

## Dishman Pharmaceuticals and Chemicals Ltd (Q3FY07)

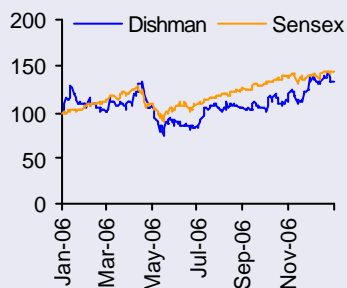
### Recommendation Maintain BUY

CMP	Rs249
Target Price	Rs286
Upside	14.9%
52 Week H/L	Rs266/Rs118
Average Volumes	1,18,936
Market Cap	Rs2bn
Face Value	Rs2
BSE Code	532526
NSE Code	DISHMAN
Bloomberg	DISH@IN
Reuters	DISH.BO

### Share holding pattern

Dec '06	(%)
Promoters	71.18
Institutions	23.46
Public	3.24
Others	2.12

### Share price chart



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**Dishman Pharmaceuticals and Chemicals Limited's (Dishman) Q3 FY07 results were in line with expectations. Sales recorded a growth of 181% to Rs1.7bn driven by CRAMS which includes the full impact of Carbogen Amcis (CA-sales Rs820mn) for the first time. Sales for EM (Eposartan Mesylate) to Solvay are back on track after a sluggish H1 FY07 and on target to record Rs1bn for FY07. Operating profit margin (OPM) declined by 110bps to 28.2% as CA has lower margins as compared to other business segments of Dishman. Consolidation of CA which has led to higher depreciation and interest outgo restricted PAT growth to 25% to Rs244mn, translating into an annualized EPS of Rs12 on a fully diluted basis.**

**Post result conference call with the management has further reaffirmed our view that Dishman would be one of the best bets in the growing outsourcing space. Starting with Solvay as its only client in 2003, Dishman has made significant progress in this space, emerging as a preferred supplier for big pharma companies (GSK, Merck, Krka, AZN, Sanofi Aventis). CA business is gaining increasing momentum surpassing its own estimates for CY06. With capacity at Amcis nearing saturation, a few customers have expressed an in principle approval to shift operations to Dishman India. This we believe is a very positive sign for both Dishman and the industry at large as it shows confidence in Dishman's IPR adherence.**

**Apart from CRAMS, Dishman has also made significant progress in the Electrolyte QUATs business and has signed a couple of long term contracts with global majors. One contract with Ferro Corporation worth US\$6mn annually is progressing smoothly. In addition, Dishman has broadened its top management by appointing a COO and a CFO, which indicates robust growth in the years to come.**

**We are very positive on Dishman's CRAMS strategy and believe Dishman will be able to leverage strongly on the relations developed with big pharma companies in CRAMS. At Rs250, the stock is trading at 22.7x FY07E EPS of Rs11 and 14.9x FY08E EPS of Rs16.8. We maintain BUY with a target price of Rs286 based on 17x FY08 earnings.**

### Financial highlights

Period to (Rs in mn)	FY04 (12)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
Sales	1,686	1,873	2,774	5,581	8,722
Growth (%)	41.3	11.1	48.1	101.2	56.3
APAT	202	322	508	893	1,363
Growth (%)	29.5	59.4	57.8	75.7	52.7
OPM (%)	24.6	26.9	23.3	22.5	23.5
ROCE (%)	20.3	16.9	11.7	13.3	16.7
EPS (Rs)	3.9	4.7	7.4	11.0	16.8
P/E	63.7	53.2	33.7	22.7	14.9
EV/EBIDTA	32.0	34.1	23.7	14.5	9.5

### Sales driven by increasing traction in CRAMS

Dishman witnessed a strong Q3 with sales growing by 181% yoy (48.5% qoq) to Rs1.7bn. Sales reflect for the first time full impact of Carbogen Amcis (CA) acquisition. CA recorded sales of Rs820mn as compared to Rs520mn in Q2 FY07 (40 days of operations). Sales to Solvay were also back on track after a sluggish H1FY07 which was impacted due to deferment of shipment of starting material of EM. Marketable Molecules segment recorded a growth of 71% to Rs340mn driven by higher volumes in the international market. Dishman's contract to supply electronic QUATs to Ferro worth US\$6mn annually is progressing smoothly. Dishman highlighted signing a contract with Nippon Kasei valued at US\$5.5mn spread over the next two quarters.

### Revenue breakup (Rs mn)

Period to	Q3 FY07	Q3 FY06	% growth	9M FY07
Contract Manufacturing	900	290	210.3	2,075
Contract Research	500	130	284.6	658
CRAMS	1,400	420	233.3	2,733
MM	340	199	70.9	1,078
Total	1,740	619	181.1	3,811

Source: Company

### Margin decline due to consolidation of CA with Dishman

Operating Profit Margin (OPM) declined by 110bps to 28.2% on account of consolidation with CA, which has lower margins than Dishman's base business. CA has OPM of 19% on account of lower capacity utilization at Carbogen. However with the integration with Dishman, margins are expected to improve to 23.5% by FY08.

### Declining margins, higher interest and depreciation cost restricts profitability growth

Interest cost and depreciation cost increased substantially on account of full impact of consolidation with CA. In addition, commissioning of the R&D centre also increased depreciation. Consequently profitability growth was restricted at 25% to Rs244mn, translating into an annualized EPS of Rs12 on a fully diluted basis. For 9M FY07, annualized EPS stood at Rs9.9.

### Other Highlights

- √ Dishman is in talks with 3 CA customers to source Hi Potent API's from India due to capacity constraints at Amcis. This Hi-Po plant could be amongst the very few plants in India which will have capacity greater than Amcis.
- √ Dishman's other contracts are gaining scale with major MNC's like Sanofi Aventis, GSK, Novartis looking at signing contract manufacturing deals with the company.
- √ Dishman is likely to incur capex of Rs1bn for FY08. This will include setting up a Hi-Po plant in India and capacity expansion at CA.
- √ The company is venturing into the Japanese market by tying up with a local player. Dishman's role would be to supply low end APIs and the technology to manufacture the same. Japan is likely to contribute from FY09.
- √ Saudi Arabia JV is progressing well and the company has been allotted 35,000 sq. ft. of land. The proposal has also been cleared by the government. Revenue from this JV is likely to start in FY08.
- √ Shifting of low end QUATS to China is on track. Commercial production is likely to start by Dec 2007 and full impact would be realized in FY09. High end QUATS would be manufactured in India.

**Quarterly Financials**

Period to (Rs mn)	Q3 FY07	Q3 FY06	% change	9M FY07	9M FY06	% change
Net sales	1,737	619	180.6	3,728	1,914	94.8
Expenditure	(1,248)	(438)	184.9	(2,793)	(1,446)	93.2
Operating Profit	489	181	170.2	936	468	100.1
Other Income	34	44	(22.7)	110	99	11.1
PBDIT	523	225	132.4	1046	567	84.6
Interest	(72)	(1)	-	(118)	(42)	181.0
Depreciation	(156)	(27)	477.8	(232)	(77)	201.3
PBT	295	197	49.7	696	448	55.4
Tax	(51)	(3)	-	(98)	(24)	308.3
PAT	244	194	25.8	598	424	41.1
OPM	28.2	29.2	-	25.1	24.5	
Equity	137.6	138.1		137.6	138.1	
EPS	14.2	11.2		11.6	8.2	
P/E@250	17.6			21.6		

## Financials

### Projected Income Statement

Period to (Rs in mn)	FY04 (12)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
Net Sales	1,686	1,873	2,774	5,581	8,722
Operating expenses	(1,271)	(1,369)	(2,129)	(4,325)	(6,673)
Operating profit	415	504	645	1256	2049
Other income	21	28	79	140	87
PBIDT	436	532	724	1396	2136
Interest	(127)	(110)	(60)	(157)	(232)
Depreciation	(76)	(83)	(122)	(274)	(390)
Profit before tax (PBT)	233	339	542	965	1,514
Tax	(26)	(7)	(34)	(72)	(151)
Profit after tax (PAT)	207	332	508	893	1363
Extraordinary / prior period items	(5)	(10)	0	0	0
Adjusted profit after tax (APAT)	202	322	508	893	1,363

### Projected Balance Sheet

Period to (Rs in mn)	FY04 (12)	FY05 (12)	FY06P (12)	FY07P (12)	FY08P (12)
<b>Sources</b>					
Equity Share Capital	103	137	137	162	162
Reserves & Surplus	561	1,334	1,747	2,563	3,836
Net Worth	664	1,471	1,884	2,725	3,998
Loan Funds	1,107	1,183	3,255	5,725	6,482
Def Tax liability	28	1	(0)	7	23
<b>Total</b>	<b>1,799</b>	<b>2,655</b>	<b>5,139</b>	<b>8,457</b>	<b>10,503</b>
<b>Uses</b>					
Gross Block	1,295	1,550	2,190	4,771	6,034
Accd Depreciation	(242)	(321)	(440)	(714)	(1,104)
Net Block	1,053	1,229	1,750	4,057	4,930
Capital WIP	61	128	373	213	202
Total Fixed Assets	1,114	1,357	2,123	4,270	5,132
Investments	4	4	75	75	75
Total Current Assets	1,140	1,853	3,746	5,692	7,361
Total Current Liabilities	(489)	(567)	(816)	(1,580)	(2,065)
Net Working Capital	651	1,286	2,931	4,113	5,295
Miscellaneous expenditure	30	8	10	0	0
<b>Total</b>	<b>1,799</b>	<b>2,655</b>	<b>5,139</b>	<b>8,457</b>	<b>10,503</b>

**Key Ratios**

Period to	FY04 (12)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
<b>Per share ratios (Rs)</b>					
Consolidated EPS	3.9	4.7	7.4	11.0	16.8
Div per share	0.5	0.5	0.7	0.7	0.8
Book value per share	12.9	21.5	27.5	33.6	49.4
<b>Valuation ratios (x)</b>					
P/E	63.7	53.2	33.7	22.7	14.9
P/BV	19.4	11.6	9.1	7.4	5.1
M Cap/Sales	7.6	9.1	6.2	3.6	2.3
EV/EBIDTA	32.0	34.1	23.7	14.5	9.5
<b>Profitability ratios (%)</b>					
OPM	24.6	26.9	23.3	22.5	23.5
PAT	12.0	17.2	18.3	16.0	15.6
ROCE	20.3	16.9	11.7	13.3	16.7
RONW	30.4	21.9	27.0	32.8	34.1
<b>Liquidity ratios</b>					
Current ratio	2.3	3.3	4.6	3.6	3.6
Debtors days	66.5	130	114	122	91
Inventory days	126.4	159	142	142	113
Creditors days	84.9	87	86	91	78
<b>Leverage ratios</b>					
Debt / Total equity	1.67	0.80	1.73	2.10	1.62
<b>Component ratios</b>					
Raw material and manufacturing cost	53.1	48.2	54.8	53.0	52.2
Staff cost	11.2	11.6	12.4	12.0	12.2
Selling expenses	4.9	5.9	3.6	6.0	5.8
Other expenses	6.2	7.4	6.0	6.5	6.3
<b>Payout ratios</b>					
Dividend payout	15.0	11.9	10.6	7.2	5.4
Tax payout	11.2	2.1	6.3	7.5	10.0



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