NEUTRAL

Price	Rs561
Target Price	-
Investment Period	-

Stock Info

Sector	Pharmaceutical
Market Cap (Rs cr)	20,931
Beta	0.57
52 WK High / Low	593/300
Avg Daily Volume	3,75,491
Face Value (Rs)	5
BSE Sensex	15,185
Nifty	4,524
BSE Code	500359
NSE Code	RANBAXY
Reuters Code	RANB.BO
Bloomberg Code	RBXY IN

Shareholding Pattern (%)

Promoters	34.8
MF/Banks/Indian FIs	23.3
FII/ NRIs/ OCBs	21.0
Indian Public	20.9

Abs.	**3m**	**1yr**	**3yr**
Sensex (%)	(5.8)	7.8	123.9
Ranbaxy (%)	23.7	51.5	4.8

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Ranbaxy stake sale to Daiichi Sankyo

- **Contours of the Deal:** In one of its kind deal in the corporate space, Daiichi Sankyo Co., the second largest pharmaceutical company in Japan, has taken a stake in India's largest pharmaceutical company, Ranbaxy Laboratories. This is also the first of the instances of a Generic and Innovator company coming together.

  According to the agreement, Daiichi has taken full 34.8% stake held by the promoters of Ranbaxy at Rs737 per share. With this, Daiichi would make an open offer for upto 20% additional stake in Ranbaxy. Apart from this Daiichi would be issued preferential shares and warrants of 46,258,063 and 23,834,333 respectively, at Rs737/share. The warrants can be exercised by Daiichi within 6-18 months after the issue. With this, assuming conversion of the FCCB, fully diluted Equity of Ranbaxy would go up from 38.2cr to 48.6cr, a dilution of 27%.

  On a fully diluted basis, the deal values Ranbaxy at $8.5bn. At current levels, Ranbaxy would be valued at 4x EV/Sales and 24.7x EV/EBITDA on CY2009E Earnings. The stake buyout is expected to be completed by March 2009 and on completion, Ranbaxy would become a subsidiary of Daiichi Sankyo. Further, Ranbaxy's NCE business unit, which was supposed to be demerged into a different entity, will continue to remain under its fold and will not be demerged as of now.

- **What does the Deal entail for Ranbaxy?** Daiichi Sankyo is a leading century-old Japanese pharmaceutical company, having a portfolio of proprietary drugs. With Sales of $8bn, the company is ranked 22nd in the global pecking order. The company derives majority of its revenues from the Regulated markets with Japan being the key market. On the R&D front, the company focuses on the six areas of cardiovascular diseases, glucose metabolic disorders, infectious diseases, cancer, immunity and allergies, and bones/joint diseases. The company spent around 18.6% of Sales on R&D (in FY2007). Currently, it has a pipeline of around 10 molecules in Phase III. Thus, with this acquisition, the company would get access to the proprietary drug portfolio of Daiichi and catapult Ranbaxy-Daiichi combined to the to 15th largest Pharma company in the world. Further, the fund infusion by Daiichi through the preferential issue and warrants would infuse $1.2bn in Ranbaxy and enable it to retire its debt. Ranbaxy expects to have cash surplus of around Rs3,000cr, which would further strengthen its balance sheet and business (through both the organic and in-organic routes).

- **Management at the helm remains the same:** As per the agreement, the Board will have 10 members, with 4 from Ranbaxy and 6 from Daiichi. Malvinder Singh will continue to be the CEO and MD and will also become a member of the senior global management of Daiichi.

- **Daiichi Sankyo to gain from the global spread of Ranbaxy:** Acquisition of Ranbaxy would provide Daiichi Sankyo a presence in high-growth Emerging markets like India, China and Eastern Europe. Further, with Ranbaxy being present in more than 40 countries provides a strong front for Daiichi Sankyo to launch its products. Along with providing a front-end, the deal also provides Daiichi a strong generic product portfolio with strong visibility on First-To-File (FTF) product (20 FTF products addressing a market opportunity of $26bn) launches over the next few years. Large blockbuster drugs will go off patent globally over the next five year span. Ranbaxy is well-positioned to capture the upsides from the same drawing from its product pipeline. In fact, Ranbaxy's FTF product pipeline is the best in the space and captures major upsides from the large blockbuster drugs going off patent in the next few years. Daiichi would leverage Ranbaxy's strengths in the generic markets to strengthen its presence in the emerging generic market in Japan. Apart from the generic markets, Daiichi would also benefit by leveraging the low-cost advantage of the Indian assets both in Manufacturing and R&D. Thus, Daiichi could use Ranbaxy as an out-sourcing hub for its products. However, management has not indicated the potential upsides that could accrue to Ranbaxy on account of the same.

- **Open offer for Zenotech Labs:** Acquisition of the stake in Ranbaxy would entail an open offer for Zentoech in which Ranbaxy holds 46.95%. However, in companies like Krebs Biochem, Jupiter Biosciences and Orchid Chemicals where Ranbaxy's stake is lesser than 20%, an open offer from Daiichi is ruled out.

- **Upsides from the stock limited after the up-move**: After severe underperformance over the last couple of years, the Ranbaxy stock had witnessed a strong run-up in the last one month, rising by more than 40% during the period. We have revised our SOTP Target Price downwards to factor in the Equity dilution in the near term to Rs535 (Rs603). Our Target Price also factors in the strong cash inflows expected following the fund infusion by Daiichi. As per the open offer (Rs737), at the current market price of Rs561 and acceptance ratio of 33% (assuming conversion of the FCCBs and issue of the preferential shares), the Fair Price works out to Rs602, an upside of a mere 7%. **Hence, given the risk–reward ratio, we recommend investors to subscribe to the open offer.**

Key Financial (Consolidated)

YE Dec (Rs cr)	CY2006	CY2007	CY2008E	CY2009E
Net Sales	**6,012.6**	**6,641.3**	**7,412.8**	**9,163.4**
% chg	*17.9*	*10.5*	*11.6*	*23.6*
Adj Net Profit	**510.9**	**554.0**	**713.1**	**937.2**
% chg	*95.2*	*8.4*	*28.7*	*31.4*
FDEPS (Rs)	**10.5**	**11.4**	**14.7**	**19.3**
EBITDA Margin (%)	14.2	10.5	16.2	15.9
P/E (x)	**53.4**	**49.2**	**38.2**	**29.1**
RoE (%)	20.1	20.1	10.5	8.7
RoCE (%)	**16.3**	**16.0**	**13.1**	**11.3**
P/BV (x)	6.3	5.4	2.1	2.0
EV/Sales (x)	**4.1**	**3.7**	**3.2**	**2.6**
EV/EBITDA (x)	28.2	23.7	19.4	16.2

Source – Company, Angel Research

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Ratings (Returns) :	Buy (Upside > 15%)	Accumulate (Upside upto 15%)	Neutral (5 to -5%)
	Reduce (Downside upto 15%)	Sell (Downside > 15%)	