16th JAN 2024

INITIATING COVERAGE

ETHOS LTD

AXIS SECURITIES

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Initiating Coverage
16th January, 2024

Ethos Ltd
Retail

BUY
Target Price
3,050

Ethos: The Timeless Elegance

We are initiating coverage on Ethos Ltd. with a BUY recommendation and a price target of Rs 3,050/share, representing an upside of 27% from the CMP. Our confidence in Ethos's promising future is grounded in the company's robust and consistent performance over the past several quarters. This trend is expected to persist in the coming years, supported by factors such as consistently strong Same Store Sales Growth (SSSG) of over 15% and an improving EBITDA margins trend, rising from 11.3% in FY20 to 14.5% in FY23. This performance is attributed to the company's continued focus on store expansion and an increased emphasis on growing its exclusive brands portfolio, resulting in an overall Average Selling Price (ASP) increase of 2.2x from Rs 84,200 in FY20 to Rs 187,500 in H1FY24.

With a target of reaching 140-150 stores in the next four years, along with an intensified focus on increasing overall ASP, scaling up the Certified Pre-owned watch segment, and expanding the exclusive brand portfolio, Ethos is expected to achieve healthy Revenue/PAT growth of 35%/42% CAGR, respectively, over FY23-26E. This growth trajectory is anticipated to elevate the company's Return on Capital Employed (ROCE) from 16% in FY23 to 20% in FY26.

Investment Thesis

Structural growth trend in the Luxury space

India is at the cusp of a luxury demand boom. According to some estimates, the Luxury market in India will expand 5x in the next decade as the number of affluent consumers in the country continues to multiply with higher aspiration and disposable income. In recent years, the sales of luxury products have been at an all-time high in many luxury segments including luxury cars (up 3x), luxury real estate (up 2x), Premium clothing, etc. Moreover, The demand for luxury products is not restricted to metros but also has extended to Tier 2 and 3 cities. This represents an unprecedented opportunity for retailers of premium and luxury products like Ethos.

Ethos is embracing the transformation for the next leg of growth

- **Foraying into the fast-growing Certified Pre-Owned (CPO) segment** due to the shortage of new luxury watches is a step in the right direction. CPO is an asset-light model. It has lower Capex and requires a lower working capital cycle of 50-60 days vs. 140-150 days for new watches. As a result, it has a higher ROCE of 20%+ vs. 15-18% for new watches.
- **Increasing share of high-margin exclusive brands in the portfolio** is expected to drive the overall margins profile, given that these brands command 2x gross margins (~35-40%) compared to non-exclusive brands. As of now, exclusive brands contribute ~ 30% to the sales, a figure that is projected to rise in the coming years.
- **Diversifying into fast-growing other luxury segments such as Luggage (Rimowa) and Jewellery (Messika and Bvlgari)** though the company is at a nascent stage in this segment, it is staging for future growth as it could be its next growth driver.
- **Room for margin and ROCE expansion:** We expect the company's EBITDA margin to expand 100bps to 15.6% by FY26E from 14.5% in FY23, led by 1) Improving product mix – gradual increase in the ASP and exclusive brand portfolio, 2) Store expansion and operating leverage, and 3) Increasing CPO business further improving the company's ROCE from 16% in FY23 to 20% in FY26E.

Valuation & Recommendation

Given the investment thesis outlined above, we anticipate robust CAGR growth for the company in terms of Revenue (35%) and PAT (42%) over FY23-26E. This positive trajectory is expected to enhance the overall return profile for the company. Currently, at the CMP, the company is trading at 44x/32x its FY25/26E EPS. With improved visibility in earnings growth and a stronger return profile, the stock appears attractive within the Small-cap space. **We initiate the coverage on Ethos Ltd. with a BUY rating and value the company at 40x FY26 EPS to arrive at a TP of Rs 3,050/Share, implying an upside of 27% from the CMP.**

Key Financials (Consolidated)

(Rs Cr)	FY23	FY24E	FY25E	FY26E
Net Sales	789	1,085	1,462	1,931
EBIDTA	114	168	227	301
Net Profit	60	88	124	171
EPS, Rs	26.6	39.1	55.1	76.2
PER, x	90	61	44	32
EV/EBITDA, x	46	32	23	18
ROE, %	9	12	15	17

Source: Company, Axis Research

CMP as of 15th Jan, 2024

CMP (Rs)	2406
Upside /Downside (%)	27%
High/Low (Rs)	2410/918
Market cap (Cr)	5,891
Avg.daily vol '000.(6M) Shrs	73.018
No. of shares (Cr)	2.5

Shareholding (%)

	Jun-23	Sep-23	Dec-23
Promoter	63.8	63.8	57.9
FII	6.5	6.7	10.4
MF's/UTIs	8.2	7.6	9.9
FI's/Banks	0.0	0.0	0.0
Others	21.5	21.9	21.8

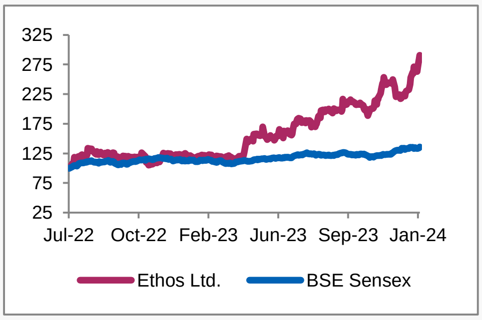
Financial & Valuations

Y/E Mar (Rs Cr)	FY24E	FY25E	FY26E
Net Sales	1,085	1,462	1,931
EBIDTA	168	227	301
Net Profit	88	124	171
EPS, Rs	39.1	55.1	76.2
PER, x	61	44	32
EV/EBIDTA, x	32	23	18
ROE, %	12	15	17
Debt/Equity (%)	0.2	0.1	0.1

YoY Growth in %

Y/E Dec	FY24E	FY25E	FY26E
Net Sales	37.6%	34.7%	32.1%
EBITDA	46.6%	35.4%	32.5%
Net Profit	47.2%	40.9%	38.2%

Relative performance



Source: Ace Equity, Axis Securities

Preeyam Tolia
Research Analyst
email: preeyam.tolia@axissecurities.in

Suhanee Shome
Research Associate
email: suhanee.shome@axissecurities.in

Financial Story in Charts

Exhibit 1: Revenue is expected to grow 35% CAGR over FY23-26 with store expansion and SSSG growth of 12-15%

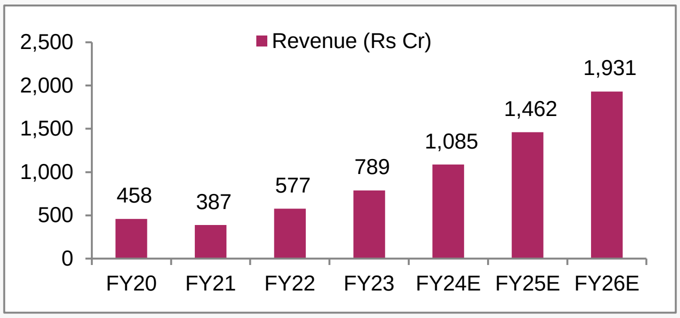
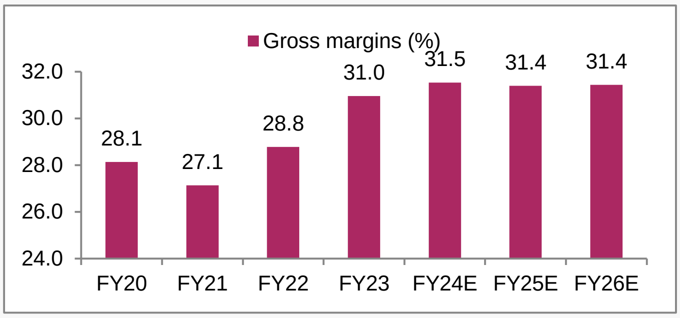


Exhibit 2: Increase share of high-margin premium watches will drive gross margins



Source: Company, Axis Securities

Exhibit 3: EBITDA margins are likely to improve due to strong operating leverage

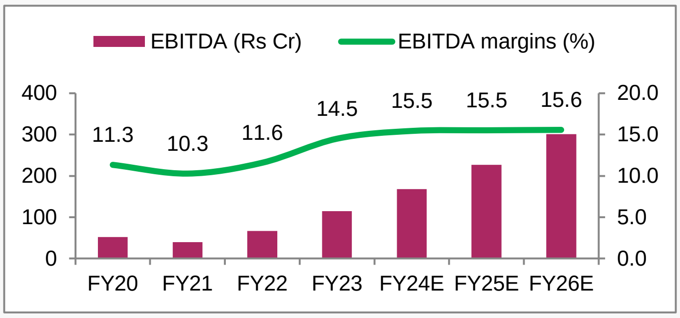
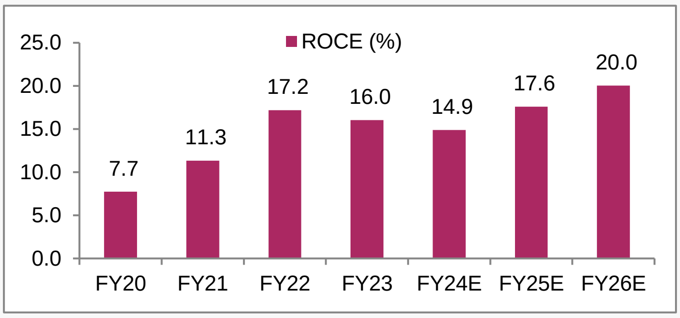


Exhibit 4: Increasing share of CPO and strong operating efficiency will drive overall ROCE



Source: Company, Axis Securities

Exhibit 5: Focus on the premium and luxury segment has driven overall ASP

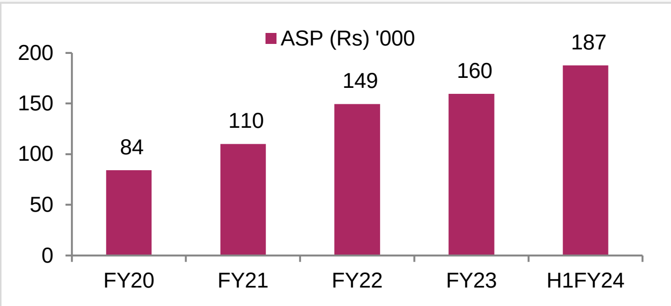
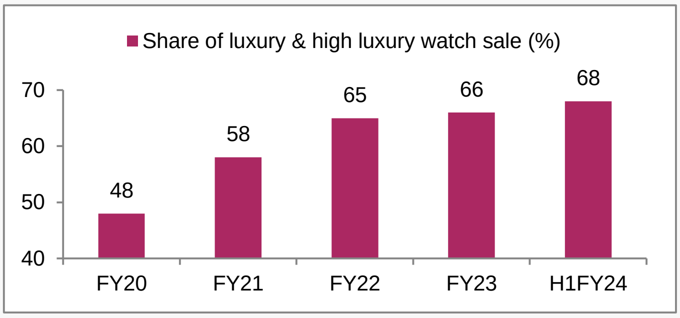


Exhibit 6: Increasing share of premium and luxury segment, driving margins



Source: Company, Axis Securities

Exhibit 7: Increasing the share of CPO is a step in the right direction

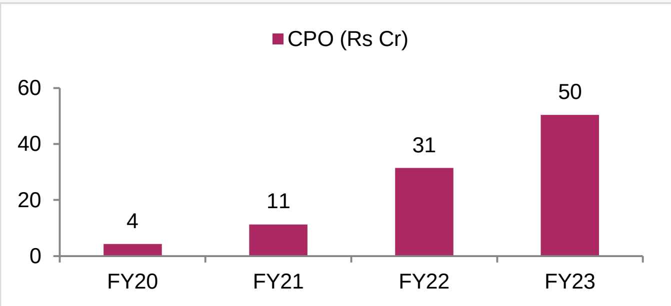
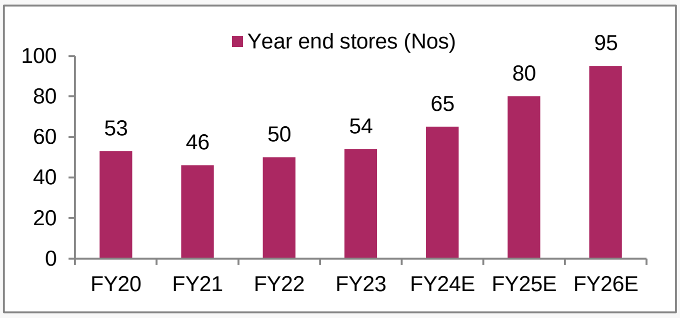


Exhibit 8: On an expansion spree….



Source: Company, Axis Securities

Company Overview

Ethos Ltd was established in 2003 and is one of India's largest luxury and premium watch retailers. It has a 20% market share in the luxury segment and 13% in the premium watch segment. The company is a subsidiary of KDDL and has a presence in 23 cities in India with 60+ stores.It also has an omnichannel presence and offers products through its websites (www.ethoswatches.com&www.scondmovement.com) and social media platforms.

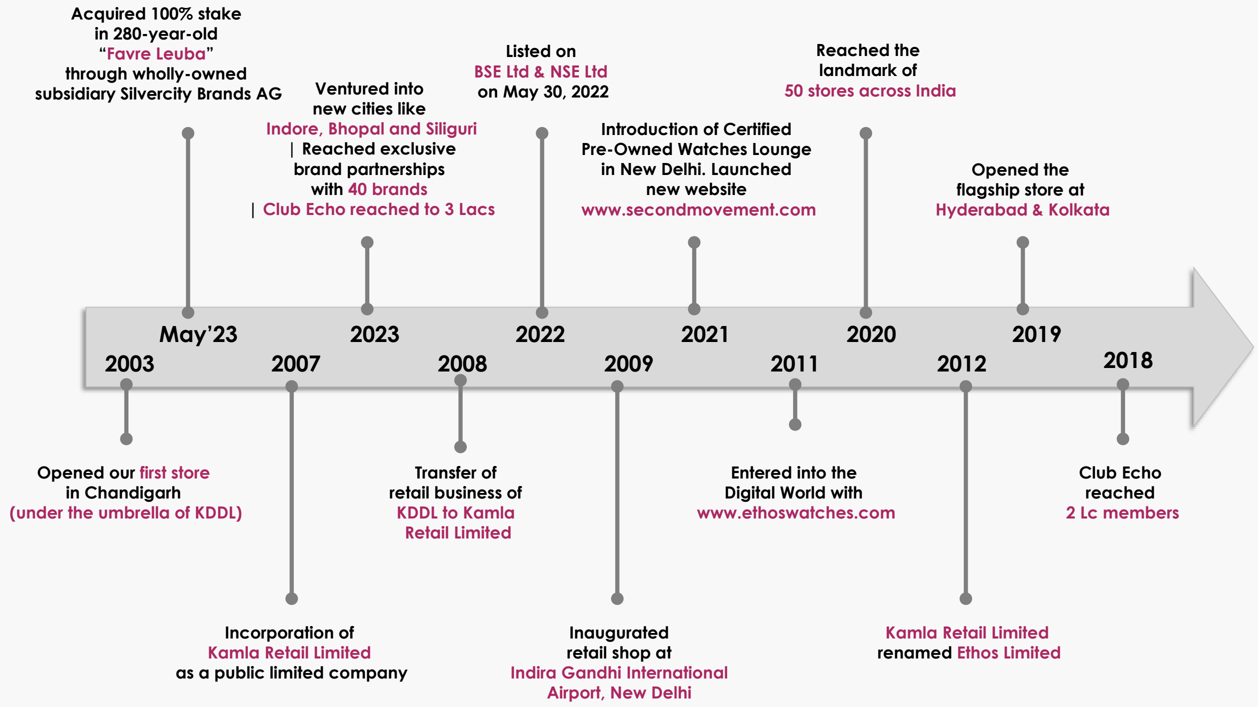
- *India's largest luxury and premium watch retailer.*
- *Ethos has 20% market share in Luxury segment.*
- *Portfolio of 46 exclusive brands.*

In India, the company caters to over 60+ premium and luxury watch brands, which includes 46+ exclusive brands that are available exclusively at Ethos. It has over 7000 SKUs of premium, bridge to luxury, luxury and high-luxury watches. Some of the notable brands include Rolex, Breitling, Omega, Frederique Constant, Jacob & Co, Ulyssse Nardin, etc. Furthermore, in May'23, Ethos acquired a 100% stake in 280-year-old "Favre Leuba" through its wholly-owned subsidiary Silvercity Brands AG.

Ethos is a market leader in the Certified Pre-Owned (CPO) luxury watch market where the company sells and buys pre-owned luxury watches providing a 360 inspection and verification of watches with a certified two-year warranty.

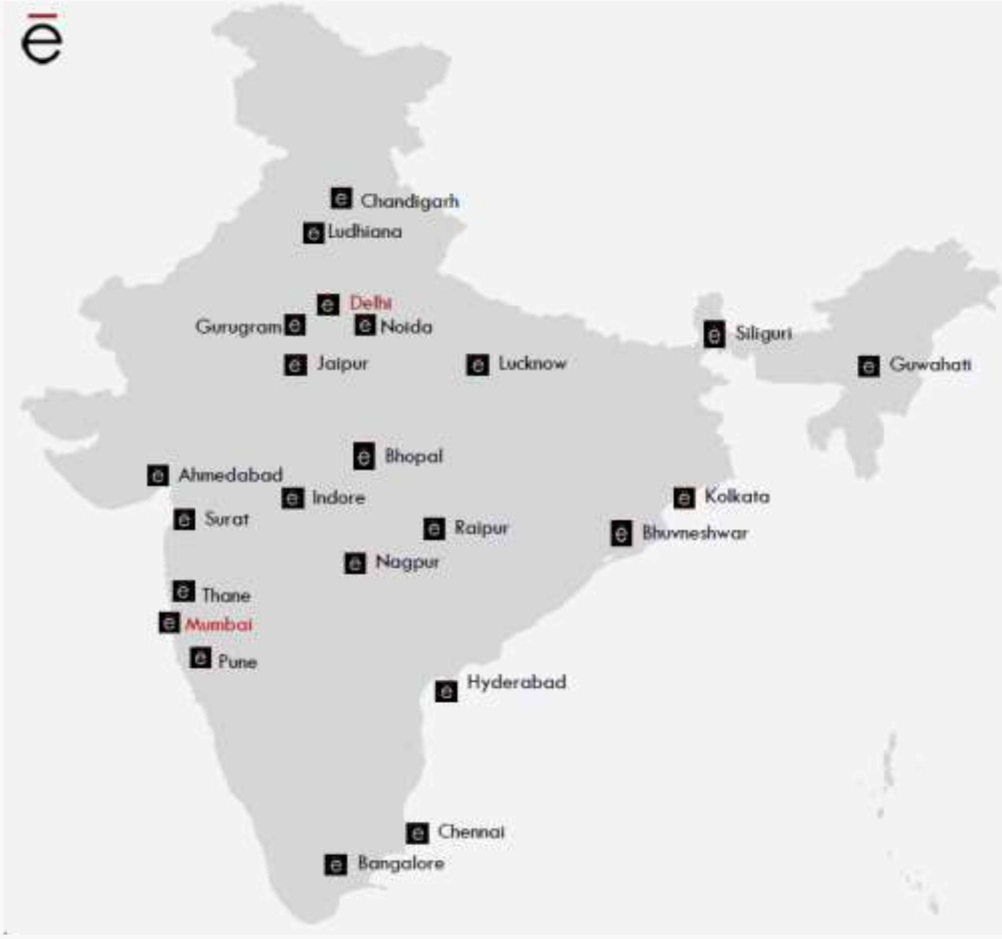
To diversify into other luxury categories, Ethos has signed a partnership agreement with Messika & Bvlgari and Rimowa to sell their high-end jewellery and travel accessories in India.

Exhibit 9: Key Milestones



Source: Company, ASL

Exhibit 10: Presence across 23 cities in India



Source: Company, ASL

Strong Business Model

A. strong product portfolio provides a long-term sustainable advantage

Ethos caters to over 60+ premium and luxury watch brands in India and still adding, which includes 46 exclusive brands that are available exclusively at Ethos. It has over 7000 SKUs (the largest amongst its peers) of - premium, bridge luxury, luxury and high-luxury watches. Ethos has ~20% market share in the organised luxury watch segment and ~13% in the overall watch market, much of the success is attributed to its promoter group company - KDDL Ltd (est. 1981) where it has developed long-term relations with global watch brands by exporting watch dials, thereby gaining valuable insights in the watch industry, which has been instrumental in building strong relationships with global luxury watch brands.

Typically, the company earns retailer margins of 20%-25% in the premium watches range, 25%-28% in the bridge-to-luxury segment, and 20%-35% in the luxury & above segments.

Exhibit 11: Ethos mainly caters to the luxury watch segment and is gradually reducing focus on Rs <50,000 segment

		Market size (Rs Cr)			
Segment	**Definition**	**FY20**	**FY25E**	**CAGR (%)**	**SKUs***
Premium watch market	Premium (Rs < 1 L)	3,370	5,950	12%	973 (19%)
Luxury watch market	Bridge to Luxury (Rs 1 L to 2.5 L)	1,700	3,133	13%	1510 (29%)
	Luxury (Rs 2.5 L- 10 L)	810	1,492	13%	1730 (33%)
	High Luxury (Rs > 10 L)	540	1,040	14%	1011 (19%)

Source: Company RHP, ASL, *SKU as on 4th Jan, 2024 – www.ethoswatches.com

Elaborate store network and strong omni channel presence

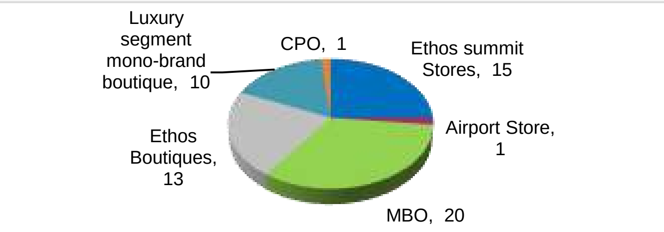
Ethos outright purchases watches from brands and sells them through its expansive store network across metros, tier-1/2/3 cities along its own website. Currently, Ethos has 60+ stores and operates two sets of store formats – MBO (Multiple Brand Outlets) and Exclusive Brand Outlets. The MBO stores are typically 1000-2500 sq.ft stores and are named– Ethos and Ethos Summit stores, the summit stores start with a portfolio that is higher in price point and the Ethos stores are mid to high price point stores.

To bolster its omni channel presence, the company has the backing of an in-house digital team comprising over 70 individuals, including trained watch specialists. Additionally, there are 25 online luxury watch consultants dedicated to addressing customer queries that come through the online portal. This setup aids customers in their research and decision-making process when selecting a watch.

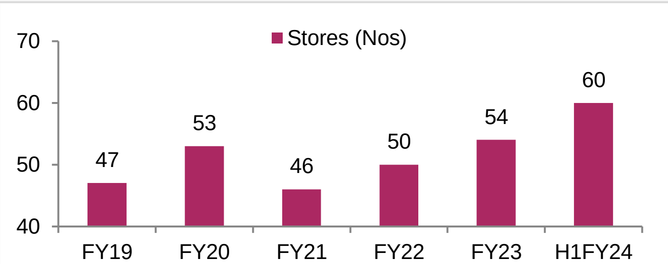
Going omni-channel has helped the company in several ways – 1) It can offer customers a vast catalogue of ~5,000-7,000 SKUs of collection to choose from which otherwise not be possible in physical stores, 2) It helps expand a larger customer base and reach into smaller towns where purchasing power of luxury products is increasing and, 3) It enables them to collect rich database of customers.

A typical 1,000 sq.ft store requires a Capex of Rs 6-6.5Cr (Rs 1.2 Cr in Capex + Rs 5 Cr in inventory) and normally the stores achieve break-even in the same year. On the other hand, it has a payback period of three years including inventory. The majority of the stores are in malls and hence Ethos has to depend upon the schedule of opening of the new malls.

Exhibit 12: Ethos is present across formats



Store count by format - H1FY24 (Nos)

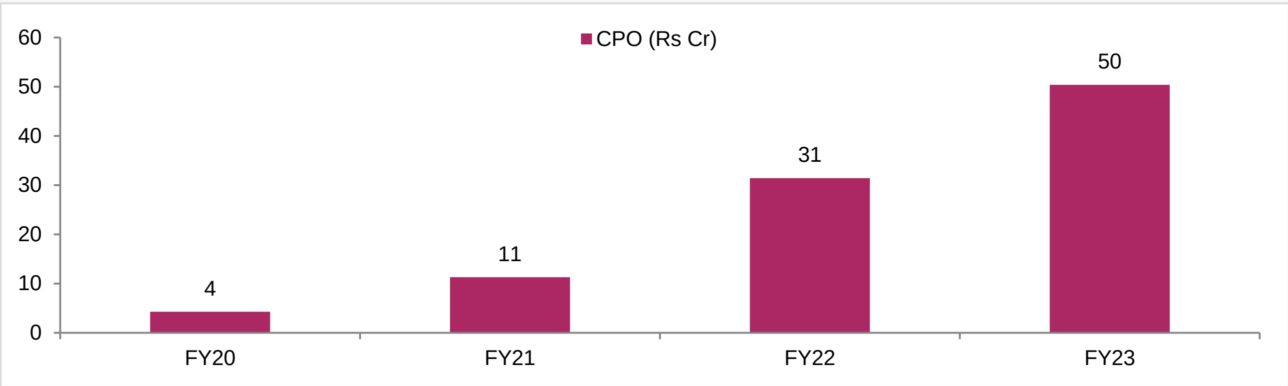


Source: Company, Axis Securities

Certified Pre-Owned (CPO) segment

In addition to retailing new premium & luxury watches, Ethos has ventured into the Certified Pre-Owned (CPO) luxury watch & bags (pilot) market in India in 2019. Under the CPO model, the company buys and sells pre-owned watches. Globally it is one of the fastest-growing models in the luxury watch space, mainly driven by a shortage in the new luxury watch market. Ethos had a first-mover advantage in India and has a dedicated CPO luxury watch lounge in New Delhi while it also operates through www.secondmovement.com. The company purchases watches from genuine sellers and after an extensive process of investigation, validation and refurbishment by expert watchmakers at a cutting-edge technical facility, puts them up for sale. The sale is supported by certification and a two-year warranty. Ethos reported Rs 50 Cr (6% of sales) in FY23.

Exhibit 13: CPO is expected to be the next growth driver for the company

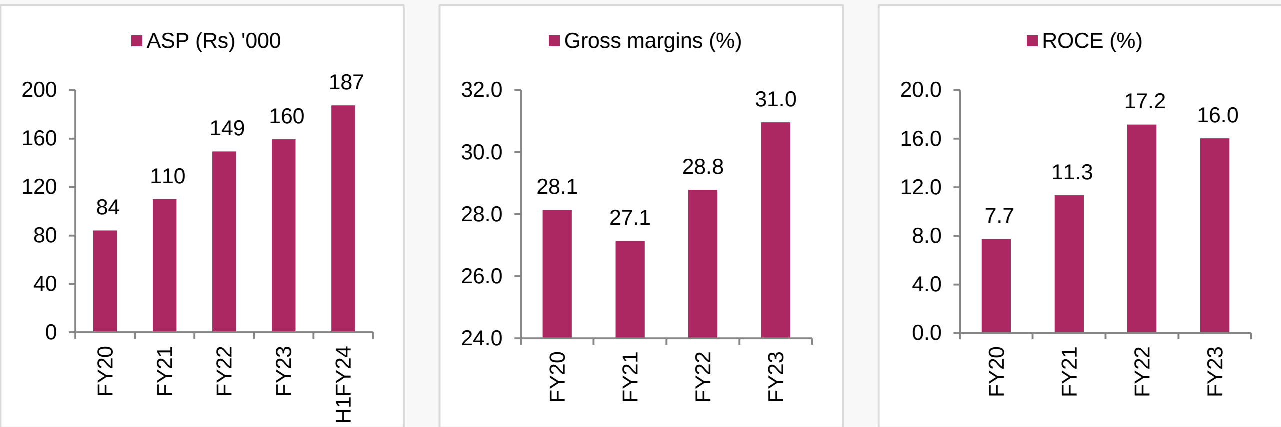


Source: Company, ASL

Driving premiumisation, leading to superior margins and return profile

The company's Q2FY24 SSSG stood at 23% (~24% in H1FY24) vs. 30% in H1FY23. It is still strong compared to the overall slowdown in the retail industry and most of the growth is attributed to an increase in Average Selling Price (ASP) which currently now stands at Rs 1,87,500. The company undertook strategic initiatives a few years back to defocus the watches that are priced at Rs <50,000 and focus on watches that are Rs >50,000 as competition in the former price point is higher. Hence, over FY20 and H1FY24 its ASP increased 2.2x from Rs 84,200 in FY20 to Rs 1,87,500; a realization growth of 22% CAGR. The increase in ASP has further led to its gross margin expansion which improved 210bps from 28.1% in FY20 to 31% in FY23.Consequently, its ROCE improved from 9% in FY20 to 17% in FY23,thanks to the company's premiumisation strategy.

Exhibit 14: Best-in-class margins and return profiles over the years



Source: Company, ASL

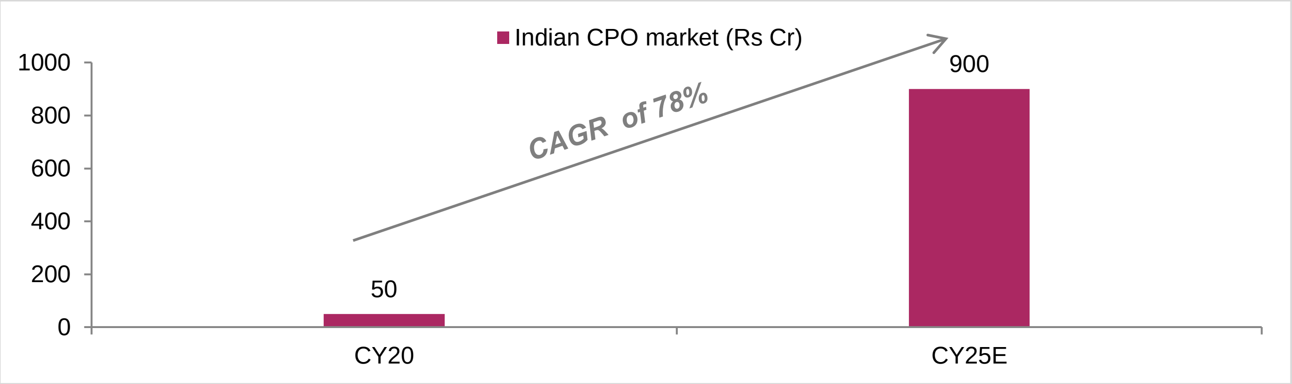
Key Growth Drivers

A. Certified Pre-Owned segment – Key growth driver for the company in coming years

The globally organized Certified Pre-Owned (CPO) Luxury Watch market was valued at $18Bn in CY20. It is expected to grow at 9% CAGR from CY19 to CY25 to reach $27 Bn. Furthermore, the contribution of the overall CPO market to the Premium and luxury watch market globally is expected to reach 46% in CY25 from 33% in CY20.

The Indian CPO market had a slower start and it is increasing the pace. The Indian luxury Pre-owned/CPO market was valued at ~Rs 40-50 Cr in FY20, which was largely dominated by the unorganized sector, contributing almost 80% of the market. On the other hand, the organised CPO market was valued at ~Rs 10-15 Cr in FY20 and growing at 30% CAGR. In comparison, the overall premium & luxury watch market in India was valued at Rs 6,610 Cr in FY20, making the Indian CPO market only ~0.2% of the Overall Premium & Luxury watch market and provide huge scope for market expansion.

Exhibit 15: Indian CPO market is expected to grow at 78% CAGR over CY20-25E, organised CPO is expected to account for 75% of the total CPO market from its current share of 25%-30%.



Source: Company RHP, ASL

Certified Pre-Owned (CPO) Business Achieves 61% YoY Revenue Growth in FY23: Ethos entered the Certified Pre-Owned (CPO) business in 2019, securing a first-mover advantage in the organized CPO market, which remains largely unorganized in India. In FY23, Ethos reported revenue growth of Rs 50 Cr (constituting 6% of sales), marking a remarkable 61% YoY increase and achieving an impressive CAGR of 127% over FY20-23. The company anticipates strong growth momentum for the CPO business in FY24, driven by sustained demand for pre-owned luxury watches.

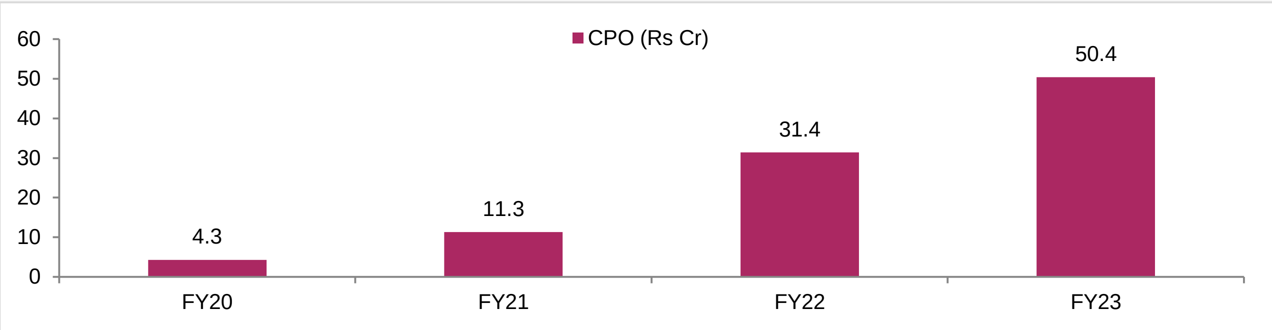
Ethos conducts CPO watch sales through its website, www.secondmovement.com, and operates a dedicated CPO luxury watch lounge in New Delhi. While management notes that this business doesn't require many stores to operate hence planning to add miniscule store, it will be opening the next store in Mumbai and an additional 1-2 stores in other metro cities in the coming years.

Media reports highlight key growth drivers for pre-owned watches, including:

- A prolonged waiting period, sometimes exceeding a year, for luxury watches in the primary market due to short supply, whereas there is no waiting period in the secondary market.
- The boom in demand for second-hand luxury watches in recent years, with popular brands like Rolex, Patek Philippe, Cartier, and Omega commanding high resale values due to shortages. Some luxury watches can yield an average annual return of 11-15%, turning them into an alternative asset class for certain investors.
- The provision of an entry point for the new High Net Worth Individual (HNI) consumer class, particularly in the age group of 18-30 years. The secondary market serves as a destination for the first-time purchase of luxury watches, and it's estimated that this age group will contribute 50-60% of pre-owned luxury watch sales by 2030.

While retailing pre-owned watches carries lower gross margins of 20-25% compared to over 30% in new watches, it requires lower capital expenditure (Capex) and has a shorter working capital cycle of 55-60 days, as opposed to 140-150 days for new watches. Consequently, it boasts a higher return profile (ROCE) of over 20%, surpassing the 15-18% range for new watches.

Exhibit 16: Robust Short-term Outlook



Source: Company, ASL

Why Ethos is well-placed in the CPO market?

The pre-owned watch segment poses challenges due to the meticulous examination required for each watch before purchase or sale. This demands in-depth knowledge of watch brands, and the refurbishing process necessitates the skills of watchmakers—a resource not readily available in India due to the loss of the mechanical watch manufacturing tradition after HMT ceased its operations.

Ethos has addressed this challenge by implementing a robust training program. Watchmakers undergo specialized training abroad, enhancing their expertise in refurbishing watches. However, the scarcity of watchmakers remains a constraint. Currently, Ethos boasts 17 watchmakers with proficiency in watch refurbishment, and the company is committed to ongoing efforts to expand this workforce through training initiatives.

This shortage of skilled manpower parallels challenges seen in the jewellery business, where India faces a scarcity of skilled/traditional 'Karigars,' renowned in the jewellery industry. In response to this crisis, Titan, for instance, took the initiative years ago to provide comprehensive training and create an optimal working environment for Karigars.

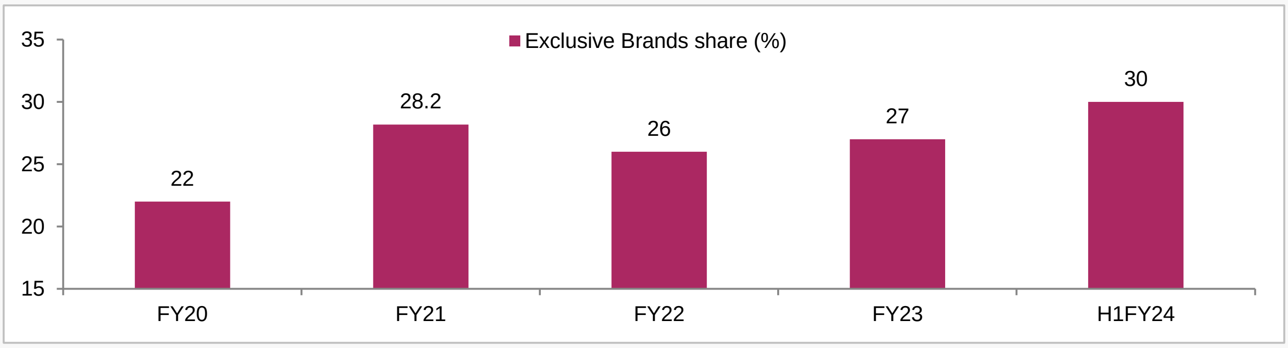
How does the Outright Purchase Model work (buying from the seller)?

- Ethos purchases watches only from India does not import and has a dedicated team of Watch-Specialists.
- Seller posts the information about the watch they need to sell along with pictures to the Ethos online portal and other channels
- Based on details provided by the seller, Ethos shares the quote within 24 hours and if the seller agrees, the watch consultant reaches out to the seller to have the watch collected for physical examination.
- Upon receiving the watch, the watch will be inspected for its physical condition and authenticity (smuggled, fake, etc.) to finalize the purchase.
- Once the watch passes the inspection, the fund is transferred to the seller
- Tricky parts - some of the watches need restoration which requires ordering spare parts which becomes trickier for old watches. It can take 4-6 weeks for restoration and after restoration and testing, the watch is certified by Ethos.
- Typically when the watch is listed on the website it sells within 30 days.

B. Increasing the share of Exclusive Brands will provide a sustained competitive advantage over the long-term

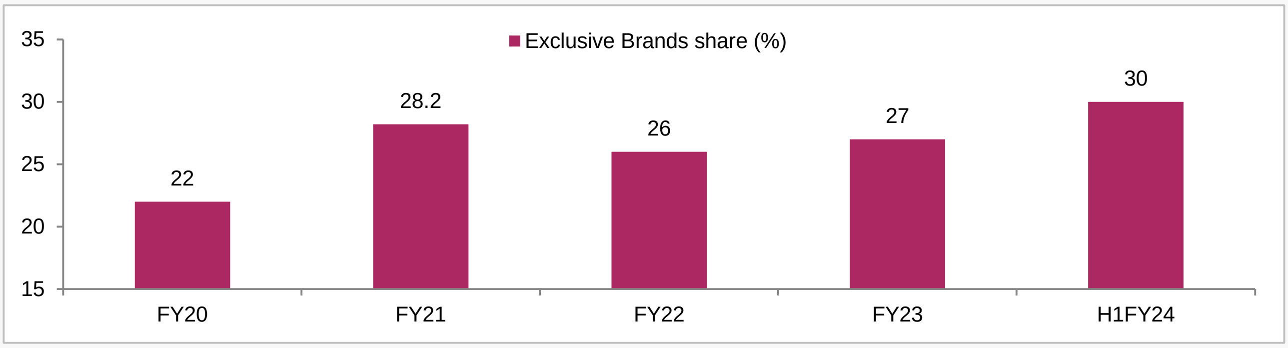
Ethos has 60 brands in the portfolio out of which ~42 brands are exclusively available to Ethos, which contributes ~30% of the sales. Ethos is in constant endeavour to increase the share of exclusive brands portfolio. Over FY19-23, the exclusive brand contribution has increased from 22% in FY20 to 30% in H1FY24. Typically, exclusive brands carrya 2x gross margin (35-40%) compared to non-exclusive brands. As the company endeavours to increase the share of exclusive brands, we expect it will help the company to increase its margins profile.

Exhibit 17: Exclusive brand is key for long-term sustainable growth



Source: Company, ASL

Exhibit 18: Exclusive brand carries higher margins which will drive the overall gross margin profile of the company in the coming years



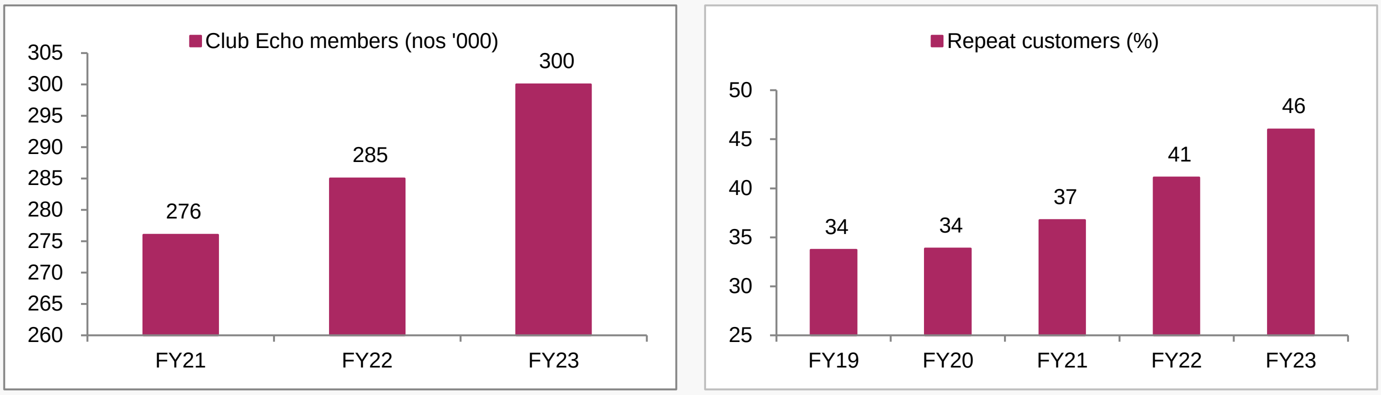
Source: Company, ASL

Strategic Advantage: Exclusive Tie-Ups and Customer Loyalty at Ethos Ltd

Exclusive tie-ups play a pivotal role in creating distinctive value propositions, particularly when targeting High Net Worth Individuals (HNIs) and ultra-HNI clients. These partnerships not only enhance negotiating power with luxury watch brands but also position retailers uniquely. Ethos, with its extensive store network and a substantial customer database of approximately 0.3 Mn HNI clients, emerges as an ideal partner for luxury brands.

Over the years, Ethos has meticulously built a robust customer database, primarily through its flagship membership program, Club Echo, active for 14 years. This initiative has yielded a wealth of customer data, providing invaluable insights into buying behaviour. Club Echo not only aids in understanding customer preferences but also cultivates loyalty through incentive schemes, driving repeat purchases. Additionally, it proves instrumental in reducing servicing costs by enabling effective and timely communication with customers. This strategic approach underscores Ethos's success in the luxury watch market.

Exhibit 19: Club Echo provides a huge client database, making Ethos an ideal partner and facilitating repeat purchases



Source: Company, Axis Securities

Exclusive partnership is a win-win for retailers as well as brands

Exclusive brand partnerships help the brands in curating the products as per local taste and preference based on retailers' knowledge of core markets which leads to faster adoption and visibility of the new brands entering into the country.

Case in point –

1) **Faster store expansion –** Ulysee Nardin which is well known in India and has been present in India for nearly two decades has partnered with Ethos to strengthen its presence in the rapidly growing Indian luxury watch market.
2) **India-specific launch –** Jacob & Co launched an exclusive 11-piece Jacob Steel Epic X collection for the launch of the Boutique store priced at Rs 26 Lc/watch sold out in 36 hours.Subsequently,a gold edition of this collection was launched with a price tag of Rs 56 Lc/watch which was expected to be sold out in the same month. Moreover, Jacob & Co launched its most popular Astronomia collection in India called Astronomia Art India which had four hand-graved and hand-painted Indian monuments – the Taj Mahal, Lotus Temple, The India Gate and The Qutub Minar in the dial.

Exhibit 20: Jacob & Co. undertook a localized approach to enter into Indian market – (1) Jacob Steel Epic X, (2) Astronomia

Source: www.ethoswatches.com

Preferred Partner in Luxury: Ethos's Strategic Edge in Watch Brand Collaborations**

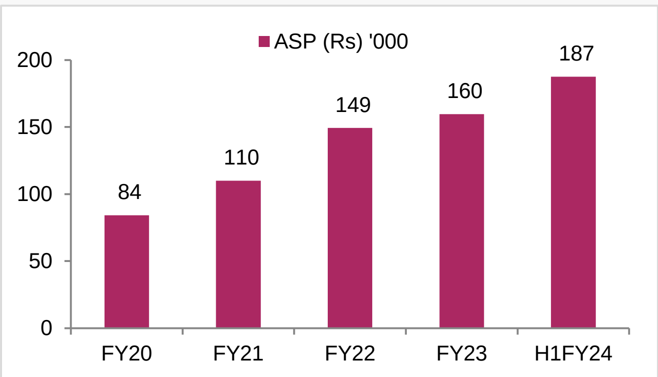
As the demand for luxury watch brands surges in India, there's a growing trend among these brands to seek partnerships with local retail players. Ethos, with its extensive track record in dealing with some of the world's most prestigious watch brands and a widespread store network across India, is poised to emerge as the preferred partner for many. This strategic advantage positions Ethos as a frontrunner in fostering collaborations with an array of luxury watch brands aiming to tap into the flourishing Indian market.

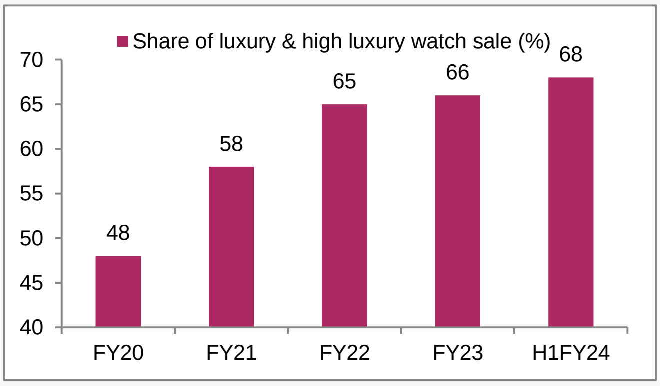
C. Focus on increasing share of premium and luxury watches driving overall ASP for the company

Embracing a strategic shift three years ago, Ethos adopted a cautious approach by gradually steering away from the fashion segment (below Rs 50,000) towards higher price points (above Rs 50,000). This deliberate move has posed challenges to volume growth in recent quarters. However, the Average Selling Price (ASP) has seen a remarkable doubling, soaring from Rs 84,200 in FY20 to Rs 187,500 in H1FY24, marking a substantial 22% Compound Annual Growth Rate (CAGR). This calculated shift was propelled by factors such as heightened competition in the Rs 25,000-50,000 range, increasing smartwatch prevalence, constraints in shelf space within stores, and the allure of limited competition in the rapidly expanding luxury segment.

Ethos still sells watches under Rs <50,000 online, however, it highlighted that going ahead it will keep the right balance between entry-level and luxury watches as it penetrates into smaller towns. We believe ASP is likely to increase on a steady basis as it introduces more premium and exclusive brands to the portfolio.

Exhibit 21: ASP has seen an increasing trend as the share of luxury watches increases





Source: Company, Axis Securities

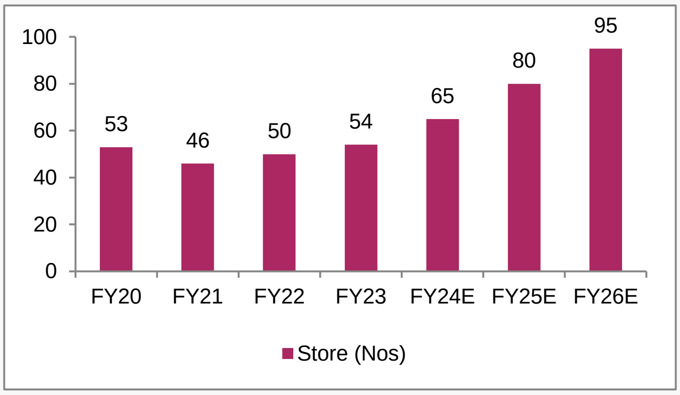
D. On an expansion spree…

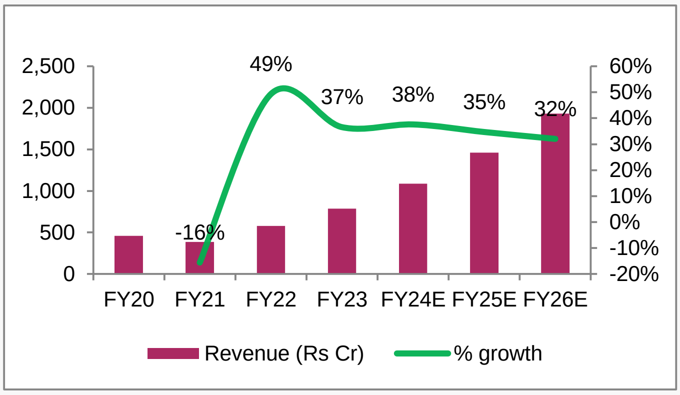
As of Q2FY24, Ethos operates 60 stores across 23 cities, primarily in metros and tier-1 cities. A strategic shift is underway as the company aims to establish a presence in smaller Tier 2/3 and suburban areas, where increasing purchasing power is driving demand for premium and luxury brands, recent store openings in Siliguri, Bhubaneshwar, Raipur, and Surat reflect this strategy. The store expansion plan has been revised to reach 145-150 stores in the next four years, up from the earlier target of 75 stores.

A recent successful QIP raised Rs 175 Cr, adding to the cash balance of Rs 180 Cr as of H1FY24, providing a strong financial position for expansion. Despite flat additions in H1FY24 due to delayed mall openings, confidence in accelerated guidance stems from the profitability of all recently added stores, some achieving profitability in the third month of operation. Ethos anticipates robust store openings in H2FY24. With an increased store opening guidance and a projected 12%-15% same-store sales Growth (SSSG) vs. the previous 8-9%, the company expects sustained and improved SSSG for new outlets over the next 7-10 years.

In the case of Chandigarh, the luxury market wasn't robust seven to eight years ago. Ethos initially sold mid to high-price point watches but not at the very high end. Over the years, as the market evolved and purchasing power increased, Ethos strategically added more high-priced brands. Today, after 15 years, Chandigarh continues to exhibit high Same Store Sales Growth (SSSG).

Exhibit 22: Ethos is on an expansion spree, thus driving sustained revenue growth





Source: Company, Axis Securities

E. Favre Leuba – Can it rejuvenate the 286-year-old brand?

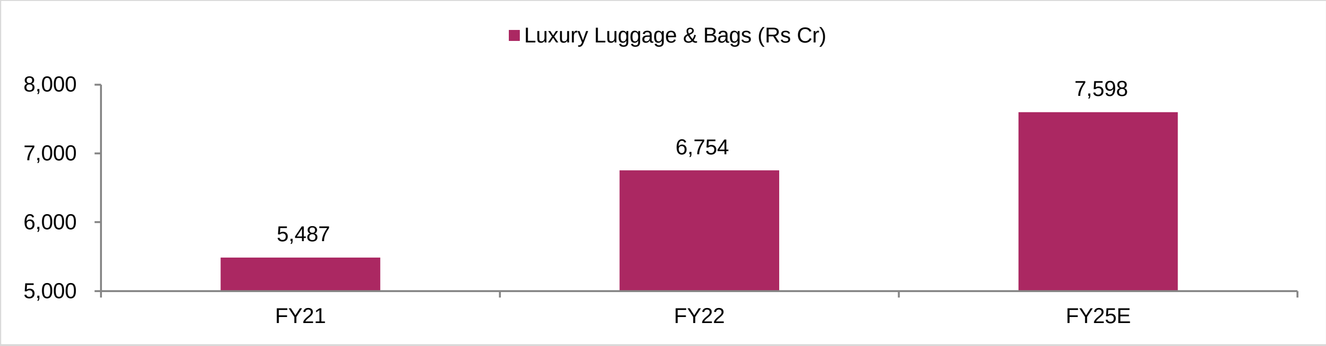
Favre Leuba is the second-oldest Swiss watch brand in the world, established in 1737, with over 286 years of heritage. Ethos, through its subsidiary Silvercity Brands AG, acquired a 100% stake in Favre Leuba Gmbh in May'23.

Please note, that Titan first acquired Favre Leuba in 2011 for Rs 14 Cr. While Titan tried to revive the brand by investing cumulatively Rs 275 Cr, by the end of 2020, it announced scraping the brand. However, Ethos is confident of reviving the brand and working towards a global launch of the brand in FY25. Being a Swiss brand, Ethos is likely to operate the entire marketing strategy and production of Favre Leuba in Switzerland. As per the management, the brand has huge potential in India and the company is well-placed to rejuvenate the brand after Titan failed to revive the brand in India.

F. Spreading its wings into other luxury categories

Luxury Luggage - The company has entered into the luxury luggage segment by entering an exclusive agreement with LVMH's Rimova, the brand that is in the luxury luggage segment. It opened its first store in Oct'23 and plans to open a few more stores in the coming years. Globally Rimowa has done $1 Bn in revenue.

Exhibit 23: Indian Luxury luggage and Bags market is expected to grow 8.5% CAGR over FY21-25



Source: Company, Axis Securities

2) Luxury Jewellery - Ethos launched a high-end luxury jewellery range from Messika and Bvlgari (recently added).Currently, the segment is in the pilot stage; however,the company expects the branded luxury jewellery category could be the next growth driver. Margins in the jewellery business are slightly higher than in watches.

The untapped potential of the Indian market for international luxury jewellery is gaining recognition among brands and retailers. Tiffany & Co., an esteemed international luxury jewellery brand, ventured into the Indian market in Jan'20 through a partnership with the Reliance group, inaugurating its flagship store at New Delhi's luxury mall, The Chanakya. Tiffany & Co. further expanded its presence by launching its e-commerce brand website in Oct'21. Similarly, Cartier offers its jewellery through exclusive stores, showcasing a diverse range of categories such as Watches, Eyewear, Leather goods, and Fragrances, among others. This trend extends to other luxury jewellery brands like Hermes, Chopard, and BVLGARI.

Currently, this market holds a potential for Vertical specialists like Ethos dealing in Watches as a primary category.

Case in point - The Watches of Switzerland Group is a global retailer of luxury watches with partnerships with brands like Rolex, Patek, Philippe, Audemars Piguet, Cartier, Omega, Tag Heuer, Breitling and Tudor. The group has a leading market position in the UK market and has established its presence in the USA too. It has 211 stores as of H1FY24

The brand, primarily positioned as a Luxury watch retailer, is now a key player in the adjacent category of Luxury Jewellery. As of H1FY24, 88% of its revenue came from Luxury watches, ~6% from Luxury Jewellery, and ~6% from 'Others' including Fashion and classic watches and jewellery, sale of gifts, servicing, repairs and insurance. The group has partnered with Luxury Jewellery brands like Messika, Gucci, Bvlgari, Mikimoto, Chopard, Roberto Coin,FOPE etc. and has established itself as the largest jewellery retail firm in the UK.

Exhibit 24: Indian Luxury luggage and Bags market is expected to grow 8.5% CAGR over FY21-25

Source: Company, Axis Securities

Exhibit 25: Indian Jewellery & Accessories market is expected to grow at 11% CAGR over FY21-25

Source: Company, Axis Securities

Outlook & Valuation

India is poised for a surge in luxury demand, with projections suggesting a fivefold expansion in the luxury market over the next decade. The growing number of affluent consumers, driven by increased aspirations and disposable income, has led to record-breaking sales in various luxury segments such as vehicles, real estate, and clothing. Notably, this surge is not confined to metropolitan areas but also extends to Tier 2 and 3 cities. This presents an unparalleled opportunity for premium and luxury product retailers like Ethos.

We believe Ethos ticks all the boxes to take advantage of the structural story in the Indian Luxury space

- **Stellar Performance:** Robust SSSG, Expanding EBITDA Margins, and Enhanced ROCE from FY20 to FY23: Its ability to showcase consistently strong SSSG (+20%) and improving EBITDA margins trend - 11.3% in FY20 to 14.5% FY23 led by continued focus on driving store expansion and increase focus on increasing share of exclusive brands portfolio thus driving overall ASP by 2.2x from Rs 84,200 in FY20 to Rs 187,500 H1FY24 and hence subsequently it has seen ROCE improvement from 8% to 16% over FY20-23, which is likely to further increase in coming years.
- **Strategic Expansion:** Capitalizing on the Certified Pre-Owned (CPO) Market with Diversification into Luxury Bags: Foraying into the fast-growing Certified Pre-Owned (CPO) segment due to the shortage of new luxury watches is a step in the right direction. CPO is asset light model it has lower Capex and a lower working capital cycle of 50-60 days vs. 140-150 days for new watches as a result it has higher returns of +20% vs. 15-18% for new watches. Currently, the majority of revenue in CPO comes from watches, however recently it has also forayed into the luxury CPO bags segment.
- **Enhancing Margins:** Strategic Emphasis on High-Margin Exclusive Brands: Increasing the share of the high-margin exclusive brands' portfolio will drive the overall margins profile as it carries 2x gross margins (35-40%) compared to non-exclusive brands. Currently, exclusive brands contribute ~30% of the sales which is likely to increase in coming years.
- **Diversification Drive:** Expanding Portfolio to Include Luggage and Jewellery: Diversifying into fast-growing other luxury segments such as Luggage (Rimowa) and Jewellery (Messika and Bvlgari) though at a nascent stage, however, it is staging for future growth as it could be the next growth driver for the company. Globally, Watches of Switzerland has seen decent success in scaling up the Luxury Jewellery category.
- We expect the company to deliver healthy Revenue/EBITDA/PAT growth of 35%/38%/42% CAGR over FY23-26E respectively, which will lead to the overall return profile for the company going up. We expect its ROCE to increase from 16% in FY23 to 20% in FY26. At CMP, the company is currently trading at 44x/32x its FY25/26 EPS and with a better earnings growth visibility and return profile the stock looks attractive in the Smallcap space. **We initiate the coverage on Ethos Ltd with a BUY rating and value the company at 40x FY26 EPS to arrive at a TP of Rs 3050/Share, implying an upside of 27% from the CMP.**

Peers comparison

	M.Cap (Rs Cr)	Rating	Target Price (Rs)	EBITDA Margin (%)		P/E (%)		ROE (%)		ROCE (%)	
				FY25E	FY26E	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Ethos	**5,878**	**BUY**	**3050**	**15.5**	**15.6**	**43.6**	**31.5**	**14.7**	**16.9**	**17.6**	**20.0**
Trent	1,14,209	BUY	2750	16.2	16.5	93.4	73.4	24.4	24.0	17.7	18.7
ABFRL	22,124	HOLD	205	12.7	13.0	NA	NA	NA	NA	NA	NA
TITAN*	3,33,457	Not rated	Not rated	12.4	12.7	71.3	58.6	27.8	27.3	32.4	31.1

Source: Company, Bloomberg, Axis Securities

Management Profile

Name	Description
Yashovardhan Saboo *Managing Director*	He holds a postgraduate diploma in management from IIM Ahmedabad. He is the promoter of KDDL Limited and has vast experience in the manufacturing and retail industry. He was also conferred with the "Udyog Ratna" award from PHDCCI in 2005.
Pranav Shankar Saboo *Chief Executive Officer*	He has been associated with Ethos since 2015 and is also the founder of Dream Digital Technology Limited, a multi-faceted digital marketing company. He was later appointed as the CEO of Ethos in 2018.
Ritesh Kumar Agarwal *Chief Executive Officer*	He is an associate member of ICAI and also holds a bachelor's degree in Commerce from Sambalpur University. He has 17 years of experience in Finance. He has previously worked with Spencer's Retail Limited, Baxter Pharmaceuticals Private Limited, Intertek India Private Limited and Pricewaterhouse Coopers Private Limited. He has joined Ethos in 2021.
Manoj Subramaniam *COO*	He has been associated with Ethos since 2020. He holds a bachelor's degree in Commerce from SIES College of Commerce and Economics and an MBA from the Institute of Technology and Management in academic association with New Hampshire. Previously, he has worked with Swatch Group, Swiss Watch House LLC and Just Lifestyle.
Juhi Chaturvedi *Head-Merchandising*	She has been associated with the company since 2007. She holds a bachelor's degree in Science from Government MLB Girls' College, Bhopal and a Diploma in Materials Management from Rani Durgavati Vishwavidyalaya. Previously, She served Indian Army as a Major.

Source: Company

Risk & Mitigation

- **Consumer change requires swift adaption:** Ethos may face the challenge of evolving consumer needs and preferences, so the company is compelled to undergo rapid transformation in its offerings. There has been always a high degree of interaction through the merchandising team which keeps updated on the latest launched products across the stores of Ethos. In case of any failure to adapt may result in a gradual erosion of the consumer base.
- **Geographic expansion challenges:** Ethos's nature of penetrating new geographies, especially in Tier 2 and Tier 3 cities, can create challenges as the market for premium and luxury watches may be limited. Therefore, Ethos always do extensive research on the location before jumping with the premium products through analysing the online consumer behaviour and demand.
- **Supply risk:** A disrupted supply of premium and luxury watches and insufficient inventory maintenance may jeopardize the client demands of Ethos. Hence, Ethos makes sure that adequate stocks are maintained in their respective retail stores by analysing the data on stock churning, selling patterns and zonal preferences.
- **Location and approval risk:** The lack of securing ideal retail space in prime locations like shopping malls, airports etc and the delay in license formalities and obtaining property approvals can impede Ethos business operations and growth. But, most of the time, malls and commercial complexes' first choice is Ethos, being the largest retailer of premium and luxury watches. Hence, Ethos gets ample time to complete all these formalities before any store expansion.
- **Currency risk:** Ethos have foreign currency payables for the supply of the products, and are, therefore, exposed to foreign exchange risk between the Rsand CHF (Swiss Franc) and Euro. Any significant fluctuation in the value of the Rs. against such currencies may adversely affect the performance. Any appreciation of foreign currencies against the Rs. may result in a reduction of margins and consequently have an adverse effect on business and the result of operations. Hence company need to enter into forward contracts.
- **Demand for luxury watches:** Though the company remains extremely confident in the future aspects of luxury and premium watches in India, however, having said that, it is also known that there is a substantial decline in the growth of watches as a time-keeping instrument. Watches are now rather used as a collectable accessory and Ethos being the leader in this category substantially mitigates the risk. However, any decline in consumer spending may affect the demand for luxury watches.

Industry Overview

Growth of Luxury Products in India

The luxury Goods market in India as of FY21 stood at Rs 45,210 Cr while it is expected to grow at 11% CAGR over FY21-25 to reach Rs 69,430Cr.

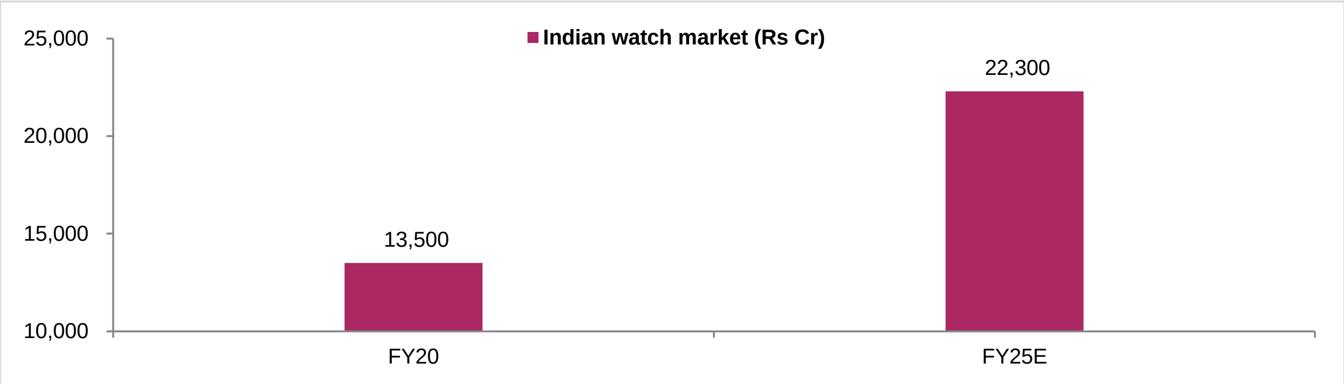
Sector	FY21	FY25E	CAGR %
Luxury Jewellery and Accessories	6,210	9,500	11.2%
Premium and Luxury Cars	16,130	25,120	11.7%
Luxury Fashion & Lifestyle*	14,520	21,810	10.7%
Others	8,350	13,000	11.7%
Total	**45,210**	**69,430**	**11.3%**

Source: Ethos DRHP, *Luxury fashion and Lifestyle includes Luxury Watches, Luxury Beauty, Luxury Eyewear and Luxury Apparels and Footwear

Indian watch market

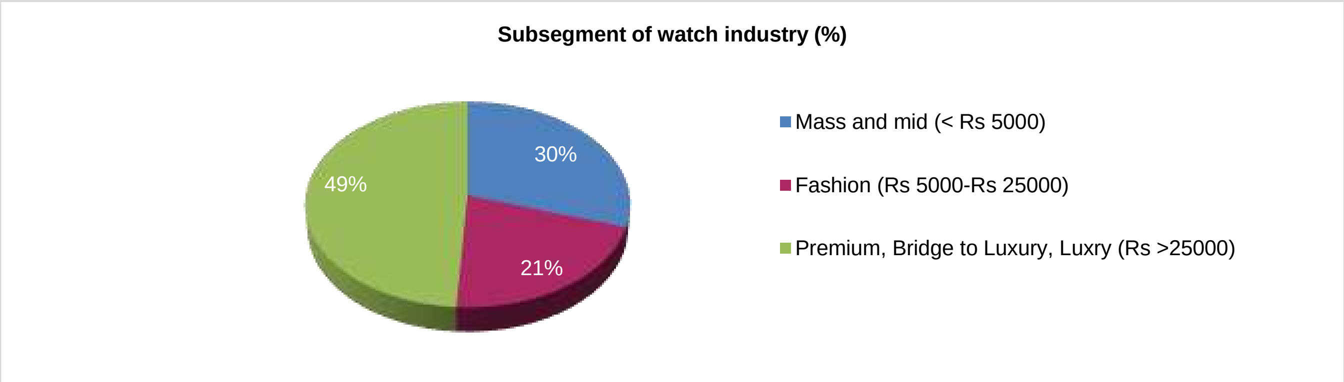
The watch market in India was valued at Rs 13,500 Cr in FY20 and is expected to grow at a CAGR of 10.6% to reach Rs 22,300 Cr by FY25, on the back of factors like increased discretionary spend on the watches category, opening more organized channels of purchase like MBOs and online marketplaces & vertical specialists, increased penetration of smartwatches in mid to premium category, omnichannel market organization etc.

Exhibit 26: Indian watch industry is expected to grow ~11% CAGR over FY20-25



Source: Company, Axis Securities

Exhibit 27: The Indian watch market is further segmented based on basis of – Mass & mid-segment, Fashion and Premium & Luxury



Source: Company, Axis Securities

Exhibit 28: Segmentation of the Indian Watch market by Price – Ethos is mainly present in the Premium to High luxury segment.

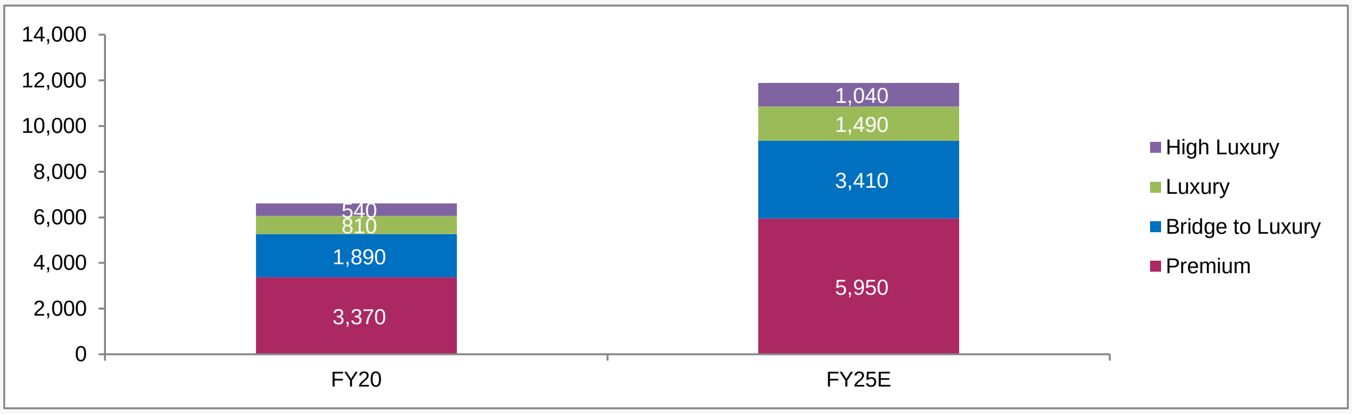
Category	Price Range (INR)	Key Brands
High Luxury	>10,00,000	ROLEX, GP GIRARD-PERREGAUX, H. Moser & Cie., PATEK PHI GENEV, BOVET 1822
Luxury	2,50,000-10,00,000	OMEGA, ZENITH, PANERAI, BREITLING, CARL F. BUCHERER
Bridge to Luxury	1,00,000 -2,50,000	TITONI, LONGINES, ORIS, RADO, TAG HEUER
Premium	25,000 -1,00,000	TISSOT, SEIKO, MOVADO, RAYMOND WEIL GENEVE, JUNGHANS
Fashion	5,000 -25,000	TITAN RAGA, Fossil, G-SHOCK
Mass	<5,000	maxima, SONATA, CASIO

Source: Company, Axis Securities

Premium & Luxury Watches in India

The Premium & Luxury Watch Market stood at Rs 6,610 Cr in FY20 and is expected to grow at CAGR 12.5% to Rs 11,890 Cr by FY25. It comprises the segments High Luxury (Rs 10 lakhs >), Luxury (Rs 2.5 to 10 lakhs), Bridge to Luxury (Rs 1 to 2.5 lakhs), and Premium Watches (Rs 25,000 to 1 lakhs). The High luxury market is growing faster than other segments & the overall market, at a CAGR of 14% and is expected to reach Rs 1,040 Cr in FY25 from Rs 540 Cr in FY20.

Exhibit 29: Indian Premium & Luxury Watch Market is expected to grow 12.5% CAGR over FY20-25E



Source: Company, Axis Securities

Retail perspective – Vertical specialist and EBO

Primarily two routes exist for luxury and premium brands sold in the country (i) Multi Brand Retail led through Vertical Specialists, and (ii) Exclusive Brand retail led. Vertical Specialist MBO-led RTM occupies a 58% share of the total retail sales of premium and luxury watches in the country, whereas EBO-led RTM occupies a 26% share of this total retail sales.

In the Vertical Specialist MBO route to market in India, Luxury and Premium watch retail sales are dominated byNational player Ethos and regional/local MBO players like Kapoor Watch and Johnson Watch Company

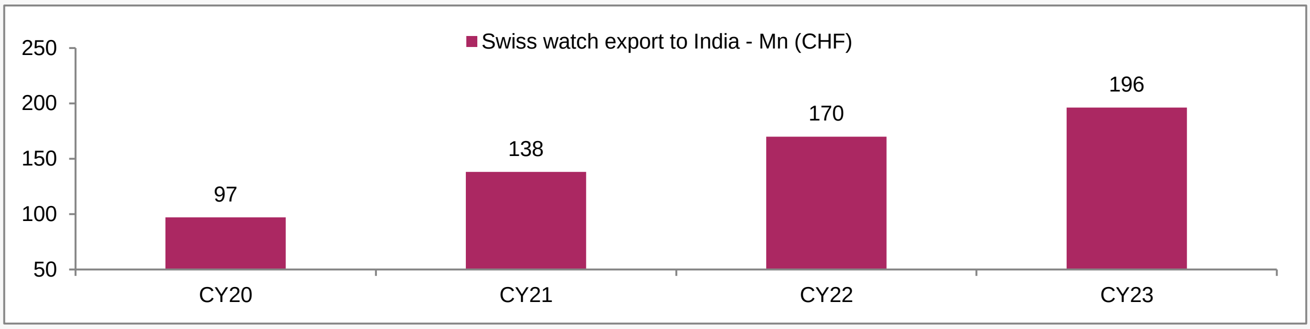
Ethos dominates the Premium and Luxury watch market by a significant margin

	Market share in watch market (FY20)	
Vertical Specialist Premium & Luxury MBOs	**Luxury**	**Premium & Luxury**
Ethos Limited	20%	13%
Kapoor Watch	10%	7%
Johnson Watch	7%	7%
Zimson	6%	4%
Kamal Watch	5%	4%
Khimani Watch	2%	2%
Helvetica Boutique	2%	1%

Swiss watch exports are on a rising trend

According to the Federation of the Swiss watch industry data, India is placed at 22nd position globally in the world distribution of Swiss watch exports. India exports have significantly increased over ~2x from CHF 97 Mn in CY20 to CHF 196 Mn in CY23. The significant rise in the UHNWI and HNWI, an increase in disposable income, has led to an increase in the demand for luxury watches in India. India's UHNWI is expected to grow by 63% reaching 11,198 by FY25. The enthusiasm of global luxury brands to get a foothold in India's burgeoning luxury market clearly demonstrates that the domestic luxury market is on the cusp of strong growth.

Exhibit 30: Swiss watch export to India is up 2x in the last 3 years



Source: Company, Axis Securities

Financials (Consolidated)

Profit & Loss **(Rs Cr)**

Y/E Mar	FY23	FY24E	FY25E	FY26E
Net sales	**789**	**1,085**	**1,462**	**1,931**
Growth, %	36.6	37.6	34.7	32.1
Total income	789	1,085	1,462	1,931
Raw material expenses	(544)	(743)	(1,003)	(1,324)
Employee expenses	(53)	(71)	(96)	(130)
Other Operating expenses	(77)	(103)	(136)	(177)
EBITDA (Core)	**114**	**168**	**227**	**301**
Growth, %	71.0	46.6	35.4	32.5
Margin, %	14.5	15.5	15.5	15.6
Depreciation	(35)	(50)	(61)	(71)
EBIT	**80**	**118**	**166**	**230**
Growth, %	125.4	47.4	41.1	38.4
Margin, %	10.1	10.8	11.3	11.9
Interest paid	(14)	(16)	(17)	(19)
Other Income	15	16	18	20
Non-recurring Items	-	-	-	-
Pre-tax profit	**80**	**118**	**167**	**230**
Tax provided	(20)	(30)	(43)	(59)
Profit after tax	**60**	**88**	**124**	**171**
Growth, %	156.0	47.2	40.9	38.2
Net Profit (adjusted)	**60**	**88**	**124**	**171**
Unadj. shares (Cr)	2.3	2.3	2.3	2.3
Wtd avg shares (Cr)	2.3	2.3	2.3	2.3

Source: Company, Axis Securities

Balance Sheet **(Rs Cr)**

Y/E Mar	FY23	FY24E	FY25E	FY26E
Cash & bank	229	208	209	243
Marketable securities at cost	-	-	-	-
Debtors	6	9	11	15
Inventory	340	468	630	832
Other current assets	64	64	64	64
Total current assets	639	748	914	1,155
Investments	2	2	2	2
Gross fixed assets	230	295	360	420
Less: Depreciation	(29)	(79)	(140)	(212)
Add: Capital WIP	-	-	-	-
Net fixed assets	201	216	220	208
Non-current assets	27	27	27	27
Total assets	**880**	**1,004**	**1,174**	**1,403**
Current liabilities	228	264	310	368
Provisions	2	2	2	2
Total current liabilities	230	266	312	370
Non-current liabilities	18	18	18	18
Total liabilities	248	285	331	388
Paid-up capital	23	23	23	23
Reserves & surplus	608	696	820	992
Shareholders' equity	631	720	844	1,015
Total equity & liabilities	**880**	**1,004**	**1,174**	**1,403**

Source: Company, Axis Securities

Cash Flow (Rs Cr)

Y/E Mar	FY23	FY24E	FY25E	FY26E
Pre-tax profit	80	118	167	230
Depreciation	35	50	61	71
Chg in working capital	(119)	(94)	(119)	(148)
Total tax paid	(20)	(30)	(43)	(59)
Other operating activities	-	-	-	-
Cash flow from operating activities	**(24)**	**44**	**66**	**94**
Capital expenditure	(106)	(65)	(65)	(60)
Other investing activities	-	-	-	-
Cash flow from investing activities	**(107)**	**(65)**	**(65)**	**(60)**
Free cash flow	(131)	(21)	1	34
Other financing activities	-	-	-	-
Cash flow from financing activities	**(16)**	**-**	**-**	**-**
Net chg in cash	(147)	(21)	1	34
Opening cash balance	40	229	208	209
Closing cash balance	229	208	209	243

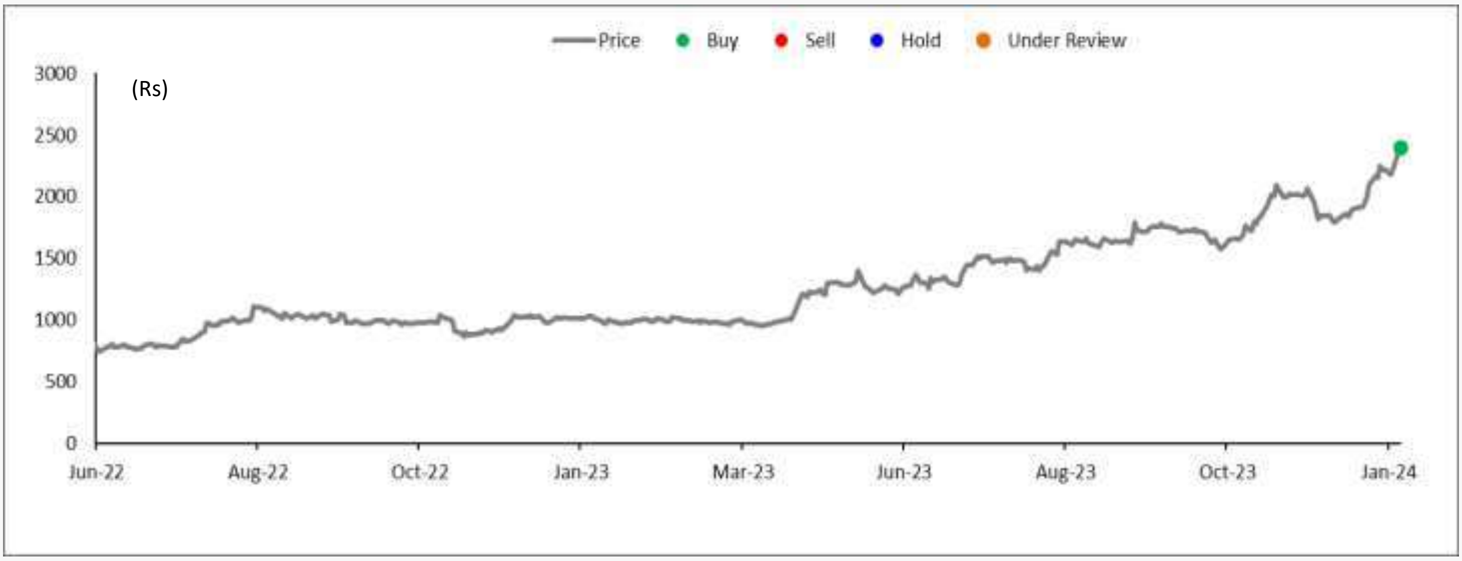
Source: Company, Axis Securities

Ratio Analysis (x) / (%)

Y/E Mar	FY23	FY24E	FY25E	FY26E
Per Share data				
EPS (INR)	26.6	39.1	55.1	76.2
Growth, %	109.3	47.2	40.9	38.2
Book NAV/share (INR)	280.5	319.6	374.7	450.8
FDEPS (INR)	26.6	39.1	55.1	76.2
CEPS (INR)	41.9	61.4	82.3	107.9
CFPS (INR)	(7.7)	12.4	21.3	33.2
Return ratios				
Return on assets (%)	10.7	11.0	13.0	14.8
Return on equity (%)	9.5	12.2	14.7	16.9
Return on capital employed (%)	16.0	14.9	17.6	20.0
Turnover ratios				
Asset turnover (x)	1.9	2.0	2.2	2.4
Sales/Total assets (x)	1.1	1.2	1.3	1.5
Sales/Net FA (x)	4.8	5.2	6.7	9.0
Working capital/Sales (x)	0.2	0.3	0.3	0.3
Receivable days	2.9	2.9	2.9	2.9
Inventory days	157.3	157.3	157.3	157.3
Payable days	52.3	52.9	52.9	53.0
Working capital days	84.2	92.8	98.6	102.7
Liquidity ratios				
Current ratio (x)	2.8	2.8	2.9	3.1
Quick ratio (x)	1.3	1.1	0.9	0.9
Interest cover (x)	5.6	7.5	9.7	12.2
Total debt/Equity (%)	0.2	0.2	0.1	0.1
Valuation				
PER (x)	90.4	61.4	43.6	31.5
PEG (x) - y-o-y growth	0.8	1.3	1.1	0.8
Price/Book (x)	8.6	7.5	6.4	5.3
EV/Net sales (x)	6.7	4.9	3.6	2.7
EV/EBITDA (x)	46.3	31.7	23.4	17.5
EV/EBIT (x)	66.4	45.2	32.0	23.0

Source: Company, Axis Securities

Ethos Ltd Price Chart and Recommendation History



Date	Reco	TP	Research
16-Jan-24	BUY	3,050	Initiating Coverage

Source: Axis Securities

About the analyst

Analyst: Preeyam Tolia

Contact Details: preeyam.tolia@axissecurites.in

Sector:FMCG & Retail

Analyst Bio: Preeyam Tolia is MBA and CFA Level 1 and part of the Axis Securities Research Team.

About the analyst

Analyst: Suhanee Shome

Contact Details: suhanee.shome@axissecurites.in

Sector:FMCG & Retail

Analyst Bio: Suhanee Shome is MBA and part of the Axis Securities Research Team..

Disclosures:

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NEERAJ CHADAWAR

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