Stock Idea

Sector: Logistics March 22, 2021

Transport Corporation of India Limited

Delivering a strong growth story

Sharekhan
by BNP PARIBAS

Powered by Sharekhan's 3R Research Philosophy

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Transport Corporation of India Limited

Delivering a strong growth story

Logistics	Sharekhan code: TCI	Initiating Coverage

Summary

- We initiate coverage on Transport Corporation of India Limited (TCI) with a Buy and SOTP-based price target of Rs. 354.
- TCI is well-set to benefit from strong growth outlook for logistics given its six-decade track record in offering integrated multi-modal transport and supply chain solutions.
- Rising share in LTL freight and value-addition in FTL freight, besides a revival in auto and non-auto SCM and expansion of seaways biz would help PAT clock a 15% CAGR over FY2021-FY2023.
- GST-led tailwinds, impact of COVID-19, government thrust on AtmaNirbhar Bharat and global supply chain re-alignments would be key growth drivers.

3R MATRIX	+	=	-
Right Sector (RS)		✓	
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

Reco/View	
Reco:	**Buy**
CMP:	**Rs. 243**
Price Target:	**Rs. 354**

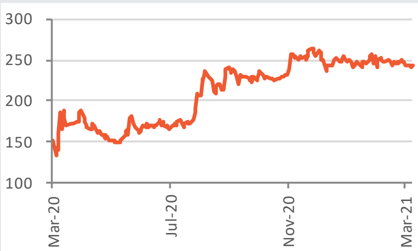
Company details

Market cap:	Rs. 1,871 cr
52-week high/low:	Rs. 279/194
NSE volume: (No of shares)	0.6 lakh
BSE code:	532349
NSE code:	TCI
Free float: (No of shares)	2.6 cr

Shareholding (%)

Promoters	66.8
FII	1.5
DII	12.4
Others	19.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.0	-0.3	3.2	60.3
Relative to Sensex	-3.2	-9.8	-27.9	-6.3

Sharekhan Research, Bloomberg

Transport Corporation of India Limited (TCI) has over six decades of experience in the logistics industry with an integrated multi-modal and supply chain solutions capabilities. The company's strong presence in roads (4,500 trucks including 120 owned, 800 branches pan-India, only national player to provide both LTL and FTL transportation), rail (through its subsidiary with industry leader Concor, TCI Concor), and Seaways (six owned ships catering to both eastern and western coastal lines) gives it a distinctive competitive advantage to capture the strong growth potential of the logistics industry. All its three key operating segments viz. Freight (52%/20% FY2020 revenue/ EBITDA share), Supply Chain Management (34%/37% revenue/EBITDA), and Seaways (12%/42% revenue/EBITDA share) are poised for growth going ahead. Higher share of LTL revenue (40%+ over two years from current 33%, has 2x+ OPM vis-à-vis FTL) along with increasing value-added services in FTL is expected to drive freight revenue and operating profit at 13%/20.7% CAGR over FY2021E-FY2023E. Strong rebound in the auto sector during FY2021, positive growth outlook for the auto sector, and high growth in non-auto (especially e-commerce and FMCG) are expected to drive the SCM segment (~80% auto exposure, 12msf boxed warehouses with ~17% owned), which is slated to grow its revenue and operating profit by 15.3%/18.5% CAGR over FY2021E-FY2023E). Higher capacity utilisation along with addition of one more ship in FY2022 (eyeing second hand ship of 9-10 years old with 800+ container capacity at a budget of Rs. 60 crore-70 crore) would drive the seaways segment (revenue/operating profit to grow at a 12.5% CAGR over FY2021E-FY2023E). Overall, healthy double-digit revenue growth across its key verticals along with margin expansion levers in freight and SCM business is expected to drive its consolidated revenue/operating profit/PAT at a CAGR of 13.9%/18.3%/15.4% over FY2021E-FY2023E. TCI is expected to benefit from the logistics sector's growth tailwinds led by GST (business moving towards the organised sector), impact of COVID-19 (increased outsourcing of logistics services to prevent supply chain disruptions in future), government thrust on Atmanirbhar Bharat (PLI incentives to increase domestic manufacturing in turn leading to increased logistics needs), and global supply chain re-alignments (India expected to be one of the key beneficiaries of China +1 strategy for global manufacturers). We expect TCI to be on a long-term growth trajectory, driven by positive sectoral fundamentals and its inherent strengths and capabilities.

Firing all cylinders

TCI has been able to ramp up its multi-modal capabilities over FY2016-FY2020. The company's freight business (revenue/operating profit grew at a 10.5%/17.1% CAGR) growth was led by increased LTL revenue share from 25% to 33% and is further expected to rise to 40%+ by FY2023E. The SCM business grew (revenue/operating profit grew at 11%/9.1% CAGR) despite getting impacted in FY2020 due to auto slowdown; we see the scenario now reversing. Seaways has grown handsomely at a 27.6%/33.6% CAGR in revenue/operating profit with addition of a ship at almost every two years (which will be repeated in FY2022 with addition of a ship). Operating cash flow (OCF) of the company has risen by 2.3x from Rs. 109 crore in FY2016 to Rs. 252 crore in FY2020. We expect TCI to generate almost Rs. 240 crore average OCF per annum over FY2021-FY2023. TCI has also lowered its net debt from Rs. 343 crore in FY2020 to almost Rs. 270 crore during 9MFY2021. Capex of Rs. 300 crore-350 crore during FY2022-FY2023 can be funded through internal accruals, keeping net debt/equity low at just 0.2x by FY2023E.

Our Call

Valuation – Initiate with Buy assigning a SOTP-based PT of Rs. 354: We have valued TCI on SOTP basis, assigning different valuation multiple for each segment considering the growth outlook, OPM, and RoCEs. We value its freight business at 6x its EV/EBITDA on FY2023E earnings (discount to VRL Logistics owing to lower LTL presence leading to lower OPM and RoCE profile). We value SCM at 10x its EV/EBITDA on FY2023E earnings (discount to Mahindra Logistics, which has higher OPM and RoCE profile). We value Seaways at 7x its EV/EBITDA, owing to its healthy growth and RoCE profile. The JV transystem is valued at 1x its investment. On aggregate basis, we have arrived at an SOTP-based price target (PT) of Rs. 354. We initiate our coverage on the stock with a Buy rating.

Key risk

Weak macroeconomic environment and auto industry outlook affect business growth of the company.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	2,753.6	2,717.8	2,702.7	3,158.6	3,507.6
OPM (%)	9.1	8.9	8.8	9.1	9.5
Adjusted PAT	145.1	152.2	144.7	166.6	192.7
% Y-o-Y growth	*17.8*	*4.9*	*(4.9)*	*15.1*	*15.7*
Adjusted EPS (Rs.)	18.9	19.8	18.8	21.7	25.1
P/E (x)	12.8	12.3	12.9	11.2	9.7
P/B (x)	2.1	1.8	1.6	1.4	1.3
EV/EBITDA (x)	8.6	8.9	9.0	7.5	6.4
RoNW (%)	17.5	15.9	13.3	13.7	14.0
RoCE (%)	10.5	9.7	8.9	9.5	10.2

Source: Company, Sharekhan estimates

Executive Summary

3R Research Positioning Summary

- **Right Sector:**
  Highly fragmented sector with hugh unorganized market provide immense growth potential for organized players.
- **Right Quality:**
  Over six decades of experience with multi-modal and supply chain capabilities.
- **Right Valuation:**
  Discounted valuation multiples in key operating segments vis-à-vis industry peers.

Valuation and return potential

- **Price Target:** We value the company with SOTP based price target assigning valuation multiples considering growth and return profiles.
- **Reasonable valuation:** Assigning discounted valuation multiples for freight and SCM business vis-à-vis industry peers.

Catalysts

Long-term triggers

- Indian logistics sector to remain key focus area as government envisages to lower logistics costs as a % of GDP bringing efficiencies.
- Sectoral growth tailwinds led by GST, covid impact, Atmanirbhar Bharat, National Logistics policy, global supply realignments etc.

Medium Term Triggers

- Strong growth potential across freight, SCM and seaways divisions led by multiple triggers.
- Covid impact has lead to increase in logistics outsourcing to prevent supply chain disruptions.

Key Risks

Weak macros, weakness in auto sector, increase in competitive intensity.

Earnings and Balance sheet highlights

- **Strong earnings:** Net earnings grew at a 15% CAGR over FY2016-FY2020.
- **Operating Cash-flow generation:** OCF of the company has risen by 2.3x from Rs. 109 crore in FY2016 to Rs. 252 crore in FY2020.
- **Strong balance sheet:** net debt reduced from Rs. 343 crore in FY2020 to almost Rs. 270 crore during 9MFY2021;
- **Best working capital cycle:** One of the lowest working capital cycles in the industry.

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Why we like space – The logistics industry has the potential to grow multi-fold led by reforms such as GST, E-way bill, National Logistics Policy, Make in India to name a few.

India's organised logistics industry has a huge growth potential owing to highly fragmented and un-organised market dominance. Players having multi-modal and supply chain capabilities are expected to be at the forefront to capture the high-growth potential of the industry.

Indian Logistics Industry

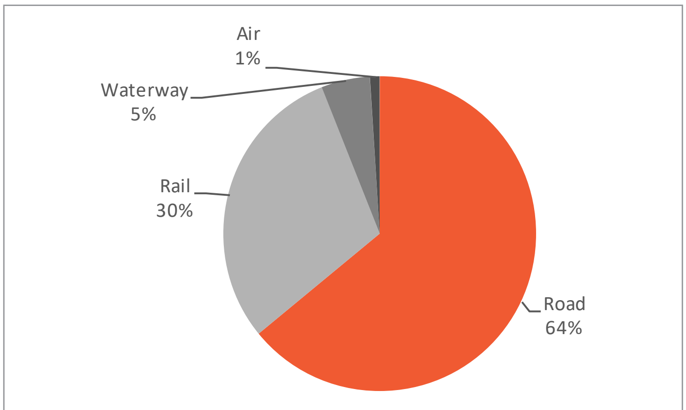
Indian Logistics – Highly fragmented

India's supply chain and logistics sector are one of the largest globally, with a logistics industry of $215 billion and reporting a CAGR of 10.5%. It is highly fragmented with a large number of unorganised players. However, despite its size and criticality to economic growth, India's supply chain is marred by an unbalanced logistics modal mix, high indirect costs, poor infrastructure, fragmented networks, and lack of technology adoption. The sector has the potential to grow multifold. While there is a need for the highly fragmented Indian logistics market to get more organised, there is also a need to reduce logistics cost to 10% by 2022 from about 14% now. Only 10%-15% of the $215-billion Indian logistics market is owned by organised players.The logistics sector in India has been witnessing strong growth in the past few years due to some revolutionary reforms such as the introduction of GST, E-way bill, eased foreign direct investment (FDI) norms; renewed government infrastructure spending; and greater access to global markets. Growth in manufacturing envisioned through the Make in India initiative is projected to demand high levels of logistics efficiency and newer and bigger warehouses.

Multi-modal mix of logistics transportation

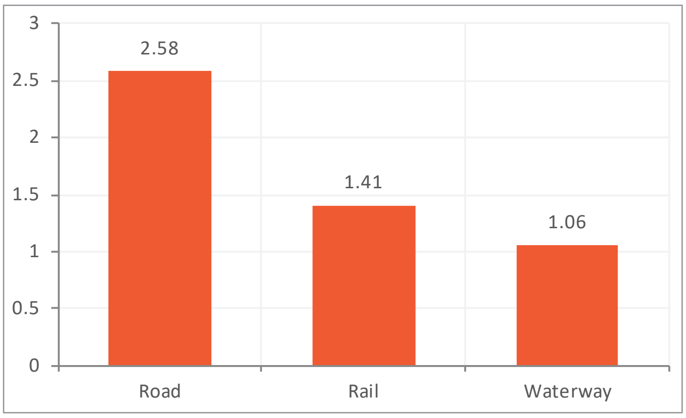
A modal mix heavily skewed towards transportation by road is at the root of the unwarranted logistics costs. Transportation represents approximately 40% of logistics costs, which amount to 6% of GDP. Transportation by road makes up the lion's share of this cost, at about 64%, followed by rail at 30% and waterway and air transport at 5% and 1%, respectively. This heavy dependence on road networks, combined with poor transportation infrastructure, makes transportation costs balloon. Currently, per-tonne-km cost of transportation via the road network is almost double that of rail and waterways at Rs. 2.58/tonne-km, compared to Rs. 1.41/tonne-km for rail and Rs. 1.06/tonne-km for waterways. India's rail and sea network are highly under-utilised due to lack of supporting infrastructure.

Transportation mode mix



Source: Industry, Sharekhan Research

Per tonne cost of transportation (Rs./tonne-km)

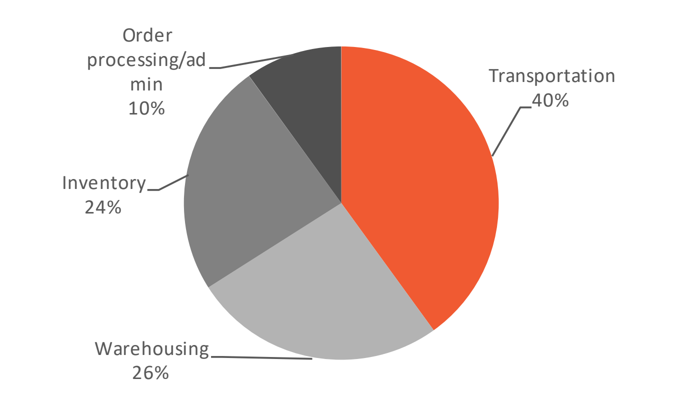


Source: Industry, Sharekhan Research

India's high logistics cost as a % of GDP

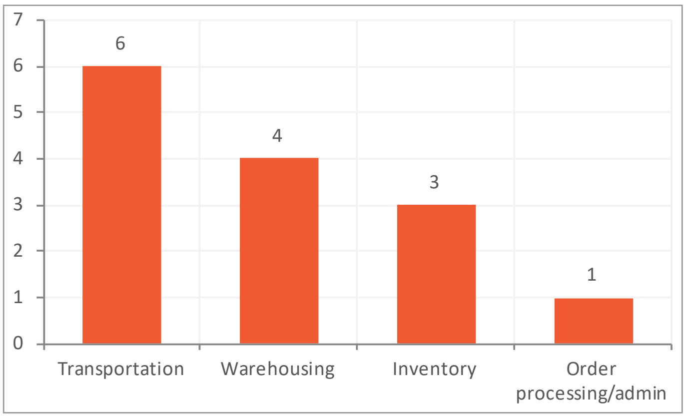
Logistics costs in the Indian supply chain amount to almost $400 billion, or 14% of GDP. A comparison with global peers shows that logistics costs amount to 8%-10% of GDP in the US and Europe and 9% in China. The global average is close to 8% of GDP. Other South-Asian countries, such as Thailand and Vietnam, also have high logistics costs. These countries' costs reach 14% and 16%-17% of GDP, respectively.

Logistics cost mix for Indian SC



Source: Industry, Sharekhan Research

Logistics cost mix as a % of GDP



Source: Industry, Sharekhan Research

Vision to reduce logistics cost to 7%-8% of GDP

India will aim to reduce its logistics cost to 7%-8% of GDP. To achieve this, India will optimise the logistics modal mix to global benchmarks, with roads constituting 25%-30%, railways comprising 50%-55% and waterways accounting for 20%-25% of transportation modes. Transportation infrastructure will be efficient and fully utilised. India will also reduce indirect or hidden costs to 20%-25% through efficient inventory management and monitoring. In addition, she will optimise turnaround time to 700-800 kilometers per day, with the target of increasing truck trips by 50%. It will also aim to increase the throughput of the road network by improving the quality of roads and increasing the proportion of national highways in the total road network. India will aim to increase the average speed of freight trains to 50 kmph and increase loading capacity and connectivity to industry. In warehousing, cold chain storage infrastructure will be expanded to bridge the gap between required and available capacity and aim to reduce agricultural produce wastage to less than 10%. The private-public partnership (PPP) models will be encouraged to ensure faster progress in optimising the logistics and warehousing networks. India will work towards digitisation of more than 90% of data and strategic implementation of technologies such as artificial intelligence, blockchain, and IoT. The supply chain will look towards machine learning and algorithm development for optimised demand planning and forecasting to minimize inventory costs and eliminate wastage.

Opportunities for the Indian logistics industry

Supply chains getting revamped: India's supply chains will go through huge transformations in the next few years as the impact of COVID-19 continues to challenge demand and supply frameworks. Due to widespread disruptions, supply chains are either broken or severely affected. As ongoing supply-side issues start getting addressed, there will be demand contraction in several industry segments creating further disorder. Organisations would need to adapt to this new reality to build supply-chain resilience. The first and most important change will be the rise of domestic sourcing to make supply chains more local. Despite being a large exporter of pharmaceuticals, India is still largely dependent on China for APIs. This will push the establishment of global value chains in India to not only serve domestic but also export markets.

Large companies and MSMEs to receive a boost under Atmanirbhar Bharat Abhiyan: Global brands will be likely to de-risk their supply chains and this will bring some shift of manufacturing to new locations, of which India will surely benefit. The Make in India initiative will receive the required boost as companies look at alternatives to their current supply chains. MSMEs will gear up in the new normal, with government incentives and support, through the recently announced economic stimulus package. Simplification of systems and processes and a national market will enable them to scale up.

Growth of Multimodal Logistics: As cargo moves nationally, crisscrossing multiple states, multimodal transport using a combination of rail, sea, and road will gain dominance. Typically, multimodal transport's first and last-mile is mostly local with a shorter lead, thereby reducing inter-state movements and the number of touch points for cargo. To prevent the spread of the virus, it would be desirable to reduce the number of touch points any product goes through in the entire supply chain, from production to handling till the doorstep of businesses and homes.

Adoption of automation and modern handling systems: Automation in handling systems including palletisation of cargo, conveyor systems, robotics, drones, and drop boxes, amongst others, will see an accelerated trend. These are critical to achieve the speed, efficiency, and resiliency needed to meet both demands of today's complex markets and to keep the lines of supply moving and open both in times of normalcy and time of crisis. A rapid shift towards omni-channel procurement would be visible. Reducing the spread of the virus would also mean an increase in phytosanitary standards in handling of food grade products.

New Demand of Essentials: The pandemic has clearly shifted consumer preferences to essentials which include a host of sanitisation items. Demand for these items will lead to more manufacturing across India and globally. In India, it is roughly estimated that demand for sanitisers is anywhere between 30 million-50 million litres a month, whilst capacity is only around 10 million, thereby creating huge opportunities. As a result of government's new policies, sectors such as agriculture, agro chemicals, and allied industries will hugely benefit leading to an increase in the farm sector and food processing industries. The need for cold supply chain and regular logistics and storage will see a surge. Pharmaceuticals, APIs, chemicals will see enhanced capacities too. India API imports from China averaged almost 70% of consumption by value and importers are at risk of supply disruptions and unexpected price movements. If Big Pharmas wants to diversify their supply chain, India could be a good destination for them to outsource API.

Social distancing impact will boost e-commerce and omni-channel in logistics: Consumers would naturally refrain from going to malls and shopping complexes due to fear of the pandemic and adopt social distancing. This behaviour will lead to increased home deliveries, need for e-commerce and omni-channels to service consumers much more than ever. This will also lead to increased warehousing solutions, investments in material handling, and material storage equipment as customers would minimise human touchpoints everywhere in the value chain. Middle-mile and last-mile delivery requirements in terms of two-wheelers (2W) and four-wheelers (4W) will also see a rise in demand thereof. With increased move towards e-commerce and online orders, future service expectations will change. This will lead to investment in virtual agents built using AI technology offering customers instant, on-demand service. This will also accelerate the future of customer experience in categories such as agent agility, channel choice, real-time workforce management, and prevalence of AI virtual agents.

Warehousing: Consolidation + Increase in Safety Stock: Manufacturers will want to ensure that their supply chains are de-risked and prepared for the new normal by having safety stocks. They will modernise and digitise their processes to ensure minimal human intervention. This is a real opportunity for all logistics and third-party logistics (3PL) companies. Recovery for the warehousing segment could be quick post the pandemic because of strong inherent demand, especially from sectors such as e-commerce, 3PL, FMCG (for essential goods/services), and pharmaceuticals. Even during the lockdown, warehousing space requirements for players, especially dealing with essential items, witnessed increased demand in terms of enquiries and expression of interest. There is a strong pipeline of development for the warehousing and logistics space, which is underway in the country. E-commerce and 3PL/logistics service providers would remain dominant occupiers and growth is set to regain, based on changing behavioural pattern of consumer and smaller manufacturers trying to use 3PL/logistics service providers to gain scale and operational efficiency.

Digital transformation leading to productivity and efficiency: There is no doubt that with massive changes in supply chains, digital transformation of the industry will be hastened. From planning to execution, every element of the logistics process will be reconsidered, repurposed, and digitised. Moving forward, technology will play a key role in enabling better logistics. More importantly technology will help companies manage their resources better and give deep-dive analytics to enable better decision-making. Digital transformation has the potential to create a leaner and smarter logistics by ensuring smoother interface among logistics stakeholders for seamless delivery. New entrants in the sector are start-ups that have been leveraging state-of-the-art technologies for improving performance and efficiency in supply chain operations. Start-ups will also look at revamping their existing supply chains to make them nimble and more adaptive to change. There would be a need to boost digital capabilities through online customer portals, developing industry leading products, which ensure customers contact-less experience with digital PoDs, smart automation, and seamless track and trace of products and physical touchpoints.

Demand drivers in medium to long terms

Short to medium-term drivers	Long-term drivers
Specific sector boost: Agriculture, food processing, pharma, textile, and chemicals	Increasing shift to domestic supply chains & advent of global value chains to India
Increased demand for warehousing for safety stock with consolidation of locations	Changing consumer trends: ecommerce, omni channel, urbanisation
Increase in modern handling systems such as pallets and conveyors.	Government thrust on infrastructure development such as future DFCs and focus on multimodal
Shift towards alternate transport modes. Containerise movement to boost up	Regulatory reforms and promoting digitisation in transactions and operations

Government initiatives to boost growth in the logistics sector:

- **Development of logistics-related infrastructure:** Government initiatives such as Bharatmala Pariyojana, Dedicated Freight Corridors (DFCs), 35 Multi Modal Logistics Parks (MMLPs) across India, Sagarmala, and inland waterways will increase efficiency of the logistics sector significantly. The government had accorded infrastructure status to the logistics sector in 2017, with the objective of reducing logistics costs. This will provide multiple benefits to the sector, including access to infrastructure lending at easier terms and competitive rates, access to external commercial borrowings (ECBs), longer maturity loans from insurance companies, and making them eligible to borrow from India Infrastructure Financing Co. Ltd. (IIFCL).

- **Ease of doing business:** GST has transformed the way the Indian logistics industry earlier functioned. This has resulted in a shift in business from unorganised to the organised sector. Post GST, companies have beenconsolidating their supply chains for efficiency and leasing large format warehouses. Faster movement of goods resulted in higher efficiency, thereby resulting in cost savings.

- **Implementation of e-way bill system:** Implementation of e-way bill systemstreamlined documentation and quicker movement of goods across states in India. The regulatory burden has come down considerably, leading to enhanced transparency and better compliance. The proposed e-invoicing, which has got postponed from the implementation date of April 2020 should lead to ease of doing business and build transparency.

- **National Logistics Policy:** This policy has been formulated with the aim to enable integrated development of the logistics sector in the country to spur economic growth and trade competitiveness boosting the MSME sector and leading to improvement in the Ease of Doing Business (EODB) rankings. This will be enabled by creating an integrated, seamless, green, and cost-effective logistics network by leveraging best-in-class technology, processes, and skilled manpower.

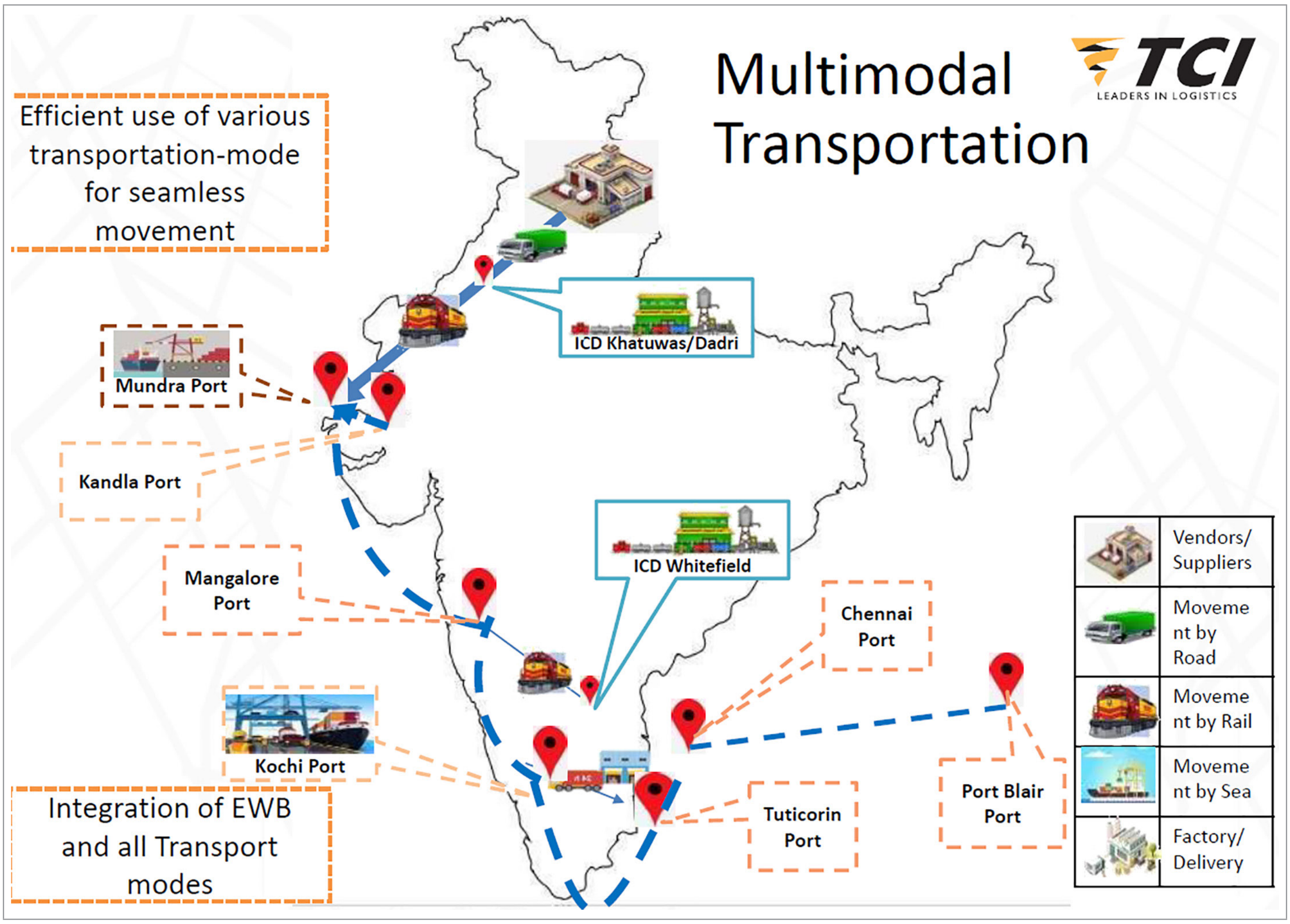
Why we like TCI – Strong capabilities in multi-modal logistics and supply chain business with over six decades of experience give a competitive edge over peers.

TCI is poised for healthy long-term growth led by increasing LTL share and value-added services in FTL for freight, high-growth outlook in both auto and non-auto segments for SCM, and continuous capacity additions for Seaways.

An integrated multi-modal logistics and supply chain solutions provider

TCI provides end-to-end logistics and supply chain solutions in India and the SAARC region through multiple modes including road, rail, and sea with over six decades of industry experience. The company's freight division has access to 4,500 trucks for placement, including owned 120 trucks. The freight division has 800 branches across all states with offices in major districts of the country. For sea transport, the company owns six ships with 82,000 DWT (deadweight tonnage) catering to both eastern and western coastal lines of the country. For rail transport, it has a subsidiary, TCI Concor Multimodal solutions with 51% stake. TCI's strong pan-India multi-modal capabilities give it a strong competitive advantage to offer most efficient solutions for its clients.

Multi-modal capabilities



Source: Company, Sharekhan Research

SCM business leverages multi-modal capabilities

The company's SCM business (34% of FY2020 consolidated revenue) leverages the transportation network of the company in road, rail, and seaways. The company is able to provide contract logistics and 3PL services to its clients offering both transportation and warehousing services. The company's SCM business is entirely B2B with the automotive segment comprising ~80% share, rest being FMCG, pharma, textiles, e-commerce, chemicals, among others. In e-commerce, the company only provides warehousing services, as last-mile delivery is a very low-margin business. In SCM, the top 7-8 companies comprise 70%-80% of segmental revenue. The strong multi-modal presence of the company benefits TCI in gaining supply chain management business.

Segment-wise details

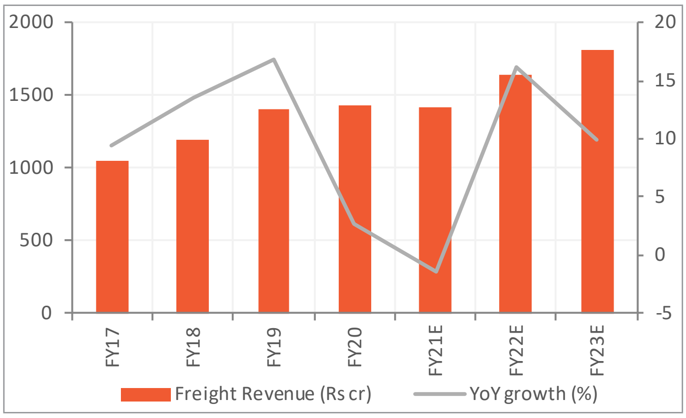
Segments	Freight	Supply Chain Solutions	Seaways
Services	Full truck load (FTL), less than truck load (LTL), small packages and consignments, over dimensional cargoes (ODC), Project Heavy Haul (PHH), and Foldable Large Containers (FLCs) through road, rail and sea.	Supply chain design and reengineering, logistics support to third-party, warehousingmanagement and other similar services.	Leading player in coastal shipping, non-vessel owned common carrier (NVOCC), and project cargo.
FY2020 Revenue (share)	Rs. 1,437 crore (52%)	Rs. 950 crore (34%)	Rs. 344 crore (12%)
FY2020 EBITDA (%)	3.7	10.0	31.6
RoCE (%)	15.5	16.4	15.9

Source: Company, Sharekhan Research

Freight business to be driven by LTL and value-added services in FTL

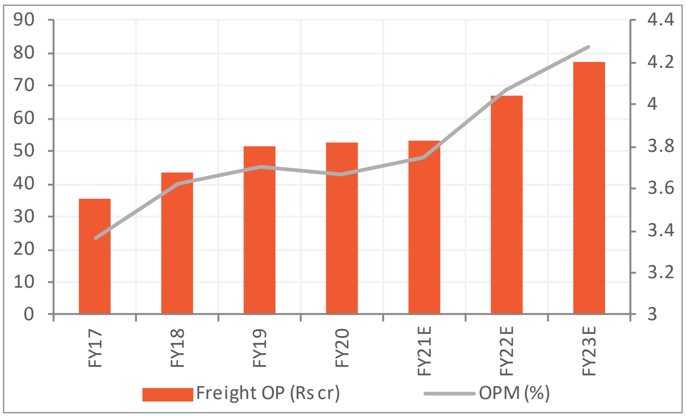
TCI is the only national player that caters to both LTL and FTL segments. TCI has been able to grow its freight business revenue at a 10.5% CAGR over FY2016-FY2020, which includes revenue from its subsidiary, TCI Concor. Growth was also supported by increasing LTL revenue share, which has risen from 25% three to four years back to now 33%. LTL business has over 2x operating margins vis-à-vis FTL business along with lower working capital cycle. Consequently, the company's freight operating profit (including other income) had reported at a 17.1% CAGR over FY2016-FY2020. Hence, the company is targeting LTL share to increase to 40%+ over the next two years, which should aid in improvement in operating profit margin (OPM) for the freight business. Additionally, it is also focusing on providing value-added services in the FTL segment to improve its OPM. We expect TCI's freight revenue to report a 13% CAGR over FY2021E-FY2023E with OPM growing at a 21% CAGR, led by improvement in OPM led by higher revenue share of LTL business and improvement in FTL

Freight revenue trend



Source: Company, Sharekhan Research

Freight Operating profit (including other income)



Source: Company, Sharekhan Research

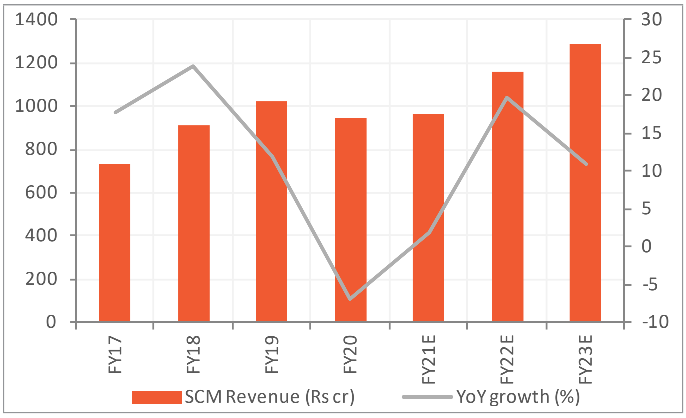
margins through value-added services.

SCM business to be driven by auto rebound and non-auto growth

TCI's SCM business is entirely B2B with dependence on the automotive sector, which comprises ~80%, rest being FMCG, pharma, textiles, e-commerce, and chemicals. In e-commerce, the company only provides warehousing services, as last-mile delivery is a very low-margin business. SCM revenue has reported an 11% CAGR over FY2016-FY2020, with FY2020 posting a 7% y-o-y decline on account of slowdown in the automotive sector. Further, SCM's OPM has remained at 10.5% average over FY2016-FY2019, while it is at 10% in FY2020.

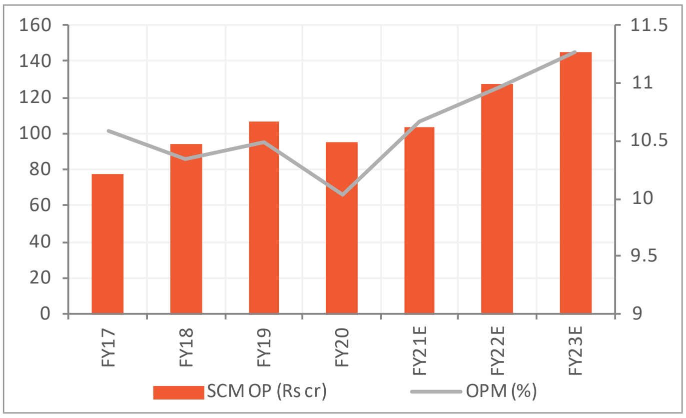
TCI has 12msf boxed warehouses, of which 17%-18% are owned and the balance are customer owned or leased. The company has started yard warehouses catering to factory finished units. It is the first one to do 20,000 cars kept in yard in Bangaluru for a North-based player. Strong rebound in the auto sector during FY2021, positive growth outlook for the auto sector, and high growth in non-auto (especially e-commerce and

SCM revenue trend



Source: Company, Sharekhan Research

SCM Operating profit (including other income)



Source: Company, Sharekhan Research

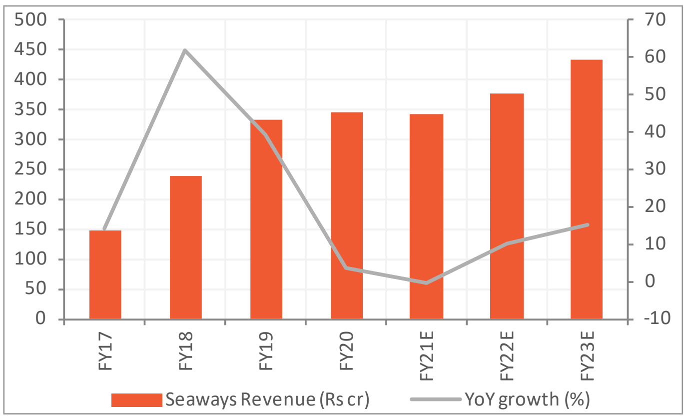
FMCG) are expected to drive SCM revenue going ahead. We expect SCM revenue to report a 15.3% CAGR over FY2021E-FY2023E. Further, higher revenue along with cost optimisation should lead to higher growth at operating level. Hence, we expect OPM for SCM to grow at a 18.5% CAGR over FY2021E-FY2023E.

Seaways – Strong fundamentals led by business acumen

TCI had seven ships with DWT of 96,000,of which it sold one ship having 400 container capacity in mid-February leading to now six ships with DWT of 82,000. The company normally works on coastal lines of India. On the eastern route, from Chennai to Andaman & Nicobar Islands, and on Western route, Kandla to Mangalore to Tuticorn to Kochi and back.

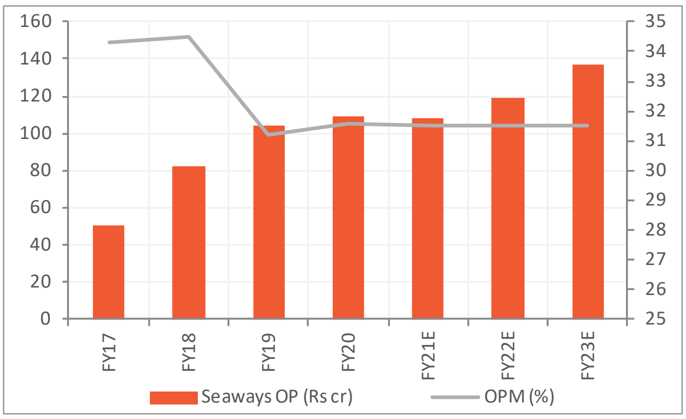
Seaways revenue had grown at a handsome 27.6% CAGR over FY2016-FY2020, led by addition of capacities with new ships getting added at almost every two years. Average OPM generated by the division is 31.5% over FY2016-FY2020. During the next year, it would be adding a second-hand ship (9-10 years old) with 800+ container capacity at a budget of Rs. 60 crore-70 crore. The additional capacity would further boost revenue during FY2023. The company's prudent capital expenditure on second-hand ships has led to improved

Seaways revenue trend



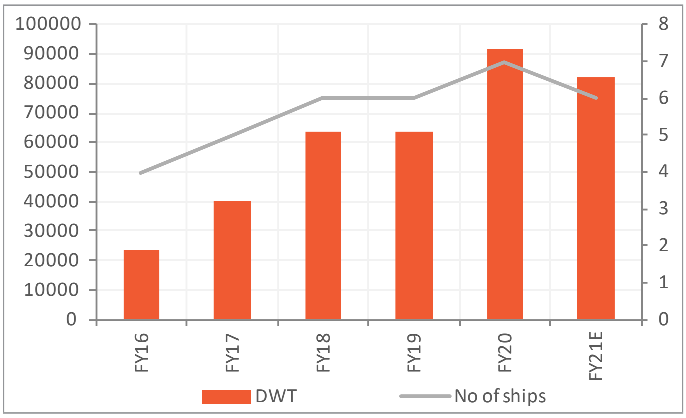
Source: Company, Sharekhan Research

Seaways Operating profit (including other income)



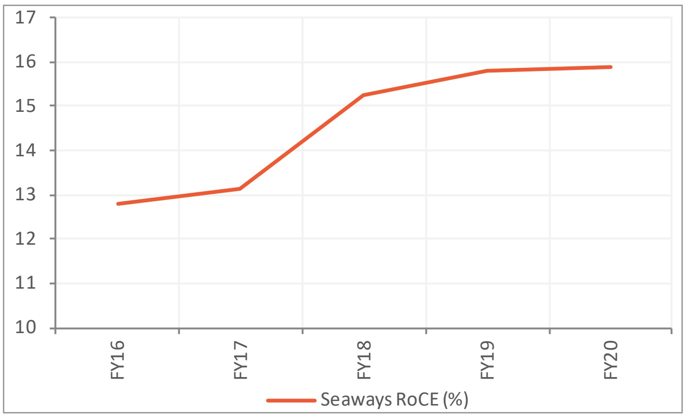
Source: Company, Sharekhan Research

Seaways capacity addition trend



Source: Company, Sharekhan Research

Seaways RoCE trend



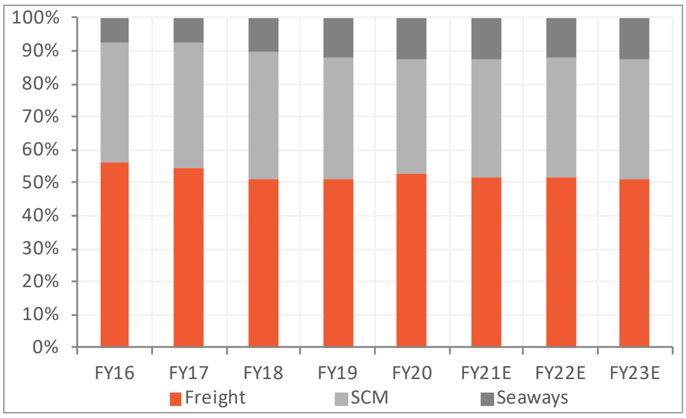
Source: Company, Sharekhan Research

revenue profile, higher OPM, and healthy RoCE for the business. We expect Seaways revenue and OPM to generate a 12.5% CAGR over FY2021E-FY2023E, as we have not yet factored the addition of new ships during FY2022 (which can lead to much higher revenue during FY2023).

Healthy revenue mix, OPM expansion to drive RoCEs

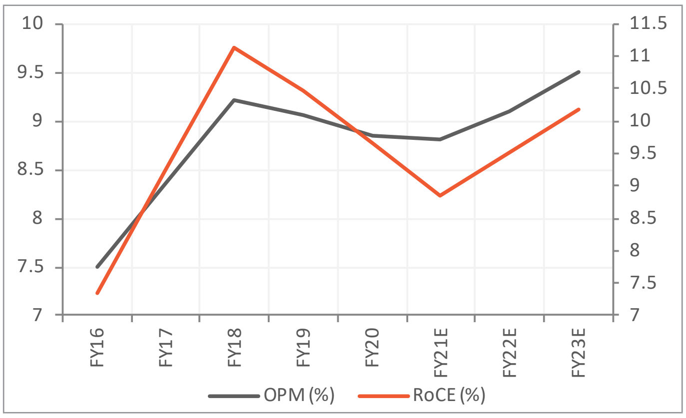
We expect TCI's RoCE to improve from the trough of 8.7% in FY2021 to 10.2% in FY2023, led by higher contribution of LTL revenue in freight, higher revenue from Seaways, and high revenue growth in SCM business. We expect freight OPM to increase from 3.7% in FY2021 to 4.3% in FY2023, led by higher LTL revenue contribution and value-added services in the FTL segment. SCM's OPM is expected to improve from 10.7% in FY2021 to 11.3% as the auto segment's revival leads to better absorption of fixed costs. The Seaways segment is expected to maintain its high OPM at 31.5% over FY2021-FY2023, supported by higher capacity utilisation. All of the

Segment-wise revenue mix



Source: Company, Sharekhan Research

OPM & RoCE trend



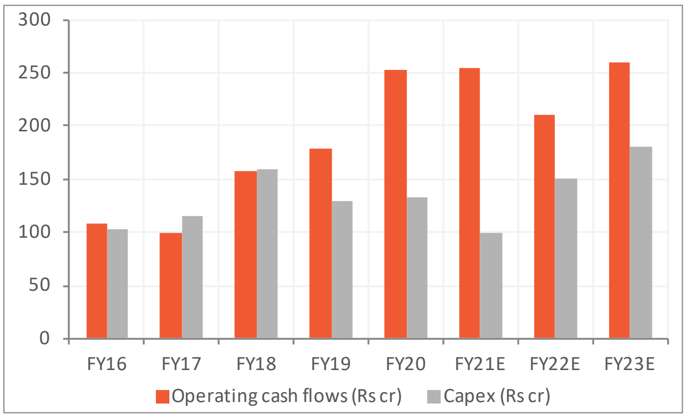
Source: Company, Sharekhan Research

above would lead to improvement in overall operating margins of the company from 8.8% in FY2021 to 9.5%. Healthy revenue growth profile across its three core verticals should lead to more or less similar segment-wise revenue mix viz. Freight (51%), SCM (36%), and Seaways (12%).

Strong OCF, high capex with declining leverage

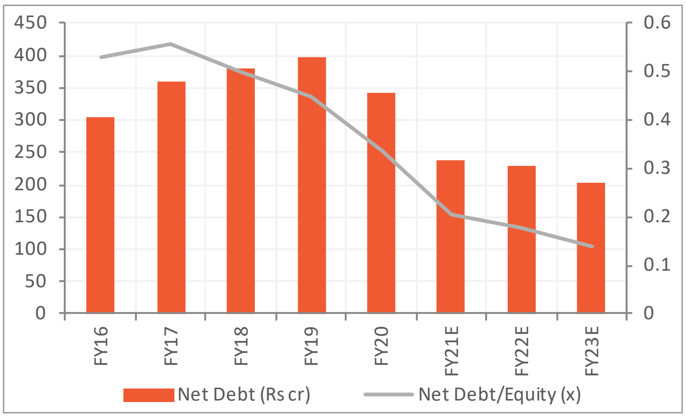
TCI has consistently generated strong operating cash flows during FY2016-FY2020, which have driven by higher capital expenditure. OCF of the company has risen by 2.3x from Rs. 109 crore in FY2016 to Rs. 252 crore in FY2020. Apart from strong operating profit growth of 16.8% CAGR over FY2016-FY2020, the company has maintained tight working capital, which has led to increased OCF generation. We expect TCI to generate Rs. 240 crore average OCF per annum over FY2021-FY2023, led by a 18.3% CAGR rise in operating profit and tight working capital management continuing over the same period. TCI has also lowered its net debt from Rs. 343 crore in FY2020 to almost Rs. 270 crore during 9MFY2021. The company would be incurring capex of

OCF/Capex trend



Source: Company, Sharekhan Research

Leverage trend



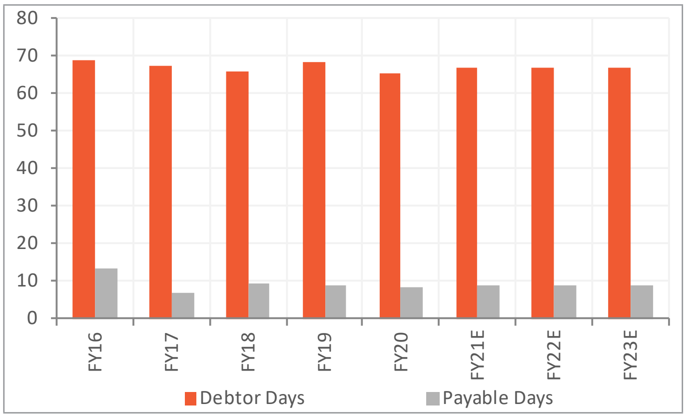
Source: Company, Sharekhan Research

Rs. 100 crore in FY2021, Rs. 150 crore in FY2022, and Rs. 150 crore-200 crore in FY2023. We believe capex to be funded through internal accruals along with improvement in net debt/equity from 0.3x in FY2020 to 0.2x in FY2023.

Tight working capital management

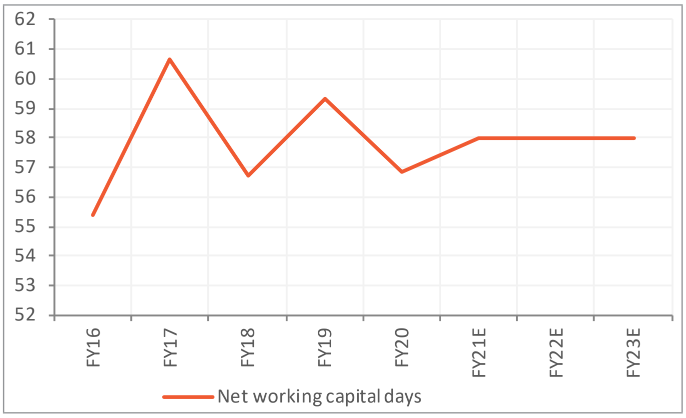
TCI has consistently focused on maintaining tight working capital management. The company's net working capital days have remained range bound at 55 to 61 days during FY2016-FY2020 on account of maintaining debtor days at 65 to 69 days. We expect TCI to maintain net working capital days at 58 days over FY2021-FY2023.

Inventory/Debtors/Payables trend



Source: Company, Sharekhan Research

Net Working Capital trend



Source: Company, Sharekhan Research

Management Interaction Highlights:

- **Logistics industry outlook:** In the past two years, the industry had witnessed muted growth owing to weak macroeconomic environment followed by COVID-19 pandemic. Government thrust remains on the logistics sector and it has been trying to regulate the sector. Key structural positive developments for the sector are 1) GST implementation, which has led to shift of business to the organised sector from the unorgainsed sector; 2) technological push over the past 3 to 4 years created hygiene in the sector; and 3) post COVID-19, the tendency to outsource logistics is high because of supply chain disruption caused by COVID-19. Other positive triggers for the sector are shifting of global supply chain led by China +1 strategies and government policies such as PLI. Within India, there is a huge market for logistics for organised players to grow.
- **Guidance:** The company targets 16%-17% topline growth and improvement in RoCEs every year.
- **Auto exposure:** The company is present in both industrial auto (earth-moving equipment, farm equipment, and infra) and mobility (such as 2W and 4W). Through Transystem (JV), the company works with Toyota

only, which had seen slower recovery and has a presence in the higher-end segment. Hence, strong growth in the auto sector was not visible recently. The company had made Rs. 4 crore investment in Transystem 20 years back. The JV has equity reserves of more than Rs. 200 crore; capital employed looks on the higher side.

- **Freight business:** Over the past three to four years, the LTL mix has increased from 25% to 33%, which has led to margin improvement and RoCE improvement as LTL has more than 2x margins than FTL segment, with lower working capital requirement. The company expects that in the next eight to nine quarters, LTL should contribute 40%+ share. The company has 4,500 trucks for placement, of which 120 are owned. The company follows the asset-light model. The company has 800 branches across all states with offices in major districts. The company targets to achieve 4.5%-5.0% EBITDA margin over the next eight to nine quarters. The SME segment comprises 20%-25% mix. The company is the only national player to cater to both FTL and LTL segments. The company is targeting minimum 12%-13% p.a. growth in the freight business.

- **Supply chain management:** TCI Express, which is a group company, is an LTL company with time-bound services with altogether different customers than TCI. TCI has 12msf boxed warehouses, of which 17%-18% are owned and the balance are customer owned or leased. The company has started yard warehouses catering to factory finished units. The company is the first to do 20,000 cars kept in yard in Bangaluru for a North-based player. The SCM business is B2B with 80% comprising the auto segment, rest being FMCG, e-commerce, pharma, chemicals. In e-commerce, the company has exposure to warehousing only. The top 7-8 companies comprise 70%-80% of revenue.

- **Seaways:** The company has seven ships, with DWT of 96,000,of which it sold one ship having 400 container capacity in mid-February, leading to now six ships with DWT of 82,000. The company had been adding capacity every 15-18 months. During the next year, the company would be adding a second-hand ship (9-10 years old) with 800+ container capacity at a budget of Rs. 60 crore-70 crore. The company normally works on coastal lines of India. On the eastern route, from Chennai to Andaman & Nicobar Islands, and on the western route, from Kandla to Mangalore to Tuticorn to Kochi and back. Normal OPM of the business is 27%-28%, while it had 31% OPM as one-off. The company is a 20%+ RoCE business.

- **Concor JV:** TCI's stake in the JV is 51%. The company generated Rs. 300 crore revenue in FY2020. TCI is PAT positive for the past three years with 5%-6% EBITDA margin. TCI is under the wait and watch mode with respect to divestment process of Concor and its impact on the JV.

- **TCI cold chain:** The cold chain business was hived off in 2019 into a separate subsidiary. The company has 90+ referrer trucks and about 10,000 pellet capacity. TCI will increase the capacity as demand pans out.

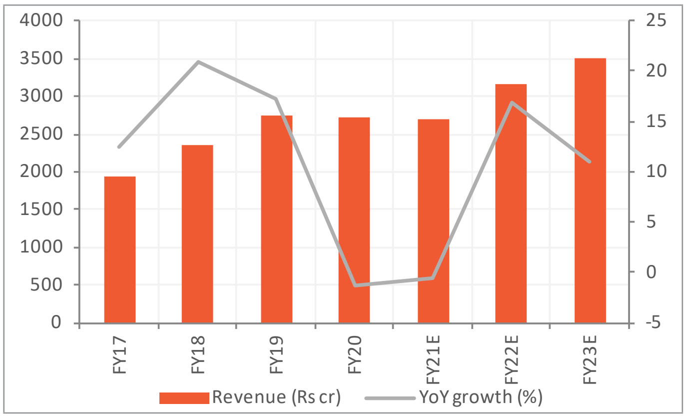
- **TCI Developers:** There is no cross holding between TCI and TCI Developers. The properties are built to suit TCI's usage, for which it pays lease charges. The company has not firmed up any plans on building logistic parks.

- **Capex:** The company would incur capex of Rs. 100 crore in FY2021, Rs. 150 crore in FY2022, and Rs. 150 crore-200 crore in FY2023.

- **Debt:** The company has debt of around Rs. 280 crore and cash of Rs. 12 crore-15 crore.

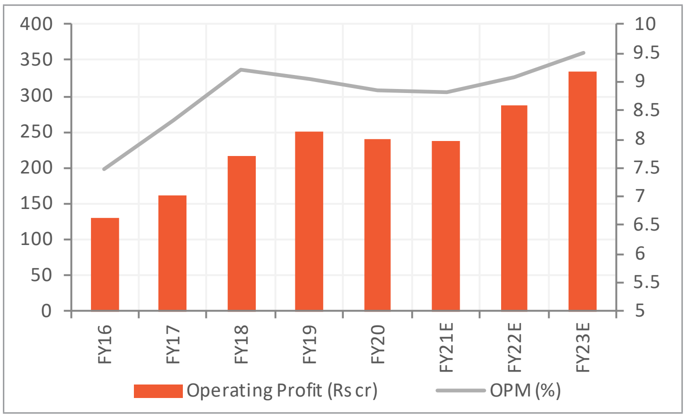
Financials in charts

Revenue trend



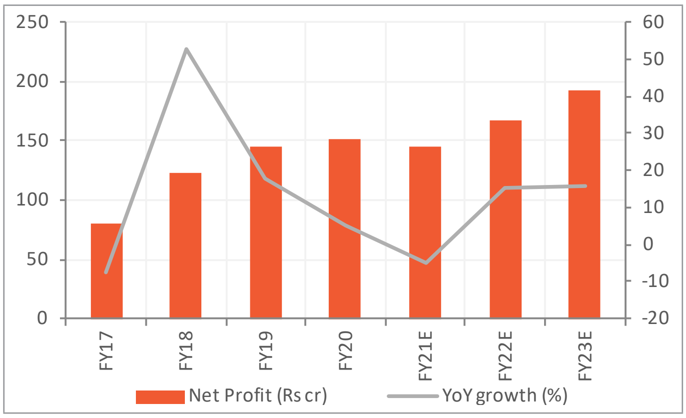
Source: Company, Sharekhan Research

EBITDA trend



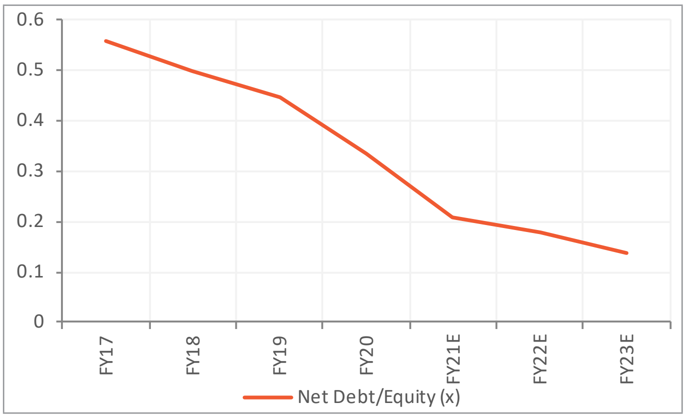
Source: Company, Sharekhan Research

Net Profit trend



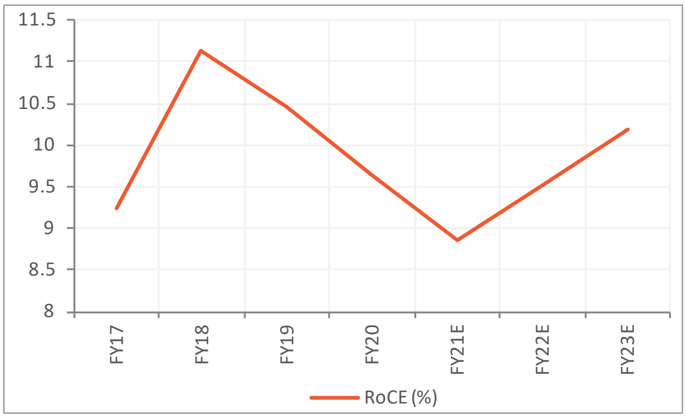
Source: Company, Sharekhan Research

Net Debt/Equity trend



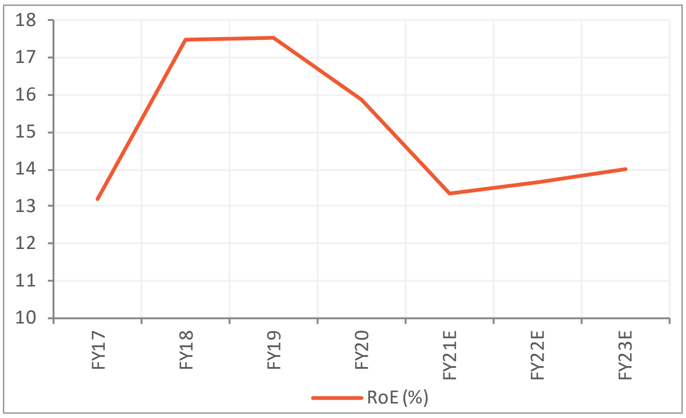
Source: Company, Sharekhan Research

ROCE trend



Source: Company, Sharekhan Research

ROE trend



Source: Company, Sharekhan Research

Valuations - High headroom to narrow valuation multiple for key businesses

We value TCI on SOTP basis assigning different valuation multiples for each segment depending on the growth potential and return ratios relative to comparable peers. The company's revenue/operating profit/ net profit is expected to grow by 14%/18%/15% over FY2021-FY2023E, led by growth across key verticals.

■ Sector View – Pace of recovery to be gradual; Although 3PL companies are better placed

The logistics industry had been severely hit by the pandemic, impacting the overall trade environment both domestically as well as globally. Though domestic indicators such as e-way bill generations andFASTag collections among others highlight m-o-mimprovement, the international EXIM environment is yet to show clear signs of revival. EXIM volumes continue to remain weak with frequent imbalance in trade. Competitive intensity remains high as many companies are going after weak volumes in the industry, putting pressure on profitability. Hence, we expect the pace of recovery in the logistics industry, especially in the EXIM business, to be gradual. However, the 3PL industry has seen faster improvement in operations, led by segments such as e-commerce, pharma,and FMCG. Hence, within the logistics industry, 3PL companies are better placed.

■ Company Outlook – Strong headroom for long-term growth

TCI has a strong long-term growth potential as it operates in a fragmented and highly unorganised logistics industry. The company's presence in multi-modal logistics along with the supply chain business with over six decades of experience gives it a distinctive advantage to capture the high growth potential in the logistics sector. TCI is expected to benefit from the logistics sector's growth tailwinds, led by GST, increased outsourcing of logistics services owing to COVID-19, government's thrust on Atmanirbhar Bharat, and global supply chain re-alignments. We expect TCI to be on a long-term growth trajectory, driven by positive sectoral fundamentals and its inherent strengths and capabilities.

■ Valuation – Initiate with Buy assigning an SOTP based PT of Rs. 354

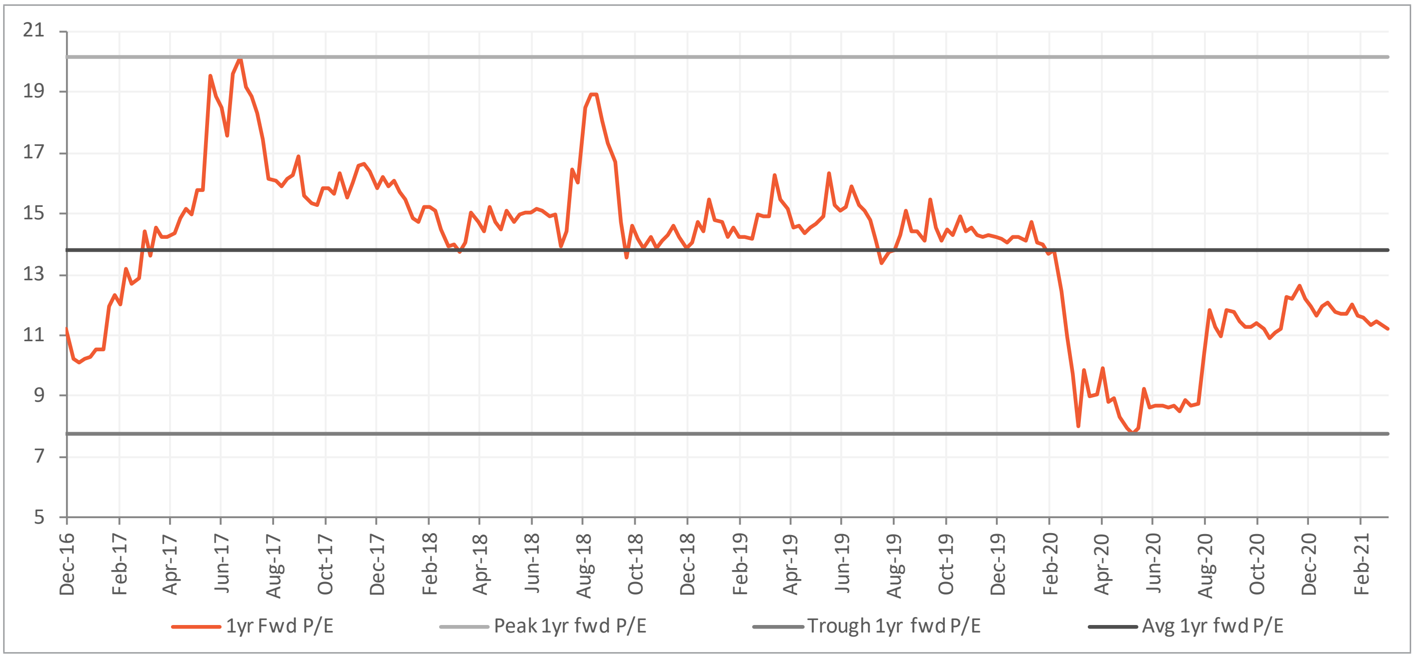
We have valued TCI on an SOTP basis, assigning a different valuation multiple for each segment, considering the growth outlook, OPM, and RoCEs. We value its freight business at 6x its EV/EBITDA on FY2023E earnings (discount to VRL Logistics owing to lower LTL presence leading to lower OPM and RoCE profile). We value SCM at 10x its EV/EBITDA on FY2023E earnings (discount to Mahindra Logistics, which has higher OPM and RoCE profile). We value Seaways at 7x its EV/EBITDA, owing to its healthy growth and RoCE profile. The JV transystem is valued at 1x its investment. On aggregate, we have arrived at an SOTP-based PT of Rs. 354. We initiate our coverage on the stock with a Buy rating.

Valuation Summary

Particulars	Valuation method	EV (Rs cr)	Value per share (Rs)
Freight	6x EV/EBITDA on FY2023E	463	60
SCM	10x EV/EBITDA on FY2023E	1450	189
Seaways	7x EV/EBITDA on FY2023E	958	125
Less: Net Debt		268	35
Vaue of core verticals		**2604**	**339**
Transystem JV	1x P/B	117	15
Price Target			**354**

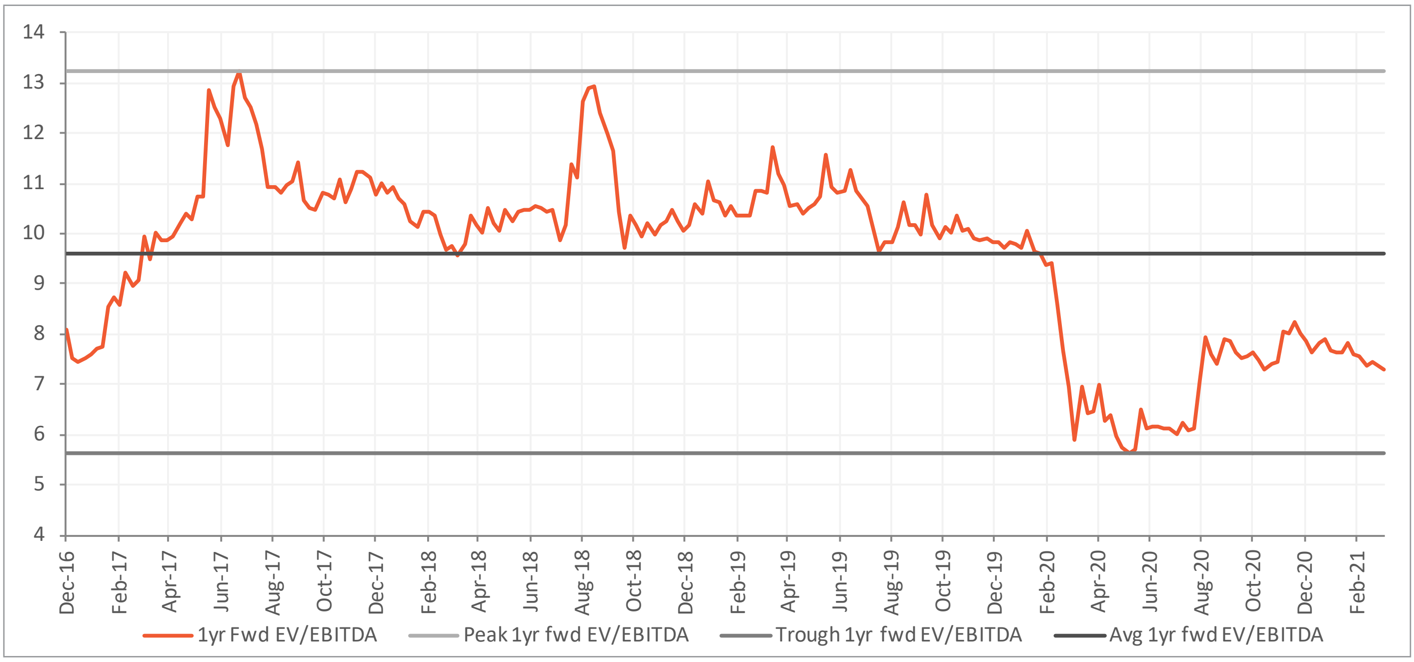
Source: Company, Sharekhan Research

One-year forward P/E (x) band



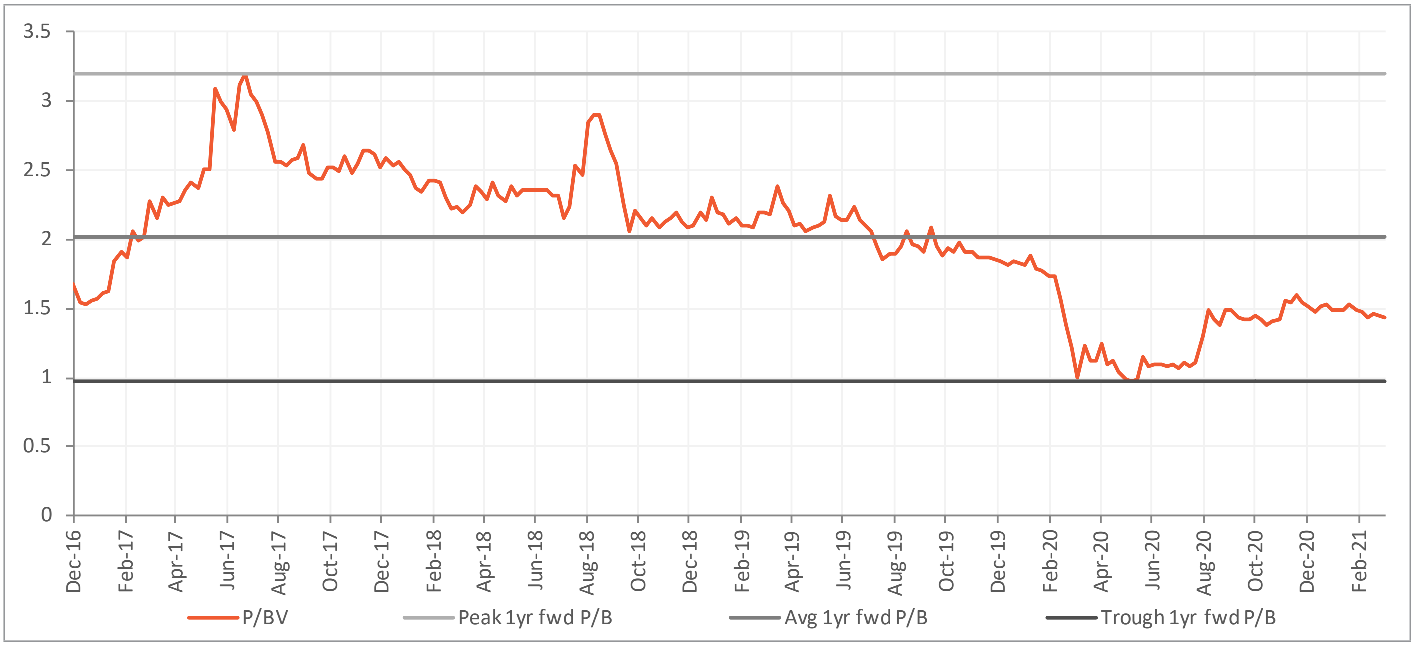
Source: Company, Sharekhan

One-year forward EV/EBITDA (x) band



Source: Company, Sharekhan

One-year forward P/B (x) band



Source: Company, Sharekhan

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
TCI	11.2	9.7	7.5	6.4	1.4	1.3	13.7	14.0
TCI Express	28.7	23.8	21.1	17.4	6.7	5.4	26.0	25.4
VRL Logistics*	19.4	16.2	6.6	5.9	3.1	2.7	16.0	16.9
Mahindra Logistics	55.2	41.5	18.8	15.6	5.2	4.6	11.0	12.9
Gateway Distriparks	25.1	19.2	8.9	7.7	1.5	1.4	5.8	7.5
Container Corporation of India*	34.4	27.7	9.5	7.7	3.1	3.0	9.3	11.0

*Source: Sharekhan Research; * consensus estimates*

Financials (Consolidated)

Statement of Profit and Loss Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net sales	**2,753.6**	**2,717.8**	**2,702.7**	**3,158.6**	**3,507.6**
Growth (%)	*17.2*	*(1.3)*	*(0.6)*	*16.9*	*11.0*
Total Expenditure	2,504.1	2,477.3	2,464.6	2,871.5	3,174.1
Cost of Revenues	2,251.5	2,214.3	2,223.1	2,599.0	2,873.1
Employee	140.2	157.2	141.5	155.6	171.2
Other Expenditure	112.4	105.8	100.0	116.9	129.8
Operating profit	**249.5**	**240.5**	**238.1**	**287.1**	**333.5**
Growth (%)	*15.3*	*(3.6)*	*(1.0)*	*20.6*	*16.2*
Operating profit Margin %	9.1	8.9	8.8	9.1	9.5
Depreciation	77.4	82.5	88.4	98.1	111.0
EBIT	**172.1**	**158.0**	**149.7**	**189.0**	**222.5**
EBIT margin (%)	6.2	5.8	5.5	6.0	6.3
Other Income	19.5	20.1	20.1	20.1	20.1
Interest Expenses	37.4	34.3	27.9	26.3	26.3
E/O item	(0.7)	(9.9)	(8.2)	-	-
PBT	153.5	134.0	133.8	182.8	216.3
Tax	33.3	15.9	21.4	40.4	47.8
Effective Tax rate (%)	21.7	11.9	16.0	22.1	22.1
Net profit before MI	120.2	118.0	112.3	142.4	168.5
Income from JV	25.1	25.2	25.0	25.0	25.0
Minority Interest	0.9	0.8	0.8	0.8	0.8
Adjusted Net profit	**144.4**	**142.4**	**136.5**	**166.6**	**192.7**
E/O item	(0.7)	(9.9)	(8.2)	-	-
Reported net profit	145.1	152.2	144.7	166.6	192.7
Growth (%)	*17.8*	*4.9*	*(4.9)*	*15.1*	*15.7*
EPS	**18.9**	**19.8**	**18.8**	**21.7**	**25.1**
Growth (%)	*17.8*	*4.7*	*(4.9)*	*15.1*	*15.7*

Source: Company, Sharekhan Research

Balance Sheet Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Equity share capital	15.3	15.4	15.4	15.4	15.4
Reserves & surplus	876.6	1,008.5	1,133.1	1,274.5	1,442.0
Net worth	**892.0**	**1,023.9**	**1,148.5**	**1,289.9**	**1,457.4**
Minority Interests	5.2	5.7	5.7	5.7	5.7
Total Loan funds	414.2	368.6	328.6	328.6	328.6
Net deferred taxes	39.0	30.2	30.2	30.2	30.2
Total Liabilities	**1,350.4**	**1,428.3**	**1,512.9**	**1,654.3**	**1,821.9**
Net Block	726.8	771.7	783.3	835.2	904.2
CWIP	4.0	21.6	21.6	21.6	21.6
Investment	116.8	135.3	135.3	135.3	135.3
Current Asset	**768.3**	**754.7**	**834.6**	**940.7**	**1,049.6**
Inventories	5.3	6.6	9.0	11.0	13.0
Sundry Debtors	515.1	487.3	496.1	579.8	643.9
Cash & Bank balance	15.5	25.9	91.6	99.4	127.0
Loans & Advances	135.5	122.8	125.9	138.5	153.8
Other current assets	96.9	112.0	112.0	112.0	112.0
Current liabilities & pro.	**265.6**	**255.0**	**262.0**	**278.5**	**288.9**
Current liabilities	259.1	244.8	251.8	268.3	278.7
Provisions	6.5	10.2	10.2	10.2	10.2
Net current asset	**502.8**	**499.7**	**572.7**	**662.2**	**760.7**
Total Assets	**1,350.4**	**1,428.3**	**1,512.9**	**1,654.3**	**1,821.9**

Source: Company, Sharekhan Research

Cash Flow Statement Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Cash flow from operating activities	179.1	252.3	254.5	210.1	259.9
Cash flow from investing activities	(153.7)	(137.5)	(100.8)	(150.8)	(180.8)
Cash flow from financing activities	(24.1)	(104.4)	(88.0)	(51.5)	(51.5)
Net change in cash and cash equivalents	1.3	10.4	65.7	7.8	27.6
Opening Cash balance	14.2	15.5	25.9	91.6	99.4
Closing Cash balance	15.5	25.9	91.6	99.4	127.0
Free Cash Flows (FCFF)	7.4	101.1	108.2	13.6	33.4
Free Cash Flows to Equity (FCFE)	(129.8)	(36.3)	4.0	(142.2)	(152.4)

Source: Company, Sharekhan Research

Key Ratios

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Margins (%)					
GPM	18.2	18.5	17.7	17.7	18.1
OPM	9.1	8.9	8.8	9.1	9.5
NPM	5.2	5.2	5.1	5.3	5.5
Tax rate	**21.7**	**11.9**	**16.0**	**22.1**	**22.1**
As a% age of revenue (%)					
Cost of Revenues	81.8	81.5	82.3	82.3	81.9
Employee Cost	5.1	5.8	5.2	4.9	4.9
Other Expenses	4.1	3.9	3.7	3.7	3.7
Financial ratios					
Debt / Equity (x)	0.5	0.4	0.3	0.3	0.2
Inventory days	0.7	0.9	1.2	1.3	1.4
Debtor days	68.3	65.4	67.0	67.0	67.0
Payable days	8.9	8.6	9.0	9.0	9.0
Working capital cycle	60.0	57.8	59.2	59.3	59.4
Adjusted EPS (Rs.)	18.9	19.8	18.8	21.7	25.1
Cash EPS (Rs.)	28.9	29.3	29.3	34.5	39.5
Dividend Per Share (Rs.)	1.8	2.0	2.0	2.5	2.5
Dividend Payout Ratio (%)	9.5	10.1	10.6	11.5	10.0
Book Value Per Share (Rs.)	116.1	133.3	149.5	167.9	189.7
RoNW (%)	17.5	15.9	13.3	13.7	14.0
RoCE (%)	10.5	9.7	8.9	9.5	10.2
Valuation ratios					
CMP (Rs.)	243.0	243.0	243.0	243.0	243.0
P/E (x)	12.8	12.3	12.9	11.2	9.7
Mcap (Rs. crore)	1,866.9	1,866.9	1,866.9	1,866.9	1,866.9
Market cap / Sales (x)	0.7	0.7	0.7	0.6	0.5
Enterprise Value (Rs. crore)	2,265.5	2,209.5	2,103.9	2,096.1	2,068.5
EV / Sales (x)	0.8	0.8	0.8	0.7	0.6
EV / EBIDTA (x)	8.6	8.9	9.0	7.5	6.4
Price / Book value (BV)	2.1	1.8	1.6	1.4	1.3
Dividend yield (%)	0.7	0.8	0.8	1.0	1.0
Growth ratios (%)					
Revenue	17.2	(1.3)	(0.6)	16.9	11.0
Operating profit	15.3	(3.6)	(1.0)	20.6	16.2
Profit before tax	18.6	(6.7)	(1.3)	28.8	18.3
Adjusted PAT	17.8	4.9	(4.9)	15.1	15.7
EPS	17.8	4.7	(4.9)	15.1	15.7

Source: Company, Sharekhan Research

About company

TCI is India's leading integrated supply chain and logistics solutions provider with over six decades of experience. The company has an extensive pan-India network with presence across major districts. TCI has 12 mn. sq. ft. of warehousing space. The company has three broad business verticals. TCI Freight: It transports cargo on FTL/ LTL/small packages and consignments/over dimensional cargo.TCI Supply Chain Solutions: The core service offerings are supply chain consultancy, inbound logistics, warehousing/distribution centre management and outbound logistics. TCI Seaways: TCI Seaways owns six ships and caters to coastal cargo requirements for transporting containers and bulk cargo.

Investment theme

TCI has a strong long-term growth potential as it operates in a fragmented and highly unorganised logistics industry. The company's presence in multi-modal logistics along with supply chain business with over six decades of experience gives it a distinctive advantage to capture the high growth potential in the logistics sector. TCI is expected to benefit from the logistics sector growth tailwinds, led by GST, increased outsourcing of logistics services owing to COVID-19, government's thrust on Atmanirbhar Bharat, and global supply chain re-alignments. We expect TCI to be on a long-term growth trajectory, driven by positive sectoral fundamentals and its inherent strengths and capabilities.

Key Risks

- Slowdown in the macro-economy leading to weak logistics industry outlook.
- High concentration towards the automotive industry.
- Highly competitive industry.

Additional Data

Key management personnel

Mr. D P Agarwal	Chairman & Managing Director
Mr. Vineet Agarwal	Managing Director
Mr. Ashish Tiwari	Group Chief Financial Officer
Ms. Archana Pandey	Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	HDFC AMC	6.36
2	HDFC Trustee	3.11
3	C. Robeco AMC	2.81
4	IDFC AMC	2.64
5	Sundaram AMC	1.07
6	Dimensional Fund	0.91
7	TATA AMC	0.83
8	GIC AMC	0.60
9	JP Morgan	0.51
10	LIC Nomura MF	0.46

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

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