



KINETIC

Report



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KINETIC ENGINEERING LTD.

Annual Report 2004 - 2005

New Strategic Business Unit created for auto-component manufacturing

Last year, Kinetic Auto Systems, a special new strategic business unit (SBU) was created to tap business opportunity in manufacturing of auto-components for the Indian as well as global automotive industry. Kinetic Auto Systems will harness our inherent strengths in this area including expertise, facilities and skilled manpower.

Reliance Capital Limited picks up 14.81% equity stake in Kinetic Engineering

Reliance Capital Limited acquired 14.81% equity stake in Kinetic Engineering. The investment will be utilized for building Kinetic Auto Systems for manufacturing of automotive components for Indian and global automotive companies.

A new premium brand logo adopted



For our two wheeler manufacturing and marketing business, last year we adopted a new brand logo to create a new, more contemporary identity. The new logo now appears on all Kinetic two wheelers, dealership insignia, advertising and other brand related initiatives. A new website has also been designed and launched to reflect the new brand identity.

Visit at www.kinetic2wheelers.com

Exciting Kinetic Comet launched, won "Import Bike of the Year" award from Business Standard Motoring

We introduced a limited edition of the exciting 250cc high-performance and high technology stunner Comet which is India's most premium and aspirational motorcycle. Comet won the "Import Bike of the Year" award from renowned automobile specialist magazine Business Standard Motoring.

KINETIC ENGINEERING LIMITED

Board of Directors

Mr. A. H. FIRODIA	Chairman
Dr. N. A. KALYANI	
Mr. S. C. SHAH	
Dr. K. H. SANCHETI	
Mr. S.C. BHAVE	
Mr. S. R. SANGHI	
Mr. S. R. KOTECHA	
Mr. M. K. KHERA	Joint Managing Director
Mrs. SULAJJA FIRODIA MOTWANI	Joint Managing Director

Auditors

M/s. P G BHAGWAT
Chartered Accountants, Pune

Cost Auditors

M/s.DHANANJAY V. JOSHI & CO.
Cost Accountants, Pune

Index

Page No.

Bankers

STATE BANK OF INDIA
CANARA BANK
PUNJAB NATIONAL BANK
IDBI BANK LTD.
BANK OF BARODA
STATE BANK OF INDORE
ICICI BANK LTD.

1. AGM Notice	2
2. Directors' Report	4
3. Management Discussion and Analysis Report	7
4. Report on Corporate Governance	9
5. Certificate from Auditors on Compliance of Corporate Governance	15
6. Auditors' Report	16
7. Balance Sheet, P&L A/c, Schedules and Cash Flow	20
8. Statement u/s 212	40
9. Auditors' Report on Consolidated Financial Statements	42
10. Consolidated B/S, P&L A/c, Schedules and Cash Flow	43
11. Proxy Form	59

Registered Office

D1 BLOCK, PLOT NO.18/2,
CHINCHWAD, PUNE - 411 019.

KINETIC ENGINEERING LIMITED

NOTICE

NOTICE is hereby given that the 35th Annual General Meeting of the Members of KINETIC ENGINEERING LIMITED will be held on Wednesday, 22nd March, 2006 at 9.30 a.m. at the Registered Office of the Company at D-1 Block, Plot No. 18/2, MIDC, Chinchwad, Pune - 411 019 to transact the following business:

ORDINARY BUSINESS

1. To consider and adopt the Directors' Report, the Audited Balance Sheet as at 30th September, 2005 and the Profit and Loss Account for the 18 months period ended on that date together with Auditors' Report thereon.
2. To appoint a Director in place of Dr. K.H. Sancheti, who retires by rotation and being eligible, offers himself for re-appointment.
3. To appoint a Director in place of Mr. S. R. Kotecha, who retires by rotation and being eligible, offers himself for re-appointment.
4. To appoint Auditors and fix their remuneration.

SPECIAL BUSINESS

5. To appoint Mr. S. C. Bhavé as Director of the Company who holds office of Director upto the date of ensuing Annual General Meeting and in respect of whom the Company has received a Notice in writing from a member proposing his candidature for the office of Director and signifying his intention to move the following Resolution as an Ordinary Resolution :

"RESOLVED THAT Mr. S.C. Bhavé be and is hereby appointed as Director of the Company."

NOTES :

1. A MEMBER ENTITLED TO ATTEND AND VOTE AT THE SAID MEETING IS ENTITLED TO APPOINT A PROXY TO ATTEND AND VOTE INSTEAD OF HIMSELF AND A PROXY NEED NOT BE A MEMBER.
2. The Explanatory Statement setting out the material facts concerning the Special Business mentioned in item No. 5 of Notice of the Meeting as required by Section 173 of the Companies Act, 1956 and information in respect of the Directors seeking re-appointment at the Annual General Meeting (Item Nos. 2 and 3 of the Notice) as per clause 49 of the Listing Agreement, are annexed hereto.
3. The Register of Members and Share Transfer Books of the Company will be closed from Wednesday, 1st February, 2006 to Friday, 10th February, 2006 (both days inclusive) for the purpose of Annual General Meeting.
4. In view of amended Section 205C of the Companies Act, 1956 followed by the issue of Investor Education & Protection Fund (awareness and protection of the investors) Rules, 2001, any money transferred by the Company to the unpaid dividend account and remaining unclaimed for a period of seven years from the date of such transfer shall be transferred by the Company to Investor Education & Protection Fund (IEPF) set up by the Central Government. Accordingly, the Company has transferred to IEPF the unclaimed dividend for the year ended 31st March, 1997 on 9th November, 2004. The Unclaimed Dividend for the year ended 31st March, 1998 has been transferred to IEPF on 6th December, 2005.

The amount of dividend remaining unclaimed for a period of 7 years from the date of transfer to unpaid dividend account for every subsequent years upto 2001-2002, will also be transferred to IEPF every year. No claims shall lie thereafter against IEPF or the Company in respect of the amounts transferred as aforesaid.
5. Members desirous of obtaining any information concerning the accounts or operations of the Company are requested to address their questions to Finance Department so as to reach at least 10 days before the date of the meeting so that the information required may be made available at the meeting.

By Order of the Board Directors
For KINETIC ENGINEERING LIMITED



A. H. FIRODIA
Chairman

Pune
30th December, 2005

EXPLANATORY STATEMENT PURSUANT TO SECTION 173 OF THE COMPANIES ACT, 1956 AND INFORMATION IN RESPECT OF DIRECTORS SEEKING RE-APPOINTMENT AT THIS ANNUAL GENERAL MEETING AS PER CLAUSE 49 OF THE LISTING AGREEMENT.**Mr. S. C. Bhave**

Mr. S. C. Bhave, 63, is retired Chief General Manager of State Bank of India (SBI). During his service of more than 3 decades with SBI, he has held responsible positions in Indian as well as foreign Branches of SBI. He is Nominee Director of SBI from 31/1/2005. Presently he is on the Board of Directors of Ventura Textiles Ltd. as Nominee Director of SBI.

Dr. K. H. Sancheti

Dr. K. H. Sancheti, 69, is one of the most renowned Orthopaedic Surgeon in the Country and is Honorary Surgeon to H. E. Governor of Maharashtra. Dr. Sancheti comes from a humble background. He graduated from Pune University and did his Post Graduation from Mumbai and Chicago (US) Universities. He has done innovative work to design and develop artificial knee-joint and successfully introduced the knee transplant technique which is widely used in India and abroad. He did pioneering work in starting Sancheti Hospital and Sancheti Institute for Orthopaedics and Rehabilitation. The R & D Centre of the hospital has produced several publications so far. He is very actively involved in many social activities holding diagnostic and operative camps. Dr. Sancheti was awarded "Padmashree", the much coveted decoration for his public service. Dr. Sancheti is on the Board of Envair Electrodyne Ltd, Poona Health Services Pvt. Ltd. and Medicon Enterprises Pvt. Ltd.

Mr. S. R. Kotecha

Mr. S. R. Kotecha, 54, is MS Automobiles from Kansas State University, USA. He has 27 years working experience in manufacture of auto components. He is Chairman of Champ Engineering Pvt. Ltd. of which Engineering Division manufactures auto components. He has published research papers on crop agronomy and has done research on innovative farming methods. He is President of Indian Tissue Culture Association. He has also gained experience of handling Accounts, Finance & Commercial matters.

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KINETIC ENGINEERING LIMITED

DIRECTORS' REPORT 2004-2005

To

The Members,

Your Directors present 35th Annual Report and Audited Statement of Accounts of the Company for the 18 months period ended 30th September, 2005.

CHANGE IN FINANCIAL YEAR

Accounting year of the Company was extended by 6 months. Accordingly, the Statement of Accounts is prepared for the 18 months period ended 30th September, 2005.

FINANCIAL HIGHLIGHTS

	2004-05 (18 months)	2003-04 (12 months)
	(Rs. in lakhs)	
Gross Sales and other Income	24288	24022
Loss for the period / year	(5496)	(5166)
Profit / (Loss) carried Forward		
Last year	2665	7831
This year	(2831)	2665

Please refer to the "Management Discussions and Analysis Report" which inter-alia discusses performance of the Company for the 18 months period ended 30th September, 2005.

YEAR IN RETROSPECT

- Last year *Kinetic Auto Systems*, a special new strategic business unit (SBU) was created to tap business opportunity in manufacturing of auto-components for the Indian as well as global automotive industry. Kinetic Auto Systems will harness our inherent strengths in this area.
- Reliance Capital Limited acquired 14.81% equity stake in Kinetic Engineering. The investment will be utilised for building *Kinetic Auto Systems* for manufacturing of automotive components for Indian and global automotive companies.
- For our two wheeler manufacturing and marketing business, last year we adopted a new brand logo to create a new, more contemporary identity. The new logo now appears on all Kinetic two wheelers, dealership insignia, advertising and other brand related initiatives. A new website has also been designed and launched to reflect the new brand identity.
- Significant efforts have been made to strengthen our international presence and build Kinetic into a global brand including opening of new markets (such as South Africa, Egypt etc.), increasing sales in important existing countries such as Sri Lanka, Bangladesh and reviving earlier markets such as Argentina. Kinetic has participated in the *Milan Fair* as well as *Made in India* shows in Colombo and Johannesburg. Our motorcycle GF series is being homologated for exporting to Canada and several other destinations.
- We introduced a limited edition of the exciting 250cc high-performance and high technology stunner *Comet* which is India's most premium and aspirational motorcycle. *Comet* won the "Import Bike of the Year" award from renowned automobile specialist magazine Business Standard Motoring.

FRESH INFUSION OF FUNDS

With a view to create and build *Kinetic Auto Systems*, strategic investments were welcomed into Kinetic Engineering and the Company allotted following securities on 29th November, 2005 :

- i) To Reliance Capital Limited:
 - a. 7,15,000 Equity shares of Rs. 10 each at a price of Rs. 178 per share amounting to Rs. 12.73 Crores.
 - b. 1,50,00,000 redeemable preference shares of Rs. 10 each amounting to Rs. 15 Crores.
 - c. 6,00,000 convertible Warrants @ Rs. 178 with a right to subscribe to one Equity share of Rs. 10 each.
- ii) To Ambit Corporate Services Private Limited :
 - a. 50,500 Equity shares of Rs. 10 each at a price of Rs. 178 per share amounting to Rs. 90 lacs.
 - b. 1,00,000 convertible Warrants @ Rs. 178 with a right to subscribe to one Equity share of Rs. 10 each.

35th Annual Report 2004 - 2005

- iii) To Micro Age Instruments Private Limited - 9,00,000 convertible Warrants @ Rs. 178 with a right to subscribe to one Equity share of Rs. 10 each.

The above preferential allotment of equity / preference shares and warrants has resulted into higher inflow of funds with a minimal increase to the capital base due to larger portion of the funds coming in by way of share premium.

RESEARCH & DEVELOPMENT AND TECHNOLOGY ABSORPTION

Our research and development team has been working on a new motorcycle scheduled to be launched in the first quarter of calendar year 2006. The new motorcycle is likely to be named *Stryker*. The *Stryker* will feature a 100cc 4 stroke engine and will combine high fuel efficiency with a comfortable ride, attractive styling and useful features.

Research and development is viewed as crucial for development of the Company. These activities aid us in expanding and upgrading our product portfolio and improving our offerings to our customers.

Total investment in Research & Development (R&D) during the period under review was Rs. 292 lakhs which represents 1.47 % of the Company's turnover.

This year, we launched the 250cc High Performance bike COMET 250 in collaboration with Hyosung Motors of South Korea. This bike was customised for Indian market by our R&D team. The bike was launched in a "Limited Edition" format and created a lot of excitement in the market.

Some of the measures for conservation of energy undertaken during the period under review were :

- Reduction in Contract Demand from 3000 KVA to 2500 KVA and control of maximum demand below 1500 KVA thus saving electricity bill.
- Maintained Unity Power Factor throughout the year and got incentives in electricity bill.
- Installed Electronic Ballast for lighting in Paint Shop & Engine Assembly.
- Installed 5 hp motor in place of 7.5 hp in Paint Shop Oven Blower.
- Replaced hose pipe by PU tubing in Gear Box assembly to reduce air leakages (20 Nos Connections).
- Installed 125W Mercury Vapour lamps instead of 250W in Gear Line of Machine Shop.
- Effective measures were taken for reduction in transformer losses throughout the year.

The above measures have resulted in substantial savings in energy cost.

Our future energy conservation plans are as follows:

- Use of Flx - max (dipole magnets) on fuel line for LPG on SQF furnace.
- Use of Flx - max (dipole magnets) on fuel line for LDO on thermopac /burner.
- To maintain Unity Power Factor throughout the year and get incentives in MSEB bill.
- Installation of 125 W Mercury Vapour Lamps instead of 250 W in Shaft & Welding Line & Crank Shaft Line of Machine Shop.
- Development of awareness among the staff & workers for energy conservation.

FOREIGN EXCHANGE EARNINGS AND OUTGO

The information on foreign exchange earnings and outgo is contained in Schedule-15 Notes to the Accounts (Point Nos. 12,13 and 14)

LABOUR SITUATION

Relations between labour and management are cordial at all manufacturing plants of the Company.

DIRECTORS' RESPONSIBILITY STATEMENT

Pursuant to Section 217(2AA) of the Companies Act, 1956, your Directors confirm that:

- in preparation of the accounts for the period under review, your Company has followed the applicable accounting standards;
- appropriate accounting policies have been selected and applied consistently and efforts have been made to present reasonable and prudent judgements and estimates in order to present a true and fair view of the state of affairs of the Company as on 30th September, 2005;
- proper and sufficient care has been taken for the maintenance of adequate accounting records in accordance with the provisions of the Companies Act, 1956 for safeguarding the assets of the Company and for preventing and detecting fraud and other irregularities;
- the annual accounts for the period under review have been prepared on a 'going concern' basis.

KINETIC ENGINEERING LIMITED

MANAGEMENT DISCUSSION & ANALYSIS REPORT

Management Discussion & Analysis Report, pursuant to Clause 49 of the Listing Agreement, forms part of this report and the same is annexed as Annexure-1.

REPORT ON CORPORATE GOVERNANCE

A separate report on Corporate Governance is annexed as Annexure-2.

SUBSIDIARY COMPANY AND CONSOLIDATED ACCOUNTS

Report and accounts of the subsidiary company 'Kinetic Motor Company Limited' is annexed to this report along with the statement under Section 212 of the Companies Act, 1956. However, taking into consideration the mandatory requirement under Clause 32 of the Listing Agreement to present consolidated accounts which provide members with consolidated position of the Company including its subsidiaries, members are provided with the report and accounts of the Company treating these as abridged accounts as contemplated by Section 219 of the Companies Act, 1956. Members desirous of receiving the audited annual accounts of Kinetic Motor Company Limited may write to the Company at its Registered Office for a copy of the same.

FIXED DEPOSITS

61 deposits amounting to Rs.8.90 lakhs were matured and unclaimed as on 30th September, 2005, out of which 11 deposits amounting to Rs.1.74 lakhs have since been claimed and refunded.

COST AUDITORS

The Board of Directors appointed Dhananjay V. Joshi & Company as Cost Auditors of the Company under Section 233B of the Companies Act, 1956 for the year 2005-06. Approval of the Central Government has been received.

DIRECTORS

- Mr. S.C. Bhawe was appointed as Nominee Director of State Bank of India w.e.f. 31st January, 2005. Mr. S. C. Bhawe holds office of Director upto the date of the ensuing Annual General Meeting. The Company has received notice from a member under Section 257 of the Companies Act, 1956 proposing his candidature for the office of director. Appropriate resolution in this regard is appearing in the Notice of ensuing Annual General Meeting.
- Mr. P. P. Chhabria ceased to be Director of the Company with effect from 15th March, 2005. The Board of Directors place on record the contribution made by Mr. P. P. Chhabria.
- Dr. K. H. Sancheti and Mr. S. R. Kotecha, Directors of the Company retire by rotation and being eligible, offer themselves for re-appointment.

AUDITORS

Your auditors M/s. P. G. Bhagwat, Chartered Accountants, retire at the forthcoming Annual General Meeting and, being eligible, have given their consent for re-appointment.

PARTICULARS OF EMPLOYEES

Particulars of Employees as required under Section 217 (2A) of the Companies Act, 1956 read with Companies (Particulars of Employees) Rules, 1975 form part of this report. However, as per the provisions of Section 219(1)(b)(iv) of the Companies Act, 1956, the report and the accounts are being sent to the shareholders of the Company, excluding the statement of particulars of employees under Section 217(2A) of the Companies Act. Any shareholder interested in obtaining a copy of the said statement may write to the Company at the Registered Office of the Company.

ACKNOWLEDGEMENT

Your directors express their sincere thanks to financial institutions, banks, dealers, suppliers and stakeholders for the support extended to the Company and also wish to place on record their appreciation of the dedicated services rendered by the employees of the Company.

For and on behalf of the Board of Directors



A. H. FIRODIA
Chairman

Pune
30th December, 2005

Management Discussion & Analysis Report**Industry structure and development, sectoral and product-wise performance****Two-wheelers**

- Two-wheelers continue to be popular mode of transport in India due to affordability, high fuel efficiency and convenience, accounting for 80% of all vehicle sales in the country, with an estimated market size of 6.6 million two wheelers annually
- The two-wheeler market has grown at a compounded annual rate of 12% for last five years
- Motorcycles account for 80% of the two-wheeler industry off take, with scooters and mopeds accounting for 15% and 5% market share respectively. In 2004-05, motorcycles, scooters and mopeds recorded growths of 20.2%, 4.7% and 5.5% respectively
- The motorcycles market can be further segmented as:
 - Entry level – These are basic, no frills motorcycles (typically with 100cc, 4 stroke engines) at lowest price, accounting for 35% of the motorcycles segment
 - Deluxe or executive – These are motorcycles with 100-125cc, 4 stroke engines, good styling and user-friendly features priced a little higher than entry-level motorcycles, accounting for 54% of the motorcycles market
 - Premium – these are motorcycles with 150cc (or higher) engines for improved performance, styling and features, priced at a premium to the entry level or executive motorcycles. They represent 10% of total motorcycles off take respectively

Auto components

The global economy leading to free flow of goods and the resultant demanding customer looking for high quality at the lowest costs forcing even the largest companies to look at delivering higher value through cost reduction. India offers both, high quality and low cost and is a natural choice for outsourcing various products and services and will increasingly become more and more dominant.

Manufacturing in India is a well-established industry over last several decades. The local vehicle industry is growing and the local auto component companies are well organised to cater to the needs of the domestic industry. India boasts of a huge pool of trained engineers.

Given this strength and India's long experience in manufacturing, we have now developed a great pool of supervisory strength in engineering companies. Government policies over the years have resulted in foreign companies entering India through JVs and Indian companies have internalised the technologies that they learnt from their JV partners. All in all, India has strong engineering strength and depth. As a result, in many industries, including automotive, India can create world class manufacturing products.

Global companies, with their own pressures on sales and margins, are keen to take advantage of disintegration of global barriers and outsource from low cost countries. Indian industry is well positioned to take on this opportunity or challenge and deliver to the quality, cost and volume needs of the global majors.

Company's performance**Two-wheelers**

During the 18 months period ended 30th September, 2005 ('period under review'), the Company produced 60761 nos. two-wheelers as against 87060 nos. in the previous year ended 31st March, 2004 ('previous year'). During the period under review, Company sold 77509 nos. as against sale of 86788 nos. in the previous year.

The Company is a new entrant into the highly competitive motorcycle segment. In face of intense competition from well-established players, the Company has not yet been able to garner large sales volumes of its newly launched motorcycles. Lower sales coupled with higher expenses in marketing of new models and increased cost of inputs such as raw materials have led to continuation of losses for the Company. In order to maintain competitiveness, the Company had to absorb increases in cost of inputs. These factors have resulted into net loss of Rs. 55 Crores for the period under review.

The Company has decided to adopt a new strategy for motorcycles which would focus on lowered advertising spends, increased rural penetration and newer products. The Company will also continue to grow exports of motorcycles and mopeds, building on the good response received from overseas markets.

Auto components

Kinetic Engineering already has expertise, skilled manpower and well equipped facilities for manufacturing of auto-components. A new strategic business unit *Kinetic Auto Systems* has been created with a view to leverage inhouse strengths and capitalise on the good growth opportunities in this area. During the period under review, the Company sourced and accepted orders for manufacturing of auto components from domestic companies as well as from abroad, including well-known Fortune 500 companies.

The Company's revenue from auto-component business during the period under review was Rs. 33 Crores. Based on inherent strengths and good response in this business unit, the Company expects to clock excellent growth in this business in the coming years.

KINETIC ENGINEERING LIMITED

Opportunities, Threats, Risks and Concerns

Motorcycle industry in India is very competitive and dominated by well-established players. Increasing market penetration in this segment requires higher amount of sustainability, financial support and consolidation of resources. Though the motorcycle market is expected to grow at compounded annual growth rate of 12% upto 2009, the competition is also intensifying leading to difficulties for small players to grow. Mopeds segment appears to have stabilised at current levels and retains a value proposition as a low-cost basic transport product with load carrying utility; but may not clock high growth or contribute large volumes.

Auto-component is a promising opportunity for the Company as we can harness existing infrastructure and resources effectively. India's auto-component manufacturing industry enjoys significant global labour advantages on account of availability of a vast pool of skilled labour and qualified engineers with knowledge of English language at comparatively lower cost. Internationally renowned consultants such as McKinsey & Company estimate that India's exports of auto components can grow to \$20 billion.

Your Company has appointed a firm of international repute to advise on auto-component business. Your Company already has rich experience in auto-component business from the stage of designing to manufacturing and the in-house facilities and skilled manpower. In view of these inherent strengths, auto-component manufacturing business would help the Company to turn around and become a profitable business.

Business outlook and overview

Two-wheelers

Your Company has recently added motorcycles to its business portfolio and invested substantial resources for establishing manufacturing facilities, developing and marketing new motorcycles over the last few years. However, it has not been able to generate significant sales volumes in the highly competitive market and the Company has reported net loss for last three years. As stated earlier, the Company has decided to adopt a new strategy for motorcycles which would focus on lowered advertising spends, increased rural penetration and newer products. The Company will also continue to grow exports of motorcycles and mopeds, building on the good response received from overseas markets.

Auto components

Historically, Kinetic has been highly vertically integrated as one of the pioneers in India's automotive segment and early entrants at a time when the components industry was not very well developed. As a result, the group always had a large strength in manufacture of components, especially engines, engine parts like gears, variators etc. in addition to design and manufacture of complete vehicles. There is also large design strength and a well-equipped tool-engineering centre.

Kinetic Auto Systems will specifically produce engines and engine parts for global organisations. Kinetic has unique strengths in this area, including depth of engineering, excellent facilities and ability to become a provider of high end products like entire engines or important engine parts.

In fact, we estimate that it will also provide stability and high profitability strength to the group in light of the intense and cut-throat competition expected in the vehicles industry.

These efforts would help bring about improvement in topline and financial position in the years to come.

Quality

Your Company has already built up a quality system in tune with the requirements of ISO 9001. We strive for total customer satisfaction through relationship building and providing superior after sales service. Your Company has a well-established system of fixing problems at sight, on the spot analysis and prevention of recurrence of the problem in the future.

Internal Control System

The Company has adequate internal control system commensurate with its size and nature of business for ensuring efficiency of operations and protection of Company's assets. The Company's Audit Committee periodically reviews compliance with Company's policies, procedures and laws.

Financial performance with reference to Operational performance

Gross Sales and other income in the period under review were Rs. 243 Crores as against Rs. 240 Crores in the previous year. Net Loss for the period under review is Rs. 55 Crores as against Rs. 52 Crores in the previous year. Debtors were reduced from Rs. 84 Crores on 31/3/2004 to Rs. 56 Crores on 30/9/2005.

Human Resource Development

The Company continues to invest in development of human resources. Annually, training requirements are identified, mapped and correspondingly, training sessions are organised with a view to promote continuous learning. Special attention is provided to good health and safety of employees. Through a systematic annual performance appraisal and review system, roll and competency mapping and performance linked career planning, Kinetic's HR team organises on job enrichment, job rotation, transfer, re-deployment, training, promotion and compensation revision. There were 1675 number of employees on roll of the Company as on 30th September, 2005.

Cautionary Statement

The report contains estimates and expectations, which could be 'forward looking'. Actual results, however, might differ from expectations, as the same depend upon many uncertainties.