# Piercing the Small/Midcap Investing Chakravyuh with Samit Vartak

**Nooresh Merani**: So Samit, great to have you here on the podcast. What we'll be discussing today is everything about you. And we'll be poking you on all the things you've done over the last 10 years. Congratulations on your PMS completing 10 years. So a good time to talk with you, because you'll have a lot more learnings to share. And we would love it to be a candid conversation. So don't be worried about whatever you want to talk about. So we'll start with. Let us know something about you, and how you got into the markets in the first place. Because you've had multiple areas of work before you got into the PMS side.

**Samit Vartak**: Yes. So, I think my path to the market is very different from most investors because I was an engineer. So, I grew up in a small village 100 kilometres north of Mumbai, and we are from a farming background. Most of our generation was into farming. I was the first one to even graduate. So, none of us had any idea about what the stock market was. I did my engineering. Fortunately, I was able to come to Bombay, which was in 1987, after my 10th standard. I did my college and then engineering in Mumbai. And around 1994, I think that I graduated. And I had no idea. My father used to tell me about Engineers, and maybe some Collectors, Doctors. So, I had a few careers in my mind about what I wanted to do. I had taken civil engineering. So, I thought, okay, it looks great because I can build buildings, some bridges and all of that. In the village, it was a very simple life from morning to evening.

Other than the school part, we used to attend, we mostly just played and had fun. We had a beach in our town. So we used to go to the beach, we used to climb trees, and play all sorts of games because everyone had time. So that was the fun part. And then when I came to Bombay, I took a while to adjust because I couldn't speak English.

I was sort of horrified when I had to converse with anyone. So the initial part was very difficult. And I thought everyone was so smart around me. How do I even survive in this kind of competition? Because everyone was doing classes, they were going to Agarwal's classes. And, yeah, it took me a while. Imagine that I was going for engineering, and then, until I completed my 11th, I had never even heard of something called an IIT.

And then I saw people preparing for IIT for years. That's how it was. It was completely just a random career with no real thought, something which I thought, okay, I'm good at maths, so, let me go into engineering. I chose civil engineering as it made sense, and got into that. So that's how I got into engineering. From campus, I got a job in Mahindra and Mahindra, and I did the job for two to three years.

And then, I wasn't sure. I didn't like that engineering part that much. So one of my classmates was appearing for GMAT and was applying to a few MBA colleges in the US. At that time, it used to be a very physical process of applying. You have to write a letter, and then the university will send you a form, and then you have to fill up the form. It was a long process. It used to take months to even get those forms. He applied to the top colleges and had a couple of forms left, which were reasonably-ranked MBA schools, like 15th or 20th, rank. He came to my hostel room. And he said, “Why don't you also think about applying?” I have a couple of extra forms. So that made sense because I didn't know what I was going to do anyway, and what's the harm in at least applying?

So then I quickly prepared for my GMAT. I gave my GMAT within a month and then applied to these two colleges. One was at Washington University in St. Louis, and the other one was at Ohio State University. And fortunately, both universities gave me admission, and one of the universities gave me a scholarship to come.

So that's how I went to the US in 1997. It was just pure luck. And ironically, my friend never ended up going to the US, which was like preparing for months or years. And that's how I went to the US. And then what happened was in 1997, there was the “dot com boom”, things were just hyped up. Then a lot of my classmates were basically doing investments in IPOs, on the side, and that's how I sort of got hooked up. There were a couple of IITians in our college, and they were really passionate about Wall Street. They used to just talk about all kinds of traders trading on Wall Street, and because I was hanging around with them, I got really fascinated with that.

And I said I should at least take classes on investment. So during my MBA, whatever courses I could take on investment, I took. Then when I completed my MBA in 1999, I wasn't sure what I wanted to do anyways. In 1999, the way was sort of turning around, things were coming down. And from a second-tier, 15th or 16th-ranked school, it wasn't that easy to get into the top-tier Wall Street firm.

So I took my first job, which was with PwC Consulting. Because of my engineering background, I took that job and fortunately for me, that gave me an opportunity to work with a lot of management because my role was to basically work with mostly manufacturing management and look at their activities and analyse what were the redundancies/ inefficiencies in the operations and recommend which are the best ways to cut cost, reduce those inefficiencies, and improve profitability, and then through that, thinking about growth. I worked with so many different management in different industries, from a dairy farm to auto ancillaries, to auto companies, to even logistical companies because of the eCommerce, which was developing.

So that was a really good experience because I could see from inside, how management thought, how companies worked at the ground level. In the meantime, I started investing in the market in 1999. 1999 was the worst time probably to come into the market because everything was just downhill. And I got my signing bonus. So, I said that now, I should start. So, I started investing and because the markets were coming down, of course, you would lose money. The kind of knowledge that I gained in the MBA, was completely inadequate. The initial phase was probably pure luck that I did well but then, things started just going downhill. And then you try to recover your losses. The US gives you so much money margin, that you can take leverage many many times. So, that's sort of a trap. It's just a trap to destroy your money much faster. So, that's what happened.

That had a big impact on me because whatever money I lost was massive money for my family back home. And I stopped investing for a couple of years. After that, I enrolled myself on the CFA program. I did the CFA and then started reading a lot about all kinds of investing styles - from Warren Buffett to technicals, to quant-based and all other kinds of investing. I had no idea what was the right thing as an initial investor, I think it's great to try different styles.

And then I restarted with a little more knowledge and with the CFA, I started investing in 2003 or 2004. Then I decided that this is what I really want to do full-time. And then my next step was to get more towards finance. So then I moved to Silicon Valley with Deloitte Financial Advisory and they were basically doing valuations for many companies out there. So, that was a little more relevant. Actually whatever knowledge I gained was really useful, because investments are all about understanding businesses and understanding valuation.

When I went to the US, there itself, I said with some experience, I would come back to India. So in 2006, we came back to India. I came in as an associate director with Ernst and Young Valuation practice in Mumbai. Then, at the first opportunity, I jumped into private equity, because at that time, there was a boom time and private equity was doing great. So, I joined and I took probably a 70% pay cut because that was my first real investment-related job. So I took that pay cut and joined. That was the real start of a full-time sort of investment. Until then, it was just a hobby on the part-time side. But then, when the 2008 crash started, I was very well prepared for that compared to the first crash when I was wiped out.

That's when slowly I realised that it's all about business. So, I spent from 2006 to 2012, meeting probably 400 companies during that time. That was my passion, meeting companies, understanding the businesses, putting myself in their shoes in terms of how you strategically plan your growth forward and trying to understand as much as possible. My reading also tilted more towards whatever helped me understand businesses, business models, and why some companies are doing this, versus their competition doing that. So for me, that became more interesting. And then, in 2012, I started SageOne, and the journey started. But that's a little bit longer. That was how I got into investments.

**Puneet Khurana**: So Samit, thanks a lot for that. I think in the initial part of the years, an individual decides what kind of investor he is going to be. And that's where the context which you have provided is actually very important for the next few questions, which are going to be on the investment side of things. But just to get the chronology a bit correct - So when did you start investing for the first time? that was in 1999, you did levered investing. Did I get that correct?

**Samit Vartak**: Initially, I started with pure investment. And, the first few months were great because the markets were just booming. But after the peak in 2000, it started going down. Once you start losing money, you try to recover. I used to invest in companies like Siebel, i2, Sienna, and Jupiter. And those corrected like 30% - 40% in a matter of a few months. And then you realise that it's so cheap. So you want to make up the money very quickly. Then you lever up. You want to buy more, and that's where I started levering or using the margin that the exchanges/ brokers used to provide.

**Puneet Khurana**: Okay, and one more thing which you said, which I captured was that in 2008 you were much better prepared for the investment world than you were in 1999. Can you go a bit more into detail about what you mean by that - when you say you were more prepared? Are you talking more from a capital perspective? Or were you waiting for the markets to do something? What do you mean by preparation in that sense of the word?

**Samit Vartak**: See, I think I learned a few things. There are a few mistakes that a starting investor makes. So one is, of course, you believe too much what other people are saying. So if there is a company and there are, say 20 analysts who are covering that company and all 20 are saying buy, you tend to believe that's the best buy that I'm going to do. So that was my first learning - if everyone is saying buy and everyone is already invested, that means generally it's not a great buy. So that was a mistake I used to make. I used to see which company has the most 'buy' and estimate that. Secondly, as the markets start falling, your instinct is to start buying because you think that it's available at 30% to 40% cheaper rate. That falling knife is something which I realised. Just because the price has fallen by 30% or 40%, doesn't mean it's cheap in value. After all, you have to evaluate the business much better.

The crisis started in January 2008 and then, Bank of America, Merrill Lynch, and Lehman Brothers, all of that started. And at that time, I thought that this is not something which is going to end very quickly. So even if the market prices were down by 20%, 30%, or 40% I never jumped to buy. I have held on to whatever cash I had. And of course, fortune or luck was also a factor. When I came to India, I set a little bit into cash because I wasn't aware of a lot of companies in India. That's because I never tracked the Indian market well. So I took my time to deploy. When things started going down, fortunately, I had 30%-40% of the cash. And, like previously, I didn't start catching the falling knife. So that was a big difference. And then I started understanding the businesses, understanding the environment, how the financial crisis will have an impact on each of the companies, and which companies will probably be able to survive. So I was much more rational rather than listening to others to make my decisions.

**Nooresh Merani**: Interesting. So in 2008, you did not lever up? How did you end up in 2012? You've been from business to valuations to private equity? How did you get into SageOne? And you can tell us the start and how did this happen?

**Samit Vartak**: My passion was always to do something on my own. I had done the job for many years, and with the job, after all, you're not free to do what you want to do. You are guided by the company processes, maybe the company philosophy, style, and all of that. And, since I had never worked on the sell side or buy side before, I had no baggage of any style. It was all experiments on my own money and on me. Over the years, I had fine-tuned what really works for me by reducing volatility with not too many big drawdowns and betting on companies. So I never ever try to benchmark myself against indices. As an independent investor and a small investor, I had to compound my money. It's not just about beating the benchmark, but I had to compound my money. So I always targeted every three to four years, I need to sort of double my wealth. That was something that I targeted for myself.

And then I started thinking, is it something that I can replicate for the clients? Fortunately, during that time, from 2000, and especially after 2009, I started focusing completely on the listed market because I was on the private equity side, I used to meet a lot of promoters, and a couple of us used to discuss investments. And then I started informally advising them about what kind of stocks to invest in. A couple of stocks at that time, I remember I used to be very gung ho about Bajaj Finance and Kaveri. Those were my top conviction at that time. I used to tell them that this is what is happening in the company, and they need to invest. So, they invested. Whatever tiny money they had, they invested. So 2009 to 2011 was anyways a great period, but 2012 was a bad period. But because I was invested in Bajaj Finance, Kaveri, PI industries, those kinds of companies, they kept on doing pretty well. And because of that experience, I got much more confidence that even in a not-so-good cycle, if I pick the right companies, I can do pretty well.

By that time I had enough comfort because of corporate governance issues in India, and then private equity also gave me the opportunity to do due diligence on companies. So, I got much in-depth knowledge about what managements do, and how they sort of fudge the P&L, and balance sheet. I worked with auditors also because they also were part of the due diligence. So, that gave me a first-hand experience of what things can go or which can be tweaked. In 2012 again, I had no one else other than those couple of promoters who joined me with one crore each. I didn't have my own capital, nor did I have a network of clients, but I thought this is what I want to do. This is my passion and my style, which I had developed on my own, and I thought it worked pretty well. And I never tried to even get a job on the listed side anywhere. So I said, even if I don't make money, this is my passion and I'm right away going to jump into it.

**Puneet Khurana**: Samit, before we go to the investment side of things and go more into your philosophy of investments I wanted to dwell a bit on a couple of decisions which you have mentioned in your life, even though it was a passing mention but they are very difficult decisions, right? So the first decision, which seems to be the game changer for you is your decision to move from being the associated director with the E&Y to the private equity by taking a 70% cut. Not an easy decision. I've been there, and I know that it's not an easy decision by any stretch of the imagination. And many people get inspired by these kinds of stories, but they don't get the underlying environment or ecosystem that helped them take that decision. I want to go a bit more into that. Because I have heard stories where people want to take those decisions and when they tell me their circumstances, I tell them, boss, I would not have taken that decision if I were you. Right? So, the ecosystem plays a good role. What were your circumstances at a personal level, when you made that shift? Were you married? Did you have any family members dependent on you? Just give us the context of that decision.

**Samit Vartak**: You're right. I think it's one of the most difficult decisions, especially when you have a monthly check coming in and are sort of saying no to that. So I was married and had two kids. At that time, I was the only one working. So the family was completely dependent on that. But even with that sort of 70% cut in pay, the money that I was making was good enough for me to actually survive. When we came in, the first thing we did was, we bought a house. We had to take maybe 50% kind of a loan on that house, but the money was enough to pay and survive reasonably well with a decent lifestyle. So, that was something which definitely helped. But after sort of having worked for almost 13 or 14 years by then, the salary that I was making was very very small compared to my kind of experience with, coming from the US and having worked with the Big Four. Most comparable, sort of experienced professionals was making 3X the money that I was making. But still, it was enough. Our requirements were not much. We just bought a two-bedroom flat in Prabhadevi. And that too, a very old flat, we just renovated that. So it was also a very small investment that we did. So because of my farming background through which I came in, my requirements were very little. And so I was able to take the decision much more comfortably.

**Nooresh Merani**: So dude, two decisions- so you came back from the US to India. Then in India, took a 70% cut. Didn't people ask you “Are you mad?” (slight laugh)

**Samit Vartak**: No, I didn't tell people. Fortunately, my family was always supportive, mainly my wife. So she knew how passionate I was about this, and this is what I wanted to do in my life. So I thought if my passion is clear, and of course, you yourself have to believe that you're good at it, and you will be able to sort of deliver on this, it's just a matter of time before you make up the money. So, it's always easy to say that, follow your passion and the money will follow. But, for me to make real money was quite a long. So I took this jump in 2007 and I did not make much money until probably 2018 or 2019. I started SageOne but until that point, you know, there's a lot of investment that you need to make and at your level, you don't make much of a salary. So, it took me a good 12 years to really start making money and whatever money I was making was only on the investment side. But my starting capital was very small. After coming back to India, having put up the equity and buying into the house, you don't really make much. Even if you make, say 10x money on your capital, it's not going to be that big when you're starting capital itself is small. So, you need to first also earn money, right? And that earning money started way late in the 2018 or 2019 period. So, yes, if you have the passion, follow your passion and the money will follow. But remember, it may follow after 10 or 12 years. (slight laugh)

**Puneet Khurana**: Actually, that brings me to the second part of the question in terms of the game-changing decisions. Going back, it sounds very obvious that okay, in 2012 starting, SageOne was a good decision if you start your measurement from today. But as you rightly said, at that point in time, first of all, how was it possible for you? Because in 2012, you said you had no capital? Your clients were only two as you rightly said, right? Two crores of starting capital? How was it even possible for you to start? Because there are initial net worth requirements to start a PMS. How did you go around making that decision or coming up with a PMS and not going the normal route of let's say, an advisory or a brokerage or something like that?

**Samit Vartak**: No, initially, I started with advisory. In 2012, there was actually no advisory license. You could just do advisory. The advisory license started in, I think they came out with the regulation in January 2013. And it takes some time for you to register, right? So I said that I could work from home. I don't really have many fixed costs. I was just alone, I didn't have a team or anyone. So I said, I will do exactly what I do for myself. So what I did was, for my clients, I didn't just advise them, I also made them open an account with one of the brokers, where even my account was. Then I took the POA to do the execution on their basis. And then with my account, even their execution used to happen. That's how I started with the really minimal cost at my end. And then once I got bigger enough, I went for the PMS and went through the process. But initially, when I started, I said, for me, it's more important that I keep my costs as low as possible. Because I didn't have the sort of net worth required for a PMS licence. So it took me a while to even get started.

**Puneet Khurana**: Okay, and just to get the chronology in place, when is it that you started your PMS or you took the PMS licence in the more official sense?

**Samit Vartak**: So I took the PMS licence in 2016. So until then, when the advisory licence came, I took the investment advisory licence at that time. There were also issues with the PMS licence then. When we were speaking with lawyers, at that time, what used to happen was in the PMS, you don't get a contract note, because it's a pooled account. So, the buying and selling happen at the PMS level and not at the client level. So, there were taxation issues. When the Modi government came in, Arun Jaitley clarified in the budget regarding this that it will be up to the investor to classify it as an investment or as a trade. So, you can declare, and then you stick with it. The officer cannot challenge you. And when that clarity came in, that's when I said okay, it makes sense to apply for the PMS license. Until then, PMS had a lot of issues with investment. The IT guys kept coming after you. And that's why we applied in 2016.

**Puneet Khurana:** Okay, so now you have mentioned styles when it comes to listed markets, which is not there in private equity. Let's talk about styles. In many of your interviews, you have talked about business quality and then we'll come to the four pillars on which you have named your company also 'SAGE'. But you also mentioned in the initial questions that you experimented with a lot of things, right? You experimented with Quant, Warren Buffett, technicals, and many things. Just take us through the journey before you reached your current situation, or even in 2012 when you started Sage. I'm guessing that when you started Sage, you had much more clarity on your style. But let you take us through the journey of reaching that style. How did you reach that style? What did you experiment with? What did you lose? What did you learn and so on and so forth?

**Samit Vartak**: So see, in 2001 and onwards, my real education started. Then I started reading a lot of books, like Warren Buffett, which spoke about fundamentals and all of that, which made sense but that also required that you spend a lot of time really going in-depth into companies. And doing that as a sole investor with a full-time job in the US, which needs you to work 12 to 16 hours a day, wasn't practical enough for me. So during that time, I also came across this CANSLIM style. I think Bill O'Neil stated that. There is a newspaper, *Investors Business Daily*, which does a lot of fundamental ranking for you. So fundamental momentum, even within an industry does the ranking for you, and it gives you a score. So with that at least I got some shortlist of companies to look deeper into. It wasn't just in the US. So that made a lot of sense to me that having a combination of technical as well as fundamental and then momentum wise, where earnings, it's not just the price momentum, but also the earnings momentum and that too relative momentum against the industry. So at least that gave me a starting point to look into because otherwise, there are 1000s of companies that you really look into.

So, I started focusing on the top 25-30 companies within which I looked at companies which made sense to me, the industries I like and then where there was growth. So the focus was completely on fundamental momentum and earnings growth. And maybe it's pure luck that the time was really good. From 2003 to 2007, everything was going well. But because I did that, I got the confidence that this works. So I continued doing that without really I mean, I couldn't visit the company or talk to the management just on a very passive level, just looked at the financial statements and how the earnings were coming through, and it worked pretty well for me. And so when I came back to India, that kind of data wasn't available for the Indian markets. And that's when I said, I wasn't sure what to invest in India and hence whatever money I had, I kept it in cash.

In 2008, I invested in a house in Andheri and we sold that. So I got a few lakhs of profit. That was in early 2008. And if I was like my previous self in 1999, I would have right away jumped into catching all these falling knives around me. But fortunately, I kept that cash for a long period of time, because I wanted to get comfortable in terms of understanding these businesses. But the bottom line for me was always earnings momentum, where are the relative outperformance and all of that. Private equity gave me that opportunity, at least, to go around and meet companies. At least I had a framework for looking at the companies, which took its own time. And after 2008 or 2009 anyway, the markets had fallen so much that I knew companies like Gujarat Fluoro which were available at one time EV/EBITDA. There were so many companies available at like two times or three times EV/EBITDA. So then, if you have the money, and you invest in any of those companies, you will do pretty much fine.

So again, there was also a lot of luck involved, because of my initial phase of experience, I sat on cash, and by the time markets collapsed I had enough cash to invest and that did pretty well. And then as I got more and more exposure to meeting companies and then actually evaluating these companies, I ended up at least with the right framework, picking the right set of companies. All of these companies whether it's Bajaj Finance, Kaveri, or PI, were really really cheap even in 2011 or 2012. They never really got rerated. Their earnings momentum was so strong, that even if you don't get rerating just because of the earnings momentum, you could make a lot of money. So the time period in which I experienced the Indian corporate was also very good for me in terms of starting your investments, and that worked out pretty well.

**Nooresh Merani**: So, in terms of what we are talking about Kaveri Seeds, I think you have an interesting story to share. And now that you don't own the stock, you can talk much more easily about how you got in and I think you almost wrote a note also on the exit. There was a lot of scuttlebutt involved in terms of actually accepting the numbers, I suppose.

**Samit Vartak**: Right. Kaveri seeds, at that time, was in the initial phase. So you're always excited and being a farmer, I also connected well with that company. Not just me, but a lot of other investors like Manish also used to go, even I think, Girish Gulati, the Delhi investor, also was doing scuttlebutt on Kaveri. So we could always connect together to share what everyone was finding. The pre-monsoon was the peak time for looking at which seeds were selling the most. There were two big markets - one was Andhra Pradesh and the other one was Maharashtra. So if you could go to that Cotton Belt, and talk to the farmers and also talk to the retailer who was selling the cotton seed packets, you could see which company was selling the most. There were two big ones. Nuziveedu was the biggest one, which had almost 20% market share and Kaveri Seeds only had 5% market share. And based on our scuttlebutt, we realised that there was not much of a difference between Nuziveedu's quality of seeds and Kaveri's. Actually, with Kaveri, the farmers used to give feedback that a couple of those seeds were really good. And hence, we thought that there is no reason why Kaveri should not reach that 15% or 20% kind of market share. So, there itself just because of market share gain, they should probably at least triple their top line from here. And hence, we took that call.

But after all, as a long-term quality investor, one has to realise that Kaveri can always be regulated. Whenever it comes to farming, pricing and government, things can change in a matter of a day. And that's what actually happened, the seeds were in such short supply, that many a time it used to sell in the black market. So the price of the packet officially was like ₹ 900 a packet. But there were times when it was selling at ₹1200 or ₹1600 in the black market, unofficially. So I think because of that Maharashtra government came in, and they set up a slab, that you can't sell this above ₹800, and then the government is going to control the pricing. And with that, you realise that the business model has completely failed. As soon as the business model fails, you've got to realise that your hypothesis now has completely changed. You have to change with the changes and circumstances. So fortunately for me I completely exited Kaveri Seeds. At that time, I was managing money in SageOne. So for the clients as well, I completely exited. The group with which I was connected, said that's okay, it's a minor change and we are completely fine holding on. Because the P/E multiple was still low for this company, and it was always like 13 or 14 P/E multiple. So many of those investors kept on holding it, and I, fortunately, got out. And I think the price then was ₹800. And then slowly, it came down to like ₹400. Even today, the price is after probably eight years, it's still at ₹500 or ₹600.

**Nooresh Merani**: And with Kaveri, I remember, people had an issue in terms of no tax because of agricultural income. Tell us more about how you accepted that all the numbers are true.

**Samit Vartak**: I think one of the checks that we did at that time was that the technology was from Monsanto. So they had to pay a royalty to Monsanto. Right? So the question is if they're selling a number of packets, an equivalent amount of royalty has to go to Monsanto. And fortunately, we had some connections in Monsanto, where we could cross-check that there was that much royalty paid. And that gave us that comfort that okay, the sales are real. While speaking to farmers, we got a first-hand report on the quality of seed and that was good enough that at least the sales are not fake. They are not just on paper because that is very easy. When you're not paying tax, who is going to question it? So it's very easy to fake sales. But with Monsanto in between, we got that comfort and we were fine investing.

**Puneet Khurana**: Samit, now let's give a structure to your investments and how you go about selection, allocation, and all the key components of investment style. From what I figured out while reading your memos, and from your website, and many other communications which you have done in various media houses, your selection is reflected in the name which you have. Right? So when you say Sage, you're talking about sustainable, accountable, growth-oriented efficient businesses. So this pretty much zeros down what kind of companies you're looking at. Is that a fair assessment or you do deviate from it, you know, sometimes you start with a name but then the investment philosophy has evolved over a period.

**Samit Vartak**: That's completely fair. We definitely look for things which are sustainably structured in nature. Growth is definitely our primary focus. Valuation is something that is important but that's never a starting point. So that's completely what we look for and stick with.

**Puneet Khurana**: So let's expand it a bit. When you say sustainable, what exactly are you evaluating? What are all things you're looking at in the business when you're looking at sustainability? Similarly, when it comes to accountability, what are the parameters which help you evaluate these? So let's start one by one. Can you take us through what you mean by sustainable and what exactly are you looking for?

**Samit Vartak**: Yeah, so for sustainable, for example, we don't invest in commodity companies. Commodity means that companies may be selling commodity products but the business model is not commoditized. So I'm invested in APL Apollo, which you may call that it sells commodities. But the business model is not a commodity because it has the pricing power or pass-through power, that even if the steel price is at ₹30 or ₹60, generally they end up making the EBITDA per ton. So EBITDA per ton is sustainable, so then we are fine with that. Whereas, if you look at say, Tata Steel, their cost structure is almost fixed. It doesn't change with the change in steel prices. And the selling price has nothing to do with the cost structure. Because the selling price is driven by global factors. Tata Steel cannot get up the price. Hence their profitability is not sustainable at all. It can be usually profitable or it can go into losses. So that's a commodity kind of business. So we stay away from such businesses. So, when we exited Kaveri Seeds, I mean, that was the big issue, that now the margins are not sustainable. Because the cost structure is not something which is in control of Kaveri, but the selling price is set by the government. So, now the margins are not sustainable. Who knows whether the government will drop that price from ₹800 a packet to ₹700. So the company should have the freedom that their margins and profitability are sustainable. And that is what we look for in businesses.

**Puneet Khurana**: Does that also take out certain industries or companies that go through certain tailwinds, which do last, let's say, one cycle or four or five years kind of cycles? Because not all businesses are structural throughout the journey of 20 years. Some go through periods of sustainability and then they go through struggles, and then the cycle turns, etc. So, does that sustainability angle take out those four or five-year cycles also? Or do you evaluate them in a different way?

**Samit Vartak**: See, as an investor, you can't have a 10-year kind of a view. So I think there is a different period in terms of two aspects of investment. One is you have to evaluate in terms of growth, what is your growth horizon. So as I said, we look for companies where the earnings will double in 3 to 4 years because if you're looking for portfolios doubling in 3 to 4 years, your earnings have to double in 3 to 4 years. So whether the sustainability is pretty much guaranteed or sustainable, during that time, the EBITDA margins and the profitability, are what we look for. But when you're evaluating risk, it has to be evaluated from a much longer-term perspective. Because that disruption or risk can come in at any point in time, you cannot time it. So with that growth of 3 to 4 years, you got to see what is the worst-case scenario possible in terms of risk and whether that risk can come in. So if disruption is one of the risks, say in the combustion engine, at that time, if you think that the risk can come in the next 3 years or 4 years, even if you think that the margins are sustainable, you stay away from such companies. So generally, you look for your investment horizon, and it's sort of a rolling ball. At every point in time, you keep on evaluating, in the next 3 to 4 years, what is, first of all, the sustainability of profitability and sustainability of growth? And then what is the possibility of that big risk hitting you, and sort of disrupting that business? So, sustainability can, at least in terms of margins and growth, need to be there for your investment horizon. For me, it's not 10 years, it's generally 2, 3, or 4 years - that is the investment horizon. And you keep on moving that forward as you go along. And whenever you think, okay, now, the possibility of this is very likely, and it's going to happen in your investment horizon, you get out of that business.

**Puneet Khurana**: Let me pick up a few things that you said in that explanation. You said you're looking for 3 to 4 years of doubling the earnings in the businesses in which you're investing because that's your ultimate investment goal also for investments you're making. I'm guessing rerating is an optionality you are counting on but that's not the underlying principle of your investment. Can you then give your point about the valuation? It's very clear that you are not focusing way too much on valuation but more on the growth part of the business. Where do you draw the line? Can you give your views on the valuation front also?

**Samit Vartak**: See, at least in my experience, if I look at all the multi-baggers that I have invested in, right from say Kaveri, Bajaj Finance, Aarti industries, PI industries, La Opala, APL Apollo, Deepak Nitrite, or BKT(Balkrishna Industries) for all those, the starting valuation was very cheap. So, unfortunately, the starting point and the P/E multiple is not always in your hand as a fund manager. As a fund manager, you get money every day. Right? So, the only sustainable way of generating that, you know, if I double in 4 years, it's 18% return, if I double in 3 years, it's 26% return. So the 18% to 26% range of returns is only possible if the earnings growth is at least that much. The valuation rerating involves a lot of luck based on your starting point. But my experience is- if you want a real multi-bagger which is going to go up like 5x or 10x in the next 3 or 4 years, it will not happen if the valuation is not really really cheap. So, that may happen or it may not happen. You will not find such companies every time. In a 10-year phase, you will have 2 or 3 such times, when you are able to find those companies at such valuation.

So one time was in 2012-2013, and the next phase came in probably in 2018-2019 or during COVID times. So in the last 10 years, I would say there were only two real such phases, where you could find such valuation multiples. Otherwise from 2014 to mid-2018, companies were at a high valuation. Those starting points will very rarely deliver you these huge multi-baggers. Similar is the time today, with such valuations today, you can make consistent returns. That 18% to 26% is possible. But if you're looking for large multi-baggers, it will only happen through valuation or rerating. I mean, imagine that, in Bajaj Finance, the starting price to book was 1 to 1.5 times. And that over the next 5 to 6 years went up to 9 times, so there was huge rerating. For PI Industries the starting multiple was 15 times, today, it trades at, 45 to 60 times. So generally I've seen that in a huge multi-bagger which is about 10x, in a 4 or 5 years kind of a period, the 2x to 3x returns are only because of P/E multiple rerating. The remaining 2 to 3 times multiple will be because of the earnings growing at that kind of rate. But as a fund manager, you don't have that kind of flexibility of just keeping on waiting for such times.

**Puneet Khurana**: But Samit, let me invert that again. So as you rightly said, as a fund manager, you don't have the choice of when the capital is coming to you. I understand that valuation might not be in your favour all the time for a rerating to play, and hence the focus on the growth aspect of it. But then there is the reverse side that when there are valuations, which are completely anti return possibility, where there is a higher derating possibility, forget about rerating. So, how do you deal with those kinds of phases? Because growth is not something you can compensate for by saying that since this has derated I will see some growth. So how do you deal with that?

**Samit Vartak**: As you go along and your experience, I mean, that's a real threat, you may not think about. Whatever you may propagate like you have a 10-year horizon or an investor may also think that I'm a very long-term investor, but what happens is that when there is a derating, it is so sharp. Whether you look at the 2008 time period, or even the 2013 period or COVID times the P/E multiple dropped by almost 40% to 50%. So, a normal 25 multiple, became a 15 multiple. Now going back from 15 to 25, it's almost 60% to 70% return. So, unless your earnings growth is 60% to 70% during that phase, you will end up losing money. So even we have had such periods. At the 2017 peak, our portfolio's P/E multiple was at 30 to 33 times. And at the bottom of March 2020, during COVID times the P/E multiple was at 15 times. So it was almost half. And during that time, even if my earnings doubled in that 2 - 2.5 years, my portfolio returns will be zero. So when you look at the last 10 years, there were periods of almost 3.5 years when we made no money. So we took a conscious call in 2017, that we will not accept further money. For a year, we stopped taking any money. Even last year, in the small-cap fund, we said we will not take any money. I mean, that's the only thing you can do. And you warn your investor that this is the situation.

See, what happens is that investors also have asset allocation, especially the ones that come to us. These are large families and they give us 2%, 3%, 4% or 5% of their net worth. It's not their entire wealth. Most investors do not give us their entire wealth. Mostly, it's in single digits, and then it's a part of their asset allocation. So in terms of valuation, they need to play around with the asset allocation, how much to invest in alternative assets, fixed income, or equity. Within equity also, they think, about where to sort of concentrate, from which fund house to take it out, and which fund house to put in. So those kinds of things are done by them. So at our end, we can say that this is not the right time to come in, don't give us any more money, or if there are investors who are coming in for the first time, we'll just not take them. So I haven't really found a solution beyond that. Because as a fund manager, I may think valuation is high, but what if it continues for the next 3 years or 4 years? You will never know. That's just a highly probable event that returns from here on are going to be very very difficult, but not necessarily something which is going to play out. So even I need to keep that possibility as an outcome. And accordingly, I can't just go on my limb and say, this is the time to just get out of everything. Because I never know. What if, after 2017, India got into a real boom phase for the next 10 years, then I would have fallen on my face.

**Nooresh Merani**: So going into that part, because we've seen all your memos, and I've been reading for a long time, is the quantitative part, which you put in wherein you do a lot of market analysis of all the stocks, the earnings of all the stocks? I've seen, you compare the top 400 companies, the bottom 400 companies, and the earnings growth. Is this something that helps you? You launched and you've done superbly well in your small cap, but your timing was just precious in terms of the time when you came out because you launched in 2019, and not in 2018. And I think there was a memo at the start of 2018 and your take on long-term capital gains affecting the valuations, which you did. So could you tell us more about how this whole quantitative side of it helps you decide not just investments, but this sort of asset allocation call? Because you were buying into a small cap, but you launched a small cap fund only in 2019.

**Samit Vartak**: What happened was as you become big, liquidity is such a big issue, that you end up migrating more and more towards mid-caps and large caps. And when you have such a large universe, it's like 80% of your companies are in that bottom 10% of the valuation. That's a small cap, which is almost impractical for most fund managers, who are managing anything about say 500 crores. So, there is that huge universe, which is so inefficient. As a fund which had grown to 700 to 800 crores, we had to let go of those opportunities. And then, as Nooresh said that I keep on doing a lot of slices and dice of data and some of that I do present in my memo. But there is a lot of other data which I keep on evaluating in terms of what is completely out of favour kind of asset class or which sectors within the equities. Small caps at that time had presented a valuation gap and as well as the FII & DII. In addition to the long-term capital gains, there was also the heavy reclassification of mutual funds, because of which fund managers had to forcefully exit. And I had seen myself that if ever, I have to buy 1% of a company, within a matter of a few days, the impact cost was at least 15% to 20%. So, that's how illiquid Indian markets are. Even now if I have to buy 1% of a company in a matter of 3 to 4 days, the impact cost can be sometimes as high as 30% or 40%. So you can imagine that if you're forced to exit out of these mutual funds of so many of these companies, it is natural that those stocks and while selling the impact cost, sometimes becomes even higher, because there is no one in front to buy.

And hence, I thought that was a factor in almost all the small-cap companies because all the mutual funds had to forcefully get out. And I thought that was one of the best times to come into the market. Hence, we said this is the time to come into the market. During my launch call, I had said that I had never told my in-laws to invest in the stock market, because the stock market is so uncertain, and they have never experienced it (slight laugh). I even told them in 2019, that whatever excess money they have, just invest in this. So that was the first time ever they invested in the stock market. But even when we launched, there was not much of a response from the investor because the times were so bad, that it took a lot of guts to come into the small-cap space then. It was so beaten down. But that's the time you got to come into the market. And hopefully, that is what we will keep on doing, that when we launch a certain thing, it is so out of favour, that for most investors at least the experience will be good. And with consistently doing that, they will at least realize that whenever we come out with something, it is better than the average time to come into that sort of class.

**Puneet Khurana**: Samit, so we are now going into the portfolio side of things. Before that, I want to finish what we started on the selection part, we did cover sustainability, and we did cover growth-oriented. Can you also comment on what you mean by accountable and efficient? And how do you measure those parameters when it comes to the companies you're buying?

**Samit Vartak**: See, accountability is more of the management quality. It's whatever they say, whatever they have committed, they deliver on that. So that is what we look for. It's all about the management quality or the accountability of the management in terms of execution. And efficiency is more about capital allocation. When you're looking for growth kind of companies which we look for, you have to be very very efficient in terms of capital allocation. This is because the reinvestment is continuous. When you're growing at 18% to 26%, most companies' ROE is going to be in that 20% to 25% range. So almost all of the capital, you need to reinvest into the business to keep on growing at that rate. So you need to be very, very efficient. That is one of the biggest factors we try to evaluate in the future investments that they do, the incremental return on investment has to be higher than their existing return on investment. Because you don't need to go down the value curve, just for growth's sake. You don't want to invest in poor-quality opportunities. So that's really important. And that's the only way you can without having to leverage, will be able to keep on sustaining your growth rate. Because if you leverage, it actually doesn't remain sustainable. At a certain point, you'd have to completely stop.

**Puneet Khurana**: That brings me to two questions when it comes to capital allocation. Correct me if I'm wrong, but my assessment then becomes that the first criterion is going to be past good asset allocation when you are selecting a company. So you're not going to go into the stories of where the turnarounds will happen or where the efficiency will come in, but the management has no record whatsoever of doing it in the past. So I'm guessing that you will let go of those kinds of opportunities. So hence, looking at past capital allocation is an important criterion for you, which you can judge using return ratios. Is that a fair understanding?

**Samit Vartak**: There's no other proof.

**Puneet Khurana**: There is no other proof, right? And secondly, so then the question becomes more of incremental capital and the scalability of whether it is there or not for them to deploy that capital, but you're not going to make an assessment call on new capital making more returns than what they have done in the past.

**Samit Vartak**: That shows that their capital allocation decision is good. Otherwise, I mean, there are always opportunities. If you just want to make 12% or 13% return on investment, there are millions of opportunities. But you need to focus on the ones where at least it will have 20% plus.

**Puneet Khurana**: The second thing you said is that just when the capital allocation is not there, you don't want to go down the quality curve to chase growth. Do you make those kinds of decisions on the valuation side also? So when we were discussing valuation, I wanted to ask you this, you said valuations are crucial for the next few years of returns especially when they are on the higher side because there is a possibility of derating. In this scenario, when you find your companies to be in that zone, do you make a shift out of those companies? Primarily, because now they have gone into the zone where it's pretty much given that derating is going to be the future rather than rerating. Do you make those decisions?

**Samit Vartak**: So on your first question of not going down for valuation, I mean that just because there is growth, it doesn't mean your valuation will increase, right? Suppose investors expect their return on equity from the company or return on investment from the company, say, at 18% level, and the company invests in opportunities where the return on investment is going to be 12%. In that case, actually, you're destroying value. Your P/E multiple as well as your total market value will actually come down. So that is something which is very very important that they need to invest where their P/E multiple, as well as market valuation, should go up.

In terms of derating, after all, it's all about making returns. So for example, if I have a company which is trading at a P/E multiple of 10 times, I think that for that kind of quality of company, its multiple seems really low. And say, 3 years down the line, its earnings, say goes up by 20% and the P/E multiple also goes up by 20%. So overall, maybe you will make 40% return during those 3 years. Whereas, in your other company where the P/E multiple is say 40 times where you know that, it may be above its fair valuation. But in the next 3 years, it is going to double its earnings. So even if the P/E multiple comes down from 40 times to maybe by 10% or 15%, you know, my return from 100%, will come down maybe to 80% or 85%. So, still, I'm going to make more money. So that's the call you need to make what is your starting multiple? What is the ending multiple? And in between what is going to happen to the earnings? So, sometimes derating also is reasonable enough for you to invest. Because at least the returns are going to be more.

**Puneet Khurana**: let's take that same example, which you did slightly further, and say that the P/E multiple now is in an uncomfortable zone. It's not 40 but let's say it's 80. At that point in time, so my question is, do you make exit calls? or even allocation adjustments based on valuations if the valuation goes really really berserk?

**Samit Vartak**: See, because I've done a professional valuation, I think one thing is very clear to me the fair value is not one number. Fair value in valuation is a pretty large range. So a fair valuation can be from 20 times multiple to even 40 times multiple. But beyond 40 times or 45-50 times, it's an extraordinarily expensive valuation, below 20 times is really really cheap. So whenever the valuation is beyond, say, extraordinary, those times, if we are invested, we'll get out if we're not invested we will not invest. But we are pretty flexible in terms of that fair value range. So there, I'm okay because I don't know whether 20 times is the right multiple for it or 40 times is the right multiple. But at 45 times I know it is not the right multiple for it.

**Puneet Khurana**: Okay so, we are now moving more towards the allocation of the portfolio side. But on the point that you just mentioned, let me ask you a follow-up question. So let's say you are in that zone, where you take that exit decision because the valuation has gone into a very uncomfortable zone. By the very act of selling, you will have cash available to you, and cash brings in the mental liability of redeployment, so to speak. Generally, that kind of market environment comes when overall markets are also pretty overheated. And if you want to find the value you have to go down the quality curve. So is there a decision of how much cash you want to be in? Let's say you're in a very overheated market. How do you manage this aspect of allocation?

**Samit Vartak**: Yeah, I think that's a very important aspect because what happens is that whenever you have cash, a fund manager's natural tendency or there is too much urge to just deploy that somewhere. Because you think that you may lose out on the opportunities. So there's a huge opportunity cost. As a long-term investor, if you want to take the right decision for long-term returns, you have to set certain rules for exiting. And if at that point, there is not a better opportunity to enter, then better you stay out of the market. I mean, that's the only strategy which will make you have higher cash when there is complete froth in the market. So we are completely fine going even up to 35% or 40% cash. If we are exiting and if we don't find opportunities, we can wait and watch. I think it's very difficult to do that, but as a prudent strategy, I think the investors will get a lot of confidence. Especially when the market cycles have shrunk so short, the volatility has also increased, and these kinds of corrections happen more often these days. So as a long-term fund manager, you don't have to think that you need to be completely invested for all 10 years. I have gone through phases where there are periods when you make no money for a long period of time, 3 or 4 years. And at that time, the opportunities sometimes you get are so attractive that even if you have 15% or 20% cash, that cash can be equivalent to having 40% cash, because the valuations that you get are probably at 50%, 60%, or 70% discount during that time. So cash is usually valuable.

**Puneet Khurana**: Okay, but let me also bring in an argument that 100% cash people bring to the table majority of the time. See, I like to go in cash myself, so this argument is not mine. But what I've heard often is that history has taught us that the overvaluation zone goes to crazy overvaluation zones in the absolutely euphoric market. So imagine yourself sitting in a 2006 kind of environment where companies were overvalued and then they became crazy valued, right? So when your yardstick to exit is based on valuation? you can take yourself out of the game and go in that 35 % or 40 % kind of cash much before the market peaks out. And that impacts your relative return tremendously. I mean, a relative performance so to speak. Are you saying that decision will make back those 40 lost opportunities on the flip side in the cheap markets? Or is that a decision which worries you or how do you deal with this argument of 100% cash?

**Samit Vartak**: See, I think a lot of the argument of 100% cash is by large fund managers where they get a lot of institutional money.

**Puneet Khurana**: I'm sorry, I'll correct 100% equity, not 100% cash twice. That's my bad.

**Samit Vartak**: Many fund managers just focus on the outperformance of the market. So that's their mandate they have to outperform the market. So whether it's going up or down, it doesn't matter to them, the absolute returns are not important. It's the relative returns, which are important because it's all about the asset allocation that their clients have done at their end. So that is also fair. It also depends on the investor, what is its mandate? Is it an absolute return in the long run? Or is it a relative return to them in the long run? So for someone like us, if you're focusing on absolute return, you're right, I think there could be periods where there is a huge bull market, like what happened from 2003 to 2008 period. But it happens once, I don't know in how many years, not even in 10 years. But because of that sort of experience, you keep on taking decisions based on that one event, right? I don't know whether it's the right decision. It may not happen. But if you're patient enough, after 2008, the market, the small-cap and mid-cap index went down by 74% or 75%. So it probably gave up the last 2 or 3 years of gains.

Because to go back to that level, you have to go back for 4X now. So, if you're patient enough, and if you're sitting on cash, even those huge bull runs, actually rationally make sense. In normal markets, I think these days you know, the corrections happen very often. And that 20% to 30% kind of a correction is so often these days, that I think you don't have to go back into 35% to 40% cash at every point in time. Those are the situations when they are really super expensive and here even if it's 15% or 20% kind of cash, you still are invested at 80% or 85%. But that 15% to 20% cash, when you get the opportunity sometimes to buy at 40% to 50% discount is extremely valuable. It makes up more than having just invested 100%. Because in a down market, it's very difficult to exit, especially for a small and mid-cap fund manager, it is almost impossible to exit and create cash during a down cycle. It can only be done when times are good. I think 15% to 20% cash is reasonable enough with not too much of an opportunity cost.

**Nooresh Merani**: So when was the last time you took a big cash call in the PMS or personally?

**Samit Vartak**: My personal portfolio and PMS are exact replication. So the last cash call that we had taken was during COVID times. And I had also written a note to my clients during that time about why we had taken a cash call, but that was more of a macro cash call. Whenever there are too many unknown unknowns, which was the case then, COVID was such an unknown event. And the implication of COVID was even more unknown. How will the government react to it and with that what kind of impact it will have on the economy and corporate India? There was so much unknown that, for me, it didn't make sense to be 100% invested at that time. And the time that you got to exit was very short. I thought let's slowly take a cash call, and we got into like 15% or 17% cash. Our goal was to probably raise 20% to 25% cash during that time. But the next Monday it opened like 10%, down. Now, what do we do? But still, we were about 17% to 18% cash, and if it was a slow sort of down, then we would have been more in cash. But what we thought will happen over the next 3 to 4 months, happened in the next 2 weeks. After the 23rd even India announced a full lockdown. And by that time markets were down 30%. And we said now, at least COVID risk, even if it's not known exactly, but a lot of it is priced into the market. And then the actions taken by the government were also pretty known, that they are just going for a huge lockdown and then they will shut it down for 2 or 3 weeks and then open it up. So we had gotten some sense of what it was going to evolve into, and then the market was down by 30% to 35%. So we thought let's reinvest now and within the next 10 days, we had reinvested all the capital that we had.

**Puneet Khurana**: Samit, we have discussed valuation-based selling. You sell when you find overvaluation in your companies. What are the other reasons when you get out of your positions? Both from the business side, I mean, when you're making money or when you're losing money. So how do you evaluate those situations from the selling perspective?

**Samit Vartak**: For us, because we have a clear goal we need to invest in companies where the earnings will double in the next 3 to 4 years. After every quarter, we do evaluate, whether that's still possible going forward. Because it's all about looking forward. Just because since investment, say the earnings have gone up by 50%. Now we only are left with 50%. That doesn't make sense, because, by that time, even the prices should have reacted. So it's all about looking forward like 3 to 4 years. Can they still double the earnings? At any point, we think that's like a remote possibility, we exit. So the most common exit for us is because fundamentally the company is not meeting what we are looking for. Valuation sometimes as I said, we have a pretty patient sort of range of fair valuation. Whenever they crossed that range and now we think that there is a huge possibility that the earnings are only going to double in 4 years and then the multiples are most likely going to derate, then that's also a reason that we will exit. So even if, say the earnings probably are meeting the lower end of our criteria, but the valuations are so expensive, then highly likely that the valuations can correct by 20-30% or even 50%. That's also a reason for us to exit. And then other common reasons like some events whether regulatory reasons or the management taking the wrong capital allocation decision or some corporate governance issue, then there is not much patience that we have.

**Puneet Khurana**: And what is your wait period? So let's say you entered into the thesis, the growth is showing up, but the price is down and you know the market is just not recognizing it and it can happen for years and years, sometimes, you know, the market can go into that phase of not giving value to the company. So do you have a waiting period after which you say, okay, the market is right, we are wrong?

**Samit Vartak**: One has to evaluate what is the reason. Sometimes what happens is that there is a temporary phase like what happened in the last couple of quarters. The earnings are taking a hit because the fixed costs and a lot of raw material costs have gone up, and it takes a couple of quarters for the company to pass on the pricing. So if there is a reason that we understand the underperformance of earnings, we can wait and watch. But sometimes, if we realise, this is probably a permanent structural change, which happened, so now sustainability is a big factor, which is under risk, then, we don't wait too long. Maybe a couple of quarters, 2 to 3 quarters is the max, we would wait. And then we would exit. Because, after all, you can't be certain.

**Puneet Khurana**: Has there ever been a case where the market has not recognized an investment, you've invested for multiple years and you held on to it? I'm just trying to gauge your holding power in those scenarios.

**Samit Vartak**: If the earnings have come through, they have generally been recognized. It's mostly like you going wrong in your thesis, in terms of fundamental earnings growth, which is when markets generally penalize you. They actually even give you a derated multiple. But I don't remember a circumstance when the earnings multiplied, and then the markets don't care about it.

**Nooresh Merani:** So there we go to the places where you have made a mistake in your thesis, so maybe you could give us a few examples.

**Samit Vartak**: Most of the time, the thesis has been that sustainability is a big problem. For example, Indo Count. They are into bed linen, and then I visited their warehouses and showroom in New York and got really good feedback from the designers and the customers. But now they were getting into the larger market of bed toppings, fashion design, and all of that, which was a bigger market for them. We thought that there is a huge growth trigger. Valuations were also at 13 or 14 times kind of a multiple. But then with the quarter results, we were shocked by the kind of margin pressures they had, with the good growth pressure they had, even after getting into a  segment. So we started digging further into it.

We then realise that Amazon was completely aggressive coming into the market. They were taking away market share from their customers. And if the customers are losing market share, it puts pressure on the vendor or the supplier. That's what happened in this case. So, we evaluated and realized that this is a much longer-term structural destruction and then as soon as margins and growth come under pressure, generally the P/E multiple gets derated very quickly. And that's what happened. So, of course, we got out with a loss of 35% or so, but we took that call within a couple of quarters.

**Puneet Khurana**: Samit, we have got most of your selection and portfolio management. One last question from my side at least is on the allocation front. How do you decide your initial allocations to the stock? And are you a partial position builder or you are an investor in one go kind of investor? Similarly, when it is up to selling, do you trim down your positions or do you move out of positions? Can you give us some colour on the allocation? How do you manage that?

**Samit Vartak**: So for the allocation decision for us that 16 to 17 stocks are a good balance in terms of the number of stocks, where we are not too diversified, neither we are too concentrated. With 16 stocks if you do the right diversification, you take away 95% of the systemic risk. So that is a good number. It means that on average we need to have an allocation of around 6% to 7%. So our allocation ranges between, at the lower end 4% and at the higher end 10%, at cost. The ranking has to be based on wherever we have the highest conviction in terms of taking care of the risks and the higher returns possible, they will tend to be more towards the 10% and the other way around would be up to 4%. But most often, we will start with 4% allocation for most stocks. And then as we get more convinced we will invest because whatever you do, at the initial phases of your investment, you will have much lesser knowledge than what you will have maybe 1 or 2 years down the line.

So, with that confidence built up, you will slowly keep on building the position. Sometimes that build-up happens in a matter of a few months, like 3 or 4 months, sometimes it may happen over a period of time. For example, companies which we have held on for a very long period of time, like PI industries, Bajaj finance, or APL Apollo, there even within our horizon period, we sometimes have had 4% allocation sometimes we've had 14% or 15% allocation. This is because with an initial allocation of 10% also, sometimes the market doesn't grow, but the stock grows and your allocation goes up.

We also do some tactical changes during that time, depending on the valuation. So valuation also is the determining factor. If you thought that, it's an attractive company at a valuation of, say, 30 times. Then the stock goes up very sharply, without earnings going up, and the P/E multiple goes to 40 times. Of course, it deserves less allocation. So if you thought 10% was the right allocation at 30 times then at 40 times 10% isn't the right allocation. It will probably have a 7% or 8% allocation as the right allocation. So that also keeps on changing, but we do it slowly. During exit, most of the time it is at one time. Very rarely we have done a slow exit. It will happen within a matter of a month or so.

**Puneet Khurana**: So only selling, where you're trimming your position for the reasons you mentioned. Otherwise, if you've decided to move out of the position, you will move out in one go. It's not about profit booking, partial profit booking or any such thing. Understood. Unfortunately, time is always a constraint. But I want to have one podcast with you where we only talk spirituality because I heard one of your podcasts where you talk about that, and it's an area of interest from mine, but I wanted this one to be more investing-centric.

In one of them we will not talk about investing, we'll move solely into the spiritual side of things. But one point I do want to cover is that I have seen that in your life, serendipity has pretty much played the role at all the key junctures. Be it you going to the US, be it your losses and your entry point into the market in 1999, be it coming to India and not finding IBD because I'm guessing if IBD was there in India, you probably would not have changed your style. How do you bring that aspect of your life and learnings of serendipity working for you into your investment style? if at all you do, or you don't try to mix the two when you know this, just give us a colour on that.

**Samit Vartak**: What I have learnt in life is that you're going through experiences. There is no point in me stamping an event whether it's a good event or bad. Just because I made a lot of money this year, doesn't mean it led me to happiness. Because after all, my end goal has to be happiness. So I don't judge an event. Even if something bad happens to me, I don't know what the repercussions of that are going forward. My job is only to take action. Events will keep on happening. I need to believe in the universe, saying that, the universe is what will take care of the results for me, and which are going to be good. Because I am not a judge of whether an event is good for me. I am not at that level to know what is happening today is good for me. For example, you propose to someone and she accepts the proposal and she becomes your wife. But then you can go through a really bad divorce five years down the line. So something which you thought was a great event may turn out to be one of the worst decisions of your life.

So why will you judge an event? Let life unfold in front of you. You keep on taking decisions based on what you think is right. Follow your passion and let the results come to you. And that's how I would do. In terms of changing my job, I thought that was the right decision for me or starting SageOne that was the right decision for me. Going to the US I had no option anyway. So, I just took the best option which was available to me. But you just need to keep on taking decisions without getting affected. Even if things are happening great, I think, you should not get too excited. If things are happening badly, you never know what is going to happen maybe a few years down the line. So take it as it is. If the universe has delivered you something, accept it with a full heart. Don't create friction by saying, I wanted this and I wanted that. Keep the flow clear and stay open to it. And generally what is right for you will come to you.

**Puneet Khurana**: Just to ask one last point on that is that even though you don't judge the events, you do learn from your decision, which you have made in past. Even though the decisions are not made with the best information, people tend to go back and reflect on the decisions they made and they try to come up with learnings from those decisions. That is one exercise which I've always found to be helpful but futile also because we judge the decisions as if we had all the information while making those decisions, which actually comes to us much later, and then we reflect on those decisions. So are you saying that's a futile exercise to do? Do you go back and reflect on your decisions and say, why would I take that decision?

**Samit Vartak**: When you live life, you collect a lot of data memory and based on that, your decision-making can change. Because through experience, you learn what is right and what is wrong. You need to make a decision with full intellect and with full compassion for others. With intellect, it means that you have to analyze what happened in the past, and based on that you need to take a decision. But just because you have taken a wrong decision, you don't need to repent and keep on thinking that. It's okay that it happened. Now going forward, you need to incorporate that learning and keep the decision. But you may again go wrong and that's also fine. You keep open to that kind of a possibility and not keep on fearing that, have I taken the wrong decision? Because that's like you're living a tight life. You need to live a free life with acceptance of what is going to come without any kind of fear.

**Nooresh Merani**: So, we are coming towards the end. I'll suggest a segment where Puneet asks you random questions but you have to answer in a line. I think I'll let Puneet start with a question. And a random question out of nowhere and you need to give it in a line. (slight laugh)

**Puneet Khurana**: We haven't planned this, okay, so it's going to be random for us also. The best book you've ever read and you learning from that.

**Samit Vartak**: Ashtavakra Gita. Learning is the same thing we spoke about.

**Nooresh Merani**: Earnings growth above accountability and efficiency or the other way around? Are you okay to let go of accountability for earnings growth?

**Samit Vartak**: Earnings growth is the main thing but there has to be some accountability

**Nooresh Merani**: so it's basically earnings growth above accountability

**Samit Vartak**: Yes

**Puneet Khurana**: Many times investors leave many companies based on very minor forensic issues. How serious are you about the forensics part of balance sheets or financial statements?

**Samit Vartak**: If you find some fraud in terms of numbers or if there are wrong data to evaluate, that's a complete NO. Just stay away from it.

**Nooresh Merani**: So BAAP investing or not? Buy At Any Price or not?

**Samit Vartak**: No. It should be within that reasonable range but the range has to be a little flexible. I don't need to be that stringent about that one number, that above this I'm not gonna buy.

**Puneet Khurana**: If you weren't an investor what would you have been?

**Samit Vartak**: I would have probably been a monk. Nothing else makes sense to me.

**Puneet Khurana**: Perfect. Absolutely pleased Samit. It was great talking to you. Learned a lot. I'm going to go through the podcast and make my notes. But it was brilliant talking to you. We'll definitely do one more podcast where we will not talk about investing. We will only talk about spirituality. But thank you for giving us your time.

**Samit Vartak**: My pleasure. Thank you so much.

**Nooresh Merani**: It's great interacting.

**Samit Vartak**: It’s absolutely my pleasure Nooresh and Puneet. Take care

**Puneet Khurana**: Thank you so much. All right bye thank you.