

June 23, 2022

Set to enter the big league...

About the stock: Incorporated in 2008 by Prahladbhai Patel, PSP Projects (PSP) is one of the prominent contractors offering a diversified range of construction and allied services. Its focus remains on industrial, institutional, government, government residential and residential projects.

- PSP reported 34.3%, 31.2%, 31.3% CAGR in topline, EBITDA, PAT CAGR, respectively, during FY17-22
- Prudent management, net debt free, robust return ratios (RoCE: ~25+%)

FY22 Performance: PSP reported strong results in FY22– albeit on a lower base.

- Revenue improved 40.9% YoY (to ₹ 1,749 crore) driven by its comfortable order book position and pick-up in execution
- EBITDA margins improved significantly by 380 bps YoY to 14.7%
- PAT doubled to ₹ 162 crore (PAT margin: 9.3%)

What should investors do? PSP's share price has grown at ~18% CAGR over the past five years (from ₹ 217 in June 2017 to ₹ 504 levels in June 2022).

- We initiate coverage under Nano Nivesh format with a **BUY** rating

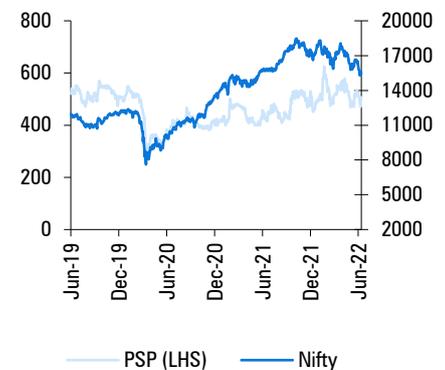
Target Price and Valuation: We value PSP at ₹ 630 i.e. 12.5x FY24E P/E

Key triggers for future price performance:

- PSP's pre-qualification for public projects would rise to ₹ 2,000+ crore with the completion of the Surat Diamond Bourse (SDB) project. Addition of big ticket sized project is expected to boost its overall order book position
- Strong focus by the government on affordable housing, Smart Cities Mission and industrial corridors coupled with expected pick-up in private players' capex may translate into robust inflows for PSP
- Diversification in select states offers a bigger opportunity pie
- Significant traction and orders for pre-cast facility is likely to bring incremental benefits and associated revenue
- We expect revenue, earning CAGR of 15.3%, 5.9%, respectively, in FY22-24E



Price Performance



Research Analyst

Bhupendra Tiwary, CFA
bhupendra.tiwary@icicisecurities.com

Lokesh Kashikar
lokesh.kashikar@icicisecurities.com

Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	FY22	5 Year CAGR (FY17-22)	FY23E	FY24E	2 Year CAGR (FY21-24E)
Net Sales	1,044.0	1,499.3	1,240.9	1,748.8	34.3	2,035.7	2,325.2	15.3
EBITDA	148.9	191.0	134.8	256.5	31.2	254.0	298.8	7.9
EBITDA Margin (%)	14.3	12.7	10.9	14.7		12.5	12.8	
Net Profit	90.2	129.3	80.8	162.4	31.3	153.0	182.1	5.9
EPS (₹)	25.1	35.9	22.4	45.1		42.5	50.6	
P/E (x)	20.1	14.0	22.4	11.2		11.9	10.0	
Price / Book (x)	4.9	4.0	3.4	2.6		2.2	1.9	
EV/EBITDA (x)	10.9	8.9	12.4	6.8		7.0	5.9	
RoCE (%)	37.6	35.9	20.7	31.0		24.9	24.9	
RoE (%)	24.3	28.3	15.5	23.7		18.9	19.0	

Source: Company, ICICI Direct Research

Description

Incorporated in August 2008, PSP Projects (PSP) is a Gujarat based construction company offering a diversified range of construction and allied services across industrial, institutional, government, government residential and residential projects in India. It offers a bouquet of services ranging from planning & design to construction & post-construction activities. Since inception, the company has successfully completed 183 projects whereas work on 43 projects is currently in-progress. Geographically, PSP is currently diversified with a presence in six states viz. Gujarat, Rajasthan, Karnataka, Uttar Pradesh, Maharashtra and New Delhi. Additionally, the company is likely to get a major boost with completion of SDB project valued at ~₹ 1,850 crore. With its completion, pre-qualification for public projects would rise to ₹ 2,000+ crore, which will aid it to bag larger sized projects.

History and track record

- **2008:** Incorporated by first generation civil engineer; started off as a construction contractor
- **2010:** Awarded project for work on beautification of riverfront and construction of Chief Minister's office
- **2011-12:** Extended its services to MEP, interior & O&M segment
- **2013-14:** Forayed into EPC project for affordable housing in Ahmedabad
- **2015:** First order inside the first Smart City - GIFT City. Later PSP did six projects in GIFT
- **2016:** Started operations in Karnataka and Rajasthan
- **2017:** Listed on NSE and BSE raising ₹ 211.7 crore; secured SDB project initially valued at ₹ 1,575 crore
- **2020:** Started operations in Uttar Pradesh with a marquee project "Beautification of Sri Kashi Vishwanath Dham"
- **2021:** Commissioned pre-cast facility at Sanand, Gujarat with the objective to provide technological upgradation

Exhibit 1: Earnings Estimates

₹ Crore	FY20	FY21	FY22	FY23E	FY24E
Sales	1,499.3	1,240.9	1,748.8	2,035.7	2,325.2
EBITDA	191.0	134.8	256.5	254.0	298.8
PAT	129.3	80.8	162.4	153.0	182.1
EPS	35.9	22.4	45.1	42.5	50.6

Source: Company, ICICI Direct Research

Exhibit 2: Technical Chart (Weekly Bar Chart)



Source: Bloomberg, ICICI Direct Research

Stock data

Particular	Amount
Market Capitalisation (₹ crore)	1,813.7
Debt (FY22) (₹ crore)	114.7
Cash (FY22) (₹ crore)	195.2
EV (₹ crore)	1,733.2
52 week H/L (₹)	639 / 406
Equity capital (₹ crore)	36.0
Face value (₹)	₹ 10

Valuation

(x)	FY21	FY22	FY23E	FY24E
P/E	22.1	11.0	11.7	9.8
EV / EBITDA	12.2	6.7	6.9	5.8
P/BV	3.3	2.6	2.2	1.9
RoNW (%)	15.5	23.7	18.9	19.0
RoCE (%)	20.7	31.0	24.9	24.9

Quarterly Performance

	Q1 FY22	Q2 FY22	Q3 FY22	Q4 FY22
Sales	317.4	390.4	485.6	555.3
EBITDA	39.4	54.7	74.1	88.1
EBITDA (%)	12.4	14.0	15.3	15.9
Other Income	3.8	4.6	7.6	5.4
PAT	25.1	36.6	46.9	53.8
EPS	7.0	10.2	13.0	14.9

Shareholding trend (%)

	Jun-21	Sep-21	Dec-21	Mar-22
Promoter	74.2	69.9	70.2	70.2
FII	1.3	1.5	1.7	1.8
DII	4.0	4.7	5.7	4.8
Others	20.6	23.9	22.4	23.2

Technical View

The historical multi time frame price structure analysis reveals some interesting facets supporting a bullish scenario for PSP Projects from a medium term perspective.

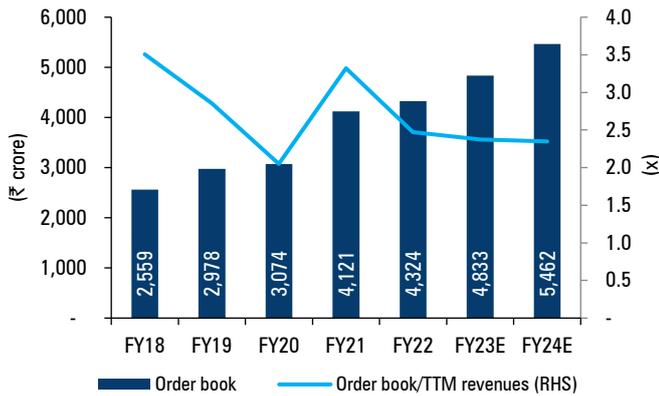
The share price has been broadly oscillating in the price band of ₹ 600-400 over past four years, indicating a significant time correction behind us.

On the price front, the stock has exhibited a strong resilience in ongoing corrective phase wherein it made a strong base around ₹ 440 that is value of 100-week average, which has been held on multiple occasions since CY20.

Considering the resilience and the significant time correction behind us, the share price at the current juncture provides a favourable risk-reward with bullish setup. On the higher side, lifetime high around ₹ 620 would be the initial target price over the next few quarters

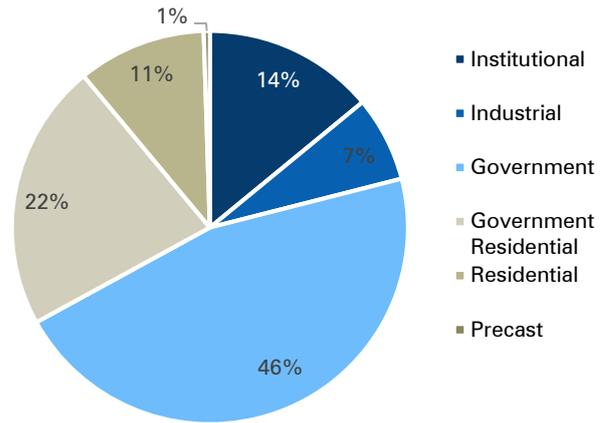
Story in charts

Exhibit 1: Order book* trend



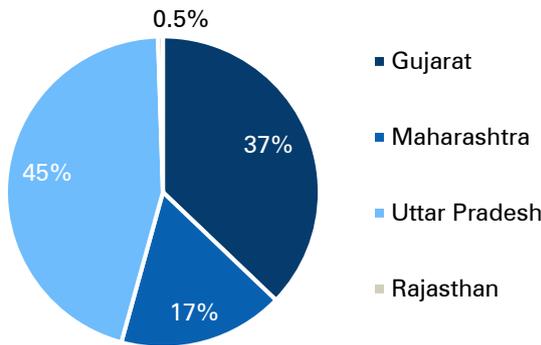
Source: Company, ICICI Direct Research

Exhibit 2: Order book* spread across major verticals



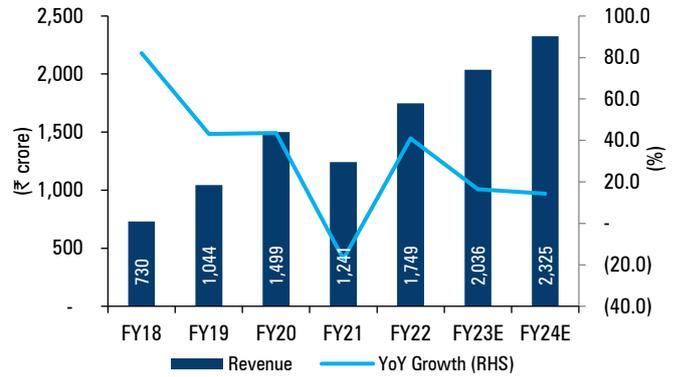
Source: Company, ICICI Direct Research* Order book worth ₹ 4,324 at FY22-end

Exhibit 3: Home state Gujarat contributes 37%*



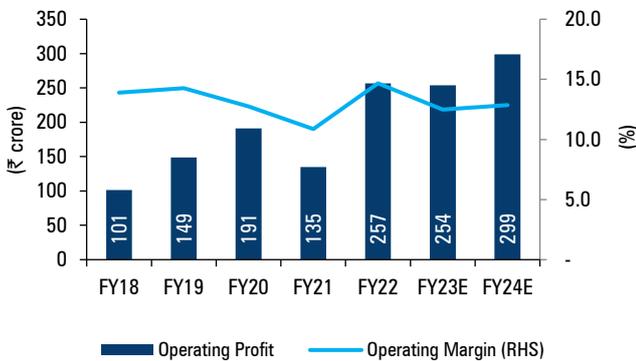
Source: Company, ICICI Direct Research; * Order book worth ₹ 4,324 crore at FY22-end

Exhibit 4: Revenue to improve at 15.3% CAGR*



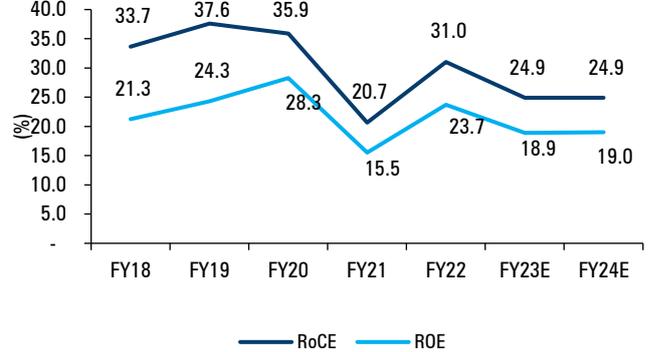
Source: Company, ICICI Direct Research; during FY22-24E

Exhibit 5: Margins to moderate



Source: Company, ICICI Direct Research

Exhibit 6: Strong return ratios



Source: Company, ICICI Direct Research

What's the story?

Strong experience in construction business; emphasis on handpicked segments bodes well

PSP has established itself as one of the leading contractors in and around Gujarat for institutional, industrial, residential and government projects by leveraging its strong experience of 183 project deliveries in the EPC construction sector. Additionally, it has filled a vacuum that is vitally occupied by an organised player in the project ticket size of ₹ 100-300 crore. Further, its dedicated focus towards handpicked segments has kept its business model asset-light (no exposure towards asset heavy segments such as roads - HAM/BOT, power T&D and railways sectors). Also, its healthy track record of timely completion and quality work, coupled with good management touchpoints has led to a strong brand recall. Thus, there are repeat orders from existing clients and incremental orders from new clients. Since its incorporation, the company has executed 29 projects for Zydus Cadila group, 15 for Torrent Pharmaceuticals, seven for Adani Group and six for the Claris Group.

Entrenched in Gujarat; spreading wings to other promising regions

PSP has predominantly been a Gujarat-focused player having operated on numerous marquee assignments such as Surat Diamond Bourse, GIFT City, Gujarat Vidhan Sabha building and Sabarmati Riverfront Development projects. The execution of majority of projects in a particular region has aided the company to develop strong competencies across numerous stages of project life cycle. However, the company has started exploring other promising regions to diversify itself and become future-ready with a pan-India presence over the medium-to-longer term. In line with these, its home state - Gujarat now contributes merely 37% to the overall order book (worth ₹ 4,324 crore as on March 31, 2022) while Uttar Pradesh and Maharashtra form a noteworthy 45% and 17%, respectively. Going forward, its focus on geographical diversification by bagging various projects in various parts of the country is likely to open incremental opportunities for the company.

SDB in completion mode; to enter big league with increase in pre-qualification

PSP achieved a major breakthrough in October 2017 when it secured a key contract work for Surat Diamond Bourse (SDB) project spread over 66 lakh sq ft area. This was the company's maiden project having a project value >₹ 1,000 crore, outbidding competitors such as Shapoorji Pallonji and L&T. Currently, the project is in completion stage wherein the company has handed-over the towers while the entire handover is expected by June 2022-end. With its completion, PSP's pre-qualification for public projects would rise to ₹ 2,000+ crore. This, in turn, would help the company to bag larger sized projects.

Pre-cast facility to bring incremental benefits; total revenue potential of ~₹ 300 crore on full capacity

The Indian construction industry witnessed a major setback during the peak of the pandemic era largely impacted by migration of labour to their respective native places, increased project-related costs and significantly slowed down execution pace. This has also increased the overall project completion time-period. However, in-order to reduce the impact, to some extent, PSP has come out with innovative ways wherein it would be able to manufacture major elements of building and infrastructure industry like beams, columns, slabs, load bearing walls, partition walls, staircase, and lift cores in its pre-cast facility in Sanand, Gujarat. This is likely to substantially reduce the time/effort required via traditional building methods by way of maximum pre-fabrication, thereby reducing turnaround-time and increasing operating efficiencies. Under phase-1, the plant (spread across 60 acres; factory shed of 2 lakh sq ft) has a production capacity of 1 mn sq ft (capex: ₹ 109 crore) with revenue potential of ~₹ 100-125 crore at full capacity. Work on this facility is now complete. Additionally, the annual production capacity is expected to increase to 3 mn sq ft (with incremental ₹ 20-25 crore capex on machineries; revenue potential would increase to ~₹ 300-350 crore). Till now, total orders received from pre-cast segment is to the tune of ₹ 59 crore. First order received was from L&T worth ₹ 49 crores as part of National High Speed Rail project while balance orders are from residential and industrial segments. Discussions are also going on with L&T and other clients for more potential orders. Margins are expected to be in-line with EPC orders.

Healthy order book position; pick-up in momentum in inflows to continue

As on March 31, 2022, PSP's order book was healthy at ₹ 4,324 crore, which improved >5x over past five years. Most of its projects are in the execution/mobilisation stage (excluding two EWS Housing projects in Bhiwandi and Pandharpur worth ~₹ 730 crore). Additionally, PSP has secured orders worth ~₹ 550 crore post FY22 and is L1 for a government medical college in Gujarat with bid value of ₹ 615 crore - strengthening its order book position even further (3.1x current order book to FY22 revenues). Moreover, its bid pipeline remains equally strong (worth ₹ 4,500 crore) with improved economic activity in target states like Gujarat, Uttar Pradesh and Maharashtra post Covid-19 related slowdown. These provide ample business opportunities given its strong reputation associated with quality work and track record of successful execution. We expect the improved momentum in order inflows to continue with better opportunities coming from both - government and private clients, its expansion into different states, and improved eligibility of higher-ticket size projects.

Revenue to reach ₹ 2,300+ crore by FY24E; margins to moderate to ~12.5-13%

PSP reported 55.2% revenue CAGR in FY17-20, mainly backed by improved order book position and pick-up in execution skills. However, the pace was impacted during FY21 due to the Covid-19 pandemic. In-turn, the company reported 17.2% decline in FY21 topline (H1 FY21 revenue: ₹ 350 crore; H2 revenue: ₹ 891 crore). Nevertheless, PSP regained its lost momentum in execution during FY22 with normalisation in construction activities and posted healthy 40.9% YoY topline growth. Going forward, we expect the improved momentum in execution to continue, which would enable the company to post 15.3% CAGR over FY22-24E (to ₹ 2,325 crore in FY24E) with comfortable order book position, healthy expected in inflows and pick-up in execution. Operating margin is expected to moderate to 12.8% in FY24E (from 14.7% in FY22) to be impacted by increasing volatility in raw material prices, higher competitive intensity, meaningful contribution from pre-cast facility (expects margin at slightly lower than EPC business), higher contribution from fixed-price government jobs and uncertainty arising due to geographical diversification. However, built-in escalation clauses in most private projects for raw material price variations provide some cushion.

Net cash positive position, prudent working capital management augur well

PSP has a lean balance sheet structure backed by its asset light model (no investments in metro and roads projects) and has a net cash positive position. While capex incurred towards pre-cast facility (₹ 109 crore) has increased the debt-level, to some extent, we do not expect a major swing in its net debt position further as incremental free cash flows would be sufficient for its working capital and capex requirement, going forward. Also, the company has exhibited prudent working cycle management. In most projects, PSP earns mobilisation advances to the tune of 5-10%. Long standing relationships with suppliers ensure favourable credit terms while use of technology backs prudent inventory management skills. The company also commands superior return ratios (RoE, RoCE at ~19%, ~25%, respectively, during FY24E).

Exit from US subsidiary –end of key overhang

PSP, via its whole owned subsidiary PSP Projects INC, was operating projects in Livermore and San Francisco (US). However, the company was working as a developer in these projects, which included building houses in its owned land parcels. While overall loans and investments in this subsidiary was in the tune of ~₹ 25 crore (till December 31, 2021), there was no clarity on the total capital requirements – giving rise to noteworthy risk to its overall balance sheet position. Thankfully, the company has managed to divest its 100% stake in the subsidiary recently and recovered its complete investments, extended loans & advances. With this, PSP's overall operations now remains in India largely related to its core EPC business.

Trading at decent valuation of 10x 24E P/E

PSP is set to enter the big leagues, mainly backed by a) its rich construction experience, b) eligibility to bid for higher-ticket size project with improvement in pre-qualification criteria, c) geographical diversification, d) healthy order book position, e) strong revenue visibility and decent margins and f) healthy return ratios. At the CMP, the company is currently trading at a valuation of 10x FY24E P/E. We have a **BUY** recommendation with a target price of ₹ 630 (12.5x FY24E P/E).

Exhibit 3: Key project details

Description of Project	Location	Name of client	Contract Value (₹ crore)	Order book Value (₹ crore)
Medical Colleges & Hospitals At 7 Locations	Uttar Pradesh	Public Works Department	1,491	1,343
High Rise Buildings cum Commercial units - EWS Housing Project under PMAY, Bhiwandi	Maharashtra	Municipal Corporation	601	601
Sports Complex	Gujarat	Municipal Corporation	504	504
Residential Project	Gujarat	Private Developer	499	423
IIM Ahmedabad - Construction of faculty house, student hostels and new academic block	Gujarat	Indian Institute Of Management	328	106
Affordable Housing Project, Pandharpur	Maharashtra	Municipal Corporation	158	126
Construction of steel plant	Gujarat	Private Company	257	210
Construction of Residential Buildings of PAC Mahila Battalion at Badaun, UP	Uttar Pradesh	Public Works Department	239	239

Source: ICICI Direct Research, Company

Key risk and concerns

PSP largely dependent on single promoter

Prahaladbhai Patel, promoter and executive director - Chairperson, has 30+ years of experience in the construction business. In these years, Mr Patel has gained precious industry relationships, identified technical know-how and has excellent commitment towards its projects. However, we feel that very few individuals among its 1,400 employees are responsible for key decision-making and Mr Patel's personal involvement is integral to each project life cycle. With increasing project volumes, such micro promoter involvement may not be possible, which may lead to some execution issues.

Significant increase in raw material prices may impact margin performance

Timely and cost-effective execution of PSP's projects is largely dependent on adequate and timely supply of raw materials, chief among them being steel, cement, stone, bricks, wood, aggregate, concrete, sand, sanitary and plumbing items. Since the second half of CY20, prices have been trending higher owing to supply crunch, supply-chain disruptions and increased demand from construction industries. A sharp rise in input costs is likely to weigh on margins if high cement and steel prices persist for a longer time frame.

Increase in competitive intensity may impact order inflows

Competitive intensity in the construction industry has been amplified immensely post disruptions caused by Covid-19 pandemic. We believe aggressive bidding (by competitors) and higher competition may result in lower inflows and moderation in margins, going forward. Additionally, entry into unchartered territories and bagging of projects aggressively may impact the company's performance.

Financial Summary

Exhibit 4: Profit & Loss statement

(Year-end March)	FY21	FY22	FY23E	FY24E
Net Sales	1,240.9	1,748.8	2,035.7	2,325.2
Growth (%)	(17.2)	40.9	16.4	14.2
Raw Material Cost	1,040.2	1,391.3	1,663.1	1,885.8
Employee Cost	50.9	72.3	92.1	110.5
Other Expenditure	15.0	28.6	26.5	30.2
Total Operating Expenditure	1,106.0	1,492.3	1,781.7	2,026.5
EBITDA	134.8	256.5	254.0	298.8
Growth (%)	(29.4)	90.3	(1.0)	17.6
Other income	16.9	21.3	22.6	24.1
Depreciation	25.6	32.1	43.2	48.1
EBIT	126.1	245.7	233.4	274.8
Interest	14.7	26.4	28.9	31.4
PBT	111.4	219.3	204.6	243.4
Tax	27.9	56.9	51.6	61.3
Rep. PAT	83.5	162.4	153.0	182.1
Exceptional items				
Adj. Net Profit	83.5	162.4	153.0	182.1
Growth (%)	(35.4)	94.4	(5.8)	19.0
EPS (₹)	22.4	45.1	42.5	50.6

Source: Company, ICICI Direct Research

Exhibit 5: Cash Flow Statement

(₹ Crore)	FY21	FY22	FY23E	FY24E
Profit after Tax	80.8	162.4	153.0	182.1
Depreciation	25.6	32.1	43.2	48.1
Interest	14.7	26.4	28.9	31.4
Others	(20.3)	(21.4)	(22.6)	(24.1)
Cash Flow before wc changes	100.8	199.4	202.4	237.4
Net Increase in Current Assets	32.9	(161.8)	(142.0)	(134.5)
Net Increase in Current Liabilities	(55.9)	95.8	18.0	56.5
Net CF from operating activities	77.8	133.4	78.5	159.4
Net purchase of Fixed Assets	(75.6)	(81.6)	(50.1)	(50.1)
Others	38.3	(77.0)	(15.2)	(14.1)
Net CF from Investing Activities	(37.3)	(158.6)	(65.3)	(64.2)
Proceeds from share capital	0.1	(1.3)	(0.0)	-
Proceeds/Repayment from Loan	6.1	33.7	20.3	19.6
Interest paid	(14.7)	(26.4)	(28.9)	(31.4)
Others	-	(14.4)	(27.0)	(36.0)
Net CF rom Financing Activities	(8.5)	(8.4)	(35.6)	(47.8)
Net Cash flow	32.0	(33.6)	(22.4)	47.4
Opening Cash and Cash Equivalent	196.7	228.8	195.2	172.8
Closing Cash & cash equivalents	228.8	195.2	172.8	220.2

Source: Company, ICICI Direct Research

Exhibit 6: Balance Sheet

(Year-end March)	FY21	FY22	FY23E	FY24E
Liabilities				
Equity capital	36.0	36.0	36.0	36.0
Reserves & Surplus	502.0	648.7	774.7	920.8
Networth	538.0	684.7	810.7	956.8
Loan Funds	81.0	114.7	135.0	154.5
Deferred Tax liability	(9.2)	(9.4)	(9.4)	(9.4)
Other financial liabilities	0.8	1.5	1.8	2.2
Total Liabilities	610.6	791.5	938.2	1,104.2
Assets				
Net Block	116.2	207.4	214.3	216.4
Capital WIP	41.6	-	-	-
Non-current Investments	0.8	0.7	0.8	1.0
Othe non-current assets	131.4	229.8	267.5	305.5
Loans	-	-	-	-
Inventories	89.2	80.6	111.5	127.4
Trade Receivables	222.0	311.8	384.8	465.0
Cash & Bank Balances	228.8	195.2	172.8	220.2
Loans & Advances	8.5	5.9	6.9	7.9
Other current assets	142.6	225.8	262.9	300.3
Total current assets	691.1	819.4	938.9	1,120.8
Total Current liabilities	370.6	465.7	483.4	539.5
Net Current Assets	320.5	353.7	455.5	581.3
Total Assets	610.6	791.5	938.2	1,104.2

Source: Company, ICICI Direct Research

Exhibit 7: Key Ratios

(Year-end March)	FY21	FY22	FY23E	FY24E
Per share data (₹)				
Reported EPS	22.4	45.1	42.5	50.6
Cash EPS	29.6	54.0	54.5	63.9
BV per share	149.4	190.2	225.2	265.8
Revenue per share	344.7	485.8	565.5	645.9
Cash Per Share	63.5	54.2	48.0	61.2
Operating Ratios (%)				
EBITDA Margin	10.9	14.7	12.5	12.8
EBIT/ Net Sales	8.8	12.8	10.4	10.8
PAT Margin	6.7	9.3	7.5	7.8
Inventory days	26.2	16.8	20.0	20.0
Debtor days	65.3	65.1	69.0	73.0
Creditor days	76.4	53.8	52.0	50.0
Return Ratios (%)				
RoE	15.5	23.7	18.9	19.0
RoCE	20.7	31.0	24.9	24.9
RoIC	32.2	37.7	27.6	28.4
Valuation Ratios (x)				
P/E	22.4	11.2	11.9	10.0
EV / EBITDA	12.4	6.8	7.0	5.9
EV / Net Sales	1.3	1.0	0.9	0.8
Price to Book Value	3.4	2.6	2.2	1.9
Solvency Ratios (x)				
Debt / EBITDA	0.6	0.4	0.5	0.5
Net Debt / Equity	(0.3)	(0.1)	(0.0)	(0.1)

Source: Company, ICICI Direct Research

Key risks to investing in Nano stocks

- Nano stocks may not be in the limelight and inherently being micro cap in nature will have a high risk return profile
- We advise clients to be disciplined in investing at all times. Allocate only a small proportion of your investible income to these stocks and diversify well
- Try to diversify your exposure within the Nano stocks as well by investing equal proportions in several picks
- These stocks may have low volumes and trade infrequently
- Micro cap stocks the world over are, to a large extent, affected by the “Pump and Dump” phenomenon of inflated price buying and depressed price selling
- As explained above, the clients should be patient and trade only through limit orders on any side of the trade
- The risk of volatility remains in such micro cap stocks as they can move up or down with large buy/sell orders
- The fair value of Nano stocks is subject to expected growth potential in the future. Though due diligence has been done to a fair extent, the actualisation of growth still has a degree of uncertainty attached to it

Nano stocks report tries to highlight companies with good and scalable business models, dependable management and sound financials. However, these stocks may not be in the limelight and have a high risk high return potential. Please watch out for the following factors before investing in these stocks:

Allocate a small proportion of your investible income to these stocks and diversify well. If you choose to invest in these stocks, most of your assets allocated towards equity should remain in more stable investments like stocks of large companies. Moreover, try to diversify your exposure within the Nano stocks as well by investing equal proportions in several picks. This will help you avoid losing too much of your total wealth if the investments do not turn out well. When you invest in micro-cap stocks there is a higher risk of impairment.

These stocks may have low volumes and trade infrequently. This can create a situation in which you may not be able to find any willing buyers for your stocks when you wish to sell. We advise our clients to be patient and trade only through limit orders to avoid volatile fluctuations, both while putting a buy and sell order in these stocks.

RATING RATIONALE

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Buy: > 15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: < -15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

**ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com**

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