

CMP Rs 317
Rating BUY
Target Rs 680 (+115%)



D. S. KULKARNI DEVELOPERS LTD

DSK IN (Bloomberg) / DSKL.BO (Reuters)

On wings of expansion beyond Pune

November 17, 2006

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Disclaimer & disclosures

This report must be read with the disclaimer and disclosures on the last page that form part of it

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D. S. KULKARNI DEVELOPERS LTD



Bloomberg code :
Reuters code :
www.dskdl.com

DSK IN
DSKL.BO

BSE Sensex :
NSE Nifty :

13,506
3,877

Company data

O/S shares :
Market cap (Rs) :
Market cap (US\$) :
52 - wk Hi/Lo (Rs) :
Avg. daily vol. (3mth) :
Face Value (Rs) :

22mn
7bn
155mn
446 / 91
217,698
10

Share holding pattern, %

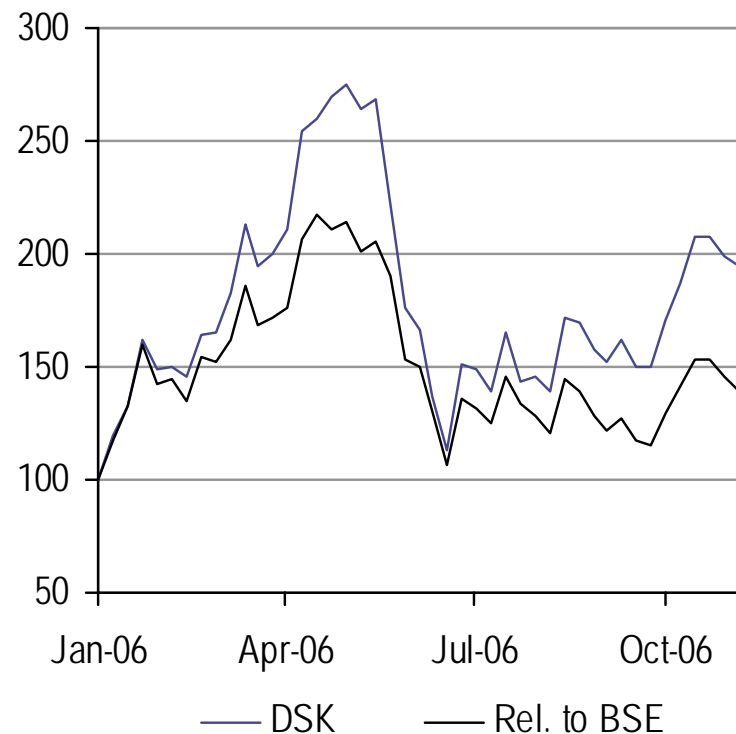
Promoters :
FII / NRI :
FI / MF/ Banks :
Pvt. Corp. Bodies :
Public & Others :

21.42
41.82
11.4
4.95
20.41

Price performance, %

	1mth	3mth	1yr
Abs	-0.6	18.4	198.4
Rel to BSE	-5.4	0.7	142.4

Price vs. Sensex



Source: Bloomberg, Man Financial Research

Investment argument

- DSKDL is a niche real estate company with more than 90% of its interests in residential properties in and around Pune. However, it is spreading its wings in Mumbai, Bangalore, Hyderabad, Delhi, and USA.
- The company has constructed and handed over 15,000 tenements (approximately 12.5 mn sq. ft) in the past.
- The company's ongoing projects indicate that it will build on an average 4 mn sq. ft. of property for the next four years, including FY07; 90% of these tenements are in and around Pune.
- The company has a unique policy of transferring acquired land at a significant discount to the market price to DSKDL and the management says that it will continue with this policy in the foreseeable future.
- The company is known for its innovative customer-centric approach and has also three quality certifications (the only construction company to have these)
- The company has 650 acres (28.3 mn sq. ft, based on FSI of 1) of unused land spread across Pune, Mumbai, and Bangalore which is lying vacant and projects on this land are presumed to begin six years from FY07.
- NPV of ongoing projects and unused land with 35% discount comes to Rs 688, a 115% premium to CMP of Rs 317. We have debited Rs 17.5bn for consideration paid to privately held companies.
- The management indicates that it will go through the SPV route for undertaking larger projects in future wherein it will maintain 75-80% of the equity interest while the rest is offloaded in favour of a VC partner after valuing the specific project
- Above NPV does not take into account the upside from projects in Hyderabad (400 acres land), Delhi (500 acres), and the project in the US (3,000 acres land bank) to construct 280 villas in Connecticut.
- Risks: Overdependence on Pune's residential real estate market, transfer pricing policies, propensity to fund larger working capital in order to take advantage of rising residential property prices trend. Pune is a developing market for IT and ITES industry with demand-supply favouring the rising price trend. The company's past transfer pricing arrangements have been transparent benefiting shareholders of DSKDL and management indicates those to continue in foreseeable future.

Valuation Summary

Y/E Mar, Rs mn	FY05	FY06	FY07E	FY08E	FY09E	FY10E
Net Sales	534	1,330	2,772	4,298	7,610	9,558
Growth, %	4.5	149.0	108.5	55.0	77.1	25.6
Core EBIDTA	67	216	713	1,477	2,543	4,231
EBIDTA margins, %	12.5	16.2	25.7	34.4	33.4	44.3
Net profit	37	176	413	956	1,472	2,595
EPS, Rs	3.3	16.0	25.0	43.5	66.9	117.9
EPS Growth, %	146.7	378.7	56.4	73.7	53.9	76.3
PER, x	94.8	19.8	12.7	7.3	4.7	2.7
EV/EBIDTA, x	61.3	20.6	9.9	5.8	4.6	3.0
EV/Net Sales, x	7.7	3.3	2.5	2.0	1.6	1.3
Price/Book Value, x	15.9	10.1	5.8	4.1	2.3	1.3
ROIC, %	5.5	9.1	15.2	25.6	21.6	27.4
ROE, %	16.8	51.1	45.9	56.8	49.4	48.6
Dividend Yield, %	0.3	1.4	1.0	0.7	0.8	0.8

Source: Man Financial Research

Introduction - DSKDL

- Mr. D.S Kulkarni, Chairman & Managing Director - DSKDL, is a first-generation entrepreneur. He started his career in 1970, at the age of 20, with a modest business of cleaning and perfuming telephones under the name of " Tele-Smell ".
- This business was followed by painting, plumbing, electrical works, interior works, and house repairs. This is how he learned the functional aspects of an accomplished house.
- Subsequently, he ventured into construction in 1981.
- The flagship company D. S. Kulkarni Developers Ltd. (DSKDL) was incorporated in 1991.
- DSKDL has constructed and handed-over more than 15,000 tenements, approx. (12.5 mn) sq. ft. of constructed are since then.
- DSKDL is well known for many innovative, transparent, and customer friendly initiatives.

Introduction - DSKDL

- DSKDL is the only construction company with three quality certifications – ISO 9001:2000, 14001:2004 and OHSAS 18001:1999.
- 70% of its customers are NRIs from USA, UK, Dubai, Bahrain, Kuwait, Kenya and Australia
- Currently, its projects are in full-swing at Pune, Mumbai, and Bangalore. All three are strategic locations since the service industry dominates in these regions.
 - ✓ Hyderabad – Development of 400 acres of land (via agreement with an international institution) and consequent sale of properties is awaiting regulatory approvals
 - ✓ Delhi – 500 acres of land – strategically located near NH-24 at a distance of 30 kms from Connaught Place
- DSKDL has recently floated a 100% subsidiary in USA, to take up the residential projects there. USA – land bank of 3,000 acres (280 villas in Connecticut)
- Similar forays are planned for Middle East and Australia.
 - ✓ Australia – coming up with residential projects
 - ✓ Middle East – planning to enter the piling work as contractors (management intends to take advantage of high margins that this activity enjoys)

Shareholder friendly transfer pricing policy and customer friendly approach



- Transfer pricing mechanism of land held by privately held or proprietary companies
 - ✓ Transfer Price = [Acquisition cost (including the expenses to get the land cleared)+ carrying cost+ interest burden + 15-20% margin] or the market price, whichever is lower. (Typically, the land transfer has taken place at a discount of 50% to the market price)
- DSKDL does not invite/market any pre-launch advance bookings.
- It arranges self-exhibitions at a large scale displaying project models, perspectives and also offers simultaneous bookings from different cities and locations.
- DSKDL has got a unique policy of imposing a self-penalty in case of delay in delivery of project in the presence of thousands gathered for the ground breaking ceremony.
- DSKDL has a policy of displaying the completed building for two days to the public at a large scale — showcasing its workmanship, quality of construction, and delivery of commitment.

Shareholder friendly transfer pricing policy and customer friendly approach



- DSKDL is well known for its customer-centric approach. The company has got a customer care division that arrange customers' meets and get together at its project sites during the construction period.
- DSKDL provides after sales service to its customers beyond the committed period. The company not only keep written and oral commitments, but goes beyond that by helping its customers in their social aspects and fulfilling their basic needs like opening bank accounts, cooking gas connections, telephone connections, payment of electricity/telephone bills, and other outgoings, etc.

ORGANISATION CHART D.S.KULKARNI DEVELOPERS LTD.



Management

BOARD OF DIRECTORS

**D.S.KULKARNI
CHAIRMAN & MD.**

**H.D.KULKARNI
PRESIDENT**



**RABINDER SINGH
CTO
PUNE**

**SUMIT ARORA
VP - BUSINESS DEVE.
MUMBAI**

**SHRIKANT BHAGAVAT
ASSOCIATE
BANGALORE**

**SUNIL DOMALE
CAO
PUNE**



**N.M.PHADKE
VP-ENGG.
MUMBAI**

**HRC RAO
CEO, BANGALORE**

**P.S.KULKARNI
VP ISD**

**S.N.KULKARNI
VP SECRETARIAL**



**R.D.NEWASKAR
VP PLANNING & BUDGET**

**M.B.BANHATTI
VP EXECUTION**

**G.K.KENJALE
VP QUALITY & MAINTENANCE**

**A.R.PURANDARE
VP ACCOUNTS**

**S.B.PUROHIT
VP HR & ADMIN**

**G.V.PATIL
VP MARKETING**

**K.P.VANJAPE
VP LEGAL**



Current Projects

- DSK Vishwa - IT Park
 - ✓ Sinhadgad Road, Pune
 - ✓ Salable Area 1,200,000 sq. ft.
 - ✓ Sales revenue expected -- Rs 3.6bn (US\$ 78.26mn)
 - ✓ 13 storied – 4 towers
 - ✓ Probably the largest floor plate IT park in India - 79,000 sq. ft. - equipped with all modern amenities
 - ✓ Possession by December 2007

- DSK Garden Enclave Kondhwa, Pune
 - ✓ Salable Area 244,176 sq. ft.
 - ✓ Sales revenue expected -- Rs 549 mn
 - ✓ 176 designer apartments
 - ✓ Possession by December 2007

Current Projects

- DSK Madhuban, Andheri (E), Near International Airport, Mumbai
 - ✓ Salable area – 309,024 sq. ft.
 - ✓ Sales revenue expected – Rs 1.24bn (US\$ 26.87mn)
 - ✓ 252 elegant apartments
 - ✓ Possession by February 2008

- DSK Saptasur (Vishwa Ph. IV) Sinhagad Road, Pune
 - ✓ Salable area – 475,496 sq. ft.
 - ✓ Sales revenue expected -- Rs 785mn
 - ✓ 418 Nos. – 1/2/3 BHK Apartments
 - ✓ Possession by December 2007

- DSK Sayantara, Sinhagad Road, Pune
 - ✓ Salable area – 494,463 sq. ft.
 - ✓ Sales revenue expected Rs 451mn
 - ✓ Bungalow plots – 132 nos.

Current Projects

- DSK Sundarban, Hadapsar, Pune
 - ✓ Salable area – 626,016 sq. ft.
 - ✓ Sales revenue expected -- Rs 1.0bn
 - ✓ Cozy township of 600 apartments & shops
 - ✓ Possession by December 2007

- DSK Rohan, Model Colony, Pune
 - ✓ Salable area -- 14,997 sq. ft.
 - ✓ Sales revenue expected -- Rs 43mn (US\$ 0.9 mn)
 - ✓ Premium Apartments in prime location
 - ✓ Possession by December 2006

Current Projects

- DSK Frangipani, Camp, Pune
 - ✓ Salable area – 134,220 sq. ft.
 - ✓ Sales revenue expected -- Rs 537mn (US\$ 11.67mn)
 - ✓ 80 super luxurious apartments
 - ✓ Possession by December 2006

- DSK Fortuna, Sarjapura Road, Bangalore
 - ✓ Salable area – 117,394 sq. ft.
 - ✓ Sales revenue expected -- Rs 305mn (US\$ 6.63mn)
 - ✓ Premium residential apartments
 - ✓ Possession by December 2008

Upcoming Projects

- DSK Torino, Mysore Road, Bangalore
 - ✓ Salable area -- 290,400 sq. ft.
 - ✓ Sales revenue expected -- Rs 697mn (US\$ 15.15mn)
 - ✓ Residential cum commercial complex
 - ✓ Expected to commence soon

- DSK Project, Balewadi, Pune
 - ✓ Salable area – 825,100 sq. ft.
 - ✓ Sales revenue expected -- Rs 2.04bn (US\$ 44.39 mn)
 - ✓ Residential complex
 - ✓ Expected to commence soon

Upcoming Projects

- DSK Sapphire, Wakad, Pune
 - ✓ Salable area – 78,664 sq. ft.
 - ✓ Sales revenue expected -- Rs 197mn (US\$ 4.28 mn)
 - ✓ Residential complex
 - ✓ Expected to commence soon

- DSK Empire, Furusungi, Pune
 - ✓ Salable area – 7,677,450 sq. ft.
 - ✓ Sales revenue expected -- Rs 28.41bn (US\$ 617.53mn)
 - ✓ Commercial plaza and special integrated township
 - ✓ Expected to commence soon

Roadmap Up to Financial Year Ending 31st March 2012

Total area to be developed/constructed (as on date). 95% of this is in and around Pune	17,440,007 sq. ft.
Work – in – progress (out of above)	4,537,016 sq. ft.
Work to be commenced shortly	12,902,991 sq. ft.
Total sales proceeds expected from sale of above starting with FY 2005-06 up to FY 2011-12	Rs mn 51,302
Total profit before tax expected from sale of above starting with FY 2005-06 up to FY 2011-12	Rs mn 18,213

Source: Man Financial Research

Valuation thesis

Ongoing projects - I

Development Schedule	FY07E	FY08E	FY09E	FY10E	Terminal Value
(mn. Sq ft project completions)	4	4	4	4	4
Pune					
Average Selling price (sq ft)	2,500	2,625	2,756	2,894	3,039
Less:					
Construction Cost (sq ft)	1,225	1,313	1,378	1,447	1,519
% of sales	49%	50%	50%	50%	50%
Development Cost (sq ft)	109	131	138	145	152
% of sales	4%	5%	5%	5%	5%
Selling & Admin Cost (sq ft)	60	66	69	72	76
% of sales	2%	3%	3%	3%	3%
Operating Profit	1,106	1,116	1,171	1,230	1,291
Tax outgo	111	335	351	369	387
Tax rate	0.1	0.3	0.3	0.3	0.3
Net cash / sq ft	996	781	820	861	904

Source: Man Financial Research

Valuation thesis

Ongoing projects - I

Development Schedule	FY07E	FY08E	FY09E	FY10E	Terminal value
Mumbai					
Average Selling price (sq ft)	4,000	4,200	4,410	4,631	4,862
Less:					
Construction Cost (sq ft)	1,200	1,302	1,367	1,435	1,507
% of sales	30%	31%	31%	31%	31%
Development Cost (sq ft)	100	126	132	139	146
% of sales	3%	3%	3%	3%	3%
Selling & Admin Cost (sq ft)	180	210	221	232	243
% of sales	4%	5%	5%	5%	5%
Operating Profit	2,520	2,562	2,690	2,825	2,966
Tax Outgo	252	769	807	847	890
Tax rate	0.1	0.3	0.3	0.3	0.3
Net cash / sq ft	2268	1793	1883	1977	2076

Source: Man Financial Research

Valuation thesis

Ongoing projects - I

Development Schedule	FY07E	FY08E	FY09E	FY10E	Terminal value
Bangalore					
Average Selling price (sq ft)	2,500	2,625	2,756	2,894	3,039
Less:					
Construction Cost (sq ft)	1,067	1,155	1,213	1,273	1,337
% of sales	43%	44%	44%	44%	44%
Development Cost (sq ft)	92	131	138	145	152
% of sales	4%	5%	5%	5%	5%
Selling & Admin Cost (sq ft)	115	131	138	145	152
% of sales	5%	5%	5%	5%	5%
Operating Profit	1,227	1,208	1,268	1,331	1,398
Tax Outgo	123	362	380	399	419
Tax rate	0.1	0.3	0.3	0.3	0.3
Net cash / sq ft	1,104	845	888	932	978

Source: Man Financial Research

Valuation thesis

Ongoing projects - I

Development Schedule	FY07E	FY08E	FY09E	FY10E	Terminal value
Weighted Net Cash / sq ft	1,021	800	840	882	927
Discount rate (%)	0.15	0.15	0.15	0.15	0.15
NPV / sq ft	1,021	697	637	583	
NPV (Rs mn)	4,083	2,788	2,549	2,330	
TV / sq ft					9,411
TV (Rs mn)					37,645
NPV - TV (Rs mn)					21,640
NPV - Total (Rs mn)	33,390				

Source: Man Financial Research

Underlying Assumptions

- **Project completion:** We have taken an average 4-mn sq ft of completion in a year, as indicated by the management.
- **Revenue assumption:** 95% of the company's projects are residential in nature. We have used the average selling price currently prevailing in three cities i.e. Pune, Mumbai & Bangalore (the cities in which the company has presence) in FY07E. Beyond FY07E, we have taken a 5% increase in the selling price for each year.
- **Costs assumption:** We have maintained all the costs viz. construction cost, development cost and selling and administrative cost as a % of sales for all the years.
- **Tax Rate:** We have taken a tax rate of 10% for FY07E and assumed a tax rate of 30% beyond FY07E due to discontinuation of Section 80IB. The management has indicated that the benefit of Section 80 IB might be extended or they might qualify under MAT (tax rate @ 12.5%). But, we have taken the tax rate @ 30% on a conservative basis.
- **Weighted average method:** We have arrived at the weighted net cash/sq ft, using the distribution proportion of the ongoing projects in the cities. The ongoing projects encompass a total salable area of 17.44 mn sq ft with 96% coming from Pune alone and 2% each from Mumbai and Bangalore.
- **Discount Rate:** We have taken the cost of equity as 14.85% for the purpose of discounting. We have arrived at the same by taking the risk-free rate @ 7.5% and the risk premium of 7.35% [obtained by multiplying the risk premium of 6.5% and beta of 1.13 (source: Bloomberg)]

Valuation thesis

- The company has 650 acres (28.3 mn sq ft, based on the FSI of 1) of land spread across Pune, Mumbai and Bangalore, which is lying vacant and projects on this land are presumed to begin six years from FY07

Vacant land bank valuation - II

Weighted Net Cash / sq ft	803
Discount rate	14.85
No. of years discounting	6
NPV/sq ft	350
Total no of mn sq ft	28
NPV of land bank (Rs mn)	9,912

Source: Man Financial Research

Underlying Assumptions

- Net cash/ per sq ft
 - ✓ We have taken the weighted net cash per sq ft. on the basis of the proportion of the land bank in the cities of Pune (92%), Mumbai (2%) and the remaining (5%) from Bangalore.

- Discount rate
 - ✓ We have taken the cost of equity as 14.85% for the purpose of discounting. We have arrived at the same by taking the risk-free rate @ 7.5% and the risk premium of 7.35% [obtained by multiplying the risk premium of 6.5% and beta of 1.13 (source: Bloomberg)]

- Period of discounting
 - ✓ We have taken six years for the purpose of the idle land bank on a conservative basis. Typically, it takes three years to develop a residential project starting from the scratch.

Composite valuation - III

	Rs mn
NPV of land bank (Rs mn)	9,912
NPV of ongoing projects (Rs mn)	33,390
Less: Existing Debt + Rs 1bn for forthcoming projects	2,042
Less: Existing Customer Advances	739
Less: Consideration to be paid to privately held companies on account of transfer of land	17,500
Implied Market value	23,021
Number of O/S shares (mn)	22
NPV /share	1046
CMP (Rs)	317
Premium / Discount to NPV	-70%
35% discount to NAV	680
Potential Upside	115%

Source: Man Financial Research

Underlying Assumptions

- **Transfer Price**
 - ✓ The land bank is with the privately held companies of promoters. The company follows the policy of transferring the land at a transfer price of discount to the existing market value (~ Rs 35 bn). We have taken a discount of 50% to the current market value, hence arriving at a value of Rs 17.5bn.

- **Discount to NPV**
 - ✓ We have taken a discount of 35% to the existing NPV (as against the normal 20-25% discount witnessed in the industry). However, there is ~ 115% upside potential from the current levels even after taking a conservative discount rate of 35%.

Risk factors

- DSKDL's business operations are concentrated in just one city, albeit, with significant demand potential. However, the management is taking steps to expand into Mumbai, Bangalore, Delhi, Hyderabad, and overseas. As such, ongoing projects are subjected to price volatility in the Pune market.
- The management sells a major portion of tenements in any project only after 90% completion. This will benefit the company in the rising prices scenario. This also means higher working capital requirement for the company as against the norm of the industry to pre-sell the tenements
- Because of the archaic land-holding regulations in India, the land bought in the individuals name or in a private company's name has to be transferred to DSKDL at a transfer price. It is to the management's credit, that till now such transfer has taken place at rates substantially lower than then prevailing market rates. Management has indicated that they would like to continue the same policy in future.
- Mr Kulkarni's wife is administratively involved in the company.

Dynamics of Pune real estate market

■ Demand

- ✓ The leasing activity has remained subdued compared to previous quarters resulting in an absorption of approximately 5,00,000 ft². Demand was mainly driven by IT/ITES and spread across sectors like BPO and research laboratories. The absorption was approximately 45% by IT/ITES and 5% by the manufacturing sector in Pune, Magarpatta city and Kalyani Nagar are reported to have captured most of the office space demand.

■ Supply

- ✓ Although there have been no significant additions (approximately 0.6 million sq.ft.) to supply levels during the quarter, there is an expectation towards infusion of about 6.75 million ft² of supply through 2006 to end-2007. As per market information, commitments have already been made for approximately 1.5 million ft². Thus, the net supply for the next two years is estimated at about 5.25 million ft². Further, several developers have acquired land parcels for built-to-suit constructions, with a total building capacity for approximately 3.2 million ft². With large scale supply additions described hitherto; the prices are likely to remain stable in Pune in the medium term.

- Values

- ✓ Capital values across the micro-markets have remained stable during the quarter. The values of prime properties at Camp and on Bund Garden Road command high capital values, estimated to be in the range of Rs 4,300–4,700/ft² (US\$ 97- 106/ft²). Average capital values of Grade-A properties in Deccan have remained stable and are estimated to be in the range of 3,200–3,500/ft² (US\$ 72-79/ft²). Values at the suburban micro-market of Aundh have increased marginally and are in the range of Rs 2,900–3,200/ft² (US\$ 65-72/ft²) while those at Kalyani Nagar also have increased marginally at Rs 2,500 – 2,800/ft² (US\$ 56-63/ft²).

** Note: Data for the above analysis is for Q1CY06*

Source: Cushman & Wakefield

Past Projects

- DSK Raanwara, Bavdhan, Pune
 - ✓ An eco – friendly township. Winner of various awards.
- DSK Akashganga, Aundh, Pune
 - ✓ A residential complex situated in the prestigious locality of Pune
- DSK Vasant Vaibhav, Model Colony, Pune
 - ✓ A nine storied building
- DSK Chandradeep, Mukundnagar, Pune
 - ✓ Sold 150 flats in just 1 1/2 hour.
- DSK Gandharva Heights, Shivajinagar, Pune
 - ✓ State of the art commercial complex situated in the heart of Pune
- DSK Trilok, Dadar, Mumbai
 - ✓ A residential complex located in the central suburb Mumbai.
- DSK Sahil, Vile Parle, Mumbai
 - ✓ Located in the western suburb of Mumbai.

Awards & Recognitions

- HIND RATTAN Sword of Honor award conferred at Bahrain
- Entrepreneurs' International Award
- The Company is considered as a global growth company by world renowned, Switzerland based World Economic Forum
- Conferred prestigious award of C. M. Shah BEST CONCRETE TECHNOLOGY for the year 1999 by the Institute of Engineers, Pune
- DSKDL having ISO 9001 : 2000, ISO 14001 : 2004, OHSAS 18001 : 1999 Certification.
- AESA award for Best Architect Design and Landscaping Award for DSK Raanwara Project.
- Best Industrial Building Award and Best Fascia Glazing Award for building DSK Toyota by All India Association of Construction Contractors.
- Recognition by Guinness Book of World records for its record breaking booking of 1000 flats in a week for its DSK Vishwa Phase-I.

THANK YOU

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