

## JUBILANT ORGANOSYS

INR 304

On course

BUY



Jubilant Organosys's (Jubilant) 2QFY08 results were slightly above estimates in terms of revenues and in line with our expectations on the EBITDA and net profit fronts. Revenues increased by 32.7% to INR 6,183 mn, EBITDA margins increased from 17.2% to 18.3% Y-o-Y, and net profit increased by 102.2% to INR 1,100 mn. The company's net profit was boosted by other income of INR 385 mn which included forex gain of INR 289 mn on account of outstanding FCCBs. The tax rate of 6.5% for the quarter (compared to 20% expectation for FY08) was also a factor which boosted the net profit.

The pharma and life sciences products (PLSP) business, boosted by Hollister sales, recorded a robust growth of 53.9% Y-o-Y. Industrial and performance polymers (IPP) recorded growth of 10.3% for the quarter. We believe the company will be able to deliver significant growth in PLSP and IPP segments driven by the Hollister acquisition and the Syngenta contract announced recently.

We expect significant growth in the PLSP business (organic and inorganic), coupled with steady growth in industrial products, and performance polymers to help Jubilant achieve a 35% CAGR for EPS from FY07-09E.

We have revised our earnings estimates upwards by 14% for FY09E. At CMP of INR 304, the stock currently trades at a P/E 13.2 on FY09E earnings. We reiterate our 'BUY' recommendation on the stock.

#### \* Pharma division: Vanguard of growth

Pharma and life sciences products (PLSP) contributed ~60% to revenues, which grew ~54% Y-o-Y (including Hollister revenues) for the quarter. Jubilant is focused on drug discovery and development services (DDDS), which will start contributing meaningfully to its total revenues from the latter half of FY08E. Currently, the company has 15 molecules in Phase III, 17 in Phase II, and 23 in Phase I. This will be an important step for Jubilant, as margins in this business are much higher than in any other segment.

In the quarter, PBIT margins of the PLSP business were 20.9%, a decrease of about 180bps compared with 2QFY07. There are some subsidiaries in this segment which are still making losses, but are expected to turnaround by FY09E.

#### Financials

Year to March	Q2FY08	Q2FY07	% change	Q1FY08	% change	FY08E	FY09E
Revenues (INR mn)	6,183	4,659	32.7	5,400	14.5	24,333	29,259
EBITDA (INR mn)	1,133	801	41.4	952	19.0	4,745	5,749
Net profit (INR mn)	1,100	544	102.2	1,429	(23.0)	4,434	4,218
EPS (INR)	6.1	3.8	59.9	7.9	(23.0)	24.2	23.0
P/E (x)						12.5	13.2
EV/EBITDA (x)						14.4	11.6

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Reuters : JUBO.BO  
Bloomberg : JOL IN

#### Market Data

52-week range (INR) : 364 / 209  
Share in issue (mn) : 143.4  
M cap (INR bn/USD mn) : 43.8 / 1,108.3  
Avg. Daily Vol. BSE/NSE ('000) : 64.7

#### Share Holding Pattern (%)

Promoters : 51.9  
MFs, Fls & Banks : 2.4  
Fls : 28.1  
Others : 17.6

Table 1: Revenue break-up

(INR mn)	Q208	Q207	Y-o-Y Change (%)	Q108	Q-o-Q Change (%)	FY07	FY06	Y-o-Y Change (%)
<b>Revenues</b>								
Pharma & Lifescience products	3,682.0	2,392.0	53.9	3,113.0	18.3	9,226.0	6,773.0	36.2
<i>% of total sales</i>	59.6	51.3		57.6		51.0	45.2	
Industrial products	2,501.0	2,267.0	10.3	2,287.0	9.4	8,871.0	8,217.0	8.0
<i>% of total sales</i>	40.4	48.7		42.4		49.0	54.8	
<b>Total revenues</b>	<b>6,183</b>	<b>4,659</b>	<b>32.7</b>	<b>5,400</b>	<b>14.5</b>	<b>18,097</b>	<b>14,990</b>	<b>20.7</b>
<b>PBIT</b>								
Pharma & Lifescience products	771.0	543.0	42.0	646.0	19.3	1,797.0	1,261.0	42.5
<i>% PBIT margin</i>	20.9	22.7		20.8		19.5	18.6	
<i>% of Total PBIT</i>	62.0	71.2		66.1		63.5	62.6	
Industrial products	472.0	220.0	114.5	331.0	42.6	1,033.0	753.0	37.2
<i>% PBIT margin</i>	18.9	9.7		14.5		11.6	9.2	
<i>% of Total PBIT</i>	38.0	28.8		33.9		36.5	37.4	
<b>Total PBIT</b>	<b>1,243</b>	<b>763</b>	<b>62.9</b>	<b>977.0</b>	<b>27.2</b>	<b>2,830</b>	<b>2,014</b>	<b>40.5</b>
<i>% PBIT Margin</i>	20.1	16.4		18.1		15.6	13.4	

Source: Company

**\* Industrial products and performance polymers: Stable growth expected**

Growth in the industrial products and polymers division, which contributed ~40% to revenues, was at 10.3% Y-o-Y for the quarter. We expect these segments to have a steady growth of ~10% for the next two years. Improved pricing environment and a reduction in raw material prices resulted in a significant PBIT margin of 18.9% compared to 9.7% in the corresponding quarter of the previous year.

**\* Hollister acquisition: Improved performance leading to better margins**

The company acquired Hollister in the US for USD 122.5 mn. Hollister had revenues of USD 55 mn and EBITDA of USD 10.9 mn in CY06. Jubilant is planning additional capex of USD 40 mn in the acquired entity for increasing its capacity.

Hollister has contributed ~ INR 1,050 mn to the topline in the past four months. In the second quarter, Hollister recorded revenues of ~ INR 770 mn. We expect a similar run rate in H2FY07. This quarter, inclusion of Hollister numbers resulted in an in gross margin improvement which was offset by a significant increase in salaries and wage costs.

On a longer term, we believe this acquisition is an important step for Jubilant to move up the value chain and be present across various stages of the product lifecycle.

**\* Jubilant First Trust Healthcare: INR 1,700 mn capex over two years**

The company has entered in the healthcare business, in which it plans to make capital expenditure of ~ INR 1,700 mn over the next two years to reach a capacity of around 1,000 beds. We believe the company will be looking for inorganic growth opportunities in this segment.

\* **Financials: Steady performance**

Consolidated revenues, including one month revenues of Hollister, rose to INR 6,183 mn, growing at 32.7% Y-o-Y. The company reported an 'other income' of INR 385 mn which included exchange gains from FCCBs of INR 289 mn. The EBITDA margin of 18.3% reflects the incrementally increasing contribution of the PLSP franchise, which was higher by 110bps Y-o-Y. Tax rate of 6.5% for the quarter boosted the net margin for the quarter. The company has guided an annual tax rate of ~12% for FY08. Net profit, at INR 1,100 mn, was 102% higher Y-o-Y. Adjusted net profit, independent of gains on foreign currency borrowings of INR 289 mn, rose to INR 811 mn, 4% above our expectation.

\* **Outlook and valuations**

The company has retained the revenue growth guidance of 35% for FY08. We expect revenues to grow at a CAGR of ~27% for (FY07E-09E). We believe that Jubilant will be able to show continuous growth, driven by its PLSP business. Some positive triggers on the API business could provide upsides to our estimates.

With Hollister's acquisition, we believe Jubilant will be able to deliver better margins going forward. Besides this, increased revenues from the contract research segment are also likely to boost the company's margins.

We expect better CRAMS performance, new API products launches, and integration of Hollister to drive Jubilant's growth. We believe the company is likely to deliver EPS CAGR of 35% from FY07-09E. At CMP of INR 304, the stock currently trades at P/E of 13.2x on our FY09E earnings. We maintain our **'BUY'** recommendation.

Financial snapshot								(INR mn)
Year to March	Q2FY08	Q2FY07	Growth (%)	Q1FY08	Growth (%)	FY07	FY08E	FY09E
<b>Total operating income</b>	6,183	4,659	32.7	5,400	14.5	18,097	24,333	29,259
Total expenses	5,050	3,858	30.9	4,448	13.5	14,902	19,588	23,510
Cost of goods sold	2,450	2,184	12.2	2,571	(4.7)	8,836	10,585	12,655
Raw material cost (including adj. to stock)	2,189	1,944	12.6	2,433	(10.0)	7,908	10,585	12,655
Purchase of traded goods	117	97	20.6	-		928	-	-
Gross profit	3,733	2,475	50.8	2,829	32.0	9,261	13,748	16,605
Other expenses	2,744	1,817	51.0	2,015	36.2	6,066	9,003	10,855
Stores and spares consumed	466	283	64.7	312	49.4	1,133	1,460	1,756
Power and fuel	397	347	14.4	348	14.1	1,305	1,582	1,902
Salaries, wages, other payments	1,029	545	88.8	694	48.3	2,149	3,966	4,828
Selling, admin and general expenses	706	504	40.1	547	29.1	1,479	1,995	2,370
Other exp	146	138	5.8	114	28.1	-	-	-
EBITDA	1,133	801	41.4	952	19.0	3,195	4,745	5,749
Other income	385	145	165.5	996	(61.3)	576	1,582	396
PBDIT	1,518	946	60.5	1,948	(22.1)	3,771	6,327	6,145
Depreciation	237	153	54.9	194	22.2	623	872	1,067
Interest	109	37	194.6	84	29.8	195	387	258
PBT	1,172	756	55.0	1,670	(29.8)	2,953	5,067	4,820
Tax (including deferred tax)	76	215	(64.7)	273	(72.2)	712	633	603
PAT	1,096	541	102.6	1,397	(21.5)	2,241	4,434	4,218
Minority interest	(4)	(3)		(32)		(39)	-	-
Net profit for eq	1,100	544	102.2	1,429	(23.0)	2,280	4,434	4,218
Equity capital (FV INR 1)	144	143		144		181	181	181
Dividend per share (INR)						-	2.0	2.0
Number of shares	181	143		181		181	183	183
EPS (INR)	6.1	3.8	59.9	7.9	(23.0)	12.6	24.2	23.0
PE (x)						24.2	12.5	13.2
EV/EBITDA (x)						19.7	14.4	11.6
M. Cap/Revenues (x)						3.0	2.3	1.9
<b>as % of net revenues</b>								
Other income	6.2	3.1		18.4		0.5	0.5	0.5
Total expenses	81.7	82.8		82.4		82.3	80.5	80.4
Depreciation	3.8	3.3		3.6		3.4	3.6	3.6
Gross profit	60.3	53.2		52.8		51.2	56.5	56.8
EBITDA	18.3	17.2		17.6		17.7	19.5	19.7
Net profit	17.8	11.7		26.5		12.6	18.2	14.4
Tax rate	6.5	28.4		16.3		28.6	12.5	12.5

## Company Description

Jubilant, an integrated CRAMS player has revenues flowing from pharma and life science products (~60% revenues) and the rest from the industrial chemicals and performance polymers division. It has its own generic business, wherein it has capabilities to sell its own APIs and some formulations. The company also has presence in the contract research space through its subsidiaries - Biosys, Chemsys, and Clinsys. It has recently decided to venture into the healthcare segment by setting up hospitals in West Bengal.

## Investment Theme

Jubilant has strong presence in acetlys and pyridines, enabling high degree of integration in its business model. This helps the company offer its services at much lower costs than some of its competitors. The PLSP business' contribution to total revenues is expected to increase to 60% by FY08E, which will help the company improve overall margins. Over the next few years, Jubilant is expected to launch some new products in its API and formulations businesses, which will help the PLSP division post higher growth rate. Moreover, some of its subsidiaries and acquisitions, which are dragging down the company's margins, are expected to turnaround in the next two years. Hollister, a recently acquired contract manufacturer of sterile injectables, in our view, will be an important growth driver for the company going forward.

## Key Risks

- Molasses account for 70% of Jubilant's raw material cost, hence, any adverse movement in molasses prices will offset Jubilant's gross margins.
- Integrating all the acquired entities and deriving synergies out of these inorganic growth initiatives could be a challenge.
- If the pricing pressure in APIs is higher-than-expected, it will affect Jubilant's margins adversely.

## Financials Statements

<b>Income statement</b>					<b>(INR Mn)</b>
<b>Year to March</b>	<b>FY05</b>	<b>FY06</b>	<b>FY07</b>	<b>FY08E</b>	<b>FY09E</b>
Income from operations	11,703	14,990	18,097	24,333	29,259
Gross sales	12,737	16,179	19,434	24,333	29,259
Less: excise	1,034	1,189	1,337	-	-
Net sales	11,703	14,990	18,097	24,333	29,259
Total operating expenses	9,627	12,820	14,902	19,588	23,510
Materials cost	5,943	7,854	8,836	10,585	12,655
Employee cost	807	1,360	2,149	3,966	4,828
S,G&A	1,247	1,684	1,479	1,995	2,370
Other expenses	1,630	1,922	2,438	3,042	3,657
EBITDA	2,076	2,170	3,195	4,745	5,749
Other income	166	197	576	1,582	396
Depreciation and amortisation	381	513	623	872	1,067
Interest	220	173	195	387	258
Profit before tax	1,641	1,681	2,953	5,067	4,820
Provision for tax	431	392	712	633	603
PAT (inc. pre minority interests)	1,210	1,289	2,241	4,434	4,218
Minority interest & others	18	(8)	(39)	-	-
PAT for equity shareholders	1,192	1,297	2,280	4,434	4,218
Shares outstanding (mn)	129.6	142.5	181.3	183.0	183.0
Dividend per share (INR)	1.2	1.3	0.0	2.0	2.0
Dividend payout (%)	13.6	13.7	-	8.3	8.7

### Common size metrics- as % of net revenues

<b>Year to March</b>	<b>FY05</b>	<b>FY06</b>	<b>FY07</b>	<b>FY08E</b>	<b>FY09E</b>
Material cost	50.8	52.4	48.8	43.5	43.3
Employee cost	6.9	9.1	11.9	16.3	16.5
Other expenses	13.9	12.8	13.5	12.5	12.5
Depreciation	3.3	3.4	3.4	3.6	3.6
Interest expenditure	1.9	1.2	1.1	1.6	0.9
EBITDA margins	17.7	14.5	17.7	19.5	19.7
Net profit margins	10.2	8.7	12.6	18.2	14.4

### Growth metrics (%)

<b>Year to March</b>	<b>FY05</b>	<b>FY06</b>	<b>FY07</b>	<b>FY08E</b>	<b>FY09E</b>
Revenues	36.2	28.1	20.7	34.5	20.2
EBITDA	33.9	4.5	47.2	48.5	21.2
Net profit	52.4	8.8	75.8	94.5	(4.9)
EPS	37.9	(1.1)	38.2	92.6	(4.9)

<b>Balance sheet</b>					<b>(INR Mn)</b>
<b>As on 31st March</b>	<b>FY05</b>	<b>FY06</b>	<b>FY07</b>	<b>FY08E</b>	<b>FY09E</b>
Shareholders funds	5,045	8,257	9,061	14,414	19,513
Capital	130	142	144	181	181
Reserves & surplus	4,915	8,115	8,918	14,233	19,331
Borrowings	3,719	7,220	16,526	20,096	13,216
Secured loans	2,056	3,345	4,172	7,742	862
Unsecured loans	1,663	3,875	12,354	12,354	12,354
Deferred tax liability (net)	858	1,042	1,360	900	900
Minority interest	51	151	174	-	-
Other term liabilities	-	-	-	300	300
<b>Sources of funds</b>	<b>9,672</b>	<b>16,670</b>	<b>27,122</b>	<b>35,710</b>	<b>33,929</b>
Gross block	9,443	14,020	16,671	22,096	25,306
Depreciation	3,151	3,779	4,392	5,265	6,331
Net block	6,292	10,242	12,279	16,832	18,975
Capital work in progress	977	1,290	2,357	-	-
Investments	2	2	39	3,900	3,900
Inventories	1,937	3,117	3,532	4,759	5,508
Sundry debtors	1,765	2,479	2,948	4,333	5,211
Cash and bank balances	376	1,390	8,749	7,460	1,870
Loans and advances	1,220	1,963	2,425	2,433	2,926
Total current assets	5,298	8,949	17,654	18,985	15,514
Current liabilities	2,223	2,693	2,918	3,121	3,575
Provisions	730	1,152	2,330	886	886
Total current liabilities and provisions	2,953	3,844	5,248	4,007	4,461
Net current assets	2,346	5,105	12,406	14,978	11,054
Others	56	32	41	-	-
<b>Uses of funds</b>	<b>9,672</b>	<b>16,670</b>	<b>27,122</b>	<b>35,710</b>	<b>33,929</b>
Book value per share (INR)	39	58	50	79	107

<b>Cash flow statement</b>					<b>(INR Mn)</b>
<b>Year to March</b>	<b>FY05</b>	<b>FY06</b>	<b>FY07</b>	<b>FY08E</b>	<b>FY09E</b>
Cash flow from operations	1,503	1,925	2,894	5,306	5,284
Cash for working capital	(81)	(1,745)	58	(3,861)	(1,665)
Net operating cash flow	1,423	179	2,952	1,445	3,619
Net purchase of fixed assets	2,630	4,890	3,718	3,068	3,210
Net purchase of investments	(80)	(207)	(273)	4,280	-
Net cash flow from investing	(2,550)	(4,683)	(3,445)	(7,349)	(3,210)
Proceeds from equity capital	1,264	5,417	7,830	4,488	(5,999)
Proceeds from LTB/STB	11	100	23	126	-
Net cash flow from financing	1,275	5,517	7,853	4,614	(5,999)
<b>Free cash flow</b>	<b>(1,027)</b>	<b>(4,586)</b>	<b>(799)</b>	<b>(1,284)</b>	<b>635</b>

**Ratios**

Year to March	FY05	FY06	FY07	FY08E	FY09E
ROE (%)	23.6	15.7	25.2	30.8	21.6
ROCE (%)	19.2	11.1	11.6	15.3	15.0
Inventory days	111.7	132.6	153.5	143.0	148.1
Debtors days	49.7	51.7	54.7	54.6	59.5
Fixed assets T/o (x)	1.4	1.3	1.2	1.3	1.2
Debt/equity	0.7	0.9	1.8	1.4	0.7

**Valuation parameters**

Year to March	FY05	FY06	FY07	FY08E	FY09E
EPS (INR.)	9.2	9.1	12.6	24.2	23.0
<i>Y-o-Y growth (%)</i>	37.9	(1.1)	38.2	92.6	(4.9)
CEPS (INR)	12.1	12.7	16.0	29.0	28.9
P/E (x)	33.0	33.4	24.2	12.5	13.2
Price/BV(x)	7.8	5.2	6.1	3.9	2.9
EV/Sales (x)	3.7	3.3	3.5	2.8	2.3
EV/EBITDA (x)	20.6	22.7	19.7	14.4	11.6



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**Coverage group(s) of stocks by primary analyst(s): Pharmaceuticals:**

Aurobindo Pharma, Cadila Healthcare, Cipla, Dishman Pharmaceuticals and Chemicals, Dr.Reddy's Laboratories, Glaxosmithkline Pharmaceuticals, Glenmark, Ipca Laboratories, Jubilant Organosys, Lupin, Nicholas Piramal India, Ranbaxy Laboratories, Sun Pharmaceuticals Industries, Torrent Pharmaceuticals and United Phosphorus.

**Jubilant Organosys**



**Recent Research**

Date	Company	Title	Price (INR)	Recos
11-Oct-07	Pharma	Fact Sheet		
17-Sep-07	Pharma	Fact Sheet		
03-Sep-07	Nicholas Piramal	Unlocking value...; Event Update	288	Buy
03-Sep-07	Aurobindo Pharma	In fine fettle; Visit Note	619	Buy

**Distribution of Ratings / Market Cap**

**Edelweiss Research Coverage Universe**

	Buy	Accumulate	Reduce	Sell	Total
Rating Distribution*	101	44	24	6	183

\* 6 stocks under review / 2 rating withheld

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	86	66	31

**Rating Interpretation**

Rating	Expected to
Buy	appreciate more than 20% over a 12-month period
Accumulate	appreciate up to 20% over a 12-month period
Reduce	depreciate up to 10% over a 12-month period
Sell	depreciate more than 10% over a 12-month period

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