

India
HOLD (Initiating coverage)

Consensus ratings*:	Buy 9 Hold 2 Sell 0
Current price:	Rs2,470
Target price:	Rs2,519
Previous target:	NA
Up/downside:	2.0%
EIP Research / Consensus:	-20.0%
Reuters:	
Bloomberg:	GALSURF IN
Market cap:	US\$1,071m Rs87,575m
Average daily turnover:	US\$0.7m Rs61.0m
Current shares o/s:	35.5m
Free float:	29.1%

*Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	2.6	5.2	(13.9)
Relative (%)	0.5	4.5	(22.6)

Major shareholders	% held
Promoter & Promoter Group	70.9
FII	2.9
DII	12.7

Analyst(s)

Satish KUMAR

 T (91) 22 4161 1562
 E satish.kumar@incredcapital.com

Vipraw SRIVASTAVA

 T (91) 22 4161 1500
 E vipraw.srivastava@incredcapital.com

Abbas PUNJANI

 T (91) 22 4161 1598
 E abbas.punjani@incredcapital.com

Galaxy Surfactants Ltd

A commodity business with fair valuation

- As supply chain problems and the power crisis ease in Europe, extraordinary gross profit (GP) will normalize, leading to a PAT CAGR of -3.2% over FY23F-26F. RoE, in our view, will decline to 12.9% in FY26F from 22.5% in FY23F.
- A slew of macro factors, including volatile market situation in the AMET region, decrease in consumption in the US and the UK coupled with the current rate hike cycle act as headwinds, although the company's fundamentals are sound.
- We value the stock at 25.9x FY25F EPS, equal to the long-term mean. We initiate coverage on it with a HOLD rating and a target price of Rs2,519. Please note that our EPS estimates do not include the benefits like export incentives in Egypt announced during 3QFY23 results, which inflate the EPS currently.

The AMET conundrum and collapsing spreads in major molecules

A significant chunk of Galaxy Surfactants or GSL's revenue comes from the AMET region (Africa, Middle East and Turkiye), which is close to 33%. GSL has a manufacturing plant in Egypt where it mainly produces performance surfactants and exports to neighbouring countries. This region is facing strong headwinds particularly due to the prevailing macroeconomic scenario, such as depreciation of Egyptian pound and rampant inflation. This, coupled with supply chain problems like declining manufacturing PMI in Egypt, will severely hamper GSL's growth prospects, in our view. Moreover, sodium lauryl sulfate and lauryl alcohol ethoxylate, two molecules which contribute close to 50% of GSL's revenue, have been witnessing declining spreads over their raw materials. These spreads touched an all-time high in the previous few quarters due to supply chain problems and rising fuel costs. As the supply chain stabilizes and Germany's energy problem is resolved (by buying more LNG, see our [Report 1](#) and [Report 2](#)), coupled with its main competitor BASF returning to full production, the spreads will reduce, thereby hurting the topline of GSL.

Monopoly status in domestic home and personal care category

GSL is one of the few players who focus solely on the home and personal care or the HPC category. It has more than 60% market share in the domestic category. GSL also caters to the AMET region and rest of the world (RoW) including the US & the UK. GSL makes two types of surfactants: performance (60% contribution to revenue and are low margin, high volume, mainly sold in India and AMET region) and specialty (40% revenue contribution and high margin, low volume, mainly sold in Europe & RoW).

We value GSL at 25.9x FY25F EPS; initiate coverage with HOLD rating

GSL's EPS growth rate for the next two years is low, in our view, at a -3.2% CAGR (FY23F-26F). Also, we believe the company's RoE will decline from 22.5% in FY23F to 12.9% in FY25F. Due to falling EPS growth and a declining returns ratio, we have valued GSL at 25.9x FY25F EPS, equal to the long-term mean. We have assigned a HOLD rating to the stock with a target price of Rs2,519. Downside risks: More volatility in AMET market conditions, as S&P downgraded Egypt's economy outlook to negative from stable. Upside risk: Any rise in consumption in the US where GSL sells high-margin specialty surfactants.

Financial Summary

	Mar-22A	Mar-23F	Mar-24F	Mar-25F	Mar-26F
Revenue (Rsm)	36,857	45,279	43,323	45,272	47,536
Operating EBITDA (Rsm)	4,007	5,692	4,856	5,172	5,570
Net Profit (Rsm)	2,628	3,988	3,109	3,319	3,612
Core EPS (Rs)	74.1	112.5	87.7	93.6	101.9
Core EPS Growth	(13.0%)	51.8%	(22.0%)	6.7%	8.8%
FD Core P/E (x)	33.33	21.96	28.17	26.39	24.25
DPS (Rs)	10.8	4.9	3.6	8.4	26.5
Dividend Yield	0.44%	0.20%	0.14%	0.34%	1.07%
EV/EBITDA (x)	22.59	15.40	17.70	16.29	14.63
P/FCFE (x)	(299.01)	29.59	43.11	39.16	24.33
Net Gearing	18.7%	0.4%	(7.1%)	(12.7%)	(20.6%)
P/BV (x)	5.56	4.44	3.84	3.35	2.95
ROE	18.3%	22.5%	14.6%	13.6%	12.9%

% Change In Core EPS Estimates

InCred Research/Consensus EPS (x)

SOURCE: INCRED RESEARCH, COMPANY REPORTS

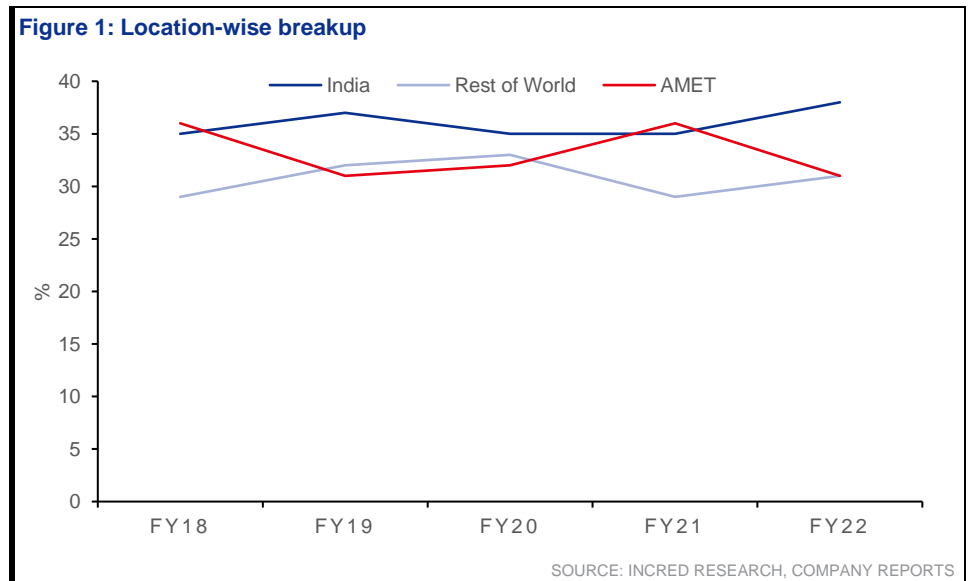
Growth headwinds on the cards

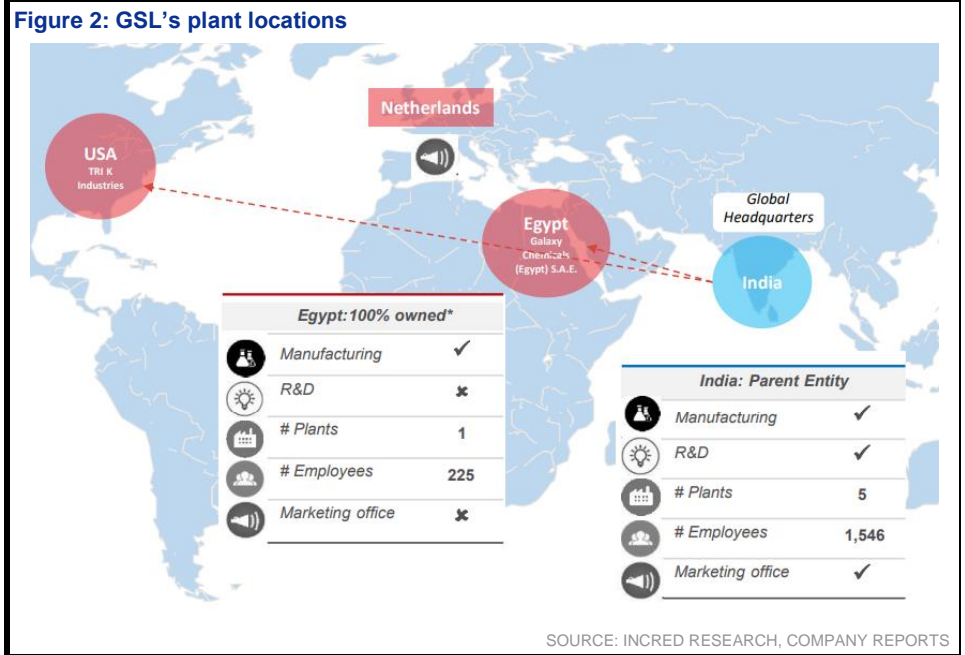
Galaxy Surfactants (GSL) mainly deals in performance (high volume and low margin) and specialty (low volume and high margin) surfactants, wherein performance comprises close to 60% of volume and the remaining is specialty. GSL's business caters to three geographies, mainly India (performance surfactants dominated, close to 85%), AMET (performance surfactants dominated) and RoW (covers the US & the UK and caters to specialty). Each of these geographies contribute roughly one-third to its total volume. Major headwinds lie in the AMET region, which has been facing a volatile market scenario due to geopolitical problems. Depreciation in Egyptian Pound and rising rate hikes by Egypt's central bank has been hurting consumer sentiment, leading to volume decline in previous quarters. The specialty segment has also been hit, as the main specialty markets i.e. the US and the UK, are facing recessionary fears, hurting the spending power of end-consumers.

Business analysis

An export-oriented business ►

Galaxy Surfactants is mainly an export-oriented business as the international business constitutes almost 66% of its portfolio - one more reason why macroeconomic factors are so important for this company. As far as its India business is concerned, here too the ratio is 50:50, i.e., it exports half of what it makes in the country.

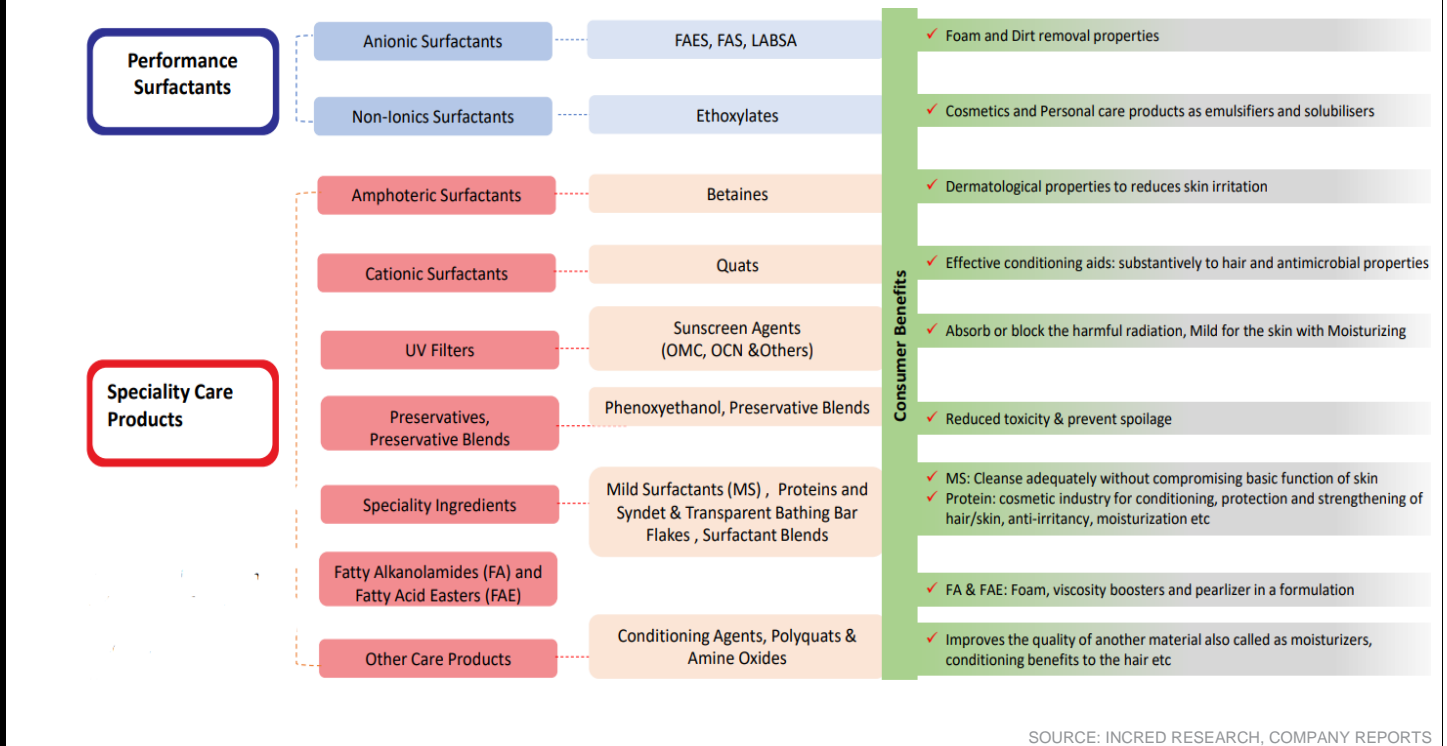




An established global supplier to major FMCG brands ►

Galaxy Surfactants or GSL is a supplier to all the major fast moving consumer goods or FMCG brands in India and abroad. Surfactants are surface-active agents. In other words, these are molecules that are used to help reduce tension of water on a given surface and help it spread more evenly. Adding surfactants to cleansing products helps the solution to spread more evenly and covers more of the surface being cleaned. Surfactants find application in almost every industry, ranging from household cleansing, industrial cleansing and personal care products. While GSL commenced operations as a local supplier to FMCG companies in India, it has diversified its operations to supply to Asia Pacific, AMET and Europe. Its clients include Cavin-Kare, Colgate-Palmolive, Dabur India, Henkel, Himalaya, L'Oréal and so on. In terms of volume, surfactants stand at 16.35mt (in 2015), which will increase to 22.97mt (2024F).

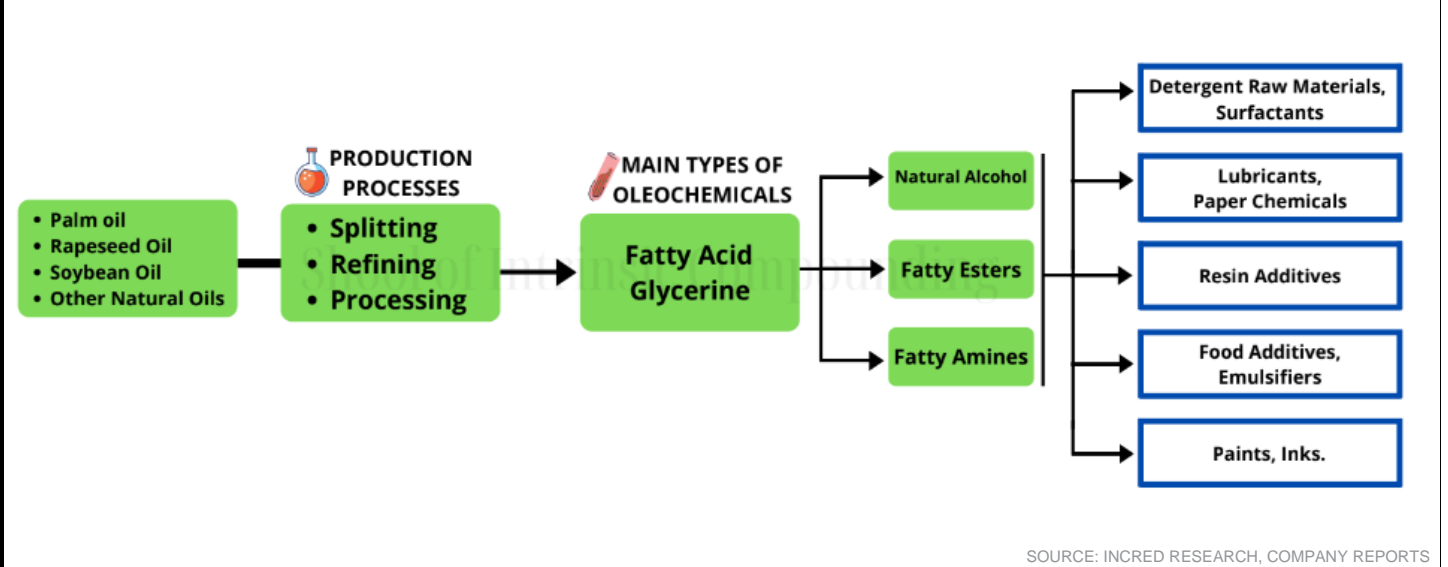
Figure 3: Portfolio of Galaxy Surfactants



Shift from petrochemicals to oleochemicals➤

If we go back to the 1970s, surfactants' primary feedstock was petrochemicals. Petrochemicals are those chemicals which are formed as a by-product during the refining of crude oil. But as the world becomes more conscious about climate change, there have been increasing regulations with respect to petrochemicals. And as these regulations come to the fore, there has been a value migration from petrochemicals to oleochemicals. Oleochemicals are chemical compounds derived from natural fats and oils that can be used as raw materials. In the case of GSL, nearly 50-60% of surfactants are made from oleochemicals. The company's primary raw material is lauryl alcohol, which is a derivative of palm kernel oil (please keep in mind that palm oil is different from palm kernel oil, and most of Indonesia's export regulations relate to palm oil and not palm kernel oil). Lauryl alcohol is important because it is highly volatile and hence, up and down movements in its prices can exert pressure on GSL's margins. In that case, the risk management framework of the company becomes very important and GSL has excelled in the same. In situations of extreme price volatility, GSL manages it by striking short-term deals with its clients, which allows the company to effectively pass on the hike and as clients in this sector are sticky, it makes the task easier.

Figure 4: Standard oleochemicals production process and their primary applications



India remains one of the main markets of GSL where usage of surfactants is in line with the global pattern ➤

Figure 5: Surfactants application industry globally

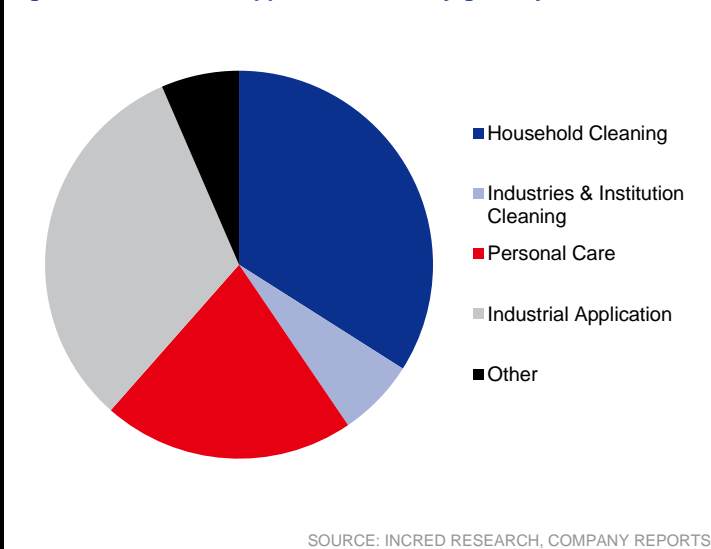
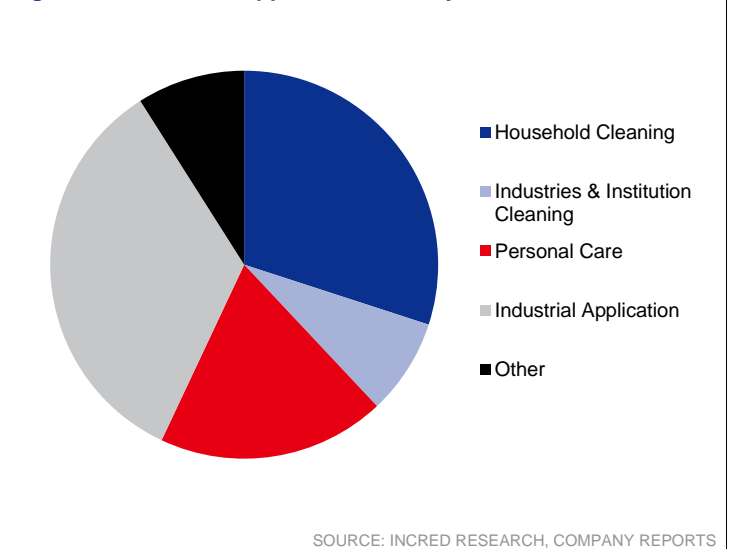


Figure 6: Surfactants application industry in India

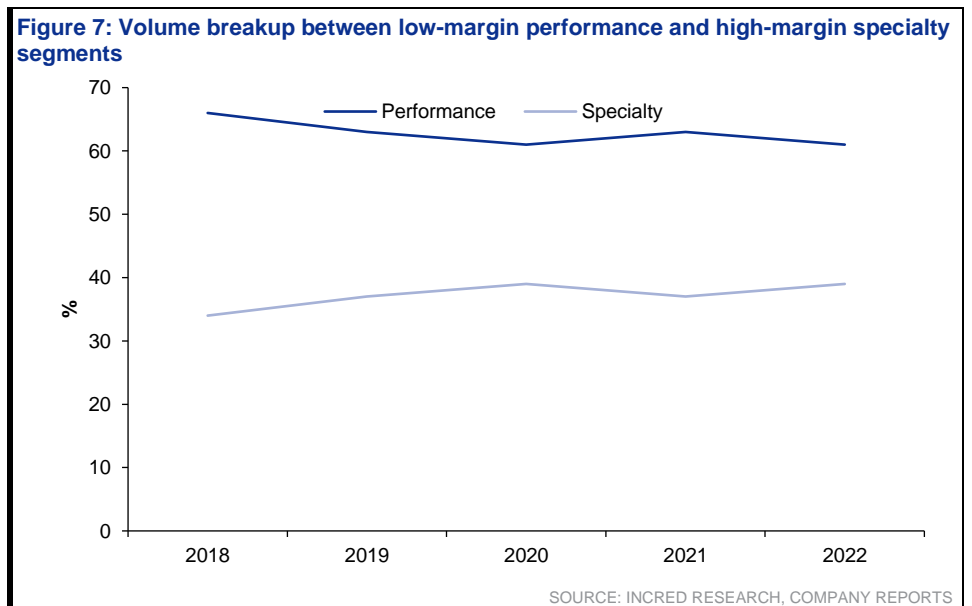


Cracked the process chemistry for phenoxyethanol >

Phenoxyethanol is a common preservative used in various industries, including personal care, pharma and food processing. It is used to prevent the growth of bacteria and other microorganisms in these products. Phenoxyethanols were introduced in the industry primarily to replace parabens. Parabens are synthetic chemicals which are used in beauty products for giving them a longer shelf life. They are similar in properties to phenoxyethanols in the sense that they also prevent the growth of fungi and other microorganisms. However, parabens are harmful as they have been linked to lower testosterone levels, breast cancer and ecological harm. Hence, GSL introduced paraben-free products, and achieved a sales growth of Rs2.5bn from Rs100m in its preservatives-free portfolio. As far as the size of the industry is concerned, the global market for preservatives was valued at US\$2.4bn in 2020 and is projected to reach US\$3.2bn by 2025F, growing at a CAGR of 5.5% during the forecast period. Galaxy Surfactants is the market leader in phenoxyethanol, and in fact the company has acquired process chemistry expertise in this chemical as it can manufacture phenoxyethanol according to different grades required by the market with minimum impurities. However, one should keep in mind that phenoxyethanol could have potential toxic effects if used in a concentration of more than 1%. Various scientific experiments conducted in the US and Europe have led to the conclusion that the use of phenoxyethanol in concentrations greater than 1% can lead to rashes and other skin-related infections. In fact, applying layers of cosmetics one over another can potentially be dangerous too as it can lead to a concentration greater than 1% in certain localized areas on the skin. It should also be noted that the demand for organic and natural preservatives is growing over synthetic preservatives like phenoxyethanol, but it remains in use currently due to effectiveness and affordability.

The specialty chemical part of the business is increasing over time >

As can be seen in the chart above, volumes in performance and specialty segments have remained constant in the past few years. This is expected to continue for the next five-to-six years as domestic and AMET markets have still not attained that level of premiumization to go for pricey specialty products.



Volatile raw material prices >

The primary raw materials for GSL include lauryl alcohol (used in performance surfactants), ethylene oxide (used in the manufacture of phenoxyethanol) and LABSA (linear alkyl benzene sulphonic acid used in the manufacture of

performance surfactants in Egypt). LABSA is a petroleum-based surfactant, and its prices move in tandem with crude oil.

Figure 8: Raw material breakup for Galaxy Surfactants

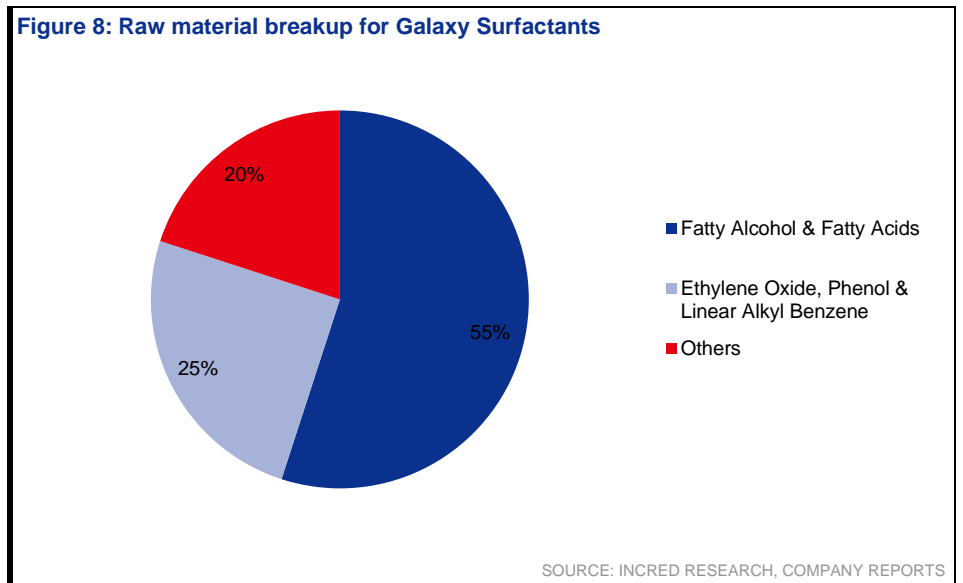


Figure 9: Lauryl alcohol price trend (in Rs/kg)

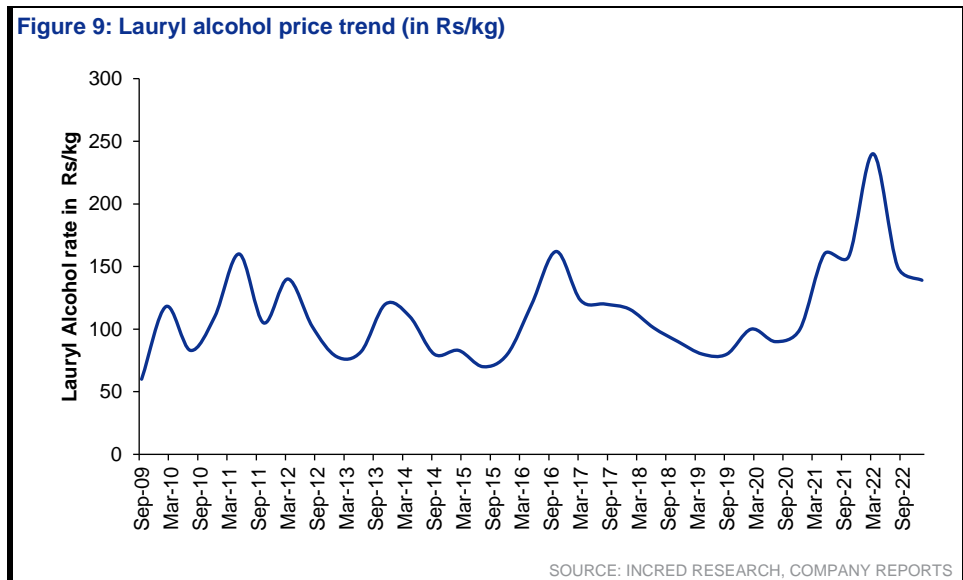


Figure 10: Linear alkyl benzene price trend (in Rs/kg)

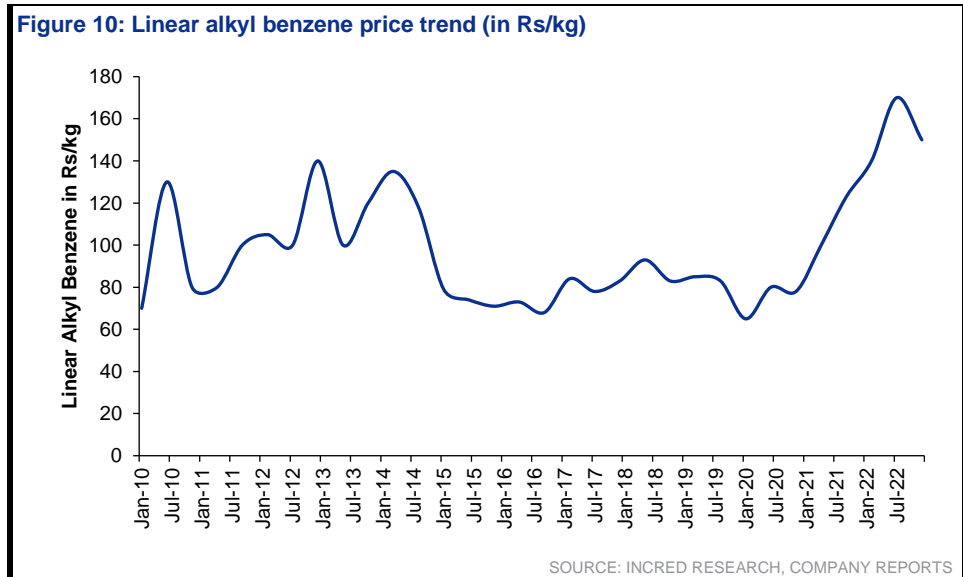
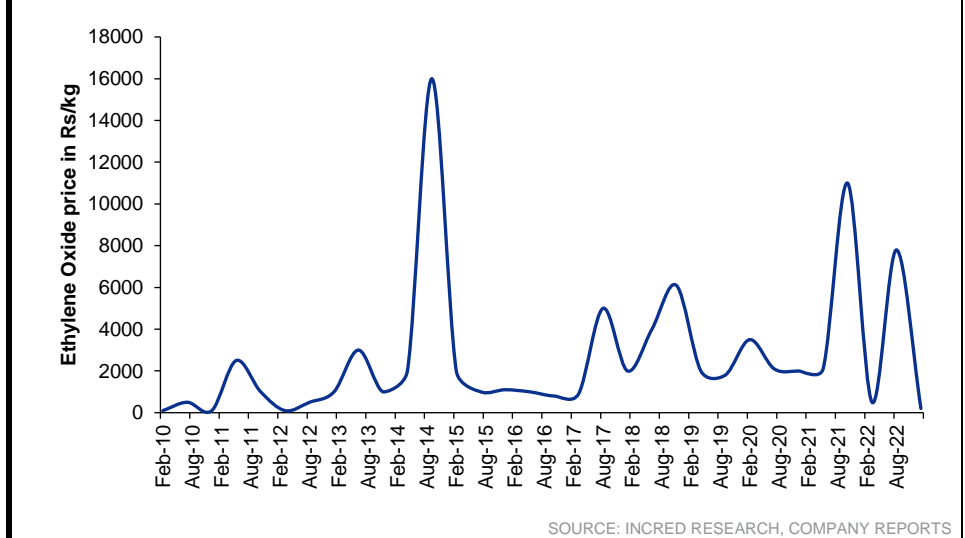
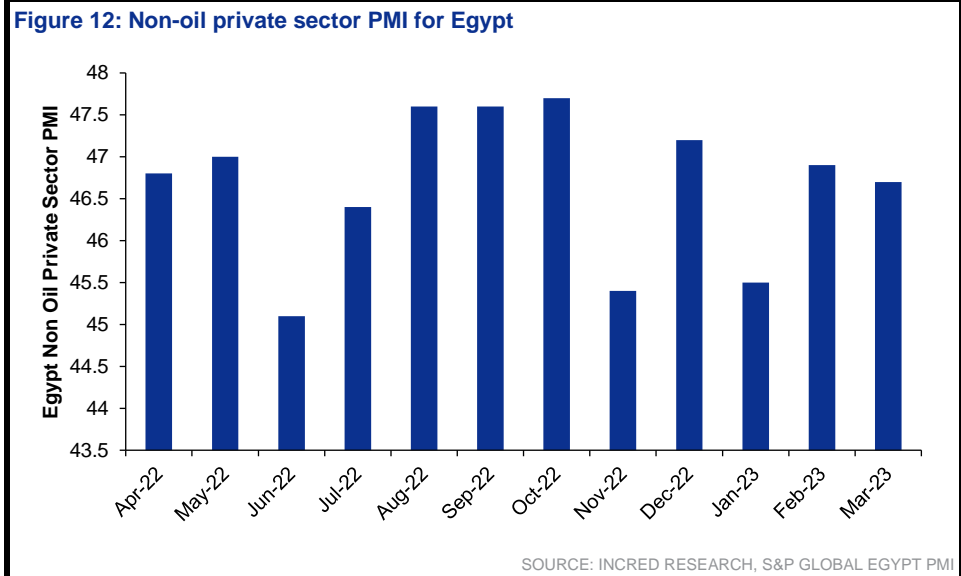


Figure 11: Ethylene oxide price trend (in Rs/kg)

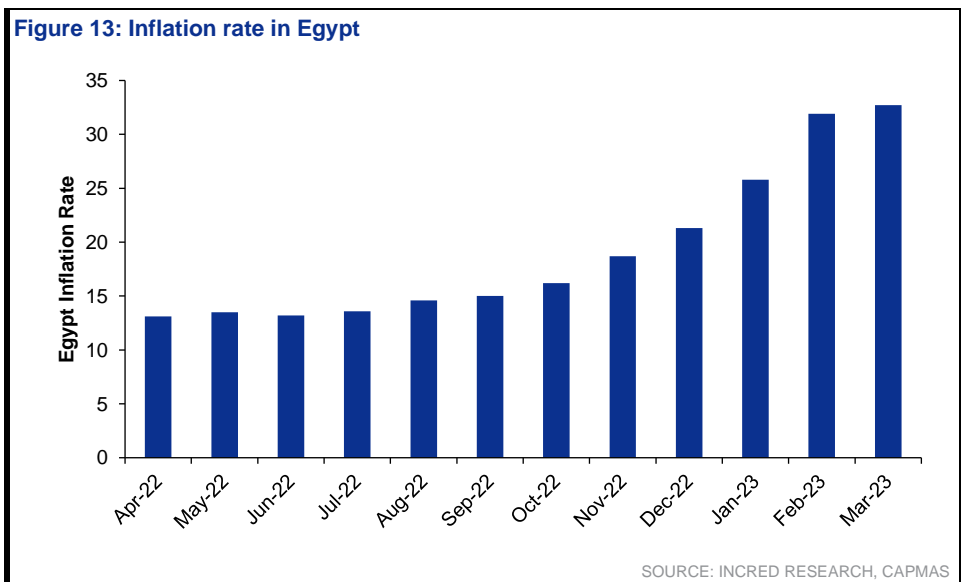
As can be seen from the charts above, raw material prices for GSL are quite volatile, particularly lauryl alcohol and linear alkyl benzene or LAB. LAB is mainly used in its Egyptian plant for manufacturing performance surfactants and presents a significant supply side challenge as demand in the AMET region is quite volatile and hence, it's a major challenge for GSL to pass on the increased raw material prices to its clients. As a result, the volume from the AMET region is quite volatile because the challenges involved are unique from the supply side as well as the demand side. In India, lauryl alcohol is a major ingredient for producing performance surfactants. Lauryl alcohol is an oleochemical sourced from a palm kernel derivative, mostly from southeast Asia. As the performance surfactant market is a commodity market involving intense competition, these fluctuations in raw materials prices erode margins, which is reflected in our valuation of GSL.

The AMET conundrum

A significant chunk of GSL's revenue comes from the AMET region (Africa, Middle East and Turkiye). The company has a manufacturing plant in Egypt where it mainly produces performance surfactants and exports to neighbouring countries. Please note that as far as the performance surfactants are concerned, they can only be transported to nearby regions because they are bulky and hence, the rationale behind setting up the plant in Egypt. On the other hand, specialty surfactants can be exported to faraway countries. As GSL's entire base of operations is in Egypt, a major portion of its strategy depends on what is happening in the Egyptian market. In FY19, when the Egyptian market was in doldrums, the company ventured into other Africa and Middle East countries including Kenya, Lebanon, the UAE and Jordan. One important point of consideration for these regions is higher inflation, as was seen in the case of Türkiye (Türkiye contributes 9% -10% to overall revenue) and this leads to significant downtrading. Downtrading is a consumer behaviour where buyers switch from an expensive or a bigger product to either low-unit packs or lower-end brands. This can lead to a drop in volume for FMCG companies, who in this case are clients of GSL. But downtrading is not much of a problem for GSL in the Indian market, as GSL has a strong reach across T1, T2 and T3 clients. Here T1 refers to large MNCs, T2 refers to regional players and T3 refers to local players. However, this is not the case in Egypt where GSL mostly caters to T1 players and hence, changes in the market scenario leads to significant downtrading in favour of T3 players. This can be also seen in the quarterly results as AMET constantly shows volatility in volume. It is going to be further exacerbated with the Egyptian Pound constantly depreciating and inflation rising significantly. Recently, rating agency S&P also downgraded its outlook on the Egyptian economy from stable to negative, which can lead to further volume contraction in FY24F.



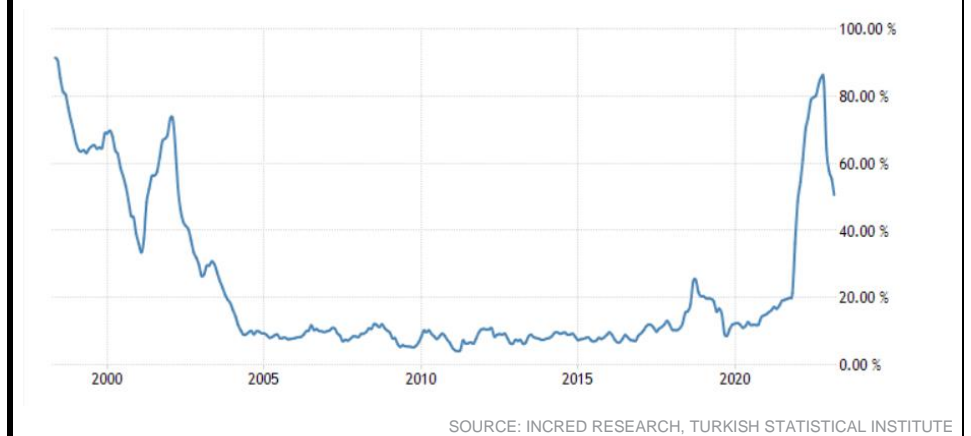
The S&P Global Egypt PMI decreased slightly in Mar 2023 from 46.9 to 46.7, extending the current trend of decline to more than two years. As severe inflationary pressure and a decline in customer demand negatively impacted the non-oil businesses, new orders fell further. At the same time, the output continued to decline, despite minor easing, and stood at the lowest level for five months, in part due to persistent access problems related to crucial inputs caused by import prohibition and currency limitations. As companies maintained their prices in an effort to increase demand, output charges decreased to a five-month low and were significantly weaker than overall input cost pressure. Finally, companies continued to show a little optimism, despite the prices moving to a three-month high, but the year-ahead activity was still among the weakest since records began in early 2012.



In Mar 2023, Egypt's annual urban inflation rate increased to 32.7% from 31.9% in the previous month, but it was still below market expectation of 33.6%. Inflation reached its highest level since Jul 2017 as a result of a round of currency devaluations that began in Mar 2022. Given the recent decline in the value of the currency and the increase in demand during the holy month of Ramadan, food and non-alcoholic beverage prices, which are by far the most important in the Consumer Price Index or CPI basket, experienced the greatest upward pressure (62.9 percent vs. 61.8% in Feb). Markets had anticipated that Egypt's annual core inflation rate, which excludes volatile commodities like food, would increase further to 42.25%, but instead it fell to 39.50% in Mar 2023 from a record 40.26% in Feb

2023. These levels of inflation are going to hurt consumer spending level, something which greatly affects GSL's business in Egypt.

Figure 14: Inflation data for Turkiye



There are signs of improvement in Turkiye, which contributes 9-10% to GSL's revenue. Inflation numbers are encouraging, although they are still at a multi-year high. PMI index for Turkiye also showed an improvement, which further indicated a rebuild in the coming quarters. After the devastating earthquake which struck Turkiye, the country is showing signs of growth, which could be a tailwind for GSL in FY24F, although not a major one.

Figure 15: Consumer Confidence Index or CCI in the UK; although there has been a slight increase, CCI is still at a multi-year low, and it should be noted that a number below 100 shows a pessimist stance

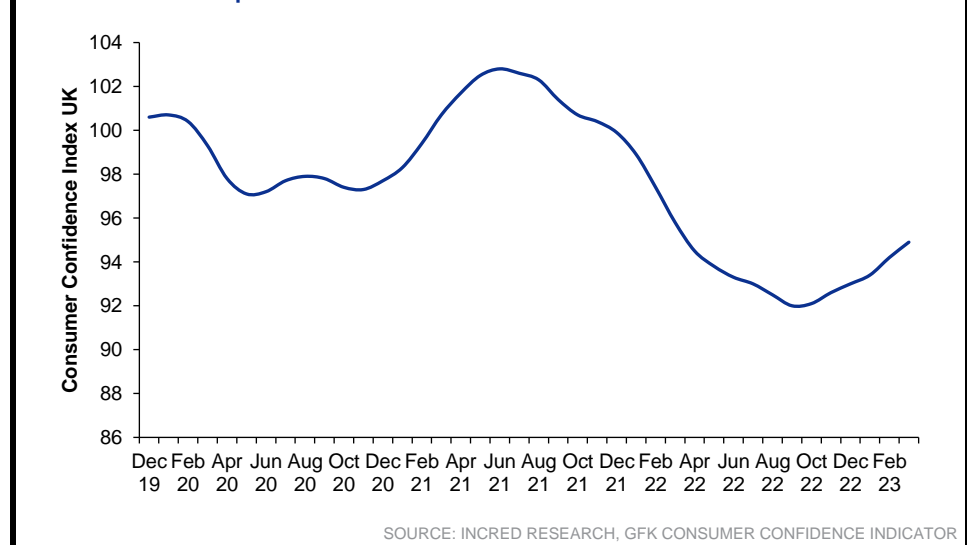
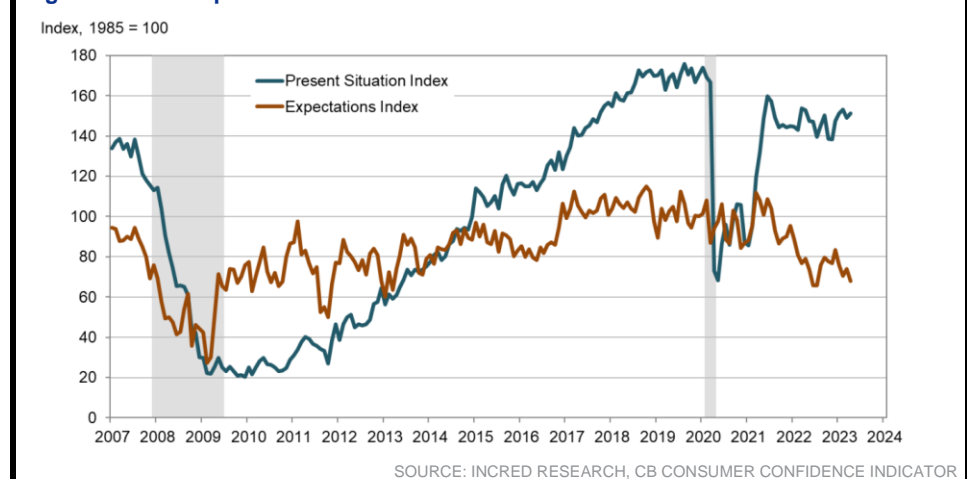


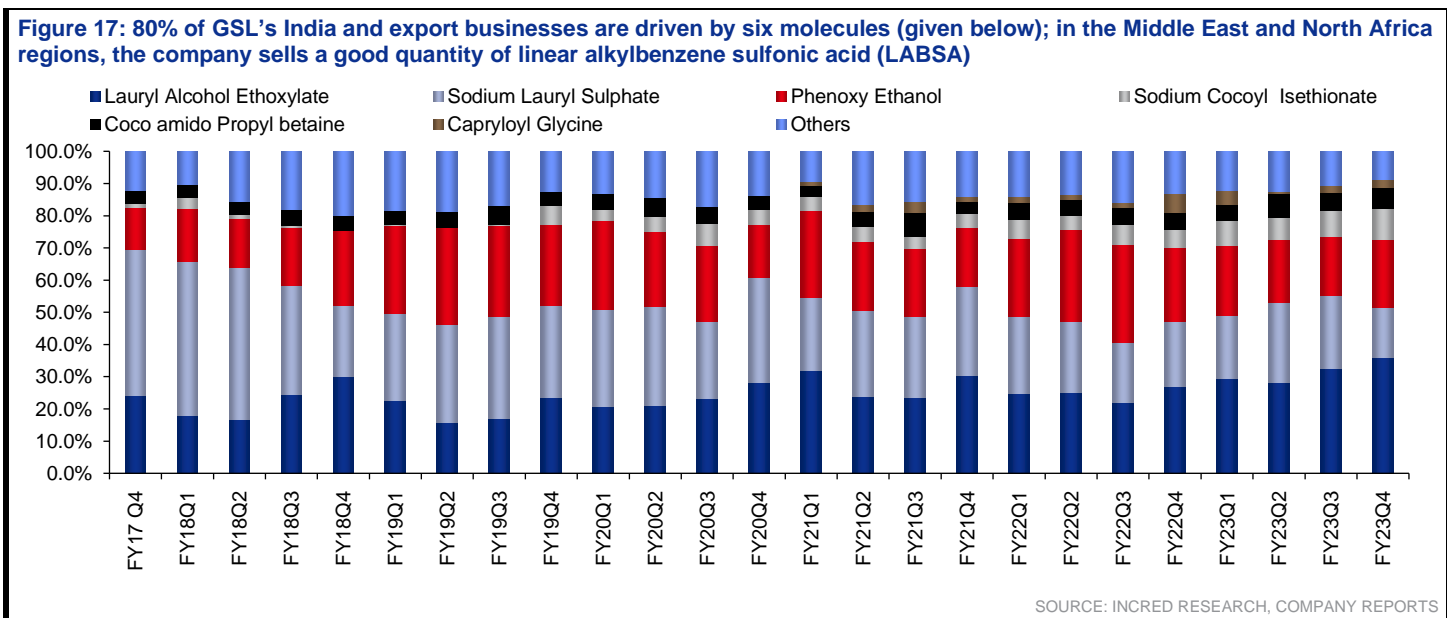
Figure 16: The Expectations Index for USA



As far as the USA is concerned, the Consumer Confidence Index consists of two parts, the Present Situation Index (40% weightage in Index) and Expectations Index (60% weightage in Index). The Present Situation Index explains the consumer’s perspective towards the current business scenario and the Expectations Index talks about the expected business scenario in the medium- to short-term. As can be seen from the chart above, the Expectations Index is at a multi-year low, and in fact it’s even lower than peak pandemic times and hence, this will affect GSL’s sales in the US and Americas. It must be noted that a number below 100 shows a pessimist stance.

GSL’s product portfolio comprises seven key molecules

While GSL manufactures multiple chemicals under various business heads, the key molecules which form more than 80% of its volume in India and the USA/ UK are 1) lauryl alcohol ethoxylate, 2) sodium lauryl sulphate, 3) phenoxy ethanol, 4) sodium cocoyl isethionate, 5) coco amido propyl betaine, and 6) capryloyl glycine. In the Middle East and North Africa regions, GSL sells a good quantity of linear alkylbenzene sulfonic acid (LABSA).



Usage of linear alkylbenzene sulfonic acid (LABSA) ➤

- LABSA is commonly used as a surfactant in the production of various detergents, such as laundry detergents, dishwashing detergents, and household cleaners. It is also used in the production of emulsifiers, wetting agents, and dispersants.
- LABSA is preferred over other surfactants due to its high solubility in water, strong cleaning power, and low cost. It is particularly effective in removing oil and grease stains from clothes and surfaces.
- In addition to its use in the detergent industry, LABSA is also used in the leather industry, agricultural industry, and in the production of various industrial cleaning products.

How LABSA is manufactured? ➤

Linear alkylbenzene sulfonic acid (LABSA) is typically manufactured through a process called sulfonation, which involves the reaction of linear alkylbenzene with sulfuric acid. Here are the basic steps involved in the manufacturing process:

- Preparation of linear alkylbenzene:** Linear alkylbenzene is prepared from kerosene or petroleum distillate and benzene using a catalyst such as aluminum chloride.
- Sulfonation:** The prepared linear alkylbenzene is mixed with concentrated sulfuric acid in a reactor vessel under controlled temperature and agitation. The

reaction takes place with the sulfuric acid attacking the alkyl side chain, resulting in the formation of sulfonic acid.

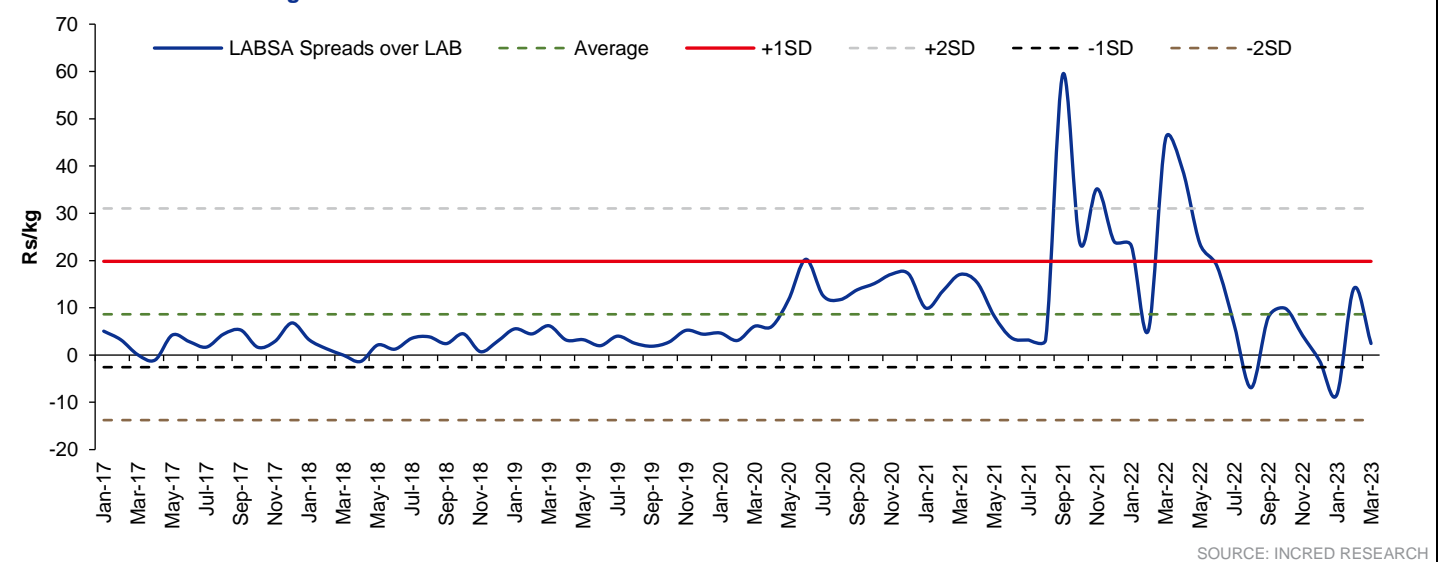
3. **Neutralization:** The sulfonic acid is then neutralized with an alkaline solution such as sodium hydroxide or ammonia to form LABSA. This step also helps to remove any unreacted sulfuric acid.
4. **Separation:** The LABSA solution is then separated from the reaction mixture using a centrifuge or filter.
5. **Drying:** The separated LABSA is then dried to remove any remaining moisture and to produce a powdered or liquid form suitable for use in various applications.

The quality of LABSA depends on the purity of the starting materials, the reaction conditions, and the effectiveness of the separation and drying steps.

Covid-related supply chain problems led to expansion of LABSA spreads but as they are easing, the spreads are falling ➤

We have analysed LABSA spreads over linear alkyl benzene and post supply chain shock easing, its spreads are collapsing.

Figure 18: LABSA spreads over LAB peaked in May 2022 and are falling since then; we expect gross spreads of LABSA over LAB to stabilize around Rs 9-10/kg



SOURCE: INCRED RESEARCH

Usage of lauryl alcohol ethoxylate ➤

Lauryl alcohol ethoxylate is a type of non-ionic surfactant that is widely used in various industries due to its excellent emulsifying, wetting, and dispersing properties. Here are some common uses of lauryl alcohol ethoxylate:

1. **Household and personal care products:** Lauryl alcohol ethoxylate is commonly used in the production of household and personal care products such as laundry detergents, shampoos, body washes, and liquid soaps. It helps to reduce the surface tension of the water, allowing for better cleaning and foaming properties.
2. **Agriculture:** Lauryl alcohol ethoxylate is used in the agriculture industry as a wetting agent, emulsifier, and dispersant for pesticides, herbicides, and fungicides. It helps to improve the absorption and efficacy of the chemicals, as well as the adhesion to the plant surfaces.
3. **Industrial applications:** Lauryl alcohol ethoxylate is used in various industrial applications such as in the production of coatings, paints, and inks. It helps to improve the spreading and wetting properties of these products.
4. **Oil and gas industry:** Lauryl alcohol ethoxylate is used as a surfactant in the oil and gas industry to increase the recovery of crude oil from reservoirs. It

helps to reduce the surface tension of the water and improve the displacement of the oil.

Lauryl alcohol ethoxylate manufacturing process ►

Lauryl alcohol ethoxylate is typically manufactured through a process called ethoxylation, which involves the reaction of lauryl alcohol with ethylene oxide. Here are the basic steps involved in the manufacturing process:

1. **Preparation of lauryl alcohol:** Lauryl alcohol is prepared by the catalytic hydrogenation of natural fatty acids or by the reaction of ethylene with an alcohol in the presence of a catalyst.
2. **Ethoxylation:** The prepared lauryl alcohol is then mixed with ethylene oxide in the presence of a catalyst and under controlled temperature and pressure conditions. The reaction between the lauryl alcohol and ethylene oxide results in the formation of lauryl alcohol ethoxylate.
3. **Neutralization:** The lauryl alcohol ethoxylate is then neutralized with an alkaline solution such as sodium hydroxide to remove any unreacted ethylene oxide and to adjust the pH of the final product.
4. **Purification:** The lauryl alcohol ethoxylate solution is then purified by removing any impurities using a series of filtration and distillation steps.
5. **Drying:** The purified lauryl alcohol ethoxylate is then dried to remove any remaining moisture and to produce a powdered or liquid form suitable for use in various applications.

Lauryl alcohol ethoxylate - key manufacturers ►

There are many manufacturers of lauryl alcohol ethoxylate worldwide, ranging from small regional producers to large multinational corporations. Here are some of the key manufacturers of lauryl alcohol ethoxylate:

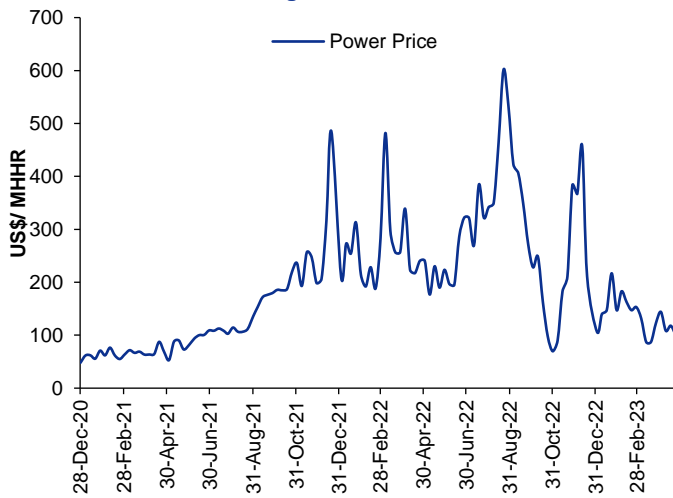
1. **BASF SE:** BASF is a German chemical company and one of the largest manufacturers of lauryl alcohol ethoxylate in the world. The company produces a wide range of lauryl alcohol ethoxylate products under the trade name Lutensol.
2. **Shell Chemicals:** It is a global chemical company that produces lauryl alcohol ethoxylate under the trade name Neodol. The company offers a variety of lauryl alcohol ethoxylate products with different degrees of ethoxylation and chain lengths.
3. **Dow Chemical Company:** It is an American multinational chemical company that produces lauryl alcohol ethoxylate under the trade name Tergitol. The company offers a range of lauryl alcohol ethoxylate products with different HLB (Hydrophilic-Lipophilic Balance) values and degrees of ethoxylation.
4. **Huntsman Corporation:** It is an American multinational chemical company that produces lauryl alcohol ethoxylate under the trade name Ethomeen. The company offers a range of lauryl alcohol ethoxylate products with different degrees of ethoxylation and chain lengths.
5. **Sasol:** It is a South African petrochemical company that produces lauryl alcohol ethoxylate under the trade name Alfol. The company offers a range of lauryl alcohol ethoxylate products with different degrees of ethoxylation and chain lengths.

European power crisis led to the decline in production, which led to the rise in spreads, but the same are falling now ►

The power consumption for producing 1t of lauryl alcohol ethoxylate can range from around 2,000 to 5,000kWh, depending on the specific process used. However, it is important to note that these figures are highly dependent on the specific conditions of the manufacturing process and may vary widely from one facility to another.

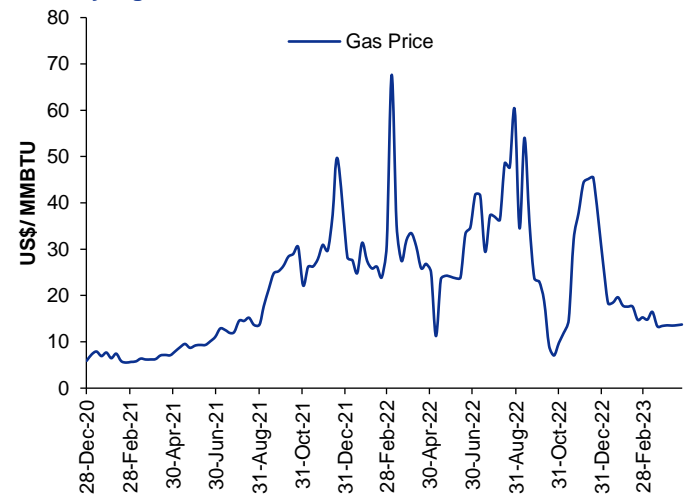
The rise in power prices in Europe led to the decline in production but as power prices stabilize, production will stage a comeback, which will lead to the decline in product spreads.

Figure 19: European power prices have declined but are still above the historical average...



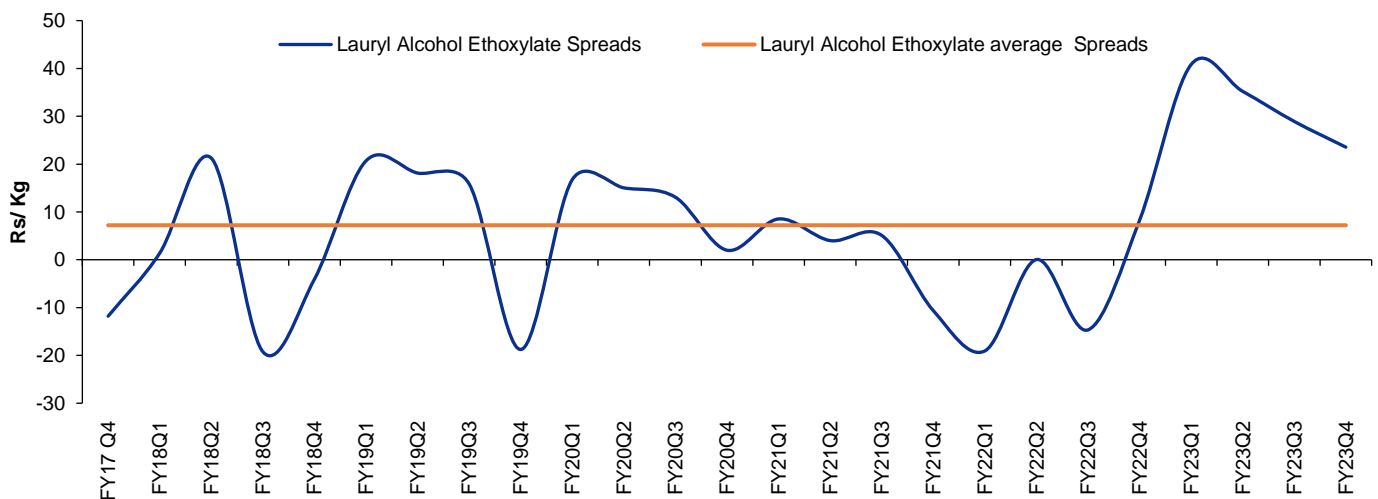
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 20: ...as even after the decline, European gas prices are still very high over the historical mean



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 21: As production ramps up post power crisis in Europe, lauryl alcohol ethoxylate spreads over raw material will fall



SOURCE: INCRED RESEARCH

Usage of sodium lauryl sulphate ➤

Sodium lauryl sulphate (SLS) is a common ingredient in many personal care and cleaning products due to its ability to create foam and its detergent properties. Here are some of its uses:

- 1. Personal care products:** SLS is widely used in personal care products such as shampoos, soaps, toothpaste, and body washes as a foaming agent and emulsifier. It helps to create a rich lather and suspends dirt and oil particles in water, making it easier to rinse them away.
- 2. Cleaning products:** SLS is also used in cleaning products such as dishwashing liquids, laundry detergents, and all-purpose cleaners as a surfactant to help remove dirt, grease, and stains.
- 3. Pharmaceuticals:** SLS is used in some pharmaceutical products as a solubilizer and emulsifier to help disperse active ingredients and improve their absorption.
- 4. Textile and leather industry:** SLS is used in textile and leather industries as a wetting agent, emulsifier and detergent.

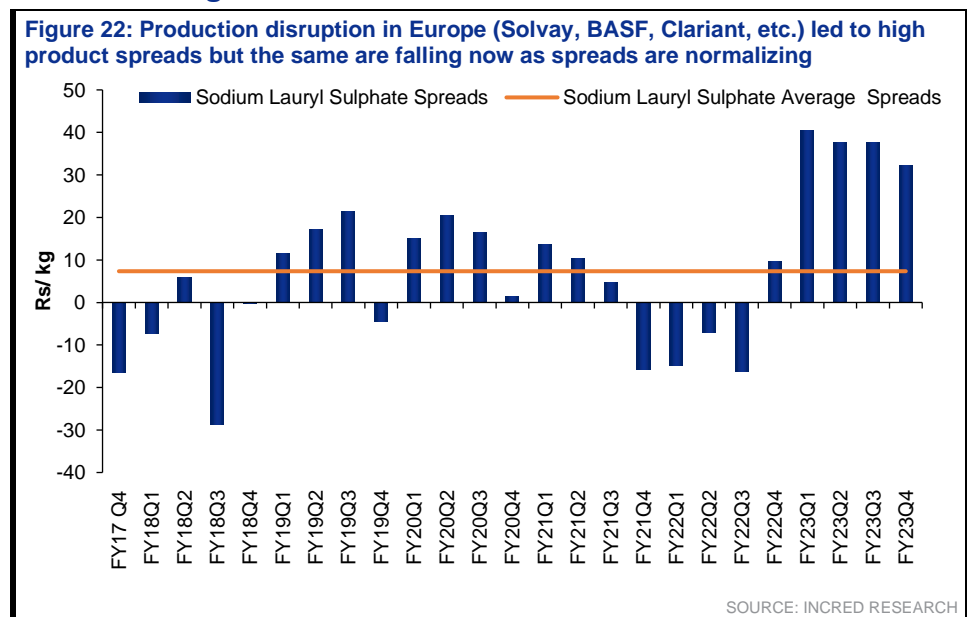
- Agriculture:** SLS is used in agriculture as a wetting agent and pesticide adjuvant.

Sodium lauryl sulphate manufacturers ▶

There are many manufacturers of sodium lauryl sulphate (SLS) around the world. Here are some of the major producers:

- BASF:** It is a global chemical company based in Germany that produces a wide range of chemicals and materials, including SLS. The company's SLS products are marketed under the brand name Lutensol.
- Stepan Company:** It is a US-based manufacturer of specialty chemicals, including SLS. The company offers a range of SLS products, including low-foaming and low-irritation varieties.
- Solvay:** It is a global chemical company based in Belgium that produces a wide range of chemicals and materials, including SLS. The company's SLS products are marketed under the brand name Rhodapex.
- Clariant:** It is a Swiss specialty chemical company that produces a variety of chemicals and materials, including SLS. The company's SLS products are marketed under the brand name Hostapur.
- Kao Corporation:** It is a Japanese chemical and consumer goods company that produces a range of personal care and cleaning products, including SLS. The company's SLS products are marketed under the brand name Surfactant.

Production disruption led to the rise in product spreads, which are correcting now ▶



Usage of phenoxyethanol ▶

Phenoxyethanol is a versatile chemical compound with a wide range of applications in various industries. Here are some common uses of phenoxyethanol:

- Preservative:** Phenoxyethanol is commonly used as a preservative in cosmetics, personal care products, and pharmaceuticals. It helps to inhibit the growth of bacteria, fungi, and other microorganisms in these products, extending their shelf life.
- Solvent:** Phenoxyethanol is a good solvent for many substances and is used in a variety of industrial applications such as inks, dyes, and resins.
- Fragrance ingredient:** Phenoxyethanol has a mild, floral scent that makes it a popular ingredient in fragrances and perfumes.
- Antiseptic:** Phenoxyethanol has antiseptic properties, and it is used in some topical antiseptic products and wound dressings.

5. Vaccine preservative: Phenoxyethanol is used as a preservative in some vaccines to prevent the growth of bacteria and fungi during storage.
6. Disinfectant: Phenoxyethanol is used as a disinfectant in some household and industrial cleaning products.
7. Coalescing agent: Phenoxyethanol is a coalescing agent used in the production of latex paints to help the paint form a uniform film.

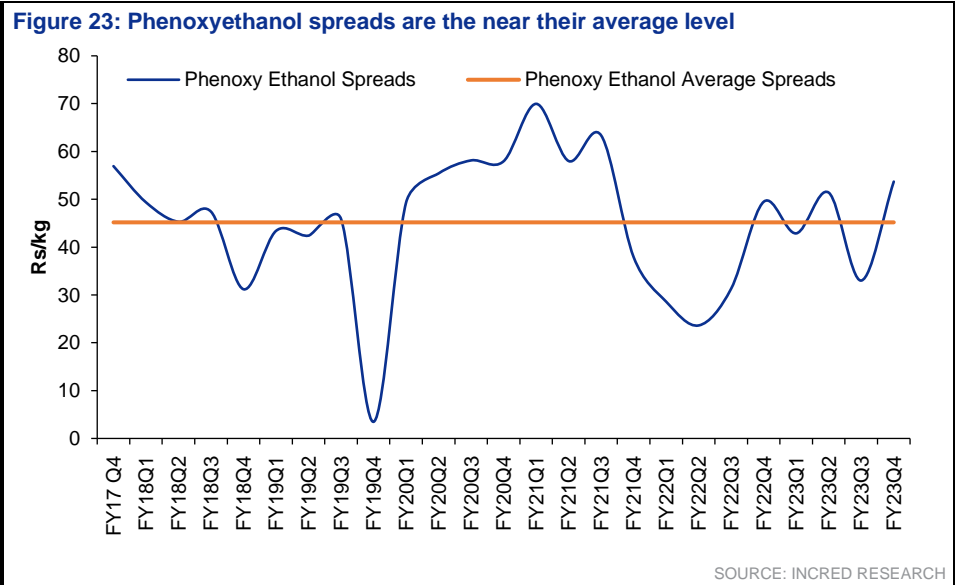
Phenoxyethanol manufacturers ►

Phenoxyethanol is produced by several manufacturers around the world. Here are some of the major manufacturers of phenoxyethanol:

1. BASF SE
2. The Dow Chemical Company
3. AkzoNobel
4. Symrise AG
5. Lonza Group
6. Clariant
7. Galaxy Surfactants

Phenoxyethanol spreads steady as power crisis in Europe did not result in a big disruption ►

Apart from BASF and Symrise AG, there are no big German companies who make phenoxyethanol. Switzerland didn't face a big crisis as such and hence, we didn't witness big volatility in phenoxyethanol spreads over its raw material.



Usage of sodium cocoyl isethionate ►

Sodium cocoyl isethionate (SCI) is a mild surfactant derived from coconut oil. It is commonly used in personal care and cosmetic products due to its gentle nature and excellent cleansing properties. Here are some of the most common uses of sodium cocoyl isethionate:

1. Cleansing agent: Sodium cocoyl isethionate is an effective cleansing agent that removes dirt, oil, and impurities from the skin and hair without causing irritation or dryness.
2. Foam booster: Sodium cocoyl isethionate is a foaming agent that helps to produce rich and stable lather in personal care and cosmetic products such as shampoos, shower gels, and facial cleansers.
3. Moisturizing agent: Sodium cocoyl isethionate has moisturizing properties that help to keep the skin and hair hydrated and soft.

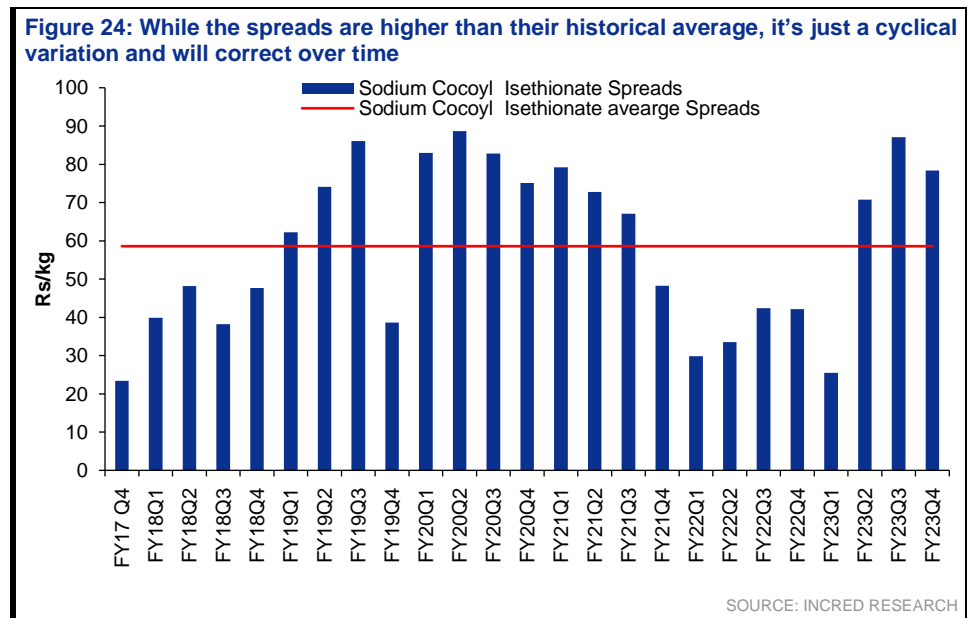
- Emulsifier: Sodium cocoyl isethionate is an effective emulsifier that helps to mix oil and water-based ingredients in cosmetic and personal care formulations.
- pH adjuster: Sodium cocoyl isethionate can be used as a pH adjuster in cosmetic and personal care products to maintain the desired pH level.
- Thickening agent: Sodium cocoyl isethionate can be used as a thickening agent in cosmetic and personal care products to increase their viscosity and improve their texture.

Sodium cocoyl isethionate manufacturers ➤

- Innospec Inc.: It is a global specialty chemicals company that produces a range of surfactants, including sodium cocoyl Isethionate.
- BASF SE
- Stepan Company: It is an US-based manufacturer of specialty chemicals and produces sodium cocoyl isethionate for use in personal care and cosmetic products.
- AkzoNobel
- Kao Corporation

Apart from general post Covid-19 pandemic supply chain disruption-driven rise in spreads, we don't see any any froth in product spreads ➤

While BASF would have been hurt because of the power crisis in Germany and a fall in production, other companies may not have taken a hit. Hence, the spreads have also not risen massively over their historical mean. As of now, they are slightly higher than their historical mean, which may correct as the global slowdown hits the industry.



Usage of cocoamidopropyl betaine ➤

Cocoamidopropyl betaine (CAPB) is a synthetic surfactant that is commonly used in personal care and cleaning products. It is derived from coconut oil and is valued for its ability to create a rich lather and effectively remove dirt and oil. Some common uses of cocoamidopropyl betaine include:

- Shampoos: CAPB is often used as a primary ingredient in shampoos because of its excellent foaming properties, mildness and ability to clean hair effectively.
- Body Washes: Similar to its use in shampoos, CAPB is used in body washes to create a rich lather and cleanse the skin.

3. Facial Cleansers: Cocoamidopropyl betaine is often used in facial cleansers due to its mildness and the ability to clean the skin without stripping away natural oils.
4. Hand Soaps: CAPB is commonly used in hand soaps to create a lather and help remove dirt and bacteria from the hands.
5. Baby Products: Due to its mildness and low irritation potential, cocoamidopropyl betaine is a common ingredient in baby shampoos, body washes and other personal care products.
6. Household Cleaners: CAPB is also used in household cleaners such as all-purpose cleaners, carpet cleaners and laundry detergents due to its ability to remove stains and dirt effectively.

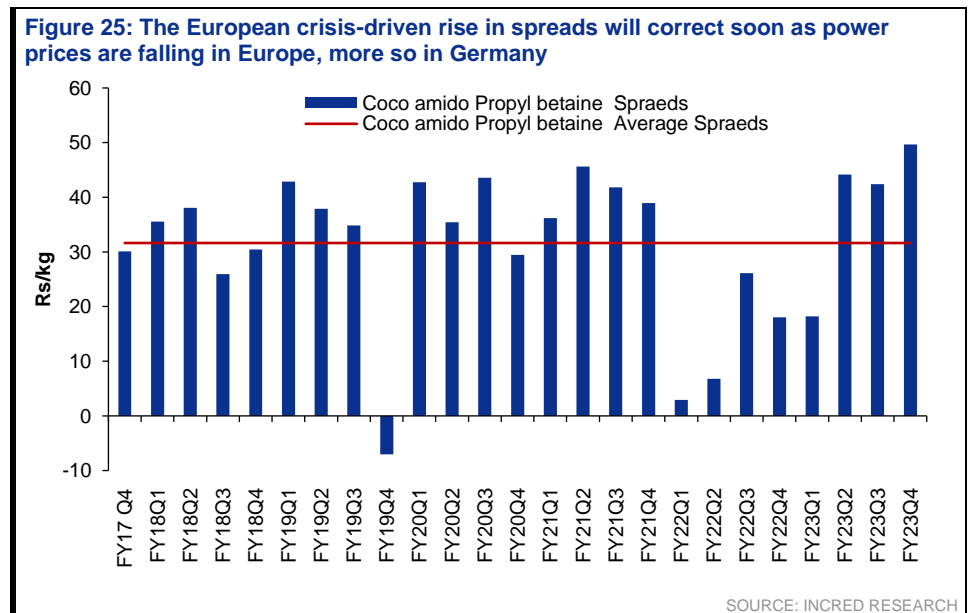
Cocoamidopropyl betaine manufacturers ➤

There are many manufacturers of cocoamidopropyl betaine (CAPB) around the world. Here are some of the well-known manufacturers:

1. BASF
2. Solvay
3. Stepan Company
4. Clariant
5. Innospec

Cocoamidopropyl betaine supernormal product spreads will correct ➤

Apart from Stephen Company, most other companies producing cocoamidopropyl betaine are based in Europe. The production problem in Germany is coming to an end (with Germany increasing the purchase of LNG, courtesy commissioning of regas capacity).



Usage of capryloyl glycine ➤

Capryloyl glycine is a synthetic peptide that is commonly used in cosmetic formulations due to its various beneficial properties. Some of the common uses of capryloyl glycine are:

1. Skin Care: Capryloyl glycine is used in skin care formulations due to its ability to reduce excess oil production on the skin's surface. It is often included in products formulated for oily or acne-prone skin.
2. Anti-aging: Capryloyl glycine is believed to have anti-aging benefits due to its ability to support the skin's natural moisture barrier and promote collagen production. It can be found in various anti-aging serums and creams.

3. Hair Care: Capryloyl glycine is used in hair care products due to its ability to condition the hair and improve its manageability. It is often included in shampoos, conditioners, and styling products.
4. Deodorants: Capryloyl glycine is included in deodorant formulations due to its ability to reduce the growth of odour-causing bacteria on the skin's surface.
5. Oral care: Capryloyl glycine is used in toothpastes and mouthwash formulations due to its ability to reduce the growth of bacteria that can cause bad breath and gum disease.

Overall, capryloyl glycine is valued for its ability to improve the effectiveness of various cosmetic formulations and promote healthy skin and hair.

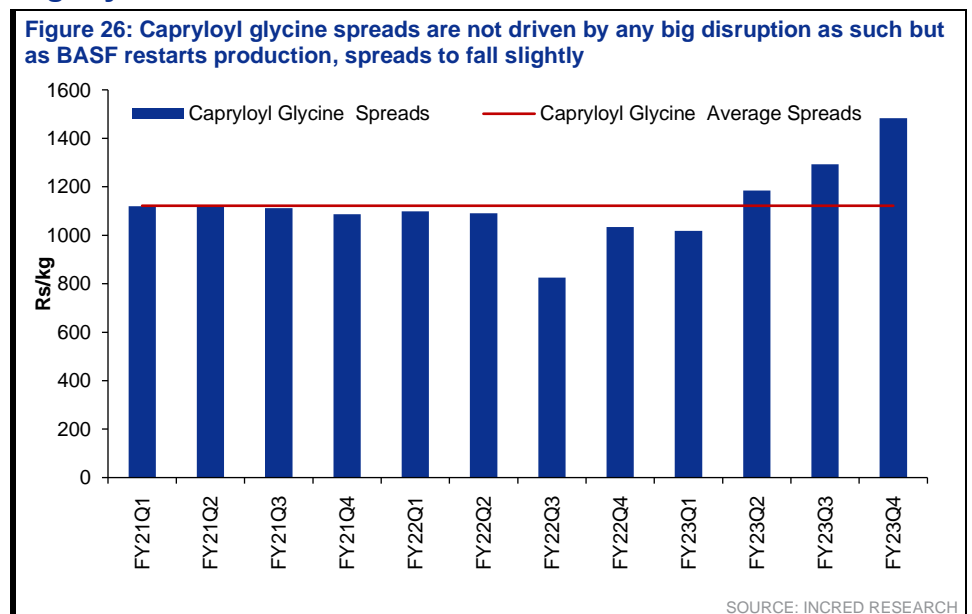
Capryloyl glycine manufacturers >

Capryloyl glycine is produced by several manufacturers around the world. Here are some companies that produce capryloyl glycine:

1. **Ajinomoto**: It is a Japanese company that produces a range of specialty chemicals and food products. The company produces capryloyl glycine under the brand name Amilite.
2. **DSM**: It is a Dutch company that produces a range of nutritional and specialty chemicals. The company produces capryloyl glycine under the brand name SYN-UP.
3. **Evonik**: It is a German specialty chemicals company that produces a range of products, including capryloyl glycine under the brand name TEGO Cosmo C 100.
4. **BASF**
5. **Sinoway Industrial Company**: It is a Chinese company that produces various chemicals, including capryloyl glycine which it offers under the brand name Sinoway C8G.

These are just a few examples of the several manufacturers of capryloyl glycine around the world. It is always important to choose a reputed manufacturer and ensure that their products meet the necessary quality and safety standards for specific application.

Capryloyl glycine spreads are not driven by any big disruption as such but as BASF restarts production, spreads to fall slightly >

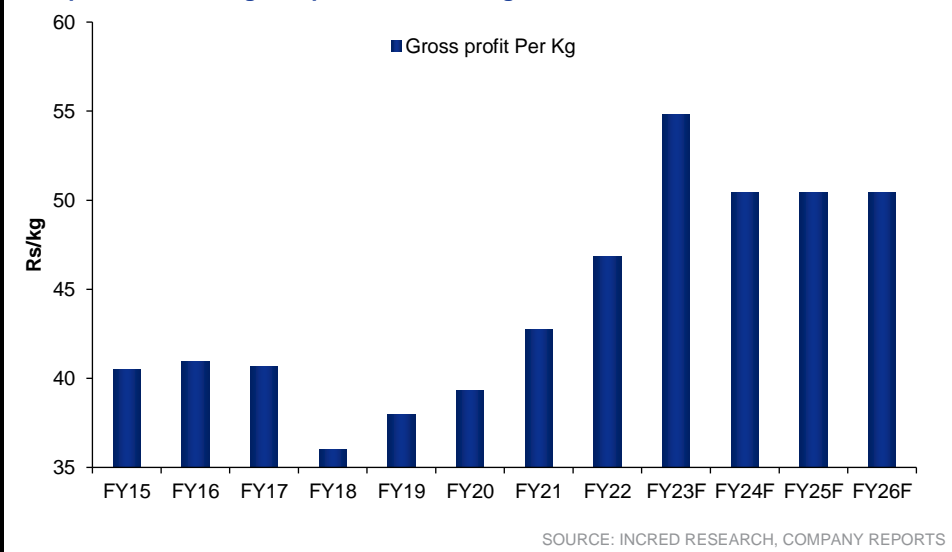


Earnings and valuation

The EPS will decline over FY23F-26F, in our view, at a 3.2% CAGR (FY23F-25F). At the same time, we believe the company’s RoE will decline from 22.5% in FY23F to 12.9% in FY26F. The key for GSL to succeed is improvement in the AMET market and low raw material prices – both these factors are well outside GSL’s control. An increase in the specialty portfolio may help improve margins but the company expects its mix to be in the range of 60-40 (60% in favour of the performance segment), at least for the next 5-10 years. Hence, headwinds in the AMET region and recession fears in the US will impact the valuation of GSL in FY24F.

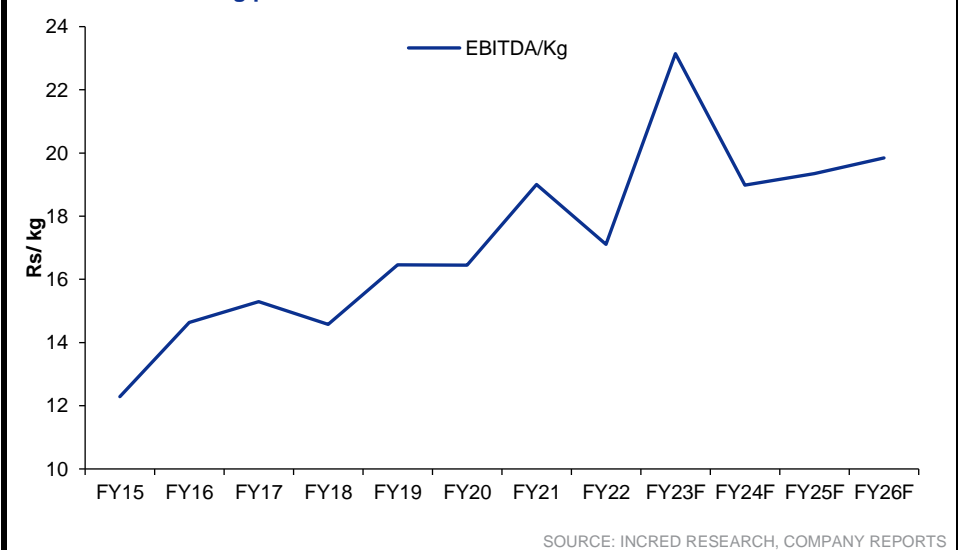
As supply chain normalizes and Germany restarts production, gross profit will fall ➤

Figure 27: FY23 has many one-time benefits like one-time grant and a production disruption-led rise in gross profit – these things will normalize in FY24F and onwards



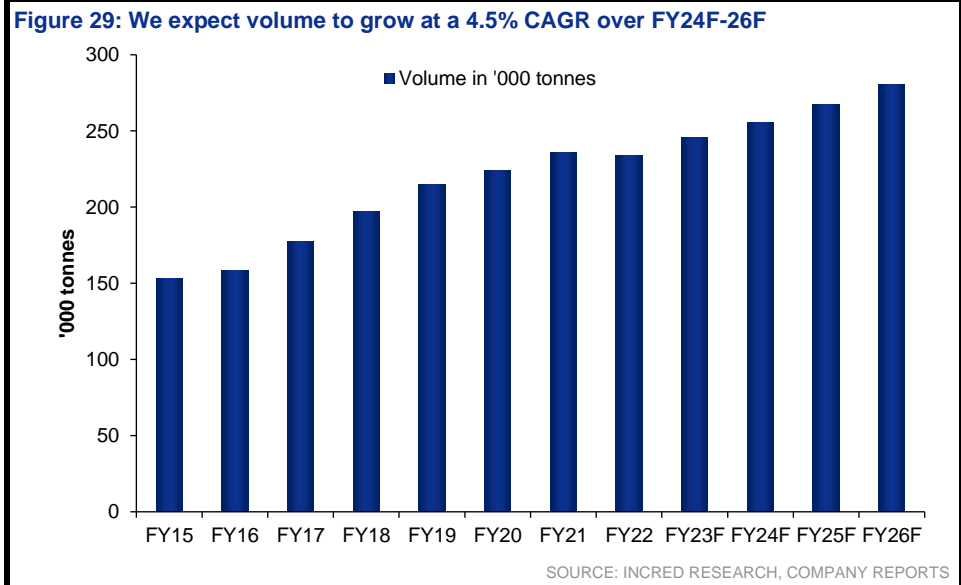
Consequently, EBITDA/kg will fall going ahead ➤

Figure 28: We expect EBITDA/kg to fall in FY24F, and due to operational leverage recover in the coming period



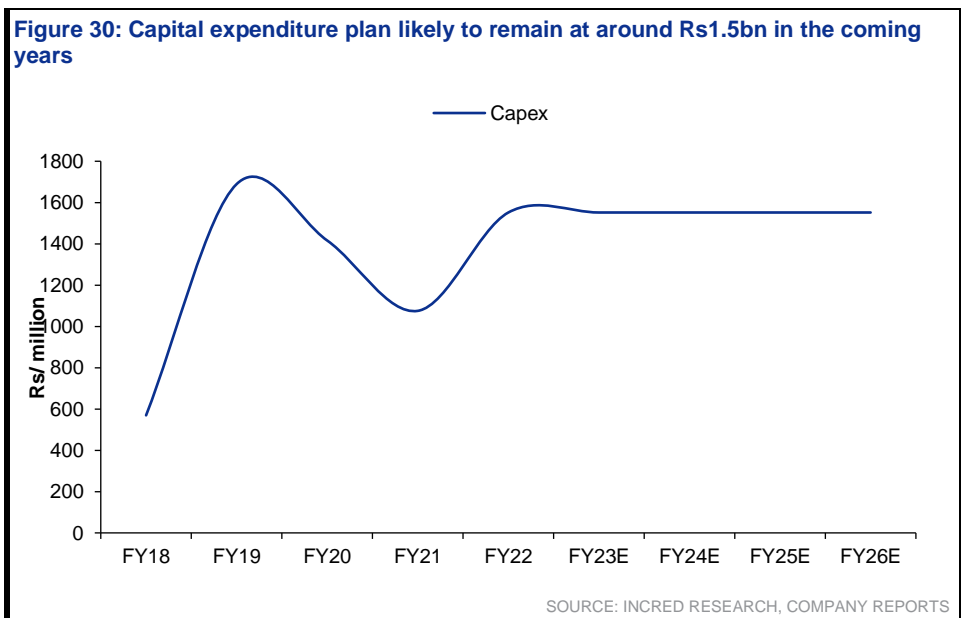
Global slowdown will lead to lower-than-historical average growth going ahead ➤

Historical volume growth has been 6% but we believe that in the coming three years, volume growth of the company will average around 4.5% CAGR.



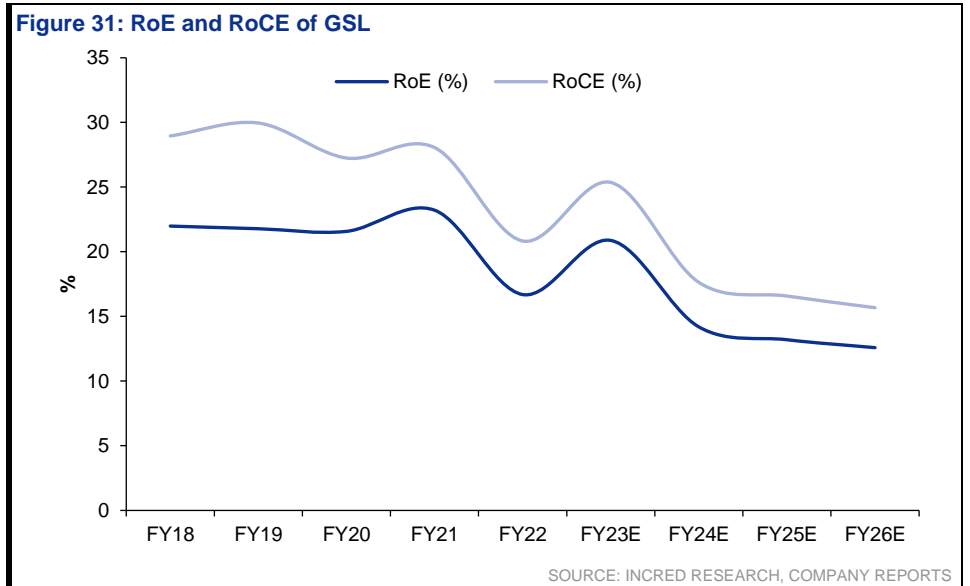
Capex likely to remain around Rs1.5bn/year over FY24F-26F ➤

GSL needs to go for aggressive capex in FY24F and beyond if it has to maintain a volume growth of 6%-8%. One thing which needs to be noted is that it takes three-to-four years for greenfield capex in performance surfactants to come to fruition, whereas the time period is seven-to-eight years for specialty surfactants. Hence, the company plans to incur brownfield capex for the time being, but such a long gestation period means demand forecasting becomes very important from GSL's perspective. This could prove tricky, especially in the AMET region, where the volume is highly volatile and hence, GSL must proceed with caution. As far as India is concerned, the company has acquired land bank near its Jhagadia plant for future capacity expansion.



RoE and RoCE to fall ➤

RoE and RoCE are expected to remain depressed in the medium- to short-term as the company's profitability will take a hit due to the prevailing macroeconomic factors. Although GSL has kept its RoCE greater than 20% for a large part of the last decade, it will be interesting to see whether the company will be able to deliver under these challenging conditions. It must be noted that RoCE decreased to 16% in FY22, and the same is expected to happen in FY23F as well.



We have used P/E to value commodity chemical companies ➤

We have valued GSL on a P/E basis as we consider it a more appropriate valuation method for commodity chemical companies than the discounted cash flow or DCF or EV/EBITDA methodologies. In our view, DCF is not a suitable valuation method because the earnings of chemicals companies are highly cyclical and forecasting long-term earnings reliably is very difficult. We believe a balance sheet-based valuation is inappropriate as short-term debt may rise because of inventory cycles, and in case of GSL it could be due to volatility in the prices of raw materials like lauryl alcohol and linear alkyl benzene.

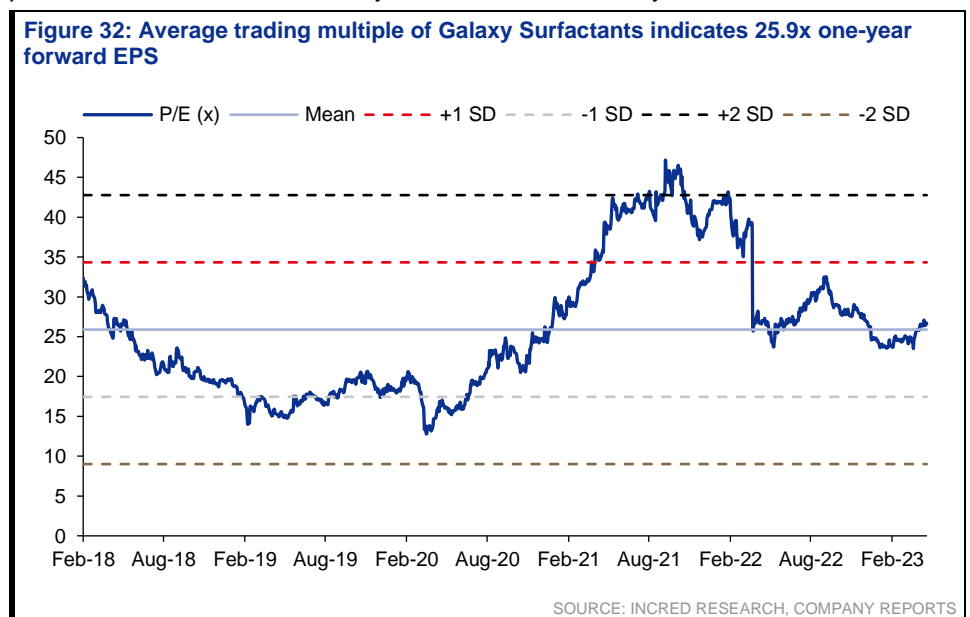


Figure 33: Target price valuation

FY25F EPS	97.2	Rs/ Share
Target Multiple	25.9	X
TP	2,519	Rs/ Share

SOURCE: INCRED RESEARCH, COMPANY REPORTS

We have valued GSL at 25.9x FY25F EPS as:

- We forecast a revenue CAGR of 2% and a PAT CAGR of -3.2% over FY23F-26F. The company’s RoE is set to dip from 20.9% in FY23F to 12.6% in FY26F. While asset utilization is almost constant, we expect the declining profitability to result in depressed RoE.
- As GSL is a unique business with no direct peers as such, it can act as a proxy to FMCG as most of its clients are FMCG companies. P&G and Colgate-

Palmolive are reporting flattish sales YoY, and the same goes for Godrej Consumer Products and Marico. This shows the slowly reviving consumer demand in the domestic market and hence, could be a headwind for GSL in the short- to medium-term.

- The same goes for AMET and RoW markets, which are facing major headwinds due to volatile market conditions in the AMET region and recession fears in the US, both of which account for a major portion of GSL's RoW market.
- The way forward for GSL is to focus on the domestic market currently, as the prospects in the international market are bleak. But whether it can increase profitability enough remains to be seen as GSL is mainly an export-oriented company, with 66% of its sales coming from the international market.

Risks

Downside risks

- The crude oil spike-linked rise in raw materials prices could be a negative surprise for GSL. As LABSA and ethylene oxide are crude oil derivatives, any spike in their prices could affect margins. This would be particularly tricky in the AMET region where it would be difficult to pass on increased prices due to the weak macroeconomic environment. The same goes for lauryl alcohol, which is a palm kernel oil derivative.
- The other risk could be further deterioration in Egypt's economy, which may lead to increased inflation, further deteriorating the spending power of end-consumers. This could lead to significant downtrading, resulting in multinationals losing market share. It will impact GSL as the company mostly caters to T1 customers in the AMET region.

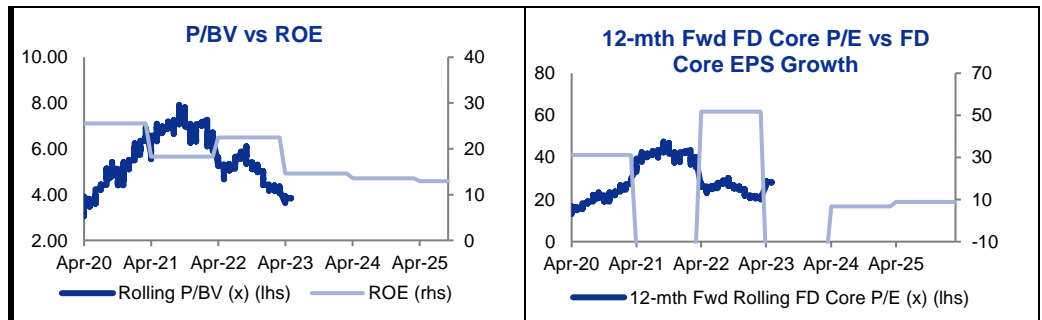
Upside risks

- Demand revival in the US and AMET markets could be a positive surprise, as it will lead to increased consumer spending and thereby lead to volume growth.
- Any regulation which favours green chemistry in the US could boost GSL's volume because it has a slight edge in that field. Recent regulations on dioxane usage could be cited as an example.
- The domestic market could mitigate the slowdown in the AMET region if India's economy remains resilient and consumer spending increases. In India, GSL has close to 60% market share and could further penetrate the market, especially in performance surfactants.

Key management personnel

- Mr. Unnathan Shekhar (Promoter, Managing Director) - He has been associated with the company since 20 May 1986. He holds a bachelor's degree in chemical engineering from the University Department of Chemical Technology, Mumbai and a Post Graduate Diploma in Management from Indian Institute of Management, Calcutta.
- Mr. K. Natarajan (Executive Director & COO) - He is an executive director and the chief operating officer of the company. He has been associated with GSL since 21 Apr 1993. He holds a bachelor's degree in commerce from University of Mumbai and is a cost accountant from the Institute of Cost and Works Accountants of India. He completed the Advanced Management Programme from the Harvard Business School in May 2016.
- Mr. G. Ramakrishnan (Promoter, Non-Executive Director) - He is the promoter and non-executive director of the company. He has been associated with the company since 20 May 1986. He holds a master's degree in commerce from the University of Bombay. He is a fellow member of The Institute of Chartered Accountants of India and the Institute of Cost and Works Accountants of India. He is also a qualified company secretary from The Institute of Company Secretaries of India.

BY THE NUMBERS



Profit & Loss

(Rs mn)	Mar-22A	Mar-23F	Mar-24F	Mar-25F	Mar-26F
Total Net Revenues	36,857	45,279	43,323	45,272	47,536
Gross Profit	10,972	13,479	12,897	13,477	14,151
Operating EBITDA	4,007	5,692	4,856	5,172	5,570
Depreciation And Amortisation	(711)	(754)	(833)	(904)	(968)
Operating EBIT	3,297	4,938	4,023	4,268	4,602
Financial Income/(Expense)	(129)	(257)	(257)	(257)	(257)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	125	125	125	125	125
Profit Before Tax (pre-EI)	3,293	4,806	3,891	4,136	4,470
Exceptional Items					
Pre-tax Profit	3,293	4,806	3,891	4,136	4,470
Taxation	(665)	(817)	(782)	(817)	(858)
Exceptional Income - post-tax					
Profit After Tax	2,628	3,988	3,109	3,319	3,612
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	2,628	3,988	3,109	3,319	3,612
Recurring Net Profit	2,628	3,988	3,109	3,319	3,612
Fully Diluted Recurring Net Profit	2,628	3,988	3,109	3,319	3,612

Cash Flow

(Rs mn)	Mar-22A	Mar-23F	Mar-24F	Mar-25F	Mar-26F
EBITDA	4,007	5,692	4,856	5,172	5,570
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(3,450)				
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	246	32	(8)	(49)	(49)
Net Interest (Paid)/Received	(159)	(129)	(129)	(129)	(129)
Tax Paid	(1,036)	(844)	(896)	(966)	
Cashflow From Operations	(393)	4,752	3,824	4,028	5,392
Capex	(1,552)	(1,552)	(1,552)	(1,552)	(1,552)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments	438	438	438	438	438
Other Investing Cashflow	272	272	272	272	272
Cash Flow From Investing	(841)	(841)	(841)	(841)	(841)
Debt Raised/(repaid)	941	(951)	(951)	(951)	(951)
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(142)	(142)	(142)	(142)	(142)
Preferred Dividends					
Other Financing Cashflow	(207)	(207)	(207)	(207)	(207)
Cash Flow From Financing	592	(1,301)	(1,301)	(1,301)	(1,301)
Total Cash Generated	(643)	2,610	1,682	1,887	3,250
Free Cashflow To Equity	(293)	2,960	2,032	2,236	3,600
Free Cashflow To Firm	(1,106)	4,039	3,111	3,316	4,679

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rs mn)	Mar-22A	Mar-23F	Mar-24F	Mar-25F	Mar-26F
Total Cash And Equivalents	711	3,219	2,680	3,322	6,109
Total Debtors	6,380	6,590	6,306	6,590	6,919
Inventories	7,118	6,272	6,001	6,272	6,585
Total Other Current Assets	1,527	1,911	1,828	1,910	2,006
Total Current Assets	15,736	17,993	16,816	18,094	21,619
Fixed Assets	6,092	6,890	7,608	8,256	8,840
Total Investments					
Intangible Assets	82	82	82	82	82
Total Other Non-Current Assets	4,095	5,092	6,200	7,175	7,175
Total Non-current Assets	10,269	12,063	13,890	15,513	16,097
Short-term Debt	2,864	2,309	736		
Current Portion of Long-Term Debt					
Total Creditors	5,189	5,563	5,323	5,562	5,841
Other Current Liabilities	525	525	525	525	525
Total Current Liabilities	8,577	8,396	6,583	6,087	6,365
Total Long-term Debt	796	989	315		
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	487	487	487	487	487
Total Non-current Liabilities	1,283	1,476	802	487	487
Total Provisions	402	402	402	402	402
Total Liabilities	10,262	10,275	7,787	6,976	7,254
Shareholders Equity	15,744	19,718	22,813	26,118	29,716
Minority Interests					
Total Equity	15,744	19,718	22,813	26,118	29,716

Key Ratios					
	Mar-22A	Mar-23F	Mar-24F	Mar-25F	Mar-26F
Revenue Growth	32.4%	22.8%	(4.3%)	4.5%	5.0%
Operating EBITDA Growth	(10.7%)	42.0%	(14.7%)	6.5%	7.7%
Operating EBITDA Margin	10.9%	12.6%	11.2%	11.4%	11.7%
Net Cash Per Share (Rs)	(83.17)	(2.23)	45.95	93.70	172.30
BVPS (Rs)	444.04	556.14	643.44	736.65	838.13
Gross Interest Cover	25.65	38.42	31.31	33.21	35.81
Effective Tax Rate	20.2%	17.0%	20.1%	19.8%	19.2%
Net Dividend Payout Ratio	5.4%	3.6%	4.6%	4.3%	3.9%
Accounts Receivables Days	54.81	52.28	54.33	51.98	51.86
Inventory Days	80.35	76.85	73.62	70.45	70.28
Accounts Payables Days	63.16	61.70	65.30	62.48	62.33
ROIC (%)	12.6%	17.8%	13.6%	13.2%	13.6%
ROCE (%)	18.5%	23.0%	17.0%	16.9%	16.3%
Return On Average Assets	11.7%	14.9%	10.9%	10.9%	10.7%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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