

Pharmaceuticals & Biotechnology

Premium valuations limit upside

We see limited upside as most Indian generics are trading at premium valuations to the US generic sector. Only Ranbaxy and Dr Reddy's offer about 20% potential upside, but the high NPVs of Para IV/NCE pipelines could make them unattractive for some.

Table 1 : Valuation comparables, FY09F

	PER (x)	EV/ EBITDA (x)	P/ sales (x)	Upside to TP	Reco	Target blended PE (x) (US\$m)	NPV
Cipla	18.7	21.4	3.9	2%	Hold	22.6	-
Dr Reddy's	12.7	12.1	2.2	24%	Buy	18.9	320
Lupin	19.6	12.0	2.4	-3%	Hold	17.7	-
Ranbaxy	18.2	14.3	2.1	31%	Buy	22.6	755
Sun Pharma	21.8	18.3	7.6	-3%	Hold	23.4	43
Wockhardt	12.9	10	2	5%	*Buy	16.8	-
Indian generics	18.9	14.7	3.4				
European generics	17.4	9.5	2.5				
US generics	14.9	7.6	2.2				

* The stock has attained our target price and we will revisit our recommendation pending consolidation of the recent Negma acquisition
Source: ABN AMRO forecasts

Premium multiples; limited upside potential

Indian generic companies are trading at an average premium of 27% to the FY09F PERs of their US counterparts on consensus estimates. We agree the regional sales mix of Indian companies warrants a premium, but the sector's 25-30% revenue exposure to the US, the UK and the increasing commoditisation in Western European markets like Germany indicate limited potential upside from current levels. The premium valuations for Ranbaxy and Dr Reddy's are still lower than the average and, when coupled with the NPV of their ParaIV/ R&D pipelines, offer around 20% appreciation potential.

Valuing companies on SOTP; Ranbaxy remains our top pick

We have assigned higher values to the domestic formulations business of Indian companies. We have assigned lower values (in descending order) to their businesses in Russia/CIS and Eastern Europe owing to under-penetration of generics, exposure to the high-margin branded formulations business and strong growth we expect in these regions. We have valued potential Para IV exclusivities and authorised-generic deals on an NPV basis, as one-off items PE-based valuations are not applicable. Ranbaxy remains our top pick in the sector and we forecast the company will make 66% of its 2007 profit from emerging economies. The stock is trading at 17.5x FY07F earnings (ex-Lipitor) and our target price of Rs505 implies 31% potential upside.

Lupin and Wockhardt achieve fair value; Cipla downgraded

Lupin (we downgraded the stock to Hold from Buy; see our report, *Solid prospects in the price*, dated 10 May 2007) and Wockhardt have appreciated 25-30% since January 2007, reaching our fair value estimates. We recently cut our earnings estimates for Cipla by 20%, downgrading it to a Hold (from Buy) in view of weak growth guidance and higher-than-expected margin pressure (see our report, *Results and guidance disappoint*, dated 27 April 2007). Dr Reddy's has been an underperformer on concerns about Betapharm's performance and remains our high-risk Buy recommendation. We retain our Hold on Sun Pharma and Glenmark. Over the same period, Ranbaxy's share price dropped nearly 25% on negative news, but has recovered the entire loss over the past three weeks, following in-line results and the USFDA approval for pravastatin. Ex-Para IV NPV, we estimate Ranbaxy and Dr Reddy's offer upside potential of less than 10%, which may not be an attractive risk-reward proposition for some.

India

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Not much upside left

We see little upside in Indian generics stocks: they are expensive relative to US and European peers on FY09F PEs. Ranbaxy and Dr Reddy's offer potential upside, but only after factoring in one-off opportunities.

Premium valuations too high

Pricing pressures in commodity generics markets like the US and the UK have been well documented in various industry reports and argue for exposure to branded generics markets for sustainability in growth and profitability. Indian generics pharma stocks present an exposure mix to the commodity and branded generics space. Furthermore, the emerging economies in which these companies operate offer core consumption-driven growth. This, in our view, warrants premium valuations for the Indian generics pharma sector vis-à-vis US firms.

Indian generics stocks are now trading at an average 2008F PE of 18.9x vs 14.9x for US generics stocks (on Bloomberg consensus estimates), which represents a 27% premium for Indian stocks despite our 16% earnings growth forecasts (compared with US companies' 22% consensus earnings growth forecast). European generics firms' 26% projected consensus earnings growth is comparable to that of US companies. On price/sales and EV/EBITDA, Indian companies' premiums are even higher, at 51% and 93%, respectively. We agree that the regional sales mix of Indian firms warrants a premium, but believe the sector's 25-30% revenue exposure to the US and the increasing commoditisation in Western European markets like Germany indicate limited potential upside from current levels.

Table 2 : Valuation multiples

	Price (local currency)	Sales (Rsm)	Op profit (Rsm)	OPM	PER (x)	EV/EBITDA (x)	P/Sales (x)	EPS growth
Indian generics (FY09F)				22%	18.9	14.7	3.4	16%
Dr Reddy's	689.70	52,300	10,756	21%	12.7	12.1	2.2	34%
Sun Pharma	995.40	25,441	8,977	35%	21.8	18.3	7.6	12%
Cipla	207.95	41,715	9,484	23%	18.7	21.4	3.9	17%
Lupin	713.55	24,182	4,166	17%	19.6	12.0	2.4	-7%
Ranbaxy	385.90	69,019	10,606	15%	18.2	14.3	2.1	14%
Wockhardt	407.55	21,838	5,043	23%	12.9	10.0	2.0	24%
European generics (2008F)				26%	17.4	9.5	2.5	26%
Gedeon Richter	37,145	198,210	63,743	32%	14.6	12.1	3.6	14%
Krka	867.57	862	261	30%	19.1	10.8	3.5	19%
Actavis	78.2	155,731	37,108	24%	16.6	7.7	1.9	48%
Stada	48.37	1,676	333	20%	17.6	9.9	1.7	22%
Pliva	630	7,551	1,550	21%	19.8	8.7	1.9	24%
Zentiva	1461	22,408	6,434	29%	17.3	8.1	2.5	22%
US generics (2008F)				27%	14.9	7.6	2.2	22%
Barr Labs	52.25	1,993	768	39%	13.6	5.8	2.9	17%
Mylan	22.64	1,968	659	33%	14.3	6.8	2.7	0%
Watson	31.33	2,573	486	19%	16.7	7.6	1.2	49%
Par	27.11	745	106	14%	16.9	9.8	1.3	82%
Teva	38.41	10,259	3,072	30%	15.0	8.0	3.0	15%

Note: PER is based on FY09 estimates, 2008 for Ranbaxy and Wockhardt; all priced on close of business 10 May 2007
Source: ABN AMRO forecasts for Dr Reddy's, Sun Pharma, Cipla, Lupin, Ranbaxy, Wockhardt; IBES consensus for others

We retain Ranbaxy as our top pick with a target price of Rs505, which represents a potential upside of 31%. We believe the stock's premium valuation is still below the Indian sector average and we see upside potential given that 66% of its business comes from emerging economies. Furthermore, we see the expected launch of the generic version of Lipitor in 2010-11 as a near certainty, and accordingly add Rs65 to our fair-value calculation. Ex-Lipitor, the stock is trading at 17.5x 2007F earnings, which in our view is cheap. Besides, we think the stock has near-term triggers vis-à-vis the peer group.

We recently cut EPS estimates for Cipla by 20% and downgraded it to a Hold following weak growth guidance and increasing margin pressure. Lupin and Wockhardt have run up 30% since January 2007, and are now trading at our fair-value estimates. We retain a Hold on Sun Pharma and Glenmark. Dr Reddy's is the only other stock for which we see a potential upside of over 15%, but much will depend on the performance of its subsidiary Betapharm. Excluding the NPVs of Para IV opportunities, we estimate Ranbaxy and Dr Reddy's offer a potential upside of only about 10%, which may be unattractive to some investors.

Valuation on SOTP and NPV

The US pharma market is marked by significant earnings volatility. We expect Dr Reddy's earnings to increase by 450% in FY07 on the back of one-time gains from the simvastatin (gZocor) AG deal and exclusivity on ondansetron (gZofran), but then decline by 14% in FY08. Ranbaxy could show similar volatility, with potential windfall earnings from the generic version of Lipitor in 2010F followed by a relatively lean patch. Given such volatility, valuations based on PE multiples could be tricky. As such, we value one-off opportunities on the basis of NPV.

Sum-of-the-parts valuation used to focus on regional exposures, and NPV used for one-offs and R&D-related potential upside

For core sustainable earnings we focus on regional exposures. We use blended PE valuations based on the regional mix with relatively higher valuation assigned to branded generics markets like Eastern Europe and India, which we believe offer high growth and strong margins vis-à-vis commoditised generics markets such as the US and Western Europe.

We combine our NPV and SOTP to derive our valuation methodology (broad assumptions highlighted in Table 11). We believe this approach allows us to value appropriately the more sustainable parts of Indian firms' business while valuing one-off opportunities conservatively.

Table 3 : Sum-of-the-parts and NPV valuation assumptions, FY08F

Region/business	Valuation	Comments
US	PE - 16x	Our valuation multiple is in line with the US generics sector (companies with 80%+ exposure to the US). We forecast about 5% 2006-10 revenue CAGR over the next five years. This highly competitive market faces price erosion and declining margins.
Western Europe	PE - 16-18x	We have imputed a range of multiples in view of the varying exposure to underpenetrated markets. The US and UK markets present similar conditions, while the southern European markets are underpenetrated and therefore provide volume growth potential. Heavy regulatory reforms are under way, leading to price cuts and declining margins.
Russia/CIS/Romania, etc	PE - 20x	The valuation premium vis-à-vis western Europe is due to higher growth potential and margins in these regions. We forecast about 20% revenue CAGR for 2006-10, as per-capita spend on drugs is set to increase. Branded formulations fetch high margins.
India	PE - 20-25x	Valuation represents domestic growth and the quality of the domestic portfolio. We expect the overall pharma market to grow at about 15% pa. We estimate a US\$3bn-4bn domestic opportunity through 2010, assuming a conservative 8-9% market CAGR over 2006-10.
Bulk business	PE - 13x	In line with the segment multiple.
One-off opportunities	NPV	We use a DCF model to value litigation outcomes, AG arrangements and R&D pipeline

Source: IBES, ABN AMRO forecasts

Company valuations

Based on our SOTP valuations, we recommend Ranbaxy and Dr Reddy's as our top picks in the sector. Our valuation assumes pipeline NPV of 17% for Ranbaxy and 10% for Dr Reddy's, which may be considered risky by some. We present below snapshot valuations for FY08F for all the stocks in the ABN AMRO Indian generics universe.

Table 4 : Cipla (Hold, TP Rs213)

US\$m	Value break down	Contribution	Comments
India formulations	3,446	87%	Valued at 25x; 50%+ contribution to sales; strong franchise in respiratory drugs and 40%+ chronic portfolio
Anti-retrovirals (ARVs)	207	5%	Valued on PE of 16x considering strong competition and dropping prices
Export formulations	204	5%	Valued on blended PE of 18x
Export Bulk	84	2%	In-line with sector bulk business valuations
Total	3,940		

Source: ABN AMRO forecasts

Table 5 : Dr Reddy's Labs (Buy, TP Rs855)

US\$m	Value break down	Contribution	Comments
India formulations	825	26%	Valued at 25x; 42% chronic portfolio
Betapharm	742	23%	Valued at 10% discounted to Stada, the leader in Germany at PER of 18x
RoW formulations	555	18%	Valued at 20x; Strong growth rate in Russia CIS and high margins in formulations
US generics	283	9%	Valued on a PER of 16x; 10-15% premium to US generic players for 'India' advantage
Contract Pharma	241	8%	20% premium to bulk valuations; Mexican acquisition increases the bulk content of the business
Balaglitazone	204	6%	NPV valuation; US\$300m peak sales in year 3 of launch
Bulk	165	5%	In line with sector bulk business valuations
NPV of one-offs	115	4%	NPV of eight products disclosed, with seven FTF opportunities and one settlement; generics portfolio covers innovators' drugs with aggregate annual sales of US\$7.5bn
Western Europe excl. Betapharm	41	1%	In line with US generics; mid-single digits NPMs assumed
Total	3,171		

Source: ABN AMRO forecasts

Table 6 : Glenmark Pharma (Hold, TP Rs656)

US\$m	Value break down	Contribution	Comments
R&D	962	48%	Option valuation of two deals i.e. 'Oglemilast' and GRC 8200
India formulations	450	22%	Valued at 20x; high dermatology focus
US generics	256	13%	Valued on a PER of 16x; 10-15% premium to US generic players for 'India' advantage
RoW formulations	197	10%	Blended PER of 18x for regions like Russia/ CIS/ CEE/Asia/ Africa
Latin America generics	101	5%	Valued on a PER of 16x in line with US (both US and LatAM businesses of Glenmark are quite nascent)
Bulk	51	3%	In line with sector bulk business valuations
Total	2,017		

Source: ABN AMRO forecasts

Table 7 : Lupin (Hold, TP Rs695)

US\$m	Value break down	Contribution	Comments
India formulations	861	63%	Valued at 20x; only 26% chronic portfolio
US generics	357	26%	Valued on a PER of 16x; higher NPM on account of branded product Suprax and presence in products with limited competition
Bulk	89	7%	In line with sector bulk business valuations at 13x
RoW formulations	57	4%	Valued on a blended PER of 18x
NPV of one-offs	3	0%	NPV for the limited competition upside potential in 'cefdinir' for three months in FY08
Total	1,359		

Source: ABN AMRO forecasts

Table 8 : Ranbaxy (Buy, TP Rs505)

US\$m	Value break down	Contribution	Comments
India formulations	1,581	35%	Valued at 25x; Ranbaxy's revenues in the Indian formulations market are next only to Cipla's
US generics	597	13%	Valued on a PER of 16x; 10-15% premium to US generic players for 'India' advantage
Generic Lipitor NPV	580	13%	NPV valuation; US\$1.6bn sales and US\$792m profit expected
Central Europe	429	9%	Valued on a PER of 18x given the growth in these markets and its 'branded formulations' nature
Terapia	403	9%	Valued on a PER of 20x; Romania is also in the preferred business region
Russia/CIS	311	7%	Valued on a PER of 20x; Russia/CIS are in our preferred business region
Asia/ Latin America/ Middle East	259	6%	Blended PER of 17x for regions like Asia/ Africa/ Middle East/ Latam
NPV of one-offs	176	4%	NPV of \$15bn of branded sales targeted though Para IV FTF till 2011 ex-generic Lipitor
Western Europe	134	3%	Valued on P/sales of 1; Loss-making geography for the company
Bulk	70	2%	In line with sector bulk business valuations
Total	4,540		

Source: ABN AMRO forecasts

Table 9 : Sun Pharma (Hold, TP Rs1017)*

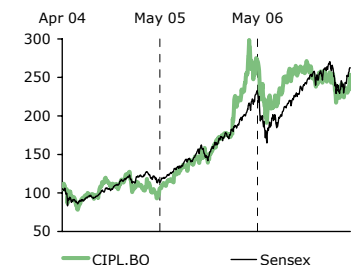
US\$m	Value break down	Contribution	Comments
India formulations	2,913	62%	Valued at 25x; 40% chronic portfolio with high margins; tax rate very low boosting up NPMs
Implied value of proposed R&D demerger	500	11%	Demerger suggests value of US\$288m from earnings upside due to cost savings, implying an NPV of about US\$200m for three molecules. This is reasonable, in our view.
US generics	477	10%	Valued on a PER of 16x; in-line with valuation of Caraco accounting for preference shares
RoW formulations	409	9%	PER of 20x for presence in high-growth regions and high exposure to branded formulations
Bulk	338	7%	In-line with sector bulk business valuations
NPV of one-offs	43	1%	NPV of 6 FTF opportunities. Brand sales targeted are \$3b
Total	4,680		

Source: ABN AMRO forecasts. *The TP includes the value of the R&D demerger and will be updated once the demerged entity is listed

Table 10 : Wockhardt (Buy, TP Rs428) *

US\$m	Value break down	Contribution	Comments
India formulations	720	63%	Valued at 20x; 25% chronic portfolio
Europe generics	296	26%	In-line with US generics; high exposure to the UK, which is a commoditised market
RoW formulations	64	6%	Valued on a blended PER of 18x given the growth in these markets and its exposure to branded formulations
US generics	27	2%	20% discount to major players on account of accounting issues in the US and R&D capitalisation policy
Bulk	27	2%	In-line with sector bulk business valuations
Total	1,134		

Source: ABN AMRO forecasts. *The stock has attained our target price; we are currently reviewing our outlook in light of the recent Negma acquisition.



Stock borrowing: n/a

Volatility (30-day): 29.89%

Volatility (6-month trend): ↑

52-week range: 280.35-178.00

Sensex: 14228.88

BBG AP Pharm & Biotech: 170.62

Source: ABN AMRO, Bloomberg

Results and guidance disappoint

We cut our 2008F earnings by 20% for Cipla on significantly lower-than-expected 4Q07 profit. Management guidance also looks very conservative at 10-12% top-line and bottom-line growth. We downgrade to Hold and reduce our target price to Rs213.

Key forecasts

	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue (Rsm)	22226.8	29443.1	35146.5	42245.3	48867.7
EBITDA (Rsm)	4634.8	6321.9	7652.4▼	7797.8▼	9308.4▼
Reported net profit (Rsm)	4096.1	6076.6	6609.2▼	7080.2▼	8315.0▼
Normalised net profit (Rsm) ¹	4096.1	6076.6	6609.2	7080.2	8315.0
Normalised EPS (Rs)	5.46	8.11	8.51▼	9.12▼	10.7▼
Dividend per share (Rs)	1.40	2.07	2.26▼	2.42▼	2.84▼
Dividend yield (%)	0.64	0.96	1.04	1.11	1.31
Normalised PE (x)	39.7	26.8	25.5▼	23.8▲	20.3▲
EV/EBITDA (x)	36.8	27.3	21.8	21.6	17.7
Price/book value (x)	10.5	8.21	5.24	4.54	3.92
ROIC (%)	16.8	19.2	16.7	13.5	13.3

1. Post-goodwill amortisation and pre-exceptional items

Accounting Standard: Local GAAP

Source: Company data, ABN AMRO forecasts

year to Mar, fully diluted

4Q07 performance disappoints

Cipla's 4Q07 (March year-end) net profit fell a sharp 26% yoy, vs our 5% decline forecast. The disappointing performance was due mainly to sales being skewed towards more low-margin anti-retrovirals (ARVs) and due to increasing competitive pressure in the US market. Sales grew only 6% yoy to Rs9.2bn. The company's 4Q07 EBITDA margin declined 460bp to 15%, the lowest in the past 16 quarters. The company ended the year with a net profit of Rs6.6bn and reported EPS of Rs8.8.

Guidance looks very conservative

Management says Cipla should be able to deliver 10-12% yoy top-line and bottom-line growth. It also expects EBITDA margin to be sustained at 15% levels. The company appears to be facing pressure in the US market. However, the contribution of the US to its overall profit is low at 10-15%, so it should have little impact on Cipla's profitability. We think the already-high share of ARVs will increase further, which may keep margins under pressure as evidenced by the 2Q07 results. Despite all this, we think the key profitability element for Cipla is its Indian business, which accounts for nearly 50% of its total sales, and should contribute positively in the upcoming quarters after a weak seasonality in 4Q. Overall, we think the 15% operating guidance is on the conservative side, but we accept the fact that the days of 20% operating margins are now over, at least in the near term.

Downward revisions to earnings and target price

We reduce our FY08 estimates considering the lower FY07 base and lower growth prospects. We expect Cipla to report net profit of Rs7,080m (7% yoy growth) and EPS of Rs9.1. The stock trades at 23.8x our FY08 estimates. We use a SOTP-based methodology to value the Indian generic companies, assigning higher value to the emerging geographies in Eastern Europe and India. In light of the above, we cut our target price for Cipla is Rs213 (from Rs284) and downgrade our rating to Hold (from Buy).

Priced at close of business 27 April 2007. Use of ▲▼ indicates that the line item has changed by at least 5%.

CIPLA: KEY FINANCIAL DATA

Income statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	22226.8	29443.1	35146.5	42245.3	48867.7
Cost of sales	-17592	-23121	-27494	-34447	-39559
Operating costs	n/a	n/a	n/a	n/a	n/a
EBITDA	4634.8	6321.9	7652.4	7797.8	9308.4
DDA & Impairment (ex gw)	-550.5	-801.8	-1040.8	-1104.2	-1300.0
EBITA	4084.3	5520.1	6611.6	6693.7	8008.4
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	4084.3	5520.1	6611.6	6693.7	8008.4
Net interest	-76.3	-114.2	-69.6	-67.2	-29.7
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	1138.2	1692.7	1467.2	1703.2	1803.7
Reported PTP	5146.1	7098.6	8009.2	8329.7	9782.4
Taxation	-1050.0	-1022.0	-1400.0	-1249.4	-1467.4
Minority interests	n/a	n/a	n/a	n/a	n/a
Exceptionals (post-tax)	0.00	0.00	0.00	0.00	0.00
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	4096.1	6076.6	6609.2	7080.2	8315.0
Normalised Items Excl. GW	0.00	0.00	0.00	0.00	0.00
Normalised net profit	4096.1	6076.6	6609.2	7080.2	8315.0

Source: Company data, ABN AMRO forecasts

year to Mar

Balance sheet

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Cash & market secs (1)	112.0	444.8	6347.3	3187.8	4993.0
Other current assets	17378.5	22478.0	26696.7	32677.2	37698.8
Tangible fixed assets	8448.7	11436.2	14411.2	17307.0	17007.0
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	183.0	224.3	250.0	300.0	325.0
Total assets	26122.3	34583.3	47705.2	53472.1	60023.9
Short term debt (2)	n/a	n/a	n/a	n/a	n/a
Trade & oth current liab	7784.4	9082.0	9976.4	12149.3	14115.8
Long term debt (3)	1912.0	4689.1	4189.1	2689.1	1189.1
Oth non-current liab	889.5	979.5	1381.5	1460.6	1656.5
Total liabilities	10585.8	14750.6	15547.0	16299.0	16961.4
Total equity (incl min)	15536.3	19832.9	32158.2	37173.0	43062.5
Total liab & sh equity	26122.1	34583.5	47705.2	53472.1	60023.9
Net debt (2+3-1)	1800.0	4244.3	-2158.2	-498.7	-3803.9

Source: Company data, ABN AMRO forecasts

year ended Mar

Cash flow statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
EBITDA	4634.8	6321.9	7652.4	7797.8	9308.4
Change in working capital	-2272.0	-4377.8	-3479.6	-3945.1	-3415.3
Net interest (pd) / rec	1061.8	1578.5	1397.6	1636.0	1774.0
Taxes paid	-1050.0	-1022.0	-1400.0	-1249.4	-1467.4
Other oper cash items	-8.40	-183.8	-15.8	0.00	0.00
Cash flow from ops (1)	2366.2	2316.9	4154.6	4239.3	6199.8
Capex (2)	-2458.8	-3800.0	-4000.0	-4000.0	-1000.0
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	1121.1	148.3	-25.7	-50.0	-25.0
Cash flow from invest (3)	-1337.6	-3651.8	-4025.7	-4050.0	-1025.0
Incr / (decr) in equity	0.02	0.02	7644.0	0.00	0.00
Incr / (decr) in debt	-193.8	2777.1	-500.0	-1500.0	-1500.0
Ordinary dividend paid	-1014.8	-1199.1	-1772.6	-1928.0	-2065.4
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	230.0	90.0	402.0	79.2	195.8
Cash flow from fin (5)	-978.7	1668.1	5773.4	-3348.8	-3369.5
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Inc/(decr) cash (1+3+5+6)	49.9	333.2	5902.3	-3159.5	1805.2
Equity FCF (1+2+4)	-92.6	-1483.2	154.6	239.3	5199.8

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Mar

CIPLA: PERFORMANCE AND VALUATION

Standard ratios	Cipla					Lupin Ltd			Wockhardt		
Performance	FY05A	FY06A	FY07F	FY08F	FY09F	FY07F	FY08F	FY09F	FY06F	FY07F	FY08F
Sales growth (%)	18.4	32.8	18.7	20.3	15.8	17.0	28.2	-1.22	21.8	31.9	15.0
EBITDA growth (%)	18.0	36.4	21.0	1.90	19.4	22.8	67.7	-16.6	11.3	28.8	17.9
EBIT growth (%)	15.8	35.2	19.8	1.24	19.6	25.0	77.0	-22.0	8.44	31.3	19.7
Normalised EPS growth (%)	29.5	48.3	4.99	7.13	17.4	27.5	63.4	-4.38	-2.96	21.7	23.8
EBITDA margin (%)	21.2	21.8	22.3	18.9	19.4	13.8	18.1	15.3	21.3	20.8	21.3
EBIT margin (%)	18.7	19.1	19.2	16.2	16.7	11.5	15.9	12.6	18.0	18.0	18.7
Net profit margin (%)	18.8	21.0	19.2	17.1	17.4	11.1	14.2	13.7	14.5	13.4	14.4
Return on avg assets (%)	17.2	20.3	16.2	14.1	14.7	9.04	13.5	11.0	10.6	11.5	12.1
Return on avg equity (%)	29.1	34.4	25.4	20.4	20.7	31.0	37.7	27.4	25.6	23.0	21.7
ROIC (%)	16.8	19.2	16.7	13.5	13.3	12.7	20.4	14.3	20.0	21.9	22.7
ROIC - WACC (%)	6.43	8.75	4.51	1.31	1.10	0.56	8.26	2.16	8.49	10.4	11.2
				<i>year to Mar</i>			<i>year to Mar</i>			<i>year to Dec</i>	
Valuation											
EV/sales (x)	7.81	5.97	4.84	4.07	3.44	3.35	2.55	2.44	3.01	2.20	1.79
EV/EBITDA (x)	36.8	27.3	21.8	21.6	17.7	24.2	14.1	16.0	14.2	10.6	8.38
EV/EBITDA @ tgt price (x)	36.1	26.8	21.3	21.2	17.4	23.7	13.8	15.7	14.1	10.6	8.35
EV/EBIT (x)	41.7	31.3	25.2	25.1	20.6	29.1	16.0	19.5	16.7	12.3	9.56
EV/invested capital (x)	9.35	6.90	5.30	4.41	4.03	5.17	4.53	4.45	4.28	3.58	3.08
Price/book value (x)	10.5	8.21	5.24	4.54	3.92	7.80	5.61	4.46	4.50	3.39	2.60
Equity FCF yield (%)	-0.06	-0.91	0.09	0.14	3.08	1.53	3.47	6.28	0.90	2.32	4.95
Normalised PE (x)	39.7	26.8	25.5	23.8	20.3	28.3	17.3	18.1	20.5	16.8	13.6
Norm PE @tgt price (x)	39.0	26.3	25.0	23.4	19.9	27.8	17.0	17.8	20.4	16.8	13.5
Dividend yield (%)	0.64	0.96	1.04	1.11	1.31	0.66	0.75	0.88	1.17	1.17	1.40
				<i>year to Mar</i>			<i>year to Mar</i>			<i>year to Dec</i>	
Per share data	FY05A	FY06A	FY07F	FY08F	FY09F	Solvency	FY05A	FY06A	FY07F	FY08F	FY09F
Tot adj dil sh, ave (m)	749.7	749.7	776.7	776.7	776.7	Net debt to equity (%)	11.6	21.4	-6.71	-1.34	-8.83
Reported EPS (INR)	5.46	8.11	8.51	9.12	10.7	Net debt to tot ass (%)	6.89	12.3	-4.52	-0.93	-6.34
Normalised EPS (INR)	5.46	8.11	8.51	9.12	10.7	Net debt to EBITDA	0.39	0.67	-0.28	-0.06	-0.41
Dividend per share (INR)	1.40	2.07	2.26	2.42	2.84	Current ratio (x)	2.25	2.52	3.31	2.95	3.02
Equity FCF per share (INR)	-0.12	-1.98	0.20	0.31	6.70	Operating CF int cov (x)	-2.22	-1.12	-2.97	-2.35	-3.32
Book value per sh (INR)	20.7	26.5	41.4	47.9	55.4	Dividend cover (x)	3.90	3.91	3.91	3.91	3.91
				<i>year to Mar</i>						<i>year to Mar</i>	

Priced as follows: CIPL.BO - Rs217.10; LUPN.BO - Rs709.10; WCKH.BO - Rs429.15
Source: Company data, ABN AMRO forecasts

CIPLA: VALUATION METHODOLOGY

We assign a higher valuation to the 'branded formulations' business of Indian generic companies than to the 'commoditised generics' business in the US, the UK and some parts of EU. We assign only 16x PE to Cipla's ARV business, given strong competition and a declining price trend for first-line ARV therapies (see our report, *Distancing from the US*, dated 12 January 2007, for further details on valuation).

Table 3 : SOTP valuation, based on 2008F numbers

Business (Rs m)	Export - formulations	ARVs	Export - Bulk	Domestic
Sales	142	215	161	492
Net profit	11	13	6	138
Net revenue from segments	1,010			
Net profit from segments	169			
	Value (Rsm)	PER	Implied P/sales	
Export formulations at blended PER of 18x	204	18	1.4	
ARVs at PE of 16x	207	16	1.0	
Export bulk at PE of 13x	84	13	0.5	
Total ex-India formulations value	494			
Current market cap	4,623			
Implied india formulations value	4,129			
Implied India formulations PE	30			
TARGET PRICE (Rs)	213			

Source: ABN AMRO estimates

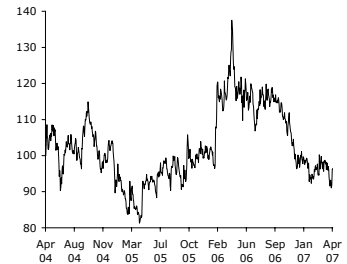
Cipla

Company description

Cipla is one of the premier Indian pharmaceutical companies. It is headed by Dr Hamied, who owns 41% of the company and is the driving force behind its success. Cipla has strong R&D capabilities and supplies bulk drugs and formulations to a number of generic companies in Europe and the US. It is well known for its different drug-delivery capabilities in anti-asthma research.

Hold

Price relative to country



Strategic analysis

Average SWOT company score: 3

Revenue breakdown, FY08F

Strengths

Wide range of products with strength in anti-infective and anti-asthma franchise. Strong research and development. **4**

Weaknesses

Management depth. No initiative as yet to increase its presence in the advanced markets. Succession an issue. **2**

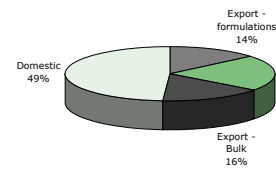
Opportunities

The huge US market for generics, the South African AIDS market and the anti-asthma market in Europe. **4**

Threats

Increasing competition from other players. A lot of smaller companies are emerging with business models similar to Cipla's. Pressure on margins is likely. **3**

Scoring range is 1-5 (high score is good)



Source: ABN AMRO forecasts

Market data

Headquarters
Mumbai Central, Mumbai-400 008. India.

Website
www.cipla.com

Shares in issue
776.7m

Freefloat
59%

Majority shareholders
Dr. Hamied & associates (40%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 2+

Broker recommendations

Supplier power

Fully backward integrated. Strength in R&D helps produce complex products in the anti-asthma range. **3+**

Barriers to entry

Historically, Cipla's research in asthma and anti-infective products has been strong. Its drug-delivery technology in anti-asthma products is difficult to replicate, in our view. **3+**

Customer power

Customers have a wide range of products to choose from, given the stiff competition in the anti-infective segment in the domestic market. **2-**

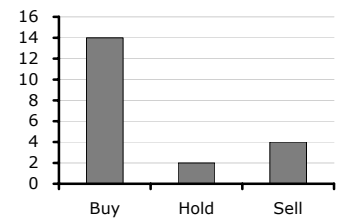
Substitute products

Some therapeutic groups like anti-histamines, antibiotics and pain-management products are substitutable. However, Cipla's different technology in asthma means it has pricing power. **2+**

Rivalry

Intense competition from various players, mainly in the domestic market. Some of these companies compete with Cipla overseas as well. **2-**

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

Dr Reddy's Laboratories

One-offs appear priced in

We await positive surprises from Dr Reddy's R&D pipeline, as we believe the sustainable business will provide moderate upside from current levels. We re-initiate coverage with a Buy recommendation and a sum-of-the-parts-based target of Rs855.

Key forecasts

	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue (Rsm)	19471.5	24266.0	60413.9	51397.1	57477.4
EBITDA (Rsm)	1378.3	2187.5	12982.1	11262.1	13765.9
Reported net profit (Rsm)	210.8	1628.9	7831.9	6762.5	9029.6
Normalised net profit (Rsm) ¹	210.8	1308.9	7831.9	6762.5	9029.6
Normalised EPS (Rs)	1.38	8.55	47.0	40.6	54.2
Dividend per share (Rs)	2.82	2.85	5.17	6.09	10.8
Dividend yield (%)	0.36	0.37	0.67	0.79	1.40
Normalised PE (x)	562.7	90.6	16.5	19.1	14.3
EV/EBITDA (x)	38.1	36.8	6.10	6.47	4.68
Price/book value (x)	5.66	5.33	4.42	3.69	3.06
ROIC (%)	0.53	5.61	13.6	9.82	12.3

1. Post-goodwill amortisation and pre-exceptional items
 Source: Company data, ABN AMRO forecasts
 Accounting Standard: US GAAP

year to Mar, fully diluted

Betapharm performance will be crucial

We expect Betapharm to contribute more than 25% to Dr Reddy's (DRL) FY08 profit. Immediately after its acquisition, Betapharm was subjected to price cuts in Germany, thereby causing a gross margin decline of around 1500bp to 55%. We expect margin to improve to closer to 60% in FY08, but any further setbacks could have a significant impact on DRL's earnings. We note that at the time of acquisition, Betapharm had gross margins that were in line with DRL's branded-formulations business and would have had a higher valuation in our SOTP model. However, with margin now just above the US generics business, we assign around 10% premium valuation to Betapharm relative to the US generics. Stada, the leader in the German market, trades at an 8-10% premium to our valuation of Betapharm, which looks fair to us.

Balaglitazone NPV estimated at US\$204m

DRL has completed phase II trials for Balaglitazone. We await commencement of phase III trials and choose to include the value of this molecule in our target price calculation. To recap, DRL has partnered with Rheoscience for this molecule, giving it rights for the EU and China and retaining rights for US and RoW. We are not very excited as far as glitazones are concerned, as top brands in the space are going generic and there is competition from the DPP4 and GLP1 oral anti-diabetic molecules. While we expect a higher probability of success now that the drug has passed phase II studies, we estimate peak sales of US\$300m in the third year of launch. We have not included the potential of RoW sales in our valuation.

Sum-of-the-parts valuation at Rs855

We have devised a sum-of-the-parts valuation methodology based on the region/business focus. This gives us a valuation of Rs855 for DRL, which includes the R&D NPV of Rs204. The stock trades at 17.8x FY08F PE, excluding Balaglitazone NPV, and we believe should offer comfort on the Betapharm front over the next couple of quarters. We anticipate positive news flow on R&D in the near term and recommend a Buy on the stock.

Buy

Absolute performance

n/a

Short term

Neutral

Market relative to region

Pharmaceuticals & Biotechnology

India

Price

Rs775.25

Target price

Rs855.00

Market capitalisation

Rs59.31bn (US\$1.33bn)

Avg (12mth) daily turnover

Rs126.27m (US\$2.80m)

Reuters

REDY.BO

Bloomberg

DRRD IN

Asset allocation

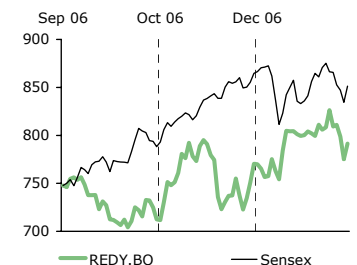
Equities Underweight

Cash Overweight

Bonds Overweight

Price performance (1M) (3M) (12M)

Price (Rs)	775.3	712.3	n/a
Absolute %	-0.0	8.8	n/a
Rel market %	-1.7	-1.4	n/a
Rel sector %	1.6	8.8	n/a



Stock borrowing: Difficult

Volatility (30-day): 25.77%

Volatility (6-month trend): →

52-week range: 958.30-475.70

Sensex: 13630.71

BBG AP Pharm & Biotech: 160.83

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional

Equities Team

www.abnamrobroking.co.in

Priced at close of business 10 January 2007. Use of ▲ ▼ indicates that the line item has changed by at least 5%.

DR REDDY'S LABORATORIES: KEY FINANCIAL DATA

Income statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	19471.5	24266.0	60413.9	51397.1	57477.4
Cost of sales	-9385.8	-12416	-33167	-25335	-27671
Operating costs	-8707.4	-9662.1	-14265	-14800	-16041
EBITDA	1378.3	2187.5	12982.1	11262.1	13765.9
DDA & Impairment (ex gw)	-1256.4	-939.6	-2742.4	-2782.8	-3072.6
EBITA	121.9	1247.9	10239.7	8479.3	10693.4
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	121.9	1247.9	10239.7	8479.3	10693.4
Net interest	271.9	0.00	-920.2	-640.9	-279.5
Associates (pre-tax)	-58.1	-88.2	-40.0	-100.0	-125.0
Forex gain / (loss)	-488.8	-126.3	-100.0	-100.0	-100.0
Exceptionals (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	259.7	534.0	200.0	225.0	250.0
Reported PTP	106.6	1567.3	9379.5	7863.3	10438.8
Taxation	94.3	-258.4	-1547.6	-1100.9	-1409.2
Minority interests	9.94	-0.08	0.00	0.00	0.00
Exceptionals (post-tax)	n/a	320.0	n/a	n/a	n/a
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	210.8	1628.9	7831.9	6762.5	9029.6
Normalised Items Excl. GW	0.00	320.0	0.00	0.00	0.00
Normalised net profit	210.8	1308.9	7831.9	6762.5	9029.6

Source: Company data, ABN AMRO forecasts

year to Mar

Balance sheet

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Cash & market secs (1)	9656.6	9802.4	5329.9	6518.1	9928.9
Other current assets	8696.2	14756.4	36118.4	30776.8	34412.8
Tangible fixed assets	7058.3	9086.3	9407.8	12483.8	12250.7
Intang assets (incl gw)	2588.4	33669.1	32205.3	30846.5	29607.0
Oth non-curr assets	1288.8	1453.8	1470.0	1470.0	1470.0
Total assets	29288.3	68768.1	84531.4	82095.2	87669.4
Short term debt (2)	2796.3	9132.5	9000.0	9000.0	9000.0
Trade & oth current liab	4785.6	9612.4	21377.3	17245.2	19083.2
Long term debt (3)	25.1	20937.1	15937.1	10937.1	5937.1
Oth non-current liab	728.1	6814.3	8975.3	9923.1	11435.5
Total liabilities	8335.2	46496.3	55289.7	47105.4	45455.9
Total equity (incl min)	20952.7	22271.3	29241.7	34989.8	42213.5
Total liab & sh equity	29287.9	68767.7	84531.4	82095.2	87669.4
Net debt (2+3-1)	-6829.2	21192.9	19857.2	13519.0	5108.2

Source: Company data, ABN AMRO forecasts

year ended Mar

Cash flow statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
EBITDA	1378.3	2187.5	12982.1	11262.1	13765.9
Change in working capital	713.4	-1980.9	-9140.3	1378.5	-1776.8
Net interest (pd) / rec	531.6	534.0	-720.2	-415.9	-29.5
Taxes paid	94.3	-258.4	-1547.6	-1100.9	-1409.2
Other oper cash items	-610.1	-67.0	79.0	-219.1	-246.0
Cash flow from ops (1)	2107.5	415.2	1652.9	10904.7	10304.3
Capex (2)	-1906.3	-34048	-1600.0	-4500.0	-1600.0
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	2939.4	-5886.0	5698.6	0.00	0.00
Cash flow from invest (3)	1033.1	-39934	4098.6	-4500.0	-1600.0
Incr / (decr) in equity	0.00	173.5	0.00	0.00	0.00
Incr / (decr) in debt	2323.2	28168.0	-5808.2	-5150.0	-5000.0
Ordinary dividend paid	-431.6	-436.4	-861.5	-1014.4	-1805.9
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-120.4	6038.8	2160.9	947.9	1512.4
Cash flow from fin (5)	1771.2	33943.9	-4508.8	-5216.5	-5293.5
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Incr/(decr) cash (1+3+5+6)	4911.8	-5575.2	1242.7	1188.2	3410.8
Equity FCF (1+2+4)	201.2	-33633	52.9	6404.7	8704.3

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Mar

DR REDDY'S LABORATORIES: PERFORMANCE AND VALUATION

Standard ratios	Dr Reddy's					Ranbaxy Laboratories			Sun Pharmaceutical		
Performance	FY05A	FY06A	FY07F	FY08F	FY09F	FY06F	FY07F	FY08F	FY07F	FY08F	FY09F
Sales growth (%)	-3.04	24.6	149.0	-14.9	11.8	15.8	19.1	7.21	26.9	19.7	14.6
EBITDA growth (%)	-49.8	58.7	493.5	-13.2	22.2	568.0	41.6	11.9	35.5	23.9	13.1
EBIT growth (%)	-93.2	923.3	720.6	-17.2	26.1	n/a	47.8	10.1	36.2	25.6	13.3
Normalised EPS growth (%)	-91.5	520.8	449.9	-13.7	33.5	103.1	49.6	13.1	25.2	17.6	12.0
EBITDA margin (%)	7.08	9.01	21.5	21.9	24.0	14.9	17.7	18.5	33.3	34.5	34.0
EBIT margin (%)	0.63	5.14	16.9	16.5	18.6	11.7	14.5	14.9	29.4	30.8	30.5
Net profit margin (%)	1.08	5.39	13.0	13.2	15.7	8.44	10.6	11.2	35.5	34.9	34.1
Return on avg assets (%)	-0.05	1.95	11.0	8.62	10.9	7.73	9.42	9.53	17.7	18.6	17.7
Return on avg equity (%)	1.00	6.06	30.4	21.1	23.4	19.6	26.1	25.6	40.5	36.8	31.5
ROIC (%)	0.53	5.61	13.6	9.82	12.3	9.86	10.3	10.8	28.7	34.5	35.2
ROIC - WACC (%)	-9.88	-4.79	1.38	-2.36	0.09	0.00	0.00	0.00	16.5	17.2	12.8
				<i>year to Mar</i>			<i>year to Dec</i>			<i>year to Mar</i>	
Valuation											
EV/sales (x)	2.70	3.32	1.31	1.42	1.12	3.36	2.81	2.57	10.0	8.17	6.89
EV/EBITDA (x)	38.1	36.8	6.10	6.47	4.68	22.6	15.9	13.9	30.1	23.7	20.3
EV/EBITDA @ tgt price (x)	42.5	39.6	6.57	7.01	5.12	26.9	18.9	16.6	31.3	24.6	21.1
EV/EBIT (x)	430.4	64.5	7.73	8.59	6.02	28.8	19.4	17.3	34.2	26.5	22.6
EV/invested capital (x)	3.58	1.62	1.39	1.27	1.12	3.13	2.96	2.88	9.39	8.25	7.32
Price/book value (x)	5.66	5.33	4.42	3.69	3.06	6.20	5.35	4.65	10.4	7.72	6.01
Equity FCF yield (%)	0.17	-28.3	0.04	4.96	6.74	2.06	2.67	4.86	3.39	3.20	3.83
Normalised PE (x)	562.7	90.6	16.5	19.1	14.3	32.9	22.0	19.5	28.3	24.0	21.5
Norm PE @tgt price (x)	620.6	100.0	18.2	21.1	15.8	40.5	27.1	23.9	29.3	25.0	22.3
Dividend yield (%)	0.36	0.37	0.67	0.79	1.40	1.56	1.86	2.43	0.74	0.83	0.94
				<i>year to Mar</i>			<i>year to Dec</i>			<i>year to Mar</i>	
Per share data	FY05A	FY06A	FY07F	FY08F	FY09F	Solvency	FY05A	FY06A	FY07F	FY08F	FY09F
Tot adj dil sh, ave (m)	153.0	153.0	166.5	166.5	166.5	Net debt to equity (%)	-32.6	95.2	67.9	38.6	12.1
Reported EPS (INR)	1.38	10.6	47.0	40.6	54.2	Net debt to tot ass (%)	-23.3	30.8	23.5	16.5	5.83
Normalised EPS (INR)	1.38	8.55	47.0	40.6	54.2	Net debt to EBITDA	-4.95	9.69	1.53	1.20	0.37
Dividend per share (INR)	2.82	2.85	5.17	6.09	10.8	Current ratio (x)	2.42	1.31	1.36	1.42	1.58
Equity FCF per share (INR)	1.31	-219.8	0.32	38.5	52.3	Operating CF int cov (x)	-2.79	-0.26	5.44	29.9	397.9
Book value per sh (INR)	136.9	145.5	175.6	210.1	253.5	Dividend cover (x)	0.49	3.00	9.09	6.67	5.00
				<i>year to Mar</i>						<i>year to Mar</i>	

Priced as follows: REDY.BO - Rs775.25; RANB.BO - Rs411.00; SUN.BO - Rs979.5
Source: Company data, ABN AMRO forecasts

DR REDDY'S LABORATORIES: VALUATION METHODOLOGY

Valuation, FY08F

(US\$m)	US generics	Betapharm	West europe	Formulations RoW	API	Cpharma & other	India formulations
Sales	136	242	43	154	254	155	157
Profit after tax	18	41	3	28	13	15	33
Total sales	1,142						
Net profit	150						
	Value	PE (x)	Implied P/sales (x)				
US generics at PE of 16x	283	16.0	2.1				
Betapharm at 10% discount to Stada at PE of 18x	742	18.0	3.1				
W Europe at PE of 16x	41	16.0	1.0				
Formulations RoW (Russia/CIS) at PE of 20x	555	20.0	3.6				
API at PE of 13x	165	13.0	0.7				
Cpharma at 20% premium to API at PE of 15.5x	241	15.5	1.6				
Total ex-India formulations value	2,028						
Add: R&D valuation	204						
Add: Imitrex NPV	22						
Add: NPV of disclosed Para IV exclusivities	93						
Subtotal	2,349						
Current market cap (post dilution)	2,876						
Implied India formulations value	528						
Implied India formulations PE (x)		16					
Fair valuation of Indian formulations		25					
Value upside/downside of Indian formulations	297						
Target price (Rs)	855						

Source: ABN AMRO estimates

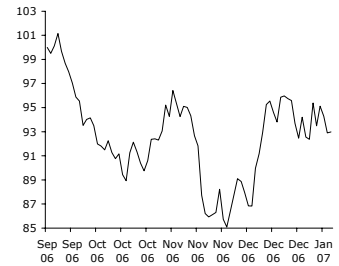
Dr Reddy's Laboratories

Company description

Established in 1984, Dr Reddy's Laboratories (NYSE:RDY) is an emerging global pharmaceutical company with proven basic research capabilities. The company develops, manufactures and markets a wide range of pharmaceutical products in India and overseas. Dr Reddy's produces finished dosage forms, active pharmaceutical ingredients, diagnostic kits, critical care and biotechnology products. Its basic research programme focuses on diabetes, cancer, bacterial infections and pain management.

Buy

Price relative to country



Strategic analysis

Average SWOT company score: 4

Revenue breakdown, FY08F

Strengths

Drug discovery research, emerging strength in biotechnology, USFDA-approved manufacturing facility. **4**

Weaknesses

A lack of marketing presence in the US. DRL is building critical mass in its US and European operations, which will address this weakness, in our view. **2**

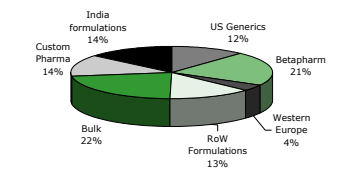
Opportunities

Large US market for generics. Other non-regulated markets such as China, Brazil, CIS, Russia and India. **5**

Threats

Increasing competition in the generics segment in the US. Slowdown in the number of drugs going off-patent in the future. **3**

Scoring range is 1-5 (high score is good)



Source: ABN AMRO forecasts

Market data

Headquarters

7-1-27, Amerpeet, Hyderabad-500 016, India.

Website

www.drreddys.com

Shares in issue

76.5m

Freefloat

74%

Majority shareholders

Dr. Anji Reddy and associates (26%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 4+

Broker recommendations

Supplier power

Superior backward-integrated manufacturing facilities approved by the FDA. Hence, no problem with raw-material supplies. **5+**

Barriers to entry

Strong R&D background focusing on new drug discoveries, legal expertise. Strength in chemical synthesis difficult to replicate. **5+**

Customer power

Key products have pricing power. In the generics market in countries like the US, the lower the price, the higher the market share. **3+**

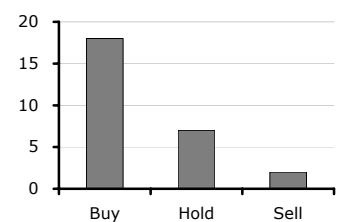
Substitute products

Older products are substitutable. Hence, there is a need to innovate constantly to launch complex products in the market. **2+**

Rivalry

Strong competition from various players that are well entrenched in the advanced markets that Dr Reddy's Labs is targeting. **3+**

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

Glenmark Pharmaceuticals

Continue to wait and watch

Glenmark's 4Q07 result was in line, but guidance for FY08 seems aggressive. We have revised our forecasts to factor in the new guidance. We believe the stock is fairly valued, given milestone uncertainties and the nascent US generics business. Hold, TP Rs656.

Key forecasts

	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue (Rsm)	6120.3	7575.8	12420.0	15522.3	18476.4
EBITDA (Rsm)	1557.3	1372.0	4280.3▲	5201.6▲	6038.5▲
Reported net profit (Rsm)	1065.3	867.6	3102.5▲	3789.8	4815.3▲
Normalised net profit (Rsm) ¹	1065.3	867.6	3102.5	3789.8	4815.3
Normalised EPS (Rs)	8.25	6.72	24.0▲	29.3	37.3▲
Dividend per share (Rs)	0.70	0.70	1.27	1.69	1.69
Dividend yield (%)	0.11	0.11	0.20	0.26	0.26
Normalised PE (x)	77.3	95.0	26.6▼	21.7	17.1▼
EV/EBITDA (x)	50.5	59.7	19.2	15.5	12.8
Price/book value (x)	25.0	21.0	12.0	7.89	5.48
ROIC (%)	37.8	17.0	36.2	34.1	34.7

1. Post-goodwill amortisation and pre-exceptional items
Accounting Standard: Local GAAP
Source: Company data, ABN AMRO forecasts

year to Mar, fully diluted

4Q07 results in line; strong guidance for FY08

Glenmark's 4Q07 results were in line with our forecast, with sales at Rs3.4bn (up 50% yoy) and net profit at Rs633m. Sales performance was mixed: in LatAm countries, quarterly revenue was nearly equal to the number for the previous nine months; domestic sales, which account for nearly 40% of Glenmark's total, grew only 1% yoy. EBITDA margin was stable, at around 30%, and should be monitored closely, in our view. For FY08, the company has projected sales of US\$419m and net profit of US\$125m. Note that this guidance assumes US\$69m in NCE milestone receipts. Nonetheless, guidance on the core business is strong (earnings CAGR of 54% over FY07-09). We have revised our forecast to factor in part of this guidance.

Significant option value; current deals priced in

We ascribe an 'option value' of around US\$1bn to Oglemilast and GRC8200 outlicensing deals. We believe these deals are already priced in; indeed, a further delay of two quarters in the long-awaited US\$30m milestone receipt for Oglemilast from Forest Labs could turn into an overhang for the stock. The company says it expects two more outlicensing deals in the near future. This possibility, in our view, represents potential upside of US\$200m-400m in the stock's market valuation. We have not included these potential upsides in our estimates.

Core business forecast aggressive; fairly valued

Glenmark has projected sales of US\$350m in its core business for FY08. This assumes revenue growth of 80% in the US, which, in our view, is aggressive given: 1) the US generics industry has seen significant price erosion on the back of intense competition; 2) Glenmark has been in the market for just over a year; and 3) its portfolio mainly comprises Para III drugs. While Glenmark's current revenue run-rate in the US appears strong at US\$20m/quarter, its performance needs to be watched over the next couple of quarters to gauge its sustainability. We have raised our SOTP-based target price from Rs603 to Rs656 to factor in the change in our forecasts. However, we believe the stock is fairly valued at 18x core earnings with a valuation of US\$1bn for outlicensing deals. We assign no value for potential deals in the pipeline. Recommend Hold.

Priced at close of business 27 April 2007. Use of ▲▼ indicates that the line item has changed by at least 5%.

Hold

Absolute performance

n/a

Short term (0-60 days)

Neutral

Market relative to region

Pharmaceuticals

India

Price

Rs637.95

Target price

Rs656.00 (from Rs603.00)

Market capitalisation

Rs75.60bn (US\$1.84bn)

Avg (12mth) daily turnover

Rs122.72m (US\$2.76m)

Reuters

GLEN.BO

Bloomberg

GNP IN

Asset allocation

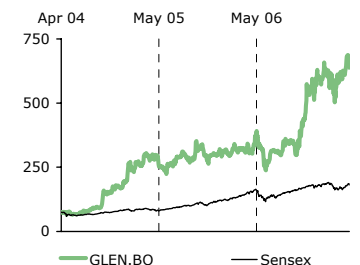
Equities Underweight

Cash Overweight

Bonds Overweight

Price performance (1M) (3M) (12M)

	1M	3M	12M
Price (Rs)	621.2	635.5	322.5
Absolute %	2.7	0.4	97.8
Rel market %	-3.1	3.1	68.3
Rel sector %	1.3	-3.8	77.7



Stock borrowing: Moderate

Volatility (30-day): 38.27%

Volatility (6-month trend): ↓

52-week range: 709.25-228.00

Sensex: 13908.58

BBG AP Pharm & Biotech: 169.61

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional
Equities Team

www.abnamrobroking.co.in

GLENMARK PHARMACEUTICALS: KEY FINANCIAL DATA

Income statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	6120.3	7575.8	12420.0	15522.3	18476.4
Cost of sales	-2714.6	-3817.3	-5086.0	-6534.3	-7894.3
Operating costs	-1848.3	-2386.5	-3053.7	-3786.3	-4543.6
EBITDA	1557.3	1372.0	4280.3	5201.6	6038.5
DDA & Impairment (ex gw)	-164.2	-232.3	-426.3	-496.3	-541.1
EBITA	1393.2	1139.6	3854.0	4705.3	5497.4
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	1393.2	1139.6	3854.0	4705.3	5497.4
Net interest	-172.6	-181.7	-403.9	-382.7	-309.4
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	52.3	162.7	160.7	146.1	171.0
Reported PTP	1272.8	1120.6	3610.9	4468.8	5359.0
Taxation	-201.4	-241.0	-499.7	-670.3	-535.9
Minority interests	0.00	0.00	0.00	0.00	0.00
Exceptionals (post-tax)	n/a	n/a	n/a	n/a	n/a
Other post-tax items	-6.10	-12.0	-8.60	-8.60	-7.74
Reported net profit	1065.3	867.6	3102.5	3789.8	4815.3
Normalised Items Excl. GW	0.00	0.00	0.00	0.00	0.00
Normalised net profit	1065.3	867.6	3102.5	3789.8	4815.3

Source: Company data, ABN AMRO forecasts

year to Mar

Balance sheet

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Cash & market secs (1)	1272.7	1056.0	1045.7	2062.1	4243.0
Other current assets	4148.3	6358.9	9746.3	12253.8	14633.8
Tangible fixed assets	3502.8	5804.7	6264.6	6418.3	6377.1
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	171.6	213.1	225.0	250.0	300.0
Total assets	9095.4	13432.6	17281.5	20984.2	25553.9
Short term debt (2)	n/a	n/a	n/a	n/a	n/a
Trade & oth current liab	1122.7	1727.5	2427.5	3082.6	3701.1
Long term debt (3)	4374.6	7354.0	7482.8	6860.1	6141.2
Oth non-current liab	309.1	420.0	500.0	600.0	675.0
Total liabilities	5806.4	9501.5	10410.3	10542.7	10517.3
Total equity (incl min)	3289.2	3931.1	6871.2	10441.6	15036.6
Total liab & sh equity	9095.5	13432.6	17281.5	20984.2	25553.9
Net debt (2+3-1)	3101.9	6298.1	6437.2	4798.0	1898.2

Source: Company data, ABN AMRO forecasts

year ended Mar

Cash flow statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
EBITDA	1557.3	1372.0	4280.3	5201.6	6038.5
Change in working capital	-1264.8	-1605.1	-2687.4	-1852.5	-1761.4
Net interest (pd) / rec	-172.6	-181.7	-403.9	-382.7	-309.4
Taxes paid	-201.4	-241.0	-499.7	-670.3	-535.9
Other oper cash items	101.2	273.5	240.7	246.1	246.0
Cash flow from ops (1)	19.7	-382.3	930.0	2542.2	3677.8
Capex (2)	-2051.5	-2106.1	-1200.0	-650.0	-500.0
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	116.5	-490.8	298.5	-25.0	-50.0
Cash flow from invest (3)	-1935.0	-2596.9	-901.5	-675.0	-550.0
Incr / (decr) in equity	218.7	0.29	0.00	0.00	0.00
Incr / (decr) in debt	3225.9	2979.4	128.8	-622.8	-718.9
Ordinary dividend paid	-94.0	-94.8	-171.0	-228.1	-228.1
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-243.8	-140.2	-16.1	0.00	0.00
Cash flow from fin (5)	3106.9	2744.7	-58.3	-850.8	-946.9
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Incr/(decr) cash (1+3+5+6)	1191.6	-234.5	-29.8	1016.4	2180.9
Equity FCF (1+2+4)	-2031.8	-2488.4	-270.0	1892.2	3177.8

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Mar

GLENMARK PHARMACEUTICALS: PERFORMANCE AND VALUATION

Standard ratios	Glenmark Pharma					Ranbaxy Laboratories			Dr Reddy's Laboratories		
	FY05A	FY06A	FY07F	FY08F	FY09F	FY06F	FY07F	FY08F	FY07F	FY08F	FY09F
Performance											
Sales growth (%)	60.8	23.8	63.9	25.0	19.0	18.0	16.3	8.44	149.0	-14.9	11.8
EBITDA growth (%)	125.3	-11.9	212.0	21.5	16.1	532.0	36.4	14.5	493.5	-13.2	22.2
EBIT growth (%)	140.1	-18.2	238.2	22.1	16.8	n/a	42.1	13.2	720.6	-17.2	26.1
Normalised EPS growth (%)	134.5	-18.6	257.6	22.2	27.1	118.9	37.0	14.1	449.9	-13.7	33.5
EBITDA margin (%)	25.4	18.1	34.5	33.5	32.7	13.8	16.2	17.1	21.5	21.9	24.0
EBIT margin (%)	22.8	15.0	31.0	30.3	29.8	10.6	13.0	13.6	16.9	16.5	18.6
Net profit margin (%)	17.4	11.5	25.0	24.4	26.1	8.93	10.5	11.1	13.0	13.2	15.7
Return on avg assets (%)	18.3	9.42	22.9	21.9	22.1	8.25	8.97	9.17	11.0	8.62	10.9
Return on avg equity (%)	37.8	24.0	57.4	43.8	37.8	21.0	25.6	25.4	30.4	21.1	23.4
ROIC (%)	37.8	17.0	36.2	34.1	34.7	9.14	9.21	10.1	13.6	9.82	12.3
ROIC - WACC (%)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.38	-2.36	0.09
				<i>year to Mar</i>			<i>year to Dec</i>			<i>year to Mar</i>	
Valuation											
EV/sales (x)	12.9	10.8	6.61	5.18	4.19	3.03	2.58	2.33	1.24	1.33	1.04
EV/EBITDA (x)	50.5	59.7	19.2	15.5	12.8	22.0	16.0	13.6	5.76	6.07	4.36
EV/EBITDA @ tgt price (x)	51.9	61.3	19.7	15.9	13.2	28.4	20.7	17.7	6.57	7.01	5.12
EV/EBIT (x)	56.5	71.9	21.3	17.1	14.1	28.6	19.9	17.2	7.30	8.06	5.61
EV/invested capital (x)	11.7	7.69	5.94	5.08	4.40	2.88	2.75	2.67	1.31	1.19	1.04
Price/book value (x)	25.0	21.0	12.0	7.89	5.48	5.58	4.82	4.20	4.08	3.41	2.83
Equity FCF yield (%)	-2.47	-3.02	-0.33	2.30	3.86	2.70	3.51	5.28	0.04	5.36	7.29
Normalised PE (x)	77.3	95.0	26.6	21.7	17.1	27.7	20.2	17.7	15.2	17.7	13.2
Norm PE @tgt price (x)	79.5	97.6	27.3	22.4	17.6	37.6	27.4	24.0	18.2	21.1	15.8
Dividend yield (%)	0.11	0.11	0.20	0.26	0.26	1.86	2.02	2.69	0.72	0.85	1.51
				<i>year to Mar</i>			<i>year to Dec</i>			<i>year to Mar</i>	
Per share data	FY05A	FY06A	FY07F	FY08F	FY09F	Solvency	FY05A	FY06A	FY07F	FY08F	FY09F
Tot adj dil sh, ave (m)	129.1	129.1	129.1	129.1	129.1	Net debt to equity (%)	94.3	160.2	93.7	46.0	12.6
Reported EPS (INR)	8.25	6.72	24.0	29.3	37.3	Net debt to tot ass (%)	34.1	46.9	37.2	22.9	7.43
Normalised EPS (INR)	8.25	6.72	24.0	29.3	37.3	Net debt to EBITDA	1.99	4.59	1.50	0.92	0.31
Dividend per share (INR)	0.70	0.70	1.27	1.69	1.69	Current ratio (x)	4.83	4.29	4.45	4.64	5.10
Equity FCF per share (INR)	-15.7	-19.3	-2.09	14.7	24.6	Operating CF int cov (x)	2.28	0.22	4.54	9.39	14.6
Book value per sh (INR)	25.5	30.4	53.2	80.9	116.4	Dividend cover (x)	14.8	12.1	24.1	22.0	28.0
				<i>year to Mar</i>						<i>year to Mar</i>	

Priced as follows: GLEN.BO - Rs637.95; RANB.BO - Rs369.95; REDY.BO - Rs711.80
Source: Company data, ABN AMRO forecasts

GLENMARK PHARMACEUTICALS: VALUATION METHODOLOGY

Table 4 : Valuation

Business	US generics	Brazil	Formulations RoW	API	India formulations
Sales	80	42	61	40	112
NPM	20%	15%	18%	10%	20%
PAT	16	6	11	4	22
Total sales	335				
Net profit	60				
NPM	18%				
	Value	PER	Implied P/sales		
US generics at PER of 16x	256	16	3.2		
Brazil at PER of 16x	101	16	2.4		
Formulations RoW (Russia/CIS) at PER of 18x	197	18	3.2		
API at PER of 13x	51	13	1.3		
Total ex-India formulations value	605				
Add: R&D valuation	962				
Subtotal	1567				
Current Mcap (post dilution)	2109				
Implied India formulations value	543				
Implied India formulations PER	24				
Fair valuation of Indian formulations	20				
(Discount)/premium to sector valuation	21%				
Target price (Rs)	656				

Source: ABN AMRO

Glenmark Pharmaceuticals

Company description

Glenmark is among the top 10 pharmaceutical companies in India in the formulations business. The business model of the company revolves around NCE research and sale of API and formulations in the domestic as well as international markets. The company has recently forayed into regulated markets like the US for the sale of generic drugs and on the drug discovery front has been able to outlicense its asthma molecule to Forest Labs and Teijin Pharma.

Hold

Price relative to country



Strategic analysis

Average SWOT company score: 3

FY08F revenue mix

Strengths

4

Ahead of the learning curve with respect to peers on drug-discovery-based R&D. A fully integrated player in the generic drugs space.

Weaknesses

2

Almost 50% of earnings come from milestone payments, given the R&D success. Still in the nascent stage in US and needs to build up the generic drug basket offerings.

Opportunities

4

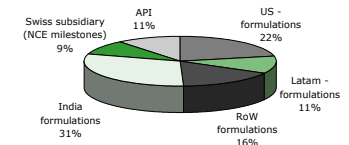
R&D pipeline can materialise into out-licensing deals. Glenmark still needs to venture into the regulated European markets.

Threats

3

Early failure in R&D may put further projects on back burner. Withdrawal by any of the licensing partners could also be a risk.

Scoring range is 1-5 (high score is good)



Source: ABN AMRO forecast

Market data

Headquarters

B/2 Mahalaxmi Chambers, 22 Bhulabhai Desai Road, Mumbai 400 026, India

Website

www.glenmarkpharma.com

Shares in issue

118.5m

Freefloat

45%

Majority shareholders

Promoters (55%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 3+

Broker recommendations

Supplier power

3+

Backward integration and manufacturing facilities approved by the FDA pose no problem with raw-material supplies.

Barriers to entry

4+

R&D programme is fairly advanced, making it easy for the company to be ahead of peers in lead development in certain therapeutic areas. This should raise barriers for any fresh lead in the same.

Customer power

2+

A fairly old player in the domestic market. In the US generic market, the lower the price, the higher the market share generally.

Substitute products

2-

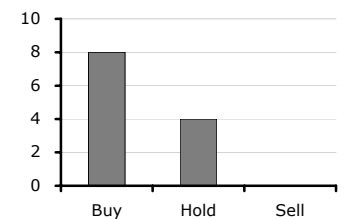
Mainly targeting off-patent generic products for regulated markets. Any generic company with an ANDA approval can create substitution pressure.

Rivalry

2+

Low competition on the R&D front. However, the US generic market continues to be highly competitive.

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

Lupin Ltd

Solid prospects in the price

We see limited potential for a positive surprise to our FY08 estimates, given increased competition on Cefdinir and Suprax. The 4Q07 result also failed to generate confidence of a margin increase. We find the stock fairly valued and downgrade to Hold.

Key forecasts

	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue (Rsm)	12611.4	16954.0	20137.5	25075.9	26615.8
EBITDA (Rsm)	1334.2	2235.6	2922.7▲	4395.4	4037.7▲
Reported net profit (Rsm)	918.5	1729.9	3085.9▲	3470.1	3213.2▼
Normalised net profit (Rsm) ¹	918.5	1729.9	2285.7	3470.1	3213.2
Normalised EPS (Rs)	11.4	19.6	25.9	39.4	36.5▼
Dividend per share (Rs)	3.25	3.26	4.69	5.31	6.25
Dividend yield (%)	0.46	0.46	0.66	0.75	0.88
Normalised PE (x)	62.0	36.1	27.3	18.0	19.4▲
EV/EBITDA (x)	50.1	30.0	22.4	14.5	15.2
Price/book value (x)	11.6	10.0	7.03	5.26	4.30
ROIC (%)	7.29	11.7	13.7	19.3	15.4

1. Post-goodwill amortisation and pre-exceptional items
Accounting Standard: Indian GAAP
Source: Company data, ABN AMRO forecasts

year to Mar, fully diluted

Cefdinir - launched 'at risk'

The Markman hearing for Cefdinir has gone in favour of Lupin and the company has launched the product 'at risk'. Management said the launch was not planned to happen this soon, but was done more as a reaction to Sandoz's launch. Importantly, this means supply constraints could affect the market share in initial weeks. We expect Lupin to garner a market share of at least 20% given limited competition and as it has approvals for all dosage forms. That said, we now believe any upside surprise from an extended period of Cefdinir sales exclusivity for Lupin is unlikely, and so maintain our forecasts on this.

4QFY07 result - operating level disappointment

EBITDA margin fell 300bp qoq in 4QFY07 on the back of higher R&D and staff costs. Gross margin also fell qoq, which was surprising given strong Suprax sales during the US flu season. However, net profit was in line with expectations due to higher other income and lower-than-expected tax rates. FY08 OPM could improve due to the Cefdinir opportunity, but the decline in 4QFY07 margin despite strong domestic growth and Suprax sales, and the guidance of 20% growth in R&D spend for FY08, suggest no improvement in core business performance going forward.

Downgrade to Hold

The stock has passed our sum-of-the-parts target price of Rs695. Its PER multiples of 18x FY08F and 19x FY09F are now in line with the average for local peers under our coverage, and so support our neutral stance. We downgrade the stock to Hold (from Buy) until there is more clarity on FY09 prospects, which at this point suggest a 7.5% earnings decline. Management talked of the possibility of out-licensing one NCE molecule and making an acquisition, but this is not in our estimates.

Hold

(from Buy)

Absolute performance

n/a

Short term (0-60 days)

Neutral

Market relative to region

Pharmaceuticals & Biotechnology

India

Price

Rs709.05

Target price

Rs695.00

Market capitalisation

Rs62.50bn (US\$1.53bn)

Avg (12mth) daily turnover

Rs23.59m (US\$0.53m)

Reuters

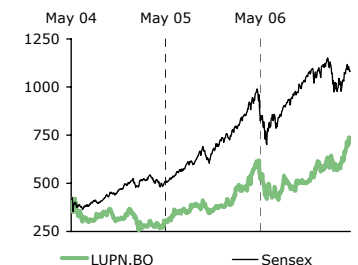
Bloomberg

LUPN.BO

LPC IN

Price performance (1M) (3M) (12M)

Price (Rs)	633.9	607.9	611.9
Absolute %	11.9	16.6	15.9
Rel market %	7.0	23.0	5.2
Rel sector %	12.6	15.1	8.1



Stock borrowing: Difficult

Volatility (30-day): 30.02%

Volatility (6-month trend): ↑

52-week range: 755.00-405.52

Sensex: 13781.51

BBG AP Pharm & Biotech: 167.95

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional
Equities Team

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LUPIN LTD: KEY FINANCIAL DATA

Income statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	12611.4	16954.0	20137.5	25075.9	26615.8
Cost of sales	-9127.3	-11586	-13434	-16337	-17833
Operating costs	-2149.9	-3132.7	-3781.0	-4343.5	-4745.2
EBITDA	1334.2	2235.6	2922.7	4395.4	4037.7
DDA & Impairment (ex gw)	-336.2	-408.8	-466.1	-562.5	-686.2
EBITA	998.0	1826.8	2456.6	3833.0	3351.5
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	998.0	1826.8	2456.6	3833.0	3351.5
Net interest	-253.3	-240.8	-299.1	-230.1	-171.4
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	0.00	0.00	800.2	0.00	0.00
Other pre-tax items	205.0	669.0	774.0	905.0	740.0
Reported PTP	949.7	2255.0	3731.7	4507.9	3920.0
Taxation	-27.4	-521.3	-645.0	-1036.8	-705.6
Minority interests	-3.80	-3.80	-0.80	-1.00	-1.25
Exceptionals (post-tax)	n/a	n/a	n/a	n/a	n/a
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	918.5	1729.9	3085.9	3470.1	3213.2
Normalised Items Excl. GW	0.00	0.00	800.2	0.00	0.00
Normalised net profit	918.5	1729.9	2285.7	3470.1	3213.2

Source: Company data, ABN AMRO forecasts

year to Mar

Balance sheet

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Cash & market secs (1)	270.7	4774.2	4849.7	5635.7	7601.8
Other current assets	6918.5	8900.2	10393.2	12600.3	13271.5
Tangible fixed assets	6327.0	6717.8	7204.7	7342.2	7156.0
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	26.4	28.0	28.0	28.0	28.0
Total assets	13542.6	20420.2	22475.6	25606.2	28057.3
Short term debt (2)	n/a	n/a	n/a	n/a	n/a
Trade & oth current liab	3130.1	3983.6	4691.4	5761.5	6216.5
Long term debt (3)	4572.1	9249.0	7926.1	7000.2	6352.0
Oth non-current liab	946.6	954.8	966.6	967.6	968.9
Total liabilities	8648.8	14187.4	13584.1	13729.2	13537.3
Total equity (incl min)	4893.8	6233.2	8891.5	11877.0	14520.0
Total liab & sh equity	13542.6	20420.6	22475.6	25606.2	28057.3
Net debt (2+3-1)	4301.4	4474.8	3076.4	1364.5	-1249.8

Source: Company data, ABN AMRO forecasts

year ended Mar

Cash flow statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
EBITDA	1334.2	2235.6	2922.7	4395.4	4037.7
Change in working capital	-293.0	-1128.2	-785.3	-1137.0	-216.2
Net interest (pd) / rec	-48.3	428.2	474.9	674.9	568.6
Taxes paid	-27.4	-521.3	-645.0	-1036.8	-705.6
Other oper cash items	-40.3	0.60	810.4	-1.00	-1.25
Cash flow from ops (1)	925.2	1014.9	2777.8	2895.5	3683.2
Capex (2)	-746.2	-1214.7	-1000.0	-700.0	-500.0
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	-526.4	444.4	52.1	0.00	0.00
Cash flow from invest (3)	-1272.6	-770.3	-947.9	-700.0	-500.0
Incr / (decr) in equity	3.80	3.80	0.80	1.00	1.25
Incr / (decr) in debt	624.0	4676.9	-1322.8	-926.0	-648.2
Ordinary dividend paid	-298.2	-297.5	-427.6	-484.6	-570.1
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-13.1	-93.0	0.00	0.00	0.00
Cash flow from fin (5)	316.5	4290.2	-1749.7	-1409.6	-1217.1
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Inc/(decr) cash (1+3+5+6)	-30.9	4534.8	80.2	785.9	1966.1
Equity FCF (1+2+4)	179.0	-199.8	1777.8	2195.5	3183.2

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Mar

LUPIN LTD: PERFORMANCE AND VALUATION

Standard ratios	Lupin					Cipla			Wockhardt		
Performance	FY05A	FY06A	FY07F	FY08F	FY09F	FY07F	FY08F	FY09F	FY06F	FY07F	FY08F
Sales growth (%)	3.78	34.4	18.8	24.5	6.14	18.7	20.3	15.8	21.8	31.9	15.0
EBITDA growth (%)	-39.9	67.6	30.7	50.4	-8.14	21.0	1.90	19.4	11.3	28.8	17.9
EBIT growth (%)	-48.1	83.0	34.5	56.0	-12.6	19.8	1.24	19.6	8.44	31.3	19.7
Normalised EPS growth (%)	-33.3	71.5	32.1	51.8	-7.40	4.99	7.13	17.4	-2.96	21.7	23.8
EBITDA margin (%)	10.6	13.2	14.5	17.5	15.2	22.3	18.9	19.4	21.3	20.8	21.3
EBIT margin (%)	7.91	10.8	12.2	15.3	12.6	19.2	16.2	16.7	18.0	18.0	18.7
Net profit margin (%)	7.28	10.2	11.4	13.8	12.1	19.2	17.1	17.4	14.5	13.4	14.4
Return on avg assets (%)	7.38	8.57	9.22	12.6	10.6	16.2	14.1	14.7	10.6	11.5	12.1
Return on avg equity (%)	20.0	31.1	30.2	33.4	24.3	25.4	20.4	20.7	25.6	23.0	21.7
ROIC (%)	7.29	11.7	13.7	19.3	15.4	16.7	13.5	13.3	20.0	21.9	22.7
ROIC - WACC (%)	-3.11	1.32	1.53	7.10	3.17	4.51	1.31	1.10	8.49	10.4	11.2
				<i>year to Mar</i>			<i>year to Mar</i>			<i>year to Dec</i>	
Valuation											
EV/sales (x)	5.30	3.95	3.26	2.55	2.30	4.63	3.89	3.29	2.87	2.09	1.69
EV/EBITDA (x)	50.1	30.0	22.4	14.5	15.2	20.8	20.6	16.9	13.5	10.1	7.93
EV/EBITDA @ tgt price (x)	49.1	29.4	22.0	14.2	14.9	21.3	21.2	17.4	14.1	10.6	8.35
EV/EBIT (x)	66.9	36.7	26.7	16.7	18.3	24.1	24.0	19.7	15.9	11.7	9.05
EV/invested capital (x)	6.59	5.75	5.08	4.50	4.31	5.08	4.22	3.85	4.08	3.41	2.91
Price/book value (x)	11.6	10.0	7.03	5.26	4.30	5.02	4.34	3.75	4.29	3.23	2.48
Equity FCF yield (%)	0.31	-0.32	2.84	3.51	5.09	0.10	0.15	3.22	0.94	2.44	5.20
Normalised PE (x)	62.0	36.1	27.3	18.0	19.4	24.4	22.8	19.4	19.5	16.0	12.9
Norm PE @tgt price (x)	60.7	35.4	26.8	17.7	19.1	25.0	23.4	19.9	20.4	16.8	13.5
Dividend yield (%)	0.46	0.46	0.66	0.75	0.88	1.09	1.16	1.37	1.22	1.22	1.47
				<i>year to Mar</i>			<i>year to Mar</i>			<i>year to Dec</i>	
Per share data	FY05A	FY06A	FY07F	FY08F	FY09F	Solvency	FY05A	FY06A	FY07F	FY08F	FY09F
Tot adj dil sh, ave (m)	80.3	88.1	88.1	88.1	88.1	Net debt to equity (%)	87.9	71.8	34.6	11.5	-8.61
Reported EPS (INR)	11.4	19.6	35.0	39.4	36.5	Net debt to tot ass (%)	31.8	21.9	13.7	5.33	-4.45
Normalised EPS (INR)	11.4	19.6	25.9	39.4	36.5	Net debt to EBITDA	3.22	2.00	1.05	0.31	-0.31
Dividend per share (INR)	3.25	3.26	4.69	5.31	6.25	Current ratio (x)	2.30	3.43	3.25	3.17	3.36
Equity FCF per share (INR)	2.23	-2.27	20.2	24.9	36.1	Operating CF int cov (x)	20.7	-2.59	-6.21	-4.83	-6.72
Book value per sh (INR)	61.0	70.7	100.9	134.8	164.7	Dividend cover (x)	3.52	6.63	6.10	8.16	6.43
				<i>year to Mar</i>						<i>year to Mar</i>	

Priced as follows: LUPN.BO - Rs709.05; CIPL.BO - Rs207.85; WCKH.BO - Rs408.30
Source: Company data, ABN AMRO forecasts

LUPIN LTD: VALUATION METHODOLOGY

Table 5 : Sum of the parts valuation

Business (US\$ m)	US generics	RoW formulations	Bulk	Domestic
Base sales	86	74	181	215
Base net profit	8	7	7	43
Cefdinir sales	41			
Cefdinir Net profit	18			
Net revenue from segments	597			
Net profit from segments	83			
	Value (Rs m)	PER	Implied P/Sales	
US generics at PER of 16x	357	16.0	2.8	
RoW formulations at PER of 18x	132	18.0	1.8	
API at PER of 13x	89	13.0	0.5	
Total Ex-India formulations value	578			
Add: cefdinir one off profits	3			
Subtotal	581			
Current Market Capitalisation	1,257			
Implied india formulations value	676			
Implied India formulations PER		16.0		
Fair PER		20.0		
Target price (Rs)	695			

Source: ABN AMRO estimates

Lupin Ltd

Company description

Lupin is among the top 10 pharmaceutical companies in India, with a strong R&D capability focused on process chemistry, fermentation, new drug delivery systems and new chemical entities. It has a wide product basket across anti-TB, cephalosporin and cardiovascular therapeutic segments in addition to a recent entry in the growing diabetes and CNS segments. Seven of the company's products figure among the top 300 Indian pharmaceutical brands. Lupin is fully integrated from the intermediate stage to finished dosages, with strong abilities in chemical fermentation technologies. Most of its plants are approved by the USFDA, UK MHRA and WHO.

Hold

Price relative to country



Strategic analysis

Average SWOT company score: 3

Sales breakdown, FY07F

Strengths

Strong process development skills in cephalosporins, fermentation technology, USFDA approved facilities for both API and finished dosages, including injectables. **4**

Weaknesses

Lack of marketing and distribution presence in the US, still dependent on APIs, which are subject to pricing pressure. **1**

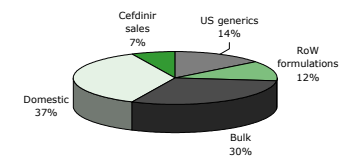
Opportunities

US and European market for generics, especially key cephalosporins and statins, which have high entry barriers. **4**

Threats

Increasing competition in the generics segment in the US and a decline in the number of drugs going off-patent in the future. **3**

Scoring range is 1-5 (high score is good)



Source: ABN AMRO forecasts

Market data

Headquarters
159 CST Road, Kalina, Santacruz E
Mumbai 400 098, India

Website
www.lupinworld.com

Shares in issue
88.1m

Freefloat
49%

Majority shareholders
Promoter Group (51%), Citicorp (13%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 3+

Broker recommendations

Supplier power

Backward integration and enhanced economies of scale, manufacturing facilities approved by the USFDA. Hence, no problem with raw-material supplies. **3+**

Barriers to entry

Strength in fermentation technology difficult to replicate. Creating powerful position in value-added cephalosporins, statins and prils. **4+**

Customer power

Key products have pricing power. In the US and Western European generics market, the lower the price, the higher the market share. **2+**

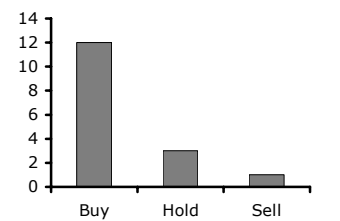
Substitute products

Older products in the anti-TB and anti-infective range are substitutable. Hence, the need to innovate constantly in order to launch complex products in the market. **2-**

Rivalry

Strong competition from a number of players who are well entrenched in the advanced markets that Lupin is targeting. **2-**

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

Ranbaxy Laboratories

Valuations warrant a relook

Ranbaxy's stock has declined 22% over the past six weeks, compared to a 9% drop in the BSE Sensex. There has been no change in the fundamentals to warrant downgrades, and we believe this is a good opportunity to enter the stock. Buy with a TP of Rs505.

Key forecasts

	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue (Rsm)	52450.7	51019.5	60216.0	70019.6	75926.8
EBITDA (Rsm)	7943.7	1314.7	8309.0	11333.1	12979.4
Reported net profit (Rsm)	6985.1	2616.9	5151.0	7365.7	8405.4
Normalised net profit (Rsm) ¹	7357.0	2283.7	5377.0	7365.7	8405.4
Normalised EPS (Rs)	19.8	6.14	13.4	18.4	21.0
Dividend per share (Rs)	8.51	8.52	6.93	7.53	10.0
Dividend yield (%)	2.58	2.58	2.10	2.28	3.03
Normalised PE (x)	16.7	53.7	24.6	17.9	15.7
EV/EBITDA (x)	17.5	113.8	20.0	14.5	12.3
Price/book value (x)	4.88	5.02	4.95	4.28	3.73
ROIC (%)	16.0	-0.24	9.14	9.21	10.1

1. Post-goodwill amortisation and pre-exceptional items
Accounting Standard: Local GAAP
Source: Company data, ABN AMRO forecasts

year to Dec, fully diluted

Pessimism overdone

The prospect of Ranbaxy acquiring Merck KGAA's generics business at an expensive valuation was an overhang on Ranbaxy's stock. Recent press reports suggest it is now out of the race, removing overpayment fears. It seems clear that management is now unlikely to take rash steps just to gain size. We remain uncertain about the outcome of Federal officials' recent search at Ranbaxy's US office, but note the company received tentative approval for zolpidem (gAmbien) afterwards, and its US operations continue as normal. Last year, the stock fell sharply after the US FDA issued a warning regarding the company's Paonta Sahib facility, delaying approval for pravastatin 80mg. The FDA reinspected the plant in February and we expect the facility to be cleared, leading to approval and launch of pravastatin in CY07F. We believe the stock's recent decline is due to unwarranted pessimism on Ranbaxy's US operations, which we estimate will contribute only 18-20% of profits in CY07.

Significant FTF opportunities beckon

Ranbaxy's portfolio includes 19 molecules in which it could win 180-day exclusivity over the next 3-5 years. These molecules' branded-market annual sales add up to US\$25bn. We believe these opportunities should be valued on an NPV basis, as PE valuations on one-off earnings can be volatile. While Lipitor (annual sales: US\$8bn) accounts for a third of the potential FTF pipeline, we believe the remaining US\$16bn is significantly larger than the FTF pipeline of any other Indian generics player. We estimate the portfolio's NPV at US\$176m, based on conservative assumptions of shared exclusivity, the presence of an authorised generic, 50% probability of launch and 35% price erosion in the exclusivity period. The launch of Lipitor in 2010-11 now appears to be a certainty, whose NPV we estimate at US\$550m-600m.

Valuations look exceedingly cheap; maintain target price of Rs505

We value Indian generics companies by a sum of the parts, factoring in regional/business mix. We forecast Ranbaxy will record net profit of US\$165m (Rs18.4/share) in CY07, on which it is trading at 17.8x. Factoring in the NPV of Lipitor and the strong FTF pipeline, valuations look attractive at 13.2x one-year-forward earnings. Our SOTP/NPV-based target price suggests upside of 50% from the current price. Buy.

Priced at close of business 23 March 2007. Use of ▲ ▼ indicates that the line item has changed by at least 5%.

Mafatlal Chambers – C Wing, Ground Floor, N.M. Joshi Marg, Lower Parel (E), Mumbai 400 013, India. Tel : +91 022 6754 8411 Fax : +91 022 6754 8420

Buy

Absolute performance

n/a

Short term (0-60 days)

Neutral

Market relative to region

Pharmaceuticals & Biotechnology

India

Price

Rs330.15

Target price

Rs505.00

Market capitalisation

Rs133.08bn (US\$3.03bn)

Avg (12mth) daily turnover

Rs177.35m (US\$3.92m)

Reuters

RANB.BO

Bloomberg

RBXY IN

Asset allocation

Equities Underweight

Cash Overweight

Bonds Overweight

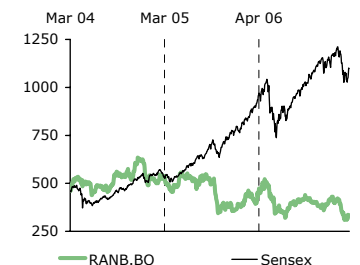
Price performance (1M) (3M) (12M)

Price (Rs) 356.5 386.8 393.1

Absolute % -7.4 -14.6 -16.0

Rel market % -5.0 -13.4 -31.5

Rel sector % -7.9 -16.1 -30.2



Stock borrowing: n/a

Volatility (30-day): 45.36%

Volatility (6-month trend): ↑

52-week range: 530.00-305.50

Sensex: 13285.93

BBG AP Pharm & Biotech: 171.35

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional

Equities Team

www.abnamrobroking.co.in

RANBAXY LABORATORIES: KEY FINANCIAL DATA

Income statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue	52450.7	51019.5	60216.0	70019.6	75926.8
Cost of sales	-28636	-31548	-30420	-35360	-37963
Operating costs	-15871	-18157	-21487	-23327	-24984
EBITDA	7943.7	1314.7	8309.0	11333.1	12979.4
DDA & Impairment (ex gw)	-1214.8	-1444.5	-1911.0	-2238.9	-2686.7
EBITA	6728.9	-129.8	6398.0	9094.2	10292.6
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	6728.9	-129.8	6398.0	9094.2	10292.6
Net interest	-334.9	-671.2	-1080.0	-1179.6	-1288.7
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	-371.9	333.1	-226.0	0.00	0.00
Other pre-tax items	2869.6	2412.7	1473.0	1148.8	1347.5
Reported PTP	8891.7	1944.8	6565.0	9063.4	10351.5
Taxation	-1881.1	697.6	-1361.0	-1631.4	-1863.3
Minority interests	-25.5	-25.5	-53.0	-66.3	-82.8
Exceptionals (post-tax)	n/a	n/a	n/a	n/a	n/a
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	6985.1	2616.9	5151.0	7365.7	8405.4
Normalised Items Excl. GW	-371.9	333.1	-226.0	0.00	0.00
Normalised net profit	7357.0	2283.7	5377.0	7365.7	8405.4

Source: Company data, ABN AMRO forecasts

year to Dec

Balance sheet

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Cash & market secs (1)	1339.4	2430.1	6961.3	12529.7	20483.7
Other current assets	33581.5	30848.7	33131.8	38520.4	41603.7
Tangible fixed assets	18169.7	26186.9	42980.7	42357.2	41347.6
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	1020.4	2920.1	3020.0	3150.0	3250.0
Total assets	54111.0	62385.7	86093.8	96557.3	106685
Short term debt (2)	n/a	n/a	n/a	n/a	n/a
Trade & oth current liab	18389.1	15007.9	15749.6	18310.6	19761.8
Long term debt (3)	8527.3	20042.6	40844.8	44610.1	48736.0
Oth non-current liab	1908.5	2699.3	2599.3	2499.3	2399.3
Total liabilities	28824.8	37749.8	59193.6	65420.0	70897.1
Total equity (incl min)	25286.2	24635.9	26900.2	31137.4	35787.9
Total liab & sh equity	54111.0	62385.7	86093.8	96557.3	106685
Net debt (2+3-1)	7187.9	17612.5	33883.5	32080.4	28252.3

Source: Company data, ABN AMRO forecasts

year ended Dec

Cash flow statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
EBITDA	7943.7	1314.7	8309.0	11333.1	12979.4
Change in working capital	558.0	-648.4	-1541.5	-2827.5	-1632.2
Net interest (pd) / rec	2534.7	1741.5	393.0	-30.8	58.8
Taxes paid	-1881.1	697.6	-1361.0	-1631.4	-1863.3
Other oper cash items	-328.4	302.0	-226.0	n/a	n/a
Cash flow from ops (1)	8827.0	3407.4	5573.5	6843.4	9542.7
Capex (2)	-8469.7	-9508.1	-1559.5	-1615.5	-1677.1
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	-15.7	12.1	-48.3	-30.0	0.00
Cash flow from invest (3)	-8485.4	-9496.1	-1607.8	-1645.5	-1677.1
Incr / (decr) in equity	3.47	3.30	0.00	0.00	0.00
Incr / (decr) in debt	2677.4	11515.3	20802.1	3765.3	4125.9
Ordinary dividend paid	-3603.0	-3614.5	-2939.7	-3194.8	-3837.6
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	339.6	-724.9	-165.7	-200.0	-200.0
Cash flow from fin (5)	-582.5	7179.3	17696.7	370.5	88.3
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Incr/(decr) cash (1+3+5+6)	-241.0	1090.6	21662.4	5568.4	7954.0
Equity FCF (1+2+4)	357.2	-6100.7	4014.0	5227.9	7865.7

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Dec

RANBAXY LABORATORIES: PERFORMANCE AND VALUATION

Standard ratios	Ranbaxy Lab					Dr Reddy's Laboratories			Sun Pharmaceutical		
Performance	FY04A	FY05A	FY06F	FY07F	FY08F	FY07F	FY08F	FY09F	FY07F	FY08F	FY09F
Sales growth (%)	17.6	-2.73	18.0	16.3	8.44	149.0	-14.9	11.8	26.9	19.7	14.6
EBITDA growth (%)	11.1	-83.4	532.0	36.4	14.5	493.5	-13.2	22.2	35.5	23.9	13.1
EBIT growth (%)	13.3	n/a	n/a	42.1	13.2	720.6	-17.2	26.1	36.2	25.6	13.3
Normalised EPS growth (%)	1.58	-69.0	118.9	37.0	14.1	449.9	-13.7	33.5	25.2	17.6	12.0
EBITDA margin (%)	15.1	2.58	13.8	16.2	17.1	21.5	21.9	24.0	33.3	34.5	34.0
EBIT margin (%)	12.8	-0.25	10.6	13.0	13.6	16.9	16.5	18.6	29.4	30.8	30.5
Net profit margin (%)	14.0	4.48	8.93	10.5	11.1	13.0	13.2	15.7	35.5	34.9	34.1
Return on avg assets (%)	15.7	4.70	8.25	8.97	9.17	11.0	8.62	10.9	17.7	18.6	17.7
Return on avg equity (%)	31.5	9.21	21.0	25.6	25.4	30.4	21.1	23.4	40.5	36.8	31.5
ROIC (%)	16.0	-0.24	9.14	9.21	10.1	13.6	9.82	12.3	28.7	34.5	35.2
ROIC - WACC (%)	0.00	0.00	0.00	0.00	0.00	1.38	-2.36	0.09	16.5	17.2	12.8
				<i>year to Dec</i>			<i>year to Mar</i>			<i>year to Mar</i>	
Valuation											
EV/sales (x)	2.65	2.93	2.76	2.34	2.11	1.20	1.29	1.00	10.6	8.63	7.29
EV/EBITDA (x)	17.5	113.8	20.0	14.5	12.3	5.58	5.87	4.19	31.8	25.0	21.4
EV/EBITDA @ tgt price (x)	26.3	167.0	28.4	20.7	17.7	6.57	7.01	5.12	31.3	24.6	21.1
EV/EBIT (x)	20.7	n/m	25.9	18.0	15.6	7.07	7.79	5.39	36.1	28.0	23.9
EV/invested capital (x)	4.05	3.33	2.62	2.50	2.41	1.27	1.15	1.00	9.90	8.71	7.75
Price/book value (x)	4.88	5.02	4.95	4.28	3.73	3.91	3.27	2.71	10.9	8.15	6.33
Equity FCF yield (%)	0.29	-4.97	3.04	3.96	5.96	0.05	5.60	7.61	3.21	3.04	3.63
Normalised PE (x)	16.7	53.7	24.6	17.9	15.7	14.6	16.9	12.7	29.8	25.3	22.6
Norm PE @tgt price (x)	25.5	82.2	37.6	27.4	24.0	18.2	21.1	15.8	29.3	25.0	22.3
Dividend yield (%)	2.58	2.58	2.10	2.28	3.03	0.75	0.89	1.58	0.70	0.79	0.89
				<i>year to Dec</i>			<i>year to Mar</i>			<i>year to Mar</i>	
Per share data	FY04A	FY05A	FY06F	FY07F	FY08F	Solvency	FY04A	FY05A	FY06F	FY07F	FY08F
Tot adj dil sh, ave (m)	371.1	371.8	399.9	399.9	399.9	Net debt to equity (%)	28.4	71.5	126.0	103.0	78.9
Reported EPS (INR)	18.8	7.04	12.9	18.4	21.0	Net debt to tot ass (%)	13.3	28.2	39.4	33.2	26.5
Normalised EPS (INR)	19.8	6.14	13.4	18.4	21.0	Net debt to EBITDA	0.90	13.4	4.08	2.83	2.18
Dividend per share (INR)	8.51	8.52	6.93	7.53	10.0	Current ratio (x)	1.90	2.22	2.55	2.79	3.14
Equity FCF per share (INR)	0.96	-16.4	10.0	13.1	19.7	Operating CF int cov (x)	-3.22	-0.56	-16.6	276.3	-192.9
Book value per sh (INR)	67.7	65.8	66.7	77.1	88.6	Dividend cover (x)	2.33	0.72	2.09	2.63	2.50
				<i>year to Dec</i>						<i>year to Dec</i>	

Priced as follows: RANB.BO - Rs330.15; REDY.BO - Rs686.65; SUN.BO - Rs1033.05
Source: Company data, ABN AMRO forecasts

RANBAXY LABORATORIES: VALUATION METHODOLOGY

Table 4 : Valuation CY07F

(US\$m)	US Generics	Western Europe	Central Europe	Russia/CIS	Rumania	Asia/LatAm/Mid East	API	India	Total
Total sales	446	127	188	97	112	162	121	316	1569
Net profit	38	(13)	24	16	20	11	5	63	165
Net revenue from segments	1569								
Net profit from segments	165								
	Value	PER	Implied P/Sales						
US generics at PER of 16x	605	16	1.4						
W Europe at P/Sales of 1	127	NA	1.0						
CE at PER of 18x	439	18	2.3						
Russia/CIS PER of 20x	311	20	3.2						
Terapia at PER of 20x	403	20	3.6						
Asia/LatAm and M East at PER of 17.x	192	17	1.2						
API at PER of 13x	70	13	0.6						
Total Ex-India formulations value	2147								
Add: Lipitor NPV	580								
Add: NPV of Para IV exclusivities	176								
Sub total	2903								
Current Mcap (assuming FCCB dilution)	2977								
Implied India formulations value	74								
Implied India formulations PER	1								
Fair PE for India formulations	25								
Value upside for India formulations	1507								
TARGET PRICE (Rs)	505								

Source: ABN AMRO forecasts

Ranbaxy Laboratories

Company description

Ranbaxy is the largest domestic pharmaceutical company in India. It is recognised for its research-based approach and accent on exports. It is now rapidly making significant inroads in the advanced markets. The company is ramping up its filings and registrations and is making a push into the US, which is the world's largest generics market. Ranbaxy is also bringing out novel drug-delivery systems and was the first Indian company to licence a product in this field to Bayer AG.

Buy

Price relative to country



Strategic analysis

Average SWOT company score: 4

Strengths

Drug-discovery research. US FDA-approved manufacturing facilities. Strong pipeline of generic drugs in advanced markets. **4**

Weaknesses

The company's high exposure to mature anti-infective segments in the domestic market is affecting growth. **2**

Opportunities

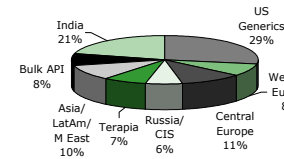
The substantial US market for generics; other non-regulated markets such as Brazil, Russia, CIS, China and India. **5**

Threats

Increased competition in the generics segment in the US. Slowdown in the number of drugs going off patent in future. **3**

Scoring range is 1-5 (high score is good)

Revenue break up



Source: Company

Market data

Headquarters

19, Nehru Place, New Delhi - 110 019, India.

Website

ranbaxy.com

Shares in issue

399.9m

Freefloat

68%

Majority shareholders

Promoters and Associates (32%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 4+

Broker recommendations

Supplier power

Strong backward integration, FDA-approved manufacturing facilities, hence no problems in raw material supplies. **5+**

Barriers to entry

Strong R&D background focusing upon new drug-delivery technology. Strength in chemical synthesis and distribution network difficult to replicate. **4+**

Customer power

Key products have pricing power. But in the generics market of the West, "the lower the price, the better the market share." **3+**

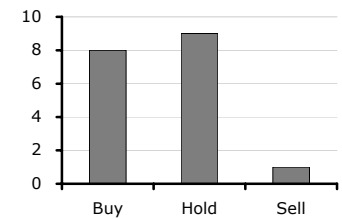
Substitute products

Older products are substitutes. Hence, company needs to innovate constantly to bring complex products to market. **3+**

Rivalry

Strong competition from several players who are well entrenched in the advanced markets Ranbaxy targets. **3+**

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

Sun Pharmaceutical

Hold until demerger provides clarity

Sun's current price suggests a fair value of US\$500m for its innovative R&D business based on our sum-of-the-parts valuation. We await the demerger for clarity on the R&D portfolio, and re-initiate coverage with a Hold recommendation.

Key forecasts

	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue (Rsm)	11432.9	15931.4	20217.3	24207.2	27735.4
EBITDA (Rsm)	4167.5	4974.6	6738.5	8345.8	9438.4
Reported net profit (Rsm)	3961.2	5731.0	7177.4	8440.5	9452.0
Normalised net profit (Rsm) ¹	3961.2	5731.0	7177.4	8440.5	9452.0
Normalised EPS (Rs)	19.1	27.7	34.7	40.8	45.6
Dividend per share (Rs)	3.75	5.95	7.21	8.17	9.17
Dividend yield (%)	0.38	0.61	0.74	0.83	0.94
Normalised PE (x)	51.2	35.4	28.3	24.0	21.5
EV/EBITDA (x)	50.2	41.5	30.1	23.7	20.3
Price/book value (x)	17.9	12.8	10.4	7.72	6.01
ROIC (%)	30.9	23.2	28.7	34.5	35.2

1. Post-goodwill amortisation and pre-exceptional items
Source: Company data, ABN AMRO forecasts
Accounting Standard: Local GAAP

year to Mar, fully diluted

Strong player in India formulations...

India formulations contribute nearly 50% of Sun Pharma's revenue and this is likely to grow by 14-16% over the medium term. Sun has been targeting the niche and chronic segments with its 'lifestyle' drugs portfolio, and has high operating margins in the domestic market. Contributions from RoW formulations are also rising, which augurs well as our valuation method places more value on the high-growth, high-margin branded formulations businesses in India and the developing markets.

... and also doing well in the US

Caraco, Sun's US subsidiary, has been growing at 25%-plus for the past couple of years, a period when the US pricing environment remained tough. This is reflected in the company's performance. Caraco's gross margin was close to 60% over FY04-05, but fell nearly 14ppt by 1H07. It has stabilised at about 50% over the past few quarters. The company has been helped to some extent by the launch of tramadol (gUltracet), which has seen limited competition. We find its operating performance good, given the limited product basket and lack of significant exclusive opportunities. Sun Pharma is involved in a few Para IV litigations that could provide significant upside in the event of favourable outcomes. However, we note the minority payout is likely to rise significantly as Caraco's contribution to consolidated financials grows.

R&D demerger soon... value already built in

Sun Pharma announced the decision to demerge its innovative R&D division nine months ago, and intends to complete the process soon. The company has given no details about its R&D pipeline, other than that it consists of one NCE in the anti-allergy domain and two NDDS products. It is difficult to value the business given the limited information. Assuming the current share price is fair, we arrive at an implied valuation of US\$500m for Sun's R&D business.

We recommend a Hold until the demerger

Our sum-of-the-parts valuation, based on the business/regional analysis, is Rs1,017, implying a value of Rs109 for the R&D entity. We are unable to assign a reasonable value to this entity at this point, but considering our strong operating forecasts over the medium term, we recommend Hold until there is further clarity on the demerger.

Priced at close of business 10 January 2007. Use of ▲ ▼ indicates that the line item has changed by at least 5%.

Mafatal Chambers – C Wing, Ground Floor, N.M. Joshi Marg, Lower Parel (E), Mumbai 400 013, India. Tel : +91 022 6754 8411 Fax : +91 022 6754 8420

Hold

Absolute performance

n/a

Short term

Neutral

Market relative to region

Pharmaceuticals & Biotechnology

India

Price

Rs979.50

Target price

Rs1017.00

Market capitalisation

Rs202.87bn (US\$4.55bn)

Avg (12mth) daily turnover

Rs49.00m (US\$1.08m)

Reuters

SUN.BO

Bloomberg

SUNP IN

Asset allocation

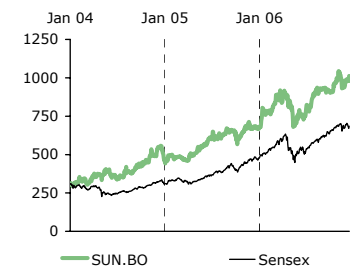
Equities Underweight

Cash Overweight

Bonds Overweight

Price performance (1M) (3M) (12M)

	1M	3M	12M
Price (Rs)	994.5	917.7	680.9
Absolute %	-1.5	6.7	43.9
Rel market %	-3.2	-3.3	-0.3
Rel sector %	0.1	6.7	26.7



Stock borrowing: Difficult

Volatility (30-day): 30%

Volatility (6-month trend): ↓

52-week range: 1065.00-639.95

Sensex: 13630.71

BBG AP Pharm & Biotech: 160.83

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional
Equities Team

www.abnamrobroking.co.in

SUN PHARMACEUTICAL: KEY FINANCIAL DATA

Income statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	11432.9	15931.4	20217.3	24207.2	27735.4
Cost of sales	-3233.5	-4935.1	-6001.4	-7171.7	-8322.9
Operating costs	-4031.9	-6021.7	-7477.5	-8689.8	-9974.1
EBITDA	4167.5	4974.6	6738.5	8345.8	9438.4
DDA & Impairment (ex gw)	-406.0	-614.5	-800.4	-886.1	-986.1
EBITA	3761.5	4360.1	5938.1	7459.7	8452.3
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	3761.5	4360.1	5938.1	7459.7	8452.3
Net interest	117.9	869.3	0.00	0.00	0.00
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	329.6	738.9	1475.5	1694.5	1941.5
Reported PTP	4209.0	5968.3	7413.6	9154.2	10393.7
Taxation	-204.8	-239.3	70.3	-45.8	-103.9
Minority interests	-42.2	2.80	-305.7	-667.1	-837.0
Exceptionals (post-tax)	n/a	n/a	n/a	n/a	n/a
Other post-tax items	-0.80	-0.84	-0.84	-0.84	-0.84
Reported net profit	3961.2	5731.0	7177.4	8440.5	9452.0
Normalised Items Excl. GW	0.00	0.00	0.00	0.00	0.00
Normalised net profit	3961.2	5731.0	7177.4	8440.5	9452.0

Source: Company data, ABN AMRO forecasts

year to Mar

Balance sheet

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
Cash & market secs (1)	11808.9	15322.8	18581.0	23856.2	30380.5
Other current assets	7137.4	11197.6	12678.5	15167.1	17479.3
Tangible fixed assets	5719.2	8562.8	8690.0	9303.9	9817.8
Intang assets (incl gw)	1537.6	506.9	506.9	506.9	506.9
Oth non-curr assets	6978.2	3955.6	4349.9	4509.5	4650.6
Total assets	33181.3	39545.7	44806.3	53343.6	62835.1
Short term debt (2)	n/a	n/a	n/a	n/a	n/a
Trade & oth current liab	2586.5	3514.5	4603.2	5506.8	6345.7
Long term debt (3)	18013.6	18389.0	18389.0	18389.0	18389.0
Oth non-current liab	1112.7	1409.0	1619.5	1872.2	2175.4
Total liabilities	21712.8	23312.5	24611.7	25768.0	26910.1
Total equity (incl min)	11468.8	16233.2	20194.5	27575.6	35925.0
Total liab & sh equity	33181.6	39545.7	44806.3	53343.6	62835.1
Net debt (2+3-1)	6421.4	3422.5	164.3	-5110.9	-11635

Source: Company data, ABN AMRO forecasts

year ended Mar

Cash flow statement

Rsm	FY05A	FY06A	FY07F	FY08F	FY09F
EBITDA	4167.5	4974.6	6738.5	8345.8	9438.4
Change in working capital	-688.9	-3132.2	-392.2	-1585.0	-1473.3
Net interest (pd) / rec	117.9	869.3	0.00	0.00	0.00
Taxes paid	-204.8	-239.3	70.3	-45.8	-103.9
Other oper cash items	410.6	1975.8	1402.7	1280.1	1407.7
Cash flow from ops (1)	3802.3	4448.2	7819.4	7995.1	9268.8
Capex (2)	-1574.7	-4535.5	-950.0	-1500.0	-1500.0
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	-4728.5	4053.3	-394.3	-159.6	-141.1
Cash flow from invest (3)	-6303.2	-482.2	-1344.3	-1659.6	-1641.1
Incr / (decr) in equity	401.1	171.6	309.0	667.6	837.0
Incr / (decr) in debt	14099.9	515.0	0.00	0.00	0.00
Ordinary dividend paid	-729.7	-1167.4	-1525.8	-1727.9	-1940.4
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-406.7	28.5	-2000.0	0.00	0.00
Cash flow from fin (5)	13364.6	-452.4	-3216.9	-1060.3	-1103.4
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Inc/(decr) cash (1+3+5+6)	10863.7	3513.6	3258.2	5275.2	6524.3
Equity FCF (1+2+4)	2227.6	-87.3	6869.4	6495.1	7768.8

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Mar

SUN PHARMACEUTICAL: PERFORMANCE AND VALUATION

Standard ratios	Sun Pharma					Ranbaxy Laboratories			Cipla		
Performance	FY05A	FY06A	FY07F	FY08F	FY09F	FY06F	FY07F	FY08F	FY07F	FY08F	FY09F
Sales growth (%)	21.1	39.3	26.9	19.7	14.6	15.8	19.1	7.21	17.9	25.7	19.5
EBITDA growth (%)	5.92	19.4	35.5	23.9	13.1	568.0	41.6	11.9	39.1	33.9	28.8
EBIT growth (%)	3.09	15.9	36.2	25.6	13.3	n/a	47.8	10.1	41.9	34.4	29.5
Normalised EPS growth (%)	14.6	44.7	25.2	17.6	12.0	103.1	49.6	13.1	14.8	33.3	27.6
EBITDA margin (%)	36.5	31.2	33.3	34.5	34.0	14.9	17.7	18.5	25.7	27.4	29.5
EBIT margin (%)	32.9	27.4	29.4	30.8	30.5	11.7	14.5	14.9	22.9	24.5	26.6
Net profit margin (%)	34.6	36.0	35.5	34.9	34.1	8.44	10.6	11.2	21.1	22.4	23.9
Return on avg assets (%)	16.1	13.4	17.7	18.6	17.7	7.73	9.42	9.53	17.7	18.7	20.3
Return on avg equity (%)	40.7	42.1	40.5	36.8	31.5	19.6	26.1	25.6	27.6	26.8	28.1
ROIC (%)	30.9	23.2	28.7	34.5	35.2	9.86	10.3	10.8	19.8	21.5	22.9
ROIC - WACC (%)	20.5	12.8	16.5	17.2	12.8	0.00	0.00	0.00	7.59	9.32	10.7
				<i>year to Mar</i>			<i>year to Dec</i>			<i>year to Mar</i>	
Valuation											
EV/sales (x)	18.3	12.9	10.0	8.17	6.89	3.36	2.81	2.57	5.44	4.32	3.50
EV/EBITDA (x)	50.2	41.5	30.1	23.7	20.3	22.6	15.9	13.9	21.2	15.8	11.9
EV/EBITDA @ tgt price (x)	52.1	43.0	31.3	24.6	21.1	26.9	18.9	16.6	24.8	18.5	13.9
EV/EBIT (x)	55.6	47.3	34.2	26.5	22.6	28.8	19.4	17.3	23.7	17.6	13.2
EV/invested capital (x)	11.1	9.96	9.39	8.25	7.32	3.13	2.96	2.88	6.01	4.92	4.41
Price/book value (x)	17.9	12.8	10.4	7.72	6.01	6.20	5.35	4.65	5.80	4.79	3.93
Equity FCF yield (%)	1.10	-0.04	3.39	3.20	3.83	2.06	2.67	4.86	0.53	1.18	4.53
Normalised PE (x)	51.2	35.4	28.3	24.0	21.5	32.9	22.0	19.5	26.2	19.6	15.4
Norm PE @tgt price (x)	53.2	36.8	29.3	25.0	22.3	40.5	27.1	23.9	30.5	22.9	17.9
Dividend yield (%)	0.38	0.61	0.74	0.83	0.94	1.56	1.86	2.43	1.01	1.35	1.72
				<i>year to Mar</i>			<i>year to Dec</i>			<i>year to Mar</i>	
Per share data	FY05A	FY06A	FY07F	FY08F	FY09F	Solvency	FY05A	FY06A	FY07F	FY08F	FY09F
Tot adj dil sh, ave (m)	207.1	207.1	207.1	207.1	207.1	Net debt to equity (%)	56.0	21.1	0.81	-18.5	-32.4
Reported EPS (INR)	19.1	27.7	34.7	40.8	45.6	Net debt to tot ass (%)	19.4	8.65	0.37	-9.58	-18.5
Normalised EPS (INR)	19.1	27.7	34.7	40.8	45.6	Net debt to EBITDA	1.54	0.69	0.02	-0.61	-1.23
Dividend per share (INR)	3.75	5.95	7.21	8.17	9.17	Current ratio (x)	7.33	7.55	6.79	7.09	7.54
Equity FCF per share (INR)	10.8	-0.42	33.2	31.4	37.5	Operating CF int cov (x)	-33.0	-4.39	0.00	0.00	0.00
Book value per sh (INR)	54.6	76.8	94.4	126.8	163.1	Dividend cover (x)	5.69	5.60	5.36	5.57	5.56
				<i>year to Mar</i>						<i>year to Mar</i>	

Priced as follows: SUN.BO - Rs979.50; RANB.BO - Rs411; CIPL.BO - Rs243.3
Source: Company data, ABN AMRO forecasts

SUN PHARMACEUTICAL: VALUATION METHODOLOGY

Valuation, FY08F

(US\$m)	US generics	Export formulations	Bulk	India
Base sales	140	57	104	279
Base net profit	45	20	26	112
Total sales	580			
Net profit	203			
Minority payout adjustment	(15)			
Net profit	188			
	Value	PE (x)	Implied P/sales (x)	
US generics	477	16	3.4	
Formulations RoW (Russia/CIS)	409	20	1.5	
API	338	13	3.3	
Total ex-India formulations value	1,224			
Add: R&D valuation	500			
Add: NPV of para IV exclusivities	43			
Subtotal	1,767			
Current market cap (post dilution)	4,372			
Implied India formulations value	2,606			
Implied India formulations PE (x)		23		
Fair PE of Indian formulations		25		
Value upside/(downside) in India formulations	307			
Target price (Rs)	1,017			

Source: ABN AMRO forecasts

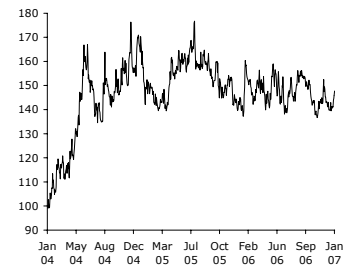
Sun Pharmaceutical

Company description

Sun Pharma is ranked fifth among the Indian pharma companies based on prescriptions, with a 3.01% market share. However, in niche therapy areas such as psychiatry, neurology, cardiology, diabetology, gastroenterology and orthopedics, Sun Pharma ranks among the top-three Indian companies. It holds a 67% equity stake in Detroit-based Caraco Pharma, which is a manufacturer and distributor of generic drugs.

Hold

Price relative to country



Strategic analysis

Average SWOT company score: 3

Revenue breakdown, FY07F

Strengths

Leader in complex and niche therapeutic areas in the domestic formulations business; these include psychiatry, neurology and cardiology. **4**

Weaknesses

Weak formulations exports franchise in non-regulated markets; based predominantly in Asian markets. We also see lack of management depth. **2**

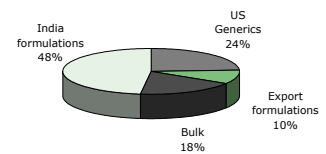
Opportunities

The US generics market is growing with a number of patent expiries. Also, European markets are opening up to generics. **4**

Threats

Increasing competition in the generics markets in the US and Europe. Slowdown in the number of drugs going off-patent in the future. **3**

Scoring range is 1-5 (high score is good)



Source: Company data, ABN AMRO forecasts

Market data

Headquarters

Acme Plaza, Andheri Kurla Road, Andheri (E), Mumbai 400 059, India.

Website

sunpharma.com

Shares in issue

207.1m

Freefloat

29%

Majority shareholders

Indian Promoters (66%), Persons acting in concert (6%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 3+

Broker recommendations

Supplier power

Vertically integrated, not dependent on outside suppliers. Manufacturing facilities are approved by the USFDA, hence no problem in raw-material supplies. **4+**

Barriers to entry

Barriers exists in domestic neurology, psychotropic, cardiology and gastro products. Strength in chemical synthesis difficult to replicate. **3+**

Customer power

Pricing power in some therapeutic groups. However, in the advanced generics markets, the lower the price, the higher the market share. **3+**

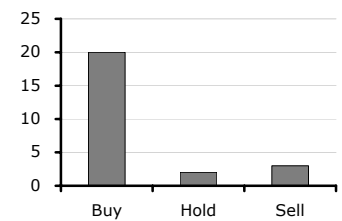
Substitute products

Older products are substitutable. Hence, the company needs to innovate constantly to bring complex products to the market. **3-**

Rivalry

Strong competition from a number of players who are well entrenched in the advanced markets that Sun Pharma is targeting. **2-**

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

Wockhardt

Valuations look attractive

Our sum-of-the-parts valuation for Wockhardt suggests a fair value of Rs428 per share. Trading at 13x 2007F PE, we find the stock interesting because the company derives 35% of revenue from India formulations. We re-initiate coverage at Buy.

Key forecasts

	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue (Rsm)	12516.0	14121.0	17194.6	22686.9	26090.1
EBITDA (Rsm)	2699.3	3286.7	3658.8	4714.1	5560.0
Reported net profit (Rsm)	2141.1	2571.1	2495.0	3036.5	3758.6
Normalised net profit (Rsm) ¹	2135.1	2571.1	2495.0	3036.5	3758.6
Normalised EPS (Rs)	17.9	21.6	21.0	25.5	31.6
Dividend per share (Rs)	4.58	4.59	5.00	5.00	6.00
Dividend yield (%)	1.35	1.35	1.47	1.47	1.77
Normalised PE (x)	18.9	15.7	16.2	13.3	10.7
EV/EBITDA (x)	15.5	12.9	11.2	8.33	6.46
Price/book value (x)	5.99	4.95	3.56	2.68	2.06
ROIC (%)	23.7	24.1	20.0	21.9	22.7

1. Post-goodwill amortisation and pre-exceptional items
Source: Company data, ABN AMRO forecasts
Accounting Standard: Local GAAP

year to Dec, fully diluted

Valuations look cheap

The recent decline in Wockhardt's share price has left it trading at 13x 2007F PE. We acknowledge the company has been having some issues with its US generics business, but it generates 35% of revenue from India and RoW 'branded formulations'. Our sum-of-the-parts methodology assigns a higher valuation to the branded formulations business, making Wockhardt an interesting investment case based purely on valuations.

Accounting issues and US generics overhang

Wockhardt has been riddled with accounting issues in the US generics space, where it did not account properly for the chargeback, inflating revenues in the process. The company identified this last year and has taken steps to set things right. We estimate the US generics business contributes only 7% to Wockhardt's revenue and even less to its profitability, and we therefore believe the chargeback accounting issue is priced in by more than is necessary.

R&D capitalisation does not augur well

Wockhardt has decided to capitalise its ANDA filing costs to match revenue and costs of development. This is against the industry norm, whereby all the leading companies expense off R&D as and when it occurs. In a way, we believe Wockhardt is inflating its earnings in the near term, which may have been affected by the aggressive ANDA filings. We are not proponents of this and, for fair valuation purposes, adjust reported earnings for the capitalised amount.

Target price of Rs428

Based on our sum-of-the-parts valuation methodology focusing on the regional business mix, we assign discounted multiples to Wockhardt's US and UK generics business. We use a higher multiple for the India formulations business in line with the company's India peers, given its decent portfolio of brands, growth in line with the industry and the recent acquisition of Dumex's portfolio. We arrive at a target price of Rs428, which offers 26% potential upside. We see little downside from current levels as the company has weathered negative news flow over the past year and we now expect it to re-rate in the medium term. We re-initiate coverage at Buy.

Priced at close of business 10 January 2007. Use of ▲ ▼ indicates that the line item has changed by at least 5%.

Mafatal Chambers – C Wing, Ground Floor, N.M. Joshi Marg, Lower Parel (E), Mumbai 400 013, India. Tel : +91 022 6754 8411 Fax : +91 022 6754 8420

Buy

Absolute performance

n/a

Short term

Neutral

Market relative to region

Pharmaceuticals & Biotechnology

India

Price

Rs339.25

Target price

Rs428.00

Market capitalisation

Rs40.37bn (US\$905.42m)

Avg (12mth) daily turnover

Rs29.41m (US\$0.65m)

Reuters

WCKH.BO

Bloomberg

WPL IN

Asset allocation

Equities Underweight

Cash Overweight

Bonds Overweight

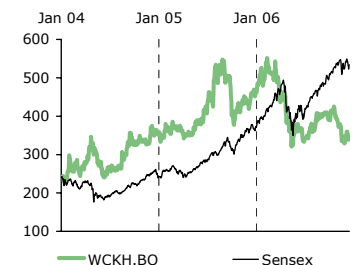
Price performance (1M) (3M) (12M)

Price (Rs) 370.9 409.2 457.5

Absolute % -8.5 -17.1 -25.9

Rel market % -10.1 -24.9 -48.6

Rel sector % -7.0 -17.1 -34.7



Stock borrowing: Impossible

Volatility (30-day): 30.09%

Volatility (6-month trend): ↓

52-week range: 562.00-318.00

Sensex: 13630.71

BBG AP Pharm & Biotech: 160.83

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional
Equities Team

www.abnamrobroking.co.in

WOCKHARDT: KEY FINANCIAL DATA

Income statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue	12516.0	14121.0	17194.6	22686.9	26090.1
Cost of sales	-5218.0	-5771.4	-6697.3	-9415.0	-10958
Operating costs	-4598.8	-5063.0	-6838.5	-8557.7	-9572.3
EBITDA	2699.3	3286.7	3658.8	4714.1	5560.0
DDA & Impairment (ex gw)	-368.0	-426.2	-557.0	-641.0	-686.0
EBITA	2331.2	2860.4	3101.8	4073.1	4873.9
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	2331.2	2860.4	3101.8	4073.1	4873.9
Net interest	-200.3	-261.3	94.5	12.0	30.9
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	374.8	346.0	160.0	125.0	165.0
Reported PTP	2505.7	2945.2	3356.3	4210.1	5069.8
Taxation	-370.5	-374.1	-503.4	-673.6	-811.2
Minority interests	n/a	n/a	n/a	n/a	n/a
Exceptionals (post-tax)	6.00	n/a	n/a	n/a	n/a
Other post-tax items	0.00	0.00	-357.8	-500.0	-500.0
Reported net profit	2141.1	2571.1	2495.0	3036.5	3758.6
Normalised Items Excl. GW	6.00	0.00	0.00	0.00	0.00
Normalised net profit	2135.1	2571.1	2495.0	3036.5	3758.6

Source: Company data, ABN AMRO forecasts

year to Dec

Balance sheet

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Cash & market secs (1)	7354.8	7139.3	7743.6	8978.3	11689.4
Other current assets	5213.0	6465.9	7466.6	9567.2	11867.8
Tangible fixed assets	4983.1	5478.2	6721.2	7080.1	6894.1
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	1637.3	2405.7	2505.0	2755.0	3005.0
Total assets	19188.2	21489.1	24436.3	28380.6	33456.3
Short term debt (2)	n/a	n/a	n/a	n/a	n/a
Trade & oth current liab	2479.0	2561.2	2770.8	3580.5	4527.3
Long term debt (3)	8914.3	9065.1	8515.1	7865.1	7215.1
Oth non-current liab	1629.2	1701.8	1815.3	1884.4	2089.8
Total liabilities	13022.5	13328.1	13101.2	13330.0	13832.3
Total equity (incl min)	6165.7	8161.0	11335.1	15050.6	19624.0
Total liab & sh equity	19188.2	21489.1	24436.3	28380.6	33456.3
Net debt (2+3-1)	1559.4	1925.8	771.5	-1113.2	-4474.3

Source: Company data, ABN AMRO forecasts

year ended Dec

Cash flow statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
EBITDA	2699.3	3286.7	3658.8	4714.1	5560.0
Change in working capital	-221.9	-1115.5	-696.1	-1240.9	-1168.0
Net interest (pd) / rec	174.4	84.8	254.5	137.0	195.9
Taxes paid	-370.5	-374.1	-503.4	-673.6	-811.2
Other oper cash items	0.00	0.00	-357.8	-500.0	-500.0
Cash flow from ops (1)	2281.3	1881.9	2356.0	2436.6	3276.6
Capex (2)	-1621.5	-1689.5	-1897.4	-1250.0	-750.0
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	-2.58	-0.25	-1.86	0.00	0.00
Cash flow from invest (3)	-1624.0	-1689.7	-1899.3	-1250.0	-750.0
Incr / (decr) in equity	182.0	1.52	0.00	0.00	0.00
Incr / (decr) in debt	5612.6	150.9	-550.0	-650.0	-650.0
Ordinary dividend paid	-617.1	-623.9	679.0	679.0	814.8
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-10.4	63.8	18.5	19.1	19.7
Cash flow from fin (5)	5167.2	-407.7	147.6	48.1	184.5
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Inc/(decr) cash (1+3+5+6)	5824.4	-215.5	604.3	1234.7	2711.1
Equity FCF (1+2+4)	659.8	192.4	458.6	1186.6	2526.6

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Dec

WOCKHARDT: PERFORMANCE AND VALUATION

Standard ratios	Wockhardt					Cipla			Lupin Ltd		
Performance	FY04A	FY05A	FY06F	FY07F	FY08F	FY07F	FY08F	FY09F	FY07F	FY08F	FY09F
Sales growth (%)	32.9	12.8	21.8	31.9	15.0	17.9	25.7	19.5	17.0	28.2	-1.22
EBITDA growth (%)	50.4	21.8	11.3	28.8	17.9	39.1	33.9	28.8	22.8	67.7	-16.6
EBIT growth (%)	52.7	22.7	8.44	31.3	19.7	41.9	34.4	29.5	25.0	77.0	-22.0
Normalised EPS growth (%)	37.0	20.4	-2.96	21.7	23.8	14.8	33.3	27.6	27.5	63.4	-4.38
EBITDA margin (%)	21.6	23.3	21.3	20.8	21.3	25.7	27.4	29.5	13.8	18.1	15.3
EBIT margin (%)	18.6	20.3	18.0	18.0	18.7	22.9	24.5	26.6	11.5	15.9	12.6
Net profit margin (%)	17.1	18.2	14.5	13.4	14.4	21.1	22.4	23.9	11.1	14.2	13.7
Return on avg assets (%)	14.9	13.5	10.6	11.5	12.1	17.7	18.7	20.3	9.04	13.5	11.0
Return on avg equity (%)	39.6	35.9	25.6	23.0	21.7	27.6	26.8	28.1	31.0	37.7	27.4
ROIC (%)	23.7	24.1	20.0	21.9	22.7	19.8	21.5	22.9	12.7	20.4	14.3
ROIC - WACC (%)	13.6	14.0	8.49	10.4	11.2	7.59	9.32	10.7	0.56	8.26	2.16
				<i>year to Dec</i>			<i>year to Mar</i>			<i>year to Mar</i>	
Valuation											
EV/sales (x)	3.35	3.00	2.39	1.73	1.38	5.44	4.32	3.50	2.69	2.03	1.92
EV/EBITDA (x)	15.5	12.9	11.2	8.33	6.46	21.2	15.8	11.9	19.4	11.2	12.6
EV/EBITDA @ tgt price (x)	19.4	16.1	14.1	10.6	8.35	24.8	18.5	13.9	23.7	13.8	15.7
EV/EBIT (x)	18.0	14.8	13.3	9.64	7.36	23.7	17.6	13.2	23.3	12.8	15.3
EV/invested capital (x)	5.43	4.19	3.40	2.82	2.37	6.01	4.92	4.41	4.15	3.61	3.50
Price/book value (x)	5.99	4.95	3.56	2.68	2.06	5.80	4.79	3.93	6.17	4.44	3.53
Equity FCF yield (%)	1.63	0.48	1.14	2.94	6.26	0.53	1.18	4.53	1.94	4.38	7.94
Normalised PE (x)	18.9	15.7	16.2	13.3	10.7	26.2	19.6	15.4	22.4	13.7	14.3
Norm PE @tgt price (x)	23.9	19.8	20.4	16.8	13.5	30.5	22.9	17.9	27.8	17.0	17.8
Dividend yield (%)	1.35	1.35	1.47	1.47	1.77	1.01	1.35	1.72	0.84	0.95	1.11
				<i>year to Dec</i>			<i>year to Mar</i>			<i>year to Mar</i>	
Per share data	FY04A	FY05A	FY06F	FY07F	FY08F	Solvency	FY04A	FY05A	FY06F	FY07F	FY08F
Tot adj dil sh, ave (m)	119.0	119.0	119.0	119.0	119.0	Net debt to equity (%)	25.3	23.6	6.81	-7.40	-22.8
Reported EPS (INR)	18.0	21.6	21.0	25.5	31.6	Net debt to tot ass (%)	8.13	8.96	3.16	-3.92	-13.4
Normalised EPS (INR)	17.9	21.6	21.0	25.5	31.6	Net debt to EBITDA	0.58	0.59	0.21	-0.24	-0.80
Dividend per share (INR)	4.58	4.59	5.00	5.00	6.00	Current ratio (x)	5.07	5.31	5.49	5.18	5.20
Equity FCF per share (INR)	5.55	1.62	3.85	9.97	21.2	Operating CF int cov (x)	-14.2	-25.6	-10.2	-21.7	-19.9
Book value per sh (INR)	56.6	68.6	95.3	126.5	164.9	Dividend cover (x)	3.91	4.70	4.19	5.10	5.26
				<i>year to Dec</i>						<i>year to Dec</i>	

Priced as follows: WCKH.BO - Rs339.25; CIPL.BO - Rs243.3; LUPN.BO - Rs560.8
Source: Company data, ABN AMRO forecasts

WOCKHARDT: VALUATION METHODOLOGY

Table 6 : Valuation, 2007F

(US\$m)	US generics	Europe generics	RoW formulations	Bulk	Domestic
Sales	35	231	20	38	180
Profit after tax	2	23	4	2	36
Net revenue from segments	504	504			
Net profit from segments	67	67			
	Value	PE (x)	Implied P/sales (x)		
20% discount to US generics	27	13	0.8		
20% discount to Europe generics	296	13	1.3		
RoW formulations	64	18	3.2		
Bulk	27	13	0.7		
Total ex-India formulations value	413				
Current market capitalisation	900				
Implied India formulations value	487				
Implied India formulations PE (x)		14			
Fair PE of India formulations (x)		20			
Value upside/(downside) in India formulations	233				
Target price (Rs)	428				

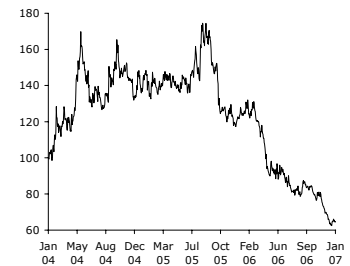
Source: ABN AMRO forecasts

Wockhardt

Company description

Wockhardt is an R&D and technology-based pharmaceutical company with a specific focus on biotechnology. It is the seventh-largest company in India, based on domestic sales. Wockhardt has an active multi-disciplinary R&D programme and employs more than 350 scientists. It has three successful biotech products in the market. The company has entered the US market as well and plans to make 10-15 generic filings in the US annually over the next few years. Recently, the company acquired a portfolio of strong brands such as Protinex and Farex from Dumex to strengthen its neutraceuticals portfolio in India. It also recently acquired Pinewood Labs, a generic company in Ireland.

Buy Price relative to country



Strategic analysis

Average SWOT company score: **3**

Revenue breakdown, FY07F

Strengths

Strong skills being developed in biotechnology, process development, USFDA-approved facilities. Expanding presence in European generics. **4**

Weaknesses

A lack of marketing and distribution presence in the US and dependence on some of its old products in the pain management category in the domestic market, which are subject to government price control. **1**

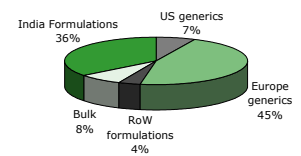
Opportunities

US and European markets for generics present a significant growth area for the company. Direct presence in the UK and Germany should help improve penetration. **4**

Threats

Increasing competition in the generics segment in the US and a slowdown in the number of drugs going off-patent in the future. **3**

Scoring range is 1-5 (high score is good)



Source: Company data, ABN AMRO forecasts

Market data

Headquarters

Wockhardt Towers, Bandra Kurla Complex, Bandra (E), Mumbai-400051, India

Website

wockhardt.com

Shares in issue

119.0m

Freefloat

26%

Majority shareholders

Habib Korakiwala and associates (74%), FIIs (5%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: **3+**

Broker recommendations

Supplier power

Backward integration, early player in biotech drugs, manufacturing facilities approved by the FDA. Hence, no problem with raw-material supplies. **3+**

Barriers to entry

Strength in biotechnology difficult to replicate. Creating a significant franchise in India and getting ready to exploit advanced markets. **4+**

Customer power

Key products have pricing power. In the US and western European generics markets, the lower the price, the higher the market share. **3+**

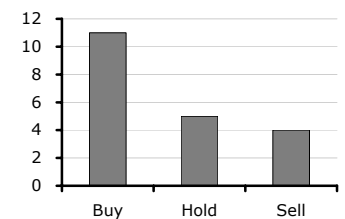
Substitute products

Older products in pain management and anti-infectives are substitutable. Hence the need to improve constantly to launch complex products in the market. **2-**

Rivalry

Strong competition from a number of players who are well entrenched in the advanced markets that Wockhardt is targeting. **2-**

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

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