

5 December, 2011

Moderator

Ladies and gentlemen, welcome to the Q2 FY'12 results call of Essel Propack Limited hosted by Emkay Global Financial Services Limited. We have with us today, Mr. Ashok Goel – Vice Chairman and Managing Director, Mr. A. V. Ganapathy – CFO, Mr. M. R. Ramasamy – President, Mr. R. Chandrasekhar – President, Mr. Vinay Mokashi – Financial controller, Mr. Ashish Patel – Head of Treasury and Mr. Niladri from Investor Relations. As a reminder, for all the participants, your lines will be in the listen-only mode. And there will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call, please signal an operator by pressing * and then zero on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Pritesh Chheda, Senior Research Analyst of Emkay Global. Thank you, and over to you Mr. Pritesh Chheda.

Pritesh Chheda

Thank you Lavina. Good afternoon everybody and thank you for joining us today. We would like to welcome the management of Essel Propack Limited thanking them for giving us the opportunity to host this call. Today we have Mr. Ashok Goel – Vice Chairman and Managing Director, Mr. A. V. Ganapathy - CFO, Mr. M. R. Ramasamy – President, Mr. R. Chandrasekhar – President, Mr. Vinay Mokashi - Financial controller, Mr. Ashish Patel - Head of Treasury and Mr. Niladri Nandi – Investor Relations. I would now like to hand over the call to Mr. Ashok Goel for the opening remarks and there after we will open it for Q&A. Over to you sir.

Ashok Goel

Thank you Pritesh and I thank Emkay for hosting this event as usual and all of a warm welcome. I'm sure you have received the note on the 2Q results. I will not go exactly over it, but however I will point some highlights. The global operation did have a net profit of Rs. 92 million on a sale of Rs. 396.3 crores. Even though the net sales have increased by 7.5%, the net profit is lower by 31.8%. Which of course is a concern and I'm sure you have lot of questions around it. We will try to address them, but this reduction in profit over last year is primarily due to couple of factors. Major one is domestic cost increased coupled with the exchange rate, that's the way it has gone. We have also seen slowdown in Europe which is in-line with what is happening in the overall general economy of Europe. So we are seeing that impact. And in China we have businesses performing good, except for one aberration. And that aberration we believe is temporary and what is that? That is one our contract customer, I can't give you the name. Have some branding issue on a particular variant. As a result, off take of that particular variant has been lower and that is the sole contributory factor for reduction in volumes in China. We expect that this branding issue that the customer had, will be back on track by December this year and so China should be able to come back on its numbers. But they have in the meanwhile increased their volumes on exports, but that obviously is not good enough to compensate the temporarily loss from that particular customer in terms of volumes we have. Other than that there is no concern in China. When it comes to India standalone we have couple of factors. One of course is price increase and Second one is the exchange rate impact. Then we have increase in power cost which is gone up by about 11.2%. And we are taking certain measures to optimize that. Then this year we have some lease equipments in India. So what does it do, when we pay operating lease charges versus the own equipments, when we own the equipment interest and depreciation is charged below the EBITDA line. Whereas when you operation lease, lease charges comes as operating cost. So therefore it is coming above the EBITDA line. But that is on the EBITDA but that make some impact on PAT. Then we have minimum wages increases in the states that we operate. So the cost the labor went up by 15% average. Moreover, since our capacities are running full, we have done some outsourcing of certain services. So that costs have come in. And we obviously have some corrective plans for second half of the year. There are certain factors which we have recognized, we know that we can take steps.

There are certain factors like European economy where we are trying our best to keep our capacity utilized but that's purely external factors. So is the case in China which is an external factor. In India we have recognized certain phases based on these cost increases. We have identified some actions to be taken. While in America, things have performed as per plan. So is the case with flexible packaging which is so far doing as per plans. So there are factors which are beyond outside of our control, there are factors within our control. And we see that in H2 we will take those corrective steps apart from inventory reduction plans we have which is about \$.10 million that we will roll out for the second half. Then I will hand over the platform to my colleague. Pritesh, you want to go with the question answers straight away, you want to add anything in it?

Pritesh Chheda

I think we can start with the Q&A. Or maybe we could just give the numbers and then we can start with the Q&A.

R. Chandrasekhar

Good afternoon everybody. For this quarter the consolidated sales was 396 crores representing a growth of 7.5% over last year. Sequentially again we have grown about 10.1%. Operating profit that is before other income, interest and exceptional item is 35.8 crores. That's declined by about 13.75 compared to previous quarter however it has grown by about 16.9%. In that sense the growth which has come in this quarter over the last quarter has been profitable on a sales growth of 10% we have actually grown our operating profit by 16.9%. Overall net profit for the quarter is 9.2 crores. As Ashok mentioned it's a reduction of almost 32% compared to the last year. But sequentially it is almost flat, just 1.3% lower than the previous quarter. Overall for the half year company has achieved a consolidated sales of 756 crores representing a 7.9% increase in the top line and a net profit of 18.4 crores representing decline of about 16.65 compared to the last year. So that's on the overall picture. In terms of the regions, during this quarter, the AMESA and America as well as the Europe – always of the three regions recorded an increase compared to the previous year. AMESA recorded a revenue growth of almost 12.8%. In Americas we grew 7.6%, Europe we grew 8.4%. In terms of sequentially also AMESA recorded a growth of 7.6%. Americas grew 16% and Europe about little less than 1%, on the East Asia Pacific, look at just before touched upon that where we grew compared to last year; there was a decline of 9%. Which we believe is a very temporarily blip. But all the while it has cost lot of impact for us in the quarter results. Sequentially however EAP has picked up compared to the last quarter by about 9%. Where, as in terms of profitability again AMESA has grown about 14.2% over last over. Americas have really turned around and we are almost 6 times what were on a small base of profit last year. In Europe, we have been impacted. Our profitability has dipped this quarter and which will explain in the question answer session. Largely impacted by two things, one is issue in Germany and the second one is in terms of some of the market to market losses due to the sharp exchange fluctuation during this quarter. Overall on a half yearly basis, the revenue in AMESA has grown 7.6%. Americas have grown 16%. East Asia Pacific have grown 14% and to show basically that the overall growth engine is still on. There have been sudden one off issues which have made some deep impact. Which believe that this should get corrected. Back to you Pritesh.

Pritesh Chheda

Lavina we can start the Q&A?

Moderator

We will now begin with the question and answer session. Anyone who wishes to ask a question may press * and 1 on your touch-tone telephone. If you decide, you want to withdraw your question from the question queue, please press * and 2 to remove yourself from the queue. Participants, if you have a question, you may press * and 1 at this time. The first question is from the line of Vijeta Maheshwari from Nirmalbang Securities. Please go ahead.

Question and Answer Session

Vijeta Maheshwari

Good afternoon sir. Sir I just want to know, last year quarter, if I remember correctly, you have said that you have increased the prices in July to pass on the raw material prices we have increased the prices. But its not shown in your Q2 results. Any reason for that?

Ashok Goel

Yeah it's a good question. See we did increase the prices. We did get the price increase. But after that the price momentum has stayed on the north side curve coupled with exchange rate differential. So we do have net lag effect of about 2.5% of price increase. Even after taking that price increase which mentioned that last quarter. So that 2.5% is making a difference.

Vijeta Maheshwari

So are we able to pass on the prices in the coming quarter? Or are going to suffer the raw material pressure.

Ashok Goel

No we are going to immediately – we actually initiative steps to ask for price increases. And so that will slowly happen in this quarter. And coupled with that, we are now seeing some softening of raw material prices. So we may end up getting some benefit also.

Okay. Sir you have said that there was some problem with the customer in China. Can you just throw some light at how is the scenario right now? Are you able to sort out the issue with the customer or is it going to pertain for a longer period?

Ashok Goel

Okay, let me explain. We have no issue with customer at all. So we are supplying them, we are 100% supplier to that customer. We are supplying parts quantities. It is the customer's internal issue, they have something to do with branding we don't exactly know what it is. So that particular variant of that brand is under some sort of restructuring or what is going on, we obviously don't know. And even if we knew, we what obviously are kind of barred from revealing that as a part of customer confidentiality. We are in constant touch with this customer. This customer constantly reassures that that by December, they should be done with this issue and they will resume normal off take.

Vijeta Maheshwari

And how much of the percentages this customer has in your total revenue from the EAP region?

Ashok Goel

This customer, the short fall we can tell you. It's about 10% of total.

Vijeta Maheshwari

What I'm asking is sir, what is the total percentage in the revenue generated in EAP region?

Ashok Goel

I can tell you in the PAT terms it has impacted us in PAT terms about Rs 5 crore to 6 crore. The reduced uptake.

Vijeta Maheshwari

Can you just tell us by what percentage you are expected to record your top line and bottom line in FY'12 and FY'13?

Ashok Goel

FY'12 we will have 12% growth for sure, that's what we believe that we will. That is volume terms. IN FY'13, Ganesh?

Ashok Goel

FY'13 yeah around similar 10% to 12%. Yes long-term plan.

Vijeta Maheshwari

Okay. And what about the bottom line?

R. Chandrasekhar

See bottom line our plan is by FY'13 to reach levels we had reached in 2006. About 98 crores. That's what we are working on. That's our plan.

Ashok Goel

98 crores on PAT terms.

Vijeta Maheshwari

In FY'13?

Ashok Goel

Yes.

Vijeta Maheshwari

Okay. And are you like, as you are operating margins have dwindled a lot in your Q1 and Q2 FY'12. So what kind of initiatives you are taken to bring back your operating margin at the same level of 2006 of the FY'11 levels?

Ashok Goel

See this cost escalation that have happened, I'm particular referring to India, which is increase in labor cost, power cost, raw material cost. These we are working on so that we sort of neutralize the labor cost increase. Then we are working on reduction of inventories. So that it has least impact on the increased raw material. Now going forward we have to watch carefully as we currently see in the price opening up of raw materials. And we are also working on alternative power source, because in some units, we have to run our own DG sets, which become prohibitively expensive because of the quality of power. In spite of the fact that power tariff itself has gone up. So we are working with alternative source of power and also trying make sure how do we reduce using our own Genset. So we cannot offset the complete cost of this, but of course partially we will work on it. Then we are working on how to rationalize our capacities and also work on the variants, which are more profitable for example the growth in India is skewed towards smaller diameter tubes. A smaller diameter tubes typically give us low sales price and because it is low sales price you obviously get lower margin in percentage terms. So that's something we have to work on, on product mix. We do have some plans. On the other hand, last year, we expanded the plastic tube capacities. So effectively this year, these capacities have come up. We have increased the sales, but we have not fully ramped up in terms of sales that we expect to happen and which of course is value added product. And therefore, we should partly compensate the depression that we have in the profit. These are few of the steps that we are working on.

Vijeta Maheshwari

Are we running on full capacity or, what is the capacity utilization as of now?

Ashok Goel

In India, on laminated tube side we are running more or less full. On plastic tube there is still about 30% we can go up. And that's what we are targeting at. And of course we are expecting some more growth to come but that will come in Jan to March quarter. That we are making trying - seeing that how not to increase the capacity and yet meet the customer demand. So in that sense sweating the assets little bit more.

Vijeta Maheshwari

Sir I was just checking your share holding pattern. Your foreign promoters holding has come down to 0.06%. Indian promoter holding has increased to 69.07%. If you just can throw some light why the foreign promoter holding has come down such drastically from 10% to 0.06%?

Ashok Goel

That must be some interstate promoter transfers. So it doesn't mean anything as far as we are concerned.

Vijeta Maheshwari

Okay. And if you can throw light, what kind of growth you are expecting in Europe because right now Europe is still in a very bad situation. And if you can throw some light on Europe and other regions, how much growth are you expecting?

Ashok Goel

Compared to September 10 the same period last year the growth has been around 7% to 8% in Europe. This is despite the fact that we are seeing a general slowdown in Germany that we have lost some volumes, but we are seeing an upswing as far as Poland is concerned. And that is at 78%. Going forward we expect to retain up to March the same 7% to 8% growth rate. You won't see anything different happening as far as Europe is concerned. Two things, one is that we have made a formal announcement about shifting our capacities from the plant in England into Poland. So obviously there will be some churn which will happen in the customer portfolios, very minimal but there will be some churn. And the second thing is that plastic tube business, we have been seeing some fairly stable growth which has come in the last 6 months. We expect to continue to build on that going forward. The other regions as far as Russia is concerned, it's a very flat volume. There is not much of a difference. And it again a part of Europe. Germany have had a very bad first six months that is April to September has been lower growth and we expect that to pick up after Jan of next year. Moving across to the Americas, four businesses. One is the plastic tube business which has been a problem child for us. Then we are now doing fairly very stable volumes and very near the breakeven point at the EBITDA levels. We still further did see an acceleration of volumes to happen in the period Jan to March from wherever we are today. BP, which is the laminated tube business, is highly contractual in nature. Most of the growth depends on the contractual customer and the newer customers whom we continue to add. And it has been a stable, I will say it's a very stable 6% growth on the business. Columbia again has grown fairly robust this year compared to the previous year. And in Mexico, there has been poor off take in the first quarter of this year. That is April to June quarter. But now they are back and the volumes are ramping up from August onwards.

Vijeta Maheshwari

And sir last question what kind of PAT you are expecting in FY'12?

R. Chandrasekhar

Yeah see normally I don't think we are basically issuing guidance's on this ones. But definitely we will take into account of the fact that we have had an impact of this on volumes, which although it's going to impact my results for this particular financial year. So we would have, in the normal course with our volume growth of around 12% we would have probably grown our profit by at least about 20% 25%. So I believe that this particular which is going to create EBITDA for dampening all that one. Depends on how we make it up in the next two quarters.

Vijeta Maheshwari

Thanks a lot sir. I wish you always the best.

Pritesh Chheda

Just on the capacity utilization side sir, if you could give us the same for EAP as a region, Europe as a region and US Americas as a region?

R. Chandrasekhar

If querying this one particular customer incident, we have major set backs. Customer has assured that going forward from this quarter onwards this would get corrected slowly. So once its corrected, they will go back to their normal utilization levels to normal profit levels. And definitely it should happen Q4 of this year. There may be a mixed one on Q3. That's October to December quarter. But certainly January to March quarter it will get corrected.

Pritesh Chheda

capacity utilization is...

R. Chandrasekhar

From the name plate capacity that we normally operate around 70% 71%. I think we should get back to that level.

Pritesh Chheda

What is the utilization currently in Americas and Europe?

Ashok Goel

In the US laminated tube business we are currently at about 65% to 67% utilization. In the plastic tube business it is much lower. Its currently around 50% utilization. Colombia is much higher its about 87- 88%. Mexico after the capacity addition has happened, it is lower now. We are ramping up, it's about 55%, 56%. Europe there are two business plastic as well as planning. Germany is very low its about 50% utilization. Russia is about 60% at odd utilization. The plastic in Poland is also currently at about 50% utilization.

Pritesh Chheda

Russia is how much?

Ashok Goel

Russia is about 60% utilization.

Pritesh Chheda

And in China i.e. EAP?

Ashok Goel

EAP is currently around 68% utilization. We will go back to 70 to 72.

Pritesh Chheda

Secondly for the quarter and for the first half, what has been the blended volume growth for us and what are the price led growth. Its first question. Second, we have seen gross margin compression on a YoY basis. So just wanted to understand what has been the raw material price increase corresponding to the price increases that we have taken?

R. Chandrasekhar

Pritesh let me throw little bit light on this. Second question first and then we can come back to the first. If you really see this quarter as I said, there were major factor which have really dampened the results actually. It is not that wide spread. One is that the material cost increase. For two successive quarters we are seeing the input prices going up. Input in our case consist of polymers, the consist of oils and polypropylene. And also there are some specialized polymers which we use. Now what happens in a business like us is that we operate on what is called a pass through which is done prospectively. So when you are on a constantly increasing, say the prices are going up like in the first quarter, we experience close to about 10% of the increase. And the second quarter we have seen an increase of about 7.7% to 9%. Now when this happens, what happens is, the material cost is almost for us about 45% to 50% of our sale price, we will see that dampening coming in the gross margin because of the lag effect. Now, the moment the pressure stabilizes or when they start dropping, we will see the margins once again recovering back. Now incidentally its very interesting if you see the same quarter of last year. In fact prices were much on even and just slightly dropping and during similar period our cost increases is only about a percent. So that actually accentuate when you compare the difference. So on a 8% to 9% price increase the cost increase which I experience today, you see my margin dropping by about 2.5% in terms of material cost. So that's one thing. And we have a pass through mechanism with all our contract customers. And non-contractual customers we have a process of revising the prices. As these things take place, we do believe that the margin should come back. Roughly I'm estimating about 2% to 2.5% impact on the margin on account of the material prices. That's one. The second thing again, we were talking about capacity utilization. If you see our growth in the quarter II, over quarter I has been double digit. In fact we are geared to grow even more with our capacity. That's not an issue. The main issue is that we have a significant volume impact which has happened as Ashok mentioned in the outset. Which we believe today is still a temporary blip, because it has not resulted in any market share loss. But then when such sort of a volume impact comes from a contractual customer, it is not very easy for us in a very short frame to fill it up. And secondly that this sort of volumes will be filled up by the same customer as he bounces back and start filling his pipeline. So that's the situation where what happens is. The volume has not come up and therefore it is impacting again. My EBITDA to the extent of close to about 2.5%. So roughly if you really look at this quarter, but for this two impact. My EBITDA should have been already in the region close to about 19% to 20%. Now coming to the mix you wanted, in terms of the revenue. We have almost we are continuing same pattern. My total revenue coming out of laminated tube is about 295 crores, which is 74%. Plastic tubes are accounting for about 45 crores, around 12%. And the specialty packaging is accounting for about 57 crores, which is about 14% of our revenue. And broadly the trend is same the half year. We are about out of 757 crores of turn over, 567 is from laminated tube. 84 is from plastic tubes and 106 crores from specialty packaging.

Pritesh Chheda

Wanted to know the price led and the volume led growth in H1 and the quarter II.

Ashok Goel

Okay. In terms of quarter II, my volume growth has been about 1.8% in the laminated tube. Whereas in the case of plastic tube it has been almost double. So roughly we should be anywhere in the region close to 2.5% in terms of volume growth for the quarter. And in the half year it would be about 5%.

Pritesh Chheda

5% is for plastic tube?

R. Chandrasekhar

No I'm talking about total tubing

Pritesh Chheda

Total tubing quarter I was how much?

R. Chandrasekhar

Yeah in total tubing for quarter II is 2.5% and half year is 5.7%.

Pritesh Chheda

So, means in the quarter I you must have grown higher than the 5.7?

R. Chandrasekhar

Yes, that's true. That is said, one off impact is coming for us in the volumes.

Pritesh Chheda

Okay. And if you could give us the same number for the three regions, the rough volume growth for H1?

R. Chandrasekhar

At the region level I don't have.

Ashok Goel

Can I give you the revenue growth

Pritesh Chheda

I have the revenue growth.

Ashok Goel

Yeah. If you look at quarter on quarter, that is you are comparing the quarter September '11 with September '10. AMESA grew by around 12.8%, Americas by 7.6% Europe by 8.4% and EAP contracted by 9.2%.

Pritesh Chheda

Yeah but that's the revenue growth, value? You want the growth? Our financial could also tell us both for EAP and AMESA, that is the segment I and segment II. The loss in EBITDA margins that we have seen over the years, it is more transitional in nature or is it structural? If it is structural then what element should one consider as structural because in AMESA the loss in margins is from 19 to 12. So you have got 700 bps. And in EAP it is from 30 to 18.

R. Chandrasekhar

Okay I would not get an immediate answer to this Pritesh for the simple reason that I think over the couple of years we have done some amount reclassification in this reporting, okay. Because there were couple of things we had. We had external sales, internal sales and then we had a medical devices business in the past. So what I could probably do is that, if you can give me the page with which you are referring, let me put it on a comparable basis and then I would be able to explain to you much better.

Pritesh Chheda

So the medical decides by was classified in which?

R. Chandrasekhar

Yeah it was there in both Americas as well as in EAP region.

Pritesh Chheda

Okay. So if you could tell us AMESA, my question was in AMESA and EAP and not Americas. So the AMESA the loss of gross margins over the years, is it transitional in nature or is it been structural? If it is so then, so if you could highlight, what would be new margins in this business?

R. Chandrasekhar

Definitely, I think in AMESA we have a mix of two business which has come together. One is the tubing business under Essel Propack Limited and other is the specially packaging under PAPL right? So since 2006 and PAPL EBIT margin are lower compared to what you have seen in margin of Essel Propack Limited. So I take your point, because what is really happening is over a period of time if you look at very old, say 10 years ago you will definitely see a that's the impact of the completion or

whatever it is. But overall the last two years,, I think the margins have not shown any sort of that trend. If at all there is a increase in the volume, we should be getting a little bit of sales benefit coming in. So what will do we its much easier for me to understand the reference points you are looking at. And probably I think we will back to with a proper answer with actual numbers, if that is okay with you.

Pritesh Chheda

And you commented on the FX part in the quarter. If could quantify the FX impact in quarter.

R. Chandrasekhar

FX impact anyway we are quantifying in our publication for that. There are two impacts. All the FX impact has been put down in row number 6. It's about 3.26 crores for the quarter. And there is also about crore which you are carrying as a credit in the balance sheet, because of the accounting standard requirement. So net impact is about 2.4 crs.

Pritesh Chheda

And this is transactional in nature, or it is translational?

R. Chandrasekhar

It is not translational because what is impacting the P&L account is either transactional or marked to market. Some are realized, some are not realized. Typically non realized ones would be increased in financials.

Pritesh Chheda

So these are the chunk of it not realized?

Ashok Goel

Yes, I would get so. So these are all open for contracts on various currencies?

R. Chandrasekhar

No these are the two things which get adjusted as per as accounting standard in exchange and losses. One is our market to market growth at the end of each quarter. Mark-to-market the current assets and liabilities in foreign currencies. And other one is your net impact of your forward premium which you have paid and which you have received. So on a whole I think we are mostly hedges on most of our positions. And therefore the type of movement which has happened in the market and the exchange in lines which we are seeing is very much low compared to what the volatility in the market has been. Couple of areas which I mentioned in my opening address is that where we have some market to market losses of significance. Of course in the places where the currencies are little bit exotic like in Rubble and Mexican peso

Pritesh Chheda

So you might have gained on account of your assets and liabilities. Assets basically and you would have lost on account of open forward contracts and the net offered is 3 crores?

Ashok Goel

No there are no open forward contracts. It is just that there are open dues. So if a bought a material and they have paid creditor, its an open due. I have done any forward or a derivative or any such position. We don't trade on it.

R. Chandrasekhar

see our forward contracts are purely for hedging. So what happens is, if any gain or loss on the forward position is offset by the underlying gain or loss. So therefore we don't have any such issue of a speculative or that sort of a position in the market. But the moment I do a forward I'm hedged there. I won't have any more impact on the P&L at all.

Pritesh Chheda

And my last question is on the Europe side our business is growing but so is the EBITDA loss grown in the quarter?

Ashok Goel

Yeah compared to the last year, for this quarter our total loss in the Europe region will be contributed mainly by the Russia, Germany and the UK operation. Poland is more or less stable at this point time. In Russia as you said we have had some what you call currency evaluation at the end of quarter which is accounting for last part of it. But for that Russia would have been also almost on the same level as there has been no deterioration there. In UK as Chandra already explained that we are going through this process of shifting and therefore to an extent there will be impact of what you call, the fixed cost for a few more months. And Germany is one where basically it's a profitable operation for us but which has actually has tanked during this quarter and to an extent in the previous quarter. And that's why you are seeing the European losses on the higher side compared to the last year.

Pritesh Chheda

Okay. Navina can we check for questions?

Moderator

Sure. Participants, if you have a question, you may press * and 1 on your touch-tone telephone.

Pritesh Chheda

I don't think there are any more questions.

Moderator

No Pritesh, we don't have any further questions.

Pritesh Chheda

I think sir we should wind up the call?

Ashok Goel

Right.

Pritesh Chheda

So on behalf of Emkay, I would once again like to thank everyone for joining the call today. We would take this opportunity to thank the management for giving us the chance to hold the conference call for the quarter II numbers. We wish everyone happy Diwali and prosperous New Year. Over to you Mr. Goel if you have closing comment.

Ashok Goel

As usual I appreciate for taking time out all of you. And Emkay for hosting the event. And we all do wish everyone and the families a very Happy and Prosperous New Year. Thank you very much.

Moderator

On behalf of Emkay Global Financial Services Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines.

Note:

1. This document has been edited to improve readability.
2. Blanks in this transcript represent inaudible or incomprehensible words.

Emkay Global Financial Services Ltd.

Corporate Add: B – Ruby Mills Tower, 7th Floor, South East Wing, Senapati Bapat Marg, Dadar (W), Mumbai - 400028 India.

Tel.: +912266121212 Web: www.emkayglobal.com

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