

Results below expectations

23rd January 2009

BUY

Price	Target Price
Rs214	Rs304

Sensex –	8,814
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Price Performance

(%)	1M	3M	6M	12M
Absolute	(10)	(8)	(26)	(11)
Rel. to Sensex	2	12	26	71

Source: Bloomberg

Stock Details

Sector	Pharmaceuticals
Reuters	PIRA.BO
Bloomberg	PIHC@IN
Equity Capital (Rs mn)	418
Face Value (Rs)	2
No of shares o/s (mn)	209
52 Week H/L (Rs)	389/180
Market Cap (Rs bn /USD mn)	46/938
Daily Avg Vol (No of shares)	128780
Daily Avg Turnover (US\$ mn)	0.6

Shareholding Pattern (%)

	30/12/08	30/9/08	31/06/08
Promoters	49.6	49.6	49.3
FII/NRI	24.4	25.0	24.6
Institutions	9.3	8.1	8.0
Private Corp.	5.9	5.9	6.7
Public	10.9	11.4	11.4

Source: Capitaline

Manoj Garg

manoj.garg@emkayshare.com

+91 22 6612 1257

Akshat Vyas

akshat.vyas@emkayshare.com

+91 22 6612 1491

Piramal Healthcare's Q3FY09 revenues grew by 15% to Rs8.3bn. The lower growth in revenue was mainly on the back of decline in the CMG segment from the assets outside India. Though the CMG business from Indian assets grew by 45% to Rs 805mn but still it was below our expectations. On the domestic front, the company has reported a growth of 22% thus outpacing the industry growth of 10.3%. The growth in domestic formulation business is on the back of increased contribution from key therapeutic segment. EBIDTA for the quarter was up by 18% to Rs1555mn thereby improving the EBIDTA margins for the quarter to 18.8% (18.3% in Q3FY08) mainly driven by margins expansion in CMG space. During Q3FY09 the reported PAT declined by 17.7% to Rs599 mn in Q3FY09 (Rs 728 mn in Q3FY08) due to Forex loss of Rs 352 mn as compared to a forex gain of Rs 75mn. However after adjusting the Forex loss/gain, the Adjusted PAT witnessed a growth of 29% to Rs 926mn. Adjusted EPS for Q3FY09 stood at Rs4.4 (up by 29%). At the CMP of Rs 214, the stock is trading at 10.5x FY09E EPS of 20.4 and 8.6x FY10E EPS of 24.7. We maintain our Buy with a Target Price of Rs 304.

Key Highlights

- Domestic formulation business grew by 22% to Rs4.1bn driven by strong growth in key therapeutic area. On like to like basis, growth in domestic segment is 18% (acquisition of Khandelwal brands contributed 4% additional growth) vs. 10.3% industry growth. Higher growth in the domestic formulation is because of restructuring initiatives taken by the management in last one year. Management has indicated that on sustainable basis, they expect domestic formulation business to grow at 15% going forward.
- CMG business grew by 3.6% to Rs2.6bn. The CMG business from Indian assets grew by 45% to Rs805mn, while business from overseas assets de-grew by 8.4% on the back of slowdown from small biotech companies (contributes 4% of Canadian operation) due to credit crisis and shifting of low margin contracts from Avecia to India. Management has revised their revenue guidance for CMG business from Indian assets to Rs3.7bn from Rs4bn for FY09E because of lower takeoff by global pharma companies to reduce channel inventory. In 9MFY09, revenues from Indian assets were Rs2.3bn
- Pathlabs business continued to report strong momentum and grew by 35% to Rs425mn.
- Overall revenues for 9M FY09 grew by 16.3% to Rs24.3bn on the back of 23% growth in domestic formulation business and 52% growth in CMG business from Indian assets.
- EBIDTA for the quarter grew by 18% to Rs1.56bn largely driven by improved product mix and margin expansion in CMG business. Company restructuring initiative at Morpeth resulted improvement in operating margins in CMG segment.
- Piramal has incurred MTM loss of Rs351.5mn during the quarter and indicated that realized loss for Q4FY09 would be Rs250mn (provided currency remain at the same level), which they have already provided in unrealized losses. The unrealized loss for 9M FY09 is Rs590mn and realized loss is Rs400mn.
- The total debt as on date is Rs12.7bn of which US\$45mn and GBP11mn is in foreign currency. Most of the foreign currency loans are long term with a repayment schedule of 2.5 to 5 years. During the quarter the interest cost has gone up by 115% to Rs261mn on the back of increased debt (impact of Rs60mn) and higher interest rate (impact of Rs30mn).

- RPAT for the quarter de-grew by 18% to Rs599mn, however adjusted to forex loss/gain; PAT grew by 29% to Rs926mn.
- The other current assets during the quarter grew by 61% to Rs5.2bn. This was mainly on account of Rs750mn loan to Piramal Life Sciences, Rs650mn towards extended working capital to Minrad Inc, Rs161mn to Rx Elite (distributor of Minrad in US) and MAT credit of Rs130mn. Piramal Healthcare has earned Rs25mn as interest income from Piramal Life Sciences.
- Management has maintained its annual guidance of 16% growth in topline and an EPS of Rs21 for FY09E.

Outlook and Valuation

Piramal Healthcare provides us with a balanced mix of steady domestic formulation business and high growth CRAMS opportunity. We believe that initiative taken by management to improve its domestic formulation business has started paying off and company has outpaced the industry growth by 2x in 9M FY09. Though on the long term sustainable basis, we believe that domestic formulation business will grow in-line with the industry growth (13-14% annually). However, in the CMG business, we have witnessed some slowdown on account of reduction in inventory by large pharma company and impact of credit crisis on small biotech companies, which has impacted the growth. Though management has indicated robust Q4FY09 outlook, however we preferred to be bit conservative on CMG business for the next 2-3 quarters.

We expect revenue and earning CAGR of 15.7% and 19.8% over FY08-11E. The higher earnings growth compared to revenue growth is because of improved operating performance in CRAMS space. We believe that positive cash flow from FY10E onwards, strong return ratios and likely D/E of 0.24 by FY11E, Piramal Healthcare is a good investment opportunity. At the CMP of Rs 214, the stock is trading at 10.5x FY09E EPS of 20.4 and 8.6x FY10E EPS of 24.7. We maintain our Buy with a Target Price of Rs 304.

Key Financials

Income Statement Y/E, Mar (Rs. m)	Standalone					Consolidated					
	Q3FY09	Q3FY08	Y-o-Y Gr.(%)	Q2FY09	Q-o-Q Gr.(%)	9MFY09	9MFY08	Y-o-Y Gr.(%)	FY08	FY09E	FY10E
Net Sales	8283	7201	15%	8843	-6%	24169	20755	16%	28522	33893	39096
Expenses	6728	5883	14%	7474	-10%	19452	17668	10%	23312	27232	31324
Raw Materials	3291	2869	15%	3345	-2%	9153	7989	15%	10930	12956	14824
% of sales	39.7	39.8	0%	37.8	5%	37.9	38.5	-2%	38.3	38.2	37.9
Employee cost	1172	1103	6%	1421	-18%	3810	3526	8%	4709	5536	6326
% of sales	14.1	15.3	-8%	16.1	-12%	15.8	17.0	-7%	16.5	16.3	16.2
R&D exp	200.1	199.5	0%	231	-13%	647.0	1210.3		805.5	841.3	970.2
% of sales	2.4	2.8	-13%	2.6	-7%	2.7	5.8		2.8	2.5	2.5
Other expenses	2066	1711	21%	2477	-17%	5842	4943	18%	6867	7898	9205
% of sales	24.9	23.8	5%	25	-1%	24.2	23.8	1%	24	23	24
Adjusted EBIDTA	1555	1318	18%	1630.2	-5%	4717	3086	53%	5210	6661	7772
EBIDTA %	18.8	18.3	50 bps	18.4	40 bps	19.5	14.9	460 bps	18.3	19.7	19.9
Other income	43	88	-52%	51	-16%	135	199	-32%	670	437	526
Interest	261	122	115%	170	53%	552	344	60%	866	1074	1099
Depreciation	295	269	9%	288	2%	853	781	9%	947	1147	1287
PBT	1042.1	1015.8	3%	1222.4	-15%	3447.6	2159.6	60%	3727.9	4877.2	5911.5
Total Tax	71.8	78.9	-9%	114.0	-37%	272.4	221.7	23%	376.6	599.9	727.1
Effective tax rate (%)	6.9	7.8	-11%	16.5	-58%	7.9	10.3	-23%	10.1	12.3	12.3
RPAT	598.7	727.6	-18%	733.9	-18%	2013.5	2008.6	0%	3337.8	3137.6	5170.9
E/O items	351.5	-18.5		262.2		1126.2	-70.6		-339.3	1126.2	0.0
Adjusted PAT	926.0	717.8	29%	996.1	-7%	3061.5	1946.9	57%	3677.1	4263.8	5170.9
			120					330			
Net Margin (%)	11.2	10.0	bps	11.3	(10) bps	12.7	9.4	bps	12.9	12.6	13.2
EPS (diluted)	4.4	3.4	29%	4.8	-7%	14.6	9.3	57%	17.6	20.4	24.7

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Emkay Global Financial Services Ltd.,

Paragon Center, H -13 -16, 1st Floor, Pandurang Budhkar Marg, Worli, Mumbai – 400 013.

Tel: +91-22-66121212, Fax: +91-22-66242410