

Ranbaxy Laboratories

STOCK INFO.	BLOOMBERG
BSE Sensex: 8,377	RBXY IN
	REUTERS CODE
S&P CNX: 2,537	RANB.BO

13 October 2005

Sell
Rs458
Previous Recommendation: Sell

Equity Shares (m)	371.1
52-Week Range	650/437
1,6,12 Rel. Perf. (%)	-15/-37/-62
M.Cap. (Rs b)	170.1
M.Cap. (US\$ b)	3.8

YEAR END	NET SALES (RS M)	PAT (RS M)	EPS (RS)	EPS GROWTH (%)	P/E (X)	P/BV (X)	ROE (%)	ROCE (%)	EV/ SALES	EV/ EBITDA
12/04A	54,220	7,279	19.6	-0.9	23.4	6.8	29.1	27.7	3.3	18.1
12/05E	53,884	4,716	12.7	-34.0	35.8	6.3	19.4	19.2	3.3	27.5
12/06E	65,083	7,490	20.1	58.8	22.5	5.6	27.1	26.1	2.7	17.9

Ranbaxy loses key Lipitor Patent challenge in UK

The UK lower court upheld the '633 patent and invalidated the '281 patent on Pfizer's Lipitor. Ranbaxy had challenged both the patents. The company needed to win both the patent challenges for a successful launch in UK. The court ruling will prevent a UK launch for Ranbaxy till 2011 as well as erode investor sentiments regarding the outcome of the litigation in the US lower court. Ranbaxy is currently valued at 35.8x CY05E and 22.5x CY06E consolidated earnings (excluding upsides from patent challenges). Despite a correction of 7% today, we believe that valuations are rich since the potential upsides from generic Lipitor have been partly factored into current valuations. With the UK court ruling going against Ranbaxy, we believe that the stock price will "shed" the Lipitor premium. Long-term valuations will hinge on the outcome of the patent litigation in USA. We re-iterate our **Sell** recommendation on the stock.

Impact for UK market: Ranbaxy had to win both the patent challenges for a successful launch of generic Lipitor in UK. Based on the latest ruling, Ranbaxy will not be able to launch generic Lipitor in UK till 2011 (unless it wins in the appeals court). Lipitor generated revenues of about USD450m in UK.

Impact for US market: Lipitor commands revenues of USD8b in US and is the most important market for the Lipitor franchise. Past precedents suggest that court rulings

on patent challenges vary from country-to-country. Hence, the UK court ruling will not have any bearing for the US lower court ruling, which is expected by December 2005.

There have been unconfirmed rumours of a possibility of an out-of-court settlement between Pfizer and Ranbaxy regarding Lipitor patent challenge. A successful UK court ruling may have improved the probability of such a settlement. However, since the UK court has ruled against Ranbaxy (for the '633 patent), the probability of the out-of-court settlement has reduced. **We do not completely rule out the possibility of such a settlement since court verdicts can differ from country-to-country. But, the UK ruling clearly weakens Ranbaxy's positioning.**

UK patent ruling

In UK, the '633 patent is the compound patent claiming the active ingredient in Lipitor (i.e. Atorvastatin) while the '281 patent claims the calcium salt of Atorvastatin. We believe that the '633 patent is more important since it claims the active ingredient and expires in UK in Nov-2011. The '281 patent expires in 2010. In giving his judgment, the judge indicated that the '281 patent was not valid on grounds of "anticipation and obviousness". Both Ranbaxy and Pfizer have indicated that they will appeal the ruling for the '633 patent and '281 patent respectively. The decision of the appeals court is expected in 2006.

In USA, Ranbaxy has challenged Pfizer's '893 patent (known as '633 in UK) & '995 patent ('281 in UK). The '893 patent expires in 2010 and the '995 patent expires in 2011 in USA. Ranbaxy will have to win both the patent challenges for a successful launch. Both the above patents cover Atorvastatin Calcium as a molecule. While the '893 patent encompasses a class of compounds including the Atorvastatin (Lipitor) molecule (i.e. it is the compound patent), the '995 patent encompasses the single enantiomer version of Atorvastatin Calcium.

Ranbaxy is asserting the following in USA:

- 1) The extension (from 2006 to 2010) of the '893 patent was improperly granted.
- 2) Invalidity and double patenting or obviousness of the '995 patent.

Ranbaxy would need to successfully litigate both the '995 and the '893 patent to launch a generic version of Lipitor.

Valuation and Outlook

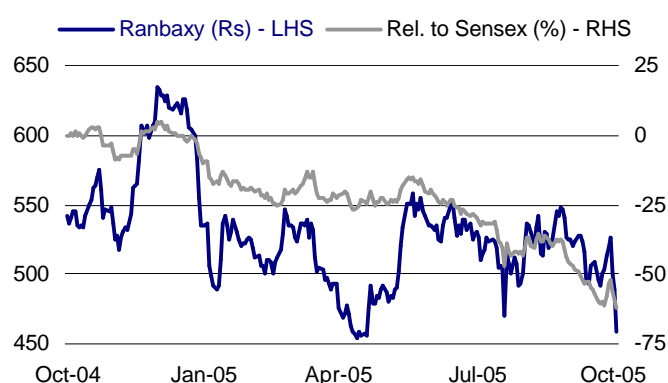
Ranbaxy had guided top-line growth in single digits and a decline in bottom-line for CY05E. It has indicated that H2CY05E will be better than H1CY05E due to new launches in USA and EU. We forecast revenue growth of 3% for CY05E and 20% for CY06E. The growth in CY06E will be led mainly by the launch of Simvastatin and Pravastatin in the US markets, which are likely to record revenues of USD60m. The low-base effect of CY05E will also help in showing higher growth for CY06E.

We expect Ranbaxy's earnings to record a de-growth of 34% for CY05E (estimated EPS of Rs 12.6 excluding upsides from uncertain events like patent challenges, technology licensing and NCE licensing). We have downgraded our CY05E earnings by 22% and our CY06E earnings by 4.5% to reflect the intense pricing pressure in the US generics market, which we believe will continue

for some more time. We expect a 59% growth in earnings for CY06E to Rs20.1 as large products like Simvastatin and Pravastatin are expected to be launched in the US generics market in CY06E. Our estimates for CY06E do not include upsides from patent challenges.

We believe that, given its strong product pipeline, Ranbaxy is well positioned to exploit the potential of regulated generic markets in the long-term with about USD40-50b worth of drugs going off-patent over the next 4 years. At 35.8x CY05E and 22.5x CY06E earnings, it is a typical case of a good business being available at rich valuations. We believe that risks are increasing in the generics space for Ranbaxy with innovator companies vigorously defending their patents, making IPR related upsides for generic companies more uncertain than ever. The recent consolidation in the global generics industry (Teva taking over Ivax and Sandoz taking over Hexal/Eon) has significantly widened the gap between these top two players and other generic companies including Ranbaxy. We expect further consolidation in the generics space and do not rule out Ranbaxy aligning itself with another large generic player to gain critical mass. This may force it to acquire assets at high valuations, which may dilute returns for existing investors. We re-iterate our **Sell** recommendation on the stock despite the recent correction in the stock price.

STOCK PERFORMANCE (1 YEAR)



N O T E S

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Disclosure of Interest Statement**Ranbaxy Laboratories**

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| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |

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