



Sterite Optical
Technologies Ltd

The backbone of broadband

Global Connectivity



to the Last Mile

Annual
Report **2004-05**

Board of Directors

Navin Agarwal
Arun Tadarwal
Haigreve Khaitan
Pravin Agarwal
Dr. Anand Agarwal
(CEO & Executive Director)

Company Secretary

Sandeep Deshmukh

Chief Financial Officer

S L Bajaj

Auditors

Deloitte Haskins & Sells
Chartered Accountants

Bankers

ABN AMRO Bank N.Y.
HDFC Bank Limited
ICICI Bank Limited
Punjab National Bank
State Bank of India

Registered Office

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Aurangabad - 431 136
Maharashtra, India

Registrar and Transfer Agents

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(Unit: Sterlite Optical Technologies Ltd.)
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contents

Message from the CEO	03
Management Discussion & Analysis Report	04
Directors' Report	09
Corporate Governance Report	13
Auditor's Report	21
Balance Sheet	24
Profit & Loss Account	25
Cash Flow Statement	26
Schedules to Accounts	27
Balance Sheet Abstract	41
Statement of Subsidiaries	42
Consolidated Accounts	43
Notice of Annual General Meeting	59

Board of Directors & Management Committee

Mr. Navin Agarwal - Non-Executive Director

Mr. Navin Agarwal has been overseeing the Sterlite Group's operations in India for many years. He has over 19 years of experience of general management and commercial matters, having been involved in Sterlite since its inception.



Mr. Arun Tadarwal - Non-Executive & Independent Director

Mr. Arun Tadarwal, Partner of Tadarwal & Tadarwal, a firm of Chartered Accountants based in Mumbai, holds a Bachelors Degree in Commerce and is a member of The Institute of Chartered Accountants of India. Mr. Tadarwal has rich and varied experience spanning over two decades in Finance and Audit.



Mr. Haigreve Khaitan - Non-Executive & Independent Director

Mr. Haigreve Khaitan, Partner of Khaitan & Co, a firm of Lawyers based in Mumbai, holds a Bachelors Degree in Legislative Laws. Mr. Khaitan has varied experience spanning over eight years in Commercial and Corporate laws, Tax laws, Mergers and Acquisitions, Restructuring, Foreign Collaboration, Licensing etc. He is also a member of the Board of various reputed companies.



Mr. Pravin Agarwal - Non-Executive Director

Mr. Pravin Agarwal holds a Bachelors Degree in Commerce. Mr. Pravin Agarwal has rich experience in the Industry spanning over twenty-five years. Mr. Agarwal is a Whole time Director of The Madras Aluminium Company Limited. Mr. Pravin Agarwal has been overseeing the Sterlite Group's operations in India for many years and he is actively involved in the operations of Sterlite's Transmission Business Division.



Dr. Anand Agarwal - CEO & Executive Director

Dr. Anand Agarwal is responsible for Sterlite's range of Telecom Products; which include Optical Fiber, Fiber Optic Cables and Copper Telecommunication Cables. Previously, Dr. Anand Agarwal was the Chief Operating Officer, responsible for Sterlite's Optical Fiber Business Division. Dr. Anand Agarwal joined Sterlite in 1995 and has held various positions including manufacturing, quality assurance and business development. Prior to joining the Sterlite Group, Dr. Anand Agarwal worked with Siemens. Dr. Anand Agarwal holds a Bachelor of Technology degree in Metallurgical Engineering from the Indian Institute of Technology (IIT Kanpur); and his Master's degree and PhD in Materials Engineering from the Rensselaer Polytechnic Institute, USA.



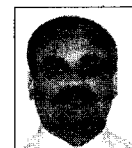
Mr. S L Bajaj - Chief Financial Officer

Mr. S L Bajaj is responsible for Finance and Accounts for the Company. Previously, Mr. S L Bajaj was the Senior General Manager at Sterlite Industries (India) Limited and was responsible for MIS and Accounts. Mr. S L Bajaj joined the Sterlite Group in 1995 and his key focus areas have been MIS and Finance. Mr. S L Bajaj holds a Chartered Accountant degree from the Institute of Chartered Accountants of India.



Mr. Pankaj Khanna - Chief Operating Officer

Mr. Pankaj Khanna is responsible for Sterlite's range of Optical Fiber Products. Previously, Mr. Pankaj Khanna was the General Manager Projects, responsible for new projects at Sterlite's Optical Fiber Business Division. Mr. Pankaj Khanna joined Sterlite in 2000 and his key focus area has been process development. Mr. Pankaj Khanna holds a Bachelor of Technology degree in Mechanical Engineering from the Indian Institute of Technology (IIT-Kanpur).



Mr. KS Rao - Marketing Director

Mr. K S Rao is responsible for sales of Sterlite's range of Fiber Optic Products, Copper Telecom Cables and Access Solutions. Mr. KS Rao is also responsible for development of new business opportunities. Previously, KS Rao was the Chief Operating Officer, responsible for Sterlite's Fiber Optic Cables and Copper Telecom Cables Business Divisions. Mr. KS Rao joined Sterlite in 1993 and his key focus area has been manufacturing and product development. Mr. KS Rao holds a Bachelor of Technology degree in Mechanical Engineering.



Global Connectivity to the Last Mile

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Sterlite's 7 million km of Optical Fiber is carrying voice, data and pictures. Enabling people to communicate better, reach out farther.

Sterlite's advanced technology, which helps carry and deliver more data at the speed of light, is the key component in the broadband and convergence revolution that is sweeping across the globe. Manufactured at fully integrated and technologically advanced facilities, our products exceed the standards set by various international telecommunication bodies.

The next time you speak on the phone, watch TV or surf the internet, think of the invisible backbone that enables you to enjoy life to the fullest.

Think of Sterlite Optical Technologies ...
The backbone of broadband™



Message from the CEO

We are glad to present the Annual Report for the Year 2004-05.

This year has seen us restore our financial health as a result of good demand for Sterlite Fiber Optic Products worldwide. Compared with the previous year, income from operations increased to Rs. 3,758.55 Million in 2004-05, with net profits of Rs. 102.20 Million as compared to a net loss of Rs. 189.53 Million in the last fiscal.

Our strategy of evolving cost structures has enabled us to become one of the lowest cost producers of Optical Fiber worldwide. The demand generation for our products in high-growth markets globally and the consolidation of our market share in India, has borne significant results.

Today, we have a footprint in International markets like China, the African Continent, Middle East and Europe. We exported to over twenty countries in 2004-05. We expect the seeds sown in international markets over the past two years, to reap results in the forthcoming years.

In this year, our Copper Telecom Cables business has also stabilized and going forward, we expect a steady revenue generation from this division from international markets as well.

Based on customer inputs, we strive to develop products & integrated solutions to meet telecommunication and broadband network requirements. During the year we have launched two new Optical Fiber Products: *OH-Lite™* and *Giga-Lite™* and we have commenced manufacture of *SuperLAN™* Cables. Sterlite now has products that range from long-haul fibers, to access multi-mode fibers to desk structured cables.

With bandwidth hungry applications continuously being developed and adopted across the world, Optical Fiber is the medium of choice for development of Broadband Networks. With its comprehensive product solutions developed for address long-haul, access and premise networks, Sterlite is a 'one-stop-shop' for our customers across the globe, forming the backbone of broadband.

During the year, our technology development team has filed ten patent applications for innovations in our products and processes. A product patent for Sterlite's dispersion shifted fiber with low dispersion slope, *DOF-Lite™ RS*, was granted in the United States.

This year's financial results have put us back in the black. We intend to sustain this momentum and are using innovative partnerships to increase our global presence. All in all, this was a good year, where in we achieved success through our strategy decided on three years ago.

The Management Committee and I remain as confident as ever that we would continue along our path towards long-term growth; based on the strength of our culture of continuous improvement in all our business processes, the strength of our leadership team and the strength of our core value system.

I take this opportunity to thank you, our shareholders, for your encouragement and support and we look forward to continuing our service to you.

Here's looking forward to exciting & promising times ahead !!

Sincerely

Dr. Anand Agarwal
CEO & Executive Director

Management Discussion & Analysis Report

INDUSTRY STRUCTURE AND DEVELOPMENTS

Indian Economy

The Indian economy has performed well during 2004-05. Buoyed by impressive performance of industry and service sector, GDP growth in 2004-05 was about 6.9%. In FY 2005-06 GDP is estimated to grow by 7-8%.

Agriculture and allied sectors are expected to register modest growth of 1.1% in 2004-05, however there is positive trend for industrial growth due to improved capital utilization, better industrial climate and expanding domestic and external demand, which is expected to be around 9%. The service sector is also expected to register about 8.9% growth. It is encouraging to note that service sector now constitutes more than 51% of the GDP.

The outlook for Indian economy in current year appears upbeat. Removal of infrastructure bottlenecks, introducing of labor reforms, restructuring of taxation, improving efficiency of systems should help in achieving the 10% GDP growth in the coming years. In real long-term perspective, Indian economy is projected to be the third largest economy by 2035 with the share of 14% of global economy. The overall future is therefore promising.

Telecom and Telecom Cables Industry

It is believed that Broadband and wireless networks, as well as the likely convergence of various technologies and standards will drive the telecom market growth in India over the next few years.

Today, India offers exciting opportunities in telecom and has great appetite for broadband. Triple-Play will provide the impetus for broadband growth in the country. The total wireline and wireless subscriber base in India has zoomed from 4.8 Million subscribers in 1992 to almost 100 Million subscribers in 2005, with an expected further doubling of this figure in next three years. Broadband subscriber growth is likely to be at even faster rates as the market matures.

Convergence of various services on the same mode is the future. MTNL, primarily a wireline player in India is now aggressively pushing forward its broadband services that feature applications such as entertainment and data. Entertainment is likely to be the killer application in a market that boasts of higher cable television penetration than telephone or PC penetration.

The entry of BSNL and MTNL into the broadband arena will influence the entire industry and allow for a much larger playing field. The two companies combined plan to have at least a Million broadband subscribers by the end of the year and four Million by the end of 2006. Indian Government's policy of deregulation will support to build and optimally manage fast and efficient networks, which in turn help in expanding Telecom Cables production. The telecom-manufacturing sector in India is likely to ride this boom.

Further deregulation of the market, which is already one of the most competitive markets in the world, will allow for aggressive expansion of telecom service providers. Along with that, the adoption of Next Generation Network (NGN) will mean more opportunity as well as the capability for more applications. India is expected to have its first operational 3G network this year itself. With the emergence of India as a crucial emerging market, global telecom vendors are looking at India to launch their latest technologies and applications. It is predicted that India can become a global delivery center for telecom applications worldwide, and can leverage its strategic strength in technology to reach out a wider global audience in the telecom space.

With a vibrant wireless industry, the wireline sector will see rapid development as applications grow and the rates for applications like leased lines decrease. Lower costs will be directly proportional to higher broadband penetration in the country.

OPERATIONAL PERFORMANCE, SEGMENT-WISE PERFORMANCE AND FINANCIAL ANALYSIS

The year 2004-05 has been a fairly good year for the Company especially on the backdrop of losses suffered by the Company in the last two years, which was on account of sudden drop in volumes and realization in the telecom cables industry, globally. The Company's net income from operations aggregated Rs. 3,758.55 Million compared to Rs. 1,095.34 Million in the previous year. Profit before interest, depreciation, tax and provision for contingencies aggregated Rs. 473.40 Million compared to a loss of Rs. 65.90 Million in the previous year.

After providing Rs. 104.12 Million for interest, Rs. 266.76 Million for depreciation, and after tax credit (Net) Rs. 0.32 Million (deferred and current tax), the net profit after tax aggregated Rs. 102.20 Million as compared to net loss (before exceptional income and tax credit) of Rs. 449.97 Million in the previous year. The Company's net loss after exceptional income and tax credit in the previous year was Rs. 189.53 Million.

The Company has achieved a significant turnaround in this financial year. The improvement in the Company's performance has been supplemented with the recovery in demand by the industry, consolidation of the Company's market share in India, success in sales to Overseas Markets and significant cost reductions achieved by the Company.

A snapshot of salient features of Company's performance during the year :

- 60% increase in total sales volumes of uncabled Optical Fiber, compared with total sales volumes in FY 2003-04
- 51% increase in international sales compared with 2003-04
- Commencement of exports of Copper Telecom Cables to Africa and receipt of orders from SAARC countries
- Doubled our market share for Optical Fiber in China, over that in the previous year
- Approval for products in five overseas markets.

Segment-wise Performance

Optical Fiber Business

Your Company is the only integrated manufacturer of optical fiber in the country with a manufacturing capacity of 4 Million kilometer (km) and has a strong focus on improvement of productivity and reduction in cost. This has provided your Company with a competitive cost advantage compared to other players in the global market.

Production of optical fiber during the year was 1.86 Million kilometers compared to 1.07 Million kilometers in the previous year. Production of fiber optic cables aggregated 0.72 Million fiber kilometers (FKM) compared to 0.43 Million fiber kilometers (FKM) in the previous year. Your Company continues to be the largest manufacturer of optical Fiber products in India with the share for Fiber Optic Products in India of about 60%. Your Company has achieved a significant market share in China for its uncabled Optical Fiber.

Your Company was the exclusive supplier of 754km of Fiber Optic Cables for an ONGC Videsh Project being executed in Sudan and of Fiber Optic Cables for Government of Assam's e-Governance Project (Pilot Phase).

Copper Telecom Cables Business

Restart of the Copper Telecom Cable business has been another important feature of this year's performance. Total sales of Copper Telecom Cables in the year under review were Rs. 1,915.21 Million for supplies of 2.85 Million conductor kilometers (CKM) of Copper Telecom Cables. This was mainly to BSNL and MTNL. This sales revenue amounted to 51% of the total sales of the Company during FY 2004-05. Your Company's estimated market share for Copper Telecom Cables in India is 25%.

Financial Analysis

Capital Structure:

Total shareholder's fund as at March 31, 2005 aggregated Rs. 2,609.35 Million of which equity capital was Rs. 279.97 Million comprising 55,994,567 shares of Rs. 5 each.

Loan Profile:

The Company's long term debt decreased by Rs. 100.00 Million to Rs. 400.00 Million while working capital borrowings increased by Rs. 10.08 Million to Rs. 657.47 Million. The Company has repaid Rs. 100.00 Million of borrowing. The debt equity ratio of the Company as at March 31, 2005 was 0.56 compared to 0.67 in the previous year-end. The average cost of debt funds outstanding as at March 31, 2005 was about 7 %. The total capital employed by the Company decreased by Rs. 108.43 Million to Rs. 4,075.28 Million.

Gross Block and Investments: The Gross Block including capital work in progress increased by Rs. 27.33 Million to Rs. 5,683.73 Million mainly on account of addition of routine capital expenditure and disposal of NPAs.

Inventory and Debtors:

In rease in inventories as at March 31, 2005 by Rs. 83.02 Million was due to restart of the Copper Telecom Cables facility and a strong order book. Debtors have increased in absolute terms and represent 100 days of turnover compared to 54 days in the previous year. This is mainly due to supply of Copper Telecom Cables in February and March of 2005 to BSNL as per contract terms.

Loans and Advances:

Loans and Advances as at March 31, 2005 decreased by Rs. 254.84 Million mainly on account of adjustment of taxation advance on completion of assessment and refund of Income Tax during the year.

Cash Flow:

The cash flow summary for the year is as follows:

Net Cash provided/(used) for: Rs. Million

- Operating activities 588.17
- Investing activities (148.91)
- Financing activities (314.84)

The cash inflow from operating activities was primarily used for repayment of borrowings and loan to subsidiary company.

FUTURE OUTLOOK

India is experiencing unprecedented growth in telecommunications. This growth is estimated to lead to an expenditure of over US\$ 50 billion over the next six years ending 2010. The subscriber base for telephony services continued to maintain its general growth. At the end of March 2005, total fixed lines were 43.18 Million and mobiles were 36.3 Million, taking the telephony subscriber base of the country to 79.5 Million. This is projected to increase to 175 Million by 2010. The tele-density is expected to grow from 7.02 in 2004 up to 15 by 2010. The Telecom Regulatory Authority of India (TRAI), has projected that Internet subscriptions will increase from 4.1 Million in 2003 to 6 Million in 2005, to 18 Million by 2007 and to 40 Million by 2010.

Broadband subscriptions will rise from 0.2 Million in 2003 to 3 Million in 2005, to 9 Million in 2007 and to 20 Million by 2010. Broadband will be a preferred carrier with the Central Government for e-governance in India, favoring the rising use of online education, tele-medicine networks and connectivity for rural knowledge centers. Greater use of online services in commerce, industry and transportation will create a boom for broadband. The regulator has suggested a range of measures for an open-sky policy for DTH, VSAT and up linking using satellites that should boost broadband.

All these figures indicate growth potential to your Company as a leading supplier of Optical Fiber and Cables.

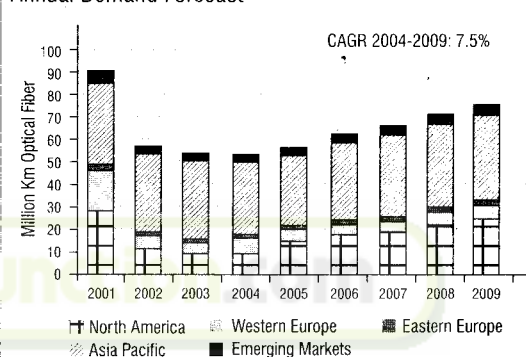
As per CRU International - a UK based research agency, 2004 was the year of growth in demand for the Optical Fiber Industry. The global demand for Optical Fiber Products increased to 60.8 Million-km in 2004; a 3% increase over that in 2003. CRU has also tracked the global price trends for Optical Fibers and these prices have attained stability over the last six business quarters.

There has been the recent spate of activity in the US, conditions within Europe are improving and emerging markets are seeing much stronger demand than previously estimated. This increase in demand has been attributed to rapidly growing industry segments such as Broadband, Voice over Internet Protocol (VoIP), Streaming Media, technological innovations in fiber optics and Dense Wavelength Division Multiplexing (DWDM).

Broadband access technologies are now being deployed, as Fiber-to-the-Premise (FTTP) is gaining acceptability among broadband subscribers. Juniper Research has predicted that the global broadband subscriber base is forecast to grow from over 0.12 billion in 2004 to over 0.32 billion in 2009. Thus there would be sustenance in demand going forward from 2005. With the deployment of FTTP/ FTTH gaining popularity across the world, and proof of its economic viability, FTTH is as the next growth driver for the industry.

In its market report released in March 2005, KMI Corp., a leading international telecom research agency, corroborates that 2004 was the year of changing fortunes for the convergence industry. KMI predicts that worldwide demand would grow at a CAGR of 7.5% from 2004 to 2009, which reflects the level of sustainable growth enjoyed by the telecom segment prior to the technology bubble of the late 1990s.

Annual Demand Forecast



Source: KMI's 2005 Worldwide Optical Fiber and Cable Markets

The Indian Fiber Optic Industry: 2004 and beyond

Initial estimates for the fiber-optic industry in India in FY 2004-05, based on market information and published sources, also indicate that 2004-05 was the year of turnaround and growth in the Indian Fiber Optic Industry. After an abnormally depressed demand in 2003-04, there has been a recovery and increase in demand in 2004-05 to about 2 Million-km of cabled fiber. This represents a CAGR of about 7% from 2003 through 2005.

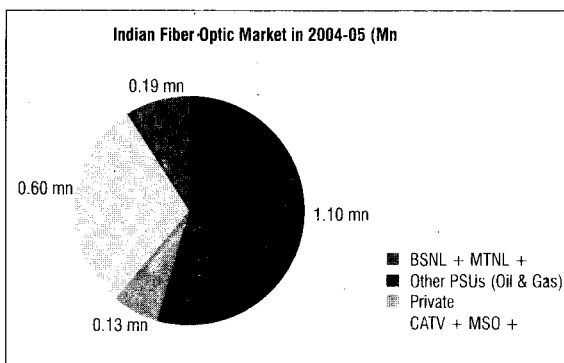
The Government incumbents like BSNL, MTNL and RailTel continued to be the largest buyers of fiber optic cables, closely followed by the Indian Private Telecom Incumbents.

The Indian Government as a buyer of Fiber Optic Cables through the Telecom Incumbents & Public Sector Undertakings such as the Oil and Gas Sector, Power Sector, etc. cumulatively constituted about 60% of the total purchases of Fiber Optic Cables in India in FY 2004-05.

With the formulation of the Broadband Policy in October 2004 and the subsequent race to build networks that are capable of meeting the broadband subscriber targets laid down by the IT & Telecommunications Ministry, 2004-05 showed a healthy demand growth. There is also an increasing adoption of fiber-based networks by the Cable TV Segment, Multi-Service Operators (MSOs) and e-Governance State Initiatives.

Indicating the future trends in the telecom industry, in its quarterly report published in February 2005, Cris-Infac believes that over the medium term, demand for fiber optic cables is expected to grow at a CAGR of 17%. These higher off-takes of fiber optic cables will be dependent on the success of broadband services in several pilot cities, which have been initiated in the past few months.

A study carried out on the future of Copper Telecom Cables in India, by the Economic Times stated that the copper lines laid by telecom companies which were considered obsolete, redundant and expensive in the wireless world, have got a fresh lease of life with the launch of broadband services in the country.



Source: Industry Estimates

Telcom companies are expecting broadband services to spark off a fresh interest in landline phones. This is likely to increase the demand for Copper Telecom Cables.

The purchase plans announced by the major buyers of Copper Telecom Cable in India, indicate a minimum requirement of about 120 Lckm in 2005-06.

Sterlite's Sales Approach for 2005-06

Over the past 2 years, Sterlite has consciously realigned its sales efforts to focus on judicious mix of products, mix of sustained growth markets and future potential markets.

In India, Sterlite will continue to serve the traditional buyers of Fiber Optic Cables and Copper Telecom Cables such as BSNL, MTNL, Railways, Oil & Gas Sector and the Private Telecom Players like Reliance, Tata and Bharti. There has also been a concerted focus on development of supplementary markets for Sterlite's range of products. In FY 2004-05, Sterlite's export sales amounted to approximately Rs. 342.71 Million as against Rs. 277.41 of the last year of Fiber Optic Products.

However, with enhanced overseas regional focus, Sterlite's sales to various global markets has been targeted substantially higher in FY 2005-06. This confidence has been enhanced with the success in receiving initial trial orders, followed by repeat orders from several prestigious global manufacturers of Optical Fiber Cables. Additionally, activities have been initiated to address the demand for Optical Fiber, Fiber Optic Cables and Copper Telecom Cables to future potential growth markets in Africa and Eastern & Central Europe.

Over the past 2 years, there has been consolidation and rationalization of supply capacity for manufacture of Optical Fiber and Fiber Optic Cables by global majors. However, a large number of their plants that are still in operation are located in regions that have traditionally higher overheads than encountered in plants located in India and other South East Asian countries. In addition, 2004-05 has seen the certain mergers of leading players. 2005-06 should see further consolidation of the industry and normalization of capacity utilization. Sterlite has an inherent strength in constantly challenging theoretical limits in baseline manufacturing costs, making it today, one of the most cost effective Optical Fiber and Fiber Optic Cable manufacturers in the world, giving the competitive edge to effectively address sales to our chosen focus markets.

RISKS AND CONCERNS

Business Risks

Lower volumes and prices in the domestic and global markets will have an impact on the Company's revenues and profits. However, the management is cautiously optimistic about the likely recovery in the global telecommunication space with the easing of supply side pressures, increased focus on sales into various overseas markets and demand recovery in domestic market. The Company's focus on cost reduction, which has yielded positive results, will be the critical factor in mitigating margin pressures. Further, new product launches and long-term relationships with domestic telecom companies will aid in stabilizing cash flows.

Technology Risk

Product obsolescence risks are inherent in the optical fiber business. The management has accorded high priority to in-house Research and Development in order to ensure continuous product development and quality improvements of existing product offerings.

During the FY 2004-05, the company launched three new products especially designed for Access and Premise Networks.

- (a) OH-Lite™ Low-water-peak Single Mode Optical Fiber
- (b) Giga-Lite™ Multi Mode Optical Fiber for Gigabit Ethernet Applications
- (c) SuperLAN™ Cat 5e and Cat 6 Cables

During the FY 2004-05, our Research and Development team had filed applications for ten patents for products and processes. Of the four patents that had been filed in the FY 2003-04, a patent for dispersion shifted fiber with low dispersion slope, was granted in the US. Of the balance 13 filed patents, at least four patent grants are expected during FY 2005-06. Once granted, these patents would be valid for tenure of twenty years.

Additionally, the Research and Development team is at an advanced stage in the preparation of several process and product patent applications, and expect to file at least fifteen patents during FY 2005-06.

Financial Risks

Financial risk primarily pertains to foreign currency exposure risk. The Company has a well-defined system of hedging its foreign currency exposures, both in the capital and revenue account, after expending natural hedges from exports.



INTERNAL CONTROL SYSTEMS AND THEIR ADEQUACY

Enterprise Resource Planning (ERP) was implemented in the Company in the year 2000. At various stages of implementation and thereafter, steps have been taken to ensure that appropriate controls are embedded in the software and the internal audit function reviews these controls periodically. In addition, the adequacy of controls in the ERP system is reviewed periodically.

The Company has appointed independent audit firm, with the expertise and specialized staff to carry on the internal audit of the Company's operations. They carry on internal audit at unit level. The reports on audit findings and action taken are tabled at each Audit Committee meeting. The actions are taken on the basis of recommendations of the Audit Committee. The Company has well designed procedures, manuals and policies to execute financial transactions.

HUMAN RESOURCES

Creativity and dedication of all our employees represent the most precious assets of the Company. For the growth of the organization, the human resource function has an important role to play not only in identifying and recruiting suitable individuals but also developing and rewarding its employees. The Company has remained focused on strengthening human capital through continuous training and development and by upgrading skills of employees to meet the Company's objectives. This will enable the Company to have a common goal and vision and produce the team and leaders who drive the Company to the next level. The Company had employed 352 persons as on March 31, 2005.

CAUTIONARY STATEMENT

Statements in the Management Discussion and Analysis describing the Company's objectives, projections, estimates, and expectations may be "forward looking statements" within the meaning of applicable securities laws and regulations. Actual results could differ materially from those expressed or implied. Important factors that could make a difference to the Company's operations include economic conditions affecting demand/supply and price conditions in the domestic and overseas markets in which the Company operates, changes in the Government regulations, tax laws, certain presumptions on which estimates are based and other incidental factors.

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