

India Update

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Highlights

Sector/event Impact

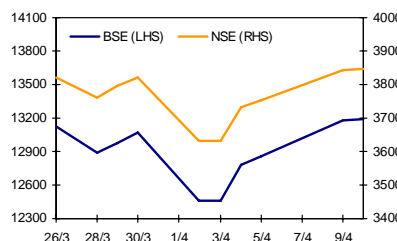
PHARMA: We expect the i-SEC pharma universe to record a strong 66% YoY surge in PAT in Q4FY07E, driven by 32% sales growth and 421bps EBITDA margin expansion. The key factors driving this growth are ANDAs with exclusivity, new launches, acquisitions, healthy growth in the domestic market and improved cost discipline. After accounting for this splendid performance, FY07E would end on a strong note with 62% YoY jump in PAT. Further, we expect the trend of positive newsflow on the drug discovery research front to continue in FY08 with Glenmark occupying centre stage. Based on our 'pick & choose' investment strategy, we reiterate Sun Pharma and Glenmark Pharma as the top BUYs among large-caps and Alembic as the preferred pick among mid-caps in the sector.

News Snippets

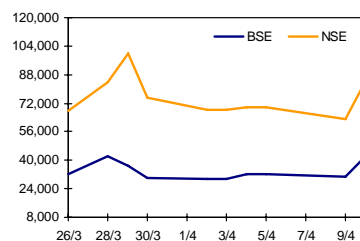
Corporate

- BHEL has raised its research & development spend to Rs2.3bn for FY07, up from Rs1.5bn last year. By '12, its R&D expenditure is estimated to cross the Rs10bn mark with the projected turnover of the entire company at US\$10bn. (Business Line)
- NTPC is open to importing equipment from Chinese vendors in an effort to contain project costs for its new power stations. The company is also eyeing the possibility of tying-up with Chinese suppliers for 4,000MW ultra mega power projects in the pipeline. (Business Line)
- Reliance Communications is mulling outsourcing its entire IT requirement in a 10-year contract for US\$1.5bn. (The Economic Times)
- Arvind Mills is planning to establish nearly 100 Megamart stores in India over the next five years to reach a total of 150 stores in 100 cities with an investment outlay of Rs300-400mn. (The Economic Times)
- Suzlon Energy has upped the ante in the battle for REpower by increasing its offer to 150/share or 7.14% higher than French giant Areva's 140/share offer. (The Economic Times)

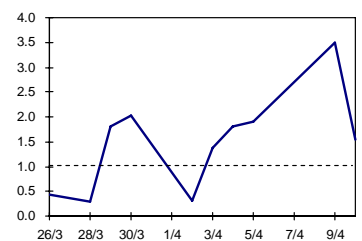
Market movement over last fortnight



Volumes in Rs mn (BSE and NSE)



Advances & Declines ratio (BSE)



Market data as on Apr 10, 2007

INDICES		
		% chg (DoD)
BSE Sensex	13190	0.09
S&P CNX Nifty	3848	(2.38)
BSE 100	6668	0.32
BSE 200	1576	0.34
Instanex Skindia DR	2273	1.56
Mindex	5536	(0.96)

OVERSEAS MARKETS

		% chg (DoD)
Dow Jones	12574	0.04
Nasdaq Comp.	2478	0.34
S&P 500	1448	0.26
Hang Seng	20348	0.68
Nikkei	17665	(0.45)

ADVANCES/DECLINES (BSE)

Group	A	B1	B2
Advances	134	442	476
Declines	70	252	357
Unchanged	2	18	32

FII TURNOVER (BSE+NSE)*

(Rs mn)	Bought	Sold	Net
	23,410	17,735	5,675

NEW HIGHS AND LOWS (BSE)

Group	A	B1	B2
Highs	4	14	13
Lows	-	1	4

CURRENCY

US\$1 = Rs42.85

* FII turnover (BSE + NSE) as on April 9, 2007

Quarterly Results Preview

PHARMA

In full bloom

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We expect the i-SEC pharma universe to record a strong 66% YoY surge in PAT in Q4FY07E, driven by 32% sales growth and 421bps EBITDA margin expansion. The key factors driving this growth are ANDAs with exclusivity, new launches, acquisitions, healthy growth in the domestic market and improved cost discipline. After accounting for this splendid performance, FY07E would end on a strong note with 62% YoY jump in PAT. Further, we expect the trend of positive newsflow on the drug discovery research front to continue in FY08 with Glenmark occupying centre stage. Based on our 'pick & choose' investment strategy, we reiterate Sun Pharma and Glenmark Pharma as the top BUYs among large-caps and Alembic as the preferred pick among mid-caps in the sector.

- **Growth engine – Full throttle ahead.** Despite a robust 60% YTD FY07 surge in PAT for the i-SEC pharma universe, we believe there is still scope for growth. Driven by product launches (including some with exclusivity), margin-accretive acquisitions, healthy growth in the domestic market, improving cost discipline and a strong 52% surge in exports (contributing 63% to total sales), aggregate net profits for the i-SEC pharma universe would likely grow 66% YoY to Rs10bn in Q4FY07E. We expect Dr. Reddy's Laboratories (DRL) to report the highest PAT in the universe at Rs2.1bn, scripting the biggest turnaround from a loss of Rs244mn a year ago. Among other companies, Sun Pharma would register the highest PAT growth at 55% YoY, whereas GSK Pharma would be the lowest with 1% PAT growth. Excluding DRL and Ranbaxy (with greater weightage and stronger results), the aggregate sales and PAT growth are at 21% and 25% respectively.
- **Drug discovery research stole the limelight in Q4FY07.** After Glenmark bagged an out-licensing deal for GRC8200 for €190mn (€25mn up-front already received) plus royalties in Q3FY07, drug discovery research remained in the news in Q4FY07 as well. Further, for the first time ever, Sun Pharma disclosed its R&D pipeline, which we value at ~US\$620mn (or Rs132/share). Sun Pharma's de-merged R&D entity, Sun Pharma Advanced Research (SPARC), would be listed by end-June '07, which we believe would create significant value over the next 3-5 years. Further, as per the modified new agreement, Ranbaxy would promote NCEs up to the proof-of-concept stage and if they reach the market, the company could potentially earn over US\$100mn milestone payment and double-digit royalties on sales.
- **Reiterate 'pick & choose' strategy for FY08.** Based on our Q4FY07E forecast, we expect FY07 to end on a high note with consolidated PAT for the sector surging 62% YoY to Rs42.8bn. On this high base, we expect a healthy 19% YoY PAT growth (29% excluding DRL) in FY08E on the back of new launches, full benefits from acquisitions and improved cost discipline. Additionally, we expect strong newsflow on the drug discovery research front. Also, on account of the defensive nature of the pharma business and India's global competitiveness, a likely receding risk appetite (given the choppy stock markets YTD FY07) as well as 20% underperformance in the past one year by the sector, our 'pick & choose' investment strategy assumes greater significance in FY08. On the back of this strategy, we expect our top BUYs (Sun and Glenmark) in the sector to generate ~25% RoI in FY08E.

Table 1: Quarterly summary

Company (Rs mn)	Sales			EBITDA			Recurring PAT		
	% change			% change			% change		
	JFM07*	YoY	QoQ	JFM07*	YoY	QoQ	JFM07*	YoY	QoQ
Sun Pharma	5,140	26.8	(4.8)	1,680	73.3	(3.1)	1,834	55.0	(7.8)
Glenmark	2,033	22.3	0.7	500	47.2	(3.4)	302	20.3	(6.4)
DRL	13,304	93.6	(9.8)	3,494	503.9	20.2	2,122	(970.9)	36.5
Cipla	10,503	23.4	26.7	2,476	37.3	12.9	2,090	22.2	13.4
Ranbaxy	15,694	24.2	(7.5)	1,919	34.8	(16.8)	924	36.6	(29.7)
Cadila	4,072	21.1	(11.6)	690	5.2	(16.1)	370	14.2	(24.8)
Alembic	1,619	15.4	(11.6)	243	16.1	(29.3)	129	22.4	(44.5)
Wockhardt	5,013	42.8	(4.8)	1,177	51.7	(3.6)	826	26.3	(5.2)
GSK Pharma	4,174	(2.1)	30.3	1,501	0.8	52.4	1,047	1.2	53.6
Aventis	2,316	16.0	5.0	608	16.4	35.1	436	12.1	17.8
Total	63,869	32.3	(1.1)	14,288	63.0	6.0	10,080	65.7	4.2

* January-March '07

Source: i-SEC Research

Details in our report '*In full bloom*' dated April 11, 2007.

Comment

AVIATION – Jet Airways (Hold)

Event: Jet Airways has reportedly revived its bid to acquire Air Sahara

Impact: Slightly negative for Jet. As per media reports, Jet Airways has once again revived its bid to acquire Air Sahara, possibly triggered by the Civil Aviation Ministry's comment that the deal did not fail earlier due to procedural delays. Jet has therefore decided to acquire Air Sahara rather than compensating it for the scrapped deal.

The acquisition would salvage Rs1.8bn invested in Air Sahara earlier and Rs5bn paid to Air Sahara's shareholders. Nevertheless, we believe, the net current outgo would still be high.

What does Jet Airways get from the deal?

- Possession of 20 Boeing 737s and 7 CRJ-200s (smaller aircraft operating on short haul destinations) that would, however, add to Jet's fleet complexity
- Increased access to airport infrastructure especially in light of the recent freeze on peak hour landing slots
- Network of airports and related physical assets, most of which, however, would be duplicated
- Widening the gap with competition, especially Kingfisher
- Likely synergies with economies of scale
- Availability of international landing rights

Deal valuation would need to be benchmarked taking in account that Jet is 5x the size of Air Sahara and trades at an EV of ~Rs12bn. Further, Jet's operations are close to profitability. Based on media reports, the current deal values Air Sahara in the Rs18.5-22bn range with the net current payout at ~Rs13-14bn.

At this valuation, Air Sahara's assets look expensive because of the following:

- A large portion of the infrastructure, human resources and route frequencies are overlapping
- All Air Sahara aircraft are on lease, agreements for which may not be as favourable for Jet
- Air Sahara's high cost operations may further pressurise Jet's overall profitability at a time when Jet is on the threshold of sustainable profitability
- The previously announced Air Sahara deal had potential value for Jet as it provided ready access to the US operations. Based on this, Jet had probably ordered its wide-bodied aircraft. However, with the approval for Jet's own US operations in place and the delay in initial plans (thus allowing other players to fuel their business plans), we do not see any material benefit from the Air Sahara deal at present
- As regards deals valuation, Air Deccan trades at a market capitalisation of less than Rs10bn despite commanding ~2.5x Air Sahara's market share, larger airport presence and a better brand image
- Similarly, SpiceJet commands higher market share as compared with Air Sahara apart from running cost efficient operations
- Air Sahara was valued at ~US\$300mn (Rs13.5bn) by Kingfisher last year; since then, Air Sahara's market share has almost halved

Imponderables

- What happens to Air Sahara's already ordered fleet for expansion? If Jet continues with the order, it would further pressurise Jet's balance sheet
- Jet's own expansion plan on domestic routes consists of adding 12 aircraft by FY09E, which may be reviewed after materialisation of the deal
- Would Jet possibly run Air Sahara as a low cost airline subsidiary?

The merger, nevertheless, augurs well for the industry since it would remove a weak player from the market. Further, the discontinuation of Air Sahara's indiscriminate discounts, in order to survive, would not hurt other airlines in the industry anymore.

Recent reports/updates		
Analyst	Company/Sector	Date
Rajesh Vora	Pharma Quarterly results preview: In full bloom	Apr 11
S. Ramesh / Amit	Oil&Gas Quarterly results preview: Full blast ahead	Apr 9
Anand / Shilpa Yadav	FMCG Quarterly results preview: On a promising note	Apr 9
Rajesh Vora	Wockhardt: On come-back trail	Apr 5
Poonam Nishal	Utilities Quarterly results preview: Waiting for Godot	Apr 5
Amar Kedia	Aviation Quarterly results preview: Mixed bag	Apr 3
Rajesh Vora	Glenmark Pharma: Raising the bar	Apr 3
Amar Kedia	SpiceJet: Tempest to blow past	Apr 3
Poonam Nishal	Telecom Quarterly results preview: Swelling volumes to script success	Apr 2
S. Ramesh	Gujarat Gas: Set for new highs	Mar 30
Rajesh Vora	Cadila Healthcare: Run to form	Mar 26
Amar Kedia	Balmer Lawrie: Stirring up	Mar 23
Anand Shah	Nestle: On an accelerated growth path	Mar 22
S. Ramesh	Netback margin monthly: Refining, the lone star shining	Mar 19
Rajesh Vora	Sun Pharma: The Sun SPARCles	Mar 16
Vikash Mantri	Jagran Prakashan (Unrated): Augmenting clout	Mar 15
Shilpa Gupta	Speedometer (Mar '07) – Balanced manoeuvre	Mar 14
Eq. Research Team	Union Budget Review 2007-08	Mar 1
S. Ramesh	Gujarat Gas Company: Higher gas costs hit margins	Feb 26
S. Ramesh	Netback margin monthly: Refining sweetens the pot	Feb 21
S. Ramesh	Oil&Gas sector update: Halcyon days ahead	Feb 15
Rajesh Vora	Dr. Reddy's Lab: Bolstering the base	Feb 9
Amar Kedia	Aviation Sector: Clear horizons	Feb 9
Anand Shah	Godrej Consumer: Outshining the rank	Feb 6
Poonam Nishal	Bharti Airtel: Ringing in success	Feb 5
Vinay Patel	Monetary policy review: Yet another surprise	Feb 1
Shekhar Singh	MphasiS: In the fray	Feb 1

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