

India
HOLD (Initiating coverage)

Consensus ratings*: Buy 5 Hold 0 Sell 0

Current price:	Rs1,024
Target price:	Rs1,124
Previous target:	NA
Up/downside:	9.8%
EIP Research / Consensus:	-2.4%
Reuters:	
Bloomberg:	AETHER IN
Market cap:	US\$1,650m Rs135,744m
Average daily turnover:	US\$2.0m Rs161.9m
Current shares o/s:	0.0m
Free float:	18.0%

*Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(4.1)	8.1	20.9
Relative (%)	(6.2)	(0.2)	5.2

Major shareholders	% held
Promoters	82.0
SBI Magnum Mid Cap	9.0
Retail	2.0

Aether Industries Ltd

Process chemistry expertise backed by R&D

- Aether Industries manufactures intermediates that are used in a variety of end-user industries like pharmaceuticals, agrochemicals, oil & gas, etc.
- Process chemistry expertise, which is independent of end products, & well-diversified portfolio backed by strong R&D outlines its clear growth trajectory.
- We value the stock at 40x EV/EBITDA and initiate coverage on it with a HOLD rating and a target price of Rs1,124.

Process chemistry expertise acts as a major entry barrier

Aether Industries (Aether) is present in various not-so-easy-to-replicate chemistries like Grignard, Organolithium and Coupling Reaction, which offers it numerous advantages. These chemistries are difficult to optimize and hence, serve as a major entry barrier. Moreover, the focus on chemistry, rather than the end product, allows the company to switch between products, offering it a higher top line and better margins. It is also one of the few specialty chemical companies to have three different business models, such as contract manufacturing, large-scale manufacturing, and CRAMS in only five years of beginning commercial production.

Strong R&D backbone to lead the way

Aether's R&D spending, as a percentage of its sales, is a way higher than its peers (close to 7%). This is the highest R&D spending in India's specialty chemicals industry. As a result, Aether has commercialized close to 25 products. This has also ensured a strong pipeline of new products, offering the opportunity of import substitution for the company, thereby weaning away market share from Chinese specialty chemical players.

Huge capex-led growth on the cards

Aether is incurring a significant amount of capex, as its net block is expected to double in FY26 from the FY23 level. The company is currently in the process of expanding manufacturing capacities at its Facility 3 (for large-scale manufacturing), Facility 4 (exclusively for contract manufacturing), and Facility 5 (housing polyols and various new projects). With a capex plan worth nearly Rs13bn in the next few years, Aether's topline is likely to show multifold growth when the plants are fully commercialized (latest by FY28F).

We value stock at 40x EV/EBITDA; initiate coverage with HOLD rating

Aether is likely to register a 25% revenue CAGR over FY23-26F, and in the meantime it may also register EBITDA margin expansion of 300bp mainly due to the rising share of margin-accretive CRAMS division. Aether is also incurring significant capex, which will further aid growth. However, a lot of it already appears to be discounted in the stock price. We have assigned a HOLD rating to the stock with a target price of Rs1,124 and a two-year forward EV/EBITDA of 40x. The key downside risk is a fall in prices of intermediate molecules, which will affect revenue growth of Aether. Any delay in the capex plan can also dent the company's valuation. The upside risk is a rapid rise in global prices of molecules.

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Financial Summary

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue (Rsm)	5,900	6,511	7,596	11,014	12,974
Operating EBITDA (Rsm)	1,681	1,862	2,127	3,414	4,152
Net Profit (Rsm)	1,089	1,304	1,407	2,320	2,762
Core EPS (Rs)	10.2	11.0	10.9	17.5	20.8
Core EPS Growth	33.7%	7.9%	(0.5%)	59.8%	19.1%
FD Core P/E (x)	100.47	93.15	93.65	58.59	49.21
DPS (Rs)	0.0	0.0	0.0	0.0	0.0
Dividend Yield	0.00%	0.00%	0.00%	0.00%	0.00%
EV/EBITDA (x)	66.69	64.68	57.86	37.59	31.16
P/FCFE (x)	(84.43)	(24.01)	242.74	(376.46)	5,076.47
Net Gearing	69.0%	(8.2%)	(40.3%)	(31.8%)	(24.6%)
P/BV (x)	29.84	10.25	6.32	5.71	5.11
ROE	38.8%	16.0%	8.3%	10.2%	11.0%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

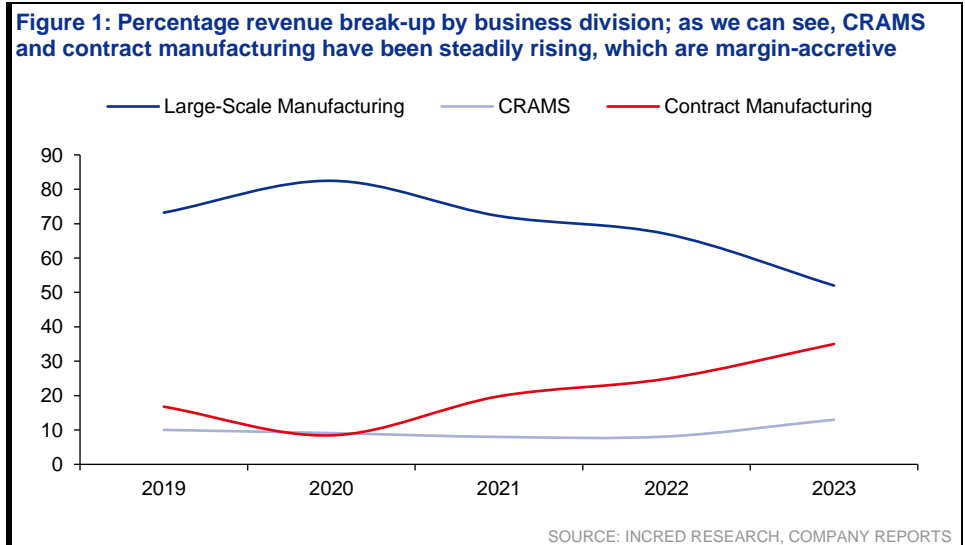
Strong fundamentals with a diverse portfolio

Aether Industries (Aether) is a specialty chemicals company mainly focusing on manufacturing intermediates for pharmaceutical and agrochemical companies. Intermediates serve as raw materials for APIs (active pharmaceutical ingredients) in the case of pharmaceutical companies and as AIs (active ingredients) for agrochemical companies (large-scale manufacturing). Aether also has revenue contribution from CRAMS (contract research and manufacturing services) and an exclusive manufacturing division. In FY23, the revenue contribution from large-scale manufacturing, CRAMS and the exclusive manufacturing division was 52%, 13% and 34%, respectively. Aether's important differentiator is its focus on a chemistry-driven approach rather than product-driven, which enables it to have a well-diversified portfolio coupled with fungible capacity. Moreover, its presence in the not-so-easy-to-replicate chemistry provides it a key entry barrier. This is further corroborated by its high R&D expenses, as a percentage of sales, among its specialty chemicals peers.

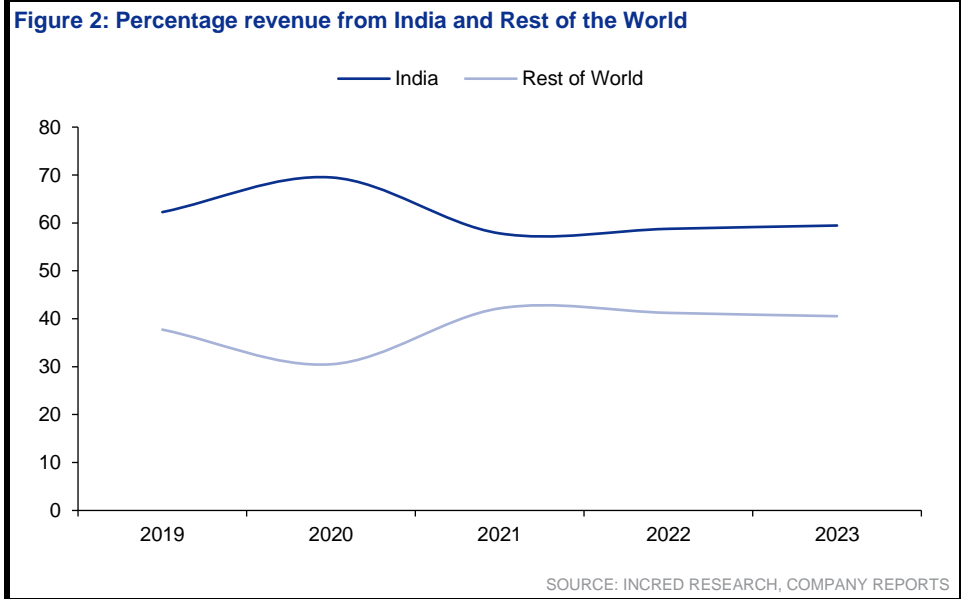
Business Analysis

Three business divisions►

Aether's revenue mainly comes from its three business divisions such as large-scale manufacturing, CRAMS, and contract/exclusive manufacturing. Out of these three business divisions, CRAMS has the highest EBITDA margin of 70%, contract manufacturing's EBITDA margin is around 32% and large-scale manufacturing has the lowest margin of around 25-28%.

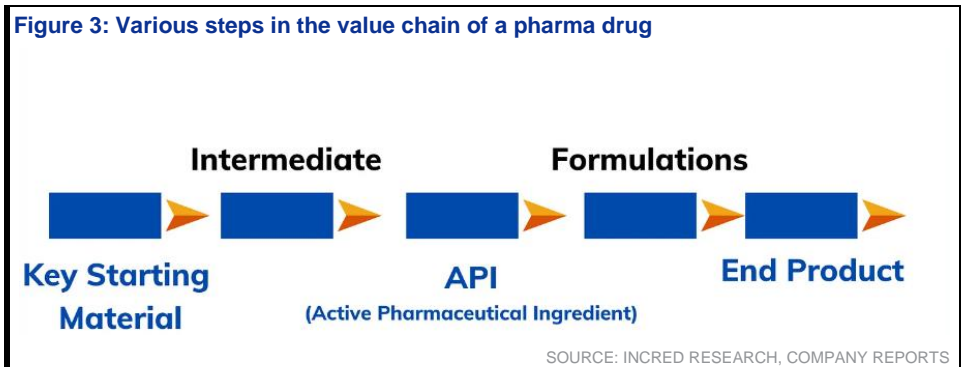


Aether's primary thesis, while manufacturing a chemical, involves import substitution, i.e., it takes on the manufacturing of mainly those products for which India is dependent on imports, mostly from China. As a result, a significant chunk of its revenue comes from India. This trend is expected to continue as the company is looking to expand into more import-substitution products.



Large-scale manufacturing >

Large-scale manufacturing is the largest revenue contributor to Aether's topline. In this division, Aether manufactures intermediates for pharmaceutical companies. To understand what intermediates are, let's look at the value chain of a pharma drug. The first stage in the manufacturing of a drug is the key starting material, which is a raw material that is significant for manufacturing the intermediates. Technically, key starting material has been adopted to indicate the point where regulatory control and good manufacturing practices must be introduced into the manufacturing of a drug substance. The key starting material is used to make intermediates, which can be called raw material for APIs, and this is where Aether specializes. The API is the most important part of a drug, and it is what acts on the disease. Finally, this API is formulated in tablet/capsule/liquid form, based on the usage, which is finally consumed by the patient.



What differentiates Aether from other specialty chemical players >

Aether's main differentiator is its focus on a chemistry-driven approach rather than a product-driven approach. It means Aether focuses on the chemistry used in the manufacture of the product, rather than the product itself. This allows it to have a well-diversified portfolio without overtly relying on a single product. Also, its presence in the not-so-easy-to-replicate chemistries serves as a significant entry barrier for the company. As a result, the price per kg for Aether's molecules is higher compared with other specialty chemical players.

Figure 4: Aether enjoys a significant premium over its peers as far as the realization is concerned

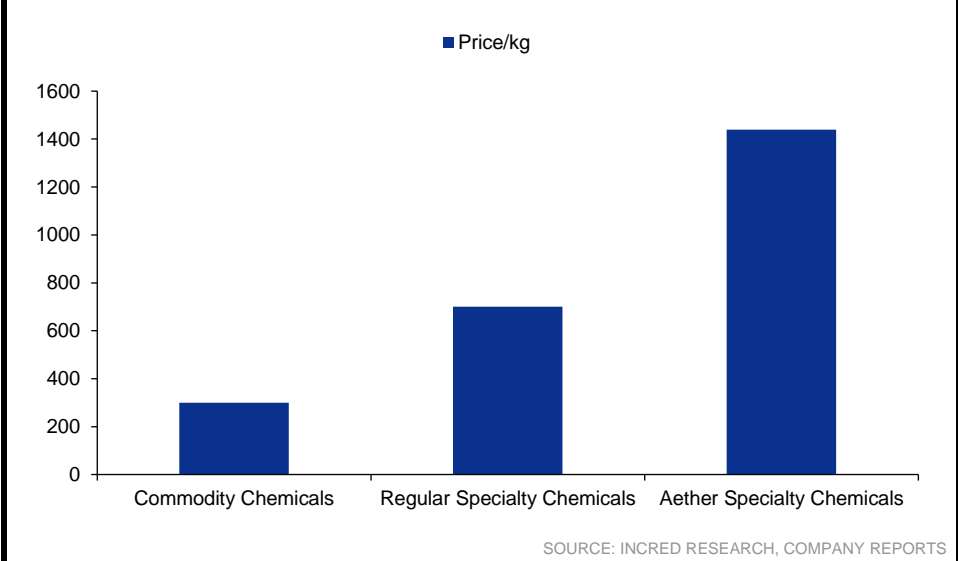


Figure 5: The more the number of steps in the manufacturing process, the more significant are the barriers to entry

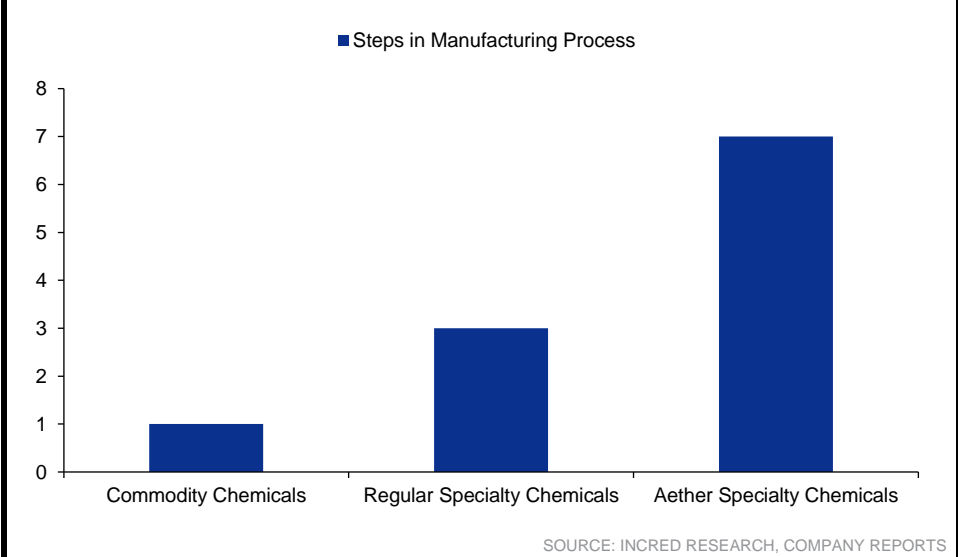
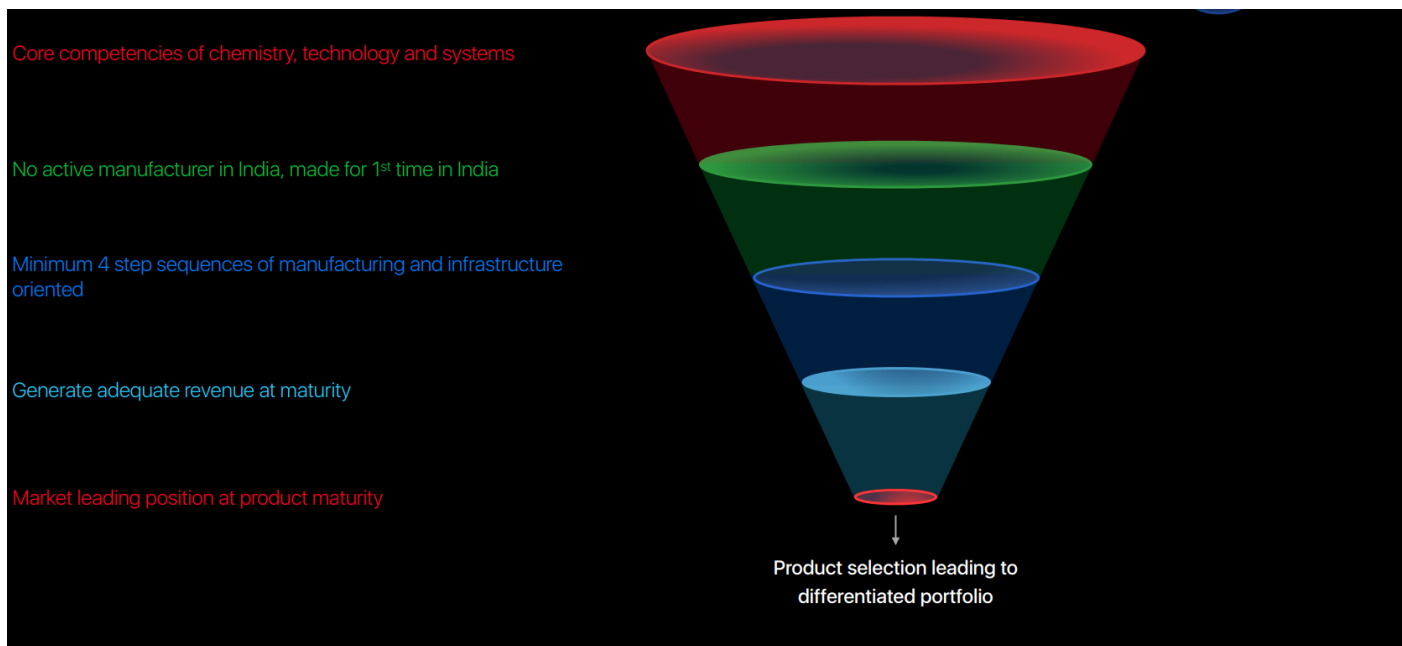


Figure 6: Aether's product selection methodology



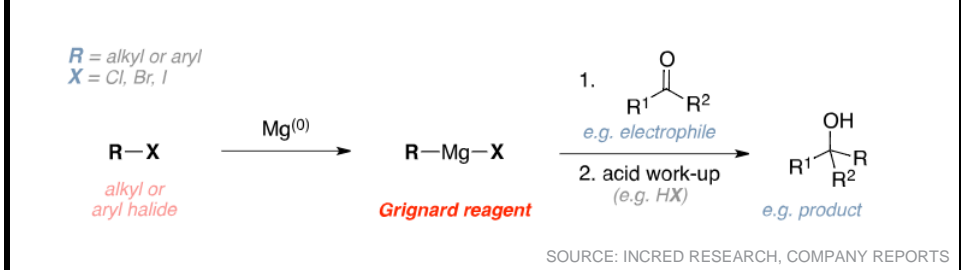
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Grignard's Chemistry ►

Out of the various chemistry skills which Aether possesses, Grignard's Chemistry is the one which employs the greatest number of molecules. Let's understand it right from the basics.

- When you have some specific molecules and want to use them to produce other molecules, you must break chemical bonds between some atoms and establish new chemical bonds between other atoms. **But it's difficult to break the bonds as the bonds between carbon atoms are very strong. Mr. Victor Grignard gave us the first reaction that could be used to break and form new bonds between carbon atoms.**
- Mr. Grignard first discovered that finely crushed magnesium can be dissolved in ether mixed with bromoalkene. This leads to the formation of a substance that has later been called the Grignard reagent, which again can react with many different substances such as ketones, aldehydes, and alkenes. An alkene, by the way, is a chemical substance that consists only carbon and hydrogen and is 'unsaturated' – in the sense that at least two carbon atoms are attached to each other by a double bond. When the substance is called bromoalkene, the name means that at least one of the hydrogen atoms has been replaced with bromine.
- The Grignard reaction leads to the formation of alcohols based on the original molecules, and the alcohols can again be used as raw material in the production of many new products. This reaction is not only very useful but also easy to run. You can basically start the whole process just by shaking the ingredients in a test tube.
- **But it has been very frustrating for chemists that they failed to understand how such a basic chemical reaction works at the molecular level. This lack of knowledge led to, among other things, that process optimization became very difficult.**
- Hence, this underlines the importance of Aether's process chemistry expertise in Grignard Chemistry, as there are not many who understand how the reaction functions. As a result, all those who have very high barriers to entry can enjoy a premium in the pricing of their products compared to peers.

Figure 7: A simple reaction illustrating Grignard Chemistry



Aether’s molecules for large-scale manufacturing ➤

Aether is well-diversified as far as its large-scale manufacturing portfolio is concerned. It mainly consists of pharma and agri intermediates. This division is, however, expected to face some pricing pressure due to the re-entry of Chinese players in the fray and hence, could lead to dilution of the company’s margins in FY24F. Aether has also started the production of five new intermediates (3-R-amino-1-butanol, IBCC, 10-MISB, 1,3-dimethyl adamantane, and trans-4-amino-cyclohexanol) and these products are expected to contribute to the topline in FY25F.

Figure 8: Topline contribution in FY23 from Aether’s large-scale manufacturing of molecules

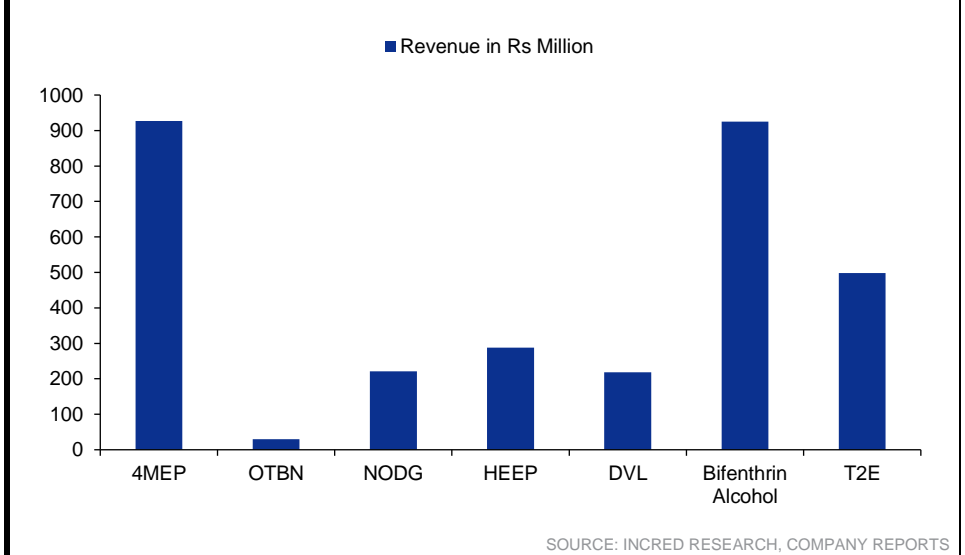
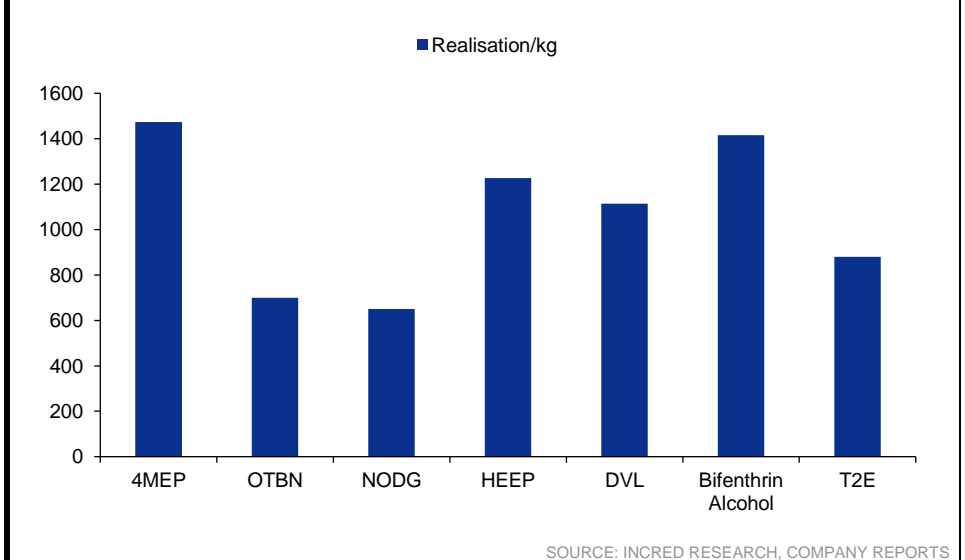


Figure 9: As can be seen from this graph, 4MEP and bifenthrin alcohol have a higher realization compared to other molecules and thus, have a higher revenue contribution



A look at these molecules in depth

4-(2-methoxyethyl) phenol or 4MEP➤

4-(2-methoxyethyl) phenol (4MEP) is one of the key intermediates used in the production of Metoprolol. Metoprolol is used alone, or in a combination with other medications, to treat high blood pressure. It widens the walls of blood vessels, thus making the flow of blood easier, and falls into the category of beta-blocker. To this date, it is one of the preferred beta-blockers in general clinical guidelines and it is widely prescribed in the Netherlands, New Zealand, and the US. Metoprolol is commonly employed as a succinate and tartrate derivative, depending on whether the formulation is designed to be of immediate release or extended release. **Approximately 0.7MT (metric tonne) of 4-(2-methoxy ethyl) phenol is required to manufacture 1.0mt (million tonne) of Metoprolol derivatives.** Other than to produce Metoprolol, there is no other key end-application for 4MEP.

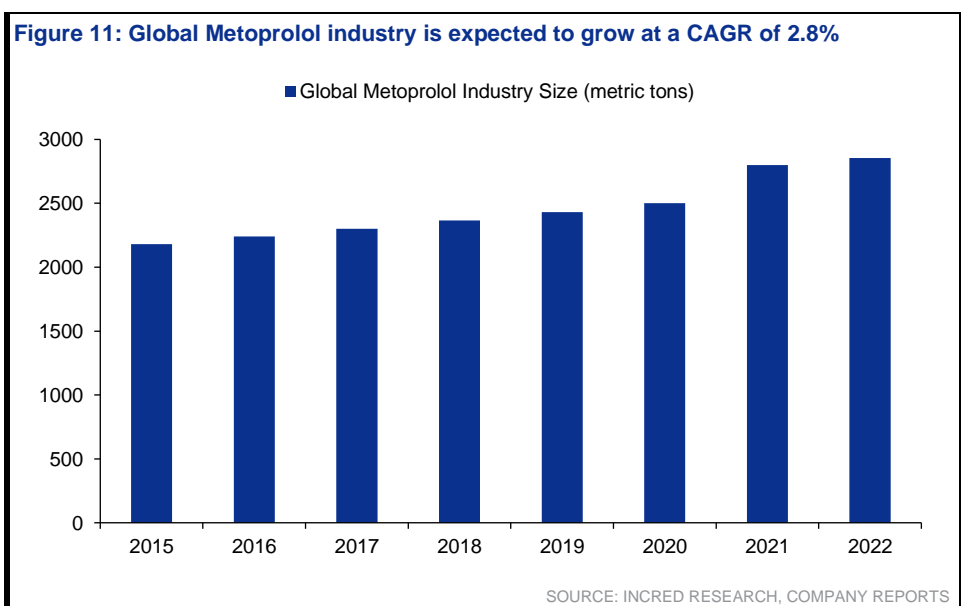
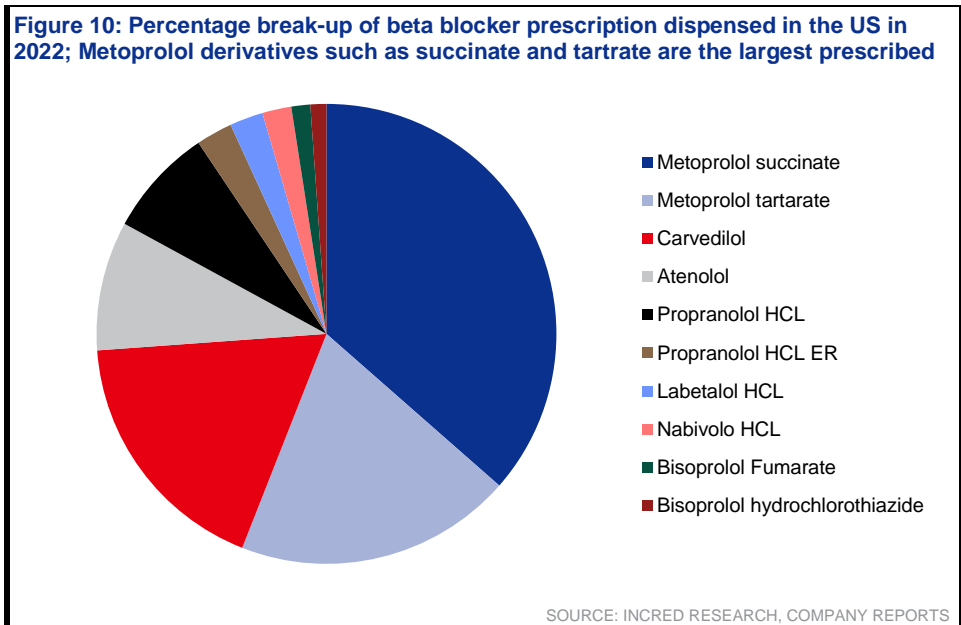


Figure 12: It requires 0.7MT of 4MEP to manufacture 1mt of metoprolol derivatives

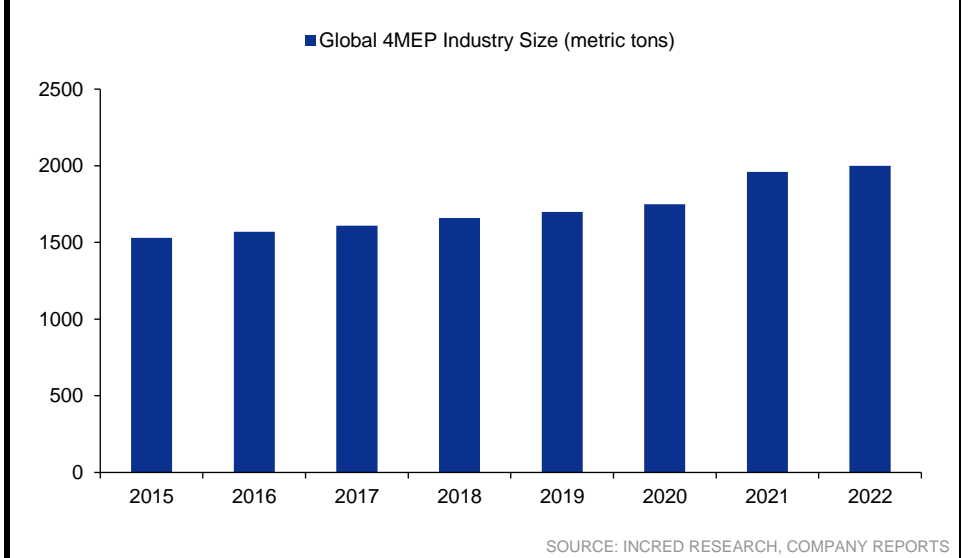


Figure 13: Aether is the largest producer of 4MEP in the world

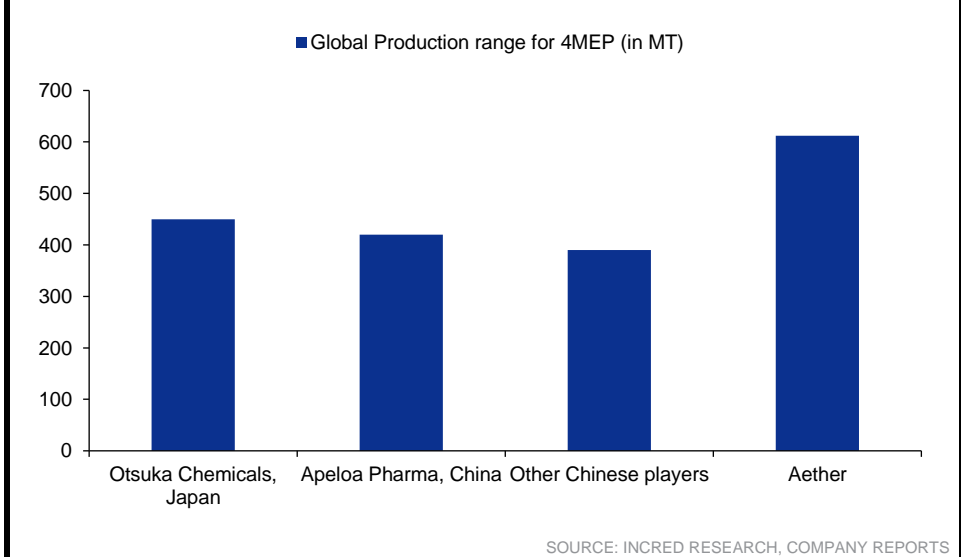
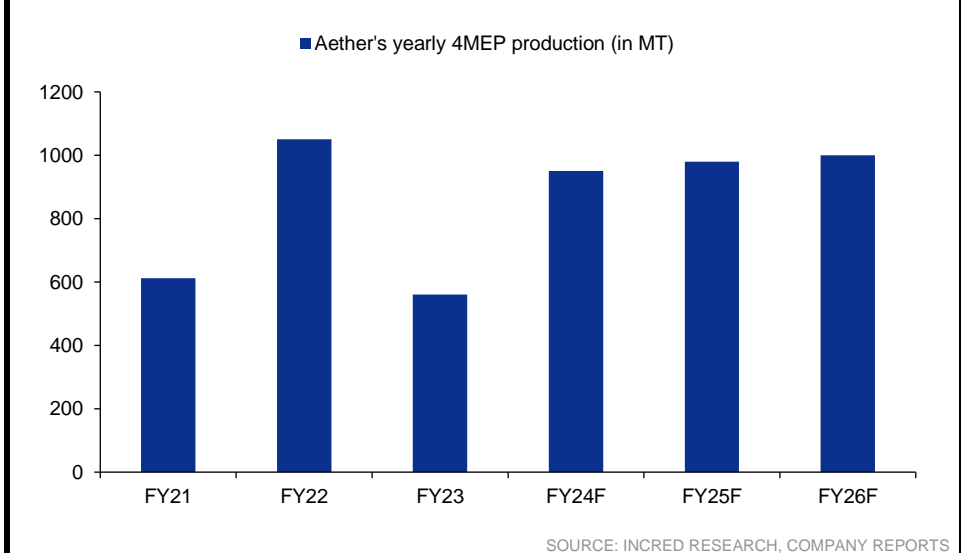
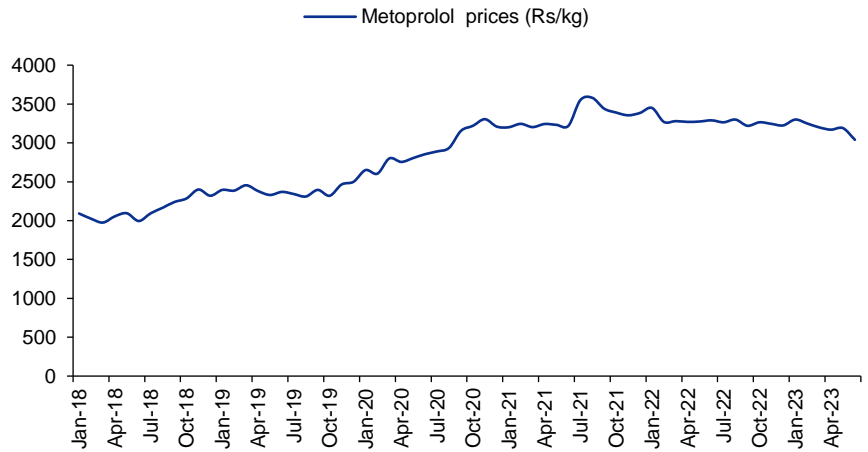


Figure 14: Aether's yearly 4MEP production volume



Aether’s yearly production volume for 4MEP is expected to increase as it has signed a production deal with its competitor Otsuka to produce 300MT 4MEP yearly during FY24F-26F. The sharp production decline so far in 2023 was because of the excess inventory plaguing the entire pharmaceutical industry.

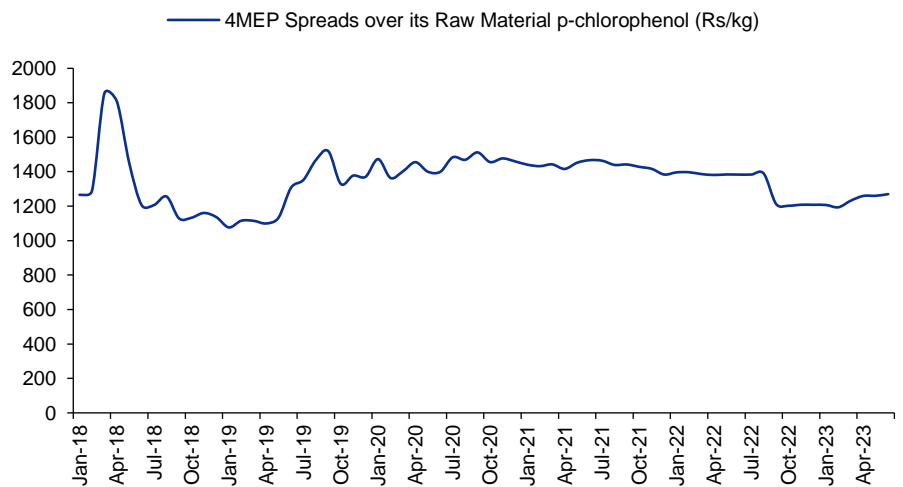
Figure 15: Metoprolol prices have showed signs of a downtrend in recent months



SOURCE: INCRED RESEARCH, COMPANY REPORTS

However, declining Metoprolol prices, in recent months, could affect margins and the topline going ahead.

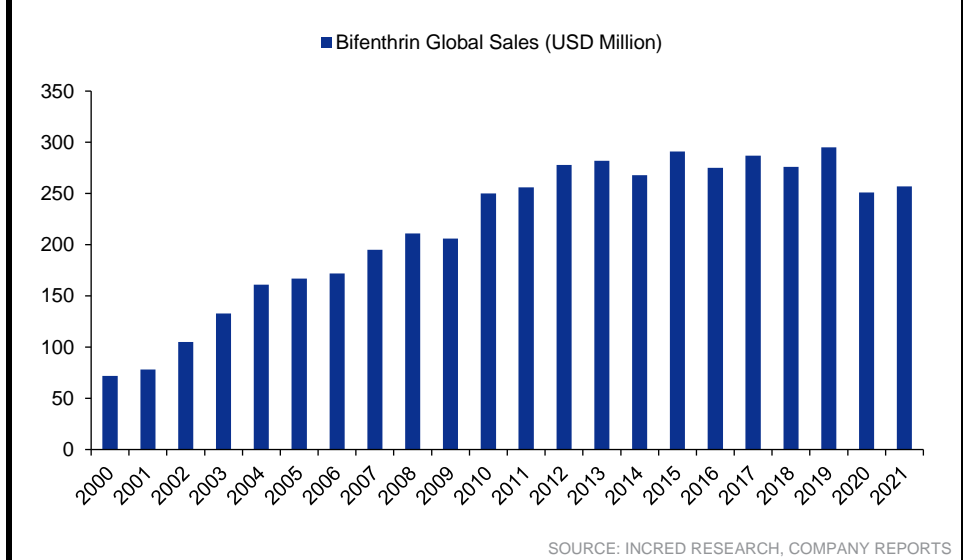
Figure 16: 4MEP’s spreads over its raw material have decreased in recent months



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Bifenthrin alcohol >

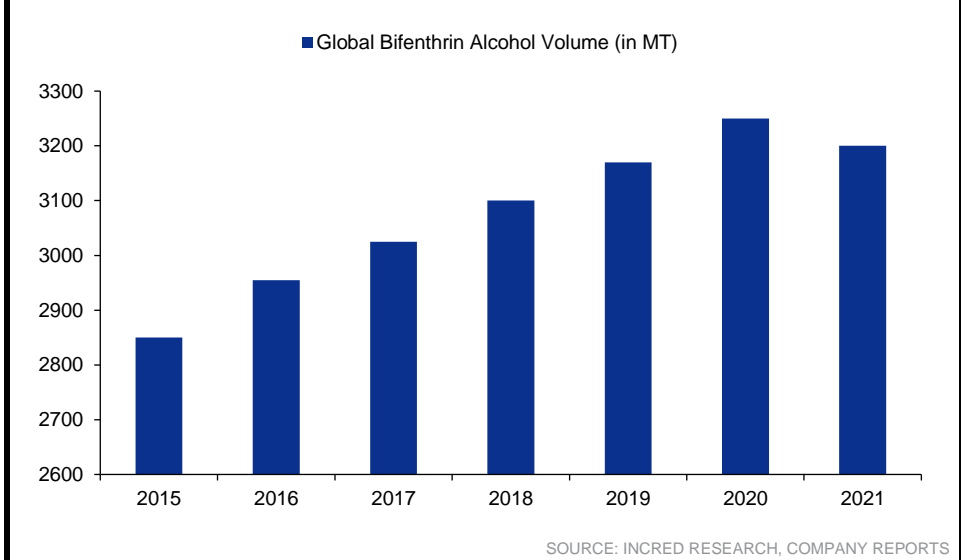
Bifenthrin alcohol is used as an intermediate in the manufacture of bifenthrin. Bifenthrin belongs to the broad-spectrum pyrethroid that benefits from activity against certain mite species. Originally launched in 1986, bifenthrin is now FMC’s (an insecticide manufacturer) most commercially significant insecticide. This novel pyrethroid is used to control a broad range of insect pests including whiteflies, insect larvae and mites. Nearly 0.4MT of bifenthrin alcohol is required to produce 1MT of bifenthrin.

Figure 17: Bifenthrin's global sales have stagnated

Sales of bifenthrin have stagnated due to it being in a class of insecticides, called pyrethroids. Pyrethroids are dying products.

- While pyrethroids have been widely used as insecticides for the past several years, there have been rising concerns about their potential impact on human health and the environment. As a result, some specific pyrethroid products have faced restrictions or a ban in certain regions.
- There have been concerns regarding the potential health effects of pyrethroids, particularly their impact on the human nervous system. Although pyrethroids are generally considered to have low toxicity to humans, there have been reports of acute poisoning, especially among individuals who are excessively exposed or have underlying health conditions. Some studies have also suggested possible links between pyrethroid exposure and specific health issues, such as neurodevelopmental disorders and endocrine disruption. These concerns have led to increased scrutiny and regulatory action.
- Pyrethroids can have harmful effects on non-target organisms and ecosystems. They can be toxic to beneficial insects, including bees and aquatic organisms. Pyrethroids can persist in the environment for extended periods, leading to accumulation in water bodies, soil, and vegetation. This persistence can increase the risk of exposure for non-target organisms and potentially disrupt the ecological balance. In some cases, restrictions on pyrethroid use have been imposed to protect biodiversity and reduce the ecological impact.
- Prolonged and widespread use of pyrethroids has led to the development of resistance in specific insect populations. Over time, pests can evolve mechanisms to detoxify or tolerate pyrethroids, rendering them ineffective. When resistance occurs, higher concentrations or alternative insecticides are often required to achieve the desired pest control. This issue highlights the need for diversified pest management strategies and the responsible use of pyrethroids.

Figure 18: Bifenthrin alcohol volume has also stagnated



Aether is the only manufacturer of bifenthrin alcohol (BFA) in India. Aether started commercial production of BFA in Aug 2021 and currently has a production capacity of 480MT per annum. Globally, the market is crowded with Chinese players providing the intermediate like Changzhou Booming Crop Science Co., Hefeng Agro Co., Jiangsu Chunjiangruntian Agrochemical Co., Jiangsu Huifeng Agrochemical Co. and more. Chinese players are major suppliers for Indian agrochemical companies. India imported nearly 1,100MT of bifenthrin alcohol in 2020-21. In calendar year 2020, the Chinese players produced 2,750-2,790MT of BFA, accounting for approximately 85% to 86% of the global market share in BFA, while other global players produced 460-500MT of BFA, accounting for the remaining 14% to 15%.

Figure 19: Bifenthrin alcohol prices have declined considerably

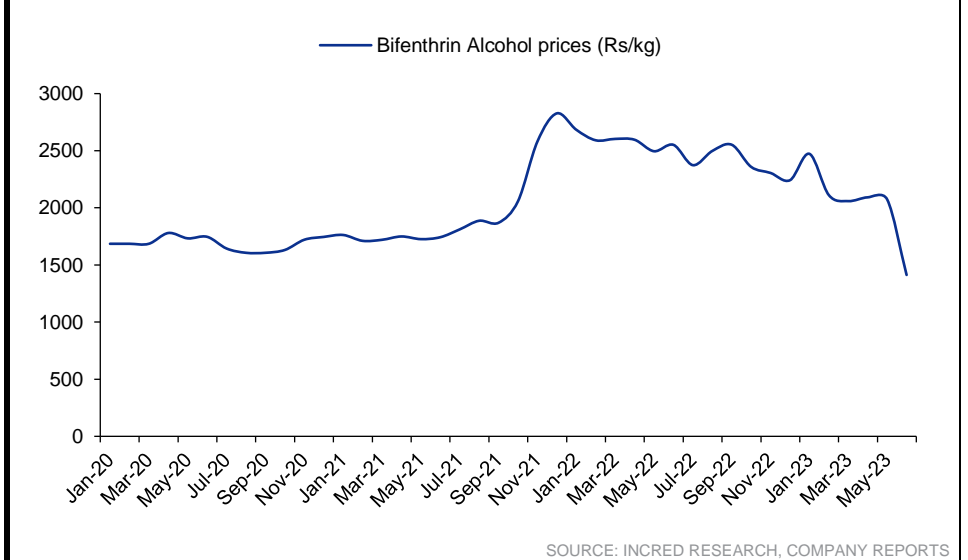
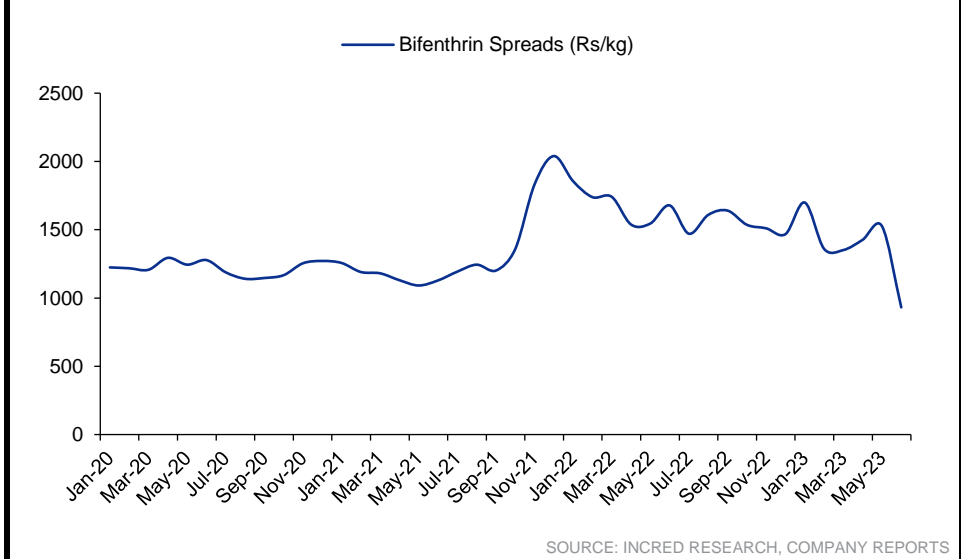


Figure 20: Consequently, its spreads over key raw material 2,6-dichlorotoluene have also declined



Thiophene-2-ethanol (T2E) ➤

Thiophene-2-ethanol (T2E) is one of the key intermediates for manufacturing clopidogrel, an antiplatelet drug. Antiplatelet drugs, often called platelet agglutination inhibitors, are a class of therapeutics that help in reducing or preventing blood coagulation by limiting the activity of platelets to stick or bind together. Clotting of blood is a physiological action of the body which helps in controlling external bleeding during injuries. But this tendency of blood clotting may not be useful when there are no injuries or cuts. Hence, antiplatelet drug agents are therapeutically used to stop clotting when not required.

- In the production process, 115kg of T2E is added to produce 180kg (12.91 molecular weight, 91.85%) of clopidogrel. This gives a stoichiometry of nearly 0.65kg of T2E for production of 1kg of clopidogrel.
- **The volume of the global T2E industry grew at a CAGR of 57.7% from 80MT in 2015 to 780MT in 2020 and is expected to grow at a CAGR of 12.7% from 780MT in 2020 to 1,420MT in 2025F (Source: Aether’s DRHP).**
- Aether was the largest manufacturer of T2E in the world in 2020, in terms of production volume, and the only manufacturer of this product in India. Aether’s production volume of T2E grew at a CAGR of 75.7% from 72MT in 2017 to 392 MT in 2020. In the calendar year 2020, Aether accounted for nearly 50% of the global T2E market.

Figure 21: Global T2E market is expected to grow at a CAGR of 12.5% over 2021-25F

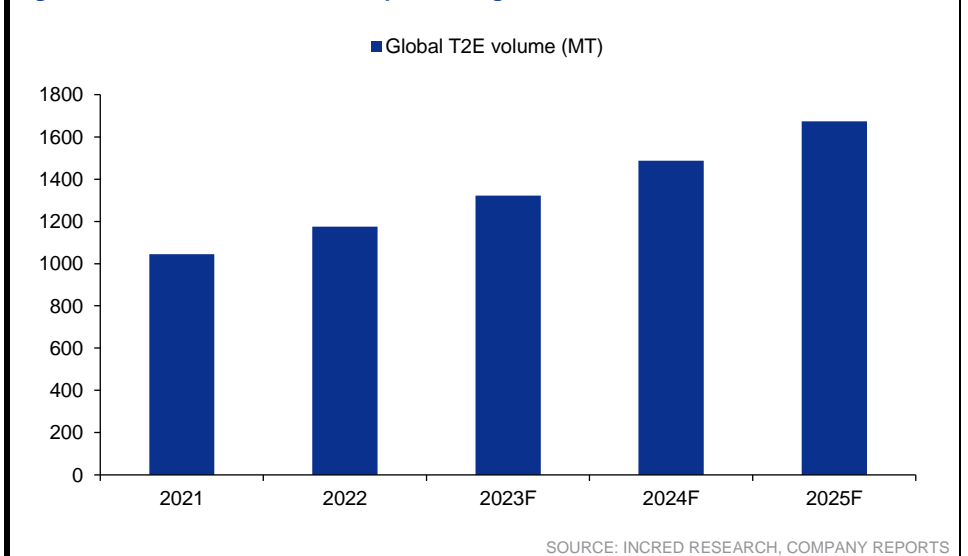
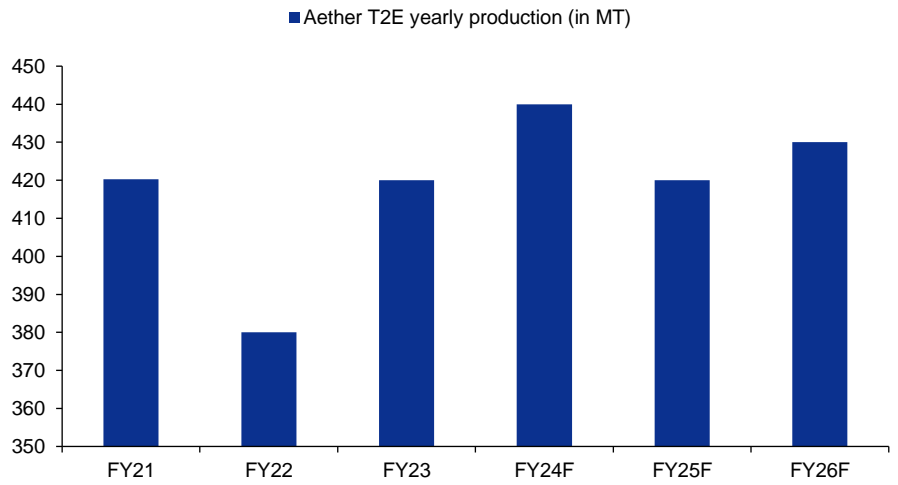
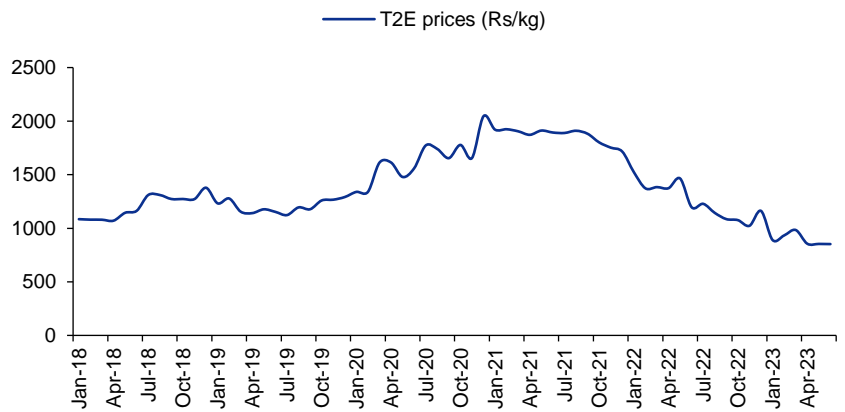


Figure 22: We expect Aether's T2E volume to decline in future, as it launches products with a higher realization coupled with the decline in prices of T2E



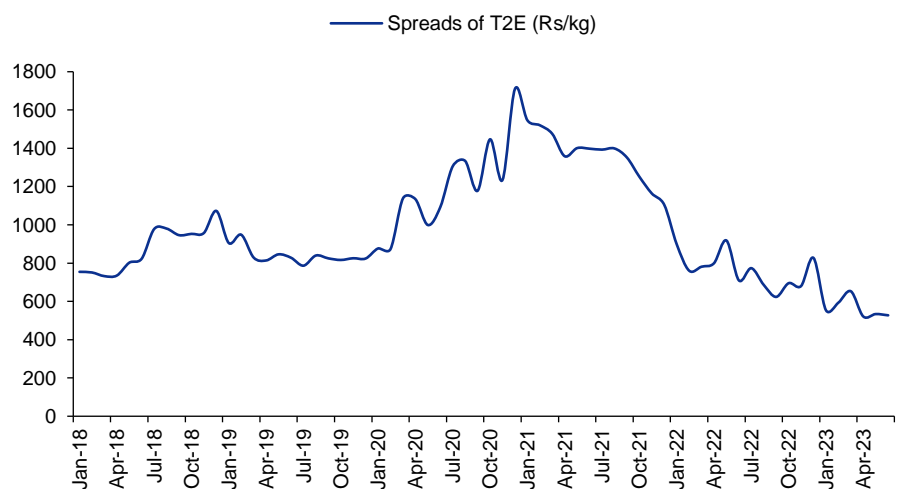
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 23: Global T2E prices decline to all-time lows



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 24: Consequently, spreads of T2E over its key raw material thiophene also decline



SOURCE: INCRED RESEARCH, COMPANY REPORTS

1-2-(2hydroxyethoxy) ethyl piperazine (HEEP) ►

1-[2-(2-hydroxyethoxy) ethyl] piperazine (HEEP) is used in chemical synthesis for manufacturing two APIs, namely quetiapine and hydroxyzine.

- **Quetiapine is a medicine used for the treatment of schizophrenia.** It may be used as part of a treatment program to treat bipolar disorder and schizophrenia in children and teenagers. Quetiapine is in a class of medications called atypical antipsychotics.
- Psychosis is a disorder where the person may face serious distortion of behaviour, thought, perception and recognition of reality. The patient may experience hallucinations and delusions along with having a wrong evaluation and misperception of other people, facts, or situations. Psychosis is not a condition but rather gets triggered due to other conditions such as stress, traumatic experiences, or physical conditions, namely brain tumor, Parkinson's disease or due to alcohol or drug misuse.
- **Hydroxyzine is used in adults and children to relieve itching caused by allergic skin reactions.** It is also used alone or with other medications in adults and children to relieve anxiety and tension. Hydroxyzine is also used along with other medications in adults and children as a sedative before and after general anesthesia for surgery. Hydroxyzine is in a class of medications called antihistamines. It works by blocking the action of histamine, a substance in the body that causes allergic symptoms. It also works by decreasing activity in the brain.
- **The global HEEP market is dominated by Indian companies with three major intermediate manufacturers operating in the market.** Aether is the largest manufacturer of HEEP in India and globally. Aether's production volume of HEEP grew at a CAGR of 50.6% from 76MT in calendar year 2018 to 200MT in calendar year 2020. Aether enjoys a 34% market share in the global HEEP market during the year.
- **However, quetiapine sales have been declining considerably due to availability of better anti-psychotic drugs.**

Figure 25: Aether is the market leader in global HEEP production

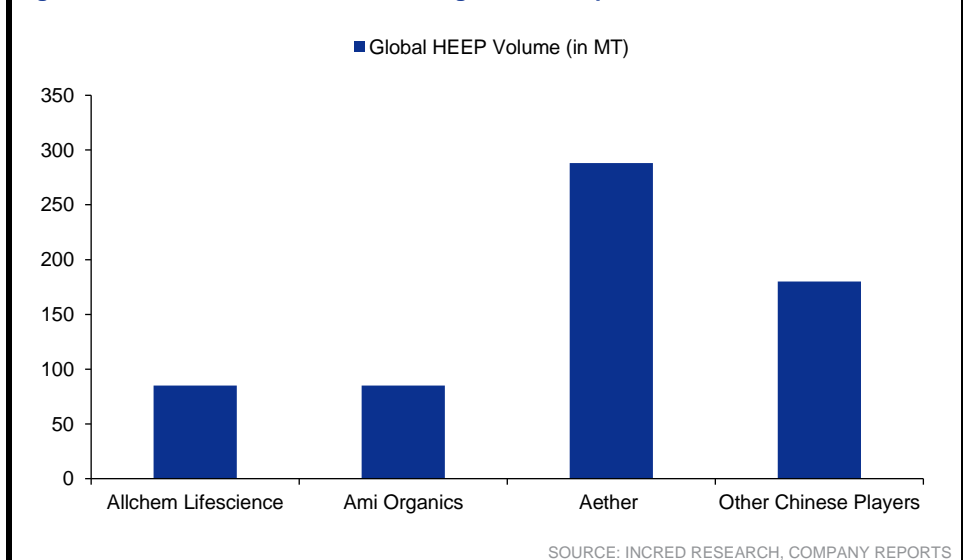


Figure 26: Quetiapine sales have been steadily declining in the US, indicating a bleak outlook

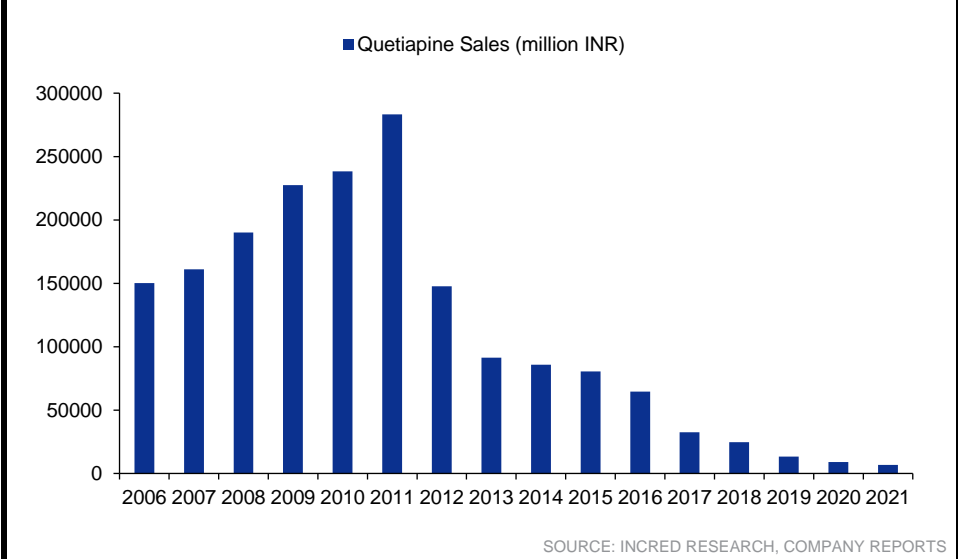
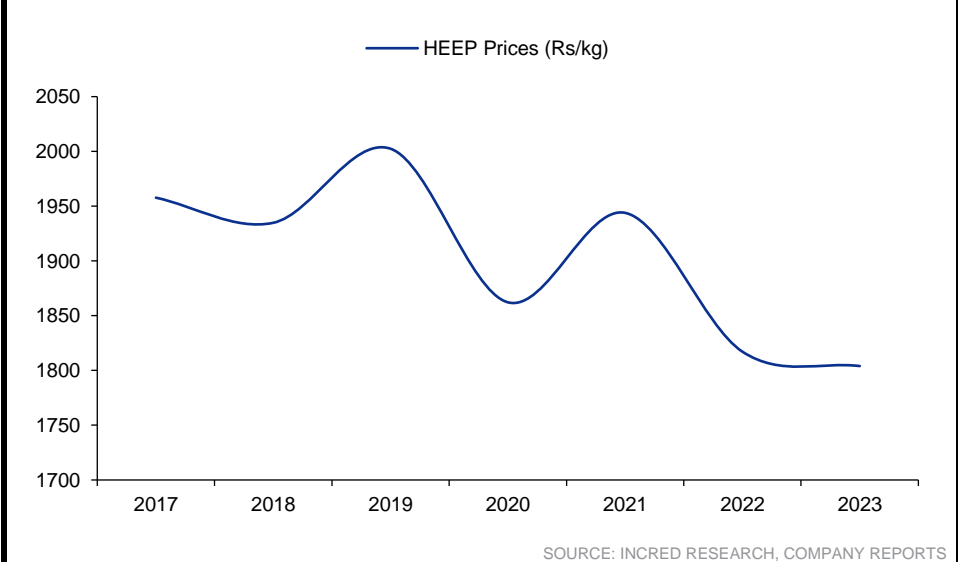


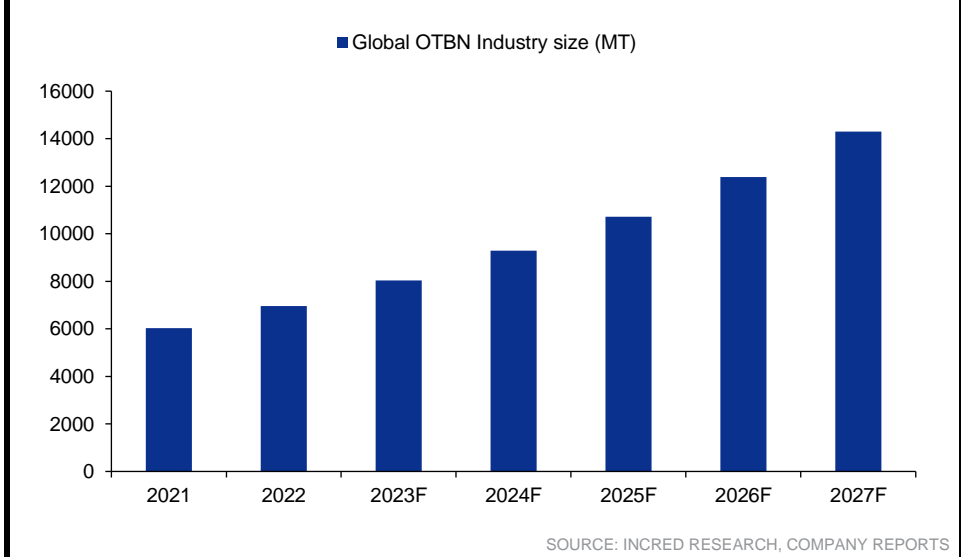
Figure 27: HEEP prices also decline considerably, which will affect Aether's margins in FY24F



Ortho tolyl benzo nitrile (OTBN) ➤

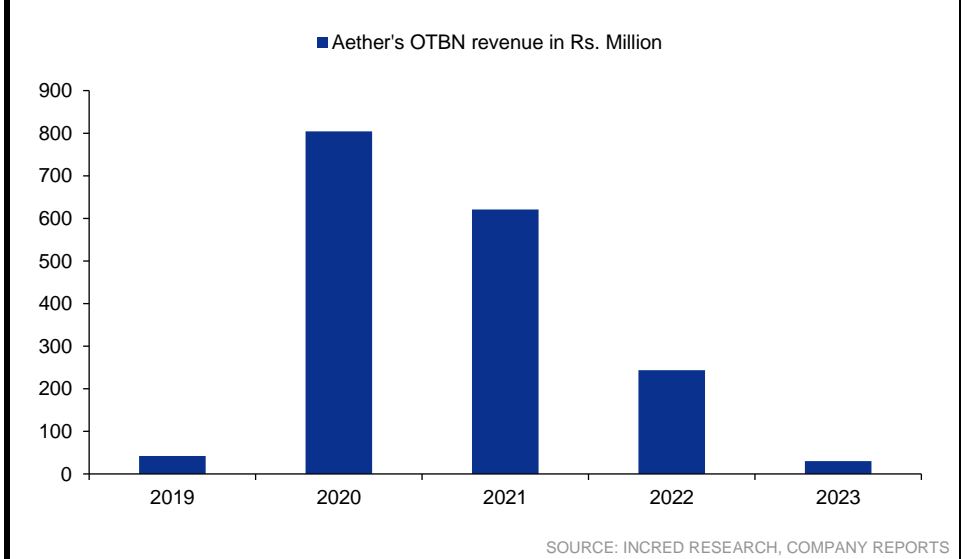
Ortho tolyl benzo nitrile/4-methyl-2-cyanobiphenyl (OTBN) is a key intermediate for manufacturing a variety of Sartan drugs as blood pressure lowering agents. Sartans are the latest generation of anti-hypertensive drugs, which have good anti-hypertensive effect and drug tolerance, less adverse reaction, and have protective effect on target organs. Sartans have less reaction on internal organs and therefore, their use is increasing consistently. Sartans can be divided into five categories: Valsartan, Irbesartan, Telmisartan, Losartan and Others.

Figure 28: OTBN market has been expanding rapidly and is expected to register a CAGR of 15.5% over 2021-27F

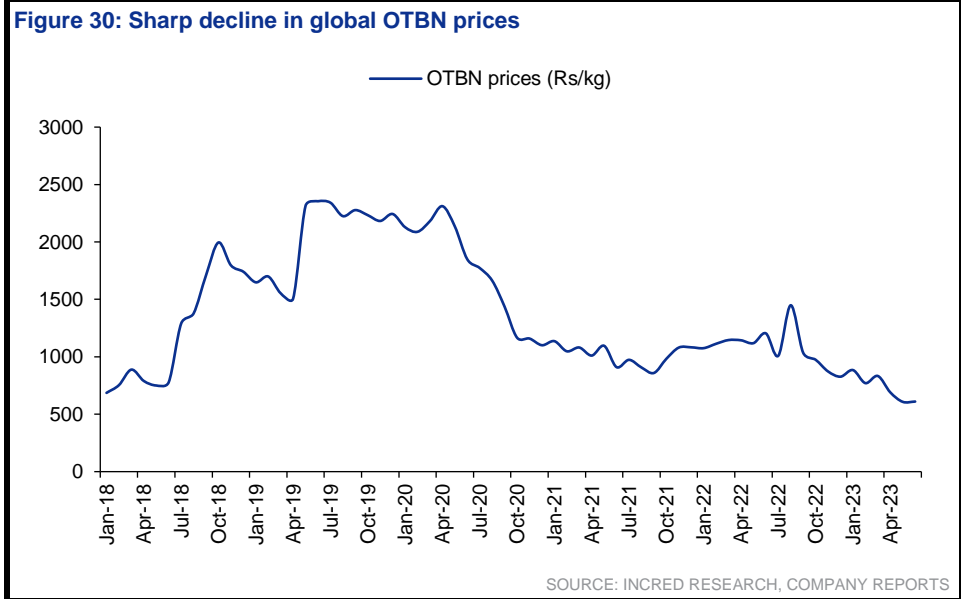


However, OTBN’s topline contribution to Aether has decreased considerably.

Figure 29: Sharp decrease in Aether’s OTBN revenue



This is mainly due to a significant decrease in global OTBN prices.



Aether’s new products in the pipeline ➤

Aether will start producing five intermediates for pharma APIs from FY24F at its new facility of 3,500MT capacity. It is expected to attain 60-65% capacity utilization by FY25F and will significantly contribute to Aether’s topline. These intermediates will mainly replace Chinese imports, as Indian API manufacturers are entirely dependent on China for these products.

Figure 31: List of new intermediates to be manufactured by Aether from FY24F

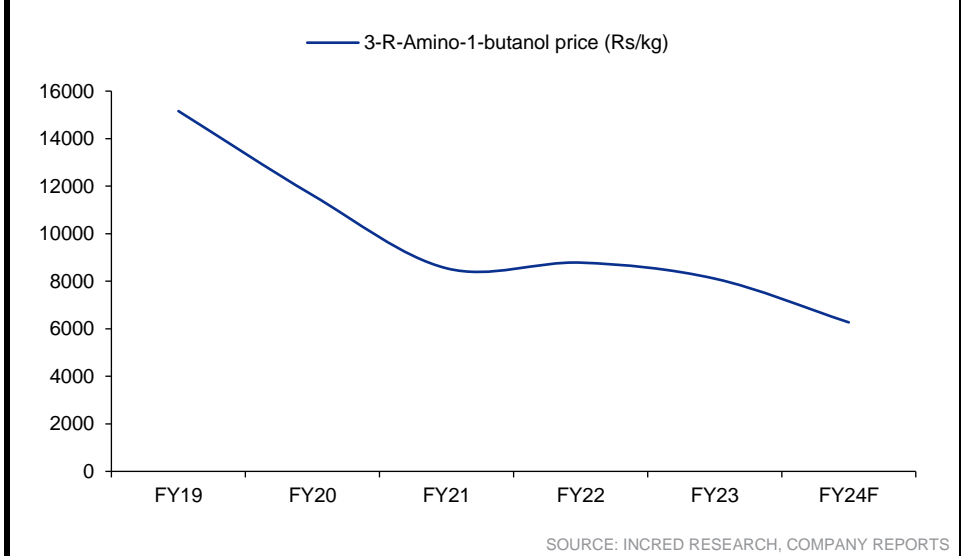
API	Intermediate	Import Volume (MT)	Realisation (Rs/kg)	Import Value (Rs. Million)
Dolutegravir	3-R-amino-1-butanol	200	6,271	1,254
Carbamazepine	IBCC	300	3,586	1,076
Oxcarbazepine	10-MISB	602	6,500	3,913
Ambroxol	TACH	127	3,213	408
Memantine	DMTA	15	7,965	119

SOURCE: INCRED RESEARCH, COMPANY REPORTS

3-R-amino-1-butanol ➤

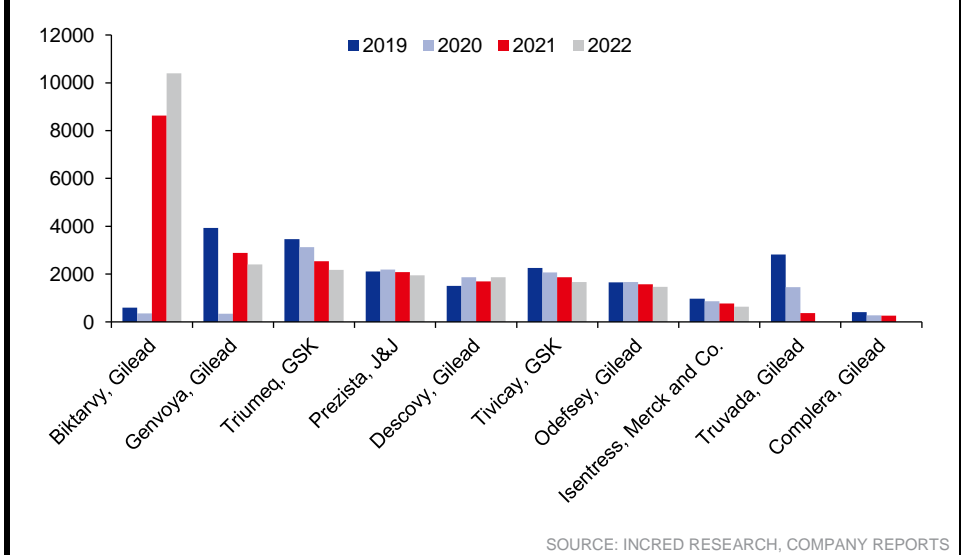
3-R-amino-1-butanol is an intermediate for dolutegravir API. Dolutegravir (DTG) is an API for antiretroviral medication used, together with other medications, to treat HIV/AIDS. It may also be used, as a part of post-exposure prophylaxis, to prevent HIV infection following potential exposure. It is an oral medication. Dolutegravir is mainly given as a triple-combination therapy in combination with tenofovir and lamivudine. As an antiretroviral or ARV drug, the major market for this drug is in LMIC (low middle-income countries), mainly Africa and the Southeast Asia region. Approximately 24–26m people in Africa are afflicted with AIDS, compared to 38–40m people worldwide. As a result, roughly 55–60% of those who are infected reside in Africa. Approximately 0.6kg of 3-R-amino-1-butanol is needed to manufacture 1kg of dolutegravir. 3-R-amino-1-butanol's global tonnage might be between 500MT and 550MT, compared to dolutegravir's global tonnage of roughly 800-900MT. Laurus Labs, Divi's Labs, Mylan Labs, and MacLeods Pharma are some of the prominent companies in India that use this intermediate.

Figure 32: 3-R-amino-1-butanol realization decreases from its FY19 high level

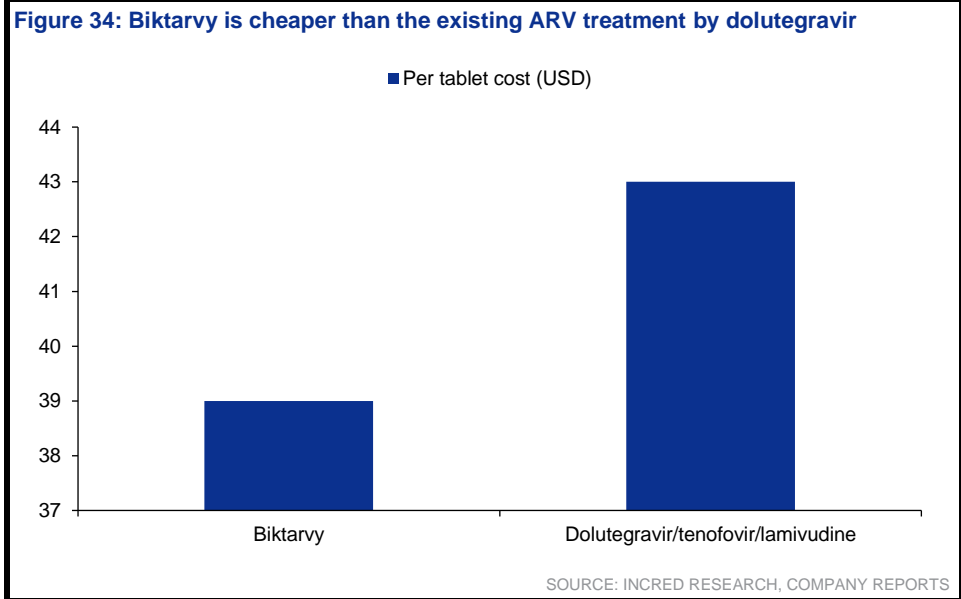


Realization of 3-R-amino-1-butanol has declined considerably. However, this decline is expected further, with the introduction of a new HIV drug by Gilead called biktarvy. Biktarvy is associated with faster cell count recovery and favourable virologic outcomes compared with other antiretroviral therapy (ART) among patients with advanced HIV infection, according to a recent study. Moreover, Gilead also conducted its BRAAVE trial, specifically on the black population, and found the biktarvy treatment to be quite effective (98% efficacy), even on those who were switching from dolutegravir treatment. No wonder this drug has garnered a 50% market share in the US within a short span.

Figure 33: Revenue of top-selling HIV AIDS drugs (in US\$m); as we can see, Biktarvy has outpaced them all in terms of sales

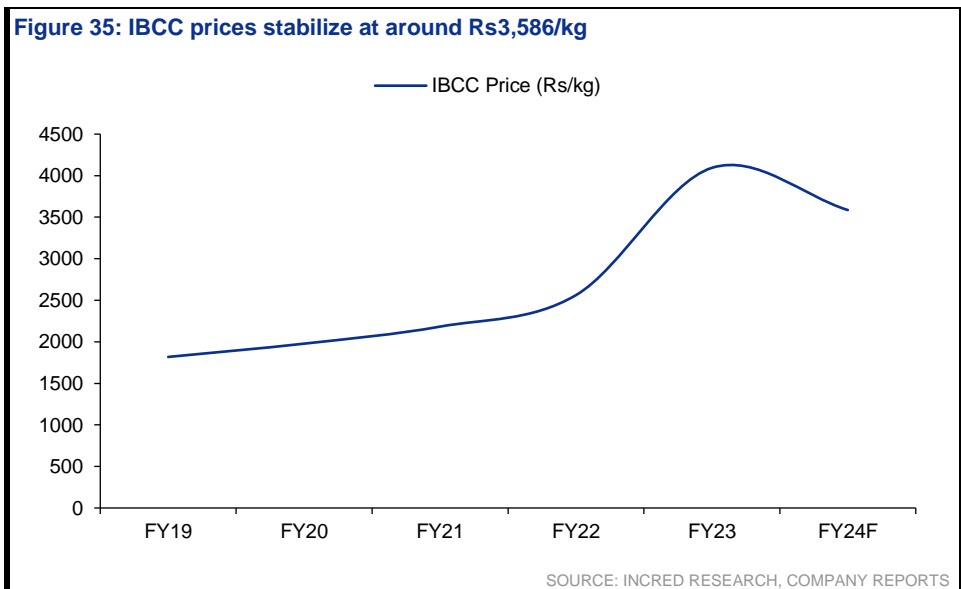


Biktarvy is also cheaper than dolutegravir, with less side effects. As a result, Americans are choosing biktarvy over dolutegravir.



Iminostilbene carbonyl chloride (IBCC) ➤

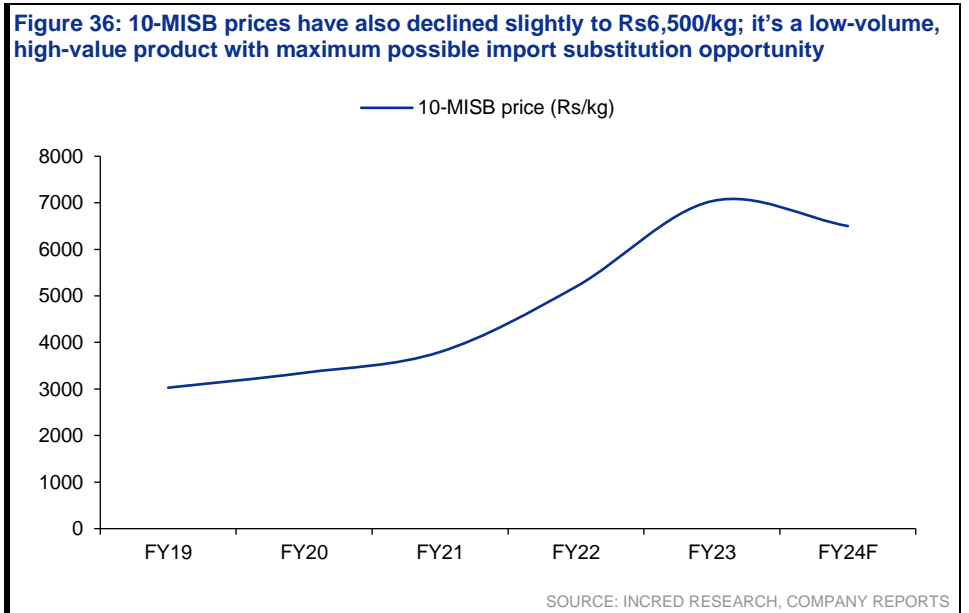
IBCC is an intermediate for the carbamazepine API. Carbamazepine is used to prevent and control seizures. This medication is known as an anti-convulsant or anti-epileptic drug. It works by reducing the spread of seizure activity in the brain and restoring the normal balance of nerve activity. The drug is sold under many brand names such as Pitol, Carbatrol, Tegretol, and Tegretol XR, among others. **According to Iqvia's projections, the global tonnage of carbamazepine in CY22 was between 950 and 1,000MT. 1.15kg of IBCC is used to produce 1kg of carbamazepine.** Among others, Sun Pharmaceutical Industries, Amoli Organics, and Bajaj Healthcare are some of the country's largest IBCC customers. India buys IBCC from China alone for about US\$15–16m per year (at a cost of about US\$45–50/kg or about 300MT).



10-methoxy iminostilbene (10-MISB) ➤

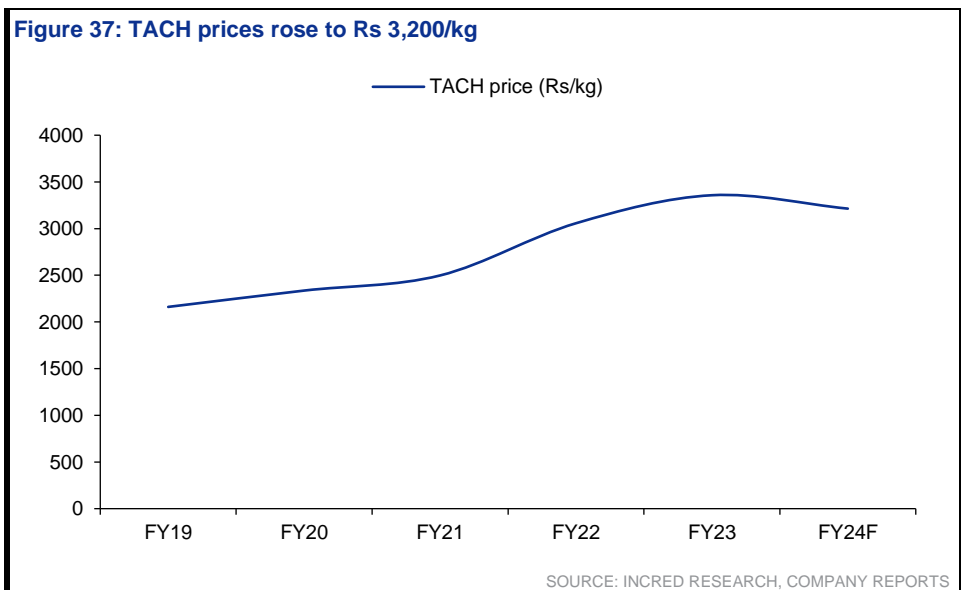
10-MISB is an intermediate for the oxcarbazepine API. Oxcarbazepine is an anti-convulsant. It works by decreasing nerve impulses that cause seizures and pain. This medication is known as an anti-convulsant or anti-epileptic drug. Epilepsy is a disorder of the central nervous system which causes abnormal brain activity, periods or seizures of unusual behaviour and loss of awareness at times. This drug API is either used alone or along with other drugs for treating partial seizure. **Oxcarbazepine API's global tonnage in CY22 was estimated by Iqvia to be between 480MT and 500MT. Approximately 1kg of 10-MISB is required to**

produce 1kg of oxcarbazepine. Prior to the Covid-19 pandemic, India imported all its 10-MISB requirement from China for about US\$25–30m per year (at a cost of about US\$45–50/kg). Among others, Sun Pharmaceutical Industries, Jubilant Generics, and Laurus Labs are some of the biggest 10-MISB buyers in India.



Trans-4-amino-cyclohexanol (TACH) ➤

TACH is an intermediate for ambroxol API. Ambroxol is a drug that breaks up phlegm and is used in the treatment of respiratory diseases associated with viscid or excessive mucus. 1kg of ambroxol is produced from 0.42kg of TACH. According to industry statistics, there is a 120–130mtpa global demand for ambroxol API. Anuh Pharma, Cadila Healthcare, Delta Finocem, and Ami Lifesciences, among others, are prominent users of TACH in India. **TACH imports in India during the past couple of years averaged between US\$2-3m per year, and they are all coming from China.**

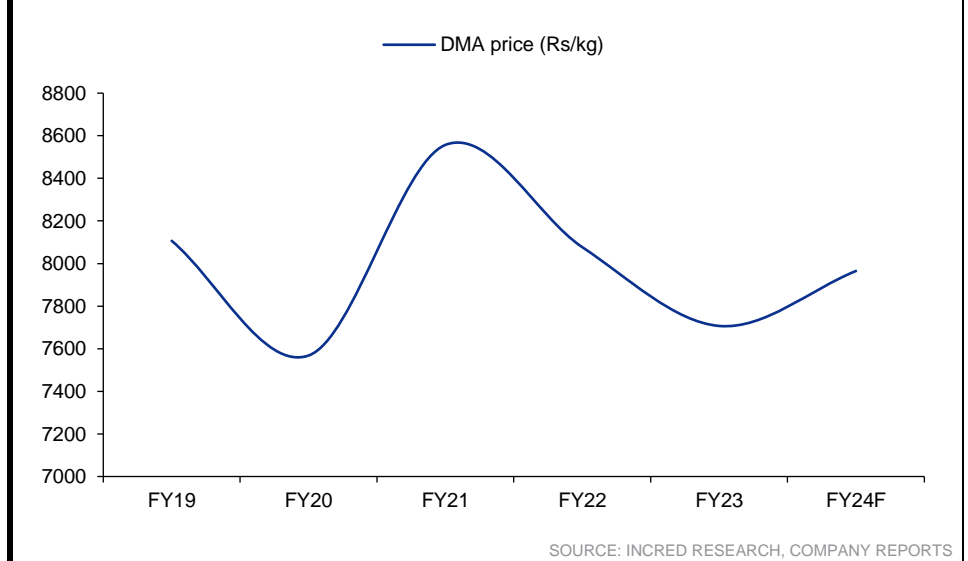


1,3-dimethyl adamantane (DMTA) ➤

1,3-dimethyl adamantane (DMTA) is an intermediate used in the production of memantine. Memantine is used in the treatment of Alzheimer's disease. **1kg of memantine API is produced from 1.33kg of 1,3-dimethyl adamantane (DMTA).** According to industry statistics, there may be 65–70MT of memantine API in the world. Dr Reddy's Laboratories, Mylan, Alembic, and Hetero Drug,

among others, frequently use DMTA in India. **India has imported DMTA worth between US\$1m and US\$2m annually, primarily from China.** Therefore, by generating DMTA, Aether may eliminate the need for imports of the memantine intermediate from China.

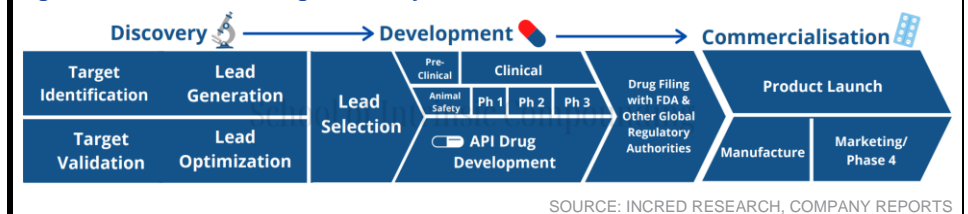
Figure 38: DMTA prices have stayed at around Rs7,965/kg



Contract research and manufacturing services (CRAMS) ➤

To get an understanding of the CRAMS business model, let’s start from the basics. In nature, there are various types of diseases caused by a variety of microbes. As a result, there’s a constant need for innovation by global innovators. These innovators are companies which sell patented drugs, not the generic versions, for example Pfizer, GSK, and Gilead, to name a few. So, these companies spend close to 20-22% of their sales on R&D. Below is a diagram describing the value chain of the drug manufacturing process.

Figure 39: Timeline of Drug Discovery Process



- Discovery phase:** Discovery phase covers the process from target identification to target validation to lead generation and lead optimization. The focus at this stage is to narrow down thousands of compounds to a few hundred, promising possibilities for further research and development. Typically, scientists begin with basic research on the physiological target and develop hypothetical mechanisms of action, which could potentially bring about the desired outcome. Following basic research, researchers look for a lead compound—a promising molecule that could influence the target in line with the projected hypotheses and potentially become a medicine. Researchers do this in various ways, including creating a molecule, using high-throughput screening techniques to select a few promising possibilities from among thousands of potential candidates, finding compounds from nature, and using biotechnology to genetically engineer living systems to produce disease-fighting molecules.
- Development:** After the new molecule (NME) discovery stage narrows down thousands of compounds to a few hundred promising possibilities, these molecules enter the development stage. The development stage spans pre-clinical and clinical testing, in addition to drug substance and drug product development.

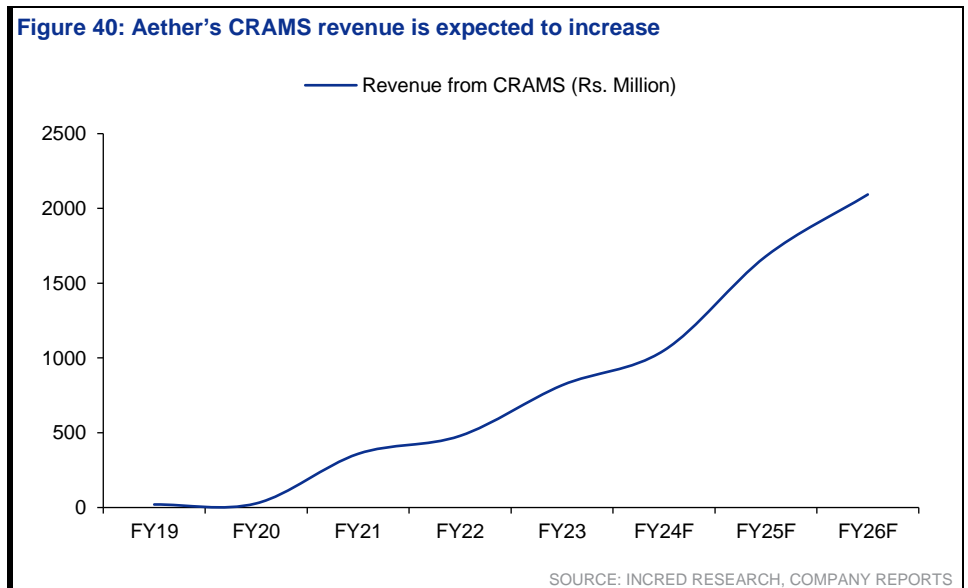
- Manufacturing:** NMEs can be used by millions of people or sometimes by a small, select population, and often are on the market for many years. Consequently, manufacturing facilities must be carefully designed so that the commercialized product can be consistently and efficiently produced at the highest level of quality.

The need for CRAMS industry ➤

CRAMS industry is essential because it is a way for global innovator giants to outsource their research and manufacturing to decrease their overall R&D cost. Outsourcing discovery and development work is an established alternative to in-house development among multinational organizations. While traditionally multinational organizations had looked at outsourcing to reduce their research and development (R&D) expenditure, the R&D outsourcing industry is evolving from a mere leveraging of cost arbitrage to enhancing R&D productivity and reducing the time-to-market.

Aether’s CRAMS division ➤

CRAMS division is important for Aether, as it enjoys a 70% EBITDA margin in this business. This is mainly because clients cover the raw material cost for CRAMS and hence, Aether’s margins are high. Currently, CRAMS contributes 13% to Aether’s topline, and this is expected to increase to 16% by FY26F. This division also works as a launch pad for the contract/exclusive manufacturing division.

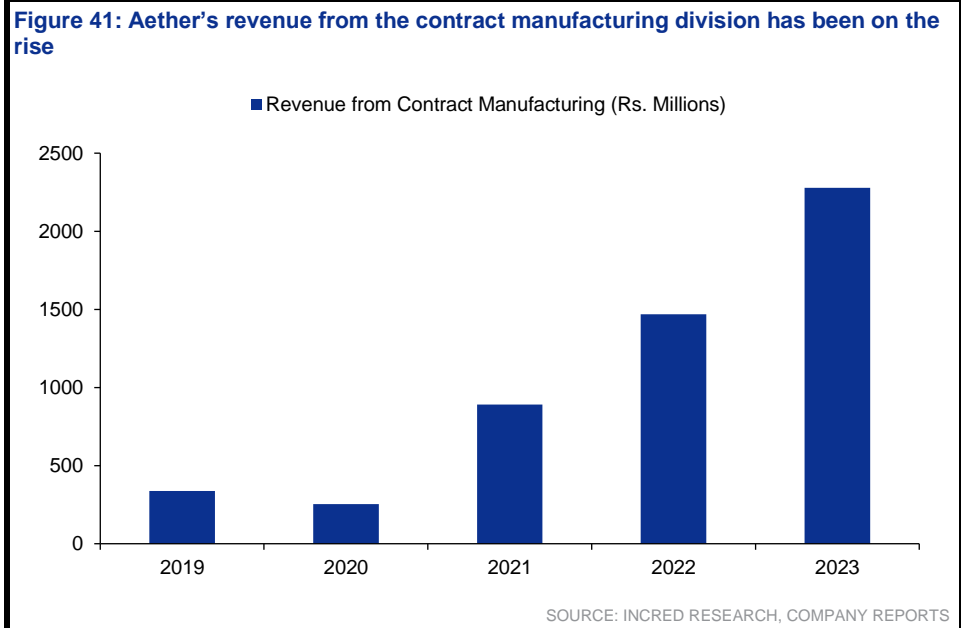


Polaroid’s deal with Aether ➤

Aether has signed a CRAMS deal with Polaroid for Polaroid films, which is expected to contribute about Rs1,200m in the next three years. This is expected to increase the current revenue of Rs817m by almost 50% to Rs.1,200m, which will be a significant contribution.

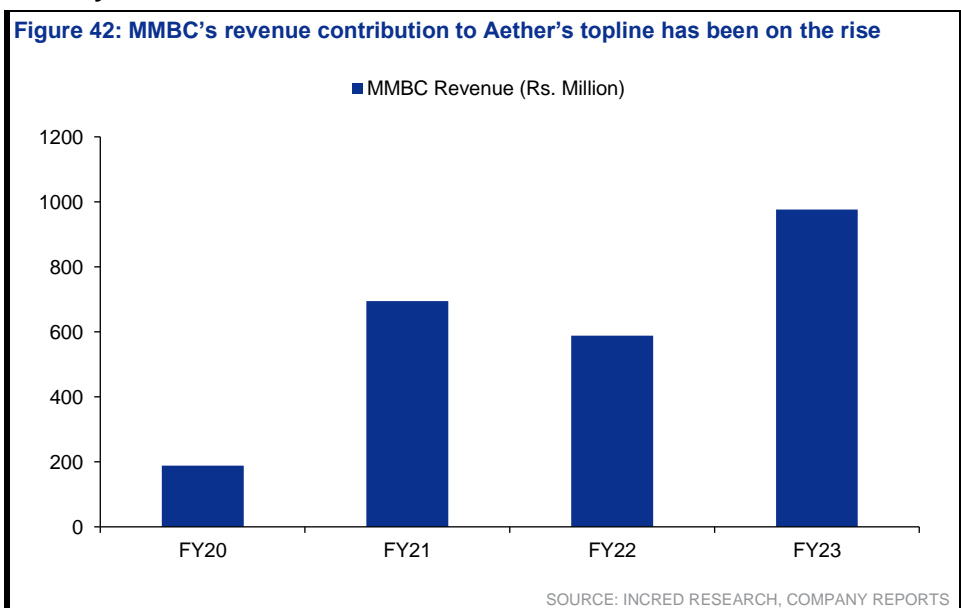
Contract/exclusive manufacturing ➤

Contract manufacturing works as an expansion of the CRAMS division. Aether takes on projects in the CRAMS division, but the volume is low. Once the company gains the trust of its clients, the project moves on from CRAMS to the high-volume contract manufacturing division, where the EBITDA margin is around 30-35%. Aether manufactures MMBC (intermediate for methoxyfenozide), and polyol (the Saudi Aramco deal) as a part of its contract manufacturing division’s business.



3-methoxy-2- methylbenzoyl chloride (MMBC) ➤

MMBC is an intermediate for the active ingredient (AI) methoxyfenozide, an insecticide manufactured by Corteva Agrisciences. Methoxyfenozide is a new specific benzoyl hydrazide insecticide for insect growth regulation. Methoxyfenozide belongs to the moulting accelerating compounds (MAC) class. MAC products are relatively slow in action, but they possess good residual activity and are active on specific pests such as beet armyworm. Methoxyfenozide is mainly used in vegetables and farmland to control lepidopteran pests on vegetables (melons and fruit), apple, corn, cotton, grapes, kiwi, walnut, flowers, beet, tea, and field crops (rice, sorghum, and soybean). **Nearly 500kg of MMBC is required for producing 1,000kg of methoxyfenozide.** The key global manufacturers of MMBC include WeylChem US, Aether, and Jiangsu Kefeite Biochemistry Technology. WeylChem US accounts for approximately 66% of the global market. **Aether is the second-largest manufacturer of MMBC in the world, with a 14% market share in terms of production volume, and it is also the only manufacturer of MMBC in India.**



Converge polyols ➤

Aether collaborated with Saudi Aramco to develop converge polyols. They jointly developed the manufacturing process and validated the production on a pre-commercial scale. **This novel technology allows the production of converge polyols with up to 40% weight of carbon dioxide.**

- Saudi Aramco acquired the converge product line and associated operations and technologies from the US-based Novomer Inc. in 2016. A proprietary catalyst is used for preparing converge polyols. The catalyst takes waste carbon dioxide as the primary feedstock. The catalyst combines it with propylene oxide to create polypropylene (propylene carbonate), a high-performance polyurethane building block.
- Converge polyols are unique and cost-effective. Convestro, formerly Bayer Material Science, is attempting to prepare polyether polycarbonate polyols that will use 20% waste carbon dioxide feedstock. This makes Saudi Aramco's product superior as it is using 40% weight of waste carbon dioxide, plus it gets the advantage of being first-to-market. Converge polyols are a competitive and sustainable alternative to conventional petrol-based polyols used in CASE industries (coatings, adhesives, sealants and elastomers). Compared to traditional polyols, they have a one-third carbon footprint. Making converge polyols is more cost-effective as waste carbon dioxide is cheaper than conventional petroleum-based raw materials. Moreover, the cost of manufacturing converge polyols is, on average, 30% less than the cost of manufacturing traditional polyols.
- Converge polyols are superior to existing products with a ready customer base. When these polyols are incorporated into polyurethane, the product has superior material performance in strength, abrasion, hardness, and tear strength, more significant load-bearing capacity, chemical and weather resistance, and reduced heat combustion. Due to these properties, converge polyols find usage in automotive and furniture industries. Overall, they are broad-spectrum products that can be used from automobile seats to building insulation parts. They have several applications, including flexible foam, rigid insulation foam for construction, industrial use, appliance coating, adhesives, sealants, and elastomers, which signifies a broad customer base ready for the product.
- **Aether and converge polyol - a significant advantage to the company.** The CASE polyol industry has a market size of more than 1,000ktpa. Saudi Aramco targets a market of 850ktpa and a CAGR of 5%. **Aether will manufacture 2,000MT of the product, in volume terms, for Saudi Aramco, at a price close to Rs400/kg.** The company could end up supplying up to 30,000MT in the long term. It will supply globally to different Aramco locations. Aether can generate Rs1.5bn-2.0bn of revenue in FY26F via this collaboration. Another advantage is that this establishes Aether's relationship with Saudi Aramco, which has a specialty and intermediate chemical portfolio, paving the way for future collaborations.

Financial valuation

Robust fundamentals with a strong R&D presence ➤

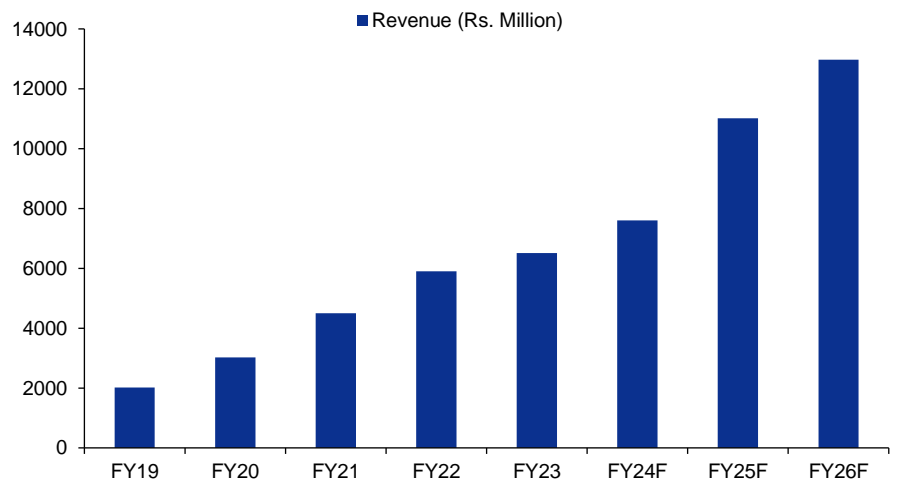
The EPS growth rate of Aether for the next three years is good, in our view, at a 22% CAGR (FY23-26F). At the same time, we believe the company's RoE will increase from 8% in FY23F to 10% in FY25F. Although Aether's portfolio will face some headwinds in FY24F due to falling intermediate prices, its well diversified portfolio, coupled with a best-in-house research team, will help it sail through. Aether's foray into five new pharma intermediates will start contributing to the topline by FY26F, which will further boost the EPS.

Figure 43: Aether's IPO funds utilization

Fresh Issue (in Rs mn)	Offer for Sale (in Rs mn)
6,270	1,720
Funds Utilisation (in million Rs)	
CapEx Funding	1,630
Repayment of Debt	1,379
Working Capital Requirements	1,650
Remaining Balance	3,331

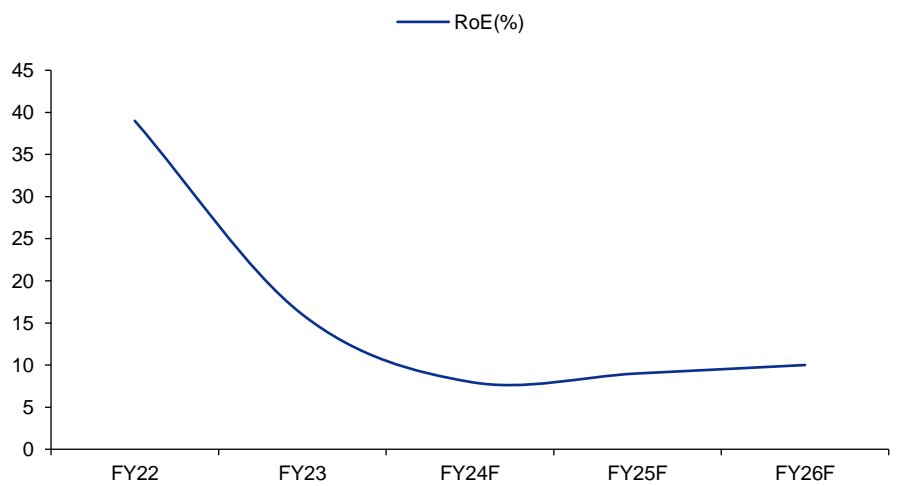
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 44: Aether's topline is expected to grow at a CAGR of 25% over FY23-26F



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 45: RoE to show a bit of decline, as the company has recently done a QIP



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 46: The EBITDA margin to improve as the proportion of CRAMS in the overall business increases

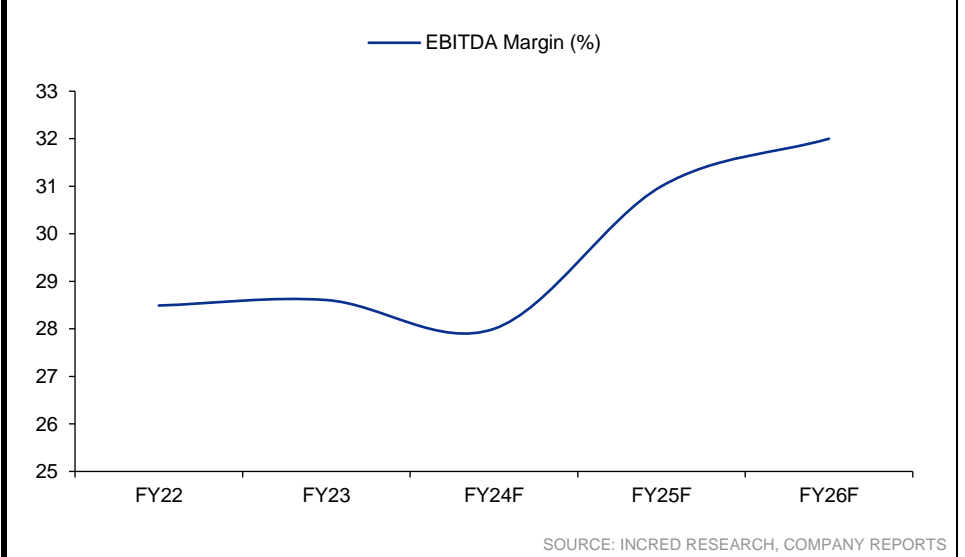


Figure 47: The EBITDA margin improvement to be aided by a favourable revenue mix

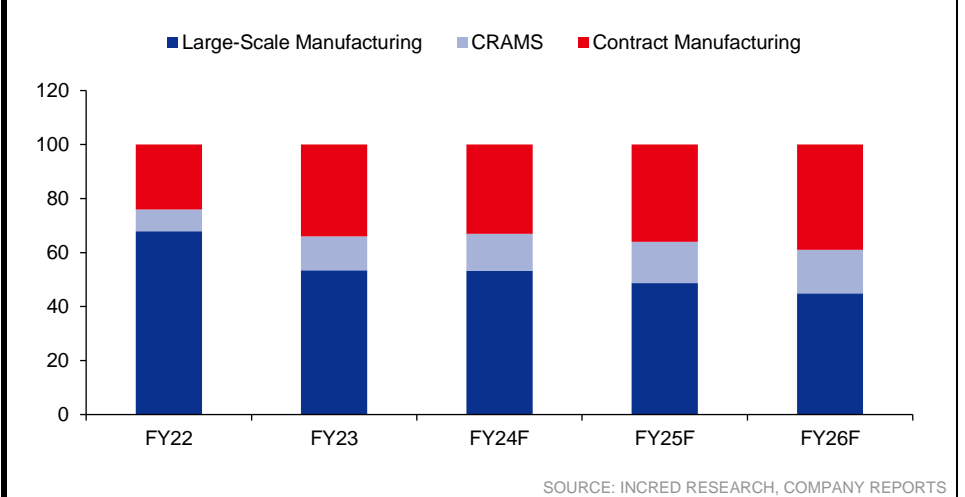


Figure 48: Aether has been investing aggressively in R&D

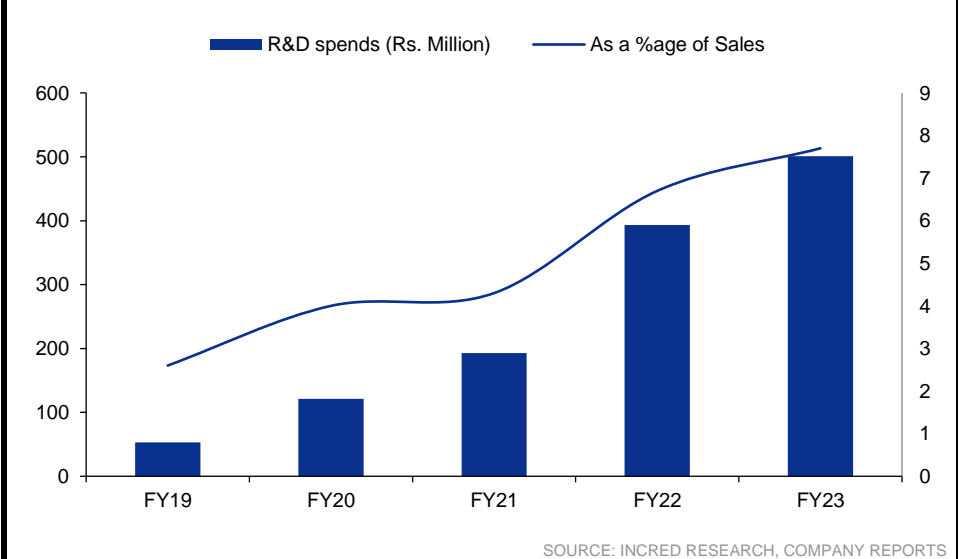


Figure 49: Aether's net block is expected to double from its FY23 level

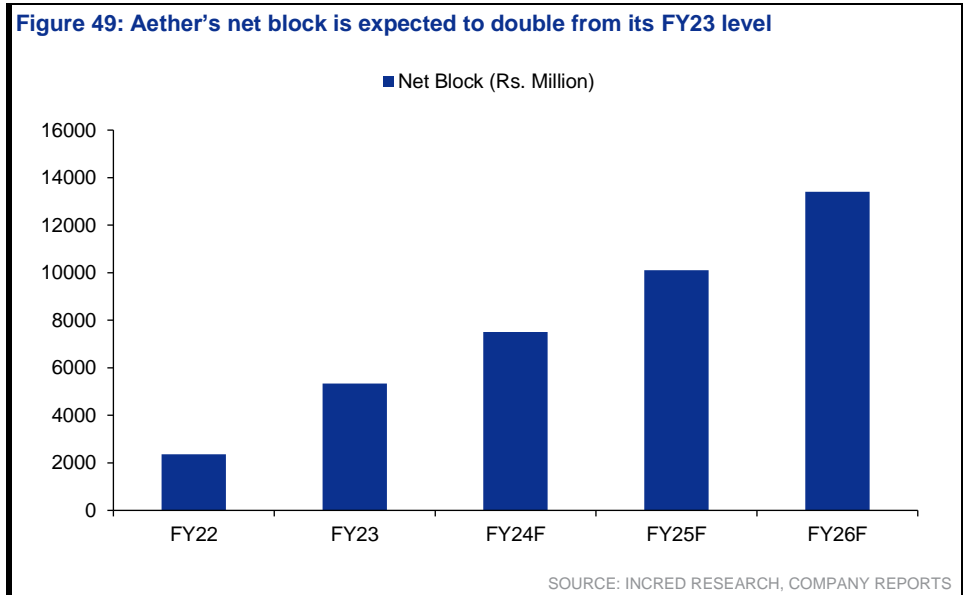


Figure 50: Asset turns will take a hit in the near term due to a significant amount of capex

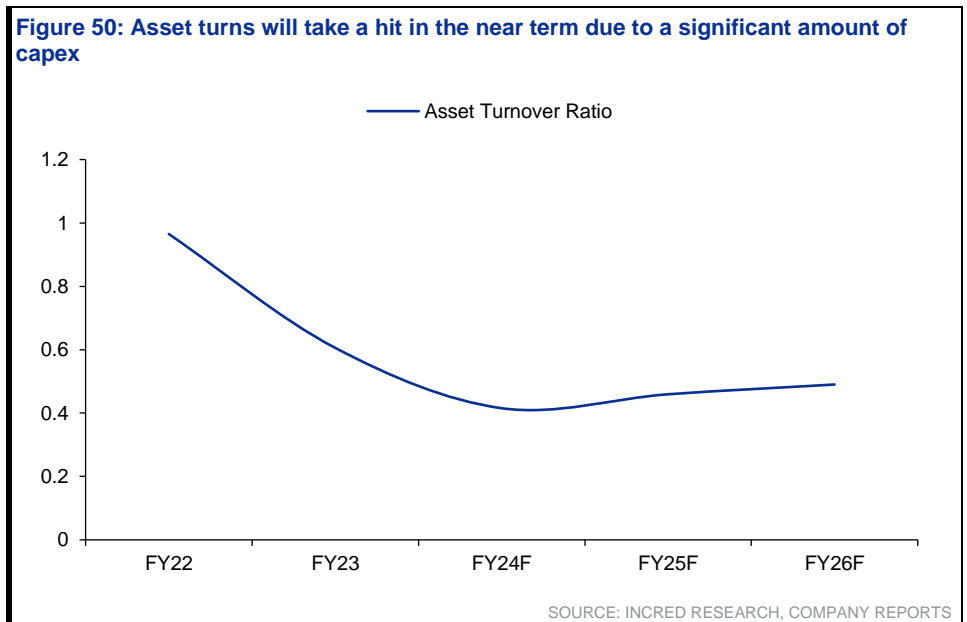


Figure 51: Aether's CAGR comparison with peers; as we can see, Aether is in the high-growth phase (source: Aether DRHP)

Particulars	Vinati Organics	Clean Science and Tech	PI Industries	Navin Fluorine	Fine Organics	Aether Industries
Operating EBITDA	-8.75%	37.83%	32.52%	19.01%	-7.64%	53.65%
RoE	-19.41%	1.20%	-12.25%	6.47%	-22.68%	-17.91%
RoCE	-25.85%	12.00%	5.29%	8.31%	-17.66%	6.44%
RoA	-18.60%	2.44%	-3.73%	12.04%	-22.22%	21.49%
Operating Expenses	-7.58%	-0.68%	25.47%	5.78%	6.29%	48.23%
PAT	-2.36%	42.53%	34.16%	31.42%	-6.02%	74.58%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

We have used EV/EBITDA to value chemical companies ➤

We have valued Aether on an EV/EBITDA basis as we consider it a more appropriate valuation method for chemical companies than the discounted cash flow or DCF or P/E methodologies. In our view, DCF is not a suitable valuation method because the earnings of chemical companies are highly cyclical and forecasting long-term earnings reliably is very difficult. We believe a P/E based forecast is inappropriate as the company is incurring a significant amount of capex, thus suppressing its profit after tax.

Figure 52: Target price valuation

FY24F EBITDA	2,127
FY25F EBITDA	3,414
FY26F EBITDA	4,152
Two-year forward EV/EBITDA (x)	40x
Target Price (Rs)	1,124

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 53: Aether's valuation comparison with its peers; as we can see, Aether gets a premium from its markets due to its process chemistry expertise & a low base

	EV/EBITDA(TTM)
Vinati Organics	27.85
Clean Science and Technology	31.6
PI Industries	30.6
Navin Fluorine	38.3
Fine Organics	16.2
Aether Industries	62.8

SOURCE: INCRED RESEARCH, COMPANY REPORTS

We have valued Aether at 40x EV/EBITDA as:

- Aether, which has a solid R&D foundation, has concentrated on mastering multiple chemistries and value chains. Because of this, it is now able to pursue two goals at once: replacing imports with domestic production while also partnering with significant international companies. Additionally, by creating converge polyol technology, it has demonstrated its global footprint. It can swap or create new goods extremely quickly because the method is driven by chemistry rather than by the product or the source material.
- Aether offers a variety of chemistries, including cross coupling, organometallic, organolithium, and Grignard. It is challenging to optimize several elements of the Grignard reaction, according to multiple research white papers. Additionally, cross coupling reactions are also the subject of ongoing research. In our opinion, Aether's inclusion in these chemistries shows that it can manage complex chemistries, and this serves as a significant barrier to entry for other companies.

Downside risks >

- The major downside risk associated with Aether is a further decrease in the prices of key intermediates, which will affect its large-scale manufacturing division. As Aether trades at a significantly high valuation currently, a lot of growth is already discounted, and any deviation from that trajectory could affect the stock price.
- Changes in major raw material prices could hurt realization. As 70% of the company's raw materials are crude oil-based derivatives, the inability to pass on price hikes to end-customers may have a substantial impact on the company's per-unit realization and, consequently, on operations and profitability.

Upside risks >

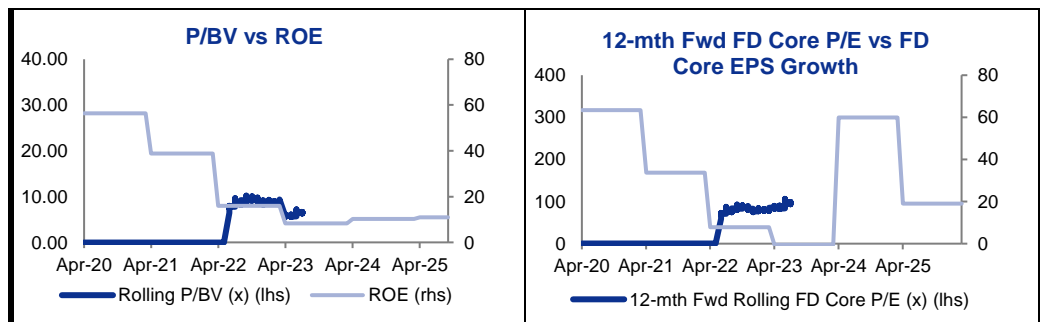
- If Aether wins any large-value order in the CRAMS division, it could be a major upside as the company enjoys a 70% EBITDA margin in the CRAMS business. The ramp-up of its converge polyol capabilities could also be an upside risk.

Key management personnel >

- **Ashwin Desai** is the promoter and managing director of the company. He graduated from the Institute of Chemical Technology (ICT, formerly University Department of Chemical Technology, UDCT) with a bachelor's degree in chemical engineering. Indian Chemical Technology presented him with the Distinguished Alumnus award in 2010. He was a founding member of Anupam Rasayan India prior to Aether's establishment and served as its chairman and managing director till 2013.

- **Aman Desai** is the promoter and whole-time director on the board of the company. He graduated from the Institute of Chemical Technology with a Bachelor of Science degree in Chemical Technology (Intermediates and Dyestuff Technology; ICT, formerly known as University Department of Chemical Technology, UDCT), and Michigan State University awarded him a Doctor of Philosophy (PhD) in Organic Chemistry with a focus on chiral chemistry. In 2010, Chemical & Engineering News as well as the Journal of the American Chemical Society both published his PhD study. He has 25 articles in international technical journals as the author or co-author. He has received four US patents, which are all published internationally.
- **Rohan Desai** is the promoter and whole-time director on the board of the company. He has a bachelor's degree from South Gujarat University of Commerce (SPB VNSG), Surat. Mr. Desai was previously a director at Anupam Rasayan India until 2013.
- **Purnima Desai** is the promoter and whole-time director on the board of the company. She has a bachelor's degree from the University of Delhi (1975). She was previously a director at Anupam Rasayan India until 2013.

BY THE NUMBERS



Profit & Loss

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Net Revenues	5,900	6,511	7,596	11,014	12,974
Gross Profit	3,020	3,337	3,874	5,948	7,136
Operating EBITDA	1,681	1,862	2,127	3,414	4,152
Depreciation And Amortisation	(155)	(232)	(450)	(606)	(804)
Operating EBIT	1,526	1,630	1,677	2,808	3,347
Financial Income/(Expense)	(131)	(51)	(4)	(4)	(4)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	70	166	228	330	389
Profit Before Tax (pre-EI)	1,465	1,745	1,901	3,135	3,733
Exceptional Items					
Pre-tax Profit	1,465	1,745	1,901	3,135	3,733
Taxation	(375)	(441)	(494)	(815)	(970)
Exceptional Income - post-tax					
Profit After Tax	1,089	1,304	1,407	2,320	2,762
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	1,089	1,304	1,407	2,320	2,762
Recurring Net Profit	1,089	1,304	1,407	2,320	2,762
Fully Diluted Recurring Net Profit	1,089	1,304	1,407	2,320	2,762

Cash Flow

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
EBITDA	1,681	1,862	2,127	3,414	4,152
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(1,452)	(1,696)	623	(1,006)	(597)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	186	138	236	338	397
Net Interest (Paid)/Received	(131)	(51)	(4)	(4)	(4)
Tax Paid	(338)	(318)	(356)	(587)	(699)
Cashflow From Operations	(54)	(66)	2,626	2,156	3,249
Capex	(1,517)	(3,567)	(2,166)	(2,600)	(3,305)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	8	83	83	83	83
Cash Flow From Investing	(1,509)	(3,484)	(2,084)	(2,517)	(3,222)
Debt Raised/(repaid)	268	(1,510)			
Proceeds From Issue Of Shares	1,032	7,259	7,579	9	9
Shares Repurchased					
Dividends Paid					
Preferred Dividends					
Other Financing Cashflow	389	(1,357)	4	4	4
Cash Flow From Financing	1,688	4,392	7,583	13	13
Total Cash Generated	125	843	8,126	(348)	40
Free Cashflow To Equity	(1,296)	(5,060)	543	(361)	27
Free Cashflow To Firm	(1,433)	(3,498)	547	(357)	31

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Cash And Equivalents	180	1,023	8,665	7,573	6,553
Total Debtors	1,635	2,590	2,659	3,855	4,541
Inventories	1,627	2,488	2,047	2,027	2,043
Total Other Current Assets	656	651	366	478	535
Total Current Assets	4,098	6,752	13,737	13,933	13,672
Fixed Assets	2,933	5,705	7,700	10,250	13,505
Total Investments	2	2	2	2	2
Intangible Assets	216	1,128	1,129	1,129	1,129
Total Other Non-Current Assets	450	212	212	212	212
Total Non-current Assets	3,600	7,047	9,042	11,592	14,847
Short-term Debt	1,633	1	1	1	1
Current Portion of Long-Term Debt					
Total Creditors	699	815	782	1,064	1,226
Other Current Liabilities	85	113	113	113	113
Total Current Liabilities	2,416	929	896	1,178	1,340
Total Long-term Debt	1,218				
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	57	156	156	156	156
Total Non-current Liabilities	1,275	156	156	156	156
Total Provisions	139	268	222	367	437
Total Liabilities	3,829	1,353	1,274	1,701	1,933
Shareholders Equity	3,869	12,446	21,505	23,824	26,587
Minority Interests					
Total Equity	3,869	12,446	21,505	23,824	26,587

Key Ratios					
	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue Growth	31.2%	10.3%	16.7%	45.0%	17.8%
Operating EBITDA Growth	49.9%	10.8%	14.2%	60.5%	21.6%
Operating EBITDA Margin	28.5%	28.6%	28.0%	31.0%	32.0%
Net Cash Per Share (Rs)	(23.70)	8.21	65.29	57.06	49.38
BVPS (Rs)	34.33	99.96	162.05	179.54	200.35
Gross Interest Cover	11.63	32.01	419.25	702.12	836.83
Effective Tax Rate	25.6%	25.3%	26.0%	26.0%	26.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	84.04	118.42	126.09	107.93	118.10
Inventory Days	156.80	236.66	222.34	146.74	127.23
Accounts Payables Days	74.53	87.05	78.29	66.48	71.59
ROIC (%)	29.1%	18.1%	10.5%	15.7%	14.8%
ROCE (%)	28.3%	16.7%	9.7%	12.2%	13.1%
Return On Average Assets	19.4%	12.5%	7.7%	9.6%	10.2%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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