Morning Insight

JUNE 26, 2019

	25-Jun	% Chg 1 Day	% Chg 1 Mth	% Chg 3 Mths
Indian Indices				
SENSEX Index	39,435	0.8	0.0	3.1
NIFTY Index	11,796	0.8	(0.4)	2.7
NSEBANK Index	30,847	0.8	(1.2)	3.2
NIFTY 500 Index	9,633	0.7	(0.9)	1.3
CNXMcap Index	17,473	0.7	(1.3)	(1.9)
BSESMCAP Index	14,108	0.3	(4.0)	(3.9)
World Indices				
Dow Jones	26,548	(0.7)	3.8	3.5
Nasdaq	7,885	(1.5)	3.2	2.5
FTSE	7,422	0.1	2.0	3.1
NIKKEI	21,194	(0.4)	(0.2)	(1.6)
Hangseng	28,186	(1.1)	3.2	(1.1)
Shanghai	2,982	(0.9)	4.6	(0.4)

Value traded (Rs cr)	25-Jun	% Chg Day
Cash BSE	1,769	(45.5)
Cash NSE	29,818	18.5
Derivatives	1,158,000	44.1

Net inflows (Rs cr)	24-Jun	MTD	YTD
FII	57	(1,064)	76,983
Mutual Fund	1,248	4,773	7,275

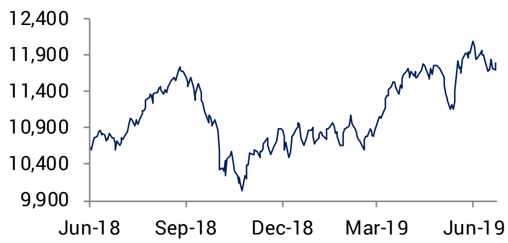
Nifty Gainers & Losers 25-Jun	Price (Rs)	Chg (%)	Vol (mn)
Gainers			
JSW Steel Ltd	267	3.6	9.6
BPCL	393	3.2	6.2
Reliance Ind	1,296	2.7	6.8
Losers			
Yes Bank Ltd	110	(1.7)	56.9
Bharti Infra	270	(1.1)	2.0
Asian Paints	1,363	(1.0)	1.4

Advances / Declines (BSE) 25-Jun	A	B	T	Total	% total
Advances	270	477	23	770	100
Declines	188	491	55	734	95
Unchanged	3	29	15	47	6

Commodity	25-Jun	% Chg 1 Day	% Chg 1 Mth	% Chg 3 Mths
Crude (US$/BBL)	65.8	1.1	(4.2)	(3.2)
Gold (US$/OZ)	1,423.5	0.3	9.6	7.0
Silver (US$/OZ)	15.4	(0.5)	4.7	(1.1)

Debt / Forex Market	25-Jun	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	6.9	6.9	7.2	7.3
Re/US$	69.3	69.4	69.5	68.9

Nifty



Source: Bloomberg

News Highlights

- On account of higher recoveries from big-ticket stressed assets and slow accretion of fresh non-performing assets (NPAs), the asset quality of banks will improve significantly, with gross NPAs shrinking 350 basis points (bps) to 8 per cent by March 2020, stated a report by credit rating agency Crisil. (BS)
- The Centre has planned to set up a common online platform for the Real Estate Regulatory Authority (RERA) of all states and UTs, a move which will provide an opportunity to home-buyers, builders and authorities to exchange views. (ET)
- **Larsen and Toubro Ltd (L&T)** has acquired a controlling stake in IT services company Mindtree Ltd. The report comes within months of Mindtree rejecting a hostile takeover bid from L&T, saying that the plan was of no value for the firm or its shareholders. (Mint)
- **Godrej Properties,** the real estate arm of the Godrej Group launched its qualified institutional placement (QIP) offering to raise around ₹21 bn (around $300 million), according to exchange filings. The company has set a floor price of ₹928 apiece for the share sale. (Mint)
- Troubled **Dewan Housing Finance (DHFL)** said it has defaulted on unsecured commercial paper of ₹2.25 bn and it will be paid over the next few days. The payment was due on Tuesday. (BL)
- **Zee Entertainment Enterprises Ltd.** offered financial support to its promoters at a time Subhash Chandra-led Essel Group struggled to repay lenders. The broadcaster provided loans, deposits and advances worth Rs 1.75 bn to related parties, including promoter-owned entities, in the financial year ended March 2019, according to an exchange filing. (BQ)
- Oil-to-telecom conglomerate **Reliance Industries Ltd.** said it has signed pacts with overseas lenders to avail long-term loans of $1.85 billion (about Rs 129 bn) to finance its capital expenditure. (BQ)
- **Adani Power** said it will acquire GMR Chhattisgarh Energy Ltd (GCEL) as the consortium of lenders has approved its resolution plan. (Mint)
- **Spicejet** launches eight new non-stop international flights.(Moneycontrol)
- **NTPC** won 40 MW solar power project from Uttar Pradesh Power Company. (Moneycontrol)

What's Inside

- **Company Update:** Mahindra Holidays and Resorts India Ltd

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, IE = Indian Express, BL = Business Line, BQ = BloombergQuint, ToI: Times of India, BSE = Bombay Stock Exchange, MC = Moneycontrol

Company Update

MAHINDRA HOLIDAYS AND RESORTS INDIA LTD

PRICE RS.230 **TARGET RS.276** **BUY**

In our recent interaction with the management of Mahindra Holidays and Resorts India Ltd (MHRIL), the company has maintained its stance on adding right quality members which will positively impact its margins and cash flows in the longer run. The company will continue to add new room inventories through greenfield capex as well as leased properties. HCRO's performance in FY19 took a hit on account of certain one-offs and it is expected to do well in the longer run.

Key Highlights

- Management has highlighted four levers for growth which includes 1) increasing geographical reach, 2) innovation in acquisition, 3) member engagement and 4) digitalization and analytics.
- The company is adopting innovative approach in member acquisition. It is utilizing various channels like digital, referrals, tie-ups with brands, etc which will reduce the cost of acquisition of the members.
- MHRIL targets to grow its room inventory from 3595 in FY19 to ~5000 by FY24 which implies 6.8% CAGR in the period. The company targets to add inventory through 1) greenfield/brownfield, 2) lease and 3) acquisition route and targets ~Rs 8-10 bn of capex by FY24. It has generated strong cashflows of over Rs 10 bn in the last four years and has cash balance of Rs 5.7 bn which will support the funding requirement.
- The adoption of Ind AS 115 has reduced total reported revenue and EBITDA margin without impacting cashflows. As per the management, the change in the accounting standard has increased predictability of the revenue model.
- HCRO faced certain challenges in FY19 due to 1) exceptionally warm summer in Finland last year impacted spa hotels and timeshare business and 2) challenges in construction of projects in Sweden. It has appointed new CEO in HCRO and is positive on the business in the longer run based on operational synergy with Indian operations.
- Indian hospitality industry is highly skewed towards non branded hotels and only 5% of Indian rooms are from branded chains. There is huge opportunity for the branded chains to grow in the Indian hospitality market.

Outlook

We believe that the vacation ownership (VO) business in India has strong potential to grow keeping in mind under penetration, rising discretionary spending towards tour and leisure segment, etc which is positive for MHRIL in the longer run. MHRIL's focus on adding right kind of members and rationalization of sales and marketing spend may impact near term growth rate, but will have positive impact on resort income, margins and cash flows. Further, addition of new locations and room inventory would support membership growth in the longer run. We believe that the company will continue to generate strong cash flows in the longer run and would keep its balance sheet debt free. The stock is presently trading at FY20E/21E PE of 18.5x/17.8x based on EPS of Rs. 12.4/12.9 respectively. We maintain Buy on the stock with SOTP based target price of Rs 276.

Stock Details

Market cap (Rs mn)	:	30744
52-wk Hi/Lo (Rs)	:	321 / 185
Face Value (Rs)	:	10
3M Avg. daily vol (Nos)	:	35,951
Shares o/s (mn)	:	134

Source: Bloomberg

Financial Summary - Standalone

Y/E Mar (Rs mn)	FY19	FY20E	FY21E
Revenue	11,252	12,361	13,431
Growth (%)	5.7	9.9	8.7
EBITDA	2,475	2,748	2,986
EBITDA margin (%)	22.0	22.2	22.2
PAT	1,557	1,652	1,718
EPS	11.7	12.4	12.9
EPS Growth (%)	15.9	6.1	4.0
BV (Rs/share)	120	127	134
Dividend/share (Rs)	4.0	5.0	5.5
ROE (%)	13.2	10.1	9.9
ROCE (%)	16.6	12.4	11.9
P/E (x)	19.6	18.5	17.8
EV/EBITDA (x)	12.2	11.0	9.8
P/BV (x)	1.9	1.8	1.7

Source: Company, Kotak Securities - PCG

Shareholding Pattern (%)

(%)	Mar 19	Dec-18	Sep-18
Promoters	67.3	67.3	67.5
FII	6.0	6.0	13.4
DII	12.8	12.8	7.3
Others	13.5	13.5	11.9

Source: Bloomberg

Price Performance (%)

(%)	1M	3M	6M
MHRL	4.8	(4.6)	18.5
Nifty	(0.4)	2.7	9.9

Source: Bloomberg

Price chart (Rs)

Source: Bloomberg

Pankaj Kumar
pankajr.kumar@kotak.com
+91 22 6218 6434

Opportunities galore in Indian hospitality sector

The size of Indian Domestic travel and tourism industry was at USD 247 bn and is estimated to grow at a CAGR of 7% per annum till 2028. The leisure travel accounts for 95% of the overall spend and dominates the overall segment. The expenditure on experience particularly local exploration and recreation accounts for USD 9 bn in terms of size and is estimated to grow at a CAGR of 13% from 2018-21. There is increased preferences of tourists for new and less established locations that have witnessed much higher growth.

Indian hospitality industry is highly skewed towards non branded hotels and only 5% of Indian rooms are from branded chains. In developed market like US, 71% of the room inventories are from branded chains. Thus, there is huge opportunity for the branded chains to grow in the Indian hospitality market. The branded players are focusing on T-2/T-3 cities where 50% of their supplies are expected to come.

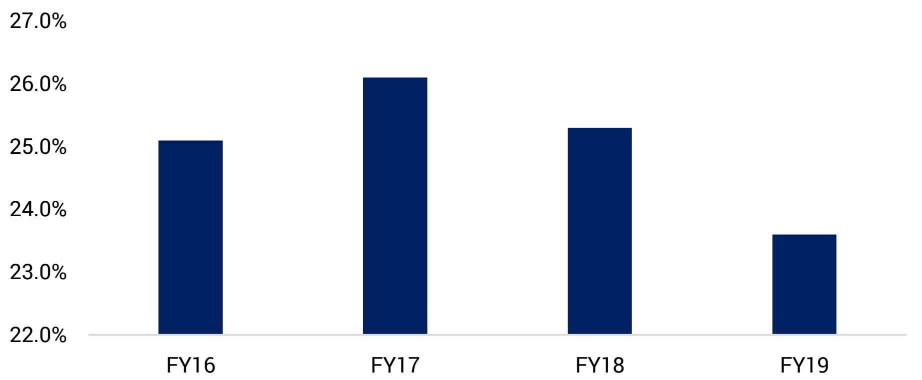
The occupancy rate for FY18 was 66.6% which is moving towards highs of 71.6% (during 2005-06). In order to meet the demand, the number of hotel rooms are estimated to grow at a CAGR of 4% in the next 5 years.

However, there are concerns over slowdown in consumptions. In the recent time, the domestic discretionary spending has witnessed slowdown with weak consumer sentiment.

Identified four key growth drivers

MHRIL has identified four levers for growth which includes 1) increasing geographical reach, 2) innovation in acquisition, 3) member engagement and 4) digitalization and analytics. Over the period, the company increased penetration to new geographies. Contribution from top 17 cities has reduced from 60% to 40% in the last 10 years. The company has added new markets in tier 2 and tier 3 cities like Indore, Raipur, Rajkot, Karnal, etc. It is also expanding global footprints to geographies with high Indian expats such as Saudi Arabia, South Africa and Bangladesh. The company is adopting innovative approach in member acquisition. It is utilizing various channels like digital, referrals, tie-ups with brands etc which will reduce the cost of acquisition of the members. The cost of acquisition of member which was over 25% in FY16-18 has reduced to 23.6% in FY19. The company is focusing on members' engagement through experiential activities, experiences at specialty restaurants, curated vacations, etc. MHRIL has taken several initiatives on digitalization for generating leads and improving member's experiences. Increased usage of mobile app for reservation of resort, current and advance EMI and ASF payment, pre-booking of resort services, etc have enhanced members' experience.

Cost of Acquisition of Member

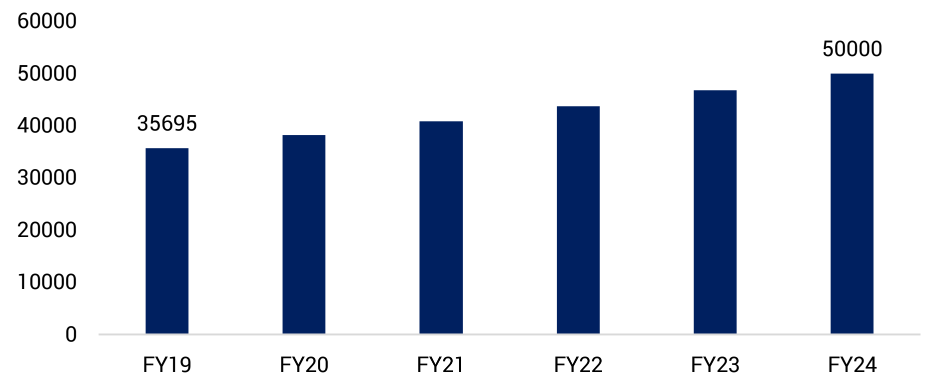


Source: Company

Targets room inventory count of ~5000 by 2024

MHRIL targets to grow its room inventory from 3595 in FY19 to ~5000 by FY24 which implies 6.8% CAGR in the period. The company targets to add inventory through 1) greenfield/brownfield, 2) lease and 3) acquisition route. It would incur Rs 8-10 bn of capex by FY24 to increase the room inventory. Through organic route, the company has already built up land bank at new unexplored destinations. The company is also having ample land at existing resorts for adding room inventory. As part of its greenfield capex plans, MHRIL is adding 156 units at Asanora, (Goa) and 56 units at Ashtamudi (Kerala), and will be operational by Q1FY20 and Q4FY20, respectively. The company has also been adding inventory at new or existing locations through leasing. Out of its present inventory of 3595, approximately over one third are from long term leased properties. The company is also flexible to acquire resorts based on fitment. Its strong balance sheet with cash balance of Rs 5.7 bn (in FY19) and future cash generation will help it in meeting organic/inorganic growth plans.

Room Addition



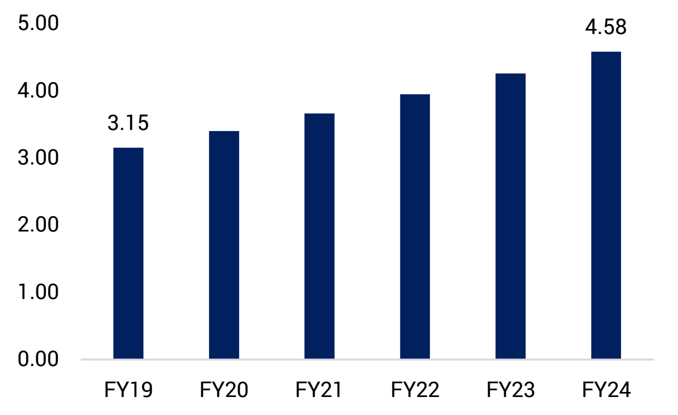
Source: Company

New accounting standard increases revenue predictability

MHRIL has adopted new accounting standard Ind AS 115 (from AS 18) retrospectively on total membership base under which VO income is recognized over the tenure of membership as against previous accounting standard (Ind AS 18) under which 60% of new membership fee was accounted upfront and balance was deferred over the membership tenure. In terms of cost, only direct expenses related to membership acquisition can be deferred over the membership period. The new AS has reduce total reported revenue and EBITDA margin.

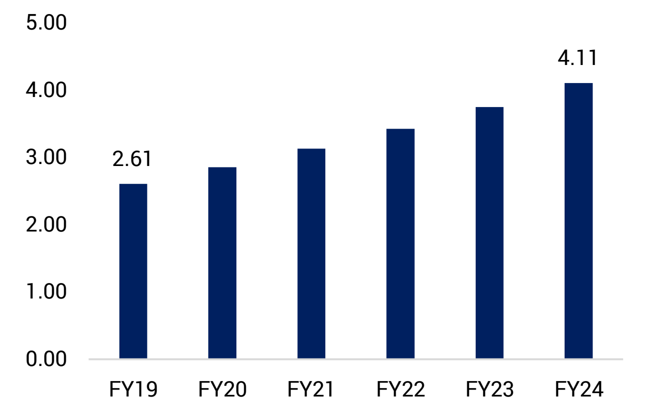
But the change in the accounting standard has increased predictability of the revenue model. Based on company's target to add new inventories, base-case scenario of constant member addition and constant AUR at FY19 levels, the revenue from VO income should increase to ~Rs 4.58 bn in FY24 as compared to Rs. 3.15 bn in FY19 (CAGR of 7.8%) with incremental deferred cost. At the base-case scenario, VO deferred revenue could increase to Rs 66.67 bn by FY24 as compared to Rs 51.1 bn in FY19 (CAGR of 5.5%). At the base-case scenario for member addition and 3% increase in ASF, ASF revenues should increase to Rs. 4.1 bn by FY 24 from Rs. 2.6 bn in FY19 (CAGR of 9.5%).

VO Revenue Recognition



Source: Company

ASF Revenue



Source: Company

HCRO faced challenges in FY19

Post acquisition of HCRO (96.47% subsidiary by MHRIL), MHRIL became the largest vacation ownership company outside of US. The acquisition also resulted in synergy in terms of operations. It has helped in offering holidays destinations in Europe for its domestic members. HCR has a total of 33 resorts across Finland, Sweden & Spain, 25 resorts in Finland, 2 resorts in Sweden and 6 resorts in Spain. Post-acquisition, the performance of HCRO improved and debt reduced from 51.7 mn euro in September 2014 (at the time of acquisition) to 22.8 Mn euro in March 19.

HCRO faced certain challenges in FY19. The company reported 2.7% decline in revenue (at 154.6 mn euro) and made a PAT of 0.5 mn Euro (Vs 4.7 mn) in FY19. The decline in performance was due to 1) exceptionally warm summer in Finland last year impacted spa hotels and timeshare business and 2) challenges in construction of projects in Sweden due to problem with contractor resulted in onetime loss of 2.9 mn Euro. HCRO is focusing on rationalizing the cost and adding new sources of revenues. The company has appointed Mr. Kavinder Singh, Managing Director and CEO of MHRIL as Vice Chairman of HCRO also. It has appointed new CEO, Ms. Maisa Romanainen for HCRO, who comes with over 29 years of experience in retail and consumer space. Based on all these, the company is positive on HCRO in the longer run.

Outlook

We believe the VO industry in India has strong potential to grow keeping in mind under penetration, rising discretionary spending towards tour and leisure segment, etc. MHRIL with its robust business model, strong management and brand image will be able to tap opportunity and beat competition from other players in hospitality business.

We believe that the company’s focus on adding right kind of members and rationalization of sales and marketing spend may impact near term growth rate, but will have positive impact on resort income, margins and cash flows. Further, addition of new locations and room inventory would support membership growth in the longer run. We believe that the company will continue to generate strong cash flows in the longer run and would keep its balance sheet debt free. The stock is presently trading at FY20E/21E PE of 18.5/17.8x based on EPS of Rs. 12.4/12.9 respectively. We maintain Buy on the stock with SOTP based target price of Rs 276.

Company Background

Mahindra Holidays & Resorts India Limited (MHRIL), part of Mahindra group and founded in 1996, is a leading player in the leisure hospitality industry operating under brand name ‘Club Mahindra’. The company is the market leader in the vacation ownership (VO) business in India with over 20 years of track record. MHRIL has built a membership base of over 2 lakh members, offering them holidays across 50+ resorts across India. In FY15, MHRIL acquired Finnish vacation ownership player ‘Holiday Club Resorts”, a leading vacation ownership company in Europe. MHRIL initially acquired 18% stake in Holiday Club Resorts Oy (HCRO) which subsequently increased to around 95%. With this acquisition, MHRIL has become the largest vacation ownership company outside US with a bouquet of 81 resorts across Thailand, Malaysia, Dubai, Finland, Sweden and Spain. Further, its members can choose to access a range of resorts globally through its RCI affiliation. The company delivers quality family holidays experience at its properties by offering various activities such as sports, adventure, fun, dance, etc. Its resorts are located at different terrain such as beaches, hill stations, jungle, deserts, etc giving bouquet of experiences.

Financials: Standalone*

Profit and Loss Statement (Rs mn)

(Year-end Mar)	FY18	FY19	FY20E	FY21E
Revenues	**10,642**	**11,252**	**12,361**	**13,431**
% change yoy	(0.8)	5.7	9.9	8.7
Employees expenses	2,428	2,704	2,975	3,272
Material Consumed	347	366	403	437
Other SG&A Expenses	3,359	3,653	4,018	4,340
Total Expenditure	8,322	8,777	9,613	10,444
EBITDA	**2,320**	**2,475**	**2,748**	**2,986**
% change yoy	(5.0)	6.7	11.0	8.7
Depreciation	548	514	718	920
EBIT	**1,772**	**1,961**	**2,030**	**2,067**
Other Income	300	451	474	498
Interest	0	0	0	0
Profit Before Tax	**2,072**	**2,412**	**2,504**	**2,564**
% change yoy	3.1	16.4	3.8	2.4
Tax	728	855	851	846
as % of EBT	35.1	35.4	34.0	33.0
PAT	1,344	1,557	1,652	1,718
% change yoy	2.8	15.9	6.1	4.0
Shares outstanding (mn)	133	133	133	133
EPS (Rs)	**10.1**	**11.7**	**12.4**	**12.9**
DPS (Rs)	4.0	4.0	5.0	5.5
CEPS(Rs)	14.2	15.6	17.9	19.9
BVPS(Rs)	57.6	120.5	127.0	133.5

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end Mar)	FY18	FY19	FY20E	FY21E
Equity	7,644	15,992	16,867	17,729
Equity Share Capital	1,328	1,329	1,329	1,329
Other Equity	6,317	14,663	15,538	16,400
Liabilities	25,233	28,560	30,384	32,663
Non-current liabilities	20,543	23,434	24,992	26,761
Financial Liabilities & Prov.	101	2,367	2,367	2,367
Other non-current liabilities	20,442	21,067	22,625	24,393
Current liabilities	4,690	5,126	5,392	5,902
Financial Liabilities	1,997	2,198	2,304	2,547
Provisions	34	55	49	53
Other current liabilities	2,660	2,872	3,039	3,302
Total Equities & Liabilities	**32,878**	**44,551**	**47,251**	**50,392**
Non-current assets	17,692	28,471	30,377	32,133
Property, Plant and Equipment	8,485	17,932	19,305	20,975
Capital work-in-progress	1,085	2,182	2,182	2,182
Intangible assets	107	101	111	121
Financial Assets	6,349	6,656	7,180	7,255
Deferred Tax Assets (Net)	135	(500)	(500)	(500)
Other non-current tax assets (Net)	1,178	1,671	1,671	1,671
Current assets	15,185	16,080	16,873	18,259
Inventories	63	56	84	92
Financial Assets	14,767	15,580	16,468	17,819
Cash & Equivalent	4,686	3,381	3,565	4,406
Other current assets	355	443	321	349
Total Assets	**32,878**	**44,551**	**47,251**	**50,392**

Source: Company, Kotak Securities – Private Client Research

Cash flow Statement (Rs mn)

(Year-end Mar)	FY18	FY19	FY20E	FY21E
Pre-Tax Profit	2,072	2,412	2,504	2,564
Depreciation	548	514	718	920
Change in WC	1,692	886	691	1,658
Other operating activities	(993)	(843)	(851)	(846)
Operating Cash Flow	**3,318**	**2,970**	**3,062**	**4,296**
Capex	(781)	(3,642)	(2,100)	(2,600)
Free Cash Flow	2,536	(672)	962	1,696
Chg in Investments & Others	(3,369)	1,329	-	-
Investment cash flow	**(4,150)**	**(2,313)**	**(2,100)**	**(2,600)**
Equity Raised	59	1	-	-
Debt Raised	-	-	-	-
Dividend & others	(535)	(634)	(778)	(855)
CF from Financing	**(477)**	**(633)**	**(778)**	**(855)**
Change in Cash	(1,308)	24	184	841
Opening Cash	1,547	239	263	447
Closing Cash	**239**	**263**	**447**	**1,287**

Source: Company, Kotak Securities – Private Client Research

*Note: * As per old accounting standard*

Ratio Analysis

(Year-end Mar)	FY18	FY19	FY20E	FY21E
Profitability Ratios				
EBITDA margin (%)	21.8	22.0	22.2	22.2
EBIT margin (%)	16.7	17.4	16.4	15.4
Net profit margin (%)	12.6	13.8	13.4	12.8
Balance Sheet Ratios:				
Receivables (days)	321	305	290	280
Inventory (days)	3	2	2	2
Payable (days)	44	43	43	44
Working capital (days)	218	242	253	240
Asset Turnover	0.4	0.3	0.3	0.3
Net Debt/ Equity	(0.6)	(0.2)	(0.2)	(0.2)
Return Ratios:				
RoCE (%)	24.6	16.6	12.4	11.9
RoE (%)	18.7	13.2	10.1	9.9
Valuation Ratios:				
P/E (x)	22.7	19.6	18.5	17.8
P/BV (x)	3.9	1.9	1.8	1.7
EV/EBITDA (x)	13.1	12.2	11.0	9.8
EV/Sales (x)	2.8	2.7	2.4	2.2

Source: Company, Kotak Securities – Private Client Research

RATING SCALE

Definitions of ratings

BUY	–	We expect the stock to deliver more than 15% returns over the next 12 months
ADD	–	We expect the stock to deliver 5% - 15% returns over the next 12 months
REDUCE	–	We expect the stock to deliver -5% - +5% returns over the next 12 months
SELL	–	We expect the stock to deliver < -5% returns over the next 12 months
NR	–	**Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
SUBSCRIBE	–	We advise investor to subscribe to the IPO.
RS	–	**Rating Suspended.** Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.
NA	–	**Not Available or Not Applicable.** The information is not available for display or is not applicable
NM	–	**Not Meaningful.** The information is not meaningful and is therefore excluded.
NOTE	–	Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

FUNDAMENTAL RESEARCH TEAM

Rusmik Oza
Head of Research
rusmik.oza@kotak.com
+91 22 6218 6441

Arun Agarwal
Auto & Auto Ancillary
arun.agarwal@kotak.com
+91 22 6218 6443

Amit Agarwal
Transportation, Paints, FMCG
agarwal.amit@kotak.com
+91 22 6218 6439

Krishna Nain
M&A, Corporate actions
krishna.nain@kotak.com
+91 22 6218 7907

K. Kathirvelu
Support Executive
k.kathirvelu@kotak.com
+91 22 6218 6427

Sanjeev Zarbade
Cap. Goods & Cons. Durables
sanjeev.zarbade@kotak.com
+91 22 6218 6424

Ruchir Khare
Cap. Goods & Cons. Durables
ruchir.khare@kotak.com
+91 22 6218 6431

Jatin Damania
Metals & Mining, Midcap
jatin.damania@kotak.com
+91 22 6218 6440

Deval Shah
Research Associate
deval.shah@kotak.com
+91 22 6218 6425

Teena Virmani
Construction, Cement, Buildg Mat
teena.virmani@kotak.com
+91 22 6218 6432

Sumit Pokharna
Oil and Gas, Information Tech
sumit.pokharna@kotak.com
+91 22 6218 6438

Pankaj Kumar
Midcap
pankajr.kumar@kotak.com
+91 22 6218 6434

TECHNICAL RESEARCH TEAM

Shrikant Chouhan
shrikant.chouhan@kotak.com
+91 22 6218 5408

Amol Athawale
amol.athawale@kotak.com
+91 20 6620 3350

Faisal Shaikh, FRM, CFTe
Research Associate
faisalf.shaikh@kotak.com
+91 22 62185499

Siddhesh Jain
Research Associate
siddhesh.jain@kotak.com
+91 22 62185498

DERIVATIVES RESEARCH TEAM

Sahaj Agrawal
sahaj.agrawal@kotak.com
+91 79 6607 2231

Malay Gandhi
malay.gandhi@kotak.com
+91 22 6218 6420

Prashanth Lalu
prashanth.lalu@kotak.com
+91 22 6218 5497

Prasenjit Biswas, CMT, CFTe
prasenjit.biswas@kotak.com
+91 33 6625 9810

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