
DOWNGRADE
CAESARSTONE | NASDAQ: CSTE
INVESTMENT RESEARCH REPORT
"A Counter to the Bullish Thesis"
RECOMMENDATION: Strong Sell

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Spruce Point Issues Follow-up Report on Caesarstone

- Since Spruce Point's initial report on Caesarstone (Nasdaq: CSTE or "the Company"), which highlighted many fundamental issues facing the Company, along with potential accounting irregularities:
  - Two key Board members have resigned for nebulous reasons pertaining to Board governance matters
  - A 5% shareholder completely exited its position
  - No stock buyback or insiders purchases have been made
  - CSTE has not reiterated its guidance, and something seems amiss in the story
- In our opinion, many of the open questions remain inadequately addressed, or completely ignored, by the Company and its group of supporting analysts. Spruce Point's follow-up report reiterates open questions and delves deeper into the issues we believe are facing Caesarstone.
- This report will highlight additional potential accounting issues which are related to capital expenditures:
  - Caesarstone's U.S. facility is vastly more expensive than peer manufacturing facilities around the world, is over budget by $30m (30% above initial estimates of $100m), and the Company does not appear to be offering specific details on the exact cost drivers of the project. The current project cost amounts to ~10% of its market cap
- Furthermore, this follow-up report will explore management's history at Tefron (OTCBB TFRFF), a formerly NYSE listed public company, that failed under the leadership of CSTE's current CEO Yosef ("Yos") Shiran:
  - A detailed behavioral analysis suggests that an eerily similar timeline and playbook of events may be unfolding at CSTE. Most notably, we find that Tefron also faced consistent issues of misguiding its capex costs
  - Its CEO Yos Shiran unloaded Tefron stock at peak prices before margins ultimately collapsed, admissions that Tefron could not adequately compete on price, and before directors would resign with one director openly questioning management's budgeting process
  - Tefron's stock ultimately fell >85% from its high before being delisted on the NYSE. A nearly identical sequence of events appears to be currently unfolding at Caesarstone

New Concerns Raised About Capex Spending, Increased Risk of Potential Acct'g Fraud

U.S. Plant Expansion 30% Over Budget (initially $100m, now $130m) and Substantially Higher Cost Than Peers

- CSTE's U.S. expansion project was announced in late 2013 and its cost, initially estimated at $100m, increased by $15m to $115m in Q2'14. Its cost estimate was raised another $15m to $130m in Q1'15 ahead of its sales guidance reduction
- On a per sqft basis, the plant expansion is ~60% more than Cambria's expansion in Minnesota and ~45% more expensive than its own Bar-Lev expansion from 2004–2007. LG is also upgrading capacity in Georgia for a total of just $90m for two production lines
- CSTE has been baiting investors about its U.S. growth story and plant expansion since 2013, and now the plant is practically idled with limited production. We also don't believe that CSTE is offering investors any detailed breakdown of its plant construction costs
- It makes no economic sense to us that CSTE invested 10% of its market cap in a plant asset with no definitive time table to full production

Heightened Risk of Potential Accounting Irregularities From Overstatement of Earnings Due to Cost Capitalization

- CSTE's motivation to raise its capex cost estimate of the U.S. facility by $30 million could be to capitalize operating costs to its balance sheet, and thereby overstate earnings. **CSTE does not disclose how much costs have been capitalized**
- CSTE's PP&E accounts have increased by more than its reported capex through the cash flow statement by ~$10m in 2013-14
- CSTE has given a variety of nebulous excuses for the $30m cost increase. Its most recent explanation was that it needs to fine tune its equipment, improve environmental conditions, and add a new showroom. We are skeptical of these explanations, especially in light of our request to the Georgia Environmental Dept that found no outstanding environmental issues
- There are precedent examples of companies having committed fraud by repeated capex line increases and overcapitalization of normal operating expenses to inflate EPS and hide sales shortfalls. For example, on September 8, 2008 the SEC charged American Italian Pasta (Nasdaq: AIPC) with accounting fraud. Is CSTE following a similar playbook?

CSTE Doesn't Even Own Its U.S. Facility, The Project Has Been 100% Pledged, and is Behind Production Schedule

- Buried in its 20-F, CSTE disclosed a transaction whereby the Bryan Country Economic Authority granted CSTE tax breaks for locating within the county. There is very limited disclosure about this financing
- We filed a Georgia Open Records Request (GORA) to unseal the documents and found that in December 2014, CSTE structured a $100m credit facility @ 6% interest cost ($35m verified draw-down as of 12/31/14). The transaction is supposedly non-cash, and structured similar to a sale/leaseback to provide tax incentives subject to investment and hiring goals. Importantly, CSTE has pledged the entire project to Bryan County which means it does not currently have title to its facility yet derives economic benefits from it
- Given that CSTE is experiencing slackening demand, and at risk of not meeting its goals (note only 107 people hired as of 5/27/15 vs. 180 required), it may not be able to reclaim ownership of its facility, which could potentially leave investors with a big tax bill and little asset value recovery in the case of bankruptcy

Additional Concerns About Management's History, Downgrading Price Target

Management's History at Tefron, A Failed Israeli Garment Manufacturer, Provides Insight Into How The Dominos May Fall

- CSTE's CEO and General Counsel and VP of Business Development worked at Tefron, a former NYSE listed public company, which collapsed from bad execution and mismanagement according to reports. **Tefron's auditor is CSTE's current auditor**
- Tefron was promoting a period of rapid sales and margin expansion along with a unique Italian manufacturing technology. CEO Shiran liquidated stock before its margins collapsed. Later Tefron admitted to investors its manufacturing technology faced problems, and it could not compete with lower cost foreign producers
- **Our analysis suggests that Tefron consistently misguided investors about its capex estimates every single year by an average of 137% per year from 2003 – 2010! Is it just a coincidence that CSTE has raised its capex estimate twice in under one year?**
- In 2009, after CEO Shiran resigned, but while Michal Baumwald was still with Tefron, Director Micha Korman resigned and questioned management's budgeting process and communication with the Board. His warning appears prescient in light of Tefron's rapid decline and ultimate delisting from the NYSE
- Ironically, two Caesarstone directors, Ram Belinkov and Avner Naveh, resigned from its Board in late September. SEC filings have given a nebulous explanation for each director's resignation, but this suggest differences of opinion over governance and Board matters

Downgrading Price Target on Weakening Fundamentals and Heightened Risk of Potential Accounting Irregularities

- A majority of our initial concerns have not been adequately addressed, most notably, how can CSTE maintain its perception of being a premium product with inconsistent quartz content messaging to consumers (88%?, 90%?, 93%?), and maintain prices with cheaper imports being offered at up to 25% lower price points?
- Recent North America import data shows the largest monthly decline in history of CSTE's products and amplifies our concerns that its 2016 sales and EPS expectations are at risk of disappointing. With its U.S. facility reportedly producing immaterial amounts of products, CSTE is dependent on imports from Israel. Thus, we believe the import data is a highly reliable indicator of future revenue and earnings shortfalls. Further, CSTE's inventory growth is now outpacing revenue growth by the widest margin since 2011
- CSTE still trades at 2.1x and 7.5x 2016E inflated Wall St. sales and EBITDA estimates (unlikely to be achieved) on the belief sales will grow 18% next year and margins can be maintained. Yet, our findings suggest that its sales may be stagnant and its EBITDA may be overstated by up to $30 million in the event it has over-capitalized its cost overrun to its balance sheet. In our view, it is trading at closer to 2.3x and 9.5x forward sales and EBITDA. It is also important to consider that since CSTE's capex may be artificially high, it should be evaluated on a free cash flow basis (CFO – capex). Free cash flow has been flat/negative for 5 out of the last 6 quarters.
- We lower our price target to ~$8.50 - $23.00/share on a 6x – 8x 2016 EBITDA (lower/realistic multiple) and assume just 5% revenue growth. We also factor in $34m of potential silicosis liabilities which analysts models' ignore. A recent TV documentary in Israel highlighting the severity of the "Caesarstone silicosis epidemic" underscores the risk to shareholders of adverse legal judgments

Open Questions For Management

Product Quality and "Premium" Branding

a. Why is a 93% quartz being advertised by CSTE and its distributors when our lab tests suggest the true quartz content is 88-89%?
b. Should CSTE consider clarifying what is considered a "Premium" quartz countertop?
c. How does CSTE maintain its "Premium" branding while continuing to lower R&D spend and headcount?
d. If the product is "Premium" why sell it as a generic product at a discount retailer like IKEA?

Market and Sales Growth

a. What is CSTE's plan with its new U.S. production facility given it is not materially producing and the market is being flooded with cheap imports from China, India, Vietnam, Russia and other countries?
b. Why does CSTE not disclose unit slab sales and average pricing per slab by product line?
c. How has CSTE historically grown sales at a 20%+ growth rate with flat U.S. TEU import data according to our source

Margin Contraction

a. Why did CSTE not cut its 2015E EBITDA range last quarter and instead maintain it by slowing the ramp of production at the new facility? Is CSTE implicitly telling investors that its sales demand no longer remains robust?
b. If the Kibbutz were not a substantial owner of CSTE, would its agreements with them increase or decrease its operating costs and what would be the margin impact? Why did a Kibbutz board member resign?
c. Why did CSTE say that its raw material price for quartz went up just 4% in the face of evidence from its own supply contracts that the annual impact was approximately double?
d. Why did CSTE request a 5 year confidentiality period for its recent quartz supply contracts?
e. How much more will CSTE bear from importing costs from places like Turkey to its U.S. production facility in Georgia?

Currency Effects

a. Why did CSTE change its functional currency to the US$ and why doesn't it discuss in more detail the impact on its margins?
b. Why does CSTE include currency effects in the Net Finance Expense income statement line item rather than reporting it as an Other Expense line item?

Anomalous Capital Expenditures

a. Why is CSTE's capex estimate for its U.S. facility 30% above its initial estimate, 60% more than comparable peer plants on a per sqft basis, and 45% more expensive than its Bar-Lev facility?
b. Why did CSTE give limited details about its Bryan Country financing and tax arrangement and why did it agree to pledge the entire project?
c. Why doesn't CSTE disclose the exact amount of costs capitalized on its balance sheet during the construction period?

Key Caesarstone Executives Worked At Tefron, a Former NYSE Listed Company That Crashed

	Tefron (Misgav Israel)	Caesarstone (Menashe Israel)
Listed	NYSE 1997 (Delisted 2011)	Nasdaq 2012
Auditor	**Kost Forer Gabbay & Kasierer**	**Kost Forer Gabbay & Kasierer**
Key Individuals	Yos Shiran, CEO Jan 2001 – Aug 2008 Michal Baumwald, Chief Legal Officer Aug 2004 – June 2009	Yos Shiran, CEO Jan 2009 - Present Michal Baumwald, GC and VP Business Dev. Sept 2009 – Present
Director Resignation	**6/22/09: Micha Korman resigns, makes claims regarding the conduct of the mgmt. communication w/Board; special committee formed**	**9/17/15: Ram Belinkov resigns due to matters related to the Board and governance concerns** **9/25/15: Avner Naveh resigns due to "difference of opinion"**
Stock Liquidations	Shiran liquidates 150,000 shares through options exercised on May 9, 2006; coincides with peak margins and stock price	Shiran granted options to purchase ordinary shares equal to 2% of the company at IPO at $11/sh. Shiran cashed out of options btw 5/30/14 & 2/28/15 at est. prices of $45 - $65
Capex Question Marks	Tefron consistently over-estimated its annual capex by an average of 137% from 2003-2010	U.S. Plant is 30% over-budget, 20-60% more expensive than close peers on sqft basis and 45% more than Bar-Lev
Key Equipment Supplier	Santoni (Italy) – "This is a very high-tech process," said Danielle Hami, Tefron's Manager of U.S. Marketing/Sales	Breton S.p.A (Italy) – Uses Breton along with its "proprietary manufacturing enhancements"
Gross Margins	Peaked at 22.8% in 2006 and plunged to -3.3% in 2009 from customer losses, admission it could not compete	Peaked in 2013 at 45.5%. Gross margins appear substantially higher than peers, and rising quartz prices + price compression may not be accurately reflected
Accounting Irregularities	Disclosed a deficiency of internal controls over financial reporting in Q1'2009 resulting in a failure to record purchasing expenses in connection with a sale made by a subsidiary (gross margin overstatement). Also had errors in sales segment reporting	Spruce Point has identified various issues related to the Company's working capital accounts and capex accounting, along with import and quartz contract data not reconciling with financial results that warrant further scrutiny

Comparison Between Caesarstone and China Integrated Energy, A Company We Exposed That Became Delisted

Many similarities between our investigative research that exposed China Integrated Energy in 2011 and Caesarstone.

Date	China Integrated Energy - 2011	Caesarstone - 2015
Listing/Ticker	Nasdaq: CBEH	Nasdaq: CSTE
Questionable Auditor	Sherb & Co. is based in the U.S. although CBEH was China-based. Sherb &Co. received significant PCAOB warning comments in 2011	Kost Forer Gabbay & Kasierer Based in Israel, and also received PCAOB audit quality citations of concern
Growth Story	Raised money from U.S. investors to build a novel and technologically advanced plant to produce biodiesel with prickly ash in China	Raised money from U.S. investors to build a technologically advanced quartz manufacturing facility in Georgia to tap U.S. "potential" demand for its products
Questionable Capex Costs	CBEH's capital expenditure efficiency was so vastly superior to any other reported biodiesel provider we analyzed. CBEH had abnormally low capex costs on a per gallon basis	Georgia plant is significantly more expensive on a price per sqft basis than globally located plants in the U.S., Canada, and Spain with not enough detail from the Company to critically analyze
Plant Utilization	Main plant was not being utilized at all, but staged for investors	U.S. plant is operating, but significantly below potential utilization at the moment
Gross Margins	Stable and consistent margins in a cyclical and commoditized business	Fairly stable gross margins even as quartz prices have risen, and pricing has gotten more competitive. Gross margins are high relative to U.S. listed building product peers
R&D Spending	Reported no spending on R&D, so it was difficult to believe that it had invented any advantage in a production process	Claims "World Class Manufacturing and R&D Capabilities" yet R&D margin has fallen significantly in the past few years to just 0.6% of sales
Difference between SEC / Foreign Financials	CBEH's SAIC Chinese financials showed a substantial departure from SEC filings	Australian and Singapore foreign filings show significantly lower gross margins, explained as due to transfer pricing

Analyst Rebuttals Weak, Our Key Questions Remain Outstanding:

Our Key Concern	Our Key Evidence	Company and Analyst Rebuttal
Product may not contain 93% quartz as advertised	Independent Lab Test	Analysts and Company say: the product contains "up to 93%" and an "optimal" amount We say: Not a single sample in our test hit 90% and CSTE allows its distributors to market 93% creating the appearance of misrepresentation to consumers.
Margins May Be Overstated Due to Quartz Prices Rising +20%	Company's Own Quartz Supply Contracts	Analysts and Company say: But the 20% increase was over 2yrs and is only one supplier contract accounting for 30% of supply We say: Yes, but that's still a 9.5% p.a. increase, more than double the 4.0% increase the company said. How could 20% over 2 years be 4% p.a.? ~67% of CSTE's quartz supply comes from Turkey and it's likely all suppliers increased prices by a similar percentage
Price Compression Leading to Margin Erosion	Channel checks and Price Quotes	Analysts say: CSTE's products are unique, and better marketed Company says: Nothing We say: Margin compression highly likely; a 25%+ pricing differential likely cannot be maintained. If FX didn't move over the last few yrs, would margins still be down? Uniqueness comes down to design, CSTE's designs can be replicated by competitors. Marketing only goes so far and will need to inc. in the future as more competition enters
Market Share May Be Eroding From More Competition	Independent Panjiva Import Data	Analysts and Company say: Trust Freedonia's paid-for research (which CSTE contributed to). CSTE has been capacity constrained so hasn't been able to grow imports We say: Our data is factual and objective. Import tonnage has been flat since late 2013 even though the Bar-Lev came fully online Q2'14. Meanwhile, foreign imports to the U.S. are rising. CSTE is no longer capacity constrained
Growing Liabilities to Silicosis Disease; Lawsuits	Company Citations in Israel Health and Medical Associations	Analysts say: Cannot be refuted, the details are buried in the company's 20-F We say: CSTE's balance sheet may not be able to sustain adverse judgments; these liabilities could impair its equity value. Analysts don't factor in potential liabilities into their valuations. The problem is serious enough that a TV program was aired in Israel
Beware of CSTE's Auditor	PCAOB Citations for Deficient Audits	Analysts and Company say: Don't worry, there is no evidence CSTE's audit was bad, financial results and accounting are perfectly fine We say: We never said CSTE was the subject of the PCAOB audit. **Let's investigate other irregularities and its auditor's past with Tefron!**

A Close Look At Caesarstone's U.S. Expansion and Capital Expenditures

A Closer Look At CSTE's U.S. Expansion Capex Reveals Substantial Red Flags

Caesarstone's Cost Per Sqft to Construct Its Richmond Hill Facility ~60% More Expensive Than Cambria's Recent Capacity Expansion in Minnesota and ~45% More Than Bar-Lev.

	Cosentino (Dekton Expansion)	Hanstone (Hanwha Corp)	Cambria (1st Expansion)	Cambria (2nd Expansion)	Caesarstone (Bar-Lev Expansion)	Caesarstone (US expansion)
Construction Date	2012 - 2013	2008 – 2009	2007	2012 - 2013	2004 - 2007	2013 - 2015
Location	Cantoria, Spain	London, Ontario CA	Le Seur, Minnesota	Le Seur, Minnesota	Bar Lev Industrial Park, Israel	Richmond Hill, Georgia
Jobs Created	300	120	N/A	200	150 - 200	130 – 180 (3)
Estimated Cost (1)	$125.0 million	$70.0 million	$45.0 million	$121.0 million	$72.6 million	$130.0 million
Facility Sqft (2)	753,473	210,000	150,000	375,000	206,430	284,167
Estimated Cost / Square foot	$166	$333	$300	$323	$352	$511

(1) Cosentino costs of EUR 100m investment at EUR 1.25 FX rate (Includes logistics platform) as per Spanish filing available here and Cosentino press release. Note: We believe the $172m cost cited in the article includes Dekton R&D costs. Cambria first expansion cost per press release and second expansion per Star Tribune article. CSTE Bar-Lev estimated cost per Globes article (NIS $180m @ 0.22 FX rate) + $33m of 2007 capex for 2nd line in CSTE F-1 filing. $130m for Georgia facility per Q1'15 management guidance. Hanstone information from press release and construction website

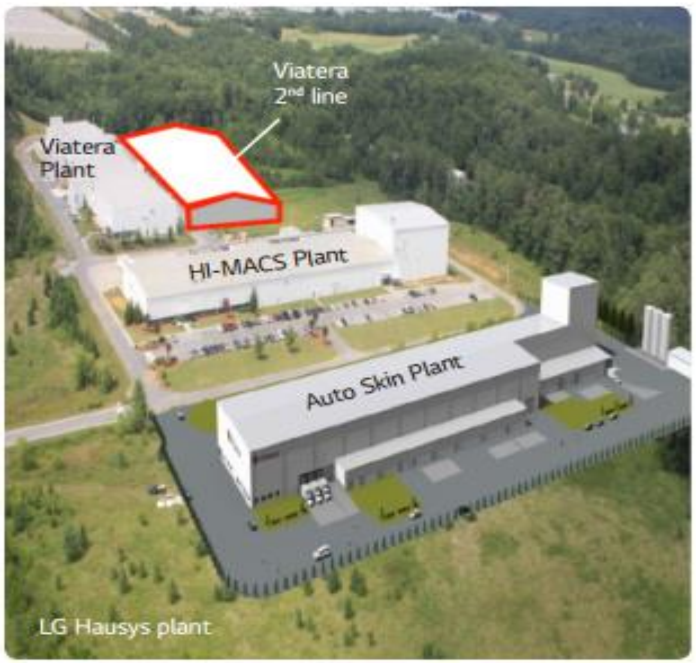
(2) 284,167 sq feet converted from 26,400 sq meters in CSTE's Annual Report 20-F page 40.

(3) Originally reported as 180 jobs created in 2013 and later as 130 jobs in 2015 despite deciding to add a second line of capacity.

A Tale of Two Georgia Countertop Facilities: LG vs. Caesarstone

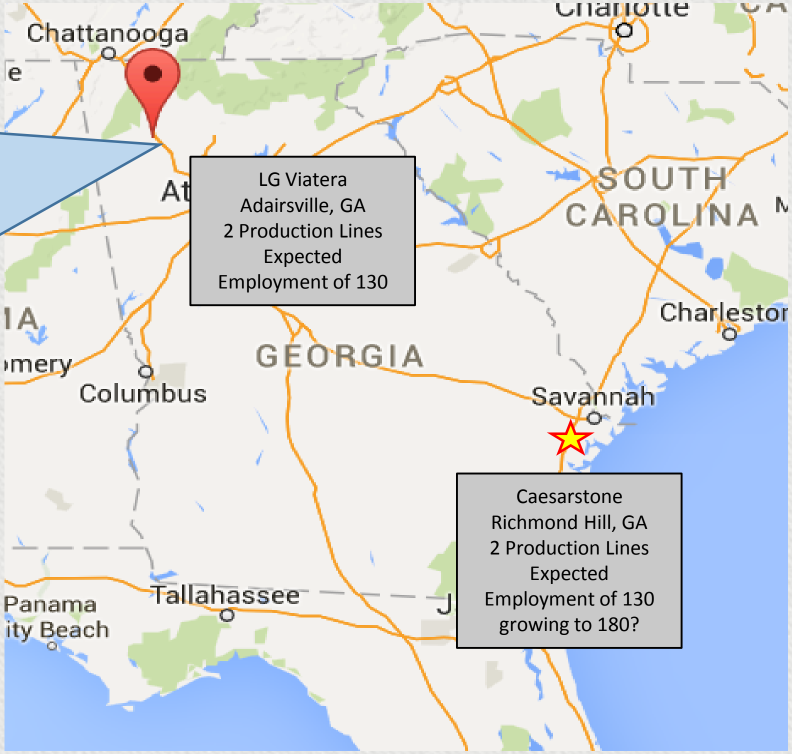
According to LG, it spent ~$50m for its initial plant in 2011, and will spend an additional $40m to add a second line which will be completed in June 2016. The all-in cost for LG's facilities and line equipment is $90m or $40m (30%) less than CSTE's project! Also CSTE reports needing to hire 50 extra full time employees by year end to run a plant with 2 production lines. CSTE does not disclose a detailed account of its capex spending, so it is difficult to understand the variance.

LG Facility All-in Cost $90m



Source: LG expansion announcement and Georgia news

Georgia Locations of LG and Caesarstone



Source: Google Maps. LG employment data from initial Georgia news in 2011 and recent article stating 50 new hires for expansion

Why Is CSTE's U.S. Plant Expansion 30% Over-Budget?

- **Project 30% over Budget**: CSTE told investors it estimated its initial U.S. expansion plan to cost $75m, with an additional $30m for a 2nd Line (Approximately $100m total cost). The cost estimate was raised to $115m in Q2'2014, and again to $130m in Q1'2015 (the last increase came before the sales guidance cut in Q2'15)

- This high cost overrun has been attributed to a variety of factors from management. The first explanation on August 7, 2014 during Q2 earnings:

  "The Company has decided to increase its investment in its US facility to approximately $115 million, compared to its earlier estimate of approximately $100 million, mostly to accommodate improvements in operations, including upgraded machinery for higher manufacturing capacity. In addition to this investment, the Company intends to start initial steps towards establishing its second building in Richmond Hill to accommodate additional manufacturing capacity in the future as needed to satisfy potential demand."

- **Coincidentally, while increasing its capex estimate by $15m in Q2'14, CSTE also raised its sales guidance range for 2014 by an identical amount**:

  "Following a strong second quarter and to reflect an improvement in both inventory and manufacturing throughput, the Company today increased its revenue guidance for the full year of 2014 to a new range of $435 to $445 million as compared to its prior range of $420 million to $430 million"

- The second increase during Q1'15 earnings on May 5, 2015 from $115m to $130m was explained in more vague terms in the press release as "expected capital expenditure related to the first and second lines" and by the CEO on the conference call:

  "With regards to the increase, it is actually a combination of a few things. There are some improvement-related investments that got into the project. We invested additional money to improve our environmental footprint that is extremely important. So that played another segment role, but there was also some partial deviation from original budget that [wasn't budget]. So the mix of those things."

- We attempted to verify CSTE's claim that environmental issues may have necessitated an increase of $15m to the project. We filed a Georgia Open Records Act request with the Georgia State Environmental Protection Division to obtain any records of env't disputes, sanctions, assessments or letters of correspondence with CSTE. Our request turned up nothing of significance

Spruce Point Capital Management

Where is the Money Going?

Two Production Lines Estimated $60 - $80m

- Based on conversations with an industry expert, a new Breton production line costs $30 - $40m
- Note: LG's recently announced line addition and building facility expansion is estimated to cost $40m in Georgia just 5 hours away
- Caesarstone is planning two lines at its facility
- Simple math suggests the lines should cost $60 - $80m, yet the Company has raised its estimated cost from $100m to $130m
- Where is the additional $50 - $70m going?
- Caesarstone does not discuss the project's cost components in its SEC filings

Everything Else: $50 - $70m?

- Showroom
- Guardhouse
- Employee welfare area
- Support and executive office areas
- Employee parking lot
- Entrance and access roads
- Railroad
- Fire pump house with tank
- Utilities
- Intermediate and finished slab storage, docks
- Material loading and unloading
- Mixing
- Press
- Polishing
- Aux support rooms
- Liquid storage

Source: Omega Construction Website

Could CSTE Be Capitalizing Costs To The Income Statement to Overstate Earnings?

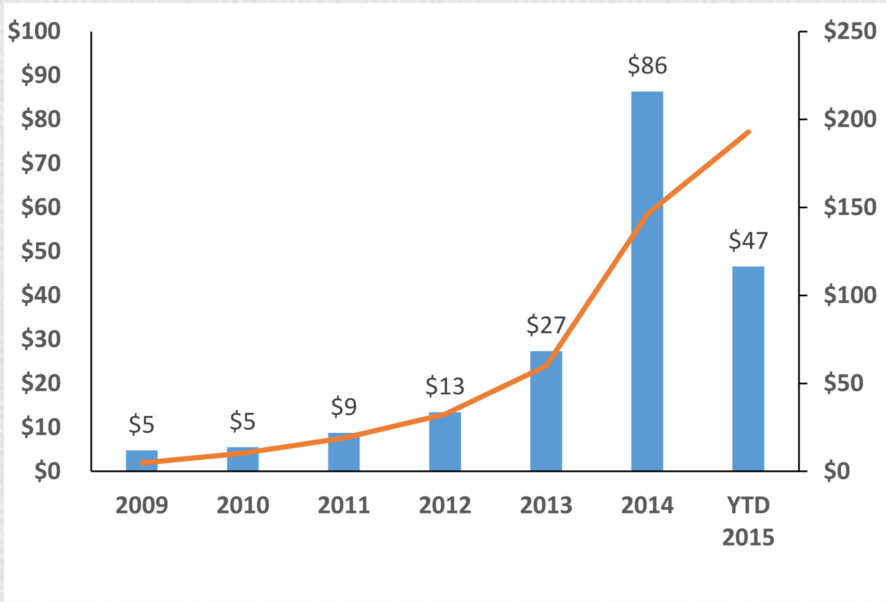
One possible explanation for CSTE's repeated increase in its U.S. plant construction is that it could provide it an ability to capitalize operating costs on the balance sheet, thereby inflating its earnings. CSTE doesn't disclose the $ amount of capitalized costs

Accounting Disclosure

"Costs recorded prior to a production line completion are reflected as construction in progress, which are recorded to Land, building and machinery assets at the date purchase. Construction in progress includes direct expenditures for the construction of the production line and is stated at cost. Capitalized costs include costs incurred under the construction contract: advisory, consulting and direct internal costs (including labor) and operating costs incurred during the construction and installation phase."

Annual and Cumulative Capex

$ in millions



Source: CSTE Annual Report 20-F, page F-20

PP&E Accounts Rising Greater Than Reported Capital Expenditures

Spruce Point Capital Management

Property, Plant and Equipment Account

	December 31,	
	2014	2013
Cost:		
Machinery and manufacturing equipment, net(1)	$ 173,937	$ 124,728
Office equipment and furniture	8,633	7,868
Motor vehicles	948	1,565
Buildings and leasehold improvements	77,281	35,686
Prepaid expenses related to operating lease(2)	939	939
	261,738	170,786
Accumulated depreciation	88,745	77,152
Depreciated cost	$ 172,993	$ 93,634

CSTE reported $86.4m of capital expenditures through the cash flow statement in 2014, and yet its PP&E accounts rose by $91m (primarily machinery and buildings). **This suggests overcapitalization of costs by ~$5m ($0.14c / share)**. Likewise, in 2013 PP&E rose by $4.3m more than capex costs.

Source: CSTE 20-F Annual Report

Spruce Point Capital Management

Capex Fraud Case Study: American Italian Pasta (Nasdaq: AIPC)

On September 8, 2008 the SEC charged the executives at American Italian Pasta (Nasdaq: AIPC) with accounting fraud. According to the SEC's complaints, the fraudulent accounting and other errors arising from inadequate internal controls, resulted in the overstatement of AIPC's pre-tax income for the relevant period by approximately $59 million, or 66%. A central aspect of the fraud was capitalization of manufacturing expenses.

From FY 2002 through the Q2'2004, AIPC fraudulently capitalized over $10 million to manufacturing assets

- AIPC had significant capital projects which typically involved additions of new pasta production lines in its manufacturing plants. The line installations generally were contracted to third parties under the direction of AIPC's engineering department. When installation of a new line was completed, AIPC's engineering department "commissioned" the line through a series of test runs and equipment adjustments. During the commissioning phase, the line produced saleable pasta in quantities that steadily increased
- Following AIPC's IPO in 1997, AIPC did not have adequate systems for measuring the internal plant labor and other costs used on capital projects. Instead of implementing a suitable system, AIPC adopted a practice of capitalizing without support internal labor and other costs used on the projects. Under this practice, internal costs capitalized were not identified specifically and segregated from ordinary operating expenses and AIPC lacked compensating internal controls.

AIPC's senior executives fraudulently inflated capitalization to long-lived manufacturing assets in at least three ways.

1. First, prior to FY 2002, senior executives instituted a practice of incorporating capitalization estimates into AIPC's annual budgets. Thereafter, month after month, through at least FY 2003, AIPC booked, contrary to GAAP, capitalization based on its budget instead of on an adequate review of actual events. During FY 2002 and 2003, to reduce reported manufacturing costs, AIPC increased the amount of capitalization improperly booked based on its budgets
2. Second, from FY 2002 through the Q1'2004, AIPC fraudulently capitalized normal manufacturing expenses that exceeded the original manufacturing budget. AIPC measured spending in excess of the manufacturing budget on a plant-wide basis, rather than with respect to individual pasta production lines. AIPC regularly capitalized, contrary to GAAP, these plant-wide variances to the budget without performing adequate analysis to determine whether they related to capital projects. Further, AIPC often capitalized the variances even when available information indicated they were unrelated to capital projects.
3. **Third, at Profit Achievement Task Force and other meetings during FY 2002 and 2003, senior AIPC executives agreed to book specific amounts of additional capitalization to offset the profit impact of sales shortfalls**. Contrary to GAAP, these amounts were booked without adequate justification and in some cases the additional costs were capitalized improperly to assets that were fully operational.

Source: SEC Fraud Complaint

CSTE's Unusual Financing Structure With Bryan County

CSTE appears to have buried the following disclosure deep in the footnotes of its 20-F Annual Report. Notice that it did not reveal the size of the loan agreement or key terms but described it as a "lease" agreement. Although DABC has title to the facility, yet CSTE believes it owns its facilities and can claim property tax abatement.

CSTE's Limited Disclosure

"In December 2014, we entered into a bond purchase loan agreement and were issued a taxable revenue bond on December 1, 2014, and executed a corresponding lease agreement, pursuant to which the Development Authority of Bryan County, an instrumentality of the State of Georgia and a public corporation ("DABC"), **has acquired legal title of our facility in Richmond Hill, in the State of Georgia, USA**, and in consideration leased such facilities back to us. In addition, the facility was pledged by DABC in favor of us and DABC has committed to re-convey title to the facility to us upon the maturity of the bond or at any time at our request, upon our payment of $100 to DABC. **Therefore, we consider such facilities to be owned by us**. This arrangement was structured to grant us property tax abatement for ten years at 100% and additional five years at 50%, subject to our satisfying certain qualifying conditions with respect to headcount, average salaries paid to our employees and the total capital investment amount in our U.S plant."

Source: CSTE 20-F Annual Report, page 41

SPRUCE POINT
CAPITAL MANAGEMENT

The Structure Looks Like Debt, But Supposedly No Cash Was Exchanged

Key Terms of Credit Facility

BOND PURCHASE LOAN AGREEMENT

This **BOND PURCHASE LOAN AGREEMENT** (this "**Agreement**"), dated as of December 1, 2014, is by and between the **DEVELOPMENT AUTHORITY OF BRYAN COUNTY** (the "**Issuer**"), an instrumentality of the State of Georgia (the "**State**") and a public corporation, created and existing under the laws of the State, and **CAESARSTONE TECHNOLOGIES USA INC.**, a Delaware corporation, in its capacity as the lessee (the "**Company**") of the Project, referred to herein, and its successors and assigns as such lessee, and in its capacity as the purchaser (the "**Purchaser**") of the hereinafter-described revenue bond of the Issuer.

WITNESSETH:

WHEREAS, the Issuer is an instrumentality of the State and a public corporation created pursuant to the provisions of the Constitution and laws of the State of Georgia, including particularly the Development Authorities Law of the State of Georgia (O.C.G.A. § 36-62-1, *et seq*., as amended) (the "**Act**"); and

WHEREAS, the Act provides that the Issuer is created for the public purpose, among other purposes, of developing and promoting for the public good industry and trade within Bryan County (the "**County**") and is authorized by the Act to issue its revenue bonds to acquire "projects" (as defined in the Act) to be located in the County; the Issuer's revenue bonds are to be issued and validated under and in accordance with the applicable provisions of the Revenue Bond Law (O.C.G.A. § 36-82-60, *et seq*.); and

WHEREAS, the Act further authorizes and empowers the Issuer: (i) to lease any such projects; (ii) to pledge, mortgage, convey, assign, hypothecate or otherwise encumber such projects and the revenues therefrom as security for the Issuer's revenue bonds; and (iii) to do any and all acts and things necessary or convenient to accomplish the purpose and powers of the Issuer; and

WHEREAS, the Issuer proposes to issue its revenue bond (the "**Bond**") in a maximum principal amount of $100,000,000 (the "**Maximum Principal Amount**"), to be issued as a single Bond in the form of a draw-down instrument to be designated "Development Authority of Bryan County Taxable Revenue Bond (Caesarstone Technologies USA Inc. Project)", which shall mature on December 1, 2024, or December 1, 2029 if the Lease Term is extended as provided in the Lease, and shall bear interest at a rate per annum of six percent (6.00%), which interest shall be payable on December 1 of each year, commencing on the first December 1 following the issuance of the Bond, with the final interest payment being due on the Maturity Date. The Bond is secured by that certain Deed to Secure Debt, Assignment of Rents and Leases and Security Agreement, of even date herewith, granted by the Issuer to the Purchaser (the "**Security Document**"). The Bond shall be in substantially the form set forth in Exhibit A to the Bond Resolution, with such variations, omissions, substitutions, legends and insertions as may be approved by the official of the Issuer who executes such Bond and by the Purchaser; and

CSTE Borrowed $35m on 12/5/14

REQUEST FOR ADVANCE UNDER BOND PURCHASE LOAN AGREEMENT,
BETWEEN THE
DEVELOPMENT AUTHORITY OF BRYAN COUNTY, AS ISSUER,
AND
CAESARSTONE TECHNOLOGIES USA INC., AS LESSEE AND AS PURCHASER,
RELATING TO THE
DEVELOPMENT AUTHORITY OF BRYAN COUNTY
TAXABLE REVENUE BOND
(CAESARSTONE TECHNOLOGIES USA INC. PROJECT)

TO: CAESARSTONE TECHNOLOGIES USA INC., as Purchaser

REQUEST FOR ADVANCE NO. 1
RELATING TO THE ABOVE-REFERENCED BOND

AMOUNT OF ADVANCE REQUESTED: $ 35,000,000 (Thirty Five Million Dollars)

DATE OF REQUEST FOR ADVANCE: December 5 2014

The undersigned, being an Authorized Company Representative of Caesarstone Technologies USA Inc., as agent for the Development Authority of Bryan County, hereby requests an advance in the amount indicated above to pay or to reimburse the Costs of the Project reflected on the accompanying Requisition(s).

The undersigned hereby certifies that:

1. The net amount of the requested advance is equal to the total amount requested in the attached Requisition(s) and the gross amount of the requested advance when added to the gross amount of previously requested advances does not exceed the Maximum Principal Amount;

2. The date that this Request for Advance is being delivered is not later than the Expiration Date set forth in Section 4 of the Bond Purchase Loan Agreement, referred to above.

3. No "Event of Default" as defined in the Bond Purchase Loan Agreement has occurred and is continuing, except:

X None
___ As described on the attached page.

CAESARSTONE TECHNOLOGIES USA INC.

Caesarstone Technologies USA, Inc.

By: ARI MAOR
Authorized Company Representative

Source: Documents received pursuant to Georgia Open Records Request with the Development Authority of Bryan County.

Spruce Point Capital Management

Project Is Pledged, Goals At Risk

CSTE must hit hiring goals for its U.S. plant to receive tax incentives. According to CSTE, the plant is operational but producing immaterial amount of products, yet CSTE wants to add additional capacity by Q4'15 and hire more workers. What will these workers do at an idle facility?

Community Investment Goals

COMMUNITY GOALS TABLE

PERFORMANCE PERIOD	COMMUNITY JOBS GOAL (cumulative)	COMMUNITY INVESTMENT GOAL (cumulative)
Commences after the expiration of the Commitment Period and continues through every calendar year thereafter during the term of the Lease Agreement and any extension of the performance period under paragraph 4, below (the "Performance Period")	180*	$70 million

*In order for the Company's interest in the Lease Agreement to be valued by the County and City for property tax purposes at 50% of the fair market value of the Project for the last five (5) years of the term of the Lease Agreement, the Company must increase its employment to a total of 250 new full-time positions on or before the eighth year following the issuance of the Bonds to the Company.

4. The Community Jobs Goal and the Community Investment Goal are each subject to the effect of Force Majeure as provided below, if the Company certifies to DABC in writing of the dates of the commencement and, if the event of Force Majeure has abated, the date of the abatement, of such event of force majeure. In the event that a Force Majeure event occurs during the Commitment Period, the Commitment Period shall be extended by the duration of the Force Majeure event, as certified by the Company. In the event that a Force Majeure event occurs during the Performance Period, the Company will be considered in compliance with its Community Jobs Goal and Community Investment Goal for the calendar year in which such Force Majeure event occurs, but the Performance Period will be extended by another year; provided that the Performance Period shall not be extended if the Company is actually in compliance for the calendar year in which such Force Majeure event occurs. Termination or expiration of the Lease Agreement will not affect such requirements hereunder, even if the Performance Period is extended beyond such termination or expiration.

54

WCSR 30578937v16

Source: Documents received pursuant to Georgia Open Records Request with the Development Authority of Bryan County.

Caesarstone Plant Opens in South Bryan

May 27, 2015

The first event Chris Carr attended as the head of the Georgia Department of Economic Development was the November 2013 groundbreaking for Caesarstone's manufacturing plant in South Bryan. Carr returned Wednesday as Caesarstone celebrated the grand opening of its plant in Belfast Commerce Centre. "To see this wonderful facility, there is definitely a 'wow' factor here," he said. "I wasn't going to miss this for anything in the world." The manufacturing plant is the first in the United States for Caesarstone, an Israeli company that produces quartz countertops. Caesarstone also is the first industry to build in Belfast Commerce Centre. The site south of Richmond Hill was chosen for the plant after Caesarstone spent about a year evaluating approximately 75 sites in several states, Development Authority of Bryan County CEO Anna Chafin said. Local leaders touted the proximity to the Port of Savannah and interstates, available workforce and "superior quality of life that's offered in Richmond Hill and the Savannah area," Chafin said.

"We have found Georgia, Bryan County — specifically, Richmond Hill — is the best place for us," Caesarstone CEO Yos Shiran said. "I think they really fell in love with the community, just as all of us have," Bryan County Commissioners Chairman Jimmy Burnsed said in a video that was played for the local and state officials and Caesarstone employees gathered for the celebration.

The first production line is up and running, and 107 people are employed at the South Bryan plant, according to Shiran. A second line is expected to be added by the end of this year, he said, which will bring about 80 more workers.

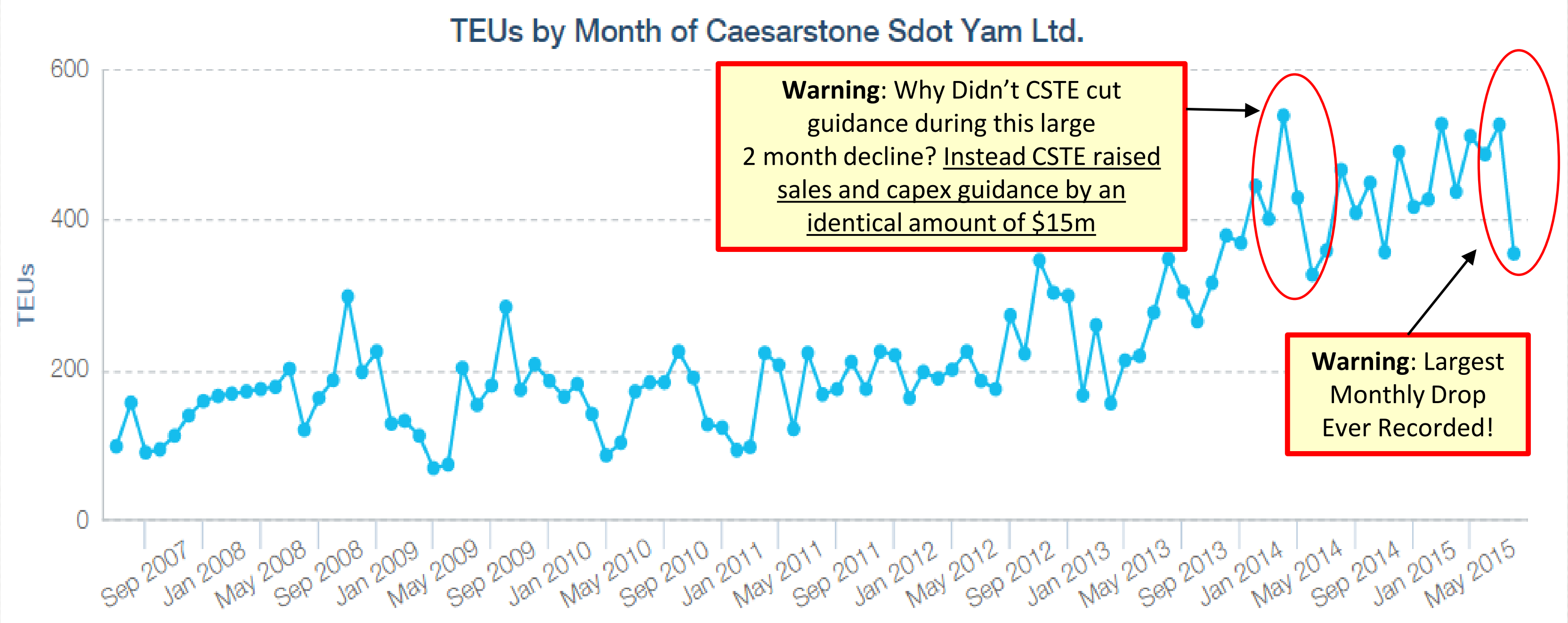
Bryan County News [Article]

Fundamental Challenges and Issues Remain

Spruce Point Capital Management

Update: Latest Import Data Signaling Massive Slowdown…

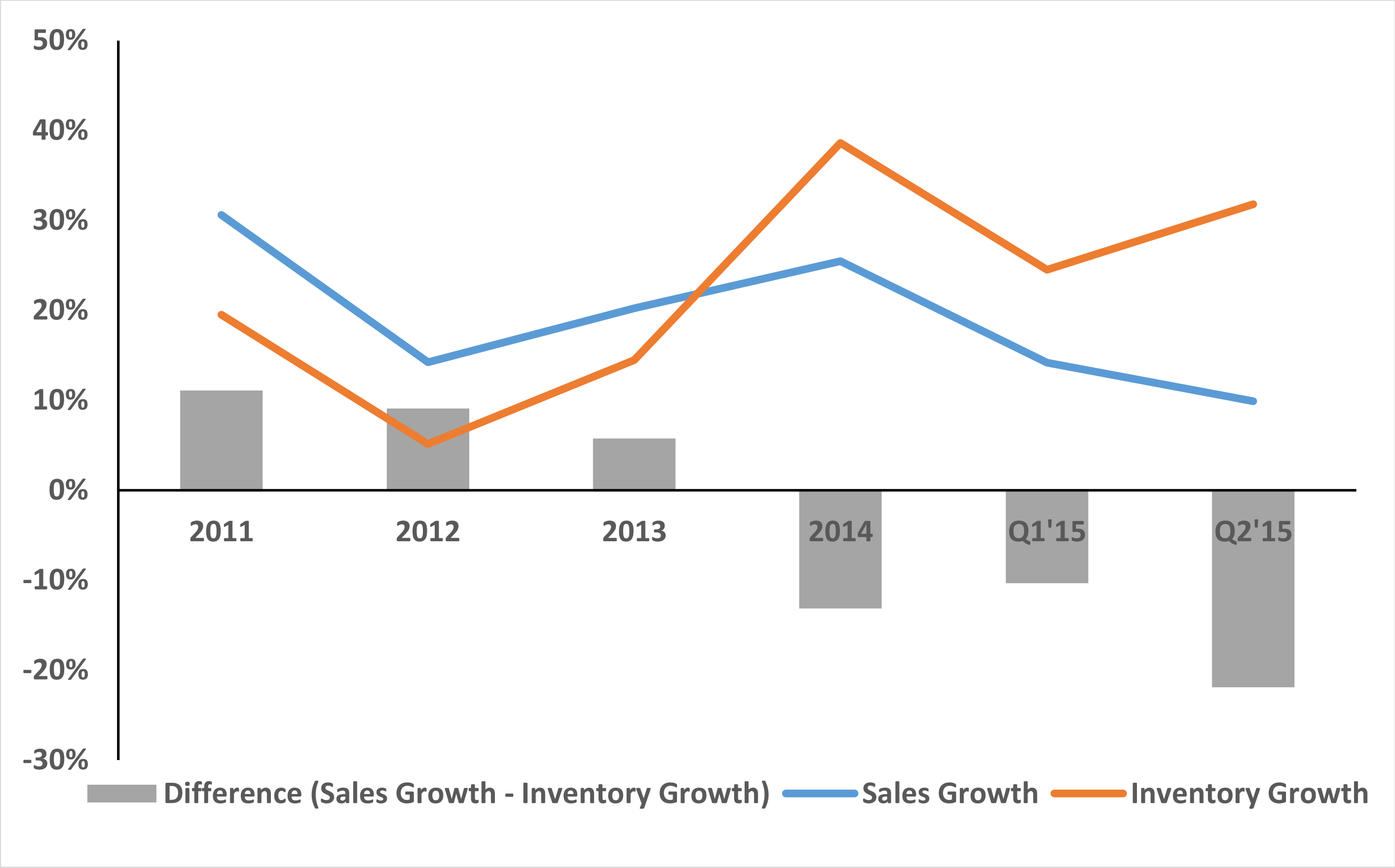
In our initial report, we argued that U.S. imports of Caesarstone were a reliable barometer of the company's quantity of slabs sold and financial performance. Caesarstone did not refute our data source or interpretation. We observe that the Company has had a dramatic slow down of imports into the U.S. in August, the largest one-month decline ever recorded and is not making up for this decline with any material domestic U.S. production. CSTE will face tough YoY comps in the coming quarter.



Source: Panjiva

CSTE Financials Suggest More Strain and Downside To Occur

Inventory Growth Outpacing Sales Growth By Widest Margin Ever



Source: Caesarstone Financials

A Second Look At The Quartz Supply Agreements, From the Volume Perspective

Previously, we pointed out that quartz price rose by approximately double the 4% rate reported by CSTE. However, looking at the quantities purchased is also insightful. Quantities purchased grew at almost half the rate of reported sales and COGS from 2012-2014.

10.5

caesarstone

February 6, 2012

To
Mikroman Madencilik Mining
Hisarardi Koyo
Yatagan Mugla
Turkey

Dear Murat, Serhat, Karabay

Following our discussions, here is a summary of our agreement re supply during 2012.

1. Quantities
Caesarstone's working plan for year 2012 is as follows:

Product		Quantity 2012 (tons)
1	2.5-4.0	1700
2	1.2-2.5	2300
3	0.7-1.2	6500
4	0.5-0.8	7800
5	0.2-0.5	15000
6	0.1-0.3	7000
7	G	7500
8	400#	20000

The above is Caesarstone's working plan with a purchases non-binding projection
"Estimated Quantities"). As always, CaesarStone will deliver to Mikroman a bindir
monthly basis, and Mikroman shall supply to CaesarStone all such Purchase Orders
Quantities.

2. Prices – during 2012 the Mikroman will charge from Caesarstone the following

fraction 0.1-4.0 – 143 US$ per ton FOB Izmir
0.062-0.2 (G) -125 US$ per ton FOB Izmir
400# (powder) – 140 US$ per ton FOB Izmir

Payment terms shall be as applied during 2011.

This summary serves as an addendum to the agreement entered between Caesars
September 27, 2010 and constitutes an integral part thereof.

If the foregoing meets with your approval and acceptance, please so in
counterparts of this Letter Agreement as provided below and return one fully exe

CAESARSTONE SDOT YAM LTD.
CaesarStone Sdot-Yam Ltd
By: Yosef Shiran
Chief Executive Officer

We hereby approve our consent to all of the above.

Mikroman Madencilik Mining
By: Murat Necmi Saran

08.02.2012
Date

Kibbutz Sdot-Yam MP Menashe 38805, Israel T + 972 4 6109 368 F + 972 4 6261 268 www.caesarstone.com

Notice total quantities of quartz ordered rose 26% From 2012-2014 (12.2% p.a), while reported COGS rose 23.5% p.a. and Sales rose 22.8% p.a. over the same period!

Confidential Treatment
Requested

4.5

caesarstone

December 19, 2013

To
Mikroman Madencilik Mining
Hisarardi Koyo
Yatagan Mugla
Turkey

Dear Murat, Serhat, Karabay,

Following our discussions, and in continuation with the Agreement entered between us on 2012 here is a summary of our agreement re supply during 2014.

1. Estimated Quantities and binding orders and supply
Caesarstone's working plan for year 2014 is as follows:

Product		Quantity 2014
1	2.5-4.0	1440
2	1.2-2.5	2000
3	[illegible]	10000
4	0.5-0.8	8000
5	0.2-0.5	23000
6	0.1-0.3	10000
7	0.063-0.2 (G)	10000
8	400#	21000

The above is Caesarstone's working plan with a non-binding purchases projection from Mikroman for year 2014 (the "Estimated Quantities") for the abovementioned products (the "Products"). Caesarstone's actual orders may significantly differ from the Estimated Quantities. As always, Caesarstone will deliver to Mikroman a binding Purchase Order on a monthly basis, and Mikroman shall supply to Caesarstone all such Purchase Orders (in accordance with the specifications set in writing by Caesarstone) up to the Estimated Quantities.

2. Prices – For quantities of the Products that shall be ordered by Caesarstone during year 2014, Mikroman will charge from Caesarstone the following prices per ton, US$170 (one hundred and seventy US Dollar), FOB Izmir.

3. Payment terms – for Products that shall be ordered by Caesarstone during year 2014 payment terms shall be the same as applied between the parties hereto during year 2013.

4. The products will be supplied by Mikroman in a timely manner and in accordance with Caesarstone's quality standards and specifications as will be updated by Caesarstone in writing from time to time, in accordance with each Caesarstone's purchase order.

5. Mikroman will maintain in confidence the terms of this agreement as well as any other confidential information of Caesarstone without time limitation.

6. This agreement and its performance will be governed by the English law and subject to the jurisdiction of the competent courts in England. Without derogating from the generality and validity of the foregoing, Caesarstone shall be entitled, at its sole discretion, to initiate legal proceedings related to this Agreement in Turkey, and in such case only same proceeding will be subject to the jurisdiction of the competent courts in Turkey.

Kibbutz Sdot-Yam MP Menashe 38805, Israel T + 972 4 6109 368 F + 972 4 6261 268 www.caesarstone.com

Source: SEC exhibit filings, received under Freedom of Information Request

Reminder: Growth Story Is Cracked, Sales and Margins To Remain Challenged

Sales Growth Unlikely to Accelerate

- **CSTE's sales growth rate has declined markedly and we believe it will continue to decline**:
  - 2012-2013: sales growth: 20%
  - 2013-2014: sales growth: 25%
  - 2015E: sales growth (per guidance): 12%
- CSTE's Q2'15 sales guidance reduction from $515-$525m to $495-$505m is the canary in the coal mine signaling further disappointments
- Disappointment comes despite the added Ikea distribution deals from 2013 and access to the DIY market
- 2016E (consensus estimate) of 18% sales growth is optimistic considering that:
  - The Chinese Yuan devaluation just made Chinese imports even cheaper
  - Canadian and Australian currencies remain under pressure (36% of sales in these countries)
  - CSTE is not levered to the multifamily housing which is a big driver of the U.S. housing cycle
  - Import data of slabs remain under pressure
  - New "super premium" category led by Dekton is being created and being marketed through the DIY channels like Home Depot
  - Questions about product quality and customer complaints remain

Margins Remain Questionable

- Despite cutting its sales guidance, CSTE maintained its EBITDA range of $123 – 129m (25.2% margin at the midpoint)
- Maintaining its EBITDA margin seems difficult in light of the following:
  - In its SEC filing, CSTE indicated it expected quartz prices to go up in 2015 by a similar amount from 2014. Based on our public access of its key quartz supply agreement, this would imply another 9.5% increase in 2015. (CSTE has not indicated it has long-term supply agreements for its new U.S. facility)
  - There is evidence of increased price competition in the quartz countertop market from new entrants at price points of 25% less. Dealer quotes support our claim of pricing pressures
  - R&D expense and margins are already razor thin. Any further cuts to R&D could sacrifice further product innovation and future competitiveness
- On the Q2'15 call CSTE explains it will get an EBITDA benefit by lowering U.S. plant start up expense from $11m to just $1.5m as a result of "less pressure to ramp up." We interpret this to mean they see weak customer demand
- As illustrated, if margins are evaluated on a constant currency basis, CSTE margins could be up to 7% less
- CSTE's Sales and Marketing margins have fallen sharply. If they don't spend more on marketing, sales growth will decline, and if they do market more, EBITDA margins will be impacted lower
- Open question remains about the degree of benefit from the related-party deals with the Kibbutz

Why Are Directors Fleeing?

Ram Belinkov Resigns

- In a 6-K filing late on September 17th, CSTE disclosed that Mr. Ram Belinkov resigned from CSTE's Board over a difference of opinion over matters related to board governance and the decision to grant the CEO stock options
- As an independent Director, his resignation put CSTE out of compliance with the Nasdaq rule requiring a Board consisting of a majority of Independent Directors
- It is noteworthy that he left the Israel Ministry of Finance in 2009 where he was a Budget Director over a difference of opinion in a budget deal
- Combine this with the fact that he is involved as a Board member with other public companies (Kafrit, Melisron), suggests he can afford to be picky with which companies he's involved with
- A quote from his former boss, Finance Ministry Accountant-General Shuki Oren said, "He (*Belinkov)* is *an honest and courageous guy who stands up for his principles*"

Source: The Jerusalem Post, Belinkov resigns
CSTE 6-K filing

Avner Naveh Resigns

- Late on Friday, September 25th after market close, CSTE filed another 6-K announcing that Mr. Avner Naveh resigned from the Board
- Mr. Naveh informed the Board that he was resigning due to a difference of opinion over matters related to the Board's work and material resolutions
- However, CSTE issued a press release giving the appearance that his resignation was primarily to regain compliance with the majority Independent Director rule. The press release did not mention any difference of opinion over Board matters
- We also observe that Mr. Naveh serves as Board member on other public companies including Ashtrom Properties Ltd and Zur Shamir Holdings Ltd

Source: CSTE 6-K filing
Caesarstone Issues Update Regarding Board of Directors

Analysts Have, And We Believe Will Continue To Be, Wrong on CSTE's Share Price

It pays to critically assess any analyst who endorses a stock and review his or her accuracy!

Stifel Nicolaus: February 26, 2015 - Buy $70 Price Target

"CSTE remains the same story today as it was when the Company IPO'd in March 2012"

"Margins have been and will continue to be buffeted by currency headwinds and the U.S. Plant expansion scheduled for 2015, but excluding these factors, margins are growing."

"We think the rare combination in building products of high growth and high returns on capital will continue for the next several years as quartz penetrates the kitchen countertop market further and CSTE takes advantage of its superior brand, product quality and distribution to grow its share"

Stifel Nicolaus: May 6, 2015 – Buy $70 Price Target

"We have no fears that the building inventory portends an issue but actually the contrary as it suggests the company is slowly getting into a better service condition that should further improve once the U.S. capacity comes on line"

"A minor disappointment was the news of an increase in the capital spending for the two lines being closer to $130 million from the previous $115 million (originally, we thought each line might be as low as $50 million of capital spending). There may be somewhat of an offset with better speeds or quality but clearly the capital being deployed is somewhat higher than previous expectations."

Stifel Nicolaus: June 17, 2015 - Buy $70 Price Target

"A compound growth rate of 30% in calendars 2015 and 2016 seems attainable and then 2017-2018 at 25% growth would put the company close to $500 million in the U.S. marketplace. We think more than half of this growth comes from the overall penetration of quartz in the U.S. marketplace and the other 30-40% will come from share gains"

Tefron Case Study: Management's Previous Failure

Caesarstone's Management Previously Worked At Tefron, An Israeli Apparel Company

If At First You Don't Succeed Selling This....

Then Try Your Luck and Expertise Selling This

Warning: Management's Previous Tenure at Tefron Ended in Failure

Key Caesarstone Members Worked at Tefron

Caesarstone CEO – Yos Shiran

Yosef Shiran has served as our Chief Executive Officer since January 2009 and serves as the chairman of our subsidiaries in the United States, Australia, Canada and Singapore. Starting from May 2014, Mr. Shiran serves as a director at Anagog Ltd., a company developing technology for parking locating and spotting. Prior to joining us, in August 2008, Mr. Shiran established operations for a company wholly-owned by him in the textile industry**. From January 2001 to August 2008, Mr. Shiran served as Chief Executive Officer and director of Tefron Ltd., an Israeli manufacturer of intimate apparel and activewear that was listed on the New York Stock Exchange and is currently listed on the Tel Aviv Stock Exchange**. From 1995 to 2000, Mr. Shiran served as Chief Executive Officer of Technoplast Industries Ltd., an injection molding and plastic extrusion manufacturing company that was listed on the Tel Aviv Stock Exchange and the London Stock Exchange.

General Counsel + VP Business Development – Michal Baumwald

Michal Baumwald Oron has served as our General Counsel since September 2009 and since January 2013, also as our Vice President Business Development. **Prior to joining us, from August 2004 to June 2009, Ms. Baumwald Oron served as Secretary and General Counsel of Tefron Ltd., an Israeli manufacturer of intimate apparel and activewear that was listed on the New York Stock Exchange and is currently listed on the Tel Aviv Stock Exchange, and from May 2003 to August 2004, Ms. Baumwald Oron served as the Legal Counsel of Tefron**.

About Tefron

Tefron Ltd. manufactures intimate apparel, active wear and swimwear sold throughout the world by such name-brand marketers as Victoria's Secret, Nike, Target, Warnaco/Calvin Klein, The Gap, Banana Republic, J.C Penny, lululemon athletica, Puma, Patagonia, Reebok, Swimwear Anywhere and El Corte Englese, as well as other well known retailers and designer labels. Through the utilization of manufacturing technologies and techniques developed or refined by us, we are able to mass-produce quality garments featuring unique designs tailored to our customers' individual specifications. Our product line includes knitted briefs, bras, tank tops, boxers, leggings, crop, T-shirts, day-wear, nightwear, bodysuits, swimwear, beach-wear, active-wear and accessories

Guess Who Audited Tefron…CSTE's Auditor!

Kost Forer Gabbay & Kasierer
2 Pal-Yam Ave.
Haifa 33095, Israel
Tel: 972 (4)8654000
Fax: 972(3) 5633443
www.ey.com.il

Source: SEC filing

Tefron Stock Performance Foreshadowing Future CSTE Performance?

During CEO Shiran's tenure at Tefron, the stock fell over >85% from its 2006 highs after margins peaked, problems emerged, and he liquidated stock

Source: Bloomberg

Follow Insider Money At Caesarstone Very Carefully….

CSTE's Financials Appear Held Together Long Enough To Allow its CEO and Big Shareholder To Sell

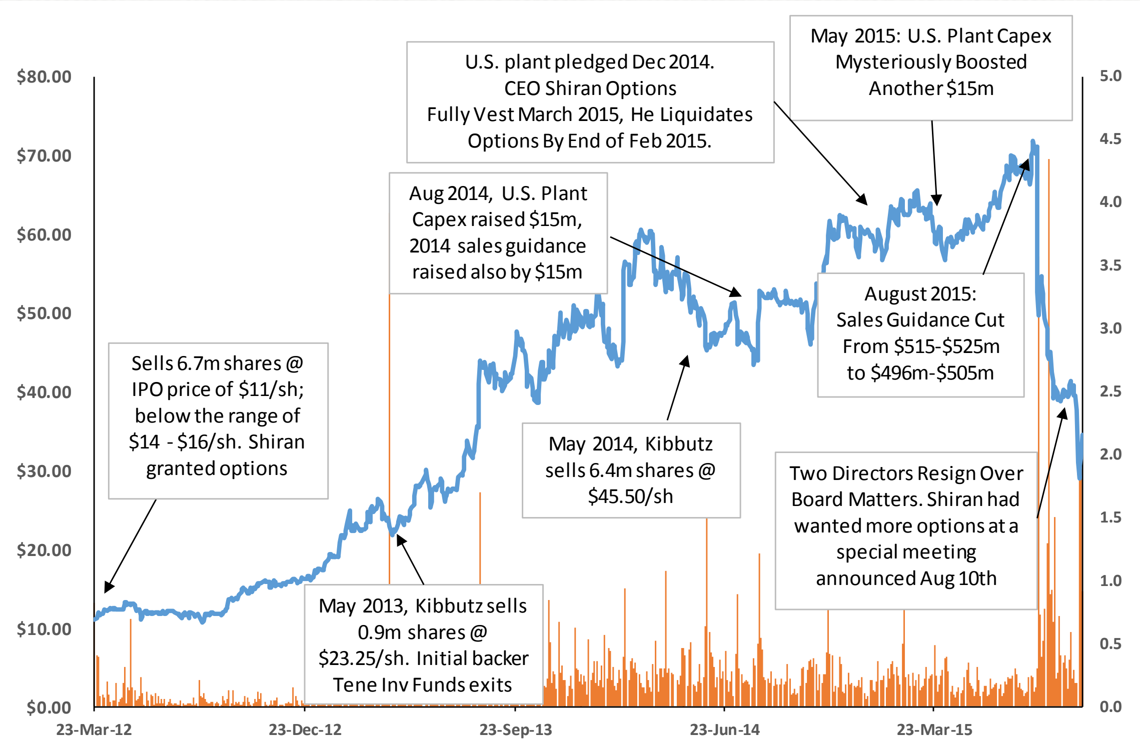
In March 2012, we granted to Yosef Shiran, our Chief Executive Officer, options to purchase ordinary shares equal to 2% of the number of our shares immediately outstanding following the pricing of our IPO in consideration for serving as a director and chairman of the board of directors of our subsidiaries in the United States, Canada, Singapore and Australia. The exercise price of the options was equal to $11.00, the IPO price per share. Additional options, totaling 19,980 shares, were issued after the exercise of the IPO's over-allotment option by the underwriters, with an exercise price of $11.00.

The options vest in 12 equal installments beginning on March 31, 2012, and subsequently, at the end of each quarter for 11 quarters, provided the services agreement between us and our CEO is in effect. All unvested options will vest automatically upon a change of control (as defined in the award agreement), the sale of all or substantially all of our assets, or in the event that Kibbutz Sdot-Yam's holdings in us decrease below 50% of our outstanding shares. Any additional benefits granted under options awarded to our other employees will apply to our CEO's options as well. **As of April 30, 2014, Yosef Shiran held 229,102 options.**

Source: 2013 20-F, page 70

As of February 28, 2015, Yosef Shiran, our Chief Executive Officer, did not hold any options. The grant of new options to Yosef Shiran, our Chief Executive Officer, is subject to the approval of 75% of our board members in office, in addition to any approvals required under the Israeli Companies Law.

Source: 2014 20-F, page 70



Key Events And CEO Quotes At Tefron Leading Up To The Collapse

Date	Event	Key Company and Yos Shiran Quotes
3/9/2006	Q4'2004 / 2005 Earnings	"Our cooperation with and sales to Nike grew substantially in 2005. Our relationship with Nike over 2005 became closer and broadened to a new level, and is an example of how our loyalty, commitment and dedication to our customers can be realized." "Moving into 2006, we are well positioned to build on our growth strategy. We intend to continue expanding our relationships with our existing customers and reach new value driven customers. We intend to expand our product lines while entering into new categories and increase the visibility of our (EFP TM) technology. "
5/8/2006	Asia JV announced and Q1'2006 Earnings	"Our first quarter results reflect strength in our active-wear and swimwear product lines in accordance with our strategic plan. We are looking for a significant increase in our active-wear revenues in the second half of the year as we work to further expand our product lines while entering into new categories and increase the visibility of our EFP(TM) technology." "**This JV marks our entrance into the Asian market, and in particular, the fast growing Chinese market**. The joint venture provides us with facilities, manpower, management and infrastructure in China. It also provides us with an existing sales and distribution channel through a leading brand. **We see significant long-term potential in this joint venture**."
5/9/2006	Stock Liquidation	Tefron's major shareholders, Norfet Limited Partnership (which is controlled by FIMI Opportunity Fund L.P. and by FIMI Israel Opportunity Fund L.P.) and Macpell Industries Ltd., and Tefron's Chief Executive Officer, Yos Shiran, had sold an aggregate of 2 million of their ordinary shares to Clal Finance Bitucha Ltd. For a price of NIS 53.34 (approximately $12) per share. Of the 2 million shares sold, 1,050,000 shares were sold by Norfet Limited Partnership, 800,000 shares were sold by Macpell Industries Ltd. and **150,000 shares were sold by Yos Shiran** following his exercise of 150,000 options to acquire shares.
8/8/2006	Q2'2006 Earnings (Hint of Issues and reasons why Tefron Could Disappoint)	"Most significantly, the increase in our revenues compared with the comparable period of last year was across all of our product lines and was accompanied by an improvement in both our gross and operating margins. Our swimwear product line performed stronger than we had expected in the first half of the year. As we move beyond the summer, we expect sales of swimwear to significantly subside in the third quarter and to increase again in the fourth quarter of 2006, due to the seasonality of the swimwear business." "To date, the (Israel) conflict, which has mainly affected the northern part of the country, has had a limited effect on our ongoing business and operations which are primarily located in northern Israel. **However, there is a possibility that the ongoing conflict will not allow us to fully increase production to meet the growing demand we are seeing in our active-wear product line**, which is beyond our original plans for the third quarter. We believe that we will achieve our previously announced target for 2006 of mid-teen percentage growth in revenues and profitability levels higher than those of 2005, at around the levels seen in the fourth quarter of 2005."
8/9/2006	Tefron Buys Director and Officer Liability Insurance	"Tefron Ltd. (the "Company") today announced that the Company's Board of Directors approved on August 8, 2006, **following the approval by the Company's Audit Committee, the purchase of a new directors' and officers' insurance policy, which will also cover directors who may be deemed to be controlling shareholders of the Company**. The insurance policy will include directors and officers of the Company's subsidiaries and will have a term of one year. Such policy covers an aggregate liability of US $15,000,000. The premium to be paid by the Company with respect to such insurance policy is approximately US $162,000."
8/9/2006	Tefron Corrects "Errors"	"Tefron today announced **corrections to its Sales by Segment table in its second quarter earnings release issued yesterday. The corrections relate to the sales by segment for the three months ended June 30, 2005 and for the six months ended June 30, 2005**. A corrected Sales by Segment table is attached as Table 1."

Key Events and CEO Quotes At Tefron Leading Up To The Collapse (Cont'd)

Date	Event	Key Company and Yos Shiran Quotes
1/23/2007	First SEC Comment Letter Revealed	"As requested, in future filings **we will revise to clarify, if true, that our officers concluded that our disclosure controls and procedures were also effective to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms**. We will also expand our disclosure to indicate that disclosure controls and procedures included, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports that we file or submit under the Act is accumulated and communicated to our management, including our principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure."
2/20/2007	Q4 and FY 2006 Earnings	"**Active-wear sales were below our initial expectations for 2006 due to a shift in timing of product flows by Nike**. **We anticipate a temporary decline in active-wear sales in the first half of 2007, and a strengthening of active-wear sales in the second half of 2007 as Nike introduces its next generation of performance apparel**. **We believe our relationship with Nike is strong**, and it remains a central part of our strategy driving our long-term growth in the active wear." "Overall, in the first half of 2007 we expect to see a slight decline in revenue as compared to the first half of last year due to the anticipated decline in active-wear revenue. Additionally, we expect a temporary reduction in operating margins in the first half of the year as compared with the first half of last year, given the ongoing weakness of the dollar versus the Israeli shekel, as well as pricing pressure in older collections of our intimate apparel product line"
4/23/2007	Director Wolfson Resigns, Sells Stock	"Arie Wolfson has resigned from the board of directors of the company. Mr. Wolfson owned shares of Tefron through his shareholding in Macpell Industries Ltd., a company publicly traded on the Tel Aviv Stock Exchange, where he also served as an officer. On April 19, 2007, Macpell announced that it had sold all of the 2,852,810 shares it held in Tefron. Accordingly, the shareholders agreement between Norfet, Macpell and Arwol was terminated." (**Note: Wolfson elected to Board at same time Kost Forer & Gabbay of E&Y appointed auditor according to a press release**)
5/7/2007	Q1'2007 Earnings	"We continue to believe that revenues for the year will be higher than those of 2006 as a result of the expected growth in active-wear sales in the second half of the year. We expect our second quarter revenues to decline in approximately 12% compared to the second quarter of 2006 **due to the anticipated temporary reduction in active-wear sales**. **We also expect a strengthening pressure on our operating margins given the ongoing weakening of the US Dollar versus the Shekel and the pricing reduction in older collections of our intimate apparel product line**. To mitigate these effects we intend to continue to transfer labor intensive production processes offshore
7/5/2007	Mid Quarter Earnings Guidance Cut	"Tefron expects, based on preliminary data, second quarter revenues of approximately $40.5 million, representing an approximately 19% decrease from second quarter 2006 revenues of $49.7 million. **The expected decrease is due mainly to lower than anticipated active-wear and intimate apparel sales. Tefron expects that third quarter revenues will further decline due to a delay in active-wear orders, as well as the seasonal reduction in sales of its swimwear product line**"
11/15/2007	JV Failure Admission and Q3'2007 Earnings	"**Tefron also announced that its contemplated joint venture in China with Langsha Knitting Co. Ltd. and Itochu Corporation has been terminated due to lack of progress with the Chinese partner**." "**The third quarter, in which we reported lower revenues and an operating loss, was a tough one for Tefron**.... With regard to the fourth quarter, we now expect active-wear sales to remain at similar levels seen over the last few quarters. A large portion of these sales will be derived from our Cut & Sew division's 'new generation' Nike products, which have a relatively lower profitability than those of the Seamless active-wear products. However, we have started manufacturing seamless products for the 'new generation' which will mostly be shipped next year, and we are very excited with the prospects of this project. These products are technologically advanced, and they have created short-term manufacturing challenges for us..."

Spruce Point Capital Management

Key Events and CEO Quotes At Tefron Leading Up To The Collapse (Cont'd)

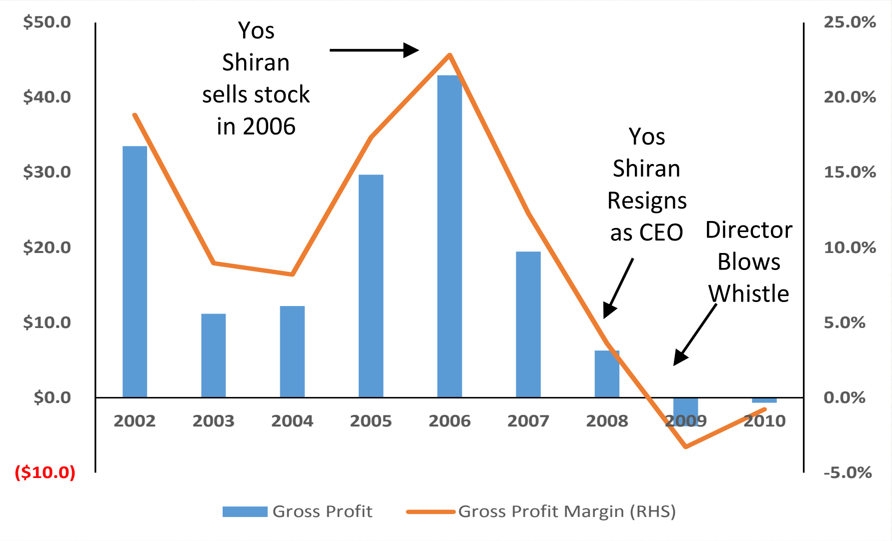
Date	Event	Key Company and Yos Shiran Quotes
12/27/2007	Board Changes	Mr. Yacov Gelbard, former CEO of the Bezeq Group, appointed as active Chairman of the Board of Directors**. The Company also announced that Mr. Yarom Oren is replacing Mr. Gillon Beck as a member of the Company's board of director**
2/28/2008	Q4'2008 and FY 2008 Earnings	"We faced a tough fourth quarter, particularly from a profitability standpoint. **The primary cause was the weak US dollar, coupled with our Hi-Tex division manufacturing hurdles**. **While we are improving our ability to overcome these hurdles, we do expect them to continue into the early part of 2008**." "We are currently working diligently to formulate a strategic and operational plan, together with the support of our new chairman, Mr. Yaacov Gelbard, intended to grow our revenue base, improve our operating efficiencies, while reducing our costs"
5/15/2008	Q1'2008 Earnings	"While we are pleased with our increase in revenues, **we still presented a net loss, mainly due to the weak US dollar against the shekel and manufacturing hurdles at our Hi-Tex division**. We are currently focusing our efforts on overcoming these hurdles and reducing our operational costs. In the next few months, we aim to finalize the operational plan that we discussed in the prior quarter, and we expect to continue implementing the plan in the second half of the year."
7/23/2008	Yos Shiran Resigns	"**Mr. Yos Shiran, the Company's CEO for the last seven and a half years, has notified the Company of his decision to resign as the CEO and as a director of the Company in favor of pursuing other business opportunities**. Mr. Shiran's resignation as CEO will take effect in 90 days. His resignation as a director of the Company is effective immediately."
6/22/2009	Director Resigns and Blows Whistle	"Tefron announced the resignation of Mr. Micha Korman from the Board of Directors of the Company effective immediately. Mr. Korman served as a director of the Company since October 2002. **Mr. Korman has raised claims regarding the conduct of the management of the Company and the communication between management and the Board of Directors of the Company**."

Follow the Gross Margins and Capital Expenditures Carefully…

- Tefron IPO'ed and was listed on the NYSE in 1997. An article in Fortune from 2000 entitled "*This Entrepreneur is Changing Underwear*" highlighted some of the stock's selling points such as fast revenue growth and marquee customers such as Victoria Secret, Calvin Klein and Target. The article also highlighted the upside from a patent application for a seamless bra that it called "revolutionary"
- Tefron would make numerous acquisitions and investments to expand in the U.S. such as Alba Waldenstein (Tefron USA, 1999), Macro Clothing (2003), Sports Innovation Division (2004) and Excelsior (2008)
- Margins would peak in 2006, which coincided with a well time stock offering by major investors, including the CEO Yos Shiran. Gross margin expansion was cited due to "*mix of higher margin products and improvements in operating efficiencies*"
- Sales plunged starting in 2007 as major customer orders ceased, and Tefron admitted that it had manufacturing issues and a cost structure was too high in relation to its competitors
- **It is noteworthy that Tefron consistently misguided its expectations for capital expenditures each year from 2003 – 2010**. Director Korman questioned management's budgeting process and communication with the Board in 2009; his warning appears to have been warranted

Tefron Gross Margins Collapse

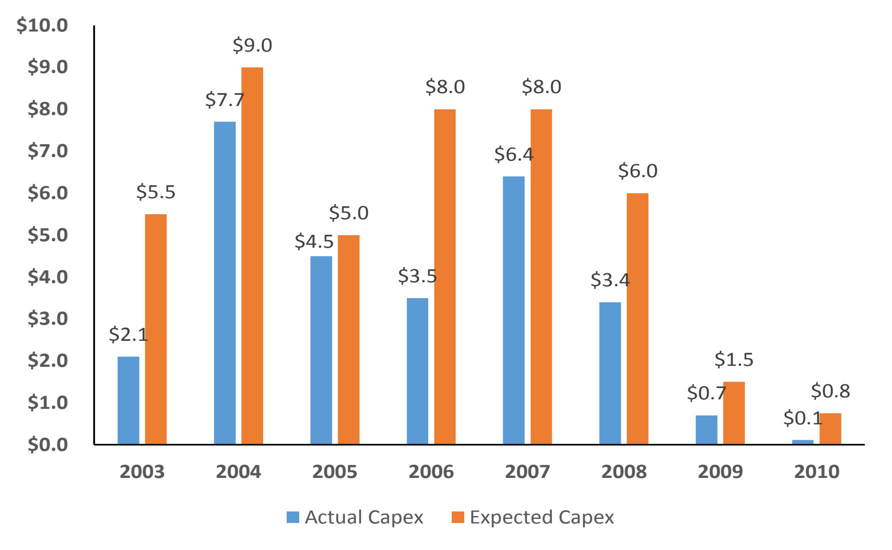
$ in millions



Note: Capex net of grants from State of Israel
Source: Tefron SEC Filings

Tefron Consistently Misguided Capex Forecast

$ in millions



% overestimate: 162% 17% 11% 129% 25% 76% 114% 564%

Note: Expected capex for 2002, 2008-2010 listed at the midpoint of the guidance range from the 20-F Annual Reports filed with the SEC

Tefron's Failure Attributed to Poor Management, Quality Control Issues

Poor Management, Quality Control, and Execution Blamed For Tefron Failure

Tefron moves seamlessly towards profit

January 1, 2012

Amit Meridor, CEO of the seamless clothing manufacturer, tells "Globes" that Tefron is well on the road to recovery.

A few minutes before we begin the interview with Amit Meridor, Tefron Ltd. (Bulletin Board: TFRFF; TASE:TFR) CEO for the last two years, we get a glimpse of a small display of clothing produced by Tefron, which helps us understand what separates it from other Israeli textile companies, what destroyed it three years ago, and what helped it recover over this past year.

Tefron went through the greatest crisis in its history three years ago. Poor management, which was exacerbated by the credit crisis, nearly drove the company to the brink of insolvency. Revenue fell, losses piled up, and the bank debt remained the same.

"**Tefron's main problem was execution, similar to many other Israel start-ups," Tefron CEO Meridor, 50, says, "Tefron developed and manufactured products, but crashed due to quality control and delivery problems**. In 2009, for example, we paid $9 million in late fees for merchandise that failed to reach customers in the US on time. This was the company's sickness, a problem that has existed from the start. Last year, we only paid a few hundred thousand dollars in late fees, which is a significant change. Tefron is finally doing what it promised to do, and is very cautious in its commitments.

Source: Israeli Globe Article

Updated Valuation

Analysts Fail to Adjust For Seriousness of Silicosis Liability

TV Program In Israel Highlights Severity of Caesarstone Silicosis Issue

Source: Youtube video
Rough Translation available here on 9/28/15

Material Potential Impact to EPS From Silicosis Liability Payout

$ in millions

	Range of Silicosis Liability Payouts				
Silicosis Liability	$20.0	$40.0	$60.0	$80.0	$100.0
Insurance Coverage	($20.0)	($20.0)	($20.0)	($20.0)	($20.0)
Earnings Hit	$0.0	$20.0	$40.0	$60.0	$80.0
Tax Rate	15%	15%	15%	15%	15%
After Tax Impact	$0.0	$17.0	$34.0	$51.0	$68.0
Shares outstanding	35.4	35.4	35.4	35.4	35.4
Per Share Impact	$0.00	$0.48	$0.96	$1.44	$1.92

Source: Caesarstone 20-F, Spruce Point estimates

Downgrading Price Target

Given our grave concerns about the integrity of Caesarstone's financials, management's past results at Tefron, recent director resignations, weak US import data, and declining FX rates (Australian and Canadian Dollar), we are downgrading our price target.

$ in millions

	2016E EV/EBITDA Multiple Range		
	6.0x	**--**	**8.0x**
EBITDA Margin Range	10%	--	20%
2016E Sales	$525.0	--	$525.0
% growth	5.0%		5.0%
Estimated EBITDA	$52.5	--	$105.0
Implied Enterprise Value	$315.0	--	$840.0
Less: Listed Debt	($20.0)	--	($20.0)
Less: Potential Silicosis Liability	($34.0)	--	($34.0)
Plus: Cash	$37.6	--	$37.6
Equity Value	**$298.6**	**--**	**$823.6**
Shares o/s	35.4	--	35.4
Price Target	$8.43	--	$23.24
% Downside	-76%	--	-33%

Note: Illustrative valuation with Spruce Point estimates

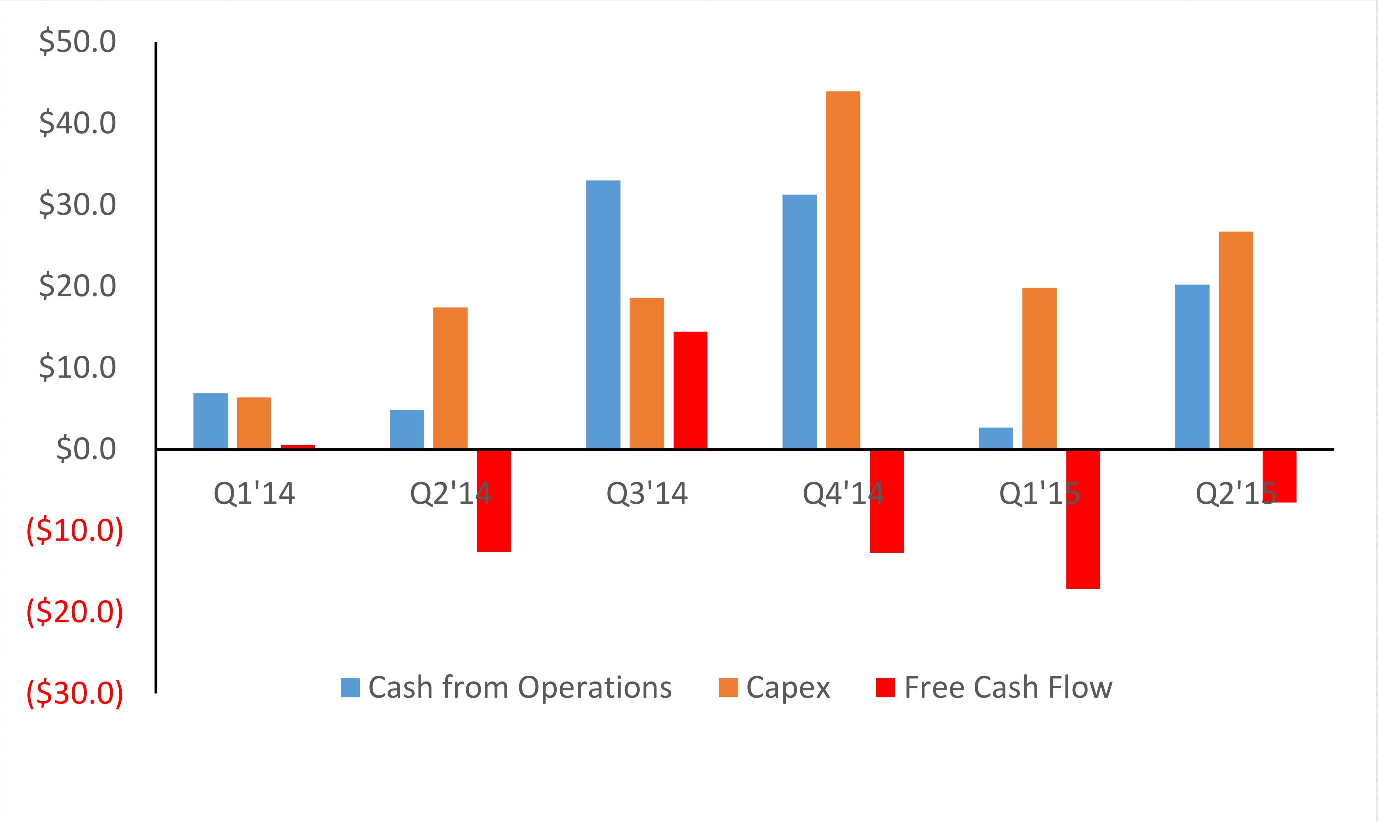
Wall St. Analysts expect 18% revenue growth next year, but we believe it to be optimistic. We estimate revenue growth will be ~5%. Based on dealer conversations, we believe CSTE has tried to historically increase prices 2-3% annually. We believe they get modest 1-2% volume growth in line with world GDP. In our opinion, EBITDA might be overstated by up to $30m from over capitalization of expenses

Wall St. Analysts fail to adjust CSTE's valuation for the likelihood of a large payout due to silicosis liabilities. If we take management's estimate for $56m of liability from the class action lawsuit (less $20m insurance coverage), we assume $34m of incremental liabilities

Key to Evaluate CSTE on a Free Cash Flow Basis

Given our concerns that CSTE's capital expenditures may be artificially high, it is important to evaluate its financial performance on a Free Cash Flow (CFO-capex) basis. We find that CSTE's Free Cash Flow has been flat/negative in 5 of the last 6 quarters.

$ in millions



Source: CSTE Financials