



## Jubilant Organosys

STOCK INFO.	BLOOMBERG
BSE Sensex: 12,858	JOL IN
	REUTERS CODE
S&P CNX: 3,711	JUBO.BO

18 October 2006

Buy

Previous Recommendation: Buy

Rs208

Equity Shares (m)	142.3
52-Week Range	290/180
1,6,12 Rel. Perf. (%)	-3/-26/-62
M.Cap. (Rs b)	29.6
M.Cap. (US\$ b)	0.6

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
03/06A	15,054	1,297	8.6	-1.2	24.2	3.6	19.6	15.4	2.4	16.3
03/07E	19,136	2,144	11.6	34.7	18.0	2.6	21.9	11.5	1.7	9.7
03/08E	21,853	2,913	15.7	35.8	13.2	2.1	23.0	10.2	1.4	7.0

Jubilant Organosys 2QFY07 results were in-line with expectations, with lower molasses prices and higher contribution from Pharma and Life Science business being the key profit drivers. Key Highlights:

- Net sales increased by 40.5% to Rs4.65b while PAT improved by 118% to Rs544m led mainly by 87% growth in Pharma & Life Science (PLSP) business (53% of total sales).
- EBITDA increased by 76% while EBITDA margins increased by 344bp to 17.2% (vs our estimates of 18.1%) led mainly by better product realizations, supply of Oxcarbazepine to the US and lower input costs (mainly molasses and ethanol). Higher staff costs (up 122%) related to recruitment of scientists for the contract research business and lower prices for acetyl products has resulted in EBITDA margins lower than our estimates.
- Jubilant has commenced supplies of Oxcarbazepine API (Novartis' Trileptal) to its partners in the US. Currently, Jubilant is the sole supplier of this product. However, an additional patent filing by Novartis has delayed the final ANDA approvals for Jubilant's partners, which have already started sourcing from Jubilant in anticipation of ANDA approvals. The company expects its partners to launch this product over the next 1-2 months.

Jubilant is likely to benefit from the increased pharmaceutical/intermediates outsourcing from India due to its existing relationships with global pharmaceutical and agrochemical players. With expected PAT CAGR of 40% for FY06-08, valuations at 17.5x FY07E and 12.9x FY08E consolidated fully diluted earnings appears reasonable. Management has guided 2HFY07 to be better than 1H FY07. Maintain **Buy**.

### QUARTERLY PERFORMANCE

(Rs Million)

Y/E MARCH	FY06				FY07				FY06	FY07E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
<b>Net Sales</b>	<b>3,267</b>	<b>3,315</b>	<b>4,234</b>	<b>4,238</b>	<b>4,124</b>	<b>4,659</b>	<b>5,246</b>	<b>5,106</b>	<b>15,054</b>	<b>19,136</b>
YoY Change (%)	22.8	12.9	46.5	31.8	26.2	40.5	23.9	20.5	28.6	27.1
Total Expenditure	2,873	2,859	3,588	3,545	3,425	3,858	4,262	4,189	12,884	15,734
<b>EBITDA</b>	<b>394</b>	<b>456</b>	<b>646</b>	<b>693</b>	<b>699</b>	<b>801</b>	<b>984</b>	<b>918</b>	<b>2,170</b>	<b>3,402</b>
Margins (%)	12.1	13.8	15.3	16.4	16.9	17.2	18.8	18.0	14.4	17.8
Depreciation	111	118	129	155	146	153	168	152	513	619
Interest	49	40	54	30	55	37	110	177	173	379
Other Income	31	34	36	96	90	145	113	125	197	473
<b>PBT after EO Expense</b>	<b>265</b>	<b>332</b>	<b>499</b>	<b>604</b>	<b>588</b>	<b>756</b>	<b>819</b>	<b>713</b>	<b>1,681</b>	<b>2,876</b>
Tax	55	80	121	136	139	215	74	-169	392	259
Deferred Tax	0	0	0	0	0	0	132	331	0	462
Rate (%)	20.8	24.1	24.2	22.5	23.6	28.4	25.1	22.7	23.3	25.1
<b>PAT</b>	<b>210</b>	<b>252</b>	<b>378</b>	<b>468</b>	<b>449</b>	<b>541</b>	<b>614</b>	<b>551</b>	<b>1,289</b>	<b>2,155</b>
Minority Interest	-3	3	12	-14	-12	-3	3	23	-8	11
<b>Adjusted PAT</b>	<b>213</b>	<b>249</b>	<b>366</b>	<b>482</b>	<b>461</b>	<b>544</b>	<b>611</b>	<b>529</b>	<b>1,297</b>	<b>2,144</b>
YoY Change (%)	-20.8	-19.9	36.1	73.8	116.4	118.5	66.9	9.7	17.7	65.3
Margins (%)	6.5	7.5	8.6	11.4	11.2	11.7	11.6	10.4	8.6	11.2

E: M0St Estimates

### Pharma and Life Science (PLSC) business drives revenue growth

Jubilant Organosys reported a 40% YoY growth in revenues (to Rs4.6b) for 2QFY07. Growth was largely driven by 87% YoY growth (to Rs2.4b) in the PLSC business. The industrial chemical business grew by 13% YoY (to Rs1.6b), driven primarily by volume growth. The performance chemical business, however, grew by only 5% YoY due to restructuring of product portfolio in favor of more profitable products.

Although some part of the growth was driven by consolidation of recently acquired Trinity Labs and Target Research, contributions from these entities are very marginal.

#### TREND IN PRODUCT MIX (RS M)

	2Q		YOY GR. (%)	1QFY07	QOQ GR. (%)
	FY07	FY06			
Pharma & LifeScie.	2,472	1,325	86.6	2,072	19.3
% of sales	53.1	40.2	50.2		
Performance Chem.	536	510	5.1	478	12.1
% of sales	11.5	15.5		11.6	
Industrial Chem.	1,651	1,461	13.0	1,574	4.9
% of sales	35.4	44.3		38.2	
<b>Total Revenues</b>	<b>4,659</b>	<b>3,296</b>	<b>41.4</b>	<b>4,124</b>	<b>13.0</b>

Source: Company/ Motilal Oswal Securities

### International operations drive revenue growth

Domestic operations grew by 3.8% YoY to Rs2.35b, whereas exports grew at 124% YoY. Growth in international operations was driven by an 218% YoY growth in regulated markets due to consolidation of recent acquisitions, higher growth in the CRAMS business and commencement of supplies of Oxcarbazepine API to the US markets.

	2Q		YOY GR. (%)	1QFY07	QOQ GR. (%)
	FY07	FY06			
Domestic	2,356	2,269	3.8	2,346	0.4
% of sales	50.6	68.8		56.9	
<b>International operations</b>					
Regulated markets	1,709	537	218.2	1,227	39.3
% of sales	36.7	16.3		29.7	
Other Markets	594	490	21.2	552	7.6
% of sales	12.7	14.9		13.4	
Total Internat. operations	2,303	1,027	124.2	1,779	29.5
% of sales	49.4	31.2		43.1	
<b>Total Rev.</b>	<b>4,659</b>	<b>3,296</b>	<b>41.4</b>	<b>4,125</b>	<b>12.9</b>

Source: Company/ Motilal Oswal Securities

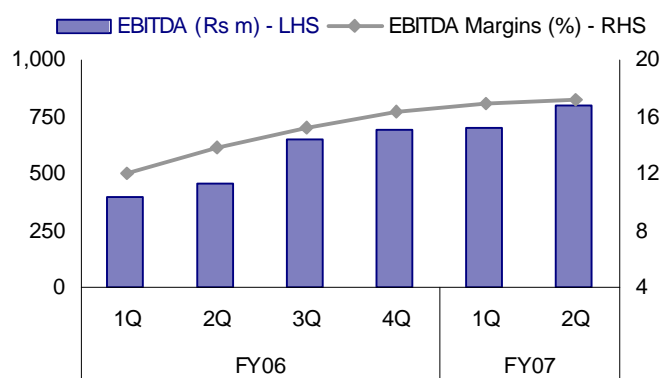
### Lower molasses prices aids margin expansion

Reduction in input costs (mainly Molasses) helped the company to improve EBITDA margins by 344bp to 17.2% for the quarter. Molasses prices have declined by about 20-25% due to the good sugarcane crop. Jubilant is reaping the benefits of lower Molasses and Ethanol prices as these are the key inputs for the company. While the recent sugar crop has been good (which will lead to higher Molasses supplies), the 5% Ethanol blending with petrol may impact Ethanol prices. Jubilant management has indicated that it does not expect any adverse input cost scenario in the coming quarters.

### Contribution of subsidiaries is improving

The company reported a consolidated PAT of Rs544m (vs stand-alone PAT of Rs542m) as compared to 2QFY06 consolidated PAT of Rs236m (vs stand-alone PAT of 269m). Management has guided that the contract research business (through its subsidiaries - Chemsys, Biosys & Clinsys) will witness improved performance in 2HFY07. This is also vindicated by the fact that the staff costs for 2Q are up 122% as the company hired more scientists for its contract research business.

#### TREND IN EBITDA



Source: Company/ Motilal Oswal Securities

### **CRAMS business: to be key growth driver**

The CRAMS division is expected to do well with increase in volumes of CRAMS I (fine chemicals) due to expanded capacity and robust business environment for CRAMS II (advance intermediates) on account of higher volumes due to addition of new products (around 3-4 every quarter), higher price realizations and softer raw material prices. Also, integration of Jubilant Clinsys with Target Research Associates, the CRO acquired in USA, will strengthen Jubilant's presence in clinical research business as it would be able to offer full service clinical operations along with data management services. We expect Jubilant's CRAMS business (including contract research) to record 36% CAGR for FY06-08.

### **Oxcarbazepine: New patent by Novartis could delay the opportunity**

Oxcarbazepine (Trileptal) is expected to be a major growth driver for Jubilant over the next couple of years. Trileptal is Novartis' US\$700m anti-epilepsy product, which went off-patent in July 2005 (including pediatric exclusivity). Although there are 10 DMFs filed for this product, Jubilant has already tied up with around 6-8 generic companies, including most of the major players, for API supply - of these, 5 have already filed their ANDAs. We believe that the ANDA approvals for Jubilant's customers in the US for Oxcarbazepine have been delayed as Novartis (the innovator) has filed a new patent expiring in Feb'2018. Jubilant has commenced supplies of Oxcarbazepine API (Novartis' Trileptal) to its partners in the US. Currently, Jubilant is the sole supplier of this product. Its partners have already started sourcing from Jubilant in anticipation of ANDA approvals. The company expects its partners to launch this product over the next 1-2 months.

### **Raised US\$200m through FCCB**

The company recently concluded its US\$200m FCCB issue priced at Rs413.45/share, with zero coupon and YTM of 7.2% maturing in 5 years. This issue was part of US\$325m in-principle approval which the company sought for growth initiatives through acquisitions and capex.

### **Targeting acquisitions in CRAMS space**

Jubilant is evaluating acquisitions in the CRAMS space with focus on getting access to more clients, critical technologies and backward integration synergies with Jubilant. Any potential acquisition is likely to be funded by the FCCB proceeds.

### **Current stock price is at significant discount to FCCB conversion**

Jubilant's current stock price (Rs208/share) is at a significant discount to the conversion rate of Rs413/share for the last of the three FCCB issues. Although, this is a 5-year FCCB with conversion planned for 2011, we believe that the company will have to make significant business initiatives (including acquisitions) and scale up the CRAMS business substantially to compel the FCCB holders to convert their bonds into equity.

### **Well placed to tap emerging opportunities**

Jubilant has achieved global scale and presence without putting undue strain on its balance sheet or profitability and return ratios. Over the last three years (FY03-06), Jubilant has expanded its revenues and gross block at a CAGR of 28% and 27% respectively, while net profit has grown at 57% CAGR. Moreover, the company has been able to achieve this while maintaining healthy return ratios in excess of 20% over this period. Also, the potential acquisition which the company is targeting could catapult Jubilant into different league. With expected EPS CAGR of 40% for FY06-08, valuations at 17.5x FY07E and 12.9x FY08E consolidated fully diluted earnings appears reasonable. Maintain **Buy**.

## Jubilant Organosys: an investment profile

### Company description

Jubilant Organosys Limited is the largest specialty chemicals company in India with high degree of vertical integration along with global scale and reach in almost all its key products. Its business model thus spans pharmaceuticals & life sciences, industrial chemicals and performance chemicals. It has forayed into API business (by acquiring Max India's API operations) and into formulations and regulatory services (by acquiring PSI n.v and PSI supply).

### Key investment arguments

- ✍ A composite and integrated player with offerings across the pharma and specialty chemicals value chain
- ✍ Growing share of the profitable Pharma business, driven by APIs (Lamotrigine & Oxcarbazepine) & CRAMS business, to ensure improved profitability, return ratios and earnings visibility

### Key investment risks

- ✍ Volatility in Molasses prices may impact the profitability of Industrial Chemicals division.
- ✍ Ability to maintain its strong relationships with global clients and build on them is critical for continued success
- ✍ Severe pricing pressure in regulated markets could impact the company's future revenues and profitability

### Recent developments

- ✍ Has raised US\$200m with conversion at Rs413.45/share for funding capex and potential acquisitions.

### Valuation and view

- ✍ Growing share of P&LS business to boost profitability and improve quality of earnings
- ✍ With global scale and reach in place, it is well placed to capitalize on the emerging opportunities for Indian pharma companies
- ✍ Valuations at 17.5x FY07E and 12.9 FY08E EPS do not fully reflect strong earnings growth and healthy return ratios, leaving room for re-rating; **Maintain Buy.**

### Sector view

- ✍ Regulated markets would remain the key sales and profit drivers in the medium term
- ✍ We are overweight on companies that are towards the end of the investment phase

#### COMPARATIVE VALUATIONS

		JUBILANT	DIVIS	NPIL
P/E (x)	FY07E	18.0	29.8	24.4
	FY08E	13.2	24.6	18.2
P/BV (x)	FY07E	2.6	7.3	4.9
	FY08E	2.1	5.9	4.3
EV/Sales (x)	FY07E	1.7	5.1	2.4
	FY08E	1.4	4.6	2.1
EV/EBITDA (x)	FY07E	9.7	19.0	15.5
	FY08E	7.0	16.3	12.7

#### SHAREHOLDING PATTERN (%)

	SEP.06	JUN.06	SEP.05
Promoter	52.0	52.0	53.2
Domestic Inst	2.2	1.8	2.3
Foreign	35.9	29.8	29.5
Others	10.0	16.4	15.0

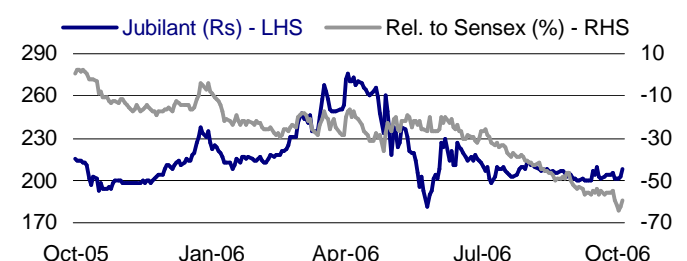
#### EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	12.1	12.9	-6.1
FY08	16.4	17.5	-6.3

#### TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
208	260	25.0	Buy

#### STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT		(Rs Million)				
Y/E MARCH	2005	2006	2007E	2008E	2009E	
<b>Net Sales</b>	<b>11,703</b>	<b>15,054</b>	<b>19,136</b>	<b>21,853</b>	<b>25,231</b>	
Change (%)	36.2	28.6	27.1	14.2	15.5	
<b>EBITDA</b>	<b>2,077</b>	<b>2,170</b>	<b>3,402</b>	<b>4,364</b>	<b>4,883</b>	
Margin (%)	17.7	14.4	17.8	20.0	19.4	
Depreciation	381	513	619	694	751	
<b>EBIT</b>	<b>1,696</b>	<b>1,657</b>	<b>2,783</b>	<b>3,670</b>	<b>4,132</b>	
Int. and Finance Charges	220	173	379	339	213	
Other Income - Rec.	166	197	473	580	564	
<b>PBT</b>	<b>1,642</b>	<b>1,681</b>	<b>2,876</b>	<b>3,911</b>	<b>4,484</b>	
Current Tax	316	254	259	352	404	
Deferred Tax	116	139	462	629	722	
Tax Rate (%)	26.3	23.3	25.1	25.1	25.1	
<b>PAT</b>	<b>1,210</b>	<b>1,289</b>	<b>2,155</b>	<b>2,931</b>	<b>3,358</b>	
Less: Minority Interest	18	-8	11	17	24	
<b>Adj Net Profit</b>	<b>1,192</b>	<b>1,297</b>	<b>2,144</b>	<b>2,913</b>	<b>3,334</b>	
Change (%)	52.4	8.8	65.4	35.9	14.4	
Margin (%)	10.2	8.6	11.2	13.3	13.2	

BALANCE SHEET		(Rs Million)				
Y/E MARCH	2005	2006	2007E	2008E	2009E	
Equity Share Capital	130	142	142	142	142	
Fully Diluted Share Capital	139	151	186	186	186	
Total Reserves	4,915	8,115	11,288	13,826	16,749	
<b>Net Worth</b>	<b>5,045</b>	<b>8,257</b>	<b>11,430</b>	<b>13,968</b>	<b>16,891</b>	
Minority Interest	51	151	162	179	203	
Deferred liabilities	858	1042	1504	2133	2855	
Total Loans	3,719	7,220	29,930	27,740	27,519	
<b>Capital Employed</b>	<b>9,672</b>	<b>16,670</b>	<b>43,026</b>	<b>44,020</b>	<b>47,468</b>	
Gross Block	8,702	11,372	13,372	14,372	15,662	
Less: Accum. Deprn.	3,151	3,779	4,398	5,091	5,842	
<b>Net Fixed Assets</b>	<b>5,551</b>	<b>7,593</b>	<b>8,974</b>	<b>9,281</b>	<b>9,820</b>	
Capital WIP	977	1,290	1,290	1,290	525	
Goodwill	741	2,649	2,344	2,344	2,344	
<b>Curr. Assets</b>	<b>5,298</b>	<b>8,949</b>	<b>34,746</b>	<b>36,084</b>	<b>40,419</b>	
Inventory	1,937	3,117	3,062	3,537	4,121	
Account Receivables	1,765	2,479	3,381	3,901	4,541	
Cash and Bank Balance	376	1,390	26,603	26,704	29,514	
Loans & Advances	1,220	1,963	1,701	1,943	2,243	
<b>Curr. Liability &amp; Prov.</b>	<b>2,953</b>	<b>3,844</b>	<b>4,364</b>	<b>5,014</b>	<b>5,675</b>	
Account Payables	2,223	2,693	3,083	3,521	4,065	
Provisions	730	1,152	1,281	1,493	1,610	
<b>Net Current Assets</b>	<b>2,346</b>	<b>5,105</b>	<b>30,383</b>	<b>31,070</b>	<b>34,744</b>	
Misc Expenditure	56	32	32	32	32	
<b>Appl. of Funds</b>	<b>9,672</b>	<b>16,670</b>	<b>43,025</b>	<b>44,019</b>	<b>47,468</b>	

E: M OSt Estimates

RATIOS						
Y/E MARCH	2005	2006	2007E	2008E	2009E	
<b>Basic (Rs)</b>						
<b>EPS</b>	<b>9.2</b>	<b>9.1</b>	<b>15.1</b>	<b>20.5</b>	<b>23.4</b>	
<b>Fully Diluted EPS</b>	<b>8.7</b>	<b>8.6</b>	<b>11.6</b>	<b>15.7</b>	<b>18.0</b>	
Cash EPS	11.3	12.0	14.9	19.4	22.0	
BV/Share	38.5	57.8	80.1	98.0	118.5	
DPS	1.3	1.3	2.0	2.8	3.2	
Payout (%)	15.5	16.1	15.5	15.5	15.5	
<b>Valuation (x)</b>						
P/E (on fully diluted EPS)	23.9	24.2	18.0	13.2	11.6	
Cash P/E	18.4	17.4	14.0	10.7	9.4	
P/BV	5.4	3.6	2.6	2.1	1.8	
EV/Sales	2.8	2.4	1.7	1.4	1.1	
EV/EBITDA	15.8	16.3	9.7	7.0	5.6	
Dividend Yield (%)	0.6	0.6	1.0	1.3	1.5	
<b>Return Ratios (%)</b>						
RoE	33.7	19.6	21.9	23.0	21.7	
RoCE	24.8	15.4	11.5	10.2	10.9	
<b>Working Capital Ratios</b>						
Asset Turnover (x)	12	0.9	0.4	0.5	0.5	
Debtor (Days)	55	60	64	65	66	
Inventory (Days)	60	76	58	59	60	
Working Capital Turnover (Days)	73	124	580	519	503	
<b>Leverage Ratio (x)</b>						
Current Ratio	1.8	2.3	8.0	7.2	7.1	
Debt/Equity	0.8	0.9	2.7	2.0	1.7	

CASH FLOW STATEMENT		(Rs Million)				
Y/E MARCH	2005	2006	2007E	2008E	2009E	
Oper. Profit/(Loss) before Tax	2,255	2,190	3,472	4,474	5,035	
Interest/Dividends Recd.	166	197	473	580	564	
(Inc)/Dec in WC	317	-1,693	-25	-545	-823	
<b>CF from Operating incl EO</b>	<b>2,362</b>	<b>436</b>	<b>3,642</b>	<b>4,128</b>	<b>4,331</b>	
(inc)/dec in FA	-1,807	-4,891	-1,696	-1,001	-526	
(Pur)/Sale of Investments	-2	0	0	0	0	
<b>CF from investments</b>	<b>-1,809</b>	<b>-4,891</b>	<b>-1,696</b>	<b>-1,001</b>	<b>-526</b>	
Issue of Shares	1,918	2,133	0	0	0	
Inc/(Dec) in Debt	-491	3,470	22,671	-2,263	-253	
Interest Paid	-227	-173	-379	-339	-213	
Dividend Paid	-185	-209	-332	-452	-517	
<b>CF from Fin. Activity</b>	<b>1,014</b>	<b>5,221</b>	<b>21,959</b>	<b>-3,053</b>	<b>-982</b>	
<b>Inc/Dec of Cash</b>	<b>1,567</b>	<b>766</b>	<b>23,905</b>	<b>74</b>	<b>2,823</b>	
Add: Beginning Balance*	334	376	1,390	26,603	26,704	
<b>Closing Balance</b>	<b>1,901</b>	<b>1,142</b>	<b>25,294</b>	<b>26,676</b>	<b>29,527</b>	

\*Cl. &amp; Opn. cash balances for FY03, FY04 and FY05 do not match due to acquisition

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**Disclosure of Interest Statement**

**Jubilant Organosys**

- |   |    |
|---|----|
| 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 |

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