

Initiating Coverage Balaji Amines Ltd.

17-November-2020



| Industry | LTP | Recommendation | Base Case Fair Value | Bull Case Fair Value | Time Horizon |
|---------------------|-----------|--|----------------------|----------------------|--------------|
| Specialty Chemicals | Rs. 949.6 | Buy on dips to Rs 904-908 band and add more on dips to Rs.840-844 band | Rs. 1000 | Rs.1077 | 2 quarters |

| | |
|-----------------------|---------------|
| HDFC Scrip Code | Balaji Amines |
| BSE Code | 530999 |
| NSE Code | BALAMINES |
| Bloomberg | BLA:IN |
| CMP Nov 14, 2020 | 949.6 |
| Equity Capital (Rscr) | 6 |
| Face Value (Re) | 2 |
| Equity Share O/S (cr) | 1.2 |
| Market Cap (Rscrs) | 3077 |
| Book Value (Rs) | 227 |
| Avg. 52 Wk Volumes | 205,000 |
| 52 Week High | 995 |
| 52 Week Low | 200 |

| Share holding Pattern % (June, 2020) | |
|--------------------------------------|-------|
| Promoters | 53.7 |
| Institutions | 2 |
| Non Institutions | 44.3 |
| Total | 100.0 |

Fundamental Research Analyst

Nirav Savai

nirav.savai@hdfcsec.com

Our Take:

Balaji Amines Ltd. (BAL) is India's largest aliphatic amine company with ~50% market share. It has been one of the consistent compounders over last decade where it's Revenues, EBITDA & PAT registered a growth of CAGR 13%, 15% and 17% respectively. It has successfully created a niche for itself in a highly capital intensive, oligopolistic industry with huge entry barriers by constant focus on import substitution and calibrated approach towards capacity expansion. More than 80% of the products produced by the company were previously imported in India while currently ~60% of its product portfolio comprises of products which are only manufactured by Balaji Amines in India which includes NMP, NEP, 2P (N Methyl/Ethyl/2 Pyrrolidone); GBL (Gamma Butyrolactone); Morpholine; DEAE (Di-Ethyl Amino Ethanol); DMAE (Di-Methyl Amino Ethanol); DMU (Di-Methyl Urea); DMF (Dimethyl Formamide) and PVPK-30 (Pharmapure Povidone). Going forward, we expect strong tailwinds to continue on the demand side mainly in products sold to Pharma and Agrochem industry (77% of revenue). Also its higher focus on launching new import substitute products in India and incremental capacity addition in Ethylamines (16,500 MT), Methylamines (50,000 MT) Di-methyl Carbonate (DMC) and Acetonitrile (9000 MT) provides good visibility of growth.

Valuations & Recommendation:

We are positive on the future earnings growth trajectory of Balaji Amines. We expect its earnings growth momentum to sustain which is likely to be mainly driven by richer product mix, gradual improvement in utilization of its new capacities and sustainable demand for amines from its end-user industries like pharma and agrochem. In our view, Balaji Amines' Revenue and PAT is likely to record a growth of 13% and 32% CAGR over FY20-22E along with consistent FCF generation, debt free status & superior ROIC (25%+).

The stock is currently trading at valuation of 18.1x FY22E earnings. We feel the base case fair value of the stock is Rs 1000 (19x FY22E) and bull case fair value is Rs 1077 (20.5x FY22E). Investors can buy the stock on dips to Rs.904-908 band (17.25x FY22E EPS) and add more on dips to Rs.840-844 band (16.0x FY22E EPS).

Financial Summary

| Particulars (Rs Mn) | Q2FY21 | Q2FY20 | YoY-% | Q1FY20 | QoQ-% | FY19 | FY20 | FY21E | FY22E |
|------------------------|--------|--------|-------|--------|-------|-------|-------|--------|--------|
| Total Operating Income | 2809 | 2304 | 22 | 2105 | 33 | 9431 | 9,358 | 10,003 | 12,053 |
| EBITDA | 698 | 457 | 53 | 511 | 37 | 1807 | 2,308 | 2,792 | 0 |
| Depreciation | 66 | 58 | 14 | 56 | 18 | 196 | 316 | 325 | 361 |
| Other Income | 24 | 29 | -16 | 25 | -1 | 42 | 50 | 34 | 36 |
| Interest Cost | 15 | 38 | -59 | 13 | 17 | 130 | 230 | 178 | 191 |
| Tax | 164 | 43 | 283 | 119 | 38 | 480 | 336 | 463 | 574 |
| APAT | 476.6 | 347.1 | 37.3 | 346.5 | 37.5 | 1,171 | 975 | 1,376 | 1,702 |
| Diluted EPS (Rs) | 14.7 | 10.7 | 37.3 | 10.7 | 37.5 | 36.1 | 30.1 | 42.5 | 52.5 |
| RoE | | | | | | 20% | 15% | 17% | 18% |
| P/E (x) | | | | | | 26.3 | 31.6 | 22.4 | 18.1 |
| EV/EBITDA | | | | | | 16.9 | 18.0 | 14.1 | 11.7 |

(Source: Company, HDFC sec)

Q2FY21 Result Review

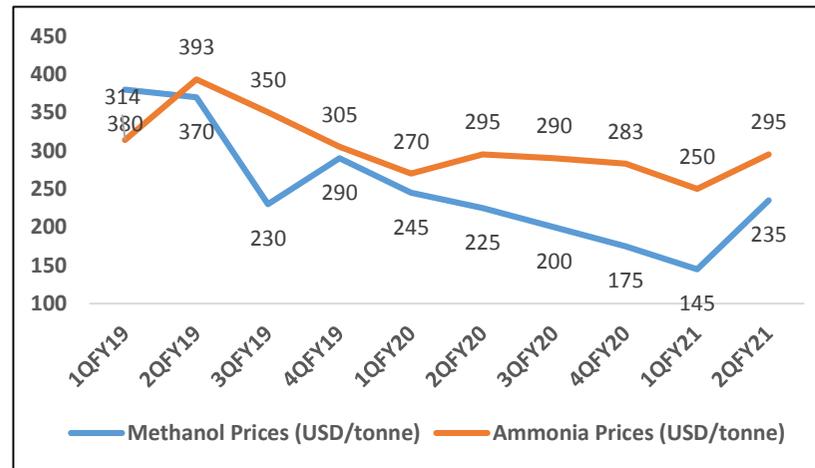
- In the midst of Covid-19 pandemic, BAL has been consistently reporting strong performance. In Q2FY21 overall revenues stood at Rs. 280.8 cr which grew by 22% YoY and 33% on sequential basis. Total volume for the quarter stood at 23.15k MT up 8% YoY while realization grew by 13% YoY to Rs. 121/Kg. Segment-wise volumes of Amines/ Derivatives and Specialty Chemicals share for the quarter stood at 22%/ 43% and 35% respectively.
- Gross and EBITDA margins stood at Rs 58/Kg (up 21% YoY) and Rs 30/ Kg (up 41% YoY). Gross margin stood at 47.5%, +314/58bps YoY/QoQ. EBITDA margin jumped by 503/60bps YoY/QoQ to 24.9%. Consequently, PAT stood at Rs 47.6 cr v/s Rs 34.7 cr in Q2FY20. On a YoY basis PAT grew by 37%.
- As per the management, post de-bottlenecking of Acetonitrile, BAL's capacity will double from 9tpd to 18 from Nov '20. Green field expansion for Ethyamines is on track and will be commissioned by Q4FY21. Apart from this, BAL management has also announced its greenfield project Phase II plans which is a capex outlay of Rs. 2Bn. It plans to set-up a separate plant for Methylamines/DMF with a capacity of 40-50kTPA/30kTPA under Greenfield phase-II project.

Recent Triggers

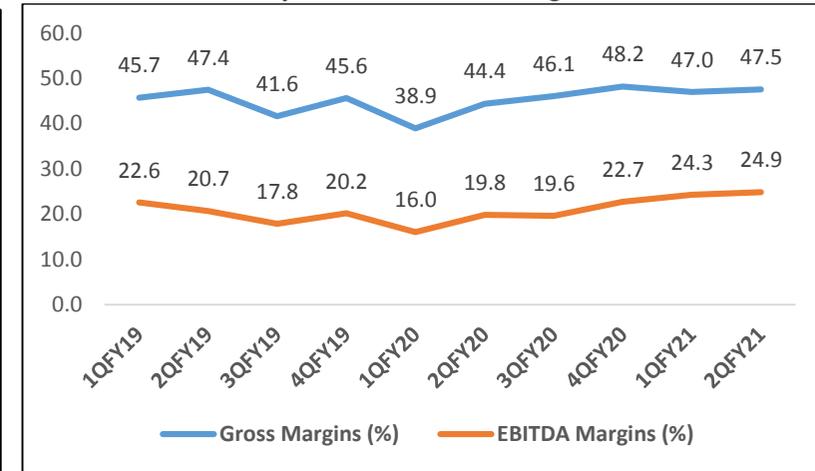
Benign raw material prices coupled with strong industry tailwinds driven by China plus one theme

Methanol, Ammonia and ethyl alcohol are key raw materials used in manufacturing aliphatic amines like methylamine and ethylamine. Methanol is mainly a crude derivate and is mainly imported from countries in the Middle East such as Saudi Arabia, Oman, Qatar, Iran etc while Ammonia is difficult to transport so is being locally sourced from domestic companies like RCF. Historically, there has been a lot of volatility in both these raw materials which in short term has an arching impact on the operating performance of the company as price hikes are taken but with a lag. However, both Ammonia and methanol prices have been stable which has resulted in strong margin uptick even in the lock down quarter.

Quarterly Methanol & Ammonia Price trend



Quarterly EBITDA & Gross Margin Trend



Also lower raw material prices had coincided with strong traction from the Pharma API and Agrochem space (combined contributes 3/4th of Balaji Amine revenues) which were mainly on the back of global geo political tension leading to China plus one strategy and import substitution (~70% dependence on China for bulk drugs/key starting material). In our view, the governments long term vision of reducing its dependence on imports and encouraging “Make in India” through various initiatives like development of bulk drugs parks and

PLI scheme (Product linked incentive-still at a very nascent stage) has a lot of potential to attract foreign investments in end-user industries like Pharma API and Agrochem which augurs well for companies like Balaji Amines.

Long Term Triggers

Commercial production of new Greenfield expansion

BAL is currently in an investment phase at its Phase I- Greenfield project, where it plans to install capacity to manufacture 16,500 tons (50 MT/day) of Ethyl amines and 9,900 tons (30 MT/day) of Di-methyl carbonate (DMC- Import substitution product, BAL 1st to manufacture in India). Post Capex, it will have the largest installed ethyl amines capacity in India of 22,500 MTPA (50MT/day) from current 6000 MTPA. Indian domestic demand for ethylamines currently stands ~20,000MTPA of which imports contribute ~10,000 MTPA. As per the management, the supply gap is likely to widen to 15,000MTPA in next 2 years. BAL aims to gradually utilize this new capacity over a decade and expects 10-15% incremental growth in the ethyl amines segment every year. Greenfield project is likely to start production Q4FY21 onwards, while the major revenue from incremental capacity to start flowing FY22 onwards. Almost 80% of Methylamines and ~50-60% of Ethylamines are used internally in production amine derivative and specialty products.

Post the commencement of this project, BAL management has approved a plan to double its Methylamines capacity. Currently it is a market leader in Methylamines segment with an installed capacity of 48.000 MTPA which it plans to augment by another 40,000-50,000 MTPA under Phase II- expansion of greenfield project. We expect, a meaningful revenue from this expansion to be visible FY24 onwards.

Apart from amines, on the specialty chemical space, BAL had started manufacturing Acetonitrile from Nov '19 onwards and has been gradually ramping up its production capacity to about 9 MT/ day. It is in the process of de-bottlenecking its Acetonitrile plant which will result in doubling the capacity from 9 MT/day to 18-20 MT/day.

Ramp-up in utilization in subsidiary company Balaji Specialty Chemicals (BSCPL):

In Oct 2017 BAL announced acquisition of 55% stake in Balaji Specialty Chemicals. Since then, BSCPL has become a subsidiary of the company with 45% of the stake with the promoters of BAL. The core focus of this company is substituting the products that have historically been procured by Indian consumers via imports from MNCs. Its current product portfolio comprises of Ethylenediamine (EDA), Piperazine (PIP), and Diethyltriamine (DETA). India is currently importing about 29,000 tons of EDA; 8,000 tons of PIP and 3,000 tons of DETA. EDA basically goes in to end user industry of agrochemicals for manufacturing Mancozeb while PIP and DETA is consumed for

applications in pharmaceuticals, polymer, coatings, etc. The total installed capacity of these products as on Sept '20 stood at 45,330 MTPA (EDA- 37,350MT, PIP- 4050MT, DETA-3150MT and amine mixtures- 780MT). BSL has got a status of mega project, where it is eligible to get back all the State-GST paid on account of the sales which is almost 50% of the total GST. The total debt in the subsidiary stood at ~Rs 130Cr.

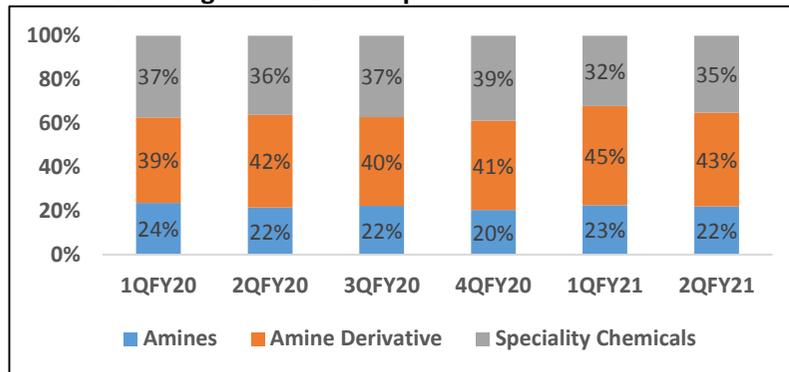
As per the management, by FY22, they expect BSCPL utilization to reach 75-80%. On optimal utilization, peak revenue at average prices of Rs 150-160/Kg can be ~Rs 400Cr. However, volume uptick and utilization trend will be key monitorables as revenue of the subsidiary is fully dependent on end-product prices. As per our estimates, we expect, BSCPL to register a Revenue, EBITDA & PAT of Rs. 180Cr, Rs 32Cr and Rs 21Cr respectively in FY22.

High focus on amine derivative and specialty products to be margin accretive

In order to accelerate its earnings growth trajectory, BAL has been persistently focusing on value-add products and expanding its product offering at regular intervals. New product selection strategy for end product for BAL is purely dependent on the competition landscape of the products in India. It only enters into categories where it is either the first or second manufacturer in India to substitute products that are being imported into the country. BAL is in constant endeavor to enrich its product mix with higher proportion of amine derivative and specialty products. We expect, higher volume growth to be driven by products like Acetonitrile, DMAC (Dimethyl Acetamide) and Specialty chemicals like NMP/NEP/2-P (Pyrrolidone) and GBL.

Recent announcement of production linked incentive scheme provides the right tailwinds for long term volume growth for BAL. Also a positive outcome of the anti-dumping duty case on DMF could further bolster its demand.

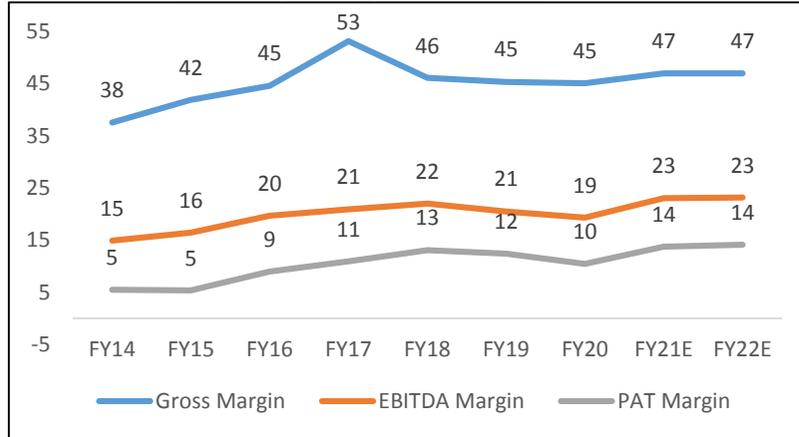
Volume-wise segmental Break-up



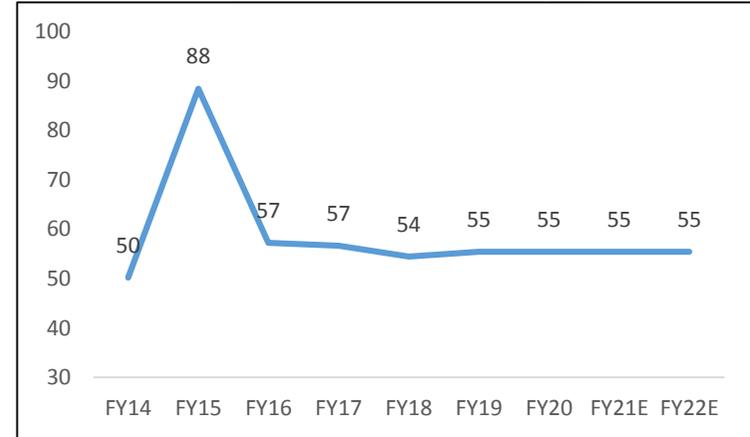
Key Financial Summary

- BAL has delivered a healthy Revenue CAGR of 13% over FY10-20 aided by its consistent focus on innovation, new product launches and scale-up of its high margin value-add and specialty chemicals segment. Going forward, we expect the company to report a revenue CAGR of 14% over FY20-22E.
- Its EBITDA and PAT grew by CAGR 15% and 17% respectively over FY10-20. Historically, its Gross and EBITDA margins have been relatively stable due to BAL's ability to pass it on higher raw material prices to end-customers albeit with a lag. Its 10-Yr average gross margins stood at ~45% while its EBITDA margin has been oscillating in the range of 17-22%. Going forward, we expect its operational performance to further improve with EBITDA and PAT likely to grow at CAGR 25% and 32% respectively over FY20-22E.
- On the cash conversion side, BAL for last 5-years has been consistently restricting itself to less 2 months (5-Yr Avg 56 days) Net D/E has been constantly falling down from 0.6x in FY16 to 0.4x in FY20 which is further likely to reduce and we expect the company to be Net debt free by FY22. Constant debt reduction (inspite of heavy capex of Rs 383Cr over FY16-20) is mainly driven by strong FCF generation (Rs 180Cr FY16-20) resulting in superior return ratios.

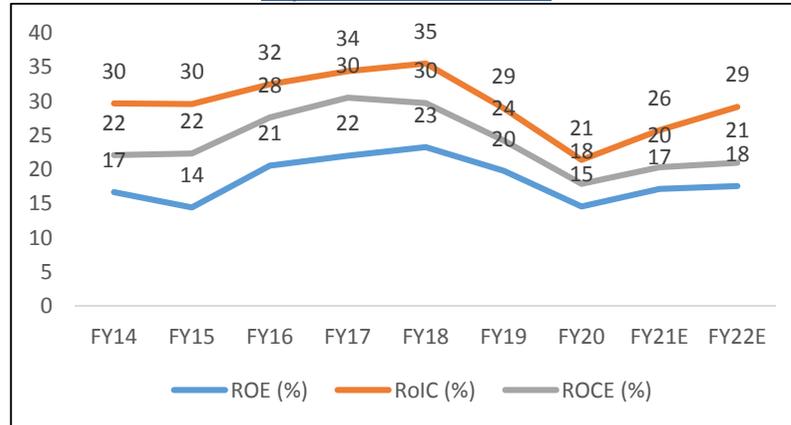
Stable Operating Performance



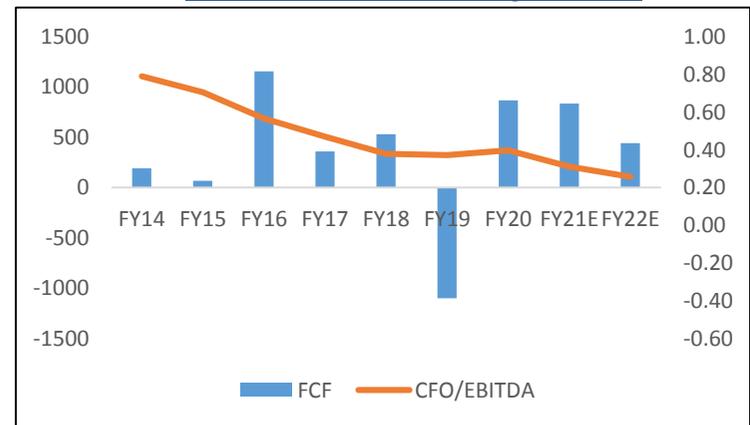
Stable Cash Conversion Cycle



Superior Return Ratio's



Consistent Free Cash Flow generation



(Source: Company, HDFC sec)

What could go wrong?

- **Sharp rise in Competitive Intensity**

Aliphatic amines is an oligopolistic industry mainly dominated by 2 large players in India. A sharp rise in competitive intensity either from cheap imports or aggressive pricing by competition can impact overall operational performance of the company.

- **Inability to grow new specialty chemical launches by Balaji Specialty Chemicals (BSCPL)**

Balaji Specialty Chemicals (BSCPL) is the subsidiary company of BAL which is only focusing on purely import substitution products. As per the management, the domestic demand for these product continues to be robust, however in case of company's inability to scale-up the business or any cheap import dumping in these products can impact the profitability and future growth trajectory of the subsidiary company.

- **Sharp rise in Raw material Inflation**

The main raw material for BAL includes methanol, ammonia, ethanol and denatured ethyl alcohol. Historically there has been high volatility in prices of these products. Higher volatility in raw material prices can impact the spread and profitability of the company in short to medium term as the company has inherent advantage of passing on the high RM prices albeit with a lag.

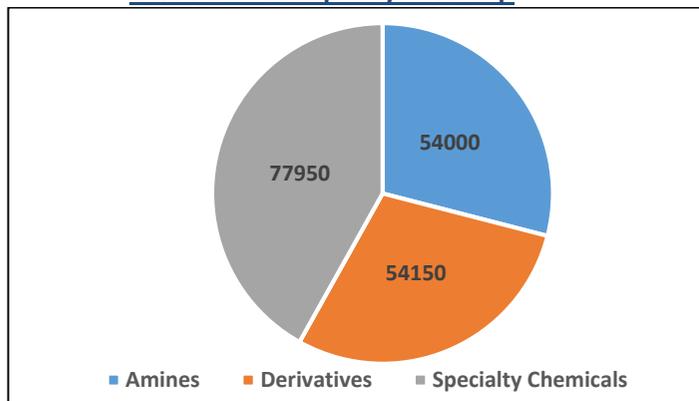
- **Continued losses in CFL unit and delayed breakeven in Hotels division** - BAL has CFL lamps facility at Medak, Telangana which was acquired vide amalgamation of Balaji Greentech Products Limited with BAL in the FY18. The unit has capital employed of Rs.29.5 cr and EBIT loss of Rs.1.6 cr in FY20 on almost nil sales. Its Hotel division had sales of Rs. 20.4 cr , EBIT of -0.3 cr and capital employed of Rs.63.8 cr in FY20. Both these divisions are pulling down the overall profitability and return ratios of the company.

Company Profile:

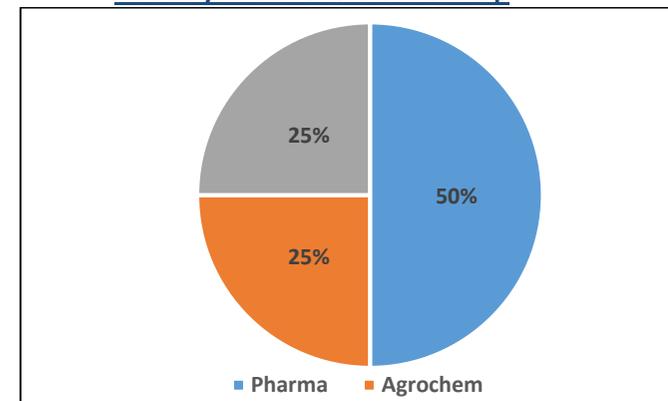
Balaji Amines Ltd, is one of the largest manufacturers of Aliphatic amines in India. Over the years, it has transformed itself from regional player with a very limited product basket to a truly Indian multinational with diverse product range of 30 products with exports across 45 countries. Exports contributes ~20% of overall revenues. More than 80% of the products produced by the company were previously imported in India. Its current installed capacity as on 184,500 MTPA. It has specialized in manufacturing Methylamines, Ethylamines and its derivatives. Industry-wise more than 3/4th of its revenue comes from Pharma (51%) & Agrochem (26%) space where its products are used

as solvents and feed additives. Its top clients includes companies like Sun Pharma, Dr Reddy's, Mylan, HIKAL, Zydus, Hetero etc. Apart from the core aliphatic amine business it also operates a 5 start hotel in Solapur –Balaji Sarovar.

Product-wise capacity Break-up



Industry-wise Revenue Break-up



(Source: Company, HDFC sec)

Peer Comparison

| Name | CMP Rs. | Mar Cap Rs.Mn. | EPS 12M Rs. | OPM % | PATM % | Div Yld % | ROE % | TTM P/E | P/BV | D/E |
|---------------|---------|----------------|-------------|-------|--------|-----------|-------|---------|------|-----|
| Balaji Amines | 950 | 30770 | 43.6 | 23% | 15% | 0.3% | 15% | 24 | 4.6 | 0.4 |
| Alkyl Amines | 3289 | 69170 | 119 | 30% | 24% | 0.3% | 41% | 31 | 10.9 | 0.1 |

(Source: Company, HDFC sec)

Financials

Income Statement

| (Rs Mn) | FY18 | FY19 | FY20 | FY21E | FY22E |
|--------------------------|--------|--------|--------|--------|--------|
| Net Revenues | 8612 | 9431 | 9358 | 10003 | 12053 |
| Growth (%) | 18% | 10% | -1% | 7% | 20% |
| Operating Expenses | 6717 | 7496 | 7550 | 7695 | 9261 |
| EBITDA | 1894.9 | 1934.1 | 1807.5 | 2307.9 | 2791.9 |
| Growth (%) | 24% | 2% | -7% | 28% | 21% |
| EBITDA Margin (%) | 22 | 20.5 | 19.3 | 23.1 | 23.2 |
| Depreciation | 192.9 | 195.5 | 316.2 | 325.2 | 361.2 |
| EBIT | 1702.1 | 1738.5 | 1491.2 | 1982.6 | 2430.7 |
| Other Income | 40.7 | 42.3 | 50.1 | 34.4 | 36.2 |
| Interest expenses | 90.4 | 130.3 | 230.3 | 178.1 | 190.9 |
| PBT | 1652.4 | 1650.6 | 1311 | 1839 | 2276 |
| Tax | 526.6 | 479.7 | 336.3 | 463.4 | 573.6 |
| RPAT | 1125.8 | 1170.9 | 974.7 | 1375.6 | 1702.4 |
| APAT | 1125.8 | 1170.9 | 974.7 | 1375.6 | 1702.4 |
| Growth (%) | 41% | 4% | -17% | 41% | 24% |
| EPS | 34.8 | 36.1 | 30.1 | 42.5 | 52.5 |

Balance Sheet

| (Rs Mn) | FY18 | FY19 | FY20 | FY21E | FY22E |
|-----------------------------------|---------------|---------------|---------------|---------------|----------------|
| SOURCE OF FUNDS | | | | | |
| Share Capital | 64.8 | 64.8 | 64.8 | 64.8 | 64.8 |
| Reserves | 4785.8 | 5855.3 | 6618.9 | 7970.1 | 9640.3 |
| Shareholders' Funds | 4850.6 | 5920.1 | 6683.7 | 8034.9 | 9705.1 |
| Long Term Debt | 424.9 | 833.3 | 1199.1 | 1274.1 | 1424.1 |
| Net Deferred Taxes | 502.2 | 457.5 | 437.3 | 437.3 | 437.3 |
| Other Liabilities | 133.4 | 163.7 | 167.6 | 152.6 | 155.8 |
| Minority Interest | | | | | |
| Total Source of Funds | 5911.1 | 7374.6 | 8487.6 | 9898.9 | 11722.3 |
| APPLICATION OF FUNDS | | | | | |
| Net Block & Goodwill | 3160.6 | 3197.5 | 5730 | 5982.8 | 6569 |
| CWIP | 1231.3 | 2694.6 | 446.3 | 700 | 910 |
| Other Non-Current Assets | 539.3 | 72.8 | 332.3 | 46.8 | 46.8 |
| Total Non-Current Assets | 4931.2 | 5964.8 | 6508.6 | 6729.6 | 7525.8 |
| Current Investments | 0 | 0 | 0 | 0.1 | 0.1 |
| Inventories | 891 | 1631.5 | 1104.4 | 1171.9 | 1412 |
| Trade Receivables | 1726.8 | 1672.2 | 2074.4 | 2005.6 | 2416.6 |
| Cash & Equivalents | 241.7 | 204 | 563.1 | 1762.6 | 2128.2 |
| Other Current Assets | 687.8 | 986.3 | 880.5 | 716.6 | 863.5 |
| Total Current Assets | 3547.2 | 4494 | 4622.5 | 5656.7 | 6820.3 |
| Short-Term Borrowings | 1093.6 | 1440.7 | 1214.8 | 1399.5 | 1355.9 |
| Trade Payables | 718.4 | 854.4 | 628.9 | 878.9 | 1059.1 |
| Other Current Liab & Provisions | 755.3 | 789.1 | 799.8 | 208.9 | 208.9 |
| Total Current Liabilities | 2567.3 | 3084.3 | 2643.4 | 2487.4 | 2623.8 |
| Net Current Assets | 979.9 | 1409.8 | 1979.1 | 3169.3 | 4196.5 |
| Total Application of Funds | 5911.1 | 7374.6 | 8487.6 | 9898.9 | 11722.3 |

Cash Flow Statement

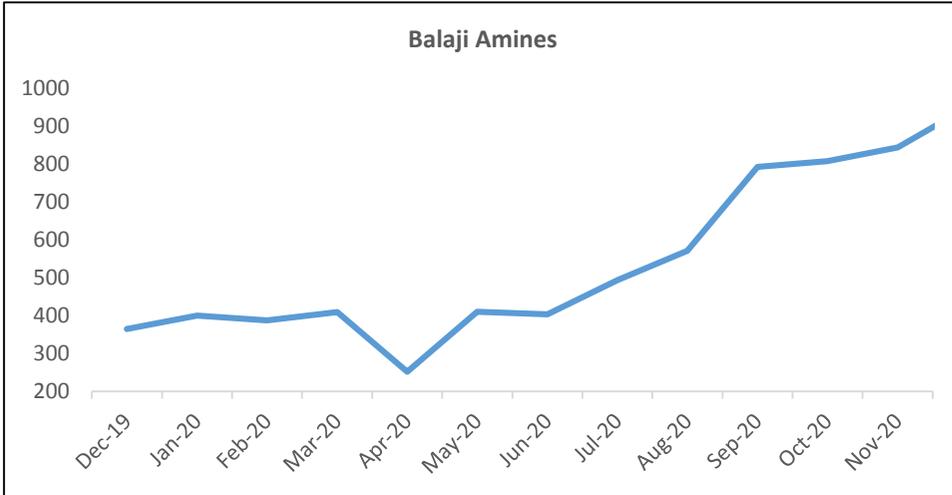
| (Rs Mn) | FY18 | FY19 | FY20 | FY21E | FY22E |
|----------------------------------|------------------|------------------|-----------------|-----------------|------------------|
| Reported PBT | 1,658.40 | 1,650.60 | 1,311.00 | 1,839.00 | 2,276.00 |
| Non-operating & EO items | -46.7 | -42.3 | -50.1 | -34.4 | -36.2 |
| Interest Expenses | 90.4 | 130.3 | 230.3 | 178.1 | 190.9 |
| Depreciation | 192.9 | 195.5 | 316.2 | 325.2 | 361.2 |
| Working Capital Change | 249 | -814.7 | 15.8 | -175.5 | -617.9 |
| Tax Paid | -532.5 | -524.4 | -356.5 | -463.4 | -573.6 |
| OPERATING CASH FLOW (a) | 1,611.40 | 595 | 1,466.70 | 1,668.90 | 1,600.50 |
| Capex | -1,079.10 | -1,695.70 | -600.5 | -831.7 | -1,157.40 |
| Free Cash Flow | 532.3 | -1,100.70 | 866.3 | 837.2 | 443.1 |
| Investments | 23.6 | 0 | 0 | -0.1 | 0 |
| Non-operating income | -473.2 | 508.8 | -209.3 | 319.9 | 36.2 |
| INVESTING CASH FLOW (b) | -1,528.80 | -1,186.90 | -809.8 | -511.9 | -1,121.20 |
| Debt Issuance / (Repaid) | 39.2 | 755.6 | 139.8 | 259.8 | 106.3 |
| Interest Expenses | -90.4 | -130.3 | -230.3 | -178.1 | -190.9 |
| FCFE | 481.1 | -475.4 | 775.7 | 918.9 | 358.5 |
| Share Capital Issuance | 0 | 0 | 0 | 0 | 0 |
| Others | 175.3 | -71.1 | -207.3 | -39.3 | -29 |
| FINANCING CASH FLOW (c) | 124.1 | 554.2 | -297.8 | 42.4 | -113.6 |
| NET CASH FLOW (a+b+c) | 206.8 | -37.7 | 359.1 | 1,199.50 | 365.6 |

Key Ratios

| | FY18 | FY19 | FY20 | FY21E | FY22E |
|-------------------------------|--------|--------|--------|--------|--------|
| EBITDA Margin | 22.00% | 20.50% | 19.30% | 23.10% | 23.20% |
| EBIT Margin | 19.80% | 18.40% | 15.90% | 19.80% | 20.20% |
| APAT Margin | 13.10% | 12.40% | 10.40% | 13.80% | 14.10% |
| RoE | 23% | 20% | 15% | 17% | 18% |
| RoCE | 30% | 24% | 18% | 20% | 21% |
| Solvency Ratio | | | | | |
| Net Debt/EBITDA (x) | 0.7 | 1.1 | 1.4 | 0.4 | 0.2 |
| Net D/E | 0.3 | 0.4 | 0.4 | 0.1 | 0.1 |
| PER SHARE DATA | | | | | |
| EPS | 34.8 | 36.1 | 30.1 | 42.5 | 52.5 |
| CEPS | 40.8 | 42.2 | 39.8 | 52.5 | 63.7 |
| Dividend | 2.2 | 2.6 | 5.4 | 0.6 | 0.8 |
| BVPS | 149.7 | 182.7 | 206.3 | 248 | 299.5 |
| Turnover Ratios (days) | | | | | |
| Debtor days | 73 | 73 | 73 | 73 | 73 |
| Inventory days | 38 | 43 | 43 | 43 | 43 |
| Creditors days | 57 | 61 | 61 | 61 | 61 |
| VALUATION | | | | | |
| P/E | 27 | 26 | 32 | 22 | 18 |
| P/BV | 6.3 | 5.2 | 4.6 | 3.8 | 3.2 |
| EV/EBITDA | 17 | 17 | 18 | 14 | 12 |
| EV / Revenues | 3.8 | 3.5 | 3.5 | 3.3 | 2.7 |
| Dividend Yield (%) | 0.3 | 0.3 | 0.6 | 0.1 | 0.1 |



One Year Stock Price Chart



(Source: Company, HDFC sec)

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HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Binkle R. Oza Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

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