7 March 2008 | 7 pages

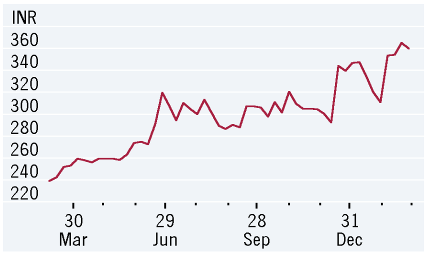
Jubilant Organosys (JUBO.BO)

Buy: Steady and Strong

- **Maintain Buy (1L)** — as we rate Jubilant as one of the superior Indian outsourcing plays, given its integrated business model with presence across the pharma & chemicals value chain. Growth momentum remains strong, visibility of revenues has improved & with the Hollister-Steir Labs acquisition strengthening its global position in innovator CRAMS, we remain positive.
- **CRAMS share growing; visibility improving** — The high margin PLSPS business (mainly CRAMS) now forms c60% of revenues & 67% of PBIT in 9m08. Visibility has also improved, with Jubilant entering into a "multi-million" dollar 5-year contract with Syngenta & reporting an order book of US$92m for CY08 (up 53% YoY). Jubilant's CRAMS business has grown at 45% CAGR (organic) over FY05-07 and looks well set to sustain the growth momentum.
- **Oxcarba boost** — Jubilant's API business got a big boost with 3 generic players getting exclusivity in oxcarbazapine. We believe that Jubilant supplies the API to Glenmark (one of the exclusivity players). Moreover, it has tie-ups with 4 more ANDA filers & is likely to be a key player in this product, in our view – leading to sustained revenues & cash flows beyond the exclusivity period.
- **Issues / Trends** — i) Research services business to gain traction in coming quarters; ii) Capacity expansion at Hollister-Stier to 120m vials/annum to come through in 1QFY09; iii) Capex of Rs2.5bn planned for FY09 with an additional Rs2bn capex in Hollister-Stier and research services business; iv) Trend in molasses prices is crucial, given that it is a key raw material especially for the non pharma business.

Buy/Low Risk	**1L**
Price (05 Mar 08)	Rs348.10
Target price	Rs415.00
Expected share price return	19.2%
Expected dividend yield	0.6%
Expected total return	**19.8%**
Market Cap	Rs50,490M US$1,255M

Price Performance (RIC: JUBO.BO, BB: JOL IN)



Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2006A	1,297	8.11	-12.1	42.9	6.0	19.6	0.4
2007A	2,280	12.56	54.7	27.7	5.5	26.4	0.4
2008E	3,154	17.37	38.3	20.0	4.2	30.2	0.5
2009E	4,014	22.11	27.3	15.7	3.2	29.2	0.6
2010E	4,902	27.00	22.1	12.9	2.5	27.4	0.6

Source: Powered by dataCentral

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Fiscal year end 31-Mar	2006	2007	2008E	2009E	2010E
Valuation Ratios					
P/E adjusted (x)	42.9	27.7	20.0	15.7	12.9
EV/EBITDA adjusted (x)	25.9	18.5	14.2	11.6	9.7
P/BV (x)	6.0	5.5	4.2	3.2	2.5
Dividend yield (%)	0.4	0.4	0.5	0.6	0.6
Per Share Data (Rs)					
EPS adjusted	8.11	12.56	17.37	22.11	27.00
EPS reported	8.11	12.56	24.74	23.62	28.51
BVPS	57.74	62.75	82.75	108.39	140.21
DPS	1.25	1.25	1.70	2.00	2.00
Profit & Loss (RsM)					
Net sales	14,990	18,097	24,215	29,926	34,130
Operating expenses	-13,332	-15,526	-20,520	-25,174	-28,427
EBIT	**1,657**	**2,571**	**3,695**	**4,752**	**5,703**
Net interest expense	-173	-195	-446	-518	-526
Non-operating/exceptionals	197	576	1,868	690	767
Pre-tax profit	**1,681**	**2,953**	**5,117**	**4,924**	**5,944**
Tax	-392	-712	-605	-604	-737
Extraord./Min.Int./Pref.div.	8	39	-20	-30	-30
Reported net income	**1,297**	**2,280**	**4,492**	**4,289**	**5,177**
Adjusted earnings	1,297	2,280	3,154	4,014	4,902
Adjusted EBITDA	2,170	3,194	4,548	5,909	6,975
Growth Rates (%)					
Sales	28.1	20.7	33.8	23.6	14.0
EBIT adjusted	-2.2	55.2	43.7	28.6	20.0
EBITDA adjusted	4.6	47.2	42.4	29.9	18.0
EPS adjusted	-12.1	54.7	38.3	27.3	22.1
Cash Flow (RsM)					
Operating cash flow	**159**	**1,868**	**2,619**	**3,921**	**5,351**
Depreciation/amortization	513	623	853	1,156	1,271
Net working capital	-1,895	-886	-3,012	-1,740	-1,355
Investing cash flow	**-4,607**	**-3,675**	**-10,043**	**-3,000**	**-3,000**
Capital expenditure	-2,736	-3,674	-10,043	-3,000	-3,000
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**5,440**	**9,630**	**2,900**	**-328**	**-328**
Borrowings	4,542	9,831	3,179	0	0
Dividends paid	-189	-203	-279	-328	-328
Change in cash	**992**	**7,823**	**-4,524**	**593**	**2,023**
Balance Sheet (RsM)					
Total assets	**20,483**	**32,329**	**38,455**	**43,377**	**48,885**
Cash & cash equivalent	1,390	8,749	2,887	3,205	4,953
Accounts receivable	2,479	2,948	3,901	4,821	5,499
Net fixed assets	11,531	14,636	23,825	25,669	27,397
Total liabilities	**12,107**	**23,134**	**26,365**	**27,571**	**28,475**
Accounts payable	2,693	2,918	3,901	4,821	5,499
Total Debt	7,220	16,526	19,705	19,705	19,705
Shareholders' funds	**8,376**	**9,195**	**12,090**	**15,806**	**20,410**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	14.5	17.7	18.8	19.7	20.4
ROE adjusted	19.6	26.4	30.2	29.2	27.4
ROIC adjusted	9.6	10.0	11.8	12.4	13.5
Net debt to equity	69.6	84.6	139.1	104.4	72.3
Total debt to capital	46.3	64.3	62.0	55.5	49.1

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Jubilant Organosys

Company description

Jubilant Organosys is the largest specialty chemicals company in India, with a high degree of vertical integration, and global scale and reach in almost all its key products. The company has established itself as a serious player from fine chemicals to advanced intermediates and APIs. More recently, it has forayed into formulations and regulatory services through acquisitions in Belgium (PSI n.v. and PSI supply) and the US (Trigyn Laboratories). It has set up wholly owned subsidiaries to tap into the high-potential areas of bioinformatics, medicinal chemistry services and clinical services.

Investment strategy

We maintain our Buy/Low Risk (1L) rating on Jubilant, with target price of Rs415. Jubilant is among the top Indian pharma outsourcing plays under our coverage. It is a story of continuous forward integration with a business model that spans pharma & life sciences (P&LS), industrial chemicals and performance chemicals. Jubilant's strong presence in acetyls and pyridines builds a high degree of integration into its business and allows it to offer services across the value chain. Besides a natural cost advantage, this allows the company to leverage its customer relationships in strong areas to scale up new businesses, thus providing an edge in an increasingly competitive industry. Jubilant's P&LS business is in the midst of a high growth phase. We expect the share of this business to increase from 51% in FY07 to 68% in FY10E. This would not only raise profitability levels but also improve earnings quality by reducing Jubilant's exposure to the more volatile non-P&LS businesses. Overall, we expect 24% and 31% CAGRs in revenues and fully diluted earnings, respectively, for FY07-10E

Valuation

We use sum-of-the-parts to value Jubilant in view of the diversified nature of its business and earnings streams. We value the P&LS and non-P&LS businesses using the EV/EBIDTA methodology but apply different target multiples to each business given the difference in their growth and operating parameters. We arrive at a one-year target price of Rs415.

We value Jubilant's P&LS business at 15x March 2009E EV/EBIDTA and the non-P&LS business at 7x March 2009E EV/EBIDTA. Our target valuation for the P&LS business is benchmarked to the upper end of Jubilant's past four-year EV/EBIDTA range. We are comfortable using a higher multiple vis-à-vis some of its mid-sized Pharma peers due to strong growth rates and the upside potential when idle FCCB proceeds are deployed in the core business. Industrial chemicals and performance chemicals are mature businesses in which Jubilant has indicated that it does not intend to make any significant incremental investment. However, the company's competitive edge in these areas would ensure that it is able to generate steady profits from these businesses. We therefore value these businesses at 7x March 2009E EBIDTA, which is in-line with the multiple that Jubilant used to trade at around four years ago when these businesses contributed almost entirely to the company's revenues and profits.

Risks

We rate Jubilant Low Risk based on our quantitative risk-rating system. The main downside risks to our target price and estimates include: (1) The generics business has become very competitive; (2) Any delay in filing / launch or a litigation loss would affect the timing and quantum of revenues and profits; (3) Inability to integrate and exploit the synergies with its acquired subsidiaries could hurt profitability; and (4) Increases in molasses prices. The main upside risks to our target price include: (1) A significant value accretive acquisition could lead to upside to our estimates; and (2) Pyridine prices could firm up in the medium term.

Appendix A-1

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#	Date	Rating	Target Price	Closing Price
1:	10 Oct 05	1L	249.80	209.47
2:	15 May 06	1L	*299.00	248.30
3:	17 Jan 07	1L	*368.00	267.95
4:	30 Apr 07	1L	*340.00	260.75
5:	18 Jul 07	1L	*386.00	310.20
6:	17 Oct 07	1L	*415.00	310.95

*Indicates change.

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