Response to SES on Proxy Advisory Report published on 23rd Nov, 2018 over Approval of Scheme of Arrangement amongst The Tata Power Company Limited and Tata Advanced Systems Limited and their respective shareholders and creditors

No	SES Observation	Response
1	Page 2 - "According to SES, the consideration paid to the Company pursuant to the scheme is significantly lower than the value of Assets transferred. Since, the asset is transferred to the Promoter of the Company, therefore, SES reckons that such a proposal is not in the interest of the public shareholders of the Company"	1. The valuation of the business, in accordance with the independent valuation reports, is ascertained at ₹ 2,230 Crore (Enterprise Value including earn-outs), whereas the comparable book value (capital employed) of the Division was ₹ 1,710.8 Crore (Net worth + Debt). Hence the sale value of business is not lower than the asset value. 2. Further the valuation is based on discounted cash flow methodology, which includes all expected future profits from respective projects. The valuation has been done by two independent agencies and their valuation reports are publicly available as part of the Scheme. The Company has also taken fairness opinion from a Category-I Merchant Banker. 3. The final valuation & earn-out structure, while agreeing with the Transferee Company, also factors in the underlying nature of defence related businesses which is of very long gestation coupled with high levels of uncertainty in realizing revenues and profits in defined timelines, with stretched working capital cycles.
2	Page 9 - "Page No. 20 of the Scheme states that the Net Asset Value of all the Assets (after deducting Long term borrowing of ₹ 544 Crores) as on the Reference Date stands at ₹ 1,317 Crores"	The net asset value (or net worth) has been incorrectly mentioned at ₹ 1,317 Crore in the report as against **₹ 1,166.8 Crore**, as provided in Annexure A on Page 19 of the Shareholder Notice as on 31st Oct, 2017 (₹ 1,317 Crore, if depreciation is excluded).
3	Page 9 - "In case, none of the criteria for Earn-out Consideration is achieved, then, **the Company is receiving a consideration of ₹ 496 Crores against a Net Asset of ₹ 1,317 Crores** incurring a loss of ₹ 821 Crores based on Net Asset valuation. Therefore, the deal becomes questionable on such account."	1. Theoretically the worst-case scenario loss would be ₹ 671 Crore, not ₹821 Crore as the Net Worth has been incorrectly mentioned at ₹ 1,317 Cr instead of ₹ 1,167 Cr, as explain in Point 2 above. 2. It is pertinent to note that the above Net Assets/ Net Worth includes investments of approx. ₹ 700 Crore in intangible & tangible assets pertaining to future orders. Thus, if future orders do not materialize, the value of net worth/net assets would also reduce to that extent due to write off of assets, net of any realizable value. 3. Hence, the value of net asset is truly not comparable with consideration since valuation is based on profit estimates and capital investments that have already been made on the expectations of future orders. It may be noted that the due to continuing delay in obtaining orders the business is currently making losses which reflects the cyclical nature of the business.

4	Page 9 - "…consideration is being received is ₹ 496 Crore. This amounts to a book loss as on date of Rs. 821 Crore. If one takes into account future earnout, the receipts will be RS 1,190 Crore over a period of time. However, this Rs. 1,190 is uncertain"	1. As explained, the value of the business has been arrived on the basis of expected cash flows from the business including future orders rather than book value. 2. Given the nature of the defence business, it will be unreasonable to expect any buyer to pay full value today when the orders are not in hand or have low visibility Hence keeping the interest of Tata Power's shareholders in mind, the Management of the Company decided not to forego the value of potential future upside and have an incentive linked to future orders (for which significant investment have already been made), which is part of total consideration
5	Page 9 - OPPORTUNITY COST ANALYSIS: "…..one needs to calculate potential profits from future projects. To do we make following assumptions that the Transferee company will breakeven at 90% of the targeted revenue after paying Earn out amount…. ….Potential Profit Margins if orders received at 100% of target value ₹ 3,920 Crore"	The analysis is misconstrued on the assumption that break-even for the Buyer is achieved at 90% of the minimum order book threshold and Transferor has the profit of ₹ 3,920 Crore, because of the following reasons: - 1. This analysis assumes that the incremental 10% order book of ₹ 2,730 Crore translates into profit of ₹ 2,730 Crore i.e. assumption of 100% profit margin on incremental orders. This is grossly inaccurate as the incremental revenue will also have costs associated with it. 2. Execution of these projects are spread over FY20-FY35 and hence the present value of profits/cash flows from these projects will be significantly different, which is wrongly compared with one time earn-out consideration. In addition, future orders will require further capex and R&D investments, which has not been considered here. 3. The understanding between Transferor & Transferee was that the actual order value may be higher or lower than the ₹ 27,300 Crore (spread across 6 programs) for achieving earn out payments. Actual order value for individual programs may be +/-10% of the specified threshold and Buyer would be largely indifferent as typically some programs may underperform, and some programs may overperform and the overall order book value may still be around ₹ 27,300 Crore.
6	Page 10 - "…..comparative data in case demerger is done and not done situation"	As explained in Point 5 above, this analysis is based on theoretical assumptions and without considering time value of money. Many of these projects require large upfront investments to develop the appropriate technologies and prototypes, irrespective of whether orders are finally received or not. This has not been factored while making the conclusions.
7	Page 10 - "From the above it is crystal clear that in all the three situation Tata Power is better off without Demerger.	SES has not considered the ongoing losses being incurred by this division due to high fixed costs and delay in receiving the expected orders. There is significant value erosion in the business due to delay in orders. This business is non-core to the

	Therefore, unless there are reasons which can discount arguments against demerger, SES finds that at least on issue of rationale and fairness the scheme fails to convince SES. In view of the above, SES is of the opinion that the proposed scheme may not be in the interest of the public shareholders of the Company and is therefore is raising concern in this regard"	Company and it will require significant management bandwidth to revive the business and recover losses. Hence in the best interest of the shareholders, it was deliberated and approved by the Board to divest this business to a buyer, who can harness the existing capabilities & infrastructure. To be fair to all stakeholders, the Company is receiving the upfront value and earn-outs for existing capabilities and future orders respectively.
8	Additional point -	The report does not compare trading multiples of listed companies to evaluate the fairness. Similar listed defence companies in India are traded at EV/EBITDA multiple of 11x-12x (Source: Kotak Mahindra Bank). Whereas, valuation realized by the Company is at EV/EBITDA multiple of 27.5x on full value and 12.9x on Upfront Amount (excluding earn-outs), which is significantly higher than the comparative multiples