VISIT UPDATE

LARGE CAP

Ranbaxy Laboratories

Maintain BUY

Price: Rs 473 | **BSE Index: 17,490** | **18 March 2010**

Share Data

Reuters code	RANB.BO
Bloomberg code	RBXY IN
Market cap. (US$ mn)	4,378
6M avg. daily turnover (US$ mn)	22
Issued shares (mn)	421
Target price (Rs)	530

Performance (%)	1M	3M	12M
Absolute	7	(10)	227
Relative	1	(13)	66

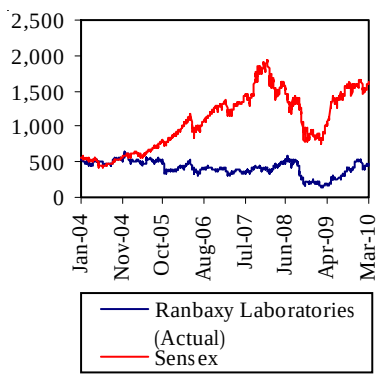
Valuation ratios

Yr to 31 Dec	CY10E	CY11E
EPS (Rs)	13.1	15.3
+/- (%)	85.8	16.5
PER (x)	35.5	30.5
PBV (x)	4.1	3.9
Dividend/Yield (%)	1.8	1.8
EV/Sales (x)	2.7	2.5
EV/EBITDA (x)	21.3	18.8

Major shareholders (%)

Promoters	64
FIIs	7
MFs	3
BFSI's	9
Public & Others	17

Relative performance



Gradual transformation in process

Ranbaxy is tackling most of its problems head-on with highest priority accorded to clearing its name in US FDA issues pertaining to manufacturing units & DOJ issue. We expect these issues to be resolved eventually but time-line seems uncertain. Other priorities include a). Improve profitability from European operations b). Roll out VIRAAT project in India where it is targeting sustained revenue growth of 20% annually c). Leverage hybrid model for key markets including Japan.

As per the mid-term plan released by Daiichi, Ranbaxy is targeted to achieve revenues of US $ 3 bn by 2012 which implies 22% CAGR in revenues. This target would presumably include some of its key FTF's like Lipitor which have been settled earlier. We continue to remain optimistic about what Ranbaxy could bring to Daiichi's table in terms of outsourcing (R&D, manufacturing, co-marketing) initiatives which could be incremental to Ranbaxy's earnings besides helping its parent in cost-savings.

We are positive on Ranbaxy and continue to maintain our Buy with a target price of Rs 530 (includes NPV of all FTF's at Rs 123 per share). At current price of Rs 473, the stock trades at 36x CY10E & 31x CY11E EPS of Rs 13 & Rs 15 respectively. Our estimates are above the guidance given by management (EPS of Rs 11 for current year) which include FTF's like Flomax (monetized partially), Lipitor launch in other markets and Nexium supplies. Key challenges/risks include uncertain time-line for resolution of US FDA & DOJ issues which can continue to keep investor sentiment subdued.

We recently met the management of Ranbaxy Laboratories and key highlights are

USFDA resolution

As indicated by the management, Ranbaxy's Dewas facility is ready for USFDA inspection. Accordingly, the company has invited USFDA to inspect the facility but no time-line for the inspection is available. The management expects the resolution of Dewas unit to be completed in the current year itself

Regarding Paonta Sahib, which is facing serious issues related to data integrity, it's resolution is expected to take a longer time. However, operations for other markets from Paonta Sahib facility continues (is certified by Japanese, UK-MHRA, Australia-TGA, etc.). The management indicated the internal target to resolve the FDA issues for both the plants is by the end of CY10E.

In December 2009, Ranbaxy's Ohm Laboratories at Gloversville, New York, USA had also received warning letter from USFDA. The plant for liquid orals manufactures most of the products supplied in the US market and contributes just 1% to the US sales. Being a dated facility (acquired in 2005 by Ranbaxy), the management was to phase-out this facility but due to USFDA warning letter, any decision on this plant has been postponed.

Coping with US FDA strictures….filing pace yet to pick-up

Ranbaxy filed for 11-12 drugs in past one year taking total ANDAs pending approval to 66

Of the 30-odd products that were banned by USFDA (import alert) to be sold in the US market, the company may have already shifted manufacturing of few products to the US plants while few products might not be pursued by the company (for commercial reasons). Site transfer of key products is an ongoing evaluation and would ensure steady flow of products for the US markets (current base business averaging about US $ 45-55 mn per quarter). Further, the company has ramped up capacity at its Ohm's facility besides filing dossiers from its new Mohali facility (SEZ for oral dosage forms).

In CY09, Ranbaxy received approvals for 5 products (primarily coming from international facilities-Ohm). The Mohali facility is yet to be inspected though it has started filing dossiers. It has filed for 11-12 drugs in past one year taking total products pending approval to ~66 ANDA's.

Drug approval post US import alert in September 2008 (all products approved from Ohm site)

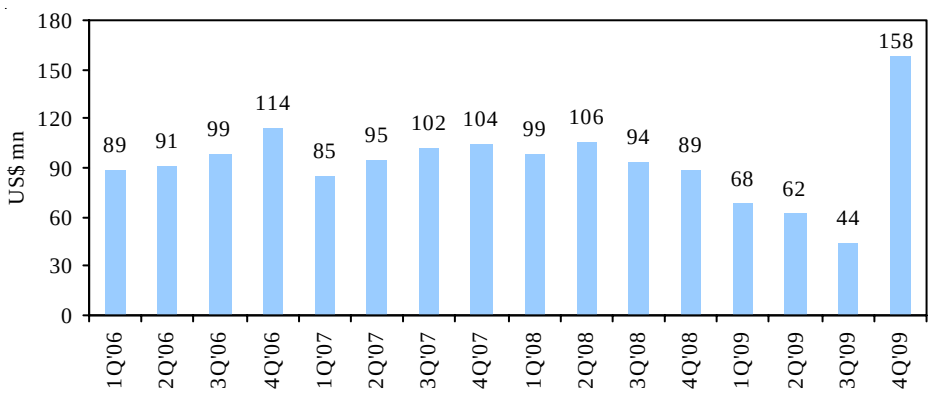
Feb-09	Sumatriptan Succinate (Imitrex)
Mar-09	Hydrochlorothiazide: Quinapril HCL
Mar-09	Ramipril
Mar-09	Topiramate
Jun-09	Oxcarbazapine suspension (180 days excl.)
Aug-09	Glycopyrrolate
Sept-09	Rocaltrol (authorised generic)

Source: USFDA, B&K research

The current focus for Ranbaxy is a). To resolve all manufacturing issues pertaining to Dewas, Paonta Sahib & Ohm facilities besides the DOJ issue. B). To ensure timely launch for FTF opportunities through alternate back-up plans (Valtrex launched on time) or alternate strategies to monetize FTF opportunity (like the recent Flomax deal with Impax)

The company has hired competent authorities / consultants for advice and the professional / legal charges are likely to exceed Rs 1.0 bn (which may not be recurring and would accrue to bottomline / margins later). Such expenses have been a drain on its margins and may have negated any cost-cutting measures it has been undertaking since the import alert.

US revenues…..bouncing back



Source: Company, B&K Research

Tamsulosin settlement with Impax….FTF monetized

Though Ranbaxy did not receive approval for Tamsulosin from FDA, it apparently had entered into a settlement with Impax and received a one-time settlement income

Though Ranbaxy did not receive approval for Tamsulosin from FDA, it apparently had entered into a settlement with Impax (which got approval from USFDA and launched the drug in US). Though details of the settlement are not disclosed, Ranbaxy has received a one-time settlement income from Impax which allows the latter to enjoy marketing exclusivity (for 8 weeks before patent expiry). This income will be part of 1Q'10 earnings for Ranbaxy. The reasons for Flomax non-approval is not known but would be launched as soon as it gets approval.

Strong product pipeline for US

Ranbaxy has ~66 products pending approval for the US market which includes 30 para IV filings and 16-18 FTFs

Currently, Ranbaxy has ~66 products pending approval for the US market. Of these, 30 products are para IV filings of which they have 16-18 FTF (First-to-file). Though the launch of Valtrex in November 2009 has provided significant upside for the company (which would continue for 1Q'10 too), one time settlement income from Impax for Tamsulosin will boost the company's profitability in CY10E.

Further, timely launch of Valcyte (Valagancyclovir) in US and Lipitor in other markets (including Canada) could provide additional upside to our CY10E earnings of Rs 13 (as compared to company guidance of EPS of Rs 11). Some of its other FTFs include Atorvastatin (Lipitor), Modafinil (Provigil), Diovan (Valsartan), Aricept (Donezepil), Esomeprazole (Nexium) and Atorvastatin+Amlodipine (Caduet) & Pioglitazone (Actos - latest settlement). The company indicated that for each FTF launch, they follow multiple approaches which include two to three back-up plans for the successful launch of the drug.

Key FTFs for Ranbaxy

API	Brand	Innovator	Market size (US$ bn)	Remarks
Esomeprazole	Nexium	AstraZeneca	1.9	Settled with Astra Zeneca
Atorvastatin	Lipitor	Pfizer	6.3	Settled with Pfizer
Modafinil	Provigil	Cephalon	1.0	Settled with Cephalon
Pioglitazone	Actos	Takeda	3.4	Settled with Takeda, shared exclusivity with Watson & Mylan
Atorvastatin + Amlodipine	Caduet	Pfizer	0.4	Settled with Pfizer
Valsartan	Diovan	Novartis	2.4	Tentative approval
Donepezil	Aricept	Eisai	0.5	Eisai and Pfizer are co-marketing the drug, Tentative approval
Tolterodine	Detrol	Pfizer	0.8	Tentative approval
Galantamine	Razadyne	Ortho Mcneil Janssen		Tentative approval
Valagancyclovir	Valcyte	Roche Palo	0.6	Not yet settled
Irbesartan	Avapro / Avalide	Sanofi Aventis	1.1	Not yet settled
Ziprasidone	Geodon	Pfizer	0.8	Not yet settled
Tiagabine	Gabitril	Cephalon		Not yet settled
Candesartan	Atacand	AstraZeneca	1.4	Not yet settled
Meropenem	Merrem	AstraZeneca	0.9	Not yet settled
Repaglinide	Prandin	Novo Nordisk		Not yet settled
Imipenem	Primaxin	Merck		Not yet settled

Settlement with Takeda for Actos

Takeda has granted Ranbaxy non exclusive royalty free license to its US patents covering Actos which had annual sales of ~US$ 3.4 bn in 2009

Ranbaxy announced its settlement with Takeda Pharma wherein it settled outstanding patent litigation related to Ranbaxy's generic equivalent of Actos (Pioglitazone HCL) tablets for the treatment of type 2 diabetes. According to the terms, Takeda has granted Ranbaxy non exclusive royalty free license to its US patents covering Actos. Actos had annual sales of ~US$ 3.4 bn for the 12 months ending December 2009, as per IMS sales data. According to the terms, Ranbaxy has certainty in the launch of Pioglitazone on August 17, 2012, or earlier under certain circumstances.

Last week, Watson also settled with Takeda for Actos implying sharing of exclusivity period with Ranbaxy. According to the current scenario with three players (including innovator) marketing the drug in US, we expect Ranbaxy to report earnings of ~Rs 7-8 during the exclusivity period.

SOTP (base earnings and FTF settlement EPS)

	CY10E	CY11E
Core EPS (includes Valtrex exclusivity in CY10E)	13.1	15.3
Future upsides (FTF's)		
Flomax*	5.0	1.3
Nexium supplies	1.0	1.3
Lipitor-Other markets	1.5	2.5
Total EPS	**20.7**	**20.4**
Assigning P/E of 20x, Target Price	**413**	**407**
NPV of FTF		
Lipitor (launch in 2011)		75
Nexium (launch in 2014, discounted NPV)		27
Caduet-US (launch in 2011 end)		5
Provigil (launch in 2011 end)		5
Valcyte (launch likely in 2011)		4
Actos (launch in 2012)		8
Sum of NPV per share for FTF's		**123**
Target price (EPS + FTF's)		**530**

*Ranbaxy did not launch Flomax but received settlement income from Impax. Though the amount received was not disclosed, we have assumed EPS of Rs 5 from Flomax settlement

If US ban is revoked on its two facilities at Dewas & Paonta Sahib, then we could see further upsides of Rs 0.7 per share in CY10E & Rs 1.3 per share in CY11E respectively (not included due to uncertainty in resolution time-frame)

Project VIRAAT…..Increased focus on domestic market

Ranbaxy will be launching its Project "Viraat" in April 2010 in order to improve its market share and doctor reach by penetrating into areas where they were not present (across existing market segments-metros, towns, etc.). The project would also involve penetration into rural India and launch of existing and new products. The company plans to launch a new product every 2 weeks (approx. 25-30 new products annually). This could include a new product (new dosage form, line extension or combination) or a new molecule altogether. New therapy areas are also being targeted.

With the launch of project 'Viraat', Ranbaxy is targeting a growth rate of 20% annually from the domestic market

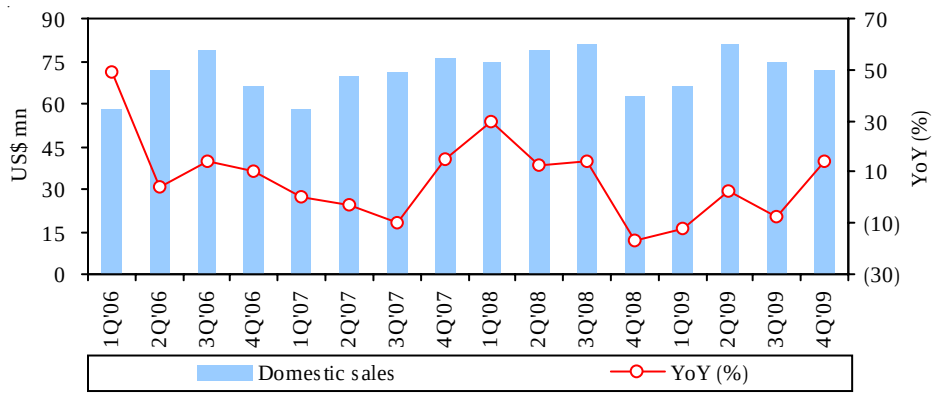
For this project, the company has recruited ~1,500 sales representatives (field force) taking its total strength to 4,000 MR's. The company currently has a strong urban presence (~ 2,500 sales representatives) with 6.5% market share. With the launch of VIRAAT, we expect the company to witness significant growth in domestic market which will be visible after 2-3 quarters. The management has targeted growth rate of 20% annually.

Ranbaxy's key brands

Therapy segment	% of rev.	Key Brands
Anti-infectives	37	Sporidex, Cifran, Mox, Zanocin, Moxclav, Oframax, Cilanem, Roscillin, Suprimox, Ranbiotic
Cardiovascular	13	Storvas, Rosuvas, Covance, Simvotin
Nutritional/Consumer	10	Revital, Chericof, Pepfiz,
Pain Mngt	10	Volini
Dermatology	7	Silverex, Zole-F, Fucidin, Diprovate, Volitra
Gastrointestinal	7	Gramogyl, Histac
Others	16	Calmpose, Pioglar,
India Revenues (US $ mn)	**300**	**Represents about 20% of Ranbaxy's global business**

Others include Respiratory, Female Healthcare, CNS & Diabetology

Domestic revenues….VIRAAT project to lift growth rates



Source: Company, B&K Research

Management to adopt 'Hybrid business model'……Mid-term Plan of Daiichi

Recently, Daiichi Sankyo (DS) announced its second mid-term business management plan (MBMP-FY2010-2012), effective April 2010. The plan will prioritize creating more innovative products while adopting a Hybrid business model' that will focus on vaccines, established pharmaceuticals, and OTC products to increase its market share.

Key highlights of Mid-Term Plan related to Ranbaxy

- DS priority is to resolve Ranbaxy related USFDA issues (import alert and AIP issues) against Dewas and Paonta Sahib facilities.
- DS plans to create and develop synergies with Ranbaxy throughout the value chain.
- DS is targeting revenue of Rs 136 bn from Ranbaxy in 2012 which implies a CAGR of 22%. This includes scaling up revenues from emerging markets from US$ 1 bn in CY09 to US$ 1.7 bn in CY12 (~ 57% of Ranbaxy's business by 2012)

- DS has plans to provide high quality, affordable generic drugs from collaboration with Ranbaxy for the Japanese market through a company Daiichi Sankyo Espha Ltd. The plan is to launch DS brands and leverage its distribution channel.
- Through hybrid business model with Ranbaxy, DS plans to expand the Olmesartan franchise, launch and build sales of Prasugrel in markets other than US, Europe and Japan.
- DS plans to build synergies by taking advantage of the strengths of DS and Ranbaxy in R&D, pharmaceutical technology, supply chain, quality & safety management and sales & marketing.

Daiichi's 2012 target (¥ bn)

Year	2009	2012	CAGR (%)
Daiichi's net sales	960	1,150	6.2
Overseas sales	488	650	–
Ranbaxy's sales	148	270	22.2
Ranbaxy's sales (US$ bn)	1.6	3.0	22.2
Ranbaxy's sales (Rs bn)	74	136	22.2
Operating income	96	180	23.3
EPS (¥)	63.9	Atleast¥ 140	
RoE (%)	5.2	Atleast 10	

Source: Daiichi Sankyo

Ranbaxy's road map till CY12E

US$ mn	CY09	CY10E	CY11E	CY12E	CY09-12E CAGR (%)	Comments
North America	397	445	419	475	6	CY10E includes revenue from Valtrex which was launched in Nov 2009.
EU	269	285	300	330	7	Key markets include Romania, France, Germany & UK
India & ME	359	431	504	593	18	Launch of project Viraat to boost India growth
CIS	86	80	80	90	2	Launch of various Daiichi research products in emerging markets could boost performance from these markets.
Asia pacific	100	120	120	120	6	
Africa	125	115	115	125	0	
ROW	71	75	85	95	10	
Total dosage Forms	1,407	1,550	1,623	1,828	9	
API	112	120	120	130	5	
Total revenue	1,519	1,670	1,743	1,958	9	Ex-FTFs, revenues to fall short of Daiichi's target
Potential revenues from FTFs & Nexium supplies	–	110	601	1,311	–	Includes potential revenues from settled FTFs like Atorvastatin, Modafinil, Esomeprazole, Caduet and Pioglitazone. Other FTFs like Donepezil, Valsartan and Valcyte have not been considered
Total revenue (including FTFs)	1,519	1,780	2,343	3,270	29	Daiichi is targetting a revenue of US$ 3 bn (270 bn Yen) from Ranbaxy in CY12E which would assume contribution from various FTFs (including Lipitor)

Source: B&K research

Daiichi Sankyo (DS) and Ranbaxy to expand business scope in Japan

Japan offers huge opportunity as it is the second largest pharmaceutical market (size of US$ 65 bn) in the world with only 17% generic penetration in volume terms and ~5% in value terms

Leveraging their business expertise, Daiichi Sankyo and Ranbaxy Laboratories are jointly planning to establish a company (Daiichi Sankyo Espha Ltd) in Japan (on 1 April 2010). The established company will focus on manufacturing and marketing generic drugs (including Daiichi Sankyo's well established drugs) in the Japanese market.

Given Daiichi's understanding of Japanese market and local presence and Ranbaxy's global expertise in generics, we believe the new company will be able to garner a significant market share in a high growth Japanese generics market. Japan offers huge opportunity as it is the second largest pharmaceutical market (size of US$ 65 bn) in the world with only 17% generic penetration in volume terms and ~5% in value terms as compared to the US (Volume-70%, value-30%). We expect significant traction to Ranbaxy's earnings from its Japanese initiatives in times to come (not factored into our estimates)

DS and Ranbaxy to focus on emerging markets

DS and Ranbaxy plans to collaborate in the fast growing emerging markets and fully deploy the Hybrid Business Model. Given Ranbaxy's presence in more than 125 countries and DS' mid term plan, we expect DS & Ranbaxy to launch products in key emerging markets such as LATAM, CIS, EU, Asia Pacific and Africa.

The synergy among the two entities has already commenced as Ranbaxy launched Daiichi's research products in India and Romania during 4QCY09. The company has also set up a new division in Mexico to market DS products and plans to launch Olmesartan in six African countries. Given this step of synergizing and forming a hybrid business model, we expect improvement in performance of Ranbaxy going forward. DS is targeting sales of US$ 1.7 bn in CY12 from US$ 1 bn in CY09 from the emerging markets.

As part of its strategy, DS has rationalized certain key markets like China and Vietnam wherein it exited from the ventures due to tough market conditions and Government intervention.

Huge R& D opportunity from Daiichi

With Daiichi and Ranbaxy hybrid business model being developed, we expect huge opportunity in R&D for Ranbaxy. The areas of interest for Daiichi would include R&D outsourcing, global outsourcing of manufacturing to India, building generic pipeline for Japan's generic market apart from other emerging market pipeline. There could be opportunity in co-marketing and in-licensing deal with Daiichi or other MNC's for India & other markets. **We continue to remain optimistic about what Ranbaxy could bring to Daiichi's table in terms of outsourcing (R&D, manufacturing, co-marketing) initiatives which could be incremental to Ranbaxy's earnings besides helping its parent in cost-savings**

CY09 results – Valtrex launch and forex gain boosting performance

For CY09, Ranbaxy's net sales grew marginally by 2% to Rs 73 bn despite USFDA ban which significantly impacted the overall business in CY08. However in CY09, the recovery is due to launch of Valtrex in the US in November 2009 (US witnessed growth of 78% with revenue of US$ 158 mn; we expect Valtrex would have contributed to ~US$ 100 mn in 4QCY09 with base business averaging about US $ 50-55 mn per quarter). The strong operational performance during CY09 was on account of Valtrex launch and cost containment measures

by the company. During the year, the company turned profitable with PAT of Rs 3.1 bn (against loss of Rs 9.3 bn in CY08) mainly due to forex gain of Rs 3.4 bn (against forex loss of Rs 18.6 bn) and deferred tax asset of Rs 2.2 bn.

Financial performance

(Rs mn)	1QCY09	2QCY09	3QCY09	4QCY09	CY08	CY09	YoY (%)
Net Sales	15,548	17,919	17,205	22,552	72,019	73,294	1.8
Operating Profit (excl.other op.inc.)	(1,045)	412	526	7,607	570	6,379	1,018.7
As a % of Sales	(6.7)	2.3	3.1	33.7	0.8	8.7	–
OPM (incl.other op.income) (%)	(5.3)	7.2	12.9	33.2	3.3	12.4	–
Other operating income	223	873	1,695	(115)	1,799	2,676	48.7
Other Income	457	400	163	1,915	2,706	2,935	8.5
Interest	246	197	121	146	2,055	710	(65.4)
Depreciation+Amortisation	639	644	654	739	2,825	2,676	(5.3)
PBT (from operations)	(1,250)	844	1,609	8,522	196	8,604	4,285.9
Forex gain/(Loss)	(1,273)	1,908	(8)	866	(7,494)	1,493	–
Extraordinary Income	(9,188)	8,067	0	0	(7,702)	0	–
Tax (incl.deferred tax) + Minority Int.	(4,101)	3,888	435	6,769	(5,651)	6,991	(223.7)
Reported PAT	(7,610)	6,931	1,166	2,619	(9,349)	3,106	(133.2)
PAT Margin (%)	(48.9)	38.7	6.8	11.6	(13.0)	4.2	–

*4QCY09 and CY09 numbers have been restated. The given numbers are not comparable.

AstraZeneca deal for Nexium supplies

Ranbaxy commenced supply of Nexium API to AstraZeneca (first batch of 160kg) in 1QCY10

The management indicated commencement of Nexium API supply (first batch of 160 kg) to AstraZeneca in 1QCY10 and expects commercial shipment to begin by the end of CY10E. Subsequently Ranbaxy may commence supply of Nexium dosage forms to AstraZeneca. Though the deal is not very significant for Ranbaxy in terms of profitability but will contribute incrementally to Ranbaxy's earnings.

In a deal between AstraZeneca and Merck, AstraZeneca will exercise its option to buy out Merck's interest in AZ's non-proton pump inhibitor (non-PPI) products this year for US$ 647 mn. The products are Atacand, Lexxel, Plendil and Entocort, as well as several products in development. The option price reflects Merck's share of projected pretax revenue for the products. The buy-out also triggers AZ's option to acquire Merck's interest in AZ's PPI products, including Nexium, in 2012 or later. As indicated by the management, the deal will not have any implication on Ranbaxy's supply deal.

European operations

As part of cost rationalization, the company closed one plant in Romania (laid off 120-130 employees)

In Europe, Ranbaxy has operations in around 16 countries with Romania, Germany, UK and France being the major contributors. During the economic slowdown, the company witnessed decline in revenues across Europe especially from Romania (sales declined from US$ 120 mn to US$ 75 mn). The company has been focusing on improving profitability by cost rationalization. As part of this, the company closed one plant in Romania (laid off 120-130 employees).

Ranbaxy enters into Vaccines/Biotech space with Biovel acquisition

Biovel's vaccines pipeline includes Typhoid vaccine, Hepatitis B vaccine and will focus on pentavalent vaccine and differentiated products

In January 2010, Ranbaxy acquired product rights and a manufacturing facility of Bangalore based Biovel Lifesciences Pvt Ltd. The deal will provide Ranbaxy to access all of Biovel's products, pipeline, IP, Know-How and manufacturing facility, located in Bangalore. The division will be headed by an ex-Wyeth US person who has varied exposure in the pharmaceutical sector. Biovel's vaccines pipeline includes Typhoid vaccine, Hepatitis B vaccine and will focus on pentavalent vaccine and differentiated products. For Ranbaxy, this acquisition was quite attractive as the investors were facing liquidity issues due to sub-prime crisis. Product launches from Biovel's pipeline is expected to commence in the next 1 year or so.

Hedging Treasury operations….current hedge position

Ranbaxy currently has outstanding forward contracts worth US$ 1 bn. These contracts are spread equally for the next 6 to 7 years and hedged at around Rs 43 – 44/US$. In CY08, with the depreciation of Rupee, the company had to make huge MTM/forex losses (~Rs 18 bn) which were fully provided in CY08. As Rupee appreciated in CY09, the company made MTM/forex profits (Rs 3.4 bn) on its outstanding contracts.

R&D activities in full swing

The company has a basic research outlay of US$ 25 mn which focuses on drug discovery/NCE pipeline

The R&D activities are going on in full swing under the leadership of Mr. Sudarshan Arora. The company has a basic research outlay of US$ 25 mn which focuses on drug discovery/NCE pipeline. In the past, Ranbaxy had signed two major R&D deals with GSK and Merck with potential licensing income of more than US$ 200 mn.

- **Ranbaxy-GSK R&D deal**

  In 2007, the company had signed a multi-year R&D agreement with GSK wherein they expanded the terms of their strategic alliance which was established in 2003.

  The expanded alliance included GSK's therapeutics of interest, such as anti-infectives, metabolic, respiratory and oncology products.

  Under the original agreement, Ranbaxy conducted the optimization chemistry for progressing drug leads to the stage of candidate selection. Under the new agreement, Ranbaxy had to advance leads beyond candidate selection to completion of clinical proof of concept. GSK will then conduct further clinical development for each program through to commercialization.

  Ranbaxy could receive more than $100 million in milestone payments for any products subsequently launched by GSK, as well as royalties on sales. Ranbaxy was to retain the right to co-commercialize the products in India. The milestones and royalties will apply to future drug discovery programs as well as Ranbaxy's two current programs under the original GSK agreement.

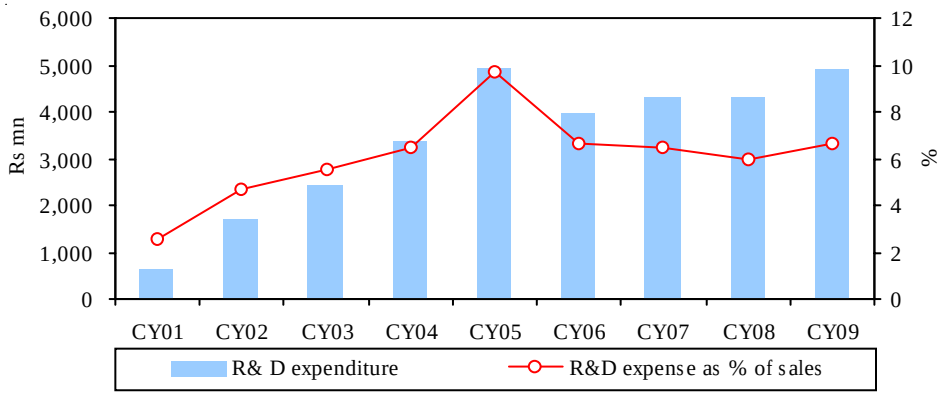
- **Ranbaxy-Merck R&D deal**

  In 2008, Ranbaxy and Merck signed a drug discovery and development agreement in the anti-infective area. As per the agreement, Ranbaxy is to develop drug candidates in the anti-bacterial and anti-fungal areas and to conduct clinical development till phase IIa.

  Pursuant to which Merck will undertake further clinical development and commercialization. The collaboration tenure is for 5 years and can be extended mutually

thereafter. Ranbaxy received an upfront payment (amount undisclosed) with the potential future milestones income totalling more than US$ 100 mn.

R&D expenditure



Source: Company, B&K Research

Daiichi-Zenotech litigation still pending

In October 2007, Ranbaxy had hiked its stake in Zenotech from 7% to 45% at Rs 160 per share. The additional stake comprises purchase of promoters' (Dr Jay Chirugapati) shares and a preferential allotment (16 per cent) by Zenotech to Ranbaxy. The acquisition also makes it mandatory for Ranbaxy to make an open offer for an additional 20% to Zenotech's shareholders as per SEBI guidelines. The open offer was also to be made at Rs 160 per share or at a SEBI recommended price. In January 2009 Daiichi Sankyo (acquired Ranbaxy in 2008) said it would launch the offer in March at a price of Rs 113.62 per share. However, the offer got delayed on prolonged review by the regulators. Post this; minority shareholders of Zenotech filed a petition about the price of the offer. The litigation is still pending and management hopes to resolve the issue in CY10E. Zenotech is a speciality generic injectables company with biotech at its core and has a niche basket of biopharmaceuticals and oncology products.

The company holds 13% stake in Orchid Chemicals through its subsidiary "Rexcel Pharmaceuticals'. The company also owns 11.6% stake in Krebs Chemicals.

Peer valuations

FY10E	CMP	Mkt. cap	EPS (Rs)				EPS CAGR (%)	P/E (x)			FY10E			
	(Rs)	(US$ bn)	FY09	FY10E	FY11E	FY12E	FY10-12E	FY10E	FY11E	FY12E	EV/Sales (x)	EV/EBITDA (x)	RoE (%)	RoCE (%)
Sun	1,667	7.7	87.8	64.5	77	87.6	16.5	25.8	21.5	19.0	8.4	26.0	17.2	17.9
Cipla	318	5.7	12.4	13.4	15	18.5	17.3	23.7	20.9	17.2	4.8	18.4	22.6	21.9
Ranbaxy	475	4.4	(4.3)	7.1	13.1	15.3	47.1	67.3	36.2	31.1	2.9	23.6	6.6	14.6
Dr Reddy	1,220	4.6	36.0	53.0	62	71.5	16.2	23.0	19.8	17.1	3.1	17.2	21.4	17.6

Income Statement

Yr end 31 Dec (Rs mn)	CY08	CY09	CY10E	CY11E
Net sales	**72,019**	**73,294**	**79,030**	**85,042**
Growth (%)	*8.8*	*1.8*	*7.8*	*7.6*
Operating expenses	(68,087)	(68,846)	(72,211)	(76,871)
Operating profit	3,932	4,448	6,820	8,170
Other operating income	(1,562)	4,608	3,000	3,000
EBITDA	**2,370**	**9,055**	**9,820**	**11,170**
Growth (%)	*(74.1)*	*282.1*	*8.4*	*13.8*
Depreciation	(2,825)	(2,676)	(3,103)	(3,290)
Other income	(4,788)	4,429	2,000	2,000
EBIT	**(5,243)**	**10,808**	**8,716**	**9,881**
Interest paid	(2,055)	(710)	(1,845)	(1,845)
Pre-tax profit (before non-recurring items)	(7,298)	10,097	6,871	8,036
Non-recurring items	(7,702)	–	–	–
Pre-tax profit (after non recurring items)	(15,000)	10,097	6,871	8,036
Tax (current + deferred)	5,651	(6,991)	(1,362)	(1,618)
Net profit	(9,349)	3,106	5,509	6,418
Minority interests	(163)	(142)	–	–
Reported PAT	(9,512)	2,965	5,509	6,418
Adjusted net profit	**(1,810)**	**2,965**	**5,509**	**6,418**
Growth (%)	*(123.4)*	*(263.8)*	*85.8*	*16.5*

Balance Sheet

Yr end 31 Dec (Rs mn)	CY08	CY09P	CY10E	CY11E
Current assets	66,922	66,692	76,063	80,984
Cash & marketable secu.	23,956	25,265	29,270	31,126
Other current assets	42,966	41,427	46,794	49,857
Investments	5,432	5,432	5,432	5,432
Net fixed assets	49,607	50,055	50,452	51,162
Total assets	**121,961**	**122,178**	**131,947**	**137,577**
Current liabilities	47,438	48,692	56,056	59,374
Total debt	43,114	39,114	40,114	40,114
Other non-currnet liab.	(12,229)	(12,229)	(12,229)	(12,229)
Total liabilities	**78,323**	**75,577**	**83,941**	**87,259**
Share capital	2,102	2,102	2,102	2,102
Reserves & Surplus	40,861	43,825	45,229	47,541
Shareholder's funds	**42,962**	**45,927**	**47,331**	**49,643**
Minorities interests	675	675	675	675
Total equity & liab.	**121,961**	**122,178**	**131,947**	**137,577**
Capital employed	**74,522**	**73,487**	**75,891**	**78,203**

Cash Flow Statement

Yr end 31 Dec (Rs mn)	CY08	CY09P	CY10E	CY11E
Pre-tax profit	(15,000)	10,097	6,871	8,036
Depreciation	(1,859)	(2,676)	(3,103)	(3,290)
Chg in working capital	23,990	2,792	(2,108)	255
Total tax paid	(5,857)	(6,991)	(1,362)	(1,618)
Other operating activities	(10,404)	–	–	–
Cash flow from oper. (a)	**(5,412)**	**8,575**	**6,505**	**9,962**
Capital expenditure	(7,385)	(3,500)	(3,500)	(4,000)
Chg in investments	(3,028)	–	–	–
Others	1,538	376	(4)	(3)
Cash flow from inv. (b)	**(8,876)**	**(3,124)**	**(3,500)**	**(4,000)**
Free cash flow (a+b)	**(14,287)**	**5,451**	**3,005**	**5,962**
Equity raised/(repaid)	34,845	–	–	–
Debt raised/(repaid)	1,699	(4,000)	1,000	–
Dividend (incl tax.)	(2,620)	–	–	(4,106)
Cash flow from fin. (c)	**33,865**	**(4,142)**	**1,000**	**(4,106)**
Net chg in cash (a+b+c)	**19,578**	**1,309**	**4,005**	**1,857**

Key Ratios

Yr end 31 Dec (%)	CY08	CY09P	CY10E	CY11E
Adjusted EPS (Rs)	(4.3)	7.1	13.1	15.3
Growth	(120.8)	(263.8)	85.8	16.5
Book NAV/Share (Rs)	103.9	111.0	114.3	119.8
Dividend/Share (Rs)	–	–	8.5	8.5
Dividend payout ratio	–	–	74.5	64.0
Tax	37.7	69.2	19.8	20.1
EBITDA margin	3.4	11.6	12.0	12.7
EBIT margin	(7.3)	14.7	11.0	11.6
RoCE	(7.2)	14.6	11.7	12.8
Net debt/Equity	43.9	29.7	22.6	17.9

Valuations

Yr end 31 Dec (x)	CY08	CY09P	CY10E	CY11E
PER	(108.0)	65.9	35.5	30.5
PCE	192.7	34.7	22.7	20.1
Price/Book	4.5	4.2	4.1	3.9
Yield (%)	–	–	1.8	1.8
EV/Net sales	2.7	2.9	2.7	2.5
EV/EBITDA	82.6	23.2	21.3	18.8

Du Pont Analysis – ROE

Yr end 31 Dec (x)	CY08	CY09P	CY10E	CY11E
Net margin (%)	(2.5)	4.0	7.0	7.5
Asset turnover	0.7	0.6	0.6	0.6
Leverage factor	3.0	2.7	2.7	2.7
Return on equity (%)	(5.0)	6.6	11.6	13.1

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