Initiating Coverage on
Indian Pharmaceutical Sector

September 2011

Indian Pharmaceuticals

Initiating Coverage

Executive Summary

Sector Outlook	Positive

Only on Prescription

We initiate coverage on the Indian Pharmaceutical sector with a positive outlook on sector fundamentals and selective optimism on coverage stocks. Indian pharma companies are set to benefit from the peak of the patent expiration wave in 2011 and 2012 with over $40bn of branded sales facing first-time generics in the world's largest pharma market. In the domestic pharma market, growth is expected to accelerate driven by rising consumption, favorable demographic trends and improving healthcare infrastructure. In the fast-growing emerging markets Indian players are expanding their direct presence and are also entering into attractive product outlicensing deals to accelerate their growth. However, given that current valuations largely capture the upsides from these opportunities, execution will be key to determining relative outperformance/ underperformance. Our top picks (Lupin, Torrent and Ipca), apart from offering the highest potential to benefit from the aforementioned opportunities, also provide the highest visibility for near-term growth. Aurobindo, Cadila and Glenmark are our least preferred stocks as they have less potential to benefit from the sectoral tailwinds and are predisposed to risk factors and challenges that could impact performance adversely.

Key sector thoughts: The biggest patent-expiration wave in history will peak in 2012 and Indian companies are well-positioned to benefit from this across regulated pharma markets, particularly in the US. However, we note that the tailwinds in the US will start to recede gradually post the peak of the patent cliff in 2012 and hence we look for companies with capabilities to grow beyond this phase. In the domestic formulations segment, we acknowledge the challenges on account of rising competition from smaller new entrants and MNCs, but growth prospects for companies with presence in attractive therapeutic segments, new product capabilities and strong marketing strategies remain intact. Impacted by declining R&D productivity and patent expiries, big pharma companies are increasingly turning to emerging markets and generics to revive their topline growth. To ride this opportunity, Indian players have partnered with them through product outlicensing and supply deals especially in emerging markets and have also focused on expanding their direct presence in certain key markets. Though thematically all coverage companies have the potential to benefit from these trends, company-specific opportunities and issues result in vastly different risk-reward profiles for each of them.

Valuation and stock picking: Our business analysis matrix based on qualitative and quantitative factors ranks Torrent, Lupin, Cadila, Ipca, Glenmark and Aurobindo from 1-6 with 1 being the best and 6 being the least preferred from a long-term perspective. Stock calls**:** ARBP (Reduce/U-PF, TP: Rs. 128), CDH (Reduce/U-PF, TP: Rs. 755), GNP (Sell/U-PF, TP: Rs. 271), IPCA (Add/O-PF, TP: Rs. 344), LPC (Buy/O-PF, TP: Rs. 548) and TRP (Buy/O-PF, TP: Rs. 701). Though we are postive on Cadila from a long-term perspective, we expect the stock to underperform over the next 12 months given the lack of near-term growth drivers and rich current valuations.

Key risks: Product approval delays, adverse litigation outcomes, adverse FDA actions, expansion of price controls and more-than-anticipated competition in the domestic market

Date	Sep 13, 2011

Market data*	
BSE SENSEX	16502
NIFTY	4947
BSE HEALTHCARE	5957

Performance (%)			
	1m	3m	6m
ARBP	-16%	-25%	-37%
CDH	-2%	-8%	36%
GNP	-2%	3%	11%
IPCA	-3%	-11%	3%
LPC	3%	7%	24%
TRP	-4%	1%	11%
BSETHC	-2%	-6%	4%
Sensex	-2%	-10%	-14%

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**prices as on September 12, 2011*

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Snapshot of Views on Stocks

Sector Outlook	Positive

Company	View	Rating
Aurobindo Pharma	• The recent import alert on Aurobindo's Unit VI facility (~$40mn of annualized sales), the warning letter for its Unit III facility and frequent product recalls have raised concerns about the sustainability of the company's growth in the US • We expect Aurobindo to face margin pressures in FY12 on account of 1) decline in dossier outlicensing sales 2) fixed costs at Unit VI, which is under import alert. Higher interest expense from the refinancing of $204mn (including redemption premium) of FCCB obligations in May 2011, will also impact profitability	**REDUCE** **UNDERPERFORM** **TP: Rs. 128**
Cadila Healthcare	• The delay in approvals due to the WL for Cadila's Moraiya facility will disrupt its growth in the US. The company had made 14 filings for injectables products from the facility, approvals for which were expected in FY12 and FY13 • Recent launches of generic docetaxel by multiple players will impact Hospira's market share and pricing resulting in lower sales for the Hospira JV in the coming quarters. Patent expiry for Protonix in the US in Jan 2011 is expected to further erode Nycomed JV sales • Acute-heavy domestic portfolio is relatively more vulnerable to competitive pressures in the domestic pharma market	**REDUCE** **UNDERPERFORM** **TP: Rs. 755**
Glenmark Pharmaceuticals	• Glenmark received 19 final ANDA approvals in FY11 (the highest for any Indian company). Opportunity to increase market shares for these products and the potential sole FTF launches (of generic Malarone and generic Cutivate) should drive strong performance for the US business in FY12 • Outlicensing of GRC 15300 (in Q1 FY11) and GBR 500 (in Q1 FY12) to Sanofi for upfront payments of $20mn and $50mn, respectively, has raised the optimism regarding Glenmark's NCE portfolio • Concerns remain on the company's balance sheet and accounting policies	**SELL** **UNDERPERFORM** **TP: Rs. 271**
Ipca Laboratories	• Ipca's focus on brand building will continue to drive its domestic formulations business • Ipca is one of the four WHO prequalified suppliers under AMFm (a $250mn opportunity) of artemether+lumefantrine (AL) and is awaiting prequalification for artesunate-amodiaquine (AS-AQ) • FDA approval for Ipca's Indore facility is expected by the end of FY12. Ipca's US sales has the potential to scale-up to Rs. 3-4bn on receiving approval for the Indore facility	**ADD** **OUTPERFORM** **TP: Rs. 344**
Lupin	• Lupin's near-term pipeline includes multiple limited-competition opportunities such as gGeodon, gFortamet, gTricor, gCombivir and oral contraceptives • The company's domestic formulations segment will continue to register above-industry growth in key chronic therapeutic segments • Lupin is set to benefit from the expected rise in generic penetration in Japan. Among Lupin's other markets, South Africa, Philippines and Australia offer significant potential	**BUY** **OUTPERFORM** **TP: Rs. 548**
Torrent Pharmaceuticals	• Chronic-heavy portfolio, recent sales force additions and new marketing initiatives will drive Torrent's domestic sales • The recently-entered contract manufacturing agreements with MNCs position the company to leverage its large product basket and strong manufacturing capabilities for volume-driven growth in fast-growing EMs • Strong balance sheet and cash generation to support major capacity expansions	**BUY** **OUTPERFORM** **TP: Rs. 701**

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Valuation Matrix

Sector Outlook	Positive

Company	Sales (Rs. mn)			EBITDA (Rs. mn)			Adj PAT (Rs. mn)			Adj EPS (Rs.)			FY11-FY13E CAGR		
	FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E	Sales	EBITDA	EPS
Aurobindo	41,259	46,335	51,511	7,042	7,559	8,686	5,397	4,890	5,322	16.9	16.8	18.3	11.7%	11.1%	4.1%
Cadila	44,647	50,050	57,617	8,607	9,635	11,523	6,950	7,461	8,591	33.9	36.4	41.9	13.6%	15.7%	11.2%
Glenmark	29,536	35,468	38,566	5,923	8,464	7,541	3,296	4,792	3,844	12.2	17.7	14.2	14.3%	12.8%	7.9%
Ipca	18,825	22,201	25,927	3,598	4,240	5,133	2,294	2,717	3,331	18.3	21.6	26.5	17.4%	19.4%	20.3%
Lupin	56,478	65,520	77,136	10,069	11,400	14,039	8,515	9,840	12,287	19.0	21.9	27.4	16.9%	18.1%	20.0%
Torrent	21,220	25,087	30,875	3,047	3,740	4,770	2,532	3,187	3,953	29.9	37.7	46.7	20.6%	25.1%	25.0%

Company	EBITDA Margin			ROE			ROCE			EV/EBITDA (x)			P/E (x)		
	FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E
Aurobindo	17.1%	16.3%	16.9%	25.2%	19.1%	18.3%	13.6%	10.2%	11.5%	8.8	8.2	7.1	7.8	7.8	7.2
Cadila	19.3%	19.3%	20.0%	36.9%	30.3%	27.6%	26.7%	23.6%	23.2%	21.0	18.7	15.7	24.5	22.9	19.9
Glenmark	20.1%	23.9%	19.6%	16.2%	21.0%	14.3%	11.9%	14.3%	11.1%	17.9	12.5	14.0	26.2	18.0	22.5
Ipca	19.1%	19.1%	19.8%	23.9%	23.3%	23.4%	18.0%	17.1%	17.6%	12.5	10.6	8.7	16.9	14.3	11.7
Lupin	17.8%	17.4%	18.2%	29.2%	26.6%	26.3%	22.2%	21.5%	22.8%	21.4	18.9	15.4	24.5	21.2	17.0
Torrent	14.4%	14.9%	15.5%	27.3%	27.6%	27.3%	19.5%	21.0%	22.8%	16.9	13.7	10.8	20.0	15.9	12.8

Company	CMP	No. of shares	Market Cap (Rs. mn)	Target Price	Upside/ downside	Rating	
						Absolute	Relative
Aurobindo	131	291	38,253	128	-3%	Reduce	U-PF
Cadila	833	205	170,607	755	-9%	Reduce	U-PF
Glenmark	319	270	86,337	271	-15%	Sell	U-PF
Ipca	309	126	38,856	344	11%	Add	O-PF
Lupin	465	446	207,592	548	18%	Buy	O-PF
Torrent	598	85	50,626	701	17%	Buy	O-PF

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Key Sector Thoughts

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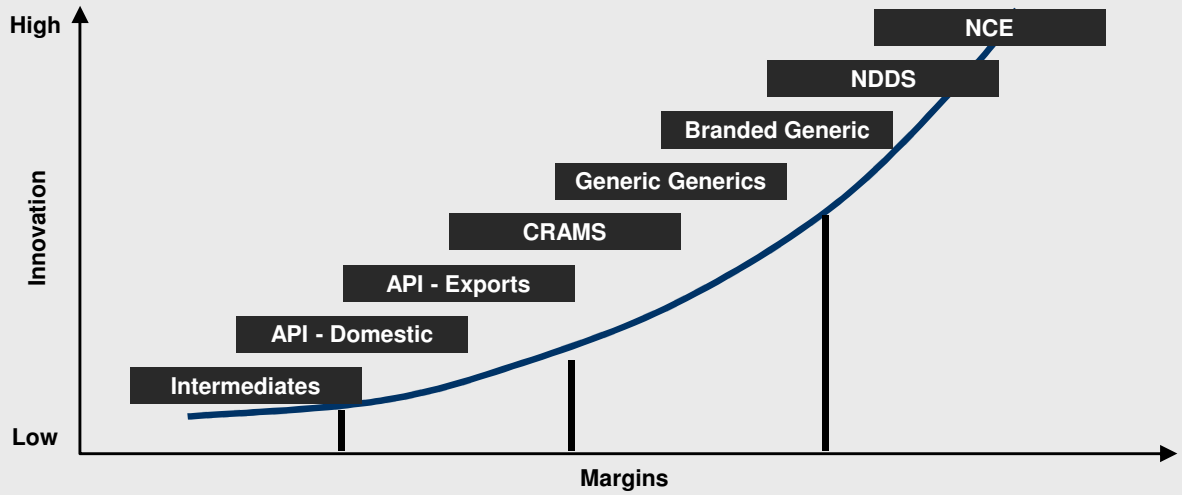
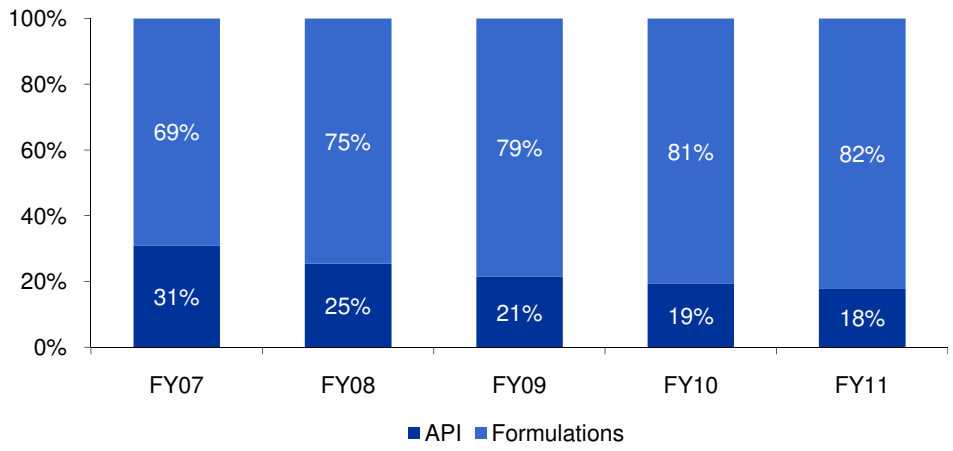
Sector Outlook Positive

Indian players are present across the pharma value chain



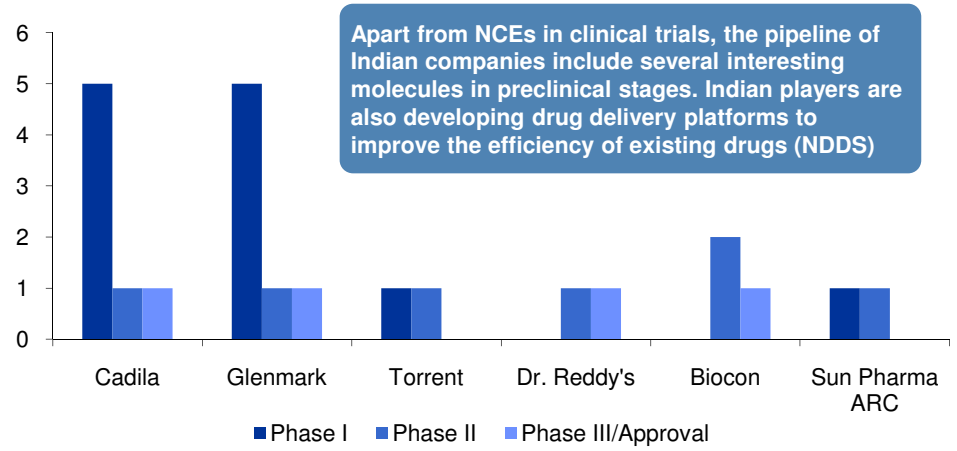
- In the last few years, Indian pharma companies have accelerated their move up the pharmaceutical value chain. Many players which were previously focused on bulk drugs and domestic formulations are now key suppliers of generic drugs in advanced pharma markets and have developed capabilities in Novel Drug Delivery Systems (NDDS) and NCE research
- The declining contribution of API sales to the topline for our coverage companies (from 31% in FY07 to 18% in FY11) is proof for this ascent
- In spite of setbacks, Indian players continue their efforts to discover new molecules. New technologies to improve the delivery of existing drugs and to enhance their efficiency (NDDS) is another emerging area of focus for many Indian players

Declining share of lower margin API sales*



*Source: Company data, Spark Capital Research, *for coverage universe*

Number of NCEs undergoing clinical trials for select Indian players



Apart from NCEs in clinical trials, the pipeline of Indian companies include several interesting molecules in preclinical stages. Indian players are also developing drug delivery platforms to improve the efficiency of existing drugs (NDDS)

Source: Company data, Spark Capital Research

Indian Pharmaceuticals

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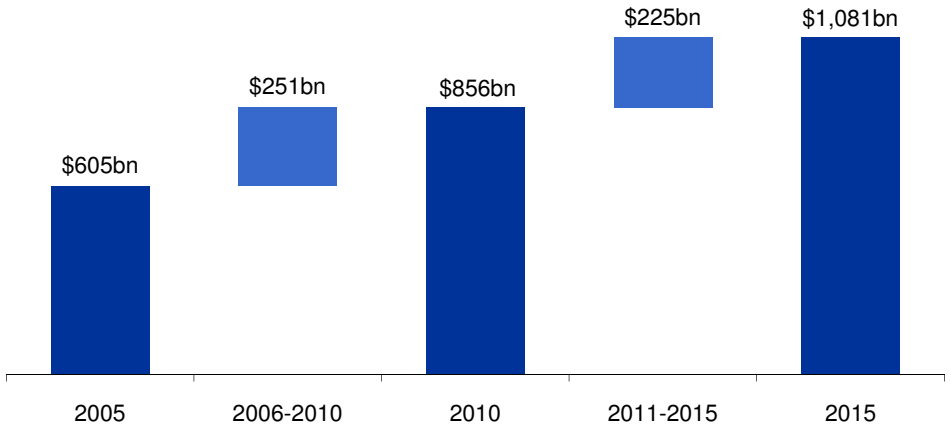
Generics to lead growth in global pharmaceutical market

Sector Outlook Positive

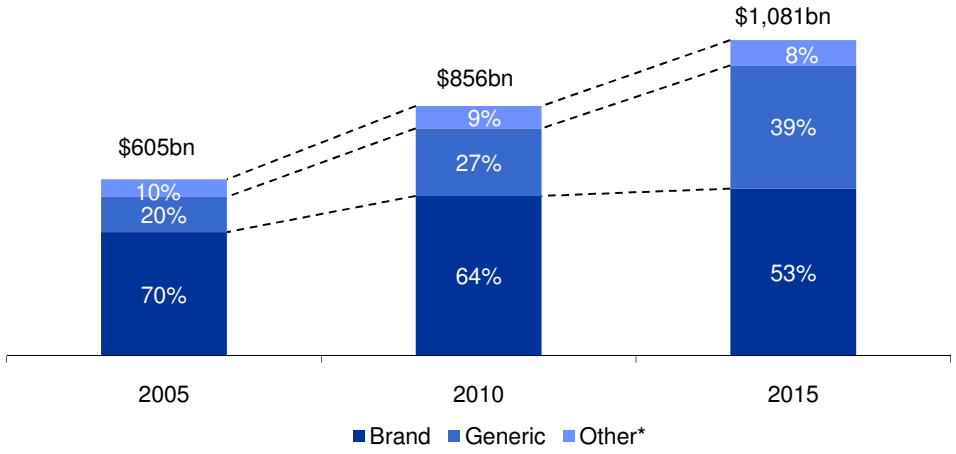
Global pharma market to reach ~$1.1tn by 2015



Source: IMS, Spark Capital Research

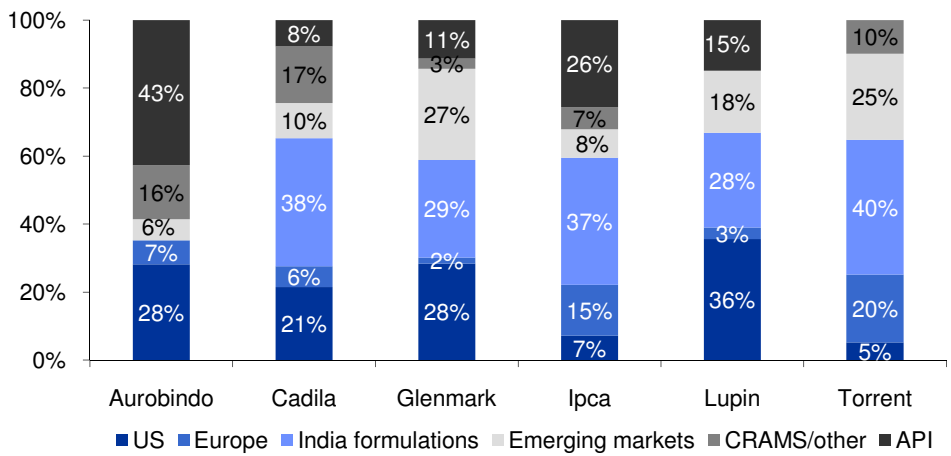
- Global spending on medicines is forecast to exceed $1tn by 2015
- The spending on generic drugs (including branded generics) is expected to grow at a CAGR of ~13% through 2015, compared to ~5% CAGR for the overall pharma market
- The share of branded drugs which accounted for ~64% of global pharma spend in 2010 is expected to decline to 53% due to
  - Generic competition for more drugs due to patent expiries
  - Higher incentives for usage of generics
  - Faster growth in emerging pharma markets where the spending is largely on generic drugs

Generics to lead growth in pharmaceutical market



*Source: IMS, Spark Capital Research, *'Other' includes OTC & non-categorized*

Business mix for coverage companies (FY11)



Source: Company data, Spark Capital Research, EM sales includes Japan for Lupin

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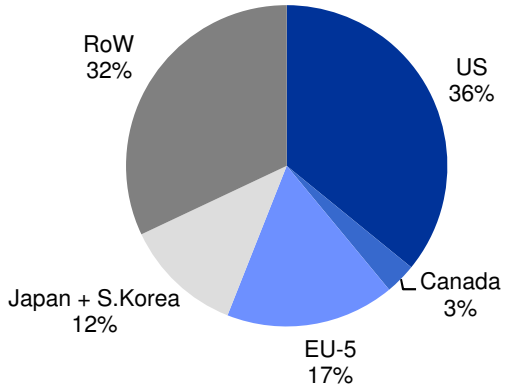
US dominates the global pharma market

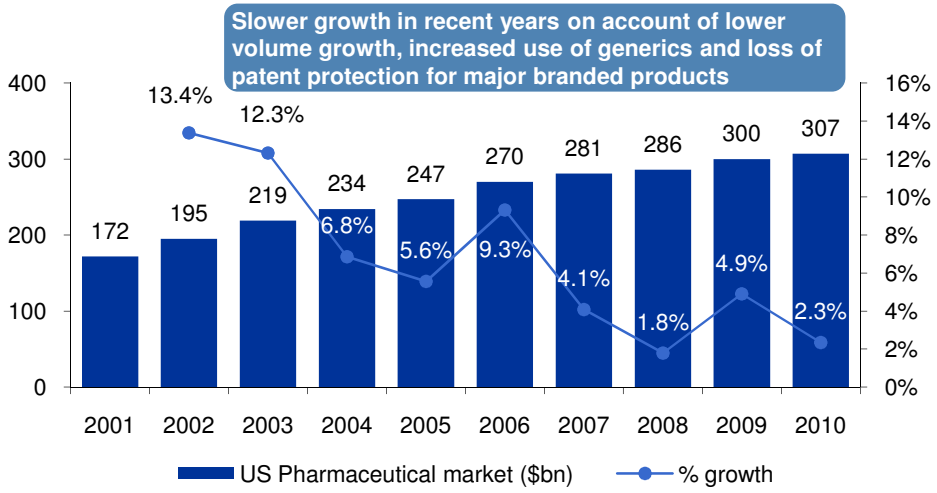
- Despite the slower growth in recent years, US remains the largest pharma market globally
- Apart from patent expiries, lower volume growth and rising generic penetration have contributed to the slower growth in the US pharma market in recent years
- The generic segment, has outpaced the overall pharma market, growing at a CAGR of 11% compared to 3% for branded drugs in 2005-2010. Indian companies have capitalized on the growth in the generic segment to emerge as key players in the US pharma market
- However, Indian companies still account for under 15% of the US generic market, implying significant potential to grow from their currently low base

US accounts for ~36% of global pharma spending



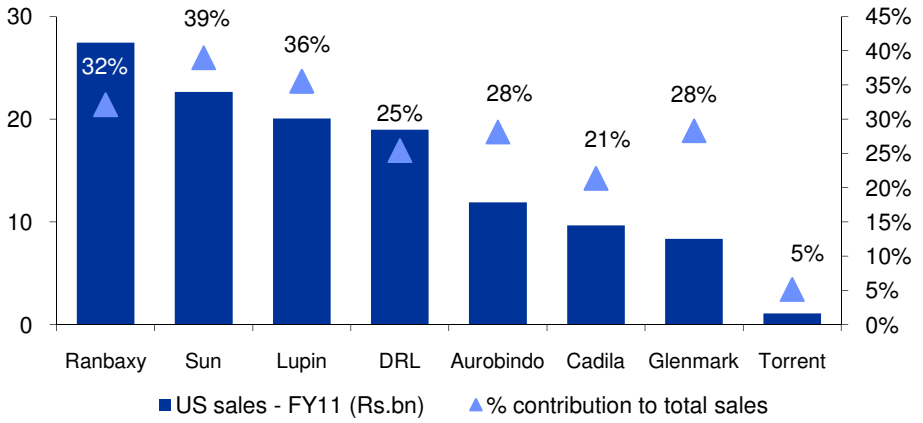
Source: IMS, Spark Capital Research

US pharma market estimated at ~$307bn in 2010



Source: IMS, Spark Capital Research

US contribution to topline for leading Indian companies in FY11*

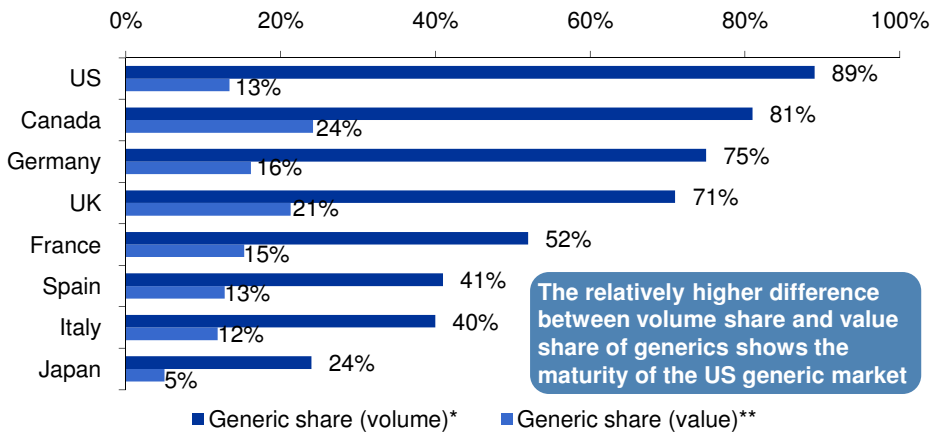


*Source: Company data, Spark Capital Research; *CY10 for Ranbaxy*

Generic penetration continues to rise in the US

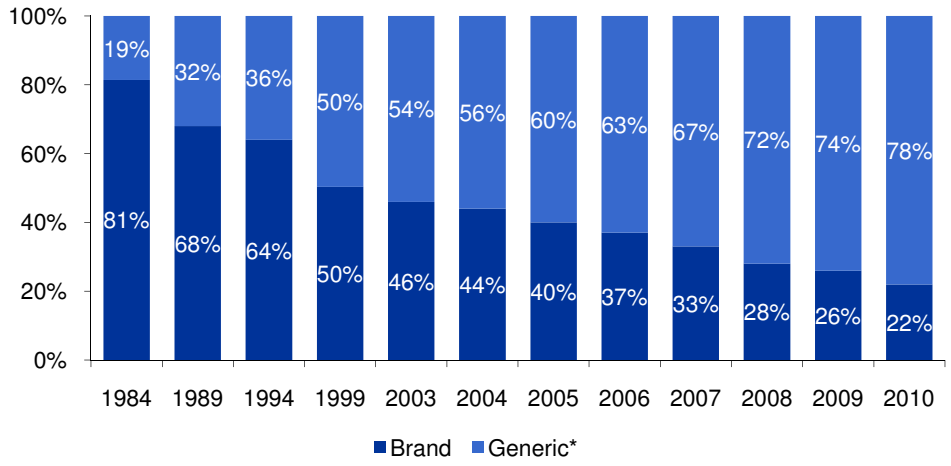
- The generic penetration (by prescriptions) in the US (89% of off-patent market, 78% of overall pharma market) is the highest among regulated pharma markets
- The volume share of generics has risen rapidly in recent years, from 50% in 1999 to 78% in 2010. The recent healthcare reforms which intends to bring 30 million more Americans under health insurance should lead to increased emphasis on use of generics and further increase in generic penetration
- The value share of generics has not increased at the same pace and is currently at 13% (25% including branded generics), offering significant potential for growth
- The difference between volume share and value share of generics in the US is significantly higher compared to most other regulated pharma markets. This indicates the maturity of the US generic market, where competition ensures the most efficient price discovery for generic drugs

Highest generic penetration among regulated pharma markets



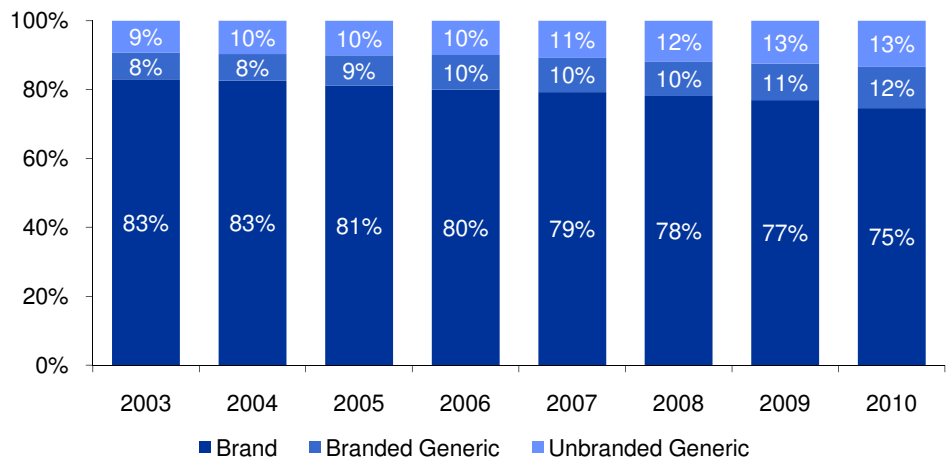
*Source: IMS, *of off-patent market,**of total pharma market (excluding branded generics)*

US generic penetration by volume



*Source: IMS, Spark Capital Research, *includes branded generics*

US generic penetration by value

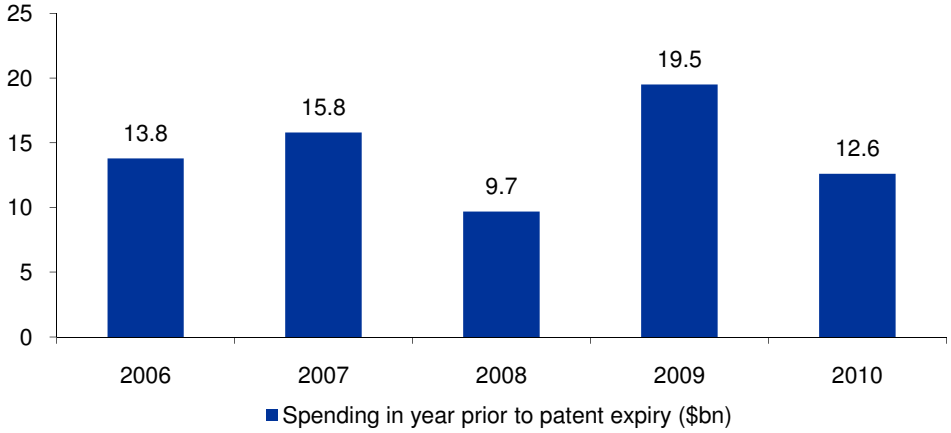


Source: IMS, Spark Capital Research

Indian players have made significant inroads in the US generic market

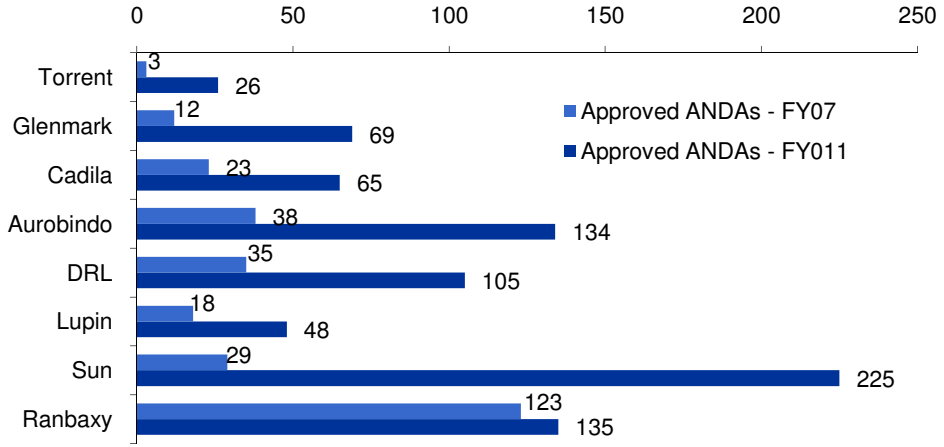
- According to IMS Health, ~$71bn of branded sales faced patent loss and competition from generics in 2006-2010
- This has contributed to growth in the generic market (excluding branded generics) from ~$25bn in 2005 to ~$41bn in 2010 (most states in the US allow pharmacists to substitute branded products with generics, when available)
- Indian pharma companies have significantly scaled up their US operations to take advantage of this opportunity. Most Indian companies currently offer a much larger basket of products in the US, compared to a few years ago, as evident from their larger portfolio of approved ANDAs
- For our coverage universe, US market has been the largest contributor to incremental sales in FY07-FY11 (excluding Torrent and Ipca which are recent entrants in the US market)

~$71bn of branded sales exposed to generics during 2006 - 2010



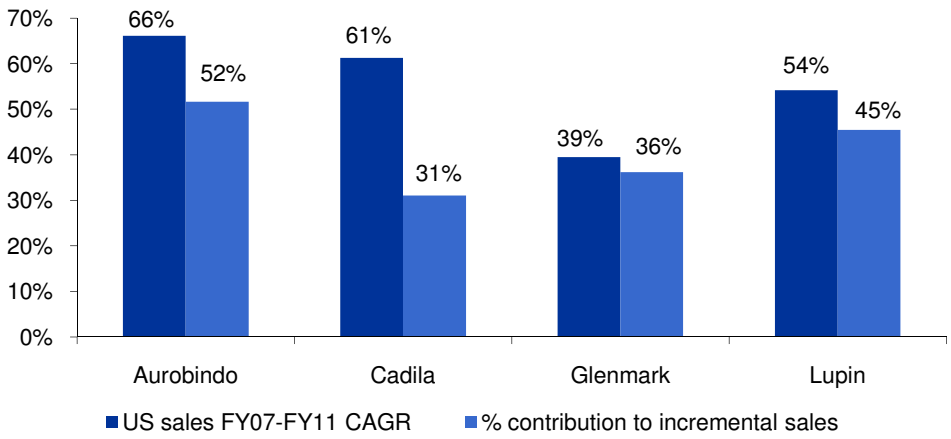
Source: IMS, Spark Capital Research

Indian companies have expanded their portfolio significantly



Source: Company data, Spark Capital Research

Highest contributor to incremental sales in recent years

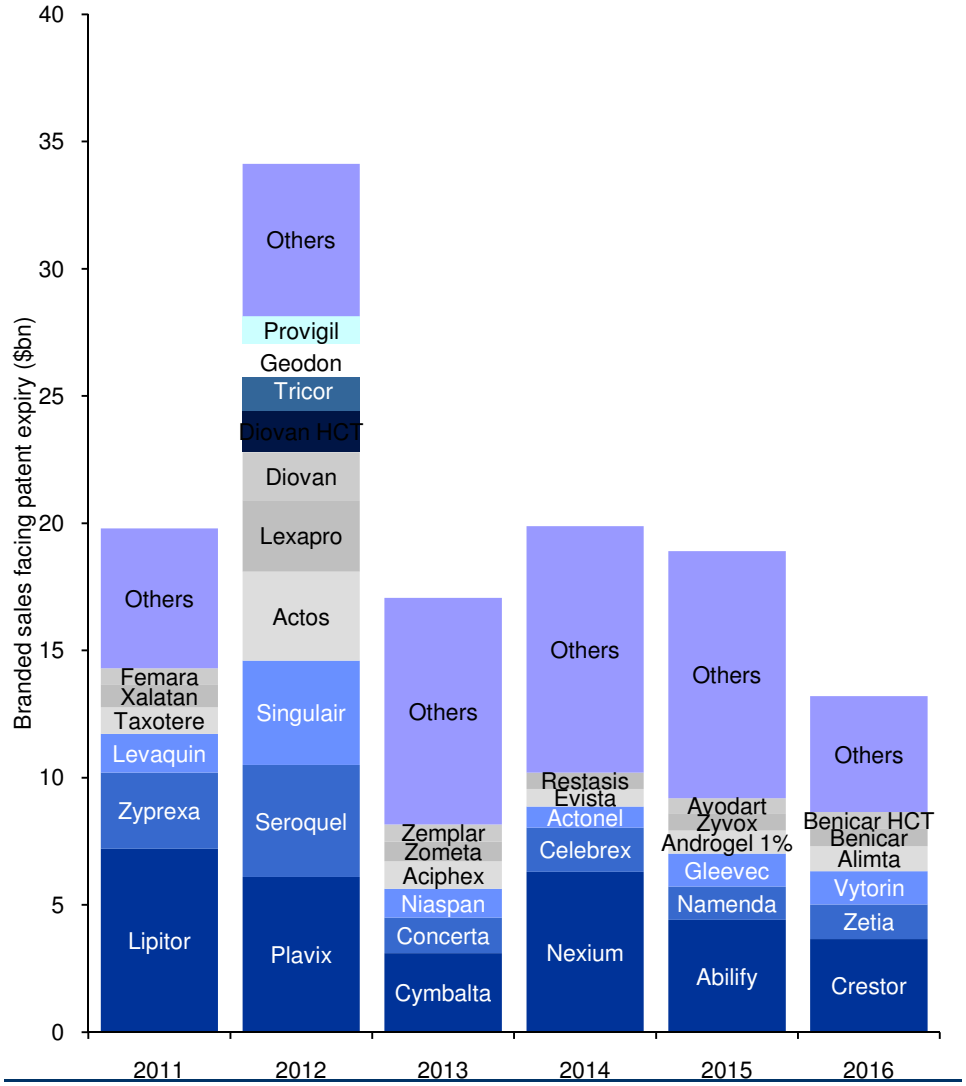


Source: Company data, Spark Capital Research

The peak of the patent expiration wave in 2012 presents huge opportunity

Sector Outlook Positive

~$125bn of US branded sales to face generic competition by 2016



Source: Spark Capital Research

- The exact generic opportunity from patent expiries is difficult to quantify (due to unknown litigation outcomes), but we expect ~$125bn of branded sales to face patent expiries during 2011-2016
- 2012 will be the peak year of growth from patent expiries for generic companies, with ~$34bn of branded sales facing generic competition for the first time in the year
- However, beyond this peak, we expect the growth in the US generic market to decline gradually, falling to mid-single digits by 2016
- We also note that beyond 2012, oral solid drugs (capsules, tablets) which are forecast to constitute ~90% of branded sales facing patent expiries during 2011-2012, become less prominent. Higher proportion of drugs losing patent protection beyond 2012 would be injectables, inhaled respiratory, opthalmic and localized delivery drugs. These drugs are more difficult-to-make and hence should face less competition and price erosion
- We expect generic companies with capabilities in these 'niche areas' to outperform beyond 2012

Top 15 products facing generic competition in 2011-2012

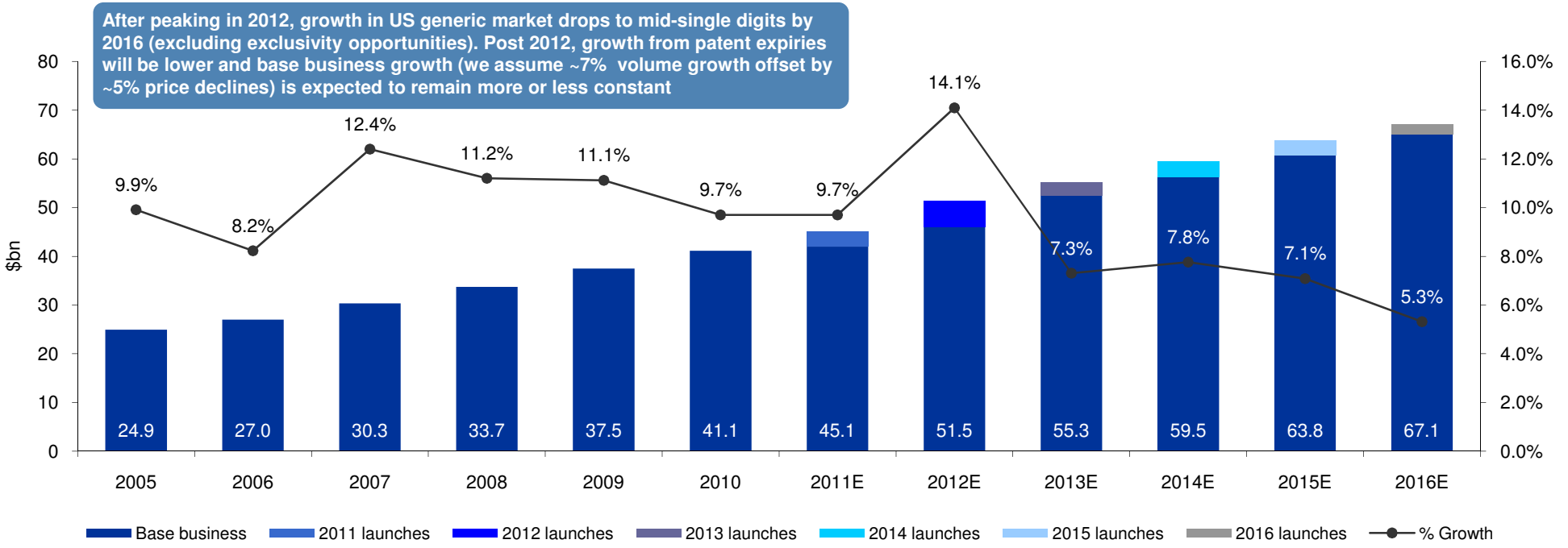
Product	Innovator	US brand sales ($bn)
Lipitor	Pfizer	7.2
Plavix	Sanofi Aventis	6.1
Seroquel	AstraZeneca	4.4
Singulair	Merck	4.1
Actos	Takeda	3.5
Zyprexa	Eli Lilly	3.0
Lexapro	Forest Labs	2.8
Diovan	Novartis	1.9
Diovan HCT	Novartis	1.6
Levaquin	J&J	1.5
Tricor	Abbott	1.3
Geodon	Pfizer	1.3
Provigil	Cephalon	1.1
Taxotere	Sanofi Aventis	1.0
Xalatan	Pfizer	0.9

Source: Spark Capital Research

US generic market to grow slower post 2012

Sector Outlook | Positive

US generic market



Source: Company data, Spark Capital Research

- Our analysis shows that, after peaking in 2012, growth in US generic market drops to mid-single digits in 2013-2016 (excluding exclusivity opportunities). Post 2012, growth from patent expiries will taper and base business growth (we assume ~7% volume growth offset by ~5% price declines) is expected to remain more or less constant. Given the slower growth in the overall generic market, we believe only those companies with capabilities in niche areas (which are likely to face less competition and price erosion) will be able to sustain growth
- Beyond 2016, we expect the growth in generic market to be even slower as more than 70% of current (2010) branded sales will already have generic competition by then, implying even lesser scope for growth from patent expiries
- We have made the following assumptions for arriving at estimates for the US generic market 1) 80% generic penetration and 80% price erosion in the year of patent expiry 2) base business to grow at ~2% (~7% volume growth offset by ~5% price declines) 3) excludes the impact of FTF exclusivities as they are difficult to model

Indian Pharmaceuticals

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Sector Outlook | Positive

US pipeline matrix for coverage companies

	Lupin	Cadila	Glenmark	Aurobindo
Branded	Branded products in the pediatric and primary care segments - Suprax, Antara and AeroChamber	-	-	-
Hormones/Oral contraceptives (OCs)	26 ANDAs filed. Approvals expected from FY13	-	15 ANDAs filed for hormonal products including OCs. 9 pending approval. Targeting a portfolio of >20 products	Filings expected from FY13/FY14
Ophthalmic	Started filing ANDAs for opthalmic products. Plans to add more filings in the next 1-2 years	-	-	Filings expected from FY13
Oncology	-	Hospira JV supplies oncology products, marketed by Hospira. Hospira recently launched docetaxel, supplied from JV	Plans to file ANDAs from Argentina-based oncology facility	-
Injectables	Markets injectable cephalosporins	~14 ANDAs filed from Moraiya facility. Approvals could get delayed due to FDA warning letter	-	Strong portfolio and pipeline of anti-infective injectables. Recently launched TazoPip is a limited-competition opportunity. Unit VI ban is a setback
Topical/Transdermal	Developing capabilities in dermatology. Filings expected over the next 1-2 years	2 filings made for transdermal products	Dermatology is strongest therapeutic area. 18 ANDA approvals received till date. 3 pending approval	-
Controlled-substances	-	Pipeline of 8 ANDA filings (through recent acquisition of Nesher)	3 ANDAs filed and approved	~10 ANDAs filed from New Jersey facility
Respiratory/Nasal	Possess capabilities in the inhaler segment (MDI, DPI). Have launched inhalers in India	2 filings for nasal products pending approval	Developing capabilities in the segment. Inhalers launched in India	-
Para IV/limited-competition	~40 para IV filings with FTF status for ~20 of them. ~6 near -term limited competition opportunities	~19 para IV filings. If approved, azelastine could be a near term limited competition opportunity	15 para IV filings pending approval. Sole FTF status for 4 products of which 2 are expected to be launched in FY12	~23 para IV filings. Mostly for commodity products

Source: Company data, Spark Capital Research

Indian Pharmaceuticals

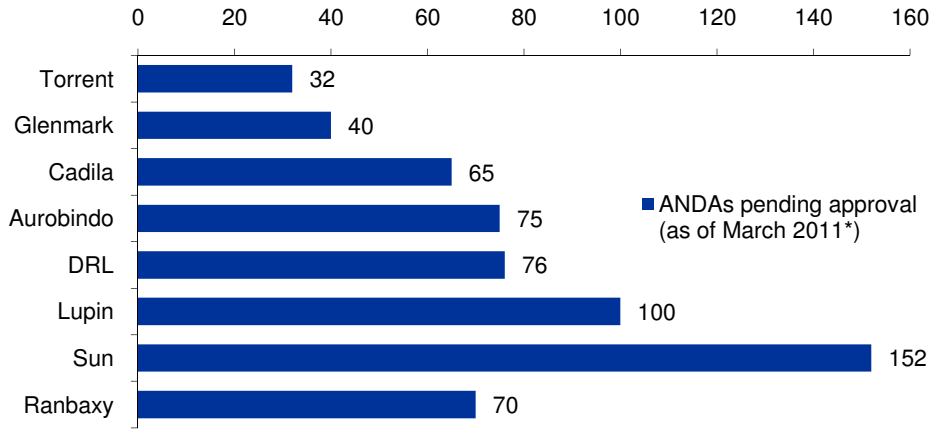
Initiating Coverage

Sector Outlook: Positive

Indian firms well-positioned to ride the patent expiry wave

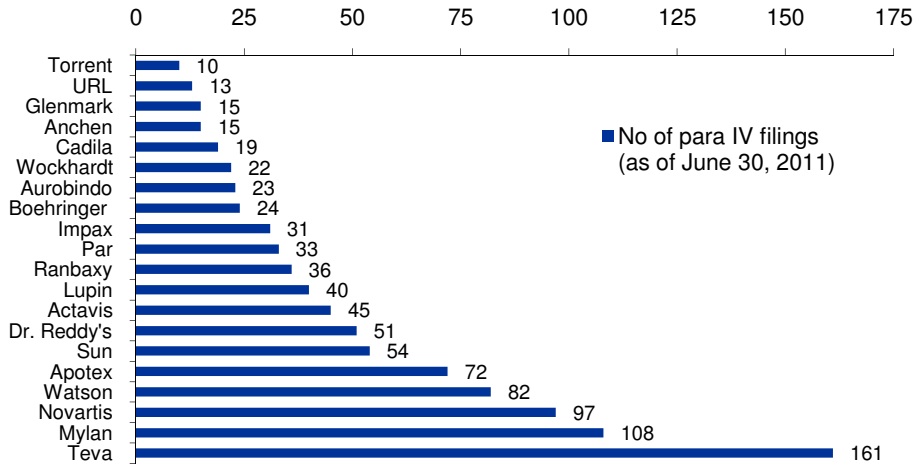
- Indian companies appear well-positioned to take advantage of the upcoming patent expiration wave in the US as suggested by their strong ANDA pipeline. Indian companies are also among the leading filers of para IV ANDAs, with many shared/sole exclusivity opportunities
- In 2011-2013E, among coverage companies, we expect Lupin (multiple limited competition opportunities) and Glenmark (para IV launches, recent launches expected to gain market share) to outperform in the US market. Torrent should also see strong growth in US sales, from a low base
- For Cadila, the WL for its Moraiya facility is a setback, as approvals for 14 injectable filings (and possibly nasal and other filings) from the facility will get delayed. For Aurobindo, the import ban on its Unit VI facility (lost sales estimated at ~$40mn) will impact its performance in the US
- For growth beyond the peak of the patent cliff in 2012, as shown by our pipeline matrix, Lupin (oral contraceptive and limited competition launches) and Glenmark (diversified portfolio with presence in niche areas) are best-positioned

ANDAs pending approval for Indian companies



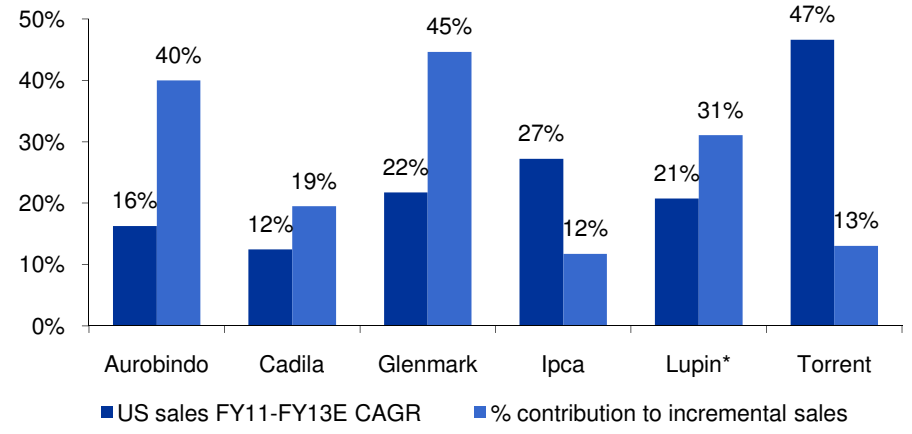
*Source: Company data, Spark Capital Research, *as of Dec 2010 for Ranbaxy*

Indian players among top para IV filers



Source: Thomson Reuters, Spark Capital Research

Contribution to incremental sales in FY11-FY13E

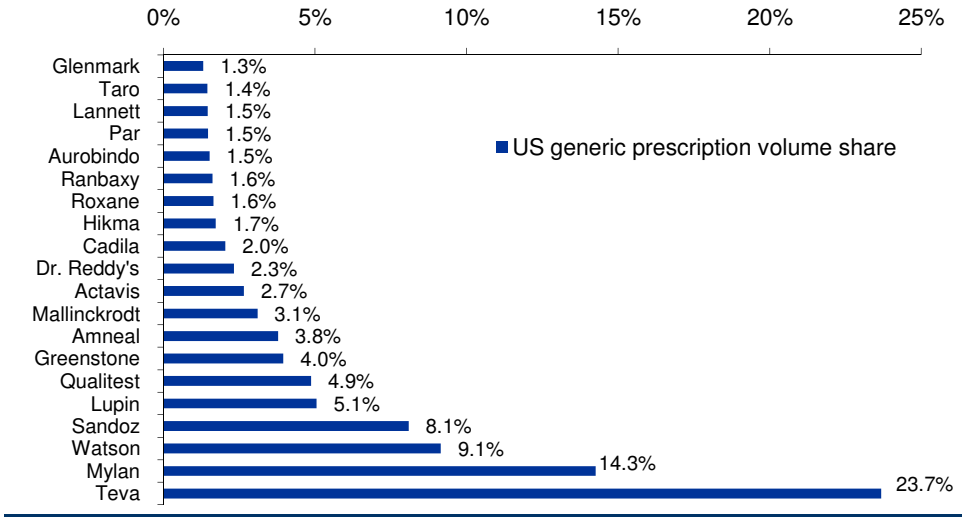


*Source: Company data, Spark Capital Research; *excludes branded business*

Competition growing bigger and stronger

Sector Outlook Positive

Competition with significant scale advantage



Source: Hikma, Spark Capital Research

- The US generic market has witnessed significant consolidation in recent years with the top 4 players (Teva, Mylan, Watson and Sandoz) almost doubling their share in the last decade (combined value share over 60% currently)
- We believe scale is important in the US generic market as it often implies stronger relationships with distributors and pharmacies and better pricing power
- These players have often resorted to acquisitions to acquire capabilities in niche areas or to gain access to new markets. Examples for the former are Mylan's recent acquisition of Bioniche to enhance its capabilities in generic injectables and Teva's acquisition of Barr to expand its women's health portfolio
- Teva's acquisition of Ratiopharm and Mylan's acquisition of Merck KGaA's generic business provided them access to key generic markets in Europe
- Indian players have largely stayed away from inorganic growth opportunities, barring a few exceptions, such as Sun Pharma's acquisition of Caraco and Taro and Cadila's recent acquisition of Nesher
- To propel their next leg of growth we believe it is imperative for Indian generic player to explore inorganic opportunities particularly in niche segments

Recent acquisitions of generic companies

Date	Acquirer	Target	Purchase Price ($bn)	Revenue multiple	Rationale for acquisition
Sep-10	Endo	Qualitest	1.2	3.4x	6th largest generic company in the US
Jul-10	Mylan	Bioniche	0.6	3.1x	Generic injectables
Mar-10	Teva	Ratiopharm	5.0	2.2x	Leading generic player in EU, particularly Germany
Jun-09	Watson	Arrow	1.0	1.6x	Authorized generic for Lipitor. Biologics through Eden Biodesign
May-09	Sandoz	Ebewe	1.3	4.7x	Specialty generics, oncology, injectables
Jul-08	Teva	Barr	7.5	3.0x	Strong in CEE. Women's health franchise
Mar-08	Teva	Bentley	0.4	3.2x	Leading player in Spain
May-07	Mylan	Merck KGaA	6.7	2.8x	Broad international presence
Feb-07	Hospira	Mayne	2.0	3.5x	Oncology, specialty injectables. Presence in EU, Australia, Canada
Mar-06	Watson	Andrx	1.9	2.7x	Sustained-release technology and difficult-to-make product pipeline
Jan-06	Teva	Ivax	7.4	3.2x	Respiratory franchise; presence in LatAm and CEE

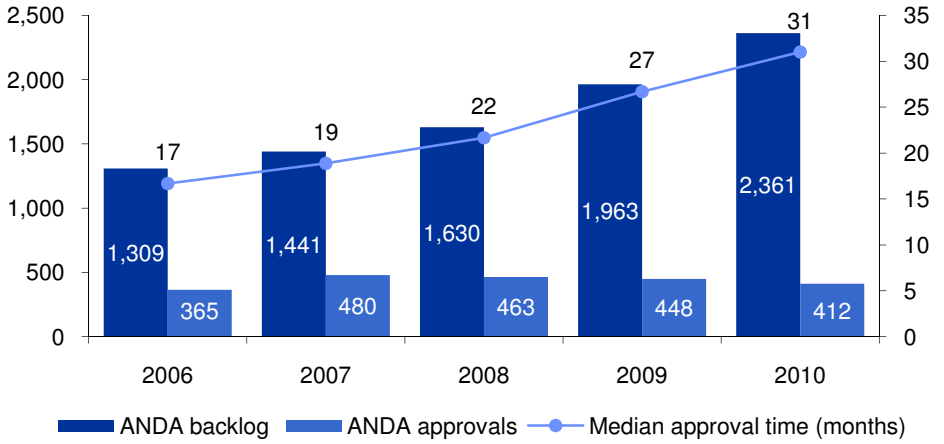
Source: Spark Capital Research

Adverse FDA actions emerging as a key challenge

Sector Outlook Positive

- The time taken for ANDA approvals has increased substantially mainly due to FDA's resource crunch. GMP violations by generic players has also contributed to higher scrutiny of ANDA applications leading to approval delays
- Number of approvals has remained more or less static since FY07 due to delays at FDA. The delays are more pronounced for non-first generics, which is often the case for many Indian players. Lesser ANDA approvals could impact the ability of Indian players to sustain their US growth rates
- In recent years FDA has become more vigilant regarding cGMP violations and has issued warning letters and import bans to several Indian players
- However, we note that these issues are not unique to Indian players and FDA has stepped up its scrutiny on larger US-based manufacturers as well. For instance, Teva received a WL for its Irvine facility (Dec 2009) and for its Jerusalem facility (Jan 2011) and Hospira received WLs for its Rocky Mount and Clayton facilities (April 2010)

Rising ANDA approval times



Source: FDA, Spark Capital Research

Recent adverse FDA actions against leading Indian players

Company	Date	Regulatory action
Dr. Reddy's	Jun-11	Dr. Reddy's Mexican facility received a WL in June 2011
Cadila	Jun-11	After reviewing Cadila's response to FDA's form 483 notice, Cadila was issued a WL for its injectables facility at Moraiya. FDA had sought corrective actions following its inspection of the facility in Jan-Feb 2011. The observations suggest failure to maintain accurate microbiological data. Cadila has 16 ANDAs for injectable products filed from the facility, the approvals for which (and possibly nasal and other filings), will get delayed
Aurobindo	Feb-11	Following inspection in Dec 2010, the FDA issued an import alert (before issuing a WL) on Aurobindo's Unit VI facility in Hyderabad, which manufactures sterile and non-sterile cephalosporin antibiotics. The WL was issued in May 2011 in which CGMP violations mainly related to microbiological documentation were detailed. The company also received a WL for its Unit III for violations of packaging and labeling norms
Sun Pharma	Aug-10	WLs for Caraco's Detroit facility in Nov 2008 and Sun's Cranbury facility in Aug 2010
Lupin	May-09	Received WL for its cephalosporin manufacturing plant in May 2009 following inspection in Nov 2008. The WL was resolved in Jan 2010 after Lupin undertook corrective actions
Ranbaxy	Sep-08	In Sep 2008, Ranbaxy received WLs accompanied by import bans for its facilities in Dewas and Paonta Sahib. In Feb 2009, FDA invoked AIP (Application Integrity Policy) against the Paonta Sahib facility. Ranbaxy's Gloversville facility received a WL in Dec 2009
Ipca	-	Ipca has been awaiting FDA approval for its manufacturing facility at Indore SEZ since Sep 2008. The delay has impacted the scale-up of its US operations. The fixed costs incurred at the facility has also impacted the company's profitability

Source: Spark Capital Research

NCE approvals declining; regulatory challenges to increase

Sector Outlook Positive

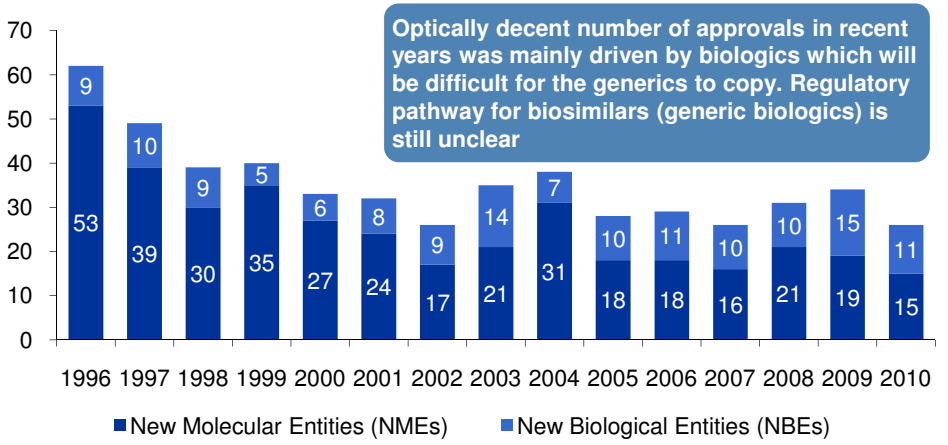
Big pharma's R&D struggles to impact generic pipeline in the long-term

- The number of NCE approvals by the FDA has declined from their peak levels and has more or less stagnated in recent years. The decline is more pronounced if measured in terms of value (peak sales potential) of approved products. The optically decent number of approvals in recent years was mainly driven by biologics which will be difficult for the generic players to copy (even if the regulatory pathway for biosimilars gets sorted out, we expect biosimilars in the US only towards the end of this decade)

FDA scrutiny on foreign manufacturers to increase

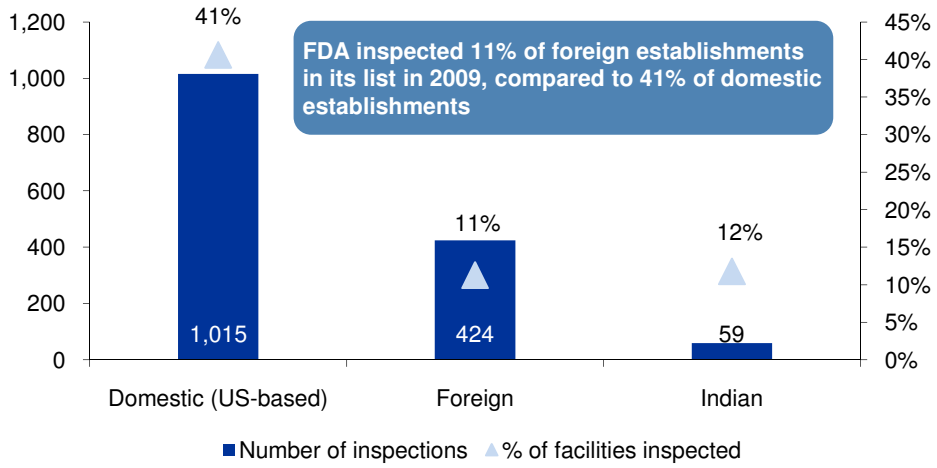
- In a recent report, the US GAO made 2 key observations and recommended corrective actions. The observations were 1) the FDA inspects foreign facilities less frequently compared to domestic facilities 2) Lesser number of GMP-only inspections on foreign facilities compared to domestic facilities; most of the inspections on foreign facilities are pre-approval in nature
- We believe corrective actions by the FDA could result in higher scrutiny on foreign FDA-approved facilities, including those in India

New drug approvals have stagnated



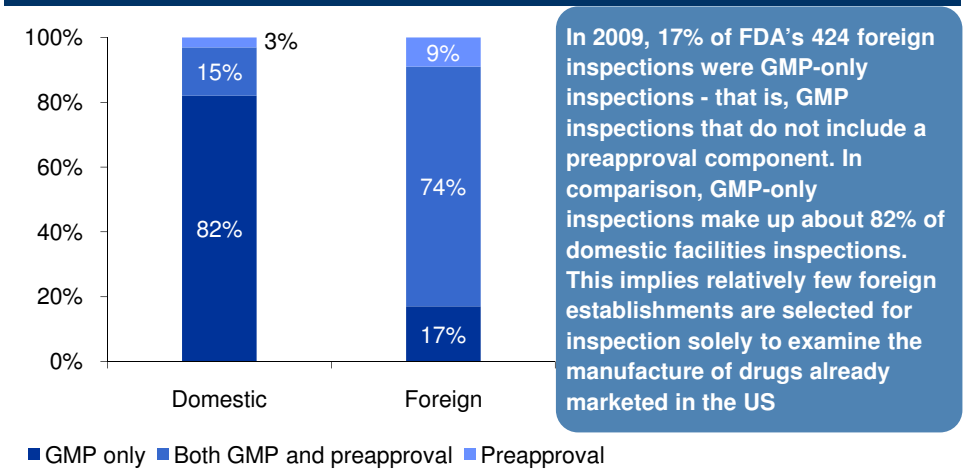
Source: FDA

FDA's foreign inspection rates lag behind domestic



Source: GAO, data for 2009

GAO recommends more GMP-only inspections on foreign facilities

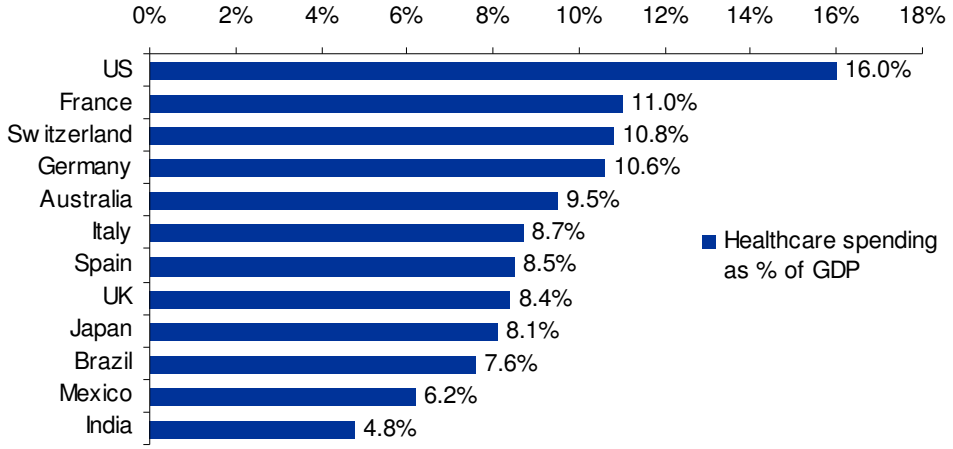


Source: GAO, data for 2009

Generic are here to stay in the US

Sector Outlook Positive

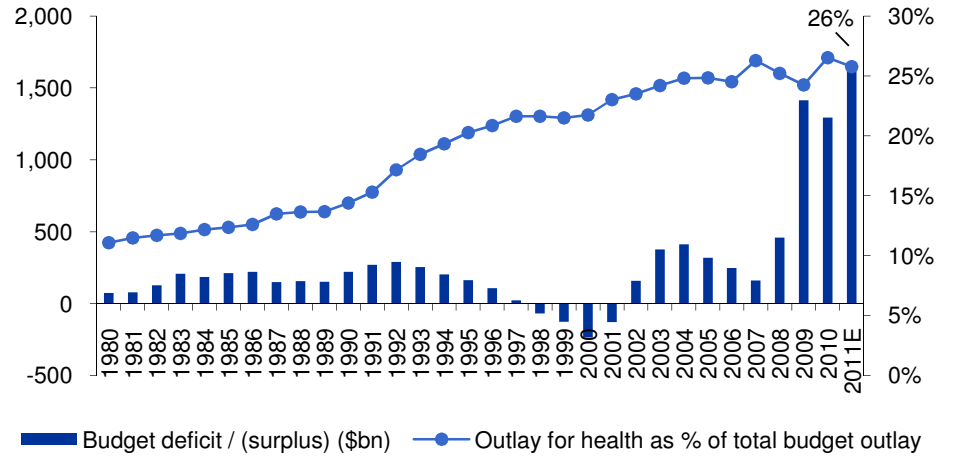
Healthcare as % of GDP



Source: IMS , Spark Capital Research

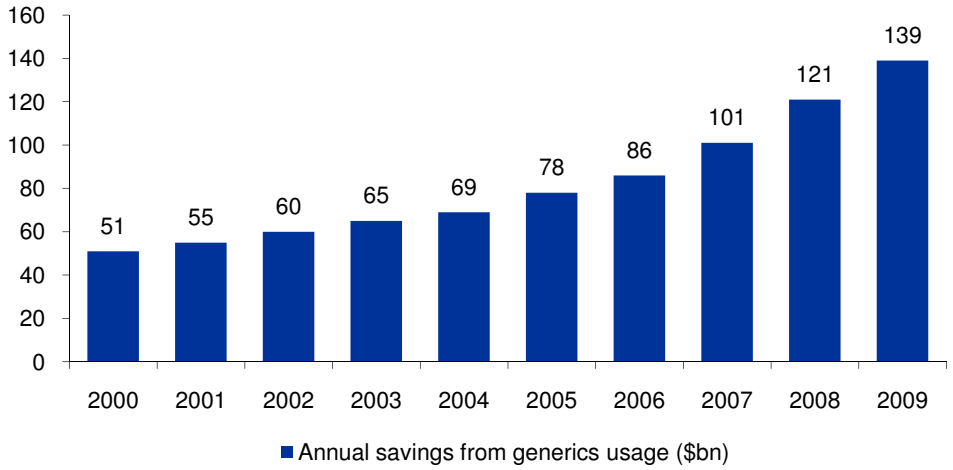
- US healthcare spending as % of GDP is the 2nd highest (after East Timor) among all nations
- Pharmaceuticals accounted for ~13% of US healthcare costs
- Per capita, the U.S. spends ~$1,054 on pharmaceuticals per year, more than any other country ($640 for France, $669 for Germany and $17 for India)
- Rising spending on healthcare has contributed significantly to the burgeoning budget deficit in the US
- Use of generics resulted in savings of ~$139bn for the US healthcare system in 2009 and we expect the annual savings figure to continue to rise
- We believe, stepping up the use of generic drugs will be central to any efforts aimed at reducing the country's healthcare bill. We also note that of the ~3,500 branded drugs in the US, less than 2,000 have generic alternatives currently, implying further room for generic growth

Rising health outlay contributing to US budget deficit



Source: US Government, Spark Capital Research

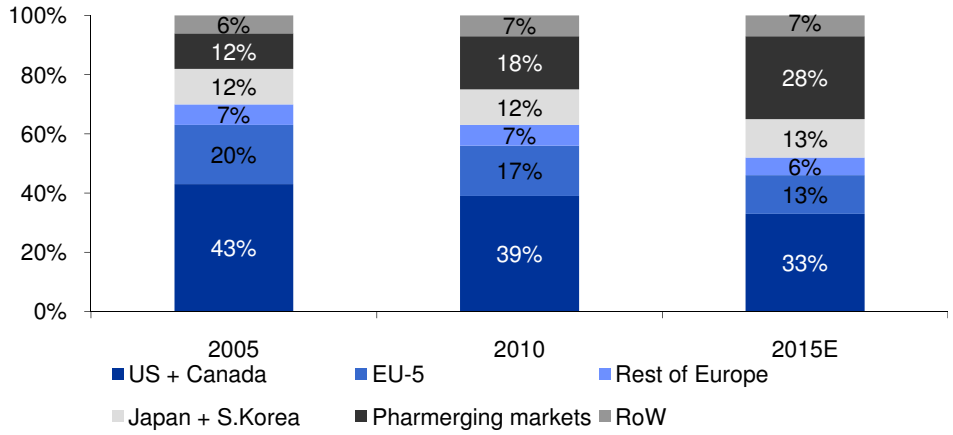
Generics saved $139.6bn for the US healthcare system in 2009



Source: GPhA, Spark Capital Research

The 'Pharmerging' opportunity

'Pharmerging markets' to outpace other markets



Source: IMS , Spark Capital Research

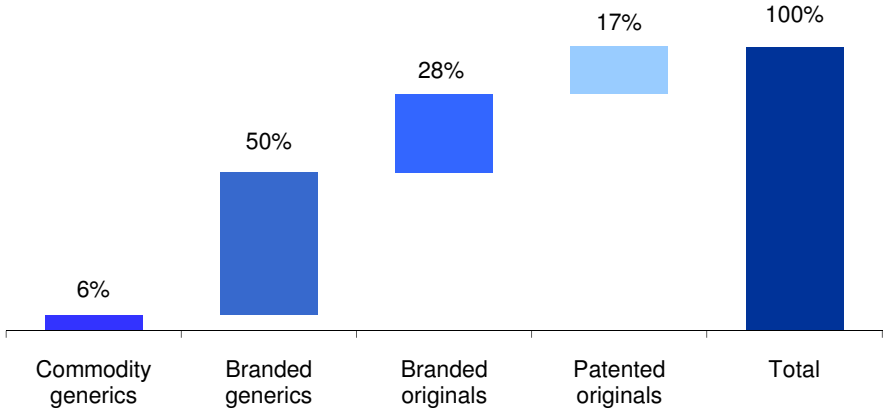
- According to IMS, much of the growth in global pharmaceutical industry will come from the 17 'pharmerging markets'. The share of regulated pharma markets (US, Canada, EU-5, Japan, South Korea) is expected to decline from 68% in 2010 to reach 59% by 2015
- Pharmerging countries are defined as those with >$1bn absolute spending growth over 2011-15 and which have GDP per capita of less than $25,000 on a purchase-price parity basis (PPP) basis. Pharmerging market growth will be led by China with expected growth of ~20% (CAGR) through 2015 followed by India (~15%), Russia (~12%) and Brazil (~12%)
- Most of these markets are branded generic in nature (similar to the Indian pharma market) with generic companies employing their own doctor-focused sale force to promote their brands. Branded generic markets tend to be more profitable than 'generic generic' markets where drugs are substitutable at the pharmacy level and distributors/insurance companies enjoy more bargaining power (for instance, the generic markets in the US, EU-5 and Japan)

Pharma markets offering high potential for coverage universe

Market	Total Pharma Market ($bn)	Out-of-pocket expense	Generic Penetration (Value)	Generic Penetration (Volume)	Indian companies present
Brazil	22.9	80%	50%	60%	Torrent, Cadila, Glenmark
Japan*	96.5	30%	6%	19%	Lupin, Cadila
Mexico	10.0	83%	40%	65%	Torrent, Cadila, Glenmark
Russia	13.6	75%	35%	70%	Glenmark, Ipca
South Africa	3.2	70%	30%	65%	Lupin, Cadila, Glenmark
Philippines	3.0	60%	15%	25%	Lupin, Glenmark

*Source: Spark Capital Research, * since the Japanese generic market is at a nascent stage and offers significant growth potential we include Japan under EMs*

Branded generics dominate in EMs



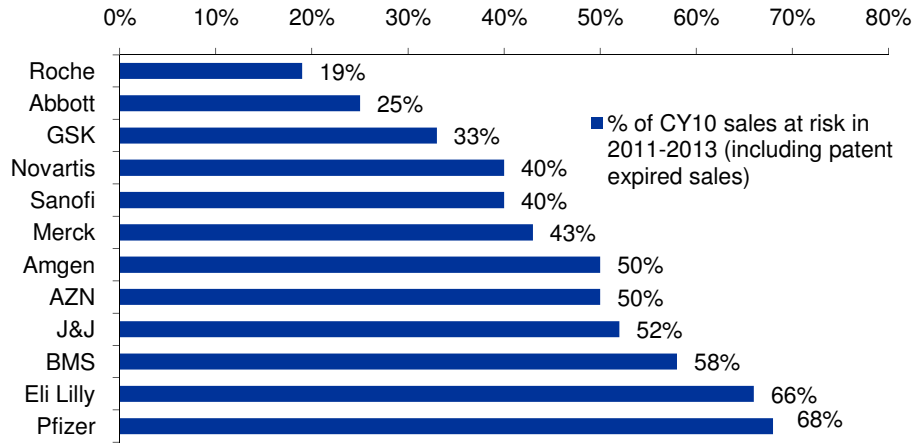
Source: AstraZeneca, Spark Capital Research

Big pharma's emerging market push

Sector Outlook Positive

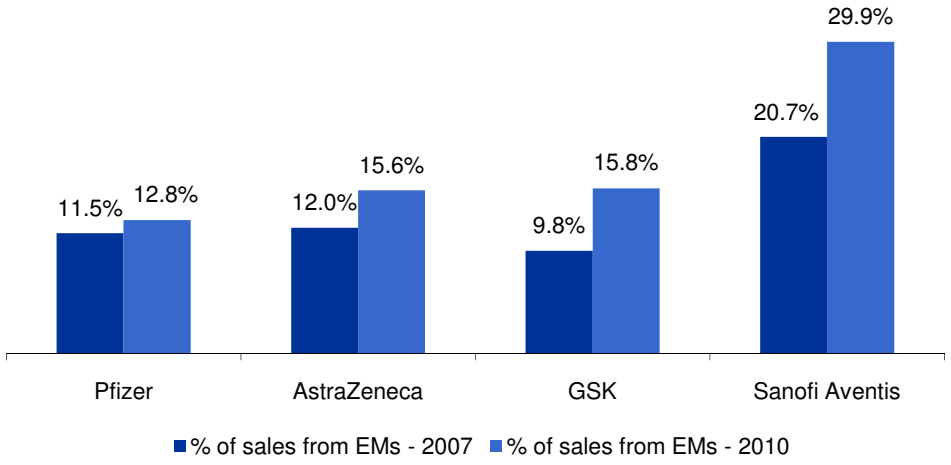
- Impacted by declining R&D productivity and patent expiries, big pharma companies are increasingly turning to emerging markets to revive their topline growth
- The high expected growth in emerging markets driven by greater government investments in healthcare, rising prevalence of chronic diseases and strengthening of regulatory and IP requirements have attracted most global pharma companies
- Most of these companies have established separate business units to exploit the potential in EMs. However, most of these markets have strong domestic companies, with advantages of local distribution networks and local manufacturing, capable of giving strong competition to the new entrants. The vastly different regulatory and cultural landscape also add to big pharma's challenges in these markets
- Big pharma companies have made several acquisitions in EMs in recent times and we expect acquisitions to continue to be a mainstay of big pharma's EM strategy

Patent cliff impacting all big pharma players



Source: EvaluatePharma, Spark Capital Research

Big pharma stepping up focus on EMs



Source: Company data, Spark Capital Research

Big pharma's recent EM acquisitions

Date	Acquirer	Target	Market	Deal Value ($mn)
Oct-10	Pfizer	Laboratorio Teuto	Brazil	240 (40% stake)
Jun-10	GSK	Laboratorios Phoenix	Argentina	253
May-10	Abbott	Piramal	India	3,720
Nov-09	Novartis	Zhejiang Tianyuan	China	125
Sep-09	Abbott	Solvay	Belgium	6,600
Jul-09	Sanofi Aventis	Shantha Biotech	India	784
May-09	GSK	Aspen Pharmacare	South Africa	418 (16% stake)
Apr-09	SanofiAventis	Medley	Brazil	690
Sep-08	SanofiAventis	Zentiva	Czech Republic	2,600
Jun-08	Daichi Sankyo	Ranbaxy	India	~4,400 (58% stake)

Source: Spark Capital Research

Indian Pharmaceuticals

Indian players set for volume-driven growth

Sector Outlook Positive

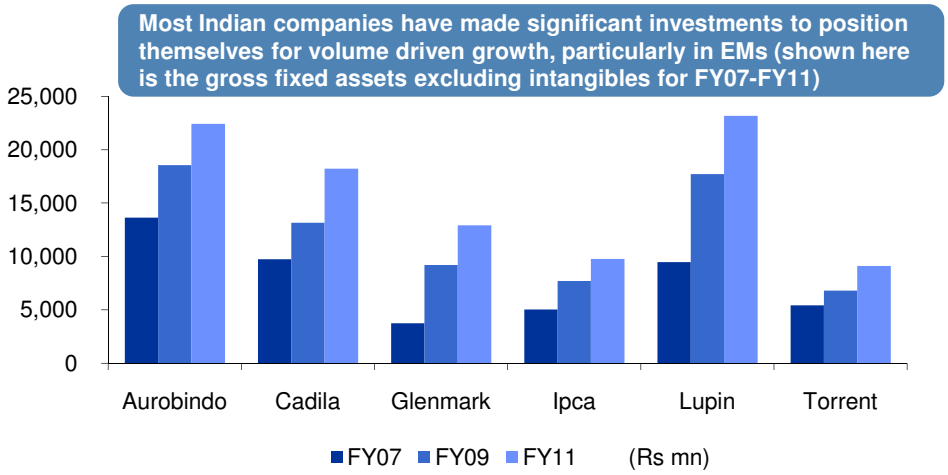
Product outlicensing deals with MNCs

Date	MNC	Domestic	Comments
Apr-11	Merck	Sun	JV to develop and sell drugs in emerging markets including India
Jan-11	Bayer	Cadila	JV to sell drugs in India
Oct-10	Pfizer	Biocon	~$350mn deal to supply biosimilar insulin to Pfizer
Sep-10	Astra Zeneca	Aurobindo	Supply 25 solid dosage and sterile products to be sold in 40 emerging markets
May-10	Abbott	Cadila	Supply of 24 products for 15 key EMs; option to increase number of products to 40; 8 products added in Q1 FY12
Mar-10	Aspen	Indoco	Supply of products including opthalmic drugs in 30 emerging markets
Mar-10	Astra Zeneca	Torrent	Supply of 18 products for 9 emerging markets with option to add more products and countries
Feb-10	Watson	Indoco	Supply sterile products to Watson for the US market
Jan-10	Pfizer	Strides	Supply of sterile injectable and oral products for US market; extended to cover more geographies in May 2010
Jun-09	Mylan	Biocon	Supply of high value generic biologic compounds to be sold globally
Jun-09	GSK	Dr. Reddy's	DRL will supply ~100 products to be sold under GSK brands in emerging markets
May-09	Pfizer	Aurobindo	Supply generic drugs (orals and injectables) across geographies
May-09	Pfizer	Claris Lifesciences	Supply of 15 injectable products for sale in regulated markets
Aug-08	Mylan	Famycare	Supply of 22 oral contraceptive products to be sold by Mylan in US
May-05	Hospira	Cadila	Vertically integrated JV (with Mayne Pharma later acquired by Hospira) to manufacture generic injectable oncology products

Source: Spark Capital Research

- Indian companies have had mixed results in EMs so far. Frequent regulatory changes (e.g. Russia), price cuts (e.g. Japan) and delay in product approvals (e.g. Brazil) all have contributed to slower-than-expected scale-up in operations for Indian companies. For some of the players, more disappointing has been the profitability of their operations in some of these countries
- Many Indian companies have entered into contract manufacturing agreements with MNCs to provide further fillip to their EM sales. Given that most of these markets require high upfront investments and have longer working capital cycles, we view these contract manufacturing deals positively. The pricing power of their MNC partners in these markets should ensure decent profitability for Indian suppliers
- Among coverage companies, Cadila (Abbott), Torrent (AstraZeneca and an undisclosed MNC) and Aurobindo (Pfizer and AstraZeneca) have entered into contract manufacturing agreements with MNCs. We believe these partnerships allow Indian players to leverage their large product baskets and cost-advantages in manufacturing

Capacity additions to support growth



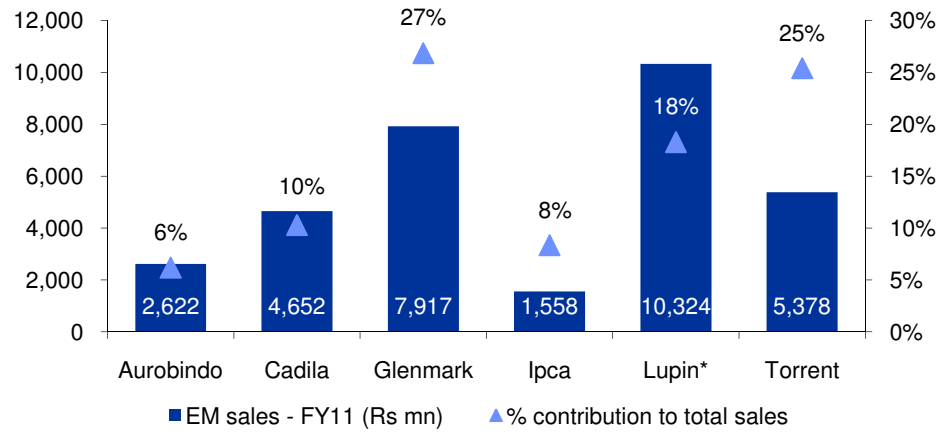
Source: Company data, Spark Capital Research

Indian Pharmaceuticals

EMs will be key contributor to near-term growth

Sector Outlook Positive

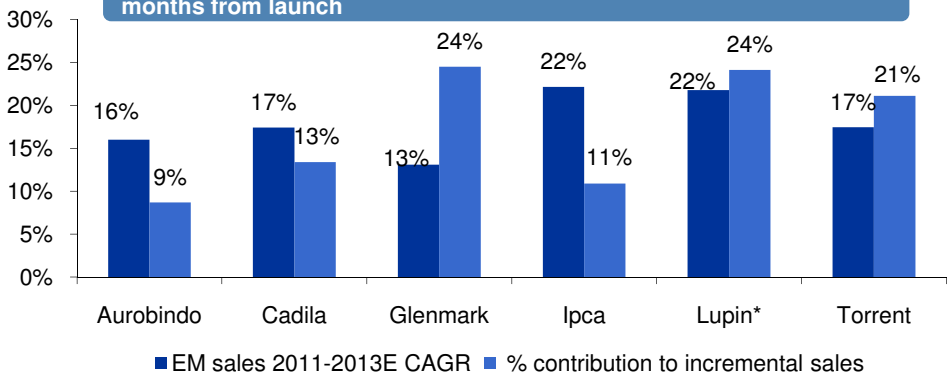
Glenmark has the highest EM exposure



*Source: Spark Capital Research, *includes Japan*

Product outlicensing to ramp up post FY13

For Cadila, Torrent and Aurobindo, EM supplies under product outlicensing deals to begin from FY13. Ramp up expected in 12-18 months from launch



*Source: Spark Capital Research, *includes Japan*

Key emerging markets for coverage companies

Company	Key markets	% of sales	Comments
Cadila	Brazil	5.0%	Entered Brazil in FY08 by acquiring Nikkho do Brasil. Cadila is the 2nd largest Indian player in Brazil
	Africa	-	Present in 7 African countries. Largest Indian player in some of these markets
	Japan	1.0%	Acquired Nippon Universal in FY07. In FY11, with the launch of Amlodipine, became the first Indian company in Japan to launch a product manufactured in India
Glenmark	Russia & CIS	8.5%	Dermatology and respiratory focused portfolio in Russia. CIS markets are Ukraine, Kazakhstan and Uzbekistan
	Latin America	6.7%	Brazilian business returned to growth in FY11. Other LatAm markets are Mexico and Venezuela
	Central & Eastern Europe	5.3%	Present in Czech Republic, Romania and Poland
Ipca	Africa	2.6% (ex institutional sales)	Present in 20 African countries. Focus on branded generics
	Russia & CIS	4.0%	Present in Russia, Ukraine and Belarus (all branded generic markets)
Lupin	Japan	11.0%	Acquired Kyowa in FY08. Kyowa currently has over 200 products and is one of the fastest growing generic companies in Japan
	South Africa	3.2%	Acquired PharmaDynamics in FY09. Currently the 6th largest generic player in South Africa
	Philippines	1.0%	Acquired Multicare Pharmaceuticals in FY09. Presence in women's health, primary care and pediatric segments
Torrent	Brazil	16.3%	Largest Indian company in Brazil. Market share of 6.8% in covered market

Source: Company data, Spark Capital Research

Domestic formulations – strong demand drivers

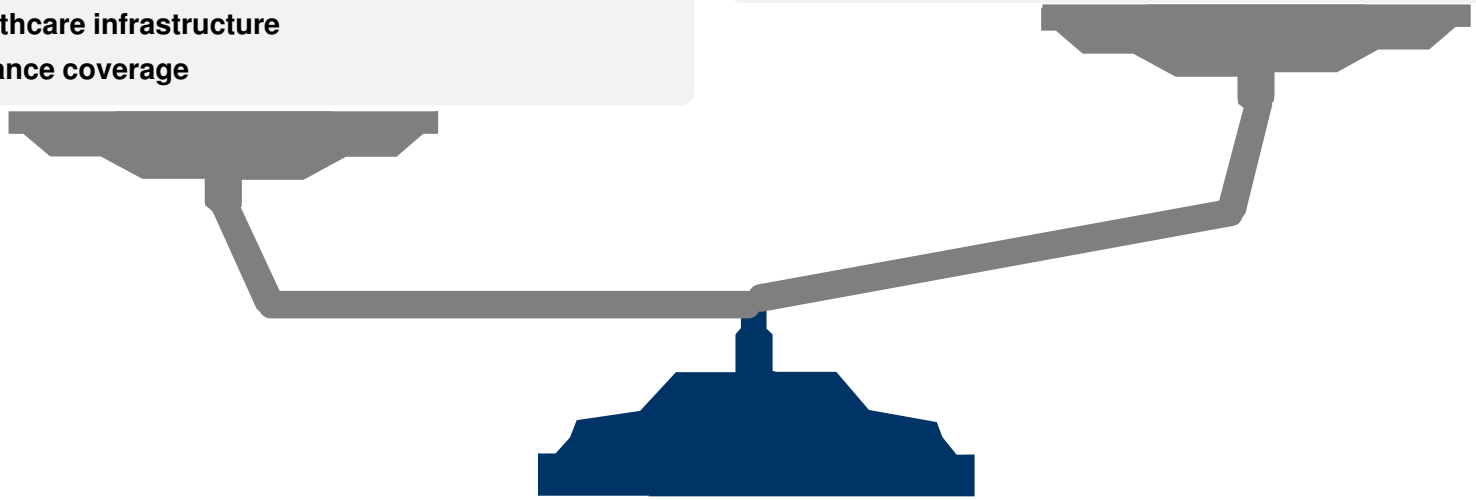
Sector Outlook	Positive

Demand drivers

- Population and economic growth
- Changing disease profile
- Changing demographics
- Higher disposable income
- Rising penetration in non-metro markets
- Improving healthcare infrastructure
- Growing insurance coverage

Challenges

- Fragmented market characterized by intense competition
- Extreme price sensitivity
- Price controls
- New product patent regime (negative for domestic companies)
- Unorganized distribution network
- Counterfeit drugs



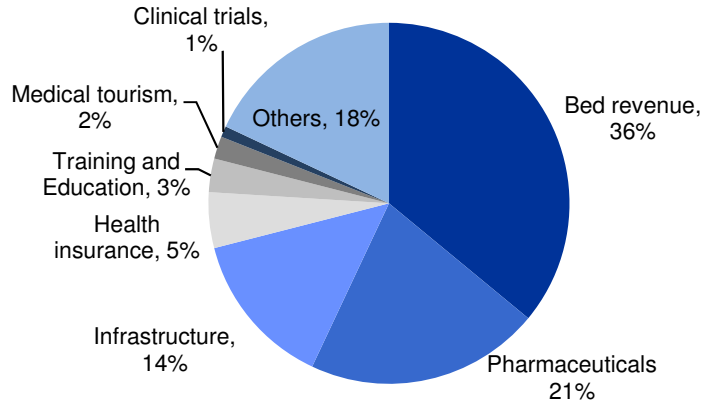
Indian Pharmaceuticals

Favorable outlook for domestic formulations

Sector Outlook Positive

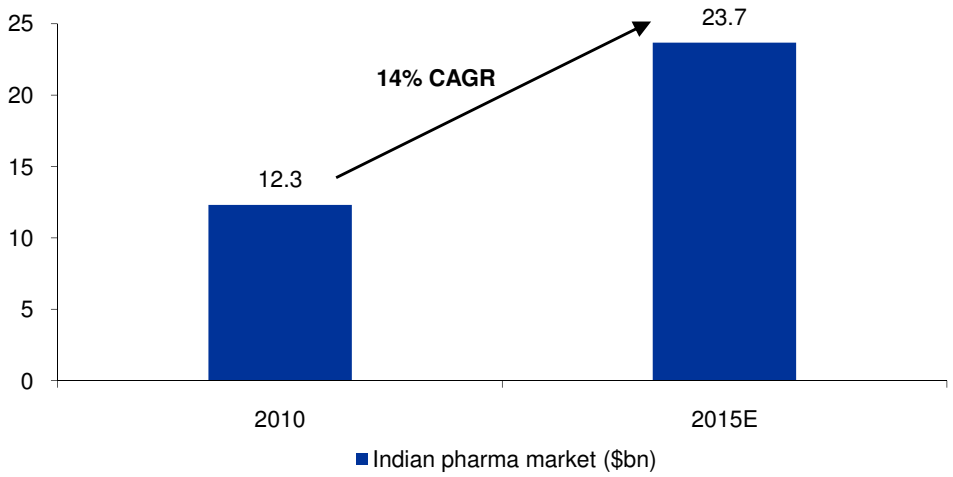
- Domestic formulations is one of the most profitable segments for Indian pharma companies. IMS forecasts the $12.3bn (2010) Indian pharmaceutical industry to grow at 14-17% in 2010-2015. Factors driving this growth include 1) rising prevalence of chronic diseases 2) rising household incomes leading to higher spending on health 3) growing health insurance penetration 4) changing demographics 4) rapidly growing healthcare delivery market 5) heavy investments in healthcare infrastructure 5) rising penetration in tier II to IV towns and rural areas
- However, our growth estimate is at the lower end of this range, considering the extreme price sensitivity and intense competition in the market. Given the semi-regulated nature of the market with low barriers to entry, we expect competition to further intensify, especially in acute segments which still constitute ~65% of the market. We attribute the slower growth rates for most of the larger players in the last couple of quarters to aggressive marketing strategies adopted by the smaller players, including huge discounts and bonuses to channels and heavy incentives to doctors and key opinion leaders.

India's healthcare industry segments



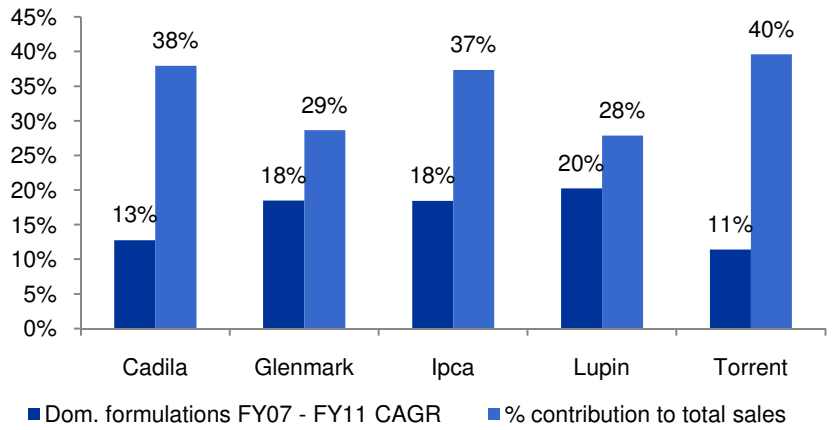
Source: Max India, Spark Capital Research

To grow at 14% CAGR through 2015



Source: Spark Capital Research

Exposure to domestic market for coverage companies

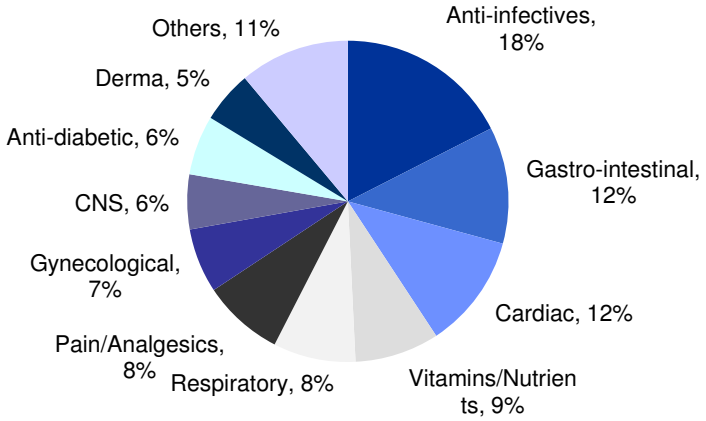


Source: Company data, Spark Capital Research

Chronic therapeutic segments gaining prominence

Sector Outlook Positive

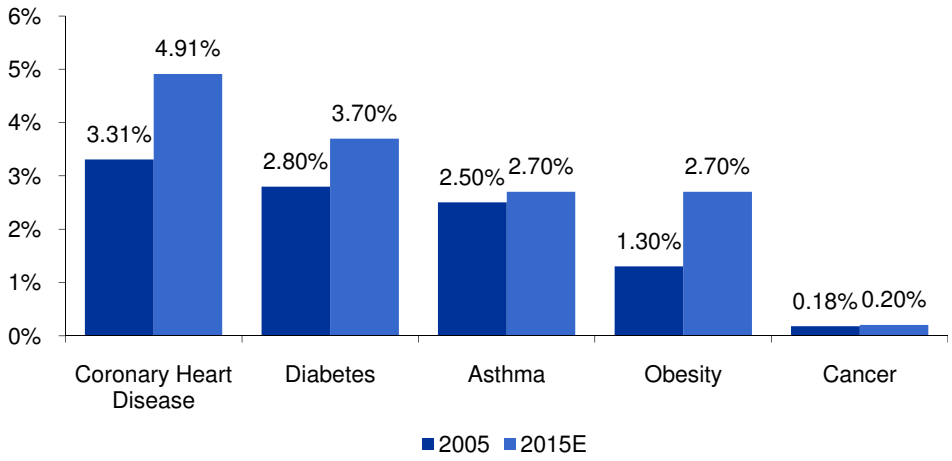
Indian pharma market by therapeutic area



Source: IBEF, Spark Capital Research

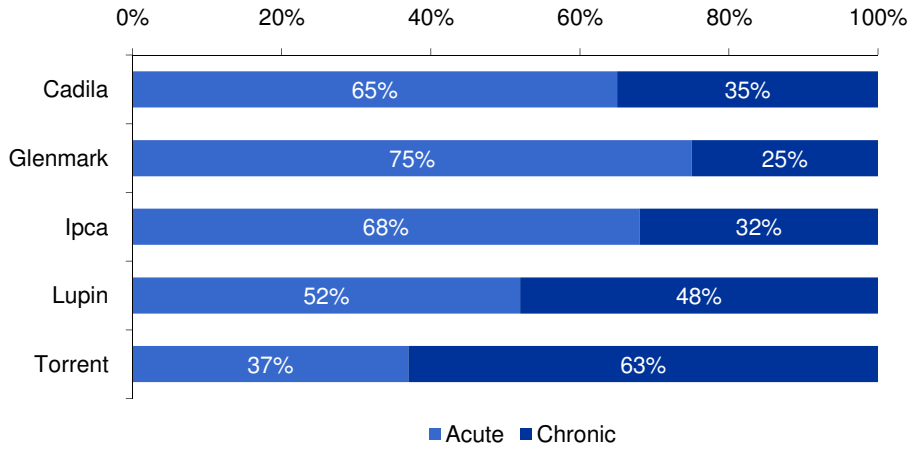
- Traditionally, acute therapies have dominated the Indian pharma market, holding a significantly higher share than chronic segments
- But, with changing lifestyles and demographics, the disease profile of the Indian population is shifting towards chronic ailments. For instance, India has the largest number of diabetics in the world. The number of diabetics is estimated at over 40 million, projected to rise to ~75 million by 2025. Cancers and cardiovascular disorders are other fast-growing disease areas. The acute vs. chronic mix in the Indian pharmaceutical market is expected to change from 65:35 currently to 60:40 by 2015
- The chronic segment tends to have a more sticky patient base due to the closer monitoring and longer duration required for treatment. The segment is also relatively immune to the aggressive pricing strategies adopted by some of the newer players
- Among our coverage companies, Torrent has the most favorable acute vs. chronic product mix, with >60% of its sales from chronic segments

Rising prevalence of several chronic diseases



Source: McKinsey, Spark Capital Research

Torrent has the most favorable acute vs. chronic sales mix

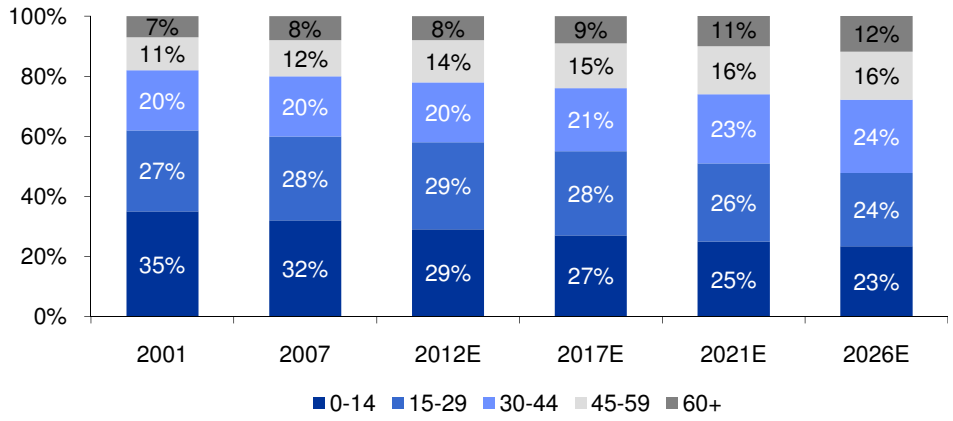


Source: Spark Capital Research

Strong long-term demand drivers

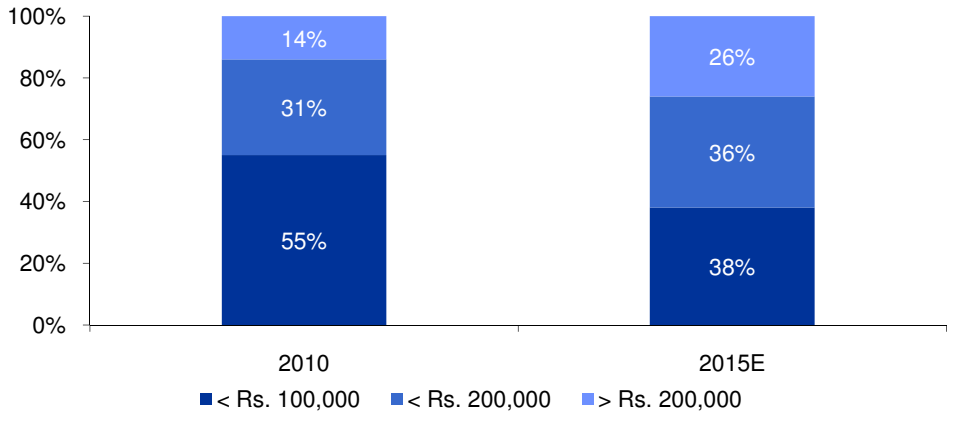
Sector Outlook Positive

Demographic shift to older-age group



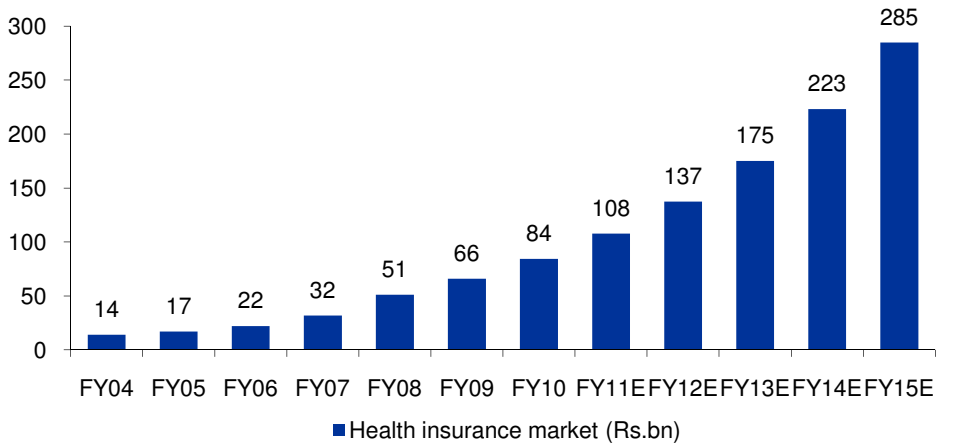
Source: Apollo Hospitals, Spark Capital Research

Rising household incomes to drive healthcare spending



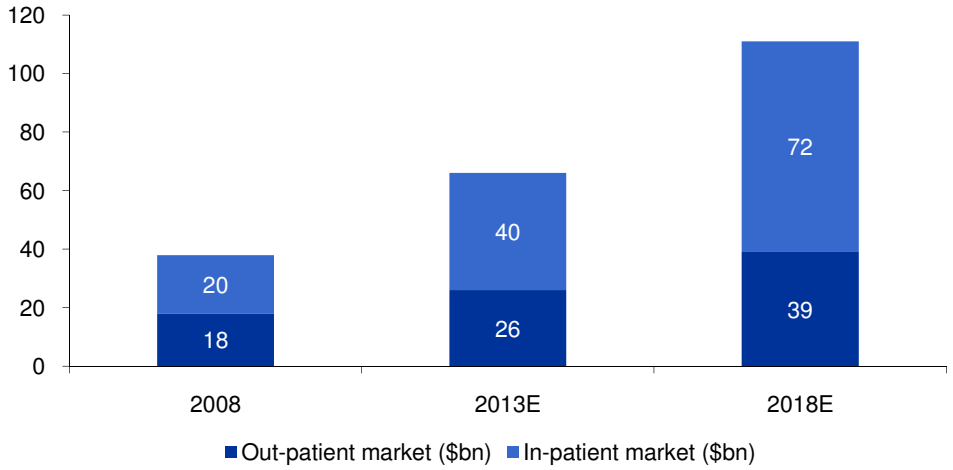
Source: Apollo Hospitals, Spark Capital Research

Growing health insurance market



Source: Max India, Spark Capital Research

Expanding healthcare delivery market



Source: Apollo Hospitals, Spark Capital Research

Coverage universe to grow above industry

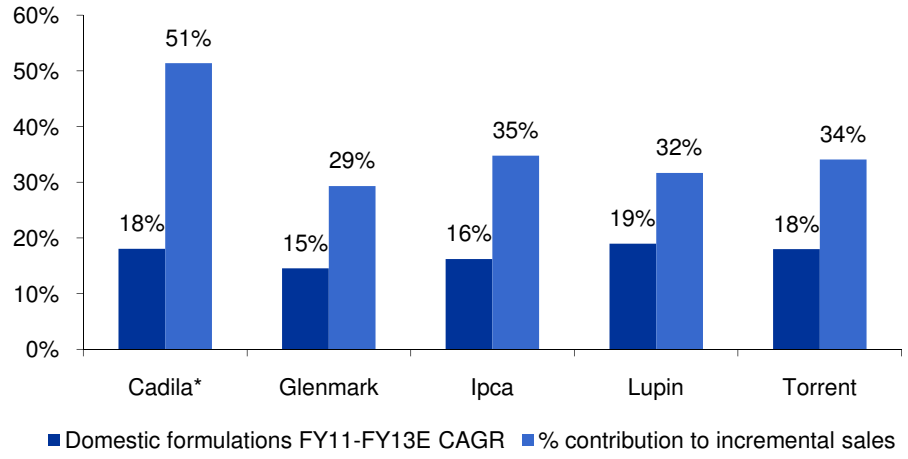
Sector Outlook Positive

Domestic formulations – snapshot

Company	Top therapeutic segments (% of domestic sales)	Key brands	Brands in top 300	Market Share	Chronic therapies	FY11-13E CAGR*	Key differentiators
Cadila	CVS (20%), GI (17%), Respiratory (11%)	Aten, Deriphyllin, Atorva, Ocid	17	3.8%	35%	18.0%	Diversified portfolio with strong brands across therapeutic segments. Recent forays into vaccines and biologics will be future growth drivers. Bayer JV to launch patented drugs from Bayer's pipeline
Glenmark	Dermatology (29%), CVS (17%), Respiratory (15%)	Candid, Ascoril, Telma	5	1.5%	25%	14.6%	Leader in dermatology (8.3% market share) segment. Strong respiratory segment (2.8% market share) with capabilities in inhalers (MDIs, DPIs)
Ipca	CVS & Anti-diabetic (27%), Anti-malarial (17%)	Zerodol, Lariago, Rapither	5	1.2%	32%	16.2%	Leading supplier of anti-malarial drugs. Also strong in anti-infective, cardiovascular and anti-diabetic segments
Lupin	CVS (21%), Anti-TB (10%), Respiratory (9%)	Tonact, Ramistar, Gluconorm G	4	2.8%	48%	19.0%	Leader in anti-TB drugs. Portfolio shifted to chronic therapies in recent years. Recent partnership with Eli Lilly to market anti-diabetics. Plans to launch biologics
Torrent	CVS (33%), CNS (21%), GI (19%)	Alprax, Topcef, Dilzem	6	1.4%	63%	18.0%	Ranked no. 2 in cardiovascular and no. 3 in neuropsychiatry segments. Expanding reach into tier II to IV cities and rural markets

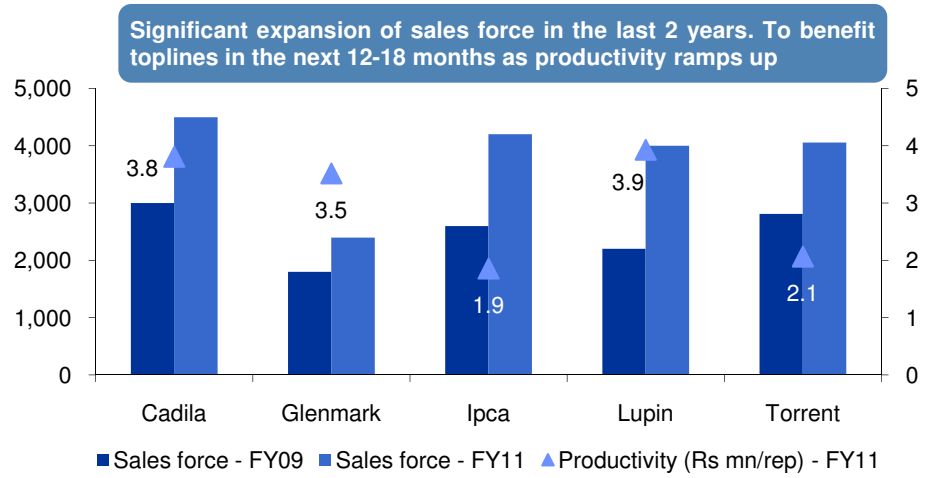
*Source: Company data, Spark Capital Research, * includes Bayer JV for Cadila*

Lupin expected to post strongest growth in FY11-FY13E



Source: Company data, Spark Capital Research, includes Bayer JV

Expansion in sales force; productivity to improve



Source: Company data, Spark Capital Research

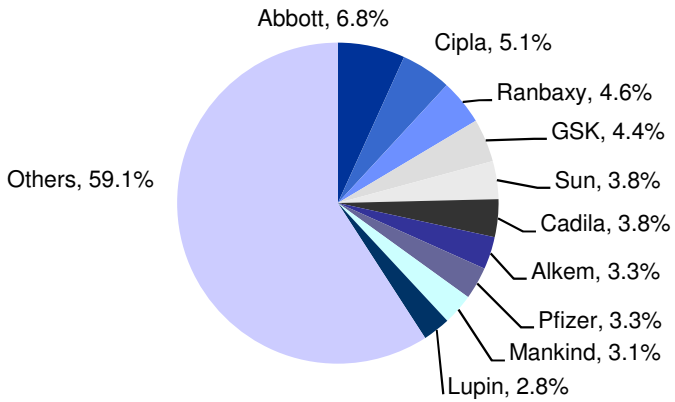
Indian Pharmaceuticals

Competitive pressure to intensify

Initiating Coverage

Sector Outlook | **Positive**

Top 10 players account for ~40% of Indian pharma market



Source: IMS MAT April 2011, Spark Capital Research

- The Indian pharmaceutical market is highly fragmented with top 10 players accounting for only ~40% of the market. Given the semi-regulated nature of the market, we expect competition to further intensify (especially in acute segments which still constitute ~65% of the market)
- Driven by a higher confidence in India's IP protection laws following the advent of the product patent regime in 2005, MNCs have shown renewed interest in the Indian pharma market. MNCs have launched branded generic products at steep discounts to their global prices enabling them to compete with the domestic players in the price sensitive Indian market. The new patent regime has also allowed MNCs to launch patented products at a premium (table shows patented products launched from 2008). IMS expects the sale of patented products to exceed $5bn by 2015
- MNCs have also taken the inorganic route by acquiring Indian companies to gain access to their infrastructure, distribution network, prescription base and local management capabilities. We expect the domestic formulations business of Indian players to remain attractive targets for MNCs

Recent acquisitions of Indian pharma companies by MNCs

Date	Acquirer	Target	Deal Value ($mn)
Dec-10	Reckitt Benckiser	Paras	726
May-10	Abbott	Piramal	3,720
Dec-09	Hospira	Orchid (injectables)	~400
Jul-09	Sanofi Aventis	Shantha Biotech	784
Jul-09	Abbott	Wockhardt (nutritional brands)	130
Jun-08	Daichi Sankyo	Ranbaxy	~4,400 (58% stake)
Apr-08	Fresenius Kabi	Dabur Pharma	~300 (91% stake)
Aug-06	Mylan	Matrix	~900

Source: Spark Capital Research

Patented products launched in India (2008-2010)

Year	Company	Product	Indication
2010	Bristol Myers Squibb	Onglyza	Diabetes
2010	Merck	Isentress	HIV
2009	GSK	Cervarix	Cervical cancer vaccine
2009	AstraZeneca	Crestor	Dyslipidemia
2009	Novartis	Galvus	Diabetes
2008	GSK	Rotarix	Rotavirus vaccine
2008	GSK	Infantrix	DP'T vaccine
2008	Pfizer	Sutent	Kidney cancer
2008	J&J	Intelence	HIV
2008	Pfizer	Champix	Smoking cessation
2008	Merck	Januvia	Diabetes
2008	GSK	Tykerb	Breast cancer
2008	Merck	Gardasil	Cervical cancer vaccine

Source: Spark Capital Research

Framework of analysis

Business Analysis –Ranking (Ranks: 1-6 with 1 being the best)

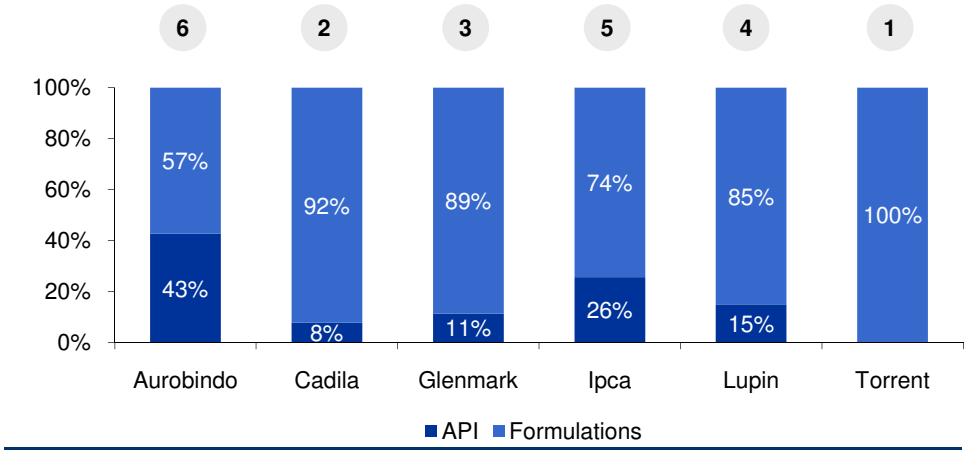
Sector Outlook	Positive

Ranks on Qualitative Parameters	Weight	Aurobindo	Cadila	Glenmark	Ipca	Lupin	Torrent
Sales mix (API vs. Formulations)	10%	6	2	3	5	4	1
Capabilities in high-end segments	10%	6	2	1	5	3	4
Compliance track record	10%	6	4	2	5	3	1
Accounting conservatism	10%	3	4	6	1	5	2
US pipeline	10%	4	3	2	6	1	5
ANDAs pending approval	10%	2	3	4	6	1	5
Acute vs. chronic mix of domestic sales	10%	6	3	5	4	2	1
Presence in key therapeutic areas	10%	6	3	4	5	1	2
Sales force productivity	10%	6	2	3	5	1	4
Positioning in other markets	10%	6	4	1	5	2	3
Qualitative Rank – 50%	**100%**	**6**	**3**	**4**	**5**	**1**	**2**
Ranks on Quantitative parameters							
EBITDA margin (Avg of FY12E and FY13E)	10%	5	1	3	2	4	6
FY11-FY13E EPS growth	20%	6	4	5	2	3	1
Working capital (FY11)	10%	5	1	6	4	3	2
Net debt / equity (FY11)	15%	5	3	6	4	2	1
RoCE (Avg of FY12E and FY13E)	15%	6	1	5	4	2	3
Fixed asset turnover (FY11)	10%	5	4	6	2	3	1
OCF / Capex (FY12 and FY13)	15%	4	2	6	5	1	3
OCF / PAT (FY12 and FY13)	5%	6	1	4	5	2	3
Quantitative Rank – 50%	**100%**	**5**	**2**	**6**	**4**	**3**	**1**
Overall Rank	**100%**	**6**	**3**	**5**	**4**	**2**	**1**

Qualitative Ranking (1/3)

Sector Outlook Positive

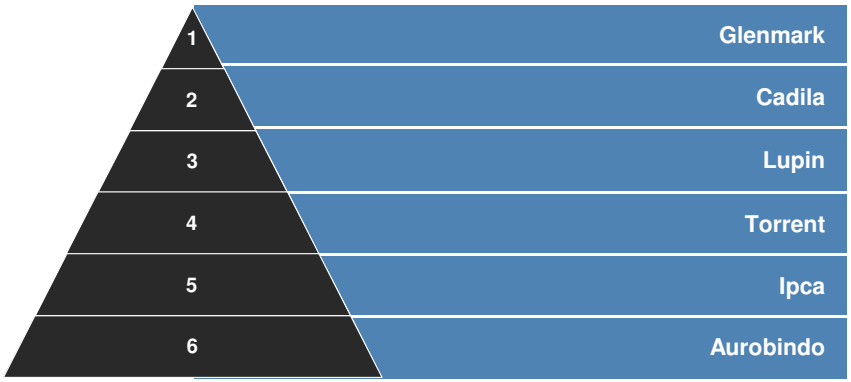
Sales mix (FY11)



Source: Company data, Spark Capital Research

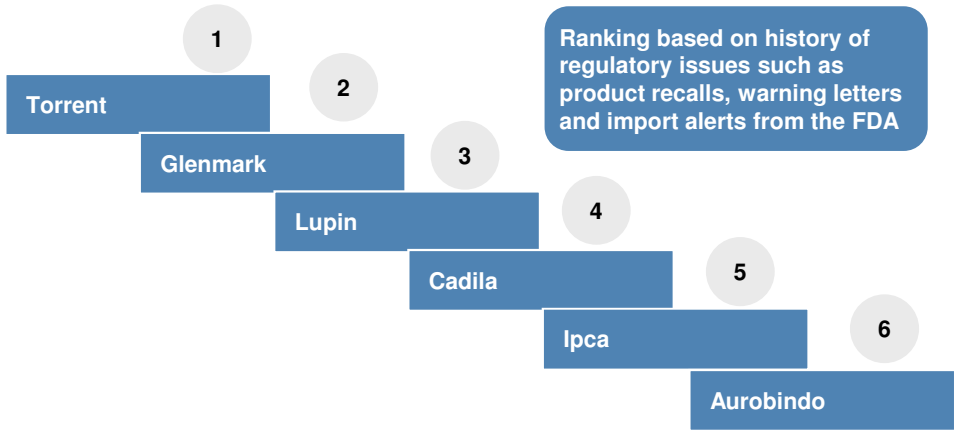
Capabilities in high-end segments

We rank companies based on their capabilities in high-end areas such as NCE research and NDDS



Source: Spark Capital Research

Compliance track record

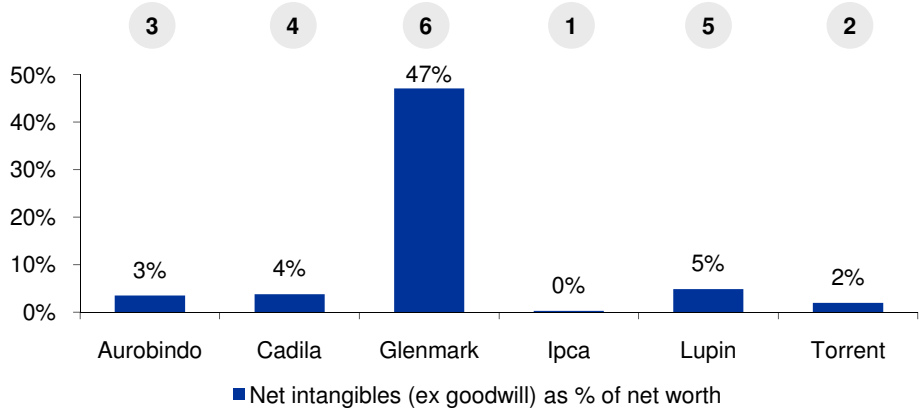


Ranking based on history of regulatory issues such as product recalls, warning letters and import alerts from the FDA

Source: Spark Capital Research

Accounting conservatism

Glenmark has continued to capitalize a significant part of R&D costs resulting in high intangible assets on its balance sheet



Source: Company data, Spark Capital Research

Qualitative Ranking (2/3)

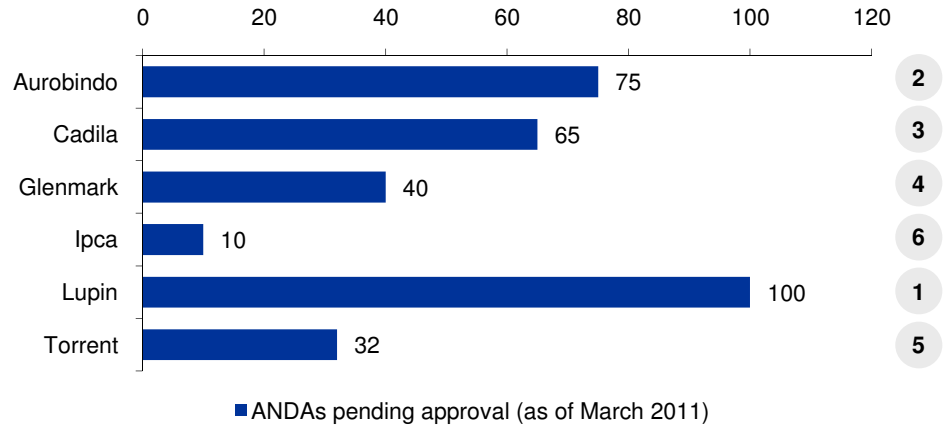
US product pipeline

	Aurobindo	Cadila	Glenmark	Lupin
Branded				
Hormones/OCs				
Ophthalmic				
Oncology				
Injectables				
Topical / transdermal				
Controlled-release				
Nasal				
Ranking	4	3	2	1

Launched | Pending approval | Filings expected

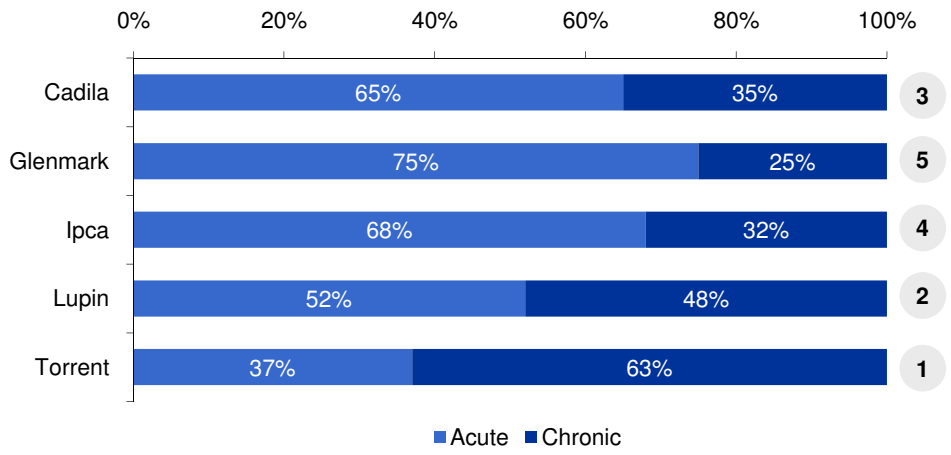
Source: Spark Capital Research

ANDAs pending approval



Source: Company data, Spark Capital Research

Acute vs. chronic mix of domestic sales



Source: Spark Capital Research

Presence in key therapeutic areas

Attractiveness

	Cadila	Glenmark	Ipca	Lupin	Torrent
Anti-diabetic					
CVS					
CNS					
Gastro-intestinal					
Dermatology					
Gynecology					
Respiratory					
Pain					
Anti-infective					
Ranking	3	4	5	1	2

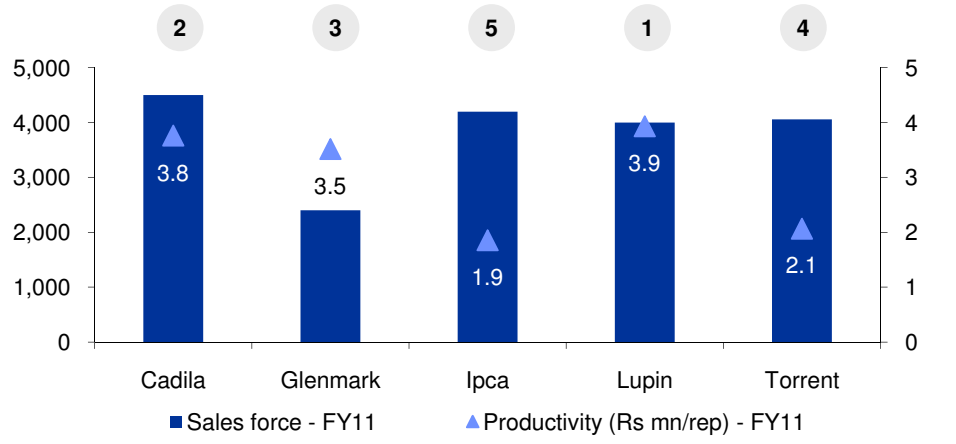
Strong | Medium | Weak

Source: Spark Capital Research

Qualitative Ranking (3/3)

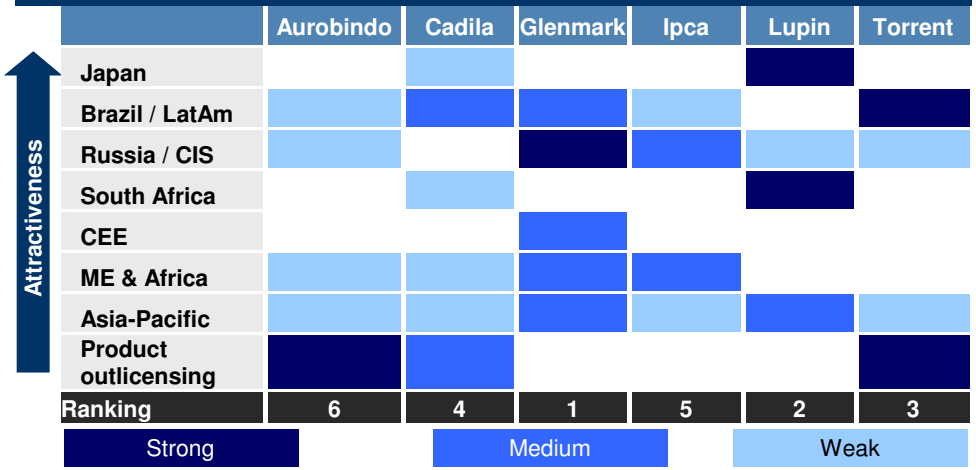
Sector Outlook	Positive

Sales force productivity



Source: Company data, Spark Capital Research

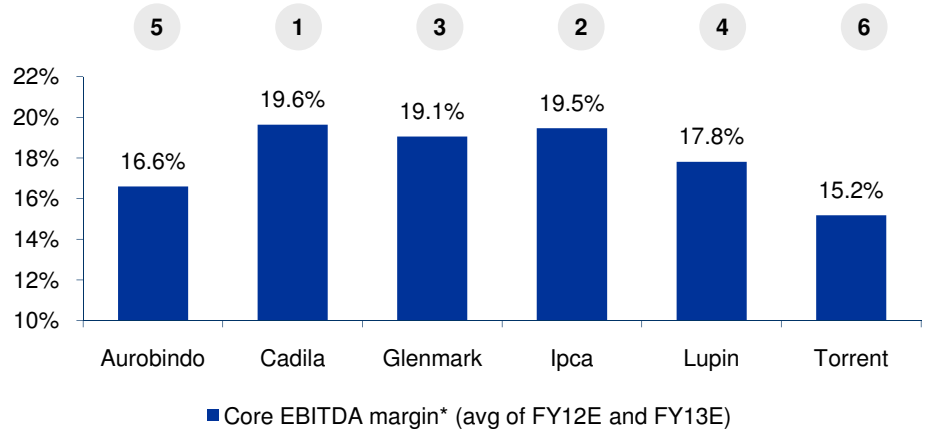
Positioning in other markets



Source: Spark Capital Research

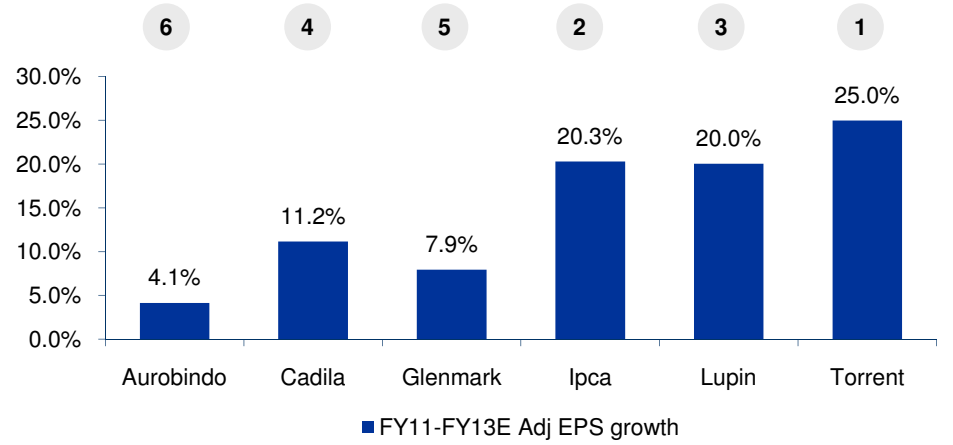
Quantitative Ranking (1/2)

Core EBITDA margin



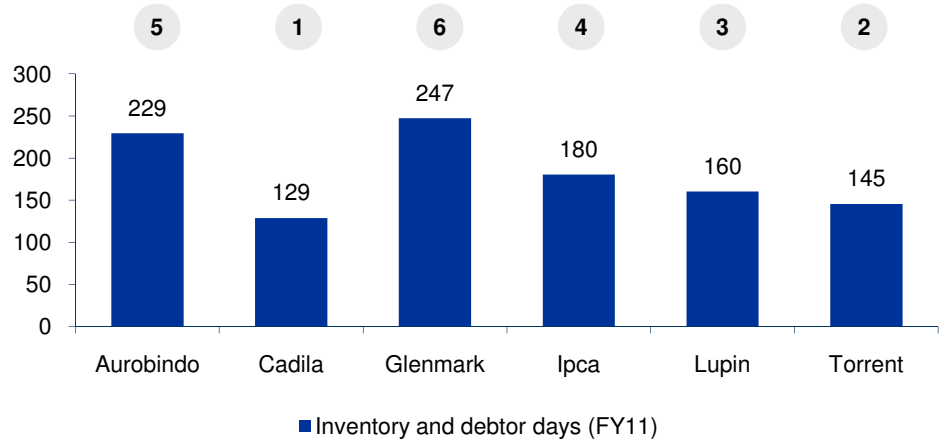
*Source: Spark Capital Research, *excludes outlicensing income & other operating income*

FY11-FY13E EPS growth



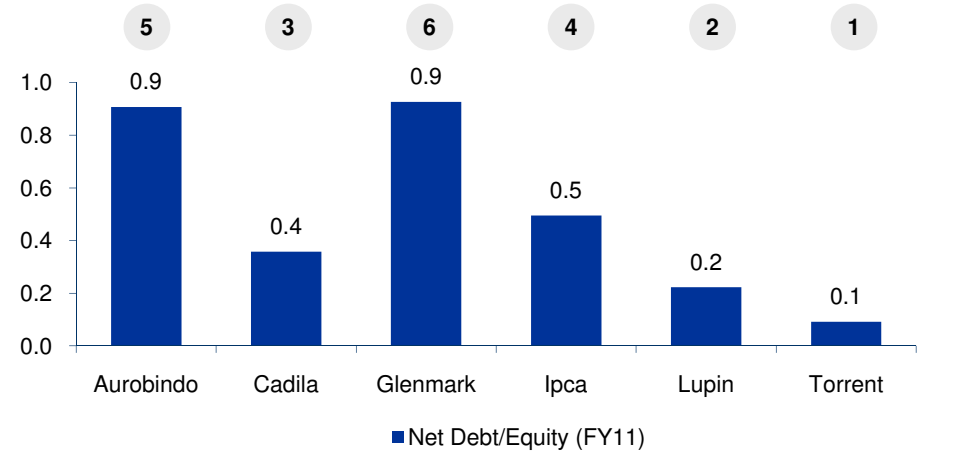
Source: Company data, Spark Capital Research

Working capital



Source: Company data, Spark Capital Research

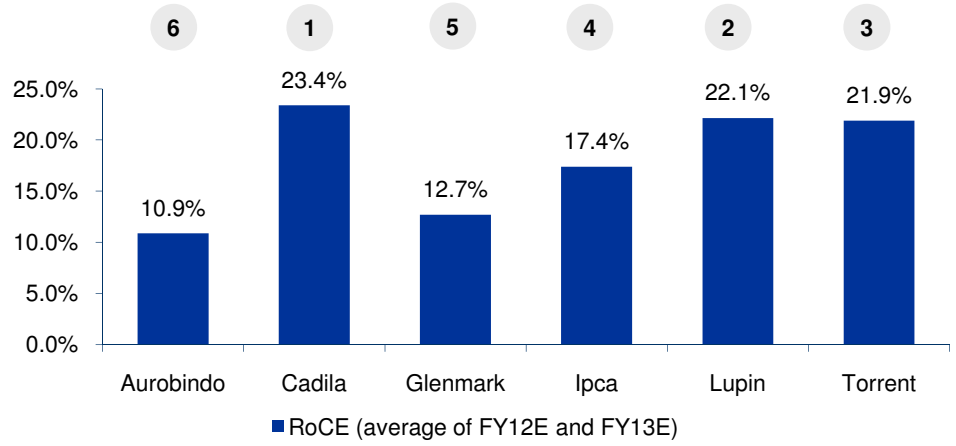
Leverage



Source: Company data, Spark Capital Research

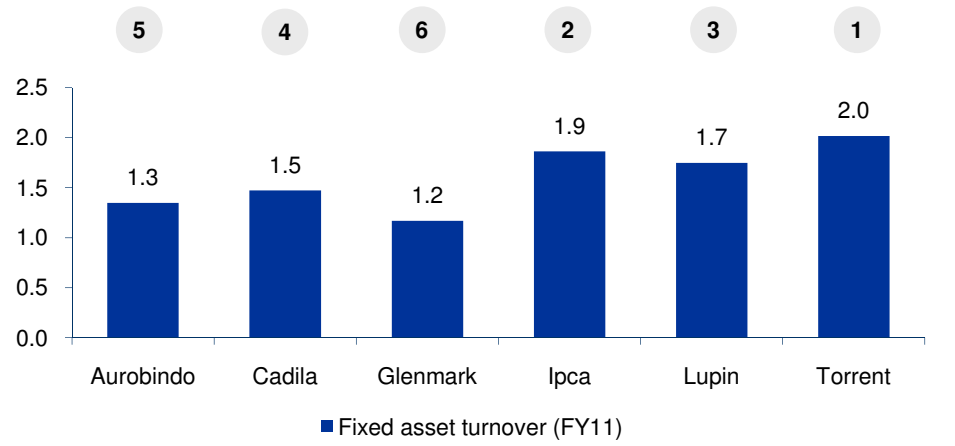
Quantitative Ranking (2/2)

RoCE



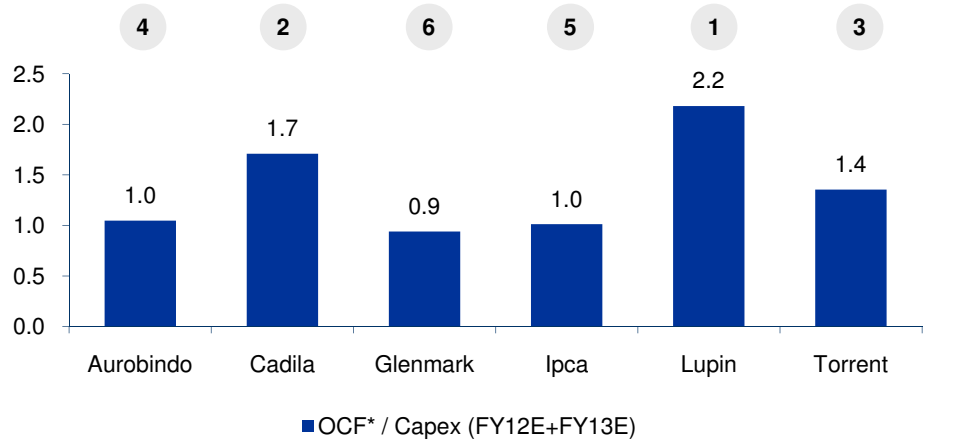
Source: Spark Capital Research

Fixed asset turnover



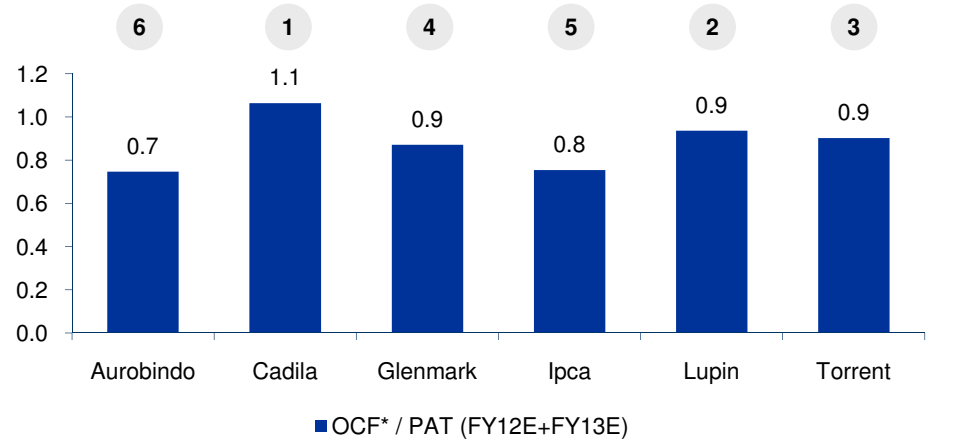
Source: Company data, Spark Capital Research

OCF / Capex



*Source: Spark Capital Research, *net of interest*

OCF / PAT



*Source: Spark Capital Research, *net of interest*

Company Section

Aurobindo Pharma

Challenging times

CMP	Rs. 131	Absolute	Reduce
Target	Rs. 128	Relative	Underperform

The recent import alert on Aurobindo's Unit VI facility (~$40mn of annualized sales), the warning letter for its Unit III facility and frequent product recalls have raised concerns about the sustainability of the company's US growth. We also expect the company's profitability to be impacted in the near-term by 1) decline in dossier outlicensing income 2) fixed costs at Unit VI 3) higher interest expense following FCCB refinancing in Q1 FY12. The stock has de-rated sharply since regulatory issues with the FDA was first made public in early 2011. We do not see concerns abating in the near-term and given the muted earnings growth in FY11-FY13E, we believe a significant re-rating of the business is unlikely. We value the stock at 7.0x FY13E EPS of Rs. 18.3 to arrive at our target price of Rs. 128 and initiate coverage with a Reduce/Underperform rating

Investment rationale

- **Regulatory challenges could derail ambitions in the US:** Aurobindo, in spite of its focus on commoditized generics, has grown rapidly in the world's largest generic market through 1) aggressive filings for a wide basket of products 2) product supply contract with Pfizer 3) competitive pricing. However, the recent import alert on its Unit VI facility (~$40mn of annualized sales), the warning letter for its Unit III facility and frequent product recalls have raised concerns about the sustainability of this growth. Though the recently launched limited-competition product Tazo-Pip (five-player market currently) could offset some of the lost sales from Unit VI, we expect the next 12-18 months to be challenging for Aurobindo's US business
- **MNC supplies to boost emerging markets sales, ARV growth to taper:** We expect Aurobindo's non-US formulations business to benefit from product supply deals with Pfizer and AstraZeneca. These deals provide Aurobindo the platform to participate in the attractive emerging markets branded generic opportunity. The company has generated income of Rs. 2bn in FY10 and Rs. 2.6bn in FY11 by outlicensing product dossiers as part of these contracts. Assuming normal regulatory timelines, we expect supplies to begin in FY13 and ramp up in FY14. We believe Aurobindo's Anti-Retroviral (ARV) business has limited growth prospects considering the funding constraints for programs such as PEPFAR and pricing pressures in the segment
- **EBITDA margins to come under stress:** We expect Aurobindo's EBITDA margins to decline in FY12 on account of 1) decline in dossier outlicensing income (from Rs. 2bn in FY10 and Rs. 2.6bn in FY11) 2) ~Rs. 600mn of fixed costs at Unit VI, which is under import alert. A slower-than-estimated growth in the US could further erode margins. The higher interest expense from the refinancing of $204mn (including redemption premium) FCCB obligations in May 2011, will also impact profitability from FY12. The company reported a net loss of Rs. 1.2bn in Q1 FY12 on account of the FCCB repayment
- **Restructuring committee exploring options to unlock value:** In spite of the shift in product mix in favor of formulations in recent years, APIs still contribute ~43% to Aurobindo's top-line. This segment mainly supplies low value SSPs and cephalosporin APIs (together ~80% of API business) in India and other emerging markets. Of late, the company has used its API capacities mostly for its own formulations business and we expect this trend to continue. The company's board has recently appointed a 'restructuring committee' to consider various options to unlock value including a demerger of the API and formulations businesses

Financial summary

Year	Sales (Rs. mn)	EBITDA (Rs. mn)	Adj PAT (Rs. mn)	Adj EPS (Rs.)	P/E (x)	ROE (%)
FY11E	41,259	7,042	5,397	16.9	7.8	25.2
FY12E	46,335	7,559	4,890	16.8	7.8	19.1
FY13E	51,511	8,686	5,322	18.3	7.2	18.3

Initiating coverage

Date	Sep 13, 2011
Market Data	
SENSEX	16502
Nifty	4947
Bloomberg	ARBP IN
Shares o/s	291mn
Market Cap	Rs. 38bn
52-wk High-Low	Rs. 275-123
3m Avg. Daily Vol	Rs. 215mn
Index member	BSETHC
Latest shareholding (%)	
Promoters	54.4
Institutions	32.3
Public	13.4

Stock performance (%)

	1m	3m	12m
ARBP	-16%	-25%	-37%
Sensex	-2%	-10%	-14%
BSETHC	-2%	-6%	4%

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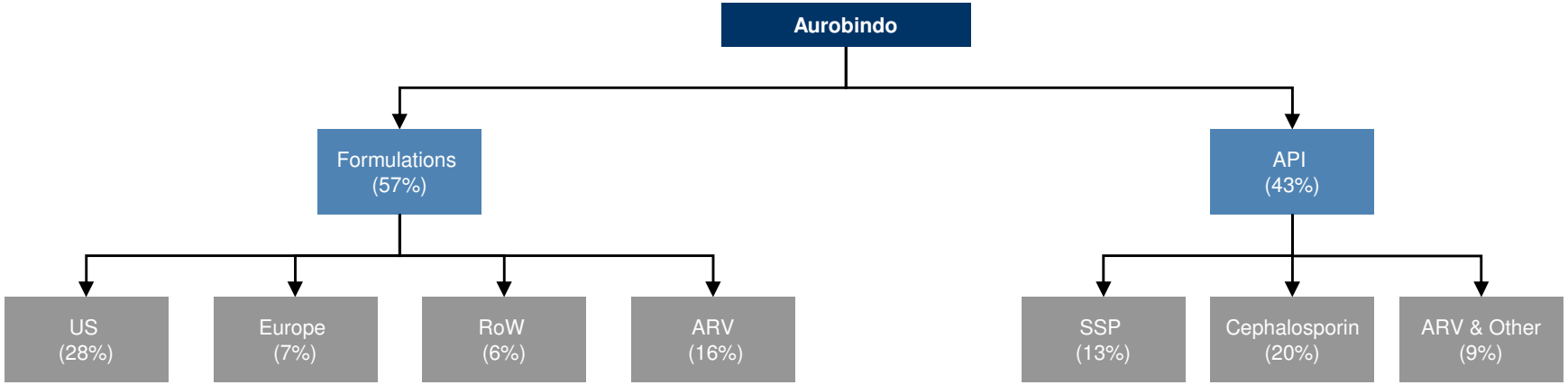
Aurobindo Pharma

CMP	Rs. 131	Absolute	Reduce
Target	Rs. 128	Relative	Underperform

Company Overview

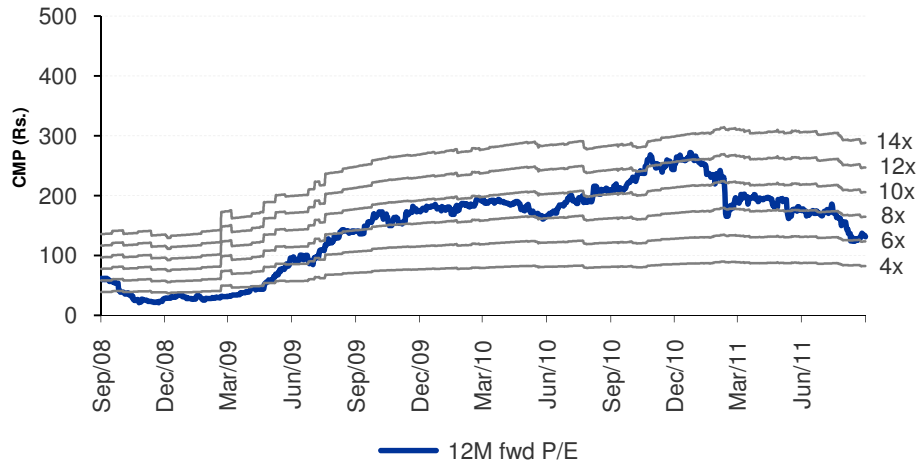
Sales breakup (FY11)



Source: Company, Spark Capital Research

At CMP of Rs. 131, Aurobindo trades at 7.8x FY12E EPS and 7.2x FY13E EPS, a huge discount to our coverage universe. The stock has de-rated sharply since regulatory issues with the FDA was first made public in early 2011. We do not see the concerns abating in the near-term and given the muted earnings growth in FY11-FY13E, we believe a significant re-rating of the business is unlikely. We value the stock at 7.0x FY13E EPS of Rs. 18.3 to arrive at our target price of Rs. 128, a 3% downside from current levels.

P/E Band



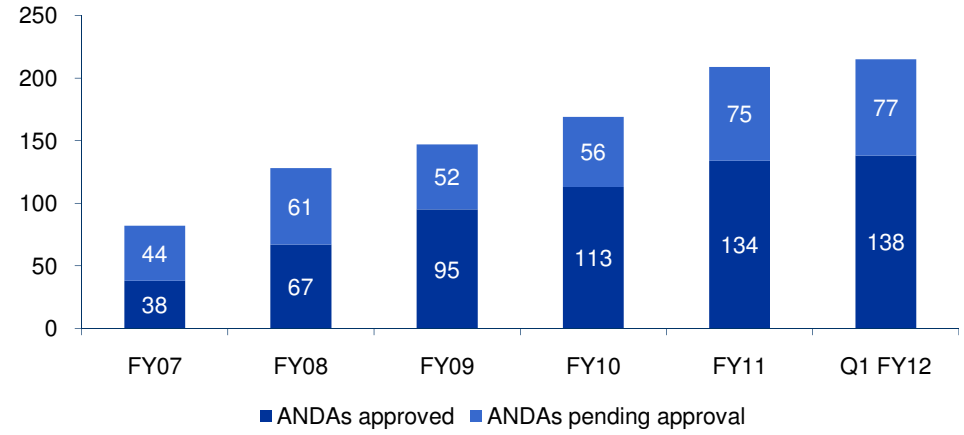
Source: Bloomberg, Spark Capital Research

Aurobindo Pharma

CMP	Rs. 131	Absolute	Reduce
Target	Rs. 128	Relative	Underperform

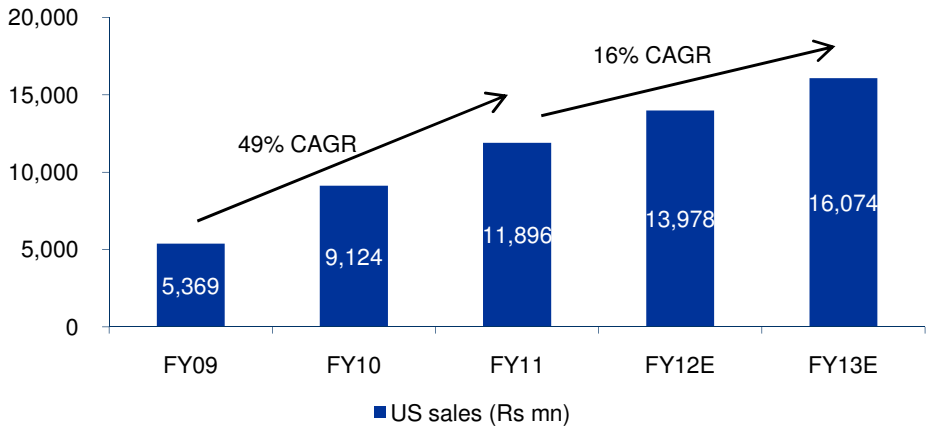
Business Overview

ANDA filings



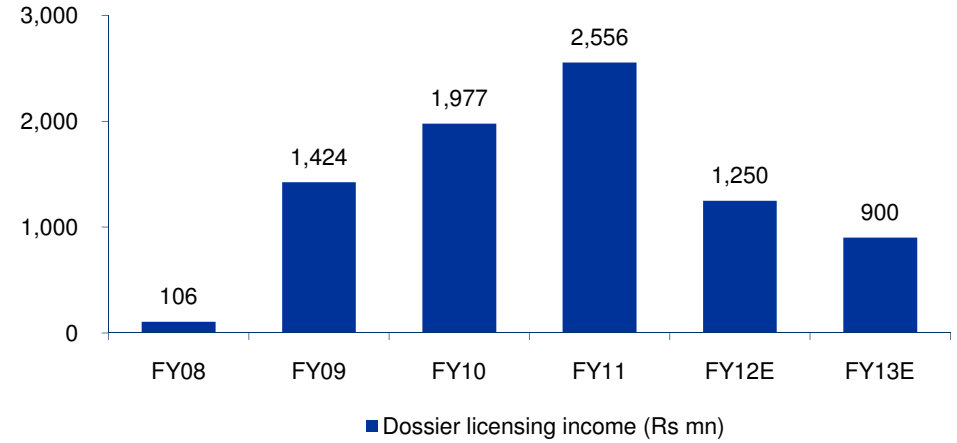
Source: Company data, Spark Capital Research

US business to grow slower



Source: Company data, Spark Capital Research

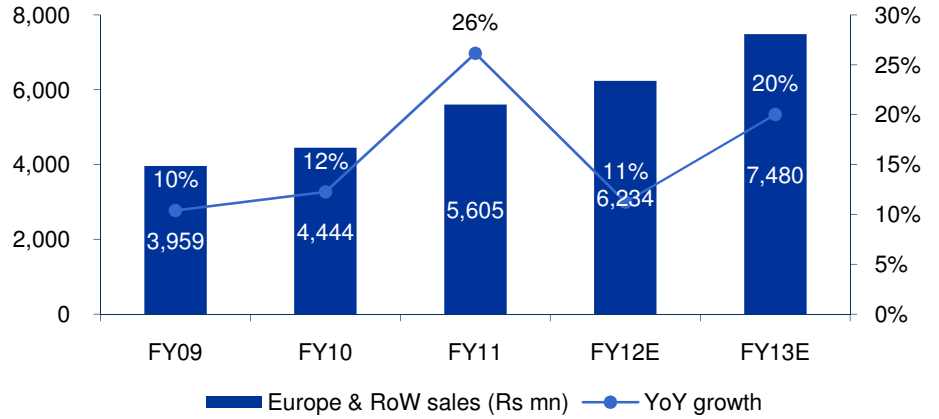
Dossier licensing income to decline from FY12



Source: Company data, Spark Capital Research

Europe & RoW sales

Europe and RoW sales to benefit from product supply deals with Pfizer and AZN



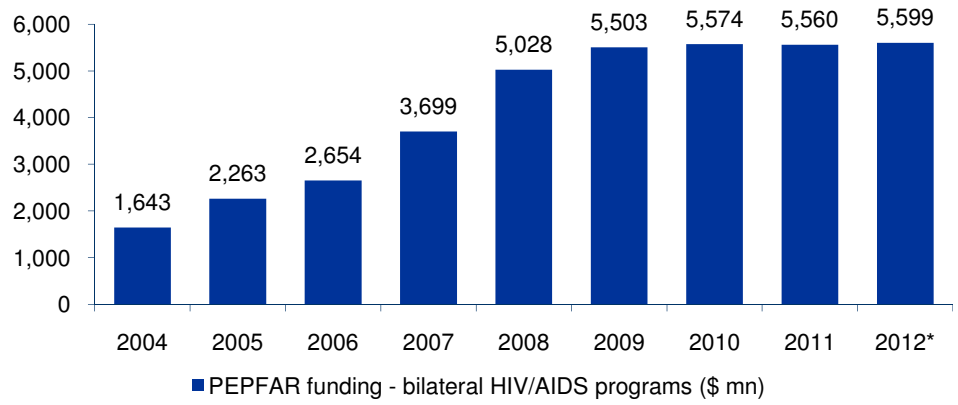
Source: Company data, Spark Capital Research

Aurobindo Pharma

CMP	Rs. 131	Absolute	Reduce
Target	Rs. 128	Relative	Underperform

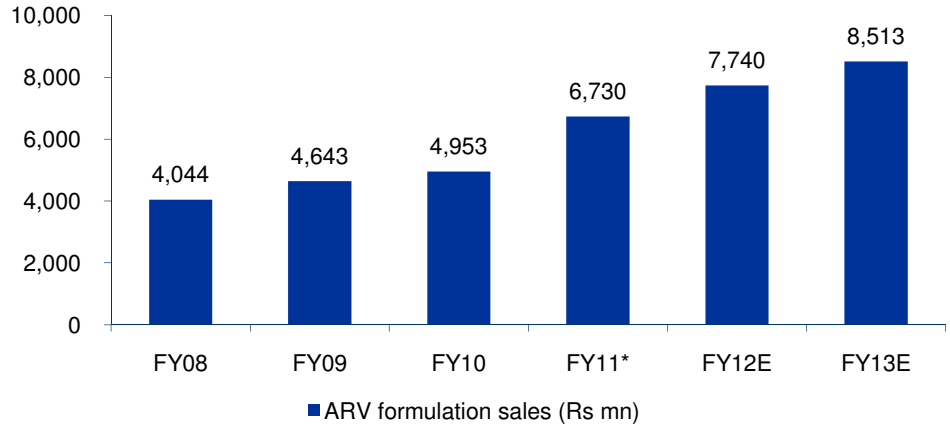
Business Overview

Flat PEPFAR bilateral HIV/AIDS budgets…



*Source: www.pepfar.gov; Spark Capital Research: *Requested*

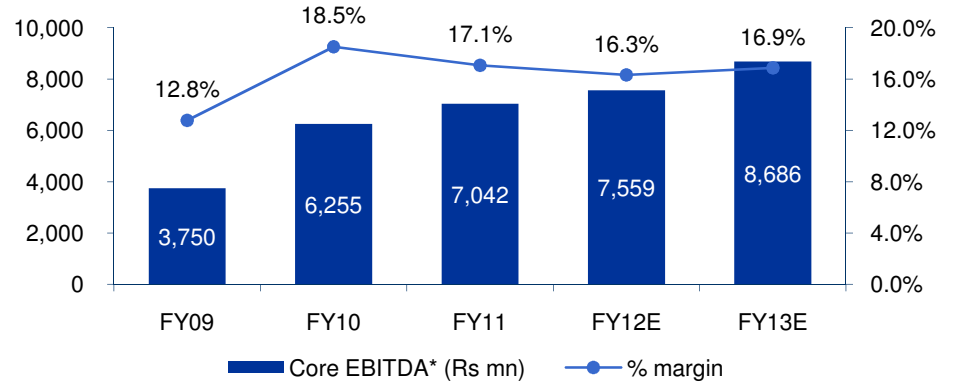
…will limit ARV segment growth



*Source: Spark Capital Research,*growth in FY11 due to segmental reclassification of sales*

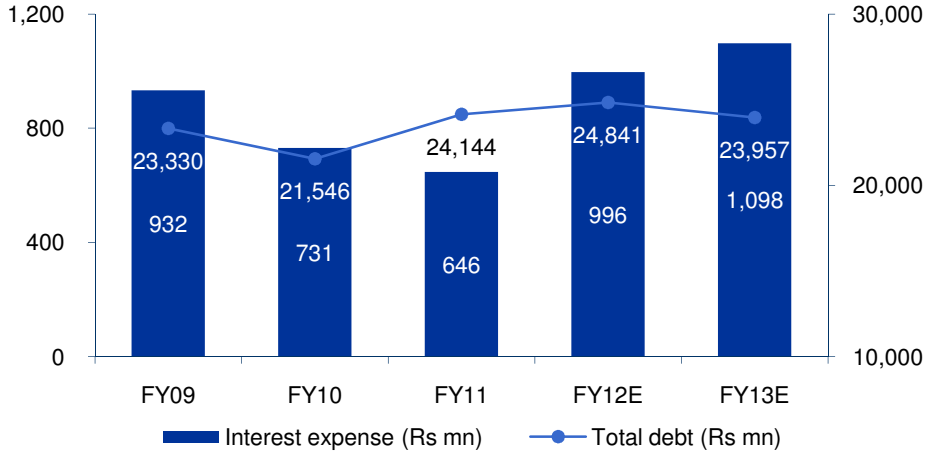
Core EBITDA margin

Core EBITDA margins to decline in FY12 mainly on account of fixed costs at Unit VI (which is under FDA import alert), estimated at ~Rs. 600mn per year



*Source: Company data, Spark Capital Research, *excludes dossier sales*

FCCB refinancing to lead to higher interest expense from FY12



Source: Company data, Spark Capital Research

Aurobindo Pharma

CMP	Rs. 131	Absolute	Reduce
Target	Rs. 128	Relative	Underperform

Financial Summary

Abridged Financial Statements (Consolidated)				
Rs. mn	FY10	FY11	FY12E	FY13E
Profit & Loss				
Net sales	**33,777**	**41,259**	**46,335**	**51,511**
EBITDA	6,255	7,042	7,559	8,686
Depreciation	(1,493)	(1,715)	(1,851)	(1,919)
EBIT	4,761	5,327	5,708	6,767
Other Income	3,493	3,305	1,553	1,193
Interest	(731)	(646)	(4,195)	(1,098)
PBT	7,523	7,985	3,065	6,862
PAT	5,634	5,635	2,395	5,322
Adjusted PAT	**4,812**	**5,397**	**4,890**	**5,322**
Balance Sheet				
Net Worth	18,334	24,539	26,567	31,448
Deferred Tax	912	1,183	1,183	1,183
Total debt	21,546	24,144	24,841	23,957
Total Networth and liabilities	**40,792**	**49,866**	**52,590**	**56,588**
Gross Fixed assets	29,778	31,416	34,416	36,916
Net fixed assets	22,809	24,422	25,571	26,152
Investments	3	385	385	385
Inventories	11,025	14,553	15,848	17,037
Sundry Debtors	9,560	12,434	13,504	16,243
Cash and bank balances	728	1,882	1,500	1,250
Loans and advances	3,746	5,053	5,670	6,302
Current liabilities	7,080	8,863	9,888	10,781
Net current assets	17,979	25,059	26,633	30,051
Total assets	**40,792**	**49,866**	**52,590**	**56,588**
Cash Flows				
Cash flows from Operations	4,287	3,434	6,429	4,627
Cash flows from Investing	(3,990)	(5,945)	(3,000)	(2,500)
Cash flows from Financing	(876)	4,070	(3,811)	(2,377)

Key metrics				
	FY10	FY11	FY12E	FY13E
Growth ratios				
Net sales	15.1%	22.2%	12.3%	11.2%
EBITDA	66.8%	12.6%	7.3%	14.9%
Adjusted PAT	111.3%	12.1%	-9.4%	8.8%
Margin ratios				
EBITDA	18.5%	17.1%	16.3%	16.9%
Adjusted PAT	14.2%	13.1%	10.6%	10.3%
Performance ratios				
RoE	31.3%	25.2%	19.1%	18.3%
RoCE	14.6%	13.6%	10.2%	11.5%
RoA	12.4%	11.9%	9.5%	9.7%
Fixed asset turnover (x)	1.2	1.3	1.4	1.4
Total asset turnover (x)	0.9	0.9	0.9	0.9
Financial stability ratios				
Net Debt to Equity (x)	1.1	0.9	0.9	0.7
Current ratio (x)	3.5	3.8	3.7	3.8
Inventory and debtor days	214	229	226	222
Creditor days	91	93	93	93
Working capital days	123	136	133	129
Interest cover (x)	6.5	8.2	1.4	6.2
Valuation metrics				
Fully Diluted Shares (mn)	316.1	320.0	291.1	291.1
Market cap (Rs.mn)	38,253			
EPS (Rs.)	**15.2**	**16.9**	**16.8**	**18.3**
P/E (x)	**8.6**	**7.8**	**7.8**	**7.2**
EV (Rs.mn)	61,681			
EV/ EBITDA (x)	9.9	8.8	8.2	7.1
BV/ share (Rs.)	57.9	76.4	91.0	107.7
Price to BV (x)	2.3	1.7	1.4	1.2

Cadila Healthcare

Speed breakers ahead

CMP	Rs. 833	Absolute	Reduce
Target	Rs. 755	Relative	Underperform

Driven by strong growth across segments, Cadila has witnessed significant re-rating in the past 2 years. The stock has traded mostly at 20-22x one-year forward earnings in the past 12 months. Though the company appears well-positioned for the long-term, we believe Cadila's premium multiples will come under pressure given the lack of near-term growth drivers. The company also faces a few challenges in the near-term which include expected delays in product approvals in the US on account of the recent WL for its Moraiya facility, slowdown in domestic sales led by acute therapies and lesser contribution from Hospira JV due to recent launches of generic docetaxel by multiple competitors. Given the FY11-FY13E earnings CAGR of 11% (vs. 43% earnings CAGR in FY09-FY11), we value the stock at 18x FY13E earnings to arrive at our target price of Rs. 755 and initiate coverage with a Reduce/Underperform rating

Investment rationale

- **Warning Letter for Moraiya facility to impact near-term prospects in the US:** Cadila received a WL from USFDA for its injectables facility at Moraiya citing failure to maintain adequate microbiological data. Though we remain confident of the company's ability to resolve the issue, the delay in approvals will impact its growth in the near-term. The company had made 14 filings for injectable products from the facility, many of which were due for approval in FY12 and FY13. Management expects no further ANDA approvals for the company this year. Cadila had grown its US generic business to over $200mn sales in FY11 (~60% FY07-FY11 CAGR), mainly on the back of highly commoditized oral solid products. Though we view the company's entry into the attractive controlled-release segment (through Nesher acquisition) and filings in other limited-competition areas such as nasal, transdermals and NDDS based products as positives for the long-term, there is little visibility into product opportunities that can drive near-term growth
- **Nycomed and Hospira JV sales to witness declines from recent levels:** Cadila's highly profitable JVs with Hospira and Nycomed had contributed significantly to its earnings growth in recent years. The patent expiry for Protonix (starting materials sourced from the JV) in the US in Jan 2011 is expected to further erode Nycomed JV sales from FY12. We expect slower ramp up of the supply of other API's from the JV due to the recent acquisition of Nycomed by Takeda. The Hospira JV posted strong sales in the last 2 quarters on the back of Hospira's launch of generic Taxotere (docetaxel) in the US, which is being supplied by the JV. However, recent launches of generic Taxotere by Sun, Accord (both dual vial products versus Hospira's single vial product) and Sandoz (single vial product) will impact Hospira's market share and pricing, resulting in lower sales for the Hospira JV in the coming quarters
- **Domestic business vulnerable to slowdown in acute segments:** After sluggish performances in the previous few years, Cadila's domestic business recovered in FY11, growing 17% YoY, mainly on the back of its aggressive sales push to achieve the $1bn sales target. The domestic pharma market has witnessed a slowdown in the last couple of quarters, particularly in acute therapies due to intense competition from smaller players and Cadila's acute heavy portfolio makes it more vulnerable. We expect the slowdown in acute segments to extend into the next couple of quarters impacting Cadila more compared to peers

Financial summary

Year	Sales (Rs. mn)	EBITDA (Rs. mn)	Adj PAT (Rs. mn)	Adj EPS (Rs.)	P/E (x)	ROE (%)
FY11	44,647	8,607	6,950	33.9	24.5	36.9
FY12E	50,050	9,635	7,461	36.4	22.9	30.3
FY13E	57,617	11,523	8,591	41.9	19.9	27.6

Initiating coverage

Date	Sep 13, 2011
Market Data	
SENSEX	16502
Nifty	4947
Bloomberg	CDH IN
Shares o/s	205mn
Market Cap	Rs. 171bn
52-wk High-Low	Rs. 987-607
3m Avg. Daily Vol	Rs. 118mn
Index member	BSETHC
Latest shareholding (%)	
Promoters	74.8
Institutions	18.3
Public	6.9

Stock performance (%)

	1m	3m	12m
CDH	-2%	-8%	36%
Sensex	-2%	-10%	-14%
BSEHTC	-2%	-6%	4%

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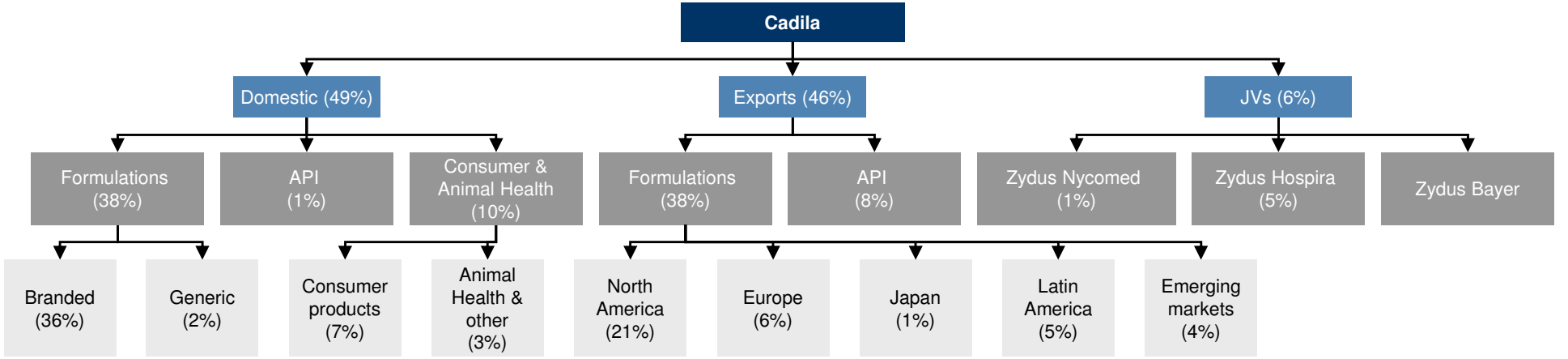
Cadila Healthcare

CMP	Rs. 833	Absolute	Reduce
Target	Rs. 755	Relative	Underperform

Company Overview

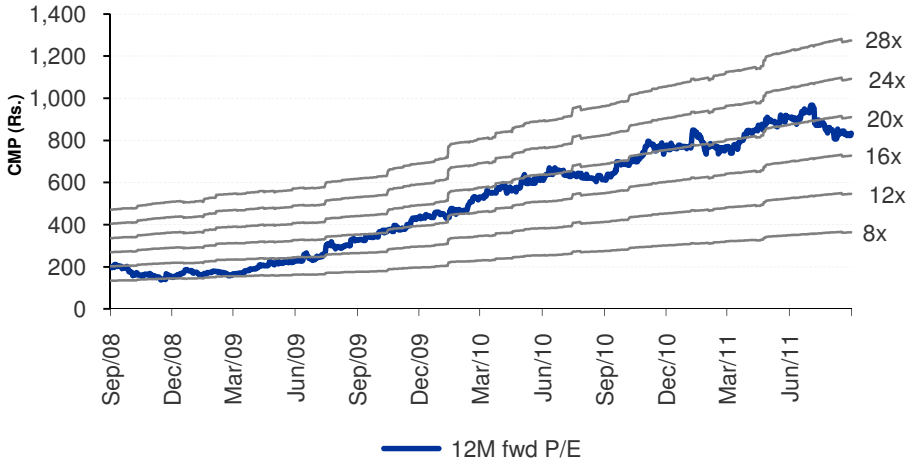
Sales breakup (FY11)



Source: Company, Spark Capital Research

Cadila has witnessed significant re-rating in the past 2 years with multiples expanding from ~10x to over 20x. In our view, the re-rating was driven by strong growth across businesses and easing of concerns related to the impact of pantoprazole patent expiry on its highly profitable Nycomed JV. Over the last 12 months, the stock has traded mostly at 20-22x one-year forward earnings. However, we believe Cadila's premium multiples will come under pressure due to lack of near-term growth drivers. Given the FY11-FY13E earnings CAGR of 11% (vs. 43% earnings CAGR in FY09-FY11), we value the stock at 18x FY13E earnings to arrive at our target price of Rs. 755, implying a 9% downside from current price.

P/E Band



Source: Bloomberg, Spark Capital Research

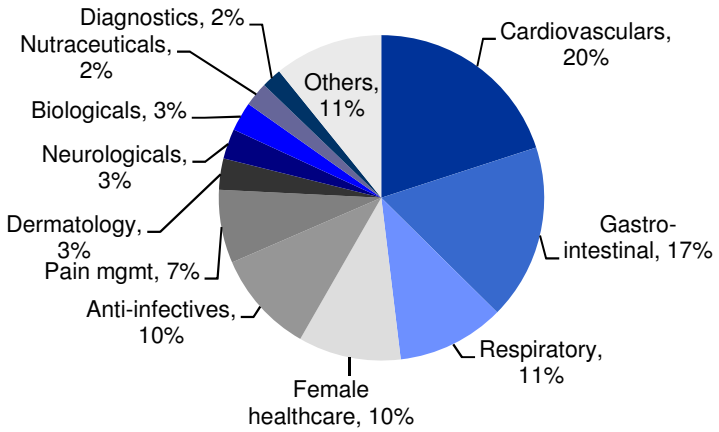
Cadila Healthcare

CMP	Rs. 833	Absolute	Reduce
Target	Rs. 755	Relative	Underperform

Business Overview

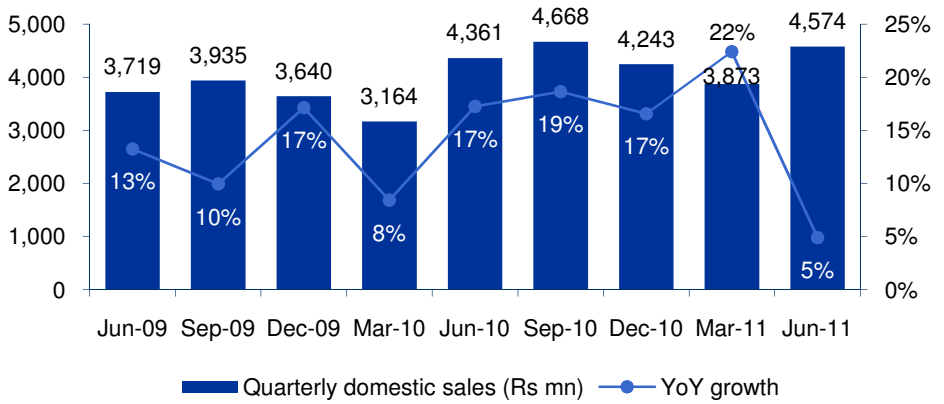
- After sluggish performances in the previous few years Cadila's domestic business recovered in FY11, growing 17% YoY, mainly on the back of its aggressive sales push to achieve the $1bn sales target. The domestic pharma market has witnessed a slowdown in the last couple of quarters, particularly in acute therapies due to intense competition from smaller players and Cadila's acute heavy portfolio makes it more vulnerable. We expect the slowdown in acute segments to extend into the next few quarters impacting Cadila more compared to its peers
- However, we identify multiple long-term value drivers for Cadila's domestic business which include: 1) Biosimilars: recently received marketing approval for erythropoietin (for chronic anemia), completed clinical trials for teriparatide (first generic player) and generic peginterferon alfa-2b (only one other generic currently) 2) Vaccines: launched Vaxiflu-S, the first indigenous H1N1 vaccine and several other vaccine programs underway 3) Bayer Zydus JV: a 50:50 JV with Bayer Healthcare which is expected to launch Bayer's patented products in India

Domestic formulations – therapeutic breakup (FY11)



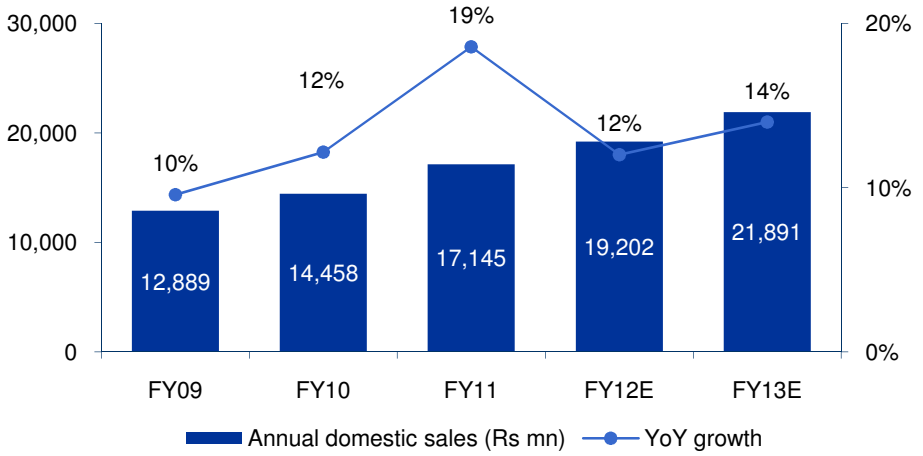
Source: Company data, Spark Capital Research

Domestic formulations – quarterly trend



Source: Company data, Spark Capital Research

Domestic formulations – annual sales*



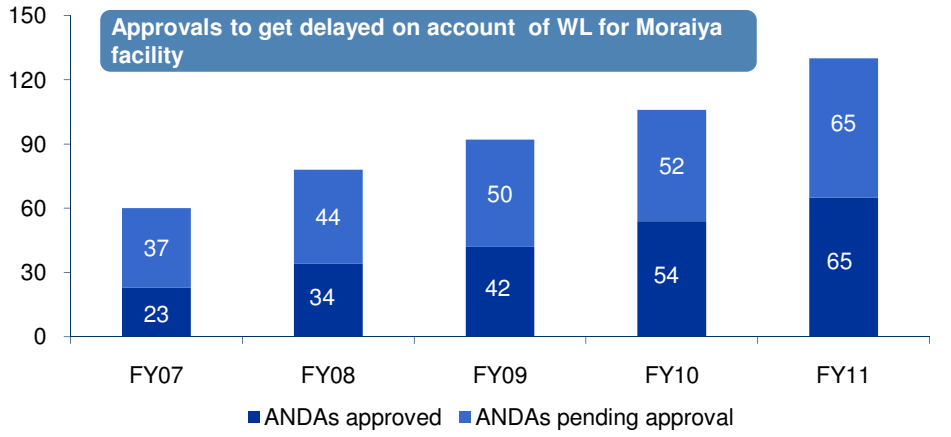
*Source: Company data, Spark Capital Research, *excluding Bayer JV*

Cadila Healthcare

CMP	Rs. 833	Absolute	Reduce
Target	Rs. 755	Relative	Underperform

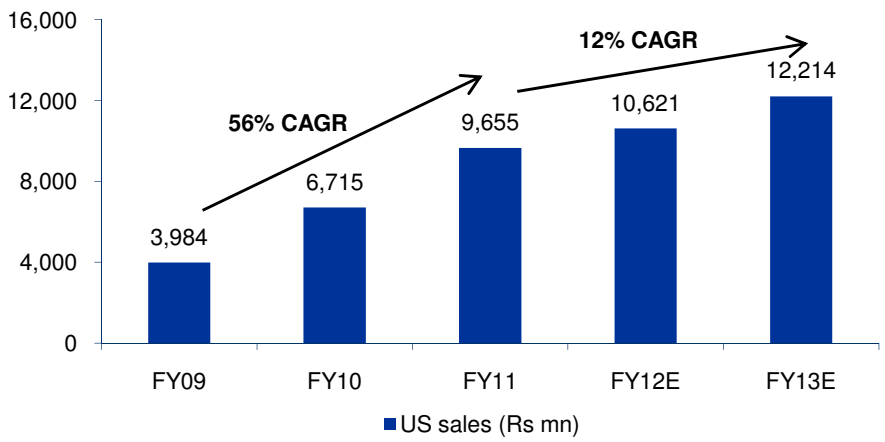
Business Overview

ANDA filings



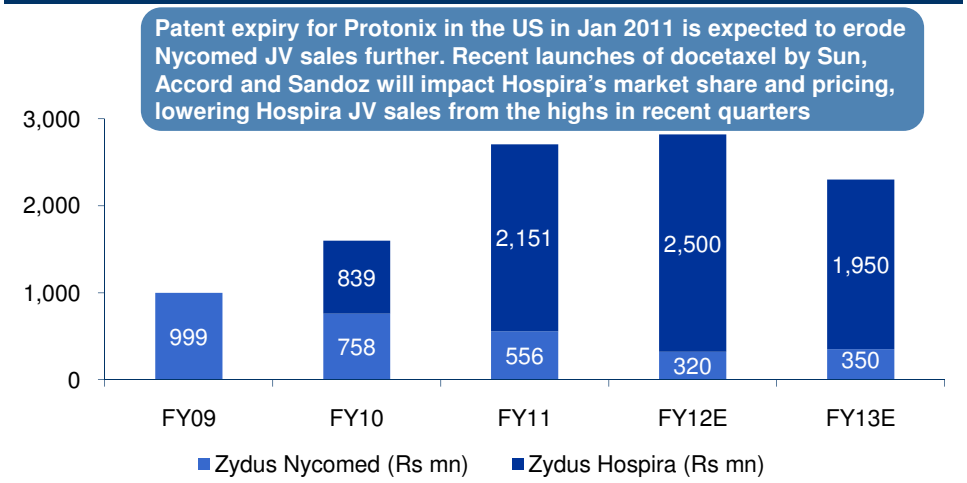
Source: Company data, Spark Capital Research

US sales to grow slower



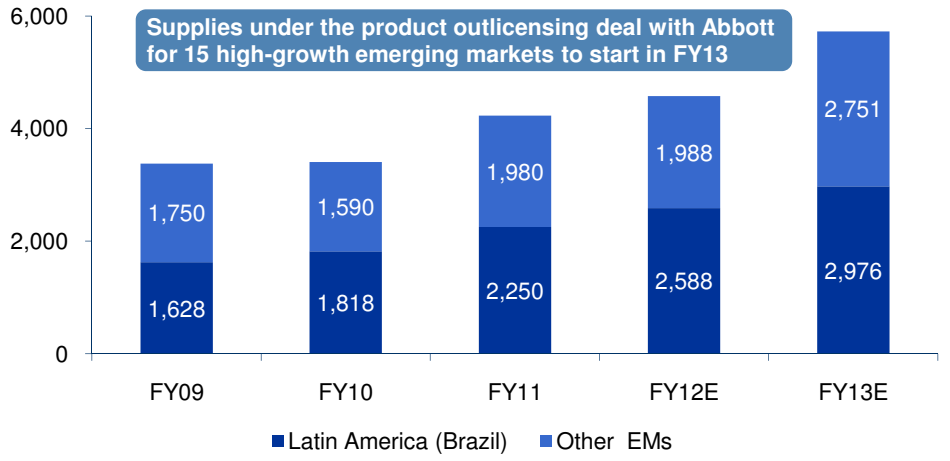
Source: Company data, Spark Capital Research

Nycomed and Hospira JVs



Source: Company data, Spark Capital Research

Abbott deal to start contributing from FY13



Source: Company data, Spark Capital Research

Cadila Healthcare

CMP	Rs. 833	Absolute	Reduce
Target	Rs. 755	Relative	Underperform

Financial Summary

Abridged Financial Statements (Consolidated)				
Rs. mn	FY10	FY11	FY12E	FY13E
Profit & Loss				
Net Sales	**35,742**	**44,647**	**50,050**	**57,617**
EBITDA	6,960	8,607	9,635	11,523
Depreciation	(1,339)	(1,269)	(1,458)	(1,693)
EBIT	5,621	7,338	8,177	9,831
Interest	(809)	(780)	(800)	(742)
Other Income	1,227	1,867	1,752	1,483
PBT	6,039	8,424	9,128	10,572
PAT	5,051	7,110	7,461	8,591
Adjusted PAT	**5,103**	**6,950**	**7,461**	**8,591**
Balance Sheet				
Net Worth	16,677	22,384	28,812	36,365
Deferred Tax	1,141	1,127	1,127	1,127
Total debt	10,905	10,973	11,464	9,329
Total Networth and liabilities	**28,723**	**34,484**	**41,402**	**46,820**
Gross Fixed assets	28,060	32,630	40,342	45,342
Net fixed assets	19,326	22,636	28,890	32,198
Investments	207	207	207	207
Inventories	7,504	8,119	9,102	10,478
Sundry Debtors	4,668	7,652	8,227	9,471
Cash and bank balances	2,507	2,952	2,659	2,925
Loans and advances	3,172	4,106	4,448	5,121
Current liabilities	8,661	11,188	12,130	13,578
Net current assets	9,190	11,641	12,305	14,416
Total assets	**28,723**	**34,484**	**41,402**	**46,820**
Cash Flows				
Cash flows from Operations	7,053	6,696	9,060	9,576
Cash flows from Investing	(3,815)	(4,530)	(7,712)	(5,000)
Cash flows from Financing	(3,248)	(1,721)	(1,641)	(4,310)

Key metrics				
	FY10	FY11	FY12E	FY13E
Growth ratios				
Net Sales	24.9%	24.9%	12.1%	15.1%
EBITDA	28.7%	23.7%	11.9%	19.6%
Adjusted PAT	49.5%	36.2%	7.4%	15.1%
Margin ratios				
EBITDA	19.5%	19.3%	19.3%	20.0%
Adjusted PAT	14.3%	15.6%	14.9%	14.9%
Performance ratios				
RoE	36.6%	36.9%	30.3%	27.6%
RoCE	23.7%	26.7%	23.6%	23.2%
RoA	19.4%	22.8%	20.4%	20.4%
Fixed asset turnover (x)	1.4	1.5	1.4	1.3
Total asset turnover (x)	1.3	1.4	1.3	1.3
Financial stability ratios				
Net Debt to Equity (x)	0.5	0.4	0.3	0.2
Current ratio (x)	2.1	2.0	2.0	2.1
Inventory and debtor days	124	129	126	126
Creditor days	92	101	97	95
Working capital days	32	28	29	31
Interest cover (x)	6.9	9.4	10.2	13.3
Valuation metrics				
Fully Diluted Shares (mn)	204.7	204.7	204.8	204.8
Market cap (Rs.mn)	170,607			
EPS (Rs.)	**24.9**	**33.9**	**36.4**	**41.9**
P/E (x)	**33.4**	**24.5**	**22.9**	**19.9**
EV (Rs.mn)	180,379			
EV/ EBITDA (x)	25.9	21.0	18.7	15.7
BV/ share (Rs.)	79.5	106.1	136.0	170.9
Price to BV (x)	10.5	7.9	6.1	4.9

Glenmark Pharma

Off the mark

CMP	Rs. 319	Absolute	Sell
Target	Rs. 271	Relative	Underperform

Among Indian pharma companies, Glenmark has the most successful track record of monetizing New Chemical Entity (NCE) research programs. Though we are positive on the potential of Glenmark's base business and NCE portfolio, the lack of clarity on the company's accounting policies and its stretched balance sheet and low return ratios concern us. We value Glenmark's base business at a multiple of 15x, a 25% discount to large caps, on account of these concerns. We ascribe a value of Rs. 50 per share for Glenmark's NCE pipeline and Rs. 8 per share for the Zetia para IV exclusivity opportunity to arrive at our target price of Rs.271. We initiate coverage with a Sell/Underperform rating

Investment rationale

- **US business to benefit from FY11 approvals:** Glenmark received 19 final ANDA approvals in FY11 (the highest for any Indian company). The opportunity to increase market share for many of these products and the potential sole FTF launches (of generic Malarone and generic Cutivate) positions Glenmark's US business on a strong footing for FY12. However, the higher base of FY11, which include generic Tarka (launched at-risk in Q1FY11, but withdrawn in Q4FY11 after an unfavorable jury verdict) and nitroglycerin (withdrawn from Q3FY11 following an FDA order) could moderate the potential YoY growth
- **Back-to-back outlicensing deals raises optimism on NCE portfolio:** Glenmark's outlicensing of GRC 15300 (in Q1 FY11) and GBR 500 (in Q1 FY12) to Sanofi for upfront payments of $20mn and $50mn, respectively, has raised the optimism regarding its NCE portfolio. Salix (Glenmark's partner) has completed phase III clinical trials in the US for Crofelemer, Glenmark's in-licensed molecule for HIV associated diarrhea. We attribute a value of Rs. 50 per share for Glenmark's NCE portfolio
- **Capitalization of costs continues to inflate EBITDA margins**: Historically, Glenmark has capitalized a significant part of its R&D expenses, resulting in high intangible assets on its balance sheet. In FY11, the company capitalized Rs. 2.3bn of internal development costs (vs. Rs. 1.4bn of expensed R&D costs). Net intangible assets increased by Rs. 2.7bn in FY11and currently net intangible assets (excluding goodwill) on the balance sheet is at Rs. 9.7bn, 47% of the company's net worth. In spite of the lower reported R&D expense, Glenmark reported a disappointing core EBITDA margin (excluding outlicensing income) of 17.6% in FY11 (Glenmark switched to IFRS in FY11, but failed to disclose IFRS figures for the previous year which makes comparisons difficult). Though management has guided to improved EBITDA margin of 22-23% for FY12, we prefer to wait for a few quarters to get comfortable on the profitability of Glenmark's base business
- **Balance sheet worries persist:** Glenmark's total debt stood at Rs. 21.1bn at the end of FY11. D/E ratio of 1.0x, though not alarming, is higher than most peers. Though, management has guided to reduction of debt using inflows from outlicensing deals, we believe capex requirements might leave no room for significant debt reduction. Though free cash flows in FY11 were boosted by reduction in receivables, we await more clarity to emerge on this front

Initiating coverage

Date	Sep 13, 2011
Market Data	
SENSEX	16502
Nifty	4947
Bloomberg	GNP IN
Shares o/s	270mn
Market Cap	Rs. 86bn
52-wk High-Low	Rs. 390-241
3m Avg. Daily Vol	Rs. 223mn
Index member	BSE100
Latest shareholding (%)	
Promoters	48.3
Institutions	38.1
Public	13.6

Stock performance (%)

	1m	3m	12m
GNP	-2%	3%	11%
Sensex	-2%	-10%	-14%
BSETHC	-2%	-6%	4%

Financial summary

Year	Sales (Rs. mn)	EBITDA (Rs. mn)	Adj PAT (Rs. mn)	Adj EPS (Rs.)	P/E (x)	ROE (%)
FY11	29,536	5,923	3,296	12.2	26.2	16.2
FY12E	35,468	8,464	4,792	17.7	18.0	21.0
FY13E	38,566	7,541	3,844	14.2	22.5	14.3

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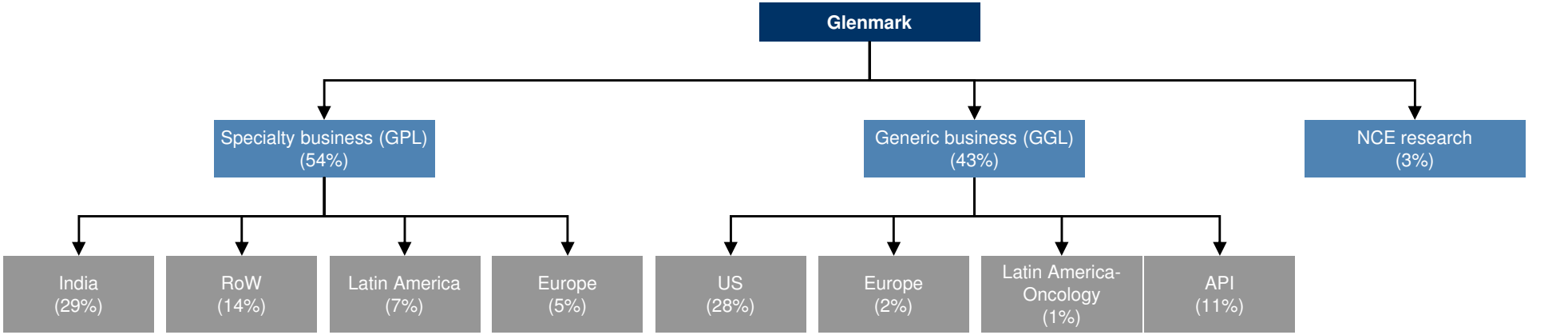
Glenmark Pharma

CMP	Rs. 319	Absolute	Sell
Target	Rs. 271	Relative	Underperform

Company Overview

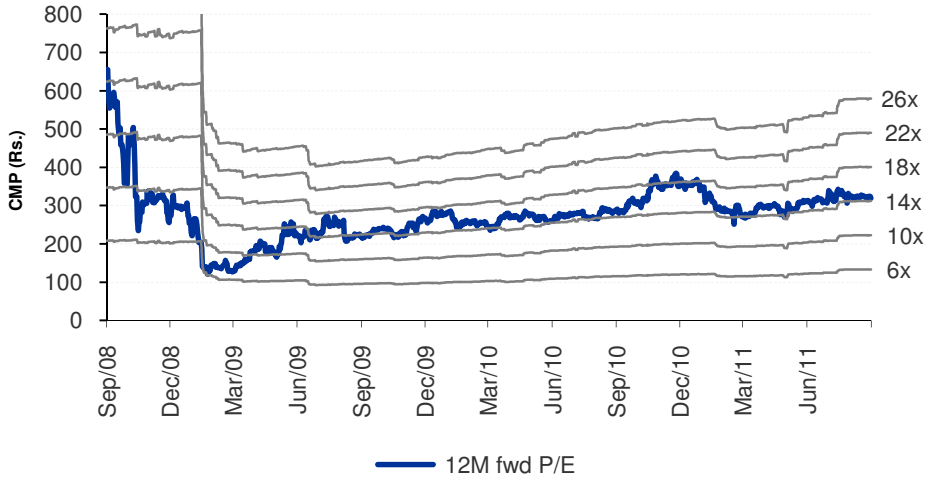
Sales breakup (FY11)



Source: Company, Spark Capital Research

We value Glenmark's base business at 15x FY13E EPS of Rs. 14.2. We use a 25% discount to sector large caps, given the less attractive growth profile, low return ratios and balance sheet and cash flow concerns. We also attach a value of Rs. 50 per share for Glenmark's NCE business and Rs. 8 per share for the Zetia sole FTF opportunity to arrive at our target price of Rs. 271, a 15% downside from current level.

P/E band



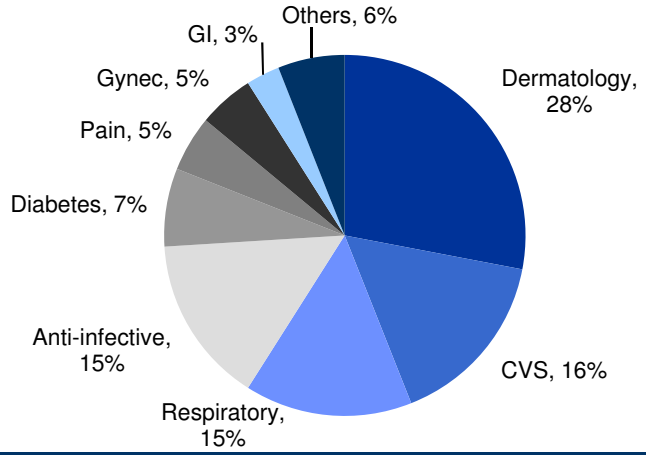
Source: Bloomberg, Spark Capital Research

Glenmark Pharma

CMP	Rs. 319	Absolute	Sell
Target	Rs. 271	Relative	Underperform

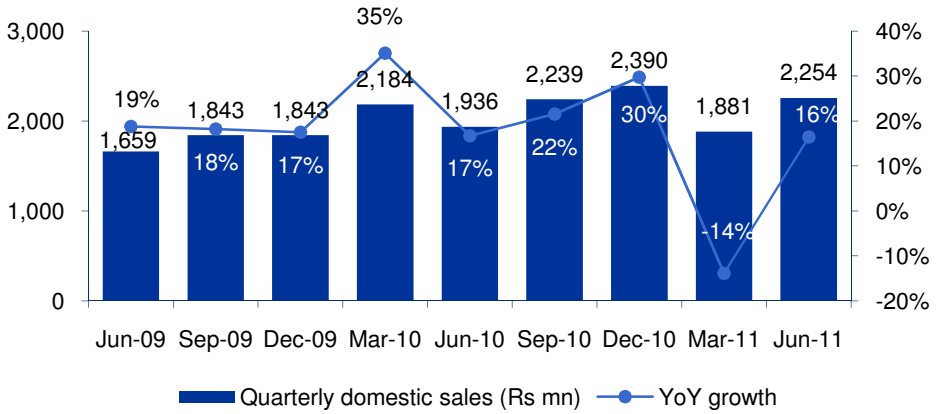
Business Overview

Domestic formulations – therapeutic breakup



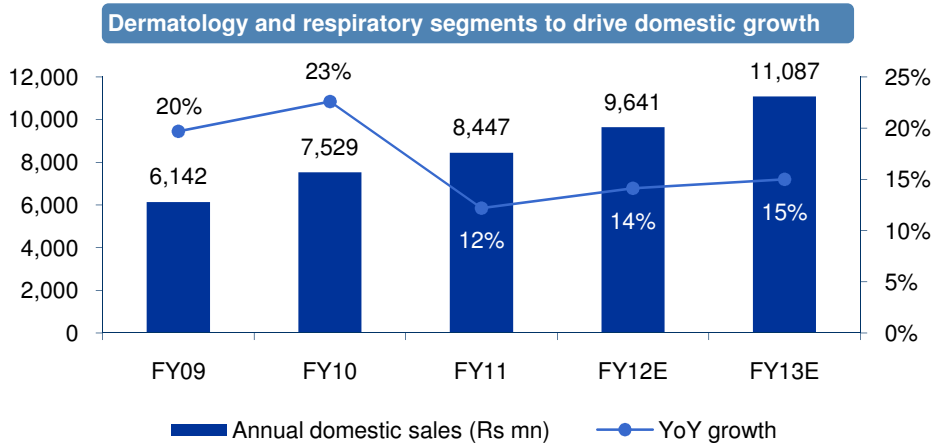
Source: Company data, Spark Capital Research

Domestic formulations – quarterly trend



Source: Company data, Spark Capital Research

Domestic formulations – annual sales



Source: Company data, Spark Capital Research

- We expect Glenmark's domestic sales to grow at a CAGR of 15% over the next 2 years driven by its strong dermatology portfolio (market share of 8.3%), and cardiology and respiratory segments. The company has recently strengthened its respiratory franchise with the launch of metered dose inhalers in India
- Glenmark received 19 final ANDA approvals in FY11 (the highest for any Indian company for the year). The opportunity to increase market share for many of these products and the potential sole FTF launches (of generic Malarone and generic Cutivate) positions Glenmark's US business on a strong footing for FY12
- However, the higher base of FY11 which include generic Tarka (launched at-risk in Q1FY11, but withdrawn in Q4FY11 after an unfavorable jury verdict) and nitroglycerin (withdrawn from Q3FY11 following an FDA order) could moderate the potential YoY growth

Glenmark Pharma

CMP	Rs. 319	Absolute	Sell
Target	Rs. 271	Relative	Underperform

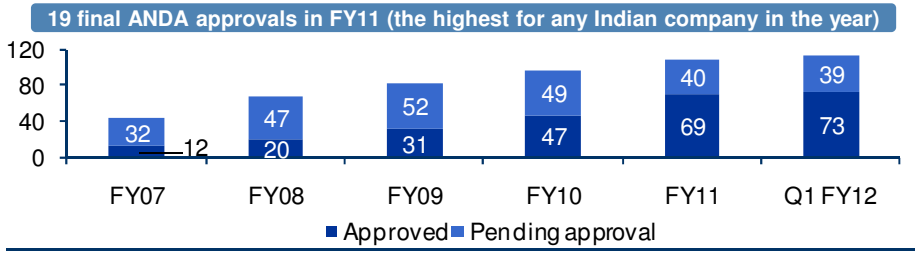
Business Overview

Key product approvals in the last 18 months

Date	Generic	Brand	Market* ($mn)	Indication
Aug-11	verapamil ER 120mg,180mg)	Isoptin SR	52	hypertension
Jul-11	ursodiol 250mg,500mg	Urso	60	primarily biliary cirrhosis
Jun-11	norgestimate + ethinyl estradiol	Ortho Tri-Cyclen	226	acne vulgaris in females
Jun-11	mupirocin oinment 2%	Bactroban	55	impetigo
May-11	fluticasone lotion 0.05%	Cutivate	48	dermatoses
Mar-11	norethindrone + ethinyl estradiol	Ovcon 35	30	oral contraceptive
Mar-11	levocetirizine	Xyzal	231	anti-allergy
Jan-11	atovaquone + proguanil 250/100	Malarone	64	malaria
Dec-10	sulphamethoxazole + trimethoprim	Bactrim	31	anti-infective
Dec-10	felodipine	Plendil	97	hypertension
Dec-10	oxycodone 5mg cap,100mg/5ml oral	-	13	pain
Oct-10	pramipexole dihydrochloride	Mirapex	520	Parkinson's disease
Aug-10	trospium chloride	Sanctura	25	bladder disorders
Aug-10	mometasone furoate 1%	Dulera	25	dermatoses
Aug-10	clotrimazole cream USP, 1%	Clotrimazole	26	topical anti-fungal
Jul-10	norethindrone 0.35mg	Micronor	43	hormonal
Jul-10	norethindrone acetate 5mg	Aygestin	27	hormonal
Jul-10	adapalene gel, 0.1%	Differin	84	acne
Apr-10	norethindrone 0.35mg	Nor-QD	43	hormonal
Mar-10	calcipotriene ointment 0.005%	Dovonex	93	psoriasis

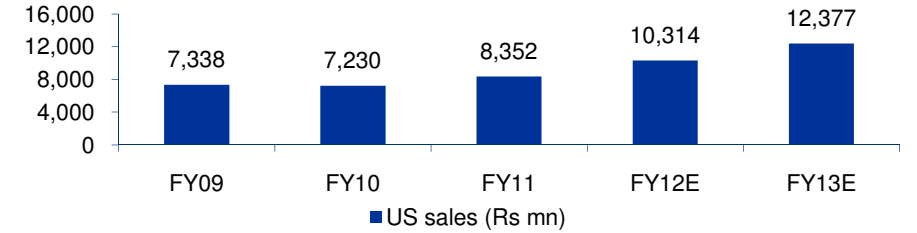
Source: Company data, Spark Capital Research

ANDA filings



Source: Company data, Spark Capital Research

Recent launches to drive US growth through FY13



Source: Company data, Spark Capital Research

Glenmark – sole FTF pipeline

Brand	Generic	Indication	Innovator	Market ($mn)	Comments
Zetia	ezetimibe	Hyper-cholesterolemia	Merck / Schering Plough	1,300	Glenmark was sued by Schering Plough in Mar 2007 for infringing the active ingredient patent ('721 patent which expires in Apr 2017). In May 2010 Glenmark settled with Merck (which acquired Schering Plough) for launch in Dec 2016
Cutivate	fluticasone lotion 0.05%	dermatoses	Nycomed	48	Glenmark sued in Dec 2008 for infringing '669 patent which expires in Oct 2019. In May 2011, Glenmark settled with Nycomed for launch in Mar 2012 under a royalty-bearing license
Malarone	atovaquone + proguanil 250/100	malaria	GSK	64	In Aug 2009, Glenmark sued on 3 patents all expiring in May 2014. Settled with GSK in Apr 2010 for launch in Q3 CY11
Locoid Lipocream	hydrocortisone butyrate	eczema	Triax, Astellas	38	In Nov 2010, Glenmark sued for infringing the '497 patent expiring in June 2014. Settled with Triax and Astellas in May 2011 for launch in Q4 CY13 under a royalty-bearing license
Tarka	trandolapril + verapamil hydrochloride	hypertension	Abbott	80	Sued in Dec 2007 on '244 patent (expiring in Feb 2015). In Q1 FY11, Glenmark launched 'at-risk' after a US District Court denied Sanofi and Abbott's motion for a preliminary injunction barring Glenmark from launching. However, in Jan 2011 a jury trial confirmed the validity of the patent and ordered Glenmark to pay $16mn in damages. Final verdict is awaited

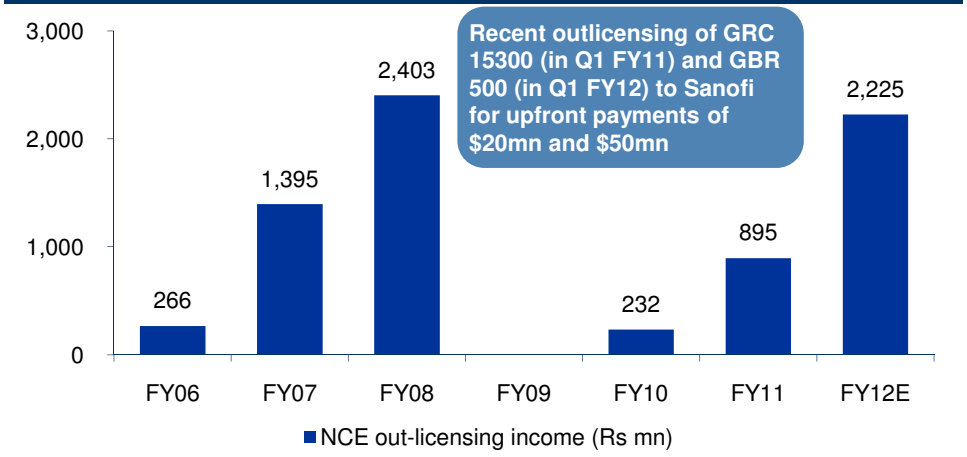
Source: Company data, Spark Capital Research

Glenmark Pharma

CMP	Rs. 319	Absolute	Sell
Target	Rs. 271	Relative	Underperform

Business Overview

NCE out-licensing revenues



- Though Glenmark has faced several setbacks in its NCE business in the past, recent outlicensing of GRC 15300 (in Q1 FY11) and GBR 500 (in Q1 FY12) to Sanofi for upfront payments of $20mn and $50mn, respectively, has raised the optimism regarding its NCE portfolio
- GBR 500 is the first biological compound developed and out-licensed by an Indian company
- Salix (Glenmark's partner) has completed phase III clinical trials in the US for Crofelemer, Glenmark's in-licensed molecule for HIV associated diarrhea
- We attribute a value of Rs.50 per share for Glenmark's NCE portfolio

Source: Company data, Spark Capital Research

Glenmark – NCE outlicensing track record

NCE	Class	Indication	Partner	Year	Milestones received ($mn)	Comments
Oglemilast / GRC 3886	PDE IV inhibitor	COPD and asthma	Forest Labs and Teijin Pharma	2004	40mn	First molecule out-licensed by Glenmark. Clinical trials abandoned in 2010 following disappointing results
Melogliptin / GRC 8200	DPP IV inhibitor	Type-II Diabetes	Merck KGaA	2006	31mn	In 2008, Merck returned the molecule to Glenmark citing reduced R&D focus on diabetes as reason. Glenmark has completed phase IIb trials for the drug and plans to start phase III trials
GRC 6211	TRPV1 antagonist	Osteoarthritis-related pain	Eli Lilly	2007	45mn	In 2008, Eli Lilly suspended further development of the drug following disappointing trial results
GRC 15300	TRPV3 antagonist	Neuropathic pain	Sanofi Aventis	2010	20mn	The first TRPV3 specific antagonist molecule to enter clinical trials. In July 2011, announced the successful completion of phase I studies in the UK. Phase IIa proof of concept study in neuropathic pain is planned to be initiated in Q3 FY12
GBR 500	VLA-2 (alpha2-beta1) integrin antagonist	Crohn's disease & other inflammatory disorders	Sanofi Aventis	2011	50mn	First-in-class therapeutic monoclonal antibody. Completed phase I dosing in the US. Plans to initiate clinical proof of concept studies in Crohn's Disease. Potential milestone payments of $613mn and double-digit royalty on sales and marketing rights in certain markets

Source: Company data, Spark Capital Research

Glenmark Pharma

CMP	Rs. 319	Absolute	Sell
Target	Rs. 271	Relative	Underperform

Financial Summary

Abridged Financial Statements (Consolidated)			
Rs. mn	FY11	FY12E	FY13E
Profit & Loss			
Net Sales	**29,536**	**35,468**	**38,566**
EBITDA	5,923	8,464	7,541
Depreciation	(947)	(1,206)	(1,346)
EBIT	4,976	7,258	6,195
Other Income	1,444	168	173
Interest	(1,605)	(1,735)	(1,791)
PBT	4,816	5,692	4,577
PAT	4,532	4,792	3,844
Adjusted PAT	**3,296**	**4,792**	**3,844**
Balance Sheet			
Net Worth	20,639	25,342	29,097
Deferred Tax	(1,081)	(1,081)	(1,081)
Total debt	21,116	21,500	22,500
Total Networth and liabilities	**40,674**	**45,761**	**50,516**
Gross Fixed assets	25,291	29,291	33,291
Net fixed assets	22,123	24,917	27,571
Investments	181	181	181
Inventories	8,070	9,367	10,828
Sundry Debtors	11,308	12,730	14,191
Cash and bank balances	1,986	1,500	1,250
Loans and advances	4,751	5,706	6,203
Current liabilities	7,746	8,640	9,709
Net current assets	18,370	20,663	22,763
Total assets	**40,674**	**45,761**	**50,516**
Cash Flows			
Cash flows from Operations	9,303	5,910	5,140
Cash flows from Investing	(3,670)	(4,954)	(4,498)
Cash flows from Financing	(4,356)	(1,442)	(892)

Key metrics			
	FY11	FY12E	FY13E
Growth ratios			
Net Sales	17.6%	20.1%	8.7%
EBITDA		42.9%	-10.9%
Adjusted PAT		45.4%	-19.8%
Margin ratios			
EBITDA	20.1%	23.9%	19.6%
Adjusted PAT	11.2%	13.5%	10.0%
Performance ratios			
RoE	16.2%	21.0%	14.3%
RoCE	11.9%	14.3%	11.1%
RoA	8.2%	11.2%	8.1%
Fixed asset turnover (x)	1.2	1.3	1.2
Total asset turnover (x)	0.7	0.8	0.8
Financial stability ratios			
Net Debt to Equity (x)	0.9	0.8	0.7
Current ratio (x)	3.4	3.4	3.3
Inventory and debtor days	247	243	238
Creditor days	130	130	130
Working capital days	117	113	108
Interest cover (x)	3.1	4.2	3.5
Valuation metrics			
Fully Diluted Shares (mn)	270.5	270.7	270.7
Market cap (Rs.mn)	86,337		
EPS (Rs.)	**12.2**	**17.7**	**14.2**
P/E (x)	**26.2**	**18.0**	**22.5**
EV (Rs.mn)	105,734		
EV/ EBITDA (x)	17.9	12.5	14.0
BV/ share (Rs.)	75.3	92.4	106.1
Price to BV (x)	4.2	3.5	3.0

IPCA Laboratories

Power brands to power growth

CMP	Rs. 309	Absolute	Add
Target	Rs. 344	Relative	Outperform

Ipca's focus on brand building will continue to drive its domestic formulations business. The company has strengthened its sales force by adding ~1,000 reps in FY11, the positive impact of which will emerge over the next 12-18 months. The company is one of the four WHO prequalified suppliers under AMFm (a $250mn opportunity) of artemether+lumefantrine (AL) and is awaiting prequalification for artesunate-amodiaquine (AS-AQ). Ipca's US sales has the potential to scale-up to Rs. 3-4bn on receiving approval for the Indore facility, which we expect by the end of FY12. We value the stock using a target multiple of 13x, the mid-point of its recent trading range of 12-14x. We refrain from using a higher multiple, in spite of the company's strong expected earnings growth (20% EPS CAGR in FY11-FY13E), on account of the uncertainties related to FDA approval for its Indore facility and the high proportion of tender-driven sales. We initiate coverage with a Add/Outperform rating and a target price of Rs.344

Investment rationale

- **Brand building to drive domestic growth:** Ipca's strategy in the domestic market is based on growing its key brands. The company's leading brands such as Lariago, HCQS, Rapither, Zerodol P and Perinorm are leaders in their respective segments and have constantly improved their market share. Ipca currently has ~150 brands in the domestic market, significantly lower compared to peers in our coverage universe, allowing it to implement a brand focused strategy. In line with this strategy, the company strengthened its sales force by adding ~1,000 reps in FY11, the positive impact of which will emerge over the next 12-18 months. The company's efforts to strengthen its chronic portfolio by launching new segments (nephrology and urology segments started operations in FY11) and new products (25 products launched in FY11), are key growth drivers in our view
- **Supplies under AMFm to boost generic sales:** Ipca started supplies under the Affordable Medicines Facility - malaria (AMFm) program in Q2 FY11, generating sales of ~Rs. 1.2bn in FY11. Ipca is one of the four WHO prequalified suppliers of artemether+lumefantrine (AL). Other prequalified suppliers are Cipla, Ajanta and Novartis. The total AMFm opportunity is estimated at ~$250mn, of which AL constitutes ~90%. The remaining 10% is constituted by artesunate-amodiaquine (AS-AQ), for which SanofiAventis is currently the only WHO prequalified supplier. Ipca is awaiting prequalification for AS-AQ which will further boost its institutional sales. According to the company, profit margins for AMFm sales is above company average
- **FDA approval for Indore facility will be key catalyst:** Ipca's Indore SEZ manufacturing facility, commissioned in Dec 2008, is still awaiting FDA inspection and approval. The first ANDA from the facility was filed over 2 years ago. The facility was recently approved by the UK-MHRA and management expects FDA approval by end of FY12. We believe Ipca's US business has the potential to scale-up to Rs. 3-4bn on receiving approval for the Indore facility. Margins have been impacted in recent quarters by fixed costs at this facility and we expect this to reverse on the facility receiving approval

Financial summary

Year	Sales (Rs. mn)	EBITDA (Rs. mn)	Adj PAT (Rs. mn)	Adj EPS (Rs.)	P/E (x)	ROE (%)
FY11E	18,825	3,598	2,294	18.3	16.9	23.9
FY12E	22,201	4,240	2,717	21.6	14.3	23.3
FY13E	25,927	5,133	3,331	26.5	11.7	23.4

Initiating coverage

Date	Sep 13, 2011
Market Data	
SENSEX	16502
Nifty	4947
Bloomberg	IPCA IN
Shares o/s	126mn
Market Cap	Rs. 39bn
52-wk High-Low	Rs. 352-255
3m Avg. Daily Vol	Rs. 38mn
Index member	BSETHC
Latest shareholding (%)	
Promoters	46.1
Institutions	32.3
Public	21.7

Stock performance (%)

	1m	3m	12m
IPCA	-3%	-11%	3%
Sensex	-2%	-10%	-14%
BSETHC	-2%	-6%	4%

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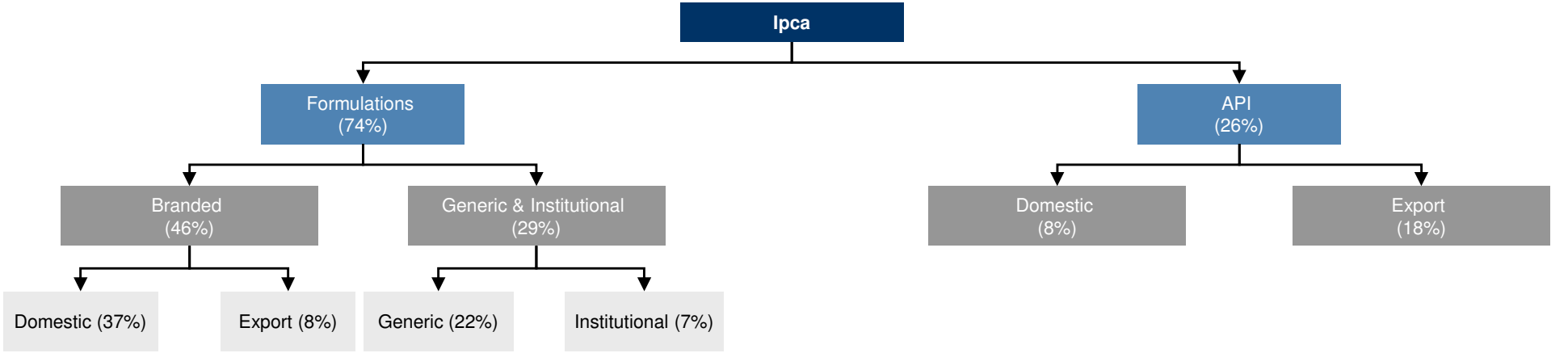
IPCA Laboratories

CMP	Rs. 309	Absolute	Add
Target	Rs. 344	Relative	Outperform

Company Overview

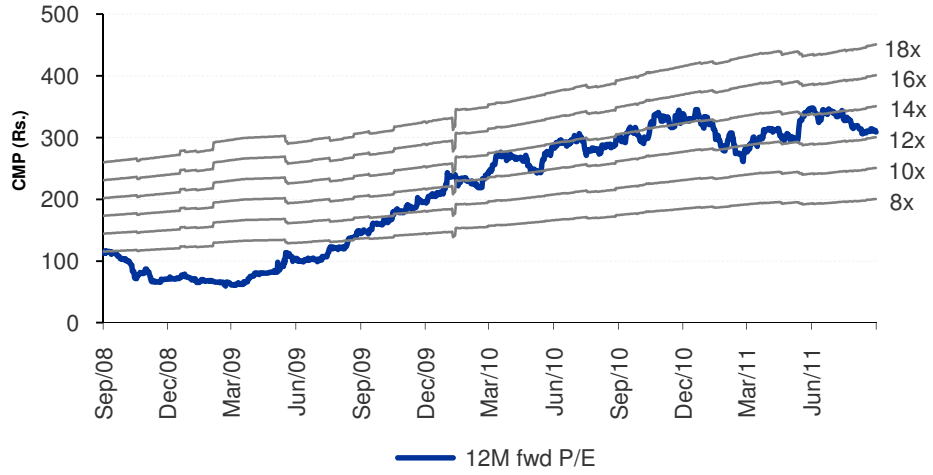
Sales breakup (FY11)



Source: Company, Spark Capital Research

Ipca has traded mostly in the 12-14x (1-year forward earnings) range over the last 12-18 months. We value the stock using a target multiple of 13x, the mid-point of this range. We refrain from using a higher multiple, in spite of Ipca's strong expected earnings growth (20% EPS CAGR in FY11-FY13E), on account of the uncertainties related to FDA approval for its Indore facility and the high proportion of tender-driven sales. Our target price of Rs. 344 implies a 11% upside from current price.

Stock performance/PE band



Source: Bloomberg, Spark Capital Research

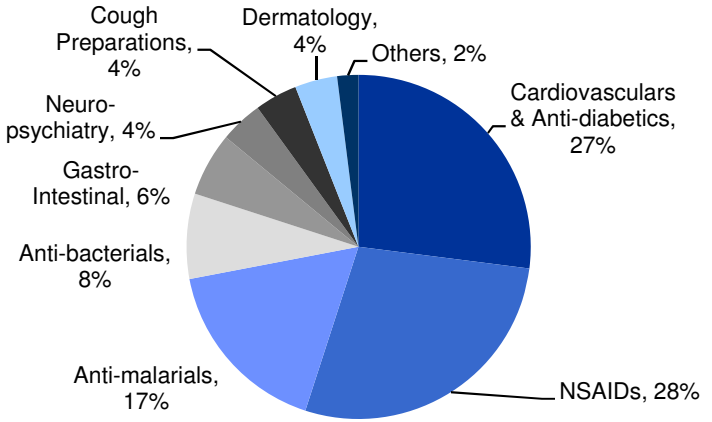
IPCA Laboratories

CMP	Rs. 309	Absolute	Add
Target	Rs. 344	Relative	Outperform

Business Overview

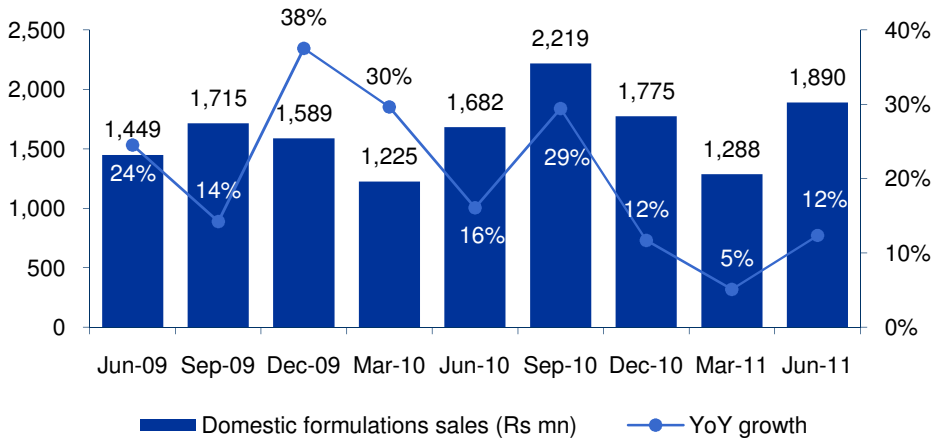
- Ipca's domestic strategy is based on growing its key brands. The company has 5 brands in the top-300 pharma brands in the country. Leading brands include Lariago, HCQS, Rapither, Zerodol P and Perinorm
- Ipca currently has ~150 brands in the domestic market, significantly lower compared to peers. The company has made ~55 launches in the last 5 years, lower compared to peers. However, this seems to be changing as the company launches products to strengthen its chronic portfolio
- Ipca's currently has a ~4,200 member sales force. The company added 600 people to its sales force in FY11, which has impacted its sales force productivity (<Rs. 2mn per MR for FY11). We expect this to correct over the next 12-18 months as the newly recruited reps becomes more productive
- Ipca's other branded markets staged a comeback in FY11, after declining sharply in FY10 (mainly due to product re-registration issues in Russia) and we expect the renewed momentum to continue

Domestic formulations – therapeutic breakup (FY11)



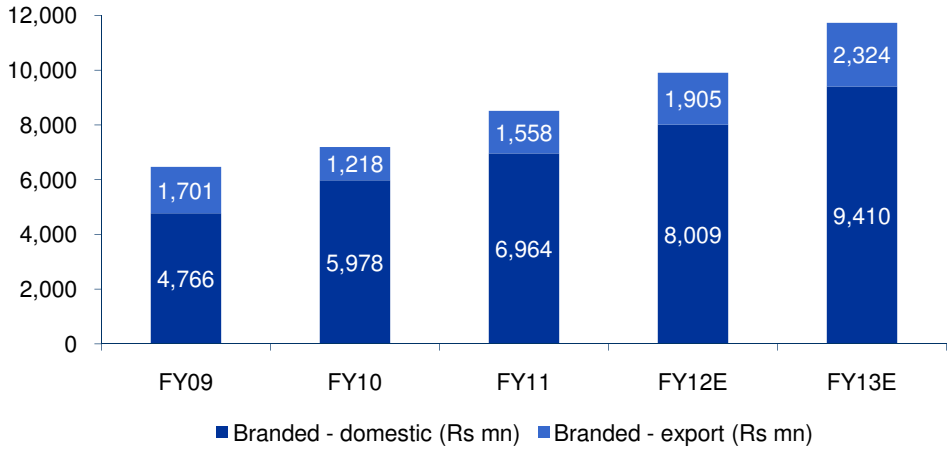
Source: Company data, Spark Capital Research

Domestic formulations – quarterly trend



Source: Company data, Spark Capital Research

Branded formulations – annual sales



Source: Company data, Spark Capital Research

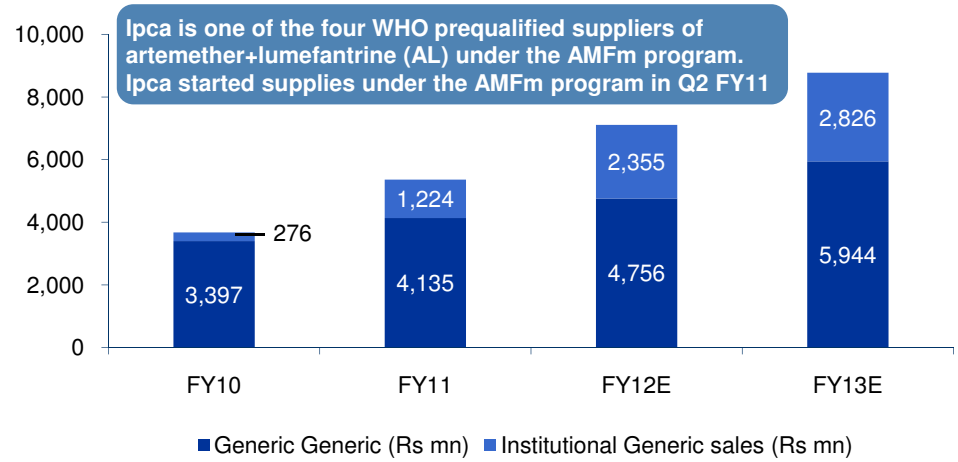
IPCA Laboratories

CMP	Rs. 309	Absolute	Add
Target	Rs. 344	Relative	Outperform

Business Overview

- ~70% of generic sales is currently from the UK with the US, Canada, Australia and New Zealand contributing the remainder
- In the US, Ipca operates under profit-sharing relationships with partners (Ranbaxy and Heritage) who handle the marketing. Ipca has 12 ANDAs approved from its Silvassa facility generating sales of Rs. 1.1bn in FY11
- Ipca's Indore SEZ manufacturing facility, commissioned in Dec 2008, is still awaiting FDA inspection and approval. The first ANDA from the facility was filed over 2 years ago. The facility was recently approved by the UK-MHRA and management expects FDA approval by end of FY12. We believe Ipca's US business has the potential to scale-up to Rs. 3-4bn on receiving approval for the Indore facility
- Fixed costs at the Indore facility has pressured margins in recent quarters

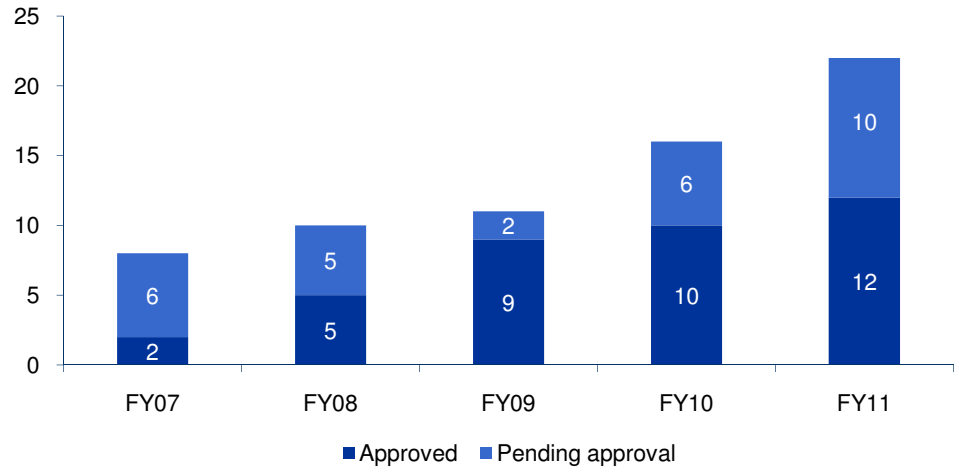
Generic sales



Source: Company data, Spark Capital Research

- Supply of anti-malarial drugs under the Affordable Medicines Facility - malaria (AMFm) program constitutes >90% of Ipca's institutional generic sales. The AMFm is a financing mechanism designed to expand access to Artemisinin-based Combination Therapies (ACTs). It is managed by the Global Fund and supported financially by the Bill & Melinda Gates Foundation, the United Kingdom Government, UNITAID and the Global Fund
- Ipca is one of the four WHO prequalified suppliers of artemether+lumefantrine (AL). Other prequalified suppliers are Cipla, Ajanta and Novartis. Ipca started supplies under the AMFm program in Q2 FY11, generating sales of ~Rs. 1.2bn in FY11. The total AMFm opportunity is estimated at ~$250mn, of which AL constitutes ~90%. The remaining 10% is constituted by artesunate-amodiaquine (AS-AQ), for which Sanofi Aventis is currently the only WHO prequalified supplier
- Ipca is awaiting prequalification for AS-AQ which will further boost institutional sales. According to the company, profit margins for AMFm sales is above company average

ANDA filings



Source: Company data, Spark Capital Research

IPCA Laboratories

CMP	Rs. 309	Absolute	Add
Target	Rs. 344	Relative	Outperform

Financial Summary

Abridged Financial Statements (Consolidated)				
Rs. mn	FY10	FY11	FY12E	FY13E
Profit & Loss				
Net Sales	**15,596**	**18,825**	**22,201**	**25,927**
EBITDA	3,265	3,598	4,240	5,133
Depreciation	(467)	(558)	(659)	(762)
EBIT	2,797	3,040	3,581	4,371
Other Income	195	681	270	304
Interest	(329)	(314)	(374)	(411)
PBT	2,663	3,407	3,476	4,264
PAT	2,054	2,628	2,717	3,331
Adjusted PAT	**2,006**	**2,294**	**2,717**	**3,331**
Balance Sheet				
Net Worth	8,643	10,509	12,799	15,679
Deferred Tax	793	807	807	807
Total debt	4,545	5,308	6,442	6,466
Total Networth and liabilities	**13,981**	**16,625**	**20,049**	**22,952**
Gross Fixed assets	9,195	11,016	13,516	15,516
Net fixed assets	6,761	8,124	9,964	11,202
Investments	325	408	408	408
Inventories	3,802	4,664	5,353	6,109
Sundry Debtors	3,880	4,637	5,468	6,386
Cash and bank balances	108	104	403	644
Loans and advances	1,201	1,182	1,182	1,182
Current liabilities	2,097	2,493	2,729	2,978
Net current assets	6,895	8,093	9,676	11,341
Total assets	**13,981**	**16,625**	**20,049**	**22,952**
Cash Flows				
Cash flows from Operations	1,913	2,115	2,383	2,963
Cash flows from Investing	(1,172)	(1,981)	(2,500)	(2,000)
Cash flows from Financing	(740)	(138)	416	(722)

Key metrics				
	FY10	FY11	FY12E	FY13E
Growth ratios				
Net Sales	21.5%	20.7%	17.9%	16.8%
EBITDA	27.3%	10.2%	17.9%	21.1%
Adjusted PAT	22.9%	14.4%	18.4%	22.6%
Margin ratios				
EBITDA	20.9%	19.1%	19.1%	19.8%
Adjusted PAT	12.9%	12.2%	12.2%	12.8%
Performance ratios				
RoE	26.8%	23.9%	23.3%	23.4%
RoCE	18.7%	18.0%	17.1%	17.6%
RoA	15.7%	15.0%	14.8%	15.5%
Fixed asset turnover (x)	1.8	1.9	1.8	1.8
Total asset turnover (x)	1.2	1.2	1.2	1.2
Financial stability ratios				
Net Debt to Equity (x)	0.5	0.5	0.5	0.4
Current ratio (x)	4.3	4.2	4.5	4.8
Inventory and debtor days	180	180	178	176
Creditor days	43	39	39	39
Working capital days	137	142	139	137
Interest cover (x)	8.5	9.7	9.6	10.6
Valuation metrics				
Fully Diluted Shares (mn)	125.1	125.5	125.9	125.9
Market cap (Rs.mn)	38,856			
EPS (Rs.)	**16.0**	**18.3**	**21.6**	**26.5**
P/E (x)	**19.3**	**16.9**	**14.3**	**11.7**
EV (Rs.mn)	44,888			
EV/ EBITDA (x)	13.7	12.5	10.6	8.7
BV/ share (Rs.)	69.1	83.8	101.8	124.6
Price to BV (x)	4.5	3.7	3.0	2.5

LUPIN

Bellwether in the making

CMP	Rs. 465	Absolute	Buy
Target	Rs. 548	Relative	Outperform

Lupin's US generic business is poised for strong near-term growth on the back of multiple limited-competition opportunities such as gGeodon, gFortamet, gTricor, gCombivir and oral contraceptives. The company's domestic formulations segment is also expected to outperform driven by increasing focus on chronic therapies. Lupin is also set to benefit from the expected rise in generic penetration in Japan. Among Lupin's other markets, South Africa, Philippines and Australia offer significant growth potential. We are in line with consensus on FY12E and FY13E earnings, but believe Lupin's long-term growth visibility is not captured in its current trading multiples. We value the stock at 20x its FY13E EPS to arrive at our target price of Rs. 548, implying an upside of 18% from current levels. We initiate coverage with a Buy/Outperform rating

Investment rationale

- **Strong pipeline provides visibility:** Lupin is currently the 5th largest (and the largest Indian) player in the US generic market (in terms of prescriptions). Lupin's near-term pipeline (refer page 55 for details) includes multiple limited-competition opportunities such as gGeodon, gFortamet, gTricor, gCombivir and oral contraceptives (4-5 player market, Lupin has made ~25 filings, approvals expected from FY13). Further, we expect Lupin to garner decent market share in some of the more commoditized shared FTF opportunities such as gLotrel (higher strengths), gLevaquin, gCymbalta and gLexapro. We expect Lupin's ability to gain market share for highly generized products (market leader in 14 out of ~30 products launched) and robust pipeline to drive strong outperformance in the near-term
- **Domestic business showing strong momentum:** Lupin has transitioned its portfolio from anti-infective and anti-TB drugs to therapies for lifestyle-related and chronic diseases over the last few years. Lupin's domestic formulations segment has consistently outpaced the industry in terms of growth in most therapeutic areas. Through a combination of in-licensed product launches (11 products in-licensed in the last two years), entry into new segments such as biologics and market share gains in recently entered segments such as gynecology and oncology, we expect Lupin to continue its domestic growth story
- **Japan, emerging markets diversify revenue base:** Lupin, through its subsidiary Kyowa, is the largest Indian player in the high-potential Japanese generic market. The Japanese government has set a near-term target to increase generic penetration in the country to 30% (by volume) by Mar 2013 (generic penetration is 22% currently compared to 78% in the US). Among Lupin's other markets, South Africa, Philippines and Australia offer significant potential
- **NDDS capabilities opens new opportunities for the long-term:** In FY10, Lupin entered into a partnership with Salix to develop an extended-release version of rifaximin using Lupin's proprietary bioadhesive technology. Recently, the company announced a tie up with Medicis to develop novel formulations using Lupin's technology (received upfront payment of $20mn). As new drug discovery becomes increasingly challenging and global pharma companies step up their efforts to improve existing drugs, we believe Lupin's capabilities in NDDS could lead to more such partnering opportunities

Financial summary

Year	Sales (Rs. mn)	EBITDA (Rs. mn)	Adj PAT (Rs. mn)	Adj EPS (Rs.)	P/E (x)	ROE (%)
FY11	56,478	10,069	8,515	19.0	24.5	29.2
FY12E	65,520	11,400	9,840	21.9	21.2	26.6
FY13E	77,136	14,039	12,287	27.4	17.0	26.3

Initiating coverage

Date	Sep 13, 2011
Market Data	
SENSEX	16502
Nifty	4947
Bloomberg	LPC IN
Shares o/s	446mn
Market Cap	Rs. 208bn
52-wk High-Low	Rs. 520-362
3m Avg. Daily Vol	Rs. 469mn
Index member	BSE100
Latest shareholding (%)	
Promoters	47.0
Institutions	42.8
Public	10.3

Stock performance (%)

	1m	3m	12m
LPC	3%	7%	24%
Sensex	-2%	-10%	-14%
BSETHC	-2%	-6%	4%

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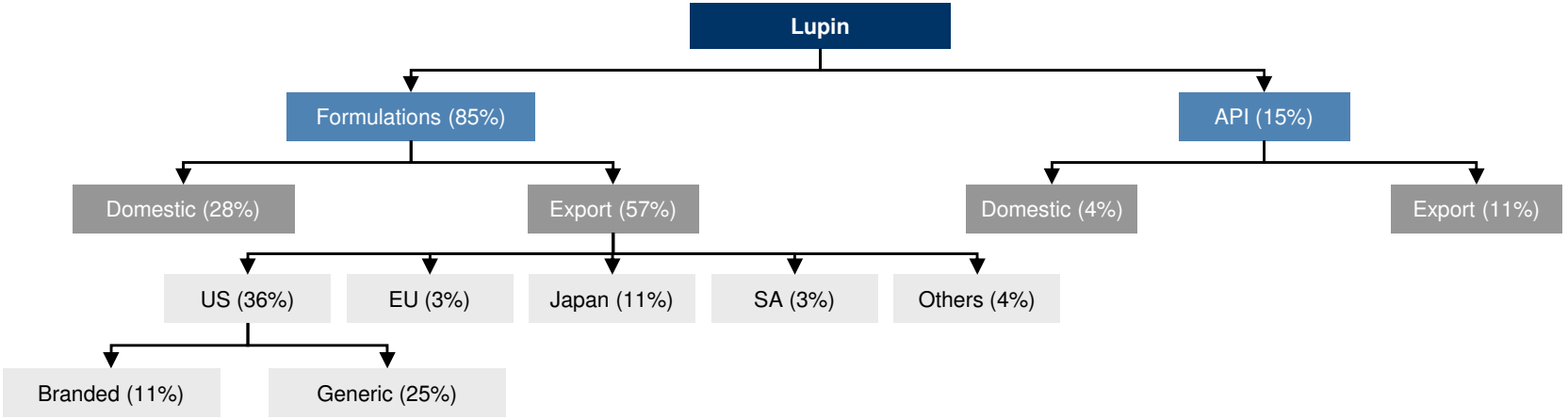
LUPIN

CMP	Rs. 465	Absolute	Buy
Target	Rs. 548	Relative	Outperform

Company Overview

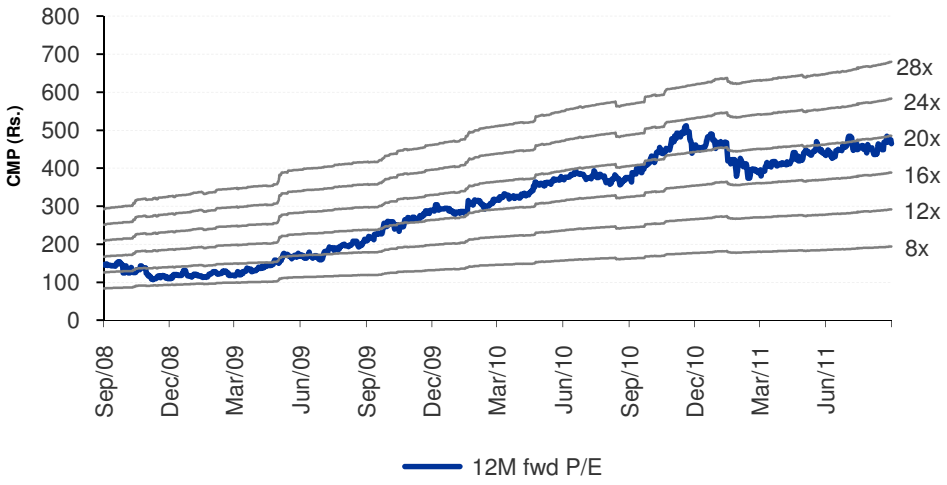
Sales breakup (FY11)



Source: Company, Spark Capital Research

At CMP of Rs. 465, Lupin trades at 21.2x and 17.0x FY12E and FY13E earnings, respectively. We are in line with consensus on FY12E and FY13E earnings, but believe Lupin's long-term growth visibility is not captured in its current trading multiples. We value the stock at 20x its FY13E EPS to arrive at our target price of Rs. 548, implying an upside of 18% from current levels.

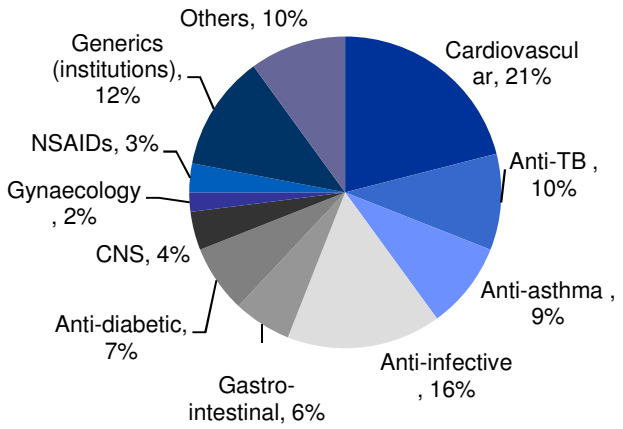
P/E band



Source: Bloomberg, Spark Capital Research

Business Overview

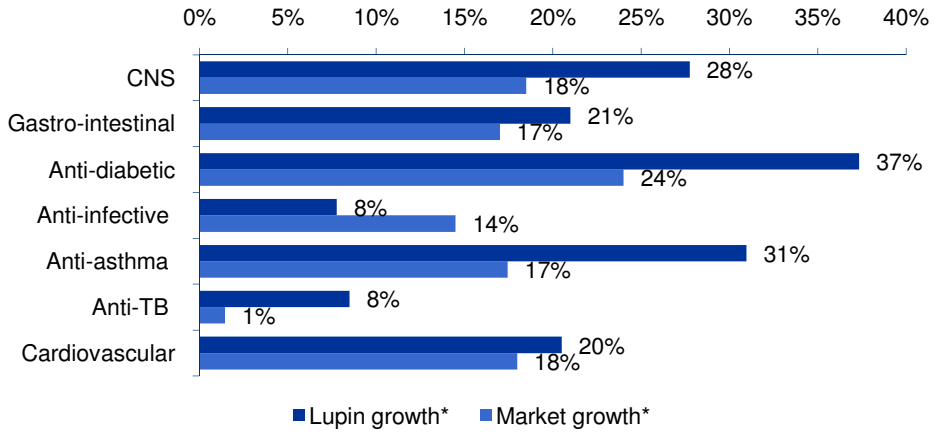
Domestic formulations – therapeutic breakup (FY11)



In recent years, Lupin has transitioned its portfolio from anti-infective and anti-TB drugs to therapies for lifestyle-related and chronic diseases. For instance, the share of anti-TB drugs has come down from 26% in FY06 to 10% in FY11

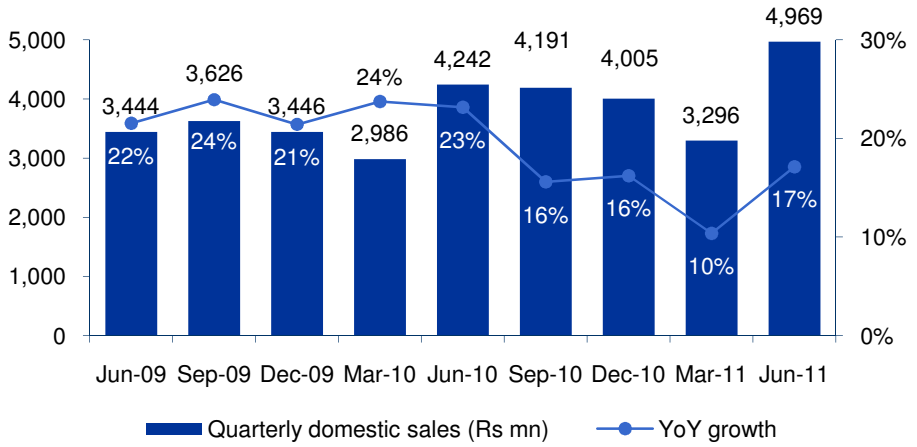
Source: Company data, Spark Capital Research

Above-industry growth in key therapeutic segments



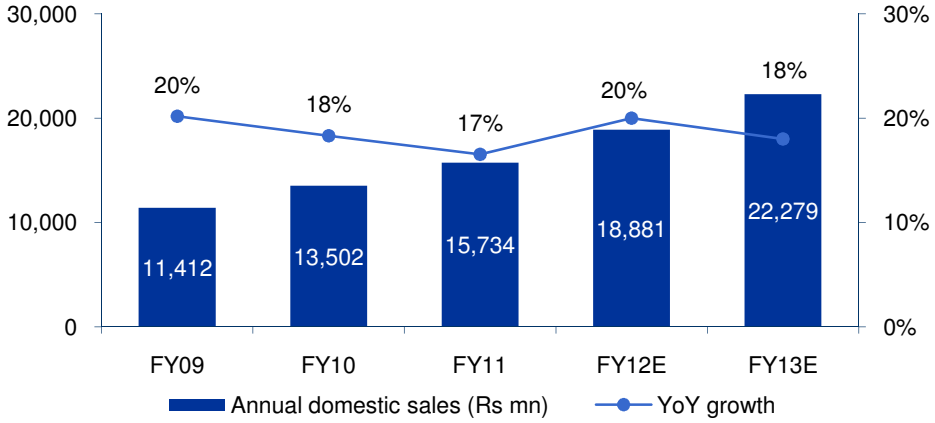
*Source: Company data, Spark Capital Research; *FY09 - FY11 CAGR*

Domestic formulations – quarterly trend



Source: Company data, Spark Capital Research

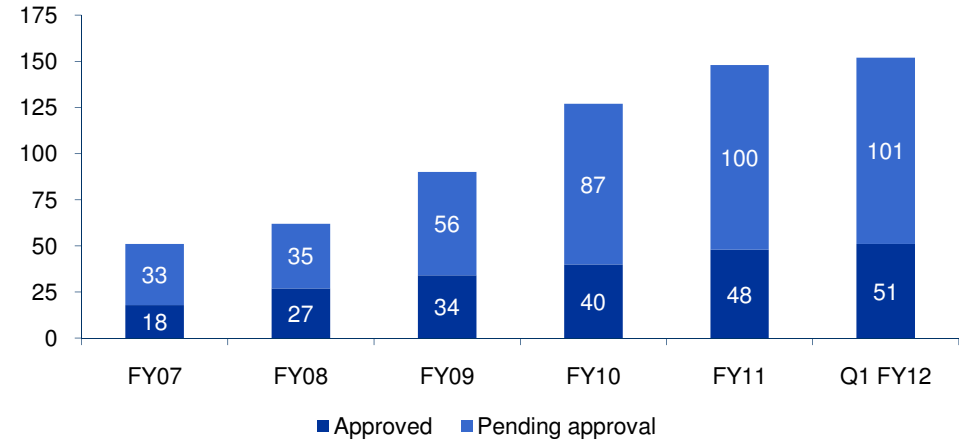
Domestic formulations – annual sales



Source: Company data, Spark Capital Research

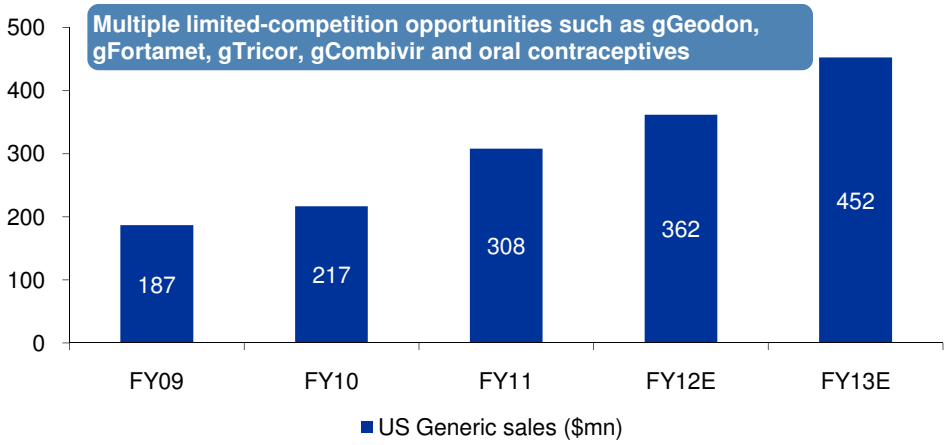
Business Overview

High number of ANDAs pending approval



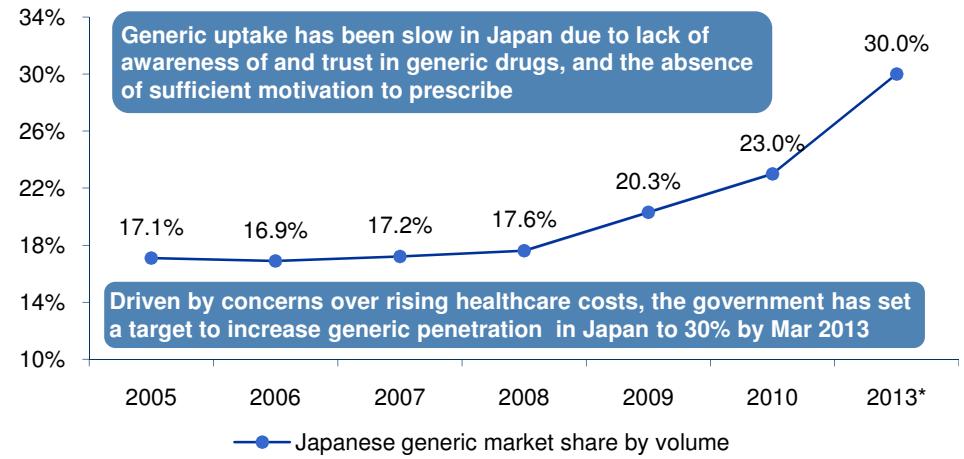
Source: Company data, Spark Capital Research

High value para IV launches to drive US generics growth…



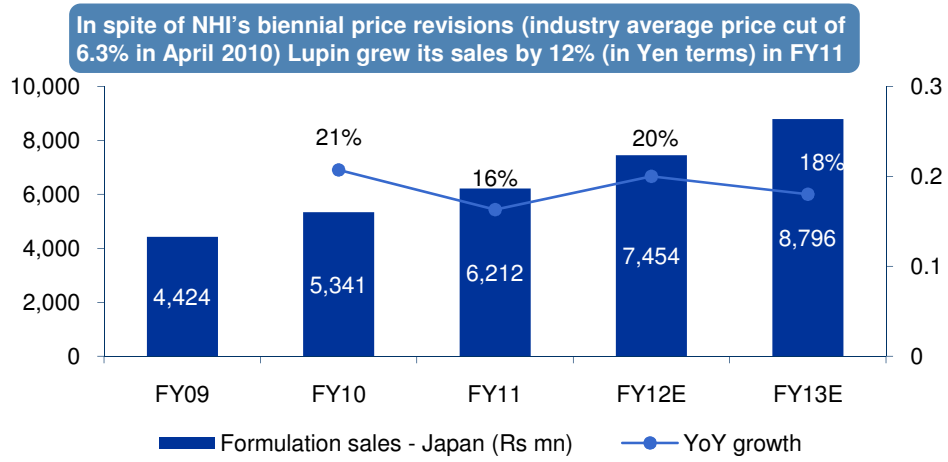
Source: Company data, Spark Capital Research

Generic penetration to rise in Japan…



Source: Spark Capital Research

…driving Lupin's sales in Japan



Source: Company data, Spark Capital Research

Near-term limited-competition opportunities for Lupin

Generic	Brand	Opportunity ($mn)	Innovator	Comments
ziprasidone	Geodon	1,027	Pfizer	Pfizer's compound patent expires in Mar 2012. 3 players (Lupin, Dr. Reddy's and Sandoz) with tentative approvals
metformin hydrochloride ER	Fortamet	83	Andrx	Lupin is sole FTF. Lupin sued by Andrx/Shionogi in Jan 2009. Mylan, the only other known ANDA filer was sued in Jan 2010. The two litigated patents ('859 and '866) expire in Mar 2018 and Mar 2021, respectively. Lupin received final approval in June 2011. 30 month stay expired in July 2011 (Lupin can launch at-risk)
ciprofloxacin suspension	Cipro DS	-	Bayer	Lupin is sole FTF (filed para IV in Oct 2009). Lupin sued by Bayer over '784 patent (expires in June 2015) in Feb 2010. Lupin hasn't challenged the only remaining patent ('347) which expires in July 2013 post-which we expect Lupin to launch. No other known filer
fenofibrate (48mg and 145mg)	Tricor	1,500	Abbott	Teva is FTF on the 145mg version and settled with Abbott in Nov 2009 (according to Abbott, "generic competition could begin as early as March 2011 but is not expected until July 2012"). Teva has not yet received approval (likely forfeiture of FTF status). Other filers for the two doses are Biovail (likely FTF on the 48mg version), Ranbaxy, Lupin, and Impax (all except Impax have settled, allowing earliest launch in June 2012)
lamivudine + zidovudine	Combivir	315	GSK	Teva FTF. Settled with GSK in May 2010. Launch expected in Q4 CY11. Lupin sued in Sep 2008 on patent '021 which expires in May 2012. We expect Lupin to launch post Teva's 180 day exclusivity, assuming FDA approval
niacin	Niaspan	1,100	Abbott	Teva is FTF. Settled with Abbott for launch in Sep 2013. Other ANDA filers include Sandoz, Sun, Lupin and Impax. We expect Lupin and others to settle to launch post Teva's 6-month exclusivity
Oral Contraceptives				
drospirenone + ethinyl estradiol (3mg/0.02mg)	Yaz	~750	Bayer	Lupin sued by Bayer in July 2010. Litigated patents expire in Jan 2014. Teva (June 2010) and Sandoz (May 2011) have launched. Other ANDA filers are Watson, Mylan and Sun. Lupin can launch after 30 month stay expires in Jan 2013 (assuming approval)
drospirenone + ethinyl estradiol (3mg/0.03mg)	Yasmin	~350	Bayer	Teva (July 2008), Watson (Sep 2010) and Sandoz (June 2011) have launched. Lupin could launch at-risk on receiving approval (we believe 30 month stay expires mid 2012) or after the expiry of '652 patent in Oct 2013. Other filers are Sun and Famycare/Mylan
ethinyl estradiol + levonorgestrel (0.03mg/0.15mg)	Seasonale	~90	Teva	Watson, Sandoz and Lupin only known filers. Watson launched in Sep 2006 and settled with Teva in May 2010 for a fully-paid license. Sandoz launched in Jan 2011. Lupin sued in Oct 2009. We expect Lupin to launch on receiving approval
ethinyl estradiol + norethindron acetate (0.02mg/1mg)	Loestrin 24 FE	~500	Warner Chilcott	Watson is FTF, sued in June 2006. Settled with Warner Chilcott in Jan 2009 to launch in Jan 2014. Lupin filed ANDA in July 2009 and settled with WC in Oct 2010. We expect Lupin to launch after Watson's 180 day exclusivity. No other known ANDA filers
ethinyl estradiol + norethindrone (0.035mg/0.4mg)	Femcon Fe	~35	Warner Chilcott	Watson and Teva FTF. Teva settled with WC in Dec 2008 and Watson settled in Jan 2009. Teva's ANDA has been approved and launched the generic in Mar 2011. Lupin filed in July 2009 and settled with WC in Oct 2010. We expect Watson and Lupin (authorized generic) to launch in Sep 2011 after Teva's 180 days exclusivity

Source: Spark Capital Research

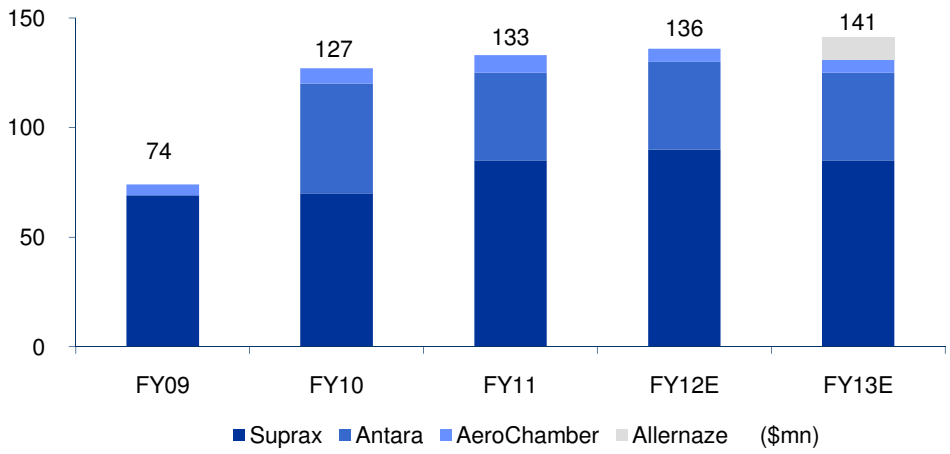
LUPIN

CMP	Rs. 465	Absolute	Buy
Target	Rs. 548	Relative	Outperform

Business Overview

- Lupin is the only Indian company with a significant branded presence in the US. Lupin's branded portfolio, which currently consists on 3 products, faces multiple headwinds. Protracted delay in the launch of Allernaze has also impacted the growth of this segment. We expect Lupin to scout for acquisitions especially in the pediatric segment to revive growth in its branded business
  - **Suprax:** Suprax was originally developed by Fujisawa and marketed by Wyeth until March 2003. Lupin acquired the brand and re-launched the oral suspension form of the drug in 2004. Lupin grew the franchise from ~$50mn sales in 2003 (under Wyeth) to ~$85mn in FY11. However, cefixime (the active ingredient in Suprax) is currently off-patent and open to generic makers to make their own versions. Lupin has delayed the entry of other generic players by launching line extensions and by filing a Citizen's Petition (which was granted by the FDA) seeking the same standards of evaluation as were applied while approving Lupin's generic version of the drug. Though exact timelines for generic entry is uncertain, we expect generic competition to the Suprax franchise by FY13. That said, we believe Lupin's strong product lifecycle extension measures should protect the Suprax franchise to a great extent even in a scenario of generic competition
  - **Antara:** Lupin acquired Antara (Fenofibrate Capsules 43 mg and 130 mg) from Oscient Pharmaceuticals (which went bankrupt) in FY10. Antara is prescribed for treatment of hypercholesterolemia and hypertriglyceridemia. The US fenofibrate products market is estimated at ~$1.9bn and Antara has market share of ~4.5%. Lupin managed to turn around the sales of the brand in Q4 FY11 after several quarters of sales decline following Oscient's bankruptcy. However, the Antara franchise is currently facing multiple headwinds
    - Shrinking fenofibrate market**:** A recent study titled ACCORD, did not support the use of a combination therapy of fenofibrate + statin vs. statin therapy alone, to reduce cardiovascular risk in patients with type 2 diabetes. The market for fenofibrate products has declined ~15% since the results of the study became known. As a result, Antara sales has stagnated in recent quarters, in spite of growing its share in the overall fenofibrate market
    - Generic Tricor**:** Tricor, sold by Abbott, is available as 48mg and 145mg tablets (Abbott used to sell Tricor as 54mg and 160mg tablets but allegedly "hopped" to the new formulations with minor variations to avoid generic competition). Teva is FTF on the 145mg version and settled with Abbott in Nov 2009 (according to Abbott, "generic competition could begin as early as March 2011 but is not expected until July 2012"). Teva has not yet received approval and has probably forfeited its FTF status. Other filers for the two doses are Biovail (likely FTF on the 48mg version), Ranbaxy, Lupin, and Impax (all except Impax have settled, allowing earliest launch in June 2012)
    - Generic Antara*:* Lupin was the first ANDA filer for a generic version of Antara and was sued by Oscient in Jan 2009. After acquiring the brand in Sep 2009, Lupin sold the FTF status to Dr. Reddy's. Ranbaxy (sued in Aug 2010) and Mylan (sued in Mar 2011) are other known ANDA filers. Both litigated patents ('574 and '331) expire in Aug 2020
  - **Aerochamber Plus***:* Aerochamber is a valved holding chamber device used with metered dose inhalers in the treatment of Asthma and COPD, in-licensed from Forest Labs in FY09. Lupin promotes the product to pediatricians using its sale force
  - **Allernaze** (triamcinolone 50mcg nasal spray used in allergic rhinitis): Acquired from Collegium Pharmaceuticals in FY10. Launch has been delayed due to operational issues

US branded business facing multiple headwinds



Source: Company data, Spark Capital Research

LUPIN

CMP	Rs. 465	Absolute	Buy
Target	Rs. 548	Relative	Outperform

Financial Summary

Abridged Financial Statements (Consolidated)				
Rs. mn	FY10	FY11	FY12E	FY13E
Profit & Loss				
Net Sales	**47,405**	**56,478**	**65,520**	**77,136**
EBITDA	8,536	10,069	11,400	14,039
Depreciation	(1,239)	(1,712)	(1,981)	(2,258)
EBIT	7,297	8,357	9,419	11,781
Other Income	1,445	1,931	2,649	3,146
Interest	(385)	(325)	(269)	(200)
PBT	8,357	9,963	11,800	14,727
PAT	6,816	8,625	9,840	12,287
Adjusted PAT	**6,641**	**8,515**	**9,840**	**12,287**
Balance Sheet				
Net Worth	25,933	33,326	42,017	52,973
Deferred Tax	1,435	1,411	1,411	1,411
Total debt	11,399	11,624	9,880	8,003
Total Networth and liabilities	**38,767**	**46,361**	**53,309**	**62,388**
Gross Fixed assets	29,713	34,956	39,956	44,456
Net fixed assets	22,640	25,881	28,899	31,141
Investments	264	32	32	32
Inventories	9,715	12,000	14,040	16,535
Sundry Debtors	11,266	12,558	14,693	17,304
Cash and bank balances	2,015	4,201	4,976	7,266
Loans and advances	4,759	6,208	6,656	7,839
Current liabilities	11,893	14,518	15,986	17,729
Net current assets	15,862	20,449	24,378	31,215
Total assets	**38,767**	**46,361**	**53,309**	**62,388**
Cash Flows				
Cash flows from Operations	6,764	7,969	9,574	11,613
Cash flows from Investing	(6,799)	(4,315)	(5,448)	(5,683)
Cash flows from Financing	1,361	(1,605)	(3,351)	(3,639)

Key metrics				
	FY10	FY11	FY12E	FY13E
Growth ratios				
Net Sales	25.5%	19.1%	16.0%	17.7%
EBITDA	31.6%	18.0%	13.2%	23.1%
Adjusted PAT	34.2%	28.2%	15.6%	24.9%
Margin ratios				
EBITDA	18.0%	17.8%	17.4%	18.2%
Adjusted PAT	14.0%	15.1%	15.0%	15.9%
Performance ratios				
RoE	33.5%	29.2%	26.6%	26.3%
RoCE	22.7%	22.2%	21.5%	22.8%
RoA	20.3%	20.4%	20.1%	21.6%
Fixed asset turnover (x)	1.8	1.7	1.7	1.8
Total asset turnover (x)	1.4	1.3	1.3	1.3
Financial stability ratios				
Net Debt to Equity (x)	0.4	0.2	0.1	0.0
Current ratio (x)	2.3	2.4	2.5	2.8
Inventory and debtor days	180	160	157	157
Creditor days	81	78	84	84
Working capital days	100	82	73	73
Interest cover (x)	19.0	25.7	35.0	58.9
Valuation metrics				
Fully Diluted Shares (mn)	438.0	448.2	448.8	448.8
Market cap (Rs.mn)	207,592			
EPS (Rs.)	**15.2**	**19.0**	**21.9**	**27.4**
P/E (x)	**30.7**	**24.5**	**21.2**	**17.0**
EV (Rs.mn)	215,530			
EV/ EBITDA (x)	25.2	21.4	18.9	15.4
BV/ share (Rs.)	58.6	73.2	92.0	115.9
Price to BV (x)	7.9	6.4	5.1	4.0

Torrent Pharmaceuticals

Positioned for chronic growth

CMP	Rs. 598	Absolute	Buy
Target	Rs. 701	Relative	Outperform

We expect Torrent's chronic-heavy portfolio, recent sales force additions and new marketing initiatives to propel its domestic sales in FY11-FY13E. The recently-entered contract manufacturing agreements with MNCs positions the company for volume-driven growth in fast-growing EMs. The ongoing capacity expansions augurs well for the long-term and the company's strong balance sheet and cash generation provides comfort on its ability to finance these projects. We value Torrent at 15x FY13E EPS (a 25% discount to large cap pharma companies) to arrive at a target price of Rs. 701 and initiate coverage with a Buy/Outperform rating

Investment rationale

- **Chronic heavy portfolio and recent sales force additions to drive domestic sales:** Chronic therapies account for ~60% of Torrent's domestic sales. The company holds no.2 and no.3 positions in the cardiovascular and neuropsychiatry segments. Torrent's strong franchise in key fast-growing chronic segments positions its domestic business favorably, in our view. The company has significantly strengthened its domestic sales force in the last two years (~1,200 reps added in the last 2 years) as it aggressively expanded into tier II to IV markets and into new therapeutic segments such as gynecology. We believe these initiatives will positively impact the company in FY12-FY13. A ramp up in sales force productivity (currently low compared to peers due to recent MR additions) should further boost domestic sales
- **US business to lead growth in international segment:** Torrent is a relatively new entrant to the US market, which contributed only 5% to its topline in FY11. We expect ~5-6 launches per year going forward given the company's recent ANDA filing momentum (13 ANDAs each filed in FY10 and FY11, 32 ANDAs pending approval currently). Torrent is the largest Indian player in the fast-growing Brazilian market and has outperformed its Indian peers in the challenging German market (where recent regulatory changes impacted every player), which are key positives in our view
- **MNC supplies to boost contract manufacturing revenues:** Torrent has recently entered into 3 contract manufacturing agreements 1) Multiproduct (initially for 9 products, later expanded to ~30 products) outlicensing agreement with Astra Zeneca for 18 key emerging markets 2) Multi-product (~50 products), multi-market outlicensing contract with undisclosed branded generic MNC for emerging markets 3) Supply of currently under-patent product to an innovator pharma company after patent expiry. These supply agreements are non-exclusive and positions Torrent to enhance its presence in fast-growing EMs, leveraging its large product basket and strong manufacturing capabilities, without the high upfront investments required if it were to enter some of these markets on its own. We expect supplies to start from FY13
- **Strong balance sheet and cash generation to support major capacity expansions:** Torrent is currently investing heavily in expanding its manufacturing facilities including greenfield projects and expansions at existing facilities. The company recently commissioned a new formulations facility at Sikkim (Rs. 1.3bn) and expanded its facility at Indrad (Rs. 1.7bn). Next in line is a 2 phase Rs. 8bn expansion at Dahej to be completed by 2016-2017. We believe these expansions position Torrent for strong long-term growth and the company's strong balance sheet and cash generation provides comfort on its ability to finance these projects

Financial summary

Year	Sales (Rs. mn)	EBITDA (Rs. mn)	Adj PAT (Rs. mn)	Adj EPS (Rs.)	P/E (x)	ROE (%)
FY11	21,220	3,047	2,532	29.9	20.0	27.3
FY12E	25,087	3,740	3,187	37.7	15.9	27.6
FY13E	30,875	4,770	3,953	46.7	12.8	27.3

Initiating coverage

Date	Sep 13, 2011
Market Data	
SENSEX	16502
Nifty	4947
Bloomberg	TRP IN
Shares o/s	85mn
Market Cap	Rs. 51bn
52-wk High-Low	Rs. 687-497
3m Avg. Daily Vol	Rs. 45mn
Index member	BSEMDCAP
Latest shareholding (%)	
Promoters	71.5
Institutions	16.8
Public	11.7

Stock performance (%)

	1m	3m	12m
TRP	-4%	1%	11%
Sensex	-2%	-10%	-14%
BSETHC	-2%	-6%	4%

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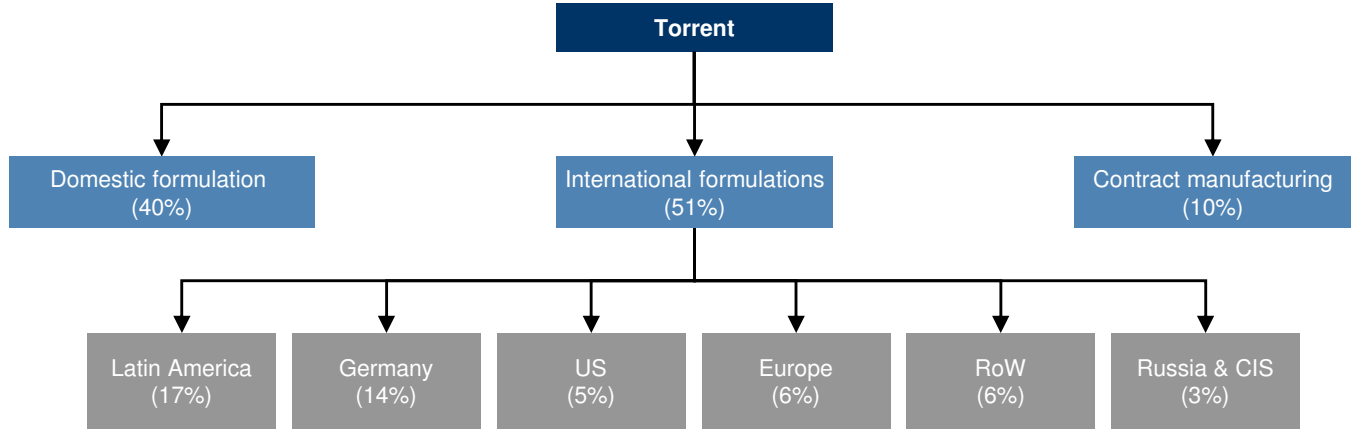
Torrent Pharmaceuticals

CMP	Rs. 598	Absolute	Buy
Target	Rs. 701	Relative	Outperform

Company Overview

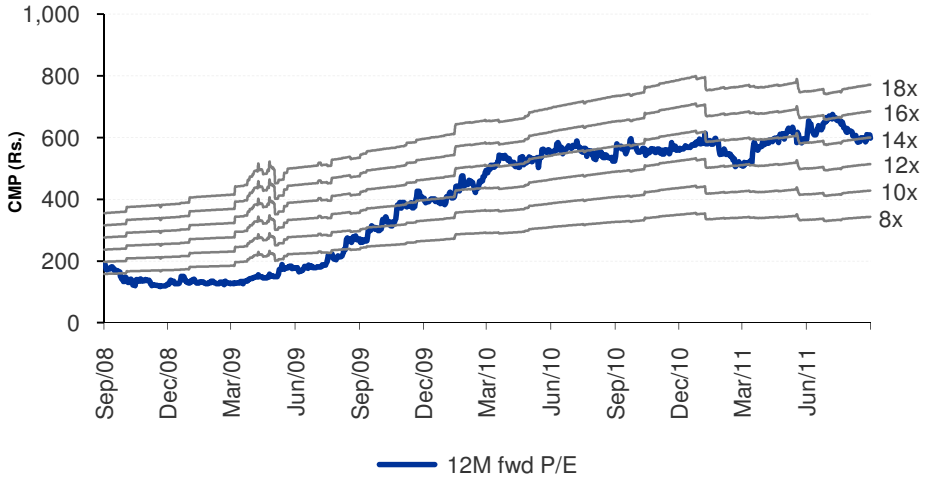
Sales breakup (FY11)



Source: Company, Spark Capital Research

In its recent history, Torrent has traded at 12-16x one-year forward earnings. Given its strong earnings momentum (25% EPS CAGR in FY11-FY13E), balance sheet strength, cash flow profile and attractive return ratios, we value Torrent at 15x FY13E EPS (a 25% discount to large cap pharma companies) to arrive at a target price of Rs. 701. Our target price implies an upside of 17% from current levels.

P/E band



Source: Bloomberg, Spark Capital Research

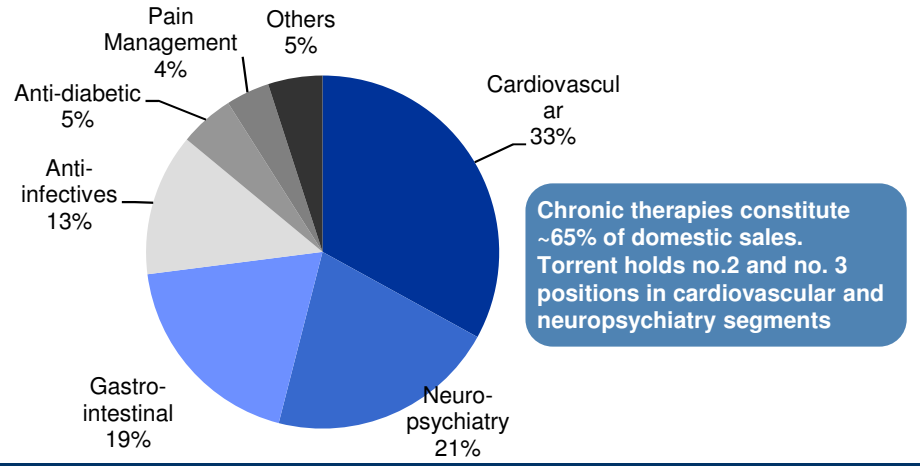
Torrent Pharmaceuticals

CMP	Rs. 598	Absolute	Buy
Target	Rs. 701	Relative	Outperform

Business Overview

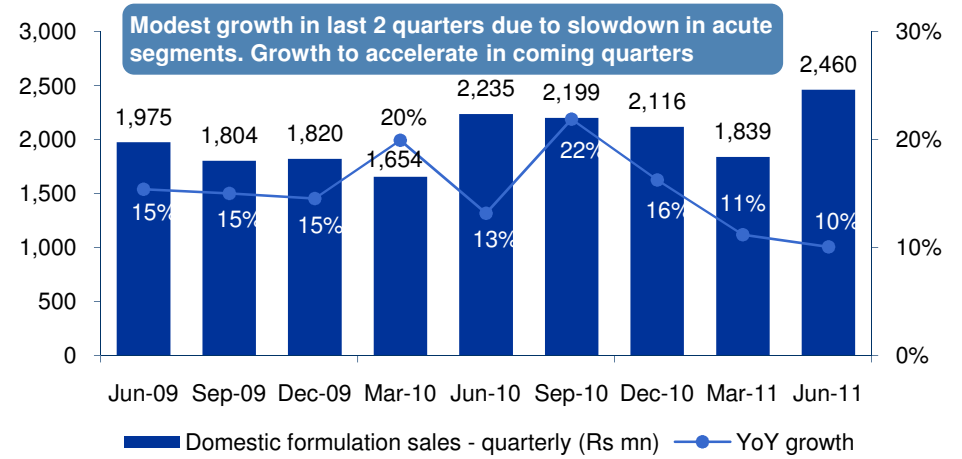
- Chronic therapies account for ~60% of Torrent's domestic sales. The company holds no.2 and no.3 positions in cardiovascular and neuropsychiatry segments. Torrent's strong franchise in key fast-growing chronic segments positions its domestic business favorably, in our view
- The company has significantly strengthened its domestic sales force in the last two years (~1,200 reps added in the last 2 years) as it aggressively expanded into tier II to IV markets and into new therapeutic segments such as gynecology. We believe these initiatives will positively impact the company in FY12-FY13. A ramp up in sales force productivity (currently low compared to peers due to recent MR additions) should further boost domestic sales
- Torrent has a strong track record of new product launches with >200 products launched in the last 5 years. In FY11, new products (launched in FY10 and FY11) contributed 6% (out of 15% total) to the company's domestic sales growth. We expect the momentum in new launches to continue going forward

Domestic formulations – therapeutic breakup (FY11)



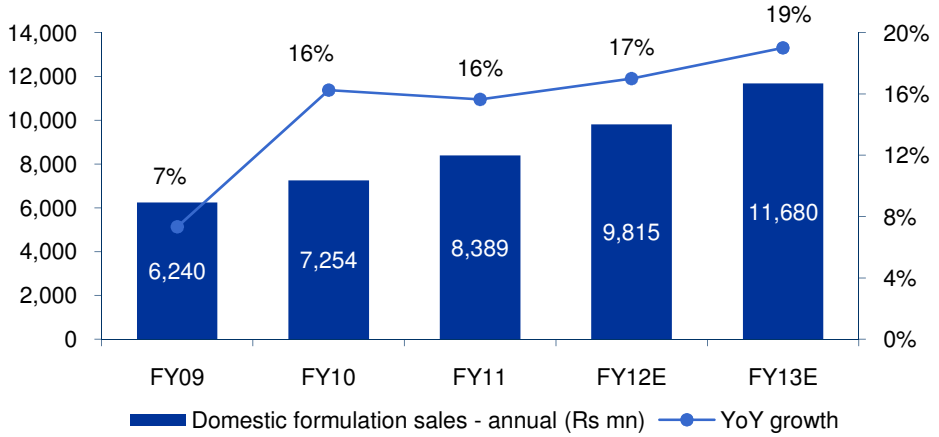
Source: Company data, Spark Capital Research

Domestic formulations – quarterly trend



Source: Company data, Spark Capital Research

Domestic formulations – annual sales



Source: Company data, Spark Capital Research

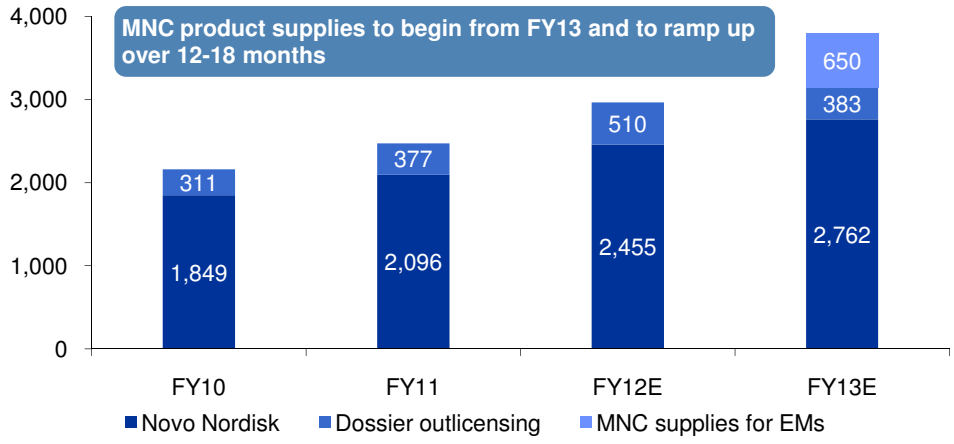
Torrent Pharmaceuticals

CMP	Rs. 598	Absolute	Buy
Target	Rs. 701	Relative	Outperform

Business Overview

- Since 1992, Torrent has been manufacturing and supplying human insulin (4 SKUs) for Novo Nordisk for the domestic market. In FY09 and FY10, Torrent entered into 3 additional contract manufacturing agreements:
  - Multiproduct (initially for 9 products, later expanded to ~30 products) outlicensing agreement with Astra Zeneca for 18 key emerging markets
  - Multi-product (~50 products), multi-market outlicensing contract with undisclosed branded generic MNC for emerging markets
  - Supply of currently under-patent product to an innovator pharma company after patent expiry
- We expect these contracts to start contributing to Torrent's contract manufacturing revenues from FY13. These supply agreements are non-exclusive and positions Torrent to leverage its large product basket and strong manufacturing capabilities without the high upfront investments required to enter most of these markets on its own

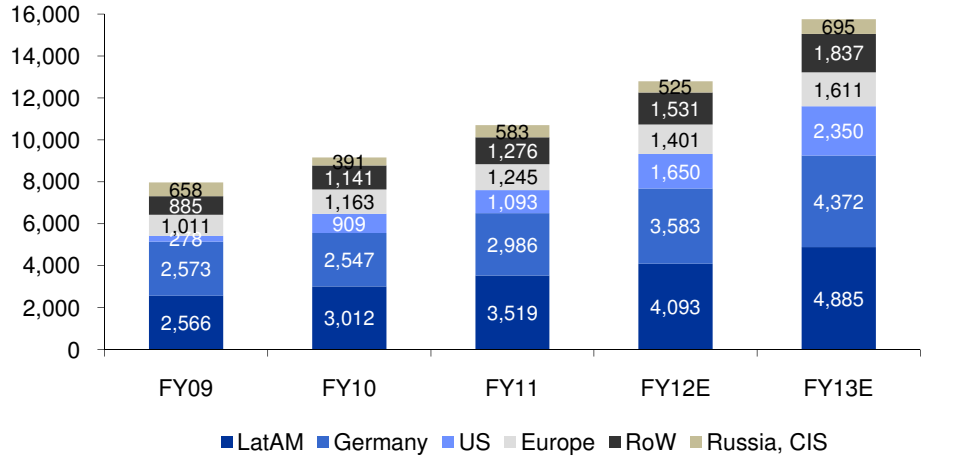
Contract manufacturing revenues



Source: Company data, Spark Capital Research

- International formulations accounted for ~50% of Torrent's topline in FY11. We believe Latin America (Brazil and Mexico), Germany and the US will be key markets for Torrent going forward
  - Latin America - Torrent is the largest Indian player in Brazil and currently has a portfolio ~27 products. The company recently entered Mexico and plans to grow its portfolio to ~30 products in 4 years
  - Germany - Torrent entered Germany through the acquisition of Heumann in 2005. The company has adapted to the regulatory changes in the German market which resulted in drastic price cuts and impacted the entire generic industry. We note that Torrent has managed to perform better than some of its Indian peers (such as Dr. Reddy's) in the last 3-4 years
  - US - Torrent is a relatively new entrant to the US market, which contributed only ~5% to its topline in FY11. The company focuses on commoditized product opportunities and on gaining market shares post-launch. We expect ~5-6 launches per year going forward given the company's recent ANDA filing momentum (13 ANDAs each filed in FY10 and FY11, 28 ANDAs approved and 32 ANDAs pending approval currently)

International formulations



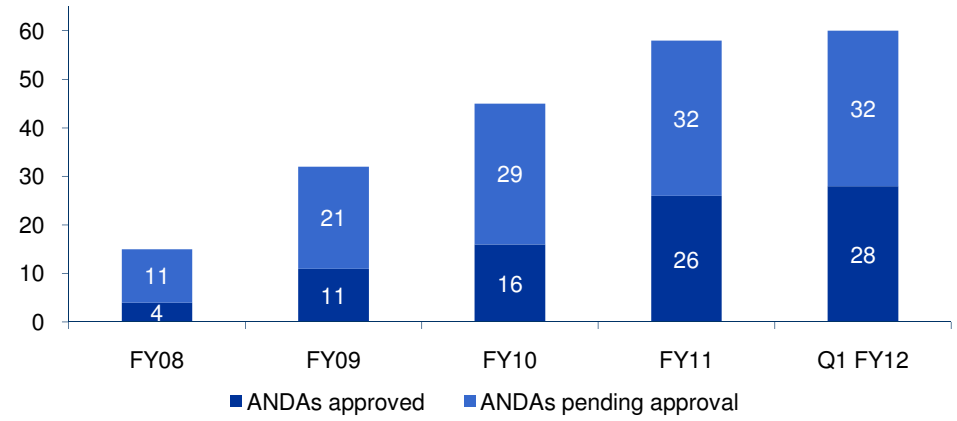
Source: Company data, Spark Capital Research

Torrent Pharmaceuticals

CMP	Rs. 598	Absolute	Buy
Target	Rs. 701	Relative	Outperform

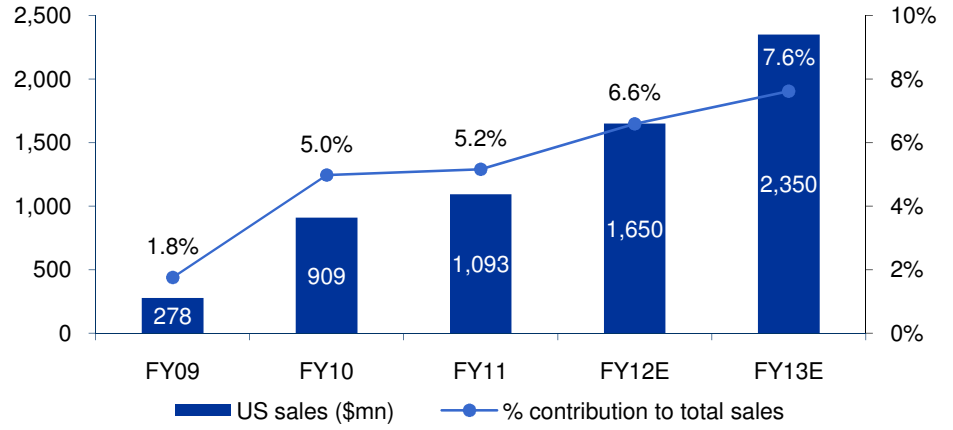
Business Overview

ANDA filings



Source: Company data, Spark Capital Research

Contribution from US to rise



Source: Company data, Spark Capital Research

Key product opportunities for Torrent in the US

					Brand Sales ($mn)		
Brand	Generic	Indication	Innovator	Para IV/FTF	US	WW	Comments
Uroxatral	alfuzosin hydrochloride	Benign Prostatic Hyperplasia	Sanofi Aventis	Yes / Yes	250	-	Torrent received final approval in July 2011. 4 other generic players with final approval
Cymbalta	duloxetine hydrochloride	Depression	Eli Lilly	Yes / No	2,772	3,459	Multiple players share FTF status. ~10 players with tentative approval including Torrent. Compound patent expires in June 2013
Actos	pioglitazone	Type 2 diabetes	Takeda	Yes / No	3,200	-	Multiple para IV filers. FTF holders (Ranbaxy, Mylan and Watson) and authorized generic (Teva) to launch in Aug 2012. Torrent sued by Takeda in July 2009. FTF exclusivity expires in Feb 2013
Crestor	rosuvastatin	Dyslipidemia	AstraZeneca	Yes / No	2,640	5,691	Multiple para IV filers with 8 players having tentative approvals. Compound patent expires in Jan 2016
Seroquel XR	quetiapine	Bipolar disorder	AstraZeneca	Yes / No	640	1,154	Multiple para IV filers. Validity of '437 patent (expiring in Nov 2017) is being litigated
Keppra XR	levetiracetam extended release	Epilepsy	UCB	No / No	-	1,372	Torrent launched the oral tablet form (multiple doses) which is a >10 player market. Torrent has tentative approval for the extended release (ER) version (multiple strengths). NCE exclusivity expires in Sep 2011. Only Orange Book listed patent ('122 patent) expires in Sep 2028
Plavix	clopidogrel	Blood thinner	Sanofi Aventis	No / No	6,666	-	Torrent has tentative approval along with multiple other players. Pediatric extension of compound patent expires in May 2012
Singulair	montelukast	Asthma/ Allergic Rhinitis	Merck	No / No	-	2,714	Torrent has tentative approval for the chewable tablet version. 3 other players with TAs. Pediatric extension of compound patent expires in Aug 2012
Lexapro	escitalopram	Anti-depressants	Forest Labs	No / No	2,300	-	>10 players with tentative approval including Torrent. Compound patent expires in Mar 2012. Teva likely FTF. Alphapharm (subsidiary of Mylan) has settled with Forest to launch 2wks prior to patent expiry

Torrent Pharmaceuticals

CMP	Rs. 598	Absolute	Buy
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Financial Summary

Abridged Financial Statements (Consolidated)				
Rs. mn	FY10	FY11	FY12E	FY13E
Profit & Loss				
Net Sales	**18,329**	**21,220**	**25,087**	**30,875**
EBITDA	3,377	3,047	3,740	4,770
Depreciation	(661)	(626)	(795)	(906)
EBIT	2,716	2,421	2,944	3,864
Interest	(291)	(387)	(357)	(274)
Other Income	1,047	1,392	1,302	1,233
PBT	3,472	3,427	3,889	4,824
PAT	2,312	2,702	3,187	3,953
Adjusted PAT	**2,232**	**2,532**	**3,187**	**3,953**
Balance Sheet				
Net Worth	8,310	10,240	12,837	16,116
Deferred Tax	499	480	480	480
Total debt	5,224	5,721	4,375	3,378
Total Networth and liabilities	**14,033**	**16,441**	**17,693**	**19,973**
Gross Fixed assets	9,228	11,829	14,079	16,579
Net fixed assets	6,510	8,541	9,996	11,590
Investments	1,412	1,460	1,460	1,460
Inventories	3,236	5,048	5,842	6,936
Sundry Debtors	2,982	3,404	4,024	4,953
Cash and bank balances	3,883	4,788	3,657	3,291
Loans and advances	1,506	2,106	2,489	3,064
Current liabilities	5,496	8,907	9,776	11,320
Net current assets	6,111	6,440	6,237	6,924
Total assets	**14,033**	**16,441**	**17,693**	**19,973**
Cash Flows				
Cash flows from Operations	2,870	3,945	3,185	3,885
Cash flows from Investing	(1,287)	(2,326)	(2,250)	(2,500)
Cash flows from Financing	(52)	(671)	(2,066)	(1,751)

Key metrics				
	FY10	FY11	FY12E	FY13E
Growth ratios				
Net Sales	15.5%	15.8%	18.2%	23.1%
EBITDA	57.4%	-9.8%	22.7%	27.6%
Adjusted PAT	15.8%	13.4%	25.9%	24.0%
Margin ratios				
EBITDA	18.4%	14.4%	14.9%	15.5%
Adjusted PAT	12.2%	11.9%	12.7%	12.8%
Performance ratios				
RoE	30.1%	27.3%	27.6%	27.3%
RoCE	19.7%	19.5%	21.0%	22.8%
RoA	17.2%	16.6%	18.7%	21.0%
Fixed asset turnover (x)	2.2	2.0	1.9	2.0
Total asset turnover (x)	1.4	1.4	1.5	1.6
Financial stability ratios				
Net Debt to Equity (x)	0.2	0.1	0.1	0.0
Current ratio (x)	2.1	1.7	1.6	1.6
Inventory and debtor days	124	145	144	141
Creditor days	117	179	165	155
Working capital days	7	(33)	(21)	(14)
Interest cover (x)	9.3	6.3	8.3	14.1
Valuation metrics				
Fully Diluted Shares (mn)	84.6	84.6	84.6	84.6
Market cap (Rs.mn)	50,626			
EPS (Rs.)	**26.4**	**29.9**	**37.7**	**46.7**
P/E (x)	**22.7**	**20.0**	**15.9**	**12.8**
EV (Rs.mn)	51,360			
EV/ EBITDA (x)	15.2	16.9	13.7	10.8
BV/ share (Rs.)	98.2	120.8	151.6	190.3
Price to BV (x)	6.1	5.0	3.9	3.1

Absolute Rating Interpretation	
BUY	Stock expected to provide positive returns of > 15% over a 1-year horizon
ADD	Stock expected to provide positive returns of <=15% over a 1-year horizon
REDUCE	Stock expected to fall <=15% over a 1-year horizon
SELL	Stock expected to fall >15% over a 1-year horizon

Relative Rating Interpretation	
OUTPERFORM	Stock expected to outperform sector index /sector peers in our coverage
UNDERPERFORM	Stock expected to underperform sector index/ sector peers in our coverage

Analyst Certification

The Research Analyst(s) who prepared the research report hereby certify that the views expressed in this research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certify that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

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