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Tel: +91-(0)22 4027 3300
Fax: +91-(0)22 6641 3377
www.khambattasecurities.com

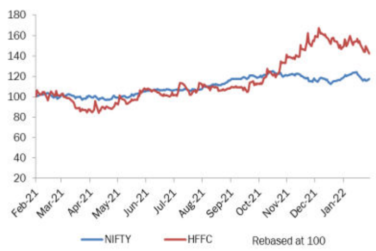
Home First Finance Company India Limited

01 February 2022

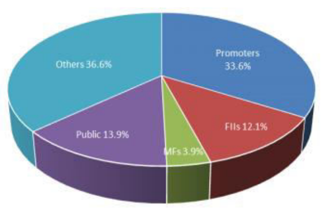
Niche home loan company with tech-driven operations — BUY

Sector	: Housing Finance
Target Price	: ₹ 988
Last Closing Price	: ₹ 753
Market Cap	: ₹ 6,598 crore
52-week High/Low	: ₹ 920/441
Daily Avg Vol (12M)	: 3,72,241
Face Value	: ₹ 2
Beta	: 0.59
Pledged Shares	: NIL
Year End	: March
BSE Scrip Code	: 543259
NSE Scrip Code	: HOMEFIRST
Bloomberg Code	: HOMEFIRS IN
Reuters Code	: HOMEFIRS.BO
NSE Nifty	: 17,340
BSE Sensex	: 58,014
Analyst	: Research Team

Price Performance



Shareholding Pattern



Initiating Coverage

Investment Summary

- Home First Finance Company India Limited (HFFC) is a technology-driven affordable housing finance company that targets first-time home buyers in the low and middle-income groups.
- India has a huge housing shortage and a lower percentage of home ownership than even many developing countries. The extremely low mortgage penetration levels in India compared to other countries presents a tremendous potential for growth of housing finance. With its focus on affordable housing finance, HFFC is well-positioned to benefit from the growing demand in the segment, driven by favourable policy initiatives.
- Through its focus on technology, HFFC has built a scalable operating model, which enables expansion of operations and drive revenue growth with lower incremental costs. The digital service delivery mechanisms and operating model bring uniformity in operations, increases customer satisfaction and aids in expansion across high-growth geographies.
- With a diversified geographical presence and a strong branch network, HFFC's has 187 touchpoints with the company targeting 80+ physical branches by end of FY22 and ~140 branches by FY24.
- HFFC utilizes a diverse range of lead-sourcing channels such as connectors, architects, contractors and affordable housing developers, in addition to conducting loan camps and micro-marketing activities, and utilizing employee and customer referrals and branch walk-in customers.
- HFFC serves a niche segment of the Indian home loans market, primarily comprising salaried home-buyers, accounting for 73% of loans. The average ticket size of HFFC's housing loans is ₹ 10.1 lakh.
- We expect strong growth in earnings and ROE, driven by healthy expansion in HFFC's loan book without compromising on asset quality. We initiate coverage on HFFC with a BUY based on a price target of ₹ 988 at a P/B ratio of 4.3x FY24E BVPS, informing an upside potential of 31% from current levels.

Key Financial Metrics

₹ crore	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
Net revenues	144.5	225.8	269.0	392.2	485.3	613.8
PPOP	72.6	123.8	166.2	262.6	316.9	393.2
PBT	65.3	107.3	134.0	226.0	270.3	330.8
PAT	45.7	79.6	100.1	169.1	202.2	247.6
PAT margin	*16.9%*	*19.0%*	*20.5%*	*27.2%*	*25.6%*	*24.3%*
Diluted EPS (₹)	7.74	10.57	12.18	19.35	23.14	28.32
BVPS (₹)	413	119	158	177	200	229

Source: Company data, Khambatta Research

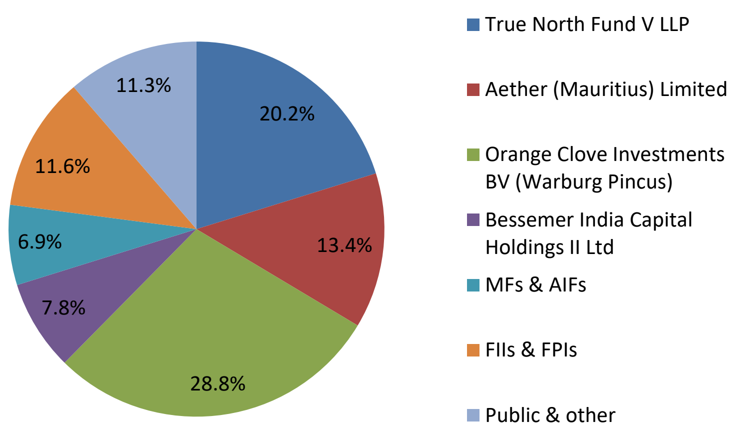
HFFC has a network of 76 branches covering 92 districts across 12 states and a union territory

Company Profile

Home First Finance Company India Limited (HFFC) is a technology-driven affordable housing finance company that targets first-time home buyers in the low and middle-income groups. The company's principal product is housing loan for the purchase or construction of homes, which comprised 91% of its gross loan assets as of December 2021. Salaried home-buyers comprise HFFC's primary customer category, accounting for 73% of gross loans while self-employed customers accounted for 26% of gross loans, as of the end of 3Q FY22. The company also offers other types of loans such as loan against property, developer finance loan, and loan for purchase of commercial property. The average ticket size of HFFC's housing loans is ₹ 10.1 lakh with an average loan-to-value ratio of 48.8%. HFFC has a network of 76 branches covering 92 districts across 12 states and a union territory (UT) with a significant presence in urbanized regions in the states of Gujarat, Maharashtra, Karnataka and Tamil Nadu. The company's credit rating has improved from 'ICRA A-' as of FY17-end to 'ICRA A+' currently.

Founded by Mr Jaithirth Rao, Mr P. S. Jayakumar and Mr Manoj Viswanathan, HFFC commenced operations in August 2010. The company is managed by professionals and promoted by True North Fund V LLP and Aether (Mauritius) Limited. Further, Bessemer and Orange Clove Investments BV (an affiliate of global private equity major Warburg Pincus) has acquired a stake in the company. HFFC listed on the stock exchanges on 03 February 2021 after successfully completing an IPO of over Rs 1,100 crore, comprising a fresh issue of Rs 265 crore.

Shareholding as of January 2022



Source: HFFC presentation

Investment Thesis

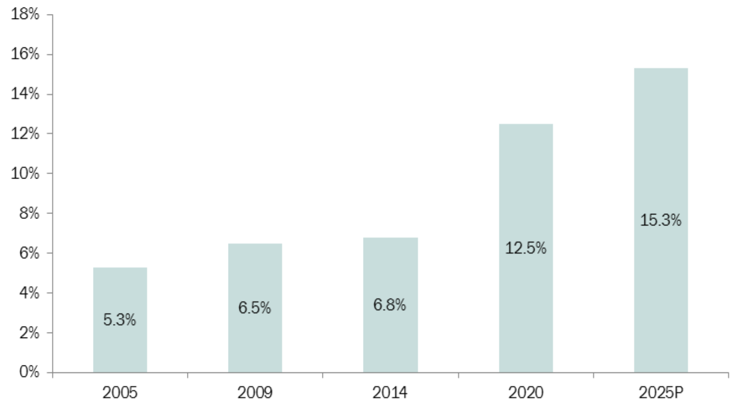
The affordable housing segment presents robust growth potential

The disbursements market share of housing finance companies increased from 37% in FY15 to 45% in FY19

India has a huge housing shortage and a lower percentage of home ownership than even many developing countries. This, together with the rapid economic growth the country has seen in the past few decades, increasing urbanization and rising incomes have led to an increasing demand for housing. The government's incentives for affordable housing, lower interest rates and easier availability of credit have all contributed to the rising demand for home ownership. The government’s “Housing for All” programme comprises the Credit Linked Subsidy Scheme (CLSS), which, as of 31 March 2021, had benefited an estimated 1.13 crore first-time homebuyers. Under this scheme, the interest subsidy on the home loan is paid to the beneficiary upfront, thereby reducing the amount of the outstanding amount and, consequently, the EMI. Affordable housing is also supported by tax incentives with developers getting 100% deduction on profits on affordable housing projects. In terms of disbursements, the share of housing finance companies increased from 37% in FY15 to 45% in FY19. With its focus on affordable housing finance, HFFC is well-positioned to benefit from the growing demand in the segment.

The extremely low mortgage penetration levels in India compared to other countries presents a tremendous potential for growth of housing finance. In FY20, India's mortgage-to-GDP ratio stood at 12.5%, which, although still low compared with other developing countries, improved significantly from 6.5% in FY09. The factors that contributed to this improvement are rising incomes, improving affordability, growing urbanisation and nuclearisation of families, emergence of tier-II and tier-III cities, ease of financing, tax incentives, and the widening reach of financiers. CRISIL Research sees the mortgage-to-GDP ratio to continue to grow steadily, reaching 15.3% by FY25.

Mortgage-to-GDP ratio in India



Source: CRISIL, Khambatta Research

Driven by technology

HFFC employs technology in the origination, underwriting, and servicing stages of the loan cycle. Its focus on tech-driven business processes helped it during the covid period, enabling the company to follow all safety protocols while interacting with customers and ensuring safety of customers as well as of the employees.

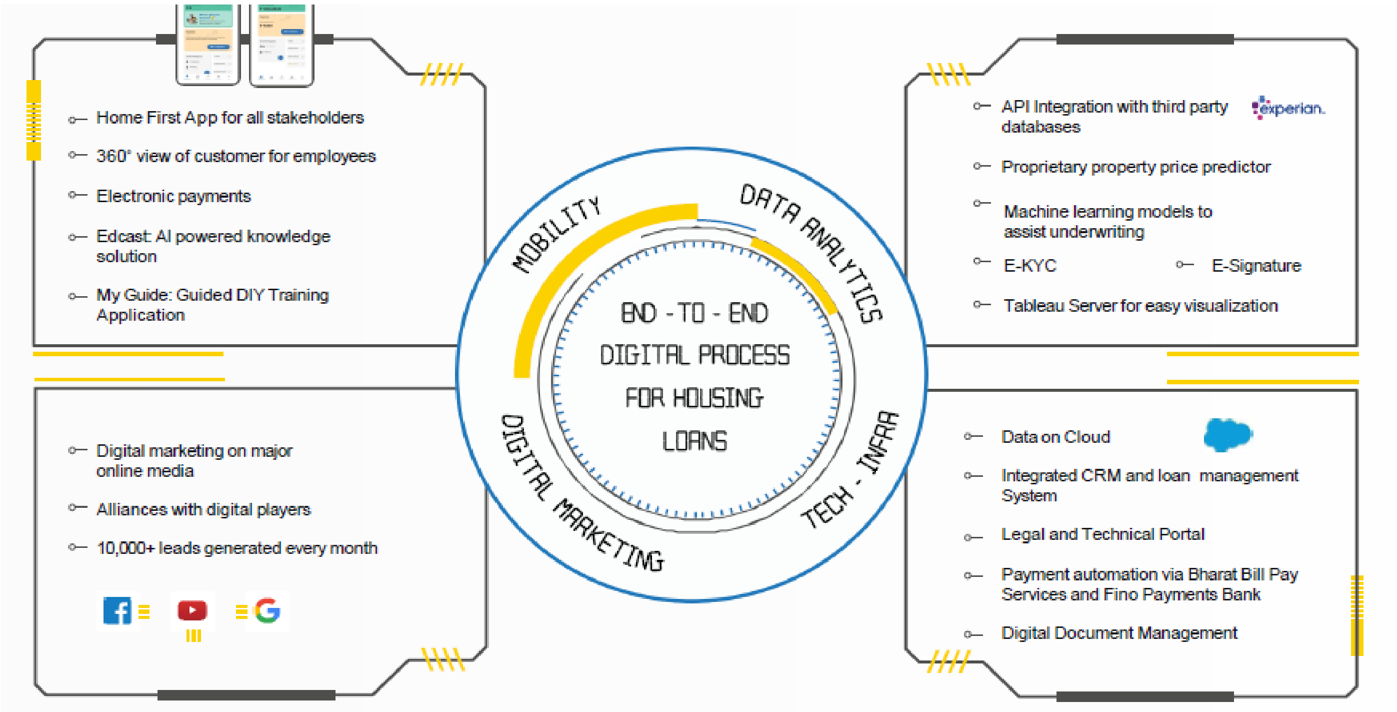
The use of technology enables HFFC to digitally capture over 100 data points of a customer

Through its focus on technology, HFFC has built a scalable operating model, which enables expansion of operations and drive revenue growth with lower incremental costs. It has established a differentiated technology framework with customized systems and tools, enhancing convenience for customers as well as increasing operational efficiency. Over the last three financial years and 1H FY21, the company invested approximately ₹ 20 crore in information technology systems. The use of technology enables the company to digitally capture over 100 data points of a customer in addition to credit bureau data, observations of front end teams, and feedback from their underwriting and management teams. HFFC captures and stores all this data on a cloud services platform. The company has also entered into arrangements with third party service providers through whom it obtains additional information such as fraud-related data, banking-, investment- and taxation-related data, and vehicle ownership of customers, which helps in identifying areas of concern and take quick and accurate decisions. The integrated customer relationship management and loan management system provides a holistic view of customers and ensures connectivity and uniformity across branches.

HFFC has also deployed proprietary machine learning customer-scoring models to assist in effective credit underwriting. The seamless integration and availability of data across platforms and users enable the company to process loans in a paperless manner and with quick turnaround times. HFFC offers mobility solutions through dedicated mobile applications for its customers to enable quick and transparent loan-related transactions as well as for its sales channels to facilitate easy capture of leads and access to real time status of loans. It uses a data lake to store the data from all different applications which expedites data consolidation, visualization, machine learning model development, and model implementation. The data lake facilitates detailed analytics, leading to better operational decisions. HFFC's information technology systems aid in leveraging economies of scale to increase productivity and reduce turnaround times and transaction costs. The company's systems are designed to facilitate a sanction within an average turnaround time of 48 hours, which is calculated from the time all customer information is collated in the database to the sanctioning of the loan. In addition, digital service delivery mechanisms and operating model bring uniformity in operations, increases customer satisfaction and aids in expansion of business in geographies that offer growth opportunities.

HFFC's systems are designed to facilitate a sanction within an average turnaround time of 48 hours

HFFC's tech-driven operating model



Source: HFFC presentation

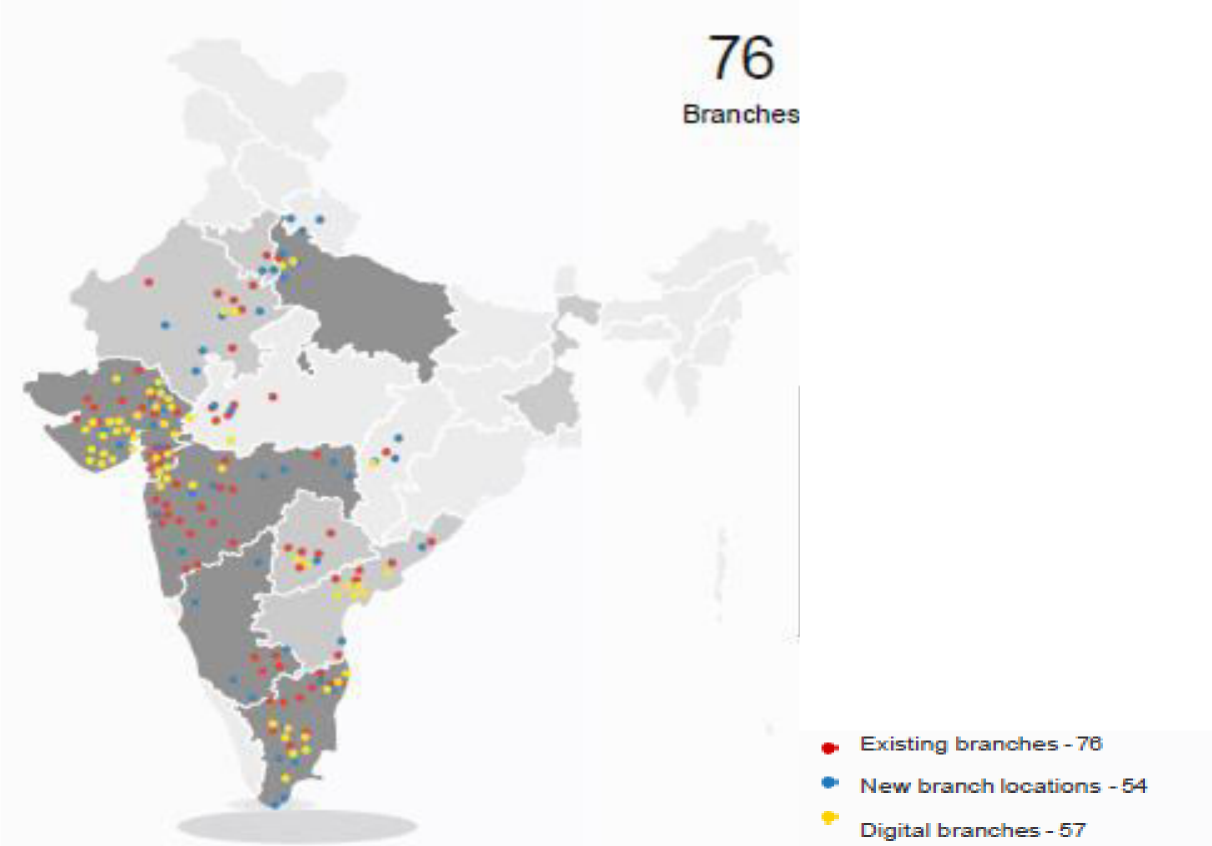
Diversified geographical presence and strong branch network

HFFC has a strong network of 76 branches in India, spread across 92 districts in 12 states/UTs with a significant presence in urbanized regions in the states of Gujarat, Maharashtra, Karnataka and Tamil Nadu. It has commenced business in 4 new physical branches and 7 new branch locations with digital presence in 15 more locations during 3QFY22. The total number of touchpoints currently stands at 187 with the company targeting 80+ physical branches by end of FY22 and ~140 branches by FY24.

Gujarat contributes 37% of HFFC's gross loan assets while Maharashtra is the second largest market at 17% of loans

HFFC has the maximum number of branches (20) in Gujarat, contributing nearly 37% of the total gross loan assets as of December 2021. Maharashtra is the second largest contributor (16.7%) after Gujarat with 17 branches. The company has a decent presence in the four southern states of Andhra Pradesh, Telangana, Tamil Nadu and Karnataka as it plans to cover all the large towns in these states. Apart from the above six states, HFFC is also present in Madhya Pradesh, Chhattisgarh, Rajasthan and Uttar Pradesh. The company has increased the scale of its operations and grown branches by adopting a strategy of contiguous expansion across regions and have strategically expanded to geographies where there is substantial demand for housing finance. According to a CRISIL report, the 11 states and the UT in which HFFC has presence accounted for approximately 79% of the affordable housing finance market in India during FY19.

HFFC's branch network



Source: HFFC presentation

HFFC's geographic footprint

States/Territories	Number of		Percentage of gross loan assets as on			
	Branches	*Districts*	Q3FY22	*FY21*	*FY20*	*FY19*
Gujarat	20	22	37.0%	38.2%	39.7%	40.8%
Maharashtra	17	15	16.7%	19.2%	21.7%	28.4%
Tamil Nadu	11	16	12.0%	11.1%	9.9%	8.5%
Karnataka	4	5	8.3%	9.1%	9.0%	8.2%
Rajasthan	6	5	5.7%	5.5%	5.0%	3.8%
Telangana	5	4	6.8%	5.5%	4.9%	3.2%
Madhya Pradesh	5	6	4.7%	4.4%	3.9%	2.6%
Uttar Pradesh & Uttarakhand	1	6	3.6%	2.9%	2.6%	2.0%
Haryana & NCR	1	3	0.9%	1.0%	1.1%	1.3%
Chhattisgarh	1	4	1.4%	1.2%	0.9%	0.8%
Andhra Pradesh	5	6	2.9%	1.9%	1.3%	0.4%
Total	**76**	**92**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

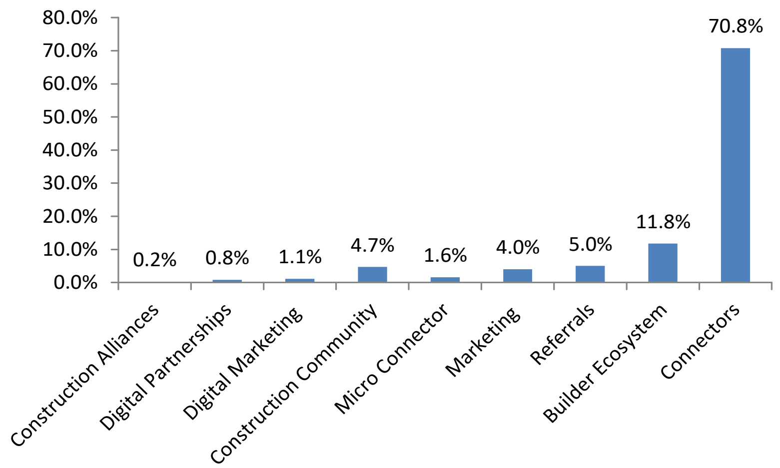
Source: HFFC presentation

Diversified/differentiated sourcing channels

HFFC's network of connectors increased from 470 in March 2018 to over 800 as of September 2020

HFFC utilizes a diverse range of lead-sourcing channels such as connectors, architects, contractors and affordable housing developers, in addition to conducting loan camps and micro-marketing activities, and utilizing employee and customer referrals and branch walk-in customers. Connectors are third-parties supplying customer leads on a commission basis are paid only when a loan is disbursed and they do not assist in the loan application process. Connectors are individuals such as insurance agents, tax practitioners and local shopkeepers. The network of connectors increased from approximately 470 active connectors as of 31 March 2018 to over 800 as of 30 September 2020. During FY20 and 1H FY21, the company sanctioned 15,591 and 2,591 loans on account of leads generated through 2,553 and 887 connectors, respectively. HFFC has further entered into arrangements with certain digital lead aggregators and other digital players within the housing and real estate ecosystem, which helps it in sourcing leads with embedded customer data. The company's presence in the most relevant housing finance markets in India and diversified lead sourcing channels has resulted in an increase in its gross loan assets and disbursements over the years.

Lead generation channels as of December 2021



Source: HFFC presentation

Niche customer base

The average ticket size of HFFC's housing loans is ₹ 10.1 lakh

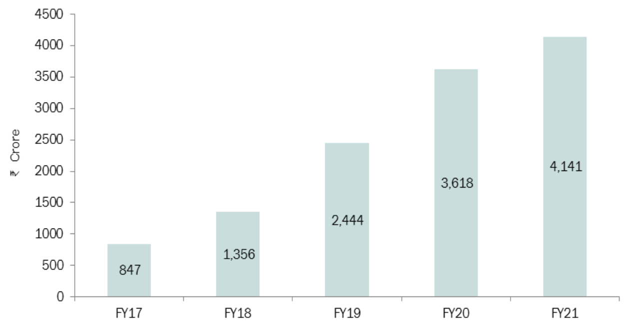
HFFC serves a niche segment of the Indian home loans market consisting of a niche customer base. The company's primary customer category comprises salaried home-buyers, accounting for 73% of its gross loans while self-employed customers accounted for 26% of gross loans, as of the end of 3Q FY22. The average ticket size of HFFC's housing loans is ₹ 10.1 lakh with an average loan-to-value ratio of 48.8%. As a majority of middle-income people taking home loans are end-users, small-ticket housing loans have relatively lower defaults and, consequently, a better credit risk profile compared to other personal loans. Further, demand for housing, especially on the lower end of the value spectrum, tends to be relatively inelastic even in a higher interest rate environment or during short-term economic slowdowns.

Strong growth in AUM, disbursements and profit

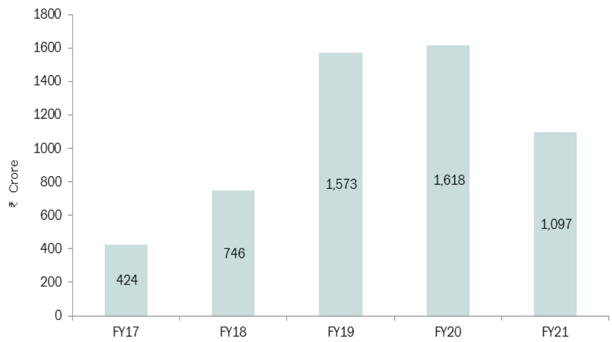
HFFC registered 45% CAGR in AUM over FY18 to FY21

HFFC witnessed strong growth (45% CAGR) in AUM over the past 3 years (FY18 to FY21). During 3QFY22, AUM grew by 26.7% to ₹4,994 crore as we expect the loan book to grow by 30% and 33% in FY23 and FY24 respectively. After registering a dip in disbursements in FY21, HFFC reported an all-time high disbursement during the quarter ended 31 December 2021 to ₹5,696 crores (+63.3% y-o-y). The total number of loan accounts has also been on a consistent rise with 50,417 loan accounts as of the end of FY21. The company registered a strong growth in profits despite maintaining high liquidity and conservative covid provisioning. We forecast PAT to grow by 20% and 22% for FY23 and FY24, respectively.

AUM

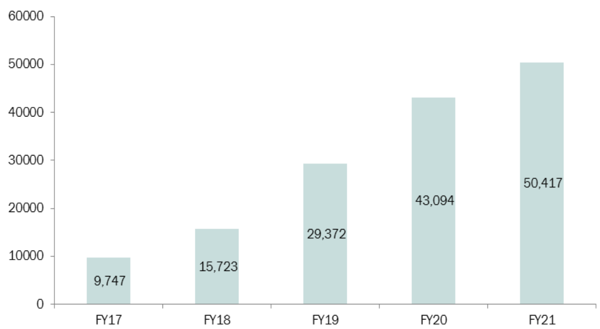


Disbursements

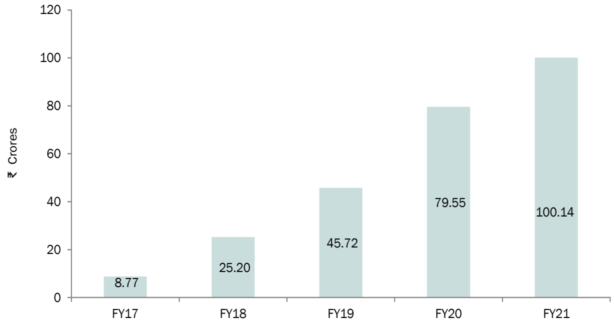


Source: Company data, Khambatta Research

Number of loan accounts



PAT



Source: Company data, Khambatta Research

Peer Comparison

We compare HFFC with listed housing finance companies operating in the affordable housing segment.

Peer Comparison: Key Financials Metrics, FY21

₹ Crore	HFFC	Aavas Financiers Ltd	Aptus Value Housing Finance India Ltd	PNB Housing Finance Ltd	Can Fin Homes Ltd
Total income	489.2	1,105.5	655.2	7,624.1	2,018.4
PAT	100.1	288.9	266.9	929.9	456.1
EPS (₹)	12.2	36.5	5.5	55.3	34.2
ROA	2.2%	3.2%	5.9%	1.3%	2.1%
ROE	7.2%	12.0%	13.5%	10.4%	17.5%
Current market cap	6,598	22,686	17,964	7,345	8,204

Source: Company data, Khambatta Research

Valuation

We initiate coverage on HFFC with a BUY at 4.3x FY24E BVPS, informing a price target of ₹ 988 and an upside potential of 31%

HFFC currently trades at FY24E forward P/E and P/B multiples of 26.6x and 3.3x

HFFC reported 36.9% y-o-y growth in NII to ₹ 71.7 crores as net revenues increased to ₹ 24.7 crore in 3Q FY22. PAT grew by ~190% to ₹ 45.9 crore during the period. Asset quality remained stable with a GNPA and NNPA ratios of 1.7% and 1.3% as of the end of 3Q FY21. The company looks to grow aggressively by doubling its branches over the next couple of years. Going forward, we have modelled NII to increase by 30% and 33% and net revenues by 24% and 26%, driven by loan book growth of 30% and 33% over FY23 and FY24, respectively, without compromising on its asset quality. We expect PAT to increase by 20% and 22% as PPOP is seen expanding by 21% and 24% in FY23 and FY24. The robust growth in PAT will translate into healthy expansion of ROA and ROE. The HFFC stock is currently trading at FY24E forward P/E and P/B multiples of 26.6x and 3.3x, respectively. Triangulating by averaging the values arrived at by the P/E and P/B methods, we initiate coverage on HFFC with a BUY at 4.3x FY24E BVPS, informing a price target of ₹ 988 and an upside potential of 31%.

Valuation

	Target Multiple	Target Price (₹)
P/E	35.0x	991
P/B	4.3x	984
Average		988

Source: Khambatta Research

Profit & Loss Account

₹ crore	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
Net interest income	105.5	161.0	203.5	270.5	352.1	468.3
Non-interest income	39.0	64.8	65.5	121.7	133.2	145.5
Net revenues	144.5	225.8	269.0	392.2	485.3	613.8
Operating expenses	67.3	94.8	95.2	122.0	160.0	211.1
Depreciation & amortization	4.6	7.2	7.6	7.6	8.5	9.5
PPOP	72.6	123.8	166.2	262.6	316.9	393.2
Provisions & impairment of assets	7.3	16.5	32.2	36.6	46.6	62.3
PBT	65.3	107.3	134.0	226.0	270.3	330.8
Tax expense	(19.6)	(27.8)	(33.9)	(56.9)	(68.0)	(83.3)
PAT	45.7	79.6	100.1	169.1	202.2	247.6
PAT margin	*16.9%*	*19.0%*	*20.5%*	*27.2%*	*25.6%*	*24.3%*
Diluted EPS (₹)	7.74	10.57	12.18	19.35	23.14	28.32

Source: Company data, Khambatta Research

Key Balance Sheet Items

₹ crore	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
Total shareholders' equity	522.7	933.4	1,380.5	1,549.7	1,751.9	1,999.5
Total debt	1,925.6	2,493.8	3,053.7	3,840.8	4,993.0	6,640.7
Loans	2,134.7	3,013.9	3,326.5	4,174.8	5,427.2	7,218.2
Investments	102.9	145.6	375.0	459.4	546.7	650.5

Source: Company data, Khambatta Research

Ratio Analysis

	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
GNPA	0.8%	1.0%	1.8%	1.8%	1.7%	1.6%
NPA	0.6%	0.8%	1.2%	1.2%	1.1%	1.0%
NIM	5.9%	5.9%	5.8%	6.2%	6.4%	6.5%
Operating cost / Total income	24.8%	22.6%	19.5%	19.6%	20.3%	20.7%
ROA	1.8%	2.3%	2.2%	3.1%	3.0%	2.8%
ROE	8.7%	8.5%	7.2%	10.9%	11.5%	12.4%
BVPS (₹)	413	119	158	177	200	229

Source: Company data, Khambatta Research

Tel: +91-(0)22 4027 3300
Fax: +91-(0)22 6641 3377
www.khambattasecurities.com

Key Risks

- With the prospects for affordable housing dependent to a large extent on government policies and budgetary allocations, any significant policy changes can potentially affect our outlook and forecast.
- With many smaller and big housing finance companies as well as banks present in the market, many of them with access to cheaper funds, further intensification of competition amongst existing and new players poses a risk to HFFC's growth and margins.
- Further severe and/or prolonged waves of covid-19 or other disruptions in the housing market can potentially have a negative impact on HFFC's AUM growth as well as asset quality.

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Guide to Khambatta's research approach

Valuation methodologies

We apply the following absolute/relative valuation methodologies to derive the 'fair value' of the stock as a part of our fundamental research:

DCF: The Discounted Cash Flow (DCF) method values an estimated stream of future free cash flows discounted to the present day, using a company's WACC or cost of equity. This method is used to estimate the attractiveness of an investment opportunity and as such provides a good measure of the company's value in absolute terms. There are several approaches to discounted cash flow analysis, including Free Cash Flow to Firm (FCFF), Free Cash Flow to Equity (FCFE) and the Dividend Discount Model (DDM). The selection of a particular approach depends on the particular company being researched and valued.

ERE: The Excess Return to Equity (ERE) method takes into consideration the absolute value of a company's return to equity in excess of its cost of equity discounted to the present day using the cost of equity. This methodology is more appropriate for valuing banking stocks than FCFF or FCFE methodologies.

Relative valuation: In relative valuation, various comparative multiples or ratios including Price/Earnings, Price/Sales, EV/Sales, EV/EBITDA, Price/Book Value are used to assess the relative worth of companies which operate in the same industry/industries and are thereby in the same peer group. Generally our approach involves the use of two multiples to estimate the relative valuation of a stock.

Other methodologies such as DuPont Analysis, CFROI, NAV and Sum-of-the-Parts (SOTP) are applied where appropriate.

Stock ratings

Buy recommendations are expected to improve, based on consideration of the fundamental view and the currency impact (where applicable) by at least 15%.

Hold recommendations are expected to improve, based on consideration of the fundamental view and the currency impact (where applicable) between 5% and 15%.

Sell recommendations are expected to improve up to 5% or deteriorate, based on consideration of the fundamental view and the currency impact (where applicable).

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