



Initiating Coverage Report on Finolex Cables Ltd.

Recommendation: STRONG BUY

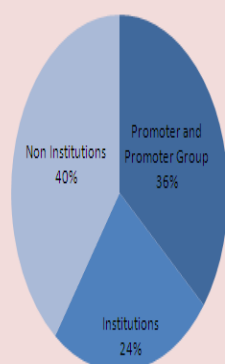
TARGET PRICE: INR 333

STRONG BUY

Market Data

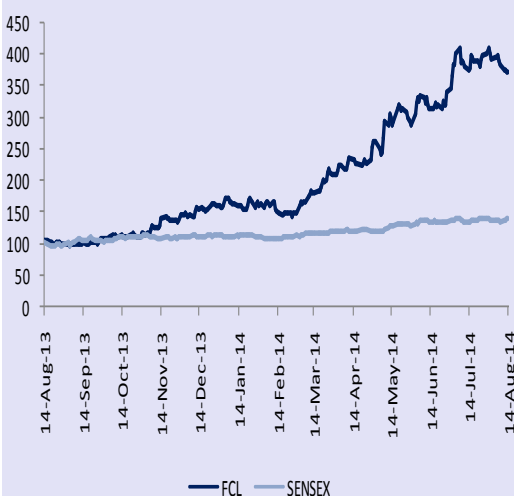
Current Market Price (INR)	194.0
Price Objective(INR)	333.3
Upside Potential (%)	71.8%
52 Week High (INR)	219.0
52 Week Low (INR)	49.7
Market Capitalization (In INR Cr)	2,967.2

Shareholding



STOCK SCAN

BSE Code	500144
NSE Code	FINCABLES
Bloomberg Ticker	FNXC.IN
Reuters Ticker	FNXC.BO
Face Value (INR)	2.0
Equity Share Capital (In INR Cr)	30.6
Average P/E	9.2x
Beta vs Sensex	0.7
Average Daily Volume (000's)	128.5
Dividend Payout Ratio	13.0%
Debt/Equity Ratio	0.4



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18th August 2014

Finolex Cables Ltd

Sector – Industrial

Finolex Cables Ltd (FCL) is one of India's largest manufacturers of electrical and telecommunication cables with 9% market share across India. FCL holds a strong brand image and value and it has manufacturing facilities at Pimpri and Urse in Pune as well as at Goa & Uttarakhand and operates under three main divisions namely: ECS, CCS, CCR and Others. It has 3,500 dealers and distributors in its traditional strongholds of South and West India and recently added over 500 channel partners in North. **We expect it to post healthy 18.3% revenue CAGR over FY14-FY17E. With strong backward integration coupled with product visibility in the west & southern region, operating margin is likely to improve by 58 bps, driving a net profit CAGR of 22.3% over FY14-FY17E. Lower working capital and capex would improve the return ratios and free cash flow in the near to longer time. We see upside momentum of FCL's earning for FY15E. Therefore we initiate coverage on FCL with a "STRONG BUY" recommendation and a target price of INR 333.**

Investment Highlights

Low capex and working capital needs coupled with healthy volume will drive return ratios-FCL poised to grow its revenue at a strong pace of 15% CAGR over FY2013-17E respectively, on the back of healthy product mix. FCL's entry into switchgear business will enhance its ROE and lead to a re-rating of the stock. Management believes that they could leverage their current distribution strength of over 4,000 dealers to make a foray in the switchgear market. We expect EBITDA to post a 16.4% CAGR over FY13-FY17E. We expect EBITDA margin to improve by 41 bps and 13 bps in FY15, FY16 respectively. There will be no major capex over FY 15-17E.

Derivative Losses- "Things of the past"-FCL's worries were largely on account of its forex losses amounting INR 3.1Bn over FY06-13. This constituted a serious overhang on valuations as the extent of losses suffered on account of these derivatives was uncertain. Currently, FCL has wound down such exposure, risk of further forex fluctuation losses have subsided. The absence of this augurs well for FCL's valuation which had taken a hit owing to such losses.

To boost margin FCL has decided to reduce sale of copper rods to third party-FCL manufactures copper rods, the raw material for its EWC products, thereby facilitating backward integration. A rated capacity of 60,000 tons and current utilisation of 60% allows it to control the quality and cost of its most crucial input. Any excess production of copper rods after captive consumption is sold off to third parties at market price.FCL is gradually reducing its exposure to the segment due to thin margins from third party transactions. We expect this trend to continue and thereby improving the margin of the company.

Sizeable hidden value-FCL has a 32% stake in Finolex Industries which it shows on its books as a historical cost of investment. We take 50% market value of the investment in our valuation model.FCL has a freehold land near Pimpri,Pune which it could monetize.

Key Financials Highlights

(Figure in INR CR)

Key Financials *	FY 10A	FY 11A	FY 12A	FY 13A	FY 14A	FY 15E	FY 16E	FY 17E
Net sales	1618.7	2035.8	2064.2	2270.7	2359.0	2628.6	3291.0	3904.6
%Growth		25.8%	1.4%	10.0%	3.9%	11.4%	25.2%	18.6%
EBITDA	195.2	171.7	175.0	228.7	247.1	286.3	362.7	420.5
EBITDA Margin %	12.1%	8.4%	8.5%	10.1%	10.5%	10.9%	11.0%	10.8%
Adjusted PAT	57.6	86.8	98.2	145.3	207.7	235.8	299.7	361.0
%Growth		50.6%	13.1%	47.9%	43.0%	13.6%	27.1%	20.5%
Net profit margin %	3.6%	4.3%	4.8%	6.4%	8.8%	9.0%	9.1%	9.2%
EPS (based on Adj.Pat)*	3.8	5.7	6.4	9.5	13.6	15.4	19.6	23.6
Book value per share *	42.0	46.9	52.3	60.4	72.1	85.6	102.9	123.6
Return on equity	20.8%	16.9%	16.8%	18.2%	17.9%	18.0%	19.0%	19.1%
P/E	15.38	9.27	5.37	5.45	10.05	12.58	9.97	8.22
P/BV	1.38	2 - 1.12	0.66	0.86	1.89	2.27	1.90	1.57
EV/EBITDA	6.91	7.48	5.11	5.39	10.05	11.40	9.14	7.61

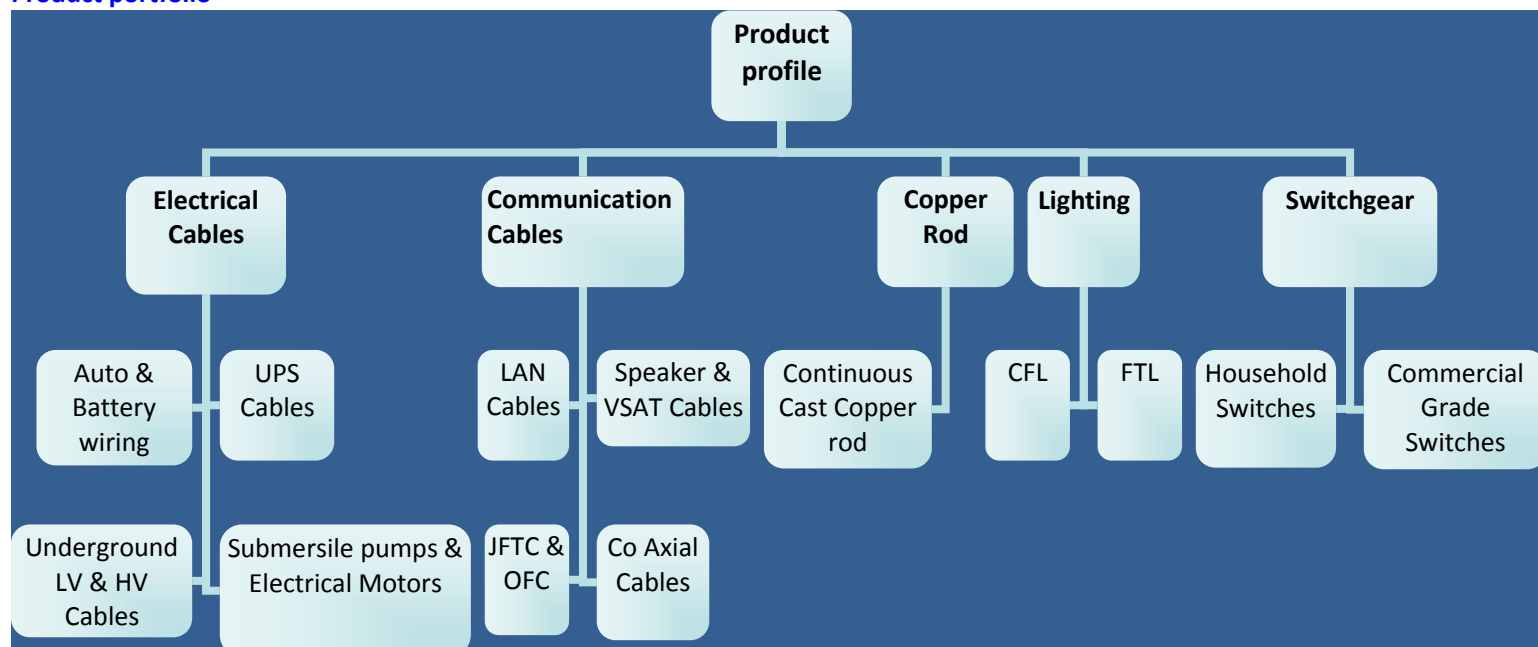
Source: Company, Microsec Research

Microsec Research

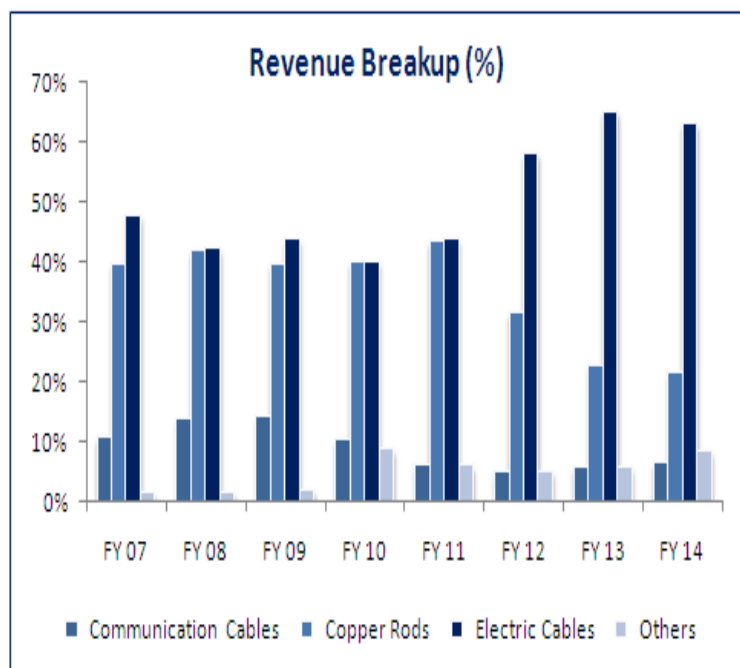
Investment Rationale

Low capex and working capital needs coupled with healthy volume will drive return ratios- FCL poised to grow its revenue at a strong pace of 15% CAGRs over FY13-17E, respectively, on the back of healthy product mix. FCL's entry into switchgear business will enhance its ROE and lead to a re-rating of the stock. Management believes that they could leverage their current distribution strength of over 4,000 dealers to make a foray in the switchgear market. We expect EBITDA to post a 16.4% CAGR over FY14-FY17E. We expect EBITDA margin to improve by 41 bps and 13 bps in FY15, FY16 respectively. There will be no major capex over FY 15-17E. FCL has outlined a capex of INR 1Bn to set up a new EWC plant in Roorkee, Uttarakhand which is expected to operationalise by Q1FY15, the plant is expected to boost production.

Product portfolio-



Source: Company, Microsec Research



Source: Company, Microsec Research

Among the product portfolio Electric cable segment contributes 63% of the total revenue with stable growth. The segment witnessed 22% CAGR of revenue growth for the last 5 years. Electric cable segment enjoys an EBIT margin of 10-11%, which is highest in the industry. This segments realization depends on prices of LME copper as it constitutes 70-78% of the total raw material costs.

Copper rods segment contributes 22% of the total revenue. FCL manufactures copper rods, the raw material for its EWC products, thereby facilitating backward integration. A rated capacity of 60,000 tons and current utilisation of 60% allows it to control the quality and cost of its most crucial input. Any excess production of copper rods after captive consumption is sold off to third parties at market price.

FCL also manufactures communications cables, which comprise 7% of its turnover. This is largely a tender based business. FCL was awarded a purchase order of over INR 2 Bn for Metal Free Optical Fibre Cable (OFC) under the National Optic Fiber Network (NOFN) project.

Electric Cables portfolio –

Electric cables (EC) segment is the main revenue driver for FCL, contributes 63% of the total revenue, EBIT margin of 10-11% and a ROCE of 48%. Electrical cables categorised into light duty electrical cables, power and control cables. Light duty electrical cables include electrical wires used extensively for electrification of industrial establishments, electrical panel wiring in industrial establishments and major equipments, consumer durable goods, automobiles, agricultural pump sets, small generator applications besides general lighting purposes. In power cable category, the Company has the ability to manufacture such cables within the range 1.1 kV to 66 kV. Power cables above 3.3 kV rating are meant for use in underground application for intra-city electricity distribution network.

FCL's 50% of the revenue comes from B2C segment (Dealer and retail network); while rest 50% of the revenue comes from B2B segment such as from construction, automotive, industrial customers. The segment witnessed 22% CAGR of revenue growth for the last 5 years. We expect FCL poised to grow at 15-20% once growth revives in the user industry. FCL manufactures copper rods, the raw material for its EWC products, thereby facilitating backward integration. **A rated capacity of 60,000 tons and current utilisation of 60% allows it to control the quality and cost of its most crucial input. Any excess production of copper rods after captive consumption is sold off to third parties at market price. This segments realization depends on prices of LME copper as it constitutes 70-78% of the total raw material costs. When the copper price increases, FCL able to pass on the incremental cost with a lag of 25-30 days and when the copper price soften than inventory piled up for price correction.**

FCL stands to benefit from the expected revival in user industries such as construction, power, telecom and automobile as the company largely depends on incremental demand from the user industry. **FCL has strong presence in the southern and western part of India where FCL established itself as a strong brand. For electric and cable business, 50% of the demand comes from the construction segment. The construction sector's growth coming in from Tier 2 and Tier 3 cities rather than restricted to metros. Moreover, with the new government's endeavor for developing a robust and stable infrastructure and customer's increasingly demanding high-quality and branded wires, potential demand outlook for cables looks positive.**

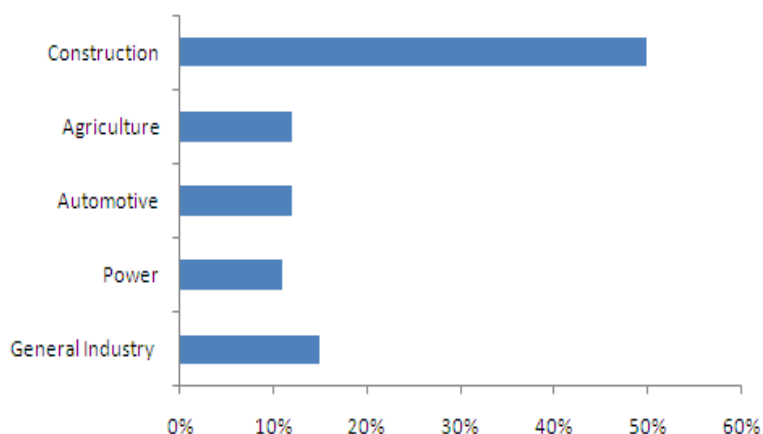
FCL is likely to benefit from the expected increase in government expenditure on transmission and distribution (T&D) infrastructure and other industrial segments. 15-20% of the total T&D spending will go to cable industry, hence we believe this will create huge opportunity for cable companies in the near to longer term. Major investments expected to be in transmission line and that will be driven by the SEBs' capex to upgrade intra-state grid to 400/765kv coupled with Power Grid's investments to increase inter regional transmission lines by upgrading to 765kv transmission lines, substations and HVDC lines will give fillip to FCL's revenue visibility.

Electric Cables Product portfolio –

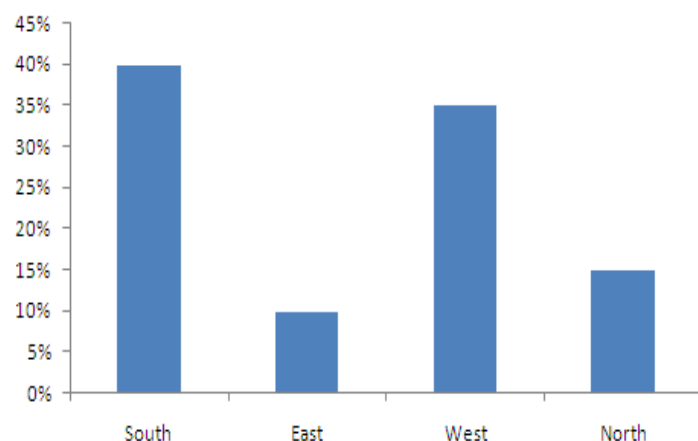
Products Covered (Electric Cable Business)	Application
1100 V PVC insulated cables.	Electrification of industrial establishments, electrical panel wiring and consumer electrical goods.
Motor winding PVC insulated cables and 3 core flat cables.	Submersible pumps and electrical motors.
Automotive/battery cables.	Wiring harness for automobile industry and battery cables for various applications.
UPS cables.	For providing power from the UPS to the computer/ appliances in the networking environment.
Heavy duty, underground, low voltage, power and control cables.	Connection to the user point from main supply of power.
Heavy duty, underground, high voltage, power cables.	Intra-city power distribution network.

Source: Company, Microsec Research

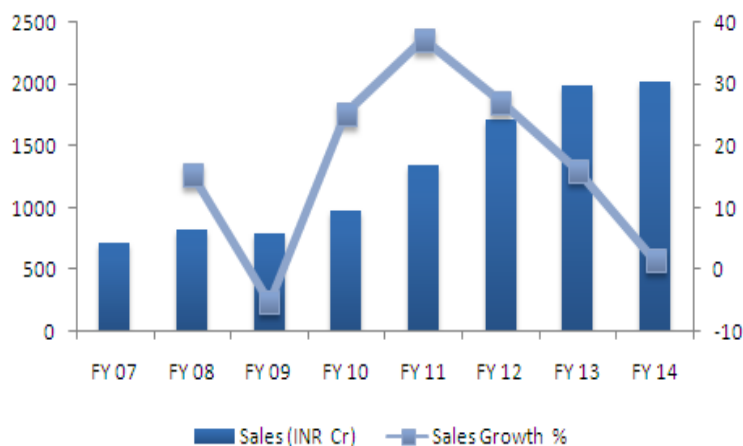
Revenue Split (Customer Wise)



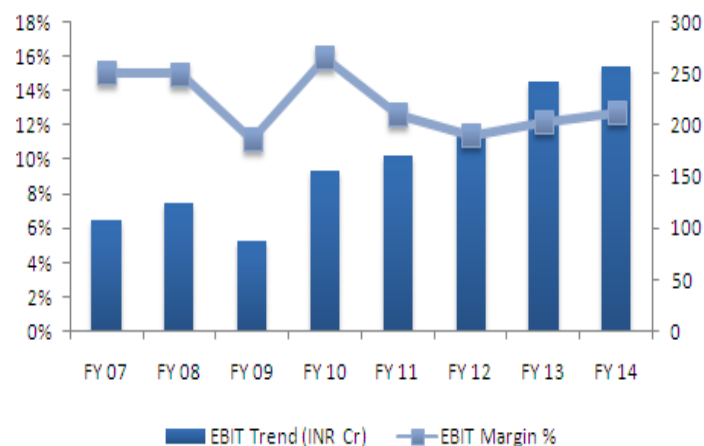
Revenue Split (Region Wise)



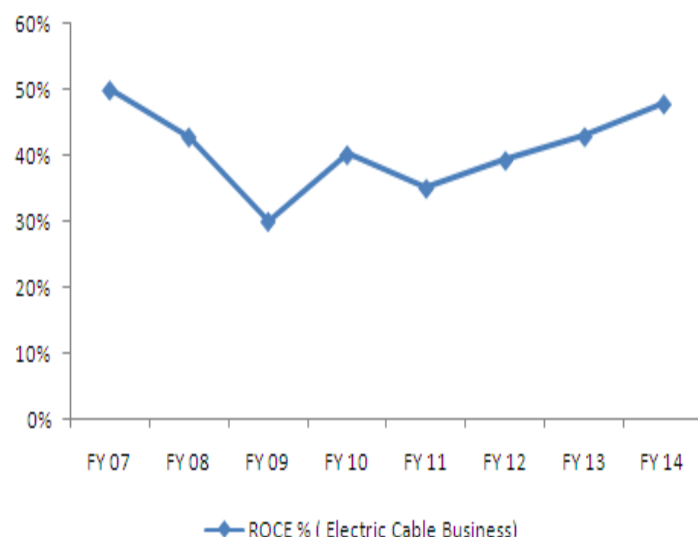
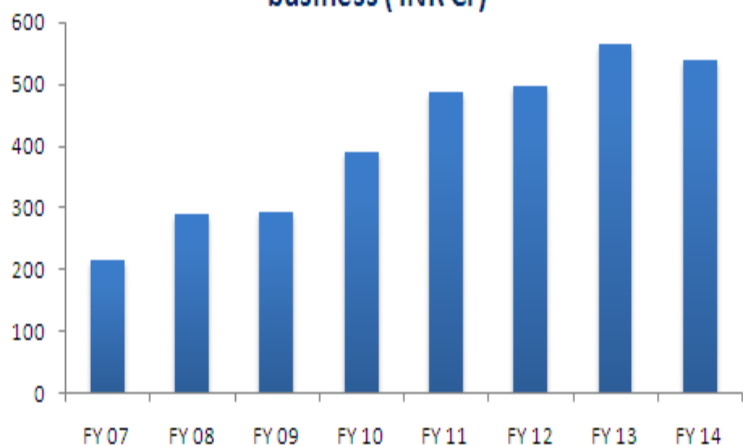
Electric Cable Business- Sales & Sales Growth %



EBIT Trend & EBIT Margin %



Trend in capital employed for Electric Cable business (INR Cr)

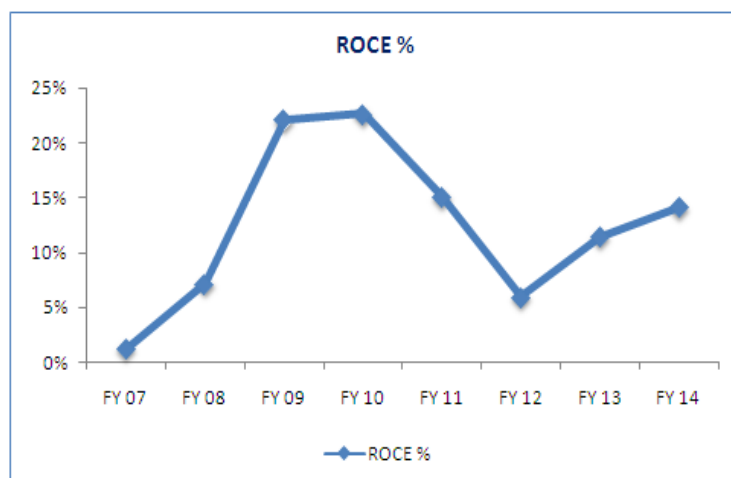
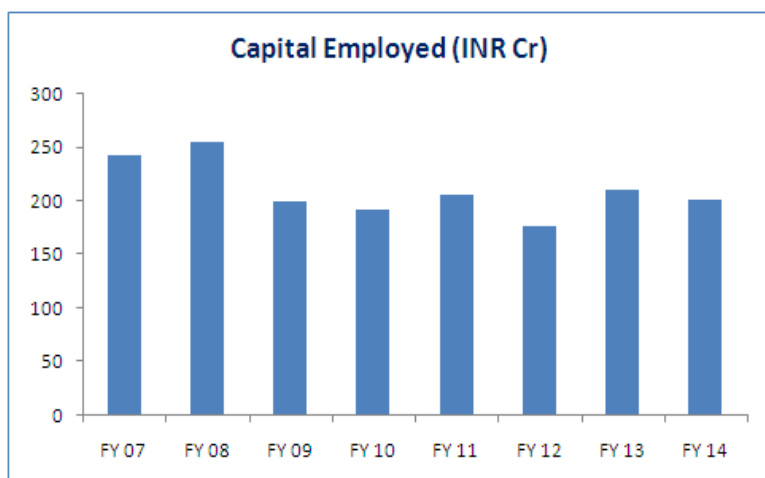
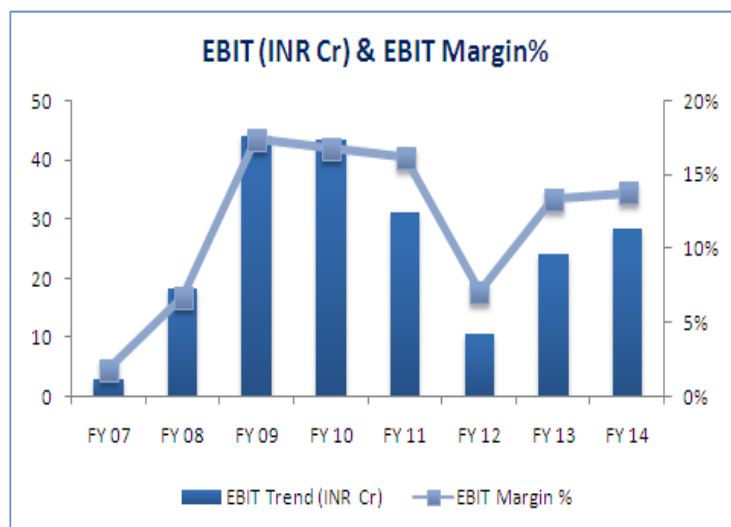
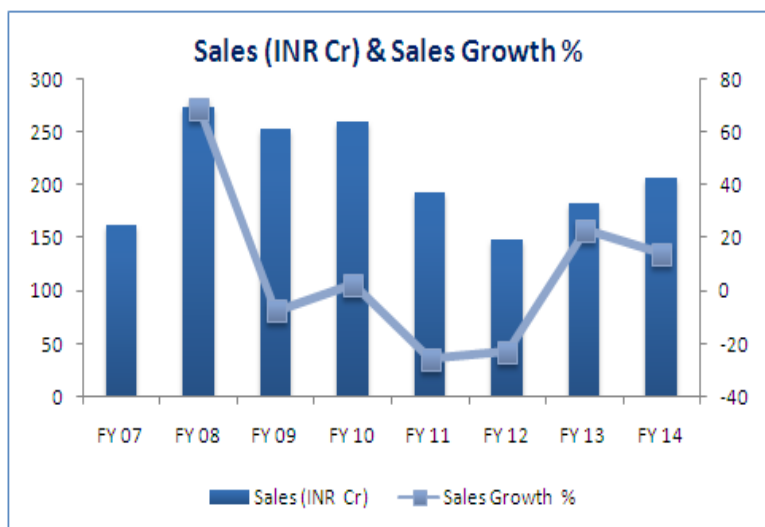


Communication Cables portfolio –

FCL manufactures communications cables, which comprise 7% of its turnover. This is largely a tender based business. FCL was awarded a purchase order of over INR 2 Bn for Metal Free Optical Fibre Cable (OFC) under the National Optic Fiber Network (NOFN) project. The communication cables segment recorded sales of INR 207 Cr for the year under review against INR 181 Cr for the earlier year. Partial rollout of 4G services in some part of India brought in business opportunities. Also, the changeover to digital transmission in several cities across the country resulted in additional demand for Coaxial cables. With attractive price offerings and the past experience of better customer service, this segment has showed an improved performance in the year under review. Capacity utilisation at all plants has shown improvement leading to better margins and profitability.

Communication Product portfolio –

Products Covered (Communication Cable Business)	Application
Jelly filled telephone cables (JFTCs)	Telephone line connections to exchanges and users..
Local area network (LAN) cables	Indoor and outdoor networking, voice and data transmission, broadband usage.
PE insulated telephone cables	Telephone instrument connections to EPABX.
Coaxial cables	Cable TV network solutions, microwave communications, mobile towers.
Optic fibre	Principal raw material for optic fibre cables.
Speaker Cables	Meant for broadcasting applications in buildings.

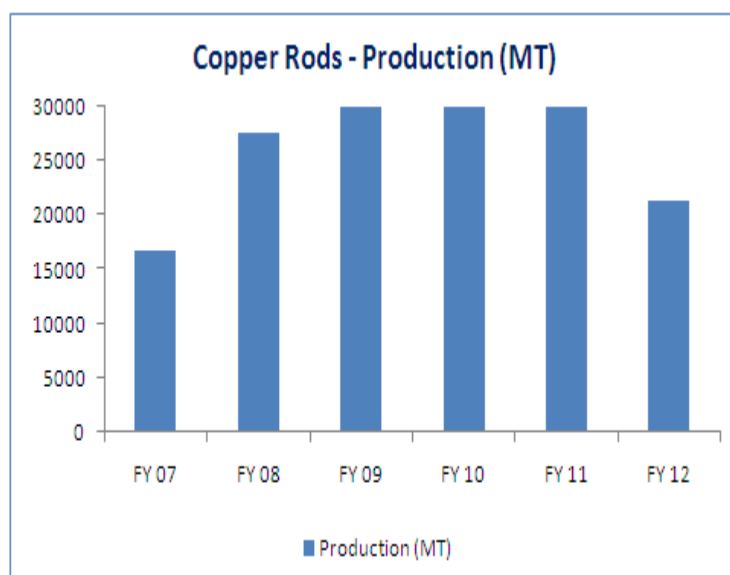
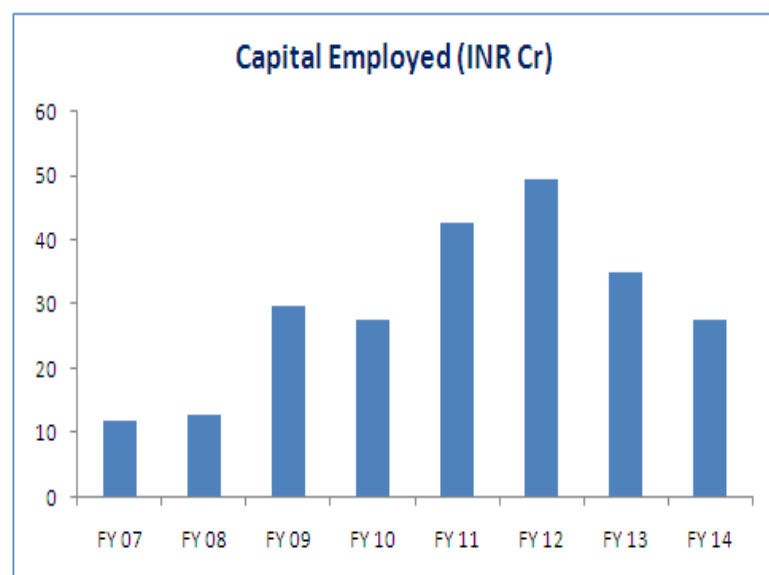
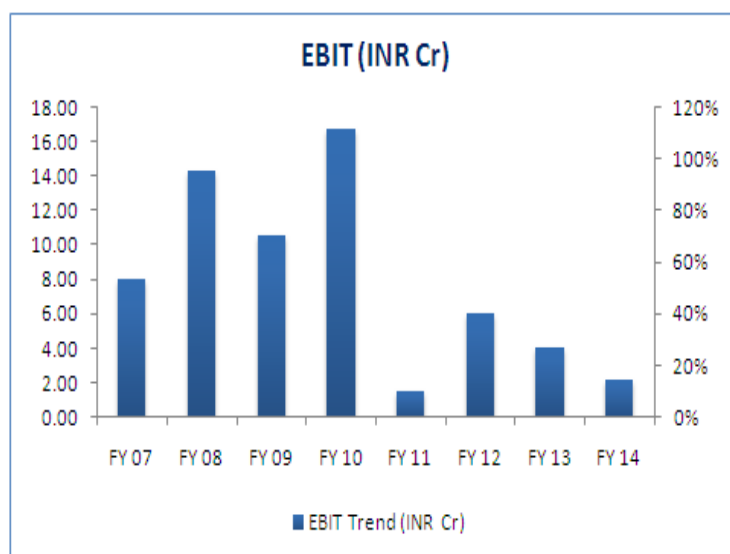
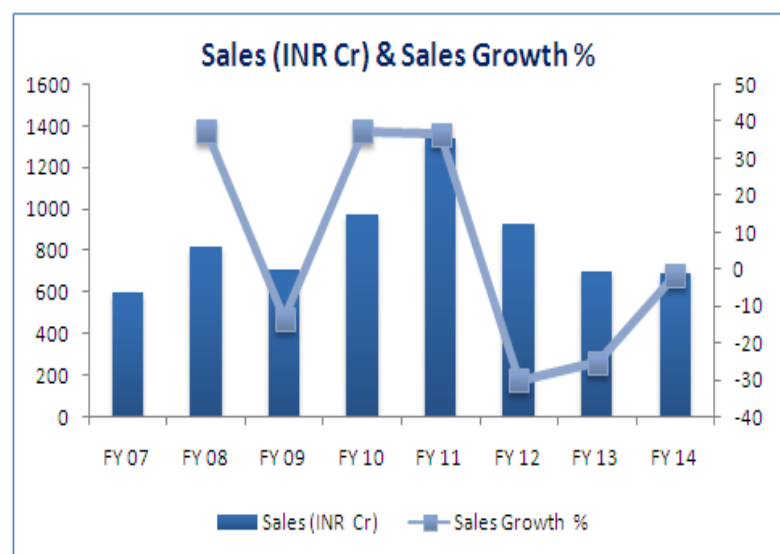


Source: Company, Microsec Research

Cooper rods portfolio –

Copper rod is the feed stock for copper based electrical and communications cables. The Company manufactures its own copper rods. The base material for producing copper rods is copper cathodes, the bulk of which are procured from local manufacturers under long term supply agreements. A smaller portion of the requirement of copper cathodes is imported as and when needed. After meeting the in-house requirement of copper rods, the balance capacity to produce copper rods is allocated for third party sale.

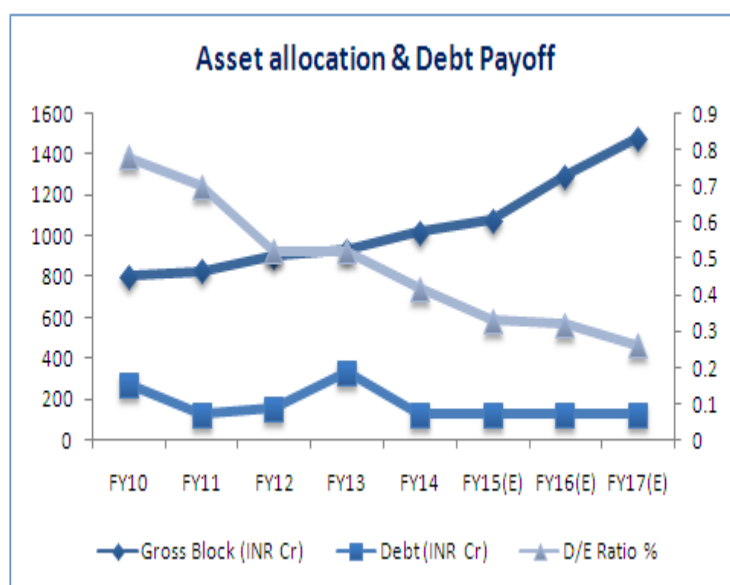
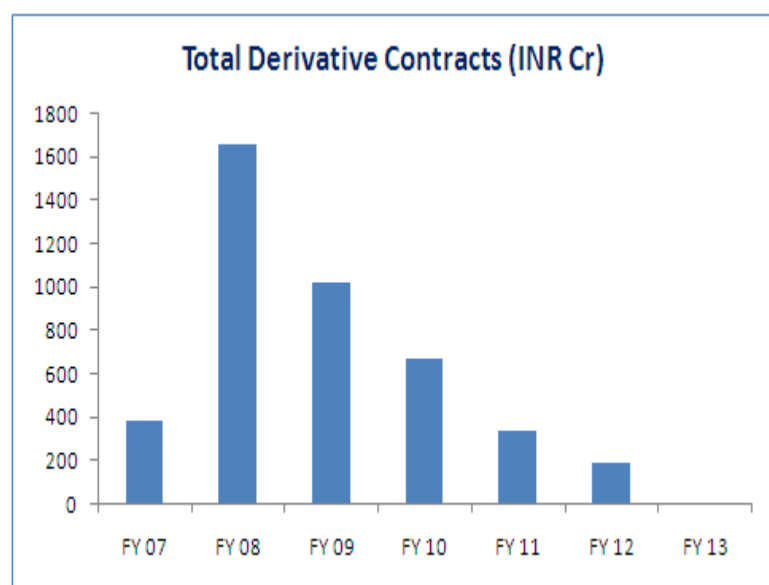
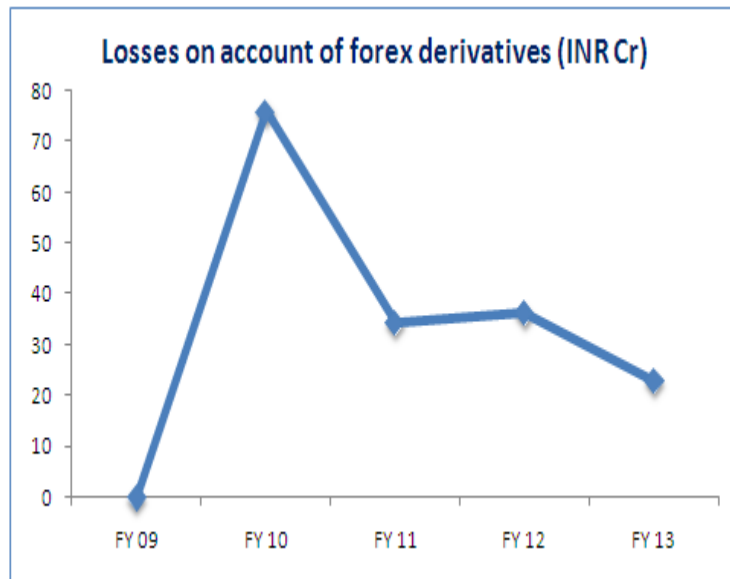
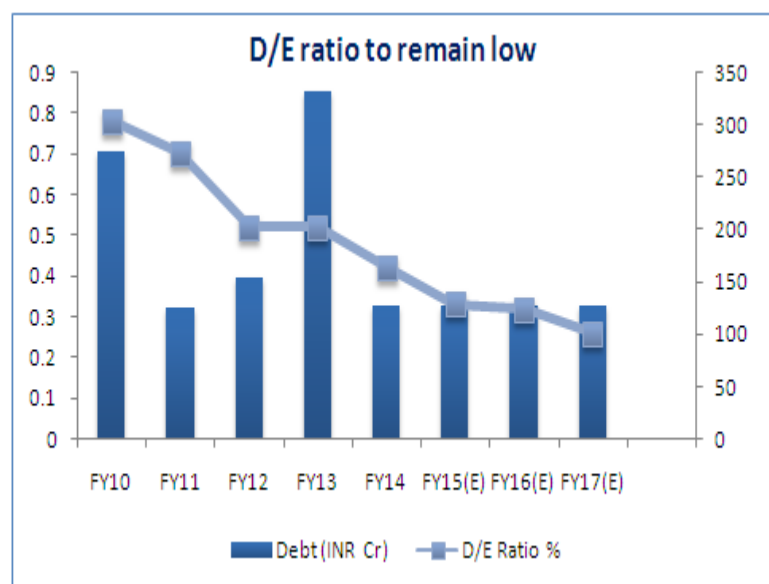
Copper rods segment contributes 22% of the total revenue. FCL manufactures copper rods, the raw material for its EWC products, thereby facilitating backward integration. A rated capacity of 60,000 tons and current utilisation of 60% allows it to control the quality and cost of its most crucial input. Any excess production of copper rods after captive consumption is sold off to third parties at market price. The copper rod production is mainly for in-house consumption. The Company's steps to set up new plants for cables as well as to expand the cable capacity at the existing plants will boost up the captive consumption of copper rods. Further, since the joint venture with J-Power Systems Corp. of Japan has commenced its operations, the venture's copper requirements would be met by your Company's copper rod plant. Accordingly the utilization of capacity at copper rod plant is expected to improve in coming years. **Copper rod business is a low margin business but it is a crucial input in the electric cable & communication cable businesses as it facilitates backward integration in these divisions apart from ensuring stable throughput and quality control.**



Source: Company, Microsec Research

Derivative Losses- "Things of the past"-

FCL's worries were largely on account of its forex losses amounting INR 3.1Bn over FY06-13. This constituted a serious overhang on valuations as the extent of losses suffered on account of these derivatives was uncertain. FCL has wound down such exposure, risk of further forex fluctuation losses have subsided. The absence of this augurs well for FCL's valuation which had taken a hit owing to such losses. Derivative losses are completely off the books as all such contracts have extinguished coupled with a reduced D/E at 0.7x from 0.2x make a strong case for higher valuations. **FCL has no outstanding derivative contracts and it recognized the entire losses over FY08-13 period, therefore we do not see any further losses from the derivative contracts. We expect debt to reduce from INR 332 Cr in FY 13 to INR 127 Cr which will bring down the D/E ratio to 0.26 in FY 17E.**

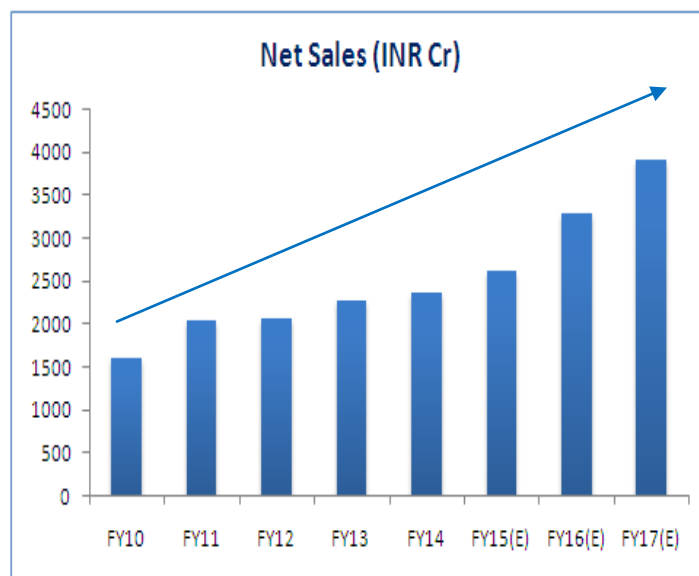
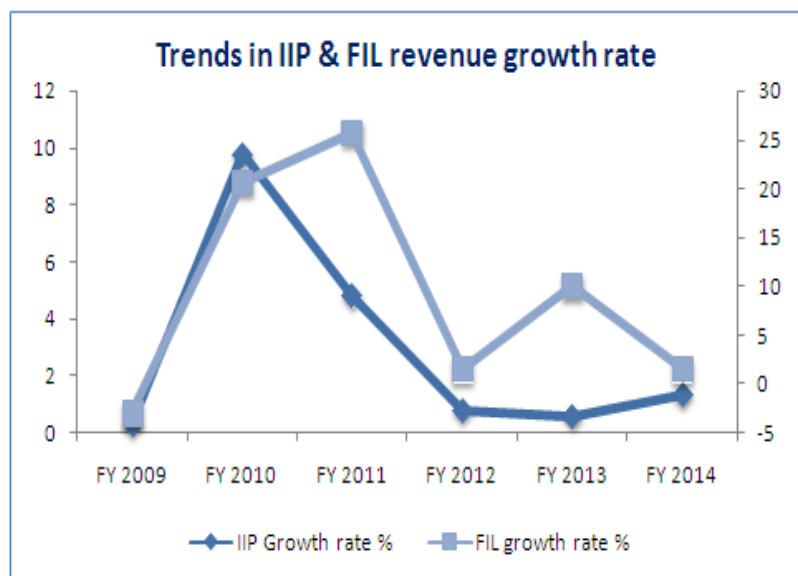


Source: Company, Microsec Research

Financial Performance

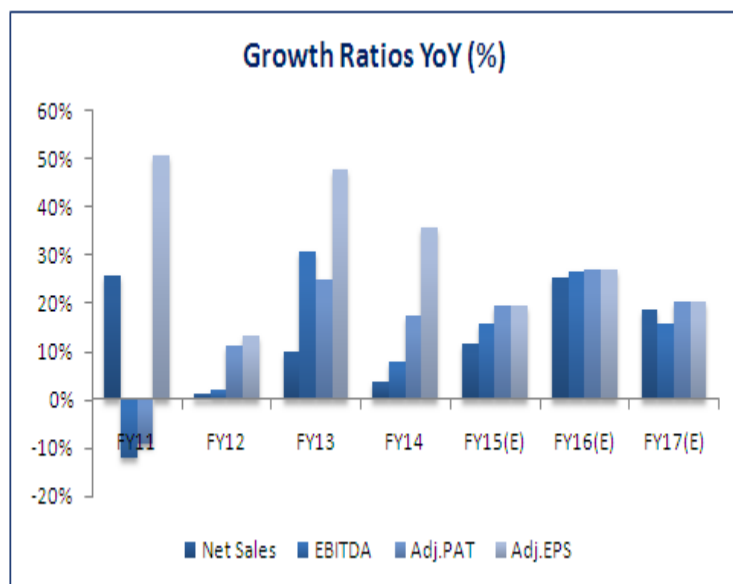
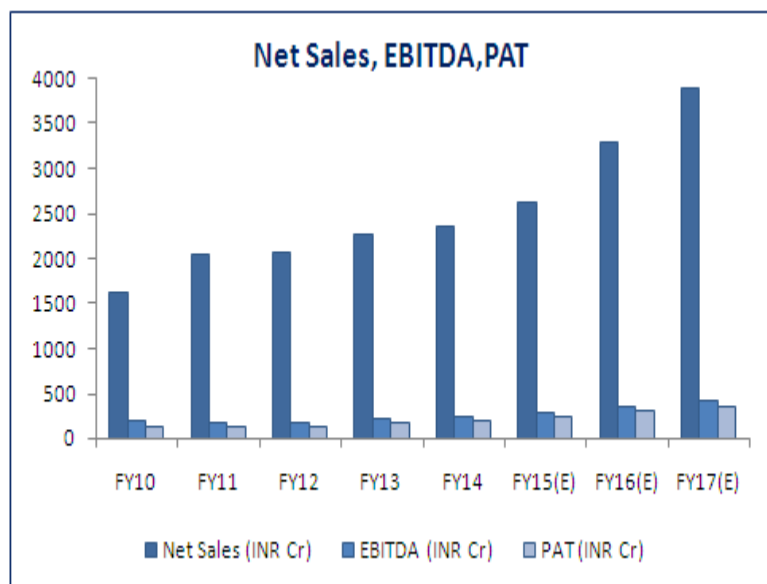
Electric Cable Business- Demand expected to pick up in FY 15-16E-We believe demand will revive for electric cable business once industrial capex improves, power project execution picks up and demand for housing revives. FCL expected to post a sales CAGR of 20.3% for its electric cable vertical. FCL has a manufacturing base in Pune and Goa, hence it has a strong presence in the western and southern market. FCL has a formidable brand recognition in this market coupled with superior product quality considered as industry's benchmark. **FCL is one of the top-three domestic manufacturers of wires and cables and capacity of 2.5m ckm, peers like Polycab and Havells have comparable manufacturing scale.**

FCL manufactures copper rods, the raw material for its EWC products, thereby facilitating backward integration. A rated capacity of 60,000 tons and current utilisation of 60% allows it to control the quality and cost of its most crucial input. Any excess production of copper rods after captive consumption is sold off to third parties at market price. FCL is gradually reducing its exposure to the segment due to thin margins from third party transactions. We expect this trend to continue and thereby improving the margin of the company. **We expect revenue to post a 15% CAGR over FY13-FY17E, on the back of underlying demand, dealer expansion in the non-western region and entry into switchgear business.**



Source: Company, Microsec Research

- ✓ FCL's revenues have demonstrated a strong correlation with domestic IIP over the past decade. We believe demand will revive for electric cable business once industrial capex improves, power project execution picks up and demand for housing revives. In FY14, as user industries were affected by the slowdown, sales grew by a minuscule 4% in FY14; we expect sales to grow by 12% in FY15E and by 25% in FY16E.
- ✓ Domestic issues like policy logjam and tighter liquidity are unlikely to be major factors in the coming years as user industry poised to grow at a healthy rate and we expect demand to pick up. FCL poised to expand its capacity at its Roorkee plant. This plant is expected to be operational by Q1FY15 to facilitate strong growth in the northern market.
- ✓ In the business verticals electrical cable contributes 63% of the total revenue and EBITDA margin is in the range of 12-13%. Electrical cables are the main focus area of business for the Company. In the longer term, we are upbeat of the demand outlook for this vertical— construction sector appears positive with development seeming more broad based and consumption being reported from interior areas of the Country rather than being limited to the larger cities; agricultural applications also appear positive and poised to continue on the growth shown in the previous years.

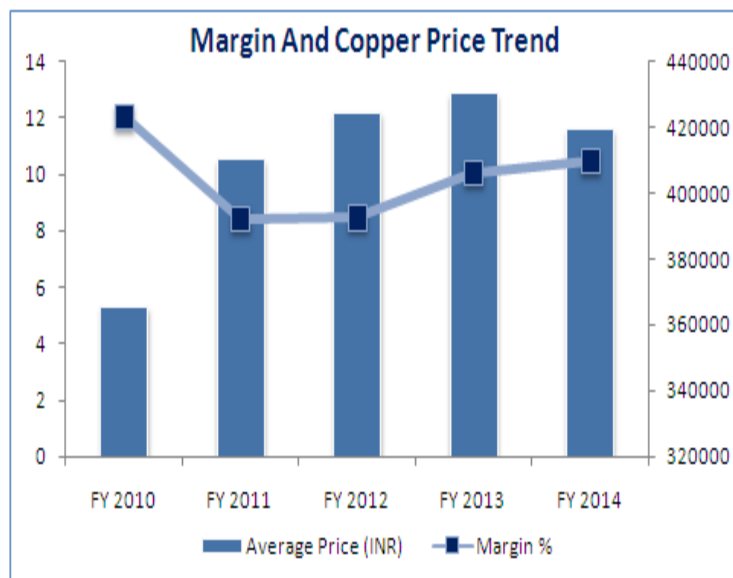
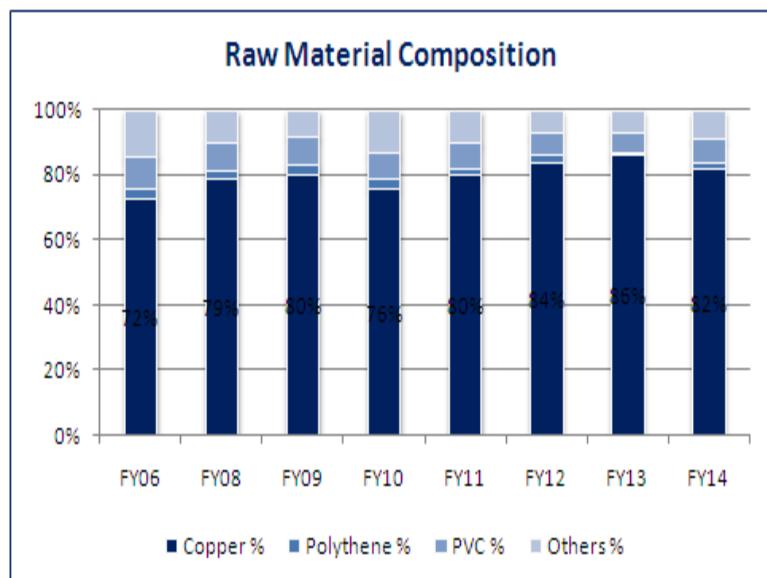


Source: Company, Microsec Research

Raw material costs to moderate in the medium term –

Raw material costs contributes 75-79% of the total sales thus leaves little room more margin expansions. FCL's main raw materials are copper, Polythene, PVC. FCL manufactures copper rods, the raw material for its EWC products, thereby facilitating backward integration. A rated capacity of 60,000 tons and current utilisation of 60% allows it to control the quality and cost of its most crucial input. Any excess production of copper rods after captive consumption is sold off to third parties at market price. FCL is gradually reducing its exposure to the segment due to thin margins from third party transactions. We expect this trend to continue and thereby improving the margin of the company.

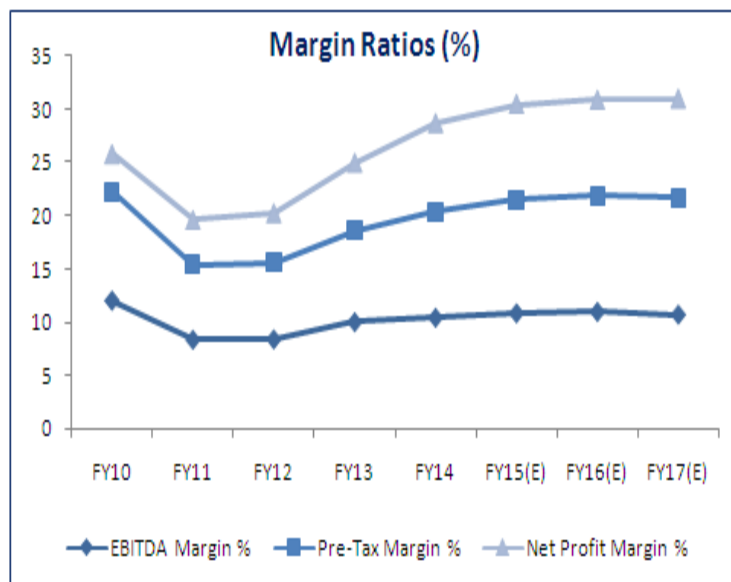
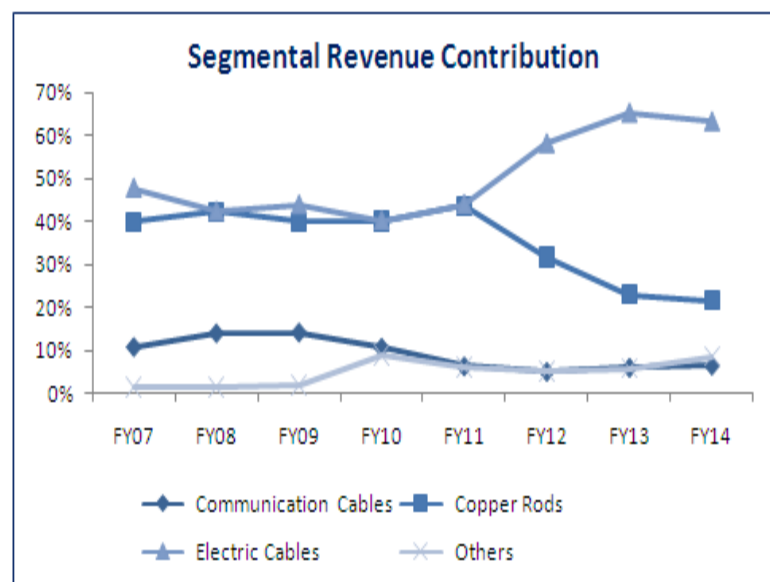
Copper are a key raw material for FCL's product portfolio and a key factor for its EBITDA margin. In FY10 FCL has benefited from softening of copper prices coupled with price hike across product portfolio helps in the expansion of the margin. But subsequently, the EBITDA margins dipped owing to higher copper prices. We believe, copper prices are likely to soften further hence FCL likely to maintain an EBITDA margin of 10-11%. The stabilization of INR against USD, better capacity utilisation and sales mix augurs well for its margin in the medium to long term.



Source: Company, Microsec Research

Revenue to grow at a CAGR of 15% and FCL expected to maintain an EBITDA margin of 10-11% over 2013-2017E-

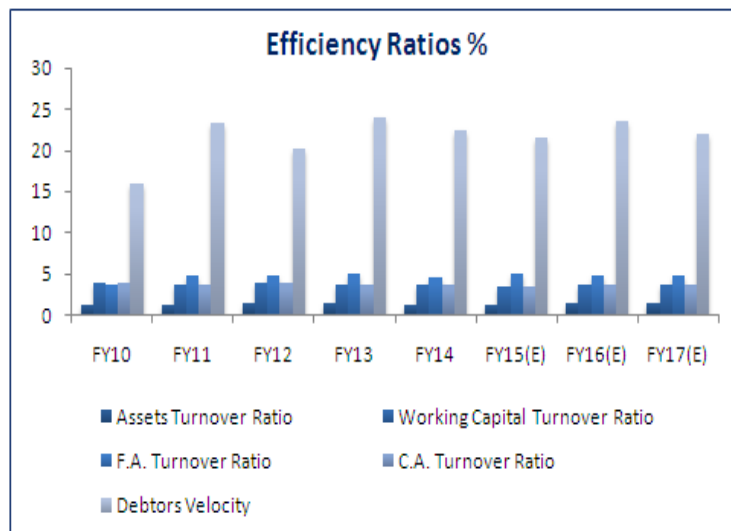
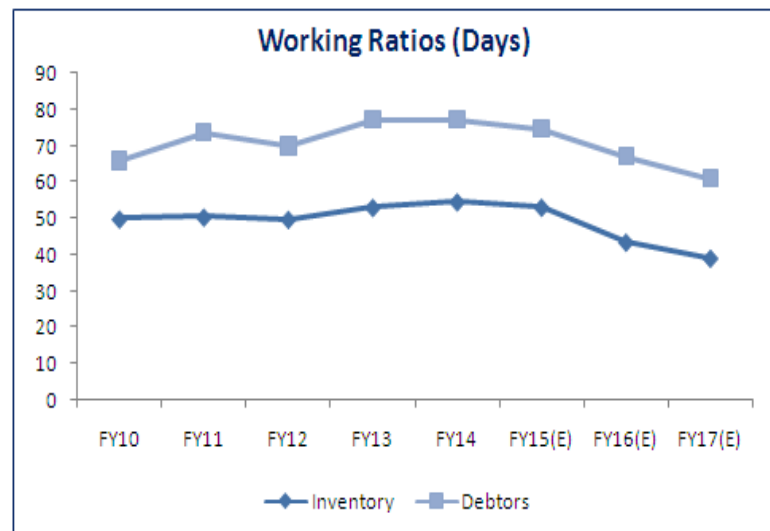
FCL expected to grow its revenue at a strong pace of 15% CAGR over 2013-17E respectively, on the back of healthy volume growth and a better product mix. We expect EBITDA margin to improve by 41 bps and 13 bps in FY15, FY16 respectively. With a 54% decline in debt over FY10-FY14, the D/E ratio would reduce to 0.26x in FY17E from 0.42x in FY14 and as result EBIT/Interest cost reduce from 11% in FY10 to 7% in FY14. We believe, following lower interest costs, net profit is expected to post a healthy 16% CAGR over FY14-FY17E.



Source: Company, Microsec Research

Strict cash on delivery, channel funding terms to improve working capital cycle –

FIL is improving working capital efficiency through: 1) Bill discounting, 2) Increase in the proportion of channel financing, and 3) Strict cash on delivery which helps in reduction of the net working capital cycle. Inventory days expected to improve to 44 from 54 in the same period. FCL has also reported asset turnover ratio of 1.26 in FY14 V/S 1.35 in FY13.

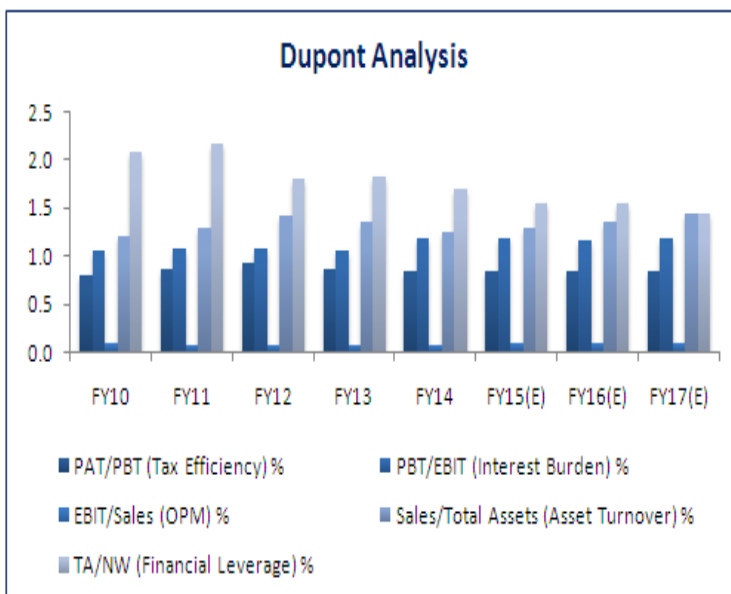
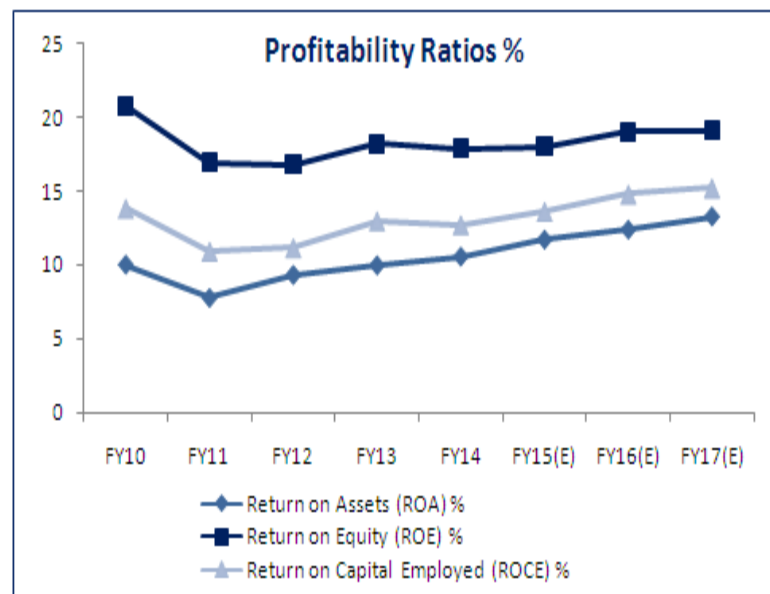
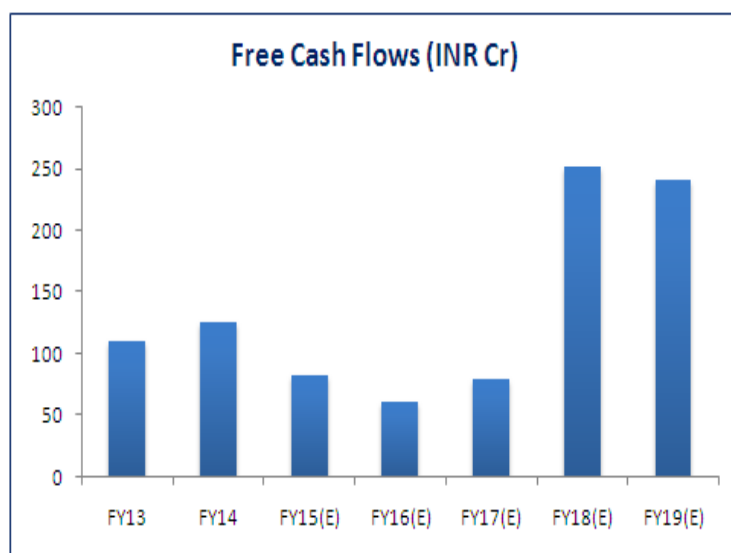
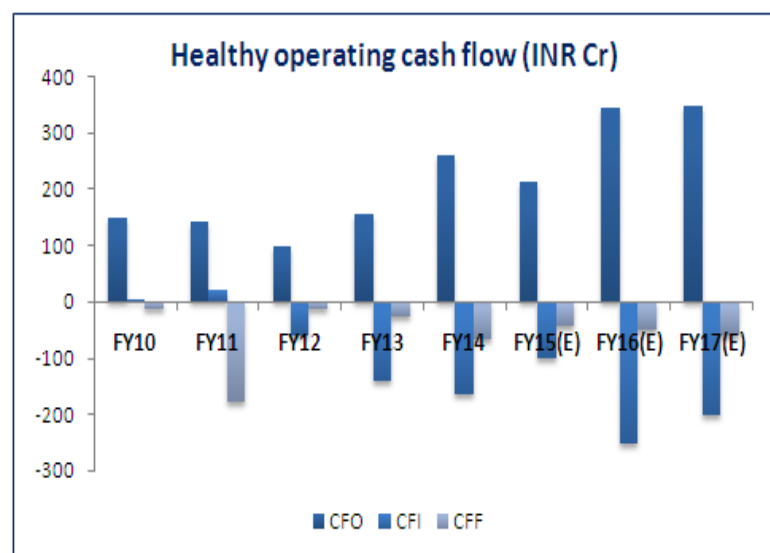


Source: Company, Microsec Research

Cash to grow at a CAGR of 41% over FY14-17E, Return ratio to improve from 2015E onwards –

FCL's worries were largely on account of its forex losses amounting INR 3.1Bn over FY06-13. This constituted a serious overhang on valuations as the extent of losses suffered on account of these derivatives was uncertain. FCL has wound down such exposure, risk of further forex fluctuation losses have subsided. The absence of this augurs well for FCL's valuation which had taken a hit owing to such losses. Derivative losses are completely off the books as all such contracts have extinguished coupled with a reduced D/E at 0.7x from 0.2x make a strong case for higher valuations.

FCL has no outstanding derivative contracts and it recognized the entire losses over FY08-13 period, therefore we do not see any further losses from the derivative contracts. FCL has undergone major capex expansion in the last two years and we do not see any major working capital needs in the medium term and therefore believe the cash and cash equivalents to grow at a CAGR of 41% over FY14-17E. Historically FCL has maintained ROE% of 18%, even in the worst of the time FCL has able to maintain a ROE% of 16%. Going forward, we believe FCL to maintain a ROE% of 18-19% on the back of improved utilization and better margins.



Source: Company, Microsec Research

Quarterly Results

Finolex Cables Ltd. Quarterly-Y-O-Y(%) -Standalone- [INR-Crore]					
DESCRIPTION	Q1 15	Q1 14	Q4 14	YOY	QOQ
Revenues	572.01	553.76	649.05	3.30%	-11.87%
Total Expenditure	516.00	502.41	573.99	2.70%	-10.10%
EBITDA	56.01	51.35	75.06	9.07%	-25.38%
EBIDTA Margins	9.79%	9.27%	11.56%	51.88 BPS	(177.28)BPS
Other Income	7.53	7.71	6.05		
Operating Profit	63.54	59.06	81.11		
Interest	3.26	3.46	3.08		
Exceptional Items					
PBDT	60.28	55.60	78.03		
Depreciation	13.89	11.42	12.24		
PBT	46.39	44.18	65.79		
Tax	11.71	10.26	-3.52	14.13%	-432.67%
Net Profit	34.68	33.92	69.31	2.24%	-49.96%
PAT Margins	6.06%	6.13%	10.68%	(6.26)BPS	(461.59)BPS
Equity Capital	30.59	30.59	30.59		
Face Value (In Rs)	2.00	2.00	2.00		
No of shares	15.30	15.30	15.30		
Diluted EPS	2.27	2.22	4.53	2.24%	-49.96%
Segmental Revenue Analysis					
Electric Cables	508.34	474.35	563.31	7.17%	-9.76%
Communication Cables	48.13	47.39	67.02	1.56%	-28.19%
Copper Rods	148.14	201.33	142.06	-26.42%	4.28%
Others	61.77	62.92	98.68	-1.83%	-37.40%
Segmental Analysis (EBIT%)					
Electric Cables	12%	11%	15%	65.40 BPS	(312.01)BPS
Communication Cables	5%	12%	17%	(708.49)BPS	(1,180.60)BPS
Copper Rods	1%	0%	0%	40.71 BPS	71.34 BPS
Others	-1%	-2%	-1%	78.69 BPS	15.40 BPS

- ✓ FCL has posted a mixed set of numbers for Q1 FY15; FCL's top-line reported a flat growth of 3% yoy to INR 572 Cr vs general expectation of INR 602 Cr. EBITDA for the quarter grew by 9% yoy while the EBITDA margin expanded by 52 bps yoy to 9.79%, mainly attributable to lower copper prices during the quarter. FCL has reported a net profit of INR 35 Cr v/s expectation of INR 42 Cr.
- ✓ We believe Q1 FY15 result is a one off event not going to be a trend setter in the coming quarter. We expect it to post healthy 18.3% revenue CAGR over FY14-FY17E. With strong backward integration coupled with product visibility in the west & southern region, operating margin is likely to improve 58 bps, driving a net profit CAGR of 22.3% over FY14-FY17E. Lower working capital and capex would improve the return ratios and free cash flow in the near to longer time.

Peer Comparison

Company (India)	CMP (INR)	M-Cap Rs cr	EBITDA %	PAT %	D/E	P/E (x)		P/BV (x)		EV/EBITDA (X)		ROE (%)	
						FY 15E	FY 16E	FY 15E	FY 16E			FY 15E	FY 16E
Havells India Ltd.	1220.3	15226.9	9.1	5.5	0.6	24.8	20.5	7.20	5.93	15.52	13.19	31.4%	30.8%
V-Guard Industries Ltd.	743.2	2218.5	8.1	4.6	0.3	24.5	19.8	5.57	4.70	14.80	12.35	24.4%	24.5%
Sterlite Technologies Ltd.	56.6	2228.9	10.7	-1.5	2.5	27.1	24.7	1.89	1.86	11.36	9.01	4.8%	7.1%
KEI Industries Ltd.	31.3	230.5	9.5	1.4	1.9	15.8	15.5	0.87	0.83	4.29	4.10	4.9%	5.1%
FINOLEX Cables Ltd	194.0	2967.2	10.5	8.8	0.4	12.6	10.0	2.27	1.90	11.40	9.14	18.0%	19.0%

Note: All figures are on Consolidated, Figures represent FY14 figures

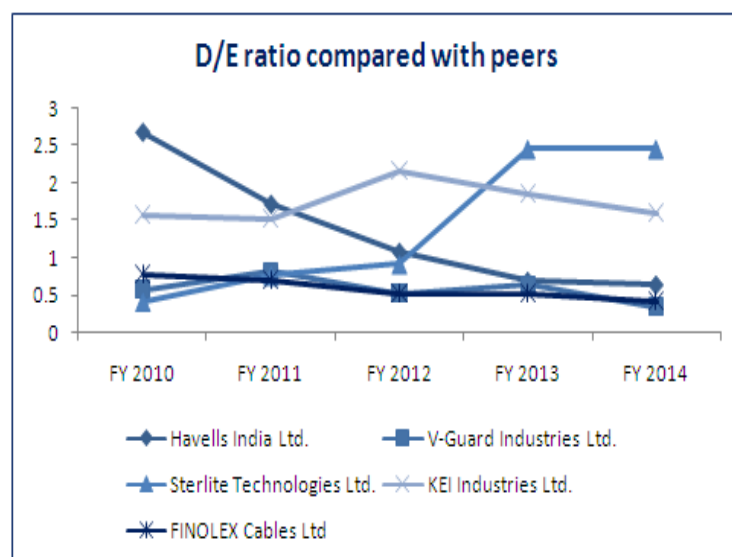
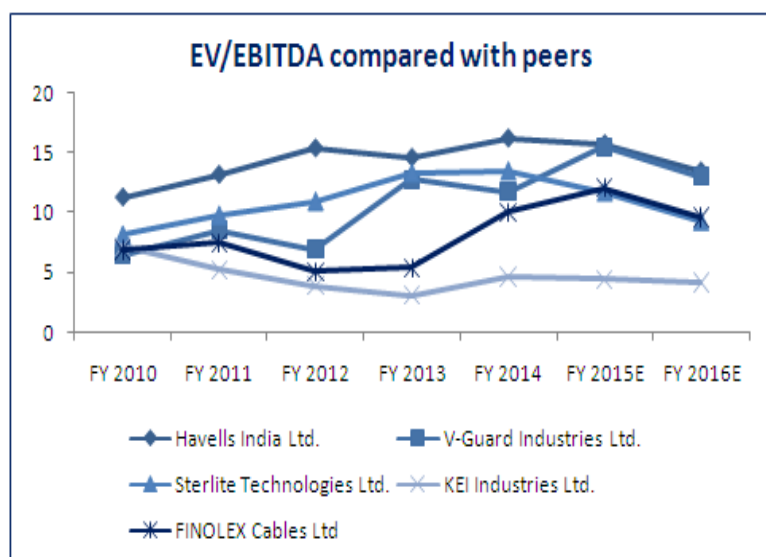
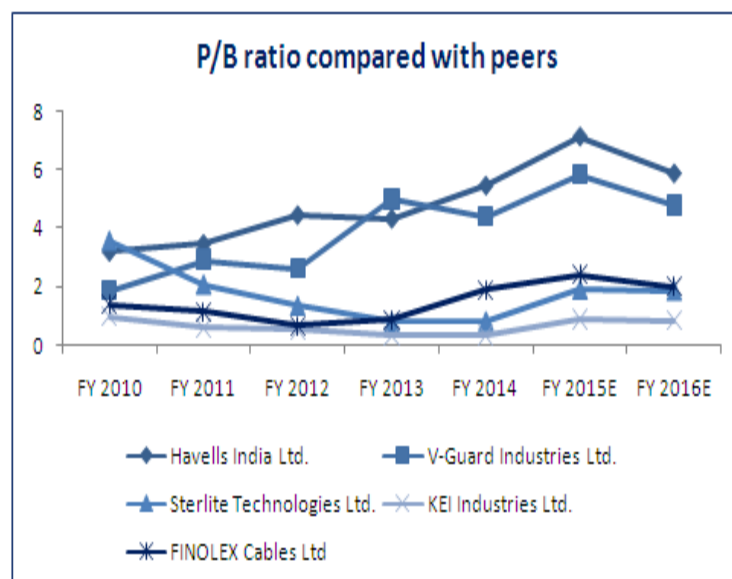
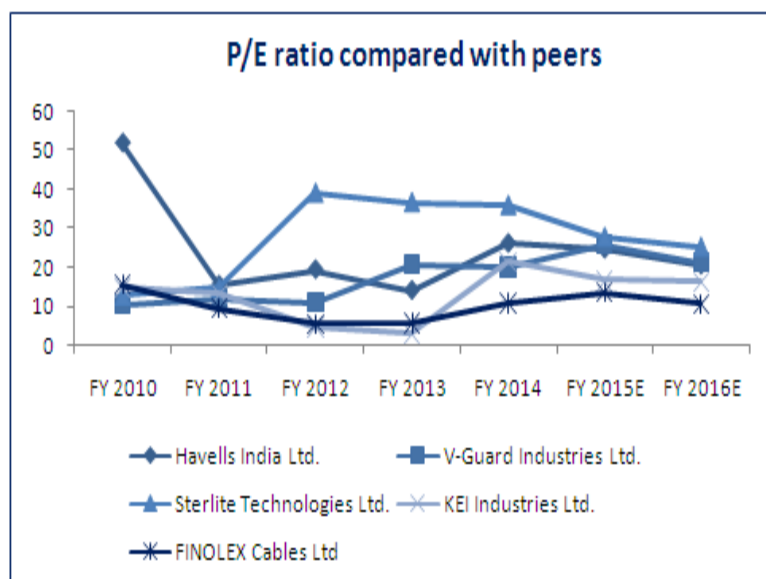
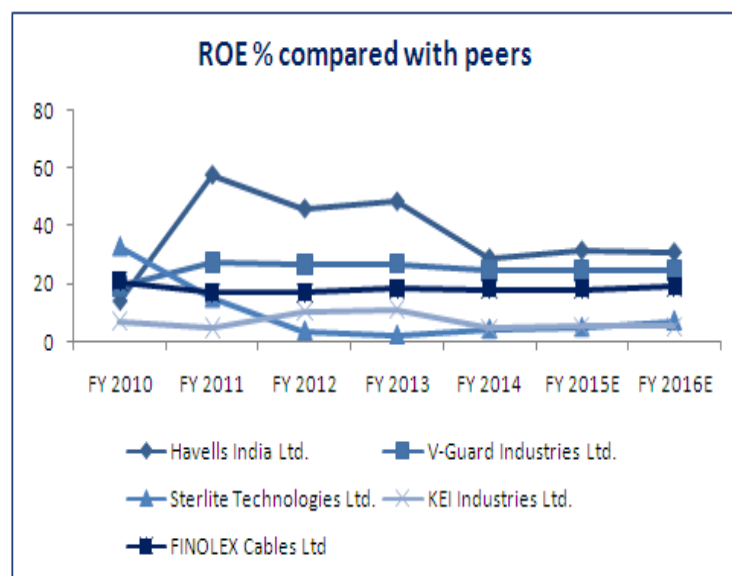
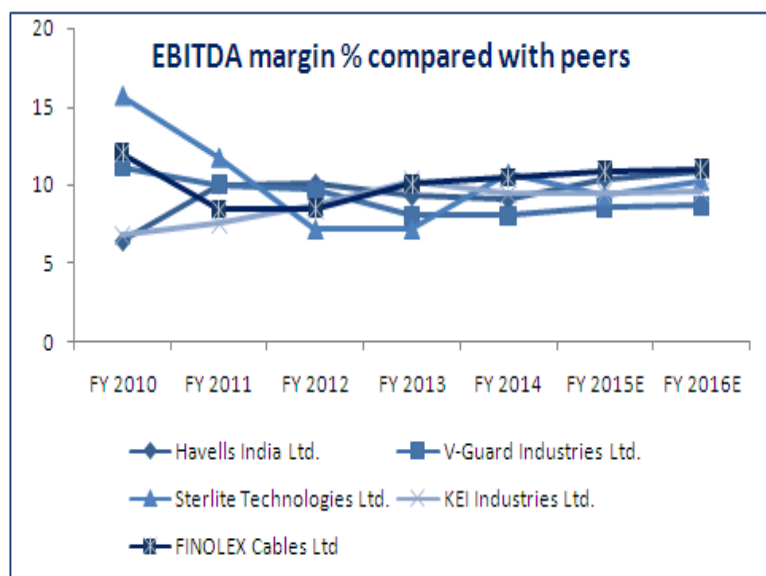
FCL to grow its revenue at a strong pace of 15% CAGRs over 2013-17E respectively, on the back of healthy volume growth and a better product mix. FCL has a strong brand recall in the western & southern part of India (FCL has significance presence in Maharashtra, Gujrat, Goa & FCL is number one in south) and the company is not inducing distributors by higher freebies as FCL solely focusing on to maintain a strong bottom line margin which is higher than the listed peers. Being the second largest electric cable manufacturer, FCL commands highest margin as its product demands premium pricing (Product pricing is 5-10% higher than its peer) for its superior quality.

FCL has maintain a steady EBITDA margin over the years and among its peers it maintains the highest margin and we believe it continue to operate within an EBITDA margin of 10-11%. We believe, copper prices are likely to soften further, the stabilization of INR against USD, better capacity utilisation and sales mix augurs well for its margin in the medium to long term.

FCL manufactures copper rods, the raw material for its EWC products, thereby facilitating backward integration. A rated capacity of 60,000 tons and current utilisation of 60% allows it to control the quality and cost of its most crucial input. Any excess production of copper rods after captive consumption is sold off to third parties at market price. FCL is gradually reducing its exposure to the segment due to thin margins from third party transactions. We expect this trend to continue and thereby improving the margin of the company.

FCL poised to report a ROE% on the range of 18-20% coupled with low leverage ratio, higher expected cash flow augurs well for the stock. FIL is improving working capital efficiency through: 1) Bill discounting, 2) Increase in the proportion of channel financing, and 3) Strict cash on delivery which helps in reduction of the net working capital cycle. Inventory days expected to improve to 44 from 54 in the same period. FCL has also reported asset turnover ratio of 1.26 in FY14 V/S 1.35 in FY 13. FCL has undergone major capex expansion in the last two years and we do not see any major working capital needs in the medium term and therefore believe the cash and cash equivalents to grow at a CAGR of 41% over FY14-17E.

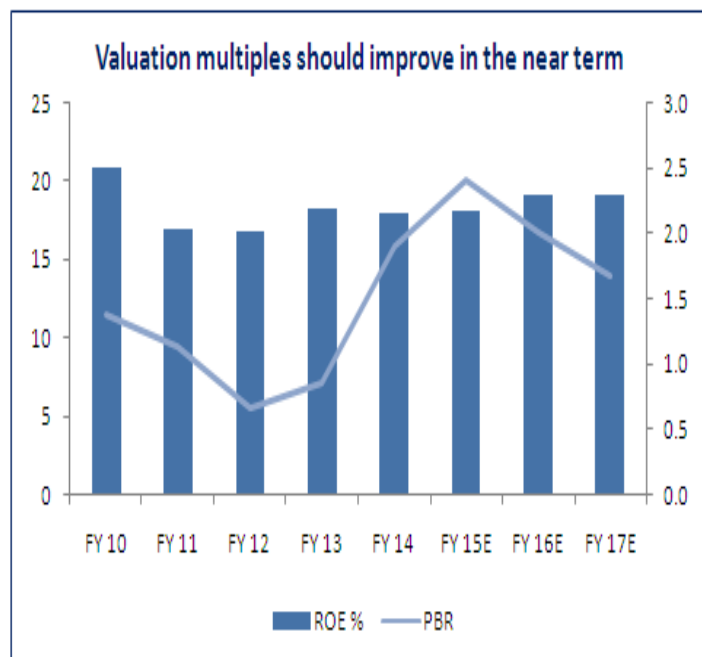
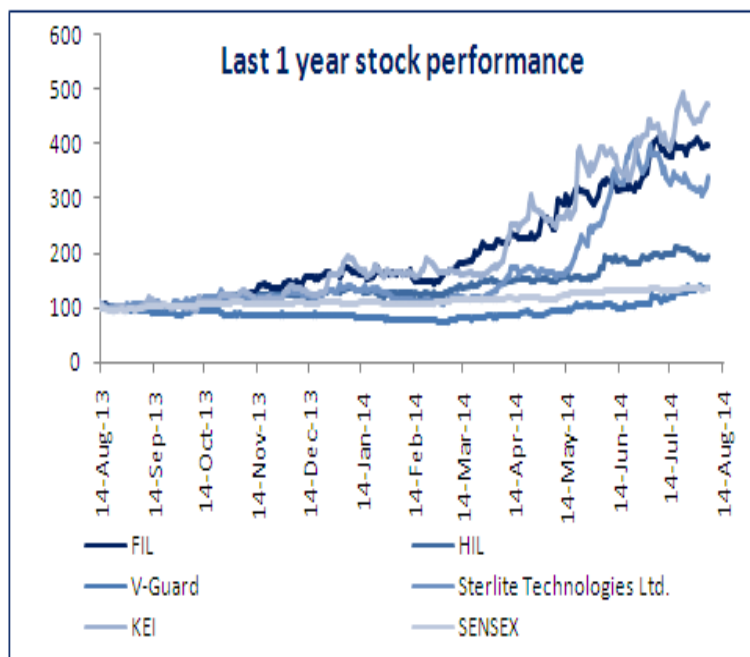
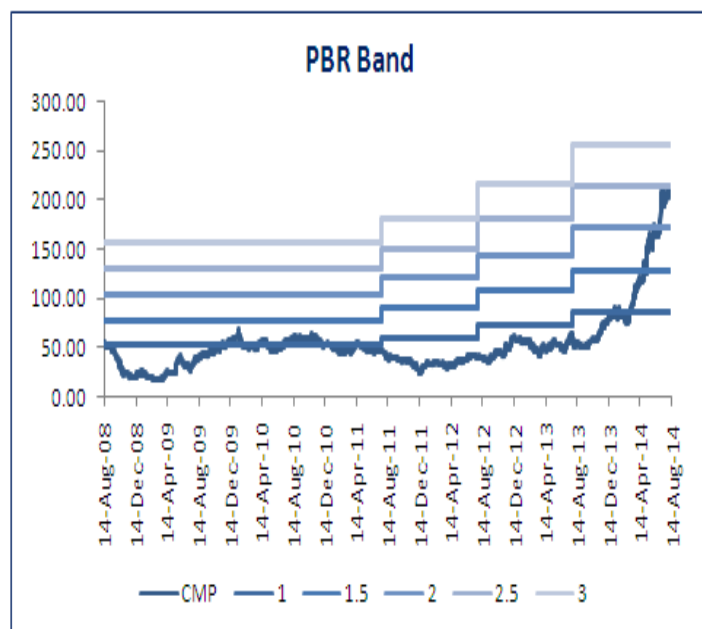
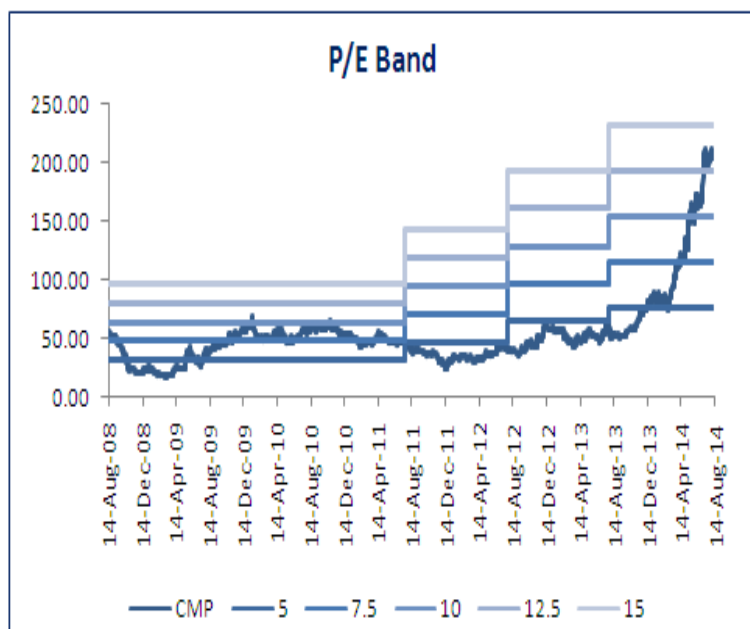
Average FY15E industry P/E multiple is 23x and FCL is trading at a P/E multiple of 13x which is a steep discount to its industry multiple. We believe the valuation gap to narrow in the medium term and we believe stock to trade between a P/E multiple of 18-20x.



Source: Company, Microsec Research

Why we are positive on the stock ?

We prefer FCL over the longer term due to (a) a scalable and de-risked business model, (b) a strong balance sheet, (c) cash flow CAGR of 41% over FY14-17E, (d) sizeable hidden value in its 32% stake in Finolex industries. For 19% overall ROE and 41% cash flow CAGR over FY14-17E, the stock trades at 2x FY16E P/B. We believe it should trade at a premium to its peers.



Source: Company, Microsec Research

Valuation & View

At the CMP of INR 194 per share, FCL is quoting at 2.27x and 1.9x its FY15E and FY16E price to book value (P/B), respectively.

We have used the sum of the parts (SOTP) method to value FCL. We have assigned a P/E multiple of 14.1x to its core cable business, for switchgear business we have taken an EV/EBITDA multiple of 11x, we value FCL's stake in Finloex industries at a 50% discount to market price. Our SOTP based price target is INR 333 which shows an upside potential of 72% from the current market price of INR 194. Hence we recommend a **"STRONG BUY"** for the stock from long term perspective.

Finloex Cable's SOTP Valuation			
Cable business	Switchgear business	Investment in Finloex	
EPS (FY 2016 E)	20 Revenue (FY16E)	270 Finloex Industry (Mcap)	3362
Average P/E	14 EBITDA %	15% Finloex Cables stake	32%
Per Share	276 EBITDA	41 Investment value	1076
	Multiple	11 Holding Company Discount (50%)	538
	EV	445.5 Valuation	538
	Less Capex	110 Per Share	35
	Equity Value	335.5	
	Per share	22	
SOTP Price		333	
Current Price		194	
Upside %		72	

Key Risks

Large unorganized sector and commodity price fluctuations-

The Company faces two principal risks in this business – firstly competition from a large unorganized sector which produces products of inferior quality but at cheap prices and secondly a highly volatile commodity market where price movements can be very sharp. The Company has been handling the risk of the competitive forces through its organized business approach by the strength of its reach, superior quality products, and safe products and maintaining high standards of service levels with its customers.

Economic slowdown-

Any slowdown in the economy, delay in reform measures may lower consumption demand of user industries.

Company snapshot

Finolex Cables, the flagship company of the Finolex Group was established in 1958 in Pune. The company has manufacturing facilities at Pimpri and Urse in Pune as well as at Goa & Uttarakhand. The company has, over the years, established its reputation as an innovative leader and quality manufacturer by continuously upgrading technology, modernizing manufacturing facilities and maintaining highest standards of quality and services. Every cable is manufactured using bright annealed electrolytic grade copper 99.97% pure manufactured in house and is insulated with virgin grade PVC (manufactured by group company Finolex Industries that is formulated in-house).

Key Milestones-

1946	• Finolex group set up in Pune under the stewardship of P.P Chhabria & KP Chhabria.
1970	• Started electrical wires for household applications.
1972	• Finolex started manufacturing PVC insulated Winding Wires & 3 Core Flat cables for submersible pumps.
1980	• Finolex started manufacturing 1.1 KV PVC insulated Power & Control Cables.
1984	• Finolex became the first Indian company in Private Organized Sector to supply JFT cables to DoT.
1993	• In 1993 Finolex Cables became the first cable company to receive ISO 9002 quality certification.
1996	• Finolex Cables is the first company in India to introduce FRLS industrial cables.
1998	• Finolex launched Electrical Switches & Compact Fluorescent Lamps (CFL's).
2006	• PVC Resin capacity was expanded from 1,30,000 MT to 2,60,000 MT.
2008	• FIL started a brand new state-of-the-art unit for manufacturing agriculture pipes and casing pipes at Urse, Pune with the capacity of 28000 MT p.a.
2009	• FCL shifted its Pimpri plant to Urse, Pune..
2011	• CL has commenced a JV with J-Power for the production, sale and installation of high voltage (HV) and extra high voltage (EHV) power transmission cables up to 500 kV.
2013	• FCL has expanded optical fibre cable facility at Goa.
2014	• 5 MW solar power plants will set up by FCL.

Income Statement

Figures in INR Cr

Particulars	FY10A	FY11A	FY12A	FY13A	FY14A	FY15(E)	FY16(E)	FY17(E)
Net Sales	1618.71	2035.76	2064.16	2270.68	2359.04	2628.63	3290.96	3904.61
% Growth	0%	25.76%	1.40%	10.01%	3.89%	11.43%	25.20%	18.65%
Total Revenue	1618.71	2035.76	2064.16	2270.68	2359.04	2628.63	3290.96	3904.61
% Growth	0%	25.76%	1.40%	10.01%	3.89%	11.43%	25.20%	18.65%
EXPENDITURES								
(Increase)/Decrease in Stocks	-61.05	-63.99	12.69	-29.65	-22.44	1.40	27.05	43.80
% of Net Sales	-4%	-3.14%	0.61%	-1.31%	-0.95%	0.05%	0.82%	1.12%
Purchase of finished goods	1.88	1.97	2.40	6.04	11.21	10.85	16.85	39.21
% of Net Sales	0%	0.10%	0.12%	0.27%	0.48%	0.41%	0.51%	1.00%
Cost of services & raw materials	1280.27	1670.92	1561.00	1712.92	1775.93	1962.70	2468.76	2935.48
% of Net Sales	79%	82.08%	75.62%	75.44%	75.28%	74.67%	75.02%	75.18%
Excise Duty	0	0	0	-3.04	-2.23			
% of Net Sales	0%	0%	0%	0%	0%	0%	0%	0%
Operating & Manufacturing Expense	143.20	151.63	97.8	74.82	83.2	93.26	97.06	108.55
% of Net Sales	9%	7%	5%	3%	4%	4%	3%	3%
Employee cost	59.22	64.73	69.48	84.59	84.83	118.22	129.02	141
% of Net Sales	4%	3%	3%	4%	4%	4%	4%	4%
Selling & Distributing Expense	0	29.54	113.21	155.57	144.36	125.68	135.68	151.68
% of Net Sales	0%	1%	5%	7%	6%	5%	4%	4%
Electricity, Power & fuel costs	0	9.23	32.57	40.69	37.07	30.19	53.88	64.39
% of Net Sales	0%	0%	2%	2%	2%	1%	2%	2%
Total Expenditures	1423.52	1864.03	1889.15	2041.94	2111.93	2342.30	2928.30	3484.11
% of Net Sales	88%	91.56%	91.52%	89.93%	89.52%	89.11%	88.98%	89.23%
EBITDA	195.19	171.73	175.01	228.74	247.11	286.33	362.66	420.50
EBITDA Margin %	12%	8.44%	8.48%	10.07%	10.48%	10.89%	11.02%	10.77%
Growth %		-12.02%	1.91%	30.70%	8.03%	15.87%	26.66%	15.95%
Depreciation & Amortisation	37.23	38.78	39.47	46.63	48.43	49.34	56.01	58.26
EBIT	157.96	132.95	135.54	182.11	198.68	236.99	306.65	362.24
Financial Charges	16.90	17.41	25.10	12.46	13.40	14.06	15.62	17.40
Other Income	24.12	26.09	35.19	24.17	48.35	57.70	64.80	85.00
PBT	165.18	141.63	145.63	193.82	233.63	280.63	355.83	429.84
Pre-tax Margin %	10.20%	6.96%	7.06%	8.54%	9.90%	10.68%	10.81%	11.01%
Tax	31.54	20.41	11.08	25.54	36.33	44.79	56.17	68.81
Effective Tax Rate %	19%	14.41%	7.61%	13.18%	15.55%	15.96%	15.78%	16.01%
Reported PAT	133.64	121.22	134.55	168.28	197.30	235.84	299.66	361.03
Net Profit Margin %	4%	4%	4.76%	6.40%	8.80%	8.97%	9.11%	9.25%
Growth in Adjusted PAT %	0%	-9.29%	11.00%	25.07%	17.25%	19.53%	27.06%	20.48%
Extraordinary Income	76.02	34.44	36.36	23.01	10.38	0.00	0.00	0.00
Net Profit (Adjusted PAT)	57.62	86.78	98.19	145.27	207.68	235.84	299.66	361.03
Shares In Issue	15.30	15.30	15.30	15.30	15.30	15.30	15.30	15.30
Adjusted EPS	3.77	5.67	6.42	9.50	13.58	15.42	19.59	23.60
Growth %	0.00%	50.61%	13.15%	47.95%	42.96%	13.56%	27.06%	20.48%

Source: Company, Microsec Research

Balance Sheet

Figures in INR Cr

Particulars	FY10A	FY11A	FY12A	FY13A	FY14A	FY15(E)	FY16(E)	FY17(E)
Gross Asset	802.45	825.70	900.22	929.18	1014.07	1,077.31	1,295.65	1,479.02
Accumulated Depreciation	383.70	422.37	470.99	517.07	542.53	591.87	647.88	706.14
Capital WIP	28.83	18.76	12.02	35.73	35.00	45.00	45.00	45.00
Net Fixed Asset	447.58	422.09	441.25	447.84	506.54	530.44	692.77	817.88
Investments & Deposits	280.27	245.15	237.21	324.09	403.14	430.89	464.61	482.99
Current Asset	414.88	552.38	537.59	632.21	654.29	778.73	916.91	1,082.38
Cash	37.16	21.29	49.00	39.81	64.86	133.09	174.66	258.91
Inventories	220.95	280.84	281.14	329.63	352.40	382.00	392.00	418.00
Trade Debtors	71.05	130.24	114.09	149.65	145.17	154.63	212.83	235.23
Loans and Advances	85.72	119.45	78.42	95.81	65.28	73.02	91.42	110.23
Other Current Assets		0.56	14.94	17.31	26.58	36.00	46.00	60.00
Current Liabilities & Provisions	192.60	344.87	228.47	283.09	304.39	274.64	344.22	336.14
Net Current Asset Excluding Cash	377.72	531.09	488.59	592.40	589.43	645.64	742.25	823.46
Capital Deployed	1,142.73	1,219.62	1,216.05	1,404.14	1,563.97	1,740.06	2,074.30	2,383.25
Non-Current Liabilities								
Secured Debt	246.57	94.60	113.91	143.09	126.69	126.69	126.69	126.69
Non-secured debt & Trade deposit	28.55	31.63	40.63	19.17	0.00	0.00	0.00	0.00
Deferred Tax Liabilities	31.91	31.04	32.61	34.47	29.52	29.52	29.52	29.52
Trade Payables	53.28	30.69	56.38	63.29	52.68	64.64	84.22	96.14
Other current liabilities	124.76	297.33	119.17	140.48	160.83	140.00	170.00	170.00
Short term Provisions	14.56	16.85	52.92	79.32	90.88	70.00	90.00	70.00
Total Liabilities	499.63	502.14	415.62	479.82	460.60	430.85	500.43	492.35
Contingent Liabilities								
Share Capital	30.59	30.59	30.59	30.59	30.59	30.59	30.59	30.59
Reserve and Surplus	612.52	686.89	769.84	893.73	1,072.78	1,278.62	1,543.28	1,860.31
Total Stock Holder's Equity	643.11	717.48	800.43	924.32	1,103.37	1,309.21	1,573.87	1,890.90
Capital Employed	1,142.74	1,219.62	1,216.05	1,404.14	1,563.97	1,740.06	2,074.30	2,383.25

Source: Company, Microsec Research

Cash Flow Statement

INR Cr

Particulars	FY10A	FY11A	FY12A	FY13A	FY14A	FY15E	FY16E	FY17E
PAT	57.62	86.78	98.19	145.27	207.68	235.84	299.66	361.03
Depreciation	37.22	38.67	48.62	46.08	25.46	49.34	56.01	58.26
Interest Expense	16.90	17.41	25.10	12.46	13.40	14.06	15.62	17.40
Other Non-Cash Charges	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Direct taxes paid	31.54	20.41	11.08	25.54	36.33	44.79	56.17	68.81
Operating Profit Before WC Changes	111.74	163.27	182.99	229.35	282.87	344.03	427.46	505.50
Changes in Current Assets (excluding cash)	(90.05)	(153.37)	42.50	(103.81)	2.97	(56.21)	(96.60)	(81.22)
Changes in Current Liabilities	21.21	152.27	(116.40)	54.62	21.30	(29.75)	69.58	(8.08)
Changes In WC	(68.85)	(1.10)	(73.90)	(49.19)	24.27	(85.96)	(27.02)	(89.30)
Cash Generated From Operations	180.59	162.17	109.09	180.16	307.14	258.07	400.43	416.20
Direct Taxes Paid	31.54	20.41	11.08	25.54	36.33	44.79	56.17	68.81
Others (provision for deferred tax)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Net Cash Generated From Operations	149.05	141.76	98.01	154.62	270.81	213.28	344.27	347.39
Cash Flow from Investing Activities								
Capital Expenditure (CAPEX)	(29.11)	(13.18)	(67.78)	(52.67)	(84.16)	(73.24)	(218.35)	(183.37)
Investments	33.83	35.12	7.94	(86.88)	(79.05)	(27.75)	(33.72)	(18.38)
Others		0.00	0.00	0.00	0.00	0.00	0.00	0.00
Net Cash Used In Investing Activities	4.72	21.95	(59.84)	(139.55)	(163.21)	(100.99)	(252.07)	(201.74)
Cash Flow from Financing Activities								
Change in Debt	(20.75)	(148.89)	28.31	7.72	(35.57)	0.00	0.00	0.00
Change in Equity	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Dividends Paid	(9.18)	(10.71)	(12.24)	(18.35)	(25.00)	(30.00)	(35.00)	(44.00)
Interest Paid	(16.90)	(17.41)	(25.10)	(12.46)	(13.40)	(14.06)	(15.62)	(17.40)
Others	(1.55)	(1.70)	(3.00)	(3.03)	(3.63)	0.00	0.00	0.00
Net Cash used in Financing Activities	-14.58	(178.71)	(12.03)	(26.12)	(77.60)	(44.06)	(50.62)	(61.40)
Net Increase in Cash and Cash Equivalents	9.04	(15.87)	27.71	(9.19)	25.05	68.23	41.58	84.25
Cash and cash equivalents At the beginning	28.12	37.16	21.29	49	39.81	64.86	133.09	174.66
Net Increase in Cash and Cash Equivalents	9.04	-15.87	27.71	-9.19	25.05	68.23	41.58	84.25
Cash and cash equivalents At the end	37.16	21.29	49.00	39.81	64.86	133.09	174.66	258.91

Source: Company, Microsec Research

Financial Ratios

	FY10A	FY11A	FY12A	FY13A	FY14A	FY15E	FY16E	FY17E
Profitability Ratios								
Return on Assets (ROA)	10.01%	7.75%	9.31%	9.97%	10.56%	11.71%	12.39%	13.28%
Return on Equity (ROE)	20.78%	16.90%	16.81%	18.21%	17.88%	18.01%	19.04%	19.09%
Return on Capital Employed (ROCE)	13.82%	10.90%	11.15%	12.97%	12.70%	13.62%	14.78%	15.20%
Dupont Analysis-ROE Decomposition								
PAT/PBT (Tax Efficiency)	0.81	0.86	0.92	0.87	0.84	0.84	0.84	0.84
PBT/EBIT (Interest Burden)	1.05	1.07	1.07	1.06	1.18	1.18	1.16	1.19
EBIT/Sales (OPM)	0.10	0.07	0.07	0.08	0.08	0.09	0.09	0.09
Sales/Total Assets (Asset Turnover)	1.21	1.30	1.43	1.35	1.26	1.30	1.36	1.44
TA/NW (Financial Leverage)	2.08	2.18	1.80	1.83	1.69	1.54	1.54	1.44
ROE	20.78	16.90	16.81	18.21	17.88	18.01	19.04	19.09
Liquidity Ratios								
Current Ratio	2.15	1.60	2.35	2.23	2.15	2.84	2.66	3.22
Acid Test Ratio	1.01	0.79	1.12	1.07	0.99	1.44	1.52	1.98
Debt-Equity Ratio	0.78	0.70	0.52	0.52	0.42	0.33	0.32	0.26
Efficiency Ratios								
Assets Turnover Ratio	1.21	1.30	1.43	1.35	1.26	1.30	1.36	1.44
Working Capital Turnover Ratio	3.90	3.69	3.84	3.59	3.61	3.38	3.59	3.61
F.A. Turnover Ratio	3.62	4.82	4.68	5.07	4.66	4.96	4.75	4.77
C.A. Turnover Ratio	3.90	3.69	3.84	3.59	3.61	3.38	3.59	3.61
Debtors Velocity	16.02	23.35	20.17	24.06	22.46	21.47	23.61	21.99
Margin Ratios (%)								
EBITDA Margin	12.06%	8.44%	8.48%	10.07%	10.48%	10.89%	11.02%	10.77%
Pre-Tax Margin	10.20%	6.96%	7.06%	8.54%	9.90%	10.68%	10.81%	11.01%
Net Profit Margin	3.56%	4.26%	4.76%	6.40%	8.80%	8.97%	9.11%	9.25%
Growth Ratios YoY (%)								
Net Sales	0.00%	25.76%	1.40%	10.01%	3.89%	11.43%	25.20%	18.65%
EBITDA	0.00%	-12.02%	1.91%	30.70%	8.03%	15.87%	26.66%	15.95%
Adj. PAT	0.00%	-9.29%	11.00%	25.07%	17.25%	19.53%	27.06%	20.48%
Adj. EPS	0.00%	50.61%	13.15%	47.95%	42.96%	13.56%	27.06%	20.48%
Working Ratios (Days)								
Inventory	49.82	50.35	49.71	52.99	54.52	53.04	43.48	39.07
Debtors	16.02	23.35	20.17	24.06	22.46	21.47	23.61	21.99
Net Working Capital Excluding Cash	377.72	531.09	488.59	592.40	589.43	645.64	742.25	823.46
Other Ratios (%)								
Other Income/PBT	14.60%	18.42%	24.16%	12.47%	20.70%	20.56%	18.21%	19.77%
Per Share (Rs.)								
Adj. EPS	3.77	5.67	6.42	9.50	13.58	15.42	19.59	23.60
CEPS	6.20	8.21	9.00	12.55	16.74	18.65	23.25	27.41
DPS	0.60	0.70	0.80	1.20	1.63	1.96	2.29	2.88
BVPS	42.05	46.91	52.33	60.43	72.14	85.60	102.90	123.63
Cash Per Share	2.43	1.39	3.20	2.60	4.24	8.70	11.42	16.93
Valuation Parameters								
P/E	15.38	9.27	5.37	5.45	10.05	12.58	9.97	8.22
P/CEPS	9.34	6.41	3.83	4.13	8.15	10.40	8.40	7.08
P/BV	1.38	1.12	0.66	0.86	1.89	2.27	1.90	1.57
EV/EBITDA	6.91	7.48	5.11	5.39	10.05	11.40	9.14	7.61
EV/SALES	0.83	0.63	0.43	0.54	1.05	1.24	1.01	0.82

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Source: Company, Microsec Research

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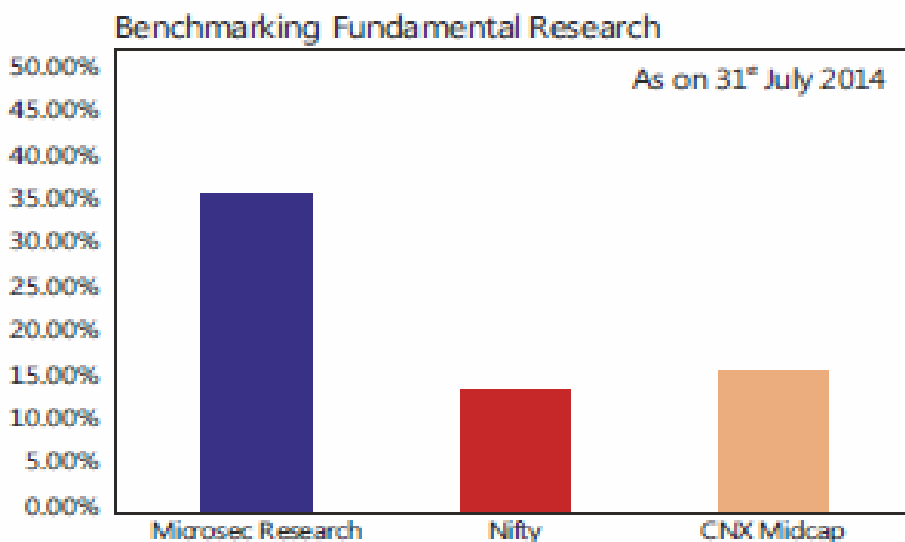
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Recommendation	Expected absolute returns (%) over 12 months
Strong Buy	>20%
Buy	between 10% and 20%
Hold	between 0% and 10%
Underperform	between 0% and -10%
Sell	< -10%

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Microsec Benchmark its Research



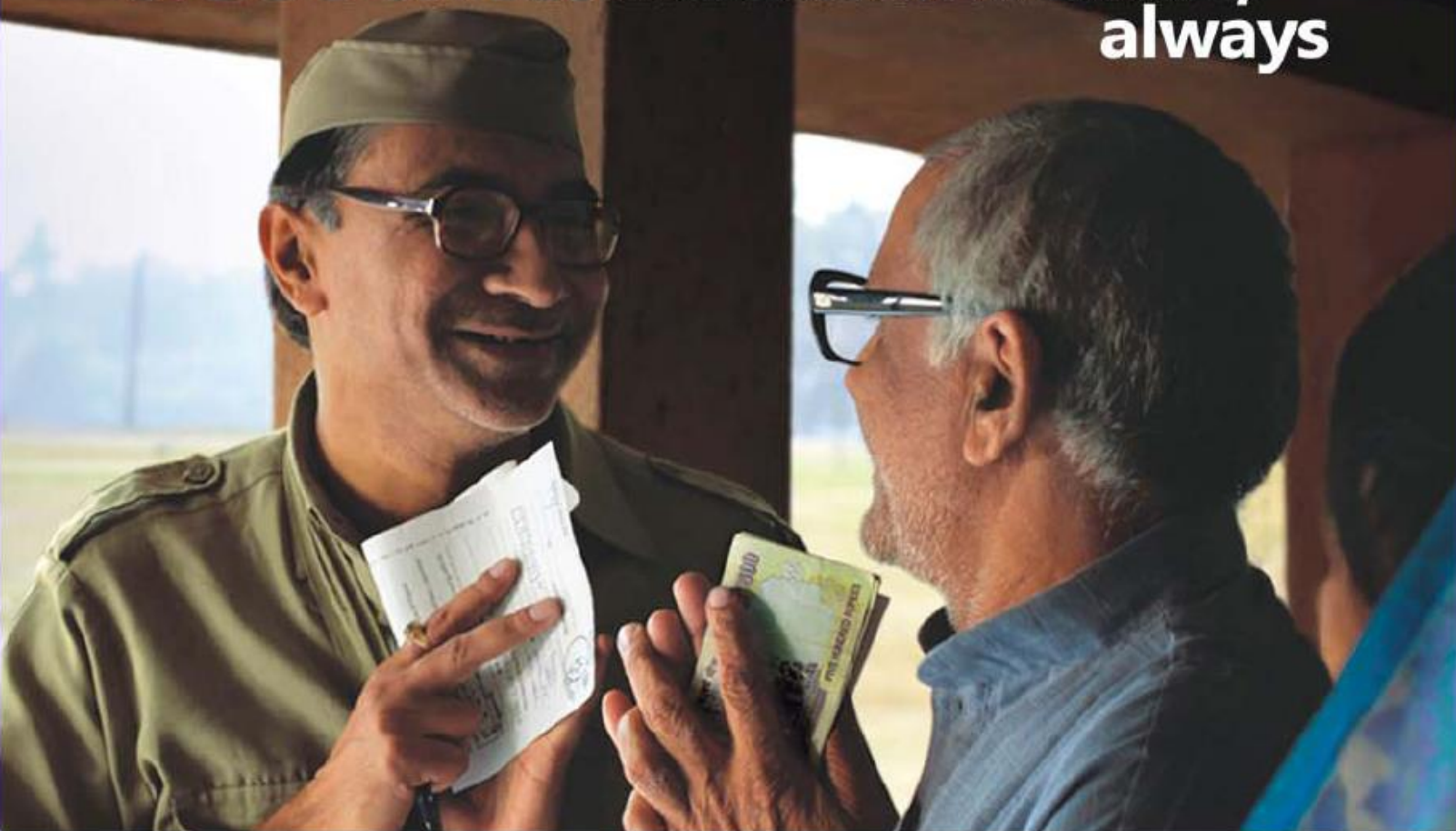
An amount of ₹ 1,00,000 invested individually in all 293 stocks ie, ₹ 2,93,00,000 investment as and when recommended has appreciated to ₹ 3,97,23,649 giving a return of 35.6 percent. On the same basis Nifty has given a return of 13 percent and CNXMID CAP has given a return of 15.2 percent.

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