

# Bata India

28 May 2015

Reuters: BATA.BO; Bloomberg: BATA IN

## Worst Is Behind; Retain Buy

Following weak demand, supply chain problem and a declining market share in online channel, Bata India (BIL) reported a 0.8% fall in revenue to Rs4,913mn for 5QFY15. Based on our ground research, we have factored in its impact and revenue was only 1.8% below our estimate of Rs5,004mn but 9.8% below Bloomberg estimate. In the wake of operating deleverage and high fixed-cost structure, operating margin declined 374bps to 9.5%, leading to 28.8%/19.3% fall in EBITDA/PAT, respectively. Adjusted net profit of Rs318mn was significantly below Bloomberg estimate of Rs419mn, but marginally below our estimate of Rs344mn. Based on our online survey published on 22 May 2015, Bata is the largest selling brand with a ~11.8% market share in offline purchases, but because of weak presence online (~4.3% market share) its overall share reduced to ~10%. With SAP implementation issue getting resolved, low base, likely demand recovery in 2HFY16 and more than 200 store additions in FY15, BIL is expected to report 12.2%/19.5% revenue growth in FY16/FY17, respectively, despite losing market share to online players. Competitor Relaxo Footwear witnessed a 624bps improvement in gross margin in 4QFY15. With a better product mix, lower crude oil prices and operating leverage, we expect BIL to report 119bps/351bps improvement in gross margin /operating margin, respectively, which will drive net profit 32.8% to Rs2,903mn over FY15-FY17E, against a 16.7% decline in FY15, leading to a sharp re-rating. We believe the worst is behind BIL and its stock price already factored in all the concerns. We have retained our estimates and TP of Rs1,355 on BIL based on 30x/17.3x FY17E P/E and EV/EBITDA, respectively.

**Subdued revenue growth because of multiple problems:** BIL started implementing SAP at its outlets from November 2014 and by February 2015 SAP was implemented at most of its ~1,450 outlets. Based on our survey on e-commerce, BIL is losing market share in online business to competitor Red Tape (Mirza International) because of the latter's aggressive discounts. Following the problems stated above coupled with weak demand, revenue fell 0.8% to Rs4,913mn, only 1.8% below our estimate but 9.8% below Bloomberg estimate. As BIL is not aggressively discounting its products, it may impact sales in the near term but it will improve brand perception/revenue in the long run once discounts offered in online channel reduces. As the supply chain problem is resolved now, we expect BIL to report a 8% revenue growth and a 14.6% net profit growth in 1QFY16.

**Likely healthy 31.8% net profit CAGR over FY15-FY17E:** Low base, absence of supply side problems, more than 200 store addition in FY15, and likely demand recovery in 2HFY16, we expect BIL to report a 12.2% revenue growth in FY16 (on April to March FY15 revenue) and 19.5% in FY17. Gross margin improved 21bps to 54.6%, 20bps above our estimate in 5QFY15. Relaxo Footwear witnessed a 624bps improvement in gross margin in 4QFY15. With more than 50% of raw materials (~20%-23% of sales) linked to crude oil prices, the recent fall in crude oil prices is expected to result in a 88bps improvement in gross margin for BIL in FY16. Improving revenue growth, higher gross margin and operating leverage will improve operating margin by 351bps, and drive net profit by a 32.8% CAGR over FY15-FY17E to Rs2,903mn.

## BUY

**Sector:** Retail

**CMP:** Rs1,039

**Target Price:** Rs1,355

**Upside:** 30%

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### Key Data

Current Shares O/S (mn)	64.3
Mkt Cap (Rsbn/US\$bn)	66.8/1
52 Wk H / L (Rs)	1,496/975
Daily Vol. (3M NSE Avg.)	275,508

### Price Performance (%)

	1 M	6 M	1 Yr
Bata India	2.0	(17.0)	(11.1)
Nifty Index	0.6	(3.0)	13.7

Source: Bloomberg

Y/E December (Rsmn)	1QFY15	4QFY15	5QFY15	Chg. (YoY) %	Chg. (QoQ) %	CY13	FY15 (15M)	Chg. (%)
<b>Net sales</b>	<b>4,954</b>	<b>5,372</b>	<b>4,913</b>	<b>(0.8)</b>	<b>(8.5)</b>	<b>20,652</b>	<b>26,940</b>	<b>4.4</b>
Net raw material & purchases of finished goods	2,257	2,397	2,228	(1.3)	(7.0)	9,488	12,378	4.4
% of sales	45.6	44.6	45.4	-	-	45.9	45.9	-
Rental expenses	692	801	783	13.2	(2.2)	2,620	3,742	14.3
% of sales	14.0	14.9	15.9	-	-	12.7	13.9	-
Other expenses	1,346	1,560	1,433	6.4	(8.1)	5,325	7,470	12.2
% of sales	27.2	29.0	29.2	-	-	25.8	27.7	-
<b>Operating profit</b>	<b>658</b>	<b>614</b>	<b>469</b>	<b>(28.8)</b>	<b>(23.7)</b>	<b>3,218</b>	<b>3,349</b>	<b>(16.8)</b>
<b>OPM (%)</b>	<b>13.3</b>	<b>11.4</b>	<b>9.5</b>	<b>-</b>	<b>-</b>	<b>15.6</b>	<b>12.4</b>	<b>-</b>
Interest costs	2.8	5.6	3.4	23.6	(38.8)	13	18	8.1
Depreciation	136	185	161	18.4	(12.8)	592	792	7.1
Other income	73	75	93	26.6	23.8	313	432	10.3
Extra-ordinary income	-	-	332	-	-	(101)	315	(350.4)
<b>PBT</b>	<b>592</b>	<b>499</b>	<b>729</b>	<b>23.1</b>	<b>46.2</b>	<b>2,826</b>	<b>3,287</b>	<b>(7.0)</b>
Provision for tax	198	149	145	(27.1)	(3.0)	919	975	(15.1)
<b>Reported PAT</b>	<b>394</b>	<b>349</b>	<b>584</b>	<b>48.3</b>	<b>67.2</b>	<b>1,907</b>	<b>2,312</b>	<b>(3.0)</b>
<b>Adjusted PAT</b>	<b>394</b>	<b>349</b>	<b>318</b>	<b>(19.3)</b>	<b>(9.0)</b>	<b>1,974</b>	<b>2,057</b>	<b>(16.6)</b>
<b>NPM (%)</b>	<b>8.0</b>	<b>6.5</b>	<b>6.5</b>	<b>-</b>	<b>-</b>	<b>9.6</b>	<b>7.6</b>	<b>-</b>

Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 1: Financial summary

Y/E December (Rsmn)	CY11	CY12	CY13	FY15 (15M)	FY16E	FY17E
Revenue	15,425	18,425	20,652	26,940	24,781	29,618
YoY (%)	22.6	19.4	12.1	4.4	15.0	19.5
EBITDA	2,305	2,744	3,220	3,349	3,453	4,720
EBITDA margin (%)	14.9	14.9	15.6	12.4	13.9	15.9
Reported PAT	2,258	1,716	1,909	2,312	2,078	2,903
Adj. PAT	1,421	1,716	1,976	2,057	2,078	2,903
EPS (Rs)	22.1	26.7	30.7	32.0	32.3	45.2
YoY (%)	49.0	20.8	15.1	(16.7)	26.3	39.7
RoE (%)	29.2	26.9	25.7	17.7	19.1	23.1
RoCE (%)	29.7	26.1	25.3	18.1	19.1	23.2
RoIC (%)	40.6	32.9	35.2	23.3	26.3	37.4
P/E (x)	47.0	38.9	33.8	40.6	32.1	23.0
Price/sales (x)	4.3	3.6	3.2	3.1	2.7	2.3
EV/ EBITDA (x)	28.5	23.7	19.9	24.1	18.2	13.0

Note: FY15 is for 15 months as the company changed its year-end from Decemeber to March. To calculate the growth rate, we have used annualised numbers

Source: Company, Nirmal Bang Institutional Equities Research

### Likely 17.2% revenue CAGR over FY15-FY17E

Most of the outlets stated that their sales can increase 2%-3% if the supply problem, particularly in premium brands like Hush Puppies, is resolved, and can result in higher same-store sale growth or SSG, which we believe is taken care of by installation of new SAP system. However, it will take some time for store managers to understand the usage of SAP. BIL is providing training to store managers to improve awareness about the system, the benefit of which will be visible in 2HFY16. BIL added ~200/38 gross stores in 12MFY15/5QFY15, respectively. BIL set up more than 150 net stores in FY15 versus 30 in CY13, which can provide ~6% revenue growth compared to 2% earlier. Its revenue from e-commerce vertical, though on a small base of ~1% of sales, is growing at a 100% CAGR. In order to penetrate smaller towns at a low cost, BIL plans to set up ~100 franchisee stores in the next two years, which are expected to add 2%-4% to revenue growth rate. Its SSG, which was negative in 5QFY15, has the potential to touch double digits in two years. Considering these facts, we expect its revenue to grow by a healthy 17.2% CAGR over FY15-FY17E.

### Nature of problem with SAP system

BIL installed a new SAP system at its ~1,450 stores during November 2014 to February 2015. Post installation of the new SAP system, BIL couldn't connect many of its stores with its warehouse and as a result, these stores didn't get supply of products for a few days. The problem persisted till February 2015. It led to a 20.9% increase in inventory against a 4.4% rise in sales. Inventory days increased by 14 to 134 in FY15 (March-end) from 120 days in CY14 (December-end). However, as the problem is resolved now, revenue is expected to touch its normal level from 1QFY16.

## Exhibit 2: Working capital analysis

(Rsmn) consolidated	CY13	1HFY15	FY15	YoY (%)	FY15 over 1HFY15 (%)
Revenue	20,652	11,175	26,940	4.4	(3.6)
<b>Inventory</b>	<b>5,827</b>	<b>5,757</b>	<b>7,047</b>	<b>20.9</b>	<b>22.4</b>
<b>Inventory days</b>	<b>120</b>	<b>90</b>	<b>134</b>	-	-
Sundry debtors	509	646	584	14.7	(9.6)
Sundry debtor days	9	9	10	-	-
Sundry creditors	3,654	4,062	4,545	24.4	11.9
Sundry creditor days	75	64	87	-	-
Net working capital	2,682	2,341	3,086	15.1	31.8
<b>Net working capital days</b>	<b>54</b>	<b>35</b>	<b>57</b>	-	-
Ex-cash current assets	10,419	11,043	11,900	14.2	7.8
As % of annualised sales	50.5	41.0	55.2	-	-
Current liabilities	5,421	5,365	6,153	13.5	14.7
As % of annualised sales	26.3	19.9	28.5	-	-
<b>Ex-cash net current assets</b>	<b>2,440</b>	<b>2,727</b>	<b>3,648</b>	<b>49.5</b>	<b>33.8</b>
<b>As % of annualised sales</b>	<b>11.8</b>	<b>10.1</b>	<b>16.9</b>	-	-

Source: Company, Nirmal Bang Institutional Equities Research

## Likely savings in raw material costs

Costs of raw materials and traded goods together accounted for 46% of the company's CY13 sales. Raw materials used for in-house footwear manufacture accounted for 16% of net sales, while traded goods accounted for 30% of sales. In respect of products manufactured in-house, the costs of more than 50% of raw materials consumed like synthetic textiles (7.6% of raw material consumption), chemicals (18.3%) and a significant portion of other raw materials (34.6%) are linked to crude oil prices. With the costs of more than 50% of raw materials consumed and traded goods (accounting for ~20%-23% of sales) linked to crude oil prices, a 37% fall in Indian basket of crude oil will improve margins of the company. As the company has inventory of 190 days (on cost basis), it will take seven months to witness the benefit of lower crude oil prices.

### Exhibit 3: Scenario analysis of improvement in gross margin

(Rsmn)	Current		1.0% increase in		1.5% increase in		2.0% increase in	
	estimates		gross margin		gross margin		gross margin	
	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E
Gross margin (%)	54.9	55.2	55.9	56.2	56.4	56.7	56.9	57.2
EBITDA (%)	13.9	15.9	14.9	16.9	15.4	17.4	15.9	17.9
EBITDA	3,453	4,720	3,701	5,017	3,825	5,165	3,949	5,313
PAT	2,078	2,903	2,245	3,103	2,329	3,203	2,413	3,303
EPS (Rs)	32.3	45.2	34.94	48.29	36.24	49.84	37.54	51.40
Change (%)	-	-	8.0	6.9	12.1	10.3	16.1	13.8
P/E (x)	32.1	23.0	29.7	21.5	28.7	20.8	27.7	20.2

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 4: Raw material cost break-up

Raw material details	Rsmn	(%)
Leather	555	16.6
Rubber	208	6.2
<b>Synthetic textile</b>	<b>256</b>	<b>7.6</b>
<b>Chemicals</b>	<b>614</b>	<b>18.3</b>
Packaging	210	6.3
Job charges	344	10.3
<b>Other materials</b>	<b>1,159</b>	<b>34.6</b>
Total	3,346	100

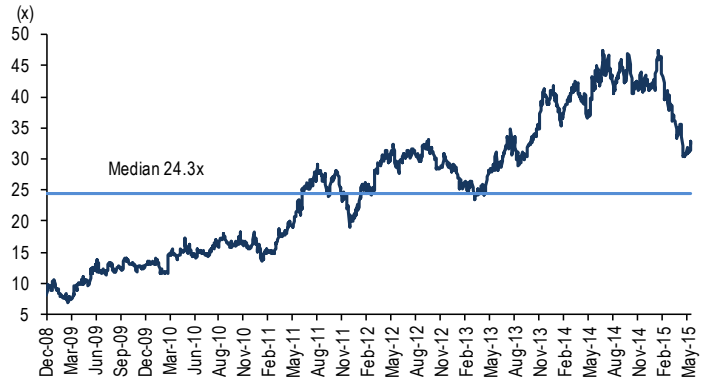
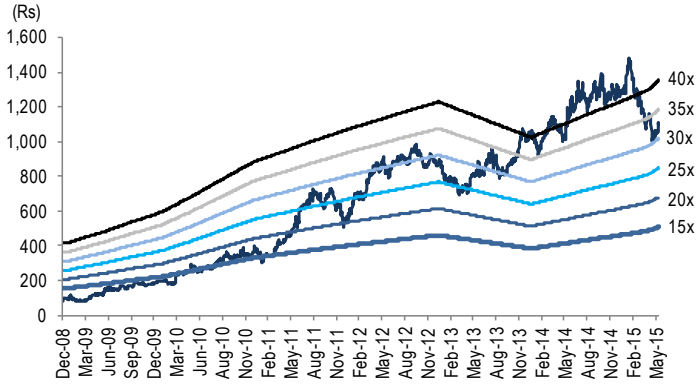
Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 5: Our estimates versus actual performance

(Rsmn)	1QFY15	4QFY15	5QFY15	YoY (%)	QoQ (%)	5QFY15E	Dev. (%)	5QFY15 BBE	Dev. (%)
Revenue	4,954	5,372	4,913	(0.8)	(8.5)	5,004	(1.8)	5,447	(9.8)
EBITDA	658	614	469	(28.8)	(23.7)	578	(18.9)	698	(32.9)
EBITDA (%)	13.3	11.4	9.5	(374)bps	(189)bps	11.6	(201)bps	12.8	(328)bps
Adjusted PAT	394	349	318	(19.3)	(9.0)	344	(7.4)	419	(24.1)

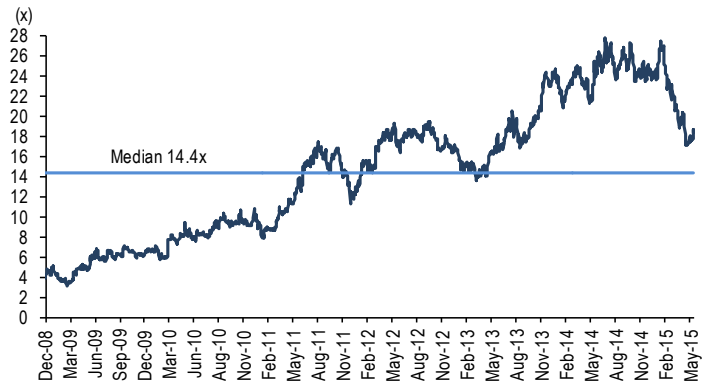
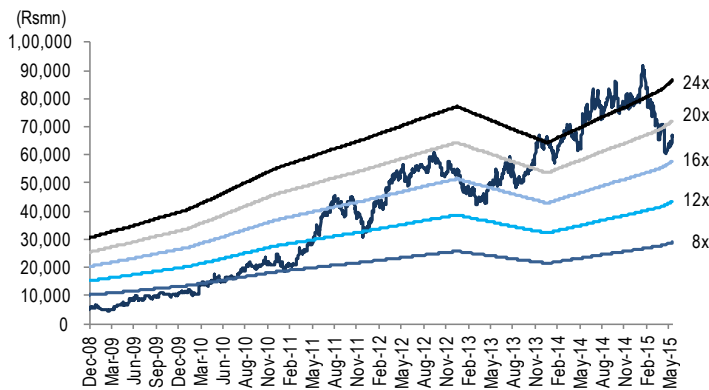
Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 6: One-year forward P/E



Source: Nirmal Bang Institutional Equities Research

## Exhibit 7: One-year forward EV/EBITDA



Source: Nirmal Bang Institutional Equities Research

## Financials (standalone)

### Exhibit 8: Income statement

Y/E December (Rsmn)	CY11	CY12	CY13	FY15(15M)	FY16E	FY17E
Net sales	15,425	18,425	20,652	26,940	24,781	29,618
Growth (%)	22.6	19.4	12.1	4.4	15.0	19.5
Raw material costs	7,265	8,680	9,488	12,378	11,168	13,258
Staff costs	1,859	1,959	2,133	3,119	2,869	3,199
Rentals	1,453	2,154	2,619	3,743	3,469	3,998
Freight costs	405	407	429	585	545	592
Commission	416	565	642	875	818	889
Others	1,723	1,915	2,121	2,891	2,458	2,962
Total expenditure	13,121	15,680	17,432	23,591	21,328	24,898
EBITDA	2,305	2,744	3,220	3,349	3,453	4,720
Growth (%)	37.3	19.1	17.3	(16.8)	28.9	36.7
EBITDA margin (%)	14.9	14.9	15.6	12.4	13.9	15.9
Other income	216	300	315	432	360	385
Extra-ordinary items	1,094	-	(101)	315	-	-
Interest costs	9	10	13	18	14	15
Gross profit	3,605	3,033	3,421	4,079	3,799	5,091
Growth (%)	105.4	(15.9)	12.8	(4.6)	16.4	34.0
Depreciation	411	514	592	792	721	790
Profit before tax	3,194	2,520	2,829	3,287	3,078	4,301
Growth (%)	123.4	(21.1)	12.3	(7.0)	17.1	39.7
Tax	936	804	920	975	1,000	1,398
Effective tax rate (%)	29.3	31.9	32.5	29.7	32.5	32.5
Reported Net profit	2,258	1,716	1,909	2,312	2,078	2,903
Growth (%)	136.8	(24.0)	11.2	(3.1)	12.3	39.7
Extra-ordinary items	838	-	(67)	255	-	-
Adjusted net profit	1,421	1,716	1,976	2,057	2,078	2,903
Growth (%)	49.0	20.8	15.1	(16.7)	26.3	39.7

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 10: Balance sheet

Y/E December (Rsmn)	CY11	CY12	CY13	FY15(15M)	FY16E	FY17E
Equity	643	643	643	643	643	643
Reserves	5,100	6,361	7,756	9,579	10,944	12,873
Net worth	5,743	7,003	8,399	10,221	11,587	13,515
Short-term loans	194	267	-	-	-	-
Long-term loans	-	-	-	-	-	-
Total loans	194	267	-	-	-	-
Deferred tax liability	(342)	(444)	(681)	(876)	(845)	(802)
<b>Liabilities</b>	<b>5,595</b>	<b>6,827</b>	<b>7,718</b>	<b>9,345</b>	<b>10,742</b>	<b>12,713</b>
Gross block	5,003	5,611	6,035	7,728	8,893	9,693
Depreciation	2,813	3,198	3,552	4,345	5,066	5,856
Net block	2,190	2,413	2,483	3,383	3,827	3,837
Capital work-in-progress	81	181	237	166	-	-
Long-term Investments	49	49	-	50	50	50
Inventories	3,913	4,621	5,827	7,047	6,517	7,608
Debtors	314	449	509	584	629	752
Cash	1,229	1,871	2,558	2,100	3,841	5,308
Other current assets	1,124	1,276	1,526	2,169	1,859	2,221
Total current assets	6,581	8,218	10,419	11,900	12,846	15,889
Creditors	2,346	2,941	3,654	4,545	4,147	4,841
Other current liabilities	959	1,093	1,767	1,608	1,834	2,221
Total current liabilities	3,305	4,034	5,421	6,153	5,981	7,063
Net current assets	3,276	4,184	4,998	5,747	6,865	8,826
<b>Total assets</b>	<b>5,595</b>	<b>6,827</b>	<b>7,718</b>	<b>9,345</b>	<b>10,742</b>	<b>12,713</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 9: Cash flow

Y/E December (Rsmn)	CY11	CY12	CY13	FY15(15M)	FY16E	FY17E
EBIT	1,894	2,230	2,627	2,557	2,732	3,930
(Inc.)/dec. in working capital	(1,300)	(267)	(127)	(1,207)	624	(495)
<b>Cash flow from operations</b>	<b>594</b>	<b>1,964</b>	<b>2,500</b>	<b>1,350</b>	<b>3,356</b>	<b>3,436</b>
Other income	216	300	315	432	360	385
Depreciation	411	514	592	792	721	790
Deferred liabilities	(31)	(101)	(237)	(195)	31	43
Interest paid (-)	(9)	(10)	(13)	(18)	(14)	(15)
Tax paid (-)	(680)	(804)	(920)	(975)	(1,000)	(1,398)
Dividend paid (-)	(447)	(448)	(489)	(489)	(712)	(975)
Extraordinary items	-	-	-	-	-	-
<b>Net cash from operations</b>	<b>54</b>	<b>1,414</b>	<b>1,749</b>	<b>897</b>	<b>2,742</b>	<b>2,267</b>
Capital expenditure (-)	(1,198)	(838)	(718)	(1,621)	(1,000)	(800)
<b>Net cash after capex</b>	<b>(1,144)</b>	<b>576</b>	<b>1,031</b>	<b>(724)</b>	<b>1,742</b>	<b>1,467</b>
Inc./(dec.) in short-term borrowing	56	73	(267)	-	-	-
Inc./(dec.) in borrowings	-	-	-	-	-	-
(Inc.)/dec. in investments	124	0	49	(50)	-	-
<b>Cash from financial activities</b>	<b>180</b>	<b>73</b>	<b>(219)</b>	<b>(50)</b>	<b>-</b>	<b>-</b>
Others / extraordinary income	838	(8)	(126)	315	(0)	0
Opening cash	1,356	1,229	1,871	2,558	2,100	3,841
Closing cash	1,229	1,871	2,558	2,100	3,841	5,308
Change in cash	(126)	642	686	(458)	1,742	1,467

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 11: Key ratios

Y/E December	CY11	CY12	CY13	FY15(15M)	FY16E	FY17E
<b>Per share (Rs)</b>						
EPS	22.1	26.7	30.7	25.6	32.3	45.2
Book value	89.4	109.0	130.7	159.1	180.3	210.3
<b>Valuation (x)</b>						
P/E	47.0	38.9	33.8	40.6	32.1	23.0
P/sales	4.3	3.6	3.2	3.1	2.7	2.3
P/BV	11.6	9.5	7.9	6.5	5.8	4.9
EV/EBITDA	28.5	23.7	19.9	24.1	18.2	13.0
EV/sales	4.3	3.5	3.1	3.0	2.5	2.1
<b>Return ratios (%)</b>						
RoIC	40.6	32.9	35.2	23.3	26.3	37.4
RoCE	29.7	26.1	25.3	18.1	19.1	23.2
RoE	29.2	26.9	25.7	17.7	19.1	23.1
<b>Margins (%)</b>						
EBITDA margin	14.9	14.9	15.6	12.4	13.9	15.9
PBIT margin	12.3	12.1	12.7	9.5	11.0	13.3
PBT margin	20.7	13.7	13.7	12.2	12.4	14.5
PAT margin	9.2	9.3	9.6	7.6	8.4	9.8
<b>Turnover ratio</b>						
Asset turnover ratio (x)	2.8	2.7	2.7	2.3	2.3	2.3
Avg. inventory period (days)	107	106	120	134	110	110
Avg. collection period (days)	7	9	9	10	9	9
Avg. payment period (days)	64	68	75	87	70	70
<b>Solvency ratios (x)</b>						
Debt-equity	0.0	0.0	-	-	-	-
Interest coverage	217.6	216.1	202.3	145.6	195.1	262.0
<b>Growth (%)</b>						
Sales	22.6	19.4	12.1	4.4	15.0	19.5
EBITDA	37.3	19.1	17.3	(16.8)	28.9	36.7
PAT	49.0	20.8	15.1	(16.7)	26.3	39.7

Source: Company, Nirmal Bang Institutional Equities Research

## Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 September 2011	Buy	639	817
1 November 2011	Buy	725	838
10 January 2012	Buy	550	838
1 March 2012	Buy	700	838
20 March 2012	Buy	725	838
20 April 2012	Buy	844	1,008
26 April 2012	Buy	855	1,008
2 May 2012	Buy	878	1,008
22 June 2012	Buy	847	1,008
10 July 2012	Buy	872	1,008
27 July 2012	Hold	896	1,008
14 August 2012	Hold	914	1,008
4 October 2012	Hold	982	1,008
1 November 2012	Sell	854	786
4 February 2013	Buy	784	1,000
27 February 2013	Buy	758	1,000
26 April 2013	Buy	704	865
8 May 2013	Hold	786	865
14 May 2013	Hold	799	865
5 June 2013	Hold	863	865
26 July 2013	Buy	876	1,064
29 July 2013	Buy	908	1,064
7 October 2013	Buy	862	1,064
31 October 2013	Buy	888	1,064
20 December 2013	Buy	1,010	1,310
7 January 2014	Buy	1,026	1,310
22 January 2014	Buy	974	1,310
13 February 2014	Buy	1,000	1,310
26 March 2014	Buy	1,130	1,310
30 March 2014	Buy	1,076	1,310
2 May 2014	Buy	1,068	1,245
22 May 2014	Buy	1,091	1,255
4 July 2014	Buy	1,343	1,592
6 August 2014	Buy	1,253	1,507
25 August 2014	Buy	1,252	1,507
10 October 2014	Buy	1,337	1,507
7 November 2014	Buy	1,274	1,502
12 December 2014	Buy	1,312	1,502
12 February 2015	Buy	1,291	1,499
13 April 2015	Buy	1,158	1,499
22 May 2015	Buy	1,121	1,355
28 May 2015	Buy	1,039	1,355

## Disclaimer

### Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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