

September 16, 2011

Price Performance

BHEL		Hold			
CMP Rs 1708		TP Rs 2150			
(%)	1M	3M	6M	12M	
Absolute	(4)	(9)	(14)	(28)	
Rel. to Nifty	5	0	(5)	(22)	

L&T		Buy			
CMP Rs 1610		TP Rs 2015			
(%)	1M	3M	6M	12M	
Absolute	(7)	(1)	(0)	(11)	
Rel. to Nifty	2	8	10	(4)	

Thermax		Buy			
CMP Rs 503		TP Rs 735			
(%)	1M	3M	6M	12M	
Absolute	(14)	(17)	(19)	(35)	
Rel. to Nifty	(6)	(9)	(10)	(30)	

Source: Bloomberg

BTG Equipments... Is this new era in the offing?

- NTPC 9x800 MW – Doosan L1 in boilers & BGR Energy L1 in turbine-generator sets. Prima facie comparison with past pricing orders indicates only marginal disruption in pricing
- With new players emerging L1, BTG equipment market splits-wide open. Hints at hectic competition, disintegration of market and fragmentation of market shares in the near future
- (1) BHEL – Boosts orderbook (de-facto L2); Concerns play out; (2) L&T – Not bagging an order a negative, but has sufficient cushion (3) Thermax – Higher stakes involved - time is ticking

NTPC 9x800 MW bulk tender ordered – Doosan (Korea) & BGR Energy emerge winners

Doosan Heavy Industries, Korea and BGR Energy-Hitachi emerged as L1 players for Boilers and Turbine-Generator (TG) sets respectively, each securing 5x800 MW orders. The other bidders in the fray were BHEL, L&T-MHI and Thermax for Boiler Sets and Bharat Forge-Alstom and JSW Energy-Toshiba were additional players in the TG sets.

L1 bidder	Order Particulars	L1 Bid-Price (Per MW)	Order Value
Doosan Heavy Industries	Boiler – 5x800 MW	Rs16.4 mn	Rs65.6 bn
BGR Energy	Turbine-Generator	Rs8.8 mn	Rs35 bn

As per predetermined terms of the contract, BHEL will hold preferential rights and option to match the respective L1 bids and emerge as de-facto L2 (in case BHEL is not L1). It will thus get boiler order for 4x800 MW and turbine-generator order for 2x800 MW.

Is the pricing action aggressive / predatory?

We compared the above bids with supercritical orders awarded in past to determine the presence and extent of predatory or aggressive pricing, if any. A prima facie comparison with past pricing (pure-play super-critical orders) indicates marginal disruption in pricing.

- **Boiler order - No under cutting:** A plain-vanilla comparison with two pure-play boiler orders secured by BHEL suggests non-existence of aggressive/predatory pricing. Erstwhile prices are actually 5-15% lower than current 9X800 MW under consideration.

Name of Company	Order details	Order size (MW)	Order value (Rs Mn)	Rs Mn per MW
BHEL	AP Genco – Krishnapatnam	2x800	25,000	15.6
BHEL	NTPC – Barh	2x660	18,500	14.0
Current order value				16.4

- **Turbine-Generator order - Probably:** However, similar comparison in case of turbine-generator indicates a possibility of aggressive pricing. At Rs8.8 mn per MW, BGR Energy price-bid is 21% lower than BHEL and about 9% lower than L&T's 1st super-critical TG order (secured in Jun'08). Referring to the above orders, there is a likelihood of predatory pricing in turbine orders.

Name of Company	Order details	Order size (MW)	Order value (Rs Mn)	Rs Mn per MW
L&T	APPDC	2x800	15,570	9.7
BHEL	NTPC - Barh	2x660	14,740	11.2
Current order value				8.8

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What does it mean for the BTG equipment market?

Outcome of the NTPC 9X800 MW tenders (namely - Doosan Heavy in Boilers and BGR Energy in Turbine) splits-wide open the BTG equipment market. This certainly hints at hectic competition in near future market with disintegration of the market and fragmentation of market shares. Only positive outcome - pricing for the equipment is not very disruptive at this juncture on comparison with the order wins in recent past (taking cues from order wins of BHEL and L&T). This also indicates that, meaningful profits could be made by the L1 bidder in the current orders versus concerns of lower profitability. However, disintegration of market and presence of more participants could open intense competition in near future, which could impact pricing and profitability in the near future.

What does it mean for players?

BHEL – No surprises here, Emerges as L2

- Knowing the tender documents of 9X800 MW, preferential treatment for BHEL was given and window for winning few orders was known fact.
- However, not emerging as L1 and opening of the sector for larger-n-stiffer competition beyond the expected names emerged as greater risk to growth.
- Though, winning (most likely on matching L1 bids) 4X800 MW in Boilers and 2X800 MW in turbines has boosted the current order backlog, it increases probability for further loss of market shares for BHEL in future ordering in market place.
- Our concerns on BHEL are playing out and with near absence of re-rating catalyst, we retain a HOLD rating with price target of Rs2150/Share.

L&T – Still time to breathe, All is not gone

- Power equipment, though focus area for L&T, contributes miniscule to near-term earnings estimates and attracts only 3% (Rs15-20 bn) of total capital employed of the company.
- But, virtually not bagging any orders in 9X800 MW is negative for the power equipment business, since L&T was formidable contender in the race.
- This could invite changes in the business strategy and could lower expectations of returns in the business venture.
- At this juncture, L&T power business has adequate orders i.e. 5940 MW Boilers and 7540 MW turbines with total value of Rs127 bn for the 4000 MW facility at Hazira, Gujarat.
- Also, L&T with its full-scale EPC capabilities in power plant stands fair chance for order wins in tendering from private utilities. We retain 'BUY' rating with price target of Rs2015/Share.

Thermax – Time is ticking

- Time is ticking for Thermax - considering its ambitious venture in super critical boilers through 51:49 JV with Babcox & Wilcox.
- The venture will attract total investment of Rs7.5 bn for 3000 MW Boiler facility in phase 1. Assuming 1:1 debt-equity ratio and 51% in JV, equity investment of Rs1.9 bn is at risk, which implies 12% of the consolidated balance sheet.
- Certainly a large play on balance sheet considering market place heading for fragmentation and tough competition. Also, core business areas for Thermax like industrial boilers, utility boilers (below 100 MW) and waste heat recovery plants is witnessing unprecedented competition from different quarters.
- However, order wins have remained strong on YTD basis with Thermax remaining an exception in stock under- coverage, which remains only positive. Current, 1-year forward PER valuation of 12.7X is attractive for free cashflow generating and debt free balance sheet. We retain BUY rating with price target of Rs735/Share.

BHEL – Financial tables**Income Statement**

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Net Sales	333,549	424,955	497,265	558,006
Growth (%)	24.8	27.4	17.0	12.2
Expenditure	273,476	335,304	399,363	454,092
Materials Consumed	198,857	234,582	298,225	343,969
Employee Cost	64,492	54,104	64,969	69,200
Manufacturing Exp	8,460	15,341	18,422	21,248
Other Exp	1,668	31,278	17,748	19,675
EBITDA	60,072	89,651	97,901	103,915
Growth (%)	41.4	49.2	9.2	6.1
EBITDA Margin (%)	18.0	21.1	19.7	18.6
Depreciation	4,580	5,441	6,959	7,971
EBIT	55,492	84,210	90,942	95,944
EBIT Margin (%)	16.6	19.8	18.3	17.2
Other Income	2,593	2,378	2,822	3,355
Interest Expenses	-7,745	-3,493	-4,301	-4,301
PBT	65,831	90,081	98,065	103,600
Tax	23,192	30,759	33,486	35,375
Effective Tax Rate (%)	35.2	34.1	34.1	34.1
Adjusted PAT	42,639	59,321	64,579	68,224
Growth (%)	40.2	39.1	8.9	5.6
Net Margin (%)	12.8	14.0	13.0	12.2
E/O items	468	815	0	0
Reported PAT	43,106	60,136	64,579	68,224
Growth (%)	37.4	39.5	7.4	5.6

Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
PBT	65,907	90,081	98,065	103,600
Depreciation	4,312	5,441	6,959	7,971
Interest Provided	336	-3,493	-4,301	-4,301
Other Non-Cash Items	-3	-5,455	0	0
Change in working Capital	-27,428	-22,182	-17,064	-5,863
Tax paid	-19,035	-30,759	-33,486	-35,375
Operating Cash Flow	24,089	33,633	50,174	66,031
Capital expenditure	-17,137	-17,623	-12,000	-7,000
Free Cash Flow	6,952	16,010	38,174	59,031
Other Income	-493	0	0	0
Investments	-275	-3,593	0	0
Investing Cash Flow	-768	-3,593	0	0
Equity Capital Raised	0	0	0	0
Loans Taken / (Repaid)	-215	356	0	0
Interest Paid	-337	3,493	4,301	4,301
Dividend Paid (Incl Tax)	-10,879	-15,249	-16,619	-17,109
Others	0	0	0	0
Financing Cash Flow	-11,430	-11,400	-12,318	-12,808
Net Change in Cash	-5,246	1,017	25,855	46,223
Opening Cash Position	103,147	97,901	96,302	122,157
Cash & Cash Equivalents	0	0	0	0
Closing Cash Position	97,901	98,918	122,157	168,380

Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Equity Share Capital	4,895	4,895	4,895	4,895
Reserves & Surplus	154,278	196,643	244,603	295,719
Networth	159,174	201,538	249,499	300,614
Secured Loans	0	0	0	0
Unsecured Loans	1,278	1,634	1,634	1,634
Loan Funds	1,278	1,634	1,634	1,634
Net Deferred Tax Liability	-15,272	-21,636	-21,636	-21,636
Total Liabilities	145,179	181,536	229,497	280,612
Gross Block	65,801	83,424	95,424	102,424
Less: Depreciation	41,505	46,946	53,905	61,876
Net block	24,154	36,336	41,377	40,406
Capital Work in Progress	15,296	15,296	15,296	15,296
Investment	798	4,392	4,392	4,392
Current Assets	429,348	514,947	617,754	721,003
Inventories	92,355	109,630	131,647	147,962
Sundry Debtors	206,888	273,546	328,481	369,191
Cash & Bank Balance	97,901	96,302	122,157	168,380
Loans & Advances	28,137	32,373	32,373	32,373
Other Current Assets	4,069	3,096	3,096	3,096
Current Lia & Prov	324,417	389,434	449,321	500,484
Current Liabilities	280,237	313,466	373,353	424,516
Provisions	44,180	75,968	75,968	75,968
Net Current Assets	104,931	125,514	168,433	220,519
Miscellaneous Exp	0	0	0	0
Total Assets	145,179	181,536	229,497	280,612

Key ratios

Y/E, Mar	FY10	FY11P	FY12E	FY13E
Profitability (%)				
EBITDA Margin	18.0	21.1	19.7	18.6
Net Margin	12.8	14.0	13.0	12.2
ROCE	45.1	53.0	45.6	38.9
ROE	29.6	32.9	28.6	24.8
RoIC	390.5	174.1	118.7	106.5
Per Share Data (Rs)				
EPS	87.1	121.2	131.9	139.4
CEPS	96.5	132.3	146.1	155.7
BVPS	325.2	411.7	509.7	614.1
DPS	23.3	31.2	34.0	35.0
Valuations (x)				
PER	19.6	14.1	12.9	12.3
P/CEPS	17.7	12.9	11.7	11.0
P/BV	5.3	4.1	3.4	2.8
EV / Sales	2.2	1.7	1.4	1.2
EV / EBITDA	12.3	8.3	7.3	6.4
Dividend Yield (%)	1.4	1.8	2.0	2.0
Gearing Ratio (x)				
Net Debt / Equity	(0.6)	(0.5)	(0.5)	(0.6)
Net Debt / EBITDA	(1.6)	(1.1)	(1.2)	(1.6)
Working Cap Cycle (days)	7.7	25.1	34.0	34.1

L&T – Consolidated Financial tables

Income Statement

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Net Sales	436,989	520,991	622,428	717,662
Growth (%)	8.3	18.3	20.7	15.3
Expenditure	371,599	439,137	530,217	607,516
Materials Consumed	273,933	326,668	394,335	454,670
Employee Cost	30,661	38,020	45,895	52,917
Manufacturing Exp	22,140	22,660	27,354	31,539
Other Exp	44,865	51,790	62,634	68,390
EBITDA	65,390	81,855	92,211	110,146
Growth (%)	16.4	25.2	12.7	19.5
EBITDA margin (%)	15.0	15.7	14.8	15.3
Depreciation	9,793	13,197	19,289	27,007
EBIT	55,597	68,658	72,922	83,139
EBIT margin (%)	12.7	13.2	11.7	11.6
Other Income	5,442	4,920	11,058	18,008
Interest expenses	6,919	8,309	9,221	10,337
PBT	54,119	65,269	74,759	90,809
Tax	20,374	23,479	26,893	32,666
Effective tax rate (%)	37.6	36.0	36.0	36.0
Adjusted PAT	33,745	41,790	47,866	58,143
Growth (%)	15.7	23.8	14.5	21.5
Net Margin (%)	7.7	8.0	7.7	8.1
(Profit)/loss from JVs/Ass/MI	71	10	559	1,319
Adj. PAT After JVs/Ass/MI	33,816	41,800	48,425	59,462
E/O items	20,691	2,761	-	-
Reported PAT	54,507	44,562	48,425	59,462
Growth (%)	12.8	23.6	15.8	22.8

Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
PBT (Ex-Other income)	73,454	65,269	74,759	90,809
Depreciation	9,793	13,197	19,289	27,007
Interest Provided	6,919	8,309	9,221	10,337
Other Non-Cash items	-18,655	2,771	559	1,319
Chg in working cap	-28,318	-63,163	-55,397	-64,649
Tax paid	-17,547	-23,479	-26,893	-32,666
Operating Cashflow	25,647	2,904	21,538	32,158
Capital expenditure	-44,800	-62,057	-27,738	-28,280
Free Cash Flow	-19,154	-59,153	-6,200	3,878
Other income	0	0	0	0
Investments	-10,802	8,500	-1,368	-1,505
Investing Cashflow	-10,802	8,500	-1,368	-1,505
Equity Capital Raised	21,327	2,570	2,561	2,561
Loans Taken / (Repaid)	43,098	110,303	36,978	45,279
Interest Paid	-6,919	-8,309	-9,221	-10,337
Dividend paid (incl tax)	-7,219	-8,794	-10,553	-12,663
Income from investments	0	0	0	0
Others	114	786	532	-112
Financing Cashflow	50,402	96,556	20,298	24,727
Net chg in cash	20,446	45,903	12,730	27,101
Opening cash position	14,590	33,216	79,119	91,849
Closing cash position	33,499	79,119	91,849	118,950

Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Equity share capital	4,699	4,707	4,707	4,707
Reserves & surplus	205,214	243,543	283,977	333,337
Net worth	209,913	248,250	288,684	338,044
Minority Interest	10,873	11,658	12,190	12,078
Secured Loans	141,859	0	0	0
Unsecured Loans	84,701	0	0	0
Loan Funds	226,561	336,864	373,842	419,121
Net deferred tax liability	1,530	1,530	1,530	1,530
Total Liabilities	448,876	598,302	676,246	770,773
Gross Block	161,081	223,138	250,876	279,155
Less: Depreciation	37,476	50,673	69,961	96,969
Net block	123,605	172,465	180,914	182,187
Capital work in progress	66,184	66,184	66,184	66,184
Investment	99,279	90,779	92,147	93,652
Current Assets	417,009	535,845	644,818	764,799
Inventories	23,782	42,996	68,955	99,168
Sundry debtors	125,280	142,097	171,531	197,776
Cash & bank balance	33,216	79,119	91,849	118,950
Loans & advances	160,299	197,200	238,049	274,472
Other current assets	0	0	0	0
Current lia & Prov	257,201	266,971	307,817	336,048
Current liabilities	232,459	240,593	275,968	299,556
Provisions	24,743	26,378	31,849	36,492
Net current assets	159,808	268,874	337,001	428,751
Misc. exp	-	-	-	-
Total Assets	448,876	598,302	676,246	770,773

Key ratios

Y/E, Mar	FY10	FY11P	FY12E	FY13E
Profitability (%)				
EBITDA Margin	15.0	15.7	14.8	15.3
Net Margin	7.7	8.0	7.7	8.1
ROCE	15.6	14.3	13.5	14.2
ROE	19.3	18.2	18.0	19.0
RoIC	22.2	19.0	17.1	16.9
Per Share Data (Rs)				
EPS	56.2	68.9	79.8	98.0
CEPS	70.7	87.4	104.7	131.1
BVPS	348.6	409.3	476.0	557.4
DPS	12.5	14.5	17.4	20.9
Valuations (x)				
PER	28.7	23.4	20.2	16.4
P/CEPS	22.8	18.4	15.4	12.3
P/BV	4.6	3.9	3.4	2.9
EV / Sales	2.5	2.2	1.9	1.7
EV / EBITDA	16.5	14.1	12.8	10.9
Dividend Yield (%)	0.8	0.9	1.1	1.3
Gearing Ratio (x)				
Net Debt/ Equity	0.5	0.7	0.7	0.7
Net Debt/EBITDA	1.6	2.2	2.2	2.0
Working Cap Cycle (days)	113.6	151.7	177.6	194.7

Thermax – Consolidated Financial tables

Income Statement

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
Net Sales	33,678	53,350	59,763	66,143
Growth (%)	-2.5	58.4	12.0	10.7
Expenditure	29,524	47,495	52,746	58,334
Materials Consumed	20,452	36,474	40,262	44,559
Employee Cost	3,300	4,597	5,150	5,700
Manufacturing Exp	2,883	2,918	3,269	3,618
Other Exp	2,891	3,505	4,066	4,457
EBITDA	4,154	5,855	7,017	7,808
Growth (%)	-2.0	4.1	2.0	1.1
EBITDA margin (%)	12.3	11.0	11.7	11.8
Depreciation	442	541	584	610
EBIT	3,712	5,314	6,432	7,199
EBIT margin (%)	11.0	10.0	10.8	10.9
Other Income	314	467	539	582
Interest expenses	20	41	41	41
PBT	4,005	5,740	6,930	7,740
Tax	1,416	1,967	2,375	2,652
Effective tax rate (%)	35.4	34.3	34.3	34.3
Adjusted PAT	2,589	3,773	4,556	5,088
Growth (%)	-8.5	45.7	20.7	11.7
Net Margin (%)	7.7	7.2	7.7	7.8
(Profit)/loss from JVs/Ass/MI	-4	-47	-47	-47
Adjusted PAT After JVs/Ass/MI	2,593	3,820	4,603	5,135
E/O items	-1,150	-4	0	0
Reported PAT	1,443	3,817	4,603	5,135
Growth (%)	-50.0	164.4	20.6	11.6

Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
PBT	4,004	5,737	6,977	7,787
Depreciation	442	516	584	610
Interest Provided	20	41	41	41
Other Non-Cash items	133	-1,149	0	0
Chg in working cap	3,709	-910	491	241
Tax paid	-1,439	-1,911	-2,375	-2,652
Operating Cashflow	6,869	2,324	5,719	6,027
Capital expenditure	-840	-1,507	-500	-500
Free Cash Flow	6,030	818	5,219	5,527
Other income	0	0	0	0
Investments	-2,263	-544	0	0
Investing Cashflow	-2,263	-544	0	0
Equity Capital Raised	0	0	0	0
Loans Taken / (Repaid)	39	1,166	-1,400	0
Interest Paid	-20	-41	-41	-41
Dividend paid (incl tax)	-697	-695	-1,301	-1,338
Income from investments	-82	-84	0	0
Others	0	173.5	0	0
Financing Cashflow	-760	520	-2,742	-1,379
Net change in cash	3,006	794	2,477	4,147
Opening cash position	3,696	6,702	7,496	9,973
Closing cash position	6,702	7,496	9,973	14,121

Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
Equity share capital	238	238	238	238
Reserves & surplus	10,544	12,911	16,213	20,009
Net worth	10,782	13,149	16,451	20,248
Minority Interest	94	520	520	520
Secured Loans	80	1,476	76	76
Unsecured Loans	0	4	4	4
Loan Funds	80	1,479	79	79
Net deferred tax liability	144	298	298	298
Total Liabilities	11,099	15,447	17,349	21,145
Gross Block	7,418	10,677	11,531	12,031
Less: Depreciation	2,048	2,824	3,408	4,017
Net block	5,369	7,853	8,124	8,014
Capital work in progress	115	354	0	0
Investment	3,703	2,415	2,415	2,415
Current Assets	23,477	28,650	33,454	40,030
Inventories	4,916	6,155	6,225	6,890
Sundry debtors	7,984	10,672	12,706	14,062
Cash & bank balance	6,702	7,496	9,973	14,121
Loans & advances	3,282	3,596	3,819	4,226
Other current assets	594	731	731	731
Current lia & Prov	21,566	23,826	26,644	29,314
Current liabilities	20,581	22,193	25,011	27,681
Provisions	985	1,633	1,633	1,633
Net current assets	1,912	4,824	6,810	10,716
Misc. exp	0	0	0	0
Total Assets	11,099	15,447	17,349	21,145

Key ratios

Y/E, Mar	FY10	FY11	FY12E	FY13E
Profitability (%)				
EBITDA Margin	12.3	11.0	11.7	11.8
Net Margin	7.7	7.2	7.7	7.8
ROCE	38.0	43.6	42.5	40.4
ROE	24.4	28.8	28.1	26.7
RoIC	137.8	184.5	126.8	150.4
Per Share Data (Rs)				
EPS	21.8	32.1	38.6	43.1
CEPS	25.5	36.6	43.5	48.2
BVPS	90.5	110.4	138.1	169.9
DPS	6.0	9.0	10.9	11.2
Valuations (x)				
PER	23.1	15.7	13.0	11.7
P/CEPS	19.7	13.7	11.6	10.4
P/BV	5.6	4.6	3.6	3.0
EV / Sales	1.5	1.0	0.8	0.7
EV / EBITDA	11.9	8.8	6.8	5.6
Dividend Yield (%)	1.2	1.8	2.2	2.2
Gearing Ratio (x)				
Net Debt/ Equity	-1.0	-0.6	-0.7	-0.8
Net Debt/EBITDA	-2.5	-1.4	-1.8	-2.1
Working Cap Cycle (days)	29.8	23.0	35.5	48.4

Emkay Global Financial Services Ltd.

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