Aventis Pharma

STOCK INFO.	BLOOMBERG
BSE Sensex: 13,024	HOEC IN
	REUTERS CODE
S&P CNX: 3,769	AVPH.BO

Equity Shares (m)	23.0
52-Week Range	2,140/1,241
1,6,12 Rel. Perf. (%)	-11/-32/-57
M.Cap. (Rs b)	34.8
M.Cap. (US$ b)	0.8

30 October 2006 **Buy**

Previous Recommendation: Buy Rs1,512

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
12/05A	8,019	1,602	69.6	11.2	21.7	6.9	31.6	46.4	4.0	14.0
12/06E	9,010	1,753	76.1	9.4	19.9	5.6	28.1	42.0	3.4	11.9
12/07E	9,975	1,924	83.5	9.8	18.1	4.6	25.7	38.5	2.9	10.4

Aventis Pharma reported 3QCY06 EBITDA margins below estimates while PAT was boosted by other income. Key highlights include:

- Net sales grew by 9% (vs estimate of 12%) while PAT grew by 8.2% (vs estimate of 4%). Domestic sales grew by 15% to Rs1.8b while exports de-grew by 6.2% to Rs636m. This is the fourth consecutive quarter of decline in exports. Supplies to Russia and sourcing by the parent are the two main components of exports for the company. As of now, we do not have details on the key factors leading to decline in exports. Domestic sales have grown by 16% while exports have declined by 8.7% YTD.
- We believe that domestic sales of the company's pain management portfolio would have benefited in the quarter due to the sudden incidence of flu, chickengunia and dengue in various parts of the country.
- EBITDA margins declined by 390bp to 28.3% (vs estimate of 31.4%) due to higher material consumption and a 25% increase in other expenditure. Other income increased 100% to Rs156m including an interest of Rs42m on income tax refund thus boosting PAT.

We believe that Aventis will be one of the key beneficiaries of the patent regime in the long-term. The parent has a strong R&D pipeline and plans to file 18 NDAs by CY08E. We continue to remain positive on Aventis' long-term prospects. It is currently valued at 19.9x CY06E and 18.1x CY07E earnings. Maintain **Buy**.

QUARTERLY PERFORMANCE (Rs Million)

Y/E DECEMBER	CY05				CY06				CY05	CY06E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Net Sales	**1,725**	**2,134**	**2,234**	**1,929**	**2,005**	**2,228**	**2,431**	**2,346**	**8,022**	**9,010**
YoY Change (%)	*5.4*	*17.1*	*19.1*	*-2.2*	*16.2*	*4.4*	*8.8*	*21.6*	*9.8*	*12.3*
Total Expenditure	1,330	1,510	1,515	1,426	1,503	1,609	1,744	1,586	5,781	6,442
EBITDA	**395**	**624**	**719**	**503**	**502**	**619**	**687**	**759**	**2,241**	**2,567**
Margins (%)	*22.9*	*29.2*	*32.2*	*26.1*	*25.0*	*27.8*	*28.3*	*32.4*	*27.9*	*28.5*
Depreciation	44	43	43	42	43	42	43	49	172	177
Interest	0	0	0	0	0	1	0	0	0	0
Other Income	74	61	78	82	86	90	156	-62	295	270
PBT before EO Items	**425**	**642**	**754**	**543**	**545**	**666**	**800**	**648**	**2,364**	**2,660**
Extra-Ord Expense	0	0	0	0	0	0	0	0	0	0
PBT after EO Items	**425**	**642**	**754**	**543**	**545**	**666**	**800**	**648**	**2,364**	**2,660**
Tax	189	300	257	167	176	227	262	242	913	907
Effective tax Rate (%)	*44.5*	*46.7*	*34.1*	*30.8*	*32.3*	*34.1*	*32.8*	*37.4*	*38.6*	*34.1*
Reported PAT	**236**	**342**	**497**	**376**	**369**	**439**	**538**	**406**	**1,451**	**1,753**
Adj PAT	**236**	**342**	**497**	**376**	**369**	**439**	**538**	**406**	**1,451**	**1,753**
YoY Change (%)	*-13.5*	*2.4*	*16.9*	*-7.4*	*56.4*	*28.4*	*8.2*	*8.0*	*0.7*	*20.8*
Margins (%)	*13.7*	*16.0*	*22.2*	*19.5*	*18.4*	*19.7*	*22.1*	*17.3*	*18.1*	*19.5*

E: MOSt Estimates

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Decline in exports restricts sales growth

Aventis's net sales for 3QCY06 grew by 9% to Rs2.4b, primarily driven by 15% YoY growth to Rs1.8b in domestic market. However, exports business de-grew (for fourth consecutive quarter) by 6.2% to Rs636m.

TREND IN MARKET MIX (RS M)

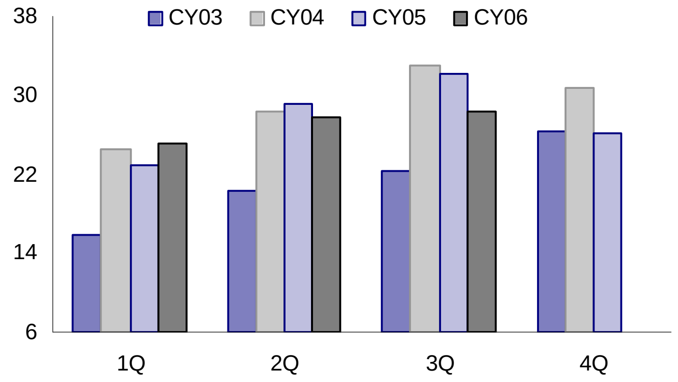
	3QCY06	3QCY05	YOY (%)	2QCY06	QOQ (%)
Net domestic sales	1795	1556	15.4	1712	4.8
% of sales	*73.8*	*69.7*		*76.8*	
Exports	636	678	-6.2	516	23.3
% of sales	*26.2*	*30.3*		*23.2*	
Net Sales	2431	2234	8.8	2228	9.1

Source: Company/Motilal Oswal Securities

EBITDA margins decline; higher other income boosts PAT

EBITDA margins declined by 390bp to 28.3% (vs estimate of 31.4%) mainly, due to higher material consumption and a 25% increase in other expenditure. Other income increased 100% to Rs156m including an interest of Rs42m on income tax refund, thus boosting PAT.

TREND IN EBITDA MARGIN (%)



Source: Company/ Motilal Oswal Securities

Withdrawal of Cox-II inhibitors may benefit Aventis India

We believe that the withdrawal of Rofecoxib and Valdecoxib (cox-II inhibitors) from the global and Indian markets due to adverse side effects may have a positive impact on the sales of older (and proven) painkillers like APL's Combiflam. Doctors and patients may not be willing to resort to cox-II inhibitors (including Rofecoxib, Celecoxib, Valdecoxib, etc) unless absolutely necessary. Historically, Combiflam has grown in single digits. Higher growth for Combiflam can have a positive impact on EBITDA margins since it commands a very high brand-equity. Products such as Combiflam are cash cows, and the company does not spend heavily on promotion for such products.

Aventis-Sanofi - Global merger

Sanofi has a 100% subsidiary in India, which is engaged in the marketing of the parent's products, especially in the CVS and CNS segments. APL's management had indicated that if this arm were to be merged with APL, it would be earnings accretive. While APL has not indicated any figures, we believe that Sanofi India has a small business generating about Rs1.0b of revenues.

On the positive side, there seems to be very little over-lap (except in the CVS segment) between APL's and Sanofi's product portfolios in the Indian market with the latter focusing on CVS and CNS segments. APL will draw strength from the combined R&D pipeline of the global parent, which has become the third largest player in the global pharmaceutical industry.

Sanofi (India) specializes in 4 main therapeutic groups, Thrombosis (major brands- Faxiparine, Tyklid and Plavix) Cardiovascular (Adenocor, Primacor) Neurlogy, (Valparin, Jume) and Internal Medicine (Ladogal Lactacyd, Fortagesic and Calcium Resonium).

New product launches may slow down

APL has been most aggressive in new launches amongst its peers and has launched most of the top products of the parent in India. Aventis launched Lantus (anti-diabetic) and Actonel (Osteoporosis) in the anti-diabetic and pain management segments in CY03. It has not launched any new products in CY04 and launched Apidra (anti-diabetic) in CY05. We believe that the parent's portfolio is very well mapped in the domestic entity, which leaves little scope of aggressive new launches going forward. The table below indicates the details on past launches as well as the status for potential new products.

AVENTIS – PORTFOLIO MAPPING WITH PARENT

PRODUCT	INDIA LAUNCH	LAUNCH YEAR	POSSIBILITY OF LAUNCH IN INDIA
Lovenox/Clexane	Y		N.A.
Plavix/Iscover - Sanofi Product	Y		N.A.
Allegra	Y	1998	N.A.
Taxotere	Y		N.A.
Stilnox/Ambien/Myslee - Sanofi Product	N		No - Global launch in 1992. Old product
Eloxatin - Sanofi Product	N		Yes - Global launch in 1996
Delix/Tritace/Triatec	Y	1994	N.A.
Lantus	Y	2003	N.A.
Aprovel/Avapro/Karvea - Sanofi Product	N		Yes - Global launch in 1997 But Indian companies have already launched this product
Copaxone	N		No – Product belongs to Teva
Amaryl	Y	1999	N.A.
Actonel	Y	2003	N.A.
Depakine - Sanofi Product	Y		N.A.
Nasacort - Sanofi Product	Status not known		
Xatral - Sanofi Product	N		Unlikely - It is a 1988 product

Source: Company/Motilal Oswal Securities

Well placed to benefit from the patent regime

Over the longer term, Aventis is well placed to benefit from the introduction of product patents, given its strengths in marketing, a supportive parent and a healthy product pipeline (of NCEs) following the formation of Sanofi-Aventis. Aventis' history of launching patented products in India, a well mapped portfolio vis-à-vis the parent and ability to build them into big brands make it one of the biggest potential beneficiaries of the product patent regime in India.

We believe that the patent regime will bring-in significant benefits for Aventis, albeit in the long-term. We expect launch of patented products from the parent's portfolio by 2008. Although clarity on this will emerge only by 2007, we present below our estimates of the potential upside to Aventis from the patent regime.

TABLE 1: AVENTIS - UPSIDE FROM PATENTED PRODUCTS (RS M)

	CY08	CY09	CY10	CY11	CY12	CY13	CY14	CY15
No. of Patented Products Launched	1	2	2	1	1	1	1	1
Total No. of Patented Products on Market	1	3	5	6	7	8	9	10
Product A	250	500	1,000	1,200	1,440	1,584	1,742	1,917
Product B	0	250	500	1,000	1,200	1,440	1,584	1,742
Product C	0	250	500	1,000	1,200	1,440	1,584	1,742
Product D	0	0	250	500	1,000	1,200	1,440	1,584
Product E	0	0	250	500	1,000	1,200	1,440	1,584
Product F	0	0	0	250	500	1,000	1,200	1,440
Product G	0	0	0	0	250	500	1,000	1,200
Product H	0	0	0	0	0	250	500	1,000
Product I	0	0	0	0	0	0	250	500
Product J	0	0	0	0	0	0	0	250
Total Sales	**250**	**1,000**	**2,500**	**4,450**	**6,590**	**8,614**	**10,740**	**12,959**
NPM (%) - Assumed	20	20	20	20	20	20	20	20
Net Profit	**50**	**200**	**500**	**890**	**1,318**	**1,723**	**2,148**	**2,592**
Incremental EPS (Rs)	2	9	22	39	57	75	93	113
P/E for patented products (x)	40	40	40	40	40	40	40	40
Valuation for patented products (Rs/share)	87	347	868	1,546	2,289	2,992	3,731	4,502

Source: Motilal Oswal Securities

TABLE 2: SANOFI-AVENTIS R&D PIPELINE

NO. OF DRUGS	PRE-CLINICAL	PHASE I	PHASE IIA	PHASE IIB	PHASE III	TOTAL
Cardiovascular	5	3	2	4	1	15
Thrombosis	4	1	1	3	1	10
Central Nervous System	10	6	3	2	7	28
Oncology	7	4	3	1	4	19
Metabolic Disorders	4	4	3	2	1	14
Internal Medicine	6	6	4	2	2	20
Vaccines	9	2	4	4	2	21
Total	**45**	**26**	**20**	**18**	**18**	**127**

Source: Sanofi-Aventis

To benefit from the parent's R&D pipeline

Sanofi-Aventis currently has 127 projects in research and development, including about 71 in clinical development and 56 in late stage (Phase II & III) development. It is planning to file about 11 NDAs and 7 vaccines by CY08E. The table above gives details on the parent's R&D pipeline.

Although, clarity on launch of these drugs will emerge only over a period of time, we believe that some of these products could be relevant for the Indian markets and are likely to be launched in India with a time-lag.

New drug policy still remains uncertain

The government is yet to finalize the new pharmaceutical policy. While it had proposed bringing the Essential Drug's List (consisting of 354 drugs) under price control, the industry has stiffly opposed it. This has prompted the government to appoint a committee consisting of members, both from the government and the industry to find an alternative to make drugs more affordable to the masses without drastically hurting the industry's pricing flexibility. This committee is yet to give its final recommendations to the government. While the contents of this proposed policy still remain uncertain, any attempt to bring in a significant number of drugs under government mandated price controls is likely to hurt the industry and all its players including APL.

Valuation and outlook

APL has an impeccable track record of brand building in the domestic market with its strategic brands recording double digit growth consistently. In the long-term, focus on growing strategic brands and strong support from the parent will augur well for the company. We believe that it is very well positioned to take advantage of the patent regime in the long-term. It is in the process of integrating Sanofi's domestic operation with itself (post the global merger). We believe that there is very little over-lap between APL and Sanofi's portfolio in India.

We believe that Aventis will be one of the key beneficiaries of the patent regime in the long-term. The parent has a strong R&D pipeline and plans to file 18 NDAs by CY08E. We continue to remain positive on Aventis' long-term prospects. It is currently valued at 19.9x CY06E and 18.1x CY07E earnings. Maintain **Buy**.

Aventis Pharma: an investment profile

Company description

Aventis (50% subsidiary of Aventis SA) is the second largest MNC and among the top 10 formulations players in India. The company has built a very strong franchise in chronic therapy areas like anti-diabetes, oncology and CVS, in the process realigning its domestic portfolio with that of its parent. Aventis is currently undergoing transformation, with the parent being taken over by Sanofi Synthelabo worldwide.

Key investment arguments

- Significant improvement in product mix, with enhanced focus on strategic products and rationalization of older products has put it back on the growth path.
- Aggressive cost cutting and improved efficiencies to add to revenue growth and boost operating performance.
- Strong parental commitment and excellent brand equity among doctors make it the best placed MNC to gain from the IPR regime. Parent plans 18 NDA filings by CY08.

Key investment risks

- Sanofi's acquisition of Aventis SA could hamper Indian operations if new parent is not committed
- Exports have been de-growing for the last four quarters
- The proposed new drug policy could adversely impact APL.

Valuation and view

- Valuations of 19.9x CY06E and 18.1x CY07E earnings do not fully factor-in the future prospects, excellent return ratios and free cash on books (around Rs 186/ share in CY06E).
- Maintain **Buy** with a target price of Rs2,100

Sector view

- Indian Pharma market expected to witness steady growth, on the back of gradual increase in the low penetration levels - companies with strong brands and marketing muscle to benefit the most
- IPR regime unlikely to lead to any major change in the near term; MNCs and large Indian players to benefit over the longer term.
- Among MNCs, we are bullish on companies where risk of conflict with 100% subsidiaries is limited.

COMPARATIVE VALUATIONS

		AVENTIS	GSK	PFIZER
P/E(x)	FY07E	19.9	25.6	22.4
	FY08E	18.1	24.3	25.4
P/BV(x)	FY07E	5.6	7.1	5.8
	FY08E	4.6	6.0	5.3
EV/Sales(x)	FY07E	3.4	5.3	3.3
	FY08E	2.9	4.8	3.6
EV/EBITDA(x)	FY07E	11.9	16.8	14.0
	FY08E	10.4	15.7	15.4

SHAREHOLDING PATTERN (%)

	SEP.06	JUN.06	SEP.05
Promoter	60.4	60.4	60.4
Domestic Inst	18.9	15.8	15.7
Foreign	9.8	13.1	12.8
Others	11.0	10.8	11.1

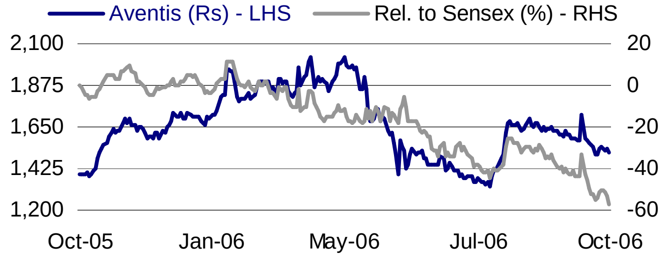
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
CY06	76.1	77.6	-1.9
CY07	83.5	88.7	-5.8

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
1,512	2,100	38.9	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					(Rs Million)
Y/E DECEMBER	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Exports	2,041	2,287	2,566	2,951	3,394
Net Domestic Sales	5,266	5,732	6,444	7,024	7,726
Net Sales	**7,307**	**8,019**	**9,010**	**9,975**	**11,120**
Change (%)	*12.0*	*9.8*	*12.3*	*10.7*	*11.5*
Total Expenditure	5,162	5,741	6,442	7,171	7,986
EBITDA	**2,145**	**2,278**	**2,567**	**2,803**	**3,134**
Change (%)	*53.5*	*6.2*	*12.7*	*9.2*	*11.8*
Margin (%)	*29.4*	*28.4*	*28.5*	*28.1*	*28.2*
Depreciation	168	172	177	195	205
Int. and Finance Charges	1	0	0	0	0
Other Income - Rec.	218	295	270	311	378
PBT & EO Items	**2,194**	**2,401**	**2,660**	**2,920**	**3,307**
Change (%)	*58.9*	*9.4*	*10.8*	*9.8*	*13.3*
Extra Ordinary Income/(Exp)	68	0	0	0	0
PBT after EO Items	**2,262**	**2,401**	**2,660**	**2,920**	**3,307**
Tax	777	799	907	996	1,128
Tax Rate (%)	*34.4*	*33.3*	*34.1*	*34.1*	*34.1*
Reported PAT	**1,485**	**1,602**	**1,753**	**1,924**	**2,179**
PAT Adj for EO Items	**1,440**	**1,602**	**1,753**	**1,924**	**2,179**
Change (%)	*53.5*	*11.2*	*9.4*	*9.8*	*13.3*
Margin (%)	*19.7*	*20.0*	*19.5*	*19.3*	*19.6*

BALANCE SHEET					(Rs Million)
Y/E DECEMBER	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Equity Share Capital	230	230	230	230	230
Reserves	3,810	4,838	6,000	7,267	8,725
Revaluation Reserves	178	170	161	153	145
Net Worth	**4,218**	**5,238**	**6,392**	**7,651**	**9,100**
Loans	0	0	0	0	0
Deferred Tax Liabilities	-5	-57	-57	-57	-57
Capital Employed	**4,213**	**5,181**	**6,334**	**7,594**	**9,043**
Gross Block	2,742	2,794	2,924	3,074	3,233
Less: Accum. Deprn.	1,225	1,389	1,575	1,778	1,991
Net Fixed Assets	**1,517**	**1,405**	**1,349**	**1,296**	**1,241**
Capital WIP	28	13	25	25	25
Investments	53	53	53	53	53
Curr. Assets	**4,111**	**5,419**	**6,321**	**7,793**	**9,468**
Inventory	1,016	1,363	916	944	979
Account Receivables	918	510	924	1,022	1,138
Cash and Bank Balance	1,673	2,944	4,253	5,594	7,112
Others	504	601	228	233	239
Curr. Liability & Prov.	**1,496**	**1,710**	**1,414**	**1,574**	**1,745**
Account Payables	665	846	823	917	1,023
Provisions	831	864	591	656	722
Net Current Assets	**2,616**	**3,709**	**4,907**	**6,219**	**7,723**
Appl. of Funds	**4,213**	**5,181**	**6,334**	**7,594**	**9,043**

E: MOSt Estimates

RATIOS					
Y/E DECEMBER	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Basic (Rs)					
EPS	**62.5**	**69.6**	**76.1**	**83.5**	**94.6**
Cash EPS	69.8	77.0	83.8	92.0	103.5
BV/Share	175.4	220.1	270.5	325.6	388.8
DPS	16.0	16.0	22.5	25.0	27.5
Payout (%)	28.1	26.4	33.7	34.1	33.1
Valuation (x)					
P/E	24.2	21.7	19.9	18.1	16.0
Cash P/E	21.6	19.6	18.0	16.4	14.6
P/BV	8.6	6.9	5.6	4.6	3.9
EV/Sales	4.5	4.0	3.4	2.9	2.5
EV/EBITDA	15.5	14.0	11.9	10.4	8.8
Dividend Yield (%)	1.1	1.1	1.5	1.7	1.8
Return Ratios (%)					
RoE	35.6	31.6	28.1	25.7	24.3
RoCE	52.1	46.4	42.0	38.5	36.6
Working Capital Ratios					
Asset Turnover (x)	1.7	1.5	1.4	1.3	1.2
Debtor (Days)	46	23	37	37	37
Inventory (Days)	51	62	37	35	32
Working Capital (Days)	47	35	26	23	20
Leverage Ratio					
Current Ratio	2.7	3.2	4.5	5.0	5.4
Debt/Equity	0.0	0.0	0.0	0.0	0.0

CASH FLOW STATEMENT					(Rs Million)
Y/E DECEMBER	**2004**	**2005**	**2006E**	**2007E**	**2008E**
OP/(Loss) before Tax	2,145	2,278	2,567	2,803	3,134
Interest/Dividends Recd.	218	295	270	311	378
Direct Taxes Paid	-772	-851	-907	-996	-1,128
(Inc)/Dec in WC	-560	177	112	28	14
CF from Operations	**1,032**	**1,900**	**2,042**	**2,147**	**2,398**
EO Items	68	0	0	0	0
CF from Ope (EO items)	**1,100**	**1,900**	**2,042**	**2,147**	**2,398**
(Inc)/Dec in FA	-73	-54	-142	-150	-158
(Pur)/Sale of Investments	0	0	0	0	0
CF from Investments	**-73**	**-54**	**-141**	**-150**	**-158**
Issue of Shares	-54	-151	0	0	0
(Inc)/Dec in Debt	-152	0	0	0	0
Interest Paid	-1	0	0	0	0
Dividend Paid	-417	-423	-591	-656	-722
CF from Fin. Activity	**-625**	**-574**	**-591**	**-656**	**-722**
Inc/Dec of Cash	**402**	**1,271**	**1,310**	**1,341**	**1,518**
Add: Beginning Balance	1,271	1,673	2,944	4,253	5,594
Closing Balance	**1,673**	**2,944**	**4,253**	**5,594**	**7,112**

N O T E S

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Disclosure of Interest Statement	Aventis Pharma
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No