



3R MATRIX

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

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS	✓	↔	✓
RQ	✓	↔	✓
RV	✓	↔	✓

ESG Disclosure Score

NEW

ESG RISK RATING

Updated Oct 08, 2021

15.77

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

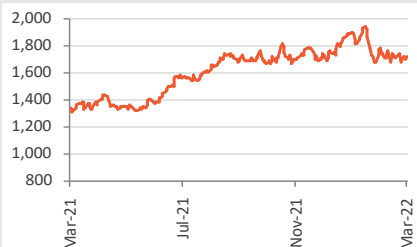
Company details

Market cap:	Rs. 723,652 cr
52-week high/low:	Rs. 1953 / 1306
NSE volume: (No of shares)	59.8 lakh
BSE code:	500209
NSE code:	INFY
Free float: (No of shares)	365.4 cr

Shareholding (%)

Promoters	13.1
FII	33.9
DII	17.2
Others	35.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.9	-1.6	2.6	28.1
Relative to Sensex	3.5	4.2	6.5	20.9

Sharekhan Research, Bloomberg

IT & ITES	Sharekhan code: INFY	
Reco/View: Buy	↔	CMP: Rs. 1,721 Price Target: Rs. 2,300 ↔
↑ Upgrade	↔ Maintain	↓ Downgrade

Summary

- Infosys is well-equipped to deliver industry-leading organic growth among large peers in FY2023E, led by broad-based demand, healthy deal wins, strong deal pipeline, and strong execution.
- Q4 usually remains a soft quarter on growth for Infosys owing to fewer working days and weak client spending. Margins are expected to remain under pressure in Q4FY22 owing to visa expenses and rising costs of backfill attrition and lower utilization.
- Headwinds including wage inflation, higher travel costs and supply-side issues would impact margins in FY2023E, while pricing leverage, lower subcontractor costs, and pyramid rationalisation would offset these headwinds to a large extent.
- We maintain a Buy on Infosys with an unchanged PT of Rs. 2,300, given strong revenue growth potential, market share gains, and strong demand.

Our interaction with Infosys' management indicates that the demand environment remains reasonable strong led by increasing spends on cloud migration and digital transformation program. The company's early investments in Cloud capabilities, localisation, deal advisory channels and sales & marketing capabilities position it to benefit from vendor consolidation, cost take-outs, captive carve-outs and core modernisation programs. Cloud migration remains the largest contributor to its total digital revenue (\$10 bn annual run rate) and the company is engaged in other cloud-related work such as private Cloud, hybrid Cloud, SaaS implementation and cloud-native application development. We expect Infosys would continue to report industry-leading organic revenue growth among large peers in FY2023E, led by broad-based traction across industries, strong digital capabilities and gaining market share.

- Well poised to lead industry:** Demand for IT services continues to remain strong and is led by increasing spends on cloud migration and digital transformation initiatives, legacy modernisation and spends on new emerging areas. The company's early investments in cloud capabilities provide it the ability to align with the clients' cloud transformation journey. Hence, we believe the company is well-positioned to benefit from strong demand post-Cloud migration phase as enterprises are likely increase tech spends substantially to develop Cloud-native applications and participate in cloud-based ecosystems. We believe Infosys is well poised to report industry-leading growth in FY2023E, given broad-based demand, healthy deal wins, strong deal pipeline and solid execution.
- Q4 – A weak season:** Sequential revenue growth is likely to moderate in Q4FY2022 compared to 7% constant currency (CC) revenue growth in Q3FY2022. Q4 usually remains a soft quarter for Infosys owing to fewer working days and weak client spending as budgets are not on track. Further, the growth would be impacted due to anticipated lower license sales in March 2022 quarter and absence of incremental revenue contribution from Daimler deal. However, the company would commence Data Centre work as part of Daimler deal during Q4 and Cloud-related work in Q1FY2023E.
- Margins to stay stressed in Q4; pricing to act as a lever in FY23:** Margins are expected to remain under pressure in Q4FY2022 owing to visa expenses, higher expenses to backfill attrition, and weak seasonality. Though pricing remains under pressure in core segment given competitive environment and automation, the pricing in the digital side business remains better as the company has trained its sales force to communicate the value that Infosys delivers during execution of projects. Headwinds including wage inflation, lower utilisation rate, increase in travel expenses and supply-side challenges to impact margins in FY2023E, while pricing leverage, reduction in sub-contractor expenses, cost optimisation, and pyramid rationalisation would largely offset these headwinds.

Our Call

Valuation – Strong demand, maintain Buy with a PT of Rs. 2,300: We believe Infosys is well-equipped to deliver industry-leading organic growth among the large peers in the medium term. Though the company would face margin headwinds in the near term, we believe the pressure would reduce during FY2023E considering ease of supply side issues, pricing leverage and reduction in subcontractor expenses. Infosys is expected to report USD revenue and earnings growth of 13.4% and 14.1%, respectively, over FY2022-FY2024E. At CMP, the stock trades at 28x/25x its FY2023E/FY2024E earnings, which is justified, given strong growth potential, robust deal pipeline, and solid execution. We like Infosys because of its strong capabilities, a strong capital allocation policy, and prudent investments in capabilities that will be required in future. Hence, we maintain a Buy rating on the stock with an unchanged price target (PT) of Rs. 2,300.

Key Risks

Rupee appreciation and/or adverse cross-currency movements, slackening pace in deal closures, and/or constraints in local talent supply in the US would affect earnings

Valuation (Consolidated)

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	1,00,473.0	1,21,764.7	1,42,824.9	1,61,865.5
OPM (%)	27.8	26.4	26.0	25.8
Adjusted PAT	19,423.0	22,266.5	25,557.0	28,963.3
% YoY growth	17.0	14.6	14.8	13.3
Adjusted EPS (Rs.)	45.6	52.9	61.0	69.1
P/E (x)	37.7	32.5	28.2	24.9
P/B (x)	5.1	4.9	4.6	4.1
EV/EBITDA (x)	25.4	22.0	19.0	16.7
RoNW (%)	25.3	27.5	29.6	30.4
RoCE (%)	31.9	33.4	36.6	38.4

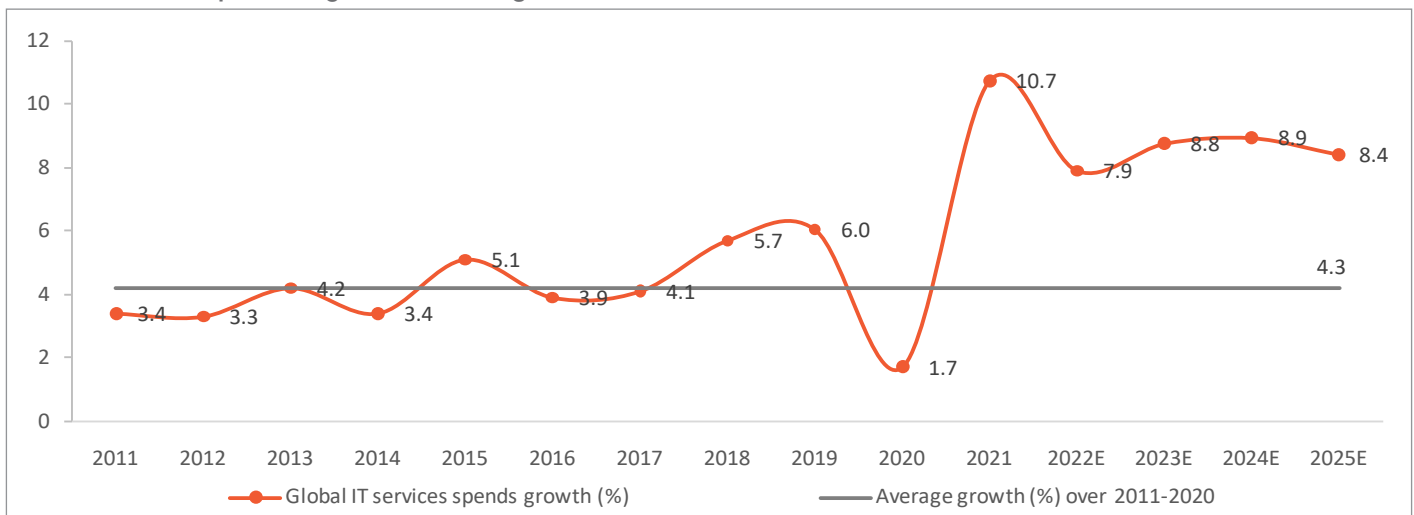
Source: Company; Sharekhan estimates

Strong demand environment here to stay

Spending on Cloud migration and digital transformation initiatives undertaken by the enterprises continues to be strong across industries and geographies as organisations want to enhance business resilience and agility, catch up with cloud-native competitors, reduce costs and improve customer experience. In addition, talent shortage in developed markets including US and Europe is driving the outsourcing demand for Indian IT service vendors. We expect strong demand environment would be led by emergence of a new operating model, increased spending on both cloud and digital transformation works, core modernisation and higher spending in new emerging areas such as security, AI & ML, ESG, and data and analytics. It is estimated that IT spends are expected to reach at 5% of total revenue of an enterprise over the next 5-10 years from 2-3% currently.

Gartner expects worldwide IT spend to rise by 5.1% y-o-y to \$4.5 trillion in 2022. Of this, IT services spend would grow by 7.9% in CY2022 compared to 10.7% in CY2021. Gartner expects IT services spending is likely to remain strong at an 8.9% CAGR over CY2022-FY2025, which will be significantly higher than the average growth of 5.6% during 2016-2021. Consulting (+11%) and application implementation and managed services (+9%) are expected to grow faster than BPO (+7%) and infrastructure implementation and managed services (+4%) in CY2022E.

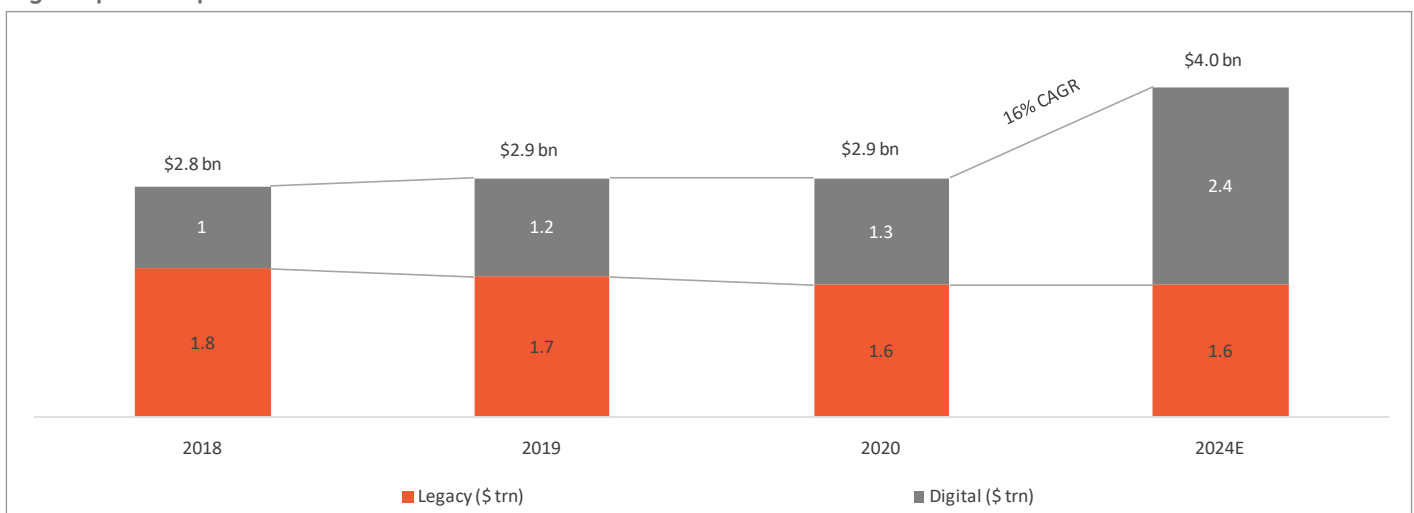
Global IT services spend likely to remain strong



Source: Gartner, Sharekhan Research

Enterprises that had invested in digital technologies would navigate challenges better than others. Hence, leaders have been rapidly scaling up investments in digital technologies to drive growth, while laggards and legacy companies are sharply focusing on building technology capabilities for their existential. Investment in digital technologies is expected to double from 2020 levels to approximately \$2.4 trillion in 2024.

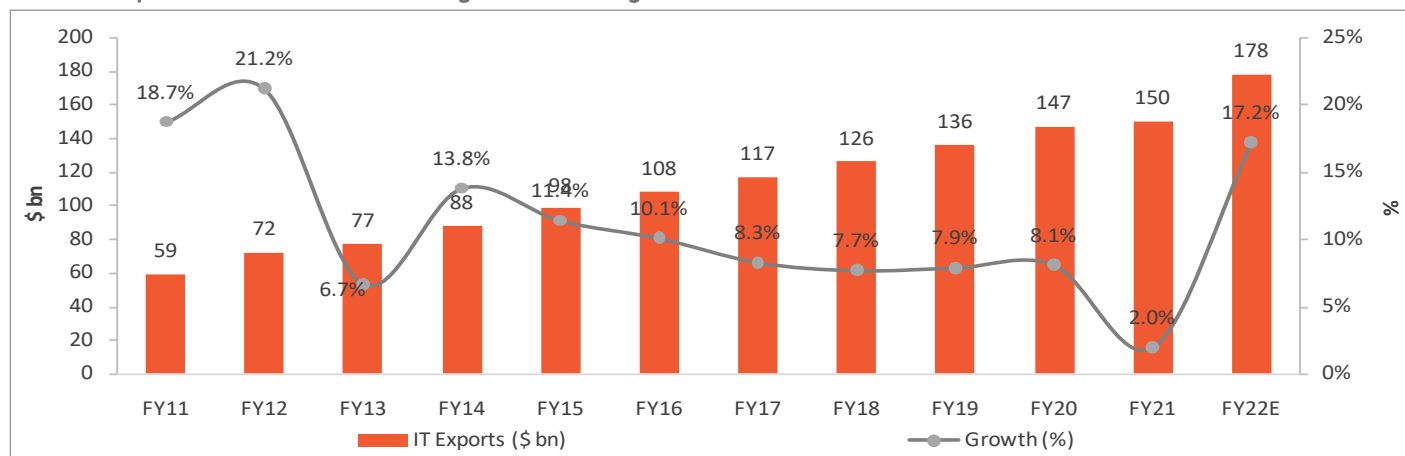
Digital spends to post 16% CAGR over 2020-2024



Source: Zinnov, Sharekhan Research

As per NASSCOM, the Indian IT industry is estimated to grow at 15.5% in FY2022, reaching \$227 billion revenue. Further, India has strong digital talent with 5 million+ tech workforce. As per NASSCOM's survey (NASSCOM Tech CEO Survey 2022), over 70% of CXOs believe that the industry would continue to grow strongly in FY2023E. Further, it is estimated that Indian technology industry is expected to touch \$350 billion by FY2026E from \$227 billion in FY2022E, growing at 11-14% per annum.

Indian IT exports continue to remain strong over next 3-4 years



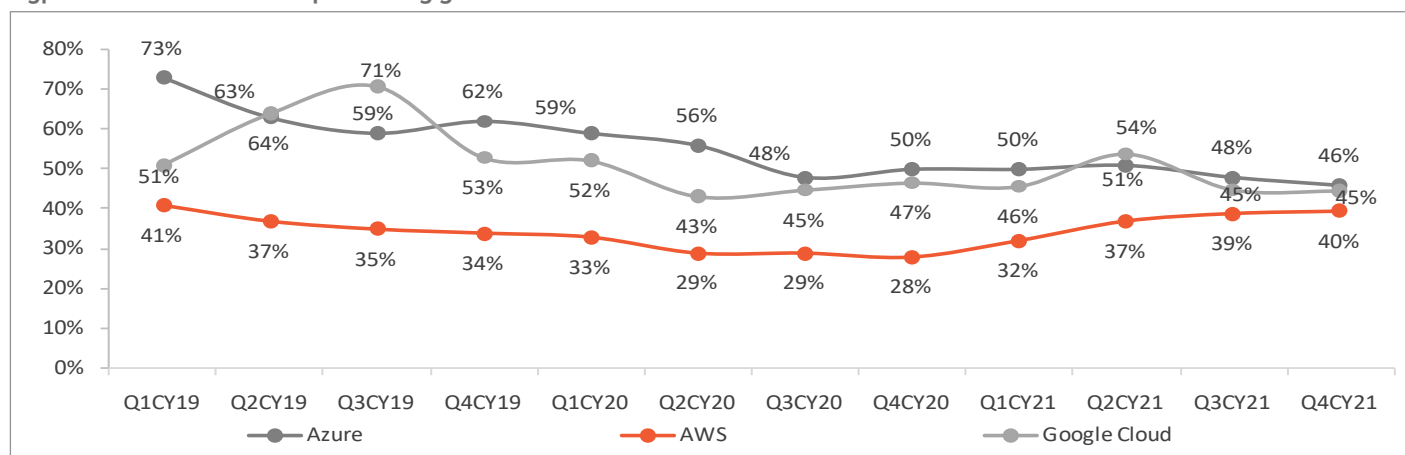
Source: NASSCOM, Sharekhan Research

Cloud tops enterprises' priority list; Infosys well poised to capture opportunities

The global Cloud computing market is projected to grow at a CAGR of 17.9% to \$792 billion by 2028 from \$250 billion in 2021. Enterprises' IT spending would move to Horizon-2 and Horizon-3 initiatives once the significant portion of cloud migration (Horizon-1) is completed. The phases of cloud migration journey are – (a) moving work-load to cloud (Horizon-1), (b) development of cloud native applications (Horizon 2), and (c) integration across ecosystem (Horizon-3). While Cloud migration opportunity is democratic, we believe Horizon 2 and Horizon 3 opportunities will be more judicious. It is estimated that 30-40% of workloads have moved to Cloud and this can increase to 70-80% in the next 3-4 years. Consequently, enterprises would increase IT services spends substantially to participate in cloud-based ecosystems (including AI, data, and analytics spend) to derive benefits from new innovations in the form of Horizon-2 and Horizon-3 transformation initiatives. IDC expect the managed Cloud services industry to double in terms of revenue over CY20-CY25E.

Infosys is engaged with its clients to redesign their core and build new cloud-first capabilities to create seamless experiences in public, private, and hybrid cloud, across PaaS, SaaS, and IaaS landscapes. Infosys Cobalt capabilities are resonating well with clients, given its strong capabilities and strong partner ecosystem with hyperscalers and downstream players. Infosys Cobalt has been helping the company to win mega deals such as Daimler, Vanguard and among others in the recent past and remains the largest contributor to its total digital revenue (\$10 bn annual run rate). The company's early investments in cloud capabilities provide it the ability to align with the clients' cloud transformation journey and to straddle across private, hybrid Cloud, multiple Cloud and hybrid multi-cloud environments of clients' IT landscape.

Hyperscalers continue to report strong growth



Source: Sharekhan Research

Cloud migration at the infancy stage; huge headroom for growth

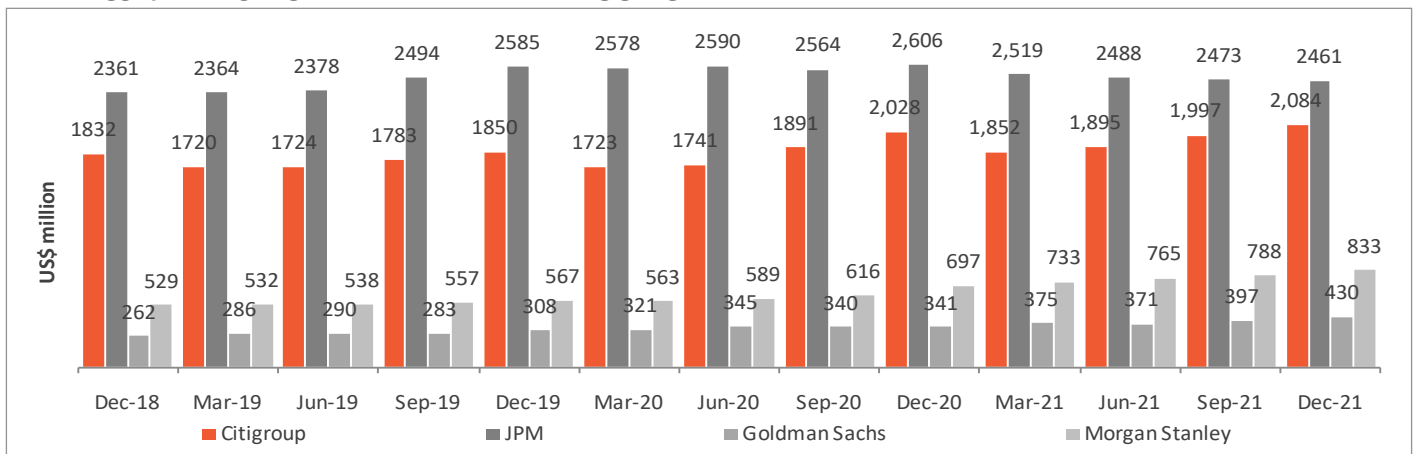


Source: IDC, Sharekhan Research

Strong BFS tech spending likely to be sustainable in CY2022

The intensity of technology spending by the BFS firms is expected to remain strong in CY2022 even after a higher budget allocation towards technologies in CY2021. Post the pandemic, BFS firms have been investing on digital channels because of improving customer experience, reducing expense, gaining market share, and combating competition from well-funded fintech firms and large technology companies. In addition, higher online penetration of banking products and services and reduction of physical branches are the drivers for increasing tech budget by the BFS firms. Hence, we believe the tech spends by the BFS companies would remain strong across sub-verticals (capital markets, payments, retail banking, wealth management, cards, etc), across large and mid-sized banks and across the technology stack in the medium-term as BFS companies are driving cloud transformation programs to build resilient and scalable platforms.

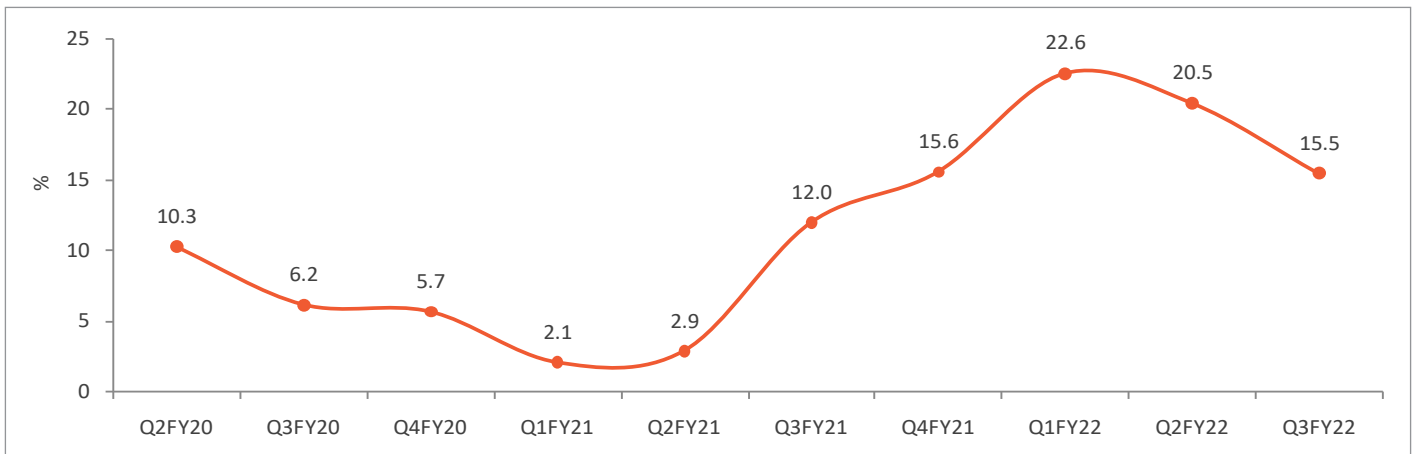
Technology spends by large US banks to remain strong going ahead



Source: Sharekhan Research

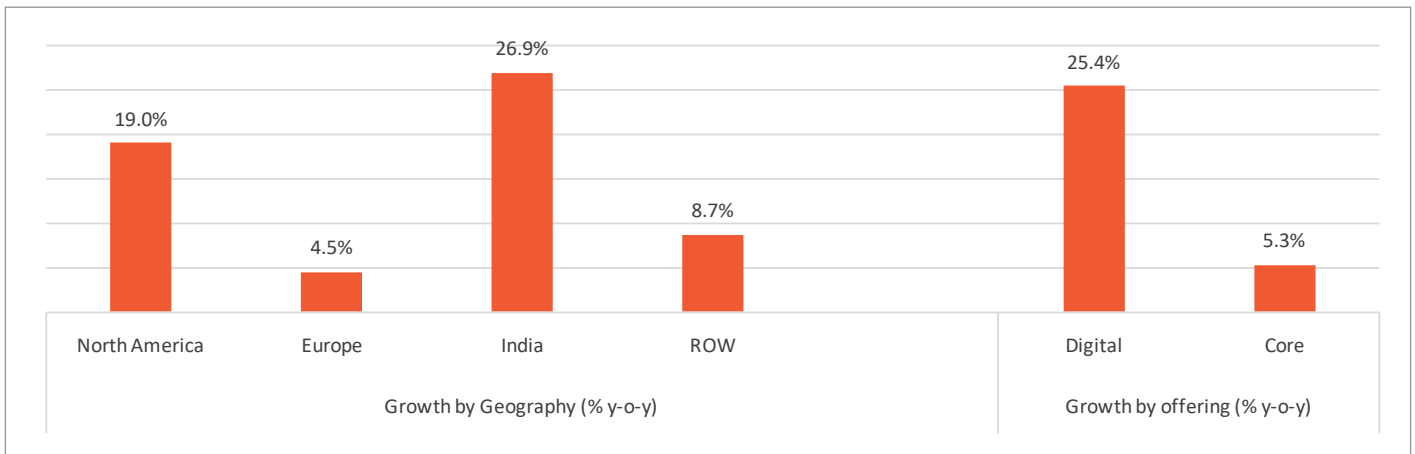
We don't see any major impact on tech budgets of large BFS firms even if the interest rate increases in the US. The BFS firms are committed for IT spending on cloud migration and digital transformation programs. Infosys' continuous efforts in building capability at sub-vertical levels such as regional banking, retirement services, and payments positions it well to capture market opportunity amid the current strong demand environment. This is evident from the strong growth in its financial services vertical for the past several quarters. Given Infosys' deep domain expertise, robust delivery capabilities, transformation solutions across sub-segments of BFS, and strong tech spends by BFS firms, we believe Infosys would sustain its strong growth momentum in its BFSI vertical going ahead.

Infosys' BFSI constant-currency revenue growth trend (% y-o-y)



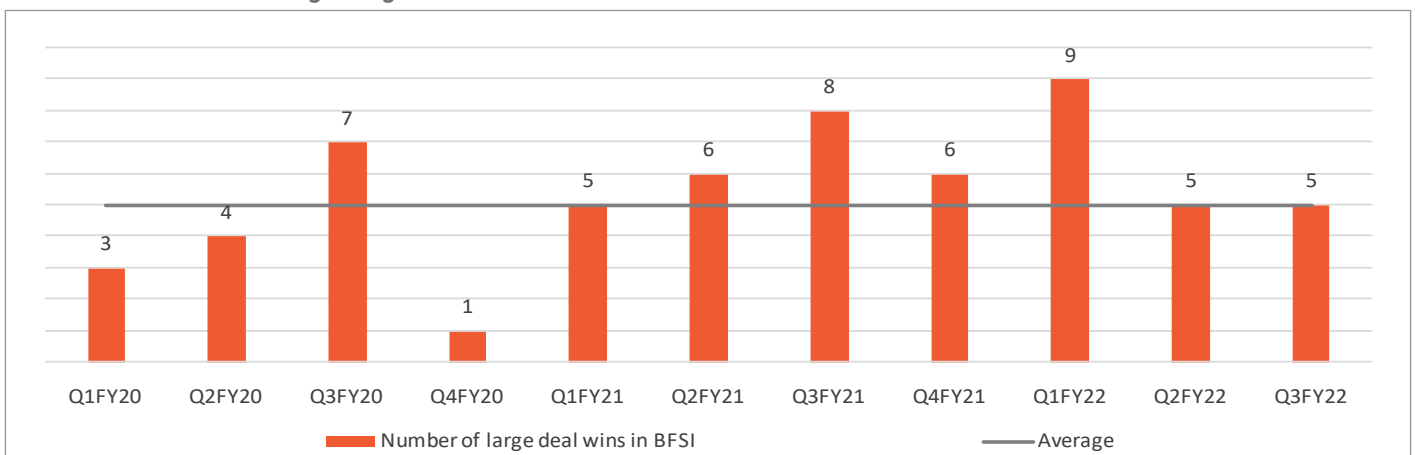
Source: Sharekhan Research

Q3FY2022: BFSI USD revenue growth y-o-y across geographies and offerings



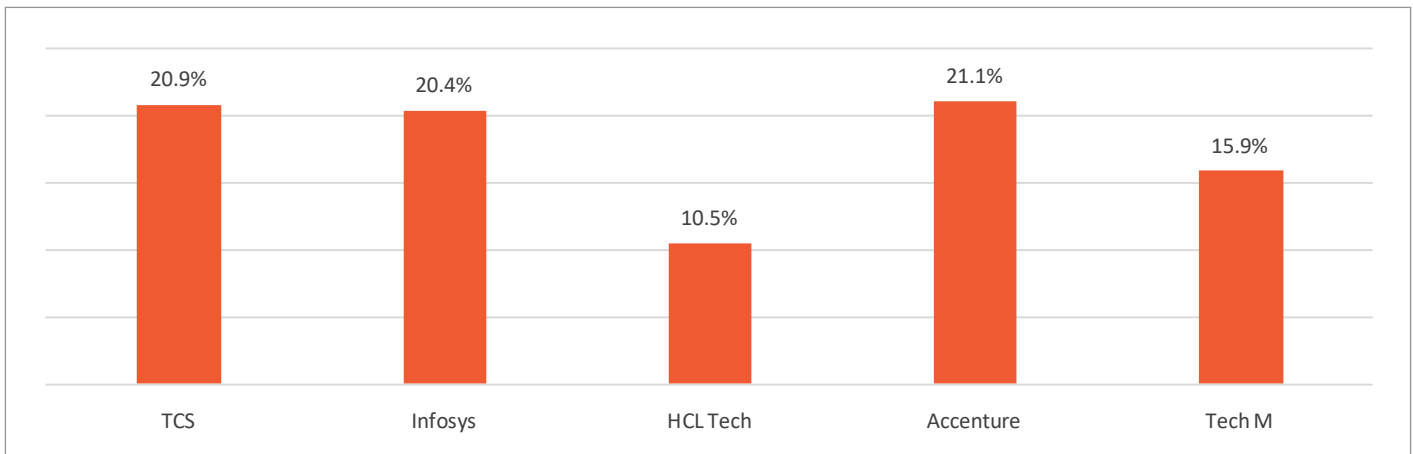
Source: Sharekhan Research

Number of BFSI deal wins by Infosys



Source: Company, Sharekhan Research

Infosys BFSI is one of the fast growing among peers in Q3



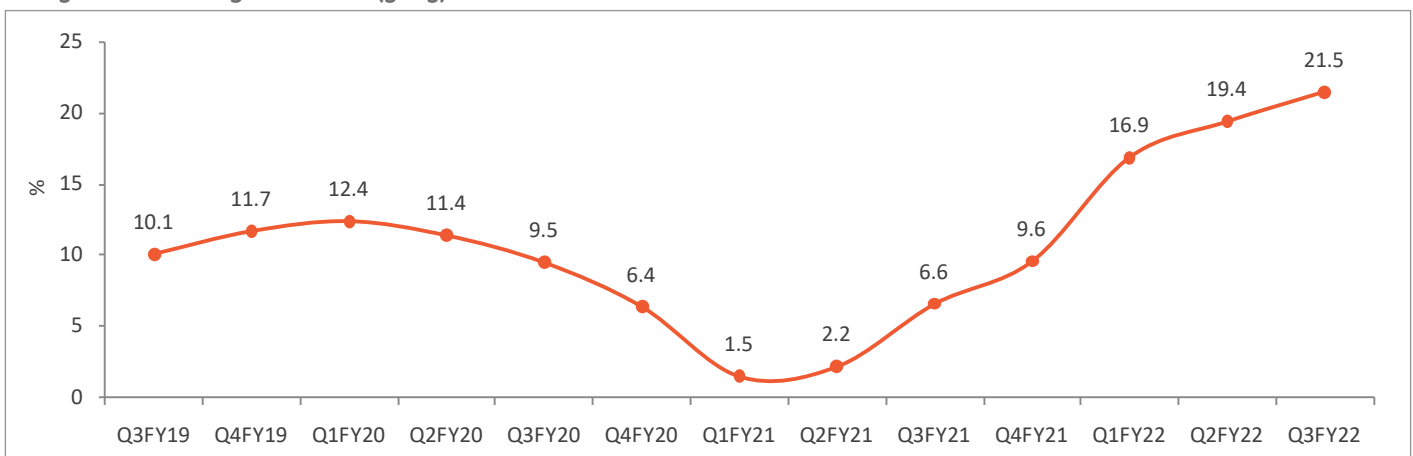
Source: Company, Sharekhan Research * last twelve months y-o-y

Growth to moderate in Q4 due to weak seasonality; expect to post industry leading growth in FY2023E

The management maintained its earlier commentary on the demand outlook as it has not witnessed any incremental changes in demand so far during the quarter. Infosys reported strong USD revenue growth of 20.9% y-o-y in 9MFY2022, which is on track to achieve industry-leading organic growth in FY2022 among its large peers. The company increased FY2022E revenue growth guidance to 19.5-20% from 16.5-17.5% earlier and 12-14% at the beginning of the year. Though the revision in guidance was impressive, sequential revenue growth would moderate in Q4FY2022 compared to 7% constant currency (CC) revenue growth in Q3FY2022. Q4 is usually a soft quarter for Infosys owing to fewer working days and weak client spending as budgets are not on track. Further, the growth would be affected by anticipated lower license sales in March'22 quarter and absence of incremental revenue contribution from the Daimler deal.

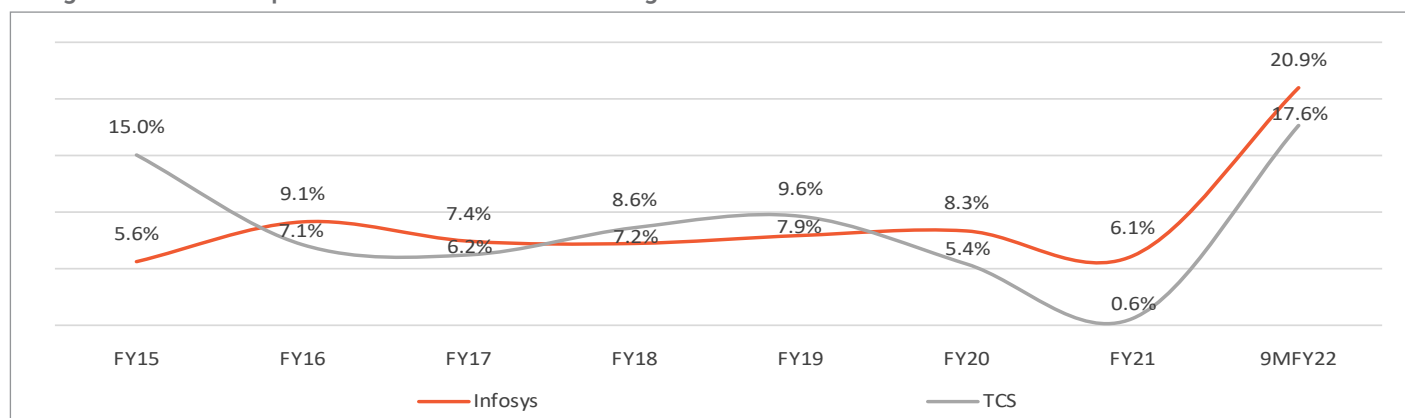
Demand environment for IT services continues to remain strong and is led by increasing spends on cloud and digital transformation initiatives, core modernization and higher spending in the new emerging areas. Infosys' investments in cloud capabilities, localisation, deal advisory channels and sales and marketing position it to remain at the forefront of its client's digital transformation journey. The company's flattish growth in core business portfolio and strong growth in digital business indicate the company's ability to gain market share, consistent winning of large deals and new logo additions. Hence, we forecast that the company would continue to report industry-leading revenue growth in FY2023E.

Infosys' CC revenue growth trend (y-o-y)



Source: Company; Sharekhan Research

Infosys continues to outperform TCS for third consecutive years

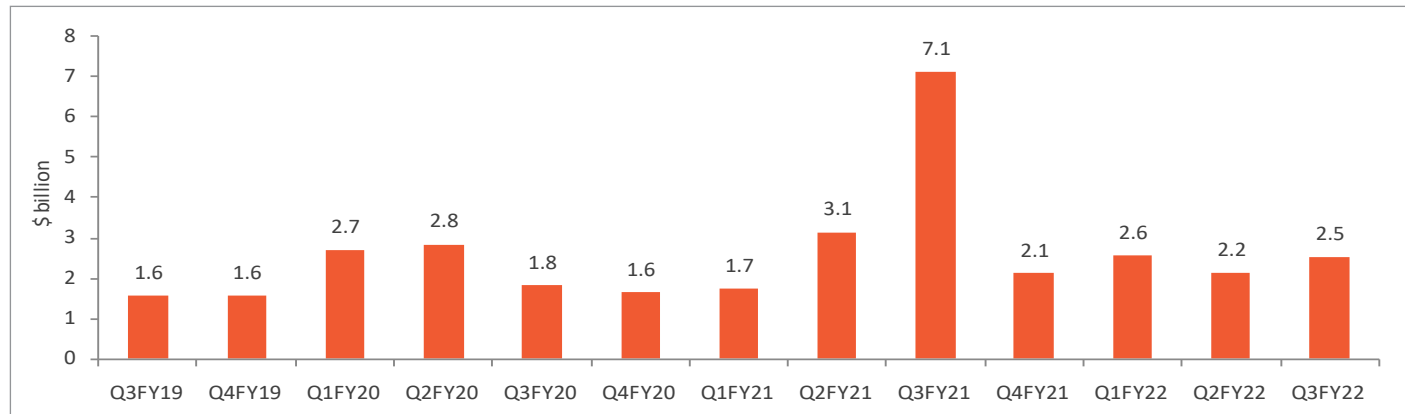


Source: Company; Sharekhan Research

Deal conversion rate likely to remain healthy

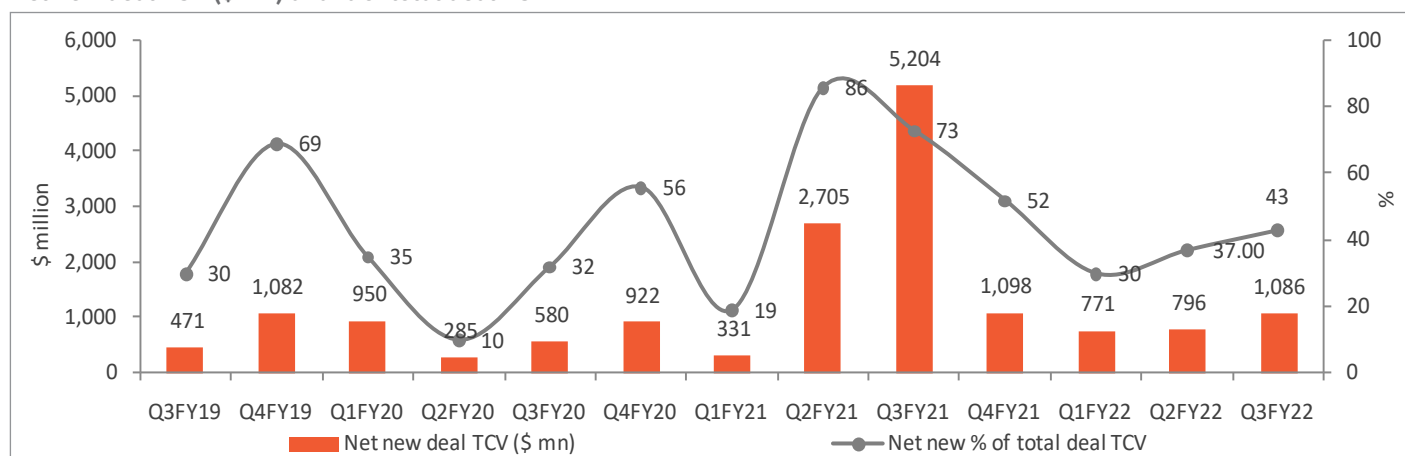
Absence of mega deals has not been a growth constraint as the demand remains reasonable string on increased discretionary spending. Infosys signed large deal TCVs of \$2.5 billion in Q3FY2022, down 65% y-o-y. Further, the company's last-twelve-month deal TCVs also declined 32% y-o-y to \$9.4 billion. However, the company has won 92 large deals in last one year and has added 100+ new logos each quarter over last four quarters. The company indicated that the deal pipeline (comprising both large and small deals) remains strong given its investments in capabilities required by clients and strong participation in their transformation journeys. The management stated that the deal pipeline contains a large number of large deals, mega-deals, and vendor consolidation deals. We believe sustained demand strength and steady conversion of the deal pipeline would drive deal win momentum going forward.

TCV of deal wins (\$ bn)



Source: Company; Sharekhan Research

Net new deal TCV (\$ mn) and % of total deal TCV



Source: Company; Sharekhan Research

Fresher hiring to be robust in FY2023

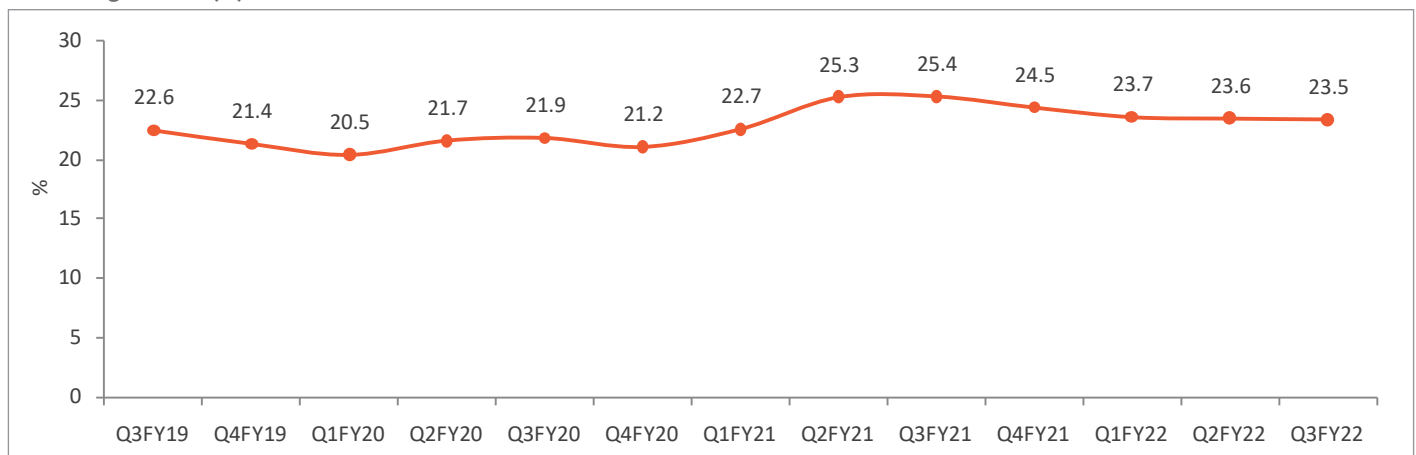
The company has increased its fresher hiring plans to 55,000 in FY2022 from 25,000 at the beginning of the year to meet the higher demand. Management stated that the company has recruited around 45,000 freshers during 9MFY2022. The company plans to hire a similar number of freshers in FY2023E to cool off the supply side challenges and improve margins by reducing lateral hires and replacing subcontractors.

Expect margin to stay under pressure in Q4; pricing to act as a lever in FY23

EBIT margins are expected to remain under pressure in Q4FY2022 owing to (1) visa expenses, (2) higher expenses to backfill attrition, (3) decline in utilisation, (4) elevated subcontractor expenses and (4) weak seasonality.

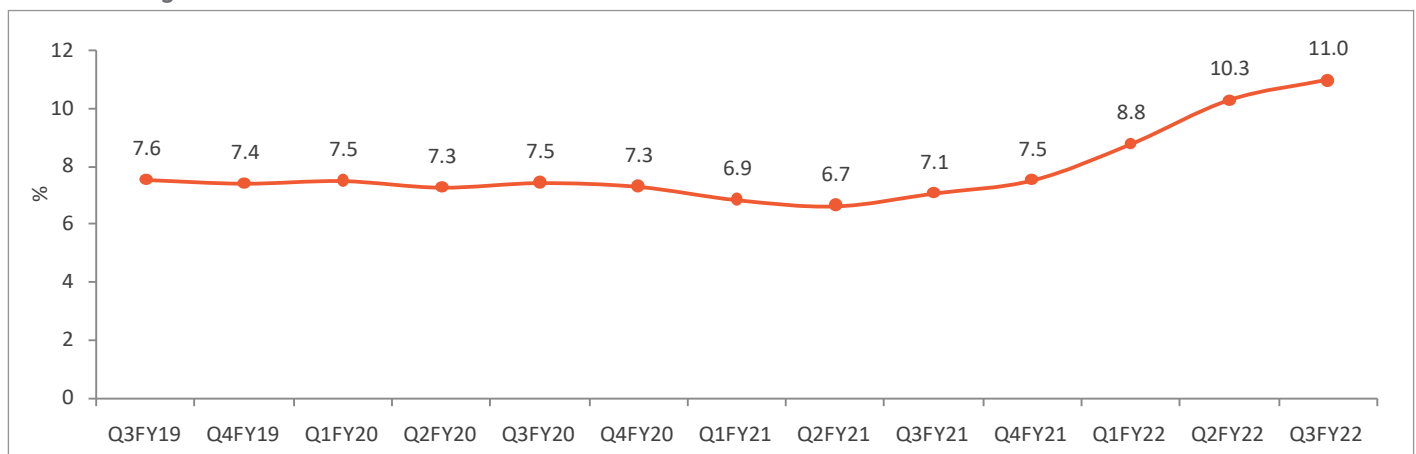
As supply-side challenges are expected to continue for next few quarters given strong demand environments and lack of digital talents, Indian IT services companies are trying to focus on value-added selling, higher pricing in new bookings and bringing the right level of Cost of Living Adjustments (COLA) during renewals to offset higher talent expenses. Though pricing remains under pressure in core segment given competitive environment and automation, the pricing in the digital side business remains better as the company has trained its sales force to communicate the value that Infosys delivers during execution of projects. Further, management expects utilisation would stay at 84-86% going ahead versus 80-83% before pre-pandemic times. Though headwinds including wage inflation, lower utilisation rate, increase in travel expenses, and supply-side challenges to impact margins in FY2023E, we believe pricing leverage, lower sub-contractor expenses, cost optimisation, pyramid rationalisation and currency tailwinds to offset these margin headwinds to a large extent.

EBIT margin trend (%)



Source: Company; Sharekhan Research

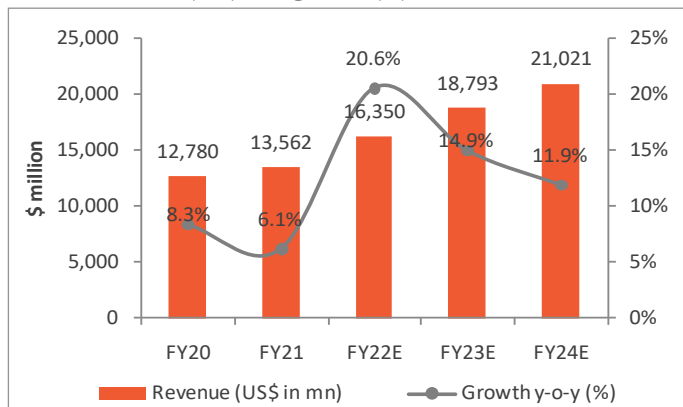
Subcontracting costs as a % of revenue



Source: Company; Sharekhan Research

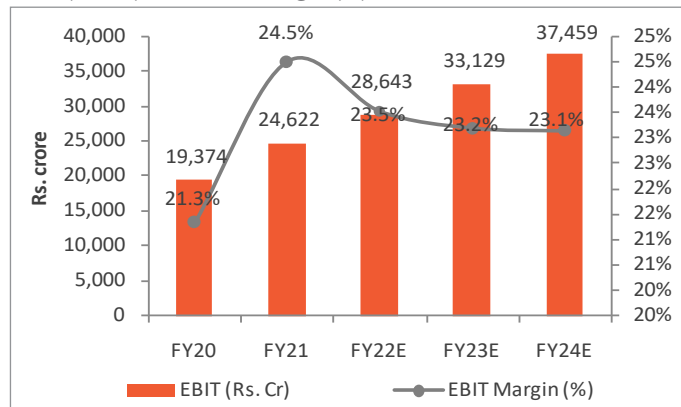
Financials in charts

Revenue in US\$ (mn) and growth (%)



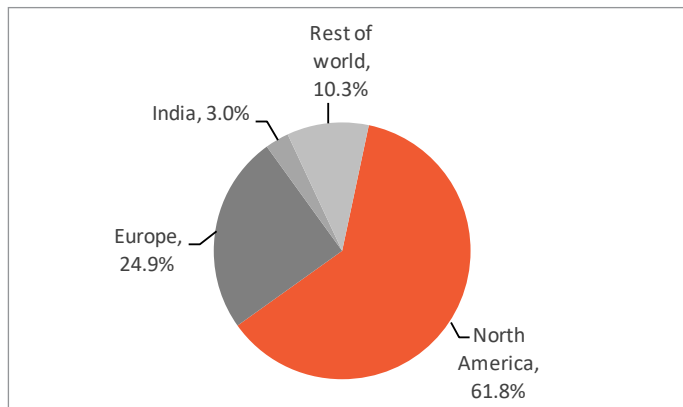
Source: Company, Sharekhan Research

EBIT (Rs. cr) and EBIT margin (%)



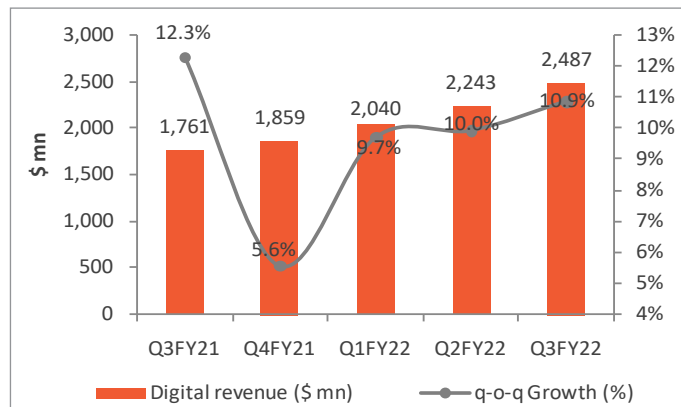
Source: Company, Sharekhan Research

Geography break-up (%)



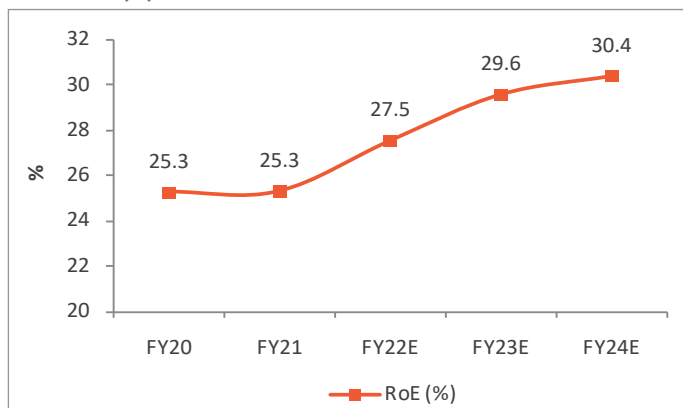
Source: Company, Sharekhan Research

Digital revenue (\$ mn) and growth (%)



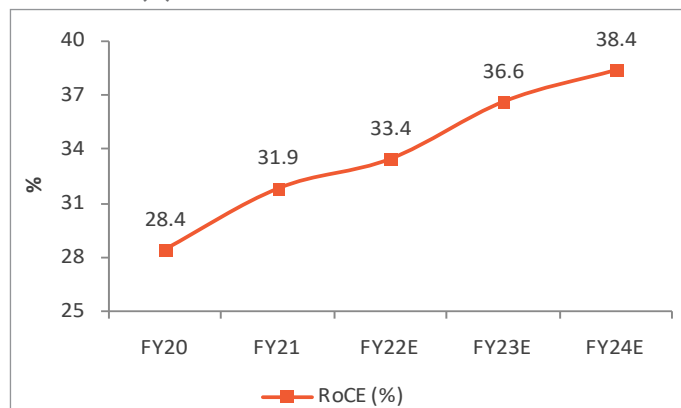
Source: Company, Sharekhan Research

RoE trend (%)



Source: Company, Sharekhan Research

RoCE trend (%)



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Technology spending to accelerate going forward

We believe the need for business continuity, operational resilience, and the switch to digital transactions have led to strong demand for IT services post the pandemic. Industry analysts such as Gartner estimate that IT services spending would grow by 8-8.5% in the next four years as compared to the average of 4.3% achieved over 2011-20. Consulting (+11%) and application implementation and managed services (+9%) are expected to grow faster than BPO (+7%) and infra implementation and managed services (+4%) in CY2022E. Forecasts indicate higher demand for Cloud infrastructure services, a potential increase in specialised software, potential investments in transformation projects by clients, and increased online adoption across verticals.

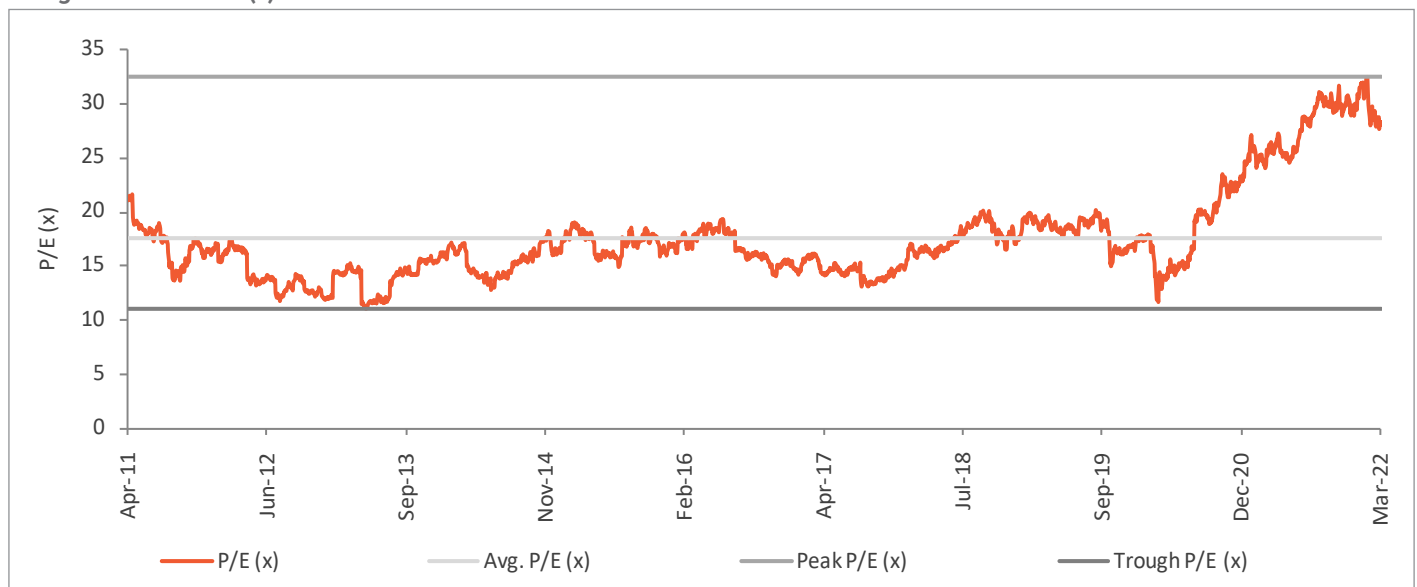
■ Company outlook - Well positioned to capture opportunities

Infosys services a large number of Fortune 500/Global 500 clients who have strong balance sheets and are able to hold on better amid the economic downturn. Further, Infosys has aggressively invested in digital technologies in the past few years to capture a large portion of upcoming digital and cloud transformation spends. Given strong relationships with clients and robust execution capabilities, Infosys is well positioned to capitalise on opportunities from clients' transformation journeys and report industry-leading organic revenue growth among peers in the medium-term.

■ Valuation - Maintain Buy with a PT of Rs. 2,300

We believe Infosys is well-equipped to deliver industry-leading organic growth among the large peers in the medium term. Though the company would face margin headwinds in the near term, we believe the pressure would reduce during FY2023E considering ease of supply side issues, pricing leverage and reduction in subcontractor expenses. Infosys is expected to report USD revenue and earnings growth of 13.4% and 14.1%, respectively, over FY2022-FY2024E. At CMP, the stock trades at 28x/25x its FY2023E/FY2024E earnings, which is justified, given strong growth potential, robust deal pipeline, and solid execution. We like Infosys because of its strong capabilities, a strong capital allocation policy, and prudent investments in capabilities that will be required in future. Hence, we maintain a Buy rating on the stock with an unchanged price target (PT) of Rs. 2,300.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Founded in 1981, Infosys is the second largest (\$13,562 million in FY2021) IT services company in India in terms of export revenue with headcount of 2.7 lakh employees. BFSI accounts for the largest chunk of revenue (~32% of total revenue), followed by retail, energy and utilities, and communication. Region wise, North America and Europe continue to be the mainstay. Digital revenue continued to have a strong growth momentum in the past few quarters and now contributes 58.5% to total revenue.

Investment theme

Infosys has accelerated deal wins momentum through engagement with deal advisors, consulting firms, and private equity players. Effectively, the strong large deal trajectory provides better revenue growth visibility. Further, revitalisation of sales and investment in digital competencies have certainly helped the company to drive its digital business. Sharp focus on execution and augmentation of digital capabilities through investments can bring Infosys back on its high-growth trajectory. Given strong deal wins, strengthening relationships with large clients, and continued digital momentum, we believe Infosys is well positioned to catch up with leaders on revenue growth in the coming years.

Key Risks

1) Regulatory visa norms could have an impact on employee expenses; 2) any instability in leadership; additional exits at senior management level; 3) Rupee appreciation and/or adverse cross-currency movements; and 4) increasing attrition rate.

Additional Data

Key management personnel

Nandan M. Nilekani	Co-founder and Non-Executive Chairman
Salil Parekh	Chief Executive Officer
Nilanjan Roy	Chief Financial Officer
Ravi Kumar S	President, Deputy COO
Mohit Joshi	President, Head – BFSI and HCLS

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Deutsche Bank Trust Co Americas	17.20
2	Life Insurance Corp of India	5.67
3	BlackRock Inc.	4.61
4	SBI Funds Management Pvt. Ltd.	3.15
5	The Vanguard Group Inc.	2.67
6	Republic of Singapore	1.81
7	ICICI Prudential Asset Management	1.43
8	UTI Asset Management Co Limited	1.23
9	Government Pension Fund – Global	1.10
10	Norges Bank	1.10

Source: Bloomberg

Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a position in the companies mentioned in the article.

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 deteriorating 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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