

March 5, 2008

Rating	Not Rated
Price	Rs250
Target Price	NA
Implied Upside	NA
Sensex	16,340

(Prices as on March 4, 2008)

Trading Data

Market Cap. (Rs bn)	31.4
Shares o/s (m)	249.8
Free Float	28.0%
Avg. Daily Vol ('000)	17.2
Avg. Daily Value (Rs m)	5.0

Major Shareholders

Promoters	72.0%
Foreign	4.7%
Domestic Inst.	16.4%
Public & Others	6.9%

Stock Performance

(%)	1M	6M	12M
Absolute	(6.5)	(22.9)	(17.6)
Relative	5.3	(29.4)	(50.1)

Price Performance (RIC: CADI.BO, BB: CDH IN)



Source: Bloomberg

■ **Company business:** Cadila Healthcare (CHL) is one of the largest integrated pharma companies in India. CHL is focusing on fast growing markets of Brazil, Russia and Japan. The company derives 67% of its revenue from the domestic market, 23% from the US and Europe, and 10% from emerging markets. It has three long-term contracts for intermediates and formulation supplies to global pharma companies. It has signed 26 contracts with MNCs with peak revenue potential of US\$40m (Rs1.6bn).

■ CHL has strong presence in consumer products and currently markets *Sugar Free*, *Everyuth* and *Nutralite* in the domestic market. All these products are growing over 20% p.a. and are likely to be future growth driver for the company.

■ **Capex:** CHL is likely to spend Rs1.2-1.5bn capex per annum over the next two years.

■ **Financials:** Based on our first cut estimates, the company is likely to report 29% YoY growth in consolidated sales and 9.3% YoY growth in consolidated net profit for FY08. We expect EBIDTA margin to be maintained at 19.2% in FY08. CHL is likely to report RoE of 26% and RoCE of 19% for FY08.

■ **Valuation:** The stock currently trades at 11.9x FY08E EPS of Rs21.1. With strong presence in the domestic market, in-licensing of products, introduction of rural field force and entry into dermatology segment, we expect the company to perform well in future. We are positive on the long-term prospects of the company.

Key financials (Y/e March)	FY05	FY06	FY07	FY08E*
Revenue (Rs m)	12,472	14,845	18,288	23,540
Growth (%)	—	19.0	23.2	28.7
EBITDA (Rs m)	2,269	2,877	3,521	4,510
PAT (Rs m)	1,152	1,650	2,415	2,640
EPS (Rs)	9.3	13.1	18.6	21.1
Growth (%)	—	40.7	41.8	13.3
Net DPS (Rs)	—	—	—	—

Source: Company Data; PL Research

* First cut estimates

Profitability & valuation	FY05	FY06	FY07	FY08E*
EBITDA margin (%)	18.2	19.4	19.3	19.2
RoE (%)	17.3	23.6	30.9	26.4
RoCE (%)	12.6	16.0	19.3	18.9
EV / sales (x)	1.6	1.4	2.0	1.5
EV / EBITDA (x)	8.6	7.0	10.2	7.8
PE (x)	26.8	19.0	13.4	11.8
P / BV (x)	2.6	2.2	3.6	3.0
Net dividend yield (%)	—	—	—	—

Source: Company Data; PL Research

* First cut estimates

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Potential upsides

- The company enjoys excise and tax benefits for Baddi and Sikkim facilities and hence has an edge over its competitors.
- CHL is the only producer of transdermal patches and suppositories in India. Hence, these products offer higher margins than other formulations.
- The company has recently added special field force to tap the rural market. This is likely to improve topline of the company.
- CHL has launched 39 new products in FY07, of which eight were 1st in India. These are likely to be future growth drivers for CHL.
- The company has plans to increase its international sales by 3.1x from US\$134m (Rs5.36bn) in FY07 to US\$410m (Rs16.4bn) in CY10.
- The company has 38 ANDA pending approval with the US FDA and has plans to file 15-20 ANDA per year over the next 2-3 years. This is likely to give its US business critical mass.
- CHL has signed 26 other contracts with MNCs, with peak revenue potential of US\$40m (Rs1.6bn).
- The company has plans to invest Rs800m in SEZ Pharmez near Ahmedabad. Revenue from the same is likely to accrue from FY11 onwards.

Valuation

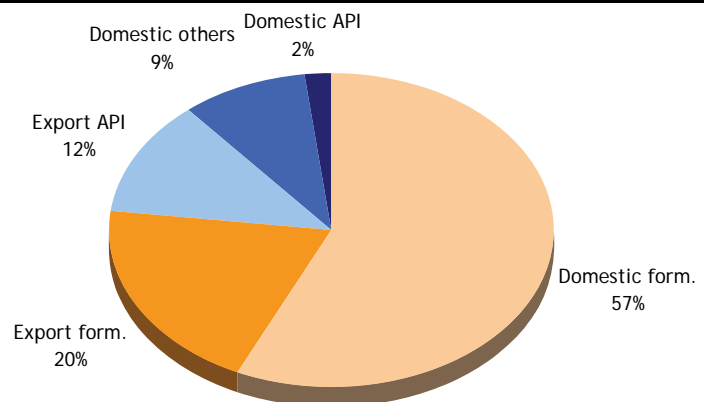
- Based on our first cut estimates, the company is likely to report 29% YoY growth in consolidated sales and 9.3% YoY growth in consolidated net profit for FY08. We expect EBIDTA margin to be maintained at 19.2% in FY08. CHL is likely to report RoE of 26% and RoCE of 19% for FY08.
- The stock currently trades at 11.9x FY08E EPS of Rs21.1. With its strong presence in the domestic market, in-licensing of products, introduction of rural field force and entry into dermatology segment, we expect the company to perform well in future. We are positive on the long-term prospects of the company.

Company Business

Domestic

CHL is amongst India's leading integrated pharma companies and ranks 5th in the domestic formulations market. It has strong presence in generic markets of the US, France and Brazil, and is likely to consolidate its presence in these markets. The company has a strong R&D team and has no plans to hive-off its research business into a separate company. The company's revenue break-up for FY07 has been shown in the following chart:

Revenue break-up (FY07)



Source: Company Data, PL Research

As seen from the above chart, CHL derived 67% of its revenue from the domestic market, 23% from the US and Europe, and 10% from emerging markets. Since it derives a portion of its revenue in dollar terms, the company does not have large exposure to the dollar.

CHL's formulation business reported strong growth of 69% CAGR over FY04-FY07, and is likely to report healthy growth in future. Its domestic manufacturing facilities are located at Baddi and Sikkim.

CHL has in-licensing agreements with three German companies -- Schering AG, Boehringer Ingelheim and Meda Pharma. These companies are research-based companies and have innovative products. Hence, the company is not likely to face major competition in the domestic market.

The company has recently acquired Liva Healthcare. This has given it an entry into Rs15bn dermatology market in India.



Global

In the developed markets, CHL has presence in the US generic market, Europe and Japan. It has recently acquired Nippon Universal Pharmaceuticals, Japan. This will give it an entry into the highly lucrative Japanese pharma market for launching its products.

In the emerging market, CHL has presence in Russia and CIS, Sri Lanka, Vietnam, Africa, Middle-East and Brazil.

For the US market, CHL has filed 57 DMF and 70 ANDA and has received approval for 32 ANDA. Over 50% of the ANDA are based on own API and hence the company will have better margin due to integration. CHL has plans to launch 8-10 generic products per annum in the US and expects 30-32% growth in the US generic market.

The company has launched over 100 generics in France and expects 35-40% growth in this market. CHL has introduced 13 new products from India in France and has plans to launch 12-15 products per annum. It has recently acquired Nikkho do Brazil for €5.2m. Nikkho provides Cadila an entry into the fast growing branded generic market in Brazil.

Consumer products

CHL has been marketing low calorie sweetener *Sugar Free* and *Everyuth* skin care products for over 15 years. *Sugar Free* has a market share of over 75% in the domestic market and is growing over 20% per annum. *Everyuth* has been growing at over 20% CAGR over last three years.

In March 2006, the company acquired 62% stake in Carnation Nutra Foods, the manufacturers of *Nutralite* - India's largest selling margarine and substitute for butter.

The consumer products division currently contributes 9% of CHL's total revenue.

Contract research

CHL has three long-term contracts for the supply of:

1. Pantoprazole intermediate to Zydus Nycomed (a 50:50 JV)
2. Agiolax manufacturing for Madaus AG
3. Anti-cancer products for Zydus Hospira (a 50:50 JV)



All these contracts are for specialised products and hence have higher margins.

CHL has signed 26 other contracts with MNCs with peak revenue potential of US\$40m (Rs1.6bn).

R & D

- CHL focuses on NCE and NDDS in the areas of dyslipidemia, inflammation, diabetes and obesity. The company has a pipeline of five NCE molecules. Its lead molecule ZYH1 in Dyslipidemia is currently undergoing Phase II clinical trials.
- Currently, over 600 scientists are employed in the R & D activities.

Income Statement (consolidated) (Rs m)

Y/e March	FY05	FY06	FY07	FY08E*
Net sales	12,472	14,845	18,288	23,540
Operating expenses	10,203	11,968	14,767	19,030
(Inc) / Dec in stock	(369)	(99)	(917)	(520)
Material cost	5,154	5,787	7,289	8,640
<i>% of sales</i>	<i>38.4</i>	<i>38.3</i>	<i>34.8</i>	<i>34.5</i>
Staff cost	1,630	1,804	2,110	2,780
<i>% of sales</i>	<i>13.1</i>	<i>12.2</i>	<i>11.5</i>	<i>11.8</i>
Other expenses	3,788	4,476	6,285	8,130
<i>% of sales</i>	<i>30.4</i>	<i>30.2</i>	<i>34.4</i>	<i>34.5</i>
Operating profit	2,269	2,877	3,521	4,510
<i>Operating margin (%)</i>	<i>18.2</i>	<i>19.4</i>	<i>19.3</i>	<i>19.2</i>
Other income	29	36	264	10
EBIDTA	2,298	2,913	3,785	4,520
<i>EBIDTA margin (%)</i>	<i>18.4</i>	<i>19.6</i>	<i>20.7</i>	<i>19.2</i>
Depreciation	709	779	823	1,020
EBIT	1,589	2,134	2,962	3,500
<i>EBIT margin (%)</i>	<i>12.7</i>	<i>14.4</i>	<i>16.2</i>	<i>14.9</i>
Interest + forex fluctuations	245	251	223	260
Profit before tax	1,344	1,883	2,739	3,240
Tax provision	192	233	324	600
<i>Effective tax rate (%)</i>	<i>14.3</i>	<i>12.4</i>	<i>11.8</i>	<i>18.5</i>
PAT before EO	1,152	1,650	2,415	2,640
Extraordinary items	125	125	-	120
PAT after EO items	1,027	1,525	2,415	2,520
Adjustment on consolidation	20	(1)	(77)	10
Net profit	1,047	1,524	2,338	2,530



Balance Sheet (consolidated)

(Rs m)

Y/e March	FY05	FY06	FY07	FY08E*
Sources of funds				
Equity share capital	314	314	628	628
Reserves & surplus	5,619	6,675	8,027	9,818
Networth	5,933	6,989	8,655	10,446
Minority interest	-	7	142	142
Total debt	3,834	4,432	4,535	3,900
Deferred tax liability	1,010	1,097	1,137	1,187
Total	10,777	12,525	14,469	15,675
Application of funds				
Gross block	11,158	12,086	13,527	15,000
Avg. gross block	11,158	11,622	12,807	14,264
Less: Accum. depreciation	3,677	4,393	4,968	5,988
Net block	7,481	7,693	8,559	9,012
Capital work-in-progress	425	636	1,224	1,350
Investments	467	714	261	300
Current assets, loans & adv.	4,992	6,491	9,871	10,902
Inventories	2,221	2,475	3,896	4,100
Sundry debtors	1,235	1,990	2,784	3,150
Cash and bank balance	612	438	990	1,202
Loans and advances	924	1,588	2,201	2,450
Less: Current liab. & prov.	2,666	3,009	5,446	5,889
Current liabilities	2,060	2,404	4,588	4,600
Provisions	606	605	858	1,289
Net current assets	2,326	3,482	4,425	5,013
Miscellaneous exp. not w/off	78	-	-	-
Total	10,777	12,525	14,469	15,675



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PL's Recommendation Nomenclature

BUY	: > 15% Outperformance to BSE Sensex	Outperformer (OP)	: 5 to 15% Outperformance to Sensex
Market Performer (MP)	: -5 to 5% of Sensex Movement	Underperformer (UP)	: -5 to -15% of Underperformance to Sensex
Sell	: <-15% Relative to Sensex		
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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