UNIFI CAPITAL

Review | Q1 FY2026

Acknowledging Context

After a few quarters where earnings momentum and liquidity conditions began to align well, Q1 FY26 has underscored how delicate this alignment can be. Global trade flows have acted as a scaffolding for sector-specific fundamentals, while India's equity valuations remain elevated. Numbers suggest earnings breadth has narrowed, policy and trade frictions can stretch near-term visibility, and that discipline in portfolio construction is more valuable than chasing every passing theme. The market is undergoing a phase of re-anchoring expectations, and our approach is to focus on businesses where earnings visibility and balance-sheet resilience give us confidence, while remaining vigilant to risks that are more cyclical than structural.

Q1 FY 2026 | Earnings growth remains subdued

Beneath the headline numbers, corporate India's earnings are showing signs of moderation. Reported earnings for the NIFTY 50 at 7.1% are modest on the surface, and excluding the distortions of commodities, the core, non-cyclical component of growth is struggling to rise above 5%. What explains the narrowness? First, banks are digesting NIM compression and a more rational stance on unsecured credit, even as asset quality stays benign. As a result, earnings are moderating off a high base. Second, consumption defensives have long normalized price/mix tailwinds and continue to battle the input cost/growth mix, resulting in softer operating leverage. Third, discretionary IT spend remains hesitant, and deal cycles are elongated, impacting revenue conversion at the top end. Put together, the 'quality core' of earnings is under pressure even as the indices hold up. This is not a strong base for market trading at elevated multiples.

Meanwhile, the US tariff actions [since August 27, 2025] have introduced a level of uncertainty that will only be resolved after you are in receipt of this note. Friction in export-linked sectors, including textiles, gems and jewelry, chemicals, leather, and select auto parts, clouds visibility in the near term. They may well be timing risk rather than terminal one, but they nevertheless complicate the outlook over the near term.

With non-cyclical growth running close to 5% and policy acting as a stabilizer rather than a spur, the market's tolerance for a narrative premium will be under pressure. In this construct, we align with businesses that demonstrate pricing power, cash conversion, and balance-sheet strength, and avoid firms where multiple expansions have outpaced earnings certainty.

Why this matters now: This backdrop only reinforces the value of discipline. We are consciously leaning into businesses where earnings are underwritten by durable demand, pricing power, and cash flow strength, rather than those fueled by cyclicals and sentiment. Similarly, we are trimming or avoiding names where valuations have outpaced earnings visibility. In other words, we are positioning portfolios not for the best-case scenario, but for the most probable one. Under these circumstances, we value the resilience of a business as the most essential variable. This is the compass we use to navigate volatility without sacrificing the compounding core of your capital.

Q1 FY 2026 Earnings Update

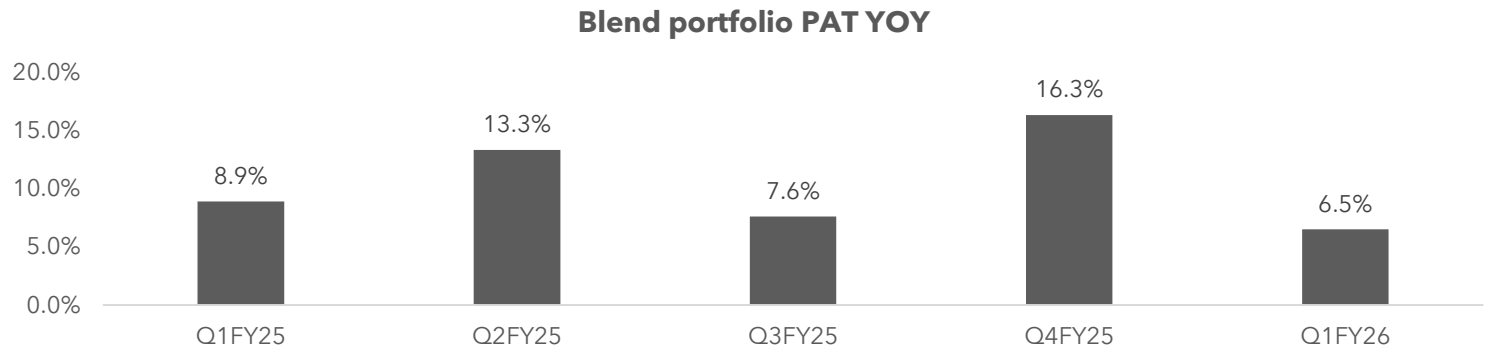
A Modest start to the year

Q1 FY26 was a relatively modest quarter for India Inc., with earnings growth remaining measured. The aggregate net profit of the Nifty-500 universe rose 8% YoY, reflecting stability rather than momentum, as sectoral trends offered little by way of positive surprise. The overall sentiment and outlook suggest a recovery path in the second half of the year.

NSE500	Adj PAT, Cr		
Sector	**Q1 June-25**	**Q1 June-26**	**YoY**
Banks-Private	48,337	47,814	-1%
Banks-PSU	43,638	45,753	5%
Consumer	16,845	17,520	4%
Consumer Durables	2,177	2,275	5%
Healthcare	16,138	17,044	6%
Automobiles	24,859	24,653	-1%
Utilities	31,212	29,186	-6%
Capital Goods	9,967	11,429	15%
Infrastructure	5,263	5,076	-4%
Technology	31,651	33,723	7%
Pharma	12,277	13,516	10%

Credit growth moderated to ~9-10% in Q1 FY26, compared to around 15-16% over the past two years, reflecting the combined impact of regulatory caution on NBFCs and unsecured retail lending. The moderation, coupled with the repo rate cut, weighed on NIMs during the quarter. Asset quality remained resilient, with GNPA and NNPA ratios at multi-year lows. The **consumer discretionary and staples** sectors reported muted topline performance amid a slowdown in urban consumption, while volatile feedstock costs further weighed on margins, resulting in tepid earnings growth. **Select Capital Goods and Industrials** firms reported a sharp uptick in order inflows and a good business cycle, while operating leverage improved across several firms. The **healthcare sector** remained resilient, supported by strong performances from hospital chains and CDMO players, alongside steady growth in domestic formulation businesses. Select **Passenger vehicles and tractors** witnessed sustained growth, whereas two-wheeler volumes softened after several quarters of expansion, reflecting the impact of a high base. However, **IT Services** remains an outlier due to continued macro uncertainty in the US and Europe, as well as disruption led by new-age technologies.

Unifi's portfolio companies delivered a weighted average earnings growth of c.8.3% ex-financials and c.6.5% at a portfolio level for Q1 FY 2026, supported by high return ratios and reasonable forward valuations.



In sectors such as agri-inputs, automobiles, asset management, healthcare, and manufacturing, Unifi's portfolio holdings have reported material expansion in business operations, order book, sustained margin resilience, and earnings outlook. While product distributors and infrastructure sectors witnessed a temporary slowdown, the outlook remains strong, supported by structural demand drivers, policy tailwinds, and ongoing execution improvements that position these businesses for a recovery in the coming quarters.

Portfolio Positioning

Credit – 16% | Growth Normalization with Stable Asset Quality and Selective Lending Tailwinds.

Systemic credit growth has cooled to ~9–10% YoY as the post-pandemic rebound normalizes, unsecured retail slows, and large corporates tap the bond market where pricing is competitive. We view this as a recalibration, and Banks are prioritizing risk-adjusted returns over headline growth—tightening unsecured personal credit and microfinance, and favoring secured retail and better-rated corporates. That pivot is healthy for franchise quality and RoE durability.

Within financials, our positioning is focused and selective. Staying true to our GARP (Growth at a Reasonable Price) framework, we continue to hold one of India's largest public-sector banks, which gained market share in FY25 while maintaining better asset quality than its peers through conservative underwriting and a diversified loan book, with low credit costs and a clear path to mid-teen RoEs. To address a broader question on why a PSU, specifically the investee company, has gained market share through FY25 without stretching its risk appetite, broadened its retail and SME engines, and improved liability granularity. Technology investments are yielding improvements in origination, lower operating expenses-to-assets, and higher cross-sell intensity—important ingredients for operating leverage as volumes stabilize. Capital buffers remain comfortable, allowing the bank to fund growth without dilutive equity. Against this backdrop, today's valuation still prices in caution rather than the franchise improvements we are seeing; that asymmetry offers a margin of safety and attractive upside.

In parallel, we added a leading private-sector bank last quarter—backed by strong governance, proven management, and superior growth visibility—which we see as a compelling re-rating candidate as the market recognizes its fundamentals. The current squeeze on NIMs is essentially a timing effect: loan yields have reset down swiftly after policy easing, while deposit costs will decline with a lag. The earnings impact on the sector must be viewed in this context. As we navigate FY26, our positioning within financials remains nuanced, towards institutions with strong underwriting capabilities, low credit costs, and room for valuation re-rating. The credit environment is shifting from a volume-driven to a quality-driven phase, and our portfolio reflects that pivot.

Hospitals & Healthcare – 10% | Operating Leverage Meets Structural Demand

India’s private healthcare sector continues to deliver robust performance, underpinned by sustained growth in Average Revenue Per Occupied Bed (ARPOB), rising patient throughput, and steadily expanding margins. What was once a premiumisation “theme” has now become a visible earnings driver: ARPOBs are trending higher across listed players, supported by richer specialty mix, higher inflows of international patients, and greater adoption of robotic surgeries, day-care formats, and other high-value procedures.

We remain invested in a leading East–South hospital chain with deep presence in the affordable and mid-market segments. Its overseas assets have scaled up strongly, contributing meaningfully to profits, while execution in India continues to anchor growth. The company is also building adjacencies that should add incremental growth engines over the medium term. Alongside, we hold exposure to a premium chain in the NCR and East, where brand strength and scale provide a durable advantage in metropolitan markets.

With improving visibility on free cash flow and a disciplined reinvestment strategy, our healthcare holdings are well placed to capture both cyclical margin expansion and secular demand growth. In our view, this combination of operating leverage, structural tailwinds, and balance-sheet strength makes healthcare one of the most attractive long-term themes in the current market environment.

Infrastructure – 8% | Outlook Has Improved

India's infrastructure sector is witnessing a gradual recovery in execution momentum, with spending this year concentrated in metros, railways, and power. At the state level, outlays are rising in Andhra Pradesh and Bihar. Our exposure within the sector remains aligned to companies focused on execution-intensive areas such as water treatment and urban construction. After navigating a weaker cycle, these businesses are now seeing stronger order book conversion. We believe the outlook for such firms has materially improved compared to recent quarters, supported by increasing execution visibility and disciplined balance sheets. With a robust inflow pipeline and operating leverage gains ahead, they are well-positioned to benefit from the next phase of infrastructure-led growth.

Product Distribution – 8% | Consistent Growth

Globally, enterprise demand for computing is accelerating, aided by shorter product cycles and rapid innovation that both drive obsolescence and progress. At the same time, consumers are becoming increasingly connected, with rising adoption across various segments, including retail, education, home, and business, as well as cloud and SaaS solutions. A notable shift is also underway toward premium products and more frequent upgrade cycles. Against this backdrop, we hold exposure to a leading global ICT distributor with a strong presence in India, strategically positioned to capture this expanding demand and deliver sustained growth.

Our portfolio company reported a healthy 22% revenue increase and 12% earnings growth year-on-year. In India an well as the rest of its global operations, the core business is strong, continuing to benefit from its leadership in IT distribution across India and the Middle East, with strong relationships with OEMs and a diversified product mix. Growth in cloud, cybersecurity, and enterprise solutions is broadening revenue streams beyond traditional hardware distribution, improving both margin visibility and cash flow.

Its subsidiary in Turkey, accounting for about 6% of revenue, has been suffering from the troubled economic conditions in that country. The company made meaningful provisions to account for delayed receivables and is scaling down its business exposure gradually. Given the limited size of the Turkey business, the market's reaction appears to have focused disproportionately on it, overshadowing the strength of the core earnings engine. We view this as a short-term aberration. The company has already adjusted its operating model in the region, and as the lira stabilises and demand normalises, we expect the drag to fade.

IT Services – 5%| Reduced Exposure

We have meaningfully pared back our exposure to Indian IT services, reflecting a reassessment of the sector's headwinds. The demand environment remains soft, with lengthening decision cycles and muted discretionary technology spend. At the same time, the deflationary impact of generative AI is becoming increasingly visible, as delivery models shift away from traditional people-intensive structures and pricing power comes under pressure. While large-cap IT companies have broadly defended margins, revenue growth across the sector remains stuck in low single digits, with little sign of acceleration in the near term. In this context, we have taken a selective stance, focusing only on businesses that combine three qualities: (1) a smaller base that allows for faster growth from lower revenue levels, (2) a strong, executable order book offering visibility into the next 12–18 months, and (3) product leadership in specialised verticals with higher structural growth.

Our current holding is in IT products and a mid-sized IT provider that continues to win wallet share in chosen verticals and geographies. We believe such niche leaders, with differentiated propositions and focused execution, are better positioned to navigate the transition that the broader sector must still grapple with.

Agriculture – 5% | Strong Season and Execution

The Indian agriculture sector is poised for a healthy kharif season, aided by above-normal monsoon levels and comfortable reservoir positions. Structural tailwinds such as higher Minimum Support Prices and improving farm economics continue to underpin rural demand. Within this backdrop, our portfolio comprises two differentiated players that are deeply integrated across the agricultural value chain—one a leader in complex fertilizers and crop advisory solutions, and the other a global innovator in crop protection and bioscience technologies.

Execution-wise, both businesses are at different but encouraging stages of their strategic roadmap: the fertilizer-led company has gained market share in key southern and eastern states, supported by backward integration, efficient distribution, and an increasing focus on value-added products, while the crop protection company is in the midst of a recovery following operational initiatives undertaken last year. Together, they are well-positioned to benefit from favorable weather, increasing input intensity, and policy support for sustainable agricultural inputs.

Asset Management - 5% | Growing Participation

The Indian asset management industry continues to experience strong tailwinds, marked by expanding retail participation, SIP-driven inflows, and greater acceptance of equity ownership. Monthly SIP contributions now exceed ₹28,000 crore, underscoring the increasing breadth of participation. The rise of passive and hybrid strategies, alongside robust participation in mid- and small-cap funds, points to a market that is deepening and diversifying in earnest.

Aligned with this trend, our portfolio holds two differentiated holdings in the asset management space—one an incumbent industry leader with scale, distribution, and performance; the other a credible challenger with higher growth optionality and improving performance and operating leverage. We believe the asset management industry in India is transitioning into a long-duration growth compounder, and our holdings are well-placed to benefit from this shift.

Automobiles – 5% | A Singular Bet on Market Share Gains

Within the Indian automobile landscape, our alignment is highly selective and centered around one OEM that executes with precision on volume expansion and value accretion. While most players in the PV space are grappling with intense competitive pressure and uneven EV adoption, our investee company stands out for its robust product pipeline, above-industry growth rates, and consistent market share gains in both ICE and EV segments. Complementing this, the ongoing agri-cycle tailwind has supported healthy tractor volumes, where the OEM continues to consolidate its leadership through sustained market share gains.

Specialty API – 5% | Executing well

We have exposure to two mid-sized pharmaceutical companies with differentiated business models and growth drivers. The first is an API player focused on building a diversified portfolio of low-volume, high-value products while adhering to stringent compliance standards. Integrated across the value chain, the company supports clients throughout the entire product lifecycle. It is now leveraging its established relationships in the generic API space to enter the CDMO segment. With a change in ownership and sharper capital allocation, we see potential for stronger growth over the medium to long term.

Our second exposure is to a pharmaceutical company engaged in the research, manufacturing, and marketing of OTC products, with facilities in India, the UK, and the US that are fully compliant with global regulatory standards, including the US FDA, UK MHRA, and Australia's TGA. With ongoing capacity expansions and a pipeline of new product launches, the company is well-positioned to benefit from operating leverage, driving margin improvement, and growth in the near to medium term.

GST Rationalisation: A Clearer, Simpler Path Ahead

India's forthcoming GST overhaul, paring down the tax structure to just two slabs and delivering an average ~10% rate cut, represents a meaningful policy pivot, one that promises to reinforce consumption and streamline enterprise economics.
At the consumer level, fewer slabs mean fewer anomalies: fewer goods stuck in mid-slabs, fewer price distortions between urban and rural markets, and lesser friction at the point of sale. A streamlined rate structure, combined with a 10%-average reduction, has the potential to translate quickly into lower prices for end goods, stimulating discretionary spending at a time when demand momentum is seeking reinforcement.

For businesses, the impact is equally noteworthy. Simplified GST architecture eases compliance burdens and reduces the administrative drag on working capital. Especially for small and mid-sized enterprises, the reform frees up cash that would otherwise be tied in elaborate input-tax credit reconciliations, invigorating working-capital cycles and helping under-leveraged sectors get a shot in the arm. In aggregate, the reform enhances the price-volume balance: firms might opt to pass on a portion of the rate cut to consumers, helping revive demand, while also operating with better margins due to efficiency gains—particularly in distribution and retail. The simplification also lowers the bar for MSMEs to integrate into formal value-chains, potentially boosting tax compliance and widening the GST net over time. In short, this is more than a cosmetic rate change; it's a structural policy lever that stands to give consumption its most tangible boost since the pandemic-era stimulus, with effects that could echo into FY26 and beyond.

Road Ahead

While the June quarter has underscored the importance of staying selective, the bigger picture for India remains constructive. In the short term, the government's renewed focus on consumption, as evidenced by GST rationalization, will provide a timely boost to demand, complementing the secular improvement already seen in rural incomes. Growth is also expected to receive a statistical boost in FY26, with front-loaded government spending on both capital expenditure and revenue programs, which will support activity in the second half of the year. On international trade, where the headlines have been noisy, the actual impact is likely to be contained—goods exports to the U.S. are only 2% of GDP, and the tariff-hit segments account for closer to 1%.

Taken together, these levers point to an economy that can navigate short-term turbulence and still compound steadily. Our portfolio philosophy remains aligned with this opportunity: lean into resilience, participate in secular demand trends, and stay alert to valuation discipline—ensuring that capital is positioned to benefit from both the cyclical lifts of FY26 and the structural drivers that lie beyond.

Managing risk while pursuing absolute returns

Our approach remains unchanged: bottom-up stock selection, sectoral agility, valuation discipline, and proactive risk management. We are not a model-portfolio manager, and positioning will vary across mandates; what is common is the intent to compound capital meaningfully while managing downside risk. FY26 will likely bring as much noise as clarity, with bouts of volatility shaped by earnings dispersion, policy shifts, and global trade narratives. In such an environment, risk management is as important as return generation. We focus on deploying capital where balance sheets are resilient, cash-flow visibility is strong, and valuations provide a margin of safety. This discipline allows us to stay invested through cycles while protecting portfolios from excesses, ensuring that returns are not just relative to a benchmark but are absolute, durable, and compounding in nature.

The following sections outline our investment strategies and provide a performance summary for Q1 FY26. Individual portfolios will vary in holdings and proportions based on the timing of your investments. Please do not hesitate to contact your relationship manager for a detailed review of your portfolios.

Review of Strategies

We have outlined each of our investment strategies in the following sections, along with a summary of how the fundamentals of our key holdings have performed in Q1 FY26. Tail positions that are on their way out of the portfolios have not been discussed. Individual portfolios will vary in holdings and proportion based on the timing of your investment with Unifi. For a detailed review of your portfolios, please do not hesitate to contact your relationship manager.

Blend

The Blend strategy continues to cherry-pick ideas from across the four distinct themes managed by Unifi, thereby investing in "the best of our best" and participating in opportunities across the breadth of the market. The ideas represent a mix of emergent themes, corporate actions, and fundamentally attractive bottom-up opportunities. We continue to focus on delivering superior risk-adjusted returns from an absolute perspective.

As of Aug 2025	FY 26E
Wt. Avg PE	22.8x
Wt. Avg PB	5.2x
Wt. Avg ROE	20.8%
Wt. Avg Mcap	Rs.117,559cr

BC AD

The strategy continues to invest in sectors that are currently witnessing a shift in market share from the unorganized to organized players. As India's economy rapidly grows in scale and sophistication, several sectors are poised to undergo significant changes over the next decade. Most of our invested companies are likely to experience an increase in their market share, as marginal players find it difficult to operate in the new environment

As of Aug 2025	FY 26E
Wt. Avg PE	23.3x
Wt. Avg PB	5.4x
Wt. Avg ROE	21.3%
Wt. Avg Mcap	Rs.115,084cr

BCAD2: Breakout 20

The BCAD 2 Breakout 20 strategy seeks to invest in sectors that are witnessing structurally high growth rates driven by demographic led consumption and larger stream of disposable incomes. The fund continues to focus on large operators with competitive advantage at scale, consolidating position in their respective categories.

As of Aug 2025	FY 26E
Wt. Avg PE	23.2x
Wt. Avg PB	5.4x
Wt. Avg ROE	21.3%
Wt. Avg Mcap	Rs. 111,764cr

APJ

The fund seeks to deliver absolute returns over a five year horizon through investments in sectors that will benefit from the next stage of India's growth on the back of improvement in India's infrastructure, and policy climate. The APJ fund continues to focus on firms delivering manufacturing excellence broadly across technology, pharmaceuticals, materials, and infrastructure in general

As of Aug 2025	FY 26E
Wt. Avg PE	20.0x
Wt. Avg PB	4.0x
Wt. Avg ROE	20.0%
Wt. Avg Mcap	Rs.124,036cr

ISS

The Insider Shadow Strategy invests in fundamentally sound companies where there has been an increase in the promoter holding. Typically, such an action by the controlling shareholder demonstrates their conviction that the company's growth prospects, or inherent value, is not captured in the stock price at that moment. Unifi's proposition is to gain from the eventual balancing of the value-price mismatch in the market by identifying and investing in such companies after a detailed review of their fundamentals and corporate governance standards

As of Aug 2025	FY 26E
Wt. Avg PE	19.9x
Wt. Avg PB	3.8x
Wt. Avg ROE	17.6%
Wt. Avg Mcap	Rs.108,804Cr

Risk

Risk	Mitigants
Geo-political risks	Any geo political tensions between India and neighboring countries can disrupt supply chain in the region. This might have a non-linear impact on business.
Raw material inflation	India continues to be dependent on the supply of feedstock whose pricing is global in nature. Key categories would be crude, metals, minerals, and natural commodities. Sharp movement in their underlying prices will have a short-term financial impact on the companies. The situation in China [political] has the potential to disrupt the supply chain of a few of our investee companies.
Liquidity risk (in case of NBFCs)	The NBFC led liquidity crisis in India has had a systemic effect on the entire economy. Our investee companies have been able to tap diversified sources of liquidity on the back of their long-term track record of comfortable asset quality and asset-liability-management (ALM). However, sustained deterioration of the asset quality can continue to affect our holdings in Banks and NBFCs.
Foreign Exchange risk	The foreign exchange system continues to be guided by global developments. Our investee companies in the IT sector are subject to sharp movements in the USD and GBP. They mitigate the same via hedging, but there remains a portion of revenues that continue to be subject to the vagaries in fx movements. Most of our non-IT exposure is to companies that derive their revenues from the domestic market. The revenue from exports would be minimal for each strategy as a whole, and where relevant, are adequately hedged. A sharp depreciation in the INR will affect the import of feedstock (higher prices) which can lead to a brief moment of earnings-related volatility.
Leverage risk	Except for financial companies, most of the operating companies in the strategies carry nil to moderate debt on their balance sheets with a track record of having managed leverage well in the past. Their leverage is monitored regularly.
Technology Obsolescence	Technological changes can render the products/services of a company obsolete and thereby hurt its profitability and valuation. Such a risk is generally minimized by limiting the aggregate exposure of portfolio to such investments to less than 10% of value.
Governance risk	We avoid investing in companies with a known history of corporate governance issues. If such issue arises in an existing investment, we stop additional purchases and start optimally exiting the investment.
Concentration risk	At the portfolio level, such risks are minimized by limiting the aggregate exposure of portfolio to such investments to less than 10% of value at the time of investment.
Stock Illiquidity risk	High Impact cost, due to thin trading at the time of buying or selling is endemic to small & mid-caps. We plan our investment decisions, size of the investment and trading strategies to minimize the costs due to illiquidity.
Key Man Risk	Small and mid-caps are frequently managed by a key promoter / person on whom the business is completely reliant and without whom the business would be materially inferior. We generally avoid such names and in cases where we make any exceptions, the aggregate exposure of portfolio to such investments is limited to less than 10% by value.

Slowdown in global consumption	The wallet-share of the investee companies in the global manufacturing value chain, does not pose a significant risk of loss of business to their vendors. New and high growth areas such as Lithium-Ion batteries, EV vehicles are in relative infancy stage and have a strong growth curve ahead of them.
Softness in IT product spends	The convergence to digital software solutions is a 'must do' proposition and our investee companies have exhibited significant traction in competing in this space. A combination of their recent deal wins, and current bid pipelines bode well for their future.

Thank you for placing your trust in Unifi.

Sincerely

Baidik Sarkar
Head - Research

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