Punj Lloyd Limited

Value Analysis of Manufacturing System Integration Division ("MSID") as at 31 March 2015

Draft Report

July 1, 2015

Price Waterhouse & Co LLP
Chartered Accountants

Punj Lloyd Ltd.
Group Headquarters, 78 Institutional Area,
Sector 32, Gurgaon 122 001
Haryana, India

Kind attention: Mr. Nidhi Narang, CFO

July 1, 2015

Price Waterhouse & Company LLP
Building 10C, 17th & 18th floor,
DLF Cyber City
Gurgaon – 122002, Haryana
India
Telephone (124) 3306 000
Facsimile (124) 3306 999

Dear Sir,

Draft Report prepared by Price Waterhouse & Co LLP ("PW&Co LLP") in connection with the Value Analysis of Manufacturing System Integration Division ("MSID" or the "Division")

This report has been prepared solely for Punj Lloyd Limited ("PLL") in connection with value analysis of its Manufacturing and System Integration Division ("MSID").

Punj Lloyd Group along with its three entities Punj Lloyd Limited ("PLL"), PL Engineering Limited, Sembawang Engineers and Constructors Pte. Limited and their subsidiaries, joint ventures and associates, is engaged in the business of engineering, procurement and construction in the field of oil, gas and infrastructure sectors.

We understand that PLL has set up MSID, which is a 65 acre facility at Malanpur, Gwalior, Madhya Pradesh. While the unit caters primarily to the Defense and Aerospace sector, it also manufactures components for other engineering sectors like power and transportation to balance capacities and get optimal machine utilization.

Further, Punj Lloyd Infrastructure Limited ("PLIL") is a subsidiary of PLL. We understand that Management of PLL (the "Management") is exploring the possibility of a sale of MSID to PLIL.

In this context, we (Price Waterhouse & Co LLP) have been requested to assist the Management in carrying out value analysis of MSID for internal strategic decision making purposes.

We understand that the valuation is to be carried out as at **March 31, 2015 ("Value Analysis date")**.

Our report has been prepared solely for the Management of PLL for internal benefit and use, in connection with the objective outlined above. The Management may share the report with the Board of Directors and the statutory audit committee. The information shall be provided to auditors only for information purposes in connection with their statutory audit and is not a substitute for their own independent audit procedures. Further it may be noted that PW&Co LLP accepts no responsibility or liability for damage arising from any other use or purpose. Our report is not to be used, referred to or distributed for any other purpose or to any other person without our written permission. We will not accept any liability to any other third party to whom our report is produced/ shown or in whose hands it may come. We shall not be called upon to prove or defend the Value Analysis in any forum within the scope of the present engagement.

In the event that you wish to share our report, or findings thereof with any third party, it shall require our written consent. While this consent would not be unreasonably withheld, we would require a hold harmless letter in a form expressly agreed by us from each such party, to whom the report is proposed to be given.

Our discussions/ interactions with the Management in respect of this Value Analysis is limited to the discussions on the assumptions used in the projections. We will not present our report nor shall be called upon to explain, prove or defend our report at, or before, any forum or authority. As requested, we will discuss our Value Analysis report with the team handling the project at PLL.

To the fullest extent permitted by law, PW&Co LLP accepts no duty of care to any third party in connection with the provision of this report and/or any related information or explanation (together, the "Information"). Accordingly, regardless of the form of action, whether in contract, tort (including, without limitation, negligence) or otherwise, and to the extent permitted by applicable law, PW&Co LLP accepts no liability of any kind to any third party and disclaims all responsibility for the consequences of any third party acting or refraining to act in reliance on the Information.

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This report forms an integral whole and cannot be split in parts. The outcome of Value Analysis can only lead to proper conclusions if the report as a whole is taken into account.

Value Analysis may be based on estimates of future financial performance or opinions that represent reasonable expectations at a particular point in time, but such information, estimates or opinions are not offered as predictions or as assurances that a particular level of income or profit will be achieved, that events will occur, or that a particular price will be offered or accepted. Actual results achieved during the period covered by the prospective financial analysis will vary from these estimates, and the variations may be material. Consequently, this information cannot be relied upon to the same extent as that derived from audited accounts for completed accounting periods. We express no opinion as to how closely the actual results will correspond to the results projected.

We are not required to and have not carried out an audit of nor independently verified the accuracy, reasonableness and completeness of the carved out financial statements of the Division, financial forecasts or key assumptions provided to us for our analysis. Accordingly, we do not express an opinion or offer any form of assurance regarding the accuracy, reasonableness or completeness of these data. We have also used available market data, including those from Bloomberg, Capitaline and other public domains, where appropriate, for which we are not responsible in terms of content and accuracy.

We have not carried out a due diligence exercise or any other validation procedure on the assets and liabilities as part of the Value Analysis.

By its very nature, Value Analysis cannot be regarded as an exact science and the conclusions arrived at in many cases will of necessity be subjective and dependent on the exercise of individual judgment. There is, therefore, no indisputable single value and we normally express our assessment as falling within a likely range. While we consider our range of values to be both reasonable and defensible based on the information available to us, others may place a different value on the business.

Actual results achieved during the period covered by the prospective financial analysis will vary from these estimates, and the variations may be material. Consequently, this information cannot be relied upon to the same extent as that derived from audited accounts for completed accounting periods. We express no opinion as to how closely the actual results will correspond to the results projected.

The value achieved, in case of a transaction, may be different than our Value Analysis depending upon the circumstances and timing of the transaction, if any. The knowledge, negotiability and motivations of the buyers and sellers will also affect actual price achieved. Accordingly, our Value Analysis will not necessarily be the price at which any agreement proceeds. The final transaction price is something on which the parties themselves have to agree.

Please note that our report is in draft form and may be subject to further work, revisions and other factors, which may mean that this draft is substantially different from the final report. Accordingly, this draft should not be relied upon for any purpose whatsoever. If you require any clarification or further information, please do not hesitate to contact me on + 91 - 124 – 3306014.

Yours faithfully,

Rajan Wadhawan

Partner

Table of Content

Glossary of Terms and Abbreviations

Term	Definition
bps	Basis points
CAGR	Compounded Annual Growth Rate
Capex	Capital Expenditure
CAPM	Capital Asset Pricing Model
EBITDA	Earnings Before Interest, Tax, Depreciation and Amortization
EV	Enterprise Value
FCF	Free Cash Flow
FY	Financial Year (From 1 April to 31 March)
INR	Indian National Rupee
Management	Management of Punj Lloyd Limited
MAT	Minimum Alternate Tax
Mn	Million
MSID	Manufacturing and System Integration Division
NWC	Net Working Capital

Glossary of Terms and Abbreviations

Term	Definition
PBT	Profit Before Tax
PAT	Profit After Tax
Projection Period / Forecast Period	FY16-FY20 (1 April 2015 to 31 March 2020)
PW & Co LLP	Price Waterhouse & Co LLP
PLL	Punj Lloyd Limited
PLIL	Punj Lloyd Infrastructure Limited
R&D	Research and Development
Value Analysis Date	As at 31 March 2015
WACC	Weighted Average Cost of Capital
Y-o-Y	Year-on-Year

Introduction

1

Background

Punj Lloyd Group:

- Punj Lloyd Group along with its three entities Punj Lloyd Limited ("PLL"), PL Engineering Limited, Sembawang Engineers and Constructors Pte. Limited and their subsidiaries, joint ventures and associates, is engaged in the business of engineering, procurement and construction in the field of oil, gas and infrastructure sectors.

Manufacturing and System Integration Division ("MSID") Overview:

- PLL's Manufacturing and Systems Integration Division, located at Gwalior, established in the year 2012, is a line fabrication and assembly facility for Defense systems. It is spread over 65 acres of land, capable of high precision manufacturing for both ferrous and non-ferrous material.
- In addition, the facility handles fabrication and machining of land system components, assembly, integration and testing of weapons and maintenance and repair of existing weapons of the Indian Defense Forces.
- We understand that MSID is capable of creating complex aero-structures, air frames and accessories. Also, the Division has participated in tenders for manufacturing and upgradation of weapons for the Government of India.
- Per Management, MSID has been accredited with ISO 9001, ISO 14001, OHSAS 18001, ISO 50001 (Energy Management System) and the AS 9100C Aerospace Standard.

Manufacturing facility:

As Per Management information, the MSID facility comprises:

- Metallurgy and Metrology laboratories;
- Fully equipped fabrication shop, including water jet cutting and stress relieving machines;
- Large bed sizes CNC machines capable of handling ferrous and non ferrous material including composites.

Key Clients:

- As per Management, MSID's clients are spread across sectors like Energy, Aviation and Aerospace, Defense, Transportation & Mining and Shipping.
- Some of the key clients include HAL, Gun Carriage Factory, Nuclear Power Corporation of India, Raja Ramanna Centre for Advanced Technology and Bharat Heavy Electricals Ltd.
- PLL has agreements with leading global companies for collaboration in Indian Defense Programs for a wide range of products including artillery systems, Air Defense gun systems, armored vehicle technology, assault rifles and carbines.

Historical Performance – Income Statement Snapshot

We have relied on the carved out financial statements of MSID for the period March 31, 2013 to March 31, 2015 as provided to us by the Management. It may be noted that we have independently not verified the accuracy and adequacy of these financial statements.

Revenues:

- We understand that MSID was set up as a greenfield facility in the year 2012 and began its operations by mainly catering to the requirements of the Punj Lloyd Group's infrastructure and construction operations. Gradually, as the business began to establish itself, orders started to flow, which has resulted in revenues increasing from INR 14 million in FY13 to INR 191 million in FY15.

Raw material consumption:

- Raw material primarily comprises special steel alloys, titanium, tungsten, aluminum die blocks and other tools, spares and components.
- MSID commenced operations in FY13 and initially the Division was carrying out production of sample/trials. The external order inflow started to increase from FY14 onwards and with this ramp-up in business, the raw material cost as a percentage of revenues started stabilizing in FY14. The raw material consumption as percentage of revenues was 43% in FY15.

	Financial year ending March 31,		
INR million	**2013**	**2014**	**2015**
Net Revenues	14	49	191
Total revenues	**14**	**49**	**191**
Y-o-Y growth		248%	289%
Raw material consumed	18	22	82
% of operating revenues	*129%*	*46%*	*43%*
Employee cost	58	59	68
% of operating revenues	*409%*	*119%*	*36%*
Other expenses	64	61	55
% of operating revenues	*457%*	*125%*	*29%*
Total expenses	**140**	**142**	**205**
Y-o-Y growth		2%	44%
% of operating revenues	*995%*	*290%*	*107%*
Operating EBITDA	**(126)**	**(93)**	**(14)**
EBITDA margin	*-895%*	*-190%*	*-7%*

Source: Management information.

Historical Performance – Income Statement Snapshot

Employee cost:

- Employee cost comprises salary, wages, bonus, contributions towards employee provident fund and other staff welfare schemes. Additionally, it also includes employee cost on contractual laborers.
- Employee cost as a percentage of revenue was at 36% in FY15. As per Management, the employee cost did not grow in line with revenues mainly due to hiring of low cost labor on contractual basis to execute job-work and limited increase in managerial team.

Other expenses:

- Other expenses primarily constitutes travelling & accommodation cost, other manufacturing expenses such as machining charges, power, fuel and water, repairs and maintenance of building, plant and machinery, etc. It also includes land lease rent, selling, general and administrative expenses.
- Other expenses decreased from INR 61 million in FY14 to INR 55 million in FY15. As per Management, this is mainly on account of reduction in travelling & accommodation expenses for managerial team and rationalization of other expenses.

EBITDA margins:

- EBITDA remained negative throughout the period FY13 to FY15. However, as the business started to grow post FY14, the EBITDA margins improved mainly on account of better absorption of fixed expenses.

	Financial year ending March 31,		
INR million	**2013**	**2014**	**2015**
Net Revenues	14	49	191
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Operating EBITDA	**(126)**	**(93)**	**(14)**
EBITDA margin	*-895%*	*-190%*	*-7%*

Source: Management information.

Historical Performance – Balance Sheet Snapshot

Fixed assets:

- As at March 31, 2015, plant and machinery constitutes ~60% of the total Gross Block while building constitutes ~30% and balance comprises land, office equipment, vehicles, tools, furniture & fixtures.
- We understand that the facility is located on 65 acres of land at Malanpur, Gwalior, Madhya Pradesh. Further, we understand that this land is leased for a period of 30 years (starting from November 9, 2009) by Industrial Infrastructure Development Corporation Gwalior Madhya Pradesh Limited.

Long term loans and advances:

- We understand that the loans and advances relates to the amount deposited with the Central Excise Department.

Operating net working capital:

- Current assets primarily constitutes inventories, unbilled revenues (work in progress), trade receivables and loans and advances whereas current liabilities comprises trade payables and other liabilities. Further, other liabilities comprises amount outstanding towards statutory authorities and advance received from customers.
- Management informed that inventory level depends on the nature of job/contract. Historically, since the operations were small, MSID was engaged in manufacturing of products which did not require large inventory.
- Based on our discussions, trade receivables days outstanding are generally in the range of 80 days to 100 days. As at March 31, 2015 the trade receivable days was at 81 days.

	Financial year ending March 31,		
INR million	2013	2014	2015
Gross Block	**1,199**	**1,204**	**1,202**
Less: Acc. Depreciation	(56)	(108)	(181)
Net Block	**1,144**	**1,095**	**1,021**
Current Assets			
Inventories	1	0	0
Unbilled revenue (work-in-progress)	-	20	84
Trade receivables	9	6	42
Loans and advances	82	93	109
Less: Current Liabilities & Provisions			
Trade payables *	83	100	135
Other liabilities	24	36	68
Net Current Assets (excld. Cash)	**(16)**	**(16)**	**33**
CAPITAL EMPLOYED	**1,127**	**1,080**	**1,054**
Add: Accumulated losses	162	313	399
Adj. CAPITAL EMPLOYED	**1,290**	**1,393**	**1,453**
Funded by:			
Head Office	1,184	1,283	1,321
Short term borrowing	24	16	7
Trade Payable considered as debt	83	100	135
Less: Cash in hand	2	6	10
TOTAL FUNDING	**1,290**	**1,393**	**1,453**

Source: Management information.
** According to Management, ~50% of the Trade Payables appearing in the Balance Sheet are payable to other businesses/SBU's of PLL. For our analysis, the same have been considered as debt.*

Historical Performance – Balance Sheet Snapshot

Operating net working capital (Contd'):

- Adjusted net working capital (post adjustment of 50% Trade Payables of INR 135 million considered as debt) as at March 31, 2015 amounts to INR 33 million.
- Management informed that the entire cash and bank balances appearing in the balance sheet is to be considered as surplus.

Debt:

- Management represented that short term borrowings of INR 7 million appearing in the balance sheet as at March 31, 2015 is at an interest rate of 12% p.a.

Contingent liabilities:

- Management represented that there are no contingent liabilities appearing at at March 31, 2015 that would materially impact the valuation.

	Financial year ending March 31,		
INR million	**2013**	**2014**	**2015**
Gross Block	**1,199**	**1,204**	**1,202**
Less: Acc. Depreciation	(56)	(108)	(181)
Net Block	**1,144**	**1,095**	**1,021**
Current Assets			
Inventories	1	0	0
Unbilled revenue (work-in-progress)	-	20	84
Trade receivables	9	6	42
Loans and advances	82	93	109
Less: Current Liabilities & Provisions			
Trade payables *	83	100	135
Other liabilities	24	36	68
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TOTAL FUNDING	**1,290**	**1,393**	**1,453**

Source: Management information.
** According to Management, ~50% of the Trade Payables appearing in the Balance Sheet are payable to other businesses/SBU's of PLL. For our analysis, the same have been considered as debt.*

Value Analysis

1.1

Value Analysis approaches and principal assumptions

Basis of Value Analysis

- The basis of the Value Analysis that we have adopted in arriving at our Value Analysis is "Fair Value". We define Fair Value as the price which a business might reasonably be expected to fetch, in money or money's worth in an open market sale, between a willing buyer and a willing seller, both of whom are equally well informed about the business and the markets in which it operates and each of whom is deemed to be acting for its self-interest.
- Value Analysis has been carried out as at **March 31, 2015** ("Value Analysis Date").

Value Analysis approaches adopted

Generally the following approaches are used while carrying out Value Analysis:

- **Income Approach:** This approach indicates the value of a business based on the value of the cash flows that the business can be expected to generate in the future.
- **Market Approach**: This approach indicates the value of a business based on a comparison of the business to comparable publicly traded companies and as well as prior business transactions in the industry.

  The Market Approach indicates the value of a business on a going concern basis, based on a comparison of the business to comparable publicly traded companies and as well as prior business transactions in the industry. We understand that there are no listed guideline companies in India which are strictly comparable to MSID's business in terms of business profile and customer concentration. Hence, Market Multiple Method was not considered in our Value Analysis.

  Further, Market Transactions Method, was not considered owing to the absence of strictly comparable transactions and paucity of publicly available data on transactions in the relevant industry.

- **Net Asset Value Approach:** This approach indicates the value of the business by adjusting the assets and liabilities appearing in the balance sheet of the company which is being valued as at the Value Analysis date. This approach is based on the summation of individual piecemeal values of the underlying assets less the book value of the liabilities. This value may not be a good indicator of the realizable value as it merely reflects historic costs and requires adjustments on account of estimated disposal costs and possible shortfall or appreciation in realization of both fixed assets and net current assets.

For our analysis Net Asset Value Approach has been considered for benchmarking purposes. For our analysis under this approach, we have relied on the Balance Sheet presented as at March 31, 2015. The book values have been adjusted considering the Fair market value certificate of fixed assets dated January 7, 2015 prepared by a third party valuer, K. LAL & ASSOCIATES, as provided to us by the Management and no adjustment for the value of intangibles, if any comprised in the business has been carried out.

Value Analysis approaches and principal assumptions

Principal Assumptions

- Our Value Analysis is subject to specific representations and assumptions which you consider necessary and appropriate. In addition, please refer the following section on the key assumptions underlying the Value Analysis.
  - MSID is valued on a going concern basis. The business continues to operate till the end of forecast period i.e. FY20, which will enable the achievement of the financial forecasts;
  - Information provided by the Management is up to the date of this report fairly reflects MSID's business, financial and operating positions. In addition, for the purpose of this exercise, Management has provided us carved out financials of MSID for the period March 31, 2013 to March 31, 2015. It may be noted that we have independently not verified these financials;
  - We understand that the facility is located on 65 acres of land at Malanpur, Gwalior, Madhya Pradesh. Further, we understand that this land is leased for a period of 30 years (starting from November 9, 2009) by Industrial Infrastructure Development Corporation Gwalior Madhya Pradesh Limited. As per Management representation, there are no surplus/idle assets that are attributable to MSID;
  - There are no undisclosed actual or contingent assets or liabilities, no unusual obligations or substantial commitments, other than in the ordinary course of business and as reflected in the financials, nor any litigation pending or threatened, which would have a material impact on the Value Analysis of MSID;
  - The other assumptions specifically outlined in the ensuing sections of this report hold true.

Sources of Information

- The key information we have received and used in our value analysis include:
    - Carved out financial statements* of MSID for FY13, FY14 and FY15;
    - Lease deed dated November 9, 2009 for land in Industrial Area Ghirongi, Malanpur, Gwalior, Madhya Pradesh;
    - Business plan along with the underlying assumptions for MSID as prepared by the Management over the period FY16 to FY20 ("Projected Period" or "Forecast Period"), which the Management believes to be their best estimate of the expected future operating results;
    - Fair market value certificate of fixed assets dated January 7, 2015 prepared by a third party valuer, K. LAL & ASSOCIATES, as provided to us by the Management.
    - other information provided by the Management.
- We have also used publicly available information sources (e.g. Bloomberg and Capitaline), to gather industry related information including comparable companies;

**Note: We have not independently verified the carved out financial statements of MSID as prepared by the Management.*

- In addition, we have obtained information through discussion and correspondence with the Management. We had discussions with Mr. Ashok Wadhawan (President-Manufacturing Division) and Mr. Rahul Maheshwari (Senior Manager-Finance) and;
- We have also undertaken analysis of other facts and data considered pertinent to this value analysis.

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Projected financial performance

Forecasts for the “Projection period”/ “Forecast period” (FY16 -FY20) as provided by the Management are shown below. The forecast revenues for MSID, comprises revenues from component manufacturing and Defense Program. Revenues from component manufacturing comprises revenues from sale of parts and aerostructures to Defense and Aerospace sector.

Management informed that revenues from Defense Program relates to potential revenues from manufacturing and upgradation of weapons for the Government of India. From discussions with Management, we understand that MSID had bid for Defense tender ~4.5 years ago that is currently pending approval from Defense Ministry. There is a high likely hood of MSID winning the above mentioned bid mainly due to the fact that MSID’s product has already cleared the technical qualification and now remains as one of the only two bidders for the tender (originally there were a total of 6 bidders).

	Financial year ending March 31,					
INR million	2015 Actual	2016 Forecast	2017 Forecast	2018 Forecast	2019 Forecast	2020 Forecast
Net Revenues (Component Manufacturing)	191	450	700	1,100	1,500	2,000
Y-o-Y growth		*136%*	*56%*	*57%*	*36%*	*33%*
Net Revenues (Defense Program)	-	-	250	1,250	1,500	1,393
Y-o-Y growth		*n/a*	*n/a*	*400%*	*20%*	*-7%*
Total Revenues	**191**	**450**	**950**	**2,350**	**3,000**	**3,393**
Y-o-Y growth		*136%*	*111%*	*147%*	*28%*	*13%*
Raw materials consumed (Manufacturing)	82	162	252	385	525	700
% of operating revenues	*43%*	*36%*	*36%*	*35%*	*35%*	*35%*
Raw materials consumed (Defense Program)	-	-	183	913	1,095	1,017
% of operating revenues	*n/a*	*n/a*	*73%*	*73%*	*73%*	*73%*
Total raw material consumed	**82**	**162**	**435**	**1,298**	**1,620**	**1,717**
% of operating revenues	*43%*	*36%*	*46%*	*55%*	*54%*	*51%*
Other expenses (Manufacturing)	122	194	294	451	615	820
% of operating revenues	*64%*	*43%*	*42%*	*41%*	*41%*	*41%*
Other expenses (Defense Program)	-	150	220	220	160	251
% of operating revenues			*88%*	*18%*	*11%*	*18%*
Total expenses	**205**	**506**	**949**	**1,969**	**2,395**	**2,788**
% of operating revenues	*107%*	*112%*	*100%*	*84%*	*80%*	*82%*
Operating EBITDA (Manufacturing)	**(14)**	**95**	**154**	**264**	**360**	**480**
EBITDA Margins	*-7%*	*21%*	*22%*	*24%*	*24%*	*24%*
Operating EBITDA (Defense Program)	**-**	**(150)**	**(153)**	**118**	**245**	**125**
EBITDA Margins	*n/a*	*n/a*	*-61%*	*9%*	*16%*	*9%*
Total EBITDA	**(14)**	**(56)**	**2**	**382**	**605**	**605**
EBITDA Margins	***-7%***	***-12%***	***0%***	***16%***	***20%***	***18%***

Source: Management information.

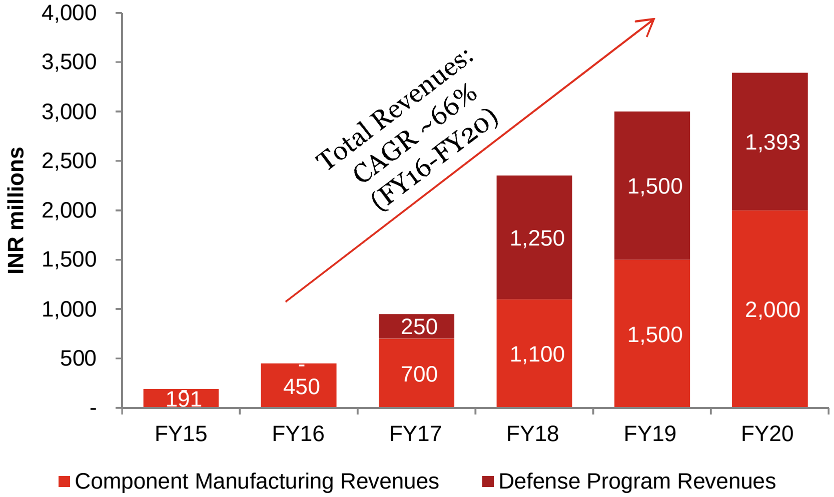
Projected financial performance

Management has provided us projected income statement of MSID (constituting component manufacturing and Defense Program business) for the period FY16 to FY20.

Operating revenues:

- We understand that revenues for MSID, comprises revenue from component manufacturing and Defense Program business.
- Revenues from component manufacturing business are projected to significantly increase from INR 191 million in FY15 to INR 450 million in FY16.
- Management informed that the Division has a confirmed order book of ~ INR 450 million which is expected to be executed in the FY16.
- Going forward, revenues from component manufacturing business is expected to increase at a CAGR of ~45% from FY16 to FY20. This expected increase is based on;
  - current order book;
  - executed Memorandum of Understanding ("MOU")* with international partners, for supply of components to small arms manufacturers and Aerostructures.
- Per Management additional revenues over the projection period as a result of supplying components to small arms manufacturers is expected to contribute ~INR 1,000 million and the revenues from sale of Aerostructures are expected from FY18 onwards.
- As discussed earlier the projected revenues from the Defense Program business are expected from a Defense Project for which bid had been submitted ~4.5 years ago. Management expects revenues of ~ INR 4,400 million from the award of this contract the over the projection period FY17 to FY20.

Operating revenues:



Source: Management information

**Owing to its confidentiality, limited information was made available to us*

Projected financial performance

Raw Material Consumption ("RMC"):

- Per Management historically the raw material prices for component manufacturing business remained high since the quantum of orders were small and it was directly purchasing all the raw materials. However, as per Management with orders size increasing and alteration in product mix Raw Material Consumption as a percentage of revenues for component manufacturing business is expected to decrease from 43% in FY15 to 36% in FY16. Subsequently, it is expected to be in the range of 35% to 36% during FY17 to FY20.
- Management represented that Raw Material Cost for the Defense Program business is specific to the Defense Project for which bid had been submitted. Management expects RMC as a percentage of revenues for Defense Program business to remain at 73% over the projection period FY17 to FY20.

Other expenses:

- Other expenses during the projection period primarily comprises job work related cost, other manufacturing cost, employee salaries, repair and maintenance, land lease rentals and selling, general and administrative expenses.
- Other expenses of component manufacturing business as a percentage of revenues are expected to decrease from ~64% in FY15 to ~43% in FY16, mainly on account of increase in volumes leading to economies of scale. Further, Management expects this percentage to remain in the range of 41% to 42% during the period FY17 to FY20.

Other expenses (Contd'):

- Other expenses for Defense Program business comprises other manufacturing cost and trial and marketing costs incurred to focus on other Defense Program tenders. We understand that Management intends to bid for additional Defense Programs for which it expects to incur certain trial and marketing costs in FY20. Given this, Managements expects other expenses as a percentage of revenues to sharply increase from 11% in FY19 to 18% in FY20, mainly due to increase in these costs.

EBITDA margins:

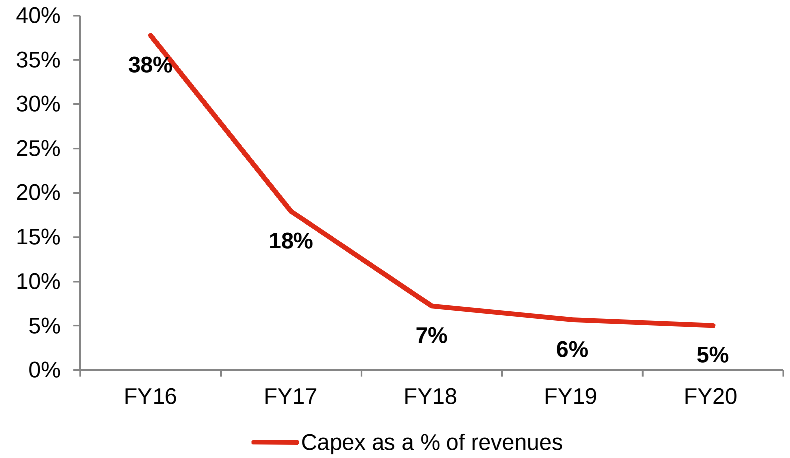
- Management expects EBITDA margin for component manufacturing business to significantly improve from negative 7% in FY15 to 21% in FY16, mainly on account of:
  - ✓ Change in the product mix during this period which will result in decreasing the raw material expenses (refer raw material consumption section for details) and;
  - ✓ Achieving economies of scale during this period leading to better absorption of expenses (refer other expenses section for details);
- Management expects EBITDA margins to remain in the range of 22%-24% during FY17 to FY20 on account of better price realization. As per Management, EBITDA margins for MSID is expected to be higher vis-à-vis other players in the industry mainly on account of it operating in a niche segment requiring specialized manufacturing capabilities.
- EBITDA margins for the Defense Program business is expected to remain negative during the period FY16 to FY17 mainly on account of high expenses and low revenues. However, Management expects EBITDA margins to stabilize at 9% in FY20.

Projected financial performance

Capital Expenditure ("capex")

- We understand that Management has envisaged a total capital outlay of INR 850 million, which is equally spread over the projection period i.e. INR 170 million of capex expected every year.
- Further, Management represented that out of total capex of INR 850 million, ~INR 400 million is towards setting up of infrastructure for manufacturing of Aerostructures, ~INR 220 million is towards ramping up of component manufacturing facility for small arms manufacturing and ~INR 110 million is incurred for enhancement of the existing capacity. Balance INR 120 million of capex is for execution of Defense Program project.

Capital expenditure

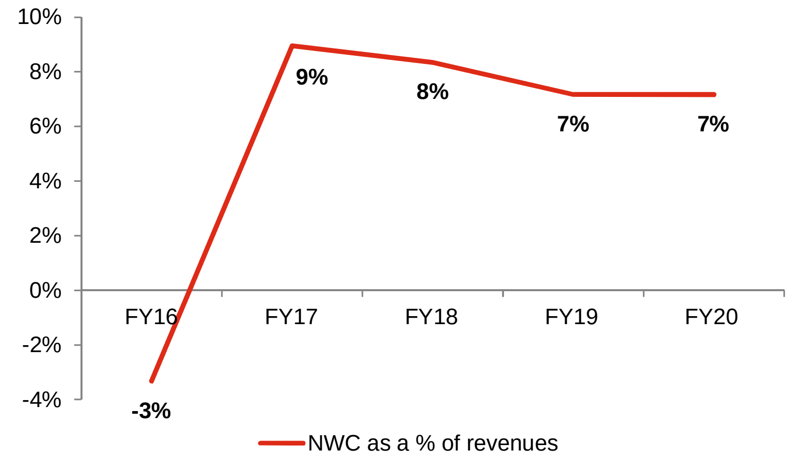


Source: Management information, PW&Co LLP analysis

Operating working capital requirement:

- Operating net working capital is estimated to increase from negative 3% of operating revenues in FY16 to 9% in FY17. This is mainly on account of increase in revenues which results in high proportion of revenues being accounted as trade receivable and work in progress (unbilled revenues).
- Going forward, net working capital as a percentage of revenues is projected to remain in the range of 7% to 8% during the period FY18 to FY20.

Net working capital



Source: Management information, PW&Co LLP analysis

Value Analysis – Income approach

Weighted Average Cost of Capital

- The Weighted Average Cost of Capital ("WACC") represents the weighted average return attributable to all of the assets of the business. We have used Capital Asset Pricing Model ("CAPM") for estimation of Cost of Equity and WACC.
- For the purpose of arriving at the debt-equity ratio of MSID, we have considered the industry debt-equity ratio i.e. ~22.8%.
- We have considered a range of additional risk premium of 1.75% - 2.25% to factor in the additional risks on account of;
    - risk pertaining to achievement of significant growth in revenues and EBITDA margins during the projection period;
    - uncertainty regarding the successful winning of the tenders relating to Defense projects.
- Based on the above, we have considered WACC in the range of 14.00% to 14.50%. Please refer Appendix 1 for details.
- We have assumed that the cash flows accrue to MSID uniformly through the year, and have thus considered a mid-period discounting factor for this analysis.

Taxation:

- We understand that the Division has accumulated business losses and unabsorbed depreciation amounting to INR 615 million as at Value Analysis Date. For our analysis the same have been considered and tax outflows have been determined based on applicable tax rates as per Income Tax Act, 1961, i.e. 34.61% corporate tax rate and 21.34% MAT rate whichever is applicable.

Terminal Value

- We have assumed a perpetuity growth rate in the range of 4.75% to 5.25% in our terminal value calculations considering industry and macro economic factors.
- Management represented that for the terminal period, capex can been assumed at INR 155 million assuming a useful life of the assets as ~13 years.

Interest bearing Debt, Non-operating Assets and Contingent Liabilities

- Debt represented as short term borrowing appearing in the balance sheet of MSID as at March 31, 2015 is INR 7 million. Additionally, Management represented that an amount of INR 135 million included within the trade payables appearing as at March 31, 2015, is considered as debt funding from the Punj Lloyd Group.
- We understand from the Management that there are no non-operating assets other than surplus cash as on the Value Analysis date.
- Further, Management represented that there are no contingent liabilities as at March 31, 2015.

Projected Free cash flows

INR million		Fiscal Year ending March 31, 2015	2016	2017	2018	2019	2020	Normalized Period
Operating Revenue		**191**	**450**	**950**	**2,350**	**3,000**	**3,393**	**3,563**
Revenue growth		*289.0%*	*136.0%*	*111.1%*	*147.4%*	*27.7%*	*13.1%*	*5.0%*
Operating EBITDA		**(14)**	**(56)**	**2**	**382**	**605**	**605**	**636**
EBITDA Margin		*-7.3%*	*-12.3%*	*0.2%*	*16.2%*	*20.2%*	*17.8%*	*17.8%*
Less: Depreciation		-	107	114	121	127	131	131
EBIT		**-**	**(163)**	**(112)**	**260**	**478**	**474**	**504**
EBIT margin			*-36.2%*	*-11.8%*	*11.1%*	*15.9%*	*14.0%*	*14.2%*
Tax	***34.61%***	-	**-**	**-**	**7**	**113**	**112**	**175**
Tax as a % of EBIT					*2.58%*	*23.55%*	*23.59%*	*34.61%*
Operating Income (after Tax)			**(163)**	**(112)**	**254**	**365**	**362**	**330**
Plus: Depreciation			107	114	121	127	131	131
Less: Capital expenditure			170	170	170	170	170	155
as % of Revenue			*37.8%*	*17.9%*	*7.2%*	*5.7%*	*5.0%*	*4.4%*
Less: Change in net working capital			(48)	100	111	19	28	12
Free Cash Flows		-	**(177)**	**(269)**	**94**	**303**	**295**	**294**

Sensitivity Analysis
(Discount rate vs Long term growth)

Enterprise Value	14.00%	14.25%	14.50%
4.75%	1,850	1,784	1,721
5.00%	1,902	1,832	1,767
5.25%	1,956	1,883	1,814

Low Indication: Enterprise Value	**1,721**
High Indication: Enterprise Value	**1,956**

Source: Management information, PW&Co LLP analysis

Based on this Approach the Value Analysis of MSID is assessed to be in the range of INR 1,721 million - INR 1,956 million

Value Analysis – Net Asset Value Approach

For benchmarking purposes only

- The value under this approach, particularly when this approximates the realizable value, is often used as an estimate of “break-up value”, and therefore, is particularly relevant in the event of liquidation. Given the purpose of the Value Analysis, the value as per the Net Asset Value approach has been considered for benchmarking purposes only.
- We have arrived at the adjusted enterprise value of MSID under the Net Asset Value approach, which is based on summation of the individual piecemeal values of the underlying assets of MSID.
- For estimation of adjusted enterprise value, book value of Net Block as of March 31, 2015 (as provided by the Management) comprising land, building, plant and machinery, furniture, fixtures & office equipment and tools is adjusted to reflect the fair market value. For fair market value of fixed assets, we have relied on fair market value certificate of K.LAL & ASSOCIATES dated January 7, 2015, provided to us by the Management. We have not carried out any independent verification /due diligence on the valuation provided by the said valuer
- Using this approach, the enterprise value of MSID as at March 31, 2015 is ~**INR 1,580 million.** It may be relevant to mention that while this captures the current replacement value of tangible assets, it does not take into account the intangibles comprised in the business such as, licenses, goodwill, customer/supplier relationships, workforce etc.

Net Asset Value (“NAV”) Approach

INR million	Book Value as of March 31, 2015	Value considered as of March 31, 2015
Net Block		
Land	53	80
Building	330	423
Furniture and office equipment	11	26
Intangibles	2	2
Plant and Machinery	601	977
Tools	24	39
Vehicles	0	0
Total Non Current Assets (A)	**1,021**	**1,547** *
NET CURRENT ASSETS		
Current Assets		
Inventories	0	0
Unbilled revenues	84	84
Trade receivables	42	42
Loans and advances	109	109
Total current assets	**236**	**236**
Current Liabilities & Provisions		
Trade Payables	135	135
Other Current Liabilities	68	68
Total current liabilities and provisions (B)	**203**	**203**
Total Net Current Assets (A+B)	**33**	**33**
ENTERPRISE VALUE	**1,054**	**1,580**

Source: Management information and PW&Co LLP analysis
**For fair market value of fixed assets, we have relied on fair market value certificate of K.LAL & ASSOCIATES dated January 7, 2015, provided to us by the Management. We have not carried out any independent verification /due diligence on the valuation provided by the said valuer*

Value Analysis – Conclusion

In concluding on our Value Analysis, it may be noted our premise is fair value for the purpose of this engagement. Fair Value is defined as the price which a business might reasonably be expected to fetch, in money or money's worth in an open market sale, between a willing buyer and a willing seller, both of whom are equally well informed about the business.

As discussed earlier, the enterprise value arrived under the net asset approach is for benchmarking purposes only.

For the purpose of arriving at the Enterprise Value range, we have placed reliance on DCF method, (an application of the Income approach), considering the lack of strictly comparable listed companies in India. Accordingly, the 100% Enterprise Value for MSID works out to be in the range of :

INR 1,721 million to INR 1,956 million

	Value Range	
INR million	**Low**	**High**
Value summary		
Income Approach-DCF Method	**1,721**	**1,956**
Enterprise Value	**1,721**	**1,956**
Enterprise Value for benchmarking purposes		
Adjusted Net Asset Value	*1,580*	*1,580*

Source: Management information, PW&Co LLP analysis

Appendix 1: Weighted Average Cost of Capital

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Appendix 1: Weighted Average Cost of Capital

Particulars		Range		Source
Risk free rate as at March 31, 2015		7.8%		Risk Free Rate based on Zero Coupon Yield Curve as at March 31st, 2015 (Source: NSE)
Market Risk-premium		7.0%		Price Waterhouse & Co LLP consensus rate
Additional risk premium	1.75%	2.0%	2.25%	On account of a) higher revenue growth rate assumed during the projection period and; b) uncertanity regarding the successful winning of the tenders relating to defence projects bid by the Company.
Unlevered beta		0.70		Based on the analysis of the guideline companies unlevered beta
Debt-Equity ratio		22.8%		Industry Debt equity ratio median considered
Relevered beta		0.86		The beta (rounded) is relevered using selected D/E.
Cost of debt (pre-tax)		12.0%		Per Management information
Tax rate		34.6%		Corporate tax rate considered as per the notification of the Finance Bill, 2015.
Cost of debt (post-tax)		**7.8%**		
Cost of Equity (rounded)		**15.8%**		Cost of Equity = Rf + B (Rp) + Additional risk premium
WACC (Post-Tax)	**14.0%**	**14.3%**	**14.5%**	**WACC = (Kd * D/E + Ke) / (1 + D/E)**

PW&Co LLP analysis

Companies in component manufacturing industry considered for beta includes Bharat Forge, Sundaram Fasteners, MM Forgings, Alicon Castings, Nelcast and Dynamatic Technology. Refer Appendix 2 for brief business description.

Appendix 2: Guideline comparable companies

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Appendix 3: Guideline Comparable Companies

Company	Business description
Bharat Forge Limited	Bharat Forge Limited manufactures steel forgings and machined components for the automotive, diesel engine, railway, earthmoving, cement, sugar, steel, coal, ship building and oilfield industries. The Company specializes in Closed Die as well as Open Die Forgings.
Sundram Fasteners Limited	Sundram Fasteners Limited manufactures a wide range of nuts, bolts and related fastener equipment. Products include high-tensile fasteners and equipment for the automotive industry, such as cold extruded parts, radiator caps and gear shifters. The Company also manufactures water pumps and fuel pumps.
M M Forgings	MM Forgings is engaged in manufacturing forging components. The Company manufactures steel forgings in raw, semi-machined and fully machined stages in various grades of carbon, alloy, micro-alloy and stainless steels in the weight range of 0.20 kilograms to 60 kilograms. The Company caters to the forging requirements of almost all sections of industry.
Alicon Cast.	Alicon Castalloy Ltd. manufactures aluminium alloy castings. The Company produces parts for the automotive, agricultural equipment, marine, medical devices, locomotive, extreme sports apparatus and power industries.
Nelcast	Nelcast Limited manufactures a wide range of ductile iron and grey iron castings ranging from 0.5 Kgs to 250 Kgs. The Company's products include grey iron castings, cylinder blocks, housings, rear hubs, spring, shackle, brackets, and exhaust manifolds.
Dynamatic Tech.	Dynamatic Technologies Limited is an India-based company, engaged in the business of manufacturing automotive components, hydraulics gear pumps, aerospace components and wind farm power generation. The Company designs and builds engineered products for automotive, aeronautic, hydraulic and defense industries. The Company is organized into four business segments: Hydraulic and Precision Engineering (HPE), which comprises hydraulic pumps, hand pumps, lift assemblies, valves and power packs; Automotive Components (AUC), which comprises case front, water pumps, intake manifolds and exhaust manifold; Aerospace (ASP) comprises airframe structures, precision aerospace, components and Homeland division and others comprising wind farm and corporate division, and Research farm (RF), which is engaged in finding solutions by testing and validating pumps used in mechanized farming and earth moving sectors to suit real time field conditions.

Source: Bloomberg Database

Appendix 3: Contact information

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Contact Information

For further information please contact:

Name: Rajan Wadhawan

Designation: Partner

Tel. no.: (91) 124 330 60 14

e-mail: rajan.wadhawan@in.pwc.com

Name: Dhruva Sabharwal

Designation: Associate Director

Tel. no.: (91) 124 3306348

e-mail: dhruva.sabharwal@in.pwc.com