



## Snowball Capital Annual Letter to Shareholders – 2076-77

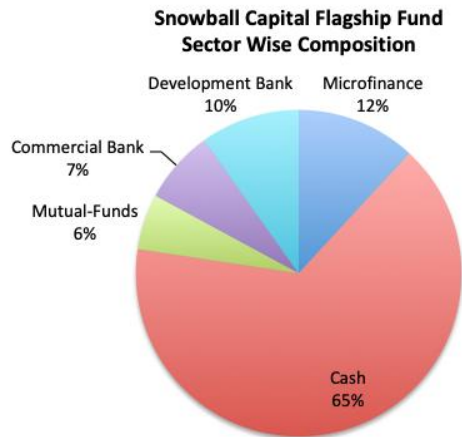
Dear Shareholder,

What a year it has been. The goal of this letter remains to communicate to you what we are thinking with regard to the markets and our holdings, update you on how your portfolio has performed and perhaps shed a light on why, and to reiterate our investment philosophy and processes. If I were to write a single piece each year, it would be this annual letter to you, our shareholders.

Starting Q2 of 2076-77, we have been running two portfolios – one managed by the Snowball team and a separate private portfolio managed by myself but advised by Snowball. The difference in the two portfolios is primarily to do with legal technicalities rather than philosophical differences. Hence, there is a significant overlap in the two portfolio’s holdings. Furthermore, Girish, our Managing Director, my family members, and I are the largest shareholders in Snowball’s Flagship fund.

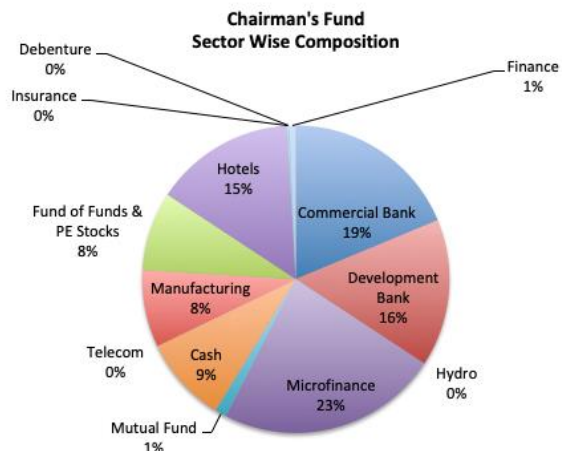
### Snowball Cap Flagship Portfolio

S.N.	Portfolio	Portfolio Weightage
1	<b>CBBL</b>	11.90%
2	<b>NICA</b>	7.26%
3	<b>LVF1</b>	5.50%
4	<b>GBBL</b>	4.41%
5	<b>MNBBL</b>	5.45%



### Snowball Cap Chairman’s Portfolio

S.N.	Portfolio	Portfolio Weightage
1	<b>TRH</b>	14.34%
2	<b>NICA</b>	9.43%
3	<b>Sanima</b>	9.30%
	<b>NMBHF1</b>	1.04%
4	<b>BNT</b>	6.95%
5	<b>CBBL</b>	10.65%
6	<b>MNBBL</b>	9.96%
7	<b>GBBL</b>	5.56%
	<b>Fund of Funds</b>	7.46%
8	<b>DDBL</b>	7.45%
	<b>PE Stocks</b>	0.86%
	<b>LEMF</b>	0.19%
9	<b>SKBBL</b>	5.11%
	<b>NICAD8283</b>	0.04%
	<b>HDL</b>	1.15%
	<b>JFL</b>	0.70%
	<b>OHL</b>	0.47%
	<b>NRIC</b>	0.17%
	<b>NICLBSL</b>	0.08%

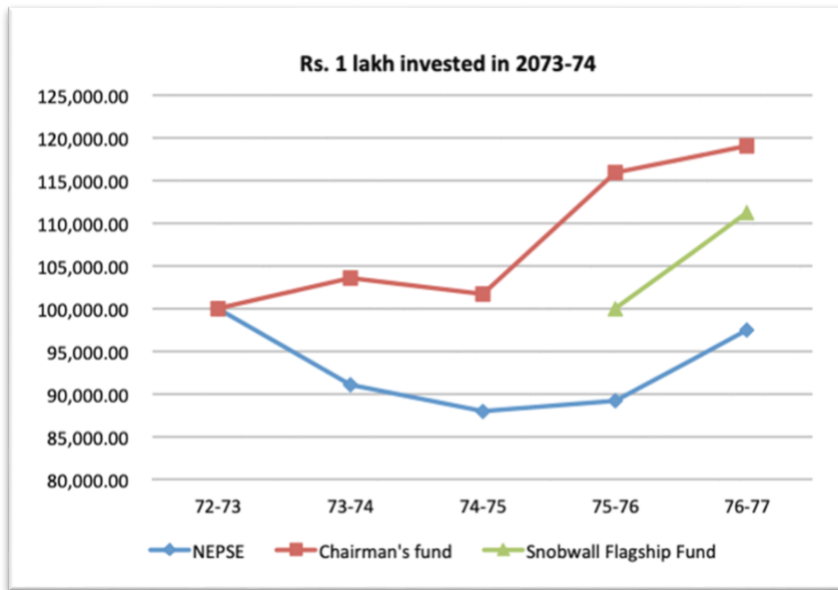




In what was perhaps the most turbulent year we have seen in our short career of 4 years, we etched out a return of 2.72%, comfortably beaten by NEPSE, which witnessed a return of 9.30%. The Snowball Flagship portfolio generated a return of 11.16% before fees, which beat NEPSE by almost 200 basis points.

### Our record since inception

	Invested Amount:		100,000.00			
	Nepse		Chairman's Fund		Snowball Flagship Fund	
73-74	-9%	91,000.00	3.62%	103,620.00		
74-75	-3.32%	87,978.80	-1.85%	101,703.03		
75-76	1.40%	89,210.50	13.87%	115,809.24		
76-77	9.30%	97,507.08	2.72%	118,959.25	11.16%	111,160.00
Total Return	-2.4929%		18.96%		11.16%	



While beating the industry benchmark (NEPSE), over the last twelve months and the past four years, does give us a certain sense of satisfaction, we are painfully aware that the returns are not remarkable in an absolute sense. However, we are not worried as we have just gone through one of the lengthiest bear markets in Nepal’s history and come out relatively unscathed. We expect our returns to be adequate and in line with our targets following a full economic/stock market cycle.

### Our Portfolio

In line with our value-based philosophy, we seek to identify companies whose stock price is trading below that of its intrinsic value. The trick of the trade or the secret sauce lies in accurately coming up with the intrinsic value of any particular company. There are a variety of ways to derive that magical number, some methods more logical and rooted in reality than others mostly taught in business schools, unfortunately.



## GROUP A

When we value a company, some of the key things we look at are:

- **Earning power** – the businesses' ability to generate consistent earnings over a long period of time.
- **Competitive moat** – its ability to protect its earning power from the forces of competition. This is a very important characteristic that is critical for long-term success and can come in a variety of forms (regulatory, scale, technology, brand, etc.).
- **Unrealized or unseen asset value** – mismatch between a company's assets' market/liquidation value and its carrying value. Examples may be land holdings or its investment in unlisted shares of high value.
- **Growth prospects and compounding ability** – a company's ability to continue growing and reinvesting its earnings generating returns above its cost of capital. This is the most difficult aspect to identify since it involves making a conjecture about the future. Although historical trends point towards a certain direction, it is by no means a guarantee that the historical trend will continue in the same direction.

Companies we identify based on the above criteria are companies that we invest in and hold indefinitely bar significant changes. We call this cluster of companies 'Group A' and they comprise of 71.3% of the Chairman's fund and around 30% of the Snowball Flagship Fund.

The companies in this group are:

- **TRH (Taragon Regency Hotel – Hyatt)**

We have held this stock since day 1. Although the industry is not the most attractive, given the hyper competition coming up in the market, high capital intensity, and its vulnerability to exogenous shocks (earthquake, Covid, political turbulence, etc.), we like TRH for the following reasons.

- Significantly undervalued assets (carrying value is 20% of actual market value)
- Competitive moat (high quality brand recognition both locally and internationally and the large size of the property. There is no other hotel which can accommodate 2500+ guests for events, banquets, etc)
- Zero debt and growing/compounding cash pile (this will help it survive any exogenous shocks for multiple years even with zero revenue)
- **NICA (NIC Asia Bank)**

NICA has grown aggressively in the last five years and has attracted a lot of naysayers, specially its peers and competitors in the industry. Its growth is often classified as 'high risk'. However, the rate of growth has stalled in the last two years. We have held NICA for exactly three years now. The reasons we still like NICA are

- Undervalued given its earnings power and growth



- Promoters (and subsequently management) and shareholders' interests are aligned. More importantly, promoters are fearless and constantly look to push the boundaries of growth and what the 'norm' is in its industry.
- Risk is diversified away by its focus on retail rather than corporate clients (a game changer in the Nepali banking sector)
- **SANIMA (Sanima Bank)**

We believe that Sanima Bank is one of those rare companies, which has demonstrated its ability to constantly grow and compound its earnings at an attractive rate. We like Sanima for a variety of reasons:

- It is a consistent leader in the industry in key categories such as balance sheet growth, NPL, profitability, return on equity and assets, among others.
- Very good and proven management
- International best practices adopted (maybe due to the owners who are primarily high net worth NRNs)

Sanima would fit perfectly in Saurubh Mukherjee's coffee can portfolio (companies that compound consistently by growing their topline and reinvesting their earnings at rates significantly above its cost). We bought this company three years ago and continue to add positions whenever valuations dip below our estimate of the intrinsic value.

- **BNT (Bottlers Nepal Terai, Coca Cola bottling plant)**

Bottler's Nepal is a stock that is largely ignored in the Nepali stock market. This can perhaps be due to its high nominal price per share (Rs. 6,500). Even amongst experienced investors (or rather speculators), there is a common misguided notion of the stock being 'expensive' based on its nominal value. We seek to take advantage of such misconceptions. We like BNT because

- It has a long runway for growth
- Growth in Nepal will come from BNT (Chitwan plant) since BNL (the Kathmandu plant) is constrained by physical space and BNT recently invested around Rs. 350 cr in a new plant to expand production significantly
- Powerful moat to protect its earning power over time
  - o Brand (Cocacola and its portfolio of brands are not going to go away any time soon. And consistent with their global and historical strategy, they continue to invest heavily in maintaining this brand. This level of investment simply cannot be matched by any other company in the foreseeable future)
  - o Distribution and nation-wide reach
  - o Product familiarity and habit

- **CBBL (Chhimek Laghubitta Bikas Bank)**

Chhimek is a leader in the micro-finance sector and has performed exceptionally well over the last decade with eye watering growth and very high return on its equity coupled with low NPL levels. While the company faces some headwinds with ever changing regulations and its



large size (an impediment to its high historical growth rate), we like CBBL for the following reasons:

- We expect them to maintain their market leadership
- Growth will be slower but high ROE and high reinvestment opportunity makes it an attractive holding for years to come
- Move from institutional source of funding to retail source of funding (through member deposits) which will lower cost of capital as well as lower funding risks.
- A lot of the issues plaguing the industry are getting resolved (multiple membership and loans by the same person, lack of a common industry database, etc.)
- Competition is consolidating
- Valuations are attractive given growth levels and consistently high ROE
- **MNBBL (Muktinath Bikash Bank) & GBBL (Garima Bikash Bank)**

Both Muktinath Bikash Bank and Garima Bikash Bank are leading national level development banks. As the industry has consolidated over the last couple of years due to a large number of mergers and acquisitions, we believe both these banks will be amongst the half a dozen development banks still standing. These two development banks will remain in our portfolio because:

- Growth is high and consistent (will continue as industry consolidates)
- There will always be 'room' for a development bank to serve customers ignored or not reached by the commercial banks
- Valuations are extremely low (single digit PE sometimes)
- Consistently high ROE and other performance indicators
- Low levels of NPA and both the banks seem to be very well run
- **SKBBL (Sana Kisaan Bittiya Bikaas Bank Ltd)**

SKBBL is a quazi-government wholesale microfinance bank which lends to other micro finance companies and captures a spread. Although we tend to dislike government run institutions due to its chronic underperformance, political meddling, and incompetent bureaucracy, SKBBL is an exception. They have some unique characteristics, which has resulted in them enjoying a very powerful moat.

- Their funding source is from the government at an extremely low cost (biggest moat)
- They are geared towards cooperatives and micro-finance companies focused on agriculture; a political priority for whichever party is in the government. And since there are not many institutions or mechanisms that have the ability to facilitate benefits for the agriculture sector, SKBBL ends up being a recipient of significant amounts of our national development budget, virtually guaranteeing its growth
- Since it lends to other lending institutions, the risk is extremely low

Valuations are a bit prohibitive at the moment but SKBBL has emerged as a new favorite of ours.

We have not sold a single share of most of these companies, some of which have been in our portfolio for 4 years now. In certain cases we trim positions to adjust its proportion in the overall portfolio and book some trading profits while lowering our average purchase price.



Bar any negative changes in the characteristics of these companies, we expect to hold on to these stocks forever.

### *GROUP B*

The second kinds of investments we make, lumped together in what we categorize under Group B, are arbitrage opportunities. These exist in various forms in the market, primarily in close-end mutual funds. Other forms of arbitrage opportunities we are exploring are companies going through mergers and acquisitions (specially if trading is allowed post announcement), conversion of share class (from promoter to public), and other pair trades. The companies under this group in our portfolio are:

- NMBHF1 (NMB Hybrid Fund -1, a mutual fund)
- LEMF (Laxmi Equity Mutual Fund)

While some of them may not be pure arbitrages, the risk/return profile or odds are sufficient for us to label this as arbitrage (minimum of 90% upside probability and 10% of downside probability and the downside loss limit less than 5%). Currently, only 2% of our portfolio is invested in these opportunities. The number varies over the year as the number and scale of opportunities appear.

### *GROUP C*

These are the stocks we are either currently in the process of buying or selling. A lot of these stocks get recycled as we revise or reaffirm our thesis. Stocks under this category are:

- HDL (Himalayan Distillery)
- OHL (Oriental Hotel Limited – Radisson Hotel)
- JFL (finance company)
- NRIC (Nepal Reinsurance Company)

### **Algorithmic & Systematic Investing**

At Snowball Capital, one of our core values is continuous learning. We are always seeking to challenge our most cherished ideas and beliefs and are constantly pushing the boundaries of our circle of competence.

In the process, we discover things about the markets as well as about ourselves. Seeped in a value-investing based philosophy, we have been studying and back testing various algorithmic and systematic investing strategies and have found some that have generated remarkable returns. For the first time, we will be investing a small portion of our funds (2% of the portfolio) in one of these algorithmic strategies. We are pleased to report that so far, this algorithm has outperformed the market by 394 basis points (3.94%), generating a return of 11.18% absolute return in the past 2.5 months. We have ten more months to see how this eventually pans out.

We will be live testing this strategy with similar amounts over the next 2 years before making it a more permanent and meaningful part of our portfolio. We are cautiously optimistic on this front.



### **Concluding remarks**

Over the last four years of investing in the Nepali equity markets, we have come to appreciate the role that luck and chance plays. We are also more mindful of a myriad of challenges, our shortcomings, and various biases that affect our decision-making.

Although we diligently track the macro economic conditions and monitor the market cycle, the valuation cycle, the liquidity and interest rate cycles, we are acutely aware that the future is impossible to predict. Unsurprisingly, we find it difficult to miss a chance to dismiss and ridicule the scores of technical analysis, chartist, and market timers who claim otherwise.

Howard Marks states: "We reach our conclusions, limited by the inadequacy of our foresight and influenced by our optimistic or pessimistic biases. And we learn from experience how hard it is to get the answer right. That leads me to end with a great bit of wisdom from Charlie Munger concerning the process of unlocking the mysteries of the markets: "It's not supposed to be easy. Anyone who finds it easy is stupid."

This couldn't be truer for our team as well. Our quest to unlocking the mysteries of the market is alive and well. Though we can never claim to have found the elixir, we rest on the shoulder of value investing giants and we trust that this process will yield attractive rates of returns over the years.

We are sincerely grateful for your continued trust in our ability to compound your valuable investment.

On to Greater Heights,

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Yurop Man Shrestha

Chairman,  
Snowball Capital