Clean Science & Technology

Ongoing capex on track amidst lingering demand challenges
- Clean Science (CLEAN) missed our 1QFY24 EBITDA estimate, with a gross margin of 61.4% (vs. expected 69.8%), due to increased raw material costs and sales decline. EBITDAM stood at 40.5% (vs. 39% in 1QFY23). FMCG Chemicals grew QoQ in 1QFY24, while Performance Chemicals and Pharma & Agro Intermediates declined.
- The management attributed the sales decline to 2/3rd volume decrease and 1/3rd lower prices. However, the company maintained its market share as the overall market also declined, adversely impacting product volumes. The current product prices are at their lowest, but the management does not anticipate further declines, due to increasing raw material costs linked to rising crude prices.
- The company launched HALS701 and HALS770 in Dec ’22 and started fulfilling commercial orders in 4QFY23. However, the uptake has been slower due to reduced global demand for master batches. The current p-BQ utilization stands at ~20%, falling short of the expected specifications. However, a recovery is anticipated in the next three months, which is likely to result in a decreasing trend in p-BQ imports.
- The HALS expansion in Unit IV will cost INR 1.8b and is scheduled to be commissioned by Dec ’23, adding 15ktpa capacity (including 2ktpa from Unit III). Additionally, the company plans INR 2b worth of capex for new products, targeted to be operational by end-1HFY25.
- We anticipate continued demand challenges in 2QFY24. Consequently, we have revised down our revenue estimate by 13%, and EBITDA/EPS estimate by 14% each for FY24, and revenue/EBITDA/EPS estimates by 7% each for FY25. The stock is currently trading at 41x FY25E P/E with an EPS of INR 31.5 and 29x FY25E EV/EBITDA. Our target price is INR 1,260, based on 40x FY25E P/E.
- We reiterate our Neutral rating on the stock.

Miss led by lower sales and higher RM costs; sharp sequential decline in margin
- The company reported revenue below our estimates at INR1.9b (-14% est., -20% YoY)
- Gross margin stood at 61.4% (down 910bp QoQ, was at 61% 1QFY23).
- EBITDA margin stood at 40.5% (down 800bp QoQ, was at 39% in 1QFY23).
- EBITDA stood at INR761m (our est. at INR1b, down 17% YoY).
- PAT came in at INR589m (our est. at INR743m, down 6% YoY).

Segmental highlights
- Revenues from Pharma Chemicals stood at INR357m (down 34% YoY). Both volumes and realization declined with volumes declining more than realization
Revenues from **Performance Chemicals** stood at INR1.3b (down 18% YoY). Both volumes and realization declined with volumes declining more than realization.

Revenues from **FMCG Chemicals** stood at INR245m (up 4% YoY). Volumes increased but realization declined.

### Other highlights

- Revenue from the domestic market stood at 37%, while the rest was exports.
  - The domestic market was less impacted than the exports market.
  - Revenue share from Americas increased in the quarter.
- CLEAN incurred a total capex of INR900m in 1QFY24 (INR1.9b in FY23). The construction work for Clean Fino-Chem Ltd. remains on track as per the latest update.
  - Investment in subsidiary includes INR850m.

### Valuation and view

- CLEAN is actively pursuing R&D and has entered the HALS series, which has an estimated global market size of USD 1b. It is the first Indian company to develop the HALS series and is also working on other products in its R&D pipeline. Additionally, the company has declared a capex of INR 2b for new products, with further details to be announced later in FY24.
- CLEAN is expected to generate INR 2.8b in FCF during FY24-25, with a planned capex of INR 4b for the same period. The company plans to finance this capex through internal accruals and is projected to maintain a net cash position in the future.
- The stock is currently trading at 41x FY25E P/E with an EPS of INR 31.5 and 29x FY25E EV/EBITDA. Our target price is INR1,260, based on 40x FY25E EPS. We maintain a Neutral rating on the stock.

<table>
<thead>
<tr>
<th>Consolidated - Quarterly Snapshot</th>
<th>FY23</th>
<th>FY24</th>
<th>FY23</th>
<th>FY24E</th>
<th>FY24E</th>
<th>Var.</th>
<th>(INR m)</th>
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<tbody>
<tr>
<td>Y/E March</td>
<td>1Q</td>
<td>2Q</td>
<td>3Q</td>
<td>4Q</td>
<td>1Q</td>
<td>2Q</td>
<td>3Q</td>
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<td>2,169</td>
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<td>2,543</td>
<td>2,832</td>
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<td>61.6</td>
<td>31.3</td>
<td>6.0</td>
<td>19.6</td>
<td>2.7</td>
<td>3.2</td>
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<td>Gross Margin (%)</td>
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<td>1,045</td>
<td>1,134</td>
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<tr>
<td>PBT</td>
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<td>31.3</td>
<td>30.7</td>
<td>30.0</td>
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</table>

### Segment-wise Revenue (INR m)

- **Performance Chemicals**: 1,545, 1,645, 1,688, 1,582, 1,260, 1,851, 2,105, 2,126, 6,457, 4,912, 1,608, -22
- **Pharma & Agro Intermediates**: 538, 432, 380, 428, 357, 404, 430, 405, 1,778, 1,240, 338, 6
- **FMCG Chemicals**: 234, 296, 285, 215, 245, 263, 269, 1,029, 795, 207, 18
- **Others**: 23, 102, 24, -56, 19, 25, 28, 23, 94, 70, 33, -44

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3 August 2023
Highlights from the management interaction

- This year is expected to be characterized by benign inflation and a stable supply chain.
  - As a result, destocking is likely to occur, making this year a buyers’ market, in contrast to the sellers’ market experienced last year
    - Leading to reduced volumes and sales realization
- No significant loss in market share of the company. Overall market has declined because of which volumes have declined in the quarter.
- One-time gain of INR90m was recorded in 1QFY23, which got adjusted in last years’ consolidated results.
  - Therefore, earnings declined only 6% YoY even as sales is down 20% YoY in 1QFY24.
- All capex continues to be incurred through internal accruals.
- 2/3rd decline because of volumes and 1/3rd decline because of prices in 1QFY24
  - Current prices are the worst ever seen by the company and the management does not expect further decline in prices.
  - FG prices are not expected to go below current prices with crude prices also increasing once again.
- The DCC plant is currently operating at 80% utilization, and Guaiacol has seen significant demand due to issues with cough syrup in Indonesia and Iraq, both of which are being supplied by India.
  - Taiwan and Chinese customers are expected to offset lost volumes from Indian customers.
  - The company could go for plan B if pharma demand for Guaiacol does not pick up fast enough.
- HALS offtake is currently slower due to slower-than-expected demand for master batches of the product worldwide.
  - Less than 50% capacity utilization, expect to touch 50% capacity utilization by the next two quarters.
  - Revenues to start flowing in from the new HALS capacities (under the WOS) from FY25.
- ‘Other income’ was higher because of forex gain of INR56m and treasury gain of INR60m.
- TBHQ was primarily undertaken to cater to the demand of the existing customers of BHA and AP.
- Hydroquinone is being sourced through the overseas market by the customers.
- The company is facing issues with obtaining the specific color (yellow) required for P-BQ, leading to an increase in imports into the country, while domestic supplies are currently limited.
  - Management expects these issues to subside within the next three months.
  - P-BQ utilizations stands at 20%.
- Average utilization levels stood at 60%/ 62%/ 70% for Performance Chemicals/ Pharma & Agro Intermediates/ FMCG Chemicals.
- Demand issues continue to exist in 2QFY24 as well; management expects markets to rebound in 2HFY24.
- New products would be in performance Chemicals and pharma and agro intermediates.
1QFY24 story in charts

Exhibit 1: Revenue declined 13% QoQ and 20% YoY... 

- Gross Sales (INR b) 
- Growth YoY (%)

Source: Company, MOFSL

Exhibit 2: ...with GM and EBITDAM expanding 

- Gross Margin (%) 
- EBITDA margin (%)

Source: Company, MOFSL

Exhibit 3: EBITDA declined 28% QoQ and 17% YoY 

- EBITDA (INR b) 
- Growth YoY (%)

Source: Company, MOFSL

Exhibit 4: PAT declined 27% YoY and 6% QoQ 

- PAT (INR b) 
- Growth YoY (%)

Source: Company, MOFSL

Exhibit 5: Revenue from Perf. and Pharma & Agro Chemicals declined QoQ but increased for FMCG Chemicals in 1Q... 

- Others 
- FMCG Chemicals 
- Pharma & Agro Intermediates 
- Performance Chemicals 
- Segment-wise Revenue (INR b)

Source: Company, MOFSL

Exhibit 6: ...with the share of FMCG Chemicals in the overall mix improving to 33% and declining for perf. chemicals 

- Others 
- FMCG Chemicals 
- Pharma & Agro Intermediates 
- Performance Chemicals 

Revenue Mix (%)

Source: Company, MOFSL
Exhibit 7: Domestic sales declined 14% YoY and grew 8% for RoW

Source: Company, MOFSL

Exhibit 8: Contribution from domestic market increased

Geographical mix (%)

Source: Company, MOFSL

Exhibit 9: Contribution from India and RoW increased, while it declined for Europe and China QoQ

Region wise Mix (%)

Source: Company, MOSL
Clean Science

Financial story in charts

Exhibit 10: Expect 18% revenue CAGR over FY23-25...

- FMCG Chemicals
- Pharma & Agro Intermediates
- Performance Chemicals
- Total Revenue

INR b

Source: Company, MOFSL

Exhibit 11: ...driven by contribution from Performance Chemicals

- Others
- FMCG Chemicals
- Pharma & Agro Intermediates
- Performance Chemicals

Source: Company, MOFSL

Exhibit 12: EBITDA margin to normalize with commissioning of HALS and capacity ramp up of the same...

INR b

Source: Company, MOFSL

Exhibit 13: ...and commissioning of new products by end-1HFY25 in the subsidiary CFCL

INR b

Source: Company, MOFSL

Exhibit 14: Return profile to moderate vs. FY21 due to capacity additions (at unit III and IV) ...

Source: Company, MOFSL

Exhibit 15: ...and capex of INR4b (to be funded via internal accruals) over FY24-25

Source: Company, MOFSL
## Financials and valuations

### Consolidated - Financial Snapshot  
(INR m)

<table>
<thead>
<tr>
<th>Y/E March</th>
<th>FY18</th>
<th>FY19</th>
<th>FY20</th>
<th>FY21</th>
<th>FY22</th>
<th>FY23</th>
<th>FY24E</th>
<th>FY25E</th>
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</thead>
<tbody>
<tr>
<td>Total Income from Operations</td>
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<td>6,849</td>
<td>9,358</td>
<td>9,435</td>
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<td>Change (%)</td>
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<td>63.1</td>
<td>6.6</td>
<td>22.2</td>
<td>33.7</td>
<td>36.6</td>
<td>0.8</td>
<td>19.7</td>
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<td>Gross Margin (%)</td>
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<td>75.9</td>
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<td>2,999</td>
<td>4,021</td>
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<td>Margin (%)</td>
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<td>172</td>
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<td>1,823</td>
<td>2,673</td>
<td>3,048</td>
<td>3,956</td>
<td>3,810</td>
<td>4,472</td>
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<tr>
<td>PBT after EO Exp.</td>
<td>699</td>
<td>1,365</td>
<td>1,823</td>
<td>2,673</td>
<td>3,048</td>
<td>3,956</td>
<td>3,810</td>
<td>4,472</td>
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<td>1,396</td>
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<td>2,851</td>
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<td>1,984</td>
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### Consolidated - Balance Sheet  
(INR m)

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<th>Y/E March</th>
<th>FY18</th>
<th>FY19</th>
<th>FY20</th>
<th>FY21</th>
<th>FY22</th>
<th>FY23</th>
<th>FY24E</th>
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<td>Curr. Liability &amp; Prov.</td>
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<td>390</td>
<td>749</td>
<td>1,023</td>
<td>1,350</td>
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<td>Other Current Liabilities</td>
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<td>162</td>
<td>387</td>
<td>408</td>
<td>324</td>
<td>370</td>
<td>373</td>
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<td>Provisions</td>
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<td>5</td>
<td>8</td>
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<tr>
<td>Net Current Assets</td>
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<td>2,587</td>
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<td>Appl. of Funds</td>
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<td>15,417</td>
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## Financials and valuations

### Ratios

<table>
<thead>
<tr>
<th>Y/E March</th>
<th>FY18</th>
<th>FY19</th>
<th>FY20</th>
<th>FY21</th>
<th>FY22</th>
<th>FY23</th>
<th>FY24E</th>
<th>FY25E</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Basic (INR)</strong></td>
<td></td>
<td></td>
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<tr>
<td>EPS</td>
<td>4.6</td>
<td>9.2</td>
<td>13.1</td>
<td>18.7</td>
<td>21.5</td>
<td>27.8</td>
<td>26.8</td>
<td>31.5</td>
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<tr>
<td>EPS Growth (%)</td>
<td>3.9</td>
<td>100.7</td>
<td>43.0</td>
<td>42.1</td>
<td>15.2</td>
<td>29.2</td>
<td>-3.4</td>
<td>17.4</td>
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<tr>
<td>Cash EPS</td>
<td>5.3</td>
<td>10.2</td>
<td>14.4</td>
<td>20.3</td>
<td>23.9</td>
<td>31.2</td>
<td>31.1</td>
<td>36.1</td>
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<tr>
<td>BV/Share</td>
<td>17.7</td>
<td>25.6</td>
<td>32.2</td>
<td>50.8</td>
<td>72.3</td>
<td>95.1</td>
<td>117.1</td>
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<td>DPS</td>
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<td>1.0</td>
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<td>5.0</td>
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<td>5.7</td>
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<tr>
<td>Payout (%)</td>
<td>4.7</td>
<td>9.5</td>
<td>7.4</td>
<td>1.7</td>
<td>15.1</td>
<td>18.0</td>
<td>18.0</td>
<td>18.0</td>
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<tr>
<td><strong>Valuation (x)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>P/E</td>
<td>284</td>
<td>141</td>
<td>99</td>
<td>70</td>
<td>60</td>
<td>47</td>
<td>48.4</td>
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<td>Cash P/E</td>
<td>246</td>
<td>127</td>
<td>90</td>
<td>64</td>
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<tr>
<td>P/BV</td>
<td>74</td>
<td>51</td>
<td>40</td>
<td>26</td>
<td>18</td>
<td>14</td>
<td>11</td>
<td>9</td>
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<tr>
<td>EV/Sales</td>
<td>57</td>
<td>35</td>
<td>33</td>
<td>27</td>
<td>20</td>
<td>15</td>
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<tr>
<td>EV/EBITDA</td>
<td>189</td>
<td>101</td>
<td>74</td>
<td>53</td>
<td>46</td>
<td>34</td>
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<td>29</td>
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<tr>
<td>Dividend Yield (%)</td>
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<td>0.1</td>
<td>0.1</td>
<td>0.0</td>
<td>0.3</td>
<td>0.4</td>
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<td>FCF per share</td>
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<td>4</td>
<td>10</td>
<td>10</td>
<td>-1</td>
<td>10</td>
<td>12</td>
<td>14</td>
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<td><strong>Return Ratios (%)</strong></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>RoE</td>
<td>29</td>
<td>42</td>
<td>45</td>
<td>45</td>
<td>35</td>
<td>33</td>
<td>25</td>
<td>24</td>
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<tr>
<td>RoCE</td>
<td>28</td>
<td>40</td>
<td>43</td>
<td>43</td>
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<tr>
<td>RoIC</td>
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<td>77</td>
<td>56</td>
<td>48</td>
<td>38</td>
<td>40</td>
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<tr>
<td><strong>Working Capital Ratios</strong></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Fixed Asset Turnover (x)</td>
<td>2.7</td>
<td>3.4</td>
<td>2.9</td>
<td>2.9</td>
<td>2.8</td>
<td>2.5</td>
<td>1.9</td>
<td>2.0</td>
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<tr>
<td>Asset Turnover (x)</td>
<td>1.2</td>
<td>1.4</td>
<td>1.2</td>
<td>0.9</td>
<td>0.9</td>
<td>0.9</td>
<td>0.7</td>
<td>0.7</td>
</tr>
<tr>
<td>Inventory (Days)</td>
<td>44</td>
<td>34</td>
<td>30</td>
<td>38</td>
<td>47</td>
<td>42</td>
<td>42</td>
<td>42</td>
</tr>
<tr>
<td>Debtor (Days)</td>
<td>60</td>
<td>55</td>
<td>61</td>
<td>53</td>
<td>82</td>
<td>57</td>
<td>57</td>
<td>57</td>
</tr>
<tr>
<td>Creditor (Days)</td>
<td>40</td>
<td>21</td>
<td>31</td>
<td>43</td>
<td>54</td>
<td>31</td>
<td>31</td>
<td>31</td>
</tr>
<tr>
<td><strong>Leverage Ratio (x)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>Current Ratio</td>
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<td>1.8</td>
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<td>2.7</td>
<td>3.3</td>
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<td>Net Debt/Equity</td>
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<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>-0.1</td>
<td>0.0</td>
<td>-0.1</td>
<td>-0.1</td>
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### Consolidated - Cash Flow Statement (INR m)

<table>
<thead>
<tr>
<th>Y/E March</th>
<th>FY18</th>
<th>FY19</th>
<th>FY20</th>
<th>FY21</th>
<th>FY22</th>
<th>FY23</th>
<th>FY24E</th>
<th>FY25E</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>OP/(Loss) before Tax</strong></td>
<td>699</td>
<td>1,365</td>
<td>1,823</td>
<td>2,673</td>
<td>3,048</td>
<td>3,956</td>
<td>3,810</td>
<td>4,472</td>
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<td>Depreciation</td>
<td>76</td>
<td>110</td>
<td>137</td>
<td>172</td>
<td>249</td>
<td>361</td>
<td>456</td>
<td>494</td>
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<td>Interest Expenses</td>
<td>1</td>
<td>0</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Others</td>
<td>-18</td>
<td>-65</td>
<td>-67</td>
<td>-109</td>
<td>-126</td>
<td>-153</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Direct Taxes Paid</td>
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<td>-355</td>
<td>-424</td>
<td>-659</td>
<td>-691</td>
<td>-945</td>
<td>-959</td>
<td>-1,126</td>
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<tr>
<td>(Inc)/Dec in WC</td>
<td>-89</td>
<td>-208</td>
<td>131</td>
<td>-149</td>
<td>-1,209</td>
<td>-428</td>
<td>-15</td>
<td>-373</td>
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<tr>
<td><strong>CF from Operations</strong></td>
<td>449</td>
<td>848</td>
<td>1,601</td>
<td>1,928</td>
<td>1,273</td>
<td>2,793</td>
<td>3,295</td>
<td>3,470</td>
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<tr>
<td>(Inc)/Dec in FA</td>
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<td>-388</td>
<td>-503</td>
<td>-840</td>
<td>-1,396</td>
<td>-1,727</td>
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<tr>
<td><strong>Free Cash Flow</strong></td>
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<td>460</td>
<td>1,098</td>
<td>1,088</td>
<td>-123</td>
<td>1,067</td>
<td>1,295</td>
<td>1,470</td>
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<td>Change in Investments</td>
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<td>-576</td>
<td>-563</td>
<td>-1,078</td>
<td>532</td>
<td>-1,410</td>
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<td>Others</td>
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<td>3</td>
<td>51</td>
<td>78</td>
<td>439</td>
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<td><strong>CF from Investments</strong></td>
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<td>-950</td>
<td>-1,063</td>
<td>-1,867</td>
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<td>-2,698</td>
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<td>0</td>
<td>9</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>Inc/(Dec) in Debt</td>
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<td>1</td>
<td>-24</td>
<td>0</td>
<td>0</td>
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<td>0</td>
</tr>
<tr>
<td>Interest Paid</td>
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<td>0</td>
<td>1</td>
<td>-1</td>
<td>1</td>
<td>-1</td>
<td>1</td>
<td>-3</td>
</tr>
<tr>
<td>Dividend Paid</td>
<td>-51</td>
<td>-128</td>
<td>-153</td>
<td>-33</td>
<td>0</td>
<td>-558</td>
<td>-513</td>
<td>-602</td>
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<td>Others</td>
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<td>10</td>
<td>386</td>
<td>-1</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td><strong>CF from Fin. Activity</strong></td>
<td>-44</td>
<td>-98</td>
<td>-540</td>
<td>-59</td>
<td>-1</td>
<td>-550</td>
<td>-516</td>
<td>-605</td>
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<tr>
<td>Inc/Dec of Cash</td>
<td>230</td>
<td>-200</td>
<td>-3</td>
<td>1</td>
<td>486</td>
<td>-454</td>
<td>779</td>
<td>865</td>
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<tr>
<td>Opening Balance</td>
<td>65</td>
<td>295</td>
<td>95</td>
<td>92</td>
<td>93</td>
<td>579</td>
<td>125</td>
<td>904</td>
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<tr>
<td>Closing Balance</td>
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<td>95</td>
<td>92</td>
<td>93</td>
<td>579</td>
<td>125</td>
<td>903</td>
<td>1,769</td>
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</tbody>
</table>

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**Explanation of Investment Rating**

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<tr>
<th>Investment Rating</th>
<th>Expected return (over 12-month)</th>
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<tbody>
<tr>
<td>BUY</td>
<td>&gt;=15%</td>
</tr>
<tr>
<td>SELL</td>
<td>&lt; -10%</td>
</tr>
<tr>
<td>NEUTRAL</td>
<td>-10% to 15%</td>
</tr>
<tr>
<td>UNDER REVIEW</td>
<td>Rating may undergo a change</td>
</tr>
<tr>
<td>NOT RATED</td>
<td>We have forward looking estimates for the stock but we refrain from assigning recommendation</td>
</tr>
</tbody>
</table>

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Registered Office Address: Motilal Oswal Tower, Rahimullah Sayari Road, Opposite Parel ST Depot, Prabhadevi, Mumbai-400 025, Tel No: 022 - 71934200 / 71934263; www.motilaloswal.com.

Correspondence Address: Palm Spring Centre, 2nd Floor, Palm Court Complex, New Link Road, Malad (West), Mumbai- 400 064, Tel No: 022 71851000. Details of Compliance Officer: Neeraj Agarwal, Email Id: na@motilaloswal.com, Contact No. 022-40548085.

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<thead>
<tr>
<th>Contact Person</th>
<th>Contact No.</th>
<th>Email ID</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ms. Hemangi Date</td>
<td>022-40548000 / 022 67490600</td>
<td><a href="mailto:query@motilaloswal.com">query@motilaloswal.com</a></td>
</tr>
<tr>
<td>Ms. Kumud Upadhyay</td>
<td>022-40548082</td>
<td><a href="mailto:servicehead@motilaloswal.com">servicehead@motilaloswal.com</a></td>
</tr>
<tr>
<td>Mr. Ajay Menon</td>
<td>022-40548083</td>
<td><a href="mailto:jmn@motilaloswal.com">jmn@motilaloswal.com</a></td>
</tr>
</tbody>
</table>

Registration details of group entities: Motilal Oswal Financial Services Ltd. (MOFSL) INZ200158538 (BSE: NSE:MCMXNOCSL), CDSL and NSDL IN-DR-16-2015, Research Analyst: ARN: INH000000412. AMFI ARN: 146822. RDA Corporate Agent – CA0579. Motilal Oswal Financial Services Ltd. is a distributor of Mutual Funds, PMS, Fixed Deposit, Insurance, Bond, NCDs and IPO products. Customer having any query/feedback/clarification may write to query@motilaloswal.com. In case of grievances for any of the services rendered by Motilal Oswal Financial Services Limited (MOFSL) write to grievances@motilaloswal.com, for DP to dp@grievances@motilaloswal.com.