

July 15, 2010

# Piramal Healthcare (NICPIR)

Rs 504

## WHAT'S CHANGED...

PRICE TARGET .....	Changed from Rs 595 to Rs 589
EPS of residual business (FY11E) .....	Rs 4.6
EPS of residual business (FY12E) .....	Rs 5.9
RATING .....	Unchanged

## Diagnostic business off the shelf...

Piramal Healthcare has signed a definitive agreement to sell its diagnostic business to Super Ranbaxy Laboratories (SRL) for a consideration of Rs 600 crore. SRL is promoted by Malvinder and Shivinder Singh. Piramal will receive Rs 300 crore on closure of the deal and a final payment of Rs 300 crore after three years. The deal is valued at 3x the revenue of the diagnostics business and is expected to close by the end of Q3FY11. The diagnostics business contributed ~5.6% to the FY10 topline. The deal includes transfer of 107 laboratories, ~300 collection centres and ~450 employees to SRL. Post the deal, SRL will have the largest pathology and radiology network. Piramal will have 10% equity participation in SRL valued at Rs 135 crore, which it will exit after three years. We estimate the residual businesses will clock an EPS of ~Rs 5.9 in FY12E. Valuing the cash per share from Abbott and SRL at Rs 518 and residual business at Rs 71, we have arrived at a fair value of Rs 589 for PHIL, providing 17% upside from current levels. We maintain our BUY rating on the stock.

### ■ Highlights of the deal

PHIL has retained its CRAMS, global critical care, domestic API and vitamins/minerals business. The company is considering a special dividend post the deal. The company will look at acquisitions to complement the residual business and enter newer businesses.

## Valuation

PHIL is set to receive US\$3.3 billion on NPV value from Abbott and Rs 600 crore from SRL. This works out to Rs 518 per share (post long-term capital gains taxed at 21.5%, book value adjustment and debt repayment of ~Rs 1300 crore). The residual business is valued at Rs 71 (12x FY12E EPS). We have rated PHIL as **BUY** with a target price of Rs 589. With cash utilisation by the management post the deal we expect the stock to get re-rated, going forward.

### Exhibit 1: Financial Summary

(Rs Crore)	FY08	FY09	FY10	FY11E	FY12E
Net Sales	2848.3	3281.1	3671.1	4102.8	4633.3
EBITDA	517.1	581.3	740.9	843.5	977.7
Net Profit	333.8	316.2	481.8	528.1	638.4
EPS	16.0	15.1	23.1	25.3	30.5
PE	32.0	33.8	22.2	20.2	16.7
EV/EBITDA	21.8	20.5	16.1	13.9	11.8
RoNW (%)	30.7	24.0	28.3	25.4	25.3
RoCE (%)	24.6	17.7	18.8	20.9	22.7

Source: Company, ICICIdirect.com Research

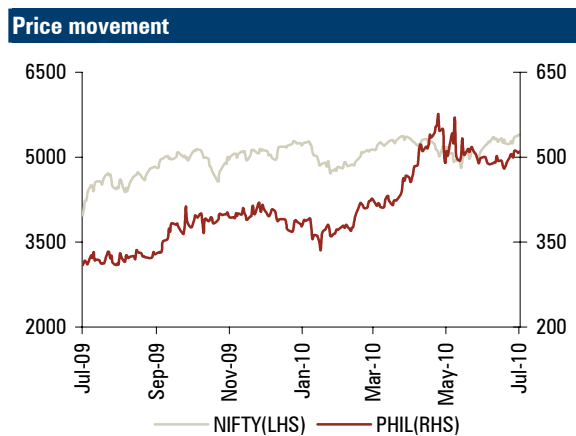
Rating matrix	
Rating	: Buy
Target	: Rs 589
Target Period	: 12-15 months
Potential Upside	: 17 %

Key Financials				
(Rs Crore)	FY09	FY10	FY11E*	FY12E*
Net Sales	3281.1	3671.1	4102.8	4633.3
EBITDA	581.3	740.9	843.5	977.7
Net Profit	316.2	481.8	528.1	638.4

Valuation Summary				
	FY09	FY10	FY11E*	FY12E*
EPS (Rs)	15.1	23.1	25.3	30.5
PE (x)	33.3	21.9	19.9	16.5
Target PE (x)	38.9	25.5	23.3	19.3
EV to EBITDA (x)	20.3	15.9	13.7	11.7
Price to book (x)	8.0	6.2	5.0	4.2
RoNW (%)	24.0	28.3	25.4	25.3
RoCE (%)	17.7	18.8	20.9	22.7

\* Will be revised post successful closure of deals

Stock data	
Market Capitalisation (Rs Crore)	10530.5
Debt (FY10), (Rs Crore)	1418.1
Cash (FY10), (Rs Crore)	138.2
EV (Rs Cr)	11810.4
52 week H/L	600/300
Equity capital (Rs Crore)	41.8
Face value (Rs)	2.0
MF Holding (%)	3.3
FII Holding (%)	26.1



Analyst's name	
Siddhant Khandekar	siddhant.khandekar@icicisecurities.com
Ashish Thavkar	ashish.thavkar@icicisecurities.com

### ■ The deal

We have valued the residual business at Rs 71/share on FY12E earnings. We have valued the cash inflow from Abbott, including the upfront payment (US\$2.12 billion) and the discounted value of the annuity payments adjusted for debt repayment and book value and capital gains tax, at Rs 496/share. The deal with SRL has been valued at Rs 22/share while the residual business has been valued at 12x FY12E EPS of Rs 71/share. The combined value of the entity stands at Rs 589/share. We expect the stock to get re-rated on account of deployment of cash by the management.

<b>Exhibit 2: Deal structure</b>		<b>(Rs Crore)</b>			
<b>Piramal - Abbott Deal</b>					
	<b>Upfront</b>	<b>Annuity payment (US\$ 400 mn from FY11)</b>			
Payment from Abbott (US\$ 2.12 bn)	9540	1800	1800	1800	1800
NPV, discounted at 15%	14679.0				
Adjusted for BV	13979.0				
Less Capital gains tax at 21.5%	3005.5				
Less Debt Repayment	1300.0				
Total Cash	10373.5				
<b>Cash Per Share</b>	<b>496.3</b>				
<b>Piramal - SRL Deal</b>					
	<b>Upfront</b>	<b>To be received after 3 years</b>			
Payment from SRL	300	300			
NPV, discounted at 15%	497.3				
Adjusted for BV	202.3				
Less Capital gains tax at 21.5%	43.5				
Total Cash	453.8				
<b>Cash Per Share</b>	<b>21.7</b>				
<b>Residual business valuation</b>					
FY12 estimated PAT	124.2				
FY12E EPS	5.9				
<b>Target price at 12x FY12E EPS</b>	<b>71.3</b>				
<b>Target Price per share (post deal)</b>	<b>589.4</b>				

Source: Company, ICICIdirect.com Research

### ■ Residual business to remain key focus

Post the deal with Abbott and SRL, PHIL has been left with the CRAMS, global critical care, domestic API and vitamins/minerals business. These businesses contributed ~40% to the FY10 topline. We expect a revamp in the international CRAMS business to lead the majority of the growth, going ahead. We expect the India-based assets to offset a decline in the international CRAMS business in the near term. The Abbott-PHIL and SRL-PHIL deal will lead to greater focus for PHIL to turn around its CRAMS business and drive the future growth of the critical care and the OTC businesses.

#### Exhibit 3: PHIL's business break-up

(Rs Crore)	FY08	% share	FY09	% share	FY10	% share
<b>Sold-out Business</b>						
<b>Healthcare Solutions *</b>	<b>1291.4</b>	<b>45.0</b>	<b>1604.9</b>	<b>48.9</b>	<b>2000.2</b>	<b>54.5</b>
<b>Diagnostics</b>	<b>98.5</b>	<b>3.4</b>	<b>169.0</b>	<b>5.1</b>	<b>206.4</b>	<b>5.6</b>
<b>Residual Business</b>						
<b>Pharma Solutions</b>	<b>1008.1</b>	<b>35.2</b>	<b>1060.6</b>	<b>32.3</b>	<b>885.0</b>	<b>24.1</b>
From Assets in India	225.9	7.9	392.5	12.0	375.9	10.2
From Assets o/s India	782.2	27.3	668.1	20.4	509.1	13.9
<b>Global Critical Care</b>	<b>119.4</b>	<b>4.2</b>	<b>131.6</b>	<b>4.0</b>	<b>327.7</b>	<b>8.9</b>
<b>Others</b>	<b>350.2</b>	<b>12.2</b>	<b>315.0</b>	<b>9.6</b>	<b>251.7</b>	<b>6.9</b>
<b>Total</b>	<b>2867.5</b>	<b>100.0</b>	<b>3281.1</b>	<b>100.0</b>	<b>3671.1</b>	<b>100.0</b>

Source: Company, ICICIdirect.com Research

\* Retained domestic API and vitamins/minerals business

#### Valuation

In the contract manufacturing space, PHIL grew at a slower pace on account of control over the channel inventory by PHIL's CRAMS clients. We believe PHIL's CRAMS business will see a recovery in FY11 as innovator pharma companies come out of the current mode of inventory de-stocking. New orders from Pfizer will help revive Morepeth operations. We believe growth in the overseas CRAMS business will improve during FY11E. We expect the India-based assets to offset a decline in the international CRAMS business in the near term. We expect margin expansion from Minrad operations due to sales ramp up and better sourcing.

Going ahead, we expect the stock to get re-rated on account of a) future strategy and outlook b) incremental revenue from Minrad c) higher contribution of the CMG business and d) utilisation of cash. Margin improvement will be aided by a) higher realisation at Minrad and b) cost saving on account of closure of the Huddersfield facility.

PHIL is set to receive US\$3.3 billion on NPV value from Abbott and Rs 600 crore from SRL. This works out to Rs 518 per share (post long-term capital gains taxed at 21.5%, book value adjustment and debt repayment of ~Rs 1300 crore). The residual business is valued at Rs 71 (12x FY12E EPS). We have rated PHIL as **BUY** with a target price of Rs 589. With cash utilisation by the management post the deal we expect the stock to get re-rated, going forward.

## ICICIdirect.com Coverage Universe

Alembic					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	ALECHE	<b>CMP</b>	56	<b>FY08</b>	1003.2	8.0	7.0	8.1	32.6	19.1
		<b>Target</b>	41	<b>FY09</b>	1116.1	3.4*	16.8	9.8	14.0*	11.3
<b>MCap</b>	781.6	<b>Upside (%)</b>	-27	<b>FY10</b>	1138.2	3.0	19.1	10.1	11.7	9.7
				<b>FY11E</b>	1223.9	4.1	13.8	8.6	14.5	11.3
Biocon					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	BIOCON	<b>CMP</b>	303	<b>FY09</b>	1608.7	12.0	25.1	20.3	11.4	13.2
		<b>Target</b>	335	<b>FY10</b>	2367.8	14.7	20.7	13.6	12.4	15.6
<b>MCap</b>	6054.0	<b>Upside (%)</b>	11	<b>FY11E</b>	2668.5	17.2	17.6	11.5	13.2	16.7
				<b>FY12E</b>	3039.6	20.4	14.9	9.6	13.9	17.6
Dishman					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	DISHPHA	<b>CMP</b>	217	<b>FY09</b>	1062.4	18.2	11.9	9.3	20.9	13.6
		<b>Target</b>	218	<b>FY10</b>	915.4	14.6	14.9	12.1	15.0	9.1
<b>MCap</b>	1716.4	<b>Upside (%)</b>	1	<b>FY11</b>	1075.3	19.6	11.1	9.2	17.1	11.1
				<b>FY12E</b>	1256.5	21.4	10.1	7.8	16.4	11.9
IPCA Labs					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	IPCLAB	<b>CMP</b>	294	<b>FY09</b>	1283.8	8.1	37.6	4.7	16.0	19.6
		<b>Target</b>	311	<b>FY10</b>	1559.6	16.4	18.4	3.7	23.7	20.5
<b>MCap</b>	3787.5	<b>Upside (%)</b>	6	<b>FY11E</b>	1878.0	19.9	15.2	3.0	23.1	22.5
				<b>FY12E</b>	2237.2	23.9	12.7	2.3	22.4	24.1
Piramal Health					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	NICPIR	<b>CMP</b>	504	<b>FY09</b>	3281.1	15.1	33.3	20.3	24.0	17.7
		<b>Target</b>	589	<b>FY10</b>	3671.1	23.1	21.9	15.9	28.3	18.8
<b>MCap</b>	10530.5	<b>Upside (%)</b>	17	<b>FY11E</b>	4102.8	25.3	19.9	13.7	25.4	20.9
				<b>FY12E</b>	4633.3	30.5	16.5	11.7	25.3	22.7
Sun Pharma					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	SUNPHA	<b>CMP</b>	1744	<b>FY09</b>	4271.4	88.1	19.8	18.6	25.9	28.5
		<b>Target</b>	1644	<b>FY10</b>	4019.8	65.2	26.7	25.2	17.8	19.6
<b>MCap</b>	36128.6	<b>Upside (%)</b>	-6	<b>FY11E</b>	4464.8	71.7	24.3	22.3	16.8	18.8
				<b>FY12E</b>	5151.8	82.2	21.2	18.5	16.7	18.5
Glenmark					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	GLEPHA	<b>CMP</b>	280	<b>FY09</b>	2093.0	7.7	36.5	21.0	19.4	16.4
		<b>Target</b>	325	<b>FY10</b>	2484.9	12.2	23.0	15.0	13.9	14.6
<b>MCap</b>	7542.0	<b>Upside (%)</b>	16	<b>FY11E</b>	2927.1	15.9	17.5	11.6	18.6	17.7
				<b>FY12E</b>	3390.1	21.7	12.9	9.2	20.9	20.3
Lupin					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	LUPIN	<b>CMP</b>	1875	<b>FY08</b>	2706.4	49.8	37.7	37.4	31.9	22.2
		<b>Target</b>	2101	<b>FY09</b>	3775.9	61.3	30.6	25.7	35.6	23.6
<b>MCap</b>	16621.5	<b>Upside (%)</b>	12	<b>FY10</b>	4740.5	78.7	23.8	20.5	33.0	25.8
				<b>FY11E</b>	5930.3	93.0	20.2	15.5	27.2	25.4
				<b>FY12E</b>	6997.7	116.7	16.1	12.0	24.9	24.7
Unichem Labs					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	UNILAB	<b>CMP</b>	489	<b>FY09</b>	735.2	30.0	16.3	12.4	22.3	23.2
		<b>Target</b>	511	<b>FY10</b>	765.5	36.9	13.3	9.5	23.3	25.7
<b>MCap</b>	1763.3	<b>Upside (%)</b>	4	<b>FY11E</b>	905.7	42.1	11.6	7.7	22.4	26.1
				<b>FY12E</b>	1057.8	51.1	9.6	6.2	23.0	26.9
Indoco Remedies					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
<b>Idirect Code</b>	INDREM	<b>CMP</b>	475	<b>FY09</b>	350.6	25.6	18.6	13.2	11.3	10.9
		<b>Target</b>	403	<b>FY10</b>	398.3	34.2	13.9	11.1	13.3	11.1
<b>MCap</b>	583.5	<b>Upside (%)</b>	-15	<b>FY11E</b>	466.1	42.6	11.2	8.3	14.3	13.5
				<b>FY12E</b>	530.6	49.0	9.7	7.2	14.3	13.8

## RATING RATIONALE

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 Buy: Between 10% and 20%;  
 Add: Up to 10%;  
 Reduce: Up to -10%  
 Sell: -10% or more;

**Pankaj Pandey**

**Head – Research**

**pankaj.pandey@icicisecurities.com**

**ICICIdirect.com Research Desk,  
 ICICI Securities Limited,  
 7<sup>th</sup> Floor, Akruti Centre Point,  
 MIDC Main Road, Marol Naka,  
 Andheri (East)  
 Mumbai – 400 093**

**research@icicidirect.com**

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