Rs.430
Target Price: Rs.429
Potential Upside: 0%

Ranbaxy Labs

Relative to sector: **Underperformer**

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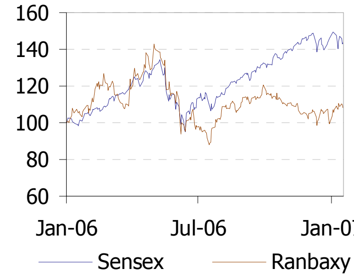
Relative Performance



Source: Bloomberg, ENAM Research

Stock data

No. of shares	: 372mn
Market cap	: Rs.161bn
52 week high/low	: Rs.530/ Rs.317
Avg. daily vol. (6mth)	: 1.4mn shares
Bloomberg code	: RBXY IN
Reuters code	: RANB.BO

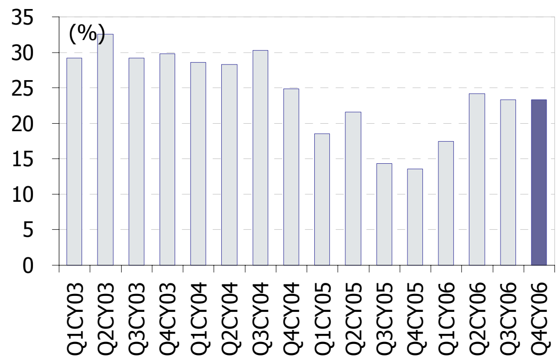
Shareholding (%)		Dec-06	QoQ chg
Promoters	:	34.9	0.0
FIIs	:	18.5	(1.1)
MFs / UTI	:	3.2	0.1
Banks / FIs	:	15.9	1.2
Others	:	27.6	(0.3)

SLOW ROAD TO RECOVERY

Ranbaxy's Q4CY06 results indicate reasonably good topline growth in major markets (Europe, CIS, Africa and North America), and a sharp 8.8% rise in EBIDTA margin to 15%. Consolidated global sales were up 22.3% YoY to Rs.17bn while EBIDTA was up 216% YoY to Rs 2.7bn, due to lower excise (down 43% YoY), and R&D expense (down 3%). The cost cuts led to 357% YoY jump in PAT at Rs 1.83bn.

The performance could have been better but for the continuing delay in resolution of issues raised by the US FDA regarding its Paonta Sahib facility, which have delayed approval and launch of 80mg pravastatin. While the exclusivity on the product remains with Ranbaxy, the value of the opportunity has obviously been depleted by the expiry of Teva's exclusivity on the other strengths as well as the expiry of exclusivity on the competing product, simvastatin.

Pre-R&D EBIDTA as % of sales



Source: Company, ENAM Research

Integration will be key, maintain Underperformer

At CMP (Rs 430), the stock quotes at 25.7x CY07E EPS of Rs 16.7. While its belt-tightening measures can prop up EBIDTA margin, we remain concerned about integration issues for its slew of acquisitions and retain our sector **Underperformer** rating. We have reduced our CY07E estimates by 9%.

Financial summary

Y/E Dec	Sales (Rs.mn)	Adj.PAT (Rs. mn)	Consensus EPS* (Rs.)	EPS# (Rs.)	Change YoY (%)	P/E (x)	RoE (%)	RoCE (%)	EV/EBIDTA (x)	DPS (Rs.)
2005	51,036	2,284	-	5.7	(69)	75.4	9.1	5.8	57.2	8.5
2006	60,217	5,377	-	13.4	135	32.0	21.4	14.1	19.0	10.0
2007E	69,286	6,703	13.8	16.7	25	25.7	25.4	14.4	15.9	12.0
2008E	74,971	7,818	18.5	19.5	17	22.0	27.8	15.3	14.3	14.0

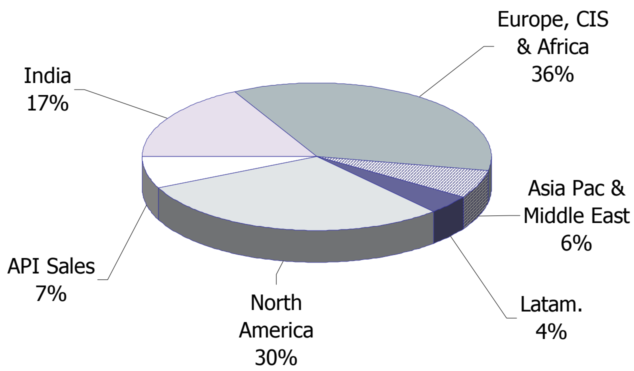
Source: *Consensus broker estimates, Company, ENAM estimates. # On fully diluted basis equity of 400.5mn shares

Results update

	Quarter ended					12 months ended		
(Rs. mn)	Dec-06	Dec-05	% Chg	Sep-06	% Chg	Dec-07E	Dec-06	% Chg
Total Dosage Form Sales	15,907	12,527	27.0	14,282	11.4	64,225	55,490	24.1
API Sales	1,164	1,241	(6.2)	1,196	(2.6)	5,561	5,234	(8.0)
Allied Businesses	-	286	-	-	-	-	-	-
Gross Sales	**17,077**	**14,055**	**21.5**	**15,478**	**10.3**	**69,755**	**60,699**	**17.0**
Excise Duty	102	178	(42.7)	133	(23.3)	469	482	(44.0)
Net Sales	**16,975**	**13,877**	**22.3**	**15,345**	**10.6**	**69,286**	**60,217**	**18.0**
Other Operating Income	794	604	31.5	(184)	(531.5)	2,425	1,124	72.8
Net revenue	**17,769**	**13,642**	**30.2**	**12,981**	**36.9**	**71,711**	**61,341**	**16.1**
EBIDTA	**2,665**	**844**	**215.8**	**2,697**	**(1.2)**	**11,284**	**9,434**	**203.2**
Other income	484	(168)	-	106	356.6	615	349	(43.4)
PBIDT	**3,149**	**676**	**365.8**	**2,803**	**12.3**	**11,899**	**9,783**	**162.5**
Depreciation	531	447	18.8	496	7.1	2,005	1,911	32.3
Interest	247	195	26.7	299	(17.4)	1,363	1,080	60.9
PBT	**2,371**	**34**	**6,873.5**	**2,008**	**18.1**	**8,530**	**6,792**	**321.4**
Tax	512	(377)	-	378	35.4	1,791	1,361	-
Minority Interest	26	10	160.0	11	136.4	36	53	109.9
Adjusted PAT	**1,833**	**401**	**357.1**	**1,619**	**13.2**	**6,703**	**5,377**	**135.4**
Extra ordinary income/ (exp.)	-	285	-	(226)	-	-	(226)	-
Reported PAT	**1,833**	**686**	**167.2**	**1,393**	**31.6**	**6,703**	**5,151**	**101.6**
No. of shares (mn)	400	400	-	400	-	400	400	-
EBIDTA margin (%)	15.0	6.2	-	20.8	-	15.7	15.4	-
PBIDT margin (%)	15.4	4.7	-	17.9	-	14.3	13.8	-
EPS - annualized (Rs.)	**18.3**	**4.0**	**357.1**	**16.2**	**13.2**	**16.7**	**13.4**	**135.4**

Source: ENAM Research, Company data

Sales Breakdown – Q4CY06



Source: Company

US sales will be under pressure

At USD108mn, Q4CY06 revenues from the US market were up 16% YoY and 13% on a QoQ basis. For CY06, Ranbaxy had US revenues of USD380mn (up 15% YoY), largely driven by sales of USD62mn from 80mg simvastatin (Zocor) tablets during the 180-day exclusivity period. Obviously, the expiry of simvastatin exclusivity will hit revenues from this key geography hard, in 2007.

Ranbaxy has filed 197 ANDAs in the US to date, of which 121 have been approved. Of 76 filings pending with the US FDA, it believes it is first-to-file on 20 molecules.

Europe – Acquiring growth

Sales in Europe were down 6% YoY to USD52mn during the quarter. Pricing pressures in the major markets of UK, France and Germany saw cumulative revenues from the three regions declining 14% YoY to USD34mn. While CY06 sales from its operations in France also declined 6% YoY to USD69mn, there was a silver lining – the operations, hitherto unprofitable, reported a small profit at the EBITDA level after manufacturing of many products was transferred to its facilities in India.

Across Europe, during the current year Ranbaxy has also acquired generic businesses in Spain, Italy and Belgium. The performance of these – particularly given the pricing pressures across the region – will be key to medium term profitability for the company.

Modest growth in BRICS markets

Sales in the BRIC markets were up 45% YoY at USD137mn for the quarter and up 31% YoY to USD477mn for CY06. A key driver was the performance of Russia (including Ukraine and Romania), where sales were up 161% YoY to USD53mn for the quarter. However, this includes turnover from the Romanian generics player Terapia (acquired in Q3CY06), where it has doubled the field force and invested in upgrading facilities over the last two quarters.

India sales were up 10% YoY to USD61mn; it remains the largest player in the domestic formulations market with a 5.10% market share (down from 5.27% as at end-Q3CY06). The company is focusing on chronic care therapies such as cardiovascular, diabetes, respiratory and urology (21% of sales) and NDDS products (9% of sales). During the quarter, Ranbaxy inked an in-licensing deal with Debiopharm to market its cardiovascular drug vapreotide acetate. This follows the two deals in Q3CY06 - with Ethypharm (for a micronized fenofibrate + atorvastatin combination tablet) and with Gilead for tenofovir.

Among the other BRIC markets, while South Africa reported flat sales at USD6mn, price cuts saw sales in China fall 2% YoY to USD4mn. Sales in Brazil were up 96% YoY to USD8mn, albeit off a small base.

R&D costs set to rise

R&D costs were flat at Rs.1.2bn in Q4CY06 and down 21% YoY to Rs.3.9bn for CY06. This contributed in a significant measure to arrest the decline in EBIDTA margins seen through CY05. Costs were cut by conducting more BA/ BE studies in India (rather than through CROs abroad) and by forgoing expensive litigation (wherever possible) in favour of out-of-court settlements. However, the increasing number of regulatory filings globally and changes in regulatory requirements in some markets (e.g. Brazil) will result in R&D expenses rising in CY07, back to CY05 levels of ~Rs 5bn.

Ranbaxy has begun Phase IIb rising single dose studies on RBx 11160 for malaria, in India, Thailand and Africa and combination studies for the same molecule with piperaquine in Switzerland.

Other highlights

The trend reversal in the depreciation of the rupee towards end-2006 helped the company report a Rs 460mn gain on forex positions during the quarter. However, while its domestic operations had sufficient tax shields, on a consolidated basis it provided tax at an effective rate of 21% for the year. This effective tax rate is likely to be maintained in CY07.

Ranbaxy guided towards 15% topline growth and EBIDTA margin at CY06 level through CY07.

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