ROCE with incremental ROCE and unit economics to avoid penalising early-stage investment in capabilities.

- **Leadership and durability** – From this refined universe, we focus on leadership franchises for the reasons outlined earlier: durability, bargaining power, culture, and balance sheet strength. Together,

long-term ROCE and demonstrated leadership tilt the odds in our favour before we begin detailed valuation work.

At What Price – Margin of Safety and Expected IRR

“Margin of safety” is, to us, the most important concept in investing. A wonderful business bought at the wrong price can still be a poor investment. Our valuation discipline has three components:

- **Intrinsic value analysis** – We use multiple valuation approaches to estimate a conservative range of intrinsic value. We prefer to buy when a business trades meaningfully below its own long-term valuation bands (often framed as below one standard deviation from its long-term average multiples).
- **Scenario analysis and expected IRR** – For each investment, we run bear, base, and bull scenarios, focusing on revenue growth, margins, reinvestment rates, and capital intensity. We look for opportunities where the *expected* internal rate of return (IRR) over the long term exceeds 20%, without requiring heroic assumptions.
- **Patience in execution** – We are not “trigger happy.” Many ideas live on our watchlist for months or even years before price and fundamentals intersect at an attractive point. Cash is typically a residual of our opportunity set, not a top-down call.

Price discipline is one of the few levers entirely under our control; we intend to use it.

How Much to Buy – Position Sizing and Risk Management

Position sizing is where philosophy meets risk management.

- **Starting sizes.** We typically initiate positions at 1–3% of the portfolio.
- **Maximum positions.** Under normal circumstances, we do not deploy more than 8% of capital into any single name at cost, though successful holdings may grow above that level over time.
- **Number of holdings.** We expect to own roughly 25–50 franchises in the UCITS fund – concentrated enough for each holding to matter, diversified enough that no single mistake can define the outcome.

The aim is clear: **good outcomes across many scenarios**, rather than spectacular outcomes in a narrow one. We want the destiny of the fund to be defined by the collective performance of the portfolio, not by one lucky or unlucky decision.

Portfolio Construction in a UCITS Framework

The UCITS structure imposes sensible constraints around diversification and liquidity. We embrace these as features, not bugs.

Within this framework, we construct the portfolio as follows:

- **Concentrated but diversified.** Around 25 – 50 holdings, each a high-conviction idea, with position sizes scaled by conviction, quality, and liquidity.
- **High liquidity.** We avoid structurally illiquid names; positions are sized such that the portfolio can honour typical UCITS liquidity requirements without forced selling.
- **Sector balance.** We do not run top-down sector views, but we do monitor aggregate exposures to avoid over-concentration in any single theme or risk factor.
- **No macro or timing calls.** We do not take deliberate currency or interest-rate bets, nor do we seek to time the market using cash levels. Our edge, if any, comes from bottom-up business selection, not macro forecasting.

We measure risk primarily as the possibility of permanent loss of capital, not as deviation from an index on a monthly sheet. Volatility is a feature of equity markets; our job is to make sure it works in your favour over time, not against you.

“On the Ground” Research and the Devil’s Advocate

Our process is research-heavy and field-driven. We spend substantial time understanding companies through management meetings, channel checks, customer and competitor conversations, plant and branch visits, and data work.

For every portfolio (or potential) holding, one team member plays the role of “Devil’s Advocate” – their explicit job is to stress-test the thesis, surface risks, and challenge consensus thinking internally.

This structure forces us to continuously revisit our assumptions, particularly on downside scenarios and the risk of permanent capital loss.

Performance Ground Rules: How to Judge Us

This may be the most important section of the letter.

1. No guarantees – only process

We cannot promise any rate of return. Markets are inherently uncertain, and there will be periods – sometimes extended – where prices diverge from underlying business value. What we can promise is that:

- Our investments will be chosen for value, quality, and durability, not popularity.
- We will do our utmost to minimise the risk of permanent capital loss via a margin of safety, robust balance sheets, and diversification across high-quality businesses.
- Our own capital will be meaningfully invested in the Fund alongside yours, aligning our interests closely.

2. Time horizon: Rolling 3–5 years, not single quarters or years

We believe three years is the absolute minimum period over which our approach can be judged, and five years is preferable.

There will be:

- Quarters – and even full years – of underperformance versus the index, especially in speculative bull phases where lower-quality businesses lead.
- Periods when our style (quality, price discipline, low turnover) is unfashionable.
- Phases where the Indian market itself goes through sharp corrections or long, dull sideways moves.

If your reference frame is 3–6 months, this fund will likely frustrate you. If your frame is 3–5+ years, and you care about capital compounding and downside protection, then our approach should be well aligned with your objectives.

3. *Yardstick: Broad Indian equity indices over full cycles*

Whether we have done a good or poor job should not be judged by whether the Fund is up or down in any given year, but by how it performs relative to broad Indian equity indices over rolling multi-year periods.

- If we outperform meaningfully over 3–5 year rolling windows, especially with a focus on quality and risk management, we would consider that a good outcome.
- If, over such periods, we consistently lag Indian equities despite adhering to our philosophy and process, you should question whether we deserve your capital.

4. *What we will not do*

To avoid confusion, it is equally important to clarify what we will not do:

- We will not attempt to predict short-term moves in the market, interest rates, currencies, or elections.
- We will not trade actively to manufacture short-term performance at the cost of long-term compounding.
- We will not chase fads merely because they are working in the market if they do not meet our quality and valuation thresholds.

There will undoubtedly be tempting opportunities to deviate from this discipline. Our commitment is that we will resist them.

Communication: What to Expect from Our Letters

Just as Buffett used his partnership letters to reinforce his ground rules and teach his partners how he thought about investing, we intend to use these letters to:

- Reiterate and refine our investment philosophy and process.
- Update you on portfolio activity – new investments, exits, and major changes in weights – with the appropriate level of detail.

- Share case studies from the portfolio that illuminate how we think about business quality, valuation, and risk.
- Provide an honest assessment of our performance versus our stated objectives and benchmarks, with an emphasis on rolling multi-year periods.

We will not provide running commentary on every market move or attempt to explain short-term price noise with grand narratives. Where we are unsure, we will say so.

Closing Thoughts

Charlie Munger once said, “All I want to know is where I’m going to die, so I’ll never go there.” In investing, the equivalent is to identify the minefields – low-quality businesses, poor governance, over-optimistic valuations, and excessive concentration – and avoid them rigorously.

We are comfortable with errors of omission – the opportunities we miss because they do not meet our quality or price thresholds. We are *not* comfortable with errors of commission – investing your capital in businesses that are fundamentally weak, poorly governed, or egregiously overvalued.

If we can: one, consistently own high-quality, leadership franchises; two, maintain discipline on price and position size; three, stay invested through cycles without trying to outguess every macro datapoint, and four, keep our own behaviour rational when the world around us is anything but, then we believe we have a good chance of delivering satisfactory, and hopefully superior, compounding for you over the long run.

Thank you again for your trust at the very beginning of this journey. It is a responsibility we take seriously, as stewards of your capital.

We look forward to writing to you in the years ahead.

Warm regards,



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