



"Prime Focus Earnings Conference Call"

August 18, 2011





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- Moderator:** Ladies and gentlemen, good day and welcome to the Prime Focus Q1 FY'12 Earnings Conference Call hosted by Centrum Broking. As a reminder, for the duration of this conference, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, please signal an operator by pressing "*" and then "0" on your touchtone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Ankit Kedia from Centrum Broking. Thank you and over to you Sir.
- Ankit Kedia:** Thank you Melissa. Good morning everyone. We at Centrum Broking are glad to organize the Prime Focus Q1 FY'12 conference call. Today, we have Mr. Namit Malhotra, Managing Director and Mr. Nishant Fadia, CFO of Prime Focus. Over to you Nishant for some opening remarks.
- Nishant Fadia:** I will quickly in two minutes take you through the results and then go over to Namit. We have seen good growth this year on the back of the 2D to 3D business and we have delivered three big movies for the Hollywood Summer, with Green Lantern, Transformers and Harry Potter and going ahead also over the next few quarters there is a robust order book in place so 2D to 3D business looks completely on-track for robust growth.
- Namit Malhotra:** Last year when we started building this entire pipeline of work and business we have seen continuing growth and very good positioning for the company in terms of our ability to not just get some contracts that are part of movies, but actually we are starting to get more and more visibility in getting big chunks that impact the entire movies themselves and that is clearly helping position Prime Focus as a much stronger brand from back specific business perspective. We are also seeing fairly interestingly growth curve coming along with the breakthrough we made with News Corporation and Star TV in India, where we have again taken on the position of completely digitizing the entire network operations as a broadcaster like that, which is again a fairly huge opportunity for the company to transition itself amongst its core services to the next level of technology lead service which is very unique and very clearly presenting the future of the company. Because of the way the brand has evolved in the international markets there is a huge focus now that is going to building the visual effects order book because we find that last year the entire capacity and the infrastructure was built in India for visual effects has completely been taken up by 3D initiatives and we are now after having built that position and profile the studio that control the visual effects expenditure as well as 3D we see a good amount of interest that is starting to flow back in as we are trying to set the visual effects strategy on the same lines of the 3D strategy which is think is not currently showing huge growth in the current quarters, but I think it is something that we will see as an incremental benefit that the company should benefit from through managing to deliver consolidated and a consistent delivery mechanism for the studios and some of these big budget movies.



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On the Bollywood side of the business, we believe that the businesses have been going through some transition. This first Q1 is a little unique compared to most years with the world cup and IPL running back to back had obviously a fairly negative impact in the overall Bollywood box office numbers with much few film releasing in Q1 and the general model in Bollywood also going through a shift where the movies are coming back with high customer experience from a viewing perspective and we are hopeful that we will be able to see some benefits of the transformation of the Bollywood business model in the next few quarters as the business side of the Bollywood business makes that transition. We overall see that our business and our global positioning is only helping the company to operate in a much more consolidated and integrated fashion, which basically goes back to our very initial plan of building a model that de-risks itself across various markets and geographies and sectors of the business where we are playing a good balance between broadcast services, advertising services and film side and while there may be one big growth opportunities in one side like 3D that has happened in the last one month we believe that the other kickers in the businesses are also reasonably well setup for augmenting the overall revolution and take it to the next phase of our growth.

We generally presented a reasonable set of numbers where there is lot of optimism within the company based on where we are at, we obviously are seeing fairly large amount of investment and CapEx that has undergone to set up the entire operations for Star TV or the operations for the 3D scale up with a huge number of recruitments in our staffs and being added which is not directly producing revenue at this point only because we are in the mode of building a lot of talent pool and resource pool as the business comes in we are obviously trying to build capacity ahead of time and that may have some short term impact on the overall margin play, but I think we believe that the overall margin play will actually get up and become much more effective as we go down the few quarters where we see the roll out of our facilities and training up of people that ultimately starts to deliver a greater productive output out of India and making sure we are maximizing capacity utilization and the build up that we have incurred so far on building these businesses and doing a revolution.

The general outlook of the overall business seems very positive at this point and the company continues to remain pretty confident of being able to hopefully deliver a year, which is in-line with this growth story and general projections.

Nishant Fadia:

One more thing I would like to add I am sure everybody wants the revenue breakup, it will surely come as a question so the revenue breakup is- there is a \$21 million revenue from the US, which is the 2D to 3D and the visual effect business within that about \$17 million is the 2D to 3D business and \$4 million is the VFX business, Rs.21 Crores of revenues from the local Indian business, Rs.5 Crores from Prime Focus Technologies, which is the clear platform where the clear platform is the host and about Rs.60 Crores from the UK business.



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- Moderator:** Thank you. Ladies and gentlemen, we will now begin with the question and answer session. We have the first question from the line of Nayan Mehta from 21st Century Shares & Securities. Please go ahead.
- Nayan Mehta:** Probably I missed out couple of data points on the breakup of the revenue, I request you if you can just repeat the same thing?
- Namit Malhotra:** We got \$21 million of revenue from the US, which is essentially the 2D to 3D and the visual effect business, further breakup of that is \$17 million is the 2D to 3D business and \$4 million from visual effect business, Rs.21 Crores is from the local Indian business, Rs.5 Crores is from Prime Focus Technologies, which shows a host of clear platform and Rs.60 Crores from the UK business.
- Nayan Mehta:** Secondly is it possible to give a breakup of the margins on London and US?
- Namit Malhotra:** Do you want it now or offline, I do not have the information right now, I can send you offline.
- Nayan Mehta:** The VFX and 3D comprise of about, how much is the total consolidated sales?
- Namit Malhotra:** It is about Rs.95 Crores, \$21 million.
- Nayan Mehta:** That is about 55% of total sales because earlier the figure was little lesser.
- Namit Malhotra:** US will contribute more to the topline than the rest of the geographies.
- Nayan Mehta:** You mentioned that the ramping up in employees actually had an impact on the standalone results, also some of the other expenses have gone up, what would this hike in expenses which is on a year-on-year basis 100% jump in the employee and some of the SG&A expenses, so what kind of growth would it propel going forward- your standalone results?
- Namit Malhotra:** I think the way to analyze that is currently it is a lot of the growth that is currently being captured is captured between I do not know if we need to make the assessment more specifically on the standalone basis because it is the consolidated numbers that should be viewed because the fact that you can see that there is a cost increase, but the cost increase is ultimately towards what business is being generated in the international operations of the company, on a consolidated basis you see a let out of the consolidated business growth, which is going towards billing your own subsidiary basically, I would obviously recommend that everybody looks at the operating margin especially on a consolidated basis because that will give you an accurate view of how the business is tracking on a quarter-on-quarter and year-on-year basis rather than look at the



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standalone business because standalone business right now is not able to completely visibly show what the overall construct of the growth and direction of the company is.

Nayan Mehta: Secondly talking on the EBITDA margins, standalone last year full year was about 40%, 41% operating margins and the consolidated was about 31% to 32% excluding other income now this year we have seen in Q1 the margins are about 25% to 26%, 25.7% on consolidated basis and standalone is...

Namit Malhotra: 28% on console.

Nayan Mehta: Excluding other income also?

Namit Malhotra: Yes.

Nayan Mehta: Rs.420 Crores of EBITDA and Rs.167 Crores of profit about 25.7% something whatever there has been an drop on consolidated largely because of I believe lower EBITDA in standalone also, but going forward do you think that you would be able to maintain the same margins of FY'11 on consolidated basis or you will catch up in the remaining three quarters the margins which has seen a decline?

Namit Malhotra: I think that certainly the margin play will improve with the overall utilization happening out of India, for that particular part of the business there will be margin growth, but what we have to also view in reasonable light is the fact that there are other elements of the business like I said the Bollywood business in the Q1 has not performed to its original level, so you are seeing a negative impact on the overall margins not only because of one part which is developmental, because there has been an operating part of the business, which has not necessarily done what it did last year from the overall construct of all the services that we provide because of the cricket matches that had a fairly strong impact on the first quarter of the year, now that has an impact on not just Bollywood but even the South India film market business, the overall film business was not playing out and there is a whole delivery that was being held back because of what is going on, so what we are seeing obviously is that there is an increase in the personal cost from growth at the international business side which is a positive thing which is where the margins actually will enhance but on the other hand what is also see there is a drop in the domestic film business, which is owed to special factors which are not necessarily a yearly phenomenon and we anticipate to see overall also. The overall analysis should be based on both the parts in consumption rather than seeing it in one light. The international business the theme that India scale up to do more and more work. We will actually see a margin expansion rather than a drop. On the other end we also do Indian business and that business actually will catch up, so it is all normal traction of what it should be doing regardless of the international business.



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- Nayan Mehta:** One think on the FCCB, if you could give some clarification there are some notes in the results, you can throw some light and simplify it for us what exactly is the outstanding amount?
- Nishant Fadia:** The entire FCCB is outstanding, which is \$55 billion, regards to the note to accounts, this has been a repetitive note over the last few quarters and it basically states that we are not revaluing it in our books because we believe it is a non-monetary liability so the foreign exchange reevaluation does not happen and the premium on the conversion has not been factored in because again it is a non-monetary item which are the back-ended interest.
- Nayan Mehta:** What is the conversion price of these bonds?
- Nishant Fadia:** 111, conversion is in December 2012.
- Nayan Mehta:** What kind of equity dilution will happen at that time assuming the conversion rate?
- Nishant Fadia:** The conversion rate is 13.5%.
- Nayan Mehta:** Lastly is that claim of Rs.6.5 Crores from shareholders of (indiscernible) 17.28 business, which was acquired by subsidiaries, what is the status on that?
- Nishant Fadia:** That has been settled out of court with the litigants. It is award of 2 Crores settlement.
- Moderator:** The next question is from the line of Mayur Gathani from OHM Group. Please go ahead.
- Mayur Gathani:** I want to have couple of updates, order book figures if you give us for VFX and 2D, 3D for the current year?
- Nishant Fadia:** We can only give the total consolidated number, which is currently we are tracking about 90 million in order book over the next 24 months without getting in to more detail on that.
- Mayur Gathani:** Any further updates on this clear technology, are we getting in to tie up with any other broadcasters?
- Namit Malhotra:** We are obviously talking to everybody in the business right now because Star TV obviously is a very big win and everybody is waiting and watching how the implementation phase is run where I think everyday we are making very good progress on that side. We are very hopeful that through the course of the year we will have few more networks that will come on board, our platform and others will have good news for the company.
- Mayur Gathani:** Regarding this Disney takeover of UTV does it impact our tie up with them?



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- Namit Malhotra:** No. I do not think so because the management does not change and that is the most important thing. I am hoping that with Disney acquiring UTV that hopefully we should be able to leverage some of our relationships to do something for Disney. I am obviously hoping to expand that relationship a little further on that basis.
- Mayur Gathani:** You did mention that the domestic film business is not doing well or has been impacted because of cricket; I understand that it has not been doing well for quite sometime or it is just a one-time phenomenon that this quarter it has impacted?
- Namit Malhotra:** The general growth in the Indian film business has been flat because if you see the kind of movies that has been doing well of late are very heavy, Bollywood star driven ones and the industry is really waiting to make a transition from the current model to what is prevalent in the best, which is to bring in more of the super-hero genre of movies, now you will see this year Shahrukh Khan's first big super hero film called RA One for which Prime Focus is again providing complete 3D conversion services, which is releasing on Diwali and that again will hopefully spell the trend for the next wave of movies that will come for the Indian audiences, so I think that is where the industry will start to prosper because otherwise what has happened since the time the global recession hit, most film producers and distributors started playing a much more safe game and at least what they thought was a fair game and they ended up producing movies that had greater dependence on stars and that also has not necessarily worked very well barring a few movies here and there, so I think the general Bollywood model is up for a rehaul overall of the kind of movies and the kind of movies that they are making and that should bring a definite bug back into the business because we have seen some of the big movies like Dhoom-3 with Aamir Khan being launched, Krrish-3 is being launched, lot of good big movies are now starting to come back and that I think will herald a new signal for the growth of the Bollywood business.
- Mayur Gathani:** Getting back to the same point, RA One you have done some 2D to 3D conversion for that movie as well?
- Namit Malhotra:** Yes we have already doing it.
- Moderator:** The next question is from the line of Pankaj Chopra from Shanti Asset Management; please go ahead.
- Pankaj Chopra:** I was wanting to understand in a bleak economic scenario does it impact the amount of budgets these movie making companies spend on making new movies, does the number of movies have come elasticity to the economic scenario in some way. Do the number of movies which are made in Hollywood or probably not so much Bollywood I guess that the funding is not so related to the economy, but I guess in Hollywood that would be a big chunk, funding for the studios there



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would be an issue in a bleak economic environment and secondly we may extend this question to the 2D to 3D conversion does that get impacted in some sense because of lack of funds?

Namit Malhotra:

First of all I think the lack of funding in Hollywood is a phenomenon hit by the independent film market, not really the studios. Studios are all well capitalized and are in a position to reasonably finance what is their slate of movies, general Hollywood numbers this year of only the best, which has been in a few years; you had three billion dollar films in the summer itself. You had Pirates of the Caribbean, Transformers and Harry Potter all hitting more than a billion dollar in the box office for Disney, Warner and Paramount. All three again happened to be in 3D by the way, so the question really is that 3D as a medium is clearly driving additional revenue for the studios and they clearly will continue to be in that zone because the decision is more than the studios made by the filmmakers and if you see the level of film makers in Hollywood that have adopted to 3D it is like the top ten Hollywood film makers are all making their film in 3D that is something that we are going anywhere, anytime soon because we are going to get the biggest movies, biggest film markers all in 3D, other thing is that financing for the studios as I said is not stuck through direct impact on the economy because ultimately the studios will end up, studio really depends on its overall revenues not just on theaters, but even downstream revenues if the movies are not made. The studio business is impacted severely and we have seen in all three recessions in the past but the studios have actually done well most of the spending for the upper income and the lower income groups in a film is one of the cheapest source of entertainment here in the US as it is in India as well, people do not really find themselves saving money on movie tickets, they end up saving money on several other areas so the film business continues to be robust on that count and I think that 3D is a new welcome for the audiences to go in and see the films, what you have seen is a debate in the industry where the consumer or the media is questioning the amount of premium that is being charged, they are charging 38%-40% premium in the US to watch the film in 3D whereas a 3D film cost for studio overall less money to produce. There is bit of a issue that a capitalist country like America has is how can you be having lower cost of producing and higher ticket price, I think its more of that question which is being sparked more than anything else and as far as the global box office is concerned the international markets today contribute to Hollywood more significantly than the domestic box office and in the international markets the business is normally robust but it is also doing very well in 3D. I hope I have answered both the questions because the 3D and the overall box office and financing are all looped together. One is actually driving the other in terms of a higher revenue and a lower cost of production because just remember 3D means it is all digital that means to that extent there is no more celluloid film print being sent out which is a huge saving for any studio and they are releasing a film in 3D versus releasing a film on the regular film formate, so it is actually a way for them to curtail their cost, curtail piracy and increase revenue by selling more expensive tickets, not a single studio has commented to any of the debate that the media is having about 3D because they know they are doing very well on that account.



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- Pankaj Chopra:** Just stressing on one point which you mentioned earlier that individual film makers would be affected, is there a large number of individual film makers in the US or its more studio dominated industry?
- Namit Malhotra:** Even though it is studio dominated but the studio is ultimately out of share of the film maker, the studios cannot make a film without film marker. If Peter Jackson who made Lord of the Rings is making Hobbit in 3D or Spielberg is making Tintin in 3D or Martin Scorsese is making Hugo Cabret in 3D or Ridley Scott is in 3D and even Steven Soderbergh you name any of the top film makers that are out there from a box-office perspective and you will see that everybody is in 3D, Spiderman-4 which is going to be released next year is in 3D, Men in Black is going to be in 3D, it is like every big major Hollywood film which is a franchise which was not in 3D before is in 3D next year and current year, so what that does is if the biggest film and the best film come out in 3D that automatically drives the audiences back and the studio decisions are based on film makers and that is how the cycle actually works for anything.
- Pankaj Chopra:** How do you see competition in this, you have been doing pretty nicely in terms of growth, what is constraining growth, is it the capability to get people and at what level do you see the business itself, availability as a constraint?
- Nishant Fadia:** Obviously it is a new business. Avatar released like 18 months ago, the first film clash released on April 2 last year. We are talking about less than 15 months because the first time a film was converted to 2D to 3D completely, that is only 15 months old but we have seen this level of growth, it is substantially great, we were 50 to 60 people last year, now we have more than 3,000 people today operating out of India in 3D conversion side, so it has been a huge growth curve and I think we have done a decent job in managing that growth and making sure that our production pipeline and our capabilities are performing well. Obviously there has been constraints in scaling up based on the availability of how much capital and how much trained manpower is there and I think between that and how the market is growing it has made fairly good advancements in planning ahead and getting ourselves ready for the overall positioning that is happening.
- Pankaj Chopra:** Are there any big players of comparable size as yours where the scale up is as rapid or is that you are probably the first on the block with this kind of a size?
- Nishant Fadia:** I think we are clearly ahead of the curve from everybody else in terms of size, our second and third combined are the capacity we do, but that being said it does not mean that anybody who sees a big opportunity tomorrow is going to feel like they want to be part of that business and everybody is going to try and take a bigger hit regardless of whether they can do or no. We at least have managed to build that positioning within the studio because what you must note is there are ultimately only six studios in Hollywood and we have almost worked with every studio in the



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last one year to 15 months at a certain level where we have done about their best and biggest film. The studio themselves recognize the leader in the pack and they understand that Prime Focus today has an edge above the general market competition as they recognize us as being of top quality and big player in that slate, now that does create enough room for somebody else to come in on that, I cannot say but I think I definitely do believe that we are in a good position to get the first look at what comes out.

Pankaj Chopra:

May be its a bit provocative, do you see think this could be a fashion or fad and then 3D would again move back, of course the experience is completely different and at any point of time one may say that this is here to stay but does it at all worry you that this could be passing phase for the industry. You expect much more almost every movie having some parts of 3D getting in?

Nishant Fadia:

I can forward lots of article if I have the same question here in Hollywood everyday, what I am saying is that, if it was just a gimmick it would have worked for one film, two films and four films and stopped, the fact that you are getting such a diverse buy-in from some of the best film markers of the top and that is what like going back to that ultimately worldwide the film industry is led by filmmakers and audiences go and watch those films because you know that those are the big 10, 20 movies of the year that you are going to watch come what may and when those guys have made a decision to be on 3D and they are not going back to 2D it is almost like you see any big technological change that has happened in the film business. People when you talk of a studio they say in the 1970's and 80's, people asked question whether every film should be made in color because there was cost implications in making in color and they felt that some of the more classic pieces of film should not be made in color and that should be made in black and white because that had a certain formality and seriousness to it, there was a time when people argued the same thing about sound, you see and you hear the film makers speak about this everyday they find this is a new tool in the toolbox to say their stories better, there is no gimmick, it is not like you have watched the movie and you are feeling enough of 3D, because you are seeing a film and drawing you in to the experience which is what the biggest challenge any good filmmaker has is how to keep their audiences gripped in to the film and that is what 3D has given them, it cuts piracy, it cuts distribution costs, finally in this revolution also like the recent Wimbledon final matches were covered in 3D and broadcasted in UK which was a big success, the driver of home entertainment which something comes in and becomes a standard it take few years like HD for example India is catching on the high definition but today being here in US every major broadcaster and every major channel is in HD. When HD came everybody had this question why would I have the HD, why is it better, why would I spend money but the reality is everything is today in HD, 3D is in fact much more of a game changer than HD was, in fact today I got an email saying HTC mobile phone company launched a mobile in 3D. LG are now going to ask glasses-free 3D TV, Toshiba has a laptop which is 3D without glasses, so the whole ecosystem around the business is moving towards that side and there is no real reason why games are in 3D



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there is no reason why people have problem with it especially with the technology becoming more and more accessible. It is becoming another way for you to engage in the experience. Ultimately the reason why the studios are not revolting is because what the studios have done very cleverly here is what they have seen happen is that there is a market, if they had the same 2D movie how would they increase the price and the ticket, what is the basis to increase the rate ticket price. So what they have all done very cleverly is they used the opportunities of having got the 3D window and have pushed the ticket prices up to 38%-40% and what they ultimately slowly start doing it get people use to fill higher ticket price and that is ultimately driving more revenue, which is what any business wants. The whole argument is so heavily tilted in the direction of benefits that I do not really see it going away also because all the TV manufacturers in the world, computer manufacturers even Apple has patented a technology for glasses free and lets talk about the next i-Pad version being in 3D film and there is so much that is happening that when we say that it needs to get structured you know it is like I would not compare to the dotcom era but there was so much of hype but the fact is that this is a one year old technology and any technology takes a little bit of time to get accepted and we are seeing greater acceptance everyday, so I do not think that is a concern at all.

Moderator: Thank you. The next question is the followup from the line of Mayur Gathani from OHM group. Please go ahead.

Mayur Gathani: Can you give me the CapEx for FY'12 and cash and debt on the books?

Nishant Fadia: We are packing between \$15-\$17 million of CapEx. Debt on books currently is the FCCB plus 250 Crores of consolidated debt is on the books and profile for that 250 Crores is 100 Crores is working capital 80 Crores is property related loan, balance is term debt which is about 65 Crores.

Mayur Gathani: And the UK business would constitute of what VFX and 3D as well?

Nishant Fadia: The UK business it does have a VFX element but it is essentially post in VFX for the advertising and broadcast market out of London.

Mayur Gathani: Basically television?

Nishant Fadia: Yes.

Mayur Gathani: And local Indian business would mean post production?

Nishant Fadia: Post production and visual effects.

Mayur Gathani: Can you repeat what you meant by UK business?



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- Nishant Fadia:** Its television broadcasting and advertising post production and VFX for the London market.
- Moderator:** The next question is the followup from the line of Nayan Mehta from 21st Century Shares & Securities. Please go ahead.
- Nayan Mehta:** We have tied up with Eros for digitalization of their entire library, how lucrative is this business and how many more such opportunities are available with other entities in India?
- Namit Malhotra:** This is the prime technology deal, they are using the same technology we have so. What is interesting is the first phase of digitalization of the entire library and next phase of the business is the monetization of the library as they start syndicating all their content across all the various markets and we get fees for all that happens post. We think this is going to be one of the biggest (indiscernible) 41.23 in our portfolio and it is going to shine because it is a captive consumption business that once you set up digital archives we are going to control the future monetization where there is a fixed revenue stream and we believe that any and every content company whatever they do is the potential customer for our technology platform so the market has been seeded by our technology.
- Nayan Mehta:** Could you give us some color on this particular instance Eros International's thousand titles what could be the kind of revenue initially a digitalization and then the monetization, and per title what is the kind of potential?
- Namit Malhotra:** I do not want to give a speculative position. Currently there is a cost at which we do the digitalization and the next stage of the process is where they start syndicating the content. Syndicating the content across television new media and other platforms is little bit grey in the sense of speculating today we all know that the same content has been sent to airlines and on You Tube and on mobile partners worldwide and there is a constant reprocessing of the data. The numbers it is a little sensitive to publicly announce that from a competitive standpoint but I can say that it is pretty lucrative.
- Nayan Mehta:** Is there a possibility that 2D films existing Hindi 2D titles can be converted into 3D on a larger space going forward. What is the will from the production house or what is the will of the producer to convert and allow the film to be made in 3D?
- Namit Malhotra:** It is very good. Everybody is currently waiting and watching the see where they are ultimately lined in terms of how many 3D screens are available in India for Indian films other options that everybody looking for is in Hollywood we have the Star Wars movie releasing, we have got Titanic releasing, obviously a lot will count on how that box office does, if the box office is good you can be sure that a lot of producers will join in the bandwagon.



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- Nayan Mehta:** More opportunities will be existing in Hollywood than in Bollywood for conversion from the existing 2D to 3D?
- Namit Malhotra:** What is happening is that, lot of Bollywood films practically which are not in 3D will come out in 3D, so you can imagine if 10 or 20 movies a year in Bollywood comes out in 3D that itself is a huge market, that itself will becomes a 200-300 crores market.
- Nayan Mehta:** Can you replicate the same digitalization of liability in Hollywood also something on that or whether they already digitized?
- Nishant Fadia:** No they are not digitized. We are hoping to encash on the next stage.
- Moderator:** As we have no further questions. I would you like to hand the floor back Mr. Ankit Kedia. Please go ahead sir.
- Ankit Kedia:** I would just like to thank the management for taking their time out and giving us the outlook on the business and quarterly numbers thank everyone for joining us.
- Moderator:** Thank you gentlemen of the management. Ladies and gentleman on behalf of Centrum Broking that concludes this conference call.