



MOTILAL OSWAL

*Initiating Coverage*  
SECTOR: PHARMACEUTICALS

# Dishman Pharma



Striking it right

**Contents**

---

	<b>Page No.</b>
<b>Investment case .....</b>	<b>4-15</b>
<b>Preferred supplier for Solvay .....</b>	<b>4</b>
<b>Carbogen AMCIS (CA) acquisition .....</b>	<b>7</b>
<b>Other businesses .....</b>	<b>13</b>
<b>Proposed capex programs .....</b>	<b>15</b>
<b>Valuation and outlook .....</b>	<b>16-18</b>
<b>Financial statements .....</b>	<b>19-22</b>

---

## Dishman Pharma

STOCK INFO.	BLOOMBERG DISH IN
BSE Sensex: 13,607	REUTERS CODE DISH.BO
S&P CNX: 3,985	

17 April 2007

Buy

Initiating Coverage

Rs226

Y/E MARCH	2006	2007E	2008E	2009E
Sales (Rs m)	2,760	5,534	8,513	9,552
EBITDA (Rs m)	633	1,451	2,292	2,604
Adj. NP (Rs m)	475	847	1,273	1,476
Adj. EPS (Rs)	5.8	10.3	15.5	18.0
EPS Growth (%)	20.4	77.6	50.3	16.0
BV/Share (Rs)	27.3	44.0	59.5	77.5
P/E (x)	39.0	21.9	14.6	12.6
P/BV (x)	8.3	5.2	3.8	2.9
EV/EBITDA (x)	32.2	16.1	10.8	9.2
EV/Sales (x)	7.4	4.2	2.9	2.5
RoE (%)	28.5	33.5	34.1	29.8
RoCE (%)	14.5	17.7	19.6	18.6

## KEY FINANCIALS

Shares Outstanding (m)	81.6
Market Cap. (Rs b)	18.5
Market Cap. (US\$ b)	0.4
Past 3 yrs. Sales Growth (%)	33.4
Past 3 yrs. NP Growth (%)	43.9
Dividend Payout (%)	11.7
Dividend Yield (%)	0.3

## STOCK DATA

52-Week Range	273/132
Major Shareholders (as of March 2007)	%
Promoters	67.8
Domestic Institutions	14.0
FII/FDIs	12.3
Others	5.9
Average Daily Turnover	
Volume ('000 shares)	137.8
Value (Rs million)	30.3
1/6/12 Month Rel. Performance (%)	4/7/-7
1/6/12 Month Abs. Performance (%)	13/12/11

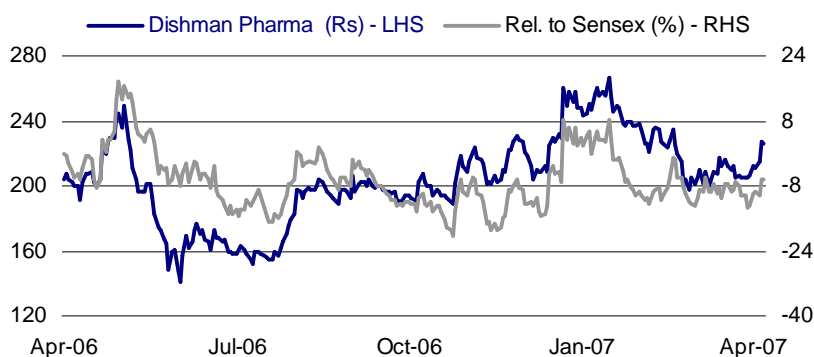
**Moving upscale from chemicals to CRAMS:** Dishman is transitioning from a chemicals supplier to a full fledged CRAMS player. Signing of new CRAMS contracts and the Carbogen-AMCIS (CA) acquisition will enable the company to increase its CRAMS contribution from 53% of sales in FY06 to about 80% by FY08E resulting in a 430bp increase in EBITDA margins between FY06-09.

**Key step forward — the CA acquisition:** The CA acquisition has, in one stroke, enhanced Dishman's capabilities across the complete range of services spanning the CRAMS value chain. Further, it has opened the doorway for access to high potency capabilities and a significant number of new client relationships, besides doubling Dishman's revenues. CA is expected to grow at a CAGR of about 15-18% in CY07E and CY08E.

**Customer base being expanded:** Partnerships with large innovators like GSK, Merck, Astra Zeneca, J&J and Novartis imply good long-term potential for the CRAMS business, resulting in 25% revenue CAGR (excl. CA) for FY06-09.

**Likely to benefit from increased out-sourcing from India:** Dishman is likely to be one of the key beneficiaries of the increased outsourcing from India, resulting in 32% earnings CAGR over FY07-FY09. The stock is currently valued at 14.6x FY08E and 12.6x FY09E consolidated earnings. RoE is estimated at between 30-34% and RoCE in the 18-20% range over FY07-FY09. We initiate coverage with a **Buy** with a price target of Rs270 (15x FY09E earnings) implying an upside of 19.5%.

## STOCK PERFORMANCE (1 YEAR)



## Investment case

Dishman Pharmaceuticals & Chemicals Ltd. (Dishman) is set to emerge as India's leading contract manufacturing organization for pharmaceutical intermediates and actives. The company is integrating forward from being a pure chemicals company to the pharmaceuticals business. Besides being value accretive, this trend allows Dishman to gain improved realizations in select drug segments. To take this initiative forward, Dishman acquired Carbogen AMCIS AG (CA), a Swiss research-based company with three production facilities in Switzerland for manufacture of high-potent, high-value products from Solutia Europe.

It has also enhanced its capabilities from being just a manufacturer to one of being a Contract Research & Manufacturing Services (CRAMS) player offering the complete range of services in the CRAMS value chain. Dishman has been able to achieve this by signing up a higher number of API supply contracts and via acquisition of Carbogen AMCIS (CA). This acquisition has transformed Dishman's business mix and has filled a large gap in its CRAMS offering.

*The following are key valuation triggers ahead*

In this scenario, the key triggers that will determine Dishman's valuations ahead include:

1. Scale up in the Solvay contract
2. Successful execution of other contracts
3. Scale up in Carbogen's capacity utilization
4. Integration of Carbogen AMCIS-Dishman operations to take advantage of inherent synergies

### **Preferred supplier for Solvay**

*Dishman is currently a key supplier to Solvay*

#### **Solvay's EM supplies will get a boost going forward**

Dishman is currently a key supplier of Eprosartan Mesylate API (anti-hypertensive) to Solvay, which markets it under the brand, Teveten. Solvay sources this product from two of its key suppliers – Dishman & Lonza. Dishman also supplies some intermediates of Eprosartan Mesylate to Solvay, but in negligible amounts. The Solvay contract is valid until 2008 and extendable annually thereafter. However, the patent for Eprosartan Mesylate (EM) is valid until 2013.

Solvay also commenced selling Teveten Plus some years ago. Teveten Plus is a combination of 600mg Eprosartan and 12.5mg Hydrochlorothiazide — a diuretic that contributes to a stronger blood pressure lowering activity. Teveten Plus is used to treat hard-to-control hypertension, particularly systolic hypertension.

**US FDA inspection of Dishman's new facility to boost EM sales:** The US FDA has recently successfully completed inspection of Dishman's facility located at Bavla in Gujarat. This is a 100% EOU, set up to exclusively manufacture EM for being supplied to Solvay. By implication, this would mean that Solvay will source its EM requirement for the US markets from Dishman.

Currently Solvay sources about 50% of its EM requirement from Dishman. The latter has expanded its capacity at the Bavla facility from 60 tpa to 200 tpa in order to meet the increased offtake from Solvay. On the back of the potentially higher volume offtake ahead, we expect EM supplies to Solvay to generate about Rs940m of revenues (up 34% YoY) for Dishman in FY07E. Supplies are expected to stabilize at ~Rs1.5b by FY09E, resulting in a 33% revenue CAGR for FY06-09.

### Looking beyond Solvay – other contracts to ramp up in coming years

*Expect gradual ramp-up in other contracts*

Currently, Solvay is Dishman's major client contributing close to 17% of Dishman's total sales and about 23% of its CRAMS revenues. To reduce its dependence on a single customer, Dishman has entered into supply arrangements with several other MNCs for both on-patent as well off-patent supplies of APIs and intermediates.

The company is currently working on various projects for MNCs such as Astra Zeneca, Merck, GlaxoSmithKline, J&J and Sepracor among others. Some of these supplies are likely to gain visibility in FY08E. The table below indicates Dishman's relationships with some of these MNCs.

#### DISHMAN – CRAMS RELATIONSHIPS

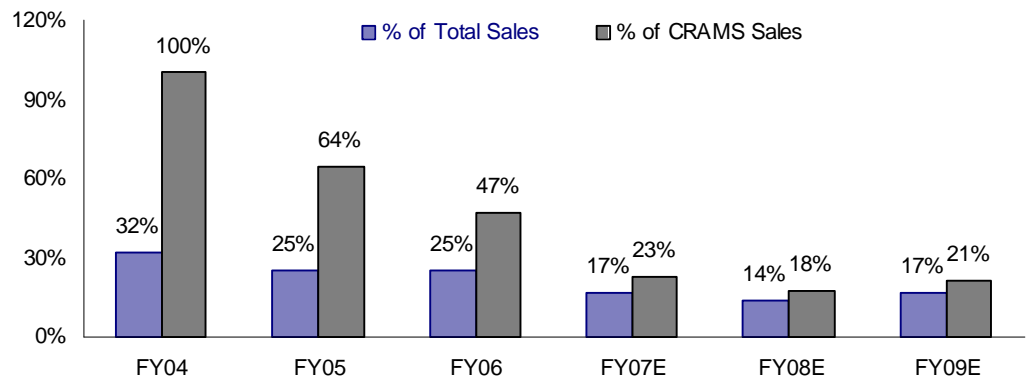
COMPANY	RELATIONSHIP
Solvay	Supply of EM & intermediates. Working on more products
GSK	Currently working on 3 products for which API manufacturing will be transferred to Dishman over next two years
AstraZeneca	Currently supplying Nexium intermediate. Will supply one API through a JV. Also negotiating from 3 more API contracts
Merck	Has supplied Omeprazole intermediate in the past. Currently supplying an anti-hypertensive precursor to one of Merck's suppliers
J&J	CCS supplies
Sepracor	Currently working on 5 chiral products. Ramp-up expected in FY09/FY10
Novartis	CCS supplies
Eli Lilly	CCS supplies
Genzyme	CCS supplies

*Source: Company/ Motilal Oswal Securities*

*CA acquisition, more supply contracts with MNCs, to lower the Solvay dependency*

**Dependence on Solvay has reduced considerably:** The signing of more supply contracts with various multinational companies as well as the CA acquisition have reduced Dishman's dependence on Solvay to a great extent. The latter accounted for about 32% of Dishman's total revenues and 100% of its CRAMS revenues in FY04. This proportion is now expected to come down to about 17% and 23% respectively for FY07E. Given the strong relationship with Solvay, we expect the latter's contribution to range between 15-20% of Dishman's total sales in forthcoming years.

DISHMAN – SOLVAY CONTRIBUTION



Source: Company/Motilal Oswal Securities

*Increasing focus on contract research*

### Contract research – closing gaps in the CRAMS value chain

Dishman has begun to focus on the contract research segment with a view to develop a capability so that it may offer a complete range of services across the CRAMS value chain. A new R&D center was commissioned some time ago, which will focus on contract research, new product development, development of 'potent' molecules and development of future generics and preparation of drug master files. Dishman is currently working on many FTE and CCS contracts for various MNCs (e.g. Novartis, Eli Lilly, J&J etc.). This center will have about 200 scientists working on various projects.

### Carbogen AMCIS (CA) acquisition – Key thrust forward in the CRAMS space

Dishman acquired the pharmaceutical services business of Solutia (i.e. Carbogen-AMCIS, CA, in Switzerland) for US\$74.5m (~ 0.7x EV/Sales and 4x EV/EBITDA based on CY06 financials). The acquisition was funded by a combination of FCCB issue (US\$50m), internal accrual and debt. Being effective from mid-August 2006, the acquisition will only partly contribute to Dishman's revenues for FY07E.

### CA has a long standing track record of CRAMS servicing

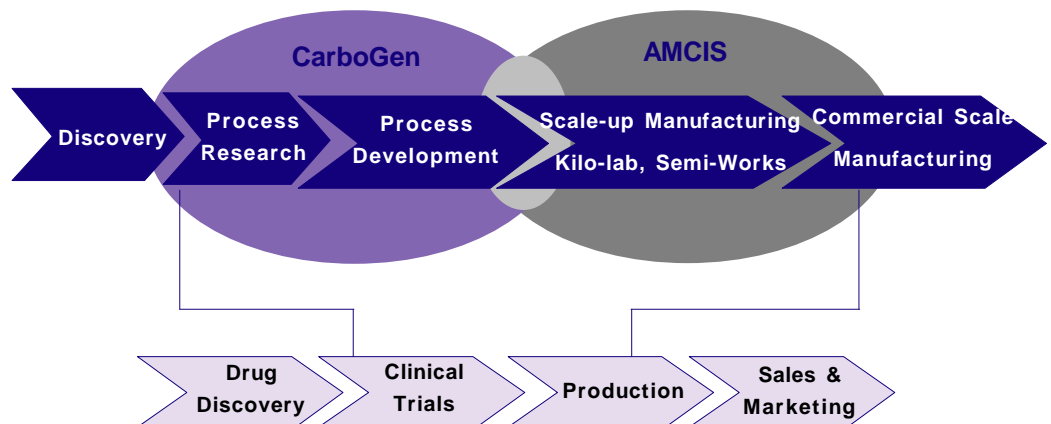
*Post CA acquisition, combined entity equipped to serve the entire drug lifecycle of 15-20 years*

CA is a pharmaceutical services provider, offering a broad portfolio of drug development and commercialization services to the pharmaceutical and biopharmaceutical industries at all stages of drug development since 1982. CA has a customer base comprising mid-sized pharmaceutical and biopharmaceutical companies as well as the large MNCs. It enjoys business relationships with 7 of 10 pharmaceutical majors with 75% of its revenues accruing from the USA. Owing to its strong CRAMS capabilities (discussed below), CA has been able to retain most of its customers despite the restructuring undertaken by its parent (Solutia). In fact, around 90% of its 2005 revenue was generated from repeat customers. The operations of Carbogen and AMCIS were merged last year to constitute CA. Carbogen's specialty is handling contract research projects, whereas AMCIS has a repertoire of seven APIs under long term contract manufacturing (at its USFDA and Swiss medic approved facility). The combined entity has the capability of serving the entire drug life cycle of 15-20 years.

*CA has conferred a new dimension to Dishman's CRAMS offering*

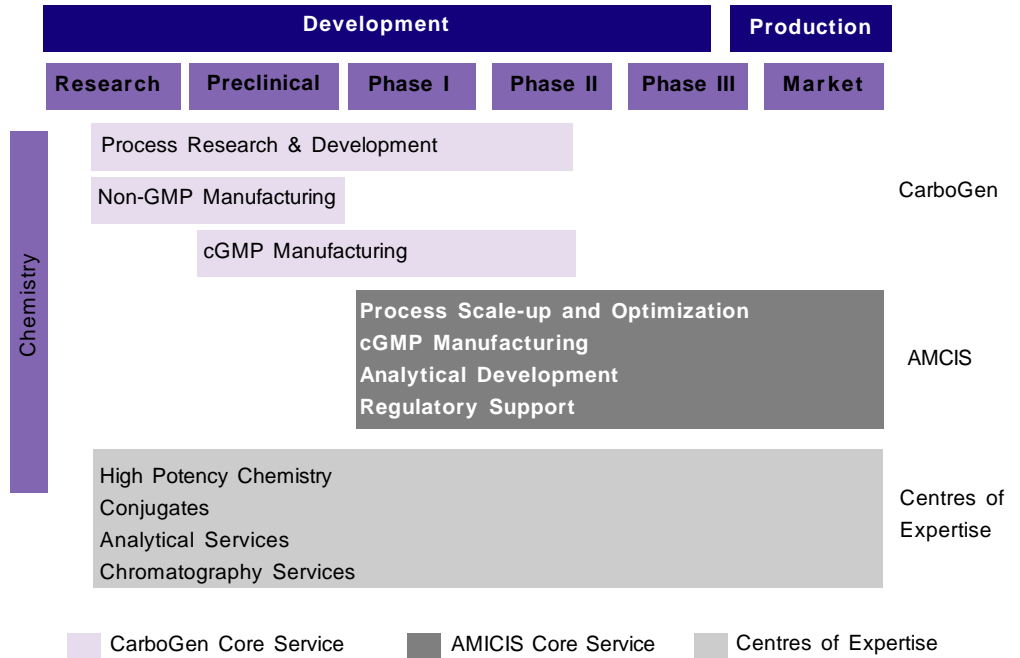
Dishman expects to drive synergies with CA by expanding the combined product basket and renewing its focus on key accounts. Dishman will be able to improve CA's profitability by outsourcing development of intermediates to India and leveraging on Dishman's marketing support for Asia Pacific etc. This acquisition has completely transformed the business mix of Dishman by giving Dishman's CRAMS offering a new dimension.

CARBOGEN-AMCIS - CRAMS PRESENCE



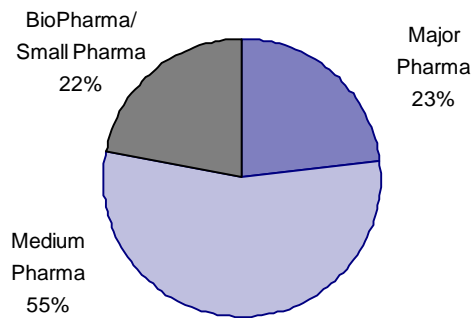
Source: Company/Motilal Oswal Securities

CA – SANPSHOT OF CAPABILITIES

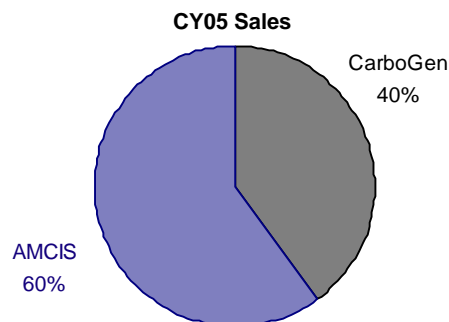


Source: Company/Motilal Oswal Securities

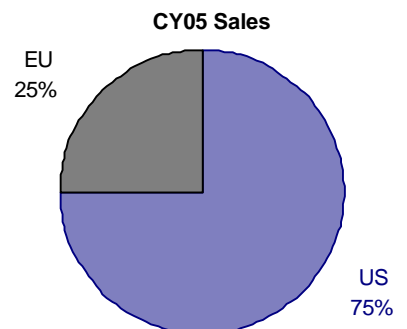
CA – SNAPSHOT OF OPERATIONS (2005)



REVENUE BREAKUP (CARBOGEN & AMCIS)



GEOGRAPHICAL BREAKUP (US & EU)



Source: Company/Motilal Oswal Securities



### **High potency capability to augur well, long term**

Globally, pharmaceutical research trends are shifting in the direction of developing more receptor-specific drugs to improve drug efficacy. Typical examples include drugs in the oncology and hormone related segments. It is estimated that currently about 25% of the NCEs in various stages of development can be categorized in the 'Highly Potent' category. This figure is likely to increase significantly over the next 4-5 years to about 50%, as more drugs are added to this category. High potency drugs are likely to need high containment environment for manufacturing, implying higher capital cost for such drugs. However, the highly concentrated nature of the drug necessitates low volume requirements (a few kilograms only for clinical quantities), making in-house investment uneconomic for innovators. Innovators' need for access to high potency capability opens up a significant opportunity for CRAMS players, in whom the former can take recourse to fill the lacuna in their service requirement.

Small/mid-sized pharmaceutical and biotech companies are gaining traction in the NCE research space due to their focused approach and specific technical skills. Given their size and availability of resources, these companies are unlikely to invest in high potency manufacturing units, giving rise to compulsory outsourcing of such activities. Hence, having access to a high potency facility has become imperative for CRAMS players to service their clients.

### **CA can offer complete solutions for high potency drugs**

*CA capable of offering the complete range of services for high potency drugs*

With the help of the facilities at both Carbogen and AMCIS, CA will be able to offer the complete range of services (from pre-clinical to commercialization stage) for high potency drugs. While Carbogen has the capability to meet a customer's requirement for the pre-clinical to Phase II trials stage, AMCIS has the capability to scale up the manufacturing process from Phase III to the commercialization stage. We believe that CA currently has many customers for which it has undertaken high potency drug development (details undisclosed); this is likely to augur well for the company in the coming years.

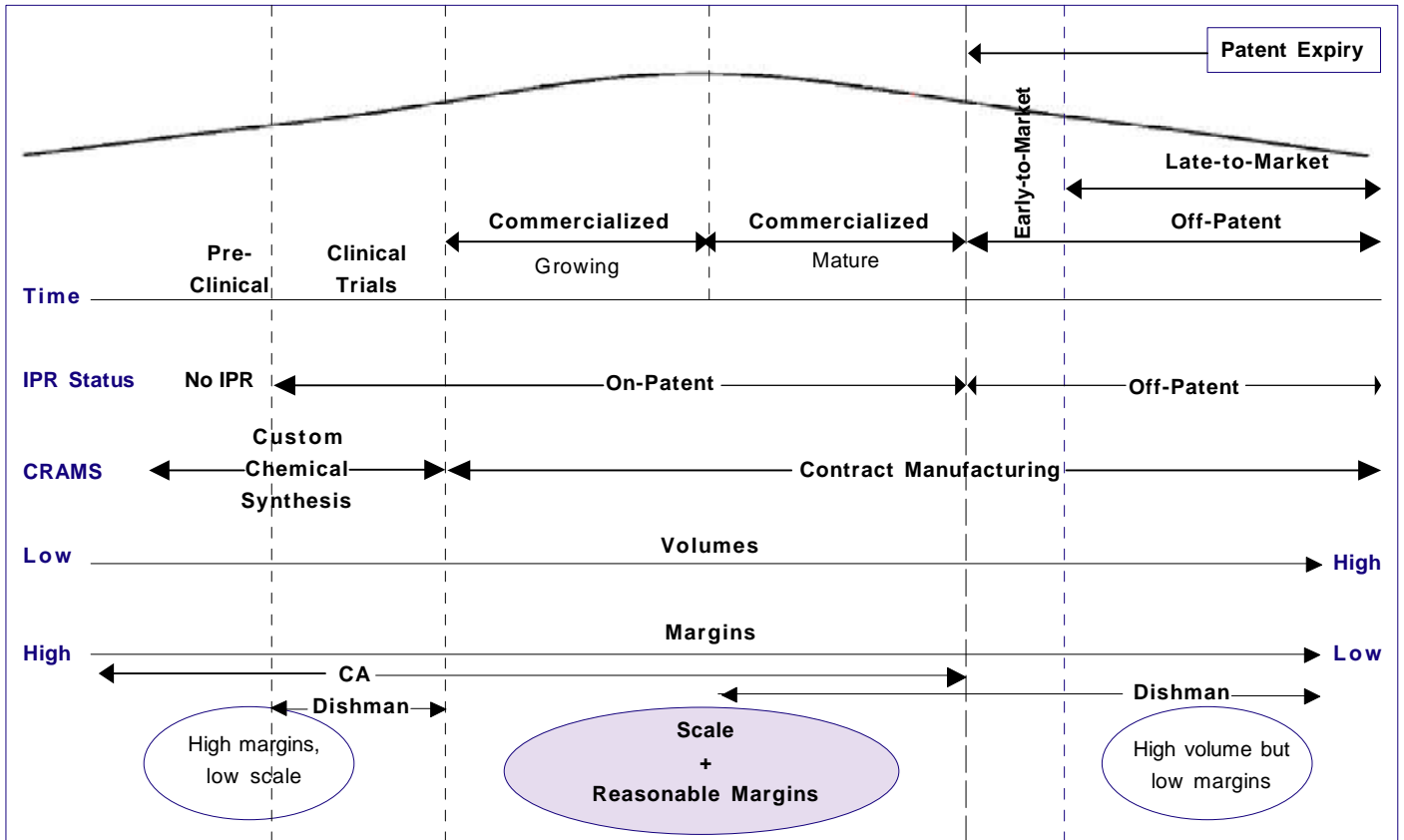
### **CA-Dishman tie-up will offer services across the CRAMS value chain**

The integrated operations of CA and Dishman will enable the combined entity to offer a complete range of services across the entire CRAMS value chain from the clinical testing stage to the manufacturing stage.

*Dishman to enhance CA's prospects on the back of synergies between them*

Dishman will enhance CA's business prospects by driving synergies between the two companies. Jointly, the Indian and Swiss businesses can serve the entire drug life cycle of 15-20 years — expanding the product range and renewing the focus on key accounts will enhance the scale of operations. Dishman also expects to leverage its operational efficiency in India to improve margins in the Swiss operations. This acquisition will boost Dishman's contract manufacturing business from Carbogen's customers and will thrust Dishman into a league whereby it will now be one of the few contract manufacturing organizations in India with high potency manufacturing capability.

CRAMS VALUE CHAIN (SHOW POSITIONING OF CA & DISHMAN)



Source: Company/Motilal Oswal Securities

**CA operations gradually ramping up**

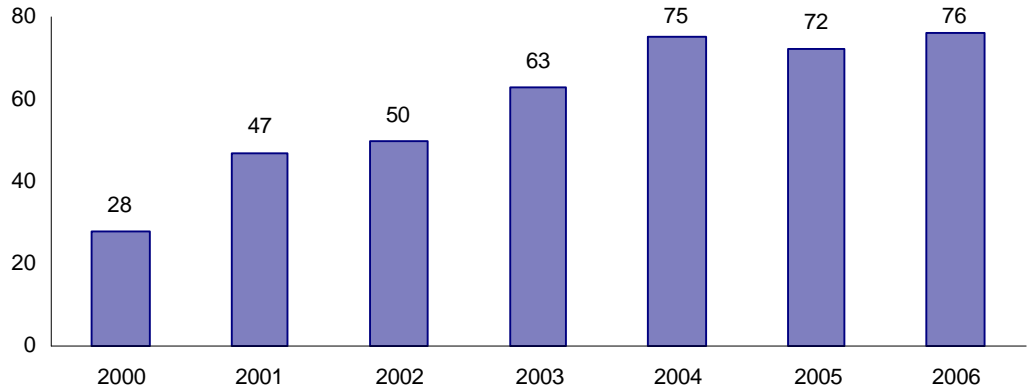
CA’s revenues have been ramping up gradually over the past four years, led mainly by addition of new clients as well as increased traction from existing clients. It has recently renewed orders worth 96% of total sales. While Carbogen has received some new orders recently (details not disclosed), AMCIS has renewed orders worth CHF30m with contracts valid up to 2011.

**Carbogen’s facilities are underutilized, AMCIS operating at full capacity**

Carbogen currently has a pipeline of 40 projects in clinical trials (25 in phase-I, 9 in phase-II and 6 in phase-III). On an average, Carbogen handles about 300-400 projects every year (incl. pre-clinical). These projects currently utilize about 50% of Carbogen’s capacity and hence we believe there is significant room to add new customers. However, AMCIS is operating at almost full capacity and hence will have to expand capacities or resort to acquisitions to take on new manufacturing assignments.

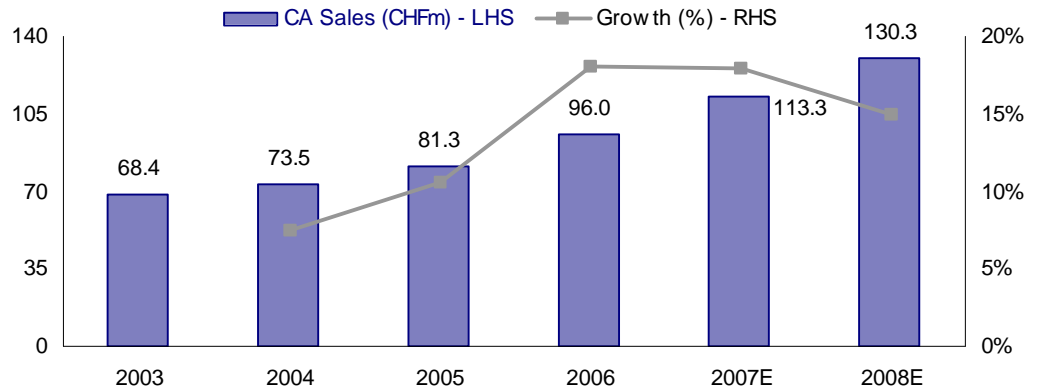
CA – NO. OF CUSTOMERS

*Significant customer ramp-up implies good long-term potential as well as de-risking of operations*



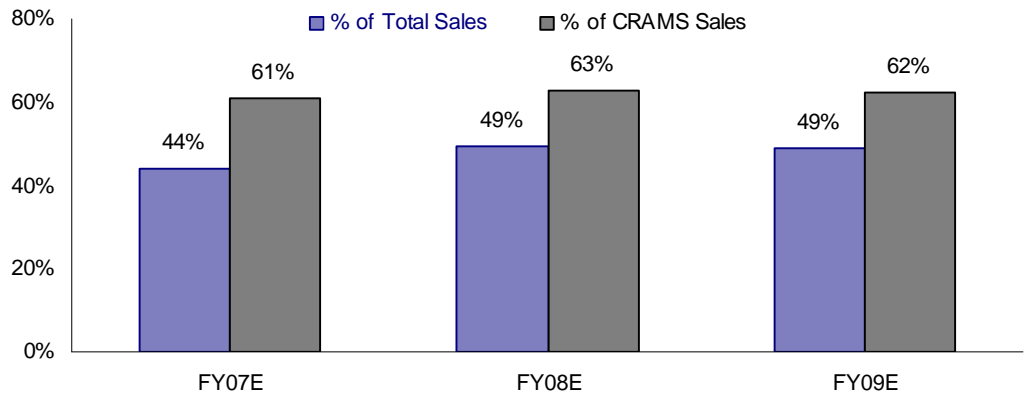
CA – REVENUE BUILD UP

*Secular growth between 200-08*



CA CONTRIBUTION TO DISHMAN

*Carbogen AMCIS to account for almost 50% of Dishman's consolidated revenues*



Source: Company/Motilal Oswal Securities

### **Evaluating further acquisitions**

*Dishman is evaluating further acquisitions*

Dishman has indicated that it is currently evaluating acquisitions targeted at:

1. An oncology API & formulation unit
2. Small niche acquisitions in the US, which will give CA proximity to its US clients (US accounts for about 75% of CA revenues).
3. Small companies with strong IPR in niche technological areas such as biotech and nanotechnology.

CA has identified two acquisition opportunities:

1. A European biotech company with a strong IPR base (estimated value at Euro10m).
2. A mid-west US based company with a facility for contract manufacturing oncology APIs and formulations — possibly involving a deal size of approximately US\$20m.

### **AMCIS' high potency capacity to be doubled**

AMCIS plans to nearly double its high potency capacity at a capex of about CHF8m (Rs300m). This will enable it to be ready for two new oncology products, which are currently awaiting marketing authorizations.

**Other businesses - will scale-up in long-term****Smaller acquisitions unlikely to contribute significantly in medium term**

Besides the CA acquisition, Dishman has, in the past, acquired two small companies with individual niches. These include:

**1. Synprotec DCR Ltd., UK:** Synprotec is a UK-based Contract Research company endowed with contract R&D capabilities in the UK and a strong customer base, having serviced leading global pharmaceutical MNCs and specialty chemical companies. Although, at the time of the acquisition Synprotec had contracts from various MNCs, we believe that its performance in the short term will be adversely impacted as it was a supplier of CCS material for Pfizer's Torcetrapib (which has failed). Currently, the synergies between Synprotec and CA operations are being evaluated.

**2. Innovative Ozone Services Inc. (IO3S):** IO3S is one of the very few companies globally in the field of consultancy and research in Ozone Chemistry. It has a fully developed laboratory as well as a pilot plant for Ozone-based reactions. At the time of acquisition, it had an order book comprising assignments of several molecules for various MNCs.

While both these acquisitions are unlikely to add significantly to Dishman's revenues, we believe the tie-ups would introduce a new dimension in customer relationships to Dishman. These various relationships could be expanded as Dishman and CA together address the entire value chain in the CRAMS segment.

**Dishman enjoys strong global positioning for QUATS; to grow at steady 15%**

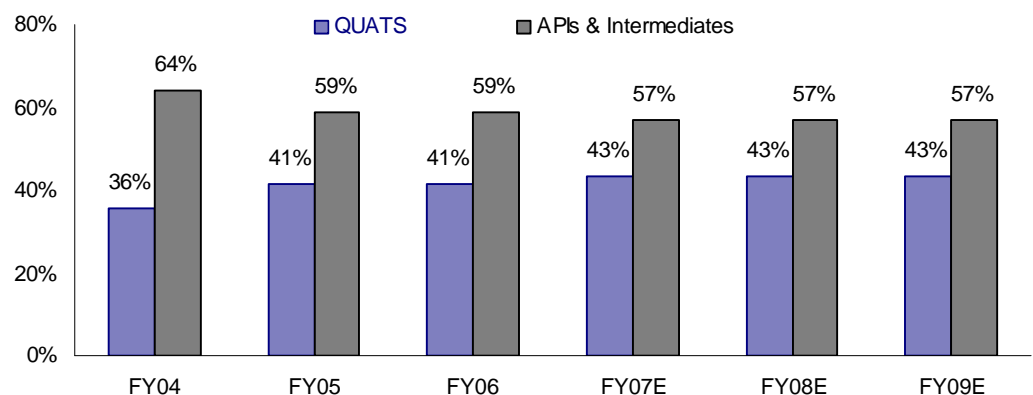
*Strong positioning in  
QUATS business*

Dishman's other major division – Marketable Molecules (MM-26% of FY07E revenues) comprises Quaternary Ammonium Compounds (QUATS), specialty chemicals, API and intermediates manufactured on a regular production basis. A majority of the MM production is exported to the US, Europe, Japan, the Middle East and South Africa. QUATS accounts for about 40-45% of total MM revenues while APIs and intermediates contribute the remaining 55-60%. We expect MM revenues to grow at a steady 13% over the next 2-3 years, led by Dishman's strong positioning in the QUATS segment.

**Focus on high-value QUATS:** Dishman produces a broad basket of QUATS, which is used as a catalyst to transfer a reactant from one phase to another. As a catalyst, QUATS provides benefits such as initiating the reaction of compounds thereby decreasing reaction time. The company is among the leading suppliers globally with capacities close to 1,500 tpa. Since, QUATS is used for catalysis (i.e. in small quantities), the additional cost involved in using it is negligible and the benefits are compelling.

Previously, the company focused on increasing the volume of its QUATS business to ensure optimum utilization of its capacities and to establish first-time customers. Since QUATS comprise chemicals which are of the nature of a commodity, they do not enjoy very high margins (except for certain specialized QUATS). Having established itself as a leading QUATS company globally, Dishman has now started focusing on high-value QUATS manufacture whilst shifting the manufacture of low-value QUATS to China. These high-value QUATS (electronic-grade) have specialized applications in car batteries, energy saving processes, performance enhancement in oil & gas industry etc.

QUATS AND APIS &amp; INTERMEDIATES CONTRIBUTION TO MM



Source: Company/Motilal Oswal Securities

*Setting up QUATS base in China to counter low-cost Chinese manufacturers*

**QUATS initiative in China:** To compete with low-cost Chinese manufacturers, Dishman is in the process of setting up a manufacturing base for QUATS in China. It has already acquired 80,000 sq.m. of industrial land in Shanghai Chemical Industry park at a cost of about US\$4m for this purpose. Dishman's China operations will be operational by December 2007 and will involve total capex of about US\$7m.

**QUATS – stepping stone for pharmaceutical supplies:** Dishman's QUATS business has served as a stepping stone in establishing the company's pharmaceutical supplies business. Since QUATS is used in the pharmaceutical industry, it has given Dishman an opportunity to demonstrate its process chemistry skills to its pharmaceutical customers. This has helped Dishman develop its pharmaceutical supplies business through supplies of APIs and Intermediates, finally culminating in some of the CRAMS contracts.

### **The Saudi Arabia initiative – full contribution to start from FY10**

Dishman has entered into a Joint Venture (JV) with The Arab Company for Drug Industries and Medical Appliances (ACDIMA), Saudi Pharmaceutical Industries, Medical Appliances Corporation (SPIMACO) and Takamul Holding Company for Investments (THC) to set up an API manufacturing facility. Dishman, ACDIMA, SPIMACO and THC will jointly hold the equity in ratio of 30%, 25%, 25% and 20% respectively.

The JV will set up a facility in Saudi Arabia to manufacture about 20 APIs, based on the knowhow that Dishman will supply, for domestic consumption as well as export. Dishman will also supply key intermediates to the JV for production of APIs. However, progress in setting up the facility has been slow and the unit is likely to be operational by November-December 2008. We expect a gradual ramp-up in revenues for this unit and have not included any sales from this initiative in our estimates. The total contribution from this JV will be visible only in FY10. Whilst Dishman will receive about US\$6m as technical fees for setting up the facility, it will also have to invest in the equity of the JV (not quantified).

### Disinfectants initiative — will take time to scale up

*The disinfectant bulk actives initiative will take time to become visible*

Dishman has developed about 15 disinfectant bulk actives for popular hospital disinfectants such as Cetrimide, as well as for some high-value disinfectants. Some of these high-value disinfectants are not being offered by any company globally with appropriate master Drug Master File (DMFs). Dishman plans to exploit this opportunity by establishing a disinfectants division, which will make products for surgical disinfections, hospital disinfections, wound dressings etc. The company also plans to file several application related patents for some of the high-value disinfectants. The company intends to market these products globally through partners and is in the process of evaluating such tie-ups. We believe that this initiative will take some time to scale up, hence we have not factored in revenues from this division in our estimates.

### Proposed capex programs

#### Capex/investments of Rs1.87b over for FY07-FY08

Dishman has plans for significant capex/investments to augment existing capacities and for investments in various initiatives (China, Saudi Arabia). The following table summarizes Dishman's proposed capex/investments:

PROPOSED ACTIVITY	CAPEX (RS M)	FUNDING
Expansion of Dishman's facilities in India (FY07-08)	1,270	Internal accruals & debt
Doubling of AMCIS high-potency capacity	300	
Dishman's Chinese initiative	300	
<b>Total</b>	<b>1,870</b>	

### Further acquisitions may lead to equity dilution

Dishman (through CA) is targeting the following acquisitions:

ACQUISITION	ESTIMATED COST (US\$M)	FUNDING
Small US footprint for proximity to US customers	N.A.	Internal accruals & debt
Small companies with access to biotech & nanotech capabilities	12	
Oncology API & formulation unit in the US	20	
<b>Total</b>	<b>32</b>	

Source: Company/Motilal Oswal Securities

Dishman had proposed to fund these potential acquisitions through a FCCB issue which it subsequently shelved implying that the acquisitions may not go through in the near future. We believe that the company may resort to equity dilution as and when these acquisitions materialize.

## Valuation and outlook

*Key determinants of valuations* The key factors which will determine Dishman's future valuations include:

1. Scale up in the Solvay contract
2. Successful execution of other contracts
3. Scale up in Carbogen's capacity utilization
4. Integration of Carbogen AMCIS-Dishman operations to take advantage of inherent synergies

Over the past few years Dishman has transitioned from being merely a supplier of chemicals (mainly QUATS, an ammonium compound, and intermediates) to supplying pharmaceuticals. It has also enhanced its capabilities from being just a manufacturer to one of being a Contract Research & Manufacturing Services (CRAMS) player offering the complete range of services in the CRAMS value chain. Dishman has been able to achieve this capability by signing up for a higher number of API supply contracts and via acquisition of Carbogen AMCIS (CA). This acquisition has transformed Dishman's business mix and has filled a large gap in its CRAMS offering.

*Dishman is likely to be a key beneficiary of the higher pharma outsourcing from India*

We believe that Dishman will be a key beneficiary of the increased pharmaceutical outsourcing from India. Strong relationships with MNC pharmaceutical companies coupled with access to new customers through the CA acquisition should augur well for the company's CRAMS business. We understand that very few companies in India are prepared to exploit the outsourcing opportunity, as most pharmaceutical companies have very strong generic businesses which, indirectly competes with global MNCs. Dishman is one of the few players from India which has adopted a collaborative approach with global MNCs and is hence likely to benefit from the increased outsourcing from India.

We expect Dishman' core revenues (excluding CA acquisition) to grow at 20% CAGR over FY06-FY09. CA is expected to record about 15-18% growth in CY07E and CY08E. Contribution of CRAMS (including CA) is expected to improve from 53% of total revenues in FY06 to about 80% by FY09E, led by scale-up in EM supplies to Solvay, contribution from new contracts and the CA acquisition. Supplies to Solvay are expected to record 33% CAGR over FY06-FY09 while other contracts (excl. CA) are expected to grow at 17% CAGR. The Marketable Molecules (MM) division is expected to record a steady 13% CAGR in revenues for this period. We have not assumed any revenues from Dishman's initiatives in China and Saudi Arabia, as we believe that upsides from these measures are still some time away.



## REVENUE MODEL (RS M)

	FY05	FY06	FY07E	FY08E	FY09E	CAGR (FY06-09)
Solvay Contracts	480.0	700.0	940.0	1,222.0	1,631.4	33
YoY (%)		46	34	30	34	
% of Total	26	25	17	14	17	
Other Supplies	264.5	777.2	659.8	1,336.2	1,252.0	17
YoY (%)		194	-15	103	-6	
% of Total	14	28	12	16	13	
Carbogen-AMCIS (CA)	0.0	0.0	2,507.3	4,313.3	4,781.0	
YoY (%)				72	11	
% of Total	0	0	45	51	50	
Total CRAMS Revenues	744.5	1,477.2	4,107.1	6,871.5	7,664.4	73
YoY (%)		98	178	67	12	
% of Total	40	53	74	81	80	
Marketable Molecules	1,129.1	1,297.2	1,427.0	1,641.0	1,887.2	13
YoY (%)		15	10	15	15	
% of Total	60	47	26	19	20	
<b>Total Net Revenues</b>	<b>1,873.6</b>	<b>2,774.4</b>	<b>5,534.1</b>	<b>8,512.5</b>	<b>9,551.5</b>	<b>51</b>
<b>YoY (%)</b>		<b>48</b>	<b>99</b>	<b>54</b>	<b>12</b>	
Total Net Revenues (excl CA)	1,873.6	2,774.4	3,026.7	4,199.2	4,770.6	20
YoY (%)		48	9	39	14	

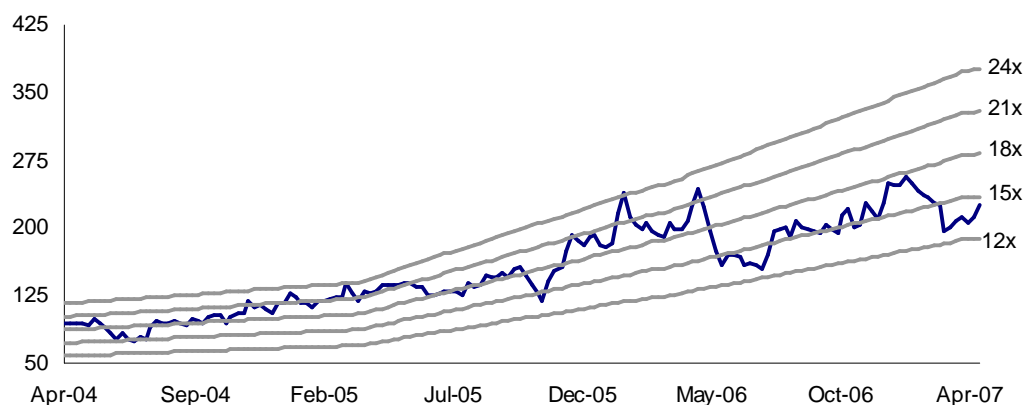
Source: Company/Motilal Oswal Securities

We expect stable EBITDA margins at about 26-27% over FY07-FY09 despite the CA acquisition (which has lower EBITDA margins at about 18%), due to increased supplies to Solvay, contribution from new manufacturing contracts and improving margins in the QUATS business. Fully diluted earnings are expected to record 32% CAGR over FY07-FY09.

*We initiate coverage  
with a Buy*

**Valuation and recommendation:** Dishman is currently valued at 14.6x FY08E and 12.6x FY09E consolidated earnings. Given Dishman's capabilities to offer the complete range of CRAMS services (from the pre-clinical stage up to commercialization), we believe that valuations are likely to expand gradually as new CRAMS assignments start contributing to revenues. CRAMS will account for about 80% of consolidated revenues FY08E onward. RoE is estimated in the 30-34% range and RoCE in the 18-20% range over FY07-FY09. We initiate coverage with a **Buy** with a price target of Rs270 (15x FY09E earnings) implying an upside of 19.5%. Further equity dilution to fund potential acquisitions remains a key risk.

## PER BAND



Source: Motilal Oswal Securities

## COMPARATIVE VALUATIONS

		DISHMAN	DIVI'S	SHASUN
P/E (x)	FY08E	14.6	27.8	9.0
	FY09E	12.6	22.7	6.3
P/BV (x)	FY08E	3.8	7.8	2.2
	FY09E	2.9	6.1	1.8
EV/Sales (x)	FY08E	2.9	5.8	0.6
	FY09E	2.5	4.9	0.5
EV/EBITDA (x)	FY08E	10.8	19.2	6.0
	FY09E	9.2	16.1	4.6

Source: Motilal Oswal Securities

## Concerns

- Needs a broad-based management structure:** Dishman is growing at a hectic pace led by its CRAMS initiatives and acquisitions. While on the one hand it has more than doubled its revenues via the CA acquisition; on the other, it has entered into new supply arrangements with various MNCs requiring expansion of its existing facilities. It is also investing in its initiatives in China and Saudi Arabia.

CA is evaluating potential acquisitions and has already identified two targets. With management resources being spread across all these initiatives, broadening the management structure is imperative. We note the company has recently appointed a new Chief Operating Officer and a new Chief Financial Officer.

- Retaining CA management team:** It is imperative for Dishman to retain the existing management team of CA to ensure a smooth integration with the Indian operations.
- Consolidation:** The global pharmaceutical industry is in the throes of significant consolidation with large mergers (to increase size and gain scale) and acquisition of smaller R&D companies (to strengthen R&D pipelines). We view this as a significant risk to the global CRAMS industry, as consolidation amongst customers may lead to loss of business. In fact, consolidation has been the chief reason for the significant decline in fortunes of CRAMS players some years ago.

INCOME STATEMENT		(RS MILLION)				
Y/E MARCH	2004	2005	2006	2007E	2008E	2009E
Net Sales	1,676	1,864	2,760	5,534	8,513	9,552
<i>Change (%)</i>	44.2	11.3	48.1	100.5	53.8	12.2
Total Expenditure	1,260	1,360	2,128	4,083	6,220	6,947
<i>% of Sales</i>	75.2	73.0	77.1	73.8	73.1	72.7
<b>EBITDA</b>	<b>416</b>	<b>504</b>	<b>633</b>	<b>1,451</b>	<b>2,292</b>	<b>2,604</b>
<i>Margin (%)</i>	24.8	27.0	22.9	26.2	26.9	27.3
Depreciation	76	83	120	393	515	563
EBIT	340	421	512	1,058	1,778	2,041
Int. and Finance Charges	127	110	59	196	364	424
Other Income - Rec.	21	29	54	140	120	120
<b>PBT before EO Expense</b>	<b>234</b>	<b>340</b>	<b>506</b>	<b>1,002</b>	<b>1,533</b>	<b>1,737</b>
Extra Ordinary Expense/(Income)		0	0	0	0	0
<b>PBT after EO Expense</b>	<b>234</b>	<b>340</b>	<b>506</b>	<b>1,002</b>	<b>1,533</b>	<b>1,737</b>
Current Tax	18	35	33	140	230	226
Deferred Tax	9	-27	-2	15	31	35
<i>Tax Rate (%)</i>	11.5	2.3	6.2	15.5	17.0	15.0
<b>Reported PAT</b>	<b>208</b>	<b>332</b>	<b>475</b>	<b>847</b>	<b>1,273</b>	<b>1,476</b>
<b>PAT Adj for EO Items</b>	<b>208</b>	<b>332</b>	<b>475</b>	<b>847</b>	<b>1,273</b>	<b>1,476</b>
<i>Change (%)</i>	30.3	60.0	43.0	78.3	50.3	16.0
<i>Margin (%)</i>	12.38	17.81	17.20	15.30	14.95	15.46

E: MOST Estimates

BALANCE SHEET							(RS MILLION)
Y/E MARCH	2004	2005	2006	2007E	2008E	2009E	
Equity Share Capital	103	137	137	144	144	144	
Fully Diluted Equity Capital	103	137	163	164	164	164	
Total Reserves	561	1,333	1,748	3,043	4,163	5,462	
<b>Net Worth</b>	<b>664</b>	<b>1,471</b>	<b>1,885</b>	<b>3,187</b>	<b>4,307</b>	<b>5,606</b>	
Deferred liabilities	28	1	0	15	45	80	
Total Loans	1,107	1,183	3,255	5,268	6,586	6,716	
<b>Capital Employed</b>	<b>1,800</b>	<b>2,655</b>	<b>5,140</b>	<b>8,469</b>	<b>10,938</b>	<b>12,402</b>	
Gross Block	1,295	1,550	2,190	7,640	9,513	9,913	
Less: Accum. Deprn.	242	321	440	3,148	3,662	4,226	
<b>Net Fixed Assets</b>	<b>1,053</b>	<b>1,229</b>	<b>1,750</b>	<b>4,493</b>	<b>5,851</b>	<b>5,688</b>	
Capital WIP	61	129	373	323	150	150	
Investments	4	4	75	40	40	40	
<b>Curr. Assets</b>	<b>1,140</b>	<b>1,853</b>	<b>3,746</b>	<b>5,271</b>	<b>7,451</b>	<b>9,368</b>	
Inventory	584	814	1,082	2,214	3,150	3,534	
Account Receivables	307	668	863	1,937	2,979	3,343	
Cash and Bank Balance	70	92	1,352	429	258	1,297	
Loans & Advances	179	280	449	692	1,064	1,194	
<b>Curr. Liability &amp; Prov.</b>	<b>489</b>	<b>567</b>	<b>816</b>	<b>1,668</b>	<b>2,564</b>	<b>2,854</b>	
Account Payables	392	446	657	1,384	2,128	2,388	
Provisions	97	121	159	284	436	466	
<b>Net Current Assets</b>	<b>651</b>	<b>1,286</b>	<b>2,930</b>	<b>3,604</b>	<b>4,887</b>	<b>6,514</b>	
<b>Appl. of Funds</b>	<b>1,800</b>	<b>2,655</b>	<b>5,140</b>	<b>8,469</b>	<b>10,938</b>	<b>12,402</b>	

*E: MOSt Estimates*

## RATIOS

Y/E MARCH	2004	2005	2006	2007E	2008E	2009E
<b>Basic (Rs)</b>						
<b>EPS (fully diluted)</b>	<b>2.0</b>	<b>4.8</b>	<b>5.8</b>	<b>10.3</b>	<b>15.5</b>	<b>18.0</b>
Cash EPS (fully diluted)	2.7	6.0	7.3	15.1	21.8	24.9
BV/Share	6.2	21.3	27.3	44.0	59.5	77.5
DPS	0.1	0.5	0.7	1.4	2.1	2.5
Payout (%)	14.9	11.7	11.6	12.0	12.0	12.0
<b>Valuation (x)</b>						
P/E (fully diluted)			39.1	22.0	14.6	12.6
Cash P/E (fully diluted)			31.2	15.0	10.4	9.1
P/BV			8.3	5.2	3.8	2.9
EV/Sales			7.4	4.2	2.9	2.5
EV/EBITDA			32.4	16.1	10.9	9.2
Dividend Yield (%)			0.3	0.6	0.9	1.1
<b>Return Ratios (%)</b>						
RoE	36.4	31.7	28.5	33.5	34.1	29.8
RoCE	22.1	20.5	14.5	17.7	19.6	18.6
<b>Working Capital Ratios</b>						
Debtor (Days)	65	128	113	125	125	125
Creditor (Days)	351	338	345	223	223	228
Inventory (Days)	127	159	143	146	135	135
Working Capital Turnover (Days)	127	234	209	209	198	199
<b>Leverage Ratio (x)</b>						
Current Ratio	2.3	3.3	4.6	3.2	2.9	3.3
Debt/Equity	1.7	0.8	1.7	1.7	1.5	1.2

E: MOST Estimates

CASH FLOW STATEMENT							(RS MILLION)
Y/E MARCH	2004	2005	2006	2007E	2008E	2009E	
Oper. Profit/(Loss) before Tax	416	504	633	1,451	2,292	2,604	
Interest/Dividends Recd.	21	29	54	140	120	120	
Direct Taxes Paid	-18	-35	-33	-140	-230	-226	
(Inc)/Dec in WC	-156	-613	-384	-1,596	-1,455	-587	
<b>CF from Operations</b>	<b>263</b>	<b>-115</b>	<b>269</b>	<b>-145</b>	<b>728</b>	<b>1,911</b>	
EO Expense / (Income)	0	0	0	0	0	0	
<b>CF from Operating incl EO Expense</b>	<b>263</b>	<b>-115</b>	<b>269</b>	<b>-145</b>	<b>728</b>	<b>1,911</b>	
(inc)/dec in FA	-148	-303	-890	-3,085	-1,700	-400	
(Pur)/Sale of Investments	0	0	-71	35	0	0	
<b>CF from Investments</b>	<b>-148</b>	<b>-303</b>	<b>-961</b>	<b>-3,050</b>	<b>-1,700</b>	<b>-400</b>	
Issue of Shares	-23	514	-6	557	0	0	
(Inc)/Dec in Debt	91	75	2,072	2,013	1,318	130	
Interest Paid	-127	-110	-59	-196	-364	-424	
Dividend Paid	-31	-39	-55	-102	-153	-177	
Others	20	0	0	0	0	0	
<b>CF from Fin. Activity</b>	<b>-69</b>	<b>440</b>	<b>1,952</b>	<b>2,272</b>	<b>801</b>	<b>-471</b>	
<b>Inc/Dec of Cash</b>	<b>46</b>	<b>22</b>	<b>1,261</b>	<b>-923</b>	<b>-171</b>	<b>1,040</b>	
Add: Beginning Balance	70	70	92	1,352	429	258	
Closing Balance	117	92	1,352	429	258	1,297	

E: MOST Estimates

**N O T E S**



For more copies or other information, contact

**Institutional:** Navin Agarwal. **Retail:** Manish Shah

Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: inquire@motilaloswal.com

**Motilal Oswal Securities Ltd, 3rd Floor, Hoechst House, Nariman Point, Mumbai 400 021**

This report is for the personal information of the authorized recipient and does not construe to be any investment, legal or taxation advice to you. Motilal Oswal Securities Limited (*hereinafter referred as MOST*) is not soliciting any action based upon it. This report is not for public distribution and has been furnished to you solely for your information and should not be reproduced or redistributed to any other person in any form.

The report is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon such. MOST or any of its affiliates or employees shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. MOST or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

MOST and/or its affiliates and/or employees may have interests/ positions, financial or otherwise in the securities mentioned in this report. To enhance transparency, MOST has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report.

**Disclosure of Interest Statement**

1. Analyst ownership of the stock
2. Group/Directors ownership of the stock
3. Broking relationship with company covered
4. Investment Banking relationship with company covered

**Dishman Pharma**

No  
No  
No  
Yes

This information is subject to change without any prior notice. MOST reserves the right to make modifications and alternations to this statement as may be required from time to time. Nevertheless, MOST is committed to providing independent and transparent recommendations to its clients, and would be happy to provide information in response to specific client queries.